CLASS XII

PART A : Accounting for Partnership Firms and Companies

Unit 1 : Accounting for Partnership Firms - Fundamentals

1 Partnership : features, Partnership deed.

2. Provisions of the Indian Partnership Act 1932 in the absence of partnership deed.

3. Fixed v/s fluctuating capital accounts, division of profit among partners, guarantee of profits, past, adjustment (relating to interest on capital, interest on drawing, salary and profit sharing ratio), preparation of P & L Appropriation account.

4. Goodwill : nature, factors affecting and methods of valuation - average profit, super profit, and capitalization.

Unit 2 : Accounting for Partnership firms : Reconstitution and Dissolution

1 Change in the Profit sharing Ration among the existing partners - sacrificing ratio, gaining ratio. Accounting for revaluation of assets and re-assessment of liabilities and distribution of reserves and accumulated profits.

2. Admission of a partner - effect of admission of a partner on change in the profit sharing ratio, treatment of goodwill (as per AS 26), treatment for revaluation of assets and re assessment of liabilities, treatment of reserves and accumulated profits, adjustment of capital accounts and preparation of balance sheet.

3. Retirement and death of a partner : effect of retirement/death of a partner on change in profit sharing ratio, treatment of goodwill, treatment for revaluation of assets and reassessment of liabilities, adjustment of accumulated profits and reserves, calculation of deceased partner's share of profit till date of death. Preparation of deceades partner's capital account, executors's account and preparation of balance sheet.

4. Dissolution of partnership firms : types of dissolution of firm. Settlement of accounts-preparation of realization account, and other related accounts (excluding piecemeal distribution, sale to a company and insolvency of partner's firm).

Unit 3 : Accounting for Share Capital

1 Share and share capital : nature and types.

2. Accounting for share capital : issues and allotment of equity shares, private placement of shares, Public subscription of shares - over subscription and under subscription of shares; Issue at par and at premium and at discount, calls in advance and arrears, issue of shares for consideration other than cash.

3. Accounting treatment of forfeiture and re-issue of shares.

4. Disclosure of share capital in company's Balance Sheet only.

Unit 4 : Accounting for Debentures

1 Debentures : Issue of debentures at par, at premium and at discount. Issue of debentures for consideration other than cash, debentures as collateral security, interest on debentures

2. Redemption of debentures : Lump Sum, draw of lots and conversion

PART B : Financial Statement Analysis

Unit 5 : Analysis of financial Statements

1. Financial statement of a company : balance sheet of company in the prescribed from with major headings and sub headings (as per schedule VI to the Companies Act 1956).

2. Financial Statement Analysis : objectives and limitations.

3. Tools for Financial Statement Analysis : comparative statements, common size statements, cash flow analysis ratio analysis.

4. According ratios : current ratio and quick ratio.

5. Solvency Ratios : Debt of Equity Ratio, Total Asset to Debt Ratio, Proprietary Ratio, Interest Coverage Ratio.

6. Activity ratios : Stock Turnover Ratio, Debtors Turnover Ratio, Creditors Turnover Ratio, Working Capital Turnover Ratio

7. Profitability Ratios : Gross Profit Ratio, Operating Ratio, Creditors Turnover Ratio, Working Capital Turnover Ratio.
8. Profitability Ratios : Gross Profit Ratio, Operating Ratio, Operating Profit Ratio, Net Profit Ratio and Return on Investment.

Unit 6 : Cash Flow Statement

1. Meaning objectives and preparation (as per AS 3 revised) (Indirect Method)

Unit 7 : Project Work

1. Kindly refer to the Guidlines published by the CBSE

Part C : Computerised Accounting

Unit 5 Overview of Computerised Accounting System

1. Introduction : Application in Accounting
2. Features of Computerised Accounting System
3. Structure of CAS
4. Software Packages :

   - Generic

Chapters

CHAPTER 1

Accounting for Partnership Firms Fundamentals

According to Section- 4 of the Indian Partnership Act, 1932 :

"Partnership is the relationship between persons who have agreed to the share the profits of a business carried on by all or any one of them acting for all"

Features of Partnership

1. There must be at least two persons to form a valid partnership. Section 11 of the Indian Partnership Act, 1932 restrict the **(maximum) number of partners to 10 for carrying on banking business and 20 for other kind of business.**
2. **Partnership comes into existence by an agreement (**either written or oral) among the partners. The written agreement among teh partners is called Partnership Deed.
3. A Partnership can formed for the purpose of **carrying at sharing the profits** or losses of the business
4. An agreement between the partners must be aimed at **sharing the profits or losses** of the business.
5. **A partnership can be carried on by all or any one of them acting for all.**

PARTNERSHIP DEED

The partnership deed is a written agreement among the partners which contains the terms of agreement. A partnership deed should contain the following points:

1. Name and address of the firm.
2. Name and addresses of the partners.
3. Nature of the business
4. Terms of Partnership
5. Capital contribution by each partner.
6. Interest on capital
7. Drawings and interest on drawings.
8. Profit sharing ratio
9. Interest on loan.
10. Partner's Salary/commission etc.
11. Method for valuation of goodwill

12. Accounting period of the firm
13. Rights and duties of partners.

Benefits of Partnership deed

(1) Helps to avoid dispute in future

(2) It is an evidence in the court

(3) Facilitates functioning of business by avoiding misunderstanding

RULES APPLICABLE IN THE ABSENCE OF PARTNERSHIP DEED

Profit sharing Ratio	**Equal**
Interest on Capital	**No Interest on Capital is to be allowed to any Partner**
Interest on Drawings	**No interst on Drawings is to be charged from any Partner**
Salary on Commission to a Partner	**Not Allowed**
Interest on loan by a Partner	**Interest is allowed @6% per annum**

DISTRIBUTION OF PROFITS AMONG 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 absesnce of Partnership Deed). It is an extension of Profit and Loss Acccount. **It is nominal account.**

The Journal Entries regarding Profit and Loss Appropriation Account are as follows:

1. For transfer of balance of Profit and Loss Account

Profit and Loss A/c Dr.

To Profit and Loss Appropriation A/c

(Being net profit transferred to P & L Appropriation A/c)

2. **For Interest on Capital**

1. For allowing Interest on capital

Interest on Capital A/c

To Partners' Capital/Current A/cs

(Being interest on capital allwoed @ ___ % p.a)

2. For transferring Interest on Capital to Profit and Loss Appropriation A/c :

Profit and Loss Appropriation A/c Dr.

To Interest on Capital A/c

(Being interest on capital transferre to P & L Appropriation A/c)

3. ***For Salary of Commission payable to a partner***

i. For allowing Salary or Commission to a partner :
Partner's Salary/Commission A/c Dr.

To Partner's Capital /Current A/cs

(Being salary/commission payable to a partner)

ii. For transferring Partner's Salary/Commission A/c to Profit and Loss Appropriation A/c :

Profit and Loss appropriation A/c Dr.

To Partner's Salary/ Commission A/c

4. ***For transfer of Reserves :***

Profit and Loss Appropriation A/c Dr.

To Reserve A/c

(Being reserve created)

5. ***For Interest on Drawings :***

1. For charging interest on a partner's drawings :

Partner's Capital/Current A/c Dr.

To Interest on Drawings A/c

(Being interest on drawings charged @ ____%p.a.)

2. For transferring Interest on drawings to Profit and Loss Appropriation A/c : Dr.

Interest on Drawings A/c

To Profit and Loss Appropriation A/c

(Being interest on drawings transferred to P & L Apprpriation A/c)

6. ***For transfer to Profit (i.e. Credit Balance of Profit and Loss Appropriation Account***

Profit and Loss Appropriation A/c Dr.

To Partners Capital A/cs

(Being profits distributed among partners)

SPECIMEN OF PROFIT AND LOSS APPROPRIATION ACCOUNT

Profit and Loss Appropriation Account

For the year ending on ________________

Dr. **Cr.**

Particulars	₹	Particulars	₹
To Interest on Capital A B To Partner's Salary/ Commission To Reserves To Profits transferred to capital A/c of : A B		By Profit Loss A/c (Net Profits transferred from P& L A/c) By Interst on Drawings A B	

PARTNERS' CAPITAL ACCOUNTS

Partner's Capital Accounts : It is an account which represents the partner's interst 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 following any of the following two methods:

(1) Fixed Capital Accounts

(2) Fluctuating Capital Accounts

1. Fixed Capital Accounts

Under this method the following two accounts are maintained:

1. **Capital Account**

This account will always show a credit balance. Balance of Capital account remains fixed and only the following two transactions are recorded in the Fixed Capital Accounts:

Additional Capital Introduced

Capital Withdrawn or Drawings out of Capital

Dr. **Partner's Capital A/cs** Cr.

Particulars	X ₹	Y ₹	**Particulars**	X ₹	Y ₹
To Cash/ Bank A/c			By Balance b/d		
(Capital Withdrawn)			(Opening Cr. Balance)		
To Balance c/d			By Cash/Bank A/c		
(Closing balance)			(Additional Capital		
			Introduced)		

2. 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

Dr. **Partner's Capital A/cs** Cr.

Particulars	X ₹	Y ₹	**Particulars**	X ₹	Y ₹
To Balance b/d			By Balance b/d		
(Opening Dr. Balance)			(Opening Cr. Balance)		
To Drawings			By Interest on Capital		
(out of Profits)			By Partner's Salary or		
To Interest on Drawings			Commission		
To Profit and Loss A/c			By Profit and Loss		
(Share in losses)			Appropriation A/c		
To Balance c/d			(Share in Profits)		
(Closing credit Balance)			By Balance c/d		
			Closing Dr. Balance		

Note :

1. ***Debit balance of Current Account is shown in Assets side of Balance Sheet.***
2. ***Credit balance of Current Account is shown in Liabilities side of Balance Sheet.***
3. ***Balance of Capital Accounts are always shown in Liabilities side of Balance Sheet as this account will always show a credit balance when capital is fixed***

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

Dr. **Partner's Capital A/cs** **Cr.**

Particulars	X ₹	Y ₹	**Particulars**	X ₹	Y ₹
To Balance b/d			By Balance b/d		
(Opening Dr. Balance)			(Opening Cr. Balance)		
To Cash/Bank A/c			By Cash/ Bank A/c		
(Capital Withdrawn)			(Additional Capital		
To Drawings			Intoduced)		
(out of profits)			By Interest on Capital		
To Interest on Drawings			By Partner's Salary or		
To Profit and Loss A/c			Commission		
(Share in losses)			By Profit and Loss		
To Balance c/d			Appropriation A/c		
(Closing credit Balance)			(Share in Profits)		
			By Balance c/d		
			(Closing Dr. Balance)		

INTEREST ON CAPITAL

Interest on partners' capital will be allowed only when it has been specifically mentioned in the partnership deed. Interest on Capital can be treated as either:

a. An Appropriation of profit; or

b. A Charge against profits

A. Interest on Capital : An Appropriation of Profits:

In Case of Losses	***Interest on Capital is NOT ALLOWED***
In Case of Sufficient Profits	***Interest on Capital is ALLOWED IN FULL***
In case of Insufficient Profits	***Interest on Capital is allowed only to the extent of profits 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 or losses

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a. In case of Sufficient Profits

Profit and Loss Appropriation A/c Dr.

To Interest on Capital A/c

(Being interest on capital transferred to P & L Appropriation A/c)

b. In case of Insufficient Profits or Losses

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

To Interest on Capital A/c

(Being interest on capital transferred to P&L Adjustment A/c)

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		₹
Capital at the End		
Add : 1. Drawings	xxxxxx	________
2. Interest on Drawings	xxxxxx	
3. Losses during the Year	xxxxxx	________

Less : 1. Additional Capital Introduced	(xxxxxx)	
2. Profits during the year	(xxxxxx)	
	--------	(------------)
Opening Capital		________

For additional capital interest is calculated for period for which capital is utilised e.g if additional capital is introduced on 1 April in firm where accounts are closed on 31st December

Interest = Amount introduced x Rate/100x9/12

as money is utilised for 9 months

INTEREST ON DRAWINGS

Interest on drawings in charged by the firm only when it is clearly mentioned in Partnership Deed. It is calculated with reference to the time period for which the money was withdrawn.

Case 1 : When Rate of Interest on Drawings is given in %

Interest on Drawings is calculated with a flat rate irrespective of date of drawings.

Case 2 : ***When Rate of Interest on Drawings is given in % p. a.***

1. **When date of Drawings is not given**

   Interest on Drawing = Total Drawings x Rate/100 x 6/12

   Note : Interest is calculated for a period of 6 months

2. **When date of Drawings is given**

   Interest on Drawing = Total Drawings x Rate/100 x Time Left after drawings/12

Case 3 : When different amount are withdrawn on different date :

We have the following two methods to calculate the amount of Interest on Drawing :

1. **Simple Interest Method**

   In this method, interest on drawing is calculated for each amount of drawing indivdually of the basis of periods for which

2. **Product Method**

   In this method, the amounts of drawings are multiplied by the period for which it remained withdrawn during the period, Interest for 1 month is calculated on the sum of these products.

We can explain the above mentioned two methods with the help of an example.

Example :

Aarushi and Simran are partners in a firm. During the year ended on 31st March 2011 Aarushi makes the drawings as under :

Date of Drawing	Amount (₹)
01-08-2010	5,000
31-12-2010	10,000
31-03-2011	15,000

Partnership Deed provided that partners are to be charged interest on drawings @ 12% p.a. Calculate the interest chargeable to Aarushi Drawing by using Simple Interest Method and Product Method.

SOLUTION

1. Simple Interest Method

Date of Withdrawal	Amount of Drawings (₹)	Months till March 31, 2011	Interest @ 12% p.a (₹)
01.08.2010	5,000	08	400
31.12.2010	10,000	03	300
31.03.2011	15,000	00	000
			700

2. Product Method

Date of Withdrawal	Amount of Drawings (₹)	Months for which amount has withdrawn till December 31, 2011	Product (₹)
01.08.2010	5,000	08	40,000
31.12.2010	10,000	03	30,000
31.03.2011	15,000	00	00000
			70,000

Interest on Drawing = Total Product x Rate/100xTime/12 (in months)

= 70,000x12/100x1/12

= ₹ 700

Case 4 : When an equal amount is withdrawn regularly

Interest on Drawing can be calculated using either Product Method or Direct Method (i.e., Short Cut Method)

Direct Method will be used only if all the following three conditions are satisfied :

1. Amount should be same throughout the period
2. Date of Drawings should be same throughout the period
3. Drawings should be made throughout the period regularly without any gap.

Interst on Drawing = Total Product x Rate/100 x T/12

T= Time (in months) for which interest is to be charged

T=Time left after first drawing + Time left after last drawing/2

Value of T under Different circumstances will be as under :

	Monthly Drawings for 12 Months	Quarterly Drawings for 12 Months	Half-Yearly Drawings for 12 Months	Monthly Drawings for 06 Months
When drawing are made in the Beginning of each period	**6.5**	**7.5**	**9**	**3.5**
When drawing are made in the Middle of each period	**6**	**6**	**6**	**3**

When drawing are made in the End of each period	**5.5**	**4.5**	**3**	**2.5**

Illustration :

Calculate interest on drawings of Mr. X @10% p.a if he withdrew ₹ 1000 per month (i) In the begnning of each Month (ii) In the middle of each month (iii) at end of each month.

Total Amount withdrawn = ₹1000x12 = 12,000

(i) Interest on drawing = Amount x Rate/100 x 6.5/12

= 12,000 x 10/100x6.5/12 = ₹ 650

(ii) Interest on drawing = Amount x Rate/100 x 6/12

= 12,000 x10/100x6/12 =₹600

(iii) Interest on drawing = Amount x Rate/100x5.5/12

= 12,000 x 10/100 x 5.5/12 = ₹550

Illustration 2

Calculate interest on drawing of Vimal if the withdrew Rs.48000 in year withdrawn evenly (1) at beginning of each Quarter (ii) in the middle of each Quarter (iii) at end of each Quarter rate is 10%P. A.

Solution

Case I - Drawing made on begnning of each Quarter

Interest on drawing = Amount x Rate/100 x 7.5/12

= 48,000 x 10/100 x 7.5/12 = Rs.3,000

Case II - Drawing made in middle of each quarter

Interest on drawing = Amount x Rate/100 x 6/12

= 48,000 x 10/100 x 6/12 = Rs.2,400

Case III - Drawings made at end of each quarter

Interest on drawing = Amount x Rate/100 x 4.5/12

= 48,000x10/100 x 4.5/12 = Rs.1800

Similarly Interest can be calculated by following farmulas

Half yearly Drawings for year when

(a) Drawings are made in the begnning of each period (half-year)

Interest on drawing = Amount x Rate/100 x 9/12

(b) Drawings are made in the middle of each period (half year)

Interes on drawing = Amount x Rate/100 x 6/12

(c) Drawings are made at the end of each period (half year)

Interest on drawing = Amount x Rate/100 x 3/12

For monthly drawings for 6 months

(a) Drawings are made in beginning of each month

Interst = Amount x Rate/100 x 3.5/12

(b) When drawings are made in the middle of each month

Interest = Amount x Rate/100 x 3/12

(c) When drawings are made at the end of each month
Interest = Amount x Rate/100 x 2.5/12

INTEREST ON PARTNER'S LOAN

It is a charge against profits. It is provided irrespective of profits or loss. It will also be provided in the absence of Partnership Deed @ 6% per annum.

The following entries are passed to record the interest on partner's loan

i. For allowing Interest on loan:

Interest on Partner's Loan A/c Dr.

To Partner's Loan A/c

(Being interest on loan allowed @___% p.a.)

ii. For transferring Interest on Loan to Profit and Loss A/c:

Profit and Loss A/c Dr.

To Interest on Loan A/c

(Being interest on loan transferred to P & L A/c)

It is always DEBITED to Profit and Loss A/c
Rent paid to a partner is also a charge against profits and it will also be DEBITED to Profit and Loss A/c.

Q.1. A and B entered into partnership on 1st April, 2010 without any partnership deed. They introduced capitals of Rs. 5, 00,000 and Rs. 3, 00,000 respectively. On 31st October, 2010, A advanced Rs. 2, 00,000 by way of loan to the firm without any agreement as to interest.

The Profit and Loss Account for the year ended 31-03-2011 showed a profit of Rs. 4, 30,000 but the partners could not agree upon the amount of interest on Loan to be charged and the basis of division of profits. Pass a Journal Entry for the distribution of the Profits between the partners and prepare the Capital A/cs of both the partners and Loan A/c of 'A'.

SOLUTION :

Profit and Loss Appropriation Account
For the year ending on 31st March, 2011

Dr. **Cr.**

Particulars	₹	Particulars	₹
To Profits transferred to Capital A/c of :		By Profit and Loss A/c Rs.	
A - 2,12,500		(Net Profits 4,30,000	
B - 2,12,500		Less : Interest on	
	4,25,000	A's Loan (5,000)	4,25,000
	4,25,000		**4,25,000**

Dr. **Partner's Capital A/cs** Cr

Date	Particular	A	B	Date	Particular	A	B
31.03.2011	To Balance c/d	7,12,500	5,12,500	01.04.2010	By Bank A/c	5,00,000	3,00,000
				31.03.2011	By Profit and Loss Appropriation A/c	2,12,500	2,12,500
		7,12,500	5,12,500			7,12,500	5,12,500

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Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.2011	Profit and Loss Appropriation A/c Dr		4,25,000	
	To A's Capital A/c			2,12,500
	To B's Capital A/c			2,12,500
	(Being profit distributed among the partners)			

Dr. **A's Loan A/c** Cr.

Date	Particulars	Amount	Date	Particulars	Amount Rs.
2011 March, 31	To Balance c/d	2,05,000	2010 Oct., 31	By Bank A/c	2,00,000
			2011 March, 31	By Interest on Loan A/c	5,000
		2,05,000			2,05,000

Note : Interest on A's Loan = Loan Amount x Rate /100x Time Left after Loan Taken/12
= 2,00,000x 6/100x 05/12
= Rs.5,000

PAST ADJUSTMENTS

If, after preparation of Final Accounts of firm, it is found that some errors or omission in accounts has occurred than such errors or omissions are rectified in the next year by passing an adjustment entry.

A statement is prepared to ascertain the net effect of such errors or omissions on partner's capital/current accounts in the following manner.

Particulars	A Rs.	B Rs.	C Rs.
A. Amount to be given (CREDITED) * Interest on Capital (Not allowed or provided at a lower rate) * Partner's Salary or Commission etc. (Omitted to be recorded) * Actual Profits (To be distributed in correct ratio)			
TOTAL A			
B. Amount already given to be taken back now (DEBITED) * Interest on Capital (If given at a higher rate) * Interest on Drawings (if not charged) * Profits already distributed in worng ratio (debited now)			
TOTAL B			
Net Effect (A-B)	+/-	+/-	+/-

+ Indicates Amount to be Credited to Partner's Capital Account
- indicates Amount to be Debited to Partner's Capital Account

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Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Partner's Capital A/c (Amount to be Debited) Dr To Partners' Capital A/c (Amount to be Credited) (Being adjustment entry passed)			

During Past - adjustment it is not compulsory that capital accounts of all partner's are affected. More than one partner's Capital Account may be debited or credited but amount of debit & credit shold be equal

Q.1 : Manoj Sahil and Dipankar are partners in a firm sharing profits and losses equally. The have omitted interest ob Capital @10% per annum for three years ended on 31st March, 2011. Their fixed Capital on which interest was to be calculated throughout the were :

Manoj	Rs.3,00,000
Sahil	Rs.2,00,000
Dipankar	Rs.1,00,000

Give the necessary adjusting journal entry with working notes.

SOLUTION :

Books of Manoj, Sahil and Dipankar

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Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Dipankar's Current A/c Dr.		30,000	
	To Manoj's Current A/c			30,000
	(Being adjustment entry passed)			

STATEMENT SHOWING ADJUSTMENT

Particulars	Manoj Rs.	Sahil Rs.	Dipankar Rs.
A. Amount to be given (Credited)			
Interest on Capital	90,000	60,000	30,000
Total A	90,000	60,000	30,000
B. Amount already given to be taken back now (DEBITED) :			
Excess Profit taken back from teh partners in their profit sharing ratio	60,000	60,000	60,000
(Rs.90,000+60,000+30,000 = 1,80,000)			
Total B	***60,000***	***60,000***	***60,000***
Net Effect (A-B)	***30,000*** ***Credit***	***Nil***	***30,000*** ***Debit***

Hint :- As closing balance sheet is given so before calculation of interest opening capital should be calculated

Q2. A and B are partners in a firm sharing profits and losses in the ratio of 3:2. The following was the Balance Sheet of the firm as on 31-03-2011 :

BALANCE SHEET
AS ON 31-03-2011

Liabilities	₹	Assets	₹
Capitals :		Sundry Assets	80,000
Rs.			
A 60,000			
B 20,000	80,000		
	80,000		**80,000**

The profits Rs.30,000 for the year ended 31-03-2011 were divided between the partners without allowing interest on capital @ 12% p.a. and salary to A Rs.1,000 per month. During the year A withdrew Rs.10,000 and B Rs.20,000.

Pass the necessary adjustment entry and show your working clearly

The profits ₹30,000 for the year ended 31-03-2011 were divided between the partners without allowing interest on capital @ 12% p.a. and salary to A ₹1,000 per month. During the year A withdrew ₹10,000 and B ₹20,000.

Pass the necessary adjustment entry and show your working clearly

Books of A and B

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Date	Particulars	L.F.	Debit ₹	Credit ₹
	B's Capital A/c Dr.		30,000	
	To A's Capital A/c			30,000
	(Being interest on capital and salary to A not Charged, now rectified)			

Working Notes :

1. Calculation of Opening Capital : As Closing Balance Sheet is given so before calculation of interest opening capital should be calculated

Particulars	A ₹	B ₹
Capital at the End	60,000	20,000
Add : 1. Drawings	10,000	20,000
	70,000	40,000
Less : Profits during the year	(18,000)	(12,000)
Opening Capital	52,000	28,000

2. Calculation of Net Effect

STATEMENT SHOWING ADJUSTMENT

Particulars	A ₹	B ₹
A. Amount to be given (CREDITED)		
Interest on Capital (Not provided)	6,240	3,360
Salary to A (Not provided)	12,000	------
TOTAL A	18,240	3,360
B. Amount already given to be taken back now (DEBITED) :		
Loss to the firm due to Interest on Capital and Salary to A be debited to the partners in their profit sharing ratio (Rs.18,240+3,360=21,600)	12,960	8,640
TOTAL B	12,960	8,640
NET Effect (A-B)	5,280 Credit	5,280 Debit

GUARANTEE OF PROFITS TO A PARTNER

Guarantee is an assurance given to the partner of the firm that at least a fixed amount shall be given to him/her irrespective of his/her actual share in profits of the firm. If actual share in profits is less than the guaranteed amount in that case the deficit amount shall be borne either by the firm or by any partner as the case may be.

Note : *Guarantee to a partner is given for minimum share in profits. If the actual share in profits is more than the minimum guaranteed amount then the actual profits will be allowed to the partner*

Case : **1. When guarantee is given by FIRM (i.e., by all the Partners of the firm)**

1. Guaranteed amount to a partner is written in Profit and Loss Appropriation A/c

2. Remaining profits are distributed among the remaining partners in their remaining ratio.

Case 2: When guarantee is given by a partner or partners to another partner

1. **Calculate the share in profits for the partner to whom guarantee is given**
2. **If share in profits is more than the guaranteed amount, distribute the profits as per the profit and loss sharing ratio in usual manner.**
3. **If share in profits is less than the guaranteed amount, find the difference between the share in profits and the guaranteed amount and the difference is known as Deficiency.**
   Deficiency is distributed among the partner or partners who guaranteed in a certain ratio and subtracted from his or their respective shares.

Q. A and B were partners in a firm sharing profits and losses in the ratio of 3:2. They admit C for 1/6th share in profits and guaranteed that his share of profits will not be less then Rs. 25,000. Total profits of the firm were Rs. 90,000. Calculate share of profits for each partner when:

1. Guarantee is given by firm.
2. Guarantee is given by A
3. Guarantee is given by A and B equally.

SOLUTION:

Case 1. When Guarantee is given by firm

Profit and Loss Appropriation Account
For the year ending on 31ST March, 2011

Dr. **Cr.**

Particulars	₹	Particulars	₹
To A's Capital A/c		By Profit and Loss A/c	
(3/5 of Rs.65,000)	39,000		90,000
To B's Capital A/c			
(2/5 of Rs.65,000)	26,000		
To C's Capital A/c			
(1/6 of Rs.90,000 or Rs.			
25,000 whichever is more	25,000		
	90,000		90,000

Case 2. When Guarantee is given by A

Profit and Loss Appropriation Account
For the year ending on 31ST March, 2011

Dr. **Cr.**

Particulars		₹	Particulars	₹
To A's Capital A/c			By Profit and Loss A/c	
(3/6 of Rs.90,000)	45,000		(Net Profits)	90,000
Less : Deficiency				
Borne for C	(10,000)	35,000		
To B's Capital A/c				
(2/6 of Rs.90,000)		30,000		
To C's Capital A/c				
(1/6 of Rs.90,000	15,000			
Add : Deficiencey				
Recover from A	10,000	25,000		
		90,000		90,000

Case 3. When Guarantee is given by A and B equally

Profit and Loss Appropriation Account
For the year ending on 31ST March, 2011

Dr. **Cr.**

Particulars		₹	Particulars	₹
To A's Capital A/c			By Profit and Loss A/c	
(3/6 of Rs.90,000)	45,000		(Net Profits)	90,000
Less : Deficiency				
Borne for C				
(1/2 of 10,000)	5,000	30,000		

To B's Capital A/c				
(2/6 of Rs.90,000)	30,000			
Less : Deficiency				
Borne for C				
(1/2 of 10,000)	5,000			
	----------	25,000		
To C's Capital A/c				
(1/6 of Rs.90,000	15,000			
Add : Deficiency				
Recover from A	5,000			
Deficiency				
Recover From B	5,000	25,000		
		90,000		90,000

CHAPTER 2

Goodwill : Nature and Valuation

Meaning of Goodwill:

Goodwill places the organization at a good position due to which the organization is able to earn higher profits without any extra efforts. Goodwill cannot be seen but felt.

Therefore goodwill is called an Intangible asset.

Factors affecting the value of Goodwill :

1. Efficient management
2. Quality of products
3. Location of business
4. Availability of raw material
5. Favorable contracts

Need for valuing goodwill : Whenever the mutual rights of the partners changes then party which makes a sacrifice must be compensated. This basis of compensation is goodwill so we need to calculate goodwill.

Mutual rights change under following circumstances

1) When profit sharing ratio changes

2) On admission of a partner

3) On Retirement or death of a partner

4) When amalganation of two firms taken place.

5) When partnership firm is sold.

Methods of valuation of goodwill :

1. Average profit method
2. Super profit method
3. Capitalization method

Average Profit Method

The profit earned by a Firm during previous accounting periods on an average basis is called average profit. Goodwill is calculated on the basis of average profit due to future expectations of earning capacity of the firm.

Illustration 1. (Average Profit Method)

Akanksha,Chetna and Dipanshu are partners in a firm sharing profits and losses in the ratio of 3:2:1. They decide to take Jatin into partnership from January 1,2012 for 1/5 share in the future profits. For this purpose , goodwill is to be valued at 2 times the average annual profits of the previous four years. The average profits for the past four years were:

Formula

Average Profit = Total Profits/No. of Years

Goodwill = Average Profit x Number of years of purchase.

Year	₹
2008	96,000
2009	60,600
2010	62,400
2011	84,400

Calculate the value of goodwill.

Solution:

Year	₹
2008	96,000
2009	60,600
2010	62,400
2011	84,400
Total	3,03,400

Average Profit = Total Profit/No. of Years

Average profit = 3,03,400/4=75,850

Goodwill = Average Profit x Number of Years of Purchase

Goodwill = 75,850x2=1,51,700

Super Profit Method

If a firm earns higher profit in comparison to normal profit (generally earned by other firms of same industry) then the difference is called Super Profit. Goodwill is calculated on the basis of Super profit due to future expectations of learning capacity of the firm.

Super profit = Average profit - Normal profit

Normal Profit = Investment (Capital Employed) x Normal Rate of Return/100

Illustration 2. (Super Profit Method)

A firm earned net profits during the last three years as :

Year	2008-09	2009-10	2010-11
Profit (₹)	36,000	40,000	44,000

The capital investment of the firm is ₹ 1,20,000. A fair return on the capital having regard to the risk involved is 10%. Calculate the value of goodwill on the basis of three years purchase of the average profit for the last three years.

Solution :

Average profit : 36000+40000+44000/3=40000

Normal Profit = Capital Employed x Normal Rate of Return/100

Normal Profit : 120000x10/100 = 12,000

Super profit = Average profit - Normal profit

= 40,000-12,000=28,000

Goodwill = Super profit x number of years purchased

= 28,000 x 3 = 84,000

Capitalisation Method

In this method capitalized value of the firm is calculated on the basis of normal rate of return. Difference between teh capitalized value and actual capital employed is called goodwill.

Illustration 3 (Capitalisation Method)

A earns ₹ 1,20,000 as its annual profits, the rates of normal profit being 10% The assets of teh firm amounted to ₹ 14,40,000 and liabilities to ₹ 4,80,000. Find out the value of goodwill by capitalization method.

Solution :

Capitalized value of the firm = Average profit x 1000/ Rate of normal profit

= 1,20,000x10/100 = 12,00,0005

Capital employed = Total assets - liabilities

= 14,40,000 - 4,80,000 = 9,60,000

Goodwill = capitalized value - capital employeed

= 12,00,000-9,60,000=2,40,000

Illustration 4 . (Average profit method)

A and B are partners in a firm. They admit C into the firm. The goodwill for the purpose is to be calculated at 2 year's purchase of the average normal profits of the last three years which were ₹ 10,000, ₹ 15,000 and ₹ 30,000 respectively. Second years profit included profit on sale of Machinery ₹ 10,000. Find the value of goodwill of the firm on C's Admission.

Solution

(1) Calculation of Average Profit :

Year ended	₹
Ist Year	10,000
2nd Year (₹15,000-₹10,000)	5,000
3rd Year	30,000
Total Profits	45,000

Average profit = Total profit/No. of years

= ₹ 45,000/3=15,000

Illustration 5 (Super profit method)

The average net profits expected of a firm in future are ₹ 68,000 per year and capital invested in the business by the firm is ₹ 3,50,000. The rate of interest expected from capital invested in this class of business is 12%. The remuneration of the partners is estimated to be ₹ 8,000 for the year. You are required to find out the value of goodwill on the basis of two years' purchase of super profits.

Solution

Average Profit = Average Net Profit - Partner's remuneration

(1) Average profit = ₹ 68,000-₹ 8,000 = ₹60,000

(ii) Normal profit= Capital employed x Normal rate of return/100

= ₹ 3,50,000x12/100= ₹ 42,000

(iii) Super Profit = Average profit - Normal profit

= ₹ 60,000- ₹ 42,000 = ₹ 18,000

(iv) Value of goodwill = Super profit x No. of years ' purchase

= ₹ 18,000x2 = ₹ 36,000

Illustration 6. (Super profit method)

On April 1st, 1998 an existing firm had assets of ₹ 75,000 including cash of ₹ 5,000. The partners' capital accounts showed a balance of ₹ 60,000 and reserves constituted the rest. If the normal rate of return is 20% and the goodwill of the firm is valued at ₹ 24,000 at 4 years purchase of super profits, find the averages profits of the firm

Solution :

(1) Calculation of Normal Profit :

Capital employed x normal rate/100

=75,000x20/100 = ₹ 15,000

(2) Calculation of Super Profit :

Goodwill = Super profit x No. of years' purchase

₹ 24,000 = Super Profit x4

Super Profit = ₹ 24,000 = ₹6,000

(3) Calculating of Average Profit :

Super Profit = Average Profit - Normal Profit

₹ 6,000 = Average Profit - ₹ 15,000

Average Profit = ₹ 6,000+ ₹ 15,000 = ₹ 21,000

CHAPTER 3

Reconstitution of Partnership

Meaning of Reconstitution:

Any change in agreement of partnershipis called reconstitution of partnership firm. In following circumstances a partnership firm may be reconstituted:

1. Change in Profit Sharing Ratio
2. Admission of a partner
3. Retirement/Death of a partner

Change in profit sharing ratio among the existing partners

Meaning:

When all the partners of a firm agree to change their profit sharing ratio, the ratio may be changed. In this case one profit is purchasing a share of partner from another one. In other words, share of one partner may increase and share of another partner may decrease.

Accounting treatment of goodwill:

In case of change in profit sharing ratio, the gaining partner must compensate the sacrificing partner by paying the proportionate amount of goodwill.

Illustration 1

Amit and Kajal were partners in a firm sharing profits in the ratio of 3:2. With effect from January 1,2012 they agreed to share profits equally. For this purpose the goodwill of the firm was valued at '60,000. Pass the necessary journal entry.

Solution:

Old ratio of A and B = 3:2

New ratio of A and B = 1:1

Sacrifice or Gain:

Amit = 3/5 – 1/2 = 6-5/10 = 1/10 Sacrifice

Kajal = 2/5 – 1/2 = 4-5/10 = 1/10 Gain

Journal

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2012 Jan 1	Kajal capital A/c Dr. To Amit' Capital A/c (Adjustment for goodwill on change in profit sharing ratio)		6,000	 6,000

Accounting treatment of Reserves and Accumulated Profits:

Case (i) When reserves and accumulated profits/losses are to be distributed

At the time of change in profit sharing ratio, if there are some reserves or accumulated profits/losses existing in the books of the firm, these should be distributed to partners in their old profit sharing ratio.

Illustration 2 : Vaishali, Vinod and Anjali are partners sharing profits in the ratio of 4:3:2. From April 1,2011, they decided to share the profits equally. On that date their books showed a credit balance of '3,60,000 in the profit and loss account and a balance of ' 90,000 in the General reserve. Record the journal entry for distribution of these profits and reserves.

Solution :

Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
2011	Profit & Loss	Dr.		3,60,000	
Apr. 1	General Reserve A/c	Dr.		90,000	
	To Vaishali's Capital A/c				2,00,000
	To Vinod's Capital A/c				1,50,000
	To Anjali's Capital A/c				1,00,000
	(Profit and general reserve distributed in old ratio)				

Illustration 3 : Anjum and Kanchan are partners sharing profits and losses in the ration of 3:2, From April 1, 2011 they decided to share the profits in the ratio of 2:1. On that date, profit and loss account showed a debit balance of ₹ 1,20,000. Record the Journal for transferring this to partner's capital accounts.

Solution :

Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
2011	Anjum's capital A/c	Dr.		72,000	
Apr. 1	Kanchan's capital A/c	Dr.		48,000	
	To Profit and Loss A/c				1,20,000
	(Undistributed losses transferred to partners' capital accounts in old ratio)				

Case (ii) When accumulated profits/losses are not be distributed at the time of change in ratio

Partners may decide that reserves and accumulated profits/losses will not be affected and remains in the books with same figure. In this case, the gaining partner must compensate the sacrificing partner by the share gained by him i.e.

Gaining Partner's Capital A/c Dr.

To Sacrificing Partner's Capital A/c.

Illustration 4: Keshav, Meenakshi and Mohit sharing profit and losses in the ratio of 1:2:2,decide to share future profit equally with effect from April 1, 2011. On that date general reserve showed a balance of ₹ 2,40,000. Partners do not want to distribute the reserves. You are required to give the adjusting entry.

Solution: Keshav : Meenakshi : Mohit

Old ratio 1/5 : 2/5 : 2/5

New ratio 1/3 : 1/3 : 1/3

Sacrifice or Gain:

Keshav = 1/5 – 1/3 = 3-5/15 = 2/15 (Gain)

Meenakshi = 2/5 – 1/3 = 6-5/15 = 1/15 (Sacrifice)

Mohit = 2/5 – 1/3 = 6-5/15 = 1/15 (Sacrifice)

Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
2011	Keshav's capital A/c	Dr.		32,000	
Apr. 1	To Meenakshi's capital A/c				16,000
	To Mohit's capital A/c				16,000
	(Adjustment for General reserve on change in profit sharing ratio				

Illustration 5: Neha, Niharika, and Nitin are partners sharing profits and losses in the ratio of 2:3:4. They decided to change their ratio and their new ratio is 4:3:2. They also decided to pass a single journal entry to adjust the following without affecting their book values:

	₹
Profit & Loss account	80,000
General Reserve	40,000
Advertisement Suspense A/c	30,000

You are required to give the single journal entry to adjust the above.

Solution:

Profit & Loss account	80,000
Add: General Reserve	40,000
	1,20,000
Less: Advertisement Suspense	30,000
Total amount to be adjusted	90,000

	Neha	Niharika	Nitn
Old ratio	2/9	3/9	4/9
New ration	4/9	3/9	2/9

Sacrifice or Gain :

Neha = 2/9-4/9=-2/9 (Gain)
Niharika = 3/9-3/9=0 (No change)
Nitin = 4/9-2/9=2/9 (Sacrifice)

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Date	Particulars	L.F.	Debit ₹	Credit ₹
	Neha's capital A/c Dr.		20,000	
	To Nitin's capital A/c			20,000
	(adjustment for profit & loss A/c, General reserves and advertisment Suspense A/c			

Accounting treatment for Revaluation of Assets and reassessment of Liabilities on change in Profit sharing ratio:

At the time of change in profit sharing ratio of existing partners, Assets and liabilities of a firm must be revalued because actual realizable value of assets and liabilities may be different from their book values. Change in the assets and liabilities belongs to the period prior to change in profit sharing ratio and therefore it must be shared in old profit sharing ratio.

Revaluation of assets and liabilities may be treated in two ways:

(i) When revised values are to be shown in the books.

(ii) When revised values are not to be shown in the books

When revised values are to be shown in the books:

In this case revaluation of assets and liabilities is completed with the help of "Revaluation Account". This account is also known as "Profit and Loss Adjustment Account". All losses due to revaluation are shown in debit side of this account and all gains due to revaluation are shown in credit side of this account.

Note : (1) Increase in the value of an Asset and decrease in the value of a liability result in profit.

(2) Decrease in the value of any asset and Increase in the value of liability gives loss.

Illustration 6:

Piyush, Puja and Praveen are partners sharing profits and losses in the ratio of 3:3:2. There balance sheet as on March 31st 2011 was as follows.

Liabilities		₹	Assets	₹
Sundry creditors		48,000	Cash at bank	74,000
Bank Loan		72,000	Sundry debtors	88,000
Capital :			Stock	2,40,000
Piyush	4,00,000		Machinery	3,18,000
Puja	3,00,000		Building	4,00,000
Praveen	3,00,000	10,00,000		
		11,20,000		11,20,000

Partners decided that with effect from April 1, 2011, they would share profits and losses in the ratio of 4:3:2. It was agreed that:

(i) Stock be valued at ₹ 2,20,000.

(ii) Machinery is to be depreciated at 10%.

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

(iv) Building is to be appreciatd by 20%.

(v) A liability for ₹ 5,000 included in sundry creditors is not likely to arise.

Partners agreed that the revised value are to be recorded in the books. You are required to prepare journal, revaluation account, partners capital account and revised balance sheet.

Journal

Date	Particulars	L.F.	Debit ₹	Credit ₹
2011	Revaluation A/c Dr.		56,200	
	To Stock			20,000
	To Machinery			31,800
	To Provision for doubtful debts A/c			
	(Revaluation of assets)			
	Building A/c		80,000	
	Sundry creditors		5,000	
	To Revaluation A/c			85,000
	(Revaluation of assets and liabilities)			
	Revaluation A/c		28,800	
	To Piyush's capital A/c			10,800
	To Pooja's capital A/c			10,800
	To Praveen's capital A/c			7,200
	(Profit on revaluation)			

Revaluation Account

Particulars		₹	Particulars	₹
To stock		20,000	By building	80,000
To machinery		31,800	By sundry creditors	5,000
To Provision for doubtful debts		4,400		
To profit distributed :				
Piyush	10,800			
Pooja	10,800			
Praveen	7,200			
		28,800		
		85,000		85,000

Partners' Capital Account

Particulars	Piyush	Pooja	Praveen	Particulars	Piyush	Pooja	Praveen
To balance c/d	4,10,800	3,10,800	3,07,200	By balance b/d By reval -uation	4,00,000	3,00,000	3,00,000
					10,800	10,800	7,200
	4,10,800	3,10,800	3,07,200		4,10,800	3,10,800	3,07,200

Balance Sheet
as on April 1, 2011

Liabilities		₹	Assets		₹
Sundry creditors		43,000	Cash at bank		74,000
Bank Loan		72,000	Sundry debtors	88,000	
Capital account :			Less : provision 5%	4,400	83,600
Piyush	4,10,000				
Puja	3,10,800		Stock		2,20,000
Praveen	3,07,200		Machinery		2,86,200
		10,28,800	Building		4,80,000
		11,43,800			11,43,800

When revised values are not to be shown in the books.

Illustration 7.

In illustration 6, Partners agreed that the revised value of assets and liabilities are not to be shown in the books. You are required to record the effect by passing a single journal entry. Also prepare the revised value balance sheet.

Gain due to revaluation		₹
Building		80,000
Sundry creditors		5,000
	Total A	**85,000**
Less: loss due to revaluation		
Stock		20,000
Machinery		31,800
Provision for doubtful debts		4,400
	Total B	**56,200**
Net gain from revaluation	**Total (A-B)**	28,800

Old Ratio = 3:3:2

New Ratio = 4:3:2

Sacrifice or Gain :

Piyush = 3/8-4/9 = -5/72 (Gain)

Pooja = 3/8-3/9 = 3/72 (Sacrifice)

Praveen = 2/8-29 = 2/72 (Sacrifice)

Amount to be adjusted :

Piyush = ₹ 28,800 x 5/72 = ₹ 2,000 Debit

Pooja = ₹ 28,800 x 3/72 = ₹ 1,200 Credit

Praveen = ₹ 28,800 x 2/72 = ₹ 800 Credit

Journal

Date	Particulars		L.F. Rs.	Debit Rs.	Credit
2011	Piyush's capital A/c	Dr.		2,000	
Apr. 1	To Pooja's capital A/c				1,200
	To Praveen's capital A/c				800
	(Adjustment for profit on revaluation)				

Capital Accounts

Particulars	Piyush	Pooja	Praveen	Particulars	Piyush	Pooja	Praveen
To Pooja's Capital A/c	1,200	-	-	By Balance b/d	4,00,000	3,00,000	3,00,000
To Praveen Capital A/c	800	-	-	By Piyush's Capital A/c	-	1,200	800
To Balance C/d	3,98,000	3,01,200	3,00,800				
	4,00,000	3,01,200	3,00,800		4,00,000	3,01,200	3,00,800

Balance Sheet
as on April 1, 2011

Liabilities		₹	Assets	₹
Sundry Creditors		48,000	Cash at bank	74,000
Bank Loan		72,000	Sundry debtors	88,000
Capital account :			Stock	2,40,000
Piyush	3,98,000		Machinery	3,18,000
Puja	3,01,200		Building	4,00,000
Praveen	3,00,800			
		10,00,000		
		11,20,000		11,20,000

CHAPTER 4

Accounting for Partnership Firms : Admission of a partner

Meaning:

When a new partner is admitted in a running business due to the requirement of more capital or may be to take advantage of the experience and competence of the newly admitted partner or any other reason, it is called admission of a partner in partnership firm.

According to section 31(1) of Indian partnership Act,1932, "**A new partner can be admitted only with the consent of all the existing partners.**"

At the time of admission of a new partner, following adjustments are required:

1. Calculation of new profit sharing ratio and sacrificing ratio.
2. Accounting treatment of Goodwill.
3. Accounting treatment of accumulated profit.
4. Accounting treatment of revaluation of assets and reassessment of liabilities.
5. Adjustment of capital in new profit sharing ratio.

1. Calculation of new profit sharing ratio.

Following types of problems may arise for the calculation of new profit sharing ratio.

Case (i) **When old ratio is given and share of new partner is given.**

Illustration 1. (When new partner acquires his share from all partners in their old ratio)

A and B are partners in a firm sharing profits and losses in the ratio 1:2.They admitted C into the partnership and

decided to give him 1/3rd share of the future profits. Find the new ratio of the partners. *(CBSE 2003)*

Solution

(i) Calculation of Sacrifice Share:

A's sacrifice = 1/3 of 1/3 = 1/9

B's sacrifice = 2/3 of 1/3 = 2/9

Sacrificing Ration = 1/9 : 2/9 = 1:2

which is equal to old ratio

(ii) Calculation of New Profit sharing Ratio:

New share=Old share- Sacrifice share

A's new share =1/3-1/9=3-1/9=2/9

B's new share =2/3-2/9=6-2/9=4/9

C's new share =1/9+ 2/9 = 3/9

New ratio among A,B and C: 2/9:4/9:3/9=2:4:3 respectively

Note: Unless agreed otherwise, it is presumed that the new partner acquires his share in profits from the old partners in their old profit sharing ratio.

Alternative Method :

Old Ratio = A:B

1:2

Let the profit of the firm = 1

C's share (New Partner) = 1/3

Remaining Profit = 1-1/3 = 2/3

Now this profit 2/3 will be divided between the old partners in their old ratio i.e., 1:2

A's new Profit = 1/3 of 2/3 = 1/3 x2/3 = 2/9

B's new Profit = 2/3 of 2/3 = 2/3x2/3 = 4/9

C's profit = 1/3 or 1/3 x 3/3 = 3/9

Hence the new ratio = 2:4:3

Note- In this case only New Partner's share is given then Sacrificing Ratio = Old Ratio = 1:2 There is no need to calculate it

Case (ii) When new partner acquires his/her share from all partners in agreed share.

Illustration 2. (When new partner acquires his share from all partners in agreed share)

L and M are partners in a firm sharing profits and losses in the ratio of 7: 3. They admitted N for 3/7th share,which he takes 2/7th from L and 1/7 from M. Calculate the new profit sharing ratio.*(CBSE 1999 Compt., 2001, 2003)*

Solution.

(i) As sacrifice share of old partners are given in the question itself, hence there is no need to calculate it.

(ii) Calculation of New profit sharing ratio:

New share=old share-sacrifice share

L's new share =7/10-2/7=49-20/70=29/70

M's new share =3/10-1/7=21-10/70=11/70

N's new share =2/7+1/7=3/7(given)

New ratio among L,M and N =29/70:11/70:3/7 = 29:11:30/70 =29:11:30

Case (iii) When new partner acquires his/her share from all partners in certain ratio.

Illustration 3.

X and Y are partners in a firm sharing profit and losses in the ratio of 3:2.Z is admitted as partner in the firm for 1/6th share in profits. Z acquires his share from X and Y in the ratio of 2:1. Calculate new profit sharing ratio of partners.

(CBSE 2003)

Solution.

(i) Calculation of Sacrifice share:

Given sacrificing Ratio = X:Y = 2:1,

therefore :

X's sacrifice = 2/3of 1/6=2/18

Y's sacrifice =1/3of 1/6 =1/18

(ii) Calculation of New Profit Sharing Ratio:

New share = Old share-Sacrifice share

X's new share =3/5-2/8=54-10/90=44/90

Y's new share =2/5-1/18=36-5/90=31/90

Z's new share =2/18+1/18=3/18or 1/6 (Given)

New ratio among X,Y and Z = 44/90:31/90:1/6=44:31:15/90=44:31:15

Case (iv) When new partner acquires his share from all partners as a fraction of their share.

Illustration 4. (When new partner acquires his share from all partners as a fraction of their share)

A and B are partners in a firm sharing profit and losses in the ratio of 5:3. A surrenders 1/5th of his share, whereas B surrenders 1/3 of his share in favour of C, a new partner. Calculate the new profit sharing ratio

.(CBSE 2003, AI 2004)

Solution.

(i) Calculation of sacrifice share

A sacrifices 1/5th of his share i.e., 1/5of 5/8 = 5/40 or 1/8

B sacrifices 1/3th of his share i.e.,1/3of3/8= 3/24 or 1/8

(ii) Calculation of New profit shaing Ratio :

New share =Old share – sacrifice share

A's new share =5/8-1/8=4/8

B's new share = 3/8 -1/8 = 2/8

C's new share = 1/8 + 1/8 = 2/8

New ratio among A, B and C = 4/8:2/8:2/8 = 4:2:2/8 = 2:1:1

Case (v) When new partner does not acquire his/her share from all partners

Illustration 5. (when new partner does not acquire his share from all partners)

A, B and C are partners sharing profits in the ratio of 3:2:1. They admit D for 1/6 share. C would retain his old share. Calculate new ratio of all partners.

(CBSE 2002 Compt.)

Solution.

(i) Calculation of sacrifice share : (Only A and B will sacrifice in ratio of 3:2)

A's sacrifice = 3/5 of 1/6 = 3/30 or 1/10

B's sacrifice = 2/5 of 1/6 = 2/30 or 1/15

C's sacrifice = 0

(ii) Calculation of new profit sharing ratio :

New share = Old share – Sacrifice share

A's new share = 3/6 – 1/10 = 30-6/60 = 24/60

B's new share = 2/6 – 1/15 = 30-6/90 = 24/90

C's new share = 1/6 – 0 = 1/6

D's new share = 1/10 + 1/15 = 3+2/30 = 5/30 = 1/6

New ratio among A, B, C and D

24/60:24/90:1/6:1/6 = 72:48:30:30/180 = 12:8:5:5

Case (vi) When more than one partner is admitted.

Illustration 6. (when more than one partner is admitted simultaneously)

X and Y are partners sharing profits in the ratio of 3:2. They admit P and Q as new partners. X surrendered 1/3 of his share in favour of P and Y surrendered ¼ of his share in favour of Q. Calculate the new profit sharing ratio of X, Y, P and Q.

(CBSE 2002 Compt.)

Solution.

(i) Calculation of sacrifice share : (only A and B will sacrifice in the ratio 3:2)
X surrenders 1/3 of his share in favour of P = 1/3 of 5/3 = 3/15 or 1/5
Y surrenders 1/4 of his share in favour of Q = 1/4 of 2/5 = 2/20 or 1/10

2. **Accounting Treatment of Goodwill.**

At the time of admission of a partner, treatment of Goodwill is necessary to compensate the old partners for their sacrifice. The incoming partner must compensate the existing partners because he is going to acquire the right to share future profits and this share is sacrificed by old partners. If goodwill (Premium) is paid to old partners privately or outside the business by the new partner then no entry is required in the books of the firm.

There may be different situations about the treatment of goodwill at the time of the admission of the new partner :

(i) Goodwill (premium) brought in by the new partner in cash and retained in the business

Illustration 7. (All partners sacrifice)

A and B are partners sharing profits and losses in the ratio of 3:2. They admit C into partnership for ¼ share in profits. C brings ' 3,00,000 as capital and ' 1,00,000 as goodwill. New profit sharing ratio of the partners shall be 3:3:2. Pass necessary Journal entries.*(CBSE 2003)*

Journal

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Bank A/c Dr.		4,40,000	
	To Premium for Goodwill A/c			1,00,000
	To C's Capital A/c			3,00,000
	(Being the amount of goodwill and capital brought in by new partner C)			
	Premium for Goodwill A/c Dr.		1,00,000	
	To A's capital A/c			90,000
	To B's capital A/c			10,000
	(Being the amount of goodwill distributed between A and B in their sacrificing ratio i.e., 9:1)			

Note : Sacrificing ratio = Old ration - New ratio
A= 3/5-3/8 = 24-15/40 = 9/40
B = 2/5-3/8 = 16-15/40 = 1/40

This sacrificing ratio between A and B i.e., 9:1.

Illustration 8. (Sacrificing ratio is to be calculated)

A and B are partners in a firm sharing profits and losses in the ratio of 3:2 A new partner C is admitted. A surrenders 1/5 of his share and B 2/5 of his share in favour of C. For purpose of C's admission, goodwill of the firm is valued at ' 75,000 and C brings his share ofgoodwill in cash which is retained in the firm's books. Journalise the above transactions.

(CBSE 2003)

Journal

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Bank A/c Dr.		21,000	
	To Premium for Goodwill A/c			21,000
	(Being the amount of goodwill and capital brought in by new partner C)			
	Premium for Goodwill A/c Dr.		21,000	
	To A's capital A/c			9,000
	To B's capital A/c			12,000
	(Being the amount of goodwill distributed between A and B in their sacrificing ratio i.e., 3:4)			

Note :(i) Calculation of sacrificing ratio :

A's sacrifice, 1/5 of his share = 1/5 of 3/5 = 3/25

B's sacrifice, 2/5 of his share = 2/5 of 2/5 = 4/25

Sacrificing ratio between A and B i.e., 3/25:4/25 = 3:4

(ii) Calculation of C's share of profit :

C's share of profit = 3/25+4/25 = 7/25

(iii) Calculation of C's share of goodwill :

75,000 x 7/25 = 21,000

Treatment of Existing Goodwill shown in the books

If goodwill already shown in the balance sheet, it should be written off by debiting old partners in their old profit sharing ratio.

Illustration 9. (Existing goodwill to be written off)

A and B are partners in a firm sharing profits and losses in the ratio of 3:2. They admit C into partnership for 1/5 share. C brings ₹30,000 as capital and ₹10,000 as goodwill. At the time of admission of C, goodwill appears in the balance sheet of A and B at ₹ 3,000. New profit sharing ratio of partners shall be 5:3:2. Pass necessary entries.

(CBSE 2003)

Journal

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank A/c Dr.		40,000	
	To Premium for Goodwill A/c			30,000
	To C's Capital A/c			10,000
	(Being the amount of goodwill and capital brought in by new partner C)			
	Premium for Goodwill A/c Dr.		10,000	
	To A's capital A/c			5,000
	To B's capital A/c			5,000
	(Being the amount of goodwill distributed between A and B in their sacrificing ratio i.e., 1:1)			
	A's capital A/c Dr.			
	B's capital A/c Dr.			
	To Goodwill A/c		1,800	
	(Being existing goodwill written off between		1,200	
	old partners in their old ratio i.e., 3:2)			3,000

Notes : Sacrificing ratio = Old ratio – New ratio

A = 3/5 – 5/10 = 6-5/10 = 1/10

B = 2/5 – 3/10 = 4-3/10 = 1/10

Sacrificing ratio between A and B 1:1 i.e., equal.

Case (ii) Premiumbrought in kind:

Illustration 10. (premium brought in kind)

Anubhav and Babita are partners in a firm sharing profits and losses in the ratio of 3:2. On April 1,2003 they admit

Deepak as a new partner for 3/13 share in the profits. Deepak contributed the following assets towards his capital

and for his share of goodwill :

Land ₹ 90,000, machinery ₹ 70,000, stock ₹ 60,000 and debtors ₹ 40,000. On the date of admission of Deepak, the goodwill of the firm was valued at ₹5,20,000, which is not appear in the books. Record necessaries journal entries in the books of the firm. Show your calculations clearly.

(NCERT, CBSE 2004 Compl)

Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Land A/c	Dr.		90,000	
	Machinery A/c	Dr.		70,000	
	Stock A/c	Dr.		40,000	
	Debtors A/c	Dr.		60,000	
	To Premium for Goodwill A/c(5,20,000x3/13)				1,20,000
	To Deepak's Capital A/c (Balancing figure)				1,40,000
	(Being the amount of goodwill and capital brought in kind by new partner)				
	Premium for Goodwill A/c	Dr.		1,20,000	
	To Anubhav's capital A/c				72,000
	To Babita's capital A/c				48,000
	(Being the amount of goodwill distributed between Anubhav and Babita in their sacrificing ratio i.e. 3:2)				

Note : Here Sacrificing Ratio = Old Ratio i.e., 3:2

Case (iii) Amount of goodwill which was brought in by new partner, is withdrawn by old partners:

In this case one additional Journal entry may be passed :

Old Partners' Capital A/c Dr.

To Bank/Cash A/c

(Cash withdrawn by old partners)

Case (iv) when the new partner is unable to bring his share of goodwill in cash

Sometimes the new partner does not bring his share of goodwill in cash. Then his share of goodwill is calculated and adjusted by the following Journal entry.

Now Partners' Capital A/c Dr.
To old partners Capital A/cs
(in the sacrificing ratio).

Illustration 11 :

Neeta and Sumita are partners sharing profits and losses in the sates 2:1. They admit Geeta as a partner for 1/4th Share. Geeta pays Rs.50,000 as capital but does not bring any amount for goodwill. The goodwill of the new firm is valued at ₹36,000. Give Journal entries.

(CBSE 1997, 2003)

Solution

Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
1.	Cash A/c	Dr.		50,000	
	To Geeta's Capital A/c				50,000
	Being the amount of Capital brought in cash by the new partner)				
2.	Geeta's Capital A/c	Dr.		9,000	
	To Neeta's Capital A/c				6,000
	To Sunita's Capital A/c				3,000
	Being the amount of new Partner's share of goodwill transferred to old Partner's Capital A/c in their sacrificing ratio i.e.2:1)				

Working Note :

(1) As nothing is given about sacrifice etc. except the old ratio and the new partners share of profit

Sacrificing Ratio = Old Ratio = 2:1

(2) Goodwill of the firm = Rs.36,000

Geeta's share of profit = 1/4

Geeta's share of Goodwill = Rs.36,000x1/4 = Rs.9,000

Case (v) Partly goodwill brought in by new partner :

Illustration 12. (Partly premium brought in cash)

Sheetal and Raman share profits equally. They admit Chinki into partnership. Chinki pays only ‘ 1,000 for premium out of his share of premium of ‘ 1,800 for 1/4 share of profit. Goodwill Account appears in the books at ‘ 6,000. All partners have decided that goodwill should not appear in the books of the new firm. Journalise.

(CBSE 1997, 2003)

Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Bank A/c	Dr.		1,000	
	To Premium for Goodwill A/c				1,000
	(Being the amount of goodwill brought in cash by new partner)				
	Premium for Goodwill A/c	Dr.		1,000	
	Chinki's capital A/c	Dr.		800	
	To Sheetal's capital A/c				900
	To Raman's capital A/c				900
	(Being Chinki's share of goodwill transferred to sacrificing partners in their sacrificing ratio i.e., 1:1)				
	Sheetal's capital A/c	Dr.		3,000	
	Raman's capital A/c	Dr.		3,000	
	To Goodwill A/c				6,000
	(Being existing goodwill written off between old partners in their old ration i.e., equal)				

Case (vi) Gain made by an old partner :

Illustration 13. (Sacrifice/Gain made by a partner)

Ashok and Ravi were partners in a firm sharing profits and losses in the ratio of 7:3. They admitted Chander as a new partner. The new profit ratio between Ashok,Ravi and Chander will be 2:2:1. Chander brought ‘ 24,000 for his share of his goodwill. Pass necessary journal entries for the treatment of goodwill.

(CBSE 2000)

Solution :

Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Bank A/c	Dr.		24,000	
	To Premium for Goodwill A/c				24,000
	(Being the amount of goodwill brought in by new partner)				
	Premium for Goodwill A/c	Dr.		24,000	
	Ravi's capital A/c	Dr.		12,000	
	To Ashok's capital A/c				36,000
	(Being the goodwill credited to Ashok's capital A/c)				

Note : Calculation of sacrifice/gain share of partners(s) :

Sacrificing ration = Old ratio-New ratio

Ashok = 7/10 – 2/5 = 7-4/10 = 3/10 sacrifice

Ravi = 3/10 – 2/5 = 3-4/10 = (-1/10) gain

Being negative result, it shows gain. Since Ravi is gaining equal to 1/10 in the profits, therefore, he will also compensate Ashok proportionately. For 1/5 share Chander brought ₹ 24,000, therefore, Ravi will compensate Ashok by ₹ 12,000 i.e., 24,000 x 5/1 x 1/10.

Case (vii) Hidden Goodwill

Illustration 14.

A and B are partners with capitals of ₹ 26,000 and ₹ 22,000 respectively. They admit C as partner with 1/4th share in the profits of the firm. C brings ₹ 26,000 as his share of capital. Give journal entry to record goodwill on C's admission.

(CBSE 2001 Compt.)

Journal

Date	**Particulars**	**L.F.**	**Debit ₹**	**Credit ₹**
	Bank A/c Dr.		26,000	
	To C's capital A/c			26,000
	(Being the amount of goodwill brought in by new partner)			
	C's capital A/c Dr.		7,500	
	To A's capital A/c			3,750
	To B's capital A/c			3,750
	(Being the goodwill credited to sacrificing partners' capital a/cs in their sacrificing ratio i.e., equal)			

Notes :(1) Calculation of C's share of goodwill :

Total capital of new firm on basis of C's capital i.e., 26,000 x 4/1	1,04,000
Total capital of A and B and C i.e., ₹26,000 + ₹ 22,000 + ₹ 26,000	(74,000)
Goodwill of the firm	30,000
Thus C's share of goodwill = 30,000 x 1/4 =	₹ 7,500

(2) In the absence of information, profits will be shared equally.

3. Accounting treatment of Accumulated Profits.

Accumulated profits and reserves are distributed to partners in their old profit sharing ratio.

If old partners are not interested to distribute, these accumulated profits are adjusted in the same manner

as goodwill and the following adjusting entry will be passed.

New Partner's capital A/c Dr. (New share)

To old partners' capital A/c (Sacrificing ratio)

4. Accounting treatment for revaluation of assets and re -assessment of liabilities :

The assets and liabilities are generally revalued at the time of admission of a new partner. Revaluation Account is prepared for this purpose in the same way as in case of change in profit sharing ratio. This account is debited with all losses and credited with all gains. Balance of Revaluation Account is transferred to old partners in their old ratio.

Illustration 15.

Following is the Balance Sheet of Shashi and Ashu sharing profit as 3:2.

Liabilities	₹	Assets		₹
Creditors	18,000	Debtors	22,000	
General reserve	25,000	Less provision for		
		D. D.	1,000	21,000
Workmens compensation fund	15,000	Land and Building		18,000
Capital : Shashi	15,000	Plant and machinery		12,000
Ashu	10,000	Stock		11,000
		Bank		21,000
	83,000			83,000

On admission of Tanya for 1/6th share in the profit it was decided that:

(i) Provision for doubtful debts to be increased by ₹ 1,500.

(ii) Value of land and building to be increased to ₹ 21,000.

(iii) Value of stock to be increased by ₹ 2,500.

(iv) The liability of workmen's compensation fund was determined to be ₹ 12,000.

(v) Tanya brought in as her share of goodwill ₹ 10,000 in cash.

(vi) Tanya was to bring further cash of ₹ 15,000 for her capital.

Prepare Revaluation A/c, Capital A/c and the Balance Sheet of the new firm. ***(CBSE 2001)***

Solution :

Revaluation Account

Particulars	₹	Particulars	₹
To Provision for D. D.	1,500	By Land and Building A/c	3,000
To Capital A/cs :		By Stock	2,500
Shashi 3/5 2,400			
Ashu 2/5 1,600	4,000		
	5,500		5,500

Partners' Capital Account

Particulars	Sashi	Ashu	Tanya	Particulars	Shashi	Ashu	Tanya
To balance c/d	40,200	26,800	15,000	By balance b/d	15,000	10,000	–
				By general reserve	15,000	10,000	–
				By workmen's compensation A/c	1,800	1,200	–
				By Revaluation A/c	2,400	1,600	–
				By Bank A/c	–	–	15,000
				By Premium for goodwill	6,000	4,000	–
	40,200	26,800	15,000		40,200	26,800	15,000

Balance Sheet of the New Firm

Liabilities		₹	Assets		₹
Creditors		18,000	Debtors	22,000	
Workmen compensation fund		12,000	Less provision for D. D.	2,500	19,500
Capital :	Shashi	40,200	Land and Building		21,000
	Ashu	26,800	Plant and machinery		12,000
	Tanya	15,000	Stock		13,500
			Bank		46,000
		1,12,000			1,12,000

Illustration 16. : A, B and are partners sharing profits and losses in the ratio of 2:3:5. On 31st March 2001, their Balance Sheet was as follows

Liabilities			₹	Assets	₹
Capital				Cash	18,000
	A	36,000		Bills receivable	24,000
	B	44,000		Furniture	28,000
	C	52,000	1,32,000	Stock	44,000
Creditors			64,000	Debtors	42,000
Bill Payable			32,000	Investments	32,000
Profit and Loss Account			14,000	Machinery	34,000
				Goodwill	20,000
			2,42,000		2,42,000

They admit D into partnership on the following terms:

(i) Furniture and Machinery to be depreciated by 15%.

(ii) Stock is revaluated at ₹ 48,000.

(iii) Goodwill to be valued at ₹ 24,000.

(iv) Outstanding rent amount to ₹ 1,800.

(v) Prepaid salaries ₹ 800.

(vi) D to bring ₹ 32,000. Towards his capital for 1/6th share.

Prepare Revaluation Account, Partners Capital Accounts and Balance Sheet of the new firm

(CBSE 2001)

Solution :

Revaluation Account

Particulars	₹	Particulars		₹
To furniture A/c	4,200	By Stock A/c		4,000
To Machinery A/c	5,100	By Prepaid salaries A/c		800
To Outstanding rent A/c	1,800	By Capital A/c (loss) :		
		A 2/10	1,260	
		B 3/10	1,890	
		C 5/10	3,150	6,300
	11,100			11,100

Partners' Capital Account

Particulars	A (₹)	B (₹)	C (₹)	D (₹)	Particulars	A (₹)	B (₹)	C (₹)	D (₹)
To Revaluation A/c	1,260	1,890	3,150	–	By balance c/d	36,000	44,000	52,000	–
ToGoodwill A/c	4,000	6,000	10,000	–	By P/L A/c	2,800	4,200	7,000	–
To A's capital	–	–	–	8,00	By D's	–	–	–	
To B's capital	–	–	–	1,000	capital	8,000	1,200	2,000	–
To C's capital	–	–	–	2,000					
To Balance C/d	34,340	41,510	47,850	28,000	ByCashA/c				32,000
	39,600	49,400	61,000	32,000		39,600	49,900	61,000	32,000

Balance Sheet of New Firm

Liabilities			₹	Assets	₹
Capital :				Cash	50,000
	A	34,340		Bill Receivable	24,000
	B	41,510		Furniture	23,800
	C	47,850		Stock	48,000
	D	28,000	1,51,700	Debtors	42,000
Creditors			64,000	Investment	32,000
Bills Payable			32,000	Machinery	28,900
Outstanding rent			1,800	Prepaid salaries	800
			2,49,500		2,49,500

5. Adjustment of capital in new profit sharing ratio

Illustration 17 A, B and C are partners sharing profits and losses in the ratio of 5:3:2 On March 31st, 1998 their Balance Sheet was as follows :

Liabilities			₹	Assets	₹
Capital :				Cash	18,000
	A	36,000		Bill receivable	14,000
	B	44,000		Stock	44,000
	C	52,000	1,32,000	Debtors	42,000
Creditors			64,000	Machinery	94,000
Bills Payable			32,000	Goodwill	20,000
General Reserve			14,000		
			2,32,000		2,32,000

They decided to admit D into the partnership on the following terms:

(i) Machinery is to be depreciated by 15 %.

(ii) Stock is to be revalued at ₹ 48,000.

(iii) A, B and C have a joint life policy whose surrender value is ₹ 12,000.

(iv) Outstanding rent is ₹ 1,900.

(v) D is to bring ₹ 6,000 as goodwill and sufficient capital for a 2/5th share in the capitals of firm.

Prepare Revaluation A/c, Partner's Capital A/c, Cash A/c and Balance Sheet of the new firm.

(CBSE 2001 Compt.)

Revaluation Account

Particulars	₹	Particulars		₹
To Machinery A/c	14,100	By Stock A/c		4,000
To Outstanding Rent	1,900	By Capital A/c (Loss) :		
		A 5/10	6,000	
		B 3/10	3,600	
		C 2/10	2,400	12,000
	16,000			16,000

Partners' Capital Account

Particulars	A (₹)	B (₹)	C (₹)	D (₹)	Particulars	A (₹)	B (₹)	C (₹)	D (₹)
To Goodwill A/c	10,000	6,000	4,000	–	By Balance b/d	36,000	44,000	52,000	–
ToRevaluation	6,000	3,600	2,400	–	By General reserve	7,000	4,200	2,800	–
A/c	36,000	44,000	52,000	–	By Joint life policy	6,000	3,600	2,400	–
To Balance c/d					By Premium				
	52,000	53,600	58,400	–	for goodwill	3,000	1,800	1,200	–
	36,000	44,000	52,000	88,000	By Balance	36,000	44,000	52,000	–
To Balance c/d					b/d	–	–	–	–
	36,000	44,000	52,000	88,000	By cash A/c	36,000	44,000	52,000	88,000

Note : Combined capital of A, B and C for 3/5 (1-2/5) = 1,32,000

Thus total capital of the firm = 1,32,000x5/3 = ₹ 2,20,000

D's share of capital = 2,20,000x2/5 = ₹ 88,000

Balance Sheet of the New Firm

Liabilities		₹	Assets	₹
Creditors		64,000	Cash	1,12,000
Bill Payable		22,000	Bills receivable	14,000
Outstanding rent		1,900	Stock	48,000
Capital			Debtors	42,000
A	36,000		Machinery	79,000
B	44,000		Joint Life Policy	12,000
C	52,000			
D	88,000	2,20,000		
		3,07,900		3,07,900

Illustration 18 : Following is the Balance Sheet of A, B and C sharing profits and losses in the ratio of 6:5:3 respectively

Liabilities	₹	Assets	₹
Creditors	37,800	Cash	3,780
Bill Payable	12,600	Debtors	52,920
General reserve	21,000	Stock	58,800
A's capital	70,800	Furniture	14,700
B's capital	59,700	Land and Building	90,300
C's capital	29,100	Goodwill	10,500
	2,31,000		2,31,000

They agreed to take into partnership giving 1/0th share in profits on the following terms :

(a) Furniture to be depreciated by ₹ 1,840 Stock by 10%

(b) A provision of ₹ 2,640 to be made for an outstanding bill for repairs.

(c) That land and building be brought up to ₹ 1,19,700.

(d) That the goodwill is valued at ₹ 28,140.

(e) That D should bring in ₹ 35,400 as his capital

(f) After making the above adjustments the capital of old partners be adjusted in proportion to D's Capital by bringing in cash or excess to be paid off.

D's Capital by bringing in cash or excess to be paid off.

Prepare Revaluation Account, Capital Account of Partners and balance Sheet of new firm.

(CBSE 1997 Compt.)

Solution :

Revaluation Account

Particulars			₹	Particulars	₹
To furniture A/c			1,840	By Land and Building A/c	29,400
To stock A/c			5,880		
To O/S repairs A/c			2,640		
To capital A/cs :					
A	6/14	8,160			
B	5/14	6,800			
C	3/14	4,080	19,040		
			29,400		29,400

Partners' Capital Account

Particulars	A (₹)	B (₹)	C (₹)	D (₹)	Particulars	A (₹)	B (₹)	C (₹)	D (₹)
To Goodwill	4,500	3,750	2,250	–	By Balance b/d	70,800	59,700	29,100	–
To A's capital	–	–	–	1,508	By General	9,000	7,500	4,500	–
To B's capital	–	–	–	1,256	reserve	8,160	6,800	4,080	–
To C's capital	–	–	–	754	By rev-	–	–	–	35,400
To Balance c/d	84,968	71,506	38,184	31,882	-aluation A/c	1,508	1,256	754	–
	89,468	75,256	38,434	35,400	By cash A/c	89,468	75,256	38,434	35,400
To balance c/d	95,646	79,705	47,823	31,882	By D's Capital				
					By balance b/d	84,968	71,506	36,184	31,382
					By cash A/c	10,678	8,199	11,639	–
	95,646	79,705	47,823	31,882		95,646	79,705	47,823	31,882

Balance Sheet of the New Firm

Liabilities			₹	Assets	₹
Creditors			37,800	Cash	69,696
Bills Payable			12,600	Debtors	52,920
Outstanding repairs			2,640	Stock	12,860
Capital				Furniture	12,860
	A	95,646			
	B	79,705			
	C	47,823			

D 31,882			
	2,55,056		3,08,096
	3,08,096		3,08,096

Notes : Calculation of New Profit Sharing Ratio :

1. Share given to D=1/8, Balance of profit = 1-1/8=7/8. Hence,

   A's Share = 7/8x6/14=42/112

   B's Share = 7/8x5/14 = 35/112

   C's Share = 7/8x3/14 = 21/112

   A B C D

   New Ratio : 42/112 : 35/112 : 21/112 : 1/8 = 42 : 35 : 21 : 14/112 or 6 : 5 : 3 : 2.

2. Calculation of new capital of A, B, and C based on D's Capital for 1/8 share is ₹ 31,882. Thus

   Capital of whole firm = 31,882 x 8/1 = ₹ 2,55,056. Therefore

   A's Capital = 2,55,056x6/16= 95,646

   B's Capital = 2,55,056x5/16 = 79,705

   C's Capital = 2,55,056 x 3/16 = 47,823

Illustration 19 : A and B are parents in a firm sharing profits and losses in the ratio of 3:2. Their balance sheet was as follows on 1st January, 1993 :

Liabilities		₹	Assets	₹
Sundry creditors		15,000	Plant	30,000
Capital			Patents	10,000
A	30,000		Stock	20,000
B	25,000	55,000	Debtors	18,000
General reserve		10,000	Bank	2,000
		80,000		80,000

C is admitted as a partner on the above date on the following terms :

(i) He will pay ₹ 10,000 as goodwill for one-fourth share in the profit of the firm.

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

Plant at 32,000; Stock at ₹ 18,000; Debtors at book figure less a provision of 5 percet for bad debts.

(iii) It was found that the creditors included a sum of ₹ 1,400 which was not to be paid. But it was also found that there was a liability for compensation to workers amountint to ₹ 2,000.

(iv) C was to introduce ₹ 20,000 as capital and the capitals of other partners were to be adjusted in the new profit sharing ratio For this Purpose, current accounts were to be opened.

Give Revaluation Account, Capital Account and Balance Sheet after C's admission.

(CBSE 1994)

Solution :

Dr. **Revaluation Account** **Cr.**

Particulars	₹	Particulars	₹
To stock A/c	2,000	By plant A/c	2,000
To provision for D. D. A/c	900	By creditors A/c	1,400
To outstanding liability A/c	2,000	By capital A/c (loss) :	
		A 3/5 900	
		B 2/5 600	1,500
	4,900		4,900

Dr. **Partner's Capital Accounts** **Cr.**

Particulars	A	B	C	Particulars	A	B	C
To Revaluation A/c	900	600	–	By Balance b/d	30,000	25,000	–
To Balance c/d	41,100	32,400	20,000	By General Reserve	6,000	4,000	–
				By Bank A/c	–	–	20,000
				By Premium	6,000	4,000	–
	42,000	33,000	20,000		42,000	33,000	20,000
To Current A/c	5,100	8,400	–				
To Balance c/d	36,000	24,000	20,000	By balance b/d	41,100	32,400	20,000
	41,100	32,400	20,000		41,100	32,400	20,000

Dr. **Partner's Current Account** **Cr.**

Particulars	A (₹)	B (₹)	C (₹)	Particulars	A (₹)	B (₹)	C (₹)
To balance c/d	5,100	8,400	–	By capital A/cs	5,100	8,400	–

Balance Sheet (after C's admission)

Liabilities		₹	Assets	₹
Sundry Creditors		13,600	Plant	32,000
Outstanding liability		2,000	Patents	10,000
Capital A/cs :			Stock	18,000
A	36,000		Debtors 18,000	
B	24,000		Less : provision for D. D. (900)	17,100
C	20,000	80,000	Bank	32,000
Current A/cs :				
A	5,100			
B	8,400	13,500		
		1,09,100		1,09,100

Notes : (1) Calculation of new profit sharing ration :

Share given to C=1/4; Balance of Profit = 1-1/4 = 3/4

A' share = 3/4x3/5 = 9/20 A : B : C

B' share = 3/4x2/5= 6/20 9/20 : 6/20 : 1/4

C's share (given) = 1/4 or 9:6:5/20 = 9:6:5

(2) New capital of A and B : Based on C's capital, the total capital of the firm will work out i.e.,

C's capital for 1/4th share = 20,000

Thus the capital of whole firm = 20,000x4/1 = ₹ 80,000

Therefore, based on their new profit new profit sharing ratio, the capital of A and B will be.

A's share of capital = 80,000 x 9/20 = ₹ 36,000

B's share of capital = 80,000 x 6/20 = ₹ 24,000

CHAPTER 5

Retirement/Death of a Partner

Introduction - Like admission and change in profit sharing ratio, in case of retirement or death also the existing partnership deed comes to an end and the new one comes into existence among the remaining partners. There is not much difference in the accounting treatment at the time of retirement or in the event of death.

<u>Amount due to retiring deceased Partner</u>

(To be credited to his capital account)

1. Credit Balance of his capital.
2. Credit Balance of his current account (if any)
3. Share of Goodwill.
4. Share of Reserves or Undistributed profits.
5. His share in the profit revaluation of assets and liabilities.
6. Share in profits upto the date of Retirement/Death.
7. Interest on capital if involved.
8. Salary if any

Deduction from the above sum (to be debited to the capital account)

1. Debit balance of his current account (if any)
2. Share of Goodwill to be written off.
3. Share of Accumulated loss.
4. Drawings and interest on drawings (if any)
5. Share of loss on account of Revaluation of assets and liabilities.
6. His share of business loss.

Accounting Treatement

1. Calculation of new profit sharing ration and gaining ratio
2. Treatment of goodwill.
3. Revaluation a/c preparation with the adjustment in the respect of unrecorded assets/ liabilities.
4. Distribution of reserves and accumulated profits/loss.
5. Ascertainment of share of profits/loss till the date of retirement/death.
6. Adjustment of capital if required
7. Settlement of the Accounts due to Retired/Deceased partner.

New Profit Sharing Ratio & Gaining Ratio

New Profit Sharing Ratio - It is the ratio in which the remaining partners will share further profits after retirement/death.

Gaining ratio - It is the ratio in which the continuing partners have acquired the share from the outgoing partner

Calulation of the two ratios

Following situations may arise.

1. When no information about new ratio or gaining ratio is given in the question

In this case it is considered that the share of the retiring partner is acquired by the remaining partners in the old ratio. Then no need to calculate the new ratio/gaining ratio as it will be the same as before.

Example 1 :- A Band C are partners sharing profit and loss in the ratio of 3:2:1 then on retirement of the gaining ratio/new ratio will be

A- 2:1
B- 3:1
C- 3:2

2. Gaining ratio is given which is different than the old ratio
In this case

New share of continuing partner = his old share + gained from the outgoing partner.

Example 2 : A, B & C share profits in the ratio 3:2:1. On C's death his share is taken by A & B in the ratio of 2:1 Calculate new ratio

Solution - In this case gaining ratio = 2:1 (given)
A's old share = 3/6, B's old share = 2/6 & C's share = 1/6
A's gain = 2/3 of C's share = 2/3*1/6 = 2/18
B's gain = 1/3 of C's share = 1/3 * 1/6= 1/18
A's new share = A's old share + A's gain
= 3/6+2/18 = 11/18
B's new share = B's old share+B's gain
= 2/6+1/18= 7/18
New ratio = 11:7

3. If the new ratio is given then
Gaining ratio = New Ratio - Old Ratio

Example 3 :- A, B & C are partners in the ratio of 3:2:1 C retires & A & B decide to share future profit in the ratio of 5:3
A's Gain = 5/8-3/6 = 3/24
B's Gain = 3/8-2/6=1/24
Gaining ratio = 3:1

Distinction between the Sacrificing and Gaining Ratio

Basis	Sacrificing Ratio	Gaining Ratio
1. Meaning	It is the ratio in which the old partners surrender a part of their share of profits in favour of a new partner.	It is the ratio in which the remaining partner's acquire the outgoing partner's share of profit
2. When calculated	At the time of admission of a new partner	At the time of retirement or death of a partner.
3. Formula	Sacrificing Ratio= Old Ratio- New Ratio	Gaining Ratio= New Ratio- Old Ratio
4. Purpose	New partners share of goodwill is divided between old partners in this ratio.	Retiring or deceased partner's share of goodwill is paid by the continuing partners in this ratio

Treatment of Goodwill

According to accounting standard - 10, Goodwill account can't be raised. Therefore only adjustment entry is done for goodwill.

Steps to be followed :-

1. When old goodwill appears in the books then first of all this is written off in the old ratio.

Remember Old Goodwill Old Ratio

All Partners' capital A/c Dr

To Good will A/c

2. After writing off old goodwill **adjustment of retiring partner's share of goodwill will be made** through the following journal entry.

Remaining Partner's Cap A/c Dr (in gaining ratio)

To Retiring/Deceased Partner's Cap A/c

Example 4 : M, N & P are partners in a firm. P retires & the goodwill of the firm is valued at Rs.30000. M & N decide to share future profits in the ratio of 3:2. Pass necessary adjustment entries.

1. If goodwill A/c already appears in teh books at Rs.18000
2. When no goodwill A/c appears in the books.

Solution :- Old ratio of M, N & P = 1:1:1 (since profit sharing ratio is not given it is treated as equal)

New ratio= 3:2

M's gain = 3/5-1/3= 4/15

N's gain = 2/5-1/3= 1/15

Gaining ratio = 4:1

P's shareof goodwill = 30,000*1/3 = 10,000

Case 1.

1. Old goodwill will be written off in the old ratio i.e. 1:1:1

M's Capital A/c Dr 6000

N's Capital A/c Dr. 6000

P's Capital A/c Dr 6000

To Goodwill A/c 18000

2. Adjustment entry will be done in gaining ratio

M's Capital A/c Dr.8000

N's Capital A/c Dr.2000

To P's Capital A/c 10,000

Case 2. When No goodwill already appears in the books then only second entry will be done.

Hidden goodwill

Sometimes goodwill is not given in the question directly. But if a firm **agrees to pay a sum which is more than his balance in capital a/c after making all adjustment with respect to reserves, revaluation of assets and liabilities etc. then excess amount is treated as his share of goodwill (known as hidden goodwill)**

EXAMPLE 5 : Let R, S & T are partners in a firm sharing profit & loss in the ratio of 2:2:1. T Retires and his balance in capital a/c after adjustment for reserve & revaluation of assets & liabilities comes out to be Rs.50000. R & S agree to pay him Rs.60000. Give journal entry for the adjustmnet of goodwill.

Solution

New ratio between R & S = gaining ratio = 2:2 or 1:1

T's share of goodwill (hidden) = Rs.60000-50000=10000

Hence adjustment entry is

R's capital a/c Dr 5000

S's capital a/c Dr 5000

To T's capital a/c 10000

(T's share of goodwill adjusted in gaining ratio i.e. 1:1)

3. Revaluation of Assets and Reassessment Liabilities

Revaluation A/c is prepared in the same way as in the case of admission of a new partner. Profit and loss on revaluation is transferred among all the partners in old ratio.

4. Adjustment of Reserves and Surplus (Profits)

(Appearing in the Balance Sheet- Liability Side)

(a) General Reseve A/c	**Dr.**
Reserve Fund A/c	**Dr.**
P& L A/c (Credit Balance)	**Dr.**
To all partners Capital/Current A/c in old ratio.	

Example 6 :- X, Y and Z are partners in a firm sharing profits and losses in the ratio of 2:1:1, Y retires on 31st March, 2011. On that date, there was a balance of Rs.24,000 in general reserve and Rs.16,000 in profit and loss A/c of the firm. Give Journal entries.

Solution

General Reserve A/c	**Dr 24,000**	
P & L A/c	**Dr 16,000**	
To X's Cap A/c		**20,000**
To Y's Cap A/c		**10,000**
To Z's Cap A/c		**10,000**

(Reserve & Surplus amount distributed in old ratio on Y's retirement)

b) Specific Funds - If the specific funds such as workmen's compensation fund or investment fluctuation fund are in excess of actual requirement, the excess will be transferred to the Capital A/c in old ratio.

Workment Compensation Fund A/c	Dr
Investment Fluctuation Fund A/c	Dr
To All Partner's Cap A/cs	

Example 7 : P, Q and Rare partner's sharing profits and losses in the ration of 3:2:1. P retires and on that date there was workmen's compensation fund amount Rs.30,000 in the Balance Sheet. But actual liability on this account was for Rs.12,000 only on that date. Give Journal Entry.

Solution

Excess amount in Workmen's Compensation Fund =
Rs.30,000-Rs.12,000= Rs.18,000 (Cr)
This will be transferred to all partner's Capital A/c in old ratio
Journal Entry

W. Compensation Fund A/c	Dr 18,000
To P's Cap A/c	9000
To Q's Cap A/c	6000
To R's Cap A/c	3000

(Excess amount in W. Comp. Fund istrfd to partner's Cap A/cs in old ratio)

c) For distributing accumulated losses

(I.e. P & L A/c debit balance shown on the Asset side of Balance Sheet)

All partner's Cap/Current A/c Dr (in old ratio)

To P & L A/c

Example 8 :- A, B and C are equal partner's. A retires and on that date there was a debit balance of Rs.15,000 in P & L A/c. Give Journal entry.

Solution

A's Cap A/c Dr 5,000

B's Cap A/c	Dr	5,000	
C's Cap A/c	Dr	5,000	
To P & L A/c			15,000

(Loss in P & L A/c written off in old ratio on A's retirement)

5. Adjustmetn of Joint Life Policy (JLP)

Introduction

JLP means the policy taken by the firm on the lives of the partners. When any of teh partners dies the insurance company pays the whole amount which makes the payment easy to deceased partner's legal representatives in case of death.

Accounting treatment in case of retirement

Case1. . When premium paid is considered as Revenue Expenditure – In this case the premium paid is debited to P&L A/c and JLP A/c doesn't appear in the balance sheet. In this case the **Retiring partner's share** in the **surrender value** of **JLP will be debited to the remaining partners Cap A/c in gaining ratio.**

I.e. Remaining Partner's Cap A/c Dr

To Retiring Partner's Cap A/c

Example 9: -D, E and F are partners in a firm sharing profit & losses in the ratio of 3:2:1. F retires on 31st March 2011. The firm had a JLP of Rs.80,000, the surrender value of which was Rs.18,000 on that date annual premium paid on the policy of Rs.10,000 which was debited to P&L A/c every Year. Give adjustment entry if no JLP A/c appears in the Balance Sheet.

Solution

F's share in the surrender value = 1/6*18000=Rs.3000

Gaining Ratio b/w D: E=3:2

Adjustment Entry

D's Cap A/c Dr1800

E's Cap A/c Dr1200

To F's Cap A/c 3000

(F's share in the surrender value of JLP adjusted in gaining ratio)

Case2. . When premium paid is considered as Capital Expenditure- In this case the JLP A/c will be already appearing in the Balance Sheet at surrender value. Then no further treatment is required because it means that the retiring partners share is already included in his Cap A/c.

Disposal of the Amount Due to the Retiring Partner

The outgoing partners A/c is settled as per the terms of partnership deed. Three cases maybe there as given below-

1. When the retiring partner is paid full amount either in cash or by cheque.

Retiring Partner's Cap A/c Dr

To Cash or Bank A/c

2. When the retiring partner is paid nothing in cash then the whole amount due is trfd to his loan
A/c.

Retiring Partner's Cap A/c Dr
To retiring partner's Loan A/c

3. When Retiring Partner is partly paid in cash and the remaining amount is treated as Loan.

Retiring Partner's Cap A/c Dr (Total Amount due)
To Cash/Bank A/c (Amount Paid)
To Retiring Partner's Loan A/c(Amount of Loan)

Settlement of Loan of the Retiring Partner

Loan of the retiring partner is disposed off according to the pre decided terms and conditions among the partners. Normally the Principal amount is paid in **few equal installments**. In such cases **interest is credited to the Loan A/c on the basis of the amount outstanding at the beginning of each year** and the amount paid is debited to loan A/c.The following Journal entries are done

a) For interest on Loan.

Interest A/c Dr
To Retiring partner's Loan A/c

b) For the payment of installment.

Retiring Partner's Loan A/c Dr
To Cash/ Bank A/c

Example 10: -A, B, and C are partners in a firm. B retires from the firm on 1st Jan 2008. On the date of his retirement Rs.66, 000 were due to him. It was decided that the payment will be done in 3 equal yearly installments together with interest @ 10%p.a. on the unpaid balance. Prepare B's Loan A/c.

B's Loan A/c

Date	Particulars	LF	Amt.(₹)	Date	Particulars	LF	Amt (₹)
2008				2008	B's Cap A/c	F	66,000
Dec 31	Bank A/c			Jan 1			
	(22,000+6600)		28,600	Dec31	Interest A/c		
"	Balance c/d		44,000				6,600
2009			**72,600**		(10% of 66,000)		**(72,600)**
Dec 31	Bank A/c		26,400	2009	Balance b/d		44,000
"	Balance c/d		22,000	Jan 1			
				Dec 31	Interest A/c (10%		4,400
			48,400		of 44,000)		**48,400**
2010				2010			
Dec 31	Bank A/c		24,200	Jan 1	Balance b/d		22,000
	(Final Payment)			Dec 31			
					Interest A/c (		2,200
			24,200		10% of 22,000)		**24,200**

Adjustment of Capitals

At the time of retirement /death, the remaining partners may decide to **adjust their capitals** in their **new profit sharing Ratio**. Then

- **The sum of their capitals will be treated as the total capital of the new firm which will be divided in their New Profit Sharing Ratio.**
- **Excess or Deficiency of capital in the individual capital A/c is calculated.**
- **Such excess or shortage is adjusted by withdrawal or contribution in cash or transferring to their current A/cs.**

JOURNAL ENTRIES

a) **For excess Capital withdrawn by the Partners**

Partner's capital A/c Dr

To Cash/Bank A/c

b) **For deficiency, cash will be brought in by the partner**

Cash/Bank A/c Dr

To Partner's Cap A/c

Example 11:-X, Y and Z are partners in a firm sharing profits in the ratio of 2:2:1. X retires and after all adjustments the Capital A/cs of the Y and Z have a balance of ₹ 70,000 and ₹ 50, 000 respectively. They decided to adjust their capitals in new profit sharing ratio by withdrawing or bringing cash. Give necessary Journal entries and show your working clearly.

Solution

The capital of the new firm

= Total capital of Y and Z after adjustments

=₹ 70, 000+50, 000

=₹ 1,20,000

	Y	Z
New Capital based on New Ratio i.e. 2:1 (total being 1,20,000)	80,000	40,000
Existing capital after adjustments	70,000	50,000
Cash is being brought in or paid off	**10,000 (brought in)**	**10,000 (to be paid)**

Journal Entries

	Dr. (₹)	Cr. (₹)
1. Bank A/c Dr To Y's Cap A/c (Amount to be brought in by Y)	10,000	10,000
2. Z's Cap A/c Dr (Amount to be withdrawn by Z)	10,000	10,000

Problem : (Preparation of balance sheet of the reconstituted firm) Vijay, Vivek and Vinay wre partners in a firm sharing profits in 2:2:1 ratio. On 31.03.2006 Vivek retire from the firm. On the date of Vivek's retirement the balance sheet of the firm was as follows :

Balance Sheet of Vijay, Vivek and Vinay

As at 31.03.2006

Liabilities		Amount (₹)	Assets		Amount (₹)
Creditors		54,000	Bank		55,200
Bills Payable		24,000	Debtors	12,000	
Outstanding Rent		4,400	Less : Provision for		
Provision for Legal		12,000	doubtful debts	800	11,200
Claims			Stock		18,000
Capitals :			Furniture		8,000
Vijay	92,000		Premises		1,94,000
Vivek	60,000				
Vinay	40,000	1,92,000			
		2,86,400			2,86,400

On Vivek's retirement it was agreedthat:

i. Premises will be appreciated by 5% and furniture will be appreciated by ₹ 2, 000. Stockwill be depreciated by 10%.

ii. Provision for bad debts was to be made at 5% on debtors and provision for legal damages to be made for ₹ 14, 400.

iii. Goodwill of the firm is valued at ₹ 48,000.

iv. ₹ 50,000 from Vivek's Capital A/C will be transferred to his loan A/c and the balance will be paid by cheque.

Prepare revaluation a/c, partners Capital A/cs And Balance Sheet of Vijay and Vinay after Vivek's retirement.

[CBSE 2007(outside Delhi)]

Solution :-

Revaluation Account

Dr. **Cr.**

Particulars	Amount (₹)	Assets	Amount (₹)
To Stock	1,800	By Premises	9,700
To Provision for legal Claim	2,400	By Furniture	2,000
		By Provision For doubtful debts	
To profit Transferred			
Vijay 3,080			
Vivek 3,080			
Vinay 1,540			
	7,700		
	11,900		11,900

Capital Accounts

Dr. **Cr.**

Particulars	Piyush	Pooja	Praveen	Particulars	Piyush	Pooja	Praveen
To Vivek's Capital	12,800	–	6,400	By Balance b/d	92,000	60,000	40,000
To Vivek's Loan	–	50,000	–	By revaluation A/c	3,080	3,080	1,540
To Bank	–	32,280	–	By Vijay's Capital	–	12,800	–
To Balance	82,280	–	35,140	By Vinay's c/d Capital	–	6,400	–
	95,080	82,280	41,540		95,080	82,280	41,540

Balance Sheet
As at 31st March 2006

Liabilities	Amount (₹)	Assets	Amount (₹)
Creditors	54,400	Bank	22,920
Bills payable	24,000	Debtors	
Outstanding Rent	4,400	12,000	11,400
Provision for legal claims	14,400	Less provision	16,200
Vivek's Loan	50,000	<u>600</u>	10,000
Vijay's Capital	82,280	Stock	2,03,700
Vinay's Capital	35,140	Furniture	
		Premises	
	2,64,220		2,64,220

WORKING NOTE:-

1. New provision of bad debts on debtors(5%)=5%of Rs.12,000=600
   Old provision = Rs. 800 as given in the balance Sheet
   Excess of Rs. 200 is profit &trfd to revaluation A/c
2. Goodwill of the firm =48,000
   Vivek share =48,000*2/5=Rs.19,200
   Will be given by Vijay &Vinay in Gaining Ratio i.e. 2:1
3. Vivek's total amount due on retirement= Rs. 82,280
   Less amount trfd to his loan A/c = Rs. 50,000
   Amount to be paid by cheque = Rs.32,280

Death of a Partner

Accounting treatment in the case of death is same as in the case of retirement except the following:-

1. The deceased partners claim is transferred to **his executer's account.**
2. Normally the **retirement** takes place at the **end of the Accounting Period** but the **death** may **occur at any time**. Hence the **claim of deceased partner** shall also **include his share of profit or loss, interest on capital and drawings if any from the date of the last balance sheet to the date of his death.**
3. On death of a partner, the **insurance company** pays the **entire amount of the sum assured on JLP**.

The treatment of profits and JLP will be taken up one by one as follows-

I. Calculation of Profits/Loss for the Intervening Period

It is calculated by any one of the two methods given below:-

a) On Time Basis: - in this method **proportionally profit** for the time period is calculated either on the **basis of last year's profit or on the basis of average profits of last few years** and then deceased partner's share is calculated based on his share of profits.

Example 1.- A, B and C are partners sharing profits in the ratio of 3:2:1. A dies on 31st July 2011. The profits of the firm for the year ending 31st March 2011 were ₹ 42000. Calculate A's share for the period from 1st April to 31st July 2011 on the basis of last year's profits. Pass necessary journal entry also.

Solution – A's profit = Preceding year's profit x Proportionate Period x Share of A

= ₹ 42, 000x4/12x3/6

= ₹ 7, 000

Journal Entry

	Dr. (Rs.)	Dr. (Rs.)
P&L Suspense A/c Dr	7,000	
To A's Capital A/c		7,000

b) On Turnover or Sales Basis- In this method the profits upto the date of death for the current year are calculated on the **basis of current year's sales upto the date of death by using the formula.**

Profits for the current year upto the date of death =

(Sales of the current year upto the date of death/total sales of last year)x Profit for the last year.

Then from this **profit the deceased partner's share of profit is calculated.**

Example2 – If in the example- 1 given above the sales for the last year are Rs.2, 10, 000 and for the current year upto 31^{st} July are say Rs.90, 000 then Profits from 1^{st} April to 31^{st} July 2011

= (90, 000/2, 10,000)x42,000

= Rs.18, 000

A's share = Rs.18, 000x3/6=Rs. 9, 000

Journal Entry will be

P&L Suspense A/c Dr 9, 000

To A's Capital A/c 9, 000

c) Life Policy- Life policies on the lives of the partners is taken by a firm to arrange money to settle the account of deceased partner. It may be of two types:-

1) Joint Life Policy- It is taken jointly by the firm **on the lives of all the partners**. **If any** of the **partners dies**, the **insurance company pays whole of the amount.**

2) Individual life policies- Sometimes the firm takes **individual life policies** on the lives of partners **instead of one single Joint life policy.** In this case the insurance company pays the **full sum assured** on the **life policy of the deceased partner only.**

Accounting Treatment

Case 1 – When surrender values are not appearing in the books.

a) For the amount to be received on maturity (death) of a partner.

i. Insurance Co. A/c Dr

To Life Policy A/C

(For the amount due on the death of a partner)

ii. Life Policy A/c Dr

To All Partner's Capital A/cs

(For the amount due transferred to all partners' capital A/cs in old ratio)

b) For **deceased partners share in the surrender values** of the life policies of **surviving partners.**

Remaining Partners Capital A/c Dr

To Deceased Partner's Capital A/c

(For deceased partner's share in the surrender values of surviving partner's life policies **adjusted in gaining ratio**)

Example3 : A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1**, B dies** and on that there was a JLP for R.60, 000 for which annual premium of Rs.6, 000 was paid out of profits.

Surrender value of the policy on the date of death was Rs.12, 000. Give necessary journal entries.

Solution –

Note . Here (In case of JLP) surrender value is not important because on death of any partner, insurance

company pays the full amount as on maturity i.e. Rs.60, 000.

Journal entry

1. Insurance Co. A/c Dr	**60, 000**	
To Joint Life Policy A/c		**60,000**
(Sum due on B's death)		
2. JL Policy A/c Dr	**60,000**	
To A's Cap A/c		**30,000**
To B's Cap A/c		**20,000**
To C's Cap A/c		**10,000**

(Amount transferred in all partners Capital in old ratio)

Example 4. X, Y and Z are partners in a firm sharing profits and losses in the ratio of 3:2:1, A dies and on that date there were three life policies of Rs.30, 000 on the life of A, Rs.20, 000 on life of B and Rs.10, 000 on the life of C. Surrender value of this policies on the date of death was 40%. Give journal entries on A's death if no policy A/c appears in the Balance Sheet.

Solution –

I) For A's policies

(a) Insurance Co. A/c Dr	**30,000**	
To Life Policy A/c		**30,000**
(Amount due on A's Policy on A's Death)		
(b) Life Policy A/c Dr	**30, 000**	
To A's Cap A/c		**15,000**

To B's Cap A/c **10,000**

To C's Cap A/c **5,000**

(Amount transferred in old ratio)

II) For B's and C's Policies

Maturity amount of B's Policy= 20, 000

Maturity amount of C's Policy= 10, 000

Total = 30,000

Surrender Value =40%of Rs.30, 000

=Rs.12, 000

A's share in the surrender value = (3/6) x12, 000=Rs.6000

Gaining ratio between B and C= 2:1

Adjustment entry

B's capital A/c Dr 4,000

C's capital A/c Dr 2,000

To A's capital A/c 6, 000

(Adjustment of retiring partners share in surrender values of B and C's policies in gaining ratio)

Case2- when surrender values already appears in the Balance Sheet.

1. For the amount to be received from the Insurance Co. on Joint Life policy or the Policy in the name of deceased partner.

(a) Insurance Co. A/c Dr

To life policy A/c

(For the amount due on the death of a Partner)

(b) Life policy A/c Dr**(By the Amount received less surrender value)**

To All Partner's Capital A/c

2. **No entry for the surviving partners policies**.

Example 5- In the 3rd example if the surrender value of Rs.12, 000 is shown in the Balance Sheet then following entries will be passed.

Solution -

1. Insurance Co. A/c Dr 60, 000

To JLP A/c 60,000

(Amount due on JLP on B's death)

2. J.L Policy A/c Dr	**48,000**
To A's Capital A/c	**24,000**
To B's Capital A/c	**16,000**
To C's Capital A/c	**8,000**

(Balance in JL Policy A/c has transferred to all Partners Capital A/cs in old ratio)

Working note- J.L.Policy A/c

Amount due to Insurance Co. (Credited to JLP) = Rs 60,000

Less Surrender value already Appearing on the debit of JLP = Rs 12,000

Balance amount in the credit side of JLP to be transferred top all partners Cap A/cs =Rs48, 000

Complete question generally asked for 6 marks

Problem- (Death of a partner) M, N and O were partners in a firm sharing profits and losses equally.

Their Balance Sheet on 31-12-2009 was as follows

Liabilities			Amount (₹)	Assets	Amount (₹)
Capitals :	M	70,000		Plant and machinery	60,000
	N	70,000		Stock	30,000
	O	70,000		Sundry Debtors	95,000
General Reserve			2,10,000	Cash at Bank	40,000
Creditors			30,000	Cash in Hand	35,000
			20,000		
			2,60,000		**2,60,000**

N died on 14th March, 2010. According to the Partnership Deed, executers of the deceased partner are entitle to:

(i) Balance of partner's capital A/c.

(ii) Interest on capital @ 5% p.a.

(iii) Share of goodwill calculated on the basis of twice the average of past three years profits.

(iv) Share of profits from the closure of the last accounting year till the date of death on the basis of twice the average of three completed year's profits before death.

Profits for 2007, 2008 and 2009 were Rs. 80, 000, Rs. 90,000, Rs 1, 00,000 respectively. Show the working for deceased partner's share of goodwill and profits till the date of his death. Pass the necessary journal entries and prepare N's Capital A/c to be renderer to his executers.

(CBSE 2011, Delhi)

Solution

Date	Particulars	L.F.	Debit ₹	Credit ₹
2010 14th March	General Reserve A/c Dr To N's Capital A/c (Being transfer of N's share of general reserve of his Capital A/c)		10,000	10,000

	Interest on Capital A/c Dr To N's Capital A/c (Being interest 5% p. a. credited to N's Capital A/c upto 14/03/2010)		700	700
	M's Capital A/c Dr O's Capital A/c Dr To N's Capital A/c (Being goodwill adjusted in gaining ratio i.e. 1:1)		30,000 30,000	60,000
	Profit and Loss Supense A/c Dr To N's Capital A/c (Being the transfer to N's share of profit to his capital A/c)		12,000	12,000
	N's Capital A/c Dr To N's Executor A/c (Being the transfer of amount due to N's executor A/c)		1,52,700	1,52,700

N's Capital A/c

Particulars	Rs.	Particulars	Rs.
To N's Executors A/c	1,52,700	By Balance b/d	70,000
		By General Reserve A/c	10,000
		By Interest on Capital A/c **(70,000 *5/100*73/365)**	700
		By M's Capital A/c	30,000
		By O's Capital A/c	30,000
		By Profit & Loss Suspense A/c (90,000*2*73/365*1/3)	12,000
	1,52,700		1,52,700

Working Note:

1) Calculation of Goodwill

Average profit for 3years=(Rs.80, 000+90,000+1,00,000)/3
=90,000

Goodwill of the firm=Average Profit*No. Of Year of Purchase=90,000*2=Rs.1, 80,000

Total N's Share in Goodwill=1, 80,000*1/3=60,000

2) Time from the date of last balance Sheet(31st December,2009) to the date of death(14th March, 2010)

=31 days of January+28 days of Feb (2010 is not a leap year)+14 days of March
=73 days

CHAPTER 6

DISSOLUTION OF A PARTNERSHIP FIRM

Dissolution of a firm: As per Indian Partnership Act, 1932: ***"Dissolution of firm means termination of partnership among all the partners of the firm".*** When a firm is dissolved, the business of the firm terminates. All the assets of the firm are disposed off and all outsiders' liabilities and partners' loan and partners capitals are paid.

Dissolution of Partnership: ***Dissolution of Partnership refers to termination of old partnership agreement (i.e., Partnership Deed) and a reconstruction of the firm.*** It may take place on

Change in profit sharing ratio among the existing partner;

– Admission of a partner; and

– Retirement or Death of a partner.

It may or may not result into closing down of the business as the remaining partners may decide to carry on the business under a new agreement.

Types of dissolution of firms : A partnership firm can be dissolved in any of the following ways :

(A) Without the intervention of the court :

(1) When all partners agree to dissolve the firm (Sec. 40);

(2) Compulsory Dissolution (Sec. 41)

(i) When all or all but one partner of the firm become insolvent.

(ii) when business of the firm become unlawful.

(3) On the happening of any of the following events : (Sec. 42)

(i) On the insolvency of a partner.

(ii) On the fulfilment of the objective of the firm for which the firm was formed.

(iii) On the expiry of the term (period) for which the firm was formed.

(4) By Notice (Sec. 43) : When the duration of the partnership firm is not fixed and it is at will of the partners. Any partner by giving notice to other partners can dissolve the firm.

(B) Dissolution by order of the court (Sec 44) : A court on application by a partner may order the dissolution of the firm under the following circumstances :

(1) When a partner has become of unsound mind.

(2) When a partner has become permanently incapable of performing his duties as a partner.

(3) When a partner is found guilty of misconduct that may harm the partnership.

(4) When a partner consistently and deliberately commits breach of partnership agreement.

(5) When a partner transfer whole of his interest in the business firm to a third party, without the consent of existing partners.

(6) When the court is satisfied that the partnership firm cannot be carried on except at a loss.

(7) When the court find is that the dissolution of firm is justified and equitable.

ACCOUNTING TREATMENT ON DISSOLUTION

On dissolution of a firm, the following accounts are opened to close the books of the firm:

– Realisation Account;
– Partner's Loan Account;
– Partners' Capital Accounts; and
– Cash or Bank Account.

Realisation Account: It is ***nominal account*** opened on the dissolution of a firm ***to ascertain the profit or loss on realisation of assets and payments of outsiders' liabilities***. This account is closed by transferring the balance (i.e., profit or loss on realisation) to partner's capital accounts.

Preparation of Realisation Account

The following Journal Entries are passed:

A. For Closing Assets Accounts :

Realisation A/C Dr.
To Sundry Assets A/C
(Being assets transferred to Realisation A/c)

Note :
1. Cash and Bank balance are not transferred to Realisation Account.
2. Assets (tangible and intangible) are transferred to Realisation Account at their ***Gross Value***

3. Fictitious Assets such as Debit balance of Profit and Loss Account or Advertisement Suspense Account etc. are not transferred to Realisation Account. These are directly debited to partners' capital accounts in their profit sharing ratio by passing the following entry:

Partner's capital A/c Dr.
To Profit and Loss A/c
To Advertisement Suspense A/c
(Being Balance of losses transferred to capital accounts)

4. Provisions against assets such as Provision for Depreciation or Provision for Bad & Doubtful debts etc. are transferred to Realisation Account by passing a

separate entry:

Provision's for Bad Debts A/c Dr.
Provision's for Depreciation A/c Dr.
Joint Life Policy Reserve A/c Dr.
Investment Fluctuation Fund A/c Dr.
Machinery Replacement Reserve A/c Dr.
To Realisation A/c
(Being Provisions & Reserves Against Assets transferred to Realisation Account)

B. For Closing Liabilities Accounts :

Sundry Liabilities A/cs Dr.
To Realisation A/c
(Being sundry liabilities transferred to Realisation A/c)

Note:

1. Only third parties liabilities/outsiders' liabilities are transferred to Realisation A/c.

2. Balance of Partner's Loan Accounts are not transferred to Realisation Account. Separate accounts are opened to settle such liabilities.

3. Undistributed profits and reserves are also not transferred to Realisation A/c. These are directly credited to partners' capital accounts in their profit – sharing ratio by passing the following entry:

Profit and Loss A/c Dr.
General Reserves A/c Dr.
Reserve Fund A/c Dr.
Contingency Reserve A/c Dr.
To Partners' Capital A/cs
(Being balance of undistributed profits transferred to capital accounts)

4. Provident Fund is a liability on the firm towards employees and hence it is transferred to Realisation A/c

5. If any liability is expected to arise against any fund or reserve e.g., Workmen's Compensation Fund, then an amount equal to such liability is transferred to Realisation A/c and balance ,if any, is distributed among the partners in their profit-sharing ratio by passing the following entry:

Workmen's Compensation Fund A/c Dr.
To Realisation A/c (Liability)
To Partners' Capital A/cs (Balance, if any)
(Being liability against workmen's compensation fund transferred to Realisation A/c and balance

distributed among partners)

Example. Workmen's Compensation Fund shown in the liability side of Balance Sheet is Rs. 50,000. At the time of dissolution liability against this fund is estimated at Rs. 30,000. Pass necessary Journal Entry.

Workmen's Compensation Fund A/c Dr.	**50,000**	
To Realisation A/c		**30,000**
To A's Capital A/cs		**10,000**
To B's Capital A/cs		**10,000**

(Being liability against workmen's compensation fund transferred to Realisation A/c and balance distributed among partners)

C. For Realisation of Assets (whether recorded or unrecorded

a. When assets are sold for cash

Cash/Bank A/c Dr.

To Realisation A/c

(Being assets sold for cash)

b. When assets are taken over by any partner

Partner's Capital A/c Dr.

To Realisation A/c

(Being assets taken over by any partner)

c. When assets are taken over by any creditor in part or full payment of his dues :

I. **In case of Full Settlement** :

i. NO ENTRY is passed for the transfer of assets to the creditor

ii. NO ENTRY is passed for the payment to creditor

II. In case of Part Settlement :

i. NO ENTRY is passed for the transfer of assets to the creditor.

ii. The agreed amount of asset is deducted from the claims of the creditor and the balance is paid to him.

Note:

1. If nothing is stated regarding the realisation of any tangible assets then such assets should be assumed to be realized at book value

2. ***If nothing is stated regarding the realisation of any intangible assets like goodwill, patents, trade marks etc. then it is assumed that such assets have not realized any amount.***

D. For Payments of Liabilities

a. When liabilities are paid in cash

Realisation A/c Dr.

To Cash/Bank A/c

(Being liabilities paid in cash)

b. When liabilities are taken over by any partner

Realisation A/c Dr.

To Partner's Capital A/c

(Being liabilities taken over by a partner)

c. When assets are taken over by any creditor in part or full payment of his dues :

I. In case of Full Settlement:

i. NO ENTRY is passed for the transfer of assets to the creditor

ii. NO ENTRY is passed for the payment to creditor

II. In case of Part Payment:

i. NO ENTRY is passed for the transfer of assets to the creditor

ii. The agreed amount of asset is deducted from the claims of the creditor and the balance is paid to him.

Note:

If nothing is stated regarding the settlement of any outside liability, then it should be assumed that the amount equal to book value is paid.

E. For Realisation Expenses

a. When expenses are paid by firm and borne by firm:

Realisation A/c Dr.

To Cash/Bank A/c

(Being realisation expenses paid in cash)

b.When expenses are paid by any partner and borne by firm:

Realisation A/c Dr.

To Partner's Capital A/c

(Being realisation expenses paid by a partner)

c.When expenses are paid by firm (on behalf of any partner) and borne by any partner:

Partner's Capital A/c Dr.

To Cash/Bank A/c

(Being realisation expenses paid on behalf of a partner)

d. When expenses are paid by any partner and borne by same partner :

NO ENTRY

e. When a partner is paid a fixed amount for bearing realisation expenses then :

i. Actual expenses are not to be considered; and

ii. **Realisation A/c** **Dr. [With Fixed Amount]**

To Partner's Capital A/c

(Being realisation expenses paid by a partner)

f. When expenses are paid by one partner and borne by another partner:

Partner's Capital A/c **Dr. (Who borne the expenses)**

To Partner's Capital A/c **(Who pays the expenses)**

(Being realisation expenses paid by one partner and borne by another partner)

F. For Closing Realisation Account

a. When Realisation A/c discloses profit (in case total of credit side is more than the total of debit side)

Realisation A/c **Dr.**

To Partners' Capital A/cs

(Being profit on realisation transferred to partners' capital A/cs)

b. When Realisation A/c discloses loss (in case total of debit side is more than the total of credit side)

Partners' Capital A/cs **Dr.**

To Realisation A/c

(Being loss on realisation transferred to partners' capital A/cs)

FORMAT OF REALISATION ACCOUNT

Realisation Account

Dr. **Cr.**

Particulars	Rs.	Particulars	Rs.
To Sundry Assets A/c (Excluding cash or bank balance, fictitious assets, Dr. balance of P & L A/c, Dr. balance of partners' capital/ current A/cs, Loans to partners		**By Sundry Liabilities A/c** (Excluding Cr. Balance of P & L A/c, Reserves, Partners' capital/current A/cs, Loan from Partner and Bank Overdraft)	
To Cash/Bank A/c (Amount paid for discharging liabilities-recorded and unrecorded)		**By Provision on any Assets A/c** (Such as Provision for Depreciation, Provision for Doubtful Debts, Joint Life Policy Reserve etc.	
To Cash Bank A/c Expenses on Realisation)		**By Cash/Bank A/c** (Amount received on realisation of assets-recorded and unrecorded)	
To Partner's Capital A/cs (Liabilities taken over by a commission payable to him or any expenses payable to him or		**By Partners' Capital A/cs** (Assets taken over by a partner - recorded or unrecorded)	
To partners' Capital A/cs (For transferring profit on Realisation)		**By Partners' Capital A/cs** (For transferring loss on Realisation)	

Preparation of Partners' Loan Account

If a partner has given any loan to firm, his loan will be paid
- After payament of all the outside liabilities : but
- Before making any payment to partners on account of capital

Partner's Loan A/c Dr.
To Cash/Bank A/c
(Being loan of a partner paid)

Dr. **Partner's Loan A/c** **Cr.**

Particulars	Rs.	Particulars	Rs.
To Cash/Bank A/c		By Balance b/d	

Note :

If the firm has given a loan to any partner then such loan account will show a debi balance and will appear on the asset side of Balance Sheet of the firm. Such loan accounts are settled through partner's capital account by passing the following entry :

Partner's Capital A/c ***Dr.***
To Partner's Loan A/c
(Being loan to partner transferred to his Capital A/c)

Preparation of Partner's Capital Accounts

After the transfer of

- Undistributed profits and reserves

- Profit on Realisation

- Any liability taken over by any partner

And

- Undistributed losses and fictitious assets

- Loss on realisation

- Any assets taken over by any partner

The balance of partners' capital A/cs are closed in the following manner

a. For making final payment to a partner (if total of credit side is more than the total of debit side)

Partner's Capital A/c **Dr.**

To Cash/Bank A/c

(Being excess paid to partner in cash)

b. For any amount received from a partner against debit balance in his capital account

Cash/Bank A/c **Dr.**

To Partners' Capital

(Being cash brought in by any partner)

Dr. **Partner's Capital A/cs** **Cr.**

Particulars	Rs.	Rs.	Particulars	Rs.	Rs.
To Balance b/d (Dr. Balance)			By balance b/d (Cr. Balance)		
To Profit and Loss A/c			By General Reserve A/c		
To Advertisement			By Profit and Loss A/c		
To Realisation A/c (Assets taken)			Compensation Fund		
To Realisation A/c (Loss on Realisation			By Realisation A/c (Liabilities taken)		
To Cash/Bank A/c (Excess cash paid)			By Realisation A/c (Profit on Realisation)		
			By Cash/Bank A/c (Cash brought in)		

Preparation of Cash or Bank Account

This account is prepared at the end and closed last of all. This account helps in verification of the airthmetical accuracy of accounts as both sides of this account must be equal. **There should be no balance left in Cash or Bank A/c.**

Note :

If cash and bank balance (or Bank Overdraft) both are given in the Balance Sheet, only one A/c is prepared, either a Cash A/c or a Bank A/c. If Cash A/c is opened, an entry for withdrawing the bank balance is made :

Cash A/c Dr.
To Bank A/c
(Being cash withdrawn from Bank)

If Bank A/c is opened, an entry for depositing the cash into bank is passed.

Bank A/c Dr.
To Cash A/c
(Being cash deposited into Bank)

Dr. **Cash/Bank/A/c** **Cr.**

Particulars	**Rs.**	**Particulars**	**Rs.**
To Balance b/d (Cash in Hand or Cash at Bank) To Realisation A/c (Assets Realised) To Partners' Capital A/cs (Cash brought in by partner)		By Balance b/d (Bank Overdraft) By Realisation A/c (Liabilities Paid) By Realisation A/c (Realisation Expenses Paid) By Partner's Loan A/c (Partner's Loan Paid) By Partners' Capital A/cs (Excess cash paid to partner	

Distinction between Revaluation Account and Realisation Account

Basis of Difference	**Revaluation Account**	**Realisation Account**
Purpose	It is prepared to show assets and liablities in the books at their revised values	It is prepared to ascertain the profit or loss on sale of assets and repayment of liabilities.
When to be prepared	It is prepared at the time of change in profit sharing ratio among the existing partner, admission, retirement and death of a partner.	It is prepared at the time of dissolution of a firm
Preparation of Account	This account may be prepared at a number of times during the life of a firm	This account is prepared only once during the life of a firm

Contents	This account records only those assets and liabilities whose book values have been changed	This account records all assets (except cash, fictious assets etc.) and all outside liabilities
Result	A firm continues its business even after the preparation of revaluation account.	A firm comes to an end after preparation of realisation account

Preparation of Memorandum Balance Sheet

If a balance sheet on the date of dissolution is not given in the question, then it is always advisable to prepare Memorandum Balance Sheet on the date of dissolution to ascertain the amount of balancing figure.

Note :

- In the absence of any other information "Sundry Assets" should be treated as balacing figure on the assets side of Balance Sheet.
- If the balances of Partners' Capital A/cs are not given as on the date of dissolution, first we will find the balance of partners' capital accounts as on the date of dissolution by recasting the capital accounts.
- When "Sundry Assets" are given in the question and nothing is specified about the difference on the asset side of Balance Sheet, the difference should be treated as Dr. balance of Profit and Loss A/c.

Some common mistakes committed by the students in Examination

- Entries for Assets or liabilities taken by partners
- Dissolution Expenses
- Realisation of unrecorded assets
- Payments of Unrecorded Liabilities
- Treatment of Fictitious Assets

Due care should be taken while showing the effect of above mentioned items.

Practical Problem

Q1. : Following is the Balance Sheet of X and Y, who share profits and losses in the ratioof 4:1, as at 31st March, 2011 :

Balance Sheet
As on 31st March, 2011

Liabilities	Rs.	Assets		Rs.
Sundry Creditors	8,000	Bank		20,000
Bank Overdraft	6,000	Debtors	17,000	
X's Wife Loan	8,000	Less : Provision	(2,000)	15,000
Y's Loan	3,000	Stock		15,000
Investment Fluctuation Fund		Investments		25,000
Capital	5,000	Buildings		25,000
X		Goodwill		10,000
Y	50,000	Profit and Loss A/c		10,000
	40,000			
	1,20,000			1,20,000

The firm was dissolved on the above date and the following arrangements were decided upon :

(i) X agreed to pay off his wife's loan.

(ii) Debtors of Rs.5,000 proved bad.

(iii) Others assets realised - Investments 20% less; and Goodwill at 60%

(iv) One of the creditors for Rs.5,000 was paid only Rs.3,000

(v) Buildings were auctioned for Rs.30,000 and auctioneer's commission amounted to Rs.1,000.

(vi) Y took over part for Stock at Rs.4,000 (being 20% less that the book valve). Balance stock realised 50%.

(vii) Realisation expenses amounted to Rs.2,000.

Prepare Realisation A/c, Partners' Capital A/cs and Bank A/c

Solution :

Dr. **Realisation Account** **Cr.**

Particulars	Rs.	Particulars	Rs.
To Goodwill	10,000	By Investment Fluctuation	
To Buildings	25,000	Fund	5,000
To Investments	25,000	By Provision for Doubtful	
To Stock	15,000	Debts	2,000
To Debtors	17,000	By Creditors	8,000
To X's Capital A/c		By X's Wife Loan	6,000
(X's brother loan)	8,000	By Bank A/c :	8,000
		(Asset realised	
		Debtors 12,000	
(Creditors)	6,000	Investments 20,000	
To Bank A/c		Goodwill 6,000	
(Expenses on Realisation	6,000	Buildings 29,000	
		Stock 5,000	
			72,000
		By Y's Capital A/c	
		(Stock)	4,000
		By Loss transferred to :	
		X's Capital A/cs 7,200	
		Y's Capital A/cs 1,800	
			9,000
	1,08,000		1,08,000

Partner's Capital A/cs

Dr. Particulars	X Rs.	Y Rs.	Particulars	X Rs.	Cr. Y Rs.
To Profit and Loss A/c	8,000	2,000	By Balance b/d	50,000	40,000
To Realisation A/c			(Cr. Balance)		
(Assets taken)	–	4,000	By Realisation A/c		
To Realisation A/c			(Liabilities taken)	8,000	
(Loss on Realisation	7,200	1,800			
To Bank A/c					
(Excess cash paid)	42,800	42,800			
	58,000	58,000		58,000	40,000

Cash/Bank A/c

Dr. Particulars	Rs.	Particulars	Cr. Rs.
To Balance b/d		By Balance b/d	6,000
(Cash at Bank)	20,000	(Bank Overdraft)	
To Realisation A/c		By Realisation A/c	
(Assets Realised)	72,000	(Liabilities Paid)	6,000
To Partners' Capital A/c		By Realisation A/c	
(Cash brought in by Partner		Realisation Expenses Paid)	2,000
		By Y's Loan A/c	3,000
		(Partner's Loan Paid)	
		By X' Capital A/c	42,800
		By Y's Capital A/c	32,200
	92,000		92,000

Q2. A and B were partners in a firm from 1-4-2008 with capitals of Rs.60,000 and Rs.40,000 respectively. They shared profits and losses in the ratio of 3:2. The carried on business for 2 years. In the first year, they made a profit of Rs.50,000 and in the 2nd year ending on 31st March 2010, they incurred a loss of Rs.20,000. As the business was no longer profitable, they decided to wind up. Creditors on that date were Rs.20,000. The partners withdrew Rs.8,000 each per year for their personal expenses. The assets realised Rs.1,00,000. The expenses on realisation were Rs.3,000. Prepare Realisation A/c and Partner's Capital A/c and show your working clearly.

Solution :

Book of A and B

Realisation Account

Particulars	Rs.	Particulars	Rs.
To Sundry Assets	1,18,000	By Creditors	20,000
To Bank A/c (Creditors)	20,000	By Bank A/c (Assets realised)	
To Bank A/c (Expenses on Realisation	3,000	By Loss transferred to : A's Capital A/cs 12,600 B's Capital A/cs 8,400	21,000
	1,41,000		1,41,000

Working Notes :

(i)

Partner's Capital A/cs

Dr. **Cr.**

Date	Particulars	A Rs.	B Rs.	Date	Particulars	A Rs.	B Rs.
2008 ?	To Bank A/c (Drawings)	8,000	8,000	1.04.08	By Cash A/c	60,000	60,000
31.03.2009	To Balance c/d	82,000	52,000	31.03.09	By Profit and Loss A/c	30,000	30,000
		90,000	60,000			90,000	60,000
2009 ?	To Bank A/c (Drawings)	8,000	8,000	1.04.09	By Balance b/d	82,000	52,000
31.03.09	To Profit and Loss A/c	12,000	8,000				
31.03.09	To Balance c/d	62,000	36,000				
		82,000	52,000			82,000	52,000
				1.4.10	By Balance b/d	62,000	36,000
01.04.10	To Realisation A/c (Loss)	12,600	8,400				
	To Bank A/c	49,400	27,600				
		6,2000	36,000			62,000	36,000

(ii)

Memorandum Balance Sheet

Liabilities	Rs.	Assets	Rs.
Capital		Sundry Assets	
		(Balancing Figure)	1,18,000
Rs.			
A 62,000			
B 36,000	98,000		
Creditors	20,000		
	1,18,000		1,18,000

Q.3 A and B share profitss and losses in the ration of 5:2. They have decided to dissolve the firm. Assets and external liabilities have been transferred to Realisation A/c. Pass the Journal Entries to affect the following :

(a) Bank Loan of Rs.12,000 is paid off.

(b) A was to bear all expenses of Realisation for which he is given a commission of Rs.400.

(c) Deferred Advertisement Expenditure A/c appeared in the book at Rs.28,000.

(d) Stock worth Rs.1,600 was taken over by B at Rs.1,200.

(e) As unrecorded Computer realized Rs.7,000.

(f) There was an outstanding bill for repairs for Rs.2,000. which was paid off.

Solution

Date	Particulars	L.F.	Debit ₹	Credit ₹
a	Realisation A/c Dr.		12,000	
	To Bank A/c			12,000
	(Being bank loan discharged)			
b	Realisation A/c Dr.		400	
	To A's Capital A/c			400
	(Being commission credited to A)			
c.	A's Capital A/c Dr.		20,000	
	B's Capital A/c Dr.		8,000	
	To Deferred Advertisement Expenditure A/c			28,000
	(Being the deferred advertisement expenditure			
	Written off)		1,200	
d.	B's Capital A/c Dr.			1,200
	To Realisation A/c			
	(Being Stock taken over by B at Rs.1,2000			
e.	Bank A/c Dr.		7,000	
	To Realisation A/c			7,000
	(Being unrecorded computer sold for Rs.7,000)			
f.	Realisation A/c Dr.		2,000	
	To Bank A/c			2,000
	(Being bank loan discharged)			

CHAPTER 7

Accounting for Share Capital

Company-: It is

1. A Form of business organization
2. It is an Association of persons who provide capital
3. Is an artificial, invisible and intangible
4. Has separate legal identity
5. Has Perpetual existence
6. Has Common seal
7. is not affected by death , insolvency or insanity of individual

Private company-:

According to section 3(1)(iii)

1. Has paid up capital of one lakh
2. Maximum number of members is 50
3. It restricts the right to transfer of shares
4. Prohibits any invitation to public to subscribe for shares and Debentures
5. Prohibits any invitation or acceptance of deposits from persons other than its members , directors or their relatives

PUBLIC COMPANY-:

According to section 3(1)(iv)

1. Is not a private company
2. Has minimum paid up capital of 5 lakhs or higher as may be prescribed
3. Is a private company which is subsidiary of a company which is not a private company

GOVERNMENT COMPANY

As per section 617 is a company in which more than 50% of paid up capital is held by Central or State Government or both

FOREIGN COMPANY

Section 591of Act states this type of company is incorporated outside India but has established business in India.

Incorporation of company

There are 4 stages

1. Promotion- conceiving an idea of business
2. Incorporation or registration
3. Capital subscription - which means raising capital
4. Commencement of business for which certificate of Commencement of business is to be obtained.

- **Some important definitions(theory questions)**

MINIMUM SUBSCRIPTION :It is number of shares on which amount received is sufficient to commence business .

PROSPECTUS :It is an invitation to public for subscription of shares or debentures.

PRELIMINARY EXPENSES : are expenses incurred for incorporating the company are carried in balance sheet unless these are written off.

CAPITAL- means amount invested in the business for the purpose of earning revenue. In case of company money is contributed by public and people who contribute money are called shareholders.

SHARE CAPITAL: capital raised by issue of shares is called share capital.

AUTHORISED CAPITAL-:Also Called as Nominal or registered capital .It is the maximum amount of capital a company can issue . It is stated in ***Memorandum of Association.***

ISSUED CAPITAL-: this is part of authorized capital which is offered to public for subscription. It cannot exceed authorized capital .

SUBSCRIBED CAPITAL : It is part of issued capital subscribed or applied by public.

CALLED UP CAPITAL : It is the amount of nominal value of shares that has been called up by the company for payment by the subscriber towards the share.

PAID UP CAPITAL : It is part of called up capital that the members of company or shareholders have paid.

Example : X Ltd. is registered with the following share capital 1,25,000 equity shares of Rs. 10 each, payable in the following manner 10% on application,20% on allotment ,30% on first call the balance on final call .

The company offered for subscription 80,000 equity shares .The public applied for 75,000 share

The company duly allotted these shares .It made only first call by 31st March 2010.The first call was received on all shares except 300 equity shares. Prepare Balance Sheet of Company

Disclosure of share capital in Company's Balance Sheet

Revised Form of Balance Sheet of X Ltd. as per Schedule VI Part I as at 31.03.2012

Particulars	**Note No.**	**Figure on 31.03.2010 (end of current period)**	**Figure as on 31.03.2009 (end of previous Year**
Equity and Liabilities			
1) Shareholder's Funds			
a) Share Capital	1	4,49,100	
Total		4,49,100	
ASSETS			
Current Assets			
Cash & Cash Equivalent	2	4,49,100	
		4,49,100	

Note No. :- 1

Authorised Captial		
1,25,000 equity shares @ ₹ 10 each		12,50,000
Issued Capital		
80000 Equity Shares @ ₹ 10 each		8,00,000
Subscribed & Paid up		
75000 eq. shares of @ ₹ 10 each		
issued to public @ ₹ 6	4,50,000	
Less : Unpaid calls	900	4,49,100
		4,49,100

Note No. 2 :	Amount received on application	
	75000 @ ₹ 1(10%)	75,000
	Amount received on allotment	1,50,000
	75000 sh @ ₹ 2(20%)	
	Amount Received on call	2,24,100
	74700 Shares @ ₹ 3(30%)	
		4,49,100

RESERVE CAPITAL : It is that part of uncalled capital which the company reserve to be called only upon winding up of company. For this a special resolution has to be passed

CAPITAL RESERVE : It is capital profit not available for distribution as dividend.

- It is represented in balance sheet of company as Reserves and Surplus under the heading Shareholders' Funds

CLASSES OF SHARES : There are two classes of shares

1. Preference shares
2. Equity shares

> 1. Preference shares : are shares which get preferential right in respect of
> A) Right of dividend
> B) Repayment of capital on winding up

Equity shares : The shares which are not preference shares are called equity shares and do not get preference in above respect.

ISSUE OF SHARES

Shares can be issued in two ways

1. for cash
2. for consideration other than cash

Terms of issue of share : shares can be issued in three ways

1. Issue of shares at Par
2. Issue of shares at Premium
3. Issue of shares at Discount

Shares payable in Instalments

1. First instalment paid along with application is called as application money.
2. Second instalment paid on allotment is called as allotment money.

3. Subsequent instalment paid are called as call money calls can be more than one and called First call, second call or as the case may be

ISSUE OF SHARES FOR CASH AT PAR : This means shares are issued at face value

Journal entries

For application money received	Bank Account Dr. To Share Application A/c	(No. of application received Amount received
On acceptance of application	Share Application Account Dr. To Share Capital Account	(No of shares alloted x amount called on each)
For allotment money due	Share Allotment Account Dr. To Share Capital A/c	(No. of shares alloted x amount called on each share)
On receipt of allotment money	Bank Account Dr. To Share Allotment A/c	(No. of application allotted x Amount received on each share or actual amount received)
For call money due	Share Call A/c Dr. To Share Capital Account	(No. of shares alloted x amount called on each share)
On receipt of calls money	Bank Account Dr. To Share Call A/c	(No. of application allotted x Amount received on each share

NOTE : For each entry narration is compulsory as given in example below and carries marks columns are compulsory table should be made in proper format (all columns are compulsory) after each entry in column of particulars line must be drawn.

Example : X Ltd. invited application for 10,000 shares of the value of Rs.10 each. The amount is payable as Rs.2 on application and Rs.5 on allotment and balance on First and Final call. Teh whole of the above issue was applied and cash duly recived. Give Journal entries for the above transaction.

In the Books of X Ltd.

Solution

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr. To Share Application A/c (Being the application money received on 10,000 shares at Rs.2 per share)		20,000	 20,000
	Share Application A/c Dr. To Share Capital A/c (Being the transfer of application money on 10,000 shares to share capital account		20,000	 20,000

	Share Allotment A/c Dr. To Share Capital A/c (Being the amount due on 10,000 sharesat Rs.5 per share)		50,000	50,000
	Bank Account Dr. To Share Allotment A/c (Being the receipt of Rs.5 on 10,000 shares)		50,000	50,000
	Share Call A/c Dr. To Share Capital A/c (Being the amount due on 10,000 shares at Rs.3 per share		30,000	30,000
	Bank Account Dr. To Share Call A/c (Being the receipt of Rs.3 on 10,000 shares		30,000	30,000

ISSUES OF SHARES AT PREMIUM : It is issue of share at more than face value. (Section 78)

This premium can be utilised for

1. Issue of bonus shares
2. Write off preliminary expenses, discount, commission on issue of shares
3. Buy back of shares
4. Redemption of debentures o preference shares

JOURNAL ENTRIES ARE

For application money received	Bank Account Dr. To Share Application A/c	(No. of application receivedx Amount received on each share
On acceptance of application	Share Application Account Dr. To Share Capital Account To Securities Premium A/c	(with total application money) (share capital received on application) (amount of premium received if any)
For allotment money due	Share Allotment Account Dr To Share capital Account To Securities Premium	(No of shares alloted x amount called on each share (securities premium due
On receipt of money	Bank Account Dr To Share Allotment A/c	(No. of application alloted x Amount received on each share i.e. actual amount received
For call money due	Share Call Account Dr. To Share Capital Account To Securities Premium	(No of shares allotted x amount called on share)

On receipt of calls money	Bank Account To Share call Account	(Actual amount received)

Example : V 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)
On Application	Rs.2
On Application	Rs.2

All shares were duly subscribed and all money duly received. Pass necessary Journal

IN THE BOOKS OF V Ltd. JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr. To Equity Share Application A/c (Being the application money received on 20,000 shares at Rs.4 per share)		80,000	 80,000
	Equity Share Application A/c Dr. To Share Capital A/c (Being the transfer of application money on 20,000 shares to share capital account)		80,000	 80,000
	Share Allotment A/c Dr. To Equity Share Capital A/c To Securities premium Account (Being the amount due on 20,000 shares at Rs.5 including premium of Rs.3 per share		1,00,000	 40,000 60,000
	Bank Account Dr. To Share Allotment A/c (Being the receipt of Rs.5 on 20,000 shares)		1,00,000	 1,00,000
	Equity Share First Call A/c Dr. To Equity Share Capital A/c (Being the amount due on 20,000 shares at Rs.2 per share)		40,000	 40,000
	Bank Account Dr. To Equity Share First Call A/c (Being the receipt of Rs.2 on 20,000 shares)		40,000	 40,000
	Equity Share second and Final Call A/c Dr. To Equity Share Capital A/c (Being the amount due on 20,000 shares at Rs.2 per share)		40,000	 40,000
	Bank Account Dr. To Equity Share Second and Final Call. A/c (Being the receipt of Rs.2 on 20,000 shares)		40,000	 40,000

ISSUE OF SHARES AT DISCOUNT : When a company issues shares at price less than its face value it is issue of shares at discount.

Section 79 imposes restrictions on issue at discount According to this

1. Shares must be of the class already issued.
2. Ordinary resolution must be passed in the general meeting which should specify maximum discount.
3. Rate of discount should not be more than 10%
4. Sanction from company Law board must be obtained and shares must be issued within two months of permission.
5. At least one year should have passed since commencement of business has begun

NOTE : Unless specified Discount is given on allotment

JOURNAL ENTRIES (ON ALLOTMENT)

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Allotment Account Dr.		Net Amount due	
	Discount on issue of shares Account Dr.		Amount of discount	
	To Share Capital (Being the net amount due on allotment)			Face value of share
	Bank Account Dr.		Net Amount	
	To Share Allotment Account (Being the amount received on allotment			Net Amount

Example :

J. K. India Ltd. issued 10,000 shares of Rs.10 each at a dscount of 10% payable Rs.5 on application, Rs.3 on allotment and Rs.2 on First and Final Call.

Only 9,000 shares were applied for and the allotment was made to all the applicants.

Give necessary y journal entries in the book of the Company.

JOURNAL ENTRIES

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr.		36,000	
	To Share Application Account (Being application money received on 9000 shares @Rs.4 per share)			36,000
	Share Application Account Dr.		36,000	
	To Share Capital account (Being the application money transferred to Share Capital Account)			36,000

	Share Allotment Account Dr. Discount on issue of shares Account To Share Capital (Being the allotment money due on 9,000 shares @ Rs.3 per share. The amount of discount is @Rs.1)	27,000 9,000	 36,000
	Bank Account Dr. To Share Allotment Account (Being application money received on 9000 shares @Rs.3 per share	27,000	 27,000
	Share First and Final Call Account Dr. To Share Capital Account (Being the call money due on 9,000 shares @Rs.2 per share)	18,000	 18,000
	Bank account Dr. To Share First and Final call Account (Being money received on 9000 shares @ Rs.3 per share	18,000	 18,000

SHARES ISSUE FOR CONSIDERATION OTHER THAN CASH

When a company purchase any fixed asset or business and makes the payment to the vendor in form of issue of shares in place of cash it is called the issue of shares for consideration other than cash.

Share can be issued at par, at premium or discount.

JOURNAL ENTRIES

Date	Particulars	L.F.	Debit ₹	Credit ₹
	On purchase of asset Sudry Asset Account Dr. To Vendor		Amount of purchase price	
	On purchase of business When purchase consideration is more than net asset Sundry Asset Account Dr. Goodwill Account (B/F) Dr. To Liability To Vendor		 Agreed value (Purchase consideration - Net assets)	 Agreed Value Purchase Consideration
	When purchase consideration is less than net asset Sundry Asset Account Dr.		 Agreed value	

To Liability To Vendor To Capital Reserve (B/F)			Agreed Value Purchase Consideration (Sundry asset less- purchase consideration)
On issue of share a) At PAR Vendor Dr. To Share Capital		Nominal Value	
b) At premium Vendor Dr. To Share Capital To Securities Premium		Purchase Price	 Nominal value Amount of Premium
c) Vendor Dr. Discount on issue of shares Dr. To Share Capital		Purchase Price Amount & discount	 Value & Share

NOTE : When name of vendor is given then we write the name of vendor

Example : Atlas 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 if shares

a) Issued at par

b) Issued at premium of 12%

c) Issued at discount of 10%

JOURNAL ENTRIES

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Machinery Account Dr. To HMT Ltd. To Bank Account (Being the machine purchased and Rs.10,000 paid cash and balance to be paid by issue of shares)		64,000	 54,000 10,000
	a) When shares are issued at par HMT Ltd. (Vendor) Dr.		 54,000	

	To Share Capital		54,000
	(Being 5,400 shares of Rs.10 each at par to HMT Ltd.)		
	b) When shares are issued at premium of 20%	54,000	
	HMT Ltd. (Vendor) Dr.		45,000
	To Share Capital Account		9000
	To Security Premium Account		
	(Being 4,500 shares of issued to vendor at a premium of Rs.2 per share 54,000/10+2=4500)		
	c) When shares are issued at discount of 10%		
	HMT Ltd. (Vendor)	54,000	
	Discount on issue of shares Account Dr.	600	
	To Share Capital Account Dr.		60,000
	(Being 6,000 shares issued at 10% discount to HMT Ltd.)		
	54,000/10-9=6000)		

Purchase of business example :

A company issued 15,000 fully paid up equity shares of Rs.100 each for the purchase of the following assets and liabilities from Gupta Bros..

Plant -	Rs.3,50,000	Stock	Rs.4,50,000
Land and Building	Rs.6,00,000	Sundry Creditors	Rs.1,00,000

pass necessary Journal entries

JOURNAL ENTRIES

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Plant Account	Dr.		3,50,000	
	Land and Building Account	Dr.		6,00,000	
	Stock Account	Dr.		4,50,000	
	Goodwill Account	Dr.		2,00,000	
	To sundry creditors Account				1,00,000
	To Gupta Bros.				15,00,000
	(Being the purchase of business)				
	Gupta Bros.			15,00,000	
	To Equity Shares Capital Account				15,00,000
	Being issue of 15,000 shares of Rs.100 each as payment of business price				

Calculation : Goodwill = purchase consideration + liablilities - assets = Rs.15,00,000+ Rs.1,00,000- Rs.14,00,000= Rs.2,00,000

Q. :- A company purchased a running business from Mahesh for a sum of ₹ 1,50,000 payable as Rs.1,20,000 in fully paid equity shares of Rs.10 each and balance in cash. The assets and liabilities consisted of the following

Plant and Machinery	₹ 40,000	Stock	₹ 50,000
Building	₹ 40,000	Cash	₹ 20,000
Sundry debtors	₹ 30,000	Sundry creditors	₹ 20,000

pass necessary Journal entries

JOURNAL

Date	**Particulars**	**L.F.**	**Debit ₹**	**Credit ₹**
	Plant and Machinery Account Dr.		40,000	
	Building Account Dr.		40,000	
	Sundry debtors Account Dr.		30,000	
	Stock Account Dr.		50,000	
	Cash Account Dr.		20,000	
	To Sundry creditors			20,000
	To Mahesh			1,50,000
	To Capital Reserve			10,000
	(Being the assets and liabilities taken over)			
	Mahesh Dr.		1,50,000	
	To Equity share capital Account			1,20,000
	To Bank Account			30,000
	(Being the payment made to Mahesh in form of shares			

Calculations ; Net assets = total assets - liabilities = Rs.1,800,000-Rs.20,000= Rs.1,60,000
Capital reserve = Net Asset- purchase consideration = Rs.1,60,000-Rs.1,50,000= Rs.10,000

Sweat equity Shares : [section 79 A] These are the shares which are issued by the companies to its employees or directos at a discount or for consideration other than cash for providing knowhow or intellectual property rights or value addition

These can be issued only after one year of commencement of business and is reward for their hard work.

Private placement of shares : [section 81 (1A) This is an issue of shares of securites to a relatively small selected group of persons not to the public.

This is governed by SEBI guidlines and requires special resolution to be passed in General Body meeting.

Under subscription : When the number of received is less than the number of shares offered to public it is under subscription

Oversubscription : When the number of received is more than the number of shares offered to public it is oversubscription.

In such cases we

1. Either reject the excess applications

2. make prorata allotment

3. pratially refund amount on other prorata allotment is made

Right issue : The existing share holders have a right under section 81 to subscribe for fresh capital of shares of company for consideration decided by the company in proportion to existing shareholdings. This is called right issue.

Preferential Allotment : It is way of infusing fresh capital (out of public issue) in business by issuing shares or warrants to the specified entities at specified price. These entities are those who want to have stake in company like promoters, financial institutions, venture capitalists etc.

ESCROW ACCOUNTS : Funds placed in trust with a third party by a borrower for a specific purpose and to be delivered to the borrower only upon the fulfillment of certain conditions.

Employees stock option plan (ESOP) : This is employee compensation scheme through which companies want to introduce a sense of belongingess among the employees. Under this scheme a certain number of shares are reserved for purchase and issue to key permanent employees at a price much lower than the market price. Such shares have lock in period.

Buy back of shares : The repurchase of stock by the company that issued it, as to reduce holdings of a single investor or increase the value of sahres by reducing their number

This can be done out of free reserves, security premium or proceeds of securities

Employees stock Purchase Scheme (ESPS) :

About Employee Stock Purchase Plans

Companies offer Employess Stock Purchase Plans to employees to allow them the opportunity to share the success of the firm. A stock purchase plan enables employees to purchase their company's common stock, often at a discount from the market price.

JOURNAL ENTRY

Bank account	Dr. (issue price)
Employee compensation Expenses	Dr. (accounting value of option)
To Equity Share Capital	(face value)
To securities premium	(market price-face value)

Call in arrear : 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 Company can charge interest on this

Accounting treatment

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Call-in- Arrear Account Dr. To Relevant call Account/Allotment Account (Being the call amount not received)			

	When call amount is received Bank Account Dr. To Call in Arrear Account (Being the amount of call received)			
	On making the interest due Sundry Member Account To interest on Call-in-Arrear Account (Being the amount of interest due)			
	On receipt of the interest Bank Account Dr. To Sundry Member Account (Being the amount of interest received)			
	When interest is transferred to profit and loss account Interest on Call-in-Arrear Account Dr. To Profit and Loss Account (Being the amount transferred to Profit and Loss Account)			

Calls in advance : Any amount paid in excess of what they has asked to pay is called as call in advance. Interest is received on this at rate mentioned in Article of Association or 6% as per Table A.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	On receiving money in advance Bank Account Dr. To Call-in-Advance Account (Being the amount of call received)			
	On adjustment of the advance Call-in-Advance Account Dr. To Relevant call Account (Being the amount adjusted on call becoming due)			
	On interest becoming due Interest on Call-in-Advance Account Dr. To Sundry Member Account (Being the interest due to member)			
	On payment of interest Sundry Member Account Dr. To Bank Account (Being the interest paid to member			
	When interest is transferred to Profit and loss account Profit and Loss Account Dr. To Interest on Call-in-Advance Account (Being the amount trnaferred to Proft and Loss Account)			

Forfeiture of shares : If on allotment fo share allottees fail to pay the amount on any call his money is forfeited or withheld by company this is called forfeiture of so forteit means to take away or to withdraw the rights of a person.

Forfeiture of share referes to the cancellation or termination of membership of a share holder by taking away the shares and rights of membership.

Forfeiture of shares issued at par

Accounting treatment :

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account Dr.		Amount Called	
	To Various Unpaid Calls/Calls in arrear Account			Amount unpaid
	To Forfeited Shares			Amount paid

Example : Jai Jawan holding 10 shares of Rs.10 each of which Rs.2 on application Rs.2 on allotment but could not pay Rs.3 on first call. His shares were forfeited by the Directors. Give Journal entry.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account (10x8) Dr.		80	
	To Forfeited Shares Account (10x5)			50
	To share First Call Accounts (10x3)			30
	(Being 10 shares forfeited for non-payment of call money)			

Forfeiture of shares issued at premium. For this there are two conditions

1. the premium has been received
2. the premium has not been received

when the premium has been received : In such case premium received will not be forfeited and will not come anywhere :

Accounting treatment :

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account Dr.			
	To Share Forfeited Account			
	To Share First Call Account			

Example 1000 shares of Rs.10 each issued at a premium of Rs.2 per share are forfeited on which Rs.8 (including premium) have been received. Final call of Rs.4 has not been received Pass necessary entry.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account (1,000x10) Dr.		10,000	
	To Shares Forfeited Account (1000x6)			6,000
	To Share First Call Account (1,000x4)			4,000
	(Being 1,000 shares forfeited for non payment of Final call money)			

The premium has not been received : In such case security premium is debited with the amount of premium not received

Accounting treatment :

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account Dr.			
	Security Premium Account Dr.			
	To Shares Forfeited Account			
	To Shares Unpaid Call Account)			
	(Being 1,000 shares forfeited for non payment of allotment and calls money)			

Example 1000 shares of Rs.10 each issued at a premium of Rs.2 per share are forfeited on which only application money of Rs.4 has been received and Rs.8 (including premium) has not been received. Pass necessary entries.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account (1,000x10) Dr.		10,000	
	Security Premium Account (1000x2) Dr.		2,000	
	To Share Forfeited Account (1000x4)			4000
	To Share Unpaid Call Account (1000x8)			8000
	(Being 1,000 shares forfeited for non payment of allotment and calls money			

Forfeiture of shares issued at discount

Accounting treatment :

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account Dr.			
	To Discount on issue of share Account			
	To Shares Forfeited Account			
	To Share Unpaid Call Account			

Example A Ltd. Forfeited 1000 shares of Rs.100 each issued at discount of Rs.10 per share Final call of Rs.20 has not been made on these shares. Rs.40 has been received per share Pass necessary entry.

Accounting treatment :

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account Dr.		80,000	
	To Discount on issue of share Account			10,000
	To Shares Forfeited Account			40,000
	To Share Unpaid Call Account			30,000
	(Being 1000 shares forfeited)			

Reissue of forfeited shares : forfeited shares can be issued to some investor. This is called as reissue of shares These can be issued at par, premium or discount but discount cannot exceed the forfeited amount

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	REISSUE AT PAR			
	Bank Account Dr.			
	To Share Capital Account			
	REISSUE AT PREMIUM			
	Bank Account Dr.			
	To Share Capital Account			
	To Security Premium Account			
	REISSUE AT DISCOUNT			
	Bank Account Dr.			
	Forfeitted Shares Account Dr.			
	To Share Capital Account			
	BALANCE OF FORFEITED SHARES ACCOUNT			
	Forfeited Shares Account Dr.			
	To Capital Reserve			

Forfeiture of Shares originally issued at par and reissued at a discount

Example A Ltd. Forfeited 200 shares of Rs.10 each fully called up held by X for non payment of allotment money of Rs.3 per share & Final call of Rs.4 per share. He paid the application money of Rs.3 per share. These shares were reissued to Y for Rs.8 per shares pass necessary entry.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account Dr.		2,000	
	To share Allotment Account (20x3)			600
	To Shares Final Call Account (200x4)			800
	To Shares Forfeited Account (200x3)			600
	(Being 200 shares forfeited held by X)			
	Bank Account (200x8) Dr.		1,600	
	Forfeited Shares Account (200x2) Dr.		400	
	To Share Capital Account (200x10)			2,000
	(Being re-issue of forfeited shares to Y)			
	Forfeited Shares Account Dr.		200	
	To Capital Reserve			200
	(Being the transfer of profit on reissue to Capital Reserve)			

Forfeiture of Shares originally issued at premium and reissued at a discount

Example A Ltd. Forfeited 100 shares of Rs.100 each issued at a premium of 50% to be paid at time allotment on which first call of Rs.30 per equity share was not received, final call of Rs.20 is yet to be made. These shares were reissued at Rs.70 per share at Rs.80 paid up. Pass necessary entries.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account (100x80) Dr.		8,000	
	To Shares First Call Account (100x50)			5,000
	To Shares Forfeited Account (100x30)			3,000
	(Being 100 shares forfeited for non-payment of calls money)			
	Bank Account (100x70) Dr.		7,000	
	Forfeited Shares Account (100x10) Dr.		1,000	
	To Share Capital Account (100x80)			8,000
	(Being re-issue 100 forfeited shares at Rs.70 per share at Rs.80 paid up)			
	Forfeited Shares Account Dr.		4,000	
	To Capital Reserve			4,000
	(Being the transfer of profit on reissue to Capital Reserve)			

Forfeiture of Shares originally issued at discount and reissued at a premium

Y Ltd. Forfeited 800 equity shares of Rs.100 each issued at a discount of 10% for non-payment of first and final call of Rs.3 per share. The forfeited shares were reissued at Rs.12 per share as fully paid up. Pass necessary journal entries in the books of company.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Share Capital Account (800x100)		80,000	
	To Discount on issue of Shares Account (800x10)			8,000
	To Shares and Final Call Account (800x3)			2,400
	To Shares Forfeited Account			69,600
	(Being 800 shares forfeited for non-payment of final call money			
	Bank Account (800x12 Dr.		9,600	
	Shares Forfeited Account (100x10) Dr.		62,400	
	Discount on issue of Shares Account Dr.		8,000	
	To Share Capital Account (100x80)			
	(Being re-issue 800 forfeited shares at Rs.12 per share at fully paid up paid up			
	Forfeited Shares Account Dr.		4,000	
	To Capital Reserve			4,000
	(Being the transfer of profit on reissue to Capital Reserve)			

PRO-RATA-ALLOTMENT When there is oversubscription of shares either the excess amount is refunded or proportionate shares are allotted. Allotment of proportionate shares is called as Pro-Rata Allotment.

Example : AB Ltd. Invited applications for 1,00,000 Equity shares Rs.10 each payable as Rs.2 on application, Rs.3 on Allotment and the balance on first and final call. Application were received for 3,00,000 shares and shares were allotted on pro-rata basis. The excess application money was to be adjusted against allotment only. M a shareholder who has applied for 3,000 shares failed to pay the call money and his shares were forfeited and re-issued at Rs.8 per share as fully paid. Pass journal entries.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr		6,00,000	
	To Equity Share Application Account			6,00,000
	(Being the application money received on 3,00,000 shares at Rs.2 per share)			
	Equity Share Application Account Dr		6,00,000	

	To Equity Share Capital Account To Equity Share Allotment Account To Bank Account (Being the amount of application money adjusted in t share capital allotment and balance refunded			2,00,000 3,00,000 1,00,000
	Equity Share Allotment Account Dr. To Share Equity Capital Account (Being the amount due for allotment)		3,00,000	3,00,000
	Equity Share First & Final Call AccountDr. To Share Capital A/c (Being the amount due for final call)		5,00,000	5,00,000
	Bank Account Dr. To Equity Share First & Final Call Account (Being the receipt of Rs.5 on 99,000 shares)		4,95,000	4,95,000
	Equity Share Capital Account (100x10) Dr. To Shares First & Final Call Account (100x50) To Shares Forfeited Account (1000x50) (Being 1000 shares forfeited for non-payment of first and final call money		10,000	5,000 5,000
	Bank Account (1000x8) Dr. Shares Forfeited Account (1000x2) Dr. To Share Capital Account (100x10) (Being re-issue 1000 forfeited shares at Rs.8 per share at Rs.10 paid up)		8,000 2,000	10,000
	Forfeited Shares Account Dr. To Capital Reserve (Being the transfer of profit on reissue to Capital Reserve)		3,000	3,000

Note there is no bank account after allotment as all due money is already received

When cash book is also prepared then Bank account entries are not passed in journal but are passed only is cash book

For example AB Ltd. Invited application for 1,00,000 Equity shares Rs.10 each payable as Rs.2 on application, Rs.3 on Allotment and the balance on first and final call. Applications were received for 3,00,000 shares and shares were allotted on pro-rata basis. The excess application money was to be adjusted against allotment only. M a sharehodler who has applied for 3,000 shares failed to pay the call money and his shares were forfeited and re-issued at Rs.8 per share as fully paid. Pass journal entries.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Equity Share Application Account Dr.		5,00,000	
	To Equity Share Capital Account			2,00,000
	To Equity Share Allotment Account			3,00,000
	(Being the amount of application money adjusted in t share capital allotment and balance refunded			
	Equity Share Allotment Account Dr.		3,00,000	
	To Share Equity Capital Account			3,00,000
	(Being the amount due for allotment)			
	Equity Share First & Final Call AccountDr.		5,00,000	
	To Share Capital A/c			5,00,000
	(Being the amount due for final call			
	Equity Share Capital Account (1000x10) Dr.		10,000	
	To Shares First & Final Call Account (100x50)			5000
	To Shares Forfeited Account (1000x5)			5000
	(Being 1000 shares forfeited for non-payment			
	Forfeited Shares Account Dr.		3,000	
	To Capital Reserve			3,000
	(Being the transfer of profit on reissue to Capital Reserve)			

CASH BOOK (BANK COLUMN ONLY)

Particulars	Rs.	Particulars	Rs.
To Share application account	5,00,000	By Share application account	1,00,000
To Share allotment account	Nil	By balance c/d	9,03,000
To Share call account	4,95,000		
	8,000		
	10,03,000		10,03,000

CHAPTER 8

Accounting for Debentures

DEBENTURES :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. In some countries the term is used interchangeably with bond, loan stock or note. A debenture is thus like a **certificate of loan** or a loan bond evidencing the fact that the company is liable to pay a specified amount with interest and although the money raised by the debentures becomes a part of the company's capital structure, it does not become share capital.

Note : Debenture is instrument that is not secured by physical asset or collateral

In case of bond interest is not declared.

Debentures are generally freely transferable by the debenture holder. Debenture holders have no rights to vote in the company's general meetings of shareholders,The interest paid to them is a charge against profit in the company's financial statements.

Types of debentures

Convertibility point of view : there are two types of debentures:

Convertible debentures, which are can be converted into equity shares of the issuing company after a predetermined period of time.

These may be Partly Convertible Debentures (PCD): A part of these instruments are converted into Equity shares in the future at notice of the issuer. The issuer decides the ratio for conversion. This is normally **decided at the time of subscription.**

· Fully convertible Debentures (FCD): These are fully convertible into Equity shares at the issuer's notice. The ratio of conversion is decided by the issuer. Upon conversion the investors enjoy the same status as ordinary shareholders of the company.

Non-convertible debentures, which are simply regular debentures, cannot be converted into equity shares of the liable company. They are debentures without the convertibility feature, they usually carry higher interest rates than their convertible counterparts.

On basis of Security, debentures are classified into:·

Secured Debentures: These instruments are secured by a charge on the fixed assets of the issuer company. So if the issuer fails on payment of either the principal or interest amount, his assets can be sold to repay the liability to the investors

Unsecured Debentures: These instrument are unsecured in the sense that if the issuer defaults on payment of the interest or principal amount, the investor is treated like along other unsecured creditors of the company .

From redemption point of view

Redeemable Debentures:- Redeemable debentures are those which are redeemed or paid off after the termination of fixed term. The amount paid off includes the principal amount and the current year's interest. The company always has the option of either to redeem a specific number of debentures each year or redeem all the debentures at specified date.

Irredeemable or Perpetual Debentures:- Irredeemable debentures are those debentures which do not have any fixed date of redemption. They are redeemed either in the event of winding up or at a very remote period of time. Irredeemable or perpetual debenture holders

can never force the company to redeem their debentures.

Issue of Debentures :

Debentures can be issued in two ways

1 . for cash

2. for consideration other than cash

3. As collateral security

Terms of issue of: Debentures can be issued in two ways

1 .Issue of Debentures at Par

2. Issue of Debentures at Premium

Debentures payable in Instalments

1. First instalment paid along with application is called as application money

2. Second instalment paid on allotment is called as allotment money

3. Subsequent instalments paid are called as call money calls can be more than one and called First call, second call or as the case may be ISSUE OF Debentures FOR CASH AT PAR : This means shares are issued at face value

JOURNAL ENTRIES

On receipt of application	Bank Account Dr. To Debenture Application Account	With the application money received
On acceptance of application	Debenture Application Account Dr. To Debenture Account	With the amount of of application money on allotted debentures
On making allotment money due	Debenture Allotment Account Dr. To Debenture Account	With the amount due on allotment of debentures
On adjustment of excess debenture application money	Debenture Application Acccount Dr. To Bank Account	With the surplus money on rejectedshares
On receipt of allotment money	Bank Account Dr. To Debenture Allotment Account	With the amount actually received
On making calls	Debenture Call Account Dr. To Debenture Account	With the amount due on particular call of debentures
On receipt of call money	Bank Account	With the amount actually received

Issue of Debenture at par : This means Debentures are issued at face value

Example

Raj Ltd. Issued 2,000 12% Debentures of Rs.100 each at par payable Rs.25 on Application, Rs.50 on Allotment and the balance on first and final call. In all 3,000 application were received. Allotment was made to 2,000 applicants others were rejected. Give Journal entries.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr.		75,000	
	To 12% Debenture Application Account			75,000
	(Being the application money received on 3,000 debentures @Rs.25 per debenture)			
	12% Debenture Application Account Dr.		75,000	
	To 12% Debenture Account			50,000
	To Bank Account			25,000
	(Being the transfer of application money to debenture account and refund made on rejedected Applications)			
	12% Debenture Allotment Account Dr.		1,00,000	
	To 12% Debenture Account			1,00,000
	(Being the allotment money due on 2,000 debentures @Rs.50)			
	Bank Account Dr.		1,00,000	
	To 12% Debenture Allotment Account			1,00,000
	(Being the application money received)			
	12% Debenture First & Final Call Account Dr.		50,000	
	To 12% Debenture Account			50,000
	(Being the call money due on 2,000 debentures @ Rs.25)			
	Bank Account Dr.		50,000	
	To 12% Debentur First & Call Account			50,000
	(Being the application money received)			

Importan : If % of debenture is given then it must be written along with Debenture

ISSUE OF DEBENTURES AT PREMIUM : It is issue of Debenture at more than face value

Note : Premium is Presumed To be Demanded on Allotment Unless Specified and Credited to Securities Premium Account

Example Z Ltd. Invited applications for 5,000, 8% Debentures of Rs.100 each at a premium of 2%, Rs.40 were payable on Application and balance an allotment. Applications were received for 4,800 shares and accepted in full. All money duly received. Journalise the transactions.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr.		1,92,000	
	To Debenture Application Account			1,92,000
	(Being the application money received on 4800 debentures @Rs.40 per debenture)			
	8% Debenture Application Account Dr.		1,92,000	
	To Debenture Account			1,92,000
	(Being the transfer of application money to 8% debenture account)			
	12% Debenture Allotment Account Dr.		2,97,600	
	To 8% Debenture Account			288000
	To Security Premium Account			9600
	(Being the allotment money due on 4,800 debentures @Rs.60 and premium of Rs.2 share)			
	Bank Account Dr.		2,97,600	
	To Debenture Allotment Account			2,97,600
	(Being the application money received)			

Oversubscription of debentures : In such case excess application are rejected or partial or Pro-rata allotment is done or combination of both is carried on.

Ganga Ltd. issued 2,000 debentures of Rs.100 each at a premium of 10% payable Rs.25 on application Rs.40 (including premium) payable on allotment and balance on First and final Call. In all 3,500 application were received 500 application were rejected and allotment was made to applicants of 3,000 debentures on Pro-rata basis. The excess money was adjusted on allotment. Give journal entries.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr.		87,500	
	To 12% Debenture Application Account			87,500
	(Being the application money received on 3,500 debentures @Rs.25 per debenture)			
	12% Debenture Application Account Dr.		87,500	
	To 12% Debenture Account			50,000
	To Bank Account			12,500
	To Debenture Allotment Account			25,000
	(Being the transfer of application money to debentureaccountand refund made on rejected Applications)			

	12% Debenture Allotment Account Dr. To 12% Debenture Account To Security Premium Account (Being the allotment money due on 2,000 debentures @Rs.30 and premium of Rs.10)		80,000	 60,000 20,000
	Bank Account Dr. To 12% Debenture Allotment Account (Being the application money received Rs.80,000-Rs.25,000)		55,000	 55,000
	12% Debenture First & Final Call Account Dr. To 12% Debenture Account (Being the call money due on 2,000 debentures @Rs.45)		90,000	 90,000
	Bank Account Dr. To 12% Debenture First & Call Account (Being the application money received)		90,000	 90,000

Issue of debentures for consideration other than cash

When Debentures are issued for purchase of asset

When Debentures are issued for purchase of asset at par	Sundry Asset Account Dr. To Vendor	With the purchase consideration
	Vendor Dr. To Debenture Account	
When Debentures are issued for purchase of asset at premium	Sundry Assets Account Dr. To Vendor	With the purchase Consideration
	Vendor Dr. To Debenture Account To Security Premium Account	 No. of debentures x par value No. of debentures x premium
When business is purchased and debentures issued	When Purchase consideration is equal to net value of assets Sundry Assets Account Dr. To Sundry Liabilities Account To Vendor	 Value of asset Value of liability Purchase consideration
	When Purchase consideration more than net value of assets Sundry Asset Account Dr. Goodwill account Dr. To Sundry Liabilities Account	 Value of asset Excess of purchase value

	To Vendor When Purchase consideration is less than net value of asset Sundry Assets Account Dr To Sundry Liabilities Account To Capital Reserve To Vendor	Purchase Consideration Value of asset Value of liability Excess liabilitiy Purchase consideration

Example : A company purchased assets of book value of Rs.99,000 from Girish. I t was agreed that Purchase consideration be paid by issuing 11% Debentures of Rs.100 each. Assume Debentures have been issued (i) at par (ii) at a premium of 10%.

Give Journal

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Sundry Assets Account	Dr.		99,000	
	To Girish				99,000
	(for assets purchase)				
(i)	Debentures are issued at par				
	Girish	Dr.			
	To 11% Debentures			99,000	
	(For the issue of debenture at par)				99,000
(ii)	Debentures are issued at premium				
	Girish	Dr.			
	To 11% Debentures			99,000	
	To Security Premium Account				90,000
	For issue of 900 debentures of Rs.100 each at 10% premium)				9,000

When Purchase consideration is more than net value of assets

A company issued debentures of Rs.100 each at par for the purchase of the following assets and liabilities from Gupta Bros. at purchase consideration of Rs.15,00,000

Plant-	Rs.3,50,000	Stock	Rs.4,50,000
Land and Building	Rs.6,00,000	Sundry Creditors	Rs.1,00,000

pass necessary Journal entries

JOURNAL

Date	Particulars		L.F.	Debit ₹	Credit ₹
	Plant Account	Dr.		3,50,000	
	Land and Building Account	Dr.		6,00,000	
	Stock Account	Dr.		4,50,000	

	Goodwill Account Dr. To Sundry creditors Account To Gupta Bros. (Being the purchase of business)	2,00,000	 1,00,000 15,00,000
	Gupta Bros To Debenture Account (Being issue of 15,000 shares of Rs.100 each as payment of business price)	 15,00,000	 15,00,000

Calculation : Goodwill = purchase consideration+liabilities

assets = Rs.15,00,000+Rs.1,00,000-Rs.14,00,000 =Rs.1,00,000

When Purchase consideration is less than net value of assets

Zee Ltd. Took over the following assets and liabilities of business of Usha Ltd.

ASSETS : Machinery-Rs.1,00,000, Furniture Rs.1,80,000 Stock-Rs.20,000

Liabilities - Creditors Rs.80,000

The purchase price was agreed at Rs.1,08,000. This is to settle by issue of 12% Debentures at premium of 20% pass necessary Journal entries.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Machine Account Dr. Furniture Account Dr. Stock Account Dr. To Creditors Account To Capital Reserve To Usha Co. Ltd. (Being the purchase of business)		1,00,000 1,80,00 20,000	 80,000 1,12,000 1,08,000
	Usha Co. Ltd. To 12% Debenture Account To Security Premium Account Being issue of 900 debentures of Rs.100 each at premium of 20%)			

Calculations ; Net assets = total assets-liabilities = Rs.3,00,000-Rs.80,000=Rs.2,20,000

Capital reserve = Net assets - purchase consideration = Rs.2,20,000-Rs.1,08,000 = Rs.1,12,000

Collateral security means security provided to lenderin 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 loan amount and the principal security is exhausted. In case the need to excercise the right dose 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. This is used when there are no assets to mortgage.

In the accounting books of the company issue of debentues as collateral security can be credited in two ways.

(i) First method : 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

(ii) on the liability side of the balance sheet under the heading Secured Loans and Advances.

Liabilities	Rs.	Assets	Rs.
Secured Loans Bank Loan (Secured by issue of % Debentures as collateral security)			

(ii) Entry to be made in the books of account the company

A journal entry is made on the issue of debentures as a collateral security, Debentures suspense Account is debited because no cash is reeived for such issue

Following journal entry will be made

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Debenture Suspense Account Dr To Debentrues Account (Being the issue of Debentues of Rs.... each issued as collateral security)			

It is represented in Balance Sheet

Balance Sheet as on

Liabilities	Rs.	Assets	Rs.
Secured Loans Debenture issued as collateral security Loan from the Banks		Miscellaneous Expenditure Debenture Suspense Account	

Example : A company took a loan of Rs.3,80,000 from Vaish Cooperative Bank Ltd. and issued 13% debentures of Rs.4,00,000 as a collateral security. Explain how will you deal with the issue of debentrues in the books of the company.

Solution :

Method No. 1

BALANCE SHEET

Liabilities	Rs.	Assets	Rs.
Capital Reserve and Surplus **SECURED LOANS** Debentures (In addition .... 4,000 Debentures of each issued as collateral security) Loan from Vaish Co-Op Bank (secured by the issue of 4,000 debentures of Rs.100 each issued as collateral security)	4,00,000		

Method No. 2

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Debenture Suspense Account Dr.		4,00,000	
	To 13% Debenture Account			4,00,000
	(Being the issue of 4,000 Debenture of Rs.100 each issued as collateral security)			

BALANCE SHEET (EXTRACT)

Liabilities	Rs.	Assets	Rs.
SECURED LOANS 4,000, 13% Debentures 100 each (issued as collateral security)	4,00,000	Miscellaneous Expenditure Debentures Suspense Al	4,00,000
Loan from Vaish Co-Op Bank (secured by the issue of 4,000 debentures of Rs.100 each issued as collateral security)	3,80,000		

Various cases from the point of view : Various terms of issue and redemption are

Case No.	Condition of issue	Condition of redemption
1.	Issued at par	Redemption at par
2.	Issued at premium	Redemption at par
3.	Issued at par	Redemption at premium
4.	Issued at premium	Redemption at premium

When Debentures are issued at par and redeemable at par

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr.			
	To % Debenture Application Account			
	(Being the application money received			
	Debenture Application Account Dr.			
	to % Debenture Account			
	(Being the transfer of application money to debenture account)			

Example : Larsen and Tourbo Ltd. Issued 50,000 8% debentures of Rs.100 each payable on application at par and redeemable at par any time after 7 years from the date of the issue Record necessary entries for the issue of debentures in the book of Company.

Solution : Books of Larsen & Turbo Ltd. Issued 50,000 8% debentures of Rs.100 each payable on application at par and redeemable at par any time after 7 years from the date of the issue Record necessary entries for the issue of debentures in the book of Company.

Solution : Books of Larsen & Toubro Ltd.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr.		50,00,000	
	To % Debenture Application Account			50,00,000
	(Being the application money received)			
	Debenture Application Account Dr.		50,00,000	
	To % Debentures Account			50,00,000
	(Being the transfer of application money to debenture account)			

When Debentures are issued at premium redeemable at par

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr.			
	To% Debenture Application Account			
	(Being the application money received)			
	Debenture Application Account Dr.			
	To % Debenture Account			
	To Security Premium Account			
	(Being the debenture issued at premium and redemable at par			

Example : Green Ltd. Issued Rs.80,000, 9% Debenture at a premium of 5% redeemable at par Give the necessary Journal entry.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr. To % Debenture Application Account (Being the application money received)		84,000	 84,000
	Debenture Application Account Dr. To % Debenture Account To Security Premium Account (Being the debenture issued at premium and redeemable at par)		84,000	 80,000 4,000

When Debentures are issued at par redeemable at premium

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr. To % Debenture Application Account (Being the application money received)			
	Debenture Application Account Dr. Loss on issue of Debenture Account Dr. To % Debenture Account To Security Premium Account (Being the debenture issued at premium and redeemable at par)			

Example : White Ltd. Issued Rs.60,000, 9% Debenture at par & redeemable at 10% premium. Give the necessary Journal entry.

JOURNAL

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr. To % Debenture Application Account (Being the application money received)		60,000	 60,000
	Debenture Application Account Dr. Loss on issue of Debenture Account Dr. To % Debenture Account To Security Premium Account (Being the debenture issued at premium and redeemable at par)		60,000 6,000	 60,000 6,000

When Debentures are issued at Premium redeemable at premium

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr. To % Debenture Application Account (Being the application money received) Debenture Application Account Dr. Loss on issue of Debenture Account Dr. To % Debenture Account To Premium on Redemption of Debenture account (Being the debenture issued at premium and redeemable at premium)			

Example : Give Journal Entry assuming the face value of 10% debenturesat Rs.100 issued at Rs.105 and repayable at Rs.110.

Date	Particulars	L.F.	Debit ₹	Credit ₹
	Bank Account Dr. To % Debenture Application Account (Being the application money received)		105	 105
	Debenture Application Account Dr. Loss on issue of Debenture Account Dr. To % Debenture Account To Security Premium Account To Premium on Redemption of Debenture account (Being the debenture issued at 5% premium and redeemable at 10% premium)		105 10	 100 5 10

WRITING OFF LOSS ON ISSUE OF DEBENTURES

The loss on issue of debentures is fictitious asset and shown on assets side of Balance Sheet and should be written off as soon as possible by debiting profit and loss account

Profit and Loss Account Dr.

To Loss on issue of Debentures A/c

WRITING OFF LOSS ON ISSUE OF DEBENTURES

First Method : When debentues are redeemed after fixed period here loss is spread equally over life of debenture therefore called equal instalment method.

Example : A limited company has issed Rs.1,00,000 9% debentures at a discount of 6% 1st Jan 2000. These debenture are to be redeemed equally over 3 years starting from the end of 1st year show discount on issue account for 3 years

Loss on issue of Debentures Account = Amount x rate/100 = 1,00,000x6/100

= Rs.6.

		Rs.			Rs.
1.1.2000	To 9% Debenture Account	6,000	31.12.2001	By Profit Loss Account	2,400
				By Balance c/d	3,600
		6,000			6,000
1.1.2001	To Balance b/d	3,600	31.12.2001	By Profit & Loss Account	1,800
				By Balance c/d	1,800
		3,600			3,600
1.1.2002	To Balance b/d	1,800	31.12.2002	By Profit & Loss Account	1,200
		1,800			1,800
1.1.2003	To Balance b/d	600	31.12.2003	By Profit & Loss Account	600

Proportion Method or variable instalment method : In this method loss on issue of debenture is written off each year in proportion to amount of debenture which reduces with every instalment paid

Example : A limited company has issued Rs.1,00,000 9% debentures at a discount of 6% 1st Jan 2000. These debenture are to be redeemed in equal instalments over 4 years starting from the end of 1st year show discount on issue account for 4 years.

Loss on issue of Debentures Account = Amount x rate/100= 1,00,000x6/100 = Rs.6,000

Year	Outstanding Debentures	Ratios	Amount of Loss to be written off
Ist	1,00,000		Rs.6,000x4/10=Rs.2,400
2nd	75,000	3	Rs.6000x 3 = Rs.1,800
3rd	50,000	2	Rs.6000x2/10=Rs.1,200
4th	25,000	1	Rs.6000x1/10 = Rs.600

Discount on issue of Debenture Account

		Rs.			Rs.
1.1.2000	To 9% Debenture Account	6,000	31.12.2000	By Profit & Loss Account	2,000
				By Balance c/d	4,000
		6,000			**6,000**
1.1.2001	To Balance b/d	4,000		By Profit & Loss Account	2,000
1.1.2002	To Balance b/d	**4,000**			**4,000**
		2,000		By Profit & Loss Account	2,000

Interest on Debentures :

Interest on Debentures is calculated at a final eate on its face value and is usually payable half yearly & is paid even company is suffering from loss because it is charge on profit.

Incoem Tax is deducted from interest before payment to debenture holders

Journal Entries

(1) When Interest is Due

Debenture's interest A/c Dr (Green Interest)
To Debenture holder A/c (Net interest)
To Income Tax Payable A/c (Income Tax deducted)

(2) When interest is paid

Debenture holder A/c Dr (With interest)
To Bank A/c

(3) On payment of Income Tax to Garenment

Income Tax payable at Dr
To Bank A/c (Amount of Income tax deducted at source)

(4) On transfer of interest on debenture to Profit & loss Account

Profit & Loss A/c Dr.
To Debenture interest A/c (amount of interest)

Illustration :

ABC Company Ltd., had 6% debentures of Rs.1,00,000 on 1st January 2009 on which interest is paid on 30th June and 31st December pass necessary journal entries for the payment of interest for the year 2009, 10% tax is deducted at source from interest and remitted immediately. Books are closed on 31st December.

Date	**Particulars**		**L.F.**	**Debit ₹**	**Credit ₹**
June 30 2009	Interest on Debenture A/c	Dr.		3,000	
	To Interest Account A/c				2,700
	To Income Tax				300
	Interest Accrued Tax Payable				
June 30	Interest Accrued A/c	Dr.		2,700	

2009	Tax Payable A/c		300	
	To Bank			3,000
	(Interest & tax paid)			
Dec.31	Interest on Debenture A/c Dr.		3,000	
2009	To Interest Accrued			2,700
	To Tax Payable			300
Dec. 31	Interest Accrued Dr.		2,700	
2009	Tax Payable A/c Dr.		300	
	To Bank			3000
	(Interest & tax paid)			
Dec.31	Profit & Loss Account Dr.		6,000	
	To Interest on Debenture A/c			6,000
	(Interest transfered to P&L Account)			

Insert on Debentures :

Insert on Debentures is calculated at a fixed rate on its face value and is usually payable half yearly is paid even company is suffering from loss becuase it is change on profit. Income Tax is deducted from interest before payment to debenture holders

JOURNAL ENTRIES

(1) When Interest is Due

Debenture's interest A/c Dr. (Gross Interest)
 To Debenture holder A/c (Net Interest)
 To Income Tax Payable A/c (Income Tax deducted)

(2) When Interest is paid

Debenture holder A/c Dr. (With interest)
 To Bank A/c

(3) On payment of Income Tax to Government

Income Tax Payable A/c Dr.
 To Bank A/c (Amount of Income Tax deducted at source)

(4) On transfer of interest on debenture to profit and loss Account

Profit & Loss A/c Dr.
 To Debenture interest A/c (Amount of Interest)

Illustration

ABC Company Ltd., had 6% debentures of Rs.1,00,000 on 1st January 2009 on which interest is paid on 30th June and 31st December. Pass necessary journal entries for the payment of interest for the year 2009. 10% tax is deducted at source from interest and remitted immediately. Books are closed on 31st December.

ABC Ltd.
JOURNAL

Date	Particulars	L.F.	Dr. Amount	Cr.Amount
June 30 2009	Interest on Debenture A/c Dr.		3,000	
	To Interest Account A/c			2,700
	To Income Tax			300
	(Interest Accued less Tax Payable)			
June 30	Interest Accrued A/c Dr.		2,700	
	Tax Payable A/c Dr.		3,00	
	To Bank			3,000
	(Interest & Tax paid)			
Dec.31	Interest on Debenture A/c Dr.		3,000	
	To Interest Accrual			2,700
	To Tax Payable			300
Dec.31	Interest Accrual Dr.		2,700	
	Tax Payable A/c Dr.		300	
	To Bank			3000
	(Interest & Tax Paid)			
Dec.31	Profit and Loss Account Dr.		6,000	
	To Interest on Debenture A/c			6,000
	(Interest Transfered to P & L Account)			

(1) When Interest is Due

Debenture's interest A/c Dr (Green Interest)
To Debenture holder A/c (Net interest)
To Income Tax Payable A/c (Income Tax deducted)

(2) When interest is paid

Debenture holder A/c Dr (With interest)
To Bank A/c

(3) On payment of Income Tax to Garenment

Income Tax payable at Dr
To Bank A/c (Amount of Income tax deducted at source)

(4) On transfer of interest on debenture to Profit & loss Account

Profit & Loss A/c Dr.
To Debenture interest A/c (amount of interest)

CHAPTER 9

Redemption of Debenture

Meaning : Redemption of debentures means repayment of the due amount of debentures to the debenture holders. It may be at par or at premium.

Time of redemption : **(a) At maturity :** when repayment is made at the date of maturity of debentures which is determined at the time of issue of debentures.

(b) Before maturity : If articles of association and terms of issue mentioned in prospectus allows, then a company can redeem its debentures before maturity date.

Redemption methods : **(1) Redemption is Lump-sum :-** When redemption is made at the expiry of a specific period, as per the terms of issue.

(2) Redemtion by draw of lots :- In this method a certain proportion of debentures are redeem each year, the debenture for which repayment is to be made is selected by draw.

(3) Redemtion by purchase in open market :- if articles of association of a company authorize, it may purchase its own debentures from open market i.e. stock exchange.

Advantage of this method : 1. When market price of own debentures is low than the redeemable value.

2. Decrease the amount of interest payable to outsiders.

3. if term of issue is provided that debentures are to be redeemed at premium then such premium can be decrease.

Sometimes company can purchase the debentures at more than the redeemable value due to the following reasons :

1. To maintain the solvency ratio.

2. To utlize the surplus money or funds which are lying idle with the company.

3. When rate of interest on debentures is more than the current market rate of interest on debentures in the industry.

4. Redemption by conversion : As per the terms of issue, convertible debentures may be covert into shares or new debentures at the option of debenture holders. This option of conversion is given to the debentureholder within specific period. In this case no need to transfer profit to Debenture Redemption Reserve Account.

Sources of Redemption of debentures.

1. Proceeds from fresh issue of share capital or debenture holders.

2. From accumulated profits.

3. Proceeds from sale of fixed assets.

4. A company may purchases its own debentures out of its surplus funds.

Two terms which are used in the redemption of debentures :

1. Redemption out of capital : when a company not used its reserve or accumulated profit for redemption of its debentures. It is called redemption out of capital. So company using this method are not transfer it profit to DRR A/c. But as per SEBI guidelines it is necessary for a company to transfer 50% amount of nominal value of debentures to be redeemed in DRR A/c before redemption of debentures commence.

2. Redemption out of profit : Redemption out of profit means that adequate amount of profits are transferred to DRR A/c from P&L Appropriation A/c before the redemption of debenture commences. This reduce the amount available for dividends to shareholders.

NOTE : If it is mentioned in question that redemption is out of capital then DRR should also created with 50% of the nominal value of debentures.
If it is mentioned that redemption is out of profit then DRR should be created with the 100% of the nominal value of debentures.
If nothing is mention about the source of redemption than as per SEBI guidelines 50% of nominal value of debentures is to be transferred to DRR A/c.
If in any particular question DRR is already existed with more than 50% amount of nominal value of debentures, then in this case total 100% of nominal value of debentures is to be transferred to DRR A/c

Debenture Redemption Reserve : Debenture redemption reserve is a reserve representing retentions out of profit made for the purpose of redemption of debentures.

Amount of DRR to be created : Section 117 (c) of the Indian Companies Act 1956 requires that, an adequate amount of profit should be transferred to DRR before redemption commences. However the adequate amount is not specified by the companies Act.

SEBI has issued guidlines for the redemption of debentures whereby :

1. An amount equivalent to 50% of the amount of debentures issue must be transferred to DRR before redemption of debentures commences.

This provision is applicable for non-convertible debentures or non-convertible part of party convertible debentures.

After all the debentures are redeemed, this account is closed by transferring to general reserve account.

Exception to the creation of DRR as per SEBI guidlines :

1. All infrastructure companies, wholly engaged in the business related to development maintenance and operation of infrastructure facilities.
2. A company issuing debentures maturity period of not more than 18 months.
3. Debentures issued by Banking Companies.
4. Companies issuing privately placed debentures.

The above types of companies are exempted by SEBI from creating DRR. However the above types of companies can create DRR(at it option) for the redemption of debentures.

Redemption method : **(1) Redemption in Lump-sum**

(A) Redemption at Par : **Illustration 1.** X Ltd. Redeemed its 10,000 10% Debentures of Rs.10 each at par on 31st March, 2011.

X Ltd.

Date	**Particulars**	**Debit ₹**	**Credit ₹**
2011 March,31	Profit & Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being transfer of Profit to Deb. Red Reserve A/c)	50,000	 50,000

March,31	10% Debentures A/c Dr. To Debentureholders A/c (Being the amount due to debenture holders)	1,00,000	 1,00,000
March,31	Debenture holders A/c Dr. To Bank A/c (Being the amount paid to the debanture holder	1,00,000	 1,00,000
March,31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being Deb. Red. Reserve A/c closed by transfer to General Reserve)	50,000	 50,000

(B) Redemption At Premium : Illustration 2. Z Ltd. Redeemed its 1,00,000 10% Debentures of Rs.10 each at 5% premium on 31st March, 2011.

Z Ltd.

Date	**Particulars**	**Debit** ₹	**Credit** ₹
2011 March, 31	Profit & Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being Profit transfer to DRR A/c	5,00,000	 5,00,000
March,31	10% Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders A/c (Being the amount due to debenture holders	1,00,000 50,000	 10,50,000
March,31	Debentureholders A/c Dr. To Bank A/c (Being the amount to the debenture holders)	10,50,000	 10,50,000
March,31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being Deb. Red Reserve A/c closed by transfer to General Reserve A/c)	5,00,000	 5,00,000

Illust. 3 : Rajesh Export Ltd. has 2,000, 9% Debentures of Rs.100 each due on redemption on 31st March 2011. Debentures redemption reserve has a balance of Rs.30,000 on that date. Record the necessary journal entries at the time of redemption of debentures.

Date	**Rajesh Export Ltd.** **Particulars**	**Debit** ₹	**Credit** ₹
2011 March, 31	Profit & Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c	70,000	 70,000
March, 31	(Being the profit transfer to DRR A/c) 10% Debentures A/c Dr. To Debentureholder a/c (Being the amount due to debanture holders)	2,00,000	 2,00,000

March, 31	Debentureholders A/c Dr. To Bank A/c (Being the amount paid to the debenture holders)	2,00,000	2,00,000
March, 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being Deb. Red Resource A/c closed by transfer General Reserve a/c)	1,00,000	1,00,000

Illust. 4 : Rahul Ltd. has 50,000, 9% Debentures of Rs.50 each due on redemption on 31st March 2011. Debentures redemption reserve has a balance of Rs.15,00,000 on that date. Record the necessary journal entries at the time of redemption of debentures.

Rajesh Export Ltd.

Date	Particulars	Debit ₹	Credit ₹
2011 March, 31	Profit & Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being the Profit transfer DR A/c)	10,00,000	10,00,000
March, 31	10% Debentures A/c Dr. To Debentureholder a/c (Being the amount due to debanture holders)	25,00,000	25,00,000
March, 31	Debentureholder A/c Dr. To Bank A/c (Being the amount paid to the debenture holders)	25,00,000	25,00,000
March, 31	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being Debenture Redemption Reserve A/c transferred to Gen. Reserved A/c)	25,00,000	25,00,000

Note : In this case DRR is Already more than 50% of nominal value of debentures, then it is created upto the 100% of the nominal value of debenture

Illust.5 : Saket Ltd.(an infrastructure co.) has outstanding 10,000, 9% Debentues of Rs.50 each due on redemption on 31st March, 2011. Record the necessary journal entries at the time of redemption of debentures.

Rajesh Export Ltd.

Date	Particulars	Debit ₹	Credit ₹
2011 31st March,	Profit & Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being the profit transferred to DRR A/c)	2,50,000	2,50,000
31st March	10% Debentures A/c Dr. To Debentureholders A/c	5,00,000	5,00,000

	(Being the amount due to debenture holders)		
31st March	Debentureholders A/c Dr.	5,00,000	
	To Bank A/c		5,00,000
	(Being the amount paid to the debenture holders		
31st	Debenture Redemption Reserve A/c Dr,	2,50,000	
	To General Reserve A/c		2,50,000
	(Being Deb. Red. Res. A/c transferred to Gen. Reserve A/c)		

(Note : The infrastructure Companies are exempted from creating DRR as per SEBI guidlines. However these companies may create DRR at its option.)

Redemption Method : 2 Draw of lots

Illustration 6 : S Ltd. redeemed its Rs.10,000, 8% Debentures out of capital by drawing a Lot on 30 Nov.2011 Journalise.

S Ltd.

Date	**Particulars**	**Debit ₹**	**Credit ₹**
2011 30th Nov.	Profit & Loss Appropriation A/c Dr.	5,000	
	To Debenture Redemption Reserve A/c		5,000
	(Being the Profit transfed to DRR A/c)		
30th Nov.	10% Debenture A/c Dr.	10,000	
	To Debenture holders A/c		10,000
	(Being the amount due to debenture holders)		
30th Nov.	Debenture holders A/c Dr.	10,000	
	To Bank A/c		10,000
	(Being the amount due to debenture holders)		

(Note : the DRR Balance will be transferreed to General Reserve after all the debentures are redeemed)

Illustration 7 : Y Ltd. redeemed its Rs.20,000, 9% debentures out of profit by drawing of lot on 30th Nov. 2011. Journalise.

Y Ltd.

Date	**Particulars**	**Debit ₹**	**Credit ₹**
2011	Profit & Loss Appropriation A/c Dr.	20,000	
30th Nov.	To Debenture Redemption Reserve A/c		20,000
	(Being the Profit transferred to DRR A/c)		
30th	10% Debentures A/c Dr.	20,000	
Nov.	To Debentureholders A/c		20,000
	(Being the Profit transferred to DRR A/c)		
30th	Debentureholder A/c Dr.	20,000	
Nov.	To Bank A/c		20,000
	(Being the amount paid to Debentured)		

(Note : the DRR Balance will be transferred to General Reserve after all the debentures are redeemed.)

Redemption method 3 : Redemption of Debentures by Conversion : A Company may offer to the debentureholder to convert their debenture into a new class of securities like Equity shares or preference share or new debentures. The debentureholder may accept the offer or not. If debentures are converted.

Calculation of Number of new securities to be issued

= Amount due to debentureholders/Issue Price

Issue Price = Nominal Price + Securities Premium on Issue of New Securities

Or Isse Price = Nominal Price- Discount on Issue of New Securities.

Illustration 8 : 2000, 8% Debenture Rs.100 each issued at par redeemable at 5% premium were converted into equity share of Rs.10 each at par, Journalise.

Solution :

JOURNAL

Date	Particulars	Debit ₹	Credit ₹
	8% Debentures A/c Dr.	2,00,000	
	Premium on Redemption of Debentures A/c Dr.	10,000	
	To Debenturholder A/c		2,10,000
	(Being the amount due debentureholder)		
	Debentureholders A/c Dr.	2,10,000	
	To Equity Share Capital A/c		2,10,000
	(Being the conversion of 2,000, 8% Debentures in 21,000 equity share of ₹ 10 issued at par		

Number of Equity shares to be issued : ₹ 2,10,000/10=21,000

Illustration 9 : L Ltd. redeemed 4,000 9% Debentures of ₹ 100 each which were issued at par by converting them into 10% Preference Share of ₹ 10 each issued at a premium of 25% Journalise.

Solution :

L Ltd.

Date	Particulars	Debit ₹	Credit ₹
	8% Debentures A/c Dr.	4,00,000	
	To Debentureholder A/c		4,00,000
	(Being the amount due debentureholder		
	Debentureholders A/c Dr.	4,00,000	
	10% Preference Share Capital A/c		3,20,000

	To Equity Share Capital A/c (Being the conversion of 4,000, 9% Debentures in 32,000 equity share of ₹ 10 issued at ₹ 12.50)			80,000

Number of Preference shares to be issued : ₹ 4,00,000/12.50 = 32,000

Illustration 10. : Jai Ltd. redeemed ₹ 1,80,000, 12% Debentures of ₹ 100 each at 110% by converting them into equity shares of ₹ 100 each, ₹ 90 paid-up Journalise.

Solution

Jai Ltd.

Date	**Particulars**	**Debit** ₹	**Credit** ₹
	8% Debentures A/c Dr.	1,80,000	
	Premium on Redemption of Debentures A/c Dr.	18,000	
	To Debentureholder a/c		1,98,000
	(Being the amount due debentureholder)		
	Debentureholders A/c Dr.	1,98,000	
	To Equity Share Capital A/c		1,98,000
	(Being the conversion of 1,800, 12% Debentures in 2200 Equity share of ₹ 10, ₹ 90 paid-up)		

Number of Equity shares to be issued : ₹ 1,98,000/90= 2,200 Equity Shares

Illustration 11. : Rashi Ltd. redeemed 5,280, 12% Debentures of ₹ 100 each, at 110% by converting them into equity shares of ₹ 100 each, at 4% discount. Journalise.

Solution

Rashi Ltd.

Date	**Particulars**	**Debit** ₹	**Credit** ₹
	12% Debentures A/c Dr.	5,28,000	
	Premium on Redemption of Debentures A/c Dr.	52,800	
	To Debentureholder A/c		5,80,800
	(Being the amount due debentureholder)		
	Debentureholders A/c Dr.	5,80,800	
	Discount on issue of shares A/c Dr.	24,200	
	To Equity Share Capital A/c		6,05,000
	(Being the conversion of 5,280, 12% Debentures in 6,050 Equity share of ₹ 100 at ₹ 96.00 each		

Number of Equity shares to be issued : ₹ 5,80,800/96.00 = 6050 Equity Shares

Illustration : 12 Pass the necessary journal entries for the issue and redemption of

Debentures in the following cases :

(i) 10,000 10% Debentures of ₹ 120 each issued at 5% premium repayable at par.

(ii) 20,000 9% Debentures of ₹ 200 each issued at 20% premium repayable at 30% premium

Date	Particulars	L.F.	Debit ₹	Credit ₹
(i)	Bank A/c Dr. To Debenture Application and Allotment A/c (Being receipt of Application money)		12,60,000	 12,60,000
	Debenture Application and Allotment A/c Dr. To 10% Debenture A/c To Securities Premium A/c (Being Issue of 10% Debenture at premium redeemable at par)		12,60,000	 12,00,000 60,000
At the time of redem	10% Debenture A/c Dr. To Debentureholder A/c (Being amount due to debentureholder)		12,00,000	 12,00,000
	Debentureholder A/c Dr. To Bank A/c (Being the amount paid to debentureholders)		12,00,000	 12,00,000
(ii)	Bank A/c Dr. To Debenture Application and Allotment A/c (Being receipt of Application money)		48,00,000	 48,00,000
	Debenture Application and Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 9% Debenture A/c To Securities Premium A/c To Premium on Redemption of Debentures A/c (Being Issue of 9% Debenture at premium redeemable at premium)		48,00,000 12,00,000	 40,00,000 8,00,000 12,00,000
At the time of redeem	9% Debenture A/c Dr. Premium on Redemption of Debenture A/c Dr. To Debentureholder A/c (Being amount due to debentureholder		40,00,000 12,00,000	 52,00,000
	Debentureholder A/c Dr. To Bank A/c (Being the amount paid to debenture holders)		52,00,000	 52,00,000

Conversion of Debentures into shares which are originally issued at a Discount : When debentures are originally issued at discount, discount on issue of debenture account is debited with the amount of discount, Discount on issue of debenture account is written off during the time period of debenture as as issue date to redemption date.

Note : By the maturity date the discount on issue of debenture account is fully written off from the Profit & Loss A/c.

(a) When conversion done after the maturity of debenture :- The conversion is done with the full amount of debenture the discount on issue of debenture account is fully written off, so discount account is not credited on the date of conversion in maturity of debentures : e.g.

1st April, 2005 X Ltd. issued 20,000, 9% debentures of Rs.10 each at a discount of 10% redeemable at par after 5 years by converting them into equity shares of Rs.10 each issued at a premium of 25% pass journal entries for the redemption of debentures.

Sol :

Date	Particulars	L.F.	Debit ₹	Credit ₹
1.4. 2010	9% Debentures A/c Dr. To Debentures holders A/c (Being amount due to debenture holders on conversion at muturity date)		2,00,000	 2,00,000
1.4. 2010	Debenture holders A/c Dr. To Equity Share Capital To Securities Premium A/c (Being amount due on conversion discharge by issue of 16,000 equity shares) 2,00,000/12.5=16,000		2,00,000	 1,60,000 40,000

(1) Discount A/c already written off. conversion is done with the full amount of Debentures.

(B) Conversion before Maturity date of redemption of debentures : In this situation the discount on isssue of debentures account is not fully written off because conversion is before the due date of the redemption. So the actual amount received on issue of debenture at the time of issue is to be determined and it should be taken as amount due to debenture holders and new equity shares are to be issued for the amount actually received at the time of issue of debentures. If this rule is not applied, the provisional conditions of section 79 of the companies Act 1956 would be violated.

If a company, convert it debentures into equity share before the maturity, then Discount in issue of debentures Account should be credited with the amount if discount which has not yet been written off and Profit & Loss Account should be credited with the amount of discount which has already written off e.g.

On 1st April 2010, X Ltd. issued 50,000, 10% Debentures of Rs.10 each at 4% discount and redeemable at par after 5 year. It offered the debentureholders option to convert their debentures in equity share of Rs.10 each after 31st March, 2012. On 1st April, 2012, 25% of debentureholders accepted & exercised their option. Give necessary journal entries at the time of converssion of debentures.

Date	Particulars	Debit ₹	Credit ₹
1.4. 2010	10% Debentures A/c Dr. To Discount on issue of Deb. A/c To Profit & Loss A/c To Debenture holder's A/c	1,25,000	 3,000 2,000 1,20,000

	(Being the amount due to debenture holder's on conversion of debentures)		
1.4. 2012	Debentureholder's A/c Dr.	1,20,000	
	To Equity Share Capital A/c		1,20,000
	(Being the issue of 12,000 Equity Shares of Rs.10 each at par on conversion of 12,500 10% Debanturs		

Note : In the above Illustration discount on issue of debentures account is credited with the amount of discount not written off on the conversion date i.e. total Debenture.

Total No. of Debentures issue = ₹ 50,000

Debentures to be converted 25% of 50,000 = 12,500 debentures of ₹ 10/- each

Total Discount at the time of issue on 12,500 10% Debentures =

12500x10=125000x4/100= ₹ 5000, term of Deb.5 years.

Discount written off per year = 5000/5= Rs.1,000

Discount written off of between issue date (1/4/2010) to conversion date (1/4/2012) is two year = 1000x2=Rs.2000.

Discount not written off Rs.5,000-2,000 = Rs.3,000

Discount in issue of Debenture Account should be credited with Rs.3000

Discount in issue of debenture has the debit balance ₹ 3000 on the date of conversion of debentures. so the discount on issue of debenture Account should be credited with ₹ 3000.

Discount on issue of debentures Rs.2000 has been written off by debited the profit and loss account till on conversion of debenture date so Profit & Loss a/c should be credited with Rs.2,000.

Note If there is no information about the date of conversion, it will be assumed that conversion took place before the date of motutiry. In this case it is not possible to calculate the amount of discount which has been written off upto date of conversion and which has not written off. It is assumed in this case that no discount has been written off and discount on issue of debenture account should be credited with whole amount of discount e.g.

X Ltd. redeemed its 1,000; 10% Debentures of Rs.100 each which were issued at a discount of 5% by converting them into equity shares of Rs.10 each issued at a Premium of 25% Journalise.

Date	**Particulars**	**Debit ₹**	**Credit ₹**
	10% Debentures A/c Dr.	1,00,000	
	To Discount on issue of debentures A/c		5,000
	To Debentureholders A/c		95,000
	(Being the amount due to debenture holders)		
	Debenture holders A/c Dr.	95,000	
	To Equity Share Capital a/c (7600x10)		76,000
	To Securities Premium A/c (7600x2.5)		19,000
	(Being the issue of 7600 equity shares of Rs.10 each at 12.50 = 95000/12.5=7600)		

Note : The provision of Sec 79 of companies Act, 1956 applies only on the issue of shares only. The amount of discount on issue of debentures should be considered for when redemption is made on conversion into share only. If redemption is made on conversion into new class of debenture, then the provision of Sec 79 not violated. The discount on issue of debenture account should not be credited e.g. 2,500, 10% Debentures of ₹ 100 each issued at a discount of 5% and redeemable at par after each 4 years were converted into 14% Debentures of ₹ 10 each issued at par before maturity. Give the necessary journal entries for redeemption of debentures

Sol. :

Date	Particulars		Debit ₹	Credit ₹
	10% Debentures A/c	Dr.	2,50,000	
	To Debenture holder's A/c			2,50,000
	(Being the amount due to debenture holders)			
	Debentureholder's A/c	Dr.	2,50,000	
	To 14% Debentures A/c			2,50,000
	(Being issue of 25,000; 14% Debentures of ₹ 10 each at par on conversion = 2,50,000/10=25,000 debenturs			

Illusration 13 :- Journalise the following transactions :

(i) A Ltd. redeemed 5,000, 12% debentures of ₹ 100 each which were issued at a discount of 8% by converted them into equity shares of ₹ 10 each issued at par.

(ii) B Ltd. redeemed 600, 14% debentures of ₹ 10 each which were issued at a discount of 5% by converting them 12% preference shares of ₹ 100 each at a premium of ₹ 25 per share.

(iii) C Ltd. redeemed 1000, 10% Debentures of ₹ 100 each which were issued at a discount of 10% by converting them equity shares of ₹ 50 each, ₹ 45 paid-up.

(iv) D Ltd. redeemed 4000, 12% Debentures of ₹ 100 each which were issued at a discount of 35% by converting them into 8% Debentures ₹100 each issued at par, before the maturity date of debentures.

Sol. :

Date	Particulars		Debit ₹	Credit ₹
(i)	12% Debentures A/c	Dr.	5,00,000	
	To Discount on issue of Debentures A/c			40,000
	To Debenture holders A/c			4,60,000
	(Being the amount due to debentureholders			
	Debentureholders A/c	Dr.	4,60,000	
	To Equity Share Capital A/c			4,60,000
	(Being amount due to debentureholders on conversion discharged issue of 4,60,000/10 = 46,000 equity shares of ₹ 10 each			
(ii)	14% Debentures A/c	Dr.	60,000	

	To Discount on issue of Debentures A/c		3,000
	To Debenture holders A/c		57,000
	(Being the amount due to debentureholders		
	Debentureholders A/c Dr.	57,000	
	To 12% performance share capital a/c		45,600
	To Securities Premium A/c		11,400
	(Being amount due to debentureholders on conversion discharged by issue of 57000/125=456 12% preference shares at a premium of Rs.25 each		
(iii)	10% Debentures A/c Dr.	1,00,000	
	To Discount on issue of Debentures A/c		10,000
	To Debenture holders A/c		90,000
	(Being the amount due to debentureholders)		
	Debentureholders A/c Dr.	90,000	
	To Equity share capital A/c		90,000
	(Being amount due to debentureholders on conversion discharged by issue of 90,000/45=2000 Equity shares of ₹ 50 each, ₹ 45 paid-up)		
(iv)	12% Debentures A/c Dr.	4,00,000	
	To Debentureholders A/c		4,00,000
	(Being amount due to debenture holders)		
	Debentureholders A/c Dr.	4,00,000	
	To 8% Debentures		4,00,000
	(Being the amount due to debenture holders on conversion discharged by issue of 4,00,000/10 4000,8) Debenture of Rs.100 each at par)		

Note : In the above first three cases nothing is mentioned about the date of issue & date of maturity of debentures. It is assumed that debentures were redeemed before maturity date & discount on issue of debentures A/c credited with the amount of discount allowed at the time of issue.The new shares under Sec. 79 would be issued amount equal to Net amount received from debentureholders at the time of issue of original from debentureholders.

Case 4. Sector-79 does not apply on issue of debentures discount A/c not credited in the solution.

CHAPTER 10

Financial Statement of Companies

Basic Financial Statement also called Final Accounts

1. Income Statement :- It show the net result of business operation i.e. Net/profit/Net loss during an accounting period (or Trading and profit & loss A/c)

FORM OF BALANCE SHEET

Name of the Company ....

Balance Sheet as at ....

Particulars	**Note No.**	**Fig. for the Curent Year**	**Fig. for the Previous Year**
I. EQUITY AND LIABILITIES			
(i) Shareholders' Fund			
(ii) Share Application pending allotment			
(iii) Non Current Liabilities			
(iv)Current Liabilites			
Total			
II. ASSETS			
(i) Non-Current Assets			
(ii) Current Assets			
Total			

Hence we see that there are only four major headings under equity and liability side whereas Asset side consist of only two majour heading

Subheading under various major heading

Equity and Liability

(1) Shareholder's Fund

(a) Share Capital

(b) Reserves and Surplus

(c) Money received against share warrants

(2) Non Current Liabilities

(a) Long term borrowings - Bonds, Debenture, loans from Banks etc are included.

(b) Deferred tax liabilities.

(c) Other long term liabilities - It include trade payable which outstanding for more than 12 months.

(3) Current Liabilities

(a) Short term borrowings

(b) Trade Payables (Creditors and Bills Payable)

(c) Other Current Liabilities - Include current maturities of long-term debt., Interest accrued but not due & interest acerued and due on borrowings, outstanding expenses, calls in advance, unclaimed dividents etc.

ASSETS

(1) Non Current Assets

(a) Fixed Assets :- This subheading is divided into tangible, Intangible Assets and Capital-work-in-progress.

(b) Non-Current Investments.

(c) Deferred Tax Assets

(d) Long term Loans and Advances

(e) Other Non-Current Assets

(2) Current Assets

(a) Current Investment (i.e. upto one year)

(b) Inventories - Raw material, stock in trade work in progress, stores and spares and loose tools etc. are also included alongwith the finished goods

(c) Trade Receivables - Sunday Debtors, BIR

(d) Cash and Cash Equivalents

(e) Short term loan and advances

(f) Other current Assets - It include prepaid expenses, interest ocerued on investments etc.

Note- 1. Miscellaneous Expenditure and the Debit Balance of Profit and Loss A/c are not shown separately.

2. Profit & Loss A/c - Debit Balance is shown as a minus item under Reserve and Surplus.

3. Miscellaneous Expenditure items are subtraeted from the security premium on the equity and liability heading and in the absence of such a reserve these are shown as a other Non-Current Assets or other current Assets as per instructions.

Contingent Liabilities :-

These are the liabilities which are not liabilities on the date but may arise upon the happening of a certain event. These are not added in the Amount of liabilities and are shown only as footnotes.

Remember some examples :-

- Disputed claims not as knowledge as debts on that date
- Uncalled liability on partly paid shares
- Arrears of dividends on cumulative preference shares.
- Bills discounted but not matured
- Guarantee for loans

Some Example of Miscellaneous Expenditure (Must Remember) :-

- Preliminary Expenses
- Expenses on issue of shares on debentures
- Discount allowed on the issue of shares/deb.
- Development expenditure not adjusted.
- Interest paid out of capital during construction period.

Some Important Items normally asked in the Exam :

Equity and Liability head

S. No.	Items	Major Heading	Subheading
1.	Proposed Dividend	Current Liability	Short-term Provision
2.	Unclaimed Dividend	Current Liability	Other Current Liabilities
3.	Bills Payable	Current Liability	Trade Payable

4.	Provision for Tax	Current Liability	Short-term Provision
5.	Outstanding Salaries	Current Liability	Other Current Liabilites
6.	Preliminary Expenses	Shareholders' Fund	Subtracted from security premium under Reserve and Surplus.
7.	Authorised Capital	Shareholder's Fund	Share Capital
8.	Debenture	Non-Current Liabilities	Long-term Borrowings
9.	Sinking Fund	Shareholder's Fund	Reserve and Surplus
10.	Provision for Provident Fund	Non-Current Liabilities	Long-term provision
11.	Security Premium	Shareholders' fund	Reserve and Surplus
12.	Creditors	Current Liabilities	Trade Payable

Assets head

S. No.	Items	Major Heading	Subheading
1.	Patents and Trade Marks	Non-Current Assets	Intangible Assets
2.	Bills Receivables & Debtors	Current Assets	Trade Receivable
3.	Prepaid Expesnes	Current Assets	Other Current Assets
4.	Advances Recoverable in Cash	Current Assets	Short-term Loans and Advances
5.	Goodwill	Non-Current Assets	Intangible Assets
6.	Loose Tools	Current Assets	Inventories
7.	Bank/Cash Balance	Current Assets	Cash & Cash Equivalents
8.	Investments	Non-Current Assets	Non-Current Investment
9.	Work-in progress	Current Assets	Inventories
10.	Govt. Securities	Non Current Assets	Non-Current Investment

Financial Statement Analysis

Meaning - In the words of Finney and miller 'Financial Analysis consists in separating facts according to some definite plan arranging them in groups according to certain circumstances and then presenting them in a convenient and easily readable and understandable form.'

Objectives/Need

- To measure the profitability of the business
- To measure the financial strength of the business
- To make comparative study within the firm and with other forms
- To judge the effciency of Management
- To provide useful information to the Management
- To find out the capability of payment of interest, dividend etc.
- To find out the trend of the business

Significance or Importance of Financial Analysis

For Management - To know the profitability, liquidity and solvency condition to measure the effectiveness of own decision taken and take corrective measure in future.

For Investors :- Want to know the earning capacity and future growth prospects of the business which helps in assessing the safety of their investment and reasonable return.
For Creditors :- Short term creditors want to know the liquidity condition of the business where as long term creditors want to know the solvency will be able to pay the interest constantly.
For Govt. :- To know the profitability condition for taking taxation decision and to find out the company.
For Employees :- To know the progress of the company for assessing Bonus, increase in wages and ensure stability of their job.

Limitation of Financial Analysis

- Based on basic financial statement which themselves suffer from certain limitations.
- Don't reflect changes in price level.
- Affected by the personal ability and bias of the Analyst.
- Lack of qualitative analysis as only those transaction and events are recorded which can be measured in terms of money.
- When different accounting policies are followed then the comparison of two financial statement becomes unreliable.
- Single years' Analysis of financial statement have limited use.

Types of financial Analysis

Horizontal Analysis :- In this, figure for two or more years are compared and analyzed. It is also called dynamic Analyses.
Examples :- Comparison of sales, profits, cost of goods sold for two or more than 2 years.
Vertical Ananlysis :- In this type, Financial Statement for a single year is analyzed. It involves the study of relationship between two quantities of balance sheet or P & L A/c of a single years or period.
Example :- Common size statements.

Tool of Financial Analysis

Comparative Statement :- Financial Statement of two years is compared. Absolute change and then the percentage change in figure are calculated. It is a form of **Horizontal Analysis**
Common Size Statement : Various figure of single year Financial Statement are converted in to percentage with resepect to some common base. In **Income Statement sales** in take as base (i.e.100) where as in **Balance Shettotal assets** are taken as base.
Trend Analysis :- Here trend percentage are calculted for a number of years taking one year as a base year. This helps is assessing the trend of increase or decrease in various items.
Accounting Ratios :- Study of relationship between various items is known as Ratio analysis.
Cash Flow Statement :- It shows the inflow and outflow of cash and cash equivalents during a particular period which helps in finding out the causes of changes in cash between the two dates.
Fund Flow Statement :- It indicates the reasons of changing in working capital during a particular time period. It shows sources (inflow) and Applications (Outflow) of funds.
Break - even Analysis :- It is a point where total of sales is exactly equal to the total of cost to the total of cost of sales i.e. the firm has neither any profit nor any loss. **It is also**

calledas No Profit-No Loss Point.

Comparative Statement Preparation :-

Steps :-

- Put the fig. of Financial Statement of two year side by side (previous year amount in the Ist column

- In the next column write the difference of the two fig. For increase with respect to the previous year's (+) sign and Decrease put (-) sign.

- Percentage increase or decrease is calculated by the formula given below :-

Absolute increase or decrease * 100

Fig. for the previous year

Format for Comparative Balance Sheet

COMPARATIVE BALANCE SHEET

As at 31st March, 2010 and 2011

Particulars	**2002**	**2003**	**Absolute increase or Decrease over 2010**	**% Increase or decrease in relation to 2011**
	Rs.	**Rs.**	**Rs.**	**%**
Fixed Assets (A)	–	–	–	
Investment (B)				
Working Capital				
Current Assets (i)	–	–	–	
Current Liabilities(ii)	–	–	–	
Working Capital (i-ii)	–	–	–	
Capital Employed (A+B+C+)				
Less : Long-term Debts (e.g.	–	–	–	
debentures)	–	–	–	
Shareholder's Funds				
Represented by :				
Preference Share Capital	–	–	–	
+ Equity Share Capital	–	–	–	
+ Net Reserve and Surplus	–	–	–	
	–	–	–	

Example 1.

From the following information, prepare Balance Sheet of X Ltd. :-

Particulars	**31.03.2006**	**31.03.2007**
	Rs.	**Rs.**
Currrent Assets	13,00,000	18,20,000
12% Debentures	5,00,000	4,00,000
Equity Share Capital	10,00,000	10,00,000

Fixed Assets	15,00,000	20,00,000
Investments	2,00,000	50,000
Current Liabilities	9,00,000	12,70,000
Reserves and Surplus	6,00,000	12,00,000

Solution :

COMPARITIVE BALANCE SHEET OF X LTD.

As on 31st March 2006 & 2007

Particulars	**2002** **Rs.**	**2003** **Rs.**	**Increase or decrease over 2006** **Rs.**	**% Increase or decrease in relation to 2011** **%**
Fixed Assets (A)	15,00,000	20,00,000	+5,00,000	+33.33
Investments (B)	2,00,000	50,000	-1,50,000	-75
Working Capital :-				
Current Assets (1)	13,00,000	18,20,000	+5,20,000	+40
Current Liabilities (2)	9,00,000	12,70,000	+3,70,000	+41.11
Working Capital (c) (1-2)	4,00,000	5,50,000	+1,50,000	+37.50
Capital Employed (A+B+C)	21,00,000	26,00,000	5,00,000	+23.81
Less : 12% Debenture	5,00,000	4,00,000	-1,00,000	-20
Shareholder's Funds	16,00,000	22,00,000	+6,00,000	+37.50
Represented by :-				
Equity Share Capital	10,00,000	10,00,000	-	-
+Reseve and Surplus	6,00,000	12,00,000	+6,00,000	+100
Shareholder's Funds	16,00,000	22,00,000	+6,00,000	+37.50

Format of a Comparative Income Statement

COMPARATIVE INCOME STATEMENT

For the year ended 31st March, 2010 and 2011

Particulars	**2010** **Rs.**	**2011** **Rs.**	**Absolute increase or decrease over 2010** **Rs.**	**% Increase or decrease in relation to 2011** **%**
Net sales	–	–	–	–
Less : Cost of goods sold	–	–	–	–
Gross Profit (A)	–	–	–	–
Less : Operating Expenses : (See note 1)				
Office & administration Expenses				
Selling & distribution expenses				

Total operating expenses (B)				
Operating profit (A-B)	–	–	–	–
Add : Non-Operating Income (note2)				
Total Income	–	–	–	–
Less : Non-Operating Expenses (See note 3)	–	–	–	–
Net Income (profit) before tax				
Less : tax				
Net Income (profit) after tax				

Note (1) Operating Expenses : These refer to the indirect expenses relating to the principal revenue generating activities of the enterprise. These include :

- Office and Administrative expenses such a salary, postage, depreciation etc.
- Selling and Distribution expenses
- Cash discount allowed to customers
- Bad debts and Provision for doubtful debts.
- Interest on short term debts

(2) Non-operating Incomes : These refer to the incomes which are not from the principal revnue producing activities. These include :

- Interest and dividend received on long term investments
- Rent received
- Profit on sale of fixed assets
- Compensation for acquisition of land

(3) Non-operating Expenses : These refer to the expenses and losses which are not related to the operating activities. These include :

- Interest on long term debts
- Loss on sale of fixed assets
- Intangible assets written off such as goodwill, patents etc.
- Fictitious assets written off such as preliminary expenses, underwriting commission, discount on issue of share of debentures etc.

Example 2. Prepare a Comparative Income statement Ahmed Ltd., with the help of the following information :-

	31.03.2000	**31.03.2001**
	Rs.	**Rs.**
Sales	5,00,000	8,00,000
Cost of Goods Sold	3,00,000	5,00,000
Direct Expenses	40,000	20,000
Indirect Expesnes	30,000	40,000
Income Tax	40%	50

(C. B. S. E. 2002)

SOLUTION : COMPARATIVE INCOME STATEMENT

Particulars	31.03.2000 Rs.	31.03.2001 Rs.	Absolute Change Rs.	% Change
Sales	5,00,000	8,00,000	3,00,000	60.00
Less : Cost of goods sold	3,00,000	5,00,000	2,00,000	66.67
Gross Profit	2,00,000	3,00,000	1,00,000	50.00
Less : Indirect Expenses	30,000	40,000	10,000	33.33
Net Profit before tax	1,70,000	2,60,000	90,000	52.94
Less : Income tax	68,000	1,30,000	62,000	91.18
Net Profit after tax	1,02,000	1,30,000	28,000	27.45

Importance of Comparative Statement

- To make the data simple and more understandable.
- To indicate the trend with respect to the previous year.
- To compare the firm performance with the performance of other firm in the same business.

Common Size Statement Preparation

STEPS

1. Put the absolute amounts of two years side by side. Previous year's amount in the first column and current year in the 2nd column.
2. Calculate the percentage of each items w.r.t the common base by using the formula
   Percentage of the item =
   Absolute figure of the item of the year x 100/Base figure of that year
3. Base figure for the **Income statement** is taken as total sales whereas for **Balance Sheet** it is **total assets.**
4. 3rd column is for Previous year's Percentage and 4th column is for current year's percentage.

Format of Balance Sheet As at 31st March 2010 & 2011

Particulars	Absolute Amounts		Percentage & Balance Sheet Total	
	2010 Rs.	2011 Rs.	2010 %	2011 %
Equity and Liabilities				
Equity Share Capital	–	–	–	–
Preference Share Capital	–	–	–	–
Reserve and Surplus (Net)	–	–	–	–
Non-Current Liabilities	–	–	–	–
Current Liabilities	–	–	–	–
Short-term Provisions	–	–	–	–
Total	–	–	–	–
Assets				
Non-Current Assets	–	–	–	–
Non-Current Investmnets	–	–	–	–
Current Assets	–	–	–	–
Total	–	–	–	–

Note - Net Reserve and Surplus means total of all reserves less Miscellaneous Expenditure

Example 3 :- Prepare a common size balance sheet fromt he following data :-
Balance Sheet as on 31st March 2010 and 2012

Particulars

	31.03.2010 (Rs.)	31.03.2011 (Rs.)
Equity and Liabilities		
Equity Sahre Capital	6,00,000	6,00,000
Reserve and Surplus		
General Reserve		
	6,80,000	10,00,000
10% Debentures	3,00,000	3,00,000
Bills Payable	84,000	1,40,000
Creditors	3,28,000	4,50,000
Outstanding Expenses	8,000	10,000
Total	20,00,000	25,00,000
ASSETS :-		
Land and Building	8,00,000	7,50,000
Plant & Machinery	3,00,000	5,00,000
Furniture	1,00,000	1,06,250
Stock-in-trade	4,50,000	6,25,000
Sundry Debtors	2,55,000	4,10,000
Cash at Bank	95,000	1,08,750
Total	20,00,000	25,00,000

SOLUTION

COMMON SIZE BALANCE SHEET
As at 31st March 2010 and 2011

Particulars	**Absolute Amounts**		**Percentage & Balance Sheet Total**	
	2010 Rs.	**2011 Rs.**	**2010 %**	**2011 %**
Equity and Liabilities				
Equity Share Capital	6,00,000	6,00,000	30	24.00%
Reserve and Surplus	6,80,000	10,00,000	34	40.00
Non Current Liabilities (Debentures)	3,00,000	3,00,000	15	12.00
Current Liabilities	4,20,000	6,00,000	21	24.00
Total	20,00,000	25,00,000	100	100.00
Assets				
Non Current Assets	12,00,000	13,56,250	60	54.25
Current Assets (Stock, Debtors & Cash)	8,00,000	11,43,750	40	45.75
Total	20,00,000	25,00,000	100	100.00

Format of a Common Size Income Statement

COMMON SIZE INCOME STATEMENT

For the year ended 31st March, 2010 and 2011

Particulars	Absolute Amounts		Percentage & Balance Sheet Total	
	2010	2011	2010	2011
Net Sales	Rs.	Rs.	%	%
Less : Cost of Goods Sold	–	–	–	–
Gross Profit (A)	–	–	–	–
Less : Operating Expenses :	–	–	–	–
Office & Administration Expenses	–	–	–	–
Selling & Distribution Expesnses	–	–	–	–
Total Operating Expenses (B)	–	–	–	–
Operating Profit (A-B)	–	–	–	–
Add : Non-Operating Incomes	–	–	–	–
Total Income	–	–	–	–
Less : Non-operating Expenses	–	–	–	–
Net Income (Profit) before tax				
Less : Tax	–	–	–	–
Net Income (Profit) after tax	–	–	–	–

Example 4 : Prepare a Common Size of Income Statement from the following Statement :-

Particulars	2007 Rs.	2008 Rs.	Particular	2007 Rs.	2008 Rs.
To Cost of Goods Sold	60,000	60,000	By Net Sales	1,00,000	1,20,000
To Gross Profit c/d	40,000	54,000			
	1,00,000	1,20,000		1,00,000	1,20,000
To Office and Admn. Exp.	12,000	12,000	By Gross Proft b/d	40,000	54,000
To Selling and Distribution Exp.	5,000	9,600			
To Net Profit	23,000	32,400			
	40,000	54,400		40,000	54,000

COMMON SIZE INCOME STATEMENT

Particulars	Absolute Amounts		Percentage of Net Sales	
	2007	2008	2007	2008
Net Sales	1,00,000	1,20,000	100	100
Less : Cost of Goods Sold	60,000	66,000	60(1)	55(4)
Gross Profit	40,000	54,000	40(2)	45(5)
Less : Operating Expenses :-				
Office and Administration Exp.	12,000	12,000	12(3)	10(6)
Selling and Distribution Exp.	5,000	9,600	5	8
Operating Income	23,000	32,400	23	27

All percentage will be calculated on the basis of Net Sales. Calculating of Percentages is as follows :

	Year 2007	Year 2008
Note :	(1) 60,000x100/1,00,000 = 60%	(4) 66,000x100/1,20,000 = 55%
	(2) 40,000x100/1,00,000 = 40%	(5) 54,000x100/1,20,000 = 45%
	(3) 12,000x100/1,00,000 = 12%	(6) 12,000x100/1,20,000 = 10%

Importance of Common Size Statements

- Provides common base for comparison irrespective of the size of individual item.
- It presents the change in various items in relation is net sales, total assets or total liabilities.
- It establish the trend in various items of financial statements.

CHAPTER 11

Accounting Ratios

Accounting Ratio : It is arithmetical relationship between two accounting variables.
Ratio Analysis : A tool used by individuals to conduct a quantitative analysis of infomation in a company's financial statements

Expression of ratios : Ratios are expressed in

1. Pure form like 2:1 all current ratios are expressed in pure form.
2. Percentage e.g. 15% all profitability ratios are presented in percentage form
3. Times like 4 times all turnonver ratios are presented in no. of times
4. Fraction like 3/4 or .75 all solvency ratios are presented in fractions except Interest Coverage Ratio which is presented in Number of times :

Classification or types of ratios

Ratios are classified into 4 categories

1. Liquidity Ratios also called as short term solvency ratios.
2. Solvency Ratios
3. Activity ratios also known as Turnover ratios or Performance ratios
4. Profitability ratios

Note : For Calculation of ratios Formula must be written as it carries marks

Liquidity Ratios : Thesemeasure short term solvency, i.e. the firm's ability to pay current dues. These are

1. Current Ratio also called as working capital ratio
2. Liquid Ratio also called as quick ratio or acid test ratio.

Current ratio is relationship of current assets with current liabilities.

1. CURRENT RATIO = CURRENT ASSETS/CURRENT LIABILITIES

Current assets are assets that can be converted into cash or cash equivalent within short period of time usually a year and current liabilities are those are to be paid in short period.

Example : Current assets are : Cash, Bank, Debtor, Stock (also called as Inventory), Perpaid Expenses and Marketable Securities (highly liquid investment with very little risk of changes in value), Accrued income.

Current Liabilities are : Creditors, Bills Payable, Bank Overdraft, Outstanding Expenses, Advance Income, Unclaimed Dividend, Provision for taxation.

Significance : It assesses ability of business to pay short term liability promptly.

Ideal Ratio : 2:1

Low ratio indicates cannot meet short term liability.

High ratio indicates funds not used effciently and lying idle or poor investment (important for Project work)

Example : XYZ Company's total current assets are Rs.10,000,000 and its total current liabilities are Rs.8,000,000 then its current ratio would be Rs.10,000,000 divided by

Rs.8,00,000 which is equal to 1.25 XYZ Company would be in relatively good short-term financial standing.

Computation of ratio

From the following balance sheet of M/s.Ram Ltd. calculate current ratio as on 31.03.2010

Liabilities	Rs.	Assets	Rs.
Capital	21,000	Fixed Assets	17,000
Reserves	1,500	Stock	6,200
Profit and Loss Account	2,500	Debtors	3,200
Bank Overdraft	2,000	Cash	6,600
Sundry Creditors	6,000		
	33,000		33,000

Solution :

Current Ratio = Current Assets/ Current Liabilities

= Stock+Debtors+Cash/Bank Overdraft+ Sundry Creditors

= Rs.6,200+Rs.3,200+Rs.6,600

= Rs.16,000/Rs.8,000= 2:1

Alternatively current assets can be calculated as

Current Assets = Working Capital + Current Liabilities

Current Assets = Total Assets - Fixed Assets

Current Liabilities = Total Assets-Capital Employed

Indirect question

On payment of current liablity Current Assets and Current Liability reduce to same extent, in such cases ratio change e.g. If current assets are Rs.40,000 and current liabilities are Rs.20,000 on payment of Rs.10,000 to creditors the cash (current asset) will decrease to Rs.30,000 (Rs.40,000 - Rs.10,000) & current liabilities will decrease to Rs.10,000 (Rs.20,000-Rs.10,000)

In first case current ratio is 2:1

Rs.40,000/Rs.20,000

And is second case it is 3:1

Rs.30,000/Rs.10,000

Example :A ratio of Current Assets (Rs.3,00,000) & Current Liabilities(Rs.2 ,00,000) is 1.5:1 . Firm want to maintain it at 2:1 by paying part of Current Liabilities. Compute the amount of Current Liabilities that should be paid.

Current Ratio = Current Assets / Current Liabilities

$\frac{1.5}{1} = \frac{Rs.3,00,000}{Rs.2,00,000}$

Let the amount paid as Current Liabilities is Rs. X

After the payment

$\frac{2}{1} = \frac{Rs.3,00,000 - x}{Rs.2,00,000 - x}$

Rs.3,00,000 –x = 2 (Rs. 2,00,000 –x)

= Rs 3,00,000-x = Rs. 4,00,000 -2x

=Rs. 4,00,000 - Rs. 3,00,000 =2x- x

X = Rs 1,00,000

So Current Liabilities to be paid off is Rs. 1,00,000

Similarly if Current Assets are purchased on credit same amount is added in Current Assets as well as Current Liabilities and ratio changes.

2.LIQUID RATIO : .It is relationship of liquid assets with current liabilities

$$\text{LIQUID RATIO} = \frac{\text{LIQUID ASSETS}}{\text{CURRENT LIABILITIES}}$$

Significance : It assesses short term solvency (debt paying capacity) and is better indicator of liquidity as some current assets are not easily converted to cash.

LIQUID ASSETS = Current Assets- (Stock+ prepaid expenses)

Ideal ratio is 1:1.

Example : Calculate Quick ratio Stock Rs. 80,000 ,Working Capital Rs.2,40,000 Current Assets Rs.4,00,000

Current Liabilities = Current Assets - Working Capital

= Rs.4,00,000 - Rs.2,40,000 = Rs.1,60,000

Quick Assets = Current Assets –Stock = Rs.4,00,000 - Rs. 80,000 = Rs. 3,20,000

$$\text{Quick ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}}$$

$= \frac{Rs.\ 3,20,000}{Rs.1,60,000} = 2:1$

Calculation of either assets or liability on any unknown figure from two given ratios : In such caseswe write down formulae of both ratios and with the help of given figure find out missing figures by means of equation

Example : X Ltd. Has a Current Ratio of 4.5:1 and Quick ratio of 3:1. If the Inventory is Rs. 36,000, find out Current Assets , Current Liabilities and Quick Assets

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{4.5}{1}$$

Let the Current Liabilities are Ythen

Current Assets = 4.5 Y

$$\text{Quick ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}} = \frac{3}{1}$$

Quick Assets = 3 Y

Stock = Current Assets – Quick Assets

Rs.36,000 = 4.5Y- 3Y

Rs.36,000 = 1.5Y

$$Y = Rs.\frac{36000}{1.5}$$

=Rs.24,000

Current Assets = 4.5 x =4.5x24000 = Rs.1,08,000

Quick Assets = 3 Y =3X24000=Rs. 72,000

<u>**Solvency ratios**</u> : Solvency **ratios convey an enterprise' ability to meet long term obligations which means in long term they have sound financial position to pay their debts. Important solvency ratios are Debt- Equity Ratio, Total Assets to Debts Ratio and Proprietary Ratio.**

<u>**3.Debt- Equity Ratio**</u> : It is measure of **financial leverage**. It tells about long term soundness or financial position. A Debt equity ratio of 2:1 is permissible but it varies from industry to industry.

$$\text{Debt- Equity Ratio} = \frac{\textit{Debt}\text{(Long term Loans)}}{\text{Equity (Shareholders Funds)}}$$

Equity = Shareholders Funds (equity share capital ,preference share capital ,reserves and surplus less losses and fictitious assets (miscellaneous expenses, discount on issue of debenture).

Debt : Long term Loans–debentures and long term loans from financial institutions.

Significance : I t measures safety margin available to providers of long term loan .A firm with a debt equity ratio of 2 or less exposes its lenders relatively lesser risk. A firm with a high debt-equity ratio exposes lenders to greater risk as borrowed funds are more than owners funds.

Example : With the help of the given information calculate Debt- Equity Ratio

Particulars	Rs.
Equity Share Capital	5,00,000
9% Preference Share Capital	4,00,000
12% Debentures	2,40,000
General Reserves	70,000
Current Assets	2,00,000
Current Liabilities	1,50,000
Preliminary expenses	10,000

$$\text{Debt- Equity Ratio} = \frac{\text{Debt (Long term Loans)}}{\text{Equity (Shareholders Funds}}$$

$$\frac{\text{12\% Debenture}}{\text{Equity Share Capital +9\% Preference Share Capital + General Reserves - Preliminary expenses}}$$

$$= \frac{\text{Rs. 2,40,000}}{\text{Rs.5,00,000 +Rs. 4,00,000 +Rs.70,000- Rs.10,000}}$$

$$= \frac{\text{Rs.2,40,000}}{\text{Rs. 9,60,000}} = .25:1$$

4. **<u>Total Assets to Debts Ratio</u>** : It establishes relation between total assets and total long term debts.

$$\text{Total Assets to Debts} = \frac{\text{Total Assets}}{\text{Long- term Debts}}$$

Total Assets= Long- term Debts + Shareholders Funds + Current Liabilities (as calculated from liability side of balance sheet) or

Total Assets = Fixed Assets +Current Assets(as calculated from assets side of balance sheet)

It measures the safety margin available to providers of long term loans .High ratio shows higher security to lenders and low ratio represents risky financial position

From the following balance sheet compute Total Assets to Debt Ratio

Balance Sheet of Y Ltd.

Particulars	**Note No.**	**Figures for Current Years**	
Equity and Liabilities			
1. Shareholder's Funds			
(a) Share Capital		15,00,000	
(b) Reserves		3,00,000	
Non-Current Liabilities			
12% Loan (Long Term)			
Current Liabilities		6,00,000	
Total		36,00,000	
Assets			
Non Current Assets			

Fixed Assets		22,50,000	
Current Assets			
Inventories		9,37,500	
Other Current Assets		10,12,500	
Total		36,00,000	

Total Assets on Debt Ratio = Total Assets/Long Term Debts

= 36,00,000/12,00,000 = 3:1

5.<u>ProprietaryRatio</u> : It establishes relation between proprietor's funds and total assets .

$$\text{Proprietary Ratio} = \frac{\text{proprietor's funds or Shareholders Funds}}{\text{Total assets- fictiousassets}}$$

This ratio highlights the general financial position of enterprise It measures the safety margin available to creditors. High ratio shows higher security to creditors but improper mix of owners funds and loan and low ratio represents inadequate cover to creditors .

Example :From the following calculate proprietary ratio:

Balance Sheet of ABC Ltd.

Particulars	**Note No.**	**Figures for Current Years**	
Equity and Liabilities			
1. Shareholder's Funds			
(a) Share Capital		4,50,000	
(b) Reserves General Reserves		1,80,000	
Non-Current Liabilities			
Long Term borrowing			
(12% Debentures)		75,000	
Current Liabilities			
Trade Payable (Creditors)		45,000	
Total		7,50,000	
2. Assets			
Non Current Assets			
(a) Fixed Assets		3,75,000	
(b) Non-Current Investments		2,25,000	
Cureent Assets			
Other Current Assets		1,50,000	
Total		7,50,000	

Ans. : Proprietory Ratio = Shareholder's Funds/Total Assets

Shareholder Funds = Share Capital+Reserves = 4,50,000+1,80,000=6,30,000

Propritory Ratio = 6,30,000/7,50,000= .84:1

6. Interest Coverage Ratio : This ratio establishes relationhip between the net profit before interest & tax and interest payable on long term debts. Since interest is charge on profit, net profit taken to calculate ratio is before interest & tax it determines ease with which a company can pay interest expense on outstanding debt.

Interest Coverage Ratio = Net Profit before Interest & Tax/Interest

Objective & Significance - Objective is to ascertain the amount of profit available to cover the interest charge.

Parties interested Debentureholders under of long term credit

High Ratio is better for lenders as it indicates higher safety margin

Illustration 1

Calculate Interest Coverage Ratio

Net Profit (after taxes) =	₹ 1,00,000
Fixed interest charges on long =	₹ 20,000
Term borrowing	
Rate of tax	50%

Solution

Interest Coverage Ratio = Net Profit Before Interest & Tax/Interest

= 1,00,000+1,00,000(tax)+20,000/20,000

= 1,00,000+1,00,000 (tax)+20,000/20,000 = 2,20,000/20,000=11 Times

Illustration 2 :- From the following ulternation calculate interest coverage ratio :-

10,000 equity shares of ₹ 10 each	₹ 1,00,000
8% Preference Shares	₹ 70,000
10% Debentures	₹ 50,000
Long term Loans from Banks	₹ 50,000
Interest on long term loans from bank	₹ 50,000
Profit before tax	₹ 75,000
Tax	₹ 9,000

Solution : Interest on Debentures = 50,000 x10/100= 25000

Profit before Interest & Tax = Profit after tax + tax + Interest on debentures + Interest on Long term Loans

= 75,000+9,000+5000+5000=Rs.94,000

Interest Coverage Ratio = Profit before Interest & Tax/Interst = 94,000/10,000

=9.4 Times

ACTIVITIES RATIOS : These ratios measure the **efficiency of asset management** and measure the effectiveness with which a concern uses resources at its disposal. These show rotation of concerned item within accounting period.

7. INVENTORY TURNOVER RATIO : It is also called as Stock turnover ratio. This ratio is a relationship between the cost of goods sold during a particular period of time and the cost of average inventory during a particular period. It is expressed in number of times

This ratio indicates whether investment in stock is within proper limit or not. This shows how quickly inventory is sold. Generally higher ratio I considered better but very high ratio shows overtrading and low ratio means stock is piled up or overinvestment in stock.

INVENTORY TURNOVER RATIO= Cost of goods sold/Average stock

Average stock = Opening stock + Closing stock /2

Example :

The cost of goods sold is Rs.500,000. The opening stock is Rs.40,000 and the closing stock is Rs.60,000 (at cost). Calculate inventory turnover ratio

Calculation :

Inventory Turnover Ratio = Cost of goods sold/Average stock
Average stock = Opening Stock+Closing Stock/2
Rs.40,000+Rs.60,000/2 = Rs.50,000

Inventory Turnover Ratio = $\frac{\text{Rs.500,000}}{\text{Rs. 50,000}}$ = 10 times

Cost of goods sold =Sales –Gross Profit

Closing stock = Opening Stock+ Purchases + Direct expenses - Cost of goods sold

Or Closing stock = Opening Stock+ Purchases+ Gross Profit –sales

Example The opening stock is Rs.29,000 and the closing stock Rs.29,000.Sales are Rs. 3,00,000Gross Profit 25% on cost . Calculate inventory turnover ratio

Inventory Turnover Ratio (ITR) = $\frac{\text{Cost of goods sold}}{\text{Average stock}}$

Let Cost of goods sold is y

Gross Profit 25% of y ,i.e $\frac{y}{4}$

Cost of goods sold +Gross Profit = Sales

Rs.3,00,000 = Y+ $\frac{Y}{4}$

4y+y= Rs.12,00,000

Y=$\frac{12,00,000}{5}$= 2,40,000

Average stock = $\frac{\text{Opening stock +Closing stock}}{2}$

=$\frac{\text{Rs29,000 +Rs.31000}}{2}$ =Rs. 30,000

Inventory Turnover Ratio (ITR) = $\frac{\text{Cost of goods sold}}{\text{Average stock}}$

= $\frac{\text{Rs.2,40,000}}{\text{Rs.30,000}}$ = 8 times

IF the stock amount is not given but relation between them by means of equation we find out Opening stock &Closing stock

Example : A company's Stock Turnover Ratio is 5 times. Stock at theend is Rs20,000 more than at the beginning. Sales are Rs 8,00,000 . rate of Gross profit is 25% on Cost .Find out stock

Cost of goods sold =Sales –Gross Profit)

Let the Cost of goods sold is C

Then $C = Rs\ \frac{8,00,000 - C}{4}$

$= Rs\ 8,00,000 = C + \frac{C}{4}$

$= Rs8,00,000 = \frac{5C}{4}$

$C = Rs.8,00,000 \times \frac{4}{5} = Rs.6,40,000$

Let the Opening stock is y the closing stock is = y+ Rs. 20,000

Average stock = $\frac{\text{Opening stock +Closing stock/}}{2}$

= y+ y+ Rs. 20,000 /2

Stock Turnover Ratio = $\frac{\text{Cost of goods sold}}{\text{Average stock}}$

$5 = \frac{Rs.6,40,000}{\frac{y + y + Rs.20,000}{2}}$

5y +5y +1,00,000 = Rs. 12,80,000

10y = Rs. 12,80,000 – Rs.1,00,000

$Y = \frac{11,80,000}{10} == Rs.1,18,000$

So opening stock is Rs.1,18,000 and closing stock isis Rs.1,18,000 + Rs.20,000= Rs.1,38,000

8.Debtors Turnover Ratio or Receivable Turnover Ratio : Ratio of net credit sales to average trade debtors is called debtors turnover ratio. It is also known as receivables turnover ratio. This ratio is expressed in times.

Accounts receivables is the term which includes trade debtors and bills receivables.

Following formula is used to calculate debtors turnover ratio:

Receivables turnover ratio=$\frac{\text{Annual net credit sales}}{\text{Average accounts receivables}}$

Or $\frac{\text{Annual net credit sales}}{\text{Average debtors}}$

Where accounts receivables = Trade debtors + Bills receivables

Example: Credit sales Rs.25,000; Return inwards Rs.1,000; Debtors Rs.3,000; Bills Receivables Rs.1,000.Calculate debtors turnover ratio

Calculation: Debtors Turnover Ratio = Net Credit Sales / Average accounts receivables

Net Credit Sales = Credit sales-sales return = Rs. 25000 – Rs.1,000 = Rs. 24,000Debtors Turnover Ratio = Annual net credit sales / Average accounts receivables

$= Rs.\frac{24,000}{4} = 6$ times

Significance of the Ratio:

Accounts receivable turnover ratio or debtors turnover ratio indicates the number of times the debtors are turned over a year. This shows after how much time the funds are collected on account of credit sales The higher the value of debtors turnover the more efficient is the management of debtors or more liquid the debtors are. Similarly, low debtors turnover ratio implies inefficient management of debtors or less liquid debtors. It is the reliable measure of the time of cash flow from credit sales.

The term Debtor Collection Period indicates the average time taken to collect trade debts. In other words, a reducing period of time is an indicator of increasing efficiency.

$$\text{Debtor Collection Period} = \frac{\text{Average Debtors}}{\text{Credit Sales}} \times 365 \ (= \text{No. of days})$$

$$\text{Or} \quad \text{Debtor Collection Period} = \frac{\text{Average Debtors}}{\text{Credit Sales}} \times 12 \ (= \text{No. of months})$$

$$\left(\text{Average debtors} = \frac{\text{debtors at the beginning of the year + debtors at the end of the year,}}{2}\right.$$

$$\text{Average Collection Period} = \frac{12}{\text{Debtors Turnover Ratio (in months)}} \text{ or}$$

$$\frac{365}{\text{Debtors Turnover Ratio (in days)}}$$

Credit sales can be calculated as

Net Credit sales =Cash received from debtors + Closing debtors – opening debtors

Example : Calculate Debtors Turnover Ratio and debt collection period from the following closing debtors are Rs. 40,000 credit sales 25% of cash sales closing debtors are Rs. 60,000.Total sales are2,00,000

Total sales = credit sales + cash sales

Let cash sales are A

$$\text{Total sales} = \text{Rs. } 2,00,000 = A + \frac{25\ A}{100}$$

$$= \text{Rs. } 2,00,000 = A + \frac{A}{4}$$

$$A = \text{Rs.}1,60,000 \text{ then credit sales are} = \frac{\text{Rs.}1,60,000}{4} = \text{Rs.}40,000$$

$$\text{Average Debtors} = \frac{\text{Closing debtors + opening debtors}}{2}$$

$$= \frac{\text{Rs.}40,000 + \text{Rs.}60,000}{2} = \quad = \text{Rs.}30,000$$

$$\text{Debtors Turnover Ratio} == \frac{\text{Annual net credit sales}}{\text{Average debtors}}$$

$$= \frac{\text{Rs.}40,000}{\text{Rs.}30,000} = 1.33 \text{ times}$$

Debt Collection Period = $\frac{\text{Average Debtors}}{\text{Credit Sales}}$ x 12 (no. of months)

= $\frac{\text{Rs.30,000x12}}{\text{Rs.40000}}$=9 months

Alternatively Debt Collection Period = $\frac{12}{\text{debtors turnover ratio}} = \frac{12}{1.33}$ =9 months

9.Working Capital Turnover Ratio: Working capital turnover ratio indicates the velocity of the utilization of net working capital.This ratio represents the number of times the working capital is turned over in the course of year . It shows activity of Working capital

Working Capital Turnover Ratio = $\frac{\text{Cost of Sales}}{\text{Net Working capital}}$

alternatively

Working capital turnover ratio = $\frac{\text{Cost of sales}}{\text{Average net working capital}}$

Where,

Cost of sales = Opening stock + Net purchases + Direct expenses – Closing stock

Net working capital = Current assets – Current liabilities

Average of networking capital is calculated, as usual, opening + closing dividing by 2. However, if the information regarding cost of sales and opening balance of networking capital is not available then the formulae should be substituted as:

$\frac{\text{Net sales}}{\text{Net working capital}}$

Objective : This shows whether or not working capital has been effectively utilised

A high ratio indicates efficient utilization of working capital But a very high working capital turnover ratio may also mean lack of sufficient working capital which is not a good situation.

Example:

Cash	10,000
Bills Receivables	5,000
Sundry Debtors	25,000
Stock	20,000
Sundry Creditors	30,000
Cost of sales	150,000

Calculate working capital turnover ratio

Calculation:

Working Capital Turnover Ratio = $\frac{\text{Cost of Sales}}{\text{Working Capital}}$

Current Assets = Rs.10,000+Rs.5,000+Rs.25,000+Rs.20,000 = Rs.60,000

Current Liabilities = 30,000

Net Working Capital = Current Assets - Current Liabilities = Rs.60,000-Rs.30,000 = Rs.30,000

So the woking Capital Turnover Ratio = 150,000/30 = 5 times

10. Creditors Turover Ratio : This is also called as **Payable Turnover Ratio... It is relationship between net credit purchase and total payable or average payable. Total payables are bills payable and creditors**

Creditors Turnover Ratio= Net credit purchases/totalor average payable

Average payable = (Opening creditors + Opening bills payable)+(closing creditors + closing bills payable)/2

Average payment period = total or average payable/Net credit purchases x No of months or days in year

Objectives : High ratio shows strict terms by suppliers and quick payment after a short period and low ratio shows liberal credit terms granted by supplier.

Example : Calculate Creditors Turnover Ratio and debt payment period from the following closing creditors are Rs. 4,50,000 and opening creditors are Rs. 1,50,000 and closing bills payable are Rs.50,000 & opening bills payable are Rs. 1,50,000 .Total purchases are Rs. 21,00,000 ,purchase return Rs. 1,00,000 . Cash purchases are Rs. 4,00,000

Creditors Turnover Ratio $= \frac{\text{Net credit purchases}}{\text{total or average payable}}$

Net credit purchases = total purchases –cash purchases –purchase return

= Rs 21,00,000 – Rs.4 ,00,000 – Rs.1,00,000 = Rs 16,00,000

Average payable = $\frac{\text{closing creditors + opening creditors +closing bills payable + opening bills payable}}{4}$

$= \frac{\text{Rs. 4,50,000 + Rs. 1,50,000 + Rs.50,000 + Rs. 1,50,000}}{2} = \frac{\text{Rs.8,00,000}}{2}$

= Rs. 4,00,000

Creditors Turnover Ratio $= \frac{\text{Net credit purchases}}{\text{total or average payable}}$

$= \frac{\text{Rs 16,00,000}}{\text{Rs. 4,00,000}}$ = 4 times

<u>**Profitability ratios**</u> are used to **assess a business' ability to generate earnings as compared to expenses over a specified time period.** Profitability is overall measure of efficiency and performance of business. The important ratios are Gross Profit Ratio , Operating Profit Ratio,Net Profit Ratio , Return on Investment, Earning Per Share, Dividend Per Share and Price Earnings Ratio

<u>11.Gross Profit Ratio</u> :The gross profit ratio is **relationship of gross profit to net sales**. This ratio shows how a company controls the cost of its inventory and the manufacturing of its products and subsequently pass on the costs to its customers. The larger the gross profit ratio, the better for the company.

The calculation is:= $\frac{\text{Gross Profit}}{\text{Net Sales}} \times 100$

Net Sales = Gross Sales (cash as well as credit sales) –Sales Return

Gross Profit = Net Sales – Cost of goods sold

In the case of a trading business

Cost of goods sold =opening stock + purchases - closing stock + all direct expenses relating to purchases.

In the case of manufacturing concern

Cost of goods sold =, cost of raw materials + wage +, direct expenses +all manufacturing expenses.(the expenses charged to profit and loss account or operating expenses are excluded from the calculation of cost of goods sold)

Objective :**Gross profit ratio may be indicated to what extent the selling prices of goods per unit may be reduced without incurring losses on operations. It reflects efficiency with which a firm**

produces its products. As the gross profit is found by deducting cost of goods sold from net sales, higher the gross profit better it is.

There is no standard GP ratio for evaluation. It may vary from business to business. However, the gross profit earned should be sufficient to recover all operating expenses and to build up reserves after paying all fixed interest charges and dividends.

Example : In a business cash sales are Rs.72,000 and credit sales are Rs. 8,000 Cost of goods sold is Rs. 60,000 find out gross profit ratio.

Net sales = cash sales + credit sales = Rs. 72,000 + Rs. 8,000 = Rs. 80,000

Cost of goods sold = Rs.60,000

Gross Profit = Net Sales – Cost of Goods Sold = Rs.80,000 – Rs 60,000 = Rs.20,000

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{net sales}} \times 100 = \frac{\text{Rs.}20{,}000}{\text{Rs. }80{,}000} \times 100$$

$$= 25\%$$

12.Operating Ratio : This is calculated to find out relationship between operating cost and net sales. It excludes non operating income and expenses which have no impact on production and sales for example : interest and dividend received on investment, interest on loan and debentures and profit and loss on sales of fixed assets.

$$\text{Operating Ratio} = \frac{\text{Cost of Goods Sold + Operating Expenses}}{\text{Net Sales}} \times 100 \quad \text{OR}$$

$$\text{Operating Ratio} = \frac{\text{Operating Cost}}{\text{Net Sales}} \times 100$$

Operating Expenses = Administrative Expenses + Selling and Distributing Expenses + Interest of Long Term loans + Discount Allowed and Bad Debts

Significance : **This shows operational efficiency of business & percentage of sales absorbed by cost of sales and operating expenses. Lower ratios is considered better because it means higher margin to meet interest, dividend etc.**

Example : From the details given below calculated operating ratio:

(i) Gross Profit Ratio
(ii) Stock Turnover Ratio
(iii) Operating Ratio
(iv) Debtors Turnover Ratio

	Rs.
Sales	1,50,000
Cost of goods sold	1,20,000
Opening Stock	29,000
Closing Stock	31,000
Debtors	16,000
Operating Expenses	16,000
Net Fixed assets	1,10,.000

$$\text{Operating Ratio} = \frac{\text{Cost of Goods Sold + Operating Expenses}}{\text{Net Sales}} \times 100$$

$$= \frac{1,20,000 = 16,000}{1,50,000} \times 100 = 90.67\%$$

Operating Profit Ratio measures the relationship between Operating Profit and Net Sales.

$$\text{Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Net Sales}} \times 100$$

Operating Profit = Net Profit + Non-Operating Expenses – Non Operating Income.

Operating Ratio + Operating Profit Ratio = 100

Operating Profits = Net Sales-Operating Cost

Operating Profits = Gross Profit-Operating Expenses

Illustration 1

Compute Operating Profit Ratio from the following

	₹
Net Profit	6,00,000
Less on Sale of furniture	20,000
Profit on Sale of Investment	60,000
Interest paid on loan	60,000
Interest from Investment	40,000
Sales	11,60,000

Solution :- Non-Operating Expenses = Interest on Loan+Loss on sale of furniture

= ₹ 60,000+20,000 = ₹ 80,000

Non-Operating Income = Interest Received on Investment + Profit on sale of Investment

= ₹ 40,000+60,000 = ₹ 1,00,000

Operating Profit = Net Profit+Non Operating Expenses - Non-Operating Income

= 6,00,000+80,000-1,00,000= ₹ 5,80,000

Operating profit Ratio = Operating Profit/Net Sales x100

= 5,80,000/11,60,000x100= 50%

Illustration 2

Calculate Operating Profit ratio when Net Sales are ₹ 10,00,000, Gross Profit is 20% &

Operating Expenses ₹ 20,000

Solution :- Gross Profit = 20/100x10,00,000 = 2,00,000

Operating Profit = Gross Profit - Operating Cost

= 2,00,000-20,000 = ₹ 1,80,000

Operating Profit Ratio = Operating Profit/Net Sales x100

= 1,80,000/10,00,000x100 = 18%

Operating Profits can be calculated by formula

Net Operating Profits = Net Sales - (Opening Stock + Purchase + administrative expenses + Selling Expenses - Closing Stock)

13.Net Profit Ratio :Net Profit Ratio is the most often margin ratio used. The Net Profit Ratio shows how much of each sales shows up as net income after all expenses are paid. For example, if the net profit margin is 5%, that means that 5 cents of every Rupee.is profit. It is relationship between Net Profit and Net Sales in terms of percentage.

Net Profit = Gross Profit – indirect cost (Administrative, Marketing and non- operating expenses + non- operating incomes.

$$\text{Net Profit ratio} = \frac{\text{Net Profit}}{\text{Total Sales}} \times 100$$

Net Profit Ratio is calculated by taking profit before tax (PBT) OR Profit after tax(PAT)

$$\frac{\text{Profit Before Tax}}{\text{Net Sales}} \times 100$$

OR

$$\frac{\text{Profit After Tax}}{\text{Net Sales}} \times 100$$

Significance: **The net profit margin measures profitability after consideration of all expenses including taxes, interest, and depreciation. It is indicator of Overall Operational Efficiency. Higher Ratio is better but it should be compared with the industry standard.**

Example :Total Sales = Cash Sales + Credit Sales

Cash Sales = Rs.2,00,0

Credit Sales = 90 % of total sales

It means cash sales were 10% of the total sales

$$\text{Total Sales} = \frac{\text{Cash Sales} \times 100}{10} = \frac{\text{Rs.}2,00,000 \times 100}{10} = \text{Rs.}20,00,000$$

$$\text{Gross Profit} = \text{Rs.}20,00,000 \times \frac{25}{100} = \text{Rs.}5,00,000$$

Net Profit : Gross Profit – Indirect Expenses

= Rs.5,00,000 – Rs. 20,000 = Rs. 4,80,000

$$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Net Sales}} \times 100 = \frac{\text{Rs.}4,80,000}{\text{Rs.}20,00,000} \times 100 = 24\ \%$$

14.<u>Return on investment or Return on Capital Employed Ratio</u>

Return on Capital Employed Ratio establishes the relationship of Profit (Profit means profit before interest and tax) with capital employed. This ratio is calculated normally in the case of companies as :

$$\frac{\text{Profit Before Interest, Tax and Dividend}}{\text{Capital Employed}} \times 100$$

The ratio is usually expressed in percentage.

Capital employed = Share capital (both preference and equity) + Reserves and Surplus + Long-term loans – Fictitious assets (like preliminary expenses) –non operating assets like investment .

Note :Non operating assets are excluded while determining the capital employed so income from investment should also be excluded from profit.

Significance : **This ratio measures the efficiency resources used in the business. Higher Ratio if favourable and shows firm ability to use available resources efficiently to generate income.it judges overall performance of enterprise or its departments.**

From the following details, calculate Return on investment-

Particulars	Rs.
Gross Profit	2,60,000
Selling and Distribution Expenses	72,000
10% Debentures	1,50,000
Tax	30,000
Fixed Assets	6,50,000
Current Assets	3,00,000
Current Liabilities	1,20,000

Return on investment = $\frac{\text{Profit before interest, Tax and Dividend}}{\text{Capital Employed}} \times 100$

=Rs. 2,60,000 – Rs. 72,000 = Rs,1,88,000

Capital Employed = Net fixed Assets = Working Capital (Current Assets – Current Liablities)

= Rs.6,50,000 + (3,00,000 – 1,20,000) = Rs. 6,50,000 + 1,80,000 = Rs.8,30,000

Return on Investment = $\frac{\text{Rs.}1,88,000}{\text{Rs.}8,30,000} \times 100 = 22.65\%$

Misc Problem : With the help of the given information, calculate any three of the following ratios :

(i) Oerating Ratio (ii) Current Ratio (iii) Stock Turnover Ratio and (iv) Debt Equity Ratio

Particulars	**₹**
Equity Share Capital	5,00,000
9% Preference Share Capital	4,00,000
12% Debenture (Non-Current Liabilities)	2,40,000
General Reserve	40,000
Sales	8,00,000
Opening stock	48,000
Purchases	5,00,000
Wages	30,000
Closing Stock	52,000
Selling & Distribution Expenses	6,000
Other Current Assets	2,00,000
Current Liabilities	1,50,000

Sol. :

Operating Ratio = Operating Cost/Net Sales x 100

Operating Cost : Cost of Goods sold + Selling & distribution Expenses

Cost of Goods sold = opening stock+purchase + wages (Direct Expenses) - Closing stock

= Rs.48,000+Rs.5,00,000+Rs.30,000-Rs.52,000 = Rs.5,26,000

Operating Cost= Rs.5,26,000+Rs.6,000 = Rs.5,32,000

Operating Ratio = Rs.5,32,000/Rs.8,00,000x100 = 66.5%

Current Ratio = Current Assets/Current Liabilities

Current Assets = Stock + Other Current Liabilities = Rs.52,000+Rs.2,00,000 = Rs.2,52,000

Current Ratio = Rs.2,52,000/Rs.1,50,000= 1.68:1

Stock Turnover Ratio = Cost of goods sold/Average Stock

Average Stock = Opening Stock+ Closing Stock/2 = Rs.48,000+Rs.52,000= Rs.50,000

Stock Turnover Ratio = Rs.5,26,000/Rs.50,000= 10.52 times

Debt Equity Ratio = Debts (Long Term Loan)

Equity Shareholder's Funds

=Rs.2,40,000/Rs.9,40,000 = 255:1

Advantage

1. Judging operating efficiency of Business
2. Useful for casting
3. Useful in location weak points

4. Useful in Inter and intra firm comparison

Limitations :

1. No standard definition

2. If different accounting policies are followed comparison is meaningless

3. Ignores qualitative factors

Interest Coverage Ratio : This ratio establishes relationship between the net profit before interest & tax and interest payable on long term debts. Since interest is change on profit net profit taken to calculate ratio is before interest & tax. It determines case with which a company can pay interest on outstanding debt.

CHAPTER 12

CASH FLOW STATEMENT

Meaning : It is a statement that shows flow (inflow or outflow) of cash and cash equivalents during a given period of time.

As per Accounting Standard-3 (Revised) the changes resulting in the flow of cash & cash equivalents arises on account of three types of activities i.e.

(1) Cash flow from Operating Activities.

(2) Cash flow from Investing Activities.

(3) Cash flow from Financing Activities.

Cash : Cash comprises cash in hand and demad deposits with bank.

Cash equivalents : Cash equivalents are short-term higly liquid investment that are readily convertible into known amount of cash and which are subject to an insignificant risk of change in the value (of shotterm investment). Generally theses investment have a maturity period of less than three months.

Some example of cash equivalent : Bank overdraft, cash credit, short-term deposits, maketable securities, treasury bills, commercial papers, money market funds (mutual fund), investment in preference shares if redeemable within three months and ensure that there is no risk of the failure of the company.

Some type of transaction which are considered movement between cash and cash equivaletns are given below :

1. Cash deposited into bank.
2. Cash withdrawn from bank.
3. Sale of cash equivalent securities (e.g. sale of short term investment, sale of commercial papers)
4. Purchase of cash equivalent securities (e.g. Purchase of short-term investment, Purchase of Treasury bills).

The above types of transaction are part of cash and cash equivaltens, so these are included in opening and closing cash and cash equivalent only. So these types of transanction not be included in cash from different activities like operating, investing, financing activities.

Preparation of cash flow statement :

Cash flow from operating activities	________
Cash flow from investing activities	________
Cash flow from financing activities	________
Net increase/decrease in cash & cash equivalent	(Total of the above three activities)
Add : Cash & Cash equivalent in the beginning of the year (Given in opening balance sheet)	________
Cash & Cash equivalent at the end of the year	________

Note : The student should ensure that the cash & Cash equivalent at the end of the year as calculated above will be same as cash & cash equivalent given in closing balance sheet

OBJECTIVES OF CASH FLOW STATMEMENT :

1. To ascertain how mach cash or cash equivalents have been **generated** or **used** in **different activities** i.e. operating/investing/financing activity.
2. To ascertain the **net changes in cash and cash equivalents.**
3. To assesss the **causes of difference** between actual cash & cash equivalent and related net earning/income.
4. To help in **formulation of financial policies** such as dividend policy, fixed assests policy, capital structure related policy.
5. To help in **short-term financial planing**.
6. To ascertain the **liquidity** of enterprises

LIMITATIONS OF CASH FLOW STATEMENT

1. Non cash transaction are not taken into consideration like sahres or debentures issued to vendores, deprecaition charged during the year.
2. It is a statement related with past data.
3. It is not used for judging the profitability of enterprises.
4. Accrual accounting concept is ignored in this statement e.g. credi sales, credit purchases, outstanding expesnes, accrued income are not included.

Computation of Cash flow from different activities.

(1) Cash flow from operating activities : operating activities are the main revenue generating activities of the enterprises. It includes tha transaction also which are not included in investing and financing activities.

Accounting standard -3 (Revised) has suggested two methods of computing net cash from operating activities (A) Direct Method (B) Indirect Method.

(C) Indirect Method of calculating the cash flow from Operating Activities :

Under this method Net Profit Before Tax and Extra-ordinary Item is the starting point further calculations.

Calculations of Net Profit Before Tax Extra - ordinary Item :

Difference between closing balance and opening balance of profit & loss A/c	____
Add : 1. Proposes divident for current year	____
2. Interim Divident paid during the year.	____
3. Profit Transferred to Reserve	
(If reserve of current year increased from previous year)	____
4. Provision for Taxation made durning the year	____
Less : 1 Refund of Tax credited to P & L A/c	____
2. Extraordinary item if any Credited to P & L A/c	____
Net Profit Before Tax and Extra-ordinary Item	

Extraordinary items : These items are not related to normal business operation and not included in investing and financing activities

Format for Cash Flow from Operation Activities

Particulars	(₹)
1. Cash Flow from Operating Activities	
(A) Net Profit Before Tax and Extra-ordinary Item	______
Adjustment for non-cash and non-operating itmes	
Add : 1. Derpreciation charged during the current year	
2. Preliminay expesnes, Discount on issue of shares and debentures written off	
3. Goodwill, Patents and Trademark Amortised (written off)	
4. Interes on Borrowing and Debentures.	
5. Loss on Sale of Fixed Assets	______
Less : 1. Interest income	
2. Dividend Income	
3. Rental income	______
4. Profit on sale of Fixed Assets	______
(B) Operating Profit before Working Capital changes	
Add : Increase in Current Liabilities and	______
Decrease in current Assets (other than cash and cash equivalent)	
Less : Increase in current Assets (other than cash and cash equivalent) and Decrease in current liabilities	
(C) Cash Generated from operations	
Less : Income tax paid (Net of Refund received)	
(D) Cash flow before Extraordinary item	
Extraordinary items +/-	
(E) Net Cash From (or used in) Operating Activities	

For the calculation of Proposed Dividend during the current year the proposed dividend account is to be prepared as follows :

Dr. Cr.

Proposed Dividend Account

Date	Particular	₹	Date	Particulars	₹
	To (Dividend payable A/c)	______		By Balance b/d	______
	To balance c/d	______		By Profit & Loss A/c (Proposed dividend during the current year)	______

For the calculation of Provision for Taxation made during the current year the Provision for taxation account is to be prepared as follows:

Dr. Provision for Taxation Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Bank A/c (Tax Paid during the current year)	………		By Balance b/d	…………
	To balance c/d	………..		By Profit & loss A/c (Provision for taxation made during the current year)	……………

Illustration 2.X ltd made a profit of ₹ 1,00,000 after considering the following items:

1.Depreciation on fixed assets ₹ 20,000. 2. Writing off preliminary expenses ₹ 10,000

3.Loss on sale of furniture ₹ 1,000. 4.Provision of Taxation ₹ 1,60,000.

5. Transfer to General reserve ₹ 14,000 6. Profit on sale of Machinery ₹ 6,000.

The following additional information is available to you:

Particulars	31-03-2007 (₹)	31-03-2008 (₹)
Debtors	24,000	30,000
Creditors	20,000	30,000
Bills Receivables	20,000	17,000
Bills Payables	16,000	12,000
Prepaid Expenses	400	600

Calculate Cash Flow from Operating Activities.

Solution. Calculation of Net Profit Before Tax And Extra-ordinary Item

Net Profit (Given)	₹1,00,000
Add: Provision for Taxation	₹1,60,000

Transfer to general reserve	₹ 14,000
Net Profit Before Tax And Extra-ordinary Item	₹2,74,000

CASH FLOW FROM OPERATING ACTIVITIES

Particulars	₹	₹
Net Profit Before Tax And Extra-ordinary Item		2,74,000
Adjustment for non-cash and non-operating items		
Add: Depreciation on fixed assets	20,000	
Preliminary expenses written off	10,000	
Loss on sale of furniture	1,000	31,000
		3,05,000
Less: Profit on sale on machinery	6000	(6,000)
Operating Profit before working capital changes		2,99,000
Add: Increase in creditors	10,000	
Decrease in Bills Receivables	3,000	13,000
		3,12,000
Less: Increase in Debtors	6,000	
Increase in Prepaid Expenses	200	
Decrease in Bills Payables	4,000	(10,200)
Cash generated from operation		3,01,800
Less: Income tax Paid		(1,60,000)
Cash Flow from Operating Activities		1,41,800

2. Cash Flow from Investing Activities:

Investing activities are those activities which related to the acquisition (Buying) and disposal (selling) of fixed assets and investment(other than cash equivalents). It also includes income from fixed assets and investment like Rent Received, interest received on investment, dividend received on investment in shares and mutual funds.

Inflows of Cash : (plus items)	Outflows of Cash(minus items)
1. Cash Received from sales of fixed Assets. 2. Cash Received from sales of Investment. 3. Interest Received. 4. Dividend Received. 5. Rent Received	1. Cash paid for purchase of fixed assets. 2. Cash paid for purchase of Investment. 3. Cash paid for purchase of intangible fixed assets like goodwill, patents and copy writes.

For the calculation of sale or purchases of fixed assets and investment, the following accounts are prepared:1. Fixed Assets Account 2. Investment Account.

Fixed Assets Account: Fixed assets may be prepared by two methods

(a) at written down value method(when provision for depreciation account/accumulated depreciation account is not maintained)

Dr. Fixed Assets Account (at written down value) Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d			By Bank A/c(Sale of investment)	
	To Bank A/c (additional purchase)			By Depreciation A/c (Dep. on fixed assets sold)	
	To Profit &Loss A/c (profit on sale of fixed assets)	---------		By Profit & loss A/c (Loss on sale of fixed assets)	-------
				By Depreciation A/c (Current year dep. on remaining fixed assets)	
				By balance c/d	----------

Fixed Assets (at cost) : when provision for depreciation account or accumulated depreciation account separately maintained. In this method two account name fixed assets account and provision for reciation account is maintained.

Dr. Fixed Assets Account (at original cost) Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d			By Bank A/c(Sale of investment)	
	To Bank A/c(additional purchase)			By Depreciation A/c	
	To Profit &Loss A/c	---------		(Dep. on fixed assets sold)	
	(profit on sale of fixed assets)			By Profit & loss A/c	
				(Loss on sale of fixed assets)	
				By balance c/d	----------

Dr. Provision for Depreciation Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Fixed Assets A/c (total Depreciation on fixed assets sold)	..		By Balance b/d	....
	To balance c/d	………..		By Profit & loss A/c	....
				(Depreciation charged on fixed assets during the current year)	

Preparation of Investment Account:

Dr. Investment Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	________		By Bank A/c (Sale of investment)	________
	To Bank A/c (additional purchase)	________		By Profit & loss A/c	________
	To Profit &Loss A/c	---------		(Loss on sale of Investment)	
	(profit on sale of Investment)			By balance c/d	________

Illustration 3. From the following information calculate cash flow from investing activities:

Particulars	31-03-2010(₹)	31-03-2011(₹)
Machinery (at Cost)	5,00,000	5,50,000
Accumulated Depreciation	1,00,000,	1,20,000
Patents	2,00,000,	1,20,000
Goodwill	1,50,000	2,00,000
Investment	2,50,000	5,00,000

Additional information:

(i) During the year , a machine costing ₹ 50,000 with its accumulated depreciation of ₹ 25,000 was sold for ₹20,000.

(ii) Patents were written off to the extent of ₹ 60,000 and some patents were sold at a profit of ₹ 10,000.

(iii) 40% of the investment held in the beginning of the year were sold at 10% Profit.

(iv) Interest received on investment ₹ 25,500.

(v) Dividend received on investment ₹ 8,500.

(vi) Rent received ₹ 5,000.

Solution:

Cash Flow from Financing Activities

Particulars	₹
Proceeds from sale of machinery	20,000
Proceeds from sale of investment	1,10,000
Proceeds from sale of Patents	30,000
Cash paid of purchase of machinery	(1,00,000)
Cash paid of purchase of Investment	(3,50,000)
Interest Received	25,500
Dividend Received	8,500
Rent Received	5,000
Net Cash Used in Investing Activities	(2,51,000)

Working Notes:

Dr. Investment Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	2,50,000		By Bank A/c (Sale of investment)	1,10,000
	To Profit &Loss A/c(profit on sale of Investment)	10,000			
	To Bank A/c (additional purchase)	3,50,000		By balance c/d	5,00,000
		6,10,000			6,10,000

Dr. Machinery Account (at original cost) Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	5,00,000		By Bank A/c(Sale of Machinery)	20,000
	To Bank A/c(additional purchase)	1,00,000		By Depreciation A/c (Dep. on Machinery sold)	25,000
				By Profit & loss A/c (Loss on sale of Machinery)	5,000
				By balance c/d	5,50,000
		6,00,000			6,00,000

Dr. Provision for Depreciation Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Machinery A/c (total Depreciation on machinery sold)	25,000		By Balance b/d	1,00,000
	To balance c/d	1,20,000		By Profit & loss A/c(Depreciation charged on machinery during the current year)	45,000
		1,45,000			1,45,000

Dr. Patents Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	2,00,000		By Bank A/c	30,000
	To Profit &Loss A/c	10,000		(Sale of Patents)	
	(profit on sale of Patents)			By Profit&Loss A/c	60,000
				(Written off)	
				By balance c/d	1,20,000
		2,10,000			2,10,000

4. **Cash Flow from Financing Activities:**

Financing activities are those activities that result in the changes in size and composition of the share capital (equity and preference) and borrowed fund of the business enterprises. Generally cost related to these funds also included in financing activities like interest paid on loan and debenture and dividend paid on equity and preference share capital.

Inflows of Cash : (plus items)	Outflows of Cash(minus items)
1.Cash Received from Issue of equity shares capital. 2. Cash Received from Issue of preference shares capital. 3.Cash Received from taking long-term loan.	1Cash paid for repayment of long-term loan. 2.Redemption of Preference share capital in cash 3.Redempton of Debenture in cash 4. Buy back of Equity shares. 5. Interest paid on long-term loan and debentures. 6. Final Dividend paid 7. interim dividend paid

Illustration 4.From the following information, calculate the net cash flow from Financing Activities:

Particulars	31-03-2010(₹)	31-03-2011(₹)
Equity Share Capital	10,00,000	16,00,000
9% Debentures	1,50,000,	1,00,000
Proposed Dividend	3,00,000,	3,50,000
Dividend Payable	--------	50,000
10% Preference Share Capital	2,00,000	3,00,000

Additional information:

1. Interest paid on Debentures ₹ 12,500.
2. During the year 20010-2011, company issued bonus shares to equity shareholders in the ration of 2:1 by capitalizing reserve.
3. The interim dividend of ₹ 75,000 has been paid during the year.
4. 9% Debentures were redeemed as 5% premium.
5. 10% preference shares were issued at 2% discount.

Solution:

Cash Flow from Financing Activities

Particulars	₹
Proceeds from Issue of Equity Share Capital	1,00,000
Proceeds from Issue of 10%Preference Share Capital (1,00,000x98%)	98,000
Cash paid for Redemption of 9% Debentures (50,000x 105%)	(52,500)
Interest paid on Debentures	(12,500)
Interim Dividend paid	(75,000)
Final Dividend paid (3,00,000-50,000)	(2,50,000)
Net Cash Used in Financing Activities	1,92,000

Note: 1.Bonus shares issued to equity shareholder are not to be shown in the cash flow statement because there is no flow of cash by this activity.

2. If any other information is not given in the question about final dividend paid amount then the previous year proposed dividend is assumed as dividend payable in current year. Current year proposed dividend amount is assumed as proposed dividend in current year and to be added in operating activities to calculated net profit before tax and extraordinary item.

3. Previous year proposed dividend - unpaid dividend = final dividend paid during the current year is cash used in financing activities.

Comprehensive :

Illustration No. 5 : Prepare a cash flow statement from the following Balance Sheet of Dev' Ltd. :-

Particulars		**31.03.2011 (₹)**	**31.03.2012 (₹)**
I. Equity and Liabilities			
1. Shareholder's funds :			
(a) Share Capital		65	65
(b) Reserve and Surplus	1	42.5	25
2. Share Application money pending allotment		–	–
3. Non-current Liabilities		–	–
4. Current Liabilities		–	–
Trade Payables		10.5	7.7
Total		118	77.7
II. Assets			
1. Non-current Assets			
(a) Fixed Assets		83	46.7
2. Current Assets			
(a) Inventories		13	11
(b) Trade Receivables		19.5	18
(c) Cash and Cash equivalents		2.5	2
Total		118	77.7

Notes to Account No. 1

Particulars	**31.03.2012 (₹)**	**31.03.2011 (₹)**
Reserve and Surplus		
1. Shareholder's funds :		
General Reserve	27,500	15,000
Profit and Loss A/c	15,000	10,000
Total	42,500	25,000

Additional Information :

(1) Depreciation on fixed assets for the year 2011-12 was Rs.14,700

(2) An interim divided of Rs.7000 has been paid to the shareholders during the year.

Solution : Calculation of Net Profit before tax and Extra ordinary item :

Net Profit as Per Profit & Loss A/c (15000-10000)	5,000
Add : Transfer to General Reserve (27,500-15,000)	12,500
Interim Dividend Paid during the year	7,000
Net Profit Before Tax and Extraordinary item	24,500

Cash Flow Statement
for the year ended 31st March 2012

Particulars

	(Rs.) 31.03.2012	**(Rs.) 31.03.2011**
(A) Cash Flow from Operating Activities :		
Net Profit before tax and Extra-ordinary item	24,500	
Adjustment for Non Cash and Non-operating item :		
Add : Depreciation on fixed Assets	14,700	
Operating Profit before Working Capital Changes		39,200
Adjustment for Working Capital Changes :		
Add : Increase in Trade Creditors	2,800	
Less : Increase in Stock	(2,000)	
Increase in Debtors	(1,500)	(700)
Cash flow from Operating Activities		38,500
(B) Cash Flow from Investing Activities		
Purchase of Fixed Assets	(51000)	
Net Cash used in Investing Activities		(51000)
(C) Cash flow from financing Activities		
Proceeds from issue of equity share capital	20,000	
Interim Dividend Paid	(7,000)	
Net Cash from Financing Activities	13,000	13,000
Net Increase in Cash and Cash Equivalents		500
Cash and Cash equivalents in the beginning of the year		2000
Cash and Cash equivalents at the and of the year		2500

Dr. **Fixed Assets A/c (on original cost)** **Cr.**

Date	Particulars	Rs.	Date	Particulars	Rs.
	To Balance b/d	46,700		By Depreciation A/c	14,700
	To Bank A/c	51,000		(Current year dep. on remaining fixed assets)	
	(Additional purchase)			By balance c/d	83,000

Deletions from the Syllabus

Meaning of Private Placement of Shares and Employee Stock option Plan.

Writing Off Loss on Issue of Debentures.

Redemption of Debentures through purchase in Open Market.

Fixed Assets Turnover Ratio.

Current Assets Turnover Ratio.

Earning Per Share

Dividend Per Share.

Price Earning Ratio.

New Additions in the Syllabus

Guarantee of Profits.

Accounting for Private Placement of Shares.

Interest on Debentures.

Balance Sheet of a Company in the prescribed form with major headings and sub headings (as per Revised Schedule VI Part I of the Companies Act, 1956).

Interest Coverage Ratio.

Operating Profit Ratio.

Supplementary material of accountancy

List of chapters

Accountancy class XII

Partnership: Fundamentals

Guarantee of profits

An assurance is given to a partner that a <u>minimum amount</u> is given to him irrespective of profits

The firm or the partner who has given the guarantee is DEBITED

The partner to whom guarantee has been given is CREDITED.

This guarantee can be given in any one of the following forms----

(Guarantee of minimum profits to a partner by firm)

A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1 with a guarantee of minimum profits to C for ` 15,000. Total profits of the firm for the year ended on December 31, 2012 amounted ` 60,000. Prepare a profit and loss appropriation account to show the distribution of profits as per terms of partnership deed.

When Guarantee of minimum profit to a partner is given by the firm, we can solve the question in two different methods.

METHOD 1-----<u>Out of total profits of 60,000, C has been credited with 15,000(guaranteed amount)and the balance of profit distributed among A and B in their profit sharing ratio</u>

Profit and Loss Appropriation Account

For the year ending on 31ST March, 2012

Dr. **Cr.**

Particulars	`	Particulars	`
To A's Capital A/c (3/5 of ` 45,000)	27,000	By Profit and Loss A/c (Net Profits)	60,000
To B's Capital A/c (2/5 of ` 45,000)	18,000		
To C's Capital A/c (1/6 of ` 60,000 or `15,000 whichever is more)	15,000		
	60,000		60,000

METHOD 2

<u>C has been credited for 10,000 by the firm &</u>

<u>C has been credited with 5,000 by debiting A and B in their profit sharing ratio</u>

Profit and Loss Appropriation Account

For the year ending on 31ST March, 2012

Dr. **Cr.**

Particulars	`	**Particulars**	`
To A's Capital A/c **(3/6 of ` 60,000) 30,000** **Less: Deficiency** **Borne for C (3,000)** **-------**	**27,000**	**By Profit and Loss A/c** **(Net Profits)**	**60,000**
To B's Capital A/c **(2/6 of ` 60,000)** **20,000** **Less: Deficiency** **Borne for C (2,000)** **-------**	**18,000**		
To C's Capital A/c **(1/6 of ` 60,000** **10,000** **Add: Deficiency** **Recovered from A 3,000** **Add: Deficiency** **Recovered from B 2,000** **-------**	**15,000**		
	60,000 **-------------**		**60,000** **------------**

➢ **<u>Working Note:</u>**

Minimum guarantee to C = `15,000

Less: C's actual share in profits = ` 10,000

Deficiency in profits = ` 15,000 - ` 10,000 = **5,000**

This deficiency will be borne by A and B in their profits sharing ratio i.e., 3:2.

(Guarantee of minimum profits to a partner by other partners in a specific ratio)

1. A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1 with a guarantee of minimum profits to C for ˆ 15,000. Total profits of the firm for the year ended on December 31, 2012 amounted ˆ60,000. Any excess payable to C on account of such guarantee shall be borne by A and B in equal ratio.

Prepare a profit and loss appropriation account to show the distribution of profits as per terms of partnership deed.

Solution----

<u>C has been credited by debiting firm for 10,000 &</u>

<u>C has been credited by debiting A and B in specific ratio , i.e, equal</u>

Profit and Loss Appropriation Account

For the year ending on 31ST March, 2012

Dr. **Cr.**

Particulars	**`**	**Particulars**	**`**
To A's Capital A/c (3/6 of ` 60,000) 30,000 Less: Deficiency Borne for C (2,500) -------	**27,500**	**By Profit and Loss A/c (Net Profits)**	**60,000**
To B's Capital A/c (2/6 of ` 60,000) 20,000 Less: Deficiency Borne for C (2,500) -------	**17,500**		
To C's Capital A/c (1/6 of ˆ 60,000 10,000 Add: Deficiency Recovered from A 2,500 Add: Deficiency Recovered from B 2,500 -------	**15,000**		
	60,000 **-------------**		**60,000** **------------**

❖ **<u>Working Note:</u>**

Minimum guarantee to C = ˆ15,000

Less: C's actual share in profits = ˆ 10,000

Deficiency in profits = ˆ 15,000 - ˆ 10,000 = ˆ 5,000

This deficiency will be borne by A and B in **equal ratio i.e., 1:1.**

(Guarantee of minimum profits to a partner by other partner – one partner only)

A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1 with a guarantee of minimum profits to C for ˆ 15,000. Total profits of the firm for the year ended on December 31, 2012 amounted ˆ60,000. Any excess payable to C on account of such guarantee shall be borne by A.

Prepare a profit and loss appropriation account to show the distribution of profits as per terms of partnership deed.

C has been credited by debiting firm for 10,000 &

C has been credited by debiting A only for 5,000

Profit and Loss Appropriation Account

For the year ending on 31ST March, 2012

Dr. Cr.

Particulars	ˆ	Particulars	ˆ
To A's Capital A/c (3/6 of ˆ 60,000) 30,000 Less: Deficiency Borne for C (5,000) -------	25,000	By Profit and Loss A/c (Net Profits)	60,000
To B's Capital A/c (2/6 of ˆ 60,000)	20,000		
To C's Capital A/c (1/6 of ˆ 60,000 10,000 Add: Deficiency Recovered from A 5,000 -------	15,000		
	60,000		60,000

2. A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1 with a guarantee of minimum profits to C for ˆ 15,000. Total profits of the firm for the year ended on December 31, 2012 amounted ˆ60,000. Any excess payable to C on account of such guarantee shall be borne by B.

Prepare a profit and loss appropriation account to show the distribution of profits as per terms of partnership deed.

C has been credited by debiting firm for 10,000 &

C has been credited by debiting B only for 5,000

SOLUTION:

Profit and Loss Appropriation Account

For the year ending on 31^{ST} March, 2012

Dr. Cr.

Particulars	ˆ	Particulars	ˆ
To A's Capital A/c (3/6 of ˆ 60,000)	30.000	By Profit and Loss A/c (Net Profits)	60,000
To B's Capital A/c (2/6 of ˆ 60,000) 20,000 Less: Deficiency Borne for C (5,000) -------	15,000		
To C's Capital A/c (1/6 of ˆ 60,000 10,000 Add: Deficiency Recovered from B 5,000 -------	15,000		
	60,000 -------------		60,000 ------------

❖ **Working Note:**

Minimum guarantee to C = ˆ15,000

Less: C's actual share in profits = ˆ 10,000

Deficiency in profits = ˆ 15,000 - ˆ 10,000 = ˆ 5,000

In 4 question deficiency will be borne by <u>A only</u>

<u>In 5 question deficiency to borne by B only</u>

(Guarantee of minimum profits to firm by partners)

3. A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1. The partnership deed provided the following:

1. Interest on Capital is to be provided @ 10% p.a.
2. Interest on drawings is to be charged @ 12% p.a.
3. Salary payable to C ˆ 2,000 per month.
4. C had guaranteed that the firm would earn a profits of ˆ 1,20,000 before charging or allowing interest and salary payable to partners.

Capital of A,B, and C at the beginning of the year were ˆ 1,00,000, ˆ 80,000 and ˆ 60,000 respectively. Drawings of the partners during the year ended on 31st March, 2012 were A: ˆ 20,000, B: ˆ 15,000 and c: ˆ 10,000.

The actual profits before interest and salary amounted to ˆ 1,10,000.

Prepare Profit and Loss Appropriation Account for the year ending on 31st March, 2012. .
Profit and Loss Appropriation Account

For the year ending on 31ST March, 2012

Dr. Cr.

Particulars	ˆ	Particulars	ˆ
To Interest on Capital:		By Profit and Loss A/c	
(@ 10% p.a.)		(Net Profits)	1,10,000
A 10,000		By C's Capital A/c	10,000
B 8,000		By Interest on Drawings:	
C 6,000	24.000	(@12% p.a. for 6 months	
-------		as the date of drawings is	
To Salary to C		not given)	
(ˆ 2,000 X 12)	24,000	A 1,200	
To Profits transferred to		B 900	
Capital A/cs of:		C 600	
A 37,350		______	2,700
B 24,900			
C 12,450			
______	74,700		
	1,22,700		1,22,700
	-------------		------------

- ❖ **Note: Firm's profit is ˆ 1,10,000 (i.e., ˆ 10,000 less than the amount guaranteed by C) .**
- ❖ **As such ˆ 10,000 will be debited to C's Capital A/c and credited to Profit and Loss Appropriation A/c.**

(Actual amount of profit is more than the guaranteed amount)

1. A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1 with a guarantee of minimum profits to C for ˆ 15,000. Total profits of the firm for the year ended on December 31, 2012 amounted ˆ1,20,000. Any excess payable to C on account of such guarantee shall be borne by B.

Prepare a profit and loss appropriation account to show the distribution of profits as per terms of partnership deed. Profit and Loss Appropriation Account

For the year ending on 31ST March, 2012

Dr. Cr.

Particulars	ˆ	Particulars	ˆ
To A's Capital A/c (3/6 of ˆ 1,20,000)	60.000	By Profit and Loss A/c (Net Profits)	1,20,000
To B's Capital A/c (2/6 of ˆ 1,20,000)	40,000		
To C's Capital A/c (1/6 of ˆ 1,20,000 or ˆ15,000 whichever is higher)	20,000		
	1,20,000		1,20,000
	-------------		------------

- **<u>Working note</u>**

<u>Share of Actual profits=20,000</u>

<u>Guaranteed amount=15,000</u>

Values Involved in above questions-

- **Financial Security,**
- **Mutual Understanding,**
- **Team Spirit.**
- **Transparency**

<u>Questions regarding Past Adjustment</u>

Q.7 Asha, Bela and Cheena were sharing profits equally. Their capitals were ` 40,000; ` 20,000 and ` 30,000 respectively. After closing the accounts for the year 2004, it was found that the interest on capital @ 10% p.a. was not allowed before distributing the profits. It was decided to pass a single adjusting entry to rectify the accounts of the year 2004. Journalise. (CBSE 2005)

Solution 7:

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
2005 Jan.1	Bela's capital A/c Dr. To Asha's capital A/c (adjustment of interest on capital for the year 2004)		1,000	1,000

Working Note:

	Asha	Bela	Cheena	Total
Interest on capital Cr.	4,000	2,000	3,000	9,000
Profit to be recovered Dr.	3,000	3,000	3,000	9,000
Adjustment	1,000	1,000	---	---
	Cr.	Dr.	---	---

Q.8 A, B, C and D are partners sharing profits & Losses in the ratio of 4:3:3:2. Their respective fixed capitals on March 31,2010 were ` 60,000, ` 90,000, ` 1,20,000 and ` 90,000. After preparing the final accounts for the year ended March 31,2010, it was discovered that interest on capital @ 12% p.a. was not allowed and interest on drawings amounting to ` 2,000, ` 2,500, ` 1,500 and ` 1,000 respectively was also not charged.

Pass the necessary adjustment Journal entry showing your workings clearly.

(CBSE 2011)

Solution 8:

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
2010	A's current A/c Dr.		6,867	
Apr.1	B's current A/c Dr.		750	
	To C's current A/c			3,850
	To D's current A/c			3,767
	(Adjustment of interest on capital and interest on drawings for the year 2009-10)			

Working Note:

	A	B	C	D	Total
Interest on capital Cr.	7,200	10,800	14,400	10,800	43,200
Interest on drawings Dr.	2,000	2,500	1,500	1,000	7,000
Profit to be recovered Dr.	12,067	9,050	9,050	6,033	36,200
Total Dr.	14,067	11,550	10,550	7,033	
Adjustment	6,867	750	3,850	3,767	
	Dr.	Dr.	Cr.	Cr.	

Q.9 Ram, Shyam and Mohan are partners in a firm sharing profits and losses in the ratio of 2:1:2. Their fixed capitals were ` 3,00,000, ` 1,00,000 and ` 2,00,000 respectively. Interest on capital for the year 1996 was credited to them @ 9% p.a. instead of 10% p.a.. Showing your working notes clearly, pass necessary adjusting Journal entry.

Solution 9:

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
1997 Jan.1	Shyam's current A/c Dr. Mohan's current A/c Dr. To Ram's current A/c (adjustment of interest on capital for the year 1996)		200 400	 600

Working Note:

	Ram	Shyam	Mohan	Total
1% Interest on capital Cr.	3,000	1,000	2,000	6,000
Profit to be recovered Dr.	2,400	1,200	2,400	6,000
Adjustment	600 Cr.	200 Dr.	400	

Q.10 Mohan, Vijay and Anil are equal partners, the balances in their capital accounts being ` 30,000, ` 25,000 and ` 20,000 respectively. In arriving at these figures, the profits for the year ended December 31,1992 are ` 24,000 had already been credited to partners in the proportion in which they shared profits. Their drawings were:

Mohan ` 5,000, Vijay ` 4,000 and Anil ` 3,000 in 1992.

Subsequently, the following omissions were noticed and it was decided to bring them into account.

(i) Interest on capital @ 10% p.a.
(ii) Interest on Drawings: Mohan ` 250, Vijay ` 200and Anil ` 150.

Make the necessary rectifications through a Journal entry and show your workings clearly. (CBSE 1994)

Solution 10:

Calculation of Opening Capital

	Mohan	Vijay	Anil
Closing capital	30,000	25,000	20,000
Add: Drawings	5,000	4,000	3,000
	35,000	29,000	23,000
Less: Profit already distributed	8,000	8,000	8,000
Opening capital	27,000	21,000	15,000
Interest on capital @ 10% p.a.	2,700	2,100	1,500

Table Showing Adjustment

		Mohan	Vijay	Anil	Total
Interest on capital	Cr.	2,700	2,100	1,500	6,300
Interest on drawings	Dr.	250	200	150	600
Profit to be recovered	Dr.	1,900	1,900	1,900	5,700

Total Dr. Adjustment	2,150 550 Cr.	2,100 ---	2,050 550 Dr.	6,300

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
1993 Jan.1	Anil's capital A/c Dr. To Mohan's capital A/c (adjustment of interest on capital and interest on drawings for the year 1992)		550	 550

Q.11 X, Y and Z are partners in a firm who share profits in the ratio of 2:3:5. The firm earned a profit of ` 1,50,000 for the year ended December 31,2004. The profit by mistake was distributed among X, Y and Z in the ratio of 3:2:1 respectively. This error was noted only in the beginning of the next year.

Pass necessary Journal entry to rectify the error. (CBSE 2005)

Solution 11:

Table Showing Adjustment

	X	Y	Z	Total
Profit already distributed Cr.	75,000	50,000	25,000	1,50,000
Profit to be distributed Dr.	30,000	45,000	75,000	1,50,000
Adjustment	45,000 Dr.	5,000 Dr.	50,000 Cr.	

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
2005 Jan.1	X's capital A/c Dr. Y's capital A/c Dr. To Z's capital A/c (adjustment of profit sharing ratio for the year 2004)		45,000 5,000	 50,000

Values Involved in questions of past adjustments:

- **Admitting errors committed**
- **Rectifying those errors**
- **Communicating the correct information**

Reconstitution of Partnership: Change in Profit Sharing Ratio

Q.12 P, Q and R are partners sharing profits equally. They decided that in future R will get 1/5 share in profits and remaining profit will be shared by P and Q equally. On the day of change, firm's goodwill is valued at ` 60,000. Give Journal entries arising on account of change in profit- sharing ratio. Also identify the value involves in adjustment of goodwill.

Solution 12:

Value involves: Reward for sacrifice
Change in share of:
P = 1/3-2/5 = 5-6/15 = - 1/15 (Gain)
Q = 1/3-2/5 = 5-6/15 = - 1/15 (Gain)
R = 1/3-1/5 = 5-3/15 = 2/15 (Sacrifice)

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
	P's capital A/c Dr.		2,000	
	Q's capital A/c Dr.		2,000	
	To R's capital A/c			4,000
	(adjustment of goodwill for change in profit sharing ratio)			

Reconstitution of Partnership: Death of a Partner

Q.13 G, H and I were partners in a firm sharing profits in the ratio of 4:3:3. On March 31, 2006, their Balance Sheet was as follows:

Balance Sheet

As at March 31, 2006

Liabilities		`	Assets	`
Creditors		87,000	Buildings	1,70,000
Reserve		33,000	Machinery	1,20,000
Capitals			Stock	40,000
G	1,05,000		Debtors	45,000
H	85,000		Cash	15,000
I	80,000	2,70,000		
		3,90,000		3,90,000

H died on June 30,2006. Under the partnership agreement, the executors of a deceased partner were entitled to:

(i) Amount standing to the credit of deceased [partner's capital account at the time of death.
(ii) Interest on capital @ 12% per annum,
(iii) His share of goodwill. The goodwill of the firm on H's death was valued at ` 2,70,000.
(iv) His share in the profit till the date of the death on the basis of last year's profit. The profit of the firm for the year ended on March 31, 2006 was ` 2,40,000.

Identify the value involves in the calculation of share of profit of deceased partner.

Prepare H's capital account to be rendered to his executors.

Solution

.   H's Capital Account

Particulars	`	Particulars	`
To H's Executor A/c	1,96,450	By balance b/d	85,000
		By interest on capital	2,550
		By G's capital A/c	46,286
		By I's capital A/c	34,714
		By P&L suspense A/c	18,000
		By reserve	9,900
	1,96,450		1,96,450

Value involved in questions of Reconstitution of Partnership

Adapting to changes
Integrity
Justification
Transparency

COMPANY ACCOUNTS

IMPLEMENTATION OF SCHEDULE VI OF COMPANIES ACT

General Instructions-

- Revised Schedule VI applicable on all the companies with effect from 1st April, 2011
- In case of any controversy, Accounting Standards will prevail over the Schedule;
- Only Vertical format of Balance Sheet is prescribed;
- Prescribes minimum disclosure requirements in the Balance Sheet. All other disclosures as required by the Companies Act, 1956 shall be made in the notes to accounts in addition to the requirements set out in this Schedule.
- Shareholding of more than 5% shares in the company now needs to be disclosed;
- Share allotments for non-cash consideration, buy back to be disclosed;
- Where the normal operating cycle cannot be identified, it is assumed to have duration of twelve months. New name for P & L Account is "Statement of Profit and Loss";
- Format for Statement of Profit and Loss has been prescribed
- Segregation of Revenue components into revenue from:

  -sale of products,

  -sale of services, and

  -other operating revenues

Equity and Liabilities

- Liabilities side of Balance Sheet is known as 'Equity and Liabilities' and shown as Part A of Balance Sheet (Vertical Form)
- Current/ Non-Current Distinction-- If entity does not have unconditional right to defer settlement of liability for at least 12 months after reporting period, it will be treated as CURRENT
- All expenses or provisions or advances or loans etc. which are accrued and payable within 12 months are current liabilities.
- **Provisions** to be shown under Long – term provisions and Short-term provisions.
- **Loss from Statement of Profit and Loss** is to be deducted from existing credit balance in Statement of Profit and Loss under 'Reserves and Surplus'.

- If the net amount after transfer, results is negative amount, it is shown as negative amount under the head Statement of Profit and Loss.

- Statement of Profit and Loss (Dr. Balance) will be disclosed under the head "Reserves and Surplus".

- Share application money pending allotment is not a part of Shareholders' Funds;

Assets

- All items of assets and liabilities are to be bifurcated between current and non-current portions and presented separately on the face of the Balance Sheet.

- Fixed assets were shown under one broad category i.e. fixed assets. Fixed assets are classified into:
  - ✓ Tangible Assets;
  - ✓ Intangible Assets;
  - ✓ Capital Work – in – progress;
  - ✓ Intangible Assets under Development.

- **Provision for Doubtful Debts** is not deducted from Trade Receivables but is shown as short-term Provisions under Current Liabilities.

- **Loose Tools** is to be classified as 'Inventory' under Current Assets.

- "Sundry Debtors" has been replaced with the term "Trade Receivables";

- Disclosure of trade receivables outstanding for a period exceeding six months from the date of bill/invoice is due for payment;

- Separate head for Intangible Assets and Intangible Assets under Development;

- Capital Advances have to be shown separately under "Loans and Advances" instead of Fixed Assets;

FORMAT OF REVISED SCHEDULE VI

The Ministry of Corporates Affairs specified the format of Schedule VI vide Notification No. S.O. 447(E), dated 28th February 2011 as follows:

Part I: Form of Balance Sheet

Name of the Company

Balance Sheet as at 31 March, 20X2				
Particulars		Note No.	**As at 31 March, 20X2**	**As at 31 March, 20X1**
			`	`
A	**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			
B	**ASSETS**			
1	**Non-current assets**			
	(a) Fixed assets			
	(i) Tangible assets			
	(ii) Intangible assets			
	(iii) Capital work-in-progress			
	(iv) Intangible assets under development			
	(v) Fixed assets held for sale			
	(b) Non-current 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 equivalents			
	(e) Short-term loans and advances			
	(f) Other current assets			
	TOTAL			

General Instructions for Preparation of Balance Sheet

<u>CURRENT ASSETS</u>

1. An asset shall be classified as current when it satisfies **<u>any of the following criteria</u>**: (a) it is expected to be realised in, or is intended for sale or consumption in, the company's normal operating cycle;
(b) it is held primarily for the purpose of being traded;
(c) it is expected to be realised within twelve months after the reporting date; or
(d) it is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.
All other assets shall be classified as non-current.

<u>OPERATING CYCLE</u>

2. An operating cycle is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents. Where the **normal operating cycle cannot be identified, it is assumed to have duration of 12 months.**

<u>CURRENT LIABILTY</u>

3. A liability shall be classified as current when it satisfies **any of the following criteria**: (a) it is expected to be settled in the company's normal operating cycle;
(b) it is held primarily for the purpose of being traded;
(c) it is due to be settled within twelve months after the reporting date; or
(d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.
All other liabilities shall be classified as non-current.
4. A receivable shall be classified as a **'trade receivable'** if it is in respect of the amount due on account of goods sold or services rendered in the normal course of business.
5. A payable shall be classified as a **'trade payable'** if it is in respect of the amount due on account of goods purchased or services received in the normal course of business.

6. A company shall disclose the following in notes to accounts:

6A. Share capital

Clauses (a) to (l) of Notes 6 A deal with disclosures for Share Capital and such disclosures are required for each class of share capital (different classes of preference shares to be treated separately).

a. The number and amount of shares authorized

b. The number of shares issued, subscribed and fully paid, and subscribed but not fully paid

c. Par value per share

d. A reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period

e. The rights, preferences and restrictions attaching to each class of shares including restrictions on the distribution of dividends and the repayment of capital

f. Shares in respect of each class in the company held by its holding capacity or its ultimate holding company including shares held by or by subsidiaries or associates of the holding company or the ultimate holding company in aggregate

g. Shares in the company held by each
h. Shareholder holding more than 5 per cent shares specifying the number of shares held
i. Shares reserved for issue under options and contracts/commitments for the sale of shares/disinvestment, including the terms and amounts
j. For the period of five years immediately preceding the date as at which the balance sheet is prepared : i. aggregate number and class of shares allotted as fully paid up pursuant to contract(s) without payment being received in cash.
ii. Aggregate number and class of shares allotted as fully paid up by way of bonus shares.
iii. Aggregate number and class of shares bought back.

k. Terms of any securities convertible into equity/preference shares issued along with the earliest date of conversion in descending order starting from the farthest such date
l. Calls unpaid (showing aggregate value of calls unpaid by directors and officers)

6B. Reserves and Surplus
(i) Reserve and surplus shall classified as follows
a) Capital Reserves
b) Capital Redemption Reserve
c) Securities Premium Reserve
d) Debenture Redemption Reserve
e) Revaluation Reserve
f) Share Options Outstanding Account
g) Other Reserves (specify the nature and purpose of reserve and the amount in respect thereof)
h) Surplus i.e. balance in Statement of Profit & Loss disclosing allocations and appropriations such as dividend, bonus shares and transfer to/from reserves, etc.
(Additions and deductions since the last Balance Sheet to be shown under each of the specified head)
(ii) A reserve specifically represented by earmarked investments shall be termed as a 'fund'.

(i) Debit balance of statement of profit and loss shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserves and Surplus', after adjusting negative balance of surplus, if any, shall be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative.

6C. Non-Current Liabilities
a. Long-term borrowings: • Long-term borrowings shall be classified as: (a) Bonds/debentures;
(b) Term loans;
• from banks;
• from other parties;
(c) Deferred payment liabilities;
(d) Deposits;
(e) Loans and advances from related parties;
(f) Long term maturities of finance lease obligations;
(g) Other loans and advances (specify nature).
• Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.

• Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed. The word “others” used in the phrase “directors or others” would mean any person or entity other than a director.

• Bonds/debentures (along with the rate of interest and particulars of redemption or conversion, as the case may be) shall be stated in descending order of maturity or conversion, starting from farthest redemption or conversion date, as the case may be. Where bonds/debentures are redeemable by installments, the date of maturity for this purpose must be reckoned as the date on which the first installment becomes due.

Particulars of any redeemed bonds/ debentures which the company has power to reissue shall be disclosed.

• Period and amount of continuing default as on the Balance Sheet date in repayment of loans and interest shall be specified separately in each case.

b. <u>Other Long-term liabilities</u>
This should be classified into:
a) Trade payables; and
b) Others.
c. Long-Term Provisions
This should be classified into
a) provision for employee benefits and
b) others specifying the nature.

6D<u>. Current Liabilities</u>
a. <u>Short-term borrowings;</u> (i) (a) Loans repayable on demand
• from banks;
• from other parties.
(b) Loans and advances from related parties;
(c) Deposits;
(d) Other loans and advances (specify nature).
(ii) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.
(iii) Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed.
(iv) Period and amount of default as on the Balance Sheet date in repayment of loans and interest, shall be specified separately in each case.
b. <u>Other current liabilities</u>

The amounts shall be classified as:
(a) Current maturities of long-term debt;

(b) Current maturities of finance lease obligations;
(c) Interest accrued but not due on borrowings;
(d) Interest accrued and due on borrowings;
(e) Income received in advance;
(f) Unpaid dividends;

(g) Application money received for allotment of securities and due for refund and interest accrued thereon;
(h) Unpaid matured deposits and interest accrued thereon;
(i) Unpaid matured debentures and interest accrued thereon;

c. Short-term provisions

The amounts shall be classified as:
(a) Provision for employee benefits;
(b) Others (specify nature).

6E. Non-Current Asset

a. Tangible assets

(i) Classification shall be given as:
(a) Land.
(b) Buildings.
(c) Plant and Equipment.
(d) Furniture and Fixtures.
(e) Vehicles.
(f) Office equipment.
(g) Others (specify nature).
(ii) Assets under lease shall be separately specified under each class of asset.

b. Intangible assets

(i) Classification shall be given as:
(a) Goodwill.
(b) Brands /trademarks.
(c) Computer software.
(d) Mastheads and publishing titles.
(E) Copyrights, and patents and other intellectual property rights, services and operating rights. (F) Recipes, formulae, models, designs and prototypes.

(h) Licenses and franchise.

(c. Non-current investments

- Non-current investments shall be classified as trade investments and other investments and further classified as:
  - Investment property;
  - Investments in Equity Instruments;
  - Investments in preference shares
  - Investments in Government or trust securities;
  - Investments in debentures or bonds;
  - Investments in Mutual Funds;
  - Investments in partnership firms

(h) Other non-current investments (specify nature)

d. Long-term loans and advances

(i) Long-term loans and advances shall be classified as:

(a)Capital Advances;

(b)Security Deposits;

(c)Loans and advances to related parties (giving details thereof);

(d)Other loans and advances (specify nature).
(ii) The above shall also be separately sub-classified as:
(a)Secured, considered good;
(b)Unsecured, considered good;
(c)Doubtful.
(iii) Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.
(iv) Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other persons or amounts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

e. <u>Other non-current assets</u>

Other non-current assets shall be classified as:
(i) Long Term Trade Receivables (including trade receivables on deferred credit terms);
(ii) Others (specify nature)
(iii) Long term Trade Receivables, shall be sub-classified as:
(i) (a) Secured, considered good;
(b)Unsecured considered good;
(c)Doubtful
(ii) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.
(iii) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

6F. Current Investment

a<u>. Current Investments</u>

(i) Current investments shall be classified as:
(a) Investments in Equity Instruments;
(b) Investment in Preference Shares
(c) Investments in government or trust securities;
(d) Investments in debentures or bonds;
(e) Investments in Mutual Funds;
(f) Investments in partnership firms
(g) Other investments (specify nature).

b<u>. Inventories</u>

(i) Inventories shall be classified as:
(a)Raw materials;
(b)Work-in-progress;
(c)Finished goods;

(d)Stock-in-trade (in respect of goods acquired for trading);
(e)Stores and spares;
(f)Loose tools;
(g)Others (specify nature).
(ii) Goods-in-transit shall be disclosed under the relevant sub-head of inventories. Mode of valuation shall be stated.

c. <u>Trade Receivables</u>

(i) Aggregate amount of Trade Receivables outstanding for a period exceeding six months from the date they are due for payment should be separately stated.
(ii) Trade receivables shall be sub-classified as:
(a) Secured, considered good;
(b) Unsecured considered good;
(c) Doubtful.
(iii) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.

(ii) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

d<u>. Cash and cash equivalents</u>

(i) Cash and cash equivalents shall be classified as:
(a) Balances with banks;
(b) Cheques, drafts on hand;
(c) Cash on hand;
(d) Others (specify nature).
(ii) Earmarked balances with banks (for example, for unpaid dividend) shall be separately stated.

(iii) Balances with banks to the extent held as margin money or security against the borrowings, guarantees, other commitments shall be disclosed separately.
(iv) Repatriation restrictions, if any, in respect of cash and bank balances shall be separately stated.
(v) **Bank deposits with more than 12 months maturity shall be disclosed separately**.

e<u>. Short-term loans and advances</u>

(i) Short-term loans and advances shall be classified as:
(a) Loans and advances to related parties (giving details thereof);
(b) Others (specify nature).
(ii) The above shall also be sub-classified as:
(a) Secured, considered good;
(b) Unsecured, considered good;
(c) Doubtful.
(iii) Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.
(iv) Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other person or amounts due by firms or private

companies respectively in which any director is a partner or a director or a member shall be separately stated.

f. <u>Other current assets</u> (specify nature).

This is an all-inclusive heading, which incorporates current assets that do not fit into any other asset categories.

6G. <u>Contingent liabilities and commitments</u> (to the extent not provided for)
(i) Contingent liabilities shall be classified as:
(a)Claims against the company not acknowledged as debt;
(b)Guarantees;
(c)Other money for which the company is contingently liable
(ii) Commitments shall be classified as:
(a) Estimated amount of contracts remaining to be executed on capital account and not provided for;
(b) Uncalled liability on shares and other investments partly paid
(c) Other commitments (specify nature).

Question Where will you show the following items in the Balance Sheet of a Company ?

1. Share Capital
2. Goodwill
3. Cash in hand
4. Debentures
5. Sundry debtors

SOLUTION:

Sr. No.	Items	Major Headings	Headings	Sub Headings
1	Share Capital	Equity and Liabilities	Shareholders' Funds	-----------------------
2	Goodwill	Assets	Non-Current Assets	Intangible Assets
3	Cash in hand	Assets	Current Assets	Cash and cash Equivalents
4	Debentures	Equity and Liabilities	Non-Current Liabilities	Long-term Borrowings
5	Sundry debtors	Assets	Current Assets	Trade Receivables

Question
Where will you show the following items in the Balance Sheet of a Company ?

1. General Reserve
2. Patents
3. Cash at Bank
4. Bank Loan (Payable after 7 years)
   Bills Receivables

SOLUTION:

Sr. No.	Items	Major Headings	Headings	Sub Headings
1	General Reserve	Equity and Liabilities	Shareholders' Funds	Reserve and Surplus
2	Patents	Assets	Non-Current Assets	Intangible Assets
3	Cash at Bank	Assets	Current Assets	Cash and cash Equivalents
4	Bank Loan	Equity and Liabilities	Non-Current Liabilities	Long-term Borrowings
5	Bills Receivables	Assets	Current Assets	Trade Receivables

Question

Prepare a Balance Sheet of SRK Ltd. as on 31st March, 2012 from the following details:

	(ˆin '000)
Reserve and Surplus	400
Share Capital	800
8% Debentures	300
Creditors	100
Bills Payables	80
Proposed Dividend	20
Fixed Assets (tangible)	1,000
Goodwill	150
Inventories	100
Sundry Debtors	250
Cash in Hand	60
Cash at Bank	140

SRK Ltd.

Balance Sheet as at 31st March, 2012

Particulars	**Note No.**	**Figures as at the end of current reporting**	**Figures as at the end of the previous reporting**
1	2	3	4

I. EQUITY AND LIABILITIES			
(1) Shareholders' funds			
(a) Share capital		800	
(b) Reserves and surplus		400	
(c) Money received against share warrants		--------	
(2) Share application money Pending allotment			
(3) Non-current liabilities			
(a)Long-term borrowings		300	
(b) Deferred tax liabilities (Net) (c) Other Long term liabilities (d) Long-term provisions			
(4) Current liabilities			
(a) Short-term borrowings		180	
(b) Trade payables			
(c) Other current liabilities		20	
(d) Short-term provisions			
TOTAL		**1,700**	

II. ASSETS			
(1) Non-current assets			
(a) Fixed assets			
(i) Tangible assets		1,000	
(ii) Intangible assets		150	
(iii) Capital work-in-progress			
(iv) Intangible assets under development			
(b) Non-current investments			
(c) Deferred tax assets(net)			
(d) Long term loans and advances			
(e) Other non-current assets			
(2) Current Assets			
(a) Current investments		100	
(b) Inventories		250	
(c) Trade receivables		200	
(d) Cash and cash equivalents			
(e) Short term loans and advances			
(f) Other current assets			
		1,700	
Total			

Prepare a Balance Sheet of XYZ Ltd. as on 31st March, 2012 from the following details:

	(ˆin ‘000)
General Reserve	200
Profit and Loss Account	200
Equity Share Capital	600
Preference Share Capital	200

8% Bank Loan	200
Creditors	200
Bills Payables	60
Proposed Dividend	40
Fixed Assets (tangible)	800
Patents	130
Trade Marks	70
Inventories	300
Bills Receivables	200
Cash in Hand	110
Cash at Bank	60
Short term marketable securities	30

XYZ Ltd.
Balance Sheet as at 31st March, 2012

Particulars	**Note No.**	**Figures as at the end of current reporting**	**Figures as at the end of the previous reporting**
1	2	3	4

I. EQUITY AND LIABILITIES			
(1) Shareholders' funds			
(a) Share capital		800	
(b) Reserves and surplus		400	
(c) Money received against share warrants		--------	
(2) Share application money Pending allotment			
(3) Non-current liabilities			
(a)Long-term borrowings		200	
(b) Deferred tax liabilities (Net) (c) Other Long term liabilities (d) Long-term provisions			
(4) Current liabilities			
(a) Short-term borrowings		260	
(b) Trade payables			
(c) Other current liabilities		40	
(d) Short-term provisions			
TOTAL		**1,700**	

II. ASSETS			
(1) Non-current assets			
(a) Fixed assets			
(i) Tangible assets		800	
(ii) Intangible assets		200	
(iii) Capital work-in-progress			
(iv)Intangible assets under development			
(b) Non-current investments			
(c) Deferred tax assets(net)			
(d) Long term loans and advances			
(e) Other non-current assets			
(2) Current Assets			
(a) Current investments		300	
(b) Inventories		200	
(c) Trade receivables		200	
(d) Cash and cash equivalents			
(e) Short term loans and advances			
(f) Other current assets			
Total		**1,700**	

Values involved in presentation of Balance Sheet---

- Orderliness
- Communication of material information
- Complying with legal provisions

Accounting for issue of share capital

PRESENTATION OF SHARE CAPITAL

Question S T L Global Ltd. was formed with a nominal Share Capital of ` 40,00,000 divided into 4,00,000 shares of ` 10 each. The Company offers 1,30,000 shares to the public payable ` 3 per share on Application, ` 3 per share on Allotment and the balance on First and Final Call. Applications were received for 1,20,000 shares. All money payable on allotment was duly received, except on 200 shares held by Y. First and Final Call was not made by the Company.

How would you show the relevant items in the Balance Sheet of S T L Global Ltd.?

SOLUTION:

BALANCE SHEET OF S T L Global LTD.

as at..................

Equity and Liabilities	***Note No.***	`	`
Shareholder's Funds:			
(a) Share Capital	(1)		**14,34,000**
Assets	***Note No.***	`	`
Current Assets:			
Cash and Cash Equivalents (cash at Bank)			**14,34,000**

Notes to Accounts:

(1)Share Capital		`	`
Authorised Capital:			
4,00,000 shares of ` 10 each			**40,00,000**
Issued Capital:			
1,30,000 shares of `10 each			13,00,000
Subscribed but not Fully Paid Capital:			
1,20,000 shares of ` 10 each			
` 6 per share called-up	14,40,000		
Less: Calls in Arrears (200 shares × ` 3)		6,000	
		14,34,000	

Question--

.Shree Ganesh Jewelry House Ltd. Issued 40,000 shares of ` 10 each at a discount of 10%. Payments were to be made as—on Application ` 3; on Allotment ` 4 and on First and Final Call ` 2.

Applications were received for 36,000 shares and all were accepted. All money was duly received.

Pass necessary entries in the Books of Company and also show the Balance Sheet of the Company.

SOLUTION: Journal

		`	`
Bank A/c	Dr.	1,08,000	
To Share Application A/c			1,08,000
(Money received on application for 36,000 shares @ ` 3 per shares)			
Share Application A/c	Dr.	1,08,000	
To Share Capital A/c			1,08,000
(Transfer of application money to share capital A/c)			
Share Allotment A/c	Dr.	1,44,000	
Discount on issue of shares A/C	Dr.	36,000	
To Share Capital A/c			1,80,000
(Amount due on allotment, excluding discount)			
Bank A/c	Dr.	1,44,000	
To Share Allotment A/c			1,44,000
(Allotment money received)			
Share first and Final call A/c	Dr.	72,000	
To Share Capital A/c			72,000
(Share first and final call due)			
Bank A/c	Dr.	72,000	
To Share First and Final call A/c			72,000
(Share first and final call money received)			

BALANCE SHEET OF Shree Ganesh Jewelry House LTD.

As on…………

Equity and Liabilities	**Note No.**	`	`
Shareholder's Funds:			
1. Share Capital	**1**	**3,60,000**	

Other Current/Non-Current Assets:		
Unamortized Expenses (Share Discount)	36,000	
Current Assets:		
Cash and Cash Equivalents (Cash at Bank)	3,24,000	**3,60,000**

Notes to Accounts:

		`	`
2.	**Share Capital**		
	Authorised Capital	--------	
	Issue Capital:		
	40,000 Shares of ` 10 each		**4,00,000**
	Subscribed and fully paid:		
	36,000 Shares of ` 10 each fully paid up		**3,60,000**

Question

Cinevistaas Ltd. Issued 30,000 Preference shares of ` 100 each at a discount of 5%. Payments were to be made as — ` 25 on Application; ` 35 on Allotment and ` 35 on First and Final Call.

The applications for 28,000 shares were received and all were accepted. All the money was duly received except the first and final call on 400 shares.

Give the necessary Journal Entries and prepare Cash Book of the Company. Also give the Opening Balance Sheet of the Company.

CASH BOOK (Bank Column)

	`		`
To Preference Share		By Balance	26,46,000
Application A/c	7,00,000		
To Preference Share			
Allotment A/c	9,80,000		
To Preference Share First &			
Final Call A/c	9,66,000		
	26,46,000		26,46,000

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Preference Share Application A/c	Dr.	7,00,000	
To Preference Share Capital A/c			7,00,000
(Application money transferred to capital A/c)			
Preference Share Allotment A/c	Dr.	9,80,000	
Share Discount A/c	Dr.	1,40,000	
To Preference Share Capital A/c			11,20,000
(Allotment due and ` 5 per share debited to share discount A/c)			
Preference Share First & Final Call A/c	Dr.	9,80,000	
To Preference Share Capital A/c			9,80,000
(Amount due on first & final call A/c)			
Calls in Arrears A/c	Dr.	14,000	
To Preference Share First & Final Call A/c			14,000
(First and Final call @ `35 per share unpaid on 400 shares)			

BALANCE SHEET OF Cinevistaas LTD.
As on……………..

Equity and Liabilities	**Note No.**	`	`
Shareholder's Funds:			
3. Share Capital	**1**	**27,86,000**	

Assets	**Note No.**	`	`
Other Current/Non-Current Assets:			
Unamortized Expenses (Share Discount)		1,40,000	
Current Assets;			
Cash and Cash Equivalents (Cash at Bank)		26,46,000	

Notes to Accounts:

` `

4. Share Capital

Authorised:		
…….Shares of `……each	**……….**	
Issued:		
30,000 Preference Shares of ` 100 each		**30,00,000**
Subscribed but not fully paid:		
28,000 Preference Shares of ` 100 each	**28,00,000**	
Less: Calls in Arrear	**14,000**	**27,86,000**

Note: When Cash Book Entries are asked in the question, all cash transactions are to be recorded in Cash Book, other non-cash transactions should be entered in the journal.

Question .

Sibar Media & Entertainment Ltd. invited applications for 1,00,000 shares of `10 each at a discount of 6% payable as follows:

On Application	3
On Allotment	2.40
On First and Final Call	4

The applications were received for 90,000 shares and all of these were accepted. All money due were received except the first and final call on 2,000 shares which were forfeited. 1,000 shares were re-issued @ ` 9 per share as fully paid. Assuming that all requirements of law were complied with, pass Entries in the Journal of the company. Also show how these transactions will be reflected in the compnay's Balance Sheet.

Sibar Media & Entertainment Ltd.

Journal

		`	`
Bank A/c	Dr.	2,70,000	
To Share Application A/c			2,70,000
(Application money received on 90,000 shares @ ` 3 per share)			
Share Application A/c	Dr.	2,70,000	
To Share Capital A/c			2,70,000
(Application money transferred to Share Capital A/c)			
Share Allotment A/c	Dr.	2,16,000	
Share Discount A/c	Dr.	54,000	
To Share Capital A/c			2,70,000
(Allotment money due on 90,000 shares; ` 2.40 per share debited to Share Allotment A/c and ` 0.60 per share debited to Share Discount A/c)			

Particulars		Dr. (`)	Cr. (`)
Bank A/c	Dr.	2,16,000	
To Share Allotment A/c			2,16,000
(Allotment money received on 90,000 shares @ ` 2.40 per share)			
Share First & Final Call A/c	Dr.	3,60,000	
To Share Capital A/c			3,60,000
(First call due on 90,000 shares at ` 4 per share)			
Bank A/c	Dr.	3,52,000	
To Share First & Final Call A/c			3,52,000
(Share first and final call received on 88,000 shares @ ` 4 per share)			
Share Capital A/c	Dr.	20,000	
To Share First & Final Call A/c			8,000
To Share Discount A/c			1,200
To Share Forfeiture A/c			10,800
(Forfeiture of 2,000 shares for non-payment of first and final call)			
Bank A/c	Dr.	9,000	
Share Discount A/c	Dr.	600	
Share Forfeiture A/c	Dr.	400	
To Share Capital A/c			10,000
(Re-issue of 1,000 shares @ ` 9 per share, ` 0.60 per share debited to Discount A/c and the balance of ` 0.40 per share charged from forfeiture A/c)			
Share Forfeiture A/c	Dr.	5,000	
To Capital Reserve A/c			5,000
(Profit on 1,000 re-issued shares transferred to Capital Reserve A/c from share forfeiture A/C)			

BALANCE SHEET OF Sibar Media & Entertainment Ltd.

As on……….

Equity and Liabilities	**Note No.**	`	`

Shareholder’s Funds:			
5. Share Capital	**1**		**8,95,400**
6. Reserve and Surplus	**2**		**5000**
		9,00,400	

Assets	**Note No.**	`	`
Other Current/Non-Current Assets:			
Unamortized Expenses (Share Discount)	4	**53,400**	
Current Assets:			
Cash and Cash Equivalents (Cash at Bank)		**8,47,000**	
		9,00,400	

Notes to Accounts:

	`	`
7. Share Capital:		
Authorised:		
Issued Capital:		
1,00,000 Shares of ` 10 each		**10,00,000**
Subscribed and fully paid:		
89,000 Shares of ` 10 each fully paid up	**8,90,000**	
Add: Share Forfeiture A/c	**5,400**	**8,95,400**

	`
8. Reserves and Surplus	
Capital Reserve A/c	**5,000**

Note (3) As profit on 2,000 shares $= ` 10,800$ `

Therefore, Profit on 1,000 Shares $= \frac{10,800}{200} \times 100$ =

5,400

Less Loss on Re-issue: 1,000 Shares × ` 0.40 = 400

Transferred to Capital Reserve
5,000

(4)Share Discount: ` 0.60 per share on 89,000 Shares

Question

Daisy Systems Ltd. Issued 50,000 Equity Shares of ` 10 each, at a discount of 10%, payable as follows:

On Application	` 2.50 per share
On Allotment	` 3 per share
On First Call	` 1.50 per share
On Final Call	The balance amount

Applications were received for 65,000 shares and the Directors made pro-rata allotment to the applicants for 60,000 shares.

The Directors did not make the final Call. X did not pay allotment and first call money on 1,000 shares allotted to him while Y did not pay the First Call on his 2,000 Shares. These shares were forfeited and 2,200 of these shares were re-issued to Mr. Gupta as ` 8 paid at ` 6.50 per share, whole of Y's shares being included in the re-issued shares. Show the journal entries to record the above transactions and prepare the Balance Sheet.

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		`	`
Bank A/c	Dr.	1,62,500	
To Equity Share Application A/c			1,62,500
(Application money received on 65,000 shares @ ` 5 per share)			
Equity Share Application A/c	Dr.	1,62,500	
To Equity Share Capital A/c			1,25,000
To Equity Share Allotment A/c			25,000
To Bank A/c			12,500
(Application money transferred to Share Capital A/c for 50,000 shares; to allotment A/c for 5,000 shares and amount returned on 2,500 shares @ ` 2.50 per share)			
Equity Share Allotment A/c	Dr.	1,50,000	
Share Discount A/c	Dr.	50,000	
To Equity Share Capital A/c			2,00,000
(Allotment due on 50,000 shares @ ` 3 per share)			
Bank A/c	Dr.	1,22,500	
To Equity Share Allotment A/c			1,22,500
(Allotment money received on 49,000 shares)			
Equity Share First Call A/c	Dr.	75,000	

To Equity Share Capital A/c			75,000
(First call due on 50,000 shares @ ` 1.50 per share)			
Bank A/c	Dr.	70,500	
To Equity Share First Call A/c			70,500
(First call received on 47,000 shares @ ` 1.5 per share)			
Equity Share Capital A/c (3,000 × ` 8)	Dr.	24,000	
To Equity Share Allotment A/c			2,500
To Equity Share First Call A/c			4,500
To Share Discount A/c			3,000
To Share Forfeiture A/c			14,000
(Forfeiture of 1,000 shares of X and 1,000 shares of Y)			
Bank A/c	Dr.	14,300	
Share Discount A/c	Dr.	2,200	
Share Forfeiture A/c	Dr.	1,100	
To Equity Share Capital A/c			17, 600
(Re-issue of 2,200 shares @ ` 6.50 per share)			
Share Forfeiture A/c	Dr.	10,500	
To Capital Reserve A/c			10,500
(Profit on the re-issue of 2,200 shares transferred to Capita Reserve A/c)			

BALANCE SHEET OF Daisy Systems LTD.

As on………..

Equity and Liabilities	**Note No.**	`	`
Shareholder's Funds:			
Share Capital	**1**	**3,96,000**	
Reserve and Surplus (Capital Reserve)		**10,500**	
		4,06,500	

Assets	**Note No.**	`	`
Other Current/Non-Current Assets:			
Unamortized Expenses (Share Discount)		49,200	
Current Assets:			
Cash and Cash Equivalents (Cash at Bank)		3,57,300	
		4,06,500	

Issue of Debentures

Q. Claris Life Sciences Ltd. issued 5,000 14% Debentures of ` 100 each at a discount of 10%. Pass the necessary journal entries in the books of the company for the issue of debentures when debentures were to be:

(i) Redeemed at par.

(ii) Redeemed at a premium of 5%.

Date	Particulars	L. F.	Dr.(`)	Cr.(`)
	Bank A/c Dr. To Debenture Application and Allotment (Application money received on 5,000 debentures @ ` 90 each)		4,50,000	 4,50,000
	Debenture Application and Allotment Dr. Discount on issue of debentures Dr. To 14% Debentures (5,000 14% Debentures of ` 100 each issues at a discount of 10%)		4,50,000 50,000	 5,00,000
	--			
	Debenture Application and Allotment Dr. Discount on issue of debentures Dr. To 14% Debentures To Premium on redemption of debentures (5,000 14% debentures of ` 100 each issues at a discount of 10% but redeemable at a premium of 5%)		4,50,000 75,000	 5,00,000 25,000

Q. Kirloskar Multimedia Ltd. purchased machinery costing ` 16,72,000. It was agreed that the purchase consideration be paid by issuing 13% Debentures of ` 100 each. Assume debentures are issued (i) at par, (ii) at a premium of 10% and (iii) at a discount of 5%. Give necessary journal entries.

Journal

Date	Particulars	L. F.	Dr.(`)	Cr.(`)
	Machinery A/c Dr. To Vendor (machinery purchased from vendor)		16,72,000	 16,72,000
	Vendor Dr. To 13% Debentures (15,960 13% debentures of ` 100 each issued at par.)		 16,72,000	 16,72,000
	Vendor Dr.		16,72,000	

	To 13% debentures A/c To securities premium (15,200 13% debentures of ` 100 each issued at a premium of 10%)			15,20,000 1,52,000
	Vendor Dr. Discount on issue of debentures Dr. To 13% debentures (17,600 13% debentures of ` 100 each issued at a discount of 5%)		16,72,000 88,000	 17,60,000

Q. Zenith Infotech Ltd. issued Debentures of ` 1,00,000 at par redeemable at the end of four years at a premium of 20%. Show the 'loss on Issue of Debentures Account' till it is written off completely. Books of Zenith Infotech Ltd.

Loss on Issue of Debentures Account

Date	Particulars	L.F.	`	Date	Particulars	L. F.	`
Year I	To premium on redemption on debentures A/c		20,000	Year I	By Profit & loss A/c By balance c/d		5,000 15,000
			20,000				20,000
Year II	To Balance b/d		15,000	Year II	By Profit & loss A/c By balance c/d		5,000 10,000
			15,000				15,000
Year III	To Balance b/d		10,000	Year III	By Profit & loss A/c By balance c/d		5,000 5,000
			10,000				10,000
Year IV	To Blanco b/d		5,000	Year IV	By Profit & loss A/c		5,000

Q. Archana Software Ltd. issues 6,000 15% Debentures of ` 100 each at a discount of 10%. The amount was payable as follows:

On Application 50

On Allotment 40

Applications for 8,000 debentures were received. Allotment was made to all the applicants on pro-rata basis. Identify the value involved in the decision of allotment.

Give Journal entries in the books of the company.

Journal

Date	Particulars	L. F	Dr.(`)	Cr.(`)
	Bank A/c Dr.		4,00,000	

	To Debenture Application A/c (Application money received on 8,000 debentures @ ` 50 each)			4,00,000
	Debenture Application Dr. To 15% Debentures To Debentures Allotment (Application money transferred to 15% Debentures account and Debentures Allotment A/c		4,00,000	 3,00,000 1,00,000
	Debenture Allotment Dr. Discount on Issue of Debenture Dr. To 15% Debentures (Allotment money due on 6,000 debentures at ` 40 each) ---		2,40,000 60,000	 3,00,000
	Bank A/c Dr. To Debenture Allotment (Allotment money received)		1,40,000	 1,40,000

Question A Ltd. issued 5,000 10% Debenture of ` 100 each at a discount of 20%. All the amount was payable with the application. Applications were received for 4,000 Debentures only. All due amount duly received. Give the necessary journal entries in the books of A Ltd. at the time of issue of Debentures In the Books of A Ltd.

Journal

Date	Particulars	Dr. (`)	Cr. (`)
	Bank A/c Dr. To Debenture Application and Allotment A/c (Being Debenture Appllication amount received for 4,000 debentures @ ` 80 each)	3,20,000	 3,20,000
	Debenture Application and Allotment A/c Dr. Discount on issue of Debentures A/c Dr. To 10% Debentures A/c (Being application money adjusted at the time of allotment of debentures)	3,20,000 80,000	 4,00,000

Question

Give journal entries for issue of debentures in the following cases and also prepare balance sheet in each case.

I. Issued 1,000 7% debentures of Rs. 100 each at par, redeemable at par.

Solution I. Journal

Date	*Particulars*	*L.F.*	*Dr. (Rs.)*	*Cr. (Rs.)*
	Bank A/c. Dr. To Debentures Applications A/c. (Application money received)		1,00,000	 1,00,000
	Debentures Application A/c. Dr. To 7% Debentures A/c (Issue of debentures at par, redeemable at par)		1,00,000	 1,00,000

Balance Sheet of …..

As at 31st December, 2012 (assumed)

	Particulars	*Note No.*	**(Rs.)**
I (3)	**Equity and Liabilities** **Non-Current Liabilities** (a) Long-term Borrowings	 1	 1,00,000
II (2)	**Assets** **Current Assets** (e) Cash and Cash Equivalents	 2	 1,00,000

Notes to Balance Sheet

Note No.1 **Long-term Borrowings :** 1,000 , 7% Debentures of Rs. 100 each	(Rs.) 1,00,000
Note no.2 **Cash and Cash Equivalents :** Cash at Bank	 1,00,000

II. Issued 1,000 7% debentures of Rs. 100 at a Premium of 5%, redeemable at par.

Solution II Journal

Date	Particulars	L.F.	Dr. (Rs.)	Cr. (Rs.)
	Bank A/c. Dr. To Debentures Applications A/c. (Application money on 1,000 debentures @ Rs. 105 each received)		1,05,000	 1,05,000
	Debentures Application A/c. Dr. To 7% Debentures A/c. To Securities Premium A/c (Debentures issued at premium repayable at par)		1,05,000	 1,00,000 5,000

Balance Sheet of …..

	Particulars	Note No.	(Rs.)
I	**Equity and Liabilities**		
(1)	**Shareholders' Fund**		
	(b) Reserve and surplus	1	5,000
(3)	**Non-Current Liabilities**		
	(a) Long-term borrowings	2	1,00,000
			1,05,000
II	**Assets**		
(2)	**Current Assets**		
	(d) Cash and Cash Equivalents	3	1,05,000

Notes to Balance Sheet

	(Rs.)
Note No.1	
Reserve and Surplus :	
Securities Premium Reserve	5,000
Note no.2	
Long-term Borrowings :	
1,000 , 7% Debentures of Rs. 100 each	1,00,000
Note No.3	
Cash and Cash Equivalents :	
Cash at Bank	1,05,000

III. Issued 1,000 7% debentures of Rs. 100 each at a discount of 5%, redeemable at par.

Solution III Journal

Date	*Particulars*	*L.F.*	*Dr. (Rs.)*	*Cr. (Rs.)*
	Bank A/c. Dr. To Debentures Applications A/c. (Application money on 1,000 debentures @ Rs. 95 each received)		95,000	 95,000
	Debentures Application A/c. Dr. Discount on issue of Debentures A/c. Dr. To 7% Debentures A/c. (Debentures issued at discount, repayable at par)		95,000 5,000	 1,00,000

Balance Sheet of …..

	Particulars	*Note No.*	**(Rs.)**
I (1)	**Equity and Liabilities** **Shareholders' Fund** (a) Long-term borrowings	 1	 1,00,000
II (1) (2)	**Assets** **Non-current Assets** (e) Other Non-current Assets **Current Assets** (d) Cash and Cash Equivalents	 2 3	 5,000 95,000 1,00,000

Notes to Balance Sheet	
Note No.1	(Rs.)
Long-term Borrowings :	
1,000 , 7% Debentures of Rs. 100 each	1,00,000
Note no.2	
Other Non-current Assets	
Discount on Issue of Debentures	5,000
Note No.3	
Cash and Cash Equivalents :	
Cash at Bank	95,000

IV. Issued 1,000 7% debentures of Rs. 100 each at par, redeemable at 5% Premium.

Solution IV Journal

Date	*Particulars*	*L.F.*	*Dr. (Rs.)*	*Cr. (Rs.)*
	Bank A/c. Dr.		1,00,000	
	To Debentures Applications A/c.			1,00,000
	(Application money received)			
	Debentures Application A/c. Dr.		1,00,000	
	Loss on issue of Debentures A/c. Dr.		5,000	
	To 7% Debentures A/c.			1,00,000
	To Premium on Redemption A/c.			5,000
	(Debentures issued at par, repayable at premium)			

Balance Sheet of …..

	Particulars	*Note No.*	**(Rs.)**
I	**Equity and Liabilities**		
(3)	**Non-current liabilities**		
	(a) Long-term borrowings	1	1,00,000
	(c) Other Long-term Liabilities		5,000
	Total		1,05,000
II	**Assets**		
(1)	**Non-current Assets**		
	(e) Other Non-current Assets	2	5,000
(2)	**Current Assets**		
	(d) Cash and Cash Equivalents	3	1,00,000

	Total		1,05,000

Notes to Balance Sheet

Note No.1	(Rs.)
Non-current Liabilities :	
(a) Long-term Borrowings :	
1,000 , 7% Debentures of Rs. 100 each	1,00,000
(b) Other long-term Liabilities	
Premium on Redemption	5,000
	1,05,000
Note no.2	
Other Non-current Assets :	
Loss on Issue of Debentures	5,000
Note No.3	
Cash and Cash Equivalents :	
Cash at Bank	1,00,000

V. Issued 1,000 7% debentures at a discount of 5%, redeemable at a Premium of 5%.

Solution V Journal

Date	***Particulars***	***L.F.***	***Dr. (Rs.)***	***Cr. (Rs.)***
	Bank A/c. Dr. To Debentures Applications A/c. (Application money on Rs. 95 each received)		95,000	 95,000
	Debentures Application A/c. Dr. Loss on issue of Debentures A/c. Dr. To 7% Debentures A/c. To Premium on Redemption A/c. (Debentures issued at discount of 5% repayable @ 5% premium)		95,000 10,000	 1,00,000 5,000

Balance Sheet of …..

	Particulars	*Note No.*	**(Rs.)**
I	**Equity and Liabilities**		
(3)	**Non-current liabilities**		
	(a) Long-term borrowings	1	1,00,000
	(c) Other Long-term Liabilities		5,000
	Total		1,05,000
II	**Assets**		
(1)	**Non-current Assets**		
	(e) Other Non-current Assets	2	5,000
(2)	**Current Assets**		
	(d) Cash and Cash Equivalents	3	1,00,000
	Total		1,05,000

Notes to Balance Sheet

	(Rs.)
Note No.1	
Non-current Liabilities :	
(a) Long-term Borrowings :	
1,000 , 7% Debentures of Rs. 100 each	1,00,000
(b) Other long-term Liabilities	
Premium on Redemption	5,000
	1,05,000
Note no.2	
Other Non-current Assets :	
Loss on Issue of Debentures	5,000
Note No.3	
Cash and Cash Equivalents :	
Cash at Bank	1,00,000

VI. Issued 1,000 7% debentures at a premium of 5%, redeemable at a Premium of 8%.

Solution VI Journal

Date	*Particulars*	*L.F.*	*Dr. (Rs.)*	*Cr. (Rs.)*
	Bank A/c. Dr.		1,05,000	
	To Debentures Applications A/c.			1,05,000
	(Application money on @ Rs.105 per debentures)			

	Debentures Application A/c. Dr. Loss on issue of Debentures A/c. Dr. To 7% Debentures A/c. To Securities premium A/c. To Premium on Redemption A/c. (Debentures issued at a premium of 5% repayable @ 8% premium)		1,05,000 8,000	 1,00,000 5,000 8,000

Balance Sheet of …..

	Particulars	*Note No.*	**(Rs.)**
I	**Equity and Liabilities**		
(1)	**Shareholders' Fund**		
	(b) Reserves and surplus	1	5,000
(3)	**Non-Current Liabilities**		
	(a) Long-term borrowings	2	1,00,000
	(c) Other Long-term Liabilities		8,000
	Total		1,13,000
II	**Assets**		
(1)	**Non-current Assets**		
	(e) Other Non-current Assets	3	8,000
(2)	**Current Assets**		
	(d) Cash and Cash Equivalents	4	1,05,000
	Total		1,13,000

Notes to Balance Sheet

Note No.1	(Rs.)
Reserve and Surplus :	
Securities Premium	5,000
Note no.2	
Non-current liabilities :	
(a) Long-term Borrowings :	
1,000 , 7% Debentures of Rs. 100 each	1,00,000
(b) Other Long-term liabilities	
Premium on redemption	8,000
	1,08,000
Note No.3	
Other Non-current Assets:	
Loss on Issue on Debentures	8,000
Note No.4	
Cash and Cash Equivalents :	
Cash at Bank	1,05,000

(Issue of Debentures at Discount)

. PQR Ltd. Has issued 2,000, 10% Debentures of ˆ 100 each at ˆ 92 each. Applications were received for 2,500 debentures. The Co. has decided to make pro-rata allotment to all applicants. Full amount was payable at the time of application.

Pass necessary Journal entries in the books of PQR Ltd.

JOURNAL

Date	Particulars	L.F.	Debit ˆ	Credit ˆ
	Bank A/c Dr.		2,30,000	
	To Debenture Application and Allotment A/c			2,30,000
	(Being application money received on 2,500 debentures @ ˆ 92 per debenture)			
	Debenture Application and Allotment A/c Dr.		2,30,000	
	Discount on Issue of Debentures A/c Dr.		16,000	
	To 10% Debentures A/c			2,00,000
	To Bank A/c			46,000
	(Being application money adjusted on 2,000 debentures and extra money refunded)			

(Issue of Debentures at Discount)

XYZ Ltd. has issued 3,000, 8% Debentures of ˆ 100 each at a discount of 5%. Full amount was payable at the time of application. Issue was fully subscribed by the public.

Pass necessary Journal entries in the books of XYZ Ltd.

JOURNAL

Date	Particulars	L.F.	Debit ˆ	Credit ˆ
	Bank A/c Dr		2,85,000	
	To Debenture Application and Allotment A/c			2,85,000
	(Being application money received on 3,000 debentures @ ˆ 95 per debenture)			
	Debenture Application and Allotment A/c Dr		2,85,000	
	Discount on Issue of Debentures A/c Dr.		15,000	
	To 8% Debentures A/c			3,00,000
	(Being application money adjusted at the time of allotment of debentures)			

(Issue of Debentures as Collateral Security)

MUST READ IT CAREFULLY

X Ltd. Had 12,00,000, 11% Debentures outstanding on 1st April, 2008. During the year, it took a loan of Rs. 4 Lakh from canara Bank for which company deposited debentures of Rs. 5 Lakh as collateral security.

Pass journal entries and show how these transactions will appear in Balance Sheet of the company.

(C.B.S.E., 2004-C)

Solution.

First method. **No entry is passed for debentures.**

Journal

Date	Particulars	L.F.	Dr.(Rs.)	Cr.(
2008	Bank A/c Dr. To Canara Bank's loan A/c (Loan taken from bank against collateral security of debentures worth Rs. 5 Lakhs)		4,00,000	 4,00,(

Balance Sheet of X ltd.

As at 31st March, 2012 (*assumed)*

	Particulars	Note No.	(Rs.)
I (3)	Equity and Liabilities Non-Current Liabilities (a) Long-term Borrowings	 1	 16,00,000

Notes to Balance Sheet

Note No. 1 **Long-term Borrowings :** 11% Debentures Bank Loan (Against collateral security of debentures Rs. 5,00,000	 12,00 4,00 16,00

Second method. **Entry for debentures is also passed.**

Journal

Date	Particulars	L.F.	Dr.(Rs.)	Cr.(
	Bank A/c Dr. To Canara Bank's loan A/c (Loan taken from bank)		4,00,000	 4,00,(
	Debentures Suspense A/c. Dr. To 11% Debentures A/c. (Issue of Rs. 5,00,000 debentures issued as collateral		5,00,000	 5,00,(

	security)			

Presentation of debenture and blank loan will remain same as explained in Balance Sheet under 1st method, however, presentation of information in note will differ.

Balance Sheet of X ltd.

As at 31st March, 2012 (*assumed)*

	Particulars	Note No.	(Rs.)
I (3)	Equity and Liabilities Non-Current Liabilities (a) Long-term Borrowings	1	16,00,000

IInd method

Notes to Balance Sheet

Note No. 1 **Other Long-term Borrowings :**		
11% Debentures	17,00,000	
Less : Debentures Suspense A/c.	5,00,000	12,00
Bank Loan (Against collateral security of debentures Rs. 5,00,000		4,00
		16,00

22. On 1st April, 2012 A Ltd. took a loan of ^ 5, 00,000 from the State Bank of India for which the company issued 8 % Debentures of ^ 6, 00,000 as collateral security. Record the issue of debentures in the books of the co. and also show how the debentures and bank loan will appear in the Balance Sheet of the company. **JOURNAL**

Date	Particulars	L.F.	Debit ^	Credit ^

	Bank A/c Dr. To Bank Loan A/c (Being loan taken from bank of 5,00,000)		5,00,000	5,00,000
	Debenture Suspense A/c Dr. To 8% Debentures A/c (Being the issuance of debentures as collateral security)		6,00,000	6,00,000

Balance Sheet of A Ltd.

As at 1st April, 2012

Particulars	Note No.	Figure as at the end of current accounting period	Figure as at the end of previous accounting period
I.EQUITY AND LIABILITIES			
(1) Shareholders' Funds			
(2) Share Application Money Pending Allotment			
(3) Non-Current Liabilities	1	5,00,000	____________
TOTAL		5,00,000	

Notes to Accounts:

Particulars	Figure as at the end of current accounting	Figure as at the end of previous accounting

	period	period
Note No. 1. Non Current Liabilities: Bank Loan 8% Debentures 6,00,000 **Less:** Debenture Suspense A/c (6,00,000)	5,00,000 ________	
Total	5,00,000	

s

ABC Ltd had ` 15,00,000, 10% Debentures outstanding as on 1st April, 2012. On 1st Sept.2012 Company took a loan of ` 5,00,000 from the Punjab National Bank for which the company placed with the bank , 10%Debentures for ` 7,00,000 as collateral Security. Pass journal entries, if any. Also show how the debentures and Bank Loan will appear in the company's Balance Sheet as on 31st March,2013.

Solution: JOURNAL of ABC Ltd.

Date	Particulars	Dr. (`)	Cr. (`)
2012 1st Sept.	Bank A/c Dr. To Bank Loan A/c (Loan taken from bank of `5,00,0000)	5,00,000	5,00,000
	Debentures Suspense A/c Dr. To 10% DebenturesA/c (Issue of Debentures as Collateral Security)	7,00,000	7,00,000

Balance Sheet of ABC Ltd.

Notes to Accounts:

Note I.

Particulars	As on 31.03.2012 (`)	As on 01.03.2012 (`)
Long Term Borrowings		
(i) 10%Debentures 22,00,000		
Less: Debentures Suspense A/c 7,00,000	15,00,000	15,00,000
(ii) Bank Loan	5,00,000	-----------
Total	20,00,000	15,00,000

Redemption of Debentures:

Question. AB Power Ltd., an infrastructure company has outstanding 10 lac, 9% Debentures of ` 5 each due for redemption on 30st Sept.2012. Record the necessary entries at the time of redemption of debentures. Journal of AN Power Ltd.

(` in Lac)

Date	Particulars	Dr. (`)	Cr. (`)
30th Sept	9%Debentures A/c Dr.	50	
	To Debentureholders' A/c		50
	(Being the amount due to Debentureholders on redemption)		
	Debentureholders' A/c Dr.	50	
	To Bank A/c		50
	(Being the amount due to Debentureholders paid)		

Note: As per SEBI Guideline, Infrastructure companies are exempted from creating Debenture Redemption Reserve.

Question Abha Ltd. Has 5,000 ; 10% Debentures of ` 20 each due for redemption on 30th sept. 2012. Debenture Redemption Reserve has a Balance of ` 20,000 on that date. .

Record the necessary entries at the time of redemption of debentures Journal in the Books of Abha Ltd.

Date	Particulars	Dr. (`)	Cr. (`)
	Profit And Loss Appropriation A/c Dr.	30,000	
	To Debenture Redemption Reserve A/c		30,000
	(Being the required amount transferred to DRR)		
	10%Debentures A/c Dr.	1,00,000	
	To Debentureholders' A/c		1,00,000
	(Being the amount due to Debentureholders on redemption)		
	Debentureholders' A/c Dr.	1,00,000	
	To Bank A/c		1,00,000
	(Being the amount due to Debentureholders paid)		
	Debenture Redemption Reserve A/c Dr.	50,000	
	To General Reserve A/c		50,000
	(Being the DRR transferred to General Reserve)		

Note: DRR existed in the book with ` 20,000 , As per SEBI guidline DRR is required for minimum 50% of debenentures face value e.i. ` 50,000 total DRR required . So the with the difference amount (50,000-20,000) is credited.

Question Vivek Transport Ltd. Has 5,000 ; 10% Debentures of ` 20 each due for redemption on 30th sept. 2012. Debenture Redemption Reserve has a Balance of ` 80,000 on that date. . Record the necessary entries at the time of redemption of debentures.

Solution: Journal in the Books of Vivek Transport Ltd.

Date	Particulars	Dr. (`)	Cr. (`)
	Profit And Loss Appropriation A/c Dr.	20,000	
	To Debenture Redemption Reserve A/c		20,000
	(Being the required amount transferred to DRR)		

	10%Debentures A/c Dr. To Debentureholders' A/c (Being the amount due to Debentureholders on redemption)	1,00,000	1,00,000
	Debentureholders' A/c Dr. To Bank A/c (Being the amount due to Debentureholders paid)	1,00,000	1,00,000
	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being the DRR transferred to General Reserve)	1,00,000	1,00,000

Note:1. DRR exists in the books more than 50% of the debentures face value, so it assumed that redemption is out of profit. In this case DRR is to be created upto 100% face value of Debentures. So DRR A/c is credited with the difference amount e.i. `1,00,000-`80,000=`20,000.

Question -- Rahul Ltd. redeemed ` 25,00,000 ; 12% Debentures at a premium of 5% out of Profit on 30th sept. 2012. Pass the necessary journal entries for the redemption of debentures

Solution: Journal in the Books of Rahul Ltd.

Date	Particulars	Dr. (`)	Cr. (`)
	Profit And Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being the required amount transferred to DRR)	25,00,000	25,00,000

	12%Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders' A/c (Being the amount due to Debentureholders on redemption)	25,00,000 1,25,000	 26,25,000
	Debentureholders' A/c Dr. To Bank A/c (Being the amount due to Debentureholders paid)	26,25,000	 26,25,000
	Debenture Redemption Reserve A/c Dr. To General Reserve A/c (Being the DRR transferred to General Reserve on the redemption of all Debentures)	25,00,000	 25,00,000

Note: 1. If in any question it is mentioned that redemption of debenture is out of profit , then the Debenture Redemption Reserve A/c should be created with the full face value(100%) of debentures. If DRR is created only with 50% of the total amount of debentures, it would mean that remaining 50% of the debentures have been redeemed out of capital.

(2) So, it would be clear if in question it is mentioned the redemption is out of profit, then an amount equal to total amount of debentures (100% of face value of debentures) to be transferred to DRR A/c. in all other case (except Companyies exempted by the SEBI) DRR would be created with the 50% of the face of the debentures.

Question Rajesh Ltd. has issued 25,000 ;10% Debentures of ` 100 each of which half the amount is due for redemption on 30th Sept. 2012 at a premium of 5%.The company has in its Debenture Redemption Reserve Account a balance of ` 5,40,000. Record the necessary journal entries at the time of Redemption of Debentures. Journal in the Books of Rajesh Ltd.

Date	Particulars	Dr. (`)	Cr. (`)

	Profit And Loss Appropriation A/c Dr. To Debenture Redemption Reserve A/c (Being the required amount transferred to DRR)	7,10,000	 7,100,000
	12%Debentures A/c Dr. Premium on Redemption of Debentures A/c Dr. To Debentureholders' A/c (Being the amount due to Debentureholders on redemption)	12,50,000 62,500	 13,12,500
	Debentureholders' A/c Dr. To Bank A/c (Being the amount due to Debentureholders paid)	13,12,500	 13,12,500

Note: 1. In this question only half of the total debenture is to be redeemed , as per SEBI guideline A company shall create DRR equivalent to al least of 50% of the amount of debentures issued before starting the redemption of debentures So, DRR A/c is to be created with the amount ` 12,50,000 (e . i. 50% of ` 25,00,000), not related with the amount of debentures to be redeemed.

2. Debenture Redemption Reserve will be transferred to General Reserve when all the debentures are redeemed.

Question--- Pass necessary journal entries in the books of Arbind T. Ltd. in the following case for the redemption of 2,000; 10% Debentures of ` 10 each when issued at par

Debentures redeemed at par by conversion into 13% Preference shares of ` 20 each.

Debentures redeemed at a premium of 10% by conversion into Equity Shares issued at par.
Journal in the Books of Arbind T. Ltd.

Date	Particulars	Dr. (`)	Cr. (`)

	10% Debentures A/c Dr. To Debentureholders' A/c (Being the amount due on redemption)	20,000	 20,000
	Debentureholders' A/c Dr. To 13% Preference Share Capital A/c (amount due to Debentureholders discharged by issue of 1000 preference shares of `20 each re. i. 20,000/20)	20,000	 20,000
	10% Debentures A/c Dr. Premium of Redemption of Debentures A/c Dr. To Debentureholders' A/c (Being the amount due on redemption)	20,000 2,000	 22,000
	Debentureholders' A/c Dr. To Equity Share Capital A/c (amount due to Debentureholders discharged by issue of Equity shares at par))	22,000	 22,000
	10% Debentures A/c Dr. Premium of Redemption of Debentures A/c Dr. To Debentureholders' A/c (Being the amount due on redemption)	20,000 2,000	 22,000
	Debentureholders' A/c Dr. To Equity Share Capital A/c To Securities Premium Reserve A/c (amount due to Debentureholders discharged by issue of Equity shares at a premium of 25% e. i. 22,000/125%=17,600	22,000	 17,600 4,400

Question -- Pass necessary journal entries in the books of M.L.B. Ltd. in the following case for the redemption of 2,000; 10% Debentures of ` 10 each when Debentures originally issued at a discount of 10%

i. Conversion into 13% Preference shares of ` 20 each.

ii. Conversion into Equity Shares of ` 25 issued at par.

Debentures redeemed at premium of 10% by conversion into 12% Debentures of ` 50issued at a par. Journal in the Books of M.L. B. Ltd.

Date	Particulars	Dr. (`)	Cr. (`)
	10% Debentures A/c Dr.	20,000	
	To Debentureholders' A/c		18,000
	To Discount on issue of Debentures A/c		2,000
	(Being the amount due on redemption)		
	Debentureholders' A/c Dr.	18,000	
	To 13% Preference Share Capital A/c		18,000
	(amount due to Debentureholders discharged by issue of 900 preference shares of `20 each re. i. 18,000/20)		
	10% Debentures A/c Dr.	20,000	
	To Debentureholders' A/c		18,000
	To Discount on issue of Debentures A/c		2,000
	(Being the amount due on redemption)		
	Debentureholders' A/c Dr.	18,000	
	To Equity Share Capital A/c		18,,000
	(amount due to Debentureholders discharged by issue of 720Equity shares of `25 at par e. i. 18000/25)		
	10% Debentures A/c Dr.	20,000	
	. To Debentureholders' A/c		20,000
	(Being the amount due on redemption)		
	Debentureholders' A/c Dr.	20,000	
	To 12% Debentures A/c		20,000
	(amount due to Debentureholders discharged by issue of400 ,12% Debentures e. i.		

	20,000/50=400)		

Values involved in issue of SHARE CAPITAL AND DEBENTURES------------

Communication of material information

Complying with legal provisions

Orderliness

Common Size and Comparative Statements

Format of Statement of Profit and Loss

Revenue from operations		xxx
Other Incomes	xxx	
Total Revenue	xxx	
Expenses:		
Cost of material		xxx
Employee benefit expense		xxx
Total Expenses		xxx
Profit before tax		xxx
Tax expense		xxx
Profit after tax		xxx

From the following information prepare a comparative income Statement of victor Ltd.

	2006 `	2007 `
Revenue from Operations	15,00,000	18,00,000
Cost of Goods Sold	11,00,000	14,00,000
Indirect Expenses	20% of Gross Profit	25% of Gross Profit
Income Tax	50%	50%

(C.B.S.E. 2008, Outside Delhi)

❖

❖ **Solution 1.** Comparative Income Statement
For the year 2006 and 2007

Particulars	2006 `	2007 `	Absolute Change `	%Change
Revenue from Operations	15,00,000	18,00,000	3,00,000	+20%
Less: Cost of Goods Sold	11,00,000	14,00,000	3,00,000	+27.27%
Gross Profit	4,00,000	4,00,000		

Less: Indirect Expenses	80,000	1,00,000	20,000	+25%
Net Profit before tax	3,20,000	3,00,000	-20,000	-6.25%
Less: Income Tax	1,60,000	1,50,000	-10,000	-6.25%
Net Profit After Tax	1,60,000	1,50,000	-10,000	-6.25%

Prepare a Comparative Income Statement of Ahmed Ltd., with the help of the following information:

	31.3.2000 `	31.3.2001 `
Revenue from Operations	5,00,000	8,00,000
Cost of Goods Sold	3,00,000	5,00,000
Direct Expenses	40,000	20,000
Indirect Expenses	30,000	40,000
Income Tax	40%	50%

(C.B.S.E. 2002)

Solution 2. Comparative Income Statement

Particular	31.3.2000 `	31.3.2001 `	Absolute Change `	%Change
Revenue from Operations	5,00,000	8,00,000	3,00,000	60,00
Less: Cost of Goods Sold	3,00,000	5,00,000	2,00,000	66.67
Gross Profit	2,00,000	3,00,000	1,00,000	50,00
Less: Indirect Expenses	30,000	40,000	10,000	33.33
Net profit before Tax	1,70,000	2,60,000	90,000	52.94
Less: Income Tax	68,000	1,30,000	62,000	91.18
Net Profit after Tax	1,02,000	1,30,000	28,000	27.45

Hint: Direct expenses are ignored since they are already included in the cost of goods sold.
Prepare a Comparative Income Statement from the following information

Question--

Particulars	31.3.2009 `	31.3.2010 `
Revenues from Operations	30,00,0000	40,00,000
Cost of Goods Sold	60% of Sales	55% of Sales
Paid wages	25,000	30,000
Operating Expenses	20% of Gross Profit	25% of Gross Profit
Income Tax	40%	40%

(C.B.S.E. 20011, Set II)

Solution 3. Comparative Income Statement

for the years ended on 31st March 2009 and 2010

Particular	31.3.2009 `	31.3.2010 `	Absolute Change `	%Increase or Decrease
Revenue from Operations	30,00,000	40,00,000	10,00,000	33.33
Less: Cost of Goods Sold	18,00,000	22,00,000	4,00,000	22.22
Gross Profit	12,00,000	18,00,000	6,00,000	50.00
Less: Operating Expenses	2,40,000	4,50,000	2,10,000	87.50
Net Profit before Tax	9,60,000	13,50,000	3,90,000	40,63
Less: Income Tax @ 40%	3,84,000	5,40,000	1,56,000	40.63
Net Profit after tax	5,76,000	8,10,000	2,34,000	40.63

Note: Wages is a direct expense. It is ignored because it is already included in the cost of goods sold.

1. From the following details make out a comparative and common size statements:

Particulars	*2011* `	*2012* `
Revenue from operations	16,00,000	20,00,000
Cost of Goods Sold	8,00,000	10,00,000

Indirect Expenses 2,00,000 1,00,000
Tax rate 40%

Solution:

Comparative Income Statement

Particulars	*2011 `*	*2012 `*	Absolute Change	% Change
Revenue from operations	16,00,000	20,00,000	4,00,000	25
Less: Cost of Goods Sold	8,00,000	10,00,000	2,00,000	25
Gross Profit	8,00,000	10,00,000	2,00,000	25
Less: Indirect Expenses	2,00,000	1,00,000	(1,00,000)	(50)
Net Profit before Tax	6,00,000	9,00,000	3,00,000	50
Less: Income Tax	2,40,000	3,60,000	1,20,000	50
Net Profit after Tax	3,60,000	5,40,000	1,80,000	50

Common Size Income Statement

Particulars	*2011 `*	*2012 `*	Common Size	
			2011 `	2012 `
Revenue from operations	16,00,000	20,00,000	100	100
Less: Cost of Goods Sold	8,00,000	10,00,000	50	50
Gross Profit	8,00,000	10,00,000	50	50
Less: Indirect Expenses	2,00,000	1,00,000	12.5	5
Net Profit before Tax	6,00,000	9,00,000	37.5	45
Less: Income Tax	2,40,000	3,60,000	15	18
Net Profit after Tax	3,60,000	5,40,000	22.5	27

2. Prepare a comparative and common size income statement with the help of the following information:

Particulars	*2011 `*	*2012 `*
Revenue from operations	8,00,000	10,00,000
Cost of material	4,00,000	6,00,000
Employee benefit expense	1,50,000	2,00,000
Provision for Tax	1,00,000	1,30,000

Solution:

Comparative Income Statement

Particulars	*2011 `*	*2012 `*	Absolute Change	% Change
Revenue from operations	8,00,000	10,00,000	2,00,000	25
Less: Cost of material	4,00,000	6,00,000	2,00,000	50
Gross Profit	4,00,000	4,00,000	0	0
Less: Employee benefit expenses	1,50,000	2,00,000	50,000	33.33
Net Profit before Tax	2,50,000	2,00,000	(50,000)	(20)
Less: Provision for Tax	1,00,000	1,30,000	30,000	30
Net Profit after Tax	1,50,000	70,000	(80,000)	(53.33)

Common Size Income Statement

Particulars	*2011 `*	*2012 `*	Common Size 2011 `	Common Size 2012 `
Revenue from operations	8,00,000	10,00,000	100	100
Less: Cost of material	4,00,000	6,00,000	50	60
Gross Profit	4,00,000	4,00,000	50	40
Less: Employee benefit expenses	1,50,000	2,00,000	18.75	20
Net Profit before Tax	2,50,000	2,00,000	31.25	20
Less: Provision for Tax	1,00,000	1,30,000	12.5	13
Net Profit after Tax	1,50,000	70,000	18.75	7

3. From the following information, prepare a comparative and common size income statement:

Particulars	*2011 `*	*2012 `*
Revenue from Operations	13,20,000	18,00,000
Other Incomes	1,50,000	2,00,000
Cost of material	7,00,000	11,00,000
Employee benefit expense	2,50,000	3,50,000
Tax	50%	50%

Solution:

Comparative Income Statement

Particulars	*2011 `*	*2012 `*	Absolute Change	% Change
Revenue from operations	13,20,000	18,00,000	4,80,000	36.36
Less: Cost of material	7,00,000	11,00,000	4,00,000	57.14
Gross Profit	6,20,000	7,00,000	80,000	12.90
Less: Employee benefit expenses	2,50,000	3,50,000	1,00,000	40
Add: Other Incomes	1,50,000	2,00,000	50,000	33.33
Net Profit before Tax	1,00,000	1,50,000	50,000	50
Less: Provision for Tax	50,000	75,000	25,000	50
Net Profit after Tax	50,000	75,000	25,000	50

Common Size Income Statement

Particulars	*2011 `*	*2012 `*	Common Size 2011 `	Common Size 2012 `
Revenue from operations	13,20,000	18,00,000	100	100
Less: Cost of material	7,00,000	11,00,000	53.03	61.11
Gross Profit	6,20,000	7,00,000	46.97	38.89
Less: Employee benefit expenses	2,50,000	3,50,000	18.94	19.44
Add: Other Incomes	1,50,000	2,00,000	11.36	11.11
Net Profit before Tax	1,00,000	1,50,000	7.58	8.33
Less: Provision for Tax	50,000	75,000	3.79	4.17
Net Profit after Tax	50,000	75,000	3.79	4.16

4. Prepare a horizontal and vertical income statement of 'S Ltd', with the help of the following information:

Particulars	*2011*	*2012*
Revenue from operations	1,00,000	2,00,000
Cost of material (of revenue)	60%	70%
Employee benefit expense (of revenue)	20%	25%
Rate of income tax	50% of profit before tax	

Solution:

Comparative Income Statement

Particulars	*2011* `	*2012* `	Absolute Change	% Change
Revenue from operations	1,00,000	2,00,000	1,00,000	50
Less: Cost of material	60,000	1,40,000	80,000	133.33
Gross Profit	40,000	60,000	20,000	50
Less: Employee benefit expenses	20,000	50,000	30,000	150
Net Profit before Tax	20,000	10,000	(10,000)	(50)
Less: Provision for Tax	10,000	5,000	(5,000)	(50)
Net Profit after Tax	10,000	5,000	(5,000)	(50)

Common Size Income Statement

Particulars	*2011* `	*2012* `	Common Size	
			2011 `	2012 `
Revenue from operations	1,00,000	2,00,000	100	100
Less: Cost of material	60,000	1,40,000	60	70
Gross Profit	40,000	60,000	40	30
Less: Employee benefit expenses	20,000	50,000	20	25
Net Profit before Tax	20,000	10,000	20	5
Less: Provision for Tax	10,000	5,000	10	2.5
Net Profit after Tax	10,000	5,000	10	2.5

5. Prepare comparative and common size income statement with the help of the following information:

Particulars	*2012*	*2011*
Revenue from operations	3,00,000	2,00,000
Cost of material (of revenue)	70%	60%
Employee benefit expense (of revenue)	20%	30%
Income Tax Rate (of profit before tax)	50%	50%

Solution:

Comparative Income Statement

Particulars	*2011 `*	*2012 `*	Absolute Change	% Change
Revenue from operations	2,00,000	3,00,000	1,00,000	50
Less: Cost of material	1,20,000	2,10,000	90,000	75
Gross Profit	80,000	90,000	10,000	12.5
Less: Employee benefit expenses	60,000	60,000	0	0
Net Profit before Tax	20,000	30,000	10,000	50
Less: Provision for Tax	10,000	15,000	5,000	50
Net Profit after Tax	10,000	15,000	5,000	50

Common Size Income Statement

Particulars	*2011 `*	*2012 `*	Common Size	
			2011 `	2012 `
Revenue from operations	2,00,000	3,00,000	100	100
Less: Cost of material	1,20,000	2,10,000	60	70
Gross Profit	80,000	90,000	40	30
Less: Employee benefit expenses	60,000	60,000	30	20
Net Profit before Tax	20,000	30,000	10	10
Less: Provision for Tax	10,000	15,000	5	5
Net Profit after Tax	10,000	15,000	5	5

6. Prepare comparative and common size income statement with the help of the following information:

Particulars	*2012*	*2011*
Revenue from operations	5,00,000	4,00,000
Cost of material (of revenue)	60%	55%
Employee benefit expense (of revenue)	20%	25%
Income Tax Rate (of profit before tax)	50%	50%

Solution:

Comparative Income Statement

Particulars	*2011 `*	*2012 `*	Absolute Change	% Change
Revenue from operations	4,00,000	5,00,000	1,00,000	25
Less: Cost of material	2,20,000	3,00,000	90,000	40.91
Gross Profit	1,80,000	2,00,000	20,000	11.11
Less: Employee benefit expenses	1,00,000	1,00,000	0	0

Net Profit before Tax	80,000	1,00,000	20,000	25
Less: Provision for Tax	40,000	50,000	10,000	25
Net Profit after Tax	40,000	50,000	10,000	25

Common Size Income Statement

Particulars	*2011 `*	*2012 `*	Common Size	
			2011 `	2012 `
Revenue from operations	4,00,000	5,00,000	100	100
Less: Cost of material	2,20,000	3,00,000	55	60
Gross Profit	1,80,000	2,00,000	45	40
Less: Employee benefit expenses	1,00,000	1,00,000	25	20
Net Profit before Tax	80,000	1,00,000	20	20
Less: Provision for Tax	40,000	50,000	10	10
Net Profit after Tax	40,000	50,000	10	10

7. From the following balance sheets, prepare comparative and common size balance sheet of D Ltd.:

Particulars	Note No.	2010-11 `	2011-12 `
Equity and Liabilities			
(1) Shareholders Fund			
(a) Share Capital		15,00,000	20,00,000
(b) Reserves & Surplus		4,00,000	3,00,000
(2) Non Current Liabilities			
Long Term Borrowings		6,00,000	9,00,000
(3) Current Liabilities			
Trade Payables		2,00,000	3,00,000
Total		27,00,000	35,00,000
Assets			
(1) Non Current Assets			
(a) Fixed Assets			
(i) Tangible Assets		15,00,000	20,00,000
(ii) Intangible Assets		6,00,000	9,00,000
(2) Current Assets			
(a) Inventories		4,00,000	3,00,000
(b) Cash and Cash equivalents		2,00,000	3,00,000
Total		27,00,000	35,00,000

Solution:

Comparative Balance Sheet

Particulars	*2011 `*	*2012 `*	Absolute Change	% Change
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	15,00,000	20,00,000	5,00,000	33.33
(b) Reserves & Surplus	4,00,000	3,00,000	(1,00,000)	(25)
(2) Non Current Liabilities				
Long Term Borrowings	6,00,000	9,00,000	3,00,000	50
(3) Current Liabilities				
Trade Payables	2,00,000	3,00,000	1,00,000	50
Total	27,00,000	35,00,000	8,00,000	29.63
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	15,00,000	20,00,000	5,00,000	33.33
(ii) Intangible Assets	6,00,000	9,00,000	3,00,000	50
(2) Current Assets				
(a) Inventories	4,00,000	3,00,000	(1,00,000)	(25)
(b) Cash and Cash equivalents	2,00,000	3,00,000	1,00,000	50
Total	27,00,000	35,00,000	8,00,000	29.63

Common Size Balance Sheet

Particulars	*2011 `*	*2012 `*	Common Size	
			2011 `	2012 `
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	15,00,000	20,00,000	55.56	57.14
(b) Reserves & Surplus	4,00,000	3,00,000	14.81	8.57
(2) Non Current Liabilities				
Long Term Borrowings	6,00,000	9,00,000	22.22	25.71
(3) Current Liabilities				
Trade Payables	2,00,000	3,00,000	7.41	8.58
Total	27,00,000	35,00,000	100	100
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	15,00,000	20,00,000	55.56	57.14
(ii) Intangible Assets	6,00,000	9,00,000	22.22	25.71
(2) Current Assets				
(a) Inventories	4,00,000	3,00,000	14.81	8.57
(b) Cash and Cash equivalents	2,00,000	3,00,000	7.41	8.58
Total	27,00,000	35,00,000	100	100

8. From the following balance sheets, prepare comparative and common size balance sheet of D Ltd.:

Particulars	Note No.	2010-11 `	2011-12 `
Equity and Liabilities			
(1) Shareholders Fund			
(a) Share Capital		30,00,000	40,00,000
(b) Reserves & Surplus		4,00,000	6,00,000
(2) Non Current Liabilities			
Long Term Borrowings		10,00,000	12,00,000
(3) Current Liabilities			
Trade Payables		6,00,000	2,00,000
Total		50,00,000	60,00,000
Assets			
(1) Non Current Assets			
(a) Fixed Assets			
(i) Tangible Assets		30,00,000	40,00,000
(ii) Intangible Assets		6,00,000	2,00,000
(2) Current Assets			
(a) Inventories		10,00,000	12,00,000
(b) Cash and Cash equivalents		4,00,000	6,00,000
Total		50,00,000	60,00,000

Solution:

Comparative Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Absolute Change	% Change
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	30,00,000	40,00,000	10,00,000	33.33
(b) Reserves & Surplus	4,00,000	6,00,000	2,00,000	50
(2) Non Current Liabilities				
Long Term Borrowings	10,00,000	12,00,000	2,00,000	20
(3) Current Liabilities				
Trade Payables	6,00,000	2,00,000	(4,00,000)	(66.67)
Total	50,00,000	60,00,000	10,00,000	20
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	30,00,000	40,00,000	10,00,000	33.33
(ii) Intangible Assets	6,00,000	2,00,000	(4,00,000)	(66.67)
(2) Current Assets				
(a) Inventories	10,00,000	12,00,000	2,00,000	20
(b) Cash and Cash equivalents	4,00,000	6,00,000	2,00,000	50
	50,00,000	60,00,000	10,00,000	20

Total				

Common Size Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Common Size	
			2011 `	2012 `
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	30,00,000	40,00,000	60	66.67
(b) Reserves & Surplus	4,00,000	6,00,000	8	10
(2) Non Current Liabilities				
Long Term Borrowings	10,00,000	12,00,000	20	20
(3) Current Liabilities				
Trade Payables	6,00,000	2,00,000	12	3.33
Total	50,00,000	60,00,000	100	100
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	30,00,000	40,00,000	60	66.67
(ii) Intangible Assets	6,00,000	2,00,000	12	3.33
(2) Current Assets				
(a) Inventories	10,00,000	12,00,000	20	20
(b) Cash and Cash equivalents	4,00,000	6,00,000	8	10
Total	50,00,000	60,00,000	100	100

9. From the following balance sheets, prepare comparative and common size balance sheet of D Ltd.:

Particulars	Note No.	2011-12 `	2010-11 `
Equity and Liabilities			
(1) Shareholders Fund			
Share Capital		3,50,000	3,00,000
(2) Non Current Liabilities			
Long Term Borrowings		1,00,000	2,00,000
(3) Current Liabilities			
Trade Payables		1,50,000	1,00,000
Total		6,00,000	6,00,000
Assets			
(1) Non Current Assets			
Fixed Assets			
(i) Tangible Assets		4,00,000	3,00,000
(2) Current Assets			
(a) Inventories		2,00,000	3,00,000
Total		6,00,000	6,00,000

Solution:

Comparative Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Absolute Change	% Change
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	3,00,000	3,50,000	50,000	16.67
(2) Non Current Liabilities				
Long Term Borrowings	2,00,000	1,00,000	(1,00,000)	(50)
(3) Current Liabilities				
Trade Payables	1,00,000	1,50,000	50,000	50
Total	6,00,000	6,00,000	0	0
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	3,00,000	4,00,000	1,00,000	33.33
(2) Current Assets				
(a) Inventories	3,00,000	2,00,000	(1,00,000)	(33.33)
Total	6,00,000	6,00,000	0	0

Common Size Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Common Size	
			2011 `	2012 `
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	3,00,000	3,50,000	50	58.33
(2) Non Current Liabilities				
Long Term Borrowings	2,00,000	1,00,000	33.33	16.67
(3) Current Liabilities				
Trade Payables	1,00,000	1,50,000	16.67	25
Total	6,00,000	6,00,000	100	100

Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	3,00,000	4,00,000	50	66.67
(2) Current Assets				
(a) Inventories	3,00,000	2,00,000	50	33.33
Total	6,00,000	6,00,000	100	100

10. From the following balance sheets, prepare comparative and common size balance sheet of D Ltd.:

Particulars	Note No.	2010-11 `	2011-12 `
<u>Equity and Liabilities</u>			
(1) Shareholders Fund			
(a) Share Capital		9,00,000	7,50,000
(b) Reserves & Surplus		2,25,000	1,50,000
(2) Non Current Liabilities			
Long Term Borrowings		3,00,000	4,20,000
(3) Current Liabilities			
Trade Payables		5,55,000	5,85,000
Total		19,80,000	19,05,000
<u>Assets</u>			
(1) Non Current Assets			
(a) Fixed Assets			
(i) Tangible Assets		11,55,000	12,45,000
(2) Current Assets			
(a) Inventories		8,25,000	6,60,000
Total		19,80,000	19,05,000

Solution:

Comparative Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Absolute Change	% Change
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	9,00,000	7,50,000	(1,50,000)	(16.67)
(b) Reserves & Surplus	2,25,000	1,50,000	(75,000)	(33.33)
(2) Non Current Liabilities				
Long Term Borrowings	3,00,000	4,20,000	1,20,000	40
(3) Current Liabilities				

Trade Payables	5,55,000	5,85,000	30,000	5.41
Total				
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets				
(2) Current Assets	19,80,000	19,05,000	75,000	3.79
(a) Inventories				
Total				
	11,55,000	12,45,000	90,000	7.79
	8,25,000	6,60,000	(1,65,000)	20
	19,80,000	19,05,000	75,000	3.79

Common Size Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Common Size 2011 `	Common Size 2012 `
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	9,00,000	7,50,000	45.45	39.37
(b) Reserves & Surplus	2,25,000	1,50,000	11.36	7.87
(2) Non Current Liabilities				
Long Term Borrowings	3,00,000	4,20,000	15.15	22.05
(3) Current Liabilities				
Trade Payables	5,55,000	5,85,000	28.04	30.71
Total	19,80,000	19,05,000	100	100
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	11,55,000	12,45,000	58.33	65.35
(2) Current Assets				
(a) Inventories	8,25,000	6,60,000	41.67	34.65
Total	19,80,000	19,05,000	100	100

11. From the following balance sheets, prepare comparative and common size balance sheet of D Ltd.:

Particulars	Note No.	2010-11 `	2011-12 `
<u>Equity and Liabilities</u>			

(1) Shareholders Fund			
(a) Share Capital		25,00,000	25,00,000
(b) Reserves & Surplus		5,00,000	6,00,000
(2) Non Current Liabilities			
Long Term Borrowings		15,00,000	15,00,000
(3) Current Liabilities			
Trade Payables		5,00,000	5,50,000
Total		50,00,000	51,50,000
Assets			
(1) Non Current Assets			
(a) Fixed Assets			
(i) Tangible Assets		30,00,000	36,00,000
(b) Non Current Investments		5,00,000	5,00,000
(2) Current Assets			
(a) Inventories		15,00,000	10,50,000
Total		50,00,000	51,50,000

Solution:

Comparative Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Absolute Change	% Change
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	25,00,000	25,00,000	0	0
(b) Reserves & Surplus	5,00,000	6,00,000	1,00,000	20
(2) Non Current Liabilities				
Long Term Borrowings	15,00,000	15,00,000	0	0
(3) Current Liabilities				
Trade Payables	5,00,000	5,50,000	50,000	10
Total	50,00,000	51,50,000	1,50,000	3
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	30,00,000	36,00,000	6,00,000	20
(b) Non Current Investments	5,00,000	5,00,000	0	0
(2) Current Assets				
(a) Inventories	15,00,000	10,50,000	(4,50,000)	(3)
Total	50,00,000	51,50,000	1,50,000	3

Common Size Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Common Size	
			2011 `	2012 `
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	25,00,000	25,00,000	50	48.54
(b) Reserves & Surplus	5,00,000	6,00,000	10	11.65
(2) Non Current Liabilities				
Long Term Borrowings	15,00,000	15,00,000	30	29.13
(3) Current Liabilities				
Trade Payables	5,00,000	5,50,000	10	10.68
Total	50,00,000	51,50,000	100	100
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	30,00,000	36,00,000	60	69.90
(b) Non Current Investments	5,00,000	5,00,000	10	9.71
(2) Current Assets				
(a) Inventories	15,00,000	10,50,000	30	20.39
Total	50,00,000	51,50,000	100	100

12. From the following balance sheets, prepare a Comparative and Common Size Balance Sheet of Asha Ltd. :

Particulars	Note No.	2012 `	2011 `
1. Equity and Liabilities			
(1) Shareholders' funds			
Share Capital		7,50,000	6,00,000
(2) Current Liabilities			
Trade Payables		2,00,000	2,50,000
Total		9,50,000	8,50,000
II. Assets			
(1) Non-Current Assets			
Fixed Assets			
(i) Tangible Assets		4,00,000	5,00,000
(2) Current Assets			
a) Inventories		1,00,000	1,00,000
b) Trade receivables		3,50,000	2,00,000
c) Cash and Cash Equivalents		1,00,000	50,000
Total		9,50,000	8,50,000

Solution:

Comparative Balance Sheet

Particulars	*2011* `	*2012* `	Absolute Change	% Change
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	6,00,000	7,50,000	1,50,000	25
(2) Current Liabilities				
Trade Payables	2,50,000	2,00,000	(50,000)	(20)
Total	8,50,000	9,50,000	1,00,000	11.76
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	5,00,000	4,00,000	(1,00,000)	(20)
(2) Current Assets				
a) Inventories	1,00,000	1,00,000	0	0
b) Trade receivables	2,00,000	3,50,000	1,50,000	75
c) Cash and Cash Equivalents	50,000	1,00,000	50,000	100
Total	8,50,000	9,50,000	1,00,000	11.76

Common Size Balance Sheet

Particulars	*Mar. 31, 2011* `	*Mar. 31, 2012* `	Common Size	
			2011 `	2012 `
Equity and Liabilities				
(1) Shareholders Fund				
(a) Share Capital	6,00,000	7,50,000	70.59	78.95
(2) Current Liabilities				
Trade Payables	2,50,000	2,00,000	29.41	21.05
Total	8,50,000	9,50,000	100	100
Assets				
(1) Non Current Assets				
(a) Fixed Assets				
(i) Tangible Assets	5,00,000	4,00,000	58.82	42.11
(2) Current Assets				
a) Inventories	1,00,000	1,00,000	11.76	10.53
b) Trade receivables	2,00,000	3,50,000	23.53	36.84
c) Cash and Cash	50,000	1,00,000	5.89	10.52

Equivalents Total	8,50,000	9,50,000	100	100

Values involved in Comparative Analysis and Common size statements—

Critical analysis

Decision making

Scientific temperament

Transparency

Comparative financial information for interested parties

Core Values involved in RATIO ANALYSIS—

❖ Transparancy

❖ Security—financial

❖ Efficiency in utilization of resourses provided by community

❖ Scientific and critical analysis

Accounting Ratios

Question 4.

Calculate the current ratio and quick ratio from the following particulars and also give your comments about the same:

		`
Cash		4,000
Trade Receivables		1,00,000
Inventories:	`	
Raw Materials	20,000	
Worker-in-Progress	70,000	
Finished Goods	60,000	1,50,000
Prepaid Expenses		5,000
Land and Buildings		2,50,000
Patents		18,000
Loose Tools		26,000
Goodwill		1,00,000
Bank Overdraft		55,000
Trade Payables		85,000

15% Debentures	80,000

SOLUTION 4.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Current Assets = Cash + Trade Receivables + Inventories + Prepaid Expenses

= `4,000 + 1,00+000 + 1,50,000 + 5,000

= `2,59,000

Current Liabilities = Bank Overdraft + Trade Payables

= `55,000 + 85,000

= `1,40,000

$$\text{Current Ratio} = \frac{2,59,000}{1,40,000} = 1.85 : 1$$

$$\text{Quick Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}$$

Liquid Assets = Cash + Trade Receivables

= `4,000 + 1,00,000 = `1,04,000

$$\text{Quick Ratio} = \frac{1,04,000}{1,40,000} = .743 : 1$$

Comments: The ideal current ratio should be 2 : 1. But in this case the current ratio is 1.85 : 1 which is less than the idela ratio. Therefore, it can be said that the short-term financial position of the company is not satisfactory.

The ideal quick ratio should be 1 : 1. But in this case the quick ratio is .743 : 1, hence, the short-term financial position cannot be said to be satisfactory.

QUESTION 5.

Calculate (i) Debt-Equity Ratio; (ii) Total Assets to Debt Ratio; and (iii) Proprietary Ratio from the particulars given in the following balance sheet:

BALANCE SHEET

As at 31st March, 2012

Particulars		`
I. EQUITY AND LIABILITIES		
Equity Share Capital		3,00,000
Preference Share Capital		1,00,000
Reserves		50,000
Profit & Loss Balance		65,000
12% Mortgage Loan		1,80,000
Current Liabilities		1,20,000
	TOTAL	8,15,000
II. ASSETS:		
Fixed Assets		4,50,000
Share Issue Expenses		15,000
Current Assets		3,50,000
	TOTAL	8,15,000

What conclusions do you draw from the above ratios?

SOLUTION 5.

(i) Debt Equity Ratio = $\frac{\text{Debt}}{\text{Equity}}$ or $\frac{\text{Long term Loans}}{\text{Shareholder's Funds}}$

Shareholder's Funds = Equity Share Capital + Pref. Share Capital + Reserves + P & L Balance – Share Issue Exp.

= 3,00,000 + 1,00,000 + 50,000 + 65,000 – 15,000

= 5,00,000

Mortgage Loan is Long Term Loan,

Hence, Debt Equity Ratio = $\frac{1,80,000}{5,00,000} = .36:1$

Comments: This ratio indicates what proportion of funds is provided by Long-term loans in comparison to Shareholder's funds. Generally, the ratio should not be more than 2 : 1. Debt-Equity ratio of the above company is .36:1, which indicates that long-term loans are only .36 in comparison to shareholder's funds. Hence, it may be considered that the long-term financial position of the company is very sound.

(ii) Total Assets to Debt Ratio = $\frac{\text{Total Assets}}{\text{Debt}}$

$= \frac{\text{Fixed Assets} + \text{Current Assets}}{\text{Long-term Loans}}$

$= \frac{4,50,000 + 3,50,000}{1,80,000} = 4.44:1$

Comments: Total assets of this company are 4.44 times in comparison to long-term debts of the company. The higher ratio indicates the use of lower debts in financing the assets which means higher security to lenders.

(iii) Proprietary Ratio = $\frac{\text{Equity}}{\text{Total Assets}}$

$= \frac{\text{Shareholder's Funds}}{\text{Fixed Assets} + \text{Current Assets}}$

$= \frac{5,00,000}{4,50,000 + 3,50,000}$

= 0.625 or 62.5%

Comments: Shareholder's Funds of this Company are 62.5% in comparison to total assets of the company. In other words, 62.5% of the total assets of the company are funded by equity which indicates that the long-term financial position of the company is very sound.

QUESTION 6.

From the following balance sheet and other information calculate (i) Working Capital Turnover Ratio, (ii) Debt Equity Ratio and (iii) Trade Receivables Turnover Ratio.

BALANCE SHHET

As at 31st March, 2012

Particulars		`
I. EQUITY AND LIABILITIES		
Share Capital		2,00,000
General Reserve		80,000
Profit and Loss		1,20,000
Loan @ 15%		2,40,000
Trade Payables		1,00,000
	TOTAL	7,40,000
II. ASSETS:		
Fixed Assets		3,60,000

Inventory		80,000
Trade Receivables	1,80,000	
Cash		1,00,000
Preliminary Expenses		20,000
	TOTAL	7,40,000

(i) Sales during the year amounted to `3,80,000.

(ii) Sales returns during the year amounted to `20,000.

SOLUTION 6.

(i) Working Capital Turnover Ratio = $\dfrac{\text{Net Sales}}{\text{Working Capital}}$

Current Assets = Cash + Inventory + Trade Receivables

= `1,00,000 + `80,000 + `2,60,000

= `3,60,000

Current Liabilities = Trade Payables

= `1,00,000

Working Capital = Current Assets – Current Liabilities

= `3,60,000 – `1,00,000 = `2,60,000

Working Capital Turnover Ratio = $\dfrac{3,60,000}{2,60,000} = 1.38 \text{ times}$

(ii) Debt-Equity Ratio = $\dfrac{\text{Debt}}{\text{Equity}}$ or $\dfrac{\text{Long term Loans}}{\text{Shareholder's Funds}}$

Long term Loans = Loan @ 15%

= `2,40,000

Shareholder's Funds = Share Capital + General Reserve + Profit and Loss (–) Preliminary Expenses

= `2,00,000 + `80,000 + `1,20,000 – `20,000

= `3,80,000

$$\text{Debt-Equity Ratio} = \frac{2,40,000}{3,80,000} = .63:1$$

$$\text{(iii) Trade Receivables Turnover Ratio} = \frac{\text{Net Sales}}{\text{Trade Receivables}}$$

$$\text{Trade Receivables Turnover Ratio} = \frac{3,60,000}{1,80,000} = 2 \text{ times}$$

QUESTION 7.

Following is the Balance of X Ltd. As on 31st March, 2012:

Particulars		`
I. EQUITY AND LIABILITIES		
Share Capital		20,00,000
Reserve		5,00,000
Profit for the year		12,00,000
10% Loans		10,00,000
Current Liabilities		8,00,000
	TOTAL	55,00,000
II. ASSETS:		
Fixed Assets		29,00,000
Current Assets		25,00,000
Underwriting Commission		1,00,000
	TOTAL	55,00,000

Find out 'Return on Capital Employed.

SOLUTION 7.

$$\text{Return on Capital Employed} = \frac{\text{Profit before Interest and Tax}}{\text{Capital Empoyed}} \times 100$$

Profit before Interest =

	`
Profit for the year	12,00,000
Add: Interest on Loan (10% on 10,00,000)	1,00,000
	13,00,000

Capital Employed = Share Capital + Reserves + Loans + Profit for the year Underwriting Commission

= `20,00,000 + `5,00,000 + `10,000,000 + `12,00,000 – `1,00,000

= `46,00,000

$$\text{Return on Capital Employed} = \frac{`13,00,000}{`46,00,000} \times 100 = 28.26\%$$

Working Note: Capital Employed can also be calculated as under:

	`
Fixed Assets	29,00,000
Add: Working Capital (Current Assets `25,00,000	
Less Current	17,00,000
Liabilities `8,00,000)	46,00,000

QUESTION 8.

Following is the Balance Sheet of X Ltd. as on 31st March, 2012.

Particulars	`
I. EQUITY AND LIABILITIES	
Equity Share Capital: 40,000 Equity Shares of `10 each	4,00,000

12% Preference Share Capital		2,00,000
Reserves		50,000
Profit & Loss Balance		2,20,000
15% Debentures		1,00,000
Current Liabilities		2,30,000
	TOTAL	12,00,000
II. ASSETS:		
Fixed Assets		8,00,000
Underwriting Commission		20,000
Current Assets		3,80,000
	TOTAL	12,00,000

Profit for the current year before payment of Interest and Tax amounted to `3,55,000. You are required to calculate Return on Investment (R.O.I.).

SOLUTION 8.

Return on Investment (R.O.I) = $\frac{\text{Profit before Interset and Tax}}{\text{Capital Employed}}5100$

Capital Employed = Equity Share Capital + Preference Share Capital + Reserves + P & L A/c + Debentures – Underwriting Commission

= `4,00,000 + `2,00,000 + `50,000 + `2,20,000 + `1,00,000 – `20,000

= `9,50,000

R.O.I = $\frac{3,55,000}{9,50,000} \times 100 = 37.43\%$

Note: When a Balance Sheet is given in the question, the Profit & Loss A/c balance given in it already includes the Current Year's profit. Hence, it is not added again while calculating capital employed.

Cash-Flow Statement

According to

Revised Schedule VI Part I of Companies Act, 1956

Cash-Flow Statement

QUESTION

Prepare a Cash Flow Statement from the following Balance Sheets of Gokaldas Exports Ltd.

Particulars	Note No.	31-3-2011 `	31-3-2012 `
A. **EQUITY AND LIABILITIES**			
1. Shareholders' Funds			
(a) Share Capital		4,00,000	5,00,000
(b) Reserves and Surplus	1	2,35,000	3,25,000
2. Non-Current Liabilities			
(a) Long term borrowings	2	3,00,000	3,10,000
3. Current Liabilities			
(a) Trade Payables 80,000		95,000	
TOTAL		10,15,000	12,30,000
B. **ASSETS:**			
1. Non-Current Assets			
(a) Fixed Assets			

(i) Tangible Assets	3	5,00,000	7,00,000
(b) Non-Current Investments		70,000	56,000
(c) Other Non-Current Assets	4	20,000	15,000
2. Current Assets			
(a) Inventories		2,10,000	2,80,000
(b)Trade Receivables		1,40,000	1,14,000
(c) Cash and Cash equivalents	5	70,000	60,000
(d) Other Current Assets	6	5,000	5,000
TOTAL		10,15,000	12,30,000

Total interest paid during the year amounted to ` 37,800.

Note 1

Particulars	As on 31.3.2011 (`)	As on 31.3.2012 (`)
General Reserve	1,25,000	1,35,000
Profit & Loss Balance	1,10,000	1,90,000

Note 2

Particulars	As on 31.3.2011 (`)	As on 31.3.2012 (`)
12% Debentures	2,00,000	1,50,000
14% Mortgage Loan	1,00,000	1,60,000

Note 3

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
(i) Tangible Assets		
Machinery	5,00,000	7,00,000

Note 4

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Unmortised Expenses	20,000	15,000

Note 5

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Cash	20,000	40,000
Bank	50,000	20,000

Note 6

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Unmortised Expenses	5,000	5,000

SOLUTION 9.

CASH FLOW STATEMENT (Indirect Method)

A. Cash flows from Operating Activities:		`	`
Net profit before taxation			
Profit as per Profit & Loss Statement		20,000	
(`60,000–`40,000)			
Adjustments for:			
Goodwill written off		30,000	
Preliminary Expenses written off		8,000	
Interest Paid		9,000	
Operating profit before working capital change		67,000	
Add: Decrease in Current Assets:			
Prepaid Expenses	2,000		
Add: Increase in Current Liabilities			
Trade Payables	15,000		
Outstanding Expenses	10,000	27,000	
		94,000	
Less: Increase in Current Assets:			
Inventories (Stock)	40,000		
Trade Receivables	70,000	1,10,000	
Net cash used in operating activities		(16,000)	(16,000)
B. Cash flows from Investing Activities:			
Purchase of Land & Buildings		(80,000)	

Purchase of Long-term Investments	(25,000)		
Net cash used in investing activities	(1,05,000)	(1,05,000)	

C. Cash flows from Financing Activities:

Issue of shares		1,00,000	
Proceeds from Public Deposits		45,000	
Interest Paid		(9,000)	
Net cash from financing activities	1,36,000	1,36,000	
Net Increase in cash and cash equivalents		15,000	
Cash and cash equivalents at the beginning of the period (See Note 1)			45,000
Cash and cash equivalents at the end of the period (See Note 1)			60,000

Note: (1) Cash and cash equivalents include cash in hand, bank balance and short-term investments. Hence cash and cash equivalents in this question will amount to:

		2011	**2012**
		`	`
Cash		15,000	13,000
Bank		20,000	32,000
Short-term Investments		10,000	15,000
	45,000	60,000	

QUESTION

From the following Balance Sheets of Voltamp Ltd. as on 31.3.2011 and 31.3.2012, prepare a Cash Flow Statement:

Particulars	Note No.	31-3-2011 `	31-3-2012 `
A. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		2,00,000	2,00,000
(b) Reserves and Surplus	1	1,10,000	1,75,000
2. Current Liabilities			
(a) Trade Payables 1,39,000		1,28,000	
(b) Other Current Liabilities	2	6,000	
(c) Short-term Provisions	3	35,000	45,000
TOTAL		4,90,000	5,48,000
B. ASSETS:			
1. Non-Current Assets			
(a) Fixed Assets			
(i) Tangible Assets	4	1,50,000	2,00,000
(i) Intangible Assets	5	40,000	30,000
(b) Other Non-Current Assets	6	23,000	16,000
2. Current Assets			

(a) Current Investments		12,000	15,000
(b) Inventories		1,80,000	2,15,000
(c)Trade Receivables		60,000	50,000
(c) Cash and Cash equivalents		8,000	10,000
(d) Short-term Loans and advances	7	10,000	5,000
(d) Other Current Assets	8	7,000	7,000
TOTAL		4,90,000	5,48,000

Note 1

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
General Reserve	1,00,000	1,00,000
Profit & Loss Balance	10,000	1,75,000

Note 2

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Outstanding Salaries	6,000	—

Note 3

Particulars	As on 31.3.2011 (`)	As on 31.3.2012 (`)
(c) Short-term Provisions		
Provision for Taxation	35,000	45,000

Note 4

Particulars	As on 31.3.2011 (`)	As on 31.3.2012 (`)
Machinery	1,50,000	2,00,000

Note 5

Particulars	As on 31.3.2011 (`)	As on 31.3.2012 (`)
Goodwill	40,000	30,000

Note 6

Particulars	As on 31.3.2011 (`)	As on 31.3.2012 (`)
Unmortised Expenses	23,000	16,000

Note 7

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Prepaid Expenses	10,000	5,000

Note 6

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Unmortised Expenses	7,000	7,000

Additional Information:

I. Machinery whose original cost was ` 50,000 was sold for ` 10,000 during the year. Accumulated depreciation on this machinery was ` 26,000.

II. Depreciation on Machinery charged during the year ` 20,000.

III. Dividend paid during the year @10% on Equity share Capital.

SOLUTION

CASH FLOW STATEMENT (Indirect Method)

A. Cash flows Operating Activities:

Net profit before taxation:		
Increase in Reserves & Surplus	65,000	
+Provision for Taxation for 2012	45,000	
+Dividend paid (10% on ` 2,00,000)	20,000	1,30,000
Adjustments for:		

	Depreciation on Machinery	20,000		
	Loss on sale of Machinery	14,000		
	Goodwill written off	10,000		
	Preliminary Expenses written off	4,000		
	Underwriting commission			
	Written off	3,000	51,000	
	Operating profit before working		1,81,000	
	capital changes			
	Add: Decrease in Current Assets:			
	Trade Receivable	10,000		
	Prepaid Expenses	5,000	15,000	
			1,96,000	
	Less: Increase in Current Assets:			
	Inventory (Stock)	35,000		
	Less: Decrease in Current Liabilities:			
	Trade Payable	11,000		
	Outstanding Salaries	6,000	52,000	
			1,44,000	
	Payment of Tax (for 2011)		35,000	
	Net cash from operating activities		1,09,000	1,09,000
B.	**Cash flows from Investing Activities:**			
	Purchase of Machinery (1)		(94,000)	
	Sale of Machinery		10,000	
	Net cash used in investing activities		(84,000)	(84,000)

C. Cash flows from Financing Activities:

Dividend paid	(20,000)	(20,000)
Net increase in cash and cash equivalents	5,000	
Cash and cash equivalents at the beginning of the period (Bank`8,000+Short term Investments `12,000)	20,000	
Cash and cash equivalents at the end of the period (Bank ` 10,000 + Short term Investments `15,000)	25,000	

Working Note:

1.

MACHINERY ACCOUNT

(On written down value)

	`		`
To Balanced b/d	1,50,000	By Bank (Sale)	10,000
To Bank A/c (Balancing Fig. being purchase)	94,000	By P & L A/c (Loss)	
		By Current Year's Depreciation	20,000
		By Balanced c/d	2,00,000
	2,44,000		2,44,000

QUESTION

From the following Balance Sheets of Virgo Global Media Limited, as on 31.3.2011 and 31.3.2012, prepare a Cash Flow Statement:

Particulars	Note No.	31-3-2011 `	31-3-2012 `
A. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		90,000	1,30,000
(b) Reserves and Surplus	1	50,000	85,000
2. Current Liabilities			
(a) Trade Payables 17,400		22,000	
TOTAL		1,57,400	2,37,000
B. ASSETS:			
1. Non-Current Assets			
(a) Fixed Assets			
(i) Tangible Assets		93,400	1,66,000
(b) Other Non-Current Assets	2	1,000	
2. Current Assets			
(a) Inventories		22,000	26,000
(b)Trade Receivables		36,000	39,000
(c) Cash and Cash equivalents		4,000	5,000
(d) Other Current Assets	3	1,000	1,000
TOTAL		1,57,400	2,37,000

Note 1

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
General Reserve	30,000	55,000
Profit & Loss Balance	20,000	30,000

Note 2

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Unmortised Expenses	1,000	

Note 3

Particulars	As on 31.3.2011	As on 31.3.2012
	(`)	(`)
Unmortised Expenses	1,000	1,000

Additional Information:

I. Depreciation charged on fixed assets for the year 2011-2012 was ` 20,000.

II. Income Tax ` 5,000 has been paid during the year.

(C.B.S.E. 2011, Outside Delhi)

SOLUTION

CASH FLOW STATEMENT

For the year ended 31st March, 2012

		`	`
A. Cash flows from Operating Activities:			
Net Profit before tax:			
Profit as per Balance Sheet (`30,000 – `20,000)	10,000		
+ Income Tax Paid	5,000		
+ Transfer to Reserve	25,000		
Add: Item to be added (Non-cash items)		21,000	
Depreciation	20,000	61,000	
Preliminary Expenses written off	1,000	4,600	
Operating profit before Working Capital Changes		65,600	
Add: Increases in Trade Payables			
		7,000	53,000
Less: Increase in Inventory	4,000	58,600	
Increase in Trade Receivables	3,000	5,000	
Cash Flow from Operating Activities before Tax			(92,600)
Less: Income Tax Paid			
Cash Flow from Operating Activities after Tax		(92,600)	
B. Cash flows from Investing Activities:			40,000
Purchase of fixed assets (None 1)			1,000
Net Cash used in Investing Activities		40,000	4,000
C. Cash flows from Financing Activities			5,000
Issue of Share Capital			
Cash flow from Financing Activities			
D. Net Increase in Cash & Cash Equivalents (A + B + C)			
Add: Cash & Cash Equivalents at the Beginning of the period			
Cash & Cash Equivalents at the end of the period			

Working Note: (1)

Particulars	`	Particulars	`
To Balance b/d	93,400	By Depreciation A/c	20,000
To Bank A/c (Purchases)		By Balance c/d	1,66,000
(Balancing figure)	92,600		
	1,86,000		1,86,000

QUESTION

From the following information, prepare Cash Flow Statement:

Balance Sheet

as at 31.03.2012 and 31.03.2011

	Particulars	Note No.	31-3-2012 `	31-3-2011 `
A.	**EQUITY AND LIABILITIES**			
	1. Shareholders’ Funds			
	(a) Share Capital	1	1,00,000	80,000
	(b) Reserves and Surplus	2	6,400	6,000
	2. Non-Current Liabilities			
	(a) Long-term Borrowings	3	14,000	12,000
	2. Current Liabilities			
	(a) Trade Payables 22,000		24,000	
	(b) Short-term Provisions	4	20,000	16,000
	TOTAL		1,62,400	1,38,000
B.	**ASSETS:**			
	1. Non-Current Assets			
	(a) Fixed Assets			

(i) Tangible Assets		50,000	60,000
2. Current Assets			
(a) Inventories		70,000	60,000
(b)Trade Receivables		48,000	40,000
(c) Cash and Cash equivalents	5	(6,600)	(22,600)
(d) Short-term Loans and advances		1,000	600
TOTAL		1,62,400	1,38,000

Note 1

Particulars	As on 31.3.2012	As on 31.3.2011
	(`)	(`)
Equity Share Capital	80,000	55,000
12% Preference Share Capital	20,000	25,000

Note 2

Particulars	As on 31.3.2012	As on 31.3.2011
	(`)	(`)
General Reserve	4,000	4,000
Profit & Loss Balance	2,400	2,000

Note 3

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
15% Debentures	14,000	12,000

Note 4

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
Provision for Taxation	8,400	6,000
Proposed Dividend	11,600	10,000

Note 5

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
Cash	7,000	2,400
Bank Overdraft	(13,600)	(25,000)

Additional Information:

(a) Provision for tax made ` 9,400.

(b) Fixed assets sold for ` 10,000, their cost ` 20,000 and accumulated depreciation till date of sale is ` 6,000.

(c) An interim dividend paid during the year ` 9,000.

(d) Depreciation charged during the year ` 8,000.

SOLUTION

CASH FLOW STATEMENT (Indirect Method)

for the year ended 31st March, 2012

		`	`
A. Cash Flows from Operating Activities			
Net profit before taxation:			
Profit as per Balance Sheet (`2,400 - `2,000)	400		
+ Proposed Dividend for 2012	11,600		
+ Interim Dividend paid	9,000		
+ Provision for Taxation	9,400	34,000	
Adjustments for:			
Depreciation (3)	14,000		
Loss on sale of fixed assets	4,000		
Interest on Debentures	1,800	19,800	
Operating profit before working capital changes		50,200	
Less: Increase in Current Assets:			
Inventories	10,000		
Trade Receivables	8,000		
Prepaid Expenses	400		

Decrease in Current Liabilities:

Trade Payables 2,000

(20,400)

Cash generated from operating activities 29,800

Less: Income Tax paid (4) (7,000)

Net cash from Operating Activities 22,800 22,800

B. Cash Flows from Investing Activities:		
Sale of Fixed assets	(10,000)	
Purchase of fixed Assets (2)	(18,000)	
Net Cash used in investing activities	(8,000)	(8,000)
C. Cash Flows from Financing Activities:		
Issue of equity share capital	25,000	
Redemption of performance share capital	(5,000)	
Issue of Debentures	2,000	
Payment of proposed dividend (for 2011)	(10,000)	
Interim dividend paid	(9,000)	
Net cash from financing activities	1,200	1,200
Net Increase in cash and cash equivalents		16,000
Cash and cash equivalents at the beginning of the period (Cash `2,400 – Bank Overdraft `25,000)		(22,600)
Cash and cash equivalents at the end of the period (Cash `7,000 – Bank Overdraft ` 13,600)		(6,600)

Working Notes: (1) It is assumed that debentures have been issued at the end of current accounting period. Hence interest on debentures is 15% on ` 12,000.

(2) Fixed Assets Account (On Original Cost)

` `

To Balance b/d 82,000 By Bank (Sale) 10,000

To Bank (Balancing figure,

being purchase) 18,000 By Accumulated Depreciation A/c (Being depreciation on fixed assets sold) 6,000

By P & L A/c (Loss on 4,000

sale of fixed assets)

By Balance c/d 80,000

1,00,000 1.00.000

(3) Accumulated Depreciation Account

To Fixed Assets A/c (transfer of depreciation on fixed assets sold) 6000 By Balance b/d 22,000

By P & L A/c (Balancing figure, being current year's deprecation) 14,000

To Balance c/d 30,000

36,000 36,000

(4) Provision tax Account

` `

To Bank (balancing figure, By Balance b/d (Given) 6,000

Being payment made) 7,000 By P & L A/c (provision

made In 2012 (Given) 9,400

15,400 15,400

Question

Prepare a cash flow statement from the following:

Income Statement

(for the year ended 31st march, 2012)

	`	`
Sales	25,40,000	
Less: Cost of goods sold		20,60,000
Gross profit		4,80,000
Less: Operating expenses (including depreciation on Machinery ` 54,000)	1,90,000	
Goodwill written off	16,000	
Interest on Debentures	20,000	
Provision for Tax	34,000	2,60,000
Net Income		2,20,000

Particulars	Note No.	31-3-2012 `	31-3-2011 `
A. EQUITY AND LIABILITIES			
1. Shareholders' Funds			

(a) Share Capital		5,00,000	4,00,000
(b) Reserves and Surplus	1	3,96,000	1,66,000
2. Non-Current Liabilities			
(a) Long-term borrowings	2	1,50,000	2,00,000
3. Current Liabilities			
(a) Trade Payables		1,06,000	70,000
(b) Other Current Liabilities	3		4,000
(c) Short-term Provisions	4	32,000	25,000
TOTAL		11,84,000	8,65,000
B. ASSETS:			
1. Non-Current Assets			
(a) Fixed Assets			
(i) Tangible Assets	5	6,18,000	3,60,000
(i) Intangible Assets	6	24,000	40, 000
(b) Non-Current Investments		76,000	50,000
2. Current Assets			
(a) Current Investments		8,000	10,000
(b) Inventories		2,80,000	2,33,000
(c)Trade Receivables		1,36,000	1,50,000
(d) Cash and Cash equivalents		42,000	22,000

TOTAL	11,84,000	8,65,000

Note 1

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
Securities Premium	10,000	
Reserves & surplus	3,86,000	1,66,000

Note 2

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
12% Debentures	1,50,000	2,00,000

Note 3

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
Outstanding Expenses		4,000

Note 4

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
Provision for Taxation	32,000	25,000

Note 5

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
Building	1,88,000	
Machinery	4,30,000	3,60,000

Note 6

Particulars	As on 31.3.2012 (`)	As on 31.3.2011 (`)
Goodwill	24,000	40,000

SOLUTION

CASH FLOW STATEMENT

(Indirect Method)

A. **Cash flows from operating activities:**	`	`
Net Profit before taxation:		
Net Profit ` 2,20,000 + Provision		2,54,000
for tax `34,000)		
Adjustments for:		
Depreciation on Machinery		54,000
Goodwill written off	16,000	
Interest on Debentures		20,000
Operating profit before working capital	3,44,000	
Changes		
Add: Decrease in Current Assets:		
Trade Receivables	14,000	
Add: Increase in Current		
Liabilities:		
Trade Payables 14,000		
Add: Increase in Current Assets:		
Trade Payables 36,000	50,000	
		3,94,000
Less: Increase in Current Assets:		
Inventory	47,000	
Less: Decrease in Current Liabilities:		
Accrued Expenses	4,000	51,000

Cash generated from operating activities		3,43,000	
Payment of Tax(1)		(27,000)	
Net Cash from operating activities		3,16,000	3,16,000
B. Cash flows from Investing Activities:			
Purchase of Building	(1,88,000)		
Purchase of Machinery (2)		(1,24,000_	
Purchase of Long-term Investments		(26,000)	
Net Cash used in investing activities		(3,38,000)	(3,38,000)
C. Cash flows from Financing Activities:			
Issue of Share Capital		1,00,000	
Securities Premium		10,000	
Redemption of Debentures		(50,000)	
Payment of interest on Debentures		(20,000)	
Net Cash from financing activities		40,000	40,000
Net increase in Cash and Cash equivalents			18,000
Cash and Cash equivalents at the beginning of The period(3).		32,000	
Cash and Cash equivalents at the end of The period(3).			50,000

Notes: (1)

PROVISION FOR TAX Account

	`		`
To Bank (Balancing fig. being) Payment made)	27,000	By Balance b/d	25,000
		By P&L A/c (Provision	

To Balance c/d	32.000	Made in current year)	34,000
	59,000		59,000

(2)

MACHINERY Account

	`		`
To Balance b/d	3,60,000	ByP&LA/c (Depreciation)	54,000
To Bank (Balancing figure,		By Balance c/d	4,30,000
Being purchase)	1,24,000		
	4,84,000		4,84,000

(3)

Cash and Cash equivalents:

	31st March 2011 `	31st March 2012 `
Cash	37,000	60,000
+Short-term Investments	10,000	8,000
	47,000	68,000
–Bank Overdraft	15,000	18,000
	32,000	50,000

Values involved in Cash flow statement----

- **Scientific and critical ability to analyse the flow of cash**
- **Communicating the material information**
- **Ability to analyse the short term financial security and stability**

- **Transparency**

Every question of Accountancy signifies one or the other value. Business proceeds ahead with certain values which are quantified by Accountancy. Accountancy is just not figures. On one hand it has intrinsic values and on the other there are moral values imbibed into it. Accounting inherits the following values--- (suggestive not exhaustive)

- **Integrity.**
- **Professional competence with due care**
- **Commitment to excellence**
- **Transparency**
- **Objectivity and independence**
- **Confidentiality**
- **Communicating the material information**
- **Analysis, problem solving and critical thinking**
- **Admitting errors and rectifying them**
- **Efficient utilisation of resources**
- **Commitment to pay its liabilities in time**

While learning Accountancy it is observed that the child remains upto a level of figure or intrinsic values only. There is a need that the child also appreciates and learns the moral values associated with these figures, imbibes the same in his day to day life and carries the same to his professional life to become a responsible and committed citizen of INDIA. In the following questions an attempt has been made to bring out these values for the teaching learning community to ponder and practice

Values are the significant and fundamental dimensions of human life and indicate how one adheres, attaches and reacts in life situations or circumstances. They are the blue prints or action plan which orient and decide the thinking, action feelings and behavior itself.

- ***Values does not mean going back to the superstitions but to bring in harmony with the present social and cultural conditions, which are acceptable to the society.***
- *Values Cannot be scientifically investigated or proven*
- ***Values affect how we practice***

CORE VALUES OF A BUSINESS:

- **Accountability**- Responsibility of our actions that influence the lives of our customers and fellow workers.
- **Balance-** Maintaining Healthy life and work balance for workers.
- **Collaboration-**Collaborating within and outside the company to give the best.
- **Commitment-**Commitment to roll great product, service and other initiatives that impact lives both within and outside the organization.
- **Community**- A sense of responsibility and contribution to society that define our existence.
- **Consistency**-Be consistent in offering the best for wonderful experience.
- **Diversity-** Respecting the diversity and giving the best of the composition.
- **Efficiency-** Being efficient and effective in our approach to give best solution each time.
- **Empowerment-** Empowering the employees to take initiative and give the best.
- **Fun-** Having fun and celebrating small successes in our journey to achieve big.
- **Innovation-** To come out with new creative ideas that have the potential to change the world.

- **Integrity-**To act with honesty and integrity without compromising the truth.
- **Leadership-** The courage to lead from front and shape future.
- **Ownership-** Taking ownership of the company and customer success.
- **Passion-**Putting the heart and mind in the work to get the best.
- **Quality-**Giving the best and unmatched results for all round satisfaction.
- **Respect-**Giving due respect to self and others and maintain the environment of team work and growth.
- **Risk Taking-** Encouraging self and others to take risk for a bright future.
- **Safety-** Ensuring the safety of people and making sure to give them trouble free experience.
- **Service Excellence-** Giving the best and world class service and achieving excellence each passing day.

Partnership – Fundamentals

- X, Y and Z are partners with ` 72,000, ` 80,000 and ` 1,00,000 as their capitals respectively. The profit for the year ending March 31, 2012 was ` 7,20,000. Before distributing profits they donated 10% of profits to a 'Non-Govt. organization' as charity for welfare of educationally backward section of the society. Out of the remaining profit, ` 4,00,000 is divisible as 5:3:2 ratio and the remaining is to be divided amongst them equally.

Identify the value involves by the partnership form of X,Y and Z. Prepare Profit and Loss appropriation Account and partner's Capital Account.

- Aakash and Bhola entered into partnership on January 1, 2012 contributing ` 1,20,000 and ` 1,60,000 as capitals respectively. Their partnership firm started the business of manufacturing shoes. They decided to allow a discount of 30% on shoes for school going children. They share profits in the ratio of 7:3. The profits for the year were ` 9,60,000.

  Prepare Profit and Loss Appropriation Account and the partner's Capital Accounts. Also identify the value involved in this question.

- Renu and Reshma shared profits as 7:3. Renu want to give admission to her friend Rehana as a new partner. Reshma agrees with this decision of Renu. Rehana is a physically challenged lady and admitted with a ¼th share in profits. Renu and Reshma gave her a guarantee that her share of profit will never be less than ` 1,20,000 p.a., the profits for the last two years ended March 31, 2011 and March 31, 2012 were ` 1,60,000 and ` 2,40,000 respectively. Identify the human value involved in this case and prepare Profit and Loss Appropriation Account for the two years.

- Ramesh and Gurmeet are two friends belonging to Hindu and Sikh religion respectively. They started a business of wire manufacturing in the form of a partnership firm. They know that the factory of wire manufacturing pollutes the environment. Therefore there are two options available before them. First option is that the factory can be opened in rural area where local residents are poor and illiterate. Second option is that an advanced pollution control plant can be installed in their factory to control the pollution. They decided to choose the second option which involves an additional cost of ` 2, 00,000. To arrange this amount, they admitted their fast friend John as a new partner for equal share in the future profits.

John brought` 2,50,000 as his share of capital. Ramesh and Gurmeet gave him a guarantee that his share of profit will not be less than ` 60,000 p. a. At the end of first year the firm earns a profit of ` 1,50,000.

Mention the value involved in this question. Write the effects of choosing option available before Ramesh and Gurmeet. Prepare the Profit and Loss Appropriation Account for the first year.

- A, B and C are in a partnership. A is appointed for carrying on the business of the firm by the other partners. A has decided to purchase the goods from a firm in which his wife and his son are partners at a double rate then the prevailing market rate without disclosing this fact to others partners of the firm.

  State which values have been violated by A by not disclosing this information to B and C.

- A, B and C are partners in a firm. C used firm’s money to buy shares without disclosing it other partners. Which value C is violating and what will be the treatment of profit earned by C?

- After completing MBA, Arun and Radha want to start a new business but they don’t have sufficient capital. They contacted their common friend Sita, a rich lady with low vision. They decided to form a partnership firm with a capital of Rs.25,00,000 with a ratio of 80% by Sita, 10% each by Arun and Radha respectively. The partnership deed provided as follows:-

    - Interest on capital @12% p.a.

    - Salary to active partners Arun and Radha @ 9,000 p.m.

The firm earned a net profit of 9,66,000 during the year. Sita decided to donate half of her profits to a school for differently abled children.
State which values are being reflected in the above case and also prepare Profit and loss appropriation a/c for the year.

- A and B are partners in a firm having a workmen compensation reserve of 10,00,000. A worker, Rohan died in an accident while working for the firm. The firm paid 500,000 as compensation to his family and offered a job to his wife and also arranged for the education of his son. State which values are being reflected in the above case and also show the treatment of workmen compensation reserve if A and B now decide to change their profit sharing ratio from 3:1 to equal ratio. Workmen compensation reserve will not be shown in the books of new firms.

- A and B are partners in a firm. A manages all business as a representative of firm. For execution of a sales order to a valuable customer A incurred ` 5,000 for delivery in quick time. B is not agreeing to reimburse the above expenses from the firm's accounts. Explain the treatment of above expense and describe which value is violatedby the partners.

- What are the values involved in the formation of a partnership firm?

- What are the values disclosed by a Partnership Deed?

- In the absence of partnership deed, interest on Advances/Loan by a partner is to be paid @ 6% p.a. What value is depicted in this provision of Indian Partnership Act, 1932?

- XYZ Cycles Ltd., a manufacturer of cycles and tri-cycles has decided to donate 100 tri-cycles worth ˆ 3,00,000 to differently abled children in the **CWSN** (Children with special needs) **assessment camp organized by Directorate of Education, Delhi on 3rd December on occasion of "World Disabled Day"**

  State the values that are being reflected in the above case.

A,B and C were partners in a firm. A died in a road accident. A's family has no other source of income. B and C has decided to admit A's son D , a minor, in the partnership firm .. Firm guaranteed that his share in profits will not be less than ˆ 1,00,000 in a year.

State the values that are being reflected in the above case.

ABC Ltd., a manufacturer of very popular liquid soap, has decided to supply its popular product 'Safe Hand Wash' worth ˆ 50,000 to 25 schools in the different areas of the city on the occasion of **'Global Handwash Day' on the 15th October** at free of cost.

State the values that are being reflected in the above case.

Sita and Geeta are working as marketing executive in a MNC dealing in cosmetic products. After working for 5 years in MNC, both of them realized that they should start their own business, but both of them individually don't have sufficient funds for starting the business. Therefore, they have decided to form a partnership firm with equal amount of capital. Both are agreed that they will actively participate in the operation of the business and to share the profits or losses of the business equally. They have decided to appoint Sangeeta, their common friend, as a manager.

State the values that are being reflected in the above case.

- A, B and C are partners in a firm which deals in woolen garments. D who runs a NGO and also a friend of C contacted him for supplying 1,000 woolen jackets for distributing among the students of **EWS (Economical Weaker Section) of the society studying in a school for 'out of school children' run under SSA program**. D requested C to provide the jackets at the lowest possible rate. C discussed the matter with the other partners of the firm and the firm decided to provide required no. of jackets at 'No Profit No Loss' to the NGO of D.

State the values that are being reflected in the above case.

Ram is a graduate in Business Administration. After completing B.B.A., he tried very hard for a job but he didn't get any opportunity to work due to recession in the economy. Then he realized that he should start his own business at the ground floor of his house lying vacant. Since he didn't have sufficient funds to invest in the business, he cannot start the business alone.

Ram contacted one of his friends, Anuj and convinced him to start a business with him in partnership. Anuj decided to invest in the business and to form a partnership with Ram but Anuj wants to get the firm registered.

State the values that are being reflected in the above case.

19.A and B are partners in a firm. A manages all business as a representative of firm. For execution of a sales order a valuable customer A incurred Rs. 5,000 for delivery in quick time. B does not agree to reimburse the above expenses from the firm's accounts. Explain the treatment of above expense and describe which value is violated by the partners.

20.A, B and C are partners in a firm. C used firm's money to buy shares without disclosing it to other partners. Which value C is violating and what will be treatment of profit earned by doing so?

21A and B are partners in a firm having workmen compensation reserve of Rs.10, 00,000. A worker, Rohan, died with an accident. The firm paid his successors Rs.5, 00,000 and gave employment to his wife and arranged for his child education.

Which values are being indicated in the question and what will be the treatment of workmen compensation reserve if A and B decide to change their profit sharing ratio from 3:2 to 2:3

22.A, B and C are partners in a firm having fixed capital of Rs.5lacs, 3lacs and 2lacs respectively. Firm earned profits of Rs.1, 50,000 during the year ending 31^{st} march, 2011. These profits were divided in capital ratio instead of 2:2:1.

Pass adjustment entry for the above and also state which value is being reflected through this question?

Reconstitution of Partnership- Admission of Partner

- Deepa and Shweta are friends and after completion of their study they started a business of readymade Garments by constituting a partnership firm with a profit sharing ratio as 3:2 respectively.

Their partnership firm earns huge profits during few years. **They decided to start a scholarship of ` 10,000 p.a. for meritorious and poor students.** On January 1, 2012 they admit Joney, their manager as a new partner with 1/5$^{th}$ share in future profits. The value of goodwill of the form is ` 3,50,000 and Joney is not able to bring his share of goodwill in cash. Joney belongs to a Religious minority community and isexpert in business management. He contributes ` 50,000 as his capital and old partners want to pass an adjusting entry for the treatment of goodwill.

Identify the value is involved in this question and pass the journal entries on admission of Joney. Also calculate the new profit sharing ratio.

- Amar and Bashir are sharing profits in the ratio of 3:2 respectively. They admit their friend Chandni with one fourth share in the future profits. Chandni belongs to economic weaker section of the society and not able to bring her share of goodwill. Goodwill of the firm is valued at ` 20,000. Chandni contributes ` 30,000 as her share of capital.

Identify the value involved in this question. Give Journal entries in the books of the firm to record the above transactions.

- X and Y were partners in a firm sharing profits in the ratio of 3:2. On March 31, 2012, their Balance Sheet was as follows:

Liabilities	`	Assets	`
Sundry Creditors	1,00,000	Land & Building	2,00,000
Bills Payable	40,000	Machinery	1,60,000
Outstanding Expenses	20,000	Stock	2,00,000
Capital Accounts:		Debtors	80,000

X 3,60,000 Y 1,40,000	5,00,000	Cash	20,000
	6,60,000		6,60,000

On the above date, Z was admitted as a new partner in the firm for ¼ share in the profits on the following terms:

Z will bring ` 2, 40,000 for her capital and ` 40,000 for her share of goodwill. Machinery was to be depreciated by 10% and Land & Building was to be appreciated by ` 60,000. A provision of 5% was to be created for doubtful debts.

Salary outstanding was ` 10,000.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of the new firm.

Which values of life does Revaluation Account signify?

Dissolution of Partnership Firms

- Following is the Balance Sheet of X and Y, who share profits and losses in the ratio of 4:1, as at 31st March, 2011:

Balance Sheet

As on 31st March, 2011

Liabilities	`	Assets	`
Sundry Creditors	8,000	Bank Debtors	20,000

Bank Overdraft	6,000	17,000	
X's Wife Loan	8,000	Less : Provision (2,000)	15,000
Y's Loan	3,000	Stock	15,000
Investment Fluctuation Fund	5,000	Investments	25,000
Capital		Buildings	25,000
X	50,000	Goodwill	10,000
Y	40,000	Profit and Loss A/c	10,000
	------------		---------
	1,20,000		1,20,000

The firm was dissolved on the above date and the following arrangements were decided upon:

(i) Y is authorized to sell the assets of the firm and he will get a fixed amount of ` 2,000 for his work.

(i) X agreed to pay off his wife's loan.

(ii) Debtors of ` 5,000 proved bad.

(iii) Y decided to sale the building for ` 9,000 to his brother. Market value of the building was ˆ 80,000.

(iv) Others assets realized – Investments 20% less; and Goodwill at 60%. (v) One of the creditors for ˆ 5,000 was paid only ˆ 3,000.

(vi) Y took over part of Stock at ` 4,000 (being 20% less that the book valve).

Balance stock realized 50%.

(vii) Realization expenses amounted to ` 2,000.

State which value are being violated in the above question and also prepare Realization A/c.

Company Account- Issue of Shares

- Shiksha India Ltd. issues 1, 00,000 shares of ` 10 each payable ` 5 on application, ` 3 on allotment and ` 2 on first and final call. Public applied for 1, 40,000 shares and the company made the allotment to all the applicants on pro-rata basis.

  Identify the value involves in the decision of company regarding allotment of shares. Pass the journal entries in the books of the company.

- Rehan Ltd. issues 50,000 shares of ` 10 each payable ` 4 on application and ` 6 on allotment. According to the <u>**SEBI**</u> guidelines, a minimum of the net offer should be reserved for small investors. Therefore, out of these 50,000 shares, 50% portion is reserved for retail (small) investors. Issue has been fully subscribed. Identify the value involves in this question and pass the Journal entries in the books of Rehan Ltd.

Company Account- Issue of Debentures

- Board of Directors of Pearl Global Industries Ltd. wants to start a new unit at a remote area of Assam. The new unit can be started in the form of labor intensive with a capital of ` 5 crore or in the form of automatic plant with a capital of ` 30 crore. Directors decided to start this unit in the form of **labor intensive for generation of employment opportunities in remote areas**. Therefore company purchased land for ` 2, 00,00,000 and machinery for ` 3,00,00,000. In consideration of these assets Company issues 13% Debentures at par.

  Identify the values involves in the decision of directors of Pearl Global Ltd. and Journalize the transactions.

- According to the **SEBI** guidelines, Debentures can be secured by a charge on the assets of the company. A 'Debenture Trust Deed' is entered into between the company and the debenture holders. . Identify the values involved in this decision of **SEBI.**

- A Ltd. issued Rs. 10lacs 9% debentures of Rs. 100 each on 1st April, 2008 redeemable in five equal instalments through draw of lots beginning from the year ending 31st march 2011. Assume that Company has transferred sufficient amount to Debenture redemption reserve.

Pass journal entries for redemption of debentures for 1st year and state the value symbolised by redeeming the debentures through draw of lots?

- Creation of Debenture Redemption Reserve by company indicates which value?

- INFRA Developers Ltd. (an infrastructure company) issued 5, 00,000 8% Debentures of Rs.100 each on April 1, 2008 redeemable on April 1, 2012. How much amount of Debenture Redemption Reserve is required before the redemption of debentures?

Which value SEBI wants to promote by having special provision for Infrastructure Company?

- The operating ratio of A ltd. is 55% and that of B Ltd. is 65%. Which company is following the value of efficient utilization of resources and explain your answer?
- Balance sheet of A Ltd. Showed a balance of Rs.25 Lacs as Cash and Cash equivalents while working capital requirement of Rs. 5Lacs on an average. Which value do you think is missing in the financial planning of the company?

Analysis of financial statements

- Prepare Comparative Statement from the following:

	31st March, 2007	31st March, 2008
	`	`
Revenue from Operations	10,00,000	12,50,000
Cost of Goods Sold	5,00,000	6,50,000
Operating Expenses	50,000	60,000

Interest on investments @ Rs.30.000 and taxes payable @ 50%. Identify the values involved in preparation of comparative statement.

(C.B.S.E. 2009)

37.Prepare a comparative income statement of X Ltd., with the help of the following information and identify the value involved in it-

	2011	2012
Revenue from Operations	1, 00,000	2, 00,000
Cost of Goods Sold	60% of Sale	70% of sales
Indirect Expenses	10% of Gross Profit	
Rate of Income Tax	50% of Net Profit before Tax	

38. Following particulars are given to you:

		`
Closing Inventory		2,00,000
Trade Receivables	1,08,000	
Less: Provision for Doubtful Debts	8,000	1,00,000
Cash		30,000
Marketable Securities		20,000
Income Tax paid in Advance		10,000
Share Issue Expenses		15,000
Liability for Current Taxation		20,000
Liability for Future Taxation		30,000
Trade Payables		34,000
Outstanding Salaries		5,000
Bank Overdraft		25,000
Dividends Payable		36,000

Calculate the Liquidity Ratio and Comment on the short-term financial position of the company. Identify the values involved in this question.

39.From the following balance sheets of ABC Ltd., find out cash from operating activities only:

Particulars		31-3-2011	31-3-2012
• **EQUITY AND LIABILITIES**			
Shareholder's Funds:			
Equity Share Capital		30,000	35,000
Reserve and Surplus:	31.3.2011	31.3.2012	
General Reserve	10,000	15,000	
Profit and Loss Balance	(6,000)*	7,000	
	4,000	22,0004,000	22,000
10% Debentures		21,000	25,000
Trade Payables		8,500	12,500
TOTAL		63,500	94,500
• **ASSETS:**			
Machinery		41,000	54,000
Less: Provision for Depreciation		9,000	13,000
		32,000	41,000
Goodwill		10,000	8,000
10% Investments			3,000
8,000			
Inventory		6,000	24,500
Cash and Bank		12,000	13,000

Discount on Debentures	500	
TOTAL	63,500	94,500

*Bracket denotes negative balance.

Additional Information:

Debentures were issued on 31.3.2012.

Investments were made on 31.3.2012.

Identify the value involved in preparation of cash flow statement.

40.From the following Balance Sheets of Surya Roshni Ltd., as on 31st March 2011 and 2012, prepare a statement of cash flow:

Particulars	**2011**	**2012**
• **EQUITY AND LIABILITIES** `		`
Equity Share Capital	3,00,000	4,00,000
Preference Share Capital	1,00,000	75,000
Securities Premium 60,000		—
Profit & Loss Balance	10,000	72,000
15% Debentures	2,00,000	2,50,000
Trade Payables	50,000	1,10,000
TOTAL	6,40,000	9,67,000
• **ASSETS:**		
Fixed Assets	2,00,000	5,00,000
Less: Accumulated Depreciation	30,000	48,000

			1,70,000	4,52,000
Non-Current Investments			40,000	45,000
Inventory			1,50,000	2,00,000
	2011	2012		
Trade Receivables	1,76,000	56,000		
Less: Provision for				
Doubtful Debts	10,000	16,000		
	1,66,000	40,000	1,66,000	40,000
Bank			94,000	2,14,000
Discount on Issue of Debentures			20,000	16,000
	TOTAL		6,40,000	9,67,000

Additional Information:

- Dividend paid during the year ` 36,000.
- Investment costing ` 10,000 were sold at a profit of 40%.
- Fixed Assets Costing ` 20,000 (accumulated depreciation ` 8,000) were sold for ` 17,000.

Additional debentures amounting to ` 50,000 were issued at par on 1st August 2011. Interest on debentures has been paid regularly.Mention the values involved in it.

41Jamshedji Tata conceived an idea of formation of company in 1908 when East India Company was ruling Indian market . He selected hilly region bordering three states Jharkhand(then part of Bihar) ,Orissa and West Bengal All states were thickly populated and poor .Area he chose was rich in Iron ore so he decided to develop Iron and Steel Industry . He wanted to tap unproductive savings of public and Issued capital of

Rs. 5,00,000. Area was undeveloped so he decided to spend 10% of profits every year for providing Infrastructure to employees. To begin with he provided them accommodation and later he spent amount for schools, hospitals, development of playground and gardens and also contributed in road construction. He also built temples, mosques and churches. Employees were satisfied and worked hard as a result profit grew substantially 20% every year and more Industries were floated by him .Which values lead him to this road of success.(Any FIVE)

42 Cadbury India Ltd. A chocolate company launched a factory in Baddi a small town of Himachal Pradesh .The workers who enter in factory have to wash their hands with sanitizer and wear overcoat, cap and shoes which are sterilized every day for which company spends Rs. 3,00,000 per month . All employees working in factory wear gloves and not allowed to touch directly either raw material or final product .

All employees irrespective of post have to take food in mess at the same place and same food for this company spends Rs.4,00,000 per month .Which values are taken care of ?

(Last two questions can be utilised in Business Studies also)

<u>Answers/Solutions</u>

1. Value involved: (i) Socials Responsibility

(ii) Help to weaker section of the society

Profit and Loss Appropriation Account
For the year ended on March 31,2012

Particulars	`	Particulars	`
To charity to N.G.O.	72,000	By Net Profit	7,20,000
To profit Distributed			
X 1,50,000 + 1,16,000 = 2,66,000			
Y 90,000 + 1,16,000 = 2,06,000	6,48,000		
	7,20,000		7,20,000
Z 60,000 + 1,16,000 = 1,76,000			

Partner's Capital Account

Date	Particulars	X	Y	Z	Date	Particulars	X	Y	Z
2012 Mar.31	To balance c/d	3,38,000	2,86,000	2,76,000	2011 Apr. 1	by balance b/d	72,000	80,000	1,00,000
					2012 Mar.31	By P/L Appropriation	2,66,000	2,06,000	1,76,000
		3,38,000	2,86,000	2,76,000			3,38,000	2,86,000	2,76,000

2.Values : (i) Motivation to school going children

(ii) Help to increase the literacy rate.

Profit and Loss Appropriation Account

For the year ended on March 31,2012

Particulars	`	Particulars	`
To profit Distributed Aakash 6,72,000 Bhola 2,88,000	9,60,000	By Net Profit	9,60,000
	9,60,000		9,60,000

Partner's Capital Account

Date	Particulars	Aakash	Bhola	Date	Particulars	Aakash	Bhola
2012 Dec. 31	To Balance c/d	7,92,000	4,48,000	2012 Jan.1	By Bank	1,20,000	1,60,000
				Dec. 31	By P&L Appropriation A/c	6,72,000	2,88,000
		7,92,000	4,48,000			7,92,000	4,48,000

3. Value involved:

(i) Good relations between persons of different religions.

(ii) Women empowerment

(iii) Welfare of differently abled persons.

(iv) Protection of the interest of differently abled

(v) National integration

Profit & Loss Appropriation Account

For the year ended on March 31, 2011

Particulars	`	Particulars	`
To profit distributed Renu 84,000-56,000 = 24,000 Reshma 36,000-24,000= 12,000 Rehana 40,000+80,000 = 1,20,000	1,60,000 1,60,000	By Net Profit	1,60,000 1,60,000

Profit & Loss Appropriation Account

For the year ended on March 31, 2012

Particulars	`	Particulars	`
To profit distributed Renu 1,26,000-42,000= 24,000 Reshma 54,000-18,000= 36,000 Rehana 60,000+60,000 = 1,20,000	2,40,000 2,40,000	By Net Profit	2,40,000 2,40,000

4. Value involved:

(i) Good relations between different religions

(ii) National integration

(iii) Development of minorities

(iv) Awareness about pollution control

(v) Use of advanced technology

Profit & Loss Appropriation Account

For the year ended on _ _ _ _ _ _ _ _ _ _

Particulars	`	Particulars	`
To profit distributed Ramesh 50,000-5,000 = 45,000 Gurmeet 50,000-5,000 = 45,000 John 50,000+10,000 = <u>60,000</u>	1,50,000	By Net Profit	1,50,000
	1,50,000		1,50,000

5. As A is working on behalf of the other partners, it is his moral duty to work for the benefit of the firm and not to earn any undisclosed profits. By ignoring the interests of the firm and favoring his wife and son, A has violated the following values:

- Honesty
- Integrity

- Truth
- Breach of mutual trust

6. C has violated the following values:

- Honesty
- Integrity
- Truth
- Breach of mutual trust

C will have to return firm's money alongwith any profits earned.

7. Following values are being reflected :-

- Sensitivity towards differently abled individuals.
- Empowering women entrepreneurship.
- Efficient utilization of surplus funds.
- Mutual trust and co-operation

Profit and Loss Appropriation Account

For the year ending on__________________

Dr.
Cr.

Particulars	**Rs.**	**Particulars**	**Rs.**

To Interest on Capital **Arun 30000** **Radha 30000** **Sita 240000** **To Partner's Salary** **Arun 108000** **Radha 108000** **To Profits transferred to capital A/c of :** **Arun 150000** **Radha 150000** **Sita 150000**	**300000** **216000** **450000** **966000** **------------**	**By Profit and Loss A/c** **(Net Profits transferred from P & L A/c)**	**966000** 966000 ------------

8. Following values are being reflected :-

- Mutual trust and co-operation
- Fulfillment of social responsibility
- Sympathy

JOURNAL

Date	Particulars	L.F.	Debit	Credit Rs.
a	Workmen compensation Reserve A/c Dr.		5,00,000	

	To Rohan's Executor A/c (Being compensation due to Rohan's executor.)			5,00,000
b	Rohan's Executor A/c Dr. To Bank A/c (Being compensation paid to Rohan'sExecutor)		5,00,000	5,00,000
c	Workmen compensation Reserve A/c Dr. To A's Capital A/c To B's Capital A/c (Being workmen's compensation fund distributed among partners in their old ratio.)		5,00,000	3,75,000 1,25,000

9. It is the right of A to get indemnified against the payment which he paid for the firms business. B violated the following values:

- Mutual trust and co-operation
- Integrity
- Truth

- Acknowledgement

10. Values

1. Unity
2. Pooling of Resources
3. Efficient use of resources

11. Values:

1. Transparancy
2. Evidence
3. Awareness

12. Values:

- Financial Security
- Sure Return on capital employed.

13. Following values are being reflected:-

1. By helping the differently abled children to come school, co. is promoting R.T.E.(Right To Education Act)
2. Fulfillment of social responsibility

3. Promoting the rights of differently abled children.

14. Following values are being reflected:-

- Sympathy.
- Protection of rights of a minor.
- Helping the family of deceased partner.

15. Following values are being reflected:-

- Fulfillment of social responsibility.
- Spreading health awareness among children.
- Developing hygienic habits among children.

16. Following values are being reflected:-

- Women entrepreneurship.
- Mutual trust
- Co-operation
- Women empowerment.

17. Following values are being reflected:-

- Upliftment of education of children belonging to EWS

- Promoting RTE by helping student of EWS in their education.
- Mutual trust
- Co-operation.

18. Following values are being reflected:-

- Best use of available resources.
- Decision making.
- Mutual trust
- Co-operation.
- Initiative.
- Awareness of legal environment.

19. It is the right of A to get indemnified against the payment which he paid for the firms business. B violated the following values:

- Mutual trust and co-operation
- Integrity
- Truth
- Acknowledgement

20.C has violated mutual trust/honesty. Firm's money will be refunded to the firm along with profits earned. In case there is any loss through this transaction it will be borne by the partner himself.

21. Journal

Date	Particulars	LF	Dr. Amount	Cr. Amount
	Workmen Compensation Res. a/c Dr.		5,00,000	
	To Claim against Workmen.Compensation.Reserve.			5,00,000
	(Being Compensation allowed to Rohan's successors)			
	Claim against W.C.R. a/c Dr.		5,00,000	
	To Bank a/c			5,00,000
	(Being compensation paid)			
	B's Capital a/c Dr.		1,00,000	
	To A's Capital a/c			1,00,000
	(Being adjustment made due to changes In profit-sharing ratio)			

Working notes:

B’s Gaining ratio = New ratio-old ratio 3/5-2/5 =1/5

A’s Sacrificing ratio = Old ratio-New ratio 3/5-2/5 =1/5

Adjustment for workmen compensation reserve 1/5 of Rs.5,00,000i.e Rs.1,00,000.

Values involved—

1 Gratitute towards employees.

2.Promoting education

3.Concern for family

22. Analytical Table

Particulars Firm A B C

Dr. Cr. Dr. Cr. Dr. Cr. Dr. Cr.

Profit taken back

In capital ratio 150,000 75,000 50,000
25,000

Profits in 2:2:1 150,000 60,000 60,000
30,000

Total 150,000 150,000 75,000 60,000 50,000 60,000
25,000 30,000 --

15,000 Dr. 10,000 Cr.5000 Cr.

Journal

Date	Particulars	LF	Dr. Amount	Cr. Amount
	A's Current a/c Dr.		15,000	
	To B's Current a/c			10,000
	To C's Current a/c			5,000
	(Being adjustment made for the Wrong appropriation of profits)			

Values involved-

1.Admitting mistakes

2.Rectifying one's mistakes

23. Value involves:

(i) Women entrepreneurship

(ii) Women empowerment

(iii) Contribution for welfare of poor students

(iv) Welfare of minorities

(v) National integration

	Deepa	Shweta
	3	2

Share of new partner Joney = 1/5

Remaining share for Deepa and Shweta = 1-1/5 = 4/5

New share of Deepa = 4/5*3/5 = 12/25

New share of Shweta = 4/5*2/5 = 8/25

Share of Joney = 1/5*5/5 = 5/25

New ratio = 12:8:5

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
2012	Bank A/c		1,50,000	
Jan.1	Dr.			1,50,000
	To Joney’s capital A/c			
	(New [partner Joney brings in his			
	share of goodwill)		70,000	
	Joney’s capital A/c			42,000
	Dr.			28,000
	To Deepa’s capital A/c			
	To Shweta’s capital A/c			
	(Adjustment of goodwill on			
	admission of Joney)			

24. Value involved-

(i) Help to economic weaker section of society

(ii) Women empowerment

(iii) National Integration

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
2012 Jan.1	Cash A/c Dr.		30,000	
	To Chandani's capital A/c			30,000
	(New partner Chandani brings in her share of goodwill)			
	Chandani's capital A/c Dr.		5,000	
	To Amar's capital A/c			3,000
	To Bashir's capital A/c			2,000
	(Adjustment of goodwill on admission of Chandani)			

25. Following values are being violated:-

- Mutual trust
- Honesty
- Revaluation account signifies Adaptability according to changes in life.
- Transparancy

Solution:

Revaluation Account

Particulars	`	Particulars	`
To Machinery To Provision for Doubtful Debts To Salary Outstanding To Profit Distributed: X 18,000 Y 12,000	16,000 4,000 10,000 30,000	By Land & Building	60,000
	60,000		60,000

Partners' Capital accounts

Particulars	X	Y	Z	Particulars	X	Y	Z
To Balance c/d	4,02,000	1,68,000	2,40,000	By Balance b/d By Cash By Premium By Revaluation	3,60,000 24,000 18,000	1,40,000 16,000 12,000	2,40,000
	4,02,000	1,68,000	2,40,000		4,02,000	1,68,000	2,40,000

Balance Sheet

Liabilities	`	Assets	`
Sundry Creditors	1,00,000	Land & Building	2,60,000
Bills Payable	40,000	Machinery	1,44,000
Outstanding Expenses	20,000	Stock	2,00,000
Salary Outstanding	10,000	Debtors	
Capital Accounts:		80,000	
X		Less: Provision	76,000
4,02,000		4,000	3,00,000
Y			
1,68,000	8,10,000	Cash	
Z			
2,40,000			
	9,80,000		9,80,000

26.

Dr. **Realization Account** **Cr**

Particulars	`	**Particulars**	`
To Goodwill	10,000	By Investment	
To Buildings	25,000	Fluctuation Fund	5,000
To Investments	25,000	By Provision for	
To Stock	15,000	Doubtful Debts	2,000
To Debtors	17,000	By Creditors	8,000
To X's Capital A/c		By X's Wife Loan	6,000
(X's wife loan)	8,000	By Bank A/c:	8,000
To Bank A/c:		(Assets realized	
(Creditors)		Debtors	

To Y's Capital A/c (Expenses on Realisation)	6,000 2,000 1,08,000 -------------	12,000 Investments 20,000 Goodwill 6,000 Buildings 9,000 Stock 5,000) (10,000*50/100) --------- By Y's Capital A/c (Stock) By Loss transferred to: X's Capital A/c 23,200 Y's Capital A/c 5,800 --------- -	 72,000 4,000 29,000 1,08,000 __________ ------------

Values involved—

1.Mutual understanding

2 Transparancy

27 Values:

(i) Equality

(ii) Equal opportunity to all members of public

Shiksha India Ltd.

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
	Bank A/c		7,00,000	
	Dr.			7,00,000
	To share application A/c			
	(Application money received on			
	1,40,000 shares @ ` 5 each)		7,00,000	
	Share Application A/c			5,00,000
	Dr.			2,00,000
	To share capital A/c			
	To share allotment A/c			
	(Application money transferred to		3,00,000	
	share capital A/c and share			3,00,000
	allotment A/c)			
	Share Allotment A/c			
	Dr.		1,00,000	
	To share capital A/c			1,00,000
	(Allotment money due on			
	1,00,000 shares @ ` 3 each)		2,00,000	
	Bank A/c			2,00,000
	Dr.			
	To Share Allotment A/c			
	(Allotment money received)		2,00,000	
	Share first & final call A/c			2,00,000
	Dr.			
	To share capital A/c			
	(first and final call money due on			
	1,00,000 shares @ ` 2 each)			
	Bank A/c			

	Dr. To share first & and final call (first and final call money received)			

28. Values Involves:

(i) protection of interest of small investors

(ii) Promoting the habit of saving in people

(iii) Helpful in capital formation

Rehan Ltd.

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
	bank A/c		2,00,000	
	Dr.			2,00,000
	to Share Application A/c			
	(Application money received on			
	50,000 shares @ ` 4 each)		2,00,000	
	Share application A/c			2,00,000
	Dr.			
	To share capital A/c			
	(Application money transferred to		3,00,000	
	share capital A/c)			3,00,000
	Share Allotment A/c			
	Dr.			
	To Share capital A/c		3,00,000	
	(Allotment money due on 50,000			3,00,000

	shares @ ` 6 each) Bank A/c Dr. To Share Allotment A/c (Allotment money received)			

29. Value involved:

(i) Generation of employment opportunities

(ii) Balanced regional development

Journal

Date	Particulars	L.F.	Dr.(`)	Cr.(`)
	Land A/c Dr.		2,00,000	
	Machinery Dr.		3,00,000	
	To Vendor			5,00,000
	(Assets purchased)			
	Vendor Dr.		5,00,000	
	To 13% Debentures			5,00,000
	(5,00,000 13% Debentures of ` 100 each issued at par)			

30. Value Involved

(i) Protection of interest of debenture holders.

31Journal

Date Particulars LF Dr. Amount Cr. Amount

2011				
March 31	9% Debentures a/c	Dr.	100,000	
	To Debenture holders			100,000
	(Being payment due to Debenture Holders on redemption)			

March 31	Debenture holders a/c	Dr.	100,000	
	To Bank a/c			100,000
	(Being payment made)			

By redeeming Debentures through draw of lots, Company is showing the following values:-

- Equal opportunity to every Debenture holder in redemption of Debentures.
- Judicious and rational decision making by the company to pay its debts in installments.

32 It indicates about the value of foresightedness and judiciously paying the liability in phased manner by the company.

33.No Debenture Redemption Reserve is to be created since SEBI has exempted infrastructure companies.

SEBI wants to promote National Development by exempting infrastructure companies so that it may utilise its funds in timely completion of the projects.

34.A Ltd. is using the value of efficient utilization of resources because operating ratio shows the percentage of sales that is absorbed by the cost of sales and operating expenses. A lower operating ratio is always better.

35 The company is violating the value of "Efficient utilization of resources". It should utilize the funds productively so that it can earn extra income.

36 Values: Estimation with due care

Analytical ability

Comparative income statement

for the year ended March 31, 2007 and March 31, 2008

Particulars	31-3-2007	31-3-2008	Absolute Increase or Decrease	% Increase or Decrease
	`	`	`	%
Revenue from Operations	10,00,000	12,50,000	+2,50,000	+ 25.00
Less: Cost of Goods sold	5,00,000	6,50,000	+ 1,50,000	+ 30.00
Gross Profit	5,00,00	6,00,000	+ 1,00,000	+ 20.00

Less: Operating Expenses	50,000	60,000	+ 10,000	+ 20.00
Operating Profit	4,50,000	5,40,000	+ 90,000	+ 20.00
Add: Other Income	30,000	30,000		
N.P. before Tax	4,80,000	5,70,000	+90,000	+ 18.75
Less: Income Tax @ 50%	2,40,000	2,85,000	+ 45,000	+ 18.75
N.P. After Tax	2,40,000	2,85,000	+45,000	+18.75

37

Values: Estimation.

Analytical ability

Comparative Income Statement

Particulars	2011	2012	Absolute Change	%Change
	`	`	`	
Revenue from Operations	1,00,000	2,00,000	1,00,000	100.00
Less: Cost of Goods Sold	60,000	1,40,000	80,000	133,33
Gross Profit	40,000	60,000	20,000	50.00
Less: Indirect Expenses	4,000	6,000	2,000	50.00
Net Profit before Tax	36,000	54,000	18,000	50.00
Less: Income Tax	18,000	27,000	9,000	50.00
Net Profit after Tax	18,000	27,000	9,000	50.00

38

Values: Decision Making andForesightedness**.**

Liquidity Ratios include the following two ratios:

- Current Ratio, and (b) Quick Ratio
- Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liabilities}}$

Current Assets = Closing Inventory + Trade Receivables + Cash + Marketable Securities + Income Tax Paid in Advance

= ` 2,00,000 + ` 1,00,000 + ` 30,000 + ` 20,000 + `10,000

= `3,60,000

Current Liabilities = Taxation (Current) + Trade Payables + Outstanding Salaries + Bank Overdraft + Dividents Payable

= `20,000 + `34,000 + `5,000 + `25,000 + `36,000

= `1,20,000

Current Ratio = $\frac{3,60,000}{1,20,000} = 3:1$

- Quick Ratio = $\frac{\text{Liquid Assets}}{\text{Current Liabilities}}$

Liquid Assets = Trade Receivables + Cash + Marketable Securities

= `1,00,000 + `30,000 + `20,000

= `1,50,000

Quick Ratio = $\frac{1,50,000}{1,20,000} = 1.25:1$

Comments: The short-term financial position of the company is sound because its current ratio is 3 : 1, which is more than the ideal ratio of 2 : 1. Liquid ratio o the company is 1.25 : 1, which is also more than the ideal ratio of 1 : 1. Therefore, it can be said that the company is in a position to pay its current liabilities instantly.

Cash Flow Statement

39

Values Involves: Analytical thinking

CALCULATION OF CASH FROM OPERATING ACTIVITIES

(Indirect Method)

	`	`
Net Profit before taxation:		
Profit during the year (See Note 1) 13,000		18,000
Add: Transfer to General Reserve 5,000		
Adjustments for:		
Interest on Debentures (10% on `21,000)	2,100	
Depreciation (`13,000 – `9,000)	4,000	
Goodwill written off	2,000	
Discount on Debentures written off	500	8,600
		26,600
Less: Interest on Investments		300
Operating profit before working capital changes		26,300
Add: Increase in Current Liabilities:		
Trade Payables		4,000
		30,300

Less: Increase in Current Assets:	
Inventory	18,500
Net Cash from Operating Activities	11,800

Note 1: Negative balance of Profit & Loss amounting to ` 6,000 appearing in the balance sheet on 31.3.2011 represents an amount of loss. In the current year, after covering this loss of ` 6,000 the Profit & Loss shows a profit of ` 7,000. It means that net profit during the current year must have been ` 7,000 + ` 6,000 = ` 13,000.

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CASH FLOW STATEMENT

(Indirect Method)

		`	`
• **Cash flows from Operating Activities:**			
Net profit before taxation:			
Profit during the year (1)	82,000		
+Dividend paid	36,000	1,18,000	
Adjustments for:			
Depreciation on fixed assets(3)		26,000	
Provision for doubtful debts		6,000	
Discount on issue written off		4,000	
Interest Paid		35,000	
		1,89,000	
Less: Profit on sale of investments	4,000		
Profit on sale of fixed assets	5,000	9,000	
Operating profit before working		1,80,000	

capital change			
Add: Decrease in Current Assets:			
Trade Receivables	1,20,000		
Increase in Current Liabilities:			
Trade Payables	60,000	1,80,000	
		3,60,000	
Less: Increase in Current Assets:			
Inventory		50,000	
Net cash from operating activities		3,10,000	3,10,000
• **Cash flows from Investing Activities:**			
Purchase of Fixed Assets (2)		(3,20,000)	
Sale of Fixed Assets		17,000	
Purchase of Investments (4)		(15,000)	
Sale of Investments		14,000	
Net cash used in investing activities		(3,04,000)	(3,04,000)
• **Cash flows from financing activities:**			
Issue of Equity Shares		1,00,000	
Premium received on issue of shares		60,000	
Issue of Debentures		50,000	
Redemption (Repayment) of Preference Shares		(25,000)	
Dividend paid		(36,000)	
Interest paid		(35,000)	
Net cash from financing activities		1,14,000	1,14,000
Net increase in cash and cash equivalents			1,20,000
Cash and cash equivalents at the beginning of the period			94,000

Cash and cash equivalents at the end of the Period	2,14,000

Note: 1. Negative balance of Profit & Loss amounting to ` 10,000 appearing in the Balance Sheet on 31st March, 2011 represent an amount of loss. In the current year, after covering this loss of ` 10,000, the Profit ~ Loss shows a profit of ` 72,000. It means that net profit during the current year must have been ` 72,000 + ` 10,000 = ` 82,000.

2.

FIXED ASSETS A/C (On Original Cost)

	`		`
To Balance b/d	2,000	By Bank (sale)	17,000
To P & L A/c (Being Profit on the sale of fixed Assets)	5,000	By Accumulated Dep. A/c (Being depreciation on fixed assets sold)	8,000
To Bank A/c (Balancing Fig. being purchases)	3,20,000	By Balance c/d	5,00,000
	5,25,000		5,25,000

3.

ACCUMULATED DEPRECIATION A/C

`		`	
To Fixed Assets A/c (being the transfer of Depreciation on fixed Assets sold)	8,000	By Balance b/d	30,000
TO Balance c/d	48,000	By P & L A/c (Balancing figure, being current year's depreciation	26,000

	56,000		56,000

4.

INVESTMENTS A/C

	`		`
To Balance b/d	40,000	By Bank A/c	
To P&L A/c (Profit		(Sale proceeds)	14,000
On sale of			
Investments)	4,000	By Balance c/d	45,000
To Bank A/c (Balancing			
Fig.-being purchases)	15,000		
	59,000		59,000

Value –Analytical ability

Ability to judge the flow of cash

41.Because of following values he proved to be successful

- Courage – he was first Indian to start industry during British period
- entrepreneurship
- social issues---sensitivity towards education

sensitivity towards environment

- respect for all religions
- unity as people of all three states worked together happily
- channelizing saving leading to capital formation
- rural development
- motivation of employees
- best utilization of resources
- nation building

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- Equality all employees treated equally
- Health consciousness—use of sanitizer and sterilised clothes
- Balanced regional development
- Employment to people of hills raising their standard of living

HOTS (HIGHER ORDER THINKING SKILLS)

Not-for-profit Organisation and Partnership Accounts

Chapter 1
Accounting for Not-for- Profit Organisation

1. " A non profit organisation follows hybrid system of accounting". Do you agree with this.

Yes. A non profit organisation follow the combination of cash and accrual system ie, hybrid system.

2. "Receipts and Payments Account is similar to a cash book". Do you agree? Comment.

Yes, it is similar to a cash book and hence it serves the purpose of a cash book. All cash transactions, whether revenue or capital in nature are accounted for. This accounts begins with opening balance of cash and gives the cash balance at the end of the period.

3. From the following particulars calculate the total amount of subscription to be credited to Income and Expenditure account for the year 2002.

		Rs.
Subscription received during 2002	-	5,000
Subscription outstanding in 2001	-	200
Subscription outstanding in 2002	-	500
Subscription received in advance in 2001	-	400
Subscription received in advance in 2002	-	300

Soln:

Dr. Subscription Account Cr.

Particulars	Amount	Particulars	Amount
To Subscription outstanding in 2001	200	By Cash	5,000
To Subscription received in advance in 2002	300	By Subscription outstanding in 2002	500
To Subscription transferred to Income & Expenditure a/c	5,400	By Subscription received in advance in 2001	400
	5,900		5,900

4. From the following particulars, prepare a subscription account for the year 2001, total subscription received during the year 2001 is Rs. 10,000 (including Rs. 600 for the year 2,000 and Rs. 400 for the year 2002). Subscription received in advance in the year 2000 for the year 2001 was amounted to Rs. 500. Subscriptions outstanding during the year 2001 is Rs. 550.

Soln:

Dr. Subscription Account Cr.

Particulars	Amount	Particulars	Amount
		By Subscription received during the year 10000 **Less** Subscription for the year 2000 600 9400 **Less** Subscription for the year 2002 400	9,000
To Subscription transferred to Income & Expenditure a/c	10,050	By Subscription received in advance	500
		By Subscription outstanding during the year 2001	550
	10,050		10,050

5. From the following particulars of General Club, prepare a salary account for the year ending 31st March 2003.

		Rs.
Salary paid during the accounting year	-	11,500
Salary outstanding on 01.04.2002	-	700
Salary paid in advance on 01.04.2002	-	550
Salary outstanding on 31.03.2003	-	850
Salary paid in advance on 31.03.2003	-	250

Soln:

Dr. Salary Account Cr.

Particulars	Amount	Particulars	Amount
To Cash	11,500	By Salary outstanding on 2002	700
To Salary paid in advance on 2002	550	By Salary paid in advance on 2003	250
To Salary outstanding on 2003	850	By Salary transferred to Income & Expenditure a/c	11,950
	12,900		12,900

6. The following particulars are extracted from the books of National Club. Locker rent received during the year 2001 amounted to Rs. 2,400. Rent outstanding on 01.01.2001 was Rs. 300 and that on 31.12.2001 was Rs. 150. Rent received in advance for the year 2002 was Rs. 250. You are required to prepare Locker Rent Account, for the year ending 31st December 2001.

Soln:

Dr. **Locker Rent Account** Cr.

Particulars	Amount	Particulars	Amount
To Rent outstanding on 2000	300	By Cash	2,400
To Rent received in advance for the year 2002	250	By Rent outstanding on 2001	150
To Locker rent transferred to Income & Expenditure a/c	2,000		
	2,550		2,550

7. Calculate from the following particulars, the amount of stationery to be debited to Income and Expenditure Account.

		Rs.
Cash purchases of stationery during the year	-	2,100
Due for stationery on closing date	-	180
Stock of stationery on opening date	-	210
Stock of stationery on closing date	-	130

Soln:

		Rs.
Cash purchases of stationery during the year	-	2,100
Add Due for stationery on closing date	-	180
		2,280
Add Stock of stationery on opening date	-	210
		2,490
Less Stock of stationery on closing date	-	130
Amount of stationery debited to Income & Expenditure Account	-	2,360

Chapter 2
Partnership - Basic Concepts

1 Aby and Anu are partners sharing profits in the ratio of 4:1. Their capital a/c balances are

Aby : 4,00,000, Anu : 5,00,000

Profit made during the year was Rs. 1,00,000.

Anu is of the opinion that their agreement must include a provision for interest on capital @10% p.a. otherwise the profit sharing ratio must be made equal. Why did Anu put forward such an opinion? Will it be worthwhile to her if such changes are made. Which of the above conditions is more advantageous to her? Give your advice?

Ans: (a) If interest on capital charged @10% p.a.

Profit of the firm = 1,00,000

Less Interest on capital

Aby $400000 \times \frac{10}{100} = 40{,}000$

Anu $500000 \times \frac{10}{100} = 50{,}000$ 90,000

Balance of profit 10,000

Share of profit of Anu = $10000 \times \frac{1}{5}$ 2,000

Total increase in the capital of Anu

= Share of profit + Interest on capital

= 2000 + 50000 = 52,000

(b) If profit sharing ratio is equal

Profit of the firm = Rs. 1,00,000

Share of profit of Anu = $100000 \times \frac{1}{2}$ = Rs. 50,000

Before taking the above two conditions, Anu will get only $\frac{1}{5}$ of total profit ie, $100000 \times \frac{1}{5}$ = Rs. 20,000.

But in the Ist case she will get Rs. 52,000 and in the 2nd case she will get Rs. 50,000. So the 1st case, ie interest on capital charged @10% p.a is more advantages to her.

2. Sanu and Manu are in partnership, who have not made any written agreement. Sanu has given a loan of Rs. 12,000 to the firm in addition to his capital contribution. During the year the firm made a net loss of Rs. 40,000.
Regarding the interest on loan, Manu is of the opinion that no interest be paid being the loan was not external one. Is Mr. Manu right in his stand? State your views.

Ans: In the absence of any provision regarding the rate of interest on loan in the Partnership Deed, relevant provision in respect of interest on loan is applicable to all partnership firm as laid down in the Indian Partnership Act of 1932. As per this rule, firm should give 6% interest p.a. to Sanu's loan.

3. **After closing the books of accounts, it was discovered that an item, interest on capital was omitted to be recorded in the books of accounts. Even then, there was no difference in the closing balance of capital account, before and after the treatment of the item. What do you infer from this?**

   Ans: If the partners share of capital and their profit sharing ratio remains same, there was no difference in the closing balance of capital account, before and after the treatment of interest on capital.

4. **"Partnership deed must be in writing". Do you agree with the statement? Give reasons in favour of having partnership deed in writing?**

   The Partnership Act doesnot make it obligatory that agreement should be in writing. However, it is always advisable to put the partnership agreement in writing. An oral agreement may cause disputes in future. A written agreement helps

   (a) To maintain peaceful atmosphere and run business smoothly

   (b) To avoid future disputes, quarrels, and misunderstanding among the partners

   (c) To remind the partners about their rights, duties and liabilities and

   (d) To avoid contradictions.

5. **Paul, Kumar and Lakshman are partners in a firm, sharing profit and losses in the ratio of 3:2:1. After the preparation of final accounts, it was discovered that interest on drawings had not been taken into consideration. The interest on drawings of partners amounted to Rs. 600, Rs. 400 and Rs. 200. Give necessary adjustment journal entry**

   Ans: Journal entry

Paul's capital a/c	Dr.	600	
Kumar's capital a/c	Dr.	400	
Lakshman's capital a/c	Dr.	200	
Profit and Loss Adjustment a/c			1,200

6. **The partner's capital account prepared by Mr. Jose, an accountant in Gokul and Co, where Mr. Lakshman and Mrs. Seetha are partners, is given below. Rectify the errors, if any in the capital accounts prepared by him and show the partners capital accounts under fixed capital method. What should have been the profit of the firm as per profit and loss account?**

Partners' capital a/c

Particulars	Lakshman	Seetha	Particulars	Lakshman	Seetha
Salary	1,000	2,000	Balance b/d	10,000	15,000
Interest			Drawings	5,000	12,000
on capital	2,000	3,000	Commission	----	2,000
Profit and loss			Interest on		
Appropriation a/c	7,000	3,000	drawings	250	600
Balance c/d	5,250	21,600			
	15,250	29,600		15,250	29,600

Soln:

Partners' capital a/c

Particulars	Lakshman	Seetha	Particulars	Lakshman	Seetha
To Drawings	5,000	12,000	By Balance b/d	10,000	15,000
To Interest on			By Salary	1,000	2,000
drawings	250	600	By Interest on		
			capital	2,000	3,000
			By Commission	----	2,000
To Balance c/d	14,750	12,400	By P&L		
			Appropriation a/c	7,000	3,000
	20,000	25,000		20,000	25,000

Profit & Loss Appropriation a/c

Particulars		Amount	Particulars		Amount
To Salary			By Profit as per P & L a/c		19,150
Lakshman	1000		(Balancing figure)		
Seetha	2000	3,000	By Interest on drawings		
To Interest on capital			Lakshman	250	
Lakshman	2000		Seetha	600	850
Seetha	3000	5,000			
To Commission - Seetha			2,000		
To Balance of profit					
Lakshman	7000				
Seetha	3000	10,000			
		20,000			20,000

Preparation of capital a/c as per Fixed capital method

Capital a/c

Particulars	Laksh-man	Seetha	Particulars	Laksh-man	Seetha
			By Balance b/d	10,000	15,000
To Balance c/d	10,000	15,000			
	10,000	15,000		10,000	15,000

Current a/c

Particulars	Laksh-man	Seetha	Particulars	Laksh-man	Seetha
To Drawings	5,000	12,000	By Salary	1,000	2,000
To Interest on drawings	250	600	By Interest on capital	2,000	3,000
			By Commission	----	2,000
			By P & L Appropriation	7,000	3,000
To Balance c/d	4,750		By Balance c/d	----	2,600
	10,000	12,600		10,000	12,600

Chapter 3
Admission of a Partner

1. **On 01.01.2005 Ravi and Mathew started partnership with the following, in the ratio of 2 : 1 which is there profits sharing ratio too.**

   Fixed Assets Rs. 3,00,000; Current assets Rs. 3,80,000 Current liabilities Rs. 80,000

   During the year they made a profit of Rs. 90,000 and drawings of Rs. 15,000 each for which they have passed the following entries.

(i) Cash a/c	Dr.	90,000	
Profit and loss a/c			90,000
(ii) Ravi's capital a/c	Dr.	15,000	
Mathew's capital a/c	Dr.	15,000	
Cash a/c			30,000

   On 01.01.06, they admitted Jameel into partnership with a capital contribution of Rs. 1,60,000 and Rs. 30,000 towards his share of goodwill. On this date, they have valued the assets and liabilities as follows. Fixed assets Rs. 2,10,000; Current assets Rs. 4,20,000 Current liabilities Rs. 70,000. There was a liability on account of bills discounted Rs. 20,000

   Prepare: (a) Capital accounts (b) Revaluation accounts (c) Balance sheet of the new firm

Ans: Calculation of opening capital

Capital = Assets – Liabilities

= 300000 + 380000 – 80000 = 6,00,000

Share of Ravi = $600000 \times \frac{2}{3} = 4,00,000$

Share of Mathew = $600000 \times \frac{1}{3} = 2,00,000$

Calculation of sacrificing ratio

Sacrificing ratio = Old ratio – New ratio

Old ratio of Ravi & Mathew = 2 : 1

New ratio of Ravi, Mathew & Jameel = 1 : 1 : 1

Sacrificing ratio of Ravi = $\frac{2}{3} - \frac{1}{3} = \frac{1}{3}$

Sacrificing ratio of Mathew = $\frac{1}{3} - \frac{1}{3} = 0$

$\therefore$ Full goodwill should be credited to Ravi's capital a/c

Revaluation a/c

Particulars	Amount	Particulars	Amount
Fixed assets	90,000	Current assets	40,000
Liabilities on bills discounted	20,000	Current liability	10,000
		Capital	
		Ravi: $60000 \times \frac{2}{3}$	40,000
		Mathew $60000 \times \frac{1}{3}$	20,000
	1,10,000		1,10,000

Dr. **Partners' Capital Accounts** Cr.

Particulars	Ravi	Mathew	Jameel	Particulars	Ravi	Mathew	Jameel
Drawings	15,000	15,000		Balance b/d	400,000	200,000	
Revaluation	40,000	20,000		Cash			1,60,000
Balance c/d	4,35,000	1,95,000	1,60,000	P & L a/c	60,000	30,000	
				Goodwill	30,000		
	4,90,000	2,30,000	1,60,000		4,90,000	2,30,000	1,60,000

Cash a/c

Particulars	Amount	Particulars	Amount
P & L a/c	90,000	Ravi's capital a/c	15,000
Jameel capital	1,60,000	Mathew's capital	15,000
Goodwill	30,000	Balance c/d	2,50,000
	2,80,000		2,80,000

Balance sheet of Ravi, Mathew & Jameel

Liabilities	Amount	Assets	Amount
Capitals:		Fixed asset	2,10,000
Ravi	4,35,000	Current asset	4,20,000
Mathew	1,95,000	Cash	2,50,000
Jameel	1,60,000		
Current liability	70,000		
Liability on bill discounted	20,000		
	8,80,000		8,80,000

2. Mr. Farook and Vinod decide to admit Mr. Karthik as a new partner in their firm. He is required to bring Rs. 10,000 as capital and Rs. 2,000 towards goodwill. What rights can a new partner acquire by contributing towards capital and goodwill?

(i) Right to share the profits of the firm

(ii) Right in the assets of the firm

3. Haridas and Sudheer Raj are partners in a firm sharing profits in the ratio of 3 : 2. On 01.04.2004, they admit Ramdas into the firm for a 5th share in profits. Ramdas contributed the following in respect of his capital and goodwill.

Stock Rs. 10,000 Furniture Rs. 20,000

Plant Rs. 30,000 Building Rs. 40,000

Goodwill has been valued at 2 year's purchase of super profit of past 3 years.

01-04-2002 Profit Rs. 18,000

01-04-2003 Profit Rs. 25,000

01-04-2004 Profit Rs. 32,000

Capital employed is Rs. 2,00,000 and normal rate of return is 10%.

Give journal entries in respect of:

(a) Capital contributed by Ramdas

(b) Goodwill brought in by him

Goodwill = Super profit × No. of years of purchase

Super profit = Average profit – Normal profit

$$\text{Average profit} = \frac{\text{Total profit}}{\text{No.of years}} = \frac{18000 + 25000 + 32000}{3}$$

$$= \frac{75000}{3} = \text{Rs. } 25{,}000$$

$$\text{Normal profit} = \text{Capital employed} \times \frac{\text{Rate}}{100}$$

$$= 200000 \times \frac{10}{100} = \text{Rs. } 20{,}000$$

Super profit = 25000 – 20000 = 5,000

Goodwill = 5000 × 2 = 10,000

$$\text{Share of Ramdas} = 10000 \times \frac{1}{5} = \text{Rs. } 2000$$

Calculation of sacrificing ratio

Sacrificing ratio = Old ratio – New ratio

Old ratio of Haridas & Sudheer = 3 : 2

Ramdas will get $\frac{1}{5}$ share.

$$\therefore \text{Remaining} = 1 - \frac{1}{5} = \frac{4}{5}$$

$$\text{New ratio of Haridas} = \frac{4}{5} \times \frac{3}{5} = \frac{12}{25}$$

$$\text{New ratio of Sudheer} = \frac{4}{5} \times \frac{2}{5} = \frac{8}{25}$$

$$\text{New ratio of Ramdas} = \frac{1}{5} \times \frac{5}{5} = \frac{5}{25}$$

Ratio = 12 : 8 : 5

$$\text{Sacrificing ratio of Haridas} = \frac{3}{5} - \frac{12}{25} = \frac{15-12}{25} = \frac{3}{25}$$

$$\text{Sacrificing ratio of Sudheer} = \frac{2}{5} - \frac{8}{25} = \frac{10-8}{25} = \frac{2}{25}$$

Ratio = 3 : 2

Journal entry

1.	Stock	Dr.	10,000	
	Furniture	Dr.	20,000	
	Plant	Dr.	30,000	
	Building	Dr.	40,000	
	Capital			98,000
	Goodwill			2,000
	(Capital and goodwill brought in)			
2.	Goodwill a/c	Dr.	2,000	
	Haridas			1,200
	Sudheer capital			800
	(Goodwill transferred to old partners capital a/c)			

Chapter 4

Reconstitution of a Partnership Firm

Retirement/Death of a Partner

1. Thomas, Biju and Sunil were partners sharing profits in the ratio of 3:2:1 with a capital balance of Rs. 1,00,000, Rs. 75,000 and Rs. 50,000. They had a joint life policy for Rs. 3,00,000. On 15.10.06 Sunil died. The company admitted for a claim of Rs. 3,60,000 on his death. The firm's profit and loss had a debit balance of Rs. 60,000.

Ascertain: (a) The amount due to Sunil

(b) Pass journal entries regarding the distribution of joint life policy. (c) Prepare capital accounts.

Soln: (a) Amount due to Sunil = Rs. 1,00,000 (See point C)

(b) Journal entry

Joint Life Policy a/c	Dr.	3,60,000	
To Thomas capital a/c			1,80,000
To Biju capital a/c			1,20,000
To Sunil capital a/c			60,000

(c)

Capital a/cs

Particulars	Thomas	Biju	Sunil	Particulars	Thomas	Biju	Sunil
To P & L a/c	30,000	20,000	10,000	By Balance b/d	100,000	75,000	50,000
To Sunil's executors a/c			100,000	By Joint life policy	180,000	120,000	60,000
To Balance c/d	250,000	1,75,000					
	280,000	195000	110,000		280,000	195000	110,000

2. Aby, Suby and Minu are partners sharing profits in the ratio of 5:3:2. Minu retired on 31.09.06. The capital account balance and share of reserve due to Minu together amounted to Rs. 1,80,000. But Aby and Suby agreed to pay him Rs. 2,40,000. The new profit sharing ratio of Aby and Suby have been fixed at 3:2.

(i) Why has Minu been paid over and above the actual amount due to him?

(ii) Give a journal entry to record this through capital a/c adjustments.

Soln: (i) Extra amount paid to Minu = 240000 – 180000

= 60,000

That amount is treated as the share of goodwill to Minu

(ii) Journal entry

Aby's capital a/c	Dr.	30,000	
Suby's capital a/c	Dr.	30,000	
To Minu's capital a/c			60,000

(Share of goodwill transferred in gaining ratio)

(ii) Calculation of Gaining ratio

Gaining ratio = New ratio – Old ratio

New ratio of Aby & Suby = 3 : 2 ie $\frac{3}{5}$ & $\frac{2}{5}$

Old ratio of Aby, Suby & Minu = 5 : 3 : 2

ie $\frac{5}{10}$, $\frac{3}{10}$ & $\frac{2}{10}$

Gaining ratio of Aby = $\frac{3}{5} - \frac{5}{10} = \frac{6-5}{10} = \frac{1}{10}$

Gaining ratio of Suby = $\frac{2}{5} - \frac{3}{10} = \frac{4-3}{10} = \frac{1}{10}$

Gaining ratio = 1 : 1 ie $\frac{1}{2} : \frac{1}{2}$

3. Debee, Sedee and Nedee are in partnership, who were sharing profits in the ratio of 3 : 2:1. On 31.03.05, Nedee left the firm as per agreement. The following details are available.

Balance sheet

Liability	Amount	Asset	Amount
Capital a/cs		Balance with Bank of Baroda	4,000
Debee	30,000		
Sedee	20,000	Loan to Nedee	18,000
Nedee	10,000	Receivables	6,000
General Reserve	18,000	Stock	8,000
		Plant 18,000	
		Building	24,000
	78,000		78,000

(i) Depreciate fixed assets @ 10%

(ii) Only General reserve is to be credited to the extent of Nedee's share through capital adjustment of the partners.

(iii) Receivables are sold to a debt collection agency at Rs. 5,400/-

Nedee's accounts are to be settled soon either by paying off or bringing in necessary cash as the case may be. Prepare the necessary a/c to show the amount due to Nedee.

Revaluation a/c

Particulars	Amount	Particulars		Amount
To Plant	1,800	By Debee capital a/c	2400	
To Building a/c	2,400	Sedee capital a/c	1600	
To Receivable	600	Nedee's capital a/c	800	4,800
	4,800			4,800

Capital a/c of Nedee

Particulars	Amount	Particulars	Amount
To Loan to Nedee	18,000	By Balance b/d	10,000
To Revaluation a/c	800	By General reserve	3,000
		By Cash (Amount to be received)	5,800
	18,800		18,800

4. Following particulars are given to you on 31.03.2006

Particulars	Amount Rs.	Particulars	Amount Rs.
Creditors	9,000	Cash	40,000
Provision for depreciation on plant	1,60,000	Other current asset	22,000
		Plant	1,80,000
General Reserve	9,000		
Capital: Akhil	22,000		
Bikhil	22,000		
Nikkil	20,000		
	2,42,000		2,42,000

On the above date Nikkil retired.

(a) The entire plant was sold for Rs. 12,000

(b) Nikkil's share of goodwill was valued at Rs. 3,000

(c) General reserve to be adjusted to the extend of Nikkil's share through a capital adjustment entry.

(d) Fee receivable has to be taken into a/c Rs. 5,000 which has not been brought into the books so far

Prepare: (a) Revaluation account (b) Capital accounts

(c) Balance sheet

Plant a/c

Particulars	Amount	Particulars	Amount
To Balance b/d	1,80,000	By Provision for depreciation on plant 1,60,000	
		By Cash	12,000
		By Revaluation a/c (loss) (b/f)	8,000
	1,80,000		1,80,000

Revaluation a/c

Particulars	Amount	Particulars	Amount
To Plant a/c	8,000	By Fees receivable	5,000
		By Loss transferred to	
		Akhil capital a/c	
		$3000 \times \frac{1}{3}$ 1000	
		Bikhil capital a/c	
		$3000 \times \frac{1}{3}$ 1000	
		Nikkil capital a/c	
		$3000 \times \frac{1}{3}$ 1000	3,000
	8,000		8,000

(1) Adjusting entry for goodwill

Akhil capital a/c $3000 \times \frac{1}{2}$ 1,500

Bikhil capital a/c $3000 \times \frac{1}{2}$ 1,500

To Nikkil capital a/c 3,000

(ii) Adjusting entry for General Reserve

Akhil's capital a/c $3000 \times \frac{1}{2}$ 1,500

Bikhil's capital a/c $3000 \times \frac{1}{2}$ 1,500

Nikkil's capital a/c $\left(9000 \times \frac{1}{3}\right)$ 3,000

Capital a/c

Particulars	Akhil	Bikhil	Nikkil	Particulars	Akhil	Bikhil	Nikkil
To Revaluation a/c	1,000	1,000	1,000	By Balance b/d	22,000	22,000	20,000
To Nikkil capital a/c	1,500	1,500		By Akhil capital a/c			1,500
To Nikkil capital a/c	1,500	1,500		By Bikhil capital a/c			1,500
To Nikkil loan a/c			25,000	By Akhil capital a/c			1,500
To Balance c/d	18,000	18,000		By Bikhil capital a/c			1,500
	22,000	22,000	26,000		22,000	22,000	26,000

Balance sheet

Liability	Amount	Asset	Amount
Creditors	9,000	Cash	52,000
General Reserve	9,000	(40000 + 12000 (plant sold)	
Capital account:		Other current assets	22,000
Akhil capital	18,000	Fees receivable	5,000
Bikhil capital	18,000		
Nikkil loan a/c	25,000		
	79,000		79,000

5. Heisal, Roy and A. Gomez are in partnership sharing profits in their capital ratio. The Balance sheet on 15th March, 2006 is given below.

Balance sheet

Liability	Amount	Asset	Amount
Reserve fund	18,000	Bank balance with SBI	11,000
Expenses O/s	3,000	Marketable scrips	20,000
Bank O.D. with Bank		Stock	21,000
of Baroda	31,000	Investments (long term)	30,000
Capital account		Furniture	9,000
Heizal	10,000	Land & Building	21,000
Roy	20,000		
A. Gomez	30,000		
	1,12,000		1,12,000

Further information on retirement of Roy on 15th June, 2006

Profit for 3 months - Rs. 9,000

Drawings: Heisal - Rs. 1,000

Roy - Rs. 2,000

A. Gomez - Rs. 3,000

Interest on capital @ 5% p.a

Salary to Roy Rs. 300 p.m.

The firm had a fixed deposit worth Rs. 3,000 which has not accounted so far, has to be brought into the books. Marketable scrips were valued at Rs. 23,000.

Prepare: (a) Profit and loss appropriation a/c

(b) Capital a/c (c) Balance sheet

Soln:

Profit & Loss Appropriation a/c

Particulars		Amount	Particulars	Amount
To Interest on capital			By Balance b/d	9,000
Heisal $10000 \times \frac{5}{100} \times \frac{3}{12}$	125			
Roy $20000 \times \frac{5}{100} \times \frac{3}{12}$	250			
Gomez $30000 \times \frac{5}{100} \times \frac{3}{12}$	375	750		
Salary to Roy 300 × 3		900		
Profit transferred to captial a/c				
Heisal $7350 \times \frac{1}{6}$	1225			
Roy $7350 \times \frac{2}{6}$	2450			
Gomez $7350 \times \frac{3}{6}$	3675	7,350		
		9,000		9,000

Revaluation a/c

Particulars		Amount	Particulars	Amount
Profit transferred to capital a/c			Fixed deposit	3,000
			Marketable scrips	3,000
Heisal 6000 × $\frac{1}{6}$	1000			
Roy 6000 × $\frac{2}{6}$	2000			
Gomez 6000× $\frac{3}{6}$	3000	6,000		
		6,000		6,000

Capital a/cs

Particulars	Heisal	Roy	Gomez	Particulars	Heisal	Roy	Gomez
Drawings	1,000	2,000	3,000	Balance b/d	10,000	20,000	30,000
Roy's loan a/c (B/F)		29,600		Reserve fund	3,000	6,000	9,000
Balance c/d	14,350		43,050	P & L appropriation a/c	1,225	2,450	3,675
				Revaluation a/c	1,000	2,000	3,000
				Interest on capital	125	250	375
				Salary	900		
	15,350	31,600	46,050		15,350	31,600	46,050

Balance sheet

Liability		Amount	Asset	Amount
Expenses outstanding		3,000	Bank balance with SBI	11,000
Bank overdraft		31,000	Marketable scrips	23,000
Capital a/c -			Stock	21,000
Heizal	14,350		Investment 30,000	
Gomez		43,050	Furniture	9,000
Roy's loan a/c		29,600	Land & Building	21,000
			Fixed deposit	3,000
			Profit adjustment a/c (9000 – drawings 6000)	3,000
		1,21,000		1,21,000

6. Abu, Neha and Kiran are equal partners. The ledger accounts as on 31.03.2006 shows the following balances.

Expenses outstanding	Rs. 3,000
Trade credit	Rs. 13,000
Cash	Rs. 2,000
Rent receivable	Rs. 1,000
Accounts receivable	Rs. 13,000
Capital	
Abu - Rs. 30,000	
Neha - Rs. 15,000	
Kiran - Rs. 15,000	
Office equipments	Rs. 50,000
Stock	Rs. 10,000

During the year the firm made a net profit of Rs. 60,000 out of which the following distributions are to be made.

Salary to Abu Rs. 4,000

Commission to Neha Rs. 2,000

Interest on capital @10% each

Kiran retired from the firm on 31.03.2006. Office equipments are revalued at Rs. 60,000 and stock Rs. 9,000.

Prepare:

(a) Profit and Loss appropriation a/c

(b) Revaluation a/c (c) Capital accounts

(d) Balance sheet

Soln:

Profit and Loss Appropriation a/c

Particulars		Amount	Particulars	Amount
Salary - Abu		4,000	By Balance b/d	60,000
Commission - Neha		2,000		
Interest on capital				
Abu 30000 × $\frac{10}{100}$		3,000		
Neha 15000 × $\frac{10}{100}$		1,500		
Kiran 15000 × $\frac{10}{100}$		1,500		
Profit transferred to capital a/c				
Abu 48000 × $\frac{1}{3}$	16000			
Neha 48000 × $\frac{1}{3}$	16000			
Kiran 48000 × $\frac{1}{3}$	16000	48,000		
		60,000		60,000

HOTS (Higher Order Thinking skills)

Revaluation a/c

Particulars	Amount	Particulars	Amount
Stock	1,000	Office equipment	10,000
Profit transferred to capital a/c			
Abu $9000 \times \frac{1}{3}$ 3000			
Neha $9000 \times \frac{1}{3}$ 3000			
Kiran $9000 \times \frac{1}{3}$ 3000	9,000		
	10,000		10,000

Balance sheet

Liability	Amount	Asset	Amount
Expenses outstanding	3,000	Cash	2,000
Trade credit	13,000	Rent receivable	1,000
Capital: Abu	56,000	Accounts receivable	13,000
Neha	37,500	Office equipments	60,000
Kiran's loan a/c	35,500	Stock	9,000
		P & L adjustment	60,000
	1,45,000		1,45,000

Capital a/c

Particulars	Abu	Neha	Kiran	Particulars	Abu	Neha	Kiran
				Balance b/d	30,000	15,000	15,000
				P & L			
				Appropriation a/c	16,000	16,000	16,000
				Revaluation a/c	3,000	3,000	3,000
				Salary			4,000
Kiran's loan a/c			35,500	Commission		2,000	
Balance c/d	56,000	37,500		Interest on capital	3,000	1,500	1,500
	56,000	37,500	35,500		56,000	37,500	35,500

Chapter 5
Dissolution of Partnership Firm

1. You are given the following particulars
   Furniture of book value of Rs. 10,000
   Loss on sale - Rs. 2,000
   If it had been taken over by Anil, a partner what would have been the journal entry on
   (a) Dissolution (b) On reconstitution
   Journal entry
   (a) Anil's capital a/c Dr. 8,000
   Realisation a/c 8,000
   (b) Anil's capital a/c Dr. 8,000
   Revaluation a/c Dr. 2,000
   Furniture a/c 10,000
2. Complete the series
   (a) Sacrificing ratio : admission
   Gaining ratio : ?
   (b) Dissolution : Realisation a/c
   Reconstitution : ?
   (c) Trading a/c : Profit and loss a/c
   Profit & loss a/c : ?
   (d) Balance of capital a/c : Balance sheet
   Balance of profit and loss appropriation a/c:?
   (a) Retirement (b) Revaluation a/c
   (c) Profit and loss appropriation a/c
   (d) Capital accounts
3. Boby, Jestin and Sudheer are in partnership in the ratio of 3:2:3. They have decided to dissolve the firm. On the date of dissolution total creditors were Rs. 16,000; Bills discounted Rs. 2,650 during the year, has become a real liability which has to be paid, though this has not been recorded anywhere in the books of accounts. Their capital account balances were Boby Rs. 12,000; Jestin Rs. 10,000; Sudheer Rs. 8,000 respectively. Boby advance Rs. 14,000 besides his capital account.

Find out: (a) Total Sundry Assets (b) Realisation a/c
(c) Capital accounts of partners

(a) Value of asset

Asset = Capital + Liability

= 12000 + 10000 + 8000 + 14000 + 16000

= Rs. 60,000

Realisation a/c

Particulars	Amount	Particulars	Amount
To Liability on bills discounted	2,650	By Loss transferred to Capital a/c	
		Boby $2650 \times \frac{3}{8}$ 994	
		Jestin $2650 \times \frac{2}{8}$ 662	
		Sudheer $2650 \times \frac{3}{8}$ 994	2,650
	2,650		2,650

Capital a/cs

Particulars	Boby	Jestin	Sudheer	Particulars	Boby	Jestin	Sudheer
To Realisatin	994	662	994	By Balance b/d	12,000	10,000	8,000
				By Loan	14,000		
To Balance c/d	25,006	9,338	7,006				
	26,000	10,000	8,000		26,000	10,000	8,000

4. **Should you pass any entry for the payment of creditors worth Rs. 5,000 on dissolution, if they accept stock of the same value? If yes, what is the journal entry?**

   Ans: No journal entry will be passed as they have accepted stock of same value.

5. **What entry would you pass for the following transactions on the dissolution of a firm having partners Vishal and Rakesh. (i) An unrecorded asset realised Rs. 6,200**

   (ii) Dissolution expenses amounted to Rs. 3,200

   (iii) Creditors already transferred to realisation account were paid Rs. 88,000

   (iv) Stock worth Rs. 5,400 already transferred to realisation account was sold for Rs. 4,100

   (v) Profit on realisation Rs. 48,000 to be distributed between partners, Vishal and Rakesh?

   Passing Journal Entries

   (i) Cash a/c Dr. 6,200
   Realisation a/c 6,200

   (ii) Realisation a/c Dr. 3,200
   Cash 3,200

   (iii) Realisation a/c Dr. 88,000
   Cash 88,000

   (iv) Cash a/c Dr. 4,100
   Realisation a/c 4,100

   (v) Realisation a/c Dr. 48,000
   Vishal capital a/c 24,000
   Rakesh capital a/c 24,000

6. **Richard and Gere, partners of 'Sun Chemicals', decided to dissolve the firm. You are required to pass journal entries for the following transactions at the time of dissolution.**

   (i) Expenses of dissolution amounted to Rs. 500, paid by Mr. Richard.

   (ii) Stock worth Rs. 3,000 which was already transferred to realisation account was taken over by Mr. Richard.

   (iii) Profit on realisation Rs. 6,000 has to be distributed to Mr. Richard and Gere in the ratio 2:1.

   Journal entry

   (i) Realisation a/c Dr. 500
   Richard's capital a/c 500

   (ii) Richard's capital a/c Dr. 3,000
   Realisation a/c 3,000

   (iii) Realisation a/c Dr. 6,000
   Richard's capital a/c 4,000
   Gere's capital a/c 2,000

7. **Toya and Soya are partners sharing profits and losses equally. They decided to dissolve the firm on 15th March, 2005 which resulted in a loss of Rs. 30,000. The capital accounts of Toya and Soya was Rs. 20,000 and Rs. 30,000 respectively. The cash account showed a balance of Rs. 20,000.**

   You are required to pass journal entries for

   (i) Transfer of loss to the capital account of partners

   (ii) Making final payments to the partners.

   (i) Journal entry for transfer of loss
   Toya's capital a/c Dr. 15,000
   Soya's capital a/c Dr. 15,000
   Realisation a/c 30,000

   (ii) Journal entry for final payment of partners
   Toya's capital a/c Dr. 5,000
   Soya's capital a/c Dr. 15,000
   Cash a/c 20,000

Company Accounts and Analysis of Financial Statements

Chapter 1 - Accounting for Share capital

1. Choose the correct answer.

(i) In order to perform obligations under the scheme of buy back of shares, a company is required to open an Escrow account which is created by:
 (a) Deposit of acceptable securities
 (b) Bank guarantee in favour of a merchant bank
 (c) Cash deposited with a commercial bank
 (d) Any of these

(ii) A company can buy back its equity shares from
 (a) Existing equity share holders (b) Open market
 (c) Forfieted share holders (d) Both A & B

(iii) ESOP offered by a company will create/retain
 (a) A sense of belongingness
 (b) High caliber employees
 (c) Higher productivity (d) All of these

2. The memorandum of a company has an authorised capital of Rs. 1,00,00,000 divided into equity shares of Rs. 10/- each. The company intends to make a fresh issue of 1,00,000 shares at a discount of 10%. What is your opinion to the above issue?

3. Make pairs of the following terms regarding company accounts.
 Discount on reissue of forfeited shares, Balance left on reissue in the forfeited shares a/c, capital reserve, share forfeited account.

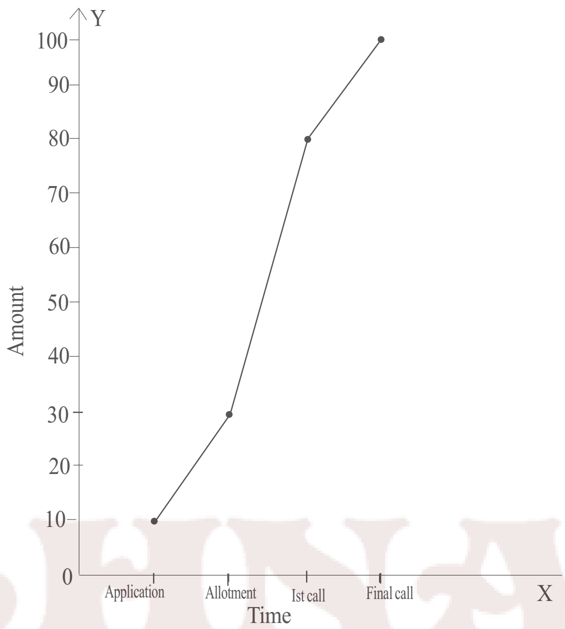
Answers

1. (i) Any of these (ii) Both A & B (iii) All of these
2. The company cannot make fresh issue of shares at a discount
3. Balance left on reissue in the forfeited shares a/c
 - Capital reserve
 Discount on reissue of forfeited shares
 - Shares forfeited a/c

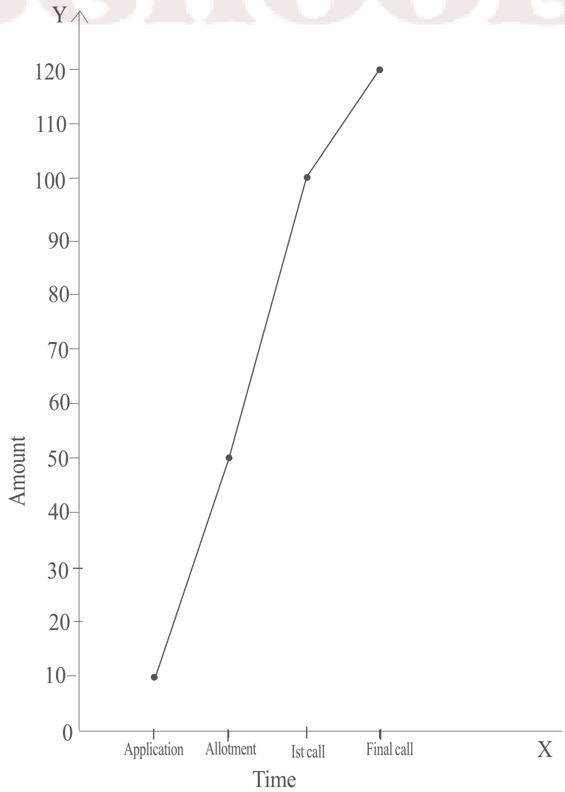
4. A company issues shares with a face value of Rs. 100 each to be collected as per the following schedule.

 1 On application Rs. 10
 2 15 days later - On allotment Rs. 20
 3 1 month later - On 1st call Rs. 50
 4 1 month later - On 2nd call Rs. 20

(a) You are required to prepare a sequential diagram representing time on the X axis and value on the Y axis on step by step approach where cumulated value comes to hundred.



(b) Suppose premium is collected at Rs. 20 per share how will you incorporate it in the diagram.



Chapter 2 - Issue and Redemption of Debentures

1. Sun Ltd. issued 1000 8% debentures of Rs. 1000 each as fully paid to Star Ltd. as consideration for a machinery purchased. Pass necessary journal entries.

Soln:

	Particulars	L.F	Debit Rs.	Credit Rs.
	Machinery a/c Dr. Star Ltd. [The purchase of assets and the purchase price became due]		10,00,000	 10,00,000
	Star Ltd a/c Dr. 8% Debentures a/c [The payment of purchase consideration by issue of debentures]		10,00,000	 10,00,000

2. Analyse the following table and identify the dual aspects of transactions and state your reasons.

Transaction	Accounts involved	A/c debited A/c credited	Narration
(i) Bank loan raised	Bank a/c Bank loan a/c	?	?
(ii) Issue of debentures as collateral security	Method 1 Not recorded in the books		?
	or		
	Method 2 Debenture suspense a/c X% debentures a/c	?	?

Soln: (i) Bank loan raised

Bank a/c Dr.

Bank loan a/c

(Raising of bank loan)

(ii) Issue of debenture as collateral security

Method 1

No journal entry is made in the books because the debentures will become above only when the loan is not repaid.

Method 2

Debenture syspense a/c Dr.

X% debentures a/c

(Issue of debentures as collateral security)

3. Identify the terms of issue and redemption of debentures from the given journal entries and write appropriate narrations, for debentures having a face value of Rs. 1000.

Case I

	Particulars		Debit	Credit
(a)	Bank a/c Dr. 10% Debentures a/c Securities premium a/c ( )		21,00,000	 20,00,000 1,00,000
(b)	10% Debentures a/c Dr. Debenture holders a/c ( )		20,00,000	 20,00,000
(c)	Debenture holders Dr. Bank a/c ( )		20,00,000	 20,00,000

Case II

	Particulars		Debit	Credit
(a)	Bank a/c Dr. Loss on issue of debentures Dr. 10% debentures a/c Premium on redemption of debentures a/c ( )		20,00,000 1,00,000	 20,00,000 1,00,000
(b)	0% Debentures a/c Dr. Premium on redemption of debentures a/c Dr. Debenture holders a/c ( )		20,00,000 1,00,000	 21,00,000
(c)	Debenture holders a/c Dr. Bank a/c ( )		21,00,000	 21,00,000

Soln: Case I: Issued at premium and redeemable at par

Narrations : (a) The issue of 2,000 debentures of Rs. 1,000 each at Rs. 1,050.

(b) The debentures due for redemption.

(c) The amount paid on redemption

Case II: Issued at par and redeemable at premium

Narrations: (a) The issue of 2000 debentures of Rs. 1000 each and redeemable at Rs. 1,050.

(b) The debentures along with premium due for redemption

(c) The amount paid on redemption.

4. New India Ltd. has outstanding 1,100 10% debentures of Rs. 200 each. On April 1, 2005, the Board of Directors have decided to purchase 20% of own debenture for cancellation at Rs. 200 each. Record necessary entries for the same.

Soln: Books of New India Ltd.

Journal

Date	Particulars	L.F	Debit Rs.	Credit Rs.
	Own debentures a/c Dr.		44,000	
	Bank a/c			44,000
	(Purchased its own debentures @ Rs. 200 each) (1100 × 20% = 220)			
	10% Debentures a/c Dr.		44,000	
	Own debentures a/c			44,000
	(Own debenture purchased are cancelled)			

5. On 1st January, 2006, the company purchased debentures of the face value of Rs. 2,00,000 for Rs. 1,97,800 in the open market, held them as investments for one year and then cancelled them.

Date	Particulars	L.F	Debit	Credit
2006 Jan.1	Own debentures Dr.		1,97,800	
	Bank			1,97,800
	(Purchase of own debentures of the face value of Rs. 2,00,000 for Rs. 1,97,800)			
Jan.1	9% Debentures Dr.		2,00,000	
	Own Debentures			1,97,800
	Profit on cancellation of Own Debentures a/c			2,200
	(Cancellation of own debentures of the face value of Rs. 2,00,000 purchased last year for Rs. 1,97,800)			
,,	Profit on cancellation of Own Debentures a/c Dr.		2,200	
	To Capital Reserve a/c			2,200
	(Transfer of profit on cancellation of own debentures to capital reserve)			

6. Traders Ltd. issued on 1st Jan. 2004, 5000, 8% Debentures of Rs. 100 each at a discount of 5%. They are repayable after 5 years at a premium of 5%. All the debentures have been subscribed. Pass entry on 1st Jan 2004.

Soln: Journal

Date	Particulars	L.F	Debit Rs.	Credit Rs.
	Bank a/c(With the amount received) Dr.		4,75,000	
	Discount on issue of debentures a/c Dr. (With the discount allowed)		5,000	
	Loss on issue of debentures a/c Dr. (With the premium payable on redemption)		25,000	
	Traders Ltd (With the nominal value)			5,00,000
	Premium on redemption of debentures a/c (With the premium payable on redemption)			25,000

7. A company purchases its own debentures having a paid up value of Rs. 10,000 for Rs. 10,500. Pass journal entry.

Soln:

Journal

Date	Particulars	L.F	Debit	Credit
	X% debentures a/c Dr.		10,000	
	Loss on redemption of debentures a/c Dr.		500	
	Bank a/c			10,500
	(Debentures are purchased at higher price)			

8. XYZ Ltd. issued 10,000 12% debentures of Rs. 100 each at par. They are redeemable at a premium of 5% after six years. Pass entries at the time of issue of debentures and at the time of redemption of debentures.

Soln:

Journal

Date	Particulars	L.F	Debit	Credit
	Bank a/c Dr.		1000000	
	Loss on issue of debentures a/c Dr.		50000	
	12% debentures a/c			1000000
	Premium on redemption of debentures a/c			50000
	(Being the issue of debentures at par and redeemable at premium)			
	12% debentures a/c Dr.		1000000	
	Premium on redemption of debentures a/c Dr.		50000	
	Debenture holders a/c			1050000
	(The debentures along with premium due for redemption)			
	Debenture holders a/c Dr.		1050000	
	Bank a/c			1050000
	(The amount paid on redemption)			

Chapter 3 - Financial Statements of a Company

1. Describe the general requirements of the Companies Act 1956 for the preparation and presentation of Balance Sheet of a company.

The following are the main provisions laid down by the Companies Act 1956 regarding the preparation and presentation of final accounts of companies.

a) The Balance Sheet and Profit and Loss Account are to be drawn up in strict confirmity with the provisions of Section 211 and Schedule VI of the Companies Act.

b) The annual accounts and every other documents annexed or attached to it must be filed with the Registrar of Companies together with the audit report.

c) The annual accounts must given a true and fair view of the state of affairs of the company at the end of the financial year and the result of operations during the period.

2. Prepare a layout of information required to given under the heading 'share capital'.

Share Capital		
Authorised		
-------- shares of Rs. ------ each	×××	
Issued		
-------- shares of Rs. ------- each	×××	
Subscribed		
------ shares of Rs. ------- each		
Rs. ------ per share called up	×××	
Less : Unpaid calls	×××	
	×××	
Add : Forfeited shares	×××	×××

3. State under which headings the following items will appear.

(i) Share forfeited account
(ii) Unclaimed dividend
(iii) Share premium account
(iv) Proposed dividend
(v) Sundry creditors
(vi) Provision for taxation
(vii) Income received in advance
(viii) Fixed deposits

(i) Share forfeited account - Share capital
(ii) Share premium account - Reserves and Surplus
(iii) Unclaimed dividend - Current liability
(iv) Proposed dividend - Provision
(v) Sundry creditors - Current liabilities
(vi) Provision for taxation - Provision
(vii) Income received in advance - Current liabilities
(viii) Fixed deposits - Unsecured loans

4. Explain the treatment of the following items in the Balance Sheet.

(i) Forfeited shares
(ii) Interest accrued but not due on loans (iii) Calls in arrears (iv) Interest to be paid in secured loans

(i) Add the amount to subscribed capital.
(ii) Show it under the heading current liabilities.
(iii) Subtract it from subscribed capital.
(iv) Show it under the heading secured loans.

5. Record the items which are included under the heading 'Current Assets' and 'Loans and Advances'.

A. Current Assets

1. Interest accrued on investments
2. Stores and spare parts
3. Loose tools
4. Stock-in-trade
5. Work-in-progress
6. Sundry debtors
7. Cash balance in hand
8. Bank balance

B. Loans and Advances

9. a. Advances and loans to subsidiaries.
   b. Advances and loans in partnership firm in which company or any of its subsidiaries is a partner.
10. Bills of Exchange
11. Advances recoverable in cash or kind or for value to be received.
12. Balances with customs, port trust etc.

Chapter 4 - Analysis of Financial Statements

1. **Which of the following analysis helps a company to stop selling goods on account to its customers.**

   (a) Debit analysis (b) Credit analysis

   (c) Capacity analysis (d) Debt analysis

   Credit Analysis

2. **Which analysis helps a company to stop raising debt funds?**

   (a) Debt analysis (b) Debit analysis

   (c) Credit analysis (d) All of the above

   Debt analysis

3. **Make pairs from the following terms which is related to the Balance sheet.**

   Current liability, share premium, debentures, reserves and surplus, secured loans, sundry creditors.

   Current liability - Sundry creditors

   Share premium - Reserves and surplus

   Debentures - Secured loan

4. **Financial statements doesn't record certain aspects which are more worthwhile than monetary aspects.**

   (i) Why such aspects cannot be recorded?

   (ii) Giving examples of such aspects.

   The money measurement assumption (monetary unit assumption) underlines the fact that in accounting every worth recording event, happening or transaction is recorded in terms of money. General health condition of the chairman of the company, working conditions in which a worker has to work etc. cannot be expressed in money terms and therefore are not recorded in the books.

Chapter 5 - Accounting Ratios

1. **(a) Why do the suppliers of goods arrive at various ratios from the financial statements? Explain.**

   Accounting Ratios analysing the information contained in financial statements for assessing the solvency, efficiency and profitability of the firms.

   (b) Calculate the ratios from the given particulars in which creditors are very much interested?

Sundry creditors	**40,000**
Expenses payable	**10,000**
Fixed assets	**2,00,000**
Cash	**10,000**
Debtors	**60,000**
Stock	**25,000**
Bank	**15,000**

$$\text{Current Ratios} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

$$= \frac{110000}{50000} = 2.2 : 1$$

$$\text{Liquid ratio} = \frac{\text{Liquid assets}}{\text{Current liabilities}}$$

$$= \frac{85000}{50000} = 5.67 : 1$$

2. **Given**

Equity share capital	**75,000**
Reserves and Surplus	**25,000**

Profit and loss a/c 50,000

Debentures 1,00,000

Sundry creditors 25,000

(a) How much is the share holders fund?

(b) How much could be the total assets?

(c) Find out a proportion between share holders fund and total assets.

(a) Share holders fund = Equity share capital + Reserves and surplus + Profit and loss a/c

$= 75000 + 25000 + 50000$

= Rs. 1,50,000

(b) Total assets = Total liabilities = Rs. 2,75,000

(c) Ratio between shareholders fund and total assets

$$= \frac{\text{Shareholders fund}}{\text{Total assets}}$$

$$= \frac{150000}{2,75,000} \times 100 = 55\%$$

3. **Read out the data carefully.**

Average stock held 40,000

Cost of goods sold 2,00,000

Can you ascertain the average number of days within which the stock gets exhausted?

$$\text{Debtors Turnover Ratio} = \frac{\text{Cost of goods sold}}{\text{Average stock held}}$$

$$= \frac{200000}{40000} = 5$$

$$\therefore \text{ Average number of days} = \frac{365}{5} = 73 \text{ days}$$

4. **How much is the value of average debtors if**

Cash sales : Rs. 80,000

Credit sales : Rs. 20,000

Number of days the debts are collected is 73.

$$\text{Debtors Turnover Ratio} = \frac{\text{Net Credit Sales}}{\text{Average debtors}}$$

Average collection period

$$= \frac{365}{\text{Debtors Turnover Ratio}}$$

$$73 = \frac{365}{\text{Debtors Turnover Ratio}}$$

$$\text{Debtors Turnover Ratio} = \frac{365}{73} = 5$$

$$\text{Debtors Turnover Ratio} = \frac{\text{Net credit sales}}{\text{Average debtors}}$$

$$5 = \frac{20000}{\text{Average debtors}}$$

$$\therefore \text{ Average debtors} = \frac{20000}{5} = \text{Rs. } 4000$$

5. **The average payment period of Duplo Ltd is 24 days while that of for Keltron Ltd. it is 36 days. In which firm the suppliers will show interest to supply goods on credit. Why?**

A lower credit period signifies that the creditors are being paid promptly,thus enhancing the credit worthiness of the company. So in this case Duplo Ltd. is prompt and quick in settling debts.