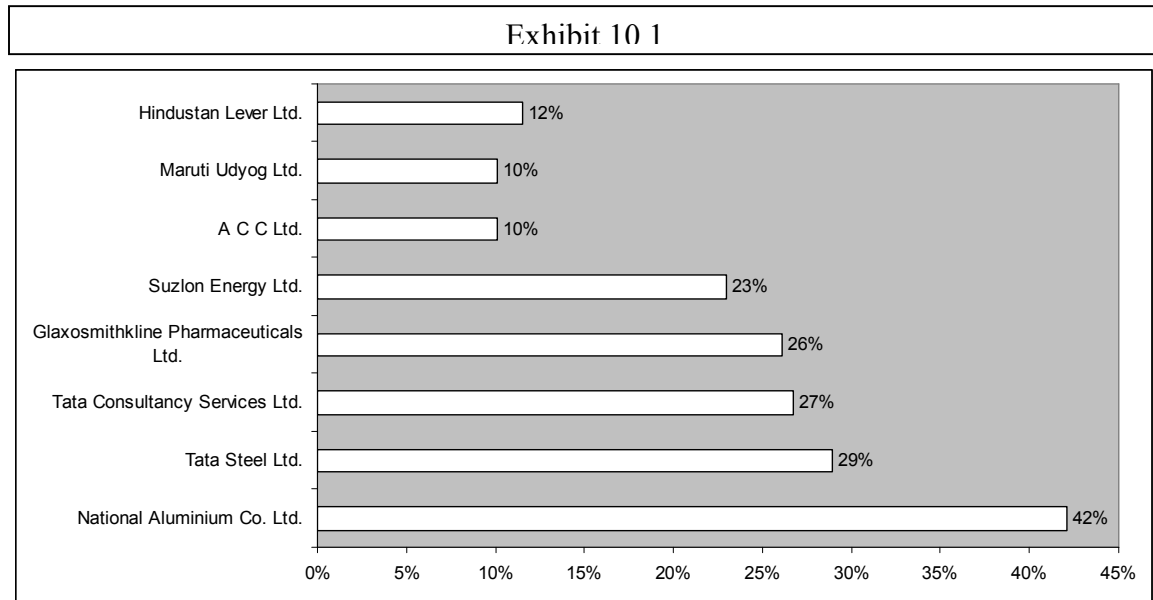


Introduction

The operations of a company is generally manufacturing, buying , and selling a product or a service. Infosys sells IT based solutions, McDonald's sells fast food; Tata Steel sells steel; Bajaj Auto sells automobiles. The performance of a company depends on its ability to make profits from its main operating activity. Exhibit 10.1 shows operating profit as percentage of sales of some of well known companies of India for the year ending March 31 2006.



Operating profit is the excess of the revenue over the cost of goods sold (COGS) and other operating expenses. Operating profit depends on the operating cycle.

Operating Cycle

Operating cycle is the time taken buying inventory and receiving cash proceeds from its sales. It is generally presented in terms of days. Operating cycle can be gross operating cycle or net operating cycle.

- Gross operating cycle is determined by adding inventory days and the collection period.
- Net operating cycle is determined by deducting payment period from the gross operating cycle.

The operating cycle of a manufacturing company differs from that of a service company. Generally the operating cycle of a manufacturing company is longer than that of a service company. Table 10.1 shows the gross and net operating cycle of selected Indian companies.

Table 10.1		
Operating Cycle (days) as on 31st March 2006		
	Gross Operating Cycle	Net Operating Cycle
ONGC	576.57	531.83
A C C Ltd.	218.23	204.68
Hindalco Industries Ltd.	176.76	107.8
Tata Steel Ltd.	169.9	75.33
Larsen & Toubro Ltd.	139.4	35.24
Hindustan Lever Ltd.	104.72	-5.44

According to the Accounting Standard-3 (Cash Flow Statement), cash flows from operating activities are primarily derived from the principal revenue-producing activities of the enterprise. Therefore, they generally result from the transactions and other events that enter into the determination of net profit or loss. Examples of cash flows from operating activities are:

- cash receipts from the sale of goods and the rendering of services;
- cash receipts from royalties, fees, commissions and other revenue;
- cash payments to suppliers for goods and services;
- cash payments to and on behalf of employees;
- cash receipts and cash payments of an insurance enterprise for premiums and claims, annuities and other policy benefits;
- cash payments or refunds of income taxes unless they can be specifically identified with financing and investing activities; and
- cash receipts and payments relating to futures contracts, forward contracts, option contracts and swap contracts when the contracts are held for dealing or trading purposes.

If the operating activities are undertaken on credit, there will be corresponding liabilities. Such liabilities are shown in the balance sheet as Current Liabilities: Creditors and Outstanding Expenses

Accounting Issues Relating to Operating Decisions

Following are the important activities under the operating activities:

- Accounting of Purchase of Goods
- Accounting of Sale of Goods or Revenue
- Accounting of Operating Expenses

Accounting of Purchase of Goods

Purchases of revenue goods may be made for cash or on credit. Purchases are generally recorded when the goods are received from the seller.

- If goods are purchased for cash, there will be a corresponding decrease in the cash;
- If the goods are purchased on credit, there will be a corresponding increase of liabilities

Purchase and Accounting Equation

When goods are purchased on credit or cash, the accounting equation will be affected as follows:

Example 10.1

Table 10.2 shows the assets and the corresponding sources as on 1st April 2006.

Table 10.2					
Accounting Equation					
Sources			Assets		
12% Loan +	Profit +	Capital =	Cash +	Debtors+	Plant
50000	30000	20000	50000	60000	35000

The company acquires stock of goods costing 45,000 for cash. Observe the following changes in the new accounting equation as shown in table 10.3:

- Reduction of cash to the extent of Rs. 45,000
- Increase in stock to the extent of Rs. 45,000

Table 10.3						
Accounting Equation						
Sources			Assets			
12% Loans +	Profit +	Capital =	Cash +	Debtors+	Plant +	Stock
50000	30000	20000	5000	60000	35000	45000

Now let us see the accounting equation, if the stock is acquired on credit. Suppose the company acquires further stock costing Rs. 50,000 on credit from Mr X. The accounting equation after the credit purchase is shown by the table 10.4

10.4							
Accounting Equation							
Sources				Assets			
Mr.X +	12% Loans +	Profit +	Capital =	Cash +	Debtors+	Plant +	Stock
50000	50000	30000	20000	5000	60000	35000	95000

Purchase and Financial Statements

As mentioned in the previous section, purchase of revenue goods will affect the cash flow statement (in the case of cash purchases) and the balance sheet. Summary of the impact on the financial statements is as follows:

- Cash Flow Statement: Goods purchased for cash is shown as reduction in cash.

- Balance Sheet: Stock is shown as an asset.
- Income Statement: No effect until the stock is sold. When the stock sold, it becomes cost of goods sold (COGS) and is shown as an expense

Example 10.2

Assets and the corresponding sources of ABC Ltd as on 1st April 2006 are shown by Table 10.5. Transactions during the first quarter are as follows:

- Purchased stock of goods for cash = 30,000
- Depreciation on plant = 500
- Paid interest = 3000

Observe the following

- Goods purchased will appear as assets on the balance sheet
- Purchase of goods is not treated as an expense till they are sold.
- Interest and depreciation for the period are the other expenses.

Table 10.5	
Balance Sheet	
Sources	
Capital	50,000
10% Loan	100,000
	150,000
Assets	
Plant	30,000
Furniture	20,000
Cash	100,000
	150,000

Table 10.6	
Income Statement	
Sales	0
Less	
COGS	0
Depreciation	500
Interest	3,000
	3,500
Profit	-3,500

Table 10.7	
Cash Flow Statement	
Opening Balance	100000
Add	
Sales	0
Less	
Stock	30000
Interest	3000
	33000
Closing Balance	67000

Table 10.8	
Balance Sheet	
Sources	
Capital	50,000
10% Loan	100,000
Profit	-3,500
	146,500
Assets	
Plant	29,500
Furniture	20,000
Goods	30000
Cash	67,000
	146,500

Accounting for Sale of Goods/Revenue: Meaning

Accounting for revenue recognition is governed by the Accounting Standard- 9(AS-9). According to the AS-9, revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and rewards arising from the use of resources by them. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration. Revenue is also called sales or service charges and is the basis for determining the profit or loss for a particular period. Since the companies follow accrual

concept of accounting, actual collection is not an issue for recognizing the revenue. Excess of revenue over the expenses is treated as profit.

Table 10.9 shows the operating income and profit of Satyam Computers Services limited.

Table 10.9						
Income Statement for the year ending						
Year	Mar-03		Mar-04		Mar-05	
Sales	202,365	99%	254,154	97%	346,423	98%
Other income	2,786	1%	8,173	3%	8,255	2%
Total Income	205,151	100%	262,328	100%	354,678	100%
Expenditure						
Operating Expenses	140,512	68%	184,897	70%	257,508	73%
PBDIT	64,639	32%	77,431	30%	97,170	27%
Less: Interest	72	0.04%	75	0%	76	0%
PBDT	64,567	31%	77,356	29%	97,095	27%
Less: Depreciation	12,418	6%	11,162	4%	10,394	3%
PBT	36,903	18%	66,194	25%	86,700	24%
Tax provision	6,160	3%	10,615	4%	11,674	3%
PAT	30,742	15%	55,579	21%	75,026	21%

Source: Annual Reports of the Company

Revenue Recognition

Revenue recognition is the issue of timing of recognizing the revenue in the income statement to determine the profit or loss. Revenue is recognised or recorded in the incomes statement as follows:

Sale of goods and Accounting Equation

Sale of goods happens when the seller transfers the property in the goods to the buyer for a consideration. The transfer of property in goods, in most cases, results in or coincides with the transfer of significant risks and rewards of ownership to the buyer. Actual payment may take place later on.

Example- 10.3

Table 10.10 shows the assets and the corresponding sources of ABC Ltd as on 1st April 2006.

Table 10.10			
Accounting Equation			
Loan +	Capital =	Cash +	Stock
100,000	50,000	80,000	70,000

Let us see the impact on the equation if the 50% of the stock is sold for Rs.80,000. Table 10.11 shows the accounting ignoring other expenses and interest on the loan. Observe the following changes:

- Cash increases by Rs. 80,000
- Stock decreases by Rs. 35,000
- The balancing figure of Rs. 45,000 is treated as profit

Table 10.11				
Accounting Equation				
Profit+	Loan +	Capital =	Cash +	Stock
45,000	100,000	50,000	160,000	35,000

Or,

Table 10.12 shows the accounting equation, if the goods are sold on credit to Mr. X. Observe the following changes:

- Stock decreases by Rs. 35,000
- No change in cash
- Debtors appear to the extent of 80,000
- The balancing figure of Rs. 45,000 is treated as profit

Table 10.12					
Accounting Equation					
Profit+	Loan +	Capital =	Cash +	Stock +	Mr. x
45,000	100,000	50,000	80,000	35,000	80,000

Actual receipt of cash is not a condition for recognizing the revenue in financial statements. Let us continue with the above example:

Sale of Revenue Goods and Financial Statements

In the case of sale of goods, revenue is recognised when the property is transferred by the seller to the buyer. According to the AS-9, the transfer of property in goods, in most cases, results in or coincides with the transfer of significant risks and rewards of ownership to the buyer.

As mentioned in the previous section, sale of revenue goods will affect the cash flow statement (in case of cash sales) and the balance sheet. Summary of the impact on the financial statements is as follows:

- Cash Flow Statement: Sale of goods for cash is shown as a receipt.
- Income Statement: When the stock is sold, the corresponding cost becomes cost of goods sold (COGS) and is shown as an expense. Sales are shown as an income.
- Balance Sheet: Unsold stock is shown as an asset.

Example 10.4

ABC Ltd started business with a capital of Rs. 50,000 and a 12% loan of 100,000. Transactions during the first year:

- Purchased stock of revenue goods = 70,000
- Sold 50% of the goods for Rs. 80,000
- Other expenses = 5,000
- Interest paid = 12,000.

Table 10.13	
Opening Balance Sheet	
Capital	50,000
Loan	100,000
	150,000
Cash	150,000
	150,000

Table 10.14	
Income Statement	
Sales	80,000
Less	
COGS	35,000
Expenses	5,000
Interest	12,000
	52,000
Profit	28,000

Table 10.15	
Cash Flow Statement	
Capital	50,000
Loan	100,000
Sales	80,000
	230,000
Less	
Stock	70,000
Expenses	5,000
Interest	12,000
	87,000
Cash balance	143,000

Table 10.16	
Closing Balance Sheet	
Capital	50,000
Loan	100,000
Profit	28,000
	178,000
Cash	143,000
Stock	35,000
	178,000

Revenue Recognition in the case of Services

According to the As-9, revenue from the service should be recognised in one of the following methods:

- **Proportionate Completion Method:** Proportionate completion method is a method of accounting which recognises revenue in the statement of profit and loss proportionately with the degree of completion of services under a contract.
- **Completed service method:** Completed service contract method is a method of accounting which recognises revenue in the statement of profit and loss only when the rendering of services under a contract is completed or substantially completed.

Example 10.5

ABC Ltd provides networking services to several companies. The assets and sources of the company are shown in the table 10.17.

Table 10.17			
Balance Sheet			
Capital	10,000	Computers	90000
Profit	80000	Cash	20000
12% Loan	20000		
	110,000		110,000

During the year the company received an order to set up the computer centre of a group of local schools (8 schools) for a consolidated fee of Rs. 450,000. Other expenses per year are Rs. 25,000. Entire money was also collected as an advance. Company completed the job in 2 years. During the first year work was completed in five schools. The financial statements under the different methods of revenue recognition are as follows.

Proportionate Completion Method

Under this method the income is distributed over the two years as follows:

- Revenue (Income Statement)
 - First year = $450,000 \times \frac{5}{8} = 281,250$
 - Second year = $450,000 \times \frac{3}{8} = 168,750$
- Cash collection in the first year (Cash Flow Statement)
 - Collection received from the customers = Rs. 450,000
- Advance to be shown as a liability (Balance Sheet)
 - Collection to the extent not treated as income is shown as a liability.
 - Advance from Customer = Collection from customer – Current Income = $450,000 - 281,250 = 168,750$. Income received but not due is treated as a liability.
- Interest Expense (Income Statement) = $12\% \text{ on } 20,000 = 2,400$
- Accumulated Profit (Balance Sheet) = Opening Profit + Current Profit = $80,000 + 253,850 = 333,850$
- Assumption: No depreciation

First Year Financial Statements: Income statement, cash flow statement for the first year and the balance sheet as at the end of the first year are shown in table 10.18 through table 10.20.

Table 10.18	
Income Statement	
Service Charges	281,250
Less Expenses	25,000
Interest	2,400
Profit	253,850

Table 10.19	
Cash Flow Statement	
Opening CIH	20,000
Service Charges	450,000
Less Expenses	25,000
Interest	2,400
CIH	442,600

Table 10.20	
Balance Sheet	
Capital	10,000
Accumulated Profit	333,850
Loan	20,000
Advance	168,750
	532,600
Computers	90,000
Cash	442,600

Table 10.21	
Income Statement	
Service Charges	168,750
Less Expenses	25,000
Interest	2,400
Profit	141,350

Table 10.22	
CFS	
Opening CIH	442,600
Service Charges	0
Less Expenses	25,000
Interest	2,400
CIH	415,200

Table 10.23	
Balance Sheet	
Capital	10,000
Accumulated Profit	475,200
Loan	20,000
Advance	0
	505,200
Computers	90,000
Cash	415,200
	505,200

Completed service method

Under this method the income will recognised only in the second year:

- Revenue:
- First year Nil
- Second year = 450,000
- Cash collection (first year) = 450,000
- Advance = Collection from customer – Current Income = 450,000

First Year Financial Statements: Income statement, cash flow statement for the first year and the balance sheet as at the end of the first year are shown in table 10.24 through table 10.26.

Table 10.24	
Income Statement	
Service Charges	0
Less	
Expenses	25,000
Interest	2,400
Profit	-27,400

Table 10.25	
CFS	
Opening CIH	20,000
Service Charges	450,000
Less	
Expenses	25,000
Interest	2,400
CIH	442,600

Table 10.26	
Balance Sheet	
Capital	10,000
Accumulated Profit	52,600
Loan	20,000
Advance	450,000
	532,600
Computers	90,000
Cash	442,600
	532,600

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Second Year Financial Statements: Income statement, cash flow statement for the first year and the balance sheet as at the end of the first year are shown in table 10.27 through table 10.29.

Table 10.27	
Income Statement	
Service Charges	450,000
Less	
Expenses	25,000
Interest	2,400
Profit	422,600

Table 10.28	
CFS	
Opening CIH	442,600
Service Charges	0
Less	
Expenses	25,000
Interest	2,400
CIH	415,200

Table 10.29	
Balance Sheet	
Capital	10,000
Accumulated Profit	475,200
Loan	20,000
Advance	0
	505,200
Computers	90,000
Cash	415,200
	505,200

Sales through Credit Card

Now days most of the companies accept payment through the credit cards. Some of popular credit cards are VISA and MASTER Card. Companies accepts payments through the cards to attract the customers. The banks generally charge a service charge on the credit card amount. So the entire sale proceeds will not be an income for the company. The charge should be shown as an expense or discount.

Are all cards same? No. Sales through the VISA card are generally treated as cash or bank sales. Sales through the Diners Club card or AMEX card will be treated as credit sales.

Discount on Sales

A company may offer discount to its customers. Such discounts can be divided into two broad categories:

- Trade Discount
- Cash Discount

Trade Discount is generally given as an incentive for large purchases. Whereas the cash discount is given as an incentive for prompt payment. Separate account is maintained in the books for cash discount.

Example 10.6

Assets and the corresponding sources of ABC Ltd as on 1st April 2006 by the table 10.30

Table 10.30					
Accounting Equation					
Sources			Assets		
Profit+	12% Loan +	Capital =	Cash +	Stock +	Debtors
45,000	100,000	50,000	80,000	35,000	80,000

During the period, the company gave incentive of 10% discount to all those customers who paid money within 10 days. Mr. X, who owes, Rs. 30,000 paid the money due.

- Discount: is shown as expense in the income statement = 3,000
- Collection = 30,000 – 3,000 = 27,000 shown as a receipt in the Cash Flow Statement
- Interest for the quarter = 3000
- No income during the period
- Accumulated profit = opening profit – current loss = 45,000 - 6,000 = 39,000
- Debtors = Opening Debtors – Collection – Discount = 80,000 - 27,000 – 3000 = 42,000

Financial Statements at the end of the first quarter: Income statement, cash flow statement for the first quarter and the balance sheet as at the end of the first quarter are shown in table 10.31 through table 10.33.

Table 10.31	
Income Statement	
Sales	0
Less	
Discount	3,000
Interest	3,000
Profit	-6,000

Table 10.32	
Cash Flow Statement	
Opening CIH	80,000
Collection	27,000
Less	
Interest	3000
CIH	104,000

Table 10.33	
Balance Sheet	
Capital	50,000
Profit	39,000
Loan	100,000
	189,000
Stock	35,000
Cash	104,000
Debtors	50,000
	189,000

Accounting for Bad Debts

When the receivables become uncollectible they are called bad-debts. Such bad-debts are shown as a loss in the income statement and the debtors to that extent are reduced in the balance sheet.

Example 10.7

Table 10.34 shows the balance sheet of ABC as on 1st April 2006

Table 10.34			
Balance Sheet as on 1 st April 2006			
Sources		Assets	
Capital	50,000	Stock	35,000
Profit	42,000	Cash	107,000
10% Loan	100,000	Debtors	50,000
	192,000		192,000

During the year 2006 year, the company had the following transactions:

- Collection from debtors = 45,000
- Balance of the debtor became bad debt
- Interest paid = 10,000 (10% on loan)
- No sales during the period.
- No other expense

Financial Statements at the end of the year: Income statement, cash flow statement for the year and the balance sheet as at the end year are shown in table 10.35 through table 10.37.

Table 10.35	
Income Statement	
Sales	0
Less	
Bad Debts	5,000
Interest	12,000
Profit	-17,000

Table 10.36	
Cash Flow Statement	
Opening CIH	107,000
Collection	45,000
Less	
Interest	12,000
CIH	140,000

Table 10.37	
Balance Sheet	
Capital	50,000
Profit	25,000
Loan	100,000
	175,000
Stock	35,000
Cash	140,000
Debtors	0
	175,000

Some times the bad debts are recovered on a later date. At the time of the collection, bad-debt recovered is shown as an income and there will be a corresponding increase in the cash balance.

Sale of Debtors: Factoring

Generally companies wait till the due date and then collect the amount from the debtors. That is the normal treatment of debtors. However, now days companies sell their receivables. By doing so the companies expedite the process of collection instead of waiting till due date.

The process of selling the debtors is called factoring. The party to whom the debtors are sold is called a factor. A factor is a bank or a financial intermediary that buys debtors. The factor, in turn collects money from the debtor on the due date. Factor charges a commission for providing such service. Such commission is treated as an expense in the books of the seller. Factoring can be broadly divided into two categories: non-recourse and recourse factoring

Non Recourse factoring: It is the most comprehensive type of factoring arrangement offering all types of services namely:

- Finance
- Sales Ledger Administration
- Collection
- Debt Protection
- Advisory Services

It gives protection against bad debts to the client. In other words, in case the customer fails to pay, the factor will have 'no recourse' to the client and will have to absorb the bad debts himself.

Recourse Factoring : In this type of factoring arrangement, the factor provides all types of facilities except debt protection. In other words, the client is responsible for any bad debts incurred.

Example 10.8

Table 10.38 shows the balance sheet of ABC Ltd as on 1st April 2006

Table 10.38			
Balance Sheet			
Capital	50,000	Stock	35,000
Profit	27,000	Cash	100,000
12% Loan	100,000	Debtors	42,000
	177,000		177,000

During the month of May, the company sold the debtors to a bank. The bank charged a commission of 4%.

The financial statements at the end of the month are shown by table 10.39 to table 10.41

- Expenses for the month = 4% of 42,000 = 1,680
- Money collected from the bank in consideration of the transferring of debtors = Rs. 40,320
- Interest for the month = Rs. 1,000
- No other incomes and expenses

Table 10.39	
Income Statement	
Sales	0
Less	
Commission	1,680
Interest	1,000
Profit	-2,680

Table 10.40	
Cash Flow Statement	
Opening CIH	100,000
Collection from the factor	40,320
Less	
Interest	1,000
CIH	139,320

Table 10.41	
Balance Sheet	
Capital	50,000
Profit	24,320
Loan	100,000
	174,320
Stock	35,000
Cash	139,320
Debtors	0
	174,320

Accounting for Bills Receivables

Some times companies ask for a negotiable instrument as an acknowledgement of the debt. It shows the period after which the debtor pays money. Such instrument is called Bills Receivables or Notes Receivable. Bills receivable is shown as an asset in the books of the seller. The seller of the goods can use the bills receivable as follows:

- Retain till the date of maturity and collect the money due from the debtor.
- Discount it with the bankers
- Endorse it in favour of creditors.

Example 10.9

Following is the balance sheet of ABC Ltd. as on 1st April 2006

Table 10.42			
Balance Sheet as on 1 st April 2006			
Sources		Assets	
Capital	50,000	Stock	35,000
Profit	27,000	Cash	100,000
12% Loan	100,000	Debtors	42,000
	177,000		177,000

Transactions during the month of May are as follows:

- Sold stock on credit for Rs. 50,000 and received a bill (negotiable instrument) for a period of three months

Financial statements for the month of May are shown by table 10.43 to table 10.45.

Table 10.43	
Income Statement	
Sales	50,000
Less	
COGS	35,000
Interest	1,000
Profit	14,000

Table 10.44	
Cash Flow Statement	
Opening CIH	100,000
Less	
Interest	1,000
CIH	99,000

Table 10.45	
Balance Sheet	
Capital	50,000
Profit	41,000
12% Loan	100,000
	191,000
Stock	0
Cash	99,000
Bills Receivable	50,000
Debtors	42,000
	191,000

Accounting for Operating Expenses

Every company incurs several expenses for undertaking the operations. Some of the common and important expenses are as follows:

- Employee Related Expenses
- Repairs and Maintenance Expenses
- Administration Expenses

Impact of these expenses on the accounting equation and the financial statements are shown through the following example

Example 10.10

Table 10.46 shows the assets and the corresponding sources of ABC Ltd. as on 1st April 2006:

Table 10.46					
Accounting Equation as 1 st April 2006					
Profit+	Loan +	Capital =	Cash +	Stock +	Debtors
80,000	100,000	150,000	130,000	70,000	130,000

During the first quarter, the company incurred the following expenses:

- Rent paid for the entire year: 60,000
- Salary per month: 10,000; Salary for June to be paid in July
- Telephone expenses paid: 5000

Accounting equation at the end of the first quarter (30th June) shown by table 10.47

Table 10.47							
Accounting Equation as on 30 th June 2006							
Profit+	OS Salary+	Loan +	Capital =	Cash +	Stock +	Debtors +	Advance Rent
30,000	10,000	100,000	150,000	45,000	70,000	130,000	45000

Profit reduced by 50,000 due to the following expenses:

- Rent: 15,000
- Salary: 30,000
- Telephone Expenses: 5000

Cash reduced by 85,000 due to the following payments:

- Rent: 60,000: Excess (45,000) paid over the rent for the period will be treated as an asset
- Salary: 20,000: Balance to be paid (10,000) will be treated as a liability
- Telephone Expenses = 5000

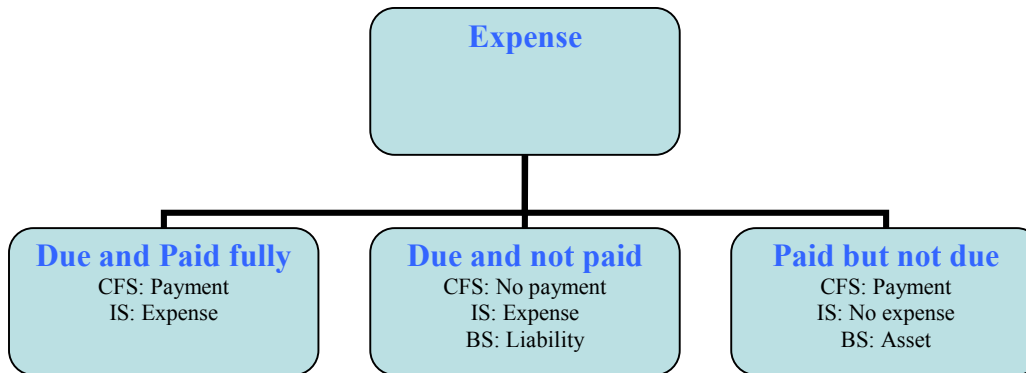
Financial statement for the quarter are shown by the tables 10.48 through 10.50

Table 10.48	
Income Statement	
Sales	0
Less	
Salary	30,000
Rent	15000
Telephone Exp	5000
	-
Profit	50.000

Table 10.49	
CFS	
Opening CIH	130,000
Less	
Telephone Expense	5000
Rent	60000
Salary	20000
Closing CIH	45,000

Table 10.50	
Balance Sheet	
Capital	150,000
Profit	30,000
Loan	100,000
Outstanding Salary	10,000
	290,000
Stock	70,000
Cash	45,000
Prepaid Rent	45,000
Debtors	130,000
	290,000

So when a company incurs expenses either the cash reduces immediately or a liability is created. Relationship between expenses and payment can be shown as follows:



Example 10.11

On 1st April 2006, started business with capital of Rs. 50,000. Other transactions during the first quarter are as follows:

- Paid insurance premium for the year = Rs. 12,000
 - Payment CFS = 12,000 (Cash Flow Statement)
 - Expenses for the quarter = Rs. 3,000 (Income Statement)
 - Premium paid but not due = Rs. 9,000 (Balance Sheet)
- Salary for the quarter paid = Rs. 15,000
 - Payment = 15,000 (Cash Flow Statement)
 - Expenses for the quarter = Rs. 15,000 (Income Statement)
- Rent due but not paid = Rs. 30,000
 - Payment = Nil (Cash Flow Statement)
 - Expenses for the quarter = Rs. 30,000 (Income Statement)
 - Expense due but not paid = Rs. 30,000 (Balance Sheet)

Financial statements for the quarter ending June 2006 are shown by table 10.51 through table 10.53

Table 10.51	
Income Statement	
Incomes	0
Expenses	
Insurance Premium	3,000
Salary	15,000
Rent	30,000
	48,000
Profit	-48,000

Table 10.52	
Cash Flow Statement	
Capital	50,000
Payments	
Insurance Premium	12,000
Salary	15,000
Rent	0
Total	27,000
CIH	23,000

Table 10.53	
Balance Sheet	
Capital	50,000
Outstanding Rent	30,000
Profit	-48,000
	32,000
Cash	23,000
Prepaid Insurance	9,000
	32,000

Table 10.54 shows the revenue and expenses of some of the well known companies of India.

Revenue and Expenses of Tata Companies						
Rs. Crore (Non-Annualised)	TCS	Tata Motors			Tata Steel	
Income						
Operating income	11,236	99%	23,568	96%	17,140	97%
Other income	65	1%	609	2%	258	1%
Change in stocks	4	0%	257	1%	105	1%
Non-recurring income	41	0%	201	1%	98	1%
	11,346	100%	24,636	100%	17,601	100%
Expenditure		0%		0%	0	0%
Operating expenses	831	7%	14,633	59%	3,762	21%
Purchase of finished goods	123	1%	1,143	5%	1,352	8%
Energy (power & fuel)	67	1%	259	1%	898	5%
Salaries & wages	5,177	46%	3,436	14%	2,060	12%
VRS expenses	0	0%	498	2%	81	0%
Indirect taxes	20	0%	335	1%	1,004	6%
Other expenses	1,706	15%	1,706	7%	2,372	13%
Less: expenses capitalised	0	0%	309	1%	113	1%
Non-recurring expenses	0	0%	55	0%	41	0%
	7,924	70%	22,374	91%	11,682	66%
Profits / losses		0%		0%	0	0%
PBDIT	3,422	30%	2,880	12%	6,144	35%
Financial charges	52	0%	302	1%	170	1%
PBDT	3,370	30%	2,578	10%	5,975	34%
Depreciation	257	2%	524	2%	734	4%
PBT	3,112	27%	2,054	8%	5,241	30%
Tax provision	396	3%	525	2%	1,734	10%
PAT	2,717	24%	1,529	6%	3,506	20%
		0%		0%	0	0%
Appropriation of profits		0%		0%	0	0%
Dividends	753	7%	568	2%	820	5%
Retained earnings	1,964	17%	961	4%	2,686	15%

Most of the companies show the extra-ordinary items (expenses and incomes) in the income statements. Such items are those which occur once in a while and include the follow:

- Profit or loss on the sale of fixed assets
- Profit or loss on the sale of investments
- Refund of direct taxes
- Employee separation or expenses
- Provision for diminution/appreciation in the value of investments

Revenue Recognition when delivery is subject to conditions:

Some times the delivery of goods is subject to certain conditions of the agreement. In such cases the revenue should be recognized as follows:

- Sales on Approval: Revenue should be recognized when the buyer confirms that that he has approved the sales and buy the goods. Till that date, goods send on approval should not be included in sales.
- Sales with Warranty: Sales should be recognized immediately when the goods are sold. However, a provisions should be created for the warranty.
- Subscription for publication: Revenue should be recognized on straight-line base over the time.
- Installment Sale: In this case, the equal annual or monthly installment should be segregated into sales and principal.
- Admission fee: Revenue from the performance of artists should be recognized when the event take place.
- Subsequent uncertainty in collection: When a company expects some uncertainty in the collection of revenue, it is necessary to create provisions to that effect.

Accounting Policies Relating to Revenue Recognition**ABB Ltd**

Sales of products and services are recognised when significant risks and rewards of ownership of products are passed on to customers or when the service has been provided. Sales are stated at contractual realisable values, net of excise duty, sales tax, value added tax and trade discounts.

Revenues from long-term contracts are recognised on the percentage of completion method, in proportion that the contract costs incurred for work performed up to the reporting date bear to the estimated total contract costs. Contract revenue earned in excess of billing has been reflected under "Other Current Assets" and billing in excess of contract revenue has been reflected under "Liabilities" in the balance sheet.

Full provision is made for any loss in the year in which it is first foreseen.

Liquidated damages/penalties are provided for as per the contract terms wherever there is a delayed delivery attributable to the Company.

Commission income is recognised as per contracts/receipt of credit note.

Dividend income is recognised when the right to receive dividend is established.

Interest income is recognised on the time proportion method.

Mahindra & Mahindra Ltd.

Sales of products and services are recognised when the products are shipped or services rendered. In respect of sale of property (concerning property development activity), the Company accounts for the income on the percentage of completion basis. [Refer paragraph (H) below].

Dividend from investments are recognised in the Profit and Loss

Account when the right to receive payment is established.

Marico Ltd.

(i) Domestic Sales are recognised at the point of dispatch of goods to the customers and stated net off trade discount and exclusive of sales tax but inclusive of excise duty. ;

(ii) Export sales are recognised based on bill of lading,

(iii) Revenue from services is recognized on rendering of the service

(iv) Agency commission is recognised upon effecting sales on behalf of the principal, (v) Interest and other income are recognised on accrual basis, (h) Retirement benefits

The Company has various schemes of retirement benefits, namely, provident fund, superannuation fund, gratuity and leave encashment. Provident, superannuation and gratuity funds are administered through trustees and the Company's contribution thereto is charged to revenue every year. Leave encashment and gratuity are provided for on the basis of actuarial valuation as at the year end by an independent actuary.

Dr. Reddy's Laboratories

Revenue from sale of goods is recognised when significant risks and rewards in respect of ownership of products are transferred to customers. Revenue from domestic sales of formulation products is recognised on despatch of products to stockists by clearing and forwarding agents of the Company. Revenue from domestic sales

of active pharmaceutical ingredients and intermediates is recognised on despatch of products from the factories of the Company. Revenue from export sales is recognised on shipment of products.

Revenue from product sales is stated exclusive of returns, sales tax and applicable trade discounts and allowances.

Service income is recognised as per the terms of contracts with customers when the related services are performed, or the agreed milestones are achieved.

Dividend income is recognised when the unconditional right to receive the income is established. Income from interest on deposits, loans and interest bearing securities is recognised on the time proportionate method.

Export entitlements under the Duty Entitlement Pass Book ("DEPB") scheme are recognised as income when the right to receive credit as per the terms of the scheme is established in respect of the exports made and where there is no significant uncertainty regarding the ultimate collection of the relevant export proceeds.

The Company enters into certain dossier sales, licensing and supply arrangements with certain third parties. These arrangements include certain performance obligations by the Company. Revenue from such arrangements is recognised in the period in which the Company completes all its performance obligations.

Satyam computers

Revenue from professional services consist primarily of revenue earned from services performed on a "time and material" basis. The related revenue is recognized as and when the services are performed.

The Company also performs time bound fixed-price engagements, under which revenue is recognized using the percentage of completion method of accounting. The cumulative impact of any revision in estimates of the percentage of work completed is reflected in the year in which the change becomes known. Provisions for estimated losses on such engagements are made during the year in which a loss becomes probable and can be reasonably estimated.

Amounts received or billed in advance of services performed are recorded as advance from customers/unearned revenue. Unbilled revenue, included in debtors, represents amounts recognized based on services performed in advance of billing in accordance with contract terms.