Footwear India Limited

Footwear India Limited (FWI) had been in existence for more than six decades in the country and was one of the leading footwear manufacturers of the country. It had strategic investments from and technical collaboration with Footwear Canada. The Balance Sheet as 31-Dec-2001 is given in Exhibit 1. The numbers at the end of the year 2002 were not very pleasing.

At the end of the year 2002, the company had achieved a sales turnover of more than Rs.8,500 million. This was higher than the turnover of year 2001, but the guess was that the annual results would not be up to the mark. Already FWI had started identifying reasons as "under recovery of expenses at manufacturing facilites due to reduced production as well as increased markdowns on slow moving stocks." The capacity utilization of the company was less than 50% in all its business categories. It was a difficult year, and the results were showing.

FWI sold its products through its own outlets – where the sales were only on cash/credit cards. Sales revenue from these outlets amounted to Rs.4,556[3]. In addition FWI had a system of franchisee outlets. These outlets had a usual credit period of around 60 days. Sales through franchisees during the year amounted to Rs.4,060.

In addition, the company had the following additional receipts in cash:

Income from the repairs division	14
Sale of Scrap and miscellaneous income	52
Interest Receipts	10
Sale of Fixed Assets	45
Bad Debts written off, recovered	02
Receipts from Sundry Debtors	4,100
Total	**Rs.4,223**

All interest that was due for the year was received. Interest received was the net of tax deducted at source. The Gross amount of interest income for the year was Rs.15, of which Rs.3 was accrued but not yet due.

In case of Fixed Assets, the company had sold during the year, property comprising of residential colony, land and building at Faridabad. These assets were very old assets and were re-valued in the year 1982. The difference between the original cost and the re-valuation was put in a separate re-valuation reserve, not available for distribution. Every year, when these re-valued assets were depreciated, the proportionate depreciation pertaining to the historic cost was charged off in the income statement, while the proportionate depreciation on the revalued portion was reduced from the re-valuation reserve. Thus, at the end of the useful life of the asset, the revaluation reserve would come back to zero. During the year, some of these assets were sold. On the whole, the company made a profit on the sale of these assets. The details of historic cost, revalued costs and accumulated depreciation on the assets sold during the year are given below:

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1 Prepared by Professor M S Sriram, based on published annual reports. Some items have been reclassified for purposes of clarity and simplicity

2 All Figures in this case are in Rs.Million.

Asset	Historic Cost	Revalued Cost	Accumulated Depreciation on historc cost	Accumulated Depreciation charged to Revaluation Reserve	Net Value
Land	10	30			30
Building and other assets	20	58	7	28	23
Total	30	88	7	28	53

The other **payments** made by FWI during the year were as follows:

Payment to creditors	2,165
Purchase of finished goods	1,527
Purchase of stores and spares	46
Power, fuel, processing charges rates and taxes	745
Excise Duty	400
Repairs of plant and machinery	40
Freight and Despatch	262
Other Administrative expenses (Insurance, Travel expenses, rent, salary)	2,746
Total	**7,931**

During the year, there was an additional cash outflow of Rs.45 towards capital work in progress – which pertained to a new facility being set up in Peenya, near Bangalore. This work was continuing, and no Capital WIP was transferred to Fixed Assets during the year. It was ascertained that interest expenses pertaining to a loan borrowed for construction of the Peenya facility amounting to Rs.5 was not added to the capital Work-in-Process account. This amount was a part of the total interest expenses of the company. For the year the interest expenses of the company was Rs. 90. (The interest payments during the year were actually only Rs.85)

The following year-end adjustments were to be considered for FWI

Total purchase of raw materials on credit	2,350
Depreciation on Historical cost (other fixed assets)	135
Depreciation on Revalued portion (other fixed assets)	45
Excise Duty payable at the end of the year	42
Closing Stock of Raw Material (net of pilferage of Rs.12)	190
Closing Stock of Work in Process	152
Closing Stock of Stores and spares	42
Closing Stock of Finished Goods	1,548
Additional provision for bad debts to be made	100
Bad debts to be written off	12

In addition to the above, there was a claim of Rs.50 raised by the sales tax department in Uttar Pradesh against the company. However, the company had gone in appeal against the department. The legal advisers of the company had indicated that the company was on a strong footing and the likelihood of winning the case was high.

The dividend that was proposed at the end of last year was paid during the year.

After accounting for all the above accounts, a provision for taxation amounting to 35% of the income and 2% surcharge on the tax was to be made. (Please note that the income tax department allows all expenses to be charged while arriving at the taxable income, except provision for bad debts. However, actual write off of bad debts can be claimed as an expense).

The company had not made any advance payments of tax, except for the tax deducted at source on its interest income. However, the company had settled its past years tax dues, which was finally assessed at Rs.310.

Considering that it was a difficult year, the management did not propose any dividend for the year. Any profits earned during the year were to be transferred to the general reserve account.

Exhibit 1

Footwear India Limited Balance sheet as at 31st Dec, 2001			
Particulars	**Amount Rs in Millions**		
Sources of Funds:			
Shareholders' Funds			
Equity Shares of Rs.10 each fully paid up			514
Reserves and Surplus			
Revaluation Reserve		1436	
Share premium account		824	
General Reserve		651	2911
Loan Funds			
Secured Loans		79	
Unsecured Loans from Financial Institutions		515	594
Total			**4019**
Application of Funds			
Fixed Assets			
Land			1071
Other Fixed Assets			
Gross Block		2305	
Accumulated Depreciation		1300	1005
Capital Work in Progress			7
Investments			49
Net Current Assets			
Current Assets, Loans and Advances			
Raw Material Inventory	217		
Work in Progress Inventory	128		
Finished Goods Inventory	1806		
Stores, Spares and Packing Materials Inventory	46	2197	
Sundry Debtors	1295		
Less Provision for Doubtful Debts	49	1246	
Cash and Bank Balances		39	
		3482	
Less Current Liabilities and Provisions			
Trade Creditors	1193		
Interest Payable	6		
Provision for Taxation	309		
Excise Duty	2		
Provision for Payment of Dividend and tax on Dividend	85	1595	1887
Total			**4019**