Financial Statements Analysis and Reporting
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Lecture – 29
Corporate Financial Statements Part-V

Welcome students! So, we were talking in the last part of discussion about the preparation of the financial statements. So, I was telling you that we have the trial balance here. So, we are having the total of debit balances, total of credit balances and both the sides are same.

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The following is the Trial Balance of Mamta Fashions Ltd. as on 31st March, 2016

Sr. No.	Head of Account	Amount (Dr.)	Amount (Cr.)
1.	Premises	3,60,800	
2.	Plant & Machinery	4,95,000	
3.	Opening Inventory	1,12,500	
4.	Debtors	1,06,050	
5.	Land	87,500	
6.	Cash in Hand	4,725	
7.	Current Account	45,500	
8.	Bills Receivables	58,875	
9.	Purchases	27,00,000	
10.	Preliminary expenses	7,500	
11.	Wages	86,970	
12.	General expenses	10,252	
13.	Salaries	90,338	
14.	Bad Debts	3,165	
15.	Interest on term loan	27,000	
16.	Equity share capital		3,00,000
17.	10% Preference Share Capital		1,00,000
18.	Secured Loan @ 12% p.a.		4,50,000
19.	P&I A/C Balance as on 1.4.2015		39,375
20.	Bills Payables		55,500
21.	Creditors		83,000
22.	Sales		31,20,000
23.	General Reserves as on 1.4.2015		37,500
24.	Central Sales tax Payable		10,800
	Total	**4,196,175**	**4,19,6175**

So, here and, as I told you that all the assets and expenses have the debit balance and, all the liabilities and incomes have the credit balance. So, you see that all premises asset having a debit balance; plant and machinery having a debit balance, inventory is a asset having a debit balance. So, all the asset; salaries are expenses having a debit balance, general expenses are expenses having a debit balance. And then, we have preliminary express having a debit balance. And then, we have the, look at the liability. Share capital is a liability credit balance, secured loan is a liability credit balance. Then, it is the bills payable is a liability credit balance, creditor is liability credit balance.

So, it is a set rule. Always be clear about it that all the assets and expenses will always have a debit balance. If you, for example, preparing the say ledger accounts and balancing it or maybe you are preparing the trial balance and you are putting the different balances on the different sides. And, if you find sometimes that it is a asset and having a credit balance, you always assume it or you should be sure that there is something wrong at it or some liability has having a debit balance. In the trial balance, it is coming on the debit balance side of the trial balance. You assume or be sure that it is there is something wrong in it because liabilities cannot have a debit balance. Asset cannot have a credit balance. Expenses can never have a credit balance and income cannot have a debit balance.

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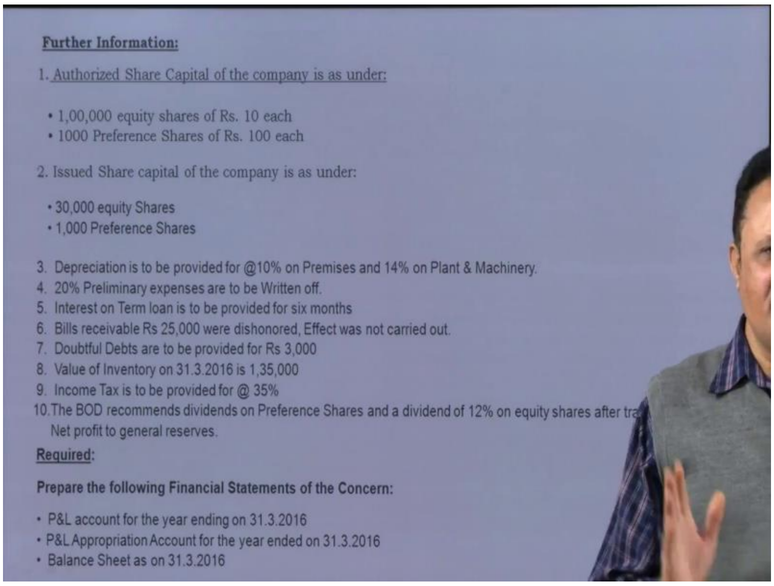

So, these are the some basic rules we should be clear about it. So, total of this Mamta fashions balance is; you can say, that is, 41, 96, 175; 41, 96, 175. This is the total. And then, we have some additional information which is quite interesting. Now, you see that we have the additional information here; share capital. So you see, I told you in my previous discussion that we have the information about the authorized share capital and then the issued share capital. So, this is authorized share capital, which is company is authorized to; means, at the time of registration company is authorized that during its forfeitable life that company can issue how much is equity shares; 1,00,000 equity shares of 10 rupees each. It means, total share capital the company can raise from the market by selling the shares to the general public to the extent of 10,00,000.

Similarly, 1,000 preference shares at the rate of 100, so the preference capital can be raised to the tune of 1,00,000. So, total 11,00,000 of the capital can be raised by this company by selling the shares in the market. Now, we talk about the issued share capital. Out of 1,00,000 of the raised shares, company has issued the 30,000 shares of 10 rupees each. It means, 3,00,000 of the capital has been issued by the company. And, they have also got it because it is issued and this is the, they have received it. And, 1,000 preference shares have been sold in the market at rupees 100 per share. So, again 1,00,000 preference share capital is fully exhausted. And, equity share capital is exhausted to the extent of 30 percent. And, still 70 percent of the capital is there; company wants later on, at some later date. They can issue 70,000 more shares in the market and to raise seven more lakhs from the market by selling the shares to the general public.

So, equity capital is exhausted to the extent of 30 percent. And, preference capital is exhausted to the full extent. Now after this, if this equity capital is also fully exhausted all the ten 1,00,000 shares are issued in the market. And, say all the 1,000 preference shares are issued in the market, after that still the company needs, then they have to go to the registrar of companies. We have to request the registrar of companies to revise this authorized capital. They have to get it authorized. They have to get, to get a revised and this authorized capital has to be increased from the 1,00,000 equity shares to maybe 2,00,000 or 3,00,000 equity shares, depending upon the requirements of the company.

Similarly, if they want to increase the, reissue the say further issue, the preference capital also. They will have to go to the registrar of companies and request that our limit for issuing the preference share should also be raised. And, after that we have some items like (Refer Time: 05:06) the depreciation is the one item, which we have already dealt with. How to deal with it that is clear. We have one item here. That is a preliminary expenses; 20 percent preliminary expenses.

I would like to share with you that what are the preliminary expenses and how to adjust them. Preliminary expenses are those expenses, which are incurred before the company comes into existence. Say, as I told you that memorandum of association is required, article of association is required. When the company goes public, prospectus is required. Then, so many other kind of the official work, clerical work and then other things are required to be done. Project report has to prepare for certain projects. So there, so many preliminary expenses which have to be incurred by the company before it comes into existence; before it comes into existence.

Now, at that time only these are expenses and no incomes because company has not yet started the production. So, when the company has not yet started the production and there is no as such incomes to the company, so these expenses are recorded and kept reserved. And, when the company starts its business and the revenue start coming in and when the company prepares its profit and loss account and balance sheet, then what happens? If these expenses are small, then they are debited in the first year profit and loss account and they are recovered from the profit and loss account. It means, from the revenue of the sales and then that amount which is spent earlier in the market that is recovered. But, if it is a big amount, then in that case it is not justified to recover it from the first year's profit and loss account because in that case, the loss will go down seriously.

So, in this case the loss can be reduced and then these preliminary expenses are capitalized; means we show these expenses in the as total expenses, say for example, total expenses are 2,00,000. So, we will show this 2,00,000. Expenses of preliminary expenses 2,00,000 as a asset in the balance sheet. These are treated like the prepaid expenses, as we have been treating the prepaid expenses, so they are treated as a prepaid expenses. Total amount of the prepaid expense is shown as a asset in the balance sheet. And in the first year, but percentage of these expenses is to be written off that is brought and debited in the profit and loss account.

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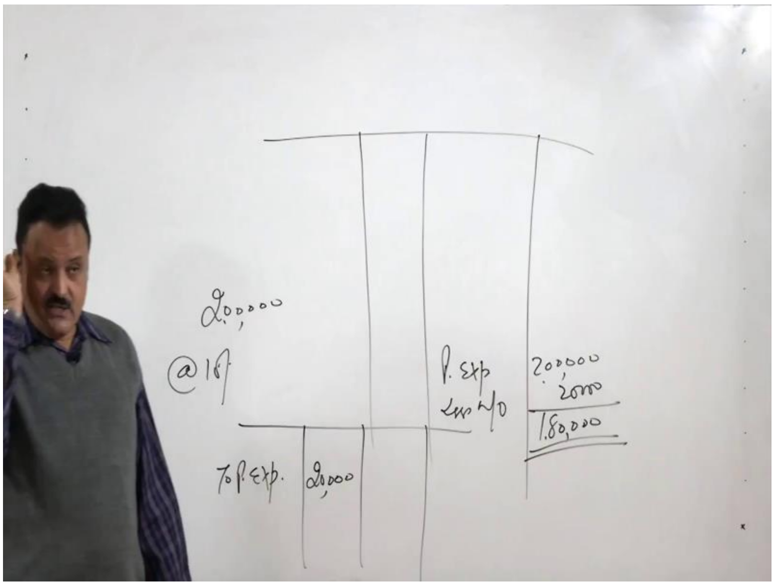

For example, the total expenses are 2,00,000. So, when we will prepare the balance sheet we will be showing it. We will take it to the balance sheet and will show in the beginning of the balance sheet, that is, the preliminary expenses. And, here it is 2,00,000. That amount is shown here. And, we have decided that these expenses will be written off at the rate of 10 percent per annum. So it means, out of this when you are preparing the profit and loss account, then 10 percent of 2,00,000 will be to preliminary expenses. They will be provided here and will be debited in the profit and loss account. So, it is 20,000. Amount will be debited here. And, if the 20,000 amount is debited here, so how much it is left here? less return of 20,000. So, the balance left here is 1,80,000 rupees.

So, this way we, after maybe say ten years, this amount will become 0. And, we have recovered the total amount through profit and loss account. So, same way as we provide for depreciation, then we say that this preliminary expense is a asset. And that part of the asset, which is used in one year that is reduced. So, it is like the process of depreciation. We recover this preliminary expenses. And, this process of providing depreciation and then writing it off or recovering the preliminary expenses through profit and loss account is called as a process of amortization. This is called as a process of amortization. So, through the process of amortization, these preliminary expenses are recovered and first they are capitalized, shown in the balance sheet as a total amount. And then, every year a certain percentage is taken to the profit and loss account. And then, we try to recover these expenses. So, this is the way how we deal with the preliminary expenses.

Then, is the interest on term loans. We have already taken care of bill receivables are known to us, doubtful debts are to be provided here. One thing is given to us; bill receivable rupees 25,000, but dishonored. What is the meaning of dishonored? Dishonored means that as I told you in the last part of discussion that say when any goods are purchased on credit by one party from the other party or by one company from the other company, then the seller supplies the goods. And then, at the same time they write a bill and present it before the buyer and buyer accepts it. So, it means it becomes a legal document proof that, yes, buyer has bought the goods, suppliers has sold the goods and buyer has to pay to the supplier at the later date. But, when that later date comes and buyer, for example, refuses to make the payment. Maybe because of one of the another pretext, he says that I do not have the money, he says that I will not pay, he says that goods were defective, so why should I pay? Any kinds of excuses he can take.

So, if he takes any kind of excuse, in that case that bill when it is sent to him that look it is, you have purchased this goods from us, this payment is due, now you make the payment. But, when he refuses to make the payment and he returns the bill back to the supplier of selling company, then that bill is considered as dishonored. So, how to treat that in the accounting books that we will be also discussing. Doubtful debts, we have already done. Inventory is the closing stock that we have done. Income tax, almost we have done. We will do it again.

And, now we will deal with the problem of dividend. That is dividend on the preference shares and on the equity shares we have to provide for. And then, we will have to create some general reserve also.

So, what is required to be done? We have to prepare the profit and loss account for the year ending on 31st March 2016. Profit and loss appropriation account also on the same date and the balance sheet on the same date, we have to prepare. So, we are learning how to prepare the profit and loss appropriation account also. That is, the additional new account. We will be learning how to prepare it.

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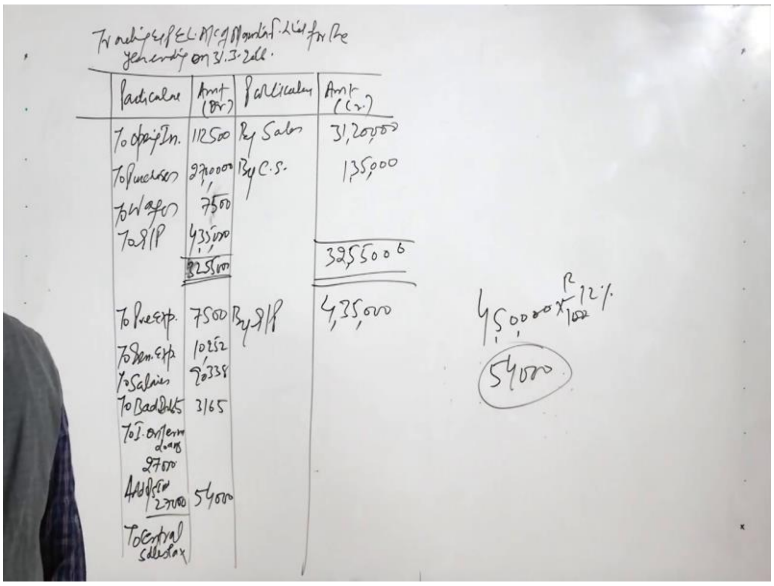

Now, let us start preparing the financial statements of Mamta fashion and we will start with the trading account, which is very simple; no, nothing new. And, as we have been doing in the past, same way we will be doing here also.

So, this is the trading account of Mamta Fashion and then trading. And then, then we will be going further with a profit and loss account and then will be; profit and loss appropriation account and then will be preparing the balance sheet. So, let us start from here. That is the profit and loss account of Mamta Fashion. This is trading and profit and loss account of Mamta Fashion Limited for the year, for the year ending on 31st, for the year ending on 31st March 2016; 31st March 2016. So, it is again particulars. This is amount, this is particulars and amount, this is debit and this is the credit balance.

So, let us start searching for the items to be taken to the trading account. First, we are starting with the opening inventory. So, it is ‘To opening inventory’. And, the opening inventory here is 1,12,500. 1,12,500. We will not take that as land, cash, bills receivables. Yes, we will take purchases ‘To purchases’. To purchases. So, it is 27,00,000. 27,00,000 is the purchases amount. Then, we have preliminary expenses; no wages. To wages, wages amount is 7,500. And then, we have to look for the any other direct expense, if it is there. So, general expenses no, salaries no, bad debts no, interest on term loans no, equity share capital no, tends and preference share capital no, secured loans no; it means there is nothing now left here.

So, let us check for the, we will take go to the credit side now. ‘By sales’. By sales. So, this amount is 31,020; 31,20,000. And then, we have to go for the closing stock, that is, ‘By closing stock’. And, if you look for the closing stock it is given somewhere here, that is, the value of inventory on 31st March 2016 is somewhere. It is 1,35,000; is 1,35,000. So, this is the value of inventory. Or, there is any adjustment? First is share capital depreciation, preliminary expenses, interest, bill receivables, doubtful debts, value of inventory, income tax, nothing is there.

So, now I think we can easily calculate the amount of gross profit or loss. So, it is 0 0 0 5 5. Then, it is 2, and it is 32,55,000. And, now we will have to calculate the gross profit. ‘To gross profit’ And, when we calculate the gross profit here, the gross profit figure is going to be; let us calculate here; this is 1,12,500, 27,00,000. So, it is going to be 28, 12, 500. And then, it is going to be 7,500. So, it is 0 0, then it is 0 1 0 1 2. And, 28,20,000. So, we have total amount of this 32,55,000. So, it is 28,00,000 and 20,000. So, it 0 0 5, so it is 3, and then it is 4,35,000.

So, the amount of your gross profit is 4, 35,000. So, to ‘To gp’ is 4,35,000. And, both the sides are equal now. 32, 55,000. And, both the sides are same. Both the sides are equal. So, we can total it up again. 0, then it is again 0, then it is 5 5 10 1. Then it is 3, then it is 7 10. And, it is 5 15 1. And, it is 3. And then, the total amount is; so, it is 32, 55,000. And, the amount of the gross profit is 4,35,000. Amount of the gross profit is 4,35,000, which we have calculated. Now it will be brought down to the credit side by gross profit. So, it is 4,35,000. And then, it is; the other expenses we will have to take.

We will have to deal with the other expenses like the other direct expenses. Premises we will not be taking, plant and machinery, no opening inventory. We have taken debtors no, land no, cash in hand. Current account is a bank balance. Receivables, purchases, we have done. So, we will be taking now the preliminary expenses. First item will be. So, we will start from this only. And, you can keep on ticking that which we have taken that will not take it again. So, it is ‘to preliminary expenses’, and that amount is 7,500. Then, we will be taking the other items; preliminary expenses, 7500. Wages, we have already taken, general expenses, we have, now we have to take the general expenses, that is, ‘To general expense’. To general expense.

So, when we take the general expenses, here 10,252 is the general expense. Is there any adjustment with regard to the general expenses? There is no adjustment with regard to the general expenses. We have taken it. Similarly, now we will be taking the salaries 'To salaries'. To salaries, so we will be taking the salaries and salaries are 90,338. Is there any adjustment here? If we talk about the salaries, depreciation, preliminary expenses, interest on term loan bill, receivable, doubtful debts, value of inventory, income tax. No, there is no adjustment with regard to salaries. We have already adjusted all the salaries here. It is 90,338. 90,338 are the salaries.

Then, we will be talking about the bad debts. 'To bad debts'. To bad debts. This amount is 31, 065. But are, there are some, I think, adjustments for this. Let us check this adjustment. What is the adjustment here? We will be taking doubtful debts are to be provided 3,000. So, it means that we will be taking it separately and there is nothing with regard to the bad debts. So, it is 3 1 6 5 can be taken directly to the outer column. 3 1 6 5. This is 3 1 6 5. Then, we have others; interest on term loans. Yes, this is important. 'To interest on term loans'. 'To interest on term loans'.

So, this interest which is already paid is 27,000. We will put it in the inner column. Why we are putting in inner column? I would like to tell you that what is the total term loan? If you look at the figure of the total term loan, we will have to see here; secured loan is this one. That is, secured loan 12 percent. And, this is 4,50,000. So, we have taken the loan of 4, 50,000; which means it is 12 percent. So, the rate of interest is 12 percent. So, what is 12 percent on the 4,50,000? If you calculate when it is 54,000, total amount of the interest works out to be 54,000. So, it means if it is 54,000. And, it is shown that the interest to the extent of 27,000 has been paid. It means, there is a balance of interest to be paid. So, it is add. Outstanding interest and that is 27,000. So, total interest figure will be 54,000. Total interest figure will be 54,000.

So, here it is the interest, we have taken. Equity share capital no, preference share capital no, secured loans, only interest had to be taken. So, we have taken profit and loss account balance as on one 1 st April 2015. Now, what is this balance? This balance is the opening balance of the profit and loss account, which is not yet added into the capital. It is kept as open in the revenue account in the profit and loss account. And, this will be added into this year's profit. And then, the total may be added into the capital. It has not been added. We do not know the reason why it has been kept as open, otherwise I should have been added in the share capital, but it has been kept as open.

So, this plus this year's profit, when we would prepare the profit and loss appropriation account, there we will be showing and will be adding it up. And, we will be transferring it to the, after paying the dividend, after creating certain specific reserve, the general reserves will be remaining amount, will be transferred to the share capital in the balance sheet. So, it is the, done. So, bills payable is a liability credit is a liability sales is we have taken. General reserves, a balance is also there. So, when we create a general reserves this year, we will add it up into the previous year's balance. So, the total balance will be there and the profit and loss appropriation account. And finally, that balance will be transferred to the balance sheet.

Then, we have the central sales tax payable. So, will have to take that tax also which is central sales tax payable. So, we will be taking that also. And, the income tax part is different. So, we will be taking the 'To central sales tax'. To central sales tax. Central sales tax is 10,800. Central sales tax is 10,800. So, almost we have taken all the expenses, premises, plant and machinery, opening inventory, debtors, land, cash in hand, bills receivables, purchases, preliminary expenses, wages, general expenses, salaries, bad debts, term loans, equity capital, then 10 percent, preference capital, secured loan, bills payable, creditors sales, general reserve will be taken later on, central sales tax we have taken.

Now, we talk about the, yes, we will be taking now the other items like your depreciation. So, we will be taking the items like the depreciation.

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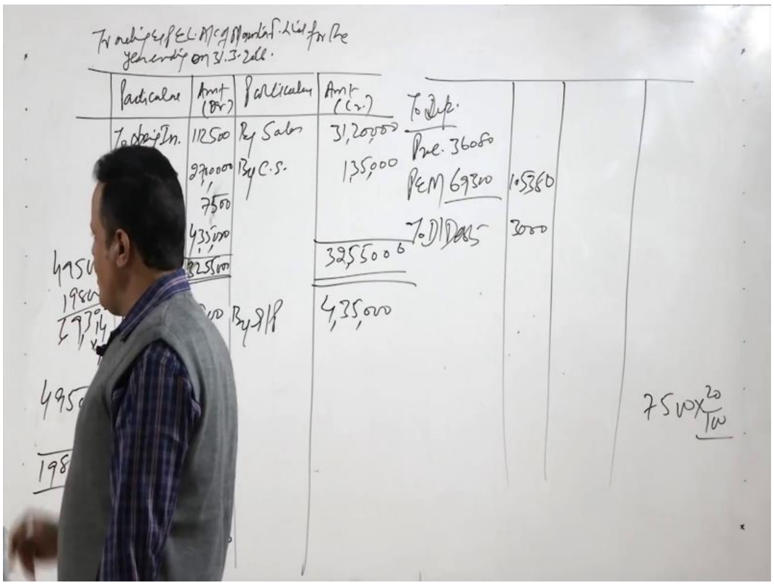

So, we are continuing this account here. That is why I kept the space and now I am extending it here. So, it is ‘To depreciation’. And, depreciation has to be provided on the depreciation to be provided at the rate of 10 percent on premises and 14 percent on the plant and machinery.

So, it is, premises is 3,60,008. So, it is 10 percent of this will be 36,080; is going to be the depreciation we are going to provide on it. The percentage given to us is 10 percent on the provided on the premises. So, 10 percent of this is 36,080. So, this is on the premises 36,080. Then, we have 36,080 is on this. And then, next item given to us was plant and machinery at the rate of 14 percent. So, plant and machinery 14 percent is going to be provided. So, it is a say 4,95,000. It is at the rate of the percentage given to us is the 14 percent. So, 14 percent is this works out as 49,500 as 10 percent and we will have to provide the 4 percent more on this. So, 4 percent of this will be something like 0 0, 5 4 sar 0 20 22, 9, 4 9 sar 36 and 38 3, this is 19,800 more. So, this works out as 0 0. Then it is 3 1 19 1, it is 69,000.

So, this depreciation will be on the plant and machinery. It is going to be on plant and machinery. The depreciation is going to be 69,000 and 3,000. So, there is no other item here. If we take this total depreciation, this is 0 8, then it is 300, then it is a 5, this is 1,05, 380. It is the depreciation amount. Preliminary expenses are to be written off 20 percent. So, total preliminary expenses given to us were here that is the amount is, preliminary expenses amount is 7,500. Sorry, we have not to take the total sub preliminary expenses. We have to provide only for the 20 percent.

So, it means total is 75. So, that will go to the balance sheet. And out of this, we have to take the 20 percent. It means, we have to only debit in the profit and loss account of this year is the 1,500. And then, we will have to take the other items like your depreciation we have taken, preliminary expenses we have taken, interest on loan, interest on term loan is to be provided for 6 months.

So, we have already taken the interest on loan for the 6 months. And then, bill receivable; dishonored, not to be taken here. Doubtful debts? Yes, we will be taking one more item ‘To doubtful debts’. To doubtful debts and, this amount is 3,000. So, we will be taking the 3,000 as doubtful debts. Value of inventory; we have already taken income tax. We will be taking later on and other things.

So, I think there is nothing left now to be taken on the expense side of profit and loss account. And, we have taken almost all the items; preliminary expenses, general expenses, salaries, bad debts, then interest on term loan, then it is general expenses, central sale tax, depreciation and the doubtful debts.

Now, we will be talking about the credit side of the profit and loss account, where they will be recording the incomes. And then, we will calculate the net profit before tax, we will provide for the tax and then we will take the, calculate the net profit after tax. So, this is solved. And then, after that we will be preparing the profit and loss appropriation account. This all, we will be doing in the next part of discussion.

Thank you very much.