Declaration and payment of Dividend:

Question Bank

MCQs:

Q1) ABC limited has a paid up capital of INR 2,50,000, comprising of 2,500 shares of INR 100 face value. The shares are traded in NSE and has market value of INR 1,000 each.

The Board declared dividend of 10 %. The amount payable as dividend would be which of the following:

1) INR 25,000
2) INR 2,50,000
3) INR 2500
4) INR 25,00,000

Q2) The final rate of dividend declared by the BOD was 10%. The members want to change the rate that can be finally declared. Which of the following shall be not be allowable as dividend rate :

1)2 %

2)7%

3)0%

4)15%

Q3) Kiara Ltd wants to declare dividend , however want to utilize previous years free reserves due to shortfall of current years profit. Which of the following does not need to be taken care before utilizing such amounts:

1) Deducting depreciation

2) Adding back notional gains
3) Adding back capital gains
4) Adding back non-recurring expenses.

Q4) Roby Ltd had Kiara as their major shareholders. Roby Ltd has performed well but reserves seems less for declaring dividend. The BOD of Roby Ltd want to declare the dividend. The rates of dividend declared for the past three years are as:

Year 1 – 2 %

Year 2 – 3%

Year 3 – 10 %

The rate of dividend cannot exceed:

1)2 %

2) 3%

3) 5%

4) 10%

Q5) The unpaid or unclaimed Dividend need to be transferred to UDA account within the expiry of 7 days of:

1) 30 days from declaration
2) 30 days from bank confirmation
3) Immediately on declaration
4) 15 days from declaration

Descriptive:

Q1) What does Dividend mean? What are the different types of shares and the various dividend provision with respect to it?

Q2) How can Dividend be classified based on time i.e. when declared? What are the various provisions with respect to the same?

Q3) State the provisions with respect to provision and declaration of dividend.

Q4) State the provisions with respective to declaration of dividend in case of inadequacy of profits.

Q5) State the various provisions regarding the Investor Education and Protection Fund (IEPF).

Scenario Based MCQs:

Kiara Ltd has been in existence since last 2 years. The general reserves, issued capital and paid up capital stands as INR 140 Lacs , INR 200 Lacs and INR 100 lacs respectively. The shares have market value of INR 200 Lacs. The Company was established in the year 20X0 and runs the business of fashion accessories. The profits were increasing consistently over the period of two years. The company declared dividend @ 15 % in the first year of business. The rate of dividend increased to 17 % in the next year of business. Mr. Roby a Chartered Accountant has been appointed as the financial controller of Kiara Ltd. He has a proven record for correcting the books of accounts and have always been acclaimed to make books adhere to laws and standards. The Board in the third year makes a proposal of 20%. Mr. Roby starts the internal control and figures out that depreciation charge to the extent of INR 4 Lacs in missing for the last year. Further the expenses of INR 6 lacs seems unjustified. And he proposes to write off depreciation and add back inadmissible expenses. He further advises that distribution of dividend @ 20 % is inadmissible and advises BOD to fix the cap to 16 % which was average of two years dividend.

Keeping in view the above scenario and the Second Proviso to Sec. 123 provide your view to the company with regards to:

1) The rate of dividend that the company can declare in the third year as per dividend declaration and payment rules. Is Mr. Roby correct with respect to the capping of dividend rate?
2) Is Mr. Roby correct in making adjustments to the profit?

3) What shall be consequences in case depreciation is not provided in the books of accounts?
4) With respect to second year dividend it has been around 30 days since declaration that members whose dividend comprising of INR 1lacs has not been claimed. Explain the provisions for the same. What shall be consequences in case the company fails to follow the same?
5) Mr. Roby suggests a minimum transfer to general reserve of 5 % of net profits before dividend. Is he correct in his suggestion?

Answers Hints :

MCQs:

1) Correct answer is 1 as dividend is payable on face value. Therefore 10% of 250000= 25000
2) The correct answer is 4 as shareholders cannot increase the rate of dividend as was declared by BOD. Rest all are less than the rate suggested by BOD.
3) Correct answer is 4 as all other are required to be adjusted for the purpose of calculation of dividend.
4) Correct answer is 3 (avg rate for three years=(2+3+20)/3)
5) Correct answer is 1 (30 days from declaration)

Scenario based:

1) CONDITION I of Declaration of Dividend when there is inadequacy or Absence of Profits (Second Proviso to Sec. 123). Provided that the rate of dividend declared shall not exceed the average of the rates at which dividend was declared by the company in the immediately preceding three years. Rate of Dividend ≤ (RD1 +RD2 + RD3)/3 Where, RD1, RD2, RD3 are rates at which dividend was declared by the company in the immediately preceding three years. However, this condition shall not apply if the company has not declared any dividend in each of the three preceding financial years , hence MR. R is not correct for putting the capping.

2) Yes Roby is correct in making corrective entries as provision for declaration of dividend and payment provide that before declaring the dividend previous losses and depreciation not provided in previous year or years are required to be set off against profit of the company for the current year . In computing profits any amount representing unrealised gains, notional gains or revaluation of assets and any change in carrying amount of an asset or of a liability on measurement of the asset or the liability at fair value shall be excluded.
3) Dividend is an apportionment from revenue profits. Therefore, dividend should never be declared out of capital. This is also the reason for prohibition on issue of shares at a discount which you studied in the topic Share Capital and Debentures. "Depreciation" is a notional estimate of the reduction in the value of an asset due to i. wear and tear, ii. efflux of time, iii. improvements in technology etc. If depreciation is not provided for there will be two consequences: i. The value of the asset will be overstated in Balance Sheet ii. The profits of the current year will be overstated. At the time of winding up of the company the value of assets appearing in the Balance-sheet would appear to be sufficient to repay the capital of the shareholders but the actual realizable value thereof will be a paltry sum which may not be sufficient even to meet the expenses of winding up.
4) Unpaid or Unclaimed Dividend to be transferred to the Unpaid Dividend Account- Where a dividend has been declared by a company but has not been paid or claimed within thirty (30) days from the date of declaration, the

company shall, within seven (7) days from the expiry of the said period of 30 days, transfer the total amount of unpaid or unclaimed dividend to a special account called the Unpaid Dividend Account (UDA). The UDA shall be opened by the company in any scheduled bank.

Punishment for Contravention- If a company fails to comply with any of the requirements of this section, such company shall be liable to a penalty of one lakh rupees and in case of continuing failure, with a further penalty of five hundred rupees for each day after the first during which such failure continues, subject to a maximum of ten lakh rupees and every officer of the company who is in default shall be liable to a penalty of twenty-five thousand rupees and in case of continuing failure, with a further penalty of one hundred rupees for each day after the first during which such failure continues, subject to a maximum of two lakh rupees.

5) Transfer of profits to reserves for any financial year has been left to the discretion of the company. Therefore, a company is free to transfer any portion of its profit to reserves as it may deem fit. It may also decide not to transfer any amount to reserves.

   Hence Mr. Roby is not correct in making this suggestion.