

CUET · ACCOUNTANCY · CLASS XII · CODE 301

Financial Statements of a Company

CUET unit: Analysis of Financial Statements → Financial
Statements

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Snapshot

- Establishes the legal-format presentation of a company's annual accounts under **Schedule III of the Companies Act, 2013** — both the Balance Sheet (Part I) and the Statement of Profit & Loss (Part II).
- Defines what financial statements ARE (recorded facts, conventions, postulates, personal judgements) and what they DO (assist users in decision-making).
- Heavy CUET focus on **classification of items under correct major head and sub-head** — e.g. Securities Premium → Reserves & Surplus; Calls-in-arrears → deducted from Subscribed Capital; Loose Tools → Inventories; Preliminary Expenses → written off, residual under Other Current/Non-current Assets.
- Drills the **current vs non-current bifurcation** (12-month / operating-cycle rule) which governs every line on the Balance Sheet.
- Distinguishes broad heads on the face of the P&L — Revenue from operations, Other income, the five expense buckets, Profit before tax, Tax, Profit/(Loss) for the period.

Detailed Notes

2.1 Core concepts

- **Financial statements** are the basic and formal annual reports through which corporate management communicates financial information to owners and external parties; they refer to the **balance sheet** (position statement), the **statement of profit and loss**, and the **cash flow statement** (NCERT §3.1, p. 144).
- The **nature** of financial statements rests on four pillars: (1) Recorded Facts (historical cost basis), (2) Accounting Conventions (cost-or-market-lower, materiality, conservatism), (3) Postulates (going concern, money measurement, realisation), and (4) Personal Judgements (depreciation life, doubtful-debt provision, inventory valuation) (NCERT §3.2, pp. 145–146).
- **Objectives** of financial statements: provide information about (i) economic resources and obligations, (ii) earning capacity, (iii) cash flows, (iv) effectiveness of management, (v) activities affecting society, and (vi) accounting policies followed (NCERT §3.3, pp. 146–147).

- **Types:** balance sheet + statement of profit and loss are mandatory for every company under the Companies Act 2013; cash flow statement is additionally prepared to show movement of funds (NCERT §3.4, p. 147).
- Every Indian company must prepare its accounts in the form prescribed by **revised Schedule III** of the Companies Act, 2013, EXCEPT insurance/banking companies and companies for which a separate form is prescribed under any other Act (NCERT §3.4 Important Features, p. 148).
- **Balance Sheet — Equity & Liabilities** side has four heads: (1) Shareholders' Funds [Share Capital; Reserves & Surplus; Money received against share warrants], (2) Share Application money pending allotment, (3) Non-current Liabilities [Long-term borrowings; Deferred tax liabilities (net); Other long-term liabilities; Long-term provisions], (4) Current Liabilities [Short-term borrowings; Trade payables; Other current liabilities; Short-term provisions] (NCERT Exhibit 3.1, pp. 147–148).
- **Balance Sheet — Assets** side has two heads: (1) Non-Current Assets [Fixed assets — Tangible / Intangible / Capital WIP / Intangible under development; Non-current investments; Deferred tax assets (net); Long-term loans & advances; Other non-current assets], (2) Current Assets [Current investments; Inventories; Trade receivables; Cash & cash equivalents; Short-term loans & advances; Other current assets] (NCERT Exhibit 3.1, p. 148).
- **Schedule III rules:** accounting standards prevail over Schedule III; vertical format is mandatory; rounding-off is mandatory based on turnover (<₹100 cr → nearest hundreds/thousands/lakhs/millions; >₹100 cr → nearest lakhs or millions); debit balance of statement of profit & loss is shown as a NEGATIVE figure under "Surplus"; "Sundry Debtors/Creditors" are now "Trade Receivables/Payables" (NCERT §3.4 Important Features, pp. 148–149).
- **Reserves and Surplus** is sub-classified into: Capital Reserve, Capital Redemption Reserve, Securities Premium Reserve, Debenture Redemption Reserve, Revaluation Reserve, Share Options Outstanding Account, Other Reserves, and Surplus (balance in statement of profit and loss) (NCERT §3.4 Reserve and Surplus, p. 151).
- A reserve specifically represented by earmarked investments is termed a "**Fund**"; balance of Reserves & Surplus is reported even if negative after adjusting debit balance of P&L (NCERT §3.4 Reserve and Surplus, p. 151).
- **Share Capital disclosure** in Notes to Accounts includes Authorised, Issued, Subscribed-and-fully-paid-up, Subscribed-but-not-fully-paid-up; **Calls-in-arrears are deducted** from subscribed-but-not-fully-paid-up capital, and **Share Forfeiture A/c (amount originally paid up)** is added back (NCERT Illustration 1, pp. 150, 152).
- **Current vs Non-current classification:** an item is CURRENT if it is involved in the entity's operating cycle, OR expected to be realised/settled within 12 months, OR held primarily for trading, OR is cash/cash equivalent, OR if the entity does not have an unconditional right to defer settlement of a liability for at least 12 months after

the reporting period; all other items are non-current (NCERT §3.4 Current/Non-current distinction, p. 153).

- **Special classification rules:** Deferred tax assets/liabilities are ALWAYS non-current; All inventories are ALWAYS current; Fixed assets (both tangible and intangible) are ALWAYS non-current — even if useful life is less than 12 months; Cash and cash equivalents are ALWAYS current; Investments are split into current and non-current based on the 12-month rule (NCERT §3.4, pp. 155–156).
- **Borrowings** are split: long-term (repayable beyond 12 months / operating cycle) under Non-current Liabilities; short-term (on demand or original tenure ≤ 12 months) under Current Liabilities; **current maturities of long-term debt** are shown under "Other current liabilities" with a Note (NCERT §3.4 Borrowings, pp. 154–155).
- **Proposed Dividend** is shown in Notes to Accounts as a **contingent liability** (per AS-4) until approved by shareholders in AGM — proposed dividend of previous year becomes a current-year liability after declaration (NCERT §3.4 Proposed Dividend, p. 155).
- **Preliminary Expenses** must be written off completely in the year incurred — first from Securities Premium, then from Statement of P&L; **discount on issue of debentures** is also written off in the same year (NCERT §3.4 Important points after Illustration 2, p. 154).
- **Statement of Profit and Loss (Schedule III Part II)** lists: I. Revenue from operations, II. Other income, III. Total Revenue (I+II), IV. Expenses [Cost of materials consumed; Purchases of stock-in-trade; Changes in inventories of finished goods, WIP and stock-in-trade; Employee benefits expense; Finance costs; Depreciation and amortisation expense; Other expenses], V. Profit before exceptional items and tax (III–IV), VI. Exceptional items, VII. Profit before extraordinary items and tax (V–VI), VIII. Extraordinary items, IX. Profit before tax (VII–VIII), X. Tax expense, XI. Profit/(Loss) from continuing operations (IX–X), XII–XIV. Discontinuing operations, XV. Profit/(Loss) for the period, XVI. EPS (Basic + Diluted) (NCERT Exhibit 3.2, pp. 161–162).
- **Revenue from operations** = sale of products + sale of services + other operating revenues (for a finance company it includes interest, dividend and income from other financial services) (NCERT §3.4.2 item 1, p. 162).
- **Other income** = interest income (for non-finance companies), dividend income, net gain/loss on sale of investments, other non-operating income (NCERT §3.4.2 item 2, p. 162).
- **Expense heads** are five buckets: Cost of materials consumed (manufacturing), Purchase of stock-in-trade (trading), Changes in inventories (opening – closing of FG/WIP/stock-in-trade), Employee benefits (salaries, wages, leave encashment, staff welfare), Finance costs (interest only — bank charges go under Other Expenses), Depreciation & Amortisation (depreciation = fixed assets, amortisation = intangibles), Other Expenses (residual) (NCERT §3.4.2 item 3, pp. 162–163).

- **Uses of financial statements:** stewardship report, basis for fiscal policy, basis for credit decisions, guidance for prospective investors, guide on value of existing investment, aid to trade associations, aid to stock exchanges (NCERT §3.5, pp. 164–165).
- **Limitations:** do not reflect current market situation (historical cost basis), assets may not realise stated values on forced liquidation, bias from personal judgement, aggregate information only, vital qualitative information missing, only interim reports for a point in time (NCERT §3.6, pp. 165–166).

2.2 Definitions to memorise

Term	Definition	Page
Financial Statements	Basic and formal annual reports through which corporate management communicates financial information to owners and external parties — includes balance sheet, statement of profit and loss, and cash flow statement.	144
Going Concern Postulate	Assumption that the enterprise will continue to exist for a long period of time, so assets are shown on historical cost basis.	145
Money Measurement Postulate	Assumption that the value of money will remain the same in different periods, so assets purchased at different times are shown at the amount paid.	145
Realisation Postulate	Revenue is included in the sales of the year in which the sale was undertaken even though the sale price may be received over several years.	146
Trade Payables	New Schedule III term replacing "Sundry Creditors" — current liability for purchase of goods/services in the normal course of business.	149, 155
Trade Receivables	New Schedule III term replacing "Sundry Debtors" — amounts realisable within 12 months from sale of goods or services rendered in the normal course of business.	149, 156
Current Asset	An item involved in the operating cycle, expected to be realised within 12 months, held primarily for trading, or cash and cash equivalents.	153
Current Liability	A liability expected to be settled within 12 months or where the entity has no unconditional right to defer settlement for at least 12 months.	153
Fund (in Reserves & Surplus)	A reserve specifically represented by earmarked investments.	151
Revenue from Operations	Sale of products + sale of services + other operating revenues; for a finance company also includes interest, dividend and income from other financial services.	162
Finance Costs		163

Term	Definition	Page
	Interest charges on borrowings during the year (other financial expenses like bank charges go under Other Expenses).	
Depreciation	The diminution in the value of fixed assets (writing off intangibles is called amortisation).	163
Proposed Dividend	Dividend proposed by Board of Directors but pending approval at AGM — shown in Notes to Accounts as contingent liability (AS-4).	155

2.3 Diagrams / processes to remember

- **Exhibit 3.1 — Form of Balance Sheet (Schedule III Part I)**, pp. 147–148: vertical format with I. Equity & Liabilities (Shareholders' funds → Share application money pending allotment → Non-current liabilities → Current liabilities) and II. Assets (Non-current → Current); two amount columns (current period and previous period).
- **Exhibit 3.2 — Form of Statement of Profit and Loss (Schedule III Part II)**, pp. 161–162: vertical format with Items I to XVI ending in EPS (Basic and Diluted).
- **Box 1 — Rounding-off rule based on turnover**, p. 149: turnover < ₹100 cr → nearest hundreds/thousands/lakhs/millions; turnover > ₹100 cr → nearest lakhs or millions.
- **Illustration 1 — Share Capital presentation with calls-in-arrears and forfeiture**, p. 152: subscribed-but-not-fully-paid capital is shown net of calls-in-arrears, then forfeited share account (amount originally paid up on forfeited shares) is added.

2.4 Common confusions / NTA trap points

- **Loose Tools** → classified under **Inventories** (current asset), NOT under Tangible Fixed Assets (NCERT Illustration 6, p. 160).
- **Securities Premium Reserve** is part of **Reserves & Surplus**, NOT a part of Share Capital (NCERT §3.4 Reserve and Surplus, p. 151).
- **Preliminary Expenses** must be **fully written off** in the year incurred — first against Securities Premium, then against Statement of P&L; they do NOT linger as a fictitious asset on the balance sheet (NCERT Important points, p. 154).
- **Calls-in-arrears** are DEDUCTED from Subscribed-but-not-fully-paid-up capital; **Calls-in-advance** are a current liability under "Other current liabilities" — students confuse the two (NCERT Illustration 1, p. 152).
- **Deferred tax assets/liabilities are ALWAYS non-current** under Schedule III — even though they may settle in less than 12 months in substance (NCERT §3.4, p. 155).
- **Inventories are ALWAYS current**, and **Fixed Assets are ALWAYS non-current** regardless of useful life — Schedule III overrides general logic (NCERT §3.4 Fixed assets / Inventories, pp. 156).

- **Proposed Dividend** is a contingent liability in Notes to Accounts (per AS-4) — students mistakenly place it under Short-term Provisions on the face of the balance sheet (NCERT §3.4 Proposed Dividend, p. 155).
- **Bank charges** go under **Other Expenses**, NOT Finance Costs — Finance Costs is ONLY interest on borrowings (NCERT §3.4.2 item 3(e), p. 163).
- **Trade Receivables vs Trade Payables.** New Schedule III names — replacing Sundry Debtors and Sundry Creditors (NCERT p. 149).
- **Reserve vs Fund.** A reserve specifically represented by earmarked investments is termed a "Fund" (NCERT §3.4 Reserve and Surplus, p. 151).
- **Schedule III prevails on format, AS prevails on substance.** Where there is a conflict, the Accounting Standards override Schedule III (NCERT §3.4 Important Features, p. 148).
- **Rounding-off mandatory.** Based on turnover: <₹100 cr → nearest hundreds/thousands/lakhs/millions; >₹100 cr → nearest lakhs or millions (NCERT p. 149).

2.5 Journal entry templates

Although Schedule III is a presentation standard rather than a journal-entry chapter, the following entries are the journal counterparts to the Balance Sheet and P&L line items most often tested.

(a) Transfer of profit to General Reserve (NCERT § 3.4 Reserve and Surplus, p. 151)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Mar 31	Statement of Profit and LossDr.		1,00,000	
	To General Reserve A/c			1,00,000
	(Being amount transferred to General Reserve — shown under Reserves and Surplus)			

(b) Securities premium received on share issue (NCERT § 3.4 Reserve and Surplus, p. 151)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Apr 1	Bank A/cDr.		12,00,000	
	To Share Capital A/c			10,00,000
	To Securities Premium Reserve A/c			2,00,000
	(Being shares issued at premium; premium goes to Reserves and Surplus, not Share Capital)			

(c) Forfeiture amount on partly-paid shares treatment (NCERT Illus. 1, p. 152)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Jul 1	Share Capital A/cDr.		30,000	
	To Calls-in-Arrears A/c			6,000
	To Share Forfeiture A/c			24,000
	(Being 300 shares of ₹100 each forfeited; calls-in-arrears ₹20 per share unpaid)			

(d) Provision for tax (NCERT § 3.4.2 item 4, p. 163)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Mar 31	Statement of Profit and LossDr.		50,000	
	To Provision for Tax A/c			50,000
	(Being provision for current tax; shown under Short-term Provisions)			

(e) Interest on debentures (Finance Cost) (NCERT § 3.4.2 item 3(e), p. 163)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Mar 31	Finance Cost A/cDr.		10,000	
	To Debentureholders A/c			10,000
	(Being 10% interest on debentures of ₹1,00,000 — shown as Finance Cost in P&L)			

(f) Writing off preliminary expenses fully (NCERT § 3.4 Important Points, p. 154)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Mar 31	Securities Premium Reserve A/cDr.		30,000	
	Statement of Profit and LossDr.		20,000	
	To Preliminary Expenses A/c			50,000
	(Being preliminary expenses fully written off in year of incurrance — first from Securities Premium, then from P&L)			

(g) Recording proposed dividend disclosure (AS-4 — NCERT § 3.4, p. 155)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Mar 31	(Proposed dividend shown in Notes to Accounts as contingent liability per AS-4; no journal entry until AGM approval)			
(After AGM)	Statement of Profit and LossDr.		1,00,000	
	To Dividend Payable A/c			1,00,000
	(Being dividend declared at AGM — now a current liability)			

(h) Closing inventory of loose tools (NCERT Illus. 6, p. 161)

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
Mar 31	Inventories — Loose Tools A/cDr.		1,52,000	
	To Trading A/c			1,52,000
	(Being loose tools brought into closing inventory — classified as current asset under Inventories, not as fixed asset)			

Practice MCQs

Q1. Under Schedule III Part I of the Companies Act, 2013, "Securities Premium Reserve" is classified under which major head and sub-head of the balance sheet?

- A. Shareholders' Funds → Share Capital
- B. Shareholders' Funds → Reserves and Surplus
- C. Non-current Liabilities → Other long-term liabilities
- D. Current Liabilities → Other current liabilities

Q2. While preparing the balance sheet of a company, where will "Loose Tools" appear?

- A. Non-current Assets → Fixed Assets → Tangible Assets
- B. Non-current Assets → Other non-current assets
- C. Current Assets → Inventories
- D. Current Assets → Other current assets

Q3. A company has Subscribed but not fully paid-up capital of 300 equity shares of ₹100 each fully called up. Calls-in-arrears amount to ₹6,000 (300 × ₹20). In the Notes to Accounts, how is this presented?

- A. Subscribed capital is shown gross at ₹30,000 and calls-in-arrears are shown separately as a current asset
- B. Subscribed capital is shown at ₹30,000 LESS Calls-in-arrears ₹6,000 = ₹24,000
- C. Subscribed capital is shown at ₹24,000 directly without disclosing calls-in-arrears
- D. Calls-in-arrears of ₹6,000 are added to Reserves and Surplus

 **5 more MCQs + answer key**

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PYQ Alignment

This chapter is one of the highest-yielding chapters for CUET (UG) Accountancy under the "Analysis of Financial Statements" unit — typically 6–9 MCQs per year, with NTA favouring (a) classify-this-item questions mapping balance-sheet items to their Schedule III major head and sub-head, (b) statement-based questions on the current vs non-current rule and special classification exceptions (deferred tax, inventories, fixed assets), and (c) short numerical questions requiring computation of Profit before tax from given P&L data per Schedule III Part II.

CUET 2025 — Actual PYQs from this chapter

Q.37 (CUET 2025) Match List-I with List-II: (A) Reserves and Surplus → (I) Share options outstanding account; (B) Non-current liabilities → (II) Long-term provisions; (C) Current liabilities → (III) Short-term borrowing; (D) Shareholders' funds → (IV) Calls in arrears.

- A) A-I, B-II, C-III, D-IV B) A-III, B-II, C-I, D-IV C) A-II, B-III, C-IV, D-I D) A-IV, B-III, C-II, D-I

Tests: §2 Schedule III Part I — major heads and sub-heads of Equity & Liabilities.

Answer: Not in extracted key

CUET 2023 — Actual PYQs from this chapter

Q.17 (CUET 2023) Security Premium in Balance Sheet appears under:

- A) Reserve and Surplus B) Share Capital C) Equity Share Capital D) Shares and Liabilities Tests: §2 Schedule III classification — Securities Premium as a Reserves and Surplus sub-head. Answer: Not in extracted key

Q.18 (CUET 2023) An annual report is furnished by a company to its:

- A) Directors B) Auditors C) Shareholders D) Management Tests: §1 Nature and uses of Financial Statements — primary users of the Annual Report. Answer: Not in extracted key

Q.34 (CUET 2023) Current liabilities include: (A) Trade receivables (B) Unclaimed dividend (C) Interest accrued but not due on loan (D) Acceptances (E) 12% debentures redeemable after four years

- A) (A),(B),(C) only B) (B),(C),(D) only C) (A),(C),(D) only D) (A),(B),(D) only Tests: §2 Schedule III — twelve-month operating cycle test for current vs non-current liabilities.

Answer: Not in extracted key