

COMPANY ACCOUNTS



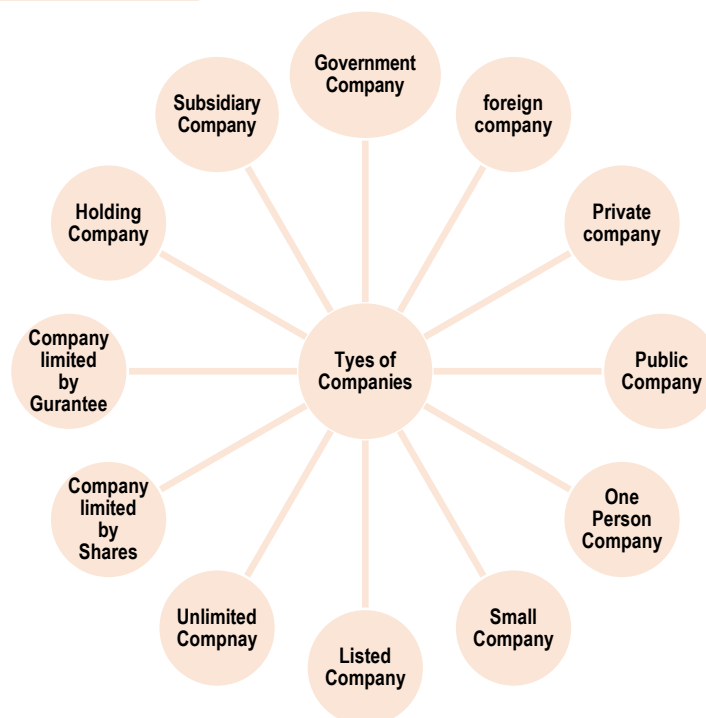
UNIT – 1 INTRODUCTION TO COMPANY ACCOUNTS

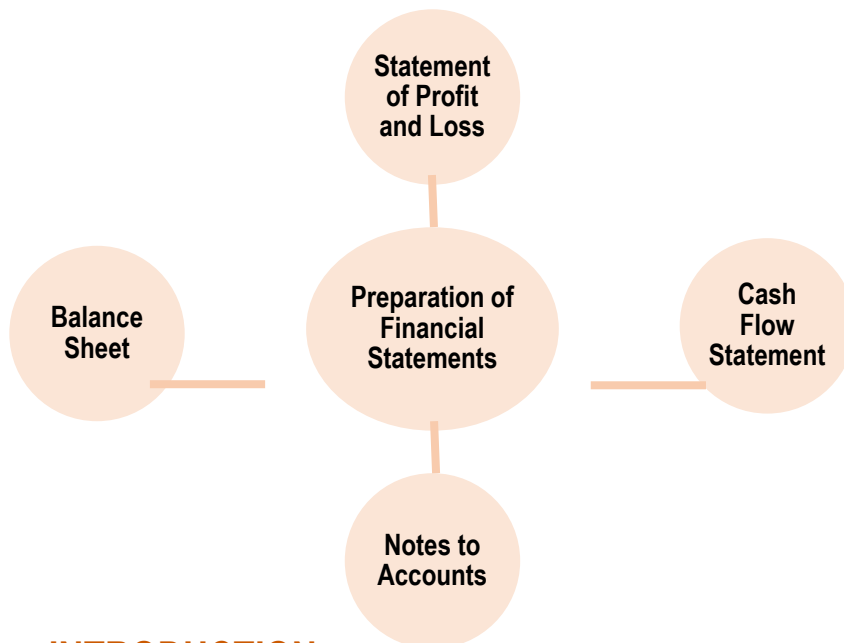
LEARNING OUTCOMES

After studying this unit, you would be able to:

- ◆ Understand the reason for the existence and survival of a company.
- ◆ Learn the nature and types of companies.
- ◆ Explain the salient features of a company.
- ◆ Understand the purpose of preparing the financial statements of the company.

UNIT OVERVIEW





1.1 INTRODUCTION

The never-ending human desire to grow and grow further has given rise to the expansion of business activities, which in turn has necessitated the need to increase the scale of operations so as to provide goods and services to the ever-increasing needs of the growing population of consumers. Large amount of money, modern technology, large human contribution etc. is required for it, which is not possible to arrange under partnership or proprietorship. To overcome this difficulty, the concept of 'Company' or 'Corporation' came into existence.

While the invention of steam power ignited the human imagination to build big machines for the mass production of goods, the need to separate the management from ownership gave birth to a form of organisation today known as 'company'.

Company form of organisation is one of the ingenious creations of human mind, which has enabled the business to carry on its wealth creation activities through optimum utilisation of resources. In course of time, company has become an important institutional form for business enterprise, which has carved out a key place for itself in the field of business operations as well as in the wealth-generating functions of society.



1.2 MEANING OF COMPANY

The word 'Company', in everyday usage, implies an assemblage of persons for social purpose, companionship or fellowship. As a form of organisation, the word 'company' implies a group of people who voluntarily agree to form a company.

The word 'company' is derived from the Latin word 'com' i.e. with or together and 'panis' i.e. bread. Originally the word referred to an association of persons or merchant men discussing matters and taking food together. However, in law 'company' is termed as company which is formed and incorporated under the Companies Act, 2013 or an existing company formed and registered under any of the previous company laws. As per this definition of law, there must be group of persons who agree to form a company under the law and once so formed; it

becomes a separate legal entity having perpetual succession with a distinct name of its own and a common seal. Its existence is not affected by the change of members.

Company begs its origin in law. It is an organisation consisting of individuals, called shareholders by virtue of holding the shares of a company, who are authorised by law to elect a board of directors and, through it, to act as a separate legal entity as regards its activities. Generally, the capital of the company consists of transferable shares, and members have limited liabilities.

To get to the heart of the nature of the company, let us examine the concept of company propounded under corporate jurisprudence.

According to Justice Marshal, “A corporation is an artificial being, invisible, intangible and existing only in the contemplation of law”.

In the same manner, Lord Justice Hanay has defined a company as “an artificial person created by law with a perpetual succession and a common seal”.

A common thread running through the various definitions of ‘company’ is that it is an association of persons created by law as a separate body for a special purpose. At the same time, definitions have laid down certain characteristics of a corporate organisation, which make it out as a separate and unique organisation which enables the people to contribute their wealth to the capital of the company by subscribing to its shares and appointing elected representatives to carry out the business.



1.3 SALIENT FEATURES OF A COMPANY

Following are the salient features of a company:

1. *Incorporated Association:* A company comes into existence through the operation of law. Therefore, incorporation of company under the Companies Act is must. Without such registration, no company can come into existence. Being created by law, it is regarded as an artificial legal person.
2. *Separate Legal Entity:* A company has a separate legal entity and is not affected by changes in its membership. Therefore, being a separate business entity, a company can contract, sue and be sued in its incorporated name and capacity.
3. *Perpetual Existence:* Since company has existence independent of its members, it continues to be in existence despite the death, insolvency or change of members.
4. *Common Seal:* Company is not a natural person; therefore, it cannot sign the documents in the manner as a natural person would do. In order to enable the company to sign its documents, it is provided with a legal tool called ‘Common Seal’. The common seal is affixed on all documents by the person authorised to do so who in turn puts his signature for and on behalf of the company. Companies Act, 2013 required common seal to be affixed on certain documents (such as bill of exchange, share certificates, etc.) Now, the use of common seal has been made optional. All such documents which required affixing the common seal may now instead be signed by two directors or one director and a company secretary of the company.
5. *Limited Liability:* The liability of every shareholder of a company is limited to the amount he has agreed to pay to the company on the shares allotted to him. If such shares are fully paid-up, he is subject to no further liability.

6. *Distinction between Ownership and Management:* Since the number of shareholders is very large and may be distributed at different geographical locations, it becomes difficult for them to carry on the operational management of the company on a day-to-day basis. This gives rise to the need of separation of the management and ownership.
7. *Not a citizen:* A company is not a citizen in the same sense as a natural person is, though it is created by the process of law. It has a legal existence but does not enjoy the citizenship rights and duties as are enjoyed by the natural citizens.
8. *Transferability of Shares:* The capital is contributed by the shareholders through the subscription of shares. Such shares are transferable by its members except in case of a private limited company, which may have certain restrictions on such transferability.
9. *Maintenance of Books:* A limited company is required by law to keep a prescribed set of account books and any failure in this regard attracts penalties.
10. *Periodic Audit:* A company has to get its accounts periodically audited through the chartered accountants appointed for the purpose by the shareholders on the recommendation of board of directors.
11. *Right of Access to Information:* The right of the shareholders of a company to inspect its books of account, with the exception of books open for inspection under the Statute, is governed by the Articles of Association. The shareholders have a right to seek information from the directors by participating in the meetings of the company and through the periodic reports.



1.4 TYPES OF COMPANIES

1. Government Company

According to Section 2(45) of the Companies Act, 2013, “Government company” means any company in which not less than fifty-one per cent of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company.

2. Foreign Company

According to Section 2 (42) of the Companies Act, 2013, “Foreign company” means any company or body corporate incorporated outside India which –

- (a) Has a place of business in India whether by itself or through an agent physically or through electronic mode; and
- (b) Conducts any business activity in India in any other manner.

3. Private Company

Section 2(68) of the Companies Act, 2013 defines ‘Private company’ as a company which by its articles,

- i. Restrict the right to transfer its shares;
- ii. Except in case of One Person Company limits the number of its members to two hundred: Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this sub-clause, be treated as a single member:

Provided further that—

- (A) Persons who are in the employment of the company; and
 - (B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased, shall not be included in the number of members; and
- (iii) Prohibits any invitation to the public to subscribe for any securities of the company. Shares of a Private Company are not listed on Stock Exchange.

4. Public Company

Section 2(71) of the Companies Act, 2013 defines Public Company as a company which— (a) is not a private company; provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.

A company which is a listed public company if it gets unlisted continues to be a public company.

No Minimum Paid-up Share Capital: The minimum paid-up share capital requirement of INR 1,00,000 (in case of a private company) and INR 5,00,000 (in case of a public company) has been done away with under Companies Act, 2013. Accordingly, no minimum paid-up capital requirements will now apply for incorporating private as well as public companies in India.

5. One Person Company

Section 2 (62) of the Companies Act, 2013 defines “One Person Company” as a company which has only one person as a member.

6. Small Company

Section 2(85) of the Companies Act, 2013 defines “Small company” means a company, other than a public company

- (i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; and
- (ii) turnover of which as per its last profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than hundred crore rupees:

Provided that nothing in this clause should apply to:

- (A) a holding company or a subsidiary company
- (B) a company registered under section 8
- (C) a company or body corporate governed by any special Act

7. Listed Company

As per Section 2 (52) of the Companies Act, 2013, “listed company” means a company which has any of its securities listed on any recognised stock exchange.

The company, whose shares are not listed on any recognised stock exchange, is called “Unlisted Company”.

An unlisted company can be a public company or a private company.

8. Unlimited Company

Section 2 (92) of the Companies Act, 2013 defines “Unlimited company” means a company not having any limit on the liability of its members.

9. Company limited by Shares

As per Section 2(22) of the Companies Act, 2013, “Company limited by shares” means a company having the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them.

10. Company limited by Guarantee

As per Section 2(21) of the Companies Act, 2013, “company limited by guarantee” means a company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being wound up.

11. Holding Company

According to Section 2 (46) of the Companies Act, 2103, “Holding company”, in relation to one or more other companies, means a company of which such companies are subsidiary companies.

12. Subsidiary Company

Section 2(87) of the Companies Act, 2013 defines “subsidiary company” as a company in which the holding company:

- (i) Controls the composition of the Board of Directors; or
- (ii) Exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies.

A company shall be deemed to be a subsidiary company of the holding company even if there is indirect control through the subsidiary company (ies). The control over the composition of a subsidiary company’s Board of Directors means exercise of some power to appoint or remove all or a majority of the directors of the subsidiary company.



1.5 MAINTENANCE OF BOOKS OF ACCOUNT

As per Section 128 of the Companies Act, 2013, every company shall prepare and keep at its registered office books of account and other relevant books and papers and financial statement for every financial year which give a true and fair view of the state of the affairs of the company, including that of its branch office or offices, if any, and explain the transactions effected both at the registered office and its branches and such books shall be kept on accrual basis and according to the double entry system of accounting:

Provided further that the company may keep such books of account or other relevant papers in electronic mode in such manner as may be prescribed.



1.6 PREPARATION OF FINANCIAL STATEMENTS

Under Section 129 of the Companies Act, 2013, the financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the notified accounting standards and shall be in the form or forms as may be provided for different class or classes of companies, as prescribed in Schedule III. The Board of Directors of the company shall lay financial statements at every annual general meeting of a company.

Financial Statements as per Section 2(40) of the Companies Act, 2013, inter-alia include -

- i. A balance sheet as at the end of the financial year;
- ii. A profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;
- iii. cash flow statement for the financial year;
- iv. A statement of changes in equity, if applicable; and
- v. (any explanatory not annexed to, or forming part of, any document referred to in sub-clause (i) to sub-clause (iv):

Provided that the financial statement, with respect to One Person Company, small company and dormant company, may not include the cash flow statement.

Requisites of Financial Statements

It shall give a true and fair view of the state of affairs of the company as at the end of the financial year.

Provisions Applicable

- (1) Specific Act is Applicable

For instance, any

- (a) Insurance company
- (b) Banking company or
- (c) Any company engaged in generation or supply of electricity* or
- (d) Any other class of company for which a Form of balance sheet or Profit and loss account has been prescribed under the Act governing such class of company.

- (2) In case of all other companies:

Balance Sheet as per Form set out in Part I of Schedule III and Statement of Profit and Loss as per Part II of Schedule III.

Compliance with Accounting Standards

As per Section 129 of the Companies Act, it is mandatory to comply with accounting standards notified by the Central Government from time to time.

Schedule III of the Companies Act, 2013

As per Section 129 of the Companies Act, 2013, Financial statements shall give a true and fair view of the state of affairs of the company or companies and comply with the accounting standards notified under Section 133 and

shall be in the form or forms as may be provided for different class or classes of companies in Schedule III under the Act.

PART I – Form of BALANCE SHEET

Name of the Company.....

Balance Sheet as at.....

(₹ in.....)

Particulars	Notes No.	Figures as at end of the current reporting period	Figures as at end of the previous reporting period
EQUITY AND LIABILITIES			
1. Shareholders' funds			
a. Share capital (A)		xxx	xxx
b. Reserves and Surplus (B)		xxx	xxx
c. Money received against share warrants		xxx	xxx
2. Share application money pending allotment		xxx	xxx
3. Non-current liabilities			
a. Long-term borrowings (C)		xxx	xxx
b. Deferred tax liabilities (Net)		xxx	xxx
c. Other long term liabilities		xxx	xxx
d. Long-term provisions (D)		xxx	xxx
4. Current liabilities			
a. Short-term borrowings (E)		xxx	xxx
b. Trade Payables		xxx	xxx
c. Other current liabilities (F)		xxx	xxx
d. Short-term provisions		xxx	xxx
Total		xxx	xxx
ASSETS			
1. Non-current assets			
a.			
i. Property, Plant and Equipment		xxx	xxx
ii. Intangible assets (H)		xxx	xxx
iii. Capital Work-in-progress		xxx	xxx
iv. Intangible assets under development		xxx	xxx
b. Non-current investments (I)		xxx	xxx
c. Deferred tax assets (Net)		xxx	xxx

	d. Long-term loans and advances (J)		XXX	XXX
	e. Other non-current assets		XXX	XXX
2.	Current assets			
	a. Current investments (K)		XXX	XXX
	b. Inventories (L)		XXX	XXX
	c. Trade receivables		XXX	XXX
	d. Cash and cash equivalents (M)		XXX	XXX
	e. Short-term loans and advances		XXX	XXX
	f. Other current assets		XXX	XXX
	Total		XXX	XXX

Some items are to be explained as follows:

A. SHARE CAPITAL

For each class of share capital following points is to be kept in mind:

- i. The number and amount of shares authorised.
- ii. The number of shares which are issued, subscribed and fully paid and which are issued, subscribed but not fully paid.
- iii. The par value per share.
- iv. Shares outstanding at the beginning and at the end of the reporting period should be reconciled.
- v. Calls unpaid.
- vi. Forfeited shares.

B. RESERVES AND SURPLUS

Reserves and surplus can be distributed among the following sub-heads:

- i. Capital reserves
- ii. Capital redemption reserves
- iii. Securities Premium
- iv. Debenture Redemption reserve
- v. Revaluation reserve
- vi. Surplus; the balance as per profit and loss statement
- vii. Other reserves (specify the nature and purpose)

C. LONG TERM BORROWINGS

Long term borrowings can be classified under the following sub-heads:

- i. Bonds/Debentures
- ii. Term loans
- iii. Deferred payment liabilities

- iv. Deposits
- v. Long term maturities of finance lease obligations
- vi. Loans and advances from related parties
- vii. Other loans and advances (specify nature)

D. LONG TERM PROVISIONS

This can be classified as follows:

- i. Employee benefits provision like gratuity, provident fund etc.
- ii. Other provisions (specify the nature)

E. SHORT TERM BORROWINGS

Short term borrowings can be classified among the following sub-heads:

- i. Loans repayable on demand
- ii. Loans and advances from related parties
- iii. Deposits
- iv. Other loans and advances (specify the nature)

F. OTHER CURRENT LIABILITIES

Some of the other current liabilities can be grouped as under:

- i. Interest accrued but not/and due on borrowings
- ii. Income received in advance
- iii. Unpaid dividends
- iv. Application money received for allotment of securities and due for refund and interest accrued thereon
- v. Other current liabilities (specify the nature)

G. PROPERTY, PLANT AND EQUIPMENT

Property, Plant and Equipment can be classified as follows:

- i. Land
- ii. Buildings
- iii. Plant and Equipments
- iv. Furniture and Fixtures
- v. Vehicles
- vi. Office equipments
- vii. Others (specify the nature)

A detailed report showing additions, disposals, acquisitions through business combinations and other adjustments and amount related to depreciation, impairment losses, revaluation etc. should be provided for each class of asset.

H. INTANGIBLE ASSETS

Intangible assets can be classified as follows:

- i. Goodwill
- ii. Brands/trademarks
- iii. Computer software
- iv. Mining rights
- v. Publishing titles
- vi. Copyrights, patents and other intellectual property rights, services and operating rights.
- vii. Licence and franchise
- viii. Recipes, models, designs, formulae and prototypes
- ix. Others (specify the nature)

A detailed report showing additions, disposals, acquisitions through business combinations and other adjustments and amount related to depreciation, impairment losses, revaluation etc. should be provided for each class of asset.

I. NON-CURRENT INVESTMENTS

Investments can be classified as under:

- i. Investments in property
- ii. Investments in equity instruments
- iii. Investments in preference shares
- iv. Investments in governments or trust securities
- v. Investments in debentures or bonds
- vi. Investments in mutual funds
- vii. Investments in partnership firms
- viii. Other non-current investments (specify the nature)

J. LONG TERM LOANS AND ADVANCES

It can be classified under the following sub-groups:

- i. Capital advances
- ii. Security deposits
- iii. Loans and advances to related parties
- iv. Other loans and advances (specify nature)

The above shall also be sub-classified as follows:

- i. Secured, considered goods
- ii. Unsecured, considered goods

iii. Doubtful

K. CURRENT INVESTMENTS

It can be classified as follows:

- i. Investments in equity instruments
- ii. Investments in preference shares
- iii. Investments in government or trust securities
- iv. Investments in bonds or debentures
- v. Investments in mutual funds
- vi. Investments in partnership firms
- vii. Other investments (specify the nature)

L. INVENTORIES

Inventories can be classified as:

- i. Raw materials
- ii. Work-in-progress
- iii. Stores and spares
- iv. Finished goods
- v. Loose tools
- vi. Stock in trade
- vii. Goods in transit
- viii. Others (specify the nature)

M. CASH AND CASH EQUIVALENTS

The following head can be classified as follows:

- i. Balances with banks
- ii. Cheques, drafts in hand
- iii. Cash in hand
- iv. Others (specify the nature)

PART II – Form of STATEMENT OF PROFIT AND LOSS

Name of the Company.....

Profit and Loss Statement for the year ended

(₹ in.....)

Particulars		Note No.	Figures for the current reporting period		Figures for the previous reporting period	
i.	Revenue from operations			xxx		xxx

II.	Other income		xxx		xxx
III.	Total Revenue (I + II)		xxx		xxx
IV.	Expenses:		xxx		xxx
	Cost of materials consumed		xxx		xxx
	Purchases of Stock-in-Trade		xxx		xxx
	Changes in inventories of finished goods, Work-in-Progress and Stock-in-Trade		xxx		xxx
	Employee benefits expense		xxx		xxx
	Finance costs		xxx		xxx
	Depreciation and amortization expense		xxx		xxx
	Other expenses		xxx		xxx
	Total expenses		xxx		xxx
V.	Profit before exceptional and extraordinary items and tax (III-IV)		xxx		xxx
VI.	Exceptional items		xxx		xxx
VII.	Profit before extraordinary items and tax (V-VI)		xxx		xxx
VIII.	Extraordinary Items		xxx		xxx
IX.	Profit before tax (VII-VIII)		xxx		xxx
X.	Tax expense:				
	(1) Current tax	xxx		xxx	
	(2) Deferred tax	xxx	xxx	xxx	xxx
XI.	Profit (Loss) for the period from continuing operations (VII-VIII)		xxx		xxx
XII.	Profit/(Loss) from discontinuing operations		xxx		xxx
XIII.	Tax expense of discontinuing operations		xxx		xxx
XIV.	Profit/(Loss) from discontinuing operations (after tax) (XII-XIII)		xxx		xxx
XV.	Profit (Loss) for the period (XI + XIV)		xxx		xxx
XVI.	Earnings per equity share:				
	(1) Basic		xxx		xxx
	(2) Diluted		xxx		xxx

SUMMARY

- 'Company' is termed as an entity which is formed and incorporated under the Companies Act, 2013 or an existing company formed and registered under any of the previous company laws.
- Salient features of a company include: Incorporated Association; Separate Legal Entity; Perpetual Existence; Common Seal; Limited Liability; Distinction between Ownership and Management; Not a citizen; Transferability of Shares; Maintenance of Books; Periodic Audit; Right of Access to Information.

3. Types of companies: Government Company; Foreign Company; Private Company; Public Company; One Person Company; Small Company; Listed Company; Unlimited Company; Company limited by Shares; Company limited by Guarantee; Holding Company; Subsidiary Company.
4. The financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the notified accounting standards and shall be in the form or forms as may be provided for different class or classes of companies, as prescribed in Schedule III to the Companies Act, 2013. Financial Statements as per Section 2(40) of the Companies Act, 2013, include balance sheet as at the end of the financial year; profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year; cash flow statement for the financial year; statement of changes in equity, if applicable; and any explanatory note annexed to.

TEST YOUR KNOWLEDGE

True and False

1. Every public company is a listed company.
2. Shares of a private company are not listed on stock exchange.
3. It is not mandatory to incorporate a company under the companies act.
4. Company is an artificial, legal person created by law.
5. Death, insolvency or change of members affects the existence of a company.
6. If the shares are fully paid-up by the shareholder, he is subject to no further liability.
7. Public limited company has restrictions on transferability of shares.
8. Financial statements of company show the financial position of the business.
9. Schedule I gives proforma of Balance Sheet.

Multiple Choice Questions

1. Which of the following statement is not a feature of a Company?
 - (a) Separate legal entity
 - (b) Perpetual Existence
 - (c) Members have unlimited liability
2. In a Government Company, the holding of the Central Government in paid-up capital should not be less than
 - (a) 25%
 - (b) 50 %
 - (c) 51%
3. Which of the following statement is true in case of a Foreign Company?
 - (a) A Company incorporated in India and has place of business outside India.
 - (b) A Company incorporated outside India and has a place of business in India.
 - (c) A Company incorporated in India and has a place of business in India.

4. Which of the following statements is not a feature of a private company?
- (a) Restricts the rights of members to transfer its shares.
 - (b) Does not restrict on the number of its members to any limit.
 - (c) Does not involve participation of public in general.

Theory Questions

1. Explain salient features of a company in brief.
2. Write short note on:
 - (i) Foreign company.
 - (ii) Small company.
 - (iii) Company limited by guarantee.

ANSWER/HINTS

True and False

1. False: Listed companies are those which are listed on the stock exchange. Shares of listed companies are open to general public. Every listed company is a public company but every public company is not a listed company.
2. True: Only the shares of public company are listed on stock exchange. Every listed company is a public company.
3. False: It is mandatory to incorporate a company under the Companies Act. Without such incorporation, a company cannot come into existence.
4. True: Company comes into existence through the operation of law. It is a separate entity distinct from its members.
5. False: Company is a separate legal entity created by law. Death, insolvency or change of member does not affect its existence.
6. True: Liability of shareholders is limited to the extent of the unpaid share capital. So, if shares are fully paid-up, he is subject to no further liability.
7. False: Shares of public company are freely transferable. Transferability of shares is restricted in a private limited company.
8. True: Financial statements give a true & fair view of the state of affairs of the company. Financial statements include profit and loss account, balance sheet, etc.
9. False: Schedule III Part I explains proforma of Balance Sheet.

Multiple Choice Questions

1. (c) 2. (c) 3. (b) 4. (b)

Theoretical Question

1. Refer para 1.3 of this unit for salient features of a company.

2. (i) **Foreign Company**

According to Section 2 (42) of the Companies Act, 2013, "Foreign company" means any company or body corporate incorporated outside India which –

- (a) Has a place of business in India whether by itself or through an agent physically or through electronic mode; and
- (b) Conducts any business activity in India in any other manner.

(ii) **Small Company**

Section 2(85) of the Companies Act, 2013 defines "Small company" means a company, other than a public company.

- (i) paid-up share capital of which does not exceed fifty lakh rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; or
- (ii) turnover of which as per its last profit and loss account for the immediately preceding financial year does not exceed two crore rupees or such higher amount as may be prescribed which shall not be more than hundred crore rupees.

Provided that nothing in this clause should apply to:

- (A) a holding company or a subsidiary company
- (B) a company registered under section 8
- (C) a company or body corporate governed by any special Act

(iii) **Company limited by Guarantee**

As per Section 2(21) of the Companies Act, 2013, "company limited by guarantee" means a company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being wound up.