



Financial Accounting

SYLLABUS

UNIT-I

Evolution of Accounting in India : Contribution of Shri Kalyan Subramani Aiyar (K.S. Aiyar) 1859-1940 known as father of Accountancy in India. Introduction of Indian Accounting System, Nature and scope of Accounting. Generally Accepted Accounting Principles: Concepts and Conventions. Indian Accounting Standards. Accounting Mechanics: Double Entry System, Preparation of Journal, Ledger and Trial Balance, Profit and Loss A/c, Balance Sheet, Concept of Income and its Measurement.

UNIT-II

Hire Purchase Accounts : Accounting Records in the Books of Hire Purchaser and Vendor, Different Methods of Calculation of Interest and Cash Price, Maintenance of Suspense Account, Default in Payment and Partial Returns of Goods.

Installment Payment System : Difference between Hire Purchase and Installment Payment System. Accounting Records in the book of Purchaser & Vendor, Interest suspense account.

UNIT-III

Departmental Accounts : Meaning, Objects and Importance, Advantage, Methods of Departmental Accounts, Final Accounts of Non-Corporate Departmental Business, Allocation of Indirect Expenses.

Branch Account : Meaning and Objectives of Branch Account, Importance and Advantages, Classification of Branches, Accounting of Branch Accounts under various Methods including Foreign Branch.

UNIT-IV

Royalty Accounts : Accounting Records for Royalty in the books of Landlords and Lessee, Recoupment of Shortworking, Sub-lease, Shortworking Reserve Account, Nazarana.

Insolvency Accounts : (For Individuals/sole trade only) main provisions of IBC 2016, Preparation of Accounts under latest provisions.

Insurance Claims : Computation of claim under loss of Stock Policy & Loss of Profit policy.

Registered Office

Vidya Lok, Baghpat Road, T.P. Nagar,
Meerut, Uttar Pradesh (NCR) 250 002
Phone : 0121-2513177, 2513277
www.vidyauniversitypress.com

© Publisher

Editing & Writing

Research and Development Cell

Printer

Vidya University Press

CONTENTS

UNIT-I	: Evolution of Accounting in India	...3
UNIT-II	: Hire-Purchase Accounts and Instalment Payment System	...33
UNIT-III	: Departmental Accounts and Branch Accounts	...59
UNIT-IV	: Royalty Accounts & Insolvency Accounts	...99
○	Model Paper	...135

UNIT-I

Evolution of Accounting in India

SECTION-A (VERY SHORT ANSWER TYPE) QUESTIONS

Q.1. What do you know about Shri Kalyan Subramani Aiyar?

Ans. Shri Kalyan Subramani was known as father of accounting in India. Shri Kalyan Subramani Aiyar (1859-1940), better known as K. S. Aiyar, was a pioneer of commercial and accounting in India. He started and established educational courses and institutions dedicated to commerce and accounting. He also served as the headmaster of first commercial school in India started by the Pachiyappa College Charities at Madras from 1886 to 1889.

Q.2. Mention any two main objectives of accounting.

Ans. The objectives of accounting can be stated as follows:

1. **To keep systematic records:** Accounting is done to keep a systematic record of financial transactions, like purchase of goods, sale of goods, cash receipts and cash payments. Systematic record of various assets and liabilities of the business is also to be maintained.
2. **To ascertain the net effect of the business operations i.e., profit or loss of business:** We know that the primary objective of business is to make profit and the businessman is very much interested in knowing the same. A proper record of income and expenses facilitates the preparation of the profit and loss account (income statement). The profit and loss account reveals the profit earned or loss incurred by the business firm during a particular period.

Q.3. What do you mean by 'Accounting Standards' or AS?

Ans. Accounting Standards or AS may be described as the written policy documents, which are issued by an expert accounting body or Government or other regulatory body, covering the aspects of recognition, measurement, accounting treatment, presentation of disclosure of accounting transactions in financial statement. Accounting Standards are selected set of accounting policies or board guidelines regarding the principles, concepts and conventions issued by Institute of Chartered Accountants of India. Accounting Standards are issued for the preparation of uniform and consistent financial statements and also for other disclosures affecting the different users of accounting informations. Its nature is recommendatory or mandatory.

Q.4. Define the term 'Accounting Standard' in the words of T.P. Ghosh and Kohler.

Ans. According to T.P. Ghosh, "Accounting Standards are the policy documents issued by recognised expert accounting body relating to various aspects of measurement, treatment and disclose of accounting transactions and events."

According to Kohler, "Accounting Statndards are a mode of conduct imposed on accountant and by custom, law and professional body."

Q.5. Write the contents of Accounting Standards.

Ans. In practice, Accounting Standard has following contents:

1. A statement of the concepts and fundamental accounting principles defining to the accounting standard.
2. Definition of the terms used in the accounting standard.
3. The manner of applying accounting principles for formulating the accounting standard.
4. The presentation of disclosure requirements in complying with accounting standard.
5. Class of enterprises to which the accounting standard will apply.
6. Date from which the accounting standard will be effective.
7. Nature of accounting standard—recommendatory or mandatory.

Q.6. What do you mean by ledger?

Ans. Ledger is a book which contains all accounts affected by various transactions in a business. Ledger can be termed as a classified and summarised record of business transactions relating to all personal, real and nominal accounts.

All transactions which are first recorded in the journal, must invariably be posted into the concerned accounts in the ledger. This is necessary because Journal is just a chronological record of transactions, identifying the accounts to be debited and credited. It does not help us know the net effect of various transactions affecting a particular account.

Q.7. Explain the advantages of double entry system.

Ans. This system has the following advantages:

1. It provides complete and reliable record of all business transactions because it records both effects.
2. It supplies full information about the incomes and expenses, assets and liabilities of the business. It, thus, helps the management in taking appropriate decisions.
3. The arithmetical accuracy of the books of account can be ascertained by preparing a trial balance.
4. The financial result of the operations of the business i.e., profit or loss, can be easily ascertained.

Q.8. What do you mean by accounting?

Ans. Accounting is a discipline which records, classifies and summarises data and presents it in a convenient form to various levels of management in an organisation for decision-making purposes. It helps managers prepare their budget plans realistically so that the expenditure could be watched against the budget allocation, and corrective action could be taken, wherever necessary. It also helps outsiders i.e. shareholders/ government, to know the working of the business firm, by presenting data about its activities, profit or loss and its assets and liabilities.

Q.9. What is meant by Profit And Loss Account?

Ans. A Profit and Loss Account provides us with an overview of our company's revenue and expenses over a given period of time. These figures will show us whether our business made a profit or loss over that period (usually either one month or consolidated months over the course of a year). As a result, it's one of the most important financial documents our business will need to produce.

Q.10. Define the term 'National Income'.

Ans. National Income of any country means the complete value of the goods and services produced by any country during its financial year. It is thus the consequence of all economic activities that are running in any country during the period of one year. It is valued in terms of money. In short, one can say that the national income of any country is the total amount of income that is accrued by it through various economic activities in one year. It is also helpful in determining the progress of the country. It includes wages, interest, rent, profit, received by factors of production like labour, capital, land entrepreneurship of a nation.

Q.11. What is meant by balance sheet?

Ans. A balance sheet is a statement of assets, liabilities and capital of an organisation as on a particular date. In short, it shows what a company owns and owes. Additionally, it shows the amount invested in the business. Along with other financial statements helps to calculate the profitability, liquidity, leverage and efficiency of a business.

A balance sheet has assets on one side and liabilities and capital on the other side both the sides are always equal.

Therefore, $\text{Assets} = \text{Liabilities} + \text{Capital}$.

Q.12. What is accounting convention?

Ans. An accounting convention refers to common practices which are universally followed in recording and presenting accounting information of the business entity. They are followed like customs, traditions, etc. in a society. Accounting conventions are evolved through the regular and consistent practice over the years to facilitate uniform recording in the books of accounts. Accounting conventions help in comparing accounting data of different business units or of the same unit for different periods. These have been used for a long period are: Convention of consistency, Convention of full disclosure, Convention of materiality and Convention of conservatism.

SECTION-B (SHORT ANSWER TYPE) QUESTIONS

Q.1. Discuss the objectives and contents of Accounting Standards.

Ans. Objectives of Accounting Standards

The main purposes/aims/objectives of Accounting Standards are as follows:

1. To standardize the diverse accounting policies and practices with a view to eliminate to the extent possible the non-comparability of financial statements and add the reliability to financial statements.
2. To ensure all required significant policies to be adopted in the preparation and presentation of financial statements.
3. To permit flexibility to make the necessary adjustments in preparation of accounting records.
4. To make financial statement more effective, useful, relevant and meaningful.
5. To present the financial statement in reliable and comparable form.
6. To disclose accounting policies in case of change in accounting process or principles.
7. To ensure direct effect on the working results and financial position of a business.

Contents of Accounting Standards

Accounting standard has following contents:

1. Date from which the accounting standard will be effective.
2. Definition of the terms used in Accounting Standard.
3. The manner of applying accounting principles for formulating the accounting standard.
4. The presentation of disclosure requirements in complying with accounting standard.
5. Class of enterprises to which the accounting standard will apply.
6. A statement of the concepts and fundamental accounting principles defining to the accounting standard.

Q.2. Explain the various definitions of Accounting Standards.

Ans. Main definitions are as follows :

Accounting Standards may be defined as, Standardised Accounting Policy and Terminology issued by a recognised expert accountant body. These standards are universally accepted. The sole objective of Accounting Standards is to harmonise the diversified policies to make the system more useful and effective.

According to International Accounting Standard Committee: The uniform, definite and universally accepted accounting rules developed by International Accounting Standard Committee (IASC) are known as Accounting Standard. As per, T.P. Ghosh, "Accounting Standards are the policy documents issued by recognised expert accounting body relating to various aspects of measurement, treatment and disclose of accounting transactions and events. Kohler opines, "Accounting Standrads are a mode of conduct imposed on accountant and by custom, law and professional body." Accounting Standard means the standard of accounting recommended by the Institute of chartered Accountants of India and prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standrads constituted under section 210 A (1) of Indian Companies Act, 1956.

Q.3. Explain briefly the advantages and needs of Accounting Standards.

Ans. **Advantages of Accounting Standards**

The advantages of Accounting Standrad may be listed as follows:

1. It helps in providing the norms on the basis of which financial statements should be prepared.
2. It makes accounting process more meaningful and informative.
3. It boosts the credibility and reliability of financial statements.
4. It ensures the consistensy, uniformity, relevency and comparability of fiancial statements.
5. It helps in reducing the chances of conflicts, manipulations and frauds.
6. It controls the controversy of accounting practices.

Need for Accounting Standards

The need for Accounting Standards can be listed as follows:

1. To determine the managerial accountability, corporate accountability and financial accountability.
2. To improve the relevancy, simplicity, credibility and reliability of financial statement.
3. To help in explaining the accounting terminology.
4. To remove the rigidity of accounting policies.
5. To present a logical view on controversial accounting practices.

6. To give scientific approach to disclosure and presentation of financial statement.
7. To prevent the users from reaching and misleading conclusions.
8. To prevent manipulation of data by the management and others.

Q.4. Discuss the nature of Accounting Standards as per practical accounting.

Ans. Nature of Accounting Standards

According to practical accounting nature of accounting standards are as follows:

1. It is an accounting rule and procedures relating to measurement, valuation and disclosure issued by the Council of the Institute of Chartered Accountants of India.
2. Accounting Standards are made taking into account the laws of the country, business customs, business environments, business laws, economic policies and Constitution of the country.
3. Making accounting informations and financial statements more comparable, flexible and meaningful.
4. Serving the accountants as a guide in the accounting treatment. They provide basis on which accounts are prepared. For example, Accounting Standard-2 provides the methods of valuation of inventions.
5. Determining the accounting policies and practices.
6. It prescribes a suitable accounting treatment among the alternatives.
7. It provides the bases of accounting process and the financial areas of accounting.
8. Acting as a harmonizer and removes the conflict on accounting issues.
9. It is descriptive in nature and serves as a dictator of accounting principles.
10. Accounting Standards are recommendatory or mandatory in nature.

Q.5. Discuss the convergence to IFRS in India.

Ans. Indian accountants and businessmen feel the need for convergence with IFRS. Capital markets provide an important explanation for this change. Some Indian companies are already listed on overseas stock exchanges and many more will list in the future. Internationally acceptable accounting standards are becoming the language of communication for Indian companies.

Also, the recent stream of overseas acquisitions by Indian companies makes a compelling case for adoption of high quality standards to convince foreign enterprises about the financial standing as also the disclosure and governance standards of Indian acquirers. Convergence with IFRS would require several changes in Indian laws and decision processes.

In India, the Institute of Chartered Accountants of India (ICAI) is on the way towards convergence of its Standards with Global Standards. Divergences have been minimized to the maximum possible extent in the areas wherein full convergence is difficult. Recognizing the growing need of full convergence of Indian Accounting Standards with IFRSs, ICAI constituted a Task Force to examine various issues involved. Full convergence involves adoption of IFRSs in the same form as that issued by the IASB. While formulating the Accounting Standards, ICAI recognizes the legal and other conditions prevailing in India and makes deviations from the corresponding IFRSs.

The Accounting Standard Board in consultation with the Ministry of Corporate Affairs (MCA) for convergence of Indian Accounting Standards with International Financial Reporting Standards (IFRS), has decided that there will be two separate sets of Accounting Standards viz. (i) Indian Accounting Standards converged with the IFRS standards which are being

converged by eliminating the differences of the Indian Accounting Standards vis-a-vis IFRS (known as Ind AS) and (ii) Existing Notified Accounting Standards.

Q.6. Explain the features and objectives of human resource accounting.

Ans. Main Features of Human Resource Accounting

Following are main features of Human Resource Accounting:

1. It is a system of accounting in which identification of human resources is made. All categories of people employed in the organization from top management to bottom are included in human resources.
2. Investments made in human resources is recorded.
3. Measurement of cost and value of human resources is made.
4. Record is also maintained for the changes occurring in human resources over a period of time.
5. Information generated about human resources is communicated through financial statements to the interested parties. Thus H.R.A. is a part of Management Information System.

Objectives of Human Resource Accounting

This accounting system is such a thought whose object is to determine the following things:

1. What is the number and value of efficient, sincere and committed people in the organization?
2. Whether the benefit derived from the people working in the organization is higher than the cost (cost involved in recruiting, attracting and retaining these people).
3. Whether the factors motivating for the work and also offering commitment to the work are correctly measured.

Q.7. Discuss the major effects of inflation on financial statements.

Ans. Effects of Inflation on Financial Statements

Prominent effects of inflation on financial statements are described below:

1. **Valuation of Stock** : Under traditional accounting system, stock is valued either at cost or market price, whichever is less. If during the year the prices of goods purchased or sold increase, the amount of profit would be increased, if such price rise is not adjusted to valuation of stock.
2. **Capital is not Intact** : Since in the case of inflation real profit is less than the reported profit, therefore, whatever is distributed as dividend, that is out of such profit which has not been earned. Thus dividend distribution is not out of profit but out of capital and thus capital erodes and it is not kept as intact.
3. **Inadequate Funds for Replacement** : Under traditional accounting depreciation is calculated by dividing historical costs of the asset by the number of years of economic life of the assets. The objective is only to accumulate that much of amount in the form of depreciation at the end of economic life of the assets, for which the assets was purchased, so that new assets in place of old asset is purchased by accumulated amount or fund. But due to inflation (i.e., rise in the cost of asset) the cost of new asset (replacing asset) might have increased so much that accumulated fund becomes inadequate for replacement. For example, a machinery costing ₹ 1,00,000 was purchased in the year 2004. This life was 10 years and ₹ 10,000 p.a. was deducted as

depreciation. The price-level increased by 40% after 10 years of economic life. The accumulated depreciation after 10 years would be ₹ 1,00,000 but for replacement ₹ 1,00,000 + 40% i.e., ₹ 1,40,000 would be needed. Thus there will be shortage of ₹ 40,000.

4. **Understatement of Assets :** It is normally felt that the Balance Sheet portrays the true and fair view of the financial position of the enterprise. But the fact is otherwise. Since fixed assets are shown in the Balance Sheet at cost minus depreciation, and this value is less than present current value or realisable value, therefore assets shown in the Balance Sheet do never disclose real value. For example, a land was purchased for ₹ 20,000 in 2018. In balance sheet of 2019 also, this would have been shown at ₹ 20,000, while in 2020 the value of this land would have been ₹ 2,00,000. In this way, the Balance Sheet fails to predict the true situation of the concern.

Q.8. Discuss the major reasons for the emergence of price-level accounting. Also give the various definitions of accounting for inflation.

Ans. Reasons for the Emergence of Price-Level Accounting

It is revealed from the discussion made thus far that the distorted picture presented by financial statements in the case of inflation are due to the factors mentioned below. Since inflation accounting is needed to reflect these illusory and distorted pictures, these factors are also considered responsible for the emergence of inflation accounting :

1. Presentation of incorrect picture by financial statements during the period of price-level changes because of showing the fixed assets at cost;
2. At the time of rise in prices, reporting of notional and overstated profit due to over valuation of stock and lower amount of depreciation charged;
3. Erosion of capital due to more payment of dividend and tax than what is due on the basis of real profit;
4. Difficulties in asset replacement on account of deficiency of fund due to inflation;
5. Inadequacy of working capital due to rise in price-level;
6. Losses on holding monetary assets like cash, debtors, etc. and gains on monetary items of liabilities.

Definition of Accounting for Inflation

The whole set of accounting procedures designed for adjustments of various accounting items for the changes in price-levels may be called Accounting for price-level. In other words, Accounting for price-level is that accounting technique by which transactions are recorded at current prices and the effect of changes in price-level on accounting items is neutralised or such effects are made clear alongwith transactions recorded at historical costs. Few definitions given by the experts are given below :

According to **J. Batty**, "The term revaluation accounting is used to denote the methods used for overcoming the problems connected with fixed assets replacement in a period of rising prices."

As per **Foulke**, "Stabilised Accounting is a method of converting values by means of an index number from cost or depreciated cost to current economic values."

H. Chakravarty opines, "The principle of replacement accounting is that for determination of income, revenues are matched not against actual cost but against what is expected cost for replacement of stock sold and the portion of assets depleted in the process of business operations."

Q.9. K.S. Aiyar is known as 'Father of Accountancy in India.' Explain the biography of K.S. Aiyar.

Ans. Shri Kalyan Subramani Aiyar (1859-1940), better known as K. S. Aiyar, was a pioneer of commercial and accounting education in India. He started and established educational courses and institutions dedicated to commerce and accounting. He also served as the headmaster of first Commercial School in India started by the Pachiyappa College Charities at Madras from 1886 to 1889. He got elected as an Associate of the Society of Incorporated Accountants & Auditors (SIAA) of the UK in 1890 and started his public practice. He set up his own firm, in 1900, probably the earliest accountants' firm in India established by an Indian. Starting his practice in Calicut in 1897, he shifted to Bombay in 1900. In fact, it was Sir Byramjee Jeejeebhoy, a 19th century philanthropist and a big land owner, who founded several educational institutions in Bombay, invited Shri Aiyar to Bombay in the first decade of the twentieth century and later appointed him the Principal of the Byramjee Jeejeebhoy Parsee Charitable Institution (B.J.P.C.I), Bombay. Shri Aiyar later converted that Institution into College of Commerce in 1900, which aimed at preparing students for the London Chamber of Commerce examinations. Within a couple of months, he also started the first Night School of Commerce in Bombay. He credited for procuring the permission in 1905 from the SIAA to train apprentices in India for their London examinations. Shri Sorab S. Engineer was the first Incorporated Accountant to serve his apprenticeship in India under Shri Aiyar in his firm from 1905 to 1908, and then served the same firm for another five years. Shri Engineer has been proclaimed guru of the first President of The Institute of Chartered Accountants of India, Shri G.P. Kapadia. In 1912, Shri Aiyar instituted the first Bachelor of Commerce degree in the Bombay University. He established an important education centre of commerce Sydenham Collehe of Commerce, in Bombay in 1913, and acted as its first honorary Principal. Shri Aiyar wrote the scheme of the Government Diploma in Accountancy (GDA) for the Government of Bombay on the recommendations of the Accountancy Diploma Board.

SECTION-C LONG ANSWER TYPE QUESTIONS

Q.1. Define the term 'Accounting'. Also discuss the scope of accounting.

Ans. **Accounting**

The American Accounting Association defines Accounting as the process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users of the information. This definition stresses three aspects viz., identifying, measuring and communicating economic information.

In the words of the Committee on Terminology appointed by the American Institute of Certified Public Accountants, "Accounting is the art of recording, classifying and summarizing in a significant manner and in terms of money, transactions and events which are, in part at least of financial character and interpreting the results thereof". This is a popular definition of accounting and it outlines the nature and scope of accounting activity.

A business is generally started with proprietor's funds i.e., capital. The proprietor may also acquire additional funds from outsiders like banks and creditors. These funds are utilised to acquire the assets needed for business and also to carry out other business activities. In the process many transactions and events take place. The accountant has to identify all such transactions and events, measure them in terms of money, and record them in appropriate

books of account. Then, he has to classify them under separate heads of accounts, summarise periodically in the form of Profit and Loss Account and Balance Sheet; and analyse, interpret and communicate the results thereof to the interested parties. Accounting can thus be broadly defined as follows;

Accounting is the process of identifying, measuring, recording, classifying, summarising, analysing, interpreting, and communicating the financial transactions and events in monetary terms.

Scope of Accounting

The above definitions clearly bring out the scope of accounting. This can now be outlined as follows:

1. Accounting is concerned with financial transactions and events which bring about a change in the resources (or wealth) position of the business firm. Such transactions have to be identified first, as and when they occur. It is not difficult because, there will be proof in the form of a bill or receipt (called vouchers). With the help of these bills and receipts, identification of a transaction is easy. For example, when you purchase something you get a bill, when you make payment, you get a receipt.
2. These transactions are to be measured or expressed in terms of money, if not done already. Generally, this problem will not arise, because the statement of proof expresses the transaction in terms of money. For example, if ten books are purchased at the rate of ₹ 20 each, then the bill is prepared for ₹ 200. But, if an event cannot be expressed in monetary terms, it will not come under the scope of accounting.
3. The transactions which are identified and measured are to be recorded in a book called journal or in one of its sub-divisions.
4. The recorded transactions are to be classified with a view to group transactions of similar nature at one place. The work of classification is done in a separate book called ledger. In the ledger, a separate account is opened for each item so that all transactions relating to it can be brought to one place. For example, all payments of salaries are brought to salaries account.
5. The recording and classification of many transactions will result in a mass of financial data. It is, therefore, necessary to summarise such data periodically (at least once a year), in a significant and meaningful form. The summarisation is done in the form of profit and loss account which reveals the profit made or loss incurred, and the balance sheet which reveals the financial position.
6. The summary results will have to be analysed, interpreted (critically explained) and communicated to interested parties. Accounting information is generally communicated in the form of a 'report'. Big organisations generally present printed reports, called published accounts.

Q.2. What do you know about 'Accounting Principles'? Explain the following accounting concepts :

1. Business entity concept
2. Money measurement concept
3. Objective evidence concept

Ans. Accounting Principles

Accounting is a system evolved to achieve a set of objectives. The objectives identify the goals and purposes of financial record keeping and reporting. In order to achieve the goals, we need

a set of rules or guidelines. These guidelines are termed here as 'Basic Accounting Concepts'. The term 'concept' means an idea or thought. Basic accounting concepts are the fundamental ideas or basic assumptions underlying the theory and practice of financial accounting. These concepts are also termed as 'Generally Accepted Accounting Principles'. These are the broad working rules of accounting activity, developed and accepted by the accounting profession. They are evolved (and are still evolving) over a period in response to the changing business environment and the specific needs of the users of accounting information.

The concepts guide the identification of events and transactions to be accounted for, their measurement and recording, and the method of summarising and reporting to interested parties. The concepts, thus, help in bringing about uniformity in the practice accounting.

An indepth understanding of these concepts will place the student in a better position to appreciate accounting system. Of course, it may be difficult to comprehend all these concepts at a stretch. We, therefore, advise you to revisit these concepts, after giving at least one reading of this course material.

These concepts may be classified into two broad groups:

1. Concepts to be observed at the recording stage *i.e.* while recording the transactions, and
2. Concepts to be observed at the reporting stage, *i.e.* the time of preparing the final accounts.

Accounting Concepts

1. **Business Entity Concept** : Business entity means a unit of organised business activity. In that sense, a provision store, a cloth dealer, an industrial establishment or electricity supply undertaking, a bank, a school, a hospital, etc. are all business entities.

From the accounting point of view, every business enterprise is an entity separate and distinct from its proprietor(s)/owner(s). The accounting system gives information only about the business and not about its owner(s). In other words, we record those transactions in the books of account which relate only to the business. The owner's personal affairs (his expenditure on housing, food, clothing, etc.) will not appear in the books of account of his business. However, when personal expenditure of the owner is met from business funds it shall also be recorded in the business books. It will be recorded as drawings by the proprietor and not as business expenditure.

Another implication of business entity concept is that the owner of business is to be treated as a creditor who also has a claim over the assets of the business. As such, the amount invested by him (capital) is regarded as a liability for the business.

The business entity concept is applicable to all forms of business organisations. This distinction can be easily maintained in the case of a limited company because the company has a legal entity of its own. But such distinction becomes difficult in case of a sole proprietorship or partnership because in the eyes of the law, the partner or the sole proprietor are not considered separate entities. They are personally liable for all business transactions. But, for accounting purposes, they are to be treated as separate entities. This enables them to ascertain the profit or loss of business more conveniently and accurately.

2. **Money Measurement Concept** : Usually, business deals in a variety of items having different physical units such as kilograms, quintals, tons, metres, litres, etc. If the sales

and purchases of different items are recorded in terms of their physical units, adding them together will pose problems. But, if these are recorded in a common denomination, their total becomes homogeneous and meaningful. Therefore, we need a common unit of measurement. Money does this function. It is adopted as the common measuring unit for the purpose of accounting. All recording, therefore, is done in terms of the standard currency of the country where business is set up. For example, in India, it is done in terms of Rupees, in USA it is done in terms of US Dollars, and so on.

Another implication of money measurement concept is that only those transactions and events are to be recorded in the books of account which can be expressed in terms of money such as purchases, sales, payment of salaries, goods lost in accident, etc., other happenings (non-monetary) like death of an efficient manager or the appointment of an accountant, howsoever important they may be, are not recorded in the books of account. This is because their effect is not measurable or quantifiable in terms of money.

This approach has its own drawbacks. The value of money changes over a period of time. The value of rupee today is much less than what it was in 1961. Such a change is nowhere reflected in accounts. This is the reason why the accounting data does not reflect the true and fair view of the affairs of the business.

Hence, now-a-days, it is considered desirable to provide additional data showing the effect of changes in the price level on the reported income and the assets and liabilities of the business.

3. **Objective Evidence Concept** : The term objectivity refers to being free from bias or free from subjectivity. Accounting measurements are to be unbiased and verifiable independently. For this purpose, all accounting transactions should be evidenced and supported by documents such as bills, invoices, receipts, cash memos, etc. These supporting documents (vouchers) form the basis for making entries in the books of account and for their verification by auditors afterwards. As for the items like depreciation and the provision for doubtful debts where no documentary evidence is available, the policy statements made by management are treated as the necessary evidence.

Q.3. Discuss the following accounting concepts which are to be observed at the recording stage:

1. Historical record concept
2. Cost concept
3. Dual aspect concept

Ans. 1. **Historical record concept** : You know that after identifying the transactions and measuring them in terms of money, we record them in the books of account. According to the historical record concept, we record only those transactions which have actually taken place and not those which may take place (future transactions). It is because accounting record presupposes that the transactions are to be identified and objectively evidenced. This is possible only in the case of past (actually happened) transactions. The future transactions can hardly be identified and measured accurately. You also know that all transactions are to be recorded in chronological (datewise) order. This leads to the preparation of a historical record of all transactions. It also implies that we simply record the facts and nothing else.

As you will study later we make provision for some expected losses such as doubtful debts. This may be contrary to what is stated in historical record concept. But this is done only at the time of ascertaining the profit or loss of the business. It is not a routine item. This is done in accordance with another concept called Conservatism Concept about which you will study later.

2. **Cost Concept :** Business activity, in essence, is an exchange of money. The price paid (or agreed to be paid in case of a credit transaction) at the time of purchase is called cost. According to the cost concept, all assets are recorded in books at their original purchase price. This cost also forms an appropriate basis for all subsequent accounting for the assets. For example, if the business buys a machine for ₹ 80,000 it would be recorded in books at ₹ 80,000. In case its market value increases later on to ₹ 1,00,000 (or decreases to ₹ 50,000) it will continue to be shown at ₹ 80,000 and not at its market value.

This does not mean, however, that the asset will always be shown at cost. You know that with passage of time, the value of an asset decreases. Hence it may systematically be reduced from year to year by charging depreciation and the asset be shown in the balance sheet at the depreciated value. The depreciation is usually charged as a fixed percentage of cost. It bears no relationship with changes in its market value. In other words, the value at which the assets are shown in the balance sheet has no relevance to its market value. This, no doubt, makes it difficult to assess the true financial position of the business. It is, therefore, regarded as an important limitation of the cost concept. But this approach is preferred because, firstly it is difficult and time consuming to ascertain the market values, and secondly there will be too much of subjectivity in assessing the current values. However, this limitation has been overcome with the help of inflation accounting.

3. **Dual Aspect Concept :** This is the basic aspect of accounting. According to this concept, every business transaction has a two-fold effect. In commercial context, it is a famous dictum that "every receiver is also a giver and every giver is also a receiver". For example, if you purchase a machine for ₹8,000, you receive machine on the one hand and give ₹8,000 on the other. Thus, this transaction has a two-fold effect i.e.,

(i) increase in one asset and (ii) decrease in another. Similarly, if you buy goods worth ₹500 on credit it will increase an asset (stock of goods) on the one hand and increase a liability (creditors) on the other. Thus, every business transaction involves two aspects:

(i) the receiving aspect, and (ii) the giving aspect. In case of the first example you find that the receiving aspect is machinery and the giving aspect is cash. In the second example the receiving aspect is goods and the giving aspect is the creditor. If complete record of transactions is to be made, it would be necessary to record both the aspects in books of account. This principle is the core of double entry book-keeping and if this is strictly followed, it is called 'Double Entry System of Book-keeping'.

Let us understand another accounting implication of the dual aspect concept. To start with, the initial funds (capital) required by the business are contributed by

the owner. If necessary, additional funds are provided by the outsiders (creditors). As per the dual aspect concept all these receipts create corresponding obligations for their repayment. In other words, a contribution to the business, either in cash or kind, not only increases its resources (assets), but also its obligations (liabilities/equities) correspondingly. Thus, at any given point of time, the total assets and the total liabilities must be equal. This equality is called 'balance sheet equation' or 'accounting equation'. It is stated as under:

$$\text{Liabilities (Equities)} = \text{Assets}$$

or

$$\text{Capital} + \text{Outside Liabilities} = \text{Assets}$$

Q.4. Discuss Accounting Standards in India. Also explain the procedure for issuing Accounting Standards in India.

Ans. Introduction to AS in India

The Accounting Standards issued by ICAI did not have any legal support till 1999 when Indian Companies Act was amended to make it obligatory for complying with the accounting policies framed by the Central Govt. in Consultation with NACAS (National Accounting Committee on Accounting Standards). It was also provided that the standards issued by the Institute of Chartered Accountants of India shall be applicable till the formulation of accounting standards by NACAS. A provision has also been made for 'Directors' Responsibility Statement' to report on the Compliance of accounting standards and deviations if any along with reasons for such deviation. At the same time, auditors of the company are already entrusted with this responsibility as per by laws of the Institute of Chartered Accountants of India. Thus, the amendment of Companies Act has ensured justifiable place for accounting standards in the Indian Corporate reporting system. SEBI (Security Exchange Board of India) has added a new clause in the listing agreement to provide that listed enterprises shall mandatorily comply with all the Accounting Standards issued by the ICAI from time to time. Again, notification of Insurance Regulatory and Development Authority (IRDA) requires insurance enterprises to follow the accounting standards issued by the ICAI.

Apart from the corporate bodies, the Council of Institute of Chartered Accountants of India has made various accounting standards mandatory in respect of certain non-corporate entities such as partnership firms, sole proprietary concerns/individuals, societies, trusts, A.O.P. and H.U.F. where financial statements of such entities are statutorily required to be audited, e.g. under Section 44AB of the Income Tax Act, 1961.

Procedure for Issuing Accounting Standards in India

The Institute of Chartered Accountants of India (ICAI) constituted the Accounting Standards Board on 21st April, 1977 with a view to harmonise the diverse accounting policies and practices in use in India and also to develop in the field of accounting at international level. It is one of the member of International Accounting Standards Committee. This Board is also committed to develop and to integrate the standards issued by IASC to the extent possible in the light of conditions and practices prevailing in India.

The composition of the Accounting Standards Board is broad-based with a view to ensuring participation of all interest-groups in the process of formulation of standards. These interest groups include industry, various departments of Government and regulatory authorities, financial institutions and academic and professional bodies. Industry is represented by their apex level associations, viz. Associated Chamber of Commerce and Industry of India,

Federation of Indian Chamber of Commerce and Industry and Confederation of Indian Industries. As regards government departments and regulatory authorities, Reserve Bank of India, Department of Company Affairs, Central Board of Direct Taxes, Comptroller and Auditor General of India, Controller of General Accounts, Security Exchange Board of India, and Central Board of Excise and Customs are represented on the ASB. Beside these, representatives of academic and professional institutions such as universities, IIMS, ICWA and ICSI are also represented on the ISB. Members of the Central Council of ICAI are also on the ASB.

The main function of the ASB is to develop accounting standards in India and to ensure their applicability. Whatever the standards formulated by Accounting Standards Board, they are in accordance with conditions prevailing in India, local conventions and applicable laws, so that these standards are set by the ICAI and are complied with by the parties in preparing and presenting the financial accounts and also that these standards are made mandatory. The ASB has adopted a very objective approach to rules and limitations relating to the publication of financial statements with a view to eliminate the double accounting policy and also to limit the alternatives in selecting from the diverse alternate methods of accounting. This Board formulated standards for practical applications of those principles which were experienced for performing accounting activities on the basis of basic concepts. The Board also explains the terms used in financial statements along with the formulation of standards and there is need it can modify and improve the defined terms used in accounting according to changed situation.

If the enterprises, for whom the Board has formulated the accounting standards, have any problem or difficulty in complying or applying the Standards, they can have guidelines from the Board. The function of Accounting Standard Board is not only to decide and to incorporate accounting standards but also to revise and to modify from time to time the standards issued as per the changed situation is also within its purview.

Q.5. Explain the matching concept of accounting. What are the rules to be followed for this purpose?

Ans.

Matching Concept

This is also called 'Matching of Costs against Revenues Concept'. To work out profit or loss of an accounting year, it is necessary to bring together all revenues and costs pertaining to that accounting year. In other words, expenses incurred in an accounting year should be matched with the revenues earned during that year. The crux of the problem, therefore, is that appropriate costs must be matched against appropriate revenues. For this purpose, first we have to recognise the inflows (revenues) during an accounting period and the costs incurred in securing those inflows. Then, the sum of the costs should be deducted from the sum of the revenues to arrive at the net result of that period. Let us now understand how to recognise the revenues and costs in relation to an accounting period. Rules of Matching Concept.

Rules of Matching Concept

For this purpose, the following rules are followed:

1. **The Timing of Revenue Recognition** : Revenue is recognised in the period in which it is earned or realised. The revenue recognition is primarily based on realisation principle which clearly states that in identifying revenues with a specific period one must look to when the various transactions occurred rather than to the period in which cash inflow occurred. Thus,

- (i) In case of the sale of goods (or services) revenue is regarded as realised when sales actually take place and not when cash is received. In other words, credit sales are treated as revenue when sales are made and not when money is received from the debtors.
 - (ii) Income such as rent, interest, commission, etc. are recognised on a time basis. The revenue from such items is taken to the Profit and Loss Account of the year during which it is earned. Let us assume that the business purchased some government securities on October 1, 2018 for ₹ 20,000 carrying interest at 12 per cent. The interest is payable half yearly on April 1 and October 1 every year. The first instalment of interest (₹ 1,200) is received on April 1, 2019. The Profit and Loss Account is being prepared for the year 2018 (January 1, 2018 to December 31, 2018). The interest amounting to ₹ 600 earned during October 1 to December 31 must be shown as the income from interest on investments in the Profit and Loss Account for 2018 though the amount has not been received in 2018.
- 2. The Timing of Costs Recognition :** The matching principle holds that the expenses should be recognised in the same period as the associated revenues. Thus,
- (i) The cost of goods have to be matched with their sales revenue. This means that while preparing the Profit and Loss Account for a particular year, you should not take the cost of all the goods produced during that year, but consider only the cost of goods that have actually been sold during that year. The cost of goods sold is arrived at by deducting the cost of closing stock from the cost of goods produced.
 - (ii) Expenses such as salaries, wages, interest, rent, insurance, etc., are recognised on time basis. In other words, they are related to the year in which the service is obtained or the expense is incurred, whether paid immediately or payable at a later date.
 - (iii) Costs like depreciation on fixed assets are also allocated on time basis.

Thus, all revenue earned during an accounting year, whether received or not, and all costs incurred, whether paid or not have to be taken into account while preparing the Profit and Loss Account for the year. Similarly, any amount received or paid during the current year which actually relates to the previous year or the following accounting year, must be eliminated from the current year's revenue and costs. This gives rise to another aspect viz., the accrual basis of accounting about which you will learn later.

Q.6. Explain the following accounting concept which are to be observed at the reporting stage:

- | | |
|-----------------------------------|-------------------------------|
| 1. Conservation Concept | 2. Consistency Concept |
| 3. Full disclosure Concept | 4. Materiality Concept |

Ans. 1. Conservatism Concept : This is also known as Prudence Concept understatement of assets or revenues, and overstatement of liabilities or costs. This is in accordance with the traditional view which states 'anticipate no profits but anticipate all losses'. In other words, you should account for profits only when they are actually realised. But in case of losses, you should take into account even those losses which may be a remote possibility. This is why closing stock is valued at cost price or market price whichever is lower. Provision for doubtful debts and provision for discounts on debtors are also made according to this concept.

2. **Consistency Concept** : The principle of consistency means 'conformity from period to period with unchanging policies and procedures'. It means that accounting method adopted should not be changed from year to year. For example, the principle of valuing closing stock 'at cost price or market price whichever is lower' should be followed year after year. Similarly, if depreciation on fixed assets is provided on straight line basis, it should be followed consistently year after year. Consistency eliminates personal bias and helps in achieving comparable results.

If this principle of consistency, is not followed, the accounting information about an enterprise cannot be usefully compared with similar information about other enterprises and so also within the same enterprise for some other period. Consistent use of the same methods and bases from one period to another, enhances the utility of the financial statement.

However, consistency does not prohibit change. Desirable changes are always welcome. But such changes should be completely disclosed while presenting the financial statements.

3. **Full Disclosure Concept** : You know the financial statements are the basic means of communicating financial information to all interested parties. These statements are the only source for assessing the performance of the enterprise for investors, lenders, suppliers, and others. Therefore, financial statements and their accompanying foot-notes should completely disclose all relevant information of a material nature which relate to the profit and loss and the financial position of the business. This enables the users of the financial statements to make correct assessment about the profitability and financial soundness of the enterprise. It is, therefore, necessary that the disclosure should be full, fair and adequate.
4. **Materiality Concept** : This concept is closely related to the Full Disclosure Concept. Full disclosure does not mean that everything should be disclosed. It only means that all relevant and material information must be disclosed. Materiality primarily relates to the relevance and reliability of information. An item is considered material if there is a reasonable expectation that the knowledge of it would influence the decision of the users of the financial statements. All such material information should be disclosed through the financial statements and the accompanying notes. For example, commission paid to sole selling agents, if any, should be disclosed separately in the Profit and Loss Account. Similarly, if there is a change in the method or rate of depreciation, this fact must be duly reported in the financial statements.

A strict adherence to accounting principles is not required for items of little significance or of non-material nature. For example, erasers, pencils, scales, etc., are used for a long period, but they are not treated as assets. They are treated as expenses. This does not affect the amount of profit or loss materially.

Similarly, while showing the amounts of various items in the financial statements, they can be approximated up to paise. Even if they are shown to the nearest rupee or hundreds, there may not be any material effect. For example, if an amount of ₹ 2,45,923.28 is shown as ₹ 2,45,900 it does not make much difference for assessment of the performance of the enterprise.

Q.7. What is Journal? What are the steps in journalising?**Ans.****Journal**

A Journal is called a book of prime entry (also called book of original entry) because all business transactions are entered first in this book. The word 'Journal' means a daily record. The transactions are recorded in this book in the order in which they occur i.e., they are entered in a chronological order. In this book, both aspects i.e., the receiving aspect and the giving aspect of the transaction, are recorded. The process of recording a transaction in the journal is called Journalising. The entries made in the journal are called 'journal entries'.

Steps in Journalising

In recording various business transactions in the journal, the most important aspect is the entry in the 'Particulars' column. Any mistake in this regard would lead to incorrect accounting. Hence, you should analyse the transaction carefully before making such entries. The following steps shall help you do such analysis:

1. Take up the transaction, one by one. Read and analyse the transaction carefully from the business entity point of view, and identify the two accounts that are being affected by the transaction.
2. You are aware that accounts have been classified as personal, real and nominal accounts. Hence, after identifying the two accounts that are affected by the transaction, you must determine, in respect of each account, whether it is a personal account or a real account or a nominal account.
3. Each class of account has its own rule of debit and credit, which you have already learnt. Now, apply the relevant rules and decide which account is to be debited and which is to be credited.

The three steps explained above will have to be repeated in respect of every transaction. We have simply reinforced the point here to help you journalise correctly.

Besides identifying the accounts to be debited and credited, you should be equally careful about the date of the transaction and the amounts with which each account is to be debited or credited. Now let us take a transaction, analyse it and see how a complete journal entry will be made.

Sold goods to Saran Brothers on credit for ₹ 500 on January 3, 2018

Step 1: From the business point of view, it is a sale of goods on credit. In this case, the receiving aspect is Saran Brothers (as they receive the goods) and the giving aspect is Goods (as goods go out). So, the two accounts affected are 'Saran Brothers' Account' and 'Goods Account'.

Step 2: The next step is to classify the accounts identified in the step 1. You are aware that Saran Brothers' Account is a personal account because it relates to persons, and Goods Account is a real account as it relates to property of the business.

Step 3: The rule for personal accounts is 'debit the receiver and credit the giver'. Saran Brothers receive the goods. So Saran Brothers' Account will be 'debited'. The rule for real accounts is 'debit what comes in and credit what goes out'. Goods go out of business. So, Goods Account will be credited.

Having identified that Saran Brothers' Account is to be debited and Goods Account is to be credited, the entry will be recorded in the journal as follows:

Date	Particulars	L.F.	Dr. Amount (₹)	Cr. Amount (₹)
2018 Jan. 3	Saran Brothers To Goods Account (Being goods sold on credit)	Dr. —	500	500

Q.8. Arnab commenced business on January 1, 2022. His transactions for the month are given below. Journalise them.

2022		(₹)
Jan. 1	Commenced business with a capital of	1,50,000
Jan. 2	Bought goods from Ajeet & Co.	35,000
Jan. 3	Sold goods for cash	6,000
Jan. 4	Purchased furniture	6,000
Jan. 7	Purchased goods on account from Gautam & Co.	18,000
Jan. 8	Returned goods to Gautam & Co.	600
Jan. 8	paid for advertisement	1,000
Jan. 10	Cash sales	5,000
Jan. 13	Sold goods to Venkat	6,000
Jan. 14	Venkat returns goods	400
Jan. 19	Paid Ajeet and Co. on account	18,000
Jan. 25	Paid office expenses	300
Jan. 26	Received from Venkat on account	3,000
Jan. 31	paid salaries	5,000
Jan. 31	Drew cash for private expenses	3,000

Sol. Journal

Date	Particulars	L.F.	Dr. Amount (₹)	Cr. Amount (₹)
2022 Jan. 1	Cash Account To Capital Account (Being capital bought in)	Dr.	1,50,000	1,50,000
Jan. 2	Purchase Account To Ajeet and Co's Account (Being credit purchase)	Dr.	35,000	35,000
Jan. 3	Cash Account To Sales Account (Being cash sales)	Dr.	6,000	6,000
Jan. 4	Furniture Account To Cash Account (Being furniture purchased)	Dr.	8,000	8,000

Jan. 7	Purchase Account To Gautam & Co's Account (Being credit Purchase)	Dr.	18,000	18,000
Jan. 8	Gautam & Co's Account To Returns Outwards Account (Being goods returned to Gautam & Co.)	Dr.	600	600
Jan. 8	Advertisement Account To Cash Account (Being payment, for advertisement)	Dr.	1,000	1,000
Jan. 10	Cash Account To Sales Account (Being cash sales)	Dr.	5,000	5,000
Jan. 13	Venkat's Account To Sales Account (Being credit sales)	Dr.	6,000	6,000
Jan. 14	Returns Inwards Account To Venkat's Account (Being goods returned by Venkat)	Dr.	400	400
Jan. 19	Ajeet & Co's Account To Cash Account (Being cash paid on account)	Dr.	18,000	18,000
Jan. 25	Office Expenses Account To Cash Account (Being office expenses)	Dr.	300	300
Jan. 26	Cash Account To Venkat's Account (Being cash received on account)	Dr.	3,000	3,000
Jan. 31	Salaries Account To Cash Account (Being salaries paid)	Dr.	5,000	5,000
Jan. 31	Drawing Accounts To Cash Account (Being cash withdrawn for personal use)	Dr.	3,000	3,000

Q.9. Enter the following transactions in the journal:

2022

- April 1 Bought an almirah for ₹ 450, and paid ₹ 30 for cartage.
 April 2 Proprietor took away goods worth ₹ 200 for personal use.
 April 3 Gave goods worth ₹ 100 in charity.
 April 4 Sold an old machine for ₹ 2,000.

- April 5 Paid insurance premium ₹ 90.
 April 6 Purchased goods worth ₹ 5,000 for cash less 20 trade discount.
 April 7 Received ₹ 980 from Kisan Chand, and allowed him ₹ 20 cash discount.
 April 8 ₹ 500 were due to Ghanshyam. Paid ₹ 480 in full settlement of his account.
 April 9 Cash of ₹ 560 was stolen from the cash box.
 April 10 Han Singh, a debtor became insolvent. He owed ₹ 400. A final composition of 50 paise in a rupee was received.
 April 11 Sold goods to Karim ₹ 800.
 April 12 Paid into bank ₹ 400.

Sol.

Journal

Date	Particulars	L.F.	Dr. Amount (₹)	Cr. Amount (₹)
2022				
June 1	Furniture A/c To Cash A/c (Being purchase of an almirah for ₹ 450, Cartage paid ₹ 30)	Dr.	480	480
June 2	Drawings & A/c To Purchase A/c (Being goods taken away by the proprietor for personal use).	Dr.	200	200
June 3	Charity A/c To Purchase A/c (Being goods given in charity)	Dr.	100	100
June 4	Cash A/c To Machinery A/c (Being sale of old machinery)	Dr.	2,000	2,000
June 5	Insurance A/c To Cash A/c (Being payment of insurance premium)	Dr.	90	90
June 6	Purchase A/c To Cash A/c (Being purchase of goods)	Dr.	4,000	4,000
June 7	Cash A/c Discount Allowed A/c To Kishan Chand (Being cash received from him, discount allowed ₹ 20)	Dr. Dr.	980 20	1000
June 8	Ghanshyam To Cash A/c To Discount Received A/c (Being cash paid to him, discount received ₹ 20)	Dr.	500	480 20

June 9	Loss by Theft A/c	Dr.	560	
	To Cash A/c (Being loss by theft)			560
June 10	Cash A/c	Dr.	200	
	Bad Debts A/c	Dr.	200	
	To Hari Singh			400
	(Being cash received from him, discount allowed ₹ 20)			
June 11	Karim	Dr.	800	
	To Sales A/c			800
	(Being credit sales)			
June 12	Bank A/c	Dr.	400	
	To Cash (Being cash paid into bank)			400
			10,530	10,530

Q.10. Prepare a Trial Balance from the following balances taken from the books of Ankush Jha Ji on March 31, 2021 :

	(₹)		(₹)
Capital	1,80,000	Discount Received	360
Stock (1-4-2020)	49,200	Bills Payable	12,270
Sales	2,43,600	Sundry Creditors	31,110
Gas & Water	2,520	Returns Outwards	19,200
Land & Buildings	60,000	Bank Charges	3,000
Machinery	55,470	Drawings	14,550
Debtors	1,07,400	Trade Expenses	2,970
Commission (Dr.)	4,410	Cash	2,400
Plant	30,810	Bank	15,780
Carriage	3,370	Purchases	96,480
Rent Received	1,290	Rates & Taxes	2,520
Insurance	3,180	Furniture	3,750
Returns Inwards	5,970	Bills Receivable	4,410
Salaries	19,640		

Sol. Trial Balance as on March 31, 2021

Name of Account	L.F.	Dr. Balances (₹)	Cr. Balances (₹)
Capital		—	1,80,000
Stock (1-4-2020)		49,200	—
Sales		—	2,43,600
Gas and Water		2,520	—
Land & Buildings		60,000	—
Machinery		55,470	—
Debtors		1,07,400	—
Commission (Dr.)		4,410	—

Plant	30,810	—
Carriage	3,370	—
Rent Received	—	1,290
Salaries	19,640	—
Insurance	3,180	—
Returns Inwards	5,970	—
Discount Received	—	360
Bills Payable	—	12,270
Sundry Creditors	—	31,110
Returns Outwards	—	19,200
Bank Charges	3,000	—
Drawings	14,550	—
Trade Expenses	2,970	—
Cash	2,400	—
Bank	15,780	—
Purchases	96,480	—
Rates & Taxes	2,520	—
Furniture	3,750	—
Bills Receivable	4,410	—
Total	4,87,830	4,87,830

Q.11. Explain the concept of double entry system. Also explain its merits and demerits.

Ans.

Concept of Double Entry System

There are many systems of presenting business transactions in accounting books e.g., Maha-jani system, Cash system, Double entry system, etc. The use of these systems depends upon the size and type of business and nature of transactions. But in modern business world, double entry system of book-keeping is more popular and widely used. The focus of the double entry system is that every business transaction has two aspects, i.e., when we receive something, we give something else in return. This approach of writing both the aspects of the transactions is known double entry system of accounting. Of the two accounts one account is given debit while the other is given credit with an equal amount. Thus, on any date the debits must be equal to the credits.

Evolution of Double Entry System

The double entry system was originated in Italy in 15th century. First of all in 1494 Lucas Pacioli, the famous mathematician of Venice of Venice city of Italy wrote his first book "De Computiset Scripturise" and mentioned method of accounting in one of its part. Emphasis was given on division and utility of waste book. Journal, Ledger, etc. In 1543 Hume Old Castle translated it in English and after that many learned persons showed their views and gave it a new shape.

The following are the three distinct stages of a complete system of double entry :

- Recording the transactions in the journal.
- Classifying the transactions in the journal by posting them to the appropriate ledger accounts and then preparing a trial balance.
- Closing the books and preparing the final accounts.

Merits of Double Entry System

1. **Full description** : Every financial transaction is recorded in two related accounts separately in which full particulars are given for each transaction.
2. **Knowledge of some important information regarding business** : In Double entry system, real and nominal accounts are also maintained together with personal accounts. The information about capital employed, assets and liabilities can be obtained easily.
3. **Testing of Mathematical Accuracy** : Under this system, each debit entry has a credit entry due to which arithmetical accuracy can be checked with the help of trial balance.
4. **Less chances of fraud** : Under this system, double entry of each transaction reduces the possibility of forgery and fraud. Fraud can be avoided and traced easily.
5. **Information of Profit and Loss** : Under this system, profit and loss account is prepared at the end of the certain period to find profit and loss.
6. **Knowledge of Economic Status** : With the help of balance sheet, the economic and financial status of the business can be obtained easily.
7. **Comparatively Study and useful results** : Trading, profit and loss account and balance sheet of current year can be compared with trading, profit & loss account and balance sheet of previous year to obtain useful analysis and conclusions.

Demerits of Double Entry System

1. It is difficult to follow the rules of debit and credit in this system.
2. Though this system is fully scientific even then there are chances of errors and mistakes.
3. It is necessary to follow the principles and even a small mistake may give erroneous results.
4. It is an expensive system for small traders.
5. In order to get full efficiency in the system, it is necessary to have education, training and practical knowledge of accounts.

Q.12. Journalise the following transactions, post them into ledger, balance the accounts and prepare a Trial Balance.

2017		(₹)
March 1	Shyam Sunder & Sons commenced business with cash	80,000
March 2	Purchased goods for cash	36,000
March 3	Machinery purchased for cash	4,000
March 4	Purchased goods from: Raghu	22,000
	Dilip	30,000
March 6	Returned goods to Raghu	4,000
March 8	Paid to Raghu in full settlement of his account	17,500
March 10	Sold goods to Mahesh Chand & Co. for ₹ 32,000 at 5% trade discount	
March 13	Received cash from Mahesh Chand & Co.	19,800
	Discount allowed	200

March 15	Paid cash to Dilip	14,850
	Discount received	150
March 20	Sold goods for cash	25,000
March 24	Sold goods for cash to Sudhir Ltd.	18,000
March 25	Paid for Rent	1,500
March 26	Received for Commission	2,000
March 28	Withdrew by Proprietor for his personal use	5,000
March 28	Purchased a fan for Proprietor's house	1,200

Sol.

Journal
In the Books of ...

Date	Particulars	L.F.	Dr. Amount (₹)	Cr. Amount (₹)
2017				
Mar. 01	Cash A/c Dr. To Capital A/c (Business started with cash)		80,000	80,000
Mar. 02	Purchase A/c Dr. To Cash A/c (Goods purchased for cash)		36,000	36,000
Mar. 03	Machinery A/c Dr. To Cash A/c (Machinery purchased for cash)		4,000	4,000
Mar. 04	Purchases A/c Dr. To Raghu's A/c To Dilip's A/c (Goods purchased on credit from Raghu and Dilip)		52,000	22,000 30,000
Mar. 06	Raghu's A/c Dr. To purchases Return A/c (Goods returned to Raghu)		4,000	4,000
Mar. 08	Raghu's A/c Dr. To Cash A/c To Discount Received A/c (Cash paid to Raghu in full settlement)		18,000	17,500 500
Mar. 10	Mahesh Chand & Co. Dr. To Sales A/c (Goods sold to Mahesh Chand & Co. at trade discount)		30,400	30,400
Mar. 13	Cash A/c Dr. Discount Allowed A/c To Mahesh Chand & Co. (Cash received from Mahesh Chand & Co.)		19,800 200	20,000

Mar. 15	Dilip's A/c To Cash A/c To Discount Received A/c (Cash paid to Dilip)	Dr.	15,000	14,850 150
Mar. 20	Cash A/c (Goods sold for cash)	Dr.	25,000	25,000
Mar. 24	Cash A/c To Sales A/c (Goods sold for cash)	Dr.	18,000	18,000
Mar. 25	Rent A/c To Cash A/c (Rent paid)	Dr.	1,500	1,500
Mar. 26	Cash A/c To Commission A/c (Commission received)	Dr.	2,000	2,000
Mar. 28	Drawings A/c To Cash A/c (Cash withdrawn and fan purchased for personal use)		6,200	6,200
	Total		3,12,100	3,12,100

Dr.				Cr.			
Cash Account							
Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 01	Capital A/c		80,000	Mar. 02	Purchases A/c		36,000
Mar. 13	Mahesh Chand & Co.		19,800	Mar. 03	Machinery A/c		4,000
Mar. 20	Sales A/c		25,000	Mar. 08	Raghu's A/c		17,500
Mar. 24	Sales A/c		18,000	Mar. 15	Dilip's A/c		14,850
Mar. 26	Commission A/c		2,000	Mar. 25	Rent A/c		1,500
				Mar. 28	Drawings A/c		6,200
				Mar. 31	Balance c/d		64,750
			1,44,800				1,44,800
2017							
Apr. 01	Balance b/d		64,750				

Dr.				Cr.			
Capital Account							
Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 31	Balance c/d		80,000	Mar. 01	Cash A/c		80,000
			80,000				80,000
				2017			
				Apr. 01	Balance b/d		80,000

Dr. Purchase Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 02	Cash A/c		36,000	Mar. 31	Balance c/d		88,000
Mar. 04	Raghu's A/c		22,000				
	Dilip's A/c		30,000				
			88,000				88,000
2017							
Apr. 01	Balance b/d		88,000				

Dr. Machinery Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 03	Cash A/c		4,000	Mar. 31	Balance c/d		4,000
			4,000				4,000
2017							
Apr. 01	Balance b/d		4,000				

Dr. Raghu's Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 06	Purchases Return A/c		4,000	Mar. 04	Purchases A/c		22,000
Mar. 08	Cash A/c		17,500				
	Discount Received A/c		500				
			22,000				22,000

Dr. Dilip's Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 15	Cash A/c		14,850	Mar. 04	Purchases A/c		30,000
Mar. 15	Discount Received A/c		150				
Mar. 31	Balance c/d		15,000				
			30,000				30,000
				2017			
				Apr. 01	Balance b/d		15,000

Dr. Purchase Return Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 31	Balance c/d		4,000	Mar. 06	Raghu's A/c		4,000
			4,000				4,000
				2017			
				Apr. 01	Balance b/d		4,000

Dr. Discount Received Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 31	Balance c/d		650	Mar. 08	Raghu's A/c		500
			650	Mar. 15	Dilip's A/c		150
							650
				2017			
				Apr. 01	Balance b/d		650

Dr. Discount Allowed Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 13	Mahesh Chand & Co.		200	Mar. 31	Balance c/d		200
			200				200
2017							
Apr. 01	Balance b/d		200				

Dr. Mahesh Chand & Co. Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017				2017			
Mar. 10	Sales A/c		30,400	Mar. 13	Cash A/c		19,800
			30,400		Discount Allowed A/c		200
				Mar. 13	Balance c/d		10,400
							30,400
2017							
Apr. 01	Balance b/d		10,400				

Dr. Rent Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017 Mar. 25	Cash A/c		1,500	2017 Mar. 31	Balance c/d		1,500
			1,500				1,500
2017 Apr. 01	Balance b/d		1,500				

Dr. Commission Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017 Mar. 31	Balance c/d		2,000	2017 Mar. 26	Cash A/c		2,000
			2,000				2,000
				2017 Apr. 01	Balance b/d		2,000

Dr. Drawings Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017 Mar. 28	Cash A/c		6,200	2017 Mar. 31	Balance c/d		6,200
			6,200				6,200
				2017 Apr. 01	Balance b/d		6,200

Dr. Sales Account Cr.

Date	Particulars	J.F.	Amount (₹)	Date	Particulars	J.F.	Amount (₹)
2017 Mar. 31	Balance c/d		73,400	2017 Mar. 10	Mahesh Chand & Co.		30,400
				Mar. 20	Cash A/c		25,000
				Mar. 24	Cash A/c		18,000
			73,400				73,400
				2017 Apr. 01	Balance b/d		73,400

Trial Balance
as on March 31, 2017

Name of Accounts	L.F.	Dr. Balances Amount (₹)	Cr. Balances Amount (₹)
Cash A/c		64,750	
Capital A/c			80,000
Purchases A/c		88,000	

Machinery A/c		4,000	
Dilip's A/c			15,000
Purchases return A/c			4,000
Discount Received A/c			650
Discount Allowed A/c		200	
Mahesh Chand & Co.			
Rent A/c		10,400	
Commission A/c		1,500	2,000
Drawings A/c		6,200	
Sales A/c			73,400
Total		1,75,050	1,75,050

Q.13. From the following trial balance of M/s Kaushal Traders, prepare Trading and Profit and Loss Account for the year ended 31st March, 2012 and a Balance Sheet as on that date:

Dr. Balances	(₹)	Cr. Balances	(₹)
Opening stock on 1st April, 2011	16,000	Capital	80,000
Purchases	75,000	Sales	2,00,000
Sales returns	5,000	Purchases returns	2,000
Carriage inwards	1,500	Discount	500
Plant and Machinery	40,000	Sundry creditors	10,000
Furniture and fixtures	5,000	Bills payable	1,500
Freehold property	45,650		
Cash in hand	5,000		
Carriage outwards	400		
Wages	30,000		
Salaries	18,000		
Lighting (factory)	800		
Sundry debtors	28,000		
Travelling expenses	1,200		
Rent and taxes	4,800		
Drawings	5,000		
Insurance	450		
General expenses	12,200		
	2,94,000		2,94,000

Adjustments:

- (i) Stock on 31st March 2012 was valued at ₹ 38,000 (market value ₹ 20,000).
- (ii) Wages amounting to ₹ 2,000 and salaries amounting to ₹ 1,500 are outstanding.
- (iii) Prepaid insurance amounted to ₹ 150.
- (iv) Provide depreciation on plant and machinery at 5% and on furniture and fixtures at 10%

Sol. Trading and Profit and Loss AccountDr. *for the year ending 31st March, 2012* Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
To Opening stock	16,000	By Sales	2,00,000
To Purchase	75,000	<i>Less : Sales returns</i>	<u>5,000</u>
<i>Less : Purchase returns</i>	<u>2,000</u>	By Closing stock	20,000
To Carriage inwards	1,500		
To Wages	30,000		
<i>Add : Outstanding wages</i>	<u>2,000</u>		
To Factory lighting	800		
To Gross profit c/d	91,700		
	2,15,000		2,15,000
To carriage outwards	400	By Gross profit b/d	91,700
To Salaries	18,000	By Discount	500
<i>Add : Outstanding salaries</i>	<u>1,500</u>		
To Travelling expenses	1,200		
To Rent and taxes	4,800		
To Insurances	450		
<i>Less : Prepaid insurance</i>	<u>150</u>		
To General expenses	12,200		
To Depreciation on:			
Plant and machinery	2,000		
Furniture and fixtures	<u>500</u>		
To Net profit transferred to Capital A/c	51,300		
	92,200		92,200

Balance Sheet*as on 31st March, 2012*

Liabilities	Amount (₹)	Assets	Amount (₹)
Bills payable	1,500	Cash in hand	5,000
Sundry creditors	10,000	Sundry debtors	28,000
Outstanding wages	2,000	Closing stock	20,000
Outstanding salaries	1,500	Prepaid insurance	150
Capital	80,000	Furnitures and fixtures	5,000
<i>Add : Net profit</i>	<u>51,300</u>	<i>Less : Depreciation</i>	<u>500</u>
	1,31,000	Plant and machinery	40,000
<i>Less : Drawings</i>	<u>5,000</u>	<i>Less : Depreciation</i>	<u>2,000</u>
	1,26,300	Freehold property	45,650
	1,41,300		1,41,300

Note : Closing stock is valued at cost price or market price whichever is less.

□

UNIT-II

Hire-Purchase Accounts and Instalment Payment System

SECTION-A VERY SHORT ANSWER TYPE QUESTIONS

Q.1. Define the term 'Hire-purchase system.'

Ans. Hire-purchase is the system under which the property is acquired by payments made in instalments, during the period of which the title in the property remains with the Hire Vendor. The payments prior to the final are regarded as being purely in respect of hire, and the title of the property does not pass to the hire-purchaser until such final payment or some other consideration provided for in the contract has been fulfilled. "In the case of Hire-purchase Agreements the property in the goods does not pass to the buyer until all the instalments have been paid. Each hire-purchase instalment represents a payment on account of the cash value of the goods plus interest on the outstanding balance of the cash value.

Q.2. Explain the following terms:

(i) Cash price

(ii) Hire-purchase

(iii) Instalment

Ans. (i) **Cash Price** : It is the amount for which the goods or asset can be purchased. It does not include the amount of interest.
(ii) **Hire-Purchase Price** : It is the total amount which the hire-purchaser is liable to pay for taking the ownership of goods or asset. This amount includes interest. It is always higher than the cash price amount.
(iii) **Instalment** : Hire-purchase price of goods or asset is paid in several instalments. Each instalment may include interest or not. After paying all instalments the hire-purchaser, becomes the owner of the asset.

Q.3. What are necessary accounts in hire-purchase system?

Ans. In Hire-purchase System necessary accounts include the following accounts in the books of hire-purchase or vendor.

1. **In the Books of Vendor:**

- (i) Hire-purchaser's Account
- (ii) Interest Account

2. **In the Books of Hire-purchaser:**

- (i) Asset Account
- (ii) Vendor's Account
- (iii) Interest Account
- (iv) Depreciation Account

Q.4. What is meant by 'Instalment payment system'?

Ans. Though hire-purchase and instalment system appear similar from outside because under both the systems, payment is made to the seller in instalments, but there is vast difference between the two. First system is a hire transaction which takes the form of a sale at the end, second method (Instalment Payment System) is a transaction of immediate sale; under this system instead of making payment in a lump sum, payment is made during a prescribed period by instalments and provision is made for payment of interest also. Instalment Payment System is such a system of sale in which property in goods or ownership is immediately transferred to the buyer at the time of sale and sale price is paid in instalments along with the amount of interest on unpaid balance. On default of payment of any instalment, seller is not entitled to take back the goods, but he may file a suit for the amount due.

Q.5. Discuss the main features of Instalment payment system.

Ans. Characteristics of the Instalment Payment System are as follows :

1. Under this system goods are sold and delivery is also made to the buyer, but its full price is not paid at the time of sale, therefore, this sale is like credit sale.
2. Payment of purchase price is made in agreed instalments.
3. Ownership is transferred to the buyer immediately at the time of sale.
4. On making default in payment of instalment, seller cannot take back the goods, he can only file a suit for the amount due.
5. If buyer sells these goods before payment of the last instalment to the third party, third party gets better title.

Q.6. Differentiate between hire-purchase and credit sales.

Ans. **Distinction between Hire-purchase and Credit Sales**

Basis	Hire-Purchase	Credit Sale
Transfer of Ownership	Ownership is transferred after payment of the last instalment.	Ownership is transferred at the time of purchase.
Method of Payment	Payment of price is always made by instalments.	Payment of price is generally made in a lump sum but it can be made otherwise also according to the agreement.
Right of Return of Goods	If default is made in payment of instalments, Seller can take back the goods as per legal requirements.	On default in payment, Seller cannot take back the goods but can file a suit for recovery of the price.
Better title	If Buyer sells the goods before payment of the last instalment, this new buyer does not get better title than the purchaser under credit purchase.	If Buyer sells goods before payment of full purchase price, the new buyer gets better title than the Hire-purchaser.

SECTION-B (SHORT ANSWER TYPE) QUESTIONS

Q.1. Discuss the features of Hire-purchase agreement.

Ans. Following are the main features of Hire-Purchase agreement:

1. It must be in writing and must be signed by all the parties thereto (Section 3).
2. According to Section 4 of Hire Purchases Act, 1972, the agreement must state :
 - (i) the hire purchase price of the goods to which the agreement relates;

- (ii) the cash price of the goods, that is to say, the price at which the goods may be purchased by the hirer for cash;
- (iii) the date on which the agreement shall be deemed to have commenced;
- (iv) the number of instalments by which the hire purchase price is to be paid, the amount of each of those instalments and the date (the mode of determining the date upon which it is payable) and the person to whom and the place where it is payable; and
- (v) the goods to which the agreement relates, in a manner sufficient to identify them.

Q.2. Discuss the accounting records in the books of the purchaser when the asset is recorded at cash price actually paid.

Ans. You know that in case of hire purchase, the ownership of the goods passes to the hire purchaser after the last instalment has been paid. Since the goods do not become the property of the purchaser, he does not have any right to debit the asset at its full price. Hence, no entry is passed when the asset is purchased unless it involves down payment. The entries are passed as and when the instalments become due and the amount is paid towards the price of the article. The journal entries are as follows :

1. When the asset is purchased

No entry

2. When the down payments is made

Asset A/c	Dr.
To Bank A/c	

3. When the instalment becomes due

Asset A/c	Dr. (cash price part of instalment)
Interest A/c	Dr. (interest on instalment)
To Hire Vendor	

4. When instalment is paid

Hire Vendor	Dr.
To Bank A/c	

5. When depreciation is charged

Depreciation A/c	Dr.
To Asset A/c	

6. When interest and depreciation accounts are closed by transfer to Profit & Loss A/c

Profit & Loss A/c	Dr.
To Interest A/c	
To Depreciation A/c	

It should be noted that though the asset account is debited with the amount of the cash price paid (not full cash price), the depreciation is charged on the full cash price. The Balance Sheet will reflect the amount of cash price debited to the asset account minus depreciation charged.

Q.3. Discuss the accounting records in the books of Vendor in a hire-purchase sale.

Ans. **Accounting Records in the Books of Vendor**

So far as the vendor is concerned, a hire purchase sale is just like an ordinary sale with the exception that payment is deferred over a period of time for which the vendor charged

interest. He debits the Hire Purchaser's A/c with full cash price and credit is given to Sales A/c. The interest amount is debited to Hire Purchaser's A/c as and when the instalments become due. Instalment amounts received are credited to the Hire Purchaser's A/c and debited to Bank A/c. The journal entries passed are as follows:

1. On sale of goods under hire purchase

Hire Purchaser	Dr.
To Sales A/c	(with full cash price)

2. On receiveing cash price down payment

Bank A/c	Dr.
To Hire Purchaser A/c	

3. On instalment becoming due

Hire Purchaser A/c	Dr.
To Interest A/c	

4. On getting payment on the due instalment

Bank A/c	Dr.
To Hire Purchaser A/c	

With the help of above entries, you can easily prepare the Hire Purchaser's A/c and Interest A/c.

Q.4. The cash price of a machine is ₹ 37,400 on 1st April, 2016. Its hire-purchase price is ₹ 50,000. This hire-purchase price is paid in five annual instalments in the following manner: ₹ 15,000 at the end of first year, ₹ 12,000 at the end of second year; ₹ 10,000 at the end of third year; ₹ 8000 at the end of fourth year; ₹ 5000 at the end of fifth year. Prepare Hire-Vendor's Account in the books of Hire-Purchaser A.

Sol. Calculation of Interest

$$₹ 50,000 - ₹ 37,400 = ₹ 12,600 \text{ (Interest)}$$

Instalment No.	Unpaid Amount (₹)	Calculation of Interest	Instalment-Interest = Cash Price (₹)
1st	50,000	$\frac{12,600 \times 50,000}{1,26,000} = ₹ 5,000$	15,000 – 5,000 = 10,000
2nd	50,000 – 15,000 = 35,000	$\frac{12,600 \times 35,000}{1,26,000} = ₹ 3,500$	12,000 – 3,500 = 8,500
3rd	35,000 – 12,000 = 23,000	$\frac{12,600 \times 23,000}{1,26,000} = ₹ 2,300$	10,000 – 2,300 = 7,700
4th	23,000 – 10,000 = 13,000	$\frac{12,600 \times 13,000}{1,26,000} = ₹ 1,300$	8,000 – 1,300 = 6,700
5th	13,000 – 8,000 = 5,000	$\frac{12,600 \times 5,000}{1,26,000} = ₹ 500$	5,000 – 500 = 4,500
	₹ 1,26,000		50,000 – 12,600 = 37,400

In A'S Books
Hire-Vendor's Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017			2017		
Mar. 31	To Bank A/c	15,000	Mar. 31	By Machine A/c	10,000
		15,000	Mar. 31	By Interest A/c	5,000
					15,000
2018			2018		
Mar. 31	To Bank A/c	12,000	Mar. 31	By Machine A/c	8,500
		12,000	Mar. 31	By Interest A/c	3,500
					12,000
2019			2019		
Mar. 31	To Bank A/c	10,000	Mar. 31	By Machine A/c	7,700
		10,000	Mar. 31	By Interest A/c	2,300
					10,000
2020			2020		
Mar. 31	To Bank A/c	8,000	Mar. 31	By Machine A/c	6,700
		8,000	Mar. 31	By Interest A/c	1,300
					8,000
2021			2021		
Mar. 31	To Bank A/c	5,000	Mar. 31	By Machine A/c	4,500
		5,000	Mar. 31	By Interest A/c	500
					5,000

Q.5. One machine whose cash price is ₹ 81,800 is purchased for ₹ 90,000 on Hire-Purchase System Payment of Hire-Purchase Price is made after the date of purchase in the following manner. At the end of 4 months ₹ 10,000; at the end of 6 months ₹ 15,000; at the end of 9 months ₹ 30,000; at the end of 12 months ₹ 35,000.

Machine is purchased on 1st April 2020 and the date of payment of each instalment is counted from this date. Open the Hire-Purchaser's Account in the books of Hire-Vendor, showing the balance left after payment of each instalment.

Sol.

Calculation of Interest

$$₹ 90,000 - ₹ 81,800 = ₹ 8,200 \text{ (Interest)}$$

	Period	Amount Unpaid (₹)	Product (₹)	Calculation of Interest (₹)	Instalment- Interest = Cash Price (₹)
1	4 Months	90,000	$90,000 \times 4 = 3,60,000$	$8,200 \times \frac{3,60,000}{8,20,000} = 3,600$	$10,000 - 3,600 = 6,400$
2	6 - 4 = 2 Months	$90,000 - 10,000 = 80,000$	$80,000 \times 2 = 1,60,000$	$8,200 \times \frac{1,60,000}{8,20,000} = 1,600$	$15,000 - 1,600 = 13,400$

3	9 - 6 = 3 Months	80,000 - 15,000 = 65,000	65,000 × 3 = 1,95,000	$8,200 \times \frac{1,95,000}{8,20,000} = 1,950$	30,000 - 1,950 = 28,050
4	12 - 9 = 3 Months	65,000 - 30,000 = 35,000	35,000 × 3 = 1,05,000	$8,200 \times \frac{1,05,000}{8,20,000} = 1,050$	35,000 - 1,050 = 33,950
			8,20,000		90,000 - 8,200 = 81,800

₹ 3,60,000 + 1,60,000 + 1,95,000 + 1,05,000 = ₹ 8,20,000

In the Books of Hire-Vendor Hire Purchaser's Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2020			2020		
Apr. 1	To Hire Sales A/c	81,000	July 31	By Bank A/c	10,000
July 31	To Interest A/c	3,600	July 31	By Balance c/d	75,400
		85,400			85,400
2020			2020		
Aug 1	To Balance b/d	75,400	Sept 30	By Bank A/c	15,000
Sept. 30	To Interest A/c	1,600	Sept 30	By Balance c/d	62,000
		77,000			77,000
2020			2020		
Oct 1	To Balance b/d	62,000	Dec 31	By Bank A/c	30,000
Dec 31	To Interest A/c	1,950	Dec 31	By Balance c/d	33,950
		63,950			63,950
2021			2021		
Jan 1	To Balance b/d	33,950	Mar 31	By Bank A/c	35,000
Mar 31	To Interest A/c	1,050			
		35,000			35,000

Q.6. Differentiate between hire-purchase and instalment payment system.

Ans. Difference between Hire-purchase and Instalment Payment System

Basis	Hire-Purchase System	Instalment System
Nature of contract	It is like a contract of hire, though later on it becomes sale.	It is sale from the very beginning.
Transfer of ownership	Here ownership is transferred after the payment of the last instalment.	Here ownership is transferred in the beginning at the time of sale.
Return of Goods	On default of payment of instalment, seller has a right to take back the goods.	On default of payment of instalment, seller has no right to take back the goods from the buyer.
Better Title	If buyer sells goods to the third party before payment of the last instalment, this third party does not get better title on these goods.	If the buyer sells goods to the third party before the payment of the instalment, this third party gets better title on these goods.

Responsibilities of Normal Repair	Upto the time of payment of the last instalment responsibility of normal repair is on the seller because he continues to be the owner thereof.	Here seller is not at all responsible for the repair.
Bailee Risk	Here buyer is like a bailee. Upto the payment of last instalment risk is on the seller.	Here buyer is not like a bailee. Risk is not on the seller.

SECTION-C (LONG ANSWER TYPE) QUESTIONS

Q.1. On 1st April, 2018 a Railway Company buys on Hire-Purchase System from Hire-Vendor some Thelas for ₹ 25,500, payable by three equal instalments combining principal and interest, the latter being a normal rate of 5% per annum.

Calculate the amount of annual instalment, and show Hire-vendor's Account (under Asset Accrual Method) and Interest Account for three years in the Railway Company's Ledger. (The present value of an Annuity of one Rupee for three years at 5% is ₹ 2.72325).

Sol. **Finding out Cash Value of Thelas with the help of Annuity Rate**

The Present Value of Annuity of ₹ 1 paid for 3 years @ 5% = ₹ 2.72325.

The Present Value of Annuity of ₹ $\frac{25,500}{3}$ = ₹ 8,500.

₹ 2.72325 × 8,500 = ₹ 23,147.63

Calculation of Interest

Cost Price		(₹)
23,147.63		8,500.00
7,342.62	$\frac{23,147.63 \times 5}{100} = ₹ 1,157.38$	Interest 1,157.38
15,805.01		Thela 7,342.62
7,709.75	$\frac{15,805.01 \times 5}{100} = ₹ 790.25$	Interest 790.25
8,095.26	₹ 8,500 - ₹ 8,095.26 = ₹ 404.74 (Interest)	Thela 7,709.75

In Railway Company's Ledger Hire-Vendor's Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019			2019		
Mar. 31	To Cash A/c	8,500.00	Mar 31	By Thelas A/c	7,342.62
			Mar 31	By Interest A/c	1,157.38
		8,500.00			8,500.00

2020 Mar 31	To Cash A/c	8,500.00	2020 Mar 31	By Thehas A/c	7,709.75
		8,500.00	Mar 31	By Interest A/c	790.25
					8,500.00
2021 Mar 31	To Cash A/c	8,500.00	2021 Mar 31	By Thehas A/c	8,095.26
		8,500.00	Mar 31	By Interest A/c	404.74
					8,500.00

Interest Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019 Mar 31	To Hire-Vendor's A/c	1,157.38	2019 Mar 31	By Statement of P. & L.	1,157.38
2020 Mar 31	To Hire-Vendor's A/c	790.25	2020 Mar 31	By Statement of P. & L.	790.25
2021 Mar 31	To Hire-Vendor's A/c	404.74	2021 Mar 31	By Statement of P. & L.	404.74

Q.2. On 1st April, 2017 Ronak purchased a T.V. whose cash price was ₹ 66,244 from N.R. Ltd. on Hire-purchase System and it was decided that this amount will be paid in four equal annual instalments at 8% annual interest. The present value of an annuity of one rupee for 4 years at 8% is ₹ 3.3122. Calculate the amount of interest for each instalment and also prepare Hire Vendor's Account in the books of Ronak under Assets Accrual Method.

Sol. Calculation of Instalment Amount with Interest

Instalment amount = ₹ 66,244 ÷ 3.3122 = ₹ 20,000

Calculation of Interest

Cash Price (₹)	Interest	Instalment (₹)
66,244	$₹ 66,244 \times \frac{8}{100} = ₹ 5,300$	20,000
- 14,700		- 5,300 (Interest)
51,544	$₹ 51,544 \times \frac{8}{100} = ₹ 4,124$	14,700 (T.V.)
		20,000
- 15,876		- 4,124 (Interest)
35,668	$₹ 35,668 \times \frac{8}{100} = ₹ 2,853$	15,876 (T.V.)
- 17,147		20,000
18,521		- 2,853 (Interest)
		17,147 (T.V.)
	$₹ 20,000 - ₹ 18,521 = ₹ 1,479$	

**In the Books of Ronak
Account of N.R. Ltd.**

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2018		
Mar 31	To Bank A/c	20,000	Mar 31	By T.V. A/c	14,700
			Mar 31	By Interest A/c	5,300
		20,000			20,000
2019			2019		
Mar 31	To Bank A/c	20,000	Mar 31	By T.V. A/c	15,876
			Mar 31	By Interest A/c	4,124
		20,000			20,000
2020			2020		
Mar 31	To Bank A/c	20,000	Mar 31	By T.V. A/c	17,147
			Mar 31	By Interest A/c	2,853
		20,000			20,000
2021			2021		
Mar 31	To Bank A/c	20,000	Mar 31	By T.V. A/c	18,521
			Mar 31	By Interest A/c	1,479
		20,000			20,000

Calculation of Cash Price on the Basis of Back Calculation Method

When the amount of each instalment which includes interest is given and rate of interest is also given but the amount of cash price is not given then cash price is calculated in the following manner:

- (i) First of all find out cash price of the last instalment:

$$\text{Amount of last Instalment} \times \frac{\text{Rate of Interest}}{100 + \text{Rate of Interest}}$$

= Interest included in the last instalment.

This interest is deducted from last instalment and cash price of the last instalment is found out

- (ii) Cash price of the last instalment + Amount of prior Instalment $\times \frac{\text{Rate of Interest}}{100 + \text{Rate of Interest}}$
- = Interest of the prior Instalment;

When this interest is deducted from prior instalment, cash price of the prior instalment is found out.

- (iii) The same process may be repeated for earlier instalments.

Q.3. Sudhir purchased a machine whose cash price is ₹ 45,000 on 1st June 2019 on Hire-Purchase System. Its payment is to be made in 4 half-yearly instalments of ₹2,500 each. Rate of interest is 8% per annum. Machine was destroyed by an accident on 1st June, 2021 and Sudhir received ₹35,000 from Insurance Company. Depreciation is 10% per annum. It is calculated on fixed instalment method. Sudhir closes its books every year on 31st March. Open Accrued Interest Account, Machinery Account and Interest Account in the books of Sudhir.

Sol.

Calculations of Interest

(₹)		(₹)
45,000		12,500
- 10,700	$\frac{45,000 \times 4}{100} = ₹ 1,800$	- 1,800
		<u>10,700</u>
34,300		12,500
- 11,128	$\frac{34,300 \times 4}{100} = ₹ 1,372$	- 1,372
		<u>11,128</u>
23,172		- 12,500
- 11,573	$\frac{23,172 \times 4}{100} = ₹ 926.88$ or ₹ 927 Approx.	- 927
		<u>11,573</u>
11,599		
	₹ 12,500 - ₹ 11,599 = ₹ 901 (Interest)	

$8\% \times 1/2\% = 4\%$ as instalment are half yearly.

**In the Books of Sudhir
Hire-Vendor's Account**

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019			2019		
Nov 30	To Bank A/c	12,500	June 1	By Machine A/c	45,000
2020			Nov 30	By Interest A/c	1,800
Mar 31	To Balance c/d	34,300			<u>46,800</u>
		<u>46,800</u>			
2020			2020		
May 31	To Bank A/c	12,500	April 1	By Balance b/d	34,300
Nov 30	To Bank A/c	12,500	May 31	By Interest A/c	1,372
2021			Nov 30	By Interest A/c	927
Mar 31	To Balance c/d	11,599			<u>36,509</u>
		<u>36,509</u>			
2021			2021		
May 31	To bank A/c	12,500	April 1	By Balance b/d	11,599
			May 31	By Interest A/c	901
		<u>12,500</u>			<u>12,500</u>

Machinery Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019			2020		
June 1	To Hire-Vendor's A/c	45,000	Mar 31	By Depreciation A/c	

			Mar 31	(10 months) By Balance c/d	3,750 41,250
		45,000			45,000
2020			2021		
April 1	To Balance b/d	41,250	Mar 31	By Depreciation A/c	4,500
		41,250	Mar 31	By Balance c/d	36,750
					41,250
2021			2021		
April 1	To Balance b/d	36,750	May 31	By Depreciation A/c (for 2 months)	750
			June 1	By Cash A/c	35,000
			June 1	By P.&L. A/c	1,000
		36,750			36,750

Accrued Interest Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2020			2020		
Mar 31	To Balance c/d	914.67	Mar 31	By Interest A/c	914.67
2020			2020		
April 1	To Interest A/c	914.67	April 1	By Balance b/d	914.67
2021			2021		
Mar 31	To Balance c/d	600.67	Mar 31	By Interest A/c	600.67
		1,515.34			1,515.34
2021			2021		
April 1	To Interest A/c	600.67	April 1	By Balance b/d	600.67

Working Note :

1. $45,000 \times 10/100 \times 10/12 = ₹ 3,750$

2. $45,000 \times 10/100 \times 2/12 = ₹ 750$

3. $\frac{34,300 \times 8 \times 4}{100 \times 12} = ₹ 914.67;$

4. As ₹ 901 is interest for six months, hence interest for four months Dec, 2020 to March 2021 is $\frac{901 \times 4}{6} = ₹ 600.67.$

Interest Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019			2020		
Nov 30	To Hire-Vendor's A/c	1,800.00	Mar 31	By P & L. A/c	2,714.67
2020					
Mar 31	To Accrued Interest A/c	914.67			
		2,714.67			2,714.67

2020			2020		
May 31	To Hire Vendor's A/c	1,372.00	April 1	By Accrued Int. A/c	914.67
Nov 30	To Hire-Vednor's A/c	927.00			
2021			2021		
Mar 31	To Accrued Int. A/c	600.67	Mar 31	By P & L A/c	1,985.00
		2,899.67			2,899.67
2021			2021		
May 31	To Hire-Vendor's A/c	901.00	April 1	By Accrued Int A/c	600.67
			2022		
		901.00	Mar 31	By P.&L. A/c	300.33
					901.00

Note : Interest transferred to P. & L. A/c : First year 2,714.67 + Second year ₹ 1,985 + Third year ₹ 300.33 = ₹ 5,000. Total interest is also ₹ 5,000. $12,500 \times 4 = 50,000$ Hire-purchase price ₹ 50,000 – Cash price ₹ 45000 = ₹ 5000 int.

Q.4. Cash price of a machine is ₹ 3,000 and Hire-Purchase price is ₹ 4,000. This machine is sold on Hire-Purchase System on 1st April, 2019 to the Hire-Purchaser and payment is made in four six-monthly instalments of ₹ 1,000 each. It was agreed that the machine will be maintained free of charge for a period of two years. The actual expenses of maintenance were ₹ 100 and ₹ 250 for the first and second years respectively, though past experience showed that they are ₹ 500 of which ₹ 70 are for the first year. Pass the necessary Journal entries in the books of the Hire-Vendor and open the Hire-Maintenance Suspense Account.

Sol. **Calculation of Interest**

Sales Price ₹ 4,000 – Cash Price ₹ 3,000 = ₹ 1,000 interest

Instalment	Outstanding Instalment	Ratio	Interest
I	4	4/10	$\frac{1,000 \times 4}{10} = ₹ 400$
II	3	3/10	$\frac{1,000 \times 3}{10} = ₹ 300$
III	2	2/10	$\frac{1,000 \times 2}{10} = ₹ 200$
IV	1	1/10	$\frac{1,000 \times 1}{10} = ₹ 100$
	10		₹ 1,000

Journal Entries in the books of Hire-Vendor

Date	Particulars	L.F.	Amount (₹)	Amount (₹)
2019 Apr 1	Hire-Purchaser's A/c To Hire-Sales A/c (Being sales made)	Dr.	3,000	3,000

	Hire Sales A/c	Dr.	500	
	To Maintenance Suspense A/c (Being transfer made)			500
Sept 30	Hire-Purchaser's A/c	Dr.	400	
	To Interest A/c (Being interest for half year due)			400
	Bank A/c	Dr.	1,000	
	To Hire-Purchaser's A/c (Being receipt of instalment)			1,000
2020 Mar 31	Hire-Purchaser's A/c	Dr.	300	
	To Interest A/c (Being interest for half year due)			300
	Bank A/c	Dr.	1000	
	To Hire-Purchaser's A/c (Being receipt of second instalment)			1000
	Maintenance Suspense A/c	Dr.	100	
	To Bank A/c (Being actual expenses made)			100
	Profit & Loss A/c	Dr.	30	
	To Maintenance Suspense A/c (Being excess of actual maintenance over estimated)			30
	Interest A/c	Dr.	700	
	To Profit & Loss A/c (Being transfer of interest to Profit and Loss A/c)			700
	Hire Sales A/c	Dr.	2,500	
	To Trading A/c (Being transfer of balance of Hire Sales A/c to Trading A/c)			2,500
Sept 30	Hire-Purchaser's A/c	Dr.	200	
	To Interest A/c (Being interest for half year due)			200
	Bank A/c	Dr.	1,000	
	To Hire-Purchaser's A/c (Being receipt of instalment)			1,000
2021 Mar 31	Hire-Purchaser's A/c	Dr.	100	
	To Interest A/c (Being interest for half year due)			100
	Bank A/c	Dr.	1,000	
	To Hire-Purchaser's A/c (Being receipt of third instalment)			1,000
	Maintenance Suspense A/c	Dr.	250	
	To Bank A/c (Being payment of actual expenses of maintenance)			250

Mar 31	Maintenance Suspense A/c	Dr.	180	180
	To Profit & Loss A/c			
	(Being transfer of credit balance of Maintenance Suspense A/c to Profit and Loss A/c)			
	Interest A/c	Dr.	300	300
	To Profit & Loss A/c			
	(Being transfer of interest to Profit and Loss A/c)			

Working Note :

- ₹ 400 + ₹ 300 = ₹ 700;
- ₹ 3,000 – ₹ 500 for maintenance suspense = ₹ 2,500.
- ₹ 200 + ₹ 100 = ₹ 300;

Maintenance Suspense Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2020			2019		
Mar 31	To Cash A/c	100	Apr 1	By Hire Sales A/c	500
Mar 31	To Balance c/d	430	2020		
		530	Mar 31	By P.&L. A/c	30
					530
2021			2020		
Mar 31	To Cash A/c	250	Apr 1	By Balance b/d	430
Mar 31	To P.&L. A/c	180			
		430			430

Working Note :

Balance transfer to P&L A/c of Maintenance Suspense A/c = Real Expenditure incurred- Estimate expenditure

On 31-03-2020 = 100 – 70 = ₹ 30 Dr.

On 31-03-2021 = 430 – 250 = ₹ 180 Cr.

Q.5. On 1st April, 2017 X Ltd. purchased a wagon on hire-purchase system. According to agreement ₹5,000 were paid on delivery. Balance is payable in four annual instalments of ₹ 5,000 each. The first instalment falls on 31st March, 2018 Vendor, Anand Metal Works charges interest @ $2\frac{1}{2}$ % p.a. Vendor purchased the machine at ₹ 22,500 and the cash price was ₹ 23,810. You are required to prepare Hire-purchaser Account and Provision for Unrealised Profit for Account in the books of hire vendor.

Sol.**Calculation of Interest**

(₹)	Interest	Instalment		
		Cash Price (₹)	Interest (₹)	Total (₹)
23,810				
- 5,000	Down Payment	5000	—	5,000

18,810	$\frac{18,810 \times 5}{100 \times 2} = ₹ 470.25$	4,529.75	470.25	5,000
- 4,529.75				
14,280.25	$\frac{14,280.25 \times 5}{100 \times 2} = ₹ 357$	4,643	357	5,000
- 4,643.00				
9,637.25	$\frac{9,637.25 \times 5}{100 \times 2} = ₹ 240.93$	4,759.07	240.93	5,000
- 4759.07				
4,878.18	$5,000 - 4,878.18 = ₹ 121.82$	4,878.18	121.82	5,000

Hire-Purchase Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017			2017		
Apr 1	To Hire Sales A/c	23,810	Apr 1	By Bank A/c	5,000
2018			2018		
Mar 31	To Interest A/c	470.25	Mar 31	By Bank A/c	5,000
			Mar 31	By Balance c/d	14,280.25
		24,280.25			24,280.25
2018			2019		
Apr 1	To Balance b/d	14,280.25	Mar 31	By Bank A/c	5,000
2019			Mar 31	By Balance c/d	9,637.25
Mar 31	To Interest A/c	357			
		14,637.25			14,637.25
2019			2020		
Apr 1	To Balance b/d	9,637.25	Mar 31	By Bank A/c	5,000
2015			Mar 31	By Balance c/d	4,878.18
Mar 31	To Interest A/c	240.93			
2020		9,878.18			9,878.18
Apr 1	To Balance b/d	4,878.18	Mar 31	By Bank A/c	5,000
2021					
Mar 31	To Interest A/c	121.82			
		5,000			5,000

Provision for Unrealised Profit Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2018		
Mar 31	To Balance c/d	785.68	Mar 31	By Statement of P&L	785.68

2019			2018		
Mar 31	To Statement of P&L	255.45	Apr 1	By Balance b/d	785.68
Mar 31	To Balance c/d	530.23			
		785.68			785.68
2020			2019		
Mar 31	To Statement of P&L	261.84	Apr 1	By Balance b/d	530.23
Mar 31	To Balance c/d	268.39			
		530.23			530.23
2021			2020		
Mar 31	To Statement of P&L	268.39	Apr 1	By Balance b/d	268.39

Working Note :

1. Calculations of Unrealised Profit:

$$2017-18 = \frac{14,280.25}{23,810} \times 1,310 = ₹ 785.68$$

$$2018-19 = \frac{9,637.25}{23,810} \times 1,310 = ₹ 530.23$$

$$2019-20 = \frac{4,878.18}{23,810} \times 1,310 = ₹ 268.39$$

2. Calculation of Realised Profit:

$$2018-19 = \frac{4,643}{23,810} \times 1,310 = ₹ 255.45$$

$$2019-20 = \frac{4,759.07}{23,810} \times 1,310 = ₹ 261.84$$

$$2020-21 = \frac{4,878.18}{23,810} \times 1,310 = ₹ 268.39$$

$$3. \text{ Profit} = ₹ 23,810 - 22,500 = ₹ 1,310$$

Q.6. Mr. Ankush Chaudhary purchased on instalment basis machinery on 1st April, 2016. The term was that on 31st March each year the payment of ₹ 5,000 has to be made to the vendors Sohan Lal and Company, which includes interest @ 5% on the balance of cash down price due and so on for five years completing the payment in five instalments. It was decided to depreciate the machinery @10% per annum on Reducing Balance Method. Ascertain the cash down price and show Interest Suspense Account and the Machinery Account in the Books of the buyer.

Sol. $5,000 \times 5 = ₹ 25,000$ Total Price

Calculation of Interest

Date of Instalment	Interest	Opening Cash Value (₹)
2021 Mar 31	$5,000 \times \frac{5}{105} = ₹ 238$ $5,000 + 4,762 = ₹ 9,762$	$5,000 - 238 = 4,762$

2020 Mar 31	$9,762 \times \frac{5}{105} = ₹ 465$ $5,000 + 9,297 = ₹ 14,297$	$9,762 - 465 = 9,297$
2019 Mar 31	$14,297 \times \frac{5}{105} = ₹ 681$ $5,000 + 13,616 = ₹ 18,616$	$14,297 - 681 = 13,616$
2018 Mar 31	$18,616 \times \frac{5}{105} = ₹ 886$ $5,000 + 17,730 = ₹ 22,730$	$18,616 - 886 = 17,730$
2017 Mar 31	$22,730 \times \frac{5}{105} = ₹ 1,082$	$22,730 - 1,082 = 21,648$

Analytical Table

Year	Instalment (₹)	Interest (₹)	Cash Price (₹)
2020-21	5,000	238	4,762
2019-20	5,000	465	4,535
2018-19	5,000	681	4,319
2017-18	5,000	886	4,114
2016-17	5,000	1,082	3,918
Total	25,000	3,352	21,648

In the Books of Ankush Chaudhary (Buyers) Machinery Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2016 Apr 1	To Sohan Lal & Co.	21,648	2017 Mar 31	By Depreciation A/c	2,165
			Mar 31	By Balance c/d	19,483
		21,648			21,648
2017 Apr 1	To Balance b/d	19,483	2018 Mar 31	By Depreciation A/c	1,948
			Mar 31	By Balance c/d	17,535
		19,483			19,483
2018 Apr 1	To Balance b/d	17,535	2019 Mar 31	By Depreciation A/c	1,754
			Mar 31	By Balance c/d	15,781
		17,535			17,535
2019 Apr 1	To Balance b/d	15,781	2020 Mar 31	By Depreciation A/c	1,578

			Mar 31	By Balance c/d	14,203
		15,781			15,781
2020			2021		
Apr 1	To Balance b/d	14,203	Mar 31	By Depreciation A/c	1,420
		14,203	Mar 31	By Balance c/d	12,783
2021					14,203
Apr 1	To Balance b/d	12,783			

Interest Suspense Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2016			2017		
Apr 1	To Sohan Lal and Co.	3,352	Mar 31	By Interest A/c	1,082
		3,352	Mar 31	By Balance c/d	2,270
					3,352
2017			2018		
Apr 1	To Balance b/d	2,270	Mar 31	By Interest A/c	886
		2,270	Mar 31	By Balance c/d	1,384
					2,270
2018			2019		
Apr 1	To Balance b/d	1,384	Mar 31	By Interest A/c	681
		1,384	Mar 31	By Balance c/d	703
					1,384
2019			2020		
Apr 1	To Balance b/d	703	Mar 31	By Interest A/c	465
		703	Mar 31	By Balance c/d	238
					703
2020			2021		
Apr 1	To Balance b/d	238	Mar 31	By Interest A/c	238

Q.7. Suraj Limited purchased a Truck on 1st April, 2019 on Instalment System from Kapil Limited. The cash price was ₹ 30,000. The terms of purchase were under: (i) ₹ 12,000 is paid immediately, (ii) Balance being payable by 12 quarterly instalments of ₹ 1,920 each falling due from 1st July 2019. The Financial year of Suraj. Limited ends of 31st Oct. each year. On 31st December.

2020 the Truck was sold for ₹ 20,000 and the instalment balances were settled for ₹ 10,200. Suraj Limited brings the Assets Account at cash price and spreads the interest equally over the period of instalments payments. Depreciation at 20% per annum on cost price was provided up to the date of sale. Show the Truck Account, Kapil Limited Account and Interest Suspense Account in the books of Suraj Limited.

Sol.

**In the Books of Suraj Limited
Truck Account**

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019 Apr 1	To Kapil Ltd.	30,000	2019 Sept 30	By Depreciation A/c	3,000 ¹
			Sept 30	By Balance c/d	27,000
		30,000			30,000
2019 Oct 1	To Balance b/d	27,000	2020 Sept 30	By Depreciation A/c	6,000 ²
			Sept 30	By Balance c/d	21,000
		27,000			27,000
2020 Oct 1	To Balance b/d	21,000	2020 Dec 31	By Depreciation A/c	1,500 ³
2021 Sept 30	To P.& L. A/c	500 ⁷	Dec 31	By Balance c/d	20,000
		21,500			21,500

Kapil Limited

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019 Apr 1	To Bank A/c	12,000	2019 Apr 1	By Truck A/c	30,000
July 1	To Bank A/c	1,920	Apr 1	By Interest Suspense A/c	5,040 ⁴
Sept 30	To Balance c/d	21,120			
		35,040			35,040
2019 Oct 1	To Bank A/c	1,920	2019 Oct 1	By Balance b/d	21,120
2020 Jan 1	To Bank A/c	1,920			
Apr 1	To Bank A/c	1,920			
July 1	To bank A/c	1,920			
Spet 30	To Balance c/d	13,440			
		21,120			21,120
2020 Oct 1	To Bank A/c	1,920	2020 Oct 1	By Balance b/d	13,440
Dec 31	To bank A/c	10,200			
Dec 31	To Int. Suspense A/c (Rebate)	1,320			
		13,440			13,440

Interest Suspense Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019			2019		
Apr 1	To Kapil Ltd.	5,040	Sept 30	By Statement of P. & L.	840 ⁵
			Sept 30	By Balance c/d	4,200
		5,040			5,040
2019			2020		
Oct 1	To Balance b/d	4,200	Sept 30	By Statement of P. & L.	1,680 ⁶
			Sept 30	By Balance c/d	2,520
		4,200			4,200
2020			2020		
Oct 31	To Balance b/d	2,520	Dec 31	By Kapil Ltd.	1,320
			2021		
			Sept 30	By Statement of P. & L. (balancing figure)	1,200
		2,520			2,520

Working notes :

$$1. 30,000 \times \frac{20}{100} \times \frac{1}{2} = ₹3,000;$$

$$2. 30,000 \times \frac{20}{100} = ₹6,000;$$

$$3. \frac{30,000 \times 20}{100} \times \frac{3}{12} = ₹1,500;$$

$$4. 12,000 + (1,920 \times 12) - 30,000 = ₹ 5,040;$$

$$5. \frac{5,040 \times 2}{12} = ₹840;$$

$$6. 5,040 \times \frac{4}{12} = ₹1,680$$

7. These are balancing amounts.

Q.8. On 1st April 2017, X sells a Truck to Y, on the Instalment Payment System, on the following condition: (i) The cash price of the Truck is ₹ 1,00,000. (ii) The amount is payable to X in four equal annual instalments being payable along with 12% interest, per annum on the outstanding balance, the first instalment being payable on the date of sale.

Y, in turn, hires out the Truck to X for a monthly hire of ₹ 3000 per month from 1st April, 2017. The hire charges are to be adjusted at the end of each year, against the amount due to X on account of principal and interest, any difference being settled in cash on the first day of the next year.

Y charges 20% depreciation (on the Writing Down Value Method) on the Truck. All payments are made as per the agreement. On 1st April, 2019 the truck is sold by Y to X for ₹ 15,000 in cash.

Show in Y books, the Truck Account, X's Account, Interest Suspense Account, Interest Account and Hire Charges Account.

Sol.

In the Books of Y
Truck Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017 Apr 1	To X's A/c	1,00,000	2018 Mar 31	By Depreciation A/c	20,000 ¹
			Mar 31	By balance c/d	80,000
		1,00,000			1,00,000
2018 Apr 1	To Balance b/d	80,000	2019 Mar 31	By Depreciation A/c	16,000 ²
			Mar 31	By balance c/d	64,000
		80,000			80,000
2019 Apr 1	To Balance b/d	64,000	2020 Mar 31	By Depreciation A/c	12,800 ³
			Mar 31	By balance c/d	51,200
		64,000			64,000
2020 Apr 1	To Balance b/d	51,200	2020 Apr 1	By X	15,000
			2021 Mar 31	By P.& L. A/c	36,200 ⁴
		51,200			51,200

Working Note :

1. $\frac{1,00,000 \times 20}{100} = ₹20,000;$

2. $\frac{80,000 \times 20}{100} = ₹16,000;$

3. $\frac{64,000 \times 20}{100} = ₹12,800;$

4. This amount is balancing figures.

X's Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017 Apr 1	To Cash A/c	25,000	2017 Apr 1	By Truck A/c	1,00,000
			Apr 1	By Interest Spspense A/c	18,000 ¹
2018 Mar 31	To Hire Char. A/c	36,000 ²			
Mar 31	To Balance c/d	57,000			
		1,18,000			1,18,000
2019 Mar 31	To Hire Char. A/c	36,000	2018 Apr 1	By Balance b/d	57,000
Mar 31	To Balance c/d	23,000	Apr 1	By Cash A/c	2,000 ³
		59,000			59,000

2020			2019		
Mar 31	To Hire Char. A/c	36,000	Apr 1	By Balance b/d	23,000
			Apr 1	By Cash A/c	5,000 ⁴
			2020		
			Mar 31	Balance c/d	8,000
		36,000			36,000
2020			2020		
Apr 1	To Balance b/d	8,000	Apr 1	By Cash A/c	23,000 ⁵
Apr 1	To Truck A/c	15,000			
		23,000			23,000

Working Note :

- $\text{₹ } 1,00,000 \div 4 \text{ (number of instalments)} = \text{₹ } 25,000.$
 $\text{₹ } 1,00,000 - 25,000 = 75,000 @ 12\% = \text{₹ } 9,000$
 $\text{₹ } 75,000 - 25,000 = 50,000 @ 12\% = \text{₹ } 6,000$
 $\text{₹ } 50,000 - 25,000 = 25,000 @ 12\% = \text{₹ } 3,000$
₹ 18,000

- Rent = $3,000 \times 12 = \text{₹ } 36,000;$

	Hire Charges (₹)	Principal and Interest Due (₹)	Cash Received (₹)
3. On 1.4.2018	36,000	(25,000 + 9,000)	2,000
4. On 1.4.2019	36,000	(25,000+6,000)	5,000
5. On 1.4.2020	(36,000+15,000 sale price)	(25,000+3,000)	23,000

Interest Suspense Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017			2018		
Apr 1	To X's A/c	18,000	Mar 31	By Interest A/c	9,000
			Mar 31	By Balance A/c	9,000
		18,000			18,000
2018			2019		
Apr 1	To Balance b/d	9,000	Mar 31	By Interest A/c	6,000
			Mar 31	By Balance A/c	3,000
		9,000			9,000
2019			2020		
Apr 1	To Balance b/d	3,000	Mar 31	By Interest A/c	3,000
		3,000			3,000

Interest Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017			2018		
Mar 31	To Int. Susp. A/c	9,000	Mar 31	By P. & L. A/c	9,000
2019			2019		
Mar 31	To Int. Susp. A/c	6,000	Mar 31	By P. & L. A/c	6,000
2020			2020		
Mar 31	To Int. Susp. A/c	3,000	Mar 31	By P. & L. A/c	3,000

Hire Charges Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2018		
Mar 31	To P. & L. A/c	36,000	Mar 31	By X's A/c	36,000
2019			2019		
Mar 31	To P. & L. A/c	36,000	Mar 31	By X's A/c	36,000
2020			2020		
Mar 31	To P. & L. A/c	36,000	Mar 31	By X's A/c	36,000

Q.9. A Ltd. has two departments A and B. Transfers are made between the departments of both purchased goods and manufactured goods. Goods purchased are transferred at cost and manufactured goods are transferred at selling price as in case with open market.

Transactions for the year ended 31st March, 2021 are given below:

	A Dept. (₹)	B Dept. (₹)
Opening Inventories		
Purchases	20,000	15,000
Sales	1,00,000	80,000
Wages	1,90,000	1,35,000
Closing Inventories:	12,500	7,500
Purchased goods	2,000	5,000
Manufactured goods	7,000	8,000

The following were the transfers: From A department to B department: Purchased goods ₹ 6,000; Manufactured goods ₹ 20,000; From B department to A department: Purchased goods ₹ 5,000; Manufactured goods ₹ 35,000.

Inventories were valued at cost to the department concerned. Only in closing Inventories of manufactured goods in the departments transferred finished goods are at 20%.

Prepare Departmental Statement of Profit & Loss and Companies Statement of Profit & Loss in the books of A Ltd. for the year ending on 31st March 2021.

Sol. Statement of Profit & Loss (Departmental)
(for the year ended 31st March, 2021)

	Particulars	Note No.	Figures for the Current reporting period	
			A (₹)	B (₹)
I.	Revenue from Operations	1	2,16,000	1,75,000
II.	Other income		—	—
III.	Total Revenue (I + II)		2,16,000	1,75,000
IV.	Expenses:			
	Cost of Materials consumed	2	1,51,000	1,08,000
	Purchase of stock-in-trade			
	Changes in inventories of finished goods, W.I.P. and stock-in-trade			
	Employees' benefits expenses	3	12,500	7,500
	Finance Costs			
	Depreciation and amortization and expenses			
	Other Expenses			
	Total Expenses		1,63,500	1,15,500
V.	Profit before exceptional and extraordinary items and tax (III – IV)		52,500	59,500
VI.	Exceptional Items		—	—
VII.	Profit before extraordinary items and tax (V – VI)		52,500	59,500
VIII.	Extraordinary Items		—	—
IX.	Profit before tax (VII – VIII)		52,500	59,500
X.	Tax expenses:			
	(1) Current tax			
	(2) Deferred tax			
XI.	Profit (Loss) for the period from continuing operations (IX – X)		52,500	59,500
XII.	Profit (Loss) from discontinuing operations		—	—
XIII.	Tax expenses of discontinuing operations		—	—
XIV.	Profit (Loss) from discontinuing operations (after tax) (XII – XIII)		—	—
XV.	Profit (Loss) for the period (XI+XIV)		52,500	52,500
XVI.	Earnings per equity shares:			
	(1) Basic			
	(2) Diluted			

Working Notes :

1. Revenue from Operations :

	A (₹)	B (₹)
Sales	1,90,000	1,35,000
Transfer to B	26,000	—

Transfer to A	—	40,000
	2,16,000	1,75,000

2. Cost of Materials Consumed :

	A (₹)	B (₹)
Opening Inventories	20,000	15,000
Purchases	1,00,000	80,000
Transfer from A	—	26,000
Transfer from B	40,000	—
	1,60,000	1,21,000
Less : Closing inventoried	9,000	13,000
	1,51,000	1,08,000

Statement of Profit & Loss (A Ltd.)*(for the year ended 31st March 2021)*

	Particulars	Note No.	Figures for the Current reporting period
			A (₹)
I.	Revenue from Operations		3,25,000
II.	Other Income		—
III.	Total Revenue (I+II)		3,25,000
IV.	Expenses:		
	Cost of Materials consumed	7	1,93,890
	Purchases of stock-in-trade		
	Changes in inventories of finished goods, W.I.P. and stock-in-trade	8	20,000
	Employees' benefits expenses		
	Finance Costs		
	Depreciation and amortization and expenses		
	Other Expenses		
	Total Expenses		2,13,890
V.	Profit before exceptional and extraordinary items and tax (III – IV)		1,11,110
VI.	Exceptional Items		—
VII.	Profit before extraordinary items and tax (V – VI)		1,11,110
VIII.	Extraordinary Items		—
IX.	Profit before tax (VII – VIII)		1,11,110
X.	Tax expenses:		—
	(1) Current tax		
	(2) Deferred tax		
XI.	Profit (Loss) for the period from continuing operations (IX – X)		1,11,110
XII.	Profit (Loss) from discontinuing operations		—

XIII.	Tax expenses of discontinuing operations		—
XIV.	Profit (Loss) from discontinuing operations (after tax) (XII – XIII)		—
XV.	Profit (Loss) for the period (XI + XIV)		1,11,110
XVI.	Earnings per equity shares :		
	(1) Basic		
	(2) Diluted		

Working Notes :

1. Calculations of percentage of Gross Profit to Sales in each department:

	A	B
Sales	1,90,000	1,35,000
Transfer of finished goods	20,000	35,000
	2,10,000	1,70,000
$\frac{\text{Gross Profit}}{\text{Total Sales}} \times 100$	$\frac{52,500 \times 100}{2,10,000} = 25\%$	$\frac{59,500 \times 100}{1,70,000} = 35\%$
Finished goods	$\frac{7,000 \times 20}{100} = ₹1,400$	$\frac{8,000 \times 20}{100} = ₹1,600$
Unrealised Profit in the closing stock	$\frac{1,400 \times 35}{100} = ₹490$	$\frac{1,600 \times 25}{100} = ₹400$

Total unrealised profit = ₹ 490 + ₹ 400 = ₹ 890;

Calculation of closing stock of manufactured goods of A Ltd.

A Dept. ₹ 7000 + B Dept. ₹ 8,000—Unrealised profit ₹ 890 = ₹ 14,110.

- Total O/S : ₹ 20,000 + 15,000 = ₹35,000
- Total Purchased: ₹ 1,00,000 + 80,000 = ₹ 1,80,000;
- Total wages : ₹ 12,500 + 7,500 = ₹ 20,000;
- Total Sales : ₹ 1,90,000 + 1,35,000 = ₹ 3,25,000;
- Total closing purchased goods : ₹ 2,000 + ₹ 5,000 = ₹ 7,000.

7. Cost of Materials Consumed :

Opening Inventories

Purchases

(₹)

35,000

1,80,000

2,15,000

Less : Closing inventories :

Purchased goods

Manufactured goods

7,000

14,110

21,110

1,93,890

8. Employees' benefit :

Wages

(₹)

20,000

□

UNIT-III

Departmental Accounts and Branch Accounts

SECTION-A (VERY SHORT ANSWER TYPE) QUESTIONS

Q.1. Define the term 'Departmental accounting'.

Ans. Departmental accounting is a system of accounting which maintains a separate book of account for every department or branch of a business enterprise. It is one where accounts are prepared and maintained for different departments of an organization on an individual basis for evaluating their results in a fair manner. These individual books of account are then consolidated together with accounts of head office for preparation of financial statements of business. Departmental accounting aims at recording all the expenses and revenues of each department in a separate book of accounts.

Q.2. To which type of organisations is departmental accounting most suitable?

Ans. Such accounting information system is suitable for organization operating in diversified range of activities. Departmental accounting is an efficient tool for monitoring the expenses and performance of business where several products are produced by different branches under same roof. For example, a textile industry may be producing many fabrics such as woollen, cotton and jute.

Q.3. Enlist the principles of departmental accounting.

Ans. Final accounts of departmentalized organization are prepared keeping in mind the following principles:

1. Determination of gross profit or loss and net profit or loss of every unit of business should be done separately before taking total amount to balance sheet or appropriate account of organization.
2. Bases of appropriating gains and losses to each and every unit should be given fairly.

Q.4. What do you mean by branch accounts?

Ans. Accounts which are opened in the books of head office and branches, related to branches are called branch accounts. The main objective of these accounts is to know the working ability and profit and loss of branches. Branch accounts record the trading transactions of different branches of the same business, whether such branches are situated in the same town or at other towns in India or abroad.

Q.5. What is meant by a foreign branch?

Ans. When a branch is located in a foreign country, it is called a foreign branch. Such branches will keep their books of account in foreign currency. The distinctive feature of foreign branches is that financial information received from them will be in foreign currency which has to be converted into the currency of the country of the head office before it is

incorporated in the head office books. For example, if an Indian company has a branch in Nairobi, the branch Trial Balance will be in Kenya shillings.

Q.6. What is debtors system?

Ans. This system is adopted generally for those branches which are fairly small in size. Under this system, the head office simply opens a Branch Account for each branch in which it records all transactions relating to the branch. The Branch Account is prepared in such a manner that it also helps in ascertaining the branch profit or loss.

Q.7. Explain final accounts system.

Ans. Under this system, the head office prepares a Trading and Profit and Loss Account in order to find out profit or loss of each branch and a Branch Account to find out the amount due to, or due from that branch. In this case, the Branch Account simply acts as a personal account.

Q.8. Explain the objects of branch accounts.

Ans. Objects of keeping Branch Accounts are determined by the owners of the businesses, but here only those objects have been mentioned which are normally the objects of maintaining Branch Accounts

1. Profit or loss of each branch can be found out;
2. They help in controlling branches;
3. Actual financial position of the business can be found out on the basis of Head Office and Branch accounting records,
4. Branch requirements of goods and cash can be estimated;
5. Suggestions for increasing the efficiency of the Branch can be made on the basis of Branch Accounts;
6. They help in complying the requirements of law because according to the Companies Act, 2013, maintenance of accounting record of branches by owners is essential.

Q.9. Discuss any two types of branches.

Ans. Following are the two main types of branches:

1. Branches receiving goods from Head Office at Cost Price and making Cash Sales only : These Branches receive goods from Head Office at cost and make cash sales only. All sale proceeds are sent to head office. Head Office sends amount separately for the expenses of the Branch.
2. Branches receiving Goods from Head Office at Cost Price and making Cash and Credit Sales. These Branches are like the first type of Branch, the only difference is that they sell goods on credit also.

Q.10. Explain the final accounts method in branch accounting.

Ans. This method is used by those branches which are either of medium category or higher category. In this method following accounts are prepared:

1. Branch Trading and Profit & Loss Account and
2. The Branch Account prepared under this method is of the nature of personnel Account. The assets & liabilities are also shown in Branch Accounts. The Branch Trading and Profit & Loss Account is prepared on the basis of cost. Hence, opening stock, closing stock and goods sent to Branch account if given at invoice price are always shown at cost. For this the inflated price is reduced from the invoice price. The goods in transit

sent by head office to branch should be shown along with closing stock at original cost. The goods returned by the branch should be deducted from the value of goods supplied to branch and the balance should thus be shown in debit side.

SECTION-B (SHORT ANSWER TYPE) QUESTIONS

Q.1. Explain the methods of departmental accounting.

Ans. Methods of Departmental Accounting

There are two methods that are used in departmental accounting: —

1. **Where individual set of books is maintained :** It is a method under which every branch of an organization is regarded as separate unit and therefore individual book of accounts are prepared and maintained for every unit. At the end, financial result of every department is calculated and consolidated to find the overall performance and net result of whole organization.

This method of departmental accounting involves huge costs and is preferred only by large scale organizations or where is required by the law. Companies involved in insurance business are the one which are compulsorily required to implement this system of accounting.

2. **Where all Departmental Accounts are maintained columnar-wise collectively :** Under this technique of departmental accounting, accounts of all branches are maintained collectively in columnar form by central accounts department. In this method for every department a departmental trading and profit and loss account is opened in columnar way altogether. There is a separate column for "Total" for finding out the results of different departments both on individual and collective basis. Balance Sheet is however prepared in a combining form.

Q.2. What are the main objectives of departmental accounting?

Ans. Objectives of Departmental Accounting

Main objectives of departmental accounting are as given below:

1. Evaluation of individual performance of branches which facilitates in doing comparison of results.
2. Detects financial position of every department in organization.
3. Formulation of proper plans and strategies after knowing results of each branch.
4. Calculation of remuneration and commission of managers of every department after knowing result of operations.
5. Deciding appropriate actions after measuring the performances of all divisions.
6. Assist in cost control by providing full detail information about business organization.
7. Efficient management of cost of all departments by proper allocation of cost to various departments.
8. Promotes healthy competitive spirit among distinct branches that leads to enhance the profitability.
9. Assist in taking decisions related to expansion and shutting down of business departments in accordance to their results.

Q.3. Discuss the various types of branches.

Ans. Types of Branches

Following are the main types of branches:

1. **Branches receiving goods from Head Office at Cost Price and making Cash Sales only :** These Branches receive goods from Head Office at cost and make cash sales only. All sale proceeds are sent to Head Office. Head Office sends amount separately for the expenses of the Branch.
2. **Branches receiving Goods from Head Office at Cost Price and making Cash and Credit Sales :** These Branches are like the first type of Branch, the only difference is that they sell goods on credit also.
3. **Branches receiving Goods from Head Office at Selling Price or Invoice Price and making Cash and Credit Sales :** These Branches are like the second type of Branches with the only difference that goods to these Branches are sent by the Head Office at Invoice Price which is always above Cost Price.
4. **Independent Branches :** These Branches receive goods from the Head Office and may manufacture or purchase goods from the market also. They are independent in all respects except that they are under the control of Head Office and thus they have to follow the instructions of Head Office.
5. **Foreign Branches :** These Branches may be of any type discussed above. They are known as Foreign Branches because they work in foreign countries.

Q.4. Discuss the accounting records of branches in the head office books.

Ans. Accounting Records

In case of dependent branch, the accounting records as regard to branch are kept in head office books as per following methods :

1. **Simple System or Debtor System :** When branches are very small than this method is adopted. In this method only branch account is prepared in the books of Head Office whose credit balance indicates profit and debit balance indicates loss. This method is also called as Debtor method. The Branch account prepared under this method is of the nature of nominal account.
2. **Final Accounts System :** In this method, the Branch Trading Account and Profit & Loss Account or Statement of P & L is prepared in the books of Head Office along with Branch Account. The Branch account prepared under this method is of the nature of personnel account. The object of preparing the branch account is to know what the Branch owes from head office or what Branch owes to head office, hence, the balance in Branch account is shown as By Balance c/d or To Balance c/d.
3. **Stock Debtor System :** In this method, various accounts are prepared in the books of Head office viz. Branch Stock Account, Goods Supplied to Branch, Branch Debtor Account, Branch Expenses Account, Stock Reserve Account, Branch Adjustment Account, Branch Assets Account, etc.
4. **Wholesale Branch Method :** This method is applied when the manufacturer supplies the goods to the wholeseller and also to the consumers from their own branches. The goods are transferred to branch at the same value at which it is transferred to wholesalers.

Q.5. Discuss Various merits of departmental accounting.

Ans. Advantages of Departmental Accounting

Major advantages of departmental accounting are:

1. **Reveal the success or failures of units :** This accounting determines the success rate and failure of every department within the organization. Every expense and income of these departments are properly recorded for calculating its real profitability. Amount of revenue generated by these units gives a clear idea about the one that is successful in their role and one that fails to meet their goals.
2. **Benefits to Auditors and Investors :** It supplies all relevant information in a correct manner about each unit of business to auditors and investors. Auditors can easily access to the account of each individual unit for knowing all expenses and revenues and thereby enables them in verifying the correctness of financial statements. Investors can get a clear view of portability and overall value of an organization.
3. **Determine managers commission :** Departmental accounting assist in the fair calculation of manager's commission working within different departments of the business. Commissions are paid to managers on the basis of profit earned by their respective departments. Proper accounts that are maintained separately for every unit yield right amount of their profit levels.
4. **Promote competitive spirit :** It promotes a sense of competitive spirit among all staff working within an organization. All operations of each business unit is properly monitored under this system of accounting. Team members are rewarded on the basis of performance of their departments which is revealed by the departmental book of accounts. This motivates staff to work efficiently for improving the overall performance.

Q.6. What are the major differences between branch and department.

Ans. Differences between Branch and Department

Following description indicates the difference between branches and departments :

1. **Place :** All the departments of a business remain generally under one roof, but branches of a concern are established at different places in the same town or at different towns.
2. **Objects :** Branches are opened to increase sales and to come in contact with the customers, while the departments are made to increase the efficiency of the business and to carry on work more smoothly.
3. **Accounting :** Departmental accounting record is kept at one place because they remain under one roof but branches are at different places, hence, their accounting records are kept at the places of the branches, though they are also kept at head office.
4. **Inland and Foreign :** Branches may be either inland or foreign, while departments are always inland.

Q.7. Discuss various rules regarding allocation of expenses.

Ans. Allocation of Expenses

There are many rules regarding allocation of expenses. Out of these rules, some important rules are discussed as follows :

1. **Allocation according to sales** : Sales commission, advertisement expenses, salary of salesman and sales expenses are allocated in the ratio of sales of various departments.
2. **Allocation according to place** : The expenses, whose benefit is derived by each department according to its area are allocated in the ratio of floor space occupied by each department. Examples are rates and taxes and municipal rent.
3. **Electricity Charges** : Electricity charges are divided in the ratio of number of points used in each department, but voltage used in each department is also considered for this purpose.
4. **Insurance of Goods** : Division of this expense is made on the basis of the stock of each department.
5. **Electric Power** : If electric power is used for operating machines, consumption of power by various machines is estimated and on the basis of this consumption allocation of electric power charges is made. If each department has a separate meter, electric charges are allocated on the basis of meter reading of various departments.
6. **Depreciation** : Depreciation is allocated on the basis of the values of the plant of each department.
7. **Salary of Factory Manager** : Salary of factory manager is divided in the ratio of time devoted by this manager in each department.
8. **Workmen's Compensation Insurance** : This insurance is allocated in the ratio of wages of each department.
9. **Insurance of Premises** : This insurance is apportioned in the ratio of premises occupied by each department.
10. **Repairs of Machinery** : Repairs of machinery can be allocated in the ratio of value of machinery used in each department.

Q.8. A business is carried on in three separate departments. Expenses not directly chargeable to any department are apportioned one-half to A, three-tenth to B, and one-fifth to C. From the following particulars, prepare Trading and Profit & Loss Account of the three departments (in Columnar form) showing the gross and net profit, and the percentage thereof and of the totals, to outside turnover, exclusive of inter-departmental transactions.

Stock in hand 1st April : A Department ₹ 1,782; B ₹ 560; C ₹ 125; **Stock in hand, 31st March**: A Department ₹ 1,936; B ₹ 471; C ₹ 316; **Outside Sales for the year**: A Department ₹ 11,174; B ₹ 5,613; C ₹ 4,851; **inter-departmental sales**: A to B ₹ 904; A to C ₹ 482; B to A ₹ 1,126; B to C ₹ 219; C to A ₹ 348; **Wages**: A Department ₹ 2,740; B ₹ 1,328; C ₹ 915; **Outside purchases**: A Department ₹ 4,041; B ₹ 1,537; C ₹ 1,256; **Salaries**: A Department ₹ 945; B ₹ 572; C ₹ 416.

Management Salaries ₹ 1,200; **Rent and taxes** ₹ 1,460, **Insurance** ₹ 210; **Vans, etc. expenses** ₹ 870; **Postage and Telegrams** ₹ 110; **Bad debts**: A ₹ 276; B ₹ 143, C ₹ 224; **Sundry expenses** ₹ 530; **Depreciation written off** ₹ 740; **Stationery and Printing** ₹ 260; **Advertising** ₹ 450.

Sol. Departmental Trading and Profit & Loss Account
(for the year ended.....)

Particulars	A (₹)	B (₹)	C (₹)	Total (₹)	Particulars	A (₹)	B (₹)	C (₹)	Total (₹)
To Stock	1,782	560	125	2,467	By Sales	11,174	5,613	4,851	21,638
To Purchases	4,041	1,537	1,256	6,834	By Dept. Sales	1,386	1,345	348	3,079
To Departmental Purchases	1,474	904	701	3,079	By Closing Stock	1,936	471	316	2,723
To Wages	2,740	1,328	915	4,983		<u>14,496</u>	<u>7,429</u>	<u>5,515</u>	<u>27,440</u>
To Gross Profit c/d	4,459	3,100	2,518	10,077	By Gross Profit b/d	4,459	3,100	2,518	10,077
	<u>14,496</u>	<u>7,429</u>	<u>5,515</u>	<u>27,440</u>					
To Salaries	945	572	416	1,933					
To Management Salaries	600	360	240	1,200					
To Rent & Taxes	730	438	292	1,460					
To Insurance	105	63	42	210					
To Vans, etc. Expenses	435	261	174	870					
To Postage & Telegram	55	33	22	110					
To Bad Debts	276	143	224	643					
To Sundry Exps.	265	159	106	530					
To Depreciation	370	222	148	740					
To Stationery & Printing	130	78	52	260					
To Advertising	225	135	90	450					
To Net Profit c/d to P. & L. Appropriation A/c	323	636	712	1,671					
	<u>4,459</u>	<u>3,100</u>	<u>2,518</u>	<u>10,077</u>		<u>4,459</u>	<u>3,100</u>	<u>2,518</u>	<u>10,077</u>

Statement of Percentage of Gross and Net Profit to Outside Sales

	A	B	C	Total
(i) Gross Profits	39.90%	55.23%	51.91%	46.57%
(ii) Net Profit	2.89%	11.23%	14.68%	7.72%

Working Notes :

Calculation of Inter-Departmental Purchases and Sales

	A		B		C	
	Sales (₹)	Purchases (₹)	Sales (₹)	Purchases (₹)	Sales (₹)	Purchases (₹)
A to B	904	—	—	904	—	—
A to C	482	—	—	—	—	482
B to A	—	1,126	1,126	—	—	—
B to C	—	—	219	—	—	219
C to A	—	348	—	—	348	—
Total	1,386	1,474	1,345	904	348	701

Q.9. Chaudhary and Company of Noida has their Branch at Meerut which sells goods for cash only. The following are the transactions between the Head Office and Branch Office for the year ending 31st March, 2021:

	(₹)	(₹)
Opening Stock at 1st April 2020		20,000
Goods Supplied to Branch		50,000
Cash sent to Branch for : Rent	200	
Other Expenses	100	300
Cash received from Branch during the year		60,000
Closing Stock at 31st March, 2021		15,000
Closing Balance of Petty Cash		10

From the above information, pass the necessary Journal Entries and prepare Meerut Branch Account and other necessary accounts in the books of Head Office.

**Sol. In the Books of Head Office
Journal Entries**

2020-21	Particulars	L.F.	(₹)	(₹)
	Meerut Branch A/c	Dr.	20,000	
	To Stock at Meerut Branch A/c			20,000
	(Being transfer of opening stock)			
	Meerut Branch A/c	Dr.	50,000	
	To Goods Supplied to Kanpur Branch A/c			50,000
	(Being goods supplied to Meerut Branch)			
	Meerut Branch A/c	Dr.	300	
	To Cash A/c			300
	(Being cash sent to branch for meeting the following expenses of the branch: Rent, ₹ 200; Other expenses ₹ 100)			
	Cash A/c	Dr.	60,000	
	To Meerut Branch A/c			60,000
	(Being Cash received from the Branch)			

Mar 31	Stock at Meerut Branch A/c	Dr.	15,000	
	Petty Cash at Meerut Branch A/c	Dr.	10	
	To Meerut Branch A/c			15,010
	(Being closing balance of Stock and Petty Cash at the Branch recorded)			
Mar 31	Meerut Branch A/c	Dr.	4,710	
	To General P. & L. A/c			4,710
	(Being transfer of Net Profit to General P.& L. Account)			

Meerut Branch Account
(for the year ending March 31, 2021)

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2020			2021		
Apr 1	To Stock at Meerut Branch A/c (Opening Stock)	20,000	Mar 31	By Cash A/c	60,000
	To Goods Supplied to Branch A/c	50,000		By Stock at Meerut Branch A/c	15,000
	To Cash A/c:			By Petty Cash at Meerut Branch A/c	10
	Rent 200				
2021	Other Exp. 100	300			
Mar 31	To Net Profit transferred to General P. & L. A/c	4,710 ¹			
		75,010			75,010

1. This is balancing amount.

Goods Supplied to Meerut Branch Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2021			2020		₹
Mar 31	To Purchases A/c	50,000	Apr 1	By Meerut Branch A/c	50,000
		50,000			50,000

Stock at Meerut Branch Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2020			2020		
Apr 1	To Balance b/d	20,000	Apr 1	By Meerut Branch A/c	20,000
2021			2021		
Mar 31	To Meerut Branch A/c	15,000	Mar 31	By Balance c/d	15,000
		35,000			35,000
2021					
Apr 1	To Balance b/d	15,000			

Petty Cash at Meerut Branch Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2021			2021		
Mar 31	To Meerut Branch A/c	10	Mar 31	By Balance c/d	10
2021					
APr 1	To Balance b/d	10			

General Profit & Loss Account (for the year ended March 31, 2021)

	(₹)		(₹)
		By Meerut Branch A/c	4,710

Q.10. Prepare Branch Account from the following particulars. Branch makes only cash sales:

Particulars	Amount (₹)
Opening stock	2,450
Opening petty cash	70
Outstanding salary for previous year	250
Goods sent to branch	48,000
Cash sales	58,500
Cash sent for branch expenses	3,750
Closing balance of petty cash	70

Closing stock has not been ascertained. Management gets commission @ 10% on net profit before charging such commission. Branch sells goods after adding 25% profit on the cost price.

Sol. Branch Account

Particulars	(₹)	Particulars	(₹)
To Balance b/d : Stock	2,450	By Balance b/d :	
Petty Cash	70	Outstanding Salary	250
To Goods Supplied A/c	48,000	By Cash A/c (Sales)	58,500
To Cash A/c (Exp.)	3,750	By Balance c/d :	
To Cash A/c (Comm.)	820 ²	Closing Stock	3,650 ¹
To General P. & L. A/c	7,380	Petty Cash	70
	62,470		62,470

Working Notes :

1. Closing Stock = Opening Stock + Goods sent – Cost of Goods sold

$$= 2,450 + 48,000 - \left(\frac{58,500 \times 100}{125} \right) = 2,450 + 48,000 - 46,800 = 50,450 - 46,800 = ₹ 3,650$$

2. Commission = $\left[(250 + 58,500 + 3,650 + 70) - (2,450 + 70 + 48,000 + 3,750) \right] \times \frac{10}{100} = ₹ 820$

Q.11. Akash of Meerut has a branch in Hapur. Prepare Hapur Branch Account in the books of Akash from the following particulars:

	(₹)	(₹)
Opening Stock 1.4.2020		8,000
Goods supplied to Branch		80,000
Expenses paid by Head Office:		
Wages	500	
Salaries	600	
Other Expenses	900	2,000
Exps. paid by the Branch:		
Petty expenses	300	
Carriage	500	800
Cash Sales by branch		1,10,000
Petty Cash on 31st March, 2021		500
Closing Stock on 31st March, 2021		3,000

**Ans. In the Books of Akash of Meerut
Hapur Branch Account
(for the year ended 31st March, 2021)**

Particulars	(₹)	Particulars	(₹)
To Stock at Hapur Branch A/c	8,000	By Cash A/c	1,08,700 ¹
To Goods Supplied A/c	80,000	By Stock at Hapur Branch A/c	3,000
To Cash A/c :		By Petty Cash at Hapur Branch a/c	500
Wages	500		
Salaries	600		
Other Expenses	900		
To General P. & L. A/c	22,200 ²		
	1,12,200		1,12,200

Working Notes :

1. Cash Sales ₹ 1,10,000 – (expenses paid by branch ₹ 800 + petty cash at branch ₹ 500) = ₹ 1,08,700.
2. This is balancing amount.

Q.12. Following are the particulars of Meerut branch. Its Head Office is in Gwalior. Prepare Meerut branch account in the head office books :

	(₹)
Stock 1.4.2020	16,000
Goods supplied to Branch	50,000
Expenses paid by Head Office :	(₹)
Insurance upto 31st July, 2021	1,200

Rent Paid from 1.4.2021 to 30.6.2021	1,500	
Wages 1.2.2021 to 30.04.2021	<u>2,100</u>	4,800
Cash remitted to H.O.		65,000
Closing Stock 31.3.2021		5,000

**Sol. In the Books of Gwalior Head Office
Meerut Branch Account
(for the year ended 31st March, 2021)**

Particulars	(₹)	Particulars	(₹)
To Balance b/d (Stock)	16,000	By Cash A/c	65,000
To Goods Supplied A/c	50,000	By Balance c/d :	
To Cash A/c :		Stock	5,000
Insurance 1,200		Prepaid Insurance	400 ¹
Rent 1,500		Prepaid Rent	300 ²
Wages <u>2,100</u>	4,800	Prepaid Wages	700 ³
To General P. & L. A/c	600		
	<u>71,400</u>		<u>71,400</u>

Working Notes :

1. Prepaid Insurance Premium for 4 months = $\frac{1,200 \times 4}{12} = ₹400.$
2. Prepaid Rent = $\frac{1,500 \times 3}{15} = ₹300.$
3. Prepaid Wages = $\frac{2,100 \times 1}{3} = ₹700$

Q.13. Swadeshi Co. has its Head Office at Kanpur and Branch at Etawah. The Branch sells for cash as well as credit. With the help of the following transactions which took place between Head Office and Branch Office in the year 2020-21; prepare Branch Account and Debtors Account in the books of Head Office :

	(₹)
Opening Stock	10,000
Opening Debtors	5,000
Goods Supplied to the Branch from Head Office	35,000
Cash sent to Branch for Expenses	2,000
Cash Sales	20,000
Cash Received from Debtors	10,000
Goods returned by the Branch	500
Closing Stock	6,000
Goods-in-transit from Head Office on 31st March, 2021	1,000
Goods returned by Customers	3,000
Allowed discount to Customers	500
Bad Debts	1,500
Credit Sales	30,000

Sol.

**In the Books of Head Office
Etawah Branch Account**

Dr.

(for the year ended 31st March 2021)

Cr.

Particulars	(₹)	Particulars	₹
To Opening Balance :		By Cash A/c :	
Stock 10,000		Cash Sales 20,000	
Debtors 5,000	15,000	Amount Received from Debtors 10,000	30,000
To Goods Supplied to Branch A/c + Goods in transit (1,000)	36,000	By Goods Supplied to Branch A/c	500
To Cash A/c (Expenses)	2,000	By Branch Debtors A/c	20,000
To Statement of P & L	4,500	By Stock at Branch A/c	6,000
	57,500	By Goods-in-Transit A/c	1,000
			57,500

Branch Debtors Account

Particulars	(₹)	Particulars	(₹)
To Balance b/d	5,000	By Cash A/c	10,000
To Credit Sales A/c	30,000	By Returns Inward A/c	3,000
		Discount A/c	500
		By Bad Debts A/c	1,500
		By Balance c/d	20,000
	35,000		35,000

Q.14. Ankush & Company makes purchases at the Head Office and sends the goods bought to the Branch Office for sale, no stock being retained at the Head Office. The Branch Office effects sales, keeps their own Sales Ledgers, receives cash against Ledger Accounts and pays in the whole of their cash receipts every day to the Head Office. Branch Office expenses are paid from cash remitted by the Head Office to Branches for the purpose.

From the following particulars, show the Branch Accounts in the Head Office Books in the columnar form. Also, prepare a General Profit & Loss Account assuming that the Head Office expenses amounted to ₹ 15,000 :

	X (₹)	Y (₹)	Z (₹)
Stock of Commencement at Cost	8,100	7,200	7,500
Debtors at Commencement	18,750	18,000	16,500
Goods supplied to Branches by H.O.	31,800	30,900	30,000
Rent and Taxes paid	1,200	1,050	1,125
Wages and Sundry Expenses paid	5,700	5,340	5,250
Cash received from Ledger Accounts	35,700	36,000	30,000
Cash Sales	21,300	18,750	19,500
Stock at end, at Cost	9,300	8,700	7,200

Credit Sales	40,500	39,000	34,500
Returns Inward	300	360	240
Allowance to Customers	75	60	90
Bad Debts	225	150	—

Ans.

In the Head Office Books
Branch Accounts in Columnar Form
(for the year ended.....)

Particulars	X (₹)	Y (₹)	Z (₹)	Particulars	X (₹)	Y (₹)	Z (₹)
To Stock A/c	8,100	7,200	7,500	By Cash A/c	57,000 ²	54,750	49,500 ²
To Debtors A/c	18,750	18,000	16,500	By Stock at Branch A/c	9,300	8,700	7,200
To Goods Sent A/c	31,800	30,900	30,000	By Branch Debtors A/c	22,950 ¹	20,430 ¹	20,670 ¹
To Cash A/c Rent	1,200	1,050	1,125				
Wages etc.	5,700	5,340	5,250				
To Gen. P. & L. A/c	23,700	21,390	16,995				
	89,250	83,880	77,370		89,250	83,880	77,370

Working Notes :

1.

Branch Debtors Account

	X (₹)	Y (₹)	Z (₹)		X (₹)	Y (₹)	Z (₹)
To Balance b/d	18,750	18,000	16,500	By Cash A/c	35,700	36,000	30,000
To Credit Sales A/c	40,500	39,000	34,500	By Returns Inward A/c	300	360	240
				By Allowance to Customers A/c	75	60	90
				By Bad Debts A/c	225	150	—
				By Balance c/d	22,950	20,430	20,670
	59,250	57,000	51,000		59,250	57,000	51,000

2. Total Cash Received = Cash Sales + Received from Ledger A/c

$$X = 21,300 + 35,700 = ₹ 57,000$$

$$Y = 18,750 + 36,000 = ₹ 54,750$$

$$Z = 19,500 + 30,000 = ₹ 49,500$$

General Profit & Loss Account

(for the year ended

	(₹)		(₹)
To Expenses	15,000	By X Branch	23,700
To Net Profit	47,085	By Y Branch	21,390
		By Z Branch	16,995
	62,085		62,085

Q.15. Prepare Satna Branch Account in the books of Head Office for the year 2020-21 from the following particulars:

	(₹)	
Stock 1.4.2020	5,000	
Debtors 1.4.2020	2,000	
Furniture 1.4.2020	6,000	
Prepaid Insurance 4.1.2020	1,000	
Petty Cash 1.4.2020	600	
Goods supplied to Branch	75,000	
Cash sent to branch for expenses :	(₹)	
Salaries	4,000	
Insurance	1,300	
Petty Cash	700	6,000
Outstanding Wages 31.3.2021	500	
Outstanding Wages 1.4.2020	3,000	
Cash Sales	63,000	
Debtors made direct payment to Head Office	4,000	
Debtors made payment to Branch	3,000	
Debtors returned goods direct to Head Office	2,000	
Branch returned the goods to Head Office	4,000	
Debtors 31.3.2021	9,000	
Stock 31.3.2021	3,000	
Depreciation on furniture 5% p.a.		
Credit Sales		20,000
Goods returned by debtors		3,000
Discount allowed to debtors		1,000
Petty Expenses paid by the Branch		400

Goods of ₹ 1,800 were destroyed by Fire Insurance Company admitted the claim for ₹ 1,200 only and this amount is received from Insurance Company Branch remitted necessary cash to Head Office.

Ans. In the Books of Head Office

Satna Branch Account

(for the year ended March 31 2021)

Dr.			Cr.
Particulars	(₹)	Particulars	(₹)
To Balance b/d :		By Outstanding Wages A/c	3,000
Stock	5,000	By Cash A/c :	
Debtors	2,000	(a) Cash Sales	63,000
Petty Cash	600	(b) Amount recd. direct from Debtors	4,000

Furniture	6,000		(c) Amount recd. from Debtors	300	
Prepaid Insurance	1,000	14,600	(d) Insurance Co.	1,200	71,200
To Goods Supplied A/c		75,000	By Goods Supplied A/c :		
To Cash A/c :			(a) By Branch	4,000	
Salaries	4,000		(b) By Debtors	2,000	6,000
Insurance	1,300		By Balance c/d :		
Petty Cash	700	6,000	Stock	3,000	
To Outstanding Wages A/c		500	Debtors	9,000	
To General Profit & Loss A/c		2,700	Petty Cash	900 ¹	
			Furniture	5,700 ²	18,600
		98,800			98,800

Working Notes :

	(₹)
1. Opening balance of Petty Cash	600
Add : Received from Head Office	700
	1,300
Less : Petty cash expenses	Closing Balance 400
	900
2. Furniture ₹ $\frac{6,000 \times 5}{100} = ₹ 300$; ₹ 6,000 – 300 = ₹ 5,700	

SECTION-C LONG ANSWER TYPE QUESTIONS

Q.1. The directors of Priya Ltd. want to find out the net profits of the X, Y and Z departments separately for the three months ended on 31st March, 2021. It is found impracticable actually to take stock on that date but an adequate system of departmental accounting is in use and the normal rates of gross profit for the departments concerned are 40%, 30% and 20% on turnover, respectively. Indirect expenses are charged in proportion to departmental turnover. For the above mentioned period, total indirect expenses (including those relating to other departments) were ₹ 4,200 on the total turnover of ₹ 84,000. The following are the figure for the three departments:

	X (₹)	Y (₹)	Z (₹)
Inventories on 1st April	6,000	7,000	3,000
Purchases for the period	7,000	6,500	4,700
Sales for the period	12,000	10,000	6,000
Direct Expenses	2,020	1,450	710

Prepare a statement of estimated profit making a Inventories reserve of 10% for each department on 31st March 2021.

Ans.

Statement of Profit & Loss
(for the year ended 31st March 2021)

Particulars	Note No.	Figure for the Current reporting period		
		X (₹)	Y (₹)	Z (₹)
I. Revenue from Operations		12,000	10,000	6,000
II. Other Income		—	—	—
III. Total Revenue (I+II)		12,000	10,000	6,000
IV. Expenses :				
Cost of Materials consumed	1	5,180	5,550	4,090
Purchases of stock-in-trade				
Changes in inventories of finished goods, W.I.P. and stock-in-trade				
Employees' benefits expenses				
Finance Costs				
Depreciation and amortization and expenses				
Other Expenses	2	3,402	2,745	1,371
Total Expenses		8,582	8,295	5,461
V. Profits before exceptional and extraordinary items and tax (III – IV)		3,418	1,705	539
VI. Exceptional Items		—	—	—
VII. Profit before extraordinary items and tax (V – VI)		3,418	1,705	539
VIII. Extraordinary Items		—	—	—
IX. Profit before tax (VII – VIII)		3,418	1,705	539
X. Tax expenses :		—	—	—
(1) Current tax				
(2) Deferred tax				
XI. Profit (Loss) for the period from continuing operations (IX – X)		3,418	1,705	539
XII. Profit (Loss) from discontinuing operations		—	—	—
XIII. Tax expenses of discontinuing operations		—	—	—
XIV. Profit (Loss) from discontinuing operations (after-tax) (XII – XIII)		—	—	—
XV. Profit (Loss) for the period (XI + XIV)		3,418	1,705	539
XVI. Earnings per equity shares :				
(1) Basic				
(2) Diluted				

Working Notes :

1. Cost of Material Consumed :

Particulars	X (₹)	Y (₹)	Z (₹)
Opening Inventories	6,000	7,000	3,000
Purchases	7,000	6,500	4,700
	13,000	13,500	7,700

Less : Closing Inventories	7,820	7,950	3,610
	5,180	5,550	4,090

2. Other Expenses :

	X (₹)	Y (₹)	Z (₹)
Direct Expenses	2,020	1,450	710
Indirect Expenses	600	500	300
Inventories Reserve	782	795	361
	3,402	2,745	1,371

3. Total sales = ₹ 12,000 + 10,000 + 6,000 = ₹ 28,000; $\frac{4,200 \times 28,000}{84,000} = ₹ 1,400$. These indirect

expenses are apportioned in the ratio of sales i.e., 12,000 : 10,000 : 6,000 or 12 : 10 : 6 or 6 : 5 : 3

or $\frac{6}{14} : \frac{5}{14} : \frac{3}{14}$; $\frac{1,400 \times 6}{14} = ₹ 600$;

4. $\frac{1,400 \times 5}{14} = ₹ 500$; and $\frac{1,400 \times 3}{14} = ₹ 300$;

5. Calculation of Stock Reserve :

Closing Stock = Opening Stock + Purchases + Direct Exp. + Gross Profit – Sales

X : C/S = 16,000 + 7,000 + 2,020 + Gross profit 40% on sales – 12,000
= 15,020 + 4,800 – 12,000 = 7,820

Closing Stock = ₹ 7,820

Stock Reserve 10% = $\frac{7,820 \times 10}{100} = ₹ 782$

Y : C/S = 7,000 + 6,500 + 1,450 + Gross profit 30% on sales – 10,000
= 14,950 + 3,000 – 10,000 = 7,950

Closing Stock ₹ 7,950

Stock Reserve 10% = $\frac{7,950 \times 10}{100} = ₹ 795$

Z : C/S = 3,000 + 4,700 + 710 + Gross profit 20% on sales – 6,000
= 8,410 + 1,200 – 6,000 = 3,610

Closing Stock = ₹ 3,610

Stock Reserve 10% = $3,610 \times \frac{10}{100} = ₹ 361$

Q.2. A Ltd. has two departments M and N. Transfers are made between the departments of both purchased goods and manufactured goods. Goods purchased are transferred at cost and manufactured goods are transferred at selling price as in case with open market.

Transactions for the year ended 31st March, 2021 are given as follows :

	M Dept. (₹)	N Dept. (₹)
Opening Inventories	20,000	15,000
Purchases	1,00,000	80,000

Sales	1,90,000	1,35,000
Wages	12,500	7,500
Closing Inventories :		
Purchased goods	2,000	5,000
Manufactured goods	7,000	8,000

The following were the transfers : From M department to N department: Purchased goods ₹ 6,000 Manufactured goods ₹ 20,000. From N department to M department: Purchased goods ₹ 5,000, Manufactured goods ₹ 35,000

Inventories were valued at cost to the department concerned. Only in closing Inventories of manufactured goods in the departments transferred finished goods are at 20%.

Prepare Departmental Statement of Profit & Loss and Companies Statement of Profit & Loss in the books of A Ltd. for the year ending on 31st March 2021.

Sol. **Statement of Profit & Loss (Departmental)**
(for the year ended 31st March, 2021)

Particulars	Note No.	Figures for the Current reporting period	
		M (₹)	N (₹)
I. Revenue from Operations	1	2,16,000	1,75,000
II. Other income		—	—
III. Total Revenue (I + II)		2,16,000	1,75,000
IV. Expenses :			
Cost of Materials consumed	2	1,51,000	1,08,000
Purchases of stock-in-trade			
Changes in inventories of finished goods, W.I.P. and stock-in-trade			
Employees' benefits expenses	3	12,500	7,500
Finance Costs			
Depreciation and amortization and expenses			
Other Expenses			
Total Expenses		1,63,500	1,15,500
V. Profit before exceptional and extraordinary items and tax (III-VI)		52,500	59,500
VI. Exceptional Items		—	—
VII. Profit before extraordinary items and tax (V-VI)		52,500	59,500
VIII. Extraordinary Items		—	—
IX. Profit before tax (VII-VIII)		52,500	59,500
X. Tax expenses :		—	—
(1) Current tax		—	—
(2) Deferred tax		—	—
XI. Profit (Loss) for the period from continuing operations (IX-X)		52,500	59,500

XII. Profit (Loss) from discontinuing operations		—	—
XIII. Tax expenses of discontinuing operations		—	—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII–XIII)		—	—
XV. Profit (Loss) for the period (XI+XIV)		52,500	59,500
XVI. Earnings per equity shares :			
(1) Basic			
(2) Diluted			

Working Notes :**1. Revenue from Operations :**

Particulars	M (₹)	N (₹)
Sales	1,90,000	1,35,000
Transfer to N	26,000	—
Transfer to M	—	40,000
	2,16,000	1,75,000

2. Cost of Materials Consumed:

Particulars	M (₹)	N (₹)
Opening Inventories	20,000	15,000
Purchases	1,00,000	80,000
Transfer from M	—	26,000
Transfer from N	40,000	—
	1,60,000	1,21,000
Less : Closing Inventories	9,000	13,000
	1,51,000	1,08,000

Statement of Profit & Loss (A Ltd.)*(for the year ended 31st March 2021)*

Particulars	Note No.	Figures for the Current reporting period
		A (₹)
I. Revenue from Operations		3,25,000
II. Other Income		—
III. Total Revenue (I + II)		3,25,000
IV. Expenses :		
Cost of Materials consumed	7	1,93,890
Purchases of stock-in-trade		
Changes in inventories of finished goods, W.I.P. and stock-in-trade		
Employees' benefits expenses	8	20,000
Finance Costs		

Depreciation and amortization and expenses	
Other Expenses	
Total Expenses	2,13,890
V. Profits before exceptional and extraordinary items and tax (III – IV)	1,11,110
VI. Exceptional Items	—
VII. Profit before extraordinary items and tax (V – VI)	1,11,110
VIII. Extraordinary Items	—
IX. Profit before tax (VII – VIII)	1,11,110
X. Tax expenses :	—
(1) Current tax	
(2) Deferred tax	
XI. Profit (Loss) for the period from continuing operations (IX – X)	1,11,110
XII. Profit (Loss) from discontinuing operations	—
XIII. Tax Expenses of discontinuing operations	—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII – XIII)	—
XV. Profit (Loss) for the period (XI + XIV)	1,11,110
XVI. Earnings per equity shares :	
(1) Basic	
(2) Diluted	

Working Notes :

1. Calculation of percentage of Gross Profit to Sales in each department :

	M (₹)	N (₹)
Sales	1,90,000	1,35,000
Transfer of finished goods	20,000	35,000
	2,10,000	1,70,000
$\frac{\text{Gross Profit}}{\text{Total Sales}} \times 100$	$\frac{52,500 \times 100}{2,10,000} = 25\%$	$\frac{59,500 \times 100}{1,70,000} = 35\%$
Finished goods	$\frac{7,000 \times 20}{100} = ₹ 1,400$	$\frac{8,000 \times 20}{100} = ₹ 1,600$
Unrealised Profit in the closing stock	$\frac{1,400 \times 35}{100} = ₹ 490$	$\frac{1,600 \times 25}{100} = ₹ 400$

Total unrealised profit = ₹ 490 + ₹ 400 = ₹ 890;

Calculation of closing stock of manufactured goods of A Ltd.

M Dept. ₹ 7,000 + N Dept. ₹ 8,000 – Unrealised profit ₹ 890 = ₹ 14,110.

2. Total O/S : ₹ 20,000 + 15,000 = ₹ 35,000;
3. Total purchased : ₹ 1,00,000 + 80,000 = ₹ 1,80,000;
4. Total wages : ₹ 12,500 + 7,500 = ₹ 20,000;
5. Total Sales : ₹ 1,90,000 + 1,35,000 = ₹ 3,25,000;
6. Total closing purchased goods : ₹ 2,000 + ₹ 5,000 = ₹ 7,000;

	₹		₹
7. Cost of Materials Consumed :		8. Employees' benefit :	
Opening Inventories	35,000	Wages	<u>20,000</u>
Purchases	<u>1,80,000</u>		
	2,15,000		
Less : Closing Inventories :			
Purchased goods	7,000		
Manufactured goods	<u>14,110</u>		
			<u>21,110</u>
			<u>1,93,890</u>

Q.3. Following are the particulars of three departments of Amar Ltd. :

Departments	Purchases (Units)	Opening Stock (Units)	Closing Stock (Units)
A	1,500	200	100
B	1,000	300	160
C	2,000	150	200

Additional informations:

- (i) Purchases were made at a total cost of ₹ 92,000.
- (ii) The percentage of gross profit on turnover is the same in each department.
- (iii) Purchases and sales prices are constant for the last two years.
- (iv) Selling price per unit :

L	₹ 20
M	₹ 25
N	₹ 30

Prepare Departmental Statement of Profit & Loss in the books of Amar Ltd.

Sol. Statement of Profit & Loss
(for the year ended)

Particulars	Note No.	Figures for the Current reporting period		
		L (₹)	M (₹)	N (₹)
I. Revenue from Operations		32,000	28,500	58,500
II. Other Income		—	—	—
III. Total Revenue (I + II)		<u>32,000</u>	<u>28,500</u>	<u>68,500</u>
IV. Expenses:				
Cost of Materials consumed	1	26,600	22,800	46,800
Purchases of stock-in-trade				
Changes in inventories of finished goods, W.I.P. and stock-in-trade				
Employees' benefits expenses				
Finance Costs				

Depreciation and amortization and expenses			
Other Expenses			
Total Expenses	26,600	22,800	46,800
V. Profit before exceptional and extraordinary items and tax (III – IV)	6,400	5,700	11,700
VI. Exceptional Items	—	—	—
VII. Profit before extraordinary items and tax (III – IV)	6,400	5,700	11,700
VIII. Extraordinary Items	—	—	—
IX. Profit before tax (VII – VIII)	6,400	5,700	11,700
X. Tax Expenses :			
(1) Current tax	—	—	—
(2) Deferred tax	—	—	—
XI. Profit (Loss) for the period from continuing operations (IX – X)	6,400	5,700	11,700
XII. Profit (Loss) from discontinuing operations	—	—	—
XIII. Tax expenses of discontinuing operations	—	—	—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII – XIII)	—	—	—
XV. Profit (Loss) for the period (XI + XIV)	6,400	5,700	11,700
XVI. Earnings per equity shares :			
(1) Basic			
(2) Diluted			

It is assumed that all the units are sold at their respective departmental selling price and there is no closing and opening stocks.

$$L - \text{Units } 1,500 \times ₹ 20 = ₹ 30,000$$

$$M - \text{Units } 1,000 \times ₹ 25 = ₹ 25,000$$

$$N - \text{Units } 2,000 \times ₹ 30 = ₹ 60,000$$

$$\text{Total Sales Price } ₹ 1,15,000$$

$$\text{Gross Profit} = \text{Sale Price } ₹ 1,15,000 - \text{Total Cost } ₹ 92,000 = ₹ 23,000$$

$$\text{Profit percentage on sale price is } \frac{23,000 \times 100}{1,15,000} = 20\%$$

Departmental Costs are :

$$L = ₹ \frac{20 \times 20}{100} = ₹ 4 \text{ Profit; } ₹ 20 \text{ Sale Price} - ₹ 4 \text{ Profit} = ₹ 16 \text{ Cost.}$$

$$M = ₹ \frac{25 \times 20}{100} = ₹ 5 \text{ Profit; } ₹ 25 \text{ Sale Price} - ₹ 5 \text{ Profit} = ₹ 20 \text{ Cost.}$$

$$N = ₹ \frac{30 \times 20}{100} = ₹ 6 \text{ Profit; } ₹ 30 \text{ Sale Price} - ₹ 6 \text{ Profit} = ₹ 24 \text{ Cost.}$$

Working Notes :

1. Opening Stock :

$$200 \text{ Units} \times ₹ 16 \text{ Calculated above} = ₹ 3,200$$

300 Units × ₹ 20 Calculated above = ₹ 6,000

150 Units × ₹ 24 Calculated above = ₹ 3,600

2. Purchases :

1,500 Units × ₹ 16 Calculated above = ₹ 24,000

1,000 Units × ₹ 20 Calculated above = ₹ 20,000

2000 Units × ₹ 24 Calculated above = ₹ 48,000

3. Calculation of Units Sold :

Opening Stock + Purchases - Closing Stock = Units Sold.

Units	Units	Units		Units
L 200 +	1,500 —	100	=	1,600
M 300 +	1,000 —	160	=	1,140
N 150 +	2,000 —	200	=	1,950

4. Units 1,600 Calculated above × ₹ 20 = ₹ 32,000—Sales L

Units 1,140 Calculated above × ₹ 25 = ₹ 28,500—Sales M

Units 1,950 Calculated above × ₹ 30 = ₹ 58,500—Sales N

5. Units 100 × ₹ 16 = 1,600

Units 160 × ₹ 20 = 3,200;

Units 200 × ₹ 24 = 4,800.

6. Testing the accuracy of Gross Profit:

In each case, as per instruction given in the illustration, rate of gross profit in sole is the same.

$$L = \frac{\text{Profit} \times 100}{\text{Sale}} = \frac{6,400 \times 100}{32,000} = 20\%$$

$$M = \frac{\text{Profit} \times 100}{\text{Sale}} = \frac{5,700 \times 100}{28,500} = 20\%$$

$$N = \frac{\text{Profit} \times 100}{\text{Sale}} = \frac{11,700 \times 100}{58,500} = 20\%$$

7. Cost of Materials Consumed :

	L (₹)	M (₹)	N (₹)
Opening Inventories	3,200	6,000	3,600
Purchases	24,000	20,000	48,000
	27,200	26,000	51,600
Less : Closing Inventories	1,600	3,200	4,800
	25,600	22,800	46,800

Q.4. Ravita Ltd. has three departments A, B and C. From the following particulars, calculate gross profit of the company :

Departments	A (₹)	B (₹)	C (₹)
Opening Inventories	24,000	36,000	12,000
Purchases	1,46,000	1,24,000	48,000
Actual Sales	1,72,500	1,59,400	74,600
Gross Profit on Normal Selling Price	20%	25%	33 $\frac{1}{3}$ %

During the year certain items were sold at discount and these discounts were reflected in the values of sales shown above. The items sold at discount were:

Departments	A (₹)	B (₹)	C (₹)
Sales at Normal Selling Price	10,000	3,000	1,000
Sales at Actual Price	7,500	2,400	600

Sol. Statement of Profit & Loss
(for the year ended.....)

Particulars	Note No.	Figures for the Current reporting period		
		A (₹)	B (₹)	C (₹)
I. Revenue from Operations		1,72,500	1,59,400	74,600
II. Other Income		—	—	—
III. Total Revenue (I + II)		1,72,500	1,59,400	74,600
IV. Expenses :				
Cost of Materials consumed	3	1,40,000	1,20,000	50,000
Purchases of stock-in-trade				
Changes in inventories of finished goods, W.I.P. and stock-in-trade				
Employees' benefits expenses				
Finance Costs				
Depreciation and amortization and expenses				
Other Expenses				
Total Expenses		1,40,000	1,20,000	50,000
V. Profit before exceptional and extraordinary items and tax (III – IV)		32,500	39,400	24,600
VI. Exceptional Items		—	—	—
VII. Profit before extraordinary items and tax (V – VI)		32,500	39,400	24,600
VIII. Extraordinary Items		—	—	—
IX. Profit before tax (VII – VIII)		32,500	39,400	24,600
X. Tax Expenses :		—	—	—
(1) Current tax				
(2) Deferred tax				
XI. Profit (Loss) for the period from continuing operations (IX – X)		32,500	39,400	24,600
XII. Profit (Loss) from discontinuing operations		—	—	—
XIII. Tax expenses of discontinuing operations		—	—	—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII – XIII)		—	—	—
XV. Profit (Loss) for the period (XI + XIV)		32,500	39,400	24,600
XVI. Earnings per equity shares :				
(1) Basic				
(2) Diluted				

Working Notes :**1. Ascertainment of Costs of Sales :**

	A (₹)	B (₹)	C (₹)
Sales at Actual Price	1,72,500	1,59,400	74,600
Add : Discount	2,500	600	400
Sales at Normal Price	1,75,000	1,60,000	75,000
Gross Profit on Normal Selling Price	20%	25%	33 1/3%
Cost of Sales as percentages of sales	80%	75%	66 2/3%
Value of cost of sales	1,40,000	1,20,000	50,000

2. Valuation of Closing Stock :

	A (₹)	B (₹)	C (₹)
Opening Stock	24,000	36,000	12,000
Add : Purchases	1,46,000	1,24,000	48,000
	1,70,000	1,60,000	60,000
Less : Cost of sales	1,40,000	1,20,000	50,000
Value of Closing Stock	30,000	40,000	10,000

3. Cost of Materials Consumed :

	A (₹)	B (₹)	C (₹)
Opening Inventories	24,000	36,000	12,000
Purchases	1,46,000	1,24,000	48,000
	1,70,000	1,60,000	60,000
Less : Closing Inventories	30,000	40,000	10,000
	1,40,000	1,20,000	50,000

Q.5. P Limited invoiced goods to its A Branch at cost plus 25% thereon. Both cash and credit sales are affected by the Branch. Branch expenses are paid direct from Head Office, all cash received by the Branch being remitted to Head Office. The following are the details of the transactions for the year ended 31.3.2021 :

	(₹)
Stock at 1.4.2020 at Invoice Price	8,000
Debtors as at 1.4.2020	5,200
Goods received from Head Office, at Invoice Price	40,000
Rents and Rates	600
Salaries and Wages	1,200
Sundry Expenses	300
Credit Sales for the year	30,000
Cash Received on Ledger Accounts	28,500
Returns to Head Office at Invoice Price	800
Stock as at 31.3.2021 at Invoice Price	6,000
Discounts Allowed to Customers	300
Bad Debts Written off	600
Returns from Customers	700
Cash Sales for the year	18,700

Prepare Branch Account and Branch Statement of Profit & Loss in Head Office Books.

Sol. Branch Account (Like Personal Account)
(for the year 2020-21)

	(₹)	(₹)		(₹)	(₹)
To Balance b/d :			By Cash A/c :		
Stock	8,000		(i) Cash Sales	18,700	
Debtors	5,200	13,200	(ii) Amt. Received from		
To Goods Supplied A/c		40,000	Debtors	28,500	47,200
To Cash A/c :			By Goods Supplied A/c		800
Rent, Rates etc.	600		By Closing Balances :		
Salaries & Wages	1,200		Debtors	5,100 ⁵	
Sundry Exps.	300	2,100	Stock	6,000	11,100
To Goods Supplied A/c		160 ¹	By Goods Supplied A/c		8,000 ³
To Difference in the Value of Stock A/c		1,200 ²	By Difference in the Value of Stock A/c		1,600 ⁴
To Statement of Profit & Loss		12,040			
		68,700			68,700

Working Notes :

$$1. \frac{800 \times 25}{125} = ₹160;$$

$$2. \frac{6,000 \times 25}{125} = ₹1,200;$$

$$3. \frac{40,000 \times 25}{125} = ₹8,000;$$

$$4. \frac{8,000 \times 25}{125} = ₹1,600.$$

5. **Branch Debtors Account**

	(₹)		(₹)
To Balance b/d	5,200	By Cash A/c	28,500
To Credit Sales	30,000	By Discount A/c	300
		By Bad Debts	600
		By Returns	700
		By Balance c/d	5,100
	35,200		35,200

Statement of Profit & Loss
(for the year ended 31st March 2021)

Particulars	Note No.	Figures for the Current reporting period
I. Revenue from Operations		48,000
II. Other Income		—
III. Total Revenue (I + II)		48,000
IV. Expenses :		

Cost of Materials consumed	1	32,960
Purchases of stock-in-trade		
Changes in inventories of finished goods, W.I.P. and stock-in-trade		
Employees' benefits expenses	2	1,200
Finance Costs		
Depreciation and amortization and expenses		
Other Expenses	3	1,800
Total Expenses		<u>35,960</u>
V. Profit before exceptional and extraordinary items and tax (III – IV)		12,040
VI. Exceptional items		—
VII. Profit before extraordinary items and tax (V – VI)		12,040
VIII. Extraordinary Items		—
IX. Profit before tax (VII – VIII)		12,040
X. Tax expenses :		
(1) Current tax		—
(2) Deferred tax		—
XI. Profit (Loss) for the period from continuing operations (IX – X)		<u>12,040</u>
XII. Profit (Loss) from discontinuing operations		—
XIII. Tax expenses of discontinuing operations		—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII – XIII)		—
XV. Profit (Loss) for the period (XI + XIV)		<u>12,040</u>
XVI. Earnings per equity shares :		
(1) Basic		
(2) Diluted		

Working Notes :

1. Cost of Materials consumed :	(₹)	2. Other expenses :	(₹)
Opening Stock	6,400	Bad debts	600
Goods Supplied	<u>31,360</u>	Discount	300
	37,760	Rent & Rates	600
Less : Closing stock	<u>4,800</u>	Sundry expenses	<u>300</u>
	<u>32,960</u>		<u>1,800</u>
3. Employees' benefits expenses :			
Salary & wages	<u>1,200</u>		

Q.6. Convert the following Trial Balances as on 31st March, 2021 of the Kolkata Branch which has its Head Office in London:

Particulars	(₹)	(₹)
Stock	12,600	—
Purchases	75,000	—
Sales	—	1,12,500
Debtors	27,000	—

Creditors	—	18,000
Bills Receivable	7,200	—
Bills Payable	—	6,300
Wages and Salaries	4,800	—
Rent, Rates and Taxes	3,600	—
Sundry Charges	1,500	—
Fixtures	5,000	—
Cash at Bank	33,300	—
London A/c	—	33,200
	1,70,000	1,70,000

Stock on 31st March, 2021 was ₹ 22,500. Kolkata Branch (Debit Balance) in London Branch Books was £ 2,880. Fixtures appeared in London Books at £ 350. The rate of exchange on 31st March, 2020 was ₹ 14 and on 31st March, 2021 ₹ 9. The average rate for the year 2020-21 was ₹ 12. Prepare Trading and Profit & Loss Account and Balance Sheet of the Kolkata Branch in Sterling showing how would you deal with the difference in Exchange?

Sol.

Trial Balance of Kolkata Branch

(Converted into Head Office Currency)

(as at 31st March, 2021)

Particulars	Rate of Exchange	Dr. £	Cr. £
	H.O. Figures		
Furniture and Fixtures		350 ¹	
London Office			2,880 ²
Stock in Hand	₹ 14	900 ³	
Debtors	₹ 9	3,000 ⁴	
Creditors	₹ 9		2,000 ⁵
Bills Receivable	₹ 9	800 ⁶	
Bills Payable	₹ 9		700 ⁷
Cash at Bank	₹ 9	3,700 ⁸	
Purchases	₹ 12	6,250 ⁹	
Sales	₹ 12		9,375 ¹⁰
Wages and Salaries	₹ 12	400 ¹¹	
Rent, Rates and Taxes	₹ 12	300 ¹²	
Sundry Charges	₹ 12	125 ¹³	
Difference in Exchange or Exchange Fluctuation Account			870 ¹⁴
		15,825	15,825

Working Notes :

1. This converted amount is already given in the question.
2. This converted amount is also given in the question.
3. $\frac{12,600}{14} = ₹900$;
4. $\frac{27,000}{9} = ₹3,000$;
5. $\frac{18,000}{9} = ₹2,000$;
6. $\frac{7,200}{9} = ₹800$;
7. $\frac{6,300}{9} = ₹700$;
8. $\frac{33,300}{9} = ₹3,700$;
9. $\frac{75,000}{12} = ₹6,250$;
10. $\frac{1,12,500}{12} = ₹9,375$;
11. $\frac{4,800}{12} = ₹400$;
12. $\frac{3,600}{12} = ₹300$;
13. $\frac{1,500}{12} = ₹125$.
14. This amount is the balancing figure.

In Kolkata Branch Books
Trading and Profit & Loss Account
(for the year ended 31st March, 2021)

Particulars	£	Particulars	£
To Opening Stock	900	By Sales	9,375
To Purchases	6,250	By Stock	2,500 ¹
To Wages and Salaries	400		
To Gross Profit c/d	4,325		
	11,875		11,875
To Rent, Rates and Taxes	300	By Gross Profit b/d	4,325
To Sundry Charges	125		
To Net Profit	3,900		
	4,325		4,325

Balance Sheet
(as at 31st March, 2021)

Particulars	£	Particulars	£
Creditors	2,000	Fixtures and Furniture	350
Bills Payable	700	Debtors	3,000
London A/c :		Bills Receivable	800
Balance	2,880	Stock	2,500 ¹
Profit	3,900	Cash at Bank	3,700
Exchange Fluctuation A/c	870		
	10,350		10,350

Working Notes :

1. Conversion of closing stock = $\frac{22,500}{9} = ₹2,500$

Q.7. A Limited Company with its Head Office at Delhi has a Branch Office in Kanpur which obtains supplies, partly from Head Office at cost and partly from outside supplies. The Branch keeps a separate set of Books. On 31st March, 2020, the following Trial Balance was extracted :

Particulars	Head Office		Branch Office	
	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)
Share Capital	—	30,000	—	—
Fixed Assets	16,000	—	8,000	—
Statement of Profit and Loss on 1.10.2019	—	4,000	—	—
Opening Stock at Cost	14,000	—	1,900	—
Trade Receivables and Payables	17,000	10,000	1,500	2,050
Cash	3,000	—	1,000	—
Purchases and Sales	1,20,000	1,40,000	6,750	20,500
Sundry Expenses	15,000	—	2,250	—
Goods from Head Office to Branch	—	12,000	11,500	—
Current A/c on 01.4.2019	11,000	—	—	10,350
	1,96,000	1,96,000	32,900	32,900

The difference between the balances in the Head Office and Branch Current Account is due to goods and cash being in transit at the close of the year. Fixed assets are to be depreciated at 10%. Stocks on 31st March, 2020 were : Head Office, ₹ 10,000 and Branch, ₹ 2,100. Prepare Kanpur Branch Statement of Profit & Loss, the Company's Statement of Profit and Loss for the year ended 31st March, 2020 and its Balance Sheet and Kanpur Branch Account on the same date.

Sol.

In the Books of H.O
Statement of Profit & Loss (Branch)
(for the year ended 31st March, 2020)

Particulars	Note No.	Figures for the Current reporting period
I. Revenue from Operations	1	20,500
II. Other income		—
III. Total Revenue (I + II)		20,500
IV. Expenses :		
Cost of Materials consumed	2	18,050
Purchases of stock-in-trade		
Changes in inventories of finished goods, W.I.P. and stock-in-trade		
Employees' benefits expenses		
Finance Costs		
Depreciation and amortization and expenses		

Other Expenses	3	3,050
Total Expenses		21,100
V. Profit before exceptional and extraordinary items and tax (III – IV)		600
VI. Exceptional Items		—
VII. Profit before extraordinary items and tax (V – VI)		600
VIII. Extraordinary Items		—
IX. Profit before tax (VII – VIII)		600
X. Tax expenses :		
(1) Current tax		—
(2) Deferred tax		—
XI. Profit (Loss) for the period from continuing operations (IX – X)		600
XII. Profit (Loss) from discontinuing operations		—
XIII. Tax expenses of discontinuing operations		—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII – XIII)		—
XV. Profit (Loss) for the period (XI + XIV)		600
XVI. Earnings per equity shares :		
(1) Basic		
(2) Diluted		

Working Notes :

1. Revenue from Operations :	(₹)	2. Cost of Materials Consumed :	(₹)
Sales	<u>20,500</u>	Opening Stock	1,900
		Purchase	6,750
		Goods Received from H.O.	<u>11,500</u>
			20,150
		Less : Closing Stock	<u>2,100</u>
			<u>18,050</u>
3. Other Expenses :	(₹)		
Sundry Expenses	2,250		
Depreciation	<u>800</u>		
	<u>3,050</u>		

Statement of Profit & Loss (H.O.)
(for the year ended 31st March, 2020)

Particulars	Note No.	Figures for the Current reporting period
I. Revenue from Operations	1	1,52,000
II. Other income		—
III. Total Revenue (I + II)		<u>1,52,000</u>
IV. Expenses :		

Cost of Materials consumed	2	1,24,000
Purchases of stock-in-trade		
Changes in inventories of finished goods, W.I.P. and stock-in-trade		
Employees' benefits expenses		
Finance Costs		
Depreciation and amortization and expenses		
Other expenses	3	16,600
Total Expenses		1,40,600
V. Profit before exceptional and extraordinary items and tax (III – IV)		11,400
VI. Exceptional Items		—
VII. Profit before extraordinary items and tax (V – VI)		11,400
VIII. Extraordinary Items		—
IX. Profit before tax (VII – VIII)		11,400
X. Tax expenses :		
(1) Current tax		—
(2) Deferred tax		
XI. Profit (Loss) for the period from continuing operations (IX – X)		11,400
XII. Profit (Loss) from discontinuing operations		—
XIII. Tax expenses of discontinuing operations		—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII – XIII)		—
XV. Profit (Loss) for the period (XI + XIV)		11,400
XVI. Earnings per equity shares :		
(1) Basic		
(2) Diluted		

Working Notes :

1. Revenue from Operations :	(₹)	2. Cost of Materials Consumed :	(₹)
Sales	1,40,000	Opening Stock	14,000
Goods Supplied to Branch	12,000	Purchases	1,20,000
	<u>1,52,000</u>		1,34,000
		Less : Closing Stock	10,000
			<u>1,24,000</u>
3. Other Expenses :			
Sundry Expenses	15,000		
Depreciation	1,600		
	<u>16,600</u>		

Kanpur Branch Account
(for the year ended 31st March, 2020)

	(₹)		(₹)
To Balance b/d	11,000	By Goods in Transit A/c	500
To Branch Trading A/c	22,600	By Cash in Transit A/c	150 ²
To Branch Trade Payables A/c	2,050	By Branch Trading A/c	20,150

	By Branch P. & L. A/c	3,050
	By Branch Fixed Assets A/c	7,200 ³
	By Branch Stock A/c	2,100
	By Branch Trade Receivables A/c	1,500
	By Branch Cash A/c	1,000
		<u>35,650</u>
		<u>35,650</u>

Working Notes :

	(₹)		(₹)
1. Goods from Head Office	12,000	2. Head Office Current A/c	11,000
Less : Goods received by Branch	11,500	Branch Office Current A/c	10,350
Goods in Transit	<u>500</u>	In Transit	650
3. ₹8,000 - $\left(\frac{8,000 \times 10}{100}\right) = ₹7,200.$		Less : Goods in Transit	500
		Cash in Transit	<u>150</u>

Balance Sheet
(as at 31st March, 2020)

Particulars		Note to Account	Figures for the Current reporting period
I.	Equity & Liabilities :		
	Shareholders' funds :		
	Share capital	1	30,000
	Reserves and surplus :		
	Statement of Profit & Loss (surplus)	2	14,800
	Current liabilities :		
	Trade payables	3	12,050
	Total		<u>56,850</u>
II.	Assets :		
	Non-current assets :		
	Fixed assets :		
	Tangible assets	4	21,600
	Current assets :		
	Inventories	5	12,100
	Trade receivables	6	18,500
	Cash and cash equivalents	7	4,000
	Other current assets	8	650
	Total		<u>56,850</u>

Note to Accounts :

1. Shareholders' fund :	(₹)		
Share Capital		30,000	
2. Reserve & Surplus :	(₹)		
Balance b/d (1-10-2019)		4,000	
Add : Current year's profit of H.O.		11,400	
		<u>15,400</u>	
Less :Kranpur Branch P & L (Loss)		600	
		<u>14,800</u>	
4. Tangible assets :	(₹)		
Fixed Assets			
H.O.	16,000		
Less : Depreciation	<u>1,600</u>	14,400	
Branch	8,000		
Less : Depreciation	<u>800</u>	<u>7,200</u>	
		<u>21,600</u>	
6. Trade receivables :	(₹)		
H.O.		17,000	
Branch		<u>1,500</u>	
		<u>18,500</u>	
8. Other current assets :	(₹)		
Goods in transit		500	
Remittance in transit		<u>150</u>	
		<u>650</u>	
3. Trade payables :	(₹)		
Creditors :			
H.O.		10,000	
Branch		<u>2,050</u>	<u>12,050</u>
5. Inventories :	(₹)		
H.O.		10,000	
Branch		<u>2,100</u>	<u>12,100</u>
7. Cash and cash equivalents :	(₹)		
H.O.		3,000	
Branch		<u>1,000</u>	<u>4,000</u>

Q.8. Following are the particulars of three departments of Shiva Ltd. :

Departments	Purchases (Units)	Opening Stock (Units)	Closing Stock (Units)
L	1,500	200	100
M	1,000	300	160
N	2,000	150	200

Additional informations :

- (i) Purchases were made at a total cost of ₹ 92,000.
- (ii) The percentage of gross profit on turnover is the same in each department.
- (iii) Purchases and sales prices are constant for the last two years.
- (iv) Selling price per units :

L Dept.	₹ 20
M Dept.	₹ 25
N Dept.	₹ 30

Prepare Departmental Statement of Profit & Loss in the books of Shiva Ltd.

Sol.

Statement of Profit & Loss*(for the year ended)*

Particulars	Note No.	Figures for the Current reporting period		
		L (₹)	M (₹)	N (₹)
I. Revenue from Operations		32,000	28,500	58,500
II. Other Income		—	—	—
III. Total Revenue (I + II)		32,000	28,500	58,500
IV. Expenses :				
Cost of Materials consumed	1.	26,600	22,800	46,800
Purchases of stock-in-trade				
Changes in inventories of finished goods, W.I.P. and stock-in-trade				
Employees' benefits expenses				
Finance Costs				
Depreciation and amortization and expenses				
Other Expenses				
Total Expenses		26,600	22,800	46,800
V. Profit before exceptional and extraordinary items and tax (III – IV)		6,400	5,700	11,700
VI. Exceptional Items		—	—	—
VII. Profit before extraordinary items and tax (V – VI)		6,400	5,700	11,700
VIII. Extraordinary Items		—	—	—
IX. Profit before tax (VII – VIII)		6,400	5,700	11,700
X. Tax expenses :		—	—	—
(1) Current tax				
(2) Deferred tax				
XI. Profit (Loss) for the period from continuing operations (IX – X)		6,400	5,700	11,700
XII. Profit (Loss) from discontinuing operations		—	—	—
XIII. Tax expenses of discontinuing operations		—	—	—
XIV. Profit (Loss) from discontinuing operations (after tax) (XII – XIII)		—	—	—
XI. Profit (Loss) for the period (XI + XIV)		6,400	5,700	11,700
XVI. Earnings per equity shares :				
(1) Basic				
(2) Diluted				

It is assumed that all the units are sold at their respective departmental selling price and there is no closing and opening stocks.

L—Units 1,500 × ₹ 20 = ₹	30,000
M—Units 1,000 × ₹ 25 = ₹	25,000
N—Units 2,000 × ₹ 30 = ₹	60,000
Total Sale Price ₹	1,15,000

Gross Profit = Sale Price ₹1,15,000 – Total Cost ₹92,000 = ₹23,000

Profit percentage on Sale Price is $\frac{23,000 \times 100}{1,15,000} = 20\%$

Departmental Costs are :

$$L = ₹ \frac{20 \times 20}{100} = ₹ 4 \text{ Profit; } ₹ 20 \text{ Sale Price} - ₹ 4 \text{ Profit} = ₹ 16 \text{ Cost.}$$

$$M = ₹ \frac{25 \times 20}{100} = ₹ 5 \text{ Profit; } ₹ 25 \text{ Sale Price} - ₹ 5 \text{ Profit} = ₹ 20 \text{ Cost.}$$

$$N = ₹ \frac{30 \times 20}{100} = ₹ 6 \text{ Profit; } ₹ 30 \text{ Sale Price} - ₹ 6 \text{ Profit} = ₹ 24 \text{ Cost.}$$

Working Notes :

1. Opening Stock :

200 Units × ₹ 16 Calculated above = ₹ 3,200
 300 Units × ₹ 20 Calculated above = ₹ 6,000
 150 Units × ₹ 24 Calculated above = ₹ 3,600

2. Purchases :

1,500 Units × ₹ 16 Calculated above = ₹ 24,000
 1,000 Units × ₹ 20 Calculated above = ₹ 20,000
 2,000 Units × ₹ 24 Calculated above = ₹ 48,000

3. Calculation of Units Sold

Opening Stock + Purchases – Closing Stock = Units Sold.

	Units	+	Units	–	Units	=	
L	200	+	1,500	–	100	=	1,600
M	300	+	1,000	–	160	=	1,140
N	150	+	2,000	–	200	=	1,950

4. Units 1,600 Calculated above × ₹ 20 = ₹ 32,000—Sales L

Units 1,140 Calculated above × ₹ 25 = ₹ 28,500—Sales M

Units 1,950 Calculated above × ₹ 30 = ₹ 58,500—Sales N

5. Units 100 × ₹ 16 = ₹ 1,600

Units 160 × ₹ 20 = ₹ 3,200;

Units 200 × ₹ 24 = ₹ 4,800.

6. Testing the accuracy of Gross Profit :

In each case, as per instruction given in the illustration, rate of gross profit in sale is the same.

$$L = \frac{\text{Profit} \times 100}{\text{Sale}} = \frac{6,400 \times 100}{32,000} = 20\%$$

$$M = \frac{\text{Profit} \times 100}{\text{Sale}} = \frac{5,700 \times 100}{28,500} = 20\%$$

$$N = \frac{\text{Profit} \times 100}{\text{Sale}} = \frac{11,700 \times 100}{58,500} = 20\%$$

7. Cost of Materials Consumed :

Particulars	L (₹)	M (₹)	N (₹)
Opening Inventories	3,200	6,000	3,600
Purchases	24,000	20,000	48,000
	27,200	26,000	51,600
Less : Closing Inventories	1,600	3,200	4,800
	25,600	22,800	46,800

Q.9. A Delhi Trader has independent branch at Patna. Its Trial Balance for the year ending December 31, 2018 is given below. Pass journal entries to close the books of Patna branch and prepare its Head Office Account.

Trial Balance

Dr.		(for year ended with 31 Dec., 2018)		Cr.	
Particulars	(₹)	Particulars	(₹)		
Purchases	25,600	Creditors	5,400		
Stock on 1-1-18	16,400	Sales	69,900		
Wages	13,100	Head Office	28,000		
Factory Expenses	6,800	Discount	300		
Salaries	8,000	Purchases Returns	600		
Rent	3,400				
Sundry Expenses	4,000				
Goods Received from H.O.	14,400				
Debtors	11,000				
Cash	1,500				
	1,04,200				1,04,200

Additional information :

- The accounts of the branch fixed assets were maintained in the Head Office which show machinery of ₹ 50,000 and furniture of ₹ 2,000.
- Depreciation is to be charged @ 10% on Machinery and 15% on Furniture.
- ₹ 300 are due for salaries.
- A remittance of ₹ 8,000 made by branch on December 29, 2018, was received by head office on January, 3, 2019.
- Closing stock at branch was ₹ 28,700.

**Sol. Books of Patna Branch
Journal**

Date	Particulars	(₹)	(₹)
2018			
Dec. 31	Depreciation A/c Dr. To Hed Office A/c (Being depreciation on fixed assets accounts maintained by Head Office)	5,300	5,300
Dec. 31	Cash in Transit A/c Dr. To Head Office A/c (Being outstanding salaries)	8,000	8,000
Dec. 31	Salaries A/c Dr. To Salaries Outstanding A/c (Being outstanding salaries)	300	300
Dec. 31	Profit & Loss A/c Dr. To Head Office A/c (Being net profit transferred)	2,200	2,200
Dec. 31	Head Office A/c Dr. To Debtors To Cash A/c To Cash in Transit A/c To Closing Stock A/c (Being assets account balance transferred)	49,200	11,000 1,500 8,000 28,700
Dec. 31	Creditors A/c Dr. Salaries Outstanding A/c Dr. To Head Office A/c (Being liabilities account balances transferred)	5,400 300	5,700

Dr.		Head Office Account		Cr.	
Particulars	(₹)	Particulars	(₹)		
To Balance c/d	43,500	By Balance b/d	28,000		
		By Depreciation A/c	5,300		
		By Cash in Transit A/c	8000		
		By Profit & Loss A/c	2,200		
	43,500		43,500		
To Debtors	11,000	By Balance b/d	43,500		
To Cash A/c	1,500	By Creditors	5,400		
To Cash in Transit A/c	8,000	By Salaries outstanding A/c	300		
To Closing Stock A/c	28,700				
	49,200		49,200		

Working Notes :

Dr.		Trading and Profit & Loss Account		Cr.	
		(₹)			(₹)
To Opening Stock A/c		16,400	By Sales		69,900
To Purchases	25,600		By Closing Stock		28,700
Less Return	600	25,000			
To Goods from H.O.		14,400			
To Wages		13,100			
To Factory Expenses		6,800			
To Gross Profit c/d		22,900			
		98,600			98,600
To Salaries	8,000		By Gross Profit b/d		22,900
Add O/s	300	8,300	By Discount		300
To Rent		3,400			
To Depreciation		5,300			
To Sundry Expenses		4,000			
To Net Profit		2,200			
		23,200			23,200

Notes :

- The closing entries for transfer of revenue items have been omitted.
- The balance in Head Office Account after adjustment entries and transfer of net profit is ₹ 43,500. This is equal to the net assets at Patna as given below :

	(₹)	(₹)
Assets		
Debtors	11,000	
Cash	1,500	
Cash in Transit	8,000	
Closing Stock	28,700	
Liabilities :		49,200
Creditors	5,400	
Salaries O/s	300	5,700
Net Assets		43,500

- After the assets and liabilities are transferred to Head Office Account, it stands closed.

□

UNIT-IV

Royalty Accounts & Insolvency Accounts

SECTION-A (VERY SHORT ANSWER TYPE QUESTIONS)

Q.1. Define the term 'Royalty.'

Ans. William Pickles defines royalty as, "Royalty is the remuneration payable to person in respect of the use of an asset, whether hired or purchased from such person, calculated by reference to and varying with quantities produced or sold as a result of such asset."

other definition, "The amount payable according to mutual agreement on the basis of prescribed terms and conditions for consideration of use of any Special Right during a definite period is treated as royalty. This is mostly payable on publishing a book, manufacture, Patented Article or working a mine."

Q.2. Enlist major types of royalties.

Ans. There are many types of royalties but following types of royalties are very popular :

1. Mining royalties
2. Brick-making royalties
3. Oil-wells royalties
4. Patent royalties
5. Copyright royalties
6. Royalties in connection with machines, secret process and technical knowledge, etc;
7. Royalties to foreign companies for sale of produce;
8. Trade mark royalties

Q.3. Explain the difference between rent and royalty.

Ans. Following are the main differences between rent and royalty:

1. Rent is the consideration payable for the use of some tangible asset; tangible asset here means Building and Machinery, etc. Royalty is the consideration payable for the use of special right in a tangible or intangible asset.
2. Rent is mostly payable according to time as per day, per week, per month or per year, etc., but payment of royalty depends on yield or production, etc. In the following cases rent is taken in place of royalty.
 - (a) for taking out or producing various articles from forests;
 - (b) for use of sand from river bed.
 - (c) for taking out fish, etc., from the water.

Q.4. What do you mean by 'minimum rent' with regards to royalty?

Ans. Minimum rent is the amount below which landlord never accepts in any year from the person who has to pay the royalty in case of mines. If this amount is prescribed in the agreement of Royalty then the person who has to receive a royalty will under no circumstances will receive less amount than the amount of minimum rent mentioned in the Agreement. If in any year amount of royalty is less than the amount of minimum rent, it is the amount of minimum rent which will be payable by the person who has to pay the royalty; but if the amount of royalty is more than the amount of minimum rent, royalty will be paid. The intention of the person, who receives royalty, in fixing the minimum rent, is to avoid loss, which may occur if less amount of royalty is there then the normal one. Minimum Rent is also known as Fixed Rent, Dead Rent, Flat Rent or Contract Rent.

Q.5. Explain the term 'Shortworkings.'

Ans. Excess of minimum rent over royalty is called 'Shortworkings'. Minimum Rent – Royalty = Shortworkings or $M. R. - R = S.W.$

Conditions about Shortworkings : In case of Royalty Account mostly following points are mentioned : (i) Rate of Royalty, (ii) Amount of Minimum Rent, (iii) if in any year royalty will be less than minimum rent, the amount of minimum rent will be paid, (iv) when royalty will be more than minimum rent, amount of the Shortworkings of the earlier periods may be recouped out of the excess of royalty over minimum rent. Such amount of shortworkings which may be recouped is known as Redeemable Shortworkings.

Q.6. What is meant by recoupment of Shortworkings?

Ans. There are no legal provisions for writing off shortworkings, all the conditions regarding recoupment or writing off shortworkings are based on the mutual agreement. They may be of the following types :

1. Shortworkings may be recouped in all the future years or it may be recouped throughout the period of lease;
2. It may be recouped during the first four years (or any other period) of the lease. In the case of four years, recoupment will take place only during the first four years and not afterwards, in the fourth year unwritten balance of shortworkings will be transferred to Profit & Loss Account/Statement of P & L and future year's shortworkings will also be transferred to the Profit & Loss Account/Statement of P & L of the concernings year.
3. Each year's shortworkings can be recouped in the following or next two years (or any other period).
4. Shortworkings will not be recouped in future years etc.

Q.7. What is Insolvency Act?

Ans. When a person becomes heavily indebted due to various circumstances and it becomes impossible for him to pay his debts fully, he takes shelter under the Insolvency Act. Under this Act, debtor is exempted from his various debts and his property is sold under the supervision of Government Officer. The amount realised by sale of his property is distributed amongst his creditors according to the provisions of law.

Q.8. What is meant by insolvency?

Ans. Any person, who fulfils the following two conditions, is called insolvent :

1. His liabilities should be more than his assets; and
2. He must be adjudged insolvent by a competent Court.

According to Section 2(8) of the Indian Sale of Goods Act, "A person is said to be 'insolvent' who has ceased to pay his debts in the ordinary course of business, or cannot pay his debts as they become due, whether he has committed an act of insolvency or not."

Q.9. Discuss the relationship among bankruptcy, insolvency and liquidation.

Ans. Following points highlight the relationship among bankruptcy, and liquidation.

1. **Bankruptcy** is a legal proceeding involving a person or business that is unable to repay outstanding debts. The bankruptcy process begins with a petition filed by the debtor, or by the creditors. All of the debtor's assets are measured and evaluated, and the assets may be used to repay a portion of outstanding debt.
2. **Insolvency** in lucid language, if any person or entity is unable to pay off the debts, it owes, to their creditor, on time or as and when they became due and payable, then such person or entity is regarded as "insolvent".
2. Liquidation is the winding up of a corporation or incorporated entity. There are many entities that can initiate proceedings to cause the Liquidation, those being :
 - (i) The Regulatory Bodies;
 - (ii) The Directors of a Company;
 - (iii) The Shareholders of a Company; and
 - (iv) An Unpaid Creditor of a Company.

Q.10. What informations are obtained for claims when account books are destroyed by fire?

Ans. When account books are destroyed by fire, then various informations for insurance claims obtained as under :

1. Particulars of purchases, etc. are taken by obtaining duplicate invoices from suppliers of goods.
2. Duplicate copies of outward invoices are obtained from those customers to whom goods have been sold.
3. Required particulars are obtained from bank.
4. Numerous informations are obtained on the basis of incomplete returns.
5. Other informations are procured from miscellaneous sources and various parties.

Q.11. Explain the points to be noticed while determining loss of stock.

Ans. Following points are noticed while determining loss of stock:

1. What was the stock on the first day of the year in which fire broke out, i.e., what was the opening stock in the concerned year?
2. Purchases which were made upto the date of fire are added in the above opening stock.
3. Cost price of the goods sold upto the date of fire is found out. This cost is deducted from the above total of opening stock and purchases.
4. Salvaged stock is one which has been saved from fire. The value of this saved stock is deducted from the result derived after above mentioned treatment.
5. The balance remaining after above is treated as the amount of loss of stock due to fire.

Q.12. Discuss about the applicability of Insolvency and Bankruptcy Code, 2016.

Ans. The provisions of the Code shall apply for insolvency, liquidation, voluntary liquidation or bankruptcy of the following entities :

1. Any company incorporated under the Companies Act, 2013 or under any previous law.
2. Any other company governed by any special act for the time being in force, except in so far as the said provision is inconsistent with the provisions of such Special Act.
3. Any Limited Liability Partnership under the LLP Act 2008.
4. Any other body incorporated under any law for the time being in force, as the Central Government may by notification specify in this behalf.
5. Partnership firms and individuals.

SECTION-B (SHORT ANSWER TYPE) QUESTIONS

Q.1. Explain the prominent features of the Insolvency and Bankruptcy Code, 2016.

Ans. Features of Insolvency and Bankruptcy Code, 2016

Some of the key features of the IBC are set out below :

1. **Insolvency Resolution** : The Code outlines separate insolvency resolution processes for individuals, companies and partnership firms. The process may be initiated by either the debtor or the creditors. A maximum time limit, for completion of the insolvency resolution process, has been set for corporates and individuals. For companies, the process will have to be completed in 180 days, which may be extended by 90 days, if a majority of the creditors agree. For start ups (other than partnership firms), small companies and other companies (with asset less than 1 crore), resolution process would be completed within 90 days of initiation of request which may be extended by 45 days.
2. **Insolvency regulator** : The Code establishes the Insolvency and Bankruptcy Board of India, to oversee the insolvency proceedings in the country and regulate the entities registered under it. The Board will have 10 members, including representatives from the Ministries of Finance and Law, and the Reserve Bank of India.
3. **Insolvency professionals** : The insolvency process will be managed by licensed professionals. These professionals will also control the assets of the debtor during the insolvency process.
4. **Bankruptcy and Insolvency Adjudicator** : The Code proposes two separate tribunals to oversee the process of insolvency resolution, for individuals and companies: (i) the National Company Law Tribunal for Companies and Limited Liability Partnership firms; and (ii) the Debt Recovery Tribunal for individuals and partnerships.
5. **Institutional Mechanism**: It creates an institutional mechanism for the insolvency resolution process for businesses either by coming up with a viable survival mechanism or by ensuring their prompt liquidation.
6. **Four Pillars** : IBC's institutional infrastructure comprises four pillars, viz., insolvency professionals, information utilities, adjudicating authorities and the insolvency and adjudicating authorities and the Insolvency and Bankruptcy Board of India (IBBI).

Q.2. Discuss the following terms :

(i) Financial information (ii) Corporate person (iii) Corporate applicant

Ans. (i) Financial information : In relation to a person, means one or more of the following categories of information, namely :

- (a) Records of the debt of the person ;
- (b) Records of liabilities when the person is solvent;

- (c) Records of assets of person over which security interest has been created;
 - (d) Records, if any, of instances of default by the person against any debt;
 - (e) Records of the balance sheet and cash-flow statements of the person;
 - (f) Such other informations as many be specified.
- (ii) **Corporate Person:** (a) A company as defined under Sec. 2(20) of the Companies Act, 2013; (b) A Limited Liability Partnership as defined in 2(1)(n) of Limited Liability Act, 2008; or, (c) Any other person incorporated with limited liability under any law for the time being in force but shall not include any financial service provider.
- (iii) **Corporate Applicant: It means :** (a) Corporate debtor, or (b) A member or partner of the corporate debtor who is authorised to make an application for the corporate insolvency resolution process under the constitutional document of the corporate debtor; or (d) A person who has the control and supervision over the financial affairs of the corporate debtor;

Q.3. Explain the priority of claims of the Insolvency and Bankruptcy Code, 2016.

Ans. The Code has significantly changed the priority waterfall for distribution of liquidation proceeds. It may be as follows :

The proceeds from the sale of the liquidation assets shall be distributed in the following order of priority and within such period and in such manner as may be specified, namely :

1. The insolvency resolution process costs and the liquidation costs paid in full;
2. The following debts which shall rank equally between and among the following :
 - (i) workmen's dues for the period of twenty-four months preceding the liquidation commencement date; and
 - (ii) debts owed to a secured creditor in the event such secured creditor has relinquished security in the manner set out in section 52;
3. Wages and any unpaid dues owed to employees other than workmen for the period of twelve months preceding the liquidation commencement date;
4. Financial debts owed to unsecured creditors;
5. The following dues shall rank equally between and among the following :
 - (i) any amount due to the Central Government and the State Government including the amount to be received on account of the Consolidated Fund of India and the Consolidated Fund of a State, if any, in respect of the whole or any part of the period of two years preceding the liquidation commencement date;
 - (ii) debts owed to a secured creditor for any amount unpaid following the enforcement of security interest;
6. Any remaining debts and dues;
7. Preference shareholders, if any; and
8. Equity shareholders or partners, as the case may be.

Q.4. What do you know about Insolvency Law?

Ans. Insolvency Law

In India, insolvency was governed by two Acts namely : The Presidency Towns Insolvency Act, 1909 and the Provincial Insolvency Act, 1920 (before the applicability of Insolvency and Bankruptcy Code, 2016).

The Presidency Towns Insolvency Act, 1909

This Act applies in the Presidency towns of Mumbai, Chennai and Kolkata. The first Insolvency Court in the presidency towns was established in 1828. This Act has 27 Sections and 2 Schedules.

The Provincial Insolvency Act, 1920

It applies in whole of India except the presidency towns of Mumbai (Bombay), Chennai (Madras) and Kolkata (Calcutta). There are 83 sections and 2 Schedules in this Act.

Insolvent According to Insolvency Law

A person cannot be adjudged insolvent unless he is a 'debtor' within the meaning of the insolvency law and has committed an act of insolvency. "Subject to the conditions specified in the Act, if a debtor commits an act of insolvency, an insolvency petition may be presented either by a creditor or by the debtor, and the Court may on such petition make an order adjudging him an insolvent." Acts of Insolvency. A debtor commits an act of insolvency in each of the following cases :

1. If he makes a transfer of his property or any part thereof with intent to defeat or delay his creditors.
2. If he makes any transfer of his property, or of any part thereof which would be void as a fraudulent preference if he were adjudged an insolvent.
3. If with intent to defeat or delay his creditors—he departs or remains out of the territories to which this Act extends, he departs from his dwelling house or usual place of business or otherwise absents himself, he secludes himself so as to deprive his creditors of the means of communicating with him; if any of his property has been sold in execution of the decree of any Court for the payment of money, if he petitions to be adjudged an insolvent under the provisions of this Act, if he gives notice to any of his creditors that he has suspended, or that he is about to suspend payment of his debts, or if, he is imprisoned in execution of any decree of any court for the payment of money.

Q.5. Explain the procedure of realisation of property under Provincial Insolvency Act.

Ans.

Realisation of Property

According to section 20, no doubt Court has power to appoint an interim receiver at the time of making an order admitting the petition, but according to section 56 the Court may, at the time of the order of adjudication, or at any time afterwards, appoint a receiver for the property of the insolvent and the property thereupon shall vest in such receiver.

The Receiver shall realise the property of the debtor and distribute dividends among the creditors entitled thereto.

Interest :

1. On any debt or sum certain whereon interest is not reserved or agreed for, and which is overdue when the debtor is adjudged an insolvent, and which is provable under this Act, the creditor may prove for interest at a rate not exceeding six per cent per annum
 - (i) If the debt or sum is payable by virtue of a written instrument at a certain time, from the time when such debt or sum was payable to the date of such adjudication; or
 - (ii) If the debt or sum is payable otherwise, from the time when a demand in writing has been made giving the debtor notice that interest will be claimed from the date of the demand until the time of payment to the date of such adjudication.
2. Where a debt which has been proved under this Act includes interest or any pecuniary consideration in lieu of interest, or consideration shall, for the purposes of dividend be

calculated at a rate not exceeding six per cent per annum, without prejudice to the right of a creditor to receive out of the debtor's estate any higher rate of interest to which he may be entitled after all the debts proved have been paid in full.

Q.6. Differentiate between profit and loss account and deficiency account.

Ans. Difference between Profit & Loss and Deficiency Account

S.No.	Basis	Profit & Loss Account	Deficiency Account
1.	Date of Preparation	This is often prepared at the end of the financial year.	This is prepared at the time of insolvency.
2.	Period of its Preparation	It is prepared in all the years during which business is carried on.	It is prepared only once in the life of the business and that too, only if insolvency occurs.
3.	Capital	Capital is not recorded in it.	Capital is recorded in it.
4.	Difference	Excess of debit over credit of this account is a loss and excess of credit over debit of this account is profit.	Excess of the amount of right side over the amounts of left side is called deficiency.
5.	Sides	In this account, left side is for expenses and losses and right hand side for gain and income	Its left hand side is for gains and right hand side is for losses.

Q.7. Give a specimen of Deficiency Account.

Ans. Specimen of Deficiency Account

S.No.	Particulars	(₹)	S.No.	Particulars	(₹)
1.	Excess of Assets over Liabilities or Capital		1.	Excess of Liabilities over Assets	
2.	Interest on Capital		2.	Excess of Private Liabilities over Private Assets	
3.	Profits		3.	Loss from Business	
4.	Excess of Private assets over private Liabilities		4.	Drawings	
5.	Profit on assets		5.	Speculation Losses and loss through betting	
6.	Salary or any other remuneration of the Proprietor in Business (if any)		6.	Bad Debts	
7.	Profit in speculation and betting, etc.		7.	Other Losses :	
8.	Exemption from liability			Stock	
9.	Deficiency as per list 'H' in the statement of affairs			Works	
				Furniture	
				Machinery, etc.	
				Bills discounted and dishonoured	
			8.	New Liability	
			9.	Trade Expenses	
			10.	Stock Exchange Exp, etc.	
			11.	Expenses not accounted so far	

Q.8. Differentiate between insolvency of an individual and insolvency of a firm.

Ans. The major difference between Insolvency of an Individual and Insolvency of a Firm are as follows :

S.No.	Basis	Insolvency of Individual	Insolvency of the Firm
1.	Personal Property & Business Property	Here is no distinction between business assets and private assets of the Sole Trader.	Here distinction is made between firm's assets and assets of the partners.
2.	Personal Liability & Business Liability	Here is no distinction between business liability and private liability of the Sole Trader.	Here distinction is made between firm's liabilities and partners' liabilities.
3.	Explanation	Suppose A owes ₹ 10,000 personally and he has a dwelling house of ₹ 8,000. His business liabilities are ₹ 17,000 and business assets ₹ 15,000. In case of his insolvency, his total liabilities and assets respectively will be ₹ 27,000 and ₹ 23,000. Amount of ₹ 23,000 will be distributed prorata among the creditors of ₹ 27,000.	Assets of the firm should be used first for paying the liabilities of the firm and if there is any excess of firm's assets over firm's liabilities, Assets over firm's liabilities, each partner can use his share of this excess to pay his personal liabilities. Assets of the partner will first be used for paying his own liabilities and if there is any excess of his personal assets over his personal liabilities, this excess will be used for paying the liabilities of the firm.

Q.9. What is meant by loss of stocks in insurance claims? Explain about the determination of loss of stock.

Ans. **Loss of Stock**

When fire insurance policy for loss of stock has been taken, business is protected from such loss. For this purpose one has to pay a premium. This policy is mostly for a year, but if the businessman likes, he may take it for a shorter period also. The amount for which policy is taken, is called policy amount. Information about fire loss is given to the insurance company by the insured, Insurance company sends assessors who have technical knowledge relating to the circumstances under which fire broke out and they also determine the amount of loss caused due to this fire. After making complete investigation, they give a report to the insurance company mentioning therein the causes due to which fire broke out and whether the claim is covered by the policy or not. They also mention the value of loss caused due to fire in their report. To determine the amount of loss caused by fire is a difficult task.

Determination of Loss of Stock

1. What was the stock on the first day of the year in which fire broke out, i.e., what was the opening stock in the concerned year?
2. Purchases which were made upto the date of fire are added in the above opening stock.
3. Cost price of the goods sold upto the date of fire is found out. This cost is deducted from the above total of opening stock and purchases.
4. Salvaged stock is one which has been saved from fire. The value of this saved stock is deducted from the result derived after above mentioned treatment.
5. The balance remaining after above is treated as the amount of loss of stock due to fire.

Q.10. Find out the value of stock burnt by fire from the following particulars:

Fire broke out in a factory on 1st October, 2020. Opening Stock on 1st April, 2020 was of ₹ 30,000. Purchases upto the date of fire were ₹ 60,000. The rate of gross profit on sales is 20%. Sales upto date of fire amounted to ₹ 1,00,000.

Sol.

Memorandum Trading Account
(upto the date of fire, i.e., 1st October, 2020)

	(₹)		(₹)
To Opening Stock	30,000	By Sales	1,00,000
To Purchases	60,000	By Closing Stock (Balancing figure)	10,000 ²
To Gross Profit (being 20% of sales)	20,000 ¹		
	1,10,000		1,10,000

From the above account it is clear that value of closing stock on the date of fire is ₹ 10,000.

1. $\frac{1,00,000 \times 20}{100} = ₹ 20,000$; 2. This amount is balancing figure.

Q.11. A fire occurred in the premises of Agra Branch of Ansari Bros. of Mumbai on 1st April, 2021. Stock with the exception of ₹ 9,000 (at cost) was burnt to ashes. The amount of policy was ₹ 40,000. The claim was subject to an average clause. Investigation has disclosed :

- (a) Mumbai Head Office sends goods to Agra Branch at invoice price which is 30% less than catalogue price. Goods are sold to customers at catalogue price which is cost plus 100%
- (b) Goods received from Head Office at invoice price upto 1st April, 2021 amounted to ₹ 2,03,000.
- (c) Goods sold to customers by the Branch at catalogue price upto 1st July, 2021 amounted to ₹ 2,00,000.

Ascertain the amount of claim.

Sol. **Memorandum Trading Account of Agra Branch**
(upto 1st April, 2021)

	(₹)		(₹)
To Goods from H. O. at invoice price	2,03,000	By Sales at Catalogue Price	2,00,000
To Gross Profit (30% on Catalogue Sales)	60,000	By Stock at the date of fire at invoice price (Balancing figure)	63,000
	2,63,000		2,63,000

Stock at the date of fire at actual cost (63,000)	45,000
Less : Salvage value	9,000
Actual Loss of Stock	36,000

$$\text{Claim on Average clause basis} = \frac{\text{Policy Amount}}{\text{Total Value of Stock}} \times \text{Actual Loss}$$

$$\text{Claim} = \frac{40,000}{45,000} \times 36,000 = ₹ 32,000$$

Q.12. Explain loss of profit policy. Explain the process of computation of insurance claim in loss of profit policy.

Ans. Loss of Profit Policy or Consequential Loss Policy

Due to fire, business is dislocated and businessman is not in a position to derive normal profits, hence for loss of profit, a policy is taken which is called loss of profit policy or consequential loss policy. Under this policy only the amount of loss of profit caused due to fire is given by the insurance company, the insured does not get interest on investment or rent on property etc. under this policy.

Indemnity period means a period which commences on the date of damage by fire and ends on the date when normally is restored. This period may be any period but it does not exceed twelve months. Insured decides about this indemnity period. It is necessary that the policy must be in force at the time of loss of fire.

Computation of Insurance Claim in Loss of Profit Policy

Business is dislocated due to fire, hence sales are reduced which in turn leads to decrease in profits. Short sales = Standard sales – Sales in the indemnity period.

Standard sale means the sales of the same period of previous year which is the indemnity period during current year. For example, fire broke out on 1st November, 2020 and indemnity period is from 1st November, 2020 to 31st March, 2021, then the sale for the period from 1st November, 2020 to 31st March, 2020, will be treated as standard sale, but in this sale necessary adjustments for increase or decrease may be made taking the circumstances of the current year into consideration. The amount of actual claim of loss of profit = Short sales × Percentage of gross profit.

Calculation of Percentage of Gross Profit

Gross Profit Rate = $\frac{\text{Insured standing Charges of prev. yr.} + \text{Net profit of prev. yr.}}{\text{Sales of Previous Year}} \times 100$

If there was net loss, then following method is adopted for finding out rate of gross profit.

$\frac{\text{Prev. Year's Insured standing charges} - \text{Net loss of prev. year}}{\text{Sales of Prev. Year}} \times 100$

Net loss is reduced as under when all the standing charges are not insured:

$\frac{\text{Net Loss} \times \text{Insured standing charges}}{\text{All standing charges}}$

Example. If short sales are ₹20,000 and rate of gross profit is 10%. Loss of profit due to short sales is $\frac{20,000 \times 10}{100} = ₹2,000$.

SECTION-C (LONG ANSWER TYPE) QUESTIONS

Q.1. Explain the accounting records for mining royalties in the books of Lessee.

Ans. Accounting Records in the Books of Lessee

(A) When Royalty is less than Minimum Rent

(i) When Royalty is payable

Royalties A/c

Shortworking A/c

Dr.

- To Landlord A/c
(Being royalties earned and shortworkings to be payable to the landlord)
- (ii) When payment is made
- | | |
|---------------------------------|-----|
| Landlord A/c | Dr. |
| To Bank A/c | |
| (Being amount paid to landlord) | |
- (iii) For Closing Royalty Account at the end of the year
- | | |
|---|-----|
| P. & L. A/c Statement of P & L | Dr. |
| To Royalties A/c | |
| (Being the amount of royalties transferred to P. & L. A/c/Statement of P & L) | |
- In place of above first Journal entry, i.e., (i), following two entries may be made:
- (a) Minimum Rent or Dead Rent A/c
- | | |
|--|-----|
| To Landlord A/c | Dr. |
| (Being minimum rent payable to landlord) | |
- (b) Royalties A/c
- | | |
|--|-----|
| Shortworkings A/c | Dr. |
| To Minimum Rent or Dead Rent A/c | Dr. |
| (Being the balance of Minimum Rent A/c or Dead Rent A/c transferred to Royalties and Shortworkings A/cs) | |
- It must be carefully noted that minimum rent or dead rent account is opened only in those years when royalty is less than minimum rent and specific instructions are given in the question for its preparation. Minimum Rent Account is not opened when royalty is equal to minimum rent or more than minimum rent.
- (B) When Royalty is more than Minimum Rent**
- (i) When Royalty is payable
- | | |
|--|-----|
| Royalties A/c | Dr. |
| To Landlord A/c | |
| (Being royalties earned and payable to landlord) | |
- (ii) For writing off Shortworkings, if any
- | | |
|--|-----|
| Landlord A/c | Dr. |
| To Shortworkings A/c | |
| (Being recoupment of S. W. of earlier years) | |
- (iii) For payment of amount
- | | |
|----------------------------------|-----|
| Landlord A/c | Dr. |
| To Bank A/c | |
| (Being payment made to Landlord) | |
- In Place of above (ii) and (iii) entries followings one entry may be passes:
- | | |
|---|-----|
| Landlord A.c | Dr. |
| To Shortworkings A/c | |
| To Bank A/c | |
| (Being recoupment of S. W. to the extent of ₹..... and balance paid to landlord) | |

(iv) For Closing Royalty Account at the end of the year

P. & L. A/c/Statement of P & L

Dr.

To Royalty A/c

(Being transfer of Royalties to P. & L. A/c/Statement of P & L)

(C) When Royalty is equal to Minimum Rent

(i) When Royalty is payable

Royalties A/c

Dr.

To Landlord A/c

(Being royalties earned and payable to landlord)

(ii) When payment is made

Landlord A/c

Dr.

To Bank A/c

(Being payment made to landlord)

(iii) When Royalty Account is closed at the end of the year

P. & L. A/c/Statement of P & L

Dr.

To Royalty A/c

(Being transfer of Royalties to P. & L. A/c/Statement of P & L)

Q.2. On 1.4.2017, the Arnav Colliteries Ltd. took a piece of land on lease. A minimum rent of ₹2,000 in the first year, ₹4,000 in the second year, and thereafter ₹6,000 per annum, is to be merging into a Royalty of 40 paise per ton, with power to recoup Shortworkings over the first years of the lesse only. The figures of annual output for the years from 1.4.2017 to 31.3.2021, were 1,000, 10,000, 18,000 and 20,000 ton respectively. Open the necessary accounts in the books of the Lessee.

Sol. In the Book of Arnav Colliteries Ltd.

Analytical Table

Year	Output	Royalties @ 40 P. per ton	Minimum Rent	Short-workings	Short-workings Recouped	Amount Paid	Unrecouped Shortworkings transferred to Statement of P & L
	Ton	(₹)	(₹)	(₹)	(₹)	(₹)	(₹)
2017-18	1,000	400	2,000	1,6000	—	2,000	—
2018-19	10,000	4,000	4,000	—	—	4,000	—
2019-20	18,000	7,200	6,000	—	1,200	6,000	400
2020-21	20,000	8,000	6,000	—	—	8,000	—

Royalties Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2018		
Mar. 31	To Landlord A/c	400	Mar. 31	By Statement of P & L	400

2019			2019		
Mar. 31	To Landlord A/c	4000	Mar. 31	By Statement of P & L	4,000
2020			2020		
Mar. 31	To Landlord A/c	7,200	Mar. 31	By Statement of P & L	7,200
2021			2021		
Mar. 31	To Landlord A/c	8,000	Mar. 31	By Statement of P & L	8,000

Landlord Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2018		
Mar. 31	To Cash A/c	2,000	Mar. 31	By Royalties A/c	400
		2,000	Mar. 31	By Shortworkings A/c	1,600
					2,000
2019			2019		
Mar. 31	To Cash A/c	4,000	Mar. 31	By Royalties A/c	4,000
		4,000			4,000
2020			2020		
Mar. 31	To Shortworkings A/c	1,200	Mar. 31	By Royalties A/c	7,200
	To Cash A/c	6,000			7,200
		7,200			
2021			2021		
Mar. 31	To Cash A/c	8,000	Mar. 31	By Royalties A/c	8,000

Shortworkings Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2018		
Mar. 31	To Landlord A/c	1,600	Mar. 31	By Balance c/d	1,600
2018			2019		
Apr. 1	To Balance b/d	1,600	Mar. 31	By Balance c/d	1,600
2019		1,600	2020		1,600
Apr. 1	To Balance b/d	1,600	Mar. 31	By Landlord A/c	1,200
		1,600	Mar. 31	By Statement of P & L	400
					8,000

Q.3. A Coal Company takes a lease of coal mine for a term of 8 years from 1st April, 2018 on a minimum rent of ₹12,000 per year merging in a royalty of 75 paise per ton of coal raised payable half-yearly on 30th Sep. and 31st March each year. Shortworkings can be recouped during the first three years of the lease only. Royalty which was due on 31st March, 2020 was paid on 2nd April, 2020. Coal Company closes its books on 31st March each year. Coal is raised as ahead :

	Ton
Half-year ending at 30th Sep., 2018	6,000
Half-year ending at 31st March, 2019	8,000

Half-year ending at 30th Sep., 2019	10,000
Half-year ending at 31st March, 2020	6,000
Half-year ending at 30th Sep., 2020	7,000
Half-year ending at 31st March, 2016	9,000

Prepare necessary accounts in the books of Coal Company.

Sol.

Analytical Table

Half-year	Ton	Royalty	Minimum Rent for half-year	Short-workings	Short-workings Recouped	Shortworkings Unrecouped transferred to Statement of P & L
		(₹)	(₹)	(₹)	(₹)	(₹)
30th Sept., 2018	6,000	4,500	6,000	1,500	—	—
31st Mar., 2019	8,000	6,000	6,000	—	—	—
30th Sept., 2019	10,000	7,500	6,000	—	1,500	—
31st Mar., 2020	6,000	4,500	6,000	1,500	—	—
30th Sept., 2020	7,000	5,250	6,000	750	—	—
31st Mar., 2021	9,000	6,750	6,000	—	750	1,500

Working Note :

Minimum Rent is ₹ 12,000 for one year, but for half year it is only ₹ 12,000 ÷ 2 = ₹ 6,000, hence this amount of ₹ 6,000 has been taken into consideration here.

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2018		
Sept. 30	To Bank A/c	6,000	Sept. 30	By Royalty A/c	4,500
			Sept. 30	By Shortworkings A/c	1,500
2019			2019		
Mar. 31	To Bank A/c	6,000	Mar. 31	By Royalty A/c	6,000
		12,000			12,000
2019			2019		
Sept. 30	To Bank A/c	6,000	Sept. 30	By Royalty A/c	7,500
Sept. 30	To Shortworkings A/c	1,500	2020		
Mar. 31	To Bank c/d	6,000	Mar. 31	By Royalty A/c	4,500
		13,500	Mar. 31	By Shortworkings A/c	1,500
					13,500
2020			2020		
Apr. 2	To Bank A/c	6,000	Apr. 1	By Balance b/d	6,000
Sept. 30	To Bank A/c	6,000	Sept. 30	By Royalty A/c	5,250
2021			Sept. 30	By Shortworkings A/c	750
Mar. 31	To Bank A/c	6,000	2021		
Mar. 31	To Shortworkings A/c	750	Mar. 31	By Royalty A/c	6,750
		18,750			18,750

Shortworkings Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2019		
Sept. 30	To Landlord A/c	1,500	Mar. 31	By Balance c/d	1,500
2019			2019		
Apr. 1	To Balance b/d	1,500	Sept. 30	By Landlord A/c	1,500
2020			2020		
Mar. 31	To Balance b/d	1,500	Mar. 31	By Balance c/d	1,500
		3,000			3,000
2020			2021		
Apr. 1	To Balance b/d	1,500	Mar. 31	By Landlord A/c	750
Sept. 30	To Landlord A/c	750	Mar. 31	By Statement of P & L	1,500
		2,250			2,250

Royalty Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018			2019		
Sept. 30	To Landlord A/c	4,500	Mar. 31	By Statement of P & L	10,500
2014					
Mar. 31	To Landlord A/c	6,000			
		10,500			10,500
2019			2020		
Sept. 30	To Landlord A/c	7,500	Mar. 31	By Statement of P & L	12,000
2020					
Mar. 31	To Landlord A/c	4,500			
		12,000			12,000
2020			2021		
Sept. 30	To Landlord A/c	5,250	Mar. 31	By Statement of P & L	12,000
2021					
Mar. 31	To Landlord A/c	6,750			
		12,000			12,000

Q.4. Amar took a mine for lease for 15 years @ 50 paise per ton. Minimum Rent per year is fixed at ₹ 4,000. Shortworkings can be recouped in the first four years of the lease. The tonnage raised from the mine has been as follows :

6,000 ton in I year; 9,000 ton in II year; 5,000 ton in III year; 10,000 ton in IV year and 8,000 ton in V year.

It is decided to create Shortworkings Reserve Account for an amount equal to that of shortworkings. Pass the necessary Journal entries in the books of Lessee Amar and prepare S.W. Reserve Account, Shortworkings Account, Profit and Loss Account and Balance Sheet. Books are closed every year on 31st March.

Sol.

Analytical Table

Year	Ton	Royalty	Minimum Rent (₹)	Shortworkings (₹)	Writing-off S.W. (₹)
I Yr.	6,000	3,000	4,000	1,000	—
II Yr.	9,000	4,500	4,000	—	500
III Yr.	5,000	2,500	4,000	1,500	—
IV Yr.	10,000	5,000	4,000	—	1,000
V Yr.	8,000	4,000	4,000	—	—

Journal Entries in the books of Amar (Lessee)

Date	Particulars	L.F.	Amount (₹)	Amount (₹)
1st Yr.				
Mar. 31	Royalty A/c S.W. A/c To Landlord A/c (Being Royalty and Shortworkings due and payable to Landlord)	Dr. Dr.	3,000 1,000	4,000
Mar. 31	Landlord A/c To Bank A/c (Being payment made)	Dr.	4,000	4,000
Mar. 31	P & L A/c To Shortworkings Reserve A/c (Being creation of Shortworkings Reserve A/c)	Dr.	1,000	1,000
Mar. 31	Profit and Loss A/c To Royalty A/c (Being transfer to Royalty to P & L A/c)	Dr.	3,000	3,000
2nd Yr.				
Mar. 31	Royalty A/c To Landlord A/c (Being Royalty due and payable to Landlord)	Dr.	4,500	4,500
Mar. 31	Landlord A/c To S.W. A/c To Bank A/c (Being S.Ws. recouped & Payment made to Landlord)	Dr.	4,500	500 4,000
Mar. 31	S.W. Reserve A/c To P & L A/c (Being transfer of recouped Shortworkings to P & L A/c)	Dr.	500	500
Mar. 31	P & L A/c To Royalty A/c (Being transfer of Royalty to P & L A/c)	Dr.	4,500	4,500
3rd Yr.				
Mar. 31	Royalty A/c S.W. A/c To Landlord A/c (Being Royalty & Shortworkings due & payable to landlord)	Dr. Dr.	2,500 1,500	4,000

Mar. 31	Landlord A/c Bank A/c (Being payment made)	Dr.	4,000	4,000
Mar. 31	P & L A/c To S.W. Reserve A/c (Being creation of Shortworkings Reserve Account)	Dr.	1,500	1,500
Mar. 31	P & L A/c To Royalty A/c (Being transfer of Royalty to P & L A/c)	Dr.	2,500	2,500
4th Yr. Mar. 31	Royalty A/c To Landlord A/c (Being Royalty due and payable to Landlord)	Dr.	5,000	5,000
Mar. 31	Landlord A/c To S. W. A/c To Bank A/c (Being recoupment of Shortworkings and payment made)	Dr.	5,000	1,000 4,000
Mar. 31	S.W. Reserve A/c To P. & L. A/c (Being transfer of recouped Shortworkings to P & L A/c)	Dr.	1,000	1,000
Mar. 31	P & L A/c To Royalty A/c (Being transfer of Royalty)	Dr.	5,000	5,000
Mar. 31	S.W. Reserve A/c To S.W. A/c (Being writing off unrecoupable Shortworkings)	Dr.	1,000	1,000
5th Yr. Mar. 31	Royalty A/c To Landlord A/c (Being transfer of recouped Shortworkings to P & L A/c)	Dr.	4,000	4,000
Mar. 31	Landlord A/c To Bank A/c (Being payment made)	Dr.	4,000	4,000
Mar. 31	P & L A/c To Royalty A/c (Being transfer of Royalty to P & L A/c)	Dr.	4,000	4,000

Shortworkings Reserve Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
I Yr. Mar. 31	To Balance c/d	1,000	I Yr. Mar. 31	By P & L A/c	1,000
II Yr. Mar. 31	To P & L A/c	500	II Yr. Apr. 1	By Balance b/d	1,000
Mar. 31	To Balance c/d	500			1,000
		1,000			
III Yr. Mar. 31	To Balance c/d	2,000	III Yr. Apr. 1	By Balance b/d	500

IV. Yr. Mar. 1 Sep.30	To P & L A/c To Shortworkings A/c	2,000	Mar. 31	By P & L A/c	1,500	
		1,000	IV. Yrs. Apr. 1	By Balance b/d	2,000	
		1,000				
		2,000				

Shortworkings Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
I Yr. Mar. 31	To Landlord A/c	1,000	I Yr. Mar. 31	By Balance c/d	1,000
II Yr. Apr. 1	To Balance b/d	1,000	II Yr. Mar. 31	By Landlord A/c	500
		1,000	Mar. 31	By Balance c/d	500
III Yr. Apr. 1	To Balance b/d	500			1,000
Mar. 31	To Landlord A/c	1,500	III Yr. Apr. 1	By Balance c/d	2,000
		2,000			2,000
IV Yr. Apr. 1	To Balance b/d	2,000	IV Yr. Mar. 31	By Landlord A/c	1,000
		2,000	Mar. 31	By S.W. Reserve A/c	1,000
					2,000

Profit & Loss Account

(for the year ended 31st March of I yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
To S.W. Reserve A/c	1,000		
To Royalty A/c	3,000		

Balance Sheet

(as at 31st March of I yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
S.W. Reserve	1,000	Shortworkings	1,000

Profit & Loss Account

(for the year ended 31st March of II yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
To Royalty A/c	4,500	By S.W. Reserve A/c	500

Balance Sheet
(as at 31st March of II yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
S.W. Reserve	500	Shortworkings	500

Profit & Loss Account
(for the year ended 31st March of III yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
To S.W. Reserve A/c	1,500		
To Royalty A/c	2,500		

Balance Sheet
(as at 31st March of III yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
S.W. Reserve	2,000	Shortworkings	2,000

Profit & Loss Account
(for the year ending at 31st March of IV yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
To Shortworkings A/c	1,000	By S.W. Reserve A/c	1,000

Balance Sheet
(as at 31st March of IV yr.)

No item of Balance Sheet is during this year

Profit & Loss Account
(for the year ending at 31st March of V yr.)

Particulars	Amount (₹)	Particulars	Amount (₹)
To Royalty A/c	4,000		

Q.5. Discuss the accounting records in the books of landlord and royalty reserve.

Ans. Accounting Records in the Books of Landlord and Royalty Reserve

Landlord transfers the excess of minimum rent over royalty to Royalty Reserve Account or Royalty Suspense Account. The same account is known as Shortworkings Account in the books of Lessee.

1. When Royalty is less than Minimum Rent

(a) At the time when royalty is receivable :

Lessee A/c

To Royalties Receivable A/c or Royalties A/c

To Royalty Reserve or Royalty Suspense A/c

Dr.

(Being the amount of royalties receivable earned and the difference between minimum rent and royalties receivable transferred to Royalty Reserve A/c)

(b) When above amount is received :

Bank A/c Dr.

To Lessee A/c

(Being the amount received from Lessee)

(c) For closing Royalty Receivable Account :

Royalties Receivable A/c or Royalties A/c Dr.

To P & L A/c/Statement of P & L

(Being transfer of Royalties Receivable A/c to P & L A/c/Statement of P & L)

2. When Royalty is more than Minimum Rent

(a) At the time when royalty is receivable :

Lessee A/c Dr.

To Royalties Receivable A/c

(Being the amount of Royalties Receivable earned)

(b) For writing off Royalty Reserve A/c :

Royalty Reserve or Royalty Suspense A/c Dr.

To Lessee A/c

(Being Royalty Reserve recouped)

(c) On receipt of Royalty Amount :

Bank A/c

To Lessee A/c Dr.

(Being receipt of amount from lessee)

(d) Following entry may be passed in place of above two entries (b) and (c) :

Royalty Reserve or Royalty Suspense A/c Dr.

Bank A/c Dr.

To Lessee A/c

(Being the amount of Royalty Reserve ₹ recouped and the balance received from Lessee)

(e) For closing Royalty Receivable Account :

Royalties Receivable A/c or Royalties A/c Dr.

To P & L A/c/Statement of P & L

(Being transfer of Royalties Receivable A/c to P & L A/c/Statement of P & L)

3. When Royalty receivable is equal to Minimum Rent

(a) At the time when royalty is receivable :

Lessee A/c Dr.

To Royalties Receivable A/c or Royalties A/c

(Being the amount of royalty receivable earned)

(b) On receipt of amount :

Bank A/c Dr.

To Lessee A/c

(Being receipt of amount from lessee)

(c) For closing the Account of Royalties Receivable :

Royalties Receivable A/c or Royalties A/c
To P & L A/c/Statement of P & L

Dr.

(Being transfer of Royalties Receivable A/c to P & L A/c/Statement of P & L)

Q.6. A took a mine under a lease. Royalty is ₹1 per ton and minimum rent is ₹12,000 per annum. Each year's shortworking is recoverable during the subsequent two years. If any year the normal rent was not attained due to strike, the minimum rent was to be regarded as having been reduced proportionately having regard to the length of the stoppage. The output was as follows :

	Ton
2016-17	10,000
2017-18	9,000
2018-19	13,000
2019-20	8,000
2020-21	12,000

During the year 2019-20, there was a strike for five months. Prepare landlord account and shortworkings account in the books of A. Each year A's books are closed on 31st March.

Sol.

Analytical Table

Years	Output in Ton	Royalty	Minumum Rent	Short-workings	Recoupment of S.W.	Irrecouped Shortworkings transferred to Statement of P & L
		(₹)	(₹)	(₹)	(₹)	(₹)
2016-17	10,000	10,000	12,000	2,000	—	—
2017-18	9,000	9,000	12,000	3,000	—	—
2018-19	13,000	13,000	12,000	—	1,000	1,000
2019-20	8,000	8,000	7,000	—	1,000	2,000
2020-21	12,000	12,100	12,000	—	—	—

* Minimum rent = $\frac{12,000 \times 5}{12} = ₹ 5,000$; ₹ 12,000 - 5,000 = ₹ 7,000.

In the Books of A
Landlord Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017			2017		
Mar. 31	To Bank A/c	12,000	Mar. 31	By Royalty A/c	10,000
			Mar. 31	By S.W. A/c	2,000
		12,000			12,000
2018					
Mar. 31	To Bank A/c	12,000	Mar. 31	By Royalty A/c	9,000

			Mar. 31	By S.W. A/c	3,000
		12,000			12,000
2019			2019		
Mar. 31	To S.W. A/c	1,000	Mar. 31	By Royalty A/c	13,000
Mar. 31	To Bank A/c	12,000			
		13,000			13,000
2020			2020		
Mar. 31	To S.W. A/c	1,000	Mar. 31	By Royalty A/c	8,000
Mar. 31	To Bank A/c	7,000			
		8,000			8,000
2021			2021		
Mar. 31	To Bank A/c	12,000	Mar. 31	By Royalty A/c	12,000

Shortworkings Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2017			2017		
Mar. 31	To Landlord A/c	2,000	Mar. 31	By Balance c/d	2,000
2017			2018		
Apr. 1	To Balance b/d	2,000	Mar. 31	By Balance c/d	5,000
2018					
Mar. 31	To Landlord A/c	3,000			5,000
		5,000			
2018			2019		
Apr. 1	To Balance b/d	5,000	Mar. 31	By Landlord A/c	1,000
			Mar. 31	By P & L A/c	1,000
			Mar. 31	By Balance c/d	3,000
		5,000			5,000
2019			2020		
Apr. 1	To Balance b/d	3,000	Mar. 31	By Landlord	1,000
			Mar. 31	To P & L A/c	2,000
		3,000			3,000

Q.7. On April 1, 2012, Sanjay Brick Co. acquired a lease for 15 years from Anand on lease for taking oil soil. Terms of the lease are : (i) Annual rate of Royalty is 5 Paise per 100 cubic feet of soil taken out. (ii) Minimum Rent per year is ₹1,200. (iii) On 1st April, 2012 company gave ₹3,000 to Anand for nazrana. (iv) Shortworkings can be recouped in future out of excess royalty during the first four years of the lease only. (v) Annual royalty is paid every year on 31st March, Brick-making company extracted soil in the following manner :

Years	2012-13	2013-14	2014-15	2015-16
Soil in Cubic feet	20,00,000	30,00,000	18,00,000	28,00,000

Open Nazrana Account, Royalty Account and S.W. Account in the books of Brick-making Company.

Sol. Analytical Table

Year	Earth in Cubic Feet	Royalty	M. Rent	Short-workings	Shortworkings Recouped	Unrecouped S.W. transferred to Statement of P & L
		(₹)	(₹)	(₹)	(₹)	(₹)
2012-13	20,00,000	1,000 ¹	1,200	200	—	—
2013-14	30,00,000	1,500 ²	1,200	—	200	—
2014-15	18,00,000	900 ³	1,200	300	—	—
2015-16	28,00,000	1,400 ⁴	1,200	—	200	100

Working Notes :

$$1. \frac{5 \times 2,00,000}{100 \times 100} = ₹ 1,000$$

$$2. \frac{5 \times 30,00,000}{100 \times 100} = ₹ 1,500$$

$$3. \frac{5 \times 18,00,000}{100 \times 100} = ₹ 900$$

$$4. \frac{5 \times 28,00,000}{100 \times 100} = ₹ 1,400$$

Nazrana Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2012			2012		
Apr. 1	To Bank A/c	3,000	Mar. 31	By Statement of P & L	200
			Mar. 31	By Balance c/d	2,800
		3,000			3,000
2013			2014		
Apr. 1	To Balance b/d	2,800	Mar. 31	By Statement of P & L	200
			Mar. 31	By Balance c/d	2,600
		2,800			2,800
2014			2015		
Apr. 1	To Balance b/d	2,600	Mar. 31	By Statement of P & L	200
			Mar. 31	By Balance c/d	2,400
		2,600			2,600
2015			2016		
Apr. 1	To Balance b/d	2,400	Mar. 31	By Statement of P & L	200
			Mar. 31	By Balance c/d	2,200
		2,400			2,400

Amount of ₹ 3,000 is Nazrana for 15 years, hence Nazrana for one year is : $\frac{3,000}{15} = ₹ 200$.

Anand's Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2013			2013		
Mar. 31	To Bank A/c	1,200	Mar. 31	By Royalties A/c	1,000
				By Shortworkings A/c	200
		1,200			1,200
2014			2014		
Mar. 31	To Shortworkings A/c	200	Mar. 31	By Royalties A/c	1,500
Mar. 31	To Bank A/c	1,300			
		1,500			1,500
2015			2015		
Mar. 31	To Bank A/c	1,200	Mar. 31	By Royalties A/c	9,00
			Mar. 31	By Shortworkings A/c	300
		1,200			1,200
2016			2016		
Mar. 31	To Shortworkings A/c	200	Mar. 31	By Royalties A/c	1,400
Mar. 31	To Bank A/c	1,200			
		1,400			1,400

Shortworkings Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2013			2013		
Mar. 31	To Anand	200	Mar. 31	By Balance c/d	200
2014			2014		
Ap. 1	To Balance b/d	200	Mar. 31	By Anand	200
2015			2015		
Mar. 31	To Anand	300	Mar. 31	By Balance c/d	300
2015			2016		
Apr. 1	To Balance b/d	300	Mar. 31	By Anand	200
			Mar. 31	By P & L A/c	100
		300			300

Q.8. Dr. Chaudhary wrote a book on Accountancy and gave the right of its printing and sale to Kapil & Co. on the following terms. The accounts of Kapil & Co. are closed on 31st March each year : (i) Royalty is 10% on the printed price of sold books; (ii) Price of each printed book is ₹ 30; (iii) Each year's royalty is paid on 30th April of the following year. Following account is given by Kapil & Co. to Dr. Chaudhary.

Year	Printed Books	Specimen given	Wasted Books	Closing Stock
2018-19	8,000	200	100	700
2019-20	10,000	300	100	600
2020-21	15,000	500	200	300

Open the necessary accounts in the books of Kapil & Co.

Sol. (2018-19)

Printed Books		8,000
Less : Specimen		200
Wastage		100
Closing Stock		700
		1,000
	Books sold	7,000

$$7,000 \times 30 = ₹ 2,10,000; \frac{2,10,000 \times 10}{100} = ₹ 21,000 \text{ (Royalty)}$$

(2019-20)

Last year's Closing Stock is treated as Opening Stock of Current Year.

Opening Stock ₹ 700 + Printed Books ₹ 10,000		10,700
Less : Specimen		300
Wastage		100
Closing Stock		600
		1,000
	Books sold	9,700

$$9,700 \times 30 = ₹ 2,91,000; \frac{2,91,000 \times 10}{100} = ₹ 29,100 \text{ (Royalty)}$$

Last year's Closing Stock is treated as Opening Stock of this year.

Opening Stock ₹ 600 + Printed Books ₹ 15,000		15,600
Less : Specimen		500
Wastage		200
Closing Stock		300
		1,000
	Books sold	14,600

$$14,600 \times 30 = ₹ 4,38,000; \frac{4,38,000 \times 10}{100} = ₹ 43,800 \text{ (Royalty)}$$

**In the Books of Kapil & Co.
Dr. Chaudhary's Account**

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019			2019		
Mar. 31	To Balance c/d	21,000	Mar. 31	By Royalty A/c	21,000
2019			2019		
Apr. 30	To Bank A/c	21,000	Apr. 1	By Balance b/d	21,000
2020			2020		
Mar. 31	To Balance c/d	29,100	Mar. 31	By Royalty A/c	29,100
		50,100			50,100
2020			2020		
Apr. 30	To Bank A/c	29,100	Apr. 1	By Balance b/d	29,100

2021 Mar. 31	To Balance c/d	43,800	2021 Mar. 31	By Royalty A/c	43,800
		72,900			72,900
2021 Apr. 30	To Bank A/c	43,800	2021 Apr. 1	By Balance b/d	43,800

Royalty Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2019 Mar. 31	To Dr. Chaudhary's A/c	21,000	2019 Mar. 31	By Statement of P & L	21,000
2020 Mar. 31	To Dr. Chaudhary's A/c	29,100	2020 Mar. 31	By Statement of P & L	29,100
2021 Mar. 31	To Dr. Chaudhary's A/c	43,800	2021 Mar. 31	By Statement of P & L	43,800

Q.9. Explain the procedure of insolvency.

Ans.

Procedure of Insolvency

- Petition for adjudication as insolvent may be presented either by the debtor or by the creditor in a Court having jurisdiction under this Act. This petition must be in writing and verified in the prescribed manner.
- A creditor shall not be entitled to present an insolvency petition against a debtor unless :
 - The debts owing by the debtors to the creditor, or, if two or more creditors join in the petition, the aggregate amount of debts owing to such creditors, amounts to five hundred rupees, and
 - The debt is a liquidated sum payable either immediately or at some certain future time, and
 - The act of insolvency on which the petition is grounded has occurred within three months before the presentation of petition.
- A debtor shall not be entitled to present an insolvency petition unless he is unable to pay his debts, and.
 - his debts amount to five hundred rupees; (ii) he is under arrest or imprisonment in execution of the decree of any Court for the payment of money, or (iii) an order of attachment in execution of such decree has been made and is subsisting against his property.
- When an insolvency petition has been accepted, the Court shall make an order fixing a date for hearing the petition.
- When Court makes an order for admitting the petition, it may appoint an interim receiver of the property of the debtor and may direct him to take immediate-possession thereof.
- The debtor shall on making of an order admitting the petition produce all books of account, and shall at any time thereafter give such inventories of his property, and such lists of his creditors and debtors and of the debts due to and from them, respectively,

submits to such examination in respect of his property or his creditors as may be prescribed.'

7. If the Court is satisfied that the petition is reasonable, it shall make an order of adjudication and shall specify in such order the period within which the debtor shall apply for his discharge.
8. Effect of an Order of Adjudication : (i) on making the order of adjudication, the whole of the property of the insolvent shall vest in the Court or in a Receiver and shall become divisible among the creditors, (ii) the insolvent shall aid to the utmost of his power in the realisation of his property and the distribution of his proceeds among his creditors.
9. Order of adjudication stating the name, address and description of the insolvent, the date of adjudication etc. shall be published in the Official Gazette.
10. A debtor may, at any time after the order of adjudication and within the period specified by the Court, apply to the Court for an order of discharge, the Court shall fix a day for hearing such application.
11. The Court may, after considering the objections of any creditor and where a receiver has been appointed, the report of the Receiver grant or refuse an absolute order of discharge.
12. Effect of Order of Discharge. An order of discharge shall release the insolvent from all debts provable under this Act, but it will not release the insolvent from :
 - (i) any debt due to the Government, (ii) any debt or liability incurred by means of any fraud or fraudulent breach of trust to which he was a party, (iii) any debt or liability in respect of which he has obtained for bearance by any fraud to which he was a party, or (iv) any liability under an order for maintenance made under section 488 of the Code of Criminal Procedure Act, 1898.

Q.10. Some of the liabilities of Ram, who filed his petition for insolvency on 1st Jan, 2012 are given below:

Particulars	(₹)
(i) Director's three months' salaries	12,000
(ii) Rent of landlord for four months	300 p.m.
(iii) Managing Director's three months' salary	5,000 p.m.
(iv) Income tax	7,000
(v) Half month's ground rent	400 p.m.
(vi) House and water tax	3,000
(vii) Manager's salary	3,000
(viii) Sales tax	1,000
(ix) Salaries and wages of servants and labourers according to the following descriptions:	
C— for Nov. and Dec. 2015—₹ 200 p.m.	
D— for Sept. Oct, Nov, and Dec. 2015—₹ 300 p.m.	
E—for July, Aug & Sept. 2015—₹ 200 p.m.	
F—for Nov, and Dec. 2015— ₹ 100 p.m.	
G—for July to Dec. 2015— ₹ 100 p.m.	
(x) Clerks' salaries as per following descriptions :	
H—for Nov. and Dec. 2015—₹ 300 p.m.	
I—for Sept., Oct., Nov. and Dec., 2015—₹ 200 p.m.	

J—for July to Nov. 2015—₹ 300 p.m.

K—for July to Dec. 2015—₹ 400 p.m.

(xi) Liability under Workmen's Compensation Act, ₹ 3,000.

Find out the amount of preferential creditors and non-preferential creditors according to Provincial Insolvency Act and Presidency Towns Insolvency Act.

Sol.

**Statement Showing the Amount of
Preferential and Unsecured Creditors**

Particulars	Total Amount Due	Provincial Insolvency Creditors		Presidency Towns Insolvency Act	
		Preferential Creditors	Non-preferential Creditors	Preferential Creditors	Non-preferential Creditors
	(₹)	(₹)	(₹)	(₹)	(₹)
1. Amount due to Govt. or any Local Authority :					
(i) Income tax	7,000	7,000	—	7,000	—
(ii) Sales tax	1,000	1,000	—	1,000	—
(iii) House and water tax	3,000	3,000	—	3,000	—
2. Salaries due to clerks :					
H for Nov. & Dec. @ ₹ 300 p.m.	600	20	580	300	300
I for Sept., Oct., Nov. & Dec. @ ₹ 200 p.m.	800	20	780	300	500
J for July to Nov. @ ₹ 300 p.m.	1,500	20	1,480	300	1,200
K for July to Dec. @ ₹ 400 p.m.	2,400	20	2,380	300	2,100
3. Salaries and wages of servants and labourers:					
C for Nov. & Dec. @ ₹ 200 p.m.	400	20	380	100	300
D for Sept., Oct., Nov. and Dec @ ₹ 300 p.m.	1,200	20	1,180	100	1,100
E for July, Aug. and Sept. @ ₹ 200 p.m.	600	20	580	100	500
F for Nov. and Dec. @ ₹ 100 p.m.	200	20	180	100	100
G for July to Dec. @ ₹ 100 p.m.	600	20	580	100	500
4. Liability under Workmen's Compensation Act	3,000	3,000	—	3,000	—
5. Landlord's Rent and Ground rent :					
(i) Rent of landlord for 4 months @ ₹ 300 p.m.	1,200	—	1,200	300	900
(ii) Half month's ground rent @ ₹ 400 p.m.	200	—	200	200	—

6. Miscellaneous :					
(i) Director's three months' salaries	12,000	—	12,000	—	12,000
(ii) Managing Director's three months' salary ₹ 5000 pm	15,000	—	15,000	—	15,000
(iii) Manager's Salary	3,000		3,000		3,000
Total	53,700	14,180	39,520	16,200	37,500

Q.11. Differentiate between balance sheet and statement of affairs.

Ans. Difference between Balance Sheet and Statement of Affairs

Basis	Balance Sheet	Statement of Affairs
Date of Preparation	It is often prepared at the end of the year.	It is prepared at the time of insolvency.
Use of Lists	Lists are not used for writing of assets and liabilities.	Lists are used for assets and liabilities.
Record of Assets	All real and fictitious assets are recorded in it.	Only real assets are recorded in it.
Value of Assets	Fixed assets are shown after deduction of depreciation.	Fixed assets are shown at realisable value.
Assets lodged as security	Assets lodged as a security are shown in the asset side.	The assets lodged as security are not shown in the asset side but shown in the liability side along with the concerning loan.
Record of Liabilities	Columns of gross liabilities and expected to rank are not made in it.	These columns are made in it.
Total	Total of liabilities is equal to total of assets.	Total of liabilities is more than total of assets and this excess is called deficiency.
Number	It is prepared for all the years during which business is carried on.	It is prepared only once i.e., at the time of insolvency.
Object	It is prepared for knowing the financial position of the concern.	It is prepared to show the inability of the debtor to pay his debts.
For whom prepared	It is prepared for the sake of proprietor and others.	It is prepared for the satisfaction of the Court.
Deficiency Account	Deficiency Account is not prepared along with it.	Deficiency Account is prepared along with it.
Act	In case of Sole Trader and Firm, there is no Act for its preparation but in the case of Companies it is prepared according to the Companies Act.	It is prepared according to the Presidency Towns Insolvency Act or Provincial Insolvency Act.
Preferential Creditors	Preferential Creditors are not deducted in the assets side.	Preferential Creditors are not deducted in the assets side.
Capital	Capital is shown in the liabilities side.	Capital is not shown in the liabilities side.

Q.12. Ankush of Meerut had on 31st March, 2016, assets of ₹ 66,000 including a machinery valued in the books at ₹ 6,000 and estimated to realise 70 per cent of the book value and furniture valued ₹ 2,000 (estimated to produce 40%), he also had liabilities ₹ 40,000 of which ₹ 3,000 were fully secured against the machinery and liabilities of ₹ 1,000 were secured against furniture. He filed his petition for insolvency and estimated his deficiency to be ₹ 20,000 before taking into account the following outstanding liabilities : Wages ₹ 700; Rent ₹ 800; Salaries ₹ 2,000; Income tax ₹ 100; Sales Tax ₹ 50; House tax ₹ 50 and compensation payable under workmen's compensation Act ₹ 300. Prepare his revised Statement of Affairs and Deficiency Account from the above particulars.

Sol.

Statement of Affairs
(as at 31st March, 2021)

(₹)	Particulars	(₹)	Particulars	(₹)
36,800 ⁵	Unsecured Creditors as per List A	36,800 ⁵	Property as per List E :	
	Fully secured Creditors		Sundry Assets	58,000 ⁶ 15,000 ¹
3,000	as per List B	3,000	Book Debts as per List F	—
	Security	4,200 ³	B/E as per List G	—
	Surplus thereof to contra	1,200	Add : Surplus as per contra	1,200
1,000	Partly Secured Creditors			16,200
	as per List C	1,000	Deduct : Pref. Crs. as per contra	3,200
	Security	800 ⁴		13,000
3,200 ⁷	Pref. Crs. as per List D	200	Def. as per List H	24,000
—	Deducted as per contra	3,200 ⁷		
44,000		37,000		37,000

Deficiency Account

Particulars	(₹)	Particulars	(₹)
Excess of Assets over Liabilities	26,000 ⁸	Expenses & Losses :	
Deficiency as per List H in the Statement of Affairs	24,000	On Assets	43,000 ⁹
		On Machinery	1,800 ¹⁰
		On Furniture	1,200 ¹¹
		Expenses & Taxes	
		Compensation	4,000 ¹² 50,000
	50,000		50,000

First Statement of Affairs

(₹)	Particulars	(₹)	Particulars	(₹)
36,000	Unsecured Crs. as per List A	36,000*	Property as per List E :	
3,000	Fully Secured Crs.		Sundry Assets	58,000 ⁶ 15,000 ²

	as per List B	3,000		Book Debts as per List F	—
	Security	4,200 ³		B/E as per List G	—
	Surplus thereof to contra	1,200		Add : Surplus as per contra	1,200
1,000	Partly Secured Creditors				16,200
	as per List C	1,000		Deficiency as per list 'H'	20,000
—	Security	800 ⁴	200		
	Pref. Creditors as per List D		—		
40,000			36,200		36,200

Working Notes :

1. ₹ 40,000 – (3,000 + 1,000) = ₹ 36,000
2. This is balancing figure i.e., total ₹ 16,200 – Surplus as per Contra ₹ 1,200 = ₹ 15,000.
3. ₹ 6,000 × $\frac{70}{100}$ = 4,200;
4. ₹ 2,000 × $\frac{40}{100}$ = ₹ 800;
5. ₹ 40,000 – (3,000 + 1,000) + Rent ₹ 800 = ₹ 36,800;

6. Total Assets		₹
Less : Machinery	6,000	66,000
Furniture	2,000	8,000
Sundry Assets		58,000

7. Preferential Creditors = Wages + Salaries + Income Tax + Sales Tax + House Tax + Compensation
= 700 + 2,000 + 100 + 50 + 50 + 300 = ₹ 3,200
8. ₹ 66,000 – 40,000 = 26,000;
9. ₹ 58,000 – 15,000 = ₹ 43,000;
10. ₹ 6,000 – 4,200 = ₹ 1,800;
11. ₹ 2,000 – 800 = ₹ 1,200
12. ₹ 700 + 800 + 2,000 + 100 + 50 + 50 + 300 = ₹ 4,000.

Q.13. A receiving order has been made against Bhanu of Meerut dated 15th March, 2021 the particulars of his assets and liabilities are as under:

	(₹)
Unsecured Creditors	4,487
Creditors fully secured (holding Life Insurance Policies valued at ₹ 12,315)	10,333
Creditors partly secured (the Security held is a second mortgage on assets pledged to fully secured creditors, the surplus available from the latter being estimated at ₹ 1,020)	1,582
Preferential Creditors	37
Cash in Hand	4
Life Insurance Policies, not charged (surrender value estimated ₹ 30)	
Stock and Shares (estimated to produce ₹ 154)	554
Motor Cycle (estimated to produce ₹ 249)	849
Debts ₹ 76 (of which ₹ 39 are good) estimated to realise	52

The debtor has conveyed his furniture to his wife by deed of gift dated 3rd June, 2020. The value of this item is estimated at ₹ 300. Bhanu, the debtor, transferred a cycle of ₹ 500 to his wife on 31st Dec., 2017 without consideration and on 1st

November, 2020 transferred furniture of ₹ 100 to his wife for sufficient consideration.

Bhanu commenced his business on 15th Dec., 2016 with a capital of ₹ 5,000. His profit for the year ending at 15th Dec., 2017 was ₹ 1,000 and in the remaining three years his losses respectively were ₹ 2,000, ₹ 3,000 and ₹ 4,000. His total drawings during these years were ₹ 4,000. Loss on speculation was ₹ 7,956. Prepare the Statement of Affairs and Deficiency Account.

1. Section 53 of Provincial Insolvency Act.

2. Section 54 of Provincial Insolvency Act.

Sol.

Statement of Affairs

(as at 15th March, 2021)

Gross Liabilities	Liabilities (as stated and estimated by the Debtor)	Expected to Rank	Assets (as stated and estimated by the Debtor)	Estimated to Produce
(₹)		(₹)		(₹)
4,487	Unsecured Creditors as per List A	4,487	Property as per List E	
10,333	Creditors fully Secured as per List B		Cash in hand	4
	10,333		Stock & Shares	154
	Estimated Value of Securities		Life Ins. Policy	30
	12,315		Motor Cycle	249
	Surplus		Furniture	300
	1,982			737
	Less: Amount carried to C		Book debts as per List F:	
	1,020		Good	39
	Balance to contra		Doubtful & Bad	13 ²
	962		37 ¹	
1,582	Creditors Partly Secured as per List C		Bills of Exchange as per List G	—
	1,582			
	Less : Estimated value of securities from		Surplus from Securities in the hands of Crs. fully secured	962
	1,020	562	as per contra	1,751
37	Creditors preferential as per List D		Deduct: Preferential Crs. as contra	37
	Deduct : as per contra			1,714
	37		Deficiency as per List 'H'	3,335
16,439		5,049		5,049

Deficiency Account

	(₹)		(₹)
Capital	5,000	Losses	9,000
Profit	1,000	Drawings	4,000
Surplus of Private Assets over Private Liabilities	12,345 ⁴	Bad Debts	24 ³
Furniture transferred to wife		Other Losses:	
		Stock	400

Without consideration	300	Motor Cycle	600	
Deficiency as per List 'H' in the Statement of Affairs	3,335	Speculation Loss	7,956	8,956
	21,980			21,980

Working Notes :

1. ₹ 76 – ₹ 39 = ₹ 37;

2. ₹ 52 – ₹ 39 = 13

3. ₹ 37 – 13 = ₹ 24

4. Life Insurance Policies ₹ 12,315 + 30 = ₹ 12,345. Life Insurance Policies are treated as private assets. As no private liabilities are given, whole amount of the life insurance policies is treated as surplus of privated assets over private liabilities.

Q.14. On 31st March, 2021, the Balance Sheet of Ajay and Bhaskar was as follows:

Particulars	(₹)	Particulars	(₹)
Trade Creditors	24,000	Machinery	24,000
Bills Payable	30,000	Buildings	12,000
Bank	18,000	Book Debts	24,000
Twelve Months' Rent	1,200	Cash	1,200
One Month's Salaries	1,200	Stock	37,200
Capitals :			
Ajay	12,000		
Bhaskar	12,000		
	24,000		
	98,400		98,400

Ajay owed personally ₹ 21,600 and he had in addition to his interest in the firm, a house which costs ₹ 6,000. Furniture ₹ 2,400 and Life Policies on which he had paid premiums amounting to ₹ 1,200. Bhaskar owed ₹ 16,800 and he had paid Life Premiums amounting to ₹ 3,600 and had furniture which cost ₹ 1,200. The Bank held the deeds of Ajay's property and his life policies. It became necessary to call the creditors together. The partnership assets were valued as follows: Machinery ₹ 13,080; Building ₹ 6,000; Good Book Debts ₹ 12,000; Doubtful ₹ 6,000 (estimated at ₹ 3,600); Bad ₹ 6,000; Stock ₹ 24,000. Ajay's property was considered to be worth ₹ 6,000, his Life Policies ₹ 600; and his furniture ₹ 1,800. Bhaskar's Life Policies were worth ₹ 1,800, his furniture ₹ 600.

Prepare separate Statements of Affairs and Deficiency Accounts of the firm as well as of the partners.

Sol. Statement of Affairs of Ajay and Bhaskar
(as at 31st March, 2021)

Gross Liabilities	Liabilities (as stated and estimated by the Debtor)	Expected to Rank	Assets (as stated and estimated by the Debtor)	Estimated to Produce
(₹)		(₹)		(₹)
73,200 ¹	Unsecured Creditors as per List A	73,200 ¹	Property as per List 'E' :	

— Creditors fully secured as per List B	— Cash		1,200
— Creditors partly secured as per List C	— Stock	37,200	24,000
1,200 ² Creditors Preferential as per List D	Building	12,000	6,000
Deduct as per contra ₹ 1,200 ²	Machinery	24,000	13,080
	Total as per List E		44,280
	Book Debts as per List F :		
	Good		12,000
	Doubtful	6,000	
	Bad	6,000	
		₹ 12,000	
	Estimated to Produce		3,600
	Estimated of Exchange as per List G		59,880
	Deduct: Preferential Creditors as per contra		1,200
			58,680
	Deficiency as per List H		14,520
74,400		73,200	73,200

Working Notes :

- Unsecured Creditors :
₹ 24,000 + 30,000 + 18,000 + 1,200 = 73,200.
- This is the amount of the month's salary. Whole of it is treated as preferential because number of clerks is not given.

Deficiency Account of the Firm

Particulars	(₹)	Particulars	(₹)
Excess of Assets over Liabilities	24,000	Bad Debts	8,400
Deficiency as per List H in the Statement of Affairs	14,520	Other Losses:	
		Stock	13,200
		Building	6,000
		Machinery	10,920
	38,520		30,120
			38,520

Statement of Affairs of Ajay
(as at 31st March, 2021)

(₹)	Particulars	(₹)	Particulars	(₹)
21,600	Unsecured Creditors as per List A	21,600	Property as per List E :	
	Fully Secured Creditors as per List B	—	Furniture (₹ 2,400)	1,800

Partly Secured Creditors as per List C	—	Surplus of Security held by the bank	3,030*
Preferential Creditors as per List D	—	Investment in the firm 12,000	Nil
		Total as per List E	4,830
		Book Debts as per List F	—
		Bills of Exchange as per List G	—
		Deficiency as per List H	16,770
21,600	21,600		21,600

The Bank held the deeds of Ajay's property and his Life Policy as security, but first of all it will recover its debt from the firm's assets of ₹ 58,680. This amount will be proportionately distributed amongst all the creditors which amount to ₹ 73,200. Therefore, Bank gets

$$\frac{58,680 \times 18,000}{73,200} = ₹ 14,430.$$

Calculation is made to the nearest rupee. It will recover ₹ 18,000 – ₹ 14,430 = ₹ 3,570 from Ajay's security which is house property ₹ 6,000 + Life Policy ₹ 600, i.e., ₹ 6,600. It will return ₹ 6,600 – 3,570, i.e., ₹ 3,030 as it is surplus with him.

Deficiency Account of Ajay

Particulars	(₹)	Particulars	(₹)
Excess of Assets over Liabilities	Nil*	Loss on Furniture	600
Deficiency	16,770	Loss on Policy & Prop.	4,170 ¹
		Loss on Investment in Business	12,000
	16,770		16,770

Working Note :

1. Book Value House ₹ 6,000 + Life Policy ₹ 1,200 = ₹ 7,200.

Realisable Value, House ₹ 6,000 + Life Policy ₹ 600 = ₹ 6,600; out of this amount of ₹ 6,600; bank has taken ₹ 3,570, hence balance left for Ajay is ₹ 6,600 – ₹ 3,570 = ₹ 3,030; Ajay's Loss is ₹ 7,200 – ₹ 3,030 = ₹ 4,170. There is no excess of assets over liabilities in Ajay's case as is clear from the following statement:

Ajay's Financial Position

Particulars	(₹)	Particulars	(₹)
Loan	21,600	Investment in the firm as capital	12,000
Excess of Assets over Liabilities	Nil	House	6,000
		Furniture	2,400
		Life Policy	1,200
	21,600		21,600

Statement of Affairs of Bhaskar
(as at 31st March, 2021)

(₹)	Particulars	(₹)	Particulars	(₹)
16,800	Unsecured Creditors as per List A	16,800	Property as per List E :	
—	— Fully Secured Creditors as per List B	—	— Furniture (₹ 1,200)	600
—	— Partly Secured Creditors as per List C	—	— Policies (₹ 3,600)	1,800
—	— Preferential Creditors as per List D	—	— Investment in the firm 12,000	Nil
				2,400
			Book Debts as per List F	—
			Bills of Exchange as per List G	—
			Deficiency as per List H	14,400
16,800		16,800		16,800

Deficiency Account of Bhaskar

Particulars	(₹)	Particulars	(₹)
Excess of Assets over Liabilities	Nil*	Loss on Investment in Business	12,000
Deficiency	14,400	Loss on Furniture	600
	14,400	Loss on Policies	1,800
			14,400

* There is no excess of assets over liabilities in Bhaskar's case as is clear from the following statement :

Bhaskar's Financial Position

Particulars	(₹)	Particulars	(₹)
Loan	16,800	Investment in the firm	12,000
Excess of Assets over Liabilities	Nil	Furniture	1,200
	16,800	Life Policy	3,600
			16,800

□

MODEL PAPER

Financial Accounting

B.Com.-I (SEM-II)

[M.M. : 75

Note : Attempt all the sections as per instructions.

Section-A : Very Short Answer Type Questions

Instruction : Attempt all **FIVE** questions. Each question carries **3 Marks**. Very Short Answer is required, not exceeding 75 words.

1. Mention any two main objectives of accounting.
2. What is meant by 'Instalment payment system'?
3. Define the term 'Departmental accounting'.
4. What do you mean by 'minimum rent' with regards to royalty?
5. What is meant by Profit And Loss Account?

Section-B : Short Answer Type Questions

Instruction : Attempt all **TWO** questions out of the following 3 questions. Each question carries **7.5 Marks**. Short Answer is required not exceeding 200 words.

6. Explain briefly the advantages and needs of Accounting Standards.
- Or** K.S. Aiyar is known as 'Father of Accountancy in India.' Explain the biography of K.S. Aiyar.
7. Discuss the accounting records in the books of the purchaser when the asset is recorded at cash price actually paid.
- Or** Discuss the various types of branches.
8. Explain the prominent features of the Insolvency and Bankruptcy Code,2016.
- Or** Explain the procedure of realisation of property under Provincial Insolvency Act.

Section-C : Long Answer Type Questions

Instruction : Attempt all **THREE** questions out of the following 5 questions. Each question carries **15 Marks**. Answer is required in detail, between 500-800 words.

9. Discuss Accounting Standards in India. Also explain the procedure for issuing Accounting Standards in India.
- Or** On 1st April, 2018 a Railway Company buys on Hire-Purchase System from Hire-Vendor some Thelas for ₹ 25,500, payable by three equal instalments combining principal and interest, the latter being a normal rate of 5% per annum.
Calculate the amount of annual instalment, and show Hire-vendor's Account (under Asset Accrual Method) and Interest Account for three years in the Railway Company's Ledger. (The present value of an Annuity of one Rupee for three years at 5% is ₹ 2.72325).
10. Explain the accounting records for mining royalties in the books of Lessee.

- Or** On 1st April, 2017 Ronak purchased a T.V. whose cash price was ₹ 66,244 from N.R. Ltd. on Hire-purchase System and it was decided that this amount will be paid in four equal annual instalments at 8% annual interest. The present value of an annuity of one rupee for 4 years at 8% is ₹ 3.3122. Calculate the amount of interest for each instalment and also prepare Hire Vendor's Account in the books of Ronak under Assets Accrual Method.
- 11.** What is Journal? What are the steps in journalising?
- Or** On 1.4.2017, the Arnav Colliteries Ltd. took a piece of land on lease. A minimum rent of ₹ 2,000 in the first year, ₹ 4,000 in the second year, and thereafter ₹ 6,000 per annum, is to be merging into a Royalty of 40 paise per ton, with power to recoup Shortworkings over the first years of the lesse only. The figures of annual output for the years from 1.4.2017 to 31.3.2021, were 1,000, 10,000, 18,000 and 20,000 ton respectively. Open the necessary accounts in the books of the Lessee.
- 12.** Explain the concept of double entry system. Also explain its merits and demerits.
- Or** Amar took a mine for lease for 15 years @ 50 paise per ton. Minimum Rent per year is fixed at ₹ 4,000. Shortworkings can be recouped in the first four years of the lease. The tonnage raised from the mine has been as follows :
- 6,000 ton in I year; 9,000 ton in II year; 5,000 ton in III year; 10,000 ton in IV year and 8,000 ton in V year.
- It is decided to create Shortworkings Reserve Account for an amount equal to that of shortworkings. Pass the necessary Journal entries in the books of Lessee Amar and prepare S.W. Reserve Account, Shortworkings Account, Profit and Loss Account and Balance Sheet. Books are closed every year on 31st March.
- 13.** Discuss the accounting records in the books of landlord and royalty reserve.
- Or** Cash price of a machine is ₹ 3,000 and Hire-Purchase price is ₹ 4,000. This machine is sold on Hire-Purchase System on 1st April, 2019 to the Hire-Purchaser and payment is made in four six-monthly instalments of ₹ 1,000 each. It was agreed that the machine will be maintained free of charge for a period of two years. The actual expenses of maintenance were ₹ 100 and ₹ 250 for the first and second years respectively, though past experience showed that they are ₹ 500 of which ₹ 70 are for the first year. Pass the necessary Journal entries in the books of the Hire-Vendor and open the Hire-Maintenance Suspense Account.

□

- | |
|--|
| <ul style="list-style-type: none"> ■ In the publication of this book, every care has been taken in providing a precise and errorless material, yet if any mistake has crept in, mechanically or technically, the Publisher, the Writer and the Printer shall not be responsible for the same. All disputes are subject to the court of Meerut Jurisdiction. ■ No portion of the text, title, design and mode of presentation, used in this book, be reproduced in any form. Violation of our warning leads to legal prosecution. ■ Suggestions for any improvement of this book are cordially invited and such suggestions may be incorporated in the next edition. For any type of suggestion or error you can also mail your ideas on info@vidyauniversitypress.com. 622 |
|--|