

# Provisions and Reserves

## MEANING OF KEY TERMS USED IN THE CHAPTER

1. <b>Provision</b>	Provision is an amount set aside by charging it to profit to meet a known liability, amount of which is not determined and is accounted by making best estimate.
2. <b>Reserve</b>	It is an amount set aside out of profit to meet an unknown contingency or to strengthen the financial position.
3. <b>Revenue Reserve</b>	It is the amount of reserve set aside out of revenue profit.
4. <b>Capital Reserve</b>	It is the amount of capital profit transferred to Capital Reserve.
5. <b>General Reserve</b>	It is the amount set aside out of profit not for any specific purpose.
6. <b>Specific Reserve</b>	It is the amount set aside out of profit for a specific purpose, say, Reserve for Expansion.
7. <b>Secret Reserve</b>	It is a reserve which is not disclosed in the Balance Sheet.
8. <b>Reserve Fund</b>	Amount of reserve invested outside the business, <i>i.e.</i> , reserves against which securities exist is termed as ' <b>Reserve Fund</b> '.

## CHAPTER SUMMARY

- **Provision** is made to meet known liability or contingent liability but the exact amount of which is not ascertained.
  - **Reserve** is an amount set aside out of profits to meet future contingencies or to strengthen the financial position of the enterprise. Examples of reserves are: General Reserve, Reserve for Expansion, Dividend Equalisation Reserve, etc.
  - **Reserves** may be (i) Revenue Reserves or (ii) Capital Reserves:
    - (i) *Revenue Reserves* are created out of revenue profits available for distribution as dividend. Examples are: General Reserve, Debentures Redemption Reserve, Dividend Equalisation Reserve, etc.
    - (ii) *Capital Reserves* are created out of capital profits. Examples are: Profit prior to incorporation, Profit on sale of fixed assets, etc.
  - **Secret Reserve:** The term 'Secret Reserve' is applied to a reserve the existence of which does not appear in the Balance Sheet. It is also called '**Hidden Reserve**'.
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