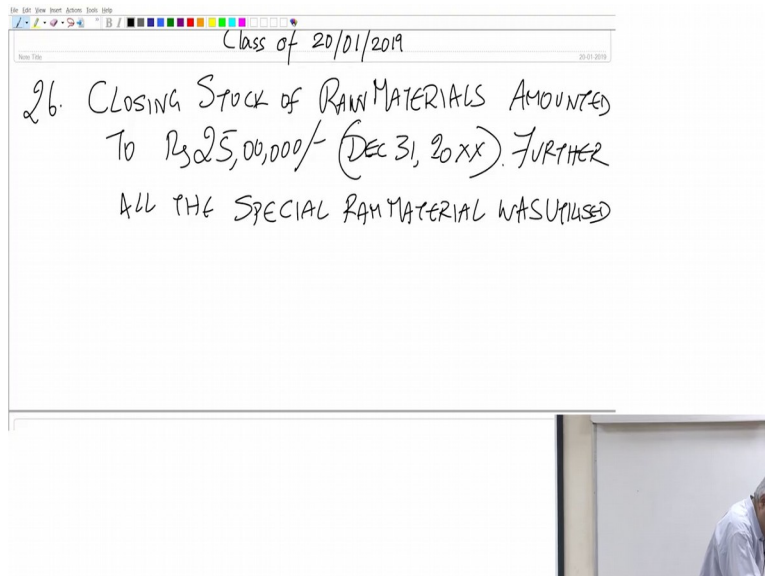


Decision making using financial accounting
Prof. Arun Kumar G
Department of Management Studies
Indian Institute of Technology, Madras

Lecture - 10
Transaction and Financial Statement

(Refer Slide Time: 00:18)



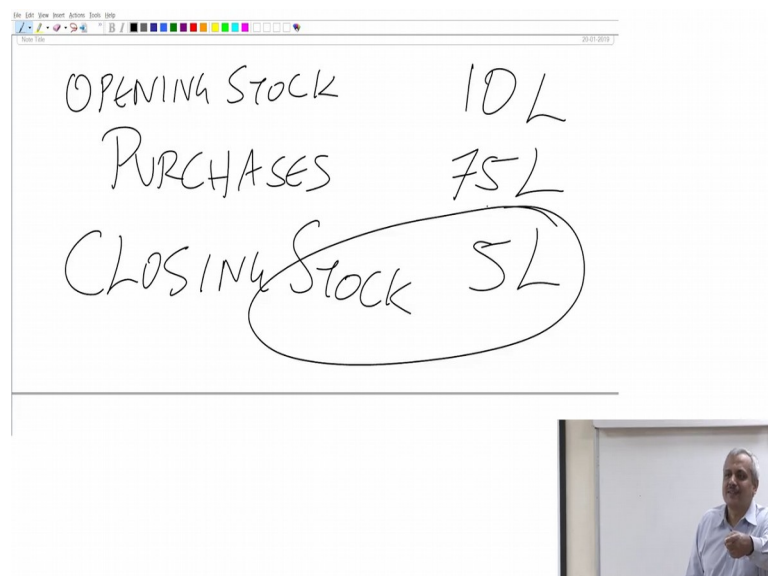
A screenshot of a digital whiteboard interface. The title bar reads "Class of 20/01/2019". The main content area contains the following handwritten text:

26. CLOSING STOCK OF RAW MATERIALS AMOUNTED TO Rs 25,00,000/- (DEC 31, 20XX). FURTHER ALL THE SPECIAL RAW MATERIAL WAS USED

Below the whiteboard, a small video inset shows a man in a light blue shirt, likely the professor, looking towards the screen.

Let me take the example out here just move to shift the screen. Now let us look at it this way. Suppose I am just going to take some numbers out there.

(Refer Slide Time: 00:28)



A screenshot of a digital whiteboard interface. The main content area contains the following handwritten text:

OPENING STOCK	10L
PURCHASES	75L
CLOSING STOCK	5L

The "CLOSING STOCK 5L" entry is circled in black. Below the whiteboard, a small video inset shows the same man in a light blue shirt, pointing towards the screen.

I have when I start that here I have a opening stock worth about 10 lakhs. During the year I make purchases worth about 75 lakhs, there is at the end of the year there is what is called as a closing stock which is worth about 5 lakhs; that means, what has happened? Materials that is available for me for this year production is 75 plus 10 85 lakhs, I may with your not?

Student: Yes sir.

What is the amount of material that I have utilized? Say 85 minus 5 which is still remaining; 80 lakhs is what I have utilized that is what will go in to their?

Student: Expenditure.

Expenditure side and these 5 lakhs will what appear in your closing balance sheet in the asset side. Am I with you in this?

Student: Yes sir. Now it is clear.

Now it is clear, beautiful, go to the excel.

(Refer Slide Time: 01:23)

	Current Assets	Current Liabilities
bank account	1,20,82,980	Creditors for spcl raw mat
cash	6,00,000	creditors
Spcl raw mat		Maintenance O/s
Raw mat inventory	25,00,000	Fuel bill O/s
Debtors	29,29,680	Pack charges O/s
Int Accrued	1,00,000	
		Deb int O/s
Div Rec	10,50,000	
Misc Exp		
Unamortized advt exp	28,12,500	
Prelim exp Unamortized	40,50,000	
Total Assets	5,08,10,160	Total Liabilities
		5,08,10,160
		Total Incon



(Refer Slide Time: 01:38)

	E	F	G	H	I	J	K
13 Long term liabilities						Fuel	3,50,000
14 M. Loan		95,00,000				Carriage inwards	2,00,000
15 8% debentures (200,000)		2,00,00,000				Dist (Carriage out)	4,00,000
16 Loan		45,00,000				Pack charges	7,00,000
17 Liab for vec		38,00,000				Int Exp	2,50,000
18						dep	20,15,000
19 Current Liabilities						Partner sal	2,00,000
20 Creditors for spcl raw mat		-				Deb int	16,00,000
21 creditors		16,90,200				employee benefits	7,15,000
22 Maintenance O/s		2,70,000				Stock of Spcl rm used	30,00,000
23 Fuel bill O/s						RM	1,04,58,200
24 Pack charges O/s							
25							
26							
27 Deb int O/s		16,00,000					
28							
29							

Clear this part of it? I have utilized the raw material. So, I have written out there raw material 25 lakhs beautiful everything you have written out here, in the expenditure, go to the expenditure, go to the expenditure have you written out there fine that part.

(Refer Slide Time: 01:47)

	E	F	G	H	I	J	K
28							
29							
30							
31							
32 Total Liabilities		5,08,10,160		Total income	21095660	Total expense	2,31,45,700
33		1,04,58,200					
34						Profit Before tax	-20,50,040
35						Tax	0
36						Profit after tax	-20,50,040
37						Dividend	
38						Retained Earnings	-20,50,040
39							
40							
41							
42							
43							
44							

Now, you go to the profit. Profit is now go further down enough thank you. Profit before tax is so, much, 20 percent of it is taxes; where 20 percent of its taxes that is assume that is obviously, paid because it is to be paid in advance. So, that part of it whatever 4,10,008 will get reduced from your.

Student: Bank account.

Will get reduce some your what a bank account out there, have you done that?

Student: It's showing loss sir.

Where is it showing loss?

Student: Minus.

Where is it?

Student: (Refer Time: 02:15).

So, when it showing loss there is a is there tax?

Student: (Refer Time: 02:21).

There is no tax out there purposely showing a loss perfectly all right. So, tax is 0 in that particular case obviously.

Student: Sir how can you declare dividend on loss?

For me?

Student: How can you declare dividend?

You can there is possibility see that is what I am trying to say. You can, it is not because what happens is, most of the time I may not have what is called as cash loss I may not have a cash loss, I may not have a cash loss you could possibly declare because if you look at the classic case was reliance long back then they started reliance petroleum that, the IPO when the add in IPO collected money before even they could get an inch of land that declared enough amount of dividend.

Because so, much of money I have invested it is earning something and expenditures are there a lot of expenditures are there to leave a good taste I can also because in anticipation of the profits also I can give dividend out there in anticipation of the profits also I can give dividends. It is not necessary that only when you make a profit you have to give dividend number 1, number 2 it is not necessary that every time you make a profit you

are going to give dividend and in this particular case that is why I have carefully added the statement, you read the statement it says 50 percent of the profit was declared as dividend. In this case have you made a profit?

Student: No.

So, can you declare a dividend? That is why I have carefully termed it that way. I carefully ensure that I have termed it 50 percent of the profit I am not given an absolute figure. I have clearly 50 percent of profit is given as dividend. Now in this case I made a loss no dividend. So, go to your capital out here.

(Refer Slide Time: 03:58)

Assets		Liabilities & Equity		Income
Fixed Assets		Shareholder's funds		
Gross Value building		95,00,000	12,00,000	Disc receiv consulting
Less: Dep		-9,50,000	Drawings by partners	Sales
Net Value of building	85,50,000			
Plant		45,00,000	P&L	Reimburse
less: dep		-2,25,000	NET WORTH	Dividend
Net value of plant	42,75,000			Int Accrue
Cars, vech		42,00,000		
less:dep		-8,40,000		
Net value of Vech	33,60,000			
Long term Investments		Long term liabilities		
Bond 6%		50,00,000	M. Loan	95,00,000
Equity inv in subsidiary		35,00,000	8% debentures (200,000)	2,00,00,000
			Loan	45,00,000
			Liab for vec	38,00,000

Now, what is happening? Your P & L basically the entire loss is born by the capital providers, the capital providers are given 1.2 crores as capital equity out there. What is it worth now? It is worth only about 94 lakhs.

With you on this, I have not taken any dividend, I have not taken any taxes because there is no tax that has been paid also that is one of the reason this statement was not there. Am I with you on this? So, if you look at your asset and liability side of the balance sheet hopefully it balances fine he is taken care of it he has done some gimmick and taken care of it.

Any way land component is land component whatever is a original cost of the purchase of the land that is what will shown unless it is there is no depreciation; obviously,. So, that is what you will basically record it is as one second am I with you.

Student: Yes sir what are (Refer Time: 04:52).

Sir the day on which the company own this the entity owns it, it becomes the property of the entity inherited not inherited we do not care.

Student: Yeah that is fine.

Student: Then the (Refer Time: 04:59).

What is the.

Student: (Refer Time: 05:03).

Move on to you are getting that somebody gifting you land, they are not giving you cash they are giving it you in the form of land value of the land will become part of your receipt out there.

Student: Obviously.

Value of the land will become part of your receipt; obviously, right that is receipt in the sense what? If he has given land is a form of capital then what happens? If he has joined I have joined as a partner I am not bringing cash I am giving you land then what happens? It gets my capital. If somebody has donated land to you then what happens? Then it is a value of the land is a receipt for you.

Student: Sir (Refer Time: 05:42) then the mean by (Refer Time: 05:43).

There are two aspects. Now there is I join your business as a partner I am not bringing any cash in the form of in the form of capital, I am not bringing any cash I am bringing a piece of land. So, what happens? Land is an asset when somebody contributes capital what happens?

There is capital on the as a share holders equity plus liability and there is cash component. In this case is since I am bring the value of the land value of the land will be the asset and my capital will be equal to the value of the land what I have contributed. I have

not contributed cash I brought it in kind that is all right. Somebody has donated land to you now when somebody has donated land to you value of the land will be an asset, that donation what you have received its a receipt it is what is called as an income, it is a what is called as a revenue for you; obviously, right not profit I mean a income. It is a receipt for you. Am I with you sir? Now you are question on the building.

Student: Now the net value of (Refer Time: 06:46) what he ask.

That part has cleared.

Student: Second is net value of building become a new gross value next year?

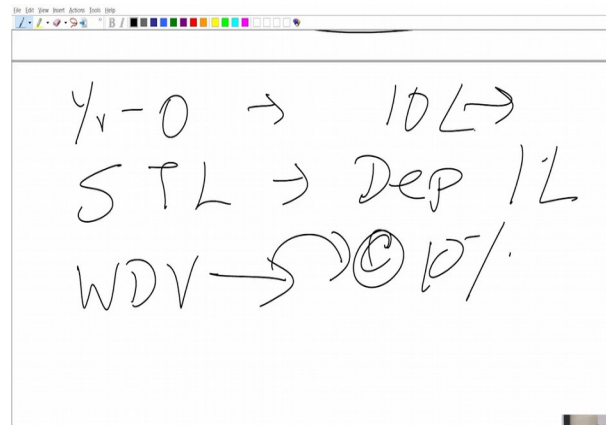
No gross value always remains the original value. Next year what happens? Go to the building thank you. Next year what happens? I will show three columns gross value of the building whatever amount, accumulated depreciation this amount, depreciation for the year further amount.

Student: And do we have to stop at 0?

You need not stop if for example, I have a plant and machinery and that machinery as a scrape value of 30000, then I stop at when it reaches 3000 out there. That is depreciation you decide depreciation over a period of 10 years, 5 years whatever it is. There are two methods of depreciation now that I start a talking about depreciation. One we call it as a straight line method, other what we normally call it WDV method Written Down Value method or reducing balancing method very simple you do not know write it down you can just remember it. Reducing balance method or written down value method supposing I having a asset.

Switch the screen.

(Refer Slide Time: 08:11)



I have an asset out there the value of the asset at the time of purchase that is here 0 is about 10 lakhs. Now I say value of the asset is 10 lakhs I use it for 10 years depreciation for 10 years now what I say straight line method I depreciate at the rate of 1 lakh per year assuming there is no scrap value and what is called as a WDV method written down value method there is certain difference out there, in a written down value method I will say depreciation at the rate of 10 at the rate of 10 percent every year. When I say 10 percent every year first year what is the depreciation? 10 percent of 10 lakhs 1 lakh.

Second year what is the value of the machinery beginning of the second year? The value of the machinery is only 9 lakhs what is the depreciation? 10 percent of that 9 lakhs second year depreciation is 90,000 third year what is the value of the machinery at the beginning? 8.1 lakh what is the value of the depreciation? 81,000 10 percent of that. So, that what happens? Reducing balance on that reducing balance every year you are calculating the depreciation of 10 percent.

So, in that case for the asset to reach the value of 0 would basically keep on infinity or near all most infinity out there. These are the two basic methods of depreciation which your tax laws allows you to follow that is all. There are few other methods we are even touching upon all that am I with you on this? This gives you a fair idea about P & L and balance sheet a P & L and balance sheet. Tomorrow in your organization when one of your accounting or finance colleagues comes and throws terms on some terms of balance

sheet and P & L you are not going to get scared that is the first thing. We are not going to get scared you are going to stand up and say yes I am going to face it kind of a staff at least you may not solve it that is ok, but at least you do not get scared day one that is the basic purpose what we intend to achieve at the end of three classes I may with you on this.

Student: Yes.

Yes sir.

Student: For any expenditure included in the P & L. You are reduced to a asset side.

Student: But the we are not touching anything in liability side how asset and liability?

If there is a what is called a as we are not touching on anything on liability what is happening? The result and profit is getting added where the result and profit is getting its basically resultant profit after the income is effecting only the. See let us take a very simple sir examples; sir I receive an income of 50000 in cash what happens income of 50000 goes up? Cash of 50000 goes up on the asset side. I make an expenditure of 25000. Expenditure goes down by 25,000 I write 25,000 my cash goes down by 25,000.

What is my asset balance? Only 25,000. What is my liability plus equity balance? The resultant profit of that 50 minus 25 gets added where? Added to the capital out there whatever is the capital. So, it takes care of it that is all yes sir come to you do not worry.

Student: (Refer Time: 11:20) there somethings called some net block (Refer Time: 11:22).

I said gross value net value gross block net block used that is all inter changeably. Gross normally if you look at your balance sheet it will be gross block net block, I said gross value net value that is all sir yes sir.

Student: On the accumulating method of. For just (Refer Time: 11:38). I have taken the depreciation to the consider (Refer Time: 11:42).

Agreed.

Student: Tax rebate.

Agreed.

Student: Next year in the accumulating method.

Accumulating is there is no accumulating is your accumulating depreciation every year. For example, the same thing go to the excel the same thing if I do it next year accumulated will be so, much.

I am not getting what depreciation for the year will be further 10 percent of this. What will be expenditure for that year? The expenditure for the year is what I have utilized for that particular year in the second year. What is that that I am utilizing? 10 percent of the this is what I am utilizing only that what you will charge depreciation for the year is what you will charge.

Student: (Refer Time: 12:20).

Sure sir.

Student: Addition of the capital. Is that the tax liability.

Which one? No addition of the capital is not supposing fresh capital gets in fused in the sets of 28th transaction you can take another I do not write do not do it. Now further capital somebody there is a third partner who is joining bringing in one crore as capital now what is happening? Your capital increases by 1 crore your bank account increases by 1 crore, he brings 1 crore in the form of a beautiful piece of land and joins as a partner what happens? Capital increases by 1 crore, your asset in the form of land increases by 1 core that is all nothing else will happen.

Student: Hope a company file who (Refer Time: 13:03). And company considered that is (Refer Time: 13:09).

Sir if you have a value of the patent; normally when you file a patent you just show it when you purchase a patent that is one it become an asset for you otherwise you have to do the valuation of a patent that is a different ball game all together brand valuation, patent valuation all that is a different ball game, we will do it quarter 5 if you take valuation is a course.

Student: But (Refer Time: 13:26) still (Refer Time: 13:28).

It will come in the asset side you I buy up a patent imagine I am buying a patent paying some amount. So, what is happening? My cash is going down my patent which is an asset because nobody else can use it, I am only I have the exclusive right for which I bought I use it as a asset out there. Patent valid for a say imagine that has life for a another 5 years. So, what happens? Every year one fifth one tenth whatever one twentieth of it I am writing off as an expenditure patent, I am utilized for this particular area patent what is called is amortized this particular year that is all.

Student: Second is a what is tax rebate?

Tax rebate is normally a tax holiday which you will get for example, imagine you are setting up the manufacturing facility in Arunachal Pradesh a car automobile assembly unit in Arunachal Pradesh, in the whole process what is happening you are providing employment to so, many people.

Because you are providing employment to so, many people and development of the state is taking place the state will give you tax rebate for some years some amount; you will say 5 year tax holiday. So, what happens? 5 year whatever profit you make you do not pay tax or they will say 5 year deferred tax holiday; that means, 5 years you calculate the tax you do not pay in the first 5 years you pay in on the 6th years onwards. Not only the 6 year tax, but also from the previous taxes out there.

Student: Sir its applicable only to company not individuals?

Individual not sir.

Student:.

Sir please keep individual always separate personal taxation is very different.

Student: Sir what is sundry debtors?

Debtors accumulate totally right I this particular company I said purchases are made some 23 times, imagine 23 times I am buying from 23 different vendors when I write it I cannot write the names of all the 23 vendors out there. So, I accumulate it and write it as sundry debtors sundry sundry is a simple English word.

Student: (Refer Time: 15:22) give me examples of inherited land donated by a particular (Refer Time: 15:23).

As a inherited non inherited let us not worry about it donation is keep, we keep let there is a.

Student: Say that land value is very high.

Student: So, I get it.

Student: But it will come in profit side because its an income.

Of course.

Student: So, if there is way where I can show it in a different way by tax planning.

Tax planning keep it aside.

Student: No like for the company is there a way (Refer Time: 15:43).

There are many multiple ways of dealing with it sir I can I will not show it as donation I will show it is a lease various options are there let us not get it in to all that.

Student: Ok.

See I that is why I told you, the last class I will spend on accounting fraud what all you can do, what all you can do, I am very sure none of you are accountants out here (Refer Time: 16:04) Hruthik Pratheeksha right you are also not an accountant right beautiful none ever accountant. So, you will give you enough methods, where in. sees I told you what is balance sheet the other day right. So, that is it.

Student: Export transactions. We are assuming 40 percent 50 percent for the currency also changes.

Of course there is always FOREX risk that you hates it and various things FOREX losses also you write FOREX profit you write. Supposing I say when I sell the goods I invoiced it at 100 dollars. When the dollar price is 60 which is not going to be there in your future at least why? When the payment comes dollar price is 75, I gain 15 rupees on the dollar that is shown as profit on FOREX transactions or gain on FOREX transactions. Now

only there is a treasury department is takes care of it the job of a treasury is a basically to park the money and hits the risk etc.

So, let us not even get in to as of now keep it as simple as this just let us keep it life is simple let us keep it simple. Agreed? At the end of every year whatever amount I have spent in the on what is called on erecting the plant out there, that will come in the asset side as capital work in progress. That is a work in progress, but that is a capital work that is a major building capital work in progress

Student: And the.

If the what is the interest though capital work in progress is the value that you are spent on that particular asset.

Student: Ok.

Whatever interest payable on the borrowing that you have made will be shown as a liability, interest payable, interest accumulated, interest accumulated as a liability.

Student: Ok that cannot be capitalized.

If you that is it can be capitalized in the sense it can be added to the loan itself it cannot be come on the asset side what happens? It will get added. See these two are different I have borrowed 50,000 as of now I spend only 25,000 my capital work in progress is 25,000 my borrowing is 50,000 the other 25,000 will always be in the form of cash out there.

Now, there is an interest on that 50,000 10 percent at the end of the year then what happens? 10 percent will be an expenditure and then the or in or I will show it as a interest due 10 percent on the liability side if or else I what I will do? I will add that interest to the.

Student: (Refer Time: 18:17).

Basically the loan that I have to pay in the process out there. Madam in your always your if for companies you are to you have to anticipate what is the earning that you are going to make and you got a planned and normally companies would have planned for the next

3 to 5 years, you can always claim return you can always claim return that is all very simple.

Student: Returns.

Need not necessary what is what is called as if you are not if you are basically shown as an expenditure then basically what happens is you are got the benefit of that. So, next year when you receive it, you will have to show it is a tax returns that is in the revenue part of it.

Student: No charges.

(Refer Slide Time: 19:06)

at the end of transaction		Profit and loss for the period 1st January to 31st December	
Liabilities & Equity		Income	Expense
Shareholder's funds		Disc received	300000 Advt exp
12,00,000 equity share@10		consulting fee	2600000 Prelim exp ammortize
Drawings by partners		Sales	1684566
P&L			
NET WORTH			
Long term liabilities			
M. Loan			
8% debentures (200,000)			
Loan			
Liab for vec			
Current Liabilities			
Creditors for spcl raw mat			
creditors			



No paid up capital is different sir, paid up capital is a money that you pay I will explain that.