

Financial Statements of a Company

Meaning

Financial statements are the basic & formal annual reports through which corporate management communicates financial info to owners and external parties. They are the end product of the ~~recording~~ accounting process.

They include :

- ① Balance Sheet - position statement, on a date
 - ② Statement of P&L - results for a period
 - ③ Cash Flow Statement - movement of cash
- + Notes to Accounts (mandatory disclosure)

Nature

They reflect a combination of :

1. Recorded facts (historical cost data)
2. Accounting conventions (cost / lower of cost or market, materiality)
3. Postulates (going concern, money measurement, realisation)
4. Personal judgements (depreciation, doubtful debts, inventory valuation)

So they show book values, not market value.

Objectives

The primary objective is to assist users in decision-making. Specific objectives :

- ① Economic resources & obligations of a business
- ② Earning capacity - predict & compare
- ③ Cash flows - amount, timing, uncertainty
- ④ Judge management effectiveness
- ⑤ Social activities of the business
- ⑥ Accounting policies - disclose significant ones

Types of Financial Statements

Two main statements + cash flow :

- (a) Balance Sheet - external reporting
- (b) Statement of P&L - internal needs too
- (c) Cash Flow Statement

Every company under Companies Act, 2013 prepares these as per revised Schedule III.

Format = Schedule III, Cos Act 2013 <-vertical

Not for : Insurance / Banking Co. or where a form is specified under any other Act.

Accounting Standards prevail over Sch. III.

Balance Sheet (Schedule III)

Heading : 'Balance Sheet as at 31st
March, 20...*' (vertical form)

I. Equity & Liabilities

1) Shareholders' Funds

(a) Share Capital

(b) Reserves & Surplus

(c) Money recd against share warrants

2) Share application money pending allotment

3) Non-current Liabilities

(a) Long-term borrowings

(b) Deferred tax liabilities (net)

(c) Other long-term liabilities

(d) Long-term provisions

4) Current Liabilities

(a) Short-term borrowings

(b) Trade payables

(c) Other current liabilities

(d) Short-term provisions

Reserves & Surplus : Capital Res, Capital

Redemption Res, Securities Premium, DRR,

Revaluation Res, Surplus (bal in P&L).

Debit bal of P&L = negative under 'Surplus'.

Balance Sheet : Assets

II. Assets

1) Non-Current Assets

(a) Fixed assets

(i) Tangible (ii) Intangible

(iii) Capital WIP (iv) Intangible u/dev

(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 & cash equivalents

(e) Short-term loans & advances

(f) Other current assets

Rounding-off Rule (Box 1)

Turnover $<$ Rs.100 cr : nearest hundreds / thousands / lakhs / millions.

Turnover $>$ Rs.100 cr : nearest lakhs / millions. Rounding is ~~optional~~ mandatory.

'Sundry Debtors/Creditors' \rightarrow 'Trade Recu/Pay'.

Current / Non-current

An item is **CURRENT** if any one holds :

- in entity's operating cycle, or
- realised/settled within 12 months, or
- held primarily for trading, or
- cash & cash equivalent, or
- no unconditional right to defer settlement ≥ 12 months.

Else **NON-CURRENT** (residual items).

Key treatment rules

Fixed assets : always non-current (even if useful life < 12 months).

Inventories : always current.

Deferred tax assets/liab : always non-current.

Cash & cash equivalent : always current.

Trade payables = ~~Sundry~~ replaces sundry creditors.

Proposed Dividend

Proposed by Board, declared by members in AGM (next FY). Shown as **CONTINGENT**

LIABILITY in Notes to Accounts (AS-4).

Last year's proposed dividend is accounted in current year after AGM approval.

Provisions : < 12 m \rightarrow short-term.

Share Capital in Notes

Dinkar Ltd : Auth cap Rs. 50,00,000 (50,000 shares of Rs. 100). Issued 40,000. Recd all calls except final call Rs. 20 on 500 shares. Forfeited 200 of these.

Notes to Accounts - Share Capital

Authorised : $50,000 \times \text{Rs. } 100 = 50,00,000$

Issued : $40,000 \times \text{Rs. } 100 = 40,00,000$

Subscribed & fully paid :

$35,500 \times 100 = 35,50,000$

Subscribed not fully paid :

300×100 called $30,000$

Less calls-in-arrears (300×20) $6,000$

$= 24,000$

Add Share Forfeiture (200×80) $16,000$

Share Capital = Rs. 35,90,000

← shown in
← Bal Sheet

Note : Calls-in-arrears are deducted from called-up capital ; forfeiture A/c is added back as it is amount already received.

Preliminary expenses : written-off fully in the year incurred (from Sec. Premium first).

Statement of Profit & Loss

'For the year ended' (Exhibit 3.2)

I. Revenue from operations

II. Other income

III. Total Revenue (I + II)

IV. Expenses :

Cost of materials consumed.

Purchases of stock-in-trade

Changes in inventories (FG, WIP) -

Employee benefits expense

Finance costs

Depreciation & amortisation

Other expenses

V. Profit before exceptional / extraordinary items & tax (III - IV)

VII. Profit before tax

X. Tax expense (current + deferred)

XV. Profit/(Loss) for the period

XVI. Earnings per share : Basic & Diluted

$$\text{Net Profit} = \text{Total Revenue} - \text{Total Exp} - \text{Tax}$$

Finance cost = only interest on borrowings.

P&L : Solved Illustration

Prepare P&L (profit before tax) - Sch III :

Sales(Net) 10,00,000 ; Purchases(adj) 4,00,000

Wages 1,20,000 ; Salaries 80,000 ;

Deprn on P&M 16,000 ; 10% deb 1,00,000. *

Statement of P&L (31 Mar 2017)

I. Revenue from operations	10,00,000
Total Income	10,00,000
II. Expenses :	
Cost of materials (adj pur)	4,00,000
Employee benefits (Wgt+Sal)	2,00,000
Finance cost (10% x 1,00,000)	10,000
Depreciation	16,000
Total Expenses	6,26,000

Profit before tax = Rs. 3,74,000

<- 10,00,000

<- 6,26,000

Wages + Salary shown together as Employee
Benefit Expenses via Notes to Accounts.

Limitations

No current situation ; assets may not realise;

bias ; aggregate info ; no qualitative info ;

only interim reports for a period.

Uses & Importance

- ① Stewardship report. mgmt performance
- ② Fiscal policy basis for govt taxation
- ③ Granting credit banks & FIs decide
- ④ Prospective investors - solvency check
- ⑤ Existing investors - continue/exit
- ⑥ Trade assoc standard ratios
- ⑦ Stock exch transparency, price quotes

Quick Recall

Users : Shareholders, Investors, Creditors,
Lenders, Customers, Mgmt, Govt, Public.

Balance* Sheet \rightarrow position on a DATE.

P&L \rightarrow results over a PERIOD.

Cash Flow \rightarrow movement of cash.

Exam Pointers

- Sch III is the source of all formats.
- Major head + Sub-head questions are common.
- Calls-in-arrears deducted ; forfeiture added.
- Proposed dividend = contingent liab (notes).
- Preliminary exp written off* fully in year.
- Loose tools, stores = inventory (current).

Practice : Illus 1-8, Numericals 1-7 (NCERT).