ACCOUNTENCY WORK BOOK

CLASS-XII

Part : A & B

Azadi Ka Amrit Mahotsav

Ek Tripura Shrestha Tripura

State Council of Educational Research and Training
Govt. of Tripura

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Class - XII

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রতন লাল নাথ
মন্ত্রী
শিক্ষা দপ্তর
ত্রিপুরা সরকার

বার্তা

শিক্ষার প্রকৃত বিকাশের জন্য, শিক্ষাকে যুগোপযোগী করে তোলার জন্য প্রয়োজন শিক্ষাসংক্রান্ত নিরন্তর গবেষণা। প্রয়োজন শিক্ষা সংশ্লিষ্ট সকলকে সময়ের সঙ্গো সঙ্গো প্রশিক্ষিত করা এবং প্রয়োজনীয় শিখন সামগ্রী, পাঠ্যক্রম ও পাঠ্যপুস্তকের বিকাশ সাধন করা। এস সি ই আর টি ত্রিপুরা রাজ্যের শিক্ষার বিকাশে এসব কাজ সুনামের সঙ্গো করে আসছে। শিক্ষার্থীর মানসিক, বৌদ্ধিক ও সামাজিক বিকাশের জন্য এস সি ই আর টি পাঠ্যক্রমকে আরো বিজ্ঞানসম্মত, নান্দনিক এবং কার্যকর করবার কাজ করে চলেছে। করা হচ্ছে সুনির্দিষ্ট পরিকল্পনার অধীনে।

এই পরিকল্পনার আওতায় পাঠ্যক্রম ও পাঠ্যপুস্তকের পাশাপাশি শিশুদের শিখন সক্ষমতা বৃদ্ধির জন্য তৈরি করা হয়েছে ওয়ার্ক বুক বা অনুশীলন পুস্তক। প্রসঙ্গাত উল্লেখ্য, ছাত্র-ছাত্রীদের সমস্যার সমাধানকে সহজতর করার লক্ষ্যে এবং তাদের শিখনকে আরো সহজ ও সাবলীল করার জন্য রাজ্য সরকার একটি উদ্যোগ গ্রহণ করেছে, যার নাম ‘প্রয়াস’। এই প্রকল্পের অধীনে এস সি ই আর টি এবং জেলা শিক্ষা আধিকারিকরা বিশিষ্ট শিক্ষকদের সহায়তা গ্রহণের মাধ্যমে প্রথম থেকে দ্বাদশ শ্রেণির ছাত্র-ছাত্রীদের জন্য ওয়ার্ক বুকগুলো সুচারুভাবে তৈরি করেছেন। ষষ্ঠ থেকে অষ্টম শ্রেণি পর্যন্ত বিজ্ঞান, গণিত, ইংরেজি, বাংলা ও সমাজবিদ্যার ওয়ার্ক বুক তৈরি হয়েছে। নবম দশম শ্রেণির জন্য হয়েছে গণিত, বিজ্ঞান, সমাজবিদ্যা, ইংরেজি ও বাংলা। একাদশ দ্বাদশ শ্রেণির ছাত্র-ছাত্রীদের জন্য ইংরেজি, বাংলা, হিসাবশাস্ত্র, পদার্থবিদ্যা, রসায়নবিদ্যা, অর্থনীতি এবং গণিত ইত্যাদি বিষয়ের জন্য তৈরি হয়েছে ওয়ার্ক বুক। এইসব ওয়ার্ক বুকের সাহায্যে ছাত্র-ছাত্রীরা জ্ঞানমূলক বিভিন্ন কার্য সম্পাদন করতে পারবে এবং তাদের চিন্তা প্রক্রিয়ার যে স্বাভাবিক ছন্দ রয়েছে, তাকে ব্যবহার করে বিভিন্ন সমস্যার সমাধান করতে পারবে। বাংলা ও ইংরেজি উভয় ভাষায় লিখিত এইসব অনুশীলন পুস্তক ছাত্র-ছাত্রীদের মধ্যে বিনামূল্যে বিতরণ করা হবে।

এই উদ্যোগে সকল শিক্ষার্থী অতিশয় উপকৃত হবে। আমার বিশ্বাস, আমাদের সকলের সক্রিয় এবং নিরলস অংশগ্রহণের মাধ্যমে ত্রিপুরার শিক্ষাজগতে একটি নতুন দিগন্তের উন্মেষ ঘটবে। ব্যক্তিগত ভাবে আমি চাই যথাযথ জ্ঞানের সঙ্গো সঙ্গো শিক্ষার্থীর সামগ্রিক বিকাশ ঘটুক এবং তার আলো রাজ্যের প্রতিটি কোণে ছড়িয়ে পড়ুক।

রতন লাল নাথ

(রতন লাল নাথ)

ACCOUNTANCY
Class-XII : Part- A & B

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Accountancy

Class-XII

Content

Part-A

Part-B

CHAPTER:1

Accounting for Not-For-Profit Organisation

Not for profit organisations refer to the organisations that are being used for the welfare of the society and are set up as charitable institutions which functions without profit motive. There main aim is to render services to its members and to the public. Such organisations include clubs, hospitals, libraries, schools, religious institutions, charitable institutions, literary societies etc.

Non- Profit organisations generaly do not have commercial owners and rely on funds from its members, contributors/ tax payers, programme revenues, fundraising events, Government aid and investment income.

The key points of Not-for –profit organisation is as follows–

i) Owners – None .

ii) Primary objective – provide services needed by society.

iii) Secondary objective – Ensure that the revenues are greater than its expenses so that the services provided can be maintained.

iv) Tax status – Exempt from income tax subject to approved by IRS(Internal Revenue Service)

v) Financial Statements required–

a) The Receipts and payments Account.

b) The Income and Expenditure Account.

c) The Balance sheet.

vi) Entity concept follow : Separate entity concept

Receipts and Payments A/c:

A Receipts and Payments Account is a summary of actual cash Receipts and Payments appearing in the cash book over a certain period (Cash and Bank Transactions). Receipts and payments A/c follow cash basis of Accounting.

Income and Expenditure A/c:

An Income and Expenditure account is the detailed summary of income and expense incurred by an organisation in a specific period /years. Income and Expenditure Account follow Accrual basis of Accounting. It is similar to the profit & loss Account of a profit seeking entity. It is prepared in the same manner in which a Trading and profit and loss Account is prepared in case of trading organisations.

Hence, all Expenses and Losses of a revenue nature are recorded on its debit side, while all income and gains of a revenue nature are recorded in credit side. These Accounts primarily serve to find out surplus or deficit balance of an not for profit organisation, taking both current income and expenses into account.

If credit side of this account is greater than debit side is known as surplus (excess of Income over Expenditure) and on the contrary, it is known as deficit (excess of Expenditure over Income)

Balance Sheet :

The Balance Sheet of a Not-for-profit organisation is prepared in the same manner as like business enterprises. The assets of these organisations are recorded on the right side and liabilities on the left side

It contains only capital items. i. e. Assets, Liabilities, Capital and Special Funds.

Incase of of Not for Profit organisations there is no Capital A/C. The difference between assets and liabilities is known by the name "Capital Fund" or "General Fund".

Capital Receipts:

These receipts have a nature of non-recurrence. Consider that, they are posted in the liabilities side of the balance sheet . They include- Life Membership Fees, Legacies, Sale of Fixed Assets etc.

Revenue Receipts:

Revenue receipts are those receipts that are received by a organisation as result of normal, routine activities. These items are appering in the debit side of Receipts and Payments A/c. Such as- subscriptions, Rent Received, Interest Received, Entrance Fees, Sale of old Newspaper etc.

Capital Expenditure:

These expenditure are generally non- recurrence in nature. Capital expenditure deals with long term items to boost the firms proficiency. Capital expenditure (CAPEX) is incurred to purchase long term assets like –Plant, machinery, building, equipment ,furniture ,fixtures etc.

Revenue Expenditure: Revenue expenditure is that part of organisations expenditure that does not result the creation of assets. payment of salaries, wages, rent, newspaper bill etc. fall in this category as revenue expenditure examples.

Certain items and Accounting Treatment- Regarding			
Sl.No.	**Item**	**Nature**	**Accounting Treatment**
1.	Donations : General Specific	 Revenue Receipts Capital Receipts	Credit side of Income and Expenditure A/c. Liability side of Balance sheet.
2.	Legacy	Capital Receipts	Liability side of Balance sheet.
3.	Life Membership Fees	Capital Receipts	Liability side of Balance sheet.
4.	Entrance Fees Or Admission Fees (In the absence of any instruction)	Revenue Receipts	Credit side of Income and Expenditure Account.

5.	Sale of old sports Materials and old Newspapers/Periodials	Revenue Receipts	Credit side of Income and Expenditure Account.
6.	Purchase of fixed Assets (Furniture, Land, Building, equipment etc.)	Capital Expenditure	Assets side of Balance Sheet
7.	Payment of Honorarium	Revenue Expenditure	Debit side of Income and Expenditure Account.
8.	Subscription	Revenue Receipts	Credit side of Income and Expenditure Account.
9.	Special/specific Fund	Capital Receipt	Liability side of Balance sheet.
10.	Sale of old Assets : Loss Profit	 Non- Operating Non- Operating	 Debit side of Income and Expenditure Account. Credit side of Income and Expenditure Account.
11.	Endowment Fund	Capital Receipts	Liability side of Balance sheet.
12.	Purchase of consumable Items	Revenue Expenditure	Debit side of Income and Expenditure Account.

For preparation of Income and Expenditure Account, follow the necessary steps as given below-

- Include all items of Revenue Receipts and Expenses on the respective side of the account for the current reporting year only.
- Ensure that no items of capital incomes and expenses are included in income and expenditure account.
- Entry for necessary adjustment is to be made against necessary items.
- Further items included in Receipts and Payments Account, depreciation, provisions and profit/Loss on sale of assets will have to be added in this account.
- Finally, after putting down all items of revenue and expenses, you will get a balance. The resulting balance then reveal the surplus or deficit for the period.

EXERCISE

(A) State whether the following statements are True or False: (Marks : 1)

1) Receipt and payment Account is a summary of all Capital Receipts and Payments.

Answer:——————————————————————

2) A credit balance of Income and Expenditure A/C denotes excess of Expenditure over Income.

Answer:——————————————————————

3) A Public Library is a non profit seeking entity.

Answer:——————————————————————

4) Donations received for a specific purposes are always capitalized.

Answer:——————————————————————

5) Receipts and Payments A/c is a Nominal A/c.

Answer :——————————————————————

6) Excess of Income over Expenditure is always added to capital fund.

Answer:——————————————————————

7) Non-cash items are shown in Income and Expenditure A/c.

Answer:——————————————————————

8) Receipts from sale of old Assets are treated as Income.

Answer:——————————————————————

9) Income is shown in the credit side of Income and Expenditure A/c.

Answer:——————————————————————

10) Receipts and payments A/c is equivalent to profit and loss A/c.

Answer:——————————————————————

(B) Fill in the blanks with appropriate word /words : (Marks : 1)

1) Donation received for a specific purpose is shown in————.
2) The regular source of income of a club is ————.
3) Receipts and Payments Account is a ———— of cash book.
4) Income and Expenditure Account is prepared on ———— basis.
5) Receipts and Payments Account is prepared on ———— basis.
6) The sale of old newspaper is of ———— nature.
7) The sale of old equipments is of ———— nature.
8) General Donation is shown in ————.
9) Not for profit organisation is a ———— legal entity.
10) An NPO does not have ———— like proprietorship, partnership and joint stock.

11) A credit balance of Income and Expenditure Account is known as ——————.
12) Subscription received in advance is shown in ——————side of closing Balance sheet.
13) Endowment fund is shown in —————— side of closing Balance sheet.
14) Sale of sports material is a —————— receipts.
15) Closing stock of stationery is shown in ——————.

(C) Answer the following MCQ'S/VSA Type question : (Marks : 1)

1) Receipts and payments A/c is a ————————————.

i)Nominal A/c ii) Real A/c ii) Personal A/c iv) None of these

Answer:——————————————————————————————

2) Subscription received but not yet earned is considered as a——————————

i) Asset ii) liability iii) Income iv) Expenditure.

Answer:——————————————————————————————

1) Give two main sources of Income for Not-for –profit organisations.

Answer:——————————————————————————————

2) What is membership subscription?

Answer:—————————————————————————

3) Which of the following financial statements is not prepared by the Not- for-profit organisation?

i)Profit and Loss A/c. ii) Income and expenditure A/c

iii) Receipts and payments A/c iv) Balance sheet.

Answer:—————————————————————————————

4) Receipts and payments A/c generally shows:-

i)A debit balance. ii)A credit Balance.

iii) Surplus or Deficit. iv) Capital fund.

Answer:————————————————————————————

7) Out of the following items which one is shown in the Receipts and payments A/c.

i)Outstanding salary ii) Depreciation.

iii)Life membership fees iv) Accrued subscription.

Answer:———————————————————————————————

8) Donation Received for a special purpose is a:

i)Liability ii) Revenue Receipt iii) Capital Receipt iv) None of these.

Answer:———————————————————————————————

9) What is a Not-for-profit organisations?

Answer:——————————————————————————————

10) In Case of specific fund is maintained the expenses exceeding the amount of the funds should be recorded on:

i) Liabilities side of the Balance sheet.

ii) Debit side of the Income and Expenditure Account.

iii) Credit side of the Income and Expenditure Account.

iv) Assets side of the Balance sheet.

Answer:—————————————————————————

11) Balance of Income and expenditure Account:

i)Cash in hand ii) Capital fund iii) Net profit

iv)Excess of Income over expenditure or vice-versa.

Answer:—————————————————————————

12) Capital fund of a Not –for-profit organisation in the beginning of the accounting year is ascertained by preparing-

i) Receipts and payments A/c.

ii) Income and Expenditure A/c.

iii) Closing Balance sheet.

iv) Opening Balance sheet.

Answer:—————————————————————————

13) Property received as a result of the will of deceased person is called:-

i) Honorarium ii) Legacy iii) Donation iv) Subscription.

Answer:—————————————————————————

14) Which of the following is non-profitable organisation?

i) Airtel ii) Tata steel iii) ultratech cement iv) Abhoy mission.

15) Describe capital Receipt?

Answer:—————————————————————————

16) What is the capital of a Non- profit organisation known as?

Answer:—————————————————————————

17) Income and Expenditure A/c records Transaction of

i) Revenue nature only ii) Capital nature only.

iii) Both Revenue and capital. iv) None of Them.

Answer : —————————————————————————

18) Not –for-profit organisation have some distinguishing features from that of profit organisations. State any one of them.

Answer : —————————————————————————

19) A non profit organisations received Rs. 10,000 as the entrance fee of a New member. If 20% of the fee has to be capitalized, what is the amount of fee needs to be shown in the Income and Expenditure A/c.

Answer : ——————————————————————————————

20) Mumbai Cricket Association gives following details in respect of match fund; Opening balance of match fund Rs. 50,000, Receipts from match Rs. 20,000, match Expenses Rs. 18,000. What amount of match fund will be shown in the balance sheet?

i) Rs. 48,000 ii) Rs. 52,000

iii) Rs. 12,000 iv) None of Them.

21) Donation received as a special purpose:

i) Should be credited to Income and Expenditure A/c.

ii) Should be debited to Income and Expenditure A/c.

iii) Should be credited to separate A/c and shown in the Balance sheet.

iv) Should not be recorded at all.

Answer : ——————————————————————————————

22) The amount of "Entrance fees" received by a not-for-profit organisations (If is received regularly) is shown in which of the following?

i) Liability side of Balance sheet ii) Assets side of Balance sheet.

iii) Debit side of Income and Expenditure A/c.

iv) Credit side of Income and Expenditure A/c.

Answer : ——————————————————————————————

23) What is endowment fund?

Answer :——————————————————————————————

24) Not for profit organisations prepare——

i) Trading Account.

ii) Trading and profit & loss Account.

iii) Income and Expenditure Account.

iv) All of the above.

Answer:——————————————————————————————

25) Source of Income for a Not for profit organisation is

i) Life member ship subscription. ii) Donation

iii) Subscription iv) All of the above.

26) Subscription received in advance during the current year is:

i) An Income ii) An asset. iii) A liability iv) None of these.

27) Amount received from sale of grass by a club is treated as:

i) Capital Receipt. ii) Revenue receipt.

iii) Asset iv) Earned Income.

Answer:——————————————————————————————————————

28) Which of the following is a Not For Profit Organisation.

i) Sports club ii) Hospitals

iii) Schools iv) All of the above.

29) When sports expenses are less than the amount of sports fund, the items are show in :

i) Receipts and payments A/c. ii) Balance sheet.

iii) Income and expenditure A/c. iv) None of the above.

Answer:——————————————————————————————————

30) Life member fee is:-

i) An asset. ii) A liability.

iii) An expenses. Iv) None of the above.

Answer:——————————————————————————————————

Very short Answer Question **(Marks : 3)**

1) Give three essential features of Receipts and payments Account.

Answer:——————————————————————————————————————

2) Give three essential features of Income and Expenditure Account.

Answer:——————————————————————————————————————

3) Explain any two of the following terms:-

a) Capital fund b) Legacy c) Subscription.

Answer:——————————————————————————————————————

4) How will you treat the following items while preparing Income and Expenditure A/c and Balance sheet of Not-For –Profit organisations?

a) Investment purchase b) Donation for building c) Sale of Fixed Assets. d) Annual subscription e) Life membership fee

Answer:——————————————————————————————————————

5) From the following information ,calculate the amount charged to Income and Expenditure A/c for sports material consumed for the year 2019-20.

Particulars	Amount (Rs.)
Creditors for sports materials(01.04.2019)	60,000
Creditors for sports materials(31.03.2020)	40,000

Stock of sports Materials (01.04.2019)	1,00,000
Amount paid to Creditors during the year 2019-20	3,80,000
Sports Material sold during the year 2019-20 (having book value 80,000).	62,000
Cash purchase of sports Materials during the year 2019-20	2,70,000

Answer:———————————————————————————————

6) From the following information, calculate the amount of sports materials that will be debited to the Income and expenditure Account of singhali sports club for the year ending 31.03.2020.

Particulars	01-04-2019 (Rs.)	31-03-2020 (Rs.)
Stock of sports Materials	1,60,000	1,20,000
Creditors for sports materials	60,000	42,000
Advance paid for sports materials	30,000	40,000

Additional information:-

Cash purchase of sports Materials during the year was Rs. 4,00,000. An amount of Rs. 2,50,000 were paid to creditors for spots material during the year.

Answer:———————————————————————————————

(7) What is capital fund ? How it is calculated?

Answer:———————————————————————————————

(8) "Income and Expenditure account of a Not- for- profit organisation is akin to profit and loss account of a business concern"- Explain the statement.

Answer:———————————————————————————————

(9) How the following items were shown in the accounts of a Not –for – profit organisation?

Particulars	Amount (Rs.)
Tournament Fund	1,00,000
Tournament Expenses	60,000
Receipts from Tournament	30,000

Answer:———————————————————————————————

(10) From the following information, prepare a Receipts and Payments Account for the year ending on 31st December,2020:

Particulars	Amount(Rs)
Opening Balance of cash in hand and at bank	28,000
Subscription Received (Including Rs 18,000 for 2019)	1,05,000
Entrance fees	16,000
Furniture purchased	14,000
Repairs and Maintenance Expenses	21,000
Locker Rent	32,000
Interest on Investment	6,000
Life membership fees	12,000
Insurance premium paid	18,000

Answer:——————————————————————

(11) Calculate the amount of subscription to be credited to Income and Expenditure Account for the year ended 31st March., 2020 in the books of people's health club.

Particulars	Amount(Rs)
Subscription	
2018-19	4,000
2019-20	1,80,000
2020-21	12,000

The club has 500 members each paying Rs 400/- as annual subscription. Subscription outstanding as on 31st march,2019 are Rs 8,000.

Answer:——————————————————————

(12) On the basis of the following information, Calculate the amount debited to stationery A/c in the Income and Expenditure Account for the year ending on March 31,2020.

Particulars	Amount(Rs)
Stock of stationery as on 1st April, 2019	30,000
Amount paid to creditors for stationery during the year 2019-20	72,000
Creditors for stationery on 1st April ,2019	22,000
Stock of stationery on 31st March,2020	18,000
Creditors for stationery on 31st March,2020	16,000

Answer:——————————————————————

(13) Show the following information in financial statements of a Not-for- profit organisation in the books of jewel sports club:

Details	Amount (Rs)
Match fund `	6,00,000
Sale of match Tickets	4,60,000
Match Expenses	10,20,000
Donation for match fund	3,80,000

Answer:————————————————————

Long Answer Type Questions **(Each Question Carries Marks 6)**

(1) Distinguish between Receipts and payments A/c and Income and Expenditure Account? (2+4)
Answer:————————————————————

(2) What is Not –for- profit organisation? State the characteristics of Not-for-profit organisation? (2+4)
Answer:————————————————————

(3) What is Receipts and payments A/c ? Explain the sailent features of Receipts and payments Account. (2+4)
Answer:————————————————————

(4) What is Income and expenditure A/c? What are the necessary steps for preparation of Income and Expenditure Account? (2+4)
Answer:————————————————————

(5) What is Balance sheet? How to prepare the balance sheet of a Not-for-profit organisation. (2+4)
Answer:————————————————————

(6) Following is the Receipts and Payments account of young star sports club, TN for the year ending on 31st March 2020.

Receipts	Amount(Rs)	Payments	Amount(Rs)
To, Balance B/D	8,600	By, Rent	24,000
To, Subscriptions	82,000	By, Sundry expenses	7,000
To, Donation	10,000	By, Equipments purchased	30,000
		By, Match Expenses	3,600
To, Match fund	8,000		
To, Donation for club House building	62,000	By, Salaries	9,600
		By, sundry expenses	6,800
To, Interest	1,200	By, Newspaper	1,200
To, sale of Grass	2,000	By Furniture purchased	32,000
To, Miscellaneous Receipts	3,600	By Balance C/D	63,200
	1,77,400		1,77,400

Subscription outstanding on31st March, 2019 were Rs 4,800 and 31st March, 2020 were Rs 8,000. Salaries outstanding on 31st march ,2019 and 31st March, 2020 were Rs 3,200 and Rs 6,800 respectively.

Prepare Income and expenditure account for the year ended 31st March, 2020 after depreciation of furniture and equipments by 10% & 5% respectively.

(7) Following is the Receipts and payments Account of the women's welfare society for the year ended December 31,2020.

Receipts	Amount (Rs)	Payments	Amount (Rs)
To, Balance B/D	2,270	By, Electric charges	1,480
To, Subscriptions	32,500	By, Lecturers fee	730
To, Endowment fund	3,250		
To, Donation	2,500	By, Rent	6,000
To, Sale of old furniture		By, Salary	1,300
(Book value Rs1000)	750		
To, profit from		By, Legal fee	1,870
Eentertainment	7,250	By, printing & Stationery	1,050
To, Interest	350	By, Books	6,500
		By, Furniture purchased	8,600
		By Treavelling expenses	600
		By office expenses	3,200
		By Balance C/D	17,540
	48,870		48,870

You are required to prepare Income and Expenditure account after considering the following adjustments:

i) Subscription still to be received are Rs 750 but subscription include Rs 500 for the year 2021.

ii) In the begaining of the year the society has building ' 20,000 and Furniture Rs 3000 and Books Rs.2000.

iii) Provide Depreciation on Furniture @5% (Including Purchase), books @ 10% and building @5%.

(8) Following is the Receipts and payments Account of Magnet Cricket club for the year ended on 31st March,2020.

Receipts	Amount (Rs)	Payments	Amount (Rs)
To, Balance B/D.	4,400	By, Rent	15,500
To, Subscription	46,100	By, Printing and	
		Stationery	6,800

To, Tournament fund	12,000		
To, Receipts from Advertisement	5,200	By, Salaries	16,200
To, Interest	1,500	By, Expenses on charity show	18,100
To, Entrance fees	1,000	By, Tournament Expenses	7,500
To, Donation	6,000	By, 10% Investment Purchased	10,000
To, Donation for Building	20,000	By, Furniture	6,000
		By, Balance C/D	16,100
	96,200		**96,200**

Subscription outstanding on 31st March, 2019 were Rs 4,500 and on 31st march, 2020 were Rs 6,000.

Rent outstanding at the begining of the year was Rs 1,000 and at the end was Rs 1,500.

Furniture was purchased on 01.07.2019. Provide depreciation @ 10% P.a

On 1st April,2019, The club had furniture valued Rs 8,000 and 10% Investments valued Rs 15,000.

Prepare Income and expenditure A/c for the year ended 31st march, 2020 and a Balance sheet as at that date.

(9) From the following Receipts and payments A/c of Jupiter club for the year ended on 31st March, 2020 prepare a Income and Expenditure Account on that date.

Receipts	Amount (Rs)	Payments	Amount(Rs)
To, Balance B/D	32,000	By, Furniture	60,000
To, Donations	42,000	By, Equipments	62,000
To, Interest on Investments	11,000	By, Salaries	12,000
To, proceeds from charity show	10,000	By, Treavelling expenses	10,000
To, Subscriptions			
2018-19 1,600		By, Stationery	10,000
2019-20 60,000			

2020-21 5,000	66,600		
		By, Balance C/D	13,400
To, sale of Equipments (book value Rs 6000)	5,800		
	1,67,400		1,67,400

Additional Information:-

i) Furniture and equipments were purchased in 01-10-19. Depreciation @ 10% p.a was to be provided on furniture and equipments.

ii) Subscription in arrear for the year 2019-20 were Rs 2000.

iii) Salary due but not paid during the year was Rs 6000.

Answer: ——————————————————————

(10) From the following Receipts and payments A/c of Rajdhani club for the year ended on 31st march, 2020.

Receipts	Amounts(Rs)	Payments	Amount(Rs)
To, balance B/D	65,000	By, Medicines	10,000
To, Subscription	68,500	By, Doctors and coaches honorarium	30,500
		By, Medical equipment	20,000
To, Entrance fees	45,000		
		By, General expenses	8,000
To, Life membership Fees	30,000	By, Furniture	30,000
To, Donation for Tournament fund	20,000	By, Newspaper	8,000
		By, Rent, Rates and Taxes	5,000
To, Sale of Furniture (Book value Rs 15000)	5,000	By, Tournament expenses	60,000
To, Miscellaneous Receipts	15,000	By, Balance C/D	77,000
	2,48,500		2,48,500

Additional Information:

Following opening balances are appeared in the books as on 01st April, 2019-

i) Tournament fund -Rs 15000

ii) Furniture Rs 30,000

iii) Medical equipment Rs 1,20,000

iv) Outstanding subscription for the year was Rs 8000 and advance subscription received (for 2020-21) during the year was Rs 5000.

v) During the year 2019-20, Depreciation on medical equipment was Rs 25,000.

vi) There were 600 members each paying an annual subscription of Rs 100.

Prepare Income and Expenditure A/c.

(11) From the following information of Mahabir Sports club, prepare Income and Expenditure A/c for the year ended on 31st December, 2019.

Receipts and payments A/c

For the year ending on 31st December, 2019

Receipts	Amount(Rs)	Payments	Amount(Rs)
To, Balance B/D	40,000	By, Furniture	1,10,000
To, Interest on Investments	2,400	By, Salaries	64,500
To, Donations	27,000	By, Equipments	20,000
To, Subscriptions	3,00,000	By, Miscellaneous Expenses	52,000
		By, Telephone charges	10,000
		By, Books	6,000
To, Rent Received	50,000	By, Printing and stationery	21,000
To, Entrance fees	18,000	By, 6% Investments (on 01.05.2019)	1,00,000
To, sale of Old News paper	2,600	By, Balance C/D	56,500
	4,40,000		4,40,000

Addition information :

Subscription received included Rs 15,000 for 2018. Subscription not received during the year were Rs20,000. Salary outstanding during the year 2019 were Rs 8000 and Rent Receivable was Rs 2000.

Opening stock of Printing and stationery was Rs 12000, where as closing stock was Rs 15000. Prepare income and expenditure A/c for the year ending on 31st December, 2019.

(12) From the following receipts and payments account of Arambag sports club for the year ended 31st March,2020 prepare Income and Expenditure Account of the club and a Balance sheet as on that date.

Receipts	Amount(Rs)	Payments	Amount(Rs)
To, Balance B/D	5,000	By, Salary	9,000
To, Subscriptions	30,000	By, Furniture	14,000
To, Entrance fee	4,000		
		By, Office expenses	11,000
To, Tournament fund	15,000	By, Tournament Expenses	21,000
To, sale of old Newspapers	2,000	By, Sports equipment	20,000
To, Legacy	18,000	By, Balance C/D	16,000
To, Life membership fees	17,000		
	91,000		91,000

Other Information:

Subscription outstanding on 31.03.2020 were Rs 40000 and on 31.03.2019 subscription outstanding was Rs 3000. Salary outstanding on 31.03.2020 was Rs 2000.

On 01.04.2019 The club had building Rs 80,000, furniture Rs 20,000, 10% Investment Rs 45,000 and sports equipments Rs 25000. Depreciation charge on These items including purchase was 10 % (except Investment).

:Answer key:

A. True / False:

1. False 2. False 3.True 4. True 5. False 6.True
7. True 8. False 9. True 10. False

B. Fill in The blanks:

1. Balance Sheet 2. Subscription 3. Summary 4. Accrual 5. Cash 6. Revenue

7. Capital 8. Income and Expenditure Account. 9. Separate 10. Capital

11. Surplus 12. Liability. 13. Liability. 14. Revenue 15. Closing Balance

C. MCQ/VSA TYPE QUESTIONS:

1. ii) Real A/c 2. ii) Liability 3. Subscription, Donation, Legacies etc. 4. See Tex book

5. i) Profit and Loss A/c 6.i) A Debit Balance . 7.iii) Life Membership fees 8.iii) Capital Receipt .

9. See Text book. 10.ii) Debit side of the Income and Expenditure Account

11. iv) Excess of Income over Expenditure or vice versa. 12.iv) Opening Balance sheet .

13. Legacy 14. Iv) Abhoy mission. 15. See work book. 16. Capital fund or General fund.

17. i) Revenue nature only.

18. To provide service for welfare.

1 9. 1 8000

20. ii) 1 52,000

21. iii) Should be credited to separate account and shown in the Balance sheet. 22.iv) Credit side of Income and Expenditure A/c. 23. An endowment fund is a financial asset, typically held by a Non-profit organization, which contains capital investment. 24.iii) Income and Expenditure Account 25. Iv) All of the above 26.iii) A liability 27.ii) Revenue Receipt. 28. Iv) All of the above 29. Ii) Balance sheet 30. Ii) A liability.

Very short answer questions : (3 marks)

5. Rs 6,50,000 6. Rs 6,62,000 9. Rs 70,000(In liability side of Balance sheet)

10. Rs 1,46,000(closing balance of cash in hand and at bank) 11. Rs 2,00,000.

12. Rs 78,000 13. Rs 4,20,00

Long answer type questions : (6 Marks)

6. Surplus (Excess of Income over Expenditure) Rs 49,800
7. Surplus (Excess of Income over Expenditure) Rs 24,590.
8. Opening capital fund Rs 30,900; surplus Rs 3950; closing Balance sheet total Rs 60,850
9. Surplus (Excess of Income over Expenditure) Rs 80,700.
10. Surplus Rs 8500
11. Surplus Rs 256100
12. Opening capital fund Rs 178000; Deficit Rs 2400; closing Balance sheet total Rs 2,12,600.

CHAPTER-2

Accounting for Partnership: Basic Concepts

Business can be structured into different forms like sole proprietorship, partnership firm or a company. Every type of business forms has its own share of limitations. As a business expands, there is a constraint of capital and more risk is associated.

Partnership is based on mutual agreement and in a partnership; they agree to share capital, profits and loss of the business. The persons who have entered into the partnership are known as partners.

Partnership is defined as per the Indian Partnership Act, 1932 as "the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all".

Features of a Partnership:-

The following features of a partnership can be discussed :

- It is an organization of two or more persons.
- A partnership business is established by an agreement.
- Partners have to share the profit and loss of the business.
- Business must be conducted legally in order to make profit.
- Partnership business must be carried by all or any one on behalf of all. Mutual and implied agency forms the basis of partnership.

Partnership Deed:-

Partnership deed is a partnership agreement between the partners of the firm which outlines the terms and conditions of the partnership between the partners. The intention of a partnership deed is to provide clear understanding of the roles of each partner, which ensures smooth running of the operations of the firm. Partnership agreement may be oral or written. It is not necessary to outline partnership agreement in writing under the Partnership Act, 1932. Still, written partnership deed is desirable than oral agreement as it helps in avoiding disputes and misunderstandings among the partners. Also, it helps in settling disputes (as the case may be) among the partners, as written partnership deed can be referred to anytime. If written partnership deed is duly signed and registered under Partnership Act, then it can be used as evidence in the court of law.

Rules applicable in the absence of Partnership Deed:

Accounting Rules Applicable in the Absence of Partnership Deed

(i) Sharing of profits and losses — Equally.

(ii) Interest on capital — Not allowed.

(iii) Remuneration or salary to the partners- Not allowed.

(iv) Interest on partners' loan — Allowed @ 6% per annum.

(v) Interest on drawings — Not charged.

Profit and Loss Appropriation Account (Distribution of Profits among Partners):

Transactions of the partnership firm are recorded according to the principles of Double-Entry Book keeping system and as in the case of a sole proprietorship concern a partnership firm will also prepare Trading Account, Profit & Loss Account and Balance Sheet at the end of every year. The only difference between accounting of a sole trader and partnership firm is that the profits of the partnership firm are divided among the partners.

A Profit and Loss Appropriation Account is prepared to show the distribution of profits among partners as per the provision of Partnership Deed (or as per the provision of Indian Partnership Act, 1932 in the absence of Partnership Deed). It is an extension of profit and Loss Account. It is nominal account. It records entries for interest on Capital, Interest on Drawings, Salary to the partner, and Division of profits among the partners.

Partner's Capital Accounts:-

It is an account which represents the partners' concern in the business.

In case of partnership business, a separate capital account is maintained for each partner. The capital accounts of partners may be maintained by any of the following two methods.

1. Fixed Capital Accounts
2. Fluctuating Capital Accounts

I. Fixed Capital Accounts:-

Under this method the original capitals invested by the partners remain constant, unless additional capital is introduced by an agreement. All entries relating to drawings, interest on capitals, interest on drawings, salary to partner, share of profits/losses are made in separate account which is called as Current Account. Thus the following two accounts are maintained when capitals are fixed.

(i) Capital Account

This account will always show a credit balance. Balance of Capital account remains fixed, it does not change every year that is why it is called fixed capital method and only the following two transactions are recorded in the Fixed Capital Accounts:

Additional Capital Introduced

Capital Withdrawn or Drawings out of Capital only

(ii) Current Account:-

The Current account may show a debit or credit balance. All the usual adjustments such as interest on capital, partner's salary/commission, drawings (out of profits), interest on drawings and share in profits or losses etc. are recorded in this account.All the Current Year's adjustments are recorded in this account, that is why it is called Current account,

Note:

i. Debit balance of Current Account is shown in Assets side of Balance Sheet.
ii. Credits balance of Current Account A/c is shown in Liabilities side of balance Sheet.
iii. Balance of Fixed Capital Accounts are always shown in Liabilities side of Balance Sheet as it will be always be credit balance.

2. **Fluctuating Capital Accounts:-**

In this method only one account i.e., Capital Account of each and every partner is prepared and all the adjustment such as interest on capital, interest on drawings etc, are recorded in this account.Under this method, Capital account may show a debit or credit balance and the balance of this account changes frequently from time to time, therefore it is called Fluctuating Capital Account. In this method the capitals are not fixed. In the absence of information, the Capital Accounts should be prepared by this method.

ACCOUNTING TREATMENT OF SOME SPECIFIC ITEMS:-

1. **INTEREST ON CAPITAL:-**

Interest on partners' capital will be allowed only when it has been particularly mentioned in the partnership deed. If interest on capital is to be allowed as per the agreement, it should be calculated with respect to the time, rate of interest and the amount of capital. Interest on Capital can be treated as either:

A. An Appropriation of profit; or

B. A charge against profit.

A. **Interest on Capital: An Appropriation of Profits:**

In case of Losses	**Interest on capital is NOT ALLOWED**
In cases of Sufficient Profits	**Interest on capital is ALLOWED IN FULL**
In case of Insufficient Profits	**Interest will be restricted to the amount of profit. Hence, profit will be distributed in the ratio of interest on capital of each partner.**

B. Interest on Capital: As a Charge against Profits:

Interest on Capital is always allowed in full irrespective of amount of profits & losses.

Note:

Interest on Capital is always calculated on the OPENING CAPITAL.

If Opening Capital is not given in the question, it should be ascertained as follows:

Particulars	**(Rs)**
Capital at the End	------------
Add: 1. Drawings xxxxxx	
2. Interest on Drawings xxxxxx	
3. Losses during the year xxx	
Less: 1. Additional Capital Introduced (xxxxxx)	
2. Profits during the year (xxxxxx)	
3. Any salary/commission received (xxxx)	
Opening Capital (xxx)	

2. Interest on Drawings:-

Interest on drawings can be computed by following either direct method or product method. Also if the partners withdraw fixed amount at fixed time interval, interest on drawings may be calculated on the basis of the average period method. Based on the dates of drawings and the amount of drawings, different methods can be followed for calculating interest on drawings

(i) Direct method

Interest is calculated on drawings for the period from the date of drawings to the date of closing date of the accounting year. The following formula is used to compute the interest on drawings:

Interest on drawings = Amount of drawings x Rate of interest x Period of interest

Period of interest refers to the period from the date of drawings to the closing date of the accounting year. This method is suitable when different amounts are withdrawn at different time intervals.

(ii) Product method

Under product method, interest is calculated on the total of the products, that is, the product of amount of drawings and the period for which the amount remained withdrawn. If the product is calculated in terms of months, then interest is calculated on the total of products at the rate per month. If the product is calculated in terms of days, then interest is calculated on the total of products at the rate per day. This method can be used in all situations as an alternative to direct method.

The procedure for calculating interest on drawings under product method is as follows:

a) Multiply each amount withdrawn by the relevant period (in months) to find out the individual product.

b) Find out the sum of all the individual products.

c) Calculate interest at the prescribed rate for one month by using the following formula.

Interest on drawings = Sum of products x Rate of interest p.a. x 1/12

(iii) Average period method

If the partners withdraw fixed amount at fixed time interval, interest on drawings may be calculated on the basis of the average period. Fixed time interval refers to withdrawal made monthly, quarterly, and half yearly, once in 2 months and once in 4 months. The following formula may be used to calculate interest on drawings:

$$\textbf{Interest on Drawings} = \left[\begin{array}{c}\textbf{Total amount of}\\ \textbf{Drawings during the year}\end{array}\right] \times \left[\begin{array}{c}\textbf{Rate of Interest}\\ \textbf{Per Annum}\end{array}\right] \times \left[\frac{\text{Average Period}}{12}\right]$$

$$\textbf{Average Period} = \frac{\left[\begin{array}{c}\textbf{Number of months from the date of}\\ \textbf{first withrawl to the end of the Year}\end{array}\right] + \left[\begin{array}{c}\textbf{Number of months from the date}\\ \textbf{of last withdrawl to the end of Year}\end{array}\right]}{2}$$

Average period is computed as follows:

The following table shows the average period in months for withdrawal made at the beginning, in the middle and at the end of every month, quarter and half-year of the year.

Frequency of withdrawl	Average period (in months)		
	Time of withdrawl		
	At the begining	In the middle	At the end
Monthly	$\frac{(12+1)}{2}=6.5$	$\frac{11.5+0.5}{2}=6$	$\frac{(11+0)}{2}=5.5$
Quarterly	$\frac{(12+3)}{2}=7.5$	$\frac{(10.5+1.5)}{2}=6$	$\frac{(9+0)}{2}=4.5$
Half-Yearly	$\frac{(12+6)}{2}=9$	$\frac{(9+3)}{2}=6$	$\frac{(6+0)}{2}=3$

EXERCISE

A. Choose the correct answer: Marks : 1

1. To commence a partnership business, what should be the minimum number of partners?
   A) 2 B) 4 C) 10 D) 20
2. What type of agreement is used to constitute a partnership business?
   A) Written agreement B) Oral agreement
   C) Written or oral agreement D) None of them
3. In partnership business, partners' liabilities are
   A) Unlimited B) Limited
   C) Limited to the capital of the business D) Both A and B
4. What is the partnership written agreement known as-?
   A) Agreement B) Partnership contract
   C) Partnership deed D) Partnership Act
5. In absence of partnership agreement, what will be the percentage of profit sharing ratio between partners?
   A) It will depend on partner's capital B) Equal
   C) It will depend on the experience of a partner D) Unequal

6. Which is not a feature of a partnership business?
   A) Limited life B) Limited liability
   C) Ease of formation D) Mutual agency
7. In which kind of partnership, one partner has unlimited liability and other partner have limited liability?
   A) General partnership B) Limited partnership
   C) Partnership-at-will D) Particular partnership
8. Which types of partnership have no agreement in terms of the duration of partnership?
   A) Partnership-at-will B) General partnership
   C) Limited partnership D) Particular partnership
9. What time would be considered if equal monthly amount is drawn as drawings at the beginning of each month?
   A) 7 months B) 6 months
   C) 5 months D) 6.5 months
10. Fluctuating capital account is credited with:
   A) Interest on capital B) Profit of the year
   C) Remuneration of partners D) All of these
I1. Interest on drawings of the Partners is a:
   A) Loss to business B) Profit to business
   C) Profit to partners D) Loss to Bank
12. Partner's salary is debited to:
   A) Trading Account B) Profit and Loss Account
   C) Profit & Loss Appropriation Account D) None of these
13. The interest on capital accounts of partners under fixed capital method is to be credited to:
   A) Partner's Capital A/c B) Profit & Loss A/c
   C) Interest A/c D) Partner's Current A/c
14. The Interest on partners' Capital Accounts under fluctuating method is to be credited to:
   A) Profit & Loss A/c B) Interest A/c
   C) Partner's Capital A/c D) None of these
15. The Current Account of the partners will always have:
   A) Debit balance B) Credit balance
   C) Either of the two D) none of these
16. Interest on partner's capital is calculated on:
   A) Opening Capital B) Closing Capital
   C) Average Capital D) None of these

17. In the absence of any agreement, the profits or losses of the firm are shared:

A) Equally | B) In Capital Ratio
C) In Different Proportions | D) None o these

18. In partnership firm profits and losses are shared:

A) Equally | B) In the Ratio of Capitals
C) As per Agreement | D) None of these

19. In an Ordinary Partnership, maximum number of partners can be:

A) 50 | B) 10
C) 15 | D) 20

20. Which accounts are opened when the capitals are fixed?

A) Only Capital Accounts | B) Only Current Accounts
C) Liability Accounts | D) Capital and Current Accounts

B. Give the answers of the following questions in one word/ sentence: **Marks - 1**

21. Define partnership?
22. What is mean by partnership deed?
23. Mention any two items of partnership deed?
24. What do you mean by guarantee of profit to a partner?
25. What will be the rate of interest on drawings in the absence of partnership deed?
26. If the same amount is withdrawn on the last day of each month, the interest on the drawings is calculated for how many months?
27. If the same amount is withdrawn on the first day of each month, the interest on the drawings is calculated for how many months?
28. If the same amount is withdrawn on the middle day of each month, the interest on the drawings is calculated for how many months?

C: Answer the following questions : **(Marks : 4/5/6)**

29: Define partnership? Discuss the Nature of partnership business.

30: what do you mean by Limited Liability partnership? Discuss about the salient features of Limited Liability partnership.

31. What is partnership deed ? mention some basic contents of partnership deed.
32. Write down the differences between fixed capital method and fluctuating capital method.
33. what do you mean by profit and loss Appropriation Account? Give a proforma of profit and loss Appropriation Account.

Numericl Questions :

34. Anil and Sunil are partners in a firm sharing profit & losses in the ratio of 5:3. On 1st April,2019 the capital of partners were Anil Rs.1,50,000; Sunil were Rs.1,20,000. The profit and loss Account of the firm for the year ended 31st March, 2020 showed a net profit of Rs.1,80,000. You are required to prepare profit and loss Appropriation Account on the basis of following conditions.

    i) Interest on capital @ 6% p.a.

    ii) Interest on Anils Loan of Rs.50,000 for the whole year.

    iii) Interest on drawings @ 6% p.a. Drawings were Anil Rs.1,000 p.m and Sunil Rs.2,000 p.m.

    iv) Sunil is to receive commission @5% on Net profit after such commission.

    v) Transfer 10% of distributable profit to the Reserve fund before distribution of profit.

35. Amar, Akbar and Ajoy are in partnership with capital of Rs.1,00,000 Rs.80,000 and Rs.60,000 respectively on 1st April, 2019. They share profit and losses in the ratio of 5:3:2, The profit & loss of the firm showed a profit of Rs.1,50,000 on 31st March, 2020.

The partnership deed provided the following:-

    i) Interest on capital @ 10% p.a.

    ii) Salary paid to Amar Rs.1,000 p.m.

    iii) Interest on drawings @6%

    iv) Each partner drew cash of Rs.750 p.m. begining of each month.

    v) Paid commission to Akbar @ 2% on gross sale (gross sale Rs. 3,75,000).

Prepare profit & loss Appropriation A/C.

36. Joy and Bijoy are partners with capitals of [1] 4,00,000 and Rs.2,00,000 respectively. The profit for the year ended 31st March 2020 wasRs.2,80,000. Show the distribution of profit after taking the following into consideration (Profit & loss Appropriation A/C).

    i) Interest on joys loan of Rs.1,00,00 to the firm provided on 1st April, 2019.

    ii) Interest on capital to be allowed @ 5% p.a.

    iii) Interest on Drawings @ 6% p.a. Joy drew [1] 3,000 p.m. at the end of each month and Bijoy drew Rs.30,000 daring the year from the firm.

    iv) Bijoy is to be allowed a commission of 4% on sales. Sales for the year were Rs.10,00,000.

    v) 10% of the divisible profits is to be kept in a reserve account.

37. Akash, Bikash and Chandan are partners of a firm. On 1st January, 2019 their capitals were-

    a) Akash- Rs.80,000;

    b) Bikash -Rs.60,000;

    c) Chandan -Rs.50,000.

All of them agreed that :-

i) Interest on capital is payable @ 5% p.a.

ii) Akash is to receive salary @ Rs.500 p.m.

iii) Bikash is to receive commission @5% on net profit after charging such commission;

iv) 10%of the net profit is to be transfered to general reserve.

The net profit for the year ended 31st December, 2019 before considering the above facts was Rs.40,000

Prepare partners capital Account.

38. Sanjoy and Bijoy are partners in a firm sharing profits and losses in the ratio of 3:2. Their capitals were Rs.1,20,000 (Sanjoy) and Rs.80,000 (Bijoy) as on January 01,2019. During the year they earned a profit of Rs.60,000. According to the partnership deed, both the partners are entitled to Rs.2,000 p.m as salary and 5% interest on their capital. They are also to be charged an interest of 5% on their drawing, irrespective of the period which is Rs.24,000 for Sanjoy and Rs.16,000 for Bijoy. Prepare partners capital Accounts when capitals are fixed.

39. A,B and P are partners in a business sharing profits and losses in the ratio of 10:6:4 with capitals of 50,000, 24,0 and Rs.26,000 respectively. Partners were entitled to 6% p.a. interest on their capitals. A and B guaranteed P that his share of profits in any year would not be less them Rs.10,000 exluding interest. During the year the firm earned a profit of Rs.50,000 before charging the interest on capital. Prepare profit and loss Appropriation Account.

40. Amit,Sumit and Ranjan were partners in a partnership firm. On 1st January, 2019 their fixed capitals were Rs.160,000, Rs.1,20,000 and Rs.1,20,000 respectively.

As per provisions of the partnership deep:

a) Ranjan was entitled for a salary of Rs.1,6,000 p.a.

b) All the partners were entitled to interest on capital @ 6% p.a.

c) Sharing profits and losses in the ratio of 2:2:1.

The net profit for the year ended 31st December, 2019 of Rs.90,000 was divided writhout providing for interest on capital and Ranjan's salary.

Pass an adjustment journal Entry to rectify the above errors on 1st January, 2020

41. A, B, C, D and E are five partners of firm. The delaits of their drawings for the year ended 31st March, 2020 are given below.

i) A's drawings during the year were Rs. 30,000.

ii) B withdrew Rs.3,000 p.m. in the begining of every month.

iii) C withdrew Rs.3,000 p.m. in the last date of every month.

iv) D withdrew Rs.3,000 p.m.in the middle date of every month.

V) E Withdrew the amount as under: April 30,2019- Rs.5,000; June 30, 2019- Rs.7,000; August 1, 2019- Rs. 4,000; October 1, 2019- Rs.10,000; January 31, 2020- Rs.4,000.

Calculate the interest on drawings of partners @ 12% p.a. for the year ended 31.03.2020.

42. A,B and C are partners in a firm. Their capital accounts showed the balance of Rs. 1,60,000, Rs.1,20,000 and Rs.1,00,000 respectively on 01.01.2020. A introduced Rs.20,000 on 01.04.2020; B withdrew Rs. 20,000 on 01.07.2020 and C introduced Rs. 10,000 on 01.07.2020 and withdrew Rs.40,000 on 01.10.2020. Interest is to be allowed @ 10% p.a. in the capitals.

Calculate the interest on capital of each partner for the year ended 31.12.2020.

Answer key

A.

1) A, 2) C, 3) A, 4) C, 5) B, 6) B, 7) B, 8) A, 9) D, 10) D,

11) B, 12) C, 13) D, 14) C, 15) C, 16) A, 17) A, 18) C, 19) A, 20) D,

21. See Textbook,

22. See Textbook,

23. i) Description of the partnership firm,

ii) Principle place of Business,

iii) Nature of business.

24. See Textbook

25. Partners will not be charged any interest on drawings.

26. 5 ½ months

27. 6 ½ months

28. 6 months

29 to 33. See Textbook

34 Profit Transferred to Anil's Capital- Rs.6,236 Profit transferred to Sunil's capital - Rs.51,742

Amount transfered to Reserve Fund- Rs.15,331

35. Profit transferred to Amar's Capital-Rs. 53,690

Profit transferred to Akbar's Capital-Rs. 32,214

Profit transferred to Ajoy's Capital-Rs. 21,475

36. Profit transferred Joy's Capital=Rs. 92,650

Profit transferred Bijoy's Capital = Rs.92,651

37. Balance of capital A/C as on 31.12.2019;

    Akash -Rs. 96,199, Bikash -Rs. 71,103, Chandan -Rs. 58,698

38. Balances of current A/C: - Sanjoy-Rs. 40,800

    Bijoy-Rs. 35,200

39. Deficiency of P's share-Rs. 1,600

    Contribution to P by A-Rs. 1,000

    Contribution to P by B- Rs. 600

40. Profits to be adjusted:-

    Amit -Rs. 6,400 (Dr.), Sumit-Rs. 8,800 (Dr.)

    Ranjan-Rs. 15,200(Cr)

41. Interest on A's drawings -Rs.1,800

    Interest on B's drawing -Rs.2,340

    Interest on C's drawing -Rs.1,980

    Interest on D's drawing -Rs.1,800

    Interest on E's drawing -Rs.2,180.

42. Interest on A's capital -Rs.17,500

    Interest on B's capital -Rs. 11,000

    Interest on C's capital -Rs.9,500.

CHAPTER -3

Admission of A Partner

When a person joins as a new partner in an existing partnership firm, is called admission of a partner. The purpose of admission of a new partner may be to raise additional capital for business or to arrange managerial skill or both. Generally, the new partner has to contribute capital to the firm and acquires his/her right to share the future profits and the assets of the firm.

During admission of a new partner, the existing agreement comes to an end and the firm is reconstituted with a new agreement. According to the Indian Partnership Act, 1932, No person shall be introduced as a partner into a firm without the consent of existing partners.

Adjustments required at the time of admission of a partner:-

The following adjustments are necessary at the time of admission of a partner:

1. Distribution of accumulated profits, reserves and losses
2. Revaluation of assets and liabilities
3. Determination of new profit-sharing ratio and sacrificing ratio
4. Adjustment for good will
5. Adjustment of capital on the basis of new profit sharing ratio (if so agreed)

1. Distribution of accumulated profits, reserves and losses

Profits and losses of earlier years which are not distributed to the partners are called accumulated profits and losses. Any reserve and accumulated profits and losses belong to the old partners should be distributed to the old partners in the old profit sharing ratio.

2. Revaluation of assets and liabilities

When a new partner is admitted into the partnership, the assets and liabilities are revalued as the current value may differ from the book value. Determination of current values of assets and liabilities is called revaluation of assets and liabilities.

New profit sharing ratio

It is very necessary to determine the new profit sharing ratio at the time of admission of a partner because the new partner is entitled to get the future profits of the firm. New profit sharing ratio is the proportion in which future profit will be distributed to all the partners.

Sacrificing ratio

The old partners may sacrifice a portion of their share of profit to the new partner. Sacrificing ratio is the proportion of the profit which is sacrificed by the old partners in favour of the new partner. The purpose of sacrificing ratio is to share the amount of goodwill brought in by the new partner.

The formula is:-

Sacrificing Share = Old share - New share.

Methods of Valuation of Goodwill

The important methods of valuation of goodwill are as follows:

1. **Average Profits Method**

   The Calculation is -

   Average Profit = Profits of Last years / No. of years

   Goodwill- Average Profits X No. of years purchased

2. **Super Profits Method**

   The Calculation is -

   Normal Profits: $\frac{\text{Capital Employed} \quad \text{Normal Rate of Return}}{100}$

   Super Profit= Average Profit- Normal Profit

   Goodwill= Super Profit x No of years' purchased

3. **Capitalisation Method**

   This method is used in two ways:-

(a) Capitalisation of average profit method.

   The Calculation is -

   Average Profit = Profits of Last years No. of years

   Capitalised value of average profit = Average profit $\times \frac{100}{\text{Normal Rate of Return}}$

   Goodwill= Capital required - capital employed

(b) Capitalisation of average profit method.

   The Calculation is -

   Normal Profits : $\frac{\text{Capital Employed} \quad \text{Normal Rate of Return}}{100}$

   Super Profit= Average Profit - Normal Profit

   Goodwill - Super profit $\times \frac{100}{\text{Normal Rate of Return}}$

Accounting *treatment* for goodwill

Accounting treatment for goodwill on admission of a partner is discussed below:

1. When new partner brings cash towards goodwill
2. When the new partner does not bring goodwill in cash or in kind
3. When the new partner brings only a part of the goodwill in cash or in kind

1. When new partner brings cash towards goodwill

When the new partner brings cash towards goodwill in addition to the amount of capital, it is distributed to the existing partners in the sacrificing ratio. The Journal entry is as follows:-

For amount of premium of Goodwill in cash:-

Cash/Bank A/c Dr.

To Premium of Goodwill A/c

For Distribution of premium of Goodwill among sacrificing partners

Premium of Goodwill A/c Dr.

To Old partner's capital A/c

2.When premium of Goodwill brought in by new partner is withdrawn by old partners. The Journal entry is as follows :-

For amount of premium of Goodwill in cash

Cash/Bank A/c Dr.

To. Premium of Goodwill A/c

For Distribution of premium of Goodwill among sacrificing partners

Premium of Goodwill A/c Dr.

To. Old partner's capital A/c

in sacrificing ratio)

For amount of goodwill withdrawn by old partners

Old partner's capital A/c Dr.

To. Cash/Bank A/c

When the new partner does not bring goodwill in cash or kind

When new partner does not bring goodwill in cash or in kind, his share of goodwill must be adjusted through the capital accounts of the partners. The following journal entry is passed.

New partners' capital A/c Dr.

To Old partners' capital / current A/c

(in sacrificing ratio)

When the new partner brings only a part of the goodwill in cash or in kind

When the new partner bring only a part of the goodwill in cash or assets. Than, for the cash or the assets brought, the respective account is debited and for the amount of brought in cash or kind, the new partner's capital account is debited. The following journal entry is passed.

Cash / Bank A/c/ Assets A/c .... Dr.

New partners' capital A/c.......... Dr.

To Old partners' capital /current A/c

(in sacrificing ratio)

Adjustment of capital on the basis of new profit sharing ratio

There can be two situations :-

(a) The new partner required to bring proportionate capital for his share of profit. New partner's capital is calculated on the basis of the capital of the reconstituted firm or on the basis of combined capitals of the old partners for their share of profit.

(b) Old partner's capital is calculated on the basis of the capital brought in by new partner for his share of profit in the business. The difference i.e. deficiency or excess in the old partners' capital account may be adjusted through the current accounts or cash may be brought in or withdrawn by the old partners.

Multiple Choice questions (Carrying 1 marks each) Choose the correct nswer

1. Revaluation A/c is a

   (a) Real A/c (b) Personal A/c

   (c) Nominal A/c (d) Impersonal A/c

2. On revaluation, increase in the value of assets leads to

   (a) Gain (b) Loss

   (c) Expense (d) None of these

3. The profit or loss on revaluation of assets and liabilities is transferred to the capital account of

   (a) Only old partners (b) Only new partner

   (c) All the partners (d) Sacrificing partners

4. If the old profit sharing ratio is less than the new profit sharing ratio of a partner, the difference is called

   (a) Capital ratio (b) Sacrificing ratio

   (c) Gaining ratio (d) None of these

5. At the time of admission, the goodwill brought by the new partner credited to the capital accounts of–

   (a) all the partners (b) the old partners

   (c) the new partner (d) the sacrificing partners

6. Which of the following statements is not true in relation to admission of a partner

   (a) Generally mutual rights of the partners change

   (b) The profits and losses of the previous years are not distributed to the old partners

   (c) The firm is reconstituted under a new agreement

   (d) The existing agreement does come to an end

7. J and K are sharing profits and losses in the ratio of 5:3. They admit Suman as apartner giving him 1/5 share of profits. Find out the sacrificing ratio.

   (a) 1:3 (b) 3:1

   (c) 5:3 (d) 3:5

8. B and K are partners sharing profits and losses in the ratio of 2:1. They admit into partnership. The new profit sharing ratio between B, K and M is agreed to 3:1:1. Find the sacrificing ratio between B and K.

   (a) 1:3 (b) 3:1

   (c) 2:1 (d) 1:2

9. When a new partner does not bring his share of Goodwill in cash, the amount is debited to

   (a) Premium A/c (b) Cash A/c

   (c) Capital A/c of new partner (d) Capital A/c of old partner

10. Profit or loss on revaluation is transferred to Partners' capital A/c's in

    (a) Old ratio (b) New ratio

    (c) Equal ratio (d) None of the above

Very short answer questions-(Carrying 1 marks each)

1. Define revaluation A/c.
2. How are accumulated profits and losses distributed among the partners at the time of admission of a new partner?
3. What is sacrificing ratio?
4. What is Goodwill?
5. State whether the following will be debited or credited in the revaluation account. (a) Depreciation on assets (b) Unrecorded Assets

SOLVE THE PROBLEMS

Question 1.

X, Y and Z are partners sharing profits and losses in the ratio of 5 : 3 : 2 . They admit M into partnership and give him 1 /5th share of profits. Find the new profit-sharing ratio.

Question 2.

R and M are sharing profits in the ratio of 7 : 3. They admit T for 3/7th share in the firm which he takes 1/7th from R and 2/7th from M. Calculate new profit-sharing ratio.

Question 3.

A and B are partners sharing profits and losses in the proportion of 7 : 3 . They agree to admit C,their manager, into partnership.He acquires his share as 1 /6th from A and 1/ 12th from B. Calculate new profit-sharing ratio.

Question 4.

A B and C were partners in a firm sharing profits in the ratio of 3:2 :1. They admitted D as a new partner for 1/7th share in the profits, which he acquired from C.

Calculate the new profit sharing ratio of A, B, C and D.

Question 5.

Bharat and Amar were partners sharing profits in the ratio of 3 : 2. They admitted Samar as a newpartner for I/5th share in the future profits of the firm which he got equally from Bharat and Amar.

Calculate the new profit-sharing ratio of Bharat, Amar and Samar.

Question 6.

M and N are partners in a firm sharing profits and losses in the ratio of 3 : 2. P is admitted as partner with 1/4 share in profit. P acquires his share from M and N in the ratio of 2 :1. Calculate new profit sharing ratio.

Question 7.

R and S are partners sharing profits in the ratio of 5 : 3. T joins the firm as a new partner. R gives1/3rd of his share and S gives 1/4th of his share to the new partner. Find out new profit-sharing ratio.

Question 8.

K and F are partners in a firm sharing profits and losses in the ratio of 7 : 3. K surrenders 2/10th from his share and F surrenders 1/10th from his share in favour of X; the new partner.

Calculate new profit-sharing ratio and sacrificing ratio.

Question 9.

P and Q were partners sharing profits in the ratio of 3 : 2. They admitted R and S as new partners P surrendered 1/3rd of his share in favour of R and Q surrendered 1/4th of his share in favour of S.Calculate new profit-sharing ratio of P,Q,R and S.

Question 10.

A and B are partners sharing profits in the ratio of 3 : 2. C is admitted as a partner. The new profit sharing ratio among A, B and C is 4 : 3 : 2 . Find out the sacrificing ratio?

Question 11.

A and B are partners sharing profits and losses in the ratio of 2 : 5. They admit C on the condition that he will bring in ₹ 10,500 as his share of goodwill in cash to be distributed between A and B. C's share in the future profits or losses will be 1/4th. What will be the new profit-sharing ratio and what amount of goodwill brought in by C will be received by A and B.

Question 12.

X and Y are partners in a firm sharing profits and losses in the ratio of 3 : 2. A new partner Z is admitted. X surrenders 1/5th of his share and Y surrenders 2/5th of his share in favour of Z. For this purpose of C's admission, goodwill of thefirm is valued at ₹ 50,000 and C brings in his share of goodwill in cash which is retained in the firm's books.

Journalise the above transactions.

Question 13.

M and N are partners in a firm sharing profits in the ratio of 3 : 2. They admit P as a new partner. The new profit-sharing ratio between M, N and P will be 5 : 3 : 2. P brought in ₹ 25,000 for his share of premium for goodwill. Pass necessary journal entries for the treatment of goodwil.

Question 14.

A and B are partners in a business sharing profits and losses in the ratio of 1/3rd and 2/3rd. On 1st April, 2018, their capitals are ₹ 8,000 and ₹ 10,000 respectively. On that date, they admit C in partnership and give him 1/4th share in the future profits. C brings in ₹ 16,000 as his capital and ₹ 12,000 as goodwill. The amount of goodwill is immediately withdrawn by the old partners in cash.

Pass journal entries and show the Capital Accounts of all the Partners. Calculate proportion in which partners would share profits and losses in future.

Question 15.

A and B were partners in a firm sharing profits and losses in the ratio of 3 : 2. They admitted C as a new partner for 3/7th share in the profit and the new profit-sharing ratio will be 2 : 2 : 3. C brought ₹ 1,00,000 as his capital and ₹ 75,000 as premium for goodwill. Half of their share of premium was withdrawn by A and B from the firm. Calculate sacrificing ratio and pass necessary journal entries for the above transactions in the books of the firm.

Question 16.

A and B are partners sharing profits in the ratio of 3 : 2. Their books show goodwill at ₹ 2,000. C is admitted with 1/4th share of profits and brings in ₹ 20,000 as his capital but is not able to bring in cash for his share of goodwill ₹ 6,000. Pass journal entries.

Question 17.

Suman and Shanti are partners in a firm sharing profits and losses in the ratio of 5 : 3. They admitted Raman as a new partner for 1/5th share of profits. Raman is to bring in ₹ 18,000 as capital and ₹ 2,000 as his share of goodwill premium. Give th necessary journal entries:

(a) When the amount of goodwill is retained in the business.

(b) When the amount of goodwill is fully withdrawn.

(c) When 50% of the amount of goodwill is withdrawn.

(d) When goodwill is paid privately.

Question 18.

Pass entries in the firm's journal for the following on admission of a partner:

(i) Machinery be depreciated by ₹ 11,000 and Building be appreciated by ₹ 32,000.

(ii) A provision be created for Doubtful Debts@ 5% of Debtors amounting to ₹ 70,000.

(iii) Provision for warranty claims be increased by ₹ 2,500.

Question 19.

Pass entries in the firm's journal for the following on admission of a partner:

(i) Unrecorded Investments worth ₹ 10,500.

(ii) Unrecorded liability towards suppliers for ₹ 3,000.

(iii) An item of ₹ 1,250 included in Sundry Creditors is not likely to be claimed and hence should bewritten back.

Question 20.

At the time of admission of a new partner C, the assets and liabilities of A and B were revalued as follows:

(a) A Provision for Doubtful Debts @10% was made on Sundry Debtors (Sundry Debtors ₹ 60,000).

(b) Creditors were written back by ₹ 4,000.

(c) Building was appreciated by 25% (Book Value of Building ₹ 2,50,000).

(d) Unrecorded Investments were worth ₹ 13,500.

(e) A Provision of ₹ 2,500 was made for an Outstanding Bill for repairs. Pass necessary journal entries.

Question 21.

X and Y are partners in a firm sharing profits and losses in the ratio of 3 : 2. On 1st April, 2019, they admit Z as a new partner for 1/5th share in profits . On that date, there was a balance of ₹ 1,10,000 in General Reserve and a debit balance of ₹ 10,000 in the Profit and Loss Account of the firm. Pass necessary journal entries regarding adjustment of reserve and accumulated profit/loss.

Question 22.

X and Y were partners in a firm sharing profits and losses in the ratio of 2 :1. Z was admitted for1/3rd share in the profits. On the date of Z's admission, the Balance Sheet of X and Y showed General Reserve ₹ 2,40,000 and a credit balance of ₹ 20,000 in Profit and Loss Account.

Pass necessary journal entries on the treatment of these items on Z's admission.

Question 23.

The profit for the last five years of a firm were as follows -year 2002 Rs. 4,60,000; year 2003 Rs. 3,90,000; year 2004 Rs. 4,10,000; year 2005 Rs. 4,40,000 and year 2006 Rs. 5,00,000. Calculate goodwill of the firm on the basis of 4 years purchase of 5 years average profits.

Question 24.

The capital employed of a business on December 31, 2001, Rs 4, 50 ,000 and the profits for the last five years were: 1997-Rs. 40,000: 1998-Rs. 50,000; 1999-Rs. 55 ,000; 2000-Rs. 70,000 and2001-Rs. 85 ,000. You are required to find out the value of goodwill base n 3 years' purchase of the super profits of the business, given that th normal rate of return is 10%.

Question 25.

A business has earned average profits of Rs. 1,10,000 during the last few years and the normal rate of return in a similar business is 10%. Ascertain the value of goodwill by capitalisation average profits method, given that the value of net assets of the business is Rs. 8,20,000.

Question 26.

Compute the value of goodwill on the basis of four years' purchase of the average profits based on the last five years? The profits for the last five years were as follows:

2002 ₹ 40,000

2003 ₹ 50,000

2004 ₹ 55,000

2005 ₹ 60,000

2006₹ 45,000

Question 27.

Capital employed in a business is Rs. 2,00,000. The normal rate of return on capital employed is 15%. During the year 2002 the firm earned a profit of Rs.46,000. Calculate goodwill on the basis of 3 years purchase of super profit?

Question 28.

The books of Ram and Bharat showed that the capital employed on 31.12.2002 was Rs. 4,00,000 and the profits for the last 5 years : 2002 Rs. 40,000; 2003 Rs. 50,000; 2004 Rs. 55,000; 2005 Rs. 70,000 and 2006 Rs. 85,000. Calculate the value of goodwill on the basis of 3 years purchase of the average super They share the profits and losses in the ratio of 3:1.They agreed to admit Rumita into the partnership firm for 1/4 share of profit which she gets entirely from Reshma profits of the last 5 years assuming that the normal rate of return is 10%?

Question 29.

R and S are partners in a firm. Their capitals were Rs. 3,00,000; Rs. 2,00,000, During the year 2002 the firm earned a profit of Rs.1,40,000. Calculate the value of goodwill of the firm assuming that the normal rate of return is 20%?

Question 30.

A business has earned average profits of Rs. 1,10,000 during the last few years.Find out the value of goodwill by capitalisation method, given that the assets of the business are Rs. 10,00,000 and its external liabilities are Rs. 1, 80,000. The normal rate of return is 10%?

Question 31.

Amar and Rana are partners sharing profits in the ratio of 3:2. Their balance sheet is shown as under on 31.03.2019.

Liabilities		**Assets -**	
Capital accounts:		Machinery	60,000
Amar 80,000		Furniture	40,000
Rana 70,000			
	1,50,000	Debtors	25,000
Reserve fund	15,000	Stock	10,000
Creditors	35,000	Prepaid insurance	40,000
		Cash at bank	25,000
	2,00,000		**2,00,000**

Ram is admitted as a new partner with a capital of Rs. 30,000 for his 1/5 share in future profits. He brings Rs.10,000 for his share of goodwill.

Following revaluations are made:

(i) Stock is to be appreciated to ₹ 12,000

(ii) Furniture is to be depreciated by 5%

(iii) Machinery is to be revalued at ₹ 82,000

Prepare the necessary ledger accounts and the balance sheet after the admission.

Question 32.

The balance sheet of Reshma and Sudipa on 31st March 2020 is as follows:

Liabilities		Assets	
Capital accounts:		Buildings	50,000
Reshma 50,000		Stock	8,000
Sudipa 30,000	80,000	Sundry debtors	60,000
General reserve	40,000	Cash at bank	32,000
P/ L., A/c	10,000		
Sundry creditors	20,000		
	1,50,000		1, 50,000

They share the profits and losses in the ratio of 3:1.They agreed to admit Rumita into the partnership firm for 1/4 share of profit which she gets entirely from Reshma.

Following are the conditions:

(i) Rumita has to bring ₹ 20,000 as capital. Her share of goodwill is valued at ₹ 4,000. She could not bring cash towards goodwill.

(ii) Depreciate buildings by 10%

(iii) Stock to be revalued at ₹ 6,000

(iv) Create provision for doubtful debts at 5% on debtors

Prepare necessary ledger accounts and the balance sheet after admission.

Question 33.

The following is the balance sheet of Jamuna and Amina as on 31.03.2019. They share the profits and losses equally.

Liabilities		Assets	
Capital accounts:		Building	70,000
Jamuna 40,000		Stock	30,000
Amina 50,000	90,000	Debtors	20,000
Creditors	35,000	Bank	15,000
General Reserve	15,000	Prepaid insurance	5,000
	1,40,000		**1,40,000**

On the above date, Tanima is admitted as a partner with 1/5 share in future profits. Followings are the terms for her admission:

(i) Tanima brings ₹ 25,000 as capital.

(ii) Her share of goodwill is ₹ 10, 000 and he brings cash for it.

(iii) The assets are to be valued as under:

Building ₹ 81, 000; Debtors ₹ 18,000; Stock ₹ 32,000

Prepare necessary ledger accounts and the balance sheet after admission.

Question 34.

Sun and Moon are partners sharing profits in the ratio of 3:2. Their balance sheet as on 1st January, 2018 was as follows:

Liabilities		Assets	
Capital accounts:		Buildings	40,000
Sun 30,000		Furniture	13,000
Moon 20,000	50,000	Stock	25,000
Creditors	50,000	Debtors	14,000
General reserve	15,000	Bills receivable	15,000
Workmen compensation fund	10,000	Bank	18,000
	1,25,000		**1,25,000**

They decided to admit Mars into partnership for 1/4 share in the profits on the followingterms:

(a) Mars has to bring in ₹ 30,000 as capital. His share of goodwill is valued at ₹ 5,000. He could not bring cash towards goodwill.

(b) That the stock be valued at ₹ 21, 000.

(c) That the furniture be depreciated by ₹ 3,000.

(d) That the value of building be depreciated by 20%.

Prepare necessary ledger accounts and the balance sheet after admission.

Question 35.

Amal and Shamal are partners in a business sharing profits and losses in the ratio of 3:2.The balance sheet of the partners on 31.03.2020 is as follows:

Liabilities	Rs.	Assets -	Rs.
Capital accounts:		Computer	50,000
Amal 4,00,000		Motor car	1,60,000
Shamal 3,00,000		Stock	4,00.000
	7,00,000		
Profit and loss	1,20,000	Debtors	3,60,000
Creditors	1,20.000	Bank	30,000
Workmen compensation fund	60,000		
	10,00,000		**10,00,000**

Kamal is admitted for 1/5 share on the following terms:

(i) Goodwill of the firm is valued at ₹ 75,000 and Kamal brought cash for his share of goodwill.

(ii) Kamal is to bring ₹ 1,50,000 as his capital.

(iii) Motor car is valued at ₹ 2,00,000; stock at ₹ 3,90,000 and debtors at ₹ 3,40,000.

(iv) Anticipated claim on workmen compensation fund is ₹ 10,000

(v) Unrecorded investment of ₹ 5,000 has to be brought into account.

Prepare revaluation account, capital accounts and balance sheet after Kamal's admission.

Question 36.

The following was the Balance Sheet of A, B and C sharing profits and losses in the ratio of 6:5:3

Liabilities	Amount	Assets	Amount
Creditors	18,900	Land and Buildings	50,400
Bills Payable	6,300		
Profit and Loss A/c	7,000	Furniture	7,350
Capital Account A	39,900	Stock	29,400
B	33.600	Debtors	26,460
C	16,800	Cash	8,890
	1,22,500		**1,22,500**

They agreed to take D into partnership and give him a share of 1/8 on the following terms: a) that D should bring in Rs. 8,820 as goodwill and Rs. 16,000 as his Capital;

(b) that furniture be depreciated by ₹ 930;

(c) that stock be depreciated by 10%

(d) that a Reserve ₹ 1,310 be created for doubtful debts.

(e) that the value of land and buildings having appreciated be brought upto Rs. 65,100;

(f) that after making the adjustments the capital accounts of the old partners be adjusted on the basis of the proportion of D's Capital to his share in the business, i.e., actual cash to be paid off to, or brought in by the old partners as the case may be.

Prepare Profit and Loss Adjustment Account, Partners' capital A/c and the Opening Balance Sheet of the new firm.

Question 37.

Aman and Baban are partners in a firm sharing profits and losses in the ratio of 2:1, Chayan is admitted into the firm with 1/4 share in profits. Chayan will bring in Rs. 30,000 as his capital and the capitals of Aman and Baban are to be adjusted in the profit sharing ratio. The Balance Sheet of Aman and Baban as on December 31, 2019 (before Chayan's admission) was as follows:

Balance Sheet of Aman and Baban as on 31.12.2019

Liabilites	Amount	Assets	Amount
Creditors	8,000	Cash in hand	2,000
Bills payable	4,000	Cash at bank	10,000
General reserve	6,000	Sundry debtor	8,000
Capital accounts:		Stock	10,000
Aman 50,000		Furniture	5,000
Baban 32,000	82,000	Machinery	25,000
		Land and Buildings	40,000
	1,00,000		**1,00,000**

It was agreed that:

(i) Chayan will bring in Rs. 12,000 as his share of goodwill premium.

(ii) Land and Buildings were valued at Rs. 44,800 and Machinery at Rs. 23,000.

(iii) A provision for doubtful debts is to be created @ 5% on debtors.

(iv) The capital accounts of Aman and Baban are to be adjusted by opening current accounts.

Record necessary journal entries, show necessary ledger accounts and prepare the Balance Sheet after admission.

Question 38.

A and B are partners in a firm sharing profits and losses in the ratio of 2:1. C is admitted into the firm with 1/4th share in profits. C will bring in Rs. 30,000 as his capital and the capitals of A and B are to be adjusted in the profit sharing ratio. The Balance Sheet of A and B as on March 31, 2020 was as follows:

Balance Sheet of A and B as on 31.03.2020

Liabilites	Amount	Assets	Amount
Creditors	9,000	Cash in hand	3,000
Bills payable	5,000	Cash at bank	9,000
General reserve	6,000	Sundry debtors	10,000
Capital accounts:		Stock	8,000
A 50,000		Furniture	4,000
B 30,000	80,000	Machinery	26,000
		Building	40,000
	1,00,000		**1,00,000**

It was agreed that:

i) C will bring in Rs. 12,000 as his share of goodwill premium.

ii) Buildings were valued at Rs. 44,600 and Machinery at Rs. 24,000

iii) A provision for doubtful debts is to be created @ 5% on debtors.

iv) The capital accounts of A and B are to be adjusted either by opening current accounts or cash accounts.

Record necessary journal entries, and prepare the Balance Sheet after admission.

ANSWER KEY (Admission of a Partner)

Multiple Choice questions Answer

1. (b) 2. (a) 3. (a) 4. (b) 5. (d) 6. (b) 7. (c) 8. (d) 9.(c) 10.(a)

Solve the Problems :

Question 1. Answer-10:6:4:5

Question 2. Answer-39:1:30

Question 3. Answer-70:33:17

Question 4. Answer-21:14:1:6

Question 5. Answer-5:3:2

Question 6. Answer-26:19:15

Question 7. Answer-40:27:29

Question 8. Answer-5:2:3

Question 9. Answer-4:3:2:1

Question 10. Answer-7:3

Question 23. Answer-17,60,000

Question 24. Answer-45,000

Question 25. Answer-2,80,000

Question 26. Answer-Rs. 2,00,000

Question 27. Answer-Rs. 48,000

Question 28. Answer-Rs. 60,000

Question 29. Answer-Rs. 2,00,000

Question 30. Answer-Rs. 2,80,000

Question 31. Answer—Revaluation a/c-22,000; Partners capital a/c- ₹ 1,08,200 ;₹ 88,800; ₹ 30,000; Balance Sheet- ₹ 2 ,62,000.

Question 32. Answer—Revaluation a/c Loss -₹ 10,000; Partners capital a/c- ₹ 84,000; ₹ 40,000; ₹ 16,000; Balance Sheet- ₹ 1,60,000.

Question 33.Answer: Revaluation profit: ₹ 11,000; Capital accounts: Jamuna: ₹ 58, 000;
Amina: ₹ 68,000; Tanima: ₹ 25,000; Balance sheet total: ₹ 1,86,000)

Question 34.Answer— Revaluation loss: ₹ 15,000; Capital accounts: Sun: - ₹ 39,000, moon ₹ 26,000, mars ₹25,000; Balance sheet total: ₹ 1,40, 000

Question 35.Answer: Revaluation profit: ₹ 15,000; Capital accounts: Areal -₹ 5,20,000; Shamal: ₹ 3,80,000; Kamal: ₹ 1,50,000; Balance sheet total: - ₹ 11,80,000)

Question 36. Answer: Gain on. revaluation Rs. 9,520 Balance Sheet Total Rs. 1,59,930

Question 37Answer: Gain on Revaluation Rs. 2,400. Balance Sheet Rs. 1,44,400.

Question 38.Answer: Gain on Revaluation Rs. 2,100. Balance Sheet Rs. 1,44,100.

CHAPTER-4

Reconstitution of A Partnership Firm : Retirement/Death of a Partner

Retirement

In a partnership firm ,a partner may retire from the firm for variety of reasons, such as old age, better business opportunity, difference with the other partners, with the consent of all other partners etc.

On retirement of a partner it become necessary to:-

(a) Ascertain the exact amount payble to the retiring partner and

(b) Settle his account by payment or transfer to his loan A/c.

Whatever may be the reason of retirement, to ascertain the exact amount payble to the retiring partner some adjustment are usually required with considering the following :-

(a) Adjustment in regard to goodwill.

(b) Adjustment in regard to revaluation of Assets and Liabilities.

(c) Adjustment in regard to settlement of undistributed profit.

(d) Balance of retiring partner's capital A/c and current A/c.

(e) Interest on capital and salary (if any) and share of profit up to the retirement.

Where retirement takes place on a date some time after the date to which the last Balance sheet and accounts were made up , profit in this case is calculated on some agreed basis or on the basis of accounts prepared as on the same date of retirement.

(a) Adjustment in regard to good will:

(b) When a partner retires, he becomes entitled to his share of the firms good-will.

Such adjustment may be made in the following ways:-

1. **Raising of goodwill**

Goodwill A/c-Dr

(full value of goodwill, existing value of goodwill in Balance sheet)

To all partners capital A/c

(in old ratio)

Written off full value of Goodwill

Continuing or remaining partners capital A/c Dr.

To Good will A/c.

New ratio which may be given in the problem if not given'

New ratio = Remaining ratio

Example :

A,B,C were partner's sharing profits as 3:2:1. If A retires remaining ratio 2:1. If B retaires it is 3:1 and if C retires it is be 3:2.

(i) Raising only outgoing partner's share of Goodwill.

Goodwill may be raised in the books only with the outgoing partner's share by

Goodwill A/c.....Dr

To outgoing partner's capital A/c

For written off

Continuing partner's capital A/c—Dr

To goodwill A/c

In gaining ratio,

Gaining ratio= New ratio –Old ratio

Alternatively only one entry may be done-

Continuining partner's capital A/c ——Dr

To Retired/ outgoing partner's capital A/c

(Only the retiring partner's portion)

(b)Adjustment in regard to revaluation of Assets and Liabilities:-

Revaluation is needed to give the retiring partner's his proper of the net Assets of the firm,

The mode of representing the revaluation is the same as already discussed regarding the Admission of a new partner, The profit or loss on revaluation is transferred to partners capital A/c (including the retiring partners) in old profit sharing ratio.

(A) Adjustment in regard to settlement of undistributed profit or losses:—

(i) If there is any undistributed reserve or profit and loss (cr) it should be shared among all partners in old ratio throng the following entry.

Profit and loss A/c—Dr

Reserve A/c ——————Dr

To All partners capital A/c (In old ratio)

ii) Where there is undistributed loss [P/L(Dr)]

The entry should be

All partners capital A/c——Dr

To P/L A/c (Dr' Balance)

c) Balance of retiring partners capital A/c and current A/c:———

On preparation of Capital A/c of all partner's , the partners balance of capital A/c (including retiring partner) The previous balance of capital A/c and current A/c will transferred to the capital A/c.

Ascertain the exact amount payble to the retiring partner

For calculating the amount of money payble to the retiring partner, the following items should be considered:-

i) Opening balance of capital and current A/c of retiring partner.

ii) Share of undistributed reserve and profit.

iii) Share of revaluation of Assets and Liabilities (Share of profit or Loss)

iv) Share of profit till the date of his retirement.

v) Share of firms goodwill.

vi) The salary / interest due to the retiring partner till the date of his retirement.

vii) The interest and drawing there on of the retiring partner.

Settle his account by payment or transfer to his loan A/c / Mode of payment of retiring partner.

The total amount due to the retiring partners can be paid off in one of the following manner:-

i) In one lumpsum :This method is suitable when the amount payble to the retiring partner is small. Under this method, the total amount is paid off at a time

ii) In installments : If the firm is unable to pay the total amount due to the partner at the time of his retirement if must recognise a liability for the remaining portion . Under this method, payment is made in instalments. The number of installmant, the time and amount of each instalment can all be decided in advance.

Generally, The total amount payble to the retiring partner is transferred to his loan A/c.

iii) **By way of an annuity:-**

The continuing partners may agree to settle the claim of the retairing partner by paing him a fixed annual sum called on annuity whether for a certain term of years or for the life time of the retiring partner.

Under this methol, the total amount payble to the retairing partner is transferred to payble to the retairing partner is transferred to an Annuity suspense A/c.

MCQ. (Marks-1)

1) Which of the following is correct ?

a. Goodwill is distributed to the partners in sacrificing ratio.

b. Goodwill is distributed to the partners in gaining ratio.

c. Goodwill is distributed to the partners in old ratio.

d. None of these.

2) Revaluation A/c is prepared in the time of

   a. Admission of a partner.
   b. Retirement of a partner.
   c. Death of a partner.
   d. All of the Above.

3) Profit of revaluation A/c is transferred to

   a. Existing partners capital A/c
   b. Remaining partners capital A/c
   c. Continue partners capital A/c
   d. All of the above

4) Gainig ratio can calculated:-

   a. New ratio–old ratio.
   b. Old ratio-New ratio.
   c. New ratio- Sacrificing ratio.
   d. Sacrificing ratio –New ratio.

5) Gaining ratio is required to distribute as per

   a. Profit on revaluation
   b. Undistributed profit
   c. Distribution for goodwill
   d. All of the above.

6) Incrcase of assets will be appeared in the revaluation A/c.

   a. Debit side.
   b. Credit side.
   c. Both side.
   d. None if these.

7) Remaining partner's means.

   a. All partner's.
   b. Retiring partner's.
   c. Continuing partner's.
   d. All of the above.

8) Existing partner's means.

   a. All partner's

b. Partners except retiring

c. Continuing partner's.

d. All of the above.

9) What treatment is made of accumulated profit and loss on the retirement of partner.

a. Credited to partners capital A/c (Old ratio)

b. Debited to partners capital A/c (New ratio)

c. Credited to remaining partners capital A/c (gaing ratio)

d. Debited to Retiring partners capital A/c

10) What journal entry will be recorded for writing off goodwill.

a. All partners capital A/c ———Dr

   To goodwill A/c (old ratio)

b. Remaining partner's capital A/c –Dr

   To goodwill A/c (gaining ratio)

c. Remaing partner's capital A/c –Dr

   To Retiring partners capital A/c(haining ratio)

d. None of these

11) On retirement of a partner goodwill be credited in the capital A/c of.

a. Retiring partner capital A/c.

b. Remaining partner's capital A/c.

c. All partners capital A/c.

d. None of These.

12) X.Y and Z are partners sharing profit and Losses on the ratio 5:2:1. If the new ratio 3:2 What will be the gaining ratio?

a. 11:14

b. 3:2

c. 2:3

d. 14:11

13) P,Q and R are partners sharing profit and losses on the ratio 5:4:3, Q retire and P and R decided to take the profit and Losses equally. What will be the gaining ratio?

a. 8:7

b. 2:3

c. 1:3

d. 10:15

14) A,B and C are partners sharing profit and Losses ¼, 3/10 and 9/20 respectively. The new ratio on the retirement of c will be.

a. 5:6

b. 8:10

c. 9:3

d. 3:1

15) Increase of Assets is credited to .

a. Revaluation A/c

b. Partners capital A/c

c. Profit and loss appropriation A/c.

d. None of These.

16) Unrecorded Assets

a. Debited to Revaluation A/c .

b. Credited to Revaluation A/c .

c. Debited to profit and Loss appropriation A/c.

d. None of These.

17) Claim of the reliring partner is paid in

a. Fully cash.

b. Fully Loan.

c. Partly cash and partly Loan A/c with agreed interest.

d. To Annuity fund after consulting with retiring partner.

Answer:-

1.b 2.d 3.a 4.a 5.c 6.b 7.c 8.a 9.a 10.c 11.c 12.d
13.c 14.b 15.a 16.b 17.d

Answer in one sentence : (Marks-1)

1. Write one reason for retirement of a partner from a firm.
2. Which adjustment are usually required for calculating the dues of the retiring partners.
3. Existing partner means? (meaning of existing partner)
4. Remaining partner means ? (meaning of Remaining partner)

5. What is the old ratio?
6. What is gaining ratio?
7. What is new ratio?
8. When gaining ratio is required?
9. Write the equation of gaining ratio.
10. How the dues of a retiring partner may be made?
11. What is Annuity ?
12. A,B and C are partner's sharing profits in the ratio of 5:3:2. A retires, calculate the gaining ratio of A and B.
13. What do you understand by retirement of a partner?
14. Give two circumstances in which gaining ratio may be applied.
15. Why the gaining ratio calculated ?
16. Why the value of goodwill necessary to determined on retirement of a partner.
17. State any one adjustment required at the time of retirement of a partner.
18. Describe the method of payment to a retiring partner. (any two).

1) X,Y,Z were partners sharing profit and Losses in the ratio 3:2:1 respectivelly. The Balance sheet of the firm on 31st Dec 2020 stood as follows:

Liabilities	Rs.	Assets	Rs.
Capital A/c			
X 40,000		Machinery	35,000
Y 30,000		Land and Building	45,000
Z 25,000		Furnitare	8,000
	95,000	Debtors	16,000
Creditors	20,000	Less; Provision	500
Bills payble	4,000		15,500
Rescrve	12000	Inventories	25000
		Cash	2500
	1,31,000		**1,31,000**

Y retire on that date subject to the following conditions:

a) Goodwill of the firm to valued at Rs 18,000 but no goodwill A/c was to appear in the books.

b) Machinery was to be depreciated by 10% and furniture by 15%.

c) Inventories was to be appreciated by 20% and Land and Building by 10%

d) The provision for doubtful debts was to be increased by Rs 1,950.

e) Provision for liability for workmen's compensation to the extent of Rs 1,650 was to be created.

It was agreed that X and Z would share profits in future in the ratio of 3:2 respectively. The amount due to Y was to transferred to his loan A/c.

You are required to prepare the revaluation A/c, Capital A/c of the partner's and the Balance sheet of the firm after the retirement of Y .

2) P.Q and R partner sharing profits at 5:3:2 their Balance sheet as 31st December 2020 is given below:

Liabilities	Rs	Assets	Rs
Capital :			
P 2,10,000		Plant and Machinery	80,000
Q 1,57,500		Furniture	9,250
R 1,05,000		Stock in trade	75000
	4,72,500	Bills Receivable	14250
Sundry creditor	40,000	Land and Building	2,62,500
		Sundry Debtor	40,500
Generel Reserve	12,500	Cash at Bank	51,000
Bills payble	21,000	Cash at Bank	13,500
	5,46,000		**5,46,000**

Q retired from the firm on the same date subject to following terms and conditions:

a) Goodwill of the entire firm is to be fixed at Rs 1,13,400 and Q share of the same be adjusted in the account's of P and R who are going to share in fulure in the proportion of 5:4.

b) Land and Building to be appreciated by 20%

c) Stock to be decreased by Rs 4980.

Prepare Revaluation A/c, partner's capital A/c and Balance sheet.

3) Amal Bimal and Kamal were partners sharing profit and losses in the ratio of 3:2:1 their Balance sheet as on 31st December 2020 was as follows:

Liabilities	Rs	Assets	Rs.
Capital		Cash at Bank	3,500
Amal	45,000	Debtors	30,000
Bimal	35,000	Stock	25,000

Kamal	25000	Plant	40,000
		Building	50,000
	1,05,000	Furniture	4,000
Reserve	15,000		
Profit and Loss a/c	12000		
Creditors	20,500		
	1,52,500		**1,52,500**

Kamal retired on that date subject to the following conditions:

i) Goodwill of the firm to be valued at Rs 36,000.

ii) Building is to be appreciated by 20%

iii) Plant and Furniture are to be depreciated by 10% and 15% respectively.

iv) Provision to be made for doubtful debts at 5%

Amal and Bimal are to bring in cash, if necessary in their profit sharing ratio to pay off Kamals dues on retirement and leave a sum of Rs 10,000 as working capital.

Prepare Revaluation A/c partner's capital A/c and the new Balance sheet.

4) A,B and C are partners sharing profit and losses in the ratio of their capital. The Balance sheet of the firm as at 31st March 2020 was as under:

Liabilities		Rs	Assets	Rs
Capital A/c				
A	80,000		Land and Building	1,00,000
B	70,000		Machinery	40,000
C	50,000		Furniture	10,000
		2,00,000	Stock in trade	70,000
Generel Reserve		60,000	Sundry Debtors	40,000
Sundry creditor		30,000	Cash at Bank	40,000
Bills payble		10,000	Cash in Hand	5000
Outstanding expenses		5000		
		3,05,000		**3,05,000**

B retires on 31st March 2020 and they agree the following adjustments:

i) Land and Building revalued at Rs1,60,000 and machinery reduccd to 90% of Book value

ii) Provision for doubtful debts is to be created @ 5% on sundry debtors.

iii) Unrecorded investment are to be brought into account Rs 11,000

iv) A creditor of Rs 5000 is not provided in the book of account

v) Rs 30,000 is to be paid to the retiring partner on the date of retirement and the balance is to be transferred to his loan account.

Show the revaluation A/c, partners capital A/c and reconstitueted Balance sheet after retirement of B.

5) X,Y and Z were in partnership sharing profit and losses equally. On 31st Dec 2020 X retaired when the firms Balance sheet was as under:

Liabilitles	Rs	Assets	Rs
Capital A/c		Land and Building	1,200
X 8,000		Plant and Machinery	6,980
Y 6,800		Sundry Debtors	8,915
Z 7,800		Investments	8,000
2	2,600		
Creditors	6,928	Cash	1,433
	29,528		**29,528**

According to partnership deed, assets were agreed to be revalued on x's retirement as under:

i) Land and Building Rs 5,800 plant and machinery Rs 6564, Investment Rs 8,400

ii) Goodwill was then valued at Rs 9,600 just for giving to the retirement.

iii) X accepted the investments at their revalued figure in part payment of his dues, Y paid in Rs 4000 as further capital and X was paid off the balance of his account.

Prepare the Revaluation A/c, partners capital A/c and the revised Balance sheet of Y and Z.

6) X,Y and Z carried on partnership sharing profits as 4:3:2, There Balance sheet on 31.12.20 was as follows:

Liabilities	Rs	Assets	Rs
Capital A	87,800	Plant and Machinery	37,000
Capital B	66,000	Land and Building	1,20,00
Capital C	43,800	Debtors	2,5000
Creditors	41,400	Lass: provision for	
		doubtful Debts	500
			24,500
		Stock	36,000
		Cash at Bank	21,000
		Cash in hand	500
	2,39,000		**2,39,000**

B retired on 31.12.2020 and these adjustments were agreed upon befor Ascertainig the amount payble to B :

i) Land and building to be appreciated by 15%.

ii) Goodwill to be valued at Rs 45,000 and B's share to be adjusted into the Accounts of A and C who decided to continues the business sharing profit as 5:3.

iii) Provision for doubtful debts raised to 5% on Debtors;

iv) A provision of Rs 650 is to be made for outstanding legal charges;

v) Stock to be reduced to Rs 32000

vi) The capital of the new firm to be adjusted in proportion to their new profit sharing ratio and actual cash to be broght in or paid off by or to the continuing partner's as the case may be.

B agreed to leave the amount due to him by the firm as loan to the firm carrying interest at 6% p.a. prepare the partner's capital A/c and also show the Balance sheet.

Answer:-

1. Profit on Revaluation Rs. 1,200.
   Transferred to Y' loan A/c Rs. 40,400.
   Balance sheet total Rs 1,33,850.
2. Profit on revaluation Rs, 47,520.
   Balance of capital A/c p->Rs 2,27,460.
   R->Rs 86,784, Total of Balance sheet Rs, 5,93,520.
   Q, s Loan Rs 2,05,776, Gaining ratio 5:22.
3. Profit on Revaluation Rs 39,900.
   Balances of capital ;Amal-1,04,040.
   Bimal - 74,360
   Amount brought by Amal Rs 25,590.
   Amount brought by Bimal Rs 17060.
   Paid to Kamal Rs 36150.
   Total of Balance sheet Rs 1,98,900.
4. Profit on Revaluation A/c Rs 60,000
   Partners capital Balance s A- Rs 1,28,000
   B- Rs 80,000
   Total of Balance sheet - Rs. 3,35,000

5. Profit on revaluation Rs. 1584,

   Balances of capital A/c Y- 9728

   X - Rs 6,728

   Total of Balance sheet Rs 23,384.

6. Balances of capital A/c;

   A- Rs 78,125, B-Rs 46,875

   Total Balance sheet Rs- 2,52,250.

Death of a partner

If a partner dies, the partner is usually dissolved. But if the surviving partner's desire so ,they may purchase the share of the deceased partner and carry on the business. In that case they have to decide:

i) The total amount payble to the legal representtative or executor or the deceased partner and

ii) The mode of such payment total amount payble includes:-

   i) The deceased partners capital A/c and current Accounts last Balance.

   ii) His share of undistributed profit /Loss

   iii) His Share of revaluation profit /Loss

   iv) His share of goodwill

   v) His share of profit /Loss made by the firm between the last year ending and the date of his death

   vi) The salary of a deacased partner, if it is provided in the partnership deed.

The following items also debited (Deducted) to the retiring partner's capital A/c.

   i) The debit balance of the partner's A/c ,

   ii) The share of goodwill in the books of account if any.

   iii) The share of loss on on revaluation .

   iv) The balance of drawing.

   v) The amount of interest on drawing.

   vi) The share of business loss of current accounting period.

The mode of payment depends on the agreement between the partner, it may be.

i) Lump sum payment:

If the firm has sufficient funds, the total amount payble on account of the deceased partner is transferred to his representative account (or executor) , such representtative's account is debited and Bank A/c is credited on payment of the dues.

ii) Instalment payment / Loan payment :-

The firm may not have enough money or funds to make prompt payment. In such a case, the total amount payble is transferred to a loan account in the name of the legal representative or executor. The Loan is paid off gradually by instalments after considering interest on unpaid balance. The word 'Loan' may or may not be appended with the account, but its gradual payment will definitely resemble the payment of loan.

Calculation of interim profit on retirement / on death during an accounting period:-

During an accounting priod retirement on death of a partner, calculation of interim profit is very important. The calculation of interim profit may calculate in the following two ways:-

i) Time Basis ii) Sales or turnover basis.

Time Basis : In this method the interim profit is calculate in the following two ways.

i) Calculation of profit on the basis of last year: In this example we can understand this easily.

A,B,C are partners sharing Profit and Losses 3:2:1. A retired/on Death 31st April 2020. If the average profit of the firm in the pervious years was Rs 1,20,000, then Mr A Is entitled to get the portion of interim profit is

$$1{,}20{,}000 \times \frac{4}{12} \quad \frac{3}{6} \left[\frac{4}{12}, \text{Death of partner on 3.4.2020 i,e 4 month's}, \frac{3}{6} \text{ is the portion of A}\right]$$

$= 20{,}000.$

Mr A will get Rs 20,000 of interim profit.

ii) On the basis of Last few year's average profit :

A,B,C are partners showing profits in the ratio 2:2:1, B retires on 30.06.2020. The profits for the last 4 years are given below:-

2016 Rs -1,50,000, 2017 Rs- 2,00,000 2018 Rs 1,80,000 and 2019 Rs 1,70,000 so Mr B's portion is –

$$\text{Average Profit} \times \frac{\text{Month}}{12} \times \frac{2}{5} \quad \left[\frac{2}{5} = \text{portion of B}\right]$$

$$= 4{,}75{,}000 \times \frac{6}{12} \times \frac{2}{5}$$

$= 35{,}000.$

$$\text{Agerage} = \frac{1{,}50{,}00+2{,}00{,}00+1{,}80{,}000+1{,}70{,}000}{4}$$

$$= \frac{7{,}00{,}000}{4}$$

$=1{,}75{,}000$]

Accounting treatment of interim profit

For transfer of interim profit to retiring partner or deceased partner's capital A/c.

Profit and Loss suspense A/c—Dr

To Retiring or Deceased partners capital A/c.

For transfer of profit and Loss suspense A/c to profit and Loss Appropriation A/c.

Profit and Loss Appropriation A/c .... Dr

To profit and Loss suspense A/c.

ii) Sales or turnover basis:-

To ascertain the interim Profit on this baris to ascertain

a) Total sales for the whole accounting period & b) Total sales for the current accounting period till to the death of partner.

Example :

A,B and C are partner's sharing profits in the ratio of 2:2:1. A retires on 1st August 2020. The accounts of the firm are closed on 31st March every year. Sales for the year ended 31st march 2020 were Rs 3,00,000 and profit for the year were Rs.60,000. Sales from the 1st April,2020 to 1st August 2020 were Rs 2,20,000. Calculate the share of interim profit of A.

Percentage of profits on sales for the year ended 31st march 2020 $= \frac{60,000}{3,00,000} \times 100$

$= 20\%$

Profit up to the date of death

i,e 1st Aug 2020 =Rs 2,20,000 X 20%

= Rs 44,000.

A,S share of interim profit = Rs 44000 $\times \frac{2}{5}$

= Rs 17,600.

Paymant of claim to the retiring partner or executors of deceased partner:

The journal entry of payment of claim to the retiring partner or executors of deceased partner is as follows:

i) When the amount due to them paid in full

Retirinig partner/Deceased Partner's Executor's A/C .... Dr.

To Bank A/c (Being the claim paid in full)

ii) When the amount due to them paid in parts and balance transferred to their loan A/C.

Retiring partner /Deceased partner's Executor A/C .... Dr.

To Bank /cash A/c
To Retiring partner/ Deceased partners Executors loan A/c
(Being the part of claim paid in cash/ Bank and balance
transferred to their Loan A/c)

Multiple Choice Questions **(Marks-1)**

1. In the retirement or death of a partner the amount of accumulated profits is transferred to all the partners capital A/c on their.
   a) Capital ratio
   b) Sacrificing Ratio
   c) New profit sharing ratio
   d) Gaining ratio
2. In the event of death of partner the total amount of death partner is payble to
   a) All partners
   b) Remaining partners
   c) Legal representative or Executor
   d) None of These.
3. The Loss on revaluation is debited to
   a) All partners capital A/c
   b) Remaining partners capital A/c
   c) Deceased partners capital A/c
   d) None of These
4. The mode of payment depend on
   a) The agreement between the partners
   b) Representative of deceased partner
   c) Continuing partner
   d) All of the above
5. For the effect of gaining ratio in the case of profit the amount will be.
   a) Increase
   b) Decrease
   c) Fixed
   d) Variable.

6. Who is appointed to pay the claim of a deceased partner?

a) Legal advisor.

b) Arbitrator

c) Executor

d) None of these

7. The interim profit of death partner Debited to

a) Profit and Loss A/c.

b) Profit and Loss Appropriation A/c.

c) Profit and Loss suspire A/c.

d) None of these.

8. The accounting procedures on death of a partner's are very similar to those / that of a partner's

a) Admission.

b) Retirement.

c) Dissolution.

d) None of These.

9. Upon death, if there is any reserve, it should be distributed amongst all partners in the

a) New ratio

b) Old ratio

c) Sacrifice ratio

d) Gaining ratio

10. The Executor of Deceased partner's are entitled to the share of goodwill of the firm as per the

a) Agreement between the partners.

b) Profit sharing ratio.

c) Equally.

d) None of These.

11. Upon death, when a memo random revaluation is prepared, assets and liabilities appear in the balance sheet at:-

a) Revalued figure.

b) Old Figure

c) None of These.

d) Both (a) and (b)

Answer:-

1) d 2) c 3) a 4) a 5) a 6) c 7) c 8) b 9) b 10) a 11) a

Objective type Question

1. On the event of death of a partner, what effect will be there on the old partnership?
2. When a partner dies, the combined share of the continuing partner's will increase or decrease?
3. In case of death of a partner can surviving partners may continue the business in the usual manner?
4. In the case of death, in what ratio the profit on revaluation of Assets and Liabilities is transferred to partner's capital Account?

1. The balance sheet of A,B and C as on 31st December 2019 is as follows:-

Liabilities	Rs	Assets	Rs
Capital A/c		Plant and Machinery	6,000
A—10,000		Furniture	8,000
B—5,000		Sundry Debtor	7,000
C—5000		Cash at Bank and hand	5200
	20,000		
Sundry creditor	3,000		
Geural Reserve	3,200		
	26,200		**26,200**

C died on 31.03.2020

Under the terms of partnership deed the executors of a deceased partner were entitled to:-

a) Amount standing to the credit of the partner's capital Account.

b) Share of goodwill on the basis of twice the average of the past three years profit.

c) Interest on capital at 5% p.a

d) Share of profit from the closing of the last financial year to the date of death on the basis of the last year's profit

Profit for 2017,2018 and 2019 were Rs. 6,000, Rs 8000 and Rs 7000 respectively.

e) Profits are shared in the ratio of capitals.

i) Prepare c's executors Account.

1) X, Y and Z were in partnership sharing profits equally. Z died on 31st March 2018. The Balance sheet of the firm as at 31st December 2018 was as under.

Liabilities	Rs	Assets	Rs
Sundry creditors	15,600	Cash in hand and	
		at Bank	4000
Capital A/c:		Debtors	18,000
X—30,000		Inventories	28,000
Y—25,000		Investment	8,000
Z—21,000		Freehold property	30,000
	76,000	Goodwill	13,500
General Reserve	6,000		
Investment fluctuation			
Reserve	2,100		
Provision for			
Doubtful debts	1800		
	1,01,500		**1,01,500**

On the date of death the following adjustments were agreed upon:-

a) Freehold property was worth Rs 54,000.

b) Debtors were all good.

c) Investment were valued at Rs 7,500 and were taken over by X at that value.

d) A liability for workmen's compensation for Rs 3000 was to be provided for.

e) Good will was to be valued at one year's purchase of the average profits of last 5 years but no goodwill account was to be continued in the books of the new firm.

f) Z's share of profit up to the date of death was to be calculated on the basis of last year's profit.

The profit of the last 5 years were as under, 2014 Rs—11,000, 2015 Rs –11,500 2016 Rs—8,000, 2017 Rs—10,000 and 2005 Rs –12,000.

Prepare

i) Capital accounts of the partner's transferring the amount due to Z to his executor's account and

ii) Balance sheet of the remaining partner's.

3) Akash, Bikash and Prakas are partner's in a firm sharing profit in the ratio of 5:3:2, on 31st March 2018 there Balance sheet was as follows:-

Liabilities	Rs	Assets	Rs
Capital A/c:			
Akas	1,20,000	Cash at Bank	20,000
Bikas	1,00,000	Cash in hand	12,000
Prakas	60,000	Plant & Machinery	1,20,000
Creditors	30,000	Building	80,000
Bills payble	14,000	Stock	40,000
Reserve	24,000	Debtors	32,000
		Patents	44,000
	3,48,000		**3,48,000**

Akas died on 1st oct 2018. It was agreed between his executors and the remaining partner's that:

a) Goodwill to be valued at 2.5 years
Purchase of average of the premises of four yours, which were. 2014—15 - Rs 52,000, 2015—16 Rs 2,48,000, 2016—17 Rs 80,000, 2017-18 Rs 60,000.

b) Interest on capital be provided at 10% p.a

c) The fixed assets be valued as below : patents Rs 32,000, Machinery Rs 1,12,000 and building s Rs 1,00,000.

d) Profit for the year 2018-19 be taken as having accrued at same rate as that of the previous year.

e) Half of the amount due to akas to be paid immediately to the executors and the balance transferred to his (Executors) Loan account.
Prepare akas's capital A/c and Akas's Executor A/c 1st oct 2018.

4) Sourav, Sachin and Swebag are partners in a firm sharing profits in the books of 5:3:2 On 31st March 2019 Their Balance sheet as under.

Liabilities	Rs	Assets	Rs
Capital A/c		Buildings	1,00,00
Sourav	1,00,000	Furniture	10,000
Sachin	1,00,000	Machinery	80,000
Swebag	90,000	Stock	40,000
Sundry creditor	50,000	Investments	40,000
Reserve fund	40,000	Sundry Debtors	50,000
		Patents	16,000
		Cash	4,000
		Bank	40,000
	3,80,000		**3,80,000**

Sourav died on 31st December 2019.The agreement between his Executors and remaining partners were as following:-

a) The assets revalued as follows:

Building Rs 1,20,000. Machinery Rs 75,000,

Furniture Rs 8000, Investment Rs 50,000. Stock Rs 35000, Patents Rs 12000 and Debtors Rs 45,000

b) The liabilities are reassessed as follows creditors Rs 45,000, and workmen's compensation Rs 5000.

c) Goodwill is to be valued at 2 year's purchase of the average profits of the previous 3years: Which were 2016-17 Rs 80,000, 2017-18 Rs 90,0000 and 2018—19 Rs 1,00,000.

d) Profit for the year ended on 31.03.19 is to be taken as the same amount of the year ended on 31.12.17.

e) Rs 30,000 is to be paid to be paid to sourav's Executors and balance to be transferred to their Loan A/c.

Prepare;

i) Sourav capital A/c transferred to sourav's Executror A/c.

ii) Profit on revaluation.

iii) Sourav's share of good will.

iv) Sourav share of interim profit

Answer

1. Amount due to C's Executors A/c –9,800.
2. i) Amount due to C's executors Rs—31,134.

   ii) Balance sheet total Rs—1,05,000.

   [Value of goodwill Rs 10,500 Balance of Capital A/c X – Rs 26,383, Y—Rs 28883. Investment fluctuation reserve Rs 500 should be deduct from Investment.]
3. Akas's Executor A/c Rs—2,28,000. (Capital A/c)

   Balance of Akas's Executor A/c Rs 1,14,000.
4. i) Sourav capital A/c transferred to sourav's executor A/c Rs 2,72,000.

   ii) Profit on revaluation Rs 9000.

   iii) Sourav's share of goodwill Rs 90,000

   iv) Sourav share of interim profit Rs 37,500

CHAPTER - 5

Disolution of Partnership

When ever a reconstitution takes place within a partnership in the form of Admission, retirement or death of a partner, the existing partnership is dissolved.

The partnership firm may however, continue if the remaining partner desire so.

But if the partnership firm is discontinued for any reason, that is called Dissolution of firm. The dissolution of a firm may take place in any one of the following circumstances:-

1. **By mutual consent :-** By mutual consent of all the partner's or in accordance with the terms of contract entered into between them.

2. **By Notice:-** Where the partnership is at will, by any partner giving notice in writing to all the other partner's of his intention to dissolve the firm.

3. **On the happening of any one of the following events:**
   - i) Expiry of the term ,where the partnership was constituted for a fixed term.
   - ii) Completion of the adventure for which the firm was constituted for a fixed term.
   - iii) Death of a partner.
   - iv) Adjudication of a partner as insolvent.

4. **Compulsory Dissolution:-**
   - i) Where all the partner or all but one are adjudged insolvent.
   - ii) If any event occurs making it unlawful for the business of the firm to be carried on.

5. **Dissolution by court:-**

According to section 44 of the Indian partnership Act the court, at the suit of a partner, may dissolve a firm on any one of the grounds namely

i) That a partner has become of unsound mind.

ii) Permanent incapability of a partner to do his duties.

iii) If a partner is guilty of misconduct that might affect prejudicially the carrying on of the business.

iv) If a partner wilfully or persistently commits breaches of partnership agreement.

v) If the partner transfers all his shares to a third party or has allowed his share to be changed under the provisions of rule 49.

vi) If the court considers that, the business can not be carried on except at loss.

vii) On any other ground or which the court consider the dissolution as just and equitable.

Mode of settlement of accounts on Dissolution:-

According to section 48 of the Indian partnership Act the following rules should be observed for settlement of accounts after dissolution, subject to agreement by partners:

a) Regarding losses :- Losses, including deficiencies of capital, shall be paid first out of profits, next out of capital, and lastly if necessary by the partners individually in the proportions in which they are entilled to share profits.

b) Regarding Assets:- The assets of the firm, including any sum's contributed by the partners to make up deficiencies of capital, shall be applied in the following manner and order.

i) In paying the debts of the firm to third parties.

ii) In paying each partner rateably what is due to him from the firm of advances as distinguished from capital.

iii) In paying to each partner rateably what is due to him as capital.

iv) The residue and if any, shall be devided among the partner's in the proportions in which they are entitled to share profits.

Where there are debts of the firm, and also separate debts due from any partner to third parties, the property of the firm shall be applied in the first instance in payment of the debts of the firm, and, if there is any surplus, the share of each partner of such surplus shall be applied in payment of his separate debts, the private property of any partner shall be applied first in the payment of his private debts, and the surplus, if any, in the payment of the debts of the firm.

FORMAT OF REALISATION ACCOUNT

Particular	Amount	Particular	Amount(RS)
To sundry assets A/C (Excluding cash, bank, ficticious assets, accumulated losses, debit balance of partner's capital account, Debit balance of partner's current account Loans to partner's)	***	By sundry liabilities A/C (Excluding partners capital, Loan from partners reserve, accumulated profit etc.)	***
To provision on any liability A/C	***	By provision on any Assets A/c	***
To Bank /cash A/C (amount paid for discharging realisation of Assets)	***	By Bank/cash A/c (amount received on Liabilities)	***

To Bank/Cash (Expenses of Realisation)	***	By Bank/cash A/c (Amount received from Unrecorded assets.	***
To partner’s capital/current A/C (liability taken over by a partner or remuneration commission paid to him or any expenses beared by him)	***	By partners capital A/C (Assets taken over by a partner recorded or unrecorded.)	***
To partners capital/ current A/c (Profit on realisation)	***	By partner’s capital/ current A/C (Loss on Realisation)	***

MULTIPLE CHOICE : **(1 Marks)**

1. Dissolution of partnership and dissolution of partnership firm are-

   a)Same things.

   b)different things.

   c) none of these.

   d) Both (a) and (b)

2. Realisation account are prepared when.

   a) Assets and liabilities are retained.

   b) Assets and liabilities are sold.

   c) To find out the net worth of the business on dissolution.

   d) None of the above

3. The court may dissolve a firm when.

   a)Insanity of a partner.

   b) By mutual consent of partner’s.

   c)when all partner’s are insolvent.

   d)None of these.

4. The solvent partner must share the deficiency of an insolvent partner.

   a)In the profit sharing ratio.

   b) In the capital ratio.

   c)Equally.

   d)None of These.

5. In the event of dissolution of partnership firm, the provision for doubtful debts is transferred to.

   a) Realisation account.

   b)partners capital account.

   c)Sundry debtors account.

   d)none of These.

6. On dissolution, if a partner undertakes to make payment of liability of the firm, the account to be debited is–

   a)Profit and loss account.

   b) Realisation account .

   c)Partners capital account.

   d) Cash account.

7. On dissolution goodwill account is transferred to.

   a) Partner's capital account.

   b) In the credit of cash account.

   c) In the debit of Realisation account.

   d) In the credit of Realisation account.

8. At the time of dissolution of partnership firm, ficticious asets are transferred to.

   a) Capital account of partners.

   b) Realisation account.

   c) cash account.

   d) partnership Loan account.

9. On dissolution of a firm , a partner paid Rs 2000 for firms Realisation expenses, which account will be debited?

   a) cash account .

   b) Realisation account.

   c) Capital account of the partner.

   d) profit and Loss account.

10. In which condition a partnership firm is deemed to dissolved?

    a) On a partner's admission.

    b) On retirement of a partner.

    c) On expiry of the period of partnership.

    d) On loss in partnership.

11. Unrecoded liability when paid on dissolution of a firm is debited to.

a) Partner's capital account

b) Realisation account.

c) Liabilities account.

d) Asset account.

12. On dissolution of the firm, amount received from sale of unrecorded assets is credited to.

a) Partner's capital account.

b) Profit and loss account.

c) Realisation account.

d) Cash account.

13. On dissolution, the final balance of capital accounts are transferred to.

a) Realisation account.

b) Cash account

c) Profit and loss account.

d) Loan accounts of partners.

14. Profit or loss of realisation account is transferred to.

a) Profit and loss A/C.

b) Capital account of partners.

c) Balance sheet.

d) None of above.

15. Cash balance shown in the balance sheet is shown on dissolution of firm in.

a) Realisation account.

b) Cash account.

c)Capital account.

d) None of the account.

Answer

1) b. 2) c. 3) a. 4) b. 5) a. 6) b. 7) a. 8) a. 9) b. 10) c. 11) c. 12) c. 13) b. 14) b. 15) b.

Objective type Question

1. What is the meaning of dissolution of firm?

2. Why realisation account is prepared?
3. How will you treat accumulated profit/losses at the time of dissolution of the firm?
4. In which ratio the balance of realisation A/c is transferred to partner's capital A/C?
5. At the time of dissolution of the firm, the Assets and liabilities appearing in the balance sheet will be transferred to which A/c ?
6. What is un-recorded asets?
7. What is unrecorded liabilities?
8. At the time of dissolution of firm when the balance of partner's capital is paid?
9. On dissolution of a firm, if any partner paid dissolution expense, what will be the journal entry?
10. On dissolution of a firm, a partner took over the furniture of Rs 20,000 at Rs 25000. By how much amount the realisation account will be credited?

1. A and B are partners in a firm, they share profit and losses in the ratio of 1:2 on 1st April 2020. They deeided to dissolve the partnership and on that date the balance sheet of the firm was as under:

Liabilities	Rs	Assets	Rs
Bills payble	10,000	Land and Building	1,20,000
Sundry creditor	20,000	Furniture	30,000
Capital A/C		Machinery and plant	80,000
A 1,50,000		Cash in hand	2,000
B 1,00,000		Cash at Bank	8,000
	2,50,000	Stock	1,02,000
General Reserve	60,000	Debtores 50,000	
B's Loan A/C	30,000	Less provision 2000	
			48,000
	3,90,000		**3,90,000**

The sales of firm properties realised Rs 1,00,000 from stock, Rs 34,000 from furniture and Rs 1,00,000 from land and Building, Rs 45,000 were collected from debtors and creditors were paid off at a discount of Rs 1,00,000.
Machinery and plant are taken over by A at their Book value. The expenses of realisation amounted to Rs 4,000
You are required to prepare the
a) Realisation account.
b) Cash Book and.
c) Partner's capital A/C.

2. A, B and C carrying on buninem in partnership decided to dissolve the firm on 31.12.19 when their balance sheet was as follows:

Liabilities	Rs	Assets	Rs
Creditors	68,000	Cash at Bank Debtors	50,000
Capital A/C		Debtors	1,24,000
		Stork	74,000
A	2,40,000	Tools	16,000
B	1,80,000	Motor car	24,000
C	1,20,000	Machinery	1,20,000
		Buildings	2,00,000
	6,08,000		**6,08,000**

The partnership deed provided that profits will be divided in the ratio of 3:2:1 respectively among A,B and C.

Assets realised as under:

Stock Rs 80,000, Machinery Rs 1,56,000, Buildings Rs 1,68,000, tools Rs 10,000, Motor Rs 50,000. Good mill Rs 1,20,000. Debtors were realised in full subject to bad debts of Rs 6000.

Creditors were seltled at a discount of Rs 1440. There was an unrecorded asset valued at Rs 6000, which was handed over to A for Rs 4000.

You are required to prepare realisation account, Bank account and partner capital account.

3. X,Y and Z were in partnership, they decided to dissolve the firm. Their position at 31st December.

Liabilities		Rs	Assets	Rs
Creditors		8,400	Cash in hand	475
Bills payble		1,500	Debtors	9,375
Loan form bank		9,000	Bills Receivable	950
X	4500		Furniture	950
Y	3000		Plant	15,900
Z	2,250		Goodwill	1,000
		9,750		
		28,650		**28,650**

They shared profits and losses in the proportion of 2:2:1 respectively.

Goodwill realised Rs 6,000. 10% of book debts proved bad and the bills receivable realised only Rs 900, The plant was sold for Rs 12000 and the office furniture was taken over by X at Book Value, the bills payable met before the due dates, earning a rebate of Rs 100. The bank loan was paid off including interest of Rs 300. The creditors were settled for Rs 8000 show the .

Realisation account cash account and the capital accounts of the partners.

4. A, B and C are in partnership sharing profit and losses equally. They decided to dissolve the partnership on 1st oct 2020 on which date the Balance shoot of the firm was as follows:

Liabilities	Rs	Assets	Rs
Capital		Capital 'C'	1,280
A- 20,000		Premises	25,650
B- 12,000		Machineny	10,800
	32,000		
Reserve	6,000	Stock	8,420
Sundry creditor	20,260	Sundry debtors	15,800
Bank Loan	2,120	Bills Receivable	1,280
		Cash at Bank	580
	63,380		63,380

The assets realised the following amounts:-

Premises Rs 16,000, machinery Rs 10,000, stock Rs 9,000, Debtors Rs 15000, Bills Receivables Rs 850. The goodwill was sold for Rs 2,500. Discount amounting Rs 260 were allowed by creditors while paying their claims.The expenses for realisation amounted to Rs 540. During the course of dissolution a liability for damages was settled at Rs 9,000 against Rs 7,000 provided in the books of the firm.

Prepare the necessary accounts to show the result of the realisation and also to close the books of the firm.

5. **X, Y and Z were partners in a firm sharing profit and losses in the ratio of 3:2:1. They clecided to dissolve to dissolve their firm w:e:f 31:12:20. The Balance sheet on which date was as follows :-**

Liabilities	Rs	Assets	Rs
Creditors	25,000	Machinery	45,000
Loan on mortgage	20,000	Stock	20,000
Joint life policy			
Reserve	12000	Debtors	30,000
Less : provision	1500		
Capital A/C	28500		
X-	45000	Joint life policy	15,000
Y-	30,000	Patents	20,000
Z-1	5,000	Cash at Bank	18500 90,000
	1,47,000		**1,47,000**

Additional information in connection with the dissolution was as follows:-

a) Joint life policy was surrendered and insurance company paid a sum of Rs 18000.

b) B took some of the patents at Rs 3500 whose book value was Rs 5000.

c) The remaining assets were realised as follows Machinery Rs 30,000, stock Rs 15,500, Debtors Rs.25,500, Patents 50% of the book value.

d) Liabilities were paid and discount of Rs 1,250 was allowed by the creditors.

e) Expenses of dissolution amounted to Rs 1,500

Prepare the necessary ledger Accounts to close the books of the firm.

Answer

1. a) Loss on Realisation Rs-24000.
   b) Cash book total Rs- 2,89,000.
   c) Capital A/c paymet to Rs 82,000 and B Rs-1,24,000
2. Profit on Realisation A Rs 1,49,440.
   Final Repayment A Rs 3,10,720, B Rs 2,29,814 and C Rs 1,44,906.
3. Profit on Realisation , A Rs 312.50
   Final Repayment X Rs 3675, Y Rs 3125 and Z Rs 2312.50.
4. Loss on Realisation , A Rs -3,484, B Rs-3483 and C Rs 3483
   Final Repayment A Rs-18516, B Rs 10,517 Mr C will brought Rs 2763.
5. Loss on Realisation, X Rs 14,375, Y Rs 9583 Z Rs 4792.
   Final payment X Rs 36625, Y Rs 20,917, Z Rs 12,208

ACCOUNTANCY : Class - XII

Part - B

CHAPTER -1

Accounting for Share Capital

Meaning of Company: -

A company is referred to as an association of people who contribute money or money's worth to a common fund and uses it for a purpose. It is an artificial person that exists as a corporate legal entity which is different from its core members or shareholders and has a common authentication utilised for its signature. Hence, it has a few definite characteristic features which categorise it from the other types of an organisation.

Characteristics/features of a Company: -

- **Corporate Body:** A company needs to be registered under the Companies Act, 2013. Any other organisation incorporated with the Registrar of Companies, and subsequently not registered cannot be considered as a company.
- **Separate Legal Entity:** A company exists as a separate legal entity which is different from its shareholders and members.
- **Limited Liability:** As the company exists as a separate entity, members of the company are not liable for the debts of the company. Liability of members of a company is limited to the extent of the shares that are held by them or by the extent of the guarantee amount
- **Transferability of Shares:** Shareholders of a public limited company can transfer their shares as per the rules laid down in the articles of association. However, in case of a private limited company, there might be some restrictions on the transfer of shares.
- **Common Seal:** The firm is an artificial entity or a person, and therefore cannot sign its name by itself. It creates the necessity of a common seal that can be used for representing the decisions made on behalf of the company.
- **Perpetual Succession:** The Company being an artificial person established by law perpetuates to exist regardless of the differences in its membership. In simple words, a company is an artificial person
- **Number of Members:** As per the Companies Act, 2013, the minimum number of members required to start a public limited company is seven while for a private limited company, it is two. The maximum number of members for a public limited company can be unlimited while it is restricted to 200 for a private limited company.

Kinds of Companies: -

Companies can be classified either on the basis of the liability of its members or on the basis of the number of members.

A. On the basis of liability of its members the companies can be classified into the following three categories:

i) Companies Limited by Shares: The liability of the shareholders is limited to the extent of the face value of shares held by them. Most Pvt Ltd companies are of this type.

ii) Companies Limited by Guarantee: In these companies, in case of liquidation, the shareholders promise to pay a certain fixed amount to cover the liabilities of the company.

iii) Unlimited Companies: There is no limit on the liability of the shareholders. In case of liquidation, they might have to pay even from their personal assets to cover the liabilities of the company. This type of company is quite uncommon today due to obvious reasons.

B. On the basis of the number of members, companies can be divided into three categories as follows:

i) Public Company: A public company means a company which (a) is not a private company; (b) is a company which is not a subsidiary of a private company.

ii) Private Company: This is a type of company that finds mention in the Companies Act, 2013. The purpose of private companies is when the business is not very large, but the owners/management still want to opt for a company over a partnership or proprietorship. A private company must have at least 2 persons, except in case of one-person company and limits the number of its members to 200.

iii) One Person Company (OPC): Section 2(62) of Companies Act defines a one-person company as a company that has only one person as to its member. Additionally, members of a company are nothing but subscribers to its memorandum of association, or its shareholders. So, an OPC is effectively a company that has only one shareholder as its member.

Share Capital of a Company : -

Share capital denotes the amount of capital raised by the issue of shares, by a company. It is collected through the issue of shares and remains with the company until its liquidation.

Categories of Share Capital: -

i) Authorised/Nominal/Registered Capital: At the time of registration of a company, the Memorandum of Association mentions the amount of capital a company is authorised to raise from the public by selling shares which is known as Authorised Capital or Normal Capital or Registered Capital. It is the maximum amount of share capital that a company can issue.

ii) Issued Capital: Generally, a part of the authorised capital is issued to the public for subscription which is known as issued capital, i.e., it is the nominal value of the shares which are offered to the public for subscription.

iii) Subscribed Capital: It is that part of "issued capital" for which applications are received from the public. The subscribed capital is allotted to the respective subscribers as per resolution passed by the directors of the company.

iv) Called up Capital: Generally, the shareholders pay the price of the shares by instalments, viz., application, allotment, First call, Final call etc. Therefore, the portion of the face value of the shares which the shareholders are called upon to pay or the company has demanded to pay is called Called-up capital.

v) Paid up Capital: The amount actually paid by the shareholders is known as Paid-up Capital.

vi) Uncalled Capital: The unpaid portion of the subscribed capital is called Uncalled Capital. In other words, it is the remainder of the issued Capital which has not been called.

vii) Reserve Capital: A company may reserve a portion of its uncalled capital to be called only in the event of winding up of the company. Such uncalled amount is called 'Reserve Capital' of the company.

Let us see the following example to show how the share capital will be shown in the balance sheet.

Share Capital		(Rs.)
Authorised or Registered or Nominal Capital:		
4,00,000 Shares of Rs. 10 each		40,00,000
Issued Capital		
2,00,000 Shares of Rs. 10 each		20,00,000
Subscribed Capital		
Subscribed but not fully paid up		
2,00,000 Shares of Rs. 10 each, Rs. 8 called up 16,00,000		15,94,000
Less: Calls in Arrears (6,000)		

Nature and Classes of Shares: -

he amount of authorised capital, together with the number of shares in which it is divided is mentioned in the Memorandum of Association but the divisions of shares in which the enterprise's capital is to be split along with their specific obligations and rights, are recommended by the Articles of Association of the company. As per The Companies Act, an enterprise can issue 2 types of shares:

- Preference shares
- Equity shares (also called ordinary shares)

Preference Shares: Preference shares, more commonly referred to as preferred stock, are shares of a company's stock with dividends that are paid out to shareholders before common stock dividends are issued. If the company enters bankruptcy, preferred stockholders are entitled to be paid from company assets before common stockholders.

Equity shares: An equity share, normally known as ordinary share is a part ownership where each member is a fractional owner and initiates the maximum entrepreneurial liability related to a trading concern. These types of shareholders in any organization possess the right to vote.

Issue of Shares: -

The issue of shares is the procedure in which enterprises allocate new shares to the shareholders. Shareholders can be either corporates or individuals. The enterprise follows the rules stipulated by Companies Act 2013 while circulating the shares. The Issue of Prospectus, Receiving Applications, Allocation of Shares are 3 key fundamental steps of the process of issuing the shares.

Minimum Subscription :

When shares are issued to the general public, the minimum amount that must be subscribed by the public so that the company can allot shares to the applicants is termed as Minimum Subscription. It is to be noted that 'minimum subscription' of capital cannot be less than 90% of the issued amount according to SEBI (Disclosure and Investor Protection) Guidelines, 2000 [6.3.8.1 and 6.3.8.2]. If this condition is not satisfied, the company shall forthwith refund the entire subscription amount received. If a delay occurs beyond 8 days from the date of closure of subscription list, the company shall be liable to pay the amount with interest at the rate of 15% [Section 73(2)].

Accounting Treatments for Issue of Shares: -

A company may issue shares at their face value or at a price other than the face value. When shares are issued at a price equal to their face value it is termed as shares issued at par. When issue price of a share is more than its face value, it is known as shares issued at a premium. If issue price of a share is less than its face value, it is called as shares issued at a discount.

The issue price of a share is normally collected in stages—along-with application, on allotment and later by making one or two calls. The shares become fully paid up only on receipt of all the money due on them.

The accounting entries pertaining to the issue of shares are as follows:

1. **For Receipt of Application**

   Bank A/c Dr.

   To Share Application A/c

   (Being Amount received on application for — shares @ Rs. per share)

2. **For Transfer of Application Money**

   Share Application A/c Dr.

   To Share Capital A/c

   (Being Application money on_______Shares transferred to Share Capital)

3. **For Money Refunded on Rejected Application**

   Share Application A/c Dr.

   To Bank A/c

   (Being Application money returned on rejected application for____shares)

4. **For Adjustment of Excess Application Money**

   Share Application A/c Dr.

   To Share Allotment A/c

   (Being Application Money on __Shares @ Rs per shares)

5. **For Amount Due on Allotment**

Share Allotment A/c Dr.

To Share Capital A/c

(Being allotment money due on shares @ Rs. per share)

6. **When allotment money is received**

Bank a/c Dr.

To share allotment A/c

(Being allotment money received)

7. **For Call Amount Due**

Share Call A/c Dr.

To Share Capital A/c

(Being Call money due on_____Shares @ Rs.____per share)

8. **For Receipt of Call Amount**

Bank A/c Dr.

To Share Call A/c

(Being Call money received)

Note: -

The journal entries (2) and (3) can also be combined as follows:

Share Application A/c Dr

To Share Capital A/c

To Bank A/c

(Being Application money on____Shares transferred to Share Capital and Application money returned on rejected application for____shares)

The journal entries (3) and (4) can also be combined as follows:

Share Application A/c Dr

To Share Allotment A/c

To Bank A/c

(Being Excess application money adjusted to share allotment and balance refunded)

Calls-in-Arrears: -

Any Amount which has been called or demanded by company from shareholders but not paid by the shareholder till the last date mentioned in call letter is called as call in arrear. Where a company maintains 'Calls in Arrears' Account, it needs to pass the following additional journal entry:

Calls in Arrears A/c Dr.

To Particular Call (e.g. Share First Call Account)

To Share Second and Final Call Account A/c

(BeingCalls in arrears brought into account)

Calls in Advance: -

A shareholder can pay the whole or part of the amount remaining unpaid on his shares even before the call is made. This is only a voluntary payment and is known as calls in advance.

The following journal entry is recorded for the amount of calls received in advance.

Bank A/c Dr.

To Calls in Advance A/c

(Being Amount received on call in advance)

On the due date of the calls, the amount of 'Calls in Advance' is adjusted by the following entry:

Calls in Advance A/c Dr.

To Particular Call A/c

(BeingCalls in advance adjusted with the call money due)

Over Subscription: -

When the number of Share application received is more than the number of shares offered to public it is known as over subscription. In this case, one of the following step can be followed :

1. Reject the excess applications
2. Make pro-rata allotment
3. Partially refund amount and on other applications pro-rata allotment is made.

1. Accounting Treatment for Rejection the excess applications and Money Returned The company may reject the applications for shares in excess of the shares offered for issue and a letter of rejection is sent to such applicants. In this case the application money received from these applicants is refunded to them in full. The journal entry made is as follows:

Share Application A/e Dr

To Bank A/c

(Being excess Application money on......shares refunded to the applicants)

2. Accounting Treatment for Making pro-rata allotment

When the directors opt to make a proportionate allotment to all applicants (called 'pro-rata' allotment), the excess application money received is normally adjusted towards the amount due on allotment.The journal entry made is as follows:

Share Application A/c Dr.

To Share Capital A/c

To Share Allotment A/c

(BeingTransfer of application money to share capital and the excess application money on........shares credited to share allotment account)

In case, the excess application money received is more than the amount due on allotment of shares, such excess amount may either be refunded or credited to calls in advance and the following entry is made:

Share Application A/c Dr

To Call-in-advance A/c

(BeingThe adjustment of excess share application money retained as call-in advance in respect of ... shares)

3. Accounting Treatment Partially refund amount and on other applications pro-rata allotment is made

When the application for some shares are rejected outrightly; and pro-rata allotment is made to the remaining applicants, the money on rejected applications is refunded and the excess application money received from applicants to whom pro-rata allotment has been made is adjusted towards the amount due on the allotment of shares allotted. The journal entries on application and allotment recorded as follows:

1 **Bank A/c** **Dr.**

To Share Application A/c

(Being Money received on application for........shares @ Rs. _ per share)

2 **Share Application A/c** **Dr.**

To Share Capital A/c

To Share Allotment A/c

To Bank A/c

(BeingTransfer of application money to share capital, and the excess application amount of pro-rata allottees credited to share allotment and the amount on rejected applications refunded)

3 **Share Allotment A/c** **Dr.**

To Share Capital Aic

(Being Amount due on the Allotment of.......shares @ Rs. _ per share)

4 **Bank A/c** **Dr.**

To Share Allotment A/c

(BeingAllotment money received after adjusting the amount already received as excess application money)

Under Subscription: -

The issue is said to have been under subscribed when the company receives applications for less number of shares than offered to the public for subscription. In this case company is not to face any problem regarding allotment since every applicant will be allotted all the shares applied for. But the company can proceed with allotment provided the subscription for shares is at least equal to the minimum required number of shares termed as minimum subscription.

Issue of Shares at a Premium : -

If a company issues its shares at a price more than its face value, the shares are said to have been issued at Premium. The difference between the issue price and face value or nominal value is called 'Premium'. If a share of Rs 10 is issued at Rs 12, it is said to have been issued at a premium of Rs 2 per share. The money received as premium is transferred to Securities Premium A/c. A company issues its shares at premium only when its financial position is very sound. It is a capital gain to the company. Securities Premium A/c is shown under the title *'Equity and Liabilities'* of the company's balance sheet under the head *'Reserves and Surpluses'*.

Accounting Treatment for Shares Issued at Premium

1. For Premium Amount called with Application money

(a) Bank A/c Dr.

To Share Application A/c

(BeingMoney received on application for —shares a@ Rs. — per share including premium)

(b) Share Application A/c Dr.

To Share Capital A/c

To Securities Premium Reserve A/c

(BeingTransfer of application money to sharecapital and securities premium account)

2. Premium Amount called with Allotment Money

(a) Share Allotment A/c Dr.

To Share Capital A/c

To Securities Premium Reserve A/c

(BeingArnount due on allotment of shares aRs — per share including premium)

(b) Bank A/c Dr.

To Share Allotment A/c

(BeingAllotment money received including premium)

3. Premium Amount called with Call Money

(a) Share Application A/c

To Share Capital Reserve A/c

To Securities Premium A/c

(BeingAmount due on lst/2nd call @Rs- per share including premium)

(b) Bank A/c Dr.

To Share Call Ale

(BeingCall money received including premium)

Issue of Shares at a Discount: -

When the issue price of share is less than the face value, shares are said to have been issued at discount. For example, when a share of the nominal value of Rs. 100 is issued at Rs. 98, it is said to have been issued at a discount of Rs two per share. As a general rule, a company cannot ordinarily issue shares at a discount. It can do so only in cases such as 'reissue of forfeited shares' (to be discussed later) and issue of sweat equity shares.

Accounting Treatment of Shares Issued at Discount :

The amount of discount is generally adjusted towards share allotment money and the following journal entry is made:

Share Allotment A/c Dr

Discount on issue of shares A/c Dr

To Share Capital A/c

(Being Allotment money due on....shares @Rs......... per share after allowing discount @Rs.......... per share)

Issue of Shares for Consideration other than Cash : -

Sometimes shares are issued to the promoters vendors of the company in lieu of the services provided by them during the incorporation of the company. These shares can also be issued either at par, at premium or at discount, and the number of shares to be issued will depend upon the price at which the shares are issued and the amount payable to the vendor. The number of shares to be issued to the vendor will be calculated as follows:

Number of shares to be issued=Amount Payable ÷ Issue Price

Forfeiture of Shares : -

Forfeiture of shares is referred to as the situation when the allotted shares are cancelled by the issuing company due to non-payment of the subscription amount as requested by the issuing company from the shareholder.

In the event of forfeiture of shares, the shareholder loses the rights and interests of being a shareholder and ceases to be a member of the organisation.

When shares are forfeited all entries relating to the shares forfeited except those relating to premium, already recorded in the accounting records must be reversed. Accordingly, share capital account is debited with the amount called-up in respect of shares are forfeited and crediting the respective unpaid calls account's or calls in arrears account with the amount already received. Thus, the journal entry will be as follows:

(a) Journal entry Forfeiture of Shares issued at Par :

Share Capital A/c (Called up amount) Dr.

To Share Forfeiture A/c (Paid up amount)

To Share Allotment A/c

To Share Calls A/c (individually)

(Being no shares forfeited for non-payment of allotment money and calls made)

(b) Journal entry to record the forfeiture of shares issued at a premium on which premium has not been fully received:

Share Capital A/c Dr.

Securities Premium Reserve A/c Dr.

To Share Forfeiture A/c

To Share Allotment A/c

To Share Calls A/c (individually)

(Being......no shares forfeited due to non-payment of allotment money and calls made)

Note: If Calls in Arrears Account is maintained, Calls in Arrears Account is credited and not the Share Allotment and Share Call/Calls Accounts.

Reissue of Forfeited Shares : -

Reissue of shares means issue of forfeited shares. The directors can either cancel or re-issue the forfeited shares. In maximum cases,they reissue such shares which may be at par, at premium or at a discount. Forfeited shares may be reissued as fully paid at a par, premium, discount. In this situation, it may be noted that the amount of discount allowed cannot exceed the amount that had been received on forfeited shares at the time of initial issue, and that the discount allowed on reissue of forfeited shares should be debited to the 'Forfeited Share Account'. The balance, if any, left in the Share-Forfeited Account relating to reissued Shares, should be treated as capital profit and transferred to Capital Reserve Account.

(A) Reissue of forfeited shares at a discount:

When the forfeited are reissued at discount, Bank account is debited by the amount received and Share capital account is credited by the shares paid-up amount. The amount of discount allowed is debited to Share Forfeited Account. The journal entry for the above will be as follows:

Bank A/c (the amount received on reissue) Dr.

Share Forfeited A/c (the amount allowed as discount) Dr.

To Share Capital A/c (face value)

But in case, this amount of discount is less than the amount forfeited, the remaining forfeited amount will be profit for the company. This profit is a capital gain to the company and is transferred to Capital Reserve account. Journal entry of the same will be as follows:

Share Forfeited A/c Dr

To Capital Reserve A/c

(BeingTransfer of surplus share forfeited amount to capital reserve A/c)

Accounting Treatment of Reissue of Forfeited Shares: -

There can be four situations of reissue of forfeited shares. These are:

(1) Reissue of forfeited shares at discount originally issued at par

(2) Reissue of shares at par or at premium, originally issued at par

(3) Reissue of forfeited shares at par, at discount and at premium originally issued at premium.

(4) Reissue of forfeited shares at par, at discount and at premium, originally issued at discount.

1. Reissue of forfeited shares issued at discount, originally issued atpar

In this case the maximum discount that can be given on reissue of forfeitedshares is the amount that has been received on these shares and is debitedto share forfeited account.

Example : -

X company Ltd. forfeited 200 shares of Rs 10 each, fully called up on which Rs. 7 have been received and final call of Rs. 3 per share remains unpaid. These shares were later on reissued for Rs. 8 per share fully paid up. Make journal entry for recording the forfeiture and reissue of shares.

Solution

	Journal Entries		**Amount (Rs)**
(i)	Share Capital A/e Dr		2000
	To Shares Forfeited A/c		1400
	To Shares Final Call A/c		600
	(BeingForfeiture of 200 shares of Rs. 10 each due to non-payment of final call of Rs 3 per share)		
(ii)	Bank A/c	Dr	1600
	Shares Forfeited A/c	Dr	400
	To Share capital A/c		2000
	(BeingReissue of 200 forfeited shares of Rs 10 each for Rs. 8 per share as fully paid up)		
(iii)	Shares forfeited A/c	Dr	1000
	To Capital Reserve A/c		1000
	(Being the Balance amount in Share Forfeited A/c transferred to Capital Reserve A/c)		

2. Reissue of forfeited shares at premium and at par, originally issued at par

In this case the whole the amount that has been credited to Shares Forfeited A/c is transferred to Capital Reserve A/c on the reissue of such shares.

Example: -

Y Ltd. forfeited 400 shares of Rs. 20 each, on which Rs 15 per share have been received and balance remains due but not paid. These shares were reissued

(a) at the rate of Rs 20 per share i.e. at par

(b) at the rate of Rs. 24 per share i.e. at premium

Make necessary journal entries for reissue of the shares by opening calls-in-arrear A/c.

Solution

Journal Entries

i) Share Capital A/c.	Dr	8,000
To call in arrear A/c		2,000
To Share are for feiture A/c		6,000
Case (a)		
(i) Bank A/c	Dr	8000
To Share Capital A/c		8000
(BeingReissue of 400 shares at the rate of Rs 20 per share)		
(ii) Shares Forfeited A/c	Dr	6000
To Capital Reserve A/c		6000
(BeingBalance amount of Share Forfeited A/c is transferred to Capital Reserve A/c)		
Case (b)		
(i) Bank A/c	Dr	9600
To Share Capital A/c		8000
To Securities Premium A/c		1600
(BeingReissue of forfeited shares at premium)		
(ii) Share Forfeited A/c	Dr	6000
To Capital Reserve A/c		6000
(BeingBalance amount of Shares Forfeited A/c is transferred to Capital Reserve A/c)		

3. Reissue of forfeited shares at par, at discount and at premium, originally issued at premium:

If the shares were originally issued at premium, it is not necessary that their reissue after forfeiture is to be at premium. Such shares can be reissued at par, at discount or at premium. If such shares are reissued at premium the premium received should be credited to Securities Premium A/c. Journal entry will be:

Bank A/c Dr

(Number of shares x amount received per share)

To Share Capital A/c

(Number of shares x amount paid up per share)

To Securities Premium A/c

(Number of shares x amount of premium per share)

Example: -

AZ Ltd. forfeited 200 shares of Rs 10 each originally issued at a premium of Rs 4 per share, the holder of which paid Rs 3 per share on application but did not pay the allotment money of Rs 7 per share (including premium) and call of Rs. 4 per share. Make necessary journal entries for the forfeiture and for reissue of these shares if:

I. Reissued at Rs 10 per share i.e. at par

II. Reissued at Rs 8 per share i.e. at discount

III. Reissued at Rs 12 per share i.e. at premium

Solution:

Journal entries

(i)	Share Capital A/c (200 x Its 10)	Dr.	2000
	Securities Premium A/c (200 x Its 4)	Dr.	800
	To Share Forfeited A/c (200 x Its 3)		600
	To Share Allotment A/c (200 x Its 7)		1400
	To Share First & Final Call A/c (200 x Rs 4)		800
	(BeingForfeiture of 200 shares for non-payment of dues)		
	Case-I		
(i)	Bank A/c	Dr.	2000
	To Share Capital A/c		2000
	(Reissue of 200 forfeited shares reissued at par)		
(ii)	Share Forfeited A/c	Dr.	600
	To Capital Reserve A/c		600
	(BeingShare Forfeited A/c balance is transferred to Capital Reserve A/c)		

As the forfeited shares have been reissued at par therefore no discount is allowed on these shares at the time of their reissue. Therefore, the full forfeited amount of Its 600 is a gain for the company which is transferred to Capital Reserve A/c.

Case II

(i)	Bank A/c	Dr.	1600
	Shares Forfeited A/c	Dr.	400
	To Share Capital		2000
	(BeingReissue of 200 forfeited shares reissued at discount)		
(ii)	Shares Forfeited A/c	Dr	200
	To Capital Reserve A/c		200
	(BeingBalance amount of Shares Forfeited A/c is transferred to Capital Reserve A/c)		

At the time of reissue of forfeited shares, a discount of Rs 2 per share is allowed so the total amount of discount of Rs 400 is adjusted from the forfeited amount of Rs 600 and the balance amount of Rs 200 is transferred to Capital Reserve A/c being a capital gain.

Case III

(i)	Bank A/c	Dr	2400
	To Share Capital A/c		2000
	To Securities Premium A/c		400
	(Being200 forfeited shares reissued at premium)		
(ii)	Share Forfeited A/c	Dr	600
	To Capital Reserve A/c		600
	(BeingBalance amount of Share Forfeited A/c transferred to Capital Reserve).		

As the forfeited shares have been issued at a premium so no amount of discount is there to be adjusted from the forfeited amount hence the total forfeited amount of Rs 600 is transferred to capital Reserve A/c as capital gain of the company.

4. Reissue of forfeited shares at par, premium and discount, originally issued at discount

When the forfeited shares originally issued at discount are reissued, the discount allowed at the time of original issue of such shares which was written back at the time of their forfeiture is again allowed. Thus, on forfeiture shares Discount A/c is credited by the amount of discount allowed at the time of issue because its effect is to be cancelled out when shares were forfeited. When the same shares are reissued, discount on issue of shares A/c is again debited by the original amount of discount.

Example: -

India infrastructure Ltd, has issued its shares of Rs. 20 each at a discount of Rs 2 per share. Mahima holding 100 shares did not pay final call of Rs 5 per share. Her shares were forfeited. Later on, the company reissued 100 shares of these forfeited shares at (I) Rs. 15 per share (II) Rs. 20 per share, and (III) Rs. 25 per share Make journal entries for the forfeiture and reissue of the shares in the books of company.

Solution :

Journal Entries

	Share Capital A/c	Dr	2000
	To Shares Forfeited A/c		1300
	To Discount on Issue of Shares A/c		200
	To Shares Final Call A/c		500
	(Being Forfeiture of 200 shares issued at discount for non-payment of final call)		

I. Reissue of shares: Reissued at Rs 15 per share

(i)	Bank A/c	Dr	1500
	Shares Forfeited A/c	Dr	500
	To Share Capital A/c		2000
	(Being 100 shares reissued at Rs 15 per share)		
(ii)	Shares Forfeited A/e	Dr	800
	To Capital Reserve A/c		800
	(Being balance in share Forfeited A/c transferred to Capital Reserve Ale)		

II. Reissue of shares: Reissued at Rs 20 per share

(i) Bank. A/c Dr 2000

To Share Capital A/c 2000

(Being100 shares reissued at Rs 20 per share)

(ii) Shares Forfeited A/c Dr 1300

To Capital Reserve A/c 1300

(Being balance in shares forfeited A/c transferred to Capital Reserve A/c)

III. Reissued at Rs. 25 per share

(i)	Bank A/c	Dr	2500
	To Share Capital A/c		2000
	To Securities Premium A/c		500
	(Being reissue of discounted shares at Rs 25 per share)		
(ii)	Shares Forfeited A/c	Dr	1300
	To Capital Reserve		1300
	(Being balance in shares forfeited A/c transferred to capital Reserve A/c)		

EXERCISE

A. Choose the correct answer: **(Mark -1)**

1. A company has ....

(A) Separate Legal Entity

(B) Perpetual Existence

(C) Limited Liability

(D) All of the Above

2. Shareholders are:

(A) Customers of the Company

(B) Owners of the Company

(C) Creditors of the Company

(D) None of these

3. Who are the real owners of a company?

(A) Government

(B) Board of Directors

(C) Equity shareholders

(D) Debenture holders

4. A Company is created by:

(A) Special act of the Parliament

(B) Companies Act

(C) Investors

(D) Members

5. An artificial person created by Law is called:

(A) Sole Tradership

(B) Partnership Firm

(C) Company

(D) All of the Above

6. The liability of members in a Company is:

(A) Limited

(B) Unlimited

(C) Stable

(D) Fluctuating

7. Maximum number of members in a private company is:

(A) 7

(B) 200

(C) 20

(D) No Limit

8. Shareholders receive from the company:

(A) Interest

(B) Commission

(C) Profit

(D) Dividend

9. Equity shares can be issued for the purpose of

(A) Cash Receipts

(B) Purchase of assets

(C) Redemption of debentures

(D) Distribution of dividend

10. The portion of the capital which can be cal led-up only on the winding up of the Company is called

(A) Authorised Capital

(B) Called up Capital

(C) Uncalled Capital

(D) Reserve Capital

11. Which of the following is not shown under the heading 'Share Capital' in a Balance Sheet:

(A) Subscribed Capital

(B) Issued Capital

(C) Reserve Capital

(D) Authorised Capital

12. According to Companies Act, Minimum Subscription has been fixed at........of the issued amount.

(A) 25%

(B) 50%

(C) 90%

(D) 100%

13. Persons who start a company are called

(A) Shareholders

(B) Directors

(C) Promoters

(D) Auditors

14. Share Application Account is in the nature of:

(A) Real Account

(B) Personal Account

(C) Nominal Account

(D) None of the above

15. On issue of shares at Premium is:

(A) Profit

(B) Income

(C) Revenue Receipt

(D) Capital Profit

16. Premium on the issue of shares should be shown

(A) On the Assets side of balance sheet

(B) On the Equity & Liabilities side of balance sheet

(C) In profit & loss Statement

(D) None of the Above

17. Amount of Calls in Arrears is shown in the Balance Sheet

(A) as deduction from issued capital

(B) as deduction from subscribed capital

(C) as addition to subscribed capital

(D) on the assets side

18. Amount of Calls in Advance is

(A) Added to Share Capital

(B) Deducted from Share Capital

(C) Shown on the Assets side

(D) Shown on the Equity & Liabilities side

19. Pro-rata allotment of shares is made when there is:

(A) Under subscription

(B) Oversubscription

(C) Equal subscription

(D) As and when desired by directors

20. If applicants for 80,000 shares were allotted 60,000 shares on prorata basis, the shareholder who was allotted 1,200 shares must have applied for:
    (A) 900 Shares
    (B) 3,600 Shares
    (C) 1,600 Shares
    (D) 4,800 Shares
21. If shares of Rs v4,00,000 are issued for purchase of assets of Rs 5,00.000, Rs 1,00,000 will be treated as :
    (A) Discount
    (B) Premium
    (C) Profit
    (D) Loss
22. Forfeiture of shares results in the reduction of :
    (A) Subscribed Capital
    (B) Authorised Capital
    (C) Reserve Capital
    (D) Fixed Assets
23. At the time of forfeiture of shares the share capital account is debited with
    (A) Face value
    (B) Called up value
    (C) Paid up value
    (D) Issued value
24. 600 shares of Rs 10 each were forfeited for non-payment of Rs 2 per share on first call and Rs 5 per share on final call. Share Forfeiture Account will be credited with:
    (A) Rs 1,200
    (B) Rs 1,800
    (C) Rs 3,000
    (D) Rs 4,200
25. Discount allowed on re-issue of forfeited shares is debited to:
    (A) Share Capital A/c
    (B) Share forfeiture A/c
    (C) Statement of Profit & Loss
    (D) General Reserve A/c

26. The balance of the forfeited shares account after re-issue of forfeited shares is transferred to :
    (A) Statement of Profit & Loss
    (B) Share Capital A/c
    (C) Capital Reserve A/c
    (D) General Reserve A/c
27. X Ltd. Company forfeited 300 shares of Rs 10 each, Rs 8 per share called up, on which Mr. A had paid application and allotment money of 06 per share. Share Forfeiture Account will be credited with:
    (A) Rs 600
    (B) Rs 1,800
    (C) Rs 1,200
    (D) Rs 2,400

B. Give the answers of the following questions in one word/ sentence: - (Mark-1)

28. What is the meaning of a company?
29. What is share capital?
30. What do you mean by Authorised Capital?
31. What do you mean by Issued Capital?
32. What do you mean by Called Up Capital?
33. What do you mean by Paid Up Capital?
34. Who are called hareholders?
35. Mention the kinds or classes of shares.
36. What is the Issue of shares?
37. What do you mean by preference shares?
38. What do you mean by equity shares?
39. What is meant by pro-rata allotment of shares?
40. Define the over subscription of shares
41. Define the under-subscription of shares.
42. Give the meaning of minimum subscription?
43. What is calls in advance?
44. What is the Forfeiture of Shares?
45. Give the meaning of 'reissue of shares'.
46. What is the maximum amount of discount at which forfeited shares can be re-issued?
47. What is meant by securities premium reserve'?
48. Give any one purpose for which the amount received as 'securities premium reserve' may be utilised.

C. Give the answers of the following Questions: - **(Marks-4/5/6)**

49. Define company. Explain in brief its characteristics.

50. What is share capital? Explain different types of share capital,

51. Explain different types of companies.

51 What is meant by over subscription of shares? What accounting treatment is given to the amount over subscribed?

53. What is 'Shares Issued at Premium? State the purposes for which Premium amount can be utilised.

54. What is meant by issue of shares at discount? State the conditions to be fulfilled for the issue of shares at discount under the Companies Act.

55. Explain in brief the terms: (i) Calls-in Arrears. (ii) Calls-in Advance

56. State the meaning of forfeiture of shares. When can shares be forfeited?

57. What accounting treatment is given to Securities Premium A/c on forfeiture of shares when:

(i) Amount of premium has been received

(ii) Amount of premium has not been received on such forfeited shares.

58. What amount is transferred to Capital Reserve A/c after reissue of forfeited shares? Why is this account transferred to capital reserve A/c?

D. Numerical Questions:

1. Jute Fabrics Ltd. issued 1,00,000 equity shares of Rs. 10 each on 1st April, 2019. The amount payable on these shares was as under:

Rs 2 per share on application.

Rs 3 per share on allotment.

Rs 5 per share on call.

Make journal entries in the books of company.

2. JPC Ltd. invited application for 10,000 shares of the value of Rs 10 each. The amount is payable as Rs2 on application and Rs 5 on allotment and balance on First and Final Call. The whole of the above issue was applied and cash duly received. Give Journal entries for the above transaction.

3. The Sigma Industries Limited was registered with a capital of Rs 50,00,000. It issued 20,000 equity shares of Rs 100 each payable as Rs 25 on application, Rs 25 on allotment and balance on 1st and final call and 10,000 9% preference shares of Rs 50 each payable as Rs 50 on application and allotment and the balance on two calls of Rs 25 each. All the shares were applied for and allotted. All money was duly received. Make necessary journal entries in the books of the company.

4. The Sun Health Care Ltd has offered to public for subscription 20000 shares of Rs 100 each payable as Rs 30 per share on application, Rs 30 per share on allotment and the balance on call. Applications were

received for 30,000 shares. Applications for 5,000 shares were rejected all together and application money was returned. Remaining applicants were allotted the offered shares. Their excess application money was adjusted towards some due on allotment. Calls were made and duly received. Make journal entries in the books of the company.

5. ABC Ltd. Issued 20,000 Equity shares of Rs 10 each at a premium of Rs 3 payable as follows:

   On Application Rs 4

   On Allotment Rs 5 (including Securities Premium)

   On First Call Rs 2

   On Final Call Rs 2

All shares were duly subscribed and all money duly received. Pass necessary Journal Entries.

6. Royal Cars Ltd. issued 1,00,000 shares of Rs 10 each at a premium of Rs 5 per share, payable as: On application Rs. 4 (including Rs 2 premium) per share

   On allotment Rs 8 (including Rs 3 premium) per share

   On call Rs. 3 per share

Applications were received for 1,00,000 shares and allotment was made to all. Make journal entries.

7. Binayak Co. Ltd. Purchased a machine from HMT Co. for Rs 64,000. It was decided to pay Rs 10,000 in cash and balance will be paid by issue of shares of Rs 10 each.

Pass journal entries when shares

(a) Issued at par

(b) Issued at premium of 20%

8. Advanced Agro Chemical Ltd. was registered with a capital of Rs 50,00,000 divided into 50,000 shares of Rs 100 each. It issued 10,000 shares at discount of Rs 10 per share, payable as:

   Rs 40 per share on application

   Rs 30 per share on allotment

   Rs 20 per share on call.

Company received applications for 15000 shares. Applicants for 12000 shares were allotted 10000 shares and applications for the remaining shares were sent letters of regret and their application money was returned. Call was made. Allotment and call money were duly received. Make journal entries in the books of the company.

9. JIB Software Ltd. offered 50000 shares of Rs 10 each to the public payable as:

   Rs 2 on application

   Rs 3 on allotment

   Rs 2 on First call and the balance as and when required.

All the shares were applied for and duly allotted but Mukesh a shareholder holding 200 shares paid the entire balance on allotment. Make necessary journal entries.

10. Nirmal Ltd. with an authorised capital of Rs.10,00,000, in shares of Rs. 10 each, issued 50,000 of such shares, payable Rs.2 per share on application, Rs. 3 on allotment, Rs.2.50 per share on first call three months later, and duly received. But when the first call of Rs.2.50 was made a shareholder holding 200 shares failed to pay the call money while another shareholder holding 400 shares paid the entire Balance. Give journal entries.

11. XYZ Ltd issued 20000 shares of Rs 10 each payable as Rs 2 per share on application, Rs 5 (including premium of Rs 2 per share) on allotment. Rs 3 per share on first call and the balance on Final Call. All the money was received except the first call money on 400 shares; which was received later on with final call. Make necessary journal entries.

12. A company has offered for subscription to the public 10000 shares of Rs 10 each. It has received applications for 15000 shares. Company has decided to allot shares on prorata basis. Gunakshi holding 200 shares failed to pay allotment money and first call money. Her shares were forfeited:

Amount payable was as under:

Rs 2 per share on application.

Rs 3 per share on allotment.

Rs 5 per share on call.

Make journal entries and prepare Balance Sheet of the company.

13. P.B. Software Ltd. issued Rs 500000 capital divided into equity shares of Rs 10 each. The shares were issued at a premium of Rs 4 per share and were payable as: Rs 3 per share on application, Rs 7 (including premium) per share on allotment and the balance on call. All the shares applied for and were duly allotted. All the money was duly received except on 500 shares on which the call money was not received. Company decided to forfeit these shares. Show the necessary journal entries.

14. The Finest Technology Company Ltd. offered to public for subscription of 50,000 shares of Rs. 20 each at a premium of Rs, 5 per share. The amount was payable as under: On application Rs. 5 per share On allotment Rs. 12 per share (Including premium of Rs 5 per share) On first call Rs. 4 per share On Second and Final call Rs. 4 per share Applications were received for all the shares. Allotment was made to all the applicants in full. Ashima failed to pay allotment and call money on 200 shares held by her. Reshma was allotted 300 shares. She did not pay the call money. Their shares were forfeited. Make necessary journal entries.

15. The Overgrowing Ltd. invited applications for 20,000 shares of Rs. 50 each at a discount of 10% payable as follows: On application Rs. 10 per share on allotment Rs. 20 per share on call Rs. 15 per share Whole of the issue was subscribed and paid for except the calls money on 200 shares which were forfeited by the company. Show the necessary journal entries.

16. Mrs Saha Tea Plantations Ltd. was registered with a capital of Rs 1 crore divided into equity shares of Rs 100 each. The company offered to public 50,000 shares at a premium of Rs 20 per share. The amount on shares was payable as:

Rs 25 on application

Rs 50 (including Rs 20 premium) on allotment

Rs 20 on first call and

Rs 25 on final call.

Applications were received for 75,000 shares. Shares were allotted to the applicants on prorata basis. Surya Kumar who was allotted 500 shares did not pay the allotment money. He also failed to pay the first call. His shares were forfeited. Sheetal was holding 200 shares did not pay the first call. Final call was not made. Make journal entries in the books of the company and also show the necessary working note.

17. Z company Ltd. forfeited 200 shares of Rs 10 each, fully called up on which Rs. 7 have been received and final call of Rs. 3 per share remains unpaid. These shares were later on reissued for Rs. 8 per share fully paid up. Pass journal entries.

18. ABC Ltd. forfeited 400 shares of Rs. 20 each, on which Rs 15 per share have been received and balance remains due but not paid. These shares were reissued

(a) at the rate of Rs 20 per share i.e. at par

(b) at the rate of Rs. 24 per share i.e. at premium

Make necessary journal entries for reissue of the shares.

19. PB Ltd. forfeited 200 shares of Rs 10 each originally issued at a premium of Rs 4 per share, the holder of which paid Rs 3 per share on application but did not pay the allotment money of Rs 7 per share (including premium) and call of Rs. 4 per share. Make necessary journal entries for the forfeiture and for reissue of these shares if:

i. Reissued at Rs 10 per share i.e. at par

ii. Reissued at Rs 8 per share i.e. at discount

iii. Reissued at Rs 12 per share i.e. at premium

20. India infrastructure Ltd. has issued its shares of Rs. 20 each at a discount of Rs 2 per share. Mahima holding 100 shares did not pay final call of Rs 5 per share. Her shares were forfeited. Later on, the company reissued 100 shares of these forfeited shares at (I) Rs. 15 per share (II) Rs. 20 per share, and (III) Rs. 25 per share. Show journal entries for the forfeiture and reissue of the shares in the books of company.

21. A company forfeited 400 shares of Rs 50 each on which only application money of Rs 10 per share and Rs 20 on allotment were received. Final call of the Rs 20 per share is not received. 300 of these shares are reissued at Rs 40 per share. Pass the journal entries.

22. Make journal entries for forfeiture and reissue of shares in the following cases:

(a) The directors of X Ltd. forfeited 400 shares of Rs 10 each fully called up on which Rs 2,400 have been received. 300 of these shares were reissued upon payment of Rs. 2,500

(b) Oracle Estate Developers Ltd. forfeited 500 shares of Rs. 10 each held by Amarjit Singh which were issued at a premium of Rs. 3 per share to be paid along with allotment money. He paid only application money of Rs 3 per share. 200 of these shares were reissued at Rs. 10 per shares

(c) Real Enterprises Ltd. forfeited 200 shares of Rs. 10 each issued at a discount of 10%, on which only Rs.4 per share have been paid. Out of these 100 shares have been reissued at Rs 7 per share.

23. Bijoy Entertain Ltd. issued 1,00,000 shares of Rs 10 each at a premium of Rs 2 per share. The amount was payable as:

Rs 3 per share on application

Rs 5 (including premium) on allotment

Rs 2 per share on first call and

Rs 2 per share on final call

Application were received for 150000 shares. All applications were accepted and allotment was made on prorata basis Sunil who was allotted 1000 shares fail to pay allotment money. On his subsequent failure of first call his shares were forfeited. Goutam who had applied for 750 shares failed to pay the two calls. His shares too were forfeited. All the shares of Sunil and 200 shares of Goutam were reissued at a discount of Rs 2 per share. Make journal entries in the books of the company and open necessary ledger accounts.

24. Singhania Century Cotton Mills Ltd was registered with a capital of Rs 1000000 divided into 1 lakh shares of Rs 10 each. 50000 shares were offered to public for subscription at a discount of Rs 1 per share. The amount was payable as Rs 5 per share on application and allotment and Rs 4 per share on call. Applications were received for 48000 shares. Call was made and money was duly received except on 1000 shares. These shares were forfeited. 800 of forfeited shares were reissued at Rs 12 per share. Make journal entries in the books of the company and Prepare the Balance sheet also.

Answer Key

A. 1. D, 2. B, 3. C, 4. B, 5. C, 6. A, 7. B, 8. D, 9. B, 10. D,
11. C, 12. C, 13. C, 14. B, 15. D, 16. B, 17. B, 18. D, 19. B, 20. C,
21. B, 22. A, 23. B, 24. B, 25. B, 26. C, 27. B

D. **Numerical Answer :**

6. a) No. of shares to be issued – 5,400
   b) No. of shares to be issued – 4,500

12. Net unpaid amount on allotment – ₹ 4,500
    Balance sheet total – ₹ 98,600

13. Share forfeited A/c – ₹ 3,000

14. Share forfeited A/c – ₹ 4,600

15. Share forfieited A/c – ₹ 6,000

16. Share forfeited A/c – ₹ 18,750

17. Capital Reserve A/c – ₹ 1,000

18. a) Capital Reserve A/c – ₹ 6,000
    b) Capital Reserve A/c – ₹ 6,000

19. i. Capital Reserve A/c – ₹ 600
    ii. Capital Reserve A/c – ₹ 200
    iii. Capital Reserve A/c – ₹ 600

20. i . Capital Reserve A/c – ₹ 1,000
    ii. Capital Reserve A/c – ₹ 1,300
    iii. Capital Reserve A/c – ₹ 1300

21. Capital Reserve A/c – ₹ 600

22. (a) Capital Reserve A/c – ₹ 1,300
    (b) Capital Reserve A/c – ₹ 600
    (c) Capital Reserve A/c – ₹ 200

23. Capital Reserve A/c – ₹ 1,800

24. Capital Reserve A/c – ₹ 4,000

CHAPTER -2

Issue and Redemption of Debenture

MEANING OF DEBENTURES:-

The term 'debenture' is derived from the Latin word `debere' which refers to borrow. A debenture is a document that either creates a debt or acknowledges it. In corporate finance, the term is used for a medium-to long-term debt instrument used by large companies to borrow money. According to the section 2(30) of The Companies Act, 2013 'Debenture' comprises of— Debenture Inventory, Bonds and any other securities of an enterprise whether comprising a charge on the assets of the enterprise or not.

DISTINCTION BETWEEN SHARE AND DEBENTURE:-

Basis	Share	Debenture
Meaning	Share means share capital of the company. Share Capital is the Internal Liability of the firm.	Debenture means Loan or debt of the company. Debenture is the external liability of the firm
Holder	The Owner Of The Share Is Called Shareholder	The Owner Is Called Debenture Holder
Return Policy	Receive Dividend Announced By The Company	Based On Fixed Or Floating Interest Rates, A Return Is Paid On Maturity
Status	Shareholders Enjoy Ownership Status In The Company	Treated As Lenders
Conversi ons	Can't Convert Equities Into Debentures	Can Be Converted Easily To Equities
Risk	High Risk	Secured Investment
Voting Rights	Shareholders Have Voting Rights In The Company	Debenture Holders Don't Have Any Rights To Vote

DIFFERENT TYPES OF DEBENTURES:

1. **From the Point of view of Security:-**

A. **Secured Debentures :** The debentures, which are secured fully or partly by a charge over the assets of the company, are called secured debentures. The charge may be either a fixed charge or a floating charge.

B. Unsecured Debentures : The debentures, which are not secured fully or partly by a charge over the assets of the company, are called unsecured debentures. The general solvency of the company is the only security for the holders. The debenture holders are treated as only unsecured creditors.

2. From the Point of view of Tenure:-

A. Redeemable Debentures : These debentures are those debentures that are due on the cessation of the time frame either in a lump-sum or in instalments during the lifetime of the enterprise. Debentures can be reclaimed either at a premium or at par.

B. Irredeemable Debentures : These debentures are also called as Perpetual Debentures as the company doesn't give any attempt for the repayment of money acquired or borrowed by circulating such debentures. These debentures are repayable on the closing up of an enterprise or on the expiry (cessation) of a long period.

3. From the Point of view of Convertibility:-

A. Convertible Debentures : Convertible debenture holders have an option of converting their holdings into equity shares. The rate of conversion and the period after which the conversion will take effect are declared in the terms and conditions of the agreement of debentures at the time of issue. These debentures are either entirely convertible or partly changeable.

B. Non-Convertible Debentures : Non-convertible debentures are simple debentures with no such option of getting converted into equity. Their state will always remain of debt and will not become equity at any point in time. It is essential to prepare an agreement that clearly expresses all the terms and conditions. Most debentures circulated by enterprises fall in this class.

4. From Coupon Rate Point of view:-

A. Specific Coupon Rate Debentures : Such debentures are issues with a specified rate of interest, and it is known as the coupon rate. The specified rate of interest may either fixed or floating. The floating interest rate is usually linked with the bank rate.

B. Zero-Coupon Rate Debentures : These debentures don't normally carry a particular rate of interest. In order to restore the investors, such types of debentures are issued at a substantial discount and the difference between the nominal value and the issued price is treated as the amount of interest associated to the period of the debentures.

5. From the view Point of Registration:-

A. Registered Debenture : A registered debenture is recorded in the register of debenture holders of the company. These debentures are such debentures within which all details comprising addresses, names and particulars of holding of the debenture holders are filed in a register kept by the enterprise. Such debentures can be moved only by performing a normal transfer deed.

B. Bearer Debentures : These debentures are debentures which are transferable by mere delivery. The company keeps no records of such debenture holders.

ISSUE OF DEBENTURES:-

By issuing debentures means issue of a certificate by the company under its seal which is an acknowledgment of debt taken by the company.

The procedure of issue of debentures by a company is similar to that of the issue of shares. A Prospectus is issued, applications are invited, and letters of allotment are issued. On rejection of applications, application money is refunded. In case of partial allotment, excess application money may be adjusted towards subsequent calls.

Issue of Debenture takes various forms which are as under:

1. Debentures issued for cash
2. Debentures issued for consideration other than cash
3. Debentures issued as collateral security.

1. DEBENTURES ISSUED FOR CASH:-

Debentures in the general course of business are issued for cash. This issue of debentures that happens can be of three kinds, just like an issue of shares, at par, at a discount, and at a premium.

i) Issue of Debenture at Par : Here the debentures will be issued exactly at their nominal price, i.e. not above or below the face value of the debentures. Now the company can decide to collect the cash all at once, in a lump sum. Or the money will be collected in instalments, like with allotment, first call, second call, last call etc. Let us see the accounting journal entries for both these cases.

(A) Money Received in One Instalment:

	Particulars		Amount	Amount
(a)	Bank Ale	Dr	xxx	
	To Debenture Application & Allotment			xxx
	(Being amount received in one installment)			

	Particulars		Amount	Amount
(b)	Debenture Application & Allotment A/c	Dr	xxx	
	To Debenture A/c			xxx
	(Being allotment being done)			

(B) Being Money Received in Two or More Instalments:-

	Particulars		Amount	Amount
(a)	Bank A/c	Dr	xxx	
	To Debenture Application A/c			xxx
	(Being amount received on application)			

Particulars			Amount	Amount
(b)	Debenture Application A/c	Dr	xxx	
	To Debenture A/c			xxx
	(Being allotment done)			

Particulars			Amount	Amount
(c)	Debenture Allotment A/c	Dr	xxx	
	To **Debenture** A/c			xxx
	(Being allotment money due)			

Particulars			Amount	Amount
(d)	Bank Aic	Dr	xxx	
	To Debenture Allotment A/c			xxx
	(Being allotment money received)			

ii) Issue at Discount :

When the debentures are issued at below face value, such issue of debentures is known as a discount issue. Like, say for example the debenture has a nominal value of 100/- but is issued for 90/, Then such debentures are said to be issued at discount.

Discount on issue of debentures is treated as a capital loss and put under "Miscellaneous Expenses" on the asset side of the balance sheet until it can be written off. Then during the life of the debentures, such discount amount is written of by debiting it to the Profit and Loss A/c. It can also be charged against the Capital Profits of the company. The accounting entries for the issue of debentures on discount and the writing of the expense are as below-

Particulars			Amount	Amount
(a)	Debenture Allotment A/c	Dr	xxx	
	Discount on Debenture A/c	Dr	xxx	
	To Debenture A/c			xxx
	(Being allotment money due)			

Particulars			Amount	Amount
(b)	Bank A/c	Dr	xxx	
	To Debenture Allotment A/c			xxx
	(Being allotment money received)			

Particulars			Amount	Amount
(c)	Profit and Loss A/c	Dr	xxx	
	To Discount on Debenture A/c			xxx
	(Being discount written off)			

iii) Issue at Premium:

Now we come to the issue of debentures at a premium, that is when more money than the nominal value is charged. So if a debenture with a face value of 100/- is sold at 1101- then it is issued at a premium. The amount of the premium is charged to a special account known as Securities Premium Reserve Account. This account will be shown on the liabilities side of the Balance Sheet under the heading of Reserves and Surplus.

The accounting entries for the issue of debentures at a premium will be as below-

Particulars			Amount	Amount
(a)	Debenture Allotment/call A/c	Dr	xxx	
	To Debenture A/c			xxx
	To Securities Premium A/c			xxx
	(Being allotment/call money due)			

Particulars			Amount	Amount
(b)	Bank A/c	Dr	xxx	
	To Debenture Allotment/Call A/c			xxx
	(Being allotment/call money received)			

2. DEBENTURES ISSUED FOR CONSIDERATION OTHER THAN CASH :

When a company purchases some assets and issues debentures as a payment for the purchase, to the vendors it is known as issue of debentures for consideration other than cash. Debentures can be issued to vendors at par, at premium and at discount

Accounting Treatments:

i) On Purchase of Assets

Sundry Assets A/c Dr (Individually)

To Vendors A/c

(Purchase of assets)

ii) On Issue of debentures

(a) At par

Vendors' A/c Dr

To Debentures A/c

(issue of debentures at par to vendors)

(b) At discount

Vendors' A/c Dr

Debentures Discount A/c Dr

To Debentures A/c

(Issue of debentures to vendors at a discount of Rs ... per debenture)

(c) At premium

Vendors' A/c Dr

To Debentures A/c

To Securities Premium A/c

(Issue of debentures to vendors at a premium of Rs per debenture)

3. DEBENTURES ISSUED AS COLLATERAL SECURITY:

Collateral security means security given in addition to the principal security. It is a subsidiary or secondary security. Whenever a company takes loan from bank or any financial institution it may issue its debentures as secondary security which is in addition to the principal security. Such an issue of debentures is known as 'issue of debentures as collateral security'. The lender will have a right over such debentures only when company fails to pay the Ioan amount and the principal security is exhausted. In case the need to exercise this right does not arise debentures will be returned back to the company. No interest is paid on the debentures issued as collateral security because company pays interest on loan.

In the accounting books of the company issue of debentures as collateral security can be credited in two ways.

(i) No journal entry to be made in the books of accounts of the company:

Debentures are issued as collateral security. A note of this fact is given on the liability side of the balance sheet under the heading Secured Loans and Advances.

(ii) Entry to be made in the books of account the company:

However, if some companies opt to pass an entry to record such a transaction, the following entries may be passed -

	Particulars		Amount	Amount
(a)	Debenture Suspense A/c	Dr	xxx	
	To Debenture A/c			xxx
	(Being debentures issued as a collateral security)			

	Particulars		Amount	Amount
(a)	Debenture A/c	Dr	xxx	
	To Debenture Suspense A/c			xxx
	(Being debentures cancelled on repayment of the loan)			

OVER SUBSCRIPTION OF DEBENTURES :-

Company if receives applications for number of debentures that exceed the number of debentures offered for subscription, it is called over subscription. There can be following treatment of the excess application money received:

(a) The total amount of excess number of applications is refunded in case the applications are totally rejected.

(b) The amount of excess application money is totally adjusted towards amount due on allotment and calls

— in case partial allotment is made,

— the excess amount is adjusted towards sums due on allotment and rest of the amount is refunded. Journal entries in the above cases will be as follows :

For refund of money if the applications are rejected:

Debentures Application A/c Dr

To Bank A/c

(Refund of money on rejected applications)

For adjustment of excess application money adjusted towards sum due on allotment :

Debentures Application A/c Dr

To Debentures Allotment A/c

(Excess application money adjusted)

TERMS OF ISSUE AND REDEMPTION OF DEBENTURES:-

Redemption of debentures refers to the repayment of these debentures by the company to the debenture holders. So the company will discharge its liability and remove it from the balance sheet. This is a major transaction for the company since the amount of money involved tends to be quite significant.

There are a few ways in which this redemption of shares can take place. These methods all have different accounting treatment as well. So let us take a look at the six (06) methods of redemption of debentures.

1. Issued at Par & Redeemable at Par :

	Particulars		Amount	Amount
(a)	Bank A/c	Dr	xxx	
	To Debenture Application & Allotment A/c			xxx
	(Being application money received)			

	Particulars		Amount	Amount
(b)	Debenture Application &			
	Allotment A/c	Dr	xxx	
	To Debentures A/c			
	(Being application money transfered)			xxx

2. Issued Discount & Redeemable at Par :

	Particulars		Amount	Amount
(a)	Bank A/c	Dr	xxx	
	To Debenture Application &			
	Allotment A/c			xxx
	(Being allotment money received)			

	Particulars		Amount	Amount
(b)	Debenture Application			
	Allotment A/c	Dr	xxx	
	Discount on Debenture A/c	Dr		xxx
	To Debenture A/c			xxx
	(Being allotment of debentures at discount)			

3. Issued at Premium & Redeemable at Par:

	Particulars		Amount	Amount
(a)	Bank A/c	Dr	xxx	
	To Debenture Application			
	& Allotment/Call A/c			xxx
	(Being allatment/call money received)			

	Particulars		Amount	Amount
(b)	Debenture Application &			
	Allotment/Call A/c	Dr	**xxx**	
	To Debenture A/c			xxx
	To Securities Premium A/c			xxx
	(Being allotment of debentures at premium)			

4. Issue at Par & Redeemable at Premium:

	Particulars		Amount	Amount
(a)	Bank. A/c	Dr	xxx	
	To Debenture Application & Allotment A/c			xxx
	(Being application money received)			

	Particulars		Amount	Amount
(b)	Debenture Application & Allotment A/c	Dr	xxx	
	Loss on Issue of Debentures	Dr		xxx (premium amount)
	To Debentures A/c			xxx (nominal value)
	To Premium on Redemption of Debenture A/c			xxx (premium amount)
	(Allotment of debentures at par, redeemable at premium)			

5. Issued at Discount & Redeemable at Premium :

	Particulars		Amount	Amount
(a)	Bank A/c	Dr	xxx	
	To Debenture Application & Allotment A/c			xxx
	(Being application money received)			

	Particulars		Amount	Amount
(b)	Debenture Application & Allotment A/c	Dr	xxx	
	Loss on Issue of Debentures	Dr	xxx (discount amout + premium on redemption)	
	To Debentures A/c			xxx (nominal value)
	To Premium on Redemption of Debenture A/c			xxx (premium amount)
	(Allotment of debentures at discount, redeemable at premium)			

6. Issued at Premium & Redeemable at Premium:

	Particulars		Amount	Amount
(a)	Bank A/c	Dr	xxx	
	To Debenture Application			
	&Allotment A/c			xxx
	(Being application money received)			

	Particulars		Amount	Amount
(b)	Debenture Application			
	& Allotment A/c	Dr	xxx	
	Loss on Issue of Debentures	Dr		xxx (premium amount)
	To Debentures A/c			xxx (nominal value)
	To Securities Premium A/c			xxx (premium on issue)
	To Premium on Redemption			
	of Debenture A/c			xxx (premium on redemption)
	(Allotment of debentures at premium, redeemable at premium)			

MEANING OF INTEREST ON DEBENTURES :-

An interest paid is a reward to all the debenture holders for investing in the debentures of an enterprise. Generally, interest is paid in a periodical systematic way at a fixed rate of interest on the face value of the debentures and is being treated as a charge on the profits.

Accounting treatment of Interest on Debenture:

1. When interest is due and tax is deducted at source:

Interest on Debentures A/c Dr.

To Debentureholders' A/c

To Income Tax Payable A/c

(Amount of interest due on debenture and tax deducted at source)

2. For payment of interest to debenture holders:

Debentureholders A/c Dr.

To Bank A/c

(Amount of interest paid to debentureholders)

3. **On transfer debenture Interest Account to statement of Profit and Loss :**

Statement of Profit and Loss Dr.

To Interest on Debentures Aic

(Debenture interest transferred to profit and loss A/c)

4. **On payment of tax deducted at source to the Government :**

Income Tax Payable A/c Dr.

To Bank Aic

(Payment of tax deducted at source on interest on debentures)

WRITING OFF DISCOUNT/ LOSS ON ISSUE OF DEBENTURES :-

The loss or discount on the issue of debentures is typically a capital loss or a fictitious asset and, hence, has to be written-off during the debentures' lifetime. The amount of loss or discount on issue of debentures has to be not be written-off during the year of its issue since the benefit of the debentures would accumulate to the enterprise till their restitution or redemption.

There are two procedures, which can be accepted for writing off loss or discount on issue of debentures against the revenue profits. They are as follows:

(A) Fixed Instalment Method

(B) Fluctuating Instalment Method:

METHODS of REDEMPTION OF DEBENTURES:-

Redemption of debentures refers to payment of the amount of debentures by the enterprise. When debentures are reclaimed, liability on account of debentures is being discharged.

There are 4 ways by which the debentures can be redeemed. Namely:

(i) Payment in lump sum

(ii) Payment in instalments

(iii) Purchase in the open market

(iv) By conversion into shares or new debentures

(i) Payment in lump sum: The enterprise reclaims the debentures by paying the fund in lump sum (round sum) to the debenture holders during the maturity hereof as per the terms and conditions of issue.

When the company pays the whole amount in lump stun, the following journal entries are recorded in the books of the company:

1. **If debentures are to be redeemed at par**

(a) Debentures A/c Dr.

To Debentureholders

(b) Debentureholders Dr.

To Bank A/c

2. If debentures are to be redeemed at premium

(a) Debentures A/c Dr.

Premium on Redemption of Debentures A/c Dr.

To Debentureholders

(ii) Payment in instalments: Under this method, usually redemption of debentures is paid in instalments on the particular date during the time in the position of the debentures. The total amount of debenture liability is being divided by the total number of years. This must be noted that the authentic debentures reclaimable are recognised by the sources of drawing the required number of lots out of the debentures outstanding for the payment.

1. If redeemed out of capital

(a) Debentures A/c Dr.

To Debentureholders A/c

(b) Debentureholders A/c Dr.

To Bank A/c

2. If redeemed out of profits

(a) Statement of profit & Loss A/c Dr.

To Debenture Redemption reserve A/c

(b) Debentures A/c Dr.

To Debentureholders A/c

(c) Debentureholders A/c Dr.

To Bank A/c

(iii) Purchase in the open market: When an enterprise buys its own debentures for the aim of cancellation, such an act of buying and cancelling the debentures comprises redemption of debentures by purchase in the open marketplace.

When the debentures are purchased from the market at a discount and cancelled, the journal entries are recorded as follows :

1. On purchase of own debentures for immediate cancellation

Debentures A/c Dr.

To Bank A/c

To Profit on Redemption of Debentures A/c

2. **On transfer of Profit on Redemption**

Profit on Redemption **of** Debenture A/c Dr.

To Capital Reserve

In case, the debentures are purchased from the market at a price which is above the nominal value of debenture, the excess will be debited to loss on redemption of debentures. The journal entry in that case will be

1. Debentures A/c Dr.

   Loss on Redemption of Debentures A/c Dr.

   To Bank A/c

2. Statement of profit and loss Dr.

   To Loss on Redemption of Debentures A/c

(iv) By Conversion into shares or new debentures : An enterprise can reclaim its debentures by transforming them into a new class of debentures or shares. If debenture holders find that the proffer is useful to them, they can exercise their right of transforming their debentures into new class of debentures or shares. These new shares or debentures can be either circulated at a premium, at a discount or at par. It may be noted that this method is applicable only to convertible debentures.

Sinking Fund — Method of redemption of Debenture:-

This is very important method of redemption of debenture. Sinking fund means take one part of profit for repayment of debenture. This is calculated with sinking fund table. This is invested in such scheme which gives us Lumsum amount so that we can easily repay the debenture without any tension. This is very popular and scientific method of redemption of debenture. In this method we open the sinking fund and sinking fund investment account. Sinking fund's other name is also Debenture Redemption Fund Account.

A. Multiple Choice Questions:- **(Marks : 1)**

1. Debenture holders are -

   (A) Promoters of the Company (B) Debtors of the Company

   (C) Creditors of the Company (D) Owners of the Company

2. Debentures represent the :

   (A) Long-term Borrowings of a Company (B) Directors' shares in a company

   (C) The Investment of Equity-Shareholders (D) Short-term Borrowings of a Company

3. A debenture holder is entitled to :

   (A)Share in profits (B) Fixed dividend

   (C) Voting rights in the company (D) Interest at the fixed rate

4. Interest payable on debentures is :

(A) An appropriation of profits of the company

(B) A charge against profits of the company

(C) Transferred to general reserve

(D) Transferred to sinking fund investment account

5. Which of the following is not a characteristic of Bearer Debentures?

(A) They are treated as negotiable instruments.

(B) Their transfer requires a deed of transfer.

(C) The interest on it is paid to the holder irrespective of identity.

(D) They are transferable by mere delivery.

6. The Principal amount of debentures will be repaid by the company either at the end of a specified period or by instalments during the life time of the company. Such types of debentures are called:

(A) Redeemable Debentures (B) Bearer Debentures

(C) Convertible Debentures (D) Irredeemable Debentures

7. The debentures whose principal amount is not repayable by the company during its life time, but the payment is made only at the time of Liquidation of the company, such debentures are called:

(A) Bearer Debentures (B) Non-Convertible Debentures

(C) Irredeemable Debentures (D) Redeemable Debentures

8. Debenture Application Account is in the natutre of

(A) Nominal Account (B) Personal Account

(C) Real Account (D) None of the above

9. Discount on issue of Debentures is in the nature of

(A) Deferred Revenue Expenditure (B) Capital loss

(C) Revenue loss (D) None of the above

10. Debentures of a Company can be issued :

(A) As a Collateral Security (B) For Consideration other than Cash

(C) For Cash (D) Any of the above

11. Premium on Redemption of Debentures Account is :

(A) Personal Account (B) Nominal Account

(C) Real Account (D) All of the Above

12. Zero Coupon Bonds are issued:

(A) At Zero Interest Rate (B) With Specified Rate of Interest

(C) Without Specified Rate of Interest (D) None of These

13. On liquidation of company, principal amount of debentures is returned:

(A) Last of All (B) First of All

(C) Before Equity Capital (D) After Equity Capital

14. Premium received on issue of debentures may be utilised for

(A) For writing off discount allowed on issue of shares

(B) For writing off preliminary expenses

(C) For writing off premium allowed on redemption of debentures

(D) For All of the Above

15. On issue of debentures as a collateral security, which account is credited?

(A) Debentures Account (B) Debenture Suspense Account

(C) Debenture Holdings Account (D) Bank Loan Account

B. Give the answers of the following questions in one word / sentence:- (Mark -1)

16. What do you mean by debenture?
17. What is meant by issue of debentures as a collateral security?
18. Why would an investor prefer to invest in the debentures of a company rather than in its share?
19. What do you mean by Redemption of Debentures?
20. Give the meaning of interest on debentures?
21. What do you mean by Debenture holders?
22. Define redeemable debentures?
23. What do you mean by Convertible debentures?
24. Define Secured Debentures?
25. Define Unsecured Debentures?

C. Give the answers of the following questions:- (Marks - 4/5/6)

26. What do you mean by debenture? What are the differences between shares and debentures?
27. Discuss about different types of Debentures?
28. What is meant by debentures issued as collateral security? How is it treated in the books of accounts of the company?

29. What is the accounting treatment in the following cases:

(a) Debentures are issued at premium (b) Debentures are issued at discount

(c) Debentures are issued in consideration other than cash

30. Explain the guidelines of SEBI for creating Debenture Redemption Reserve.

31. What is meant by conversion of debentures? Describe the method of such a conversion.

32. Can a company purchase its own debentures in the open market? Explain.

D. Numerical Questions:-

33. Sun India Ltd. issued 5,000 8% Debentures of Rs 100 each payable as follows

Rs 20 on Application

Rs 30 on Allotment

Rs. 50 on First and Final call

All the debentures were applied for and allotted. All the calls were duly received. Make necessary journal entries in the books of the company.

34. ABC Ltd. company has issued 5,000 10% Debentures of Rs 100 each at a premium of 20% payable as Rs 60 on application, Rs 60 on allotment (including premium). All the debentures were subscribed for and money was duly received. Show the journal entries.

35. B. Ltd. company has issued 2,000 9% debentures of Rs 100 each at a discount of 10% payable as Rs 40 on application, Rs 50 on allotment. Show the necessary journal entries.

36. JBC Ltd. purchased machinery for Rs 1,98,000 and issued 9% debentures of Rs 100 each to the vendors. Make journal entries if the debentures were issued :

(a) at par

(b) at a premium of Rs 10

(c) at a discount of Rs 10.

37. Surya Ltd. purchased assets of the book value of Rs. 8,00,000 and took over the liability of Rs. 2,80,000 from Mohan Bros. It was agreed that the purchase consideration, settled at Rs. 5,40,000. to be paid by issuing debentures of Rs. 100 each. What Journal entries will be made in the following three cases, if debentures are issued: (a) at par; (b) at premium of 20%; (c) at 10% discount. It was agreed that any fraction of debentures be paid in cash.

38. Sky Rocketing Company Ltd issued 6,000 10% debentures of Rs 100 each to the bank as collateral security against a loan of Rs 5,00,000 taken from the bank. Record the issue of debentures in the books of the company and show the issued Debentures in the Balance Sheet of the Company.

39. Kohima Ltd. taken a loan from S.B.I. of Rs. 4,00,000 for a period of 6 years @10% p.a. The loan is secured by a mortgage of plant and machinery since S.B.I. was not satisfied with security of plant and

machinery, the company issued 1,00,000, 10% Debentures of Rs.100 each as collateral security. Record necessary journal entries in the books of Kohima Ltd. including payment of interest on loan taken from S.B.I. for the first year. How will this loan from S.B.I. and issue of debentures as collateral security be reported in the books of company?

40. MG Ltd. issued 10% debentures (Rs.100 each) of Rs. 8,00,000 which were as follows:

    (i) Rs.4, 00,000 (nominal) for cash @90%

    (ii) To a vendor for Rs. 80,000 capital expenditure in satisfaction of his claim Rs.2,00,000 (nominal).

    (iii) To a banker for a loan of Rs. 1, 20,000 as collateral security Rs. 2,00,000 (nominal).

    The issue (i) and (ii) are redeemable at the end of 10 years at par.

    Pass necessary journal entries in the books of the company.

41. ABC Ltd. issued 75,000, 12% Debentures of ₹ 100 each on the basis of the following cases :

    (i) Debentures issued at par, redeemable at par.

    (ii) Debentures issued at discount of 5% and redeemable at par, at the end of 5 years.

    (iii) Debentures issued at premium of 10% and redeemable at par, at the end of 5 years.

    (iv) Debentures issued at par and redeemable at a premium of 10%, at the end of 10 years.

    (v) Debentures issued at a discount of 5% and redeemable at a premium of 10%, at the end of 5 years.

    (vi) Debentures issued at a premium of 10% and redeemable at a premium of 5%, at the end of 10 years.

    Pass necessay journal entries to record the above mentioned cases at the time of issue of debentures and prepare the Balance Sheet for each.

42. Give the Journal entries in each of the following alternative cases :

    (i) Issue of ₹ 1,00,000; 8% debentures of ₹ 100 each at par and redeemable at par.

    (ii) Issue of ₹ 1,00,000; 8% debentures of ₹ 100 each at a discount of 5% and redeemable at par.

    (iii) Issue of ₹ 1,00,000; 8% debentures of ₹ 100 each at a premium of 5% and redeemable at par.

    (iv) Issue of ₹ 1,00,000; 8% debentures of ₹100 each at par and redeemable at 110%.

    (v) Issue of ₹ 1,00,000; 8% debentures of ₹ 100 each at a discount of 5% and redeemable at a premium of 10%.

    (vi) Issue of ₹ 1,00,000; 8% debentures of ₹ 100 each at a premium of 5% and redemable at a premium of 10%.

ANSWER KEY

1. C, 2. A, 3. D, 4. B, 5. B, 6. A, 7. C, 8. B, 9. B, 10. D,
11. A, 12. C, 13. C, 14. D, 15. A

36. b. No. of debentures issued - 1,800

    c. No of debentures issued - 2,200

37. Amount of Goodwill - ₹ 20,000

    a) – No of debentures issued - 5,400

    b) – No of debentures issued - 4,500

    c) – No of debentures issued - 6,000

41. i) 12% Debentures A/c – ₹75,00,000

    ii) Discount on issue of Debenture A/c – ₹3,75,000

    iii) Securities Premium Reserve A/c – ₹ 7,50,000

    iv) Loss on issue of Debenture A/c – ₹ 7,50,000

    v) Loss on issue of Debenture A/c – ₹ 11,25,000

    vi) Securities Premium Reserve A/c – ₹ 7,50,000
    Loss on issue of Debenture A/c – ₹ 3,75,000

42. i) 8% Debentures A/c – ₹ 1,00,000

    ii) Discount on Issue of Debentures A/c – ₹ 5,000

    iii) Securities Premium Reserve A/c – ₹ 5,000

    iv) Loss on issue of Debentures A/c – ₹ 10,000
    Premium on Redemption of Debenture A/c – ₹ 10,000

    v) Loss on issue of Debentures A/c – ₹15,000
    Premium on Redemption of Debentures A/c – ₹ 10,000

    vi) Loss on issue of Debenture A/c – ₹ 10,000
    Securities Premium Reserve A/c – ₹ 5,000
    Premium on Redemption of Debenture A/c – ₹ 10,000

CHAPTER - 3

Financial Statements of A Company

Meaning of financial statements

Financial statements are prepared by the business firms at the end of an accounting period to ascertain the operating results and the financial position. The basic financial statements are Income statement and Balance sheet. Trading and profit and loss account shows the net results of the business and Balance sheet is a statement of assets and liabilities which shows the financial position of a business firm.

Features of financial statements

Following are the features of financial statements:

(i) Financial statements are generally prepared at the end of an accounting period.

(ii) These statements are made for the firm as a whole.

(iii) Information's are presented in a expressive way by grouping items of same nature for example, fixed assets and current assets.

(iv) Financial statements are prepared on the basis of historical cost.

(v) Financial statements are prepared on the basis ofaccounting principles and Standards, which makesthe financial statements more comparable and accurate.

Objectives of Financial Statements

Following are the Objectives of Financial Statements:

1. To provide information about economic resources and obligations of a business: They are prepared to provide sufficient, dependable and periodical information about financial resources and responsibilities of a business concern to investors and other outside parties who are having limited authority, ability or resources to obtain information.
2. To provide information about the earning capacity of a business: They are to provide useful financial information which can be profitably used to forecast, compare, and assess the earning capacity of the business firm.
3. To provide information about cash flows: They are to provide useful information to investors and creditors for forecasting, comparing and assessing, potential cash flows in terms of amount, time and related uncertainties.
4. To judge effectiveness of management: They supply valuable information for judging management's ability to use the resources of a business concern efficiently.
5. To provide Information about the activities of a business affecting the society: They have to report the activities of the business firm affecting the society, which can be determined and measured and which are essential for its social environment.

Significance of financial statements

The significance of financial statements to various interested parties are as follows:

(i) **To management:** Financial statements provide information to the management to take different decision and to have control over business various activities.

(ii) **To shareholders:** Financial statements help the shareholders to know whether the business firm has potential for growth and expansion.

(iii) **To Investors:** Financial statements help to value the securities and compares it with business firms before taking any kind of investment decisions.

(iv) **To creditors:** Financial statements help the Creditors to get information about the ability of the business firm to repay their dues.

(v) **To government:** Financial statements are necessary for the government to measure the tax liability of business and to amend industrial policies.

Limitations of financial statements

Following are the limitations of financial statements:

(i) **Ignore qualitative aspects** Qualitative aspects that is non-monetary information is also important for various business decisions. For example, efficiency of employees, competence of management, **etc.** ignored in the financial statements.

(ii) **Historical data:** Financial statements are prepared on the basis of historical data. They may not reflect the present position.

(iii) **Ignore inflationary Effects; Adjustments for price level changes are not made in** the financial statements. Hence, financial statements may not disclose the current position.

(iv) **Lack of consistency:** Various business firms may use various accounting method. Hence, comparison between two business firms becomes difficult.

(v) **Only interim reports:** Financial statements are prepared at the end of every accounting period, But, the actual position of the business can be known only when the business is shut down. That's why, financial statements may not reveal the exact position of the business firm.

Format of statement of Profit and Loss A/c

Proforma of Statement of Profit and Loss

Name of the Company....................

Statement of Profit end Loss

for the year ending..................

	Particular	Note No.	Figures for the Current Reporting Period	Figures for the previous Reporting Period
I.	Revenue from Operations		....	....
II	Other Income		....	....
III	Total Revenue (I+II)		....	....

IV	Expenses			
	Cost of Materials Consumed		....	....
	Purchases of Stock-in-trade		....	....
	Changes in Inventories of Finished Goods		....	....
	Work-in-progress and Stock-in-trade		....	....
	Employees Benefits Expenses		....	....
	Finance Costs		....	....
	Depreciation and Amortisation Expenses		....	....
	Other Expenses		....	....
V	Profit before Exceptional and Extraordinary			
	Items and Tax (III-IV)		....	....
*VI	Exceptional Items		....	....
*VII	Profit before Extraordinary Items and Tax (V-VIII)		....	....
*VIII	Extraordinary Items		....	....
IX	Profit before Tax (VII-VIII)		....	....
X	Tax Expenses			
	(1) Current Tax		....	....
	(2) Deferred Tax		....	....
XI	Profit(Loss) for the Period form			
	Continuing Operations(VII-VIII)		....	....
XII	Profit (Loss from Discontinuing Operations		....	....
XIII	Tax Expense of Discontinuing Operations		....	....
XIV	Profit(Loss) from Discontinuing Operations			
	(After tax) (XII-XIII)		....	....
XV	Profit(Loss) for the Period (XI-XIV)		....	....
XVI	Earnings per Equity Share			
	(1) Basic		....	....
	(2) Diluted		....	....

Format of Balance Sheet :-

Name of the Company....................

Balance Sheet

as at ....

Particular	Note No.	Figures for the Current Reporting Period	Figures for the previous Reporting Period
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		....	....
(b) Reserves and Surplus		....	....
*(c) Money Received Against Share Warrants		....	....
***2 Share Application Money Pending Allotment**			
3. Non-current Liabilities			
(a) Long-term Borrowings		....	....
*(b) Deferred Tax Liabilities (Net)		....	....
*(c) Other Long-term Liabilities		....	....
(d) Long-term Provisions		....	....
4. Current Liabilities			
(a) Short-term Borrowings		....	....
(b) Trade Payables		....	....
(c) Other Current Liabilities		....	....
(d) Short-term Provisions		....	....
Total			
II. ASSETS			
1. Non-current Assats			
(a) Fixed Assets			
(i) Tangible Assets		....	....
(ii) Intangible Assets		....	....
*(iii) Capital Work-in-progress		....	....
*(iv) Intangible Assets Under Development		....	....
(b) Non-cur rent Investments		....	....
*(c) Deferred Tax Assets (Net)		....	....
(d) Long-term Loans and Advances		....	....
*(e) Other Non-current Assets		....	....

2. Current Assets			
(a) Current Investments		....	....
(b) Inventories		....	....
(c) Trade Receivables		....	....
(d) Cash and Cash Eq uivalents		....	....
(e) Short-term Loans and Advances		....	....
(f) Other Current Assets		....	....
Total			

* (The accounting treatment of star marked items will not be evaluated.)

Short Answer Questions -

1. Name any four parties interested in Financial statements.
2. Name the basic financial statements of a company.
3. What are contingent liabilities?
4. What is position statement?
5. Name the major headings under which Liabilities side of the Balance Sheet is organized and presented.
6. Define Profit and Loss A/c.
7. What is Balance Sheet?
8. Name the major headings under which Asset side of the Balance Sheet is organized and presented.
9. Define operating Cycle.
10. What is cash and cash equivalents?

MULTIPLE CHOICE QUESTIONS -

Question 1 : Which of the following is the part of financial statements?

(a) Balance Sheet

(b) Profit & Loss A/c

(c) Both (a) and (b)

(d) None of these

Question 2 : Out of all which of the following is not required to be prepared under the Companies Act:

(a) Statement of Profit 86 Loss

(b) Balance Sheet

(c) Auditor's Report

(d) Fund Flow Statement

Question 3 : Equity Rs. 80,000 Liabilities Rs. 50,000 **Profit** of the year Rs. 20,000. Then total assets will be :

(a) Rs. 1,70,000

(b) Rs.1,50,000

(c) Rs. 1,10,000

(d) Rs. 80,000

Question 4 : The reserve which is created for a particular purpose and which is a charge against revenue is called:

(a) Capital Reserve

(b) General Reserve

(c) Secret Reserve

(d) Specific Reserve

Question 5 : The profit and loss of a company is:

(a) Transferred to share capital account

(b) Shown under the head of 'Current liabilities' and provisions

(c) Shown under the head 'Reserves and Surplus

(d) None of these

Question 6 : The term financial statements means :

(a) Statement of Profit & Loss and Balance Sheet

(b) Balance Sheet

(c) Statement of Profit & Loss.

(d) None of these

Question **7 :** Statement of Profit & Loss is also called

(a) Operating Profit

(b) Balance Sheet

(c) Income Statement

(d) Trading Account

Question 8 : Patents and copyrights are under the category of:

(a) Current Assets

(b) Liquid Assets

(c) Intangible Assets

(d) None of these

Question 9 : Contingent Liabilities are shown **under** the heading:

(a) Fixed Liabilities

(b) Current Liabilities

(c) As a footnote

(d) None of these

Question 10 : Preliminary Expenses are **shown in the** Balance Sheet under which head ?

(a) Fixed Assets

(b) Reserves and Surplus

(c) Loans & Advances

(d) None of these

Question 11 : Which are the followings are current assets :

(a) Stock

(b) Debtors

(c) Cash

(d) All of these

Question 12 : Under which heading of Balance Sheet general reserve is shown:

(a) Miscellaneous Expenditure

(b) Share Capital

(c) Reserves 8 Surplus

(d) None of these

Question 13 : According to provisions of Companies Act, 2013 the final accounts of a company is prepared by following which section :

(a) 128 (b) 210

(c) 129 (d) 212

Question 14 : As per which part of Schedule III of the Indian Companies Act, 2013, Indian companies have to prepare Balance Sheet:

(a) Part 1 (b) Part 2

(c) Part 3 (d) Part 4

Question 15.

Balance sheet of a company is now prepared in which form

(a) Horizontal Form (b) Vertical Form

(c) Either (a) or (b) Form (d) None of these

Question 16 : Securities Premium Account is shown on the liabilities side in **the** Balance Sheet Under the heading

(a) Reserves and Surplus

(b) Current Liabilities and Provisions

(c) Share Capital

(d) Contingent Liabilities

Question 17 : In the Balance Sheet under which head of Debentures are shown:

(a) Short-term Loan

(b) Secured Loan

(c) Current Liability

(d) Share Capital

Question 18 : Which of the following is not a part of financial statement of a Business concern ?

(a) Profit & Loss A/c

(b) Balance Sheet

(c) Ledger Account

(d) Cash Flow Statement

Question 19 : The prescribe from of Balance Sheet has given in the Schedule:

(a) VI Part I

(b) VI Part II

(c) III Part I

(d) VII Part IV

Question 20 : In the Balance Sheet under which head Share capital is shown ?

(a) Authorised Capital

(b) Issued Capital

(c) Paid-up Capital

(d) Shareholders' Funds

LONG ANSWER QUESTIONS :-

1. Explain the Features of financial statements.
2. Narrate the Objectives of Financial Statements.
3. Discuss the Significance of financial statements.
4. Briefly explain the Limitations of financial statements.

5. Show the proforma of the Balance Sheet of a Company in Vertical form along with headings and subheadings.
6. Distinguish between Current Liabilities and Non-current Liabilities.
7. Find the difference between Fixed assets and Current Assets.

PROBLEMS:-

1. Show the following items in the balance sheet as per the provisions of Schedule VI :

Particulars	Rs.
Goodwill	12,000
Discount on issue of shares	4,000
Loose tools	21,000
15% Debentures	87,000
Preliminary Expenses	3,500
Motor Vehicles	2,00,000
Provision for tax	42,000
Cash at bank	73,000
Bills receivable	11,000
Inventories	54,000
Prepaid Expenses	4,000

2. From the following information of ABC Ltd. prepare a balance sheet.

Particulars	Rs.
Stock in trade	10,00,000
Equity Share Capital	22,00,000
Plant and Machinery	10,00,000
8% Preference Share Capital	10,00,000
Debenture Redemption Reserve	5,50,000
Outstanding Expenses	3,50,000
Proposed Dividend	5,00,000
Land and Building	23,00,000
Investments	5,00,000
Cash Equivalent	10,00,000
Public Deposits	12,00,000

3. Prepare the balance sheet of **Orient** Ltd., as at March 31, 2019 from the following information.

Equity Share Capital Rs. 14,00,000;
Plant and Machinery Rs. 8,00,000;
Preference Share Capital Rs.8,00,000:
10% Debentures Rs.12,00,000.
General Reserves Rs. 6,00,000;
Bills payable Rs. 1,00,000;
Stock in trade Rs.7,00,000;
Provision for taxation Rs. 2,50,000;
Land and Building Rs.16,00,000;
Non-current Investments Rs. 9,00,000;
Cash at Bank Rs. 2,00,000;
Cash in hand Rs.3,00,000
Sundry Creditors Rs. 1,50,000;

4. From the following information prepare the balance sheet of XYZ Ltd.

Particulars	**Rs.**
Land and Building	12,50,000
Investments	50,000
Stores & Spares	1,00,000
Discount on issue of shares	10,000
Profit and Loss a/c (Dr.)	40,000
Equity Shares	9,00,000
Capital Redemption Reserve	1,00,000
10% Debentures.	4,00,000
Unpaid dividends	50,000

5. Prepare a balance sheet of **Delta Ltd.,** as at March 31, **2020 from the** following information:

Particulars	**Rs.**
General Reserve :	3,500
10% Debentures	2,300
Profit and Loss a/c:	1,200
Depreciation on fixed assets :	500
Fixed Assets :	8,800
Current Liabilities :	2,000
Preliminary Expenses :	300
10% Preference Share Capital :	5,000
Cash & Cash Equivalents :	6,000
Discount on issue of shares	400
Bills payable	1,000

Answer Key

MULTIPLE CHOICE QUESTIONS :-

1. Answer: C	2. Answer: C,	3. Answer: (b)
4. Answer: (d)	5. Answer : (c)	6. Answer : (a)
7. Answer : (c)	8. Answer (c)	9.Answer : (c)
10. Answer (d)	11. Answer (d)	12. Answer (c)
13. Answer (c)	14. Answer : (a)	15. Answer (b)
16. Answer : (a)	17. Answer : (b)	18. Answer (c)
19. Answer : (a)	20. Answer : (d)	

Problems:-

1. -------
2. Rs.58,00,000.
3. Rs.45,00,000.
4. Rs.14,50,000.
5. Rs.15,000

CHAPTER-4

Company Accounts and Analysis of Financial Statements

ANALYSIS OF FINANCIAL STATEMENTS

Financial Statement analysis is a systematic process of studying the relationship among the multiple Financial factors contained in the financial statement of a business concern to have a better understanding of the working as well as financial position of a business.

"According to finney and miller-" Financial analysis consists in separating facts according to some definite plan, arranging them in groups according to certain circumstances and them presenting them in a convinient and easily read and understandable form,"

Objectives or purposes of Financial statement Analysis:-

To measure the profitability or earning capacity of the business- analysis helps in measuring the profits and earning capacity of a business. It also ensured whether the profit exhibiting in the statement is accurate or not.

To measure the Financial strength or stability of the business – analysis help to understand the financial position of a company.

To make comparative study there are two possible way. Intra firm Comparison and inter firm comparison. Intra firm comparison analysis refers comparison within the business is with previous year or current year or from one department to another. It is also known as trend analysis. Apart from that, Inter firm comparison refers Comparison of one business to another i,e. Comparing with its peer identical group. It is also known as cross section Analysis.

To judge the efficiency of the management profits and assets of the business is the key indicators. These two key points indicates whether the business is able to utilising its resources in a efficient way or not.

To provide useful information to the manggemant-Analysis helps the management to get the useful information of the core issues (obviously financial) and help the management in taking managerial decisions.

To find out the capability for payment of Interest, dividend etc— Profitability of the business helps in judging whether the business will able to pay interest, dividend etc in time or not . Analysis helps in judging the capability of the business for payment of interest and dividend.

To measure the short term and long term solvency position of the business-Analysis helps in judging whether the business is able to pay its short and long term dues.

Comparative Statements:

Such statement showing the profitability and financial position of a business entity for different periods of time in a comparative from to get an idea about the position of the firm in two or more periods.

Firms and companies apply these with regard only two financial statements. I,e. Balance sheet and Income statements. Hence they prepare these two financial statements in the comparative form. It is mentionable that the firms need to use the same accounting principles to get a better result. This method is known as horizontal Analysis.

Steps to prepare comparative statement:

1. Firstly, Put the Absolute figures from the financial statement in the relavent years.
2. Then, find the absolute change by deducting 1^{st} year from the values of 2^{nd} year.
3. In order to find out the% change, use the given for mula

$$\frac{\text{Absolute change (Increase/decrease)}}{\text{Value of first year}} \times 100$$

Proforma:

Particulars	First year	Second year	Absolute change (Increase/Decrease)	Percentage change (increase/ Decrease)
1	2	3	4	5

Common Size Statement:

These are the statements which indicates the relationships of different items of a financial statement with some common item by showing each item as a percentage of the common item.

It enables the firms to do the inter firm as well as an Intra-firm Comparison which is almost impossible in case of comparative statements. These statements also known as vertical Analysis. It main objectives is to study the key changes and Trends in the financial position.

Steps to prepare common size statements:

1. Firstly, put the absolute figures in the relevant years columns (column No. 02 & 04)
2. Then, select a common base as 100.In case of Income statements take sales Revenue as 100. But in case of balance sheet take total assets and liabilities as 100.(Separately)
3. Find out the % value with the help of following formula

$$\frac{\text{Absolute value}}{\text{Common base value}} \times 100$$

Proforma:

Particulars	Year one	Year Two	Percentage of year 1	Percentage of year 2
1	2	3	4	5

Apart from that there are various Tools/Technique of Financial statements these are :-

1. Trend Ratio.
2. Average Analysis.
3. Statement of change in working capital.
4. Fund flow statement.
5. Cash flow statement.
6. Ratio Analysis.
7. Cost volume Ratio Analysis.

Limitations of Financial Analysis:-

Financial statement Analysis ake Financial analysis is a process through which we review and analyse the companies financial reports /statements. Although its advantages / merits are much more in Comparison of its disadvantages /demerits. In spite of that there are some disadvantages.

1. While preparing the financial analysis, firm often fail to consider the price changes.(Inflationary impact Ignored)
2. Generally Intangible records are not recorded/avoided by the business concern. It becomes ineffective and does not reflect the true and fair view of the business.
3. Firms consider only monetary aspects of financial statements. They do not consider non- monetary aspects.
4. Firms prepare the financial statements on the basis of on – going concern concept, as such it does not reflect the current position.
5. The statement do not necessarily provide any value in predicting what will happen in the future.

KEY POINTS TO REMEMBER:-

- Gross profit =Revenue from operations –cast of materials consumed.
- Change in Inventories means opening stock less closing stock.
- Employee benefit expenses means expenses incurred on employees. i.e salaries, wages, contribution to PF etc.

- Cast of Goods sold= Opening stock +Purchase-closing stock.
  (COGS)=Sales-Gross profit
- Operating Revenue means Revenue from operations.
- Operating profit = Gross Profit –Operating Expenses.
- Net profit= Gross profit—Cost of Goods sold (COGS)
- Three objectives of analysis and Interpretation of financial statements are: 3P's(progress, postion and Prospects)

EXERCISE

(A) State whether the following statements are True or False: **Marks : 1**

i) Break even point is no profit no loss point.

Answer:——————————————————————————

ii) Comparative statements are helpful in indicating the trend of changes.

Answer:——————————————————————————

iii) Financial statements includes only Balance sheet.

Answer:——————————————————————————

iv) Increase/Decrease of Gross profit depends on Net Sales.

Answer :——————————————————————————

v) Interest on loan is direct expenses.

Answer:——————————————————————————

vi) Analysis of financial statement is a tool but not a remedy.

Answer:——————————————————————————

vii) Net profit is obtained after deducting operating and Non-operating expenses from Gross profit.

Answer:——————————————————————————

viii) One of the objective of common size statement is to present the changes to various items.

Answer:——————————————————————————

ix) In a common size statement of profit and loss figure of net sales is assumed to be equal to100.

Answer:——————————————————————————

x) In a common size statement, figures of previous year are taken as base for comparison.

Answer:——————————————————————————

B) Fill in the blanks:- **Mark : 1**

i) Horizontal Analysis is also called ——————

Answer:————————————————

ii) A comparative Balance sheet shows the increase or decrease of various assets, liabilities and———

Answer: ——————————————————————————————

iii) Vertical Analysis is also called ————

Answer: ——————————————————————————————

iv) Common size statements are prepared in the form of————

Answer: ——————————————————————————————

v) In a ——————total assets or equity liabilitiy is assumed to be equal to 100.

Answer:——————————————————————————————

(C) Answer the MCQ's/ USA Type Questions: (1 mark)

i) List any two uses of analysing of financial statements?

Answer:——————————————————————————————

ii) What is Horizontal Analysis?

Answer:——————————————————————————————

iii) How can the financial strength of a business enterprise can be judged?

Answer:——————————————————————————————

iv) List any one of the objectives of analysing the financial statements?

Answer: ——————————————————————————————

v) When assets are substructed from liabilities it will be equal to—

a) Working Capital b) Goodwill c) Capital d) Income.

Answer:——————————————————————————————

vi) Profit and loss statement is also known as—

a) Statement of operations b) Statement of earnings.

c) Statement of Balance d) Statement of Income.

Answer:——————————————————————————————

v) Common size statements are prepared

a) In the form of Ratio's b) In the form of Percentage. c)In both of the above d) None of the above.

viii) The most commonly used tools for financial Analysis are:

a) Comparative Statements. b) Common size statement.

b) Accounting ratios. d) All of the above.

Answer:——————————————————————————————

ix) Current assets is also known as:-

a) Working Capital. b) cash c) Net worth d) Assets.

x) This item is not used as a tool for analysis of financial statements:-

a) Cash flow statement b) Statement of employees.

c) Common size statements d) Ratio Analysis.

xi) What is a Comparative balance sheet?

Answer:——————————————————————————

xii) Give two objectives of comparative financial statement?

Answer:——————————————————————————

xiii) What is common size statement?

Answer:——————————————————————————

xiv) What is the meaning of common size Balance sheet?

Answer:——————————————————————————

xv) Comparison of financial statements highlights the trend of the ———— of the business.

a) Probitability b) Performance c) Financial position d) All of the above.

Answer:——————————————————————————

xvi) Analysis of Financial statements comprises—

a) Balance sheet b) P & L A/c. c) Trading A/c. d) All of the above.

Answer:——————————————————————————

xvii) Comparative statements are also known as.

a) Horizontal Analysis. b) External Analysis. c) vertical Analysis. d) Internal Analysis.

Answer:——————————————————————————

xviii) Comparative Financial statements show-

a) Financial Position of a company b) Earning capacity of a concern

b) Both of them (d) None of the above.

xix) Common size financial statement are mostly prepared:

a) In proportion b) In Percentage

c) (a) and (b) both d) None of these.

Answer:——————————————————————————

xx) Balance sheet shows:-

a) Profit or loss of any business. b) Fund flow of a company.

c) Financial position of a company d) None of the above.

(D) PRACTICAL QUESTIONS (CARRYING 4MARK) **Marks : 4**

(1) Prepare a Comparative Statement of profit and loss from the following books of Apple India LTD.

Particulars	31.03.2019(Rs)	31.03.2018(Rs)
Revenue from operations	17,80,000	15,20,000
Other Income	80,000	10,000
Expenses	10,40,000	8,70,000
Income Tax	2,50,000	2,00,000

Answer:—

(2) From the following particulars are obtained from the books of ABC company Limited, Prepare a comparative statement of profit and loss:

Particulars	31.03.2020	31.03.2019
Revenue from operations	Rs 40,00,000	Rs 30,00,000
Materials Consumed	Rs 24,00,000	Rs 22,50,000
Other Expenses	10% of Materials consumed	8% of Materials consumed
Income Tax	50%	50%

Answer:—

(3) From the following information, prepare a comparative statement of profit and loss for the year ended 31st March, 2018 and 2019.

Particulars	31.03.2019	31.03.2018
Revenue from operations	Rs 9,00,000	Rs 6,00,000
Cost of Materials consumed	Rs 8,00,000	Rs5,00,000
Employee Benefit Expenses	Rs 75,000	Rs50,000
Others Expenses	Rs 20,000	Rs 10,000
Tax	50%	50%

Interest on Investments @ Rs 1,00,000 each year.

Answer:—

(4) Prepare a comparative Income statement from the following information in the books of Raman Limited.

Particulars	31.12.2019 (Rs)	31.12.2020 (Rs)
Net Sales	1,90,000	2,20,000
Cost of Goods Sold	1,40,000	1,50,000
Selling and administrative expenses	25,000	30,000
Other Incomes	12,000	30,000

Taxes	8,000	16,000
Interest paid	17,000	18,000

Answer:—

(5) Prepare a Comparative statement of profit & loss of snowmen logistics with the information given below:—

Particulars	31.12.2019(Rs)	31.12.2018(Rs)
Revenue from operations	50,00,000	80,00,000
Purchase of stock-in-Trade	30,00,000	60,00,000
Change in Inventories	(6,00,000)	(4,00,000)
Employee benefit Expenses	8,00,000	6,50,000
Other Expenses	80,000	1,00,000

Answer:—

(6) From the following information prepare a comparative income statement of Varuu beverages Limited:-

Particulars	31.03.2020(Rs)	31.03.2019(Rs)
Revenue from operations	40,00,000	30,00,000
Other Incomes	20%	30%
(% of Revenue from operations)		
Expenses	70%	60%
(% of Revenue from operation)		
Tax Rate	40%	50%

Answer:—

(7) From the following information prepare a comparative Balance sheet of ABC Limited.

Particulars	31.03.2020(Rs)	31.03.2019(Rs)
Equity share capital	25,00,000	20,00,000
Reserve and Surplus	6,00,000	15,00,000
Long Term Borrowings	15,00,000	14,00,000
Current Liabilities	6,00,000	5,50,000
Fixed Assets	30,00,000	30,00,000
Investments (Non-Currents)	15,50,000	10,00,000
Current Assets	6,50,000	14,50,000

(8) From the following Balance sheet, prepare a comparative Balance sheet of Ratul Limited:-

Particulars	Note No.	31.03.2020(Rs)	31.03.2019(Rs)
I. EQUITY AND LIABILITIES:			
1. Shareholders funds :			
a. Share capital		4,00,000	3,00,000
2. Non- current liabilities			
Long Term Borrowings		2,00,000	1,00,000
3.Current liabilities,			
Trade payables		1,00,000	2,00,000
Total		7,00,000	6,00,000
II. ASSETS :			
1. Non-Current assets			
Fixed Assets(Tangible)		5,00,000	4,00,000
2. Current Assets			
Trade Receivables		2,00,000	2,00,000
Total		7,00,000	6,00,000

Answer:————————————————————————————————

(9) Prepare a common size Balance sheet of Aptech Ltd. From the following information:-

Balance sheet

As at 31st March

Particulars	Note No.	31.03.2020	31.03.2019
I. EQUITY AND LIABILITIES.			
1. Shareholders funds :			
a) Share Capital		4,50,000	3,60,000
b) Reserve and Surplus		4,50,000	3,72,000
2. Non- Current Liabilities			
Long Term Borrowings		3,00,000	2,04,000
3. Current Liabilities:			
a) Trade payables		1,80,000	1,68,000
b) Short Term Provisions		1,20,000	96,000
		15,00,000	**12,00,000**

II . ASSETS			
1. Non-Current Assets:			
a) Fixed Assets		4,95,000	3,60,000
b) Non-Current Investments		3,75,000	3,36,000
2. Current Assets			
a) Inventory		1,80,000	1,56,000
b) Trade Receivables		3,00,000	2,16,000
c) Cash and cash equivalents		1,50,000	1,32,000
		15,00,000	**12,00,000**

10) From the following Balance sheet of Relaxo Ltd. Prepare a common size Statement.

Balance Sheet
As at 31st March

Particulars	Note No.	31.03.2019	31.03.2018
I. EQUITY AND LIABILITIES.			
1.Shareholders funds:			
a) Share Capital		2,00,000	1,02,000
b) Reserve and Surplus		1,00,000	1,50,000
Current Liabilities:			
a) Trade payables		1,00,000	48,000
Total		4,00,000	3,00,000
II . ASSETS			
2. Non-Current Assets:			
a)Fixed Assets:			
i) Tangible Assets		1,60,000	1,20,000
ii) Intangible Assets		20,000	30,000
2.Current Assets			
a) Investment		80,000	30,000
b) Trade Receivables		1,20,000	1,00,000
c) Cash and cash equivalents		20,000	20,000
		4,00,000	3,00,000

11) Prepare a Common size Income statement form the following information:

Particulars	31.03.2019(Rs)	31.03.2018(Rs)
Revenue from operations	48,00,000	28,50,000
Employee Benefit Expenses	4,00,000	1,50,000
Purchase of stock-in-Trade	32,64,000	18,76,800
Other Income	2,00,000	1,50,000
Others Expenses	3,36,000	2,23,200
Income Tax (40%)		

12) From The following information prepare a common size profit and loss of Emkay Ltd.

Particulars	31.12.2020(Rs)	31.12.2019(Rs)
Revenue from operations	18,00,000	15,00,000
Cost of materials Consumed	10,02,420	9,94,800
Employee benefit Expenses	2,39,580	1,90,200
Other Expenses	1,98,000	45,000
Income Tax(50%)		

Q: 13. Explain the importance of Financial Statement Analysis?

Answer:———————————————————————————

Q: 14. Describe the different techniques of financial analysis?

Answer:———————————————————————————

Q: 15. Explain the Limitations of financial Analysis?

Answer:———————————————————————————

Q:16. What are the importance of comparative statements ? Illustrate your answer with a reference to comparative statement.

Answer:———————————————————————————

Q:17. Differentiate between comparative and common size statements.

Answer:———————————————————————————

Answer Key

A) True or False:

i) True ii) True iii) False iv) True v) False vi) True vii) True viii) True ix) True x) False

B) Fill in the blanks:

i) Dynamic ii) Capital iii) Static iv)Percentages v) Common size Balance Sheet.

C) MCQ/VSA TYPE

i) Help full in taking Investment and credit decisions.
ii) See Text book.
iii) Its earning capacity i,e profitability and its ability to repay loan and pay dividends.
iv) To measure the earning capacity of the business
v) (c) Capital, vi)(d) Statement of Income vii)(b) In the form of percentage
viii) (d) All of the above ix) (a) Working Capital x) (b) Statement of employees
xi) See text book xii) See text book xiii) See Text book xiv) See Text book
xv) (d) all of the above xvi) (d) All of The above
xvii) (a) Horizontal Analysis xviii) (c) both of them xix) (b) In percentage
xx) (c) Financial position of a company.

(a) PRACTICAL QUESTIONS (4 Mark)

1. Profit After Tax (PAT)=2018: Rs 4,60,000; 2019: Rs 5,70,000
2. Profit After Tax (PAT)=2019: Rs 2,85,000; 2020: Rs 6,80,000
3. Profit After Tax (PAT)=2018: Rs 84,000; 2019: Rs 52,500;
4. Profit After Tax (PAT)=2019: Rs 12,000; 2020: Rs 24,000;
5. Profit Before Tax (PBT)=2018: Rs 16,50,000;2019 Rs 17,20,000
6. Profit After Tax (PAT)=2019: Rs 7,80,000; 2020: Rs 8,64,000
7. Equity share capital =25%; Reserve and surplus=(60%)
   Long Term Borrowings =7.14% Current Liabilites=9.09%
   Fixed Assets =Nil; Investments =55%; Current Assets=(55.17%)
8. Shareholders fund = 33.33%; Non –Current Labilities=100%;
   Current Liabilities=(50%); Non- Current Assets= 25%; Current Assets=Nill.
9.

(In percentage)

	31.03.19	**31.03.20**
Share capital	30.00	30.00
Reserve & Surplus	31.00	30.00
Long-Term Borrowing	17.00	20.00
Trade payables	14.00	12.00
Short Term Provisions	8.00	8.00
	100.00	**100.00**
Fixed Assets	30.00	30.00

Non –Current Assets	28.00	25.00
Inventory	13.00	12.00
Trade Receivables	18.00	20.00
Cash and Cash equivalent	11.00	10.00
	100.00	**100.00**

10.

	(In percentage)	
	31.03.18	**31.03.19**
Share Capital	34.00	50.00
Reserve and surplus	50.00	25.00
Trade Payable	16.00	25.00
	100.00	**100.00**
Tangible Assets	40.00	40.00
Intangible Assets	10.00	5.00
Investments	10.00	20.00
Trade Receivables	33.33	30.00
Cash and cash equivalents	6.67	5.00
	100.00	**100.00**

11.

	(In percentage)	
	31.03.2018	**31.03.2019**
Revenue from operations	95.00	96.00
Other Income	5.00	4.00
Total Income	**100.00**	**100.00**
Purchase of stock in Trade	62.56	65.28
Employee benefit Expenses	5.00	8.00
Other expenses	7.44	6.72
Total Expenses	75.00	80.00
Profit before Tax (PBT)	25.00	20.00
Tax	(10.00)	(8.00)
Profit After Tax	**15.00**	**12.00**

12.

	(In percentage)	
	31.12.2019	**31.12.2020**
Revenue from operations	100.00	100.00
Cost of Materials consumed	66.32	55.69
Employee benefit Expenses	12.68	13.31
Other Expenses	3.00	11.00
Total Expenses	82.00	80.00
Profit before Tax (PBT)	18.00	20.00
Tax	(9.00)	(10.00)
Profit After Tax (PAT)	9.00	10.00

CHAPTER -5

Accounting Ratios

Meaning of accounting ratios

Ratio is a mathematical expression of relationship between two related or interdependent items.

Definition of ratio analysis

Ratio analysis is a tool which involves analysing the financial statements by calculating different ratios.

According to Myers, "Ratio analysis is a study of relationship among various financial factors in a business".

Objectives of ratio analysis

Following are the objectives of ratio analysis:

(i) To simplify understanding of accounting figures.

(ii) To helps in analysis of financial statements.

(iii) To determine the operational efficiency of a business..

(iv) To help in planning and forecasting.

(v) To analyse intra firm and inter firm comparison of performance.

Advantages of ratio analysis

There are many advantages of ratio analysis. These are as follows:

1. Ratio analysis Helps to understand the effectiveness of business decisions.
2. They Simplify complex figures and establish relationships.
3. They are very much Helpful in comparative analysis of business.
4. Ratios help business in identifying the problem areas which needs more attention.
5. Ratios help in intra firm and inter firm comparison.

Limitations of Ratio Analysis

The limitations of the ratio analysis are:

1. Accounting data give an unnecessary impression of precision and finality.
2. They Ignores Price-level Changes.
3. Ratio Analysis ignore Qualitative or Non-Monetary facts.
4. Because of variations in accounting practices, a valid comparison of financial statements is not possible.

5. Forecasting of future trends based only on past analysis is not feasible.

9.5. Classification of ratios

The ratios are classified as follows:

(i) Liquidity ratios. It is expressed as a quotient.

Formula : **Current Ratio = Current Assets /Current Liabilities**

Or

Current Assets =sundry debtors, Short-term loans and advances, Short-term Investments, Stock in trade (closing)/Inventory,Bills receivable, **cash in** hand, cash at bank,prepaid expenses etc.

Current Liabilities = Bills payable and sundry creditors, short-term borrowings, Short-term provisions, outstanding expenses, unclaimed dividend, calls-in advance, etc.

Standard Ratio: 2:1.

Liquid or Quick Ratio or Acid test ratio = Liquid assets /Current Liabilities

Liquid or Quick assets = Current assets - Inventories - Prepaid expenses

Standard Ratio: 1:1.

(ii) Solvency ratios. it is expressed as a quotient.

Formula: **Debt Equity Ratio = Debt/Equity (Shareholder's Funds)**

Debt = Long-term Borrowings + Long-term Provisions

Equity = Share Capital + Reserves & Surplus **Or=** Total Assets - Total Debt

Formula:

Total Asset to Debt ratio = Total Assets/Long term Debts.

Formula:

Interest Coverage Ratio = Profit before Interest and Taxes/Interest on Long term Debts.

Formula:

Proprietary Ratio = Proprietor's Funds or Shareholders' Funds or Equity /Total Assets

Proprietors' funds = Share Capital (Equity + Preference) + Reserves and Surplus. OR

Proprietors' funds = Non-current Assets + Working Capital - Non-current Liabilities. Working Capital = Current Assets - Current Liabilities

(iii) Turnover ratios. It is expressed in Times.

Formula:

Inventory or Stock Turnover Ratio = Cost of Revenue from Operations (Cost of Goods Sold)/Average Inventory (Stock) Cost of Revenue from Operations/Cost of Goods Sold = Revenue from Operations - Gross Profit, Or

Cost of Revenue from Operations /Cost of Goods Sold= Opening Stock + Net Purchases + Direct Expenses - Closing stock.

$$\text{Average Inventory or Stock} = \frac{\text{(Opening Inventory+Closing Inventory)}}{2}$$

Formula:

Debtors or Trade Receivable Turnover Ratio= Net Credit Revenue from Operations (Net Credit Sales)/Average Trade Receivables

Net Credit Sales/Credit Revenue from Operations = Credit Sales - Sales Return Average Trade receivables. = (Opening Debtors + Closing Debtors + Opening Bills receivables + Closing Bills receivables) $\div 2$

Formula:

Creditors or Trade Payables Turnover Ratio = Net Credit Purchases /Average Trade Payables

Net credit purchase = Credit purchase - Purchase return

Average Trade Payables = (Opening Creditors +Closing Creditors + Opening Bills Payable + Closing Bills Payable) $\div 2$

Formula:

Working Capital Turnover Ratio = Revenue from Operations Or Cost of Revenue from Operations / Working Capital

Working capital = Current assets - Current liabilities

(iv) Profitability ratios.

It is expressed in percentage.

Formula:

$$\textbf{Gross Profit Ratio} \quad \frac{\text{Gross Profit}}{\text{Revenue from Operations (i.e. Net Sales)}} \times 100$$

Gross Profit = Revenue from Operations - Cost of Revenue from Operations (COGS)

Formula:

$$\textbf{Net Profit Ratio} \quad \frac{\text{Net Profit}}{\text{Revenue from Operations (i.e. Net Sales)}} \times 100$$

Formula:

$$\textbf{Operating Ratio} = \frac{\text{Cost of Revenue from operation + Operating expenses}}{\text{Net revenue from operations}} \times 100$$

Operating **Expenses =** Office, Administrative , Selling and Distribution expenses, Depreciation, amortisation etc.

Formula :

$$\textbf{Return on Investment} = \frac{\text{Net before Interest and Tax and divident}}{\text{Capital Employed}} \times 100$$

Formula :

$$\textbf{Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Net Revenue from Operations}} \times 100$$

Operating Profit = Gross profit + Operating income - Operating expenses

Multiple Choice Questions :

Choose the correct Answer :

1. Formula of Current Ratio **is**–
   (A) Liquid Assets/Current Assets
   (B) Fixed Assets/Current Assets
   (C) Current Assets/Current Liabilities
   (D) Liquid Assets/Current Liabilities
2. Two basic measures of liquidity of a business firm are–
   (A) Inventory turnover and Current ratio
   (B) Current ratio and Quick ratio
   (C) Gross Profit ratio and Operating ratio
   (D) Current ratio and Average Collection period
3. Which of the following is not liquid assets–
   (A) Bills Receivable
   (B) Debtors
   (C) Inventory
   (D) Bank Balance
4. Standard Current Ratio is–
   (A) 1 : 1
   (B) 1 : 2
   (C) 1 : 3
   (D) 2 : 1

5. Formula of Working Capital is –
   (A) Cash and Bank Balance
   (B) Capital borrowed from the Banks
   (C) Difference between Current Assets and Current Liabilities
   (D) Difference between Current Assets and Fixed Assets
6. Ideal Quick Ratio is–
   (A) 1 : 1
   (B) 1 : 2
   (C) 1 : 3
   (D) 2 : 1
7. Liquid Assets does not include –
   (A) Cash in hand
   (B) Prepaid Expenses
   (C) Marketable Securities
   (D) Trade Receivables
8. Current Assets does not include–
   (A) Prepaid Expenses
   (B) Inventory
   (C) Goodwill
   (D) Bills Receivable
9. Quick Ratio is also known as–
   (A) Acid test Ratio
   (B) Current Ratio
   (C) Working Capital Ratio
   (D) None of the Above
10. The formula for calculating Operating ratio is–
   (A) Cost of revenue from operations + Selling Expenses/Net revenue from operations
   (B) Cost of production + Operating Expenses/ Net revenue from operations
   (C) Cost of revenue from operations + Operating Expenses/Net Revenue from Operations
   (D) Cost of Production/Net revenue from operations

11. Cash Balance Rs.5,000; Trade Payables Rs.30,000; Inventory Rs.50,000; Trade Receivables Rs.65,000 and Prepaid Expenses are Rs.20,000. Liquid Ratio will be–

(A) 1.75: 1

(B) 2 : 1

(C) 3.25: 1

(D) 3: 1

12. Current Assets Rs.4,50,000; Current Liabilities Rs.2,00,000 and Inventory is Rs.50,000. Liquid Ratio will be –

(A) 2 : 1

(B) 2.25: 1

(C) 4 : 7

(D) 1.75: 1

13. Which of the following transactions will improve the Current Ratio –

(A) Cash Collected from Trade Receivables

(B) Purchase of goods for cash

(C) Payment to Creditors

(D) Credit purchase of Goods

14 The formula for calculating Liquid asset is–

(A) Current Assets – Prepaid exp.

(B) Current Assets – Inventory + Prepaid Exp.

(C) Current Assets – Inventory – Prepaid Exp.

(D) Current Assets + Inventory – Prepaid Exp.

15. Formula of Debt Equity Ratio is :

(A) Long Term Debts/Shareholder's Funds

(B) Short Term Debts/Equity Capital

(C) Total Assets/Long term Debts

(D) Shareholder's Funds/Total Assets

16. The formula for calculating Proprietary Ratio is–

(A) Long term Debts/Shareholder's Funds

(B) Total Assets/ Shareholder's Funds

(C) Shareholder's Funds/Total Assets

(D) Shareholder's Funds/Fixed Assets

17. Formula of Inventory Turnover Ratio is–
   (A) Average Inventory/Revenue from Operations
   (B) Average Inventory/Cost of Revenue from Operations
   (C) Cost of Revenue from Operations/Average Inventory
   (D) G.P./Average Inventory

18. The formula for calculating the Debtors Turnover Ratio is
   (A) $\frac{\text{Total Revenue from operations}}{\text{Average Debtors}}$
   (B) $\frac{\text{Credit Revenue from operations}}{\text{Average Debtors}}$
   (C) $\frac{\text{Net Credit Revenue from operations}}{\text{Average Debtors + Average Bills Receivable}}$
   (D) None of the Above

19. The formula for calculating Creditors Turnover Ratio is :
   (A) $\frac{\text{Net Credit Purchases}}{\text{Average Creditors}}$
   (B) $\frac{\text{Net Credit Purchases}}{\text{Average Creditors + Average bills payable}}$
   (C) $\frac{\text{Cash Purchases}}{\text{Total Creditors}}$
   (D) None of the Above

20. What will be the amount of Gross Profit, if revenue from operations are 6,00,000 and Gross Profit Ratio 20% of revenue from operations?
   (A) Rs.1,50,000
   (B) Rs.1,00,000
   (C) Rs.1,20,000
   (D) Rs.5,00,000

Very Short answer questions :

1. What is meant by Accounting Ratios?
2. Define Debt Equity Ratio
3. What do you mean by Total Asset to Debt ratio? 4.Write the formula of Acid test ratio.
5. Define Interest Coverage Ratio.
6. What do you mean by Proprietary Ratio?
7. What is Stock Turnover Ratio?
8. Write the formula of trade Receivable Turnover Ratio.
9. What do you mean by Trade Payables Turnover Ratio?
10. Write the formula of Working Capital Turnover Ratio.
11. Define Gross Profit Ratio.
12. What do you mean by Net Profit Ratio?
13. Write the formula of Operating Ratio.
14. State the Standard ratio of Current Ratio.
15. What do you mean by Operating Ratio?
16. What is capital Employed?
17. What is Current Ratio?
18. How do you calculate Working Capital?
19. State the Standard ratio of Quick Ratio.
20. Define Return on Investment.

Short answer questions :

1. Explain the Objectives of ratio analysis.
2. Discuss the Advantages of ratio analysis.
3. What are the Limitations of Ratio Analysis. Explain.
4. Describe different types of Liquidity ratios.
5. Explain different types of Solvency ratios.
6. Describe different types of Turnover ratios.
7. Discuss different types of Profitability ratios.

Problems:

1. Following is the Balance Sheet of Saha Ltd. as at March 31, 2019.

Particulars		Amount (Rs.)
I.	Equity and Liabilities	
	1. Shareholders' funds	
	a) Share capital	24,50,000
	b) Reserves and surplus	6,00,000
	2. Non-current liabilities	
	Long-term borrowings	9,00,000
	3. Current liabilities	
	a) Short-term borrowings	6,00,000
	b) Trade payables	23,60,000
	c) Short-term provisions	90,000
	Total	70,00,000
II.	Assets	
	Non-current assets	
	Fixed assets	
	- Tangible assets	45,00,000
	2. Current Assets	
	a) Inventories	12,50,000
	b) Trade receivables	9,20,000
	c) Cash and cash equivalents	2,38,000
	d) Short-term loans and advances	92,000
	Total	70,00,000

Calculate Current Ratio and Liquid Ratio.

2. Calculate the current ratio from the following information.
   Fixed assets 7,50,000; Short term investments 30,000
   Inventories 1,00,000 ;Trade creditors 90,000
   Trade debtors 2,30,000; Bills payable 40,000
   Bills receivable 80,000 ; Outstanding Expenses 20,000
   Cash 10,000.

3. Calculate quick ratio: Total current liabilities' 1,75,000; Total current assets' 4,50,000; Inventories 60,000; Prepaid expenses 40,000.
4. Sudipa Limited has a current ratio 4 : 1 and quick ratio 3 : 1; if the inventory is 35,000, calculate Current Liabilities and Current Assets.
5. Calculate Current Ratio when :

   Liquid Assets Rs. 22,00,000; Inventory is Rs. 11,00,000; and Liquid Ratio 2 : 1.
6. From the following, calculate
   (a) Debt-Equity Ratio
   (b) Total Assets to Debt Ratio
   (c) Proprietary Ratio.

   Equity Share Capital Rs. 72,700

   Preference Share Capital Rs. 27,300

   General Reserve Rs. 41,000

   Profit & Loss a/c Rs. 34,000

   Debentures Rs. 75,000

   Trade Payables Rs. 37,000

   Outstanding Expenses Rs. 13,000
7. From the following information, calculate Debt Equity Ratio, Total Assets to Debt Ratio, and Proprietary Ratio.

Particulars	Note	Rs.
I. Equity and Liabilities:		
1. Shareholders' fund		
a) Share capital		4,00,000
b) Reserves and surplus		50,000
2. Non-current Liabilities		
Long-term borrowings		1,50,000
3. Current Liabilities		50,000
		6,50,000
II. Assets		
1. Non-current Assets		
a) Fixed assets		3,25,000
b) Non-current investments		1,25,000
2. Current Assets		2.00,000
		6,50,000

8. From **the following** information, calculate Inventory turnover ratio :

Rs.

Inventory in the beginning = 19,000 Inventory at the end = 21,000 Net purchases - 46,000

Wages = 14,000

Revenue from operations = 80,000 Carriage inwards = 4,000

9. Calculate the Trade receivables turnover ratio from the following information: Rs.

Total Revenue from operations 5,00,000

Cash Revenue from operations 20% of Total Revenue from operations

Opening Trade receivables 50,000

Closing Trade receivables 1,10,000

10. Calculate the Trade payables turnover ratio from the following figures: Rs.

Credit purchases during 2019-20 = 9,00,000

Creditors on 1.4.2019= 2,50,000

Bills Payables on 1.4.2019= 50,000

Creditors on 31.3.2020 = 30,000

Bills Payables on 31.3.2020= 70,000

11. Calculate the following ratio on the basis of following information:

(i) Gross Profit Ratio (ii) Current Ratio (iii) Acid Test Ratio (iv) Inventory Turnover Ratio (v) Fixed Assets Turnover Ratio vi) Net Profit ratio.

	Rs.
Gross Profit	40,000
Revenue from Operations	1,00,000
Inventory	14,000
Salaries	5,000
Rent	2,000
Trade Receivables	28,500
Cash and Cash Equivalents	17,500
Current Liabilities	40,000
Land & Building	50,000
Plant & Machinery	35,000
Furniture	5,000

12. Compute Inventory Turnover Ratio from the following information:

Net Revenue from Operations	Rs.	1,80,000
Gross Profit Rs.	Rs.	80,000
Inventory at the end Rs.	Rs.	55,000
Excess of inventory at the end over inventory in the beginning	Rs.	10,000

13. From the following information, calculate the following ratios:

i) Liquid Ratio ii) Inventory turnover ratio iii) Return on investment iv) Gross Profit ratio.

	Rs.
Inventory in the beginning	50,000
Inventory at the end	40,000
Revenue from operations	4,00,000
Gross Profit	1,00,000
Cash and Cash Equivalents	40,000
Trade Receivables	1,10,000
Trade Payables	1,90,000
Other Current Liabilities	70,000
Share Capital	2,20,000
Reserves and Surplus	1,40,000

(Balance in the Statement of Profit & Loss A/c)

14. Calculate (i) Inventory turnover ratio (ii) Trade receivables turnover ratio (iii) Trade payables turnover ratio and (iv) Fixed assets turnover ratio from the following information obtained from Birat Ltd.

Particulars	As on 31st March, 2019	As on 31st March, 2020
Inventory	3,70,000	4,30,000
Trade receivables	7,35,000	6,65,000
Trade payables	1,90,000	2,10,000
Fixed assets	6,00,000	8,00,000

Additional information:

(i) Revenue from operations for the year(credit) 28,00,000

(ii) Purchases for the year 21,00,000

(iii) Cost of revenue from operations 20,00,000.

(iv) Cash Purchases for the year 1,00,000

15. Calculate operating profit ratio under the following cases.

Case 1: Revenue from operations 10,00,000, Operating profit 1,80,000.

Case 2: Revenue from operations 14,00,000, Operating cost 10,00,000.

Case 3: Revenue from operations 20,00,000, Gross profit 20% on revenue from operations, Operating expenses 2,00,000.

ANSWER KEY

Multiple Choice Questions

Ans : 1. C; 2. B; 3. C; 4. D; 5. C; 6. A; 7. B; 9. D; 10. D; 11. C;
12. D; 13. A; 14. C; 15. C; 16. A; 17. C; 18. C; 19. : B 20. C.

Problems:

1. Ans : Current Ratio 0.82 1, Liquid Ratio 0.41 : 1
2. Ans : Current ratio: 3:1. 3..Ans: Quick ratio: 2:1;
4. Ans: Current Assets Rs. 1,40,000, Current Liabilities Rs. 35,000; 5. Ans: Current Ratio 3 : 1. 6.Ans: Debt-Equity Ratio 0.43: 1;

   Total Assets to Debt Ratio 4 : 1; ProprietaryRatio 0.58: 1
7. Ans: Debt-Equity Ratio 3 : 1; Total Assets to Debt Ratio 4.33: 1; Proprietary Ratio 0.69: 1
8. Ans: 3.1 times; 9. Ans: 5 times ;10. Ans: 4.5 times ;
11. Ans: Gross Profit Ratio 40%; Current Ratio 1.5:1; Liquid Ratio 1.15: 1, Inventory Turnover Ratio 4.28 times; Fixed Assets Turnover Ratio .9 : 1; Net Profit ratio 33%
12. Ans: Inventory Turnover Ratio 3 times;
13. Ans: Liquid Ratio 0.57: 1; Inventory Turnover Ratio 6.66 times; Return on Investment 38.88%; Gross profit ratio 25%
14. Answer: (i) Inventory turnover ratio: 5 times; (ii) Trade receivables turnover ratio: 4 times;(iii) Trade payables turnover ratio: 10 times; (iv) Fixed assets turnover ratio: 4 times
15. Ans: Case 1- 18%; Case 2 - 28.57%; Case 3 -10%.

CHAPTER-6

Cash Flow Satement

Cash flow statement is a statement showing the changes in financial position of a business concern during different intervals of time in terms of cash and cash equivalents.

In other words, it is a summary of sources and application of cash and cash equivalents during a particular span of time.

As per Revised Accounting standard-3, it now becomes mandatory for all listed companies to prepare a cash flow statement along with other financial statements on annual basis.

Objectives of cash flow statement :-

- To ascertain the liquidity position of the company.
- To ascertain the net cash inflow or outflow of the company.
- To ascertain the net change in cash and cash equivalents i.e the difference between sources and applications of different activities.
- To enable a more realistic and prudent assessment of financial condition of the company.

Importance or uses of cash flow statement:-

The main importance for preparing cash flow statement is-

- It is vary useful for short term financial planning.
- It is very useful for preparing the cash budget.
- Easily compare with the cash budget.
- Study of the trend of cash Receipts and payments.
- It explain the deviations of cash from earnings.
- It is helpful in ascertaining cash flow from various activities separately.
- Helpful in making dividend decisions.
- Test for the managerial decisions.
- Useful for the outsiders/ suppliers of credit.

A cash flow statement shows how the business used its cash and cash equivalents during the year. Basically it aims to show the changes in a business bank balance.

Classification of cash flow:-

According to Accounting standard-3, a cash flow statement should be prepare in such a manner that it reports inflow and outflow of cash by classifying them into three categories. These are operating, investing and financing Activities.

Descriptions of inflow and outflow items of cash flow statement

Operating Activities

Cash inflows

i) Cash Sales
ii) Cash Received from Trade Receivables/Debtors.
iii) Cash Received as commission.
iv) Cash Received as fees/Royalty.
v) Income Tax Refund Received.
vi) Interest and Dividend Received in cash.
vii) Proceeds from sale of securities.
viii) Loans and advances prepaid by third parties.

Cash outflows

i) Cash Purchase
ii) Cash operating Expenses
iii) Payment to Trade payable/creditors.
iv) Payment of operating experes like wages salary etc.
v) Payment of Income Tax.
vi) Interest paid in cash
vii) Payment for purchase of securities.
viii) Loans and advances to third parties.

Investing Activities

Cash Inflows

i) Sale of fixed Assets
ii) Sale of Investments (non current and current other than Marketable securities)
iii) Interest received on Debentures.
iv) Dividend Received on Shares.

Cash outflows

i) Purchase of fixed Assets
ii) Purchase of Investments (Non current and current Other then marketable nurtures)

Financing Activities

Cash Inflows

i) Issue of shares in cash
ii) Issue of Debenturs in cash
iii) Proceeds from long term loan
iv) Proceeds from Bank overdraft/ cash Credit

Cash Outflows

i) Payment for Buy back of equity shares.
ii) Payment ofr redemption of Preferenue shares
iii) Payment for redemption of debentures
iv) Payment of loans (Short Term and Long Term)
v) Payment of Divident.
vi) Payment of Interest
vii) Repayment of Bank overdraft or Cash credit.
viii) Payment of Priliminary expenses (Including Share Issue expenses)

As per Accounting standard -3, There are two methods for preparing cash flow statement.

A. Indirect method.

B. Direct method.

Preparation of cash flow statement under Indirect method:-

i) **Operating Activities:**

Cash flow from operating activities may be obtain under two stages:-

a) Calculating the operating profit before working capital changes.

b) The effect of changes in working capital.

Stage-1

Operating profit before working capital changes can be calculated as under:-

Net profit befor Tax and Extraordinary items		***
Add: Non cash and Non- operating items debited in profit and Loan A/C:		
Depreciation	***	
Amortisation of Intangible asets	***	
Loss on sale of fixed Asets	***	
Loss on the sale of long-Term Investments		
Provision for Tax	***	
Dividend Paid	***	***
		***
Less – Non – cash and non- operating items credited in profit and Loss A/C:		
Profit on sale of fixed asets	***	
Profit on sale of long –Term Investments	***	
Operating profit before working capital changes-		***
		***

Stage-2

Effect of changes in working capital is to be considered as follows.		
Operating profit before working capital change		***
Add : Decrease in current Assets	***	
And		
Increase in current liabilities	***	
		***

Less: Increase in current Assets ***
and
Decrease in current Liability ***

***

Cash Generated from operations ***

Apart from that, the following items is to be considered :-

Cash Generated from operations ***

Less- Income Tax paid (Net Tax Refund Received) ***

Cash flow before extraordinary items ***

Adjusted extraordinary items ***

Net cash flow used from operating Activities ***

ii) Investing Activities:

The cash flow from investing activities is derived by adding all cash inflows from the sale of assets and subtracting all the cash outflow for the purchase/ payment for fixed assets/Investments.

Cash flow from Investing Activities:-

- Proceeds from sale of Fixed Assets (Positive cash flow) ***
- Proceeds from sale of Invest ments (Positive cash flow) ***
- Purchase of shares/Debentures/Fixed Assets (negative cash flow) ***
- Purchase of Investment Instruments (Stock/Bonds) (Negative cash flow) ***
- Lending of money (Negative cash flow) ***
- Collection of Loans (Positive cash flow) ***
- Proceeds of Insurance settlements related to damaged Fixed Assets (positive cash flow) ***

Net cash flow/used in Investing Activities ***

iii) Cash flow from Financing Activities :-

Cash flow from financing activities is the third stage of cash flow statement. This past contains the sum total of the changes cased by transaction with owners or lenders to other.

Items that may be included in the financing activities is as follows:-

- Repurchase /Buy back of company stock (negative cash flow) ***
- Sale of stock (Positive cash flow) ***
- Issuance of Debt (Such as bond Debenture) (Positive cash flow) ***
- Repayment of Debt (Negative cash flow) ***
- Payment of Dividends (Negative cash flow) ***

- Redemption of preference share capital ***
  (Negative cash flow)
  Net cash flow/ used from financing Activites ***

After obtaining the cash flow/used from .Operating, Investing and financing Activities, we have to calculate Net Increase/Decrease of cash and cash equivalents by adding all these items. Then after adding the begaining/ opening balance of cash and cash equivalents with Increase/ Decrease of cash and cash equivalents, we will obtain cash and cash equivalents at the end of the year.

Limitations of cash flow statements:-

- Fails to present net income.
- Fails to assess the liquidity and solvency position.
- Neither substitute of Fund flow statement nor Income statement.
- Not to assess profitability.
- Does not conform with the companies act.
- Inter- Industry comparison is not possible.

An illustration is solved under to learn low to prepare a cash flow statement with all the three sections i-e. Operating activities, Inverting activities and financing activities.

Problem:-

From the following information, prepare a cash flow statement in the books of C Ltd. For the year ended 31.12.2019

Particulars	**Amount**
Opening cash Balance	18,000
Closing cash Balance	38,000
Decrease in Stock	8,000
Increase in sundry Creditors	12,000
Sale of Fixed Assets	30,000
Repayment of long- Term loan	50,000
Net profit for the year	20,000

Solution:-

Cash flow statement
for the ended 31.12.2019

Particulars	Amount	Amount
A. Cash flows from operating Activities:		
Net profit before Tax and Extraordinary items	20,000	
Add: Decrease in current Assets :		
Stock ` 8,000		
Add: Increase in Current Liabilities :		
Sunday creditors 12,000	20,000	
Cash flow from operating Activities-	40,000	
B. Cash flow from Investing Activities:		40,000
Sale of Fixed Assets	30,000	
Cash flow from Investing Activities:		30,000
C. Cash flows from financing Activities:-		
Repayment of long Term loan	(50,000)	
Net cash used in financing Activities		(50,000)
Net Increase in cash and cash equivalents(A+B+C)		20,000
Add: Cash and cash equivalents in the begaining of the period		18,000
Cash and Cash equivalent at the end of the period		38,000

EXERCISE

i) State whether the following statements are true or False:- **(Marks-1)**

1. Cash flow statement and cash Accounts are same.

Answer: ——————————————————————

2. Cash withdrawn from bank do not affect flow of cash.

Answer:——————————————————————

3. Increase in the amount of prepaid expenses results in decrease of cash.

Answer:——————————————————————

4. Salary paid in an investing Activity.

Answer:——————————————————————

5. Investment in short term marketable securities is cash equivalent.

Answer:——————————————————————

6. Gain in sale of assets is deduct from profits earned while calculating cash flow from operating activities.

Answer:——————————————————————

7. Preliminary Expenses written off are deduct from profits earned while calculating cash flow from operating activities.

Answer:——————————————————————

8. Proceeds from long Term loans is inflow of cash.

Answer:——————————————————————

9. Sale of Gods on credit does not affect flow of cash.

Answer:——————————————————————

10. Proceeds from Goodwill is an Investing Activity.

Answer:——————————————————————

11. Buy back of shares is a financing Activity.

Answer:——————————————————————

12. Underwriting commission paid on issue of shares increases outflow of financing Activates.

Answer:——————————————————————

13. Cash flow statement is prepared on the basis of accrual basis of accounting.

Answer:——————————————————————

14. Dividend Received is a financing Activities.

Answer:——————————————————————

ii) Fill in the blanks:- **Marks-1**

1. Decrease in Bank overdraft is shown under ______ activities in a cash flow statement.

Answer:——————————————————————

2. Dividend paid is shown under ______ activities in a cash flow statement.

Answer:——————————————————————

3. Depreciation is added back to net profit to determine net profit before tax because it is a______ item.
Answer:————————————————————————————
4. Issue of Debenture is______ of cash in a cash flow statement.
Answer:——————————————————————————
5. Cash advances and loans made to third parties is shown______activities in a cash flow statement.
Answer:————————————————————————————————
6. Amount Transferred to General Reserve will affect ______activities in a cash flow statement.
Answer:————————————————————————————————
7. Cash payments to acquire intangible assets to shown under______ activates in a cash flow statement.
Answer:————————————————————————————————
8. Balance of marketable securities is shown under ______ in a cash flow statement.
Answer:————————————————————————————————
9. Amount received from Debtors is shows under______ activities in a cash flow statement.
Answer:————————————————————————————————
10. Interest paid on long term debts is shown under______ activities in a cash flow statement.
Answer:————————————————————————————————

iii) Classify the following into (a) Operating Activities, (b) Investing Activities,(c) Financing activities and(c) Cash and Cash equivalents while preparing a cash flow statement:-
Marks-1

1. Sale of Building.
2. Purchase of Furniture.
3. Cash Received from Trade Receivables.
4. Cash Sales.
5. Repayment of long Term loan.
6. Dividend paid.
7. Redemption of debentures and preference shares.
8. Manufacturing Expenses.
9. Buy back of equity shares.
10. Cash paid to sundry Creditors.
11. Issue of share capital or Debentures.
12. Interest paid on debentures.
13. Selling and distribution expenses.
14. Bank Balance.
15. Purchase of Goodwill.
16. Sale of patents.
17. Office expenses.
18. Income Tax paid.
19. Dividend Received on shares.
20. Interest Received on Investment.

21. Investment in short Term marketable securities.
22. Income Tax Refund Received
23. Bank Balance.
24. Purchase of Investments.
25. Rent Received.
26. Salary Paid.
27. Sale of Investments.
28. Commission and Royalty Received.
29. Cash paid against services taken.
30. Cash Received against services rendered.

iv)Answer The following MCQ/VSA Questions **Marks-1**

1. Define cash flow statement?

Answer:-

2. State any two advantages of preparing cash flow statement.

Answer:-

3. Give one Limitations of cash flow statement?

Answer:-

4. What is meant by cash equivalents?

Answer:-

5. What is meant by operating Activities?

Answer:-

6. Give two examples of cash flow from operating Activities?

Answer:-

7. What is meant by Investing Activities?

Answer:-

8. Give two examples of cash flow from Investing Activities?

Answer:-

9. What is meant by financing Activities?

Answer:-

10. Give two examples of cash flow from financing Activities?

Answer:-

11. The objectives of cash flow statements are—
    (a) Short Term cash planning. (b)Evaluation of liquidity.
    (c) Analysis of cash position. (d) All of the above.
12. Cash flow statement is based upon—
    (a) Cash basis of accounting. (b) Accrual basis of accounting.
    (c) Credit basis of accounting.(d) None of the above.

13. Statement of cash flow includes.

(a) Investing activities. (b) Financing activities.

(c) Operating activities. (d) All of the above.

14. Which of the following is a source of cash?

(a) Cash withdrawn from bank . (b) Cash deposited into bank.

(c) Sale of marketable securities. (d) Sale of Goods costing Rs 10,000 for 8000.

15. Which of the following is not source of cash—

(a) Purchase of machinery. (b) Issue of shares.

(c) Sale of Asset. (d) Dividend Received.

16. Which of the following is not application of cash—

(a) Increase in Bills Payable. (b) Increase in prepaid Expenses

(c) Increase in Debtors. (d) Increase in Stock.

17. An example of cash flow from operating activity is—

(a) Issue of equity shares. (b) Interest paid on Term deposits by a bank.

(c) sale of Tangible assets. (d) Purchase of own debenture

18. How you will treat payment of dividend in a cash flow statement?

(a) Operating activities. (b) Investing activities.

(c) Financing Activities. (d) Cash and cash equivalent.

19.Cash flow from an investing Activity is—

(a) Cash Received from customers. (b) Sale of Investment.

(c)Payment of Dividends. (d) Purchase of Fixed Assets.

20. Which item will comes under financial activities—

(a) Interest paid . (b) Issue of equity share.

(c) Redemption of equity share. (d) All of the above.

21. Which of the following would not be considered a cash flow from operating Activities?

(a) Interest received on loans. (b) Payments for the inventory.

(c) Tax Payments (d) Payment of Debt principle.

22. Which of the following would not represent the outflow of cash?

(a) Retirement of long term Debt. (b)Purchase of land for cash.

(c) Sale of land for cash. (d) None of the above.

23. Depreciation expense is a:

(a) Investing (b) Operating (c) Financing (d) Supplemental.

24. Retirement of long term bonds payable is a :

(a) Operating (b) Investing (c) Financing (d) All of the above.

25. Amortisation of an intangible asset under—

(a) Operating (b) Investing (c) Financing (d) All of the above.

iv) Long Type Questions:- **Marks : 3/4/5/6**

1) Define Cash flow statement? What are the objectives of cash flow statement?

Answer:————————————————————

2) Describe the various activities classified (As per As-3 revised) while preparing cash flow statement?

Answer:————————————————————

3) State the Importance/ uses of cash flow statement?

Answer:————————————————————

4) What are the limitations of cash flow statement?

Answer:————————————————————

5) Write short notes from the following:—

i)Extraordinary items ii) Non cash Transactions

iii)Interest and Dividend. Iv) Cash and cash equivalents.

Answer:————————————————————

v) PRACTICAL PROBLEMS:

Problem:-1

From the following information, Prepare a cash flow statement from operating Activities of ABC Ltd.

Particulars	**Amount(Rs)**
Balance of profit and Loss A/C 1st April, 2019	Rs 25,000
Balance of profit and Loss A/C 31st March,2020	Rs 80,000
Amortisation of Goodwill	Rs 8,000
Depreciation on Tangible Assets	Rs 2,500
Loss on sale of Machine	Rs 20,000
Provision for Taxation	Rs 15,000
Transfer to General Reserve	Rs 10,000

Decrease in Trade Receivables	Rs 22,000
Decrease in Trade payables	Rs 4,700
Outstanding expenses on 1st April, 2019	Rs 5,000
Outstanding expenses on 31st March, 2020	Rs 6,500
Prepaid Expenses on 1st April,2019	Rs 2,000

Problem:-2

The following is The position of current assets and Liabilities of D Ltd.

Particulars	31-03-2020	31-03-2019
Provision for Doubtful Debts	3,000	4,000
Short term loans	19,000	10,000
Sundry Creditors	10,000	15,000
Bills Receivable	18,000	16,000
Sundry Debtors	10,000	12,000
Bills payable	40,000	20,000

The company incurred a loss of Rs 40,000 during the year. Calculate cash flow from operating activities.

Problem: 3

From the following information of B Ltd, prepare a cash flow statement from operating Activities.

Particulars	31.03.2019	31.03.2020
Profit and Loss A/c	3,00,000	3,50,000
Provision for Depreciation	60,000	80,000
Prepaid Rent	6,000	9,000
Outstanding salary	18,000	15,000
Goodwill	40,000	32,000
Provision for Doubtful Debts	10,000	14,000
Bills Receivable	60,000	58,000
Sundry Debtors	80,000	40,000
Cash and Bank Balance	30,000	25,000

Problem: 4

Arvind Ltd. Has a net income of Rs 4,50,000 for the year ended 31st March, 2020. Depreciation for the year was Rs 2,00,000. There was a gain of Rs 60,000 on assets sold which was credited to profit and loss Account. Bills Receivable increased during the year was Rs 60,000.

Compare the cash flow statement from operating Activities.

Problem:5

From the following Balance sheet of BTC Ltd. And the additional information as at 31.12.2020, prepare a cash flow statement.

BTC Ltd.
As at 31.12.2020

	Particulars	Note No.	31.12.2019(Rs)	31.12.2020(Rs)
I.	**EQUITY AND LIABILITIES**			
	(1) Shareholders funds :			
	(a) Share Capital		20,00,000	29,00,000
	(b)Reserve and Surplus	1	6,00,000	5,00,000
	(2) Non-Current liabilities:			
	Long Term Borrowings	2	5,00,000	8,00,000
	(3) Current Liabilities:			
	Trade payables		1,00,000	1,50,000
	Short Term Provisions	3	56,000	76,000
	Total		**32,56,000**	**44,26,000**
II.	**ASSETS:**			
	(1) Non-Current Assets:			
	(a)Fixed Assets:			
	(i) Tangible Assets	4	18,00,000	25,00,000
	(ii) Intangible Assets		9,00,000	10,00,000
	(2) Current Assets:			
	(a)Current Investments		78,000	89,000
	(b) Inventories		4,00,000	8,00,000
	(c)Cash and cash equivalents		78,000	37,000
	Total		**32,56,000**	**44,26,000**

Notes to Accounts :

Note No.	Particulars	1.12.2019(Rs)	31.12.2020(Rs)
1	Reserve and Surplus:	6,00,000	5,00,000
	(Balance of statement of profit and loss A/C)	6,00,000	5,00,000
2	Long Term Borrowings:	5,00,000	8,00,000
	8% Debentures	5,00,000	8,00,000

3.	Short–Term Borrowings:	56,000	76,000
	Provision for Taxation	56,000	76,000
4.	Tangible Assets:		
	Machinery	23,00,000	31,00,000
	Less-Accumulated depreciation	(5,00,000)	(6,00,000)
		18,00,000	**25,00,000**

Additional Information :

I) During the year a machinery Costing Rs 7,00,000 on which accumulated depreciation was Rs 2,60,000 was sold for Rs 5,30,000.

II) Debentures were issued on 01.01.2020

Problem: 6

Following are the Balance sheets of cairn limited as at 31st December, 2019 and 2020.

Particulars	Note No.	31.12.2020	31.12.2019
I. EQUITY AND LIABILITIES			
(1) Shareholders funds :			
(a)Share Capital		3,50,000	3,50,000
(b)Reserve and Surplus	1	4,78,000	3,56,000
(2) Non-Current liabilities:			
Long Term Borrowings	2	1,70,000	-
(3) Current Liabilities:			
(a) Trade payables		1,09,000	2,03,000
(b) Short Term Provisions	3	35,000	40,000
		11,42,000	**9,49,000**
II. ASSETS:			
(1) Non-Current Assets:			
Fixed Assets:			
(i) Tangible Assets	4	2,20,000	3,00,000
(ii) Intangible Assets	5	60,000	50,000
(2) Current Assets:-			
(a) Current Investments		70,000	78,000
(b) Inventory		1,70,000	2,15,000
(c) Trade Receivables		4,55,000	2,10,000
(d) Cash and Bank Balance		1,67,000	96,000
		11,42,000	**9,49,000**

Note to Accounts :

Note No.	Particulars	31.12.2020	31.12.2019
1	Reserve and Surplus:		
	Retained Earnings	4,78,000	3,56,00
		4,78,000	3,56,00
2	Long Term Borrowings:		
	6% Debenture	1,70,000	-
		1,70,000	Nil
3	Short Term Provisions:		
	Provision for Taxation	35,000	40,000
		35,000	40,000
4.	Tangible assets:		
	Land	40,000	1,50,000
	Plant and Machinery	1,80,000	1,50,000
		2,20,000	**3,00,000**

Additional Information:-

(i) Depreciation on plant and Machinery is to be provided @ 10% on last years balance.

(ii) Gain on sale of land is Rs 30,000.

(iii) Interest paid on mortgage loan amounted to Rs 24,300.

(iv) Provision for Income tax made during the year 2020 was Rs 32,000.

Effect of such items on the cash flow statement:

(1) Proposed dividend :

Amount of Dividend proposed for the previous year is to be shown as outflow of cash assuming that the shareholders have approved the proposed dividend as was recommended. It will be added to determine net profit before tax and extraordinary items under cash flow from operating activities.

Whereas, No effect is to be given for Dividend that is proposed for the current year.

(2) Provision for Taxation:

(a) If the provision for taxation accounts appeare only in the balance sheet: In this case the previous year amount is Treated as outflow in operating activities and the current year amount is added while calculating the profit before Tax.

(b) If the provision for taxation accounts appears in Balance sheet and additional information is also given regarded the payment or provision for tax during the year.

In this case a separate Ledger A/C is to be prepared in the name of provision for taxation and the treatment to be done accordingly.

(3) Bonus share:

Bonus shares are additional shares given to existing shareholders without any additional cost based upon the number of numbers of shares that a shareholder hold/ owns hence bonus shares are not shown in cash flow statement because there is no flow of cash.

(4) Bank overdraft and cash credit:

As per revised CBSE Guidelines, Bank overdraft and cash credit will be treated as short Term borrowings and as per para 17 of AS-3 (Revised) Cash proceeds from short term borrowings should be classified under financing Activities instead of cash equivalents.

(5) Payment of Interim Dividend:

If Information is given regarding Interim Dividend Paid in adjustments, It will be added back to profits while Calculating Net profit before tax and extraordinary items and will also be shown as payment of cash under the heading cash flow financing Activities.

Answer Key

(I) True/False:

True: 2,3,5,6,8,9,10,11,12.

False:1,4,7,13,14.

(II) Fill in The blanks:

1. Financing 2. Financing 3. Non-Cash 4. Inflow 5.Investing. 6. Operating. 7. Investing 8. Cash and Cash equivalents 9.Operating. 10. Financing.

Answer Key

(III) Operating Activities: 3,4,8,10,1317,18,22,25,26,28,29,30.

Investing Activities : 1,2,15,16,19,20,24,27.

Financing Activities: 5,6,7,9,11,12.

Cash and cash Equivalents: 14,21,23.

(IV) VSA/MCQ'S QUESTIONS :

Q. No.1 to10: See Text book.

11.(d); 12.(a); 13.(d); 14.(d); 15.(a); 16.(c); 17.(b); 18(c); 19. (b); 20. (d); 21. (d); 22.(c); 23.(b); 24.(c); 25(a);

v) Long Type Questions:

Q.No.1 to 5: See text book

vi)PRACTICAL PROBLEMS:

Problem: 1- Net cash flow from operating Activities Rs 1,37,100

Problem : 2- Net Cash used (or lost) in operating Activities-(Rs 26000)

Problem: 3- Net cash flow from operating Activities Rs1,18,000.

Problem: 4- Net cash flow from operating Activities Rs 6,10,000.

Problem: 5- Net cash used in operating Activities(Rs 96000)
Net cash used in Investing Activities (Rs 10,70,000)
Net cash flow from financing Activities Rs 11,36,000.

Problem: 6- Net cash used in operating Activities-(Rs 1,67,700)
Net cash from Investing Activities - Rs 85,000.
Net cash from financing Activities- Rs 1,45,700.