AS 20 - Earnings Per Share

- Applicable to CFS
- Potential Equity Share is a Financial Instrument
- Example of Potential Equity Share
  - Convertible Debt instruments or preference shares into equity shares;
  - Share warrants;
  - Options - ESOP; and
  - Contingently issuable shares
- Present basic and diluted EPS, even if the amounts disclosed are **negative** (**loss per share**).

$$\text{Basic EPS} = \frac{\text{Net Profit After Tax (-) Preference Dividend [+ Tax on Divd]}}{\text{Weighted Avg. No. of Equity Shares O/s during the Period}}$$

- NPAT is After Prior Period Item & Extraordinary Item as per AS 5
- Does not include any preference dividends paid or declared during the **current period** in respect of **previous periods**.
- Weighted Avg. No. of Equity Shares O/s during the Period

01.01.2011	Opening Balance [Nos.]	1800
31.05.2011	Issue of Shares for Cash [Nos.]	600
01.11.2011	Buy Back of Shares [Nos.]	300
31.12.2011	Closing Balance [Nos.]	2100

Computation of Weighted Average:

(1,800 x12/12) **+** (600 x 7/12) **-** (300 x 2/12) = 2,100 shares.

- **<u>Time Weighting Factor</u>** [Relevant Dates for Weight]

Equity Shares Issued	Relevant Date
As Exchange For Cash	Date of Cash **Receivable**
As a Result of Conversion of Debt	Date of Conversion
In Exchange for a Settlement of Liability	Date on Which Settlement becomes Effective
Bonus Shares	**Beginning of Reporting Period**
As Part of Consideration in an Amalgamation Nature of **Merger** Nature of Purchase	 **Beginning of Year** Date of Acquisition
For Rendering Service to the Enterprise	Date of Service **Rendered**
In Lieu of Int./ Principal on other Financial Instrument	Date of Interest **Ceases to Accrue**
For Acquisition of an Asset	Date of Acquisition **Recognised**

- Partly paid shares are entitled to participate in the dividend **to the extent of amount paid**

Date	Particulars	No. of Shares Issued	Nominal Value	Amt. Paid
01.01.2011	Opening Balance	1800	10	10
31.10.2011	Issue of Shares	600	10	5

Computation of weighted average would be as follows:

(1,800x12/12) + (**[600x5/10]** x2/12) = 1,850 shares

- If enterprise has **more than one class** of equity shares, net P/L is apportioned over the different classes of shares as per their **dividend rights**.
- Equity shares of **different nominal values** but with the **same dividend rights** = Number of equity shares is calculated by **converting** all such equity shares into equivalent number of shares of the **same nominal value**.

- Weighted average number of equity shares outstanding during the period **and for all periods** presented should be **adjusted** for events, that have **changed the number of equity** shares outstanding, without a corresponding change in resources [**other than** the conversion of **potential equity shares**].

↓ Examples

  - Bonus issue;
  - Bonus element in any other issue [Eg. Rights issue];
  - Share split; and
  - Reverse share split (consolidation of shares).

<u>Bonus Issue or Share Split</u>

Issued to existing shareholders for no additional consideration. Number of shares outstanding is increased without increase in resources. Number of equity shares outstanding before the event - Adjusted as if the event had occurred at the **beginning of the earliest period reported**.

Net profit for the year 2010	18,00,000
Net profit for the year 2011	60,00,000
No. of equity shares outstanding until 30.09.2011	20,00,000
Bonus Issue 01.10.2011	2 shares for each share outstanding at 30.09.2011 20,00,000 x 2 = 40,00,000
EPS for the Year 2011	$\frac{60,00,000}{20,00,000 + 40,00,000}$ = Rs.1.00
***Adjusted** EPS for the **<u>Year 2010 [beginning of earliest period reported]</u>**	$\frac{18,00,000}{20,00,000 + \mathbf{40,00,000}}$ = Rs.0.30

* Bonus Considered **only** for Calculating **Adjusted** EPS – Not for Basic EPS for Earlier Period

<u>Rights Issue</u>

- Conversion of potential equity shares – No Bonus Element - issued for full value
- In Rights Issue - Exercise price less than fair value of shares - includes bonus element
- Number of equity shares used in calculating basic EPS for **all** periods **PRIOR** to rights issue is the number of equity shares outstanding prior to issue, **multiplied** by the following factor:

$$\frac{\text{Fair value [Market Value] per share immediately } \textbf{PRIOR} \text{ to the exercise of rights}}{\textbf{Theoretical} \text{ ex-rights fair value per share}}$$

$$\text{Theoretical ex-rights fair value per share} = \frac{A + B}{C + D}$$

A = Fair Value [Market Price] of **ALL** Shares O/s Immediately **BEFORE** Exercise of Rights
B = Total Amount Received From Exercise of Right
C = No. of Shares Outstanding **PRIOR** to Rights Offer
D = No. of Shares Issued in Exercise of Rights

Net Profit	Year 2010 : Rs. 11,00,000 Year 2011 : Rs. 15,00,000
No. of shares outstanding prior to rights	5,00,000
Rights Issue	One new share for each 5 O/s (i.e. 1,00,000 new shares) Rights issue price : Rs.15.00 Last date to exercise rights : 01.03.2011
FV of one equity share immediately prior to exercise of rights on 01.03.2011	Rs. 21.00

Theoretical ex-rights fair value per share	A + B C + D [21 x 5,00,000] + [15 x 1,00,000] = Rs. 20.00 5,00,000 + 1,00,000
Computation of **Adjustment Factor**	FV per share PRIOR to Exercise of Rights Theoretical ex-rights fair value per share 21 = **1.05** 20

Computation of EPS

Particulars	Year 2010	Year 2011
EPS for 2010 as **Originally** Reported : Rs. 11,00,000 / 500,000 shares	Rs. 2.20	
EPS for 2010 as **Restated** for Rights Issue : Rs. 11,00,000 / [500,000 sh x **1.05**]	Rs. 2.10	
EPS for 2011 including effects of Rights Issue : Rs. 15,00,000 / [500,000 x **1.05** x **2/12**] + [6,00,000 x 10/12]		Rs. 2.55

Calculating Diluted EPS

Diluted EPS = Net Profit Available for Equity Shares [After Adjustment of Diluted Earnings] / Wtd. Avg. of Sh. O/s during the period [Assuming Conversion of diluted Potential Eq. Sh. [DPES]]

Calculation of Diluted Earnings

NPAT for Equity Shareholders	xxxx
Add : Preference Dividend as Adjusted for Tax [Divd + Tax]	xxx
Add : Interest on Convertible Debentures net of Tax [Int – Tax]	xxx
Less : *Income that will Cease to Accrue on Conversion of DPES into ES as adj. for Tax	(xxx)
Net Profit available for DPES	xxxx

*Expenses will be added

Addition in No. of Shares

DPES should be deemed to have been converted into equity shares at the **Beginning** of the Period OR if issued Later, Date of Issue of PES.

Share application money pending allotment or any advance share application money as at the balance sheet date, which is not statutorily required to be kept separately and is being utilised in the business of the enterprise, is treated in the same manner as DPES for the purpose of calculation of diluted EPS.

Contingently Issuable Shares [CIS]

- Issuable upon satisfaction of certain conditions resulting from contractual arrangements.
- Included in the computation of both **BASIC** EPS **AND DILUTED** EPS from the date when the conditions under a contract are met.
- If conditions not met, for computing **DILUTED** EPS, CIS are included as of the **beginning** of the period or as of the date of contingent share agreement, if later. [If Conditions not met then do **not** include CIS in Basic EPS]
- Restatement is not permitted if conditions are not met when contingency period actually **expires subsequent** to the end of the reporting period. This provisions apply equally to PES that are issuable upon the satisfaction of certain conditions (contingently issuable PES).

Options and other share purchase arrangements

Dilutive when they would result in the issue of equity shares for **less than** fair value.

Net profit for 2011	12,00,000
Weighted average number of equity shares outstanding during 2011	5,00,000 shares

Average fair value of one equity share during 2011	20.00
Weighted average number of shares **under option** during 2011	1,00,000 shares
Exercise price for shares **under option** during 2011	15.00

	Earnings	**Shares**	**Earnings per share**
Net profit for the year 20X1	12,00,000		
Weighted average number of shares outstanding during year 20X1		5,00,000	
BASIC EPS			2.40
Number of shares under option		1,00,000	
Number of shares that would have been issued at fair value: (100,000 x 15.00)/20.00		(75,000)	
DILUTED EPS	12,00,000	5,25,000	2.29

75,000 Shares – Issued **at FV** i.e. 75000 x **20** – hence **NOT** Dilutive

1,00,000 Shares

25,000 Shares – Issued at **Less than** [or **without**] Consideration – Hence Dilutive

<u>Dilutive Potential Equity Shares</u>

- Dilutive **when & only when**, their conversion to equity shares would decrease net profit per share from continuing **ordinary operations**.
- <u>Net profit per share from continuing **ordinary operations**.</u>

  Net Profit from Ordinary Activity [As per AS 5] xx

  (-) Preference Dividend [Incl. Tax] (xx)

  (-) Items Relating to discontinued Operations [AS 24] (xx)
- **Anti-dilutive** when their conversion to equity shares would **increase EPS** or **decrease loss** per share. Effects of anti-dilutive potential equity shares are **ignored in calculating diluted EPS.**
- In order to **maximise dilution of basic** EPS, each series of potential equity shares is considered in **sequence** from the **most dilutive to least dilutive**.
- For determining the sequence = Earnings per incremental potential equity share is calculated.
- Where earnings per incremental share is the least, Potential equity share is considered most dilutive.

Earnings, i.e., Net profit attributable to equity shareholders	1,00,00,000
No. of equity shares outstanding	20,00,000
Average fair value of one equity share during the year	75.00
Potential Equity Shares	
Options	1,00,000 with exercise price of 60
Convertible Preference Shares Attributable tax, e.g., corporate dividend tax	8,00,000 shares entitled to a cumulative dividend of 8 per share. Each preference share is convertible into 2 equity shares. 10%
12% Convertible Debentures of 100 each	Nominal amount 10,00,00,000. Each debenture is convertible into 4 equity shares.
Tax rate	30%

Increase in Earnings Attributable to Equity Shareholders on Conversion of Potential Equity Shares

	Increase in Earnings	Increase in no. of Equity Shares	Earnings per Incremental Share
Options			
Increase in earnings	Nil		
No. of incremental shares issued for no consideration {1,00,000 x (75 - 60) / 75}		20,000	Nil
Convertible Preference Shares			
Increase in net profit attributable to equity shareholders as adjusted by tax [(Rs.8 x 8,00,000)+ 10% (8 x 8,00,000)]	70,40,000		
No. of incremental shares {2 x 8,00,000}		16,00,000	4.40
12% Convertible Debentures			
Increase in net profit {Rs.10,00,00,000 x 0.12 x (1-0.30)}	84,00,000		
No. of incremental shares {10,00,000 x 4}		40,00,000	2.10

Options are most dilutive as their earnings per incremental share is nil. Options will be considered first. 12% convertible debentures being second and convertible preference shares will be third.

Conversion of Diluted Earnings Per Shares

	Net Profit Attributable	No. of Equity Shares	Net profit attributable Per Share	
As reported	1,00,00,000	20,00,000	5.00	
Options	________	20,000		
	1,00,00,000	20,20,000	4.95	Dilutive
12% Convertible Debentures	84,00,000	40,00,000		
	1,84,00,000	60,20,000	3.06	Dilutive
Convertible Preference Shares	70,40,000	16,00,000		
	2,54,40,000	76,20,000	3.34	Anti- Dilutive

Diluted EPS increased when taking convertible preference shares (from 3.06 to 3.34) - Convertible preference shares are anti-dilutive and are ignored in calculating diluted EPS. Therefore, Diluted EPS is 3.06.

- Potential equity shares that **cancelled or allowed to lapse** during the **reporting** period - included in computing diluted EPS **only** for the portion of the period during which they were **outstanding**.
- Potential equity shares that converted into equity shares during the reporting period - included in the calculating diluted EPS from the beginning of the period to the date of conversion;
- From the date of conversion, Resulting equity shares are included in computing both basic and diluted EPS.

RESTATEMENT

[Para 44] If No. of equity/ potential equity shares outstanding **increases** **or** **decreases**

Due to

1. Bonus Issue
2. Share Split

Due to "Reverse Share Split" (Consolidation of Shares)

- Calculation of basic and diluted EPS should be **adjusted** for **all the periods presented**.
- If changes occur after balance sheet date but before date when financial statements are approved by BOD - per share calculations **adjusted** for **all the periods presented**.

- Enterprise is **encouraged** to provide description of equity share transactions or potential equity share transactions, **OTHER THAN** → 1. Bonus Issue

  2. Share Split & Reverse Share Split

  Which **occur after the balance sheet date.** Examples of such transactions include :

  (a) Issue for cash;

  (b) Issue to use proceeds to repay debt or preference shares outstanding at the balance sheet date;

  (c) Cancellation of equity shares outstanding at the balance sheet date;

  (d) Conversion of potential equity shares, outstanding at the balance sheet date;

  (e) Issue of warrants, options or convertible securities; and

  (f) Satisfaction of conditions that result in issue of contingently issuable shares.

↑

EPS **not** adjusted for such transactions **occurring after balance sheet date** because such transactions <u>do not affect the amount of capital used to produce the net profit or loss for the period</u>.

↓

Only Transaction Mentioned in Para 44 will be Adjusted