TOPIC - 2

(CHAPTER 4 UNIT 1 OF ICAI)

FINANCIAL STATEMENTS OF COMPANIES

SCHEDULE III TO THE COMPANIES ACT, 2013

Division I

Financial Statements for a company whose financial statements are drawn up in compliance of the Companies (Accounting Standards) Rules, 2006.

Dear Students,
In this topic, I have included important points of Schedule III relevant for Examination purpose. For full annexure u can refer ICAI Module.

GENERAL INSTRUCTIONS FOR PREPARATION OF FINANCIAL STATMENT OF A COMPANY REQUIRED TO COMPLY WITH AS

1. Every company, to which Accounting Standards apply, shall prepare its financial statements in accordance with this Schedule or with such modification as may be required under certain circumstances.
2. The disclosure requirements specified in this Schedule are in addition to and not in substitution of the disclosure requirements specified in the Indian Accounting Standards.
   Additional disclosures specified in the Accounting Standards shall be made in the Notes or by way of additional statement or statements unless required to be disclosed on the face of the Financial Statements.
3. Each item on the face of the Balance Sheet and Statement of Profit and Loss shall be cross-referenced to any related information in the Notes.
   In preparing the Financial Statements including the Notes, a balance shall be maintained between providing excessive detail that may not assist users of Financial Statements and not providing important information as a result of too much aggregation.
4. Depending upon the turnover of the company, the figures appearing in the Financial Statements shall be rounded off as below:

Turnover	Rounding off
(i) less than one hundred crore rupees	To the nearest hundreds, thousands, lakhs or millions, or decimals thereof
(li) one hundred crore rupees or more	To the nearest, lakhs, millions or crores, or decimals thereof.

Once a unit of measurement is used, it should be used uniformly in the Financial Statements.

5. **Financial Statements shall contain the corresponding amounts (comparatives) for the immediately preceding reporting period for all items shown in the Financial Statement including Notes except in the case of first Financial Statements laid before the company after incorporation.**

Part I

Balance Sheet as at......................

(Rupees in.........)

	Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
	1	2	3	4
(1)	EQUITY AND LIABILITIES			
1.	Shareholders' Fund			
a	Share Capital			
b	Reserves & Surplus			
c	Money Received Against Share Warrants			
2.	Share Application Money Pending Allotment			
3.	Non-Current Liabilities			
a	Long term borrowings			
b	Deferred Tax Liabilities (Net)			
c	Long-Term Provisions			
4.	Current liabilities			
a	Short Term Borrowings			
b	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			
c	enterprises.			
d	Other Current Liabilities			
	Short Term Provisions			
	Total			
(2)	ASSETS			
1	Non- Current Assets			
a	Property, Plant and Equipment			
	i. Tangible Assets			
	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 & Advances
e	Other Non-Current Assets
2	Current Assets Current Investments Inventories Trade receivables Cash and cash equivalents Short Term Loans and Advances Other Current Assets
	Total

GENERAL INSTRUCTIONS FOR PREPARATION OF BALANCE SHEET

1. Current Asset

An entity shall classify an asset as current when-

(a) It expects to realize the asset, or intends to sell or consume it, in its normal operating cycle; (eg. Debtors, Inventory)

(b) It holds the asset primarily for the purpose of trading; (eg. Derivative Instruments)

(c) It expects to realize the asset within twelve months after the reporting period; or

(d) The asset is cash or a cash equivalent *unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.*

An entity shall classify all other assets as non-current.

2. Operating Cycle:

The operating cycle of an entity is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents, when the entity's normal operating cycle is not clearly identifiable, it is assumed to be twelve months.

3. Current Liability:

An entity shall classify a liability as current when-

(a) It expects to settle the liability in its normal operating cycle;

(b) It holds the liability primarily for the purpose of trading;

(c) The liability is due to be settled within twelve months after the reporting period; or

(d) It does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period. Terms of a liability that could, at the option of the counterparty, result in it settlement by the issue of equity instruments do not affect its classification. (eg. Loan taken from banks)

An entity shall classify all other liabilities as non-current.

4. A receivable shall be classified as a 'trade receivable' if it is in respect of the amount due on account of goods sold or services rendered in the normal course of business.

5. A payable shall be classified as a 'trade payable' if it is in respect of the amount due on account of goods purchased or services received in the normal course of business.

6. A company shall disclose the following in the Notes:

A. Reserves & Surplus

(i) Reserves & Surplus shall be classified as-

(a) Capital Reserve;

(b) Capital Redemption Reserve;

(c) Security Premium;

(d) Debenture Redemption Reserve;

(e) Revaluation Reserve;

(f) Share Options Outstanding Account; and

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

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

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

(ii) A reserve specifically represented by earmarked investments shall be termed as a 'Fund'.

(iii) Debit balance of Statement of Profit and Loss shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserve & Surplus', after adjusting negative balance of Surplus, if any, shall be shown under the head 'Reserves & Surplus' even if the resulting figure is in the negative.

B. Non-Current Liabilities

Long-Term Borrowings	Other Long Term Liabilities	Provisions
Classified into: • Bonds/Debentures • Term Loans from Banks • Term Loans from Parties • Deferred payment liabilities • Deposits • Loans from related parties • Long term maturities of Finance	Classified into- • Trade Payables • Others	Classified into: • Provision for Employee benefits • Others

Leases • Other Loans Further Classified as Secured and Unsecured along with nature of security. Any guarantees by directors or others Terms of Repayments Period and amount of default as on BS date		

C. Current Liabilities

Borrowings	Other CL	Provisions	Trade Payables
Classified into: • Term Loans from Banks • Term Loans from Other Parties • Loans from Related Parties • Deposits • Other Loans Further Classified as Secured and Unsecured along with nature of security. Any guarantees by directors or others Period and amount of default as on BS date	Classified into- (a) Current maturities of long-term debt; (b) Current maturities of finance lease obligations; (c) Interest accrued but not due; (d) Interest accrued & due; (e) Income Received in Advance; (f) Unpaid dividends; (g) Application money received for allotment of securities to the extent refundable & interest accrued thereon; (h) Unpaid matured deposits & interest accrued thereon; (i) Unpaid matured debentures & interest accrued thereon; & (j) Others	Classified into: • Provision for Employee benefits • Others	Classified into- • Outstanding from Micro Enterprises & Small Enterprises; and • Outstanding from others For MESE, provide details regarding Principal amount and interest amount due and paid.

D. NON-CURRENT ASSETS

1. Property. Plant and Equipment:

(i) Classification shall be given as:

(a) Land

(b) Buildings

(c) Plant and Equipment

(d) Furniture and Fixtures

(e) Vehicles

(f) Office equipment

(g) Others (specify nature)

(ii) Assets under lease shall be separately specified under each class of assets

(iii) 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 and other adjustments and the related depreciation and impairment losses or reversals shall be disclosed separately.

II. Intangible assets

i. Classification shall be given as:

(a) Goodwill

(b) Brands or trademarks

(c) Computer software

(d) Mastheads and publishing titles

(e) Mining rights

(f) Copyright, patents, other intellectual property rights, services and operating rights

(g) Recipes, formulae, models, designs and prototypes

(h) Licenses and franchises

(i) Others (specify nature)

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 and other adjustments and the related amortization and impairment losses or reversals shall be disclosed separately.

III.

Investments	Loans & Advances	Other Non- Current Assets
Investments shall be classified as – (a)Trade Investments (b) Others Further Classified as Investment in – • Investment Property • Equity • Preference • Govt. & Other Sec • Debentures/Bonds • Mutual Funds	Classify loans into- • Capital Advances • Security Deposits • Loans to related Parties • Others Sub classified into – • Secured - Good • Unsecured - Good • Doubtful	Classified into- • Long Term Trade Receivables • Others Long Term Trade Receivables sub classified into – • Secured - Good • Unsecured – Good • Doubtful

• Partnership Firms • Others Investments carried at other than at Cost should be separately stated. Disclose quoted investments & their market values separately from unquoted investments.	Provision for bad & doubtful debts shall be separately disclosed under the relevant head. Loans due by directors/officers of entity shall be separately disclosed.	Provision for bad & doubtful debts shall be separately disclosed under the relevant head. Loans due by directors/officers of entity shall be separately disclosed.

IV. Bank deposits with more than 12 months maturity shall be disclosed under 'Other financial assets'.

E. Current Assets

Inventories	Investments	Trade Receivables	Cash & Cash Equivalents	Loans
Classified into- Raw Materials WIP Finished Goods Stock in Trade (acquired for trading) Stores & Spares Loose tools Others GIT shall be disclosed under sub-heads separately Mode of valuation shall be disclosed	Investments shall be classified as Equity, Pref, Govt., Debn, MF & Others. Also, details regarding Investments in Subsidiaries, Associates, JV shall also be given from above classification. Disclose quoted investments & their market values separately from unquoted investments.	Receivables outstanding for a period of more than six months from the Date they are due for payment should be separately stated. Sub classified into- Secured – Good Unsecured – Good Doubtful Provision for bad & doubtful debts shall be separately disclosed under the relevant head. Debts due by directors/officers of entity shall be separately disclosed.	Classified into- • Balance with Banks • Cheques/Drafts on hand • Cash on Hand • Others Bank Deposits with more than 12 Months maturity shall be disclosed separately.	Classify loans into- • Loans to related Parties • Others Sub classified into – • Secured - Good • Unsecured – Good • Doubtful Provision for bad & doubtful debts shall be separately disclosed under the relevant head. Loans due by directors/officers of entity shall be separately disclosed.

F. Contingent Liabilities and Commitments

(To the extent not provided for)

(I) Contingent Liabilities shall be classified as-

(a) Claims against the company not acknowledged as debt;

(b) Guarantees excluding financial guarantees; and

(c) Other money for which the company is contingently liable.

(ii) Commitments shall be classified as-

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

(b) Uncalled liability on shares and other investments partly paid; and

(c) Other commitments (specify nature).

PART II - STATEMENT OF PROFIT AND LOSS

Name of the Company.........................

Statement of Profit and Loss for the period ended................

	Particulars	Note No.	Figures as at the end of current reporting period	Figures for the previous reporting period
I	Revenue from operations	AS 9 & 7		
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 & Extra Ordinary Items items and tax (I-IV)			
VI	Exceptional Items			
VII	Profit/ (loss) before Extra-Ordinary Items and Tax (V-VI)			
VIII	Extra Ordinary Items			
IX	Profit Before Tax (VII – VIII)			
X	Tax expense: (1) Current tax (2) Deferred tax	AS – 12		
XI	Profit (Loss) for the period from continuing operations (VII - VIII)			

XII	Profit/(loss) from discontinued operations			
XIII	Tax expenses of discontinued operations			
XIV	Profit/(loss) from Discontinued operations (after tax) (XII-XIII)			
XV	Profit/(loss) for the period (XI+XIV)			
XVI	Earnings per equity share (1) Basic (2) Diluted	AS 20		

See accompanying notes to the financial statements

GENERAL INSTRUCTIONS FOR PREPARING OF STATEMENT OF PROFIT AND LOSS

1. Revenue from operations shall disclose separately in the notes (Other than Finance Company)
   (i) Sale of Products;
   (ii) Sale of Services; and
   (iii) Other operating revenues.
   (iv) Less – Excise duty
2. In respect of Finance Companies, Revenue from Operation shall include Revenue from
   (a) Interest; and
   (b) Other Financial Services
3. Finance Costs: Finance costs shall be classified as-
   (i) Interest;
   (ii) Other Borrowing Costs;
   (iii) Exchange differences regarded as an adjustment to borrowing costs; and
4. Other income: other income shall be classified as-
   (a) Interest Income;
   (b) Dividend Income;
   (c) Net Gain/Loss on sale of Investments
   (d) Other Non-Operating Income (net of expenses directly attributable to such income)
5. Additional Information: A Company shall disclose by way of notes, additional information regarding aggregate expenditure and income on the following items:
   (a) employee Benefits expense (showing separately (i) salaries and wages, (ii) contribution to provident & other funds, (iii) share based payments to employees, (iv)staff welfare expenses).
   (b) depreciation and amortisation expense;

(c) any item of income or expenditure which exceeds one per cent of the revenue from operations or Rs 1,00,000, whichever is higher,

(d) interest Income;

(e) interest Expense

(f) dividend income;

(g) net gain or loss on sale of investments;

(h) net gain or loss on foreign currency transaction and translation (other than considered as finance cost);

(i) payments to the auditor as (a) auditor, (b) for taxation matters, (c) for company law matters, (d) for other services, (e) for reimbursement of expenses;

(j) in case of companies covered under section 135, amount of expenditure incurred on corporate social responsibility activities; and

(k) details of items of exceptional nature;

Points to be kept in mind while preparing final accounts

- Requirements of Schedule III to the Companies Act;
- Accounting Standards notified by Ministry of Corporate Affairs (MCA) (AS 1 to AS 29);
- Statements and Guidance Notes issued by the Institute of Chartered Accountants of India (ICAI); which are necessary for understanding the accounting treatment/ valuation/ disclosure suggested by the ICAI.

Class Example 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.

Solution

Schedule III does not require a company to disclose the source from which bonus shares have been issued. Therefore, non-disclosure of source from which bonus shares have been issued does not violate the Schedule III to the Companies Act.

Class Example 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.*

Solution

Schedule III to the companies Act does not require that the amounts of WIP at the beginning and at the end of the accounting period to be disclosed in the statement of profit and loss. Only changes in inventories of WIP need to be disclosed in the statement of profit and loss. Non-disclosure of such change in the statement of profit and loss by the company may not amount to violation of Schedule III if the differences between opening and closing WIP are not material.

Class Example 3

Futura Ltd. had the following items under the head "Reserves and Surplus" in the Balance Sheet as on 31st March, 20X1:

	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.

Solution

Part I of Schedule III to the Companies Act, 2013 provides that debit balance of Statement of Profit and Loss (after all allocations and appropriations) should be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserves and Surplus', after adjusting negative balance of surplus, should be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative. In this case, the debit balance of profit and loss i.e. Rs 250 lakhs exceeds the total of all the reserves i.e. Rs 230 lakhs. Therefore, balance of 'Reserves and Surplus' after adjusting debit balance of profit and loss is negative by Rs 20 lakhs, which should be disclosed on the face of the balance sheet. Thus the treatment done by the company is incorrect.

Class Example 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.

Solution

As per Schedule III, a liability should be classified as current when it satisfies any of the following criteria:

(i) it is expected to be settled in the company's normal operating cycle;

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

(iii) it is due to be settled within twelve months after the reporting date; or

(iv) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date.

In the given case, instalments due on 30.09.20X1 and 31.03.20X2 will be shown under the head 'other current liabilities' as per criteria (c).

Therefore, in the balance sheet as on 31.3.20X1, Rs 8,00,000 (Rs 1,00,000 x 8 instalments) will be shown under the heading 'Long term Borrowings' and Rs 2,00,000 (Rs 1,00,000 x 2 instalments) will be shown under the heading 'Other Current Liabilities' as current maturities of loan from bank.

Note: Students may note that the questions based on preparation of Statement of Profit and Loss and Balance Sheet and explanatory notes as per Schedule III have been given in this Unit. However, questions requiring preparation of cash Flow statements have been separately given in the next unit of this chapter.

MANAGERIAL REMUNERATION

Managerial remuneration is calculated as a percentage of profit. Managerial remuneration payable by a company is governed by various sections of the Companies Act, 2013 and also Schedule V under the Companies Act, 2013.

As per Section 197 of the Companies Act, 2013, total managerial remuneration payable by a public company, to its directors, including managing director and whole-time director, and its manager in respect of any financial year ***should not exceed 11%*** of the net profits of that company for that financial year computed in the manner laid down in section 198 except that the remuneration of the directors should not be deducted from the gross profits.

The company in general meeting may, with the approval of the Central Government, authorise the payment of remuneration exceeding 11% of the net profits of the company, subject to the provisions of Schedule V. Provided further that, except with the approval of the company in general meeting,—

(i) the remuneration payable to any one managing director; or whole-time director or manager should not exceed 5% of the net profits of the company and if there are more than one such director, remuneration should not exceed 10% of the net profits to all such directors and manager taken together;

(ii) the remuneration payable to directors who are neither managing directors nor whole-time directors should not exceed,—

(A) 1% of the net profits of the company, if there is a managing or whole-time director or manager;

(B) 3% of the net profits in any other case.

Section 198 lays down how the net profit of the company will be ascertained for the purpose of calculating managerial remuneration.

Schedule V consists of four parts out of it Part II deals with Remuneration payable:

The relevant details given under Part II of Schedule V are as follows:

Section I - Remuneration payable by companies having profits:

Subject to the provisions of section 197, a company having profits in a financial year may pay remuneration to a managerial person or persons not exceeding the limits specified in such section.

Section II - Remuneration payable by companies having no profit or inadequate profit:

Where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, pay remuneration to the managerial person as follows:

	(1)	(2)
	Where the effective capital is	Limit of yearly remuneration payable should not exceed (Rupees)
(i)	Negative or less than 5 crores	60 Lakhs
(ii)	5 crores and above but less than 100 crores	84 Lakhs
(iii)	100 crores and above but less than 250 crores	120 Lakhs
(iv)	250 crores and above	120 lakhs plus 0.01% of the effective capital in excess of Rs 250 crores.

Provided that the remuneration in excess of the above limits may be paid if the resolution passed by the shareholders is a special resolution.

Explanation - It is hereby clarified that for a period less than one year, the limits should be pro-rated.

Explanation I- For the purposes of Section II of this Part, "Effective capital" means the aggregate of:

a. The paid-up share capital (excluding share application money or advances against shares);
b. Amount, if any, for the time being standing to the credit of share premium account;
c. Reserves and surplus (excluding revaluation reserve);
d. Long-term loans and deposits repayable after one year (excluding working capital loans, over drafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements)
e. As reduced by the aggregate of any investments (except in case of investment by an investment company whose principal business is acquisition of shares, stock, debentures or other securities),
f. As reduced by accumulated losses and preliminary expenses not written off.

Class Example 5.

The following is the Draft Profit & Loss A/c of Mudra Ltd., the year ended 31st March, 20X1:

		Rs			Rs
To	Administrative, Selling and		By	Balance b/d	5,72,350
	distribution expenses	8,22,542	"	Balance from	
"	Directors fees	1,34,780		Trading A/c	40,25,365
"	Interest on debentures	31,240	"	Subsidies received	2,73,925
"	Managerial remuneration	2,85,350		from Govt.	
"	Depreciation on fixed assets	5,22,543			
"	Provision for Taxation	12,42,500			
"	General Reserve	4,00,000			
"	Investment Revaluation				
	Reserve	12,500			
"	Balance c/d	14,20,185			
		48,71,640			48,71,640

Depreciation on fixed assets as per Schedule II of the Companies Act, 2013 was Rs 5,75,345. You are required to calculate the maximum limits of the managerial remuneration as per Companies Act, 2013.

Solution:

Calculation of net profit u/s 198 of the Companies Act, 2013

	Rs	Rs
Balance from Trading A/c		40,25,365
Add: Subsidies received from Government		2,73,925
		42,99,290
Less: Administrative, selling & distribution expenses	8,22,542	
Director's fees	1,34,780	

Interest on debentures	31,240	
Depreciation on fixed assets as per Schedule II	5,75,345	(15,63,907)
Profit u/s 198		27,35,383

Maximum Managerial remuneration under Companies Act, 2013= 11% of RS 27,35,383= Rs 3,00,892

Class Example 6.

The following extract of Balance Sheet of X Ltd. was obtained:

Balance Sheet (Extract) as on 31st March, 20X1

Liabilities	*Rs*
Authorised capital:	
20,000, 14% preference shares of Rs 100	*20,00,000*
2,00,000 Equity shares of Rs 100 each	*2,00,00,000*
Issued and subscribed capital:	*2,20,00,000*
15,000, 14% preference shares of Rs 100 each fully paid	*15,00,000*
1,20,000 Equity shares of Rs 100 each, Rs 80 paid-up	*96,00,000*
Share suspense account	*20,00,000*
Reserves and surplus:	
Capital reserves (Rs 1,50,000 is revaluation reserve)	*1,95,000*
Securities premium	*50,000*

Secured loans:	*Rs*
15% Debentures	*65,00,000*
Unsecured loans:	
Public deposits	*3,70,000*
Cash credit loan from SBI (short term)	*4,65,000*
Current Liabilities:	
Trade Payables	*3,45,000*
Assets:	
Investment in shares, debentures, etc.	*75,00,000*
Profit and Loss account (Dr. balance)	*15,25,000*

Share suspense account represents application money received on shares, the allotment of which is not yet made.

You are required to compute effective capital as per the provisions of Schedule V. Would your answer differ if X Ltd. is an investment company?

Solution

Computation of effective capital:

	Where X Ltd. Is a non-investment company Rs	Where X Ltd. is an investment company Rs
Paid-up share capital —		
15,000, 14% Preference shares	15,00,000	15,00,000
1,20,000 Equity shares	96,00,000	96,00,000
Capital reserves (1,95,000 – 1,50,000)	45,000	45,000

Securities premium	50,000	50,000
15% Debentures	65,00,000	65,00,000
Public Deposits	3,70,000	3,70,000
(A)	1,80,65,000	1,80,65,000
Investments	75,00,000	—
Profit and Loss account (Dr. balance)	15,25,000	15,25,000
(B)	90,25,000	15,25,000
Effective capital (A–B)	90,40,000	1,65,40,000

DIVISIBLE PROFIT

One of the important functions of company accounting is to determine the amount of profits which is available for distribution to the shareholders as dividend. This is necessary since the amount of profits disclosed by the Profit & Loss Account, in every case, is not available for distribution.

MEANING OF DIVIDEND

A dividend is a distribution of divisible profit of a company among the members according to the number of shares held by each of them in the capital of the company.

As per Section 2 (35) of the Companies Act, 2013, term "Dividend" includes interim dividend also.

Under Section 123 (1) of the Companies Act, 2013, no dividend should be declared or paid by a company for any financial year except-

(a) Out of the profits of the company for that financial year arrived at after providing for depreciation in accordance with the provisions of section 123(2), or

(b) Out of the profits for any previous financial years arrived at after providing for depreciation in accordance with the provisions of that sub section and remaining undistributed; or

(c) Out of both the above;

(d) Out of the moneys provided by the Central Government or any State Government for the payment of dividend by the Company in pursuance of any guarantee given by that government

Provided that no dividend should be declared or paid by a company from its reserves other than free reserves.

Dividends cannot be declared except out of profits.

Capital cannot be returned to the shareholders by way of dividend.

Dividend can be declared and paid by a company only out of the profits or free reserves (other than moneys provided by Central or State Govt.) as the payment of dividend from any other source will amount to payment of dividend from capital units.

Provision for Depreciation

Section 123(2) provides that depreciation must be to the extent specified in Schedule II to the Companies Act, 2013.Further, when the assets are sold, discarded, demolished or destroyed in any financial year, the excess of the written down value over its sale proceeds as scrap, if any should be written off in the same financial year.

Declaration and Payment of Dividend

For the purpose of second proviso to sub-section (1) of section 123, a company may declare dividend out of the accumulated profits earned by it in previous years and transferred by it to the reserves, in the event of inadequacy or absence of profits in any year, subject to the fulfillment of the following conditions as per Companies (Declaration and Payment of Dividend) Rules, 2014:

(1) The rate of dividend declared should not exceed the average of the rates at which dividend was declared by it in the three years immediately preceding that year: provided that this sub-rule should not apply to a company, which has not declared any dividend in each of the three preceding financial years.

(2) The total amount to be drawn from such accumulated profits should not exceed one-tenth of the sum of its paid-up share capital and free reserves as appearing in the latest audited financial statement.

(3) The amount so drawn should first be utilised to set off the losses incurred in the financial year in which dividend is declared before any dividend in respect of equity shares is declared.

(4) The balance of reserves after such withdrawal should not fall below 15% of its paid up share capital as appearing in the latest audited financial statement.

(5) No company should declare dividend unless carried over previous losses and depreciation not provided in previous year are set off against profit of the company of the current year the loss or depreciation, whichever is less, in previous years is set off against the profit of the company for the year for which dividend is declared or paid.

Transfer to Reserves

I. The Board of Directors are free and can appropriate a part of the profits to the credit of a reserve or reserves as per section 123 (1) of the Companies Act, 2013.

II. Appropriation of a part of profit is sometimes made under law.

(a) For example, under the Banking Regulation Act, a fixed percentage of the profit of a banking company must first be transferred to the General Reserve before any dividend can be distributed.

(b) Transfer of a part of profit to a reserve is also necessary where the company has undertaken, at the time of raising of loan, that before any part of its profit is distributed, a specified percentage of the profit every year should be credited to a reserve for the repayment of the loan and until the time for repayment arrives, the amount should remain invested in a specified manner.

III. Apart from appropriations aforementioned, it may also be necessary to provide for losses and arrears of depreciation and to exclude capital profit, as mentioned earlier, to arrive at the amount of divisible profit.

Dividend on preference shares

(a) Holders of preference shares are entitled to receive a dividend at a fixed rate before any dividend is declared on equity shares.

(b) But such a right can be exercised subject to there being profits and the Directors recommending payment of the dividend.

Dividend on partly paid shares:

- A company may if so authorised by its Article, pay a dividend in proportion to the amount paid on each share (Section 51 of the Companies Act, 2013).

Calls in Advance

Calls paid in advance do not rank for payment of dividend.

Class Example 7.

Due to inadequacy of profits during the year ended 31st March, 20X2, XYZ Ltd. proposes to declare 10% dividend out of general reserves. From the following particulars, ascertain the amount that can be utilised from general reserves, according to the Companies (Declaration of dividend out of Reserves) Rules, 2014:

	Rs
17,500 9% Preference shares of Rs 100 each, fully paid up	17,50,000
8,00,000 Equity shares of Rs 10 each, fully paid up	80,00,000
General Reserves as on 1.4.20X1	25,00,000

Capital Reserves as on 1.4.20X1	*3,00,000*
Revaluation Reserves as on 1.4.20X1	*3,50,000*
Net profit for the year ended 31st March, 20X2	*3,00,000*
Average rate of dividend during the last three years has been 12%.	

Solution

Amount that can be drawn from reserves for 10% dividend		
10% dividend on Rs 80,00,000		8,00,000
Profits available		
Current year profit	3,00,000	
Less: Preference dividend	(1,57,500)	(1,42,500)
Amount which can be utilised from reserves		6,57,500

Conditions as per Companies (Declaration of dividend out of Reserves) Rules, 20X1:

Condition I

Since 10% is lower than the average rate of dividend (12%), 10% dividend can be declared.

Condition II

Maximum amount that can be drawn from the accumulated profits and reserves should not exceed 10% of paid up capital plus free reserves ie. Rs 12,25,000 [10% of (80,00,000+17,50,000+25,00,000)]

Condition III

The balance of reserves after drawl Rs 18,42,500 (Rs 25,00,000 - Rs 6,57,500) should not fall below 15 % of its paid up capital ie. Rs 14,62,500 (15% of Rs 97,50,000]

Since all the three conditions are satisfied, the company can withdraw Rs 6,57,500 from accumulated reserves (as per Declaration and Payment of Dividend Rules, 2014.)

Dividend Distribution Tax

The salient features of DDT are as below:

(i) DDT is in addition to the income-tax chargeable in respect of the total income of a domestic company.

(ii) With effect from 1st Oct, 2014 dividend and income distribution tax is leviable on gross dividend/income and not on the net dividend / income distributed to shareholders and unit holders as per Income- tax Act, 1961.

(iii) DDT should be payable even if no income-tax is payable by the domestic company on its total income.

(iv) DDT is payable to the credit of the Central Government within 14 days of

(a) Declaration of any dividend,

(b) Distribution of any dividend, or

(c) Payment of any dividend.

Whichever is the earliest.

(v) DDT paid should be treated as the final payment of tax on the dividends and no further credit therefore should be claimed by the company or by any person in respect of the tax so paid.

To make clear the understanding of the concept of grossing for calculation of CDT, an example has been given as follows:

Class Example 8.

X Ltd., a domestic company, has distributed on 5th April 20X1, dividend of Rs 230 lakh to its shareholders. Compute the Dividend Distribution tax payable by X Ltd.

Solution

Calculation of corporate dividend tax

Particulars	Rs in lakh
Dividend distributed by X Ltd.	230
Add: Increase for the purpose of grossing up of dividend $[\frac{15}{100-15} \times 230]$	40.59
Gross dividend	270.59
Dividend distribution tax @ 15% [15% of Rs 270.59 lakh]	40.59
Add: Surcharge@12%	4.88
	45.47
Add: Education cess@2% and SHEC@1%	1.36
Dividend Distribution tax	46.83

Accounting for DDT

As per AS 4 (Revised), Final dividend declared after the balance sheet date is recognised in the financial year in which it has been approved by the shareholder, i.e., there is no provision for dividend on the balance sheet date (to be disclosed by way of note only).In view of this, DDT on dividend, being directly linked to the amount of the dividend concerned, should also be reflected in the accounts of the same financial year even though the actual tax liability in respect thereof may arise in a different year.

- DDT liability should be recognised in the accounts of the same financial year in which the dividend concerned is recognised.
- DDT liability should be disclosed separately in the 'Notes to Accounts' of 'Reserves and Surplus', as follows:

Dividend	xxxxx	
Dividend Distribution tax thereon	xxxxx	xxxxx

Class Example 9.

On 31st March, 20X1 X Ltd. declared dividend amounting to Rs 425 lacs for the year 20XX-20X1. The Dividend Distribution tax liability (15% of corporate dividend tax including surcharge @ 12%, Education Cess @ 2% and SHEC @ 1% i.e. 17.304%) arises as per Income-tax Act, 1961. In this case, calculate the grossing-up of dividend and separately disclose the charge for DDT in the 'Notes to Accounts' of 'Reserves and Surplus'.

Solution

Calculation of grossing-up of dividend:

Particulars	Rs in lacs
Dividend distributed by X Co.	425
Add: Increase for the purpose of grossing up of dividend $[\frac{15}{100-15} \times 425]$	75
Gross dividend	500
Dividend distribution tax @ 17.304%	86.52

(An Extract)

- 'Notes to Accounts' of 'Reserves and Surplus'
- for the year ended 31st March, 20X1

	Rs (lacs)	Rs (lacs)
Dividend	425.00	
Dividend Distribution tax	86.52	511.52

The Dividend Distribution tax should be disclosed separately under, the head 'Other Current Liabilities'. The relevant extracts of the Balance Sheet of X Ltd. can be shown as follows:

Balance Sheet as on 31st March, 20X1

'Other Current Liabilities'	Rs (lacs)
Dividend declared	425.00
Declared Distribution tax	86.52

CLASS WORK QUESTION

Question 1 ***(ICAI MODULE)***

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.

(vi) Money received against share warrant.

Question 2 **(ICAI MODULE)**

The following extract of Balance Sheet of Star Ltd. (non- investment) company was obtained:

Balance Sheet (Extract) as on 31st March, 20X1

Liabilities	Rs
Authorised capital:	
60,000, 14% preference shares of Rs 100	60,00,000
6,00,000 Equity shares of Rs 100 each	6,00,00,000
6,60,00,000	
Issued and subscribed capital:	
45,000, 14% preference shares of Rs 100 each fully paid	45,00,000
3,60,000 Equity shares of Rs 100 each, Rs 80 paid-up	2,88,00,000
Share suspense account	60,00,000
Reserves and surplus:	
Capital reserves (Rs 4,50,000 is revaluation reserve)	5,85,000
Securities premium	1,50,000
Secured loans:	
15% Debentures	1,95,00,000
Unsecured loans:	
Public deposits	11,10,000
Cash credit loan from SBI (short term)	3,95,000
Current Liabilities:	
Trade Payables	10,35,000
Assets:	
Investment in shares, debentures, etc.	2,25,00,000
Profit and Loss account (Dr. balance)	45,75,000

Share suspense account represents application money received on shares, the allotment of which is not yet made.

You are required to compute effective capital as per the provisions of Schedule V. Would your answer differ if Star Ltd. is an investment company?

Question 3 **(ICAI MODULE)**

You are required to prepare Balance sheet and statement of Profit and Loss from the following trial balance of Haria Chemicals Ltd. for the year ended 31st March, 20X1.

Haria Chemicals Ltd.

Trial Balance as at 31st March, 20X1

Particulars	Rs	Particulars	Rs
Inventory	6,80,000	Equity Shares	
Furniture	2,00,000	Capital (Shares of Rs 10 each)	25,00,000

Discount	40,000	11% Debentures	5,00,000
Loan to Directors	80,000	Bank loans	6,45,000
Advertisement	20,000	Trade payables	2,81,000
Bad debts	35,000	Sales	42,68,000
Commission	1,20,000	Rent received	46,000
Purchases	23,19,000	Transfer fees	10,000
Plant and Machinery	8,60,000	Profit & Loss account	1,39,000
Rentals	25,000	Depreciation provision:	
Current account	45,000	Machinery	1,46,000
Cash	8,000		
Interest on bank loans	1,16,000		
Preliminary expenses	10,000		
Fixtures	3,00,000		
Wages	9,00,000		
Consumables	84,000		
Freehold land	15,46,000		
Tools & Equipments	2,45,000		
Goodwill	2,65,000		
Trade receivables	4,40,000		
Dealer aids	21,000		
Transit insurance	30,000		
Trade expenses	37,000		
Distribution freight	54,000		
Debenture interest	55,000		
	85,35,000		85,35,000

Additional information: Closing Inventory on 31-3-20X1: Rs 8,23,000.

Question 4 ***(ICAI MODULE)***

The following is the Trial Balance of Omega Limited as on 31.3.20X2:

(Figures in Rs '000)

	Debit		Credit
Land at cost	220	Equity Capital (Shares of Rs 10 each)	300
Plant & Machinery at cost	770	10% Debentures	200
Trade Receivables	96	General Reserve	130
Inventories (31.3.X2)	86	Profit & Loss A/c	72
Bank	20	Securities Premium	40
Adjusted Purchases	320	Sales	700
Factory Expenses	60	Trade Payables	52
Administration Expenses	30	Provision for Depreciation	172
Selling Expenses	30	Suspense Account	4
Debenture Interest	20		
Interim Dividend Paid	18		
	1670		1670

Additional Information:

(i) The authorised share capital of the company is 40,000 shares of Rs 10 each.

(ii) *The company on the advice of independent valuer wish to revalue the land at Rs 3,60,000.*

(iii) *Declared final dividend @ 10%.*

(iv) *Suspense account of Rs 4,000 represents cash received for the sale of some of the machinery on 1.4.20X1. The cost of the machinery was Rs 10,000 and the accumulated depreciation thereon being Rs 8,000.*

(v) *Depreciation is to be provided on plant and machinery at 10% on cost.*

You are required to prepare Omega Limited's Balance Sheet as on 31.3.20X2 and Statement of Profit and Loss with notes to accounts for the year ended 31.3.20X2 as per Schedule III. Ignore previous years' figures & taxation.

Question 5 ***(ICAI MODULE)***

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 –

		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.

Question 6 ***(ICAI MODULE)***

Ring Ltd. was registered with a nominal capital of Rs 10,00,000 divided into shares of Rs 100 each. The following Trial Balance is extracted from the books on 31st March, 20X2:

Particulars	Rs	Particulars	Rs
Buildings	5,80,000	Sales	10,40,000
Machinery	2,00,000	Outstanding Expenses	4,000
Closing Stock	1,80,000	Provision for Doubtful	6,000
Loose Tools	46,000	Debts (1-4-20X1)	
Purchases (Adjusted)	4,20,000	Equity Share Capital	4,00,000
Salaries	1,20,000	General Reserve	80,000
Directors' Fees	20,000	Profit and Loss A/c	50,000
Rent	52,000	(1-4-20X1)	
Depreciation	40,000	Creditors	1,84,000
Bad Debts	12,000	Provision for depreciation:	
Investment	2,40,000	On Building 1,00,000	
Interest accrued on investment	4,000	On Machinery 1,10,000	2,10,000
Debenture Interest	56,000	14% Debentures	4,00,000
Advance Tax	1,20,000	Interest on Debentures	28,000
Sundry expenses	36,000	accrued but not due	
Debtors	2,50,000	Interest on Investments	24,000
Bank	60,000	Unclaimed dividend	10,000
	24,36,000		**24,36,000**

You are required to prepare statement of Profit and Loss for the year ending 31st March, 20X2 and Balance sheet as at that date after taking into consideration the following information:

(a) Closing stock is more than opening stock by Rs 1,60,000;

(b) Provide to doubtful debts @ 4% on Debtors

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

(d) Depreciation expense included depreciation of Rs 16,000 on Building and that of Rs 24,000 on Machinery.

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

(f) *Bills Discounted but not yet matured Rs 20,000.*

Question 7 ***(ICAI MODULE)***

You are required to prepare a Statement of Profit and Loss and Balance Sheet from the following Trial Balance extracted from the books of the International Hotels Ltd., on 31st March, 20X2:

	Dr.	Cr.
	Rs	Rs
Authorised Capital-divided into 5,000 6% Preference Shares of Rs 100 each and 10,000 equity Shares of Rs 100 each		15,00,000
Subscribed Capital -		
5,000 6% Preference Shares of Rs 100 each		5,00,000
Equity Capital		8,05,000
Purchases - Wines, Cigarettes, Cigars, etc.	45,800	
- Foodstuffs	36,200	
Wages and Salaries	28,300	
Rent, Rates and Taxes	8,900	
Laundry		750
Sales - Wines, Cigarettes, Cigars, etc.		68,400
- Food		57,600
Coal and Firewood	3,290	
Carriage and Cooliage	810	
Sundry Expenses	5,840	
Advertising	8,360	
Repairs	4,250	
Rent of Rooms		48,000
Billiard		5,700
Miscellaneous Receipts		2,800
Discount received		3,300
Transfer fees		700
Freehold Land and Building	8,50,000	
Furniture and Fittings	86,300	
Inventory on hand, 1st April, 20X1		
Wines, Cigarettes. Cigars, etc.	12,800	
Foodstuffs	5,260	
Cash in hand	2,200	
Cash with Bankers	76,380	
Preliminary and formation expenses	8,000	
2,000 Debentures of Rs 100 each (6%)		2,00,000
Profit and Loss Account		41,500
Trade payables		42,000
Trade receivables	19,260	
Investments	2,72,300	
Goodwill at cost	5,00,000	
General Reserve		2,00,000
	19,75,000	19,75,000
Wages and Salaries Outstanding	1,280	
Inventory on 31st March, 20X2		

Wines, Cigarettes and Cigars, etc.	22,500	
Foodstuffs	16,400	

Depreciation: Furniture and Fittings @ 5% p.a.: Land and Building @ 2% p.a.

The Equity capital on 1st April, 20X1 stood at Rs 7,20,000, 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 20X1. 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. The Directors declare a dividend of 8% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

Question 8 ***(ICAI MODULE)***

From the following particulars furnished by Alpha Ltd., prepare the Balance Sheet as on 31st March 20X1 as required by Part I, Schedule III of the Companies Act, 2013.

Particulars		Debit Rs	Credit Rs
Equity Share Capital (Face value of Rs 100 each)			50,00,000
Call in Arrears		5,000	
Land & Building		27,50,000	
Plant & Machinery		26,25,000	
Furniture		2,50,000	
General Reserve			10,50,000
Loan from State Financial Corporation			7,50,000
Inventory: Raw Materials Finished Goods	 2,50,000 10,00,000	 12,50,000	
Provision for Taxation			6,40,000
Trade receivables		10,00,000	
Short term Advances		2,13,500	
Profit & Loss Account			4,33,500
Cash in Hand		1,50,000	
Cash at Bank		12,35,000	
Unsecured Loan			6,05,000
Trade payables (for Goods and Expenses)			8,00,000
Loans & advances from related parties			2,00,000

The following additional information is also provided:

(i) *10,000 Equity shares were issued for consideration other than cash.*

(ii) *Trade receivables of Rs 2,60,000 are due for more than 6 months.*

(iii) *The cost of the Assets were:*

Building Rs 30,00,000, Plant & Machinery Rs 35,00,000 and Furniture Rs 3,12,500

(iv) *The balance of Rs 7,50,000 in the Loan Account with State Finance Corporation is inclusive of Rs 37,500 for Interest Accrued but not Due. The loan is secured by hypothecation of Plant & Machinery.*

(v) *Balance at Bank includes Rs 10,000 with Omega Bank Ltd., which is not a Scheduled Bank.*

(vi) *Transfer Rs 20,000 to general reserve is proposed by Board of directors.*

(vii) *Board of directors has declared dividend of 5% on the paid up capital.*

Student Notes:-