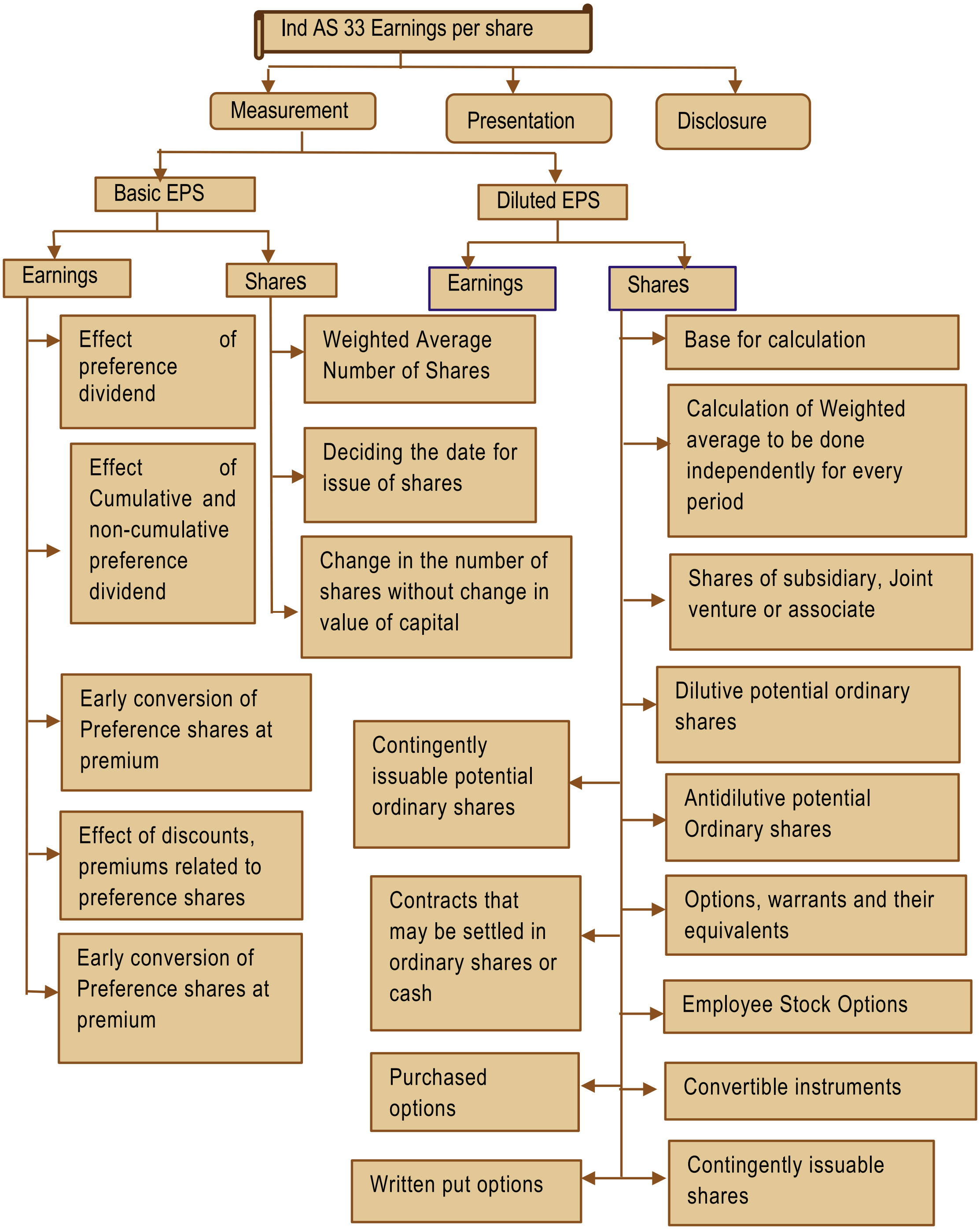
UNIT 2 : INDIAN ACCOUNTING STANDARD 33 : EARNINGS PER SHARE

LEARNING OUTCOMES

After studying this unit, you will be able to:

- Understand the objectives behind calculation and disclosure of EPS
- Define the terms used in the Standard such as basic EPS, dilution, anti-dilution, contingent share agreement, potential ordinary shares, etc.
- Work out the basic EPS after considering the important points for calculation of earnings and weighted average number of shares
- Determine the diluted EPS after considering the important points for calculation of diluted earnings and weighted average number of shares
- Deal with various peculiar situations of potential ordinary shares, contingently convertible shares, etc.
- Disclose the information regarding EPS in the financial statements

UNIT OVERVIEW



2.1 INTRODUCTION

Earnings per share (EPS) is an important measure of the performance of the company. The equity shareholders (ordinary shareholders as per Ind AS 33) invest their money in the entity as owners of the company. They undertake business risks and financial risks along with all allied systematic and non-systematic risks of the company. Generally, they would expect a higher return as compared to a debt-holder considering the risks involved on their investments.

EPS is a ratio that is widely used by financial analysts, investors and other users to gauge an entity's profitability. Its purpose is to indicate how effective an entity has been in using the resources provided by the ordinary shareholders, and to assess the entity's current net earnings. EPS also forms the basis for calculating the price-earnings ratio, which is widely used by investors and analysts to value shares.

2.2 OBJECTIVE

To prescribe principles for the determination and presentation of earnings per share:

Ind AS 33 provides detailed guidelines and lays down the principles about how to calculate earnings, weighted average number of shares and basic and diluted earnings per share, to facilitate performance comparisons between:

(i) different entities in the same reporting period:

For example, if one needs to check whether Hero Motocorp Limited is doing better than Baja Auto Limited in terms of profitability, EPS can be considered to be a measure for comparison of performance.

(ii) different reporting periods for the same entity:

One can check the performance of a company over last 5 years using EPS as a benchmark.

2.2.1 Limitation of EPS

Earnings per share data may have **limitations** because of different accounting policies that companies might have used for determining 'earnings'.

2.3 SCOPE

- This Ind AS shall apply to companies (that have issued ordinary shares) to which Ind AS notified under the Companies Act apply. In Indian context, the term 'ordinary shares' is equivalent to 'equity shares'.
- An entity that discloses earnings per share shall calculate and disclose earnings per share in accordance with this Standard.
- When an entity presents both consolidated financial statements and separate financial statements prepared in accordance with Ind AS 110, *Consolidated Financial Statements*, and Ind AS 27, *Separate Financial Statements,* respectively, the disclosures required by this Standard shall be presented both in the consolidated financial statements and separate financial statements. In consolidated financial statements such disclosures shall be based on consolidated information and in separate financial statements such disclosures shall be based on information given in separate financial statements.

The above mentioned provisions are summarised below in the following table:

Sr. No.	Type of Financial statements	EPS disclosure required	EPS computation should be based on
1	Consolidated	Yes	Information given in consolidated financial statements only
2	Separate	Yes	Information given in separate financial statements only

2.4 DEFINITIONS

1. An ***ordinary share*** is an equity instrument that is subordinate to all other classes of equity instruments. Ordinary shares participate in profit for the period only after other types of shares such as preference shares have participated. An entity may have more than one class of ordinary shares. Ordinary shares of the same class have the same rights to receive dividends.

In accordance with Ind AS 32, *Financial Instruments: Presentation*, an equity instrument is defined as a contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

2. A ***potential ordinary share*** is a financial instrument or other contract that may entitle its holder to ordinary shares.

Examples of potential ordinary shares are:

(a) financial liabilities or equity instruments, including preference shares, that are convertible into ordinary shares;

(b) options and warrants;

(c) shares that would be issued upon the satisfaction of conditions resulting from contractual arrangements, such as the purchase of a business or other assets.

Contracts that might result in the issue of ordinary shares of the entity to the holder of the contract, at the option of the issuer or the holder, are potential ordinary shares.

Example 1

ABC & Co has issued preference shares with the option to convert these into an equal number of ordinary shares in 2 years' time. They represent potential ordinary shares, even though it is not certain whether the preference shareholders will convert them into equity shares (since it will depend on the prices of each class of shares at that time). If the price of the ordinary share is higher than that of the preference shares, the holders will convert, and will make a profit. If the price is lower, they will not.

3. ***Options, warrants and their equivalents*** are financial instruments that give the holder the right to purchase ordinary shares.

4. ***Put options*** on ordinary shares are contracts that give the holder the right to sell ordinary shares at a specified price for a given period.

5. ***Dilution*** is a reduction in earnings per share or an increase in loss per share resulting from the assumption that convertible instruments are converted, that options or warrants are exercised, or that ordinary shares are issued upon the satisfaction of specified conditions.

6. ***Antidilution*** is an increase in earnings per share or a reduction in loss per share resulting from the assumption that convertible instruments are converted, that options or warrants are exercised, or that ordinary shares are issued upon the satisfaction of specified conditions.

Example 2

ABC Ltd. has interest paying debt which are convertible into ordinary shares at the option of the entity. On conversion, ABC Ltd. will save on the interest costs and in return will have to issue additional shares. In case the EPS of ABC Ltd. increases on conversion, the convertible debt would be considered as anti-dilutive. However, if the conversion will decrease the EPS, it would be considered as dilutive.

7. ***A contingent share agreement*** is an agreement to issue shares that is dependent on the satisfaction of specified conditions.

Example 3

ABC Ltd. has provided share options to its employees under a ESOP scheme. As per the scheme, the employees have to provide 3 years' services to the company for being eligible to share options at a discounted price. This is a contingent share agreement.

8. ***Contingently issuable ordinary shares*** are ordinary shares issuable for little or no cash or other consideration upon the satisfaction of specified conditions in a contingent share agreement.

Example 4

ABC Ltd. acquires XYZ Ltd.'s business in exchange for ABC Ltd.'s shares. If the share price falls by more than 25% within 6 months of the business combination, ABC Ltd. will issue more shares (for free) to XYZ Ltd., as a compensation.

2.5 MEASUREMENT

Measurement can be divided into following categories:

a. Measurement of basic earnings per share

- Measurement of earnings
- Measurement of weighted average number of shares

b. Measurement of diluted earnings per share

- Measurement of earnings for diluted EPS
- Measurement of number of shares for diluted EPS

c. Measurement in case of dilutive potential ordinary shares

d. Measurement in case of options, warrants and their equivalents

e. Measurement in case of convertible instruments

f. Measurement in case of contingently issuable shares

g. Measurement in case of contracts that may be settled in ordinary shares or cash

h. Measurement in case of purchased options and written put options

i. Dealing with retrospective adjustments

2.6 MEASUREMENT OF BASIC EARNINGS PER SHARE

2.6.1 Meaning and Formula

1. Meaning

An entity shall calculate basic earnings per share for profit or loss attributable to ordinary equity holders of the parent entity and, if presented, profit or loss from continuing operations attributable to those equity holders.

The objective of basic earnings per share information is to provide a measure of the interests of each ordinary share of a parent entity in the performance of the entity over the reporting period.

2. Formula

Basic earnings per share shall be calculated by dividing profit or loss for the period attributable to ordinary equity holders of the parent entity (the numerator) by the weighted average number of ordinary (equity) shares outstanding during the period (the denominator). It can be expressed mathematically as follows:

$$\frac{\text{Profit/Loss attributable to Equity share holders}}{\text{Weighted average number of Equity shares outstanding during the period}}$$

2.6.2 Measurement of Earnings

- For the purpose of calculating basic earnings per share, the amounts attributable to ordinary equity holders of the parent entity in respect of:

  (a) profit or loss from continuing operations attributable to the parent entity; and

  (b) profit or loss attributable to the parent entity

  shall be the amounts in (a) and (b) adjusted for the after-tax amounts of preference dividend, differences arising on the settlement of preference shares, and other similar effects of preference shares classified as equity.

  An entity that has preference shares in issue, will classify those shares as financial liabilities or equity in accordance with the principles under Ind AS 32. An adjustment is required to the profit or loss for the period, to arrive at the profit or loss attributable to ordinary equity holders for the purpose of calculating EPS, if preference shares are classified as equity. Any dividends and other appropriations would be debited directly to equity under Ind AS 32. Any dividends or other appropriations for preference shares classified as liabilities should be accounted for as finance costs in arriving at profit or loss for the period. No adjustment is required for the purpose of calculating EPS.

- Where any item of income or expense, which is otherwise required to be recognised in profit or loss in accordance with Ind AS, is debited or credited to securities premium account/other reserves, the amount in respect thereof shall be deducted from profit or loss from continuing operations for the purpose of calculating basic earnings per share.

- All items of income and expense attributable to ordinary equity holders of the parent entity that are recognised in a period, including tax expense and dividends on preference shares classified as liabilities are included in the determination of profit or loss for the period attributable to ordinary equity holders of the parent entity.

- The amount of dividends declared in respect of the year should be deducted in arriving at the profit attributable to ordinary shareholders for preference dividends that are non-cumulative.

- The dividend for the period should be taken into account, whether or not it has been declared for cumulative preference dividends. If an entity is unable to pay or declare a cumulative preference dividend, the undeclared amount of the cumulative preference dividend (net of tax, if applicable) should still be deducted in arriving at earnings for the purpose of the EPS calculation. The amount paid is not deducted in arriving at earnings for the purpose of the EPS calculation in the period in which arrears of cumulative preference dividends are paid.

- Preference shares that provide for a low initial dividend to compensate an entity for selling the preference shares at a discount, or an above-market dividend in later periods to compensate investors for purchasing preference shares at a premium, are sometimes referred to as increasing rate preference shares. Any original issue discount or premium on increasing rate preference shares is amortised to retained earnings using the effective interest method and treated as a preference dividend for the purposes of calculating earnings per share (irrespective of whether such discount or premium is debited or credited to securities premium account in view of requirements of any law).

Example 1 Increasing rate preference shares

Reference: Ind AS 33, paragraphs 12 and 15

Entity D issued non-convertible, non-redeemable class A cumulative preference shares of Rs. 100 par value on 1 January 20X1. The class A preference shares are entitled to a cumulative annual dividend of Rs. 7 per share starting in 20X4.

At the time of issue, the market rate dividend yield on the class A preference shares was 7 per cent a year. Thus, Entity D could have expected to receive proceeds of approximately Rs. 100 per class A preference share if the dividend rate of Rs. 7 per share had been in effect at the date of issue.

In consideration of the dividend payment terms, however, the class A preference shares were issued at Rs. 81.63 per share, ie at a discount of Rs. 18.37 per share. The issue price can be calculated by taking the present value of Rs. 100, discounted at 7 per cent over a three-year period.

Because the shares are classified as equity, the original issue discount is amortised to retained earnings using the effective interest method and treated as a preference dividend for earnings per share purposes. To calculate basic earnings per share, the following imputed dividend per class A preference share is deducted to determine the profit or loss attributable to ordinary equity holders of the parent entity:

Year	Carrying amount of class A preference shares 1 January	Imputed[(a)] Dividend	Carrying amount[(b)] of class A preference shares 31 December	*Dividend paid*
	Rs.	Rs.	Rs.	Rs.
20X1	81.63	5.71	87.34	–
20X2	87.34	6.12	93.46	–
20X3	93.46	6.54	100.00	–
Thereafter:	100.00	7.00	107.00	(7.00)

(a) at 7 %
(b) This is before dividend payment.

2.6.2.1 Redemption/Repurchase of preference shares at premium

Preference shares may be repurchased under an entity's tender offer to the holders. The excess of the fair value of the consideration paid to the preference shareholders over the carrying amount of the preference shares represents a return to the holders of the preference shares and a charge to retained earnings for the entity. This amount is deducted in calculating profit or loss attributable to ordinary equity holders of the parent entity.

Example 5

ABC Ltd. had issued preference shares at ₹ 100 each 10 years ago. Now ABC Ltd. buys back the shares for ₹ 120 each. ₹ 20 premium for each share is charged to retained earnings. No amount is recorded in the statement of profit and loss for this transaction. However, for EPS purposes, ₹20 for each share is charged to the statement of profit or loss for the period of the transaction.

2.6.2.2 Early conversion of Preference shares at premium

Early conversion of convertible preference shares may be induced by an entity through favourable changes to the original conversion terms or the payment of additional consideration. The excess of the fair value of the ordinary shares or other consideration paid over the fair value of the ordinary shares issuable under the original conversion terms is a return to the preference shareholders and is deducted in calculating profit or loss attributable to ordinary equity holders of the parent entity.

Illustration 1

ABC Ltd. issues 9% preference shares of fair value of ₹ 10 each on 1.4.20X1. Total value of the issue is ₹ 10,00,000. The shares are issued for a period of 5 years and would be redeemed at the end of 5th year. The shares are to be redeemed at ₹ 11 each.

At the end of the year 3, i.e. on 31.3.20X4, company finds that it has earned good returns than expected over last three years and can make the redemption of preference shares early. To compensate the shareholders for two years of dividend which they need to forego, company decided to redeem the shares at ₹ 12 each instead of original agreement of ₹ 11. Comment on the impact of early conversion of preference shares at a premium on earnings for the year 20X3-20X4 attributable to ordinary equity holders of ABC Ltd. for basic EPS.

Ignore the applicability of the standards on Financial Instruments (i.e., ignore EIR; further, the additional payment to be made can be met from Securities Premium/Reserves as Premium on Redemption) and answer on the basis of Ind AS 33 only.

Solution

In the given situation, ₹ 1 per share is the excess payment made by the company amounting to ₹ 1,00,000 in all. The amount of ₹ 1,00,000 will be deducted from the earnings of the year 20X3-20X4 while calculating the basic EPS of year 20X3-20X4.

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2.6.2.3 Excess payment to Preference share holders

Any excess of the carrying amount of preference shares over the fair value of the consideration paid to settle them is added in calculating profit or loss attributable to ordinary equity holders of the parent entity.

Illustration 2

An entity has following preference shares in issue at the end of 20X4:

- ***5% redeemable, non-cumulative preference shares:*** *These shares are classified as liabilities. During the year, an amount of ₹ 1,00,000 (computed using the coupon rate of 5% - ₹ 20,00,000 x 5%) was paid to the preference shareholders*
- ***Increasing-rate, cumulative, non-redeemable preference shares issued at a discount in 20X0, with a cumulative dividend rate from 20X5 of 10%:*** *The shares were issued at a discount to compensate the holders, because dividend payments will not commence until 20X5. The accrual for the discount in the current year, calculated using the effective interest method amounted to, say, ₹ 18,000. These shares are classified as equity – ₹ 200,000.*
- ***8% non-redeemable, non-cumulative preference shares:*** *At the beginning of the year, the entity had ₹ 100,000 8% preference shares outstanding but, at 30 June 20X4, it repurchased ₹ 50,000 of these at a discount of ₹ 1,000 – ₹ 50,000.*
- ***7% cumulative, convertible preference shares (converted in the year):*** *These shares were classified as equity, until their conversion into ordinary shares at the beginning of the year. No dividend was accrued in respect of the year, although the previous year's dividend was paid immediately prior to conversion. To induce conversion, the terms of conversion of the 7% convertible preference shares were also amended, and the revised terms entitled the preference shareholders to an additional 100 ordinary shares on conversion with a fair value of ₹ 300 – Nil.*

The profit after tax for the year 20X4 is ₹ 150,000.

Determine the adjustments for the purpose of calculating EPS.

Solution

Adjustments for the purpose of calculating EPS are made as follows:

Particulars	Amount (₹)	Amount (₹)
Profit after tax		150,000
Amortisation of discount on issue of increasing-rate preference shares (Refer Note 1)	(18,000)	
Discount on repurchase of 8% preference shares (Refer Note 2)	1,000	
Premium to induce Conversion	(30,000)	(47,000)
Profit attributable to ordinary equity holders for basic EPS (Refer Note 3-5)		1,03,000

Notes:

1. The original discount on issue of the increasing-rate preference shares is treated as amortised to retained earnings and treated as preference dividends for EPS purposes and adjusted against profit attributable to the ordinary equity holders. There is no adjustment in respect of dividend, because these do not commence until 20X5. Instead, the finance cost is represented by the amortisation of the discount in the dividend-free period. In future years, the accrual for the dividend of ₹ 20,000 will be deducted from profits.

2. The discount on repurchase of the 8% preference shares has been credited to equity so should be added to profit.

3. The dividend on the 5% preference shares has been charged to the income statement, because the preference shares are treated as liabilities, so no adjustment is required for it from the profit.

4. No accrual for the dividend on the 8% preference shares is required, because they are non-cumulative. If a dividend had been declared for the year, it would have been deducted from profit for the purpose of calculating basic EPS, because the shares are treated as equity and the dividend would have been charged to equity in the financial statements.

5. The 7% preference shares are convertible and hence correctly classified as equity. Accordingly, the additional amount paid (100 additional shares x fair value ₹ 300 per share = ₹ 30,000) to induce conversion would be taken to Equity Share Capital and Retained Earnings or Securities Premium, as the case may be (transaction with 'owners'). Therefore, this excess amount paid would require to be deducted from the Net Profit to arrive at Net Profit attributable to Equity Shareholders.

6. It may be noted that as per Sections 53 and 55 of the Companies Act, 2013, a company cannot issue shares at discount or any irredeemable preference shares. However, the above illustration has been given only to explain the concept given in Ind AS.

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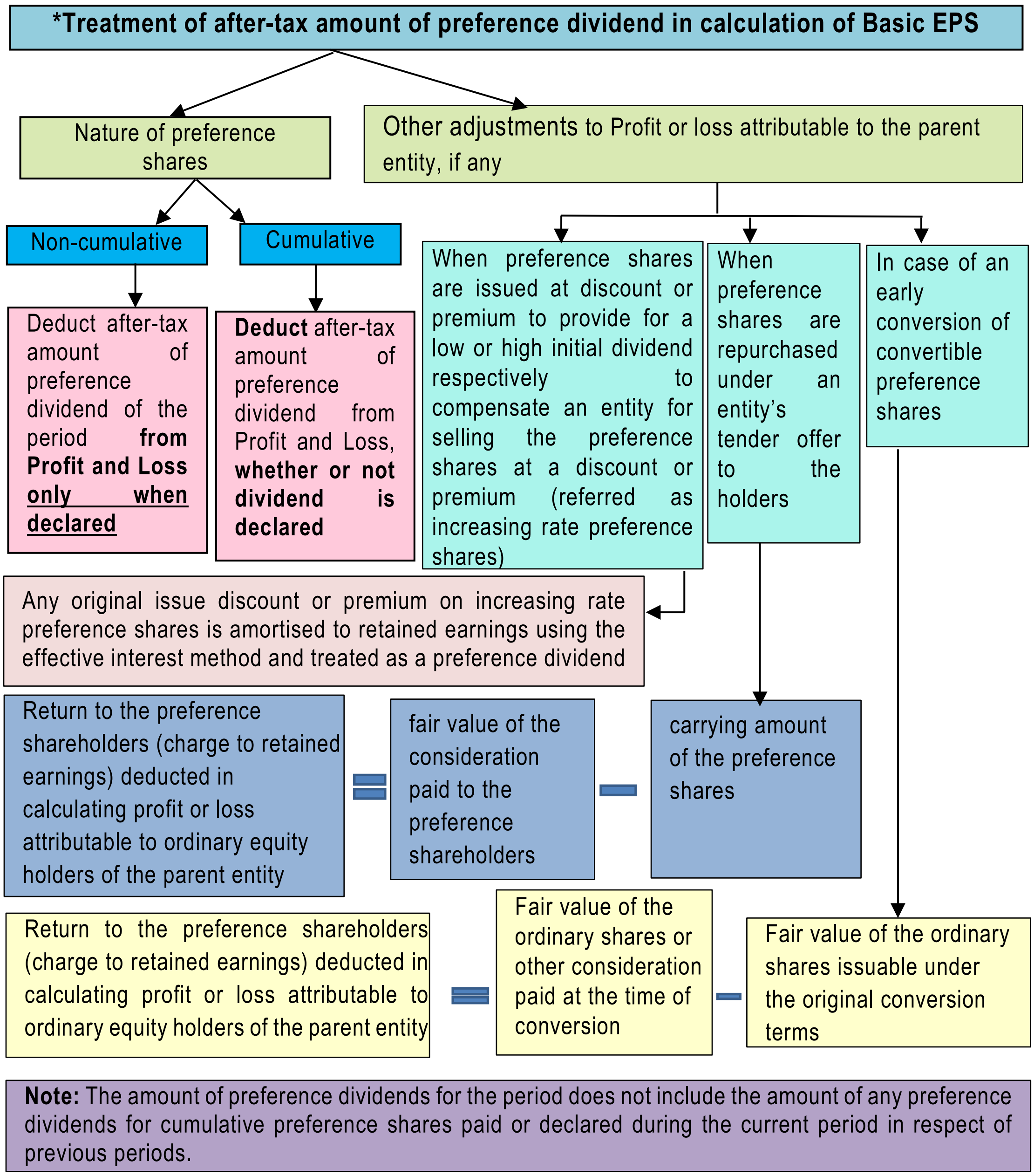
The changes given in the above two questions do not consider the impact of the Companies Act, 2013. Since Ind AS is based on IFRS which ignores country-specific statutory requirements and instead opts for a principle-based approach, solutions are given accordingly. However, the statute gains precedence over Ind AS, and hence the same needs to be followed practically.

Here, in this paper of Financial Reporting, the discussion has been restricted to the concepts of Ind AS provisions.



2.6.3 Shares

2.6.3.1 Weighted Average Number of Shares

- For the purpose of calculating basic earnings per share, the number of ordinary shares shall be the weighted average number of ordinary shares outstanding during the period.

  The weighted average number of ordinary shares outstanding during the period is the number of ordinary shares outstanding at the beginning of the period, adjusted by the number of ordinary shares bought back or issued during the period *multiplied by a time-weighting factor.*

- The time-weighting factor is the number of days that the shares are outstanding as a proportion of the total number of days in the period; a reasonable approximation of the weighted average is adequate in many circumstances.

Weighted average number of equity shares:

Ordinary shares outstanding at the beginning	xxxx
Less: Ordinary shares bought back during the period*	xxxx
Add: Ordinary shares issued during the period*	xxxx
Ordinary shares outstanding during the period	**xxxx**

*to be multiplied by time-weighting factor. The time-weighting factor is the number of days that the shares are outstanding as a proportion of the total number of days in the period.

Illustration 3

Following is the data for company XYZ in respect of number of equity shares during the financial year 20X1-20X2. Find out the number of shares for the purpose of calculation of basic EPS as per Ind AS 33.

S. No.	***Date***	***Particulars***	***No of shares***
1	*1-Apr-20X1*	*Opening balance of outstanding equity shares*	*100,000*
2	*15-Jun-20X1*	*Issue of equity shares*	*75,000*
3	*8-Nov-20X1*	*Conversion of convertible preference shares in Equity*	*50,000*
4	*22-Feb-20X2*	*Buy back of shares*	*(20,000)*
5	*31-Mar-20X2*	*Closing balance of outstanding equity shares*	*205,000*

Solution

The closing balance of the outstanding shares is 2,05,000 by a normal addition and subtraction. But as per weighted average concept, one need to find out for how many days each type of shares was actually held during the year.

The shares which were there on 1st April 20X1, were held for the whole year. Therefore, weighted average number of such shares will be given by the formula:

No of shares x no of days the shares were held during the year / 365

= 1,00,000 x 365 / 365 = 1,00,000

But the shares which were issued on 15th June 20X1, were held for only 290 days. Therefore, the weighted average number of shares will be 75,000 x 290 / 365 = 59,589.

Following the above formula, the weighted average number of shares for calculation of EPS for the year 20X1-20X2 will be as follows:

Sr. No.	Date	Particulars	No of shares	No of days shares were outstanding	Weighted average no of shares
1	1-Apr-20X1	Opening balance of outstanding equity shares	1,00,000	365	1,00,000
2	15-Jun-20X1	Issue of equity shares	75,000	290	59,589
3	8-Nov-20X1	Conversion of convertible preference shares in Equity	50,000	144	19,726
4	22-Feb-20X2	Buy back of shares	(20,000)	(38)*	(2,082)
5	31-Mar-20X2	Closing balance of outstanding equity shares	2,05,000		1,77,233

* These shares had already been considered in the shares issued. The same has been deducted assuming that the bought back shares have been extinguished immediately.

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From the above illustration, one can notice that the date of issue/ conversion/ repurchase/ transaction affecting the addition or deletion in number of shares is very crucial for calculation of weighted average number of shares.

2.6.3.2 Deciding the date for issue of shares

- Shares are usually **included** in the weighted average number of shares **from the date consideration is receivable** (which is generally the date of their issue), for example:

  (a) ordinary shares issued in **exchange for cash** are included from the date when **cash is receivable**;

  (b) ordinary shares issued on the **voluntary reinvestment of dividend** on ordinary or preference shares are included from the date when **dividend are reinvested**;

  (c) ordinary shares issued as a result of the **conversion of a debt instrument** to ordinary shares are included from the date that **interest ceases to accrue**;

  (d) ordinary shares issued **in place of interest or principal** on other financial instruments are included from the date that **interest ceases to accrue**;

  (e) ordinary shares issued in **exchange for the settlement of a liability** of the entity are included from the **settlement date**;

  (f) ordinary shares issued as **consideration for the acquisition** of an asset other than cash are included from the **date on which the acquisition is recognised**; and

  (g) ordinary shares issued for the **rendering of services** to the entity are included from the date on which as the **services are rendered**.

- Ordinary shares issued as part of the consideration transferred in a business combination are included in the weighted average number of shares from the acquisition date of the business. This is because the acquirer incorporates into its statement of profit and loss the acquiree's profits and losses from that date.

- Entities often issue instruments that are convertible into ordinary shares that may be either mandatorily convertible or convertible at the option of the issuer or holder. The issue of ordinary shares is solely dependent on the passage of time for a mandatorily convertible instrument. Ordinary shares that are issuable on the conversion of a mandatorily convertible instrument should be included in basic EPS from the date the contract is entered into.

Deciding the date for issue of shares

Shares are usually included in the weighted average number of shares from the date consideration is receivable (which is generally the date of their issue), for example:

Situation of issuance of ordinary shares	Ordinary shares are included in the weighted average number of shares from the date
When issued in exchange for cash	When cash is receivable
When issued on voluntary reinvestment of dividends (on ordinary or preference shares)	When dividends are reinvested
When issued as a result of conversion of a debt instrument to ordinary shares	When Interest ceases to accrue
Issued in place of interest or principal on other financial instruments	When Interest ceases to accrue
Issued in exchange for the settlement of a liability	On settlement date
Issued as consideration for the acquisition of an asset other than cash	When the acquired asset is recognised
Issued for rendering of services to the entity	When the services are rendered
Issued as a part of the consideration transferred in a business combination	From the date of acquisition
Issued upon the conversion of a mandatorily convertible instrument	From the date of entering into the contract

2.6.3.3 Contingently issuable shares

- Contingently issuable shares are treated as outstanding and are included in the calculation of basic earnings per share only from the date when all necessary conditions are satisfied (i.e. the events have occurred).
- Shares that are issuable solely after the passage of time are not contingently issuable shares, because the passage of time is a certainty.
- Outstanding ordinary shares that are contingently returnable (ie subject to recall) are not treated as outstanding and are excluded from the calculation of basic earnings per share until the date the shares are no longer subject to recall.

Example 6

ABC Ltd. acquires a company in 20X1 for consideration paid in shares. If the profits for calendar years 20X1 and 20X2 meet budget, ABC Ltd. will issue more shares to the vendor in February 20X3. These additional shares will be included in the weighted-average calculation from 1 January 20X3 (considering reporting date as December end), if the targets are met.

2.6.3.4 Change in the number of shares without change in value of capital

- The weighted average number of ordinary shares outstanding during the period and for all periods presented shall be adjusted for events, other than the conversion of potential ordinary shares, that have changed the number of ordinary shares outstanding without a corresponding change in resources.
- There are certain events, which will not change the total equity of the company. Still the number of outstanding equity shares will undergo a change.
- Ordinary shares may be issued, or the number of ordinary shares outstanding may be reduced, without a corresponding change in resources. Examples include:

  (a) a capitalisation or bonus issue (sometimes referred to as a stock dividend);

  (b) a bonus element in any other issue, for example a bonus element in a rights issue to existing shareholders;

  (c) a share split; and

  (d) a reverse share split (consolidation of shares).

- In a capitalisation or bonus issue or a share split, ordinary shares are issued to existing shareholders for no additional consideration. Therefore, the number of ordinary shares outstanding is increased without an increase in resources. The number of ordinary shares outstanding before the event is adjusted for the proportionate change in the number of ordinary shares outstanding as if the event had occurred at the beginning of the earliest period presented.

Example 7

On a two-for-one bonus issue, the number of ordinary shares outstanding before the issue is multiplied by three to obtain the new total number of ordinary shares, or by two to obtain the number of additional ordinary shares.

- We have seen above that for calculation of weighted average number of shares, the date of issue/contract etc. is very important. However, in case of bonus shares where the number of shares change without the change in the resources, the date will be considered from the beginning of the earliest period presented, irrespective of the fact of the date of actual capitalisation of the reserves.

Illustration 4

On 31 March, 20X2, the issued share capital of a company consisted of ₹ 100,000,000 in ordinary shares of ₹ 25 each and ₹ 500,000 in 10% cumulative non-redeemable preference shares (classified as equity) of Re 1 each. On 1 October, 20X2, the company issued 1,000,000 ordinary shares fully paid by way of capitalisation of reserves in the proportion 1:4 for the year ended 31 March, 20X3.

Profit for 20X1-20X2 and 20X2-20X3 is ₹ 450,000 and ₹ 550,000 respectively.

Calculate the basic EPS for 20X1-20X2 and 20X2-20X3.

Solution

	20X2-20X3 ₹'000	20X1-20X2 ₹'000
Calculation of earnings		
Profit for the year	550	450
Less: Preference shares dividend	(50)	(50)
Earnings (A)	500	400

	No. of shares in '000	No. of shares in '000
Number of ordinary shares		
Shares in issue for full year	4,000	4,000
Capitalisation issue at 1 October 20X2	1,000	1,000
Number of shares (B)	5,000	5,000
Earnings per ordinary share (A/B)	10 Paise	8 Paise*

*The comparative EPS for 20X1-20X2 can alternatively be calculated by adjusting the previously disclosed EPS in 20X1-20X2 (in this example, 10 Paise) by the following factor:

Number of shares before the bonus issue/ Number of shares after the bonus issue

*Adjusted EPS for 20X1-20X2 10 Paise x (4,000/ 5,000) = 8 Paise

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Illustration 5

X Ltd.

1 January *1,000,000 shares in issue*

28 February *Issued 200,000 shares at fair value*

31 August *Bonus issue 1 share for 3 shares held*

30 November *Issued 250,000 shares at fair value*

Calculate the number of shares which would be used in the basic EPS calculation. Consider reporting date as December end.

Solution

Period	Calculations	Weighted average number of shares
1 January - 28 February	1,000,000 × 2 / 12 × 4 / 3	222,222
1 March - 31 August	1,200,000 × 6 / 12 × 4 / 3	800,000
1 September - 30 November	1,600,000 × 3 / 12	400,000
1 December - 31 December	1,850,000 × 1 / 12	154,167
		1,576,389

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2.6.3.5 Rights issues

Entities might raise additional capital by issuing shares to existing shareholders, on a pro rata basis to their existing holdings, in the form of a rights issue. The rights shares can either be offered at the current market price or at a price that is below the current market price. Ordinary shares might be issued during the year by way of a rights issue at a discount to the market price. The weighting calculation should reflect the fact that the discount is effectively a bonus (stock dividend) given to the shareholders in the form of shares for no consideration. This bonus element should be factored into the calculation of the weighted average number of shares. A rights issue is equivalent to a capitalisation issue of part of the shares for no consideration and an issue of the remainder of the shares at full market price. The notional capitalisation issue reflects the bonus element inherent in the rights issue and is measured by the following fraction:

$$\frac{\text{Fair value per share immediately before the excersice of rights}}{\text{Theoretical ex-rights fair value per share}}$$

where,

Theoretical ex-rights fair value per share

<u>Fair value of all outstanding shares before exercise of right + Total amount received from exercise of rights</u>

No of shares outstanding after the exercise of rights

Illustration 6

At 31 December 20X1, the issued share capital of a company consisted of 1.8 million ordinary shares of ₹ 10 each, fully paid. The profits for the year ended 31 December 20X1 and 20X2 amounted to ₹ 630,000 and ₹ 875,000 respectively. On 31 March 20X2, the company made a rights issue on a 1 for 4 basis at ₹ 30. The market price of the shares immediately before the rights issue was ₹ 60.

Calculate EPS.

Solution

Calculation of theoretical ex rights price:

	Number of shares		₹
Initial holding	4	Market Value (4 x 60)	240
Rights taken up	1	Cost (1 x 30)	30
New holding	**5**	**Theoretical price**	**270**

Theoretical ex rights price = 270/5 = ₹ 54

Calculation of bonus element

The bonus element of the rights issue is given by the fraction:

Market price before rights issue/Theoretical ex-rights price =60 / 54 = 10/9

This corresponds to a bonus issue of 1 for 9. The bonus ratio will usually be greater than 1 (that is, the market price of the shares immediately prior to the exercise of rights is greater than the theoretical ex-rights price). If the ratio is less than 1, it might indicate that the market price has fallen significantly during the rights period, which was not anticipated when the rights issue was announced. In this situation, the rights issue should be treated as an issue of shares for cash at full market price.

It can be demonstrated, using the figures in the illustration, that a rights issue of 1 for 4 at ₹ 30 is equivalent to a bonus issue of 1 for 9 combined with an issue of shares at full market price of ₹ 54 per share. Consider an individual shareholder holding 180 shares:

	Number of shares (in '000s)	**Value**	**₹ *(in million)***
Original holding	1,800	Value at ₹60 per share	108.00
Rights shares (1:4)	450	Value at ₹30 per share	13.50
Holding after rights issue	2,250	Value at ₹54 per share	121.50

The additional 450 thousand rights shares at ₹30 can be shown to be equivalent to a bonus issue of 1 for 9 on the original holding, followed by an issue of 1:8 at full market price of ₹54 following the bonus issue, as follows:

	Number of shares (in '000s)	**Value**	**₹ *(in million)***
Original holding	1,800	Value at ₹60 per share	108.00
Bonus issue of 1 for 9	200	Value Nil	nil
	2000	**Value at ₹ 54 per share**	**108.00**
Issue of 1 for 8 at full price (450-200)	250	Value at ₹ 54 per share	13.50
Total holding	**2250**	**Value at ₹54 per share**	**121.50**

The shareholder is therefore indifferent as to whether the entity makes a rights issue of 1 for 4 at ₹ 30 per share, or a combination of a bonus issue of 1 for 9 followed by a rights issue of 1 for 8 at full market price of ₹ 54 per share.

Having calculated the bonus ratio, the ratio should be applied to adjust the number of shares in issue before the rights issue, both for the current year and for the previous year. Therefore, the weighted average number of shares in issue for the current and the previous period, adjusted for the bonus element, would be:

Weighted average number of shares:

	20X2	20X1
No of actual shares in issue before rights	1,800,000	1,800,000
Correction for bonus issue (1:9)	200,000	200,000
Deemed no of shares in issue before right issue	2,000,000	2,000,000
(1.8 million x 10/9 for the whole year)		
The no of shares after the rights issue would be		
= 1.8 million x 5/4 = 2,250,000		
Therefore, the weighted average number of shares would be		
2.0 million for the whole year		2,000,000
1.8 million x 10/9 x 3/12 (before rights issue)	500,000	-
2.25 million x 9/12 (after rights issue)	1,687,500	-
Weighted average number	**2,187,500**	**2,000,000**
	20X2	**20X1**
Calculation of earnings		**(as previously stated)**
Profits for the year	₹ 875,000	₹ 630,000
Weighted average number	2,187,500	1,800,000
Basic EPS	**40p**	**35p**
Basic EPS for 20X1 (as restated)		₹ 630,000 / 2,000,000
		= 31.50p

In practice, the restated EPS for 20X1 can also be calculated by adjusting the EPS figure of the previous year by the reciprocal of the bonus element factor:

* 35p x 9/10 = 31.50 p

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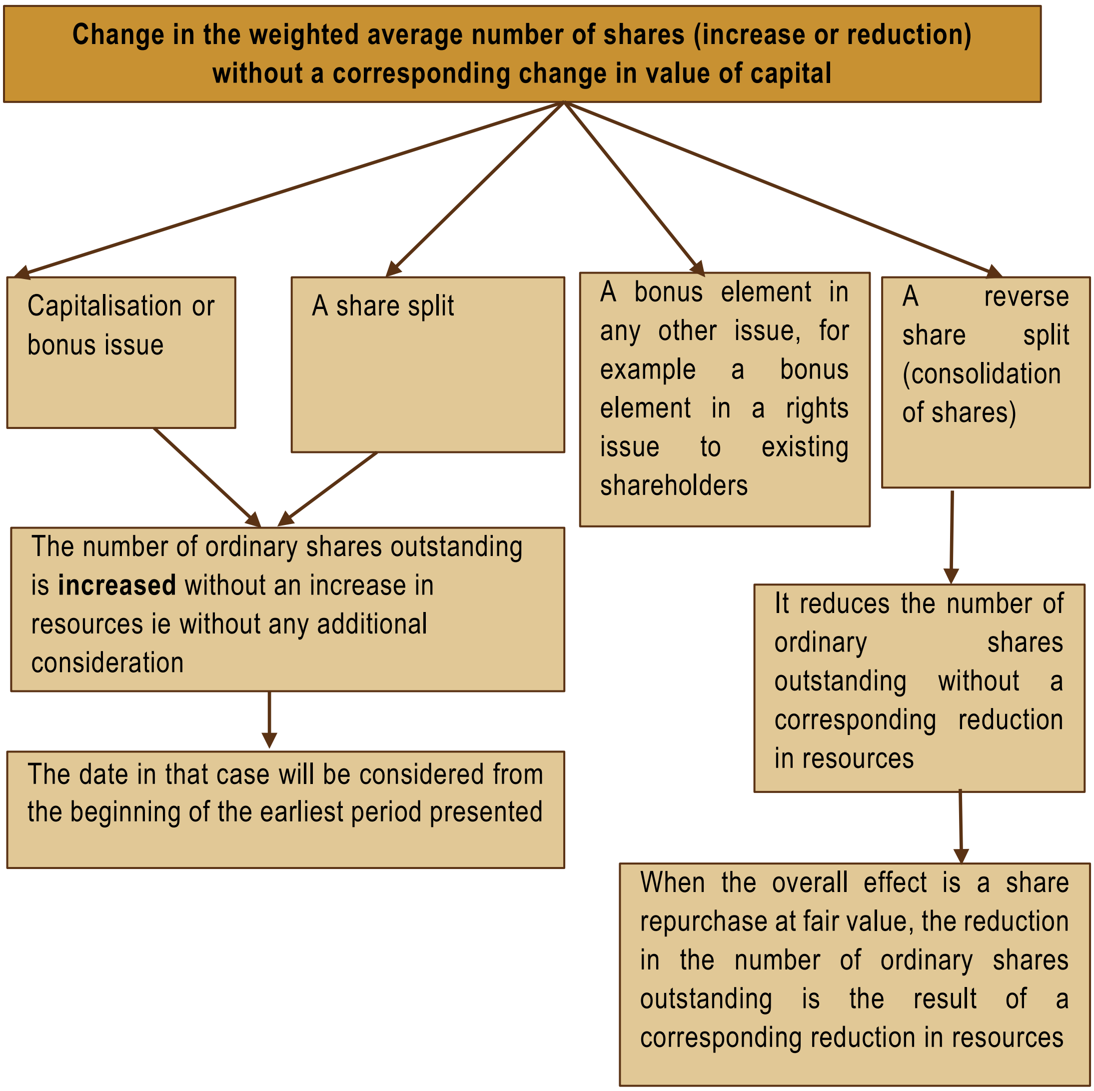
A consolidation of ordinary shares generally reduces the number of ordinary shares outstanding without a corresponding reduction in resources. However, when the overall effect is a share repurchase at fair value, the reduction in the number of ordinary shares outstanding is the result of a corresponding reduction in resources.

An example is a share consolidation combined with a special dividend. The weighted average number of ordinary shares outstanding for the period in which the combined transaction takes place is adjusted for the reduction in the number of ordinary shares from the date the special dividend is recognised.



2.7 DILUTED EARNINGS PER SHARE

2.7.1 Scope, meaning and formula

- An entity shall calculate diluted earnings per share amounts for profit or loss attributable to ordinary equity holders of the parent entity and, if presented, profit or loss from continuing operations attributable to those equity holders.
- For the purpose of calculating diluted earnings per share, an entity shall adjust profit or loss attributable to ordinary equity holders of the parent entity, and the weighted average number of shares outstanding, for the effects of all dilutive potential ordinary shares.
- The objective of diluted earnings per share is consistent with that of basic earnings per share—to provide a measure of the interest of each ordinary share in the performance of an entity—while giving effect to all dilutive potential ordinary shares outstanding during the period. As a result:
  - profit or loss attributable to ordinary equity holders of the parent entity is increased by the after-tax amount of dividend and interest recognised in the period in respect of the dilutive potential ordinary shares and is adjusted for any other changes in income or expense that would result from the conversion of the dilutive potential ordinary shares; and
  - the weighted average number of ordinary shares outstanding is increased by the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

The formula can be mathematically expressed as follows:

$$\frac{\text{Profit/Loss attributable to Equity share holders when dilutive potential shares are converted into ordinary shares}}{\text{Weighted average number of Equity shares + Weighted average number of dilutive potential ordinary shares}}$$

2.7.2 Earnings

- For the purpose of calculating diluted earnings per share, an entity shall adjust profit or loss attributable to ordinary equity holders of the parent entity, by the after-tax effect of:

  (a) any dividend or other items related to dilutive potential ordinary shares is deducted in arriving at profit or loss attributable to ordinary equity holders of the parent entity;

  (b) any interest recognised in the period related to dilutive potential ordinary shares; and

(c) any other changes in income or expense that would result from the conversion of the dilutive potential ordinary shares.

- After the potential ordinary shares are converted into ordinary shares, the new ordinary shares are entitled to participate in profit or loss attributable to ordinary equity holders of the parent entity. Therefore, profit or loss attributable to ordinary equity holders of the parent entity is adjusted for the items in (a)-(c) above and any related taxes. The expenses associated with potential ordinary shares include transaction costs and discounts accounted for in accordance with the effective interest method under Ind AS 109.

Illustration 7

Entity A has in issue 25,000 4% debentures with a nominal value of ₹ 1. The debentures are convertible to ordinary shares at a rate of 1:1 at any time until 20X9. The entity's management receives a bonus based on 1% of profit before tax.

Entity A's results for 20X2 showed a profit before tax of ₹ 80,000 and a profit after tax of ₹ 64,000 (for simplicity, a tax rate of 20% is assumed in this question).

Calculate Earnings for the purpose of diluted EPS.

Solution

For the purpose of calculating diluted EPS, the earnings should be adjusted for the reduction in the interest charge that would occur if the debentures were converted, and for the increase in the management bonus payment that would arise from the increased profit.

	Amount (₹)
Profit after tax	64,000
Add: Reduction in interest cost (25,000 × 4%) (*Refer Note*)	1,000
Less: Tax expense (1,000 × 20%)	(200)
Less: Increase in management bonus (1,000 × 1%)	(10)
Add: Tax benefit (10 × 20%)	2
Earnings for the purpose of diluted EPS	**64,792**

Note : For simplicity, this illustration does not classify the components of the convertible debenture as liabilities and equity, as required by Ind AS 32.

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2.7.3 Shares

2.7.3.1 Base for calculation

For the purpose of calculating diluted earnings per share, the number of ordinary shares shall be the weighted average number of ordinary shares ***plus*** the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares. Dilutive potential ordinary shares shall be deemed to have been converted into ordinary shares at the beginning of the period or, if later, the date of the issue of the potential ordinary shares.

2.7.3.2 Calculation of Weighted average to be done independently for every period

- Dilutive potential ordinary shares shall be determined independently for each period presented. The number of dilutive potential ordinary shares included in the year-to-date period is not a weighted average of the dilutive potential ordinary shares included in each interim computation.

- Potential ordinary shares are weighted for the period they are outstanding. Potential ordinary shares that are cancelled or allowed to lapse during the period are included in the calculation of diluted earnings per share only for the portion of the period during which they are outstanding. Potential ordinary shares that are converted into ordinary shares during the period are included in the calculation of diluted earnings per share from the beginning of the period to the date of conversion; from the date of conversion, the resulting ordinary shares are included in both basic and diluted earnings per share.

- All potential ordinary shares are assumed converted into ordinary shares at the beginning of the period or, if not in existence at the beginning of the period, at the date of issue of the potential ordinary shares. The date of issue is the date the financial instrument was issued or the granting of the rights by which they are generated. This is sometimes referred to as the 'if converted' method.

- The conversion into ordinary shares should be determined from the terms of the financial instrument or the rights granted. This determination should assume the most advantageous conversion rate or exercise price from the standpoint of the holder of the potential ordinary shares.

- Only potential ordinary shares that are dilutive are considered in the calculation of diluted EPS. Potential ordinary shares should be treated as dilutive only when their conversion to ordinary shares would decrease profit per share or increase loss per share from continuing operations attributable to ordinary equity holders.

- The effects of anti-dilutive potential ordinary shares are ignored in calculating diluted EPS. An entity might have a number of different types of potential ordinary shares in issue. Each one would need to be considered separately rather than in aggregate.
- Convertible preference shares are dilutive where the amount of dividend on such shares, declared or accrued in the period per ordinary share obtainable on conversion, is below basic EPS for continuing operations. If the amount exceeds basic EPS, the convertible preference shares are anti-dilutive.

Illustration 8

ABC Ltd. has 1,000,000 ₹ 1 ordinary shares and 1,000 ₹ 100 10% convertible bonds (issued at par), each convertible into 20 ordinary shares on demand, all of which have been in issue for the whole of the reporting period.

ABC Ltd.'s share price is ₹ 4.50 per share and earnings for the period are ₹ 500,000. The tax rate applicable to the entity is 21%.

Calculate basic EPS, earnings per incremental share for the convertible bonds and diluted EPS.

Ignore the requirements of Financial Instruments (Ind AS 109) for the purpose of this question.

Solution

Basic EPS is ₹ 0.50 per share (ie 500,000/1,000,000)

The earnings per incremental share for the convertible bonds is calculated as follows:

Earnings effect = No. of bonds x nominal value x interest cost x (1 – applicable tax rate)

= 1,000 x 100 x 10% x (1- 0.21) = ₹ 7,900.

Incremental shares calculation

Assume all bonds are converted to shares, even though this converts ₹ 100 worth of bonds into 20 shares worth only ₹ 90 and is therefore not economically rational.

This gives 1000 x 20 = 20,000 additional shares.

Earnings per incremental share = ₹ 7,900 / 20,000 = ₹ 0.395

Diluted EPS = (₹ 500,000 + ₹ 7,900) / (1,000,000 + 20,000)

= ₹ 0.498 per share.

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Illustration 9

At 30 June 20X1, the issued share capital of an entity consisted of 1,500,000 ordinary shares of ₹ 1 each. On 1 October 20X1, the entity issued ₹ 1,250,000 of 8% convertible loan stock for cash at par. Each ₹ 100 nominal value of the loan stock may be converted, at any time during the years ended 20X6 to 20X9, into the number of ordinary shares set out below:

30 June 20X6: 135 ordinary shares;

30 June 20X7: 130 ordinary shares;

30 June 20X8: 125 ordinary shares; and

30 June 20X9: 120 ordinary shares.

If the loan stocks are not converted by 20X9, they would be redeemed at par.

The written equity conversion option is accounted for as a derivative liability and marked to market through profit or loss. The change in the options' fair value reported in 20X2 and 20X3 amounted to losses of ₹ 2,500 and ₹ 2,650 respectively. It is assumed that there are no tax consequences arising from these losses.

The profit before interest, fair value movements and taxation for the year ended 30 June 20X2 and 20X3 amounted to ₹ 825,000 and ₹ 895,000 respectively and relate wholly to continuing operations. The rate of tax for both periods is 33%.

Calculate Basic and Diluted EPS.

Solution

	20X3	**20X2**
Trading results	**₹**	**₹**
A. Profit before interest, fair value movements and tax	895,000	825,000
B. Interest on 8% convertible loan stock (20X2: 9/12 × ₹100,000)	(100,000)	(75,000)
C. Change in fair value of embedded option	(2,650)	(2,500)
Profit before tax	792,350	747,500
Taxation @ 33% on (A-B)	(262,350)	(247,500)
Profit after tax	**530,000**	**500,000**
Calculation of basic EPS		
Number of equity shares outstanding	1,500,000	1,500,000
Earnings	₹ 530,000	₹ 500,000
Basic EPS	35 paise	33 paise

Calculation of diluted EPS

Test whether convertibles are dilutive:

The saving in after-tax earnings, resulting from the conversion of ₹ 100 nominal of loan stock, amounts to ₹ 100 × 8% × 67% + ₹ 2,650/12,500 = ₹ 5.36 + ₹ 0.21 = ₹ 5.57.

There will then be 135 extra shares in issue.

Therefore, the incremental EPS is 4 paise (ie. ₹ 5.57/135). As this incremental EPS is less than the basic EPS at the continuing level, it will have the effect of reducing the basic EPS of 35 paise. Hence the convertibles are dilutive.

	20X3	20X2
Adjusted earnings	₹	₹
Profit for basic EPS	530,000	500,000
Add: Interest and other charges on earnings saved	102,650	77,500
as a result of the conversion	(100,000 + 2,650)	(75000+ 2500)
Less: Tax relief thereon	(33,000)	(24,750)
Adjusted earnings for equity	**599,650**	**552,750**

Adjusted number of shares

From the conversion terms, it is clear that the maximum number of shares issuable on conversion of ₹ 1,250,000 loan stock after the end of the financial year would be at the rate of 135 shares per ₹ 100 nominal (that is, 1,687,500 shares).

	20X3	20X2
Number of equity shares for basic EPS	1,500,000	1,500,000
Maximum conversion at date of issue 1,687,500 × 9/12		1,265,625
Maximum conversion after balance sheet date	1,687,500	–
Adjusted shares	**3,187,500**	**2,765,625**
Adjusted earnings for equity	₹ 599,650	₹ 552,750
Diluted EPS (approx.)	**19 paise**	**20 paise**

Note: Since Effective Interest Rate is not given, splitting of the convertible loan into liability and equity components as envisaged under Ind AS 109 cannot be done. However, since fair values of derivatives are given, the same is considered for accounting at FVTPL.

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2.7.3.3 Shares of subsidiary, joint venture or associate

A subsidiary, joint venture or associate may issue to parties other than the parent or investors with joint control of, or significant influence over, the investee potential ordinary shares that are convertible into either ordinary shares of the subsidiary, joint venture or associate, or ordinary shares of the parent or investors with joint control of, or significant influence (the reporting entity) over, the investee. If these potential ordinary shares of the subsidiary, joint venture or associate have a dilutive effect on the basic earnings per share of the reporting entity, they are included in the calculation of diluted earnings per share.

2.7.3.4 Options, warrants and their equivalents

- For the purpose of calculating diluted earnings per share, an entity shall assume the exercise of dilutive options and warrants of the entity. The assumed proceeds from these instruments shall be regarded as having been received from the issue of ordinary shares at the average market price of ordinary shares during the period. The difference between the number of ordinary shares issued and the number of ordinary shares that would have been issued at the average market price of ordinary shares during the period shall be treated as an issue of ordinary shares for no consideration.

- Options and warrants are dilutive when they would result in the *issue of ordinary shares for less than the average market price of ordinary shares during the period.* The amount of the dilution is the average market price of ordinary shares during the period minus the issue price. Therefore, to calculate diluted earnings per share, potential ordinary shares are treated as consisting of both the following:

  (a) a contract to issue a certain number of the ordinary shares at their average market price during the period. Such ordinary shares are assumed to be fairly priced and to be neither dilutive nor antidilutive. They are ignored in the calculation of diluted earnings per share.

  (b) a contract to issue the remaining ordinary shares for no consideration. Such ordinary shares generate no proceeds and have no effect on profit or loss attributable to ordinary shares outstanding. Therefore, such shares are dilutive and are added to the number of ordinary shares outstanding in the calculation of diluted earnings per share.

Treatment of options, warrants and their equivalents

If it is a contract to issue a certain number of ordinary shares **at their average market price** during the period	If it is a contract to issue remaining ordinary shares **for no consideration**
↓	↓
Shares are assumed to be fairly priced	They generate no proceeds and have no effect on profit or loss
↓	↓
These shares are neither dilutive nor antidilutive	Such shares are dilutive
↓	↓
Ignore in the calculation of diluted earnings per share	Add to the number of ordinary shares outstanding in the calculation of Diluted EPS

Examples 8-10

8. ABC Ltd. has issued 20 lacs shares. It has also issued 1 lac warrants convertible into shares at ₹ 45 per share. The average market price of shares during the current period was ₹ 45.

   Such shares are assumed to be fairly priced, and to be neither dilutive, nor anti-dilutive. They are ignored in the calculation of diluted earnings per share.

9. ABC Ltd. has issued 20 lacs shares. It has also issued 1 lac warrants convertible into shares at ₹ 30 per share. The average market price of shares during the current period was ₹ 37. ₹ 7 (i.e. ₹ 37 - ₹ 30) is the dilution per share of the warrants.

   Such shares generate no proceeds and have no effect on profit attributable to the ordinary shares outstanding. They are dilutive and are added to the number of shares outstanding in the calculation of diluted earnings per share.

10. In 20X1, ABC Ltd. issued some staff share options that can be exercised after 3 years' service. They are treated as outstanding on the grant date in 20X1 for diluted earnings per share purposes.

Illustration 10

At 31 December 20X7 and 20X8, the issued share capital of an entity consisted of 4,000,000 ordinary shares of ₹ 25 each. The entity has granted options that give holders the right to *subscribe for ordinary shares between 20Y6 and 20Y9 at ₹ 70 per share. Options outstanding at 31 December 20X7 and 20X8 were 630,000. There were no grants, exercises or lapses of options during the year. The profit after tax, attributable to ordinary equity holders for the years ended 31 December 20X7 and 20X8, amounted to ₹ 500,000 and ₹ 600,000 respectively (wholly relating to continuing operations).*

Average market price of share:

Year ended 31 December 20X7 = ₹ 120

Year ended 31 December 20X8 = ₹ 160

Calculate basic and diluted EPS.

Solution

	20X8	**20X7**
Calculation of basic EPS		
Profit after tax	₹ 600,000	₹ 500,000
Number of share	4,000,000	4,000,000
Basic EPS (approx.)	15 paise	13 paise.
Calculation of diluted EPS		
Adjusted number of shares		
Number of shares under option:		
Issued at full market price:		
(630,000 × 70) ÷ 120		367,500
(630,000 × 70) ÷ 160	275,625	
Issued at nil consideration — dilutive	354,375	262,500
Total number of shares under option	630,000	630,000
Number of equity shares for basic EPS	4,000,000	4,000,000
Number of dilutive shares under option	354,375	262,500
Adjusted number of shares (A)	4,354,375	4,262,500
Profit after tax (B)	₹ 600,000	₹ 500,000
Diluted EPS (B/A)	14 paise	12 paise

Note: *If options had been granted or exercised during the period, the number of 'nil consideration' shares in respect of these options would be included in the diluted EPS calculation on a weighted average basis for the period prior to exercise.*

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- **Options and warrants have a dilutive effect only when the average market price of ordinary shares during the period exceeds the exercise price** of the options or warrants (i.e. they are 'in the money'). Previously reported earnings per share are not retroactively adjusted to reflect changes in prices of ordinary shares.
- For share options and other share-based payment arrangements to which Ind AS 102, *Share-based Payment,* applies, the issue price and the exercise price shall include the fair value (measured in accordance with Ind AS 102) of any goods or services to be supplied to the entity in the future under the share option or other share-based payment arrangement.

2.7.3.5 Employee Stock Options

Employee share options with fixed or determinable terms and non-vested ordinary shares are treated as options in the calculation of diluted earnings per share, even though they may be contingent on vesting. They are treated as outstanding on the grant date. Performance-based employee share options are treated as contingently issuable shares because their issue is contingent upon satisfying specified conditions in addition to the passage of time.

Illustration 11- Effects of share options on diluted earnings per share

Profit attributable to ordinary equity holders of the parent entity for year 20X1	*₹ 1,200,000*
Weighted average number of ordinary shares outstanding during year 20X1	*500,000 shares*
Average market price of one ordinary share during year 20X1	*₹ 20.00*
Weighted average number of shares under option during year 20X1	*100,000 shares*
Exercise price for shares under option during year 20X1	*₹ 15.00*

Calculate basic and diluted EPS.

Solution

Calculation of earnings per share

	Earnings	***Shares***	***Per share***
Profit attributable to ordinary equity holders of the parent entity for year 20X1	₹ 1,200,000		
Weighted average shares outstanding during year 20X1		500,000	
Basic earnings per share			**₹ 2.40**
Weighted average number of shares under option		100,000	

Weighted average number of shares that would have been issued at average market price: (100,000 × ₹ 15.00) ÷ ₹ 20.00	Refer Note	(75,000)	
Diluted earnings per share	**₹ 1,200,000**	**525,000**	**₹ 2.29**

Note: Earnings have not increased because the total number of shares has increased only by the number of shares (25,000) deemed to have been issued for no consideration.

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2.7.3.6 Convertible instruments

- The dilutive effect of convertible instruments shall be reflected in diluted earnings per share.
- Convertible preference shares are antidilutive whenever the amount of the dividend on such shares declared in or accumulated for the current period per ordinary share obtainable on conversion exceeds basic earnings per share. Similarly, convertible debt is antidilutive whenever its interest (net of tax and other changes in income or expense) per ordinary share obtainable on conversion exceeds basic earnings per share.
- The redemption or induced conversion of convertible preference shares may affect only a portion of the previously outstanding convertible preference shares. In such cases, any excess consideration is attributed to those shares that are redeemed or converted for the purpose of determining whether the remaining outstanding preference shares are dilutive. The shares redeemed or converted are considered separately from those shares that are not redeemed or converted.

2.7.3.7 Contingently issuable shares

- As in the calculation of basic earnings per share, contingently issuable ordinary shares are treated as outstanding and included in the calculation of diluted earnings per share if the conditions are satisfied (i.e. the events have occurred). Contingently issuable shares are included from the beginning of the period (or from the date of the contingent share agreement, if later). If the conditions are not satisfied, the number of contingently issuable shares included in the diluted earnings per share calculation is based on the number of shares that would be issuable if the end of the period were the end of the contingency period. Restatement is not permitted if the conditions are not met when the contingency period expires.
- If attainment or maintenance of a specified amount of earnings for a period is the condition for contingent issue and if that amount has been attained at the end of the reporting period but must be maintained beyond the end of the reporting period for an additional period, then

the additional ordinary shares are treated as outstanding, if the effect is dilutive, when calculating diluted earnings per share. In that case, the calculation of diluted earnings per share is based on the number of ordinary shares that would be issued if the amount of earnings at the end of the reporting period were the amount of earnings at the end of the contingency period. Because earnings may change in a future period, the calculation of basic earnings per share does not include such contingently issuable ordinary shares until the end of the contingency period because not all necessary conditions have been satisfied.

- The number of ordinary shares contingently issuable may depend on the future market price of the ordinary shares. In that case, if the effect is dilutive, the calculation of diluted earnings per share is based on the number of ordinary shares that would be issued if the market price at the end of the reporting period were the market price at the end of the contingency period. If the condition is based on an average of market prices over a period of time that extends beyond the end of the reporting period, the average for the period of time that has lapsed is used. Because the market price may change in a future period, the calculation of basic earnings per share does not include such contingently issuable ordinary shares until the end of the contingency period because not all necessary conditions have been satisfied.

- The number of ordinary shares contingently issuable may depend on future earnings and future prices of the ordinary shares. In such cases, the number of ordinary shares included in the diluted earnings per share calculation is based on both conditions (ie earnings to date and the current market price at the end of the reporting period). Contingently issuable ordinary shares are not included in the diluted earnings per share calculation unless both conditions are met.

- In other cases, the number of ordinary shares contingently issuable depends on a condition other than earnings or market price (for example, the opening of a specific number of retail stores). In such cases, assuming that the present status of the condition remains unchanged until the end of the contingency period, the contingently issuable ordinary shares are included in the calculation of diluted earnings per share according to the status at the end of the reporting period.

- Contingently issuable potential ordinary shares (other than those covered by a contingent share agreement, such as contingently issuable convertible instruments) are included in the calculation of diluted earnings per share as follows:

  - An entity determines whether the potential ordinary shares may be assumed to be issuable on the basis of the conditions specified for their issue in accordance with the contingent ordinary share provisions; and

- if those potential ordinary shares are to be reflected in diluted earnings per share, an entity determines their impact on the calculation of diluted earnings per share by following the provisions for options and warrants, the provisions for convertible instruments, the provisions for contracts that may be settled in ordinary shares or cash, or other provisions, as appropriate.

- However, exercise or conversion is not assumed for the purpose of calculating diluted earnings per share unless exercise or conversion of similar outstanding potential ordinary shares that are not contingently issuable is assumed.

Illustration 12- Contingently issuable shares

Ordinary shares outstanding during 20X1	*1,000,000 (there were no options, warrants or convertible instruments outstanding during the period)*

An agreement related to a recent business combination provides for the issue of additional ordinary shares based on the following conditions:

	5,000 additional ordinary shares for each new retail site opened during 20X1
	1,000 additional ordinary shares for each ₹ 1,000 of consolidated profit in excess of ₹ 2,000,000 for the year ended 31 December 20X1
Retail sites opened during the year:	*one on 1 May 20X1*
	one on 1 September 20X1
Consolidated year-to-date profit attributable to ordinary equity holders of the parent entity:	*₹ 1,100,000 as of 31 March 20X1*
	₹ 2,300,000 as of 30 June 20X1
	₹ 1,900,000 as of 30 September 20X1 (including a ₹ 450,000 loss from a discontinued operation)
	₹ 2,900,000 as of 31 December 20X1

Calculate basic and diluted EPS on quarterly as well as annual basis.

Solution

					Basic earnings per share
	First quarter	***Second quarter***	***Third quarter***	***Fourth quarter***	***Full year***
Numerator (₹)	1,100,000	1,200,000	(400,000)	1,000,000	2,900,000
Denominator:					
Ordinary shares outstanding	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Retail site contingency	–	3,333[6]	6,667[7]	10,000	5,000[8]
Earnings contingency[9]	–	–	–	–	–
Total shares	1,000,000	1,003,333	1,006,667	1,010,000	1,005,000
Basic earnings per share (₹)	1.10	1.20	(0.40)	0.99	2.89

6 5,000 shares × $^{2}/_{3}$

7 5,000 shares + (5,000 shares × $^{1}/_{3}$)

8 (5,000 shares × $^{8}/_{12}$) + (5,000 shares × $^{4}/_{12}$)

9 The earnings contingency has no effect on basic earnings per share because it is not certain that the condition is satisfied until the end of the contingency period. Profits for the year are determined / finalized on after Q4 / year is completed, i.e. in the year 20X2. Thus, the earliest when these shares can be actually issued is on 1 Jan 20X2.

					Diluted earnings per share
	First quarter	***Second quarter***	***Third quarter***	***Fourth quarter***	***Full year***
Numerator (₹)	1,100,000	1,200,000	(400,000)	1,000,000	2,900,000
Denominator:					
Ordinary shares outstanding	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Retail site contingency	–	5,000	10,000	10,000	10,000
Earnings contingency	–[10]	300,000[11]	–[12]	900,000[13]	900,000
Total shares	1,000,000	1,305,000	1,010,000	1,910,000	1,910,000
Diluted earnings per share (₹)	1.10	0.92	(0.40)[14]	0.52	1.52

10 Company A does not have year-to-date profit exceeding ₹ 2,000,000 at 31 March 20X1. The Standard does not permit projecting future earnings levels and including the related contingent shares.

11 Each quarter is treated as an independent reporting period and hence if the conditions are fulfilled during the quarter, the contingent shares are considered for Diluted EPS right from the beginning of the reporting period i.e., the quarter in the said case. [(₹ 2,300,000 – ₹ 2,000,000) ÷ 1,000] × 1,000 shares = 300,000 shares.

12 Year-to-date profit is less than ₹ 2,000,000.

13 [(₹ 2,900,000 – ₹ 2,000,000) ÷ 1,000] × 1,000 shares = 900,000 shares.

14 Because the loss during the third quarter is attributable to a loss from a discontinued operation, the antidilution rules do not apply. The control number (ie profit or loss from, continuing operations attributable to the equity holders of the parent entity) is positive. Accordingly, the effect of potential ordinary shares is included in the calculation of diluted earnings per share.

*****

2.7.3.8 Entity with discontinued operations

An entity that reports a discontinued operation should use income from continuing operations, adjusted for preferred dividends and similar adjustments, if any, as the "control number" in determining whether potential common shares are dilutive. That is, the same number of potential common shares used in computing the diluted per-share amount of income from continuing operations should be used in computing all other reported diluted per-share amounts even if the effect will be anti-dilutive compared to their respective basic per-share amounts.

Illustration 13

Assume the following facts for Company XY:

-	*Income from continuing operations:*	*INR 30,00,000*
-	*Loss from discontinued operations:*	*(INR 36,00,000)*
-	*Net loss:*	*(INR 6,00,000)*
-	*Weighted average Number of shares outstanding*	*10,00,000*
-	*Incremental common shares outstanding relating to stock options*	*2,00,000*

(a) You are required to calculate the basic and diluted EPS for Company XY from the above information.

(b) Assume, if in above case, Loss from continued operations is ₹ 10,00,000 and income from discontinued operations is ₹ 36,00,000 calculate the diluted EPS.

Solution:

(a) Step 1:

Basic EPS = Profit for the year / Weighted average Number of shares outstanding

Basic EPS (Continued Operations) = Profit from continued operations / Weighted average Number of shares outstanding

= ₹ 30,00,000 / 10,00,000 = ₹ 3.00

Basic Loss per share (Discontinued operations)	=	Loss from discontinued operations / Weighted average Number of shares outstanding
	=	₹ (36,00,000) / 10,00,000 = (₹ 3.60)
Overall Basic Loss per share	=	(₹ 6,00,000) / 10,00,000 = ₹ (0.60) (i)

Step 2: Calculation of Diluted EPS

Diluted EPS	=	Profit for the year / Adjusted Weighted average Number of shares outstanding
EPS (Continued Operations)	=	Profit from continued operations / Adjusted Weighted average Number of shares outstanding
	=	₹ 30,00,000 / 12,00,000 = ₹ 2.50
Loss per share (Discontinued operations)	=	Loss from discontinued operations / Adjusted weighted average number of shares outstanding
	=	₹ (36,00,000) / 12,00,000 = (₹ 3.00)
Overall Diluted Loss per share	=	₹ (6,00,000) / 12,00,000 = ₹ (0.50) (ii)

The income from continuing operations is the control number, there is a dilution in basic EPS for income from continuing operations (reduction of EPS from ₹ 3.00 to ₹ 2.50). Therefore, even though there is an anti-dilution [Loss per share reduced from ₹ 0.60 (i) to ₹ 0.50 (ii) above], diluted loss per share of ₹ 0.50 is reported.

(b) In case of loss from continuing operations, the potential shares are excluded since including those shares would result into anti-dilution effect on the **control number** (loss from continuing operations). Therefore, the diluted EPS will be calculated as under:

Diluted EPS	=	Profit for the year / Adjusted Weighted average Number of shares outstanding
Overall Profit	=	Loss from continuing operations + Gain from discontinued operations
	=	₹ (10,00,000) + ₹ 36,00,000 = ₹ 26,00,000
Weighted average number of shares outstanding	=	10,00,000
Diluted EPS	=	₹ 2.60

The dilutive effect of the potential common shares on EPS for income from discontinued operations and net income would not be reported because of the loss from continuing operations.

*****

2.7.3.9 Contracts that may be settled in ordinary shares or cash

- When an entity has issued a contract that may be settled in ordinary shares or cash at the entity's option, the entity shall presume that the contract will be settled in ordinary shares, and the resulting potential ordinary shares shall be included in diluted earnings per share if the effect is dilutive.
- When an issued contract that may be settled in ordinary shares or cash at the entity's option may give rise to an asset or a liability, or a hybrid instrument with both an equity and a liability component under Ind AS 32, the entity should adjust the numerator (profit or loss attributable to ordinary equity holders) for any changes in the profit or loss that would have resulted during the period if the contract had been classified wholly as an equity instrument.
- For contracts that may be settled in ordinary shares or cash at the holder's option, the more dilutive of cash settlement and share settlement shall be used in calculating diluted earnings per share.

An example of a contract that may be settled in ordinary shares or cash is a debt instrument that, on maturity, gives the entity the unrestricted right to settle the principal amount in cash or in its own ordinary shares.

Another example is a written put option that gives the holder a choice of settling in ordinary shares or cash.

Illustration 14

An entity issues 2,000 convertible bonds at the beginning of Year 1. The bonds have a three-year term and are issued at par with a face value of ₹ 1,000 per bond, giving total proceeds of ₹ 2,000,000. Interest is payable annually in arrears at a nominal annual interest rate of 6 per cent. Each bond is convertible at any time up to maturity into 250 ordinary shares. The entity has an option to settle the principal amount of the convertible bonds in ordinary shares or in cash.

When the bonds are issued, the prevailing market interest rate for similar debt without a conversion option is 9 per cent. At the issue date, the market price of one ordinary share is ₹ 3. Income tax is ignored. Entity has accounted for the convertible instrument using the principles of Financial Instruments.

Interest @ 6% for the year has already been adjusted in the profit attributable to shareholders.

Calculate basic and diluted EPS when

Profit attributable to ordinary equity holders of the parent entity Year 1	*₹ 1,000,000*
Ordinary shares outstanding	*1,200,000*
Convertible bonds outstanding	*2,000*

Solution

Assumption: Entity intends to settle only interest in cash

Allocation of proceeds of the bond issue:	
Liability component (Refer Note 1)	₹ 303,755
Equity component	₹ 1,696,245
	₹ 2,000,000

The liability and equity components would be determined in accordance with Ind AS 32. These amounts are recognised as the initial carrying amounts of the liability and equity components. The amount assigned to the issuer conversion option equity element is an addition to equity and is not adjusted.

Basic earnings per share Year 1:

$$\frac{₹1,000,000}{1,200,000} = ₹\ 0.83 \text{ per ordinary share}$$

Diluted earnings per share Year 1:

It is presumed that the issuer will settle the contract by the issue of ordinary shares. The dilutive effect is therefore calculated in accordance with the Standard.

$$\frac{₹1,000,000 + ₹27,338}{1,200,000 + 500,000} = ₹\ 0.60 \text{ per ordinary share}$$

Notes:

1. This represents the present value of the interest discounted at 9% – ₹ 120,000 payable annually in arrears for three years. ₹ 2,000,000 assumed to be settled in equity since option is with the entity will not form part of liability.

2. Profit is adjusted for the accretion of ₹ 27,338 (₹303,755 x 9%) of the liability because of the passage of time.

3. 500,000 ordinary shares = 250 ordinary shares x 2,000 convertible bonds.

*****

2.7.3.10 Purchased options

- Contracts such as purchased put options and purchased call options (ie options held by the entity on its own ordinary shares) are not included in the calculation of diluted earnings per share because including them would be antidilutive. The put option would be exercised only if the exercise price were higher than the market price and the call option would be exercised only if the exercise price were lower than the market price.

2.7.3.11 Written put options

♦ Contracts that require the entity to repurchase its own shares, such as written put options and forward purchase contracts, are reflected in the calculation of diluted earnings per share if the effect is dilutive. If these contracts are 'in the money' during the period (ie the exercise or settlement price is above the average market price for that period), the potential dilutive effect on earnings per share shall be calculated as follows:

(a) it shall be assumed that at the beginning of the period sufficient ordinary shares will be issued (at the average market price during the period) to raise proceeds to satisfy the contract;

(b) it shall be assumed that the proceeds from the issue are used to satisfy the contract (ie to buy back ordinary shares); and

(c) the incremental ordinary shares (the difference between the number of ordinary shares assumed issued and the number of ordinary shares received from satisfying the contract) shall be included in the calculation of diluted earnings per share.

Written put options

Example 11

Assume that an entity has 160 written put options outstanding on 160 of its ordinary shares, with an exercise price of ₹ 10 per option. The put obligation is therefore ₹ 1,600. The average market price of the entity's ordinary shares is ₹ 8 for the period. In calculating diluted EPS, the entity assumes that it issues 200 ordinary shares at ₹ 8 per share to raise the proceeds necessary to satisfy the put option. The difference between the 200 ordinary shares assumed to be issued and the 160 ordinary shares that would have been received on exercise of the option (that is, 40 shares) is added to the denominator (number of shares) in calculating the diluted EPS. No adjustments are made to the numerator (profit attributable to ordinary shareholders), because the shares are deemed issued for nil proceeds.

2.8 RETROSPECTIVE ADJUSTMENTS

♦ Diluted EPS of any prior period presented should not be restated for changes in the assumptions used (such as for contingently issuable shares) or for the conversion of potential ordinary shares (such as convertible debt) outstanding at the end of the previous period.

These factors are already taken into account in calculating the basic and, where applicable, the diluted EPS for the current period. Prior period's EPS data should be restated for the effects of errors and adjustments resulting from changes to accounting policies accounted for retrospectively.

- Basic and diluted EPS figures for the current period and for prior periods should include bonus issues, share splits, share consolidations and other similar events occurring during the period that change the number of shares in issue without a corresponding change in the resources of the entity (that is, retrospective application).

2.9 PRESENTATION

- An entity shall present in the statement of profit and loss basic and diluted earnings per share for profit or loss from continuing operations attributable to the ordinary equity holders of the parent entity and for profit or loss attributable to the ordinary equity holders of the parent entity for the period for each class of ordinary shares that has a different right to share in profit for the period. An entity shall present basic and diluted earnings per share with equal prominence for all periods presented.

- Earnings per share is presented for every period for which a statement of profit and loss is presented. If diluted earnings per share is reported for at least one period, it shall be reported for all periods presented, even if it equals basic earnings per share. If basic and diluted earnings per share are equal, dual presentation can be accomplished in one line in the statement of profit and loss.

- If a company does not have any potential ordinary shares, then the company's basic and diluted EPS will be same. In such a case, the company need not disclose Basic EPS and Diluted EPS separately. It may disclose basic and diluted EPS as follows (illustrative numbers only):

	20X1	20X0
Basic and Diluted EPS	3.60	2.45

- An entity that reports a discontinued operation shall disclose the basic and diluted amounts per share for the discontinued operation either in the statement of profit and loss or in the notes.

An entity shall present basic and diluted earnings per share, even if the amounts are negative (ie a loss per share).

2.10 DISCLOSURE

- An entity shall disclose the following:

  (a) The amounts used as the numerators in calculating basic and diluted earnings per share, and a reconciliation of those amounts to profit or loss attributable to the parent entity for the period. The reconciliation shall include the individual effect of each class of instruments that affects earnings per share.

  (b) the weighted average number of ordinary shares used as the denominator in calculating basic and diluted earnings per share, and a reconciliation of these denominators to each other. The reconciliation shall include the individual effect of each class of instruments that affects earnings per share.

  (c) instruments (including contingently issuable shares) that could potentially dilute basic earnings per share in the future but were not included in the calculation of diluted earnings per share because they are antidilutive for the period(s) presented.

  (d) a description of ordinary share transactions or potential ordinary share transactions (other than those arising from capitalisation, bonus issue, share split or reverse share split), that occur after the reporting period and that would have changed significantly the number of ordinary shares or potential ordinary shares outstanding at the end of the period if those transactions had occurred before the end of the reporting period.

  Examples of transactions in this para include:

  (a) an issue of shares for cash;

  (b) an issue of shares when the proceeds are used to repay debt or preference shares outstanding at the end of the reporting period;

  (c) the redemption of ordinary shares outstanding;

  (d) the conversion or exercise of potential ordinary shares outstanding at the end of the reporting period into ordinary shares;

  (e) an issue of options, warrants, or convertible instruments; and

  (f) the achievement of conditions that would result in the issue of contingently issuable shares. Earnings per share amounts are not adjusted for such transactions occurring after the reporting period because such transactions do not affect the amount of capital used to produce profit or loss for the period.

- Financial instruments and other contracts generating potential ordinary shares may incorporate terms and conditions that affect the measurement of basic and diluted earnings per share. These terms and conditions may determine whether any potential ordinary shares are dilutive and, if so, the effect on the weighted average number of shares outstanding and any consequent adjustments to profit or loss attributable to ordinary equity holders. The disclosure of the terms and conditions of such financial instruments and other contracts is encouraged, if not otherwise required.
- If an entity discloses, in addition to basic and diluted earnings per share, amounts per share using a reported component of the statement of profit and loss other than one required by this Standard, such amounts shall be calculated using the weighted average number of ordinary shares determined in accordance with this Standard.
- Basic and diluted amounts per share relating to such a component shall be disclosed with equal prominence and presented in the notes. An entity shall indicate the basis on which the numerator(s) is (are) determined, including whether amounts per share are before tax or after tax. If a component of the statement of profit and loss is used that is not reported as a line item in the statement of profit and loss, a reconciliation shall be provided between the component used and a line item that is reported in the statement of profit and loss.

2.11 ADDITIONAL TOPICS

2.11.1 Participating equity instruments and two-class ordinary shares

- The equity of some entities includes:
  - (a) instruments that participate in dividend with ordinary shares according to a predetermined formula (for example, two for one) with, at times, an upper limit on the extent of participation (for example, up to, but not beyond, a specified amount per share).
  - (b) a class of ordinary shares with a different dividend rate from that of another class of ordinary shares but without prior or senior rights.
- For the purpose of calculating diluted earnings per share, conversion is assumed for those instruments that are convertible into ordinary shares if the effect is dilutive. For those instruments that are not convertible into a class of ordinary shares, profit or loss for the period is allocated to the different classes of shares and participating equity instruments in

accordance with their dividend rights or other rights to participate in undistributed earnings. To calculate basic and diluted earnings per share:

(a) profit or loss attributable to ordinary equity holders of the parent entity is adjusted (a profit reduced and a loss increased) by the amount of dividend declared in the period for each class of shares and by the contractual amount of dividend (or interest on participating bonds) that must be paid for the period (for example, unpaid cumulative dividend).

(b) the remaining profit or loss is allocated to ordinary shares and participating equity instruments to the extent that each instrument shares in earnings as if all of the profit or loss for the period had been distributed. The total profit or loss allocated to each class of equity instrument is determined by adding together the amount allocated for dividend and the amount allocated for a participation feature.

(c) the total amount of profit or loss allocated to each class of equity instrument is divided by the number of outstanding instruments to which the earnings are allocated to determine the earnings per share for the instrument.

♦ For the calculation of diluted earnings per share, all potential ordinary shares assumed to have been issued are included in outstanding ordinary shares.

Illustration 15

An entity has two classes of shares in issue:

- *5,000 non-convertible preference shares*
- *10,000 ordinary shares*

The preference shares are entitled to a fixed dividend of ₹ 5 per share before any dividends are paid on the ordinary shares. Ordinary dividends are then paid in which the preference shareholders do not participate. Each preference share then participates in any additional ordinary dividend above ₹ 2 at a rate of 50% of any additional dividend payable on an ordinary share.

The entity's profit for the year is ₹ 100,000, and dividends of ₹ 2 per share are declared on the ordinary shares.

Compute the allocation of earnings for the purpose of calculation of Basic EPS when an entity has ordinary shares & participating equity instruments that are not convertible into ordinary shares.

Solution

The calculation of basic EPS is as follows:

	₹	₹
Profit		100,000
Less: Dividends payable for the period:		
Preference (5,000 × ₹ 5)	25,000	
Ordinary (10,000 × ₹ 2)	20,000	(45,000)
Undistributed earnings		55,000

Allocation of undistributed earnings:

Allocation per ordinary share = A

Allocation per preference share = B where B = 50% of A

(A × 10,000) + (50% × A × 5,000) = ₹ 55,000

A = 55,000 / (10,000 + 2,500) = ₹ 4.4

B = 50% of A i.e. B = ₹ 2.2

Dividend per share are:	**Preference shares ₹ per share**	**Ordinary shares ₹ per share**
Distributed earnings	5.00	2.00
Undistributed earnings	2.20	4.40
Totals	**7.20**	**6.40**

Proof: (5,000 × ₹ 7.2) + (10,000 × ₹ 6.4) = ₹100,000

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Illustration 16

(This illustration does not illustrate the classification of the components of convertible financial instruments as liabilities and equity or the classification of related interest and dividends as expenses and equity as required by Ind AS 32).

Profit for the year	*₹ 100,000*
Ordinary shares outstanding	*10,000*
Non-convertible preference shares	*6,000*
Non-cumulative annual dividend on preference shares (before any dividend is paid on ordinary shares)	*₹ 5.50 per share*

After ordinary shares have been paid a dividend of ₹ 2.10 per share, the preference shares participate in any additional dividends on a 20:80 ratio with ordinary shares.

Compute the allocation of earnings for the purpose of calculation of Basic EPS when an entity has ordinary shares & participating equity instruments that are not convertible into ordinary shares.

Solution

Dividends on preference shares paid (6000 x ₹ 5.50 per share)	₹ 33,000
Dividends on ordinary shares paid (10,000 x ₹ 2.10 per share)	₹ 21,000

Basic earnings per share is calculated as follows:	**₹**	**₹**
Profit attributable to equity holders of the parent entity		100,000
Less: Dividend paid:		
Preference	33,000	
Ordinary	21,000	(54,000)
Undistributed earnings		46,000

Allocation of undistributed earnings:

Allocation per ordinary share = A

Allocation per preference share = B; B = $^1/_4$ A

$(A \times 10{,}000) + (^1/_4 \times A \times 6{,}000) = ₹\ 46{,}000$

$A = ₹\ 46{,}000 \div (10{,}000 + 1{,}500)$

$A = ₹\ 4.00$

$B = {^1/_4}\ A$

B = Re. 1.00

Dividend per share:		
	Preference shares	**Ordinary shares**
Distributed earnings	₹ 5.50	₹ 2.10
Undistributed earnings	₹ 1.00	₹ 4.00
Totals	**₹ 6.50**	**₹ 6.10**

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2.11.2 Partly paid shares

- Where ordinary shares are issued but not fully paid, they are treated in the calculation of basic earnings per share as a fraction of an ordinary share to the extent that they were entitled to participate in dividend during the period relative to a fully paid ordinary share.
- To the extent that partly paid shares are not entitled to participate in dividend during the period they are treated as the equivalent of warrants or options in the calculation of diluted earnings per share. The unpaid balance is assumed to represent proceeds used to purchase ordinary shares. The number of shares included in diluted earnings per share is the difference between the number of shares subscribed and the number of shares assumed to be purchased.

Illustration 17

An entity issues 100,000 ordinary shares of ₹ 1 each for a consideration of ₹ 2.50 per share. Cash of ₹ 1.75 per share was received by the balance sheet date. The partly paid shares are entitled to participate in dividends for the period in proportion to the amount paid.

Calculate number of shares for calculation of Basic EPS.

Solution

The number of ordinary share equivalents that would be included in the basic EPS calculation on a weighted basis is as follows:

(100,000 × ₹ 1.75) / ₹ 2.50 = 70,000 shares.

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2.12 EXTRACTS OF FINANCIAL STATEMENTS OF LISTED ENTITIES

Extracts from Annual reports of Hindustan Unilever Ltd.

(All amounts in ₹ crores, unless otherwise stated)

Particulars	Note	Year ended 31st March, 2022	Year ended 31st March, 2021
OTHER COMPREHENSIVE INCOME			
Items that will not be reclassified subsequently to profit or loss			
Remeasurements of the net defined benefit plans	39C	41	(3)
Income tax relating to items that will not be reclassified subsequently to profit or loss			
Remeasurements of the net defined benefit plans	9A	(10)	1
Items that will be reclassified subsequently to profit or loss			
Fair value of debt instruments through other comprehensive income	18C	(1)	(0)
Fair value of cash flow hedges through other comprehensive income	18C	85	70
Income tax relating to items that will be reclassified subsequently to profit or loss			
Fair value of debt instruments through other comprehensive income	9A	0	0
Fair value of cash flow hedges through other comprehensive income	9A	(0)	(47)
OTHER COMPREHENSIVE INCOME FOR THE YEAR (B)		**115**	**21**
TOTAL COMPREHENSIVE INCOME FOR THE YEAR (A+B)		**8,933**	**7,975**
Earnings per equity share			
Basic (Face value of ₹1 each)	35	₹37.53	₹33.85
Diluted (Face value of ₹1 each)	35	₹37.53	₹33.85
Basis of preparation, measurement and significant accounting policies	2		

NOTE 35 EARNINGS PER EQUITY SHARE

Basic earnings per share is computed by dividing the net profit for the period attributable to the equity shareholders of the Company by the weighted average number of equity shares outstanding during the period. The weighted average number of equity shares outstanding during the period and for all periods presented is adjusted for events, such as bonus shares, other than the conversion of potential equity shares that have changed the number of equity shares outstanding, without a corresponding change in resources.

For the purpose of calculating diluted earnings per share, the net profit for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period is adjusted for the effects of all dilutive potential equity shares.

	Year ended 31st March, 2022	Year ended 31st March, 2021
Earnings Per Share has been computed as under:		
Profit for the year	8,818	7,954
Weighted average number of equity shares outstanding during the year	2,34,95,87,637	2,34,95,42,101
Earnings Per Share (₹) - Basic (Face value of ₹1 per share)	₹37.53	₹33.85
Add: Weighted average number of potential equity shares on account of employee stock options/performance share schemes *	3,625	50,297
Weighted average number of Equity shares (including dilutive shares) outstanding during the year	2,34,95,91,262	2,34,95,92,398
Earnings Per Share (₹) - Diluted (Face value of ₹1 per share)	₹37.53	₹33.85

* Pertains to ESOP shares vested during the year, no outstanding share options as at 31st March, 2022

(Source: Annual Report for 2021-2022 of Hindustan Unilever Ltd.)

Larsen and Toubro Ltd. (Extract of Statement of Profit and Loss)

Statement of Profit and Loss for the year ended March 31, 2022 (contd.)

₹ crore

	Note	2021-22	2021-22	2020-21	2020-21
Brought forward - other comprehensive income			58.02		39.36
B Items that will be reclassified to Profit or Loss:					
Debt instruments through other comprehensive income		(177.90)		239.46	
Income tax (expenses)/income on debt instruments through other comprehensive income		40.70		(54.79)	
			(137.20)		184.67
Exchange differences in translating the financial statements of foreign operations		(26.59)		17.56	
Income tax (expenses)/income on exchange differences in translating the financial statements of foreign operations		6.69		(4.42)	
			(19.90)		13.14
Effective portion of gains/(losses) on hedging instruments in a cash flow hedge		69.17		218.43	
Income tax (expenses)/income on effective portion of gains/(losses) on hedging instruments in a cash flow hedge		(8.59)		(69.74)	
			60.58		148.69
Cost of hedging reserve		3.06		11.80	
Income tax (expenses)/income on cost of hedging reserve		(0.77)		(2.97)	
			2.29		8.83
Other comprehensive income for the year (net of tax)			(36.21)		394.69
Total comprehensive income for the year			7843.24		12192.48
Earnings per share (EPS) of ₹ 2 each from continuing operations:					
Basic earnings per equity share (₹)	49		56.09		22.41
Diluted earnings per equity share (₹)	49		56.03		22.39
Earnings per share (EPS) of ₹ 2 each from discontinued operations:					
Basic earnings per equity share (₹)	49		–		61.61
Diluted earnings per equity share (₹)	49		–		61.54
Earnings per share (EPS) of ₹ 2 each from continuing operations & discontinued operations:					
Basic earnings per equity share (₹)	49		56.09		84.02
Diluted earnings per equity share (₹)	49		56.03		83.93
Face value per equity share (₹)			2.00		2.00
NOTES FORMING PART OF THE FINANCIAL STATEMENTS	1 to 65				

NOTE [49]

Basic and diluted Earnings per Share [EPS] computed in accordance with Ind AS 33 "Earnings per Share":

Particulars		2021-22	2020-21
Basic earnings per share			
Profit after tax from continuing operations as per accounts (₹ crore)	A	7879.45	3147.31
Profit after tax from discontinued operations as per accounts (₹ crore)	B	–	8650.48
Profit after tax from continuing and discontinued operations as per accounts (₹ crore)	C=A+B	7879.45	11797.79
Weighted average number of equity shares outstanding	D	1,40,47,47,700	1,40,41,46,937
Basic EPS from continuing operations(₹)	A/D	56.09	22.41
Basic EPS from discontinued operations(₹)	B/D	–	61.61
Basic EPS from continuing discontinued operations(₹)	C/D	56.09	84.02
Diluted earnings per share			
Profit after tax from continuing operations as per accounts (₹ crore)	A	7879.45	3147.31
Profit after tax from discontinued operations as per accounts (₹ crore)	B	–	8650.48
Profit after tax from continuing and discontinued operations as per accounts (₹ crore)	C=A+B	7879.45	11797.79
Weighted average number of equity shares outstanding	D	1,40,47,47,700	1,40,41,46,937
Add: Weighted average number of potential equity shares on account of employee stock options	E	15,40,580	14,20,264
Weighted average number of equity shares outstanding for diluted EPS	F=D+E	1,40,62,88,280	1,40,55,67,202
Diluted EPS from continuing operations(₹)	A/F	56.03	22.39
Diluted EPS from discontinued operations(₹)	B/F	–	61.54
Diluted EPS from continuing discontinued operations(₹)	C/F	56.03	83.93
Face value per share (₹)		2	2

(Source: Annual Report for 2021-2022 of Larsen and Toubro Ltd.)

Reliance Industries Ltd. (Statement of Profit and Loss)

Statement of Profit and Loss

For the year ended 31st March, 2022

(₹ in crore)

	Notes	2021-22	2020-21
Income			
Value of Sales		4,63,067	2,76,181
Income from Services		3,358	2,759
Value of Sales & Services (Revenue)		4,66,425	2,78,940
Less: GST Recovered		21,050	13,871
Revenue from Operations	26	4,45,375	2,65,069
Other Income	27	13,872	14,818
Total Income		4,59,247	2,79,887
Expenses			
Cost of Material Consumed		3,20,852	1,68,262
Purchase of Stock-in-Trade		10,691	7,301
Changes in Inventories of Finished Goods, Work-in-Progress and Stock-in-Trade	28	(7,962)	610
Excise Duty		21,672	19,402
Employee Benefits Expense	29	5,426	5,024
Finance Costs	30	9,123	16,211
Depreciation / Amortisation and Depletion Expense	1	10,276	9,199
Other Expenses	31	42,383	30,970
Total Expenses		4,12,461	2,56,979
Profit Before Exceptional Item and Tax		46,786	22,908
Exceptional Item (Net of Tax)	32	-	4,304
Profit Before Tax *		46,786	27,212
Tax Expenses *			
Current Tax	12	787	-
Deferred Tax	19	6,915	(4,732)
Profit for the Year		39,084	31,944
Other Comprehensive Income			
i. Items that will not be reclassified to Profit or Loss	27.1	241	350
ii. Income tax relating to items that will not be reclassified to Profit or Loss		(58)	(79)
iii. Items that will be reclassified to Profit or Loss	27.2	(2,705)	2,755
iv. Income tax relating to items that will be reclassified to Profit or Loss		543	(456)
Total Other Comprehensive Income/ (Loss) for the Year (Net of Tax)		(1,979)	2,570
Total Comprehensive Income for the Year		37,105	34,514
Earnings per Equity Share of Face Value of ₹ 10 Each			
Basic (in ₹) - After Exceptional Item	33	59.24	49.66
Basic (in ₹) - Before Exceptional Item	33	59.24	42.97
Diluted (in ₹) - After Exceptional Item	33	58.49	48.90
Diluted (in ₹) - Before Exceptional Item	33	58.49	42.31
Significant Accounting Policies See accompanying Notes to the Financial Statements	1 to 47		

(₹ in crore)

	2021-22	2020-21
33. Earnings Per Share (EPS)		
Face Value per Equity Share (₹)	10	10
Basic Earnings per Share (₹) - After Exceptional Item	59.24	49.66
Basic Earnings per Share (₹) - Before Exceptional Item	59.24	42.97
Net Profit after Tax as per Statement of Profit and Loss attributable to Equity Shareholders (₹ in crore) - After Exceptional Item	39,084	31,944
Net Profit after Tax as per Statement of Profit and Loss attributable to Equity Shareholders (₹ in crore) - Before Exceptional Item	39,084	27,640
Weighted Average number of Equity Shares used as denominator for calculating Basic EPS	6,59,81,11,978	6,43,28,74,848
Diluted Earnings per Share (₹) - After Exceptional Item	58.49	48.90
Diluted Earnings per Share (₹) - Before Exceptional Item	58.49	42.31
Net Profit after Tax as per Statement of Profit and Loss attributable to Equity Shareholders (₹ in crore) - After Exceptional Item	39,084	31,944
Net Profit after Tax as per Statement of Profit and Loss attributable to Equity Shareholders (₹ in crore) - Before Exceptional Item	39,084	27,640
Weighted Average number of Equity Shares used as denominator for calculating Diluted EPS	6,68,16,52,444	6,53,21,38,901
Reconciliation of Weighted Average Number of Shares Outstanding		
Weighted Average number of Equity Shares used as denominator for calculating Basic EPS ^	6,59,81,11,978	6,43,28,74,848
Total Weighted Average Potential Equity Shares *	8,35,40,466	9,92,64,053
Weighted Average number of Equity Shares used as denominator for calculating Diluted EPS	6,68,16,52,444	6,53,21,38,901

* Dilutive impact of Employee Stock Option Scheme and Partly paid Rights Issue Shares

^ Refer Note 14.9

(Source: Annual Report for 2021-2022 of Reliance Industries Ltd.)

2.13 SIGNIFICANT DIFFERENCES BETWEEN IND AS 33 AND AS 20

S. No.	Particulars	Ind AS 33	AS 20
1.	Additional disclosures	Disclosure is required for instruments (including contingently issuable shares) that could potentially dilute basic earnings per share in the future but were not included in the calculation of diluted earnings per share because they are anti-dilutive for the periods presented.	Certain additional disclosures required under Ind AS not required here.
2.	Mandatorily convertible instrument	Ordinary shares to be issued upon conversion of a mandatorily convertible instrument are included in the calculation of basic EPS from the date the contract is entered into.	No specific requirement as in Ind AS.
3.	Shares issuable after a passage of time	Ordinary shares that are issuable solely after a passage of time are not treated as contingently issuable shares because passage of time is a certainty.	No specific guidance.
4.	Contingently returnable shares	Outstanding ordinary shares that are contingently returnable are not treated as outstanding and are ignored in the calculation of basic EPS until the shares are no longer subject to recall.	No guidance on contingently returnable shares.

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. ABC Ltd

1 January 20X1	Shares in issue 1,000,000		
31 March 20X1	(a)	Rights issue 1 for 5 at 90 paise	
	(b)	Fair value of shares ₹ 1 (cum-rights price)	

Calculate the number of shares for use in the EPS calculation for the calendar year.

2.

1 January	Shares in issue	1,000,000
	5% Convertible bonds	₹ 100,000

(terms of conversion 120 ordinary shares for ₹ 100)

31 March Holders of ₹ 25,000 bonds converted to ordinary shares.

Profit for the year ended 31 December ₹ 200,000

Tax rate 30%.

Calculate basic and diluted EPS. Ignore the need to split the convertible bonds into liability and equity elements.

3.

1 January	Shares in issue	1,000,000
	Profit for the year ended 31 December	₹ 100,000
	Average fair value during period	₹ 8

The company has in issue 200,000 options to purchase equal ordinary shares

Exercise price ₹ 6

Calculate the diluted EPS for the period.

4. Calculate Basic EPS for period ending 20X0, 20X1 and 20X2, when

	20X0	20X1	20X2
Profit attributable to ordinary equity holders of the parent entity	₹ 1,100	₹ 1,500	₹ 1,800
Shares outstanding before rights issue			500 shares
Rights issue			One new share for each five outstanding shares
Exercise price			₹ 5.00
Date of rights issue			1 January 20X1
Last date to exercise rights			1 March 20X1
Market price of one ordinary share immediately before exercise on 1st March 20X1:			₹ 11.00
Reporting date			31 December

5. Calculate Subsidiary's and Group's Basic EPS and Diluted EPS, when

Parent:	
Profit attributable to ordinary equity holders of the parent entity	₹ 12,000 (excluding any earnings of, or dividends paid by, the subsidiary)
Ordinary shares outstanding	10,000
Instruments of subsidiary owned by the parent	800 ordinary shares
	30 warrants exercisable to purchase ordinary shares of subsidiary
	300 convertible preference shares
Subsidiary:	
Profit	₹ 5,400
Ordinary shares outstanding	1,000
Warrants	150, exercisable to purchase ordinary shares of the subsidiary
Exercise price	₹ 10

Average market price of one ordinary share	₹ 20
Convertible preference shares	400, each convertible into one ordinary share
Dividends on preference shares	₹ 1 per share
No inter-company eliminations or adjustments were necessary except for dividends.	
Ignore income taxes. Also, ignore classification of the components of convertible financial instruments as liabilities and equity or the classification of related interest and dividends as expenses and equity as required by Ind AS 32.	

Answers

1. Rights issue bonus fraction

	Shares	₹ per share	₹
Cum-rights	5	1	5.0
Rights	1	0.9	0.9
Ex-rights	**6**		**5.9**

Theoretical ex-rights price (5.9 / 6) = 0.9833

Bonus fraction = Cum-rights price / Theoretical ex-rights price

= 1/0.9833

	Number of shares
1 January - 31 March (1,000,000 × 3/12 × 1/.9833)	254,237
1 April - 31 December (1,200,000 × 9/12)	900,000
	1,154,237

2.

	Number of shares	Profit ₹
Profit		200,000
Ourdinary shares	1,000,000	
New shares on conversion (weighted average)		
9/12 × ₹ 25,000 / 100 × 120	22,500	-
Figures for basic EPS	1,022,500	200,000

Basic EPS is (₹ 200,000 / 1,022,500) = 0.196 per share		
Dilution adjustments		
Unconverted shares ₹ 75,000 / 100 × 120	90,000	
Interest: ₹ 75,000 × 5% × 0.7 (net of tax)		2,625
Converted shares pre conversion adjustment		
3/12 × ₹ 25,000 / 100 × 120	7,500	
Interest: [3/12 × ₹ 25,000 × 5% × 0.7]		219
	1,120,000	**202,844**
Diluted EPS is (₹ 202,844 / 1,120,000) = 0.181		

3. **Diluted EPS**

	Number of Shares	Profit (₹)	EPS
Basic	1,000,000	100,000	0.10
Dilution (Refer W.N.)	50,000	–	–
	1,050,000	100,000	0.095

Working Notes:

Proceeds of issue	(200,000 × ₹ 6)	=	1,200,000
Number that would have been issued at Fair value (1,200,000 / ₹ 8)		=	150,000
Number actually issued			200,000
Number for "free" (200,000 – 150,000)			50,000

4. **Calculation of theoretical ex-rights value per share**

$$\frac{\text{Fair value of all outstanding shares before the exercise of rights + total amount received from exercise of rights}}{\text{Number of shares outstanding before exercise + number of shares issued in the exercise}}$$

$$\frac{(₹11.00 \times 500 \text{ shares}) + (₹5.00 \times 100 \text{ shares})}{500 \text{ shares} + 100 \text{ shares}}$$

Theoretical ex-rights value per share = ₹10.00

Calculation of adjustment factor

$$\frac{\text{Fair value per share before exercise of rights}}{\text{Theoretical ex-rights value per share}} \quad \frac{₹\ 11.00}{₹\ 10.00} = 1.10$$

Calculation of basic earnings per share

	20X0	20X1	20X2
20X0 Basic EPS as originally reported: ₹1,100 / 500 shares	₹ 2.20		
20X0 Basic EPS restated for rights: ₹1,100/(500 shares x 1.1)	₹ 2.00		
20X1 Basic EPS including effects of rights issue:		₹ 2.54	
{₹1,500 / [(500 x 1.1 x 2/12) + (600x10/12)]}			
20X2 Basic EPS: ₹ 1,800 / 600 shares		₹ 3.00	

5. Subsidiary's earnings per share

Basic EPS ₹ 5.00 calculated: $\dfrac{\text{₹ 5,400 (a) – ₹400 (b)}}{\text{1,000 (c)}}$

Diluted EPS ₹ 3.66 calculated: $\dfrac{\text{₹ 5,400 (d)}}{\text{(1,000 + 75 (e) + 400(f))}}$

Notes:

(a) Subsidiary's profit attributable to ordinary equity holders.

(b) Dividends paid by subsidiary on convertible preference shares.

(c) Subsidiary's ordinary shares outstanding.

(d) Subsidiary's profit attributable to ordinary equity holders (₹ 5,000) increased by ₹ 400 preference dividends for the purpose of calculating diluted earnings per share.

(e) Incremental shares from warrants, calculated: [(₹ 20 – ₹ 10) ÷ ₹ 20] × 150.

(f) Subsidiary's ordinary shares assumed outstanding from conversion of convertible preference shares, calculated: 400 convertible preference shares × conversion factor of 1.

Consolidated earnings per share

Basic EPS ₹ 1.63 calculated: $\dfrac{\text{₹ 12,000(a) + ₹ 4,300(b)}}{\text{10,000(c)}}$

Diluted EPS ₹ 1.61 calculated: $\dfrac{\text{₹ 12,000 + ₹ 2,928(d) + ₹ 55(e) + ₹ 1,098(f)}}{\text{10,000}}$

(a) Parent's profit attributable to ordinary equity holders of the parent entity.

(b) Portion of subsidiary's profit to be included in consolidated basic earnings per share, calculated: (800 × ₹ 5.00) + (300 × Re 1.00).

(c) Parent's ordinary shares outstanding.

(d) Parent's proportionate interest in subsidiary's earnings attributable to ordinary shares, calculated: (800 ÷ 1,000) × (1,000 shares × ₹ 3.66 per share).

(e) Parent's proportionate interest in subsidiary's earnings attributable to warrants, calculated: (30 ÷ 150) × (75 incremental shares × ₹ 3.66 per share).

(f) Parent's proportionate interest in subsidiary's earnings attributable to convertible preference shares, calculated: (300 ÷ 400) × (400 shares from conversion × ₹ 3.66 per share).