2 PREPARATION OF FINANCIAL STATEMENTS

INDEX

Quote: -

"Strive not to be a Success,
but rather to be a Value".

1. 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.

1. **Rounding off Rule:** 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
(Ii) 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.

2. **Previous Year Figures:** 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.

FORMAT OF BALANCE SHEET & STATEMENT OF PROFIT AND LOSS

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	Other Non-Current Liabilities			

d	Long-Term Provisions
4.	**Current liabilities**
a	Short Term Borrowings
b	Trade Payables: (Creditors + B/P) (A) Total outstanding dues of micro enterprises and small enterprises; and (B) Total outstanding dues of creditors other than micro enterprises and small enterprises.
c	Other Current Liabilities
d	Short Term Provisions
	Total
(2)	**ASSETS**
1	**Non- Current Assets**
a	i. Property Plant and 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 & 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

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 A B	**EXPENSES** Cost of materials consumed Purchases of Stock-in-Trade			

C D E F G	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 and tax (I-IV)			
VI	Exceptional Items			
VII	Profit/ (loss) before Extra-Ordinary Items and Tax (V-VI)			
VIII	Extra Ordinary Items	AS - 5		
IX	Profit Before Tax (VII – VIII)			
X	Tax expense: (1) Current tax (2) Deferred tax	AS – 22		
XI	Profit (Loss) for the period from continuing operations (VII - VIII)			
XII	Profit/(loss) from discontinued operations	AS 24		
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		

IMPORTANT ITEMS OF BALANCE SHEET

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.

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; (e.g., Debtors, Inventory)

(b) It holds the asset primarily for the purpose of trading; (e.g., 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.

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. (e.g., Loan taken from banks)

Note:

- 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.
- 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.

RESERVES & SURPLUS

Reserves & Surplus shall be classified as-

- Capital Reserve;
- Capital Redemption Reserve;
- Security Premium;
- Debenture Redemption Reserve;
- Revaluation Reserve;
- Share Options Outstanding Account; and
- Other Reserves - (specify the nature and purpose of each reserve and the amount in respect thereof);

- 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.

Note:

- 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.
- A reserve specifically represented by earmarked investments shall be termed as a 'Fund'.

NON-CURRENT LIABILITIES

Long-Term Borrowings	Other Long-Term Liabilities	Provisions
Classified into: a) Bonds/Debentures b) Term Loans from: Banks Other Parties c) Deferred payment liabilities d) Deposits e) Loans and Advances from related parties f) Long term maturities of Finance Leases Obligation g) Other Loans and Advances (Specify Nature) h) Further Classified as Secured and Unsecured along with nature of security. i) Any guarantees by directors or others terms of Repayments j) Period and amount of default as on BS date	Classified into- • Trade Payables • Others (Non-Trade Payables)	Classified into: • Provision for Employee benefits (e.g., Gratuity) • Others

CURRENT LIABILITIES

Borrowings	Other CL	Provisions	Trade Payables
Classified into: (a) Loans Repayable on demand • from Banks • from Other Parties	Classified into- **(i)** Current maturities of finance lease obligations; **(ii)** Interest accrued but not due; **(iii)** Interest accrued & due;	Classified into: • Provision for Employee benefits (EPF, Salary etc.) • Others (Income Tax, GST etc.)	Trade Payables in respect of Micro, Small & Medium Enterprises shall be further subdivided into: Total Principal amount payable

(a) Loans and Advances from Related Parties (b) Deposits (c) Other Loans and Advances (d) Current maturities of long-term debt; 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	**(iv)** Income Received in Advance; **(v)** Unpaid dividends; **(vi)** Application money received for allotment of securities to the extent refundable & interest accrued thereon; **(vii)** Unpaid matured deposits & interest accrued thereon; **(viii)** Unpaid matured debentures & interest accrued thereon; & **(ix)** Others		Total Interest amount Payable Ageing Schedule shall also be given as under:

IMPORTANT NON-CURRENT ASSETS

Investments	Long Term 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 • Partnership Firms	Classify loans into- • Capital Advances • Security Deposits • Loans to related Parties • Others Sub classified into – • Secured - Good • Unsecured - Good • Doubtful Provision for bad & doubtful debts shall be	Classified into- • Long Term Trade Receivables • Security Deposits • Others Long Term Trade Receivables sub classified into – • Secured - Good • Unsecured – Good • Doubtful

• Others Investments carried at other than at Cost should be separately stated. Disclose quoted investments & their market values separately from unquoted investments along with aggregate Provision For diminution in Value of Investment	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. Disclose Ageing Schedule of Trade Receivables

TRADE RECEIVABLES AGEING SCHEDULE

(Amount in Rs.)

Particulars	Outstanding for following periods from due date of payment#					
	Less than 6 months	6 months - 1 year	1-2 years	2-3 years	More than 3 years	Total
(i) Undisputed Trade receivables – considered good						
(ii) Undisputed Trade Receivables – considered doubtful						
(iii) Disputed Trade Receivables considered good						
(iv) Disputed Trade Receivables considered doubtful						

IMPORTANT ITEMS 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/GST

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) Adjustment to the carrying amount of Investments.
   (i) net gain or loss on foreign currency transaction and translation (other than considered as finance cost);
   (j) 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;
   (k) in case of companies covered under section 135, amount of expenditure incurred on corporate social responsibility activities; and
   (l) details of items of exceptional nature;

IMPORTANT EXAMPLES ON SCHEDULE III items

EXAMPLE 1:

Vsmart Pvt. Ltd. has taken a loan few years back. In CY, Loan life is 4 years. There is condition under Loan agreement that V'Smart has to maintain a debt equity ratio 2:1. If the condition is not followed then the loan will be repayable on demand. In CY before 31st March, there is breach of condition by V'Smart i.e. debt equity is not maintained. What should be the classification of this loan as on 31/03?

Case 1: V'Smart has to repay on demand because of Breach therefore it is to be classified as **current** liability.

Case 2: Breach of contract is made as 01/03 & Loan becomes repayable as demand But on 25/03 V'Smart rectified this breach & Bank agreed not to demand the repayment.

Answer: Non-current

Case 3: On 01/03 there is a breach of contract hence Loan becomes repayable on demand. On 25th March, V'Smart requested bank to give grace period & Bank provided a grace period of:

Option 1: 6 months

Option 2: 15 months

(Answer: Option 1 Current and Option 2 Non-Current)

EXAMPLE 2:

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.

EXAMPLE 3:

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.

EXAMPLE 4:

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

	Amount Rs in lakh
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.

EXAMPLE 5:

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.

EXAMPLE 6:

Prince Ltd. presents its provisions for contingencies under "Reserves and Surplus" in Notes to Accounts in its financial statements. Whether this presentation is correct?

SOLUTION

The ICAI's Glossary of Terms Used in Financial Statements defines the term 'Reserve' as "the portion of earnings, receipts or other surplus of an enterprise (whether capital or revenue) appropriated by the management for a general or a specific purpose other than a provision for depreciation or diminution in the value of assets or for a known liability." 'Reserves' should be distinguished from 'provisions'. For this purpose, reference may be made to the definition of the expression `provision' in AS-29 Provisions, Contingent Liabilities and Contingent Assets.

As per AS-29, a `provision' is "a liability which can be measured only by using a substantial degree of estimation". A 'liability' is "a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits." Present obligation' – "an obligation is a present obligation if, based on the evidence available, its existence at the Balance Sheet date is considered probable, i.e., more likely than not."

EXAMPLE 7:

Anek Ltd. is a company that is required to present its financial statements as per the Division I of Schedule III. The company has trade receivables at the balance sheet date. What are the disclosures that are applicable with respect to trade receivables in the financial statements?

SOLUTION

Under Schedule III, trade receivables are required to be classified into long-term (non-current) trade receivables and short-term (current) trade receivables. Trade Receivables, shall be sub-classified as:

(i) (a) Secured, considered good;
  (b) Unsecured considered good;
  (c) Doubtful

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

(iii) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

For trade receivables outstanding, following ageing schedule shall be given:

Particulars	Outstanding for following periods from due date of payment					Total
	Less than 6 months	6 months- 1 year	1-2 years	2-3 years	More than 3 years	
(i) Undisputed Trade Receivables – considered good						
(ii) Undisputed Trade Receivables – considered doubtful						

(iii) Disputed Trade Receivables – considered good						
(iv) Disputed Trade Receivables – considered doubtful						

#similar information shall be given where no due date of payment is specified in that case disclosure shall be from the date of the transaction.

2. DIVIDEND DECLEARED AND PAID BY COMPANY

1) Source of Dividend (Which Profit can be used for distribution of Dividend):

1st Priority	• Out of Current Year Profits. • Without any limits (any amount of dividend can be distributed) • No conditions are required to be fulfilled.
2nd Priority	• Out of undistributed profits of previous year, if current year profit is not adequate • Also, some conditions are required to be fulfilled to distribute the dividend out of the previous year's profits. **Note:** Undistributed profits are also known as Accumulated Profits or Free Reserves.
Other Important Points	• Both Current year and Previous Year profits can be utilized if current year profits are insufficient. • Dividends can also be distributed out of money provided by the government when guaranteed. • Profits for the purpose of Dividend shall not include Notional Gain and Revaluation Reserves etc.

2) Conditions required to fulfilled to distribute Dividends out of PY Profits

Condition 1:	Dividend Rate shall not exceed the average Dividend Rates of Previous 3 Years. **Example:** Suppose previous 3 years dividend rates are 15%, 10% and 12% then CY Dividend Rate shall not exceed 12.33%
Condition 2:	Maximum withdrawal of profits out of Accumulated profits for dividend shall not exceed 10% of Total Paid up share capital (ESC + PSC) Plus Free Reserves as per Last Audited BS. Maximum withdrawal out of PY Profits = (Total ESC + PSC + FR) x 10%
Condition 3:	The minimum Balance remaining in Accumulated Profits/Free Reserves till PY shall be at least 15% of Total Paid up share capital (ESC + PSC). Minimum Balance means after withdrawal of Profits.

Other Points	• All three conditions must be satisfied to distribute dividends out of PY profits. • Free Reserves includes general reserves and balance of Profit and Loss A/c • Free Reserves doesn't include CRR, DRR, Security Premium A/c, Revaluation Reserves and Capital Reserves.

EXAMPLE 8:

Due to the 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.)

EXAMPLE 9:

Consider the following information:

1) 1,00,000 No. of Equity shares of 10/- each (8/-paid up)
2) 60,000 No. of Equity share of 20/- each Fully paid up
3) Non-Cumulative 10% Preference Shares of Rs. 3,00,000/-
4) Cumulative Preference Shares of 9% of Rs. 4,50,000/-
5) CY is 24-25, NP before any Dividend for 24-25 is Rs. 1,60,000/-
6) General Reserve balance as on 31/3/24 = 5,00,000/-
7) Bal. of Profit and Loss A/c on 31/3/24 = 10,00,000/-
8) Company proposed Equity Dividend of 6% for 10/- Face Value of Shares & 7.5% for 20/- Face Value of share
9) Avg. of Last 3 years Dividend Rates are 10%
10) Dividend on both Preference Shares are not Declared.

Determine whether the Proposed Dividend rate is Correct or not?

Solution: -

Step 1: Check the available Current Year Profits for Equity Share Holders:

NP before Dividend	1,20,000
(-) 9% Dividend on Cumulative Pref. Shares (mandatory)	40,500
(-) 10% Dividend on Non-Cumulative (Not Declared)	Nil
Profit available for ESH	**79,500**

Step 2: Calculate Proposed Equity Dividend for Current Year: (On paid up capital)

6% of 8,00,000	48,000
7.5% of 12,00,000	90,000
Total profit required	**1,38,000**

The profit required (step 2) to distribute proposed dividend is more than actual profit available (step 1). Therefore, Entity must utilize past year profit to the extent of 58,500/- (1,38,000 - 79,500) Subject to fulfillment of following Conditions:

Step 3: Check all three Conditions:

Condition 1: Proposed Dividend Rate should not exceed average of Last 3 years Dividend Rates. This Condition is fulfilled.

Condition 2: Maximum Withdrawal out of PY profits shall not exceed 10% of Total Paid up Share Capital + Free Reserves

1,00,000 Equity Shares of 8/- Each	8,00,000
(+) 60,000 Equity Shares of 20/- Each	12,00,000
(+) Non-Cumulative PSC	3,00,000
(+) Cumulative PSC	4,50,000
Gen. Reserve Balance	5,00,000
Bal. of P&l a/c (till PY)	1,00,000
	33,50,000

Maximum Withdrawal @10%	3,35,000

Actual withdrawal Required = 58,500. Hence Condition 2 is fulfilled.

Condition 3: Balance Remaining in PY Profits after Withdrawal shall be at least 15% of Paid up Share Capital.

Minimum Balance Required (27,50,000 x 15%)	4,12,500
Actual Balance after Withdrawal of 58,500/- (6,00,000 – 58,500)	5,41,500
Condition 3 is Fulfilled	

Final Conclusion: Dividend Rates proposed by entity are correct and PY profits can be utilized.

3. POINTS TO BE KEPT IN MIND WHILE PREPARING FINAL ACCOUNTS

1) **Adjusted Purchases means COGS**

Whenever adjusted purchases is given in Trail Balance it means this amount is including the effect of Opening and Closing Stock

So Under P&L, if we show Adjusted Purchase then changes in Inventory not to be shown.

2) However, if this statement is also given: -

Closing stock is more than Opening by X amount

That means there is a hint in Question to show purchases separately & Changes in Inventory Separately

3) **How to Account for Bad-debts and Provision for doubtful debts?**

- Bad-debts means amount from debtors not recovered and finally lost.
- Hence, Bad-debts is a loss. Therefore transfer to Statement of Profit or Loss.

Case 1 - If Bad-debts are shown in Trial Balance:

Trial Balance (Extract)

Particulars	Debit	Credit
Bad-debts	5,000	-
Trade Receivables	1,50,000	-

It means Bad- debts entry of Rs. 5,000 is already passed as under:-

Bad-debts a/c Dr	5,000	
To Trade Receivables		5,000

It means Trade Receivables appearing in trial balance is already after deduction of 5,000. Now, no need to deduct Rs. 5,000 again.

Case 2 - If trial balance shows this –

Trial Balance (Extract)

Particulars	Debit	Credit
Debtors (Trade Receivables)	2,00,000	-

Additional information :- Bad-debts of 10,000

Now since Bad-debts is not shown inside the Trial Balance it means no entry is yet passed. Debtors shown in Trial Balance are before deducting Bad-debts.

Balance Sheet (Extracts)

Particulars	Amount
Trade Receivables (2,00,000 – 10,000)	1,90,000

Statement of Profit and Loss (Extract)

Particulars	Amount
Other Expense: Bad-debts	10,000

Case 3 - If Trial Balance shows like this:-

Trial Balance (Extract)

Particulars	Debit	Credit
Debtors	2,00,000	-
Bad-debts	10,000	-
Provision for Doubtful Debts	-	25,000

Additional information:-

Provision on doubtful debts should be 15 %

It means that provision @ 15 % on debtor is = 2,00,000 x 15% is 30,000.

In Trial Balance, Provision of Rs. 25,000 is already shown.

Hence, Rs. 5,000 provision entry is yet to be passed.

Profit & Loss a/c Dr	5,000	
To Provision for DD		5,000

Final impact on Balance sheet and Statement of Profit or Loss:

Balance Sheet (Extracts)

Particulars	Amount
Trade Receivables	2,00,000
(-) Provision for DD	(30,000)
	1,70,000

Statement of Profit and Loss (Extract)

Particulars	Amount
Other Expense:	
a) Bad-debts	10,000
b) Provision for DD	5,000

3) **Loose Tools & Stores**
Expected life is more than 12 Months it should be treated as PPE
Expected life is less than 12 Months it should be treated as Inventory
If in Question Depreciation on Loose Tools is not given then we can assume it as Inventory.

4) **GP% means Gross Profit Earned on Sales.**
- GP % is always applied on Sales Figures
- But if it is given that GP margin is on cost then some Adjustments are required to apply on it.
  e.g.: - GP is 20% on Cost
  = 1/5 on Cost
  = 1/6 on Sales

5) Preliminary Expenses are always transfer to Other Expenses (P&L), if nothing is specified in Question.

6) Consumables are always treated as Other Expense (P&L)

7) Shares option outstanding means ESOPs Outstanding, they are part of Reserves & Surplus until actually issued as Share Capital
When issued as Capital, then they will be reduced from Reserves & Surplus and added to Share Capital

8) Dividend % if given in Question then it will be Calculated on Paid-up Share Capital always.

9) Payment of Dividend is not an expense. Therefore, it should be shown under Reserves & Surplus as deduction from Net Profit.

10) Whenever Question ask to Declare Equity Dividend then before declaring Equity Dividend. Preference Dividend should be Declared if Preference Share Capital is given in Question.

11) Preference Dividend shall always be paid in priority over equity Dividend out of Current Year Profits & Past Profits.

12) If in Question Preference Share Capital is Given then it is understood that we need to pay Preference Dividend in Priority

13) "Dividend" means Equity Dividend always Unless otherwise mentioned

14) Equity Dividend = Rate (%) x Paid-Up Equity Share Capital

Preference Dividend = Rate (%) x Paid-Up Preference Share Capital

15)Journal Entry for Dividend Declaration: -

Dividend is Declared out of Profits Always:

Profit & Loss A/c	Dr. (1st Priority)
General Reserve A/c	Dr. (2nd Priority)
To Dividend Payable A/c	

16) Equity Dividend Declaration (Annual Dividend or Final Dividend)

Situation 1

Dividend is declared after Balance Sheet Date

No Entry is required as on Balance Sheet Date

Show only Contingent Liabilities in Notes to A/c

Situation 2

Dividend is declared on Balance Sheet Date

Dividend is Shown on Balance sheet Date by passing Journal Entry.

Profit & Loss A/c	Dr.
To Dividend Payable A/c	

* Always apply Situation 1 only if nothing is specified in the Question about When it was Declared

17) Interim Dividend: - Dividend for less than 12 months period Declared & Paid in Same Current year.

Situation 1

Interim dividend is shown under Trail Balance on Debit side i.e. It is already Paid and entry also passed already, then deduct in Reserves & Surplus from Profit & Loss A/c or General Reserve.

Situation 2

Interim Dividend is not shown Under Trail balance but it is asked in Question to pay Interim Dividend in adjustments

P&L A/c	Dr.
To Interim Dividend Payable	

18) Treatment of Preference Dividend

PREFERNCE SHARE CAPITAL	
Cumulative PSC	**Non-Cumulative PSC**
Pref. Dividend Shall be recorded if % is known irrespective of whether it is declared or not.	If Questions says it is declared, then treat it same as Cumulative. (i.e. to be recorded)
R&S: P&L Balance - XXX (-) Pref. Dividend - XXX	If question doesn't mention anything, Ignore Any Treatment

Other Current Liability: Pref. Dividend Payable	

Note:
- In absence of any information given in question, always treat PSC as Cumulative. (ICAI Follows the Same).
- Even if company is loss making, then also cumulative preference dividend shall be recorded and to be paid in next year if there is sufficient profit in next year.

19) When Question ask to Revalue any Asset (PPE)

(a) Upward Revaluation:

Asset A/c Dr.
To Revaluation Reserve A/c

(b) Downward Revaluation:

Profit & Loss A/c Dr.
To Asset A/c

20) Fixed Deposit having original maturity of up to 3 months shall become part of Cash and Cash Equivalents. Fixed Deposits for more than 3 months but up to 12 months shall be shown as Current Investments and shall not become part of Cash and Cash Equivalents.

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.

IMPORTANT CONCEPT BUILDER EXAMPLES:

Example 10:

Trial Balance (Extract)

Particulars	Dr.	Cr.
Machines (Gross)	7,50,000	-
Provision For Depreciation	-	2,20,000
Suspense	-	15,000

Note:
1) Depreciation Rate is 15% on WDV
2) Suspense represents cash received on Sale of one machine costing Rs.45,000 on which Accumulated Depreciation till date of sale was 32,000. Date of sale is Beginning of CY

Calculate: **a)** Depreciation for CY
b) Show B/s P&L Presentation after rectification

Solution:

Rectified Journal Entry		
Suspense a/c	Dr.	15,000
Prove For Dep a/c	Dr.	32,000

To Machine a/c	45,000
To Profit on sale a/c (P&L)	2,000

Depreciation for Current Year

	Gross	Provision	Net
Machine as on Beg. of year (-) Sale	7,50,000 (45,000)	2,20,000 (32,000)	5,30,000 (13000)
Balance Before Dep. of CY	7,05,000	1,88,000	5,17,000
CY Depreciation @ 15%		77,550	(77,550)
			4,39,450

Statement of Profit or Loss (extract)	
Other Incomes: Gain on Sale of PPE	2,000
Expenses: Depreciation & Amount.	77,550

Balance Sheet (extract)

	Note	
Non-Current Assets PPE	1	4,39,450

Note 1:

Particulars	Gross	Provision	Net
Opening Bal	7,50,000	2,20,000	5,30,000
(-) Sale of Machine	(45,000)	(32,000)	(13,000)
(+) Depreciation	-	77,550	(77,550)
Closing Balances	**7,05,000**	**2,65,550**	**4,39,450**

Example 11:

Depreciation = 12% on WDV	
On 1st April	**On 1st October**
Gross Value of All Assets = 22lacs Provision for Depreciation = 8.5lacs till last year	Machine Sold Gross Value = 4,50,000 ACC. Dep. Till Last Year = 1,60,000 Sale at 3,00,000

Show the necessary accounting treatment.

Solution:

Sold Machine		Other Machine	
Particulars	**Amount**	**Particulars**	**Amount**
Gross	4,50,000	Gross	17,50,000
(-) Provision till last year	1,60,000	(-) Prove for Dep	69,0000
	2,90,000	WDV Opening	10,60,000

Dept 12%(6m)	17,400	Dept @ 12%	1,27,200

Total Depreciation = 1,44,600

Notes To PPE:

Particulars	Gross Value	Prove for Dept.	Net Value
01/04 Opening Balance	22,00,000	8,50,000	13,50,000
(+) Depreciation for The Year	-	1,44,600	(1,44,600)
(-) Sale of Asset	(45,0000)	(1,77,400)	(2,72,600)
Closing Balance	**17,50,000**	**8,17,200**	**9,32,800**

Example 12:

Trial Balance (extract) as on 31st March

	Dr.	Cr.
Share Capital 10,000 shares of 10 /- Each	-	1,03,500

Additional Info:

Out of 10,000 shares, 7,500 were fully paid & remaining 2,500 was having 8/- Paid up. During the Year, 2/- Called up From Shareholder 2500 shares. All Shareholder have paid 2/- except one Share Holder Mr. Jai holding 500 Share has not paid & his Shares were forfeited & Re- issued in Market @9/- Per Share.

How to present the above situation?

Solution:

Particulars	Amount
No. of Shares held by Mr. Jai	500
Amount already Collected by Co. from Mr. Jai	8/-
Amount Collected from Reissue	9/-
Total Amount Collected by Company	17/-
Face Value per Share	10/-
Gain to company per share	7/-
Total Gain (To be transfer to Capital Reserve) (7 x 500)	3,500/-
Share Capital shall be reduced by 3,500 and transfer to Capital Reserve	

SECTION B – MCQ's

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.
   (d) Bills receivables

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.
   (d) Share application money pending allotment

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
   (d) Deferred tax assets

4. Current maturities of long- term debt will come under
   (a) Current Liabilities.
   (b) Short term borrowings.
   (c) Long term borrowings.
   (d) Short term provisions

5. Declaration of dividends for current year is made after providing for
   (a) Depreciation of past years only.
   (b) Depreciation on assets for the current year and arrears of depreciation of past years (if any).
   (c) Depreciation on current year only and by forgoing arrears of depreciation of past years.
   (d) Excluding current year depreciation

ANSWERS	1	2	3	4	5
	c	a	a	b	b

Student Notes:-