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As 4 contingencies And events occurring After the balance sheet date

1.0 objective:

The objective of the accounting standard is to prescribe the accounting treatment for contingencies and events occurring after the balance sheet date but before approval of balance sheet by board of directors.

2.0 applicability:

To all enterprises – mandatory W.e.f 1-4-1998

3.0 NoN applicability:

- Liabilities of life assurance and general insurance enterprises;
- Obligations under retirement benefit plans; and
- Commitments arising from long term lease contracts.

4.0 ContingenCies

As per ICAI pronouncement, it is having limited applicability for the items which are shown as deductions from assets. For contingencies AS-29 shall be applied.

5.0 events occurring after balance sheet :

These are significant events, both favorable and unfavorable, that occur between the balance sheet date and the date on which the financial statements are approved by the board of directors in the case of a company and by the corresponding approving authority in the case of another entity.

There are two types of events which can be identified as

a. Adjusting Events:

- The events which provide further evidence of conditions that existed at the balance sheet date.
- Loss should be accounted in the accounts and assets and liabilities to be adjusted.
- Appropriate disclosure should be made in notes to the accounts.
- Example: debtor is insolvent as on balance sheet date but filed insolvency petition after balance sheet date but before financial statements approved by the board.
- Practical example: A Ltd., whose accounting year ends on 31/03/2013, agreed in principle to sell a plot of land on 18/03/2013 at a price to be determined by an independent valuer. Pending the agreement for sale and due to non-receipt of valuer's report, the sale of the land could not be completed up to 31/03/13. The company received the report on April 7, 2013 and the agreement was signed on April 10, 2013. The

financial statements for 2012-13 were approved by the board on May 12, 2013.

- The sale of land is an event occurring after the balance sheet date. Also, the condition, which led to the sell, existed on the balance sheet date. The signing of the agreement provides further evidence as to the condition that existed on the balance sheet date. The sale of land after the balance sheet date is therefore an adjusting event, which means the sale transaction should be recorded in books of A Ltd. for the purpose of its financial statements for 2012-13.

b. Non adjusting events:

- Those which are indicative of conditions that arose subsequent to the balance sheet date. i.e. events not related to the circumstances existing on balance sheet date, in other words entirely new events after balance sheet date.
- No adjustment in accounts.
- Appropriate disclosure should be made in notes to the accounts.
- Example :
  An earthquake destroyed a major warehouse of C Ltd. on April 20, 2013. The last accounting year of the company ended on 31/03/13 and the financial statements for the year were approved on May 8, 2013. The destruction of warehouse is a significant event occurring after the balance sheet date, but since the earthquake did not exist on the balance sheet date, the destruction by earthquake is a non-adjusting event. The value of property lost by earthquake therefore need not be recognized in financial statement of 2012-13

  The Report of the Directors* for 2012-13 should disclose the fact of earthquake together with an estimate of loss on earthquake. If no estimate of loss can be made, the report should state that loss on earthquake could not be estimated.

6.0 other points

- **Events effecting going concern assumption:** Events which are not having any evidence as on the date of balance sheet date but which are occurred after balance sheet date which are occurred after balance sheet.

  Ex: Major fire Accident for the company or factory

- **Proposed Dividend:** any divided which are proposed or declared after the balance sheet date but before approval of the financial statements should be adjusted in accounts because it belongs to the period covered by the financial statements.

- **Events occurring after approval of accounts:** any events occurred after approval of the financial statements by the board, such events should be disclosed in the director's report if they are material and involving financial commitment.

7.0 Disclosure

a) **with respect to contingencies:** if any material contingent loss is not provide for then enterprise should disclose

- the nature of the contingency;
- the uncertainties which may affect the future outcome;
- an estimate of the financial effect or
- a statement that such an estimate cannot be made.

b) **With respect to events occurring after the balance sheet date:** If any adjustment event is not provided for then enterprise should disclose

- The nature of the event
- An estimate of the financial effect, or
- A statement that such an estimate cannot be made.

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Quick revision

Objective

To prescribe the accounting of contingencies and events, that take place after the balance sheet date but before approval of financial statement by competent authority

Scope

Contingencies

As per ICAI pronouncement, it is having limited applicability for the items which are shown as deductions from assets. For contingencies AS-29 shall be applied

Events

Relating to the circumstances existing in the balance sheet

Adjusting Event

- Loss should be provided
- Assets and liabilities to be adjusted

Relating to the circumstances existing after the balance sheet made

Non adjusting event

Disclosure by way of notes to accounts

Disclosure

1. Nature of contingency or event
2. Estimate of financial effect.
3. It contingent does not provide reasons for should disclose

Practical Problems

1) A Limited Company closed its accounting year on 30.6.13 and the accounts for that period were considered and approved by the board of directors on 20th August, 2013. The company was engaged in laying pipe line for an oil company deep beneath the earth. While doing the boring work on 1.9.2013 it had met a rocky surface for which it was estimated that there would be an extra cost to the tune of Rs. 80 lakhs. You are required to state with reasons, how the event would be dealt with in the financial statements for the year ended 30.6.2013.

Solution:

Para 3.2 of AS 4 (Revised) on Contingencies and Events Occurring after the Balance Sheet Date defines 'events occurring after the balance sheet date' as 'significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which financial statements are approved by the Board of Directors in the case of a company'. The given case is discussed in the light of the above entioned definition and requirements given in paras 13-15 of the said AS 4 (Revised)

In this case the incidence, which was expected to push up cost became evident after the date of approval of the accounts. So that was not an 'event occurring after the balance sheet date'. However, this may be mentioned in the Directors' Report

2) You are an accountant preparing accounts of A Ltd. as on 31.3.2013. After year end the following events have taken place in April, 2013:

i. A fire broke out in the premises damaging, uninsured stock worth Rs. 10 lakhs (Salvage valueRs. 2 lakhs).
ii. A suit against the company's advertisement was filed by a party claiming damage of Rs. 20 lakhs.
iii. Dividend proposed @ 20% on share capital of Rs. 100 lakhs.

Describe, how above will be dealt with in the account of the company for the year ended on 31.3.2013.

Solution:

Events occurring after the Balance Sheet date that represent material changes and commitments affecting the financial position of the enterprise must be disclosed according to para 15 of AS 4 on Contingencies and Events occurring after the Balance Sheet date. Hence, fire accident and loss thereof must be disclosed.

Suit filed against the company being a contingent liability must be disclosed with the nature of contingency, an estimate of the financial effect and uncertainties which may affect the future outcome must be disclosed as per para 16 of AS 4.

There are events which, although take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature. Such items include the amount of dividend proposed or declared by the enterprise after the balance sheet date in respect of the period covered by the financial statements. Thus, dividends which are proposed or declared by the enterprise after the balance sheet date but before approval of the financial statements, should be adjusted as per para 14 of AS 4.

3) ABC Ltd. could not recover Rs. 10 lakhs from a debtor. The company is aware that the debtor is in great financial difficulty. The accounts of the company were finalized for the year ended 31.3.2005 by making a provision @ 20% of the amount due from the said debtor.

   The debtor became bankrupt in April, 2005 and nothing is recoverable from him.

   Do you advise the company to provide for the entire loss of Rs. 10 lakhs in the books of account for the year ended 31st March, 2005?

Solution:

As per AS 4 ‘Contingencies and Events occurring after the Balance Sheet Date’, adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the Balance Sheet date.

In the given case, bankruptcy of the debtor in April, 2005 and consequent non-recovery of debt is an event occurring after the balance sheet date which materially affects the determination of profits for the year ended 31.3.2005. Therefore, the company should be advised to provide for the entire amount of Rs. 10 lakhs according to para 8 of AS 4.