

AS – 20: EARNINGS PER SHARE (EPS)

- **Objective:**

Earnings Per Share (EPS) is a financial ratio that gives the information regarding earnings available for each equity share. It is a very important financial ratio for assessing the market price of the share.

The objective of this Statement is to prescribe principles for the determination and presentation of EPS. The focus of this Statement is on the denominator of the EPS calculation.

- **Scope:**

This Standard should be applied by all the entities.

However, a Small and Medium Sized Company and a Small and Medium Sized non-corporate entity falling in Level II or Level III, may not disclose diluted EPS (both including and excluding extraordinary items).

Further, a non-corporate Small and Medium Sized Entity falling in level III may not disclose the information required by paragraph 48(ii) of the standard.

In consolidated financial statements, the information required by this Standard should be presented on the basis of consolidated information.

Accordingly, in the case of holding enterprises, earnings per share is presented on the basis of consolidated financial statements as well as individual financial statements of the parent.

- **Definitions:**

No.	Terms	Description
1.	Equity share	A share other than a preference share.
2.	Preference share	A share carrying preferential rights to dividends and repayment of capital.
3.	Financial instrument	Any contract that gives rise to both a financial asset of one enterprise and a financial liability or equity shares of another enterprise. E.g. Options, Warrants, Debentures, Investments etc.
4.	Potential equity share	A financial instrument or other contract that entitles, or may entitle, its holder to equity shares. <u>Examples of potential equity shares are:</u> a. Debt instruments or preference shares, that are convertible into equity shares; b. Share warrants; c. Options including employee stock option plans: under which employees of an enterprise are entitled to receive

		equity shares as part of their remuneration and other similar plans: d. Contingently issuable shares,
5.	Share warrants / Options	Financial instruments that give the holder the right to acquire equity shares.
6.	Fair value	The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

- **Presentation:**

An enterprise should present basic and diluted EPS on the face of the statement of profit and loss for each class of equity shares that has a different right to share in the net profit for the period. An enterprise should present basic and diluted EPS with equal prominence for all periods presented.

This Statement requires an enterprise to present basic and diluted EPS, even if the amounts disclosed are negative (a loss per share).

- **Measurement:**

(A) Basic EPS

Basic EPS should be calculated by dividing the net profit or loss for the period attributable to equity shareholders by the weighted average number of equity shares outstanding during the period.

$$\text{Basic EPS} = \frac{\text{Earnings i.e. Net profit or loss for the period attributable to equity shareholders}}{\text{Weighted Average No. of equity shares outstanding during the period.}}$$

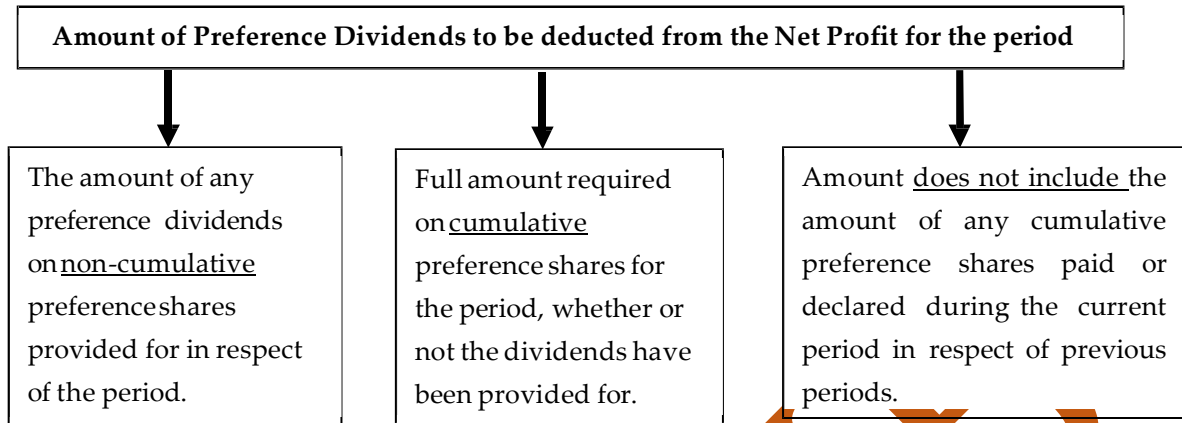
1) Earnings (Basic – Numerator):

For the purpose of calculating Basic EPS, the net profit or loss for the period attributable to equity shareholders should be the net profit or loss for the period after deducting preference dividends and any attributable tax thereto for the period. (Para 11)

All items of income and expense which are recognized in a period, including tax expense and extraordinary items, are included in the determination of the net profit or loss for the period.

Particulars	Amount (Rs.)
Earnings before Tax from ordinary operating activities	XX
(+) Extraordinary items (Income)	XX
(-) Extraordinary items (Expense)	(XX)
(-) Tax attributable to the period	(XX)
(-) Preference dividend (*)	(XX)
Profit for the purpose of calculating EPS	XX

(*) Determination of amount of preference dividend to be deducted from Net Profit:



2) **Per Share (Basic – Denominator):**

For the purpose of calculating Basic EPS, the number of equity shares should be the weighted average number of equity shares outstanding during the period. (Para 15)

The weighted average number of equity shares outstanding during the period is the number of equity shares outstanding at the beginning of the period, adjusted by the number of equity shares bought back or issued during the period multiplied by the time-weighting factor.

Time Weighting Factor:

The time-weighting factor is the number of days for which the specific shares are outstanding as a proportion of the total number of days in the period. A reasonable approximation of the weighted average is adequate in many circumstances.

In most cases, shares are included in the weighted average number of shares *from the date the consideration is receivable*.

Partly paid equity shares:

Partly paid equity shares are treated as a fraction of an equity share to the extent that they were entitled to participate in dividends relative to a fully paid equity share during the reporting period.

Shares with different face values:

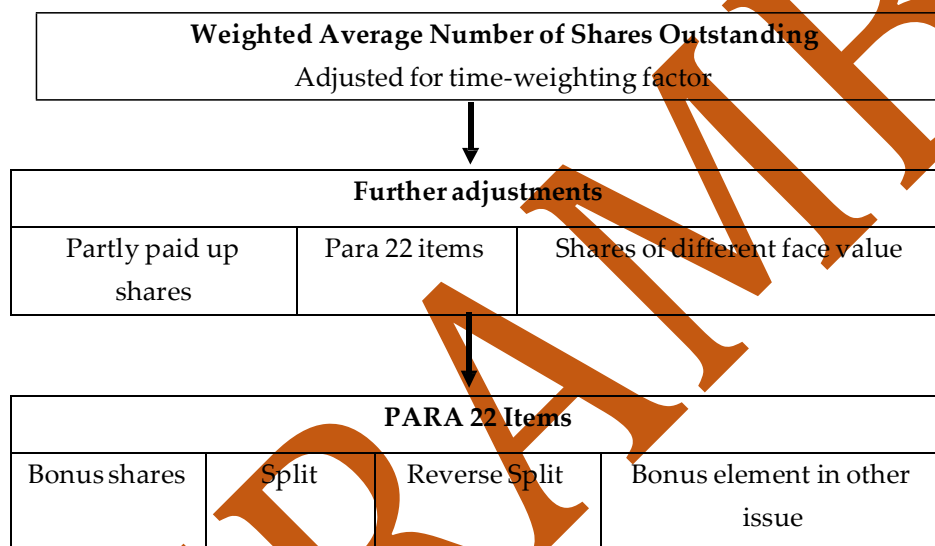
Where an enterprise has equity shares of different nominal values but with the same dividend rights, the number of equity shares is calculated by converting all such equity shares into equivalent number of shares of the same nominal value.

Para 22: The weighted average number of equity shares outstanding during the period and for all periods presented should be adjusted for events, other than the conversion of potential

equity shares that have changed the number of equity shares outstanding, without a corresponding change in resources.

Examples include:

- a. A bonus issue;
- b. A bonus element in any other issue, for example a bonus element in a rights issue to existing shareholders;
- c. A share split; and
- d. A reverse share split (consolidation of shares).



Bonus, Share Split, Reverse Share Split:

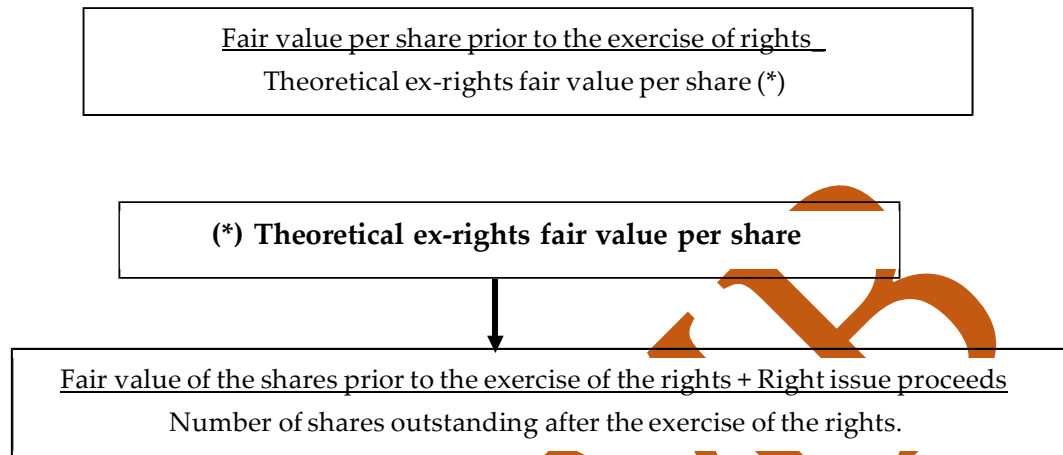
In case of a bonus issue or a share split, equity shares are issued to existing shareholders for no additional consideration. Therefore, the number of equity shares outstanding is increased without an increase in resources.

The number of equity shares outstanding before the event is adjusted for the proportionate change in the number of equity shares outstanding as if the event had occurred at the beginning of the earliest period reported.

Bonus Element in other issues (Rights Issue):

The issue of equity shares at the time of exercise or conversion of potential equity shares will not usually give rise to a bonus element, since the potential equity shares will usually have been issued for full value, resulting in a proportionate change in the resources available to the enterprise. In a rights issue, on the other hand, the exercise price is often less than the fair value of the shares. Therefore, a rights issue usually includes a bonus element.

The number of equity shares to be used in calculating basic EPS for *all periods prior to the rights issue* is the number of equity shares outstanding prior to the issue, multiplied by the following factor:



(B) Diluted Earnings Per Share:

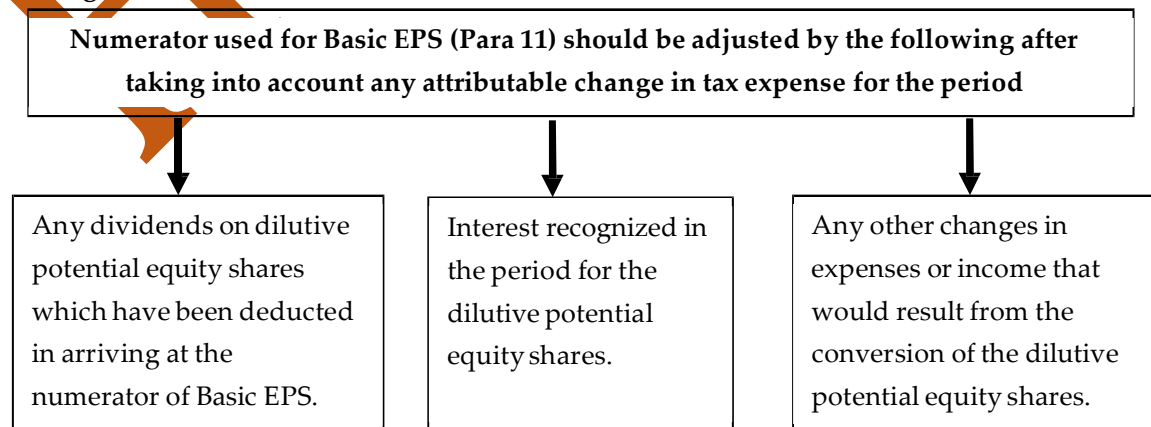
Diluted EPS is calculated when there are potential equity shares in the capital structure of the enterprises.

The objective is to depict the potential reduction in the basic EPS in future which impacts the market price per share.

Dilution is a reduction in earnings per share or an increase in loss per share resulting from the assumption that convertible debentures are converted, that options and warrants are exercised, or that ordinary shares are issued upon the satisfaction of specified conditions.

For the purpose of calculating diluted EPS, the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period i.e. numerator and denominator used for basic EPS calculation should be *adjusted for the effects of all "dilutive" potential equity shares.*

1) Earnings (Diluted – Numerator):



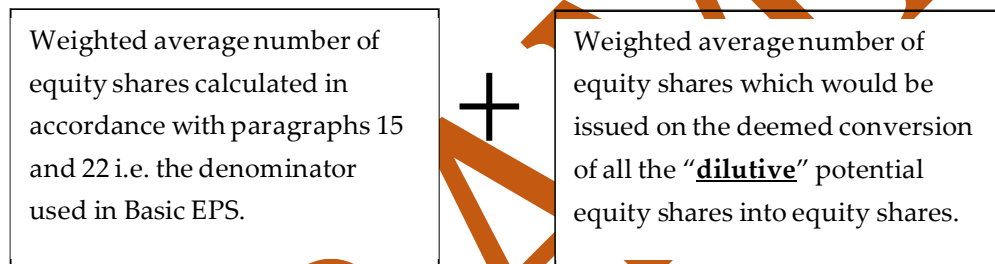
After the *potential equity shares are converted into equity shares*, the dividends, interest and other expenses or income associated with those potential equity shares will no longer be incurred (or earned). Instead, the new equity shares will be entitled to participate in the net profit attributable to equity shareholders.

Therefore, the net profit for the period attributable to equity shareholders calculated in accordance with paragraph 11 is *increased by the amount of dividends, interest and other expenses that will be saved, and reduced by the amount of income that will cease to accrue, on the conversion of the dilutive potential equity shares into equity shares.*

The amounts of dividends, interest and other expenses or income are adjusted for any attributable taxes.

2) Per Share (Diluted – Denominator):

For the purpose of calculating Diluted EPS, the number of equity shares should be:

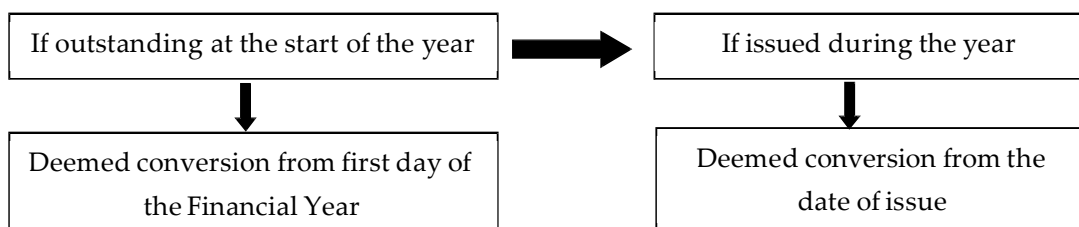


Share application money pending allotment or any advance share application money as at the balance sheet date, which is not statutorily required to be kept separately and is being utilized in the business of the enterprise, is treated in the same manner as dilutive potential equity shares for the purpose of calculation of diluted EPS.

The number of equity shares which would be issued on the conversion of dilutive potential equity shares is determined from the terms of the potential equity shares.

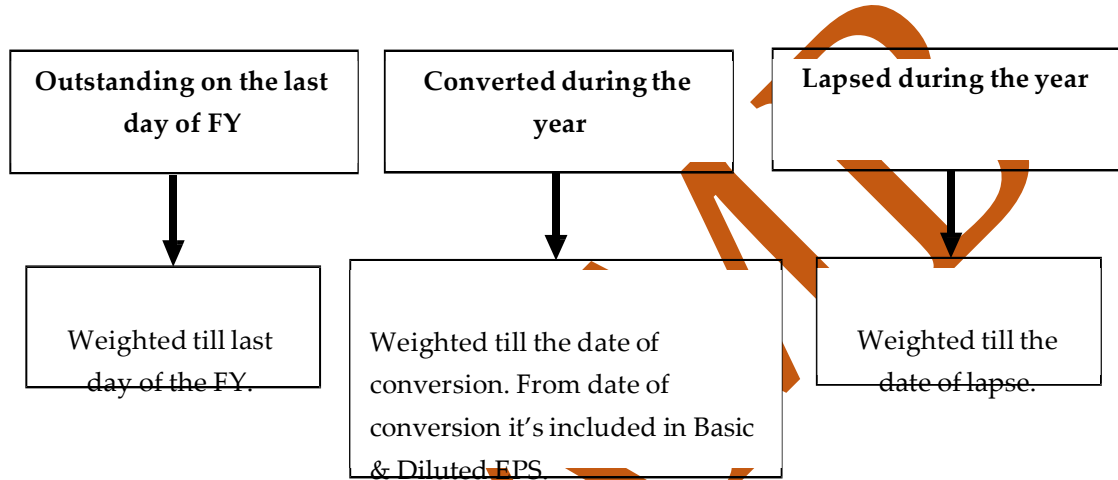
The computation assumes the most advantageous conversion rate or exercise price from the standpoint of the holder of the potential equity shares. (Conservatism requires most advantageous rate/terms to the holder)

Dilutive potential equity shares should be deemed to have been converted into equity shares at the beginning of the period or, if issued later, the date of the issue of the potential equity shares.

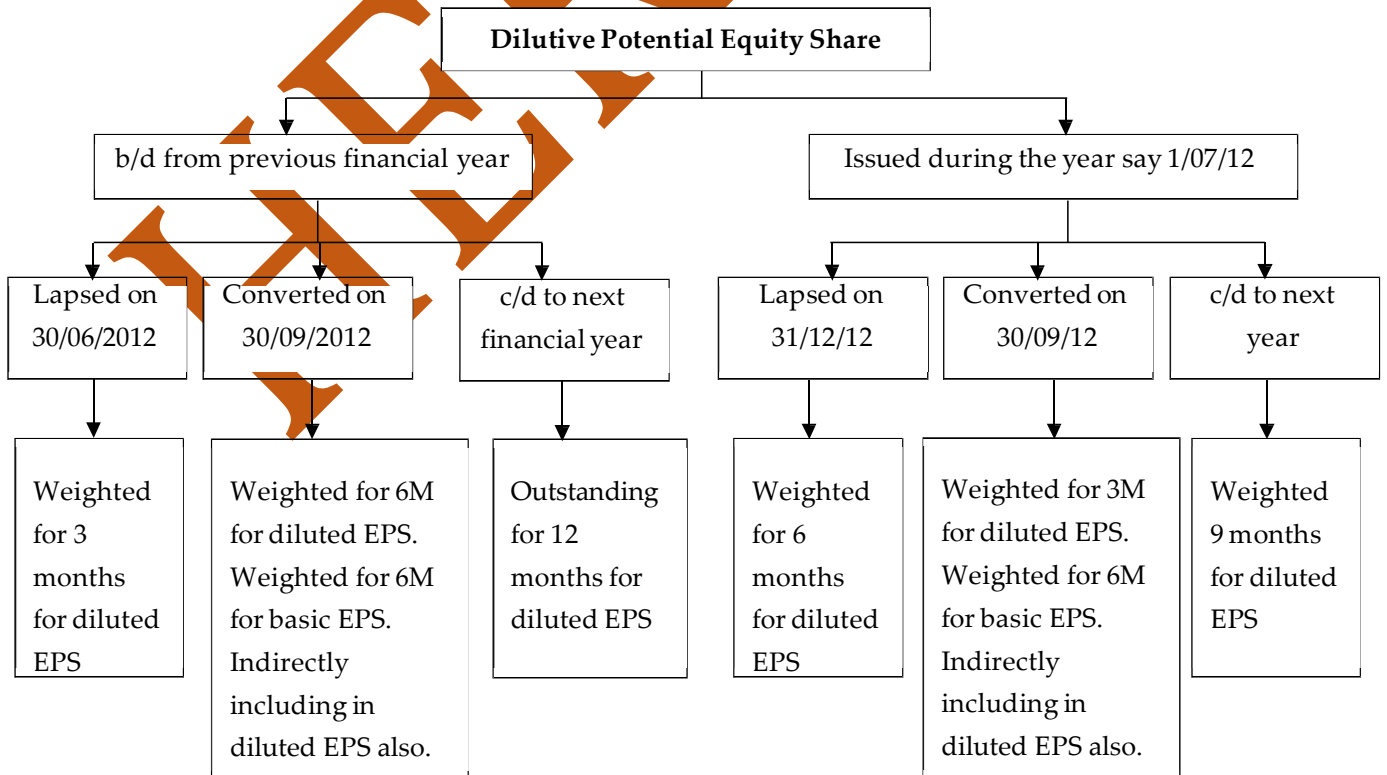


Potential Equity Shares – Weighted:

Potential equity shares are weighted for the period they were outstanding. Potential equity shares that were cancelled or allowed to lapse during the reporting period are included in the computation of diluted EPS only for the portion of the period during which they were outstanding. Potential equity shares that have been converted into equity shares during the reporting period are included in the calculation of diluted EPS from the beginning of the period to the date of conversion; from the date of conversion, the resulting equity shares are included in computing both basic and diluted EPS.



Consider financial year as April 2012 to March 2013



Example:

Consider the Financial year as 1st April 2011 till 31st March 2012

Particulars of Dilutive Potential equity share	Time Weighting Factor
Issued on 1 st January 2011 and outstanding for the year ended 31 st March 2012	12/12 (outstanding from first day of the FY till last day of FY)
Issued on 1 st January 2012 and outstanding for the year ended 31 st March 2012	3/12 (outstanding from date of issue till last day of FY)
Issued on 1 st January 2011 and converted on 30 th September 2011	6/12 (outstanding from first day of FY till date of conversion. From date of conversion its included for basic EPS calculation)
Issued on 1 st July 2011 and converted on 31 st December 2011	6/12 (outstanding from date of issue till date of conversion)
Issued on 1 st January 2011 and lapsed on 30 th June 2011	3/12 (outstanding from first day of the FY till date of lapse)
Issued on 1 st July 2011 and lapsed on 31 st December 2011	6/12 (outstanding from date of issue till the date of lapse)

Dilutive Options:

- Stock Options are financial instruments which entitles the holder to subscribe for the shares at a pre-determined price which is called as the strike price.
- When the options are executed the holder pays the strike price and the entity issues equity shares against it. This strike price is usually at a discount to the prevailing market price of the shares.
- Therefore this creates a situation where shares are issued at a discount. And when the shares are not issued at fair value there is a dilution in the EPS.
- *Please note that shares are issued when the options are executed and not when the options are issued or granted. This future diminution in the basic EPS is to be shown in calculation of diluted EPS.*
- Options and other share purchase arrangements are dilutive when they would result in the issue of equity shares for less than fair value.

Amount of the dilution = Fair Value - Issue Price

For the purpose of calculating diluted EPS, an enterprise should assume the exercise of dilutive options and other dilutive potential equity shares of the enterprise.

The assumed proceeds from these issues should be considered to be received from the issue at fair value.

The difference between the number of shares issuable and the number of shares that would have been issued at fair value should be treated as an issue of equity shares for no consideration.

And it is these equity shares which are treated as issued for no consideration that dilutes the EPS. Those shares which are treated as issued for fair value will not be dilutive in nature.

3) Dilutive Potential Equity Shares:

Potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would decrease “net profit per share from continuing ordinary operations”

An enterprise uses net profit from continuing ordinary activities, as defined in AS 5, after deducting preference dividends and any attributable tax thereto and after excluding items relating to discontinued operations as “the control figure” that is used to establish whether potential equity shares are dilutive or anti-dilutive.

Determination of whether a share is a Dilutive or Anti – Dilutive:

If	Then
Potential equity shares, on their conversion to equity shares would decrease EPS from continuing ordinary activities or increase loss per share from continuing ordinary activities	They are said to be dilutive
Potential equity shares, on their conversion to equity shares would increase EPS from continuing ordinary activities or decrease loss per share from continuing ordinary activities	They are said to be anti-dilutive.

In considering whether potential equity shares are dilutive or anti-dilutive, each issue or series of potential equity shares is considered separately rather than in aggregate.

The sequence in which potential equity shares are considered may affect whether or not they are dilutive.

Therefore, in order to maximize the dilution of basic EPS, each issue or series of potential equity shares is considered in sequence from the most dilutive to the least dilutive.

Determination of the sequence from most dilutive to least dilutive potential equity share:

For the purpose of determining the sequence from most dilutive to least dilutive potential equity shares, the earnings per incremental potential equity share is calculated.

IF earnings per incremental share	THEN potential equity share is
Is the least	Most dilutive.
Is maximum	Least dilutive.

- **Restatement:**

EPS of previous financial years is restated in certain cases in order to ensure proper comparability. If the number of equity or potential equity shares outstanding increases as a result of a bonus issue or share split or decreases as a result of a reverse share split (consolidation of shares), the calculation of basic and diluted EPS should be adjusted for all the periods presented.

If these changes occur after the balance sheet date but before the date on which the financial statements are approved by the board of directors, the per share calculations for those financial statements and any prior period financial statements presented should be based on the new number of shares. When per share calculations reflect such changes in the number of shares, that fact should be disclosed.

An enterprise does not restate diluted EPS of any prior period presented for changes in the assumptions used or for the conversion of potential equity shares into equity shares outstanding.

- **Disclosure Requirements:**

An enterprise should disclose the following:

1. Where the statement of profit and loss includes extraordinary items (AS 5), the enterprise should disclose basic and diluted EPS computed on the basis of earnings excluding extraordinary items (net of tax expense);
2.
 - a. The amounts used as the numerators in calculating basic and diluted EPS, and a reconciliation of those amounts to the net profit or loss for the period;
 - b. The weighted average number of equity shares used as the denominator in calculating basic and diluted EPS, and a reconciliation of these denominators to each other; and
 - c. The nominal value of shares along with the EPS figures.

An enterprise may wish to disclose more information than this Statement requires. Such information may help the users to evaluate the performance of the enterprise and may take the form of per share amounts for various components of net profit. Such disclosures are encouraged. However, when such amounts are disclosed, the denominators need to be calculated in accordance with this Statement in order to ensure the comparability of the per share amounts disclosed.

PRACTICAL QUESTIONS

1. 1st Jan. 2001, Number of shares outstanding = 1800,
31st May 2001- Fresh Issue for Cash = 600,
1st November 2001 – Buy Back of shares = 300.
Calculate the Weighted Average Outstanding Number of Shares as at 31/12/2001.

2. Accounting year January to December
1st January: Opening Balance 1800 shares.
31st October: Issue of 600 shares of Rs.10 each, Rs.5 paid up.
Calculate Weighted Average Outstanding Number of Shares.

3. Accounting year January to December
1st January: 2 lac Equity Shares of Rs.10 each fully paid up.
On 30th June: Fresh issue of Equity Share of Rs.5 each fully paid up, 2 lac
Calculate Weighted Average Outstanding Number of Shares.

4. In April, 2010, A Limited issued 18,00,000 Equity Shares of Rs.10 each. Rs.5 per share was called up on that date which was paid by all the shareholders. The remaining Rs.5 was called up on 01/09/2010. All the shareholders (except one having 3,60,000 shares) paid the sum in September 2010. The net profit for the year ended 31/03/2011 is Rs.33 lakhs after dividend on preference shares and dividend distribution tax of Rs.6.60 lakhs.
Compute the Basic EPS for the year ended 31st March 2011, as per AS 20.

5. Accounting year January to December
Net Profit for the year 2000 = Rs.18 lakhs
Net Profit for the year 2001 = Rs.60 lakhs
No. of Equity share outstanding till 30/09/2001 = 20 lakhs
Bonus issue on 01/10/2001 = 2 (new): 1 (old)
Calculate EPS for the year 2001 and adjusted EPS for the year 2000.

6. Accounting year January to December.
Net Profit for the year 2000 = Rs.11 lakhs
Net Profit for the year 2001 = Rs.15 lakhs
No. of shares outstanding prior to rights issue = 5 lakhs
Right issue: 1 (new): 5 (old)
Rights issue price = Rs.15
Last date of exercise rights = 1st March 2001
Fair value of Equity shares immediately prior to exercise of rights on 01/03/01 = Rs.21.
Calculate Basic EPS for the year 2001 and adjusted EPS for the year 2000.

7. Accounting year January to December

Net Profit = Rs.1 Crore

No. of equity shares outstanding = 50 lakhs

No. of 12% convertible debentures of Rs.100 each = 1 lac

(Each debenture is convertible into 10 Equity Share)

Tax rate applicable = 30%

Calculate basic & diluted EPS.

8. PAT – Rs.10 lakhs

9% Debentures of Rs.10 each – Rs.1,00,000.

Each debenture is converted into one equity share on 01/10/2012. Tax is Nil.

Number of equity shares on 01/04/2012 – 10,000 shares

Calculate Basic and Diluted EPS for year ended 31/03/2013.

9. XYZ Ltd. had issued 30,000, 15% Convertible debentures of Rs.100 each on 1st April, 2008.

The debentures are due for redemption at a premium of 5% and also conferred option to the debenture holders to convert 20% of their holding into equity shares (Nominal Value – Rs.10) at a price of Rs.15 per share. Debenture holders holding 2500 debentures did not exercise the option. Calculate the number of equity shares to be allotted to the debenture holders exercising the option to the maximum.

10. Accounting year January to December

Net profit attributable to Equity Shareholders = Rs.12 lakhs

No. of Equity Shares outstanding = 5 lakhs

Fair value of Equity Shares = Rs.20

Weighted average number of shares under the option = 1 lakh.

Exercise price of shares under option = Rs.15. Calculate Basic & Diluted EPS.

11. Accounting year January to December

Earnings attributable to Equity Shareholders = Rs.1 crore

Number of Equity Shares Outstanding = 20 lakhs

Fair value per share = Rs.75/-

Tax rate = 30%

Dividend tax = 10%

Potential Equity Share

1. Options: 1 Lakhs with exercise price of Rs.60

2. Convertible Pref. Shares: 8 lakhs shares entitled to a dividend of Rs.8 per share. Each Preference Share is convertible into 2 Equity shares.

3. 12% convertible Debentures: Nominal amount 10 crores; Face value = Rs.100.

Conversion ratio = 1:4.

Calculate basic & diluted EPS.

12. Mohur Ltd. has equity capital of Rs.40,00,000 consisting of fully paid equity shares of Rs.10 each. The net profit for the year 2004 - 05 was Rs.60,00,000. It has also issued 36,000, 10% convertible debentures of Rs.50 each. Each debenture is convertible into five equity shares. The tax rate applicable is 30%. Compute the diluted earnings.

13. Given below is the capital structure of S Ltd. as on 31st March, 2004.

Particulars	(Rs.in thousands)
Equity share capital (Shares of Rs.10 each)	40,000
Share premium	30,000
General reserve	40,000
Revaluation reserve	40,000
14% Fully convertible debentures	40,000

14% convertible debentures are of Rs.100 each and as per agreement those debentures will be converted into 5 equity shares (for each debenture). The company earned profit after tax amounting ('000) Rs.20,000 during 2003 - 2004.

You are required to calculate EPS of the company as well as the fully diluted EPS.

14. Given below is capital structure of PQR Ltd. for Calendar year 2002.

Particulars	No. of lacs	Amount Rs. in lacs
Equity shares outstanding on 1.1.2002	1,000	10,000
10% Convertibles : each to be converted into 8 equity shares	200	20,000
Net profit after tax		1,000
Basic EPS (Rs.)	1,000/1,000	1

Convertibles are assumed to be fully converted at the beginning of the year that will reduce basic EPS. Assume that tax rate is 38.5%. Compute diluted EPS

Also compute dilute EPS if interest rate in 12% and conversion into 6 Equity shares.