# FREQUENTLY ASKED QUESTIONS:

# FINANCIAL STATEMENTS

### *What do we mean by three financial statements?*

The 3 major financial statements are the Income Statement, Balance Sheet and Cash Flow Statement.

The Income Statement gives the company's revenue and expenses, and goes down to Net Income, the final line on the statement.

The Balance Sheet shows the company's Assets – its resources – such as Cash, Inventory and PP&E, as well as its Liabilities – such as Debt and Accounts Payable – and

Shareholders' Equity. Assets must equal Liabilities plus Shareholders' Equity.

The Cash Flow Statement begins with Net Income, adjusts for non-cash expenses and working capital changes, and then lists cash flow from investing and financing activities; at the end, you see the company's net change in cash."

### *What do three financial statements link with each other?*

The three statements link together as follows:

Net Income from the Income Statement flows into Shareholders' Equity on the Balance Sheet, and into the top line of the Cash Flow Statement.

Changes to Balance Sheet items appear as working capital changes on the Cash Flow.

Statement, and investing and financing activities affect Balance Sheet items such as

PP&E, Debt and Shareholders' Equity. The Cash and Shareholders' Equity items on the Balance Sheet act as "plugs," with Cash flowing in from the final line on the Cash Flow Statement.

### *What is meant by Accounts Payable?*

Accounts payable is a current liability account on the balance sheet representing the total amount of bills owed by the company to creditors.

### *What is the treatment in Financial Statements in writing down an Accounts Payable of say Rs.1000?*

The treatment in three statements is as follows:

When an *Accounts payable* is written down we record it as a gain on the Income Statement – so Pre-Tax Income goes up by Rs.1000 due to this write-down. Assuming a 30% tax rate, Net Income is up by Rs.700.

On the Cash Flow Statement, Net Income is up by Rs. 700, but we need to **subtract** that Accounts payable write-down – so Cash Flow from Operations is down by Rs. 300, and Net Change in Cash is down by Rs. 300.

On the Balance Sheet, cash is down by Rs.300 so Assets are down by Rs.300. On the other side, Debt is down by Rs.1000 but Shareholders' Equity is up by Rs. 700 because the Net Income was up by Rs. 700 – so Liabilities & Shareholders' Equity is down by Rs. 300 and it balances.

### How do we define Accounts Receivable?

Accounts receivable is a current asset account on the balance sheet representing the open invoices paid by a company's customers.

### What is the treatment in three financial statements when we write down Accounts Receivable? Please explain with an example with Accounts Receivable of Rs.1000.

The treatment is as follows:

First, on the Income Statement, the Rs.1000 write-down shows up in the Pre-Tax Income line. With a 30% tax rate, Net Income declines by Rs. 700.

On the Cash Flow Statement, Net Income is down by Rs. 700 but the write-down is a noncash expense, so we add it back – and therefore Cash Flow from Operations increases by Rs. 300.

Overall, the Net Change in Cash rises by Rs. 300.

On the Balance Sheet, Cash is now up by Rs. 300 and *accounts receivable* is down by Rs.1000. Overall, the Assets side is down by Rs. 700.

On the other side, since Net Income was down by Rs.700, Shareholders' Equity is also down by Rs.700 – and both sides balance.

### What is meant by Accrual basis of accounting?

Accrual basis of accounting is where you will record a transaction for your financial statements even if that transaction has not affected the cash balance in your bank account yet.

### What is the difference between cash-based accounting and accrual accounting?

Cash-based accounting recognizes revenue and expenses when cash is actually received or paid out; while accrual accounting recognizes revenue when collection is *reasonably certain* (i.e. after a customer has ordered the product) and recognizes expenses when they are incurred rather than when they are paid out in cash.

### If a customer pays for an Air conditioner purchases through credit card what would this look like under cash-based vs. accrual accounting?

In cash-based accounting, the revenue would not show up until the company charges the customer's credit card, receives authorization, and deposits the funds in its bank account – at which point it would show up as both Revenue on the Income Statement and Cash on the Balance Sheet.

In accrual accounting, it would show up as Revenue right away but instead of appearing in Cash on the Balance Sheet, it would go into Accounts Receivable at first. Then, once the cash is actually deposited in the company's bank account, it would "turn into" Cash.

### What is meant by Allocation methodology?

Allocation is a methodology that a company uses to split indirect costs by hours, production units, or other cost drivers.

### *What is meant by Amortization?*

Amortization is how an intangible assets cost is spread out over time. Approval authority is an internal control that specifically and explicitly states who can purchase what and how much for a company.

### *What is meant by Assets?*

Assets are items that have value to a company that can be used to generate cash flow. Assets can include property, buildings, truck or car fleets, machinery, inventory, among many.

### *What is meant by Asset access control?*

Asset access controls is an internal control strategy that ensures that assets that have a value that could cause theft are handled in ways that ensure they are not stolen – including asset tags, inventory counts, and restricting access by locked storage.

### *How do we define Audit?*

Audits are a common practice whereby accountants examine the business standard operating procedures, especially those that impact assets, for adherence to policy as a way of determining if a company is at risk with the management of any of its assets.

### *What is a Balance Sheet?*

Balance sheet is a financial statement that provides information about a business's assets, liabilities, and equity. Under IFRS it is called Statement of Financial Position (SOFP). The broad components of Balance Sheet include, Cash; Accounts Receivable; Inventory; Plants, Property & Equipment (PP&E); Accounts Payable; Accrued Expenses; Debt; Shareholders' Equity

### *What is meant by Cash basis of accounting*

As explained above Cash basis of accounting is where you will record a transaction for your financial statements only when the transaction has impacted the cash balance in your bank account.

### *What is Cash conversion cycle?*

Cash conversion cycle is a metric that combines information regarding accounts receivable, accounts payable, and inventory to examine how well these working capital accounts are turning and generating or using cash in the business.

### *What is meant by Cash flow statement?*

Cash flow statement is a financial statement that analyzes how cash has been generated and used in the company. This is a reconciliation of the cash balance that exists on the balance sheet. The Cash flow statement includes Net Income; Depreciation & Amortization; Stock-Based Compensation; Changes in Operating Assets & Liabilities; Cash Flow from Operations; Capital Expenditures; Cash Flow from Investing; Sale / Purchase of Securities; Dividends Issued; Cash Flow from Financing.

### *What is meant by Fund flow statement?*

The fund flow statement is a report on the movement of funds or working capital. It explains how working capital is raised and used during an accounting period.

### *What are the components of equity under Financial Statements?*

Components of equity are as under:

**Equity**

**I. Equity Share Capital**

for each class of equity share capital:

(a) the number and amount of shares authorised;

(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 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 percent 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:
- Aggregate number and class of shares allotted as fully paid up pursuant to contract(s) without payment being received in cash.
- Aggregate number and class of shares allotted as fully paid up by way of bonus shares.
- Aggregate number and class of shares bought back.

(j) Terms of any securities convertible into equity 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) A company shall disclose Shareholding of Promoters* as under:

| Shares held by promoters at the end of the year | | | | % Change during the year*** |
|---|---|---|---|---|
| S. No. | Promoter name | No of shares ** | % of total shares | |
| | | | | |

*Promoter here means promoter as defined in the Companies Act, 2013.

** Details shall be given separately for each class of shares

*** percentage change shall be computed with respect to the number at the beginning of the year or if issued during the year for the first time then with respect to the date of issue

### *What is meant by capital?*

Under a financial concept of capital, such as invested money or invested purchasing power, capital is synonymous with the net assets or equity of the enterprise. Under a physical concept of capital, such as operating capability, capital is regarded as the productive capacity of the enterprise based on, for example, units of output per day.

### *What is meant by Equity share capital?*

Aggregate amount of money paid or credited as paid on the shares and/or stocks of a corporate enterprise.

Equity share capital is offered to the public for an ownership stake in the company. This is a way that a corporation can generate cash by making new offerings of stock on the stock exchange.

### *What is meant by Authorised Share Capital?*

Authorised Share Capital represents the number and par value, of each class of shares that an enterprise may issue in accordance with its instrument of incorporation. This is sometimes referred to as nominal share capital.

### *What is meant by Subscribed Share Capital?*

Subscribed Share Capital represents that portion of the issued share capital which has actually been subscribed and allotted. This includes any bonus shares issued to the shareholders.

### *What is meant by Paid-up Share Capital?*

Paid-up Share Capital represents that part of the subscribed share capital for which consideration in cash or otherwise has been received. This includes bonus shares allotted by the corporate enterprise.

### *What does Other Equity comprise?*

Other Equity would include the following:

(a) Share application money pending allotment;

(b) Equity component of compound financial instruments;

(c) Reserves and Surplus:

- (i) Capital Reserve;
- (ii) Securities Premium;
- (iii) Other Reserves (specify nature);
- (iv) Retained Earnings;

(d) Debt instruments at fair value through other comprehensive income;

(e) Equity instruments at fair value through other comprehensive income;

(f) Effective portion of Cash Flow Hedges;

(g) Revaluation Surplus;

(h) Exchange differences on translating the financial statements of a foreign operation;

(i) Other items of other comprehensive income (specify nature);

(j) Money received against share warrants;

(k) Non-controlling interests (for Statement of Changes in Equity of Consolidated Financial Statements.

### *What is meant by Reserves?*

Reserve is defined as the portion of earnings, receipts or other surplus of an enterprise (whether capital or revenue) appropriated by the management for a general or a specific purpose other than a provision for depreciation of diminution in the value of assets or for a known liability.

### *When is capital redemption reserve created?*

Capital Redemption Reserve is required to be created in the followings situations:

(a) where the redemption of preference shares is out of profits, an amount equal to nominal value of shares redeemed is to be transferred to a reserve called capital redemption reserve

(b) if the buy-back of shares is out of the free reserves, the nominal value of the shares so purchased is required to be transferred to capital redemption reserve from distributable profit.

### *When is Debenture redemption reserve created?*

Where a company issues debenture, it is required to create a debenture redemption reserve for the redemption of such debentures. The company is required to credit adequate amounts, from out of its profits every year to debenture redemption reserve, until such debentures are redeemed.

On redemption of the debentures for which the reserve is created, the amounts no longer necessary to be retained in this account need to be transferred to the General Reserve.

### *What is meant by capital reserve?*

Capital reserve is defined as a reserve of a corporate enterprise which is not available for distribution as dividend.

### *What does Securities Premium stand for?*

Securities Premium stands for "excess of the issue price of shares over their face value". Security premium reserve is a reserve created for the equivalent amount under Other Equity.

### *How is gain / loss on the changes in the proportion held by non-controlling interest presented?*

An entity needs to recognize directly in 'Equity' any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received, and attribute it to the owners of the parent.

An entity may present such gain / loss separately as 'Gain/Loss on change in proportion held by non-controlling interests' shown under 'Other Reserves' by specifying the nature of such gain / loss.

### *What is meant by Retained earnings?*

Retained Earnings represent surplus i.e. balance of the relevant column in the Statement of Changes in Equity.

### *How is debit balance of profit and loss treated?*

Debit balance of Statement of Profit and Loss shall be shown as a negative figure under the head 'retained earnings'. Similarly, the balance of 'Other Equity', after adjusting negative balance of retained earnings, if any, shall be shown under the head 'Other Equity' even if the resulting figure is in the negative.

### *How is Share application money pending allotment presented in financial statements?*

Share Application money pending allotment is presented as a separate line item under Other Equity. Share application money pending allotment shall be classified into equity or liability. Share application money to the extent not refundable shall be shown in this line item.

Share application money to the extent refundable shall be separately shown under 'other financial liabilities'

### *How is Equity component of compound financial instruments presented in financial statements?*

Equity component is required to be presented as a part of 'Other Equity' under this head. On the other hand, the 'liability component of compound financial instrument' is required to be presented as a part of 'Borrowings'.

### *How are debt instruments through other comprehensive income treated?*

Investments are measured at Fair Value through Other Comprehensive Income based on the company's business model for managing the portfolio of debt instruments as well as the debt instruments' contractual cash flow characteristics. Any fair value gain or loss on debt instruments measured at FVOCI is presented as a part of Other Equity under this heading until the debt instrument is derecognized.

### *How are equity instruments through other comprehensive income treated?*

Companies have an option to designate investments in equity instruments to be measured at FVOCI. For such instruments, the cumulative fair value gain or loss is presented as a part of Other Equity under this heading.

### *How is effective portion of cash flow hedges treated?*

With respect to cash flow hedges, this component of Other Equity associated with the hedged item (i.e. cash flow hedge reserve) is adjusted to the lower of the cumulative change in the fair value of the hedging instrument and the cumulative change in the fair value of the hedged item attributable to the hedged risk.

The portion of the gain or loss on the hedging instrument that is determined to be an effective hedge (i.e. the portion that is offset by the change in the cash flow hedge reserve) is recognised in Other Comprehensive Income.

IFRS standards require that exchange differences on monetary items that qualify as hedging instruments in a cash flow hedge are recognised initially in other comprehensive income to the extent that the hedge is effective.

### *What is meant by Revaluation surplus?*

In accordance with IFRS Standard on Property, Plant and Equipment if an asset's carrying value is increased as a result of revaluation, such increase shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus. However, such increase shall be recognised in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognized in profit or loss.

### *How is exchange difference in translating financial statements under foreign operations treated?*

Pursuant to relevant IFRS Standard, the exchange differences arising on translation of the financial statements of foreign operation from functional currency to presentation currency needs to be included in this head of Other Comprehensive Income.

### *How is money received under share warrants treated?*

IFRS Standards defines 'warrants' as "financial instruments which give the holder the right to acquire equity shares".

Since shares are yet to be allotted against the same, these are not reflected as part of Share Capital but as a separate line item – 'Money received against share warrants

### *What do lease liabilities represent?*

Lease liabilities under non-current liabilities represent principal amount of such lease liability payable beyond a period of 12 months from the reporting date. Lease liabilities are to be presented under non-current financial liabilities as a line item separately from borrowings. The disclosure requirements stated above for borrowings shall not be applicable to lease liabilities.

### *What are deferred payment liabilities?*

Deferred payment liabilities would include any liability for which payment is to be made on deferred credit terms, e.g. deferred sales tax liability, deferred payment for acquisition of Property, Plant and Equipment etc.

### *What is liability component of compound instruments?*

With respect to IFRS standards, disclosure requirements as applicable to 'Borrowings' should be given for compound instruments with liability component in nature (for e.g., those instruments which entirely meet the definition of a financial liability.

### *What is security and guarantee by promoters, directors or others related to borrowings?*

Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head need to be disclosed. The word "others" used in the phrase "directors or others" would mean any person or entity other than a director. Therefore, this is not restricted to mean only related parties. Also, in cases where promoters, other shareholders or any third party have given any personal security for any borrowing, such as shares or other assets held by them, disclosure should be made thereof, though such security does not result in the classification of such borrowing as secured.

### *How are redemption of bonds / debentures treated?*

Bonds/debentures (along with the rate of interest and particulars of redemption or conversion, as the case may be) shall be stated in descending order of maturity or conversion, starting from farthest redemption or conversion date, as the case may be. Where bonds/debentures are redeemable by instalments, the date of maturity for this purpose must be reckoned as the date on which the first instalment becomes due. Particulars of any redeemed bonds/ debentures which the company has power to reissue need to be disclosed.

### *How do we define contractors?*

Contractors are individuals you hire that are paid separately from payroll and they may only work for you for a project or a shorter period time. Contractors receive a 1099 at year-end under US laws.

### *What do contract liabilities represent?*

In accordance with IFRS Standards on revenue from contract with customers, contract liability needs to be presented in Balance Sheet, when either party has performed, a contract liability related to a contract with customers. Contract liability occurs if a customer pays consideration, or an entity has a right to an amount of consideration that is unconditional (i.e. a receivable), before the entity transfers a good or service to the customer, the entity shall present the contract as a contract liability when the payment is made or the payment is due (whichever is earlier).

### *What are the components of borrowings under non-current liabilities?*

Components of borrowings under non-current liabilities are as under:

**Borrowings**

(i) Borrowings shall be classified as:
  - (a) Bonds/debentures
  - (b) Term loans
    - I from banks.
    - II from other parties.
  - (c) Deferred payment liabilities.
  - (d) Deposits.
  - (e) Loans from related parties.
  - (f) Long term maturities of finance lease obligations
  - (g) Liability component of compound financial instruments
  - (h) Other loans (specify nature).

(ii) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.

(iii) Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed.

(iv) Bonds/debentures (along with the rate of interest, and particulars of redemption or conversion, as the case may be) shall be stated in descending order of maturity or conversion, starting from farthest redemption or conversion date, as the case may be. Where bonds/debentures are redeemable by instalments, the date of maturity for this purpose must be reckoned as the date on which the first instalment becomes due.

(v) Particulars of any redeemed bonds/ debentures which the company has power to reissue shall be disclosed.

(vi) Terms of repayment of term loans and other loans shall be stated.

(vii) Period and amount of default as on the balance sheet date in repayment of borrowings and interest shall be specified separately in each case.

### *What are the components of other financial liabilities?*

Components of other financial liabilities are as follows:

**Other Financial Liabilities**

Other Financial liabilities shall be classified as:

(a) Omitted
(b) Omitted
(c) Interest accrued;
(d) Unpaid dividends;
(e) Application money received for allotment of securities to the extent refundable and interest accrued thereon;
(f) Unpaid matured deposits and interest accrued thereon;
(g) Unpaid matured debentures and interest accrued thereon;
(h) Others (specify nature).

'Long term debt' is a borrowing having a period of more than twelve months at the time of origination

### *How are current liabilities defined?*

Current liabilities are the bills due for a company in a time frame of a year or less. The most common account in current liabilities is the accounts payable balance.

### *How are current liabilities classified?*

Current liabilities are classified as follows:

**I. Borrowings**

(i) Borrowings shall be classified as:
  (a) Loans repayable on demand
    (I) from banks.
    (II) from other parties.
  (b) Loans from related parties.
  (c) Deposits.
  (d) Other loans (specify nature).

(ii) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.

(iii) Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed.

(iv) Period and amount of default as on the balance sheet date in repayment of borrowings and interest, shall be specified separately in each case.

**II. Other Financial Liabilities**

Other Financial liabilities shall be classified as:

(a) Current maturities of long-term debt;
(b) Current maturities of finance lease obligations;
(c) Interest accrued;
(d) Unpaid dividends;
(e) Application money received for allotment of securities to the extent refundable and interest accrued thereon;
(f) Unpaid matured deposits and interest accrued thereon;
(g) Unpaid matured debentures and interest accrued thereon;
(h) Others (specify nature).

'Long term debt' is a borrowing having a period of more than twelve months at the time of origination

**III. Other current liabilities**

The amounts shall be classified as:

(a) Revenue received in advance;
(b) Other advances (specify nature);
(c) Others (specify nature)

**IV. Provisions**

The amounts shall be classified as:

(i) Provision for employee benefits.
(ii) Others (specify nature).

The presentation of liabilities associated with group(s) of assets classified as held for sale and non-current assets classified as held for sale shall be in accordance with the relevant IFRS Standards.

## *What are loans payable on demand?*

Loans payable on demand should be treated as part of current borrowings. Current borrowings will include all loans payable within a period of 12 months from the date of the loan.

In the case of current borrowings, the period and amount of defaults existing as at the date of the Balance Sheet needs to be disclosed (item-wise).

## *What is meant by current maturities of long-term borrowing?*

The portion of non-current borrowings, which is due for payments within twelve months of the reporting date is required to be classified under "current maturities of long-term borrowings" while the balance amount should be classified under non-current borrowings.

## *What are the disclosure requirements related to Trade Payables?*

Disclosure requirements related to Trade Payables are:

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 (27 of 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 has 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.

For trade payables due for payment, the following ageing schedule shall be given:

Trade Payables aging schedule (Amount in Rs.)

| Particulars | Outstanding for following periods from due date of payment# | | | | |
|---|---|---|---|---|---|
| | Less than one year | One to two years | Two to three years | More than three years | Total |
| (i) MSME<br>(ii) Others | | | | | |
| (iii) Disputed dues - MSME<br>(iv) Disputed dues -others | | | | | |

# similar information shall be given where no due date of payment is specified in that case disclosure shall be from the date of the transaction.

Unbilled dues shall be disclosed separately.

### *What is the disclosure requirement related to Contingent liabilities and Commitments?*

Disclosure requirement related to Contingent liabilities and contingent assets is as under:

**Contingent Liabilities and Commitments (to the extent not provided for)**

(i) Contingent Liabilities shall be classified as:
- (a) Claims against the company not acknowledged as debt;
- (b) Guarantees excluding financial guarantees;
- (c) Other money for which the company is contingently liable.

(ii) Commitments 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).

### *How are non-current assets classified and disclosed?*

Non-current assets are classified and disclosed as follows:

**Non-Current Assets**

**I. Property, Plant and Equipment**

(i) Classification shall be given as:
   (a) Land.
   (b) Buildings.
   (c) Plant and Equipment.
   (d) Furniture and Fixtures.
   (e) Vehicles.
   (f) Office equipment.
   (g) Bearer Plants
   (h) Others (specify nature).

(ii) Assets under lease shall be separately specified under each class of assets.

(iii) 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

***How are investment properties disclosed?***

Investment properties are disclosed as follows:

**Investment Property**

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

***How is goodwill presented in Financial Statements?***

Goodwill is presented in Financial Statements as follows:

**Goodwill**

A reconciliation of the gross and net carrying amount of goodwill at the beginning and end of the reporting period showing additions, impairments, disposals and other adjustments.

***How are other intangible assets presented and disclosed in Financial Statements?***

Other intangible assets are disclosed as follows:

**Other Intangible assets**

(i) Classification shall be given as:
   (a) Brands /trademarks.
   (b) Computer software.
   (c) Mastheads and publishing titles.
   (d) Mining rights.
   (e) Copyrights, patents, other intellectual property rights, services and operating rights.
   (f) Recipes, formulae, models, designs and prototypes.
   (g) Licenses and franchises.
   (h) Others (specify nature).

(ii) 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 amortisation and impairment losses/reversals shall be disclosed separately.

### How are current assets defined?

Current assets are the assets converted to cash in the time frame of a year or less. These include cash (which is are already in its final form of cash), accounts receivable, and inventory.

### What are the constituents of current investments?

Current investments include:

(a) Investments in Equity Instruments.

(b) Investment in Preference Shares;

(c) Investments in government or trust securities.

(d) Investments in debentures or bonds.

(e) Investments in Mutual Funds;

(f) Investments in partnership firms;

(g) Other investments (specify nature).

### What are the constituents of inventories?

Constituents of inventories are as follows:

(a) Raw materials;
(b) Work-in-progress;
(c) Finished goods;
(d) Stock-in-trade (in respect of goods acquired for trading);
(e) Stores and spares;
(f) Loose tools;
(g) Others (specify nature).

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

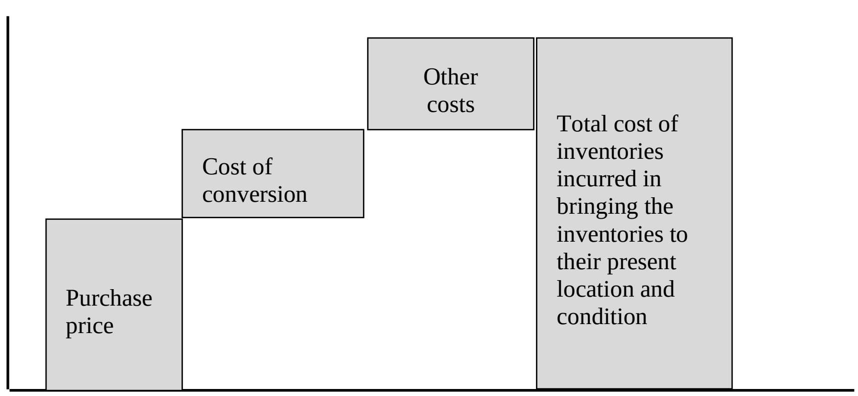
Mode of valuation shall be stated.

### How are inventories measured?

Inventories shall be measured at lower of cost and net realisable value.

### What are the elements of costs considered while valuing inventories?

The cost of inventories shall comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.



***What is the disclosure requirement of loans or advances in the nature of loans to promoters, directors, KMPs and other related parties?***

**Disclosure of Loans or Advances in the nature of loans to promoters, directors, KMPs and other related parties**

The following disclosures shall be made where Loans or Advances in the nature of loans are granted to promoters, directors, KMPs and the related parties (as defined under Companies Act, 2013), either severally or jointly with any other person, that are:

(a) repayable on demand; or

(b) without specifying any terms or period of repayment,

| Type of Borrower | Amount of loan or advance in the nature of loan outstanding | Percentage to the total Loans and Advances in the nature of loans |
|---|---|---|
| Promoters | | |
| Directors | | |
| KMPs | | |
| Related Parties | | |

***What are the disclosure requirements related to Capital Work-in-progress?***

Capital-Work-in Progress (CWIP)

(a) For Capital-work-in progress, following ageing schedule shall be given: CWIP aging schedule (amount in Rs)

| CWIP | Amount in CWIP for a period of | | | | Total* |
|---|---|---|---|---|---|
| | Less than 1 year | 1-2 years | 2-3 years | More than 3 years | |
| Projects in progress<br>Projects temporarily suspended | | | | | |

*Total shall tally with CWIP amount in the balance sheet.

(b) For capital-work-in progress, whose completion is overdue or has exceeded its cost compared to its original plan, following **CWIP completion schedule** shall be given**:**

(Amount in Rs.)

| CWIP | To be completed in | | | |
|---|---|---|---|---|
| | Less than 1 year | 1-2 years | 2-3 years | More than 3 years |
| Project 1 Project 2” | | | | |

**Details of projects where activity has been suspended shall be given separately.

***What are the disclosure requirements related to Intangible assets under development?***

**Intangible assets under development:**

(a) For Intangible assets under development, following ageing schedule shall be given:

**Intangible assets under development aging schedule** (Amount in Rs.)

| Intangible assets under development | Amount in CWIP for a period of | | | | Total* |
|---|---|---|---|---|---|
| | Less than 1 year | 1-2 years | 2-3 years | More than 3 years | |
| Projects progress in Projects temporarily suspended | | | | | |

***** Total shall tally with the amount of Intangible assets under development in the balance sheet.

(b) For Intangible assets under development, whose completion is overdue or has exceeded its cost compared to its original plan, the following **Intangible assets under development completion schedule** shall be given**:

Amount in Rs.)

| Intangible assets under development | To be completed in | | | |
|---|---|---|---|---|
| | Less than 1 Year | 1-2 years | 2-3 years | More than 3 years |
| Project 1 Project 2 | | | | |

**Details of projects where activity has been suspended shall be given separately

### *What is meant by cycle counting?*

Cycle counting is a methodology that some companies use to manage inventory count. Rather than counting all inventory once a year, you will divide your inventory into categories looking at the value of the inventory and the turnover rates.

### *What does a Statement of Profit & loss represent? What does it include?*

Financial Statement which presents the revenues and expenses of an enterprise for an accounting period and shows the excess of revenues over expenses (or vice versa) It is also known as profit and loss account.
A Statement of Profit & Loss includes, Revenue from operations; Cost of Goods Sold; SG&A (Selling, General & Administrative Expenses); Operating Income; Pretax Income; Net Income.

### *What are the presentation requirements related to Statement of Profit and Loss?*

Revenue from Operations

Other Income

Total Income (I + II)

EXPENSES:

Cost of material consumed

Purchases of stock-in-trade

Changes in inventories of finished goods, stock-in-trade and work-in-progress

Employees benefit expenses

Finance cost

Depreciation and amortisation expenses

Other expenses

Total expenses (IV)

Profit/(loss) before exceptional items and tax (I- IV)

Exceptional items

Profit/(loss) before tax (V-VI)

Tax expenses:

(a) Current tax

(b) Deferred tax

Profit (Loss) for the period from continuing operations (VII-VIII)

Profit / (loss) from discontinued operations

Tax expenses from discontinued operations

Profit / (loss) from discontinued operations (X-XI)

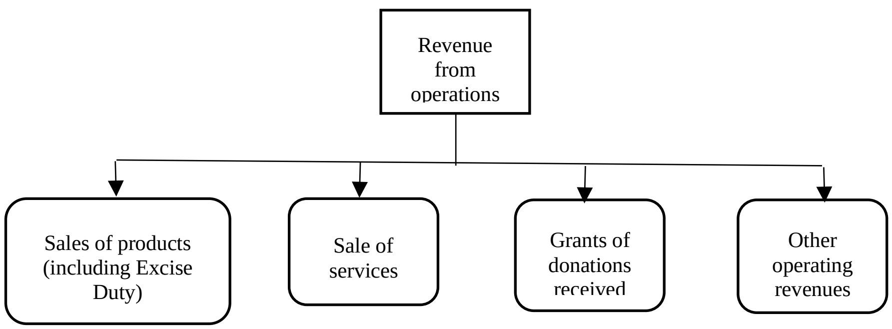
Profit/(loss) for the period (IX+XII)
Other Comprehensive Income
A (i) Items that will not be reclassified to profit or loss
(ii) Income tax relating to items that will not be reclassified to profit or loss
B (i) Items that will be reclassified to profit or loss
(ii) Income tax relating to items that will be reclassified to profit or loss

Total Comprehensive Income for the period (XIII+XIV)
(Comprising Profit (Loss) and Other Comprehensive Income for the period)
Earning per equity share (for continuing operations):

(1) Basic
(2) Diluted
Earning per equity share (for discontinued operations):
(1) Basic
(2) Diluted
Earnings per equity share (for discontinued & continuing operations)
(1) Basic
(2) Diluted

### *What does revenue from operations include?*

Revenue from operations include the following:
Revenue from operations shall disclose separately in the notes
(a) sale of products (including Excise Duty);
(b) sale of services;
(ba) Grants or donations received (relevant in case of section 8 companies only);
(c) other operating revenues




### *What does other comprehensive income include?*

Other comprehensive income includes the following:

(A) Items that will not be reclassified to profit or loss
(i) Changes in revaluation surplus;
(ii) Re-measurements of the defined benefit plans;
(iii) Equity Instruments through Other Comprehensive Income;
(iv) Fair value changes relating to own credit risk;
(v) Share of Other Comprehensive Income in Associates and Joint Ventures, to the extent not to be classified into profit or loss;
(vi) Others (specify nature).

(B) Items that will be reclassified to profit or loss
(i) Exchange differences in translating the financial statements of a foreign operation;
(ii) Debt Instruments through Other Comprehensive Income;
(iii) The effective portion of gains and loss on hedging instruments in a cash flow hedge;
(iv) Share of Other Comprehensive Income in Associates and Joint Ventures, to the extent to be classified into profit or loss;
(v) Others (specify nature).

### *What is meant by Deferred revenue?*

Deferred revenue represents revenue that cannot yet be recognized on the profit and loss statement.

### *What are the constituents of expenses?*

Constituents of expenses are as follows:

- Cost of materials consumed
- Purchases of stock – in – trade
- Changes in inventories of finished goods, work in progress and stock in trade
- Employee benefits expense
- Finance costs
- Depreciation and amortisation expenses
- Other expenses

### *What are cost drivers?*

Cost driver is an activity that drives costs to go up or down. Example: Hiring new employees is a driver of costs of software subscriptions, salaries, healthcare, etc.

### *What is meant by Cost of goods sold?*

Cost of goods sold represents the costs of manufacturing or assembling the products sold or the costs of the services the company provides to consumers.

### *How do we define employees?*

Employees are people that work for you part-time or full-time and are paid through a payroll system.

### *What do employee benefit expenses comprise? What do they represent?*

In general Employee benefits expense comprise information regarding aggregate expenditure on:

(a) Salaries and wages

(b) Contribution to Provident and other funds

(c) Staff welfare expenses

Employee benefits are all forms of considerations given by an entity in exchange of service rendered by the employees.

These are:

- Short term benefits:
- Post-employment benefits:
- Other long-term benefits:
- Termination benefits:

### *What do finance costs include?*

Finance costs include the following:

(a) interest;

(b) dividend on redeemable preference shares;

(c) exchange differences regarded as an adjustment to borrowing costs;

(d) other borrowing costs (specify nature).

### *What is meant by Depreciation?*

Depreciation is a method of expensing a tangible asset over its useful life.

### *If depreciation increases by Rs. 1000, how does it impact Financial Statements?*

The impact is as follows:

Income Statement: Operating Income would decline by Rs.1000 and assuming a 30% tax rate, Net Income would go down by Rs.700.

Cash Flow Statement: The Net Income at the top goes down by Rs.700, but the Rs.1000 depreciation is a non-cash expense that gets added back, so overall Cash Flow from Operations goes *up* by Rs.300. There are no changes elsewhere, so the overall Net Change in Cash goes up by Rs.300.

Balance Sheet: Plants, Property & Equipment goes down by Rs.1000 on the Assets side because of the Depreciation, and Cash is up by Rs.300 from the changes on the Cash Flow Statement.

Overall, Assets is down by Rs.700. Since Net Income fell by Rs.700 as well, Shareholders' Equity on the Liabilities & Shareholders' Equity side is down by Rs. 700 and both sides of the Balance Sheet balance.

### *If depreciation is a non-cash expense, why does it impact cash balance?*

Although Depreciation is a non-cash expense, it is tax-deductible. Since taxes *are* a cash expense, Depreciation affects cash by reducing the amount of taxes we pay.

### *Where is Depreciation usually disclosed on the Income Statement?*

It could be in a separate line item, or it could be embedded in Cost of Goods Sold or Operating Expenses – every company does it differently. Note that the end result for accounting questions is the same: Depreciation always reduces Pre-Tax Income.

### *What are direct costs?*

Direct costs are those costs that can be traced directly to your product or service.

### *What is the treatment if accrued compensation goes up by Rs.1000?*

First it needs to be confirmed that the accrued compensation is now being recognized as an expense (as opposed to just changing non-accrued to accrued compensation).

Assuming that is the case, Operating Expenses on the Income Statement go up by Rs.1000, Pre-Tax Income falls by Rs.1000, and Net Income falls by Rs.700 (assuming a 30% tax rate).

On the Cash Flow Statement, Net Income is down by Rs.700, and Accrued Compensation will *increase* Cash Flow by Rs.1000, so overall Cash Flow from Operations is up by Rs.300 and the Net Change in Cash at the bottom is up by Rs.300.

On the Balance Sheet, Cash is up by Rs.300 as a result, so Assets are up by Rs.300. On the Liabilities & Equity side, Accrued Compensation is a liability so Liabilities are up by Rs.1000 and Retained Earnings are down by Rs.70 due to the Net Income, so both sides balance.

### *What is discretionary income or loss?*

Discretionary income or loss is a term used by individuals to show the amount of money left over after all bills have been paid. It is a comparable concept to thinking about the net income or loss that a company earns.

### *What do exceptional items include?*

Exceptional items would include broadly the following:

(a) Write-downs of inventories to net realisable value or of property, plant and equipment to recoverable amount, as well as reversals of such write-downs;

(b) restructurings of the activities of an entity and reversals of any provisions for the costs of restructuring;

(c) disposals of items of property, plant and equipment;

(d) disposals of investments;

(e) discontinued operations;

(f) litigation settlements; and

(g) other reversals of provisions.

In case the company has more than one such item of income / expense of the above nature which is exceptional, then such items need to be disclosed on the face of the Statement of Profit and Loss.

Details of the individual items need to be disclosed in the Notes.

### *What are discontinuing operations?*

Discontinuing operations are operations that have either been disposed of or is classified as held for sale and:

(a) represents a separate major line of business or geographical area of operations,

(b) is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or

(c) is a subsidiary acquired exclusively with a view to resale. Profit or loss from

Discontinued Operations needs to be separately disclosed on the face of Statement of Profit and Loss.

### *What is meant by Drawing?*

Draw is an amount of money that a small business owner may pull out of the business rather than taking a salary from the business.

### *How do we define EBIT?*

Earnings Before Interest and Taxes (EBIT) is a number that shows you how well the operations are doing in a business. While interest and taxes occur in a business, those are not operating expenses.

### *What is meant by EBITDA?*

Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) is a number that takes out the effect of non-operating expenses of interest and taxes and takes out non-cash expenses of depreciation and amortization.

### *A company has been reflecting positive EBITDA for the past 10 years, but it recently went bankrupt. How could this happen?*

There could be the following possibilities:

- The company has been spending too much on Capital Expenditure – these are not reflected at all in EBITDA, but it could still be cash-flow negative.
- The company may incur high interest expense and is no longer able to afford its debt.
- All of the company's debt mature on one date and it is unable to refinance it due to a "credit crunch" – and it runs out of cash completely when paying back the debt.
- It has significant one-time charges (from litigation, for example) and those are high enough to bankrupt the company.

We need to remember, EBITDA excludes investment in (and depreciation of) long-term assets, interest and one-time charges – and all of these could end up bankrupting the company.

### *What is meant by negative shareholders' equity?*

Yes, this is possible in the following cases:

- Leveraged Buyouts with dividend recapitalizations – it means that the owner of the company has taken out a large portion of its equity (usually in the form of cash), which can sometimes turn the number negative.
- It can also happen if the company has been losing money consistently and therefore has a declining Retained Earnings balance, which is a portion of Shareholders' Equity.

### *What is Equity to assets ratio?*

Equity to assets ratio is a metric that assesses the company's equity compared to the total assets. Expenses are on the profit and loss statement.

### *What are operating activities under cash flow statement?*

Operating activities is a section on the cash flow statement. This section represents the operating activities of the business itself – selling products and services and managing all of the processes for the order to cash cycle and the procurement to payment cycle.

### *What is meant by investing activities?*

Investing activities represent a section on the cash flow statement that shows how a business generates or uses cash from investing activities. Investing activities can be investments into certificates of deposit or treasuries and this can include the investments that a company makes into long-term assets.

### *What are Financing activities?*

Financing activities are represented on the cash flow statement that shows how a company is generating or using cash through debt. These balances can represent loans from banks or bonds issued to investors that must be paid back.

### *What is meant by Finished goods inventory?*

Finished goods inventory represents products that are ready to sell to customers. These products often are produced using raw materials or component parts inventories.

### *What is fiscal year?*

Fiscal year represents the time frame of a year that the company uses to generate financial statements. Not all companies start their fiscal year on January 1.

### *What is meant by Free Cash flow?*

Free cash flow is the amount of cash on hand that has no "demand" on it and thus the company can use it for any purpose. Think of it as the companies "emergency fund."

### *What is meant by Income?*

Income is the amount of money an individual brings into the household. This is compared to revenue for a corporation to ground concepts in finance for businesses.

### *What are indirect costs?*

Indirect costs are the costs we know go to servicing clients or manufacturing products, but it is harder to trace these costs directly to the client or product.

### *How is liability defined?*

Liabilities is a section on the balance sheet that represents short term and long-term liabilities. This section will include the balance of bills that are owed to suppliers, and longer-term loans and debts. Limited Liability Company (LLC) is a legal form of business that protects you, as an individual, from increased exposure of legal liability.

### *How is net income or loss defined?*

Net income or loss (syn. net profit or loss): This is a line on the income statement (or profit and loss statement). This is the bottom-line number after all expenses have been deducted from revenue.

### *What is meant by net profit margin ratio?*

Net profit margin ratio is a metric that assesses how much money is left over after all expenses have been deducted from revenue on the profit and loss statement.

Net worth statement is similar in concept to the equity that is built up in a company. Net worth is the term used to apply to a person.

### *What is meant by obsolete inventory?*

Obsolete inventory is the inventory that no longer has a purpose in production, or maintenance, or has met an expiration date.

### *What are operating expenses?*

Operating expenses are the expenses that a company incurs that are not directly related to the direct sales of products and services. Another way to identify these expenses are the expenses that occur even if a sale does NOT occur. Operating income is the amount (operating income or loss) left over after costs of goods sold and operating expenses have been deducted from revenue.

### *What is meant by Period of time?*

Period of time is a naming convention that happens on financial statements. For example, a profit and loss statement represents a period of time, which can be a month, a quarter, or a year. Physical counts are a practice of internal controls to ensure that inventory is valued appropriately and being used appropriately.

### *What are internal control procedures?*

Internal control Procedures are the documentation of internal controls. All internal control procedures should be documented and available upon request. Auditors (both internal and external) use these to verify if procedures are being following as outlined. Procurement to payment cycle is how a company purchases products and services and then pays for those products/services.

### *What is meant by Raw materials inventory?*

Raw materials inventory is an inventory of individual parts that will be used to produce a finished good. For example, if you build computers, you would have microprocessors, other boards, screens, and various other raw materials that go into the production of the computer.

### *What do we mean by reconciliation?*

Reconciliations is a method by which a company can ensure that its assets are fairly represented on the balance sheet.

### *What are the non-recurring items we need to add back to a company's EBIT / EBITDA when looking at its financial statements?*

The non-recurring items are as under:

- Restructuring Charges
- Goodwill Impairment
- Asset Write-Downs
- Bad Debt Expenses
- Legal Expenses
- Disaster Expenses
- Change in Accounting Procedures

Note that to be an "add-back" or "non-recurring" charge for EBITDA / EBIT purposes, it needs to affect Operating Income on the Income Statement. So if we have one of these charges "below the line" then we do not add it back for the EBITDA / EBIT calculation.

Also, we do add back Depreciation, Amortization, and sometimes Stock-Based Compensation for EBITDA / EBIT, but that these are not "non-recurring charges" because all companies have them every year – these are just non-cash charges.

### *What is meant by segregation of duties?*

Segregation of duties is an internal control that reduces risk of loss of assets by diving up work among several individuals.

### *What is meant by short-term?*

Short-term (current) is a time frame that is under one year. Sole proprietor is the simplest form a business to create.

### *What is meant by work-in-process inventory?*

Work in process inventory is an inventory that is between raw materials and finished goods. In other words, a computer may be in the assembly process and that would be inventory that is a work in process.

### *How do we define Working capital?*

Working capital is a word that is the management of the cash, accounts receivable, inventory, and accounts payable balances.

If it's positive, it means a company can pay off its short-term liabilities with its short-term assets. It is often presented as a financial metric and its magnitude and sign (negative or positive) tells you whether or not the company is "sound."

Bankers look at **Operating Working Capital** more commonly in models, and that is defined as (Current Assets – Cash & Cash Equivalents) – (Current Liabilities – Debt).

The point of Operating Working Capital is to exclude items that relate to a company's **financing** activities – cash and debt – from the calculation.

### *What is meant by Working Capital Management?*

Working capital management helps you assess how well a company turns inventory and accounts receivable into cash and how long you can hold on to cash before paying off the accounts payable balances.

### *What is meant by negative working capital?*

Negative working capital is explained based on the following scenarios:

- Some companies with subscriptions or longer-term contracts often have negative Working Capital because of high Deferred Revenue balances.
- Retail and restaurant companies like Amazon, Wal-Mart, and McDonald's often have negative Working Capital because customers pay upfront – so they can use the cash generated to pay off their Accounts Payable rather than keeping a large cash balance on-hand. This can be a sign of business efficiency.
- In other cases, negative Working Capital could point to financial trouble or possible bankruptcy (for example, when customers *don't* pay quickly and upfront and the company is carrying a high debt balance).

### *What is the difference between capital leases and operating leases?*

Operating leases are used for short-term leasing of equipment and property, and do not involve ownership of anything. Operating lease expenses show up as operating expenses on the Income Statement.

Capital leases are used for longer-term items and give the lessee ownership rights; they depreciate and incur interest payments, and are counted as debt.

A lease is a capital lease if any one of the following 4 conditions is true:

- If there's a transfer of ownership at the end of the term.
- If there's an option to purchase the asset at a bargain price at the end of the term.
- If the term of the lease is greater than 75% of the useful life of the asset.
- If the present value of the lease payments is greater than 90% of the asset's fair market value.

### *What is virtual currency?*

Virtual currency is a digital representation of value, other than a representation of the Indian Rupee (INR) or a foreign currency ("real currency"), that functions as a unit of account, a store of value, and a medium of exchange. Some virtual currencies are convertible, which means that they have an equivalent value in real currency or act as a substitute for real currency.

### *What is crypto currency and how it needs to be disclosed in Financial Statements?*

Crypto currency is a form of digital / virtual currency generated through a series of written computer codes that rely on cryptography which is encryption and is thus independent of any central issuing authority per se.

Where the Company has traded or invested in Crypto currency or Virtual Currency during the financial year, the following shall be disclosed:

(a) profit or loss on transactions involving Crypto currency or Virtual Currency

(b) amount of currency held as at the reporting date,

(c) deposits or advances from any person for the purpose of trading or investing in Crypto Currency/virtual currency.

### *What is meant by Internal controls?*

Internal controls are procedures and documentation used by businesses to ensure that the company's assets are protected from theft or other misuse.

### *What is the treatment if inventory increases by Rs. 100 assuming that it has been paid in cash?*

The treatment is as follows:

No changes to the Income Statement.

On the Cash Flow Statement, Inventory is an asset so that *decreases* your Cash Flow from Operations – it goes down by Rs.100, as does the Net Change in Cash at the bottom.

On the Balance Sheet under Assets, Inventory is up by Rs.100 but Cash is down by Rs.100, so the changes cancel out and Assets still equals Liabilities & Shareholders' Equity.

### *Why is the Income Statement not affected by changes in Inventory?*

In the case of Inventory, the expense is only recorded when the goods associated with it are sold – so if it's just sitting in a warehouse, it does not count as a Cost of Goods Sold or Operating Expense until the company manufactures it into a product and sells it.

### *What are the additional information which need to be disclosed by way of notes?*

**Additional Information**:

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

(a) employee Benefits expense [showing separately

(i) salaries and wages,

(ii) contribution to provident and other funds,

(iii) share based payments to employees,

(iv) staff welfare expenses].

(b) depreciation and amortisation expense;

(c) any item of income or expenditure which exceeds one per cent of the revenue from operations or Rs. 10,00,000, whichever is higher, in addition to the consideration of 'materiality' as specified in clause 7 of the General Instructions for Preparation of Financial Statements of a Company;

(d) interest Income;

(e) interest Expense;

(f) dividend income;

(g) net gain or loss on sale of investments;

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

(i) payments to the auditor as

(a) auditor,

(b) for taxation matters,

(c) for company law matters,

(d) for other services,

(e) for reimbursement of expenses;

(j) in case of companies covered under section 135, amount of expenditure incurred on corporate social responsibility activities; and

(k) details of items of exceptional nature;

**(l) Undisclosed income**

This is a newly inserted requirement, whereby, the Company shall give details of any transaction not recorded in the books of accounts that has been surrendered or disclosed as income during the year in the tax assessments under the Income Tax Act, 1961 (such as, search or survey or any other relevant provisions of the Income Tax Act, 1961), unless there is immunity for disclosure under any scheme and shall also state whether the previously unrecorded income and related assets have been properly recorded in the books of account during the year.

**(m) Corporate Social Responsibility**

Where the company covered under section 135 of the Companies Act, the following shall be disclosed with regard to CSR activities:

(i) amount required to be spent by the company during the year,

(ii) amount of expenditure incurred,

(iii) shortfall at the end of the year,

(iv) total of previous years shortfall,

(v) reason for shortfall,

(vi) nature of CSR activities,

(vii) details of related party transactions, e.g., contribution to a trust controlled by the company in relation to CSR expenditure as per relevant Accounting Standard,

(viii) where a provision is made with respect to a liability incurred by entering into a contractual obligation, the movements in the provision during the year shall be shown separately.

**(n) Details of Crypto Currency or Virtual Currency**

Where the Company has traded or invested in Crypto currency or Virtual Currency during the financial year, the following shall be disclosed:

(i) profit or loss on transactions involving Crypto currency or Virtual Currency,

(ii) amount of currency held as at the reporting date,

(iii) deposits or advances from any person for the purpose of trading or investing in Crypto Currency or virtual currency.