13

Financial Statements Variation by Industry

Learning Outcomes

- To understand the differences in a Merchandising Company and a Manufacturing Company.
- To understand the variations in the Financial Statements by the Industry with the help of some real life practical cases.
- To know the differences in Financial Statements of a Merchandise Based Business and a Service Based Business.
- To understand the Differences between a Merchandiser's Income Statement and a Manufacturing Company's Income Statement.

13.1 Introduction

Organisations adapt their income statements according to their peculiar nature of business, the nature of their product(s) and many other factors including the type of the industry they are the part of. The elements of financial statements, especially the Balance Sheet and the Income and Expenditure/Profit and Loss Account statement vary to a large extent by the type of industry they are in. An income statement reflects both the total amount of revenue earned by a company and the cost of earning that revenue (denoted by 'expenses' in accounting terminology); the nature of revenues and expenses of a particular organisation largely depends on the nature of the industry it belongs to. The industries that have more expenses or more types of expenses, must disclose more information in their statements than those which have only fewer general expenses. Thus, the analysis of the Balance Sheet, Income and Cash flow statement of an organisation is based on the relative importance of different elements comprising these statements, depending on the type of industry. Broadly speaking, the industries can be classified in the following three types:

- Merchandising / Trading Firms.
- Manufacturing Firms.
- Service- providing Firms.

13.2 Differences in Merchandise Based Business and a Service Based Business

Basis	Merchandise Based Business	Service Based Business
Source of revenue	Such companies make revenue and profits off the inventory they sell, such as clothing, shoes or candles. Merchandise-based businesses rely on the sale of tangible goods to make money	Revenue is earned by providing various kinds of services.
Inventory	A trading or merchandise concern merely buys goods and sells them, barring some repacking. Thus, inventory is one of the largest assets of such enterprises and bulk of the working capital is locked up in this as it is imperative that current and future inventory be kept in reserves.	The inventory constitutes an insignificant proportion of the total assets and is limited to stationery, consumables, loose tools and similar items for service-providing firms.
Freight costs	Merchandise-based business has to consider transportation of inventory to other locations while planning company's budget.	Service-based businesses are not likely to have freight costs to deal with.
Storage and insurance costs	Paying for the storage and insurance of large amounts of inventory is a major expense for a merchandise-based business and may increase operating costs substantially depending on location and storage rates.	Such costs are almost negligible here.
Operating cycles	Merchandise-based businesses typically receive cash, buy inventory, merchandise the inventory, sell the goods and account for sales in the books.	Service-based businesses have fewer steps in managing their operating cycles. It generally consists of receiving cash, performing services and accounting for the sale of those services.

13.3 Differences in a Merchandising Company and Manufacturing Company

Basis	Merchandising Company	Manufacturing Company
Inventory	Merchandisers maintain only finished goods inventory.	Manufacturing companies have three classifications of inventory: raw materials, work- in- progress and finished goods.

Basis	Merchandising Company	Manufacturing Company
Relationship	Merchandising companies that conduct business as wholesalers, generally deal in bulk quantities and may sell only to retailers. Usually the merchandisers do not sell directly to individual customers.	Small-scale Manufacturers may sell directly to consumers. However, large manufacturing firms usually sell only to distributors, who can work as merchandiser.
Profits	Wholesale merchandisers make profits out of the mark-up, which is the amount added to the purchase price paid to the manufacturer from whom the products are bought. The merchandiser's net profit is obtained by subtracting the cost of operating expenses (the administrative, office, and distribution expenses) from gross profit. Gross profit equals sales minus the cost of goods sold, which usually comprises of inventory purchase costs, freight, octroi and similar clearing charges, cost of primary packing material etc.	Manufacturing Companies make profits by converting raw materials into finished products. These are sold at a price that covers the production costs, which comprises of cost of raw material purchased, other expenses namely, wages, factory expenses like power, fuel, consumables etc; as well as the selling and distribution expenses and the office and administrative costs.
Examples	Wal-Mart Stores Inc. is the largest merchandising company that purchases products from manufacturers and wholesalers across the globe and retails the finished products directly to consumers.	Raymond Ltd. is a leading textile manufacturing company in India

13.4 Practical Illustrations of Financial Statements Variation by the Industry

For explanation and illustration purpose, in the following paragraphs, the financial statements of each type of a selected firm is discussed. The balance sheets have been obtained from Bhatia & Bhaha Chartered Accountants.

1. Merchandising firm (Sahni Footwear),
2. Service-providing firm (Simbij Enterprises Private Limited), and
3. Manufacturing firm (Chandranchal Infrastructure Private Limited).

A. Merchandising Firms

Merchandising (retail - wholesale) firms sell finished products purchased from other firms. The main asset is inventory, which consists of finished goods. For some merchandising firms, a large amount of sales may be for cash. in such cases, the receivables balance will be relatively low. Other merchandising firms may have combination of both cash sales as well as credit sales, depending upon the requirements of the trade, in such cases, the amount of receivables will be higher appearing in the balance sheet. As there is lot of competition in this industry, gross profit ratio is often quite low, with the cost of sales and operating expenses constituting a large portion of expenses. Retailers are debt ridden as they rely on credit from wholesalers. and also offer extensive credit to customers and have outlets in high-rent locations. Wholesalers tend to be characterised by large inventories, large sales volume and chronic credit problems with retailers.

The following are the financial statements of Sahni Footwear, engaged in the business of purchase and sales of footwear. The firm purchases footwear firm Bata Ltd., Relaxo etc. and retails to customers. The firm being a trading concern has inventory of finished goods only.

Illustration-1:

M/S SAHNI FOOTWEAR -NEW DELHI

BALANCE SHEET AS AT 31.03.2017

PREV. YEAR	LIABILITIES	THIS YEAR	PREV. YEAR	ASSETS	THIS YEAR
11	**SHRI GURUJI MAHARAJ**	11	43,423	**FIXED ASSETS** (As per Schedule 'F' attached)	426,225
2,964,711	**PARTNER'S CAPITAL ACCOUNT** (As per Schedule 'A' attached)	2,721,289		**CURRENT ASSETS, LOANS & ADVANCES** A) Current Assets	
300,000	**UNSECURED LOAN** Reena Malhotra	300,000	6,993,654	a) Closing Stock **(As per inventory taken, valued & Certified by the Partners)**	7,737,362
4,804,304	**SECURED LOAN** From The South Indian Bank Ltd. (Against Stock)	4,910,331	386,412	b) Cash in Hand	441,422
	CURRENT LIABILITIES & PROVISIONS A) Current Liabilities		3,949,841	c) Trade Receivables (As per Schedule 'E' attached)	3,421,836
4,261,812	a) Trade Payables (As per Schedule 'B' attached)	4,762,376	250,000	**B) Loans & Advances** LOANS Sahni Guest House	250,000
175,510	b) Expenses Payable (As per Schedule 'C' attached)	34,300		**ADVANCES**	
			34,000	a) Earnest Money Deposits (As per Schedule 'F' attached)	34,000
			521,376	b) Advance Income Tax	53,167
			327,643	c) Duties & Taxes	364,294
12,506,349	TOTAL	12,728,307	12,506,349	TOTAL	12,728,307

For SAHNI FOOTWEAR

SD/-

PARTNER
Date: 01/09/2017
Place: New Delhi

Signed on terms of our report of even date:
For BHATIA & BHATIA
CHARTERED ACCOUNTANTS
FRN NO. 003202N of ICAI

SD/-

(R.BHATIA),F.C.A
Partner
Membership No. 17572

Note: The schedules mentioned above are not produced here keeping in mind the relevance and simplicity of readers' interest.

M/S SAHNI FOOTWEAR

TRADING AND PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31st MARCH, 2017

PREV. YEAR	PARTICULARS		THIS YEAR	PREV. YEAR	PARTICULARS		THIS YEAR
5,753,654	Opening Stock		6,993,654	28,219,232	Sales:		
26,962,752	Purchases:				Central Sale 5%	417217.85	
	Purchase 5%	9840345			Central Sales Vat Free	2277296	
	Purchase 12.5%	1,380,497			Sale 5%	9,296,109	
	Purchase Vat Free	14,666,240			Sale 12.5%	1,138,104	
	Less; Credit Note Received	718,715	25,168,367		Sales Vat Free	13,858,129	26,986,856
131,250	Carage I/W		131,580	200,900	Frieght Received		198,200
				6,993,654	Closing Stock (As per inventory taken valued & certified by the partner)		7,737,362
2,566,130	Gross Profit carried down		2,628,817				
35,413,786	TOTAL		34,922,418	35,413,786	TOTAL		34,922,418
35,180	Diwali Expenses		41,270	2,566,130	Gross Profit brought down		2,628,817
11,400	Audit Fees		11,500				
816,500	Salary to Staff		876,000				
64,500	Bonus		73,000	2970	Interest on Income Tax Refund		-
594,241	Bank Charges & Interest		652,932				
124,785	Carriage Outward		133,200	-	Credit Balnace written Back		149,051
6578	Depreciation		75,089				
9,320	Conveyance		9,155				
1,990	Dealer Commission		2,806				
11,557	Entertainment Expense		11,837				
87,285	Electrical Expenses		78,840				
3,100	Footwear Wholesale Association		5,100				
10,353	Misc. Expenses		9,469				
12,680	Packing		15,599				
1,932	Postage & Telegram		2,464				
4,453	Printing & Stationary		29,174				
170	Printer Paper		-				
24,853	Staff welfare		33,000				
26,282	Telephone Expenses		27,347				
350	Repair & Maintance		600				
98,452	Vehicle Maintainance		102,260				
1,200	Donation		-				
19,136	Cellular phone A/C		7,579				
5,220	Water Expenses		-				
308,330	Interest on Capital to Partner		305,642				
-	Vat Digital Signature		1,000				
(88)	Short and Excess		(948)				
289,341	Net Profit		273,953				
2,569,100	TOTAL		2,777,868	2,569,100	TOTAL		2,777,868
150,000	Salary to Partner		150,000	289,341	Net Profit transferred from P&I A/c		273,953
139,341	Net profit transferred to Partner's Capital A/C		123,953				
289,341	TOTAL		273,953	289,341	TOTAL		273,953

For **SAHNI FOOTWEAR**

SD/-

(PARTNER)
Date: 01/09/2017
Place: New Delhi

Signed on terms of our report of even date:
For BHATIA & BHATIA
CHARTERED ACCOUNTANTS
FRN NO. 003202N of ICAI

SD/-

(R.BHATIA),F.C.A
Partner
Membership No. 17572

B. Service Firms

A service firm earns its revenue from the service provided. As services are intangible, inventory is either nil or quite low, and it is majorly in the form of stationery or consumables. Service industries – such as railroads, airlines and public utilities – have less of a problem with flow of inventory. Their focus tends to be on balancing operating revenue against operating expenses dominated by fixed assets (depreciation, repairs, replacement, maintenance, etc.). Major expenses in such a firms can be employee benefit expenses, consultancy / professional charges, software expenses etc.

Simbij Enterprises Pvt. Ltd., is a service providing concern which renders services to foreign buyers. It checks the quality control of raw materials and finished goods as per the samples approved by the foreign buyers, sold by the Indian manufacturers. Students should observe here that there is no inventory amount appearing in the balance sheet. In the statement of profit and loss, no freight, storage and insurance costs are found.

Illustration-2:

SIMBIJ ENTERPRISES PRIVATE LIMITED
Balance Sheet as at 31st March 2016

(in Rupees)

	Particulars	Note No.	As at 31st March 2016	As at 31st March 2015
	1	2	3	4
I.	**EQUITY AND LIABILITIES**			
1.	**Shareholders' funds**			
	(a) Share capital	1	100,000	100,000
	(b) Reserves and surplus	2	24,763,614	24,487,849
3.	**Non-current liabilities**			
	(a) Long-term borrowings	3	150,000	150,000
	(b) Deferred tax liabilites (Net)	4	–	-
	(c) Long Term Provisions	5	1,266,154	1,007,477
	(d) Other Long term liabilities	6	686,311	469,680
4.	**Current liabilities**			
	(a) Short-term borrowings	7	1,125,126	3,316,090
	(b) Trade payables	8	16,950	103,947
	(c) Other current liabilities	9	374,475	742,915
	TOTAL		**28,482,630**	**30,377,958**
II.	**ASSETS**			
1.	**Non-current assets**			
	(a) Fixed assets			
	(i) Tangible assets	10	804,538	1,727,754
	(b) Deferred tax assets		390,658	294,787
2.	**Current assets**			
	(a) Current investment	11	13,156,000	14,656,000
	(b) Cash and cash equivalents	12	1,323,034	2,072,277
	(c) Short-term loans and advances	13	3,721,155	3,220,465
	(d) Other current assets	14	9,087,245	8,406,674
	TOTAL		28,482,630	**30,377,958**

For Simbij Enterprises Pvt. Ltd.

Signed in terms of our report of even date:
For **BHATIA & BHATIA**
CHARTED ACCOUNTANTS
FRN No. 00320N of ICAI

(Baljit Seghal)
Director
DIN No. 01054172
Date:

(Rashmi Ahuja)
Director
DIN No. 01054237

(R. BHATIA), F.C.A.
Partner
Membership No. 17572

Note: The schedules mentioned above are not produced here keeping in mind the relevance and simplicity of readers' interest.

SIMBIJ ENTERPRISES PRIVATE LIMITED

Statement of Profit and Loss for the year ended 31st March 2016

(in Rupees)

	Particulars	Refer Note No.	For the year ended 31st March 2016	For the year ended 31st March 2015
I.	Revenue from operations	15	7,593,727	19,367,664
II.	Other income	16	1,039,064	1,710,491
III.	**Total Revenue**		**8,632,791**	**21,078,155**
IV.	**Expenses:**			
	Employee benefits expense	17	4,715,440	9,180,206
	Finance costs	18	10,913	16,477
	Depreciation and amortization expense		747,045	1,300,094
	Other expenses	19	2,544,645	7,728,442
	Total expenses		**8,018,043**	**18,225,219**
V.	**Profit before tax**		**614,748**	**2,852,936**
VI	**Tax expense:**			
	(1) Current tax		258,677	-
	(2) Deferred tax		95,871	226,381
VII.	**Profit (Loss) for the period**		**451,942**	**3,079,317**
VII.	Earnings per equity share:			
	(1) Basic		452	3,079
	(2) Diluted		452	3,079

For Simbij Enterprises Pvt. Ltd.

SD/-

(Bijit Sehgal)
Director
DIN No. 01054172
Date:

SD/-

(Rashmi Ahuja)
Director
DIN No. 01054237

Signed in terms of our report of even date:
For **BHATIA & BHATIA**
CHARTERED ACCOUNTANTS
FRN No. 003202N of ICAI

SD/-

(R. BHATIA), F.C.A.
Partner
Membership No. 17572

C. Manufacturing Firms

A manufacturing firm will usually have large inventories which comprises of raw materials; work in process, and finished goods. There is huge investment in property, plant, and equipment. Accounts receivables may also be important element, depending on the terms of sale. The cost of sales often represents a major expense. Manufacturers tend to have a substantial investment in fixed assets (machinery, equipment and buildings) and often face major problems due to a large work-force. Income statements for manufacturing companies are typically more robust than those for other industries since manufacturers encounter a wider range of expenses than those companies that do not require extensive equipment, maintenance, shipping services or manpower.

Chandranchal Infrastructure Pvt. Ltd. is a manufacturing and trading concern engaged in manufacturing of Cast Iron Pipes and Tubes. Since, the business is a combination of manufacturing and trading — the inventory in Balance sheet comprises of raw material, semi-finished and finished goods. A significant proportion of expenses relate to repairs, insurance and depreciations.

CHANDRANCHAL INFRASTRUCTURE PRIVATE LIMITED

Balance Sheet as at 31st March, 2017

(in Rupees)

Particulars	Note No.	As at 31 March 2017	As at 31 March 2016
1	2	3	4
I. EQUITY AND LIABILITIES			
1 Shareholders' funds			
(a) Share capital	3	2,440,000	2,440,000
(b) Reserves and surplus	4	45,902,776	28,133,915
2 Non-current liabilities			
(a) Long-term borrowings	5	3,464,072	1,400,000
3 Current liabilities			
(a) Short-term borrowings	6	61,780,060	15,379,022
(b) Trade Payables	7	1,168,226	4,170,290
(c) Advances received from Customer	7	4,642,472	2,463,184
(d) Other current liabilities	7	45,441,646	4,713,535
(e) Short-term provisions	8	3,134,611	184,611
TOTAL		**167,973,862**	**58,884,557**
II. ASSETS			
1 Non-current assets			
(a) Fixed assets			
Tangible assets	9	14,454,385	14,944,522
(b) Non-current investments	10	8,478,000	8,478,000
(c) Long-term loans and advances	11	232,295	232,295
(d) Deffered Tax Asset	12	280,016	310,769
2 Current assets			
(a) Inventories	13	66,234,115	18,099,070
(b) Trade Receivables	14	64,279,371	9,984,846
(d) Cash and Cash Equivalents	15	1,071,580	5,811,772
(e) Short-Term Loans and Advances	16	12,944,099	1,023,284
TOTAL		**167,973,862**	**58,884,557**

For CHANDRANCHAL INFRASTRUCTURE PRIVATE LIMITED

SD/-
(PAWAN KUMAR KEJRIWAL)
(MANAGING DIRECTOR)

SD/-
(CHANDRAKANT KEJRIWAL)
(DIRECTOR)

Signed in terms of our report of even date
For BHATIA & BHATIA
CHARTERED ACCOUNTANTS
FRN NO 003202N OF ICAI

SD/-
(R.BHATIA) FCA
Partner

Note: The schedules mentioned above are not produced here keeping in mind the relevance and simplicity of readers' interest.

CHANDRANCHAL INFRASTRUCTURE PVT.LTD

Statement of Profit and Loss for the year ended 31st March,2017

(in Rupees)

	Particulars	Refer Note No.	For the year ended 31st March 2017	For the year ended 31st March 2016
I.	Revenue from operations	17	205,219,061	93,406,531
II.	Other income	18	14,854,205	344,432
III.	**Total Revenue (I + II)**		220,073,266	93,750,963
IV.	Expenses:			
	Cost of materials consumed	19	173,225,994	77,601,049
	Employee benefits expense	20	7,027,513	3,164,120
	Finance costs	21	4,982,709	1,750,820
	Depreciation and amortization expense		939,929	800,473
	Other expenses	22	13,147,508	9,481,476
	Total expenses		199,323,652	92,797,938
V.	**Profit before exceptional and extraordinary items and tax (III-IV)**		20,749,614	953,025
VI.	Exceptional items		-	-
VII.	**Profit before extraordinary items and tax (V - VI)**		20,749,614	953,025
VIII.	Extraordinary Items		-	-
IX.	**Profit before tax (VII- VIII)**		20,749,614	953,025
X	Tax expense:			
	(1) Current tax		2,950,000	184,611
	(2) Deferred tax Asset/(Liability)		(30,753)	127,129
XI	**Profit (Loss) for the period from continuing operations (VII-VIII)**		17,768,861	895,542
XII	**Profit/(loss) from discontinuing operations**		-	-
XIII	**Tax expense of discontinuing operations**		-	-
XIV	**Profit/(loss) from Discontinuing operations (after tax) (XII-XIII)**		17,768,861	895,542
XV	**Profit (Loss) for the period (XI + XIV)**		17,768,861	895,542
XVI	**Earnings per equity share:**			
	(1) Basic		72.82	3.67
	(2) Diluted		72.82	3.67

Signed in terms of our report of even
For BHATIA & BHATIA
CHARTERED ACCOUNTANTS
FRN NO 003202N OF ICAI

For CHANDRANCHAL INFRASTRUCTURE PVT. LTD.

SD/-
(PAWAN KUMAR KEJRIWAL)
(MANAGING DIRECTOR)

SD/-
(CHANDRAKANT KEJRIWAL)
(DIRECTOR)

SD/-
(R.BHATIA) FCA
Partner
Membership No. 017572

Differences between a Merchandiser's Income Statement and a Manufacturing Company's Income Statement

—by Kevin Johnston

An income statement reflects your small-business earnings and shows all the expenses incurred in generating that income. If your small business is a manufacturing company, you will show different categories of expenses than you would for a merchandising company. The following is the discussion for showing the cost of goods sold on an income statement for both types of companies.

Earnings

The method for reporting earnings is the same for merchandisers and manufacturers. Each type of company has sales and the total of these sales is the earnings figure. This figure does not reflect cost-of-goods expenses.

Cost of Goods for Merchandisers

Merchandisers buy goods and resell them. The cost of those goods must be subtracted from the earnings figure. The method for calculating this figure is to add inventory on hand at the beginning of the accounting period to inventory purchased during the accounting period. Subtract the inventory on hand at the end of the period, and subtract any freight charges. This is the cost-of-goods figure for a merchandiser. The merchandiser's income statement will show gross revenues minus this cost-of-goods sold.

Cost of Goods for Manufacturers

Manufacturers break the cost of goods into various categories. Raw materials expenses make up the first category of manufacturing expenses. This cost covers any components, parts or materials required to make the company's product. The manufacturer must also inventory goods-in-progress. These are partially manufactured products that could not be finished before the end of the accounting period. In addition, manufacturers must count finished products that are available for sale. Manufacturers also count the cost of manufacturing labor and factory overhead in determining expenses that are related to the cost of goods. This is quite different from merchandisers who do not include labor in cost-of-goods figures. Manufacturers do not count freight as an expense in the manufacturing process, because freight is usually paid for by the merchandiser.

Cost of Goods Manufactured

The expenses for merchandisers and manufacturers are so different that they often call their expense statements by different names. The merchandiser refers to expenses as "cost of goods sold." Manufacturers often refer to expenses and "cost of goods manufactured." The income statements for each of these types of companies may reflect this terminology.

Separate Documents

Manufacturers who generate a "cost of goods manufactured statement" may make this a separate document that is attached to the income statement. The total of the manufacturing expenses must be included in the actual income statement.