



VIMS First Year 2014-15 FOUNDATION PROGRAMME



Financial Accounting

A Presentation

by

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Financial Accounting:

- **shareholder reporting or stewardship accounting**
- **focus of financial accounting is on shareholder reporting**
- **shareholders are the owners of any business**



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Financial Accounting is defined as:

“the classification and recording of monetary transactions of an entity in accordance with established concepts, principles, accounting standards, and legal requirements and their presentation, by means of profit and loss accounts, balance sheet and cash flow statements during and at the end of an accounting period”

SOURCE: C.Wilksand M. Weaver, CIMA (UK) Reading Material-

Financial Accounting Fundamentals Stage 1, p.3



Financial Accounting is also defined

as:



“the branch of accounting that is concerned with the recording of transactions using Generally Accepted Accounting Principles (GAAP) for a business and other economic unit and with a periodic preparation of various statements from such records”



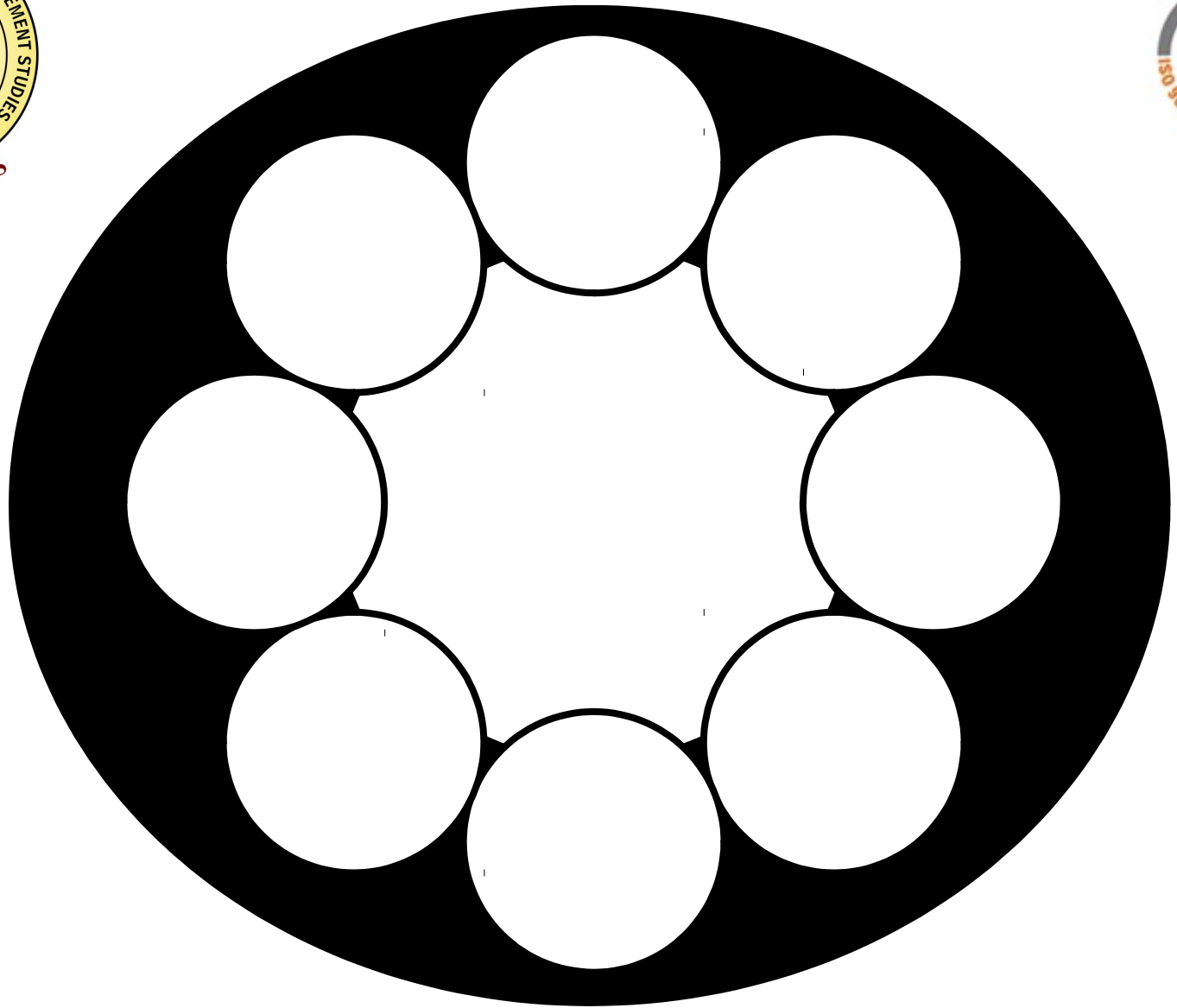
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**Accounting is a language used to communicate the happenings in
business in a quantified form and in prescribed formats
and proforma wherever necessary.**



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WHICH STAKEHOLDER?

WHY?

Owners

- To know the performance of their funds invested in the company (return on owners' funds)

Directors

- To evaluate the financial performance of the Company over a period of time and also for comparing with other firms.
- To assess the financial health and its adequacy or otherwise.
- To ensure compliance with mandatory and other benchmarks.



WHICH STAKEHOLDER?

WHY?

Creditors

How safe is the money due to them with respect to interest and principal?

Government

- Are the disclosures true, fair and consistent with law as well as cannons of accounting?
- Is the Company complying with all its statutory obligations (corporate, tax, excise, customs, value added tax and other laws.)?



WHICH STAKEHOLDER?

WHY?

Customers

➤ Will we get value for money on an ongoing basis?

Employees

➤ Is the Company safe enough to meet our salary bill, healthy enough to pay bonus and well prepared to meet terminal obligation of employees?

➤ Do the employees have a future in the Company in terms of growth and self development?



WHICH STAKEHOLDER?

WHY?

**Securities and Exchange
Board of India (SEBI)**

➤ Are the SEBI norms and disclosures adhered to?

Reserve Bank Of India (RBI)

➤ Are the rules and regulations, prescribed by the RBI regarding foreign exchange management and other matters being adhered to?



Business Transactions:

- **Individuals or firms: creditors / debtors**
- **Acquisition / disposal: fixed / non fixed assets**
- **Expenses / incomes : salaries, rent (expenses)**

sales, other income

(incomes)



Classification of Accounts and Rules of Debit (D) and Credit (C):



Three types of accounts:

- **Personal** – D receiver; C giver
- **Impersonal**
 - Real Accounts – D what comes in; C what goes out
 - Nominal Accounts – D all expenses and losses

C all incomes and gains



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Trial Balance:

- **List of debit and credit balances**
- **Debit balances represent the sum of all assets and expenses**
- **Credit balances represent the sum of all incomes and capital or owners' funds**



Accounting Equations:

BALANCE SHEET EQUATION

$$\text{Assets} = \text{Liabilities} + \text{Capital}$$

INCOME STATEMENT EQUATION

OR

PROFIT AND LOSS ACCOUNT EQUATION

$$\text{Profit} = \text{Income} - \text{Expenses}$$



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How Financial Accounting?

The financial accounting process can be captured through the following steps:

- **identifying business transactions;**
- **entering the said transactions in books of accounts;**
- **verifying the arithmetical accuracy of the record keeping process before presenting the financial position;(final accounts);**
- **enunciating accounting policies of the Company/other intentions of the management for induction into the accounts by way of adjustments**



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The end result of financial accounting is:

- **Income and other statements also known as profit and loss account for the accounting period ending.**
- **Section 211 of the Companies Act in India did not use the expression Income Statement. It used the expression Profit and Loss Account.**
- **The revised Schedule VI uses the expression Statement of Profit and Loss.**
- **Section 211 also requires that a balance sheet as on a particular date shall be prepared in a prescribed proforma.**
- **Cash flow statement and other details like historic records, vital financial and other statistics, important historic attainments and impending future events.**



Concepts Governing Financial Statements:



- **Entity Concept**
- **Going Concern**
- **Prudence (Conservatism)**
- **Duality Concept**
- **Historic Concept**
- **Accrual Concept**
- **Matching Concept**
- **Periodicity Concept**
- **Materiality Concept**
- **Objectivity Concept**

N.B: See RIL Annual Report 2012-13, pp. 120 to 122 – Significant Accounting Policies

**ULTIMATE PURPOSE:
PRESENT, TRUE AND FAIR VIEW
OF THE FINANCIAL POSITION OF BUSINESS**

Financial Statements

Understandability

Transparency

Comparability

Relevance

Reliability



Characteristics of Financial Statements:

- The International Accounting Standards Committee (IASC) (1973):

Aim : developing a common set of standards for international companies'

Purpose : "formulate and publish in the public interest, accounting standards to be observed in the presentation of financial statements and to promote their worldwide acceptance and observances".

Qualitative Characteristics : Understandability, Relevance, Transparency, Reliability and Comparability



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- **UNDERSTANDABILITY:**

- Users should be able to comprehend the disclosed information.

- Disclosures required by law cannot be omitted.

- Attempt should be made to make the disclosures as simple as possible.



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- **RELEVANCE:**

- Users should be in a position to identify the relevance of information, which is disclosed.
- Disclosures required by law are modicum disclosures.
- Companies may, in fact need to, go a step further to enhance the relevance of financial statements.



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- **TRANSPARENCY:**

- Corporate dealings need to be transparent to improve the utility of financial statements.
- Transparency is guided by the principle of materiality and the incremental cost of reporting as against the potential benefits.



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- **RELIABILITY:**

- Information presented should be true and a product of proper and prudent application of mind as well as the accounting principles.
- Vitiated if there is colourable exercise of judgement and apparent departure from neutrality.
- Practice faithful presentation of complete information by assuming a neutral and unbiased position which permits the practice of exercising prudence and due diligence.
- Importance has to be given to substance over form.



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- **COMPARABILITY:**

- Refers to consistency in presentation of accounting information and application of accounting principles.
- Refers to inter-period and inter-firm comparability.
- Difficult to achieve even on an intra-firm basis.
- Inter-firm comparability leaves much to be desired in today's World.
- International Accounting Standards an attempt is being made to unitize global accounting practices, policies and principles.



Statutes require that accounts shall be prepared and further that such preparation shall necessarily be governed and guided by:



- **prescribed formats;**
- **time limits fixed by law;**
- **mandates of other related legislation;**
- **cannons of accounting i.e. generally accepted accounting principles (GAAP) and**
- **ethical disclosures, which result in presenting a true and fair view of the accounts.**



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Companies Act, 1956:

In India, section 211(1) of the Companies Act, 1956 states that every Company shall present a Balance sheet which shall give a true and fair view of the state of affairs of the Company at the end of the financial year.

Similarly S211(2) says that every profit and loss account, now statement of profit and loss (from 31st March, 2011), of a company shall give a true and fair view of the profit or loss of the company for the financial year.



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Again in the UK S228 of the Companies Act 1985 reads as follows:

**“the balance sheet shall give a true and fair view of the state of affairs of
the company as at the end of the financial year and the profit and loss
account shall give a true and fair view of the profit or loss of the company
for the financial year.”**



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New Schedule VI for India INC:

- **Schedule VI has been revised by MCA and is applicable for all Balance Sheet made after 31st March, 2011.**
- **The Format has done away with earlier two options of format of Balance Sheet.**
- **Now only Vertical format has been permitted.**
- **General instructions for preparation of balance sheet and statement of**

profit and loss of a company in addition to the notes incorporated



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In the Indian context section 211, Schedule VI part II of the Companies Act, 1956 says that in giving the break-up of purchases, stocks and turnover, items like spare parts, jigs, tools, accessories may be grouped under suitable headings without quantities provided all those items which in value individually account for 10% or more of the total value of purchases, stocks or turnover are shown as separate or distinct items.



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In the final analysis a balance has to be struck between several conflicting or push and pull factors such as:

- **economics of information generation, presentation and communication;**
- **reliability and relevance;**
- **timeliness; and**
- **dictates of law with respect to quantum, format and periodicity of information.**



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Myth of Neutrality

It is not untrue to say that accounting may obscure or even mask more important but less easily measured dimension of business. Total neutrality is therefore a myth.



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Myth of Numbers

Everything is quantified and expressed in financial terms in the financial statements.

Quantification is looked upon with awe and respect. It is assumed that what is quantified is right, correct and unambiguous unlike words and phrases which are perceived to be vague and nebulous. This is indeed a misconception.



Revised Schedule VI - Balance Sheet

-Proforma:



- **Equity and Liabilities**
 - Shareholders' Funds
 - Share Application Money Pending Allotment
 - Non-Current Liabilities
 - Current Liabilities
 - TOTAL

- **Assets**
 - Non-Current Assets
 - Current Assets
 - TOTAL



Statement of Profit and Loss for the year ended

-Proforma:



- **Continuing Operations – Revenue**

Expenses

- **Profit / (Loss) before extra ordinary items and tax**
- **Extra ordinary items**
- **Profit / (Loss) before tax**
- **Tax expense**
- **Profit / (Loss) from continuing operations**
- **Discontinuing operations**
- **Profit / (Loss) from discontinuing operations**
- **Total Operations – Profit / Loss for the year**
- **Earnings per equity share**
 - **Face Value per Share**
 - **No. of Shares**
 - **Basic EPS**
 - **DilutedEPS**



Statement of Profit and Loss for the yearended

31st March:



- **Income**
 - **Total Revenue**

- **Expenditure**
 - **Total Expenses**
 - **Tax Expenses**
 - **Profit for the year**
 - **Earnings per equity share of face value ofRs. 10 each**
 - **Basic and diluted**

SOURCE: Reliance Industries Limited – Annual Report 2012-13,p.117



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Revised Schedule VI (Section 211):

PRELUDE

Six General Instructions Plus one note

PART I

- (1) Revised Form of Balance Sheet
- (2) General Instructions for preparation of Balance Sheet (Twenty Three Main Instructions)

AND

PART II

- Form of Statement of Profit and Loss (Sixteen Items)
(Prescribed form Introduced for the first time)
- (2) General Instructions for preparation of Statement of Profit and Loss (Five Main Instructions)



RELIANCE INDUSTRIES LIMITED Annual Report - 2012-13 (224

pages):



- **Highlights**
- **10 Year Financial Performance**
- **Letter to Shareholders**
- **The Board of Directors**
- **Reliance Foundation**
- **Company Information**
- **Financial Highlights**
- **Notice of Annual General Meeting**
- **Management's Discussion and Analysis**
- **Report on Corporate Social Responsibility**
- **Report on Corporate Governance**



RELIANCE INDUSTRIES LIMITED Annual Report - 2012-13 (224

pages):



- **Secretarial Audit Report**
- **Directors' Report**
- **Auditors' Certificate on Corporate Governance**
- **Business Responsibility Report**
- **Independent Auditors' Report on Financial Statements**
- **Balance Sheet**
- **Statement of Profit and Loss**
- **Cash Flow Statement**
- **Significant Accounting Policies**
- **Notes on Financial Statements**
- **Independent Auditors' Report on Consolidated Financial Statements**



RELIANCE INDUSTRIES LIMITED Annual Report - 2012-13 (224

pages):



- **Consolidated Balance Sheet**
- **Consolidated Statement of Profit and Loss**
- **Consolidated Cash Flow Statement**
- **Significant Accounting Policies on Consolidated Accounts**
- **Notes on Consolidated Financial Statements**
- **Financial Information of Subsidiary Companies**
- **Shareholders' Referencer**
- **Members' Feedback Form**
- **Attendance Slip and Proxy Form**



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Money is a matter of functions four

a medium, a measure, a standard and store



Thank You