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ACCOUNTING STANDARD – 4 CONTINGENCIES & EVENTS AFTER THE BALANCE SHEET DATE

QUOTE:

Keep Going, Difficult Roads Can Lead to Beautiful Destination

Objective: The objective of this standard is to provide timely information to stakeholders about the occurrence of material events after the balance sheet.

1. NON-APPLICABILITY

1. Liabilities of Life Assurance and general Insurance companies.
2. Obligations under Retirement Benefit Plans (AS 15).
3. Commitments arising from Long Term Lease Co. (AS 19)

2. MEANING OF EVENTS AFTER THE BALANCE SHEET DATE

Events (favorable or unfavorable) after the Balance Sheet date are those events that occur between the end of the reporting period and the date when the financial statements are approved by competent authority (Such as Board of Directors).

Example:

On 18th May, 20X2, the management of an entity approves financial statements for issue to its supervisory board. The supervisory board is made up solely of non-executives and may include representatives of employees and other outside interests. The supervisory board approves the financial statements on 26th May, 20X2. The financial statements are made available to shareholders and others on 1st June, 20X2. The shareholders approve the financial statements at their annual meeting on 15th July, 20X2 and the financial statements are then filed with a regulatory body on 17th July, 20X2. The financial statements are **approved for issue on 18th May, 20X2** (date of management approval for issue to the supervisory board).

3. TYPES OF EVENTS AND THEIR TREATMENT

ADJUSTING EVENTS	NON-ADJUSTING EVENTS
Events which provide <i>evidence of conditions that exist</i> on balance sheet date.	<i>Events that are Indicative of conditions that arose after the reporting period.</i> The events not related to circumstances/conditions existed on Balance sheet date; in other words, entirely new events after the BS date.
<u>Examples:</u> <ol style="list-style-type: none"> 1. Debtor declared insolvent after long outstanding receivable. 2. Settlement of litigation after balance sheet date (litigation started before balance sheet date) 3. Detection of fraud or error after balance sheet date. 4. Asset sold before balance sheet, consideration received after balance sheet date. 5. Reduction in NRV of Inventory sold after the Balance Sheet date. 	<u>Examples:</u> <ol style="list-style-type: none"> 1. Decline in the fair value of investments after the Balance Sheet. 2. Destruction of Assets of the entity by floods occurring after the reporting period. 3. Negotiation to purchase Property initiated before balance sheet date but actual transaction completed after balance sheet date.
<u>ACCOUNTING TREATMENT:</u> Adjust the Assets/Liabilities of Financial Statement which has just ended. (Existing Assets/liabilities may need to be adjusted (or) New Assets/Liabilities may be created)	<u>ACCOUNTING TREATMENT:</u> No need to adjust the Assets/liabilities of financial statement which has just ended. Only disclosure is required in case of material event.

Example of Inventory

Entity A values its inventories at cost or NRV, whichever is less. Entity A has 10 pieces of item A in its stock at the year end. Each item costs Rs. 500. All these items are sold subsequently but before the date of approval of financial statements for the reporting period at Rs. 450 per piece. The sale of inventories after the reporting period normally provides evidence about their net realisable value at the end of the reporting period.

4. SPECIAL ITEMS:

1. Equity Dividend Declared	2. Going Concern
<p>Dividend is declared after the balance sheet i.e. generally in AGM</p> <p>Hence there is no obligation regarding the balance sheet date.</p> <p>Hence it is always treated as a non-adjusting event.</p> <p>Therefore, <i>only disclosure</i> by way of contingent liability is required in financial statement.</p>	<p>If after the Balance Sheet date, the entity's going concern assumption is no longer appropriate due to happening of an event, <i>then it should adjust Assets and Liabilities of financial statement.</i> (i.e. it is treated as an adjusting event)</p> <p>Entity <i>should not</i> prepare its financial statements as per <i>Going Concern Basis.</i></p> <p>All Assets/liabilities should be remeasured at <i>realisable value (assets)</i> and <i>settlement value (liabilities).</i></p>

Note: Preference share dividend declared after balance sheet date on cumulative preference shares is adjusting event.

5. (MCQ's from ICAI Material)

1. Cash amounting to ₹ 4 lakhs, stolen by the cashier in the month of March 20X1, was detected in April, 20X1. The financial statements for the year ended 31st March, 20X1 were approved by the Board of Directors on 15th May, 20X1. As per Accounting Standards, this is _____ for the financial statements year ended on 31st March, 20X1.
 - (a) An Adjusting event.
 - (b) Non-adjusting event.
 - (c) Contingency.
 - (d) Provision

2. As per Accounting Standards, events occurring after the balance sheet date are
 - (a) Only favourable events that occur between the balance sheet date and the date when the financial statements are approved by the Board of directors.
 - (b) Only unfavourable events that occur between the balance sheet date and the date when the financial statements are approved by the Board of directors.
 - (c) Those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of directors.
 - (d) Those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are not approved by the Board of directors.

3. AS 4 does not apply to
 - (a) Obligation under retirement benefit plans.
 - (b) Commitments arising from long term lease contracts.
 - (c) liabilities of life assurance and general insurance enterprises arising from policies issued
 - (d) Both (a) & (b).

4. A Ltd. sold its building for ₹ 50 lakhs to B Ltd. and has also given the possession to B Ltd. The book value of the building is ₹ 30 lakhs. As on 31st March, 20X1, the documentation and legal formalities are pending. For the financial year ended 31st March, 20X1
 - (a) The company should record the sale.
 - (b) The company should recognise the profit of ₹ 20 lakhs in its profit and loss account.
 - (c) Both (a) and (b).
 - (d) The company should disclose the profit of ₹ 20 lakhs in notes to accounts.

ANSWERS	1	2	3	4
	a	c	d	c