Corporate Accounting

Unit-2

Company Financial Statements

(1) What do you mean by Current Assets and Non –Current Assets?

Answers: 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 12 months after the reporting date.**

All other assets shall be classified as non- current assets.

(2) What do you mean by current liabilities and non- current liabilities?

Answer: 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 12 months after the reporting date.**

All other liabilities shall be classified as non- current liabilities.

(3) What do you mean by Deferred Taxes and Deferred Tax Liabilities?

Answer: The difference between tax on accounting income and taxable income is called deferred tax.

A deferred tax liability comes into existence when the accounting income is more than taxable income.

(4) What do you mean by Deferred Tax Asset?

Answer: A deferred tax asset comes into existence when accounting income is less than taxable income. The common example is provision for doubtful debts.

(5) What do you mean by Commitments?

Answer: Commitment is defined as an agreement to perform a particular activity at a certain time in the future under certain circumstances.

(6) What do you mean by Stock Exchange Listing Fee and Filling Fee with the Registrar (ROC)?

Answer: Stock Exchange Listing Fee or share listing fee is the fee which a company is required to pay to get their shares listed in a stock exchange.

Filling Fee paid to the Registrar (ROC) means the amount paid to the ROC at the time of filing of various returns.

(7) What do you mean by Transfer Fee?

Answer: Transfer fee means the fee received by a company from the shareholders in connection with the transfer of securities. Such fee is treated as revenue income.

(8) What do you mean by Interim Dividend?

Answer: Interim dividend represents the amount of dividend declared and paid by the company during the year before the preparation of final accounts. Interim dividend is declared and paid by the Board of Directors and there is no necessity of calling a meeting of the shareholders to sanction the payment of such dividend.

(9) What do you mean by Corporate Dividend Tax?

Answer: Corporate Dividend Tax is a provision for taxation on dividend on companies. This tax is termed as ' Corporate Dividend Tax'. Any domestic company declaring, distributing or paying dividends is required to pay this tax at the rates applicable for the concerned year. This rate has been revised to 15% from 1. 4. 2007.

(10) What do you mean unpaid and unclaimed dividend?

Answer: Unpaid dividend means the dividend declared but not yet paid by the company. If there is any unpaid dividend, it will appear on the credit side of the trial balance.

Unclaimed dividend represents the amount of dividend which is declared and against which dividend warrants have been issued to the shareholders, but the same have not been collected by the shareholders.

(11) What do you mean by share warrant?

Answer: A share warrant is a bearer document of title to shares and can be issued only by public limited companies and that too has fully paid up.

(12) State the statutory provisions relating to preparation and presentation of final accounts.

Answer: The important provisions from the view point of preparation of financial statements are summarized below:

- **(a) Every company shall prepare and keep as its registered office books of account and other relevant books and papers and financial statement for every financial year.**
- **(b) Financial statements shall give a true and fair view of the state of the affairs of the company, including that of its branch office(s) , if any.**
- **(c) Such books shall be kept on accrual basis and according to the double entry system of accounting.**
- **(d) Company may keep such books of account or other relevant papers in electronic mode in such manner as may be prescribed.**
- **(e) The books of account and other books and papers maintained by the company within India shall be open for inspection at the registered office of the company or at such other place in India by any director during business hours , and in the case of financial**

information shall be maintained and produced for inspection by any director subject to such conditions as may be prescribed.

(f) The books of account of every company relating to a period of not less than 8 financial years immediately preceding a financial year, or where the company had been in existence for a period less than 8 years, in respect of all the preceding years together with the vouchers relevant to any entry in such books of account shall be kept in good order.

(g) Financial Statements shall be prepared as per the instructions and in the form or forms as may be prescribed for different class or classes of companies in Schedule III

(h) At every annual general meeting of a company, the Board of Directors of the company shall lay before such meeting financial statements for the financial year.

(13) What do you mean by Intangible assets under development?

Answer: It refers to intangible assets which are being developed by the company itself.

(14) What do you mean by Tax Deducted at Source (TDS) ?

Answer: TDS means the amount of income tax deducted from the amount payable to the payee by the person making the payment. In case of a company, there may be 2 situations in respect of TDS:

(a) TDS on payment made by the company.

(b) TDS on payments received by the company.

(15) Write a note on accounting treatment of Proposed Dividend.

Answer: Earlier proposed dividend was treated as a liability and was shown under the sub head ' Short Term Provision' under the main head ' Current Liabilities' in the Balance Sheet. But now after the Notification of the Ministry of Corporate Affairs dated 6th Of April, 2019 , regarding amended Schedule III to Companies Act 2013, and after the amendment of AS4 'Events Occurring after the Balance Sheet Date' any amount of

dividend proposed by the BOD after the balance sheet date cannot be treated as current liability. It shall be shown in the "Notes to Accounts" as Contingent Liability.

(16) What do you mean by Investors Education and Protection Fund?

Answer: If any claim against the unpaid dividend is made, the payment will be made out of Unpaid Dividend Account. But if any such money remains unpaid for a period of 7 years from the date of such transfer, shall be transferred to an account called 'Investor education and protection fund' established by the Central Govt. as per the provisions of section 125 of the Companies Act, 2013.

(17) What do you mean by calls unpaid?

Answer: Calls unpaid represent the amount not paid by the shareholders on the calls made on them by the company.

(1) What do you mean by Financial Statements . Or

Give the meaning of financial statements.

Answer: Financial Statements are formal records of financial activities of a business. Financial Statements record the performance of the business and helps in identifying the strengths and weaknesses of the business.

According to Anthony," Financial Statements, essentially are interim reports , presented annually and reflect a division of the life of an enterprise into more or less arbitrary accounting period more frequently a year'.

(2) Explain the nature/ features of Financial Statements.

Answer: Following are the characteristics of Financial Statements:

(a) Financial Statements are prepared at periodical intervals usually at the end of the accounting period, generally ,one year as per the provisions of the company law.

(b) Financial Statements are prepared by the management depicting the true and fair view of the state of affairs of the entity for the period under review.

(c) Financial Statements are summarized reports prepared on the basis of accounting records.

(d) Financial Statements are prepared following the accounting conventions.

(e) Financial Statements are influenced by the personal judgments of the policy makers that are the management.

(3) Name the items shown under the head Shareholder's Fund.

Answer: Following items are shown under the head Shareholder's Fund:

(a) Equity Share Capital. (b) Preference Share Capital. (c) Securities Premium Reserve. (d) General Reserve.

(4) Name any 3 items that can be shown under the head "Reserve and Surplus".

Answer: Following items are shown under the head "Reserve and Surplus".

(a) Capital Reserves. (b) General Reserve. (c) Securities Premium Reserve. (d) Revaluation Reserve.

(5) Name the major headings under which the liabilities and assets side of a Company's Balance Sheet is organized and presented.

Answer: Major Headings of the assets side of a Company Balance Sheet is:

(1) Non-Current Assets.

(2) Current Assets.

Major Headings of the liabilities side of a Company Balance Sheet is:

(1) Shareholder's Fund.

(2) Share Application Money Pending Allotment.

(3) Non-Current Liabilities.

(4) Current Liabilities.

(6) Give the new format of the Balance Sheet of A Company. Or

Give the format of Balance Sheet of a Company as Per Company's Act 2013.

Answer: Format prescribed under Schedule III to the Companies Act 2013 are as under:

Particulars	Note Number	Current Year	Previous Year
I. EQUITY AND LIABILITIES (1) Shareholder's Fund (2) Share Application Money Pending Allotment (3) Non-Current Liabilities. (4) Current Liabilities.			

TOTAL		**xxxx**	**xxxx**
II.ASSETS **(1) Non –Current Assets.** **(2) Current Assts.**		 **xxx** **xxx**	 **xxx** **xxx**
TOTAL		**xxxx**	**xxxx**

(7) What do you mean by Contingent liabilities? Mention any 2 items of Contingent Liabilities.

Answer: Contingent Liabilities are those liabilities that may be incurred by an entity on the outcome of an uncertain future event such as outcome of a pending lawsuit.

Examples of Contingent Liabilities are:

(a) Uncalled Liability on shares (b) Legal Liability. (c) Tort (d) Liquidated damages.

(8) What do you mean by Preliminary Expenses? Mention the items which are usually included in the list of Preliminary Expenses.

Answer: Preliminary expenses are the expenses that are incurred before the incorporation, initial stage and commencement of the business. The expenses incidental for the formation of a company are also regarded as preliminary expense. These are considered as deferred revenue expenditure.

Examples of Preliminary Expenses are:

(a) Company Incorporation Expenses (b) Logo Expenses (c) Amount paid for stamp duties.

(9) Discuss the limitations of Financial Statements.

Answer: Following are the limitations of Financial Statements:

(a) Do not reflect current situation: Financial Statements are prepared from the books and accounts after the annual closure of accounts. They provide information of past events. From such statements, current position cannot be known.

(b) Do not reflect the real value of assets: Since assets are recorded on cost basis, the book values shown in the financial statements do not reflect real value of assets.

(c)Fail to reflect changes in price level: Financial Statements are prepared from the records maintained on cost basis. The changes in price level are not considered while preparing these statements.

(d) Timely information not possible: Financial Statements are published after 3-4 months of the closure of accounts. So, in many cases they cannot give timely and relevant information for decision making.

(e) No Qualitative Information: Financial Statements provide only quantitative information and fail to provide key non-financial information like quality and

reputation of the management team and employees, labour relations, quality of work, etc.

(f) Ignores the productivity: Financial Statement ignores the productivity and the skills of the employees in an organization.

(10) Mention the objectives/ advantages/ benefits / importance of Financial Statements.

Answer: Following are the merits of Financial Statements:

(a) Helps Stock Brokers: The financial statements enable the stock brokers to judge the financial position of different concerns and take decisions about the prices to be quoted.

(b) Importance to the Consumers: Consumers use financial statements to safeguard their interest in regard to quality of products , price charged and to uphold the consumer movement.

(c) Basis for Research work: Research scholars make use of financial statements for making analysis and interpretation of data to derive new findings.

(d) Basis for making investment: Information contained in the financial statements is used to judge long-term solvency , profitability , dividend pay out as well as debt servicing capacity of the concern. The prospective investors can make their own decision whether to invest or not to invest in the company on the basis of these information contained in the financial statements.

(e) Basis to judge short term liquidity: Creditors are interested in information which enables them to determine whether amounts owing to them will be paid when due. Therefore, financial statements are important to them as the information on short term liquidity, cash flows, etc can be known from these statements.

(f) Guide to employees: Employees of the company are interested in financial statements in order to assess the stability of their employment, to lodge their claim for hike in wage, share in profit, etc.

(11) Who are the users of Financial Statements? Explain.

Answer: Following are the users of Financial Statements:

(A) Internal Users:

(1) Owners: Owners provide capital to the business and bear all the risk of the business. They want to know whether their funds are being properly utilized or not.

(2) Managers: Accounting information is useful to managers for the purpose of planning , decision making, controlling, motivating , directing and monitoring the functioning of a business entity.

__(3) Employees__: **Employees are interested in financial information in order to assess the stability of their employment, to lodge their claim for hike in wage, share in profit, bonus, etc.**

(B) External Users:

__(1) Creditors__: **Creditors use accounting information to ascertain the short term liquidity, long term liquidity or solvency position, the ability of the entity to repay the amount in scheduled time and the earning capacity.**

__(2) Consumers__: **Consumers use financial information to safeguard their interest in regard to quality of products, price charged and to uphold the consumer movement.**

__(3) Researchers__: **Research Scholars make use of financial statements for making analysis and financial journals also conduct analysis of the financial statements to report the operational result of the business entity.**

__(4) Bankers__: **Bankers who advance money to a business entity are interested in financial statements to ascertain the short term and long term debt repaying and debt servicing capacity of the business entity.**

(12) Distinguish between a Company's balance sheet and the balance sheet of a Partnership Firm.

Answer: Following are the differences between a Company's balance sheet and a partnership balance sheet:

Basis	Company's Balance Sheet	Partnership Balance Sheet
(1) Form	It is prepared in the format prescribed under the Companies Act 2013.	There is no prescribed format for balance sheet of a Partnership Firm.
(2) Easy	It is difficult to prepare.	It is easy to prepare.
(3) Time Involved	It is more time consuming.	It is less time consuming.
(4) Figures for 2 years	Figures of every item in the Balance Sheet of both previous year and current year is required to be shown.	In a Balance Sheet of a Partnership Firm, figures of only current year are shown.
(5) Audit.	The balance sheet of a company is required to be audited and signed by the Chartered Accountant.	Audit of a Partnership Firm's Balance Sheet is not compulsory except under Tax Audit.
(6) Order.	Marshalling of assets and liabilities in a Company's balance sheet is done in order of performance.	There is no prescribed order of marshalling of assets and liabilities in the balance sheet of a Partnership Firm.

(1) What are the provisions as to preparation of financial statements?

Answer: The preparation of financial statements is guided by various provisions and standards depending on the jurisdiction and the nature of the organization. However, some common principles and guidelines are widely followed across different frameworks, such as Generally Accepted Accounting Principles (GAAP) or International Financial Reporting Standards (IFRS). Here are the key provisions typically considered:

1. **Accrual Basis Accounting**: Financial statements are prepared using the accrual basis of accounting, which means transactions are recorded when they occur, not necessarily when the cash changes hands. This ensures a more accurate representation of the financial position and performance of the organization.
2. **Consistency**: Financial statements should be prepared consistently from one period to another to ensure comparability. Changes in accounting policies or methods should be disclosed and justified.
3. **Materiality**: Financial statements should reflect all material items that could influence the economic decisions of users. Materiality is assessed based on the size and nature of the item.
4. **Fair Presentation**: Financial statements should present fairly the financial position, performance, and cash flows of the entity. This involves applying accounting policies consistently and disclosing any relevant information.
5. **Going Concern Assumption**: Financial statements are prepared under the assumption that the entity will continue its operations for the foreseeable future. If this assumption is not valid, appropriate disclosures should be made.
6. **Completeness**: All relevant information should be included in the financial statements. Omissions or misstatements could mislead users.
7. **Comparability**: Financial statements should allow users to compare the entity's financial performance and position over time and with other entities. This requires consistent application of accounting principles and clear disclosure of accounting policies.
8. **Disclosure Requirements**: Financial statements should include all necessary disclosures required by relevant accounting standards or regulations. This may include information about significant accounting policies, estimates, contingent liabilities, related party transactions, and other relevant information.

9. **Consolidation**: If the entity has subsidiaries, the financial statements may need to be consolidated to present the financial position and performance of the group as a whole.
10. **Auditor's Opinion**: For publicly traded companies, the financial statements are typically subject to external audit by independent auditors who provide an opinion on whether the statements are prepared in accordance with applicable accounting standards and provide a true and fair view.

These provisions ensure that financial statements provide relevant, reliable, and comparable information for users to make informed decisions about the entity.

(2) What are the general instructions for preparation of financial statements?

Answer: The preparation of financial statements involves several steps to ensure accuracy and compliance with accounting standards. Here are the general instructions for preparing financial statements:

1. **Gather Financial Data**: Collect all relevant financial data including balance sheet items, income statement items, cash flow statement items, and any other necessary information.
2. **Organize Transactions**: Organize financial transactions according to their nature and classification. Ensure that all transactions are properly recorded and categorized.
3. **Adjust Trial Balance**: Prepare a trial balance by listing all accounts and their balances. Make any necessary adjustments for accruals, prepayments, depreciation, and other adjustments to ensure the trial balance is accurate.
4. **Prepare Financial Statements**:
    - **Income Statement**: Prepare an income statement, also known as a profit and loss statement, which shows the company's revenues, expenses, and net income or loss over a specific period.
    - **Balance Sheet**: Prepare a balance sheet, which presents the company's assets, liabilities, and shareholders' equity at a specific point in time.
    - **Cash Flow Statement**: Prepare a cash flow statement, which shows the cash inflows and outflows from operating, investing, and financing activities during a specific period.
5. **Apply Accounting Standards**: Ensure compliance with relevant accounting standards such as Generally Accepted Accounting Principles (GAAP) or

International Financial Reporting Standards (IFRS), depending on the jurisdiction and reporting requirements.

6. **Disclosures**: Provide adequate disclosures in the financial statements to provide additional information about the company's financial position, performance, and significant accounting policies.
7. **Review and Finalize**: Review the financial statements for accuracy and completeness. Verify that all calculations are correct and that the statements are in accordance with accounting standards. Make any necessary adjustments or corrections.
8. **Approval**: Obtain approval from management, board of directors, or stakeholders, depending on the company's governance structure.
9. **External Audit (Optional)**: If required, engage external auditors to conduct an audit of the financial statements to provide assurance on their accuracy and compliance with accounting standards.
10. **Distribution**: Distribute the financial statements to relevant stakeholders such as shareholders, regulatory authorities, lenders, and other interested parties.
11. **Filing (if applicable)**: File the financial statements with relevant regulatory authorities such as the Securities and Exchange Commission (SEC) in the United States or Companies House in the United Kingdom, depending on the company's legal requirements.
12. **Continuous Monitoring and Updating**: Continuously monitor the company's financial performance and update the financial statements regularly to reflect any changes or developments.

By following these general instructions, companies can ensure the accurate and timely preparation of their financial statements, which are essential for stakeholders to assess the company's financial health and make informed decisions.

(3) What are the different types of financial statements of a company?

Answer: The primary types of financial statements prepared by a company are:

1. **Income Statement (Profit and Loss Statement)**: This statement summarizes the company's revenues, expenses, gains, and losses over a specific period, typically a quarter or a fiscal year. It shows whether the company has made a profit or incurred a loss during the period.

2. **Balance Sheet (Statement of Financial Position)**: This statement provides a snapshot of a company's financial position at a specific point in time, typically the end of a quarter or fiscal year. It lists the company's assets, liabilities, and shareholders' equity, showing how assets are financed through debt or equity.
3. **Cash Flow Statement**: This statement tracks the inflow and outflow of cash and cash equivalents during a specific period, typically a quarter or fiscal year. It categorizes cash flows into operating activities, investing activities, and financing activities, providing insights into how cash is generated and used by the company.
4. **Statement of Changes in Equity (Shareholders' Equity Statement)**: This statement details changes in shareholders' equity over a specific period, typically a quarter or fiscal year. It shows how equity has changed due to net income or loss, dividends, share issuances, share repurchases, and other equity transactions.

Additionally, companies may also prepare supplementary financial statements or disclosures depending on regulatory requirements or to provide additional information to stakeholders. These may include:

5. **Notes to Financial Statements**: These are detailed explanations and additional information accompanying the primary financial statements, providing further insights into accounting policies, assumptions, contingencies, and other relevant details.
6. **Management Discussion and Analysis (MD&A)**: While not technically a financial statement, MD&A is often included in annual reports. It provides management's analysis and commentary on the company's financial performance, operations, risks, and future outlook.

These financial statements together offer a comprehensive view of a company's financial performance, position, and cash flows, aiding investors, creditors, regulators, and other stakeholders in assessing the company's financial health and making informed decisions.