

CMA Inter

Corporate Accounting

Marathon
(June 24)



CA BISHNU KEDIA

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Presentation Of Financial Statements (As Per Schedule III)

Question 1

While preparing Balance Sheet (31-03-2025), Accountant of A. Ltd is confused regarding classification of Trade Payables into current and non-current.

Sl No.	Amount due (Rs.)	Due from	To be settled on
1	1,60,000	01-06-2024	18-12-2025
2	2,10,000	01-08-2024	30-10-2026
3	90,000	01-12-2024	20-07-2026
4	40,000	01-02-2024	30-04-2026
5	2,30,000	06-03-2025	05-07-2026
6	5,60,000	12-09-2024	31-07-2025

The normal operating cycle of the company is 15 months. Advise the Accountant on classification with reason.

Question 2

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, 2011.

Particulars	₹	Particulars	₹
Inventory	6,80,000	Equity Shares	
Furniture	2,00,000	Capital (Shares of ₹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

<i>Bad debts</i>	35,000	<i>Sales</i>	42,68,000
<i>Commission</i>	1,20,000	<i>Rent received</i>	46,000
<i>Materials consumed</i>	23,19,000	<i>Transfer fees</i>	10,000
<i>Plant and Machinery</i>	8,60,000	<i>Profit & Loss account</i>	1,39,000
<i>Rentals</i>	25,000	<i>Depreciation provision:</i>	
<i>Current account</i>	45,000	<i>Machinery</i>	1,46,000
<i>Cash</i>	8,000		
<i>Interest on bank loans</i>	1,16,000		
<i>Preliminary expenses</i>	10,000		
<i>Fixtures</i>	3,00,000		
<i>Wages</i>	9,00,000		
<i>Consumables</i>	84,000		
<i>Freehold land</i>	15,46,000		
<i>Tools & Equipment</i>	2,45,000		
<i>Goodwill</i>	2,65,000		
<i>Trade receivables</i>	4,40,000		
<i>Dealer aids</i>	21,000		
<i>Transit insurance</i>	30,000		
<i>Trade expenses</i>	37,000		
<i>Distribution freight</i>	54,000		
<i>Debenture Interest</i>	55,000		
	85,35,000		85,35,000

Additional information: Closing Inventory on 31-3-2011: ₹8,23,000.

Solution

Haria Chemicals Ltd.
Balance Sheet as at 31st March, 2011

	Schedule No. (1)	Rupees as at the end of 31 st March 2011 (2)
Equity and Liabilities		
(1) Shareholders' funds :		
(a) Share Capital	1	25,00,000
(b) Reserves and Surplus	2	7,40,000
(2) Non-Current Liabilities		
(a) Long term borrowings	3	11,45,000
(3) Current Liabilities		
(a) Trade payables		2,81,000
Total		46,66,000
Assets		
(1) Non-current assets		
(a) PPE	4	30,05,000
(b) Intangible assets (goodwill)		2,65,000
(2) Current assets		
(a) Inventories		8,23,000
(b) Trade receivables		4,40,000
(c) Cash and bank balances	5	53,000
(d) Short term loans and advances	6	80,000
Total		46,66,000

Haria Chemicals Ltd.

Statement of Profit and Loss for the year ended 31st March, 2011

	Schedule	Figures	
Revenue from operations		42,68,000	
Other income	7	<u>56,000</u>	
	(A)	43,24,000	
Expenses			
Cost of materials consumed		23,19,000	
Change in inventory of goods finished	8	(1,43,000)	
Employee benefit expenses	9	9,00,000	
Finance cost	10	1,71,000	
Other expenses	11	<u>4,76,000</u>	
	(B)	<u>37,23,000</u>	
Profit before tax (A - B)			6,01,000
Provision for tax			<u>—</u>
Profit for the period			6,01,000

Notes to Accounts

1. Share capital

Authorised:

Equity share capital of ₹10 each 25,00,000

Issued and Subscribed:

Equity share capital of ₹10 each 25,00,000

2. Reserves and Surplus

Balance as per last balance sheet 1,39,000

Balance in profit and loss account 6,01,000

7,40,000

3. Long term Borrowings

11% Debentures	5,00,000
Bank loans (assumed long-term)	<u>6,45,000</u>
	<u>11,45,000</u>

4. PPE

	Gross block	Depreciation	Net Block
Freehold land	15,46,000		15,46,000
Furniture	2,00,000		2,00,000
Fixtures	3,00,000		3,00,000
Plant & Machinery	8,60,000	1,46,000	7,14,000
Tools & Equipment	<u>2,45,000</u>	-----	<u>2,45,000</u>
Total	31,51,000	1,46,000	30,05,000

5. Cash and bank balances

Cash and cash equivalents	
Current account balance	45,000
Cash	8,000
Other bank balances	<u>Nil</u>
	<u>53,000</u>

6. Short-term loans and Advances

Loan to directors	80,000
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7. Other Income

Rent received	46,000
Transfer fees	<u>10,000</u>
	<u>56,000</u>

8. Changes in inventory of finished goods, WIP & Stock in trade

Opening inventory	6,80,000
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<i>Closing inventory</i>	<u>(8,23,000)</u>	<u>(1,43,000)</u>
9. Employee benefit expense		
<i>Wages</i>		9,00,000
10. Finance cost		
<i>Interest on bank loans</i>		1,16,000
<i>Debenture interest</i>		<u>55,000</u>
		<u>1,71,000</u>
11. Other Expenses		
<i>Consumables</i>		84,000
<i>Preliminary expenses</i>		10,000
<i>Bad debts</i>		35,000
<i>Discount</i>		40,000
<i>Rentals</i>		25,000
<i>Commission</i>		1,20,000
<i>Advertisement</i>		20,000
<i>Dealers' aids</i>		21,000
<i>Transit insurance</i>		30,000
<i>Trade expenses</i>		37,000
<i>Distribution freight</i>		<u>54,000</u>
		<u>4,76,000</u>

Question 3

On 31st March, 2011 Bose and Sen Ltd. provides to you the following ledger balances after preparing its Profit and Loss Account for the year ended 31st March, 2011:

Credit Balances:

	₹
Equity shares capital, fully paid shares of ₹10 each	70,00,000
General Reserve	15,49,100
Loan from State Finance Corporation (Secured by hypothecation of Plant & Machinery Repayable within one year ₹ 2,00,000)	10,50,000
Loans: Unsecured (Long term)	8,47,000
Sundry Creditors for goods & expenses (Payable within 6 months)	14,00,000
Profit & Loss Account	7,00,000
Provision for Taxation	8,16,900
	1,33,63,000

Debit Balances:

	₹
Calls in arrear	7,000
Land	14,00,000
Buildings	20,50,000
Plant and Machinery	36,75,000
Furniture & Fixture	3,50,000
Inventories: Finished goods	14,00,000
Raw Materials	3,50,000
Trade Receivables	14,00,000
Advances: Short-term	2,98,900

Cash in hand	2,10,000
Balances with banks	17,29,000
Preliminary Expenses	93,100
Patents & Trademarks	4,00,000
	1,33,63,000

The following additional information is also provided in respect of the above balances:

1. 4,20,000 fully paid equity shares were allotted as consideration for land & buildings.
2. Cost of Building ₹ 28,00,000
3. Cost of Plant & Machinery ₹ 49,00,000
Cost of Furniture & Fixture ₹ 4,37,500
4. Trade receivables for ₹ 3,80,000 are due for more than 6 months.
5. The amount of Balances with Bank includes ₹18,000 with a bank which is not a scheduled Bank and the deposits of ₹ 5 lakhs are for a period of 9 months.
6. Unsecured loan includes ₹2,00,000 from a Bank and ₹1,00,000 from related parties.
7. Entire amount of Preliminary expenses to be written off, by adjusting from opening balance of General Reserve.

You are not required to give previous year's figures. You are required to prepare the Balance Sheet of the Company as on 31st March, 2011 as required under Schedule III to the Companies Act, 2013.

Solution

Bose and Sen Ltd.

Balance Sheet as at 31st March, 2011

Particulars		Notes	Figures at the end of current reporting period (₹)
Equity and Liabilities			
1	Shareholders' funds		
a	Share capital	1	69,93,000
b	Reserves and Surplus	2	21,56,000
2	Non-current liabilities		
a	Long-term borrowings	3	16,97,000
3	Current liabilities		
a	Trade Payables		14,00,000
b	Short term borrowings	4	2,00,000
c	Short-term provisions	5	8,16,900
	Total		1,32,62,900
Assets			
1	Non-current assets		
a	PPE	6	74,75,000
b	Intangible assets (Patents & Trade Marks)		4,00,000
2	Current assets		
a	Inventories	7	17,50,000
b	Trade receivables	8	14,00,000
c	Cash and bank balances	9	19,39,000
d	Short-term loans and advances		2,98,900
	Total		1,32,62,900

Notes to Accounts

			₹
1	Share Capital		
	Equity share capital		
	Issued, subscribed and called up		
	7,00,000 Equity Shares of ₹ 10 each	70,00,000	
	(Out of the above 4,20,000 shares have		
	been issued for consideration other	<u>(7,000)</u>	<u>69,93,000</u>
	than cash)		69,93,000
2	Less: Calls in arrears	15,49,100	
	Total	<u>(93,100)</u>	14,56,000
	Reserves and Surplus		
	General Reserve		<u>7,00,000</u>
	Less: Preliminary expenses		<u>21,56,000</u>
3	Surplus (Profit & Loss A/c)		
	Total		
	Long-term borrowings		8,50,000
	Secured		
	Term Loans		
	Loan from State Finance Corporation	2,00,000	
	(₹ 10,50,000 - ₹ 2,00,000) (Secured	1,00,000	
	by hypothecation of Plant and	<u>5,47,000</u>	<u>8,47,000</u>
	Machinery)		<u>16,97,000</u>
4	Unsecured		
	Bank Loan		
	Loan from related parties		2,00,000
	Others		
	Total		

	Short term borrowings		
	Current maturities of long-term debt-loan Instalment repayable within one year		
5	Short-term provisions		
	Provision for taxation		8,16,900
6	Property, plant and equipment		
	Land		
	Buildings		14,00,000
	Less: Depreciation	28,00,000	
	Plant & Machinery	(7,50,000) (b.f.)	20,50,000
	Less: Depreciation	49,00,000	
	Furniture & Fittings	(12,25,000)	36,75,000
	Less: Depreciation	(b.f.)	
	Total	4,37,500	
	Inventories	(87,500) (b.f.)	3,50,000
	Raw Material		74,75,000
7	Finished goods		3,50,000
			14,00,000
	Trade receivables		17,50,000
8	Debts outstanding for a period exceeding six months		3,80,000
	Other Debts		10,20,000
	Total		14,00,000
9	Cash and bank balances		
	Cash and cash equivalents		12,11,000

Cash at bank with Scheduled Banks	18,000	12,29,000
with others		2,10,000
Cash in hand		5,00,000
Other bank balances		19,39,000
Bank deposits for period of 9 months		
Total		

Question 4

Ring Ltd. was registered with a nominal capital of ₹10,00,000 divided into shares of ₹100 each. The following Trial Balance is extracted from the books on 31st March, 2012:

Particulars	₹	Particulars	₹
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 (1-4-2011)	
Purchases (finished goods)	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	(1-4-2011)	
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	<u>1,10,000</u>
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, 2012 and Balance sheet as at that date after taking into consideration the following information:

1. Closing stock is more than opening stock by ₹1,60,000;
2. Provide to doubtful debts @ 4% on Debtors
3. Make a provision for income tax @30%.
4. Depreciation expense included depreciation of ₹16,000 on Building and that of ₹24,000 on Machinery.
5. The directors declared a dividend @ 25% on 2nd April, 2012 and transfer to General Reserve @ 10%.
6. Bills Discounted but not yet matured ₹20,000.

Solution

Ring Ltd.

Profit and Loss Statement for the year ended 31st March, 2012

	Particulars	Note No.	(₹ In lacs)
I	Revenue from operations		10,40,000
II	Other income (interest on investment)		<u>24,000</u>
III	Total income [I + II]		<u>10,64,000</u>
IV	Expenses:		
	Cost of purchase [4,20,000+ 1,60,000]		5,80,000
	Changes in inventories [20,000-1,80,000]		(1,60,000)
	Employee Benefits Expense		1,20,000
	Finance Costs (debenture interest)		56,000

	Depreciation and Amortisation Expenses		40,000
	Other Expenses	8	<u>1,24,000</u>
	Total Expenses		<u>7,60,000</u>
V	Profit before Tax (III-IV)		3,04,000
VI	Tax Expenses @ 30%		(91,200)
VII	Profit for the period		2,12,800

Balance Sheet of Ring Ltd. as at 31st March, 2012

	Particulars	Note No.	₹
I	EQUITY AND LIABILITIES		
	(1) Shareholders' Funds		
	(a) Share Capital	1	4,00,000
	(b) Reserves and Surplus	2	3,42,800
	(2) Non-Current Liabilities		
	(a) Long-term Borrowings (14% debentures)		4,00,000
	(3) Current Liabilities		1,84,000
	(a) Trade Payable (Sundry Creditors)	3	42,000
	(b) Other Current Liabilities	4	91,200
	(c) Short-Term Provisions		14,60,000
II	Total		
	ASSETS		

(1)	Non-Current Assets		
	(a) PPE	5	5,70,000
	(b) Non-current Investments		2,40,000
(2)	Current Assets		
	(a) Inventories	6	2,26,000
	(b) Trade Receivables	7	2,40,000
	(c) Cash and bank balances		60,000
	(d) Short Term Loans and Advances (Advance Payment of Tax)		1,20,000
	(e) Other Current Assets (Interest accrued on investments)		4,000
	Total		14,60,000

Note: There is a Contingent Liability for bills discounted but not yet matured amounting to ₹ 20,000.

Notes to Accounts

1.	Share Capital		
	Authorised Capital		
	10,000 Equity Shares of ₹100 each		<u>10,00,000</u>
	Issued Capital		
	4,000 Equity Shares of ₹100 each		4,00,000
	Subscribed Capital and fully paid		
	4,000 Equity Shares of ₹100 each		4,00,000
2.	Reserve and Surplus		
	General Reserve [₹ 80,000 + ₹ 21,280]		1,01,280
	Balance of Statement of Profit & Loss Account		
	Opening Balance	50,000	

	Add: Profit for the period	<u>2,12,800</u>	
		2,62,800	
	Appropriations		
	Transfer to General Reserve @ 10%	<u>(21,280)</u>	<u>2,41,520</u>
			<u>3,42,800</u>
3.	Other Current Liabilities		
	Unclaimed Dividend		10,000
	Outstanding Expenses		4,000
	Interest accrued on Debentures		<u>28,000</u>
			<u>42,000</u>
4.	Short-Term Provision		
	Provision for Tax		91,200
5	Property, plant and equipment		
	Buildings	5,80,000	
	Less: Provision for Depreciation	<u>1,00,000</u>	4,80,000
	Plant and Equipment	2,00,000	
	Less: Provision for Depreciation	<u>1,10,000</u>	<u>90,000</u>
			<u>5,70,000</u>
6	Inventories		
	Closing Stock of Finished Goods	1,80,000	
	Loose Tools	<u>46,000</u>	<u>2,26,000</u>
7	Trade Receivables		
	Sundry Debtors	2,50,000	
	Less: Provision for Doubtful Debts	<u>(10,000)</u>	<u>2,40,000</u>
8.	Other Expenses		
	Rent		52,000
	Directors' Fees		20,000
	Bad Debts		12,000

Provision for Doubtful Debts (4% of ₹ 2,50,000 less ₹ 6,000)	4,000
Sundry Expenses	36,000
	1,24,000

Note: The final dividend will not be recognized as a liability at the balance sheet date (even if it is declared after reporting date but before approval of the financial statements) as per Accounting Standards. Hence, it has not been recognized in the financial statements for the year ended 31 March, 2012. Such dividends will be disclosed in notes only.

Question 5

Om Ltd. has authorized capital of ₹ 50 lakhs divided into 5,00,000 equity shares of ₹ 10 each. Their books show the following ledger balances as on 31st March, 2021:

	₹		₹
Inventory 1.4.2020	6,65,000	Bank Current Account (Dr. balance)	20,000
Discounts & Rebates allowed	30,000	Cash in hand	11,000
Carriage Inwards	57,500		
Purchases	12,32,500	Calls in Arrear @ ₹ 2 per share	10,000
Rate, Taxes and Insurance	55,000	Equity share capital (2,00,000 shares of ₹ 10 each)	20,00,000
Furniture & Fixtures	1,50,000		
Business Expenses	56,000	Trade Payables	2,40,500
Wages	14,79,000	Sales	36,17,000

Freehold Land	7,30,000	Rent (Cr.)	30,000
Plant & Machinery	7,50,000	Transfer fees received	6,500
Engineering Tools	1,50,000	Profit & Loss A/c (Cr.)	67,000
Trade Receivables	4,00,500	Repairs to Building	56,500
Advertisement Expenses	15,000	Bad debts	25,500
Commission & Brokerage Expenses	67,500		

The inventory (valued at cost or market value, which is lower) as on 31st March, 2021 was ₹ 7,05,000. Outstanding liabilities for wages ₹ 25,000 and business expenses ₹ 36,500. It was decided to transfer ₹ 10,000 to reserves.

Charge depreciation on written down values of Plant & Machinery @ 5%, Engineering Tools @ 20% and Furniture & Fixtures @10%. Provide ₹ 25,000 as doubtful debts for trade receivables. Provide for income tax @ 30%. It was decided to transfer ₹ 10,000 to reserves.

You are required to prepare Statement of Profit & Loss for the year ended 31st March, 2021 and Balance Sheet as at that date.

Solution :

Balance Sheet of Om Ltd. as at 31st March, 2021

	Particulars	Note No.	(₹)
I	Equity and Liabilities		
	(1) Shareholders' Funds		
	(a) Share Capital	1	19,90,000
	(b) Reserves and Surplus	2	3,82,000
	(2) Current Liabilities		
	(a) Trade Payables		2,40,500
	(b) Other Current Liabilities	3	61,500
	(c) Short-Term Provisions	4	1,35,000
	Total		28,09,000
II	Assets		
	(1) Non-Current Assets		
	(a) Property, Plant and Equipment	5	16,97,500
	(2) Current Assets		
	(a) Inventories		7,05,000
	(b) Trade Receivables	6	3,75,500
	(c) Cash and Cash Equivalents	7	31,000
	Total		28,09,000

Statement of Profit and Loss of Om Ltd.
for the year ended 31st March, 2021

	Particulars	Note No.	(₹)
I	Revenue from Operations		36,17,000
II	Other Income	8	36,500
III	Total Revenue [I + II]		36,53,500
IV	Expenses:		
	Cost of purchases		12,32,500
	Changes in Inventories [6,65,000-7,05,000]		(40,000)
	Employee Benefits Expenses	9	15,04,000
	Depreciation and Amortization Expenses		82,500
	Other Expenses	10	4,24,500
	Total Expenses		32,03,500
V	Profit before Tax (III-IV)		4,50,000
VI	Tax Expenses @ 30%		(1,35,000)
VII	Profit for the period		3,15,000

Notes to Accounts:

1. Share Capital

Authorized Capital	
5,00,000 Equity Shares of ₹ 10 each	50,00,000
Issued Capital	
2,00,000 Equity Shares of ₹ 10 each	20,00,000
Subscribed Capital and Fully paid	
1,95,000 Equity Shares of ₹10 each	19,50,000
Subscribed Capital but not Fully paid	
5,000 Equity Shares of ₹10 each ₹ 8 paid (Call unpaid ₹10,000)	40,000
	19,90,000

2. Reserves and Surplus

General Reserve		10,000
Surplus i.e. Balance in Statement of Profit & Loss:		
Opening Balance	67,000	
Add: Profit for the period	3,15,000	
Less: Transfer to Reserve		3,72,000
	<u>(10,000)</u>	<u>3,82,000</u>

3. Other Current Liabilities

Outstanding Expenses [25,000+36,500]	61,500
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4. Short-Term Provisions

Provision for Tax	1,35,000
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5. Property, Plant and Equipment

Particulars	Value given (₹)	Depreciation Rate	Depreciation Charged (₹)	Written down value at the end (₹)
Land	7,30,000		-	7,30,000
Plant & Machinery	7,50,000	5%	37,500	7,12,500
Furniture & Fixtures	1,50,000	10%	15,000	1,35,000
Engineering Tools	1,50,000	20%	30,000	1,20,000
	<u>17,80,000</u>		<u>82,500</u>	<u>16,97,500</u>

6. Trade Receivables

Trade receivables	4,00,500
Less: Provision for doubtful debts	(25,000)
	<u>3,75,500</u>

7. Cash & Cash Equivalent

Cash Balance	11,000
Bank Balance in current A/c	20,000
	31,000

8. Other Income

Miscellaneous Income (Transfer fees)	6,500
Rental Income	30,000
	36,500

9. Employee Benefits Expenses

Wages	14,79,000
Add: Outstanding wages	25,000
	15,04,000

10. Other Expenses

Carriage Inwards	57,500
Discount & Rebates	30,000
Advertisement	15,000
Rate, Taxes and Insurance	55,000
Repairs to Buildings	56,500
Commission & Brokerage	67,500
Miscellaneous Expenses [56,000+36,500] (Business Expenses)	92,500
Bad Debts	25,500
Provision for Doubtful Debts	25,000
	4,24,500

Cash Flow Statement

Cash Flow Statements is a statements which presents Infows and Outflows of cash and cash equivalentents during specifed period.

Cash and Cash Equivalentents

Cash comprises of cash in hand and demand deposits with banks. Cash equivalentents are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignifcant risk of changes in value. In includes short term investments or deposits or advances which can be realised within 3 months (intention for realisation is critical).

Cash Flows are infows and outflows of cash and cash equivalentents and are classified into following activities:

- 1.Cash Flow from Operating Activities.
- 2.Cash Flow from Investing Activities.
- 3.Cash Flow from Financing Activities.

Operating activities

Operating activities are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities.

Examples of cash fows from operating activities are:

- (a) cash receipts from the sale of goods and the rendering of services;
- (b) cash receipts from royalties, fees, commissions and other revenue;
- (c) cash payments to suppliers for goods and services;
- (d) cash payments to and on behalf of employees;
- (e) cash receipts and cash payments of an insurance enterprise for premiums and claims, annuities and other policy benefets;
- (f)cash payments or refunds of income taxes unless they can be specifcally

- identified with financing and investing activities; and
- (g) cash receipts and payments relating to futures contracts, forward contracts, option contracts and swap contracts when the contract are held for dealing or trading purposes.

1. Direct Method (A)

Cash Sale	xxx
Collection from Debtors	xxx
Cash Purchases	(xx)
Payment to Creditors	(xx)
Payment for Operating Expenses	(xx)
Cash Generated from Operations	xxx
Taxes Paid	(xx)
Cash Flow before extra-ordinary items	xxx
Extra-ordinary items	xxx
Net Cash from Operating Activities	xxx

2. Indirect Method (A)

Net Profit before Tax and Extraordinary Items	xxx
<u>Adjustments for Non-Cash and Non-Operating items:</u>	
Depreciation	xxx
Intangible and Fictitious assets written off	xxx
Interest Income or Expense	xxx
Dividend Received	(xxx)
Operating Profit before Working Capital changes	xxx
<u>Adjustments for Working Capital Changes:</u>	
Debtors	xxx

<i>Creditors</i>	xxx
<i>Inventories</i>	xxx
<i>Outstanding Expenses</i>	xxx
<i>Accrued Incomes</i>	<u>xxx</u>
<i>Cash generated from Operations</i>	xxx
<i>Taxes Paid</i>	<u>xxx</u>
<i>Cash Flow before Extraordinary items</i>	xxx
<i>Extraordinary items</i>	<u>xxx</u>
<i>Net Cash from Operating Activities</i>	xxx

Investing activities

Investing activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.

Cash flow from Investing Activities (B)

<i>Sale / Purchase of Fixed Assets / Investment</i>	Xxx
<i>Income from Investments</i>	<u>xxx</u>
<i>Net Cash from Investing Activities</i>	xxx

Financing activities

Financing activities are activities that result in changes in the size and composition of the owners' capital (including preference share capital in the case of a company) and borrowings of the enterprise.

Cash flow from Financing Activities (C)

<i>Issue of Share Capital</i>	xxx
<i>Loan raised / Debentures Issued</i>	xxx
<i>Share Capital Redeemed / Buy Back</i>	(xx)
<i>Loan repaid / Debentured Redeemed</i>	(xx)

<i>Interest paid</i>	(xx)
<i>Dividend paid</i>	(xx)
<i>Net Cash from Financing Activities</i>	xxx

<i>TOTAL (A + B + C)</i>	xxx
<i>Add : Opening Cash & Cash Equivalent</i>	<u>xxx</u>
<i>Closing Cash & Cash equivalent</i>	<u>xxx</u>

Important Notes:

- In case of financial entities, interest and dividend received are considered operating activities and interest paid is also considered operating activities.*
- Interest received by Financial institutions like banks, NBFC, etc. classify it as Operating Activity (For others it is investing activity)*
- Interest paid by Financial institutions like Banks, NBFC etc., classify it as Operating Activities (For others it is Financing activity)*
- Dividend Paid is always classified as Financing Activity for all the entities.*
- Investment in Subsidiary or group Company is classified as Investing Activities.*
- Taxes (including Self-Assessment Tax, TDS, Withholding tax) should be classified as follows :*
 - Corporation Dividend Tax is **Financing Activity***
 - Tax on investment income is **Investing Activity***
 - Other taxes paid are **Operating Activity***
- Extraordinary Items are reported as separate item in Cash Flows.*
 - Voluntary Retirement Compensation Paid → Operating Items*
 - Law suit payment/received → Operating Item*
 - Insurance Claim on loss of PPE → Investing Activity*
- Government Grant received for a capital asset is Investing Activity.*

9. If any exchange difference has been recognized in P/L, it should be eliminated (since it is not cash flow)

Exchange Gain → Reduce from Operating Activities & Reduce from Asset/Liability for Exchange Difference.

Exchange Loss → Add in Operating Activity & Add in Asset/Liability for exchange difference.

10. Service cost for Share Capital is called Dividend & service cost for Borrowings is called Interest.

11. Residual Items are considered as operating items.

Question 1

From the following Summary Cash Account of X Ltd. prepare Cash Flow Statement for the year ended 31st March, 2011 in accordance with AS 3 (Revised) using the direct method. The company does not have any cash equivalents.

Summary Cash Account for the year ended 31.3.2011

	₹ 000		₹ 000
Balance on 1.4.2010	50	Payment to Suppliers	2,000
Issue of Equity Shares	300	Purchase of Fixed Asset	200
Receipts from Customers	2,800	Overhead expense	200
Sale of Fixed Assets	100	Wages and Salaries	100
		Taxation	250
		Dividend	50
		Repayment of Bank Loan	300
		Balance on 31.3.2011	150
	3,250		3,250

Solution

X Ltd.

Cash Flow Statement for the year ended 31st March, 2011

(Using direct method)

	₹ 000	₹ 000
Cash flows from operating activities		
Cash receipts from customers	2,800	
Cash payments to suppliers	(2,000)	
Cash paid to employees	(100)	
Cash payments for overheads	(200)	
Cash generated from operations	500	
Income tax paid	(250)	
Net cash generated from operating activities		250
Cash flows from investing activities		
Payments for purchase of fixed assets	(200)	
Proceeds from sale of fixed assets	100	
Net cash used in investing activities		(100)
Cash flows from financing activities		
Proceeds from issuance of equity shares	300	
Bank loan repaid	(300)	
Dividend paid	(50)	
Net cash used in financing activities		(50)
Net increase in cash		100
Cash at the beginning of the year		50
Cash at the end of the year		150

Question 2

Prepare cash flow statement of M/s MNT Ltd. for the year ended 31st March, 2011 with the help of the following information:

- (1) Company sold goods for cash only.
- (2) Gross Profit Ratio was 30% for the year, gross profit amounts to ₹3,82,500.
- (3) Opening inventory was lesser than closing inventory by ₹35,000.
- (4) Wages paid during the year ₹4,92,500.
- (5) Office and selling expenses paid during the year ₹75,000.
- (6) Dividend paid during the year ₹30,000.
- (7) Bank loan repaid during the year ₹2,15,000 (included interest ₹15,000).
- (8) Trade payables on 31st March, 2010 exceed the balance on 31st March, 2011 by ₹25,000.
- (9) Amount paid to trade payables during the year ₹4,60,000.
- (10) Tax paid during the year amounts to ₹65,000 (Provision for taxation as on 31.03.2011 ₹45,000).
- (11) Investments of ₹7,00,000 sold during the year at a profit of ₹20,000.
- (12) Depreciation on fixed assets amounts to ₹85,000.
- (13) Plant and machinery purchased on 15th November, 2010 for ₹2,50,000.
- (14) Cash and Cash Equivalents on 31st March, 2010 ₹2,00,000.
- (15) Cash and Cash Equivalents on 31st March, 2011 ₹6,07,500.

Solution

M/s MNT Ltd.

Cash Flow Statement for the year ended 31st March, 2011

(Using direct method)

Particulars	₹	₹
Cash flows from Operating Activities		
Cash sales (₹ 3,82,500/.30)		12,75,000
Less: Cash payments for trade payables	(4,60,000)	
Wages Paid	(4,92,500)	(10,27,500)
Office and selling expenses	(75,000)	
Cash generated from operations before taxes		2,47,500
Income tax paid		(65,000)
Net cash generated from operating activities (A)		1,82,500
Cash flows from investing activities		
Sale of investments (7,00,000 + 20,000)	7,20,000	
Payments for purchase of Plant & machinery	(2,50,000)	
Net cash used in investing activities (B)		4,70,000
Cash flows from financing activities	(2,15,000)	
Bank loan repayment (including interest)	(30,000)	
Dividend paid		(2,45,000)
Net cash used in financing activities (C)		4,07,500
Net increase in cash (A+B+C)		2,00,000
Cash and cash equivalents at beginning of the period		6,07,500
Cash and cash equivalents at end of the period		

Question 3

On the basis of the following information prepare a Cash Flow Statement for the year ended 31st March, 2021 (Using direct method):

- (i) Total sales for the year were ₹ 597 crores out of which cash sales amounted to ₹393 crores.
- (ii) Receipts from credit customers during the year, totalled ₹ 201 crores.
- (iii) Purchases for the year amounted to ₹ 330 crores out of which credit purchases were 80%.

Balance in creditors as on

1.4.2020	₹ 126 crores
31.3.2021	₹ 138 crores

- (iv) Suppliers of other consumables and services were paid ₹ 28.5 crores in cash.
- (v) Employees of the enterprises were paid 30 crores in cash.
- (vi) Fully paid preference shares of the face value of ₹ 48 crores were redeemed. Equity shares of the face value of ₹ 30 crores were allotted as fully paid up at premium of 20%.
- (vii) Debentures of ₹ 30 crores at a premium of 10% were redeemed. Debenture holders were issued equity shares in lieu of their debentures.
- (viii) ₹ 39 crores were paid by way of income tax.
- (ix) A new machinery costing ₹ 15 was purchased.
- (x) Investment costing ₹ 27 cores were sold at a loss of ₹ 3 crores.
- (xi) Dividends totalling ₹ 22.5 crores was also paid.
- (xii) Debenture interest amounting ₹ 3 crore was paid.
- (xiii) On 31st March 2020, Balance with Bank and Cash on hand totalled ₹ 3 crores.

Solution:

Cash flow statement (using direct method) for the year ended 31st March, 2021

	(₹ in crores)	(₹ in crores)
Cash flow from operating activities		
Cash sales	393	
Cash collected from credit customers	201	
Less: Cash paid to suppliers for goods & services and to employees (Refer Working Note)	(376.5)	
Cash from operations	217.5	
Less: Income tax paid	(39)	
Net cash generated from operating activities		178.5
Cash flow from investing activities		
Payment for purchase of Machine	(15)	
Proceeds from sale of investments	24	
Net cash used in investing activities		9
Cash flow from financing activities		
Redemption of Preference shares	(48)	
Proceeds from issue of Equity shares	36	
Debenture interest paid	(3)	
Dividend Paid		
Net cash used in financing activities	<u>(22.5)</u>	(37.5)
Net increase in cash and cash equivalents		150
Add: Cash and cash equivalents as on 1.04.2020		3
Cash and cash equivalents as on 31.3.2021		153

Working Note:

Calculation of cash paid to suppliers of goods and services and to employees

	(₹ in crores)
Opening Balance in creditors Account	126
Add: Purchases (330x .8)	264
Total	390
Less: Closing balance in Creditors Account	138
Cash paid to suppliers of goods	252
Add: Cash purchases (330x .2)	66
Total cash paid for purchases to suppliers (a)	318
Add: Cash paid to suppliers of other consumables and services (b)	28.5
Add: Payment to employees (c)	30
Total cash paid to suppliers of goods & services and to employees [(a)+ (b) + (c)]	376.5

Question 4

Prepare Cash flow for Gamma Ltd., for the year ending 31.3.2011 from the following information:

- (1) Sales for the year amounted to ₹135 crores out of which 60% was cash sales.
- (2) Purchases for the year amounted to ₹55 crores out of which credit purchase was 80%.
- (3) Administrative and selling expenses amounted to ₹ 18 crores and salary paid amounted to ₹22 crores.
- (4) The Company redeemed debentures of ₹ 20 crores at a premium of 10%. Debenture holders were issued equity shares of ₹ 15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was ₹1.5 crores.

- (5) Dividend paid during the year amounted to ₹11.7 crores.
- (6) Investment costing ₹12 crores were sold at a profit of ₹2.4 crores.
- (7) ₹ 8 crores was paid towards income tax during the year.
- (8) A new plant costing ₹21 crores was purchased in part exchange of an old plant. The book value of the old plant was ₹12 crores but the vendor took over the old plant at a value of ₹10 crores only. The balance was paid in cash to the vendor.
- (9) The following balances are also provided:

	₹ in crores 1.4.2010	₹ in crores 31.3.2011
Debtors	45	50
Creditors	21	23
Bank	6	18.2

Solution

Gamma Ltd.

Cash Flow Statement for the year ended 31st March, 2011

(Using direct method)

Particulars	₹ in crores	₹ in crores
Cash flows from operating activities		
Cash sales (60% of 135)	81	
Cash receipts from Debtors	49	
[45+ (135x40%) - 50]	(11)	
Cash purchases (20% of 55)	(42)	
Cash payments to suppliers [21+ (55x80%) - 23]	(22)	
	(18)	
Cash paid to employees	37	
	(8)	

Cash payments for overheads (Adm. and selling)		29
Cash generated from operations	14.4	
Income tax paid	(11)	
Net cash generated from operating activities		3.4
Cash flows from investing activities		
Sale of investments (12+ 2.40)		
Payments for purchase of fixed assets (21 - 10)		
Net cash generated from investing activities		
Cash flows from financing activities		
Redemption of debentures (22-15)	(7)	
Interest paid	(1.5)	
Dividend paid	<u>(11.7)</u>	
Net cash used in financing activities		(20.2)
Net increase in cash		12.2
Cash at beginning of the period		6.0
Cash at end of the period		18.2

Significant non-cash items:

- (a) Debenture-holders received equity shares of ₹ 15 crores on redemption of the debentures.
- (b) Plant having book value of ₹ 12 crores was given in exchange of an asset costing ₹ 21 crores. The said plant was transferred at a value of ₹ 10 crores only, and ₹ 11 crores was paid for the balance dues towards the plant.

Question 5

The following information was provided by PQR Ltd. for the year ended 31st March, 2019 :

- (1) Gross Profit Ratio was 25% for the year, which amounts to ₹ 3,75,000.
- (2) Company sold goods for cash only.
- (3) Opening inventory was lesser than closing inventory by ₹ 25,000.
- (4) Wages paid during the year ₹ 5,55,000.
- (5) Office expenses paid during the year ₹ 35,000.
- (6) Selling expenses paid during the year ₹ 15,000.
- (7) Dividend paid during the year ₹ 40,000 (including dividend distribution tax).
- (8) Bank Loan repaid during the year ₹ 2,05,000 (included interest ₹ 5,000)
- (9) Trade Payables on 31st March, 2018 were ₹ 50,000 and on 31st March, 2019 were ₹ 35,000.
- (10) Amount paid to Trade payables during the year ₹ 6,10,000
- (11) Income Tax paid during the year amounts to ₹ 55,000 (Provision for taxation as on 31st March, 2019 ₹ 30,000).
- (12) Investments of ₹ 8,20,000 sold during the year at a profit of ₹ 20,000.
- (13) Depreciation on furniture amounts to ₹ 40,000.
- (14) Depreciation on other tangible assets amounts to ₹ 20,000.
- (15) Plant and Machinery purchased on 15th November, 2018 for ₹ 3,50,000.
- (16) On 31st March, 2019 ₹ 2,00,000, 7% Debentures were issued at face value in an exchange for a plant.
- (17) Cash and Cash equivalents on 31st March, 2018 ₹ 2,25,000.

Prepare cash flow statement for the year ended 31st March, 2019, using direct method & Calculate cash flow from operating activities, using indirect method.

Solution :

Cash Flow Statement for the year ended 31st March, 2019 (Using direct method)

Particulars	₹	₹
<i>Cash flows from Operating Activities</i>		
Cash sales (₹ 3,75,000/25%)		15,00,000
Less: Cash payments for trade payables	(6,10,000)	
Wages Paid	(5,55,000)	
Office and selling expenses ₹ (35,000 + 15,000)	(50,000)	(12,15,000)
<i>Cash generated from operations before taxes</i>		2,85,000
Income tax paid		(55,000)
<i>Net cash generated from operating activities (A)</i>		2,30,000
<i>Cash flows from Investing activities</i>		
Sale of investments ₹ (8,20,000 + 20,000)	8,40,000	
Payments for purchase of Plant & machinery	(3,50,000)	
<i>Net cash used in investing activities (B)</i>		4,90,000
<i>Cash flows from financing activities</i>		
Bank loan repayment (including interest)	(2,05,000)	
Dividend paid (including dividend distribution tax)	(40,000)	
<i>Net cash used in financing activities (C)</i>		(2,45,000)
<i>Net increase in cash (A+B+C)</i>		4,75,000
<i>Cash and cash equivalents at beginning of the period</i>		2,25,000
<i>Cash and cash equivalents at end of the period</i>		7,00,000

Cash Flow from Operating Activities' by indirect method

		₹
Net Profit for the year before tax and extraordinary items		2,80,000
Add: Non-Cash and Non-Operating Expenses:		
Depreciation		60,000
Interest Paid		5,000
Less: Non-Cash and Non-Operating Incomes:		
Profit on Sale of Investments		(20,000)
Net Profit after Adjustment for Non-Cash Items		3,25,000
Less: Decrease in trade payables	15,000	
Increase in inventory	<u>25,000</u>	(40,000)
Cash generated from operations before taxes		2,85,000

Working Note:

Calculation of net profit earned during the year

	₹	₹
Gross profit		3,75,000
Less: Office expenses, selling expenses	50,000	
Depreciation	60,000	
Interest paid		(1,15,000)
	<u>5,000</u>	2,60,000
Add: Profit on sale of investments		20,000
Net profit before tax		2,80,000

Question 6

Following information was extracted from the books of S Ltd. for the year ended 31st March, 2020 :

- (1) Net profit before taking into account income tax and after taking into account the following items was ₹30 lakhs;
 - (i) Depreciation on Property, Plant & Equipment ₹7,00,000
 - (ii) Discount on issue of debentures written off ₹45,000.
 - (iii) Interest on debentures paid ₹4,35,000
 - (iv) Investment of Book value ₹3,50,000 sold for ₹3,75,000.
 - (v) Interest received on Investments ₹70,000
- (2) Income tax paid during the year ₹ 12,80,000
- (3) Company issued 60,000 Equity Shares of ₹10 each at a premium of 20% on 10th April, 2019.
- (4) 20,000, 9% Preference Shares of ₹100 each were redeemed on 31st March, 2020 at a premium of 5%
- (5) Dividend paid during the year amounted to ₹11 Lakhs (including dividend distribution tax)
- (6) A new Plant costing ₹7 Lakhs was purchased in part exchange of an old plant on 1st January, 2020. The book value of the old plant was ₹8 Lakhs but the vendor took over the old plant at a value of ₹6 Lakhs only. The balance amount was paid to vendor through cheque on 30th March, 2020.
- (7) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31.03.2020 was ₹ 14,76,000.

The inventory on 31.03.2019 was correctly valued at ₹ 13,50,000.

- (8) Current Assets and Current Liabilities in the beginning and at the end of year 2019-2020 were as:

	As on 1 st April, 2019 (₹)	As on 31 st March, 2020 (₹)
Inventory	13,50,000	14,76,000

Trade Receivables	3,27,000	3,13,200
Cash & Bank Balances	2,40,700	3,70,500
Trade Payables	2,84,700	2,87,300
Outstanding Expenses	97,000	1,01,400

You are required to prepare a Cash Flow Statement for the year ended 31st March, 2020 as per AS 3 (revised) using the indirect method.

Solution :

S Ltd.

Cash Flow Statement for the year ended 31st March, 2020

	₹	₹
<i>Cash flows from operating activities</i>		
Net profit before taxation*		30,00,000
Adjustments for:		
Depreciation on PPE	7,00,000	
Discount on debentures	45,000	
Profit on sale of investments	(25,000)	
Interest income on investments	(70,000)	
Interest on debentures	4,35,000	
Stock adjustment	1,64,000	
{14,76,000 less 16,40,000(14,76,000/90X100)}		
Operating profit before working capital changes		12,49,000
Changes in working capital (Excluding cash and bank balance):		42,49,000
Less: Increase in inventory	(2,90,000)	
{16,40,000(14,76,000/90X100) less 13,50,000}		
Add: Decrease in Trade receivables	13,800	

Increase in trade payables	2,600	
Increase in o/s expenses	4,400	(2,69,200)
Cash generated from operations		39,79,800
Less: Income taxes paid		(12,80,000)
Net cash generated from operating activities		26,99,800
Cash flows from investing activities		
Sale of investments	3,75,000	
Interest received	70,000	
Payments for purchase of fixed assets (7,00,000 – 6,00,000)	(1,00,000)	
Net cash used in investing activities		3,45,000
Cash flows from financing activities		
Redemption of Preference shares	(21,00,000)	
Issue of shares	7,20,000	
Interest paid	(4,35,000)	
Dividend paid	(11,00,000)	
Net cash used in financing activities		(29,15,000)
Net increase in cash		1,29,800
Cash at beginning of the period		2,40,700
Cash at end of the period		3,70,500

*Net profit given in the question is after considering only the items listed as information point (1) of the question ; hence amount of loss on plant not added back.

Question 7

The balance sheets of Sun Ltd. as at 31st March 2011 and 2010 were as:

	Particulars	Notes	2011 (₹)	2010 (₹)
	Equity and Liabilities			
1	Shareholder's funds			
	(a) Share capital	1	60,000	50,000
	(b) Reserve & surplus	2	5,000	4,000
2	Current liabilities			
	(a) Trade Payables		4,000	2,500
	(b) Other current liabilities	3	-	1,000
	(c) Short term provision (provision for tax)		1,500	1,000
	Total		70,500	58,500
	Assets			
1	Non-current assets			
	(a) Property, Plant & Equipment	4	39,500	29,000
2	Current assets			
	(a) Current investments		2,000	1,000
	(b) Inventories		17,000	14,000
	(c) Trade receivables		8,000	6,000
	(d) Cash & cash equivalents	5	4,000	8,500
			70,500	58,500

Notes to accounts

	2011 (₹)	2010 (₹)
1 Share Capital		
Equity Shares of ₹10 each	<u>60,000</u>	<u>50,000</u>
2 Reserve & surplus		
Profit and Loss Account	<u>5,000</u>	<u>4,000</u>
3 Other current liabilities		
Dividend Payable	<u>-</u>	<u>1,000</u>
4 Property, plant and equipment (at WDV)		
Building	10,000	10,000
Fixtures	17,000	11,000
Vehicles	<u>12,500</u>	<u>8,000</u>
Total	<u>39,500</u>	<u>29,000</u>
5 Cash and cash equivalents		
Cash and Bank	4,000	8,500

The profit and loss statement for the year ended 31st March, 2011 disclosed:

Particulars	₹
Profit Before Tax	4,500
Tax Expense: Current tax	<u>(1,500)</u>
Profit for the year	3,000
Declared Dividend	<u>(2,000)</u>
Retained Profit	1,000

Further information is available:

	Fixtures (₹)	Vehicles (₹)
Depreciation for the year	1,000	2,500
Disposals:		
Proceeds on disposal of vehicles	—	1,700
Written down value	—	(1,000)
Profit on disposal		700

Prepare a Cash Flow Statement for the year ended 31st March, 2011.

Solution

Sun Ltd.

Cash Flow Statement

for the year ended 31st March, 2011

	₹	₹
Cash flows from operating activities		
Net Profit before taxation	4,500	
Adjustments for:		
Depreciation	3,500	
Profit on sale of vehicles (1,700 - 1,000)	(700)	
Operating profit before working capital changes	7,300	
Increase in Trade receivables	(2,000)	
Increase in inventories	(3,000)	
Increase in Trade payables	1,500	
Cash generated from operations	3,800	
Income taxes paid (W.N.I)	(1,000)	
Net cash generated from operating activities		2,800
Cash flows from investing activities		

Sale of vehicles	1,700	
Purchase of current investments	(1,000)	
Purchase of vehicles (W.N.3)	(8,000)	
Purchase of fixtures (W.N.3)	(7,000)	
Net cash used in investing activities		(14,300)
Cash flows from financing activities		
Issue of shares for cash	10,000	
Dividends paid (W.N.2)	(3,000)	
Net cash generated from financing activities		<u>7,000</u>
Net decrease in cash and cash equivalents		(4,500)
Cash and cash equivalents at beginning of period (See Note)		8,500
Cash and cash equivalents at end of period (See Note)		4,000
Note to the Cash Flow Statement		
Cash and Cash Equivalents		
	31.3.2011	31.3.2010
Bank and Cash	4,000	8,500
Cash and cash equivalents	4,000	8,500

Working Notes:

		₹
1. Income taxes paid		
Income tax expense for the year		1,500
Add: Income tax liability at the beginning of the year		1,000
		<u>2,500</u>
Less: Income tax liability at the end of the year		(1,500)
		<u>1,000</u>

2. Dividend paid		
Declared dividend for the year		2,000
Add: Amount payable at the beginning of the year		1,000
		3,000
Less: Amount payable at the end of the year		-
		3,000
3. Property, plant and equipment acquisitions		
	Fixtures	Vehicles
	₹	₹
W.D.V. at 31.3.2011	17,000	12,500
Add back:		
Depreciation for the year	1,000	2,500
Disposals	—	1,000
	18,000	16,000
Less: W.D.V. at 31.12.2010	(11,000)	(8,000)
Acquisitions during 2010-2011	7,000	8,000

Note: Current investments may not be readily convertible to a known amount of cash and may not be subject to an insignificant risk of changes in value as per the requirements of AS 3 and hence those have been considered as investing activities.

Accounts of Banking Company

The main business of a banking company is to earn interest by giving Advances and to accept Deposits.

Types of Deposits accepted:

- a. Current Account Deposits
- b. Savings Account Deposits
- c. Fixed Deposits (including Recurring Deposits)

Types of Advances:

- a. Term Loan
- b. Bills Discounted
- c. Cash credit, bank overdraft and demand loan

REBATE ON BILLS DISCOUNTED

- a. When the bills are discounted by the bank, the entire amount of discount is credited to the Interest and Discount account.

Bill Discounted A/c Dr

To Cash A/c

To Interest and Discount A/c

- b. Some of those bills may fall due for maturity after the close of the year. So, the unexpired portion of such discount is carried forward to the next year by the following entry.

Interest and Discount A/c Dr
To Rebate on Bills discounted A/c

Balance of the rebate account is to be shown in the Balance Sheet under the head of Other Liabilities.

- c. *At the beginning of next accounting year, such rebate will be closed by transferring to Interest and discount account. So, for the balance of Rebate account brought forward from last year is to be considered as income of this year and the entry will be*

Rebate on Bills Discount A/c Dr
To Interest and Discount

Note: *The due date will be included in calculating the number of days unexpired on bill discounted.*

Question 1

Calculate Rebate on Bills discounted as on 31 December, 2011 from the following data and show journal entries:

	Date of Bill	₹	Period	Rate of Discount
(i)	15.10.11	25,000	5 months	8%
(ii)	10.11.11	15,000	4 months	7%
(iii)	25.11.11	20,000	4 months	7%
(iv)	20.12.11	30,000	3 months	9%

Solution

Calculation of Rebate on Bills Discounted

₹	Due Date	Days after 31 December 2011	Discount Rate	₹
25,000	18-03-2012	$31 + 28 + 18 = 77$	8%	421.92
15,000	13-03-2012	$31 + 28 + 13 = 72$	7%	207.12
20,000	28-03-2012	$31 + 28 + 28 = 87$	7%	333.69
30,000	23-03-2012	$31 + 28 + 23 = 82$	9%	606.57
		Total		1569.30

Journal Entry

Date	Particulars	Debit ₹	Credit ₹
Dec. 31	Interest and Discount Account Dr. To Rebate on Bills Discounted (Being the provision for unexpired discount required at the end of the year)	1569.30	1569.30

Question 2

The following information is available in the books of X Bank Limited as on 31st March, 2012:

	₹
Bills discounted	1,37,05,000
Rebate on Bills discounted (as on 1.4.2011)	2,21,600
Discount received	10,56,650

Details of bills discounted are as follows:

Value of bill (₹)	Due date	Rate of Discount
18,25,000	5.6.2012	12%
50,00,000	12.6.2012	12%
28,20,000	25.6.2012	14%
40,60,000	6.7.2012	16%

Calculate the rebate on bills discounted as on 31.3.2012 and give necessary journal entries.

Solution

Statement showing rebate on bills discounted

Value	Due Date	Days after 31.3.2012	Rate of discount	Discount Amount
18,25,000	5.6.2012	$(30 + 31 + 5) = 66$	12%	39,600
50,00,000	12.6.2012	$(30 + 31 + 12) = 73$	12%	1,20,000
28,20,000	25.6.2012	$(30 + 31 + 25) = 86$	14%	93,021
40,60,000	6.7.2012	$(30 + 31 + 30 + 6) = 97$	16%	1,72,633
1,37,05,000	Rebate on bills discounted on 31.3.2012			4,25,254

In the books of X Bank Ltd.

Journal Entries

(i)	Rebate on bills discounted Account	Dr.	2,21,600	
	To Discount on bills Account			2,21,600
	[Being opening balance of rebate on bills discounted account transferred to discount on bills account]			
(ii)	Discount on bills Account	Dr.	4,25,254	
	To Rebate on bills discounted Account			4,25,254
	[Being provision made on 31 st March, 2012]			

<i>(iii)</i>	<i>Discount on bills Account</i>	<i>Dr.</i>	<i>8,52,996</i>	
	<i>To Profit and loss Account</i>			<i>8,52,996</i>
	<i>[Being transfer of discount on bills, of the year, to profit and loss account]</i>			

*Credit to Profit and Loss A/c will be as follows: ₹ (10,56,650 + 2,21,600 - 4,25,254)
= ₹8,52,996*

NON PERFORMING ASSETS:

NPA are those advances on which interest or installment remain unpaid for a period of 90 days.

Rates of Provisioning for Non-Performing Assets.

1. Standard assets: *0.25% of the outstanding amount if the loan is given to agricultural sector and SME sector enterprises 0.4% of the outstanding amount if the loan is given to other sector enterprises.*

2. Sub-Standard Advances: *15 per cent of the outstanding amount. The "unsecured exposures" will attract 25 per cent. But if the unsecured exposure is in infrastructure sector where escrow accounts are available, the provision will be 20%.*

3. Doubtful Advances: *Doubtful Advances will continue to attract 100% provision to the extent the advance is not covered by the realizable value of the security.*

(i) The secured portion of advances which have remained in "doubtful" category up to one year will attract a provision of 25 per cent;

- (ii) The secured portion of advances which have remained in "doubtful" category for more than one year but upto 3 years will attract a provision of 40 per cent; and
- (iii) The secured portion of advances which have remained in "doubtful" category for more than 3 years will continue to attract a provision of 100%

4. **Loss Assets:** 100% of the outstanding amount.

Question 3

From the following information, find out the amount of provisions to be shown in the Profit and Loss Account of AG bank.

	₹ in lakhs
Assets	
Standard	5000
Sub-standard	4000
Doubtful : for one year	800
: for three years	600
: for more than three years	<u>200</u>
Loss Assets	1000

Solution

Computation of provisions for AG Bank

Assets	Amount ₹ in lakhs	% of provision	Provision ₹ in lakhs
Standard	50,00	0.4	20
Substandard*	40,00	15	600
Doubtful for one year*	8,00	25	200
Doubtful for three years*	6,00	40	240
Doubtful for more than three years	2,00	100	200

Loss	10,00	100	1,000
Total Provision required			2,260

*All the marked sub-standard and doubtful assets are assumed as fully secured.

Question 4

From the following information of AY Limited, compute the provisions to be made in the Profit and Loss account:

	₹ in lakhs
Assets	
Standard	20,000
Substandard	16,000
Doubtful	
For one year (secured)	6,000
For two years and three years (secured)	4,000
For more than three years (secured by mortgage of plant and machinery ₹600 lakhs)	2,000
Loss Assets	1,500

Solution

Calculation of amount of provision to be made in the Profit and Loss Account

Classification of Assets	Amount of Advances	% age of provision	Amount of provision
	(₹ in lakhs)		(₹ in lakhs)
Standard assets	20,000	0.40	80
Sub-standard assets	16,000	15	2,400
Doubtful assets:			
For one year (secured)	6,000	25	1,500
For two to three years (secured)	4,000	40	1,600
For more than three years (unsecured)	1,400	100	1,400

(secured)	600	100	600
Non-recoverable assets (Loss assets)	1,500	100	<u>1,500</u>
Total provision required			<u>9,080</u>

Provision when DICGC/ECGC coverage is there on advances:

When DICGC/ECGC coverage is there then first we have to deduct the realizable value of securities held from the outstanding balance. Then we have to deduct the DICGC/ECGC coverage from the net figure which will give us the unsecured portion. On the balance amount we have to make provisions as discussed above. However, when the provision on secured portion is made, a deduction is made on DICGC/ECGC guarantee at the specified percentage.

Amount outstanding	xxx
Less: Realizable value of securities held	<u>xxx</u>
	xxx
Less: Realizable value of securities held	<u>xxx</u>
Balance	xxx
Provision required:	
On unsecured portion (full figure of balance i.e., 100%)	xxx
On secured portion :	<u>xxx</u>
Total provision	xxx

Question 5

Outstanding Balance	₹4 lakhs
ECGC Cover	50%
Period for which the advance has remained doubtful	More than 3 years remained doubtful (as on March 31, 2011)
Value of security held	₹1.50 lakhs

You are required to calculate provisions.

Solution

Provision required to be made as on 31.03.2011

Outstanding balance	₹4.00 lakhs
Less: Value of security held (Secured Portion)	<u>(₹1.50 lakhs)</u>
Unrealised balance	₹2.50 lakhs
Less: ECGC Cover (50% of unrealizable balance)	<u>(₹1.25 lakhs)</u>
Net unsecured balance	<u>₹1.25 lakhs</u>
Provision for unsecured portion of advance	₹1.25 lakhs (@ 100% of unsecured portion)
Provision for secured portion of advance	<u>₹1.50 lakhs</u> (@ 100% of the secured portion as advance has remained doubtful for over 3 years)
Total provision to be made	<u>₹ 2.75 lakhs</u>

Question 6

Outstanding Balance	₹4 lakhs
ECGC Cover	50%
Period for which the advance has remained doubtful	More than 3 years remained doubtful (as on March 31, 2011)
Value of security held (realizable value only 80%)	₹ 1.50 lakhs

You are required to calculate provisions as per applicable rates.

Solution

Provision required to be made as on 31.03.2011

Outstanding balance	₹4.00 lakhs
Less: Value of security held (80% of 1.5 lacs)	<u>(₹1.20 lakhs)</u>
Unrealized balance	₹2.80 lakhs
Less: ECGC Cover (50% of unrealizable balance)	<u>(₹1.40 lakhs)</u>
Net unsecured balance	₹1.40 lakhs
Provision for unsecured portion of advance	₹1.40 lakhs (@ 100% of unsecured portion)
Provision for secured portion of advance	<u>₹1.20 lakhs (@ 100% of the secured portion)</u>
Total provision to be made	₹ 2.60 lakhs

Bills for collection

When a bank accepts a bill for collection it has to pass the following entry in its books.

Bills for collection (Assets)	Dr.		
To Bills for collection (Liability)			

Similarly, when such bills are collected or dishonoured and returned it passes the reverse entry. So, the balance in both the account has to be equal at all the time.

Question 7

On 01.04.2011 bills for collection was 7 lacs. During 2011-12 bills received for collection amounted to 64.5 lacs. Bills collected were 47 lacs. Bills dishonoured was 5.5 lacs. Prepare Bills for collection (Assets) and Bills for Collection (Liabilities) Accounts.

Solution

Bills for Collection (Assets) Account

	₹ in lacs		₹ in lacs
To Balance b/d	7	By Bills for collection	47
To Bills for collection	64.5	By Bills dishonoured	5.5
		By Balance c/d	19
	71.5		71.5

Bills for Collection (Liabilities)

Account

	₹ in lacs		₹ in lacs
To Bills for collection	47	By Balance b/d	7
To Bills dishonoured	5.5	By Bills for collection	64.5
To Balance c/d	19		
	71.5		71.5

Acceptances and Endorsement

The bank also undertakes a liability towards its customers who agrees to pay after the bank accepts the bill. Against this liability the bank has a claim against the customer on whose behalf it has undertaken the liability.

For accepting the liability, the bank passes the following entry

<i>Constituents liability for acceptances & endorsements</i>	<i>Dr.</i>		
<i>To Acceptances & Endorsements</i>			

On honouring the acceptance by the bank, paying off by the client and even on failure of client to pay the bank has to pass the reverse entry.

But on failure of client to pay or on honouring the acceptance the bank debit the client account maintained by it. The bank also asks for the security for the above from the client.

Question 8

From the following details prepare “Acceptances, Endorsements and other Obligation A/c” as would appear in the General Ledger.

On 1.4.2011 Acceptances not yet satisfied stood at ₹22,30,000. Out of which ₹20 lacs were subsequently paid off by clients and bank had to honour the rest. A scrutiny of the Acceptance Register (for transactions during the year) revealed the following:

Client Acceptances/Guarantees Remarks:

	₹	
<i>A</i>	<i>10,00,000</i>	<i>Bank honoured on 10.6.2011</i>
<i>B</i>	<i>12,00,000</i>	<i>Party paid off on 30.9. 2011</i>
<i>C</i>	<i>5,00,000</i>	<i>Party failed to pay and bank had to honour on 30.11.2011</i>
<i>D</i>	<i>8,00,000</i>	<i>Not satisfied upto 31.3.2012</i>
<i>E</i>	<i>5,00,000</i>	<i>-do-</i>
<i>F</i>	<i>2,70,000</i>	<i>-do-</i>
<i>Total</i>	<i>42,70,000</i>	

Solution

Acceptances, Endorsements and other Obligation Account (in general ledger)

		₹ '000			₹ '000
2011-12	To Constituents' liabilities for acceptances/ guarantees etc. (Paid off by clients)	20,00	1.4.11	By Balance b/d	22,30
	To Constituent's liabilities for acceptances/ guarantees etc. (Honoured by bank ₹22.30 lakhs less ₹20 lakhs)	2,30	2011-12	By Constituents' liabilities for	
				A 10,00	
				B 12,00	
				C	
				5,00	
				D	
				8,00	
				E	42,70
				5,00	
				F	
				<u>2,70</u>	
10.6.2011	To Constituents' liabilities for acceptances/ guarantees etc. (Honoured by bank)	10,00			
30.9.2011	To Constituents' liabilities for acceptances/ guarantees etc. (Paid off by party)	12,00			
30.11.2011	To Constituent's liabilities for acceptances/ guarantees etc. (honoured by bank on party's failure to pay)				

31.3.2012	To Balance c/d	5,00		
	(Acceptances not yet satisfied)	15,70		
		65,00		65,00

FORMAT OF BALANCE SHEET

<i>Balance Sheet of..... as on 31st March.....(Year)</i>			
CAPITAL & LIABILITIES	SCHEDULE NO.	AS ON 31.3. (Current Yr.)	AS ON 31.3 (Prev. Yr.)
Capital	1		
Reserve & Surplus	2		
Deposits	3		
Borrowings	4		
Other Liabilities & Prov.	5		
TOTAL			
ASSETS			
Cash & balances with RBI	6		
Balances with banks & money at call and short notices	7		
Investments	8		
Advances	9		
Fixed Assets	10		
Other Assets	11		
TOTAL			
Contingent Liabilities	12		
Bills for Collection			

FORMAT OF PROFIT & LOSS ACCOUNT FOR THE YEAR ENDED 31ST MARCH

	SCHEDULE NO.	AS ON 31.3. (Current Yr.)	AS ON 31.3 (Prev. Yr.)
I. INCOME			
Interest earned	13		
Other Income	14		
TOTAL			
II. EXPENDITURE			
Interest Expended	15		
Operating Expenses	16		
Provision & contingencies			
TOTAL			
III. PROFIT/LOSS			
Net Profit/Loss(-) for the year			
Profit/Loss(-) brought forward			
TOTAL			
IV. APPROPRIATIONS			
Transfer to Statutory Reserve			
Transfer to Other Reserve			
Transfer to Government/Proposed Dividend			
Balance Carried over to Balance Sheet			
TOTAL			

SCHEDULE I – CAPITAL

Authorised Capital	(Various items can be grouped in accordance with convenience.)
.....Shares of ₹.... each.	
Issued Capital	
.....Shares of ₹.... each.	
Subscribed Capital	
.....Shares of ₹.... each.	
Called-up Capital	
.....Shares of ₹.... each.	
Less: Calls unpaid	

Add: Forfeited Shares	
-----------------------	--

SCHEDULE 2 RESERVES & SURPLUS

I. STATUTORY RESERVES	
Opening Balance	
Addition during the year	
Deductions during the year	
II. CAPITAL RESERVES	
Opening Balance	
Addition during the year	
Deductions during the year	
III. SHARE PREMIUM	
Opening Balance	
Addition during the year	
Deductions during the year	
IV. REVENUE AND OTHER RESERVES	This reserve shall not include Provision for depreciation or renewal of assets or for a known liability.
Opening Balance	
Addition during the year	
Deductions during the year	
V. BALANCE IN PROFIT & LOSS ACCOUNT	
TOTAL (I+II+ III + IV + V)	

SCHEDULE 3 - DEPOSITS

I. DEMAND DEPOSITS	It includes credit balance in O/D & C/C A/cs, Overdue deposits & Matured term deposits
(i) From Banks	
(ii) From Others	
II. SAVINGS BANK DEPOSITS	
III. TERM DEPOSITS	It includes cumulative and recurring deposits and ordinary staff deposits.
(i) From Banks	
(ii) From Others	
TOTAL (I + II III)	

Notes: Interest accrued shall be included with deposits but Interest accrued but not due shall be shown under Other Liabilities

SCHEDULE 4 BORROWINGS

I. BORROWINGS IN INDIA
Reserve Bank of India
Other Banks
Other Institutions & Agencies
II. BORROWINGS OUTSIDE INDIA
TOTAL (I +II)

SCHEDULE 5- OTHER LIABILITIES & PROVISIONS

I. Bills Payable
II. Inter-office adjustments (net)
III. Interest Accrued but not due
IV. Others (including provisions) This item shall include
PFT less TDS/Advance tax
Proposed dividend
Unclaimed dividend
Rebate on bills discounted
Outstanding expenses
Staff security deposits
TOTAL

SCHEDULE 6 - CASH & BALANCES WITH RESERVE BANK OF INDIA

I. CASH IN HAND
(including foreign currency notes)
II. BALANCES WITH RBI
(i) in Current Account
(ii) in Other Accounts
TOTAL (I + II)

SCHEDULE 7- BALANCES WITH BANKS & MONEY AT CALL & SHORT NOTICES

I. IN INDIA	
(i) Balances with banks	
(a) In Current Account	
(b) In Other Deposit A/c.	
(ii) Money at call and short notices	It includes deposits repayable within 15 days' notice lent in inter-bank call money market
(a) With banks	
(b) With Other Institution	
TOTAL	
II. OUTSIDE INDIA	
(i) In Current Account	
(ii) In Other Deposit Account	
(iii) Money at call and short notices	
TOTAL	
GRAND TOTAL (I + II)	

SCHEDULE 8 – INVESTMENTS

I. INVESTMENTS IN INDIA	
(i) Government Securities	
(ii) Other approved Securities	
(iii) Shares	
(iv) Debentures & Bonds	
(v) Subsidiaries and/or joint venture	
(vi) Others (to be specified)	Inv. in gold, silver and commercial paper are shown here.
TOTAL	
II. INVESTMENTS OUTSIDE INDIA	
(i) Govt. securities (incl. local authority)	
(ii) Subsidiaries and/or joint venture	
(iii) Others (to be specified)	
TOTAL	
GRAND TOTAL (I + II)	

SCHEDULE 9 – ADVANCES

A. (i) Bills purchased and discounted	Advances less provisions shall be shown here. But on standard assets provisions shall not be deducted rather shown with other liabilities.
(ii) Cash credits, overdrafts and loans repayable on demand	
(iii) Term Loans	
TOTAL	
B. (i) Secured by tangible assets	
(ii) Covered by Bank/Government guarantees Includes DICGC coverage	
(iii) Unsecured	
TOTAL	
C.I. ADVANCES IN INDIA	
(i) Priority Sectors	
(ii) Public Sector	
(iii) Banks	
(iv) Others	
TOTAL	
II. ADVANCES OUTSIDE INDIA	
(i) Due From Banks	
(ii) Due From Others	
(a) Bills purchased & discounted	
(b) Others	
TOTAL	
GRAND TOTAL (C.I + C.II)	

SCHEDULE 10 FIXED ASSETS

I. PREMISES	
At cost as on 31 st March of the prec. year.	
Additions during the year	
Deductions during the year	
Depreciation to date	
II. OTHER FIXED ASSETS (INCLUDING FURNITURE & FIXTURES)	

<i>At cost as on 31st March of the prec. year.</i>	<i>Motor vehicles and other FA are shown here</i>
<i>Additions during the year</i>	
<i>Deductions during the year</i>	
<i>Depreciation to date</i>	
TOTAL (I + II)	

SCHEDULE II- OTHER ASSETS

<i>I. Inter-Office adjustments</i>	<i>(net)</i>
<i>If Dr. balance</i>	
<i>II. Interest Accrue</i>	<i>(Int. due on inv. & int. accrued but not due on both inv. & adv. are shown here.)</i>
<i>III. Tax paid in advance/T.D.S</i>	<i>(In excess of PFT)</i>
<i>IV. Stationery and Stamps</i>	
<i>V. Non-banking assets acquired in satisfaction of claims</i>	
<i>VI. Others</i>	<i>Prepaid Expenses/ Staff Adv. & other accrued incomes are to be included here.</i>
TOTAL	

SCHEDULE 12 - CONTINGENT LIABILITIES

<i>I. Claims against the bank not acknowledged as debts</i>	
<i>II. Liability for partly paid investments</i>	
<i>III. Guarantees given on behalf of customers</i>	
<i>(a) In India</i>	
<i>(b) Outside India</i>	
<i>IV. Acceptances, endorsements and, other obligations</i>	
<i>V. Others items for which the bank is contingently liable</i>	<i>(Arrears of Preference dividend is shown here.)</i>
TOTAL	

SCHEDULE 13 - INTEREST EARNED

I. Interest/discount on advances/bills
II. Income on investments
III. Interest on balances with RBI and other inter-bank funds
IV. Others
TOTAL

SCHEDULE 14 - OTHER INCOME

I. Commission, exchange and brokerage rent.)	(includes locker rent.)
II. Profit on sale of investments	
Less: Loss on sale of investments	
III. Profit on revaluation of investments	
Less : Loss on revaluation of investments	
IV. Profit on sale of land, buildings and other assets	
Less : Loss on sale of land, buildings and other assets	
V. Profit on exchange transactions	
Less: Loss on exchange transactions	
VI. Income earned by way of dividends etc. from subsidiaries/companies	
VII. Miscellaneous Income	
TOTAL	

Note: Under items II to V loss figures may be shown in brackets

SCHEDULE 15 - INTEREST EXPENDED

I. Interest on deposits
II. Interest on Reserve Bank of India/ Inter-bank borrowings
III. Others
TOTAL

SCHEDULE 16 - OPERATING EXPENSES

<i>I. Payments to and provisions for employees</i>
<i>II. Rent, taxes and lighting</i>
<i>III. Printing and Stationery</i>
<i>IV. Advertisement and publicity</i>
<i>V. Depreciation on bank's property</i>
<i>VI. Director's fees, allowances and expenses</i>
<i>VII. Auditor's fees and expenses (including branch auditor's fees and expenses)</i>
<i>VIII. Law Charges</i>
<i>IX. Postages, telegrams, telephones, etc.</i>
<i>X. Repairs and maintenance</i>
<i>XI. Insurance</i>
<i>XII. Other Expenditure</i>
<i>TOTAL</i>

CRR-Cash Reserve Ratio:

CRR is to be maintained at 4.5% of Total Time and Demand Liabilities. Total Time and Demand Liabilities means Total Deposits.

SLR-Statutory Liquidity Ratio:

SLR is to be maintained at 18% of Total Deposits. Liquid Assets include

- a) Cash in hand*
- b) Cash with other banks*
- c) Gold*
- d) Government securities*
- e) Money at call*

Notes:

- 1. The bank has to transfer at least 25% of its annual profits to the statutory reserve. (if nothing is mentioned take 25%)*
- 2. A bank does not accrue interest on NPA. Interests on these assets are credited as income on receipt basis only.*

Accounts of Electricity Company

Electricity Act, 2003

This Act replaced the following 3 Acts:

- a. Indian Electricity Act, 1910*
- b. Electricity (Supply) Act, 1948*
- c. Electricity Regulatory Commission Act, 1998*

Features of Electricity Act, 2003 are:

- a. Separately recognised different activities of Power generation, transmission and distribution*
- b. De-licensing of Power generation except in few cases.*
- c. Minimum 10% of power generation through Renewable sources of energy like wind energy.*

Security Deposit

Distribution licensee (Electricity company) requires consumers to deposit security against the amount payable by them for electricity supplied. This security deposit is refundable to consumers on their demand. Also, interest is payable on such deposit.

Accounting of security deposit is done as follows:

- a. When security deposit is received from the consumer:*

Bank A/c Dr

To Security deposit A/c

b. When interest is accrued on such security deposit

Interst expense A/c Dr

To Accrued interest A/c (Liability)

c. For adjusting accrued interest with sales

Accrued interest A/c Dr

To Sales turnover A/c

Service Line Cum Development Charges (SLD Charges)

It is a non refundable receipt of Capital nature. There are 4 suggested Accounting Practices of SLD charges.

Accounting Practice 1

Treat as Liability and transfer proportionate amount to P/L A/c as income over the life of asset.

Accounting Practice 2

Treat as Reserve and not as liability as it is not refundable. No amount is transferred to P/L A/c.

Accounting Practice 3

Treat as Capital Reserve and transfer proportionate amount to P/L A/c as income in proportion to the depreciation.

Accounting Practice 4

Deduct from Non-current asset. Calculate depreciation on reduced amount of asset.

Grant received from Accelerated Power Development and Reforms Programme (APDRP)

Grant received under APDRP is a receipt of capital nature for Capital expenditures to be incurred by the Electricity Companies. In cash flow statement it is shown as financing activity.

Amount proportionate to Depreciation is transferred to Profit and Loss A/c as Income and balance is shown as Capital Reserve under Reserves & Surplus.

Accounting for Depreciation

Central electricity regulatory commission (CERC) prescribes the method for calculating depreciation under Regulation 21 for the purpose of calculating tariff. C&AG suggested that Electricity companies should follow the methods of depreciation as prescribed by CERC instead of Companies Act, 2013.

CERC prescribes 2 methods of depreciation:

- a. Straight line method
- b. Optimised depreciated replacement cost

Depreciation is always calculated on average cost. Average cost is calculated by dividing opening cost and closing cost.

Return on Equity

Average Capital cost = (Opening capital cost + Closing capital cost) / 2

Debt is 70% of Average capital cost.

Equity only 30 % of the Average capital cost.

So, Debt Equity Ratio is 70:30

Rate of Return on Equity is to be considered as given in the Question.

Accounts of Insurance Company

Applicable guidance on Business of an Insurance Companies

- a. Insurance Act, 1938
- b. IRDA (Insurance Regulatory Development Authority) Regulations

Types of Insurance business

- a. General Insurance
- b. Life Insurance

Financial Statements are prepared separately for Life Insurance business and General Insurance Business.

Types of General Insurance

- a. Marine Insurance
- b. Fire Insurance
- c. Miscellaneous (Burglary, Loss of Stock, Loss of Profit etc.)

Components of Financial Statements of General Insurance Business

- a. Revenue Account
- b. Profit and Loss Account
- c. Balance Sheet

Revenue Account is prepared separately for Marine, Fire and Miscellaneous Insurance Business.

In total there are 15 Schedules in Financial Statements of General Insurance Business:

- a. Revenue Account – Schedule 1 to 4
- b. Profit and Loss Account
- c. Balance Sheet – Schedule 5 to 15

Schedules of Revenue Account are:

- Schedule 1 – Premium Earned (Net)
- Schedule 2 – Claims Incurred (Net)
- Schedule 3 – Commission
- Schedule 4 – Operating Expenses Related to Insurance Business

Unexpired Risk Reserve (Provision for unexpired Risk):

Marine : 100% of Premium earned

Fire: 50% of Premium earned

Miscellaneous: 50% of Premium earned

Journal Entry for Unexpired Risk Reserve (Provision for unexpired Risk)

- a. When opening balance less than required closing balance

Revenue A/c Dr

To Unexpired Risk Reserve A/c

- b. When opening balance more than required closing balance

Unexpired Risk Reserve A/c Dr

To Revenue A/c

Steps of Claim includes:

- Intimation

- *Admitted (After surveying and legal process)*
- *Paid*

*Insurance companies have to account for claims in the year of **Intimation***

Books or Registers maintained by Insurance Companies

- Register of policies*
- Register of Claims*
- Register of licensed insurance agents*

Concept of Re-Insurance

Sometimes Insurance companies transfers risk to another company. Such a company is called ceding company. The ceding company pays the premium to the company accepting the Re-insurance.

Types of Life Insurance

- Whole life policy*
- Endowment policy*

Surrender Value

It is the amount payable by the Insurance company to the policyholders if policy is terminated before its maturity.

Net benefit paid

Claims paid by the Life Insurance companies is called Net benefit paid. It can be made in any of the following 4 ways:

- Claim on death*
- Claim on maturity*

- c. Surrender value
- d. Annuities

Life Assurance Fund

It is the accumulated Profits / Reserves (Revenue receipts – Revenue Expenses) of the Life Insurance companies. Claims are paid out of this fund.

Valuation Balance Sheet

It is a statement prepared to calculate Net Profit (Surplus) available with the Life Insurance companies. It compares the closing balance of “Life Assurance Fund” with “Net Liability” as per actuarial valuation. As per IRDA regulations, Life Insurance companies need to get their valuation of liabilities done from an actuary every 2 years.

Bonus

It is the share of Net Profit (surplus) distributed to policy holders. Life Insurance companies need to allocate 95% of their profits to policy holders. Only 5% is allocated to shareholders. Types of Bonus includes:

- a. Cash bonus : Amount paid in cash to the policy holders as bonus.
- b. Reversionary bonus: Bonus amount is added with sum assured.
- c. Bonus in reduction of premium: Premium amount is reduced by the Bonus amount.
- d. Interim Bonus: Bonus paid between 2 Valuation Balance Sheet dates

Financial Statements of Life Insurance companies

- a. Revenue Account
- b. Profit and Loss Account
- c. Balance Sheet

Revenue Account is prepared separately for Marine, Fire and Miscellaneous Insurance Business.

In total there are 15 Schedules in Financial Statements of General Insurance Business:

- a. Revenue Account – Schedule 1 to 4*
- b. Profit and Loss Account*
- c. Balance Sheet – Schedule 5 to 15*

Bonus Issue and Right Issue

Issue of Bonus Shares means Capitalisation of profits. Bonus is to be declared out of the following profits:

- a. Capital Redemption Reserve*
- b. Capital Reserve (Not Revaluation Reserve) received in Cash.*
- c. Securities Premium Reserve received in cash.*
- d. General Reserve*
- e. Profit & Loss A/c*
- f. Other reserves can also be used if they are not created for specific purpose or for meeting a particular liability or if excess amount of reserve is created than required by Law like Investment Allowance Reserve, Foreign Project Reserve, Hotel Reserve, Shipping Reserve, Development reserve.*

Note:

- a. Only fully paid equity shares can be allotted bonus shares. Reserves can be capitalised to make the partly paid shares as fully paid.*
- b. Convertible debentures are also entitled to equivalent bonus.*
- c. Revaluation reserve can not be used for Bonus issue.*
- d. Authorised capital is suitably increased, if required.*
- e. Disclosure of Bonus Issue is to be given for 5 years.*

Entry for Bonus Issue

Capital Redemption Reserve A/c.....Dr
Security Premium/Capital Reserve A/c.....Dr
Profit / Loss or General Reserve A/c..... .Dr
To Bonus to Shareholder/Bonus Issue
(Being Bonus declared)

Bonus to Shareholder/Bonus Issue.....Dr
 To Equity Share Capital
 (Being Bonus allotted)

Partly paid equity shares are required to be made fully paid.

Option 1

Receive call money

Share Final Call A/c.....Dr
 To Equity Share Capital
 (Being call money due)

+

Bank A/c.....Dr
 To Share Final Call A/c.....
 (Being amount received)

Option 2

Make Bonus Call

Share Final Call A/c.....Dr
 To Equity Share Capital
 (Being Call due)

+

Reserve A/c.....Dr
 To Share Final Call A/c
 (Being bonus call allotted)

Redemption of Preference Shares

Redemption of Preference Shares means paying back the amount of share capital to them.

Journal entries for Redemption of Preference Shares is as follows :-

- a. Preference Share Capital A/c.....Dr*
Premium on Redemption of Preference Shares (POROPS) A/c.....Dr
To Preference Shareholders A/c
(Being Preference Share Capital due for redemption)

- b. Preference Shareholders A/c.....Dr*
To Bank A/c
(Being Amount paid)

Sometimes, Question requires Sale of Investment for redemption. Then Journal Entry for sale of investment is to be passed.

Important Provisions of the Companies Act, 2013 regarding redemption of Preference Shares

At the time of redemption various provisions are to be followed. Section 55 of Companies Act, 2013 deals with Redemption of Preference Shares. The following are the important provisions to be followed while accounting for Redemption:

- No share shall be redeemed unless it is fully paid.*
If Question provides partly paid Preference shares & requires redemption, then
- make final call

- make Preference shares fully paid
- Do redemption

- Premium on redemption is to be met out of the following (In the given Order):
 - General Reserve
 - Profit & Loss A/c

General Reserve A/c / Profit & Loss...Dr
 To Premium on Redemption A/c
(Being Premium on redemption written off)

- Redemption must not result in reduction of capital. It is either through:
 - fresh issue
 - or**
 - out of profits available for dividend (by transferring the nominal value of shares redeemed to CRR)

Preference Share Capital redeemed = Capital Redemption Reserve + Fresh Issue
 Proceeds (without Premium) for the
 purpose of Redemption

- If part of the shares is redeemed out of fresh issue and part out of profits, then:
 - If Fresh Issue is at Par, remaining amount can be transferred to CRR
 - If Fresh issue is at premium, don't consider premium received for calculating the amount to be transferred to CRR.
 - If Fresh issue is at discount, discount is considered for calculating the amount to be transferred to CRR.
- CRR is made from Free Reserves like Profit/Loss, General Reserve, Dividend

Equalisation Reserve

Profit & Loss / General Reserve / Dividend Equalisation Reserve A/c.....Dr
To Capital Redemption Reserve A/c...
(Being CRR created)

- *If the details of preference shareholders are missing, redemption entry will remain same, except the payment entry received for the actual amount unpaid is shown as current liability or other current liability.*

Buyback of Shares

A company may buy back its own shares and other specified securities out of the following three sources.

- 1) Free Reserves*
- 2) Securities Premium*
- 3) Proceeds of fresh issue of shares or other specified securities.*

Free Reserves:

The free reserves for this are any reserve which as per the latest audited balance sheet is free for distribution as dividend and it includes balance in the securities premium account.

Conditions of Buyback

- 1) The shares to be bought back must be fully paid.*
- 2) The amount to be paid on buy back does not exceed 25% of total paid up capital and free reserves of the company (here paid up capital shall include both equity and preference share capital); provided that the buy back in any financial year shall not exceed 25% of its equity paid up capital in that year.*
- 3) That the buy back in any financial year shall not exceed 25% of its equity paid up capital in that year.*
- 4) The ratio of debt (secured and unsecured including current liabilities i.e., proposed dividend, outstanding expenses and provision for tax) is not more than twice the paid up capital and free reserves after such buy back. Here the equity shall be after excluding the CRR transfer amount.*

- 5) *The premium on buy back shall be provided out of securities premium or out of the free reserves of the company.*
- 6) *The company shall extinguish or physically destroy the shares so bought back within seven days of the last day of completion of buy back.*
- 7) *sum equal to the nominal value of shares so purchased shall be transferred to the CRR account out of the Free Reserves.*
- 8) *A special resolution has to be passed and the entire proceeding must be finished within 12 months of the date of passing special resolution. Buy back must be authorized by the articles.*
- 9) *The buyback of shares may be*
 - a) *From the existing shareholders on proportionate basis*
 - b) *From the open market*
 - c) *From odd lots*
 - d) *By purchasing shares issued to employees under stock option or sweat equity.*
- 10) *A company intending to buy back is required to furnish a declaration of solvency after passing the resolution of buy back.*
- 11) *A company shall not make further issue of shares within a period of 6 months from the completion of buy back except by way of buy back except by way of bonus issue, sweat equity, stock option, and conversion of subsisting debentures or preference shares.*

Journal Entries

1. On buy back of shares:

Equity Share Capital A/cDr
Premium on buy back A/cDr
To Bank A/c

2. On writing off premium on buy back

Securities Premium A/cDr
General Reserve A/cDr
Profit & Loss A/cDr
To Premium on buy back A/c

3. On transfer to CRR

Securities Premium A/c.....Dr
General Reserve.....Dr
Profit & Loss A/c.....Dr
To CRR A/c

Employee Stock Option Plans

Guidance Note on Accounting for Employee Share-Based Payments

The Guidance Note recognizes that there are two methods of accounting for employee share-based payments, viz, the fair value method and the intrinsic value method and permits as an alternative the intrinsic value method with fair value disclosures.

Important terminologies

Option: It's a right given to an employee through an ESOP to buy company shares later at a set price.

Grant: This is when the company gives an employee the option to buy shares under an ESOP.

Vesting: Before an employee can use the option, they have to meet certain requirements, like serving a specific time or hitting performance targets.

Vesting Period: The time during which an employee earns the right to use the option.

Exercise: When an employee actually buys the shares through the ESOP.

Exercise Period: The timeframe in which the employee can buy the shares using the option.

Exercise Price: The price the employee has to pay to buy the shares through the ESOP.

Intrinsic Value: *The amount by which the quoted market price of the underlying share in case of a listed enterprise or the value of the underlying share determined by an independent valuer in case of an unlisted enterprise exceeds the exercise price of an option.*

Accounting

For accounting purposes, employee share-based payment plans are classified into the following categories:

- (a) Equity-settled: Under these plans, the employees receive shares.*
- (b) Cash-settled: Under these plans, the employees receive cash based on the price (or value) of the enterprise's shares.*
- (c) Employee share-based payment plans with cash alternatives: Under these plans, either the enterprise or the employee has a choice of whether the enterprise settles the payment in cash or by issue of shares.*

Equity – Settled Employee Share-Based Payment Plans

Recognition

- An enterprise should recognize as an expense (except where service received qualifies to be included as a part of the cost of an asset) the service received in an equity-settled employee share-based payment plan when it receives the services, with a corresponding credit to an appropriate equity account, say, "Stock Options Outstanding Account"*
- An enterprise should measure the fair value shares or stock options granted at the grant date, based on market price. If market price is not available, the enterprise should estimate the fair value of the Instruments granted. (e.g., use of an option pricing model for valuing stock options)*

- *On exercise of the right to obtain shares or stock options, the enterprise issues shares on receipt of the exercise price. The shares so issued should be considered to have been issued at the consideration comprising the exercise price and the corresponding amount standing to the credit of the relevant equity amount (e.g., Stock Options Outstanding Account). In a situation where the right to obtain shares or stock options expires unexercised, the balance standing to the credit of the relevant equity account should be transferred to general reserve.*

Cash-Settled Employee Share-Based Payment Plans

- *An enterprise might grant rights such as stock appreciation rights to employees as part of their remuneration package, whereby the employees will become entitled to a future cash payment (rather than shares), based on the increase in the share price of the enterprise from a specified level over a specified period of time.*
- *An enterprise should recognize as an expense (except where service received qualifies to be included as a part of the cost of an asset) the services received in a cash-settled employee share based payment plan when it receives the services with a corresponding increase in liability by creating a provision therefore.*
- *For cash-settled employee share-based payment plan, the enterprise should measure the services received and the liability incurred at the fair value of the liability. Until the liability settled, the enterprise should re-measure the fair value of the liability at each reporting date and the date of the settlement, with any changes in fair value recognized in profit or loss for the period.*

Graded Vesting

In case the options or shares granted under an employee stock option plan do not vest on one date but have graded vesting schedule, total plan should be segregated into different groups, depending upon the vesting dates. Each of such groups would be having different vesting period and expected life and, therefore, each vesting date should be considered as a separate option grant and evaluated and accounted for accordingly. For example, suppose an employee is granted 100 option which will vest @ 25 options per year at the end of the third, fourth, fifth and sixth years. In such a case, each tranche of 25 options would be evaluated and accounted for separately.

Debentures

Debentures are long term borrowings having fixed financial charges.

Issue of Debentures-----Journal Entries

1. On receipt of debenture application money.

Bank A/c.....Dr

To Debenture Application.....Cr

(Being Debenture Application Received)

2. Debenture Application.....Dr (Amount Received)

Underwriters A/c.....Dr (Short Subscription)

To __ % Debentures A/c (Debenture paid up value)

(Being Debentures Allotted)

3. Underwriters Commission A/c Dr (Commission is on Total Contract Amount)

To Underwriters A/c

(Being underwriter commission made due)

4. Underwriters A/c.....Dr

To Bank A/c

(Being underwriters account paid)

OR

Bank A/c.....Dr

To Underwriter A/c

(Being Amount received)

5. Debenture Interest will also be charged

Debentures Interest A/c.....Dr

To Bank / Debenture Holders A/c

(Being interest charged)

Debenture Holders A/c.....Dr

To Bank A/c

(Being amount paid to debenture holders)

Profit/Loss A/c.....Dr

To Debenture Interest A/c

(Being Interest written off)

Debenture Interest A/c

<i>To Bank</i>	<i>xxx</i>	<i>By Balance b/d (accrued</i>	<i>xxx</i>
<i>To Balance c/d (closing</i>	<i>xxx</i>	<i>interest)</i>	<i>xxx</i>
<i>balance)</i>	xxx	<i>By Profit/Loss A/c (bal. fg.)</i>	xxx

2. Redemption of Debentures

Methods : A company can have following possible redemption methods :

- 1. Lumpsum Redemption (where all debenture holders are settled in full)*
- 2. Installment Method (By Drawing Lots- where few Debenture holders are settled in full)*
- 3. Open Market Operation where Company reduce Debentures by purchasing & cancelling Debentures in open markets.*
- 4. Conversion Method (where redemption is not made in cash rather it is converted into new debentures or shares)*

Note : *Journal entries for lumpsum redemption & by drawing lots redemption are similar.*

Note : Whenever Debentures are redeemed by **any method**, then such Debentures Interest **should always be** settled till date of Redemption.

Journal Entries for Redemption in Lumpsum or By Drawing Lots

1. ___ % Debentures A/c.....Dr
 Premium on Redemption.....Dr
 To Debenture Holders
 (Being Debenture due for Redemption)

2. Debenture Holder A/c.....Dr
 To Bank A/c
 (Being amount paid)

3. Profit & Loss A/c.....Dr
 To Premium on Redemption A/c
 (Being Premium written off)

4. Debenture Interest A/c.....Dr
 To Bank A/c
 (Being interest charged)

5. Profit & Loss A/c.....Dr
 To Debenture Interest A/c.....

Purchase form Open Market:

This is method of Redemption under which companies purchase own Debentures in open market & cancel them (cancel means redeem). Following are benefits :-

1. Redemption at low price is possible.

(Being investment purchased)

- *For sale of Investment – (Any Difference on sale is transferred to Profit/Loss A/c)*

Bank A/c.....Dr

To Debenture Redemption Fund A/c

(Being investment sold)

Note : *Interest earned on Investment is transferred to Profit & Loss A/c.*

4. Conversion of Debentures

Sometimes Companies convert Debentures to some other form like shares or debentures. In these cases, companies effectively reduce cash flows. If Companies convert, then following Journal Entries are passed.

- *Debenture A/c.....Dr*

Premium on Redemption.....Dr

To Debenture Holders

(Being amount transferred to Debenture Holders)

- *Debenture Holders A/c.....Dr*

*To Share Capital / New Debentures (No. of Shares/No. of Debentures**

Premium on Redemption)

To Securities Premium (Balancing Figure)

(Being debenture converted)

- *No of shares or New Debenture to be issued = Amount payable on conversion / Issue price of shares/ debenture*

Underwriting

Underwriting is the contract between the company and an underwriter wherein the underwriter agrees to subscribe the unsubscribed shares or debentures for a commission.

Types of Application

- a. *Marked Application* : It bears the stamp of an underwriter. Credit is given to the individual underwriter.
- b. *Unmarked Application* : Does not bear any stamp. Credit of unmarked application is given to all the underwriters in the ratio of Gross Liability.
- c. *Firm Underwriting*: It is an Unconditional Liability of the Underwriter. Credit of Firm underwriting can be:
 - i. *Treated as marked application* : Credit is given to the individual underwriter.
 - ii. *Treated as unmarked application* : Credit is given to all underwriters in the ratio of Gross Liability.

Important points to note:

- a. *Underwriting commission cannot be paid on shares subscribed the promoters / directors and their relatives.*
- b. Maximum commission:

On shares : 5% of the issue amount including premium.

[5% of (No. of shares underwritten X issue price)]

On shares : 2.5% of the issue amount including premium.

[2.5% of (No. of debentures underwritten X issue price)]

However, Question sometimes asks to calculate commission on Face Value.

c. *Commission is calculated on the Gross Liability of the underwriter*

d. Liability of Underwriter:

Conditional Liability = Gross Liab - Marked Appl - Unmarked Appl - Firm

Total Liab = Conditional Liab. + Firm Underwriting i.e. Unconditional liab.

Net Liability = Total Liability - Commission

Sometimes, Firm underwriting is already applied and paid by the underwriters.

In such cases,

Net Liability = Conditional Liability - Commission

e. Journal Entries

For shares to be subscribed by the underwriters:

Underwriter's A/c Dr

To E.S.C

To S.P.

For commission

Underwriting commission A/c Dr

To Underwriter's A/c

For Receipt or Payment

Bank A/c Dr (Receipt)

To Underwriter's A/c

OR

Underwriter's A/c Dr

To Bank A/c (Payment)