UNIVERSITY OF CALICUT

SCHOOL OF DISTANCE EDUCATION

STUDY MATERIAL

(II Semester)

CORE COURSE

B.Com

(2019 ADMISSION ONWARDS)

FINANCIAL ACCOUNTING (BCM2B02)

CORE COURSE

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STUDY MATERIAL

CORE COURSE

FINANCIAL ACCOUNTING

UNIVERSITY OF CALICUT

SCHOOL OF DISTANCE EDUCATION

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UNIVERSITY OF CALICUT

SCHOOL OF DISTANCE EDUCATION

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B.Com
(2019 ADMISSION ONWARDS)

CORE COURSE

FINANCIAL ACCOUNTING

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MODULE 1

ACCOUNTING FROM INCOMPLETE RECORDS-SINGLE ENTRY SYSTEM

Modern financial accounting is based on double entry system. under double entry system, both the aspect of a transaction (debit and credit) are recorded. As a result, all personal. Real and nominal accounts are opened. But this method requires more time, efforts and money. Hence small sole proprietor and partnership firms do not follow strict rules of double entry system. They maintain only cash book and personal accounts. No other accounts or records are maintained. This method of accounting known as single entry system.

Single entry system is a system of accounting, which does not follow the double entry principles. Under this system, accounts relating to debtors and creditors are maintained. Kohler defines single entry system as "a system of book keeping which as a rule only records of cash and personal accounts are maintained, it is always incomplete double entry varying with circumstances"

Features of single entry system

(i) Maintenance of personal accounts

(ii) Maintenance of cashbook

(iii) Dependence on original vouchers

(iv) It does not follow strict double entry principles

(v) The system may differ from firm to firm and therefore, no uniformity.

(vi) The system suitable in case of small firms, partnership firm. Hence, it is not suitable for corporates

Merits

(ii) It is simple method of accounting

(iii) It is economical

(iv) It is suitable for small enterprises

(v) It is possible to record transactions quickly

Demerits

1. Arithmetical accuracy cannot be checked
2. Nominal accounts are not maintained
3. It does not record of all assets and liability
4. Financial position of business cannot be judged
5. True profit cannot be ascertained
6. It is not suitable for limited companies
7. It is not acceptable to income tax authorities

Difference between single Entry system and double entry system

Basis for Comparison	Single Entry System	Double Entry System
Meaning	The system of accounting in which only one sided entry is required to record financial transactions is Single Entry System.	The accounting system, in which every transaction affects two accounts simultaneously is known as the Double Entry System.
Nature	Simple	Complex
Type of recording	Incomplete	Complete
Errors	Hard to identify	Easy to locate
Ledger	Personal and Cash Account	Personal, Real and Nominal Account
Preferable for	Small Enterprises	Big Enterprises
Preparation of Financial Statement	Difficult	Easy
Suitable for tax purposes	No	Yes
Financial position	Cannot be ascertained easily.	Can be ascertained easily.
Arithmetical Accuracy	No	yes

Types of Single Entry System

1. Pure Single Entry System: In this method, only the personal accounts are maintained and there is no information present, concerning the sales and purchases, cash in hand, and bank balance.
2. Simple Single Entry System: In a simple single entry system, cash book is maintained along with the personal accounts and these are maintained as per double entry system of bookkeeping. Cash received or paid, from/to business debtors or creditors are merely written on the bills issued or received.

3. Quasi Single Entry System: In this system, subsidiary books such as sales book, purchases book, bills receivable book and bills payable book are maintained in addition to cash book and personal accounts.

Statement of Affairs

Statement of affairs (SOA) is also identified as a record of financial position of a particular business entity at a given time. The key purpose of SOA is to afford relevant information for the interested parties such as shareholders, customers, employees, competitor, etc. Rather than exhibiting book values of the assets and liabilities, SOA considers the amount at which the organization can recover after selling off their assets and settling their outside obligations.

Difference between Statement of Affaires and balance sheet

Basis of Difference	Balance Sheet	Statement of Affairs
1. Objective	Main objective of making balance sheet is to show the financial position of any organisation.	Main objective of making statement of affairs to find the opening and closing capital in single entry system and in the liquidation of company, to find surplus or deficiency on the basis of estimated value of assets and liabilities of company.
2. System of Book Keeping	It follows double entry system of book keeping	It follows the single entry system of book keeping.

3. Arithmetical Correctness	When balance sheet's both side are matched, it means, it shows also the arithmetical correctness. Because it is prepared from trial balance and trial balance is prepared from the balance of ledger accounts.	It does not prove the arithmetical correctness because it is prepared just information of accounting record. It is not prepared on the basis of trial balance.
4. Actual and Estimated Value	All assets and liabilities are shown on the actual value.	All assets and liabilities are shown on the basis of estimation.
5. Finding of Mistake	If we forget to show any asset or liability, our balance sheet will not match. With this, we can find the mistake.	Because all the assets and liabilities are shown on our past estimation, so, if we forget any asset or liability, we can not find from statement of affair because due to wrong estimation, we can show less or more value of asset or liability.
6. Proof in Court	Court accepts balance sheet as proof of valid information.	Court does not accept it as proof of financial position of organisation because there is chance of wrong estimation of assets and liabilities.

Difference between profit and loss account and Statement of profit or loss

Profit and loss account	Statement of profit and loss
1. It is an account	1. It is a statement
2. It is prepared under double entry	2. It is prepared under single entry

system	system
3. It is starts with gross profit or loss	3. It is starts with closing capital
4. It shows the exact profit or loss	4. It does not show the exact profit or loss
5. It takes into account purchases, sales, returns and all expenses and income from ascertaining profit or loss	5. It takes into account closing and opening capitals for ascertaining profit or loss
6. It is prepared from ledger account balances only	6. It is prepared partly from ledger account balances and partly from estimates, physical verification and memory
7. It gives the reason for earning profit or incurring loss	7. It does not give the reasons for earning profit or incurring loss

Computation of profit

The profit or loss in case of a business maintaining accounts according to single entry system can be computed by two methods namely, statement of affairs method and conversion method.

Statement of affairs method or net worth method

According to this method, the profit or loss made by the business is computed by comparing the capital of the business on two different dates. The following procedure is followed

(a) A statement of affairs at the beginning of the year is prepared to ascertain capital at the beginning.

(b) Closing statement of affairs is prepared to ascertain capital at the end

(c) Profit is ascertained by

Capital at the end	Xxx
Add: drawings	Xx

	Xxxx
Less further capital introduced	Xx
Profit made during the year	-----------
	Xxx

Illustration.1

A keeps his books by single entry system. His position on 1st Jan 2011 was as follows:

Cash at bank	Rs 5000	Machinery and plant -Rs 6500	
Cash in hand	Rs 1000	Bills receivable Rs 2600	
Stock	Rs 7000	creditors Rs 2500	
Sundry debtors	Rs 8400	Bills payable -Rs 4000	

On 31st Dec 2011 his position was as under

Cash at bank	Rs 4300	Machinery and plant	Rs 6500
Cash in hand	Rs 1700	Bills receivable	Rs 3200
Stock	Rs 9000	Creditors	Rs 160
Sundry debtors	Rs 6000	Bills payable -	Rs 3200

During the year a introduced further capital of Rs 2000, and his drawings were Rs. 800 per month

Depreciate machinery and plant by 5% and create a reserve for bad and doubtful debts at 5%.from the above information prepare a statement showing the profit and loss made by him for the year ended 31st Dec 2011

Solution

Statement of affairs as *on 1st Jan 2011*

Liabilities	Rs	Assets	Rs
Creditors	2500	Bank	5000
Bills payable	4000	Cash in hand	1000
Capital(balance)	24000	Stock	7000
		Debtors	8400
		Machinery	6500
		Bills receivable	2600
	30500		30500

Statement of affairs *as on 31 dec 2011*

Liabilities	Rs	Assets	Rs
Creditors	1600	Bank	4300
Bills payable	3200	Cash in hand	1700
Capital(balance)	25275	Stock	9000

		Debtors (6000 5%)	5700
		Machinery (6500 5%)	6175
		Bills receivable	3200
	30075		30075

Statement of profit for the *year ended 31st Dec2011*

Capital as on 31/12/2011	25275
Add: drawings (800*2)	9600
	34875
Less further capital introduced	2000
	32875
Less capital as on 1/1/2011	24000
Profit made during the year	887

Illustration 2

Sri C Sharma commenced business on 1-jan-2003 with a capital of Rs 25000: Rs 20000 brought in cash and the balance in the form of machinery. On 1st October 2003 he introduced Rs 10000 in the business for which Rs 6000 were borrowed from his wife during the year. He withdraw at the rate of Rs 500 a month his position on 31st Dec 2003 was as follows

ASSETS

Stock of goods Rs 12500: sundry debtors Rs 10500: machinery Rs 6000: cash at bank Rs 3000: cash in hand Rs 500: bills receivable: Rs 3800 and furniture Rs 10000

LIABILITIES

Sundry creditors Rs 8500: loan from wife Rs 6000: bills payable Rs 1500

Ascertain his profit for the year ended 31 Dec 2003

Solution **STATEMENT OF AFFAIRS**
As at 31 12 2003

liabilities	₹	Asset	₹
Sundry creditors	8500	Stock	12500
Loan from wife	6000	Sundry debtors	10500
Bills payable	1500	Machinery	6000
Capital(balancing figure)	30300	Cash at bank	3000
		Cash in hand	500
		Bills receivable	3800
		Furniture	10000

	46300		46300

Statement of profit or loss for the year 31/12/2003

Capital at the end 32/12/2003	30300
Add drawings during the year	6000
	36300
Less additional capital introduced	4000
	32300
Less capital at the beginning	25000
Profit earned during the year	7000

Illustration 3

Sri Shankar keeps his books on single entry and following info is disclosed from his records

	31 12 2002(Rs)	31 12 2003(Rs)
Balance at bank	(Cr)2500	5500
Sundry debtors	14000	21000
Furniture	29000	27500
Stock in trade	15000	20000
Investments	6000	6000
Cash in hand	200	500
Sundry creditors	25000	29000
Bills payable	1000	600
Loan from tea pankaj	....	4000

Sri V Shankar transferred Rs 300 per month from the business to his private bank account by way of drawings. In addition, he withdraws Rs 6000 for his daughter's marriage and Rs 500 for charitable purpose. He also withdraws goods worth Rs 2500 for domestic purpose. In august 2003 he had received a lottery price of Rs 6000 of which he invested Rs 3000 in to the business. He sold some private property for Rs 8000 and processed were utilized for the business. He wants his furniture to be depreciated at 10% per annum and a reserve for doubtful debts be created at 6%.he had not paid 2 months' salary to his accountant at the rate of 400 per month and 2 months' rent of the shop was unpaid amounting to Rs 500.interest earned but not received by him was Rs 2100. Prepare a statement of profit and loss for the year ending 31-12-2003.

Solution

To calculate the opening capital, the statement of affairs as at 31-dec-2002 is prepared thus:

Statement of affairs as at 31-12-2002

Liabilities	Rs	Assets	Rs

Bank overdraft	2500	Sundry debtors	14000
Sundry creditors	25000	Furniture	29000
Bills payable	1000	Stock in trade	15000
Capital (bal.fig)	35700	Investment	6000
		Cash in hand	200
	64200		64200

Similarly, a statement of affairs at Dec 31, 2003 will show the closing capital, thus:

Statement of affairs as at 31 -12 -2003

Liabilities	₹	Assets	₹
Sundry creditors	29000	Cash at bank	5500
Bills payable	600	Sundry debtors	21000
Loan from T pankaj	4000	Furniture	27500
Capital (B/F)	46900	Stock in trade	20000
		Investment	6000
		Cash in hand	500
	80500		80500

Then arrive at the profit or loss made by him. During the year a statement of profit or loss is prepared, thus:

Capital at the end (31/12/2003)		46900
Add drawings during the period		12600
		59500
Less additional capital introduced		11000
		48500
Less capital at the beginning		35700
Profit subject to adjustment		12800
Less depreciation on furniture	2750	
10% reserve for doubtful debts	1260	
6% outstanding salary	800	
Outstanding rent	500	5310
		7490
Add interest earned but not received		2100
Net profit transferred to capital		9590

CONVERSION METHOD

Conversion of single entry in to double entry involves the complete process of journalizing, posting, balancing and preparation of trial balance. Then final accounts are to be prepared .if any information is missing, it should be ascertained by preparing the relevant accounts before preparation of final accounts

Following steps are taken

1) Prepare statement of accounts in the beginning so as to ascertain capital in the beginning
2) Prepare cashbooks, cashbook reveals missing figure cash or bank balance at the beginning or at the end as the case may be. Sometimes cashbook reveals the amount of sundry expenses or drawings or cash purchases(if credit side is shorter than debit) or cash sales or sundry incomes or capital introduced(if debit side is shorter than credit side)
3) Then prepare I(1)total debtors account (2) total creditors account,(3) bills receivable account

(4) bills payable account(these accounts help in finding out credit sales, credit purchases, debtors or credit balances

4) After preparing these accounts, calculate total sales by adding credit sales and cash sales total purchases by adding cash purchases and credit purchases
5) Information relating to nominal accounts can be ascertained from the cashbook. Real accounts and amounts outstanding are given by way of information. These accounts can be completed
6) After these it will be possible to prepare final accounts in the usual manner

<u>Specimen</u>

TOTAL DEBTORS ACCOUNT

	Rs		Rs
Opening balance of creditors	Xxx	Cash received from debtors	Xxx
Credit sales	Xxx	Bills receivable received	Xxx
Bills receivable dishonored	Xxx	Discount allowed	Xxx

		Allowances claimed	Xxx
		Return inwards	Xxx
		Bad debts	Xxx
		Transfer to/from creditors	Xxx
		Closing balance of debtors	Xxx
	xxx		Xxx

TOTAL CREDITORS ACCOUNT

	Rs		Rs
Cash paid to creditors	Xxx	Opening balances of creditors	Xxx
Bills payable accepted	Xxx	Credit purchases	Xxx
Discount received	Xxx	Bills payable dishonored	Xxx
Allowances received	Xxx		
Return outwards	Xxx		
Transfer to/ from debtors	Xxx		
Closing balance of creditors	Xxx		Xxxx
	xxxx		

BILLS RECIEVABLE ACCOUNT

	Rs		Rs
Opening balance	Xxx	Cash	Xxx
Sundry debtors	Xxx	(realization of bill)	
(B/R received)		Sundry debtors	Xxx
		(bill returned dishonored)	
	xxxx	Closing balance	Xxx
			Xxxx

BILLS PAYABLE ACCOUNTS

	Rs		Rs
Cash paid	Xxx	Opening balance	Xxx
(on account of bills payable)		Sundry creditors	Xxx
Sundry creditors	Xxx	(bills accepted)	
(B/P dishonored)			Xxxx
Closing balance	Xxx		
	xxxx		

Illustration 4

Ascertain credit sales and purchases from the following figures

Debtors	₹	creditors	₹
Opening balances	10800	opening balances	5900
Cash received	36850	cash paid	24800
Discount allowed	2000	discount received	450
Bad debts written off	450	returns	540
Returns	800	bills payable issued	2860
Bills receivable received	8400	closing balances	6200
Bills receivable dishonored	600		
Closing balance	8700		

Solution

Total debtors account

	Rs		Rs
Balance b/d	10800	Cash	36850
Bills receivable (dishonored)	600	Discount allowed	2000
Credit sales(balancing figure)	45800	Bad debts	450
		Returns	800
		Bills receivable	8400
		Balance c/d	8700
	57200		57200

Total creditors accounts

	Rs		Rs
Cash	24800	Balance b/d	5900
Discount received	450	Credit purchases	
Returns	540	(balancing figure)	28950
Bills payable	2860		
Balance c/d	6200		
	34850		34850

Illustration 5

From the following particulars extracted from the books of a trader kept under the single entry system you are asked to find out the figure for credit sales and credit purchases by preparing the total debtors account and total creditors account show also the bill receivable account and bills payable account.

Balance, 1st Jan 2011	`
Total debtors	18700
Total creditors	8500
Bills receivable	1400
Bills payable	900
Cash received from customers	46500
Cash paid to creditors	24720
Discount allowed to customers	1450
Discount received from suppliers	950
Bad debts written off	850
Returns to suppliers'	435
Returns from customers	945
Cash received against bills receivable	4660
Cash paid against bills payable	2230
Bad debts previously written off, now received	450
Bills receivable dishonored	500
Balance 31st December, 2011	
Total debtors	17800
Total creditors	9400
Bills receivable	350
Bills payable	1050

Solution

Bills receivable account

	₹		₹
Balance b/d	1400	Cash	4660
Sundry debtors	4110	Sundry debtors	500
(balancing figure)		(bills dishonored)	350
	5510	Balance c/d	5510
Balance b/d	350		

Bills payable account

	Rs		Rs
Cash	2230	Balance b/d	900
Balance c/d	1050	Sundry creditors	2380
	3280	(balancing figure)	3280
		Balance b/d	1050

Total debtors account

	Rs		Rs
Balance b/d	18700	Cash	46500
Bills receivable	500	Discount	1450
(dishonored)		Bad debts	850
Sales credit	52455	Returns	945
(balancing figure		Bills receivable	4110
		Balance c/d	17800
	71655		71655

Total creditors account

	₹		₹
Cash	24720	Balance c/d	8500
Discount	950	Purchases credit	29385
Returns	435	(balancing figure)	
Bills payable	2380		
Balance c/d	9400		
	37885		37885
		Balance b/d	940

Illustration 6

From the following data ascertain total sales

	Rs
Balance of debtors on 1-1-2011	24000
Sales returns	10000
Cash received from customers	90000
Discount allowed t them	6000
B/R received	34000

Bad debts	3000
B/R dishonored	7000
Balance of debtors as on 31-12-2011	20000
Cash sales	50000

Balance of debtors as on 31-12-2011	20000
Cash sales	50000

Total debtors account

	Rs		Rs
Balance b/d	24000	Cash	90000
B/R(dishonored)	7000	Discount	6000
Sales(credit balancing figure)	132000	B/R	34000
		Bad debts	3000
		Sales returns	10000
		Balance c/d	20000
	163000		163000

Total Sales=132000+50000=182000

Illustration 7

From the following, ascertain total purchases:

	₹
Balances of creditors on 1 1 2011	14000
Cash paid to creditors	10000
B/P given	10000
Discount allowed by them	500
Return outward	3000
Creditors as on 31 12 2011	25000
Cash purchases	10000

Solution

Total creditors account

	Rs		Rs
Cash	10000	Balance b/d	14000
B/P	10000	Purchases(credit balances)	34500
Discount	500		
Returns	3000		
Balance b/d	25000		
	48500		48500

Total purchases= 34500+10000=44500

Illustration 8

A commenced as a business as a cloth merchant on 1-1-2011 with a capital of rs 10000.on the same date he purchased furniture and fitting for cash 3000

From the following particulars obtained from his books kept by single entry, you are required prepare trading and profit and loss account for the year ending 31st December 2011 and a balance sheet on that date:

Sales (inclusive of cash Rs 7000)	17000
Purchases (inclusive of cash Rs 4000)	15000
A's drawings	1200
Salary to staff	2000
Bad debts written off	500
Business expenses	700

A took cloth worth Rs 500 from the shop for private use and paid Rs 200 to his son, but omitted to record these transactions in his books on 31st December 2011.his sundry debtors were Rs 5200.and sundry creditors Rs 3600.stock in hand on 31st Dec 2011 was Rs 6500.

A's trading & profit and loss account for the year ending 31st Dec 2011

Particulars		₹	Particulars	₹
Purchases	15000		Sales	17000
Less drawings	500	14500	Closing stock	6500
Gross profit c/d		9000		
		23500		23500
Salaries		2000		
Bad debts		500	Gross profit b/d	9000
Business expense		7000		
Net profit		5800		
		9000		9000

A's balance sheet as on 31 December 2011

		Rs		Rs
Sundry creditors		3600	Cash	2800
Capital	10000		Sundry debtors	5200
Less drawings	1900		Closing stock	6500
			Furniture	3000
	81000			
Add net profit	5800			
		13900		
		17500		17500

Working notes:

Sundry debtors account

	Rs		Rs
Sales credit	10000	Cash (balancing figure)	4300
		Bad debt	500
		Balance c/d	5200
	10000		10000

Sundry creditors account

	Rs		Rs
cash (balancing figure)	7400	Purchases – credit	11000
balance c/d	3600		
	11000		11000

Cash account

	Rs		Rs
Capital	10000	Furniture	3000
Sales	7000	Purchases	4000
Debtors	4300	Drawings(1200+200)	1400
		Salaries	2000
		Business expenses	700
		Creditors	7400
		Balance c/d(balance)	2800
	21300		21300

Illustration 9

Sunil keeps his books on single entry system. From the following information provided by him prepare a trading and profit and loss account for the year ended 31st

December 2011 and a balance sheet on that date

Particular	31 12 2010	31 12 2011
Furniture	10000	12000
Stock	6000	3000
Sundry debtors	12000	13000
Prepaid expenses	....	500
Sundry creditors	5000	....
Outstanding expenses	1400	2200
Cash	2400	800

Receipts and payment account during the year was as follows

Received from debtors	40500
Paid to creditors	19000
Carriage inwards	4500
Drawings	10000
Sundry expenses	12500
Furniture purchased	2000

Other information

There were considerable amount of cash sales. Credit purchases during the year amounted to Rs 24000.create a provision of 10% on debtors for doubtful debts.

Receipts	₹	Payment	₹
Balance b/d	2400	Creditors	19000
Debtors	40500	Carriage inwards	4500
Sales (b/f)	5900	Drawings	10000
		Sundry expenses	12500
		Furniture	2000
		Balance c/d	800
	48800		48800
Balance b/d	800		

Total Debtors Account

	₹		₹
balance b/d	12000	Cash	40500
sales (b/f)	41500	Balance b/d	13000
	53500		53500
Balance b/d	13000		

Total Creditors Account

	₹		₹
Cash	19000	Balance b/d	5000
Balance c/d	10000	purchases	24000
	29000		29000
		Balance B/d	10000

Balancesheet as on 31/12/2010

Liabilities	₹	Assets	₹
Outstanding expenses	1400	Cash	2400
Sundry creditors	5000	Debtors	12000
Capital (b/f)	24000	Furniture	10000
		Stock	6000
	30400		30400

Trading and profit and loss *account*

For the year ended31st December 2011

Particulars	₹	Particulars	₹
Opening stock	6000.	Sales:	
Purchases	2400	Cash 5900	
Carriage inwards	4500	Credit 41500	47400
Gross profit	15900	Closing stock	3000
	50400		50400
Sundry expenses 12500		G/P B/d	15900
Less prepaid 500			
Less outstanding(2010) 1400			
Add o/s 2011 2200	12800		
Provision for dd	1300		
Net profit	18000		
	15900		15900

Balance sheet as on 31/12/2011

Liabilities	₹	Assets	₹
Sundry creditors	10000	Furniture	12000
Outstanding expense	2200	Stock	3000
Capital 24000		Debtors 13000	
Add net profit 1800		Less provision 1300	11700
……..		Prepaid expenses	500
25800		cash	800
Less drawings 10000	15800		
	28000		28000

Illustration 10

From the following data, ascertain total sales

Balances of debtors on 1/1/2011	24000	Sales return	10000
Cash received from debtors	90000	Discount allowed to them	6000
BR received	34000	Bad debts	3000
BR dishonoured	7000	Balance of debtors on 31/12/2011	20000
Cash sales	50000		

Solution

Total Debtors A/c

To balance b/d	24000	By cash	90000
,, B/R (dishonored)	7000	,, Discount	6000
,, credit sales (Bal. fig.)	132000	,, B/R	34000
		,, Bad debts	3000
		,, sales returns	10000
		,, balance c/d	20000
	163000		163000

Total sales = 132000+50000 = 182000

Illustration 11

A, B and C were in partnership and towards the end of 2011 most of their records were destroyed by fire. The balance sheet as on 31st Dec. 2010 was as follows

Creditors	5500	Cash	2400
Capital		Debtors	3600
A 4500		Stock	6500
B 3000		Machinery	1440
C 1500	9000	Fixtures and fittings	600
Current Accounts		Advance payment	35
A 145		Current account (c)	170
B 100	245		
	14745		14745

The partner's drawings during 2011 have been provided at A Rs.1400; B Rs. 1000 and C Rs.650; on 31st Dec. 2011, the cash was Rs.3200, Debtors Rs.4045 stock Rs. 5900, Advance payment Rs. 25 and creditors Rs.6040. machinery is to be depreciated by 10% per annum and fixtures and fitting at 7.5%, 5% interest is to be allowed on capital. The partners share profits in the proportion of ½, 1/3 and 1/6.

You are required to prepare a statement showing the net trading profit for the year 2011 and the division of the same between partners, together with the balance sheet as on 31st

Dec.2011

Solution

Statement of affairs of M/s A, B AND C

As on 31st Dec 2011

Liabilities		Rs	Assets		Rs
Creditors		6040	Cash in hand		3200
Capital:			Debtors		4025
A	4500		Advance payment		25
B	3000		Stocks		5900
C	1500		Fixtures and fitting	600	
		9000	Less: 7.5% dep.	45	
					555
			Machinery	1440	
			Less: depreciation	144	
					1296
			Combined current account of A B & C		
					39
		15040			15040

Statement of Profit or loss of A,B and C

For the year ended 31/12/2011

Combined current accounts of A,B and C of 31/12/2011		-39
Add Drawings		
A	1400	
B	1000	
C	650	3050
Less Current Accounts of A,B and C on 1/1/2011		
A (cr)	145	
B (cr)	100	
	245	
	170	75

C (dr)		2936
Profit made during the year before allowing interest on capital Less: interest on capital (5%)		
A (4500 X 5/100)	225	
B (3000 X 5/100)	150	
C (1500 X 5/100)	75	450
		2486
Net profit made during the year		
Share of profit		
A's share = 2486 x ½ =		1243
B's share = 2486 x 1/3 =		828
C's share = 2486 x 1/6 =		415

Balance sheet of M/s A, B and C *as at 31st Dec. 2011*

liabilities		Rs	Assets		Rs
Creditors		6040	Cash		3200
Capital :			Debtors		4025
A	4500		Advance payment		25
B	3000		Stock		5900
C	1500	9000	Fixtures & fitting	600	
			Less: depreciation	45	555
A's Currents A/c					
as on 1 1 .11	145				
			Machinery	1440	
Add: profit	1243				
			Less: depreciation	144	
Add: interest	225				
					1296
			C's current A/c		
	1613				
			as on 1 1 11	170	
Less drawing	1400				
			add: drawing	650	
		213			
B's current A/c :					
				820	
As on 1 1 11	100				
			Less: interest	75	
Add: profit	150				

Add: interest	828			745	
			Less: profit	415	
	1078				
					330
Less : drawing	1000				
		78			
		15331			15331

Illustration 12

Mrs. SAJINA keeps her books of accounts under single entry system. From the following prepare Trading and profit & loss account for the year ended 31-03-2011 together with balance sheet as on that dates

Cash book analysis shows the followings:-

Interest charges	100
Personal withdrawals	2000
Staff salaries	8500
Other business exp.	7900
Payments to creditors	15000

Further details available are:

balance at bank on 31-03-2011	2425
cash in hand as on 31-03-2011	75
received from debtors	25000
cash sales	15000

	As on 1-4-2010	as on 31-3-2011
Stock in hand	9000	10220

Creditors	8000	5500
Debtors	22000	30000
Furniture	1000	1000
Office premises	15000	15000

Provide 5% interest on X's capital balance as on 1-4-2010. Provide Rs. 1500 for D/D, 5% depreciation on all fixed assets. 5% group commission to staff has to be provided for on N/P after meeting all expenses and the commission.

Solution

Trading and profit and loss a/c for the year ended 31 -03 -2011

	Rs.		Rs.
Opening stock	9000	Sales	48000
Purchase	12500	Closing stock	10220
Gross profit c/d	36720		
	58220		58220
	=======		======
Interest	100	Gross profit b/d	36720
Salaries	8500		
Expenses	7900		
Provision for doubtful debts	1500		
Interest on capital	1750		
Depreciation:			
Furniture	50		
Office premises	750		
Group commission	770		
Net profit c/d	15400		
	36720		36720

Balance sheet *as on March 31 2011*

Liabilities	Rs	Assets	Rs
Capital 35000		Premises 15000	

Add: interest	1750		Less: depreciation	750	
Add: net profit	15400				14250
			Furniture	1000	
	52150		Less: depreciation	50	
Less: Drawing	2000	50150			950
			Stock on hand		10220
Creditors		5500	Debtors	30000	
Group commission		770	Less: prov. For D/D	1500	
					28500
			Cash in bank		2425
			Cash in hand		75
		56420			56420

Working note:

(1)

CASH BOOK

2009		Rs.	2008		Rs.
March 31	To debtors	25000	March 31	By Balanceb/d (balance)	4000
	Sales	15000			
			2009 March 31	Interest	100
				Drawing	2000
				salaries	8500
				expenses	7900
				creditors	15000
				balance c/d:	
				bank	2425
				cash in hand	75
		40000			40000

(2) **Statement of affairs** ***as at April1.2010***

Liabilities	₹	Assets	₹
Capital (balance)	35000	Stock in hand	9000
Overdraft	4000	Debtors	22000
Creditors	8000	Furniture	1000
		Office premises	15000
	47000		47000

(3) Total Debtors Account

	Rs		Rs
Opening balance	22000	Cash	25000
Credit sales (bal. fig)	33000	Closing balance	30000
	55000		55000

Total sales = cash sales + credit sales
= Rs.15000+33000=48000

(4)

Total creditors account

Cash	15000	Opening balance	8000
Closing balance	5500	Purchase	12500
	20500		20500

(5)

Gross profit	Rs.36720	
Less: all expenses except commission		20550
Net profit before commission		16170
Commission 16170 x 5/105		770
Net profit after commission		15400

Trial balance

debtors	Rs.	Creditors	Rs.
Opening stock	9000	Creditors	5500
Debtors	30000	Cash sales	15000
Furniture	1000	Credit sales	33000
Premises	15000	capital	35000
Interest charges	100		
Drawing	2000		
Staff salaries	8500		
Business expense	7900		
Purchase	12500		
Cash in hand	75		
Cash at bank	2425		
	88500		88500

Multiple Choice Questions

1. Opening capital is ascertained by preparing:
   (a)Cash book (b)Creditors A/c
   (c)Debtors A/c (d)Opening statement of affairs.
2. A Single entry system it:
   (a)Complete and scientific system
   (b)Incomplete and unscientific
   (c)Incomplete and scientific
   (d)Complete and unscientific
3. Single Entry system has effect:
   (a)One effect (b)Tow effect
   (c)Three effect (d)None of the above
4. In Single entry system, it is not possible to prepare:
   (a)Receipts and payments A/c (b) Trial balance
   (c)Balance sheet (d)Account sales
5. A Single entry system is usually adopted by:
   (a)Company (b) Partnership
   (c)Government (d) None of above
6. Single Entry system is must suited where:
   (a)Cash transactions are many
   (b) Credit transactions are many.
   (c)Cash & credit transactions are more.
   (d) None of the above
7. Capital can be obtained by preparing:
   (a)Cash book (b) Statement of affairs
   (c)Debtors A/c (d) Creditors A/c
8. Credit sale can be obtained by preparing:
   (a)Cash book (b) Statement of affairs
   (c)Debtors A/c (d) Creditors A/c
9. Credit Purchase can be calculated by preparing:
   (a)Cash book (b) Statement of affairs
   (c)Debtors A/c (d) Creditors A/c

10 Cash in hand can be obtained by preparing:

(a)Cash book	(b) Statement of affairs
(c)Debtors A/c	(d) Creditors A/c

Answers

1 d, 2 b, 3.a, 4 b, 5 c, 6 a, 7 b, 8 c, 9 d, 10 a

Short answer type questions

1. What is single entry system?
2. What is meant by accounting from incomplete records?
3. Give two merits of single entry system
4. What do you mean by conversion method?
5. What is "statement of affairs"?
6. What is memorandum trading account?"
7. Name the various types of single entry
8. What do you mean by pure single entry

Short essay type questions

1. What is meant by accounting from complete records? Explain its features
2. What are the objectives of single entry?\
3. Explain the differences between single entry and double entry
4. How are profits ascertained under single entry?
5. What are the differences between statement of affairs and balance sheet
6. State the merits of single entry
7. Explain the limitations of single entry system
8. "Single entry system is not scientific" explain
9. What are the differences between profit and loss account and statement of profit and loss?
10. Explain the procedure of conversion of single entry into double entry.

Reference Books:

1. Chintan Patel, BhupendraMantri, Indian Accounting Standards, TaxmannPublications.
2. T. P, Ghosh , Illustrated Guide To Indian Accounting Standards, TaxmannPublications.

MODULE 2
COMPANY ACCOUNTS

Issue of Shares

The sole proprietorship and partnership forms of organizations have failed to meet the growing needs of modern business and industry. They have many limitations like limited capital , unlimited liability, instability etc. to remove these limitations, joint stock company form of organization came into existence.

A company may be viewed as an association of person who contribute money or money's worth to a common inventory and use it for a common purpose. It is an artificial person having corporate legal entity distinct from its members (shareholders) and has a common seal used for its signature. Thus, it has certain special features which distinguish it from the other forms of organisation. These are as follows:

- Body Corporate: A company is formed according to the provisions of Law enforced from time to time. Generally, in India, the companies are formed and registered under Companies Law except in the case of Banking and Insurance companies for which a separate Law is provided for.
- Separate Legal Entity: A company has a separate legal entity which is distinct and separate from its members. It can hold and deal with any type of property. It can enter into contracts and even open a bank account in its own name.
- Limited Liability: The liability of the members of the company is limited to the extent of unpaid amount of the shares held by them. In the case of the companies limited by guarantee, the liability of its members is limited to the extent of the guarantee given by them in the event of the company being wound up.
- Perpetual Succession: The company being an artificial person created by law continues to exist irrespective of the changes in its membership. A company can be terminated only through law. The death or insanity or insolvency of any

member of the company in no way affects the existence of the company. Members may come and go but the company continues.

- o Common Seal: The company being an artificial person, cannot sign its name by itself. Therefore, every company is required to have its own seal which acts as official signatures of the company. Any document which does not carry the common seal of the company is not binding on the company.
- o Transferability of Shares: The shares of a public limited company are freely transferable. The permission of the company or the consent of any member of the company is not necessary for the transfer of shares. But the Articles of the company can prescribe the manner in which the transfer of shares will be made.
- o May Sue or be Sued: A company being a legal person can enter into contracts and can enforce the contractual rights against others. It can sue and be sued in its name if there is a breach of contract by the company.

Kinds of Companies

Companies can be classified either on the basis of the liability of its members or on the basis of the number of members. On the basis of liability of its members the companies can be classified into the following three categories:

(i) Companies Limited by Shares: In this case, the liability of its members is limited to the extent of the nominal value of shares held by them. If a member has paid the full amount of the shares, there is no liability on his part whatsoever may be the debts of the company. He need not pay a single paise from his private property. However, if there is any liability involved, it can be enforced during the existence of the company as well as during the winding up.

(ii) Companies Limited by Guarantee: In this case, the liability of its members is limited to the amount they undertake to contribute in the event of the company being wound up. Thus, the liability of the members will arise only in the event of its winding up.

(iii) Unlimited Companies: When there is no limit on the liability of its members, the company is called an unlimited company. When the company's property is not sufficient to pay off its debts, the private property of its members can be used for the purpose. In other words, the creditors can claim their dues from its members. Such companies are not found in India even though permitted by the Companies Act, 1956.

On the basis of the number of members, companies can be divided into two categories as follows:

(i) Public Company: A public company means a company which (a) is not a private company, (b) has minimum paid up capital of Rs. 5 lakh rupees or such higher paid-up capital, as may be prescribed and (c) is a company which is not a subsidiary of a private company.

(ii) Private Company: A private company is one which has a minimum paid up capital of Rs. 1 Lakh rupees or such higher paid-up share capital as may be prescribed, and which by its articles:

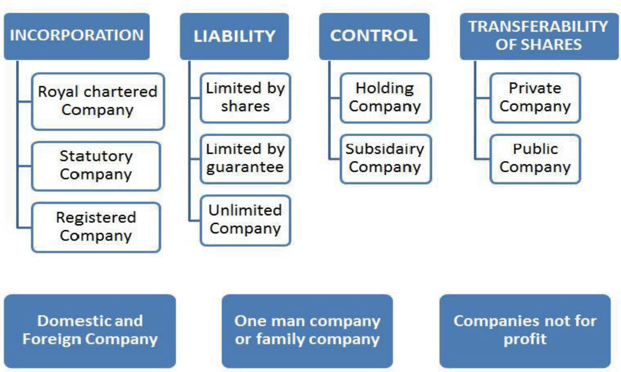
(a) restricts the right to transfer its shares;

(b) limits the number of its members to fifty (excluding its employees);

(c) prohibits any invitation to the public to subscribe for any shares in or debentures of the company.

(d) prohibits any invitation or acceptance of deposits from person other than its members, directors, and relatives.

Kinds of companies under companies Act 2013



1. Royal Chartered Company

Royal Chartered Companies are companies created by the Royal Charter. This means they are granted power or a right by the monarch or by special order of a king or a queen. Examples of Royal Chartered Companies are East India Company, BBC, Bank Of England, etc.

2. Statutory Companies

Statutory Companies are companies incorporated by means of a special act passed by the central or state legislature. They are mostly invested with compulsory powers and are responsible to carry out some special business of national importance. Some examples of statutory companies are The Reserve Bank of India (formed under RBI act, 1934), Life Insurance Corporation of India (formed under LIC Act, 1956).

3. Registered Or Incorporated Companies

All the other companies which are incorporated under the companies act passed by the government comes under this head. These companies come under existence only after they register themselves under the act and the certificate of incorporation is passed by the Registrar of companies. Google India Pvt Ltd is an example of incorporated companies.

4. Public Limited Company

The legal existence of a Public Limited Company is separate from its members (shareholders) and the liability of its members is also limited. Its existence is thus not affected by the retirement or death of its shareholders. A minimum of 7 members is needed to form a Public Limited company but there is no maximum limit on this. The company collects its capital by the sale of its shares to the shareholders. The shareholders of a company do not have the right to participate in the day-to-day management of the company, thus separating ownership from management. All the major decisions of the company are taken by the Board of Directors.

5. Private Limited Company

Private Limited (Pvt Ltd) companies have more than 2 and less than 50 members and their liability is limited or unlimited depending on the type of the company it is. Unlike Public Limited companies, here the transfer of shares is limited to its members and the general public cannot subscribe to its shares and debentures. Pvt Ltd companies are exempted from many rules and regulations which are applicable to Public Limited companies, for example, the need to file a prospectus with the Registrar, the need to hold the statutory general meeting or maintain annual reports etc. Also, it can start operations after receiving just the certificate of incorporation, whereas a Public Limited company needs a certificate of commencement as well. It is a great option if you want the advantages of limited liability and yet want greater control over your business and maintain its privacy. This is the most popular type of company for start-ups to be registered as.

6. One Person Company

One Person Company (OPC) as a company type was introduced in the Companies Act of 2013 in India. It is similar to a sole proprietorship but the owner shall have limited liability and thus his personal assets would not be at risk if losses need to be recovered or if the company is liquidated.

7. Companies Limited By Shares

The liability of the shareholders is limited to the extent of the face value of shares held by them. Most Pvt Ltd companies are of this type.

8. Companies Limited By Guarantee

In these companies, in case of liquidation, the shareholders promise to pay a certain fixed amount to cover the liabilities of the company.

9. Unlimited Companies

There is no limit on the liability of the shareholders. In case of liquidation, they might have to pay even from their personal assets to cover the liabilities of the company. This type of company is quite uncommon today due to obvious reasons.

10. Holding company and Subsidiary Company

When one company controls the management of another company, the former is called holding company and the later over which the control is exercised is termed as subsidiary company.

11. Domestic Company

A company which is based in india registered under the companies act 2013. The head office and its business operations are conducted within the country. It can either be a private or public.

12. Foreign company

A foreign company is a company incorporated outside india which establishes its business operations within india under the companies act 2013.

13. Companies not for profit

These companies obtain a license from the central government before they are registered. They are limited liability but are not required to use a word limited or private with their names.

Books of Accounts maintained by Companies

- Cash Book, Journal , Cash flow statement and Ledgers
- Copies of bills or receipts, Records of sales and purchases and Records of assets and liabilities
- Financial Statements Such as Profit and Loss account, Balance sheet and trading Account.
- Deeds, voucher and Other Documents in Physical or electronic format

Statutory books

According to the Companies Act, a company has to maintain several types of Books and Registers. Books are often classified as Statutory Books and Statistical Books. Statistical Books refer to Books of Account and such other Record Books like an Inventory. Statutory Books are those which are necessary to observe legal formalities of a company including Registers.

It is the duty of the Company Secretary to prepare and maintain the Statutory Books.

Generally the Statutory Books (including Registers) are:

(1) Register of Members.
(2) Index of Members.
(3) Register of Directors.
(4) Register of Debenture-holders.
(5) Register of Mortgages and Charges.
(6) Register of Directors' Shareholdings.
(7) Register of Contracts in which Directors is interested.
(8) Minute Books:
(a) Of Directors' Meetings;
(b) Of Members' Meetings;
(c) Of Different Committees' Meetings, etc.,

1.3 Share Capital of a Company

A company, being an artificial person, cannot generate its own capital which has necessarily to be collected from several persons. These persons are known as shareholders and the amount contributed by them is called share capital. Since the number of shareholders is very very large, a separate capital account cannot be opened for each one of them. Hence, innumerable streams of capital contribution merge their identities in a common capital account called as 'Share Capital Account'.

Categories of Share Capital

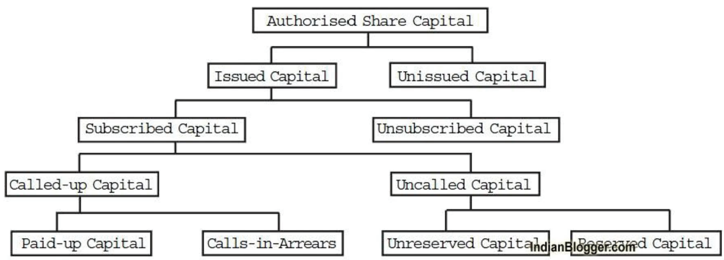
From accounting point of view the share capital of the company can be classified as follows:

1. Authorised Capital: Authorised capital is the amount of share capital which a company is authorised to issue by its Memorandum of Association. The company cannot raise more than the amount of capital as specified in the Memorandum of Association. It is also called Nominal or Registered capital. The authorised capital can be increased or decreased as per the procedure laid down in the Companies Act. It should be noted that the company need not issue the entire authorised capital for public subscription at a time. Depending upon its requirement, it may issue share capital but in any case, it should not be more than the amount of authorised capital

2. Issued Capital: It is that part of the authorised capital which is actually issued to the public for subscription including the shares allotted to vendors and the signatories to the company's memorandum. The authorised capital which is not offered for public subscription is known as 'unissued capital'. Unissued capital may be offered for public subscription at a later date
3. Subscribed Capital: It is that part of the issued capital which has been actually subscribed by the public. When the shares offered for public subscription are subscribed fully by the public the issued capital and subscribed capital would be the same. It may be noted that ultimately, the subscribed capital and issued capital are the same because if the number of share, subscribed is less than what is offered, the company allot only the number of shares for which subscription has been received. In case it is higher than what is offered, the allotment will be equal to the offer. In other words, the fact of over subscription is not reflected in the books.
4. Called up Capital: It is that part of the subscribed capital which has been called up on the shares. The company may decide to call the entire amount or part of the face value of the shares. For example, if the face value (also called nominal value) of a share allotted is Rs. 10 and the company has called up only Rs. 7 per share, in that scenario, the called up capital is Rs. 7 per share. The remaining Rs. 3 may be collected from its shareholders as and when needed.
5. Paid up Capital: It is that portion of the called up capital which has been actually received from the shareholders. When the shareholders have paid all the call amount, the called up capital is the same to the paid up capital. If any of the shareholders has not paid amount on calls, such an amount may be called as 'calls in arrears'. Therefore, paid up capital is equal to the called-up capital minus call in arrears.
6. Uncalled Capital: That portion of the subscribed capital

which has not yet been called up. As stated earlier, the company may collect this amount any time when it needs further funds.

7. Reserve Capital: A company may reserve a portion of its uncalled capital to be called only in the event of winding up of the company. Such uncalled amount is called 'Reserve Capital' of the company. It is available only for the creditors on winding up of the company.



Categories of Share Capital

Difference between Capital Reserve and Reserve Capital

The following are the major differences between capital reserve and reserve capital:

1. A portion of profit set aside that can be used for specific purposes only is known as Capital Reserve. Reserve Capital is that form of uncalled share capital that can be called up by the company only in the event of the liquidation of the company.
2. Capital Reserve the result of accumulating capital profit, whereas Reserve Capital is created out of authorized capital.
3. On the equity & liabilities side of the Balance Sheet, Capital Reserve appears under the head Reserves & Surplus. Unlike Reserve Capital, which is not disclosed at all.
4. There is a compulsion in the creation of capital reserve by every company which is not in the case of reserve capital.
5. For the creation of reserve capital, the special resolution should be passed by the company at Annual General Meeting (AGM).

6. Capital Reserve has various uses like writing off fictitious assets, or capital losses, etc. but Reserve Capital is used only when the company goes into liquidation.

Nature and Classes of Shares

Shares, refer to the units into which the total share capital of a company is divided. Thus, a share is a fractional part of the share capital and forms the basis of ownership interest in a company. The persons who contribute money through shares are called shareholders.

The amount of authorised capital, together with the number of shares in which it is divided, is stated in the Memorandum of Association but the classes of shares in which the company's capital is to be divided, along with their respective rights and obligations, are prescribed by the Articles of Association of the company. As per Section 86 of The Companies Act, a company can issue two types of shares (1) preference shares, and (2) equity shares (also called ordinary shares).

Preference Shares

According to Section 85 of The Companies Act, 1956, a preference share is one, which fulfils the following conditions :

(a) That it carries a preferential right to dividend to be paid either as a fixed amount payable to preference shareholders or an amount calculated by a fixed rate of the nominal value of each share before any dividend is paid to the equity shareholders.

(b) That with respect to capital it carries or will carry, on the winding up of the company, the preferential right to the repayment of capital before anything is paid to equity shareholders.

However, notwithstanding the above two conditions, a holder of the preference share may have a right to participate fully or to a limited extent in the surpluses of the company as specified in the Memorandum or Articles of the company. Thus, the preference shares can be participating and non-participating. Similarly, these shares can be cumulative or non-cumulative, and redeemable or irredeemable.

Types of Preference Shares

Some of the most important types of preference shares of a company are as follows:

(i) Cumulative preference shares:

Example

A preference share is said to be cumulative when the arrears of dividend are cumulative and such arrears are paid before paying any dividend to equity shareholders. Suppose a company has 10,000 8% preference shares of Rs. 100 each. The dividends for 1987 and 1988 have not been paid so far.

The directors before they can pay the dividend to equity shareholders for the year 1989, must pay the pref. dividends of Rs. 2, 40,000 i.e. for the year 1987, 1988 and 1989 before making any payment of dividend to equity shareholders for the year 1989.

(ii) Non-cumulative preference shares:

In the case of non-cumulative preference shares, the dividend is only payable out of the net profits of each year. If there are no profits in any year, the arrears of dividend cannot be claimed in the subsequent years. If the dividend on the preference shares is not paid by the company during a particular year, it lapses. Preference shares are presumed to be cumulative unless expressly described as non-cumulative.

For Example,

A company Y normally issues a ?70 quarterly dividend to its preferred shareholders. But the directors feel that there is not sufficient cash flow in the third quarter to pay a dividend.

As this is a non-cumulative stock, the company has no obligation to pay the missing dividend, and the holders of these shares have no claim against the company Y.

(iii) Participating preference shares:

Participating preference shares are those shares which are entitled in addition to preference dividend at a fixed rate, to participate in the balance of profits with equity shareholders after they get a fixed rate of dividend on their shares. The participating preference shares may also have the right to share in the surplus assets of the company on its winding up. Such a right may be expressly provided in the memorandum or articles of association of the company.

(iv) Non-participating preference shares:

Non- participating preference shares are entitled only to a fixed rate of dividend and do not share in the surplus profits. The preference shares are presumed to be non-participating, unless expressly provided in the memorandum or the articles or the terms of issue.

(v) Convertible preference shares:

Convertible preference shares are those shares which can be converted into equity shares within a certain period.

(vi) Non-Convertible preference shares:

These are those shares which do not carry the right of conversion into equity shares.

(vii) Redeemable preference shares:

A company limited by shares, may if so authorized by its articles issue preference shares which are redeemable as per the provisions laid down in Section 80. Shares may be redeemed either after a fixed period or earlier at the option of the company.

(viii) Guaranteed preference shares:

These shares carry the right of a fixed dividend even if the company makes no or insufficient profits.

Equity Shares

According to Section 85 of The Companies Act, 1956, an equity share is a share which is not a preference share. In other words, shares which do not enjoy any preferential right in the payment of dividend or repayment of capital, are termed as equity/ordinary shares. The equity shareholders are entitled to share the distributable profits of the company after satisfying the dividend rights of the preference share holders. The dividend on equity shares is not fixed and it may vary from year to year depending upon the amount of profits available for distribution. The equity share capital may be (i) with voting rights; or (ii) with differential rights as to voting, dividend or otherwise in accordance with such rules and subject to such conditions as may be prescribed.

Difference between equity shares and preference shares

1. Equity shares cannot be converted into preference shares. However, Preference shares could be converted into equity shares.
2. Equity shares are irredeemable, but preference shares are redeemable.
3. The next major difference is the 'right to vote'. In general, equity shares carry the right to vote, although preference shares do not carry voting rights.
4. If in a financial year, dividend on equity shares is not declared and paid, then the dividend for that year lapses. On the other hand, in the same situation, the preference shares dividend gets accumulated which is paid in the next financial year except in the case of non-cumulative preference shares.
5. The rate of dividend is consistent for preference shares, while the rate of equity dividend depends on the amount of profit earned by the company in the financial year. Thus it goes on changing

Sweat equity shares

'Sweat equity shares' are such equity shares, which are issued by a Company to its directors or employees at a discount or for consideration, other than cash, for providing their know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called. Sweat equity shares is one of the modes of making share based payments to employees of the company. The issue of sweat equity shares allows the company to retain the employees by rewarding them for their services. Sweat equity shares development of the company.

Employees Stock Option Scheme

Under ESOS, companies offer their equity shares to their employees. It is a scheme under which the company gives options to the wholetime directors, officers or employees to purchase, or subscribe at a future date, the equity shares at a predetermined price. This right may be exercised by the employees during the specified period. There is no obligation on the part of employees to exercise this option.

Objectives of ESOP

1. To develop the feeling of participation among employees.
2. To attract and motivate the efficient and skilled employees of the company.
3. To encourage to serve the company
4. To provide long term resources to the employees
5. To provide economic benefits by allotment of shares less than the market price etc.

Stock

Stock represents a portion of the capital of a company just like shares. It is a consolidation of fully paid shares. In the words of lord Hatherly, "stock is a set of shares put together in a bundle". Stock has no definite value. It can be of any value.

Difference between Shares and stock

The principal points of difference between share and stock are as follows:

1. A share is that smallest part of the share capital of the company which highlights the ownership of the shareholder. On the other hand, the bundle of shares of a member in a company, are collectively known as stock.
2. The share is always originally issued while the original issue of Stock is not possible.
3. A share has a definite number known as a distinctive number which distinguishes it from other shares, but a stock does not have such number.
4. Shares can be partly paid or fully paid. Conversely, Stock is always fully paid.

5. Shares can never be transferred in the fraction. As opposed to stock, can be transferred in the fraction.
6. Shares have nominal value, but the stock does not have any nominal value

Issue of Shares

A salient characteristic of the capital of a company is that the amount on its shares can be gradually collected in easy instalments spread over a period of time depending upon its growing financial requirement. The first instalment is collected along with application and is thus, known as application money, the second on allotment (termed as allotment money), and the remaining instalment are termed as first call, second call and so on. The word final is suffixed to the last instalment. However, this in no way prevents a company from calling the full amount on shares right at the time of application.

The important steps in the procedure of share issue are :

- o Issue of Prospectus: The company first issues the prospectus to the public. Prospectus is an invitation to the public that a new company has come into existence and it needs funds for doing business. It contains complete information about the company and the manner in which the money is to be collected from the prospective investors.
- o Receipt of Applications: When prospectus is issued to the public, prospective investors intending to subscribe the share capital of the company would make an application along with the application money and deposit the same with a scheduled bank as specified in the prospectus. The company has to get minimum subscription within 120 days from the date of the issue of the prospectus. If the company fails to receive the same within the said period, the company cannot proceed for the allotment of shares and application money should be returned within 130 days of the date of issue of prospectus.
- o Allotment of Shares: If minimum subscription has been received, the company may proceed for the allotment of

shares after fulfilling certain other legal formalities. Letters of allotment are sent to those whom the shares have been alloted, and letters of regret to those to whom no allotment has been made. When allotment is made, it results in a valid contract between the company and the applicants who now became the shareholders of the company.

Minimum Subscription

The minimum amount that, in the opinion of directors, must be raised to meet the needs of business operations of the company relating to:

- the price of any property purchased, or to be purchased, which has to be met wholly or partly out of the proceeds of issue;
- preliminary expenses payable by the company and any commission payable in connection with the issue of shares;
- the repayment of any money borrowed by the company for the above two matters;
- working capital; and
- any other expenditure required for the usual conduct of business operations.

It is to be noted that 'minimum subscription' of capital cannot be less than 90% of the issued amount according to SEBI (Disclosure and Investor Protection) Guidelines, 2000 [6.3.8.1 and 6.3.8.2]. If this condition is not satisfied, the company shall forthwith refund the entire subscription amount received. If a delay occurs beyond 8 days from the date of closure of subscription list, the company shall be liable to pay the amount with interest at the rate of 15% [Section 73(2)].

Shares of a company are issued either at par, at a premium or at a discount. Shares are to be issued at par when their issue price is exactly equal to their nominal value according to the terms and conditions of issue. When the shares of a company are issued more than its nominal value (face value), the excess amount is called premium . When the shares are issued at a price less than the face value of the share, it is known as shares issued at a discount. Irrespective of the fact that shares are issued at par, premium or discount, the share capital of a company as stated earlier, may be collected in instalments payable at different stages.

Accounting Treatment

On application : The amount of money paid with various instalment represents the contribution to share capital and should ultimately be credited to share capital. However, for the sake of convenience, initially individual accounts are opened for each instalment. All money received along with application is deposited with a scheduled bank in a separate account opened for the purpose. The journal entry is as follows:

Bank a/c

To share application

(Amount received on application for - shares @ Rs. ______ per share)

On allotment : When minimum subscription has been received and certain legal formalities on the allotment of shares have been duly compiled with, the directors of the company proceed to make the allotment of shares.

The allotment of shares implies a contract between the company and the applicants who now become the allottees and assume the status of shareholders or member.

The journal entries with regard to allotment of shares are as follows:

1. For Transfer of Application Money

Share Application A/c Dr.

To Share Capital A/c

(Application money on _____ Shares allotted/transferred to Share Capital)

2. For Money Refunded on Rejected Application

Share Application A/c dr

To Bank A/c

(Application money returned on rejected application for ___shares)

3. For Amount Due on Allotment

Share Allotment A/c Dr.

To Share Capital A/c

4. For Adjustment of Excess Application Money

Share Application A/c dr

To Share Allotment A/c

(Application Money on __Shares @ Rs__per shares adjusted to the amount due on allotment

For Receipt of Allotment Money

Bank A/c Dr.

To Share Allotment A/c

(Allotment money received on ___Shares @

Rs. - per share Combined Account)

Note:- The journal entries (2) and (4) can also be combined as follows:

Share Application A/c

To Share Allotment A/c

To Bank A/c

(Excess application money adjusted to share

allotment and balance refunded)

Sometimes a combined account for share application and share allotment called 'Share Application and Allotment Account' is opened in the books of a company. The combined account is based on the reasoning that allotment without application is impossible while application without allotment is meaningless. These two stages of share capital are closely inter-related. When a combined account is maintained, journal entries are recorded in the following manner:

1. For Receipt of Application and Allotment

Bank A/c Dr.

To Share Application and Allotment A/c

(Money received on applications for shares @ Rs. _____ per share).

2. For Transfer of Application Money and Allotment Amount Due

Share Application and Allotment A/c Dr.

To Share Capital A/c

(Transfer of application money to Share Capital Account for amount due or allotment of - Share @ Rs. per share)

3. For Money Refunded on Rejected Applications

Share Application and Allotment A/c Dr.

To Bank A/c

(Application money returned on rejected application for ___ shares)

4. On Receipt of Allotment Amount

Bank A/c Dr.

To Share Application and Allotment A/c

(Balance of Allotment Money Received)

On Calls : Calls play a vital role in making shares fully paid-up and for realising the full amount of shares from the shareholders. In the event of shares not being fully called up till the completion of allotment, the directors have the authority to ask for the remaining amount on shares as and when they decide about the same. It is also possible that the timing of the payment of calls by the shareholders is determined at the time of share issue itself and given in the prospectus.

Two points are important regarding the calls on shares. First, the amount on any call should not exceed 25% of the face value of shares. Second, there must be an interval of at least one month between the making of two calls unless otherwise provided by the articles of association of the company. When a call is made and the amount of the same is received, the journal entries are as given below:

1. For Call Amount Due

Share Call A/c Dr.

To Share Capital A/c

(Call money due on ___Shares @ Rs. ____ per share)

2. For Receipt of Call Amount

Bank A/c dr

To Share Call A/c

(Call money received)

The word/words First, Second, or Third must be added between the words "Share" and 'Call' in the Share Call account depending upon the identity of the call made. For example, in case of first call it will be termed as 'Share First Call Account', in case of second call it will be 'Share Second Call Account' and so on.

Another point to be noted is that the words 'and Final' will also be added to the last call, say, if second call is the last call it will be termed as 'Second and Final Call' and if it is the third call which is the last call, it will be termed as 'Third and Final Call'. It is also possible that the whole balance after allotment may be collected in one call only. In that case the first call itself, shall be termed as the 'First and Final Call'.

The following points should be kept in mind while issuing the share capital for public subscription :

1. The application money should be at least 5% of the face value of the share.
2. Calls are to be made as per the provisions of the articles of association.
3. Where there is no articles of association of its own, the following provisions of Table A will apply:

(a) A period of one month must elapse between two calls;

(b) The amount of call should not exceed 25% of the face value of the share;

(c) A minimum of 14 days' notice is given to the shareholders to pay the amount; and

(d) Calls must be made on a uniform basis on all shares within the same class.

4. The procedure for accounting for the issue of both equity and preference shares is the same. To differentiate between

the two the words 'Equity' and 'Preference' is prefixed to each and every instalment.

Illustration 1

Mona Earth Mover Limited decided to issue 12,000 shares of Rs.100 each payable at Rs.30 on application, Rs.40 on allotment, Rs.20 on first call and balance on second and final call. Applications were received for 13,000 shares. The directors decided to reject application of 1,000 shares and their application money being refunded in full. The allotment money was duly received on all the shares, and all sums due on calls are received except on 100 shares.

Record the transactions in the books of Mona Earth Movers Limited

Solution

Books of Mona Earth Mover Limited

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c Dr. To Share Application A/c (Application money on 13,000 shares @ Rs.30 per share received)		3,90,000	3,90,000
	Share Application A/c Dr. To Share Capital A/c (Application money transferred to share capital)		3,60,000	3,60,000
	Share Application A/c Dr. To Bank A/c (Application money on 1,000 shares returned]		30,000	30,000
	Share Allotment A/c Dr. To Share Capital A/c (Money due on allotment of 12,000 shares @ Rs. 40 per share)		4,80,000	4,80,000

	Bank A/c Dr. To Share Allotment A/c (Money received on 12,000 shares @ Rs. 40 per share on allotment)		4,80,000	4,80,000
	Share First Call A/c Dr. To Share Capital A/c (Money due on 12,000 shares @ Rs. 20 per share on first Call)		2,40,000	2,40,000
	Bank A/c Dr. To Share First Call A/c (First Call money received except for 100 shares)		2,38,000	2,38,000
	Share Second and Final Call A/c Dr. To Share Capital A/c (Money due on 12,000 shares @ Rs. 10 per share on Second and final Call)		1,20,000	1,20,000
	Bank A/c Dr. To Share Second and Final Call A/c (Second and final call money received except for 100 shares)		1,19,000	1,19,000

Illustration 2

Eastern Company Limited issued 40,000 shares of Rs. 10 each to the public for the subscription out of its share capital, payable as Rs. 4 on application, Rs. 3 on allotment and the balance on Ist and final call. Applications were received for 40,000 shares. The company made the allotment to the applicants in full. All the amounts due on allotment and first and final call were duly received. Give the journal entries.

Solution

Books of Eastern Company Limited

Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c	Dr.		1,60,000	
	To Share Application A/c				1,60,000
	(Application money on 40,000 shares @ Rs.4 per share received)				
	Share Application A/c	Dr.		1,60,000	
	To Share Capital A/c				1,60,000
	(Application money transferred to share capital)				
	Share Allotment A/c	Dr.		1,20,000	
	To Share Capital A/c				1,20,000
	(Money due on allotment of 40,000 shares @ Rs. 3 per share)				
	Bank A/c	Dr.		1,20,000	
	To Share allotment A/c				1,20,000
	(Money received on 40,000 shares @ Rs. 3 per share on allotment)				
	Share First and Final Call A/c	Dr.		1,20,000	
	To Share Capital A/c				1,20,000
	(Money due on 40,000 shares @ Rs. 3 per share on First and final call)				
	Bank A/c	Dr.		1,20,000	
	To Share First and Final Call A/c				1,20,000
	(First and final call money received)				

Do it Yourself

On April 01, 2015, a limited company was incorporated with an authorised capital of Rs. 40,000 divided into shares of Rs. 10 each. It offered to the public for subscription of 3,000 shares payable as follows:

On Application	Rs. 3 per share
On Allotment	Rs. 2 per share
On First Call	
(One month after allotment)	Rs.2.50 per share
On Second and Final Call	Rs. 2.50 per share

The shares were fully subscribed for by the public and application money duly received on April 15, 2015. The directors made the allotment on May 1, 2015.

How will you record the share capital transactions in the books of a company if the amounts due has been duly received, and the company maintains the combined account for application and allotment.

Fraction shares

Less than one full share of equity is called a fractional share. Such shares may be the result of stock splits, dividend reinvestment plans (DRIPs), or similar corporate actions. Typically, fractional shares aren't available from the market, and while they have value to investors.

Circumstances in which fraction shares arise

1. Stock splits don't always result in an even number of shares. A 3-for-2 stock split would create three shares for every two shares an investor owns, so an investor with an odd number of shares would end up with a fractional share after the split. Three shares would become 4½, five would become 7½, and so on.
2. Mergers and acquisitions (M&As) may also create fractional shares since companies combine new common stock using a predetermined ratio. The ratio often results in fractional shares for shareholders.
3. Mutual funds and dividend stock investors
4. Reduction and consolidation of shares
5. Reverse stock split

Calls in Arrears

It may happen that shareholders do not pay the call amount on due date. When any shareholder fails to pay the amount due on allotment or on any of the calls, such amount is known as 'Calls in Arrears'/'Unpaid Calls'. Calls in Arrears represent the debit balance of all the calls account. Such amount shall appear as 'Note to Accounts (Refer Chapter 3). However, where a company maintains 'Calls in Arrears' Account, it needs to pass the following additional journal entry:

Calls in Arrears A/c dr

To Share First Call Account A/c

To Share Second and Final Call A/c

(Calls in arrears brought into account)

The Articles of Association of a company may empower the directors to charge interest at a stipulated rate on calls in arrears. If the articles are silent in this regard, the rule contained in Table A shall be applicable which states that the interest at a rate not exceeding 5% p.a. shall have to be paid on all unpaid amounts on shares for the period intervening between the day fixed for payment and the time of actual payment thereof

On receipt of the call amount together with interest, the amount of interest shall be credited to interest account while call money shall be credited to the respective call account or to calls in arrears account. When the shareholder makes the payment of calls in arrears together with interest, the entry will be as follows:\

Bank A/c Dr.

To Calls in Arrears A/c

To Interest A/c(Calls in arrears received with interest)

Note: If nothing is specified, there is no need to take the interest on calls in arrears account and record the above entry

Illustration 3

Cronic Limited issued 10,000 equity shares of Rs. 10 each payable at Rs. 2.50 on application, Rs. 3 on allotment, Rs. 2 on first call, and the balance of Rs. 2.50 on second and final call. All the shares were fully subscribed and paid except of a shareholder having 100 shares who could not pay for second and final call. Give journal entries to record these transactions.

Solution:

Books of Cronic Limited
Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c To Share Application A/c (Money received on applications for 10,000 shares @ Rs. 2.50 per share)	Dr.		25,000	25,000
	Equity Share Application A/c To Share Capital A/c (Transfer of application money on 10,000 shares to share capital)	Dr.		25,000	25,000
	Equity Share Allotment A/c To Share Capital A/c (Amount due on the allotment of 10,000 shares @ Rs. 3 per share)	Dr.		30,000	30,000
	Bank A/c To Share Allotment A/c (Allotment money received)	Dr.		30,000	30,000
	Share First Call A/c To Share Capital A/c (First call money due on 10,000 shares @ Rs. 2 per share)	Dr.		20,000	20,000
	Bank A/c To Share First Call A/c (First call money received)	Dr.		20,000	20,000
	Share Second and Final Call A/c To Share Capital A/c (Final call money due)	Dr.		25,000	25,000
	Bank A/c Call in Arrears A/c To Share Second and Final Call A/c (Final call money received except that of 100 shares)	Dr. Dr.		24,750 250	25,000

Calls in Advance

Sometimes shareholders pay a part or the whole of the amount of the calls not yet made. The amount so received from the shareholders is known as "Calls in Advance". The amount received in advance is a liability of the company and should be credited to 'Call in Advance Account." The amount received will be adjusted towards the payment of calls as and when they becomes due. Table A of the Companies Act provides for the payment of interest on calls in advance at a rate not exceeding

6% per annum. The following journal entry is recorded for the amount of calls received in advance.

Bank A/c Dr.

To Calls in Advance A/c

(Amount received on call in advance)

On the due date of the calls, the amount of 'Calls in Advance' is adjusted by the following entry :

Calls in Advance A/c Dr.

To Particular Call A/c

(Calls in advance adjusted with the call money due)

The balance in 'Calls in Advance' account is shown as a separate item under the title Equity and Liabilities in the company's balance sheet under the head 'current liabilities', as sub-head 'others current liabilities'. It is not added to the amount of paid-up capital.As 'Calls in Advance' is a liability of the company, it is under obligation, if provided by the Articles, to pay interest on such amount from the date of its receipt up to the date when appropriate call is due for payme

The accounting treatment of interest on Calls in Advance is as follows:

1. For Payment of Interest

Interest on Calls in Advance A/c dr

To Bank A/c

(Interest paid on Calls in Advance)

Or

For Interest due

Interest on Calls in Advance A/c

To Sundry Shareholder's A/c

(Interest paid on Calls in Advance)

For Interest Paid

Sundry Shareholder's A/c

To Bank A/c

Illustration 4

Konica Limited registered with an authorised equity capital of Rs. 2,00,000 divided into 2,000 shares of Rs. 100 each, issued for subscription of 1,000 shares payable at Rs. 25 per share on application, Rs. 30 per share on allotment, Rs. 20 per share on first call and the balance as and when required.

Application money on 1,000 shares was duly received and allotment was made to them. The allotment amount was received in full, but when the first call was made, one shareholder failed to pay the amount on 100 shares held by him and another shareholder with 50 shares, paid the entire amount on his shares. The company did not make any other call.

Give the necessary journal entries in the books of the company to record these share capital transactions.

Solution

Books of Konica Limited

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c Dr.		25,000	
	To Equity Share Application A/c			25,000
	(Money received on application for 1,000 shares @ Rs. 25 per share)			
	Equity Share Application A/c Dr.		25,000	
	To Equity Share Capital A/c			25,000
	(Transfer of application money on 1,000 shares to share capital)			
	Equity Share Allotment A/c Dr.		30,000	
	To Equity Share Capital A/c			30,000
	(Amount due on the allotment of 1,000 shares @ Rs. 30 per share)			
	Bank A/c Dr.		30,000	
	To Equity Share Allotment A/c			30,000
	(Allotment money received)			
	Equity Share First Call A/c Dr.		20,000	
	To Equity Share Capital A/c			20,000
	(First call money due on 1,000 shares @ Rs. 20 per share)			
	Bank A/c Dr.		19,250	
	Calls in Arrears A/c Dr.		2,000	
	To Equity Share First Call A/c			20,000
	To Calls in Advance A/c			1,250
	(First call money received on 900 shares, calls in arrears for 100 shares @ Rs.20 per share and calls in advance for 50 shares @ Rs.25 per share.)			

Illustration5

Unique Pictures Limited was registered with an authorised capital of Rs. 5,00,000 divided into 20,000, 5% preference shares of Rs. 10 each and 30,000 equity shares of Rs. 10 each. The company issued 10,000 preference and 15,000 equity shares for public subscription. Calls on shares were made as under

	Equity Shares (Rs.)	Preference Shares (Rs.)
Application	2	2
Allotment	3	3
First Call	2.50	2.50
Second and Final Call	2.50	2.50

All these shares were fully subscribed. All the dues were received except the second and final call on 100 equity shares and on 200 preference shares. Record these transactions in the journal. You are also required to prepare the cash book and balance sheet.

Solution

Books of Unique Pictures Limited

Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Equity Share Application A/c	Dr.		30,000	
	5% Preference Share Application A/c	Dr.		20,000	
	To Equity Share Capital A/c				30,000
	To 5% Preference Share Capital A/c				20,000
	(Transfer of application money)				
	Equity Share Allotment A/c	Dr.		45,000	
	5% Preference Share Allotment A/c	Dr.		30,000	
	To Equity Share Capital A/c				45,000
	To 5% Preference Share Capital A/c				30,000
	(Amount due on allotment)				
	Equity Share First Call A/c	Dr.		37,500	
	5% Preference Share First Call A/c	Dr.		25,000	
	To Equity Share Capital A/c				37,500

	To 5% Preference Share Capital A/c (First call money due)			25,000
	Equity Share Second and Final Call A/c Dr. 5% Preference Share Second and final Call A/cDr. To Equity Share Capital A/c To 5% Preference Share Capital A/c (First call money due)		37,500 25,000	 37,500 25,000
	Call in Arrears A/c Dr. To Equity Share Second and Final Call A/c To 5% Preference Share Final Call A/c (For Calls in Arrears)		750	 250 500

Cash Book (Bank Column)

Dr. *Cr.*

Date	*Receipts*	*L.F.*	*Amount (Rs.)*	*Date*	*Payments*	*L.F.*	*Amount (Rs.)*
	Equity Share Application		30,000		Balance c/d		2,49,250
	5% Preference Share Application		20,000				
	Equity Share Allotment		45,000				
	5% Preference Share Allotment		30,000				
	Equity Share First Call		37,500				
	5% Preference Share First Call		25,000				
	Equity Share Second and Final Call		37,250				
	5% Preference Share Second and Final Call		24,500				
			2,49,250				**2,49,250**

Balance Sheet of unique pictures as at . . . . .

Particulars	Note No.	Amount (Rs.)
I. Equity and Liabilities		
1. Shareholders' Funds		
a) Share capital	1	2,49,250
		2,49,250
II. Assets		
1. Current assets		
a) Cash and Cash Equivalents	2	2,49,250
		2,49,250

Notes to Accounts

1.Share Capital		
Authorised Capital		
30,000 Equity Shares of Rs. 10 each		3,00,000
20,000 5% Preference Shares of Rs. 10 each		2,00,000
		5,00,000
Issued Capital		
15,000 Equity Shares of Rs. 10 each		1,50,000
10,000 5% Preference Shares of Rs. 10 each		1,00,000
		2,50,000

Subscribed Capital		
Subscribed and fully paid-up		
14,900 Equity Shares of Rs. 10 each	1,49,000	
9,800, 5% Preference Shares of Rs. 10 each	98,000	
		2,47,000
Subscribed but not fully paid-up		
[redacted]		
100 Equity Shares of Rs. 10 each	1,000	
Less: Calls in Arreras	-250	750
200, 5% Preference Shares of Rs. 10 each	2,000	
Less : Calls in Arrers	-500	1,500
		2,49,250

Illustration 6

Rohit & Company issued 30,000 shares of Rs.10 each payable Rs.3 on application, Rs.3 on allotment and Rs.2 on first call after two months. All money due on allotment was received, but when the first call was made a shareholder having 400 shares did not pay the first call and a shareholder of 300 shares paid the money for the second and final call of Rs.2 which had not been made as yet.Give the necessary journal entries in the books of the company.

Solution:

Books of Rohit & Company
Journal

Date	*Particulars*	*L.F.*	*Debit*	*Credit*
	Bank A/c To Share Application A/c (Application money received on 30,000 shares @ Rs.3 per share)		90,000	90,000
	Share Application A/c To Share Capital A/c (Application money transferred to share capital account)		90,000	90,000
	Share Allotment A/c To Share Capital A/c (Allotment money due on 30,000 shares @ Rs.3 per share)		90,000	90,000
	Bank A/c To Share Allotment A/c (Allotment money received)		90,000	90,000

		Share First Call A/c Dr. To Share Capital A/c (First call money due on 30,000 shares @ Rs.2 per share)	60,000	60,000
		Bank A/c Dr. Call in Arrears A/c Dr. To Share First Call A/c To Calls in Advance A/c (Calls in arrears for 400 shares @Rs.2 per share and calls in advance on 300 shares @Rs.2 per share)	59,800 800	60,000 600

Exercises

A company issued 20,000 equity shares of Rs.10 each payable Rs.3 on application, Rs.3 on allotment, Rs.2 on first call and Rs.2 on second and the final call. The allotment money was payable on or before May 01, 2015; first call money on or before August Ist, 2015; and the second and final call on or before October Ist, 2015; 'X', whom 1,000 shares were allotted, did not pay the allotment and call money; 'Y', an allottee of 600 shares, did not pay the two calls; and 'Z', whom 400 shares were allotted, did not pay the final call. Pass journal entries and prepare the balance sheet of the company.

Alfa Company Ltd. issued 10,000 shares of Rs.10 each for cash payable Rs.3 on application, Rs.2 on allotment and the balance in two equal instalments. The allotment money was payable on or before March 31, 2015; the first call money on or before 30 June, 2015; and the final call money on or before August, 31. 2015. Mr. 'A', to whom 600 shares were allotted, paid the entire remaining face value of shares allotted to him on allotment. Record journal entries in company's books and also exhibit the share capital in the balance sheet on the date.

Over Subscription

There are instances when applications for more shares of a company are received than the number offered to the public for subscription. This usually happens in respect of shares issue of well-managed and financially strong companies and is said to be a case of 'Over Subscription'

In such a condition, three alternatives are available to the directors to deal with the situation: (1) they can accept some applications in full and totally reject the others; (2) they can make a pro-rata allotment to all; and (3) they can adopt a combination of the above two alternatives which happens to be the most common course adopted in practice.

The problem of over subscription is resolved with the allotment of shares. Therefore, from the accounting point of view, it is better to place the situation of over subscription within the total frame of application and allotment, i.e. receipt of application amount, amount due on allotment and its receipt from the shareholders, and the same has been observed in the pattern of entries.

First Alternative : When the directors decide to fully accept some applications and totally reject the others, the application money received on rejected applications is fully refunded. For example, a company invited applications for 20,000 shares and received the applications for 25,000 shares. The directors rejected the applications for 5,000 shares which are in excess of the required number and refunded their application money in full. In this case, the journal entries on application and allotment will be as follows : The journal entries on application and allotment according to this alternative are as follows:

1. Bank a/c Dr
   Share application
   (money received on application of 25000 shares of Rs. …per share)
2. Share application a/c Dr
   Share capital
   Bank

(transfer of application for money 20000 for shares allotted and money refunded on applications for 5000 shares rejected)

3. Shares allotment a/c Dr

Share capital

(Amount due on the allotment 20000 shares of Rs. …… per share)

4. Bank a/c dr

Share allotment a/c

(allotment money recieved)

Second Alternative : When the directors opt to make a proportionate allotment to all applicants (called 'pro-rata' allotment), the excess application money received is normally adjusted towards the amount due on allotment. In case, the excess application money received is more than the amount due on allotment of shares, such excess amount may either be refunded or credited to calls in advance.

For example, a company invited applications for 10,000 shares and received applications for 15,000 shares. The directors decided to reject the applications for 2,500 shares outright and to make a pro-rata allotment of 10,000 shares to the applicants for the remaining 12,500 shares so that four shares are allotted for every five shares applied. In this case, the money on applications for 2,500 shares rejected would be refunded fully and that on the remaining 2,500 shares (12,500 shares - 10,000 shares) would be adjusted against the allotment amount due on 10,000 shares allotted and credited to share allotment account, the journal entries on application and allotment recorded as follows:

1. Bank A/c Dr.

To Share Application A/c

(Money received on application for 15,000 shares @ Rs. _ per share)

2 Share Application A/c Dr.

To Share Capital A/c

To Share Allotment A/c

To Bank A/c

(Transfer of application money to share capital, and the excess application amount of pro-rata allottees credited to share allotment and the amount on rejected applications refunded)

3 Share Allotment A/c Dr.

To Share Capital A/c

(Amount due on the Allotment of 10,000 shares @ Rs. _ per share)

4 Bank A/c Dr.

To Share Allotment A/c

(Allotment money received after adjusting the amount already received as excess application money)

Illustration 7

Janta Papers Limited invited applications for 1,00,000 equity shares of Rs. 25 each payable as under:

On Application Rs. 5.00 per share

On Allotment Rs. 7.50 per share

On First Call

(due two months after allotment) Rs. 7.50 per share

On Second and Final Call (due two months after First Call) Rs. 5.00 per share

Applications were received for 4,00,000 shares on January 01, 2014 and allotment was made on February 01, 2014. Record journal entries in the books of the company to record these share capital transactions under each of the following circumstances:

1. The directors decide to allot 1,00,000 shares in full to selected applicants and the applications for the remaining 3,00,000 shares were rejected outright.
2. The directors decide to make a pro-rata allotment of 25 per cent of the shares applied for to every applicant; to apply the balance of application money towards amount

due on allotment; and to refund the amount remaining thereafter.

3. The directors totally reject applications for 2,00,000 shares, accept full applications for 80,000 shares and make a pro-rata allotment of the 20,000 shares to remaining applicants and the excess application money is to be adjusted towards allotment and calls to be made.

Solution

Books of Janta Papers Limited (*First Alternative*)

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
2014 January 01	Bank A/c Dr. To Equity Share Application A/c (Money received on applications for 4,00,000 shares @ Rs. 5 per share)		20,00,000	20,00,000
February 01	Equity Share Application A/c Dr. To Equity Share Capital A/c To Bank A/c (Transfer of application money on 1,00,000 shares to share capital and money refunded on rejected applications)		20,00,000	5,00,000 15,00,000
February 01	Equity Share Allotment A/c Dr. To Equity Share Capital A/c (Amount due on the allotment of 1,00,000 shares @ Rs 7.50 per share)		7,50,000	7,50,000
	Bank A/c Dr. To Equity Share Allotment A/c (Allotment money received)		7,50,000	7,50,000
April 01	Equity Share First Call A/c Dr. To Equity Share Capital A/c (First call money due on 1,00,000 shares @ Rs. 7.50 per share)		7,50,000	7,50,000
April 01	Bank A/c Dr. To Equity Share First Call A/c (First call money received)		7,50,000	7,50,000
June 01	Equity Share Second and Final Call A/c Dr. To Equity Share Capital A/c (Final Call money due on 1,00,000 shares @ Rs. 5 per share)		5,00,000	5,00,000
June 01	Bank A/c Dr. To Equity Share Second and Final Call A/c (Final call money received)		5,00,000	5,00,000

Second Alternative

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
2014 January 01	Bank A/c Dr. To Equity Share Application A/c (Money received on applications for 4,00,000 shares @ Rs. 5 per share)		20,00,000	 20,00,000
February 01	Equity Share Application A/c Dr. To Equity Share Capital A/c To Equity Share Allotment A/c To Bank A/c (Transfer of application money on Shares allotted to share capital, excess application amount credited to allotment account and money refunded on rejected applications)		20,00,000	 5,00,000 7,50,000 7,50,000
February 01	Equity Share Allotment A/c Dr. To Equity Share Capital A/c (Amount due on the allotment of Rs. 1,00,000 shares @ Rs 7.50 per share)		7,50,000	 7,50,000

Note : The entries regarding the two calls would be the same as given in preceding method.

Third Alternative

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
2014				
January 01	Bank A/c Dr.		20,00,000	
	To Equity Share Application A/c			20,00,000
	(Money received on applications for 4,00,000 shares @ Rs. 5 per share)			
February 01	Equity Share Application A/c Dr.		20,00,000	
	To Equity Share Capital A/c			5,00,000
	To Equity Share Allotment A/c			1,50,000
	To Calls-in-Advance A/c			2,50,000
	To Bank A/c			11,00,000
	(Amount on share application adjusted to share capital, share allotment and calls in advance and the balance refunded including the money on rejected applications)			
February 01	Equity Share Allotment A/c Dr.		7,50,000	
	To Equity Share Capital A/c			7,50,000
	(Transfer of application money on shares allotted to share capital and amount due on the allotment of 1,00,000 shares @ Rs. 7.50 per share)			
	Bank A/c Dr.		6,00,000	
	To Equity Share Allotment A/c			6,00,000
	(Allotment money received)			
April 01	Equity Share First Call A/c Dr.		7,50,000	
	To Equity Share Capital A/c			7,50,000
	(First Call money due on 1,00,000 shares @ Rs. 7.50 per share)			
April 01	Bank A/c Dr.		6,00,000	
	Calls in Advance A/c Dr.		1,50,000	
	To Equity Share First Call A/c			7,50,000
	(Calls-in-advance adjusted against first call and the balance money on call received)			
June 01	Equity Share Second and Final Call A/c Dr.		5,00,000	
	To Equity Share Capital A/c			5,00,000
	(Final Call money due on 1,00,000 shares @ Rs. 5 per share)			
June 01	Bank A/c Dr.		4,00,000	
	Calls in Advance A/c Dr.		1,00,000	
	To Equity Share Second and Final Call A/c			5,00,000
	(Calls-in-advance adjusted against final call and the balance money on call received)			

Note:The balance of excess application money as a result of pro-rata distribution in journal entry 3 above is large enough to meet the demands on allotted shares in respect of the allotment and the two call money, as well as to leave an amount to be refunded along with that on the rejected applications.

Working Notes:

	(Rs.)	(Rs.)
Excess Application Money		15,00,000
Less Transfers :		
Share Allotment -		
20,000 shares @ Rs. 7.50	1,50,000	
Share Calls -		
20,000 shares @ Rs. 12.50	2,50,000	4,00,0001
Amount to be refunded (including that on the rejected applications)		11,00,000

Under Subscription

Under subscription is a situation where number of shares applied for is less than the number for which applications have been invited for subscription. For example, a comapny offered 2 lakh shares for subscription to the public but the applications were received for 1,90,000 shares, only. In such a situation, the allotment will be confirmed to 1,90,000 shares and entries shall be made accordingly. However, as stated earlier, it must be ensured that the company has received the minimum subscriptions (not less than 90% of the offer otherwise the procedure for issue of shares cannot proceed further and the company will have to refund the entire subscription amount received.

Issue of Shares at a Premium

It is quite common for the shares of financially strong and well-managed companies to be issued at a premium, i.e. at an amount more than the nominal or par value of shares. Thus, when a share of the nominal value of Rs. 100 is issued at Rs. 105, it is said to have been issued at a premium of 5 per cent.

When the issue of shares is at a premium, the amount of premium may technically be called at any stage of the issue of shares. However, premium is generally called with the amount due on allotment, sometimes with the application money and rarely with the call money. The premium amount is credited to a separate account called 'Securities Premium Account' and is shown under the title 'Equity and Liabilities' of the company's balance sheet under the head 'Reserves and Surpluses'. It can be used only for the following four purposes as laid down by Section 78 of The Companies Act 1956:

(a) to issue fully paid bonus shares to the extent not exceeding unissued share capital of the company;

(b) to write-off preliminary expenses of the company;

(c) to write-off the expenses of, or commission paid, or discount allowed on any of the shares or debentures of the company; and

(d) to pay premium on the redemption of preference shares or debentures of the company.

The journal entries for shares issued at a premium are as follows.

1. For Premium Amount called with Application money

(a) Bank A/c Dr.

To Share Application A/c

(Money received on application for - shares @ Rs. - per share including premium)

(b) Share Application A/c Dr.

To Share Capital A/c

To Securities Premium A/c

(Transfer of application money to share capital and securities premium account)

2. Premium Amount called with Allotment Money

(a) Share Allotment A/c dr

To Share Capital A/c

To Securities Premium A/c

(Amount due on allotment of shares @ Rs - per share including premium)

(b) Bank A/c Dr.

To Share Allotment A/c

(Allotment money received including premium)

3. Premium Amount called with Call Money

(a) Share Application A/c

To Share Capital A/c

To Securities Premium A/c

(Amount due on Ist/2nd call @Rs- per share including premium)

(b) Bank A/c Dr.

To Share Call A/c

(Call money received including premium)

Illustration 8

Jupiter Company Limited issued 35,000 equity shares of Rs. 10 each at a premium of Rs.2 payable as follows:

On Application Rs. 3

On Allotment Rs. 5 (including premium

Balance on First and Final Call

The issue was fully subscribed. All the money was duly received. ecord journal entries in the books of the Company.

Solution:

Books of Jupiter Company Limited

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c Dr. To Equity Share Application A/c (Money received on applications for 35,000 shares @ Rs. 3 per share)		1,05,000	 1,05,000
	Equity Share Application A/c Dr. To Equity Share Capital A/c (Transfer of application money on allotment to share capital)		1,05,000	 1,05,000
	Equity Share Allotment A/c Dr. To Equity Share Capital A/c To Securities Premium A/c (Amount due on allotment of 35,000 shares @ Rs. 5 per share including premium)		1,75,000	 1,05,000 70,000
	Bank A/c Dr. To Equity Share Allotment A/c (Money received including premium)		1,75,000	 1,75,000
	Equity Share First and Final Call A/c Dr. To Equity Share Capital A/c (Amount due on First and Final Call of Rs. 4 per share on 35,000 shares)		1,40,000	 1,40,000
	Bank A/c Dr. To Equity Share First and Final Call A/c (Money received on First and Final Call)		1,40,000	 1,40,000

Issue of Shares at a Discount

There are instances when the shares of a company are issued at a discount, i.e. at an amount less than the nominal or par value of shares, the difference between the nominal value and issue price representing discount on the issue of shares. For example, when a share of the nominal value of Rs. 100 is issued at Rs. 98, it is said to have been issued at a discount of two per cent.

As a general rule, a company cannot ordinarily issue shares at a discount. It can do so only in cases such as 'reissue of forfeited shares' (to be discussed later) and in accordance with the provisions of Section 79 of the Companies Act, 1956.

Section 79 of the Companies Act, 1956 states that a company is permitted to issue shares at a discount provided the following conditions are satisfied:

(a) The issue of shares at a discount is authorised by an ordinary resolution passed by the company at its general meeting and sanctioned by the Company Law Board now Central Government.

(b) The resolution must specify the maximum rate of discount at which the shares are to be issued but the rate of discount must not exceed 10 per cent of the nominal value of shares. The rate of discount can be more than 10 per cent if the Government is convinced that a higher rate is called for under special circumstances of a case.

(c) At least one year must have elapse since the date on which the company became entitled to commence the business.

(d) The shares are of a class which has already been issued.

(e) The shares issued within two months from the date of receiving sanction for the same from the Government or within such extended period as the Government may allow.

Whenever shares are issued at a discount, the amount of discount is brought into the books at the time of allotment by debiting an account called 'Discount on the Issue of Shares Account'. The journal entry to be passed for the purpose is as given below:

Share Allotment A/c Dr.

Discount on the Issue of Shares A/c Dr.

Share Capital A/

(Amount due on allotment of - shares Rs - per share and discount on issue brought into account

Discount on the Issue of Shares, being a loss of capital nature to the company, will be set off from 'Securities Premium' or written-off through 'Statement of Profit and Loss, over a period of 3 to 5 years as per the guidelines of ICAI.

Illustration 9

Fine Arts Limited issued to the public for subscription of 10,000 shares of Rs.10 each at a discount of 10% payable at Rs. 4 on application, Rs. 3 on allotment and Rs.2 on Ist and the final call. The issue was fully subscribed and all the money was duly received.

Record journal entries for the above in the books of the company.

Solution:

Books of Fine Arts Limited

Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c	Dr.		40,000	
	To Share Application A/c				40,000
	(Application money received on 10,000 shares @ Rs. 4 per share)				
	Share Application A/c	Dr.		40,000	
	To Share Capital A/c				40,000
	(Application money transferred to Share Capital)				
	Share Allotment A/c	Dr.		30,000	
	Discount on Issue of Share A/c	Dr.		10,000	
	To Share Capital A/c				40,000
	(Amount due @ Rs. 3 per share on Allotment and @ Re. 1 per share discount on 10,000 shares allotted)				
	Bank A/c	Dr.		30,000	
	To Share Allotment A/c				30,000
	(Allotment money received on 10,000 shares)				
	Share First and Final call A/c	Dr.		20,000	
	To Share Capital A/c				20,000
	(Final Call of Rs. 2 per share due on 10,000 shares)				

	Bank A/c Dr. To Share First and Final Call A/c (Final call money received on 10,000 shares)			20,000	20,000

Issue of Shares for Consideration other than Cash

There are instances where a company enters into an arrangement with the vendors from whom it has purchased assets, whereby the latter agrees to accept, the payment in the form of fully paid shares of the company issued to them. Normally, no such cash is received for issue of shares. These shares can also be issued either at par, at premium or at discount, and the number of shares to be issued will depend upon the price at which the shares are issued and the amount payable to the vendor. The number of shares to be issued to the vendor will be calculated as follows:

$$\text{Number of shares to be issued} = \frac{\text{Amount Payable}}{\text{Issue Price}}$$

For example, Rahul Limited purchased building from Handa Limited for Rs.5,40,000 and the payment is to be made by the issue of shares of Rs.100 each. The number of shares to be issued shall be worked out as follows in different situations:

(a) When shares are issued at par, i.e. at Rs.100

$$\text{Number of shares to be issued} = \frac{\text{Amount Payable}}{\text{Issue Price}}$$

$$= \frac{\text{Rs. } 5{,}40{,}000}{\text{Rs. } 100}$$

$$= 5{,}400 \text{ shares}$$

(b) When shares issued at a discount of 10%, i.e. at Rs.90 (100 - 10)

$$\text{Number of shares issued} = \frac{\text{Amount payable}}{\text{Issue price}}$$

$$= \frac{540000}{90}$$

(c) When shares issued at premium of 20%, i.e. at Rs.120 (100 + 20)

Number of shares to be issued = $\frac{\text{Amount Payable}}{\text{Issue Price}}$

$= \frac{\text{Rs. } 5{,}40{,}000}{\text{Rs. } 120}$

= 4,500 shares

The journal entries recorded for the shares issued for consideration other than cash in above situations will be as follows:

Books of Rahul Limited

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Building A/c Dr. To Handa Limited (Building purchased)		5,40,000	 5,40,000
(a)	***When shares are issued at par*** Handa Limited Dr. To Share Capital A/c (5,400 Shares issued at par)		 5,40,000	 5,40,000
(b)	***When shares are issued at Discount of 10%*** Handa Limited Dr. Discount on Issue of Shares A/c Dr. To Share Capital A/c (6,000 shares issued at Rs.90 per share)		 5,40,000 60,000	 6,00,000
(c)	***When shares are issued at premium of 20%*** Handa Limited Dr. To Share Capital A/c To Securities Premium A/c (4,500 shares issued at Rs.120 per share)		 5,40,000	 4,50,000 90,000

Illustration 10

Jindal and Company purchased a machine from High Life Machine Limited for Rs.3,80,000. As per purchase agreement, Rs. 20,000 were paid in cash and balance by issue of shares of Rs.100 each. What will be the entries passed if the shares are issued :

(a) at par

(b) at 10% discount

(c) at 20% premium

Solution:

Number of shares will be calculated as follows:

(vii) When shares issued at par $\frac{\text{Rs. } 3,60,000}{\text{Rs.}100}$

= 3,600 shares

(vi) When shares issued at discount $\frac{\text{Rs. } 3,60,000}{\text{Rs.}9}$

= 4000 shares

(iii) When shares issued at premium $\frac{\text{Rs. } 3,60,000}{\text{Rs.}120}$

= 3000shares

Books of Jindal and Company
Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Machine A/c Dr.		3,80,000	
	To Bank A/c			20,000
	To High Life Machine Limited			3,60,000
	(Machine purchased and Rs.20,000 paid in cash and the balance paid by issue of share)			
	(a) ***When shares are issued at par***			
	High Life Machine Limited Dr.		3,60,000	
	To Share Capital A/c			3,60,000
	(3,600 Shares of Rs.100 each)			
	(b) ***When shares are issued at discount***			
	High Life Machine Limited Dr.		3,60,000	
	Discount on Issue of Shares A/c Dr.		40,000	
	To Share Capital A/c			4,00,000
	(4,000 shares of Rs.90 per share issued at discount)			

(c) When shares are issued at premium

High Life Machine Limited Dr.	3,60,000	
To Share Capital A/c	3,00,000	
To Securities Premium A/c		60,000
(3,000 shares issued at Rs.120 per share)		

Forfeiture of Shares

It may happen that some shareholders fail to pay one or more instalments, viz. allotment money and/or call money. In such circumstances, the company can forfeit their shares, i.e. cancel their allotment and treat the amount already received thereon as forfeited to the company within the framework of the provisions in its articles. These provisions are usually based on Table A which authorise the directors to forefeit the shares for non-payment of calls made. For this purpose, they have to strictly follow the procedure laid down in this regard. Following is the accounting treatment of shares issued at par, premium or at a discount. When shares are forefeited all entries relating to the shares forfeited except those relating to premium, already recorded in the accounting records must be reversed. Accordingly, share capital account is debited with the amount called-up in respect of shares are forfeited and crediting the respective unpaid calls accounts's or calls in arrears account with the amount already received. Thus, the journal entry will be as follows:

Forfeiture of shares issued at par

Share capital a/c dr

To share forfeiture

To share allotment

To share calls

(……... shares forfeited for non payment of allotment money and calls made)

It may be noted here that when the shares are forfeited, all entries relating to the forfeited shares must be reversed except the entry relating to share premium received, if any. Accordingly, the share capital is debited to the extent to called-up capital and credited to (i) respective unpaid calls account i.e., calls in arrears and (ii) share forfeiture account with the amount already received on shares. The balance of shares forfeited account is shown as an addition to the total paid-up capital of the company under the head 'Share Capital' under title 'Equity and Liabilities' of the Balance Sheet till the forfeited shares are reissued.

Illustration 11

Honda Limited issued 10,000 equity shares of 100 each payable as follows: Rs. 20 on application, Rs. 30 on allotment, Rs. 20 on first call and Rs. 30 on second and final calls 10,000 shares were applied for and allotted. All money due was received with the exception of both calls on 300 shares held by Supriya. These shares were forfeited. Give necessary journal entries.

Solution

Books of Honda Limited

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c Dr. To Share Application A/c (Application money on 10,000 shares @Rs.20 per share received)		2,00,000	2,00,000
	Share Application A/c Dr. To Share Capital A/c (Application money transferred to share capital)		2,00,000	2,00,000
	Share Allotment A/c Dr. To Share Capital A/c (Money due on allotment of 10,000 shares @Rs. 30 per share)		3,00,000	3,00,000
	Bank A/c Dr. To Share Allotment A/c (Allotment Money received on 10,000 shares @ Rs. 30 per share on)		3,00,000	3,00,000
	Share First Call A/c Dr.		2,00,000	

	To Share Capital A/c (Money due on 10,000 shares @ Rs. 20 per share on Ist Call)			2,00,000

	Bank A/c Dr. To Share First Call A/c (First call money received except for 300 shares)		1,94,000	1,94,000
	Share Second and Final Call A/c Dr. To Share Capital A/c (Money due on 10,000 shares @ Rs. 30 per share on Second and Final Call)		3,00,000	3,00,000
	Bank A/c Dr. To Share Second and Final Call A/c (Second and Final Call money received except for 300 shares)		2,91,000	2,91,000
	Share Capital A/c Dr. To Share First Call A/c To Share Second and Final Call A/c To Share Forfeiture A/c (300 shares Forfeited)		30,000	 6,000 9,000 15,000

Forfeiture of Shares issued at a Premium: If shares were initially issued at a premium and the premium amount has been fully realised, but some of the shares are forfeited due to non-payment of call money, the accounting for treatment forfeiture shall be on the same pattern as in the case of shares issued at par. The important point to be noted in this context is that the securities premium account is not to be debited at the time of forfeiture if the premium has been received in respect of the forefeited shares and the amount of forfeiture shall be excluding premium amount.

In case, however, if the premium amount has not been received, either wholly or partially, in respect of the shares forfeited, the Securities Premium Account will also be debited with the amount of premium not received along with the Share Capital Account at the time forfeiture. This will usually be the case when even the amount due on allotment has not been received. Thus, the journal entry to record the forfeiture of shares issued at a premium on which premium has not been fully received, will be :

Share Capital A/c	Dr
Securities Premium A/c	Dr
To Share Forfeiture A/c	
To Share Allotment A/c and/or	
To Share Calls A/c (individually)	

(..... shares forefeited for non-payment of allotment money and calls made)

Note: If Calls in Arrears Account is maintained, Calls in Arrears Account is credited and not the Share Allotment and/or Share Call/Calls Accounts.

Illustration 12

Sahil, a share holder, failed to pay the money for second and final call of Rs. 20 on 1,000 shares issued to him at Rs. 120 (face value of Rs. 100 per share). His shares were forfeited after the second and final call. Give the necessary journal entry for forefeiture of the shares.

Solution:

Date	Particulars		L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Share Capital A/c	Dr.		1,00,000	
	To Share second and Final Call	A/c			20,000
	To Share Forfeiture A/c				80,000
	(Forfeiture of 1,000 shares for non-payment of the second and final call)				

Illustration

Sunena, a shareholder holding 500 shares of Rs.10 each, did not pay the allotment money of Rs. 4 per share (including a premium of Rs. 2) and the first and final call of Rs. 3. Her shares were forfeited after the first and final call. Give journal entry for forefeiture of the shares.

Solution:

Date	Particulars		L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Share Capital A/c	Dr.		5 ,000	
	Securities Premium A/c	Dr.		1,000	
	To Share Allotment A/c				2,000
	To Share first and final Call A/c				1,500
	To Share Forfeiture A/c				2,500
	(Forfeiture of 500 shares for non-payment of first and final call)				

Forfeiture of Shares Issued at a Discount: Where shares forfeited were initially issued at a discount, the discount applicable to such shares must be cancelled or written back. Hence, the Discount on Issue of Shares Account should be credited at the time of forfeiture. Thus, the journal entry to record the forfeiture will be :

Share Capital A/c Dr.

To Share Forfeiture A/c

To Discount on Issue of Shares A/c

To Share Allotment A/c

To Share Calls A/c or

To Calls in Arrears A/c

(Forefeiture of ..... shares for non-payment of allotment money and the calls made).

Illustration

Madan Limited invited application for 20,000 shares of Rs. 100 each at a discount of 10%, payable at Rs. 25 on application, Rs. 25 on allotment, Rs. 25 on first call and Rs. 15 on second and final call. Ritu who applied for 1,000 shares was allotted 600 shares and the excess application money adjusted against the allotment money on the shares allotted. These shares were forfeited after the first call. Journalise the transaction for forfeiture after she having failed to pay:

1. The allotment money and the first call; and
2. The first call only.

Solution:

Books of Madan Limited

Journal

1. When the Allotment and first call is not paid

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Share Capital A/c Dr.		51,000	
	To Discount on Issue of Shares A/c			6,000
	To Share Allotment A/c			5,000
	To Share First Call A/c			15,000
	To Share Forfeiture A/c			25,000
	(600 shares forfeited after First Call for non-payment of allotment and First Call money)			

Working Note:

Application money paid by Ritu on 1,000

Shares Application = 25,000

money required on 600 Shares allotted

Excess application = 15000

money paid by Ritu adjusted against allotment = 10000

2. When only the first call is not paid

Date	Particulars	L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Share Capital A/c Dr.		51,000	
	To Discount on issue of shares A/c			6,000
	To Share First Call A/c			15,000
	To Share Forfeiture A/c			30,000
	(600 shares forfeited after first call on non-payment of first call money)			

Illustration 13

Ashok Limited issued 3,00,000 equity shares of Rs. 10 each at a premium of Rs. 2 per share, payable as Rs. 3 on application, Rs. 5 on allotment (including premium) and the balance in two calls of equal amount.

Applications were received for 4,00,000 shares and pro-rata allotment was made to all the applicants. The excess application money was adjusted towards allotment. Mukesh who was allotted 800 shares failed to pay both the calls and his shares were forfeited after the second call. Record necessary journal entries in the books of Ashok Limited and also show the balance sheet:

Solution:

Books of Ashok Limited

Journal

Date	Particulars	L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
	Bank A/c Dr.		12,00,000	
	To Equity Share Application A/c			12,00,000
	(Application money received on 4,00,000 shares)			

	Equity Share Application A/c Dr. To Equity Share Capital A/c To Equity Share Allotment A/c (Application money on 3,00,000 shares transferred to share capital account and the excess amount adjusted to share allotment account)		12,00,000	 9,00,000 3,00,000
	Equity Share Allotment A/c Dr. To Equity Share Capital A/c To Securities Premium A/c (Allotment money due on 3,00,000 shares)		15,00,000	 9,00,000 6,00,000

	Bank A/c Dr. To Equity Share Allotment A/c (Allotment amount received after adjusting excess money received with application)		12,00,000	 12,00,000
	Equity Share First Call A/c Dr. To Equity Share Capital A/c (First Call amount due on 3,00,000 shares)		6,00,000	 6,00,000
	Bank A/c Dr. Calls in Arrears A/c Dr. To Equity Share First Call A/c (First Call amount received on 2,99,200 shares)		5,98,400 1,600	 6,00,000
	Equity Share Second and Final Call A/c Dr. To Equity Share Capital A/c (Second Call amount due on 3,00,000 Shares)		6,00,000	 6,00,000
	Bank A/c Dr. Calls in Arrears A/c Dr. To Equity Share Second and Final Call A/c (Amount on 2,99,200 shares received)		5,98,400 1,600	 6,00,000
	Equity Share Capital A/c Dr. To Share Forfeiture A/c To Call in Arrears A/c (Forfeiture of 800 shares)		8,000	 4,800 3,200

Balance Sheet of Ashok Limited as on ....

Particulars	*Note No.*	*Amount (Rs.)*
I EQUITY AND LIABILITIES		
1.Shareholders' Funds		
(a) Share Capital	1	29,96,800
(b) Reserves and Surplus	2	6,00,000
		35,96,800
II ASSETS		
1.Current Assets		
Cash and Cash Equivalents	3	35,96,800
		35,96,800

Notes to Accounts

1. Share Capital		*Rs.*
Authorised Capital		
... Equity shares of Rs. 10 each		
Issued Capital		
3,00,000 Equity shares of Rs. 10 each		**30,00,000**
Subscribed Capital		
Subscribed and Fully Paid-up		
2,99,200 Equity shares of Rs. 10 each		29,92,000
Add: Share forfeiture accounts		4,800
		29,96,800
2. ***Reserves and Surplus***		
Securities Premium Reserve		**6,00,000**
3. ***Cash and Cash Equivalents***		
Cash at bank		**35,96,800**

Illustration 14

High Light India Ltd. invited applications for 30,000 Shares of Rs. 100 each at a premium of Rs. 20 per share payable as follows :

On Application Rs. 40 (including Rs.10 premium)

On Allotment Rs. 30 (including Rs.10 premium)

On First Call Rs. 30

On Second and Final Call Rs. 20

Applications were received for 40,000 shares and pro-rata allotment was made on the application for 35,000 share. Excess application money was utilised towards allotment.

Rohan to whom 600 shares were allotted failed to pay the allotment money and his shares were forfeited immediately after allotment.

Aman who applied for 1,050 shares failed to pay first call and his share were forfeited immediatelyafter first Call.

Second and final call was made. All the money due on second call have been received.

Of the shares forfeited, 1,000 share were reissued as fully paid-up for Rs. 80 per share, which included the whole of Aman's shares.

Record necessary journal entries in the books of High Light India Ltd.

Solution:

Date	*Particulars*	*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c Dr. To Share Application A/c (Application money received on 40,000 shares)		16,00,000	16,00,000

	Particulars		Dr.	Cr.
	Share Application A/c Dr. To Share Capital A/c To Securities Premium A/c To Share Allotment A/c (Application money transferred to share capital account, securities premium account and the excess money transfered to share allotment account)		14,00,000	 9,00,000 3,00,000 2,00,000
	Share Application A/c Dr. To Bank A/c (Amount returned on 500 shares)		2,00,000	 2,00,000
	Share Allotment A/c Dr. To Share Capital A/c To Securities Premium A/c (Money due on allotment)		9,00,000	 6,00,000 3,00,000
	Bank A/c Dr. To Share Allotment A/c (Amount received in allotment)		6,86,000	 6,86,000
	Share Capital A/c Dr. Securities Premium A/c Dr. To Share Allotment A/c To Share Forfeiture A/c (Forfeiture of 600 shares of Rohan for non-payment of allotment money)		30,000 6,000	 14,000 22,000
	Share First Call A/c Dr. To Share Capital A/c (First Call money due on 29,400 shares)		8,82,000	 8,82,000
	Bank A/c Dr. To Share First Call A/c (First call money received on 28,500 shares)		8,55,000	 8,55,000
	Share Capital A/c Dr. To Share First Call A/c To Share Forfeiture A/c (Forfeiture of 900 Aman Shares)		72,000	 27,000 45,000
	Share Second and Final Call A/c Dr. To Share Capital A/c		5,70,000	 5,70,000

	(Second and Final Call money due on 28,500 shares)			
	Bank A/c Dr. To Share Second and Final Call A/c (Due money received)		5,70,000	5,70,000
	Bank A/c Dr. Share Forfeiture A/c Dr. To Share Capital A/c (Reissue of 1,000 forfeited shares)		80,000 20,000	1,00,000
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Profit on 1,000 reissued shares transferred to capital reverve)		18,333	18,333

(I)Excess amount received on Rohan's application

Rohan has been alloted = 600 Shares

He must have applied for Rs. 35,000

Rs. 30,000 600 700 Shares

		Rs.
Amount received from Rohan	= 700 × Rs. 40	28,000
Amount Adjusted on Application	= 600 × Rs. 40	(24,000)
Amount Adjusted on Allotment		4,000
Money due on Allotment	= 600 × Rs. 30	8,000
Money Adjusted		(4,000)
Balance due on Allotment		14,000

(II) Amount recieved on allotment

Total Amount due on Allotment = Rs. 30,000 × Rs. 30

= 9,00,000

Amount received on Application	(2,00,000)
	7,00,000
Amount not received on Rohan's Share	(14,000)
	6,86,000

(III) Money received on First Call

First Call money due on 29,400 shares 29,400 × Rs. 30

= 8,82,000

Application money not received on 900 Shares

900 × Rs. 30 (27,000)

8,55,000

(IV) 1000 shares have been reissued including 900 shares of Aman and Balance 100 shares of Rohan 22,000

Profit on 100 shares = 100= 3,667

600

Profit in 900 shares = 45,000

48,667

Less: Loss on reissue of 1,000 shares (20,000)

28,667

(V) Balance in Share Forfeiture Account of 500 shares

22,000

Rs. 500 = Rs. 18,333

600

Illustration 15

Working Notes :

X Ltd. issued for public subscription 40,000 equity shares of Rs. 10 each at premium of Rs. 2 per share payable as under :

On application	Rs. 4 per share
On Allotment	Rs. 5 per share (including premium)
On Call	Rs. 3 per share

Applications were received for 60,000 shares. Allotment was made pro-rata to the applicants for 48,000 shares, the remaining applications being rejected. Money overpaid on application was applied towards sums due on allotment. Shri Chitnis, to whom 1,600 shares were allotted, failed to pay the allotment money and Shri Jagdale, to whom 2,000 shares were allotted, failed to pay the call money. These shares were subsequently forfeited.

Record journal entries in the books of the company to record the above transactions

Solution:

Books of X Ltd.

Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Bank A/c	Dr.		2,40,000	
	To Equity Share Application A/c				2,40,000
	(Money received on applications for 60,000 shares @ Rs. 4 per share)				
	Equity Share Application A/c	Dr.		2,40,000	
	To Equity Share Capital A/c				1,60,000
	To Equity Share Allotment A/c				32,000
	To Bank a/c				48,000
	(Application amount transferred to share capital, excess application money under pro-rata distribution credited to share allotment and money refunded on rejected application)				
	Equity Share Allotment A/c	Dr.		2,00,000	
	To Equity Share Capital A/c				1,20,000
	To Securities Premium A/c				80,000
	(Amount due on allotment of 40,000 shares @ Rs. 5 per share including premium)				
	Bank A/c	Dr.		1,61,280	
	Calls-in-Arrears A/c	Dr.		6,720	
	To Equity Share Allotment A/c				1,68,000
	(Money received consequent upon allotment)				
	Equity Share Call A/c	Dr.		1,20,000	
	To Equity Share Capital A/c				1,20,000
	(First call money due on 40,000 shares @ Rs. 3 per share)				

	Bank A/c	Dr.		1,09,200	
	Calls-in-Arrears A/c	Dr.		10,800	
	To Equity Share Call A/c				1,20,000
	(Money received on first call)				
	Equity Share Capital A/c	Dr.		36,000	
	Securities Premium A/c	Dr.		3,200	
	To Share Forfeiture A/c				21,680
	To Call-in-Arrears A/c				17,520
	(Entry for forfeiture of 3,600 shares)				

Working Notes :

I. Amount received on allotment

	Rs.
(a) Amount due on allotment	2,00,000
40,000 shares × Rs. 5 per share	
(b) Amount actually due on allotment	2,00,000
Amount due on allotment	
Less Excess Application amount applied for allotment	32,000
Amount actually due	1,68,000
(c) Allotment amount due from Chitnis	
Allotment money due on Chitnis's share	
1,600 shares × Rs. 5 per share	8,000
Less excess application money paid	
Due to pro-rata distribution –	
(1,920 shares – 1,600 shares) 320 × 4	1,280
Allotment amount due from Chitnis	6,720

According to the ratio of pro-rata distribution (40,000 shares : 48,000 shares), for 1,600 shares to be allotted, Chitnis must have applied for 1,920 shares (1,600 shares × 6/5).

(d) Allotment money received	
(Amount actually due on Allotment)	1,68,000
Less Amount unpaid by Chitnis	(6,720)
Amount received	1,61,280

II. Balance on Shares Forfeited Account

Amount paid by Chitnis :	
1,920 Shares applied for × Rs. 4 per share	7,680
Amount paid by Jagdale :	
2,000 Shares × (Rs. 4 + Rs. 3) Rs.7 per share	14,000
Total balance	21,680

Note : Premium amount on Jagdale's shares will not be taken into account as it has been received in full by the company.

Re-issue of Forfeited Shares

The directors can either cancel or re-issue the forefeited shares. In most cases, they reissue such shares which may be at par, at premium or at a discount. Forfeited shares may be reissued as fully paid at a par, premium, discount. In this context, it may be noted that the amount of discount allowed cannot exceed the amount that had been received on forfeited shares at the time of initial issue, and that the discount allowed on reissue of forfeited shares should be debited to the 'Forfeited Share Account'. The balance, if any, left in the Share-Forfeited Account relating to reissued Shares, should be treated as capital profit and transferred to Capital Reserve Account. For example, when a company forfeits 200 shares of Rs. 10 each on which Rs. 600 had been received, it can allow a maximum discount of Rs. 600 on their reissue. Assuming that the company reissues these shares for Rs. 1,800 as fully paid, the necessary journal entry will be:

Bank A/c Dr. 1,800

Share Forfeiture A/c Dr. 200

To Share Capital A/c 2,000

(Reissue of 200 forfeited shares at Rs. 9 per share as fully paid)

This shall leave a balance of Rs. 400 in share forfeited account which should be transferred to Capital Reserve Account by recording the following journal entry:

Share Forfeiture A/c Dr. 400

To Capital Reserve 400

(Profit on reissue of forfeited shares transferred)

Another important point to be noted in this context is that the capital profit arises only in respect of the forefited share reissued, and not on all forefeited shares. Hence, when a part of the forfeited shares are reissued, the whole balance of share forfeiture account cannot be transferred to the capital reserve. In such a situation, it is only the Note : Premium amount on Jagdale's shares will not be taken into account as it has been received in proportionate amount of balance that relates to the forfeited shares reissued which should be transferred to capital reserve, ensuring that the remaining balance in share forfeiture account is proportionate to the amount forfeited on shares not yet reissued.

Illustration 16

The director of Poly Plastic Limited resolved that 200 equity shares of Rs.100 each be forfeited for non-payment of the second and final call of Rs.30 per share. Out of these, 150 shares were re-issued at Rs.60 per share to Mohit. Show the necessary journal entries .

Solution:

Books of Poly Plastic Limited

Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Share Capital A/c	Dr.		20,000	
	To Shares Forfeiture A/c				14,000
	To Share Second and Final Call A/c				6,000
	(200 shares forfeited for non-payment of final call at Rs.30 per share)				
	Bank A/c	Dr.		9,000	
	Shares Forfeiture A/c	Dr.		6,000	
	To Share Capital A/c				15,000
	(Reissue of 150 shares of Rs.100 each, issued as fully paid for Rs.60 each)				
	Shares Forfeiture A/c	Dr.		4,500	
	To Capital Reserve A/c				4,500
	(Profit on reissue of 150 forfeited shares transferred to capital reserve)				

Working Notes :

		(Rs.)
Total amount forfeited on 200 shares	=	14,000
		(200 shares × Rs.70)
Amount forfeited on 150 shares	=	10,500
		(150 shares × Rs.70)
Amount forfeited on 50 shares	=	3,500
		(50 shares × Rs.70)
Amount of loss on reissue of 150 shares	=	6,000
		(150 shares × Rs.40)
Amount of profit on reissued shares transferred to capital reserve	=	4,500
		(Rs. 10,500 - Rs.6,000)
Balance left in share forfeited account	=	3,500
		(Rs.14,000 - Rs.6,000
(equal to amount forfeited on 50 shares)		- Rs. 4,500)

Illustration 17

On January 1, 2015, the Director of X Ltd. issued for public subscription 50,000 equity shares of Rs. 10 each at Rs. 12 per share payable as to Rs. 5 on application (including premium), Rs. 4 on allotment and the balance on call on May 01, 2015.

The lists were closed on February 10, 2015 by which date applications for 70,000 shares were received. Of the cash received Rs. 40,000 was returned and Rs.60,000 was applied to the amount due on allotment, the balance of which was paid on February 16, 2015.

All the shareholders paid the call due on May 01, 2015 with the exception of an allottee of 500 shares. These shares were forfeited on September 29, 2015 and reissued us fully paid at Rs. 8 per share on November 01, 2015. The company, as a matter of policy, does not maintain a calls-in-arrears account.Give journal entries to record these share capital transactions in the books of X. Ltd.

Solution:

Book of X. Ltd. (Journal)

Date 2015	Particulars		L.F.	Debit Amount (Rs.)	Credit Amount (Rs.)
Feb.10	Bank A/c	Dr.		3,50,000	
	To Equity Share Application A/c				3,50,000
	(Amount received on application for 70,000 shares @ Rs. 5 per share Including Premium)				
Feb.16	Equity Share Application A/c	Dr.		2,50,000	
	To Equity Share Capital A/c				1,50,000
	To Securities Premium A/c				1,00,000
	(Transfer of application money on 50,000 shares to share capital and premium accounts consequent upon allotment)				
Feb.16	Equity Share Application A/c	Dr.		1,00,000	
	To Bank A/c				40,000
	To Equity Share Allotment A/c				60,000
	(Excess application money credited to share allotment and money refunded on rejected application)				
Feb.16	Equity Share Allotment A/c	Dr.		2,00,000	
	To Equity Share Capital A/c				2,00,000
	(Amount due on allotment of 50,000 Shares @ Rs. 4 per share)				
Feb.16	Bank A/c	Dr.		1,40,000	
	To Equity Share Allotment A/c				1,40,000
	(Money received on allotment)				
May 1	Equity Share First and Final Call A/c	Dr.		1,50,000	
	To Equity Share Capital A/c				1,50,000
	(First call money due)				

May 1	Bank A/c	Dr.		1,48,500	
	To Equity Share First and Final Call A/c				1,48,500
	(Money received on first call)				
Sept.29	Equity Share Capital A/c	Dr.		5,000	
	To Shares Forfeiture A/c				3,500
	To Equity Share First and Final Call A/c				1,500
	(Forfieted of 500 shares for non-payment of call)				
Nov. 1	Bank A/c	Dr.		4,000	
	Shares Forfeiture A/c	Dr.		1,000	
	To Equity Share Capital A/c				5,000
	(Reissue of 500 forfeited shares as fully paid at Rs. 8 per share)				
Nov. 1	Shares Forfeiture A/c	Dr.		2,500	
	To Capital Reserve				2,500
	(Profit on reissue of Forfeited Shares Accounts transferred to capital reserve)				

Illustration 18

A limited company forfeited 1,000 equity shares of Rs. 10 each, issued at a discount of 10 per cent, for non-payment of first call of Rs. 2 and second call of Rs. 3 per share. These shares were reissued to Kamal upon payment of Rs. 7,000 credited as fully paid. The company maintains calls-in-arrears account.

Record journal entries in the books of the company relating to forfeiture of 1,000 shares and their reissue.

Solution:

Books of A Limited Company
Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
	Equity Share Capital A/c	Dr.		10,000	
	To Shares Forfeiture A/c				4,000
	To Discount on the Issue of Shares A/c				1,000
	To Calls-in-Arrears A/c				5,000
	(Forfeiture of 1,000 shares for non-payment of call and discount on issue written back)				
	Bank A/c	Dr.		7,000	
	Discount on Issue of Shares A/c	Dr.		1,000	
	Shares Forfeiture A/c	Dr.		2,000	
	To Equity Share Capital A/c				10,000
	(Reissue of 1,000 forfeited shares as fully paid at Rs. 7 per share, discount on issue written back and the balance debited to Share Forfeiture Account)				
	Shares Forfeiture A/c	Dr.		2,000	
	To Capital Reserve A/c				2,000
	(Profit on reissue of Forfeiture Shares transfered to Capital reserve)				

Illustration 19

O Limited issued a prospectus offering 2,00,000 equity shares of Rs. 10 each, at a premium of Rs. 2 per share, payable as follows:

On Application Rs. 2.50 per share

On Allotment Rs. 4.50 per share

(including premium)

On First Call (three months from allotment)

Rs. 2.50 per share

On Second Call (three months after first call)

Rs. 2.50 per share

Subscriptions were received for 3,17,000 shares on April 23, 2014 and the

allotment made on April 30, was as under :

		Shares Allotted
(i)	Allotment in full (two applicants paid in full on allotment in respect of 4,000 shares each)	38,000
(ii)	Allotment of two shares for every three shares applied for	1,60,000
(iii)	Allotment of one share for every four shares applied for	2,000

Cash amounting to Rs. 77,500 (being application money received with applications on 31,000 shares upon which no allotments were made) was returned to applicants on May 6, 2014.

The amounts called from the allottees were received on the due dates with the exception of the final call on 100 shares. These shares were forfeited on November 15, 2014 and reissued to Aman on November 16 for payment of Rs. 9 per share.

Record journal entries other than those relating to cash, in the books of O Limited, and also show how the transactions would appear in the balance sheet, assuming that the Company paid interest due from it on October 31, 2014.

Solution:

Book of O Limited

Journal

Date 2014	*Particulars*		*L.F.*	*Debit Amount (Rs.)*	*Credit Amount (Rs.)*
April 30	Share Application A/c	Dr.		7,92,500	
	To Equity Share Capital A/c				5,00,000
	To Bank				77,500
	To Equity Share Allotment A/c				2,09,000
	To Calls in Advance				6,000
	(Transfer of Application Money to share capital after allotment and excess application money on 86,000 shares due to pro-rata allotment credited to share allotment and calls in advance)				
April 30	Equity Share Allotment A/c	Dr.		9,00,000	
	To Equity Share Capital A/c				5,00,000
	To Securities Premium A/c				4,00,000
	(Allotment amount due on 2,00,000 shares @ Rs. 4.50 per share including premium)				
	Bank A/c	Dr.		7,31,000	
	To Share Allotment				6,91,000
	To Calls in Advance				40,000
	(Allotment Money received on excess amount received adjusted)				
July 31	Equity Share First Call A/c	Dr.		5,00,000	
	To Equity Share Capital A/c				5,00,000
	(First call money due on 2,00,000 shares @ Rs. 2.50 per share)				
July 31	Bank A/c	Dr.		4,75,000	
	Calls in Advance	Dr.		25,000	
	To Share First Call				5,00,000
	(Call in advance on 8,000 shares adjusted against first call money due)				
Oct. 31	Equity Share Second and Final Call A/c	Dr.		5,00,000	
	To Equity Share Capital A/c				5,00,000
	(Second call money due on 2,00,000 shares @ Rs. 2.50 per share)				
Oct. 31	Bank A/c	Dr.		4,76,500	
	Calls in Advance A/c	Dr.		23,500	
	To Equity Share Second and Final Call A/c				5,00,000
	(Calls in advance on 8,000 shares adjusted against second call money due)				

Nov. 15	Equity Share Capital A/c Dr.		1,000	
	To Equity Share Forfeiture A/c			750
	To Equity Share Second and Final Call A/c			250
	(Forfeiture of 100 shares for the non-payment of call money)			
Nov. 16	Bank A/c Dr.		900	
	Share Forfeiture A/c		100	
	To Share Capital			1,000
	(Amount due from A for the reissue of 100 shares as fully paid at Rs. 9 per share)			
Nov. 16	Equity Share Forfeiture A/c Dr.		650	
	To Capital Reserve A/c			650
	(Profit on reissue of forfeited Shares transferred to Capital reserve)			

Cash Book

Dr. *Cr.*

Receipts	*Amount (Rs.)*	*Payments*	*Amount (Rs.)*
Equity Share Aplication	7,92,500	Equity Shares Application	77,500
Equity Share Allotment	6,85,000	Balance c/d	24,00,650
Calls in Advance	40,000		
Equity Share First Call	4,80,000		
Equity Share Second and Final Call	4,79,750		
Equity Share Capital	900		
	24,78,150		**24,78,150**

** Date column omitted.*

Working Notes :

1. Excess Application Money

Categories of Allotment	No. of Shares Applied	No. of Share Alloted	Ratio of Allotment
i	38,000	38,000	100%
ii	2,40,000	1,60,000	2/3
iii	8,000	2,000	¼
	2,86,000	**2,00,000**	

Therefore, refund of application money = (3,17,000 - 2,86,000) × Rs. 2.50

= Rs. 77,500

Application money received = Rs. 7,15,000
(2,86,000 shares @ Rs. 2.50)

Application money due : = Rs. 5,00,000
(2,00,000 shares @ Rs. 2.50)

Excess application money Rs. 2,15,000

2. Amount of Calls in Advance

As two allotees, each holding 4,000 shares, paid the full amount on allotment, amount of calls-in-advance is thus :

8,000 shares × (Rs. 2.50 + Rs. 2.50) = Rs. 40,000

Multiple Choice Questions

1. Company has ....
   (A) Separate Legal Entity (B) Perpetual Existence
   (C) Limited Liability (D) All of the Above
2. Shareholders are :
   (A) Customers of the Company
   (B) Owners of the Company
   (C) Creditors of the Company (D) None of these
3. Who are the real owners of a company?
   (A) Government (B) Board of Directors
   (C) Equity shareholders (D) Debenture holders
4. A Company is created by :
   (A) Special act of the Parliament (B) Companies Act
   (C) Investors (D) Members

5. Equity shares cannot be issued for the purpose of:
   (A) Cash Receipts (B) Purchase of assets
   (C) Redemption of debentures (D) Distribution of dividend
6. The shares on which there is no any pre-fixed rate of dividend is decided, but the rate of dividend is fluctuating every year according to the availability of profits, such share are called:
   (A) Equity Share
   (B) Non-cumulative preference share
   (C) Non-convertible preference share
   (D) Non-guaranteed preference share
7. Preference shares, in case the holders of these have a right to convert their preference shares into equity shares at their option according to the terms of issue, such shares are called:
   (A) Cumulative Preference Share
   (B) Non-cumulative Preference Share
   (C) Convertible Preference Share
   (D) Non-convertible Preference Share
8. Which shareholders have a right to receive the arrears of dividend from future profits :
   (A) Redeemable Preference Shares
   (B) Participating Preference Shares
   (C) Cumulative Preference Shares
   (D) Non-Cumulative Preference Shares
9. Which shareholders are returned their capital after some specified time :
   (A) Redeemable Preference Shares
   (B) Irredeemable Preference Shares
   (C) Cumulative Preference Shares
   (D) Participating Preference Shares
10. The following statements apply to equity/preference shareholders. Which one of them applies only to preference shareholders?
   (A) Shareholders risk the loss of investment

(B) Shareholders bear the risk of no dividends in the event of losses

(C) Shareholders usually have the right to vote

(D) Dividends are usually given at a set amount in every' financial year.

11. Unless otherwise stated, a preference share is always deemed to be :

    (A) Cumulative, participating and non-convertible

    (B) Non-cumulative, non-participating and non-convertible

    (C) Cumulative, non-participating and non-convertible

    (D) Non-cumulative, participating and non-convertible

Answers

1a, 2b, 3c, 4b, 4d, 6a, 7c, 8c, 9a, 10d, 11c

Short answer type questions

1. What is reserve capital?
2. Define equity share
3. Define sweet equity share
4. Define minimum subscription
5. What is security premium reserve?
6. What is meant by prorate allotment
7. What is meant by forfeiture of shares?
8. What is calls in arrears?
9. What is calls in advance?
10. What is surrender of shares
11. How will you treat balance in the forfeited shares account after the reissue of forfeited shares?
12. What is lien on shares?
13. What is employees stock options scheme?

Short answer type questions

1. Explain different categories of share capital
2. Distinguish between reserve capital and Capital reserve
3. Distinguish between equity shares and preference shares
4. Distinguish between stock and shares

5. What is security premium reserve? State the purpose for which balance in the security premium can be utilized?
6. State how is fraction shares treated in company accounts?
7. What are the differences between calls in arrears and calls in advance
8. What are the steps involved in annulment of forfeiture?
9. How would you calculate the profit on reissue of forfeited shares?
10. What is surrender of shares? Does it different from forfeiture of shares?
11. Distinguish between surrender of shares and forfeiture of shares?

References:

1. M.C. Shukla, T.S. Grewal and S. C. Gupta, Advanced Accounts, S. Chand &Co., New Delhi.
2. S.N. Maheswari and S.K. Maheswari, Financial Accounting.

MODULE 3

DEBENTURE

A company can borrow money for meeting its short term as well as the long term requirements. For meeting it short term requirements, a company usually borrows from a bank by way of loan, overdraft or cash credit. For meeting its long term requirements, a company generally borrows from the public by issuing debentures.

The word 'debenture' itself is a derivation of the Latin word 'debere' which means to borrow or loan. Debentures are written instruments of debt that companies issue under their common seal. They are similar to a loan certificate.

Debentures are issued to the public as a contract of repayment of money borrowed from them. These debentures are for a fixed period and a fixed interest rate that can be payable yearly or half-yearly. Debentures are also offered to the public at large, like equity shares. Debentures are actually the most common way for large companies to borrow money.

Bond: Bond is also an instrument of acknowledgement of debt. Traditionally, the Government issued bonds, but these days, bonds are also being issued by semi-government and non-governmental organisations. The terms 'debentures' and 'Bonds' are now being used inter-changeably.

Distinction between Shares and Debentures

Ownership: A 'share' represents ownership of the company whereas a debenture is only acknowledgement of Debt. A share is a part of the owned capital whereas a debenture is a part of borrowed capital.

Return: The return on shares is known as dividend while the return on debentures is called interest. The rate of return on shares may vary from year to year depending upon the profits of the company but the rate of interest on debentures is prefixed. The payment of dividend is an appropriation of profits, whereas the payment of interest is a charge on profits and is to be paid even if there is no profit.

Repayment: Normally, the amount of shares is not returned during the life of the company, whereas, generally, the debentures are issued for a specified period and repayable on the expiry of that period. However, in the year 1998, the amendements (Section 77A and 77 B sub Section 2) in the Companies Act, permitted companies to buy back its shares specially when market value of shares are less than its book value.

Voting Rights: Shareholders enjoy voting rights whereas debenture holders do not normally enjoy any voting right.

Security : Shares are not secured by any charge whereas the debentures are generally secured and carry a fixed or floating charge over the assets of the company.

Convertibility: Shares cannot be converted into debentures whereas debentures can be converted into shares if the terms of issue so provide, and in that case these are known as convertible debentures.

Types of Debentures

A company may issue different kinds of debentures which can be classified as under

From the Point of view of Security

(ii) Secured Debentures: Secured debentures refer to those debentures where a charge is created on the assets of the company for the purpose of payment in case of default. The charge may be fixed or floating. A fixed charge is created on a specific asset whereas a floating charge is on the general assets of the company. The fixed charge is created against those assets which are held by a company for use in operations not meant for sale whereas floating charge involves all assets excluding those assigned to the secured creditors.

(iii) Unsecured Debentures: Unsecured debentures do not have a specific charge on the assets of the company. However, a floating charge may be created on these debentures by default. Normally, these kinds of debentures are not issued.

From the Point of view of Tenure

(iv) Redeemable Debentures: Redeemable debentures are those which are payable on the expiry of the specific period either in lump sum or in Installments during the life time of the company. Debentures can be redeemed either at par or at premium.

(v) Irredeemable Debentures: Irredeemable debentures are also known as Perpetual Debentures because the company does not give any undertaking for the repayment of money borrowed by issuing such debentures. These debentures are repayable on the winding-up of a company or on the expiry of a long period.

From the Point of view of Convertibility

(iii) Convertible Debentures: Debentures which are convertible into equity shares or in any other security either at the option of the company or the debenture holders are called convertible debentures. These debentures are either fully convertible or partly convertible.

(iv) Non-Convertible Debentures: The debentures which cannot be converted into shares or in any other securities are called non-convertible debentures. Most debentures issued by companies fall in this category.

From Coupon Rate Point of view

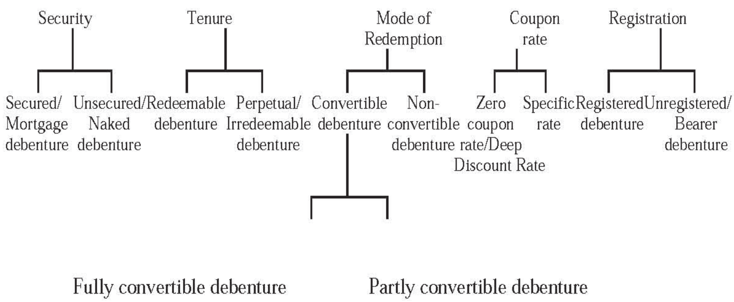
8. Specific Coupon Rate Debentures: These debentures are issued with a specified rate of interest, which is called the coupon rate. The specified rate may either be fixed or floating. The floating interest rate is usually tagged with the bank rate.
9. Zero Coupon Rate Debentures: These debentures do not carry a specific rate of interest. In order to compensate the investors, such debentures are issued at substantial discount and the difference between the nominal value and the issue price is treated as the amount of interest related to the duration of the debentures.

From the view Point of Registration

(c) Registered Debentures: Registered debentures are those debentures in respect of which all details including names, addresses and particulars of holding of the debenture holders are entered in a register kept by the company. Such debentures can be transferred only by executing a regular transfer deed.

(d) Bearer Debentures: Bearer debentures are the debentures which can be transferred by way of delivery and the company does not keep any record of the debenture holders Interest on debentures is paid to a person who produces the interest coupon attached to such debentures.

Types of Debenture/Bond



Issue of Debentures

The procedure for the issue of debentures is the same as that for the issue of shares. The intending investors apply for debentures on the basis of the prospectus issued by the company. The company may either ask for the entire amount to be paid on application or by means of installments on application, on allotment and on various calls. Debentures can be issued at par, at a premium or at a discount. They can also be issued for consideration other than cash or as a collateral security.

Issue of Debentures for Cash

Debentures are said to be issued at par when their issue price is equal to the face value. The journal entries recorded for such issue are as under:

(a) If whole amount is received in one installment

On receipt of the application money

Bank A/c Dr.

To Debenture Application & Allotment A/c

On Allotment of debentures

Debenture Application & Allotment A/c Dr.

To Debentures A/c

(b) If debenture amount is received in two installments:

On receipt of application money

Bank A/c Dr.

To Debenture Application A/c

For adjustment of applications money on allotment

Debenture Application A/c Dr.

To Debentures A/c

For allotment money due

Debenture Allotment A/c Dr.

To Debentures A/c

On receipt of allotment money

Bank A/c Dr.

To Debenture Allotment A/c

(c) If debenture money is received in more than two instalments Additional entries:

(i) On making the first call

Debenture First Call A/c Dr.

To Debentures A/c

(ii) On the receipt of the first call

Bank A/c Dr.

To Debenture First Call A/c.

Illustration

ABC Lmited issued Rs 10,000, 12% debentures of Rs 100 each payable Rs 30 on application and remaining amount on allotment. The public applied for 9,000 debentures which were fully allotted, and all the relevant allotment money was duly received. Give journal entries in the books of ABC Ltd., and exhibit the relevent information in the balance sheet.

Solution:

Books of ABC Limited

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Bank A/c Dr. To 12% Debenture Application A/c (Application money on 9,000 debentures received)		2,70,000	2,70,000
	12% Debenture Application A/c Dr. To 12% Debentures A/c (Application money transferred to debentures		2,70,000	2,70,000

	Account on allotment)			
	12% Debenture Allotment A/c Dr. To 12% Debentures A/c (Amount due on 9,000 debentures on allotment @ Rs 70 per debenture)		6,30,000	6,30,000
	Bank A/c Dr. To 12% Debenture Allotment A/c (Amount received on allotment)		6,30,000	6,30,000

ABC Limited

*Balance Sheet as at ....

Particulars	*Note No.*	*Amount (Rs)*
I. Equity and Liabilities		
Non-current liabilities	1	9,00,000
Long-term borrowings		
II. Assets		
Current assets		
Cash and cash equivalents	2	9,00,000

Particulars	*Amount (Rs)*
1. Long-term borrowings 9,000, 12% Debentures of Rs 100 each	9,00,000
2. Cash and cash equivalents Cash at bank	9,00,000

Issue of Debentures at a Discount

When a debenture is issued at a price below its nominal value, it is said to be issued at a discount. For example, the issue of Rs. 100 debentures at Rs. 95, Rs. 5 being the amount of discount. Discount on issue of debentures is a capital loss and is shown under the line item 'Other Non-Current Assets' or 'Other Current Assets' depending upon the time period in which it is to be written off. The discount on issue of debentures can be written off either by debiting it to Statement of Profit and Loss or out of Securities Premium Reserve A/c, if any, during the life time of debentures.

Discount on issue of debentures to be written off within 12 months of the balance sheet date or the period of operating cycle is shown under 'Other Current Assets' and the part which is to be written off after 12 months of balance sheet is shown under 'Other Non-Current Assets'.

The Companies Act, 2013 does not impose any restrictions upon the issue of debentures at a discount.

Illustration 1

TV Components Ltd., issued 10,000, 12% debentures of Rs 100 each at a discount of 5% payable as follows:

On application Rs 40

On allotment Rs 55

Show the journal entries including those for cash, assuming that all the installments were duly collected. Also show the relevant portion of the balance sheet.

Solution:

Books of TV Components Ltd.

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Bank A/c Dr. To 12% Debenture Application A/c (Receipt of application money @ Rs 30 per debenture)		4,00,000	 4,00,000
	12% Debenture Application A/c Dr. To 12% Debenture A/c (Transfer of application money to debenture account)		4,00,000	 4,00,000
	12% Debenture Allotment A/c Dr. Discount on Issue of Debentures A/c To 12% Debenture A/c (Allotment money due on debentures)		5,50,000 50,000	 6,00,000

	Bank A/c Dr.			5,50,000	
	To 12% Debenture Allotment A/c				5,50,000
	(Receipt of allotment money on debentures)				

TV Components Limited

Balance Sheet as at..................

Particulars	*Note No.*	*Amount (Rs)*
I. Equity and Liabilities		
1. Non-current Liabilities		
Long-term borrowings	1	10,00,000
II. Assets		
1. Non-current assets		
Other non-current assets	2	45,000
2. Current assets		
a) Cash and cash equivalents	3	9,50,000
b) Other current assets	4	5,000
		10,00,000

Notes to Accounts

Particulars	*Amount (Rs)*
1. Long-term borrowings	
10,000, 12% secured debentures of Rs 100 each	10,00,000
2. Other non-current assets	
Discount on issue of debentures	45,000
3. Cash and cash equivalents	
Cash at bank	9,50,000
4. Other current assets	
Discount on issue of debentures (To be written-off within 12 months of the balance sheet date or the period of operating cycle)	5,000

Debentures issued at Premium

A debenture is said to be issued at a premium when the price charged is more than its nominal value. For example, the issue of Rs 100 debentures for Rs 110, (Rs 10 is being the premium). The amount of premium is credited to Securities Premium Reserve account and is shown on the liabilities side of the balance sheet under the head "Reserves and Surpluses".

Illustration 2

XYZ Industries Ltd., issued 2,000, 10% debentures of Rs 100 each, at a premium of Rs 10 per debenture payable as follows:

On application	Rs 50
On allotment	Rs 60

e debentures were fully subscribed and all money was duly received. Record the journal entries in the books of a company. Show how the amounts will appear in the balance sheet.

Solution:

Books of XYZ Industries Limited
Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Bank A/c Dr.		1,00,000	
	To 10% Debenture Application A/c			1,00,000
	(Application money Rs 50 per debentures received)			
	10% Debenture Application A/c Dr.		1,00,000	
	To 10% Debentures A/c			1,00,000
	(Transfer of application money to debenture account)			
	10% Debenture Allotment A/c Dr.		1,20,000	
	To 10% Debentures A/c			1,00,000
	To Securities Premium Reserve A/c			20,000
	(Allotment money due on debentures including the premium)			
	Bank A/c Dr.		1,20,000	
	To 10% Debenture Allotment A/c			1,20,000
	(Allotment money received)			

XYZ Industries Limited
Balance Sheet as at ———

Particulars	*Note No.*	*Amount (Rs)*
I. Equity and Liabilities		
1. Shareholders' Funds		
Reserve and Surplus	1	20,000
2. Non-current Liabilities		
Long-term borrowings	2	2,00,000
		2,20,000
II. Assets		

Current Assets Cash and cash equivalents		2,20,000

Notes to Accounts

Particulars	*Amount (Rs)*
1. Reserve and surplus Securties Premium Reserve	20,000
2. Long-term borrowings 2,000, 10% debentures of Rs 100 each	2,00,000
3. Cash and cash equivalents Cash at bank	2,20,000

Illustration 3

A Limited issued 5,000, 10% debentures of Rs 100 each, at a premium of Rs 10 per debenture payable as follows:

On application Rs 25

On allotment Rs 45 (including premium)

On first and final call Rs 40

The debentures were fully subscribed and all money was duly received. Record the necessary entries in the books of the company. Show how the amounts will appear in the balance sheet.

Solution:

Books of ***A Limited***

Journal

Date	Particulars		L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Bank A/c	Dr.		1,25,000	
	To 10% Debenture Application A/c				1,25,000
	(Application money on 10% debentures received)				
	10% Debenture Application A/c	Dr.		1,25,000	
	To 10% Debentures A/c				1,25,000
	(Transfer of application money on allotment)				
	10% Debenture Allotment A/c	Dr.		2,25,000	
	To 10% Debentures A/c				1,75,000
	To Securities Premium Reserve A/c				50,000
	(Allotment money of due on debentures including the premium)				
	Bank A/c	Dr.		2,25,000	
	To 10% Debenture Allotment A/c				2,25,000
	(Allotment money received)				
	10% Debenture First & Final Call A/c	Dr.		2,00,000	
	To 10% Debentures A/c				2,00,000
	(First and final call money due on debentures)				
	Bank A/c	Dr.		2,00,000	
	To 10% Debenture First & Final Call A/c				2,00,000
	(First and final call money received)				

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
1. Shareholders' Funds		
a) Reserve and Surplus	1	50,000
2. Non-current Liabilities		
Long term borrowings	2	5,00,000
Total		5,50,000
II. Assets		
1. Current assets		
a) Cash and cash equivalents		5,50,000

Notes to Accounts

	Particulars	Amount (Rs)
1.	Reserve and surplus Securities Premium Reserve	50,000
2.	Long-term borrowings 5,000, 10% debentures of Rs 100 each	5,00,000

Over Subscription

When the number of debentures applied for is more than the number of debentures offered to the public, the issue is said to be oversubscribed. A company, however, cannot allot more debentures than it has invited for subscription. The excess money received on over subscription may, however, be retained for adjustment towards allotment and the respective calls to be made. But the money received from applicants to whom no debentures have been allotted, will be refunded to them.

Illustration 4

X Limited Issued 10,000, 12% debentures of Rs 100 each payable Rs 40 on application and Rs 60 on allotment. The public applied for 14,000 debentures. Applications for 9,000 debentures were accepted in full; applications for 2,000 debentures were allotted 1,000 debentures and the remaining applications, were rejected. All money was duly received. Journalize the transactions.

Solution:

Books of X Limited

Journal

Date	Particulars		L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Bank A/c	Dr.		5,60,000	
	To 12% Debenture Application A/c				5,60,000
	(Receipt of application money on 14,000 debentures)				
	12% Debenture Application A/c	Dr.		5,60,000	
	To 12% Debentures A/c				4,00,000
	To Debentures Allotment A/c				40,000
	To Bank A/c				1,20,000
	(Debenture Application money transferred to Debenuture A/c, Excess application money credited to Debenture Allotment account and money refunded on rejected application)				
	12% Debenture Allotment A/c	Dr.		6,00,000	
	To 12% Debentures A/c				6,00,000
	(Amount due on allotment on 10,000 debentures)				
	Bank A/c	Dr.		5,60,000	
	To Debenture Allotment A/c				5,60,000
	(Allotment money received)				

Issue of Debentures for Consideration other than Cash

Sometimes a company purchase assets from vendors and instead of making payment in cash issues debentures for consideration thereof. Such issue of debentures is called debentures issued for consideration other than cash. In that case also, the debentures may be issued at par, at a premium or at a discount then entries made in such a situation are similar to those of the shares issued for consideration other than cash, which are as follows :

1. On purchase of assets

Sundry Assets A/c Dr.

To Vendor's

2. On issue of debentures

(a) At par

Vendors Dr.

To Debentures A/c

(b)At premium

Vendors Dr.

To Debentures A/c

To Securities Premium Reserve A/c

(c) At a discount

Vendors Dr.

Discount on Issue of Debenture A/c Dr.

To Debentures A/c

Illustration 5

Aashirward Company Limited purchased assets of the book value of Rs 2,00,000 from another company and agreed to make the payment of purchase consideration by issuing 2,000, 10% debentures of Rs 100 each.

Record the necessary journal entries.

Solution:

Books of Aashirwad Company Limited

Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Sundry Assets A/c Dr. To Vendors (Assets purchased from vendors)		2,00,000	 2,00,000
	Vendors Dr. To 10% Debentures A/c (Allotment of debentures to vendors as purchase consideration)		2,00,000	 2,00,000

Illustration 6

Rai Company purchased assets of the book value of Rs 2,20,000 from another company and agreed to make the payment of purchase consideration by issuing 2,000, 10% debentures of Rs 100 each at a premium of 10%.

Record necessary journal entries.

Solution:

Books of Rai Company Limited
Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Sundry Assets A/c Dr.		2,20,000	
	To Vendors			2,20,000
	(Assets purchased from vendors)			
	Vendors Dr.		2,20,000	
	To 10% Debentures A/c			2,00,000
	To Securities Premium Reserve A/c			20,000
	(Allotment of 2,000 debentures of Rs 100 each at a premium of 10% as purchase consideration)			

Illustration 7

National Packaging Company purchased assets of the value of Rs 1,90,000 from another company and agreed to make the payment of purchase consideration by issuing 2,000, 10% debentures of Rs 100 each at a discount of 5%.

Record necessary journal entries.

Solution:

Books of National Packaging Company
Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Sundry Assets A/c Dr.		1,90,000	
	To Vendors			1,90,000
	(Assets purchased from vendors)			
	Vendors Dr.		1,90,000	
	Discount on Issue of Debenture A/c Dr.		10,000	
	To 10% Debentures A/c			2,00,000
	(Allotment of 2,000 debentures of Rs 100 each at a discount of 5% as purchase consideration)			

Illustration 8

G.S. Rai company purchased assets of the book value of Rs. 99,000 from another firm. It was agreed that purchase consideration be paid by issuing 11% debentures of Rs. 100 each. Assume debentures have been issued.

At par

At discount of 10%, and

At a premium of 10%.

Record necessary journal entries.

Solution:

Books of G.S. Rai Company Limited

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Sundry Assets A/c Dr. To Vendors (Assets purchased from vendors)		99,000	 99,000
In Ist Case	Vendors Dr. To 10% Debentures A/c (Allotment of debentures to vendors as purchase consideration)		99,000	 99,000
In IInd Case	Vendors Dr. Discount on Issue of Debenture A/c Dr. To 10% Debentures A/c (Allotment of 1,100 debenture of Rs 100 issued at discount of 10% to vendor)		99,000 11,000	 1,10,000
In IIIrd Case	Vendors Dr. To 11% Debentures A/c To Securities Premium Reserve A/c (Allotment of 900 debentures of Rs 100 issued at a premium of 10% to the vendors)		99,000	 90,000 9,000

Sometimes a company may purchase the assets as well as takeover its liabilities of another concern. It happens usually in case of purchase of the whole business of the other concern. In such a situation, the purchase consideration will be equal to the value of net assets (Assets - Liabilities) taken over, and if the whole amount of the consideration is paid by issue of debentures, the journal entry will be:

Sundry Assets A/c Dr.

To Sundry Liabilities A/c

To Vendors

(Purchase of the Vendors' business)

Illustration 9

Romi Ltd. acquired assets of Rs. 20 lakh and took over creditors of Rs. 2 lakh from Kapil Enterprises. Romi Ltd., issued 8% debentures of Rs 100 each at par as purchase consideration. Record necessary journal entries in the books of Romi Ltd.

Solution:

Books of Romi Ltd.

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Sundry Assets A/c Dr. To Kapil Enterprises To Sundry Creditors A/c (Purchase of business from Kapil Enterprises)		20,00,000	 18,00,000 2,00,000
	Kapil Enterprises Dr. To 8% Debentures A/c (Issue of 18,000, 8% debentures of Rs 100 each)		18,00,000	 18,00,000

In case of the whole business being taken over if the amount of debentures issued is more than the amount of the net assets taken over, the difference (excess) will be treated as value of goodwill and the same shall also be debited while passing the journal entry for the purchase of vender's business (see Illustration 11). But if it is the other way round, i.e., the value of debentures is less than the value of the net assets taken over the difference will be credited to capital Reserve accounts (See Illustration 12).

Illustration 10

Blue Prints Ltd., purchased building worth Rs.1,50,000, machinery worth Rs.1,40,000 and furniture worth Rs.10,000 from XYZ Co., and took over its liabilities of Rs. 20,000 for a purchase consideration of Rs. 3,15,000. Blue Prints Ltd., paid the purchase consideration by issuing 12% debentures of Rs.100 each at a premium of 5%. Record necessary journal entries.

Solution:

Books of Blue Prints Limited

Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Building A/c	Dr.		1,50,000	
	Plant & Machinery A/c	Dr.		1,40,000	
	Furniture A/c	Dr.		10,000	
	Goodwill A/c [1]	Dr.		35,000	
	To Liabilities (Sundry)				20,000
	To XYZ Co.				3,15,000
	(Purchase of assets and taking over of liabilities of XYZ Co.)				
	XYZ Co.	Dr.		3,15,000	
	To 12% Debentures A/c				3,00,000
	To Securities Premium Reserve A/c				15,000
	(Issue of 3,000 debentures at a premium of 5%)				

Note: 1. Since the purchase consideration is more than net assets taken over, the difference has been debited to goodwill account.

2. No. of debentures issued = $\frac{\text{Purchase Consideration}}{\text{Issue Price of a Debenture}}$

$= \frac{\text{Rs } 3{,}15{,}000}{105} = 3{,}000$

Illustration 11

A Limited took over the assets of Rs. 3,00,000 and liabilities of Rs.10,000 from B & Co. Ltd., for an agreed purchase consideration of Rs. 2,70,000 to be satisfied by issue of 15% debentures of Rs. 100 at 20% premium. Show the journal entries in the journal of A Limited.

Solution:

Books of *A Limited*

Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Sundry Assets A/c Dr.		3,00,000	
	To Sundry Liabilities A/c			10,000
	To B & Co. Ltd.			2,70,000
	To Capital Reserve			20,000
	(Purchased assets and took over liabilities from B Ltd.)			

B & Co. Ltd. Dr. 2,70,000

To 15% Debentures A/c 2,25,000

To Securities Premium Reserve A/c 45,000

(Issue of 2,250 debentures of Rs 100 each at a premium of 20%

Illustration 12

Suvidha Ltd. purchased machinery worth Rs.1,98,000 from Suppliers Ltd. The payment was made by issue of 12% debentures of Rs.100 each.Pass the necessary journal entries for the purchase of machinery and issue of debentures when:

- Debentures are issued at par;
- Debentures are issued at 10% discount; and
- Debentures are issued at 10% premium

Solution:

Books of Suvidha Ltd.

Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Machinery A/c Dr.		1,98,000	
	To Suppliers Ltd.			1,98,000
	(Machinery purchased)			

Case (i)	When debentures are issued at par:			
	Suppliers Ltd. Dr.		1,98,000	
	To 12% Debentures A/c			1,98,000
	(12% Debentures issued to Suppliers Ltd.)			
Case (ii)	When debentures are issued at 10% discount:			
	Suppliers Ltd. Dr.		1,98,000	
	Discount on Issue of Debentures A/c Dr.		22,000	
	To 12% Debentures A/c			2,20,000
	(12% Debentures issued to Suppliers Ltd. at 10% discount)			
Case (iii)	When debentures are issued at 10% premium:			
	Suppliers Ltd. Dr.		1,98,000	
	To 12% Debentures A/c			1,80,000
	Securities Premium Reserve A/c			18,000
	(12% Debentures issued to Suppliers Ltd. at 10% premium)			

Workings:

(a)	(Rs)
Face value of debenture	100
Less: Discount 10%	10
Value at which debenture issued	90

Number of debentures issued in case of 10% discount = $\frac{1,98,000}{90}$

= 2,200 debenture

(b)	(Rs)
Face value of debenture	100
Add: Premium 10%	10
Value at which debenture issued	110

Number of debentures issued in case of 10% premium = $\frac{1,98,000}{110}$

= 1,800 Debentures

Issue of Debentures as a Collateral Security

A collateral security may be defined as a subsidiary or secondary or additional security besides the primary security when a company obtains a loan or overdraft from a bank or any other financial Institution. It may pledge or mortgage some assets as a secured loan against the said loan. But the lending institutions may insist on additional assets as collateral security so that the amount of loan can be realised in full with the help of collateral security in case the amount from the sale of principal security falls short of the loan money. In such situation, the company may issue its own debentures to the lenders in addition to some other assets already pledged. Such an issue of debentures is known as 'Debentures issued as Collateral Security'.

If the company fails to repay the loan along with interest, the lender is free to receive his money from the sale of primary security and if the realisable value of the primary security falls short to cover the entire amount, the lender has the right to invoke the benefit of collateral security whereby debentures may either be presented for redemption or sold in the open market.

Debentures issued as collateral security can be dealt within two ways in the books of the company:

First Method

No entry is made in the books of accounts since no liability is created by such issue. However, on the liability side of the balance sheet, below the item of loan, a note to the effect that it has been secured by issue of debentures as a collateral security is appended. For example, X Company has issued 9%, 10,000 debentures of Rs.100 each for a loan of Rs.10, 00,000 taken from a bank. This fact may be shown in the balance sheet as under:

X Company
Balance Sheet as at ___________

Particulars	*Note No.*	*Amount (Rs)*
I. Equity and Liabilities		
1. Non-current Liabilities		
Long-term borrowings	1	10,00,000

Second Method

The issue of debentures as a collateral security may be recorded by means of journal entry as follows:

Journal Entries

Issue of 10,000, 9% debentures of Rs. 100 each as collateral security for bank loan of Rs. 10,00,000.

Debenture Suspense A/c Dr. 10,00,000
To 9% Debentures A/c 10,00,000

For cancellation of 9% debentures as collateral security on repayment of bank loan.

Debenture Suspense account will appear as a deduction from the debentures in notes to accounts of long-term borrowings.

When loan is repaid the above entry will be cancelled by a reverse entry :

9% Debentures A/c Dr. 10,00,000
To Debenture Suspense A/c 10,00,000

Balance Sheet of X Co. _____________ (Extract)

Particulars	*Note No.*	*Amount (Rs)*
I. Equity and Liabilities 1. Non-current Liabilities Long term borrowings	 1	 10,00,000

Notes to Accounts

Particulars	*(Rs)*	*Amount (Rs)*
1. Long term borrowings Bank loan 10,000, 9% debentures of Rs 100 each Less: Debenture suspense	 10,00,000 10,00,000	10,00,000 —
		10,00,000

Illustration 13

A company took a loan of Rs. 10,00,000 from Punjab National Bank and issued 10% debentures of Rs. 12,00,000 of Rs. 100 each as a collateral security. Explain how you will deal with the issue of debentures in the books of the company

Solution:

First Method:

Balance Sheet (Extract)

Particulars	*Note No.*	*Amount (Rs)*
I. Equity and Liabilities 1. Non-current Liabilities Long-term borrowings	 1	 10,00,000

Notes to Accounts

Particulars	*Amount (Rs)*
1. Long-term borrowings Bank loan	 10,00,000
(Secured by issue of 12,000,	

10% debentures of Rs. 100 each as Collatoral Security	

Second Method:

Journal Entries

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Debenture Suspense A/c Dr.		12,00,000	
	To 10% Debentures A/c			12,00,000
	(12,000 debenture of Rs. 100 each issued as collateral security to P.N.Bank)			

Balance Sheet (Extract)

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
1. Non-current Liabilities		
Long-term borrowings	1	10,00,000

Notes to Accounts

Particulars	(Rs)	Amount (Rs)
1. Long-term borrowings		
Secured Loan from PNB		10,00,000
12,000, 10% debentures of Rs. 100 each	12,00,000	
Less: Debenture Suspense	12,00,000	—
		10,00,000

Terms of Issue of Debentures

When a company issues debentures, it usually mentions the terms on which they will be redeemed on their maturity. Redemption of debentures means discharge of liability on account of debentures by repayment made to the debenture holders. Debentures can be redeemed either at par or at a premium.

Depending upon the terms and conditions of issue and redemption of debentures, the following six situations are commonly found in practice.

- Issued at par and redeemable at par
- Issued at discount and redeemable at par

- Issued at a premium and redeemable at par
- Issued at par and redeemable at a premium
- Issued at a discount and redeemable at a premium
- Issued at a premium and redeemable at a premium

In all the above six cases, the following journal entries will be passed:

Issue at par and redeemable at par

(a) Bank A/c Dr.

To Debenture Application & Allotment A/c (Receipt of application money)

(b) Debenture Application & Allotment A/c Dr.

To Debentures A/c

(Allotment of debentures)

Issue at a discount and redeemable at par

(a) Bank A/c Dr.

To Debenture Application & Allotment A/c (Receipt of application money)

(b) Debenture Application & Allotment A/c Dr.

Discount on Issue of Debentures A/c Dr.

To Debentures A/c

(Allotment of debentures at a discount)

Issue at premium and redemption at par

(a) Bank A/c Dr.

To Debenture Application & Allotment A/c (Receipt of application money)

(b) Debenture Application & Allotment A/c Dr.

To Debentures A/c

To Securities Premium Reserve A/c

(Allotment of debentures at a premium)

Issue at par and redeemable at premium

(a)Bank A/c Dr.

To Debenture Application & Allotment A/c

(Receipt of application money)

(b)Debenture Application & Allotment A/c Dr.

Loss on Issue of Debentures A/c Dr.

(with premium on redemption)

To Debentures A/c

(with nominal value of debenture)

To Premium on Redemption (with premium on redemption) of Debenture A/c

(Allotment of debentures at par and redeemable at a premium)

Issue at discount and redemption at premium

Bank A/c Dr.

To Debenture Application & Allotment A/c

(Receipt of application money)

Debenture Application & Allotment A/c Dr.

Loss on Issue of Debentures A/c Dr. (with discount on issue plus premium on redemption)

To Debentures A/c

(with nominal value of debenture)

To Premium on Redemption (with premium on redemption) of Debentures A/c

(Allotment of debentures at a discount and redeemable at premium)

(d) Issued at a premium and redeemable at premium

Bank A/c Dr.

To Debenture Application & Allotment A/c

(Receipt of application money)

Debenture Application & Allotment A/c Dr.

Loss on Issue of Debentures A/c Dr.

(with premium on redemption)

To Debentures A/c

(with nominal value of debenture)

To Securities Premium Reserve A/c

(with premium on issue)

To Premium on Redemption of

(with premium on redemption) Debentures A/c

Issue at par and redeemable at premium

(a) Bank A/c Dr.

To Debenture Application & Allotment A/c

(Receipt of application money)

(b) Debenture Application & Allotment A/c Dr.

Loss on Issue of Debentures A/c Dr.

(with premium on redemption)

To Debentures A/c (with nominal value of debenture)

To Premium on Redemption (with premium on redemption) of Debenture A/c

(Allotment of debentures at par and redeemable at a premium)

Issue at discount and redemption at premium

Bank A/c Dr.

To Debenture Application & Allotment A/c

(Receipt of application money)

Debenture Application & Allotment A/c Dr.

Loss on Issue of Debentures A/c Dr. (with discount on issue plus premium on redemption)

To Debentures A/c

(with nominal value of debenture)

To Premium on Redemption (with premium on redemption) of Debentures A/c

(Allotment of debentures at a discount and redeemable at premium)

Issued at a premium and redeemable at premium

Bank A/c Dr.

To Debenture Application & Allotment A/c

(Receipt of application money)

Debenture Application & Allotment A/c Dr.

Loss on Issue of Debentures A/c Dr. (with premium on redemption)

To Debentures A/c

(with nominal value of debenture)

To Securities Premium Reserve A/c (with premium on issue)

To Premium on Redemption of (with premium on redemption) Debentures A/c

Issued at a premium and redeemable at premium

Bank A/c Dr.

To Debenture Application & Allotment A/c

(Receipt of application money)

Debenture Application & Allotment A/c Dr.

Loss on Issue of Debentures A/c Dr. (with premium on redemption)

To Debentures A/c

(with nominal value of debenture)

To Securities Premium Reserve A/c

(with premium on issue)

To Premium on Redemption of (with premium on redemption) Debentures A/c

Notes: 1. When debentures are redeemable at a premium, a provision has to be made right at the time of the issue by debiting the amount to 'Loss on Issue of Debentures A/c'. It may be noted that when debentures are issued at a discount and are redeemable at a premium, the amount of discount on issue is also debited to 'Loss on Issue of Debentures'. It may be noted that when the debentures are issued at a discount and are redeemable at par, the amount debited to 'Discount on Issue of Debentures A/c' as usual.

(e) Premium on redemption is a liability of a company payable in future. It is a provision and is shown under the head Non-current liabilities under sub-head 'Long-term Borrowings' until debentures are redeemed.

(f) Loss on issue of debentures is a capital loss and it is to be written-off gradually charged to statement of profit and loss or securities premium account.

Illustration 14

Give Journal entries for the following:

2. Issue of Rs 1,00,000, 9% debentures of Rs 100 each at par and redeemable at par
3. Issue of Rs 1,00,000, 9% debentures of Rs 100 each at premium of 5% but redeemable at par.
4. Issue of Rs 1,00,000, 9% debentures of Rs 100 each at discount of 5% repayable at par.
5. Issue of Rs 1,00,000, 9% debentures of Rs 100 each at par but repayable at a premium of 5%.
6. Issue of Rs 1,00,000, 9% debentures of Rs 100 each at discount of 5% but redeemable at premium of 5%.
7. Issue of Rs 1,00,000, 9% debentures of Rs 100 each at premium of 5% and redeemable at premium of 5%.

Solution:

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
1	Bank A/c Dr. To 9% Debenture Application & Allotment A/c (Debentures Application money received)		1,00,000	 1,00,000

	Debenture Application & Allotment A/c Dr.		1,00,000	
	To 9% Debentures A/c			1,00,000
	(Application money transferred to Debentures Account)			
2	Bank A/c Dr.		1,05,000	
	To 9% Debenture Application & Allotment A/c			1,05,000
	(Debentures application money received)			
	Debenture Application & Allotment A/c Dr.		1,05,000	
	To 9% Debentures A/c			1,00,000
	To Securities Premium Reserve A/c			5,000
	(Debentures application money transferred to Debentures & Securities Premium account)			
3	Bank A/c Dr.		95,000	
	To 9% Debenture Application & Allotment A/c			95,000
	(Debentures application money received)			
	9% Debenture Application & Allotment A/c Dr.		95,000	
	Discount on Issue of Debentures A/c Dr.		5,000	
	To 9% Debentures A/c			1,00,000
	(Debentures application money transferred to Debentures account)			

4	Bank A/c Dr.		1,00,000	
	To 9% Debenture Application & Allotment A/c			1,00,000
	(Debentures Application money received)			
	Debenture Application & Allotment A/c Dr.		1,00,000	
	Loss on Issue of Debentures A/c Dr.		5,000	
	To 9% Debentures A/c			1,00,000
	To Premium on Redemption of Debentures A/c			5,000
	(Debentures Application money transferred to Debentures account)			
5	Bank A/c Dr.		95,000	
	To 9% Debenture Application & Allotment A/c			95,000
	(Debentures Application money received)			
	Debenture Application & Allotment A/c Dr.		95,000	
	Loss on Issue of Debentures A/c Dr.		10,000	
	To 9% Debentures A/c			1,00,000
	To Premium on Redemption of Debentures A/c			5,000
	(Debentures application money transferred			

	to debentures and Premium on debenture account)			
6	Bank A/c Dr. To 9% Debenture Application & Allotment A/c (Debentures Application money received)		1,05,000	1,05,000
	Debenture Application & Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 9% Debenture A/c To Premium on Redemption of Debentures A/c To Securities Premium Reserve A/c (Debenture application money transferred to debentures account)		1,05,000 5,000	1,00,000 5,000 5,000

Illustration 15

You are required to pass the journal entries relating to the issue of the debentures in the books of X Ltd., and show how they would appear in its balance sheet under the following cases:

- 120, 8% debentures of Rs 1,000 each are issued at 5% discount and repayable at par.
- 150, 7% debentures of Rs 1,000 each are issued at 5% discount and repayable at premium of 10%.
- 80, 9% debentures of Rs 1,000 each are issued at 5% premium.
- Another 400, 8% debentures of Rs 100 each are issued as collateral security against a loan of Rs 40,000.

Solution:

Books of X Ltd.

(a) Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Bank A/c Dr. To Debenture Application and Allotment A/c (Debenture application money received)		1,14,000	1,14,000
	Debenture Application and Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 8% Debentures A/c (Debentures application money transferred to Debentures A/c)		1,14,000 6,000	1,20,000

Books of X Ltd.

Balance Sheet as at______________

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
1. Non-current Liabilities		
Long-term borrowings	1	1,20,000
		1,20,000
II. Assets		
1. Non-current assets		
Other non-current assets	2	4,800
2. Current assets		
Cash and cash equivalents	3	1,14,000
Other current assets	4	1,200
		1,20,000

Notes to Accounts

Particulars	Amount (Rs)
1.Long-term borrowings	
120, 8% debentures of Rs 1,000 each	1,20,000
2.Other non-current assets	
Discount on issue of debentures	4,800
3.Cash and cash equivalents	
Cash at bank	1,14,000
4.Other current assets	
Discount on issue of debentures	1,200

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Note: Discount on Issue of Debentures is written-off in 5 years, presuming that debentures are redeemable after 5 years.

(b) Books of X Ltd.
Journal

Date	Particulars		L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Bank A/c	Dr.		1,42,500	
	To Debenture Application and Allotment A/c				
	(Debenture application money received)				1,42,500
	Debenture Application and Allotment A/c	Dr.		1,42,500	
	Loss on Issue of Debentures A/c	Dr.		22,500	
	To 8% Debentures A/c				1,50,000
	To Premium on Redemption of Debenture A/c				15,000
	(Debentures application money transferred to Debentures A/c)				

Books of X Ltd.

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Balance Sheet as at________________

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
1. Non-current Liabilities		
a) Long-term borrowings	1	1,50,000
b) Other long-term liabilities	2	15,000
		1,65,000
II. Assets		
1. Non-current assets		
Other non-current assets	3	18,000
2. Current assets		
a) Cash and cash equivalents	4	1,42,500
b) Other current assets	5	4,500
		1,65,000

Notes to Accounts

Particulars	Amount (Rs)
1. Long-term borrowings	
150, 7% debentures of Rs 1,000 each	1,50,000
2. Other long-term liabilities	
Premium on redemption of debentures	15,000
3. Other non-current assets	
Loss on issue of debentures	18,000
4. Cash and cash equivalents	
Cash at bank	1,42,500
5. Other current assets	
Loss on issue of debentures	4,500

Note: Discount on Issue of Debentures is written-off in 5 years, presuming that debentures are redeemable after 5 years.

(c) Books of X Ltd.

Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Bank A/c Dr.		84,000	
	To Debenture Application and Allotment A/c			84,000
	(Debenture application money received)			
	Debenture Application and Allotment A/c Dr.		84,000	
	To 9% Debentures A/c			80,000
	To Securities Premium Reserve A/c			4,000
	(Debentures application money transferred to Debentures A/c and securities premium reserve A/c)			

X Ltd.

Balance Sheet as at ....

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
1. Shareholder's funds		
Reserves and surplus	1	4,000
2. Non-current Liabilities		
Long-term borrowings	2	80,000
		84,000
II. Assets		
1. Current assets		
Cash and cash equivalents	3	84,000
		84,000

Notes to Accounts

Particulars	Amount (Rs)
1. Reserves and surplus	
Securities premium reserve	4,000
2. Long-term borrowings	
80, 9% debentures of Rs 1,000 each	80,000

Books of X Ltd.

(d) Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Debenture Suspense A/c Dr.		40,000	
	To 8% Debentures A/c			40,000
	(Issue of 400, 8% debentures of Rs 100 each as collateral security against a loan of Rs 40,000)			

X Ltd.

Balance Sheet as at _____________ (Extract)

Particulars	Note No.	Amount (Rs)
I. Equity and Liabilities		
1. Long-term borrowings	1	40,000

Notes to Accounts

Particulars	Amount (Rs)	Amount (Rs)
1. Long-term borrowings		
Bank loan		40,000
400, 8% debentures of Rs 100 each	40,000	
Less: Debentures suspense	40,000	-
		40,000

Excercises

Nena Limited issued 50,000, 10% debentures of Rs 100 each on the basis of the following conditions:

Debentures issued at par and redeemable at par.

Debentures issued at discount @ 5% and redeemable at par.

Debentures issued at premium @ 10% and redeemable at par.

Debentures issued at par and redeemable at premium @ 10%.

Debentures issued at discount of 5% and redeemable at a premium of 10%.

Debentures issued at premium of 6% and redeemable at a premium of 4%.

Record necessary journal entries in the above mentioned cases at the time of issue and redemption of debentures.

(b)Record necessary journal entries in each of the following cases:

27,000, 7% debentures of Rs 100 each issued at par, redeemable at par.

25,000, 7% debentures of Rs 100 each issued at par redeemable at 4% premium.

20,000, 7% debentures of Rs 100 each issued at 5% discount and redeemable at par.

30,000, 7% debentures of Rs 100 each issued at 5% discount and redeemable at 2½ % premium.

35,000, 7% debentures of Rs 100 each issued at 4% premium and redeemable at premium of 5%.

Interest on Debentures

When a company issues debentures, it is under an obligation to pay interest thereon at fixed percentage (half yearly) periodically until debentures are repaid. This percentage is usually as part of the name of debentures like 8% debentures, 10% debentures, etc., and interest payable is calculated at the nominal value of debentures.

Interest on debenture is a charge against the profit of the company and must be paid whether the company has earned any profit or not. According to Income Tax Act, 1961, a company must deduct income tax at a prescribed rate from the interest payable on debentures if it exceeds the prescribed limit. It is called Tax Deducted at Source (TDS) and is to be deposited with the tax authorities. Of course, the debentureholders can adjust this amount against the tax due from them.

Accounting Treatment

The following journal entries are recorded in the books of a company in connection with the interest on debentures:

1. When interest is due

   Debenture Interest A/c Dr.

   To Income Tax payable A/c

   To Debenture holders A/c

   (Amount of interest due on debenture and tax deducted at source)

2. For payment of interest to debenture holders

Debenture holders A/c Dr.

To Bank A/c

(Amount of interest paid to debenture holders)

On transfer debenture Interest Account to statement of Profit and Loss

Statement of Profit and Loss Dr.

To Debenture Interest A/c

(Debenture interest transferred to profit and loss A/c)

On payment of tax deducted at source to the Government

Income Tax Payable A/c Dr.

To Bank A/c

(Payment of tax deducted at source on interest on debentures)

Illustration 16

A Ltd., issued 2,000, 10% debentures of Rs 100 each on April 01, 2016 at a discount of 10% redeemable at a premium of 10%.

Give journal entries relating to the issue of debentures and debenture interest for the period ending March 31, 2017 assuming that interest was paid half yearly on September 30 and March 31 and tax deducted at source is 10%.

Solution:

Book of A Ltd.
Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
2016 Apr. 01	Bank A/c	Dr.		1,80,000	
	To 10% Debenture Application & Allotment A/c				1,80,000
	(Application money received on 2,000, 10% debentures)				
Apr. 01	10% Debentures Application & Allotment A/c	Dr.		1,80,000	
	Loss on Issue of Debenture A/c	Dr.		40,000	

	To 10% Debentures A/c			2,00,000
	To Premium on Redemption of Debentures A/c			20,000
	(Allotment of debentures at a discount of 10% and redeemable at a premium of 10%)			
Sept.30	Debenture Interest A/c Dr.		10,000	
	To Debentureholders A/c			9,000
	To Income Tax Payable A/c			1,000
	(Interest due for 6 months and tax deducted at source)			
	Income Tax payable A/c Dr.		1,000	
	Bank A/c			1000
	(Tax deducted at source paid to the government)			
2017 Sept.	Debentureholders A/c Dr.		9,000	
	To Bank A/c			9,000
	(Payment of interest)			
March 31	Debenture interest A/c Dr.		10,000	
	To Debentureholders A/c			9,000
	To Income Tax Payable A/c			1,000
	(Interest due for 6 months and tax deducted at source)			
March 31	Debenturesholders A/c Dr.		9,000	
	To Bank A/c			9,000
	(Payment of interest)			
March 31	Income Tax Payable A/c Dr.		1,000	
	To Bank A/c			1,000
	(Paid tax deducted at source to the government)			
March 31	Statement of Profit and Loss Dr.		20,000	
	To Debenture Interest A/c			20,000
	(Debenture interest transferred to profit and loss account)			

Exercise

(d) Diwakar enterprises Ltd. Issued 10,00,000, 6% debentures on April 1, 2016. Interest is paid on September 30, 2016 and March 31, 2017.

Record necessary journal entries assuming that income tax is deducted @10% of the amount of interest.

(e) Laser India Ltd. Issued 7,00,000, 8% debentures of Rs 100 each at par. Interest is to be paid on these debentures half-yearly on September 30 and March 31, every year. Record necessary journal entries asuming that income tax is deducted @ 10% of the amount of interest.

Writing-off Discount/Loss on Issue of Debentures

The discount/loss on issue of debentures is a capital loss or a fictitious asset and, therefore, must be written-off during the life time of debentures. The amount of discount/loss on issue of debentures should normally not be written-off in the year of issue itself since the benefit of the debentures would accrue to the company till their redemption. The discount/loss on it is, therefore, treated as capital loss. The discount may be charged to Securities Premium A/c or may be written-off over 3 to 5 years through statement of profit and loss as per guidelines issued by ICAI. In case, however, there are no capital profits or if the capital profits are not adequate, the amount of such discount/loss can be written-off against the revenue profits every year by passing the following journal entry.

Statement of Profit and Loss Dr.

To Discount/Loss on Issue of Debentures A/c

(Discount/loss on issue of debentures written-off)

There are two methods, which can be adopted to write off discount/loss on issue of debentures against the revenue profits. These are as follows.

(viii) Fixed Instalment Method: When the debentures are redeemed at the end of a specified period, the total amount of discount should be written off in equal instalments of fixed amount over that period. For example, if the debentures are to be redeemed after 10 years then out of the total amount of discount of Rs. 1,00,000, Rs. 10,000 will be written-off every year.

(ix) Fluctuating Instalment Method: When debentures are repaid by annual drawings or in instalments, the discount should be written-off in the ratio of debentures outstanding as at the end of each accounting year. The amount of discount, under this method, goes on reducing year. The amount of discount, under this method, goes on reducing every year and so this method may also be known as Reducing Instalment Method.

For example, a company issues Rs. 15,00,000, 9% debentures at a discount of 10% redeemable by annual drawings of Rs. 3,00,000 at the end of each year. The amount of discount to be written-off will be calculated as under:

Year	Amount utilised during the Year	Ratio
First Year	Rs. 15,00,000	5
Second Year	Rs. 12,00,000	4
Third Year	Rs. 9,00,000	3
Fourth Year	Rs. 6,00,000	2
Fifth Year	Rs. 3,00,000	1

Hence, the amount of discount to be written-off every year will be as under :

First Year	Rs. 1,50,000 5/15		=Rs. 50,000
Second Year	Rs. 1,50,000	4/15	=Rs. 40,000
Third Year	Rs. 1,50,000	3/15	=Rs. 30,000
Fourth Year	Rs. 1,50,000	2/15	=Rs. 20,000
Fifth Year	Rs. 1,50,000	1/15	=Rs. 10,000

Exercise

(vii) X Ltd. issued 2,000, 10% debentures of Rs 100 each at a discount of 8% on April, 2014 which are redeemable at par by annual drawings in 4 years commencing from March 31, 2015 as per the following redemption plan:

Ist Draw 10%, 2nd Draw 20%, 3rd Draw 30%, and 4th Draw 40%. Calculate the amount of discount to be written-off each year assuming that X Ltd., follows calendar year as its accounting year.

(viii) Z Ltd. issued 15,00,000, 10% debentures of Rs 50 each at premium of 10% payable as Rs 20 on application and balance on allotment. Debentures are redeemable at par after 6 years All the money due on allotment was called and duly received. Record necessary entries when premium money is included:

in application money

in allotment money

(ix) Z Ltd. issued 5,000, 10% debentures of Rs 100 each at a discount of 10% on 1.4.2014. The debentures are to be redeemed every year by draw of lots - 1,000 debentures to be redeemed every year starting on 31.03.2015. Record the necessary journal entries including the payment of interest and writing off the discount on issue of debentures. The interest is payable on September 30 and March 31. Z Ltd. closes its books of accounts on March 31 every year.

(x) M Ltd. issued 10,000, 8% debentures of Rs 100 each at a premium of 10% on 1.1.2016. It purchased sundry assets of the value of Rs,2,50,000 and took over the liabilities of Rs,60,000 and issued 8% debentures at a discount of 5% to the vendor. On the same date, it took loan from the Bank for Rs 1,00,000 and issued 8% debentures as Collateral Security. Record the relevant journal entries in the books of M Ltd. and prepare the extract of balance sheet on 31.03.2017. Ignore interest.

(xi) On 1.4.2016, Fast Computers Ltd. issued 20,00,000, 6% debentures of Rs 100 each at a discount of 4%, redeemable at a premium of 5% after three years. The amount was payable as follows:

On application Rs 50 per debenture, Balance on allotment,

Record the necessary journal entries for issue of debentures.

(iv) D Ltd. purchased machinery worth Rs 2,00,000 from E Ltd. on 1.4.2016. Rs 50,000 were paid immediately and the balance was paid by issue of Rs 1,60,000, 12% Debentures in D Ltd. Record the necessary journal entries for recording the transactions in the books of D Ltd.

Illustration 17

A Ltd. Company has issued Rs 1,00,000, 9% debentures at a discount of 6%.

These debentures are to be redeemed equally, spread over 5 annual instalments.

Show Discount on issue of debentures account for five years

Solution:

Books of A Ltd.

Discount on Issue of Debentures Account

Dr. *Cr.*

Date	*Particulars*	*Amount (Rs)*	*Date*	*Particulars*	*Amount (Rs)*
Ist year	Debenture	6,000	Ist year	Statement of Profit & Loss Balance c/d	2,000 4,000
		6,000			6,000
IInd year	Balance b/d	4,000	IInd year	Statement of Profit & Loss Balance c/d	1,600 2,400
		4,000			4,000
IIIrd year	Balance b/d	2,400	IIIrd year	Statement of Profit & Loss Balance c/d	1,200 1,200
		2,400			2,400
IVth year	Balance b/d	1,200	IVth year	Statement of Profit & Loss Balance c/d	800 400
		1,200			1,200
Vth year	Balance b/d	400	Vth year	Statement of Profit & Loss	400
		400			400

Workings Notes:

Total discount on the issue of debentures = $1,00,000 \times \frac{6}{100}$ = Rs 6,000

Amount of discount to be written-off is determined as follows:

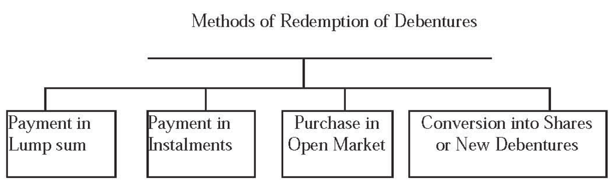
Year	Amount (Rs.)	Ratio	Amount (Rs)
1	1,00,000	5	$\frac{5}{15} \times 6,000 =$ 2,000

2	80,000	4	$\frac{4}{15} \times$ 6,000 =	1,600
3	60,000	3	$\frac{3}{15} \times$ 6,000 =	1,200
4	40,000	2	$\frac{2}{15} \times$ 6,000 =	800
5	20,000	1	$\frac{1}{15} \times$ 6,000 =	400
		15		

Redemption of Debentures

Redemption of debentures refers to extinguishing or discharging the liability on account of debentures in accordance with the terms of issue. In other words redemption of debentures means repayment of the amount of debentures by the company. There are four ways by which the debentures can be redeemed. These are :

a. Payment in lump sum
b. Payment in installments
c. Purchase in the open market
d. By conversion into shares or new debentures



Payment in lump sum : The company redeems the debentures by paying the amount in lump sum to the debentureholders at the maturity thereof as per terms of issue.

Payment in instalments : Under this method, normally redemption of debentures is made in instalments on the specified date during the tenure of the debentures. The total amount of debenture liability is divided by the number of years. It is to note that the actual debentures redeemable are identified by means of drawing the requisite number of lots out of the debentures outstanding for payment.

Purchase in open market: When a company purchases its own debentures for the purposes of cancellation, such an act of purchasing and cancelling the debentures constitutes redemption of debentures by purchase in the open market.

Conversion into shares or new debentures : A company can redeem its debentures by converting them into shares or new class of debentures. If debentureholders find that the offer is beneficial to them, they can exercise their right of converting their debentures into shares or new class of debentures. These new shares or debentures can be issued at par, at a discount or at a premium. It should be noted that only the actual proceeds of debentures are to be taken into account for ascertaining the number of shares to be issued in lieu of the debentures to be converted. If debentures were originally issued at discount, the actual amount realised from them at the time of issue would be used as the basis for computing the actual number of shares to be issued. It may be noted that this method is applicable only to convertible debentures.

The following factors should be taken into consideration by the company at the time of redemption of debentures :

1. Time of redemption of debentures :- Generally, debentures are redeemed on due date but a company may redeem its debentures before maturity date, if its articles provides for such.

   Sources of Redemption of debentures :- A company may source its redemption of debentures either out of capital or out of profits.

3. Out of Capital :- Only those companies which are exempted from creating DRR may redeem debentures out of Capital.
4. Out of Profits :- When any company planning to redeem its debentures purely out of profit, it should transfer 100 percent

of the face value of the redeemable debentures to DRR out of the surplus available for payment of dividend.

5. Out of Capital and Profits :- In case, Company is planning to redeem its debentures by using both the sources partially, it does not transfer 100 percent of face value of outstanding debentures of a particular class to DRR out of the surplus available for payment of dividend.

Redemption by Payment in Lump Sum

When the company pays the whole amount in lump sum, the following journal entries are recorded in the books of the company:

= If debentures are to be redeemed at par

(a) Debentures A/c Dr.

To Debentureholders

(b) Debentureholders Dr.

To Bank A/c

3. If debentures are to be redeemed at premium

(a) Debentures A/c Dr.

Premium on Redemption of Debentures A/c Dr.

To Debenture holders

(b) Debenture holders Dr.

To Bank A/c

Illustration 18

Give the necessary journal entries at the time of redemption of debentures in each of the following cases.

(I) X Ltd. issued 5,000, 9% debentures of Rs 100 each at par and redeemable at par at the end of 5 years out of capital.

(J) X Ltd. issued 1,000, 12% debentures of Rs 100 each at par. These debentures are redeemable at 10% premium at the end of 4 years

(K) X Ltd. issued 12% debentures of the total face value of Rs 1,00,000 at premium of 5% to be redeemed at par at the end of 4 years

(L) X Ltd. issued Rs 1,00,000, 12% debentures at a discount of 5% but redeemable at a premium of 5% at the end of 5 year

Solution:

Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
1.	9% Debentures A/c	Dr.		5,00,000	
	To Debentureholders A/c				5,00,000
	(Amount due on redemption debentures)				
	Debentureholders A/c	Dr.		5,00,000	
	To Bank A/c				5,00,000
	(Payment made to debentureholders)				
2.	12% Debentures A/c	Dr.		1,00,000	
	Premium on Redemption of Debentures A/c	Dr.		10,000	
	To Debentureholders				1,10,000
	(Amount due on redemption of debentures)				
	Debentureholders A/c	Dr.		1,10,000	
	To Bank A/c				1,10,000
	(Payment made to debentureholders)				
3.	12% Debentures A/c	Dr.		1,00,000	
	To Debentureholders A/c				1,00,000
	(Amount due on redemption)				
	Debentureholders A/c	Dr.		1,00,000	
	To Bank A/c				1,00,000
	(Payment made to debentureholders)				
4.	12% Debentures A/c	Dr.		1,00,000	
	Premium on Redemption of Debentures A/c	Dr.		5,000	
	To Debentureholders A/c				1,05,000
	(Amount due on redemption of debentures)				
	Debentureholders A/c	Dr.		1,05,000	
	To Bank A/c				1,05,000
	(Payment made to debentureholders)				

As per the provisions of the Companies Act, 2013, the company must set aside a portion of profits every year and transfer it to Debenture Redemption Reserve for redemption of debentures until the debentures are redeemed. The journal entry recorded for the purpose is as follows :

Where a company has issued debentures, it shall create a Debenture Redemption Reserve for the redemption of such debentures, to which adequate amount shall be credited, from out of its profit every year until such debentures are redeemed.

The amount credited to the Debenture Redemption Reserve shall not be utilised by the company except for the purpose of redemption of debentures.

According to Rule 18(7) of COMPANIES (SHARE CAPITAL AND DEBENTURES) RULES, 2014, the company shall create a Debenture Redemption Reserve for the purpose of redemption of debentures, in accordance with the conditions given below:

The Debenture Redemption Reserve shall be create out of the profits of thecompany available for payment of dividend;

The company shall create Debenture Redemption Reserve (DRR) in accordance with following conditions:

No DRR is required for debentures issued by All India Financial Institutions (AIFIs) regulated by Reserve Bank of India and Banking Companies for both public as well as privately placed debentures.

For NBFCs registered with the RBI and for Housing Finance Companies registered with the National Housing Bank, DRR will be 25% of the value of outstanding debentures issued through public issue as per present SEBI (Issue and Listing of Debt Securities) Regulations, 2008, and no DRR is required in the case of privately placed debentures.

For other companies including manufacturing and infrastructure companies, the adequacy of DRR will be 25% of the value of outstanding debentures issued through public issue as per present SEBI (Issue and Listing of Debt Securities) Regulations, 2008.

25% DRR is required in the case of privately placed debentures by listed companies. For unlisted companies issuing debentures on private placement basis, the DRR will be 25% of the value of outstanding debentures.

Every company required to create Debenture Redemption Reserve shall on or before the 30th day of April in each year, invest or deposit, as the case may be, a sum which shall not be less than fifteen per cent, of the amount of its debentures maturing during the year ending on the 31st day of March of the next year, in any one or more of the following methods, namely :-

Deposits with any scheduled bank, free from any charge or lien;

Securities of the Central Government or of any State Government;

Securities mentioned in sub-clauses (a) to (d) and (ee) of section 20 of the Indian Trusts Act, 1882; Bonds issued by any other company which is notified under sub-clause (f) of section 20 of the Indian Trusts Act, 1882; The amount invested or deposited as above shall not be used for any purpose other than for redemption of debentures maturing during the year referred above:

In case of partly convertible debentures, Debenture Redemption Reserve shall be created in respect of non-convertible portion of debenture issue.

The amount credited to the Debenture Redemption Reserve shall not be utilised by the company except for the purpose of redemption of debentures.

Illustration 19

XYZ Ltd. issued 200, 15% debentures of Rs 100 each on April 01, 2013 at discount of 10% redeemable at premium of 10% out of profits. Give journal entries at the time of issue and redemption of debentures if debentures are to be redeemed in lump sum at the end of 4th year. The directors decided to transfer the minimum amount to Debenture Redemption Reserve on March 31, 2016.

Solution:

Books of XYZ Ltd.
Journal

Date	*Particulars*		*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
2013 April 01	Bank A/c To Debenture Application and Allotment A/c (Application money received on debentures)	Dr.		18,000	18,000
April 01	Debenture Application and Allotment A/c Loss on Issue of Debentures A/c To 15% Debentures A/c To Premium on Redemption of Debentures A/c (Issue of Debentures at 10% discount an redeemable at 10% premium)	Dr. Dr.		18,000 4,000	20,000 2,000
2016 March 31	Balance in Statement of Profit and loss To Debenture Redemption Reserve A/c (Transfer of profits to DRR)	Dr.		5,000	5,000
April 30	Debenture Redemption Investment A/c To Bank A/c (Required amount invested in DRI)	Dr.		3,000	3,000
2017 March 31	Bank A/c To Debenture Redemption Investment (DRI encashed at the time of redemption of debentures)	Dr.		3,000	3,000
March 31	15% Debentures A/c Premium on Redemption of Debentures A/c To Debentureholders A/c (Amount due on redemption)	Dr. Dr.		20,000 2,000	22,000
March 31	Debentureholders A/c To Bank A/c (Amount paid to debentureholders)	Dr.		22,000	22,000
March 31	Debenture Redemption Reserve A/c To General Reserve	Dr.		5,000	5,000

	(Transfer of DRR to General Reserve After redemption of debentures)			

Redemption by Payment in Instalments

When, as per terms of the issue, the debentures are to be redeemed in instalments beginning from a particular year, the actual debentures to be redeemed are selected usually by draw of lots, and the redemption to be made either out of profits or out of capital. The entries will be:

3. If redeemed out of profits

(a) Statement of profit and loss Dr.

To Debenture Redemption Reserve A/c

(b) Debentures A/c Dr.

To Debenture holders

(c) Debenture holders Dr.

To Bank A/c

(a) If redeemed out of capital

(a) Debentures A/c Dr.

To Debenture holders

(b) Debenture holders Dr.

To Bank A/c

Illustration 20

ABC Ltd. issued 3,000, 14% Debentures of Rs 100 each at a discount of 5% on April 1, 2012. Interest on these debentures is payable annually on March 31 each year. The debentures are redeemable at par in three equal instalments at the end of the third, fourth and fifth year. Prepare 14% Debentures Account, Discount on Issue of Debentures Account and Debenture Interest Account in the books of the company.

Solution:

14% Debentures Account

Dr. Cr.

Date	Particulars	J.F.	Amount (Rs)	Date	Particulars	J.F.	Amount (Rs)
2013				2012			
Mar.31	Balance c/d		3,00,000	Apr.01	Debenture Application		2,85,000
					Discount on Issue of Debentures		15,000
			3,00,000				3,00,000
2014				2013			
Mar.31	Balance c/d		3,00,000	Apr.01	Balance b/d		3,00,000
			3,00,000				3,00,000
2015				2014			
Mar.31	Bank A/c		1,00,000	Apr.01	Balance b/d		3,00,000
Mar.31	Balance c/d		2,00,000				
			3,00,000				3,00,000
2016				2015			
Mar.31	Bank A/c		1,00,000	Apr.01	Balance b/d		2,00,000
Mar.31	Balance c/d		1,00,000				
			2,00,000				2,00,000
2017				2016			
Mar.31	Balance c/d		1,00,000	Apr.01	Balance b/d		1,00,000
			1,00,000				1,00,000

Debentures Interest Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2013 Mar.31	Bank		42,000	2013 Mar.31	Statement of Profit and Loss		42,000
2014 Mar.31	Bank		42,000	2014 Mar.31	Statement of Profit and Loss		42,000
2015 Mar.31	Bank		42,000	2015 Mar.31	Statement of Profit and Loss		42,000
2016 Mar.31	Bank		28,000	2016 Mar.31	Statement of Profit and Loss		28,000
2017 Mar.31	Bank		14,000	2017 Mar. 31	Statement of Profit and Loss		14,000

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2012 Apr.01	To 14% debentures A/c		15,000	2013 Mar.31	Statement of Profit and Loss		3,750
				Mar.31	Balance c/d		11,250
			15,000				15,000

2013 Apr.01	Balance b/d		11,250	2014 Mar. 31	Statement of Profit and Loss		3,750
				Mar. 31	Balance c/d		7,500
			11,250				11,250
2014 Apr.01	Balance b/d		7,500	2015 Mar. 31	Statement of Profit and Loss		3,750
				Mar. 31	Balance c/d		3,750
			7,500				7,500
2015 Apr.01	Balance b/d		3,750	2016 Mar. 31	Statement of Profit and Loss		2,500
				Mar. 31	Balance c/d		1,250
			3,750				3,750
2016 Apr.01	Balance b/d		1,250	2017 Mar. 31	Statement of Profit and Loss		1,250
			1,250				1,250

Discount on Issue Debentures Account

Working Notes:

(a)Debenture interest is calculated @ 14% on the amount of debentures outstanding in the beginning of each year. The amount of debentures outstanding on April 1, each year is:

Debenture Outstanding

	Rs
April 2012	3,00,000
April 2013	3,00,000
April 2014	3,00,000
April 2015	2,00,000
April 2016	1,00,000

(a)Discount on Issue of Debentures is written-off in the ratio of the amount of debentures outstanding in the beginning of each year. The ratio is 3:3:3:2:1. So amount of discount to be written-off will be

Year	Rs	Amount Rs
2012	Rs 15,000 × $\frac{3}{12}$	3,750
2013	Rs 15,000 × $\frac{3}{12}$	3,750
2014	Rs 15,000 × $\frac{3}{12}$	3,750
2015	Rs 15,000 × $\frac{2}{12}$	2,500
2016	Rs 15,000 × $\frac{1}{12}$	1,250

Redemption by Purchase in Open Market

When a company purchases its own debentures in the open market for the purpose of immediate cancellation, the purchase and cancellation of such debentures are termed as redemption by purchase in the open market. The advantage of such an option is that a company can redeem the debentures at its convenience whenever it has surplus funds. Secondly, the company can purchase them when they are available in market at a discount.

When the debentures are purchased from the market at a discount and cancelled, the journal entries are recorded as follows :

1. On purchase of own debentures for immediate cancellation

    Debentures A/c Dr.

    To Bank A/c

    To Profit on Redemption of Debentures A/c

2. On transfer of Profit on Redemption

    Profit on Redemption of Debenture A/c Dr.

To Capital Reserve

In case, the debentures are purchased from the market at a price which is above the nominal value of debenture, the excess will be debited to loss on redemption of debentures. The journal entry in that case will be

1. Debentures A/c Dr.

   Loss on Redemption of Debentures A/c Dr.

   To Bank A/c

2. Statement of profit and loss Dr.

   To Loss on Redemption of Debentures A/c

Illustration 21

X Ltd. purchased its own debentures of Rs 100 each of the face value of Rs 20,000 from the open market for cancellation at Rs 92. Record necessary journal entries.

Solution:

Books of X Limited
Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Debentures A/c Dr. To Bank A/c To Profit on Redemption of Debentures A/c (Own debentures purchased at Rs 92 from the market)		20,000	 18,400 1,600
	Profit on Redemption of Debenture A/c Dr. To Capital Reserve (Transfer of profit on cancellation of debentures to capital reserve)		1,600	 1,600

* Alternatively, the following two journal entries may be passed:

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Own Debentures A/c		18,000	
	To Bank A/c			18,000
	(Purchased its own debentures of Rs. 20,000 @ Rs. 92 each)			
	Debentures A/c		20,000	
	To Own Debentures A/c			18,000
	To Profit on Redemption of Debentures A/c			2,000
	(Own debentures purchased being cancelled)			

Illustration 22

X Ltd. decided to redeem 250, 12% debentures of Rs 100 each amounting to Rs 25,000. For this purpose, the company purchased debentures amounting to Rs 20000 in the open market at Rs 98.50 each. Expenses of Rs 100 was incurred on it. The balance of debentures amounting to Rs 5,000 were reedemed by draw of lots. Journalise.

Solution:

Books of X Ltd.

Journal

Date	Particulars	L.F.	Debit Amount (Rs)	Credit Amount (Rs)
	Balance in Statement of profit and loss A/c Dr.		6,250	
	To Debenture Redemption Reserve A/c			6,250
	(Transfer of profits to Debenture Reserve A/c			
	Debenture Redemption Investment A/c Dr.		3,750	
	To Bank A/c			3,750
	(Required amount invested in DRI)			

	Bank A/c Dr. To Debenture Redemption Investment A/c (DRI encashed at the time of redemption of debentures)		3,750	3,750
	12% Debentures A/c Dr. To Bank A/c To Profit on Redemption of Debentures A/c (Purchase of 200 debentures @ Rs. 98.50 plus expenses amounting to Rs. 100.)		20,000	19,800 200
	Profit on Redemption of Debentures A/c Dr. To Capital Reserve (Profit on Redemption transferred to Capital Reserve.)		200	200
	12% Debentures A/c Dr. To Bank A/c (Redemption of Rs. 50 debentures)		5,000	5,000
	Debenture Redemption Reserve A/c Dr. To General Reserve (Balance is DRR transferred to General Reserve on Redemption of Debentures)		6,250	6,250

Illustration 23

On April 01, 2013, a company made an issue of 1,000, 6% debentures of Rs 1,000 each at Rs 960 per debenture. The terms of issue provided for the redemption of 200 debentures every year starting from 31 March 2015 either by purchase or by draw of lot at par at the company's option. Rs 10,000 was written-off as the debenture discount account in years ending on March 31, 2014-15. On 31.03.2015, the company purchased for cancellation debentures of the face value of Rs 80,000 at Rs 950 per debenture and of the face value of Rs 1,20,000 at Rs 900 per debenture.

Journalise the above transaction and show the profit on redemption would be treated.

Solution:

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
2013 Apr. 01	Bank A/c Dr. To 6% Debentures Application & Allotment A/c		9,60,000	9,60,000

	(Debentures application money received)			
Apr. 01	6% Debentures Application & Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To 6% Debentures A/c (Debentures application money transferred to Debentures A/c)		9,60,000 40,000	 10,00,000
2014 Mar. 31	Statement of profit and loss Dr. To Discount on Issue of Debenture A/c (Discount on issue of debentures written-off)		10,000	 10,000
Mar. 31	Balance in Statement of profit and loss Dr. To Debenture Redemption Reserve A/c (Transfer of profits DRR)		2,00,000	 2,00,000
Apr. 30	Debenture Redemption Investment A/c Dr. To Bank A/c (Required amount invested in DRI)		30,000	 30,000
2015 Mar. 31	Bank A/c Dr. To Debenture Redemption Investment A/c (DRI encashed at the time of Redemption of debentures)		30,000	 30,000
Mar. 31	6% Debentures A/c Dr. To Bank A/c To Profit on Redemption of Debenture A/c (Redemption of 80 debentures by purchasing @ Rs 950 per debenture)		80,000	 76,000 4,000
Mar. 31	6% Debentures A/c Dr. To Bank A/c To Profit on Redemption of Debentures A/c (Redemption of 80 debentures @ Rs 900 by purchasing in open market)		1,20,000	 1,08,000 12,000
Mar. 31	Profit on Redemption of Debentures A/c Dr. To Capital Reserve A/c (Transfer of profits on cancellation of debentures of Capital Reserve A/c)		16,000	 16,000
Mar. 31	Statement of profit and loss Dr. To Discount on Issue of Debentures A/c (Discount on debentures written-off)		10,000	 10,000
Mar. 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Debenture Redemption Reserve in r/o debentures redeemed transferred to General Reserve A/c)		50,000	 50,000

Redemption by Conversion

As stated earlier the debentures can also be redeemed by converting them into shares or new debentures. If debentureholders find that the offer is beneficial to them, they will take advantage of this offer. The new shares or debentures may be issued at par, at a discount or at a premium. It may be noted that no Debenture Redemption Reserve is required in case of convertible debentures because no funds are required for redemption.

Illustration 24

Arjun Plastics Limited redeemed 1,000, 15% debentures of Rs 100 each by converting them into equity shares of Rs 10 each at a premium of Rs 2.50 per share. The company also redeemed 500 debentures by utilising Rs 50,000 out of profit. Give the necessary journal entries.

Solution:

Books of Arjun Plastic Limted
Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Statement of Profit and Loss Dr. To Debenture Redemption Reserve A/c (Transfer of profit to Debenture Redemption Reserve)		50,000	 50,000
	Debenture Redemption Investment A/c Dr. To Bank A/c (Required amount invested in DRI)		7,500	 7,500
	15% Debentures A/c Dr. To Debentureholders A/c (Amount due to debentureholders)		1,00,000	 1,00,000
	Debentureholders A/c Dr. To Equity Shares Capital A/c To Securities Premium Reserve A/c (Issue of 800 equity shares at a premium of Rs 2.50 per share)		1,00,000	 80,000 20,000
	Bank A/c Dr. To Debenture Redemption Investment A/c (DRI encashed at the time of redemption of		7,500	 7,500

	debentures)			
	Debenture A/c Dr. To Debentureholders A/c (Amount due to debentureholders)		50,000	50,000
	Debentureholders A/c Dr. To Bank A/c (Payment to debentureholders)		50,000	50,000
	Debenture Redemption Reserve A/c Dr. To General Reserve (Debenture Redemption Reserve transferred to General Reserve on redemption of Debentures)		50,000	50,000

Illustration 25

On April 01, 2013, a company made an issue of 10,000, 9% Debentures of Rs 100 each at Rs. 92 per debenture. The terms of issue provided for the redemption of 2,000 debentures every year starting from the March 31, 2016 either by conversion in to equity shares of Rs 20 each or by draw of lot at per at the company's option. On March 31, 2016, company redemption, 2,000, 9% debentures by converting them into Equity shares of Rs 20 each. Give the necessary Journal entries.

Books of a Company

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
2016 Mar. 31	9% Debentures A/c Dr. To Debentureholders A/c To Statement of Profit & Loss To Discount on Issue of Debentures A/c (Amount due to debentureholders on redemption by conversion)		2,00,000	 1,84,000 9,600 8,400
Mar. 31	Debentureholders A/c Dr. To Equity Share Capital A/c (New equity shares issued to debentureholders)		1,84,000	 1,84,000

Working Notes :-Total Discount on the issue of 10,000 Debentures = $10,00,000 \times \frac{8}{100}$

Rs 80,000

Amount of Discount to be written off is determined as follows :

Year	Amount (Rs)	Ratio	Amount (Rs)
2013-14	10,00,000	5	$80,000 \times \frac{5}{25}$ = 16,000
2014-15	10,00,000	5	$80,000 \times \frac{5}{25}$ = 16,000
2015-16	10,00,000	5	$80,000 \times \frac{5}{25}$ = 16,000
2016-17	8,00,000	4	$80,000 \times \frac{4}{25}$ = 12,800
2017-18	6,00,000	3	$80,000 \times \frac{3}{25}$ = 9,600
2018-19	4,00,000	2	$80,000 \times \frac{2}{25}$ = 6,400
2019-20	20,000	1	$80,000 \times \frac{1}{25}$ = 3,200
		25	80,000

3. Up to March 31, 2016 discount on issue of debentures written off is Rs 48,000 out of total amount of Rs. 80,000.

So, on 2,000 debentures, now converted into shares amount of discount

on issue of debentures written off is =

(2,00,000 ×8) × 48000 = Rs. 9,600

80000

10 0

Remaining amount of discount amounting to Rs. 6,400 (Rs. 16,000 - Rs. 9,600) is not written off till March 31, 2016.

Illustration 26

The balance sheet of XYZ Ltd., disclosed the following information as on March 31, 2015.

15% debentures

Debenture Redemption Fund

Debenture Redemption Fund Investment (10% Govt. Securities)

The contribution to Debenture Redemption Fund was Rs 1,30,800 p.a. for the year 2015-16 and 2016-17. Debentures are due for payment on December 31, 2017. Prepare the above accounts in the books of company assuming that securities were realised on March 31, 2017 for a sum of Rs 13,52,000 and interest on securities on March 31, was immediately invested.

Solution:

Debentures Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2016 Mar.31	Balance c/d		15,00,000	2015 Apr.01	Balance b/d		15,00,000
			15,00,000				15,00,000
2017 Mar.31	Bank		15,00,000	2016 Apr.01	Balance b/d		15,00,000
			15,00,000				15,00,000

Debentures Redemption Fund Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2016				2015			
Mar.31	Balance c/d		14,10,760	Apr.01	Balance b/d		11,63,600
				Mar.31	Interest on DRFI		1,16,360
				Mar.31	Statement of profit and loss		1,30,800
			14,10,760				14,10,760
2017	Debenture			2016			
Mar.31	Redemption Fund Investment		58,760	Apr.01	Balance b/d		14,10,760
					Interest on DRFI		1,41,076
Mar.31	General Reserve		16,23,876	2017	Statement of		1,30,800
				Mar.31	profit and loss		
			16,82,636	Mar.31			16,82,636

Debenture Redemption Fund Investment Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2015				2016			
Apr.01	Balance b/d		11,63,600	Mar.31	Balance c/d		14,10,760
2016	Bank		2,47,160*				
Mar.31			14,10,760				14,10,760
2016				2017			
Apr.01	Balance b/d		14,10,760	Mar.31	Bank		13,52,000
					Debenture Redemption Fund		58,760
			14,10,760				14,10,760

(Interest + Instalment = Rs 1,16,360 + Rs 1,30,800 = Rs 2,47,160)

Illustration 27

LCM Ltd. purchased for cancellation its own 10,00,000, 9% Debentures of Rs 500 each at Rs 480 each. Record necessary journal entries.

Solution:

Books of LCM Ltd.

Journal

Date	*Particulars*	*L.F.*	*Debit Amount (Rs)*	*Credit Amount (Rs)*
	Own Debentures A/c Dr. To Bank A/c (Purchased its own debentures @ Rs 480 each)		48,00,00,000	 48,00,00,000
	9% Debenture A/c Dr. To Own Debenture To Profit on cancellation of debentures A/c (Own debenture purchased being cancelled)		50,00,00,000	 48,00,00,000 2,00,00,000
	Profit on cancellation of debentures A/c Dr. To Capital Reserve (Profits on cancellation of debentures transferred to capital reserve)		2,00,00,000	 2,00,00,000

Illustration 28

The following balances appeared in the books of Madhu Ltd. as on April 01, 2016:

	(Rs)
12% Debentures	1,50,000
Debenture Redemption Fund	1,25,000
Debenture Redemption Fund Investments	1,25,000

The Debenture Redemption Fund Investments were represented by Rs 1,30,000, 9% Govt. Securities.

The annual instalment added to the fund was Rs 20,600. On March 31 2017, the bank balance before the receipt of interest on investments was Rs 40,000. On the date, all the investments were sold at 84% and the debentures were duly redeemed.

Prepare Debentures Account, Debenture Redemption Fund Account, Debenture Redemption Fund Investment Account and Bank Account for 2016-2017. The company closes its books on March 31, every year.

Solution:

Books of Madhu Ltd.

Debenture Redemption Fund Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2017				2016	Balance b/d		1,25,000
Mar.31	Debenture Redemption			April 1	Interest on		
				2017	Debenture Redemption		
	Fund Investment (Loss on Sale)			Mar.31	Fund Investment (9% on Rs 1,30,000)		11,700
Mar.31	General Reserve		15,800				
	(Transfer)		1,41,500	Mar.31	Statement of profit and loss		20,600
			1,57,300				1,57,300

Debenture Redemption Fund Investment Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2016				2017			
April 01	Balance b/d			Mar.31	Bank		1,09,200
					(84% of Rs		
	(Face value				1,30,000)		
	Rs 1,30,000)		1,25,000				15,800
					By Debenture Redemption Fund		
			1,25,000		(Loss on Sale)		1,25,000

Bank Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2017				2017			
Mar.31	Balance b/d		40,000	Mar.31	Debenture		1,50,000
	Interest on D.R.F Investment		11,700	Mar.31	Balance c/d		10,900
Mar.31	Debenture Redemption Fund Investment (Sales Proceeds)		1,09,200				
			1,60,900				1,60,900

12% Debentures Account

Dr. *Cr.*

Date	*Particulars*	*J.F.*	*Amount (Rs)*	*Date*	*Particulars*	*J.F.*	*Amount (Rs)*
2017 Mar.31	Bank A/c		1,50,000	2016 April 30	Balance b/d		1,50,000
			1,50,000				1,50,000

Working Notes :

(a) Interest on Debenture Redemption Fund Investments of 1,30,000 at 9% will be Rs 11,700.

(b) Investments realised at 84%. Hence, the investments of Rs 1,30,000 will realise Rs 1,09,200.

Multiple Choice Questions

1. A debenture holder is entitled to :
   (A) Fixed dividend
   (B) Share in profits
   (C) Voting rights in the company
   (D) Interest at the fixed rate
2. On liquidation of company, principal amount of debentures is returned :
   (A) First of All (B) Last of All
   (C) Before Equity Capital (D) After Equity Capital
3. Which of the following statements is false?
   (A) Debenture is a form of public borrowing.
   (B) It is customary to prefix debentures with the agreed rate of interest.
   (C) Debenture interest is a charge against profits.
   (D) The issue price and redemption value of debentures cannot differ.

4. Which of the following is not a characteristic of Bearer Debentures?
   (A) They are treated as negotiable instruments.
   (B) Their transfer requires a deed of transfer.
   (C) They are transferable by mere delivery.
   (D) The interest on it is paid to the holder irrespective of identity.
5. Which of the following statements is false?
   (A) At maturity, debenture holders get back their money.
   (B) Debentures can be forfeited for non-payment of call money.
   (C) In company's balance sheet, debentures are shown under the head Long term Borrowings.
   (D) Interest on debentures is a charge against profits
6. Which of the following statements is false :
   (A) A Company can issue redeemable debentures.
   (B) A Company can issue debentures with voting rights.
   (C) A Company can issue convertible debentures.
   (D) A Company can buy its own debentures and shares.
7. The Principal amount of debentures will be repaid by the company either at the end of a specified period or by instalments during the life time of the company. Such types of debentures are called :
   (A) Redeemable Debentures
   (B) Irredeemable Debentures
   (C) Convertible Debentures

(D) Bearer Debentures

8. The debentures whose principal amount is not repayable by the company during its life time, but the payment is made only at the time of Liquidation of the company, such debentures are called :
   (A) Bearer Debentures
   (B) Redeemable Debentures

(C) Irredeemable Debentures

(D) Non-Convertible Debentures

9. Debenture Application Account is in the nature of

   (A) Real Account (B) Personal Account

   (C) Nominal Account (D) None of the above

10. Discount on issue of Debentures is in the nature of

    (A) Revenue loss (B) Capital loss

    (C) Deferred Revenue Expenditure (D) None of the above

11. Premium received on issue of debentures may be utilised for

    (A) For writing off discount allowed on issue of shares

    (B) For writing off premium allowed on redemption of debentures

    (C) For writing off preliminary expenses

    (D) For All of the Above

Answers

1d, 2c, 3d, 4b, 5b, 6b, 7a, 8c, 9b, 10b, 11d

Short answer type questions

1. Define debenture
2. What is registered debenture
3. What is bearer debenture
4. Define secured debentures
5. Define convertible debentures
6. Distinguish between bond and debenture

Short essay type questions

1. What are debentures? Explain the need for issuing debentures
2. What are the different kinds of debentures?
3. Distinguish between registered debentures and bearer debentures?
4. Distinguish between convertible debentures and non convertible debentures?.

5. Differentiate between equity share and debentures?.
6. Can the debenture be issued for consideration other than cash? Give the journal entry
7. Explain the meaning and accounting treatment of debentures issued as collateral security?
8. What do you mean by discount on issue of debentures? How would you treat the discount on issue of debentures
9. Explain the treatment of fraction debentures with the help of an example.

References:

1. R.L. Gupta and Radhaswamy, Advanced Accounting, Sultan Chand & Sons,New Delhi.
2. Dr. Goyal V.K., Financial Accounting, Excel Books, New Delhi.

Module IV
CONVERGENCE TO INTERNATIONAL FINANCIAL REPORTING STANDARDS

When different firms use different methods of recording the transactions, comparison becomes difficult. In the absence of a uniform set of rules, there will be a lot of problems. Thus, there is a need for uniform rules and principles. This will make the preparation and presentation of financial statements easy, relevant, reliable, understandable and comparable. This is sought to be achieved by developing accounting standards.

Accounting standards are authoritative standards for financial reporting and are the primary source of generally accepted accounting principles (GAAP). Accounting standards specify how transactions and other events are to be recognized, measured, presented and disclosed in financial statements. The objective of such standards is to provide financial information to investors, lenders, creditors, contributors and others that is useful in making decisions about providing resources to the entity.

Meaning of accounting Standards

An accounting standard is a common set of principles, standards and procedures that define the basis of financial accounting policies and practices. Accounting standards improve the transparency of financial reporting in all countries. In the United States, the Generally Accepted Accounting Principles form the set of accounting standards widely accepted for preparing financial statements. International companies follow the International Financial Reporting Standards, which are set by the International Accounting Standards Board and serve as the guideline for non-U.S. GAAP companies reporting financial statements.

Objectives of Accounting Standards

Accounting is often considered the language of business, as it communicates to others the financial position of the company.

And like every language has certain syntax and grammar rules the same is true here. These rules in the case of accounting are the Accounting Standards (AS). They are the framework of rules and regulations for accounting and reporting in a country. Let us see the main objectives of forming these standards.

1. The main aim is to improve the reliability of financial statements. Now because the financial statements have to be made following the standards the users can rely on them. They know that not conforming to these standards can have serious consequences for the companies.
2. Then there is comparability. Following these standards will allow for inter-firm and intra-firm comparisons. This allows us to check the progress of the firm and its position in the market.
3. It also looks to provide one set of accounting policies that include the necessary disclosure requirements and the valuation methods of various financial transactions.

Benefits of Accounting Standards

Accounting Standards are the ruling authority in the world of accounting. It makes sure that the information provided to potential investors is not misleading in any way. Let us take a look at the benefits of AS.

1] Attains Uniformity in Accounting

Accounting Standards provides rules for standard treatment and recording of transactions. They even have a standard format for financial statements. These are steps in achieving uniformity in accounting methods.

2] Improves Reliability of Financial Statements

There are many stakeholders of a company and they rely on the financial statements for their information. Many of these stakeholders base their decisions on the data provided by these financial statements. Then there are also potential investors who make their investment decisions based on such financial statements.

So it is essential these statements present a true and fair picture of the financial situation of the company. The Accounting Standards (AS) ensure this. They make sure the statements are reliable and trustworthy.

3] Prevents Frauds and Accounting Manipulations

Accounting Standards (AS) lay down the accounting principles and methodologies that all entities must follow. One outcome of this is that the management of an entity cannot manipulate with financial data. Following these standards is not optional, it is compulsory.

So these standards make it difficult for the management to misrepresent any financial information. It even makes it harder for them to commit any frauds.

4] Assists Auditors

Now the accounting standards lay down all the accounting policies, rules, regulations, etc in a written format. These policies have to be followed. So if an auditor checks that the policies have been correctly followed he can be assured that the financial statements are true and fair.

5] Comparability

This is another major objective of accounting standards. Since all entities of the country follow the same set of standards their financial accounts become comparable to some extent. The users of the financial statements can analyze and compare the financial performances of various companies before taking any decisions.

Also, two statements of the same company from different years can be compared. This will show the growth curve of the company to the users.

6] Determining Managerial Accountability

The accounting standards help measure the performance of the management of an entity. It can help measure the management's ability to increase profitability, maintain the solvency of the firm, and other such important financial duties of the management.

Management also must wisely choose their accounting policies. Constant changes in the accounting policies lead to confusion for the user of these financial statements. Also, the principle of consistency and comparability are lost.

Development of accounting standards in india

It is essential that financial statements should reflect true and fair view of financial results of the business enterprise. In practice, different accounting methods are used in the preparation and presentation of the financial statements. "necessity is the mother of invention" is an age old adage. Accordingly, over a period of time, the accounting professionals tried to standardize set of rules and the necessary accounting procedures. This is done with a view to present financial statements in such a way as to achieve uniformity and comparability with the precision and accuracy. Such tireless activities by the accounting professionals resulted in the birth of accounting standards.

Generally accepted accounting principles in india are very lenient in permitting enterprises to adopt the accounting procedure at the discretion of individual entrepreneurs. This has led to the collapse of big corporate enterprises in india. The institute of chartered accountants of india recognized the need to harmonies the diverse accounting policies and practices in use in india. Following the development of international accounting standards, ICAI also took step to develop accounting standards in india. Accordingly, the ICAI constituted the accounting standards board on 21st April 1977.

Accounting Standard Board of India

On 21st April 1977, the Institute of Chartered Accountants of India as the premier accounting body in our country, set up "Accounting Standard Board" (ASB) to harmorize the diverse accounting policies and practice prevalent in our country.

The primary duty of ASB is to formulate the accounting standards for India. These standards may be established by the Council of the Institute in India

Objectives of Accounting Standard Board of india

The following are the objectives of the Accounting Standards Board:

1. To conceive of and suggest areas in which Accounting Standards need to be developed.
2. To formulate Accounting Standards with a view to assisting the Council of the ICAI in evolving and establishing Accounting Standards in India.
3. To examine how far the relevant International Accounting Standard/International Financial Reporting Standard (see paragraph 3 below) can be adapted while formulating the Accounting Standard and to adapt the same.
4. To review, at regular intervals, the Accounting Standards from the point of view of acceptance or changed conditions, and, if necessary, revise the same.
5. To provide, from time to time, interpretations and guidance on Accounting Standards.
6. To carry out such other functions relating to Accounting Standards.

Functions of Accounting Standard Board of india

1. Main function of ASB is to formulate accounting standards.
2. While formulation of standards ASB has to consider applicable laws, customs, social and business environment.
3. ASB has to give due consideration to IAS issued by IASC from time to time to develop own standards in light of conditions and practices being followed in India.
4. ASB has to persuade the accounting professionals and preparers of financial statements to adopt them.
5. ASB has to issue guidance notes on accounting standards.
6. To review all accounting standards from time to time.

Need and importance of global accounting standards

1. Develop of multinational corporations

Multinational and transnational companies have their head offices established in one country, while they operate in different corners of the world. this results in recording of transactions following the standards of the respective country of operation, but they have to be compiled following accounting principles of their parent nation, this has been a complicated task and a major challenge for such multinational corporations.

2. Growth of international capital market

In the present era, organization do not depend only on their domestic country for the purpose of raising their capital. They can even raise capital from the foreign markets. This requires the entities to redraft their financial statements applying the accounting standards of the foreign country/economy.

3. Legislative requirement

It was realized that having a multiplicity of accounting standards around the world is against public interest. Thus, a strong need was felt b the legislation to bring about uniformity, harmonization, rationalization, comparability, transparency, and adaptability in financial statements.

International Accounting Standards Committee (IASC)

The International Accounting Standards Committee (IASC) was formed in 1973 through an agreement made by professional accountancy bodies from Australia, Canada, France, Germany, Japan, Mexico, the Netherlands, the United Kingdom and Ireland, and the United States of America. Additional sponsoring members were added in subsequent years, and in 1982 the sponsoring "members" of the IASC comprised all of the professional accountancy bodies that were members of the International Federation of Accountants (IFAC).

From its formation in 1973 until a comprehensive reorganisation in 2000, the structure for setting International Accounting Standards was known as the International Accounting Standards Committee (IASC).

The International Accounting Standards Committee was essentially the structure, rather than a committee in the traditional sense of a group of people. There was no actual "committee" of that name.

International Accounting Standard Committee has issued certain standards. A list of such standards are given below.

IAS 1 Presentation of Financial Statements

IAS 2 Inventories

IAS 3 Consolidated Financial Statement

IAS 4 Depreciation Accounting

IAS 5 Information to Be Disclosed in Financial Statements

IAS 6 Accounting Responses to Changing Prices

IAS 7 Statement of Cash Flows

IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors

IAS 9 Accounting for Research and Development Activities

IAS 10 Events After the Reporting Period

IAS 11 Construction Contracts

IAS 12 Income Taxes

IAS 13 Presentation of Current Assets and Current Liabilities

IAS 14 Segment Reporting

IAS 15 Information Reflecting the Effects of Changing Prices

IAS 16 Property, Plant and Equipment

IAS 17 Leases

IAS 18 Revenue

IAS 19 Employee Benefits

IAS 20 Accounting for Government Grants and Disclosure of Government Assistance

IAS 21 The Effects of Changes in Foreign Exchange Rates

IAS 22 Business Combinations

IAS 23 Borrowing Costs

IAS 24 Related Party Disclosures

IAS 25 Accounting for Investments

IAS 26 Accounting and Reporting by Retirement Benefit Plans

IAS 27 Consolidated and Separate Financial Statements

IAS 28 Investments in Associates and Joint Ventures

IAS 29 Financial Reporting in Hyperinflationary Economies

IAS 30 Disclosures in the Financial Statements of Banks and Similar Financial Institutions

IAS 31 Interests In Joint Ventures

IAS 32 Financial Instruments: Presentation

IAS 33 Earnings Per Share

IAS 34 Interim Financial Reporting

IAS 35 Discontinuing Operations

IAS 36 Impairment of Assets

IAS 37 Provisions, Contingent Liabilities and Contingent Assets

IAS 38 Intangible Assets

IAS 39 Financial Instruments: Recognition and Measurement

IAS 40 Investment Property

IAS 41 Agriculture

International Accounting Standards Board (IASB)

In March 2001, the International Accounting Standards Committee (IASC) Foundation was formed as a not-for-profit corporation incorporated in the State of Delaware, US. The IASC Foundation is the parent entity of the International Accounting Standards Board, an independent accounting standard-setter based in London, UK.

On April 1, 2001, the International Accounting Standards Board (IASB) assumed accounting standard-setting responsibilities from its predecessor body, the International Accounting Standards Committee. This was the culmination of a restructuring based on the recommendations of the report Recommendations on

Shaping IASC for the Future.

INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

International Financial Reporting Standards (IFRS) is a set of accounting standards developed by an independent, not-for-profit organization called the International Accounting Standards Board (IASB).

The goal of IFRS is to provide a global framework for how public companies prepare and disclose their financial statements. IFRS provides general guidance for the preparation of financial statements, rather than setting rules for industry-specific reporting.

Having an international standard is especially important for large companies that have subsidiaries in different countries. Adopting a single set of world-wide standards will simplify accounting procedures by allowing a company to use one reporting language throughout. A single standard will also provide investors and auditors with a cohesive view of finances.

Features of IFRS

1. These are global accounting standards
2. These are 'principle based' not 'rule based'
3. IFRS are developed and maintained by IASB
4. These are issued with the intention of applying these standards across the globe on a consistent basis
5. They ensure high quality transparent reporting that would ensure comparability among the entities across the globe.
6. Every standard has a specific structure to ensure uniformity and facilitates reading, interpretation, and application.

IFRS Interpretation Committee

The IFRS Interpretations Committee (Interpretations Committee) is the interpretative body of the International Accounting Standards Board (Board). The Interpretations Committee works with the Board in supporting the application of IFRS Standards. The Interpretations Committee responds to questions about the application of the Standards and does other work at the request of the Board. The Interpretations Committee comprises 14 voting members, appointed by the Trustees of the IFRS Foundation. The members provide the best available technical expertise and diversity of international business and market experience relating to the application of IFRS Standards.

Role

The role of the Interpretations Committee is to interpret the application of IFRS Standards to ensure consistent accounting practices throughout the world and to provide timely guidance on financial reporting issues that are not specifically addressed in IFRS Standards, within the context of the Board's Conceptual Framework.

National Financial Reporting Authority (NFRA)

The National Financial Reporting Authority (NFRA) is a body constituted under the provisions of Section 132 of the Companies Act, 2013. The constitution of this authority is effective from 1st October 2018. The aim of the Central Government in this regard appears to be:

- Setting up of a separate and independent regulatory body to assist in the framing and enforcement of legislation relating to accounting & auditing and
- Improving investor and public confidence in the financial reporting of an entity.

Composition of the NFRA

The Companies Act requires the NFRA to have a chairperson who will be appointed by the Central Government and a maximum of 15 members. The appointment of such chairperson and members are subject to the following qualifications:

- They should be having an expertise in accountancy, auditing, finance or law.
- They are required to make a declaration to the Central Government that there is no conflict of interest or lack of independence in their appointment.
- All the members including the chairperson who are in full-time employment should not be associated with any audit firm (including related consultancy firms) during their term of office and 2 years after their term.

Role of the NFRA

The NFRA has the following responsibilities:

- Make recommendations on the foundation and laying down of accounting and auditing policies and standards;
- Monitor and enforce the compliance of the accounting standards and auditing standards:
- Oversee the quality of service of the professionals (such as auditors, CFOs, etc) and suggest measures required for improvement in the quality of service;
- Perform such other functions related to the above.

Prior to the constitution of this authority, the Central Government would prescribe accounting standards on the recommendation of ICAI. The ICAI would prescribe the same only after consulting with the National Advisory Committee on Accounting Standards who will provide their recommendations. The ICAI will now have to consult with the NFRA and examine its recommendations in this regard. Thus the National Advisory Committee on Accounting Standards is effectively replaced by the NFRA.

Scope of the NFRA

As discussed earlier, the NFRA has the power to investigate and also conduct quality reviews for a certain prescribed class of companies. While the draft NFRA Rules have not been prescribed yet, they would include the following class of companies if implemented as it is:

- Companies listed in India
- Unlisted Companies whose:

o Net worth ≥ Rs. 500 crore; or

o Paid up Capital ≥ Rs. 500 crore; or

o Annual turnover ≥ Rs. 1000 crore (As on 31st March of the preceding financial year); OR

o Companies whose securities are listed outside India

The NFRA also holds the power of investigation of a certain class of bodies corporate or persons (auditors) in relation to matters of professional or other misconduct by a member or firm of Chartered Accountants or auditors. In this regard, as per the draft NFRA rules, the auditors or audit firms which conduct the audit of the following category of companies or their branches (including through the network/brand to which it belongs) whether directly or indirectly, are covered:

- Audit of ≥ 200 companies in a year;
- Audit of ≥ 20 listed companies;
- Company or companies (whether listed or not), having:
  - Net Worth ≥ Rs. 500 crores; or
  - Paid up Capital ≥ Rs. 500 crores; or
  - Annual turnover ≥ Rs. 1000 crores;(As on 31st March of the immediately preceding financial year); OR
  - Company or Companies listed outside India
- SIC Interpretations were previously issued by the Standard Interpretations Committee (SIC), and were subsequently endorsed by the International Accounting Standards Board (IASB). The IFRS Interpretations Committee has reissued Interpretations in this series if it considers it necessary.
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Standard Interpretation Committee (SIC)

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Process of Setting IFRS

1. Setting the agenda:

The IASB evaluates the merits of adding a potential item to its agenda by evaluating the following:

i) Considers the relevance to users of the information and the reliability of information that could be provided if a new standard is developed,

ii) The possibility of increasing convergence because of the development of the new standards;

iii) Resource constraints if any in the development process.

2. Planning the project:

After adding the agenda, IASB make an execution plan, where it is being decided that whether the project would be done alone by IASB itself or with the collaboration with someone.

3. Developing and publishing the Discussion Paper, including public consultation:

Although a Discussion Paper is not mandatory, the IASB normally publishes it as its first publication on any major new topic to explain the issue and solicit early comment from constituents.

If the IASB decides to omit this step, it will state why.

Typically, a Discussion Paper includes:

- a comprehensive overview of the issue;
- possible approaches in addressing the issue;
- the preliminary views of its authors or the IASB; and
- an invitation to comment.

4. Developing and publishing the Exposure Draft, including public consultation:

Publication of an Exposure Draft is a mandatory step in due process. Irrespective of whether the IASB has published a Discussion Paper, an Exposure Draft is the IASB's main vehicle for consulting the public.

Unlike a Discussion Paper, an Exposure Draft sets out a specific proposal in the form of a proposed Standard (or amendment to an existing Standard).

The development of an Exposure Draft begins with the IASB considering:

- issues on the basis of staff research and recommendations;
- comments received on any Discussion Paper; and
- suggestions made by the IFRS Advisory Council, Consultative groups and accounting standard-setters, and arising from public education sessions.

After resolving issues at its meetings, the IASB instructs the staff to draft the Exposure Draft.

When the draft has been completed, and the IASB has balloted on it, the IASB publishes it for public comment.

5. Developing and publishing the Standard:

The development of an IFRS is carried out during IASB meetings, when the IASB considers the comments received on the Exposure Draft.

After resolving issues arising from the Exposure Draft, the IASB considers whether it should expose its revised proposals for public comment, for example by publishing a second Exposure Draft.

In considering the need for re-exposure, the IASB:

- identifies substantial issues that emerged during the comment period on the Exposure Draft that it had not previously considered;
- assesses the evidence that it has considered;
- evaluates whether it has sufficiently understood the issues and actively sought the views of constituents; and
- considers whether the various viewpoints were aired in the Exposure Draft and adequately discussed and reviewed in the basis for conclusions.

Drafting the IFRS

The IASB's decision on whether to publish its revised proposals for another round of comments is made in an IASB meeting. If the IASB decides that re-exposure is necessary, the due process to be followed is the same as for the first Exposure Draft.

When the IASB is satisfied that it has reached a conclusion on the issues arising from the Exposure Draft, it instructs the staff to draft the IFRS.

Finally, after the due process is completed, all outstanding issues are resolved, and the IASB members have balloted in favour of publication, the IFRS is issued.

6. Procedures after an IFRS are issued:

After an IFRS is issued, the staff and the IASB members hold regular meetings with interested parties, including other standard-setting bodies, to help understand unanticipated issues related to the practical implementation and potential impact of its proposals.

With the reorganization of International Accounting Standard Committee (IASC) to IFRS Foundation, there has been a change in various nomenclatures that are used. All the standards and interpretation that IASB has issued till 2001 were known as International Accounting Standards (IAS) and SIC respectively whereas, now all the standards and interpretations that are issued by the new body are known as International Financial Reporting Standards (IFRS) and IFRIC respectively.

Conceptual framework of IFRS

Accounting needs a conceptual framework. There is also framework for the preparation and presentation of financial statements.

Meaning of conceptual framework

A framework is the foundation of accounting standards. A conceptual framework acts as a constitution for the standard setting process. concepts are the groundwork, the basis, the foundation upon which the superstructures of standards can be created. Without a conceptual framework, a consistent approach to standard setting cannot be achieved.

Elements of conceptual framework

The elements of a conceptual framework are: objectives, quantitative characteristics of accounting information, elements of financial statements, recognition and measurement, measuring attributes, units of measure, and capital maintenance.

The highlights of the conceptual framework issued by IASB are as follows.

- **Objectives:**

  The objectives of financial statements is 'to provide information about the financial position, performance and changes in financial position of an enterprise that is useful to a wide range of user in making economic decisions'

- **Users**

  Investors, employees, lenders, suppliers, and other traders, customers, governments and their agencies, public, management, and others.

- **Underlying assumptions**

  Accrual basis and going concern.

- **Quantitative characteristics**

  Understandability, relevance, materiality, reliability, faithful representation, substance over form, neutrality, prudence, completeness and comparability.

- **Elements of financial statements**

  Assets, liabilities, equity, income, and expenses

- **Concepts of capital maintenance**

  Both financial and physical concepts of capital have been listed.

FINANCIAL ELEMENTS

Financial elements are the important part of conceptual framework, some elements are directly related to the measurement of the financial position. Other elements are directly related to the measurement of financial performance.

The elements of financial statements are the general groupings of line items contained within the statements. These elements are as follows:

- Assets. These are items of economic benefit that are expected to yield benefits in future periods. Examples are accounts receivable, inventory, and fixed assets.

- Liabilities. These are legally binding obligations payable to another entity or individual. Examples are accounts payable, taxes payable, and wages payable.
- Equity. This is the amount invested in a business by its owners, plus any remaining retained earnings.
- Revenue. This is an increase in assets or decrease in liabilities caused by the provision of services or products to customers. It is a quantification of the gross activity generated by a business. Examples are product sales and service sales.
- Expenses. This is the reduction in value of an asset as it is used to generate revenue. Examples are interest expense, compensation expense, and utilities expense.

Recognition of elements of financial statements (initial recognition)

Recognition is the process of recording an item in the financial statements. A transaction can be recorded in the books of only when it is recognized.

Meaning of recognition

Recognition is the process of incorporating in the statement of financial position or statement of comprehensive income an item that meets the definition of an element and satisfies the criteria for recognition. Elements should be recognized in the financial statement only if

a. It is probable that any future economic benefit associated with the item will flow to or from the entity;
b. The item has a cost or value that can be measured with reliability

Recognition criteria

The general criteria for recognizing elements in financial statements is provided below:

- Assets: An asset is recognized in the balance sheet when it is probable that the future economic benefits will flow to the entity and the asset has a cost or value that can be measured reliably. The economic benefits contribute, directly or indirectly, in the form of cash or cash equivalents. Even though many assets are in physical form, such as machinery, the physical form is not essentials. For example, patents and intellectual property are assets controlled by the entity and have future economic benefits.

- Liabilities: A liability is recognized in the balance sheet when it is
- Probable that an outflow of resources embodying economic benefits will result from the settlement of a present obligation and the amount at which the settlement will take place can be measured reliably. For example, accounts payables are present obligations, which will result in an outflow of resources embodying economic benefits.
- Income: Income is recognized in the income statement when an increase in future economic benefits related to an increase in an asset or a decrease of a liability has arisen that can be measured reliably. In effect, the recognition of income occurs simultaneously with the recognition of increases in assets or decreases in liabilities. For example, when a sale is made, it results in a net increase in assets (cash). Income includes both revenues and gains, such as from sale of assets that are not a part of the normal business activity.
- Expenses: Expenses are recognized when a decrease in future economic benefits related to a decrease in an asset or an increase of a liability has arisen that can be measured reliably. In effect, the recognition of expenses occurs simultaneously with the recognition of an increase in liabilities or a decrease in assets. For example, the depreciation of an asset decreases the asset and the expense is recognized. Expenses include both expenses and losses.

Measurement of the elements of financial statements

Measurement is the process of determining the monetary amounts at which the elements of the financial statements are to be recognized and carried in the balance sheet and income statement. This involves the selection of the particular basis of measurement.

A number of different measurement bases are employed to different degrees and in varying combinations in financial statements. They include the following:

(a) Historical cost. Assets are recorded at the amount of cash or cash equivalents paid or the fair value of the consideration given to acquire them at the time of their acquisition. Liabilities are recorded at the amount of proceeds received in exchange for the obligation, or in some circumstances (for example, income taxes), at the amounts of cash or cash equivalents expected to be paid to satisfy the liability in the normal course of business.

(b) Current cost. Assets are carried at the amount of cash or cash equivalents that would have to be paid if the same or an equivalent asset was acquired currently. Liabilities are carried at the undiscounted amount of cash or cash equivalents that would be required to settle the obligation currently.

(c) Realizable (settlement) value. Assets are carried at the amount of cash or cash equivalents that could currently be obtained by selling the asset in an orderly disposal. Liabilities are carried at their settlement values; that is, the undiscounted amounts of cash or cash equivalents expected to be paid to satisfy the liabilities in the normal course of business.

(d) Present value. Assets are carried at the present discounted value of the future net cash inflows that the item is expected to generate in the normal course of business. Liabilities are carried at the present discounted value of the future net cash outflows that are expected to be required to settle the liabilities in the normal course of business.

The measurement basis most commonly adopted by entities in preparing their financial statements is historical cost. This is usually combined with other measurement bases. For example, inventories are usually carried at the lower of cost and net realizable value, marketable securities may be carried at market value and pension liabilities are carried at their present value.

Fair value

Fair value simply means current market value. It is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction. It is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Thus, fair value is an exit value and transaction costs are not included.

Fair value measurement is good because

a. It provides relevant, reliable, comparable, and understandable measurement of future economic benefits, and

b. Historical cost cannot accurately reflect the value of an asset.

Principles of presentation

1. Fair presentation and compliance with IFRSs

The financial statements must "present fairly" the financial position, financial performance and cash flows of an entity. Fair presentation requires the faithful representation of the effects of transactions, other events, and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework. The application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation. [IAS 1.15]

IAS 1 requires an entity whose financial statements comply with IFRSs to make an explicit and unreserved statement of such compliance in the notes. Financial statements cannot be described as complying with IFRSs unless they comply with all the requirements of IFRSs (which includes International Financial Reporting Standards, International Accounting Standards, IFRIC Interpretations and SIC Interpretations). [IAS 1.16]

Inappropriate accounting policies are not rectified either by disclosure of the accounting policies used or by notes or explanatory material. [IAS 1.18]

IAS 1 acknowledges that, in extremely rare circumstances, management may conclude that compliance with an IFRS requirement would be so misleading that it would conflict with the objective of financial statements set out in the Framework. In such a case, the entity is required to depart from the IFRS requirement, with detailed disclosure of the nature, reasons, and impact of the departure. [IAS 1.19-21]

2. Consistency of presentation

The presentation and classification of items in the financial statements shall be retained from one period to the next unless a change is justified either by a change in circumstances or a requirement of a new IFRS. [IAS 1.45]

3. Materiality and aggregation

Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity. [IAS 1.7]*

Each material class of similar items must be presented separately in the financial statements. Dissimilar items may be aggregated only if they are individually immaterial. [IAS 1.29] However, information should not be obscured by aggregating or by providing immaterial information, materiality considerations apply to the all parts of the financial statements, and even when a standard requires a specific disclosure, materiality considerations do apply. [IAS 1.30A-31]

4. Offsetting

Assets and liabilities, and income and expenses, may not be offset unless required or permitted by an IFRS. [IAS 1.32]

5. Comparative information

IAS 1 requires that comparative information to be disclosed in respect of the previous period for all amounts reported in the financial statements, both on the face of the financial statements and in the notes, unless another Standard requires otherwise. Comparative information is provided for narrative and descriptive where it is relevant to understanding the financial statements of the current period. [IAS 1.38]

6. Statement of financial position (balance sheet)

Current and non-current classification

An entity must normally present a classified statement of financial position, separating current and non-current assets and liabilities, unless presentation based on liquidity provides information that is reliable. [IAS 1.60] In either case, if an asset (liability) category combines amounts that will be received (settled) after 12 months with assets (liabilities) that will be received (settled) within 12 months, note disclosure is required that separates the longer-term amounts from the 12-month amounts. [IAS 1.61]

Current assets are assets that are: [IAS 1.66]

- expected to be realised in the entity's normal operating cycle
- held primarily for the purpose of trading
- expected to be realised within 12 months after the reporting period
- cash and cash equivalents (unless restricted).

All other assets are non-current. [IAS 1.66]

Current liabilities are those: [IAS 1.69]

- expected to be settled within the entity's normal operating cycle
- held for purpose of trading
- due to be settled within 12 months
- for which the entity does not have the right at the end of the reporting period to defer settlement beyond 12 months.

Other liabilities are non-current.

When a long-term debt is expected to be refinanced under an existing loan facility, and the entity has the discretion to do so, the debt is classified as non-current, even if the liability would otherwise be due within 12 months. [IAS 1.73]

If a liability has become payable on demand because an entity has breached an undertaking under a long-term loan agreement on or before the reporting date, the liability is current, even if the lender has agreed, after the reporting date and before the authorisation of the financial statements for issue, not to demand payment as a consequence of the breach. [IAS 1.74] However, the liability is classified as non-current if the lender agreed by the reporting date to provide a period of grace ending at least 12 months after the end of the reporting period, within which the entity can rectify the breach and during which the lender cannot demand immediate repayment. [IAS 1.75]

Settlement by the issue of equity instruments does not impact classification. [IAS 1.76B]

7. Line items

The line items to be included on the face of the statement of financial position are: [IAS 1.54]

(a) property, plant and equipment
(b) investment property
(c) intangible assets
(d) financial assets (excluding amounts shown under (e), (h), and (i))
(e) investments accounted for using the equity method
(f) biological assets
(g) inventories
(h) trade and other receivables
(i) cash and cash equivalents
(j) assets held for sale
(k) trade and other payables
(l) provisions
(m) financial liabilities (excluding amounts shown under (k) and (l))
(n) current tax liabilities and current tax assets, as defined in IAS 12

(o) deferred tax liabilities and deferred tax assets, as defined in IAS 12
(p) liabilities included in disposal groups
(q) non-controlling interests, presented within equity
(r) issued capital and reserves attributable to owners of the parent.

Additional line items, headings and subtotals may be needed to fairly present the entity's financial position. [IAS 1.55]

When an entity presents subtotals, those subtotals shall be comprised of line items made up of amounts recognised and measured in accordance with IFRS; be presented and labelled in a clear and understandable manner; be consistent from period to period; and not be displayed with more prominence than the required subtotals and totals. [IAS 1.55A]*

8. Format of statement

IAS 1 does not prescribe the format of the statement of financial position. Assets can be presented current then non-current, or vice versa, and liabilities and equity can be presented current then non-current then equity, or vice versa. A net asset presentation (assets minus liabilities) is allowed. The long-term financing approach used in UK and elsewhere - fixed assets + current assets - short term payables = long-term debt plus equity - is also acceptable.

9. Statement of profit or loss and other comprehensive income

Concepts of profit or loss and comprehensive income

Profit or loss is defined as "the total of income less expenses, excluding the components of other comprehensive income". Other comprehensive income is defined as comprising "items of income and expense (including reclassification adjustments) that are not recognised in profit or loss as required or permitted by other IFRSs". Total comprehensive income is defined as "the change in equity during a period resulting from transactions and other events, other than those changes resulting from transactions with owners in their capacity as owners". [IAS 1.7]

10. Choice in presentation and basic requirements

An entity has a choice of presenting:

- ✦ a single statement of profit or loss and other comprehensive income, with profit or loss and other comprehensive income presented in two sections,

  or
- ✦ two statements:
  - o a separate statement of profit or loss
  - o a statement of comprehensive income, immediately following the statement of profit or loss and beginning with profit or loss [IAS 1.10A]

The statement(s) must present: [IAS 1.81A]

- ✦ profit or loss
- ✦ total other comprehensive income
- ✦ comprehensive income for the period
- ✦ an allocation of profit or loss and comprehensive income for the period between non-controlling interests and owners of the parent.

11. Profit or loss section or statement

The following minimum line items must be presented in the profit or loss section (or separate statement of profit or loss, if presented): [IAS 1.82-82A]

- ✦ revenue
- ✦ gains and losses from the derecognition of financial assets measured at amortised cost
- ✦ finance costs
- ✦ share of the profit or loss of associates and joint ventures accounted for using the equity method
- ✦ certain gains or losses associated with the reclassification of financial assets
- ✦ tax expense
- ✦ a single amount for the total of discontinued items

Expenses recognised in profit or loss should be analysed either by nature (raw materials, staffing costs, depreciation, etc.) or by function (cost of sales, selling, administrative, etc). [IAS 1.99] If an entity categorises by function, then additional information on the nature of expenses - at a minimum depreciation, amortisation and employee benefits expense - must be disclosed. [IAS 1.104]

12. Other comprehensive income section

The other comprehensive income section is required to present line items which are classified by their nature, and grouped between those items that will or will not be reclassified to profit and loss in subsequent periods. [IAS 1.82A]

An entity's share of OCI of equity-accounted associates and joint ventures is presented in aggregate as single line items based on whether or not it will subsequently be reclassified to profit or loss. [IAS 1.82A]

13. Statement of changes in equity

IAS 1 requires an entity to present a separate statement of changes in equity. The statement must show: [IAS 1.106]

- total comprehensive income for the period, showing separately amounts attributable to owners of the parent and to non-controlling interests
- the effects of any retrospective application of accounting policies or restatements made in accordance with IAS 8, separately for each component of other comprehensive income
- reconciliations between the carrying amounts at the beginning and the end of the period for each component of equity, separately disclosing:

o profit or loss

o other comprehensive income*

o transactions with owners, showing separately contributions by and distributions to owners and changes in ownership interests in subsidiaries that do not result in a loss of control

14. Notes to the financial statements

The notes must: [IAS 1.112]

- present information about the basis of preparation of the financial statements and the specific accounting policies used
- disclose any information required by IFRSs that is not presented elsewhere in the financial statements and
- provide additional information that is not presented elsewhere in the financial statements but is relevant to an understanding of any of them

Notes are presented in a systematic manner and cross-referenced from the face of the financial statements to the relevant note. [IAS 1.113]

IAS 1.114 suggests that the notes should normally be presented in the following order:*

- a statement of compliance with IFRSs
- a summary of significant accounting policies applied, including: [IAS 1.117]
    - o the measurement basis (or bases) used in preparing the financial statements
    - o the other accounting policies used that are relevant to an understanding of the financial statements
- supporting information for items presented on the face of the statement of financial position (balance sheet), statement(s) of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows, in the order in which each statement and each line item is presented
- other disclosures, including:
    - o contingent liabilities (see IAS 37) and unrecognized contractual commitments
    - o non-financial disclosures, such as the entity's financial risk management objectives and policies (see IFRS 7 Financial Instruments: Disclosures)

Principles of disclosures in financial statements

While disclosing financial information in financial statements, certain principles have to be observed.

1. Materiality

According to this convention, only the material or important facts that the business are to be disclosed through the financial statements. All other unimportant or less important information should either be totally ignored or recorded as foot notes, or merged with important items. If it is not done, accounting statement will be unnecessarily overburdened.

2. Summary of accounting policies

Judgments and key assumptions should be disclosed. An entity must disclose, in the summary of significant accounting policies or other notes, the judgments, apart from those involving estimations, that management has made in the process of applying the entity's accounting policies that have the most significant effects on the amounts recognized in the financial statements.

3. Share capital and reserves

Regarding issued share capital and reserves, the following disclosures are required: number of shares authorized, issued and fully paid, and issued but not fully paid par value, a reconciliation of the number of shares outstanding at the beginning and the end of the period, description of rights, preferences, and restrictions treasury shares, including shares held by subsidiaries and associates, shares reserved for issuance under options and contract, a description of the nature and purpose of each reserve within equity.

4. Dividends

In addition to the descriptions information in the statement of changes in equity, the following must be disclosed in the note: the amount of dividends proposed or declared before the financial statements were authorized for issue but which were not recognized as a distribution to owners during the period, and related amount per share, the amount of any cumulative preference dividends not recognized.

5. Capital disclosures:

An entity discloses information about its objectives, policies and processes for managing capital. To comply with this, the disclosure include: quantitative information about the entity's objectives, policies and processes for managing capital, including description of capital it manages, nature of external capital requirement, if any, how it is meeting its objectives, quantitative data about what the entity regards as capital changes from one period to another, whether the entity has complied with any external capital requirements, and if it has not compiled, the consequences of such non compliance.

6. Other information

The following other note disclosures are required by IFRS, if not disclosed elsewhere in information published with the financial statements: domicile and legal form of the entity's country of incorporation, address of registered office or principal place of business, description of the entity operations and principal activities, if it is part of a group, the name of its parent and the ultimate parent of the group, if it is a limited life entity, information regarding the length of the life.

IFRS convergence

The term convergence refers to bringing together two or more things. It is essential since there are accounting diversities. Convergence with IFRSs means "to design and maintain national accounting standards in a way that financial statements prepared accordance with national accounting standards draw unreserved statement of companies with IFRSs.Convergence is harmonization of national GAAP with IFRS through design and maintenance of accounting standards in a way that financial statements are prepared with national accounting standards are in compliance with IFRS.

Benefits of Convergence

1] Beneficial to the Economy

If the accounting standards are converged it will promote international business and increase the influx of capital into the country. This will help India's economy grow and expand. International investing will also mean more capital for domestic companies as well.

2] Beneficial to Investors

Convergence is a boon for investors who wish to invest in foreign markets or economies. It makes it much easier for them to study and compare the financial statements of foreign companies. Since the financial statements are made using the same set of standards it is also easier for the investors to understand and analyze them.

3] Beneficial to the Industry

With globally accepted standards the industry can also surge ahead. So convergence is important for the industry as well. It will allow the industry to lower the cost of foreign capital. If companies are not burned by adopting two different sets of standards it will allow them easier entry into the market.

4] More Transparency

Convergence will benefit the users of the financial statements as well. It will make it easier for them to understand the financial statements. And this will generate better transparency and raise the confidence of the investors to invest funds.

5] Cost Saving

Firstly it will exempt companies from maintaining separate accounting books according to separate standards. This will save a lot of work hours and money for the finance department. And also planning and executing auditing will also become easier.

Indian Accounting Standards (Ind AS)

With respect to IFRS, there are two options before country. One is to adopt IFRS as it is. This is known as IFRS adoption. Second is to converge a country's accounting standards with IFRS. That is, to modify the IFRS slightly according to the rules, laws and environment prevailing in a country.

Standard Setting Process in India

- First, the ASB will identify areas where the formulation of accounting standards may be needed

- Then the ASB will constitute study groups and panels to discuss and study the topic at hand. Such panels will prepare a draft of the standards. The draft normally includes the definition of important terms, the objective of the standard, its scope, measurement principles and the representation of said data in the financial statements.
- The ASB then carries out deliberations of the said draft of the standard. If necessary changes and revisions are made.
- Then this preliminary draft is circulated to all concerned authorities. This will generally include the members of the ICAI, and any other concerned authority like the Department of Company Affairs (DCA), the SEBI, the CBDT, Standing Conference of Public Enterprises (SCPE), Comptroller and Auditor General of India etc. These members and departments are invited to give their comments.
- Then the ASB arranges meetings with these representatives to discuss their views and concerns about the draft and its provisions
- The exposure draft is then finalized and presented to the public for their review and comments
- The comments by the public on the exposure draft will be reviewed. Then a final draft will be prepared for the review and consideration of the ICAI
- The Council of the ICAI will then review and consider the final draft of the standard. If necessary they may suggest a few modifications.
- Finally, the Accounting Standard is issued. In the case of standard for non-corporate entities, the ICAI will issue the standard. And if the relevant subject relates to a corporate entity the Central Government will issue the standard.

Financial Accounting Standards Board (FASB)

The Financial Accounting Standards Board (FASB) is an independent nonprofit organization that is responsible for establishing accounting and financial reporting standards for companies and nonprofit organizations in the United States, following generally accepted accounting principles (GAAP). The FASB was formed in 1973 to succeed the Accounting Principles Board and carry on its mission. It is based in Norwalk, Conn.

The Financial Accounting Standards Board has the authority to establish and interpret generally accepted accounting principles (GAAP) in the United States for public and private companies, as well as for nonprofit organizations. GAAP refers to a set of standards for how companies, nonprofits, and governments should prepare and present their financial statements, including any related party transactions.

The Securities and Exchange Commission (SEC) recognizes the FASB as the accounting standard setter for public companies. It is also recognized by state accounting boards, the American Institute of Certified Public Accountants (AICPA), and other organizations in the field.

The Financial Accounting Standards Board is part of a larger, independent nonprofit group that also includes the Financial Accounting Foundation (FAF), the Financial Accounting Standards Advisory Council (FASAC), the Governmental Accounting Standards Board (GASB), and the Governmental Accounting Standards Advisory Council (GASAC).

Functions of the FASB

The Financial Accounting Standards Board, also called the FASB, is an independent council concerned with accounting principles and standards in the financial sector in the United States. Unlike other similar organizations that work under the guidance of the American government, the FASB operates on its own and serves five key functions.

1. Establish Reporting Standards

One of the most important functions of the Financial Accounting Standards Board is that it is responsible for establishing the reporting standards used by financial professionals. Reporting refers to the detailed reports that accountants make and share with their clients. The FASB ensures that all accountants follow the same standards and that they create reports that those with limited financial experience can understand.

2. Improve Existing Standards

According to the official website of the Financial Accounting Standards Board, it strives to improve the existing standards used by accountants in today's world. The FASB has its own independent agency that is responsible for investigating new methods of reporting and looking at how technology changed the accounting field. That council then comes together and introduces new methods of both accounting and reporting. Accountants may also get help learning how to work with their clients and help following established reporting and practice laws.

3. Ensure Investors Receive Information

Financial accounting often requires that accountants work in large firms and for private and public companies. Those who work for larger corporations are responsible for providing investors with information regarding the profits and losses of that company each year. The Financial Accounting Standards Board ensures that investors receive that necessary information. A recent change that the organization made now gives companies the right to limit the information that they share with investors. This change allows companies to decide whether it should share additional information regarding the testing or early work into a new product. This will most likely relate more to prescription drug companies than traditional manufacturing companies.

4. Establish Accounting Principles

Generally accepted accounting principles are the principles that the U.S. Securities and Exchange Commission uses and mandates that accountants use too. One example is full disclosure principle, which gives a company the right to inform investors and the general public about all the costs that it incurs and spends every year. Constraints and assumptions are two other examples of accounting principles used today. The FASB both establishes new accounting principles and ensures that financial accountants follow all existing principles.

5. Ensure an Understanding of Principles

One of the lesser known functions of the Financial Accounting Standards Board is that it is responsible for ensuring that accountants working in the financial sector have a basic understanding of these principles. Though accountants must go through a minimum of four years of schooling that teaches them about assumptions and other principles, they may find themselves losing some of that knowledge after going to work in the field. The FASB ensures that they carry those principles with them and that they have an understanding of how to use each one while working with clients.

General differences between IFRS and Ind- AS

The differences between IFRS and Indian Accounting standards are wide and very deep routed. The following are the key differences.

1. IFRS is based on fair value concept. But, Indian accounting standards are based on historical cost.
2. Financial statements under IFRS and Indian accounting standard differ in form and substance.
3. Under IFRS, past errors are incorporated in the accounts of the years it pertains to, even if audited and adopted y shareholders. But, these are treated as adjustments in the current year under Indian accounting standards.
4. Depreciation on revalued assets needs to be routed through income statements under IFRS. But Indian accounting standards disallow such a treatment.
5. Certain Indian accounting standards offer accounting policy choices, these are not available under IFRS, Eg, use of pooling of interest method in accounting for amalgamation.
6. Indian accounting standards define assets by classes which can be depreciated at given rates, whereas IFRS promotes the concept of components of fixed assets based on their usefulness.

7. Under IFRS, prior period items will be given retrospective effect in opening equity. Under Ind as, it is not so.
8. Proposed dividend is not required to be reflected in financial statements under IFRS. But this is required to be reflected in financial statements under ind AS.
9. Under IFRS, provision made for dismantling of asset or for site closure can be capitalized. But under Ind AS, this cannot be capitalized.
10. Under IFRS, EPS has to be disclosed separately for continuing and discontinuing operations. This is not required under Ind AS.
11. The terminologies used in IFRS and Ind AS are different. For example, instead of statement of comprehensive income under IFRS, the term statement of profit or loss is used in Ind AS. Similarly in place of statement of financial position under IFRS, the term Balancesheet is used in ind AS.
12. Under IFRS/AS, profit or loss is ascertained by preparing either statement of profit and loss and other comprehensive income.

Standard-wise Difference between IFRS/IAS and Ind AS

Significant differences between IFRS/IAS-1 and Ind AS-1

1. With regard to preparation of statement of profit and loss, IFRS/IAS I provides an option either to follow the single statement approach or to follow the two statement approach. But Ind AS-1 allows only the single statement approach.
2. Another difference lies in the terminology used. For example, in Ind As-1,the term? Balancesheet"is used, while in IFRS/ IAS-1,the term
3. "Statement of Financial Position" is used. Similarly, in Ind As-1,the term "Statement of Profit and Loss" is used, but in IFRS/ IAS-1,the term "Statement of Profit and Loss and Other Comprehensive Income" is used.
4. IFRS/IAS-1 gives the option to individual entities to follow different terminology for the titles of financial statement. On

the other hand, Ind AS-1 gives only one terminology to be used by all entities.

Significant difference between IFRS/IAS-2 and Ind AS -2

No significant difference.

Significant difference between IFRS/IAS-7 and Ind AS 7

1. In case of other tan financial entities, IFRS/IAS 7 gives an option to classify the interest paid and interest and dividends received as items of operating cash flows. Ind-AS 7 does not provide such an option. It requires these items to be classified as item of financing activity and investing activity respectively.
2. IFRS/AS 7 gives an option to classify dividend paid as an item of operating activity. However, Ind AS 7 requires to it to be classified as a part of financing activity only.
3. IFRS/AS 7 does not require disclosure of extraordinary items, as there is no concept of extra ordinary item, whereas ind AS 3 requires so.
4. Ind AS 7 does not make explicit distinction between bank borrowings and bank overdraft. Whereas IFRS/IAS 7 makes so.

Significant difference between IFRS/IAS 10 Ind AS 10

There is no significant difference

Significant difference between IFRS/IAS 10 and Ind /AS 10

1. Proposed dividend after balance sheet date but before the date of the financial statement is non-adjusting event under IFRS/IAS 10. However, as per Ind AS 10, the proposed dividend is shown in the balance sheet and thus treated as adjusting event.
2. As per IFRS/IAS 10, an entity shall disclose the date when the financial statement were authorized for issue and who gave the authorization. If the entity's owners or others have the power to amend the financial statements after issue, the entity shall disclose that fact. But there is no such requirements in Ind AS 10.

Significant difference between IFRS/IAS 11 and Ind AS 11

There is no significant difference. The only difference is that IFRS/IAS 11 does not deal with accounting for construction contracts in respect of real estate developers. However, this has been dealt with as per Ind AS 11.

Significant difference between IFRS/AS 12 and Ind AS 12

1. IFRS/AS 12 is based on the balance sheet liability method where as ind AS 12 is based on income statement liability method. The income statement liability method focuses on timing differences, while the balance sheet liability method focuses on temporary differences.
2. As per Ind AS 12, deferred tax assets to be recognized to the extent there is a reasonable or virtual certainty whereas as per IFRS/IAS 12 , Deferred tax asset is recognized to the extent that it is probable that the enterprise will have sufficient taxable profit.
3. Ind AS 12 does not require numerical reconciliation between tax expenses and pre tax accounting profit. But IFRS/IAS 12 requires numerical reconciliation between tax expenses and pre tax accounting profit.
4. As per Ind AS 12 deferred tax assets and liabilities should be disclosed separately from current assets and current liability, whereas in IFRS/AS 12, deferred tax assets and liabilities are treated as non-current.

Significant difference between IFRS/AS 16 and AS 16

There is no significant difference

Significant difference between IFRS/AS 17 and Ind AS 17

1. Ind AS-17 is not applicable to lease agreement to use land, while IFRS/IAS-17 is applicable to lease agreement to use land.
2. There is difference between Ind AS17 and IFRS/IAS-17 regarding accounting treatment of sale and lease back transactions.

Significant Difference between IFRS/IAS-18 and Ind AS-18

1. Under IFRS/IAS-18,the revenue recognition from rendering of services is done on the basis of percentage of completion method, whereas in Ind AS-18,revenue from rendering of services can be recognised on proportionate completion method or completed services method.
2. IFRS/IAS-18 contains the provisions for revenue swaps. However, there are no such corresponding provisions in Ind AS-9.
3. Under IFRS/IAS-18, revenue is recognised at fair value. However, under Ind AS-18, revenue is recognised at invoice value.

Significant Difference between IFRS/IAS-19 and ind AS-19

1. There is no difference between Ind AS 19 and IFRS/IAS-19,except according to Ind AS- 19,the rate to be used to discount post employment benefit obligation shall be determined by reference to the market yields on government bonds at the balance sheet date, whereas under IFRS/IAS-19,the government bonds can be used only where there is no deep market of high quality corporate bonds.

Significant Difference++ between IFRS/IAS-20 and ind AS-20

1. Ind AS-20 does not state about fair value measurement of non-monetary grants, but Fs/TAS 20 talks about non-monetary grants at fair value at the time of initial recognition.
2. Grant in the nature of promoter contribution is credited to capital reserve as per ind AS-20. However, as per IFRS/IAS-20, such grant should be treated as deferred income.
3. Then it should be allocated over the period under which condition attached to grant is fulfilled on a systematic basis.
4. Refund of grant is treated as extra ordinary items as per Ind AS-20, whereas in IFRS/IAS-20, it is treated as change in estimate.

Significant Difference between IFRS/IAS-21 and Ind AS-21

1. IFRS/IAS-21 uses the words 'functional currency', 'presentation currency', and 'recording currency', but Ind AS-21 only use terminology of 'reporting currency',
2. Ind AS-21 covers the forward contract/hedging, while IAS/IFRS 21 does not cover it. This is covered in IFRS/IAS-39- "Financial instrument- recognition and measurement".
3. IFRS/IAS-21 recognises all the exchange differences as an expense in Profit and Loss Account. However, Ind AS-21 gives the option of amortization/capitalization of exchange difference arising on reporting of long term foreign currency monetary items.

Multiple Choice Questions

1. GAAP stands for
   a. Generally accepted accounting principles
   b. Globally accepted accounting practice
   c. Generally allowable accounting principles
   d. Generally allowable accounting practices
2. The global key professional accounting body is ----------
   a. The international accounting standards board
   b. The institute of chartered accountants of india
   c. The financial accounting standard board
   d. The international accounting standards committee
3. The original cost at which an asset or liability is acquired is known as --------
   a. Amortization b.Replacement cost
   c. Historical cost d.Carrying cost
4. The international accounting standard Committee was set up in --------
   a. 1982 b.1976 c.1967 d.2009
5. The process of converting foreign subsidiary financial

statements into the home currency is known as -------

a. Transmission b.Translation

c. Consolidation d.Reconstruction

6. Accounting in india is governed by the -----
   a. Income tax department
   b. Company law board
   c. Institute of chartered accountants of india
   d. Reserve bank of india
7. Interim dividend paid is always shown
   a. In P/L Appropriation A/c
   b. On the asset side of the B/S
   c. On the liability side of the B/S
   d. None of these.
8. Unclaimed dividend is shown in the B/S under the head
   a. Current liability b.Unsecured loan
   c. Reserve and surplus d.Provisions
9. Advance payment of tax is in the nature of
   a. Capital expenditure b.Prepaid expenses
   c. Outstanding expenses d.Revenue expenditure
10. Debentures are shown in the B/S under head.
    a. Current assets, loans and advances b.Investment
    c. Non current liabilities d.Unsecured loan
11. Preliminary expenses is an example of
    a. Fixed asset b.Current asset
    c. Investment d.Fictitious asset

Answers

1a, 2a, 3c, 4c, 5b, 6c, 7a, 8a, 9b, 10c, 11d

Short answer type questions

1. Define accounting standards
2. What are international accounting standard?
3. What are the main functions of IASB?
4. Define IFRS

5. What is IFRS adoption?
6. What is IFRS convergence?
7. What are Ind Ass?
8. Define financial elements
9. Define the term equity
10. Define the term expenses

Short essay type questions

1. Define accounting standards. What are the objectives of accounting standards?
2. What are the advantages and disadvantages of accounting standards?
3. Write a note on the development of accounting standards in india
4. What are the objectives and functions of ASB?
5. What are the objectives of IASB?
6. Discuss the role of IASB in developing IFRS
7. What are the functions of FASB?
8. What are the role of FASB in developing accounting standards and GAAPs?
9. Define IFRS. What are the features of IFRSs?
10. What is the need for IFRS convergence?
11. What are the benefits of IFRS convergence?
12. State the IFRS implementation plan in india.
13. State the differences between IFRS and Indian accounting standards.
14. Name the companies required to adopt Ind AS
15. Define financial elements. Define the various financial elements as per IASB framework.

Reference:

1. Ashok Sehgal and Deepak Sehgal, Advanced Accounting, VolumeI,Taxmann, New Delhi.
2. Jain and Narang, Financial Accounting, Kalyani Publishers.

MODULE V
Ind. AS/IFRS COMPILED FINANCIAL STATEMENTS OF COMPANIES (Ind AS1)

A company like any other organiastion, must prepare its final accounts annually. Preparation of final accounts of a company is compulsory under Section 128 of the companies act 2013. Financial statements are accounts or statements prepared at the end of the accounting period.

A financial statement compilation is a service to assist the management of a business in presenting its statements. Like any other organization, a company must prepare its final accounts annually. Preparation of final accounts of company is compulsory under Section 128 of the Companies Act, 2013. Financial Statements are accounts prepared at the end of an accounting period.

Financial Statements are set of documents representing the state of affairs of a company to the external users. Different components of the statements are interrelated and should be interpreted in totality to understand financial performance of an enterprises. The component parts of the financial statements are interrelated because they reflect different aspects of the same transactions or other events. Although each statement provides information that is different from others, none is likely to serve only a single purpose nor to provide all the information necessary for particular needs of user.

As per section 2(40) of the Companies Act 2013, financial statements of a company includes

a) A balance sheet as at the end of the financial year.
b) A profit and loss account, or in case of a company carrying on any activity not for profit, an income and expenditure account for the financial year,
c) Cash flow statement for the financial year
d) A statement of changes in equality, if applicable

e) Any explanatory note annexed to, or forming part of any document referred to in sub clause (a) to sub clause (d)

To ensure standardized presentation for easy comparability, the format of the Balance Sheet and the Statement of Profit and Loss has been prescribed in the Schedule 128 of the Companies Act, 2013. Additionally, Ind AS 1 lays down the basic requirements for the presentation of financial statements.

As per Ind AS, a complete set of financial statements comprises the following:

a) A balance sheet
b) A statement of profit and loss
c) A statement of changes in equity
d) A statement of cash flows
e) Notes comprising significant accounting policies and other explanatory information

Key requirements for presentation of financial statements

Ind AS 1 also lays down some key requirements to be followed for presenting information in financial statements. They are:

1. Going Concern: Financial statements are prepared on a going concern basis. Management has to assess the entity's ability to continue as a going concern,
2. Accrual Basis of Accounting: Financial statements, except cash flow statement, are required to be prepared using accrual basis of accounting.
3. Materiality: Each material class of similar items must be presented separately and same has to be followed for the items of dissimilar nature or function. If a line item is not individually material, it is aggregated with other items either in those statements or in the Notes.
4. Offsetting: Assets and liabilities or income and expenses are required to be shown on gross basis without offsetting against each other, unless required or permitted by an Ind AS.
5. Frequency Reporting: Financial statements must be

presented annually. If the entity changes its accounting period, then financial statements are prepared for a period longer or shorter than one year.

6. Comparative Information: Comparative information in respect of the preceding accounting period for all amounts presented in the current year's financial statements shall be given foe better analysis.
7. Consistency: Presentation and classification of items in the financial statements from period to period shall be consistently followed. However, if an Ind AS requires a change in presentation or another presentation or classification is considered to be more appropriate, the classification and presentation may be changed.
8. True and Fair: Financial statements shall present information which is relevant, reliable, comparable and understandable.

SCHEDULE III OF COMPANIES ACT 2013

Schedule III of Companies Act, 2013, is applicable for financial year commencing on or after 1st April, 2014. [Earlier, Revised Schedule IV was applicable w.e.f 1st April, 2011 as per notification dated 30th March 2011 and it was same as Schedule III.]

All companies whether private or public, whether listed or unlisted, and irrespective of their size in terms of turnover, assets, etc. will have to adhere to new format of financial statements from 2011-12 onwards.

SALIENT FEATURES OF SCHEDULE III

General instructions for preparation of Balance Sheet and statement of Profit and Loss of a company.

i. Schedule III gives a priority status to other requirements of Companies Act 2013 and Accounting standards over the Schedule itself.
ii. Disclosure requirements of the schedule are in addition to and not in substitution of disclosure requirements of Accounting Standards.
iii. Additional information/narrative descriptions about various

items of Balance Sheet and statement of Profit and Loss hall be provided in cross referenced Notes to Accounts.

iv. New norms of rounding off have been introduced.

v. Figures of immediately preceding year are to be provided except for companies preparing first set of financial statements.

vi. Terms used in the schedule hall be as per Accounting Standards.

STATEMENT OF FINANCIAL POSITION (SOFP) OR BALANCE SHEET

The statement of financial position, often called the balance sheet, is a financial statement that reports the assets, liabilities, and equity of a company on a given date. In other words, it lists the resources, obligations, and ownership details of a company on a specific day. When reading a balance sheet, it represents what the business owns and controls (the Assets), what it owes (the Liabilities) and the investment that the owner has contributed (the Equity) at a particular point in time. Theaccounting equation is:

Assets = Liabilities + Equity

General Instructions for Preparation of Financial Statements of a Company required to Comply with Ind AS

1. Every company to which Indian Accounting Standardsapply, shall prepare its financial statements in accordance with this Schedule III of the Companies Act, 2013, or with such modifications as may be required under certain circumstances.
2. Where compliance with the requirements of the Act including Indian Accounting Standards (except the option of presenting assets and liabilities in the order of liquidity as provided by the relevant Ind AS) as applicable to the companies require any change in treatment or disclose including addition, amendment, substitution or deletion in the head or sub-head or any changes inter se, in the financial statements or statements forming part thereof, the same shall

be made and the requirements under this Schedule shall stand modified accordingly.

3. The disclosure requirements specified in this Schedule are in addition to and not in substitution of the disclosure requirements specified in the Indian Accounting Standards. Additional disclosures specified in the Indian Accounting Standards shall be made in the Notes or by way of additional statements or statements unless required to be disclosed on the face of the Financial Statements. Similarly, all other disclosures as required by the Companies Act, 2013 shall be made in the Notes in addition to the requirements set out of this Schedule.

4. (i) Notes shall contain information in addition to that presented in the Financial Statements and shall provide where required -

(a) Narrative descriptions or disaggregation of items recognized in those statements and

(b) Information about items that do not qualify for recognition in those statements.

(ii) Each item on the face of the Balance Sheet, Statement of Changes in Equity and Statement of Profit and Loss shall be cross - referenced to any related information in the Notes. In preparing the Financial Statements including the Notes, a balance shall be maintained between providing excessive detail that may not assist users of Financial Statements and not providing important information as a result of too much aggregation.

5. Depending upon the turnover of the company, the figures appearing in the financial Statements shall be rounded off as below:

Turnover	Rounding Off
(i) less than one hundred crore rupees or millions, decimals thereof.	To the nearest hundreds, thousands, lakhs.
(ii) one hundred crore rupees or more decimals thereof.	To the nearest, lakhs, millions or crores

Once a unit measurement is used, it should be used uniformly in the Financial Statements.

6. FinancialStatements shall contain the corresponding amounts (comparatives) for the immediately preceding reporting period for all items shown in the FinancialStatements including Notes except in the case of first Financial Statements laid before the company after incorporation.
7. Financial Statements shall disclose all 'material' items i.e., the items if they could individually or collectively, influence the economic decisions that users make on the basis of the financial statements. Materiality depends on the size or nature of the item or a combination of both, to be judged in the particular circumstances.
8. For the purpose of this Schedule, the terms used herein shall have the same meanings assigned to them in Indian Accounting Standards.
9. Where any Act or Regulation requires specific disclosures to be made in the standalone financial statements of a company, the said disclosures shall be made in addition to those required under this Schedule.

FORMAT OF BALANCE SHEET (Table 1)

Name of the Company…………………

Balance Sheet as at……………

PARTICULARS	NOTE No.	FIGURES AS AT THE END OF CURRENT YEAR	FIGURES AS AT THE END OF PREVIOUS YEAR
I ASSETS			
(1) Non-current Assets			
a) Property, Plant and Equipment			
b) Capital work-in-progress			
c) Investment property			
d) Goodwill			
e) Other tangible assets			
f) Intangible assets under development			
g) Biological assets other than bearer plants			
h) Financial assets			
i. Investments			
ii. Trade receivables			
iii. Loans			

iv. Others (to be specified) i) Deferred tax assets (net) j) Other non-current assets **(2) Current Assets** a) Inventories b) Financial Assets i. Investments ii. Trade receivables iii. Cash and cash equivalents iv. Bank balance other than (iii) above v. Loans vi. Others (to be specified) c) Current tax asset (Net) d) Other current assets **Total Assets** EQUITY AND LIABILITIES II EQUITY a) Equity Share Capital b) Other Equity III LIABILITIES **(1) Non-current liabilities** (a)Financial liabilities i. Borrowings ii. Trade payables iii. Other financial liabilities (other than those specified in item (b), to be specified) (b) Provisions (c) Deferred tax liabilities (Net) (d) Other non-current liabilities **(2) Current Liabilities** (a) Financial liabilities i. Borrowings ii. Trade Payables iii. Other financial liabilities (other than those specified in item (c)) (b) Other current liabilities (c) Provisions (d) Current Tax Liabilities (Net) **Total Equity and Liabilities**			

Note: The upper half of the Balance Sheet is referred to as Assets and the later half is shown as Equity and Liabilities. Alternatively, first Equity and Liabilities can be shown and then Assets can be shown.

GENERAL INSTRUCTIONS FOR PREPARATION OF BALANCE SHEET

1. An asset shall be classified as current when it satisfies any of the following criteria

a) It is expected to be realized in or is intended for sale or consumption in, the company's normal operating cycle.

b) It is held primarily for the purpose of being traded.

c) It is expected to be realized within twelve months after the reporting date, or

d) It is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

All other assets shall be classified as noon - current.

2. An operating cycle is the time between the acquisition of assets for processing and then realization in cash or cash equivalents. Where the normal operating cycle cannot be identified it is assumed to have a duration of 12 months.

3. A liability shall be classified as current when it satisfies any of the following criteria

a) It is expected to be settled in the company's normal operating cycle.

b) It is held primarily for the purpose of being traded

c) It is due to be settled within twelve months after the reporting date, or

d) The company does not have an unconditional right to defer settlement of liability for at least twelve months after the reporting date. Terms of a liability that could at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect the classification.

All other liabilities shall be classified as non - current.

4. A receivable shall be classified as a trade receivable if it is in respect of the amount due on account of goods sold or services rendered in the normal course of business.

5. A payable shall be classified as a trade payable if it is in respect of the amount due on account of goods purchased of services received in the normal course of business.

6. A company shall disclose the following in the notes to accounts.

A. NON-CURRENT ASSETS

Non - current assets are those assets which are held for more than one year. They are also called long term or fixed assets. These are the assets which are intended to be used in the business over a long period of time (exceeding 12 months or the normal operating cycle of the business).

I. Property, Plant and Equipment:

i. Property, Plant and Equipment shall be classified as:

a) Land

b) Buildings

c) Plant and Equipment

d) Furniture and Fixtures

e) Vehicles

f) Office Equipment

g) Bearer Plants

h) Others (specify nature)

ii. Assets under lease shall be separately specified under each class of assets.

iii. A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations and other adjustments and the related depreciation and impairment losses or reversals shall be disclosed separately in the Notes.

II. Capital Work-in-Progress:

The capital wok-in-progress represents the expenditure incurred on acquiring or constructing tangible assets which are not yet ready for intended use. It may be noted that advances given to the supplier for acquisition of fixed assets are not included under this heading.

III. Investment Property :

Ind AS 40 defines investment property as land or building or both which is held to earn rental or capital appreciation or both. A reconciliation of the gros and net carrying amounts of each class of property at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations and other adjustments and the related depreciation and impairment losses or reversals shall be disclosed separately in the Notes.

IV. Goodwill

Goodwill is required to be presented as separate line item on the face of the balance sheet apart from 'other intangible assets'. A reconciliation of the gross and net carrying amount of goodwill at the beginning and end of the reporting period showing additions, impairments, disposals and other adjustments hall be disclosed separately.

V. Other Intangible Assets

Intangible assets are generally in the nature of rights. Intangible assets shall be classified as:

a. Brands or Trademarks
b. Computer software
c. Mastheads and publishing titles
d. Mining rights
e. Copyrights, patents, other intellectual property rights, services and operating rights
f. Recipes, formulae, models, designs and prototypes
g. Licenses and franchises
h. Others (specify nature)

These intangible assets are expected to generate economic benefits over a period of time. Hence, the cost of acquiring or developing these assets is apportioned over their useful lives. Apportioning the cost of an intangible asset over its useful life is called amortisation. Intangible assets are initially recognized at cost. They are carried in the balance sheet at cost less accumulated amortisation and any impairment losses.

A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals,acquisitions through business combintions and other adjustments and the related amortisations and impairment losses or reversals shall be disclosed separately

VI. Intangible Assets under Development

Expenditure incurred on development of intangible assets which are yet to be finished are accumulated and reported separately under this healing. Once the development of an intangible asset is completed, the amount accumulated under this head is transferred to gross carrying amount of the relevant intangible asset.

VII. Biological Asset other than Bearer Plants

A biological asset is defined in Ind AS 41 as living animal or plant. Examples of biological assets, as given in Ind AS 41, include sheep, trees in a timber plantation, diary cattle, cotton plants, sugar cane, tea bushes, oil palms, fruit trees, rubber trees,etc.

A reconciliation of the carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, dissposals, acquisitions through business combinations and other adjustments shall be disclosed separately.

VIII. Financial Assets

Financial assets generally mean cash, financial instruments of another entity (equity instruments, debts instruments) and a contractual right to receive cash or other financial assets. Accordingly, this heading includes the following:

i. Non-current investments

ii. Non-current trade receivables

iii. Non-current loans

iv. Other non-current financial assets

Non-current investments : a businessenterprise may invest its resources in acquiring the securities issued by another enterprise. Such an invrestment may be made either for controlling the other enterprise or simply for making a return either as periodical returns or capital gains. Where the intension is to hold such investments for a long period of time (usually exceeding 12 months), they are classified as non-current investments. Non-current investments can be classified as:

i. Investments in Equity Investments

ii. Investments in Preference Shares

iii. Investment in Government or trust securities;
iv. Investments in debentures or bonds;
v. Investments in Mutual Funds
vi. Investment in Partnership Firms
vii. Other Investments(specify nature)

under each classification, details shall be given of names of the bodies corporate that are:

- Subsidiaries
- Associates
- Joint ventures, or
- Structured entities,

In whom investments have been made and the nature and extent of the investments so made in each such body corporate (showing separately investments which are partly-paid). Investments in partnership firms other along with name of the firms, their partners, total capital and the shares of each partner should be disclosed separately.

The following shall be disclosed:

- o Aggregate amount of quoted investments and market value thereof;
- o Aggregate amount of unquoted investments; and
- o Aggregate amount of impairment in value of investments.

Non-current Trade Receivables: Amount outstanding to be received from the customers on the balance sheet date towards goods sold or services rendered is classified as trade receivables. Trade receivables which are expected to be realized after 12 months from the balance sheet date are classified as non-current.

- Trade receivable shall be sub-classified as:
- o Secured, considered good;
- o Unsecured considered good; and
- o Doubtful
- Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.

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

Non-current loans: loans represent the money extended by an enterprise to another as loan which is repayable in future. Loans expected to be realized after 12 months are classified as non-current loans.

Loans shall be classified as:

- Secured deposits;
- Loans to related parties (giving details thereof); and
- Other loans(specify nature)

The above shall also be separately sub-classified as:

- Secured , considered good ;
- Unsecured, considered good ; and
- Doubtful

o Allowance for bad and doubtful loans shall be disclosed under the relevant heads separately

o Loans due by directors or other officers of the company or any of them either severally or jointly with any other persons or amounts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

Other Non-current Financial Assets: non-current financial assets other than investments, trade receivables and loans are classified under this heading. Any financial asset which is non-current in nature and has not been classified in the earlier sub-headings will get disclosed under claims, receivables on account of sale of property, plant and equipment, contractually reimbursable expenses, etc., are classified as other non-current financial assets if they are realizable after 12 months.

Bank deposits of more than 12 months maturity shall be disclosed under 'Other Non-current Financial Assets'.

IX. Deferred Tax Assets

Deferred tax assets are recognized due to timing differences between the taxable income and the reported income. If due to such timing difference an enterprise has paid higher taxes in the current accounting period which will get reversed and result in lowering of tax liability in the future accounting period, the same is recognized as deferred tax asset.

X. Other Non-current Assets

This is the residual category for non-current asset. Any asset which is non-current and non-finance in nature and has not been classified in the above sub-headings will get disclosed in this heading.

Other non-current assets hall be classified as-

- Capital Advances; and
- Advances other than capital advances ;

Advances other than capital advances should be classified as:

- Security deposits;
- Advances to related parties (giving parties thereof); and
- Other advances (specify nature)

Advances to directors or other officers of the company or any of them either severally or jointly with any other persons or advances to firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

- Others (specify nature)

B. CURRENT ASSETS

Current assets include cash, cash equivalents, assets intended for sale or consumption or expected to be realized in cash within 12 months or in the company's normal operating cycle and held primarily for the purpose of being traded.

1. Inventories

The term 'inventories' include goods held by an enterprise for the purpose of consumption in the production process or which are currently in the production cycle or are being held for sale in the ordinary course of business.

Inventories shall be classified as-

- Raw materials
- Work-in-progress
- Finished goods
- Stock-in-trade (in repect of goods acquired for trading)
- Stores and spares
- Loose tool; and
- Others (specify nature).

1) Goods-in-transit shall be disclosed under the relevant sub-head of inventories.
2) Mode of valuation shall be stated.

1. Current Financial Assets

As discussed earlier, financial assets generally mean cash, financial instrument of another entity (entity instruments, debt instruments) and a contractual right to receive cash or other financial assets. Financial assets of current nature are included under this heading. Accordingly, this heading includes:

- Current investments
- Current trade receivables
- Cash and cash equivalents
- Current loans
- Other current financial assets.

a) Current Investments: an enterprise instead of keeping its short term caso surpluses in bank accounts may invest the same in financial instruments to generate higher returns. Such investments are usually made in instruments which are highly liquid and convertible into cash quickly. Current investments are intended to be sold within twelve months or within the company's operating cycle. They also include investments which have a remaining maturity of less than twelve months or within the company's operating cycle.

Investments shall be classified as-

- Investments in Equity Instruments;
- Investments in Preference Shares;
- Investments in government or trust securities;
- Investments in debentures or bonds;
- Investments in Mutual Funds
- Investments in Partnership firms; and
- Other investments (specify nature).

Under each classification, details shall be given of names of bodies corporate that are:

- Subsidiaries
- Associates
- Joint ventures or
- structured entities,

in whom investments have been made and the nature and extent of the investment so made in each such body corporate (showing separately investments which are partly-laid).

The following shall also be disclosed

- Aggregate amount of quoted investments and market value thereof;
- Aggregate amount of unquoted investments'
- Aggregate amount of impairment in value of investments.

b) Current Trade receivables: Trade receivable which are expected to be realized within 12 months from the balance sheet date or within the normal operating cycle are classified as current trade receivables. These include debtor and bills receivables.

- Trade receivables shall be sub classified as :
- Secured, considered good
- Unsecured considered good; and
- Doubtful.
- Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.
- Debts due by director or other officers of the company or any of them either severally or jointly with any other person or debt due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

c) Cash and cash equivalents: As per Ind AS-7, cash and cash equivalents include cash in hand and demand deposits with banks. Cash equivalents are defined as short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of change in value.

Cash and cash equivalents shall be classified as:

- Balances with banks (of the nature of cash and cash equivalents);
- Cheques and draft in hand;
- Cash on hand; and
- Others (specify nature).

d) Current Loans: Loans expected to be realized within 12 months of the date of the balance sheet are classified as current loan. This also security deposit given by the enterprise for various purposes during the ordinary course of business.

- Loans shall be classified as:
- Security deposits;
- Loans to related parties(giving details thereof);and

- Other(specify nature)
- The above shall also be sub-classified as-
- Secured considered good;
- Unsecured considered good; and
- Doubtful.
- Allowance for bad and doubtful loans shall be disclosed under relevant separately.
- Loans due by directors or other officers of the company or any of them either severally or jointly with any other person or amounts due by firms or private companies respectively in which any director is a partner or a director or a member shall be separately stated.

e) Current tax assets (Net)

Companies are required to pay advance tax on the estimated taxable income for the year. It may happen that the amount of tax already paid in respect current and prior periods exceeds the amount of tax due for those periods. The excess tax paid is computed for each assessment period separately.

f) Other current assets(specify nature)

This is the residual category for the current assets. Any asset which is current in nature and has not been classified in the above sub-headings will be included under this heading. Other current assets shall be classified as-

I. Advances other than capital advances

1) Advances other than capital advances shall be classified as:
    - Security Deposits;
    - Advances to related parties (giving details thereof)
    - Other advances (specify nature).
2) Advances to directors or other officers of the company or any of them either severally or jointly with any other person or amounts due by firms or private companies respectively

in which any director is a partner or a director or a member shall be separately stated.

II. Others (specify nature). These mainly include prepaid expenses and income earned nut not received.

STATEMENT OF PROFIT AND LOS (SOPL)

Also known as Profit and Loss Account. It is the primary financial statement to understand the operative performance of an enterprise during a given period. It summarize incomes earned and expenses incurred by an enterprise during a given period.The purpose of the Statement of Profit and Loss is to provide information about different sources of income and gains and also expenses and losses incurred during an accounting period. The Schedule III prescribes the vertical format to be followed showing income first followed by expenses.

FORMAT OF STATEMENT OF PROFIT AND LOSS (Table 2)

Name of the Company

	Particulars	Note No.	Figures as at the end of current year	Figures as at the end of previous year
I	Revenue from operations			
II	Other Income			
III	Total Income (I + II)			
IV	**EXPENSES**			
	Cost of materials consumed			
	Purchases of Stock –in-Trade			
	Changes in inventories of finished goods, Stock in Trade and work –in – progress			
	Employee benefits expenses			
	Finance cost			
	Depreciation			
	Other Expenses			
	Total expenses (IV)			
V	Profit / Loss before exceptional items and tax			
VI	(I-IV)			
VII	Exceptional items			
VIII	Profit / Loss before tax (V-VI)			
	Tax expense:			
	a. Current tax			
IX	b. Deferred Tax			
	Profit (Loss) for the period from continuing			
X	operations (VI-VIII)			
XI	Profit/Loss from discontinued operations			
XII	Tax expense of discontinued operations			
	Profit/Loss from discontinued operations (after			
XIII	tax) (IX-XI)			

XIV	Profit/Loss for the period (IX+XII) Other Comprehensive Income A a. Items that will not be reclassified to profit or loss b. Income tax relating to items that will not be reclassified to profit or loss B a. Items that will be reclassified to profit or loss b. Income tax relating to items that will			
XV	be reclassified to profit or loss Total Comprehensive Income for the period (XIII+XIV) (Compromising Profit (Loss) and			
XVI	Other Comprehensive Income for the period) Earnings per equity share (for continuing operation):			
XVII	1. Basic 2. Diluted Earnings per equity share (for discontinued operation):			
XVIII	1. Basic 2. Diluted Earnings per equity share (for discontinued & continuing operation): 1. Basic 2. Diluted			

Statement of Profit and Loss for the period ended

TREATMENT OF ADJUSTMENT ITEMS

4. CORPORATE DIVIDEND TAX

A dividend is the distribution of reward from a portion of the company's earnings and is paid to a class of its shareholders. In other words, the divisible profit of a company is distributed among the shareholders of a company on the basis of number of shares held. This is called dividend. Thus, dividend simply means the amount of divisible profit distributed among the shareholders. The Board of Directors will recommend the amount of profit to be distributed as dividend.

Dividends cannot be paid out of capital reserves. It should be paid out if accumulated profits. Preference dividend is paid first. Equity dividend will be paid only after the preference dividend is paid in full. If there are calls in arrears, dividend will be paid on the amount actually paid by shareholders (i.e. called-up capital minus calls in arrears). This means dividend is usually proposed or paid on paid-up capital. However, a company can make a provision in the Articles, authorizing it to propose dividend on the full nominal value of the shares.

Dividend can be declared and paid by a company and paid by a company for any financial year out of the following sources:

a) Current year's profits after providing for depreciation

b) Previous year's profits after providing for depreciation

c) Both current year's profits and previous year's profits

d) Money provided by Central Govt. or State Govt. for the payment of dividend in pursuance of a guarantee given by that Govt.

Earlier dividend distributed was taxed in the hands of the recipients (shareholders). But now companies distributing dividend are required to pay tax on such dividends. This is known as Corporate Dividend Tax (CDT). It is payable within 14 days from the date of declaration. The following pints should be noted in respect of CDT:

i. CDT is payable on any amount declared, distributed or paid by the company as dividend (interim or otherwise). The dividend may be paid out of current profit or accumulated profit.

ii. CDT is payable even if no income tax is payable by the company on its total income.

With effect from 1st October 2014 dividend distribution tax is leviable on gross dividend and not on the net dividend distributed to shareholders. Gross Dividend is the amount of dividend which is proposed to be distributed to the shareholders plus basic CDT. In other words, the actual dividend proposed is taken as net dividend. Therefore, if CDT rate is 15%, then net dividend denotes 85%. When we gross it up by dividing the net dividend by 85%, then the resultant amount is termed as gross dividend. At present, the CDT is calculated as below:

Basic CDT rate	15%
Add: Surcharge 12% of basic rate	1.8%
Add: Education Cess 4% of (Basic rate + Surcharge)	
(i.e., 4% of 16.8%)	0.672
	17.472

Corporate Dividend Tax is shown in the Notes to Accounts under the subhead "Surplus in the Statement of Profit and Loss". It is also shown in the Balance Sheet under the head "Short-term Provision".

Note: As per Ind AS 10, if the dividends are declared after reporting period but before the financial statements are approved, then the dividends are not recognized as a liability. In such case, dividends are only disclosed in the Notes because no obligationexists at the date of the financial statements. To be more clearly, in such circumstances the proposed dividend and CDT should be shown under 'Commitments' (under 'Contingent Liabilities and Commitments') in the Notes to Accounts.

If students ignore CDT while solving a problem, it should be specifically mentioned by way of a note - "Corporate dividend tax is ignored".

5. TRANSFER OF RESERVE

The Companies Act, 1956 had the provision of compulsory transfer to reserves dependingupon the rate of dividend. However, in Companies Act 2013, the compulsory provision has been removed. This means that now the Company is free to transfer any part of its profits to reserves it deems fit. Thus, the amount transferred out of the profits has now been left at the discretion of the Board of Directors.

Note: In examination questions, if nothing is given about transfer to reserve, it is advisable not to make any assumption regarding transfer to reserves. This means that if the question is silent on transfer of profit to reserves, students should not transfer any profit to reserves.

6. PROVISION FOR TAXATION

Provision for taxation is the provision made out of current profits to meet the tax obligation. There is a time gap between the provision made and payment of the actual tax liability. So it serves as a source of short-term finance during the intermediate period.

The Income Tax department will complete the assessment long time after the close of the accounting year. Therefore, the company will estimate the tax payable and on this basis it will make provision for taxation. For making provision for taxation, the following journal is required to be passed:

Statement of Profit and Loss Dr.

To Provision for Taxation A/c

Income tax is charge against profit. Hence, Provision for Taxation is treated as an expense in the Statement of Profit and Loss. Provision for Taxation will appear as liability in the Balance Sheet under the subhead "Provision" (in "others") under the head "Current Liabilities".

When the actual assessment of tax is made, balances appearing in Provision for income Tax Account, Advance Income Tax and Tax Deducted at Source on income earned by the company are transferred to Income Tax Account. If the actual assessment of tax comes to be more than provision made, the balance is deducted from the Surplus in the Balance Sheet as prior period tax expense. Similarly, if the actual assessment of tax is less than the amount provided for, the difference is added to the Surplus Account as prior period tax.

7. TDS ON INTEREST INCOME

When a company receives any interest from investments, the gross amount of the interest is shown in the Statement of Profit and Loss under the head "Other Income" (in case of Non-finance Company).

$$\text{Gross interest} = \text{Net interest} \times \frac{100}{90}$$

Suppose, a company receives Rs.27,000 as interest on investments, then Rs.30,000 (27,000 x 100/90) should be shown under 'other income' in the Statement of Profit and Loss and Rs. 3,000 tax deducted at source is shown in the Balance Sheet under the sub head 'Current Loans and Advances' under the head 'Current Assets'. Details will be given in the Notes to Accounts.

8. IMPLIED ADJUSTMENT OF INTEREST ON LOANS

When we see a loan account along with rate of interest in the trial balance (cr.) we should find whether the full amount of interest due on loan has been paid or not. The method to ascertain it is simple. Work out the total amount of interest due on loan as per given rate of interest and the date on which it was taken. Compare this amount of interest and the amount of interest (paid) given in the trail balance. If the interest paid (debit balance) is less than the total amount of interest due, the difference should be treated as outstanding interest. This is an implied adjustment.

Treatment in Final Accounts

Outstanding interest should be added to interest paid in the 'Notes to Accounts' under the head 'Finance Cost' which will appear in the Statement of Profit and Loss. At the same time, it should be shown in the 'Notes to Accounts' under the head 'Other Current Liabilities' to be shown in the Balance Sheet (liability).

9. DEPRECIATION

The monetary value of an asset decreases over time due to use, wear and tear or obsolescence. This decrease is measured as depreciation.

In other words, a decrease in an asset's value, may be caused by a number of other factors as well such as unfavorable market conditions, etc. Machinery, equipment, currency are some examples of assets that are likely to depreciate over a specific period of time. Accounting estimates the decrease in value using the information regarding the useful life of the asset. This is useful for estimation of property value for taxation purposes like property tax etc. For such assets like real estate, market and economic conditions are likely to be crucial such as in cases of economic downturn.

According to Companies Act, dividend can be declared or paid by a company only out of the profit arrived at after charging depreciation at special rates. Managerial commission or remuneration should also be determined on the net profit after charging depreciation. The Companies Act provides that the original cost, the accumulated depreciation and the written down value of each asset should be shown in the Balance Sheet. The required journal entry is:

Depreciation A/c Dr.

To Provision for Depreciation/

Accumulated Depreciation A/c

The Depreciation Account is transferred to Statement of Profit and Loss and Provision for Depreciation Account is shown in the Balance Sheet a deduction form the original cost of the Fixed Asset (in the Notes to Account).

If the depreciation appears in the trail balance, it is shown under the Statement of Profit and Loss under the head "Depreciation and Other Amortization Expenses". If it appears under adjustment, it is shown in the Statement of Profit and Loss. It is also deducted from the cost of the Fixed Assets in the Notes to Account under the head "Non-current Assets".

Companies Act 2013 does not prescribe the depreciation method to be followed by the companies, moreover, it does not prescribe the depreciation rates. However, Schedule II of the Companies Act 2013 provide indicative useful life of various assets. It also stipulates that the residual value should not be more than 5 per cent of the original cost. Usually, companies adopt the useful life indicated in Schedule II., if the company uses useful life that is different from that indicate din Schedule II, it is required to disclose the fact.

Provision for Depreciation

Sometimes the depreciation charge is credited to Provision for Depreciation Account (also called Depreciation Fund or Accumulated Depreciation) and not to the asset directly. The current year depreciation should be debited to P/L A/c. The adjusting entry is

Statement of Profit and Loss A/c Dr.

To Provision for Depreciation A/c

The total Provision for Depreciation (i.e. existing provision as per Trail Balance credit plus current year provision) should be deducted from the original cost of the asset in the 'Notes to Accounts' to be shown under the head 'Non-current Assets' in the balance sheet.

10. CLOSING STOCK

Closing stock is the amount of inventory that a business still has on hand at the end of a reporting period. This includes raw materials, work-in-process, and finished goods inventory. The amount of closing stock can be ascertained with a physical count of the inventory. Generally closing stock is not given in trail balance. It will be given under adjustment. The adjusting entry is:

Closing Stock A/c Dr.

To Statement of Profit and Loss

Generally closing stock is not given in trial balance because it is valued at the end of the year after the accounts have been closed. In other words, closing stock is not a ledger balance.

Treatment in Final Accounts

i. Closing Stock is shown in the statement of profit and loss under 'change in inventories'. Under this head, opening stock is compared with closing stock. If opening stock exceeds closing stock the difference is expense. If closing stock exceeds opening stock the difference should be treated as income (i.e. negative figures).

ii. It is also shown under the subhead 'Inventories' under the head 'Current Assets' in the Balance Sheet.

When adjusted purchases are given in the T/B, the opening stock will not appear in the Trail Balance. But closing stock will appear as a debit balance in the Trail Balance. Adjusted purchase means purchases after stock is adjusted, i.e. purchases plus opening stock minus closing stock. Adjusted purchases represents costs of goods sold. In such a case adjusted purchase will be shown under 'Expense' in the Statement of profit and loss. Neither opening stock nor closing stock would appear in the Statement of Profit and Loss (both are already adjusted in the purchase account). In this case, closing stock given in the Trail Balance will appear only at one place, i.e. the Balance Sheet.

11. PROVISIONS

(A) Provision for bad and doubtful debts

A part of the debtors at the end of the year may be irrecoverable. This means that some of the debtors are doubtful. A doubtful debt is the debt which may or may not be recovered. It is necessary to show every asset at its true value. Hence all enterprises based on their past experiences create a provision for doubtful debts to meet such a probable los in case it happens.

Provision is created at a certain percentage (based on past experience) on sundry debtors. The entry for creating provision is:

Statement of Profit and Loss Dr.
To Provision for Doubtful Debts

Treatment in Final Accounts

a) Provision appearing in the trial balance:

The provision given in the trial balance (Cr.) is the provision created last year, i.e. opening provision. It is deducted from 'Other Expenses' (to be shown in the Statement of Profit and Loss) in the 'Notes to Accounts' (taken at one place only). Alternatively, the bad debt of the current year and the new provision will be adjusted against the opening provision. The details are shown in the 'Notes to Accounts'. It should be noted that when Provision for Bad and Doubtful Debts exists, the bad debts are not transferred to Statement Profit and Loss, instead they are debited to the Provision A/c by passing the following entry:

Provision for Bad and Doubtful Debts A/c Dr.
To Bad Debt A/c

Opening or old provision is shown in the Notes to Account in the following manner:

Note No.	Particulars	Amount (Rs.)
	Other Expenses	xxx

	Less: Provision for Doubtful Debts (Opening)	xxx

Notes to Accounts

b) Provision given in the adjustments:

Provision given in the adjustment is the provision to be created in the current year, i.e. new provision. It should be taken at two places. First is should be included in the 'Other Expenses' in the Notes to Accounts to be shown in the Statement of Profit and Loss. Then it should be deducted from Sundry Debtors under the head 'Trade Receivables' in the Notes to Accounts to be shown in the Balance Sheet (assets). It is calculated at a given percentage of debtors. It should be noted that the provision (new) is to be calculated on sundry debtors after deducting additional bad debts, if any, given in the adjustments.

Notes to Accounts relating to 'Other Expenses' and 'Trade Receivables' are prepared in the following manner:

Notes to Accounts

Note No.	Particulars	Amount (Rs.)	
	Other Expenses		
	Bad Debts (given in trail balance as well as in adjustment)		xxx
	Add: Provision for Doubtful Debts		
	(new provision given in adjustment)	xxx	
			xxxx
	Less: Provision for Doubtful Debts		
	(old provision given in trail balance)	xxx	
		xxx	

Notes to Accounts

Note No.	Particulars		Amount (Rs.)
	Trade Receivables		
	Sundry Debtors		xxx
	Less: Bad Debts (given in adjustment)		
	xxx		xxx
	Less: Provision for Doubtful Debts (New provision)	xxx	xxx

(B) Provision for discount on debtors

Some amount of discount may have to be allowed in the next accounting year. However the loss belong to thecurrent period because the debtors relate to the current period.Therefore, at the end of theaccounting year aprovision is created for the anticipated loss in the form of discount that is likely to be allowed to debtors. This is called provision for discount on debtors. The adjusting entry is:

Statement of Profit and Loss Dr.

To Provision for Discount on debtors

Treatment in Final Accounts

Provision for discount on debtors will be treated in the same way as provison for doubtful debts is treated.

(C) Provision for discount on creditors

If a firm makes early payment to its creditors, it will receive discount. When it receives discount from creditors regularly, it can make a provision for the discounts which is likely to be received in the next year from the current creditors. Provision for discount on creditors is a probable income. It may be noted that creation of the provision for expected profits is against the convention of conservatism. The entry for creating provision is a follows:

Provision for Discount on Creditors A/c Dr.

To Statement of Profit and Loss

Treatment in Final Accounts

Provision for discount on creditors is calculated on sundry creditors. Provision for discount on creditors is shown in the 'Notes to Accounts' by way of deduction from 'Other Expenses' (this appears in the Statement of Profit and Loss). Then it should be deducted from sundry creditors under the head 'Trade Payables' in the 'Notes to Accounts' which appears in the Balance Sheet (liability).

12. OUTSTANDING EXPENSES

Outstanding expenses are those expenses which have been incurred during the current accounting period and are due to be paid, however, the payment is not made.Outstanding expenses are recorded in books of finance at the end of an accounting period to show the true numbers of a business.They are those expenses which remain unpaid at the end of the accounting period. In order to arrive at true profit or loss, it is necessary to take into account the outstanding or accrued expenses. The adjusting entry is:

Expenses A/c Dr.

To Outstanding Expenses A/c

Treatment in Final Accounts

i. Outstanding expenses should be added to the concerned expenses in the 'Notes to Accounts' to be shown in the statement of profit and loss.

ii. It should be shown in the Balance Sheet under the sub head 'other current liabilities' under the main head 'current liabilities'.

If outstanding expenses or accrued expenses are given in Trail Balance (Cr. Balance) then it should be shown only in Balance Sheet as a liability under the subhead 'Other Current Liabilities'. This means that it has already been adjusted by debiting the expenses (hence expense is increased) and crediting outstanding expenses (liabilities appearing on the credit side of the Trail Balance).

13. PREPAID EXPENSES

A prepaid expense is a type of asset on the balance sheet that results from a business making advanced payments for goods or services to be received in the future. Prepaid expenses are initially recorded as assets, but their value is expensed over time onto the income statement.

Prepaid expenses are the payment made in the current year but related to the next accounting year. In short, prepaid expenses are expenses paid in advance. They are also known as unexpired expenses. The adjusting entry is:

Prepaid Expenses A/c Dr.

To Expenses A/c

Treatment in Final Accounts

i. Prepared expenses should be deducted from the concerned expense in the Notes to Accounts to be shown in the Statement of Profit and Loss.

ii. Prepared expenses should also be shown in the Balance Sheet under the Sub head 'Other Current Assets' under the main head 'Current Assets'.

If prepaid expense is given in Trail Balance (Dr. balance), then it should be taken only in the Balance Sheet as asset. This means that adjustment entry has already passed.

14. ACCRUED INCOME

This is the income earned but not received by the end of the accounting year. Such incomes arise in case of interest on investments, rent on building, commission etc.

Accrued Income A/c Dr.
To Income A/c

Treatment in Final Accounts

i. Accrued income should be added to the concerned income in the Notes to Accounts to be shown in the Statement of Profit and Loss.

ii. It is also shown in the Balance Sheet under the Sub head 'Other Current Assets' under the main head 'Current Assets'.

If accrued income or outstanding income is given in trail balance (Dr. balance), then it should be taken only in Balance Sheet. This implies that the adjustment entry has already been passed. In the adjusting entry, Interest accrued on investment is debited. Hence it appears on debit side of the Trail Balance. Interest is credited and hence it is increased.

15. RECEIVED IN ADVANCE (OR UNEARNED INCOME)

Sometimes, the whole amount of income received in an accounting year does not belong to the current year. A part of it may relate to next year. Such portion of income received but nor earned is called income received in advance or unearned income. The adjusting entry is:

Income A/c Dr.
To Unearned Income A/c

Treatment in Final Accounts

i. Income received in advance should be deducted from the concerned income in the Notes to Accounts to be shown in the Statement of Profit and Loss.

ii. It is also shown in the Balance Sheet under the Sub head 'Other Current Liabilities' under the main head 'Current Liabilities'.

If income received in advance or unearned income is given in trail balance (Cr. balance), then it should be taken only in Balance Sheet. This implies that the adjustment entry has already been made.

PRACTICAL PROBLEMS

PROB 1

ArushiLtd.issued5,000,10%debenturesofRs.100eachatparbutredeemable at a premium of 5% after 5 years. Give journal entries and also prepare the balancesheetofthecompany.

Answer

Books of Arushi Ltd.

Date	Particulars	LF	Debit Rs.	Credit Rs.
	BankA/c Dr. To 10% Debenture Application and Allotment A/c (Being application money received)		5,00,000	 5,00,000
	10%DebentureApplication and AllotmentA/c Dr. Loss on Issue ofDebentures A/c Dr. To 10% DebenturesA/c To Premium on Redemption of Debentures A/c (Being debentures issued at par but redeemable at premium)		5,00,000 25,000	 5,00,000 25,000

Journal

Arushi Ltd.

Balance Sheet as on 31st March, 2013

Particulars		Note No.	31March 2013(Rs.)
I. Equity and Liabilities			
1. Non-current Liabilities			
a) Long-term borrowing		1	5,00,000
b) Other long-termliabilities		2	25,000
Total			**5,25,000**

II. Assets		
1. Non-current assets		
a) Other non-current assets	3	20,000
2. Current Assets		
a) Cash and cash equivalents	4	5,00,000
b) Other current assets	5	5,000
Total		**5,25,000**

Notes to Accounts

Particulars	Amount (Rs.)
1. Long-term borrowings	
5,000, 10% debentures of Rs. 100 each	5,00,000
2. Other long termliabilities	
Premium on redemption of debentures A/c	25,000
3. Other non-current assets	
Loss on issue of debentures	20,000
(4/5th of Rs. 25,000)	
4. Cash and cash equivalents	
Cash at bank	5,00,000
5. Other current assets	
Loss on issue of debentures	5,000
(1/5th of Rs. 25,000, i.e., amount to be written-off in next 12 months)	

PROB 2

Show the following items in the balance sheet of Sunfill Ltd.:

Particulars Amount(Rs.)

General Reserve (since 31March2012) 5,00,000

Statement of profit & loss

(debit balance)for2012-13 (3,00,000)

Answer

Books of Sunfill Ltd.

Balance Sheet as at March 31, 2013

Particulars	Note No.	31st March 2012(Rs.)	31st March 2013(Rs.)
I. Equity and Liabilities 1. Shareholders' Funds Reserve and surplus	1	2,00,000	5,00,000

Notes to Accounts

Particulars	Amount (Rs.)
1. Reserve and surplus General Reserve (1 April, 2012) Less: Statement of profit and loss (Dr. balance)	5,00,000 (3,00,000)
	2,00,000

PROB 3

Show the following items in the balance sheet of Avalon Ltd. as at March 31, 2013:

	Rs.in Lakh
General Reserve (since 31 March 2012)	5
Statement of Profit & Loss (Debit Balance) for 2012-13	(8)

<u>*Answer*</u>

Books of Avalon Ltd. Balance Sheet as on 31st March, 2013

Particulars	Note No.	31March 2013(Rs.)
I. Equity and Liabilities 1. Shareholders'Funds a) Reserve andSurplus	1	(3,00,000)

Notes to Accounts

Particulars	Amount (Rs.)
1. Reserve andSurplus i) General reserve (1 April,2012) ii) Less: Statement of profit and loss (debitbalance)	5,00,000 (8,00,000)
	(3,00,000)

PROB 4

Fromthefollowingparticulars,prepareStatementofprofitandlossfortheyear endingMarch2013.

Particulars	Rs.	Rs.

Plant and Machinery	1,60,000	
Land	6,74,000	
Depreciation on Plant and Machinery	16,000	
Purchases (Adjusted)	4,00,000	
Closing stock	1,50,000	
Wages	1,20,000	
Sales (Net)		10,00,000
Salaries	80,000	
Bank overdraft		2,00,000
10% debentures (issued on 1st April, 2012)		1,00,000
Equity share capital– shares of Rs. 100 each (fullypaid)		2,00,000
Preference share capital– 1,000 6% shares of Rs. 100 each (fully paid)		1,00,000
	16,00,000	**16,00,000**

Additional information

(i) Equity dividend @ 10% declared on paid upcapital.

(ii) Dividendonthepreferencesharecapitalpaidinfull.

(iii) Rs.2,00,000transferredtogeneralreserve

Answer

Statement of Profit and Loss for the year ending 31st March, 2013

Particulars	Note No.	Amount (Rs.)
I. **Income**		
Revenue from operations (Sales)		10,00,000
Total (I)		10,00,000
II. **Expenses**		
Cost of materials consumed (Adjusted purchase)		4,00,000
Employees benefit expenses	1	2,00,000
Finance cost		
Depreciation and amortisation		10,000
		16,000
Total (II)		6,26,000
Profit before tax (I-II)		**3,74,000**

Notes to Accounts

Particulars	Amount Rs.	Amount Rs.
Employee Benefit Expenses (i) Wages (ii) Salary	 1,20,000 80,000	 2,00,000

PROB 5

From the following ledger balances of Varun Ltd., Prepare balancesheet of the company as on 31st March, 2019.

Particulars	Rs.	Particulars	Rs.
Plant and Machinery	6,00,000	Immovable property	10,00,000
8% Debenture	8,00,000	Public deposit	5,00,000
Employees' Provident Fund	1,30,000	Provision for taxation	1,80,000
Securities Premium	80,000	Drafts on hand	5,00,000
Cash at Bank	34,000	Bills Recievable	2,40,000
24000 fully paid Equity shares of Rs.100 each Rs.50 called up	12,00,000	Brokerage on issue of shares	1,10,000
Sundry Creditors	1,16,000	Bank overdraft	1,50,000
Loan to Manager	70,000	Security Deposit	1,24,000
Deposits with ICICI Bank (5 years)	1,98,000	Trade marks	1,80,000
Prepaid insurance	1,00,000		

Answer

Balancesheet of Varun Ltd. as on 31st March, 2019

Particulars		Note No.	Amount (Rs.)
EQUITY AND LIABILITIES			
1.	**Shareholders' fund:**		
Share capital		1	12,00,000
Reserves & Surplus			80,000
2.	**Share application money pending allotment**		Nil
3.	**Non-current liabilities**		
a)	Long term borrowings	2	13,00,000
b)	Long term provisions		1,30,000
4.	**Current Liabilites**		
a)	Short term borrowings		1,50,000
b)	Trade Payables		1,16,000
c)	Short term provisions		1,80,000
TOTAL			**31,56,000**
ASSETS			
1.	**Non current Assets**		
a)	Fixed Assets		
(i)	Tangible Assets	3	16,00,000
(ii)	Intangible Assets		1,80,000
b)	Non current investment		1,98,000
c)	Long-term loans & advances		1,24,000
d)	Other non-current asset		1,10,000
2.	**Current Assets**		
1.	Trade recievables		2,40,000
2.	Cash and cash equivalents	4	5,34,000
3.	Short term loans and advances		70,000
4.	Other current assets		1,00,000
TOTAL			**31,56,000**

Notes to Accounts

1. Share Capital

Authorised Capital (24,000 Equity Shares of Rs.100 each)	**24,00,000**
Issued & Subscribed Capital (24,000 Equity Shares of Rs.100 each)	**24,00,000**
Paid up & Called up capital (24,000 Equity Shares of Rs.80 each)	**12,00,000**
TOTAL	**12,00,000**

2. **Long Term Borrowings**

8% Debenture	**8,00,000**
Public deposits	**5,00,000**
TOTAL	**13,00,000**

3. **Tangible Assets**

Plant & Machinery	**6,00,000**
Immovable Property	**10,00,000**
TOTAL	**12,00,000**

4. **Cash & Cash Equivalent**

Cash in hand	**34,000**
Drafts on hand	**5,00,000**
TOTAL	**5,34,000**

PROB 6

From the given particulars of Shine and Bright Co. Ltd. as at March 31, 2013.

Prepare balance sheet.

Particulars	Amount Rs.	Particulars	Amount Rs.
Preliminary expenses	2,40,000	Goodwill	30,000
Discount on Issue of shares	20,000	Loose Tools	12,000
10% Debentures	2,00,000	Motor vehicles	4,75,000
Stock in trade	1,40,000	Provision for tax	16,000
Cash at bank	1,35,000		
Bills receivables	1,20,000		

Answer

Book of Shine and Bright Ltd.

Balance Sheet as at March 31, 2013

Particulars	Note No.	Figure as at the end of current	Figure as at the end of previous

		reporting period	reporting period
Equity and Liabilities			
1. Non-current Liabilities	1	2,00,000	
a) Long-term borrowings			
2. Current liabilities	2	16,000	
a) Short-term provisions			
Assets			
1. Non-current assets			
a) Fixed assets	3	4,75,000	
Tangible assets	4	30,000	
Intangible assets			
2. Other non – current assets	5	2,60,000	
Current assets	6	1,52,000	
a) Inventories	7	12,000	
b) Trade receivables		1,35,000	
c) Cash and cash equivalents			

Notes to Accounts

Particulars		Amount (Rs.)
1. Long-termborrowings:		
10% debentures		2,00,000
2. Short-term provisions:		
Provision fortaxation		16,000
3. Fixedassets:		
1. Tangibleassets		
2. Motorvehicles		4,75,000
3.		
4. Intangible assets		30,000
5. Goodwill		
6.		
4. Other non-current assets	2,40,000	
Preliminaryexpenses	20,000	2,60,000
Discount on issue of debentures	1,40,000	
5. Inventories		
Stock in trade	12	1,52,000
Loosetools	,000	
6. Tradereceivables		
Billsreceivables		12,000
7. Cash & cash equivalents		
2. Cash atbank		1,35,000

Note: It has been assumed that discount on issue of debentures is not written-off in the next 12 months of the reporting period

PROB 7

Show the following items in the balance sheet of Amba Ltd. as on 31st March, 2013

	Rs.
8% Debentures	10,00,000
Equity share capital	50,00,000
Securities premium	20,000
Preliminary expenses	40,000
Statement of Profit & Loss(cr.)	1,50,000
Discount on issue of 8% debentures	
(Amount to be written in next 4 years approx.)	40,000
Loose tools	20,000
Bank balance	60,000
Cash in hand	38,000

Answer

Books of Amba Ltd. Balance Sheet as on 31st March, 2013

Particulars		Note No.	Amount (Rs.)
I. Equity and Liabilities			
1. Shareholders' Funds			
a) Share capital			50,00,000
b) Reserve and surplus		1	1,30,000
2. Non-current Liabilities			
a) Long-term borrowings		2	10,00,000
II. Assets			
1. Non-current assets			
a) Other non-current assets		3	30,000
2. Current assets			
a) Inventories		4	20,000
b) Cash and cash equivalents		5	98,000
c) Other current assets		6	10,000

Notes to Accounts

Particulars	Amount (Rs.)	Amount (Rs.)

1. Reserve andsurplus		
Securitiespremium 20,000		
Less:Preliminaryexpenses (40,000)	(20,000)	
Statement of profit and loss	1,50,000	**1,30,000**
2. Long-term borrowings 8%debentures		
3. Other non-currentassets		
Discount on issue of 8% debentures (of Rs. 40,000)		10,00,000
4. Inventory		
Loosetools		
5. Cash and cash equivalents		30,000
Bankbalance		
Cash in hand		20,000
6. Other current assets	60,000	
Discount on issue of 8% debentures	38,000	
(of Rs. 40,000)		98,000
		10,000

Multiple Choice Questions

1. Divisible profit do not include
   a. Insurance fund b.Reserve fund,
   c. profit and loss account balance d.revaluation reserve
2. loose tools are shown in the B/S under the head.
   a. Fixed asset b.Investment
   c. Current asset d.Miscellaneous expenditure
3. Discount on shares and debentures are shown in
   a. Profit and loss appropriation account
   b. Asset side of the balance sheet
   c. Liability side of the balance sheet
   d. None of these
4. Calls in arrear is
   a. Shown as current asset
   b. Deducted from share capital
   c. Shown as current liability
   d. Shown under miscellaneous expenditure

5. The amount set aside to meet the loss of bad debt is
   a. Provision b.Liability
   c. Reserve d.Contingent liability
6. In the case of joint stock company, goodwill is shown on the asset side under the head.
   a. Non current asset b.Investment
   c. Current asset d.Miscellanious expenditure
7. Advance payment of tax should be shown on the
   a. Debit side of P/L A/c
   b. Debit side of the profit and appropriation account
   c. Asset side of the balance sheet
   d. Liability side of the balance sheet
8. Which of the following item will be taken in the surplus statement
   a. Provision for taxation b.Transfer to sinking fund
   c. Contribution to PF d.Preliminary expenses written off
9. Scrip dividend means
   a. Unclaimed dividend b.Arrears of dividend
   c. Dividend paid other than cash d.Cash dividend
10. Which of the following would not appear in a limited company's surplus/Deficit statement
    a. Transfer to revaluation reserve
    b. Provision for taxation
    c. Interim dividends
    d. Transfer to general reserve

Answers

1d, 2c, 3b, 4b, 5a, 6a, 7c, 8d, 9c, 10b

Short answer type questions

1. What are the contingent liabilities?
2. What are contingent asset?
3. What are preliminary expenses?
4. What are divisible profit?

5. What do you mean by interim dividend?
6. What are reserves?
7. What are provisions?
8. What do you mean by capital reserve?
9. What do you mean by revenue reserve?
10. Distinguish between interim dividend and final dividend?
11. What is scrip dividend

Short essay type questions

1. Give proforma B/S of a company under Schedule III of the companies Act, 2013
2. Explain the treatment of provision for tax under companies act
3. Distinguish between reserve and provision
4. What are the contingent liabilities? Give examples.
5. How are preference shares treated in company final accounts?

SYLLABUS
BCM2B02FINANCIALACCOUNTING

Lecture Hours per week: 6

Credits: 4Internal: 20, External: 80, Examination 2.5 Hours

Objectives:

- To equip the students with the skills of preparing financial statements for various type of organizations.
- To enable the students to acquire knowledge about financial reporting standards and to understand corporate accounting methods.

Module I

Single Entry System of Accounting: Definition - Objectives - Advantages- Limitations-Distinction between Double entry and Single entry- Types of Single entry- Determination of Profit or Loss under single entry- Statement of Affairs/ Capital comparison method-Distinction between Balance Sheet and Statement of Affairs- Distinction between Profit and loss account and Statement of Profit and Loss- Conversion method- Practical Problems. (16 Hours, 15 marks)

Module II

Company Accounts- Issue of Shares: Introduction- Books of accounts maintained by companies- Share Capital- Phases of capital- Difference between Reserve capital and Capital Reserve- Shares and types of shares- Equity and Redeemable Preference shares - Convertible Cumulative Preference Shares (CCP shares) Sweat Equity shares- Employees Stock Option Scheme (Theory only)- Private Placement of shares- Issue of shares- Procedures- Minimum Subscription- Shares issued for consideration- Shares issued for consideration other than cash- Issue of shares at par and premium (issue at discount, not to be taught)- Treatment of Fraction shares- Application, Allotment and Calls on Shares-

Share capital allotment- Calls in arrears and calls in advance- Interest on calls in arrears and calls in advance- Difference between calls in arrears and calls in advance- Oversubscription and under subscription- Pro-rata allotment- Forfeiture and reissue of shares-Annulment of forfeiture- Surrender of shares- Distinction between forfeiture and surrender- Journal entries- Practical problems. (30 Hours, 25 marks)

Module III

Accounting for issue of Debentures :Definition - Types of debentures- Issue of Debentures- For cash, for consideration other than cash and issued as collateral security- Fraction debentures- Distinction between share and debenture- Terms of issue of debentures- Interest on debentures- Journal entries- Practical problems. (10 Hours, 10marks)

Module IV

Convergence to International Financial Reporting Standards: Meaning of Accounting Standards- need and importance of global accounting standards- Role of IASB in developing IFRS - components of IFRS (IAS,IFRS,IFRIC and SIC)- process of setting IFRS -Conceptual Framework and its contents - Definition of elements in financial statements- Criteria or principles of recognition, measurement, presentation and disclosure- convergence to IFRS- Emergence of Ind AS - Standard setting process in India- Role of NFRA -Entities required to adopt Ind AS- Role of FASB in developing US GAAP- Difference between Ind AS and IFRS .(18 Hours, 15 marks)

Module V

Ind. AS / IFRS complied Financial Statements of Companies (Ind AS1): Preparation of final accounts under new format (SOPL, SOCE and SOFP - excluding SOCF) - Treatment of adjustment items such as Corporate Dividend Tax- Transfer to

Reserve- Provision for taxation- TDS on Interest income, implied adjustment of interest on loans and other usual adjustment items such as depreciation, Closing stock, provisions, outstanding, prepaid, accrued, and received in advance -Practical problems.

(22 Hours, 15marks)

(Theory and problems may be in the ratio of 30% and 70% respectively)

Reference Books:

1. S.N. Maheshwari: Financial Accounting.
2. M.C. Shukla, T.S. Grewal and S.C. Gupta, Advanced Accounts,S.Chand& Co., New Delhi.
3. Naseem Ahmed, Nawab Ali Khan and M.L.Gupta: Fundamental of Financial Accounting, Ane Books Pvt. Ltd, NewDelhi.
4. Grewal and Gupta: Advanced Accounting
5. Dr Goyal V.K., Financial Accounting, Excel Books, NewDelhi.
6. R.L. Gupta and Radhaswamy, Advanced Accounting, Sultan Chand &Sons, NewDelhi.
7. R.K.Malhotra: Financial Management in Hotels and Restaurant Industry, AnmolPublishers
8. S.Kr. Paul: Advanced Accounting
9. B.S. Raman, Advanced Accountancy.
10. Jain &Narang: Financial Accounting
11. Ashok Sehgal and Deepak Sehgal: Advanced Accounting,Volume1,Taxmann,NewDelhi.
12. Chintal Patel, Bhupendra Mantri, India Accounting Standards, Taxmann Publications.
13. T.P. Ghosh, Illustrated Guide to India Accounting Standards, Taxmann Publications.