

11

AS 4 - Contingencies & Events Occurring After the Balance Sheet Date

Introduction

All paragraphs of AS 4 (Revised) that deal with contingencies are applicable only to the extent not covered by other Accounting Standards. For example, the impairment of financial assets such as impairment of receivables (commonly known as provision for bad and doubtful debts) is governed by this Standard. Thus, the present standard (AS 4 (Revised)) deals with the treatment and disclosure requirements in the financial statements of events occurring after the balance sheet.

Contingencies

Contingency is a condition or situation, the ultimate outcome of which, gain or loss, will be known or determined only on the occurrence, or non-occurrence, of one or more uncertain future events.

Events Occurring after the Balance Sheet Date

Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, 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 any other entity.

For example, for the year ending on 31st March 2020, financial statement is finalised and approved by the Board of the directors of the company in its meeting held on 04th September 2020. In this case the events taking place between 01st April 2020 to 04th September 2020 are termed as events occurring after the balance sheet date.

Two types of events can be identified:

- a. Adjusting events- those which provide further evidence of conditions that existed at the balance sheet date. For example a trade receivable declared insolvent and estate unable to pay full amount against whom provision for doubtful debt was created.
- b. Non-adjusting events- those which are indicative of conditions that arose subsequent to the balance sheet date.

Adjusting Events

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. For example, an adjustment may be made for a loss on a trade receivable account which is confirmed by the insolvency of a customer which occurs after the balance sheet date.

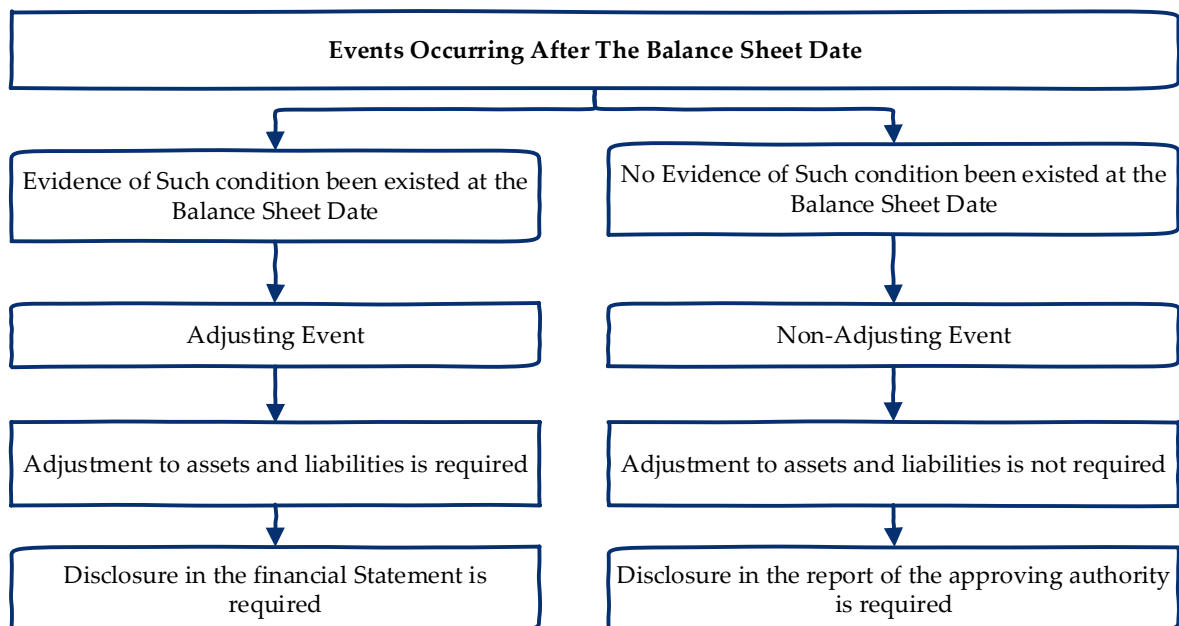
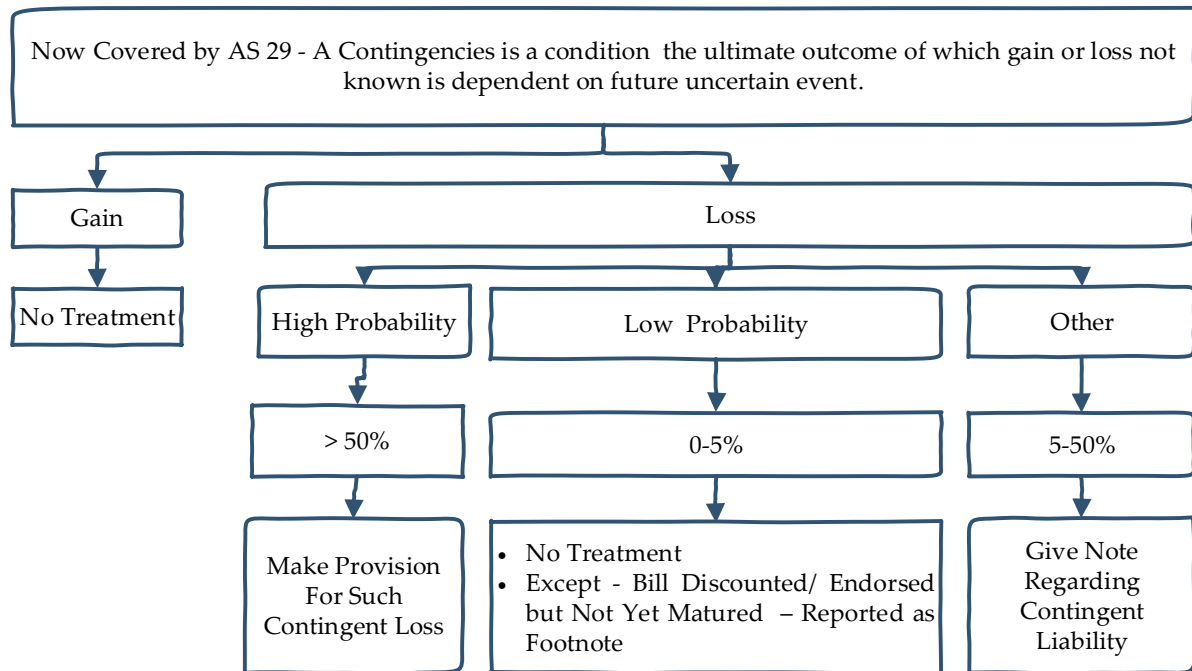
Non-Adjusting Events

Adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. An example is the decline in market value of investments between the balance sheet date and the date on which the financial statements are approved. Ordinary fluctuations in market values do not normally relate to the condition of the investments at the balance sheet date, but reflect circumstances which have occurred in the following period.

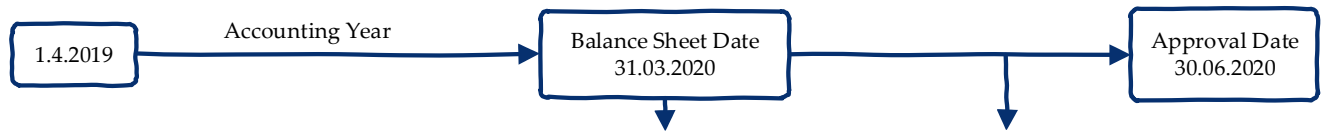
Events occurring after the balance sheet date which do not affect the figures stated in the financial statements would not normally require disclosure in the financial statements although they may be of such significance that they may require a disclosure in the report of the approving authority to enable users of financial statements to make proper evaluations and decisions.

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.

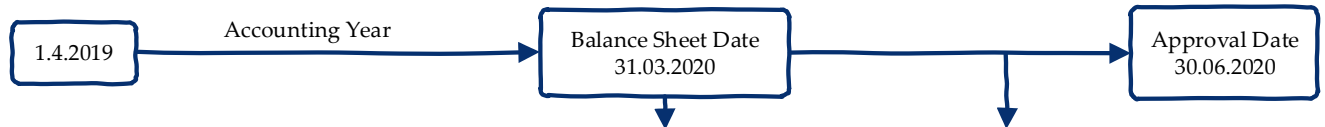
- a) Events occurring after the balance sheet date may indicate that the enterprise ceases to be a going concern. It means any event occur after the balance sheet date whose evidence of conditions was not existing on Balance Sheet Date (example Loss by Fire) but going concern assumption is affected. In case the going concern assumption is not valid (based on events occurring after the balance sheet date), the financial statements are prepared on a liquidation basis.
- b) If dividends are declared after the balance sheet date but before the financial statements are approved for issue, the dividends are not recognised as a liability at the balance sheet date because no obligation exists at that time unless a statute requires otherwise. Such dividends are disclosed in the notes. Thus, no liability for proposed dividends needs to be recognised for financial statements for year ended 2016-17 and subsequent years. Such proposed dividends are to be disclosed in the notes as per Companies (Accounting Standards) Amendment Rules, 2016.



Case 1:



Case 2:



Case 3:



Case 4:



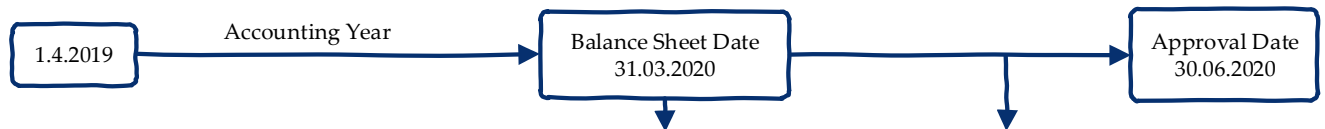
Case 5:



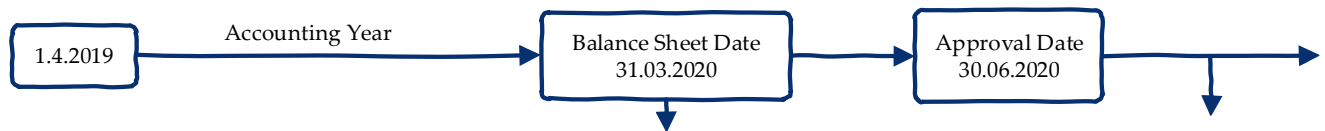
Case 6:



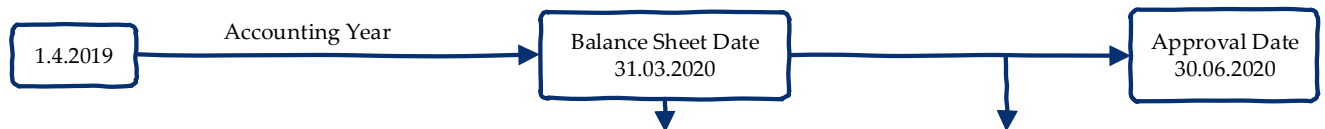
Case 7:



Case 8:



Case 9:



Case 10:



Disclosure

Disclosure of events occurring after the balance sheet date requires the following information should be provided -

1. The **nature** of the event;
2. An **estimate** of the financial effect, or a **statement** that such an estimate cannot be made.

QUESTIONS

1. [Nov. 2011, Similar in Nov. 2005, Nov. 2010 & May 2014] MEC Limited could not recover an amount of ₹ 8 lakhs from a debtor. The company is aware that the debtor is in great financial difficulty. The accounts of the company for the year ended 31-3-2011 were finalized by making a provision @ 25% of the amount due from that debtor. In May 2011, the debtor became bankrupt and nothing is recoverable from him. Do you advise the company to provide for the entire loss of ₹ 8 lakhs in books of account for the year ended 31-3-2011?

Answer:

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 if such event provides/relates to additional information to the conditions existing at the balance sheet date and is also materially affecting the valuation of assets and liabilities on the balance sheet date. As per the information given in the question, the company was aware that the debtor was already in a great financial difficulty at the time of closing of accounts. Bankruptcy of the debtor in May 2011 is only an additional information to the condition existing on the balance sheet date. Also the effect of a debtor becoming bankrupt is material as total amount of ₹ 8 lakhs will be a loss to the company. Therefore, the company is advised to provide for the entire amount of ₹ 8 lakhs in the books of account for the year ended 31st March, 2011.

2. [May 2014] In its Final Accounts for the year ended 31st March, 2014, Z Ltd. made a provision of 3% of its total debtor. On 10th March, 2014, a debtor of ₹ 5 lakhs suffered a heavy loss and became insolvent in April 2014. The loss was not insured.

State giving reasons, if the company may provide for the full loss in its accounts for the year ended 31st March, 2014.

Answer:

According to Accounting Standard 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, though the debtor became insolvent after balance sheet date, yet he had suffered heavy loss (not covered by the insurance), before the balance sheet date and this loss was the cause of the insolvency of the debtor.

Therefore the company must make full provision for bad debts amounting ₹ 5 lakhs in its final accounts for the year ended 31st March, 2014.

3. [May 2003] You are an accountant preparing accounts of A Ltd. as on 31.3.2011. After year end the following events have taken place in April, 2011:
- a. A fire broke out in the premises damaging, uninsured stock worth ₹ 10 lakhs (Salvage value ₹ 2 lakhs).
 - b. A suit against the company's advertisement was filed by a party claiming damage of ₹ 20 lakhs.

c. Dividend proposed @ 20% on share capital of ₹ 100 lakhs.

Describe, how above will be dealt with in the accounts of the company for the year ended on 31.3.2011.

Answer:

- a. Events occurring after the Balance Sheet date that represent material changes and commitments affecting the financial position of the enterprise, not relating to conditions existing on balance sheet date, is a non adjusting event only disclosure is required. Hence, fire accident and loss thereof must be disclosed in approving authorities report.
 - b. 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 AS 4 (now covered by AS-29).
 - c. As per revised AS-4, If an enterprise declares dividends after the balance sheet date, the enterprise should not recognised those dividends as a liability at the balance sheet date unless a statute requires otherwise. Such dividends should be disclosed in notes.
4. During the year 2015-2016, Raj Ltd. was sued by a competitor for ₹ 15 lakhs for infringement of a trademark. Based on the advice of the company's legal counsel, Raj Ltd. provided for a sum of ₹ 10 lakhs in its financial statements for the year ended 31st March, 2016. On 18th May, 2016, the Court decided in favour of the party alleging infringement of the trademark and ordered Raj Ltd. to pay the aggrieved party a sum of ₹ 14 lakhs. The financial statements were prepared by the company's management on 30th April, 2016, and approved by the board on 30th May, 2016.

Answer:

As per AS 4 (Revised), 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, since Raj Ltd. was sued by a competitor for infringement of a trademark during the year 2015-16 for which the provision was also made by it, the decision of the Court on 18th May, 2016, for payment of the penalty will constitute as an adjusting event because it is an event occurred before approval of the financial statements. Therefore, Raj Ltd. should adjust the provision upward by ₹ 4 lakhs to reflect the award decreed by the Court to be paid by them to its competitor.

5. **[June 2009]** A major fire has damaged the assets in a factory of a Limited Company on 5th April – five days after the year end and closure of accounts. The loss is estimated at ₹ 10 crores out of which ₹ 7 crores will be recoverable from the insurers. Explain briefly how the loss should be treated in the final accounts for the previous year.

Answer:

The loss due to break out of fire is an example of event occurring after the balance sheet date. The event being in the nature of a fire which is unpredictable does not relate to conditions existing at the balance sheet date. It has not affected the financial position as on the date of balance sheet and therefore requires no specific adjustments in the financial statements. However, AS 4 states that disclosure is generally made of events occurring after balance sheet date i.e. in subsequent periods

that represent unusual changes affecting the existence or substratum of the enterprise after the balance sheet date. In the given case, the amount of loss of assets in a factory is material and may be considered as an event affecting the substratum of the enterprise. Hence, as recommended in AS 4, disclosure of the event should be made.

6. **[May 2005]** A major fire has damaged assets in a factory of X Co. Ltd. on 8.4.2004, 8 days after the year end closing of accounts. The loss is estimated to be ₹ 16 crores (after estimating the recoverable amount of ₹ 24 crores from the Insurance Company).

If the company had no insurance cover, the loss due to fire would be ₹ 40 crores. Explain, how the loss should be treated in the Final accounts of the year ended 31.3.2004

Answer:

The present event does not relate to conditions existing at the balance sheet date. Hence, no specific adjustment is required in the financial statements for the year ending on 31.3.2004. But if the event occurring after balance sheet date gives an indication that the enterprise may cease to be a going concern, then the assets and liabilities are required to be adjusted for the financial year ended 31st March, 2004. AS 4 (Revised) requires disclosure in respect of events occurring after the balance sheet date representing unusual changes affecting the existence or substratum of the enterprise after the date of the Balance Sheet. In the present event, the loss of assets in a factory can be considered to be an event affecting the substratum of the enterprise. Hence, an appropriate disclosure should be made in the report of the approving authority.

7. **[Similar Nov. 2006, Nov 2009 & Nov 2013]** A Company entered into an agreement to sell its immovable property to another company for ₹ 35 lakhs. The property was shown in the Balance Sheet at ₹ 7 lakhs. The agreement to sell was concluded on 15th February, 2011 and sale deed was registered on 30th April, 2011.

You are required to state, with reasons, how this event would be dealt with in the financial statements for the year ended 31st March, 2011.

Answer:

According AS 4 "Contingencies and Events Occurring after the Balance Sheet Date", assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date. In the given case, sale of immovable property was carried out before the closure of the books of accounts. This is clearly an event occurring after the balance sheet date but agreement to sell was effected on 15th February 2011 i.e. before the balance sheet date. Registration of the sale deed on 30th April, 2011, simply provides additional information relating to the conditions existing at the balance sheet date. Therefore, adjustment to assets for sale of immovable property is necessary in the financial statements for the year ended 31st March, 2011.

8. In Raj Co. Ltd., theft of cash of ₹ 2 lakhs by the cashier in January, 2011 was detected in May, 2011. The accounts of the company were not yet approved by the Board of Directors of the company. Whether the theft of cash has to be adjusted in the accounts of the company for the year ended 31.3.2011. Decide.

Answer:

As per AS 4 (revised), 'Contingencies and Events Occurring After the Balance Sheet Date', assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date.

Though the theft, by the cashier ₹ 2,00,000, was detected after the balance sheet date (before approval of financial statements) but it is an additional information materially affecting the determination of the cash amount relating to conditions existing at the balance sheet date. Therefore, it is necessary to make the necessary adjustments in the financial statements of the company for the year ended 31st March, 2011 for recognition of the loss amounting ₹ 2,00,000.

9. **[May 2010]** A Company follows April to March as its financial year. The Company recognizes cheques dated 31st March or before, received from customers after balance sheet date, but before approval of financial statement by debiting 'Cheques in hand account' and crediting 'Debtors account'. The 'cheques in hand' is shown in the Balance Sheet as an item of cash and cash equivalents. All cheques in hand are presented to bank in the month of April and are also realised in the same month in normal course after deposit in the bank. State with reasons, whether the collection of cheques bearing date 31st March or before, but received after Balance Sheet date is an adjusting event and how this fact is to be disclosed by the company?

Answer:

Even if cheques bear the date 31st March or before, the cheques received after 31st March do not represent any condition existing on the balance sheet date i.e 31st March. Thus, the collection of cheques after balance sheet date is not an adjusting event. Cheques that are received after the balance sheet date should be accounted for in the period in which they are received even though the same may be dated 31st March or before as per AS 4 "Contingencies and Events Occurring after the Balance Sheet Date". Moreover, the collection of cheques after balance sheet date does not represent any material change affecting financial position of the enterprise on the balance sheet date, so no disclosure is necessary.

10. **[May 2011]** In preparing the financial statements of Lotus Limited for the year ended 31st March, 2010 you come across the following information. State with reason, how you would deal with this in the financial statements? The company invested ₹ 50 lakhs in April, 2010 in the acquisition of another company doing similar business, the negotiations for which had just started.

Answer:

As per AS 4 "Contingencies and Events Occurring after the Balance Sheet Date", events occurring after the balance sheet date which do not affect the figures stated in the financial statements would not normally require disclosure in the financial statements although they may be of such significance that they may require a disclosure in the report of the approving authority to enable users of financial statements to make proper evaluations and decisions.

The investment of ₹ 50 lakhs in April 2010 for acquisition of another company is under negotiation stage, and has not been finalized yet. On the other hand it is also not affecting the figures stated in the financial statements of 2009-10, hence the details regarding such negotiation and investment

planning of ₹ 50 lakhs in April, 2010 in the acquisition of another company should be disclosed in the Directors' Report to enable users of financial statements to make proper evaluations and decision.

11. **[May 2012]** Cashier of A-One Limited embezzled cash amounting to ₹ 6,00,000 during March, 2012. However same comes to the notice of Company management during April, 2012 only. Financial statements of the company is not yet approved by the Board of Directors of the company. With the help of provisions of AS 4 "Contingencies and Events Occurring after the Balance Sheet Date" decide, whether the embezzlement of cash should be adjusted in the books of accounts for the year ending March, 2012?

What will be your reply, if embezzlement of cash comes to the notice of company management only after approval of financial statements by the Board of Directors of the company ?

Answer:

As per AS 4, assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date.

Though the theft, by the cashier ₹ 6,00,000, was detected after the balance sheet date (before approval of financial statements) but it is an additional information materially affecting the determination of the cash amount relating to conditions existing at the balance sheet date. Therefore, it is necessary to make the necessary adjustments in the financial statements of the company for the year ended 31st March, 2012 for recognition of the loss amounting ₹ 6,00,000.

If embezzlement of cash comes to the notice of company management only after approval of financial statements by board of directors of the company, then the treatment will be done as per the provisions of AS 5. This being extra ordinary item should be disclosed in the statement of profit and loss as a part of loss for the year ending March, 2013. The nature and the amount of extra-ordinary item or prior period items should be separately disclosed on the statement of profit and loss in a manner that its impact on current profit or loss can be perceived

12. Neel Limited has its corporate office in Mumbai and sells its products to stockists all over India. On 31st March, 2013, the company wants to recognize receipt of cheques bearing date 31st March, 2013 or before, as "Cheques in Hand" by reducing "Trade Receivables". The "Cheques in Hand" is shown in the Balance Sheet as an item of cash and cash equivalents. All cheques are presented to the bank in the month of April 2013 and are also realized in the same month in normal course after deposit in the bank. State with reasons, whether each of the following is an adjusting event and how this fact is to be disclosed by the company, with reference to the relevant accounting standard.
- Cheques collected by the marketing personnel of the company from the stockists on or before 31st March, 2013.
 - Cheques sent by the stockists through courier on or before 31st March, 2013.

Answer:

- Cheques collected by the marketing personnel of the company is an adjusting event as the marketing personnels are employees of the company and therefore, are representatives of the company. Handing over of cheques by the stockist to the marketing employees discharges the

liability of the stockist. Therefore, cheques collected by the marketing personnel of the company on or before 31st March, 2013 require adjustment from the stockists' accounts i.e. from 'Trade Receivables A/c' even though these cheques (dated on or before 31st March, 2013) are presented in the bank in the month of April, 2013 in the normal course. Hence, collection of cheques by the marketing personnel is an adjusting event as per AS 4 'Contingencies and Events Occurring after the Balance Sheet Date'. Such 'cheques in hand' will be shown in the Balance Sheet as 'Cash and Cash equivalents' with a disclosure in the Notes to accounts about the accounting policy followed by the company for such cheques.

- b. Even if the cheques bear the date 31st March or before and are sent by the stockists through courier on or before 31st March, 2013, it is presumed that the cheques will be received after 31st March. Collection of cheques after 31st March, 2013 does not represent any condition existing on the balance sheet date i.e. 31st March. Thus, the collection of cheques after balance sheet date is not an adjusting event. Cheques that are received after the balance sheet date should be accounted for in the period in which they are received even though the same may be dated 31st March or before as per AS 4. Moreover, the collection of cheques after balance sheet date does not represent any material change affecting financial position of the enterprise, so no disclosure in the Director's Report is necessary.

13. [Nov. 2013] State with reasons, how the following events would be dealt with in the financial statements of Pradeep Ltd. for the year ended 31st March, 2013:

- a. An agreement to sell a land for ₹ 30 lakh to another company was entered into on 1st March, 2013. The value of land is shown at ₹ 20 lakh in the Balance Sheet as on 31st March, 2012. However, the Sale Deed was registered on 15th April, 2013.
- b. The negotiation with another company for acquisition of its business was started on 2nd February, 2013. Pradeep Ltd. invested ₹ 40 lakh on 12th April, 2013.

Answer:

- a. According to AS 4 "Contingencies and Events Occurring after the Balance Sheet Date", assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date.

In the given case, sale of immovable property was carried out before the closure of the books of accounts. This is clearly an event occurring after the balance sheet date but agreement to sell was effected on 1st March, 2013 i.e. before the balance sheet date. Registration of the sale deed on 15th April, 2013, simply provides additional information relating to the conditions existing at the balance sheet date. Therefore, adjustment to assets for sale of land is necessary in the financial statements of Pradeep Ltd. for the year ended 31st March, 2013.

- b. AS 4 (Revised) defines "Events occurring after the balance sheet date" as those 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. Accordingly, the acquisition of another company is an event occurring after the balance sheet date. However, no adjustment to assets and liabilities is required as the event

does not affect the determination and the condition of the amounts stated in the financial statements for the year ended 31st March, 2013.

Applying provisions of the standard which clearly state that/disclosure should be made in the report of the approving authority of those events occurring after the balance sheet date that represent material changes and commitments affecting the financial position of the enterprise, the investment of ₹ 40 lakhs in April, 2013 in the acquisition of another company should be disclosed in the report of the Board of Directors to enable users of financial statements to make proper evaluations and decisions.

14. **[Nov. 2018 Inter]** The accounting year of Dee Limited ended on 31st March, 2018 but the accounts were approved on 30th April, 2018. On 15th April, 2018 a fire occurred in the factory and office premises. The loss by fire is of such a magnitude that it was not possible to expect the enterprise Dee Limited to start operation again. State with reasons, whether the loss due to fire is an adjusting or non - adjusting event and how the fact of loss is to be disclosed by the company in the context of the provisions of AS-4 (Revised).

Answer:

As per AS 4 (Revised) "Contingencies and Events occurring after the Balance Sheet Date", an event occurring after the balance sheet date should be an adjusting event even if it does not reflect any condition existing on the balance sheet date, if the event is such as to indicate that the fundamental accounting assumption of going concern is no longer appropriate.

The fire occurred in the factory and office premises of an enterprise after 31 March, 2018 but before approval of financial statement of 30.4.18. The loss by fire is of such a magnitude that it is not reasonable to expect the Dee Ltd. to start operations again, i.e., the going concern assumption is not valid. Since the fire occurred after 31/03/18, the loss on fire is not a result of any condition existing on 31/03/18. But the loss due to fire is an adjusting event the entire accounts need to be prepared on a liquidation basis with adequate disclosures by the company by way of note in its financial statements in the following manner:

"Major fire occurred in the factory and office premises on 15th April, 2018 which has made impossible for the enterprise to start operations again. Therefore, the financial statements have been prepared on liquidation basis."

15. A Limited Company closed its accounting year on 30.6.2017 and the accounts for that period were considered and approved by the board of directors on 20th August, 2017. The company was engaged in laying pipe line for an oil company deep beneath the earth. While doing the boring work on 1.9.2017 it had met a rocky surface for which it was estimated that there would be an extra cost to the tune of ₹ 80 lakhs. You are required to state with reasons, how the event would be dealt with in the financial statements for the year ended 30.6.2017.

Answer:

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 mentioned definition and requirements given in 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 it is not an 'Adjusting event'.