1. Details of Module and its structure

Module Detail	
Subject Name	Accountancy
Course Name	Accountancy 04 (Class XII, Semester – 2)
Module Name/Title	Financial Statements of a Company – Part 2
Module Id	leac_20302
Pre-requisites	Basic knowledge of Financial Statements
Objectives	At the end of the lesson, the learners will be able to: • Explain meaning of Balance Sheet • State the importance of Balance Sheet • State the formula for Balance Sheet • Recall the format of Balance Sheet • Explain the terms of Balance Sheet
Keywords	Balance Sheet, Assets, Liabilities, Shareholder's funds, Schedule III.

2. Development Team

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1.1. Introduction

The financial statements are the end products of accounting process. They are prepared as per the accounting policies and accounting standards prescribed in the Companies Act. The accounting concepts, principles, procedures and also the legal environment in which the business organisations operates are also taken into consideration before their preparation. These statements are the outcome of the summarising process of accounting and are, therefore, the sources of information on the basis of which conclusions are drawn about the profitability and the financial position of a company.

Hence, they need to be arranged in a proper form with suitable contents so that the shareholders and other users of financial statements can easily understand and use them in their economic decisions in a meaningful way.

This module will cover a type of financial statement i.e. Balance Sheet. The practical question on balance sheet will be covered in the next module.

2.1. Meaning of Balance Sheet

The financial details that are prepared by the business enterprisers so as to meet the information requirement of the decision-makers are known as financial statements.

Financial statements are the basic and formal annual reports through which the corporate management communicates financial information to its owners and various other external parties which include investors, tax authorities, government, employees, etc.

Thus, financial statements are written records that convey the business activities and the financial performance of a company. One such type of financial statement is a Balance Sheet.

A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating its capital structure. It is a financial statement that provides a snapshot of what a company owns and owes, as well as the amount invested by shareholders.

Thus, Balance Sheet is required for external reporting and also for internal needs of the management like planning, decision-making and control.

Every company registered under The Companies Act 2013 shall prepare its balance sheet, to harmonise the disclosure requirement as per the schedule III of the companies act 2013 that is with the accounting standards and to converge with new reforms.

3.1. Importance of Balance Sheet

Balance sheet analysis can say many things about a company's achievement. The importance of the balance sheet are:

- Creditors, investors, and other stakeholders use this financial tool to know the financial status of a business.
- It is used to analyse a company's growth by comparing different years.
- While applying for a business loan, a company has to submit a balance sheet to the bank.
- Stakeholders can find out the business accomplishment and liquidity position of a company.
- Company's balance sheet analysis can detect business expansion and future expenses.

4.1 Formula Used for Balance Sheet

Assets=Liabilities + Shareholders' Equity

Thus, a company has to pay for all the things it owns (assets) by either borrowing money (taking on liabilities) or taking it from investors (issuing shareholders' equity).

Assets

Within the assets segment, accounts are listed from top to bottom in order of their liquidity – that is, the ease with which they can be converted into cash. They are divided into:

- Current Assets - They can be converted to cash in one year or less.
- Non-Current or long-term assets - They cannot be converted to cash in one year or less.

Here is the general order of accounts within current assets:

- **Cash and cash equivalents** are the most liquid assets and can include Treasury bills and short-term certificates of deposit, as well as hard currency.
- **Marketable securities** are equity and debt securities for which there is a liquid market.

- **Accounts receivable** refers to money that customers owe the company, perhaps including an allowance for doubtful accounts since a certain proportion of customers can be expected not to pay.
- **Inventory** is goods available for sale, valued at the lower of the cost or market price.
- **Prepaid expenses** represent the value that has already been paid for, such as insurance, advertising contracts or rent.

Long-term assets include the following:

- **Long-term investments** are securities that will not or cannot be liquidated in the next year.
- **Fixed assets** include land, machinery, equipment, buildings and other durable, generally capital-intensive assets.
- **Intangible assets** include non-physical (but still valuable) assets such as intellectual property and goodwill. In general, intangible assets are only listed on the balance sheet if they are acquired, rather than developed in-house. Their value may thus be wildly understated – by not including a globally recognized logo, for example – or just as wildly overstated.

Liabilities

Liabilities are the money that a company owes to outside parties, from bills it has to pay to suppliers to interest on bonds it has issued to creditors to rent, utilities and salaries. They are divided into:

- Current liabilities are those that are due within one year and are listed in order of their due date.
- Long-term liabilities are due at any point after one year.

Current liabilities accounts might include:

- current portion of long-term debt
- bank indebtedness
- interest payable
- wages payable
- customer prepayments
- dividends payable and others
- earned and unearned premiums
- accounts payable

Long-term liabilities can includ

- **Long-term debt**: interest and principal on bonds issued

- **Pension fund liability**: the money a company is required to pay into its employees' retirement accounts
- **Deferred tax liability**: taxes that have been accrued but will not be paid for another year (Besides timing, this figure reconciles differences between requirements for financial reporting and the way tax is assessed, such as depreciation calculations.)

Shareholders' Equity

Shareholders' equity is the money to be given to business' owners, meaning its shareholders. It is also known as "net assets," since it is equivalent to the total assets of a company minus its liabilities, that is, the debt it owes to non-shareholders.

- Retained earnings are the net earnings a company either reinvests in the business or use to pay off debt; the rest is distributed to shareholders in the form of dividends.
- Treasury stock is the stock a company has repurchased. It can be sold at a later date to raise cash.

5.1 Format of Balance Sheet

Balance Sheet as at 31st March, 20....

Particulars	**Note No.**	**Figure as at the end of Current reporting period**	**Figure as at the end of Previous reporting period**
I. EQUITY AND LIABILITIES 1. Shareholder's Funds (a)Share Capital (b)Reserves and Surplus (c) Money received against share warrants 2. Share Application money pending allotment 3. Non-current Liabilities (a) Long term borrowings (b) Deferred tax liabilities (net) (c) Other long term liabilities (d) Long term provisions 4. Current Liabilities (a) Short-term borrowings (b) Trade payables (c) Other current liabilities (d) Short-term provisions			
TOTAL			

II. ASSETS 1. Non-Current Assets (a) Fixed assets • Tangible assets • Intangible assets • Capital work-in-progress • Intangible assets under development (b) Non-current investments (c) Deferred tax assets (net) (d) Long-term loans and advances (e) Other non-current assets 2. Current Assets (a) Current investments (b) Inventories (c) Trade receivables (d) Cash and cash equivalents (e) Short term loans and advances (f) Other current assets			
TOTAL			

5.1.1 Important Features of the above Presentation

1. It applies to all Indian companies preparing financial statement as per Schedule III to the Companies Act, 2013.
2. It does not apply to :
   (i) Insurance or Banking Company
   (ii) Company for which a form of balance sheet or income statement is specified under any other Act.
3. Accounting standards shall prevail over Schedule III of the Companies Act, 2013.
4. Disclosure on the face of the financial statements or in the notes are essential and mandatory.
5. Terms in the revised Schedule III will carry the meaning as defined by the applicable accounting standards.
6. Balance to be maintained between excessive details that may not assist users of financial statements and not providing important information.
7. Current and non-current bifurcation of assets and liabilities is applicable.
8. Rounding off of figures to be reported in the financial statements is mandatory :

(i) Turnover < Rs.100 crore: Nearest hundreds, thousands, lakhs or millions or decimal.

(ii) Turnover > Rs.100 crore: Nearest lakhs or millions or decimal

9. Vertical format for presentation of financial statement is prescribed according to the above format.
10. Debit balance in the statement of profit and loss to be disclosed as negative figure under the head "Surplus".
11. Mandatory disclosure for share application money pending allotment.
12. 'Sundry Debtors' and 'Sundry Creditors' replaced by terms 'Trade Receivables' and 'Trade Payables'.

6.1 Terms used in Balance Sheet

6.1.1 Equity and Liabilities

Equity is the liability towards the shareholders and is termed as 'Shareholders' Funds'

The shareholders' funds are sub-classified in the balance sheet as :

a) Share Capital

b) Reserves and Surplus

c) Money received against Share Warrants

a) Share Capital

It means shares issued by the company for subscription and amount received against issued share capital. The person to whom shares are allotted is called a shareholder. Share Capital includes both Equity Share Capital and Preference Share Capital.

b) Reserve and Surplus

Reserves and Surplus are shown as a single account in the Balance Sheet. It is the amount set aside out of profits and other surpluses to meet future uncertainties. They are created to strengthen the financial position of the company. The following are included in the balance sheet under reserve and surplus :

i) Capital Reserve

ii) Capital Redemption Reserve

iii) Securities Premium Reserve

iv) Debenture Redemption Reserve

v) Revaluation Reserve

vi) Share Options Outstanding Account

vii) Other Reserves (Specifying nature and purpose)

viii) Surplus: Balance in statement of profit and loss; disclosing allocations and Appropriation such as dividend, bonus shares, transfer to/from reserve, etc.

c) Money received against Share Warrants

Share Warrants are the financial instruments which give the holder the right to acquire Equity Shares. They are the financial instruments which will be converted into Equity shares at a later date at a predetermined price.

6.1.2. Share Application money pending allotment

Share Application Money Pending Allotment means the amount received on the application on which allotment is not yet made (pending allotment). The process starts when any company publicly issues its equity shares to raise funds. First, it receives the application money from its applicants and the equity shares are allotted to the respective applicants on a later date.

6.1.3. Non-current Liabilities

Noncurrent liabilities, also called long-term liabilities or long-term debts, are long-term financial obligations listed on a company's balance sheet. These liabilities have obligations that become due beyond twelve months in the future, as opposed to current liabilities which are short-term debts with maturity dates within the following twelve month period**. They are classified as:**

(a) Long term borrowings
(b) Deferred tax liabilities (net)
(c) Other long term liabilities
(d) Long term provisions

(a) Long term Borrowings and other long term liabilities:

Total borrowings are categorised into long-term borrowings, short-term borrowings and current maturities to long-term debt.

(i) Loans which are repayable in more than twelve months/operating cycle are classified as long-term borrowings on the face of balance sheet.

(ii) Loans repayable on demand or whose original tenure is not more than twelve months/operating cycle are classified as short-term borrowings on the face of balance sheet.

(iii) Current maturities to long-term loan include amount repayable within twelve months/operating cycle under other current liabilities with Note to Account.

Long term borrowings are shown under the following heads:

1. Debentures
2. Bonds
3. Public Deposits
4. Loans from Banks or other parties

(b) Deferred tax liabilities (net)

A deferred tax liability occurs when a business has a certain amount of income for an accounting period and that amount is different from the taxable amount on their tax return. When the amount is less than the estimated tax, an entry is placed on the balance sheet in the form of a liability.

Deferred tax typically refers to liabilities, wherein the amount entered on the balance sheet is payable at a future time. **For e.g.**

Company XYZ owns machinery that is classified as an asset. They choose to use a certain depreciation method - in this case, an accelerated method that allows higher deductions earlier in ownership of the asset and lower deductions.

This differs from the slower, straight-line depreciation that is used by tax authorities, which means the depreciation is spread evenly over the useful life of the asset. The depreciation method affects how much the charges will be for each accounting period. Because the depreciation method chosen by Company XYZ would result in at first a larger deduction than the method used by tax authorities, their income would be higher than what would be considered the taxable income. In this case, the temporary difference would be added as a liability to the balance sheet.

(c) Long term provisions

Long term provisions are usually money set aside for employee benefits such as gratuity; leave encashment, provident funds etc.

6.1.4. Current Liabilities

Current liabilities are a company's obligations which are expected to be settled within 365 days (less than 1 year). The term 'Current' is used to indicate that the obligation is going to be settled soon, within a year. Going by that 'non-current' clearly means obligations that extend beyond 365 days.

For e.g. - if you buy a mobile phone on EMI (via a credit card) you obviously plan to repay your credit card company within a few months. This becomes your 'current liability'. However if you buy an apartment by seeking a 15 year home loan from a housing finance company, it becomes your 'non-current liability'.

The following are included in current liabilities:

(a) Short-term borrowings

These are short term obligations of the company usually undertaken by the company to meet day to day cash requirements (also called working capital requirements).

(b) Trade payables

Trade Payable also called account payable or bills payable. These are obligations payable to vendors who supply to the company. The vendors could be raw material suppliers, utility companies providing services, stationary companies etc.

(c) Other current liabilities

They are obligations associated with the statutory requirements and obligations that are not directly related to the operations of the company.

(d) Short term provisions

Short term provisions is quite similar to long term provisions, both of which deals with setting aside funds for employee benefits such as gratuity, leave encashment, provident funds etc.

6.1.5. Non-Current Assets

Non- current assets includes fixed assets both tangible and intangible assets. We are already aware about them. Another non-current asset is Capital work in progress that is a new concept that you read about now.

Capital Work In Progress includes building under construction, machinery under assembly etc at the time of preparing the balance sheet. Hence it is aptly called the "Capital Work in Progress".

The last line item is 'Intangible assets under development'. This is similar to CWIP but for intangible assets. The work in process could be patent filing, copyright filing, brand development etc.

Non- Current Investments could be – buying listed equity shares, minority stake in other companies, debentures, mutual funds etc.

Long-term loans and advances are given out by the company to other group companies, employees, suppliers, vendors etc.

6.1.6 Current Assets

Current assets are the assets that a company uses to fund its day to day operations and ongoing expenses. And, the balance sheet includes the following -

(a) Current investments
(b) Inventories
(c) Trade receivables
(d) Cash and cash equivalents
(e) Short term loans and advances
(f) Other current assets

Thus, the balance sheet includes the above mentioned components. We will discuss practical questions in the next module.

Summary

The financial details that are prepared by the business enterprisers so as to meet the information requirement of the decision-makers are known as financial statements. These statements provide financial data that require analysis, comparison and interpretation for taking decision by the external as well as internal users of accounting information.

Financial statements includes: Cash Flow statement, Statement of Profit and Loss and Balance Sheet.

A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating its capital structure. It is a financial statement that provides a snapshot of what a company owns and owes, as well as the amount invested by shareholders. Thus, Balance Sheet is required for external reporting and also for internal needs of the management like planning, decision-making and control

Every company registered under The Companies Act 2013 shall prepare its balance sheet, to harmonise the disclosure requirement as per the schedule III of the companies' act 2013 that is with the accounting standards and to converge with new reforms.

Assets=Liabilities + Shareholders' Equity

Thus, a company has to pay for all the things it owns (assets) by either borrowing money (taking on liabilities) or taking it from investors (issuing shareholders' equity).

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