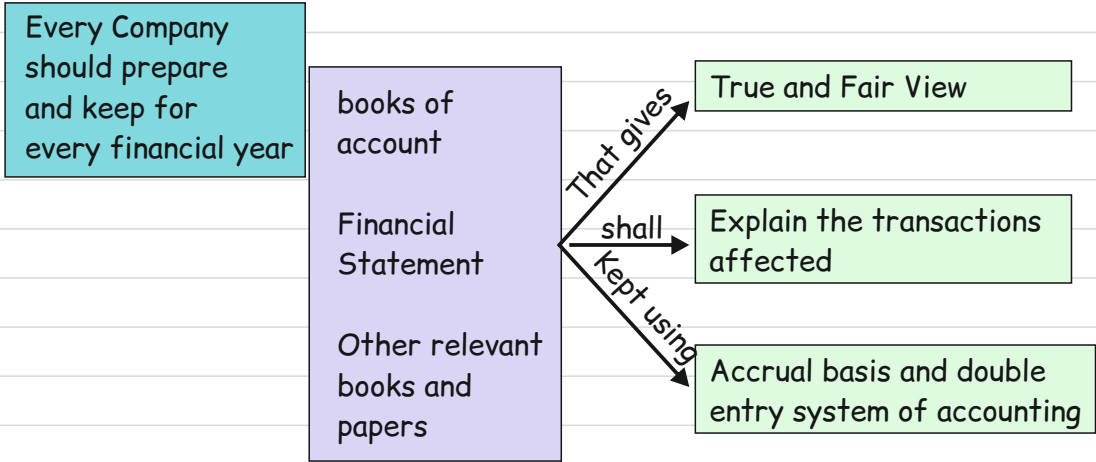


# Schedule III

## MAINTENANCE OF BOOKS OF ACCOUNT (sec. 128)



At its registered office and branch offices if any

The Books of Accounts of every company shall be kept for a minimum period of Eight Years.

### MAINTENANCE at place other than registered office:

The company should inform the ROC within seven days in case the Board of Directors decides to maintain books at a place other than the registered office.

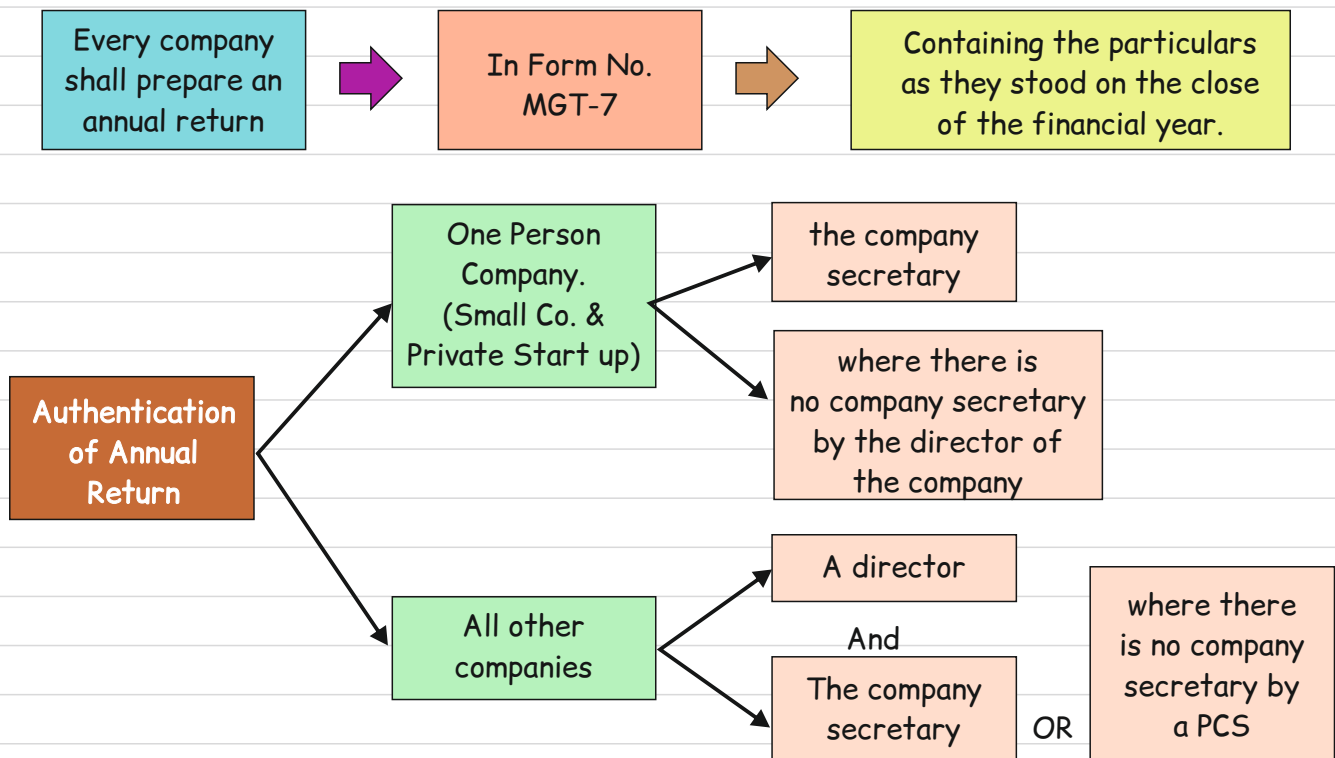
### In Case of Branch Offices

**Summarized** returns shall be sent periodically to the registered office or any other place which the BOD may decide.

Books maintained, shall be open for inspection by any director during business hours and subject to such condition as may be prescribed.

### STATUTORY BOOKS

Register of Charges (Section 85)	Register of Debenture holders And Other Security holders (Section 88)	Register of Investments of the company held in its own name (Section 187)
Register of Members (Section 88)	Register of Loans and Investments by Company (Section 186)	Minute Books (Section 118)
Register of Contracts, or arrangements in which directors are interested (Section 189)	Register of directors and key managerial personnel and their shareholding (Section 170)	Other Statistical books, records and documents are also required to be maintained by the company.

**ANNUAL RETURN [SEC. 92]****FINANCIAL STATEMENTS [SEC. 2(40)]**

- ⇒ Balance Sheet as at the end of the financial year
- ⇒ Profit and Loss Account / Income and Expenditure Account (for Sec 8 Companies) for the financial year
- ⇒ Cash flow statement for the financial year \*\*
- ⇒ A statement of changes in equity
- ⇒ Explanatory Notes annexed to, or forming part of, any document referred to above.

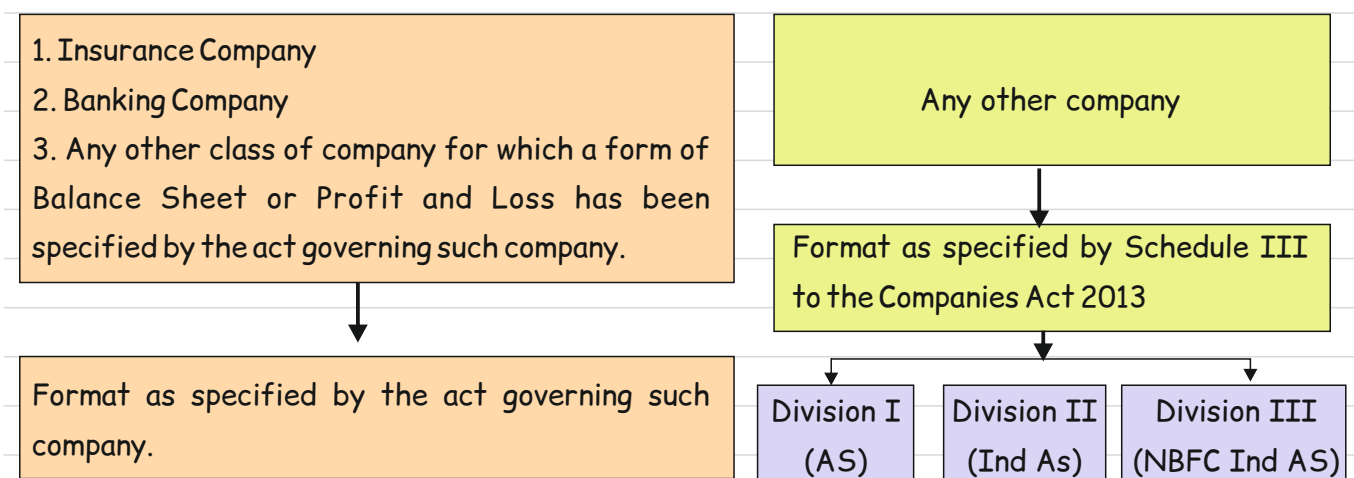
\*\* Cash flow Statement is not required in case of OPC, Small Companies and Dormant Companies.

**PERIODIC FINANCIAL STATEMENTS**

## ASPECTS TO BE CONSIDERED WHILE PREPARING FINANCIAL STATEMENTS

- ⇒ Requirements of Schedule III to the CA 2013.
  - ⇒ Requirements of other applicable statutes.
  - ⇒ Accounting Standards (AS or Ind AS as applicable) notified by MCA.\*\*
  - ⇒ Statements and Guidance Notes issued by ICAI as maybe applicable.
- \*\* Sec 133 of CA 2013 requires mandatory compliance with the applicable accounting standards.

## FORMAT FOR PREPARATION OF FINANCIAL STATEMENTS



For Company's engaged in the business of generation or supply of electricity, the Electricity Act, 2003 does not specify any format for presentation of Financial Statements. Therefore, Schedule III of the Companies Act, 2013 is followed by Electricity Companies in preparation of their financial statements.

## KEY FEATURES OF SCHEDULE III

**Schedule III has been divided into 3 Divisions:**

1. Division I: Specifies the format of financial statements for Company complying with Accounting Standards under the Companies (Accounting Standard) Rules, 2021.
2. Division II: Specifies the format of financial statements for Company complying with Indian Accounting Standards under the Companies (Indian Accounting Standard) Rules, 2015.

**Both the divisions are further subdivided into two parts:**

1. Part I - Form of Balance Sheet and general instructions for preparation of Balance Sheet
2. Part II - Form of Statement of Profit and Loss and general instructions for preparation of Statement of Profit and Loss.

Depending upon the turnover of the company, the figures appearing in the Financial Statements "Shall be" rounded off.

Schedule III gives prominence to Accounting Standards (AS and Ind AS) i.e. in case of any conflict between the AS/ Ind AS and the Schedule III, AS/ Ind AS shall prevail.



**SCHEDULE III - FORMAT****PART I - Form of BALANCE SHEET**

Particulars 1	Note No. 2	Current Year 3	Previous Year 4
<b>I. EQUITY AND LIABILITIES</b>			
(1) Shareholders' 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			
(i) total outstanding dues of micro enterprises and small enterprises; and			
(ii) total outstanding dues of creditors other than micro enterprises and small enterprises			
(c) Other current liabilities			
(d) Short-term provisions			
<b>TOTAL</b>			
<b>II. ASSETS</b>			
(1) Non-current assets			
(a) Property, Plant and Equipment			
(i) Tangible assets   (ii) Intangible assets			
(iii) Capital work-in-progress			
(iv) 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			
<b>TOTAL</b>			

## PART II - Form of STATEMENT OF PROFIT AND LOSS

Particulars	Note No.	Figures for the current reporting period	Figures for the previous reporting period
I. Revenue from operations		...	...
II. Other income		...	...
III. Total Revenue (I + II)		...	...
IV. Expenses:			
Cost of materials consumed		...	...
Purchases of Stock-in-Trade		...	...
Changes in inventories of FG, WIP and Stock-in-Trade			
Employee benefits expense		...	...
Finance costs		...	...
Depreciation and amortization expense		...	...
Other expenses		...	...
Total expenses			
V. Profit before exceptional and extraordinary items and tax (III - IV)		...	.....
VI. Exceptional items			.....
VII. Profit before extraordinary items and tax (V - VI)		...	...
VIII. Extraordinary Items			.....
IX. Profit before tax (VII - VIII)			.....
X Tax expense:			
(1) Current tax			.....
(2) Deferred tax			
XI. Profit (Loss) for the period from continuing operations (VII - VIII)		...	...
XII. Profit/(loss) from discontinuing operations		...	...
XIII. Tax expense of discontinuing operations		...	...
XIV. Profit/(loss) from Discontinuing operations (after tax)(XII - XIII)		...	...
XV. Profit (Loss) for the period (XI + XIV)		...	...
XVI. Earnings per equity share:			
(1) Basic			.....
(2) Diluted		...	...

## SHARE CAPITAL

Following are some of the important disclosures

- (a) the number and amount of shares authorized;
- (b) the number of shares issued, subscribed and fully paid, and subscribed but not fully paid;
- (c) par value per share;
- (d) a reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period;
- (e) the rights, preferences and restrictions attaching to each class of shares including restrictions on the distribution of dividends and the repayment of capital;
- (f) shares in respect of each class in the company held by its holding company or its ultimate holding company including shares held by or by subsidiaries or associates of the holding company or the ultimate holding company in aggregate;
- (g) shares in the company held by each shareholder holding more than 5 per cent. shares specifying the number of shares held;
- (h) shares reserved for issue under options and contracts/commitments for the sale of shares/disinvestment, including the terms and amounts;
- (i) for the period of five years immediately preceding the date as at which the Balance Sheet is prepared:
  - (A) Aggregate number and class of shares allotted as fully paid-up pursuant to contract(s) without payment being received in cash.
  - (B) Aggregate number and class of shares allotted as fully paid-up by way of bonus shares.
  - (C) Aggregate number and class of shares bought back.
- (j) terms of any securities convertible into equity/preference shares issued along with the earliest date of conversion in descending order starting from the farthest such date.
- (k) calls unpaid (showing aggregate value of calls unpaid by directors and officers);
- (l) forfeited shares (amount originally paid-up).
- (m) Disclosure regarding Shares held by promoters

### Let's take an example

Q. In the financial statements of the financial year 20X1-20X2, Alpha Ltd. has mentioned in the notes to accounts that during financial year, 24,000 equity shares of ₹ 10 each were issued as fully paid bonus shares. However, the source from which these bonus shares were issued has not been disclosed. Is such non-disclosure a violation of the Schedule III to the Companies Act? Comment.

## RESERVES AND SURPLUS

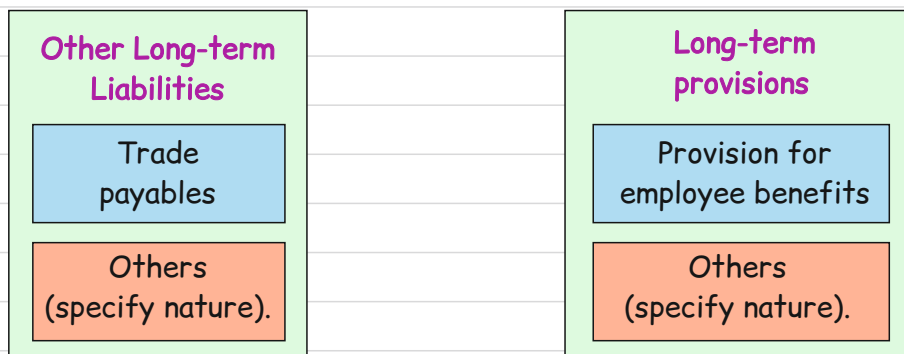
Reserves and Surplus shall be classified as:

- ⇒ Capital Reserves
  - ⇒ Capital Redemption Reserve
  - ⇒ Securities Premium Reserve
  - ⇒ Debenture Redemption Reserve
  - ⇒ Revaluation Reserve
  - ⇒ Share Options Outstanding Account
  - ⇒ Other Reserves(specify)
  - ⇒ Surplus i.e., balance in Statement of Profit and Loss
- Reserve specifically represented by earmarked investments shall be termed as a "fund".
  - Debit balance of statement of profit and loss Shall be shown as a negative figure under the head "Surplus".
  - Similarly, the balance of "Reserves and Surplus", after adjusting negative balance of surplus, if any, shall be shown under the head "Reserves and Surplus" even if the resulting figure is in the negative.

## LONG-TERM BORROWINGS

It shall be classified as:

- 1) Bonds/debentures;
  - 2) Term loans:
    - (i) from banks.
    - (ii) from other parties
  - 3) Deferred payment liabilities;
  - 4) Deposits;
  - 5) Loans and advances from related parties;
  - 6) Long term maturities of finance lease obligations;
  - 7) Other loans and advances (specify nature)
- ⇒ It shall further be sub-classified as **Secured and Unsecured**.
  - ⇒ **Terms of repayment** of term loans and other loans shall be disclosed.
  - ⇒ Period and amount of continuing default as on the balance sheet date in repayment of loans and interest (separately in each case) shall also be disclosed.
  - ⇒ Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall further be disclosed.



GK

Even if Creditors for Capital Expenditure relate to a capital asset, they may be classified as Current if they are to be settled within the Company's Normal Operating Cycle/ 12 Months unlike Capital Advances which are always classified as Non-Current.

### SHORT-TERM BORROWINGS

Short-term borrowings shall be classified as:

1. Loans repayable on demand
  - from banks.
  - from other parties.
2. Loans and advances from related parties;
3. Deposits;
4. Other loans and advances (specify nature).

Current maturities of Long Term Borrowing shall be disclosed separately, under other current liabilities.

**Further disclosures as specified in Long Term Borrowings shall be given.**

### TRADE PAYABLES

The following details relating to Micro, Small and Medium Enterprises shall be disclosed in the notes:

- (a) the principal amount and the interest due thereon (to be shown separately) remaining unpaid to any supplier at the end of each accounting year;
- (b) the amount of interest paid by the buyer in terms of section 16 of the Micro, Small and Medium Enterprises Development Act, 2006, along with the amount of the payment made to the supplier beyond the appointed day during each accounting year;
- (c) the amount of interest due and payable for the period of delay in making payment (which have been paid but beyond the appointed day during the year) but without adding the interest specified under the Micro, Small and Medium Enterprises Development Act, 2006;
- (d) the amount of interest accrued and remaining unpaid at the end of each accounting year; and
- (e) the amount of further interest remaining due and payable even in the succeeding years, until

such date when the interest dues above are actually paid to the small enterprise, for the purpose of disallowance of a deductible expenditure under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006.

### Trade Payable due for Payment

The following ageing schedule shall be given for Trade payables due for payment :

Trade Payables ageing schedule

(Amount in ₹)

Particulars	Outstanding for following periods from due date of payment #				Total
	Less than 1 year	1-2 years	2-3 years	More than 3 years	
(i) MSME					
(ii) Others					
(iii) Disputed dues - MSME					
(iv) Disputed dues- Others					

### OTHER CURRENT LIABILITIES

Other current liabilities shall be classified as:

- 1) Current maturities of long-term debt
- 2) Current maturities of finance lease obligations
- 3) Interest accrued but not due on borrowings
- 4) Interest accrued and due on borrowings
- 5) Income received in advance;
- 6) Unpaid Dividends
- 7) Application money received for allotment of securities and due for refund and interest accrued thereon.
- 8) Unpaid matured deposits and interest accrued thereon
- 9) Unpaid matured debentures and interest accrued thereon;
- 10) Other payables (specify nature).

### SHORT-TERM PROVISIONS

Short-term provisions shall be classified as:

Provision for  
employee benefits

Others  
(specify nature)

## PROPERTY, PLANT AND EQUIPMENT (PPE)

PPE shall be classified as:

- 1) Land;
- 2) Buildings;
- 3) Plant and Equipment;
- 4) Furniture and Fixtures;
- 5) Vehicles;
- 6) Office equipment;
- 7) Others (specify nature)

PPE under lease shall also be separately specified under each class of asset.

A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately.

Que. How should "PPE held for sale" be classified in the balance sheet?

Ans.

## INTANGIBLE ASSETS

Intangible Assets shall be classified as:

- 1) Goodwill;
- 2) Brands /trademarks;
- 3) Computer software;
- 4) Mastheads and publishing titles;
- 5) Mining rights;
- 6) Copyrights, and patents and other intellectual property rights, services and operating rights;
- 7) Recipes, formulae, models, designs and prototypes;
- 8) Licenses and franchise;

9) Others (specify nature).

A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately.

When does an entity recognize website costs as an intangible asset?

Ans. An entity should recognize web site costs arising from development as an intangible asset if, and only if, in addition to complying with the general requirements for recognition and initial measurement, an entity can demonstrate how its web site will generate probable future economic benefits or service potential.

### NON-CURRENT INVESTMENTS

Non-current investments shall be classified as Trade investment Other investments.

It shall further be classified as:

1. Investment property
2. Investments in Equity Instruments;
3. Investments in preference shares;
4. Investments in Government or trust securities;
5. Investments in debentures or bonds;
6. Investments in Mutual Funds;
7. Investments in partnership firms;
8. Others (specify nature).

The following shall also be disclosed:

1. Aggregate amount of quoted investments and market value thereof
2. Aggregate amount of unquoted investments
3. Aggregate provision for diminution in value of investments

Investments carried at other than at cost should be separately stated specifying the basis for valuation thereof

### LONG-TERM LOANS AND ADVANCES

**It shall be classified as:**

- 1) Capital Advances
- 2) Security Deposits
- 3) Loans and advances to related parties (giving details thereof)
- 4) Others (specify nature).

Further classification under **Secured, Unsecured and Doubtful** shall also be given.

Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.

Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other persons or amounts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

Capital Advances (CA) even if settled within 12 Months are "ALWAYS" classified as Non Current because CA is always settled for a Capital Asset.

Also, Capital Advances are not be classified under Capital Work in Progress, since they are specifically to be disclosed under LT Loans and Advances.

### OTHER NON-CURRENT ASSETS

Other non-current assets shall be classified as:

1. Long-term Trade Receivables (including trade receivables on deferred credit terms)
2. Security Deposits
3. Others (specify nature)

Further classification under Secured, Unsecured and Doubtful shall also be given.

Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

Other NCA does not include receivables on account of goods sold or services rendered as they are included in Trade Receivables. However, it includes receivables on account of other contractual obligations such as insurance claims, sale of fixed assets, contractually reimbursable expenses etc.

Thus, interest accrued on trade receivables will also be classified as Other NCA.

### CURRENT INVESTMENTS

**Current Investments shall be classified as**

- 1) Investments in Equity Instruments;
- 2) Investment in Preference Shares;
- 3) Investments in Government or trust securities;
- 4) Investments in debentures or bonds;
- 5) Investments in Mutual Funds;
- 6) Investments in partnership firms;
- 7) Others (specify nature).

**Following shall also be disclosed:**

- 1) The basis of valuation of individual investments
- 2) Aggregate amount of quoted investments and market value thereof;
- 3) Aggregate amount of unquoted investments;
- 4) Aggregate provision made for diminution in value of investments

**GK**

If a debenture is to be redeemed partly within twelve months and balance after twelve months, the amount to be redeemed within twelve months should be disclosed as current and balance should be shown as non-current.

**INVENTORIES**

It shall be classified as:

- 1) Raw materials;
- 2) Work-in-progress;
- 3) Finished goods;
- 4) Stock-in-trade (in respect of goods acquired for trading);
- 5) Stores and spares;
- 6) Loose tools;
- 7) Others (specify nature)

Goods-in-transit shall be disclosed under the relevant sub-head of inventories.

Mode of valuation shall also be stated

The heading Finished goods should comprise of all finished goods other than those acquired for trading purposes.

**TRADE RECEIVABLES**

It shall separately state Aggregate amount of Trade Receivables outstanding for a period exceeding six months from the date they are due for payment.

**It shall also shall be sub-classified as:**

- 1) Secured, considered good;
- 2) Unsecured, considered good;
- 3) Doubtful.

Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

Where no due date is specifically agreed upon, transaction date should be taken into consideration for computing the due date which may vary depending upon the nature of goods or services sold and the type of customers, etc.



<b>Cash and bank balances</b>		
<b>Cash and Cash Equivalent:</b>		
Balances with banks		
On current accounts	346.462	337.367
Deposits with original maturity of less than 3 months	66.124	279.710
On unclaimed dividend account	14.018	9.026
Cheques, drafts on hand	23.485	-
Cash on hand	1.618	1.951
	<b>451.707</b>	<b>628.054</b>
<b>Other bank balances:</b>		
Deposits with maturity for more than 12 months	0.020	0.020
Deposits with maturity for more than 3 months but less than 12 months	143.615	100.500
	<b>143.635</b>	<b>100.520</b>
Less: Amounts disclosed under other non-current assets (Refer Note 13)	(0.020)	(0.020)
	<b>143.615</b>	<b>100.500</b>
	<b>595.322</b>	<b>728.554</b>

## SHORT-TERM LOANS AND ADVANCES

**It shall be classified as:**

- 1) Loans and advances to related parties (giving details thereof);
- 2) Others (specify nature).

**It shall also shall be sub-classified as:**

- 1) Secured, considered good;
- 2) Unsecured, considered good;
- 3) Doubtful.

Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other person or amounts due by firms or private companies respectively in which any director is a partner or a director or a member shall be separately stated

<b>Short Term Loans and advances (Unsecured, considered good)</b>		
Advances to subsidiaries	3.380	0.880
Advances to suppliers	137.732	163.699
Other Receivable (net)	180.583	160.472
Advance income tax (net of Provision for taxation)	56.499	-
Balances with Central Excise, Customs and VAT authorities	68.072	84.412
	<b>446.266</b>	<b>409.463</b>

## OTHER CURRENT ASSETS

An all-inclusive heading, which incorporates current assets that do not fit into any other asset categories.

In case any amount classified under this category is doubtful, it is advisable that such doubtful amount as well as any provision made there against should be separately disclosed.

OTHER CURRENT ASSETS		
Interest Receivable	20.00	1,061.65
<b>Total</b>	<b>20.00</b>	<b>1,061.65</b>

## CONTINGENT LIABILITIES

(i) Contingent liabilities shall be classified as:

- Claims against the company not acknowledged as debt;
- Guarantees;
- Other money for which the company is contingently liable.

(ii) Commitments shall be classified as:

- Estimated amount of contracts remaining to be executed on capital account and not provided for;
- Uncalled liability on shares and other investments partly paid;
- Other commitments (specify nature).

## GENERAL POINTS

- Arrears of fixed cumulative dividends on preference shares shall also be disclosed separately.
- Where in respect of an issue of securities made or Loan for a specific purpose, the whole or part of the amount has not been used for the specific purpose at the balance sheet date, there shall be indicated by way of note how such unutilised amounts have been used or invested.
- If, in the opinion of the Board, any of the assets other than Property, Plant and Equipment and non-current investments do not have a value on realisation in the ordinary course of business at least equal to the amount at which they are stated, the fact that the Board is of that opinion, shall be stated.

## PROFIT & LOSS A/C

### ⇒ Revenue Disclosure:

- ✓ In respect of a company other than a finance company revenue from operations shall disclose separately in the notes revenue from -
  - (a) Sale of products;
  - (b) Sale of services;
  - (c) Other operating revenues;

**Less:**

(d) Indirect Taxes

✓ In respect of a finance company, revenue from operations shall include revenue from -

(a) Interest; and

(b) Other financial services.

✓ Revenue under each of the above heads shall be disclosed separately by way of notes to accounts to the extent applicable.

⇒ **Finance Costs Finance costs shall be classified as:**

(a) Interest expense;

(b) Other borrowing costs;

(c) Applicable net gain/loss on foreign currency transactions and translation.

⇒ **Other income Shall be classified as:**

(a) Interest Income (in case of a company other than a finance company);

(b) Dividend Income;

(c) Net gain/loss on sale of investments;

(d) Other non-operating income (net of expenses directly attributable to such income).

**Additional Information:**

⇒ **A Company shall disclose by way of notes additional information regarding aggregate expenditure and income on the following items:**

(i) (a) Employee Benefits Expense with bifurcation into various heads.

(b) Depreciation and amortisation expense;

(c) Any item of income or expenditure which exceeds one per cent. of the revenue from operations or ₹1,00,000, whichever is higher;

(d) Interest Income;

(e) Interest expense;

(f) Dividend income;

(g) Net gain/loss on sale of investments;

(h) Adjustments to the carrying amount of investments;

(i) Net gain or loss on foreign currency transaction and translation (other than considered as finance cost);

(j) Payments to the auditor as (a) auditor; (b) for taxation matters; (c) for company law matters; (d) for management services; (e) for other services; and (f) for reimbursement of expenses;

(k) In case of Companies covered under section 135, amount of expenditure incurred on corporate social responsibility activities;

(l) Details of items of exceptional and extraordinary nature;

(m) Prior period items;

⇒ **Trade information:**

- (a) In the case of manufacturing companies, -
  - (1) Raw materials under broad heads.
  - (2) goods purchased under broad heads.
- (b) In the case of trading companies, purchases in respect of goods traded in by the company under broad heads.
- (c) In the case of companies rendering or supplying services, gross income derived from services rendered or supplied under broad heads.
- (d) In the case of a company, which falls under more than one of the categories mentioned in (a), (b) and (c) above, it shall be sufficient compliance with the requirements herein if purchases, sales and consumption of raw material and the gross income from services rendered is shown under broad heads.
- (e) In the case of other companies, gross income derived under broad heads.

⇒ **WIP Information:** In the case of all concerns having works in progress, works-in-progress under broad heads.

⇒ **Information on Provisions:**

- (a) The aggregate, if material, of any amounts set aside or proposed to be set aside, to reserve, but not including provisions made to meet any specific liability, contingency or commitment known to exist at the date as to which the balance sheet is made up.
- (b) The aggregate, if material, of any amounts withdrawn from such reserves.
- (c) The aggregate, if material, of the amounts set aside to provisions made for meeting specific liabilities, contingencies or commitments.
- (d) The aggregate, if material, of the amounts withdrawn from such provisions, as no longer required.

⇒ **Other Stuff:**

Expenditure incurred on each of the following items, separately for each item:

- (a) Consumption of stores and spare parts;
- (b) Power and fuel;
- (c) Rent;
- (d) Repairs to buildings;
- (e) Repairs to machinery;
- (f) Insurance;
- (g) Rates and taxes, excluding, taxes on income;
- (h) Miscellaneous expenses,
- (i) Dividends from subsidiary companies.
- (j) Provisions for losses of subsidiary companies.

## WHEN AN ASSET SHALL BE CLASSIFIED AS CURRENT?

If it satisfies any of the given criteria:

- (a) it is expected to be realized, or is intended for sale or consumption, in the company's normal operating cycle; or
- (b) it is held primarily for the purpose of being traded; or
- (c) it is expected to be realized within twelve months after the reporting date; or
- (d) it is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

All other assets shall be classified as non-current.

Example:

A company has sold 10,000 tonnes of steel to its customer. The sale contract provides for a normal credit period of three months. The company's operating cycle is six months. However, the company does not expect to receive the payment within twelve months from the reporting date. Therefore, the same should be classified as "Non-Current" in the Balance Sheet. In case, if the company expects to realize the amount upto 12 months from the Balance Sheet date (though beyond operating cycle), the same should be classified as "current".

## OPERATING CYCLE

- ⇒ An operating cycle is the time between the acquisition of assets for processing and their realization in Cash or cash equivalents. Where the normal operating cycle cannot be identified, it is assumed to have a duration of twelve months.
- ⇒ Creditors are not to be deducted while calculating operating cycle.

Example:

H Ltd. engaged in the business of manufacturing lotus wine. The process of manufacturing this wine takes around 18 months. Due to this reason H Ltd. has prepared its financial statements considering its operating cycle as 18 months and accordingly classified the raw material purchased and held in stock for less than 18 months as current asset. Comment on the accuracy of the decision and the treatment of the asset by H Ltd., as per the Schedule III.

**Ans.:** As per Schedule III to the Companies Act, 2013, one of the criteria for classification of an asset as a current asset is that the asset is expected to be realised in the company's' operating cycle or is intended for sale or consumption in the company's normal operating cycle.

Further, Schedule III to the Companies Act, 2013 defines that an operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents. However, when the normal operating cycle cannot be identified, it is assumed to have duration of 12 months.

As per the facts given in the question, the process of manufacturing of lotus wine takes around 18 months; therefore, its realisation into cash and cash equivalents will be done only when it is ready for sale i.e. after 18 months. This means that normal operating cycle of the product is 18 months.

Therefore, the contention of the company's management that the operating cycle of the product lotus wine is 18 months and not 12 months is correct.

### **WHEN LIABILITY SHALL BE CLASSIFIED AS CURRENT?**

**If it satisfies any of the given criteria:**

- a) It is expected to be settled in the company normal operating cycle; or
- b) It is held primarily for the purpose of being traded; or
- c) It is due to be settled within twelve months after the reporting date; or
- d) The company does not have an unconditional right to defer settlement of the liability for least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

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

#### **Example:**

Company X has taken a five year loan. The loan contains certain debt covenants, e.g., filing of quarterly information, failing which the bank can recall the loan and demand repayment thereof. The company has not filed such information in the last quarter; as a result of which the bank has the right to recall the loan. However, based on the past experience and/or based on the discussions with the bank the management believes that default is minor and the bank will not demand the repayment of loan. Elaborate on how will the loan be classified in the Financial Statements of X?

**Ans.:** According to the definition of Current Liability, what is important is, whether a borrower has an unconditional right at the Balance Sheet date to defer the settlement irrespective of the nature of default and whether or not a bank can exercise its right to recall the loan. If the borrower does not have such right, the classification would be "current." It is pertinent to note that as per the terms and conditions of the aforesaid loan, the loan was not repayable on demand from day one. The loan became repayable on demand only on default in the debt covenant and bank has not demanded the repayment of loan upto the date of approval of the accounts. In the Indian context, the criteria of a loan becoming repayable on demand on breach of a covenant, is generally added in the terms and conditions as a matter of abundant caution. Also, banks generally do not demand repayment of loans on such minor defaults of debt covenants. Therefore, in such situations, the companies generally continue to repay the loan as per its original terms and conditions. Hence, considering that the practical implications of such minor breach are negligible in the Indian scenario, an entity could continue to classify the loan as "non-current" as on the Balance Sheet date since the loan is not actually demanded by the bank at any time prior to the date on which the Financial Statements are approved.

However, in case a bank has recalled the loan before the date of approval of the accounts on breach of a loan covenant that occurred before the year-end, the loan will have to be classified as current.

Further, the above situation should not be confused with a loan which is repayable on demand from day one. For such loans, even if the lender does not demand repayment of the loan at any time, the same would have to be continued to be classified as "current".

### **ADDITIONAL DISCLOSURE REQUIREMENTS AS PER S. III**

**I) Contingent liabilities:** It shall be classified as:

- (a) Claims against the company not acknowledged as debt;
- (b) Guarantees;
- (c) Other money for which the company is contingently liable.

**II) Commitments:** It shall be classified as:

- (a) Estimated amount of contracts remaining to be executed on capital account and not provided for;
- (b) Uncalled liability on shares and other investments partly paid;
- (c) Other commitments (specify nature).

**III) Value of imports** calculated on C.I.F basis by the company during the financial year in respect of-

- (a) Raw materials;
- (b) Components and spare parts;
- (c) Capital goods;

**IV) Expenditure in foreign currency** during the financial year on account of royalty, know-how, professional and consultation fees, interest, and other matters;

V) Total **value if all imported raw materials**, spare parts and components consumed during the financial year and the total value of all indigenous raw materials, spare parts and components similarly consumed and the percentage of each to the total consumption;

VI) The **amount remitted during the year in foreign currencies on account of dividends** with a specific mention of the total number of non-resident shareholders, the total number of shares held by them on which the dividend were due and the year to which the dividends related;

VII) Earnings in foreign exchange classified under the following heads, namely:

- a) Export of goods calculated on F.O.B. basis;
- b) Royalty, know-how, professional and consultation fees;
- c) Interest and dividend;
- d) Other income, indicating the nature thereof.

VII) Details of crypto currency & virtual currency

**PROBLEMS**

1. State under which head these accounts should be classified in Balance Sheet, as per Schedule III of the Companies Act:

- (i) Share application money received in excess of issued share capital.
- (ii) Share option outstanding account.
- (iii) Unpaid matured debenture and interest accrued thereon.
- (iv) Uncalled liability on shares and other partly paid investments.
- (v) Calls unpaid.
- (vi) Intangible Assets under development.
- (vii) Money received against share warrant.
- (viii) Long term maturity of finance lease obligation. [IPCC, May 2014, 4 Marks]

2. (i) Vasudha Ltd. provides following information:

Raw Material stock holding period: 3.5 months

Work-in-progress holding period: 1 month

Finished goods holding period: 4.5 months

Debtors collection period: 6 months

You are required to compute the operating cycle of Vasudha Ltd. What would happen if the trade payables of the company are paid in 14 months-whether these should be classified as current or non-current liability?

- (ii) The management of Kshitij Ltd. contends that the work in progress is not valued since it is difficult to ascertain the same in view of the multiple processes involved. They opine that the value of opening and closing work in progress would be more or less the same. Accordingly, the management had not separately disclosed the work in progress in its financial statements. Comment in line with Schedule III. [IPCC, Nov. 2013, 5 Marks]

3. Carrying amount of a machine is ₹ 1,00,000 (Historical cost less depreciation). The machine is expected to generate ₹ 25,000 net cash flow for 5 years. The net realizable value (or net selling price) of the machine on current date is ₹ 85,000. The enterprises required rate of earning is 10% p.a. State the value at which the enterprise should carry its machine. The present value factors at 10% are 0.909, 0.826, 0.751, 0.683 and 0.621 at the end of first, second, third, fourth and fifth year respectively. [IPCC, May 2011, 4 Marks]

## DIVISIBLE PROFITS

- ⇒ Section 2 (35) of the Companies Act, 2013, term "Dividend" includes interim dividend also.
- ⇒ A dividend is a distribution of divisible profit of a company among the members according to the number of shares held by each of them in the capital of the company and the rights attaching thereto.
- ⇒ Issue of Bonus Shares is not considered as a distribution of profits but is considered as capitalization of profits.

### GK

Berkshire Hathaway does not pay a dividend. Its chairman and CEO, Warren Buffett, believes it is more beneficial to allocate the company's earnings in other ways.

In particular, Buffett prefers to reinvest profits in things that allow his company to improve its efficiency, expand its reach, create new products and services as well as improve existing ones, and further separate itself from competitors.

The Share Price of Berkshire Hathaway is around \$ 3,00,000 i.e. approximately ₹ 2,00,00,000.

## SOURCES FROM WHICH DIVIDEND CAN BE PAID

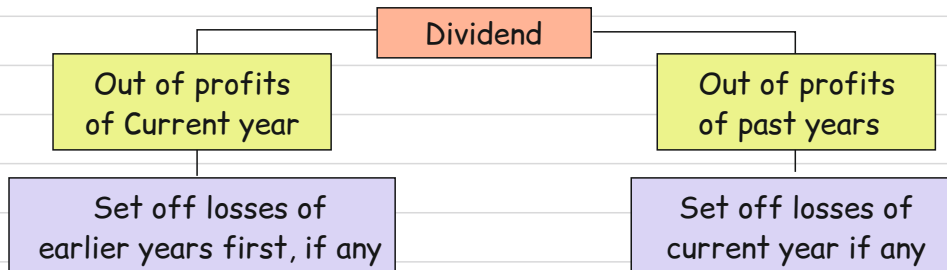
Profits of the company for that financial year arrived at after providing for depreciation	Out of the profits for any previous financial years arrived at after providing for depreciation and remaining undistributed	Out of the moneys provided by the Central Government or any State Government for the payment of dividend by the Company in pursuance of any guarantee given by that government
--	---	--

### Notes:

1. No dividend should be declared or paid by a company from its reserves, other than free reserves.
2. In computing profits any amount representing unrealized gains, notional gains or revaluation of assets and any change in carrying amount of an asset or of a liability on measurement of the asset or the liability at fair value shall be excluded.
3. **Transfer to Reserves**  
 Transfer of Profits to reserves may be made by company, overwrite, at such rates as company considers to be appropriate, before declaration of dividend.  
 Such transfer may be made by company to either General Reserve or Capital Reserve by passing resolution in General meeting or by virtue of provisions of Articles.  
 It is not mandatory to transfer profits to reserves, so there can be nil transfer as well.  
 In certain cases, mandatory transfer to reserves may be required by Act or rules. E.g. Transfer

to Debenture Redemption Reserve u/s 71(4).

4. Company shall not declare dividend unless carried over previous losses and depreciation not provided in previous year or years are set off against profit of the company for the current year.



5. **Dividend on partly paid shares:** A company may if so authorised by its Article, pay a dividend in proportion to the amount paid on each share (Section 51 of the Companies Act, 2013).

Calls in Advance: Calls paid in advance do not rank for payment of dividend.

## DECLARATION OF DIVIDEND OUT OF FREE RESERVES

A company may declare dividend out of free reserves, in the event of inadequacy or absence of profits in any year, subject to the fulfillment of following conditions:

1. The rate of dividend declared shall not exceed the average of the rates at which dividend was declared by it in the three years immediately preceding that year. This sub-rule shall not apply to a company, which has not declared any dividend in each of the three preceding financial year.
2. The total amount to be drawn from such accumulated profits shall not exceed one-tenth of the sum of its paid-up share capital and free reserves as appearing in the latest audited financial statement.
3. The amount so drawn shall first be utilized to set off the losses incurred in the financial year in which dividend is proposed to be declared before any dividend in respect of equity shares is declared.
4. The balance of reserves after such withdrawal shall not fall below fifteen per cent of its paid up share capital as appearing in the latest audited financial statement.

Note: Please note that above conditions apply only if profits were transferred to reserves. If profits were kept in Profit and Loss account itself then above conditions won't apply.

Summary:

- a) Rate of Dividend  $\leq$  Average Rate of last 3 years
- b) Amount used from Reserves  $\leq$  10% of (PUC + Free Reserves)
- c) Set off losses of current year before declaring dividend.
- d) Balance of reserves  $\geq$  15% PUC as per last audited Statement

### Illustration

Due to inadequacy of profits during the year ended 31st March, 2002, XYZ Ltd. proposes to declare 10% dividend out of general reserves. From the following particulars, ascertain the amount that can be utilised from general reserves, according to the Companies (Declaration of dividend out of Reserves) Rules, 2014:

	₹
17,500 9% Preference shares of ₹ 100 each, fully paid up	17,50,000
8,00,000 Equity shares of ₹ 10 each, fully paid up	80,00,000
General Reserves as on 1.4.2001	25,00,000
Capital Reserves as on 1.4.2001	3,00,000
Revaluation Reserves as on 1.4.2001	3,50,000
Net profit for the year ended 31st March, 2002	3,00,000
Average rate of dividend during the last five year has been 12%.	

#### Solution:

Amount that can be drawn from reserves for 10% dividend

10% dividend on ₹ 80,00,000	₹ 8,00,000
Profits available	
Current year profit	3,00,000
Less: Preference dividend	(1,57,500)      (1,42,500)
Amount which can be utilised from reserves	<u>6,57,500</u>

#### Conditions as per Companies (Declaration of dividend out of Reserves) Rules, 2001:

##### Condition I

Since 10% is lower than the average rate of dividend (12%), 10% dividend can be declared.

##### Condition II

Maximum amount that can be drawn from the accumulated profits and reserves should not exceed 10% of paid up capital plus free reserves i.e. ₹ 12,25,000 [10% of (80,00,000 + 17,50,000 + 25,00,000)]

##### Condition III

The balance of reserves after drawl ₹ 18,42,500 (₹ 25,00,000 - ₹ 6,57,500) should not fall below 15 % of its paid up capital i.e. ₹ 14,62,500 (15% of ₹ 97,50,000]

Since all the three conditions are satisfied, the company can withdraw ₹ 6,57,500 from accumulated reserves. (as per Declaration and Payment of Dividend Rules, 2014.)

## DECLARATION OF INTERIM DIVIDEND

⇒ When Interim Dividend can be declared?

The Board of Directors of a company may declare interim dividend

- during any financial year or
- at any time during the period from closure of financial year till holding of the annual general meeting

⇒ Which Profits can be used to pay Interim Dividend?

Interim Dividend can be declared

- out of the surplus in the profit and loss account or
- out of profits of the financial year for which such interim dividend is sought to be declared or
- out of profits generated in the financial year till the quarter preceding the date of declaration of the interim dividend

**Provided** that in case the company has incurred loss during the current financial year up to the end of the quarter immediately preceding the date of declaration of interim dividend, such interim dividend shall not be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.

**Example:** If BOD of Company X wants to declare an interim dividend on 3rd August 2018, but Company X has suffered a loss until the end of the quarter immediately preceding the date of declaration i.e. Quarter 1 (upto 30th July 2018), then interim dividend cannot be declared at a rate higher than the average dividends declared by the company during the immediately preceding three financial years.

## TIMELINE

