Financial Accounting
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Lecture – 04
Balance Sheet 2

Namaste, welcome to the 4th session of our Financial Accounting course; I hope you have enjoyed first three sessions and first session 1 and 2 where very much introductory. We had just started what is financial accounting, then we went to understand financial statements particularly the starting point of balance sheet which we saw how it gets emerged from business cycle, we also discussed about what is there.

In the annual report in the last session we had started a little detailed discussion of balance sheet. So, I will just go back to the formats which we have seen, those of who have first time seen the balance sheet this was the short format at one glance to understand what is a balance sheet.

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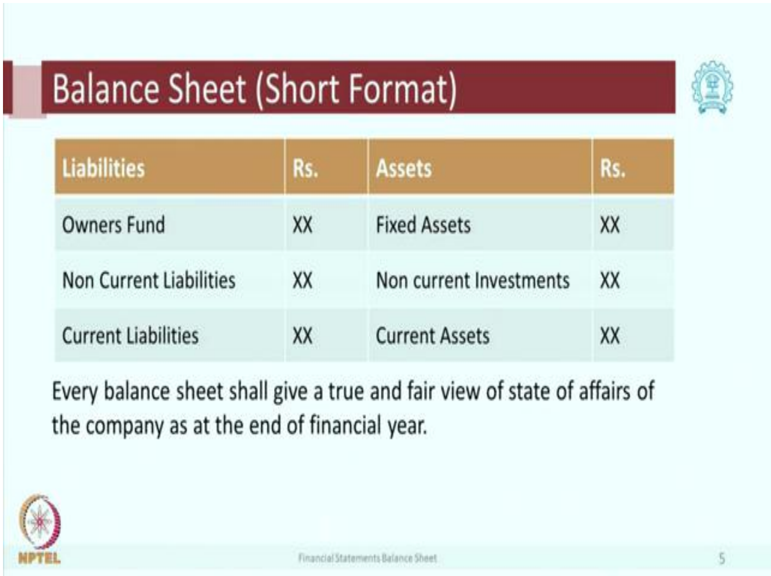

On one side we have got assets which provide a list of all the resources with the enterprise, on the other side we have got liabilities. So, liabilities are giving you the providers for the resources or there are internal people like owners who have given us owners funds, there are external people like banks who have given us external liabilities both are listed under the head liabilities.

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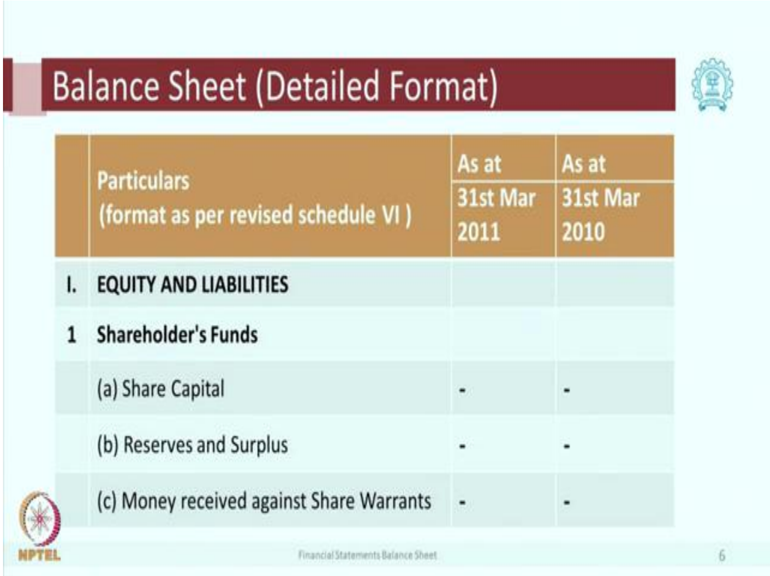

	Particulars (format as per revised schedule VI)	As at 31st Mar 2011	As at 31st Mar 2010
I.	**EQUITY AND LIABILITIES**		
1	**Shareholder's Funds**		
	(a) Share Capital	-	-
	(b) Reserves and Surplus	-	-
	(c) Money received against Share Warrants	-	-

After this we had started discussion on format as per schedule VI, now few of you may be wondering what is the schedule VI mean. Now, schedule six is a schedule under companies act. So, for all the companies the balance sheet is to be prepared as per this format. Now, under schedule VI the first item not the first part is I refers to equity and liabilities that is what we are discuss in the last session, under that you have got 1 that is shareholders funds I hope you have understood it. If you have a doubt in anything not only here, but even of the earlier items please feel free to discuss it on discussion forums. So, the team from IIT we would like to respond to all your queries please be responsive discuss a lot on your discussion forum.

As I have told you earlier I hope you have decided about your company, download the annual report of that company look at the balance sheet; as we are studying a particular financial statement please look at the balance sheet of your company. And, any doubts you have you can discuss with your classmates you can also discuss and ask it on to IIT team we will be responding to each and every question from your side ok. So, under item number 1 there are three sub items share capital, reserves and surplus and money received against share warrant.

So, capital share capital is a money which is put in by the owners, reserves and surplus refers to the profits which are ploughed in; c refers to the money which is collected from certain people and in future they will receive shares, so far they have not received any shares such money is shown as money received against share warrant. In item number 2 share application money pending allotment this is also similar; the prospective investors have paid me some money, shares are to be issued to them but are not yet issued, till that time the money is shown under item number 2 that is share application money pending allotment. Once they are allotted it will go in 1 if they are not allotted it will be refunded that is the item number 2.

Item number 3 is non-current liabilities again you have got four items a are long term borrowings. So, these are the loans taken for more than 1 year, b is deferred tax liability. Now, this is a tax liability the amount which is to be paid as tax, but not in the current year it will be paid after 2, 3, 4 years due to certain provisions under tax laws. They are differed tax liabilities later on we are going to discuss how they are calculated, but once we complete our balance sheet.

c is other long term liabilities, so other than a and b if there are deposits received for more than 1 year or if there are some salaries which are unpaid for a longer period they are all shown under other long current long term liabilities, then 3D is long term provisions. So, provisions are those items in liabilities of which the amount is not known with substantial accuracy. So, a provision is created and it is shown under 3D especially if it is for more than 1 year.

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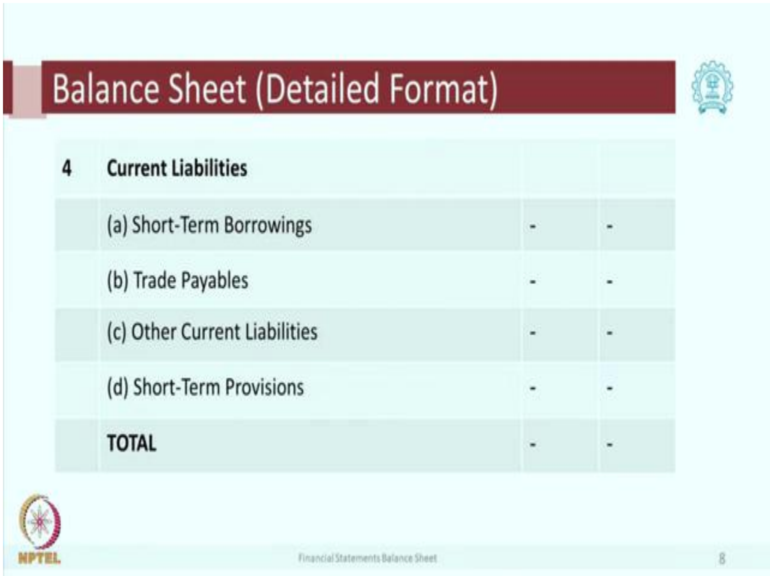

The next one which discussed was item number 4 in item number 4 a, then item number 4 where current liabilities as the name suggest these are for less than 1 year. So, 4 a is short term borrowings, so loans taken for less than 1 year 4 b we are trade payables. So, these are various purchases made, but we have not yet paid related to our regular business, so they are called as trade payables. 4 c are any other current liabilities like do you remember any examples we are discussed outstanding salaries or outstanding electricity bills or outstanding office expenses outstanding stationary charges.

So, on any expense which is not yet paid, but is payable in 1 year that is other current liabilities. 4 d are short term provisions, so again estimated liabilities which are payable in short term. So, in our last session we had come up to item 4 this was a quick revision I am taking revision every time especially in the earlier sessions but, I hope you are attentive and you have understood whatever we have discuss till now.

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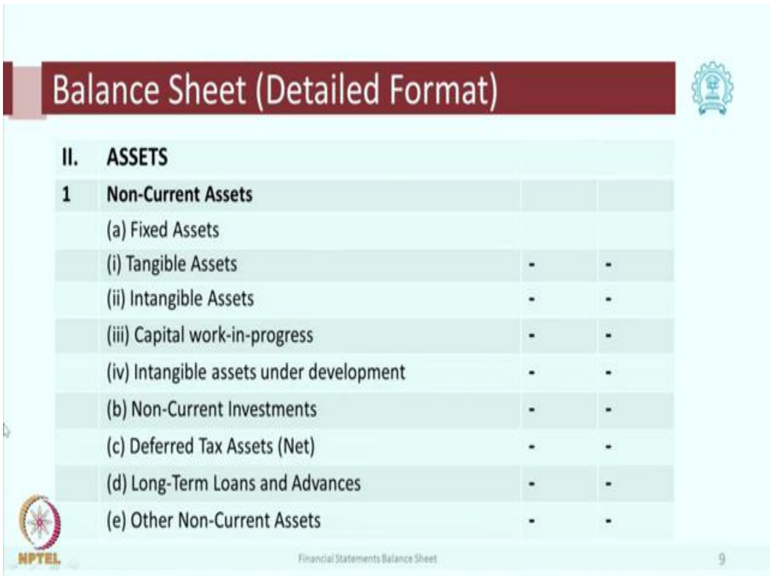

Now, let us go to the II part of balance sheet that is known as assets. So, these are the properties or these are the resources which are available with the enterprise in two again the item number 1 is noncurrent asset as the name suggests noncurrent means it is for more than 1 year or you can also call it as a long term in that you have got a; a refers to fixed assets. In a again we have got a small i and ii, so a 1 is tangible assets a 2 is intangible assets.

In our second session we are discussed what is a fixed asset I hope you remember. So, fixed assets refer to the infrastructure of the undertaking, it refers to those assets which are used for running the business cycle they themselves do not take part in business cycle, they do not get converted, but they support the money cycle. So, which are such items?

For example, we have got land, we may have a building, we may have a machinery, we may have vehicles they are with us for a longer period, they help us in doing business or they help us in doing our regular activities, but they are themselves or not getting converted, so it is not a stock ok. So, these are fixed assets they are of two types one is tangible the other is intangible.

Tangible means that can be touched, that has physically existence. So, all the examples which we discussed like land building vehicles these are all tangible second one are intangibles, they have no physical existence and cannot be touched, but they have a value. So, what are such assets can you think of any example? I think all of you use computers we can see the computer screen and the other parts that is all your hardware, but computer also has some software built into it that software you cannot touch or you cannot feel it but you can see its impact that is an example of intangible asset.

Can you think of any other example? There are patents, there are copyrights, there are trademarks these all are rights of the company or rights of the owner, but not of physical in nature it is a intellectual property all these are examples of intangible fixed assets. This is an era aware intangible assets are becoming more important than tangible assets say 100 years before tangible assets were very important. So, large companies like ford or general motors or general electric wire big companies.

Today which are the big company's? I think all of you know now it is Google, it is Facebook it is, Microsoft do they have physical assets of course, they have little bit, but most of their assets are intangible in nature anyway this was just for discussion in general for any company there will be some tangible assets some intangible assets through be shown under a 1 and 2, a 3 is capital work in progress.

Now, what is meant by work in progress? That means, some work is going on something which is under construction, capital because it's a long term. So, suppose building is under construction once it is ready then we will call it as a tangible fixed asset, right now the building is not ready, but some work is on we have spent some money and suppose it will take three years to complete. So, as of now I cannot show it is a building or as a tangible asset neither I can show the money paid just as an advanced because some work is already happened that is why it is shown as a capital work in progress.

The fourth one is intangible assets under development. Now, what is this? Just like capital work in progress lot of intangible assets are being created or being developed, but still they are not ready like you have applied for patent, but patent is not yet sanctioned, but you have already spend lot of amount on research, then that will be a intangible asset under development or for example, you are developing some software development testing has not happened.

So, it is not in the ready stage for use, but cost has been incurred in the development process that will be shown as intangible asset under development. Now, when you studied your company's balance sheet for last two three years please try to look at item 3 and 4 carefully because, this year suppose it is under construction or under development next year it will be ready. And, it would have gone into tangible or intangible asset right because we expect in 1 or 2 years the work will be completed and it will be classified either as tangible or intangible.

Suppose a particular item is shown as under construction for a long period 2, 3, 4 years, then we will have a doubt as to why that item is not getting ready, is it a fraud to show that item or there are genuine problems; if non-completing it of course, we cannot conclude anything right away. But, I am just saying that you can just look at the details of item 3 and 4 and say that these items are stagnant or they are getting ready and new items are by being newly constructed ok.

Now, this a that is fixed assets as 1, 2, 3, 4 the total of that is considered as a total of fixed assets. Now, the second item that is 1 b is non current investment, in our last to last session we are discussed a bit about what is an investment, do you remember? So, if you put in some money outside your business it is called as a investment within your own business if you construct a building construct or purchase stock purchase that is not an investment; investment means you have to give it money to some other company or somewhere else. So, can you give any examples of investments?

So, for example, shares for example, bank deposits for examples units of mutual fund if you invest money with some other company or with the bank then it is a investment if that investment is done for more than 1 year it will be shown under 1 bs non-current investment. Some of you may be interested in finance in future you might be wanting to do career in finance you would have heard of terms like portfolio management or stock market whatever the money you are putting in there that is all under 1 b.

And there is a science of how that is managed, how do you invest, when do you buy, when do you sell all those things are studied under portfolio management of course, right now will not going to it, but what portfolio they have your company has you can see from 1 b. So, when you go to balance sheet of your company have a look at 1 b to understand what type of investments they are making.

Now, go to 1 c that is deferred tax asset if you remember in the last session and even in the beginning of today's session we discussed about deferred tax liability. Now, deferred means something which is not due today or in the current year which is due in later years, if it is a liability it will be shown as a deferred tax liability this is a deferred tax asset.

So, today you will not get the benefit of it you will get it after two three years, then it is called as a deferred tax asset. Does it mean after three years government will pay you tax? Of course, no government pays us tax, but government gives you some benefits which you can use after 2 years, after 3 years benefit of remission of tax or reduction of tax that is called as a deferred tax asset. Exactly what is this item we will discuss later on, but if there is any such asset in existence it will be shown under 1 c ok.

Now, the next item is d long term loans and advances. Now, what do you mean by loans and advances? Loan is of two types; one, the company has taken loan, then it will be shown as a borrowing under the liabilities we have seen it in the last session, but suppose company gives loan, then to distinguish it from normal loans we will call it as loan and advance. So, if company gives loan to somebody or advance to somebody it is considered as a loans and advances.

So, in future if you see the word loan and advance always keep in mind that it is an asset item if there is only loan then it is a liability, if it is a loan and advance there is a hint to you that it is an asset ok. Now, since this is for a longer period we are showing it as a long term loans and advance. What can be an example? For example, suppose company gives advance to employee to purchase new house, now the housing advance will obviously not be for one year only, it may be for 5 years, ten years, 15 years, then it will be shown as a long term loan and advance.

It can also be a loan or advance given to some supplier for two three years let us say supplier wants to buy a new machinery. So, we will give some loan to be repaid after 3 years, then it will be shown as a long term loan and advance. Then 1 e other noncurrent assets, so apart from abcd if there is any other long term asset then it will be shown as a other noncurrent asset ok. So, under item 1 we have discussed whole of long term assets.

Now, let us go to second, so in assets we have got one as noncurrent, two as current I think you all know the definition these are all going to mature or which are going to be liquidated or converted within a period of 1 year. If you remember in our session 1 we have seen the business cycle. So, in a business cycle mostly it is a exchange of fixed assets noncurrent assets we will discuss or we will deal in them only after two three years, four years, five years, but current assets' transactions take place every moment, they are continuously being exchanged.

So, under 2 1 we have got current investments I think you remember what is an investment. So, we put money outside our business it is called investment, for example, if we have a three-month bank FD, then it will be shown as a current investment or if we invest in shares and sell them after two months, then it will be a current investment ok, then 2 b is inventories.

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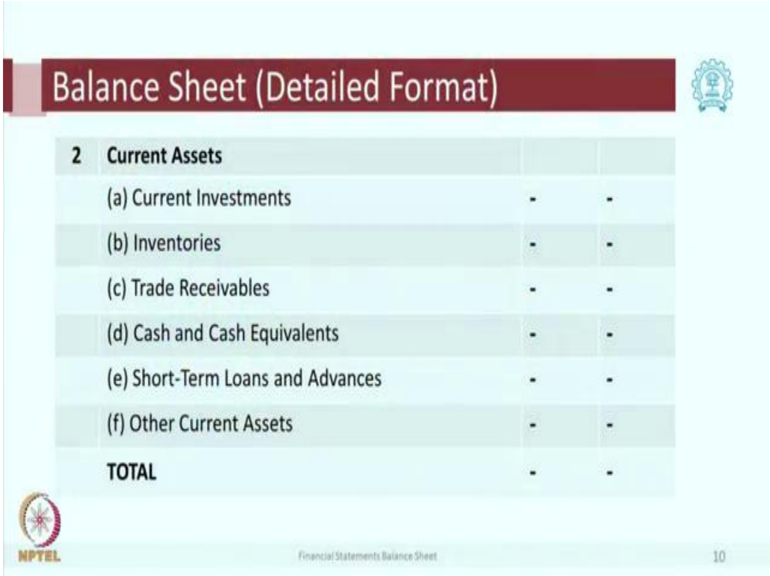

Now, what do you understand by inventory? The other name for it is stocks we might have some raw material that are converted to finished goods or we can purchase finished goods all this taken together are known as inventories. So, these are items which are meant to be converted or sold in our normal course of business which will be shown under 2 b c is trade payables sorry trade receivables we have already seen trade payables under liability. What is a trade receivable?.

In B2B business normally when we sell the goods across the counter we do not get the payment immediately, we will sell the goods, we will send the bill after 15 days, 1 month, 2 month customer will make the payment. So, till the time the money is received it is called as a trade receivable. In other words whenever we make a credit sale till the time we do not get the payment the sale amount will be shown as a trade receivable, the world trade shows that it's a day to day activities, it is a regular business activity relating to or creating a receivable for me it will be called as a trade receivable 2 c. Now 2 d cash and cash equivalent I think everybody understand cash, everybody likes cash because it is very easy to spend. What is the cash equivalent?

There are items which are almost like cash; they can be very easily converted into cash, so they are called as cash equivalents. Later on we are going to study cash flow statement if you remember that is a third statement, when we study cash flow we will go into details about what is cash and cash equivalent, but right now you can just assume it that its more or less like a cash. Now e that is short term loans and advances we have just discussed loans and advance I hope you remember. So, these are the loans given by the entity, so when we give loan to employee or to other company or advance to somebody, all that is under the head loans and advances.

So, under that if there for less than 1 year we will call it as a short term loans and advance, 2 f other current assets. So, a to e if there is a particular item which is of short term in nature, but we does not fit in a to e it will be shown under f as other current assets I hope you have got what is an asset. So, it is a total of 1 plus 2 simple if it is more than 1 year the it is non-current if less than 1 year then it is current. So, we get here the total of assets some of you might have many queries do not worry we are going to again discuss the assets taking each asset we will discuss it in detail right now let us go ahead.

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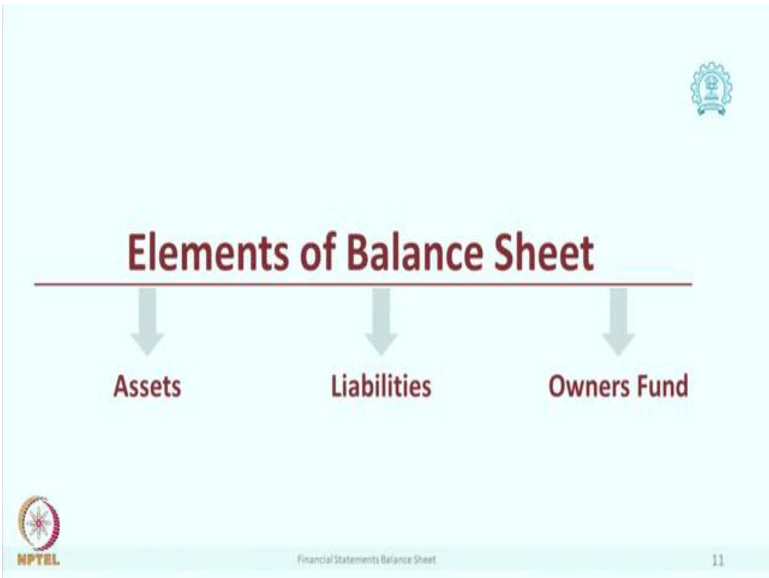

So, if you look at the elements of balance sheet there are three parts one is a asset then it is funded by a liability here I mean a external liability or by the owners which is called as owners fund. Now, let us go into detail of each item. So, how do you define an asset?

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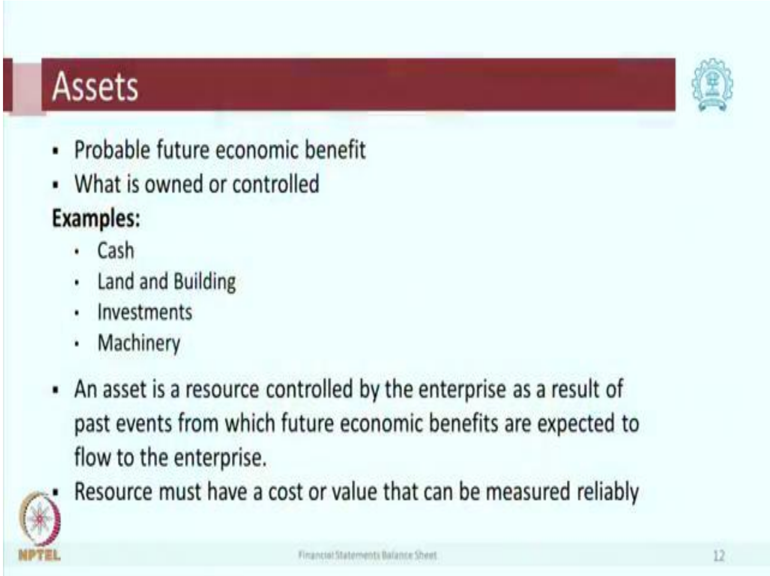

This is a probable future economic benefit what is owned or controlled. So, there are two conditions to be satisfied to be called an asset; one, the item should have an economic value and two, the item should be owned. If you remember on day 1, the first session I had told you that a particular asset does not come in balance sheet because it does not satisfy condition number 2 do you remember that item that item is a human asset, the employee, scientist, managers, executives working with the company actually they are very important asset to the entity, but that cannot be shown in the balance sheet because look at the definition it should have a probable economic value which they have, but it should also be owned or control.

So, employees are not our slaves they are not owned by the company, so they cannot be shown as owned assets that is why human assets you would not see in the balance sheet. Now, any other assets first of all you have to see whether it's a it meets this two conditions I think examples you are all aware cash, land, building, investment, machinery think of another 10 examples and I think you can include it in your assignment.

Now, again the definition is given that it is a resource controlled by the enterprise as a result of some past event, but it should have a future value. The second point is resources must have a cost or value that can be measured reliably, if we have an asset that has some value but there is no reliable estimation available, then also we cannot value it and show it in the balance sheet.

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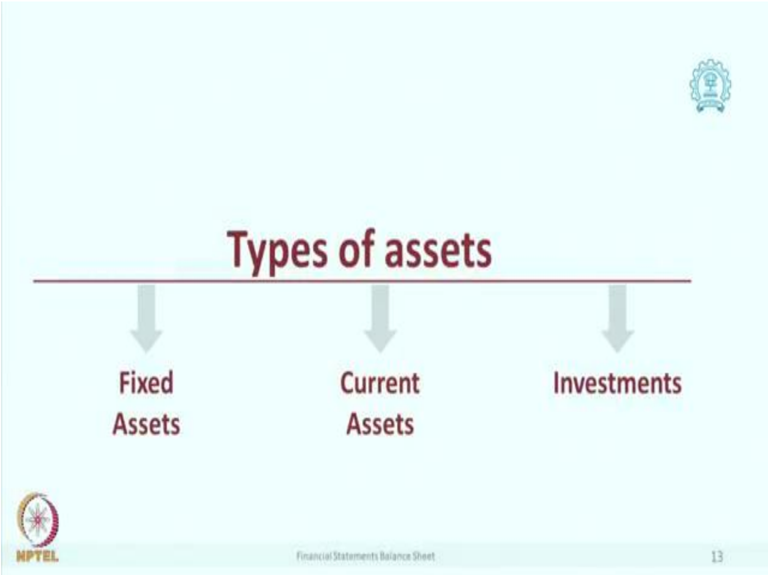

Now, the types of assets we have got fixed assets, current assets and investments. I think with this we will stop here we have already discussed it when we discuss the balance sheet, but we will take up each item now individually and will explain it in detail. But, till that time as I have told you please go to the balance sheet of your company and look at what assets they have, then only you will really have a real type of learning Namaste.