PAPER – 10 CORPORATE ACCOUNTING (50M)

CONTENTS

BLUE PRINT

Syllabus Structure:

The syllabus in this paper comprises the following topics and study weightage:

Module No.	Module Description	Weight
	Section A: Corporate Accounting	**50%**
1	Accounting for Shares and Debentures	10%
2	Preparation of the Statement of Profit and Loss and Balance Sheet (As per Schedule III of Companies Act, 2013)	10%
3	Cash Flow Statement	10%
4	Accounts of Banking, Electricity and Insurance Companies	10%
5	Accounting Standards	10%

1. ACCOUNTING FOR ISSUE AND FORFEITURE OF SHARES

MEANING OF COMPANY:

- As per Section 2(20) of the Companies Act, 2013, "Company" means a company incorporated under the Companies Act, 2013 or under any previous company law (e.g., the Companies Act, 1956).
- A company is described as a voluntary association of persons who have come together for carrying on business and sharing the profits.
- A company is an artificial person created by law, having separate entity, with a perpetual succession and common seal.

CHARACTERISTICS OF COMPANY:

- It is a distinct legal entity existing independent of its members.
- Liability of the members is limited to the extent of the face value of shares held by them.
- It has a perpetual succession.
- It is a voluntary association of persons usually for profit.
- The shares of a company are freely transferable except in case of a Private limited Company
- A company being a legal person is capable of owing, enjoying and disposing of the property in its own name.
- A company, being a separate body can sue and be sued in its own name.
- Though a company is an artificial person, yet it acts through human beings who are called directors of the company. There is a divorce between ownership and the management.

DIFFERENT TYPES OF COMPANIES:

a) Company limited by shares
b) Company limited by guarantee
c) Unlimited company
d) Private company
e) Public Company
f) One Person Company
g) Small company
h) Government company
i) Foreign company
j) Holding company
k) Subsidiary company

Regulatory Framework of Accounting in a Company:

- The Companies Act, 2013: This is the primary source of law governing the operation including accounting in a company. Section 128 to Section 137 of this Act, mainly provides the provisions related to maintenance of accounts and preparation of financial statements. In addition, the Schedule III of this Act provides the format of financial statements.
- The Company Rules: The Companies (Accounts) Rules, 2014, provides important rules regarding accounting. In addition, some other rules such as Companies (Declaration and Payment of Dividend) Rules, 2014, Companies (Corporate Social Responsibility) Rules, 2014 etc. also provides important guidance on accounting of some specific transactions.
- Accounting Standards: These are common sets of principles, standards, and procedures that define the basis of financial accounting policies and practices. As per Section 133 of Companies Act, 2013, in India, currently, two different sets of accounting standards are in force – Accounting Standards notified under Companies (Accounting Standards) Rules, 2021 and Indian Accounting Standards (or Ind ASs) notified under Companies (Indian Accounting Standards) Rules, 2015.

MAINTAINCE OF BOOKS OF ACCOUNTS:

a) As per Section 128 of the Companies Act, 2013, Every company should prepare and keep at its registered office books of account and other relevant books and papers and financial statements for every financial year which give a true and fair view of the state of the affairs of the company.

b) Financial Statements as per Section 2(40) of the Companies Act, 2013, inter-alia include

i) a balance sheet as at the end of the financial year;

ii) a profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;

iii) cash flow statement for the financial year;

iv) a statement of changes in equity, if applicable and

v) any explanatory note annexed to, or forming part of, any document referred to in (i) to (iv) above.

c) As per section 137(1) of the Companies Act, 2013, every Company is required to file with the Registrar, a copy of its financial statements along with all the attachments, within 30 days from the day on which each of the annual general meeting (AGM) is held.

Annual return:

a) In accordance with Section 92 of the Companies Act, 2013, every company should prepare an annual return in the form prescribed by the Companies Act, 2013 containing the particulars as

(i) its registered office, principal business activities, particulars of its holding, subsidiary and associate companies;

(ii) its shares, debentures and other securities and shareholding pattern;

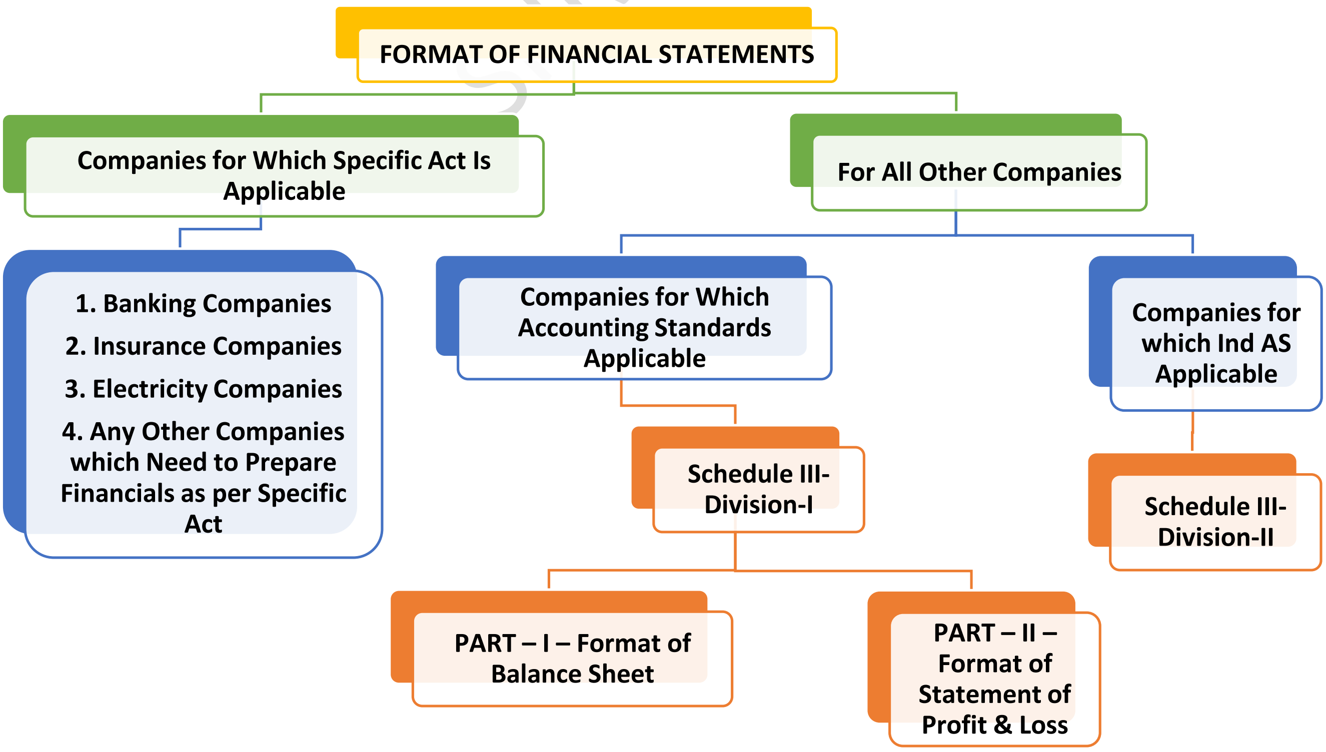
(iii) its members and debenture-holders along with changes therein since the close of the previous financial year;

(iv) its promoters, Directors, key managerial personnel along with changes therein since the close of the previous financial year;

(v) meetings of members or a class thereof, Board and its various committees along with attendance details;

(vi) remuneration of Directors and key managerial personnel etc.

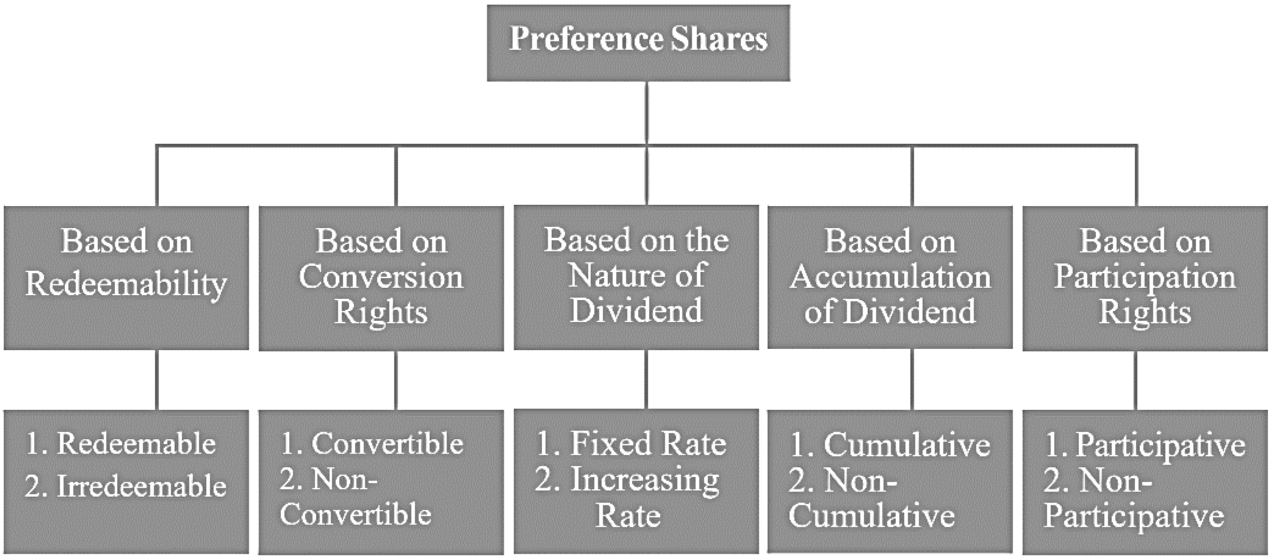
b) The annual return should be filed with the Registrar within 60 days from the day on which each of the annual general meeting (AGM) is held or where no AGM is held in any year, within 60 days from the date on which AGM should have been held along with a statement showing the reasons why AGM was not held.



Concept of Share and Share Capital: The capital raised by a company through issue of shares is known as Share capital. The total capital of a company is split into small equal parts. Each part therefore represents a 'share of the Share capital'.

Types of Shares: On the basis of the rights enjoyed by the shareholders, shares can be divided into two categories as follows

1. Preference Shares: These are shares in case of which the shareholders enjoy certain preferential right to receive dividend and repayment of capital in the event of liquidation of the company. Preference shares can further be classified into various types on different basis as shown below:



2. Equity Share: These are shares that are not preference shares. In other words, here, the shareholders do not enjoy the above two preferential rights.

On the basis of disclosure in the Balance Sheet, Share Capital is categorized as follows:

a) **Authorized Share Capital:** It is the amount of share capital that a company is permitted to issue. It is mentioned in the Capital Clause of the Memorandum of Association of the company. Authorized Share Capital is also known as Nominal Capital.

b) **Issued Share Capital:** It represents the portion of the Authorized Capital that has been offered by a company for subscription.

c) **Subscribed Capital:** It is that part of the issued capital for which applications are received from the public.

d) **Called up Capital:** It is that part of the subscribed capital that has been called up by the company for payment.

e) **Paid up Capital:** The part of the called-up capital which is offered and is actually paid by the members.

f) **Reserved Capital:** It is the portion of the uncalled capital of a company that is called-up for payment only in the event of liquidation of the company.

Various Types of Share Issue:

a) **Public Issue:** Here, the shares are offered directly to the investors for subscription. Accordingly, any person may become the shareholder of the company.

b) **Private Placement:** Here, the shares are issued by the company to a small number of selected investors preferably the financial institutions viz. large banks, mutual funds, insurance companies, pension funds etc.

c) **Rights Issue:** Here, the shares are offered to the existing shareholders of the company at a price below the market price on the basis of their proportionate shareholding.

d) **Bonus Issue:** Here, the shares are offered to the existing shareholders of the company without any consideration.

e) **Offers for sale:** An offer for sale (OFS) is a mechanism that allows promoters to reduce their holdings in listed companies transparently. These shares sold by the promoters are offered for sale directly to the public through a bidding process.

Issue Price of Shares: The price at which the shares are offered for issue by a company may be either equal to, or above, or below the face value. Accordingly, shares can be issued at par, or at a premium, or at a discount. Shares are either issued in lumpsum or in the form of Instalments. When Shares Are Issued in Instalments the following Stages of Collection of Issue Price is possible.

a) **Application Money:** It is the part of the issue price which is to be submitted along with the application for subscription.

b) **Allotment Money:** It is the money payable after shares are initially allotted.

c) **Call Money:** It is collected in subsequent instalment after collecting the allotment money. There may be multiple calls.

Note (Section 53): Except as provided in section 54, a company shall not issue shares at a discount. Any share issued by a company at a discounted price shall be void.

Accounting for Issue of Shares:

Issue of Shares at Par	**Issue of Shares at Premium**
a) Shares issued in lump sum	**a) Shares issued in lump sum**
(i) On receipt of application money Bank A/c ……………………………….Dr. To Share Application A/c (ii) For excess share application money refunded	(i) On receipt of application money (entire amount is received on application) Bank A/c ……………………………….Dr. To Share Application A/c

Share Application A/c …………………… Dr. To Bank A/c (iii) On allotment of shares Share Application A/c ………………………Dr. To Share Capital A/c	(ii) For excess share application money refunded Share Application A/c …………………… Dr. To Bank A/c (iii) On allotment of shares Share Application A/c ………………………Dr. To Share Capital A/c (Face Value x no. of shares allotted) To Securities Premium A/c (Premium x no. of shares allotted)
b) Shares Issued in Instalments	**b) Shares Issued in Instalments** (Unless otherwise stated premium is considered to be a part of allotment money)
(i) On receipt of application money Bank A/c ………………………………Dr. To Share Application A/c (ii) For excess share application money refunded Share Application A/c …………………… Dr. To Bank A/c (iii) For share application money transferred to share capital Share Application A/c ………………………Dr. To Share Capital A/c (iv) For share allotment money due Share Allotment A/c …………………………Dr. To Share Capital A/c (v) For share allotment money received Bank A/c ………………………………Dr. To Share Allotment A/c (vi) For share call money due Share Call A/c …………………………..Dr. To Share Capital A/c (vii)For share call money received Bank A/c ………………………………Dr.	(i) On receipt of application money Bank A/c ………………………………Dr. To Share Application A/c (ii) For excess share application money refunded Share Application A/c …………………… Dr. To Bank A/c (iii) For share application money transferred to share capital Share Application A/c ………………………Dr. To Share Capital A/c (iv) For share allotment money due Share Allotment A/c …………………………Dr. To Share Capital A/c To Securities Premium A/c (vi) For share allotment money received Bank A/c ………………………………Dr. To Share Allotment A/c (vii)For share call money due Share Call A/c …………………………..Dr. To Share Capital A/c (viii)For share call money received

To Share Call A/c	Bank A/c ………………………………Dr. To Share Call A/c

Important points related to Issue of Shares:

a) The power to issue shares at a premium need not be given in the Articles of Association. Premium so received shall be credited to a separate account called Securities Premium Account.

b) Section 52 of the Companies Act, 2013 gives the purposes for which share premium account may be applied by the company. These are:

1. For the issue of fully paid bonus shares to the members of the company;
2. For writing off preliminary expenses of the company;
3. For writing off the expenses of the commission paid or discount allowed on any issue of shares or debentures of the company; and
4. For providing premium payable on the redemption of any redeemable preference shares or debentures of the company.
5. For the purchase of its own shares or other securities u/s 68.

c) In case of Over Subscription and Pro-rata Allotment, Excess Application Money will be adjusted towards the Amount due on the Allotment or Calls.

d) **Calls-in-Arrear:** When the shareholders fail to pay any instalment (Allotment or call) that has been called up, the amount so unpaid is treated as calls-in-arrear. If not ultimately received, the balance of Calls-in-arrear is deducted from Called-up Capital in the Notes to Balance Sheet.

The accounting entry for calls-in-arrear is as follows:

Bank A/c …………………Dr. (Amount received)

Calls-in-arrear A/c………… Dr. (instalment amount not received)

To Share Allotment/Share Call A/c

If received subsequently, the entry will be –

Bank A/c …………………Dr.

To Calls-in-arrear A/c

e) **Calls-in-Advance:** Section 50 of the Companies Act, 2013, states that –

A company may, if so authorised by its articles, accept from any member, the whole or a part of the amount remaining unpaid on any shares held by him, even if no part of that amount has been called up.

The accounting entry for calls-in-advance are as follows:

(i) For transferring excess application money

Share Application A/c ………………. Dr.

To Calls-in-Advance A/c

(ii) For money received in advance against call

Bank A/c ……………….Dr.

To Calls-in-Advance A/c

(iii) For adjustment of calls-in-advance

Calls-in-Advance A/c …………..Dr.

To Share Call A/c

f) <u>Interest on Calls-in-Arrear & Interest on Calls-in-Advance:</u>

1. Interest on calls-in-arrear may be collected by the directors from the shareholders, if the Articles of Association so permit. In the absence of any specification, the company needs to follow 'Table F' according to which interest @ 10% p.a. from the due date to the date of actual payment is payable by the shareholders.
2. Interest may be paid by a company on calls-in-advance, if the Articles of Association so provide. In the absence of any specification, the company needs to follow 'Table F' according to which interest @ 12% p.a. from the date of receipt to the due date of the concerned instalment is payable.

<u>Interest on Calls-in-Arrear</u>	<u>Interest on Calls-in-Advance</u>
(i) For interest due Shareholders A/c ………………Dr. To Interest on Calls-in-Arrear A/c **(ii) On realization of interest** Bank A/c ……………………Dr. To Shareholders A/c **(iii) For transferring interest to Profit and Loss Account** Interest on Calls-in-Arrear A/c ……………. Dr. To Profit and Loss A/c	**(i) For interest due on calls-in-advance** Interest on Calls-in-Advance A/c …………Dr. To Shareholders A/c **(ii) On payment of interest** Shareholders A/c ……………………Dr. To Bank A/c **(iii) For transferring interest to Profit and Loss Account** Profit and Loss A/c ……………. Dr. To Interest on Calls-in-Advance A/c

g) <u>Expense on Issue of Shares:</u> The common expenses associated with share issue are printing charges of prospectus and application forms, brokerage and commission, underwriting expenses, legal charges etc. These are written off against the profits of the company in the same year.

The accounting entries are:

(i) Upon expenditure incurred

Share Issue Expenses A/c …………. Dr.

To Bank A/c

(ii) When the expenses are written off

Profit and Loss A/c …………………. Dr.

To Share Issue Expenses A/c

Issue of Shares for Consideration other than Cash

- If the shares have been allotted to any person or firm from whom the company has purchased any asset, the following entry will be passed:

  Asset A/c ………………………… Dr.

  To Share Capital A/c

  (Being ... shares allotted……in consideration of purchase of an asset for the company)

- If shares are issued to Promoters for their services, the following entry will be passed:

  Goodwill A/c ………………………… Dr.

  To Share Capital A/c

- Similarly, if shares are issued to Underwriters for underwriting commission, the following entry will be passed:

  Underwriters A/c ………………………… Dr.

  To Share Capital A/c

Forfeiture and Re-issue of Shares:

1. Where issue proceeds on shares are collected in instalments, the shareholders are expected to pay the amount of allotment and subsequent call money as and when they become due. However, if the shareholder fails to pay the same, it results in calls-in-arrear. If the Articles of the company so permit, the company may confiscate the shares on the ground of non-payment of instalments. This is known as Forfeiture of Shares. On forfeiture, however, the amount received on shares till such date is not returnable and the same becomes a capital receipt for the company and transferred to Forfeited Shares A/c.
2. The shares so forfeited may again be re-issued by the company afresh to new shareholders. This process is called Re-issue of Forfeited Shares. These shares are generally re-issued at a price lower than the face value of shares. However, the minimum re-issue price must be equal to called up value less amount collected (capital portion) on each share before forfeiture. The resulting loss is

adjusted against Forfeited Shares A/c. the balance of the Forfeited Shares A/c, representing the net profit on forfeiture and re-issue of shares, is transferred to Capital Reserve A/c.

3. In case the shares are re-issued at a price higher than the face value, the excess amount is not payable to the original shareholders. It is to be transferred to 'Securities Premium A/c'. For shares forfeited but not yet re-issued, the balance of Forfeited Shares A/c should be shown under the head Share Capital in the Balance Sheet.

<u>The accounting entries for forfeiture and re-issue are as follows</u>:

(i) On forfeiture of shares

Share Capital A/c ……………………….Dr. (Called-up value)

Securities Premium A/c …………………Dr. (Premium due but not collected)

To Calls-in-Arrear A/c (Amount unpaid)

To Forfeited Shares A/c (Capital portion received on shares forfeited)

(ii) On re-issue of shares

Bank A/c ………………………. Dr. (Proceeds from re-issue)

Forfeited Shares A/c ……………… Dr. (Discount on re-issue)

To Share Capital A/c (Paid-up value of shares re-issued)

To Securities Premium A/c (Premium on shares re-issued, if any)

(iii) On transfer of profit

Forfeited Shares A/c (Net profit on forfeiture and re-issue)

To Capital Reserve A/c

PROBLEMS FOR CLASS ROOM DISCUSSION

Problem 1:

AK Ltd. made an issue of 10,00,000 equity shares of Rs.10 each, payable fully on application. Subscriptions were received for 12,00,000 shares. Application money in respect of 2,00,000 shares was refunded and shares were duly allotted to the rest. Pass journal entries to give effect to these transactions. **(Illustration 1)**

Problem 2:

BK Ltd. made an issue of 10,00,000 equity shares of Rs.10 each, payable @ Rs.2 on application, Rs.4 on Allotment and Rs.4 on first and final call. Subscriptions were received for 12,00,000 shares. Application money in respect of 2,00,000 shares was refunded and shares were duly allotted to the rest. All the amounts were duly received. Pass journal entries to give effect to these transactions. **(Illustration 2)**

Problem 3:

AB & Co. Ltd. issued 5,00,00,000 Equity shares of Rs.10 each at a premium of Rs.4 per share payable on application. The shares were all subscribed and all money due was received. Give the Journal entries to record the above transactions. **(Illustration 3)**

Problem 4:

CD & Co. Ltd. issued 5,00,00,000 Equity shares of Rs.10 each at a premium of Rs.4 per share payable Rs.1 per share on application, Rs.6 per share on allotment (including premium), Rs.3 on first call and the balance on final call. The shares were all subscribed and all money due was received. Give the Journal entries to record the above transactions. **(Illustration 4)**

Problem 5:

EF & Co. Ltd. issued 5,00,00,000 Equity shares of Rs.10 each at a premium of Rs.4 per share payable Rs.1 per share on application, Rs.6 per share on allotment (including premium), Rs.3 on first call and the balance on final call. The shares were all subscribed and all money due was received except the first call money on 1,00,000 shares and the Final call money on 1,50,000 shares. Give the Journal entries to record the above transactions. **(Illustration 5)**

Problem 6:

GH & Co. Ltd. issued 5,000 Equity shares of Rs.10 each at par, payable Rs.2 per share on application, Rs.4 per share on allotment, Rs.4 on first call and final call. The shares were all subscribed and all money due was received. One shareholder holding 200 shares paid the call money along with the allotment money. The amount was subsequently adjusted. Give the Journal entries to record the above transactions. **(Illustration 6)**

Problem 7:

B Ltd issued 2,000 shares of Rs.100 each at a premium of 10% payable as follows:

On application Rs.20 (1st April 2021). On allotment Rs.40 (including premium) (1st June 2021). On First Call Rs.30 (1st July 2021). On Second & Final call Rs.20 (1st Aug 2021).

Applications were received for 1,800 shares and the directors made allotment in full. One shareholder to whom 40 shares were allotted paid the entire balance on his share holdings with allotment money and another share holder did not pay allotment and 1st call money on his 60 shares but which he paid with final call. Interest should be received @ 5% p.a. on calls-in-arrears and interest should be paid @ 6% p.a. on calls in Advance (as per Articles of the company).

Required: Calculated the amount of interest paid and received on calls-in-advance and calls in arrears respectively on 1st Aug. 2021 and also pass Journal entries for above transactions. **(Illustration 7)**

Problem 8:

ICC Ltd. forfeited 500 equity shares of Rs.10 each fully called up which were issued at a premium 20%. Amount payable on shares were: on application Rs.2; on allotment Rs.5; on first and final call Rs.5. Only application money was paid by the shareholders in respect of these shares. 300 shares out of the above were reissued at Rs.9 per share fully paid. Pass journal entries for the forfeiture and re-issue. **(Illustration 12)**

Problem 9:

Give journal entries for the following:

(1) PK Ltd. forfeited 10,000 equity shares of Rs.10 each for non-payment of first call of Rs.2 and final call of Rs.3 per share. These shares were reissued at a discount of Rs.3.50 per share.

(2) KP Ltd. forfeited 20,000 equity shares of Rs.15 each (including Rs.5 per share as premium), for non-payment of final call of Rs.3 per share. Out of these 10,000 shares were reissued at a discount of Rs.4 per share.

(3) KP Ltd. forfeited 15,000 equity shares of Rs.15 each (including Rs.5 per share as premium), for non-payment of allotment money Rs.8 (including premium money) and first & final call of Rs.5 per share. Out of these 10,000 shares were reissued at Rs.14 per share. **(Illustration 19)**

Problem 10:

SOS Limited issued a prospectus inviting applications for 6,000 shares of Rs.10 each at a premium of Rs.2 per share, payable as follows; On application Rs.2 per share; On allotment Rs.5 per share (including premium): On 1st call Rs.3 per share; On Second and Final Call Rs.2 per share., Applications were receive for 9,000 shares and allotment was made prorate to the applicants of 7,500 shares, the remaining applicants were refused allotment. Money overpaid on applications were applied towards sums due on allotment. D to whom 100 shares were allotted, failed to pay the allotment money and on his subsequent failure to pay the first call, his shares were forfeited. Z, the holder of 200 shares, failed to pay both the calls, and his shares were forfeited after the second and final call. Of the shares forfeited 200 shares were sold to C credited as fully paid up for Rs.8.50 per share, the whole of D's shares being included. **(Illustration 14)**

Problem 11:

JK Ltd is a company with an authorized capital of Rs.10 lacs in equity shares of Rs.10 each, of which 600000 shares had been issued and fully paid on 30th June, 2020. The company proposed to make a further issue of 100000 of these Rs.10 shares at a price of Rs.14 each the arrangements for payment being:

Rs.2 per share payable on application, to be received by 1st July 2020.

Allotment to be made on 10th July and a further Rs.5 per shares (including the premium) to be payable.

The final call for the balance to be made, and the money received by 31st January 2021.

Applications were received for 355000 shares and were dealt with as follows:

Applicants for 5000 shares received allotment in full.

Applicants for 30000 shares received an allotment of one share for every 2 applied for, no money was returned to the applicant, the surplus on application being used to reduce the amount due on allotment.

Applicants for 320000 shares received an allotment of one share for every four applied for, the money due on allotment was retained by the company, the excess being returned to the applicant.

The money due on final call was received on the due date.

You are required to record these transactions in the journal of JK Limited. **(Illustration 17)**

2. PREPERATION OF FINANCIAL STATEMENTS OF COMPANIES (SCHEDULEIII-DIVISION-I)

Meaning of Financial Statement:

Financial Statements as per Section 2(40) of the Companies Act, 2013, inter-alia include

i) a balance sheet as at the end of the financial year;

ii) a profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;

iii) cash flow statement for the financial year;

iv) any explanatory note annexed to, or forming part of, any document referred to in (i) to (iv) above

Note: However, the financial statement, with respect to one person company, small company and dormant company (Section 455) may not include cash flow statement.

Frequency of Financial Statements:

Financial statements are prepared as –

i) Annual financial statements (i.e., once a financial year)

ii) Quarterly financial statements which are prepared by listed companies on quarterly basis as per SEBI requirements.

PREPARATION OF FINANCIAL STATEMENTS AS PER COMPANIES ACT 2013:

- **Section 129(1):** The financial statements shall give a true and fair view of the state of affairs of the company, comply with the accounting standards notified under section 133 and shall be in the form or forms as may be provided for different class or classes of companies in Schedule III.
- **Section 129(2):** At every annual general meeting of a company, the Board of Directors of the company shall lay before such meeting financial statements for the financial year.
- **Section 129(3):** Where a company has one or more subsidiaries, it shall, in addition to financial statements provided under sub-section (2), prepare a consolidated financial statement.

Form and Content of Financial Statements:

The form and content of Financial Statements have been specified in Schedule III of the Companies Act, 2013. The objective of such specification is to improve the comparability of financial information across entities. Schedule III of the Companies Act, 2013 comprises of three divisions as follows:

(a) Division I: General Instructions for Preparation of Balance Sheet and Statement of Profit and Loss of a company whose Financial Statements are required to comply with the Companies (Accounting Standards) Rules, 2021.

(b) Division II: General Instructions for Preparation of Financial Statements of a company whose Financial Statements are drawn up in compliance of the Companies (Indian Accounting Standards) Rules, 2015.

(c) **Division III:** General Instructions for Preparation of Financial Statements for a Non-Banking Financial Company (NBFC) whose financial statements are drawn up in compliance of the Companies (Indian Accounting Standards) Rules, 2015.

SCHEDULE III-DIVISION-1-PART I-BALANCE SHEET

Name of the company…………….

Balance sheet as at…………………

			Particulars	Notes No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
			1	2	3	4
			EQUITY AND LIABILITIES:			
			Shareholder's funds			
1	a		Share capital			
	b		Reserves and Surplus			
	c		Money received against share warrants			
2			**Share application money pending allotment**			
			Non-current liabilities			
	a		Long term borrowings			
3	b		Deferred tax liabilities (Net)			
	c		Other long -term liabilities			
	d		Long term provisions			
			Current liabilities			
	a		Short term borrowings			
4	b		Trade Payable			
	c		Other current liabilities			
	d		Short - term provisions			
			TOTAL			
			ASSETS:			
1			Non-current assets			
	a		Property, Plant & Equipment and Intangible Assets			

		i	Property, Plant & Equipment			
		ii	Intangible assets			
		iii	Capital Work - in progress			
		iv	Intangible assets under development			
	b		Non-current investments			
	c		Deferred tax assets (Net)			
	d		Long term loans and advances			
	e		Other non-current assets			
2			**Current Assets**			
	a		Current Investments			
	b		Inventories			
	c		Trade receivables			
	d		Cash and cash equivalents			
	e		Short - term loans and advances			
	f		Other current assets			
			TOTAL			

DEFINITION OF CURRENT ASSET:

An asset shall be classified as current when it satisfies any of the following

CRITERIA:

a) it is expected to be realized in, or is intended for sale or consumption in, the company's normal operating cycle;

b) it is held primarily for the purpose of being traded;

c) it is expected to be realized within twelve months after the reporting date; or

d) it is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

DEFINITION OF CURRENT LIABILITY:

A liability shall be classified as current when it satisfies any of the following

CRITERIA:

a) It is expected to be settled in the company's normal operating cycle;

b) It is held primarily for the purpose of being traded;

c) It is due to be settled within twelve months after the reporting date; or

d) The company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

NOTES TO ACCOUNTS:

1) SHARE CAPITAL:

For each class of share capital (different classes of preference shares to be treated separately):

a) The number and amount of shares authorized;

b) The number of shares issued, subscribed and fully paid, and subscribed but not fully paid;

c) Par value per share;

d) A reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period;

e) The rights, preferences and restrictions attaching to each class of shares including restrictions on the distribution of dividends and the repayment of capital;

f) Shares in respect of each class in the company held by its holding company or its ultimate holding company including shares held by or by subsidiaries or associates of the holding company or the ultimate holding company in aggregate;

g) Shares in the company held by each shareholder holding more than 5 percent shares specifying the number of shares held;

h) Shares reserved for issue under options and contracts/commitments for the sale of shares/disinvestment, including the terms and amounts;

i) For the period of five years immediately preceding the date as at which the Balance Sheet is prepared:

(i) Aggregate number and class of shares allotted as fully paid up pursuant to contract(s) without payment being received in cash.

(ii) Aggregate number and class of shares allotted as fully paid up by way of bonus shares.

(iii) Aggregate number and class of shares bought back.

j) Terms of any securities convertible into equity/preference shares issued along with the earliest date of conversion in descending order starting from the farthest such date.

k) Calls unpaid (showing aggregate value of calls unpaid by directors and officers)

l) Forfeited shares (amount originally paid up).

m) A company shall disclose Shareholding of Promoters* as below:

Shares held by promoters at the end of the year				% Change during the year***
S. No	**Promoter name**	**No. of Shares****	**% of total shares****	
Total				

*Promoter here means promoter as defined in the Companies Act, 2013.

** Details shall be given separately for each class of shares

*** Percentage change shall be computed with respect to the number at the beginning of the year or if issued during the year for the first time then with respect to the date of issue.

1. RESERVES AND SURPLUS

a) Reserves and Surplus shall be classified as:

i) Capital Reserves;

ii) Capital Redemption Reserve;

iii) Securities Premium;

iv) Debenture Redemption Reserve;

v) Revaluation Reserve;

vi) Share Options Outstanding Account;

vii) Other Reserves – (specify the nature and purpose of each reserve and the amount in respect thereof);

viii) Surplus i.e. balance in Statement of Profit & Loss disclosing allocations and appropriations such as dividend, bonus shares and transfer to/from reserves etc.

(Additions and deductions since last balance sheet to be shown under each of the specified heads)

b) A reserve specifically represented by earmarked investments shall be termed as a 'fund'.

c) Debit balance of statement of profit and loss shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserves and Surplus', after adjusting negative balance of surplus, if any, shall be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative.

2. LONG-TERM BORROWINGS

a) Long-term borrowings shall be classified as:

i) Bonds/debentures.

ii) Term loans

1) From banks.

2) From other parties

iii) Deferred payment liabilities.

iv) Deposits.

v) Loans and advances from related parties.

vi) Long term maturities of finance lease obligations

vii) Other loans and advances (specify nature).

b) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.

3. OTHER LONG- TERM LIABILITIES

Other Long-term Liabilities shall be classified as:

a) Trade payables

b) Others

4. LONG-TERM PROVISIONS

The amounts shall be classified as:

a) Provision for employee benefits

b) Others (specify nature).

5. SHORT-TERM BORROWINGS

a) Short-term borrowings shall be classified as:

i) Loans repayable on demand

(1) From banks

(2) From other parties

ii) Loans and advances from related parties.

iii) Deposits.

iv) Other loans and advances (specify nature).

b) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.

c) Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed

d) Current maturities of long -term borrowings shall be disclosed separately.

6. OTHER CURRENT LIABILITIES

The amounts shall be classified as

a) Current maturities of finance lease obligations.

b) Interest accrued but not due on borrowings.

c) Interest accrued and due on borrowings.

d) Income received in advance.

e) Unpaid dividends

f) Application money received for allotment of securities and due for refund and interest accrued thereon.

g) Unpaid matured deposits and interest accrued thereon.

h) Unpaid matured debentures and interest accrued thereon.

i) Other payables (specify nature).

7. SHORT-TERM PROVISIONS:

The amounts shall be classified as:

a) Provision for employee benefits.

b) Others (specify nature).

8. Property, Plant and Equipment

a) Classification shall be given as:

i) Land.

ii) Buildings.

iii) Plant and Equipment.

iv) Furniture and Fixtures.

v) Vehicles.

vi) Office equipment.

vii) Others (specify nature).

b) Assets under lease shall be separately specified under each class of asset.

c) A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations, amount of change due to revaluation (if change is 10% or more in the aggregate of the net carrying value of each class of Property, Plant and Equipment) and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately.

9. INTANGIBLE ASSETS:

a) Classification shall be given as:

i) Goodwill.

ii) Brands /trademarks.

iii) Computer software.

iv) Mastheads and publishing titles.

v) Mining rights.

vi) Copyrights, and patents and other intellectual property rights, services and operating rights.

vii) Recipes, formulae, models, designs and prototypes.

viii) Licenses and franchise.

ix) Others (specify nature).

b) A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations, amount of change due to revaluation (if change is 10% or more in the aggregate of the net carrying value of each class of intangible assets) and other adjustments and the related depreciation and impairment losses or reversals shall be disclosed separately.

10. <u>NON-CURRENT INVESTMENTS:</u>

a) Non-current investments shall be classified as trade investments and other investments and further classified as:

i) Investment property.

ii) Investments in Equity Instruments.

iii) Investments in preference shares

iv) Investments in Government or trust securities.

v) Investments in debentures or bonds.

vi) Investments in Mutual Funds.

vii) Investments in partnership firms

viii) Other non-current investments (specify nature) Investments carried at other than at cost should be separately stated specifying the basis for valuation thereof.

b) The following shall also be disclosed:

i) Aggregate amount of quoted investments and market value thereof;

ii) Aggregate amount of unquoted investments.

iii) Aggregate provision for diminution in value of investments.

11. <u>LONG-TERM LOANS AND ADVANCES:</u>

a) Long-term loans and advances shall be classified as:

i) Capital Advances.

ii) Loans and advances to related parties (giving details thereof);

iii) Other loans and advances (specify nature).

b) The above shall also be separately sub-classified as:

i) Secured, considered good.

ii) Unsecured, considered good.

iii) Doubtful

12. <u>OTHER NON-CURRENT ASSETS</u>

Other non-current assets shall be classified as:

a) Long Term Trade Receivables (including trade receivables on deferred credit terms);

i) Security Deposits.

ii) (Others (specify nature);

b) Long term Trade Receivables, shall be sub-classified as:

i) Secured, considered good.

ii) Unsecured considered good.

iii) Doubtful

c) For trade receivables outstanding, ageing schedule shall be given.

13. <u>CURRENT INVESTMENTS</u>

a) Current investments shall be classified as:

i) Investments in Equity Instruments.

ii) Investment in Preference Shares

iii) Investments in government or trust securities.

iv) Investments in debentures or bonds.

v) Investments in Mutual Funds.

vi) Investments in partnership firms

vii) Other investments (specify nature)

14) <u>INVENTORIES</u>

a) Inventories shall be classified as:

i) Raw materials.

ii) Work-in-progress.

iii) Finished goods.

iv) Stock-in-trade (in respect of goods acquired for trading);

v) Stores and spares.

vi) Loose tools.

vii) Others (specify nature).

b) Goods-in-transit shall be disclosed under the relevant sub-head of inventories.

c) Mode of valuation shall be stated.

15) <u>TRADE RECEIVABLES:</u>

a) For trade receivables outstanding, Ageing schedules shall be given.

b) Trade receivables shall be sub-classified as:

i) Secured, considered good.

ii) Unsecured considered good.

iii) Doubtful.

c) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.

d) For trade receivables outstanding, the following ageing schedules shall be given.

16) <u>CASH AND CASH EQUIVALENTS</u>

a) Cash and cash equivalents shall be classified as:

i) Balances with banks.

ii) Cheques, drafts on hand.

iii) Cash on hand.

iv) Others (specify nature).

17) <u>SHORT-TERM LOANS AND ADVANCES</u>

a) Short-term loans and advances shall be classified as:

i) Loans and advances to related parties (giving details thereof);

ii) Others (specify nature).

b) The above shall also be sub-classified as:

i) Secured, considered good.

ii) Unsecured, considered good.

iii) Doubtful.

c) Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.

18) <u>OTHER CURRENT ASSETS (SPECIFY NATURE</u>).

This is an all-inclusive heading, which incorporates current assets that do not fit into any other asset categories.

19) <u>CONTINGENT LIABILITIES AND COMMITMENTS (TO THE EXTENT NOT PROVIDED FOR)</u>

a) Contingent liabilities shall be classified as:

i) Claims against the company not acknowledged as debt;

ii) Guarantees;

iii) Other money for which the company is contingently liable

b) Commitments shall be classified as:

i) Estimated amount of contracts remaining to be executed on capital account and not provided for;

ii) Uncalled liability on shares and other investments partly paid

iii) Other commitments (specify nature)

c) **<u>Additional Regulatory Information</u>**

i) Title deeds of Immovable Property not held in name of the Company

ii) Where the Company has borrowings from banks or financial institutions on the basis of security of current assets

20) Following Ratios to be disclosed:-

i) Current Ratio

ii) Debt-Equity Ratio,

iii) Debt Service Coverage Ratio,

iv) Return on Equity Ratio,

v) Inventory turnover ratio,

vi) Trade Receivables turnover ratio,

iii) Trade payables turnover ratio,

iv) Net capital turnover ratio,

v) Net profit ratio,

vi) Return on Capital employed,

vii) Return on investment

viii) Utilisation of Borrowed funds and share premium:

SCHDULE III-DIVISION-I-PART-II-STATEMENT OF PROFIT AND LOSS

Name of the company…………………..

P & l statement for the year ended…………….

	Particulars	Note No.	Figures for the current reporting period	Figures for the previous reporting period
I	Revenue from operations		xxx	xxx
II	Other Income		xxx	xxx
III	Total Revenue (I + II)		xxx	xxx
IV	Expenses:			
	Cost of materials consumed		xxx	xxx
	Purchases of Stock in Trade		xxx	xxx
	Changes in inventories of finished goods		xxx	xxx
	Changes in Work in progress and stock-in-Trade			
	Employee benefits expense			
	Finance costs			
	Depreciation and amortization expenses			
	Other expenses			
	Total Expenses			
V	Profit before exceptional and extraordinary items and tax (III -IV)		xxx	xxx
VI	Exceptional items		xxx	xxx
VII	Profit before extraordinary items and tax (V - VI)		xxx	xxx
VIII	Extraordinary items		xxx	xxx
IX	Profits before tax (VII - VIII)		xxx	xxx
X	Tax Expense:			
	(1) Current tax		xxx	xxx
	(2) Deferred tax		xxx	xxx
XI	Profit (Loss) for the period (IX - X)		xxx	xxx
XII	Earnings per equity share:			
	(1) Basic		xxx	xxx
	(2) Diluted		xxx	xxx

1) The provisions of this Part shall apply to the income and expenditure account referred to in sub-clause (ii) of Clause (40) of Section 2 in like manner as they apply to a statement of profit and loss.

2) In respect of a company other than a finance company revenue from operations shall disclose separately in the notes revenue from

i) Sale of products;

ii) Sale of services;

a) " Grants or donations received (relevant in case of section 8 companies only)";

b) Other operating revenues;

Less:

i) Excise duty

c) In respect of a finance company, revenue from operations shall include revenue from

i) Interest; and

ii) Other financial services

Revenue under each of the above heads shall be disclosed separately by way of notes to accounts to the extent applicable.

3) **Other income**

Other income shall be classified as:

a) Interest Income (in case of a company other than a finance company);

b) Dividend Income;

c) Net gain/loss on sale of investments

4) **Finance Costs**

Finance costs shall be classified as:

a) Interest expense;

b) Other borrowing costs;

c) Applicable net gain/loss on foreign currency transactions and translation.

5) **Employee benefit expenses**

a) salaries and wages,

b) contribution to provident and other funds,

c) expense on Employee Stock Option Scheme (ESOP) and Employee Stock Purchase Plan (ESPP),

d) staff welfare expenses

6) Any item of income or expenditure which exceeds one per cent of the revenue from operations or 1,00,000, whichever is higher should need to disclose separately.

7) In case of companies covered u/s 135, amount of expenditure incurred on corporate social responsibility activities.

8) Details of items of exceptional and extraordinary nature;

9) Prior period items etc

10) **Provision for Income Tax, Advance Tax and Assessed Tax of Prior Year**

There may be following three situations:

(i) When Assessed Tax Liability = Provision for Income Tax

Here, no further provision is required to be created. Now –

- If Advance tax paid = Assessed Tax Liability, Provision for Income Tax and Advance Tax squared off.
- If Advance tax paid < Assessed Tax Liability, Provision for Income Tax and Advance Tax squared off and their difference is treated as Income Tax Payable to appear under Other Current Liabilities.
- If Advance tax paid > Assessed Tax Liability, Provision for Income Tax and Advance Tax squared off and their difference is treated as Income Tax Refund to appear under Other Current Assets.

(ii) When Assessed Tax Liability > Provision for Income Tax

Here, further provision is required to be created by debiting Profit & Loss A/c. The additional Provision for income tax will appear under the line-item Tax Expense in the Statement of Profit and Loss as Prior Period Tax.

Further, adjustment of Advance tax and Provision for Income Tax shall be done in the same way as explained in situation (i).

(iii) When Assessed Tax Liability < Provision for Income Tax

Here, excess provision is required to be written back by crediting it to Profit & Loss A/c. The excess Provision for income tax will appear under the line-item Tax Expense in the Statement of Profit and Loss as Prior Period Excess Provision.

Further, adjustment of Advance tax and Provision for Income Tax shall be done in the same way as explained in situation (i).

PROBLEMS FOR CLASS ROOM DISCUSSION

A) PROBLEMS BASED ON SCHEDULE III

PROBLEM 1:

In the financial statements of the financial year 20X1-20X2, Alpha Ltd. has mentioned in the notes to accounts that during financial year, 24,000 equity shares of Rs. 10 each were issued as fully paid bonus shares. However, the source from which these bonus shares were issued has not been disclosed. Is such non-disclosure a violation of the Schedule III to the Companies Act? Comment. **(SM)**

PROBLEM 2:

The management of Loyal Ltd. contends that the work in process is not valued since it is difficult to ascertain the same in view of the multiple processes involved. They opine that the value of opening and closing work in process would be more or less the same. Accordingly, the management had not separately disclosed work in process in its financial statements. Comment in line with Schedule III. **(SM)**

PROBLEM 3:

Futura Ltd. had the following items under the head "Reserves and Surplus" in the Balance Sheet as on31st March, 20X1:

PARTICULARS	Amount Rs. in lakhs
Securities Premium Account	80
Capital Reserve	60
General Reserve	90

The company had an accumulated loss of Rs. 250 lakhs on the same date, which it has disclosed under the head "Statement of Profit and Loss" as asset in its Balance Sheet. Comment on accuracy of this treatment in line with Schedule III to the Companies Act, 2013. **(SM)**

PROBLEM 4:

Sumedha Ltd. took a loan from bank for Rs. 10,00,000 to be settled within 5 years in 10 equal half yearly instalments with interest. First instalment is due on 30.09.20X1 of Rs. 1,00,000. Determine how the loan will be classified in preparation of Financial Statements of Sumedha Ltd. for the year ended 31st March, 20X1 according to Schedule III. **(SM)**

PROBLEM 5:

State under which head these accounts should be classified in Balance Sheet, as per Schedule III of the Companies Act, 2013:

i. Share application money received in excess of issued share capital.

ii. Share option outstanding account.

iii. Unpaid matured debenture and interest accrued thereon.

iv. Uncalled liability on shares and other partly paid investments.

v. Calls unpaid. **(RTP-NOV-2021 2(b))**

PROBLEM 6:

The following is the Trial Balance of H Ltd., as on 31st March 2021. **(20M)**

	Dr.	**Cr.**
Equity Capital (Shares of 100 each)		8,05,000
5,000, 6% preference shares of Rs. 100 each		5,00,000
9% Debentures		4,00,000
General Reserve		40,00,000
Profit & Loss A/c. (of previous year)		72,000
Sales		60,00,000
Trade Payables		10,40,000
Provision for Depreciation on Plant & Machinery		1,72,000
Suspense Account		40,000
Land at cost	24,00,000	
Plant & Machinery at cost	7,70,000	
Trade Receivables	19,60,000	
Inventories (31-03-2021)	9,50,000	
Bank	2,30,900	
Adjusted Purchases	22,32,100	
Factory Expenses	15,00,000	
Administration Expenses	3,00,000	
Selling Expenses	14,00,000	

Debenture Interest	36,000	
Goodwill	12,50,000	
	1,30,29,000	**1,30,29,000**

Additional Information:

a) The authorized share capital of the company is:

5000, 6% preference shares of Rs. 100 each 5,00,000

10000, equity shares of Rs. 100 each 10,00,000

Issued equity capital as on 1st April 2020 stood at Rs. 720,000, that is 6,000 shares fully paid and 2,000 shares Rs. 60 paid. The directors made a call of Rs. 40 per share on 1st October 2020. A Shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ Rs. 90 per share as fully paid.

b) On 31st March 2021, the Directors declared a dividend of 5% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

c) The company on the advice of independent valuer wishes to revalue the land at Rs. 36,00,000.

d) Suspense account of Rs. 40,000 represents amount received for the sale of some of the machinery on 1-4-2020. The cost of the machinery was Rs. 100,000 and the accumulated depreciation thereon being Rs. 30,000.

e) Depreciation is to be provided on plant and machinery at 10% on cost.

f) Amortize 1/5th of Goodwill.

You are required to prepare H Limited's Balance Sheet as on 31-3-2021 and Statement of Profit and Loss with notes to accounts for the year ended 31-3-2021 as per Schedule III of the Companies Act, 2013. Ignore previous year's figures & taxation. **(JULY 2021 CA Q.P-4)**

PROBLEM 7:

PQR Ltd. was registered with a nominal capital of Rs.20,00,000 divided into shares of Rs.100 each. The following Trial Balance is extracted from the books on 31st March, 2021:

Particulars	Rs.	Particulars	Rs.
Buildings	11,60,000	Sales	20,80,000
Machinery	4,00,000	Outstanding Expenses	8,000
Closing Stock	3,60,000	Provision for Doubtful Debts (1-4-2020)	12,000
Loose Tools	92,000	Equity Share Capital	8,00,000
Purchases (Adjusted)	8,40,000	General Reserve	1,60,000

Salaries	2,40,000	Profit and Loss A/c (1-4-2020)	1,00,000
Directors' Fees	40,000	Creditors	3,68,000
Rent	1,04,000	Provision for depreciation:	
Depreciation	80,000	On Building	2,00,000
Bad Debts	24,000	On Machinery	2,20,000
Investment	4,80,000	14% Debentures	8,00,000
Interest accrued on investment	8,000	Interest on Debentures accrued but not due	56,000
Debenture Interest	1,12,000	Interest on Investments	48,000
Advance Tax	2,40,000	Unclaimed dividend	20,000
Sundry expenses	72,000		
Debtors	5,00,000		
Bank	1,20,000		
	48,72,000		**48,72,000**

You are required to prepare statement of Profit and Loss for the year ending 31st March, 2017 and Balance sheet as at that date after taking into consideration the following information:

(i) Closing stock is more than opening stock by Rs.3,20,000.

(ii) Provide to doubtful debts @ 4% on Debtors.

(iii) Make a provision for income tax @30%.

(iv) Depreciation expense included depreciation of Rs.32,000 on Building and that of Rs.48,000 on Machinery.

(v) The directors declared a dividend @ 25% and transfer to General Reserve @ 10%.

(vi) Bills Discounted but not yet matured Rs.40,000.

[Answer: Balance Sheet total Rs. 29,20,000] {CMA SM-ILLUSTRATION 7}

PROBLEM 8:

From the following particulars furnished by Pioneer Ltd., prepare the Balance Sheet as at 31st March, 20X1 as required by Schedule III of the Companies Act. Give notes at the foot of the Balance Sheet as may be found necessary:

Particulars	Debit Rs.	Credit Rs.
Equity Capital (Face value of Rs. 100)		10,00,000
Calls in Arrears	1,000	

Land	2,00,000	
Building	3,50,000	
Plant and Machinery	5,25,000	
Furniture	50,000	
General Reserve		2,10,000
Loan from State Financial Corporation	1,50,000	
Inventory: Finished Goods 2,00,000		
Raw Materials 50,000	2,50,000	
Provision for Taxation		68,000
Trade receivables	2,00,000	
Advances	42,700	
Dividend Payable		60,000
Profit and Loss Account		86,700
Cash Balance	30,000	
Cash at Bank	2,47,000	
Loans (Unsecured)		1,21,000
Trade payables (For Goods and Expenses)		2,00,000
	18,95,700	**18,95,700**

The following additional information is also provided:

(1) 2,000 equity shares were issued for consideration other than cash.

(2) Trade receivables of Rs. 52,000 are due for more than six months.

(3) The cost of assets:

Building	Rs. 4,00,000
Plant and Machinery	Rs. 7,00,000
Furniture	Rs. 62,500

(4) The balance of Rs. 1,50,000 in the loan account with State Finance Corporation is inclusive of Rs. 7,500 for interest accrued but not due. The loan is secured by hypothecation of the Plant and Machinery.

(5) Balance at Bank includes Rs. 2,000 with Perfect Bank Ltd., which is not a Scheduled Bank.

(6) The company had contract for the erection of machinery at Rs. 1,50,000 which is still incomplete. **(ANS: BALANCE SHEET TOTAL- RS.18,94,700) (SM)**

PROBLEM 9:

While preparing the Balance Sheet as on 31.03.2021, the Accountant of ABC Ltd. is confused regarding classification of following Trade Payables into current and non-current.

S. No	Amount due (Rs.)	Due from	To be settled on
1	3,10,000	01.04.2020	18.05.2021
2	1,80,000	01.06.2020	15.09.2022
3	40,000	01.08.2020	15.07.2022
4	15,000	01.01.2021	30.04.2022
5	2,30,000	06.03.2021	05.07.2022
6	1,08,000	15.03.2021	31.12.2021

The normal operating cycle of the company is 15 months. Advice the Accountant on classification with reason. **(CMA SM ILLUSTRATION 2)**

PROBLEM 10:

X Ltd., a manufacturer-cum trader, provides you the following details for the financial year ended on 31.03.2021.

Item of Inventory	Balance on 01.04.2020 (Rs.)	Balance on 31.03.2021 (Rs.)	Purchases during the year (Rs.)
Raw materials	2,00,000	2,50,000	5,00,000
WIP	1,20,400	1,50,200	-
Finished Goods	5,10,000	3,50,000	-
Stock in trade	59,000	1,25,000	-

You are required to draft an extract of the Statement of Profit and Loss and also show the relevant Notes to Accounts. **(CMA SM ILLUSTRATION 3)**

PROBLEM 11:

The following are the extracts from the Trial Balance of Y Ltd. on March 31, 2021: (figures in Rs.)

Provision for current tax (2019 – 20)	4,00,000	Tax deducted at source (2020 – 21)	20,000
Advance tax paid (2019 -20)	3,60,000	Advance tax paid(2020 – 21)	2,00,000

The assessment for the year 2019-20 was finalized during the year 2020-21. The total tax liability for that year was fixed at Rs.4,40,000 and the net amount payable for the year 2020-21 has not yet been paid. The net profit before tax for the year 2020-21 amounted to Rs.8,00,000. Balance of Profit & Loss

A/c at the end of 2019-20 was Rs.4,00,000. Assume corporate income tax @ 35% (inclusive of surcharge and education cess) You are required to draft:

(a) Extract of Statement of Profit and Loss for the year ended March 31,2021 along with the relevant Notes; and (b) Extract of Balance Sheet as on March 31, 2021 along with the relevant Notes.

(CMA SM ILLUSTRATION 4)

PROBLEM 12:

The following information has been extracted from the books of account of Hero Ltd. as at 31st March, 2021:

Particulars	**Dr. (Rs. '000)**	**Cr. (Rs. '000)**
Administration Expenses	480	
Cash at Bank and on Hand	228	
Cash Received on Sale of Fittings		10
Long Term Loan		70
Investments	200	
Depreciation on Fixtures, Fittings, Tools and Equipment (1st April, 2020)		260
Distribution Costs	102	
Factory Closure Costs	60	
Fixtures, Fittings, Tools and Equipment at Cost	680	
Profit & Loss Balance (at 1st April, 2020)		80
Purchase of Equipment	120	
Purchases of Goods for Resale	1710	
Sales (net of Excise Duty)		3,000
Share Capital (1,00,000 shares of Rs.10 each fully paid)		1,000
Stock (at 1st April, 2020)	140	
Trade Creditors		80
Trade Debtors	780	
	4,500	4,500

Additional Information:

1. The stock at 31st March, 2021 (valued at the lower of cost or net realizable value) was estimated to be worth Rs.2,00,000.

2. Fixtures, fittings, tools and equipment all related to administration. Depreciation is charged at a rate of 20% per annum on cost. A full year's depreciation is charged in the year of acquisition, but no depreciation is charged in the year of disposal.
3. During the year to 31st March, 2021, the Company purchased equipment of Rs.1,20,000. It also sold some fittings (which had originally cost Rs.60,000) for Rs.10,000 and for which depreciation of Rs.30,000 had been set aside.
4. The average Income tax for the Company is 50%. Factory closure cost is to be presumed as an allowable expenditure for Income tax purpose.
5. The company proposes to pay a dividend of 20% per Equity Share. Profits transferred to reserves Rs.30,000.

Prepare Hero Ltd.'s Statement of Profit and Loss for the year to 31st March, 2021 and balance Sheet as at that date in accordance with the Companies Act, 2013 as per Division I of schedule III along with the Notes on Accounts containing only the significant accounting policies.

(CMA SM ILLUSTRATION 5)

MCQ, FILL IN THE BLANKS, TRUE OR FALSE

MCQs

1) Trade payables as per Schedule III will include:

(a) Dues payable in respect to statutory obligation

(b) Interest accrued on trade payables

(c) Bills payables.

2) Securities Premium Account is shown on the liabilities side in the Balance Sheet under the heading:

(a) Reserves and Surplus.

(b) Current Liabilities.

(c) Share Capital.

3) "Fixed assets held for sale" will be classified in the company's balance sheet as

(a) Current asset

(b) Non-current asset

(c) Capital work- in- progress

4) Current maturities of long-term debt will come under

(a) Current Liabilities.

(b) Short term borrowings.

(c) Long-term borrowings.

5) Which of the following is not a current liability as per Schedule III?

(a) Bank overdraft

(b) Net deferred tax liability

(c) Dividend declared.

6) As per the Schedule III, separate disclosure is required for an item of income or expenditure which exceeds:

(a)1 % of Revenue from operations or Rs. 1,00,000 whichever is lower

(b) 1% of Revenue or Rs. 5,000

(c) 1% of Revenue from operations or Rs. 1,00,000 whichever is higher.

7) Few friends created a start-up and formed private company for production and marketing of product. At the end of financial year, their company is not required to prepare:

(a) Cash flow statement

(b) Balance Sheet and Profit & Loss Account

(c) Notes to Accounts.

8) As per Schedule III of Companies Act 2013, while preparing the financial statements in case of a Finance Company, interest received from borrowers should be shown under

(a) Revenue from operation

(b) Other Income

(c) Current assets

(d) Non-current assets

9) Installment of principal amount of long-term loan payable within next 12 months is shown under Balance Sheet of a company under the heading

(a) Non-current Assets

(b) Non-current Liabilities

(c) Current Assets

(d) Current Liabilities

10) In case of purchase of assets under instalment payment system, instalments due after 12 months from the reporting date are shown as

(a) Current liability

(b) Current assets

(c) Non-current liability

(d) Non-current assets

11) For the issuer, unpaid matured debentures and interest accrued thereon will be shown under the head

(a) Non-current liabilities

(b) Current liabilities

(c) Non-current assets

(d) Current assets

MCQ's KEY:

1. c	2. a	3. a	4. b	5. b	6. c
7. a	8. a	9. d	10. c	11. b	

State True and False:

1) Interest accrued and due should be shown under the head Other Current Liabilities in a Balance Sheet of a Company. (T)
2) Interest on loan is included in 'other operating expenses' under the Statement of Profit and Loss. (F)
3) As per Schedule III of Companies Act 2013, interest received on convertible debentures is shown under Finance Cost in the Statement of Profit and Loss. (F)
4) Part I of Schedule III is related to preparation of Profit and Loss Statement. (F)
5) Interest income in case of a Finance Company is treated as a part of revenue from Operation. (T)
6) Schedule III deals only with presentation and disclosure requirements. (T)
7) The aggregate amount of the balance of 'Reserve and Surplus', is to be shown after adjusting negative balance of surplus/ Loss, if any. (T)
8) 2,00,000, 8% Preference Shares of Rs.100 each will come under: Equity and Liabilities – Shareholders'

funds - Share Capital (Schedule III). (T)

Fill in the Blanks:

1. Interest expenses are _______________ costs.
2. Investment of Rs.45,00,000 in 40,000 12% Debenture of Rs.100 each of Amrit Ltd. will come under: Assets - Non-current Assets _______________.
3. Provision for taxation of Rs.88,000 will come under: Equity and Liabilities under ____________ Short-term Provision.
4. Short-Term Borrowings will include all Loans within a period of _____ months from the date of the loan.
5. Stock-in-Trade (in respect of goods acquired for Trading) are classified as ____________.

[Answer: 1. Finance; 2. Non-current Investments; 3. Current Liabilities; 4. 12; 5. Inventories.]

Short Essay Type Questions:

1. Write short note on: Applicability of various divisions of Schedule III of Companies Act 2013
2. Write short note on: Schedule III disclosure requirement for Trade Receivables
3. Write short note on: Schedule III disclosure requirement for Cash and Cash Equivalent
4. Write short note on: Schedule III disclosure requirement for Trade Payables

3. ACCOUNTING FOR BONUS AND RIGHTS ISSUE

MEANING:

Bonus shares are shares which are issued by a company free of cost to its existing members on a pro-rata basis.

Note:

- Established companies that have already built-up reserves sometimes decides to capitalize a part of these reserves by issuing bonus shares to existing shareholders, without requiring the shareholders to pay any consideration.
- Since bonus shares requires capitalization of reserves, it leads to decrease in Reserve & Surplus and increase in the issued capital but does not bring any change in cash flow and net worth.

WAYS TO CAPITALIZE PROFITS OR RESERVES

a. by paying up amounts unpaid on existing partly paid shares so as to make them fully paid-up shares, or

b. by issuing fully paid bonus shares to the existing members.

PROVISIONS OF THE COMPANIES ACT, 2013:

1. As per Section 63 of the Companies Act 2013, a company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of—

  a. its free reserves;

  b. the securities premium account; or

  c. the capital redemption reserve account:

  Provided that no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets.

2. As per Section 63(2) of the Companies Act, 2013, at the time of issue of Bonus shares following provisions should be complied.

  a. it is authorised by its articles;

  b. it has, on the recommendation of the Board, been authorised in the general meeting of the company;

  c. it has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;

  d. it has not defaulted in respect of the payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus;

  e. the partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up.

f. it complies with such other conditions as may be prescribed.

Note: The bonus shares shall not be issued in lieu of dividend.

SEBI GUIDELINES ON ISSUE OF BONUS ISSUES

A listed company proposing to issue bonus shares shall comply with the following requirements:

1. The articles of association of the company must contain a provision for capitalisation of reserves, etc. If there is no such provision in the articles the company must pass a resolution at its general meeting making provision in the articles of association for capitalization.
2. The company has not defaulted in payment of interest or principal in respect of fixed deposits and interest on existing debentures or principal on redemption.
3. The company has not defaulted in payment of statutory dues of the employees such as contribution to provident fund, gratuity etc.
4. The partly-paid shares, if any, outstanding on the date of allotment are required to be made fully paid-up.
5. **(a)** No company shall, pending conversion of FCDs/PCDs, issue any by way of bonus unless similar benefit is extended to the holders of such FCDs/though reservation of shares in proportion to such convertible part of FCDs or PCDs.

   (b) The shares so reserved may be issued at the time of conversion(s) of such debentures on the same terms on which the bonus issues were made.
6. The bonus issue shall be made out of free reserves built out of the genuine profits or securities premium collected in cash.
7. Reserves created by revaluation of fixed assets shall not be capitalised. 8. The declaration of bonus issue, in lieu of dividend, shall not be made.
8. A company which announces its bonus issue after the approval of the Board of directors must implement the proposal within a period of 15 days from the date of such approval (if Shareholders' approval is not required) or 2 months (if Shareholders' approval is required).
9. Once the decision to make a bonus issue is announced, the same cannot be withdrawn.

CONVERSION OF PARTLY PAID-UP SHARE TO FULLY PAID-UP SHARES

- A company may utilize its reserves to convert its partly paid shares into fully paid without asking the shareholders to contribute further against the call money due. This may be termed as bonus dividend.
- Unlike issue of fully paid bonus shares, the sources for bonus dividend shall be, however, free reserves only as Section 52 of Companies Act, 2013 allows utilization of 'Securities Premium' for issuing fully paid bonus shares only.

- Similarly, Section 55(4) of the Act prohibits the use of ‘Capital Redemption Reserve’ for purposes other than issue of fully paid-up bonus shares.

Note: Capital Reserve realized in cash can be a source of bonus dividend as well as issue of fully paid-up bonus shares.

ACCOUNTING TREATMENT:

1.Upon the sanction of an issue of bonus shares Capital Redemption Reserve Account Dr. Securities Premium Account Dr. General Reserve Account Dr. Profit & Loss Account Dr. To Bonus to Shareholders Account.	**1.Upon the sanction of bonus by converting partly paid shares into fully paid shares** General Reserve Account Dr. Profit & Loss Account Dr. To Bonus to Shareholders Account
2.Upon issue of bonus shares Bonus to Shareholders Account Dr. To Share Capital Account.	**2.On making the final call due** Share Final Call Account Dr. To Share Capital Account.
	3. On adjustment of final call Bonus to Shareholders Account Dr. To Share Final Call Account

Rights Issue of Shares

The term ‘rights issue’ has not been defined in the Companies Act, 2013. As per Regulation 2(1) (zg) of SEBI (Issue of Capital and Disclosure Requirements), 2009, “rights issue” means an offer of specified securities by a listed issuer to the shareholders of the issuer as on the record date fixed for the said purpose. The provisions relating to issue of rights shares are, however, covered in Section 62(1)(a) of the Companies Act, 2013.

Accordingly, where at any time, a company having a share capital proposes to increase its subscribed capital by the issue of further shares, such shares shall be offered to persons who, at the date of the offer, are holders of equity shares of the company in proportion, as nearly as circumstances admit, to the paid-up share capital on those shares by sending a letter of offer.

Such issue of shares shall be done subject to the following conditions:

a) the offer shall be made by notice specifying the number of shares offered.

b) The time limit shall be not less than 15 days and shall be not exceeding thirty days from the date of the offer within which the offer.

c) unless the articles of the company otherwise provide, the offer aforesaid shall be deemed to include a right exercisable by the person concerned to renounce the shares offered to him or any of them in favour of any other person.

d) after the expiry of the time specified in the notice aforesaid, or on receipt of earlier intimation from the person to whom such notice is given that he declines to accept the shares offered, the Board of Directors may dispose of them in such manner which is not dis-advantageous to the shareholders and the company.

ACCOUNTING FOR RIGHT ISSUE:

1. The accounting treatment of rights share is the same as that of issue of ordinary shares and the following journal entry will be made:

   Bank A/c Dr.

   To Equity shares capital A/c

2. In case rights shares are being offered at a premium, the premium amount is credited to the securities premium account. The accounting entry is

   Bank A/c Dr.

   To Equity Share Capital A/c

   To Securities Premium A/c

VALUE OF RIGHT:

Usually, a company offers rights issue at a price which is lower than the market price of the shares so that existing (i.e., old) shareholders may get the monetary benefit of being associated with the company for a long time. Existing shareholders who have been offered right shares and do not want to purchase these offered shares may renounce their right shares in favour of some other persons within the specified period as mentioned earlier. In such a case, the existing shareholders can make a profit by selling his right to such other person. This right can be valued in terms of money as below:

(a) Calculate the market value of shares which an existing shareholder is required to have in order to get fresh shares.

(b) Add to the above price paid for the fresh shares.

(c) Find out the average price of existing shares and fresh shares.

(d) The average price of the share should be deducted from the market price and the difference thus ascertained is value of right.

Value of right = Cum-right value of share Less Ex-right value of share

Ex-right value of the shares = [Cum-right value of the existing shares + (Rights shares X Issue Price)] Divided by (Existing Number of shares + Number of right shares)

EXCLUSIVE PROBLEMS FROM CMA SOURCE

BONUS ISSUE

PROBLEM 1:

Following items appear in the Trial Balance of M Ltd. as at 31st March, 2021:

Particulars	(Rs.)
60,000 Equity Shares of Rs. 10 each	6,00,000
Capital Redemption Reserve	45,000
Plant Revaluation Reserve	15,000
Securities Premium Account	52,500
General Reserve	1,50,000
Profit & Loss Account	75,000
Capital Reserve (including Rs. 37,500 being Profit on Sale of Machinery)	1,12,500

The company decided to issue bonus shares to its shareholders at the rate of one share for every four shares held.

Required: Pass the necessary journal entries. It is desired that there should be minimum reduction in free reserves. **(CMA SM illustration 24)**

PROBLEM 2:

Following is the extract of the Balance Sheet of YY Ltd. as at 31st March, 2021:

	Rs.
Authorised Capital	
15,000 12% Preference shares of Rs.10 each	1,50,000
1,50,000 Equity shares of Rs.10 each	15,00,000
	16,50,000
Issued and Subscribed Capital:	
12,000 12% Preference Shares of Rs.10 each fully paid	1,20,000
1,35,000 Equity shares of Rs. 10 each, Rs. 8 paid up	10,80,000
Reserves and Surplus:	
Capital Redemption Reserve	30,000
General Reserve	1,80,000
Capital Reserve	1,12,500

Securities Premium	37,500
Profit and Loss Account	2,70,000
Secured Loans:	
12% Partly Convertible Debentures @ Rs.100 each	7,50,000

On 1st April, 2021 the Company has made final call @ 2 each on 1,35,000 equity shares. The call money was received by 20th April, 2021. Thereafter the company decided to capitalise its reserves by way of bonus at the rate of one share for every four shares held. Securities premium of Rs.37,500 includes a premium of Rs.7,500 for shares issued to vendors pursuant to a scheme of amalgamation. Capital reserves include Rs.60,0000, being profit on sales of plant and machinery. 20% of 12% Debentures are convertible into equity shares of Rs.10 each fully paid on 1st June 2021.

Required: Show necessary entries in the books of the company and prepare the extract of the Balance Sheet immediately after bonus issue but before conversion of debentures. Are the convertible debenture holders entitled to bonus shares? **(CMA SM illustration 25)**

PROBLEM 3:

The following is the balance sheet of RR Company Ltd as on 31.12.2021

Liabilities:	**(Rs.)**
Issued and paid up capital:	
225000 equity shares of Rs.10 each fully called up	22,50,000
Less: Calls in arrear (25000 shares of Rs.2 each)	50,000
100000 equity shares of Rs.10 each, Rs.4 paid up	4,00,000
P/L A/c	12,50,000
Dividend Equalization Reserve	1,00,000
General Reserve	1,50,000
Development Rebate reserve	2,50,000
Capital reserve	1,50,000
Securities premium	2,50,000
Capital redemption reserve	4,00,000
Current liability	10,00,000
Total	6,15,0000
Assets:	**(Rs.)**
Non-current assets	

Fixed assets	30,00,000
Current assets	10,00,000
Cash at bank	21,50,000
Total	61,50,000

The board of directors of the company took the following decisions.

a. To forfeit the shares on which final call of Rs. 2 each is due.

b. To issue fully paid bonus shares @ 1 fully paid up share for every 2 fully paid shares held.

c. to pay bonus to the partly paid shares at an equivalent rate as in (b)above without collecting any amount from the related shareholders.

d. to reissue the forfeited shares @ Rs. 12 each fully paid up.

e. To pay dividend equivalent to 10% on share capital including bonus shares.

f. To issue right shares in the ratio of 1 fully paid up share for every four existing fully paid up shares held at Rs.15 per share.

g. To use minimum balance of profit and loss account.

Note:

1. All Capital Reserve are realised in cash.

2. One fifth of the development rebate reserve is free.

Pass necessary journal entries in the books of the company including cash transaction after the above decisions are implemented. **(CMA SM illustration 26)**

PROBLEM 4:

MG Limited was registered on 1st January 2021 with an authorised capital of Rs.3,00,000 divided into 30000 equity shares of Rs.10 each. During the next 12 months to 31st November 2021 following events occurred which related to the share capital of the company.

On 1st January 2021 the company offered for subscription of 10,000 equity shares at a price of rupees 19 each, to be paid as follows:

At the date of issue including premium	Rs.10
On allotment	Rs.4
On first and final call	Rs.5

On 30th June 2021 the company made right issue on 1 for 2 basis at Rs. 22.50 per share, payable in full on 10th July 2021.

Only 80% of the issue was subscribed for by the shareholders with a payment being made on the due date.

On 30th November 2021 Company decided to make a bonus issue of shares at par by utilising the entire balance of securities premium account.

Prepare the equity share capital account and the securities premium account of the company for the year ended 31st December 2021.

A shareholder who had subscribed initially for 140 shares had subsequently taken up 80% of the right issue and then received the bonus shares to which he was entitled.

Calculate the ultimate number of shares owned by him and the total price paid by him for those shares. **(CMA SM illustration 27)**

RIGHT ISSUE

PROBLEM 1:

A Company is planning to raise funds by making rights issue of equity shares to finance its expansion. The existing equity share capital of the company is Rs.50,00,000. The market value of its share is Rs.42. The company offers to its shareholders the right to buy 2 shares at Rs.11 each for every 5 shares held.

You are required to calculate:

i. Theoretical market price after rights issue;
ii. The value of rights; and
iii. Percentage increase in share capital. **(CMA SM illustration 22)**

PROBLEM 2:

NT Limited has an issued capital of 20000 equity shares of Rs.10 each fully called up.

The following decisions are taken by the company:

To forfeit 100 shares on which Rs.5 per share has been paid up and to be issue at Rs.15 per share as fully paid up.

To issue right shares in the ratio of 1 fully paid up shares for every 4 existing shares held, at Rs. 15 per share.

Assuming that the company has sufficient to general reserve, the above through journal entries.

(CMA SM illustration 23)

PROBLEMS PRACTICE FROM CA SOURCES

PROBLEM 1:

Alpha Company announced bonus issue to its shareholders in the ratio of 2:3 i.e. 2 shares for every 3shares held. Shareholder X has 6,000 shares before announcement of bonus issue. How much shares would he have after bonus issue? **(SM, EXAMPLE-1)**

PROBLEM 2:

Following items appear in the trial balance of Bharat Ltd. (a listed company) as on 31st March, 2011:

Particulars	Rs.
40,000 Equity Shares of Rs 10 each	4,00,000
Securities Premium (collected in cash)	30,000
Capital Redemption Reserve	55,000
General Reserve	1,05,000
Surplus; Profit and Loss Account (Cr. Balance)	50,000

The company decided to issue to equity shareholders bonus shares at the rate of 1 share for every 4 shares held and for this purpose, it decided that there should be the minimum reduction in free reserves. Pass necessary journal entries. **(SM, ILLUSTRATION 1)**

PROBLEM 3:

Pass Journal Entries in the following circumstances:

i) A Limited company with subscribed capital of Rs. 5,00,000 consisting of 50,000 Equity shares of Rs. 10 each; called up capital Rs. 7.50 per share. A bonus of Rs. 1,25,000 declared out of General Reserve to be applied in making the existing shares fully paid up.

ii) A Limited company having fully paid- up capital of Rs. 50,00,000 consisting of Equity shares of Rs. 10 each, had General Reserve of Rs. 9,00,000. It was resolved to capitalize Rs. 5,00,000 out of General Reserve by issuing 50,000 fully paid bonus shares of Rs. 10 each, each shareholder to get one such share for every ten shares held by him in the company. **(SM, ILLUSTRATION 2)**

PROBLEM 4:

Following is the extract of the Balance Sheet of Solid Ltd. as at 31st March, 2015:

Particulars	Rs.
Authorised capital	
10,000 12% Preference shares of Rs.10 each	1,00,000

1,00,000 Equity shares of Rs.10 each	10,00,000
	11,00,000
Issued and subscribed capital:	
8,000 12% Preference shares of Rs.10 each fully paid	80,000
90,000 Equity shares of Rs.10 each Rs.8 paid up	7,20,000
Reserves and Surplus:	
(a) General Reserve	1,60,000
(b) Revaluation reserve	35,000
(c) Securities Premium (collected in cash)	20,000
(d) Profit and Loss Account	2,05,000
Secured loan:	
12% Debentures @ Rs.100 each	5,00,000

On 1st April, 2015 the Company has made final call @ Rs. 2 each on 90,000 equity shares. The call money was received by 20th April, 2015. Thereafter the company decided to capitalise its reserves by way of bonus at the rate of one share for every four shares held. Show necessary entries in the books of the company and prepare the extract of the Balance Sheet immediately after bonus issue assuming that the company has passed necessary resolution at its general body meeting for increasing the authorised capital.

(ANS.: SHARE CAPITAL AFTER BONUS ISSUE: RS.12,05,000) (SM, ILLUSTRATION 3)

PROBLEM 5:

Following is the extract of the Balance Sheet of Preet Ltd. as at 31st March, 20X1

Authorised capital:	**Rs.**
15,000 12% Preference shares of Rs. 10 each	1,50,000
1,50,000 Equity shares of Rs. 10 each	15,00,000
	16,50,000
Issued and Subscribed capital:	
12,000 12% Preference shares of Rs. 10 each fully paid	1,20,000
1,35,000 Equity shares of Rs. 10 each, Rs. 8 paid up	10,80,000
Reserves and surplus:	
General Reserve	1,80,000
Capital Redemption Reserve	60,000

Securities premium (collected in cash)	37,500
Profit and Loss Account	3,00,000

On 1st April, 20X1, the Company has made final call @ Rs. 2 each on 1,35,000 equity shares. The call money was received by 20th April, 20X1. Thereafter, the company decided to capitalise its reserves by way of bonus at the rate of one share for every four shares held.

Show necessary journal entries in the books of the company and prepare the extract of the balance sheet as on 30th April, 20X1 after bonus issue. **(SM, ILLUSTRATION 4)**

PROBLEM 6:

Following is the extract of the Balance Sheet of Manoj Ltd. as at 31st March, 20X1

	Rs.
Authorised capital:	
30,000 12% Preference shares of Rs. 10 each	3,00,000
3,00,000 Equity shares of Rs. 10 each	30,00,000
	33,00,000
Issued and Subscribed capital:	
24,000 12% Preference shares of Rs. 10 each fully paid	2,40,000
2,70,000 Equity shares of Rs. 10 each, Rs. 8 paid up	21,60,000
Reserves and surplus:	
General Reserve	3,60,000
Capital Redemption Reserve	1,20,000
Securities premium (collected in cash)	75,000
Profit and Loss Account	6,00,000

On 1st April, 20X1, the Company has made final call @ Rs 2 each on 2,70,000 equity shares. The call money was received by 20th April, 20X1. Thereafter, the company decided to capitalise its reserves by way of bonus at the rate of one share for every four shares held. Show necessary journal entries inthe books of the company and prepare the extract of the balance sheet as on 30th April, 20X1 after bonus issue. **(SM, PRATICAL Q.NO.3)**

PROBLEM 7:

A company offers new shares of Rs. 100 each at 25% premium to existing shareholders on one for four bases. The cum-right market price of a share is Rs. 150. Calculate the value of a right. What should be the ex-right market price of a share? **(SM, ILLUSTRATION 5)**

PROBLEM 8:

(a) Beta Ltd. having share capital of 20,000 equity shares of Rs.10 each decides to issue rights share at the ratio of 1 for every 8 shares held at par value. Assuming all the shareholders accepted the rights issue and all money was duly received, pass journal entry in the books of the company.

(b) Omega Ltd. offers new shares of Rs. 100 each at 25% premium to existing shareholders on the basis one for five shares. The cum-right market price of a share is Rs. 200. You are required to calculate the (i) Ex-right value of a share; (ii) Value of a right share? **(RTP-MAY 2021-PROBLEM 6)**

PROBLEM 9:

Following notes pertain to the Balance Sheet of Mars Company Limited as at 31st March 20X1:

	Rs.
Authorised capital:	
50,000 12% Preference shares of Rs. 10 each	5,00,000
5,00,000 Equity shares of Rs. 10 each	50,00,000
	55,00,000
Issued and Subscribed capital:	
50,000 12% Preference shares of Rs. 10 each fully paid	5,00,000
4,00,000 Equity shares of Rs. 10 each, Rs. 8 paid up	32,00,000
Reserves and surplus:	
General Reserve	1,60,000
Capital Redemption Reserve	2,40,000
Securities premium (collected in cash)	2,75,000
Revaluation Reserve	1,00,000
Profit and Loss Account	16,00,000

On 1st April, 20X1, the Company has made final call @ RRs. 2 each on 4,00,000 equity shares. The call money was received by 25th April, 20X1. Thereafter, on 1st May 20X1 the company decided to capitalise its reserves by way of bonus at the rate of one share for every four shares held, it decided that there should be minimum reduction in free reserves.

On 1st June 20X1, the Company issued Rights shares at the rate of two shares for every five shares held on that date at issue price of Rs. 12 per share. All the rights shares were accepted by the existing shareholders and the money was duly received by 20th June 20X1.

Show necessary journal entries in the books of the company for bonus issue and rights issue.

(SM, PRACTICE PROBLEM-6)

4. BUYBACK OF SECURITIES

BUY- BACK OF SHARES:

1. Buy-back of shares means purchase of its own shares by a company.
2. When shares are bought back by a company, they should be cancelled by the company. Thus, A company cannot buy its own shares for the purpose of investment.

ADVANTAGES OF BUY-BACK OF SHARES:

1. to increase earnings per share if there is no dilution in company's earnings as the buy-back of shares reduces the outstanding number of shares.
2. to increase promoters holding as the shares which are bought back are cancelled.
3. to discourage others to make hostile bid to take over the company as the buy-back will increase the promoters holding.
4. to support the share price on the stock exchanges when the share price, in the opinion of company management, is less than its worth, especially in the depressed market.
5. to pay surplus cash to shareholders when the company does not need it for business.

PROVISIONS OF COMPANIES ACT 2013 RELATING TO BUY-BACK:

1. The Companies Act, 2013 under Section 68 (1) permits companies to buy-back their own shares and other specified securities out of:

   (i) its free reserves; or

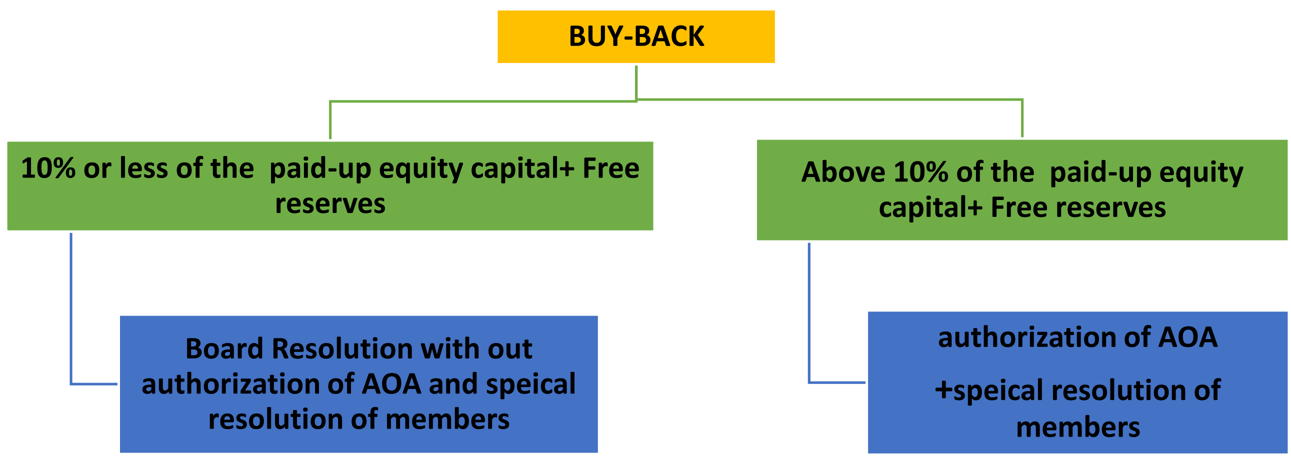
   (ii) the securities premium account; or

   (iii) the proceeds of the issue of any shares or other specified securities.

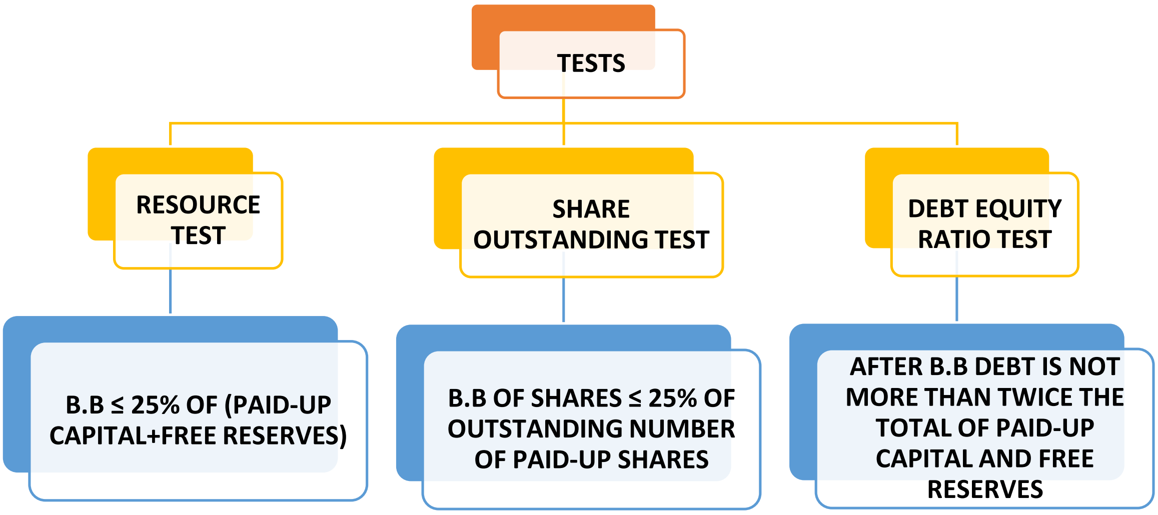
   Note: No buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other specified securities. For example, if equity shares are to be bought-back, then, preference shares may be used for the purpose.

2. **Section 68(2)**

   A.



B. <u>Maximum number of shares bought back will be lower of the results of below tests</u>



3. All the shares or other specified securities for buy-back are fully paid-up;

4. No offer of the buy-back under this sub section shall be made within a period of one year reckoned from the date of closure of a previous offer of buy-back if any. This means that there cannot be more than one buyback in one year.

5. Every buy-back shall be completed within twelve months from the date of passing the special resolution, or the resolution passed by the board of directors.

6. The buy-back may be—

(a) from the existing security holders on a proportionate basis; or

(b) from the open market; or

(c) by purchasing the securities issued to employees of the company pursuant to a scheme of stock option or sweat equity.

7. If company has passed a special resolution, before making such buy-back, file with the Registrar and the Securities and Exchange Board of India a declaration of solvency in the form as may be prescribed and verified by an affidavit to the effect that the Board of Directors has made a full inquiry into the affairs of the company as a result of which they have formed an opinion that it is capable of meeting its liabilities and will not be rendered insolvent within a period of one year of the date of declaration adopted by the Board of Directors.

8. Where a company completes a buy-back of its shares or other specified securities under this section, it shall not make further issue of same kind of shares within a period of six months except by way of bonus issue or in the discharge of subsisting obligations such as conversion of warrants, stock option scheme, sweat equity or conversion of preference shares or debentures into equity shares.

9. A company shall, after the completion of the buy-back under this section, file with the Registrar and the Securities and Exchange Board of India, a return containing such particulars relating to the buy-back within thirty days of such completion.
10. Section 69 (1) states that where a company purchases its own shares out of the free reserves or securities premium account, a sum equal to the nominal value of shares so purchased shall be transferred to the Capital Redemption Reserve Account and details of such account shall be disclosed in the Balance Sheet.
11. The Capital Redemption Reserve Account may be applied by the company in paying up unissued shares of the company to be issued to members of the company as fully paid bonus shares.
12. Premium (excess of buy-back price over the par value) paid on buy-back should be adjusted against free reserves and/or securities premium account.

EXPLANATION:

For the purposes of Section 68

1. "specified securities" includes employees' stock option or other securities as may be notified by the Central Government from time to time
2. "free reserves" includes securities premium account.

JOURNAL ENTRIES:

PARTICULARS		DEBIT	CREDIT
Bank a/c	Dr.		
To Investments a/c			
To P&l a/c			
Equity share capital A/c	Dr.		
Premium payable on buy-back A/c	Dr.		
To Equity shares buy-back A/c			
Equity shares buy-back A/c	Dr.		
To Bank A/c			
Securities premium/p&l A/c	Dr.		
To Premium payable on buy-back A/c			
Revenue reserve A/c	Dr.		
To Capital Redemption Reserve A/c			

NOTE: Above entries passed on the assumption that Buyback made by using existing resources. If buy back made from fresh issue of specified securities changes should be made accordingly.

Amount transferred to CRR and maximum equity to be bought back:

As per section 68 of the Companies Act, 2013, amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Equation 1:

Maximum permissible buy-back of equity= (Present equity sh's fund – Nominal value of buy-back transfer to CRR) – Minimum equity sh's fund to be maintained

Here Eq. sh's fund means Eq. share capital and free reserves & securities premium only.

Equation 2:

Nominal value of the shares bought –back to be transferred to CRR =

$$\frac{\textbf{Maximum buy-back X Face value}}{\textbf{Buy back price}}$$

EXCLUSIVE PROBLEMS FROM CMA SOURCE

Problem No.1:

X Co. Ltd. buys back its own 2,00,000 equity shares of Rs. 10 each at par. The company has sufficient profits otherwise available for dividend besides general reserve. No fresh issue of shares is made for this purpose. The shares are fully paid up. Journalise the transactions. **(Illustration 33)**

Problem No.2:

The BCG Co. Ltd. resolved by a special resolution to buy-back 2,00,000 of its equity shares of the face value of Rs.10 each on which Rs.8 has been paid up. The general reserve balance of the company stood at Rs.50,00,000 and no fresh issue of shares was made. Journalize the transactions.

(Illustration 34)

Problem No.3:

The share capital of Beta Co. Ltd consists of 1,00,000 equity shares of Rs.10 each, and 25,000 preference shares of Rs.100 each, fully called up. Its securities premium account shows a balance of Rs.40,000 and general reserve of Rs.7,00,000. The company decides to buy-back 20,000 equity shares of Rs.12 each. Pass the necessary journal entries **(Illustration 35)**

Problem No.4:

The PTC Co. Ltd. has a share capital of Rs.15,00,000, comprising 1,00,000 equity shares of Rs.10 each and 50,000 8% preference shares of Rs.10 each, both of which fully called up and paid up. The company has sufficient general reserve to its credit to enable it to comply with the legal formalities connected with buy-back of shares. It decides to buy-back 20% of its equity share capital at Rs.9 per share. Record the transactions in the books of the company. **(Illustration 36)**

Problem No.5:

Alpha Co. Ltd. has a paid-up equity share capital of Rs.20,00,000 in 2,00,000 shares of Rs.10 each. It resolved to buy-back 50,000 equity shares at Rs.15 per share. For this purpose. it issued 20,000 12% preference shares of Rs.10 each, at par, payable along with application. The company has to its credit Rs.2,50,000 in securities premium account and Rs.10,00,000 in the general reserve account. The company utilized the general reserve. Pass the necessary journal entries. **(Illustration 37)**

Problem No.6:

The following was the balance sheet of Diamond Ltd. as at 31st March, 2021.

Liabilities	Rs. in lakhs
10% Redeemable Preference Shares of Rs.10 each, fully paid up	2,500
Equity Shares of Rs.10 each fully paid up	8,000

Capital Redemption Reserve	1,000
Securities Premium	800
General Reserve	6,000
Profit and Loss Account	300
9% Debentures	5,000
Sundry creditors	2,300
Sundry Provisions	1,000
	26,900
Assets	
Fixed assets	14,000
Investments	3,000
Cash at Bank	1,650
Other Current assets	8,250
	26,900

On 1st April, 2021 the company redeemed all of its preference shares at a premium of 10% and bought back 25% of its equity shares @ Rs.15 per share. In order to make cash available, the company sold all the investments for Rs. 3,150 lakh and raised a bank loan amounting to Rs.2,000 lakhs on the security of the company's plant.

Pass journal entries for all the above mentioned transactions including cash transactions and prepare the company's balance sheet immediately thereafter. **(Illustration 38)**

PROBLEMS FROM CA SOURCE FOR PRACTICE

PROBLEM 1:

M Ltd. furnishes the following summarized Balance Sheet as at 31st March, 2013:

Particulars	Rs.'000	Rs.'000
EQUITY & LIABILITIES:		
Share Capital:		
Authorized Capital:		5,000
Issued and Subscribed Capital:		
3,00,000 Equity shares of Rs.10 each fully paid up	3,000	
20,000 9% Preference Shares of 100 each	2,000	
		5,000
Reserve and Surplus:		
Capital reserve	10	
Revenue reserve	4,000	
Securities premium	500	
Profit and Loss account	1,800	6,310
Non-current liabilities - 10% Debentures		400
Current liabilities and provisions		40
		11,750
ASSETS:		
Fixed Assets: Cost	3,000	
Less: Provision for depreciation	250	2,750
Non-current investments at cost		5,000
Current assets, loans and advances (including cash and bank balances)		4,000
		11,750

The company passed a resolution to Buy-back 20% of its equity capital @ Rs.15 per share. For this purpose, it sold its investments of Rs.30 lakhs for Rs.25 lakhs.

You are required to pass necessary Journal entries **(SM)**

PROBLEM 2:

Pratham Ltd. (a non-listed company) has the following Capital structure as on31st March, 20X1:

Particulars	Rs.	Rs.
Equity Share Capital (shares of Rs. 10 each fully paid		**30,00,000**
Reserves & Surplus		
General Reserve	32,50,000	
Security Premium Account	6,00,000	
Profit & Loss Account	4,30,000	
Revaluation Reserve	6,20,000	49,00,000
Loan Funds		42,00,000

You are required to compute by Debt Equity Ratio Test, the maximum number of shares that can be bought back in the light of above information, when the offer price for buy-back is Rs. 30 per share.

(**SM**)

PROBLEM 3:

Perrotte Ltd. (a non-listed company) has the following Capital Structure as on 31.03.20X1:

	Particulars		(Rs. in crores)
(1)	Equity Share Capital (Shares of Rs. 10 each fully paid)	---	330
(2)	Reserves and Surplus		
	General Reserve	240	
	Securities Premium Account	90	
	Profit & Loss Account	90	
	Infrastructure Development Reserve	180	600
(3)	Loan Funds		1,800

The Shareholders of Perrotte Ltd., on the recommendation of their Board of Directors, have approved on 12.09.20X1 a proposal to buy-back the maximum permissible number of Equity shares considering the large surplus funds available at the disposal of the company.

The prevailing market value of the company's shares is Rs. 25 per share and in order to induce the existing shareholders to offer their shares for buy-back, it was decided to offer a price of 20% over market.

You are also informed that the Infrastructure Development Reserve is created to satisfy Income-tax Act requirements.

You are required to compute the maximum number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either Rs. 1,200 crores or Rs. 1,500 crores.

Assuming that the entire buy-back is completed by 09.12.20X1, show the accounting entries in the company's books in each situation. (**SM**)

PROBLEM 4:

Anu Ltd. (a non-listed company) furnishes you with the following balance sheet as at 31st March, 20X1:

		Particulars	Notes	Rs. (in crores Rs.)
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	100
	B	Reserves and Surplus	2	300
2		**Current liabilities**		
	A	Trade Payables		40
		Total		**440**
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	3	-
	B	Non-Current Investments	4	100
2		**Current assets**		
	A	Trade receivables		140
	B	Cash and Cash equivalents		200
		Total		**440**

Notes to accounts

No.	Particulars		Rs.
1	**Share Capital** **Authorized, issued and subscribed share capital**:		
	12% Redeemable preference shares of Rs. 100 each, fully paid up		75
	Equity shares of Rs. 10 each, fully paid up		25

	Total		**<u>100</u>**
2	**Reserves and Surplus**		
	Capital reserve		15
	Securities premium		25
	Revenue reserves		<u>260</u>
	Total		**<u>300</u>**
3	**Property, Plant and Equipment**		
	PPE Cost		100
	Less: Provision for depreciation		<u>(100)</u>
	Net carrying value		**<u>NIL</u>**
4	**Non-Current Investments**		
	Non-current investments at cost (Market value Rs. 400 Cr.)		<u>100</u>

The company redeemed preference shares on 1st April, 20X1. It also bought back 50 lakhs equity shares of Rs. 10 each at Rs. 50 per share. The payments for the above were made out of the huge bank balances, which appeared as a part of current assets.

You are asked to:

(i) Pass journal entries to record the above.

(ii) Prepare balance sheet as at 1.4.20X1.

(SM)(ANS: balance sheet of Anu Ltd. as at 1.4.20X1. 340 crores)

<u>PROBLEM 5:</u>

Dee Limited (a non – listed company) furnishes the following balance sheet as at 31st March, 20X1:

(in thousand Rs.)

Particulars			Notes	Rs.
		Equity and liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	2,700
	B	Reserves and surplus	2	9,700
2		**Current liabilities**		
	A	Trade payables		1,400
		Total		**<u>13,800</u>**
		Assets		
1		**Non – current assets**		

	A	Property, plant and equipment		9,300
	B	Non – current investments		3,000
2		**Current assets**		
	A	Inventories		500
	B	Trade receivables		200
	C	Cash and cash equivalents		800
		Total		**13,800**

Notes to accounts

1	**Share capital**		
	Authorized, issued and subscribed capital:		
	2,50,000 equity shares of Rs.10 each fully paid up		2,500
	2,000, 10% preference shares of Rs.100 each (issued two months back for the purpose of buy – back)		200
	Total		2,700
2	**Reserves and surplus**		
	Capital reserve		1,000
	Revenue reserve		3,000
	Securities premium		2,200
	Profit and loss account		3,500
	Total		**9,700**

The company passed a resolution to buy – back 20% of its equity capital @ Rs.50 per share. For this purpose, it sold all of its investment for Rs.22,00,000

You are required to pass necessary journal entries and prepare the balance sheet.

(SM) (ANS: BALANCE SHEET OF DEE LTD. 1,05,00,000)

PROBLEM 6:

(in lakhs Rs.)

Particulars			**Notes**	**Rs.**
		Equity and liabilities		
1		**Shareholder's funds**		
	A	Share capital	1	120
	B	Reserve and surplus	2	118
2		**Non – current liabilities**		

		Long term barrowings	3	4
3		**Current liabilities**		
	A	Trade payables		<u>70</u>
		Total		<u>312</u>
		Assets		
1		**Non – current assets**		
	A	Property, plant and equipment		50
	B	Non – current investments		120
2		**Current assets**		
	A	Cash and cash equivalents		<u>142</u>
		Total		<u>312</u>

Notes to accounts

No.	Particulars		Rs.
1	**Share Capital**		
	Authorized, issued and subscribed capital:		
	Equity shares of Rs.10 each fully paid		100
	9% Redeemable preference shares of Rs.100 each fully paid		<u>20</u>
	Total		**<u>120</u>**
2	**Reserves and Surplus**		
	Capital reserves		8
	Revenue reserves		50
	Securities premium		<u>60</u>
	Total		<u>118</u>
3	**Long term borrowings**		
	10% Debentures		4

i) The company redeemed the preference shares at a premium of 10% on 1st April, 20X1.

ii) It also bought back 3 lakhs equity shares of Rs.10 each at Rs.30 per share. The payment for the above was made out of huge bank balances.

iii) Included in its investment were "investments in own debentures" costing Rs.2 lakhs (face value Rs. 2.20 lakhs). These debentures were cancelled on 1st April 20X1.

iv) The company had 1,00,000 equity stock options outstanding on the above- mentioned date, to the employees at Rs.20 when the market price was Rs.30 (This was included under current liabilities). On 1.04.20X1 employees exercised their options for 50,000 shares.

v) Pass the journal entries to record the above.

vi) Prepare Balance Sheet as at 01.04.20X1.

(SM) (ANS: BALANCE SHEET OF EXTRA LTD. RS. 2,08,00,000)

5. REDEMPTION OF PREFERENCE SHARES

1) **MEANING:**

Redeemable preference shares have a fixed term and hence are redeem at the end of such period. On redemption the shareholders are repaid the capital that they had invested in those shares. The redemption may occur either ‘at par’ or ‘at premium’. When the company repays an amount equal to the face value of the preference shares, it is called ‘redemption at par’. On the other hand, when a company repays more than the face value of the preference shares, it is known as ‘redemption at premium’.

2) **PROVISIONS REGARDING ISSUE AND REDEMPTION OF PREFERENCE SHARES**

Section 55 of the Act states that –

(1) No company limited by shares shall, issue any preference shares which are irredeemable.

(2) A company limited by shares may, if so, authorised by its articles, issue preference shares which are liable to be redeemed within a period not exceeding twenty years from the date of their issue subject to such conditions as may be prescribed.

Companies (Share Capital and Debentures) Rules, 2014 further states that company engaged in the setting up and dealing with of infrastructural projects may issue preference shares for a period exceeding twenty years but not exceeding thirty years, subject to the redemption of a minimum ten percent of such preference shares per year from the twenty first year onwards or earlier, on proportionate basis, at the option of the preference shareholders.

Important Points on Redemption of Preference Shares (Other than Deemed Redemption)

- Only fully paid-up preference shares can be redeemed. Partly paid-up preference shares must be converted into fully paid-up before they can be eligible for redemption.
- The repayment of capital portion can be done out of two sources –
  - (i) Profits of the company (which would otherwise be available for dividend payment)
  - (ii) Proceeds of fresh issue of shares.
- The premium on redemption, if any, shall be provided as follows:
  - (i) In case of the prescribed class of companies and whose financial statements comply with the accounting standards prescribed u/s 133 of the Companies Act, 2013 – - If the preference shares were issued on or before 01.04.2014 (date of commencement of the Companies Act, 2013), premium can be provided out of Securities Premium as well as out of Profits of the Company. If the preference shares were issued after 01.04.2014, premium can be provided only out of Profits of the Company.

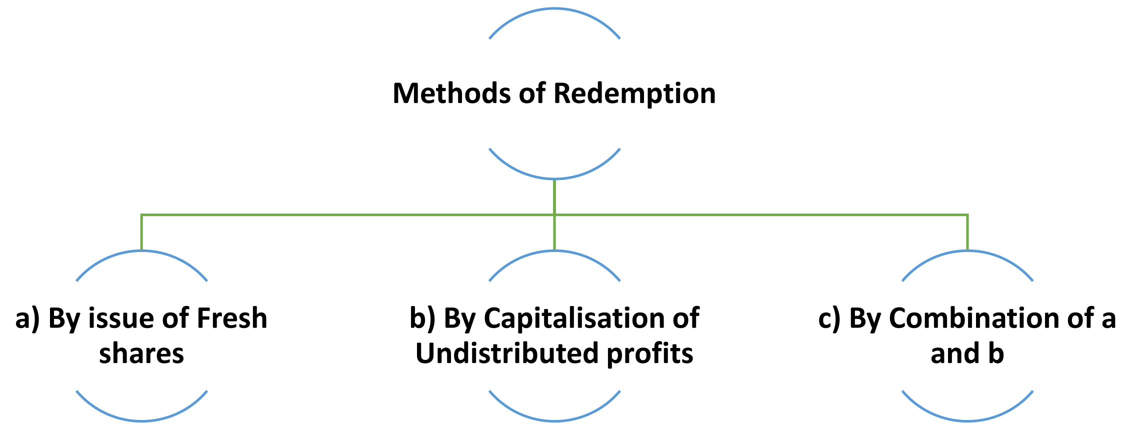
(ii) For other companies, there can be two sources of premium i.e., Securities Premium and Profits of the Company.

Note: For the purpose of payment of capital, the term 'Profits of the Company which would otherwise be available for dividend' shall mean 'free reserves. Hence, Securities Premium, Revaluation Reserve, Capital Reserve (unrealized) or any Statutory Reserve will not be eligible for this purpose. But free portion of Investment Allowance Reserve, Development Rebate Reserve, Workmen Compensation Fund will be allowed.

Note: For the purpose of payment of premium, the term 'Profits of the Company' (excluding the expression 'which would otherwise be available for dividend') means all profits of the company whether realized or not. Hence, Capital Reserve (whether released or not), all Statutory Reserve (free portion only), free portion of Investment Allowance Reserve, Development Rebate Reserve, Workmen Compensation Fund will be allowed.

- Companies may also issue fresh equity or preference shares for redemption of existing preference shares. In such a case –
  (i) If the shares are issued at par, proceeds from fresh issue = Nominal Value of shares;
  (ii) If the shares are issued at premium, proceeds from fresh issue = Nominal Value of shares (i.e., excluding premium on issue)
- A sum equal to the nominal amount of the shares to be redeemed out of profits should be transferred tom Capital Redemption Reserve (CRR). The balance of CRR so created shall only be utilized for issue of fully paid-up bonus shares.

METHODS OF REDEMPTION OF FULLY PAID-UP SHARES:



1) REDEMPTION OF PREFERENCE SHARES BY FRESH ISSUE OF SHARES:

a) One of the methods for redemption of preference shares is to use the proceeds of a fresh issue of shares. A company can issue new shares (equity shares or preference shares) and the proceeds from such new shares can be used for redemption of preference shares.

b) The proceeds from <u>issue of debentures cannot be utilised</u> for the purpose.

c) The proceeds of a <u>fresh issue of shares will not include the amount of securities premium</u> for the purpose of redemption of preference shares.

<u>JOURNAL ENTRIES:</u>

1) <u>When new shares are issued at par</u>

Bank Account Dr.

To Share Capital Account

(Being the issue of …….shares of Rs.……each for the purpose of redemption of preference shares, as per Board's Resolution No…… dated…….)

2) <u>When new shares are issued at a premium</u>

Bank Account Dr.

To Share Capital Account

To Securities Premium Account

(Being the issue of ……..shares of Rs.……each at a premium of Rs.……each for the purpose of redemption of preference shares as per Board's Resolution No….. dated……)

3) <u>When preference shares are redeemed at par</u>

Redeemable Preference Share Capital Account Dr.

To Preference Shareholders Account

4) <u>When preference shares are redeemed at a premium</u>

Redeemable Preference Share Capital Account Dr.

Premium on Redemption of Preference Shares Account Dr.

To Preference Shareholders Account

5) <u>When payment is made to preference shareholders</u>

Preference Shareholders Account Dr.

To Bank Account

6) <u>For adjustment of premium on redemption</u>

Profit and Loss Account Dr.

To Premium on Redemption of Preference Shares Account

REDEMPTION OF PREFERENCE SHARES BY CAPITALISATION OF UNDISTRIBUTED DIVISIBLE PROFITS:

Another method for redemption of preference shares, as per the Companies Act, is to use the distributable profits in place of issuing new shares. When shares are redeemed by utilising distributable profit, an amount equal to the face value of shares redeemed is transferred to Capital Redemption Reserve Account by debiting the distributable profit. In other words, some of the distributable profits are kept aside to ensure that it can never be distributed to shareholders as dividend.

JOURNAL ENTRIES:

1. For transferring nominal amount of shares redeemed to **Capital Redemption Reserve Account**.		
General Reserve Account Dr. Profit and Loss Account Dr. Or any other Divisible Profits Dr. To Capital Redemption Reserve Account (Being the amount transferred to Capital Redemption Reserve Account as per the requirement of the Act).		
2. When shares are redeemed at par		
Redeemable Preference Share Capital Account Dr. To Preference Shareholders Account (Being the amount payable on redemption of preference shares transferred to Preference Shareholders Account)		
3. When shares are redeemed at a premium		
Redeemable Preference Share Capital Account Dr. Premium on Redemptions of Preference Shares Account Dr. To Preference Shareholders Account (Being the amount payable on redemption transferred to Preference Shareholders Account)		
4. When payment is made to preference shareholders		
Preference Shareholders Account Dr. To Bank Account (Being the payment to preference shareholders as per terms)		
5. For adjustment of premium of redemption		
Divisible Profit Account Dr.		

To Premium on Redemption of Preference Shares Account (Being the premium on redemption adjusted against Profit and Loss Account)		

REDEMPTION OF PREFERENCE SHARES BY COMBINATION OF FRESH ISSUE AND CAPITALISATION OF UNDISTRIBUTED DIVISIBLE PROFITS:

A company can redeem the preference shares partly from the proceeds from new issue and partly out of profits.

Formula:

(i) Amount to be Transferred to Capital Redemption Reserve	
	Rs.
Face value of shares redeemed	xxx
Less: Proceeds from new issue	xxx
	xxx
(ii) Proceeds to be collected from New Issue	
	Rs.
Face value of shares redeemed	xxx
Less: Profits available for distribution as dividend	xxx
	xxx

MINIMUM FRESH ISSUE OF SHARES

Minimum Fresh Issue of Shares to comply the provisions of section 55	**Minimum Fresh Issue to Provide Funds for Redemption**
Minimum Number of Shares = Minimum proceeds to comply with Section 55/ Proceeds of one share.	Besides, ensuring compliance with Section 55, the fresh issue of shares is made to provide funds for making payment to preference shareholders.
Minimum proceeds to comply with Section 55 =Nominal value of preference shares to be redeemed – Maximum amount of reserve and surplus available for redemption.	Minimum number of shares = (Amount payable to preference shareholders–Funds available for redemption)/Issue price
Maximum amount of reserve and surplus available for redemption = Free reserves & surplus as per Balance sheet- Adjustment for premium on redemption payable out of	

profits- Amount retained in Free reserves as per BOD information.	
Proceeds of one share mean the par value of a share issued, if it is issued at par or premium. However, in case of issue of share at a discount, it refers to the discounted value.	
NOTE: Minimum number of shares calculated as above, needs to be adjusted for share fractions. Thus, minimum number of shares as per above includes a fraction, it must be approximated to the next higher figure to ensure that provisions of Section 55 are not violated. Secondly, if the examination problem states that the proceeds/number of shares should be a multiple of say, 10 or 50 or 100, then again the next higher multiple should be considered.	

EXCLUSIVE PROBLEMS FROM CMA SOURCE

Problem No.1

T Ltd. furnishes you with the following Balance Sheet as at 31st March, 2021 : (Rs. in Lakhs)

Equity shares of Rs. 10 each fully paid	400	
12% redeemable preference shares of Rs. 100 each fully paid	200	
Reserves and surplus:		
- Capital reserve	15	
- Share Premium	25	
- Revenue reserves	260	300
Funds Employed in :		900
Fixed assets less depreciation		560
Current assets	540	
Less : Current liabilities	200	340
		900

The company redeemed preference shares on 1st April 2021 at a premium of 10%. You are required to pass journal entries to record the above. **(Illustration 40)**

Problem No.2:

Find out in each case what amount shall be transferred to capital redemption reserve account:

Redeemable preference shares redeemed	**Fresh issue of share capital**
a. Rs. 10,00,000 at par	Rs. 10,00,000 at par
b. Rs. 10,00,000 at 5% premium	Rs. 800,000 at par
c. Rs. 10,00,000 at par	Rs. 800,000 at 10% premium
d. Rs. 10,00,000 at 5% premium	Rs. 800,000 at 10% premium

(Illustration 41)

Problem No.3:

The Balance Sheet of Pixel Ltd. as on 31.12.2021 is given below:

Liabilities	Rs. in Lakh	Assets	Rs. in Lakh
Share Capital:		Fixed Assets	140
10,00,000 Equity shares of Rs.10 each	100	Investments	40

1,00,000 Redeemable Pref. shares of Rs.100 each	100	Stock	46
Less: Call-in-arrears on 20,000 shares	(4)	Debtors	30
Security premium account	15	Bank	30
Reserve	30		
Profit and Loss account	15		
Creditors	30		
	286		286

On 1st Jan 2022, fixed assets costing Rs.40 Lakh were sold for Rs.32 Lakh. It was decided that on 1st Feb 2022, company issued sufficient number of equity shares at par so as to finance redemption and to leaving a balance of Rs.10 Lakh in the reserve. All the payments were made except to a holder of 10,000 shares who could not be traced. The company also made bonus issue to the existing equity shareholders in the ratio of 1: 10 as on 31.12.2021. You are required to pass the necessary journal entries. **(Illustration 42)**

Problem No.4:

The balance sheet of G Ltd as on 31.12.2018

Liabilities:	**(Rs.)**
Equity shares of Rs.10 each	2,00,000
Less: Calls in arrear @ Rs. 2	10,000
14% Preference Shares of Rs.100	1,00,000
Securities Premium	10,000
Investment Allowance Reserve	40,000
Development Rebate Reserve	20,000
Workmen Compensation Fund	10,000
Dividend Equalization Reserve	12,000
Profit and Loss Account	38,000
Unsecured Loans	80,000
	5,00,000
Assets	
Non-Current Assets	4,00,000
Current Assets(including Bank balance Rs. 10,000)	1,00,000
	5,00,000

The board of directors decided to redeem the preference shares on 1st January 2019 on the following conditions.

1. Issue 4000 equity shares and Rs.50,000 10% debentures. Redeem preference shares at a premium of 10%.
2. Raise necessary bank loan to provide funds for redemption and to have Rs.15,000 as balance.
3. Admit claim of Rs.40,00 for workmen compensation.
4. Utilise Rs.10,000 out of development rebate reserve for the purpose.

Necessary journal entries assuming that holders of 100 reference shares could not be traced by the company. **(Illustration 43)**

Problem No.5:

Books of M Limited show the following balances on 31st December 2020	**Rs.**
15000 present equity shares of Rs.10 each fully paid	1,50,000
2500 10% preference shares of Rs.100 each fully paid	2,50,000
500 8% redeemable preference shares pop ups Rs.108, what is Rs.70 paid up	Rs.35,000
General Reserve	75,000
Profit and Loss Account	1,60,000
Securities Premium	15,000
Investment	1,20,000
Cash at Bank	39,600

On 1st January 2021 the board of directors decided to redeem the preference shares at a premium of 8%. In order to pay of preference shareholders the company also decided to sell the Investments and use companies fund and to raise the balance by issue of sufficient number of equity shares of Rs.10 each at a premium of rupee 1 per share subject to leaving a minimum bank balance of Rs.9,000 after search Redemption.

Investments web sold at Rs.1,08,000

Show the necessary journal entries (without narration) to record the transactions. **(Illustration 44)**

PROBLEMS BASED ON REDEMPTION OF PREFERENCE SHARES THROUGH FRESH ISSUE

PROBLEM 1:

Hinduja Company Ltd. had 5,000, 8% Redeemable Preference Shares of Rs. 100 each, fully paid up. The company decided to redeem these preference shares at par by the issue of sufficient number of equity shares of Rs. 10 each fully paid up at par. You are required to pass necessary Journal Entries including cash transactions in the books of the company. (**SM, ILLUSTRATION 1**)

PROBLEM 2:

C Ltd. had 10,000, 10% Redeemable Preference Shares of Rs. 100 each, fully paid up. The company decided to redeem these preference shares at par, by issue of sufficient number of equity shares of Rs. 10 each at a premium of Rs. 2 per share as fully paid up. You are required to pass necessary Journal Entries including cash transactions in the books of the company. **(SM, ILLUSTRATION 2)**

PROBLEMS BASED ON REDEMPTION OF PREFERENCE SHARES BY CAPITALISATION OF UNDISTRIBUTED DIVISIBLE PROFITS

PROBLEM 3:

The following are the extracts from the Balance Sheet of ABC Ltd. as on 31st December, 20X1.

Share capital: 40,000 Equity shares of Rs. 10 each fully paid – Rs. 4,00,000; 1,000 10% Redeemable preference shares of Rs. 100 each fully paid – Rs. 1,00,000.

Reserve & Surplus: Capital reserve – Rs. 50,000; Securities premium – Rs. 50,000; General reserve – Rs. 75,000; Profit and Loss Account – Rs. 35,000

On 1st January 20X2, the Board of Directors decided to redeem the preference shares at par by utilisation of reserve.

You are required to pass necessary Journal Entries including cash transactions in the books of the company. (**SM, ILLUSTRATION 6**)

PROBLEMS BASED ON REDEMPTION OF PREFERENCE SHARES BY COMBINATION OF FRESH ISSUE AND CAPITALISATION OF UNDISTRIBUTED DIVISIBLE PROFITS

PROBLEM 4:

C Limited had 3,000, 12% Redeemable Preference Shares of Rs.100 each, fully paid up. The company had to redeem these shares at a premium of 10%.

It was decided by the company to issue the following:

25,000 Equity Shares of Rs.10 each at par,

1,000 14% Debentures of Rs.100 each.

The issue was fully subscribed and all amounts were received in full. The payment was duly made. The company had sufficient profits. Show Journal Entries in the books of the company.

(**SM, ILLUSTRATION 7**)

PROBLEM 5:

The capital structure of a company consists of 20,000 Equity Shares of Rs. 10 each fully paid up and 1,000 8% Redeemable Preference Shares of Rs. 100 each fully paid up (issued on 1.4.20X1).

Undistributed reserve and surplus stood as: General Reserve Rs. 80,000; Profit and Loss Account Rs. 20,000; Investment Allowance Reserve out of which Rs. 5,000, (not free for distribution as dividend) Rs. 10,000; Securities Premium Rs. 2,000, Cash at bank amounted to Rs. 98,000. Preference shares are to be redeemed at a Premium of 10% and for the purpose of redemption, the directors are empowered to make fresh issue of Equity Shares at par after utilising the undistributed reserve and surplus, subject to the conditions that a sum of Rs. 20,000 shall be retained in general reserve and which should not be utilised.

Pass Journal Entries to give effect to the above arrangements and also show how the relevant items will appear in the Balance Sheet of the company after the redemption carried out.

(**SM, ILLUSTRATION 8**)

PROBLEMS BASED ON REDEMPTION OF PARTLY CALLED-UP PREFERENCE SHARES

PROBLEM 6:

The Balance Sheet of XYZ Ltd. as at 31st December, 20X1 inter alia includes the following information:

PARTICULARS	AMOUNT
50,000, 8% Preference Shares of Rs.100 each, Rs.70 paid up	35,00,000
1,00,000 Equity Shares of Rs.100 each fully paid up	1,00,00,000
Securities Premium	5,00,000
Capital Redemption Reserve	20,00,000

General Reserve	50,00,000
Bank	15,00,000

Under the terms of their issue, the preference shares are redeemable on 31st March, 20X2 at 5% premium. In order to finance the redemption, the company makes a rights issue of 50,000 equity shares of Rs. 100 each at Rs. 110 per share, Rs. 20 being payable on application, Rs. 35 (including premium) on allotment and the balance on 1st January, 20X3. The issue was fully subscribed and allotment made on 1st March, 20X2. The money due on allotment were duly received by 31st March, 20X2. The preference shares were redeemed after fulfilling the necessary conditions of Section 55 of the Companies Act, 2013.

You are asked to pass the necessary Journal Entries and show the relevant extracts from the balance sheet as on 31st March, 20X2 with the corresponding figures as on 31st December, 20X1.

(**SM, ILLUSTRATION 9**)

PROBLEM 7:

With the help of the details in above problem and further assuming that the Preference Shareholders holding 2,000 shares fail to make the payment for the Final Call made under Section 55, you are asked to pass the necessary Journal Entries and show the relevant extracts from the balance sheet as on 31st March, 20X2 with the corresponding figures as on 31st December, 20X1 assuming that the shares in default are forfeited after giving proper notices. (**SM, ILLUSTRATION 10**)

PROBLEM 8:

The Board of Directors of a Company decided to issue minimum number of equity shares of Rs. 9 to redeem Rs. 5,00,000 preference shares. The maximum amount of divisible profits available for redemption is Rs. 3,00,000. Calculate the number of shares to be issued by the company to ensure that the provisions of Section 55 are not violated. Also determine the number of shares if the company decides to issue shares in multiples of Rs. 50 only. (**SM, ILLUSTRATION 4**)

PROBLEM 9:

X Ltd. gives you the following information as at 31st March, 20X3:

	Particulars	**Rs.**
	EQUITY AND LIABILITIES	
1.	**Shareholders' funds**	
	a Share capital	2,90,000
	b Reserves and Surplus	48,000
2.	**Current liabilities**	

	Trade Payables	56,500
	ASSETS	
1.	**Property, Plant and Equipment**	3,45,000
2.	**Non-current investments**	18,500
3.	**Current Assets**	
	Cash and cash equivalents (bank)	31,000

The share capital of the company consists of Rs.50 each equity shares of Rs.2,25,000 and Rs.100 each Preference shares of Rs.65,000(issued on 1.4.20X1). Reserves and Surplus comprises Profit and Loss Account only.

In order to facilitate the redemption of preference shares at a premium of 10%, the Company decided:

(a) to sell all the investments for Rs. 15,000.

(b) to finance part of redemption from company funds, subject to, leaving a bank balance of Rs. 12,000.

(c) to issue minimum equity share of Rs. 50 each share to raise the balance of funds required.

You are required to pass:

The necessary Journal Entries to record the above transactions and prepare the balance sheet as on completion of the above transactions. **(SM, ILLUSTRATION.5)**

PROBLEM 10:

Trinity Ltd. gives you the following information as at 31.3.20X1:

	Rs.
Property, Plant and Equipment:	
Gross Block	3,00,000
Less: Depreciation	1,00,000
	2,00,000
Investments	1,00,000
Inventory	45,000
Trade receivables	25,000
Cash and Bank Balances	50,000
Share Capital:	
Authorised :	
10,000 10% Redeemable Preference Shares of Rs. 10 each	1,00,000
90,000 Equity Shares of Rs.10 each	9,00,000

Issued, Subscribed and Paid-up Capital:	
10,000 10% Redeemable Preference Shares of Rs. 10 each	1,00,000
10,000 Equity Shares of Rs. 10 each	1,00,000
Reserves and Surplus:	
General Reserve	1,20,000
Securities Premium	70,000
Profit and Loss A/c	18,500
Current Liabilities and Provisions	11,500

For the year ended 31.3.20X2, the company made a net profit of Rs.35,000 after providing Rs.20,000 depreciation.

The following additional information is available with regard to company's operation:

1. The preference dividend for the year ended 31.3.20X2 was paid.
2. Except cash and bank balances, other current assets and current liabilities as on 31.3.20X2, was the same as on 31.3.20X1.
3. The company redeemed the preference shares at a premium of 10%.
4. The company issued bonus shares in the ratio of one share for every equity share held as on 31.3.20X2.
5. To meet the cash requirements of redemption, the company sold investments.
6. Investments were sold at 90% of cost on 31.3.20X2.

You are required to prepare necessary journal entries to record redemption and issue of bonus shares.

(SM, PRATICAL PROBLEM NO.3)

6. ISSUE & REDEMPTION OF DEBENTURES

Introduction:

Share capital is the primary source of finance for every company. However, companies are often found to raise debt capital for additional financing requirement. A company raises the debt capital either through institutional financing i.e., loans from banks and other financial institutions or may issue structured debt instruments (such as debentures and bonds). Debentures happens to be the most popular debt instruments issued by a company to raise borrowed capital.

Meaning:

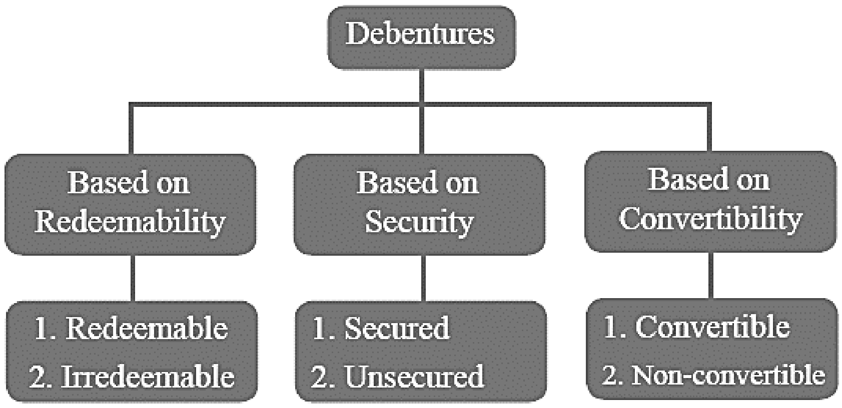
As per Section 2(30) of the Companies Act, 2013, "debenture" includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not.

Following are the features of debentures as a debt instrument.

a) Debenture is a financial instrument used to raise debt capital.
b) It is written document issued under the seal of the company.
c) It normally carries a rate of interest payable at regular interval. Such rate is termed as coupon rate.
d) Debenture may be redeemable or irredeemable.

Types of Debentures

The various types of debentures are shown in the following diagram.



Types of Debentures

a. Redeemable vs. Irredeemable Debentures

Redeemable Debentures are debentures that are repayable by a company at the end of the pre-specified time period. Irredeemable debentures are not repayable during the life-time of the company.

b. Secured vs. Unsecured Debentures

Secured Debentures are those debentures which create a charge on the assets of the company. These are also called Mortgage Debentures. Unsecured debentures are issued without the support of a collateral security. These are also called Naked Debentures.

c. **Convertible vs. Non-convertible Debentures**

Debentures which are convertible into other securities viz. equity shares, preference shares or new debentures after a specified period are referred to as Convertible Debentures. They may fully convertible or partly convertible. On the other hand, Debentures which are not convertible into any other security are referred to as Non-convertible Debentures.

Note: In all the above cases, the debentures may be issued at par or at premium or at discount to the issue price.

<u>Provisions Relating to Issue and Redemption of Debentures</u>

The provisions relating to issue and redemption of debentures are covered by Section 71 of the Companies Act, 2013 and Rule 18 of the Companies (Share Capital and Debentures) Rules, 2014.

Section 71 of the Companies Act, 2013 states that -

1. A company may issue debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption:
   Provided that the issue of debentures with an option to convert such debentures into shares, wholly or partly, shall be approved by a special resolution passed at a general meeting.
2. No company shall issue any debentures carrying any voting rights.
3. Secured debentures may be issued by a company subject to such terms and conditions as may be prescribed.
4. Where debentures are issued by a company under this section, the company shall create a debenture redemption reserve account out of the profits of the company available for payment of dividend and the amount credited to such account shall not be utilised by the company except for the redemption of debentures.
5. No company shall issue a prospectus or make an offer or invitation to the public or to its members exceeding five hundred for the subscription of its debentures, unless the company has, before such issue or offer, appointed one or more debenture trustees and the conditions governing the appointment of such trustees shall be such as may be prescribed.
6. A debenture trustee shall take steps to protect the interests of the debenture-holders and redress their grievances in accordance with such rules as may be prescribed.
7. A company shall pay interest and redeem the debentures in accordance with the terms and conditions of their issue.

8. Where at any time the debenture trustee comes to a conclusion that the assets of the company are insufficient or are likely to become insufficient to discharge the principal amount as and when it becomes due, the debenture trustee may file a petition before the Tribunal and the Tribunal may, after hearing the company and any other person interested in the matter, by order, impose such restrictions on the incurring of any further liabilities by the company as the Tribunal may consider necessary in the interests of the debenture-holders.

DRR & DRRI Provisions under the Companies Act, 2013:

1) As per Rule 18 (7) of the Companies (Share Capital and Debentures) Amendment Rules, 2019, companies should comply below provisions with respect to Debenture redemption reserve and Debenture redemption reserve investment.

a)

S.No.	Debentures issued by	Adequacy of Debenture Redemption Reserve (DRR)
1	**All India Financial Institutions (AIFIs)** regulated by Reserve Bank of India **and Banking Companies for both public** as well as **privately placed debentures**	**No DRR** is required
2	**Other Financial Institutions (FIs)** within the meaning of clause (72) of section 2 of the Companies Act, 2013	**DRR** will be **as applicable to NBFCs** registered with RBI (**as per (3) below**)
3	**For listed companies** (other than AIFIs and Banking Companies as specified in Sr. No. 1 above):	
a)	All **listed NBFCs** (registered with RBI under section 45-IA of the RBI Act,) and **listed HFCs** (Housing Finance Companies registered with National Housing Bank) **for both public** as well as **privately placed debentures**	**No DRR** is required
b)	**Other listed companies for both public** as well as **privately placed debentures**	**No DRR** is required
4	**For unlisted companies** (other than AIFIs and Banking Companies as specified in Sr. No. 1 above	

a)	All **unlisted NBFCs** (registered with RBI under section 45-IA of the RBI (Amendment) Act, 1997) and **unlisted HFCs** (Housing Finance Companies registered with National Housing Bank) **for privately placed debentures**	**No DRR** is required
b)	**Other unlisted companies**	**DRR** shall be **10% of** the **value of** the **outstanding debentures** issued

<u>NOTE:</u> In case of partly convertible debentures, DRR shall be created in respect of non- convertible portion of debentures only.

b)

(i) All listed NBFCs

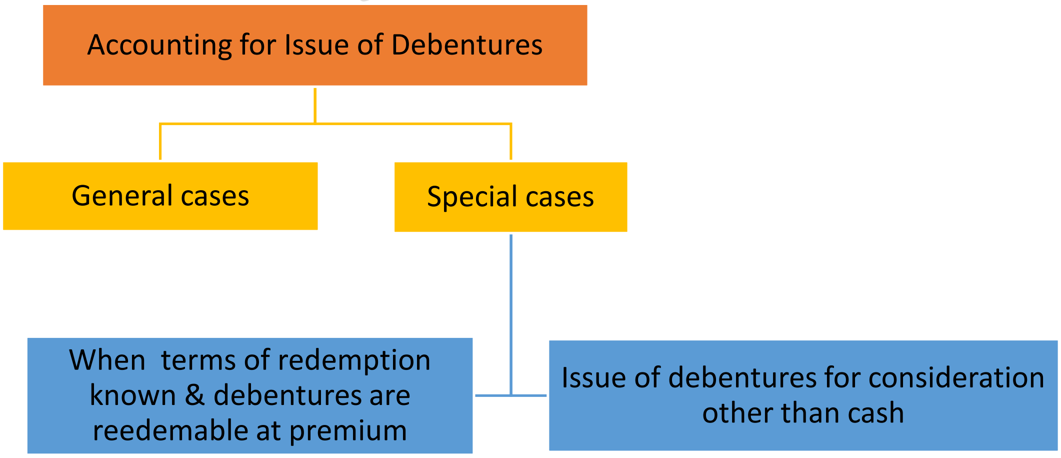
(ii) All listed HFCs

(iii) All other listed companies (other than AIFIs, Banking Companies and Other FIs); and

(iv) All unlisted companies which are not NBFCs and HFCs

<u>shall on or before the 30th day of April in each year</u>, in respect of debentures issued, deposit or invest, as the case may be, a <u>sum which should not be less than 15% of the amount of its debentures maturing during the year ending on the 31st day of March of that year.</u>

<u>JOURNAL ENTRIES:</u>



<u>Accounting for Issue of Debentures – General Cases</u>

Debentures can be issued at par or at premium or at discount. Moreover, the money can be collected in lumpsum or in instalments. The accounting entries for issue of debentures are as follows:

a. Debentures issued in lump sum.

(i) On receipt of application money

Bank A/c ……………………………….Dr.

To Debenture Application A/c

(ii) For excess debenture application money refunded

Debenture Application A/c ……………………. Dr.

To Bank A/c

(iii) On allotment of debentures

Debenture Application A/c ………………………Dr.

Discount on Issue of Debentures A/c …………….. Dr. (if issued at discount)

To Debentures A/c

To Securities Premium A/c (if issued at premium)

b. Debentures issued in instalments

(i) On receipt of application money

Bank A/c ……………………………….Dr.

To Debenture Application A/c

(ii) For excess debenture application money refunded

Debenture Application A/c ……………………. Dr.

To Bank A/c

(iii) For debenture application money transferred to share capital

Debenture Application A/c ………………………Dr.

To Share Capital A/c

(iv) For debenture allotment money due

Debenture Allotment A/c ………………………..Dr.

Discount on Issue of Debentures A/c …………….. Dr. (if issued at discount)

To Debenture Capital A/c

To Securities Premium A/c (if issued at premium)

(v) For debenture allotment money received

Bank A/c ……………………………….Dr.

To Debenture Allotment A/c

(vi) For debenture call money due

Debenture Call A/c …………………………. Dr.

To Share Capital A/c

(vii)For debenture call money received

Bank A/c ……………………………….Dr.

To Debenture Call A/c

Note: In case of issue of debentures at discount, the Discount will always be accounted in allotment. However, premium will be accounted with the instalment in which it is included. If nothing is mentioned specifically, it is accounted with allotment money.

Note: The premium on issue of debenture is included in Securities Premium A/c and the same is reflected under Reserve and Surplus in the Balance Sheet. The discount on issue of debentures is amortized over the life of the debentures on a proportionate basis. Accordingly, the amount amortized during the year is shown under Depreciation and Amortization in the Statement of Profit and Loss. The remaining amount is shown in the assets section of the Balance Sheet. The portion to be amortized over next 12 months is included in Other Current Assets while the portion that will not be amortized over next 12 months is shown in Other Non-current Assets.

- **Special Cases**

a) When terms of redemption are known and debentures are redeemable at premium

Situation	Combined entry on allotment
Issue at par, redemption at premium	Debenture Application A/c...... Dr. Loss on Issue of debentures A/c…. Dr. To Debentures A/c To Premium on Redemption of Debentures A/c
Issue at premium, redemption at premium	Debenture Application A/c...... Dr. Loss on Issue of debentures A/c…. Dr. To Debentures A/c To Securities Premium A/c To Premium on Redemption of Debentures A/c
Issue at discount, redemption at premium	Debenture Application A/c...................... Dr. Loss on Issue of Debentures A/c......... Dr. To Debentures A/c To Premium on Redemption of Debentures A/c Note: Here, Loss on Issue of Debentures A/c includes both discount on issue of debentures and premium on redemption of debentures

b) Issue of Debenture for Consideration other than Cash

a) On purchase of assets

Sundry Assets A/c …………………Dr.

To Vendor A/c

b) On issue of debentures

Vendor A/c …………………………Dr.

Discount on Issue of Debentures A/c ……….….. Dr. (if issued at discount)

To Debenture Capital A/c

To Securities Premium A/c (if issued at premium)

➢ **Accounting treatment for Debenture Redemption Fund & DRF investments: (Sinking Fund)**

a. After allotment of debentures

i) For setting aside the fixed amount of profit for redemption

Profit and Loss A/c Dr.

To Debenture Redemption Reserve A/c

ii) For investing the amount set aside for redemption

Debenture Redemption Reserve Investment A/c Dr.

To Bank A/c

iii) For receipt of interest on Debenture Redemption Reserve Investments

Bank A/c Dr.

To Interest on Debenture Redemption Reserve Investment A/c

iv) For transfer of interest on Debenture Redemption Reserve Investments (DRRI)

Interest on Debenture Redemption Reserve Investment A/c Dr.

To Profit and loss A/c*

* Considering the fact that interest is received each year through cash/bank account and it is not re-invested. Hence interest on DRR investment is not credited to DRR A/c but taken to P&L A/c. (in accordance with AS 5)

b. At the time of redemption of debentures:

v) For encashment of Debenture Redemption Reserve Investments

Bank A/c Dr.

To Debenture Redemption Reserve Investment A/c

vi) For amount due to debenture holders on redemption

Debentures A/c Dr.

To Debenture holders A/c

vii) For payment to debenture holders

Debenture holders A/c Dr.

To Bank A/c

viii) After redemption of debentures, DRR should be transferred to general reserve

DRR A/c Dr.

To General Reserve

Notes:

a) Debentures sometimes are redeemable at a premium. In such a case, premium on redemption of debentures shall have to be set off with P&L account.

When premium on redemption is due:

Premium on Redemption of Debentures A/c Dr.

To Debenture Holders A/c

For cancellation of such premium:

Profit & Loss account Dr.

To Premium on Redemption of Debentures A/c

METHODS OF REDEMPTION OF DEBENTURES:

Methods of Redemption of Debentures

- **By payment in Lumpsum method (a)**
- **By Annual drawings (b)**
- **By purchase of own debentures in open market. (c)**
- **By conversion through shares (d)**

a) BY PAYMENT IN LUMPSUM

Under payment in lumpsum method, at maturity or at the expiry of a specified period of debenture the payment of entire debenture is made in one lot or even before the expiry of the specified period.

b) BY PAYMENT IN INSTALMENTS:

Under payment in instalments method, the payment of specified portion of debenture is made in instalments at specified intervals.

c) PURCHASE OF DEBENTURES IN OPEN MARKET:

Debentures sometimes are purchased in open market. In such a case Own Debenture Account is debited and bank is credited.

Suppose a company has issued 8% debentures for Rs. 10,00,000, interest being payable on 31st March and 30th September every year. The company purchases Rs. 50,000 debentures at Rs. 96 on 1st August 20X1. This means that the company will have to pay Rs. 48,000 as principal plus Rs. 1,333 as interest for 4 months.

Entry

		Rs.	Rs.
Own Debentures (50,000 x 96/ 100)	Dr.	48,000	
Interest Account (50,000 x 8% x 4/12)	Dr.	1,333	
To Bank			49,333

It should be noted that even though Rs. 50,000 debentures have been purchased for Rs. 48,000 there is no profit. On purchase of the debentures, profit does not arise; only on sale and in this case on cancellation of debentures, profit could arise.

These debentures may be cancelled on same date. The journal entries to be passed will be the following:

		Rs.	Rs.
8% Debentures A/c	Dr.	50,000	
To Own Debentures A/c			48,000
To Profit on cancellation of debentures			2,000
(Cancellation of Rs. 50,000 Debentures)			

d) <u>Redemption through conversion of shares</u>:

Under Section 71 (1) of the Companies Act, 2013, a company may issue <u>debentures with an option to convert such debentures into shares, either wholly or partly at the time of redemption</u>. Provided that the issue of debentures with an option to convert such debentures into shares, wholly or partly, <u>should be approved by a special resolution</u> passed at a duly convened general meeting.

1. Debentures A/C Dr

To Debenture holders A/C

2. Debenture holders A/C Dr

To Equity share capital A/C

To Securities premium A/C (If shares issued with premium)

PROBLEMS EXCLUSIVE FROM CMA SOURCE

ISSUE OF DEBENTURES

Problem No.1

P Ltd. issued 50,000, 8% Debentures of Rs.100 each at a premium of Rs.20 payable as follows:
Rs.30 on application; Rs.40 on allotment (including premium); and Rs.50 on first and final call.
Applications were received for all the debentures along with the application money and allotment was made Call money was also received on due date. Pass necessary journal entries to record the issue of debentures.
What will be the entries if the entire amount is received on application? **(Illustration 45)**

Problem No.2

Journalize the following transactions. Narration is not required:
Issue of 12% 1,00,000 debentures of Rs.100 each

1. at par and redeemable at par.
2. at 10% discount and redeemable at par.
3. at 10% premium and redeemable at par.
4. at 10% premium and redeemable at a premium of 5%.
5. at par and redeemable at a premium of 5%.
6. at 10% discount and redeemable at a premium of 5%. **(Illustration 46)**

Problem No.3

Z Ltd. took over the assets of Rs.6,00,000 and liabilities of Rs.80,000 of C Ltd. for an agreed purchase consideration of Rs.5,40,000 to be satisfied by the issue of 10% Debentures of Rs.1,000 each.
Required: Show the necessary journal entries in the books of Z Ltd, assuming that—
Case (a) Such Debentures are issued at par;
Case (b) Such Debentures are issued at 20% premium; and
Case (c) Such Debentures are issued at 10% discount; **(Illustration 47)**

Problem No.4

C Ltd. secured a loan of Rs. 8,00,000 from the Axis Bank by issuing 1,000, 12% Debentures of Rs. 1000 each as collateral security.
Required: How will you treat the issue of such debentures? **(Illustration 48)**

REDEMPTION OF DEBENTURES

Problem No.5

P Ltd. had issued Rs.15,00,000, 10% Debentures which are due to be redeemed out of profits on Nov. 1, 2020 at a premium of 5%. The company had a Debenture Redemption Reserve of Rs.6,21,000. It was decided to invest the required amount in Debenture Redemption Investment on 15.4.2020. Pass necessary journal entries for recording the transactions relating to redemption of debentures.

(Illustration 49)

Problem No.6

A company issued 100,000 15% debentures of Rs. 100 each at par redeemable at a premium of 15%. After 8 years the company served notice of redemption and redeemed all debentures as per the terms of issue. You are required to make entries at the time of issue and at the time of redemption.

(Illustration 50)

Problem No.7

The Balance Sheet of AB Ltd. as on March 31, 2020 reflected 10,000, 12% Debentures of Rs.100 each outstanding. These debentures were due for redemption on July 31, 2021. The company decided to transfer Rs.5,00,000 to Debenture Redemption Reserve on March 31, 2021 and invest Rs.1,50,000 in fixed deposits with Bank of India on April 8, 2021. The investment was encashed as the debentures were redeemed on due date. Pass journal entries to record the above transactions (Ignore transactions relating to interest on debentures). **(Illustration 51)**

Problem No.8

K Ltd. issued Rs.6,00,000,13% Debentures of Rs.100 each on April 1, 2017 at a premium of 6% redeemable at a premium of 10% on March 31, 2021. The debentures were redeemed on due date. Assume that the required minimum investment was made by the company in 10% Government Securities on the last due date meant for the purpose of this redemption. Pass journal entries to record the issue and redemption of debentures. (Ignore transactions relating to interest on debentures and writing-off loss on issue of debentures). **(Illustration 52)**

Problem No.9

B Ltd. issued notice of its intention to redeem its outstanding Rs.12,00,000, 8% Debentures at 102% and offered the holders the following options to apply for the redemption moneys:

(i) 6% Cumulative Preference shares of Rs.20 each at Rs.22.50 per share; and

(ii) 10% Debentures of Rs.100 each at Rs.96.

The holders of Rs.4,80,000 debentures accepted proposal (i), and Rs.7,20,000 debenture-holders accepted proposal (ii). Pass necessary journal entries to record the above-mentioned transactions.

(Illustration 54)

PROBLEMS FROM CA SOURCE FOR PRACTICE

PROBLEM 1:

The following balances appeared in the books of a company (unlisted company other than AIFI, Banking company, NBFC and HFC) as on December 31, 20X1: 6% Mortgage 10,000 debentures of Rs. 100 each; Debenture Redemption Reserve (for redemption of debentures) Rs.50,000; Investments in deposits with a scheduled bank, free from any charge or lien Rs. 1,50,000 at interest 4% p.a. receivable on 31st December every year. Bank balance with the company is Rs. 9,00,000.

The Interest on debentures had been paid up to December 31, 20X1.

On February 28, 20X2, the investments were realised at par and the debentures were paid off at 101, together with accrued interest.

Write up the concerned ledger accounts (excluding bank transactions). Ignore taxation.

(SM, ILLUSTRATION 2)

PROBLEM 2:

The following balances appeared in the books of Paradise Ltd (unlisted company other than AIFI, Banking company, NBFC and HFC) as on 1-4-20X1:

(i) 12 % Debentures Rs. 7,50,000

(ii) Balance of DRR Rs. 25,000

(iii) DRR Investment 1,12,500 represented by 10% Rs. 1,125 Secured Bonds of the Government ofIndia of Rs. 100 each.

Annual contribution to the DRR was made on 31st March every year. On 31-3-20X2, balance at bank was Rs. 7,50,000 before receipt of interest. The investment were realised at par for redemption of debentures at a premium of 10% on the above date.

You are required to prepare the following accounts for the year ended 31st March, 20X2:

(1) Debentures Account

(2) DRR Account

(3) DRR Investment Account

(4) Bank Account

(5) Debenture Holders Account. **(SM, ILLUSTRATION 4)**

PROBLEM 3:

Sencom Limited (listed company) issued Rs. 1,50,000 5% Debentures on 30th September 20X0 on which interest is payable half yearly on 31st March and 30th September. The company has power to purchase debentures in the open market for cancellation thereof. The following purchases were made during the year ended 31st December, 20X2 and the cancellation were made on the same date. On 31 December 20X0, investments made for the purpose of redemption were Rs. 22,500.

1st March 20X2 - Rs. 25,000 nominal value purchased for Rs. 24,725 ex-interest, 1st September 20X2 - Rs. 20,000 nominal- value purchased for Rs. 20,125 cum-interest.You are required to draw up the following accounts up to the date of cancellation:

(i) Debentures Account; and

(ii) Own Debenture (Investment) Account.

Ignore taxation. **(SM, ILLUSTRATION 3)**

PROBLEM 4:

On January 1, Rama Ltd. (listed company), had 500 Debentures of Rs. 100 each outstanding in its books carrying interest at 6% per annum. In accordance with the regulatory requirements, the directors of the company acquired debentures from the open market for immediate cancellation as follows:

March 1 Rs. 5,000 at face value Rs. 98.00 (cum interest)

Aug. 1 Rs. 10,000 at face value Rs. 100.25 (cum interest)

Dec. 15 Rs. 2,500 at face value Rs. 98.50 (ex-interest)

Debenture interest is payable half-yearly, on 30th June and 31st Dec.

Show ledger accounts of Debentures and Debenture interest for the full year by splitting into first and second half years, ignoring income-tax. **(SM, ILLUSTRATION 1)**

PROBLEM 5:

XYZ Ltd. has issued 1,000, 12% convertible debentures of Rs. 100 each redeemable after a period of five years. According to the terms & conditions of the issue, these debentures were redeemable at a premium of 5%. The debenture holders also had the option at the time of redemption to convert 20% of their holdings into equity shares of Rs. 10 each at a price of Rs. 20 per share and balance in cash. Debenture holders amounting Rs. 20,000 opted to get their debentures converted into equity shares as per terms of the issue. You are required to calculate the number of shares issued and cash paid for redemption of Rs. 20,000 debenture holders. **(RTP-NOV 2020-8)**

PROBLEM 6:

The Balance Sheet of Convertible Limited (unlisted company other than AIFI, Banking company,NBFC and HFC), as at 31st March, 20X1, stood as follows:

Particulars	Note No	Rs.
Equity and liabilities		
(1) Shareholder's Funds		
(a) Share Capital	**1**	50,00,000
(b) Reserves and Surplus	**2**	1,10,00,000
(2) Non-current liabilities		

(a) Long term borrowings	**3**	1,65,00,000
(3) Current Liabilities		
(a) Other current liabilities		1,25,00,000
Total		**4,50,00,000**
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	**4**	1,60,00,000
(b) Non-current investment		15,00,000
(2) Current assets		
(a) Cash and cash equivalents		75,00,000
(b) Other current assets		2,00,00,000
		4,50,00,000

Notes to Accounts:

			Rs.
1.	**Share Capital**		
	5,00,000 shares of Rs. 10 each fully paid		50,00,000
2.	**Reserve and Surplus**		
	General Reserve	90,00,000	
	Profit & Loss Account	10,00,000	
	Debenture redemption reserve	10,00,000	1,10,00,000
3.	**Long term borrowings**		
	13.5% convertible Debentures (1,00,000 debentures of Rs. 100 each)		1,00,00,000
	Other loans		65,00,000
			1,65,00,000
4.	**Non-current investments**		
	Debenture redemption reserve investments		15,00,000

The debentures are due for redemption on 1st July, 20X1. The terms of issue of debentures provided that they were redeemable at a premium of 5% and also conferred option to the debenture holders to convert 20% of their holdings into equity shares at a predetermined price of Rs. 15.75 per share and the payment in cash.

Assuming that:

(i) Except for 100 debenture holders holding totally 25,000 debentures, the rest of them exercisedthe option for maximum conversion.

(ii) the investments were realised at par on sale; and

(iii) All the transactions are put through, without any lag, on 1st July, 20X1.

Redraft the balance sheet of the company as on 1st July, 20X1 after giving effect to the redemption. Show your calculations in respect of the number of equity shares to be allotted and the necessary cash payment. **(SM, ILLUSTRATION 6)**

PROBLEM 7:

Jeet Limited (listed company) recently made a public issue in respect of which the following information is available:

(a) No. of partly convertible debentures issued - 1,00,000; face value and issue price- Rs. 100 per debenture.

(b) Convertible portion per debenture- 60%, date of conversion- on expiry of 6 months from the date of closing of issue i.e 31.10.2020.

(c) Date of closure of subscription lists - 1.5.2020, date of allotment- 1.6.2020, rate of interest on debenture- 15% payable from the date of allotment, value of equity share for the purpose of conversion- 60 (Face Value 10).

(d) Underwriting Commission- 2%.

(e) Number of debentures applied for - 75,000.

(f) Interest payable on debentures half-yearly on 30th September and 31st March.

(g) Write relevant journal entries for all transactions arising out of the above during the year ended 31st March, 2021 (including cash and bank entries). **(RTP-NOV 2021-8)**

PROBLEM 8:

P Ltd. issued 50,000, 8% Debentures of Rs.100 each at a premium of Rs.20 payable as follows: Rs.30 on application; Rs.40 on allotment (including premium); and Rs.50 on first and final call. Applications were received for all the debentures along with the application money and allotment was made Call money was also received on due date. Pass necessary journal entries to record the issue of debentures. A) What will be the entries if the entire amount is received on application? B) What will be the entries if the amount is collected through installments? **(Illustration-45)**

PROBLEM 9:

Journalize the following transactions. Narration is not required: Issue of 12% 1,00,000 debentures of Rs.100 each

7. at par and redeemable at par.

8. at 10% discount and redeemable at par.

9. at 10% premium and redeemable at par.

10. at 10% premium and redeemable at a premium of 5%.

11. at par and redeemable at a premium of 5%.

12. at 10% discount and redeemable at a premium of 5%. **(Illustration-46)**

PROBLEM 10:

Z Ltd. took over the assets of Rs.6,00,000 and liabilities of Rs.80,000 of C Ltd. for an agreed purchase consideration of Rs.5,40,000 to be satisfied by the issue of 10% Debentures of Rs.100 each. Required: Show the necessary journal entries in the books of Z Ltd, assuming that— Case (a) Such Debentures are issued at par; Case (b) Such Debentures are issued at 20% premium; and Case (c) Such Debentures are issued at 10% discount; **(Illustration-47)**

7. ESOP, ESPP, SWEAT EQUITY SHARES

Introduction:

Now-a-days established companies, in order to retain quality human resources in the organisation, offer innovative compensation strategies to their employees including directors. One of such categories of innovative strategies involve paying compensation the value which is based on the value of the company's stock (i.e., bundle of shares).

This category of compensation scheme is popularly known as Stock Based Employee Benefit Scheme/Plan. The most common form of Stock Based Employee Benefit Scheme/Plans are (a) Employee Stock Option Plan/ Scheme (ESOP/ESOS) and (b) Employee Stock Purchase Plan/ Scheme (ESPP/ESPS).

I. Employee Stock Option Plan/ Scheme (ESOP/ESOS)

As per section 2(37) of the Companies Act, 2013, "employees' stock option" means the option given to the Directors, officers or employees of a company or of its holding company or subsidiary company or companies, if any, which gives such Directors, officers or employees, the benefit or right to purchase, or to subscribe for, the shares of the company at a future date at a pre-determined price.

The general features of ESOP are as follows:

a. It is an innovative tool for employee compensation.

b. It is an employee stock-based benefit scheme/plan.

c. It provides the employees a right to acquire company's stock at a predetermined price.

d. It is exercised on a future date.

e. It ensures employee participation in profits.

Important Terminologies

i. Option: A right (but not the obligation) which is granted to an employee pursuant to an ESOP to buy company's shares on the future date at a predetermined price.

ii. Grant: It refers to the issuance of option to the employee under an ESOP.

iii. Vesting: It refers to the requirement to be satisfied by the employee to apply the right to exercise the option.

Conditions may include certain period of service, meeting any performance standard etc.

iv. Vesting Period: It is the period during which the vesting has been granted to the employee under the ESOP.

v. Exercise: It is the act of subscribing the shares under ESOP.

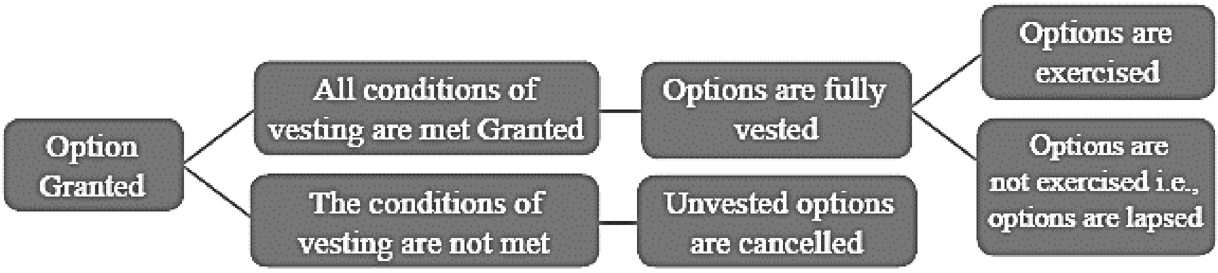
vi. Exercise Period: The time period within which the option shall be exercised.

vii. Exercise Price: It is the price payable to subscribe the shares under ESOP.

viii.Intrinsic Value: It is the excess of market price over the exercise price of shares.

<u>ESOP Process Flow</u>

The sequential steps under an ESOP are depicted in the following diagram.



<u>Provisions Regarding Employee Stock Option Plan</u>

The statutory provisions relating to ESOP are governed by Section 62 of the Companies Act, 2013 and Rule 12 of the Companies (Share Capital and Debentures) Rules, 2014.

According to Section 62 of the Companies Act, 2013, any company having a share capital may proposes to increase its subscribed capital by the issue of further shares to employees under a scheme of employees' stock option, subject to special resolution passed by company and subject to such conditions as may be prescribed.

In addition, Rule 12 of the Companies (Share Capital and Debentures) Rules, 2014 provides the terms and conditions subject to which an unlisted company can issue shares to its employees under ESOP.

Additionally, SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021 provides terms and conditions for a number of share-based employee benefit schemes including ESOP and ESPP and also for issue of sweat equity shares by listed companies.

<u>Accounting for ESOP</u>

The accounting for ESOP (and also for ESPP discussed later in this Module) is guided by the Guidance Note on Accounting for Employee Share-based Payments issued by The Institute of Chartered Accountants of India.

The accounting entries at various stages of implementing the ESOP are as follows:

Stage	Accounting Entries
a. Granting of Stock Option	At this stage no accounting entry is required.
b. Recognition of ESOP Expense This further involves the following steps: **i.** Determination of Intrinsic Value	➢ On recognition of Stock Option Expenses Employee Stock Option Expenses A/c ……Dr. To Employee Stock Option Outstanding A/c ➢ On transfer at the end of the period

Intrinsic Value = Market price per share – Exercise price per share **ii.** Determination of Gross Value of employee compensation expenses GV = No. of options expected to vest × Intrinsic vale × Expired Period / Total Vesting Period **iii.** Determine expenses to be recognized. Expenses to be recognized = GV – Cumulative expenses recognized up to earlier accounting period	Profit and Loss A/c ……………………Dr. To Employee Stock Option Expenses A/c
c. Cancellation of options during the vesting period	➢ If cumulative expenses recognized up to earlier accounting period < GV No Journal Entry is required ➢ If cumulative expenses recognized up to earlier accounting period > GV Employee Stock Option Outstanding A/c …Dr. To Employee Stock Option Expenses A/c Employee Stock Option Expenses A/c…Dr. To Profit and Loss A/c
d. Exercising of Stock Options	Bank A/c …………………………Dr. To Employee Stock Option Outstanding A/c Employee Stock Option Outstanding A/c …Dr. To Equity Share Capital A/c To Securities Premium A/c
e. Lapse of unexercised option	Employee Stock Option Outstanding A/c …Dr. To General Reserve A/c

Note:

(1) The amount of Employees Stock Option Expenses will be reflected under the sub-head Employee Benefit Expenses in the Statement of Profit and Loss.

(2) Balance of Employee Stock Option Outstanding A/c should be shown under Reserve and Surplus in the Balance Sheet.

(3) Upon exercise of the stock options, the shares issued under ESOP should be included in the Share Capital in the Balance Sheet and securities premium thereon should be included in Securities Premium.

(4) The Notes to Accounts must provide the details of ESOP.

II. Employee Stock Purchase Plan/ Scheme (ESPP/ESPS)

Employee Stock Purchase Scheme (ESPS) refers to a scheme under which the company offers shares to employees as part of a public issue or otherwise.

Accounting for Employee Stock Purchase Scheme

The fair value of ESPP shall be treated as a form of employee compensation in the financial statements of the company.

The fair value of ESPP = No. of shares to be issued under ESPP x (Fair value per share – issue price)

The accounting entries will be as follows:

(i) For shares purchased under ESPP

Bank A/c ………………………………………….Dr.

Employee Compensation Expense A/c ……………..Dr.

To Equity Share Capital Account

To Securities Premium Account

(ii) For transfer of the balance Employee Compensation Expense A/c

Profit and Loss A/c …………………………..Dr.

To Employee Compensation Expense A/c

Note:

(1) The amount of Employees Compensation Expenses will be reflected under the sub-head Employee Benefit Expenses in the Statement of Profit and Loss.

(2) Upon purchase of shares under ESPP, the shares issued should be included in the Share Capital in the Balance Sheet and securities premium thereon should be included in Securities Premium.

(3) The Notes to Accounts must provide the details of ESPP.

Issue of Sweat Equity Shares

When a company issues shares to its employees or directors for providing knowhow, intellectual properties etc., such an issue of shares is termed as issue of sweat equity shares.

As per Section 2(88) of the Companies Cat, 2013, "sweat equity shares" means such equity shares as are issued by a company to its Directors or employees at a discount or for consideration, other than cash, for providing their know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.

Provisions Relating to Issue of Sweat Equity Shares

Section 54 of the Act states that –

1. Notwithstanding anything contained in section 53, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled, namely: —

- **(a)** the issue is authorised by a special resolution passed by the company;
- **(b)** the resolution specifies the number of shares, the current market price, consideration, if any, and the class or classes of Directors or employees to whom such equity shares are to be issued;
- **(c)** where the equity shares of the company are listed on a recognised stock exchange, the sweat equity shares are issued in accordance with the regulations made by the Securities and Exchange Board in this behalf and if they are not so listed, the sweat equity shares are issued in accordance with such rules as may be prescribed.

2. The rights, limitations, restrictions and provisions as are for the time being applicable to equity shares shall be applicable to the sweat equity shares issued under this section and the holders of such shares shall rank pari passu with other equity shareholders.

Rule 8 of the Companies (Share Capital and Debentures) Rules, 2014 further states that –

- **(1)** A company other than a listed company, which is not required to comply with the Securities and Exchange Board of India Regulations on sweat equity, shall not issue sweat equity shares to its directors or employees at a discount or for consideration other than cash, for their providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called, unless the issue is authorised by a special resolution passed by the company in general meeting.
- **(2)** The special resolution authorising the issue of sweat equity shares shall be valid for making the allotment within a period of not more than twelve months from the date of passing of the special resolution.
- **(3)** The company shall not issue sweat equity shares for more than fifteen percent of the existing paid-up equity share capital in a year or shares of the issue value of rupees five crores, whichever is higher.
- **(4)** The sweat equity shares issued to directors or employees shall be locked in/non-transferable for a period of three years from the date of allotment.
- **(5)** The sweat equity shares to be issued shall be valued at a price determined by a registered valuer as the fair price giving justification for such valuation.

Accounting for Issue of Sweat Equity Shares

I. Issue of sweat equity shares for cash consideration at a discount

When sweat equity shares are issued for cash consideration at a discount, the difference between cash consideration and nominal value of sweat equity shares shall be considered as the value of intellectual property provided by the employee or director. The accounting entry shall be as follows:

Bank A/c …………………Dr.

Intellectual Property A/c ……Dr.

To Equity Share Capital A/c

Note: The details of issue of sweat equity shares shall be disclosed in the Notes to Balance Sheet on Equity Share Capital.

II. Issue of sweat equity shares for consideration other than cash

(i) Sweat equity shares issued in pursuant to acquisition of an asset

Intellectual Property A/c ……………………………………. Dr. (Value of asset)

Employee/Director's Compensation Expenses A/c …………Dr. (Difference)

To Equity Share Capital A/c

(ii) Sweat equity shares issued not in pursuant to acquisition of an asset

Employee/Director's Compensation Expenses A/c …………Dr.

To Equity Share Capital A/c

Note: Employee/Director's Compensation Expenses will be included in Employee Benefit Expenses in the Statement of Profit and Loss. The details of issue of sweat equity shares shall be disclosed in the Notes to Balance Sheet on Equity Share Capital.

PROBLEMS FOR CLASSROOM DISCUSSION

ESOP

PROBLEM 1:

ABC Ltd., a listed company, granted 2,000 options on 01.04.2019 at an exercise price of Rs.50 per share. The market price at that time was of Rs.150 per option (face value of each share being Rs.10). The maximum exercise period and the vesting period are 1 year and 2 years respectively. On 01.04.2020, 600 unvested options were lapsed while 1,200 options were exercised on 30.06.2021. The remaining options were lapsed at the end of the exercise period. Show the journal entries to record the above transactions. **(Illustration-29)**

PROBLEM 2:

K Ltd. granted option for 16,000 equity shares on 01.10.16 at Rs.80 when the market price was Rs.170. the vesting period is 4 ½ years. 8,000 unvested options lapsed on 01.12.2018. 6,000 options are exercised on 30.09.21 and 2,000 vested options lapsed at the end of the exercise period. Pass journal entries to record the above transactions. **(Illustration-30)**

ESPP

PROBLEM 3:

Y Ltd issued 2,000 shares on 1st April, 2021 under ESPP at Rs.50 when the market price was Rs.150 (face value being Rs.10). Pass necessary journal entries to record the above transactions.

(Illustration-31)

PROBLEM 4:

On 1st April, 2019, X Ltd. offered 200 shares to each of its 400 employees at Rs.25 per share. The employees are given a month to accept the shares. The shares issued under the plan shall be subject to lock-in to transfer for three years from the grant date, i.e., 30th April, 2019. The market price of shares of the company on the grant date is Rs.30 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at Rs.28 per share.

Up to 30th April, 2019, 50% of employees accepted the offer and paid Rs.25 per share purchased. Nominal value of each share is Rs.10. Record the issue of shares in the books of the company under the aforesaid plan. **(Illustration-32)**

SWEAT EQUITY SHARES

PROBLEM 5:

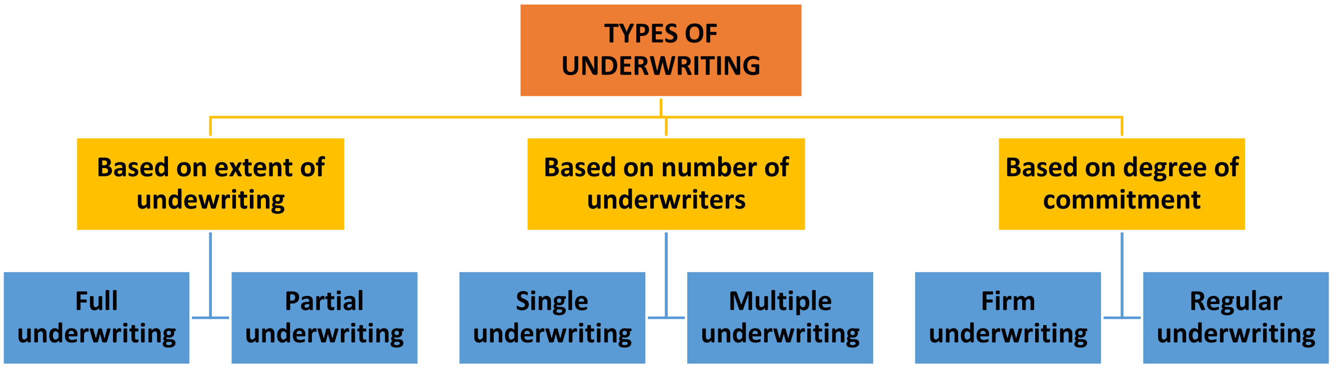
Show the accounting entries for the following.

a. Tinku Ltd. allotted 500 sweat equity shares of Rs.100 each to its directors at a discount of 6%.

b. 800 sweat equity shares of Rs.100 allotted to employees at par in consideration of technical know-how. **(Illustration-28)**

8. UNDERWRITING OF SECURITIES

Underwriting of securities is an agreement, entered into by a company (issuing the security) with a financial agency, who guarantee that no security remains unsubscribed. The concerned financial agency is known as 'underwriter'. The underwriters provide their services against certain fees known as 'underwriting commission'.



Types of Underwriting:

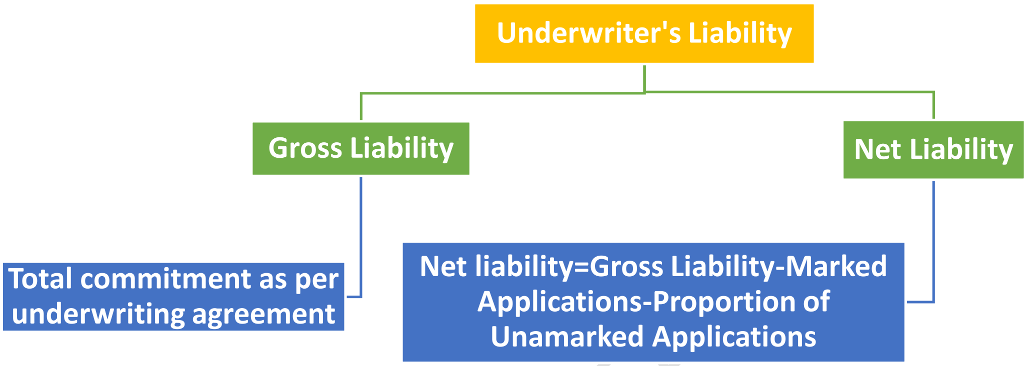
I. **Based on the extent of underwriting:** Based on the extent, underwriting can be of two types – full underwriting and partial underwriting. When the entire issue is underwritten by the underwriters, it is called Full Underwriting or Complete Underwriting. On the other hand, when only a part of the total issue is underwritten by the underwriters, it is called partial underwriting.

II. **Based on the number of underwriters:** Based on the number of underwriters involved, underwriting can be of two types – single underwriting and multiple underwriting. When the entire issue is underwritten by a single underwriter, it is called a Single Underwriting. On the other hand, when entire issue is underwritten jointly by more than one financial agency, it is referred to as syndicate or Multiple Underwriting.

III. **Based on the Degree of Commitment:** Based on the commitment of underwriters, underwriting can be of two types – firm underwriting and regular underwriting. In case of firm underwriting, the underwriter gives a specific commitment to take a specified number of shares, irrespective of the number of shares subscribed by the public. On the other hand, regular underwriting refers to the usual underwriting agreement in which the underwriters would be liable to take up the securities in the event of under-subscription.

Marked vs. Unmarked Applications:

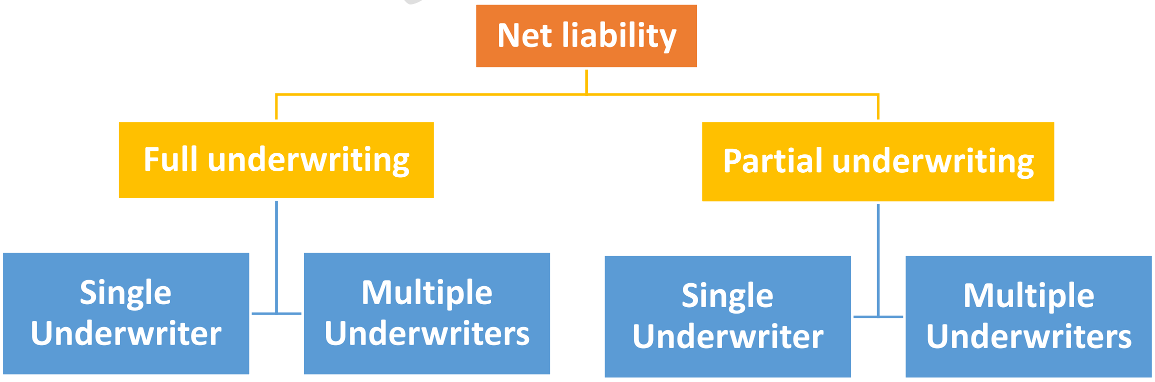
1. 'Marked' applications are those applications which bear the stamp of an underwriter.
2. The 'unmarked' applications are those applications which bear no stamp of an underwriter. These applications are received by the company directly from the public.
3. The distinction between marked and unmarked applications becomes immaterial when the whole issue is subscribed by only one underwriter or when the issue is fully subscribed in case of multiple underwriters.



Underwriting Commission: The price charged by the underwriter for his underwriting services rendered to the issuer company is called Underwriting Commission.

Underwriting Commission = [Gross Liability (in no.) x Issue Price per security] x Rate of Commission

Determination of Underwriter's Liability:



I. **When the Issue is Fully Underwritten by a Single Underwriter:**

a) Here, the underwriter is responsible for 100% of the unsubscribed issue. Since, the entire issue is underwritten by him, the distinction between marked and unmarked applications is irrelevant here. Further, the concept of firm underwriting is also not relevant in this case.

b) Underwriter's liability = No. of Shares Issued (-) No. of shares subscribed by the public.

II. <u>When the Issue is Fully Underwritten by Multiple Underwriters:</u>

a) Here, the underwriters are jointly responsible for subscription of 100% of the issue size. Thus, individual underwriters are given credits for respective marked applications. The unmarked applications are shared between all the underwriters in proportion of their "Gross Liability" or "Gross Liability (-) Marked Application" as per underwriting arrangement agreed.

b) The distinction between marked and unmarked applications is relevant here and Firm Underwriting becomes significant to decide net liability.

c) **<u>Treatment of Firm Underwriting</u>**: In case of Firm underwriting situation, the underwriter must take up the number of securities underwritten 'firm' irrespective of its liability under the regular underwriting agreement.

- **i)** **Firm underwriting treated as Marked applications:** Here, the benefit of firm underwriting is given to each individual underwriter i.e., number of shares underwritten firm is deducted from each underwriter's respective liability; or
- **ii)** **Firm underwriting is treated as Unmarked applications:** Here, the benefit is given to all underwriters in the ratio of Gross Liability.

d) Underwriter's liability = Gross Liability (-) No. of Marked applications (-) Shares of Unmarked applications (+) Firm Underwriting.

III. <u>When the Issue is Partially Underwritten by a Single Underwriter:</u>

a) In this situation, the concerned underwriter shall be responsible only for the agreed portion of the total issue. For the balance portion of the issue, the company itself shall be responsible.

b) The liability of the underwriter will be determined in the following manner:

Step 1: Gross Liability = Total Issue Size x % of underwriting

Step 2: No. of shares unsubscribed = Total no. of shares offered (–) No. of shares subscribed (including marked applications)

Step 3: Deficit of the underwriter = Gross Liability (-) Marked Applications

Step 4: Net Liability = Step 2 or Step 3 – whichever is lower.

a) **<u>Treatment of Firm Underwriting:</u>** In case the underwriter has underwritten 'firm', the liability of the underwriter should be determined by adding the number of shares underwritten 'firm' to the 'Net Liability under the underwriting contract' mentioned above. In this context, there can be two possibilities as follows:

- **(i).** **No abatement is allowed for the shares taken up 'firm':** This means that the shares underwritten 'firm' will not be adjusted against 'Net Liability under the underwriting contract' and the underwriter will have to subscribe them additionally. Therefore, here, number of shares to be taken up by the underwriter = 'Net Liability under the underwriting contract' + Firm Underwriting.

(ii). **Abatement is allowed for the shares taken up 'firm':** This means that the shares underwritten 'firm' will be adjusted against 'Net Liability under the underwriting contract'. Hence, in this case, number of shares to be taken up by the underwriter = 'Net Liability under the underwriting contract' or Firm Underwriting – whichever is higher.

IV. <u>When the Issue is Partially Underwritten by Multiple Underwriters:</u>

a) Here, the underwriters together take the responsibility of a part of the total issue and the for the remining portion, the company itself is held responsible.

b) The credit for marked applications is given to the individual underwriters. However, the credit for unmarked applications does not go to the underwriters.

<u>Accounting for Underwriting:</u>

Particulars	**Journal Entries**	**Remarks**
For shares taken up by the underwriters	Underwriters A/c ... Dr. To Share Capital A/c To Securities Premium A/c	Issue Price Face Value Premium on issue
Underwriting commission	Underwriting Commission A/c ..... Dr. To Underwriters A/c	Commission payable
Final Settlement	Bank A/c............................ Dr. Underwriters A/cOr Underwriters A/c................ Dr. To Bank A/c	Difference between Net liability under underwriting contract and commission payable.

PROBLEMS FOR CLASSROOM DISCUSSION

Problem1:

XYZ Ltd. is issuing 20,00,000 shares of Rs.10 each to the public. N Ltd. has been appointed as the underwriter for the whole issue size. The commission payable to the underwriter is 5% of the issue price. Calculate the amount of underwriting commission payable to N Ltd. if the shares are issued at par. How will your answer change if the shares are issued at 20% premium?

(Illustration 59)

Problem2:

A Ltd. issued 1,00,000 equity shares of Rs.100 each at par to the public, underwritten only by B & Co. The company received applications for 90,000 shares of which 80,000 shares were marked. Determine the liability of the B & Co.

(Illustration 60- Single Underwriter – Full Underwriting)

Problem3:

M Ltd., incorporated on April 1, 2021, issued a prospectus inviting applications for 5,00,000 equity shares of Rs.10 each. The issue was fully underwritten by A, B, C and D as follows: A - 2,00,000; B - 1,50,000; C - 1,00,000; and D - 50,000. The applications were received for 4,50,000 shares of which marked applications were as follows: A - 2,20,000; B- 90,000; C - 1,10,000; and D - 10,000. Find out the liability of the individual underwriters in each of the following cases:

(i). Unmarked applications are apportioned in the ratio of "Gross Liability"; and

(ii). Unmarked applications are apportioned in the ratio of "Gross Liability (-) Marked Applications"

(Illustration 61- Full Underwriting, Multiple Underwriters, Without Firm Underwriting, Alternative Treatment w.r.t Unmarked Applications)

Problem4:

The following underwriting took place for P Ltd. which invited applications for 10,000 shares of Rs.10 each: X: 6,000 shares Y: 2,500 shares Z: 1,500. shares In addition, there were firm underwriting as follows: X: 800 shares Y: 300 shares Z: 1,000. shares Total subscription including firm underwriting was 7,100 shares, and the forms included the following marked forms: X: 1,000 shares Y: 2,000 shares Z: 500 shares. Show the allocation of liability of the underwriters, if –

(i). Firm underwriting is treated as marked applications.

(ii). Firm underwriting is treated as unmarked applications.

(Illustration 63- Full Underwriting, Multiple underwriters, Firm underwriting with Alternative Treatment)

Problem5:

Mr. X underwrites 60% of an issue of 20,000 shares of Rs.100 each of ABC Ltd. He has also agreed for a firm underwriting for 1,600 shares. The company received applications for 13,600 shares out of which were 8,000 marked applications. Determine the number of shares to be taken up by Mr. X:

a) If the underwriting contract provides that abatement would be allowed in respect of shares taken up 'firm'.

b) If the underwriting contract provides that no abatement would be allowed in respect of shares taken up 'firm'.

(Illustration 64-Partial underwriting, Sole underwriter, Abatement allowed & Not allowed)

Problem6:

H Ltd. issued 1,50,000 shares which are underwritten as follows: A - 50%; B - 20%; and C - 20%. The underwriters made applications for firm underwriting as under: A - 6,000 shares, B - 3,000 shares, and C - 3,000 shares. The total marked forms including firm underwriting was 1,33,500 shares and they are as follow: A - 78,000 shares, B - 27,000 shares, and C – 28,500 shares. Compute the liability of each underwriter assuming shares underwritten 'firm' are treated as marked applications.

(Illustration 66 -Partial underwriting, multiple underwriters, With Firm underwriting)

Problem7:

M Ltd., incorporated on April 1, 2021, issued a prospectus inviting applications for 2,50,000 equity shares of Rs.10 each. The issue was fully underwritten by A, B, C and D as follows: A - 1,00,000; B - 75,000; C - 50,000; and D - 25,000. The applications were received for 2,25,000 shares of which marked applications were as follows: A – 1,10,000; B- 45,000; C - 55,000; and D - 5,000.: Unmarked applications are apportioned in the ratio of "Gross Liability". Underwriters' commission: 4% of the issue price.

Required: (a) Determine the underwriters' liability in shares;

(b) Determine the underwriters' liability in amount;

(c) Pass journal entries in the books of M Ltd. to record the above transactions.

(Illustration 67-Accounting for underwriting)

COMMON QUESTIONS FOR CHAPTERS 1,3,4,5,6,7

Multiple Choice Questions

1. The balance of Securities Premium A/C cannot be utilized for

A. Writing off preliminary expenses

B. Payment of dividend

C. Buyback of shares

D. Discount on issue of shares

2. Which of the following is not a Free Reserve?

A. General Reserve

B. Dividend Equalization Reserve

C. Revaluation Reserve

D. Revenue Reserve

3. Which of the following reserves cannot be used for the purpose of issuing bonus shares?

A. Revaluation Reserve

B. Dividend Equalization Reserve

C. Capital Redemption Reserve

D. General Reserve

4. Which of the following is not a condition of buy-back of securities?

A. Both fully and partly paid-up securities can be bought back.

B. Buy-back must be authorised by the Articles of Association.

C. Buy-back must be authorised by passing a special resolution in general meeting.

D. Buy-back should be completed within 1 year from the state of passing of special resolution

5. Which of the following is correct?

A. Debenture carries a fixed rate of dividend.

B. A company limited by shares may issue irredeemable preference shares.

C. Unmarked applications are those applications that bear the stamp of the underwriter

D. Except as provided in Section 54, a company shall not issue shares at a discount.

6. At present, a company can issue preference shares which is:

A. Irredeemable

B. Redeemable after the expiry of 20 years from the date of issue

C. Redeemable before the expiry of 20 years from the date of issue

D. Redeemable after the expiry of 25 years from the date of issue

7. Partly paid-up preference shares can be redeemed

A. After the permission from Company Law Board

B. After making them fully paid up

C. After passing a special resolution

D. After the permission from the BOD

8. _________of the Companies Act, 2013 prohibits issue of shares at a discount.

A. Section 53

B. Section 54

C. Section 61

D. Section 62

9. The net profit on forfeiture and reissue of equity shares is transferred to _________.

A. Capital Reserve

B. General Reserve

C. Dividend Equalization Reserve

D. Revaluation Reserve

10. Which of the following is/are statutory book(s) of a company?

A. Register of charges

B. Register of Members

C. Register of debenture holders

D. All of the above

[Answer: 1-B; 2-C; 3-A; 4-A; 5-C; 6-C; 7-B; 8-B; 9-A; 10-D]

State True or False

1. As per Sec 2(43) of the Companies Act, 2013, "Free Reserves" mean such reserves which, as per the latest audited balance sheet of a company, are available for distribution as dividend.

2. After the allotment of shares, sometimes a shareholder is not able to pay the further calls and returns his shares to the company for cancellation. Such voluntary return of shares to the company by the shareholder himself is called Forfeiture of Shares.

3. A Company cannot buy-back its shares from any person through a negotiated deals whether on or off the stock exchange.

4. A company with capital, which cannot be profitably employed, may get rid of it by resorting to buyback, and re-structure its capital and it is a disadvantage.

5. Issue of debentures as a collateral security means issue of debentures as a main security, that is, a security in addition to the prime security.

6. Debenture carries a fixed rate of dividend.
7. ‘Unmarked’ applications are those applications which bear the stamp of an underwriter.
8. The sum which is still to be paid to the Company for a share is known as calls in arrears.
9. An infrastructure company can issue preference shares with a maximum tenure of 20 years.
10. A company limited by shares shall not issue any preference shares which are irredeemable.

[Answer: 1.True; 2.False; 3.True; 4.False; 5.False; 6.True; 7.False; 8.False; 9.True; 10.True]

<u>Fill in the blanks:</u>

1. Register of Members is one of the _____________ Books maintained by a company.
2. ___________ ____________ is that part of the authorized capital which is offered to the public for subscription is called issued capital.
3. The application money to be refunded shall be credited only to the bank account from which the ______________ was remitted.
4. When a share is issued at a value greater than its face value it is said to be issued at a _____________.
5. Except as provided in section 54, a company shall not issue shares at a ______________.
6. Issue of Bonus Share decreases the ______________________________.
7. ___________________ share is permissible from the existing security holders on a proportionate basis through the tender offer.
8. At the time of cancellation of own debentures _____________ A/c is Credited.
9. There are __________ types of Underwriting Agreements.
10. A company is a distinct legal person existing _____________ of its members.

[Answer: 1. Statutory; 2. Issued Capital; 3. subscription; 4. Premium; 5. Discount; 6.Reserves &Surplus; 7. Buy-back; 8. Own Debentures; 9. Two; 10. independent]

<u>Short Essay Type Questions</u>

1. State the provisions of Companies Act, 2013 in respect of use of Securities Premium
2. State the provisions of Companies Act, 2013 in respect of issue of shares at discount
3. Write a short note on Sources of Buy-back of Equity Shares
4. Write a short note on Sources of Redemption of Preference Shares
5. Differentiate Marked and Unmarked Applications
6. What do you mean by Regular Underwriting and Firm Underwriting?

<u>Essay Type Questions</u>

1. State the Conditions for Buy-back of Equity Shares by a company.
2. State the Conditions for Redemption of Preference Shares by a company.

3. Discuss different types of preference shares.
4. Discuss various types of debentures.
5. How will you account for issue of bonus shares by a company?

Numerical Questions-Multiple Choice Questions

1. If Total issue size is 2,00,000 and the underwriter commits for 100% underwriting at a commission of 4%, what will be the commission payable if no. of applications received is 1,40,000. The issue price of shares is Rs.12 for each Rs.10 face value shares.

   a. Rs.28,800

   b. Rs.28,000

   c. Rs.30,000

   d. Rs.30,800

2. Given, paid -up share capital Rs.10,00,000 and free reserves Rs.2,00,000, what is the maximum amount permissible for buy-back of shares?

   a. Rs.2,00,000

   b. Rs.2,50,000

   c. Rs.2,80,000

   d. Rs.3,00,000

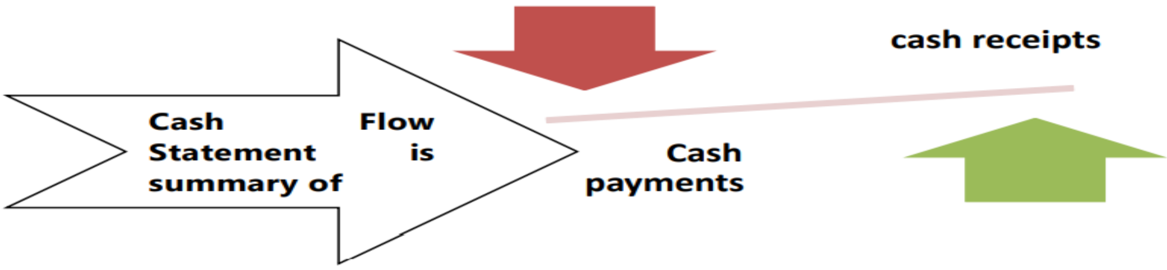
[Answer: 1-A; 2-D]

9. CASH FLOW STATEMENT (ALONG WITH AS-3)

OVERVIEW:

Introduction:

1.



2. Cash flow statements are prepared to explain the cash movements between two points of time.

Objective:

Information about the cash flows of an enterprise is useful in providing users of financial statements with a basis to assess the ability of the enterprise to generate cash and cash equivalents and the needs of the enterprise to utilise those cash flows. It helps the users of Accounts:

♦ To identify the historical changes in the flow of cash & cash equivalents.

♦ To determine the future requirement of cash & cash equivalents.

♦ To assess the ability to generate cash & cash equivalents.

♦ To estimate the further requirement of generating cash & cash equivalents.

♦ To compare the operational efficiency of different enterprises.

♦ To study the insolvency and liquidity position of an enterprise.

Definitions:

Cash comprises cash on hand and demand deposits with banks.

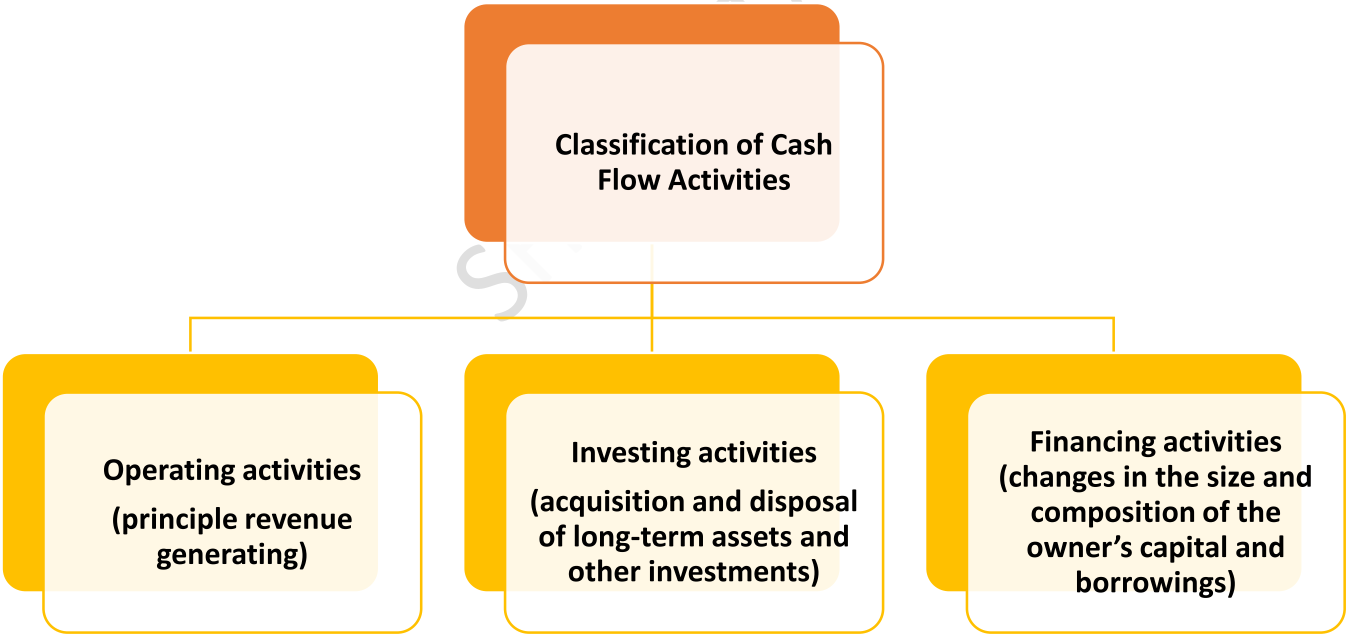
Cash equivalents are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value. A short-term investment is one, which is due for maturity within three months from the date of acquisition.

Cash flows are inflows and outflows of cash and cash equivalents.

SCOPE:

1. As per section 129-Financial statements, with respect to one person company, small company, dormant company and private company (if such a private company is a start-up), may not include the cash flow statement.
2. This Standard is mandatory for the enterprises, which fall in the category of level I, at the end of the relevant accounting period.

CLASSIFICATION OF CASH FLOW ACTIVITIES:



Operating activities are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities.

Cash flows arising from operating activities

- Key indicator of the extent to which the operations of the entity have generated sufficient cash flows to
  - repay loans
  - maintain the operating capability of the entity
  - pay dividends
  - make new investments without recourse to external sources of financing
- Primarily derived from the principal revenue-producing activities of the entity
- Generally, result from the transactions and other events that have role in the determination of net profit or loss
- Example

(a) Cash receipts from the sale of goods and the rendering of services

(b) Cash receipts from royalties, fees, commissions, and other revenue

(c) Cash payments to suppliers for goods and services

(d) Cash payments to and on behalf of employees

(e) Cash receipts and cash payments of an

insurance entity for premiums and claims annuities, and other policy benefits

(f) Cash payments or refunds of income taxes unless they can be specifically identified with financing and investing activities

(g) cash receipts and payments relating to futures contracts, forward contracts, option contracts and swap contracts when the contracts are held for dealing or trading purposes.

(h) Cash flows arising from the purchase and sale of dealing or trading securities

(i) Cash advances and loans made by financial institutions since they relate to their main revenue-producing activity

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

Cash flows arising from investing activities

Examples

Represent the extent to which expenditures have been made for resources intended to generate future income and cash flows

(a) cash payments to acquire fixed assets (including intangibles). These payments include those relating to capitalised research and development costs and selfconstructed fixed assets;

(b) cash receipts from sales of property, plant and equipment, intangibles and other long-term assets; (c) cash payments to acquire equity or debt instruments of other entities and interests in joint ventures (other than payments for those instruments considered to be cash equivalents or those held for dealing or trading purposes);

(d) cash receipts from sales of equity or debt instruments of other entities and interests in joint ventures (other than receipts for those instruments considered to be cash equivalents and those held for dealing or trading purposes);

(e) cash advances and loans made to other parties (other than advances and loans made by a financial institution);

(f) cash receipts from the repayment of advances and loans made to other parties (other than advances and loans of a financial institution);

(g) cash payments for futures contracts, forward contracts, option contracts and swap contracts except when the contracts are held for dealing or trading purposes, or the payments are classified as financing activities; and

(h) cash receipts from futures contracts, forward contracts, option contracts and swap contracts except when the contracts are held for dealing or trading purposes, or the receipts are classified as financing activities.

Financing activities are activities that result in changes in the size and composition of the owners' capital (including preference share capital in the case of a company) and borrowings of the enterprise.

Cash flows arising from financing activities

useful in predicting claims on future cash flows by providers of capital to the entity

Examples

(a) cash proceeds from issuing shares or other equity instruments;

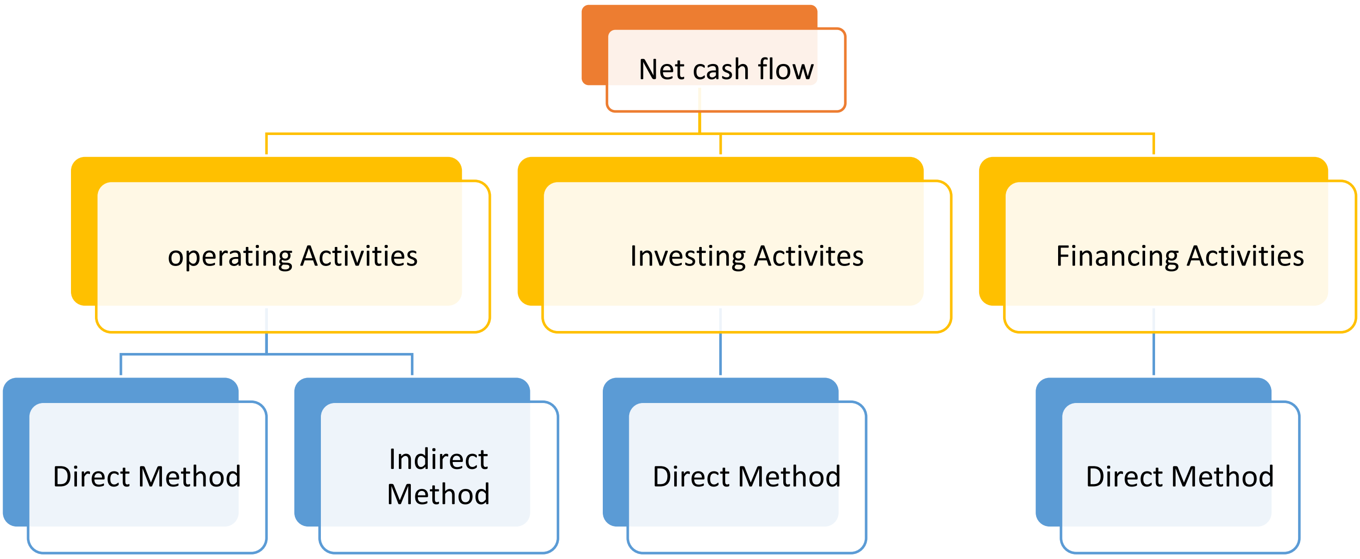
(b) cash payments to owners to acquire or redeem the entity's shares;

(c) cash proceeds from issuing debentures, loans, notes, bonds, mortgages and other short-term or long-term borrowings;

(d) cash repayments of amounts borrowed; and

(e) cash payments by a lessee for the reduction of the outstanding liability relating to a finance lease.

METHODS OF CASH FLOW STATEMENT:



Reporting Cash Flows from Operating Activities:

1. In 'Direct method' we take the gross receipts from sales, trade receivables and other operating inflows subtracted by gross payments for purchases, creditors and other expenses ignoring all non-cash items like depreciation, provisions.
2. In 'Indirect method' we start from the net profit or loss figure, eliminate the effect of any non-cash items, investing items and financing items from such profit figure i.e. all such expenses like depreciation, provisions, interest paid, loss on sale of assets etc. are added and interest received etc. are deducted. Adjustment for changes in working capital items are also made ignoring cash and cash equivalent to reach to the figure of net cash flow.

FORMAT OF CASH FLOW STATEMENT:

Cash Flow Statement of X Ltd. for the year ended March 31, 20X1 (Direct Method)

Particulars	Rs.	Rs.
Operating Activities:		
Cash received from sale of goods	xxx	
Cash received from Trade receivables	xxx	
Cash received from sale of services	xxx	xxx
Less: Payment for Cash Purchases	**xxx**	
Payment to Trade payables	xxx	
Payment to Trade expenses	xxx	

e.g. power, rent, electricity		
Payment for wages & salaries	xxx	
Payment for Income Tax	xxx	xxx
Adjustment for Extraordinary Items		xxx
Net Cash Flow from Operating Activities		xxx

Cash Flow Statement of X Ltd. for the year ended March 31, 20X1 (Indirect Method)

Particulars	Rs.	Rs.
Operating Activities:		
Closing balance of Profit & Loss Account	xxx	
Less: Opening balance of Profit & Loss Account	xxx	
Balance of P&L Account related to Current year after appropriations	xxx	
Reversal of the effects of Profit & Loss Appropriation Account	**xxx**	
Add: Provision for Income Tax	xxx	
Effects of Extraordinary Items	xxx	
Net Profit Before Tax and Extraordinary Items	xxx	
Reversal of the effects of non-cash and non-operating items	xxx	
Effects for changes in Working Capital except cash & cash equivalent	xxx	
Cash generated from operations before tax & Extraordinary Activities	xxx	
Less : Payment of Income Tax	xxx	xxx
Adjustment for Extraordinary Items		xxx
Net Cash Flow from Operating Activities		xxx

Some Important cash flow activities treatment:

Loans/Advances given and Interests earned

1. Loans and advances given and interests earned on them in the ordinary course of business are operating cash flows for financial enterprises.
2. Loans and advances given and interests earned on them are investing cash flows for non-financial enterprises.
3. Loans and advances given to subsidiaries and interests earned on them are investing cash flows for all enterprises.

4. Loans and advances given to employees and interests earned on them are operating cash flows for all enterprises.
5. Advance payments to suppliers and interests earned on them are operating cash flows for all enterprises.
6. Interests earned from customers for late payments are operating cash flows for non-financial enterprises.

Loans/Advances taken and interests paid

1. Loans and advances taken and interests paid on them in the ordinary course of business are operating cash flows for financial enterprises.
2. Loans and advances taken and interests paid on them are financing cash flows for non-financial enterprises.
3. Loans and advances taken from subsidiaries and interests paid on them are financing cash flows for all enterprises.
4. Advance taken from customers and interests paid on them are operating cash flows for non-financial enterprises.
5. Interests paid to suppliers for late payments are operating cash flows for all enterprises.
6. Interests taken as part of inventory costs in accordance with AS 16 are operating cash flows.

Investments made and dividends earned

1. Investments made and dividends earned on them in the ordinary course of business are operating cash flows for financial enterprises.
2. Investments made and dividends earned on them are investing cash flows for non-financial enterprises.
3. Investments in subsidiaries and dividends earned on them are investing cash flows for all enterprises.

Dividends Paid are financing cash outflows for all enterprises.

Income Tax

1. Tax paid on operating income is operating cash outflows for all enterprises
2. Tax deducted at source against income are operating cash outflows if concerned incomes are operating incomes and investing cash outflows if the concerned incomes are investment incomes, e.g. interest earned.
3. Tax deducted at source against expenses are operating cash inflows if concerned expenses are operating expenses and financing cash inflows if the concerned expenses are financing expenses, e.g. interests paid.

Insurance claims received

a. Insurance claims received against loss of stock or loss of profits are extraordinary operating cash inflows for all enterprises.

b. Insurance claims received against loss of fixed assets are extraordinary investing cash inflows for all enterprises.

Non-Cash transactions

Investing and financing transactions that do not require the use of cash or cash equivalents, should be excluded from a cash flow statement.

e.g.

a. Issue of bonus shares,

b. The acquisition of an enterprise by means of issue of shares; and

c. The conversion of debt to equity.

Extraordinary Items AS 3 requires separate disclosure of extraordinary cash flows, classifying them as cash flows from operating, investing or financing activities, as may be appropriate.

Acquisitions and Disposals of Subsidiaries and Other Business Units:

The aggregate cash flows arising from acquisitions and from disposals of subsidiaries or other business units should be presented separately and classified as investing activities.

Reporting Cash Flows on a Net Basis:

Generally, enterprises should report separately major classes of gross cash receipts and gross cash payments arising from operating, investing and financing activities. But, the following activities may be reported on net basis.

a. cash receipts and payments on behalf of customers when the cash flows reflect the activities of the customer rather than those of the enterprise;

Examples:

i) The acceptance and repayment of demand deposits by a bank;

ii) Funds held for customers by an investment enterprise; and

iii) Rents collected on behalf of, and paid over to, the owners of properties.

b. cash receipts and payments for items in which the turnover is quick, the amounts are large, and the maturities are short.

Examples:

i) Principal amounts relating to credit card customers;and

ii) The purchase and sale of investments by an investment entity;

Foreign Currency Cash Flows:

1. The foreign currency monetary assets (e.g. balance with bank, debtors etc.) and liabilities (e.g. creditors) are initially recognised by translating them into reporting currency by the rate of exchange transaction date. On the balance sheet date, these are restated using the rate of exchange on the balance sheet date. The difference in values is exchange gain/loss. The exchange gains and losses are recognised in the statement of profit and loss.
2. The exchange gains/losses in respect of cash and cash equivalents in foreign currency (e.g. balance in foreign currency bank account) are recognised by the principle aforesaid, and these balances are restated in the balance sheet in reporting currency at rate of exchange on balance sheet date. The change in cash or cash equivalents due to exchange gains and losses are however not cash flows. This being so, the net increases/decreases in cash or cash equivalents in the cash flow statements are stated exclusive of exchange gains and losses. The resultant difference between cash and cash equivalents as per the cash flow statement and that recognised in the balance sheet is reconciled in the note on cash flow statement.

NOTE: If any cash flow occurred in between cash & cash equivalent components, It should be ignored in cash flow statement.

Differences between AS 3 & Ind AS 7

AS 3	Ind AS 7
Existing AS 3 is not mandatory for Small and Medium Sized Companies, as defined in the Notification. However, it encourages such entities to comply with the standard.	Ind AS 7 does not offer any exclusion with regard to its applicability for certain concerns. All Ind AS compliant entities are required to prepare Cash Flow Statement.
Repayment of overdraft as demand is silent in existing AS 3.	Ind AS 7 specifically includes bank overdrafts which are repayable on demand as a part of cash and cash equivalents.
AS 3 uses the term “Reporting Currency”	Ind AS 7 uses the term “functional currency” instead of “Reporting Currency”.
AS 3 does not deal with cash flows arising from foreign subsidiaries.	Ind AS 7 deals with translation of cash flows arising from foreign subsidiaries.
AS 3 does not contain any requirement in the treatment of cash payments to manufacture or acquire assets held for rental to others and subsequently held for sale in the ordinary	Ind AS 7 requires the treatment of cash payments to manufacture or acquire assets held for rental to others and subsequently held for sale in the ordinary course of business as cash

course of business as cash flows from operating activities.	flows from operating activities. Further, treatment of cash receipts from rent and subsequent sale of such assets as cash flow from operating activity is also provided is also provided.
	Ind AS 7 provides some new examples of cash flows from financing activities like: **(i)** Cash payments to the owners to acquire or redeem entity's shares. **(ii)** Cash receipts from mortgages **(iii)** Cash payments made by lessee, for reduction of the outstanding liability, in a finance lease.
AS 3 is silent in adjusting profit or loss for the effects of: undistributed profits of associates, and non-controlling interests.	Under Ind AS 7, the net cash flow from operating activities, using the indirect method, is determined by adjusting profit or loss for the effects of: undistributed profits of associates, and non-controlling interests
AS 3 requires classification under cash flow from investing activities.	Under Ind AS 7, cash flows arising from changes in ownership interests in a subsidiary that do not result in a loss of control shall be classified as cash flows from financing activities.
AS 3 requires cash flows associated with extraordinary activities to be separately classified as arising from operating, investing and financing activities.	Ind AS 7 does not have any such requirement.
AS 3 does not have any requirements in cash flows arising from changes in ownership interests in a subsidiary.	Ind AS 7 requires to classify cash flows arising from changes in ownership interests in a subsidiary that do not result in a loss of control as cash flows from financing activities.

PROBLEMS EXCLUSIVE FROM CMA SOURCE

Problem No.1

M Ltd. had a cash balance of Rs.1,50,000 as on 30.09.2021. On 15.10.2021, M Ltd. used the cash balance to purchase a short-term bank deposit with a maturity of three months. How should this be shown in the statement of cash flow to be prepared for the quarter ended 31.12.2021?

(Illustration 1)

Problem No.2

Classify the following cash receipts and payments of a furniture company into cash from operating, investing and financing activities:

a. Receipt from sale of furniture
b. Purchases of furniture from various suppliers
c. Wages paid
d. Advertisement expenses paid
e. Credit sales of furniture
f. Misc. charges received from customers for repairs of furniture
g. Warranty claims received from the suppliers
h. Loss due to decrease in market value of the closing stock of furniture
i. Payment to suppliers of furniture
j. Depreciation on furniture of sales showrooms
k. Interest paid on bank loan
l. Profit on sale of equipment, in exchange of new equipment
m. Advance received from customers
n. GST paid
o. Equity dividend paid for the current financial year

(Illustration 2)

Problem No.3

Classify the following transactions into cash flow from operating, investing and financing activities in respect of a pharmaceutical company:

a. Issued equity shares
b. Bonus shares issued
c. Right shares issued
d. Purchased 90% shares of subsidiary company

e. Dividend received from subsidiaries

f. Dividend received from investment in other companies

g. Payment of license fees

h. Royalty received from the goods patented

i. Rent received from the letting out of free space

j. Interest received on loans to Y Ltd.

k. Preference Dividend paid

l. Interest paid on security deposits

m. Acquired the assets of a company through issue of equity shares

n. Purchased goodwill

o. Interim dividends paid

p. Sale of investment in subsidiary

(Illustration 3)

Problem No.4

On 01.01.2022, P Ltd., an Indian company, bought goods from USA for $1000 to be sold within India. The exchange rate on that date was Rs.76 = 1$. On 31.03.2022, the exchange rate moved to Rs.78 = 1 $. How will you report the above in the Cash Flow Statement?

(Illustration 4)

Problem No.5

X Ltd. provides you the following information of its cash inflow and outflow for the financial year 2021-22:

a. Dividend paid to equity and preference shareholders Rs.50,000

b. Interest paid Rs.10,000

c. Interest received on loan Rs. 20,000

d. Dividend received from Y Ltd. Rs.15,000

How will you classify the above in the Cash Flow Statement of X Ltd. if

(i) X Ltd. is a financial institution and

(ii) X Ltd. is a manufacturing concern.

(Illustration 5)

Problem No.6

B Ltd., a manufacturing concern, invested Rs.3,00,000 in a five-year bond with an effective interest rate of 10% for 4 years. It received Rs.4,40,000 on maturity. During the four years it recognised the interest income based on the effective interest rate in its income statement. How will you treat the transactions over four years and on maturity?

(Illustration 6)

Problem No.7

A Ltd. paid an advance tax amounting to Rs.3,65,000 out of which Rs.15,000 is relating to a short-term capital gain on sale of securities. How will A Ltd. report the payment of advance tax in its Cash Flow Statement?

(Illustration 7)

Problem No.8

From the given information prepare cash flow statement under both Direct and Indirect method.

Balance Sheet as at 31-12-2020 and 31- 12- 2021

(Rs. in thousands)

Ref No.		Particulars	Note No.	31.12.2021	31.12.2020
I		**EQUITY AND LIABILITIES**			
	1	**Equity**			
		(a) Equity Share capital		1,500	1,250
		(b) Reserve & Surplus		3,410	1,380
	2	**Liability**		NIL	
		Non-current liabilities		NIL	
		(a) Long-term borrowings		1,110	1,040
		Current Liabilities			
		(a) Trade payables		150	1,890
		(b) Other current liabilities		230	100
		(c) Short-term provisions		400	1,000
		Total		6,800	6,660
II		**ASSETS**			
	1	**Non-current assets**			
		(a) PPE		730	850
		(b) Non-current investments		2,500	2,500
	2	**Current assets**			
		(a) Current investments		670	135

		(b) Inventories		900	1,950
		(c) Trade receivables		1,700	1,200
		(d) Cash and cash equivalents		200	25
		Total		6,800	6,660

Notes on Accounts **(Rs. in thousands)**

1. Other Current Liabilities	**31.12.2021**	**31.12.2020**
Interest Payable	230	100
Total	230	100
2. Short Term Provision	**31.12.2021**	**31.12.2020**
Income Tax Payable	400	1,000
Total	400	1,000
3. PPE	**31.12.2021**	**31.12.2020**
Fixed Assets at cost	2,180	1,910
Less: Accumulated Depreciation	1,450	1,060
Total	730	850
4. Other Current Assets	**31.12.2021**	**31.12.2020**
Interest Receivable	100	-
Total	100	-

Statement of profit and Loss for the year ended 31 – 12 – 2021

	(Rs. in thousands)
Sales	30,650
Cost of sales	(26,000)
Gross profit	4,650
Depreciation	(450)
Administration and selling expenses	(910)
Interest expenses	(400)
Interest income	300
Dividend income	200
Foreign exchange loss	(40)
Net profit before taxation and extraordinary item	3,350
Extraordinary item - Insurance proceeds from earthquake disaster settlement	180
Net profit after extraordinary item	3,530

Income-tax	(300)
Net profit	3,230

Additional information (Rs. in thousands):

i. An amount of Rs. 250 was raised from the issue of share capital and a further Rs. 250 was raised from long-term borrowings.

ii. Interest expense was Rs. 400 of which Rs. 170 was paid during the period. Rs.100 relating to interest expenses of the prior period was also paid during the period.

iii. Dividends paid were Rs.1,200.

iv. Tax deducted at source on dividends received (included in the tax expenses of Rs.300 for the year) amounted to Rs.40

v. During the period, the enterprise acquired fixed assets for Rs.350. The payment was made in cash.

vi. Plant with original cost of Rs.80 and accumulated depreciation of Rs.60 was sold for Rs.20.

vii. Foreign exchange loss of Rs.40 represents reduction in the carrying amount of a short-term investment in foreign currency designated bonds arising out of a change in exchange rate between the date of acquisition of the investments and the balance sheet date.

viii. Sundry debtors and sundry creditors include amounts relating to credit sales and credit purchases only. **(Illustration 13)**

Problem No.9

The following is the income statement XYZ Company for the year 2020 – 21.

			(Rs.)
Sale			1,62,700
Add: Equity in ABC company's earning			6,000
			1,68,700
Expenses			
Cost of goods sold		89,300	
Salaries		34,400	
Depreciation		7,450	
Insurance		500	
Research and development		1,250	
Patent amortization		900	
Interest		10,650	
Bad debts		2,050	
Income tax:			

Current	6,600		
Deferred	1,550		
Total expenses		8,150	1,54,650
Net income			14,050

Additional information is:

1. 70% of gross revenue from sales were on credit.
2. Merchandise purchases amounting to Rs. 92,000 were on credit.
3. Salaries payable totalled Rs. 1,600 at the end of the year.
4. Amortisation of premium on bonds payable was Rs.1,350.
5. No dividends were received from the other company.
6. XYZ Company declared cash dividend of Rs. 4,000.
7. Changes in Current Assets and Current Liabilities were as follows:

	Increase (Decrease) Rs.
Cash	500
Marketable securities	1,600
Accounts receivable	(7,150)
Allowance for bad debt	(1,900)
Inventory	2,700
Prepaid insurance	700
Accounts payable (for merchandise)	5,650
Salaries payable	(2,050)
Dividends payable	(3,000)

Prepare a statement showing the amount of cash flow from operations. **(Illustration 11)**

Problem No.10

From the following figures of LK Ltd. prepare a Cash Flow Statement:

Particulars	**31.03.2020**	**31.03.2021**
Equity and Liabilities	**(Rs.)**	**(Rs.)**
Equity Share Capital	12,00,000	16,00,000
10% Preference Share Capital	4,00,000	2,80,000
Capital Reserve		40,000
General Reserve	6,80,000	8,00,000
Profit and Loss Account	2,80,000	4,04,000

9% Debentures	4,00,000	2,80,000
Current Liabilities	4,80,000	5,36,000
Provision for Tax	3,60,000	3,40,000
	38,00,000	42,80,000
Fixed Assets	32,00,000	38,00,000
Less Depreciation	9,20,000	11,60,000
	22,80,000	26,40,000
Investments	4,00,000	3,20,000
Cash	10,000	10,000
Other Current Assets	11,10,000	13,10,000
	38,00,000	42,80,000

Additional information:

1. The company sold one fixed asset for Rs.1,00,000 the cost of which was Rs. 2,00,000 and the depreciation provided on it was Rs. 80,000.
2. The company also decided to right off another fixed asset costing Rs. 56,000 on which depreciation amounting to Rs. 40,000 has been provided.
3. Depreciation on fixed assets provided Rs.3,60,000.
4. Company sold some investment at a profit of Rs. 40,000, which was credited to Capital Reserve.
5. Debentures and preference share capital where redeemed at 5% premium.
6. Company decided to value stock at cost, whereas previously, the practice was to Value stock at cost less 10%. The stock according to book on 31st March 2020 was Rs. 2,16,000. The stock as on 31st March 2021 was correctly valued at Rs. 3,00,000. **(Illustration 15)**

PROBLEMS FROM CA SOURCE FOR PRACTICE

PROBLEM1

Classify the following activities as (a) Operating Activities, (b) Investing Activities, (c) Financing Activities (d) Cash Equivalents.

(a) Purchase of Machinery.

(b) Proceeds from issuance of equity share capital

(c) Cash Sales.

(d) Proceeds from long-term borrowings.

(e) Cheques collected from Trade receivables.

(f) Cash receipts from Trade receivables.

(g) Trading Commission received.

(h) Purchase of investment.

(i) Redemption of Preference Shares.

(j) Cash Purchases.

(k) Proceeds from sale of investment

(l) Purchase of goodwill.

(m) Cash paid to suppliers.

(n) Interim Dividend paid on equity shares.

(o) Wages and salaries paid.

(p) Proceed from sale of patents.

(q) Interest received on debentures held as investment.

(r) Interest paid on Long-term borrowings.

(s) Office and Administration Expenses paid

(t) Manufacturing Overheads paid.

(u) Dividend received on shares held as investments.

(v) Rent Received on property held as investment.

(w) Selling and distribution expense paid.

(x) Income tax paid

(y) Dividend paid on Preference shares.

(z) Underwritings Commission paid.

(aa) Rent paid.

(bb) Brokerage paid on purchase of investments.

(cc) Bank Overdraft

(dd) Cash Credit

(ee) Short-term Deposits

(ff) Highly liquid Marketable Securities (without risk of change in value)

(gg) Refund of Income Tax received. **(ILLUSTARATION-1-SM)**

PROBLEM 2

Classify the following activities as per AS 3 Cash Flow Statement:

(i) Interest paid by financial enterprise

(ii) Tax deducted at source on interest received from subsidiary company

(iii) Deposit with Bank for a term of two years

(iv) Insurance claim received towards loss of machinery by fire

(v) Bad debts written off **(ILLUSTARATION-3-SM)**

PROBLEM 3:

Intelligent Ltd., a non-financial company has the following entries in its Bank Account. It has sought your advice on the treatment of the same for preparing Cash Flow Statement.

(i) Loans and Advances given to the following and interest earned on them:

(1) to suppliers

(2) to employees

(3) to its subsidiaries companies

(ii) Investment made in subsidiary Smart Ltd. and dividend received

(iii) Dividend paid for the year

(iv) TDS on interest income earned on investments made

(v) TDS on interest earned on advance given to suppliers

(vi) Insurance claim received against loss of fixed asset by fire

Discuss in the context of AS 3 Cash Flow Statement (**ILLUSTARATION-1-SM-MAIN CHAPTER)**

PROBLEM 4

X Ltd. purchased debentures of Rs. 10 lacs of Y Ltd., which are redeemable within three months. How will you show this item as per AS 3 while preparing cash flow statement for the year ended on 31st March, 20X1? **(ILLUSTARATION-2-SM)**

PROBLEM 5

The following summary cash account has been extracted from the company's accounting records:

Summary Cash Account **(Rs. In '000)**

Particulars	Amount (Rs.)	Amount (Rs.)
Balance at 1.4.2014		35
Receipts from customers		2,783
Issue of shares		300
Sale of fixed assets		128
		3,246
Payments to suppliers	2,047	
Payments for fixed assets	230	
Payments for overheads	115	
Wages and salaries	69	
Taxation	243	
Dividends	80	
Repayments of bank loan	250	**(3034)**
Balance at 31.3.2015		**212**

Prepare Cash Flow Statement of this company Hills Ltd. for the year ended 31st March, 2015 in accordance with AS-3 (Revised).

The company does not have any cash equivalents. **(Illustration-4-Main Chapter)**

Problem 6

Prepare cash flow from investing activities as per AS 3 of M/S Subham creative Limited for the year ended 31.3.2019.

Particulars	Amount Rs.
Machinery acquired by issue of shares at face value	2,00,000
Claim received for loss of machinery in earth quake	55,000
Unsecured loans given to associates	5,00,000
Interest on loan received from associate company	70,000
Pre-acquistion dividend received on investment made	52,600
Debenture interest paid	1,45,200
Term loan repaid	4,50,000
Interest received on investment (TDS of Rs.8200 was deducted on the above interest)	73,800

Purchased debentures of X Ltd. On 1st December, 2018 which are redeemable with in 3 months	3,00,000
Book value of plant & Machinery sold(loss incurred Rs.9,600)	90,000

(Nov 2019 Question Paper-1(A))

Problem7

Given below are the relevant extracts of the Balance Sheet and the Statement of Profit and Loss of ABC Ltd. along with additional information:

		Particulars	Notes	31.3.20X1 (Rs. in lakhs)	31.3.20X0 (Rs. in lakhs)
		Equity and Liabilities			
1		**Current liabilities**			
	(a)	Trade Payables		250	230
	(b)	Short term Provisions	1	200	180
	(c)	Other current liabilities	2	70	50
		Assets			
1		**Current assets**			
	(a)	Inventories		200	180
	(b)	Trade Receivables		400	250
	(c)	Other current assets	3	195	180

Statement of Profit and Loss of ABC Ltd. for the year ended 31st March, 20X1

	Particulars	Notes	Rs. in lakhs
	Revenue from operations		4,150
	Other income	4	100
	Total income (I + II)		4,250
	Expenses:		
	Purchases of Stock-in-Trade		2,400
	Change in inventories of finished goods		(20)
	Employee benefits expense		800
	Depreciation expense		100
	Finance cost	5	60

	Other expenses		200
	Total expenses		3,540
	Profit before tax (**III – IV**)		710
	Tax expense: Current tax		200
	Profit for the year from continuing operations		510

Appropriations

Balance of Profit and Loss account brought forward	50
Transfer to general reserve	200
Dividend paid	330

Notes to accounts:

		20X0-20X1 (Rs. in lakhs)	2009-20X0 (Rs. in lakhs)
1	Short term Provisions:		
	Provision for Tax	200	180
2	Other current liabilities:		
	Outstanding wages	50	40
	Outstanding expenses	20	10
	Total	70	50
3	Other current assets:		
	Advance tax	195	180
4	Other income:		
	Interest and dividend	100	
5	Finance cost:		
	Interest	60	

Compute cash flow from operating activities using both direct and indirect method.

(ILLUSTRATION-10-MAIN CHAPTER)

PROBLEM 8

Prepare cash flow statement of M/s MNT Ltd. for the year ended 31st March, 20X1 with the help of the following information:

1. Company sold goods for cash only.

2. Gross Profit Ratio was 30% for the year, gross profit amounts to Rs. 3,82,500.

3. Opening inventory was lesser than closing inventory by Rs. 35,000.

4. Wages paid during the year Rs. 4,92,500.

5. Office and selling expenses paid during the year Rs. 75,000.

6. Dividend paid during the year Rs. 30,000.

7. Bank loan repaid during the year Rs. 2,15,000 (included interest Rs. 15,000).

8. Trade payables on 31st March, 20X0 exceed the balance on 31st March, 20X1 by Rs. 25,000.

9. Amount paid to trade payables during the year Rs. 4,60,000.

10. Tax paid during the year amounts to Rs. 65,000 (Provision for taxation as on 31.03.20X1 Rs.45,000).

11. Investments of Rs. 7,00,000 sold during the year at a profit of Rs. 20,000.

12. Depreciation on fixed assets amounts to Rs. 85,000.

13. Plant and machinery purchased on 15th November, 20X0 for Rs. 2,50,000.

14. Cash and Cash Equivalents on 31st March, 20X0Rs. 2,00,000.

15. Cash and Cash Equivalents on 31st March, 20X1Rs. 6,07,500. **(Illustration-5-Main Chapter)**

PROBLEM 9

Ryan Ltd provides you the following information at the year-end, March 31, 20X1:

	Rs.	Rs.
Sales		6,98,000
Cost of Goods Sold		(5,20,000)
		1,78,000
Operating Expenses (including Depreciation Expense of Rs. 37,000)		1,47,000
		31,000
Other Income / (Expenses):		
Interest Expense paid	(23,000)	
Interest Income received	6,000	
Gain on Sale of Investments	12,000	
Loss on Sale of Plant	(3,000)	(8,000)
Income tax		(7,000)
		16,000

Information available:

	31st March 20X1 Rs.	31st March 20X0 Rs.
Plant	7,15,000	5,05,000
Less: Accumulated Depreciation	(1,03,000)	(68,000)
	6,12,000	4,37,000
Investments (Long term)	1,15,000	1,27,000
Inventory	1,44,000	1,10,000
Trade receivables	47,000	55,000
Cash	46,000	15,000
Prepaid expenses	1,000	5,000
Share Capital	4,65,000	3,15,000
Reserves and surplus	1,40,000	1,32,000
Bonds	2,95,000	2,45,000
Trade payables	50,000	43,000
Outstanding liabilities	12,000	9,000
Income taxes payable	3,000	5,000

Analysis of selected accounts and transactions during 20X0-X1

1. Purchased investments for Rs. 78,000.
2. Sold investments for Rs. 1,02,000. These investments cost Rs. 90,000.
3. Purchased plant assets for Rs. 1,20,000.
4. Sold plant assets that cost Rs.10,000 with accumulated depreciation of Rs. 2,000 for Rs. 5,000.
5. Issued Rs. 1,00,000 of bonds at face value in an exchange for plant assets on 31st March, 20X1.
6. Repaid Rs. 50,000 of bonds at face value at maturity.
7. Issued 15,000 shares of Rs. 10 each.
8. Paid cash dividends Rs. 8,000.

Prepare Cash Flow Statement as per AS-3 (Revised), using indirect method.

(ILLUSTRATION-6-MAIN CHAPTER)

PROBLEM 10

The balance sheets of Sun Ltd. for the years ended 31st March 20X1and 20X0 were summarised as:

	20X1 (Rs.)	20X0 (Rs.)
Equity Share Capital	60,000	50,000
Reserves:		

Profit and Loss Account	5,000	4,000
Current Liabilities:		
Trade payables	4,000	2,500
Taxation	1,500	1,000
Other current liabilities (Dividend payable)	-	1,000
	70,500	**58,500**
Fixed Assets (at W.D.V.)		
Premises	10,000	10,000
Fixtures	17,000	11,000
Vehicles	12,500	8,000
Current Assets:		
Short-term investments	2,000	1,000
Inventory	17,000	14,000
Trade receivables	8,000	6,000
Bank and Cash	4,000	8,500
	70,500	**58,500**

The profit and loss account for the year ended 31st March, 20X1 disclosed

	Rs.
Profit before tax	4,500
Taxation	(1,500)
Profit after tax	3,000
Declared dividends	(2,000)
Retained profit	1,000

Further information is available

Particulars	**Fixtures (Rs.)**	**Vehicles (Rs.)**
Depreciation for year	1,000	2,500
Disposals:		
Proceeds on disposal	—	1,700
Written down value	—	(1,000)
Profit on disposal		700

Prepare a Cash Flow Statement for the year ended 31st March, 20X1.

(ILLUSTRATION-7-MAIN CHAPTER)

Problem 11

How will you disclose following items while preparing Cash Flow Statement of Gagan Ltd. as per AS-3 for the year ended 31st March, 20X2?

(i) (i) 10% Debentures issued: As on 01-04-20X1 Rs. 1,10,000 As on 31-03-20X2 Rs. 77,000

(ii) Debentures were redeemed at 5% premium at the end of the year. Premium was charged to the Profit & Loss Account for the year.

(iii) Unpaid Interest on Debentures: As on 01-04-20X1 Rs. 275 as on 31-03-20X2 Rs. 1,175

(iv) Debtors of Rs. 36,000 were written off against the Provision for Doubtful Debts A/c during the year.

(v) 10% Bonds (Investments): As on 01-04-20X1 Rs. 3,50,000 , As on 31-03-20X2 Rs. 3,50,000

(vi) Accrued Interest on Investments: As on 31-03-20X2 Rs. 10,500

(PRACTICAL QUESTION-2-SM)

PROBLEM 12

From the following Balance Sheet and information, prepare Cash Flow Statement of Rani Ltd. for the year ended 31st March, 2011.

Name of the Company: Rani Ltd

Balance Sheet as at : 31st March, 2011 and 31st March, 2010

			Particulars	Notes No.	Figures as at the end of current reporting period 31-03-11	Figures as at the end of the previous reporting period 31.03.10
			1	**2**	**3**	**4**
			EQUITY AND LIABILITIES:			
1			Shareholder's funds			
	A		Share capital	**1**	6,00,000	7,00,000
	B		Reserves and Surplus	**2**	4,20,000	3,00,000
2			**Non-current liabilities:**			
	A		Long term borrowings (9 % debentures)	**3**	2,00,000	-
3			**Current liabilities:**			
	A		Trade Payables		1,15,000	1,10,000
	B		Other current liabilities	**4**	30,000	80,000

	C		Short term provision (provision for tax)		95,000	60,000
			Total		**14,60,000**	**12,50,000**
1			**ASSETS:**			
			Non-current assets			
	A		Property, plant and Equipment	**5**	9,15,000	7,00,000
	B		Non-Current Investments		50,000	80,000
2			**Current assets**			
	A		Inventories		95,000	90,000
	B		Trade receivables		2,50,000	2,25,000
	C		Cash and Cash equivalents		50,000	90,000
	D		Other Current assets		1,00,000	65,000
			Total		**14,60,000**	**12,50,000**

Notes to accounts:

Particulars	31st March, 20X1	31st March, 20X0
1.Share capital- Equity share capital	6,00,000	5,00,000
10% Redeemable Preference share capital	-	2,00,000
2.Reserves and Surplus		
Capital redemption reserve	1,00,000	-
Capital reserve	70,000	-
General reserve	1,50,000	2,50,000
Profit and Loss account	1,00,000	50,000
3.Long term borrowings		
9% Debentures	2,00,000	-
4.Other current liabilities		
Dividend payable	-	60,000
Liabilities for expenses	30,000	20,000
5.Property, plant and equipment		
Plant and machinery	7,65,000	5,00,000

Land and building	1,50,000	2,00,000
Net carrying value	**9,15,000**	**7,00,000**

(vi) A piece of land has been sold out for Rs.1,50,000 (Cost – Rs.1,20,000) and the balance land was revalued. Capital Reserve consisted of profit on revaluation of land.

(vii) On 1st April, 20X0 a plant was sold for Rs.90,000 (Original Cost – Rs.70,000 and W.D.V. – Rs.50,000) and Debentures worth Rs.1 lakh were issued at par as part consideration for plant of Rs.4.5 lakhs acquired.

(viii) Part of the investments (Cost – Rs.50,000) was sold for Rs.70,000.

(ix) Pre-acquisition dividend received Rs.5,000 was adjusted against cost of investment.

(x) Interim dividend was declared and paid @ 15% during the current year.

(xi) Income-tax liability for the current year was estimated at Rs.1,35,000.

(xii) Depreciation @ 15% has been charged on Plant and Machinery but no depreciation has been charged on Building. **(PRACTICAL QUESTION-4-SM)**

PROBLEM 13

Following information was extracted from the books of S Ltd. For the year ended 31st March 2020.

(12M)

i) Net profit before taking into account income tax and after taking into account the following items was Rs. 30 Lakhs.

- Depreciation on property, Plant & Equipment Rs. 7,00,000
- Discount on issue of debentures written off Rs. 45,000
- Interest on debentures paid Rs. 4,35,000
- Investment of Book value Rs. 3,50,000 sold for Rs. 3,75,000
- Interest received on Investments Rs. 70,000

ii) Income tax paid during the year Rs. 12,80,000

iii) Company issued 60,000 equity Shares of Rs. 10 each at a premium of 20% on 10th April 2019.

iv) 20,000, 9% Preference Shares of Rs. 100 each were redeemed on 31st March 2020 at a premium of 5%

v) Dividend paid during the year amounted to Rs. 11 Lakhs (including dividend distribution tax)

vi) A new Plant Costing Rs. 7 Lakhs was purchased in part exchange of an old plant on 1st January 2020. The book value of the old plant was Rs. 8 Lakhs, but the vendor took over the old plant at a value of Rs. 6 Lakhs only. The balance amount was paid to vendor through cheque on 30th March 2020.

vii) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31-03-2020 was Rs. 14,76,000. The inventory on 31-03-2019 was correctly valued at Rs. 13,50,000.

viii) Current Assets and Current Liabilities in the beginning and at the end of year 2019 – 2020 were as:

Particulars	**As on 1st April 2019 (Rs.)**	**As on 31st March 2020 (Rs.)**
Inventory	13,50,000	14,76,000
Trade Receivables	3,27,000	3,13,200
Cash & Bank Balances	2,40,700	3,70,500
Trade Payables	2,84,700	2,87,300
Outstanding Expenses	97,000	1,01,400

You are required to prepare a Cash Flow Statement for the year ended 31st March 2020 as per AS 3 (revised) using the indirect method. **(JAN 2021 QUESTION PAPER-4(B))**

THEORETICAL QUESTIONS

Multiple Choice Questions

1. Which of the following items would be subtracted from net income when using the indirect method of calculating cash flows provided by operating activities?

a. Depreciation expense

b. Repayment of bonds payable

c. A gain on the sale of land

d. A loss on the sale of equipment

2. Which of the following would be considered a cash-flow item from a “financing” activity?

a. A cash outflow to the government for taxes

b. A cash outflow to repurchase the firm’s own common stock

c. A cash outflow to lenders as interest

d. A cash outflow to purchase bonds issued by another company

3. The method for presenting Net cash provided by operating activities that starts with net income and adjusts it for items that affected reported net income but that did not affect cash is called as___.

a. Direct method

b. Working capital method

c. Indirect method

d. Cost-benefit method

4. Under which activites cash paid for preferred stock dividends should be shown on the statement of cash flows?

a. Investing activities

b. Financing activities

c. Noncash investing and financing activities

d. Operating activities

5. Which of the following would not be considered a cash flow from “operating” activities?

a. Payments for the inventory

b. Collection from customers

c. Tax payments

d. Payment of debt principle

6. Under which of the following, a business must generate positive net cash flow for it to survive in the long run?

a. Investing activities

b. Financing activities

c. Operating activities

d. Non cash activities

7. Depreciation is added back to profit when arriving at the cash flow from operating activities as___________.

a. Depreciation is a non-cash expenditure

b. Depreciation does not affect profit

c. Depreciation only affects the balance sheet, not the profit and loss account

d. None of Above

8. Which of the following would not represent the cash outflows for the business?

a. Purchase of building for cash

b. The sale of land for cash

c. Retirement of long-term debt

d. The payment of cash for dividends

9. The statement of cash flows does not include cash inflows and outflows for which of the following activities?

a. Financing activities

b. Investing activities

c. Operating activities

d. Revenue activities

10. Sale of copyright is concerned with cash flow from________

a. Operating activities

b. Financing activities

c. Investing activities

d. Revenue activities

[Answer: 1-C; 2-B; 3-C; 4-B; 5-D; 6-C; 7-A; 8-B; 9-D; 10-C]

State True or False

1. Dividend received by enterprise other than financial enterprise is shown as cash flow from investing activity.

2. Cash collection from customer is shown as a part of calculation of cash flow from operating activities under direct method.

3. Increase in the amount of bills receivable amounts to increase in cash flow from operating activities.

4. Payment of income tax is classified under cash flow from financing activity.
5. Interest paid by an investment company will come under cash flow from operating activity.

[Answer: 1.False; 2.True; 3.False; 4.False; 5.True]

Fill in the blanks:

1. For a finance company interest income is a Cash Flow from______________.
2. Investing and financing transactions that________________require the use of cash or cash equivalents shall be excluded from a statement of cash flows.
3. Income from dividend and interest is a part of________________.
4. For a company other than a finance company payment of interest is a_____________activity.
5. _____________ are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

[Answer: 1.Operating Activity; 2.do not; 3.Investing Activity; 4.Financing; 5.Cash equivalents]

Numerical Multiple-Choice Questions

1. Net profit for the year Rs.15,000, interest received in advance on 1st January 2021 Rs.2,000 and 31st December 2021 Rs.3,000, cash from operation will be –
   A. Rs.16,000
   B. Rs.22,000
   C. Rs.13,000
   D. Rs.15,000
2. X Ltd. purchased machinery of Rs.10,00,000 issuing a cheque of Rs.2,50,000 and 105 Debentures of Rs.7,50,000. In the cash flow statement, the transaction will be shown as______________.
   A. Outflow under investing activity Rs.10,00,000, inflow under financing activity as receipt for debentures Rs.7,50,000
   B. Outflow under investing activity Rs.2,50,000
   C. Inflow of Rs.7,50,000 as financing activity.
   D. None of the above
3. Given salary expenses Rs.40,000, Outstanding in the beginning of the year Rs.5,000 and outstanding at the end of the year Rs.10,000. Cash outflow on salary will be______.
   A. Rs.55,000
   B. Rs.45,000
   C. Rs.35,000

D. Rs.15,000

4. If the net profits earned during the year is Rs.50,000 and the amount of debtors in the beginning and end of the year is Rs.10,000 and Rs.20,000 respectively, then the cash from operating activities will be equal to_.

A. Rs.30,000

B. Rs.40,000

C. Rs.50,000

D. Rs.60,000

5. If the net profits earned during the year is Rs.50,000 and the bills receivables have decreased by Rs.10,000 during the year then the cash flow from operating activities will be equal to___.

A. Rs.30,000

B. Rs.40,000

C. Rs.50,000

D. Rs.60,000

[Answer: 1-A; 2-B; 3-C; 4-B; 5-B]

Short Essay Type Questions:

9. State the benefits of cash flow information.

10. How will you treat interest and dividend in cash flow statement?

11. How will you treat taxes on income in cash flow statement?

12. How will you treat foreign currency cash flow in cash flow statement?

Essay Type Questions:

1. State the difference between Ind AS 7 and AS 3 with respect to preparation and presentation of cash flow statement.

10. BANKING COMPANIES

Introduction:

In an economy, banks play an important role in channelizing the savings of surplus generating units (i.e., households) into investments by deficit generating units (i.e., businesses). These financial institutions manage and maintain the flow of money in the economy and further assist in payment and settlements through various services. In short, today banks are the key to an efficient economic system.

Meaning of Banking

According to Section 5(b) of the Banking Regulation Act, 1949, 'banking' means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawal by cheque, draft, order or otherwise.

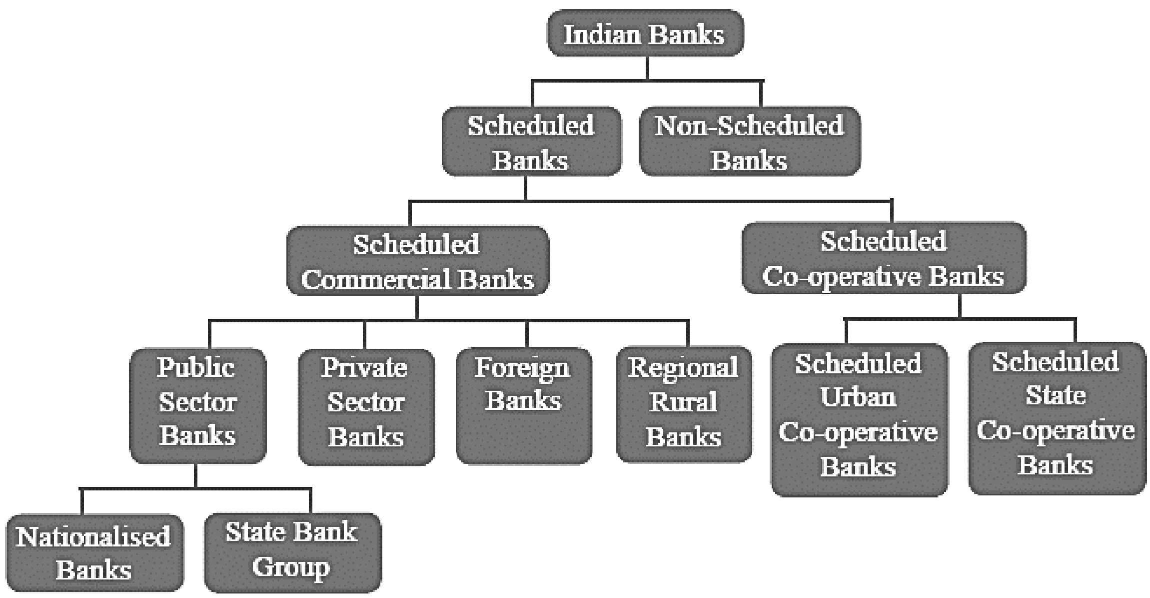
Meaning of Banking Companies

According to Section 5(c) of the Banking Regulation Act, 1949, a 'banking company' means any company which transacts the business of banking in India.

As per the Explanation to Section 5(c) as above, any company which is engaged in the manufacture of goods or carries on any trade and which accepts deposits of money from the public merely for the purpose of financing its business as such manufacturer or trader shall not be deemed to transact the business of banking within the meaning of this clause.

Types of Banks in India

The banking structure in India has many layers and sub-layers as follows:



Banking Structure in India

Banks are broadly classified as Scheduled and Non-scheduled Banks.

- Scheduled Banks are those banks which are listed in Schedule II of RBI Act, 1934. In other words, the banks which follow the guidelines of the Schedule II of RBI Act, 1934 are known as Scheduled Banks. The bank's paid-up capital and raised funds must be at least Rs.5 to qualify as a scheduled bank. Scheduled banks are liable for low-interest loans from the Reserve Bank of India and membership in clearinghouses.
- On the other hand, the banks which are not listed in the Schedule II of RBI Act, 1934, is called Non-scheduled banks. These banks are not allowed to deal in foreign exchange. Non- scheduled banks are also known as Local Area Bank.
- Scheduled banks are further classified into Commercial Banks and Co-operative Banks. The Commercial Banks are those financial institutions which accept deposit and provide services like loans, credit, opening bank accounts, locker facilities, foreign exchange and other digital services like mobile banking, Internet Banking, NEFT, RTGS etc. These are mainly profit-oriented organisations. Co-operative Banks are small scale banking institutions run on no profit no loss basis for mutual cooperation and help.
- Scheduled commercial banks include public sector banks (i.e., SBI group banks and other nationalized banks), private sector banks, foreign banks (which are incorporated in a foreign country) and regional rural banks (operating at the regional area to facilitate backward people in society).

In addition, the Reserve Bank of India, acts as the supervisor of the banking institutions and money market regulator.

Restriction on Business of Banking Company

Section 8 of the Banking Regulation Act, 1949, imposes certain restrictions on the business of a banking company. These are as follows:

i. No banking company shall directly or indirectly deal in the buying, selling or bartering of goods, except in connection with the realization of security given to or held by it;

ii. No banking company can engage in any trade, or buy, sell or barter goods for others otherwise than in connection with bills of exchange received for collection or negotiation or with such of its business or is referred to in clause (i) of sub-section (1) of section 6.

Minimum transfer of profits to reserve fund [Section 17]

Every banking company incorporated in India is required to transfer at least 25% of its profit to the reserve fund.

The profit of the year as per the profit and loss account prepared u/s 29 is to be taken as base for the purpose of such transfer and transfer to reserve fund should be made before declaration of any dividend.

If any banking company makes any appropriation from the reserve fund or securities premium account, it has to report to the Reserve Bank of India the reasons for such appropriation within 21 days.

Cash Reserve (Section 18)

Every banking company, not being a scheduled bank, has to maintain a cash reserve (CRR) of at least a percentage of the total of its demand and time liabilities in India, as on last Friday of the second preceding fortnight, as specified by RBI from time to time.

Cash reserve can be maintained with itself or by way of a balance in the Current account with the reserve bank or by way of net balance in current accounts or in one or more of the aforesaid ways.

Restrictions on Loans and Advances (Section 20)

No banking company shall

a. grant any loans or advances on the security of its own shares, or

b. enter into any commitment for granting any loan or advance to or on behalf of

   i. Any of its directors,

   ii. Any firm, in which any of its directors is interested as partner, manager, employee or guarantor, Or

   iii. Any company (not being a subsidiary of the banking company or a company registered under Section 25 of the Companies Act, 1956 or a Government Company) of which any of the directors of the banking company is a director, manager, employee or guarantor or in which he holds substantial interest, or

   iv. Any individual, in respect of whom any of its directors is a partner or guarantor.

Liquidity norms (Section 24)

Every banking company has to maintain in cash, gold or unencumbered approved securities, an amount at % prescribed (by RBI) of its demand and time liabilities in India.

However, this percentage is changed by the Reserve Bank of India from time to time considering the general economic conditions.

This is in addition to the average daily balance which a scheduled bank is required to maintain under Section 42 of the Reserve Bank of India Act, and in case of other banking companies, the cash reserve required to be maintained under Section 18 of the Banking Regulation Act.

Accounting in Banking Companies

A Bank's Book Keeping System

Under bank's Book keeping system, every transaction, particularly concerning the customers, is entered in the personal ledger directly from vouchers as soon as it takes place.

The objective of the system is

a. to keep up-to-date detailed ledgers,

b. to balance the trial balance every day,

c. to keep all control accounts in agreement with the detailed ledgers.

Main Characteristics of a Bank's Book-Keeping System

The main characteristics of a bank's system of book-keeping are as follows:

Voucher Posting	Entries in the personal ledger are made directly from vouchers instead of being posted from the books of prime entry.
Voucher Summary Sheets	The vouchers entered into different personal ledgers each day are summarized on summary sheets, totals of which are posted to the control accounts in the general ledger.
Daily Trial Balance	The general ledger trial balance is extracted and agreed every day.
Continuous Checks	All entries in the detailed personal ledgers and summary sheets are checked by persons other than those who have made the entries. A considerable force of such check is employed, with the general result that most cleric al mistakes are detected before another day begins.
Control Accounts	A trial balance of the detailed personal ledgers is prepared periodic ally, usually every two weeks, agreed with general ledger control accounts.
Double Voucher System	Two vouchers are prepared for every transaction not involving c ash-one debit voucher and another credit voucher.

Books of Accounts

Now-a-days, the daily transactions of bank are numerous. All these transactions are to be recorded immediately to reflect the exact position of each customer's account. Therefore, a bank has to adopt specialized system of book-keeping, which will ensure immediate entry of numerous transactions and keep an internal check on the books of account. To achieve these objectives, banks generally maintain a large number of subsidiary and memorandum books in addition to Principal Books of Account. These are as below:

1. **Principal Books of Accounts**

a. General Ledger	The General Ledger contains: ⅄ Control Accounts of all personal ledgers. ⅄ Profit and Loss Account. ⅄ Assets' Accounts. ⅄ Contra Accounts. **Usefulness:** It facilitates the preparation of Balance Sheet.
b. Profit and Loss Ledger	The Profit and Loss Ledger contains: ⅄ Detailed Accounts of Revenue items. ⅄ Detailed Accounts of Expense items. **Usefulness:** It facilitates the preparation of Profit and Loss Account.

2. Subsidiary Books

a. Personal Ledgers	⅄ Current Accounts Ledger. ⅄ Saving Bank Accounts Ledgers. ⅄ Fixed Deposit (often further classified by length of period of deposit) Ledgers. ⅄ Loan Ledger. ⅄ Overdraft Ledger. ⅄ Cash Credit Ledger. ⅄ Customers' Acceptances, Endorsements and Guarantee Ledgers.
b. Bill Registers	⅄ Inward Bills for Collection. ⅄ Outward Bills for Collection. ⅄ Bills Discounted and Purchased Register.

3. Subsidiary Registers

Subsidiary registers are kept for various types of transactions.

a. Demand Drafts, Telegraphic Transfers and Mail Transfers issued on Branches and Agencies.

b. Demand Drafts, Telegraphic Transfers and Mail Transfers received from Branches and Agencies.

c. Letters of Credit.

d. Letters of Guarantee

4. **Memorandum Books**

In addition to the above books and registers, various departments of a bank have to maintain a number of memorandum books to facilitate their work. They include:

1. Departmental Journals	Maintain a record of all the transfer entries originated by each department
2. Cash Department	**a.** Receiving Cashiers' Cash Book (pay-in-slips are vouchers) **b.** Paying Cashiers' Cash Book (Bearer Cheques/drafts etc. are vouchers) **c.** Main Cash Book (by person other than cashier) **d.** d. Cash Balance Book
3. Clearing Department	**a.** Outward Clearing (for cheques received from customers): (i) Clearing Cheques Received Book. (ii) Bank wise List of above Cheques (one copy of which is sent to the clearing house together with cheques). **b.** Inward Clearing (for cheques issued by customers received from other Banks).
4. Loans and Overdraft Departments'	**a.** Registers for shares and other securities held on behalf of each customer. **b.** Summary Books of Securities giving details of Government securities, shares of individual companies etc. **c.** Godown registers maintained by the godown-keeper of the bank. **d.** Price register giving the wholesale price of the commodities pledged with the bank. **e.** Overdraft Sanction register. **f.** Drawing Power book. **g.** Delivery Order books. **h.** Storage books.
5. Deposits Department	**a.** Account Opening and Closing registers. **b.** For Fixed Deposits, Rate register giving analysis of deposits according to rates. **c.** Due Date Diary **d.** Specimen signature book.

6. Establishment Department	**a.** Salary and allied registers, such as attendance register, leave register, overtime register, etc. **b.** Register of fixed assets, e.g. furniture's and fixtures, motor cars, vehicles, etc. **c.** Stationery registers **d.** Old records register.
7. General	**a.** Signature book of bank's officers. **b.** Private Telegraphic Code and Cyphers.

5. Statistical Books

These are kept in different banks based on their individual requirements. Some of the common purposes are:

a. To record Average Balance in Loan and Advances etc.

b. To record Deposits received and amount paid out each month in the various departments.

c. Number of Cheques paid.

d. Number of Cheques, Drafts, Bills etc. collected.

New Revised Formats
The Third Schedule

(See Section 29)

Form 'A'

Form of Balance Sheet

Balance Sheet of ____________________(here enter name of the Banking company)

Balance Sheet as on 31st March (Year)

(000's)

	Schedule	As on 31.3.... (Current year)	As on 31.3...... (Previous year)
Capital & Liabilities			
Capital	1		
Reserve & Surplus	2		
Deposits	3		
Borrowings	4		
Other liabilities and provisions	5		
Total			
Assets			
Cash and balances with Reserve Bank of India	6		
Balance with banks and Money at call and short notice	7		
Investments	8		
Advances	9		
Fixed Assets	10		
Other Assets	11		
Total			
Contingent liabilities	12		
Bills for collection			

Form 'B'

Form of Profit & Loss Account

for the year ended 31st March

('000)

		Schedule	Year ended As on 31.3.... (Current year)	Year ended As on 31.3.... (Previous year)
I.	**Income**			
	Interest earned	13		
	Other income	14		
	Total			
II.	**Expenditure**			
	Interest expended	15		
	Operating expenses	16		
	Provisions and contingencies			
	Total			
III.	**Profit/Loss**			
	Net profit/loss (—) for the year			
	Profit/Loss (—) brought forward			
	Total			
IV.	**Appropriations**			
	Transfer to statutory reserves			
	Transfer to other reserves			
	Transfer to Government/Proposed dividends			
	Balance carried over to balance sheet			
	Total			

Schedules forming part of Balance Sheet

Schedule 1 - Capital

	As on 31.3... (Current year)	As on 31.3... (Previous year)
I. **For Nationalised Banks**		
Capital (Fully owned by Central Government)		
II. For Banks Incorporated outside India		
Capital		
(i) (The amount brought in by banks by way of start-up capital as prescribed by RBI should be shown under this head)		
(ii) Amount of deposit kept with the RBI under Section 11(2) of the Banking Regulation Act, 1949		
Total		
III. For other Banks		
Authorised Capital		
(___Shares of Rs.____ each)		
Issued Capital		
(___Shares of Rs.____each)		
Subscribed Capital		
(____Shares of Rs.___ each)		
Called-up Capital		
(____Shares of Rs.___ each)		
Less: Calls unpaid		
Add: Forfeited shares		
Total		

Schedule 2 - Reserves and Surplus

	As on 31.3.... (Current year)	As on 31.3.... (Previous year)
I. Statutory Reserves		
Opening Balance		
Additions during the year		

Deductions during the year

II. Capital Reserves

Opening Balance

Additions during the year

Deductions during the year

III. Share Premium

Opening Balance

Additions during the year

Deductions during the year

IV. Revenue and other Reserves

Opening Balance

Additions during the year

Deductions during the year

V. Balance in Profit and loss Account

Total: (I, II, III, IV and V)

Schedule 3 - Deposits

	As on 31.3... (Current year)	As on 31.3... (Previous year)
A. I. **Demand Deposits**		
(i) From banks		
(ii) From others		
II. **Savings Bank Deposits**		
III. **Term Deposits**		
(i) From Banks		
(ii) From others		
Total: (I, II and III)		
B. (i) Deposits of branches in India		
(ii) Deposits of branches outside India		
Total		

Schedule 4 - Borrowings

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. Borrowings in India

(i) Reserve Bank of India

(ii) Other banks

(iii) Other institutions and agencies

II. Borrowings outside India

Total: (I and II)

Secured borrowings included in I & II above - Rs.

Schedule 5 - Other Liabilities and Provisions

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. Bills payable

II. Inter-office adjustments (net)

III. Interest accrued

IV. Others (including provisions)

Total

Schedule 6 - Cash and Balances with Reserve Bank of India

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. **Cash in hand** (including foreign currency notes)

II. **Balances with Reserve Bank of India**

(i) In Current Account

(ii) In Other Accounts

Total: (I & II)

Schedule 7 - Balances with Banks & Money at Call & Short Notice

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. In India

(i) Balances with banks

(a) in Current Accounts

(b) in Other Deposit Accounts

(ii) Money at call and short notice

(a) with banks

(b) with other institutions

Total: (i & ii)

II. Outside India

(i) In Current Accounts

(ii) In other Deposits Accounts

(iii) Money at call and short notice

Total

Grand Total (I & II):

<u>Schedule 8 - Investments</u>

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. Investments in India in

(i) Government securities

(ii) Other approved securities

(iii) Shares

(iv) Debentures and Bonds

(v) Subsidiaries and/or joint ventures

(vi) Others (to be specified)

Total

II. Investments outside India in

(i) Government securities

(Including local authorities)

(ii) Subsidiaries and/or joint ventures abroad

(iii) Other investments (to be specified)

Total

Grand Total: (I & II)

Schedule 9 - Advances

As on 31.3.... As on 31.3....

(Current year) (Previous year)

A. (i) Bills purchased and discounted

(ii) Cash credits, overdrafts and loans repayable on demand

(iii) Term loans

Total

B. (i) Secured by tangible assets

(ii) Covered by Bank/Government Guarantees

(iii) Unsecured

Total

C. I. **Advances in India**

(i) Priority Sectors

(ii) Public Sector

(iii) Banks

(iv) Others

Total

II. Advances outside India

(i) Due from banks

(ii) Due from others

(a) Bills purchased and discounted

(b) Syndicated loans

(c) Others

Total

Grand Total: (C. I & II)

Schedule 10 - Fixed Assets

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. Premises

At cost as on 31st March of the preceding year

Additions during the year

Deductions during the year

Depreciation to date

II. Other Fixed Assets (including Furniture and Fixtures)

At cost as on 31st March of the preceding year

Additions during the year

Deductions during the year

Depreciation to date

Total: (I & II)

Schedule 11 - Other Assets

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. Inter-office adjustments (net)

II. Interest accrued

III. Tax paid in advance/tax deducted at source

IV. Stationery and stamps

V. Non-banking assets acquired in satisfaction of claims

VI. Others*

Total

Schedule 12 - Contingent Liabilities

As on 31.3.... As on 31.3....

(Current year) (Previous year)

I. Claims against the bank not acknowledged as debts

II. Liability for partially paid investments

III. Liability on account of outstanding forward exchange contracts

IV. Guarantees given on behalf of constituents

(a) In India

(b) Outside India

V. Acceptances, endorsements and other obligations

VI. Other items for which the bank is contingently liable

Total

Schedules forming part of Profit and Loss Account

<u>Schedule 13 - Interest Earned</u>

	Year ended 31.3.... (Current year)	Year ended 31.3.... (Previous year)
I. Interest/discount on advances/bills		
II. Income on investments		
III. Interest on balances with Reserve Bank of India and other inter-bank funds		
IV. Others		
Total		

<u>Schedule 14 - Other Income</u>

	Year ended 31.3.... (Current year)	Year ended 31.3.... (Previous year)
I. Commission, exchange and brokerage		
II. Profit on sale of investments		
Less: Loss on sale of investments		
III. Profit on revaluation of investments		
Less: Loss on revaluation of investments		
IV. Profit on sale of land, building and other assets		
Less: Loss on sale of land, building and other assets		
V. Profit on exchange transactions		
Less: Loss on exchange transactions		
VI. Income earned by way of dividends etc. from subsidiaries/companies and/or joint ventures abroad/in India		
VII. Miscellaneous Income		
Total		

<u>Schedule 15 - Interest Expended</u>

	Year ended 31.3.... (Current year)	Year ended 31.3.... (Previous year)
I. Interest on deposits		
II. Interest on Reserve Bank of India/inter-bank borrowings		
III. Others		
Total		

Schedule 16 - Operating Expenses

Year ended Year ended

31.3.... 31.3....

(Current year) (Previous year)

I. Payments to and provisions for employees

II. Rent, taxes and lightingIII. Printing and stationery

IV. Advertisement and publicity

V. Depreciation on Bank's property

VI. Director's fees, allowances and expenses

VII. Auditor's fees and expenses (including branch auditor's fees and expenses)

VIII. Law Charges

IX. Postages, Telegrams, Telephones, etc.

X. Repair and maintenance

XI. Insurance

XII. Other expenditure

Total

Accounting for Some Special Transactions

Discounting of bills:

1. A bank may straight away purchase a Bill (Discounting). In this case after reducing discount charges, the balance amount is credited to the account of the customer. The total of both is debited to 'Bills purchased and discounted account'. This account is an Asset.

Bills purchased & Discounted a/c	Dr	XXXX	
To Discount on Bills discounted a/c			XXXX
To Customer a/c			XXXX

2. **Rebate on Bills Discounted:**

   (i) Banks discount hundreds of bills every day and when someone gets a bill discounted, the bank credits the discount account with the full amount of the discount, the bank will earn in respect of that bill. But in practice, it frequently happens that some of these bills will not mature by the close of the accounting year. The portion of the discount which relates to the period falling after the close of the accounting period is called 'rebate on bills discounted', or 'unearned discount'.

   (ii) Since discount on bill discounted is an income for the bank and is shown in the Profit & Loss Account under schedule 13, the amount of unexpired discount, if given in the adjustments, is deducted from schedule 13 and is also shown on the liabilities side of the balance sheet in the item 'other liabilities and provisions' in schedule 5.

Discount on Bills discounted a/c Dr XXXX

To Rebate on bills discounted a/c XXXX

(iii) The Rebate A/c is shown on the liability side of the Balance Sheet as income received which has not accrued before the close of the year. Immediately on commencement of next financial year the Rebate A/c is closed by transfer to the credit of Discount A/c.

Rebate on bills discounted a/c Dr XXXX

To Discount on Bills discounted a/c XXXX

<u>Collection of Bills:</u>

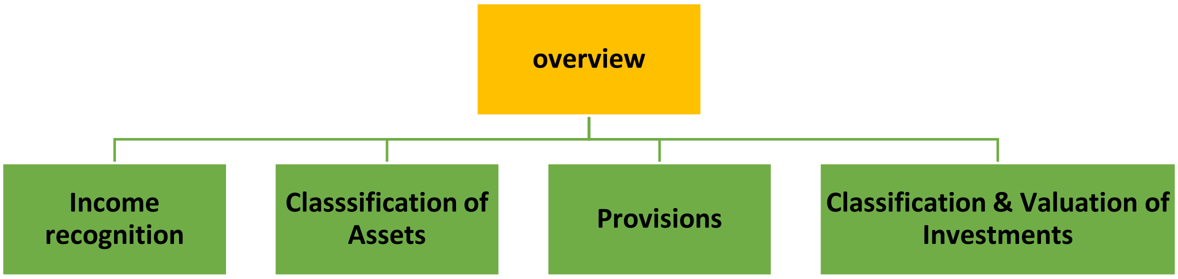
1. One of the services provided by banks to their customers is to collect the dues against Bills of Exchange from their customers on the due dates.
2. Where the bills have been discounted the proceeds of such bills on due date are treated as incomes of the bank. On the other hand, if bills have not been discounted, the proceeds on the same on maturity are credited to the account of the customer.
3. The particulars will be recorded in a separate book called Bills for Collection Register. Bills sent for collection have to be shown by way of Note as per Third Schedule.
4. Two Accounts have to be opened. They are mirror images of each other. They are:
   (i) Bills for Collection (Asset)
   (ii) Bills for Collection (Liability)

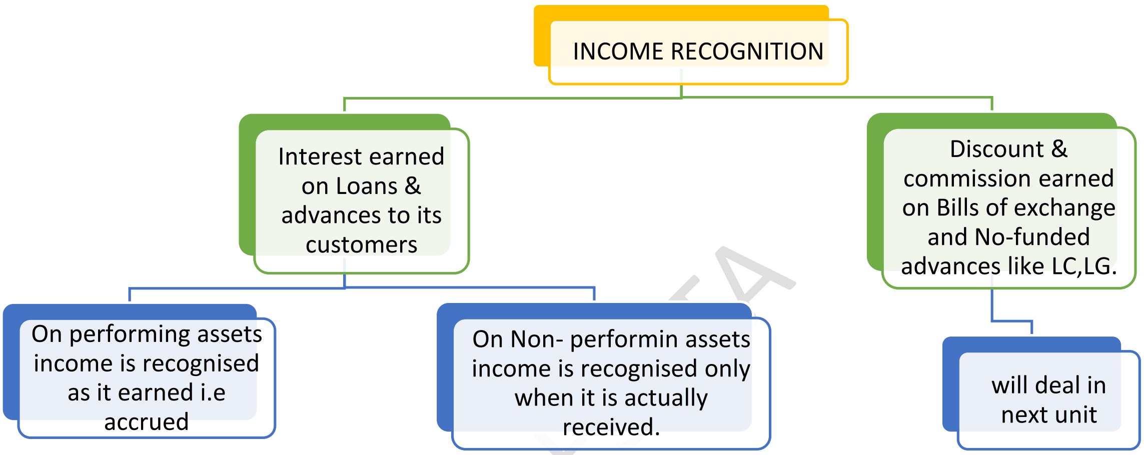
<u>Acceptance and Endorsement</u>:

1. A bank has more acceptable credit as compared to that of its customer, because of this, more often, the bank is called to accept or endorse a bill on behalf of its customers. The bank has to honour this acceptance on behalf of its client only in the event of a client failing to honour the bill on the due date.
2. As against this liability, the bank has a corresponding claim against the customer on whose behalf it has undertaken to be a party to the bill, either as an acceptor or as an endorser. As a safeguard against the customer not being able to meet the demand of the bank in this respect, usually the bank requires the customer to deposit a security equivalent to the amount of the bill accepted on his behalf.
3. Such Acceptance (Liabilities) which are outstanding at the close of the year and the corresponding asset (security) is disclosed as Contingent liability.

4. If the bill, at the end of its term, has to be retired by the bank and the amount cannot be collected from the customer on demand, the bank reimburses itself by disposing of the security deposited by the customer.

INCOME RECOGNITION, CLASSIFICATION OF ASSETS AND PROVISIONS





Performing Asset:

Performing assets are Standard assets are those which do not disclose any problems and which does not carry more than normal risk attached to the business. Simply interest on those advances received regularly without causing any problem.

Non-Performing asset:

NPA is other than performing asset.

Identification of NPA: The identification of NPA is determined on the basis of day past due basis and the same is reviewed at each reporting period.

1. **Bills purchased and discounted** become NPA if interest and / or instalment of principal remain overdue for a period exceeding 90 days.
2. **Term Loans**: become NPA if their amount (interest or principal) remain overdue wholly or partly for a period exceeding 90 days.
3. **A cash credit / overdraft** account is treated as NPA if it becomes **out of order**.

An account is treated as 'out of order' if any of the following conditions are satisfied:

(a) The outstanding balance remains continuously in excess of the sanctioned limit/drawing power for a continuous period of 90 days prior to the Balance Sheet date.

(b) Though the outstanding balance is less than the sanctioned limit/drawing power –

(i) there have been no credits for a continuous period of more than 90 days prior to the date of balance sheet; or

(ii) credits during the aforesaid period are not enough to cover the interest debited during the same period.

4. **<u>Agricultural Advances</u>**: Advances granted for agriculture purposes becomes NPA if interest and/or instalment of principal remains overdue for two crop seasons in case of short duration crops and a loan granted for long duration crops will be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season.

Long duration crops are those crops having crop season of more than one year and other crops will be treated as short duration crops.

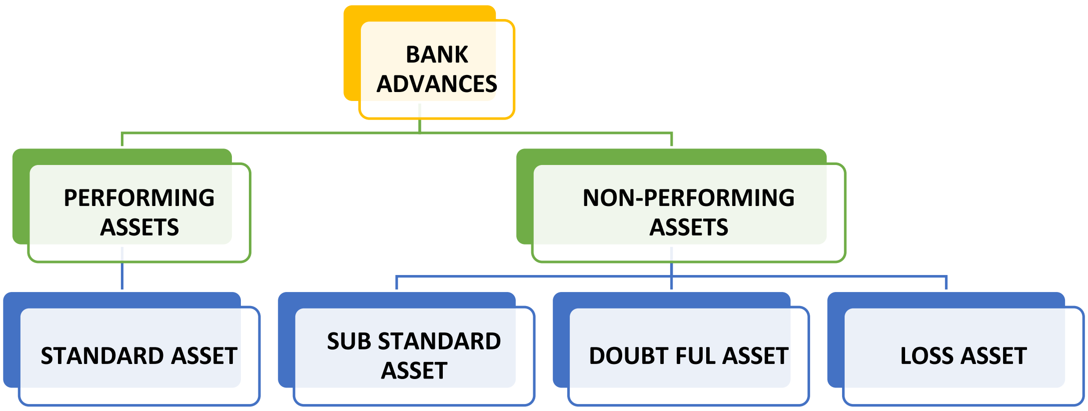
5. **<u>Advances Guaranteed by EXIM Bank</u>**: In the case of advances covered under the guarantee-cum-refinance programme of EXIM Bank, to the extent payment has been received by the bank from the EXIM Bank, the advance may not be treated as NPA. The balance should, however, be treated as NPA.

<u>IMPORTANT POINTS RELATED TO NPA:</u>

(i) **<u>Temporary Deficiencies</u>**: The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as non-availability of adequate drawing power based on the latest available stock statement etc.

(ii) **<u>Determination of NPAs- Borrower-wise, Not Facility-wise</u>**: If any of the credit facilities granted to a borrower becomes non-performing, all the facilities granted to the borrower will have to be treated as NPA without any regard to performing status of other facilities.

<u>CLASSIFICATION OF BANK ADVANCES FOR CREATION OF PROVISION:</u>



Standard assets are those which do not disclose any problems and which does not carry more than normal risk attached to the business.

Sub-standard asset is one which has been classified as an NPA for a period not exceeding 12 months.

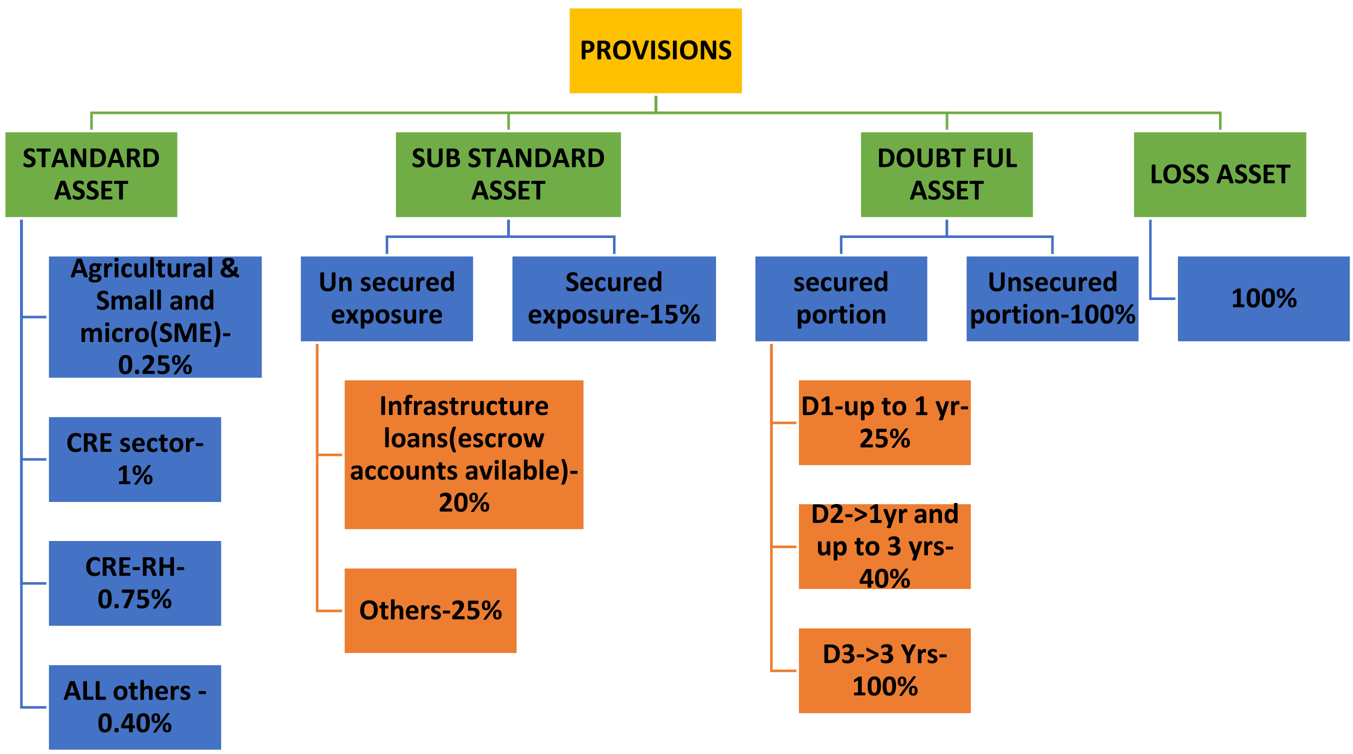
Doubtful Assets - An asset would be classified as doubtful if it has remained in the substandard category for a period of at least12 months.

Loss Assets -A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspectors but the amount has not been written off, wholly or partly.

NOTES:

1. It may be noted that the above classification is meant for the purpose of computing the amount of provision to be made in respect of advances and not for the purpose of presentation of advances in the balance sheet. The balance sheet presentation of advances is governed by the Third Schedule to the Banking Regulation Act, 1949, which requires classification of advances altogether differently.
2. **Threats to Recovery:** It has been clarified, however, that in respect of accounts where there are potential threats to recovery on account of erosion in the value of security or non-availability of security and existence of other factors such as frauds committed by borrowers, it will not be prudent for banks to clarify them first as sub-standard and thereafter as doubtful. Banks have been advised to classify such accounts straightway as doubtful or loss assets, as appropriate irrespective of the period for which the account has remained NPA.

PROVISIONS



Notes:

1. It is clarified that the Medium Enterprises will attract 0.40% standard asset provisioning.
2. Accounting and Provisioning Norms for Equipment Leasing Activity: While the accounting and provisioning norms discussed above shall also apply in respect of equipment leasing activities.
3. Since no bank is likely to extend any loans or advances without adequate security, it is prudent to assume in the questions that even in the case of substandard or doubtful or loss assets, the same are secured unless the question specifically mentions otherwise.

Provisioning for advances covered by ECGC/DICGC guarantee:

1. In the case of advances guaranteed by Export Credit Guarantee Corporation (ECGC) or Deposit Insurance Credit Guarantee Corporation (DICGC), provision is required to be made only for the balance amount of advance outstanding in excess of the amount guaranteed by the corporations.
2. In case the bank also holds a security in respect of an advance guaranteed by ECGC/DICGC, the realisable value of the security should be deducted from the outstanding balance before the ECGC/DICGC guarantee is off-set.

PROBLEMS FOR DISCUSSION CMA SOURCE

PROBLEM 1:

When closing the books of a bank on 31.03.2021 you find in the loan ledger an unsecured balance of Rs.2,00,000 in the account of a merchant whose financial condition is reported to you as bad and doubtful.

Interest on the same account amounted to Rs.20,000 during the year.

How would you deal with this item of interest in 2020-21 account?

During the year 2021-22, the bank accepts 75 paise in the rupee on account of the total debt due up to 31.03.2021.

Show the entries and the necessary accounts showing the ultimate effect of the transactions in 2021-22 books of account under Interest Suspense Method. **(Illustration 1)**

PROBLEM 2:

From the following details prepare "Acceptances, Endorsements and other Obligation A/c" as would appear in the General Ledger.

On 1.4.21 Acceptances not yet satisfied stood at Rs. 33,45,000. Out of which Rs. 30 lacs were subsequently paid off by clients and bank had to honour the rest. A scrutiny of the Acceptance Register revealed the following:

Client	Acceptances/ Guarantees (Rs.)	Remarks
P	15,00,000	Bank honoured on 10.6.21
Q	18,00,000	Party paid off on 30.9.21
R	7,50,000	Party failed to pay and bank had to honour on 30.11.21
S	12,00,000	Not satisfied up to 31.3.22
T	7,50,000	-do-
X	4,05,000	-do-
Total	64,05,000	

(Illustration 2)

PROBLEM 3:

Calculate Rebate on Bills discounted as on 31 December, 2021 from the following data and show journal entries for adjustment.

Date of Bill	Rs.	Period	Rate of Discount
(i) 15.10.2021	50,000	5 months	8%
(ii) 10.11.2021	30,000	4 months	7%
(iii) 25.11.2021	40,000	4 months	7%
(iv) 20.12.2021	60,000	3 months	9%

(Illustration 3)

PROBLEM 4:

On 31 March, 2021 Victory Bank Ltd. had a balance of Rs.18 crores in Rebate on Bill Discounted A/c. During the year ended 31st March, 2022, Victory Bank Ltd. discounted bills of exchange of Rs.8,000 crores charging interest at 18% p.a., the average period of discount being for 73 days. Of these, bills of exchange of Rs.1,200 crores were due for realization from the acceptor/customers after 31st March, 2022, the average period outstanding after 31st March, 2022 being 36.5 days.

Victory Bank Ltd. asks you to pass journal entries and show the ledger accounts pertaining to:

a. Discounting of Bills of Exchange; and

b. Rebate on bill Discounted. **(Illustration 4)**

PROBLEM 5:

The books of a bank include a loan of Rs.5,00,000 advanced on 31.12.2020, interest changeable @ 16% p.a. compounded quarterly. The security for the loan being 7,000 shares of Rs.100 each in a public limited company valued @ Rs.90 each. There is no repayment till 31.03.2022. On 31.03.2022, the value of shares declined to Rs.80 per share.

How would you classify the loan as secured or unsecured in the Balance Sheet? **Illustration 5**

PROBLEM 6:

Given below are details of interest on advance of a Commercial Bank as on 31.03.2021:

(Rs. in Crore)

Particulars	Interest Earned (Rs.)	Interest Received (Rs.)
Performing Assets		
Term Loan	240	160
Cash Credit and Overdraft	1,500	1,240

Bills Purchased and Discounted	300	300
Non-Performing Assets		
Term Loan	150	10
Cash Credit and Overdraft	300	24
Bills Purchased and Discounted	200	40

Find out the income to be recognized for the year ended 31st March 2021. **(Illustration 6)**

PROBLEM 7:

From the following information of details of advances of X Bank Limited calculate the amount of provisions to be made in Profit and Loss Account for the year ended 31.3.2021:

Asset classification	**Rs. in lakhs**
Standard	6,000
Sub-standard	4,400
Doubtful:	
For one year	1,800
For two years	1,200
For three years	800
For more than three years	600
Loss assets	1,600

(Illustration 7)

PROBLEM 8:

From the particulars given below, ascertain the amount of provision to be made against the advances of SBI, Kolkata. (Rs. in'00,000)

Particulars	**(Rs.)**
Total amount of Loans & Advances	120
Advance fully secured	70
Advance overdue for 15 months	20
Advance overdue for more than 2½ year but less than 3 years	10
(Secured by mortgage of land & building valued Rs. 5 lakhs)	—
Unsecured Advance not recoverable	20

(Illustration 8)

PROBLEM 9:

Rajatapeeta Bank Ltd. had extended the following credit lines to a Small-Scale Industry, which had not paid any Interest since March, 2015:

	Term Loan	Export Loan
Balance Outstanding on 31.03.2021	Rs. 35 lakhs	Rs. 30 lakhs
DICGC/ECGC cover	40%	50%
Securities held	Rs. 15 lakhs	Rs. 10 lakhs
Realisable value of Securities	Rs. 10 lakhs	Rs. 08 lakhs

Compute necessary provisions to be made for the year ended 31st March, 2021.

(Illustration 9)

PROBLEM 10:

From the following information find out the amount of provisions required to be made in the Profit & Loss Account of a commercial bank for the year ended 31st March, 2021:

a. Packing credit outstanding from Food Processors Rs. 90 lacs against which the bank holds securities worth Rs. 22.50 lacs. 50% of the above advance is covered by ECGC. The above advance has remained doubtful for more than 3 years.

b. Other Advances:

Assets classification	Rs. in lacs
Standard	4,500
Sub-standard	3,300
Doubtful:	
For one year	1,350
For two years	900
For three years	600
For more than 3 years	450
Loss assets	900

(Illustration 10)

PROBLEM 11:

The following are the figures extracted from the books of Y Bank Ltd. [Scheduled Commercial Bank] as on 31.3.2021.

Other information: **(Amount in Rs.)**

Interest and Discount received	20,30,000	Directors' fees and allowance	12,000
Interest paid on Deposits	12,02,000	Rent and taxes paid	54,000

Issued and Subscribed Capital	5,00,000	Stationery and printing	12,000
Reserve under Section	3,50,000	Postage and Telegram	25,000
Commission, Exchange and Brokerage	90,000	Other expenses	12,000
Rent received	30,000	Audit fees	4,000
Profit on sale of investment	95,000	Depreciation on Bank's properties	12,500
Salaries and Allowances	1,05,000		

i. Provision for bad and doubtful debts necessary Rs. 2,00,000.

j. Rebate on bills discounted as on 31.3.2021 Rs. 7,500.

k. Provide Rs.3,50,000 for income tax.

l. The directors desire to declare 10% dividend.

Make the necessary assumption and prepare the Profit and Loss Account in accordance with the law. **Illustration 11**

PROBLEM 12:

From the following trial balance and the additional information, prepare a Balance Sheet of Lakshmi Bank Ltd. a Scheduled Commercial Bank as at 31st March, 2021:

Debit balance	**Rs. (in Lakhs)**
Cash Credits	1,218.15
Cash in hand	240.23
Cash with Reserve Bank of India	67.82
Cash with other Banks	132.81
Money at c all and short notice	315.18
Gold	82.84
Government securities	365.25
Current Accounts	42.00
Premises	133.55
Furniture	95.18
Term Loan	1,189.32
	3,882.33
Credit balance	**Rs. (in Lakhs)**
Share Capital (29,70,000 equity shares of Rs.10 each fully paid up)	297.00

Statutory Reserve	346.50
Net Profit for the year (before appropriation)	225.00
Profit & Loss Account (Opening balance)	618.00
Fixed deposit Accounts	775.50
Savings Deposit Accounts	675.00
Current Accounts	780.18
Bills Payable	0.15
Borrowings from other Banks	165.00
	3,882.33

Additional Information:

a. Bills for collection: Rs. 18,10,000

b. Acceptance and endorsements: Rs. 14,12,000

c. Claims against the bank not acknowledged as debts: Rs. 55,000

d. Depreciation charged on premises: Rs. 1,10,000 and Furniture: Rs. 78,000

(Illustration 12)

PROBLEMS FOR PRACTICE

PROBLEM 1:

Given below interest on advances of a commercial bank. **(Rs. in Lakhs)**

Particulars	Performing Assets		NPA	
	Interest Earned	**Interest Received**	**Interest Earned**	**Interest Received**
Term Loans	120	80	75	5
Cash credit & OD	750	620	150	12
Bills purchased & discounted	150	150	100	20

Find out the income to be recognized for the year ended 31st March 2012.

(ANS: TOTAL INCOME TO BE RECOGNIZED: 1057L)

PROBLEM 2:

Find out the income to be recognized in the case of SS Bank for the year ended 31st March, 20X1:

			(Rs. in lakhs)	
	Performing Assets		**Non-performing Assets**	
	Interest accrued	**Interest received**	**Interest accrued**	**Interest received**
Term loans	240	160	150	10
Cash credits and overdrafts	1,500	1,240	300	24

(SM) (ANS: TOTAL INTEREST TO BE RECOGNIZED: RS.1,774 LAKHS)

PROBLEM 3:

Sanctioned limit	Rs. 60,00,000
Drawing power	Rs. 55,00,000
Amount outstanding continuously from 1.01.20X1 to 31.03.20X1	Rs. 47,00,000
Total interest debited	Rs. 3,42,000
Total credits	Rs.1,25,000

Give your comment , whether above credit facility is NPA or not?

PROBLEM 4:

1) The outstanding amount (funded as well as unfunded) as on 31st March, 20X1 was Rs.10,000. The realizable value of security of the same was Rs.8,000.
2) Period for which the advance has remained in 'doubtful' category as on 31st March, 20X1 was: 2.5 years.

Show the provisions required for the financial years ended 31 march 20X1 and 31 March 20X2

(SM) (ANS: TOTAL PROVISION RS. 5,200)

PROBLEM 5:

From the following information, find out the amount of provisions to be shown in the Profit and Loss Account of AG bank.

Assets	Rs. in lakhs
Standard	5000
Sub-standard	4000
Doubtful: for one year	800
: for three years	600
: for more than three years	200
Loss Assets	1000

(SM) (ANS: TOTAL AMOUNT OF PROVISION - 2260L)

PROBLEM 6:

From the following information of AY Limited, compute the provisions to be made in the Profit and Loss account.

Particulars	Rs. in lakhs
Assets:	
Standard	20,000
Sub standard	16,000
Doubtful	
For one year (secured)	6,000
For two to three years (secured)	4,000
For more than three years (secured by mortgage of plant and machinery of Rs.600 lakhs)	2,000
Loss assets	1,500

(SM) (ANS: TOTAL AMOUNT OF PROVISION - 9080L)

PROBLEM 7:

Outstanding balance ECGC cover Period for which the advance has remained doubtful Value of security held	Rs.4 lakhs 50% More than 3 years remained doubtful (as on march 31,20X1) Rs.1.50 lakhs

You are required to calculate provisions.

PROBLEM 8:

Outstanding balance ECGC cover Period of which the advance has remained doubtful Value of security held (realizable value only 80%)	Rs.4 lakhs 50% More than 3 years remained doubtful (as on march 31, 20X1) Rs. 1.50 lakhs

You are required to calculate provisions as per applicable rates.

(SM) (ANS: TOTAL PROVISION: RS.2.75 LAKHS)

PROBLEM 9:

In KR bank the doubtful assets (more than 3 years) as on 31-3-2012 is Rs. 1,000 lakhs. The value security (including DICGC 100% cover of Rs.100 lakhs) is ascertained at Rs.500 lakhs. How much provision must be made in the books of the bank towards doubtful assets?

(SM) (ANS: TOTAL PROVISION RS. 900L)

PROBLEM 10:

A loan outstanding of Rs 50,00,000 has DICGC cover. The loan guaranteed by DICGC is assigned a risk weight of 50%. What is the value of Risk-adjusted asset?

(SM) (ANS: VALUE OF RISK-ADJUSTED ASSET – 25L)

PROBLEM 11:

The following is an extract from Trial Balance of overseas Bank as at 31st March, 20X3

Particulars	Debit Rs.	Credit Rs.
Bills discounted	12,64,000	-
Rebate on bills discounted not due on 31st March,2012	-	22,160
Discount received		1,05,708

An analysis of the bills discounted is as follows:

Rs.	Due date in 2013	Rate of Discount in % (p.a.)
1,40,000	June 5th	14
4,36,000	June 12th	14
2,82,000	June 25th	14
4,06,000	July 6th	16

Calculate Rebate on Bills Discounted as on 31-3-20X3 and show necessary journal entries.

(SM) (ANS: REBATE ON BILLS DISCOUNTED: RS.42,317)

PROBLEM 12:

On 31st March, 20X1, Uncertain Bank had a balance of Rs.9 crores in "rebate on bills discounted" account. During the year ended 31st March, 20X2, Uncertain Bank discounted bills of exchange of Rs. 4,000 crores charging interest at 18% per annum the average period of discount being for 73 days. Of these, bills of exchange of Rs.600 crores were due for realisation from the acceptors/customers after 31st March, 20X2, the average period outstanding after 31st March, 20X2 being 36.5 days.

Uncertain Bank asks you to pass journal entries and show the ledger accounts pertaining to:

i) Discounting of bills of exchange and

ii) Rebate on bills discounted.

(SM) (ANS: TOTAL OF DISCOUNT ON BILLS A/C 153.00, REBATE ON BILLS DISCOUNTED 19.80)

PROBLEM 13:

On 01.04.20X1 Bills for collection were Rs.7,00,000. During 20X1-20X2 bills received for collection amounted to Rs.64,50,000, bills collected were Rs.47,00,000 and bills dishonoured and returned was Rs.5,50,500. Prepare Bills for collection (Assets) A/c and bills for Collection (Liability) A/c.

(SM) (ANS: Bills for collection (Assets) A/c:RS.19 LAKHS, bills for Collection (Liability) A/c: RS.19)

PROBLEM 14:

From the following details prepare "Acceptances, Endorsements and other Obligation A/c" as would in the general ledger. On 1- 4 –20X1 Acceptances not yet satisfied stood at Rs.22,30,000. Out of which Rs.20 lakhs were subsequently paid off by clients and bank had to honour the rest. A scrutiny of the Acceptance Register (for transactions during the year) revealed the following:

Client	Acceptances / Guarantees	Remarks
A	10,00,000	Bank honoured on 10-6-20X1
B	12,00,000	Party paid off on 30-9-20X1
C	5,00,000	Party failed to pay and bank had to honour on 30-11-20X1
D	8,00,000	Not satisfied up to 31-3-20X2

E	5,00,000	-DO-
F	2,70,000	-DO-
Total:	**42,70,000**	

(SM)

PROBLEM 15:

Following facts have been taken out from the records of Adarsha Bank Ltd. in respect of the year ending March 31, 20X2:

1. On 01.04.20X1 Bills for collection were Rs.7,00,000. During 20X1-20X2 bills received for collection amounted to Rs.64,50,000, bills collected were Rs.47,00,000 and bills dishonoured and returned were Rs.5,50,500. Prepare Bills for collection (Assets) A/c and bills for Collection (Liability) A/c.
2. On 01.04.20X1, Acceptance, Endorsement, etc. not yet satisfied amounted to Rs.14,50,000. During the year under question, Acceptances, Endorsements, Guarantees etc., amounted to Rs.44,00,000. Bank honoured acceptances to the extent of Rs.25,00,000 and client paid off Rs.10,00,000 against the guaranteed liability. Clients failed to pay Rs.1,00,000 which the Bank had to pay. Prepare "Acceptances, Endorsements and other Obligations A/c" as it would appear in the General ledger.
3. It is found from the books, that a loan of Rs.6,00,000 was advanced on 30.09.20X1 @ 10 per cent p.a. interest payable half yearly; but the loan was outstanding as on 31.03.20X2 without any payment recorded in the meantime, either towards principal or towards interest. The security for the loan was 10,000 fully paid shares of Rs.100 each (the market value was Rs.98 as per the Stock Exchange Information as on 30th September, 20X1). But due to fluctuations, the price fell to Rs.40 per share in January, 20X2. On 31.03.20X2, the price as per Stock Exchange rate was Rs.82 per share. State how you would classify the loan as secured / unsecured in the Balance Sheet of the Company.
4. The following balances are extracted from the Trial Balance as on 31.03.20X2:

Particulars	Dr. Rs.	Cr. Rs.
Interest and Discounts		98,00,000
Rebate for bills discounted		20,000
Bills discounted and purchased	4,00,000	

It is ascertained that the proportionate discounts not yet earned for bills to mature in 20X2-20X3 amount to Rs. 14,000. Prepare Ledger Accounts. **(SM)*(ANS.: A)***

***(ANS:* TOTAL OF BILLS FOR COLLECTION A/C 71,50,000; B) BALANCE 22,50,000; C) FULLY SECURED; D) TOTAL OF REBATE ON BILLS DISCOUNTED 20,000 AND TOTAL OF INTEREST & DISCOUNT A/C 98,06,000)**

PROBLEM 16:

From the following information, prepare Profit and Loss A/c of Dimple Bank as on 31.03.2013:

'000 Rs.	Item	Rs. In 000's
2011-12		2012-13
14,27	Interest and Discount	20,45
1,14	Income from investment	1,12
1,55	Interest on Balance with RBI	1,77
7,22	Commission, Exchange and Brokerage	7,12
12	Profit on sale of investments	1,22
6,12	Interest on Deposits	8,22
1,27	Interest to RBI	1,47
7,27	Payment to and provision for employees	8,55
1,58	Rent, taxes and lighting	1,79
1,47	Printing and stationery	2,12
1,12	Advertisement and publicity	98
98	Depreciation	98
1,48	Director's fees	2,12
1,10	Auditor's fees	1,10
50	Law charges	1,52
48	Postage, telegrams and telephones	62
42	Insurance	52
57	Repairs & maintenance	66

Also give necessary Schedules:

Other Information:

1. **The following items are already adjusted with Interest and Discount (Cr.):**

   Tax Provision ('000 Rs.) 1,48

   Provision for Doubtful Debts ('000 Rs.) 92

   Loss on sale of Investments ('000 Rs.) 12

   Rebate on Bills discounted ('000 Rs.) 55

2. **Appropriations:**

   25% of profit is transferred to Statutory Reserve.

   5% of profit is transferred to Revenue Reserve.

(SM)(ANS: BALANCE IN PROFIT & LOSS ACCOUNT CARRIED TO BALANCE SHEET -RS. 66,100)

PROBLEM 17:

From the following information, prepare Profit and Loss A/c of KC Bank for the year ended 31st March, 2013.

Items	Rs. (in '000)
Interest on cash credit	18,20
Interest on overdraft	7,50
Interest on term loans	15,40
Interest on investments	8,40
Interest on balance with RBI	1,50
Commission on remittances and transfer	75
Commission on letters of credit	1,18
Commission on government business	82
Profit on sale of land and building	27
Loss on exchange transactions	52
Interest paid on deposit	27,20
Auditors' fees and allowance	1,20
Directors' fees and allowances	2,50
Advertisements	1,80
Salaries, allowances and bonus to employees	12,40
Payment to Provident Fund	2,80
Printing and stationery	1,40
Repairs and maintenance	50
Postage, telegrams, telephones	80

Other Information:

1. **Interest on NPA is as follows:**

Particulars	Earned (Rs.'000)	Collected (Rs.'000)
Cash credit	8,20	4,00
Overdraft	450	1,00
Term Loans	750	2,50

2. **Classification of non performing advances**

('000 Rs.)

Standard	30,00
Sub-standard	11,20
Doubtful assets not covered by security	2,00
Doubtful assets covered by security for one year	50
Loss Assets	2,00

3. Investments 27,50

Bank should not keep more than 25% of its investments as 'held-for- maturity' investments. The market value of its rest 75% investments is Rs.19,75,000 as on 31.03.2013.

(SM) (ANS: BALANCE IN PROFIT & LOSS ACCOUNT- (16,60,000))

PROBLEM 18:

From the following information, prepare a Balance Sheet of ADT International Bank as on 31st March, 20X1 giving the relevant schedules. **Rs. in lakhs**

Particulars	Dr.	Cr.
Share Capital:		
19,80,000 Shares of Rs.10 each		198.00
Statutory Reserve		231.00
Net Profit before Appropriation		150.00
Profit and Loss Account		412.00
Fixed Deposit Account		517.00
Savings Deposit Account		450.00
Current Accounts	28.00	520.12
Bills Payable		0.10
Cash credits	812.10	
Borrowings from other Banks		110.00
Cash in Hand	160.15	
Cash with RBI	37.88	
Cash with other Banks	155.87	
Money at Call	210.12	
Gold	55.23	
Government Securities	110.17	

Premises	155.70	
Furniture	70.12	
Term Loan	792.88	
	2,588.22	**2,588.22**

Additional Information:

Bills of collection	18,10,000
Acceptances and endorsements	14,12,000
Claims against the Bank not acknowledged as debts	55,000
Depreciation charges - Premises	1,10,000
Furniture	78,000

50% of the Term Loans are secured by Government guarantees. 10% of cash credit is (including debit balance in current A/C) is unsecured. Transfer 25% of its profit to the reserve fund.

(SM) (ANS: TOTAL OF BALANCE SHEET - 25,88.22L)

PROBLEM 19:

A commercial bank has the following capital funds and assets. Segregate the capital funds into Tier I and Tier II capitals. Find out the capital to risk weighted assets ratio:

Capital Funds	**(Figures in Rs. lakhs)**
Equity Share Capital	4,80.00
Statutory Reserve	2,80.00
Capital Reserve (of which Rs. 280 lakhs were due to revaluation of assets and the balance due to sale)	12.10
Assets:	
Cash Balance with RBI	4.80
Balances with other Bank	12.50
Claims on Banks	28.50
Other Investments	782.50
Loans and Advances:	
(i) Guaranteed by government	128.20
(ii) Guaranteed by public sector undertakings of Government of India	702.10
(iii) Others	52,02.50

Premises, furniture and fixtures	182.00
Other Assets	201.20
Off-Balance Sheet Items: Acceptances, endorsements and letters of credit	37,02.50

(SM) (ANS: CAPITAL ADEQUACY RATIO - 7.65%)

11. ACCOUNTS OF INSURANCE COMPANY

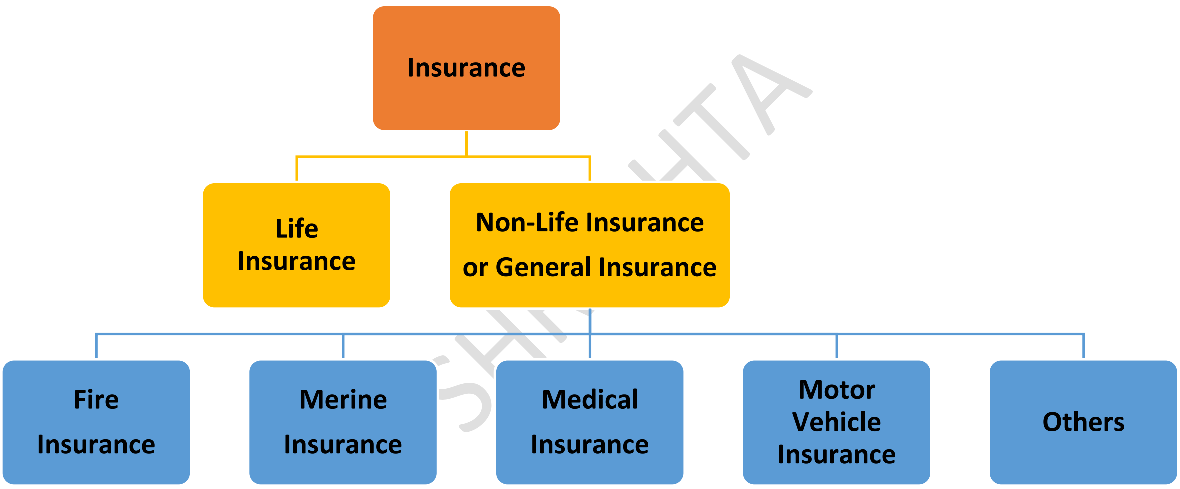
Concept of Insurance:

Insurance is a technique of risk management. It is a contract in which an individual or entity receives financial protection or reimbursement against losses from an insurance company. In insurance, several people exposed to a particular type of risk contribute small amounts called premiums to an insurance fund from which the unfortunates who actually suffer the risk are compensated. Insurance business is essentially a way of averaging the risks.

Insurance Policy

Insurance policy is a contract entered into between the insurance companies called the 'insurer' and the person who insures his risk called the 'insured'. The policy is in the form of a document which the insurance company issues after receiving the premium and which contains all terms and conditions.

Types of Insurance Policies



Life Insurance Policy: A life insurance policy is a contract between an insurance policy holder and an insurance company, where the insurer promises to pay a sum of money in exchange for a premium after a set period or upon the death of an insured person.

- Life insurance takes primarily two forms. In the case of endowment policy, the insured obtains a specified sum in the event of the insured obtaining a specified age or to the family in case the insured dies before attaining specified age. They may be again with or without profit policies.
- Whereas in the case of term policies the family of the insured (the nominee mentioned in the policy) receives a specified sum on the death of insured.

General insurance: It is a contract of indemnity. Insurer will compensate to that extent of loss suffered by insured only. Different forms of general insurance are fire, marine, motor, accident and other miscellaneous non-life insurances.

Important Concepts in Life Insurance Business

a. Premium & Recognition

- Premium is the main revenue for insurance business. It is the payment made by the insured to the Insurance Company in consideration of the contract of Insurance. The premium is generally paid annually or any other shorter time intervals. The premium amount has to be paid "front end" i.e., before the commencement of the insurance cover/ policy.
- **Recognition:** In the case of life business premium is to be recognized on due basis. Premium received in advance which represent income not relating to the accounting period must be disclosed separately in the financial statements under current liabilities. Outstanding premium shown under Current assets.

b. Claims

A claim occurs when any policy falls due for payment. In case of Life Insurance, it arises on death or on maturity of policy. In case of General Insurance, it arises only when the loss occurs. While calculating the claim outstanding at the end, the claim intimated as well as the claim intimated and accepted, both are considered.

c. Commission

Generally, insurance companies get business through agents; these agents receive commission on the basis of the amount of premium they generate for the insurance company. Commission paid to agents is shown as a debit (expense) in the Revenue Accounts.

d. Surrender Value

In the case of life insurance policy, the policy normally has value only when it matures. But to facilitate the promotion of business, insurance companies assign value to the policy on the basis of the premiums paid. Insurance companies will be prepared to pay such value on the surrender of the policy by a needy policy holder desiring to realize the policy. Therefore, the value is referred to as 'surrender value'. Surrender value is usually nil until at least two annual premiums are paid. Amount paid as surrender value is an expenditure and is similar to claims paid.

e. Paid-up Policy

A policy holder, who has difficulty in paying the premium, may be allowed an option to get the policy paid-up. In such a case, the policyholder is relieved from the obligation of paying off the rest of premium, but he will not get the full value of policy which is calculated as follows:

$$\text{Paid- up value} = \text{Sum assured} \times \frac{\text{No of Premiums Paid}}{\text{Total number of premiums payable}}$$

The amount paid on maturity in respect of paid-up policies is included in the amount of claim.

f. Bonus

It is nothing but the share of profit which is payable by the insurance company to the policyholders. There are five basic types of bonuses in insurance. These are as follows:

(i) Simple Reversionary Bonus - It is a bonus that is accrued to almost every traditional life insurance plan. A percentage of the sum assured gets added to the policy every year until maturity or the death claim.

(ii) Compound Reversionary Bonus - It is a bonus calculated as a percentage of the sum assured and the bonus accrued last year. It is again paid as a part of the maturity benefit or death benefit.

(iii) Interim Bonus - Bonus is accrued in a life insurance policy every year. However, there is a chance that the death claim occurs before the next declaration. Hence, insurers declare an interim bonus to set the policyholder's family at an advantage and benefit from the bonus amount.

(iv) Cash Bonus - In a cash bonus, the insurance company will declare the bonus and make it available for the policyholder to receive it as cash in hand. It is not accrued till maturity like the other types and is provided at the end of every year.

(v) Terminal Bonus - Terminal Bonus is a one-time bonus in insurance paid when the policyholder runs through the entire policy term or a period specified by the insurer. Thus, it is not applicable if the policy is surrendered before the term ends.

g. Re-insurance

Re-insurance means the transfer of a part of risk by the insurer. This is particularly done when the amount of insurance is very high and when it is very difficult to bear the entire risk by a single insurer, a part of the risk is to be insured with some other insurance companies. The company who reduces their risk is known as Re-insurance ceding company and the other company is known as Re-insurer.

h. Ceding Company

It is an insurance company that shifts part or all of a risk it has assumed to another insurance company. The Ceding company shares the premium amount it has received to cover the risk, with the second insurance company called the Reinsurer. In return the Reinsurer company pays commission to the Ceding company for getting the business.

i. Double Insurance

When the same risk and the same subject matter is insured with more than one insurer, i.e., more than one insurance company, it is called Double Insurance.

j. **Life Assurance Fund**

This represents the excess of revenue receipts over revenue expenditure relating to life business. The fund is available to meet the aggregate liability on all policies outstanding. Revenue Account is prepared every year to ascertain the balance of life insurance fund at the end of the year. In the preparation of Revenue Account, the opening balance of the life insurance fund is the starting point. Other items of revenue income are credited to the fund and revenue items of expense are debited. The resulting figure is the closing balance of the revenue fund.

k. **Valuation Balance Sheet**

- The balance in the life assurance fund cannot be taken as the profit made by the life insurance business. For the purpose of ascertaining the profit, the insurance company should calculate its net liability on all outstanding policies. This calculation is done by experts called actuaries and is a highly complicated mathematical process.
- For calculating net liability, the actuaries calculate the present value of future liability on all the policies in force as well as present value of future premium to be received on policies in force. The excess of the present value of future liability over the present value on future premium is called the net liability.
- It is by comparing the life insurance fund and net liability in respect of policies, that profit in respect of life insurance business can be ascertained. If the life insurance fund is more than the net liability, the difference represents the profit. On the other hand, the excess of net liability over the life assurance fund represents the loss for the inter-valuation period.
- According to Section 28 of the Life Insurance Corporation Act, 1956, 95% of the profit of life business must be distributed to the policyholders by way of 'Bonus' on with-profit policies and the remaining 5% has to be utilized for such purposes as the Government may determine.

Valuation Balance Sheet as on..............................

To Net liability as per actuary's valuation	xxxx	By Life Assurance Fund as per Balance Sheet	xxxx
To Surplus (Net Profit)		By Deficit (Net loss)	

l. **Catastrophe reserve:** Such a reserve should be created by the insurers towards losses which might arise due to entirely unexpected set of events and not for any specific known purpose. Investment of the funds of this reserve must be made in accordance with the prescription of Authority.

IRDA Regulations Regarding Preparation of Financial Statements

a. Insurers doing life insurance business should comply with the requirements of Schedule A and Insurers doing general insurance business should comply with the requirements of Schedule B. As per Schedule A and Schedule B, following accounts need to prepare in below forms:

Life Insurance-Schedule A		**General Insurance-Schedule B**	
Revenue Account	Form A-RA	Revenue Account	Form B-RA
Profit and Loss Account	Form A-PL	Profit and Loss Account	Form B-PL
Balance Sheet	Form A-BS	Balance Sheet	Form B-BS

Schedule A -Part V: Preparation of Financial Statements

(1) An insurer shall prepare the Revenue Account [Policyholders' Account], Profit and Loss Account [Shareholders' Account] and the Balance Sheet in Form A-RA, Form A-PL and Form A-BS, as prescribed in this Part.

(2) An insurer shall prepare separate Receipts and Payments Account in accordance with the Direct Method prescribed in AS 3-" Cash Flow Statement" issued by The Institute of Chartered Accountants of India.

LIFE INSURANCE BUSINESS

Name of the Insurer:

FORM A-RA

REVENUE ACCOUNT for the year ended 31st March, 20...

Policy holders' Account (Technical Account)

Particulars	**Schedule**	**Current Year (Rs. '000)**	**Previous Year (Rs. '000)**
Premiums Earned-Net			
(a) Premium	**1**		
(b) Re-insurance ceded			
(c) Re-insurance accepted			
Income from Investments			
(a) Interest, Dividends & Rent-Gross			
(b) Profit on sale/Redemption of Investments			
(c) Loss on sale/Redemption of Investments			

(d) Transfer/Gain on revaluation/ change in Fair value* **Other Income**			
Total (A)			
Commission Operating Expenses related to Insurance Business Other Expenses (to be specified) Provisions (other than taxation) **(a)** For diminution in the value of investments (Net) **(b)** Others (to be specified)	**2** **3**		
Total (B)			
Benefits Paid (Net) Interim Bonuses Paid **(a)** Gross **(b)** Amount ceded in Re-insurance **(c)** Amount accepted in Re-insurance	**4**		
Total (C)			
Surplus/(Deficit) (D) = (A) - (B) - (C) **Appropriations** Allocation of Bonus to Policy holders Transfer to Shareholders' Account Transfer to Other Reserves (to be specified) Transfer to Funds for Future Appropriations			
Total (D)			

FORM A-PL

PROFIT & LOSS ACCOUNT for the year ended 31st March, 20…..

Shareholders' Account (Non-technical Account)

Particulars	**Schedule**	**Current Year (Rs. '000)**	**Previous Year (Rs. '000)**
Balance brought forward from the Policy holders Account (Technical Account)			

Income from Investments: **(a)** Interest, Dividends & Rent-Gross **(b)** Profit on sale/Redemption of Investments **(c)** Loss on sale/Redemption of Investments Other Income (To be specified) **Total (A)** Expenses other than those directly related to the insurance business Provisions (Other than taxation) **(a)** For diminution in the value of investments (Net) **(b)** Others (to be specified) **Total (B)** Profit/ (Loss) before tax Provision for Taxation Profit/ (Loss) after tax **Appropriations** **(a)** Brought forward Reserve/Surplus from the Balance Sheet **(b)** Interim dividends paid during the year **(c)** Proposed Final Dividend **(d)** Dividend Distribution on Tax **(e)** Transfer to reserves/other accounts (to be specified)			
Profit carried forward to the Balance Sheet			

FORM A-BS

BALANCE SHEET As At 31st March, 20.......

Particular	Schedule	Current Year (Rs. '000)	Previous Year (Rs. '000)
Sources of funds			
Shareholders' funds:			
Share Capital	**5**		

Reserves and Surplus	**6**		
Sub-total			
Borrowings	**7**		
Total			
<u>Application of Funds</u>:			
Investments			
Shareholders'	**8**		
Policyholders'	**8A**		
Loans	**9**		
Fixed Assets	**10**		
Current Assets:			
Cash and Bank Balances	11		
Advances and Other Assets	12		
Sub-Total (A)			
Current Liabilities	13		
Provisions	14		
Sub-Total (B)			
Net current assets (C) = (A – B)			
Miscellaneous Expenditure			
(to the extent not written off or adjusted)	15		
Total			

Contingent Liabilities

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Partly paid-up investments **2.** Claims, other than against policies, not acknowledged as debts by the Company **3.** Underwriting Commitments outstanding **4.** Guarantees given by or on behalf of the Company		

5. Statutory Demands/Liabilities in dispute, not provided for **6.** Others (to be specified) **Total**		

Schedules Forming Part of Financial Statements

Schedule 1- Premium

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. First year premiums **2.** Renewal Premiums **3.** Single Premiums		
Total Premiums		
Premium Income from business written: **1.** In India **2.** Outside India		
Total premium (Net)		

Notes. Re-insurance premiums whether on business ceded or accepted are to be adjusted in calculation of total premium.

Schedule 2 – Commission Expenses

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
Commission Paid - **Direct-First year Premiums** - **Renewal Premiums** - **Single Premiums** **Add:** Commission on Re-insurance Accepted **Less:** Commission *on* Re-insurance Ceded		
Net Commission		

Schedule 3 - Operating Expenses Related to Insurance Business

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Employees' Remuneration & Welfare Benefits		
2. Travel, Conveyance and Vehicle Running Expenses		
3. Rents, Rates & Taxes		
4. Repairs		
5. Printing & Stationery		
6. Communication Expenses		
7. Legal & Professional Charges		
8. Medical Fees		
9. Auditors' Fees, Expenses, etc		
(a) as auditor		
(b) as adviser or in any other capacity, in respect of		
(i) Taxation Matters		
(ii) Insurance Matters		
(iii) Management Services; and		
(c) in any other capacity		
10. Advertisement and Publicity		
11. Interest & Bank Charges		
12. Others (to be specified)		
13. Depreciation		
14. Total		

Schedule 4 - Benefits Paid [Net]

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Insurance Claims:		
(a) Claims by Death,		
(b) Claims by Maturity,		
(c) Annuities/Pensions in payment,		
(d) Other benefits, specify		

2. Amount ceded in Re-insurance: **(a)** Claims by Death, **(b)** Claims by Maturity, **(c)** Annuities/Pensions in payment, **(d)** Other benefits, specify		
3. Amount accepted in Re-insurance: **(a)** Claims by Death, **(b)** Claims by Maturity, **(c)** Annuities/Pensions in payment, **(d)** Other benefits, specify		
Total		
Benefits paid to claimants: **1.** In India **2.** Outside India Total Benefits paid (Net)		

Notes:

(a) Claims include claims settlement costs, wherever applicable.

(b) The legal and other fees and expenses shall also form part of the claims cost, wherever applicable.

Schedule 5 - Share Capital

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Authorized Capital Equity Shares of Rs. each **2. Issued Capital** Equity Shares of Rs. each **3. Subscribed Capital** .... Equity Shares of Rs. **4. Called-up Capital** Equity Shares of. Rs. **5. Less: Calls unpaid** **Add:** Shares forfeited (Amount originally paid up) **Less:** Par value of Equity Shares bought back		
Total		

Schedule 5A – Pattern of Shareholding

Shareholders	Current Year		Previous Year	
	Number of Shares	% of Holding	Number of Shares	% of Holding
Shares Promoters • **Indian** • **Foreign** Others				
Total				

Schedule 6 – Reserves and Surplus (Shareholders)

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Capital Reserve		
2. Capital Redemption Reserve **3. Share Premium** **4. Revaluation Reserve** **5. General Reserves** **6. Catastrophe Reserve** **7. Other Reserves (to be specified)** **8. Balance of Profit in Profit and Loss Account** **Total**		

Schedule 7 – Borrowings

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Debentures/ Bonds **2.** Fixed Deposits **3.** Banks **4.** Financial Institutions **5.** Other entities carrying on insurance business **6.** Other (to be specified)		
Total		

Notes:

(a) The extent to which the borrowings are secured shall be separately disclosed stating the nature of the Security under each sub-head.

(b) Amounts due within 12 months from the date of Balance Sheet should be shown separately.

Schedule 8 – Investments-Shareholders

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
Long-term investments		
1. Government Securities and Government Guaranteed Bonds including Treasury Bills		
2. Other Approved Securities		
3. Other Investments		
(a) Shares		
– Equity		
– Preference		
(b) Mutual Funds		
(c) Derivative Instruments		
(d) Debentures/Bonds		
(e) Other Securities (to be specified)		
(f) Subsidiaries		
(g) Investment Properties-Real Estate		
Short-term Investments		
1. Government Securities and Government Guaranteed Bonds including Treasury Bills		
2. Other Approved Securities		
3. Other Investments		
(a) Shares		
– Equity		
– Preference		
(b) Mutual Funds		
(c) Derivative Instruments		

(d) Debentures/Bonds **(e)** Other Securities (to be specified) **(f)** Subsidiaries **(g)** Investment Properties-Real Estate **Total** **Investments** **1. In India** **2. Outside India** **Total**		

Schedule 8A Investments-Policyholders

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
Long-term Investments **1. Government Securities and Government Guaranteed Bonds including Treasury Bills** **2. Other Approved Securities** **3. Other Investments** **(a) Shares** – Equity – Preference **(b)** Mutual Funds **(c) Derivative Instruments** **(d) Debentures/Bonds** **(e)** Other Securities (to be specified) **(f)** Subsidiaries **(g)** Investment Properties-Real Estate **4. Investments in Infrastructure and Social sector** **5. Other than Approved Investments** **Short-term Investments** **1. Government securities and Government Guaranteed Bonds including Treasury Bills**		

2. Other Approved Securities **3. Other Investments** **(a) Shares** – Equity		
– Preference		
(b) Mutual Funds		
(c) Derivative Instruments **(d) Debentures/Bonds** **(e)** Other Securities (to be specified) **(f)** Subsidiaries **(g)** Investment Properties-Real Estate **4. Investments in Infrastructure and Social Sector** **5. Other than Approved Investments Total** **Investments** **1 . In India** **2 . Outside India**		
Total		

Schedule 9 – Loans

Particulars	**Current Year (Rs. '000)**	**Previous Year (Rs. '000)**
1. **Security-wise Classification Secured** **(a) On mortgage of property** – **In India** – **Outside India** **(b) On shares, Bonds, Govt. Securities, etc.** **(c)** Others (to be specified) **Unsecured** **(a)** Loans against policies **(b)** Others (to be specified) **Total**		

2. Borrower-wise classification		
(a) Central and State Governments		
(b) Banks and Financial Institutions		
(c) Subsidiaries		
(d) Companies		
(e) Loans against policies		
(f) Others (to be specified)		
Total		
3. Performance-wise classification		
(a) Loans classified as standard		
– **In India**		
– **Outside India**		
(b) Non-standard loans less provisions		
– **In India**		
– **Outside India**		
Total		
4. Maturity-wise classification		
(a) Short-term		
(b) Long-term Total		

SCHEDULE 10 – Fixed Assets

Particulars	Cost/ Gross Block				Depreciation				Net Block	
	Opening	Additions	Deductions	Closing	Up to Last Year	For the Year	On Sales/ Adjustments	To Date	As at year end	Previous year
Goodwill Intangibles (specify) Land Freehold Leasehold Property Buildings Furniture and Fittings Information Technology Equipment Vehicles Office Equipment										

Others (Specify nature)										
TOTAL										
PREVIOUS YEAR										

Schedule 11– Cash and Bank Balances

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Cash (including Cheques, Drafts and Stamps) **2. Bank Balances** **(a) Deposit Accounts** • **Short-term (due within 12 months of the date of Balance Sheet)** • **Others** **(b)** Current Accounts **(c)** Others (to be specified) **3. Money at Call and Short Notice** **(a) With Banks** **(b) With other Institutions** **4. Others (to be specified)**		
Total		
Balances with non-scheduled banks included in 2 and 3 above		
Cash & Bank Balances **1. In India** **2. Outside India**		
Total		

Schedule 12 – Advances and other assets

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
Advances **1. Reserve Deposits with Ceding Companies** **2. Advances to ceding companies** **3. Application money for investments**		

4. Pre-Payments **5. Advances to Officers/Directors** **6.** Advance Tax paid and Taxes Deducted at Source **7.** Others (to be specified) **Total (A)**		
Other Assets **1. Income accrued on investments** **2. Outstanding premiums** **3. Agents' Balances**		
4. Foreign agencies' Balances **5. Due from other entities carrying on Insurance business** **6. Due from Subsidiaries/Holding Company** **7.** Re-insurance claims/balances receivable **8.** Deposit with Reserve Bank of India [Pursuant to Section 7 of Insurance Act, 1938] **9.** Others (to be specified) **Total (B) Total (A + B)**		

Schedule 13 – Current Liabilities

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Agents' Balances		
2. Balances due to other insurance companies **3. Advances from Treaty Companies** **4.** Deposits held on re-insurance ceded **5. Premiums received in advance** **6. Sundry creditors** **7. Due to subsidiaries/holding company** **8. Claims outstanding** **9. Annuities due** **10. Due to Officers/Directors** **11. Others (to be specified)** **Total**		

Schedule 14 – Provisions

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. For taxation (less payments and taxes deducted at source)		
2. For proposed Dividends		
3. For Dividend Distribution Tax		
4. Bonus Payable to the Policyholders		
5. Others (to be specified)		
Total		

Schedule 15 – Miscellaneous Expenditure

(To the extent not written off or adjusted)

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Discount allowed in issue of shares/debentures		
2. Others (to be specified)		
Total		

Accounts of General Insurance Business

General Insurance consists of (i) Fire; (ii) Marine (iii) Accidental Insurance etc. Before incorporating I.R.D.A. (in 2012) general insurance was administrated by General Insurance Corporation of India (GICI). Every general insurance company must prepare their accounts separately for each type of insurance. Usually, the policies are issued for one year. It must be remembered that liabilities of the insurer will arise when the insured suffers any loss due to fire accident etc. If no loss is suffered by the insured no compensation will be paid and the premium which has already been paid will neither be adjusted nor be carried forward for the next year.

(a) Fire Insurance: Fire insurance means insurance against any loss which is caused by fire.

(b) Marine Insurance: a contract of marine insurance may, by its express terms, or by usage of trade, be extended so as to protect the insured against losses on inland water or any land risk which may be incidental to any sea voyage.

(c) Accidental Insurance: Practically, it is mere a contract by which the insurer promises to pay a certain some of money to the insured in case of injury by accident and to the dependents of the insured in case of death by accident.

In addition to the above, there may be travel insurance, health insurance, home insurance etc.

Examples:

In our country, there are four public sector companies (The New India Assurance Company Limited, United India Insurance Company Limited, The Oriental Insurance Company Limited, National Insurance Company Limited). Moreover, private insurance companies have also come to play. Some of them are: Bajaj Allianz General Insurance Co. Ltd., Bharti AXA General Insurance Co. Ltd., Tata AIG General Insurance Co. Ltd. etc.

Important Concepts in General Insurance Business:

a. Premium:

- In the case of general insurance premium is to be recognized as income over the contract period.
- Unearned premium and premium received in advance both of which represent income not relating to the accounting period must be disclosed separately in the financial statements. Unearned premium is the premium for the period of unexpired risk. Premium received in advance represents the premium received prior to the commencement of risk. In other words, the premium relates entirely to subsequent accounting periods.

b. Reserve for unexpired risk

- This is applicable in General Insurance business only. Insurance business is peculiar in that the entire premium is received as on single day but the risk can arise on any day. In general insurance the policy is issued for a year which means the risk is covered for a year. Chances of the risk covered occurring do not come down proportionately with the passage of time.
- For example, if on the balance sheet date, the unexpired period of a particular policy is one month (eleven months having expired) we cannot say that the risk on the policy is reduced to 1/12th of the total risk. Even on the last day of the policy company's risk is as high as it was on the day the policy was issued.
- Keeping in view the nature of the business, the Executive Committee of the General Insurance Council has laid down that in the case of marine insurance the provision for unexpired risk should be 100% of the net premium and in the case of other businesses (like accident, fire, theft, etc.) the provision should be 50% of the net premium.
- The provision made on the balance sheet date will be shown on the debit side of the revenue account instead of subtracting from premia. The balance of provision also appears in the balance sheet on the liabilities side under the heading 'balance of funds and accounts'.

- This provision will be transferred to the credit side of next year's revenue account. Thus, in the revenue account the balance of the previous year appears on the credit side and the balance provided for the current year appears on the debit side.

a. **Claims:**

- If the risk falls on the insured then he makes a claim on the insurance company. This is the first item which appears on the debit side of revenue account. Claim is shown after deducting the Re-insurance claim and also after adjusting it in the light of information given in the problem.
- It may be noted that it is not the actual amount paid but the actual loss borne which is important for revenue account. In order to calculate the loss on account of claim the claim outstanding at the end is added and claim outstanding in the beginning is deducted.
- It should be noted that in keeping with the convention of conservatism, the claim intimated is taken at par with the claim intimated and accepted but not paid. Thus while calculating the claim outstanding at the end the claim intimated as well as the claim intimated and accepted both are considered.

b. **Bonus in reduction of premium:**

- In all the cases of general insurance the policy is always taken for one year and it is to be renewed after the expiry of the policy. Whether the policy is renewed with the same company, or a fresh policy is taken with some other company, it is a standing practice that the company usually grants a reduction in premium at the prescribed rate if the insured has not made any claim.
- This rate of reduction increases every year for usually three years if the insured does not make any claim continuously year after year. This reduction is called bonus in reduction of premium.
- Total premium (without reduction) should be treated as income and bonus which is subtracted should be treated as an expense.

<u>Example:</u> If net premium received is Rs.1,26,000, Bonus in reduction of premium is Rs.14,000
The revenue account on the credit side will show Rs.1,40,000 (Rs.1,26,000 + Rs.14,000) as income and on the debit side Rs.14,000 as an expense.

c. **Re-insurance**

- In case of Re-insurance first insurer cannot retain all the premium on the policy for himself. Depending on the share of risk undertaken by the second insurer, proportionate premium must be ceded by the first insurer.
- If such a policy matures, the claim will have to be shared by both the insurers in the agreed ratio. These adjustments will have to be shown in the accounts of both the insurers. In the accounts of the first insurer amount of claim recovered from the second insurer has to be

deducted from the total claim payable by him. Similarly, the premium ceded to the second insurer has to be deducted from the total premium received.

- In the accounts of the second insurer, claims paid include claims paid on account of Re-insurance and premiums received include premium received on reinsurance business.

d. Commission on re-insurance ceded /accepted

- When company gets re-insurance business it has to pay commission to some other company. This commission is called 'commission on re-insurance accepted' and is shown as an expense in the revenue account.
- When a company passes on a part of business to some other company then this company (which gives business) gets commission from the company to whom such business is given. This commission is called 'commission on re-insurance ceded' and is a gain to the company. It appears on the credit side of revenue account.

<u>IRDA Regulations Regarding Preparation of Financial Statements</u>

Schedule B-Part V: Preparation of Financial Statements

- An insurer shall prepare the Revenue Account, Profit and Loss Account [Shareholders' Account] and the Balance Sheet in Form B-RA, Form B-PL, and Form B-BS. Provided that an insurer shall prepare Revenue Account separately for fire, marine, and miscellaneous insurance business.

FORM B - RA

Revenue Account for the year ended 31st March, 20..

(To be prepared separately fire, marine and miscellaneous insurance)

Particulars	Schedule	Current Year (Rs. '000)	Previous Year (Rs. '000)
Premiums Earned (net) Interest, Dividend and Rent -Gross	1		
Total (A)			
Claims Incurred (Net)	2		
Commission	3		
Operating Expenses related to Insurance Business	4		
Others – To be specified			
Total (B)			
Operating Profit / (loss) from Fire/ Marine/ Miscellaneous Business (A-B)			

Profit and Loss Account (Form B-PL):

Profit and Loss Account of General Insurance Company is prepared to know the overall operating result of the company. It includes income from investment in the form of dividend, interest, rent etc. Similarly it also includes expenses relating to insurance business, bad debts, provision for doubtful debts, provision for taxation etc..

FORM B – PL

Profit & Loss Account for the year ended 31st March 20...

Particulars	Schedule	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Operating Profit/(Loss)			
(a) Fire Insurance			
(b) Marine Insurance			
(c) Miscellaneous Insurance			
2. Income from investments			
(a) Interest, Dividend & Rent-Gross			
(b) Profit on sale of investments			
Less: Loss on sale of investments			
3. Other income (To be specified)			
Total (A)			
4. Provisions (other than taxation)			
(a) For diminution in the value of investments			
(b) Others (to be specified)			
5. Other expenses			
(a) Expenses other than those related to Insurance Business			
Total (B)			
Profit Before Tax			
Less: Provision for Taxation			
Profit After Tax			
Less: Catastrophe Reserve			
Profit available for appropriation			

Particulars	Schedule	Current Year (Rs. '000)	Previous Year (Rs. '000)
Appropriations **(a) Interim Dividends paid during the year** **(b) Proposed Final Dividend** **(c) Dividend Distribution Tax** **(d) Transfer to any Reserves or Other Accounts (to be specified)**			
Balance of profit/loss brought forward from last year			
Balance carried forward to Balance Sheet			

Balance Sheet

FORM – B –BS

Balance Sheet as at 31st March, 20……..

Particulars	Schedule	Current Year (Rs. '000)	Previous Year (Rs. '000)
Sources of Funds:			
Shareholders' Funds:			
Share Capital	5		
Reserves and Surplus	6		
Borrowings	7		
Fair Value Change account			
Total			
Application of Funds:			
Investments	8		
Loans	9		
Fixed assets	10		
Current Assets:			
Cash and bank balance	11		
Advances and other assets	12		
Sub-total (A)			

Current Liabilities	**13**		
Provision	**14**		
Sub-total (B)			
Net Current Assets (C) = (A)- (B) Miscellaneous expenditure (to the extent not written-off or adjusted)	**15**		
Total			

Contingent Liabilities

Particulars	Schedule	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Partly paid-up Investments **2. Claims, other than against Policies, not acknowledged as Debts by the Company** **3. Underwriting Commitments Outstanding** **4. Guarantees given by or on behalf of the Company** **5. Statutory Demands/Liabilities in dispute, not provided for** **6. Re-insurance Obligations** **7. Others (to be specified)** **Total**			

<u>Schedules Forming Part of Financial Statements</u>

<u>Schedule 1- Premium Earned (Net)</u>

Particulars	Current (Rs. '000)	Previous (Rs. '000)
<u>Premium on risks undertaken during the year (direct & re-insurance accepted)</u> Premium received on Direct & re-insurance accepted		
Add: Receivable at the end of year (direct & re-insurance accepted)		
Less: Receivable at the beginning of year (direct & re-insurance accepted) <u>Less: Premium on re-insurance ceded:</u> Paid during the year Add: Payable at the end of year		
Less: Payable at the beginning of year		

Total Premium Earned (Net) Less: Adjustment for change in provision for Unexpired Risks Premium to be reported		

Schedule 2 - Claims Incurred (Net)

Claims Settled during the year	—
— Direct business	—
— Re-insurance acceptor	—
Add: Legal charges, if any	—
Add: Surveyor's charges	—
Less: Received from Re-insurance	—
Add: Estimated liability at the end of the year	—
Less: Estimated liability at the beginning of the year	—
Claims as expenses	xxxx

Schedule 3 - Commission

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
Commission paid		
Direct **Add:** Re-insurance Accepted **Less:** Commission on Re-insurance Ceded **Net Commission**		

Schedule 4 - Operating Expenses Related to Insurance Business

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1. Employees' remuneration & welfare benefits		
2. Managerial Remuneration		
3. Travel, Conveyance & Vehicle running expenses		
4. Rents, rates & taxes		
5. Repairs		
6. Printing & Stationary		
7. Communication expenses		
8. Legal & professional charges		

9. Medical fees		
10. Auditors' fees, expenses etc.		
(a) As auditor		
(b) As advisor or in any other capacity, in respect of		
(i) Taxation matters		
(ii) Insurance matters		
(iii) Management services; and		
(c) In any other capacity		
11. Advertisement and Publicity		
12. Interest & Bank Charges		
13. Others (to be specified)		
14. Depreciation		
Total		

Schedule 5 - Share Capital

Particulars	**Current Year (Rs. '000)**	**Previous Year (Rs. '000)**
1. Authorized Capital Equity Shares of Rs.each **2. Issued Capital** Equity Shares of Rs. each **3. Subscribed Capital** Equity Shares of Rs. each **4. Called-up Capital** Equity Shares of Rs. each **5. Less: Calls unpaid** **Add:** Equity shares forfeited (Amount originally paid up) **Less:** Preliminary expenses **[Expenses including commission or brokerage on underwriting or subscription of shares]** **Total**		

Schedule 5A-Share Capital Pattern of Shareholding

	Current Year		Previous Year	
	Number of Shares	% of Holding	Number of Shares	%of Holding
Promoters * **Indian**				
* **Foreign** **Others** **Total**				

Schedule 6 - Reserves and Surplus

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1. Capital Reserve **2. Capital Redemption Reserve** **3. Share Premium** **4. General Reserves** Less: Debit balance in Profit and Loss Account Less: Amount utilized for Buy-back **5. Catastrophe Reserve** **6. Other reserves (to be specified)** **7. Balance of Profit in Profit & Loss Account**		
Total		

Schedule 7 - Borrowings

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1. Debentures / Bonds		
2. Fixed Deposits		
3. Banks		
4. Financial Institutions		
5. Other entities carrying on insurance business		
6. Others (to be specified)		
Total		

Schedule 8 - Investments

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
Long-term Investments		
1. Government Securities and Government Guaranteed bonds including Treasury Bills		
2. Other Approved Securities		
3. Other Investments		
(a) Shares		
– Equity		
– Preference		
(b) Mutual Funds		
(c) Derivative Instruments		
(d) Debentures/Bonds		
(e) Other Securities (to be specified)		
(f) Subsidiaries		
(g) Investment Properties-Real Estate		
Short-term Investments		
1. Government Securities and Government Guaranteed bonds including Treasury Bills		
2. Other Approved Securities		
3. Other Investments		
(a) Shares		
– Equity		
– Preference		
(b) Mutual Funds		
(c) Derivative Instruments		
(d) Debentures/Bonds		
(e) Other Securities (to be specified)		
(f) Subsidiaries		
(g) Investments Properties-Real Estate		
Total Investments		
1. In India		

2. Outside India		
Total		

Schedule 9 - Loans

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
1. Security-Wise Classification:		
Secured:		
(a) On mortgage of property		
(i) In India		
(ii) Outside India		
(b) Other Shares, Bonds, Govt. Securities		
(c) Others (to be specified)		
Unsecured:		
Total		
2. Borrower-Wise Classification:		
(a) Central and State Governments		
(b) Banks and Financial Institutes		
(c) Subsidiaries		
(d) Others (to be specified)		
Total		
3. Performance-Wise Classification:		
(a) Loans classified as standard		
(i) In India		
(ii) Outside India		
(b) Non-performing loans less provisions		
(i) In India		
(ii) Outside India		
Total		
4. Maturity-Wise Classification:		
(a) Short Term		
(b) Long Term		

Total		

Schedule 10 - Fixed Assets

Particulars	Cost/Gross Block Depreciation				Depreciation				Net Block	
	Opening	Additions	Deductions	Closing	Upto Last Year	For the Year	On Sales/ Adjustments	To Date	As at year end	Previous Year
Goodwill Intangibles (specify) Land-Freehold Leasehold Property Buildings Furniture & Fittings Information Technology Equipment Vehicles Office Equipment Others (Specify nature)										
Total										
Previous Year										

Schedule 11 – Cash and Bank Balances

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Cash (including Cheques, Drafts and Stamps) **2. Bank Balances** **(a) Deposit Accounts** – Short-term (due within 12 months of date of Balance Sheet) – Others **(b)** Current Accounts **(c)** Others (to be specified) **3. Money at Call and Short Notice** **(a) With Banks** **(b) With other Institutions**		
4. **Others (to be specified)**		
Total		
Balances with Non-Scheduled banks included in 2 and 3 above **Cash & Bank Balances**		

1. In India **2. Outside India**		
Total		

Schedule 12 – Advances and other Assets

Particulars	Current Year (Rs.'000)	Previous Year (Rs.'000)
Advances **1.** Reserve deposits with ceding companies **2.** Advances to ceding companies **3.** Application money for investments **4.** Prepayments **5.** Advances to Officers/ Directors **6.** Advance tax paid & taxes deducted at source **7.** Others (to be specified)		
Total (A)		
Other Assets		
1. Income accrued on investments **2.** Outstanding Premiums **3.** Agents' Balances **4.** Foreign Agencies' balances **5.** Due from other Insurance Entities **6.** Due from subsidiaries/holding **7.** Reinsurance claims/balances receivable **8.** Deposit with Reserve Bank of India [Pursuant to Section 7 of Insurance Act,1938] **9.** Others (to be specified)		
Total (B)		
Total (A+B)		

Schedule 13 – Current Liabilities

Particulars	Current Year (Rs. '000)	Previous Year (Rs. '000)
1. Reserve for Licensed premium		
2. Agents Balances **3. Balances due to other insurance companies**		

4. Advances from Treaty Companies 5. Deposits held on re-insurance ceded **6. Premiums received in advance** **7. Sundry Creditors** **8. Due to subsidiaries/holding company** **9. Claims Outstanding** **10. Due to Officers/Directors** **11. Others (to be specified)** **Total**		

Schedule 14 – Provisions

Particulars	**Current Year (Rs. '000)**	**Previous Year (Rs. '000)**
1. Reserve for Unexpired risk **2. For taxation (less advance tax paid and taxes deducted at source)**		
3. For proposed dividends **4. For dividend distribution tax** 5. Others (to be specified) **Total**		

Schedule-15 Miscellaneous Expenditure (To the extent not written off or adjusted)

Particulars	**Current Year (Rs. '000)**	**Previous Year (Rs. '000)**
1. Discount Allowed in issue of shares/ debentures		
2. Others (to be specified) **Total**		

PROBLEMS FOR CLASSROOM DISCUSSSION

Problem No 1:

The Revenue Account of a life insurance company shows the life assurance fund on 31st March, 2021 at Rs. 62,21,310 before taking into account the following items:

(i) Claims covered under re-insurance Rs. 12,000.

(ii) Bonus utilized in reduction of life insurance premium Rs. 4,500.

(iii) Interest accrued on securities Rs. 8,260.

(iv) Outstanding premium Rs. 5,410.

(v) Claims intimated but not admitted Rs. 26,500.

What is the life assurance fund after taking into account the above omissions? **(Illustration 20)**

Problem No 2:

The life insurance fund of Prakash Life Insurance Co. Ltd. was Rs. 34,00,000 on 31st March, 2021. Its actuarial valuation on 31st March, 2021 disclosed a net liability of Rs. 28,80,000. An interim bonus of Rs. 40,000 was paid to the policyholders during the previous two years. It is now proposed to carry forward Rs. 1,10,000 and to divide the balance between the policyholders and the shareholders. Show (a) the Valuation Balance Sheet, (b) the net profit for the two-year period, and (c) the distribution of the profits. **(Illustration 21)**

Problem No 3:

From the following figures of Well Life assurance Co. Ltd. prepare a Valuation Balance Sheet and Profit Distribution Statement for the year ended 31st March 2022. Also pass necessary journal entries to record the above transactions with narrations:

Particulars	Rs. (in lakhs)
Balance of Life Assurance Fund as on 1.4.2021	167.15
Interim bonus paid in the valuation period	25.00
Balance of Revenue Account for the year ended 31.3.2022	240.00
Net Liability as per valuer’s Certificates as on 31.3.2022	165.00

The company declares a reversionary bonus of Rs.185 per Rs.1,000 and gave the policyholders an option to take bonus in cash Rs.105 per Rs.1,000. Total business conducted by the company was Rs.600 lakhs. The company issued profit policy only. 3/5th of the policyholders in value opted for cash bonus. **(Illustration 22)**

Problem No 4:

The following balances appeared in the books of Happy Mutual Life Assurance Society Ltd. as on 31 March 2014: **(Rs. in lakh)**

Dr. **Cr.**

Particulars	Rs.	Particulars	Rs.
Claims less reassurance paid during the year		Life Assurance Fund at the beginning of the year	1,00,000
By death	4,400	Premium less Re-assurances	30,000
By maturity	3,000	Claims less reassurances outstanding	
Annuities	12	At the beginning of the year:	
Furniture and Office Equipment at cost (including Rs.80 lakh bought during the year)	500	By death	1,800
		By maturity	1,200
		Credit balances pending adjustments	120
Printing and Stationery	154	Consideration for annuities granted	4
Cash with Bank in current account	2,700	Interest, dividends and rents	3,600
Cash and stamp in hand	60	Registration and other Fees	4
Surrenders less Reassurances	80	Sundry Deposits	200
Commission	500	Taxation Provision	600
Expenses of Management	6,200	Premium Deposits	2,300
Sundry Deposits with insurance Companies	2	Sundry Creditors	700
		Contingency Reserve	300
Advance Payment of Tax	100	Furniture and Office Equipment Depreciation Account	80
Sundry Debtors	100		
Agents Balances	200	Building Depreciation Account	600
Income Tax	900		
Income Tax on Interest, Dividend and Rents	1,000		
Loans and Mortgages	300		
Loans on Policies	6,500		
Investments	1,04,000		
(Rs.500 lakh deposited with Reserve Bank of India)			
House Property at Cost (including Rs. 170 lakh added during the year)	10,800		
	1,41,508		1,41,508

From the foregoing balances and the following information, prepare the Balance Sheet of Happy Mutual Life Assurance Society Ltd. as on 31st March 2014 and its Revenue Account for the year ended on that date:

1. Claims less reassurance outstanding at the end of the year: By death Rs. 1,200 lakh, By maturity Rs. 800 lakh.
2. Expenses outstanding Rs. 120 lakh and prepaid Rs. 30 lakh.
3. Provide Rs. 90 lakh for depreciation on buildings, Rs.30 lakh for depreciation on furniture and office equipment and Rs. 220 lakh for taxation.
4. Premiums outstanding Rs.4,056 lakh, commission thereon Rs. 130 lakhs.
   Interests, dividends and rents outstanding (net) Rs. 60 lakh and interests and rents accrued (net) Rs.700 lakh. **(Illustration 23)**

Problem No 5:

From the following, you are required to calculate the loss on account of claim to be shown in the revenue account for the year ending 31st December, 2021:

Claims:

Intimated in	Admitted in	Paid in	Rs.
2020	2020	2021	15,000
2021	2021	2022	10,000
2019	2020	2020	5,000
2019	2020	2021	12,000
2021	2022	2022	8,000
2021	2021	2021	1,02,000

Claim on account of re-insurance was Rs.25,000 **(Illustration 24)**

Problem No 6:

Khush Raho Insurance Co. Ltd. furnishes you the following information:

(i). On 31.3.2013 it had reserve for unexpired risks to the tune of Rs.100 crore. It comprised of Rs. 37.5 crore in respect of machine insurance business; Rs.50 crore in respect of fire insurance business and Rs.12.5 crore in respect of miscellaneous insurance business.

(ii). It is the practice of Khush Raho Insurance Co. Ltd. to create reserve at 100% of net premium income in respect of marine insurance policies and at 50% of net premium in respect of fire and miscellaneous insurance business.

(iii). During the year 31st March, 2014 the following business was conducted :

Particulars	Marine (Rs. crores)	Fire (Rs. crores)	Miscellaneous (Rs. crores)
Premia collected from : **(a)** Insured (other than insurance companies) in respect of policies issued	45	107.5	30
(b) Other insurance companies in respect of risks undertaken	17.5	12.5	10
Premia paid/payable to other insurance companies on business ceded	16.75	10.75	17.5

Khush Raho Insurance Co. Ltd. asks you to :

(i). Pass journal entries relating to "unexpired risks reserve"

(ii). Show in columnar form Unexpired Risks Reserve Account for the year ended 31st March, 2014.

(Illustration 25)

Problem No 7:

From the following figures appearing in the books of Fire Insurance division of a General Insurance Company, show the amount of claim as it would appear in the Revenue Account for the year ended 31st March, 2014 :

Particulars	Direct Business	Re-Insurance
	Rs.	Rs.
Claim paid during the year	46,70,000	7,00,000
Claim Payable — 1st April, 2013	7,63,000	87,000
31st March, 2014	8,12,000	53,000
Claims received	–	2,30,000
Claims Receivable — 1st April, 2013	–	66,000
31st March, 2014	–	1,13,000
Expenses of Management	2,30,000	–
(includes Rs. 35,000 Surveyor's fee and Rs. 45,000		
Legal expenses for settlement of claims)		

(Illustration 26)

Problem No 8:

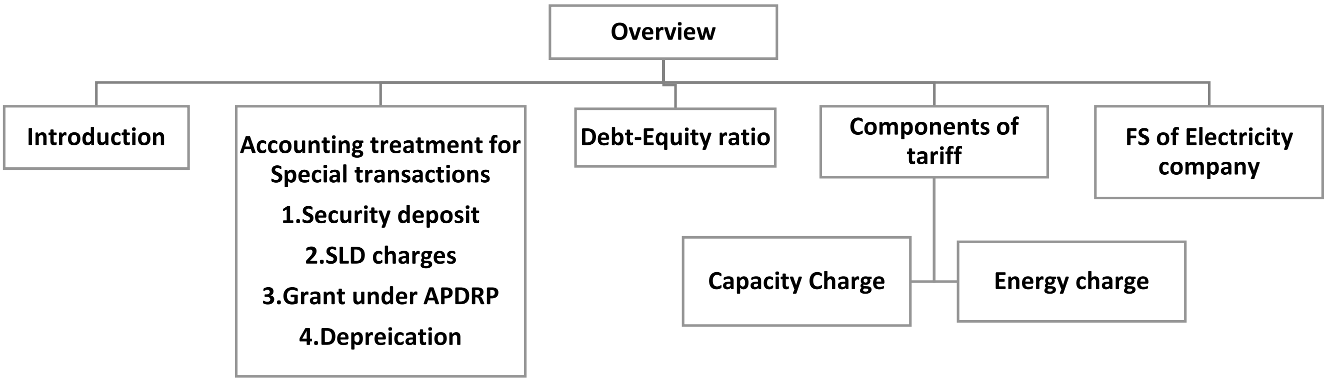
Prepare the Fire Insurance Revenue A/c as per IRDA regulations for the year ended 31st March, 2014 from the following details:

Particulars	Rs.

Claims paid	4,90,000
Legal expenses regarding claims	10,000
Premiums received	13,00,000
Re-insurance premium paid	1,00,000
Commission	3,00,000
Expenses of management	2,00,000
Provision against unexpired risk on 1st April, 2013	5,50,000
Claims unpaid on 1st April, 2013	50,000
Claims unpaid on 31st March, 2014	80,000

Create Reserve for Unexpired Risk @ 50%. **(Illustration 27)**

12. ACCOUNTS OF ELECTRICITY COMPANY



Introduction:

India is the third-largest producer and second-largest consumer of electricity worldwide, with an installed power capacity of 395.07 GW, as of January 2022. This huge demand of electricity is met by the power generation and distribution companies in India which includes thermal power generating companies, hydro power generating companies and companies producing power from other renewable sources.

Regulatory Framework for Electricity Companies:

In India, administration including accounting of electricity companies is guided by the Electricity Act, 2003. The Electricity Act, 2003 replaced the following erstwhile existing legislations, namely:

a. The Indian Electricity Act, 1910;

b. The Electricity (Supply) Act, 1948; and

c. The Electricity Regulatory Commissions Act, 1998.

Role of Central Electricity Regulatory Commission (CERC)/ State Electricity Commission (SEC):

- The CERC/SEC shall be a body corporate, having perpetual succession and a common seal with power to acquire, hold and dispose of property, both movable and immovable, and to contract and shall, by the said name, sue or be sued.
- The functions of CERS/SEC include regulating the tariff of generating companies, the inter-state transmission of electricity, to issue licenses, to levy fees, to fix trading margin etc.

Accounting in Electricity Companies

Accounting of Some Special Transactions

1. Accounting and Reporting of Security Deposit

a. The Distribution Licensee may require the consumer to deposit sufficient security against the estimated payment which may become due to him in respect of electricity supplied to the consumer.

b. The Distribution Licensee shall pay interest equivalent to the Bank Rate or more, as may be specified by the concerned State Commission.

c. The journal entries in the books of a distribution licensee will be as follows:

Date	Particulars	Dr. (Rs.)	Cr. (Rs.)
	(i) <u>On Receipt of Security Deposit</u> Bank A/c Dr. To Security Deposit A/c (Being the Security Deposit received)		
	(ii) <u>On Making Provision for Interest Accrued on Security Deposit</u> Interest Expense A/c Dr. To Interest Accrued on Security Deposit A/c (Being the Provision for Interest Accrued on Security Deposit Made)		
	(iii) <u>On Adjustment of Interest Accrued on Security Deposit in Consumer's Bill</u> Interest Accrued on Security Deposit A/c Dr. To Sales Turnover A/c (Being the Adjustment of Interest Accrued on Security Deposit in Consumer's Bill)		

d. Balance of Security Deposit A/c at the end of the accounting period should be disclosed as a Non- current Liability in the Balance Sheet as the same is, in substance, not repayable within a period of 12 months from the reporting date.

e. Balance of Interest Accrued on Security Deposit A/c at the end of the accounting period should be disclosed as Non-current Liability in the Balance Sheet.

f. Security Deposit = Load × Load Factor of the category in which the consumer falls x (Billing cycle + 45 days) × Current tariff.

2. Accounting for Service Line cum Development (SLD) Charges Received from Consumers

The Service Line cum Development (SLD) Charges can be accounted and reported under any one of the following methods:

Accounting Practice 1: SLD is accounted for as a liability and subsequently proportionate amount is transferred to Income Statement during the expected life of the Asset.

Accounting Practice 2: SLD is accounted for as Reserve as the amount is not refundable and disclosed under the head Reserves and Surplus without transferring any proportionate amount to Income Statement during the expected life of the Asset.

Accounting Practice 3: SLD is accounted for as Capital Reserve as the amount is not refundable and subsequently proportionate amount is transferred to Income Statement during the expected life of the Asset to match against depreciation on total cost of such asset.

Under this method, the journal entries in the books of the Distribution Licensee will be as follows:

In the books of Distribution Licensee -Journal

		Dr.	**Cr.**
Date	**Particulars**	**(Rs.)**	**(Rs.)**
	(i) On Receipt of SLD Charges Bank A/c Dr. To Capital Service Line Contribution A/c (Being the SLD Charges received)		
	(ii) On Transfer of Proportionate Amount to Income Statement Capital Service Line Contribution A/c Dr. To Statement of Profit and Loss (Being the Transfer of Proportionate amount to the Income Statement)		

Accounting Practice 4 (Most commonly used): SLD is accounted for as reduction in the cost of Non-Current Asset and depreciation is provided on such reduced cost.

3. Accounting for Grant Received under APDRP (Currently R-APDRP)

a. Grant received under the Accelerated Power Development and Reforms Programme (APDRP) of the Ministry of Power, Government of India towards capital expenditure is treated as capital receipt and accounted as Capital Reserve and subsequently adjusted as income (by transfer to the Statement of Profit and Loss) in the same proportion as the depreciation written off on the assets acquired out of the grant.

b. The depreciation for the year to be debited to the Statement of Profit and Loss on asset acquired out of grant to match against portion of grant transferred from Capital Reserve.

c. The unadjusted balance of Capital Reserve is disclosed under the head, Reserves and Surplus, in the Balance Sheet.

4. Accounting for Depreciation

With respect to accounting for depreciation, the following points are noteworthy:

a. In Central Electricity Regulatory Commission (Terms and Conditions of Tariff) Regulations, 2019, the rates have been specified in Appendix – I of the Regulation. These rates of depreciation shall be applicable for the purpose of tariff as well as accounting.

b. The CERC prescribes the Straight-Line Method and at rates specified in Appendix – I for the assets of the generating station and transmission system, from the effective date of commercial operation of the station shall be spread over the balance useful life of the assets.

Calculation of Depreciation for the Purpose of Tariff as per 2019 Regulation

i) The value base for the purpose of depreciation shall be the capital cost of the asset.

ii) Land other than the land held under lease shall not be a depreciable asset and its cost shall be excluded from the capital cost while computing depreciable value of the asset.

iii) Depreciation shall be calculated annually, based on Straight Line Method over the useful life of the asset and at the rates prescribed in Appendix I to the Regulation.

iv) Depreciation shall be chargeable from the first year of operation. In case of operation of the asset for part of the year, depreciation shall be charged on pro-rata basis.

Appendix – I of Central Electricity Regulatory Commission (Terms and Conditions of Tariff) Regulations, 2019

Sr. No.	Asset Particulars	Depreciation Rate (Salvage Value = 10%) SLM
A	Land under full ownership	0.00%
B	Land under lease	3.34%
C	Assets purchased new	
a.	Plant and Machinery in generating stations	5.28%
b.	Cooling towers and circulating water systems	5.28%
c.	Hydraulic works forming part of the Hydro-generating stations	5.28%
d.	Building and civil engineering works	
	Temporary erections such as wooden structures	100%
	Others	3.34%

e.	Transformers, Kiosk, sub-station equipment & other fixed apparatus (including plant)	5.28%
f.	Switchgear including cable connections	5.28%
g.	Lightning arrestor	5.28%
h.	Batteries	5.28%
i.	Overhead lines including cable support	5.28%
j.	Meters	5.28%
k.	Self-propelled vehicles	9.50%
l.	Air Conditioning Plants	
	Static	5.28%
	Portable	9.50%
m.	Office furniture and furnishing	
	Street Light fittings	5.28%
	Others	6.33%
n.	Apparatus let on hire	
	Other than motor	9.5%
	Motor	6.33%
o.	Communication equipment	6.33%
p.	I. T Equipment including software	15.00%
q.	Any other assets not covered above	5.28%

How to Calculate Weighted Average Rate of Depreciation

Step 1: Calculate Depreciation on Individual Assets (other than Freehold Land) at the Rates as per Appendix I. Cost of the Asset x Prescribed Rate of Depreciation.

Step 2: Calculate Total Depreciation on All Assets (other than Freehold Land). i.e., is the sum total of depreciation calculated on each asset. Depreciation on Asset1 + Depreciation on Asset2 + ⋯⋯⋯

Step 3: Calculate Total Capital Cost of All Assets (other than Freehold Land).

Step 4: Calculate Weighted Average Rate of Depreciation.

$$\frac{\text{Total depreciation on all assets (other than freehold land)}}{\text{Total capital cost of all assets (other than freehold land)}} \times 100$$

The weighted average rate of depreciation is used in tariff calculation.

Debt-Equity Ratio

- The Capital cost of the generating station determined by the Commission after prudence check in accordance with these regulations shall form the basis for determination of tariff for existing and new projects.
- For new projects, the debt-equity ratio of 70:30 as on date of commercial operation shall be considered. If the equity actually deployed is more than 30% of the capital cost, equity in excess of 30% shall be treated as normative loan. Where equity actually deployed is less than 30% of the capital cost, actual equity shall be considered for determination of tariff.

Components of Tariff (A Thermal Generating Station)

As per Regulation 14 of Central Electricity Regulatory Commission Regulations, 2019, the tariff for supply of electricity from a thermal generating station shall comprise two parts, namely, capacity charge (for recovery of annual fixed cost) and energy charge (for recovery of primary and secondary fuel cost and cost of limestone and any other reagent).

a. **Capacity Charges:** The capacity charges shall be derived on the basis of annual fixed cost. The Annual Fixed Cost (AFC) of a generating station shall consist of the following components:
   (i) Return on equity;
   (ii) Interest on loan capital;
   (iii) Depreciation;
   (iv) Interest on working capital; and
   (v) Operation and maintenance expenses.
b. **Energy Charges:** Energy charges shall be derived on the basis of the landed fuel cost (LFC) of a generating station and shall consist of the following cost:
   (i) Landed Fuel Cost of primary fuel;
   (ii) Cost of secondary fuel oil consumption; and
   (iii) Cost of limestone or any other reagent, as applicable.

Return on Equity

- Return on equity shall be computed in rupee terms, on the equity base determined in accordance with Regulation 18 of these regulations. The normative equity base for this purpose will be 30% of the capital cost.
- Return on equity shall be computed at the base rate of 15.50% for thermal generating station, and run-of-river hydro generating station, and at the base rate of 16.50% for the storage type hydro generating stations.

Calculation of ROE:

Statement showing Return on Equity at Normal Rate

Sr.No.	Particulars	Year 1	Year 2	Year 3
1	2	3	4	5
1	Gross Opening Equity (Normal)			
2	Less: Adjustment in Opening Equity			
3	Adjustment during the year			
4	Net Opening Equity (Normal)			
5	Add: Increase in equity due to addition during the year			
6	Less: Decrease due to De-capitalization during the year			
7	Less: Decrease due to reversal during the year			
8	Add: Increase due to discharges during the year			
9	Net closing Equity (Normal)			
10	Average Equity (Normal)			
11	Rate of ROE			
12	Total ROE			

Interest on Loan Capital

- The loans arrived at in the manner indicated in Regulation 18 of these regulations shall be considered as gross normative loan for calculation of interest on loan. Gross normative loan is 70% of the capital cost.
- The normative loan outstanding as on 1.4.2019 shall be worked out by deducting the cumulative repayment as admitted by the Commission up to 31.3.2019 from the gross normative loan.
- The interest on loan shall be calculated on the normative average loan of the year by applying the weighted average rate of interest.

Interest on Working Capital

- The working capital shall cover cost of fuel stock, advance payment towards such cost, cost towards secondary fuel oil stock, maintenance spares, receivables and operation and maintenance expenses including water charges and security expenses, for one month.
- Rate of interest on working capital shall be on normative basis and shall be considered as the bank rate as on 1.4.2019 or as on 1st April of the year during the tariff period 2019-24 in which the generating station is declared under commercial operation, whichever is later.
- Calculation of interest on working capital:

Statement of Interest on Working Capital

Sr. No.	Particulars	Year 1	Year 2	Year 3
1	2	3	4	5
1	Cost of Coal/Lignite			
2	Cost of Secondary Fuel Oil			
3	Fuel Cost			
4	Liquid Fuel Stock			
5	O & M Expenses			
6	Maintenance Spares			
7	Receivables			
8	Total Working Capital			
9	Rate of Interest			
10	Interest on Working Capital			

Operation and Maintenance Expenses

It will include normative operation and maintenance expenses. In addition, the Water Charges, Security Expenses and Capital Spares for thermal generating stations shall be allowed separately.

Preparation of Financial Statements of an Electricity Company

The financial statements of an insurance company are prepared as per Schedule III of the Companies Act,2013.

PROBLEMS FOR CLASS ROOM DISCUSSION

Problem No.1:

Consider the following information provided by ABC Power Supply Company Ltd.

Security deposit received from a customer on 01.10.2020 for Rs.2,00,000. Interest rate applicable was 8% for 2020-21 and 9% for 2021-22. The accrued interest for the year is adjusted against the bill for the immediate next quarter. Journalize the above transaction for 2020-21 and 2021-22.

(Illustration 13)

Problem No.2:

From the following calculate Weighted Average Rate of Depreciation considering the rates as per Appendix-I.

Assets	Closing Balance at Cost (Rs.)
1. Land under full ownership	14,30,000
2. Land under Lease	4,30,000
3. (a) Building & Civil Engineering Works other than Kutcha Roads	33,00,000
(b) Railways Sidings	40,00,000
(c) Temporary Erections such as Wooden Structures	10,00,000
4. IT Equipment	20,00,000
5. Self-Propelled Vehicles	30,00,000
6. Portable Air Conditioning Plants	25,00,000
7. (a) Apparatus other than Motors let on hire	15,00,000
(b) Motors let on hire	2,00,000
8. Communication Equipment	5,00,000
9. Office Furniture, Furnishing, Equipment, Fittings & Apparatus	5,00,000
10. Plants & Machinery in generating stations	2,52,00,000
11. Cooling Towers & Circulating Water Systems	10,00,000
12. Hydraulic Works Forming part of the Hydro-dams, etc.	20,00,000
13. Transformers & Switchgear	2,05,00,000
14. Lighting Arrestor, Batteries, Overhead lines including c able support	42,00,000
15. Meters	20,00,000
16. Static Air Conditioning Plants	1,00,00,000

17. Street Light Fittings	47,85,000
18. Vehicles other than Self Propelled Vehicles	2,15,000

(Illustration 14)

Problem No.3:

Consider the following information provided by XYZ Power Supply Company Ltd. (Rs. in lakhs):

Gross opening equity Rs.3,000 as on 01.04.2019.

Adjustment in opening equity – Nil

Adjustment during the year – Nil

Increase in equity due to addition during the year (over 5 years): Rs.500

Decrease due to reversal and de-capitalization (over 5 years): Nil

Increase due to discharges during the year: Nil

Rate of ROE: 18%

Calculate total ROE for the next five years. **(Illustration 15)**

Problem No.4:

From the following information Calculate Return on Equity:

1. Date of Commercial Operation of COD = 1st April 2019
2. Approved Opening Capital Cost as on 1st April 2019 = Rs.15,00,000
3. Details of allowed Additional Capital Expenditure:

	1st year	2nd year	3rd year	4th year
Additional Capital Expenditure (Allowed)	1,00,000	30,000	20,000	10,000

Rate of ROE: 15.5% **(Illustration 16)**

Problem No.5:

Consider the following estimated information provided by XYZ Power Supply Company Ltd. (Rs. In lakhs) for the next 5 years:

Cost of coal: Rs.2,000 per year

Cost of secondary fuel oil: Rs.200 per year for first 2 years and Rs.300 per year for 3-5 years

O and M expenses: Rs.250 per year for first 2 years and Rs.350 per year for 3-5 years

Maintenance spares: Rs.100 per year

Receivables: Rs.1,800 per year

Rate of interest: 12%

Calculate the interest on working capital. **(Illustration 17)**

Problem No.6:

Consider the following estimated information provided by XYZ Power Supply Company Ltd. (Rs. in lakhs) for the next 5 years:

Normative O & M expenses: Rs.2500 for Year 1 and this will increase @10% per year. Water Charges: Rs.500 for year 1 and 2 and it will increase @20% per year thereafter. Security expenses: Rs.750 per year up to year 4 and Rs.800 for 5th year.

Calculate total O & M expenses for five years. **(Illustration 18)**

Problem No.7:

The trial balance of MM Electric Supply Ltd. For the year ended 31st March, 2021 is as below:

Particulars	Dr. Balances Amount (Rs. in '000)	Cr. Balances Amount (Rs. in '000)
Share Capital:		
Equity Shares of Rs.10 each		50,000
14% Preference Shares of Rs.100 each		15,000
Patents and trade mark	2,504	
15% Debentures		24,700
16% term loan		15,300
Land (additions during the year 20,50)	12,450	
Building (additions during the year 50,80)	35,134	
Plant & Machinery	57,058	
Mains	4,524	
Meters	3,150	
Electric al Instruments	1,530	
Office Furniture	2,450	
Capital Reserve		4,020
Contingency Reserves		12,030
General Reserve		1,000
Transformers	16,440	
Opening Balance of Profit & Loss Account		350
Profit for the year 2012-13 subject to adjustments		17,100
Stock in hand	12,050	
Sundry Debtors	6,246	

Contingency Reserve Investments:		
SBI Bonds-2020	10,010	
Other Investments	2,000	
Cash & Bank	3,254	
Public lamps	3,040	
Depreciation Fund		25,816
Sundry Creditors		6,524

During 2020-21, 1,00,000, 14% Preference Shares were redeemed at a premium of 10% out of proceeds of fresh issue of equity shares of necessary amounts at a premium of 10%.

Adjustments:

a. Transfer to Contingency Reserve Rs. 1,70,000 & to General Reserve Rs. 2,00,000

b. Loss on Contingency Reserve Investment Rs. 10,000

c. Make a Provision for debts considered doubtful of Rs.1,014,000.

You are required to prepare the balance sheet as on 31st March, 2013 as per the schedule III.

(Illustration 19)

COMMON QUESTIONS FROM BANKING, INSURANCE AND ELECTRICITY COMPANY ACCOUNTS

Multiple Choice Questions

1. Rate of provisioning for advances doubtful for more than 1 year but less than 3 years is

A. 25%

B. 40%

C. 60%

D. 100%

2. Balance of Interest Accrued on Security Deposit A/C of an electricity company should be shown

A. Under Current Liability

B. Under Non-current Liability

C. Under Current Asset

D. Under Non-current Asset

3. A Banking Company needs to transfer a minimum of___of its profit to reserve fund.

A. 10%

B. 15%

C. 20%

D. 25%

4. In case of an electricity company, depreciation on assets is calculated based on the rates notified by

A. Companies Act 2013

B. State Electricity Commission

C. Central Electricity Regulatory Commission

D. Income Tax Act 1961

5. A banking company is required to maintain_provision on unsecured portion of doubtful advances.

A. 25%

B. 40%

C. 50%

D. 100%

6. Which of the following is a principle of insurance?

A. Principle of indemnity

B. Insurable interest.

C. Principle of uberrimae fidei.

D. All of the above

7. In case of an Electricity Company, balance of Security Deposit A/c at the end of the accounting period should be disclosed as

A. A current liability in the Balance Sheet

B. A non-current liability in the Balance Sheet

C. A current asset in the Balance Sheet

D. A non-current asset in the Balance Sheet

8. Which of the following is not a mandatory financial statement of a General Insurance Company as per IRDA regulations?

A. Revenue Account

B. Profit and Loss Account

C. Balance Sheet

D. Cash Flow Statement

9. Which of the following is/are a part of General Ledger of a Banking Company?

A. Control Accounts of all personal ledgers.

B. Profit and Loss Account.

C. Assets' Accounts.

D. All of the above.

10. Rate of provision on advances doubtful for more than 3 years is___.

A. 40%

B. 25%

C. 100%

D. Nil

[Answers: 1-B; 2-B; 3-D; 4-C; 5-D; 6-D; 7-B; 8-D; 9-D; 10-C]

<u>State True or False</u>

1. Every banking company incorporated in India is required to transfer at least 15% of its profit to the reserve fund.

2. A bank can maintain Cash reserve with itself or by way of a balance in the Current account with the reserve bank or by way of net balance in current accounts or in one or more of the aforesaid ways.

3. Every banking company is required to submit a return in the prescribed form and manner to the Reserve Bank of India at the end of each calendar year of all accounts in India which could not be operated for 5 years.

4. Non-performing assets bear a little amount of risk like normal risk and they do not create any trouble regarding their realization.

5. The Electricity Act, 2003 replaced four existing legislations.

6. The Central Electricity Regulatory Commission shall consist of a chairperson and 3 Members

7. In case of Electricity Company, Balance of Security Deposit A/c at the end of the accounting period should be disclosed as a Non-current liability in the Balance Sheet.

8. The value base for the purpose of depreciation for the purpose of Tariff as per Regulation 21 shall be the historical cost of the asset.

9. When the same risk and the same subject matter is insured with more than one insurer, i.e., more than one insurance company, the same is called Re-insurance Insurance.

10. Income from non-performing assets of a bank is recognized on cash basis.

[Answer: 1.False; 2.True; 3.False; 4. False; 5.False; 6.True; 7.True; 8.True; 9.False; 10.True]

<u>Fill in the Blanks</u>

1. Sometimes the insurer considers a particular risk too much for his capacity and may a part of the risk with some other insurer.

2. Bonus paid at the end along with the policy amount to the policy holders is called ______.

3. In the case of a___insurance business claim will arise either on death or maturity of policy.

4. In relation to an Electricity Company the amount of Security Deposit = Load × Load Factor of the category in which the consumer falls ×__× Current tariff.

5. ___ advance means where a bank grant advance to its customers against any tangible security.

6. Losses of theft are covered by___insurance.

7. The___Fund is available to meet the aggregate liability on all policies outstanding.

8. Revenue Account of life Insurance Business is relevant with Form -.

9. In case of Insurance company the date of discharge of claim is mentioned in the register of__.

10. Rebate on Bills Discounted = Amount of Bill × Rate of Discount ×__.

[Answer: 1.Re-insurance; 2.Revesionary Bonus; 3.Life; 4.(Billing cycle + 45 days); 5.Secured; 6.Burglary; 7.Life Assurance; 8.A – RA; 9.Claims;10.Unexpired Period/12]

Numerical Multiple-Choice Questions

A. Given, Amount of bill- 49232, Date of bill 15.01.2022, Period- 5 months, Rate of discount- 8% Calculate rebate on bill discounted, if accounting year ends on 31.03.22.

   A. Rs. 852.46

   B. Rs. 818.85

   C. Rs. 873.22

   D. Rs. 825.45

2. If a loan is identified to be a sub-standard advance with secured exposure of Rs. 200 lakh and unsecured portion of Rs. 300 lakh, calculate the provision at applicable rate in case of a banking company.

   A. Rs. 80 lakh

   B. Rs. 85 lakh

   C. Rs. 90 lakh

   D. Rs. 95 lakh

[Answer: 1-A; 2-C]

Short Essay Type Questions:

1. Discuss about the regulatory restrictions on banking companies in respect of payment of dividend.

2. Discuss about the regulatory restrictions on banking companies in respect of loans and advances.

3. What are the books of accounts to be maintained by a bank?

4. How will you account for Service Line cum Development (SLD) Charges Received from Consumers Accounting Practices?

5. How will account for the grant received by an Electricity Company under R-APDRP?

6. What is the purpose of Valuation Balance Sheet?

7. Write a short note on Life Assurance Fund.

8. What do you mean by Bonus in Reduction of Premium?

Essay Type Questions:

9. What is rebate on bills discounted? How will you adjust the same in the books of a banking company?

10. Discuss about the provisioning requirement in case of banking company on performing and non-performing assets.

11. What do you mean by Security Deposit in case of an Electricity Company? How will you treat the same in the books?

12. Discuss various principles of Insurance.

13. Differentiate between life and non-life insurance policy.

14. What do you mean by Valuation Balance Sheet? Discuss its purpose.

13. INTRODUCTION TO IND AS AND CONCEPTUAL FRAME WORK BASED ON IND AS

NEED FOR CONVERGENCE TOWARDS GLOBAL STANDARDS:

1. Multi -national corporations in search of money, to sustain on-going activities has necessitated raising of capital from all parts of the world. Each country has its own set of rules and regulations for accounting and financial reporting. Therefore, when an enterprise decides to raise capital from the markets other than the country in which it is located, the rules and regulations of that other country will apply and this in turn will require that the enterprise is in a position to understand the differences between the rules governing financial reporting in the foreign country as compared to its own country of origin. Therefore, translation and reinstatements are of utmost importance in a world that is rapidly globalising in all ways.
2. International analysts and investors would like to compare financial statements based on similar ASs, and this has led to the growing need for an internationally accepted set of ASs for cross-border filings.
3. The harmonization of financial reporting around the world will help to raise confidence of investors, generally, in the information they are using to make their decisions and assess their risks.
4. A strong need was felt by legislation to bring about uniformity, rationalisation, comparability, transparency and adaptability in financial statements. Having a multiplicity of types of ASs around the world is against the public interest.

INTERNATIONAL ACCOUNTING STANDARD AUTHORITIES:

1. With a view of achieving the objective of setting global standards, the London based group namely the International Accounting Standards Committee (IASC), responsible for developing International Accounting Standards (IAS), was established in June, 1973. It is presently known as International Accounting Standards Board (IASB). The IASC comprises the professional accountancy bodies of over 75 countries (including the ICAI).
2. Between 1997 and 1999, the IASC restructured their organisation, which resulted in formation of IASB. The standards issued by IASC Board till 31.03.2001 are known as IASs and the standards issued by IASB since 01.04.2001 are known as IFRSs.

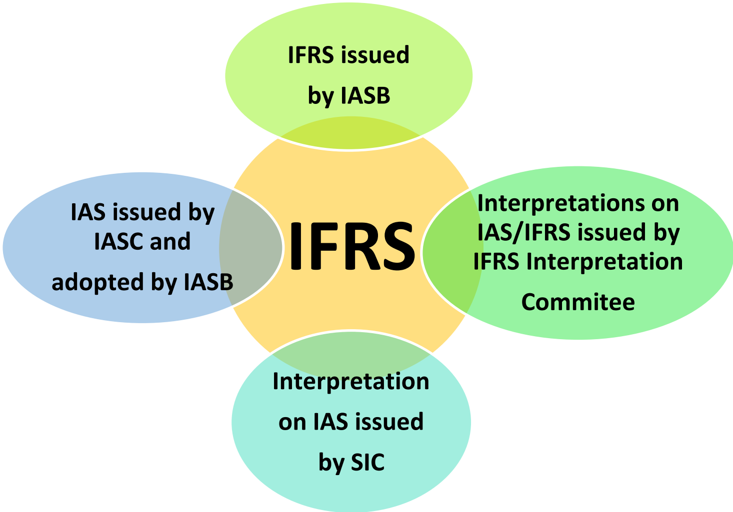
INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) AS GLOBAL STANDARDS:

The term International Financial Reporting Standards (IFRS) comprises

1) IFRS issued by IASB;

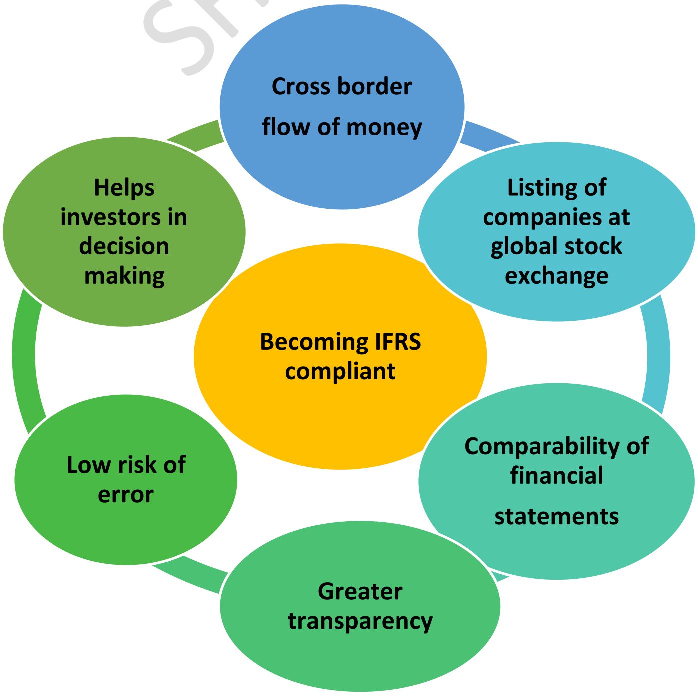
2) IAS issued by IASC;

3) Interpretations issued by the Standard Interpretations Committee (SIC) and the IFRS Interpretations Committee of the IASB.



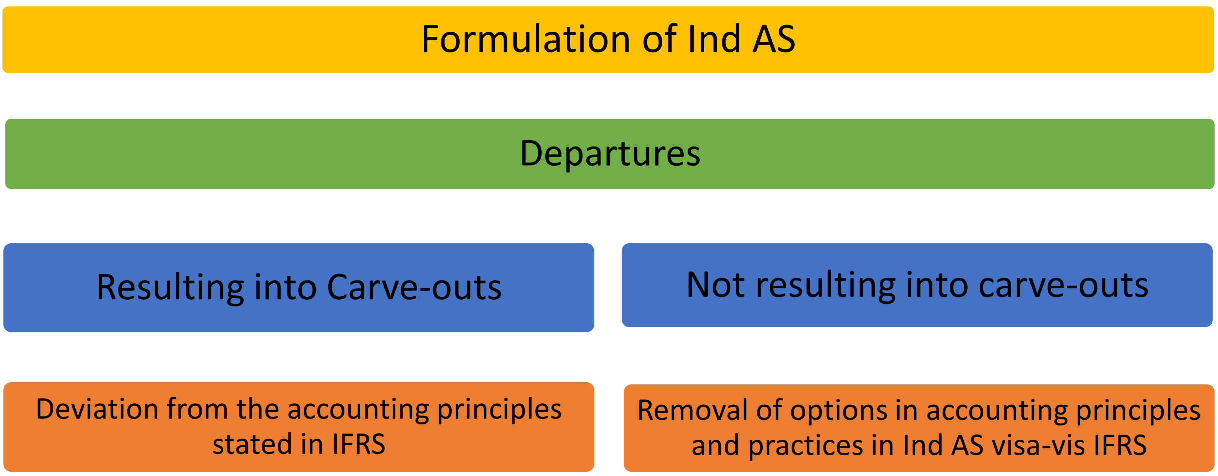
BECOMING IFRS COMPLIANT:

Any country can become IFRS compliant either by adoption process or by convergence process. Adoption would mean that the country sets a specific timetable when specific entities would be required to use IFRS as issued by the IASB. Convergence means that the country will develop high quality, compatible accounting standards and there would be alignment of the standards of different standard setters with a certain rate of compromise, by adopting the requirements of the standards either fully or partially.

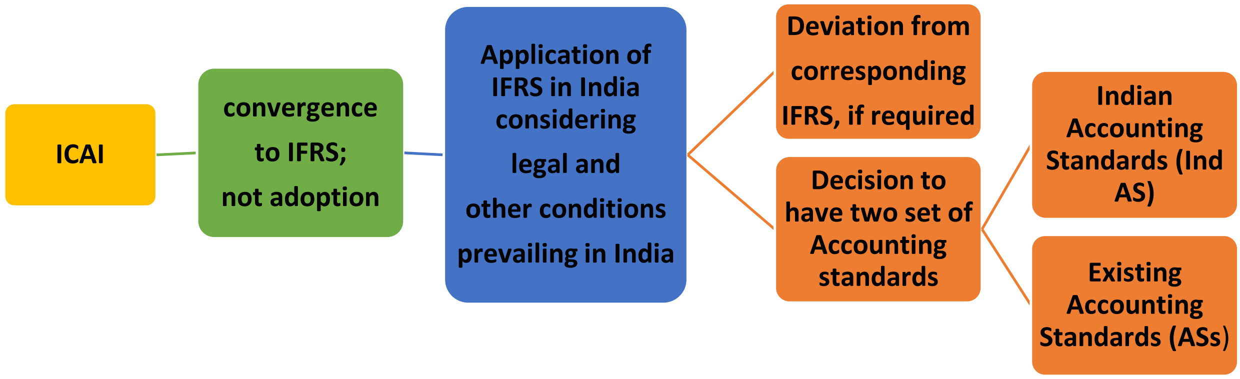


WHAT ARE IND AS?

1) The Government of India in consultation with the ICAI decided to converge and not to adopt IFRS issued by the IASB. Ind AS are IFRS converged standards issued by the Central Government of India under the supervision and control of ASB of ICAI and in consultation with NFRA.
2) Ind AS are named and numbered in the same way as the corresponding IAS. However, for Ind AS corresponding to IFRS, one need to add 100 to the IFRS number. For example IFRS 1 corresponding Ind AS number is 101.
3) Accordingly, while formulating Ind AS, efforts have been made to keep these Standards, as far as possible, in line with the corresponding IAS/IFRS and departures have been made where considered absolutely essential. Such changes related to
   - **A.** Various terminology related changes have been made to make it consistent with the terminology used in law, e.g., 'statement of profit and loss' in place of 'statement of comprehensive income' and 'balance sheet' in place of 'statement of financial position'.
   - **B.** Removal of options in accounting principles and practices in Ind AS vis-a-vis IFRS, have been made to maintain consistency and comparability of the financial statements to be prepared by following Ind AS. However, these changes will not result into carve outs.
   - **C.** Certain changes have been made considering the economic environment of the country, which is different as compared to the economic environment presumed to be in existence by IFRS. These differences are due to differences in economic conditions prevailing in India. These differences which are in deviation to the accounting principles and practices stated in IFRS, are commonly known as 'Carve-outs'.
   - **D.** Additional guidance given in Ind AS over and above what is given in IFRS, is termed as 'Carve in'.



INDIAN SCENARIO WITH RESPECT TO STANDARDS:



ROADMAP FOR IMPLEMENTATION OF INDIAN ACCOUNTING STANDARDS (IND AS):

1) For Companies other than Banks, NBFCs and Insurance Companies:

Phase I:

A. 1st April 2015 or thereafter (with Comparatives): Voluntary Basis for any company (other than Banks, NBFCs and Insurance companies) and its holding, subsidiary, Joint venture (JV) or Associate Company.

B. 1st April 2016: Mandatory Basis

i) Companies listed/in process of listing on Stock Exchanges in India or Outside India having net worth of INR 500 crore or more;

ii) Unlisted Companies having net worth of INR 500 crore or more;

iii) Parent, Subsidiary, Associate and JV of above.

Phase II: 1st April 2017: Mandatory Basis:

A. All companies which are listed/or in process of listing on Stock Exchanges in India or outside India not covered in Phase I (other than companies listed on SME Exchanges);

B. Unlisted companies having net worth of INR 250 crore or more but less than INR 500 crore;

C. Parent, Subsidiary, Associate and JV of above.

Special Points:

A. Companies listed on SME exchange are not required to apply Ind AS. Such companies shall continue to apply existing ASs unless they choose otherwise.

B. Once Ind AS are applicable, an entity shall be required to follow the Ind AS for all the subsequent financial statements i.e. there is no looking back once the Ind AS are adopted by companies.

C. Companies not covered by the above roadmap shall continue to apply Accounting Standards notified in Companies (Accounting Standards) Rules, 2006

2) **For Scheduled Commercial Banks (Excluding RRBs), Non-Banking Financial Companies (NBFCs) Insurers/Insurance Companies:**

Scheduled Commercial banks (excluding RRBs):

A. Scheduled Commercial Banks (SCBs) excluding Regional Rural Banks (RRBs) were initially required to implement Ind AS from 1 April 2018. However, RBI (Reserve Bank of India) vide a press release dated 5 April 2018, deferred the implementation of Ind AS by one year i.e. to be effective from 1 April 2019 instead of 1 April 2018.

B. Further, the RBI through a notification dated 22 March 2019, deferred the Ind AS implementation till further notice. This was because the amendments recommended by the RBI are still under consideration of the Government of India, therefore, RBI took a decision to defer the applicability of Ind AS till further notice.

C. Urban Cooperative banks (UCBs) and Regional Rural banks (RRBs) are not required to apply Ind AS.

Non-Banking Financial Companies (NBFCs)

Phase I: From 1st April, 2018 (with comparatives)

A. NBFCs (whether listed or unlisted) having net worth INR 500 crores or more

B. Holding, Subsidiary, JV and Associate companies of above NBFC other than those already covered under corporate roadmap shall also apply from said date

Phase II: From 1st April, 2019 (with comparatives)

A. NBFCs whose equity and/or debt securities are listed or are in the process of listing on any stock exchange in India or outside India and having net worth less than INR 500 crores

B. NBFCs that are unlisted having net worth INR 250 crores or more but less than INR 500 crores

C. Holding, Subsidiary, JV and Associate companies of above companies other than those already covered under corporate roadmap shall also apply Ind AS from the said date.

Special points

1) Applicable to both Consolidated and Individual Financial Statements

2) NBFC having net worth below INR 250 crores and not covered under the above provisions shall continue to apply ASs specified in Annexure to Companies (Accounting Standards) Rules, 2006.

3) Adoption of Ind AS is allowed only when required as per the roadmap. Voluntary adoption of Ind AS is not allowed.

Insurers/Insurance companies:

IRDAI, vide circular dated 21 January 2020, has deferred implementation of Ind AS in the insurance sector till further notice.

Meaning of Conceptual Framework

- The Conceptual Framework is a basic document that sets objectives and the concepts for general purpose financial reporting.
- assist the Institute in formulation of Ind ASs that are based on consistent concepts;
- assist preparers to develop consistent accounting policies when no Ind AS applies to a particular transaction.
- In India, the current version of conceptual framework issued by The Institute of Chartered Accountants of India for Ind AS based financial reporting is known as 'Conceptual Framework for Financial Reporting under Ind AS'.

Components of Conceptual Framework for Financial Reporting under Ind AS

1. Objective of general-purpose financial reporting (GPFR).
2. Qualitative characteristics of useful financial information.
3. Financial statements and the reporting entity.
4. The elements of financial statements (FS).
5. Recognition and derecognition.
6. Measurement.
7. Presentation and Disclosures.
8. Concepts of capital and capital maintenance.

1. Objectives of General-Purpose Financial Reporting

The objective of general-purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity.

2. Qualitative Characteristics of Useful Financial Information

In order to make financial information, published in the financial statements, useful for the users, the information must possess certain qualitative characteristics.

A. Fundamental Qualitative Characteristics

Fundamental qualitative characteristics include –

1. **Relevance** – financial information will be relevant if it is capable of making a difference in decisions. For this it must have predictive value, confirmatory value or both. Financial information has predictive value if it can be used as an input to processes employed by users to predict future outcomes. It has confirmatory value if it provides feedback about previous evaluations. While assessing relevance, materiality shall be considered.
2. **Faithful Representation** - To be a perfectly faithful representation, a depiction would have three characteristics. It would be complete, neutral and free from error.

B. Enhancing Qualitative Characteristics

Enhancing qualitative characteristics include the following:

1. **Comparability** – it enables users to identify and understand similarities in, and differences among, items.
2. **Verifiability** – it helps assure users that information faithfully represents the economic phenomena it purports to represent.
3. **Timeliness** - it means having information available to decision-makers in time to be capable of influencing their decisions.
4. **Understandability** - classifying, characterising and presenting information clearly and concisely makes it understandable.

3. <u>Financial Statements and the Reporting Entity</u>

- The objective of financial statements is to provide financial information about the reporting entity's assets, liabilities, equity, income and expenses that is useful to users of financial statements in assessing the prospects for future net cash inflows to the reporting entity and in assessing management's stewardship of the entity's economic resources.
- Financial information is provided in Balance Sheet, Statement of Profit and Loss and in other statements and notes. Financial statements are prepared for a specified period of time, known as reporting period.
- A reporting entity is an entity that is required or chooses to prepare financial statements. A reporting entity can be a single entity or a portion of an entity or can comprise more than one entity.
- Reporting entities prepare consolidated financial statements and unconsolidated financial statements, as required.

4. **<u>Elements of Financial Statements</u>**

The elements of financial statements defined in the Conceptual Framework are:

a. assets, liabilities and equity, which relate to a reporting entity's financial position; and

b. income and expenses, which relate to a reporting entity's financial performance.

5. **<u>Recognition and Derecognition</u>**

- Recognition is the process of capturing for inclusion in the balance sheet or the statement of profit and loss an item that meets the definition of one of the elements of financial statements - an asset, a liability, equity, income or expenses. The amount at which an asset, a liability or equity is recognized in the balance sheet is referred as its 'carrying amount'.
- Derecognition is the removal of all or part of a recognized asset or liability from an entity's balance sheet. Derecognition normally occurs when that item no longer meets the definition of an asset or of a liability. Such assets and liabilities are called transferred components.

  The accounting involves –

  a. derecognising any assets or liabilities that have expired or have been consumed, collected, fulfilled or transferred, and recognising any resulting income and expenses. Such assets and liabilities are called transferred components.

  b. continuing to recognise the assets or liabilities retained, referred to as the 'retained component', if any.

6. **<u>Measurement</u>**

Elements recognized in financial statements are quantified in monetary terms. This requires the selection of a measurement basis.

Conceptual Framework provides the following measurement bases:

A. Historical Cost

- Historical cost measures provide monetary information about assets, liabilities and related income and expenses, from the price of the transaction or other event that gave rise to them.The historical cost of an asset when it is acquired or created is the value of the costs incurred in acquiring or creating the asset, comprising the consideration paid to acquire or create the asset plus transaction costs.
- The historical cost of an asset is updated over time to depict consumption of part or all of economic resources, payments received that extinguish part or all of the asset, the effect of events that cause part or all of the historical cost of the asset to be no longer recoverable (impairment) and accrual of interest to reflect any financing component of the asset.

- The historical cost of a liability is updated over time to depict fulfilment of part or all of the liability, the effect of events that increase the value of the obligation to transfer the economic resources needed to fulfil the liability to such an extent that the liability becomes onerous and accrual of interest to reflect any financing component of the liability.

B. Current Value

Current value measures provide monetary information about assets, liabilities and related income and expenses, using information updated to reflect conditions at the measurement date. Current value measurement bases include:

a. Fair value – Fair Value is the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date.

b. Value in use and fulfilment value - Value in use is the present value of the cash flows, or other economic benefits, that an entity expects to derive from the use of an asset and from its ultimate disposal. Fulfilment value is the present value of the cash, or other economic resources, that an entity expects to be obliged to transfer as it fulfils a liability.

c. Current cost - The current cost of an asset is the cost of an equivalent asset at the measurement date, comprising the consideration that would be paid at the measurement date plus the transaction costs that would be incurred at that date.

7. <u>Presentation and Disclosure</u>

A reporting entity communicates information about its assets, liabilities, equity, income and expenses by presenting and disclosing information in its financial statements.

When developing presentation and disclosure requirements in Ind ASs a balance is needed between:

a. giving entities the flexibility to provide relevant information that faithfully represents the entity's assets, liabilities, equity, income and expenses; and

b. requiring information that is comparable, both from period to period for a reporting entity and in a single reporting period across entities.

8. <u>Concepts of Capital and Capital Maintenance</u>

Conceptual Framework provides two concepts of capital – Financial Capital and Physical Capital. Under a financial concept of capital, such as invested money, capital is synonymous with the net assets or equity of the entity. Under a physical concept of capital, such as operating capability, capital is regarded as the productive capacity of the entity. For example, units of output per day.

The concepts of capital, as above, give rise to the following concepts of capital maintenance:

a. **Financial capital maintenance:** Under this concept, a profit is earned only if the financial amount of the net assets at the end of the period exceeds the financial amount of net assets at the beginning of the period, after excluding any distributions to, and contributions from, owners during the period.

b. **Physical capital maintenance:** Under this concept, a profit is earned only if the physical productive capacity (or operating capability) of the entity (or the resources or funds needed to achieve that capacity) at the end of the period exceeds the physical productive capacity at the beginning of the period, after excluding any distributions to, and contributions from, owners during the period.

Conclusion

a. The Conceptual Framework contributes to the mission of The Institute of Chartered Accountants of India to formulate Ind ASs in order to bring transparency, accountability and efficiency to financial markets.

b. contribute to transparency by enhancing the international comparability and quality of financial information, enabling investors and other market participants to make informed economic decisions.

c. contribute to economic efficiency by helping investors to identify opportunities and risks across the world, thus improving capital allocation. For businesses, the use of a single, trusted accounting language derived from Ind ASs based on the Conceptual Framework lowers the cost of capital and reduces international reporting costs.

The formats for the Statement of Profit and Loss and Balance Sheet as per Division II of Schedule III

Format of the Statement of Profit and Loss

Name of the Company.........................

Statement of Profit and Loss for the period ended............... **(Rs.in.)**

	Particulars	**Note No.**	**Figures as at the end of current reporting period**	**Figures for the previous reporting period**
I	Revenue From operations			
II	Other Income			
III	Total Income (I + II)			
IV	Expenses:			

	Cost of materials consumed			
	Purchases of Stock-in-Trade			
	Changes in inventories of finished goods, Stock-in – Trade and work-in-progress			
	Employee benefits expense			
	Finance costs			
	Depreciation and amortization expenses			
	Other expenses			
	Total expenses (IV)			
V	Profit/(loss) before exceptional items and tax (I-IV)			
VI	Exceptional Items			
VII	Profit/ (loss) after exceptions items and tax(V-VI)			
VIII	Tax expense: (1)Current tax (2)Deferred tax			
IX	Profit (Loss) for the period from continuing operations (VII-VIII)			
X	Profit/(loss) from discontinued operations			
XI	Tax expenses of discontinued operations			
XII	Profit/(loss) from Discontinued operations (after tax) (X-XI)			
XIII	Profit/(loss) for the period (IX+XII)			
XIV	Other Comprehensive Income **A.** **(i)** Items that will not be reclassified to profit or loss **(ii)** Income tax relating to items that will not be reclassified to profit or loss **B.** **(i)** Items that will be reclassified to profit or loss **(ii)** Income tax relating to items that will be reclassified to profit or loss			
XV	Total Comprehensive Income for the period (XIII+XIV)			

	comprising Profit (Loss) and Other comprehensive Income for the period			
XVI	Earnings per equity share (for continuing operation): **(1)** Basic **(2)** Diluted			
XVII	Earnings per equity share (for discontinued operation): **(1)** Basic **(2)** Diluted			
XVIII	Earning per equity share (for discontinued & continuing operation) **(1)** Basic **(2)** Diluted			

<u>Format of the Balance Sheet</u>

Name of the Company....................

Balance Sheet as at .... **(Rs.in.)**

Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
ASSETS			
Non-current assets			
(a) Property, Plant and Equipment			
(b) Capital work-in-progress			
(c) Investment Property			
(d) Goodwill			
(e) Other Intangible assets			
(f) Intangible assets under development			
(g) Biological Assets other than bearer plants			
(h) Financial Assets			

(i) Investments			
(ii) Trade receivables			
(iii) Loans			
(i) Deferred tax assets (net)			
(j) Other non-current assets			
Current assets			
(a) Inventories			
(b) Financial Assets			
(i) Investments			
(ii) Trade receivables			
(iii) Cash and cash equivalents			
(iv) Bank balances other than(iii) above			
(v) Loans			
(vi) Others (to be specified)			
(c) Current Tax Assets (Net)			
(d) Other current assets			
Total Assets			
EQUITY AND LIABILITIES			
EQUITY			
(a) Equity Share capital			
(b) Other Equity			
LIABILITIES			
Non-current liabilities			
(a) Financial Liabilities			
(i) Borrowings			
(ii) Trade Payables:			
(A) total outstanding dues of micro enterprises and small enterprises; and			
(B) total outstanding dues of creditors other than micro enterprises and small enterprises.			
(iii) Other financial liabilities (other than those specified in item (b), to be specified)			

(b) Provisions			
(c) Deferred tax liabilities (Net)			
(d) Other non-current liabilities			
Current liabilities			
(a) Financial Liabilities			
(i) Borrowings			
(ii) Trade Payables:			
(A) total outstanding dues of micro enterprises and small enterprises; and			
(B) total outstanding dues of creditors other than micro enterprises and small enterprises.			
(iii) Other financial liabilities (other than those specified in item (c)			
(b) Other current liabilities			
(c) Provisions			
(d) Current Tax Liabilities (Net)			
Total Equity and Liabilities			

Format of the Statement showing Changes in Equity

STATEMENT OF CHANGES IN EQUITY

Name of the Company..............

A. Equity Share Capital

Balance at the beginning of the current reporting period	Changes in Equity Share Capital due to prior period errors	Restated balance at the beginning of the current reporting period	Changes in equity share capital during the current year	Balance at the end of the current reporting period

B. Other Equity

	Share application on money pending allotment	Equity componentof compound financial instrument	Reserve and Surplus				Debt Instrument through other Compre-hensive Income	Equity Instrument through Other Comprehen-sive Income	Effective portion of Cash Flow Hedges	Revaluation Surplus	Exchange differenceon translating the financial statement	Other items of Other Compr-ehensive Income	Money received against share capital	Total
			Capital Reserve	Securities Premium	Other Reserve (Specify nature)	Retained Earning								
Balance at the beginning of the reporting period														
Changes in accounting policy or priorperiod errors														
Restated balance at the beginning of the reporting period														
Total comprehensive Income for the year														
Dividends														
Transfer to retained earnings														
Balance at the end of the reporting period														

14. IND AS 2 -INVENTORIES

Objective

1. The objective of this Standard is to prescribe the accounting treatment for inventories.
2. This Standard deals with the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value.
3. It also provides guidance on the cost formulas that are used to assign costs to inventories.

Definition of Inventories

Inventories are assets:

a. held for sale in the ordinary course of business; (Finished Goods)

b. in the process of production for such sale; or (Work in progress)

c. in the form of materials or supplies to be consumed in the production process or in the rendering of services. (Raw material)

Scope

This Standard is applicable to all inventories, except:

a. financial instruments (to be accounted under Ind AS 32, Financial Instruments: Presentation and Ind AS 109, Financial Instruments)

b. biological assets (i.e., living animals or plants) related to agricultural activity and agricultural produce at the point of harvest (to be accounted under Ind AS 41, Agriculture)

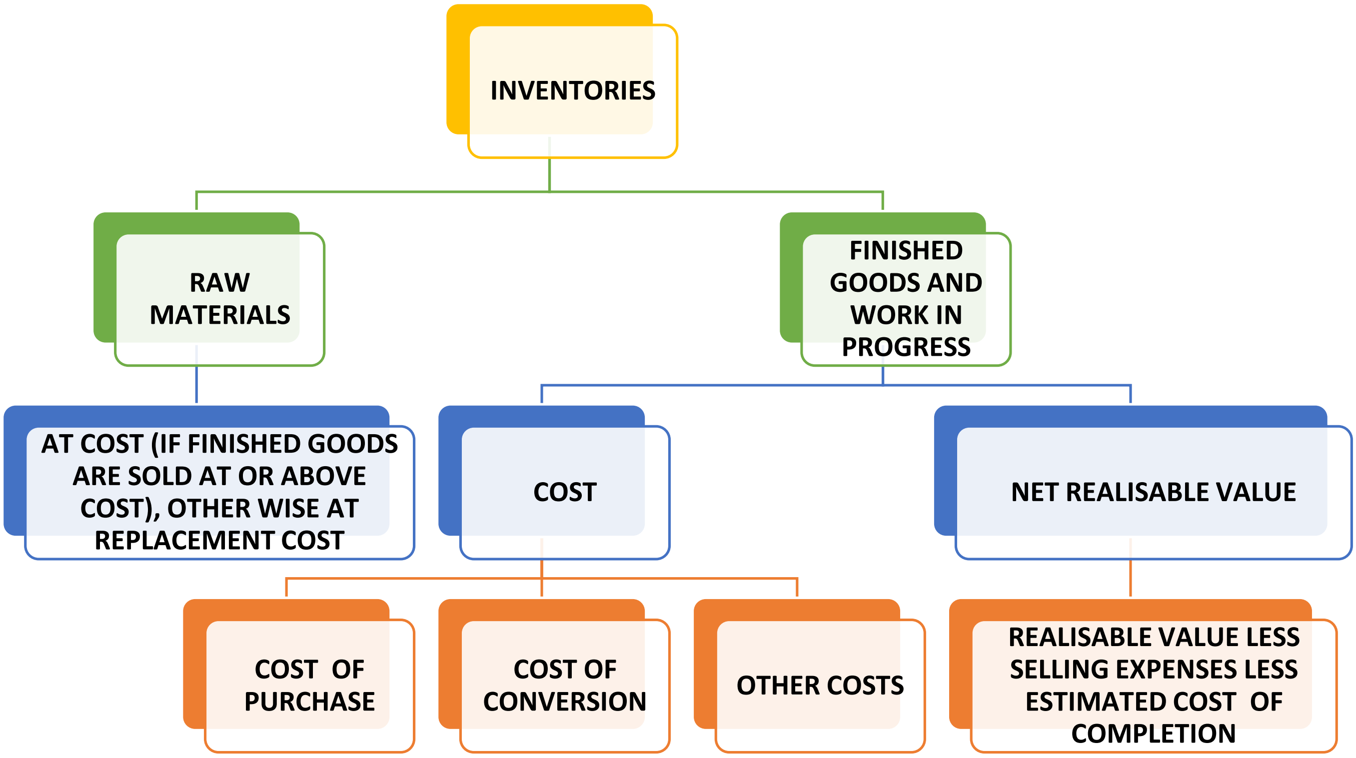
This Standard does not apply to the measurement of inventories held by:

a. producers of agricultural and forest products, agricultural produce after harvest, and minerals and mineral products, to the extent that they are measured at net realisable value in accordance with well-established practices in those industries.

b. Commodity broker-traders who measure their inventories at fair value less costs to sell.

MEASUREMENT OF INVENTORIES:

1. Inventories should be valued at the lower of cost and net realisable value.
2. Materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost. However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realisable value, the materials are written down to net realisable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realisable value.



COST OF INVENTORIES:

The cost of inventories should comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

COST OF PURCHASE:

The costs of purchase consist of the purchase price including duties and taxes (other than those subsequently recoverable by the enterprise from the taxing authorities), freight inwards and other expenditure directly attributable to the acquisition. Trade discounts, rebates, duty drawbacks and other similar items are deducted in determining the costs of purchase.

COST OF CONVERSION:

1. The costs of conversion include costs directly related to production, i.e Direct labour, Direct expenses and overheads (both variable and fixed) that are incurred in converting raw material to finished goods.
2. Fixed production overheads are those indirect costs of production that remain relatively constant regardless of the volume of production, such as depreciation and maintenance of factory buildings and the cost of factory management and administration. Variable production overheads are those indirect costs of production that vary directly, or nearly directly, with the volume of production, such as indirect materials and indirect labour.
3. Variable production overheads are assigned to each unit of production on the basis of the actual use of the production facilities. The fixed production overheads should be absorbed systematically

to units of production on the basis of normal capacity, provided actual production is equal to or less than Normal capacity. Otherwise, Actual production of units is used for absorption.

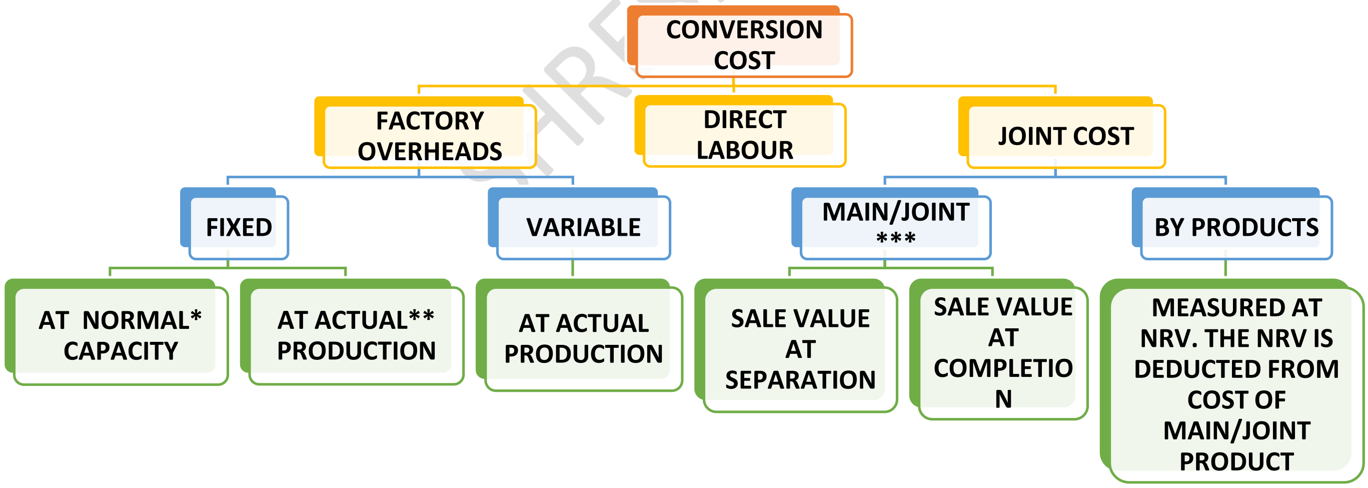
4. Normal capacity is the production expected to be achieved on an average over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance.

5. **JOINT OR BY PRODUCTS:**

   a) when joint products are produced or when there is a main product and a by-product, the costs of conversion of each product are not separately identifiable, they are allocated between the products on a rational and consistent basis.

   b) The allocation may be based, on the relative sales value of each product either at the stage in the production process when the products become separately identifiable, or at the completion of production.

   c) Most by-products as well as scrap or waste materials, by their nature, are immaterial. When this is the case, they are often measured at net realisable value and this value is deducted from the cost of the main product.



*When actual production is almost equal or lower than normal capacity.

** When actual production is higher than normal capacity.

OTHER COSTS:

Other costs are included in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.

EX: the costs of designing products for specific customers in the cost of inventories, Amortisation of intangibles for ascertaining inventory costs. I.e patents right of production or copyright for a publisher should be taken as part of inventory costs.

Exclusions from the Cost of Inventories:

1. Interest and other borrowing costs are usually considered as not relating to bringing the inventories to their present location and condition. Interests and other borrowing costs however are taken as part of inventory costs, where the inventory necessarily takes substantial period of time for getting ready for intended sale(As per IND AS23). Example of such inventory is wine.
2. Abnormal amounts of wasted materials, labour, or other production costs;
3. Storage costs, unless those cost are necessary in the production process prior to a further production stage;
4. Administrative overheads that do not contribute to bringing the inventories to their present location and condition; and
5. Selling and distribution costs.

Cost of inventories of a service provider

To the extent that service providers have inventories, they measure them at the costs of their production. These costs consist primarily of the labour and other costs of personnel directly engaged in providing the service, including supervisory personnel, and attributable overheads. Labour and other costs relating to sale and administrative personnel are not included but are recognized as expenses in the period in which they are incurred. The cost of inventories of a service provider does not include profit margins or non-attributable overheads that are often factored into prices charged by service providers.

Cost of Agricultural Produce Harvested from Biological Assets

In accordance with Ind AS 41, Agriculture, inventories comprising agricultural produce that an entity has harvested from its biological assets are measured on initial recognition at their fair value less costs to sell at the point of harvest. This is the cost of the inventories at that date for application of this Standard.

- **Fair value** is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Cost Formulas:

1. The cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects should be assigned by specific identification of their individual costs. This is an appropriate treatment for items that are segregated for a specific project, regardless of whether they have been purchased or produced.
2. In all other cases, the cost of inventory should be determined by the First-In First-Out (FIFO), or Weighted Average cost formula. The formula used should reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and condition.

Techniques for the Measurement of Cost:

1. Instead of actual, the standard costs may be taken as cost of inventory provided standards fairly approximate the actual. Such standards (for finished or partly finished units) should be set in the light of normal levels of material consumption, labour efficiency and capacity utilisation. The standards so set should be regularly reviewed and if necessary, be revised to reflect current conditions.
2. In retail business, where a large number of rapidly changing items are traded, the actual costs of items may be difficult to determine. The units dealt by a retailer however, are usually sold for similar gross margins and a retail method to determine cost in such retail trades makes use of the fact. By this method, cost of inventory is determined by reducing sale value of unsold stock by appropriate average percentage of gross margin.

Net realizable Value

1. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.
2. The comparison between cost and net realisable value should be made on itemby-item basis.In some circumstances, however, it may be appropriate to group similar or related items. This may be the case with items of inventory relating to the same product line that have similar purposes or end uses and are produced and marketed in the same geographical area.

Recognition as an Expense

1. When inventories are sold, the carrying amount of those inventories shall be recognised as an expense in the period in which the related revenue is recognised.
2. The amount of any write-down of inventories to net realisable value and all losses of inventories shall be recognised as an expense in the period the write-down or loss occurs. The amount of any

reversal of any write-down of inventories, arising from an increase in net realisable value, shall be recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

3. Some inventories may be allocated to other asset accounts, for example, inventory used as a component of self-constructed property, plant or equipment. Inventories allocated to another asset in this way are recognised as an expense during the useful life of that asset.

<u>Disclosures</u>

The financial statements shall disclose:

(a) the accounting policies adopted in measuring inventories, including the cost formula used;

(b) the total carrying amount of inventories and the carrying amount in classifications appropriate to the entity;

(c) the carrying amount of inventories carried at fair value less costs to sell;

(d) the amount of inventories recognised as an expense during the period;

(e) the amount of any write-down of inventories recognised as an expense in the period;

(f) the amount of any reversal of any write-down that is recognised as a reduction in the amount of inventories recognised as expense in the period;

Ind AS 2 vs. AS 2 – A Comparative View

Following are the major differences between Ind AS 2, Inventories and AS 2, Valuation of Inventories

S. No.	Ind AS 2	AS 2
1.	Ind AS 2 deals with subsequent recognition of cost/ carrying amount of inventories as an expense	AS 2 does not provide the same.
2.	Ind AS 2 provides separate explanation for inventories of service providers	AS 2 does not contain such an explanation.
3.	Ind AS 2 does not contain specific explanation for spares which is covered under Ind AS 16.	AS 2 says that inventories do not include spare parts, servicing equipment and standby equipment which meet the definition of property, plant and equipment as per AS 10.

4.	Ind AS 2 provides detailed guidance in case of subsequent assessment of net realisable value. It also deals with the reversal of the write-down of inventories to net realisable value to the extent of the amount of original write-down, and the recognition and disclosure thereof in the financial statements.	AS 2 does not deal with reversal.
5.	Ind AS 2 excludes from its scope only the measurement of inventories held by producers of agricultural and forest products, agricultural produce after harvest, and minerals and mineral products. However, the Standard provides guidance on measurement of such inventories.	AS 2 excludes from its scope such types of inventories.
6.	Ind AS 2 requires the use of consistent cost formulas for all inventories having a similar nature and use to the entity.	AS 2 specifically provides that the formula used in determining the cost of an item of inventory should reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and condition
7.	Ind AS 2 does not apply to measurement of inventories held by commodity broker-traders.	This aspect is not covered in the AS 2
8.	Ind AS 2 defines fair value and distinguishes between 'net realizable value' and 'fair value'	AS 2 does not contain the such definition and explanation.

PROBLEMS FOR CLASS ROOM DISCUSSION

Problem No 1:

How do you deal with the following?

On 31.3.2021, the closing stock of Gourav Ltd. includes 10,000 units costing @ Rs. 10 i.e., Rs.1,00,000. But the current market price as on that date was @ Rs. 9 i.e., Rs. 90,000.

Problem No 2:

From the following information presented by P Ltd. ascertain the value of stock to be included in Balance Sheet: Cost Price of certain stock amounted to Rs.60,000; being obsolete, it can be used for production purposes after incurring Rs.10,000 for modification. The same could be used as a raw material for an existing product, the purchase price for the same amounts to Rs.40,000.

Problem No 3:

How will you deal with the following situation?

"A company deals in purchase and sale of timber and has included notional interest charges calculated (on the paid-up share capital and free reserves) in the value of stock of timber as at the Balance Sheet date as part of cost of holding the timber".

Problem No 4:

The company deals in three products A, B and C which are neither similar nor interchangeable. At the time of closing of its account for the year 2020-21, the historical cost and net realisable value of the items of closing stock are determined as:

Items	Historical Cost (Rs. in lakhs)	Net Realizable Value (Rs. in lakhs)
A	40	28
B	32	32
C	16	24

What will be the value of closing inventories?

Problem No 5:

Z Co. Ltd. purchased goods at the cost of Rs. 40 lakhs in October 2020. Till March 2021, 75% of the stocks were sold. The company wants to disclose closing stock at Rs.10 lakhs. The expected sales value is Rs.11 lakhs and a commission at 10% on sale is payable to the agent. What is the correct closing stock to be disclosed as at 31.3.2021?

Problem No 6:

How would you deal with the following in the annual accounts of a company for the year ended 31.3.2021?

"The company has to pay delayed cotton clearing charges over and above the negotiated price for asking delayed delivery of cotton from the supplier's godown. Up to 2019-20, the company has regularly included such charges in the valuation of closing stock. This being in the nature of interest the company has decided to exclude it from closing stock valuation for the year 2020-21. This would result into decrease in profit by Rs.7.60 lakhs."

Problem No 7:

Sonar Bhandar deals in old colour TVs. It has 4 TVs the particulars of which are given below:

You are asked to compute the value of inventory to be included, in Balance Sheet for the year ended 31st March 2021.

TVs	Onida (Rs.)	Philips (Rs.)	EC (Rs.)	Sony (Rs.)	Total (Rs.)
Cost Price	10,000	20,000	35,000	50,000	1,15,000
Expenses incurred to bring into salable conditions	3,000	2,000	5,000	-	10,000
Net Realizable Value	18,000	30,000	36,000	55,000	1,39,000

Problem No 8:

The following particulars are presented by M Ltd. (deals in clothing) as on 31.3.2021: Compute the value of stock as per Ind AS 2.

Stock held by M Ltd.:

Cost Price Rs.10,550

Net Realisable Value Rs.11,500

The details of such stocks were:.

Particulars	Cost Price (Rs.)	Net Realizable Value (Rs.)
Cotton	5,600	4,960
Woolen	3,450	4,540
Synthetic	1,500	2,000
Total	10,550	11,500

Problem No 9:

The total stock of A Ltd. as on 31.3.2021 was Rs.5,00,000 of which stock amounting to Rs.31,000 were not ascertained as per Ind AS 2.

Compute the value of the said stocks as per Ind AS 2 for inclusion in financial statements as on that date.

Type of Product	Cost of Materials (Rs.)	Production Expenses incurred (Rs.)	Selling and Distribution expense to be incurred (Rs.)	Estimated Selling Price (Rs.)
P	10,000	2,000	1,000	15,000
S	5,000	---	500	4,500
T	12,000	3,000	2,000	18,000
	27,000	5,000	3,500	37,500

Problem No 10:

X Ltd. presented the following particulars as on 31.3.2021 on the total cost of product:

Particulars	Cost per unit (Rs.)
Cost of materials (Rs.12 each)	50
Manufacturing inputs	30
Total Cost	80
Profit	20
Selling Price	100

On 31.3.2021, selling price has gone down suddenly from Rs. 100 to Rs.70. Price of raw material has also gone down to Rs.8 each. X Ltd. had in its stock 6,000, units of materials which was bought as per the above rate on the same date. Compute the value of stock as on 31.03.2021.

Problem No 11:

State with reference to accounting standards how will you value the inventories in the following cases:

(i) Raw materials were purchased at Rs.100 per kg. Prices of raw materials are on the decline. The finished goods in which the raw materials is incorporated is expected to be sold at below cost. 10,000 Kgs. of raw materials is on stock at the year end. Replacement cost is Rs.80 per kg.

(ii) In a production process, normal waste is 5% of input. 5,000 MT of input were put in process resulting in a wastage of 300 MT. Cost per MT of input is Rs.1,000. The entire quantity of waste is on stock at the year-end.

(iii) Per kg of finished goods consisted of:

	Rs.
Material Cost	100
Direct Labour	20
Direct Variable Production Overhead	10

Fixed production charges for the year on normal capacity of one lakh kg is Rs.10 lakhs. 2,000 kg of finished goods are on stock at the year end.

15. EVENTS AFTER THE REPORTING PERIOD (Ind AS 10)

Introduction:

Though financial statements are to be prepared for a financial year, generally, it is not possible for an entity to prepare and finalize the financial statements on the reporting date itself. A firm takes some time to prepare and finalize the financial statements and further more time to get it approved by the board. Only after the financial statements are approved, they may be used by the users. This raises a question as to how to deal with the events occurring after the balance sheet date but before the date financial statements are approved for issue.

These events after the reporting period are accounted as per the guidelines given in Ind AS 10

Events after the reporting period:

Events occurring after the reporting period are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company, and, by the corresponding approving authority in the case of any other entity.

Two types of events can be identified:

1. **Adjusting events**- those which provide further evidence of conditions that existed at the balance sheet date. Adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date.

EXAMPLES:

(a) the settlement after the reporting period of a court case that confirms that the entity had a present obligation at the end of the reporting period. The entity adjusts any previously recognised provision related to this court case in accordance with Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets or recognises a new provision. The entity does not merely disclose a contingent liability because the settlement provides additional evidence that would be considered in accordance with paragraph 16 of Ind AS 37.

(b) the receipt of information after the reporting period indicating that an asset was impaired at the end of the reporting period, or that the amount of a previously recognised impairment loss for that asset needs to be adjusted. For example:

- **(i)** the bankruptcy of a customer that occurs after the reporting period usually confirms that a loss existed at the end of the reporting period on a trade receivable and that the entity needs to adjust the carrying amount of the trade receivable; and
- **(ii)** the sale of inventories after the reporting period may give evidence about their net realisable value at the end of the reporting period.

(c) the determination after the reporting period of the cost of assets purchased, or the proceeds from assets sold, before the end of the reporting period.

(d) the determination after the reporting period of the amount of profit-sharing or bonus payments, if the entity had a present legal or constructive obligation at the end of the reporting period to make such payments as a result of events before that date.

(e) the discovery of fraud or errors that show that the financial statements are incorrect.

2. **<u>Non-adjusting events</u>**- those which are indicative of conditions that arose subsequent to the balance sheet date. Adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. If these are Material, they may require a disclosure in the report of the approving authority to enable users of financial statements to make proper evaluations and decisions.

<u>EXAMPLES</u>:

(a) Decline in market value of investments between the end of the reporting period and the date when the financial statements are approved for issue.

(b) A major business combination or disposal of a major subsidiary after the balance sheet date.

(c) Announcing or commencing the implementation of, a major restructuring.

(d) Changes in tax rates or tax laws enacted or announced after the balance sheet date that have a significant effect on current and deferred tax assets and liabilities (Ind AS 12, Income taxes)

(e) Entering into significant commitments or contingent liabilities, for example by issuing significant guarantees;

(f) Commencing major litigation arising solely out of events that occurred after the reporting period.

Events occuring after the Balance Sheet date

Evidence of such condition been existed at the Balance Sheet date	**No evidence of such condition been existed at the Balance Sheet date**
Adjusting event	**Non-adjusting event**
Adjustment to assets and liabilities is required	**Adjustment to assets and liabilities is not required**
Disclosure in the financial statements is required	**Disclosure in the report of the approving authority is required**

<u>Going Concern:</u>

An entity shall not prepare its financial statements on a going concern basis if management determines after the reporting period either that it intends to liquidate the entity or to cease trading, or that it has no realistic alternative but to do so.

Treatment of Dividends:

If an entity declares dividends to holders of equity instruments (as defined in Ind AS 32 Financial Instruments: Presentation) after the reporting period, the entity shall not recognise those dividends as a liability at the end of the reporting period.

Distribution of Non-cash Assets to Owners (Appendix to Ind AS10):

Ind AS 10 provides the following guidelines (in Appendix of Ind AS 10) in respect of distribution of non-cash assets to the owners. However, the guidelines are applicable to the following types of non-reciprocal distributions of assets by an entity to its owners acting in their capacity as owners:

a. distributions of non-cash assets (e.g., items of property, plant and equipment, businesses as defined in Ind AS 103, ownership interests in another entity or disposal groups as defined in Ind AS 105; and

b. distributions that give owners a choice of receiving either non-cash assets or a cash alternative. The guidelines apply only to distributions in which all owners of the same class of equity instruments are treated equally. Moreover, the guidelines do not apply to a distribution of a non-cash asset that is ultimately controlled by the same party or parties before and after the distribution.

The important issues in the context of distribution of non-cash assets to owners:

a. When to recognize a dividend payable?

The liability to pay a dividend shall be recognized when the dividend is appropriately authorized and is no longer at the discretion of the entity, which is the date:

(i) when declaration of the dividend, e.g., by management or the board of directors, is approved by the relevant authority, e.g., the shareholders, if the jurisdiction requires such approval, or

(ii) when the dividend is declared, e.g., by management or the board of directors, if the jurisdiction does not require further approval.

b. Measurement of a dividend payable

(i) An entity shall measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed.

(ii) If an entity gives its owners a choice of receiving either a non-cash asset or a cash alternative, the entity shall estimate the dividend payable by considering both the fair value of each alternative and the associated probability of owners selecting each alternative.

(iii) At the end of each reporting period and at the date of settlement, the entity shall review and adjust the carrying amount of the dividend payable, with any changes in the carrying amount of the dividend payable recognised in equity as adjustments to the amount of the distribution.

c. Accounting for any difference between the carrying amount of the assets distributed and the carrying amount of the dividend payable when an entity settles the dividend payable

When an entity settles the dividend payable, it shall recognise the difference, if any, between the carrying amount of the assets distributed and the carrying amount of the dividend payable in profit or loss.

d. Presentation and Disclosure

- An entity shall present the difference mentioned above as a separate line item in profit or loss.
- An entity shall disclose the following information, if applicable:
  (i) the carrying amount of the dividend payable at the beginning and end of the period; and
  (ii) the increase or decrease in the carrying amount recognised in the period as result of a change in the fair value of the assets to be distributed.

- If, after the end of a reporting period but before the financial statements are approved for issue, an entity declares a dividend to distribute a non-cash asset, it shall disclose:
  (i) the nature of the asset to be distributed;
  (ii) the carrying amount of the asset to be distributed as of the end of the reporting period; and
  (iii) the estimated fair value of the asset to be distributed as of the end of the reporting period, if it is different from its carrying amount, and the information about the method used to determine that fair value required by Ind AS 107.

<u>Disclosures under Ind AS 10</u>

Ind AS 10 requires the following disclosures:

a) An entity shall disclose the date when the financial statements were approved for issue and who gave that approval. If the entity's owners or others have the power to amend the financial statements after issue, the entity shall disclose that fact.

b) Updating disclosure about conditions at the end of the reporting period:

(i) If an entity receives information after the reporting period about conditions that existed at the end of the reporting period, it shall update disclosures that relate to those conditions, in the light of the new information.

(ii) In some cases, an entity needs to update the disclosures in its financial statements to reflect information received after the reporting period, even when the information does not affect the amounts that it recognises in its financial statements. For example, contingent liability that existed at the end of the reporting period.

c) Non-adjusting events after the reporting period:

If non-adjusting events after the reporting period are material, non-disclosure could influence the economic decisions that users make on the basis of the financial statements. Accordingly, an entity shall disclose the following for each material category of non-adjusting event after the reporting period:

(i) the nature of the event; and

(ii) an estimate of its financial effect, or a statement that such an estimate cannot be made.

<u>Following are the major differences between Ind AS 10, Events after Reporting Period and AS 4, Contingencies and Events Occuring after Balance Sheet Date</u>

S. No	Ind AS 10	AS 4
1.	Ind AS 10 does not cover contingencies but only covers events after the reporting period	AS 4 covers contingencies as well.
2.	The standard requires material non-adjusting events to be disclosed in the financial statements.	AS 4 requires the same to be disclosed in the report of approving authority.
3.	If after the reporting date it is determined that the fundamental accounting assumption of going concern is no longer appropriate, Ind AS 10 requires a fundamental change in the basis of accounting.	AS 4 requires assets and liabilities to be adjusted for events occurring after the balance sheet date that indicate that the fundamental accounting assumption of going concern is not appropriate.
4.	In the context of going concern assumption not being valid anymore, Ind AS 10 refers to Ind AS 1, which requires an entity to make the disclosures that the financial statements are not prepared on a going concern basis together with the basis on which the financial statements are prepared and the reason thereof.	AS 4 does not require any such disclosure. However, AS 1 requires the disclosure of the fact in case going concern assumption is not followed.
5.	Consequent to carve-out made in Ind AS 1, it has been provided in the definition of 'Events after the reporting period' that in case of breach of a material provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the	No such guidance is given in AS 4.

	liability becomes payable on demand on the reporting date, if the lender, before the approval of the financial statements for issue, agrees to waive the breach, it shall be considered as an adjusting event.	
6.	Ind AS 10 includes an Appendix Distribution of Non- cash Assets to Owners which deals, inter alia, with when to recognize dividends payable to its owners.	No such guidance is given in AS 4

PROBLEMS FOR CLASS ROOM DISCUSSION

Problem No 1:

X Ltd. finalized its accounts on 31.03.2021. However, the financial statements were approved by the Board on 20.05.2021. An accident occurred in the premises of X Ltd. on 30.05.2021 and properties worth Rs.50 lakh has been lost. Will it be considered as an event after the reporting period as per the scope of Ind AS 10?

Problem No 2:

A Ltd. closed its accounting year on 31/03/2021 and the accounts for that period were considered and approved by the board of directors on 20th May, 2021. The company was engaged in boring tunnels for metro railway. While doing the boring work on 01/06/2021 it hit an aquifer and as a result 18 building were damaged. It was estimated that there would be extra cost to the tune of Rs.15 crores. You are required to state with reasons, how it would be dealt with in the financial statements for the year ended 31.03.2021.

Problem No 3:

While preparing its final accounts for the year ended 31st March, 2021, a company made a provision for doubtful debts @ 5% of its total debtors. In the last week of February 2021, a debtor for Rs.20 lakh suffered heavy loss and subsequently became insolvent in April, 2021. Can the company provide the full loss out of the insolvency of the debtor in the final accounts for the year ended on 31.03.2021?

Problem No 4:

B Ltd. supplies parts to a car manufacturer in respect of a particular model of car. On the reporting date, B Ltd. has a high level of inventory of parts due to low order levels. After the reporting date but before the date of approval of the financial statements, the car manufacturer announces that the specific model will no longer be produced. There is no alternative market for the inventory. Should B Ltd. write-down of inventory to net realizable value and adjust the inventory reported on the reporting date?

Problem No 5:

Prior to the approval of the financial statements but subsequent to the balance sheet date, C Ltd. in trading difficulties obtained a valuation of its properties for the purpose of providing additional security to its bankers. C Ltd. is also considering selling certain properties to generate additional cash. The amount estimated by the valuer is materially lower than the carrying amount attributed to the properties at the balance sheet date based on the last impairment review carried out three years ago. How should this be reflected in the financial statements?

Problem No 6:

The exchange differences arising on the translation of the bank overdraft since the balance sheet date exceed the profit for the period under review due to an adverse movement on the foreign exchange rate after year end. How should this be reflected in the financial statements?

Problem No 7:

AIR Aviation Co. Ltd. announced a restructuring programme in 2018 which was implemented in full in 2019. The workforce was adequately downsized and a number of non-profitable routes were suspended. However, in view of the still -difficult market environment, the high cost of aviation fuel and continuing declines in yields, the Board of Directors approved a further package of measures on January 31, 2020 under which the regional aircraft fleet will be reduced by at least 15 aircraft. This action is intended to reduce net annual cost by recurring Rs.200 lakh. The actions will be taken over the next 15 months. The company is expecting a break-even in 2021. Should the company prepare its financial statements on a going concern basis?

16. EARNINGS PER SHARE (Ind AS 33)

INTRODUCTION & OBJECTIVE:

1. Earnings per share (EPS) is a financial ratio indicating the amount of profit or loss for the period attributable to each equity share (ordinary share) and Ind AS 33 gives computational methodology for determination and presentation of basic and diluted earnings per share.
2. The objective of this Standard is to prescribe principles for the determination and presentation of earnings per share which will improve comparison of performance among different enterprises for the same period and among different accounting periods for the same enterprise.
3. EPS is useful for computation of Market price per share. M.P.S = E.P.S X P/E ratio.

Scope

a. This Indian Accounting Standard shall apply to companies that have issued ordinary shares to which Indian Accounting Standards (Ind ASs) notified under the Companies Act apply.

b. An entity that discloses earnings per share shall calculate and disclose earnings per share in accordance with this Standard.

c. When an entity presents both consolidated financial statements and separate financial statements prepared in accordance with Ind AS 110, Consolidated Financial Statements, and Ind AS 27, Separate Financial Statements, respectively, the disclosures required by this Standard shall be presented both in the consolidated statements and separate financial statements.

Important Definitions

Anti-dilution is an increase in earnings per share or a reduction in loss per share resulting from the assumption that convertible instruments are converted, that options or warrants are exercised, or that ordinary shares are issued upon the satisfaction of specified conditions.

A contingent share agreement is an agreement to issue shares that is dependent on the satisfaction of specified conditions.

Contingently issuable ordinary shares are ordinary shares issuable for little or no cash or other consideration upon the satisfaction of specified conditions in a contingent share agreement.

Dilution is a reduction in earnings per share or an increase in loss per share resulting from the assumption that convertible instruments are converted, that options or warrants are exercised, or that ordinary shares are issued upon the satisfaction of specified conditions.

Options, warrants and their equivalents are financial instruments that give the holder the right to purchase ordinary shares.

Put options on ordinary shares are contracts that give the holder the right to sell ordinary shares at a specified price for a given period.

Types of EPS

There are two types of EPS that are reported by an entity on the face of the Statement of Profit and Loss. These are:

a) Basic EPS; and

b) Diluted EPS

MEASUREMENT:

BASIC EARNINGS PER SHARE:

$$\frac{\textbf{Net profit (loss) attribute to equity share holders}}{\textbf{Weighted average number of equity shares outstanding during the period}}$$

EARNINGS ATTRIBUTABLE TO EQUITY SHARE HOLDERS:

PARTICULARS	AMOUNT RS.
PROFIT AFTER TAX (PAT) LESS: PREFERNCE DIVIDEND LESS: DIVIDEND DISTRIBUTION TAX ON PREFERENCE DIVIDEND IF APPLICABLE	XXXX (XXXX) (XXXX)
EARNINGS AVILABLE TO EQUITY SHARE HOLDERS	XXXX

IMPORTANT POINTS ON EAESH:

1. All items of income and expense which are recognised in a period, including tax expense and extraordinary items, are included in the determination of the net profit or loss for the period.
2. The amount of preference dividends and any attributable tax thereto for the period is deducted from the net profit for the period in order to calculate the net profit or loss for the period attributable to equity shareholders.
3. The amount of preference dividends for the period that is deducted from the net profit for the period is:
   a. The amount of any preference dividends on non-cumulative preference shares provided for in respect of the period; and

b. The full amount of the required preference dividends for cumulative preference shares for the period, whether or not the dividends have been provided for. The amount of preference dividends for the period does not include the amount of any preference dividends for cumulative preference shares paid or declared during the current period in respect of previous periods.

4. If an enterprise has more than one class of equity shares, net profit or loss for the period is apportioned over the different classes of shares in accordance with their dividend rights.

WEIGHTED AVERAGE NUMBER OF EQUITY SHARES:

WANES = NO.OF EQUITY SHARES OUT STANDING X PERIOD VALUE WEIGHT X PAID-UP VALUE WEIGHT

A) Period value weight = No. of months outstanding during the year /12 months.

B) Paid-up value weight= Paid-up value towards face value/ Face value.

C) Number of Equity shares outstanding during the period is the number of shares outstanding at the beginning of the period, adjusted by the number of equity shares bought back or issued during the period.

Effective date: It means the date from which shares are included in the weighted average number of shares. I.e In generally from the date the consideration is receivable.

1. Equity shares issued in exchange for cash are included when cash is receivable;
2. Equity shares issued as a result of the conversion of a debt instrument to equity shares are included as of the date of conversion;
3. Equity shares issued in lieu of interest or principal on other financial instruments are included as of the date interest ceases to accrue;
4. Equity shares issued in exchange for the settlement of a liability of the enterprise are included as of the date the settlement becomes effective;
5. Equity shares issued as consideration for the acquisition of an asset other than cash are included as of the date on which the acquisition is recognised; and
6. Equity shares issued for the rendering of services to the enterprise are included as the services are rendered.
7. Equity shares issued as part of the consideration in an amalgamation in the nature of purchase are included in the weighted average number of shares as of the date of the acquisition.

8. Equity shares issued as part of the consideration in an amalgamation in the nature of merger are included in the calculation of the weighted average number of shares from the beginning of the reporting period.

Bonus Issue, Share split:

1. In case of a bonus issue or a share split, equity shares are issued to existing shareholders for no additional consideration. Therefore, the number of equity shares outstanding is increased without an increase in resources.
2. The number of Equity shares outstanding before the event is adjusted for the proportionate change in the number of Equity shares outstanding as if the event had occurred at the beginning of the earliest period reported means along with the impact to current year adjustment, it will also impact the calculation of EPS of last year retrospectively.

Bonus element in Right shares:

1. In a rights issue the exercise price is often less than the fair value of the shares. Therefore, a rights issue usually includes a bonus element.
2. The number of Equity shares to be used in calculating basic earnings per share for all periods prior to the rights issue is the number of equity shares outstanding prior to the issue, multiplied by the adjustment factor.

BONUS ELEMENT

$$\frac{\text{Fair value per share immediately prior to the exercise of rights}}{\text{Theoretical ex- rights fair value per share}}$$

3. The theoretical ex-rights fair value per share is calculated by adding the aggregate fair value of the shares immediately prior to the exercise of the rights to the proceeds from the exercise of the rights, and dividing by the number of shares outstanding after the exercise of the rights.

Diluted Earnings Per Share is decrease in Basic EPS due to Dilutive potential Equity shares.

Potential equity share is a financial instrument or other contract that entitles, or may entitle, its holder to equity shares.

Examples:

a. Debt instruments, that are convertible into equity shares.

b. Preference shares, that are convertible into equity shares.

c. Options including employee stock option plans under which employees of an enterprise are entitled to receive equity shares as part of their remuneration and other similar plans;

d. Shares which would be issued upon the satisfaction of certain conditions resulting from contractual arrangements (contingently issuable shares), such as the acquisition of a business or other assets, or shares issuable under a loan contract upon default of payment of principal or interest, if the contract so provides.

Dilutive Potential Equity Shares: Potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would decrease net profit per share from continuing ordinary operations.

Earnings-Diluted Eps:

For the purpose of calculating diluted earnings per share, the amount of net profit or loss for the period attributable to equity shareholders, should be adjusted by the following, after taking into account any attributable change in tax expense for the period:

1. Any dividends on dilutive potential equity shares which have been deducted in arriving at the net profit attributable to equity shareholders;
2. Interest recognised in the period for the dilutive potential equity shares; and
3. Any other changes in expenses or income that would result from the conversion of the dilutive potential equity shares.

WANES-Diluted EPS:

1. For the purpose of calculating diluted earnings per share, the number of equity shares should be the aggregate of the weighted average number of equity shares, and the weighted average number of equity shares which would be issued on the conversion of all the dilutive potential equity shares into equity shares.
2. Dilutive potential equity shares should be deemed to have been converted into equity shares at the beginning of the period or, if issued later, the date of the issue of the potential equity shares.
3. Potential equity shares are weighted for the period they were outstanding. Potential equity shares that have been converted into equity shares during the reporting period are included in the calculation of diluted earnings per share from the beginning of the period to the date of conversion. From the date of conversion, the resulting equity shares are included in computing both basic and diluted earnings per share under WANES.

Measurement of Dilutive EPS:

1. After the potential equity shares are converted into equity shares, the dividends, interest and other expenses or income associated with those potential equity shares will no longer be incurred (or earned). Instead, the new equity shares will be entitled to participate in the net profit attributable to equity shareholders.
2. The net profit for the period attributable to equity shareholders calculated in Basic Earnings Per Share is increased by the amount of dividends, interest and other expenses that will be saved, and reduced by the amount of income that will cease to accrue, on the conversion of the dilutive potential equity shares into equity shares. The amounts of dividends, interest and other expenses or income are adjusted for any attributable taxes.
3. **Diluted EPS in case of share options**:
   For the purpose of calculating diluted earnings per share, an enterprise should assume the exercise of dilutive options and other dilutive potential equity shares of the enterprise. The difference between the number of shares issuable and the number of shares that would have been issued at fair value should be treated as an issue of equity shares for no consideration. Which is nothing but Bonus element in Options. Such Bonus element in options only considered for calculation Of Dilutive EPS.

Anti-Dilutive Potential Equity Shares:

1. Potential equity shares are anti-dilutive when their conversion to equity shares would increase earnings per share from continuing ordinary activities. The effects of anti-dilutive potential equity shares are ignored in calculating diluted earnings per share.
2. In considering whether potential equity shares are dilutive or antidilutive, each issue or series of potential equity shares is considered separately rather than in aggregate.
3. The sequence in which potential equity shares are considered may affect whether or not they are dilutive. Therefore, in order to maximise the dilution of basic earnings per share, each issue or series of potential equity shares is considered in sequence from the most dilutive to the least dilutive.
4. For the purpose of determining the sequence from most dilutive to least dilutive potential equity shares, the earnings per incremental potential equity share is calculated. Where the earnings per incremental share is the least, the potential equity share is considered most dilutive and vice-versa.

- **Purchased options**

  Contracts such as purchased put options and purchased call options (i.e., options held by the entity on its own ordinary shares) are not included in the calculation of diluted earnings per share because including them would be antidilutive.

- **Written put options**

  Contracts that require the entity to repurchase its own shares, such as written put options and forward purchase contracts, are reflected in the calculation of diluted earnings per share if the effect is dilutive. If these contracts are 'in the money' during the period (ie the exercise or settlement price is above the average market price for that period), the potential dilutive effect on earnings per share shall be calculated as follows:

  (a) it shall be assumed that at the beginning of the period sufficient ordinary shares will be issued (at the average market price during the period) to raise proceeds to satisfy the contract;

  (b) it shall be assumed that the proceeds from the issue are used to satisfy the contract (ie to buy back ordinary shares); and

  (c) the incremental ordinary shares (the difference between the number of ordinary shares assumed issued and the number of ordinary shares received from satisfying the contract) shall be included in the calculation of diluted earnings per share.

<u>**Presentation**</u>

An entity shall present in the statement of profit and loss basic and diluted earnings per share for profit or loss

- from continuing operations attributable to the ordinary equity holders of the parent entity and
- for profit or loss attributable to the ordinary equity holders of the parent entity for the period for each class of ordinary shares that has a different right to share in profit for the period.
- An entity shall present basic and diluted earnings per share with equal prominence for all periods presented.
- If basic and diluted earnings per share are equal, dual presentation can be accomplished in one line in the statement of profit and loss.
- An entity that reports a discontinued operation shall disclose the basic and diluted amounts per share for the discontinued operation either in the statement of profit and loss or in the notes.
- An entity shall present basic and diluted earnings per share, even if the amounts are negative (i.e., a loss per share).

Disclosure

An entity shall disclose the following:

(a) the amounts used as the numerators in calculating basic and diluted earnings per share, and a reconciliation of those amounts to profit or loss attributable to the parent entity for the period. The reconciliation shall include the individual effect of each class of instruments that affects earnings per share.

(b) the weighted average number of ordinary shares used as the denominator in calculating basic and diluted earnings per share, and a reconciliation of these denominators to each other. The reconciliation shall include the individual effect of each class of instruments that affects earnings per share.

(c) instruments (including contingently issuable shares) that could potentially dilute basic earnings per share in the future, but were not included in the calculation of diluted earnings per share because they are antidilutive for the period(s) presented.

(d) a description of ordinary share transactions or potential ordinary share transactions, other than those accounted for, that occur after the reporting period and that would have changed significantly the number of ordinary shares or potential ordinary shares outstanding at the end of the period if those transactions had occurred before the end of the reporting period.

If an entity discloses, in addition to basic and diluted earnings per share, amounts per share using a reported component of the statement of profit and loss other than one required by this Standard:

- Such amounts shall be calculated using the weighted average number of ordinary shares determined in accordance with this Standard.
- Basic and diluted amounts per share relating to such a component shall be disclosed with equal prominence and presented in the notes.
- An entity shall indicate the basis on which the numerator(s) is (are) determined, including whether amounts per share are before tax or after tax.

If a component of the statement of profit and loss is used that is not reported as a line item in the statement of profit and loss, a reconciliation shall be provided between the component used and a line item that is reported in the statement of profit and loss.

Ind AS 33 vs. AS 20 – A Comparative View

Following are the major differences between Ind AS 33, Earning Per Share and AS 20, Earning Per Share:

S. No.	Ind AS 33	AS 20
1.	Ordinary shares to be issued upon conversion of a mandatorily convertible instrument are included in the calculation of basic EPS from the date the contract is entered into.	No specific requirement is specified in Ind AS.
2.	Disclosure is required for instruments (including contingently issuable shares) that could potentially dilute basic earnings per share in the future but were not included in the calculation of diluted earnings per share because they are anti-dilutive for the periods presented.	No such additional disclosures are required.
3.	Ordinary shares that are issuable solely after a passage of time are not treated as contingently issuable shares because passage of time is a certainty.	No specific guidelines included.
4.	Outstanding ordinary shares that are contingently returnable are not treated as outstanding and are ignored in the calculation of basic EPS until the shares are no longer subject to recall.	No guidance available on contingently returnable shares.

PROBLEMS FOR CLASS ROOM DISCUSSION

Problem No 1:

The following information has been provided by A Ltd.

Paid up capital: 100000 ordinary shares of Rs. 1.00 = Rs. 1,00,000

20000, 10% Preference shares of Rs. 1.00 = Rs.20,000

Gross Profit for the year ended on 31.03.2021 = Rs.3,50,000

Other operating expenses = Rs.1,00,000

Tax rate 30%

Determine profit or loss attributable to ordinary equity holders.

Problem No 2:

01.04.2020 B Ltd. has 3600 ordinary shares outstanding. On 31.08.2021 it issued 1200 ordinary shares for cash. On 31.01.21 it bought back 600 ordinary shares. Calculate weighted average number of shares as on 31.03.21.

Problem No 3:

Refer to Problem No 2. If profit or loss attributable to ordinary equity holders of B Ltd. for the year ended on 31.03.21 was Rs.21,00,000, calculate Basic EPS.

Problem No 4:

D Ltd. had outstanding ordinary shares of 10,00,000on 01.04.2020. Profit for the year is Rs.20,00,000. D Ltd. had 12% 20,000 convertible debentures outstanding of Rs.100 each to be converted into 10 ordinary shares. Tax rate is 30%. Calculate (i) Basic EPS (ii) Diluted EPS

Problem No 5:

Consider the following information given by F Ltd.

Net Profit for the year ended on 31.03.2021= Rs.86,50,000 Paid-up capital: 25,00,000 ordinary shares of Rs.10 each 100000, 10% Debentures of Rs.100 each were issued on 31.09.2020. Tax rate 30% Conversion rate: 10 ordinary shares for each debenture. Calculate Diluted EPS.

Problem No 6:

E Ltd. had 10,00,000 ordinary shares outstanding on 01.04.2020. Profit for 2020-21 was Rs.24,00,000. Average fair value per share during 2020-21 was Rs. 20. E Ltd. has given share option to its employees of 2,00,000 shares at option price of Rs.15. Calculate basic EPS and diluted EPS.

Problem No 7:

X Ltd. has 320 written put options outstanding on 320 of its ordinary shares, with an exercise price of Rs. 10 per option. The put obligation is therefore Rs.3,200. The average market price of the entity's ordinary shares is Rs.8 for the period. The company expects to issue 400 ordinary shares at Rs. 8 per share to raise the proceeds necessary to satisfy the put option. How will you treat the above?

Problem No 8:

Y Ltd. supplied the following information:

Net Profit for 2019-20 = Rs.10,00,000

Net Profit for 2020-21 = Rs.15,00,000

No. of shares prior to right issue = 5,00,000

Terms of right issue: 1 new share for every 4 shares held; right issue price = Rs.20 Fair value of 1 ordinary share immediately prior to exercise of right = Rs.25 Calculate basic EPS.

Problem No 9:

C Ltd. had 10,00,000 ordinary shares outstanding as on 01.04.2020. On 01.01.2021 it issued 2 ordinary shores bonus for each shore outstanding on 31.12.2020, Profit for the year 2019-20 was Rs.9,00,000. Profit for 2020-21 was Rs.30,00,000. Calculate Basic EPS the year 2020-21 and adjusted EPS for the year 2019-20.

17. PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS (Ind AS 37)

Objective

The objective of this Standard is to ensure that appropriate recognition criteria and measurement bases are applied to provisions, contingent liabilities and contingent assets and that sufficient information is disclosed in the notes to enable users to understand their nature, timing and amount.

Scope

This Standard shall be applied by all entities in accounting for provisions, contingent liabilities and contingent assets, except

(a) those resulting from executory contracts, except where the contract is onerous; and

(b) those covered by another Standard (e.g., Ind AS 12, 17, 19, 103, 104, 115).

- **Executory contracts** are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent.
- **Onerous contracts** are contracts in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. If an enterprise has a contract that is onerous, the present obligation under the contract is recognised and measured as a provision as per this Standard.

  Example: a lease on a property that is no longer necessary but cannot be sublet.

Definition of Provision:

A provision is a liability of uncertain timing or amount.

A liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.

An obligating event is an event that creates a legal or constructive obligation that results in an entity having no realistic alternative to settling that obligation.

A legal obligation is an obligation that derives from:

(a) a contract (through its explicit or implicit terms);

(b) legislation; or

(c) other operation of law.

A constructive obligation is an obligation that derives from an entity's actions where:

(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and

(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

A provision should be recognised when:

1. An enterprise has a **present obligation** as a result of a **past event**;
2. It is **probable that an outflow of resources** embodying economic benefits will be required to settle the obligation; and
3. A **reliable estimate** can be made of the amount of the obligation.

If all the above conditions are met, then only provision should be recognised.

Example:

XYZ is in mining business. It is operating in a country where XYZ is legally bound to clean and restore the environment on expiry of license after 10 years. XYZ can reliably estimate the amount required to restore the environment caused by the mining business. Since it is a present obligation which cannot be avoided resulted from past event, it is probable that resources will flow out of business to settle the same and estimate can be measured reliably. XYZ is required to recognize a provision for the same.

Accounting for Provision

The amount of provision should be shown as an expense in profit and loss statement. Expenses relating to provision should be shown in profit and loss statement net of reimbursement. The amount of provision outstanding at the year end should be shown as a liability without netting off reimbursements, if any. The reimbursement expected should be shown as an asset.

Definition of Contingent Liability:

(a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or

(b) a present obligation that arises from past events but is not recognised because:

- **(i)** it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
- **(ii)** the amount of the obligation cannot be measured with sufficient reliability.

Example:

A customer of XYZ has filed a case against them for providing them wrong product and not returning the same. XYZ has taken legal advice from their lawyer who believes it is not probable yet that resources may be required to settle the same. Since it is not meeting all the criteria of provision, it will be treated as contingent liability and will just be disclosed in the notes.

Possible obligation - an obligation is a possible obligation if, based on the evidence available, its existence at the balance sheet date is considered not probable.

Accounting treatment:

An enterprise should not recognise a contingent liability but should be disclosed. A contingent liability is disclosed, unless the possibility of an outflow of resources embodying economic benefits is remote.

Definition of contingent asset:

Contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.

EXAMPLE: claim that an enterprise is pursuing through legal processes, where the outcome is uncertain.

Accounting treatment:

An enterprise should not recognise a contingent asset and it is not disclosed in the financial statements. It is usually disclosed in the report of the approving authority (Board of Directors in the case of a company, and, the corresponding approving authority in the case of any other enterprise), where an inflow of economic benefits is probable.

Measurement

The amount recognised as a provision shall be the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. While making estimate of amount of the provision, the following points should be considered:

a. Entity should take account of the uncertainty surrounding the transaction, this may involve an expected value calculation (suitable in situation where there is a large population e.g. determining the size of warranty provisions).

b. Provision should be measured before tax.

c. The time value of money (the amount provided should be the present value of the expected cash flows using a pre-tax discount rate).

d. Profit on expected disposal of assets, even if closely linked with the provision should not be deducted from the amount of provision. For example, a restructuring provision cannot be reduced by an expected gain on disposal of a factory that is being sold as part of the restructuring. Instead, the gain will be recognized when the factory is sold.

e. Additional evidence provided by events after balance sheet date should be considered.

f. Future events may affect the provision. For example, entity may believe that the cost of cleaning up a site at the end of its life.

g. Provision for restructuring cost should include only the direct expenditure arising from restructuring and should not include retraining or relocating cost of continuing staff marketing or investment in new system and distribution network.

Application of the Recognition and Measurement Rules:

1. **Reimbursements:**
   - **i)** An, enterprise with a present obligation may be able to seek reimbursement of part or all of the expenditure from another party, for example via:
     - An insurance contract arranged to cover a risk;
     - An indemnity clause in a contract; or
     - A warranty provided by a supplier.
   - **ii)** The basis underlying the recognition of a reimbursement is that any asset arising is separate from the related obligation. The reimbursement should be recognised as an Asset when, and only when, it is virtually certain that reimbursement will be received & if the enterprise settles the obligation. In the statement of profit and loss, the expense relating to a provision may be presented net of the amount recognised for a reimbursement.
   - **iii)** In most cases, the enterprise will remain liable for the whole of the amount in question so that the enterprise would have to settle the full amount if the third party failed to pay for any reason. In this situation, a provision is recognised for the full amount of the liability, and a separate asset for the expected reimbursement is recognised when it is virtually certain that reimbursement will be received if the enterprise settles the liability.
   - **iv)** In some cases, the enterprise will not be liable for the costs in question if the third party fails to pay. In such a case, the enterprise has no liability for those costs and they are not included in the provision.
2. **FUTURE OPERATING LOSSES:**

   Future operating losses do not meet the definition of a liability and the general recognition criteria, therefore provisions should not be recognised for future operating losses.
3. **RESTRUCTURING:**
   - **i)** A Restructuring is a programme that is planned and controlled by management, and materially changes either:

     (a) The scope of a business undertaken by an enterprise; or

     (b) The manner in which that business is conducted.

     EXAMPLES:

     a. Sale or termination of a line of business

b. The closure of business locations in a country or region or the relocation of business activities from one country or region to another

c. Changes in management structure, for example, eliminating a layer of management

d. Fundamental re-organisations that have a material effect on the nature and focus of the enterprise's operations.

ii) A provision for restructuring costs is recognised only when the recognition criteria for provisions are met. No obligation arises for the sale of an operation until the enterprise is committed to the sale, i.e., there is a binding sale agreement.

iii) A restructuring provision should include only the direct expenditures arising from the restructuring, which are those that are both:

(a) Necessarily entailed by the restructuring; and

(b) Not associated with the ongoing activities of the enterprise.

iv) Some expenses relate to the future conduct of the business and are not liabilities for restructuring at the balance sheet date.

A restructuring provision does not include such costs as:

(a) Retraining or relocating continuing staff;

(b) Marketing; or

(c) Investment in new systems and distribution networks.

Changes in Provisions

Provisions should be reviewed at each balance sheet date and adjusted to reflect the current best estimate. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision should be reversed.

Use of Provisions

A provision should be used only for expenditures for which the provision was originally recognised. Only expenditures that relate to the original provision are adjusted against it.

Disclosure:

For each class of provision, an enterprise should disclose:

(a) The carrying amount at the beginning and end of the period;

(b) Additional provisions made in the period, including increases to existing provisions;

(c) Amounts used (i.e. incurred and charged against the provision) during the period; and

(d) Unused amounts reversed during the period.

For each class of contingent liability, an enterprise should disclose:

Unless the possibility of any outflow in settlement is remote, an enterprise should disclose a brief description of the nature of the contingent liability and, where practicable:

(a) An estimate of its financial effect,

(b) An indication of the uncertainties relating to any outflow;

Ind AS 37 vs. AS 29 – A Comparative View

Following are the major differences between Ind AS 37, Provisions, Contingent Liabilities and Contingent Assets and AS 29, Provision, Contingent Liabilities and Contingent Assets.

S. No.	Ind AS 37	AS 29
1.	The definition of provision and obligating event have been revised in Ind AS 37.	
2.	Ind AS 37 also defined the terms legal and constructive obligation.	
3.	Rules relating to restructuring provisions has been revised in Ind AS 37.	
4.	When the effect of time value of money is material, Ind AS 37 requires discounting.	Discounting is not permitted except for decommissioning, restoration and similar liabilities associated with property, plant and equipment
5.	Contingent assets are not recognized but disclosed in the financial statements when an inflow of economic benefits is probable.	Contingent assets are neither recognized nor disclosed in the financial statements and are usually disclosed in the report of the approving authority.
6.	Ind AS 37 makes it clear that before a separate provision for an onerous contract is established, an entity should recognize any impairment loss that has occurred on assets dedicated to that contract in accordance with Ind AS 36.	There is no such provision in As 29.
7.	Ind AS 37 gives an exception to this principle.	AS 29 states that identifiable future operating losses up to the date of restructuring are not included in a provision.

PROBLEMS FOR CLASS ROOM DISCUSSION

Problem No 1:

An entity sells goods with a warranty under which customers are covered for the cost of repairs of any manufacturing defects that become apparent within the first six months after purchase. If minor defects were detected in all products sold, repair costs of Rs. 1 lakh would result. If major defects were detected in all products sold, repair costs of Rs. 4 lakh would result. The entity's past experience and future expectations indicate that, for the coming year, 75 per cent of the goods sold will have no defects, 20 per cent of the goods sold will have minor defects and 5 per cent of the goods sold will have major defects.

Calculate the amount to be provided.

Problem No 2:

An entity has an obligation to restore an asset for the damage it has in the past. It has Rs.20 lakh cash to pay on 31.03.2020 relating to this liability. The entity considers that 15% is an appropriate discount rate. the time value of money is considered material. Calculate the amount to be provided.

Problem No 3:

X Ltd. has become subject to an obligating event on 01.04.2020 for which the company is committed to expenditure of Rs.5,00,000 at the end of 10 years. An appropriate discount rate is 10%. Show how the same is to be treated by X Ltd. (Show treatment up to 31.03.2022)

18. EMPLOYEE BENEFITS (Ind AS 19)

- **Meaning of Employee Benefits**

  Employee benefits are all forms of considerations given by an employer directly to the employee or their spouses, children or other dependents, or to others such as trusts, insurance companies in exchange of the service rendered by the employee.

  Accounting for employee benefits is governed by Ind AS 19, Employee Benefits.

- **Objective**

  The objective of this Standard is to prescribe the accounting and disclosure for employee benefits.

  The Standard requires an entity to recognise:

  (a) a liability when an employee has provided service in exchange for employee benefits to be paid in the future; and

  (b) an expense when the entity consumes the economic benefit arising from service provided by an employee in exchange for employee benefits.

- **Scope**

  1. This Standard shall be applied by an employer in accounting for all employee benefits, except those to which Ind AS 102, Share-based Payment, applies.

  2. This Standard does not deal with reporting by employee benefit plans.

  3. The employee benefits to which this Standard applies include those provided:

  (a) under formal plans or other formal agreements between an entity and individual employees, groups of employees or their representatives;

  (b) under legislative requirements, or through industry arrangements, whereby entities are required to contribute to national, state, industry or other multi-employer plans; or

  (c) by those informal practices that give rise to a constructive obligation.

- **Meaning of an Employee**

  For the purpose of this Standard, employee includes whole time directors and management personnel as well. Further, the Standard applies to all types of employer-employee relationships and there may not necessarily be a formal relationship.

- **Type of Employee Benefits**

  According to the Standard, there are four types of employee benefits as follows:

  (a) short-term employee benefits, if expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services:

  (i) wages, salaries and social security contributions;

(ii) paid annual leave and paid sick leave;

(iii) profit-sharing and bonuses; and

(iv) non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees;

(b) post-employment benefits, such as the following:

(i) retirement benefits (e.g., pensions and lump sum payments on retirement); and

(ii) other post-employment benefits, such as post-employment life insurance an post-employment medical care;

(c) Other long-term employee benefits, such as the following:

(i) long-term paid absences such as long-service leave or sabbatical leave;

(ii) jubilee or other long-service benefits; and

(iii) long-term disability benefits; and

(d) Termination benefits including voluntary retirement benefits (VRS).

Notes:

1. Employee benefits include benefits provided either to employees or to their dependents or beneficiaries and may be settled by payments (or the provision of goods or services) made either directly to the employees, to their spouses, children or other dependents or to others, such as insurance companies.
2. An employee may provide services to an entity on a full-time, part-time, permanent, casual or temporary basis. For the purpose of this Standard, employees include directors and other management personnel.

- **Accounting for Short Term Employee Benefits**

Accounting for short-term employee benefits as classified above is simple as there is no actuarial gain or loss to be recognized, as these are accounted for on undiscounted basis. Basic principles for accounting short-employee benefits are that the undiscounted amount of short-term employee benefits should be recognized when the employee rendered service:

It is recognized as an expense unless another Standard such as Ind AS-16 “Property, Plant and Equipment” requires it to be included in the cost of assets.

- It is recognized as a liability if the amount of short-term benefits exceeds amount actually paid or spent
- It is recognized as asset (pre-paid expenses) when amount actually paid exceeds the amount of short-term benefits.

a. Treatment of Short Term Paid Absences

An entity may pay employees for absence for various reasons including holidays, sickness and short-term disability, maternity or paternity, jury service and military service. Entitlement to paid absences falls into two categories - (a) accumulating; and (b) non-accumulating.

Accumulating paid absences are those that are carried forward and can be used in future periods if the current period's entitlement is not used in full. Accumulating paid absences may be either vesting (in other words, employees are entitled to a cash payment for unused entitlement on leaving the entity) or non-vesting (when employees are not entitled to a cash payment for unused entitlement on leaving).

An entity shall recognise the expected cost of short-term employee benefits in the form of paid absences as follows:

(i) in the case of accumulating paid absences, when the employees render service that increases their entitlement to future paid absences.

(ii) in the case of non-accumulating paid absences, when the absences occur.

Cost of non-accumulating type of compensated absences is automatically computed if the employees are on the regular pay-roll. In case employees are not in the regular pay-roll, then cost should be computed during their absences in the period in which the absences occur.

An entity shall measure the expected cost of accumulating paid absences as the additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period.

b. Treatment of Profit Sharing and Bonus Plan

Under some profit-sharing plans, employees receive a share of the profit only if they remain with the entity for a specified period. Such plans create an obligation as employees render service that increases the amount to be paid if they remain in service until the end of the specified period. The measurement of such obligations reflects the possibility that some employees may leave without receiving profit-sharing payments. Similarly, an entity may not have any legal obligation to pay bonus, but it may have the practice of bonus payment. As such the entity has no realistic alternative but to make the payment.

An entity should recognize the expected cost of profit-sharing and bonus payments when and only when;

- The entity has a present obligation to make such payments as a result of past events and;
- A reliable estimate of the obligation can be made.

- **Accounting for Post-Employment Benefits**

  Post-employment benefits are employee benefits (other than termination benefits and short-term employee benefits) that are payable after the completion of employment. They include (i) retirement benefits (e.g., pensions and lump sum payments on retirement); and (ii) other post-employment benefits, such as post-employment life insurance a post-employment medical care.

  Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans, depending on the economic substance of the plan as derived from its principal terms and conditions.

A. <u>Defined Contribution Plan</u>

Under defined contribution plans, the entity's obligation is limited to the amount that it agrees to contribute to the fund. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an employer (and also by the employee) to a post-employment benefit plan or to an insurance company, together with investment returns arising from the contributions; and employer is no longer liable to pay the post-employment benefits to the employee. In consequence, actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) fall, in substance, on the employee.

Defined contribution plans may be of following three types:

(i) Multi-employer Plans;

(ii) State Plans;

(iii) Insured Benefits.

(i) Multi-employer Plans: Multi-employer plans are defined contribution plans (other than state plans) or defined benefit plans (other than state plans) that:

- pool the assets contributed by various entities that are not under common control; and
- use those assets to provide benefits to employees of more than one entity, on the basis that contribution and benefit levels are determined without regard to the identity of the entity that employs the employees.

  An entity shall classify a multi-employer plan as a defined contribution plan or a defined benefit

  plan under the terms of the plan (including any constructive obligation that goes beyond the formal terms).

  If an entity participates in a multi-employer defined benefit plan, it shall:

- account for its proportionate share of the defined benefit obligation, plan assets and cost associated with the plan in the same way as for any other defined benefit plan; and
- disclose the information required.

When sufficient information is not available to use defined benefit accounting for a multiemployer defined benefit plan, an entity shall:

(a) account for the plan as if it were a defined contribution plan; and

(b) disclose the information required.

(ii) State Plan: State plans are established by legislation to cover all entities or entities of a specific industry and are operated by national or local Government, example of such plan in India are Provident Fund administrated by the Govt. of India.

State plan may be categorized as defined contribution plan or defined benefit plan based on obligation under the plan. However, in most of the cases such plans are defined contribution plans as entities/ employer has only obligation to pay the contribution and has no obligation to pay those future benefits.

Accounting in case of State plans: As State plans are normally defined contribution plans the contribution paid by the employer is debited to expense and if payable is credited to liability account.

(iii) Insured Benefits:

Where an employer takes insurance policy from an insurance company for meeting its obligation under post-employment benefits and the employer has no obligation to pay benefits to the employee and the insurer has sole responsibility for paying the post-employment benefits. The payments of fixed premium under such contract are, in substance, the settlement of the employee benefit obligation. Therefore, entities treat such payment as contribution to defined contribution plan.

However, if employer has the obligation to pay employee benefits when they fall due or to pay further amount if insurer does not pay, such plan shall be treated as defined benefit plan and not defined contribution plan and accounting shall be done accordingly.

Note: Accounting for defined contribution plans is straightforward because the reporting entity's obligation for each period is determined by the amounts to be contributed for that period. Consequently, no actuarial assumptions are required to measure the obligation or the expense and there is no possibility of any actuarial gain or loss. Moreover, the obligations are measured on an undiscounted basis, except where they are not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service. When an employee has rendered service to an entity during a period, the entity shall recognise the contribution payable to a defined contribution plan in exchange for that service:

(a) as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the end of the reporting period, an entity shall recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund.

(b) as an expense, unless another Ind AS requires or permits the inclusion of the contribution in the cost of an asset. When contributions to a defined contribution plan are not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service, they shall be discounted.

Note: An entity shall disclose the amount recognised as an expense for defined contribution plans.

B. <u>Defined Benefits Plan</u>

Defined benefit plans are post-employment benefit plans other than defined contribution plans. Under defined benefit plans:

(a) the entity's obligation is to provide the agreed benefits to current and former employees; and

(b) actuarial risk (that benefits will cost more than expected) and investment risk fall, in substance, on the entity. If actuarial or investment experience are worse than expected, the entity's obligation may be increased.

Accounting for defined benefit plans is complex because actuarial assumptions are required to measure the obligation and the expense and there is a possibility of actuarial gains and losses. Moreover, the obligations are measured on a discounted basis because they may be settled many years after the employees render the related service.

Accounting by an entity for defined benefit plans involves the following steps:

(a) determining the deficit or surplus. This involves:

(i) using an actuarial technique, the projected unit credit method, to make a reliable estimate of the ultimate cost to the entity of the benefit that employees have earned in return for their service in the current and prior periods.

(ii) discounting that benefit in order to determine the present value of the defined benefit obligation and the current service cost.

(iii) deducting the fair value of any plan assets from the present value of the defined benefit obligation.

(b) determining the amount of the net defined benefit liability (asset) as the amount of the deficit or surplus determined in (a), adjusted for any effect of limiting a net defined benefit asset to the asset ceiling.

(c) determining amounts to be recognised in profit or loss:

(i) current service cost.

(ii) any past service cost and gain or loss on settlement.

(iii) net interest on the net defined benefit liability (asset).

(d) determining the remeasurements of the net defined benefit liability (asset), to be recognised in other comprehensive income, comprising:

(i) actuarial gains and losses;

(ii) return on plan assets, excluding amounts included in net interest on the net defined benefit liability (asset); and

(iii) any change in the effect of the asset ceiling, excluding amounts included in net interest on the net defined benefit liability (asset).

Where an entity has more than one defined benefit plan, the entity applies these procedures for each material plan separately.

An entity shall determine the net defined benefit liability (asset) with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the end of the reporting period.

C. <u>Accounting for Other Long-Term Employee Benefits</u>

Other long-term employee benefits include items such as the following, if not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service:

(a) long-term paid absences such as long-service or sabbatical leave;

(b) jubilee or other long-service benefits;

(c) long-term disability benefits;

(d) profit-sharing and bonuses; and

(e) deferred remuneration.

The accounting for long-term employee benefits is similar to post-employment defined benefit plans except that all past service cost is recognised immediately.

The measurement of other long-term employee benefits is not usually subject to the same degree of uncertainty as the measurement of post-employment benefits. For this reason, this Standard requires a simplified method of accounting for other long-term employee benefits. Unlike the accounting required for post-employment benefits, this method does not recognise remeasurements in other comprehensive income.

Although this Standard does not require specific disclosures about other long-term employee benefits, other Ind ASs may require disclosures. For example, Ind AS 24 requires disclosures about employee benefits for key management personnel. Ind AS 1 requires disclosure of employee benefits expense.

D. Accounting for Termination Benefits

Termination benefits result from either an entity's decision to terminate the employment or an employee's decision to accept an entity's offer of benefits in exchange for termination of employment. Termination benefits do not include employee benefits resulting from termination of employment at the request of the employee without an entity's offer, or as a result of mandatory retirement requirements, because those benefits are post-employment benefits.

An entity shall measure termination benefits on initial recognition, and shall measure and recognise subsequent changes, in accordance with the nature of the employee benefit, provided that if the termination benefits are an enhancement to post-employment benefits, the entity shall apply the requirements for post-employment benefits.

Otherwise:

(a) if the termination benefits are expected to be settled wholly before twelve months after the end of the annual reporting period in which the termination benefit is recognised, the entity shall apply the requirements for short-term employee benefits.

(b) if the termination benefits are not expected to be settled wholly before twelve months after the end of the annual reporting period, the entity shall apply the requirements for other long-term employee benefits.

Although this Standard does not require specific disclosures about termination benefits, other Ind ASs may require disclosures. For example, Ind AS 24 requires disclosures about employee benefits for key management personnel. Ind AS 1 requires disclosure of employee benefits expense.

Ind AS 19 vs. AS 15 – A Comparative View

Following are the major differences between Ind AS 19, Accounting for Employee Benefits and AS 15, Employee Benefits:

S. No.	Ind AS 19	AS 15
1.	In Ind AS 19, employee benefits arising from constructive obligations are also covered.	AS 15 does not deal with the same.
2.	Ind AS 19 the term 'employee' includes directors.	As per AS 15, the term 'employee' includes whole-time directors.
3.	Ind AS 19 deals with situations where there is a contractual agreement between a multi-employer plan and its participants that determines how the surplus in the plan will be	AS 15 does not deal with it.

	distributed to the participants (or the deficit funded).	
4.	As per Ind AS 19, participation in a defined benefit plan sharing risks between various entities under common control is a related party transaction for each group entity and some disclosures are required in the separate or individual financial statements of an entity.	AS 15 does not contain similar provisions.
5.	Ind AS 19 encourages, but does not mandate, entities to involve a qualified actuary in the measurement of all material post-employment benefit obligations.	No such guidelines are present in AS 15. AS 15 does recognise that enterprises would normally use the services of a qualified actuary.
6.	Detailed actuarial valuation to determine the present value of net defined benefit liability (asset) is performed with sufficient regularity so that the amounts recognized in the financial statements do not differ materially from the amounts that would have been determined at the end of the reporting period. Ind AS 19 does not specify sufficient regularity.	Detailed actuarial valuation to determine the present value of defined benefit obligation is carried out at least once every 3 years and fair value of plan assets are determined at each balance sheet date.
7.	Ind AS 19 requires that the same shall be recognised in other comprehensive income and should not be recognised in profit or loss.	AS 15 requires recognition of actuarial gains and losses immediately in the profit and loss.
8.	Ind AS 19 makes it clear that financial assumptions shall be based on market expectations, at the end of the reporting period, the period over which the obligations are to be settled.	AS 15 does not clarify the same.
9.	As per Ind AS 19, subsidiaries, associates, joint ventures and branches domiciled outside India shall discount post-employment benefit obligations arising on account of post-	As per AS 15, the rate used to discount post- employment benefit obligations should always be determined by reference to market yields at the

	employment benefit plans using the rate determined by reference to market yields at the end of the reporting period on high quality corporate bonds. In case, such subsidiaries, associates, joint ventures and branches are domiciled in countries where there is no deep market in such bonds, the market yields (at the end of the reporting period) on government bonds of that country shall be used.	balance sheet date on government bond.
10.	Under Ind AS 19, more guidance has been given for timing of recognition of termination benefits.	Recognition criteria for termination benefits differ from the criteria given in Ind AS 19.
11.	It provides guidance on accounting for contributions from employees or third parties to defined benefit plans, which are linked to service - both dependent and independent of the number of years of service.	No specific guidance.

PROBLEMS FOR CLASS ROOM DISCUSSION

Problem No 1:

A Ltd. has 100 employees. Each employee is entitled to 10 days sick leave each year. Unused sick leave is carried forward for one year. An employee avails the carried forward leave only if the current year's entitlement falls short of the leave he or she requires.

On December 31, 2020, the average unused sick leave is 2 days per employee. The management, based on experience, estimates that in the year 2021, only 10% of the employees will use one day from their carried forward leave and the rest of the employees will not require more than 10 days of leave. Average payment per employee per day is Rs.100. How will you treat this?

Problem No 2:

Mr. X is an employee of ABC Ltd. His annual salary is Rs.15 lakh. The company follows a 300 working days policy. As per the policy of the company, Mr. X is entitled to a leave of 10 days for 2020-21. He, however, utilises 8 days leave. The unutilised leaves are not allowed to be carried forward but are settled by way of payment to the employee. Compute the total employee benefit expenses of ABC Ltd. in respect of Mr. X.

Problem No 3:

A profit-sharing plan requires an entity to pay a specified proportion of its net profit for the year to employees who serve throughout the year. If no employee leaves during the year, the total profit-sharing payments for the year will be 5% of net profit. The entity estimates that some of the staff may leave during the year and therefore not entitled for profit sharing this will reduce the payment of profit-sharing plan from 5% to 4% of net profit. Advise the company.

Problem No 4:

Consider the following information:

No. of employees (same as the previous year) = 150

Employees' turnover rate = 6%

Bonus paid to each employee last year = Rs.1,00,000

Increase in bonus rate due to inflation = 7% (as per company's regular practice) Determine the liability and expense to be recognised.

Problem No 5:

The following information applies to a company's defined benefit pension plan for the year:

FMV of plan assets (beginning of the year)	Rs.2,00,000
FMV of plan assets (end of the year)	Rs.2,85,000

Employer's contribution	Rs. 70,000
Benefit paid	Rs. 50,000

Calculate the actual return on plan assets.

<u>Problem No 6:</u>

Consider the following information provided by Y Ltd:

PV of defined contribution obligations Rs.15 lakh.

Fair value of plan assets Rs.14.12 lakh

How will you treat the above for presentation in the Balance Sheet?

<u>Problem No 7:</u>

Consider the following information provided by Z Ltd:

PV of defined contribution obligations Rs.15 lakh.

Fair value of plan assets Rs.15.22 lakh

Asset ceiling Rs.0.19 lakh

How will you treat the above for presentation in the Balance Sheet?

19. PRESENTATION OF FINANCIAL STATEMENTS (Ind AS 1)

- **Introduction:**

  Financial statements are the end products of accounting. Thus, they must reflect a true and fair view of the financial performance and financial position of the organisation in order to facilitate appropriate decisions by the users of accounting information. Accordingly, the financial statements must possess certain characteristics and be prepared based on certain well-defined principles. Ind AS 1, Presentation of Financial Statements, prescribes the principles for preparation of General-Purpose Financial Statements, their structures and minimum content requirements as well as guidelines for specific disclosure in India.

- **Applicability**

  This Standard applies to all profit-oriented business undertakings including public sector business entities. Non-profit entities may also apply the provisions of this Standard with suitable modification in terminology used. It is also equally applicable to all entities which prepares Consolidated Financial Statements and Separate Financial Statements as defined in Ind AS 27, Consolidated and Separate Financial Statements. However, the standard does not apply to condensed/summarized financial statements covered by Ind AS-34, Interim Financial Reporting.

- **Meaning of General-Purpose Financial Statements**

  General purpose financial statements (referred to as 'financial statements') are those intended to meet the needs of users who are not in a position to require an entity to prepare reports tailored to their particular information needs. Hence, their use is 'General' and not specific.

- **Objectives of Financial Statements**

  1. Financial statements are a structured representation of the financial position and financial performance of an entity. The objective of financial statements is to provide information about the financial position (assets, liabilities and equity), financial performance (income/expenses, gains and losses) and cash flows (movement of cash and cash equivalent) of an entity that is useful to a wide range of users in making economic decisions. Financial statements also show the results of the management's stewardship of the resources entrusted to it

  2. The information available from financial statements, along with other information in the notes, assists users of financial statements in predicting the entity's future cash flows and, in particular, their timing and certainty.

- **Complete Set of Financial Statements**

  A complete set of financial statements comprises:

  (a) a balance sheet as at the end of the period;

(b) a statement of profit and loss for the period in a single statement of profit and loss, with profit or loss and other comprehensive income presented in two sections. The sections shall be presented together, with the profit or loss section presented first followed directly by the other comprehensive income section.;

(c) Statement of changes in equity for the period;

(d) a statement of cash flows for the period;

(e) notes, comprising a summary of significant accounting policies and other explanatory information; and comparative information in respect of the preceding period.

(f) a balance sheet as at the beginning of the preceding period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.

Note: An entity shall present with equal prominence all of the financial statements in a complete set of financial statements.

Entities may provide additional information on a voluntary basis such as Environmental Reports, Value Added Statement and Human Resource Statement.

- **General Features of Financial Statements**

  The above financial statements must possess the following features or characteristics in order to be relevant and reliable:

  a. True and fair presentation and compliance with Ind ASs.

  b. Adherence to Going Concern assumption

  c. Accrual basis of accounting

  d. Materiality and aggregation

  e. Offsetting

  f. Frequency of reporting (financial statements are to be prepared at least annually)

  g. Comparative information (information for the previous period should be disclosed unless exempted by Ind AS)

  h. Consistency of presentation (similar accounting policies should be continued; changes if any for appropriate presentation or as required by Ind AS will be allowed).

These features are discussed below.

a. True and fair presentation and compliance with Ind ASs.

Financial statements shall present a true and fair view of the financial position, financial performance and cash flows of an entity. Such presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework. The application of Ind ASs, with additional disclosure, when necessary, is presumed to result in financial statements that present a true and fair view.

An entity whose financial statements comply with Ind ASs shall make an explicit and unreserved statement of such compliance in the notes.

However, an entity cannot rectify inappropriate accounting policies either by disclosure of the accounting policies used or by notes or explanatory material. Any departure from any Ind AS requirement must be disclosed along with the financial effect of the departure on each item in the financial statements that would have been reported in complying with the requirement.

b. Going Concern

Financial statement should be prepared assuming that the entity will continue its business in foreseeable future unless management intends to liquidate the entity or cease trading or has no realistic option but to close. Material uncertainties regarding the continuance of the business, if any, should be disclosed. In case the financial statement have not been prepared on going concern basis that fact should be disclosed together with the basis on which they have been prepared.

c. Accrual basis of accounting

An entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting. Thus, asset and liabilities will be recognized when they are receivable and payable rather than when actually received or paid.

d. Materiality and aggregation

Each material class of similar items shall be presented separately in the financial statement, Items which are not material need not to be disclosed except if it is required by law.

e. Offsetting

An entity shall not offset assets and liabilities or income and expenses, unless required or permitted by an Ind AS.

f. Frequency of reporting

An entity shall present a complete set of financial statements (including comparative information) at least annually. When an entity changes the end of its reporting period and presents financial statements for a period longer or shorter than one year, an entity shall disclose the following, in addition to the period covered by the financial statements:

(a) the reason for using a longer or shorter period, and

(b) the fact that amounts presented in the financial statements are not entirely comparable.

g. Comparative information

(i) Minimum comparative information

Except when Ind ASs permit or require otherwise, an entity shall present comparative information in respect of the preceding period for all amounts reported in the current period's financial statements. An entity shall present, as a minimum, two balance sheets, two statements of profit and loss, two statements of cash flows and two statements of changes in equity, and related notes.

(ii) Additional comparative information

An entity may present comparative information in addition to the minimum comparative financial statements required by Ind ASs, as long as that information is prepared in accordance with Ind ASs.

Note: When there is change in accounting policy and such change is retrospectively applied or there is retrospective restatement of item in the financial statement then the entity shall present a minimum of three balance sheet, two profit or loss statement and two cash flow.

When it is impracticable to re-classify comparative amounts, an entity must disclose the reason thereof.

h. Consistency of presentation

Entities should retain their presentation and classification of items from one period to the next. Change may be allowed only when

(i) the change result in a more appropriate presentation

(ii) it is required by an Ind AS.

<u>Disclosure Under Ind AS 1</u>

(a) Significant Accounting Policies

An entity shall disclose in the summary of significant accounting policies:

(i) the measurement basis (or bases) used in preparing the financial statements, and

(ii) the other accounting policies used that are relevant to an understanding of the financial statements. An entity shall disclose, in the summary of significant accounting policies or other notes, the judgements, apart from those involving estimations, that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

(b) Sources of estimated uncertainty

An entity shall disclose information about the assumptions it makes about the future, and other major sources of estimation of uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

In respect of those assets and liabilities, the notes shall include details of:

(a) their nature, and

(b) their carrying amount as at the end of the reporting period.

(c) Capital Management Policies

An entity shall disclose information that enables users of its financial statements to evaluate the entity's objectives, policies and processes for managing capital. Accordingly, the entity shall disclose information relating to the qualitative aspects of capital, quantitative aspects of capital, management of both the aspects, externally imposed restrictions on capital and any violation of these restrictions during the year.

(d) Information regarding puttable financial instruments

(e) Other disclosures

An entity shall disclose in the notes:

(i) the amount of dividends proposed or declared before the financial statements were approved for issue but not recognised as a distribution to owners during the period, and the related amount per share; and

(ii) the amount of any cumulative preference dividends not recognised.

An entity shall disclose the following, if not disclosed elsewhere in information published with the financial statements:

(i) the domicile and legal form of the entity, its country of incorporation and the address of its registered office (or principal place of business, if different from the registered office);

(ii) a description of the nature of the entity's operations and its principal activities;

(iii) the name of the parent and the ultimate parent of the group; and

(iv) if it is a limited life entity, information regarding the length of its life.

COMMON QUESTIONS FROM IND AS

Multiple Choice Questions

1. The objective of Ind AS 1 Presentation of Financial Statements is to:

A. provide basis for presentation of general-purpose financial statements

B. sets out overall requirements for the presentation of financial statements,

C. sets out guidelines for financial statements structure

D. All of the above

2. An entity shall apply Ind AS 1 in:

A. preparing and presenting general purpose financial statements in accordance with Indian Accounting Standards (Ind ASs).

B. preparing and presenting financial statements in accordance with Indian Accounting Standards (Ind ASs).

C. preparing and presenting financial statements in accordance with Accounting Standards.

D. preparing and presenting general purpose financial statements in accordance with Accounting Standards.

3. Ind AS 1 "Presentation of financial statements" applies to

A. Consolidated financial statements in accordance with Ind AS 110, Consolidated Financial Statements,

B. Separate financial statements in accordance with Ind AS 27, Separate Financial Statements.

C. Both of the above

D. Only a

4. Ind AS 2, Inventories, does not apply to

A. Financial Instruments

B. Biological Assets

C. Both the above

D. (A) but not (B)

5. Cost of inventories does not include

A. costs of purchase,

B. costs of conversion

C. other costs incurred in bringing the inventories to their present location and condition

D. Finance cost

6. Which of the following costs are not excluded from cost of inventory?

A. Selling cost

B. Administrative cost

C. Abnormal loss

D. Carriage and freight inward

7. Which of the following is an employee benefit?

A. Short term employee benefits

B. Long term employee benefits

C. Termination benefits

D. All of the above

8. Which of the following is not a part of other long-term benefits?

A. long-term disability benefits

B. retirement benefits

C. profit-sharing and bonuses

D. deferred remuneration

9. Short term employee benefits include –

A. Wages

B. Salaries

C. Employer's contribution to P.F

D. All of the above

10. Which of the following is a defined contribution plan?

A. Multi-employer plan

B. State plan

C. Insured benefits

D. All of the above

[Answer: 1-D; 2-A; 3-C; 4-C; 5-D; 6-D; 7-D; 8-B; 9-D; 10-D]

Numerical-Multiple Choice Questions

11. The expected sales value of stock is Rs.20 lakhs and a commission at 10% on sale is payable to the agent. Calculate NRV.

A. Rs.12 lakh

B. Rs.14 lakh

C. Rs.16 lakh

D. Rs.18 lakh

12. 01.04.2020 B Ltd. has 1200 ordinary shares outstanding. On 31.08.2021 it issued 400 ordinary shares for cash. On 31.01.21 it bought back 200 ordinary shares. Calculate weighted average number of shares as on 31.03.21.

A. 1300

B. 1400

C. 1500

D. 1600

13. Fair value before right issue Rs.20. Theoretical ex-right fair value Rs.18. Calculate right factor.

A. 1.2

B. 1.15

C. 1.11

D. 1.10

14. Salary payable per day Rs.1000; Working days 300; leave unutilized during the year 3 days; unutilized leaves are not allowed to carried forward but are settled through payment. What is the expense to be recognised as per Ind AS 19?

A. Rs.3,00,000

B. Rs.3,30,000

C. Rs.3,03,000

D. Rs.3,000

15. Ordinary shares are 1,00,000 of Rs. 1.00;10% Preference shares are 200000 of Rs. 1.00; PAT Rs.10,00,000. Calculate basic EPS.

A. Rs.9.80

B. Rs.9.60

C. Rs.9.40

D. Rs.9.20

[Answer: 11-D; 12-B; 13-C; 14-C; 15-A]

<u>State True or False</u>

1. Abnormal amounts of wasted materials, labour or other production costs are not part of the cost of inventories.

2. Financial statement should normally be prepared assuming going concern.

3. Provisions shall be recognised for future operating losses.

4. Purchased options are dilutive.

5. Under defined contribution plans, the entity's obligation is limited to the amount that it agrees to contribute to the fund.

[Answer: 1.True; 2.True; 3.False; 4.False; 5.True]

Fill in the Blanks

1. In case of a company, events after the reporting period are event that occur between the end of the reporting period and_.
2. Voluntary retirement scheme is a type of___benefits.
3. ___ earnings per share are calculated when there are potential ordinary shares in capital structure of the entity.
4. An entity shall_the amounts recognised in its financial statements to reflect non-adjusting events after the reporting period.
5. Contingent liabilities do not have any___obligation.

[Answer: 1.date of approval of the financial statements; 2.termination; 3.Diluted; 4.not adjust; 5.present]

Comprehensive Numerical Problems

1. ABC Ltd. produced 20,00,000 units of product A during the year 2020-21 per unit cost is as follows:

Raw Material	Rs.100
Direct wages	Rs. 50
Direct Expenses	Rs.2

   Production overhead is Rs. 40,00,000 of which 40% is fixed. The company sold 16,00,000 units and 4,00,000 units were in stock as on 31/3/2021. Normal capacity is 10,00,000 units. Calculate the value of closing stock. **[Answer: Rs. 6.192 crores]**

2. Cost of Production of product M is given below: Material per unit Rs. 120

Wages per unit	Rs. 80
Overhead per unit	Rs. 50

   As on the balance sheet date, the replacement cost of raw material is Rs. 105 per unit. There were 2000 units of raw material on 31.03.2021.

   Calculate the value of closing stock of raw material in following conditions:

   (a) If finished product is sold at the rate of Rs.270 per unit, what will be value of closing stock of raw material?

   (b) If finished product is sold at the rate of Rs. 235 per unit, what will be value of closing stock of raw material? **[Answer: (a) Rs. 2,40,000. (b) Rs. 2,10,000]**

3. On the basis of the following information, calculate the actual return on pension plan assets.

   Benefits paid Rs.2,50,000

   Contribution Rs.3,25,000

FMV of plan assets at the end Rs.15,00,000

FMV of plan assets at the beginning Rs.10,00,000

[Answer: Rs.4,25,000]

4. ABC Ltd. is a pharmaceutical company. It has received an actuarial valuation for the first time for its pension scheme which revealed a surplus of Rs.10,00,000. the company wants to spread the same over the next 5 years by reducing the contribution from Rs.5,00,000 to Rs.3,00,000. The average remaining life of the employee is 10 years. You are required to advise the company.

[Answer: Actuarial gain to be immediately recognized in other comprehensive income]

5. PQR Ltd. is in a legal suit with the municipal authorities regarding property tax. The company gets a court order in its favour on 10th April, 2021, which resulted into reducing the tax liability as on 31st March, 2021. The financial statements for 2020-21 were approved by the BODs on 11th May, 2021. The management is not in favour of adjusting the event as it thinks that favourable events after the reporting period would hamper the realisation concept of accounting. Comment on the company's views in the light of Ind AS 10.

[Answer: Favourable events should also be considered]

6. The financial statements of XYZ Ltd. for the financial year 2020-21 were approved by the BOD on 10.05.2021. A fraud relating to the accounts of 2019-20 was identified on 15.04.2021. Is it an adjusting event? Give your opinion in the light of Ind AS 10.

[Answer: It is an adjusting event.]

7. Ordinary shares outstanding on 01.01.21

1000,000 Profit for the year ended on 31.12.21 Rs.1,00,000

Average fair value during the year Rs.8

The company has in issue 200,000 options to purchase equal ordinary shares at exercise price of Rs.6 per share.

Calculate the diluted EPS. **[Answer: Rs.0.95]**

8. P Ltd. had outstanding ordinary shares of 1,00,000 on 01.01.2021. Profit for the year is 2020 is Rs.2,20,000 and for 2021 is Rs.3,00,000. On 01.03.21 it issued 1 new share for every 5 shares outstanding at Rs.15. Fair value of 1 ordinary share before right issue was Rs.21. Calculate (i) Basic EPS for 2021 and (ii) Restated EPS for 2020. **[Answer: (i) Rs.2.55; (ii) 2.10]**

<u>**Short Essay Type Questions:**</u>

1. What does a complete set of financial statements include?
2. What do you mean by inventory? What is net realizable value?

3. State the disclosure requirements of Ind AS 2.
4. Discuss different types defined contribution plans.
5. How will you calculate basic EPS?
6. When is diluted EPS calculated?

Essay Type Questions:

1. Discuss the general features of financial statements.
2. How will you account for termination benefits?
3. How will you account for distribution of non-cash assets to the owners?
4. State the disclosure requirements for provisions as per Ind AS 37.
5. How will you treat written put options in calculating diluted EPS?