PARTNERSHIP: BASICS

DEFINITIONS

Partnership	Partnership is the relationship between persons who have agreed to share the profits of a business carried on by all or any one of them acting for all.
Partners	Persons who have entered into Partnership with one another are individually called Partners.
Firm	Persons who have entered into Partnership with one another are collectively called firm
Firm Name	The name under which their business is carried on is called the Firm Name

FEATURES OF PARTNERSHIP

Persons	It requires at least two persons to form a Partnership.
Agreement	An agreement is entered by all the persons concerned, setting out the terms and conditions under which the Partnership is based. When this agreement is set out in writing, it is called the ''Partnership Deed''.
Legal Business	A partnership can exist only in business. Thus, it is not the agreement alone which creates a partnership. A partnership comes into existence only when partners begin to carry on business in accordance with their agreement
Mutual Agency	The activities of the business will be carried on/managed by all or any one of them acting for all. This principle of **mutuality** is the essence of Partnership agreement
Sharing of Profit/loss	The Partners share the profits and losses of the business in the agreed ratio.

PARTNERSHIP DEED & CONTENTS

Meaning	Partnership Deed is the *written agreement* containing the terms and conditions under which the Partnership will sustain or exist.
Contents of Partnership Deed	❖ Name of the firm and the nature of the Partnership Business. ❖ Commencement and Tenure of the Business (e.g. Partnership at Will, etc.) ❖ Amount of Capital to be contributed by each Partner. ❖ Ratio for sharing the Profit/Loss of the Partnership business amongst Partners. ❖ Arrangement in respects of Drawings by Partners and limits thereon. ❖ Interest to be credited on the Capital Account of Partners. ❖ Interest to be charged on Drawings of Partners ❖ Remuneration to Partners and the basis of determining such remuneration e.g. Commission as a percentage of the Firm's Turnover, other conditions for eligibility of remuneration etc. ❖ Process of setting disputes that may arises among the Partners. ❖ Procedure for maintenance of Books of Accounts ❖ Audit of Books of Accounts ❖ Manner of valuation of Goodwill in case of admission of new partners, retirement of existing partners and death of a Partner. ❖ Procedure for settlement of Partners' claims in case of retirement/death ❖ Procedure for dissolution of Partnership
Notes	❖ When partnership deed is not registered a partnership firm is allowed to carry on business subject to certain disabilities. ❖ It is not mandatory to have a written agreement in all cases. Further, even in cases where there is a written Partnership Deed, it is not compulsory to have it registered.

DISTINCTION BETWEEN PARTNERSHIP & LIMITED LIABILITY PARTNERSHIP

BASIS	PARTNERSHIP	LIMITED LIABILITY PARTNERSHIP
Applicable Law	Indian Partnership Act 1932	The Limited Liability Partnerships Act, 2008
Registration	Optional	Compulsory
Creation	Created by an Agreement	Created by Law
Separate Legal Entity	No	Yes
Perpetual Succession	Partnerships do not have perpetual succession	It has perpetual succession and individual partners may come and go
Number of Partners	Minimum 2 and Maximum 50	Minimum 2 but no maximum limit
Ownership of Assets	Firm cannot own any assets. The partners own the assets of the firm	The LLP as an independent entity can own assets
Liability of Partners / Members	**Unlimited**: Partners are severally and jointly liable for actions of other partners and the firm and their liability extends to personal assets	Limited to the extent of their contribution towards LLP except in case of intentional fraud or wrongful act of omission or commission by a partner.

REMUNERATION, INTEREST ON CAPITAL, LOAN, DRAWINGS, PROFIT SHARING RATIO

1. **Governing Statute:** The law governing Partnership in India is the Partnership Act, 1932.
2. **Conditions not covered by Partnership Deed:** Where any situation or circumstance is not covered by the Partnership Deed or is not adequately provided for in the Partnership Deed, the Provision of the Partnership Act, 1932 will apply.

If the Deed is silent on-	Provisions of the Partnership Act
Partners' Remuneration/ Salary/ Commission	**No** Remuneration will be allowed to any Partner.
Interest on Partners' Capital	**No** IOC will be allowed to any Partner.
Interest on loan given by Partner to the Firm	**Maximum 6% p.a.** can be allowed on loan.
Interest on Partners' Drawings	**No** interest will be charged on Partners' Drawings
Profit Sharing Ratio	Profits and Losses will be shared **equally.**

PARTNER'S CAPITAL ACCOUNTS

1. **Methods of Accounting:** The transactions affecting the Partners' Capital Accounts may be accounted under any of the following methods**-**

Aspects	Fluctuating Capital Method	Fixed Capital Method
Ledger A/cs prepared	Partner's Capital Account.	1. Partner's Capital Account, and 2. Partner's Current Account.
Initial Capital contribution	Amount brought in or contribution is **credited to the Partner's Capital A/c**	Amount brought in or contributed is **credited to the Partners' Capital A/c**
Subsequent transactions	Subsequent transactions are accounted in Partner's **Capital Account**	Subsequent transactions are accounted in Partner's **Current Account**

FORMAT OF PARTNER'S CAPITAL ACCOUNT

Particulars	A	B	C	Particulars	A	B	C
To **Cash/Bank** (Withdrawal of capital, if any) To **Balance c/d**				By **Balance b/d** By **Cash/ Bank/ Assets** (Capital Contribution)			
Total				**Total**			

FORMAT OF PARTNER'S CURRENT ACCOUNT

Particulars	A	B	C	Particulars	A	B	C
To **Balance b/d** To **Drawings A/c** To **P&L A/c** - Share of Loss To **Profit & Loss Appropriation** -Interest on Drawings, if any To **Balance c/d**				By **Balance b/d** By **Profit & Loss Appropriation** -Remuneration/ Salary/Comm. -Interest on Capital -Share of Profit By **Balance c/d**			
Total				**Total**			

Note: If Capital Accounts are maintained on Fluctuating basis, all the above entries will be made in one single Capital Account only. There will not be any Current Account

PROFIT & LOSS APPROPRIATION ACCOUNT

1. **Purpose:** Profit and Loss A/c of firm will show the profit earned or loss suffered by the firm.
   To distribute the above Profit properly to the Partners, the **Profit and Loss Appropriation A/c** is used
2. **Features:**
   (a) It is **extension of P&L Account**.
   (b) It provides details of how the Net Profit for the period has been **distributed to the Partners**
   (c) The entries in P&L Appropriation A/c are **governed by the Partnership Deed**.

Note: Interest on Partners' Loan, Rent for use of Partners' premises, if any, etc. are debited to P&L A/c itself. Net Profit after charging and debiting these items, is only transferred to P&L Appropriation A/c

3. **Format:**

Dr. **Profit & Loss Appropriation A/c** **Cr.**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Interest on partner's capital A --- B ---	XX	By P&L A/c balance (Profit)	XX
To Partner's Salary A --- B ---	XX	By Interest on partner's drawings A --- B ---	XX
To Partner's Commission/Bonus A --- B ---	XX		
To Reserves (Amount transferred)	XX		
To Profits transferred in PSR: A --- B ---	XX		
Total	**XXXX**	**Total**	**XXXX**

Interest on Partners' Capital

Type of Capital	Computation of Interest on Capital (IOC)
1. Opening Capital	IOC= Opening Capital x Rate of Interest
2. Additional Capital	IOC= Additional Capital x Rate of Interest x Period of use

Interest on Capital in case of Insufficient Profits or Loss

Interest on Capital

- Deed is silent or No Deed → No IoC
- Deed provides for IoC
  - In case of Loss → No IoC
  - In case of Profit
    - Sufficient Profits [Profits ≥ IoC] → Full IoC
    - Insufficient Profits [Profits < IoC] → Profits distributed in ratio of capital
- Deed provides for IoC & specifically states it to be charge against profit → Full IoC even if there is loss

Effective Capital

Partners may agree to share profits and losses in the capital ratio. The capitals for the purpose of ratio would be determined with reference to time on the basis of weighted average method.

Example:

A and B formed a partnership with a capital contribution of Rs.1,00,000 and Rs.80,000 respectively on 1st January 2021. Profits were to be shared in the Effective Capital ratio. Interest on Capital is 6% p.a.

Date	Capital Introduced		Capital Withdrawn	
	A	B	A	B
1st April	2,00,000			
1st July		40,000	1,00,000	

Calculate: (a) Profit-sharing ratio; (b) Interest on capital

Effective capital :

A		B	
1/1	$100000 \times \frac{12}{12} = 100000$	1/1	$80000 \times \frac{12}{12} = 80000$
1/4	$200000 \times \frac{9}{12} = 150000$	1/7	$40000 \times \frac{6}{12} = 20000$
1/7	$(100000) \times 6/12 = (50000)$		
	200000		100000

Ratio (PSR) ⇒ 200000 : 100000 = 2 : 1

IOC : A = 2L × 6% = 12000 B = 1L × 6% = 6000

Interest on Partners' Drawings

- Drawings refers to amount withdrawn by Partners, in cash or in kind, for their personal use.
- Partners are supposed to pay interest on drawings only when provided by the agreement or agreed by the partners.
- Interest on drawings is gain for the business. It is recorded on credit side of P&L Appropriation A/c.
- Partner's Drawings A/c & interest on drawings is closed by transferring to debit side of Capital or Current A/c.

Interest on Drawings

- Dates of Drawings not given
  - P.a.
    - $IOD = Drawings \times \frac{Rate}{100} \times \frac{6}{12}$
  - ~~P.a.~~
    - $IOD = Drawings \times \frac{Rate}{100}$
- Dates of Drawings given
  - Amt. of each drawing same **and** Time interval b/w 2 drawings same
    - Direct Method
    - Product Method
    - Shortcut Method (Preferable)
  - Either amount not same **or** Time interval not same
    - Direct Method
    - Product Method (Preferable)
    - Shortcut Method (X)

Short cut Method :

$$IOD = Total\ Drawings \times \frac{Rate}{100} \times \frac{Average\ Time\ Period^{*}}{12}$$

TTP = Total Time Period

TI = Time Interval

* Average Time Period

	Beginning	Middle	End
	$\frac{TTP + TI}{2}$	$\frac{TTP}{2}$	$\frac{TTP - TI}{2}$
A) 12 Months Period			
a) Monthly	$\frac{12+1}{2} = 6.5$	$\frac{12}{2} = 6$	$\frac{12-1}{2} = 5.5$
b) Quarterly	$\frac{12+3}{2} = 7.5$	$\frac{12}{2} = 6$	$\frac{12-3}{2} = 4.5$
B) 6 Months Period			
a) Monthly	$\frac{6+1}{2} = 3.5$	$\frac{6}{2} = 3$	$\frac{6-1}{2} = 2.5$
b) Quarterly	$\frac{6+3}{2} = 4.5$	$\frac{6}{2} = 3$	$\frac{6-3}{2} = 1.5$

Calculation of Remuneration/ Salary/Commission to Partners

Remuneration/ Salary/ Commission to Partners, can be provided to Partners, only if the Partnership Deed so provides. The calculations are as under:-

Type of Capital	Computation
1. Remuneration/ Salary	Remuneration / Salary p.a. = Monthly Amount x No. of months
2. Commission as x % of Turnover	Commission p.a. = Sales Turnover of the Firm x Rate of Commission
3. Commission as x % of Net Profit (a) Before Commission (b) After Commission	 Net Profit before Commission x Rate of Commission /100 Net Profit before Commission x $\frac{\text{Rate of Commission}}{(100+\text{Rate of Commission})}$

Past Adjustments in capital accounts of partners

Sometimes a few errors and omissions in the recording of transactions or the preparation of financial statements are found after the final accounts have been prepared and the profits distributed among the partners.

These omissions and errors may be in respect of:

- Interest on capitals, Interest on drawings,
- Partner's salary, partner's commission or
- Outstanding expenses.
- There may also be some changes in the provisions of partnership deed or system of accounting having impact with retrospective effect.

All these acts of omission and commission need adjustments for correction.

Now instead of altering all the old accounts, necessary adjustments can be made either;

❖ Through Profit and Loss Adjustment Account, or

❖ Directly in the Capital Accounts of the concerned partners.

Journal entry for adjustment is:

Gaining partner capital/current A/c Dr.

To Sacrificing Partner capital/current A/c

TABLE

	A	B	TOTAL
Items to be Recorded			
IoC	✓	✓	✓
Salary, Commission, etc.	✓	✓	✓
Share of Profit	✓	✓	✓
IoD	(✓)	(✓)	(✓)
CR.	✓	✓	✓
Items to be Reversed			
IoC	✓	✓	✓
Salary, Commission, etc.	✓	✓	✓
Share of Profit	✓	✓	✓
IoD	(✓)	(✓)	(✓)
DR.	✓	✓	✓
Difference	✓	✓	

Guarantee of Minimum Profit to a Partner

1. **Meaning:** Sometimes, Partners may mutually agree that certain Partner (s) has the right to have **minimum amount** of profit. Such profit is called Guaranteed Profit or Guaranteed Minimum Profit.
   Example: Guarantee given to a partner 'X' by the other partners 'Y & Z' means in case of loss or insufficient profits 'X' will withdraw the minimum guaranteed amount.

2. **Treatment:**

Situation	Steps in Computation/ Treatment
(a) If Profit Share > Guaranteed Profit	Distribute the Total Available Profit in the agreed profit sharing ratio, in the usual manner.
(b) If Profit Share < Guaranteed Profit	• Distribute the Total Available Profit in the agreed profit sharing ratio, in the usual manner. • Compute the **shortfall** in Guaranteed Profit, and add that to the share of the Partner entitled to the same. • Deduct the shortfall from the Profit shares of the Other Partners, as described below

Burden of Shortfall:

Guarantee given by	Shortfall to be reduced from
(a) One of the remaining partners	That Remaining Partners Share of Profit.
(b) Remaining two or all Partners in an agreed ratio	Two or all Partners, in agreed ratio
(c) Remaining Partners in their mutual PSR	All remaining Partners in mutual PSR

Note: If the question is silent about the nature of guarantee, situation (c) given above is assumed

Example

A, B and C entered into partnership on 1.1.2021 to share profits and losses in the ratio of 5 : 3 : 2. A personally guaranteed that C's share of profit after charging interest on capitals at 5% p.a. would not be less than Rs. 30,000 in any year. Capitals of A, B and C were Rs. 3,20,000, Rs. 2,00,000 and Rs. 1,60,000 respectively. Profits for the year ending 31.12.2021 before providing for interest on partners capital was Rs. 1,59,000. You are required to prepare the Profit and Loss Appropriation Account

Profit and Loss Appropriation Account

Particulars	Amount	Particulars	Amount
To Interest on Capital A/c A 3,20,000*5% = 16,000 B 2,00,000*5% = 10,000 C 1,60,000*5% = 8,000	34,000	By Profit and Loss A/c (Net profit)	1,59,000
To Profit tfd to Capital A/c A 125,000*5/10 = 62,500 – 5,000 = 57,500 B 125,000*3/10 = 37,500 C 125,000*2/10 = 25,000 + 5,000 = 30,000	1,25,000		
	1,59,000		**1,59,000**

Question

Good, Better and Best are in partnership sharing profits and losses in the ratio 3:2:4. Their capital account balances as on 31st March, 2021 are as follows:

	Rs.
Good	1,70,000 (Cr)
Better	1,10,000 (Cr)
Best	1,22,000 (Cr)

Following further information provided:

(1) Rs. 22,240 is to be transferred to General Reserve.

(2) Good, Better and Best are paid monthly salary in cash amounting 2,400, 1,600 & 1,800 respectively.

(3) Partners are allowed interest on their closing capital balance @ 6% p.a. and are charged interest on drawings @ 8% p.a.

(4) Good and Best are entitled to commission @ 8% and 10% respectively of the net profit before making any appropriation.

(5) Better is entitled to commission @ 15% of the net profit before charging Interest on Drawings but after making all other appropriations.

(6) During the year Good withdraw Rs. 2,000 at the beginning of every month, Better Rs. 1,750 at the end of every month and Best Rs. 1,250 at the middle of every month.

(7) Firm's Accountant is entitled to a salary of Rs. 2,000 per month and a commission of 12% of net profit after charging such commission.

The Net Profit of the firm for the year ended on 31st March, 2021 before providing for any of the above adjustments was Rs. 2,76,000.

You are required to prepare Profit & Loss Appropriation A/c for the year ended on 31st March, 2021

Solution

Working Note:-

(1)

Profit = 276000

− Salary = (24000) (2000 x12)

250000

− Commission = (27000) $\left[250000 \times \frac{12}{112}\right]$

Net Profit 225000

(2) Better Commission

Profit = 225000 − 22240 − 69600 − 24120 − 18000 − 22500

=) 68540

Commission =) $68540 \times \frac{15}{100}$ =) 10281

P&L Appropriation A/c

Particulars	Amount	Particulars	Amount
To General Reserve	22240	By Net Profit	225000
To Salary		By Interest on drawings	
Good $= 2400 \times 12 =$ 28800		Good	
Better $= 1600 \times 12 =$ 19200		$24000 \times \frac{8}{100} \times \frac{6.5}{12} \Rightarrow$ 1040	
Best $= 1800 \times 12 =$ 21600	69600	Better	
To Interest on capital		$21000 \times \frac{8}{100} \times \frac{5.5}{12} \Rightarrow$ 770	
Good $= 170000 \times 6\% =$ 10200		Best	
Better $= 110000 \times 6\% =$ 6600		$15000 \times \frac{8}{100} \times \frac{6}{12} \Rightarrow$ 600	2410
Best $= 122000 \times 6\% =$ 7320	24120		
To Commission			
Good $= 225000 \times 8\% =$ 18000			
Best $= 225000 \times 10\% =$ 22500			
Better $\Rightarrow$ 10281	50781		
To Profit tfd. (B.f.)			
Good $= 60669 \times \frac{3}{9} =$ 20223			
Better $= 60669 \times \frac{2}{9} =$ 13482			
Best $= 60669 \times \frac{4}{9} =$ 26964	60669		

GOODWILL

1. Goodwill is the value of **reputation** of a Firm in respect of profits expected in future over and above the normal rate of profits earned by similar Firms in the same locality.
2. Goodwill is the benefits and advantage of the good name, reputation and connections of a business firm. It is the attractive force which brings in customers, and enhances the revenues of the firm

Types of Goodwill

A. Purchased Goodwill	B. Self-Generated Goodwill
1. **Purchased Goodwill** arises when a business is purchased, & the consideration paid therefore is more than the value of assets taken over. 2. Purchased Goodwill= Purchase Consideration **Less** Net Assets taken over 3. Purchased Goodwill is recorded in books of accounts and **is shown** in the **balance sheet.**	1. It refers to **internally generated goodwill,** that arises to the special advantages possessed by the Firm. 2. Internally Generated Goodwill is **not recorded** in the books of account, since Accounting Standard 26 issued by ICAI specifically provides so.

Situations which may involve valuation of Goodwill in case of Firms

- Change in Profit Sharing Ratio amongst the Partners,
- Admission, Retirement & Death of a Partner,
- Dissolution of the Partnership

Methods of Valuation of Goodwill

Method:1 Average Profits Method

Average Profits Method

Simple Average

Average Profits = $\frac{\text{Profits of 'n' years}}{\text{No. of Years}}$

G/W = Avg. Profits X No. of years of Purchase

Weighted Average

Weighted Average Profits = $\frac{\text{Total Weighted Profits}}{\text{Total of Weights}}$

G/W = Weighted AP X No. of years of Purchase

Computation of Adjusted Profits

Profits	xx
+ Abnormal loss	xx
− Abnormal Gain	(xx)
− Omission of Expense	(xx)
+ Omission of Income	xx
± Rectification of Errors	xx/(xx)
	xx

Method:2 Super Profits Method

G/w = Super Profits (SP) X No. of Years of Purchase

SP = Average Profits (AP) − Normal Profits (NP)

NP = Capital Employed (CE) X Rate of Return (r%)

CE = Total Assets − Outsider Liabilities (Excl. Fictitious Assets & Non Trade Investments)

Method:3 Annuity Method

G/w = Super Profits X Annuity Factor (A.F.)

$$A.F. = \sum PVF(r\%, n)$$

PVF : Present value Factor
r% : Rate of Return
n : No. of Years

Method:4 Capitalisation Method

Capitalisation Method

Capitalisation of Average Profits

G/w = Capitalised value of business (CVB) − Capital Employed

$$CVB = \frac{\text{Avg. Profits}}{r\%}$$

Capitalisation of Super Profits

$$G/w = \frac{\text{Super Profits}}{r\%}$$

<u>Sometimes Question specifies to apply Average Capital Employed</u>

Average Capital Employed = <u>Opening Capital Employed + Closing Capital Employed</u>

Example 1

A and B are partners in a firm sharing profits and losses equally. On 31st March, 2021, total assets of the firm were 8,00,000 & outsider liabilities were 3,00,000. The profits of the firm for the last 3 years were 1,30,000, 1,50,000 & 1,28,000 The rate of normal profit is 20%. On 1st April, 2021 they agreed to admit C as a partner for 1/4th share. C will bring Rs. 1,00,000 as capital.

Compute value of the goodwill of firm on admission of C, if it is to be calculated on the basis of:

a) 3 years purchase of average profit.
b) 3 years purchase of super profit
b) 3 years purchase of super profit if discounting rate is 8%
d) Capitalization method

Solution

Average Profits = (1,30,000+1,50,000+1,28,000)/3 = 1,36,000
Capital Employed = 8,00,000 – 3,00,000 = 5,00,000

a) 3 years purchase of average profits

Goodwill = 3 × Average profit = 3 × Rs. 1,36,000 = Rs. 4,08,000

b) 3 years purchase of super profit

Average profit	1,36,000
Less : Normal profit @ 20% of 5,00,000	(1,00,000)
Super profit	36,000

Value of Goodwill = 3 ×Super profit = 3 × Rs. 36,000 = Rs. 1,08,000

c) Annuity Method:
Annuity Factor for 3 years at 8% = 0.926+0.857+0.794 = 2.577
Goodwill = 36,000*2.577 = 92,772

d) Capitalization of Average Profits method

$$\text{Normal value of business} = \frac{\text{Average profit}}{\text{Normal rate of profit}} = \frac{1,36,000}{20\%} = \text{Rs. } 6,80,000$$

Normal value of business	6,80,000
Less: Actual capital employed	(5,00,000)
Value of goodwill of the firm will be	**1,80,000**

Capitalization of Super Profits method

$$\text{Goodwill} = \frac{\text{Super profit}}{\text{Normal rate of profit}} = \frac{36,000}{20\%} = 1,80,000$$

Example 2

The profits and losses for the previous years are: 2018 Profit Rs. 10,000, 2019 Loss Rs. 17,000, 2020 Profit Rs. 50,000, 2021 Profit Rs. 81,000. The average Capital employed in the business is Rs. 2,00,000. Market Rate of interest on investment 9% & Rate of risk return on capital invested in business 1%
The remuneration from alternative employment of the proprietor is Rs. 6,000 p.a. Calculate the value of goodwill on the basis of 2 years' purchases of Super Profits based on the average of 3 years.

Solution

Total Profit for 3 years = (Rs. 17,000) + Rs. 50,000 + Rs. 81,000 = Rs. 1,14,000.
Average profits = Total Profits/No. of years = 1,14,000/3 = Rs. 38,000
Average Profits for Goodwill = Rs. 38,000 – Proprietor Remuneration
= Rs. 38,000 – Rs. 6,000
= Rs. 32,000
Normal Profit=Interest on Capital employed = Rs. 20,000 (i.e. Rs. 2,00,000 x10/100) = Rs. 20,000
Super Profit = Average Profit-Normal Profit = Rs. 32,000 – Rs. 20,000 = Rs. 12,000
Goodwill = Super Profit x 2 = Rs. 12,000 x 2 =Rs. 24,000

Treatment of Goodwill in case of change in PSR

Accounting Issue involved	Journal Entry
1. Writing off Goodwill existing in books	All Partner's Capital A/c (individually) Dr. (in **old ratio**) To Goodwill A/c
2. Adjusting Goodwill on change in PSR	Gaining Partner's Capital A/c Dr. (**Gain ratio**) To Sacrificing Partners' Capital A/c (**Sacrifice Ratio**)

Note: Only Purchased Goodwill should be shown in the books of accounts. Other Goodwill value, if any in the Balance sheet, should be written off from the books of accounts.

Sacrifice	Gain
Partners whose shares in Profit have decreased as a result of change in PSR, are known as **Sacrificing Partners.**	Partners whose shares in profits have increased as a result of change in PSR, are known as **Gaining Partners**
The ratio in which Partners have agreed to reduce their profits in favour of the other Partner(s) is called **Sacrifice Ratio or Sacrificing Ratio.**	The ratio in which Partners have agreed to gain their profits from the other Partner (s) is called **Gain Ratio or Gaining Ratio**
Sacrifice Ratio = Old Ratio **less** New Ratio	**Gain Ratio** = New Ratio **less** Old Ratio

Question

A, B & C are equal partners. They wanted to change the profit sharing ratio into 4:3:2. Goodwill of the firm is valued at ₹ 90,000. Pass necessary journal entry for goodwill adjustment.

Solution

Journal Entries

Date	Particulars	L.F.	Dr. Amount	Cr. Amount
	A's Capital A/c - Dr. To C's Capital A/c (Being the adjustment for goodwill through the Partners' Capital Accounts)		10,000	10,000

Working Notes:

Particulars	A	B	C
Credit in Old Ratio (1:1:1)	30,000	30,000	30,000
Debit in New Ratio (4:3:2)	40,000	30,000	20,000
	10,000 Dr.	**-**	**10,000 Cr.**

ADMISSION OF PARTNER

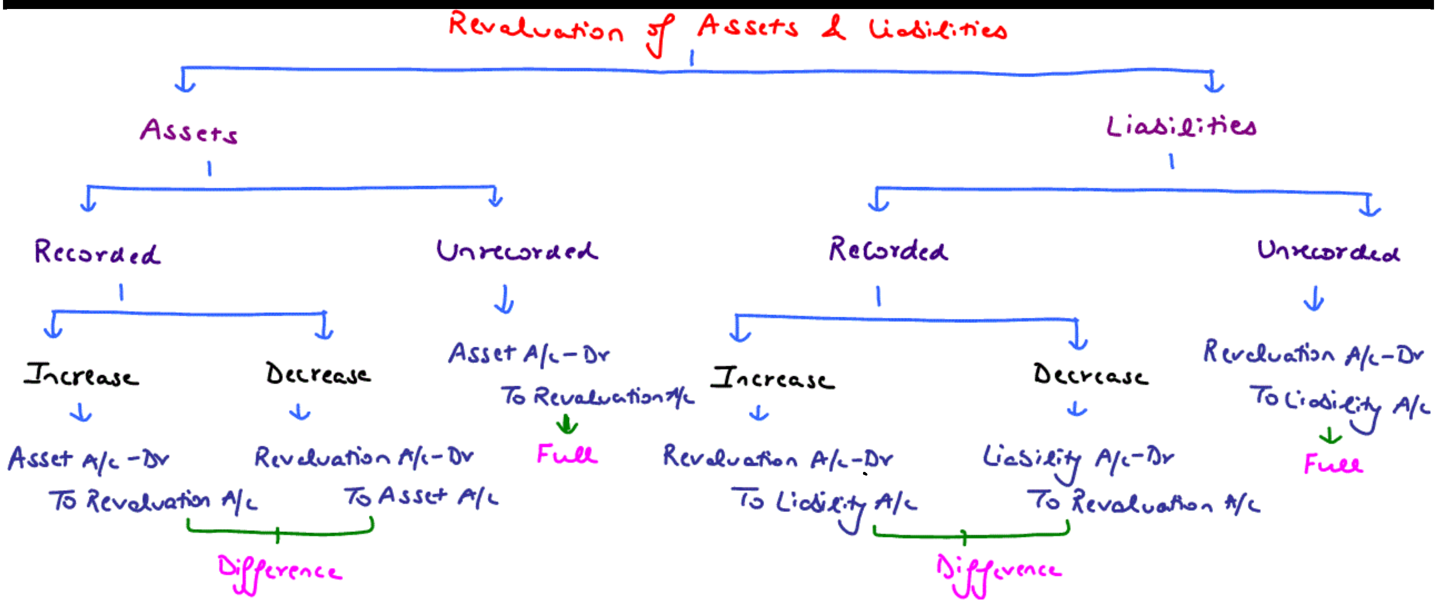
CONCEPT

New partners are admitted for the benefit of the partnership firm. New partner is admitted either for increasing the partnership capital or for strengthening the management of the firm.

Points to Note:

1) Calculation of New Ratio & Sacrificing Ratio
2) Revaluation of Assets & Liabilities
3) Treatement of Reserves
4) Treatment of Goodwill
5) Adjustment of Partners capital Accounts

Revaluation of Assets & Liabilities



Revaluation A/c

Particulars	**Amount**	**Particulars**	**Amount**
To Asset (Decrease)		By Asset (Increase)	
To Liabilities (Increase)		By Assets unrecorded	
To Liabilities unrecorded		By Liabilities (Decrease)	
To Revaluation profit (old partners in old ratio)		By Revaluation Loss (old partners in old ratio)	

Passing the entry through Capital A/c of Partners (Preparing Memorandum Revaluation Account)

1. Find the net gain or loss on Revaluation as follows
2. Entry:

    Gaining partners capital A/c (in case of profits)
            To Sacrificing partners capital A/c
    Sacrificing partners capital A/c (in case of losses)
            To Gaining partners capital A/c

Note: When profit/loss on revaluation of assets and liabilities is adjusted through capital accounts only then the assets & liabilities appear in B/sheet of new firm at their old figures.

Treatment of Reserves

Reserves

General Reserve
(P&L A/c, etc.)

General Res./P&L A/c - Dr
To Partner's Capital A/cs
(OLD RATIO)

Specific Reserve
(Investment fluctuation fund, workmen compensation reserve etc.)

If no other information given

Reserve A/c - Dr
To Partners cap. A/c

If Ques specifies liability against it

Reserve > Liability

Reserve A/c - Dr
To Liability A/c
To Partners Cap. A/c

Reserve = Liability

Reserve A/c - Dr
To Liability A/c

Reserve < Liability

Reserve A/c - Dr
Revaluation - Dr
To Liability A/c

Note: Sometimes the partner may decide not to close the Reserves / P& L A/c but to record the adjustment entry.

Gaining Partners' capital A/c Dr.
To Sacrificing Partners capital A/c

TREATMENT OF GOODWILL

Treatment of Goodwill

Old G/w
(Appearing in B/S)

Old Partner's Capital A/c - Dr
To Goodwill A/c

G/w Valued

① Bring

Cash/Bank/Asset A/c - Dr
To New Partner's cap. A/c
To Premium for G/w

② G/w Adjustment

Premium for G/w A/c - Dr
New Partner's cap. A/c - Dr
To Sacrificing Partners cap. A/c

③ Withdrawal of G/w

Sacrificing Partner's cap. A/c - Dv
To Cash/Bank A/c

ADJUSTMENT OF CAPITAL

Example 1

A & B = 3 : 2. Capital of A & B after adjustments are Rs. 80,000 & Rs. 60,000 respectively C is admitted who brings Rs.35,000 as capital for 1/5th share of profit to be acquired equally from A & B. Capital of A & B are to be adjusted on the basis of C's capital.

$A = \frac{3}{5} - \frac{1}{10} = \frac{5}{10}$

$B = \frac{2}{5} - \frac{1}{10} = \frac{3}{10}$

NR = 5:3:2

Total capital = $35000 \times \frac{5}{1}$

= 175000

A 5/10	B 3/10	C 2/10
87500	52500	35000
80000	60000	
7500 (Br.)	7500 (with.)	

Example 2

A & B = 3 : 2

Capitals of A & B after adjustments are Rs. 90,000 & Rs. 70,000. Calculate incoming partners proportionate capitals & surplus/shortage of existing capitals of old partners.

a) If C is to contribute proportionate capital for his 1/5th share or 1/5th of the total capital of new firm.

b) If C is to contribute 1/4th of the combined capitals of the existing partners.

c) If C is to contribute proportionate capital for his 1/5th share & capitals of all the partners are to be adjusted in new PSR 3:1:1

a) Total of A & B = 90000 + 70000 = 160000 (For 4/5th share)

Total capital = $160000 \times 5/4 = 200000$

C's capital = $200000 \times 1/5 = 40000$

b) C's capital = $160000 \times 1/4 = 40000$

c) Capital = 200000

	A	B	C
3:1:1	120000	40000	40000
	90000	70000	
	30000 (Br.)	30000 (WD)	

HIDDEN GOODWILL

Value of Goodwill:
Net worth (including goodwill) on the basis of capital brought by an incoming partner
(Incoming partners capital A/c x Reciprocal of his share)
Less: Net worth (excluding G/w of the firm)

Where, Net worth is Total Assets – Outsiders' Liabilities
OR
Capital of partners including new + Reserves + P & L (Cr. Bal.) - Miscellaneous expenditure

Example
A & B having PSR 3 : 2 are partners with capitals of Rs. 30,000 & Rs. 20,000 on date of C's admission for 1/5th share who brings Rs. 40,000. Following are the balances:
P & L (Cr.) = 6,000 Reserves = 55,000 Deferred Revenue Expenditure = 1,000
Find Goodwill.

Net worth (incl. G/w) $= 40000 \times \frac{5}{1} =$ 200000
Less Net worth
(30000 + 20000 + 40000 + 6000 + 55000 - 1000) (150000)
Goodwill 50000

C's share $= 50000 \times 1/5$
$= 10000$

Question

A and B were partners of a firm sharing profits and losses in the ratio 2:1. The Balance Sheet of the firm as at 31st March, 2021 was as under:

Liabilities	**Amount**	**Assets**	**Amount**
Capital Accounts		Plant and Machinery	5,00,000
A	8,00,000	Building	9,00,000
B	4,00,000	Sundry Debtors	2,50,000
Reserves	5,25,000	Stock	3,00,000
Sundry Creditors	2,75,000	Cash	1,50,000
Bills Payable	1,00,000		
	21,00,000		**21,00,000**

They agreed to admit P and Q into the partnership on the following terms:

a) The firm's goodwill to be valued at 2 years' purchase of the weighted average of the profits of the last 3 years.
   The relevant figures are:
   Year ended 31.3.2018 - Profit Rs. 37,000
   Year ended 31.3.2019 - Profit Rs. 40,000
   Year ended 31.3.2020 - Profit Rs. 45,000
b) The value of the stock and Plant & Machinery were to be reduced by 10%.
c) Building was to be valued at Rs. 10,11,000.
d) There was an unrecorded liability of Rs. 10,000.
e) A, B, P & Q agreed to share profits and losses in the ratio 3:2:1:1.
f) The value of reserve, the values of liabilities and the values of assets other than cash were not to be altered.
g) P and Q were to bring Capitals equal to their shares of profit considering B' s Capital as base after all adjustments.

You are required to prepare:

1) Memorandum Revaluation Account,
2) Partner's Capital Accounts and
3) The Balance Sheet of the newly constructed firm

Solution

Memorandum Revaluation A/c

Particulars	**Rs.**	**Particulars**	**Rs.**
To Stock	30,000	By Building	1,11,000
To Plant & Machinery	50,000		
To Unrecorded Liability	10,000		
To Profit transferred to			
A's Capital A/c	14,000		
B's Capital A/c	7,000		
	1,11,000		**1,11,000**
To Building	1,11,000	By Stock	30,000
		By Plant & Machinery	50,000
		By Unrecorded Liability	10,000
		By Loss transferred to	
		A's Capital A/c	9,000
		B's Capital A/c	6,000
		P's Capital A/c	3,000
		Q's Capital A/c	3,000
	1,11,000		**1,11,000**

Capital Accounts

	A	B	P	Q		A	B	P	Q
To Memo. Rev	9,000	6,000	3,000	3,000	By Bal b/d	8,00,000	4,00,000	-	
To Reserve	2,25,000	1,50,000	75,000	75,000	By Memo Rev.	14,000	7,000	-	
To A&B	-	-	12,000	12,000	By Reserve	3,50,000	1,75,000	-	
To Bal c/d	9,50,000	4,30,000	2,15,000	2,15,000	By P&Q	20,000	4,000	-	
					By Cash (Bal Fig)	-	-	3,05,000	3,05,000
	11,84,000	**5,86,000**	**3,05,000**	**3,05,000**		**11,84,000**	**5,86,000**	**3,05,000**	**3,05,000**

Balance Sheet

Liabilities	Amount	Assets	Amount
Capital Account		Plant & Machinery	5,00,000
A	9,50,000	Building	9,00,000
B	4,30,000	Sundry Debtors	2,50,000
P	2,15,000	Stock	3,00,000
Q	2,15,000	Cash (1,50,000+3,05,000+3,05,000)	7,60,000
Reserve	5,25,000		
Creditors	2,75,000		
Bills Payables	1,00,000		
	27,10,000		**27,10,000**

Working Notes:

1. Calculation of Goodwill : Weighted Average Profit:

Year	Profit	Weight	Weighted Profit
2018	37,000	1	37,000
2019	40,000	2	80,000
2020	45,000	3	1,35,000
		6	**2,52,000**

Weighted Average Profit = Rs. 2,52,000/6= Rs. 42,000
Goodwill is valued at 2 year's purchase
Value of Goodwill: Rs. 42,000 × 2 = Rs. 84,000

2. Adjustment for goodwill

	A	B	C	D
Cr. in Old Ratio	56,000	28,000	-	-
Dr. in New Ratio	(36,000)	(24,000)	(12,000)	(12,000)
	20,000 Cr.	**4,000 Cr.**	**12,000 Dr.**	**12,000 Dr.**

3. Calculation of closing capitals of P and Q; B's capital is taken as base.
Closing capital of B after all adjustments is 4,30,000.
Total capital of firm will be= 4,30,000 x7/2 = 15,05,000
Hence, P's and Q's closing capital should be Rs. 2,15,000 (15,05,000 x 1/7) each i.e. at par with B (as per new profit and loss sharing ratio)

Question

A, B and C is a firm sharing profits and losses in the ratio 3:2:1. Their Balance Sheet as on 31st March, 2021 is as below:

Liabilities		Rs.	Assets	Rs.
Trade Payables		17,500	Land and Buildings	17,000
Outstanding liabilities		2,200	Furniture & Fixtures	7,200
Employer's Provident Fund		5,000	Stock	12,600
General reserve		1,800	Trade Receivables	10,700
Capital Account:			Cash & Bank	5,000
A	11,000			
B	8,000			
C	7,000	26,000		
		52,500		**52,500**

The partners have agreed to take D as a partner with effect from 1st April, 2021 on the following terms:

(1) D shall bring 10,000 towards his capital.
(2) The value of stock to be increased to Rs. 14,000 and Furniture & Fixtures to be depreciated by 10%.
(3) Reserve for bad and doubtful debts should be provided at 5% of the Trade Receivables.
(4) It is found that the trade payables included a sum of Rs.1,500, which is not to be paid off.
(5) The unaccrued income is Rs. 1,045.
(6) A claim on account of workmen's compensation for Rs. 300 to be provided for.
(7) Mr. X, an old customer whose account for Rs. 2,000 was written off as bad has promised in writing to pay 65% in settlement of his full debt.
(8) The value of land and buildings to be increased by 4,100 and the value of the goodwill be fixed at Rs. 18,000 and new partner bring his share of goodwill in cash.
(9) The new profit sharing ratio shall be divided equally among the partners

The outstanding liabilities include Rs. 700 due to Ram which has been paid by A. Necessary entries were not made in the books.

It was decided that the total capital of the firm after admission of new partner would be Rs. 40,000. Capital accounts of partners will be readjusted on the basis of their profit sharing ratio and excess or deficiency will be adjusted in cash.

Prepare

(i) Revaluation Account, and
(ii) The Capital Accounts of the partners, and
(iii) Balance Sheet of the firm after admission of D

Solution

Revaluation A/c

Particulars	Rs.	Particulars	Rs.
To Furniture & Fixtures	720	By Stock	1,400
To Provision for Doubtful Debts	535	By Trade Payables	1,500
To Unaccrued incomes	1,045	By Mr. X (Debtor)	1,300
To Workmen compensation claim	300	By Land & Building	4,100
To Profit transferred to			
A's Capital A/c 2,850			
B's Capital A/c 1,900			
C's Capital A/c 950	5,700		
	8,300		**8,300**

Capital Accounts

	A	B	C	D		A	B	C	D
To A & B Cap. A/cs			1,500	4,500	By Bal b/d	11,000	8,000	7,000	-
To Cash (Bal.Fig)	9,950	2,000		-	By Revaluation A/c	2,850	1,900	950	-
To Bal c/d	10,000	10,000	10,000	10,000	By Gen. Reserve	900	600	300	-
					By C & D Cap. A/cs	4,500	1,500	-	-
					By Cash	-	-	-	14,500
					By O/s Liability	700	-	-	-
					By Cash (Bal.Fig)			3,250	
	19,950	**12,000**	**11,500**	**14,500**		**19,950**	**12,000**	**11,500**	**14,500**

Balance Sheet

Liabilities	Amount	Assets		Amount
Capital Account		Land & Building		21,100
A	10,000	Furniture & Fixtures		6,480
B	10,000	Stock		14,000
C	10,000	Trade Receivables	10,700	
D	10,000	Less Prov. for Doubtful Debts	(535)	10,165
Trade Payables	16,000	Mr. X (Debtor)		1,300
Employers Provident Fund	5,000	Cash & Bank (5,000+14,500+3,250-9,950-2,000)		10,800
Outstanding Liabilities	1,500			
Workmen compensation Claim	300			
Unaccrued incomes	1,045			
	63,845			**63,845**

Working Notes:

1. Adjustment for goodwill

	A	B	C	D
Cr. in Old Ratio (3:2:1)	9,000	6,000	3,000	-
Dr. in New Ratio (1:1:1:1)	(4,500)	(4,500)	(4,500)	(4,500)
	4,500 Cr.	**1,500 Cr.**	**1,500 Dr.**	**4,500 Dr.**

RETIREMENT OF PARTNER

CONCEPT OF RETIREMENT

- Whenever a partner retires, the continuing partners gain. So they arrange for the amount to be paid to discharge the claims of the retiring partners.
- On retirement of a partner, it is required to revalue assets and liabilities just as in the case of admission of a partner. If there is revaluation profit/loss, then such profit/loss should be distributed amongst the existing partners including the retiring partner at the existing profit sharing ratio (i.e Old PSR)
- On the retirement of a partner any undistributed profit or reserve standing at the Balance Sheet is to be credited to the Partners' Capital Accounts in the old profit sharing ratio.

Example 1
P, Q & R having PSR 4 : 3 : 2 . Q retires & surrenders 1/9th of his share in favour of P & remaining in favour of R.

Share to P = $3/9 \times \frac{1}{9} = \frac{3}{81}$

Share to R = $3/9 \times \frac{8}{9} = \frac{24}{81}$

New Share

P = $\frac{4}{9} + \frac{3}{81} = \frac{39}{81}$

R = $\frac{2}{9} + \frac{24}{81} = \frac{42}{81}$

NR = 39 : 42 = 13 : 14

Example 2
X, Y, Z having PSR 4 : 3: 2, Y retires & surrender 1/9th from his share in favour of X & remaining in favour of Z.

X share = $\frac{4}{9} + \frac{1}{9} = \frac{5}{9}$

Z share = $\frac{2}{9} + \frac{2}{9} = \frac{4}{9}$

NR = 5:4

TREATMENT OF GOODWILL

Old goodwill
↓
Already appearing in B/sheet
↓
Partner's capital A/c – Dr
  To Goodwill A/c

Goodwill arising at the time of retirement
↓
Gaining Partner's capital A/c - Dr
  To Sacrificing Partner's capital A/c

[Cr in DR
Dr in NR]

Example
X, Y & Z having PSR 2 : 3 : 5. Goodwill appearing in the books Rs. 50,000. X retires & Goodwill valued at Rs. 45,000. Y & Z decided to share equally.

X 10000
Y 15000
Z 25000
To Goodwill 50000

	X	Y	Z
Cr in OR	9000	13500	22500
Dr in NR	-	(22500)	(22500)
	9000	9000	-
	Cr.	Dr.	

HIDDEN GOODWILL

Amount agreed to be paid in full settlement	XX
Less: Capital of retiring partners after all adjustments	(XX)
Hidden goodwill of the retiring partner.	XX

Example
A, B, C having PSR 1 : 2: 3, C retires & his capital after all adjustments was Rs. 2,20,000. A & B agreed to pay to C Rs. 2,50,000. New Ratio = 1 : 3

C's share of G/w
250000 - 220000
⇒ 30000

G/w of Firm ⇒ $30000 \times 6/3 = 60000$

	A	B	C
Cr in OR (1:2:3)	10000	20000	30000
Dr in NR (1:3)	(15000)	(45000)	-
	5000	25000	30000
	Dr.	Dr.	Cr.

FINAL PAYMENT TO RETIRING PARTNER

The following adjustments are necessary in the Capital A/c:

(i) Transfer of Profit/Loss on Revaluation.
(ii) Transfer of Reserve
(iii) Transfer of Goodwill

After adjustment of the above mentioned items, the Capital Account balance standing to the credit of the retiring partner represents amount to be paid to him.
Claim of the retiring partner is payable in the following forms:

- Fully in cash
- Fully transferred to loan account to be paid later with some interest on it.
- Partly in cash and partly as loan repayable later with agreed interest.

Question

On 31st March, 2021, the balance sheet of M/s Ram, Rahul and Rohit sharing profits and losses in proportion to their capital, stood as follows:

Liabilities		Rs.	Assets	Rs.
Capital Accounts:			Land & building	2,00,000
Ram	3,00,000		Machinery	2,00,000
Rahul	2,00,000		Closing stock	1,00,000
Rohit	1,00,000	6,00,000	Sundry debtors	2,00,000
Sundry creditors		2,00,000	Cash and bank balances	1,00,000
		8,00,000		**8,00,000**

On 31st March, 2021, Ram desired to retire from the firm and the remaining partners decided to carry on. It was agreed to revalue the assets and liabilities on that date on the following basis:

1. Land and buildings be appreciated by 30%.
2. Adjustment for Machinery having net book value of Rs. 10,000 which had been scrapped during the year. The original cost of Machinery was Rs. 25,000.
3. Debts amounting Rs. 10,000 considered bad and further debts amounting Rs. 5,000 were considered doubtful and required 100% provision.
4. Liability for workmen compensation to the extent of Rs. 15,000 is to be brought into account.
5. An item of the inventory having value of Rs. 10,000 had been omitted from the stock valuation.
6. Provision of Rs. 5,000 to be made in respect of an outstanding bill of purchase.
7. Old credit balances of sundry creditors Rs. 10,000 be written back.
8. Joint life policy of the partners surrendered and cash obtained Rs. 25,000.
9. Goodwill of the entire firm be valued at Rs.1,80,000 and Ram's share of the goodwill be adjusted in the accounts of Rahul and Rohit who share the future profits equally. No goodwill account being raised.
10. The total capital of the firm is to be the same as before retirement. Individual capital be in their profit sharing ratio.
11. Amount due to Ram is to be settled on the following basis:50% on retirement and the balance 50% within one year

Prepare revaluation account, capital account of partners: Rahul & Rohit, loan account of Ram, cash account and balance sheet as on 1.4.2021 of M/s Rahul and Rohit.

Solution

Revaluation Account

Particulars	Rs.	Particulars	Rs.
To Machinery	10,000	By Land & Buildings	60,000
To Bad Debts	10,000	By Inventory/Stock	10,000
To Provision for Bad Debts	5,000	By Creditors	10,000
To Provision for Workmen Claim	15,000	By Joint Life Policy	25,000
To Provision for Bill	5,000		
To Profit on revaluation t/f to			
Ram's capital A/c	30,000		
Rahul's capital A/c	20,000		
Rohit's capital A/c	10,000		
	1,05,000		**1,05,000**

Partners' Capital Accounts

	Ram	Rahul	Rohit		Ram	Rahul	Rohit
To Ram's Capital	-	30,000	60,000	By Balance b/d	3,00,000	2,00,000	1,00,000

To Cash & Bank	2,10,000			By Revaluation A/c	30,000	20,000	10,000
To Ram's Loan	2,10,000			By Rahul's Capital	30,000		
To Balance c/d	-	3,00,000	3,00,000	By Rohit's Capital	60,000		
				By Cash & Bank	-	1,10,000	2,50,000
	4,20,000	**3,30,000**	**3,60,000**		**4,20,000**	**3,30,000**	**3,60,000**

Ram's Loan Account

Particulars	Rs.	Particulars	Rs.
To Balance c/d	2,10,000	By Ram's Capital A/c	2,10,000
	2,10,000		**2,10,000**

Cash & Bank Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	1,00,000	By Ram's Capital	2,10,000
To Joint Life Policy	25,000	By Balance c/d	2,75,000
To Rahul's Capital	1,10,000		
To Rohit's Capital	2,50,000		
	4,85,000		**4,85,000**

Balance Sheet

Liabilities	Amount	Assets	Amount
Capital Account		Land & Building	2,60,000
Rahul 3,00,000		Machinery	1,90,000
Rohit 3,00,000	6,00,000	Stock	1,10,000
Ram's Loan Account	2,10,000	Debtors 1,90,000	
Creditors	1,90,000	Less:Provision for Bad Debts(5,000)	1,85,000
Provision for Workmen Claim	15,000	Cash & Bank	2,75,000
Provision for Bill	5,000		
	10,20,000		**10,20,000**

Working Notes:

(1) Adjustment of goodwill:

Goodwill of the firm = 1,80,000

Particulars	Ram	Rahul	Rohit
Credit in Old Ratio (3:2:1)	90,000	60,000	30,000
Debit in New Ratio (1:1)		(90,000)	(90,000)
	90,000 Cr.	**30,000 Dr.**	**60,000 Dr.**

Question

Anuj Ayush and Piyush are in partnership sharing profits and losses in the ratio 2 : 2 : 1. Their Balance Sheet as on 31.3 .2021 is as follows:

Liabilities		Rs.	Assets	Rs.
Capital Account:			Fixed Assets	
Anuj	3,75,000		Plant	7,87,000
Ayush	2,80,000		Current assets	
Piyush	2,25,000	8,80,000	Stock	1,03,000
General Reserve		1,88,000	Debtors	1,56,000
Creditors		2,16,000	Bank FD	2,25,000
			Bank balance	13,000
		12,84,000		**12,84,000**

Anuj decided to retire with effect from 1.4.2021. The remaining partners agreed to share profits and losses equally in future. The following adjustments were agreed to be made upon retirement of Anuj.

(a) Goodwill was to be valued at 1year purchase of the average profits of the preceding 3 years on the date of retirement. The average profits of the past 3 years were as follows:

Year ended	Rs.
31.03.2021	3,30,000 (as per draft accounts)
31.03.2020	2,32,000
31.03.2019	2,20,900

The partners decided not to raise goodwill account in the books.

(b) The assets were revalued as follows:
Plant to be depreciated by 10%
Creditors amounting to Rs. 10,000 were omitted to be recorded;
Rs. 6,000 is to be written off from stock;
Provision for doubtful debts to be created @ 5% of the debtors;
Interest accrued on FD amounting to Rs. 9,000 was omitted to be recorded.
The above adjustments were to be made from the profit for the year ended 31.3.2021 before calculation of goodwill.

(c) Anuj agreed to take over the bank FD including interest accrued thereon in part payment of his dues and the balance would remain as a loan, carrying interest of 8% p.a.

(d) Ayush and Piyush agreed to bring in sufficient cash to make their capital proportionate and maintain a bank balance of Rs. 1,50,000.

You are required to prepare
(1) Capital accounts of partners as on 1.4.2021 giving effect to the above adjustments.
(2) Balance Sheet as on 1.4.2021 after Anuj's retirement

Solution

Partner's Capital Accounts as on 1.4.2021

	Anuj	Ayush	Piyush		Anuj	Ayush	Piyush
To Anuj		22,980	68,940	By Balance b/d	3,75,000	2,80,000	2,25,000
To Revaluation Loss	37,400	37,400	18,700	By General Reserves	75,200	75,200	37,600
To Bank FD	2,34,000			By Ayush & Piyush	91,920		
To 8% Loan	2,70,720			By Cash (Bal. fig.)		8,570	1,28,430
To Balance c/d*		3,03,390	3,03,390				
	5,42,120	**3,63,770**	**3,91,030**		**5,42,120**	**3,63,770**	**3,91,030**

Balance Sheet as on 1.4.2021 after Anuj retirement

Liabilities	Amount	Assets		Amount
Anuj's Loan	2,70,720	Plant (90% of 7,87,000)		7,08,300
Creditors (2,16,000 + 10,000)	2,26,000	Stock (1,03,000 - 6,000)		97,000
Capital Accounts*		Debtors	1,56,000	
Ayush	3,03,390	Less: Provision	(7,800)	1,48,200
Piyush	3,03,390	Bank Balance		1,50,000
	11,03,500			**11,03,500**

*Total of capital balances should be Rs.6,06,780 which is proportioned to individual partners in their profit sharing ratio.

Working Notes:

1. Profit /Loss on revaluation

Revaluation Account

	Amount		Amount
To Plant	78,700	By Interest on FD	9,000
To Creditors	10,000	By Loss on revaluation	93,500
To Inventory	6,000		
To Provision for doubtful debts	7,800		-
	1,02,500		**1,02,500**

2. Calculation of Goodwill

Goodwill Valuation

Profit of year ended	Rs.
31.3.2021 (3,30,000 less 93,500)	2,36,500
31.3.2020	2,32,000
31.3.2019	2,20,900
Total Profits	6,89,400

Average Profit = 6,89,400/3 = 2,29,800

Goodwill valued 1 year purchased amounting Rs. 2,29,800.

3. Adjustment for goodwill among partners

Particulars	Anuj	Ayush	Piyush
Credit in Old Ratio (2:2:1)	91,920	91,920	45,960
Debit in New Ratio (1:1)	-	1,14,900	1,14,900
	91,920 Cr.	**22,980 Dr.**	**68,940 Dr.**

DEATH OF PARTNER

CONCEPT OF DEATH OF PARTNER

- The problems arising on the death of a partner are similar to those arising on retirement. Assets and liabilities have to be revalued and the resultant profit or loss has to be transferred to the Capital Accounts of all partners including the deceased partner. Goodwill is dealt with exactly in the way already discussed in the case of retirement.
- The only additional point is that as death may occur on any day, the representatives of the deceased partner will be entitled to the partner's share of profit from the beginning of the year to the date of death. After ascertaining the amount due to the deceased partner, it should be credited to his Executor's Account.
- If the death takes place during the accounting period, the Executor of the deceased partner is entitled to have a share of profit upto the date of death based on the profit earned in the immediately preceding year or some other agreed basis.

The balance from Capital A/c of deceased partner is transferred to the ***Deceased Partner's Executor A/c***.

Deceased Partner's Capital A/c

Particulars	**Amount**	**Particulars**	**Amount**
To Drawings A/c		By Balance b/d	
To Interest on Drawing A/c		By Interest on capital	
To Goodwill A/c (Existing G/w written off)		By P & L Suspense A/c (Share of profit)	
To Undistributed losses		By Reserve A/c	
To Revaluation (Loss)		By Revaluation A/c (profit)	
To Deceased Partner's Executor A/c **(Bal. Fig.)**		By Gaining partners capital A/c (Share of G/w)	

How to Calculate Outgoing partner's share in profits earned from the date of last balance sheet to the date of death/retirement

Step (1):

Calculate the Profits of the firm from the date of last Balance sheet to the date of death/retirement.

i. Time Basis

$$\frac{\text{Previous year's profits Or Avg. profits of past years X No. of days/months from the date of last b/sheet}}{\text{365 days/12 months}}$$

ii. Sales basis

$$\frac{\text{Previous year's profits Or Avg. profits of past years X Sales from the date of last b/sheet}}{\text{Previous years' Sales/Average Sales of past years}}$$

Step (2):

Calculate outgoing partners share in profits.

= Step (1) X Proportion of share of outgoing partner

Accounting Treatment

I) Through P & L suspense A/c

Profit : P & L Suspense A/c Dr.
To Outgoing partner's capital A/c

Loss : Outgoing partner's capital A/c Dr.
To P & L Suspense A/c

Balance of P&L suspense A/c is transferred to the P & L Appropriation A/c at the end of accounting period.

II) Through the Capital A/c of the gaining partner
Gaining partner's capital A/c Dr.
To Outgoing partner's capital A/c

PARTNERS : A, B & C
PSR : 5:3:2

Profits = 300000

Case 1: Time Basis

Share of C = $\left(300000 \times \frac{4}{12}\right) \times \frac{2}{10} = 20000$

Case 2: Sales Basis

T/O Last Year = 5000000   T/O (4 Months) = 2000000

Share of C = $\left(300000 \times \frac{2000000}{5000000}\right) \times \frac{2}{10} = 24000$

Question

Arup and Swarup were partners. The partnership deed provides inter alia:

a) That the annual accounts be balanced on 31st December each year;
b) That the profits be allocated as follows:
   Arup: One-half; Swarup: One-third and Carried to reserve account: One Sixth;
c) That in the event of death of a partner, his executor will be entitled to the following:
   1) The capital to his credit at the date of death;
   2) His proportionate share of profit to date of death based on the average profits of the last three completed years; and
   3) His Share of goodwill based on three years' purchase of the average profits for the three preceding completed years

Trial Balance as on 31st December 2020

Particulars	Debit (Rs.)	Credit (Rs.)
Arup's Capital		90,000
Swarup's Capital		60,000
Reserve		45,000
Bills receivable	50,000	
Investment	55,000	
Cash	1,10,000	
Trade payables		20,000
Total	**2,15,000**	**2,15,000**

The profits for the three year were 2018: Rs. 51,000; 2019: Rs. 39,000 and 2020. Rs. 45,000. Swarup died on 1st May 2021.
Show the calculation of Swarup (A) Share of profits; (B) Share of Goodwill; (C) Draw up Swarup's Executors Account as would appear in the firms' ledger transferring the amount to the Loan account.

Solution

(a) Arup : Swarup : Reserve

$\frac{1}{2} : \frac{1}{3} : \frac{1}{6} = \frac{3:2:1}{6}$

(A) Calculation of Swarup Share of Profits From 1st Jan, 2021 to 1st May, 2021:

Average profits = (45000+39000+51,000)/3
= 1,35,000/3
= 45,000

Profit From 1st Jan, 2021 to 1st May, 2021 = 45000×4/12 =15000

Swarup's Share in Profit = 15000×2/5 = 6,000

(B) Calculation of Swarup's Share in Firm's Goodwill :

Average profits = (45000+39000+51,000)/3
= 1,35,000/3 = 45000

Goodwill = Average Profits × No. of year's purchase
= 45000×3
= 1,35,000

Swarup's Share in Goodwill = 1,35,000 ×2/5 = 54000

Ledger of Firm

Dr. **Swarup's Executors Account** **Cr.**

Particulars	Amount	Particulars	Amount
To Swarup's Executors Loan A/c (Bal. Fig.)	1,38,000	By Swarup's capital A/c	60,000
		By Profit & Loss Suspense A/c	6,000
		By Arup's Capital A/c (Share in Goodwill)	54,000
		By Reserve (45000×2/5)	18,000
	1,38,000		**1,38,000**

RETIREMENT/DEATH & ADMISSION

Simultaneous retirement/death and admission do not introduce any new principles of accounting.
The principles studied under admission and retirement/death are combined-the combination of the two sets of transactions.
In case there is retirement/death & simultaneous admission we need to check whether the admission is on the same date or after a subsequent period of time.

Retirement/Death & Admission on the different dates:

1) Treatment of Accumulated Profits, Revaluation of Assets & Liabilities: Adjustment of these will be between old partners in old ratio.
2) Effect of Goodwill: Separate entries will be passed since both the events are on different dates.

Retirement/Death & Admission on the same date:

1) Treatment of Accumulated Profits, Revaluation of Assets & Liabilities: Adjustment of these will be between old partners in old ratio.
2) Effect of Goodwill: Single entry will be passed since both the events are on same date.

A B C C Retired D Admitted

OR 5 : 3 : 2 A : B : D

G/w = 100000 NR 4 : 3 : 3

Case 1: Different Dates

	A	B	C
Cr in OR	50000	30000	20000
Dr in NR	(62500)	(37500)	
	12500 Dr.	7500 Dr.	20000 Cr.

	A	B	D
Cr in OR	62500	37500	-
Dr in NR	(40000)	(30000)	(30000)
	22500 Cr.	7500 Cr.	30000 Dr.

Case 2: Same Dates

	A	B	C	D
Cr in OR (5:3:2)	50000	30000	20000	-
Dr in NR (4:3:3)	(40000)	(30000)		(30000)
	10000 Cr.	-	20000 Cr.	30000 Dr.

Question

Neha & Co. is a partnership firm with partners Mr. P, Mr. Q and Mr. R, sharing profits and losses in the ratio of 10:6:4. The balance sheet of the firm as at 31st March, 2021 is as under:

Liabilities	Rs.	Assets	Rs.
Capitals		Land	10,000
P 80,000		Buildings	2,00,000

Q 20,000		Plant and machinery	1,30,000
R 30,000	1,30,000	Furniture	43,000
Reserves	20,000	Investments	12,000
Long Term Debt	3,00,000	Inventories	1,30,000
Bank Overdraft	44,000	Trade receivables	1,39,000
Trade payables	1,70,000		
	6,64,000		**6,64,000**

It was mutually agreed that Mr. Q will retire from partnership and in his place Mr. T will be admitted as a partner with effect from 1st April, 2021. For this purpose, the following adjustments are to be made:

a) Goodwill is to be valued at Rs.1 lakh but the same will not appear as an asset in the books of the reconstituted firm.

b) Buildings and plant and machinery are to be depreciated by 5% and 20% respectively. Investments are to be taken over by the retiring partner at Rs.15,000. Provision of 20% is to be made on Trade receivables to cover doubtful debts.

c) In the reconstituted firm, the total capital will be Rs. 2 lakhs which will be contributed by Mr. P, Mr. R and Mr. T in their new profit sharing ratio, which is 2:2:1.

(i) The surplus funds, if any, will be used for repaying bank overdraft.

(ii) The amount due to retiring partner shall be transferred to his loan account.

Required:

Prepare

(a) Revaluation account;

(b) Partners' capital accounts;

(c) Bank account; and

(d) Balance sheet of the reconstituted firm as on 1st April, 2021

Solution

Revaluation Account

Particulars	Rs.	Particulars		Rs.
To Buildings	10,000	By Investments		3,000
To Plant & Machinery	26,000	By Loss transferred		
To Provision for doubtful Debts	27,800	P's Capital	30,400	
		Q's Capital	18,240	
		R's Capital	12,160	60,800
	63,800			**63,800**

Partner's Capital Accounts

Particulars	P	Q	R	T	Particulars	P	Q	R	T
To Revaluation	30,400	18,240	12,160	--	By Bal. b/d	80,000	20,000	30,000	--
To Investment	--	15,000	--	--	By Reserves	10,000	6,000	4,000	--
To Q's Loan	-	22,760	-	--	By R & T's Capital	10,000	30,000	-	--
To P & Q's Capital	-	-	20,000	20,000	By Bank (Bal. Fig.)	10,400	--	78,160	60,000
To Bal. c/d	80,000	--	80,000	40,000					
	1,10,400	**56,000**	**1,12,160**	**60,000**		**1,10,400**	**56,000**	**1,12,160**	**60,000**

Bank Account

Particulars	Rs.	Particulars	Rs.
To P's Capital	10,400	By Bank Overdraft	44,000
To R's Capital	78,160	By Balance c/d	1,04,560
To T's Capital	60,000		
	1,48,560		**1,48,560**

Balance Sheet as at 01.04.2021

Liabilities		**Rs.**	**Assets**		**Rs.**
Partners' capital accounts			Land		10,000
P's capital	80,000		Buildings		1,90,000
Q's capital	80,000		Plant & Machinery		1,04,000
T's capital	40,000	2,00,000	Trade Receivables	1,39,000	
Long Term Debt		3,00,000	*Less*: Provision	(27,800)	1,11,200
Trade Payables		1,70,000	Furniture		43,000
Q's Loan Account		22,760	Inventories		1,30,000
			Balance at Bank		1,04,560
		6,92,760			**6,92,760**

Working Note:

1. Calculation for adjustment of Amount of Goodwill

Particulars	**P**	**Q**	**R**	**T**
Credit in Old Ratio (10:6:4)	50,000	30,000	20,000	
Debit in New Ratio (2:2:1)	40,000	-	40,000	20,000
	10,000 Cr.	**30,000 Cr.**	**20,000 Dr.**	**20,000 Dr.**

Right of Outgoing partner to share subsequent profits/Calculation of Relief u/s 37

Relief is allowed to outgoing partner. The same can be due to Retirement/Death.

Relief is allowed only if:

a) Outgoing partner's balance has not been fully settled

b) Firm does not allow only interest/share of profits on unsettled balance. i.e., partnership deed is silent.

❖ Relief is **higher** of the following

Unsettled balance X 6% p.a. X Period upto relief date

OR

$$\frac{\text{Profits earned upto relief date X Unsettled balance of outgoing partner}}{\text{Total capital of partners \& unsettled balance.}}$$

Note: Capital of partners should be calculated on the date of death/retirement after all adjustments.

Example

A, B, C having PSR 1 : 1 : 1. C retires on 31.10.2020 Capital of partners after all adjustments stood at Rs. 50,000, Rs. 75,000 & Rs. 1,20,000 respectively. A & B continued to carry on business without settling C's account. Final payment to C is made on 1.02.2021. Profits made during 3 months period amounted to Rs. 28,000. Find Relief u/s 37

① $120000 \times 6\% \times \frac{3}{12} = 1800$

② $28000 \times \frac{120000}{50000 + 75000 + 120000} = 28000 \times \frac{120000}{245000} = 13714$

Relief = 13714

Question

A, B and C were partners sharing profits and losses in the ratio of 2:2:1. Their Balance Sheet as on 1-4-2020 stood as follows:

Liabilities		**Rs.**	**Assets**	**Rs.**
Capital Account :			Fixed Assets	10,00,000
A	5,00,000		Inventory	2,50,000
B	4,00,000		Trade Receivables	3,50,000
C	3,00,000	12,00,000	Cash and bank	1,00,000
Reserves		1,00,000		
Trade Payables		4,00,000		
		17,00,000		**17,00,000**

On 1st October, 2020 C died. His representatives agreed that:

(i) Goodwill of the firm be valued at Rs. 5,00,000. Goodwill not to be shown off in books of Accounts.
(ii) Fixed Assets be written down by Rs. 1,00,000; and
(iii) In lieu of profits, C should be paid at the rate of 25% p.a. on his capital as on 1-4-2020.

Current years (2020-21) profits after charging depreciation of Rs. 95,000 (Rs. 50,000 related to the 1st half) was Rs. 4,05,000. Profit was evenly spread throughout the year.

The year-end figures of Inventory, Trade Receivables and Trade Payables and Cash and Bank Balances were respectively Rs. 2,30,000, 1,90,000, 3,50,000 and 43,770.

Particulars regarding their drawings are given below:

	Upto 1-10-2020	After 1-10-2020
A	41,250	50,000
B	41,250	50,000
C	17,500	

You are required:

i. Prepare the Balance Sheet of the firm as on 31.3.2021, assuming that final settlement to C's executors was made on 31.3.2021.
ii. Prepare the Capital A/cs of the partners as on 1.10.2020 & 31.3.2021

Solution

Profit after Depreciation	4,05,000
Add : Depreciation	95,000
Profit before Depreciation	**5,00,000**
Profit for the 1st half (assumed : evenly spread)	2,50,000
Less : Depreciation with respect to 1st half	(50,000)
Post Depreciation profit	**2,00,000**
Profit for the 2nd half	2,50,000
Less : Depreciation for the 2nd half	(45,000)
2nd half profit after Depreciation	**2,05,000**

P&L Appropriation Account (for the1st half)

Particulars	**Rs.**	**Particulars**	**Rs.**
To Interest on C's Capital (3,00,000*25%*6/12)	37,500	By Profit	2,00,000
To Profit t/f to			
A's capital A/c	81,250		
B's capital A/c	81,250		
	2,00,000		**2,00,000**

Partners' Capital Accounts (As on 01.10.2020)

	A	B	C		A	B	C
To Rev. loss of fixed assets	40,000	40,000	20,000	By Balance b/d	5,00,000	4,00,000	3,00,000
To Drawings	41,250	41,250	17,500	By Reserves	40,000	40,000	20,000
To C's Capital	50,000	50,000	-	By A's Cap.	-	-	50,000
To C's Exec.	-	-	4,20,000	By B's Cap.	-	-	50,000
To Bal c/d	4,90,000	3,90,000	-	By P&L App.	81,250	81,250	37,500
	6,21,250	**5,21,250**	**4,57,500**		**6,21,250**	**5,21,250**	**4,57,500**

Application of Section 37 of the Partnership Act

Either:

a) Interest = 4,20,000 X 6% X 6/12 = 12,600

or

b) Profit earned out of unsettled capital

$= 2,05,000 \times \frac{4,20,000}{(4,90,000+3,90,000+4,20,000)} = 66,230$

In the absence of specific agreement amongst partners on the above subject matter, the representatives of the deceased partner can receive at their option, interest at the rate of 6% p.a. or the share of profit earned for the amount due to the decease partner. In the above case, it would be rational to assume that the representatives would opt for Rs. 66,230

P&L Appropriation Account
(for the 2nd half)

Particulars	Rs.	Particulars	Rs.
To C's Executors A/c	66,230	By Profit	2,05,000
To Profit t/f to			
A's capital A/c	69,385		
B's capital A/c	69,385		
	2,05,000		**2,05,000**

Partners' Capital Accounts (As on 31.03.2021)

	A	B		A	B
To Drawings	50,000	50,000	By Balance b/d	4,90,000	3,90,000
To Balance c/d	5,09,385	4,09,385	By P&L App.	69,385	69,385
	5,59,385	**4,59,385**		**5,59,385**	**4,59,385**

C's Executor Account

	Rs.		Rs.
To Bank A/c	4,86,230	By C's Capital A/c	4,20,000
		By P&L App.	66,230
	4,86,230		**4,86,230**

Balance Sheet as at 31.03.21

Liabilities	Rs.	Assets		Rs.
Partners' Capital accounts		Fixed Assets	10,00,000	
A's capital	5,09,385	*Less*: Written down	(1,00,000)	
B's capital	4,09,385		9,00,000	
Trade Payables	3,50,000	*Less*: Depreciation	(95,000)	8,05,000
		Trade Receivables		1,90,000
		Inventory		2,30,000
		Cash and Bank		43,770
	12,68,770			**12,68,770**

JOINT LIFE POLICY

Insurance

- It's a contract between the two parties that if first party suffers any loss, the second party will make such loss good. Thus, the risk of one is assumed by the other.
- Party which transfers such risk is called **insured** & party which assumes such risk is called **insurer**.
- Insured pays the amount of **premium** to insurer in consideration of risk being undertaken by the insurer & in the event of mishappening, insurer provides the lump sum amount to insured in the name of claim

Types of Insurance

1.	Life Insurance	Life insurance is a contract that offers financial compensation in case of death or disability. In this amount is received generally at the time of death or maturity whichever is earlier.
2.	General Insurance	A general insurance is a contract that offers financial compensation on any loss other than death. It insures everything apart from life. In this amount is received at the time of happening of event

Joint Life Policy (JLP)

It is an insurance policy which is taken out by the partnership firm on the lives of all the partners. The amount of policy is payable by the Insurance Company either on the death or on maturity of policy, whichever is earlier. The firm pays annual premium to the insurer against the policy.

The objective of taking such a policy is to minimize the financial hardships to the event of payment of a large sum to the legal representatives of a deceased partner or to the retiring partner.

Instead of life policy taken jointly on the name of all the partners, all the partners may take individual life policies for each of them by paying the premium from the firm

ACCOUNTING TREATMENT OF JOINT LIFE POLICY

Method 1: Premium Paid is treated as Expense (Ordinary Expense Method)

In this case premium is treated as an expense and it is closed every year by transferring to profit and loss account.

1.	Payment of Premium	Insurance Premium A/c Dr. To Bank A/c
2.	Transfer to P&L A/c	Profit & Loss A/c Dr. To Insurance Premium

Example:

A, B and C shared profits and losses in the ratio of 5:3:2. They took out a joint life Policy in 2019 for Rs.1,00,000, a premium of Rs.5,000 being paid annually on 1st January. The surrender value of the policy on 31st December of various years was as follows: 2019 Nil; 2020 Rs. 3,000; 2021 Rs. 6,500. Prepare ledger accounts assuming Ordinary Expense Method.

Insurance Premium A/c

2019 1/1 To Bank A/c	5000	31/12 By P&L A/c	5000
2020 1/1 To Bank A/c	5000	31/12 By P&L A/c	5000
2021 1/1 To Bank A/c	5000	31/12 By P&L A/c	5000

Method 2: Premium Paid is treated as Asset (Surrender Value Method)

In this case insurance premium paid is first debited to life policy account and credited to bank account. At the end of the year the amount in excess of surrender value is treated as a loss and is transferred to Profit and Loss Account.

1.	Payment of Premium	JLP A/c Dr. To Bank A/c
2.	Transfer to P&L A/c	Profit & Loss A/c Dr. To JLP (JLP A/c Balance- its Surrender Value)

Example:

A, B and C shared profits and losses in the ratio of 5:3:2. They took out a joint life Policy in 2019 for Rs.1,00,000, a premium of Rs.5,000 being paid annually on 1st January. The surrender value of the policy on 31st December of various years was as follows: 2019 Nil; 2020 Rs. 3,000; 2021 Rs. 6,500. Prepare ledger accounts assuming Surrender Value Method.

JLP A/c

2019 1/1	To Bank A/c	5000	31/12	By P&L A/c	5000
2020 1/1	To Bank A/c	5000	31/12	By P&L A/c	2000
				By Bal c/d	3000
2021 1/1	To Bal b/d	3000	31/12	By P&L A/c	1500
	To Bank A/c	5000		By Bal c/d	6500

Method 3: Premium Paid is treated as Asset & Reserve is maintained (Reserve Method)

Under this method, premium paid is debited to JLP A/c and credited to Bank A/c.

At the end of the year, amount equal to premium is transferred from Profit and Loss Appropriation Account to Policy Reserve Account.

After this, policy account is brought down to its surrender value by debiting the life policy reserve account with amount which exceeds the surrender value of the policy.

1.	Payment of Premium	JLP A/c Dr. To Bank A/c
2.	Creation of Reserve	Profit & Loss Appropriation A/c Dr. To JLP Reserve
3.	Amount in excess of Surrender Value	JLP Reserve A/c Dr. To JLP A/c

Note: In the balance sheet JLP will appear on the Asset side & JLP Reserve will appear on the liability side at surrender value.

Example:

A, B and C shared profits and losses in the ratio of 5:3:2. They took out a joint life Policy in 2019 for Rs.1,00,000, a premium of Rs.5,000 being paid annually on 1st January. The surrender value of the policy on 31st December of various years was as follows: 2019 Nil; 2020 Rs. 3,000; 2021 Rs. 6,500. Prepare ledger accounts assuming Reserve Method.

JLP A/c

Date	Particulars	Amount	Date	Particulars	Amount
2019 1/1	To Bank A/c	5000	31/12	By JLP Res. A/c	5000
2020 1/1	To Bank A/c	5000	31/12	By JLP Res. A/c	2000
				By Bal c/d	3000
		5000			5000
2021 1/1	To Bal b/d	3000	31/12	By JLP Res. A/c	1500
	To Bank A/c	5000		By Bal c/d	6500
		8000			8000

JLP Reserve A/c

Date	Particulars	Amount	Date	Particulars	Amount
2019 31/12	To JLP A/c	5000	31/12	By P&L App. A/c	5000
2020 31/12	To JLP A/c	2000	31/12	By P&L App. A/c	5000
	To Bal c/d	3000			
		5000			5000
2021 31/12	To JLP A/c	1500	1/1	By Bal b/d	3000
	To Bal c/d	6500		By P&L App. A/c	5000
		8000			8000

DEATH OF PARTNER

JOINT LIFE POLICY [POLICY AMOUNT]

Ordinary Expense Method [JLP is not appearing in Books]
- Premium charged to P&L A/c every year
- Amount Received (Policy Amount) is credited to Partner's Capital A/c in PSR

Asset/Surrender Value Method [JLP appearing in Books at Surrender Value]
- JLP shown as asset at S.V.
- Amount received (net of S.V.) credited to Partner's Capital A/c

JLP & JLP Reserve Method [Reserve Method]
- Both maintained at S.V.
- Amount Received is credited to Partner's Capital A/c in PSR

<u>Example:</u>
A, B and C shared profits and losses in the ratio of 3:2:1 C died on 31.03.2021
Policy Amount 1,20,000 & Surrender Value 30,000

<u>Case 1</u>: JLP is not appearing in the books/Ordinary Expense Method
<u>Case 2</u>: JLP is appearing in the books at Surrender Value
<u>Case 3</u>: JLP & JLP Reserve are maintained at Surrender Value

<u>Common Entry</u>

Bank A/c —Dr	120000	
To JLP A/c		120000

<u>Case 1</u>

JLP A/c —Dr	120000	
To A		60000
To B		40000
To C		20000

<u>Case 2</u>

JLP A/c —Dr	90000	
To A		45000
To B		30000
To C		15000

<u>Case 3</u>

JLP Reserve A/c —Dr	120000	
To JLP		120000
JLP A/c —Dr	120000	
To A		60000
To B		40000
To C		20000

RETIREMENT OF PARTNER

JOINT LIFE POLICY [SURRENDER VALUE]

Ordinary Expense Method	Asset/Surrender Value Method	JLP & JLP Reserve Method
[JLP is not appearing in Books]	[JLP appearing in Books at Surrender Value]	[Reserve Method]
Amount Received (Surrender Value) is credited to Partner's cap. A/c in PSR	No Treatment	Distribute JLP Reserve in Their PSR

Example:
A, B and C shared profits and losses in the ratio of 3:2:1. C retired on 31.03.2021
Policy Amount 1,20,000 & Surrender Value 30,000

Case 1: JLP is not appearing in the books/Ordinary Expense Method
Case 2: JLP is appearing in the books at Surrender Value
Case 3: JLP & JLP Reserve are maintained at Surrender Value

Common Entry:

Bank A/c - Dr 30000
To JLP 30000

Case 1

JLP A/c - Dr 30000
To A 15000
To B 10000
To C 5000

Case 2

No Entry

Case 3

JLP Reserve A/c Dr. 30000
To A 15000
To B 10000
To C 5000

Important Point:

B/S

JLP 30000

Amount Rec. = 20000

Method 2:

Bank 20000
To JLP 20000

Revaluation/Capital A/c - Dr 10000
To JLP 10000

DEATH OF PARTNER

Separate/Individual Life Policy

Surrender value not appearing in books
Share in Own Policy + Share in Surrender value of Remaining Partner's Policy

Surrender value appearing in books
Share in Own Policy (Remaining Balance) [i.e. Policy Amount − S.V.]

Example:

A, B and C shared profits and losses in the ratio of 3:2:1. C died on 31.03.2021

	Policy Amount	Surrender Value
A	2,00,000	30,000
B	3,00,000	60,000
C	4,80,000	90,000

Case 1: Surrender Value not appearing in the books

Case 2: Surrender Value appearing in the books

Case 1:

Share of C = $\left(480000 \times \frac{1}{6}\right) + (30000 + 60000) \times \frac{1}{6}$

$= 80000 + 15000 = 95000$

Case 2:

Share of C = $(480000 - 90000) \times \frac{1}{6}$

$= 390000 \times \frac{1}{6} \Rightarrow 65000$

RETIREMENT OF PARTNER

Separate/Individual Life Policy

Surrender value not appearing in books
Share in Surrender value of all Partner's Life Policies

Surrender value appearing in books
No Treatment

Example:

A, B and C shared profits and losses in the ratio of 3:2:1. C retired on 31.03.2021

	Policy Amount	Surrender Value
A	2,00,000	30,000
B	3,00,000	60,000
C	4,80,000	90,000

Case 1: Surrender Value not appearing in the books

Case 2: Surrender Value appearing in the books

Case 1:

Share of C = $\left(90000 \times \frac{1}{6}\right) + (30000 + 60000) \times \frac{1}{6}$

$= 15000 + 15000 = 30000$

Case 2:

Share of C = NIL

DEPRECIATION

CONCEPT OF DEPRECIATION

Property, plant and equipment are tangible items that:

(a) are *held for use* in the production or supply of goods or services, for rental to others, or for administrative purposes; and

(b) are expected to be used during *more than* a period of *12 months*.

It is necessary that part of the acquisition cost of the fixed assets is treated or allocated as an expense in each of the accounting period in which the asset is utilized. *The amount of fixed assets allocated in such manner to respective accounting period is called depreciation.*

Meaning of Depreciation

Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life. Depreciation starts from the day asset is available for use.

OBJECTIVES FOR PROVIDING DEPRECIATION

1. True cost of production
2. Income measurement
3. True Position Statement
4. Funds for replacement

FACTORS FOR DEPRECIATION

Assessment of depreciation & amount of depreciation are usually based on the following three factors

- **Historical Cost** or other amount substituted for the Historical Cost of the Asset when revalued.
- **Estimated Useful Life**
- **Estimated Residual Value**

These factors are explained as follows -

1. **Historical Cost**:

Purchase price	XX
Add : Other Non-refundable taxes & duties	XX
Add: Any directly attributable cost of bringing the asset to its working condition for its intended use	XX
Less: Trade discount & rebates	(XX)
Cost of Asset	**XX**

2. **'Useful Life'** is either -
   (a) The period over which a depreciable asset is expected to be used by the enterprise, or
   (b) The number of production or similar units expected to be obtained from the use of the asset by the enterprise.

3. **Residual/Scrap Value** is the amount likely to be obtained by the disposal of the Fixed Asset at the end of its Useful Life.

DEPRECIABLE AMOUNT

'Depreciable Amount' of a Depreciable Asset is determined as under -

Particulars	Amount
Historical Cost, or other amount substituted for it in the Financial Statements Less: Estimated Residual Value	XX (XX)
Depreciable Amount	**XX**

METHODS OF DEPRECIATION

1. ***Methods Available***:
   The following methods are available for computing and allocating the depreciable amount of an asset over its useful life -
   - Fixed Instalment or Straight Line Method
   - Reducing Balance or Written Down Value (WDV) Method,
   - Sum of Digits of Years Method
   - Machine Hour Method,
   - Production Units Method,
   - Depletion Method,

Method 1: FIXED INSTALMENT/ORIGINAL COST OR STRAIGHT LINE METHOD (SLM)

Meaning	➢ Under this method, an equal or constant amount of depreciation is written off from Depreciable Asset every year. ➢ Suitable for assets which generates equal utility during every year of its useful life. ➢ At the end of the useful life of the asset, the cost of the asset will be NIL or equal to its Residual Value / Scrap Value.
Formula	Straight Line Depreciation $= \frac{\text{Cost of Asset Less Residual Value}}{\text{Useful Life}}$ SLM Depreciation Rate $= \frac{\text{SLM Depreciation}}{\text{Cost of Asset}} \times 100$
Example	X Ltd purchased a Machine costing Rs 10 Lakhs, having a useful life of 5 years. Its estimated Residual Value is Rs 1 Lakh. Depreciation $= \frac{10L - 1L}{5} = 180000$ p.a. Dep. Rate $= \frac{180000}{1000000} \times 100 = 18\%$

Method 2: REDUCING/DIMINISHING BALANCE/WRITTEN DOWN VALUE (WDV) METHOD

Meaning	➢ Depreciation Amount for each year is computed by applying a fixed % on the Opening Balance of the Asset (i.e. Diminishing Balance of the Asset.) ➢ Reducing Balance refers to the Written Down Value of the Asset, i.e. value of the asset as reduced by the depreciation upto the previous year. ➢ The value of the asset will never be extinguished, as it happens in SLM Method. ➢ Depreciation Rate is computed such that at the end of the useful life of the asset, the cost of asset will be equal to its Residual Value / Scrap Value.
Formula	WDV Depreciation Rate = $1 - \sqrt[n]{\frac{\text{Residual.Value}}{\text{Cost.of.Asset}}}$, where n = Useful Life.
Example	X Ltd purchased a machine costing Rs 10 Lakhs, and has ascertained its WDV rate as 10% p.a. Depreciation amounts for the first five years will be as under –

Particulars	Year 1	Year 2	Year 3
Cost / Opening WDV	1000000	900000	810000
(-)Depreciation	(100000)	(90000)	(81000)
Closing WDV	900000	810000	729000

Method 3: SUM OF DIGITS OF YEARS METHOD

Meaning	It is a variation of the WDV Method. Under this method, Depreciation Amount for each year is computed by applying the following formula -
Formula	Dep. = Depreciable Amt. x $\frac{\text{No.of years of balance useful life (including current year)}}{\text{Total of Digits of the Useful Life of the Asset (in years)}}$
Example	X Ltd purchased a machine costing Rs 78 Lakhs, having a useful life of 5 years, and estimated Scrap Value Rs 3 Lakhs. Depreciation amounts for the five years will be -

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Depreciation Amount for the year	$75 \times \frac{5}{15}$ ⇒ 25	$75 \times 4/15$ ⇒ 20	$75 \times \frac{3}{15}$ ⇒ 15	$75 \times \frac{2}{15}$ ⇒ 10	$75 \times \frac{1}{15}$ ⇒ 5

Note: Depreciation is calculated on the Depreciable Amt, i.e. Cost less Residual Value

Method 4: MACHINE HOUR METHOD

Meaning	In this method, Depreciation is computed based on the number of Machine Hours (rather than years). Where it is practicable to keep a record of the actual running hours of each machine, depreciation may be calculated on the basis of hours that the concerned machinery worked for. Under machine hour rate method of calculating depreciation, the life of a machine is not estimated in years but in hours. Thus depreciation is calculated after estimating the total number of hours that machine would work during its whole life
Formula	$\text{Dep.} = \text{Depreciable Amt} \times \frac{\text{No.of Machine Hours during the year}}{\text{Total Machine Hours during the entire useful life}}$
Example	X Ltd purchased a machine costing Rs 23,00,000, having a Scrap Value of Rs 2,30,000. The machine has a useful life of 20,700 machine hours distributed as under – • Years 1 to 3: 2,500 machine hours each, • Years 4 to 6: 2,000 machine hours each, and • Years 7 to 10: 1,800 machine hours each. In this case, Depreciation Amounts will be computed as under – Dep. (Yr 1 to 3) = $2070000 \times \frac{2500}{20700}$ = 250000 p.a. Dep. (Yr. 4 to 6) = $2070000 \times \frac{2000}{20700}$ = 200000 p.a. Dep. (Yr 7 to 10) = $2070000 \times \frac{1800}{20700}$ = 180000 p.a.

Method 5: PRODUCTION UNITS METHOD

Meaning	In this method, Depreciation is computed based on the production / output quantity.
Formula	$\text{Dep.} = \text{Depreciable Amt} \times \frac{\text{Production Quantity for the current year}}{\text{Total Estimated Production Quantity from the Machine}}$
Example	X Ltd purchased a machine costing Rs 25,00,000, having a Scrap Value of Rs 5,00,000. The machine is expected to produce 10,00,000 units of output in the following manner – • Years 1 & 2: 1,15,000 units each, • Years 3 to 7: 1,00,000 units each, and • Years 8 to 10: 90,000 units each. In this case, Depreciation Amounts will be computed as under – Dep. (Yr 1 & 2) = $20L \times \frac{115000}{10L}$ = 230000 p.a. Dep. (Yr 3 to 7) = $20L \times \frac{100000}{10L}$ = 200000 p.a. Dep. (Yr 8 to 10) = $20L \times \frac{90000}{10L}$ = 180000 p.a.

Method 6: DEPLETION METHOD

Meaning	➢ Depletion means reduction or exhaustion. ➢ This method is used in the case of Mines, Quarries, Oil Well, etc. containing only a certain estimated quantity of resources / products.
Formula	Dep. = Depreciable Amt x $\frac{\text{Quantity of Mineral / Oil extracted during current year}}{\text{Total Estimated Quantity from the Mine / Quarry / Well}}$
Example	X Ltd took a quarry on lease by paying Rs. 75,00,000. As per technical estimate, the total quantity mineral deposit is 1,00,000 tonnes. The extraction pattern is given below – • Year 1: 6,000 tones, • Years 2 to 5: 15,000 tones each, and • Years 6 & 7: 17,000 tones each. In this case, Depreciation Amounts will be computed as under – Dep. (Yr.1) = $75L \times \frac{6000}{1L} = 450000$ Dep. (Yr 2 to 5) = $75L \times \frac{15000}{1L} = 1125000$ p.a. Dep. (Yr 6 & 7) = $75L \times \frac{17000}{1L} = 1275000$ p.a.

ACCOUNTING ENTRIES FOR DEPRECIATION

Depreciation can be recorded in the books of account, under 2 approaches, which are described below -

Method	Method 1 Asset Credit Method	Method 2 Provision for Depreciation Method
Journal Entry	Depreciation A/c Dr. To Fixed Asset A/c Profit and Loss A/c Dr. To Depreciation A/c	Depreciation A/c Dr. To Provision for Depreciation A/c Profit and Loss A/c Dr. To Depreciation A/c
Provision for Depreciation A/c	There is no Provision for Depreciation Account at all.	Depreciation for each year is credited to Provision for Depreciation A/c, which shows the Accumulated Depreciation on the Asset.
Effect on Asset A/c	Asset A/c is shown at Historical Cost less Depreciation. So, balance in Asset A/c is reduced year after year.	Asset is shown in the books at Original Cost. Net Book Value = Original Cost less Accumulated Depreciation thereon.

Note: The above schemes are applicable to SLM and WDV Methods. The same treatment is applicable under - (a) Sum of Digits, (b) Machine Hours, (c) Production Units, and (d) Depletion Methods.

Example: Cost = 1000000 Life = 10 years Scrap Value = 100000 SLM

Dep. = $\frac{10L - 1L}{10}$

⇒ 90000 p.a.

Balance sheet

	Liabilities	Assets	Yr 1	Yr 2
Method 1:		Machinery	910000	820000
Method 2:		Machinery - Prov. for Dep.	1000000 (90000)	1000000 (180000)

CHANGE IN COST AND RESIDUAL VALUE/LIFE OF ASSET

CHANGE IN HISTORICAL COST

The Historical Cost of a depreciable asset may undergo subsequent changes arising as a result of increase or decrease in long term liability on account of —

(a) Exchange Rate Fluctuations,
(b) Price Adjustments,
(c) Changes in duties, or
(d) Other similar factors.

When the Historical Cost of an asset has undergone a change due to the above circumstances *the depreciation on the revised unamortised depreciable amount is provided prospectively over the residual useful life of the Asset.*

CHANGE IN ESTIMATED USEFUL LIFE & SCRAP VALUE

The useful lives & scrap values of major depreciable assets or classes of depreciable assets may be reviewed periodically. The change should be accounted for as a change in an accounting estimate
Where there is a revision of the estimated useful life or scrap value of an asset, *the unamortised depreciable amount should be charged over the revised estimate.*

Example

B Ltd. owns an asset with an original cost of Rs. 2,00,000. On acquisition, management determined that the useful life was 10 years and the residual value would be Rs. 20,000. The asset is now 8 years old, and during this time there have been no revisions to the assessed residual value. At the end of year 8, management has reviewed the useful life and residual value and has determined that the useful life can be extended to 12 years in view of the maintenance program adopted by the company. As a result, the residual value will reduce to Rs. 10,000. How would the above changes in estimates be made by B Ltd.?

Solution

The changes in estimates would be effected in the following manner:
The asset has a carrying amount of Rs. 56,000 at the end of year 8 [Rs. 2,00,000 – Rs. 1,44,000] i.e. Accumulated Depreciation.
Accumulated depreciation is calculated as
Depreciable amount {Cost less residual value} = Rs. 2,00,000 – Rs. 20,000 = Rs. 1,80,000.
Annual depreciation = Depreciable amount / Useful life = 1,80,000 / 10 = Rs. 18,000.
Accumulated depreciation = 18,000 × No. of years (8) = Rs. 1,44,000.
Revision of the useful life to 12 years results in a remaining useful life of 4 years (12 – 8).
The revised depreciable amount is Rs. 46,000. (56,000 – 10,000)
Thus, depreciation should be charged in future at Rs. 11,500 per annum (Rs. 46,000/4 years).

CHANGE IN METHOD OF DEPRECIATION

The depreciation method applied to an asset should be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method should be changed to reflect the changed pattern.
Whenever any change in depreciation method is made such change in method is treated as ***change in accounting estimate*** as per Accounting Standards.
Change in method of depreciation is applied with ***prospective effect***. Hence, depreciation is recalculated in accordance with the new method from the date method is changed.

REVALUATION OF DEPRECIABLE ASSETS

<table>
<tr><td rowspan="2">First Revaluation</td><td>Upward</td><td>Use Revaluation Surplus (R/S)</td></tr>
<tr><td>Downward</td><td>Use P & L A/c</td></tr>
<tr><td>Subsequent Revaluation</td><td colspan="2">
<table>
<tr><th>Case</th><th>1st</th><th>2nd</th><th>Ist</th><th>2nd</th></tr>
<tr><td>1</td><td>↑</td><td>↑</td><td>R/S</td><td>R/S</td></tr>
<tr><td>2</td><td>↓</td><td>↓</td><td>P & L</td><td>P & L</td></tr>
<tr><td>3</td><td>↑</td><td>↓</td><td>R/S</td><td>Use R/S 1st</td></tr>
<tr><td>4</td><td>↓</td><td>↑</td><td>P & L</td><td>Use P&L 1st</td></tr>
</table>
</td></tr>
</table>

Example

A Plant & Machinery costing Rs. 10,00,000 is depreciated on straight line assuming 10 year working life and zero residual value, for four years. At the end of fourth year, the machinery was revalued upwards by Rs. 40,000. The remaining useful life was reassessed at 8 years. Calculate depreciation for the fifth year.

Solution

Depreciable amount {Cost less residual value} = Rs. 10,00,000 – Nil = Rs. 10,00,000.
Annual depreciation = Depreciable amount / Useful life = 10,00,000 / 10 = Rs. 1,00,000.
Accumulated depreciation = 1,00,000 × No. of years (4) = Rs. 4,00,000.
Carrying amount at the end of year 4 = Rs. 6,00,000 [Rs. 10,00,000 – Rs. 4,00,000]

Revised carrying amount after revaluation = 6,00,000+40,000 = 6,40,000
Now remaining useful life 8 years . The revised depreciable amount is Rs. 6,40,000.
Thus, depreciation for 5^{th} year = Rs. 80,000 (Rs. 6,40,000/8 years).

RELATED MATTERS

CESSESATION OF DEPRECIATION

Depreciation ceases to be charged
A) When asset's residual value exceeds its carrying amount
The residual value of an asset may increase to an amount equal to or greater than its carrying amount. If it does, depreciation charge of the asset is zero unless and until its residual value subsequently decreases to an amount below its carrying amount.

B) At the *earlier of*:
• The date that the asset is retired from active use and is held for disposal, or
• The date that the asset is derecognised

RETIREMENT

Asset is retired from active use & held for disposal
❖ It is to be recorded in the books at Carrying Amount or NRV, whichever is lower.
❖ Any expected loss is recognized immediately in the P&L statement.

SALE / DISPOSAL OF DEPRECIABLE ASSETS

Sale/Disposal of Depreciable Assets in dealt with in the following manner —

1. Ascertain Depreciation for the year (upto the date of disposal), and charge the same for that year.
2. Determine Net Book Value" (or) Written Down Value of the Asset = Historical Cost less Depreciation till date, including depreciation upto the date of disposal.
3. Compare Net Book Value of Asset with its Disposal Value and ascertain Profit / (Loss) on disposal & thereafter transfer the Profit / (Loss) on disposal to the Profit and Loss Account.

Question

The M/s LG Transport purchased 10 trucks at Rs. 45,00,000 each on 1st April 2018. On October 1st, 2020, one of the trucks is involved in an accident and is completely destroyed and Rs. 27,00,000 is received from the insurance in full settlement. On the same date, another truck is purchased by the company for the sum of Rs. 50,00,000. The company writes off 20% on the original cost per annum. The company observe the calendar year as its financial year.
You are required to prepare the motor truck account for two year ending 31 Dec, 2021

Solution

Machine A/c

Date	Particulars	Amount	Date	Particulars	Amount
2020			2020		
1/1	To Balance b/d	2,92,50,000	1/10	By Bank A/c	27,00,000
1/10	To P&L A/c (Profit on Settlement of Truck)	4,50,000	1/10	By Depreciation on lost assets	6,75,000
1/10	To Bank A/c	50,00,000	31/12	By Depreciation A/c	83,50,000
			31/12	By Balance c/d	2,29,75,000
		3,47,00,000			**3,47,00,000**
2021			2021		
1/1	To Balance b/d	2,29,75,000	31/12	By Depreciation A/c	91,00,000
			31/12	By Balance c/d	1,38,75,000
		2,29,75,000			**2,29,75,000**

Working Note:

Opening balance on 01.01.2020

Original cost as on 1.4.2018	4,50,00,000
Less: Depreciation for 2018	(67,50,000)
	3,82,50,000
Less: Depreciation for 2019	(90,00,000)
	2,92,50,000

To find out Profit/Loss on settlement of truck

Original cost as on 1.4.2018	45,00,000
Less: Depreciation for 2018	(6,75,000)
	38,25,000
Less: Depreciation for 2019	(9,00,000)
	29,25,000
Less: Depreciation for 2020 (9 Months)	(6,75,000)
	22,50,000
Less: Amount received from Insurance company	(27,00,000)
Profit	**4,50,000**

Question

A Firm purchased an old Machinery for Rs. 37,000 on 1st January, 2018 and spent Rs. 3,000 on its overhauling. On 1st July 2019, another machine was purchased for Rs. 10,000. On 1st July 2020, the machinery which was purchased on 1st January 2018, was sold for Rs. 28,000 and the same day a new machinery costing Rs. 25,000 was purchased. On 1st July, 2021, the machine which was purchased on 1st July, 2019 was sold for Rs. 2,000.
Depreciation is charged @ 10% per annum on straight line method. The firm changed the method and adopted diminishing balance method with effect from 1st January, 2019 and the rate was increased to 15% per annum. The books are closed on 31st December every year.
Prepare Machinery account for four years from 1st January, 2018.

Solution

Machine A/c

Date	Particulars	Amount	Date	Particulars	Amount
2018			2018		
1/1	To Bank A/c (37,000+3,000)	40,000	31/12	By Depreciation A/c	4,000
			31/12	By Balance c/d	36,000
		40,000			**40,000**
2019			2019		
1/1	To Balance b/d	36,000	31/12	By Depreciation A/c (5,400+750)	6,150
1/7	To Bank A/c	10,000	31/12	By Balance c/d (30,600+9,250)	39,850
		46,000			**46,000**
2020			2020		
1/1	To Balance b/d	39,850	1/7	By Bank A/c	28,000
1/7	To Bank A/c	25,000	1/7	By Depreciation A/c	2,295
			1/7	By Profit & Loss A/c (Loss on sale)	305
			31/12	By Depreciation A/c (1,388+1,875)	3,263
			31/12	By Balance c/d (7,862+23,125)	30,987
		64,850			**64,850**
2021			2021		
1/1	To Balance b/d	30,987	1/7	By Bank A/c	2,000
			1/7	By Depreciation A/c	590
			1/7	By Profit & Loss A/c (Loss on sale)	5,272
			31/12	By Depreciation A/c	3,469
			31/12	By Balance c/d	19,656
		30,987			**30,987**

Working Note:

Book Value of machines (Straight line method)

	Machine 1	Machine 2	Machine 3
Cost of Machinery	40,000	10,000	25,000
Less: Depreciation for 2018	(4,000)		
Written down value as on 31.12.2018	36,000		
Less: Depreciation for 2019	(5,400)	(750) [6 months]	

Written down value as on 31.12.2019	30,600	9,250	
Less: Depreciation for 2020	(2,295) [6 months]	(1,388)	(1,875) [6 months]
Written down value as on 1.7.2020	**28,305**		
Less: Sale Proceeds	(28,000)		
Loss on Sale	**305**		
Written down value as on 31.12.2020		**7,862**	**23,125**
Depreciation for 6 months in 2021		(590)	
Written down value as on 1.7.2021		**7,272**	
Sale proceeds		(2,000)	
Loss on sale		**5,272**	
Depreciation for 2021			(3,469)
Written down value as on 31.12.2021			**19,656**

BILL OF EXCHANGE & PROMISSORY NOTE

BILL OF EXCHANGE -MEANING AND FEATURES

Meaning:

As per Sec. 5 of the Negotiable Instruments Act, 1881, a **Bill of Exchange** (B/E) is —

- an instrument in **writing,**
- containing an unconditional **order,**
- **signed** by the Maker,
- **directing** a certain person,
- to pay a certain sum of **money only**,
- to, or to the order of a certain **person** or to the **Bearer** of the instrument.

Note: When prepared by the **Maker** (i.e. Seller of Goods), it is called **Draft.** Once it is accepted by the **Acceptor** (i.e. Buyer of Goods), it becomes a valid Bill of Exchange.

Features of Bill of Exchange:

- ✓ It must be in **writing**.
- ✓ It must contain an **order** to pay. Order must be **unconditional**.
- ✓ It must be **dated**.
- ✓ The instrument must be to pay **money only** and the amount of money payable must be **certain.**
- ✓ The party must **sign** the instrument.
- ✓ It must be properly **stamped.**

Parties involved:

(a) The person who **makes** the order is known as the **Drawer** (or Maker), i.e. Seller of Goods.

(b) The person who **accepts** the order is known as the **Acceptor/ Drawee**, i.e. Buyer of Goods.

(c) The person to whom the amount is payable is known as the **Payee. [Note:** The Drawer and Payee may be the same person. Sometimes, the Drawer may order the payment to a third party, i.e. Payee.]

PROMISSORY NOTE – DEFINITION AND FEATURES

Meaning:

As per Sec. 4 of the Negotiable Instruments Act, 1881, a Promissory Note (P/N or Pro-Note) is –

- An instrument in **writing** (not being a Bank Note or a Currency Note),
- Containing an unconditional **undertaking**,
- Signed by the **Maker**,
- To pay a certain sum of **Money** only,
- To, or to the order of a certain **person**.

Note: A Promissory Note cannot be made payable to Bearer.

Features of a Promissory Note:

- ✓ P/N must be in **writing**.
- ✓ P/N must contain an **undertaking/promise to pay**. Mere acknowledgement of debt is not sufficient.
- ✓ The undertaking/promise to pay should be **unconditional and definite** (and not vague).
- ✓ P/N should be **signed by the Maker** himself.
- ✓ P/N should specify the Payee in clear terms
- ✓ Sum payable must be **certain**.
- ✓ P/N must be duly **stamped** and dated.
- ✓ It does **not** require any **acceptance**

CHART

Bills of Exchange

Bill at Sight or **Bill on presentment** or **Bill on Demand**
- When demanded then needs to make payment
- No Time Period
- No Grace Days

Bill after date → Due date considered from date of drawing of bill

Bill after Sight → From date of Acceptance of bill

(Bill after date and Bill after Sight:)
- Time Period mentioned
- 3 Days of Grace Applicable

Due Date or Date of Maturity ⇒ Date of Drawing or Date of Acceptance (After sight) + Term of Bill + 3 Days of Grace

Where term of bill can be specified no. of days or months.

Note: If the month in which period terminates has no corresponding day, period will terminate on last day of such month.

Date of Maturity is holiday

Public/Gazetted holiday → Preceding/Previous working day

[26/1, 15/8, 2/10, Sundays]

Emergency/Unforeseen/Sudden holiday → Succeeding/next working day

Example: Date of Bill 1/6/20

(a) Term 3 Months (b) Term 90 Days

Due Date/Maturity Date:

(a) 1/6/20 + 3M + 3D

⇒ 1/9/20 + 3D

⇒ 4/9/20

(b) 1/6/20 + 90D + 3D

⇒ 30/8 + 3D

⇒ 2/9/20

June = 29
July = 31
60
Aug. + 30
90

BASIC ENTRIES

Books of Drawer (A)

B - Dr	10000	
To Sales		10000
B/R - Dr	10000	
To B		10000

A → B: Sale 10000

Books of Drawee (B)

Purchases - Dr	10000	
To A		10000
A - Dr	10000	
To B/P		10000

BOOKS OF DRAWER (A)

	Held Bill Till Maturity	Discounting with Bank	Endorse to Creditor	Sent to Bank for collection
1) Event	–	Bank 9800 Discount 200 To B/R 10000	Creditor/C 10000 To B/R 10000	BSFC 10000 To B/R 10000
2) Maturity a) Honour	Bank 10000 To B/R 10000	–	–	Bank 10000 To BSFC 10000
OR b) Dishonour (Noting charges 100)	B 10100 To B/R 10000 To Bank 100	B 10100 To Bank 10100	B 10100 To C 10100	B 10100 To BSFC 10000 To Bank 100

BOOKS OF DRAWEE (B)

In all 4 cases, same entries to be passed :

Honour

B/P A/c - Dr	10000	
To Bank A/c		10000

Dishonour

B/P A/c - Dr	10000	
Noting charges A/c - Dr	100	
To A		10100

DISHONOUR OF BILL OF EXCHANGE AND PAYMENT OF NOTING CHARGES

1. **Dishonour:** Non-payment of Bill of Exchange on the due date is called **Dishonour.**
2. **Noting:** In case of dishonour of a B/E on the due date, the fact of dishonour, and the causes of dishonour should be ascertained and recorded on the B/E itself. Otherwise, the Acceptor may prove that B/E was not properly presented to him on the due date and hence can escape from his liability.
3. **Charges:** Noting Charges refers to the fees paid to a Public Official known as **"Notary Public",** who records the fact and causes of dishonour of B/E.
4. **Accounting:** Noting Charges is incurred by the person presenting the B/E on the due date, and is recoverable from the person causing the dishonour, i.e. the Acceptor.

RETIREMENT OF BILL OF EXCHANGE

1. Reason for Retirement	2. Accounting for Retirement
• Sometimes, the Acceptor of a B/E is ready to pay the amount, even before the due date. • So, the Acceptor may request the Payee, for settling the payment before due date. • This constitutes **Retirement of Bill.**	• Acceptor is entitled to receive certain Interest or Discount (called **Rebate**) for making payment before the due date. • This **Rebate** on Bills Retired before due date, constitutes Income of Acceptor, and Expense of Payee.

Example

On 1st January, 2021, A sells goods for Rs. 10,000 to B and draws a bill at three months for the amount. B accepts it and returns it to A. On 4th March, 2021, B retires his acceptance under rebate/discount of 12% per annum. Record these transactions in the journals of A and B

		A			B		
1/1	1)	B	10000		Purchases	10000	
		To Sales		10000	To A		10000
1/1	2)	B/R	10000		A	10000	
		To B		10000	To B/P		10000
4/3	3)	Bank	9900		B/P	10000	
		Disc./Rebate	100		To Bank		9900
		To B/R		10000	To Disc./Rebate		100

Rebate / Disc. = $10000 \times 12\% \times \frac{1}{12} = 100$

RENEWAL OF BILL OF EXCHANGE

1. Reason for Renewal	2. Accounting for Renewal
• Sometimes, the Acceptor of a B/E is unable to pay the amount on the due date. • In such case, the Acceptor may request the Drawer for an **extension** of time period. • This constitutes **Renewal of Bill**.	• Old B/E will be cancelled. So, the earlier Journal Entry relating to acceptance of Old B/E will be reversed. • New B/E will be made out. Journal Entries are passed for recording the New B/E. Sometimes, the value of New B/E = Value of Old B/E + Interest, if any.

The amount of the new bill may represent any of the following:

a) *Where the drawee pays nothing*: Total of amount of original bill as well as the interest for the extended time period.

b) *Where the drawee pays the interest amount at the time of renewal*: Amount of the Original bill.

c) *Where the drawee makes part payment of the original bill or interest amount or both*: That part of total of amount of original bill as well as the interest for the extended time period on unpaid amount.

A → B

1/4 —— +3M —— 4/7 —— +2M —— 7/9

Amount = 100000

Renewed @ 12% p.a.

	Case 1 (a)	Case 1 (b)	Case 2 (40000 paid) (a)	Case 2 (40000 paid) (b)
Interest paid now	✓	✗	✓	✗
Int. Amount	2000 (1L × 12% × 2/12)	2000	1200 (60000 × 12% × 2/12)	1200
New Bill	100000	102000	60000	61200

DEALING WITH INSOLVENCY OF DRAWEE

1. **Meaning:** Insolvency of the Drawee means that he will be unable to pay his liabilities. This means that bills accepted by him will be dishonoured on the due date.

Books of the Drawer

(a) For dishonour of B/R	Drawee A/c Dr. To Bills Receivable A/c
(b) For recording final amount, if any, received	Cash A/c Dr. (Amt actually received) Bad Debts A/c Dr. (Balancing Figure) To Drawee Account (Total Amount due)

Books of the Drawee

(a) For dishonour of B/R	Bills Payable A/c Dr. To Drawer A/c
(b) For recording final amount, if any, paid	Drawer Account Dr. (Total Amount due) To Cash A/c (Amt actually paid) To Deficiency A/c (Balancing Figure)

Question

Mr. B accepted a bill for Rs. 10,000 drawn on him by Mr. A on 1st August, 2020 for 3 months. This was for the amount which B owed to A. On the same date Mr. A got the bill discounted at his bank for Rs. 9,800. On the due date, B approached A for renewal of the bill. Mr. A agreed on condition that Rs. 2,000 be paid immediately along with interest on the remaining amount at 12% p.a. for 3 months and that for the remaining balance B should accept a new bill for 3 months. These arrangements were carried through. On 31st December, 2020, B became insolvent and his estate paid 40%. Prepare Journal Entries in the books of Mr. A

Solution

Books of A

Date	Particulars		L.F.	Debit	Credit
01.08.2020	Bills receivable A/c	Dr.		10,000	
	To B A/c				10,000
01.08.2020	Bank A/c	Dr.		9,800	
	Discount on Bills A/c	Dr.		200	
	To Bills Receivable A/c				10,000
04.11.2020	B A/c	Dr.		10,000	
	To Bank A/c				10,000
04.11.2020	B A/c	Dr.		240	
	To Interest A/c				240
	(Being the interest due from B for 3 months i.e., 8000x3/12x12%=240)				
04.11.2020	Cash A/c	Dr.		2,240	
	Bills receivable A/c	Dr.		8,000	
	To B A/c				10,240
31.12.2020	B A/c	Dr.		8,000	
	To Bills Receivable A/c				8,000
31.12.2020	Bank A/c	Dr.		3,200	
	Bad Debts A/c	Dr.		4,800	
	To B A/c				8,000

ACCOMODATION BILLS

1. Meaning:

(a) Generally, B/E is drawn in support of a trade transaction, i.e. credit sales. However, B/E can also be utilized for raising finance (i.e. without a trade transaction).

(b) When B/E is used for financing purposes, it is called as Accommodation Bill. (Note: An Accommodation Bill is referred to as "Kite".)

(c) A single B/E or different bills are drawn by one party on the other and discounted with the Bank, the proceeds to be shared by both parties in agreed ratio

(b) On the respective due dates of the B/E, both parties pay their respective dues to the Bank.

Question

A draws on B a bill of Rs. 45,000 on 1st June, 2020 for 3 months. B accepts the bill and sends it to A who discounted for Rs. 44,100. A immediately remits Rs. 14,700 (1/3rd proceeds) to B. On the due date A, being unable to remit the amount due, accepts a bill for Rs. 63,000 for three months which is discounted by B for Rs. 61,650. B sends Rs. 11,100 to A. On the due date A becomes insolvent, his estate paying forty paise in the rupee. Give the Journal Entries in the books of A and B.

Solution

Books of A

Date	Particulars		L.F.	Debit	Credit
01.06.2020	Bills receivable A/c	Dr.		45,000	
	To B A/c				45,000
	(Being the acceptance received from B for mutual accommodation)				
01.06.2020	Bank A/c	Dr.		44,100	
	Discount on Bills A/c	Dr.		900	
	To Bills Receivable A/c				45,000
	(Being bill discounted with bank)				
01.06.2020	B A/c	Dr.		15,000	
	To Bank A/c				14,700
	To Discount on Bills A/c				300
	(Being 1/3rd proceeds remitted to B)				
04.09.2020	B A/c	Dr.		63,000	
	To Bills Payable A/c				63,000
	(Being acceptance given to B on the failure of remittance of the amount due)				

04.09.2020	Bank A/c Dr.		11,100	
	Discount on Bills A/c Dr.		900	
	To B A/c			12,000
	(Being receipt of amount from B and discount amount credited to him)			
07.12.2020	Bills Payable A/c Dr.		63,000	
	To B A/c			63,000
	(Being acceptance to B dishonoured due to insolvency)			
07.12.2020	B A/c Dr.		42,000	
	To Bank A/c			16,800
	To Deficiency A/c			25,200
	(Being amount paid @40% & balance credited to deficiency account on failure of payment)			

Books of B

Date	Particulars	L.F.	Debit	Credit
01.06.2020	A's A/c Dr.		45,000	
	To Bills Payable A/c			45,000
	(Being the acceptance given for the bill)			
01.06.2020	Bank A/c Dr.		14,700	
	Discount on Bills A/c Dr.		300	
	To A's A/c			15,000
	(Being 1/3rd proceeds of the bill after discounting received from A)			
04.09.2020	Bills Receivable A/c Dr.		63,000	
	To A's A/c			63,000
	(Being acceptance received from A to cover the amount due from him)			
04.09.2020	Bank A/c Dr.		61,650	
	Discount on Bills A/c Dr.		1,350	
	To Bills Receivable A/c			63,000
	(Being bill discounted with bank)			
04.09.2020	Bills Payable A/c Dr.		45,000	
	To Bank A/c			45,000
	(Being own acceptance due on the date met)			
04.09.2020	A's A/c Dr.		12,000	
	To Bank A/c			11,100
	To Discount on Bills A/c			900
	(Being amount remitted to A after getting the bill discounted)			
07.12.2020	A's A/c Dr.		63,000	
	To Bank A/c			63,000
	(Being A's acceptance dishonoured on insolvency)			
07.12.2020	Bank A/c Dr.		16,800	
	Bad Debts A/c Dr.		25,200	
	To A A/c			42,000
	(Being the receipt of 40% of the amount due from A)			

TRADE BILL VS ACCOMODATION BILL

	Trade Bill	Accommodation Bill
1. Purpose	It is drawn and accepted for some consideration i.e. for trade purpose.	It is drawn and accepted without any consideration.
2. Need	It is drawn to settle a business transaction.	It is drawn to meet the financial requirements of the drawer / drawee / both temporarily.
3. Legal Status	The drawer can take legal action if the bill is dishonoured.	The drawer cannot take any legal action when the bill is dishonoured.
4. Discounting of bill	It may, or, may not be discounted with the bank.	It is always discounted with the bank.
5. Discounting charges	Discounting charges are borne by the drawer.	Divided between the drawer and drawee in the ratio of the proceeds.

Own Acceptance Received in form of B/R

(A)

B
To Sales

B/R
To B

C
To B/R

(B)

Purchases
To A

A
To B/P

B/R
To C

B/P
To B/R

(C)

B/R
To A

B
To B/R

AVERAGE DUE DATE

MEANING & USAGE

Meaning	Average Due Date is the date on which the net amount payable can be settled without causing loss of interest either to the borrower or the lender. In other words, it is the mean or equated date on which a single total payment may be made in lieu of different dates without any loss to either party.
Usage	It is used in various cases like: ❖ Cancellation of various bills of exchange due on different dates & issuance of single bill. ❖ Calculation of interest on drawings of partners. ❖ Amount lent in one installment and repayable in various installments.
Formula (Basic)	$ADD = \text{Base date} \pm \dfrac{\text{Total of Products}}{\text{Total of Amounts}}$

DUE DATE

Meaning	The due date of a bill of exchange/invoice is the date when the amount of a bill/invoice is payable by the drawee/ creditor to drawer/ debtor.
Cases	***Case 1*** : **Normal Sale/Purchase Credit Transaction (Invoice)** Due Date = Date of Invoice + Credit Period
	Case 2 : **Bill of Exchange (BOE)** Due Date = Date of Drawing bill/Date of Acceptance (If bill after sight) + Term (Usance) of Bill + 3 days of grace Where Term can be specified no. of days or months. In case Period/Term is in months then consider the corresponding day of that month & if corresponding day does not exist then take last day of the month.
Due Date if Holiday	✓ Public Holiday: Preceding Working Day (Eg: 26/1, 15/8, 2/10, Sunday) ✓ Emergency Holiday: Succeeding Working Day

Problem Type 1: Calculation of Average Due Date where one Party is Involved (Unilateral Transactions)

$$ADD = \underline{\text{Base date}} \pm \frac{\text{Total of Products}}{\text{Total of Amounts}}$$

$$ADD = \underline{\text{Base date}} \pm \frac{\text{Total of [Amount * No. of days from base date to due date]}}{\text{Total of Amounts}}$$

Points to be Noted:

- Base date may be the due date of first transaction or due date of the last transaction or any other due date but preferably earliest due date may be taken.
- While ascertaining the number of intervening days (plus or minus) between the base date and the due date of each transaction ignore the first date and include the last day.
- If amount is paid before due date, rebate/discount is given.
- If amount is paid after due date, then interest is charged.
- If no. of days to be added in base date comes in decimals then round off the same..
- If question specifies any particular date to be taken as base date then take that date as base date.

Question

A accepted the following bills drawn by B. Interest is charged @ 18% p.a.

Date of Bill	Period	Amount (Rs.)
07–03–2021	4 months	4,000
16–03–2021	3 months	5,000
08–04–2021	5 months	6,000
17–05–2021	3 months	5,000

11th September is a Gazetted holiday and 10th July is Emergency holiday

a) He wants to pay all the bills on a single day. Find out this date.
b) Find out the amount of Interest & Payment amount if settlement takes place on 30.09.2021
c) If A wants to save Rs. 157 by way of interest calculate the date on which he has to effect the payment.

Solution

Bills Receivable

Date of Bill	Term	Due date	Amount	No. of days from Base date (Base date 19th June)	Product
07–03–2021	4 months	11.07.2021	4,000	22	88,000
16–03–2021	3 months	19.06.2021	5,000	-	-
08–04–2021	5 months	10.09.2021	6,000	83	4,98,000
17–05–2021	3 months	20.08.2021	5,000	62	3,10,000
			20,000		**8,96,000**

Average due date $= \text{Base date} + \dfrac{\text{Total of Product}}{\text{Total of Amount}}$

$= 19/06/2021 + \dfrac{8,96,000}{20,000}$

$= 19/06/2021 + 45$ Days (44.8 days)

$= 03/08/2021$

b) On 30th September, 2021.

Interest $= 20,000 \times \dfrac{18}{100} \times \dfrac{58}{365} = 572.05$ r/off to 572

Total Amount $= 20,000 + 572$

$= 20,572$

c) Saving of Interest of Rs. 157 will happen by making payment early i.e before 03.08.2021

Let no. of days before 03.08.2021 = X days
Then

$$157 = 20{,}000 * \frac{18}{100} * \frac{X}{365}$$

X = 16 days
It means to save interest of 157, payment to be made 16 days before 03.08.2021 i.e on 18.07.2021.

Problem Type 2 : Calculation of Average Due Date where transactions between 2 parties are Involved (Bilateral Transactions)

When more than one party is involved i.e. where one party purchases and also sells to other party then in such a case instead of paying gross amount they may go for new amount i.e. Purchase amount and sales amount will be set off and thus we will take difference of amount and produce as Net Amount.

$$\text{ADD} = \text{Base date} \pm \frac{\text{Difference of Products}}{\text{Difference of Amounts}}$$

Base date may be considered as earliest dates of both tables

Question

Two traders Abhinav and Krishna buy goods from one another, each allowing the other one month's credit. At the end of 3 months, the accounts rendered are as follows:

Goods sold by Abhinav to Krishna		Goods sold by Krishna to Abhinav	
Date	**Amount (Rs.)**	**Date**	**Amount (Rs.)**
18th April	9,000	23rd April	7,800
15th May	10,500	24th May	7,500
16th June	12,000		

Compute date upon which balance should be paid, so that no interest is due either to Abhinav or Krishna.

Solution

Amount receivable by Abhinav (Sales by Abhinav)

Date of Transaction	Credit period (months)	Due date	Amount	No. of days from Base date (Base date 18th May)	Product
18/4	1 month	18/5	9,000	-	-
15/5	1 month	15/6	10,500	28	2,94,000
16/6	1 month	16/7	12,000	59	7,08,000
			31,500		**10,02,000**

Amount payable by Abhinav (Purchases by Abhinav)

Date of Transaction	Credit period (months)	Due date	Amount	No. of days from Base date (Base date 18th May)	Product
23/4	1 month	23/5	7,800	5	39,000
24/5	1 month	24/6	7,500	37	2,77,500
			15,300		**3,16,500**

$$\text{Average due date} = \text{Base date} + \frac{\text{Difference of Products}}{\text{Difference of Amounts}}$$

$= 18^{th}$ May + $\frac{10,02,000 - 3,16,500}{31,500 - 15,300}$

$= 18^{th}$ May + $\frac{6,85,500}{16,200}$

$= 18^{th}$ May + 42 days

$= 29^{th}$ June

On 29th June, Krishna has to pay Abhinav Rs. 16,200 to settle the account.

Problem Type 3: Calculation of Average Due Date for determining interest on drawings

When interest is chargeable on drawings, and drawings are on different dates, interest may be calculated on the basis of Average Due Date of drawings.

In that case rather than calculating interest on each drawing separately, interest can be calculated on total drawings from average due date till the end of period.

ADD= Base date ± $\frac{\text{Total of Products}}{\text{Total of Amounts}}$

Question

Mr. Yash and Mr. Harsh are partners in a firm. They had drawn the following amounts from the firm during the year ended 31.03.2021:

Date	Amount (Rs.)	Drawn by
01.05.2020	75,000	Mr. Yash
02.07.2020	20,000	Mr. Yash
15.08.2020	60,000	Mr. Harsh
31.12.2020	50,000	Mr. Harsh
04.03.2021	75,000	Mr. Harsh
31.03.2021	15,000	Mr. Yash

Interest is charged @ 10% p.a. on all drawings. Calculate interest chargeable from each partner by using Average due date system. (Consider 1st May as base date)

Solution

a) Mr. Yash

Dates	Amount	No. of days from Base date (Base date 01.05.2020)	Product
01.05.2020	75,000	0	0
02.07.2020	20,000	62	12,40,000
31.03.2021	15,000	334	50,10,000
	1,10,000		**62,50,000**

Average due date $=$ Base date + $\frac{\text{Total of Product}}{\text{Total of Amount}}$

$= 01.05.2020 + \frac{62,50,000}{1,10,000}$

$= 01.05.2020 + 57$ Days

$= 27.06.2020$

Thus, interest is chargeable for Yash from 27th June to March 31 i.e. 277 days

Interest = $1,10,000 \times \frac{10}{100} \times \frac{277}{365} = 8,348$

b) Mr. Harsh

Dates	Amount	No. of days from Base date (Base date 01.05.2020)	Product
15.08.2020	60,000	106	63,60,000
31.12.2020	50,000	244	1,22,00,000
04.03.2021	75,000	307	2,30,25,000
	1,85,000		**4,15,85,000**

Average due date $= \text{Base date} + \dfrac{\text{Total of Product}}{\text{Total of Amount}}$

$= 01.05.2020 + \dfrac{4,15,85,000}{1,85,000}$

= 01.05.2020 + 225 Days

= 12.12.2020

Thus, interest is chargeable for Yash from 12th December to March 31 i.e. 109 days

Interest = $1,85,000 \times \dfrac{10}{100} \times \dfrac{109}{365} = 5,525$

Problem Type 4: Calculation of Average Due Date when amount is paid in installments

Avg. due date = Date of Loan + $\dfrac{\text{Sum of days/months/Years from the date of lending to date of repayment of each installment}}{\text{Number of installments}}$

This formula is applicable only when repayment installment is equal else normal formula will be applied.

Question

Rs. 10,000 lent by Damini to Yamini on 1st January, 2020 is

Case 1: Repayable in 5 equal annual instalments commencing on 1st January, 2021.

Case 2: Repayable in 5 half yearly equal installments commencing from 1st January, 2021

Find the average due date and calculate interest at 5% p.a., which Damini will recover from Yamini.

Solution

Average due date

= Date of Loan + $\dfrac{\text{Sum of years from date of lending to date of repayment of each installment}}{\text{No. of installments}}$

Case 1:

$= 1/1/2020 + \dfrac{1+2+3+4+5}{5}$

= 1/1/2020 + 3 years

= 1/1/2023

Interest to be paid by Yamini = Amount X Rate X 3 years

$= 10,000 \times \dfrac{5}{100} \times 3 = 1,500$

Case 2:

$= 1/1/2020 + \dfrac{1+1.5+2+2.5+3}{5}$

= 1/1/2020 + 2 years

= 1/1/2022

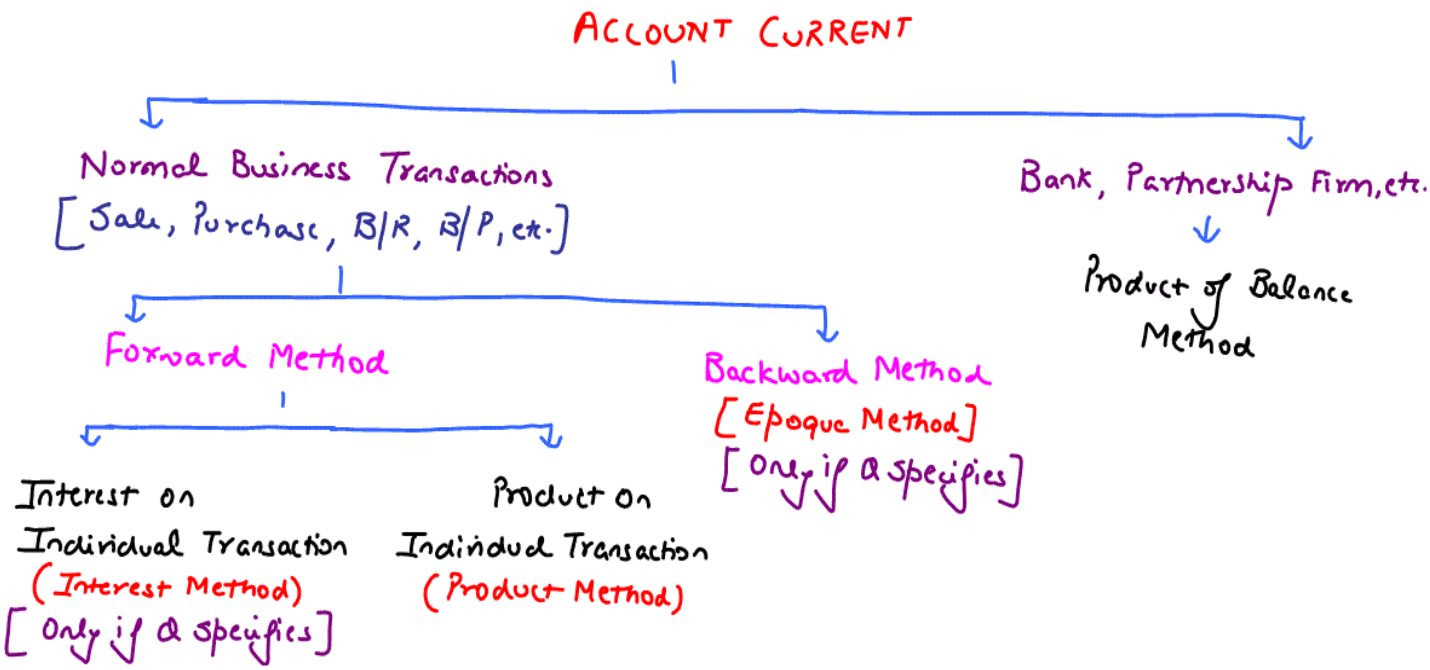
Interest to be paid by Yamini = Amount X Rate X 2 years

$= 10,000 \times \dfrac{5}{100} \times 2 = 1,000$

ACCOUNT CURRENT

MEANING & USAGE

Meaning	An Account Current is a running statement of transactions between parties for a given period of time and includes interest allowed or charged on various items. It takes the form of a ledger account. It is prepared uptoparticular date.
Usage	Some of the situations when the account current is prepared:- ❖ It is prepared when frequent transactions regularly take place between 2 parties. *<u>For Example</u>*: A trader who sells goods frequently to a merchant on credit and receives payments from him in installments at different intervals and charges interest on the amount which remains outstanding. ❖ It is also frequently prepared to set out the transactions taking place between a banker & his customer.
No. of Parties	❖ An Account Current has 2 parties : one who renders the account & : other to whom the account is rendered. This is indicated in heading of an Account Current, which is like the following:“B in Account Current with A”. It implies that B is customer, and the account is being rendered to him by A.
Methods	❖ Interest on Individual Transaction Method (Forward Method) ❖ Product of Individual Transaction / Product Method (Forward Method) ❖ Backward/Epoque Method ❖ Products of Balances Method



Problem Type 1: Preparation of Account Current with the help of Forward Method

Interest on Individual Transaction Method:
Under this method, all the transactions are arranged in the form of an account.

Steps:

- Count days from due date of transaction to the date of closing the account.
  For Balance b/d (Opening Balance) – include the date of such balance as well.
  For Transaction – Don't include the date of transaction.
  Note: If no specific date is mentioned as the date on which payment is due, the date of transaction is presumed to be due date.
- Calculate Interest for each transaction = Amount * Interest (%) * Days / 365
- Check Interest column & write 'To Balance of Interest' or 'By Balance of Interest' in the interest column
- Write such amount on *opposite side* with words 'To Interest' or 'By Interest' in main Amount Column.
- Now check the main amount column & write 'By Balance c/d' or 'To Balance c/d'

Product of Individual Transaction Method:
Steps:

- Count days from due date of transaction to the date of closing the account.
  For Balance b/d (Opening Balance) – include the date of such balance as well.
  For Transaction – Don't include the date of transaction.
  Note: If no specific date is mentioned as the date on which payment is due, the date of transaction is presumed to be due date.
- Check Product column & write 'To Balance of Product' or 'By Balance of Product' in the Product column
- Find out the interest on such balance of Products as
  [Balance of Product * Interest (%) * 1/ 365] &
  write such amount on *opposite side* with words 'To Interest' or 'By Interest' in main Amount Column.
- Now check the main amount column & write 'By Balance c/d' or 'To Balance c/d'

Red - Ink Interest:
In case the due date of a bill falls after the date of closing the account, then no interest is allowed for that. However, interest from the date of closing to such due date is written in "Red-Ink" in the appropriate side of the 'Account current'. This interest is called Red-Ink interest. This Red Ink interest is treated as negative interest.

Question 1
Draw up an Account Current by means of Interest on Individual Transaction Method & Product Method up to 31st December, 2021 to be rendered by X to Y. Consider interest @ 8% p.a.

Date (2021)	Particulars	Amount (Rs.)
July 1	Balance owing by Y	600
July 15	Goods sold to Y	900
Aug 21	Goods bought from Y	700
Aug 23	Cash received from Y	450
Oct 23	Y accepted X's bill at 3 months	300
Nov 01	Goods bought from Y	950
Dec 03	Accepted a bill drawn by Y at 3 months (due date of bill is on Sunday)	400

On 31st December,2021 X and Y settled their account after considering the interest factor. Show the cash amount received or paid by X on that date.

Question 2

Following transactions took place between L and M during the month of April, 2020:

Date	Particulars	Amount (Rs.)
1.4.2020	Amount payable by L to M	5,000
7.4.2020	Received acceptance of L to M for 2 months	2,500
10.4.2020	Bills receivable (accepted by M) on 7.2.2020 is honoured on this due date	5,000
10.4.2020	L sold goods to M (invoice dated 10.5.2020)	7,500
12.4.2020	L received cheque from M dated 15.5.2020	3,750
15.4.2020	M sold goods to L (invoice dated 15.5.2020)	3,000
20.4.2020	L returned goods sold by M on 15.4.2020	500
20.4.2020	Bill accepted by M is dishonoured on this due date	2,500

Prepare M's account in the books of L for the month of April, 2020, taking interest into account @ 10% p.a. (Consider 1 Year = 365 days)

Problem Type 2: Preparation of Account Current with help of Backward/ Epoque Method

<u>Steps:</u>

- Count days from opening date of statement to due date of transaction
  For Balance b/d (Opening Balance) – the day is '0'
  For Transaction – Include date of start as well as due date of transaction.
- On Last day. Find in rough the balance in amount column & multiply by the no. of days from opening of statement till closing of statement.
- Check Product column & write 'To Balance of Product' or 'By Balance of Product' in it
- Find out the interest on such balance of Products as
  [Balance of Product * Interest (%) * 1/ 365]
  & write such amount on <u>*same*</u> side with words 'To Interest' or 'By Interest' in the main Amount Column.
- Now check the main amount column & write 'By Balance c/d' or 'To Balance c/d'

Question

From the following transactions, draw up an Account Current by means of Backward Method up to 31st December, 2021 to be rendered by X to Y & amount of interest charging @ 8% p.a.

Date (2021)	Particulars	Amount (Rs.)
July 1	Balance owing by Y	600
July 15	Goods sold to Y	900
Aug 21	Goods bought from Y	700
Aug 23	Cash received from Y	450
Oct 23	Y accepted X's bill at 3 months	300
Nov 01	Goods bought from Y	950
Dec 03	Accepted a bill drawn by Y at 3 months (due date of bill is on Sunday)	400

On 31st December, 2021, X and Y settled their account after considering the interest factor. Show the cash amount received or paid by X on that date.

Problem Type 3: Preparation of Account Current with help of Product of Balance Method

This method, also known as periodic balance method, is usually adopted in the case of banks where the balance of account is taken out after every transaction.

Steps:

- In this case, the number of days written against each transaction are the days counted from its date or due date to the date of the following transaction. In the case of the last transaction, the number of days is counted to the close of the period.
- Each amount is multiplied with the number of days. If the amount represents a debit balance, the product is entered in the Dr. Product column; and if it represents a credit balance, the product is written in the Cr. Product column.
- The Dr. Product and Cr. Product columns are then totalled up.
- Interest is calculated on each total at the given rate of interest; and the net interest is ascertained.
- If net interest is payable to the customer, it will appear as "By Interest A/c", and if it is due from the customer, it will appear as "To Interest A/c".

Question

Ramesh has a Current Account with Partnership firm. He had a debit balance of Rs. 85,000 as on 01-07-2021. He has further deposited the following amounts:

Date	Amount (Rs.)
14-07-2021	1,23,000
18-08-2021	21,000
He withdrew the following amounts:	
Date	**Amount (Rs.)**
29-07-2021	92,000
09-09-2021	11,500

Show Ramesh's A/c in the books of the firm. Interest is to be calculated at 10% on debit balance and 8% on credit balance. You are required to prepare current account as on 30^{th} September, 2021 by means of product of balances method.

ACCOUNT CURRENT

Type 1: Preparation of Account Current with the help of Forward Method

Solution 1a

Books of Mr. X
Y in Account Current with X

Date	Particulars	Due date	Days	Amount	Interest	Date	Particulars	Due date	Days	Amount	Interest
2021		2021				2021		2021			
1/7	To Balance b/d	1/7	184	600	24.20	21/8	By Purchases A/c	21/8	132	700	20.25
15/7	To Sales A/c	15/7	169	900	33.33	23/8	By Cash A/c	23/8	130	450	12.82
3/12	To B/P A/c	5/3	(64)	400	(5.61)	23/10	By B/R A/c	25/1	(25)	300	(1.64)
31/12	To Interest A/c	-	-	8	-	1/11	By Purchases A/c	1/11	60	950	12.49
31/12	To Cash A/c	-	-	492	-	31/12	By Bal. of Interest	-	-	-	8.00
				2,400	**51.92**					**2,400**	**51.92**

Solution 1b

Books of Mr. X
Y in Account Current with X

Date	Particulars	Due date	Days	Amount	Product	Date	Particulars	Due date	Days	Amount	Product
2021		2021				2021		2021			
1/7	To Balance b/d	1/7	184	600	1,10,400	21/8	By Purchases A/c	21/8	132	700	92,400
15/7	To Sales A/c	15/7	169	900	1,52,100	23/8	By Cash A/c	23/8	130	450	58,500
3/12	To B/P A/c	5/3	(64)	400	(25,600)	23/10	By B/R A/c	25/1	(25)	300	(7,500)
31/12	To Interest A/c*	-	-	8	-	1/11	By Purchases A/c	1/11	60	950	57,000
31/12	To Cash A/c	-	-	492	-	31/12	By Bal. of Products	-	-	-	36,500
				2,400	**2,36,900**					**2,400**	**2,36,900**

$$\text{* Interest} = \left[36{,}500 \times \frac{8}{100} \times \frac{1}{365}\right] = 8$$

Solution 2

Books of L
M in Account Current with L

Date	Particulars	Due date	Days	Amount	Product	Date	Particulars	Due date	Days	Amount	Product
2020		2020				2020		2020			
7/4	To B/P A/c	10/6	(41)	2,500	(1,02,500)	1/4	By Balance b/d	¼	30	5,000	1,50,000
10/4	To Sales A/c	10/5	(10)	7,500	(75,000)	12/4	By Bank A/c	15/5	(15)	3,750	(56,250)
20/4	To Purchase return A/c	15/5	(15)	500	(7,500)	15/4	By Purchases A/c	15/5	(15)	3,000	(45,000)
20/4	To B/R A/c	20/4	10	2,500	25,000	30/4	By Interest A/c	-	-	57.19	-
30/4	To Bal. of Products	-	-	-	2,08,750	30/4	By Balance c/d	-	-	1,192.81	
				13,000	**48,750**					**13,000**	**48,750**

* Interest = $\left[2{,}08{,}750 \times \frac{10}{100} \times \frac{1}{365}\right] = 57.19$

Note: No entry is required for bill matured on 10th April since party is not contracted.

Type 2: Preparation of Account Current with the help of Backward/Epoque Method

Solution

Books of Mr. X
Y in Account Current with X

Date	Particulars	Due date	Days	Amount	Product	Date	Particulars	Due date	Days	Amount	Product
2021		2021				2021		2021			
1/7	To Balance b/d	1/7	0	600	0	21/8	By Purchases A/c	21/8	52	700	36,400
15/7	To Sales A/c	15/7	15	900	13,500	23/8	By Cash A/c	23/8	54	450	24,300
3/12	To B/P A/c	5/3	248	400	99,200	23/10	By B/R A/c	25/1	209	300	62,700
31/12	To Balance (500*184)	-	184	-	92,000	1/11	By Purchases A/c	1/11	124	950	1,17,800
31/12	To Bal of Product	-		-	36,500						
31/12	To Interest A/c*	-	-	8	-						
31/12	To Cash A/c	-	-	492	-						
				2,400	**2,41,200**					**2,400**	**2,41,200**

$$* \text{ Interest} = \left[36{,}500 \times \frac{8}{100} \times \frac{1}{365}\right] = 8$$

Type 3: Preparation of Account Current with help of Product of Balance Method

Solution

Ramesh Current A/c with Partnership firm

Date	Particulars	Dr.	Cr.	Dr./ Cr.	Balance	Days	Dr. Product	Cr. Product
1st July	To Balance b/d	85,000	-	Dr.	85,000	14	11,90,000	-
14th July	By Cash	-	1,23,000	Cr.	38,000	15	-	5,70,000
29th July	To Cash	92,000	-	Dr.	54,000	20	10,80,000	-
18th Aug	By Cash	-	21,000	Dr.	33,000	22	7,26,000	-
9th Sep	To Cash	11,500	-	Dr.	44,500	21	9,34,500	-
30th Sep	To Interest	952	-	Dr.	45,452	-	-	-
30th Sep	By Bal. c/d	-	45,452	-				
		1,89,452	**1,89,452**				**39,30,500**	**5,70,000**

Calculation of Interest

Int. on Dr. Product = 39,30,500 × 10% × 1/365 = 1076.85

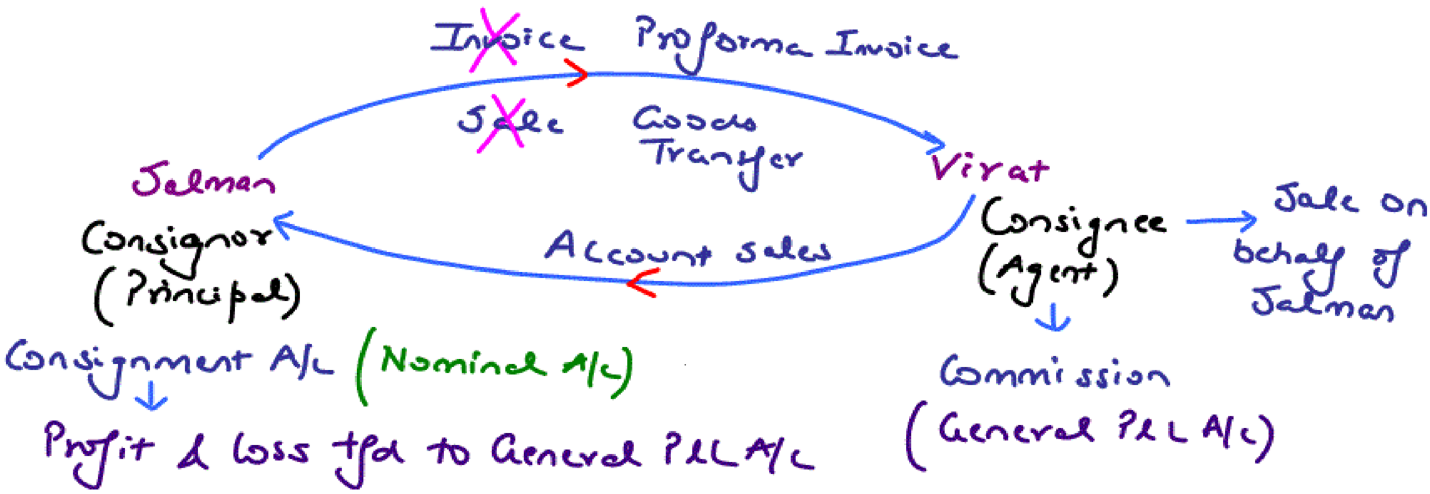
Int. on Cr. Product = 5,70,000 × 8% × 1/365 = (124.93)

Int. to be Dr. = 951.92 or 952

CONSIGNMENT

BASICS & FEATURES

Meaning	To consign means **"to send"**. *In Accounting*, ***<u>Consignment</u>*** refers to a situation where a person (called Consignor) sends good to another person (called Consignee), for the purpose of selling the goods on behalf of, and at the risk of the Consignor.
Parties	The two parties involved in a Consignment transaction are- **a) Consignor:** The person sending the goods also called as **Principal.** **b) Consignee:** The person to whom goods are sent also called as **Agent**



CONSIGNMENT AND SALE

BASIS	CONSIGNMENT	SALE
Parties	Consignor and Consignee	Seller and Buyer
Ownership of goods	Ownership remains with Consignor till goods are sold. There is no transfer of ownership to the Consignee	Ownership will be transferred to the Buyer immediately upon sale.
Risk	Risk of loss or damage of goods lies with the Consignor only	Risk of loss or damage of goods lies with buyer once the goods are sold.
Return of Goods	Consignee can return the unsold goods to the Consignor	Generally, buyer cannot return goods once it is sold to him.
Relationship b/w Parties	Principal-Agent relationship. Consignor= Principal Consignee- Agent	Creditor-Debtor relationship. Seller=Creditor(in Buyer's Books) Buyer= Debtor (in Seller's Books).
Expenses	Expenses done by consignee to receive goods & to keep it safely are borne by consignor unless there is any other agreement.	Expenses incurred by the buyer are to be borne by the buyer itself after the transfer of goods
Invoice	Proforma Invoice is prepared	Sale Invoice is prepared

JOURNAL ENTRIES IN THE BOOKS OF THE CONSIGNOR

	Transaction	Journal Entry
1.	Goods sent on Consignment	Consignment Account Dr. To Goods sent on Consignment A/c
2.	Expenses incurred by consignor, for goods sent on Consignment ("e.g. Transportation, Insurance, etc)	Consignment Account Dr. To Cash/Bank A/c
3.	Advance given by Consignee, by way of cash/cheque/bill of Exchange	Cash/ Bank/Bills Receivable A/c Dr. To Consignee Account
4.	Bills Receivable given by Consignee, discounted with bank	Bank Account Dr. Discount Account * Dr. To Bills Receivable Account * These charges can be transferred to Consignment A/c or P&L A/c.
5.	Expenses incurred by the Consignee on behalf of the Consignor (e.g. Unloading, Advertisement)	Consignment Account Dr. To Consignee Account
6.	Goods sold by the Consignee (as per Account Sales received from him)	Consignee Account Dr. To Consignment Account
7.	Commission on Sales due to Consignee	Consignment Account Dr. To Consignee Account
8.	Bad Debts as per Account Sales reported by Consignee (***Note***: Entry not applicable if the Consignee himself bears risk of Bad Debts, i.e. when Del Credere Commission is paid)	Consignment Account To Consignee Account
9.	Goods received back from the Consignee	Goods sent on Consignment A/c Dr. To Consignment Account
10.	Closing stock lying with the Consignee	Consignment Stock Account Dr. To Consignment Account
11.	Remittance received from Consignee along with Account sales	Cash/Bank/Bills Receivable A/c To Consignee Account
12.	Goods sent on Consignment A/c- balance transferred to Trading Account	Goods sent on Consignment A/c To Trading Account

Ledger Accounts

Dr. CONSIGNMENT ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Goods sent on consignment A/c To Bank A/c (Expenses of Consignor) To Consignee A/c (Expenses of Consignee) To Consignee A/c (Commission) To Consignee A/c (Bad Debts) To Profit & Loss Account (Profit) (Balancing Figure)		By Goods sent on Consignment (Return) By Consignee A/c (Sale Proceeds) By Consignment Stock Account By Profit & Loss Account (Loss) (Balancing Figure)	
Total		**Total**	

Dr.	CONSIGNEE ACCOUNT		Cr.
Particulars	**₹**	**Particulars**	**₹**
To Consignment A/c (Sales)		By Cash/Bank/B/R Acc (Advance) By Consignment A/c (Expenses) By Consignment A/c (Commission) By Consignment A/c (Bad Debts) By Cash/Bank/B/R A/c (Bal. Fig.)	
Total		**Total**	

VARIOUS TYPES OF COMMISSION

There are 3 types of Commission paid by the Consignor to the Consignee for the services rendered-

Ordinary Commission or Normal Commission	➢ It is computed at fixed percentage of **Gross Sales Proceeds** made by Consignee ➢ No distinction between Cash Sale & Credit Sale for computing Commission. ➢ The Normal Commission constitutes the remuneration of the Consignee, for the agency services rendered by him. ➢ In this case, the **Consignor** bears the risk of Bad Debts
Del Credere Commission	➢ When Del-Credere Commission is paid, **Consignee** bears the risk of Bad Debts. ➢ Del-Credere Commission is calculated on **Total Sales,** unless there is any agreement between the parties, to calculate it on Credit Sales only.
Over-riding Commission	➢ It is an extra commission paid by the Consignor- ▪ to promote sales at a higher price than specified, or ▪ to encourage Consignee to put in extra efforts in introducing the new product in the market. ➢ Depending on the Agreement, such commission will be calculated on Total Sales or on the difference between Actual Sales and Sales at Invoice Price.

VALUATION OF CLOSING STOCK LYING WITH CONSIGNEE

(a) **Principle**: Stock should be valued at Cost or Net Realizable Value, whichever is lower.

(b) **Determination of Cost**: All items of Cost incurred till the goods reach the premises of the Consignee must be taken into account.

Cost

Goods sent on Consignment + Consignor Expenses (All) + Consignee Non Recurring Expenses

Consignee Non Recurring Expenses:
- Freight / Carriage
- Octroi
- Clearing charges
- Transit Insurance
- Unloading

Recurring / Indirect Expenses: Rent, Insurance, Advertisement, etc.

(a) **Indirect Expenses** Incurred by Consignor e.g. Discount on B/R, other expenses not related to sending the goods etc. should not be considered in stock valuation.
(b) Expenses incurred **after** the goods have reached the Consignee's Godown should **not** be taken into account for stock valuation
(c) Commission Due to Consignee and Bad Debts, should **not** be included for Stock Valuation.
(d) If the question is silent, all Expenses incurred by Consignor will be included for stock Valuation, and all Expenses incurred by the Consignee will be excluded

Question 1

Mr. A of Assam sent on 18th February, 2021 a consignment of 1000 DVD players to B of Bengal costing of Rs.100 each. Expenses of Rs.1,500 were met by the consignor. B spent Rs.3,000, for clearance and selling expenses were Rs.20 per DVD player.

B sold on 15th March, 2021, 600 DVD Players @ Rs.160 per DVD Player and again on 20th May, 2021, 300 DVD Players @Rs.170.

B is entitled to a commission of Rs.25 per DVD Player sold plus ¼ of the amount by which the gross sale proceeds less total commission thereon exceeded a sum calculated@ Rs.125 per DVD Player sold. B sent the amount due to A on 30th June, 2021.

You are requested to show the consignment account and B's account in the books of A.

Solution

CONSIGNMENT ACCOUNT

Particulars	Amount	Particulars	Amount
To Goods Sent on Consignment A/c (1,000*100)	1,00,000	By B's A/c (Sales) [(600*160)+(300*170)]	1,47,000
To Bank A/c (Expenses)	1,500	By Consignment Stock A/c	10,450
To B's A/c Clearance charges 3,000 Selling Exp.(900*20) 18,000	21,000		
To B's A/c (Commission)	24,900		
To P&L A/c (Profit) – Bal. Fig.	10,050		
	1,57,450		**1,57,450**

B's ACCOUNT

Particulars	Amount	Particulars	Amount
To Consignment A/c (Sales)	1,47,000	By Consignment A/c (Expenses)	21,000
		By Consignment A/c (Commission)	24,900
		By Bank A/c (Bal. Fig.)	1,01,100
	1,47,000		**1,47,000**

W.N.-1 Commission

Let total commission be X

X = (900*25) + ¼[1,47,000-X-(900*125)]

X = 22,500 + ¼ (1,47,000-X-1,12,500)

X = 22,500 + ¼ (34,500-X)   X = 22,500 + 8,625- 1/4X

5/4 X = 31,125   X = 31,125*4/5 = 24,900

W.N.-2 Closing Stock

Particulars	Units	Amount
Goods sent on Consignment	1000	1,00,000
Consignor Expenses	-	1,500
Consignee non recurring expenses	-	3,000
	1,000	**1,04,500**

Units Left unsold = 1000 – 900 = 100

Value of Closing Stock = 1,04,500/1000 * 100 = 10,450

GOODS CONSIGNED AT ABOVE COST

1) **Goods invoiced above cost:** If the Consignor does not want to reveal real cost of goods consigned to the consignee, he may prepare the Proforma Invoice at a value **higher** than the Cost thereof.
2) **Accounting:** If goods are invoiced above cost-
   a) the goods consigned, i.e., ''Goods Sent on Consignment'', and
   b) Closing stock, will be recorded at Invoice Price in Consignment A/c.
3) **Removal of Loading:** The Loading on goods consigned, and on closing stock will be **reversed** at the end of the financial period.
   Loading = Difference between Invoice Price and Cost (i.e., Profit Element added to arrive at the Invoice Price).

Consignment A/c

To Goods sent on Consignment (Invoice Price)		By Goods sent on Consignment (Loading)	
To Stock Reserve (Loading)		By Consignment stock (Invoice Price)	

Various Cases

Case 1: Cost Rs. 60,000. Profit 20% on Cost.

Case 2: Cost Rs. 60,000. Profit 20% on Invoice Price.

Case 3: Invoice Price Rs. 60,000. Profit 20% on Cost.

Case 4: Invoice Price Rs. 60,000. Profit 20% on Invoice Price.

Question 2

M/s Ram & Co., of Delhi purchased 20,000 pieces of sarees @ Rs. 200 per saree. Out of these, 12,000 sarees were sent on consignment to M/s Laxman Traders of Bombay at the selling price of Rs. 240 per saree. The consignors paid Rs. 6,000 for packing and freight.

M/s Laxman Traders sold 10,000 sarees @ Rs. 250 per saree and incurred Rs. 2,000 towards selling expenses and remitted Rs. 10,00,000 to Delhi on account. M/s Laxman Traders are entitled to a commission of 5 percent on total sales plus a further 20 percent commission on any surplus price realised over Rs. 240 per saree.

6,000 sarees were sold at Rs.220 per saree by the consignor and selling expenses incurred 5,000. Owing to fall in the market price, the value of stock of sarees in hand is to be reduced by 10 percent.

Prepare the consignment account, Trading and P&L Acc and M/s Laxman Traders Account in the books of the Ram & Co.

Solution

Trading and P&L ACCOUNT

Particulars	Amount	Particulars	Amount
To Purchases A/c (20,000*200)	40,00,000	By Sales A/c (6,000 * 220)	13,20,000
To Gross Profit (Bal. Fig.)	80,000	By Goods sent on Consignment A/c (12,000 * 200)	24,00,000
		By Closing Stock (2,000*200)-10%	3,60,000
	40,80,000		**40,80,000**
To Selling Expenses	5,000	By Gross Profit	80,000
To Net Profit (Bal. Fig.)	3,82,900	By Consignment A/c (Profit)	3,07,900
	3,87,900		**3,87,900**

CONSIGNMENT ACCOUNT

Particulars	Amount	Particulars	Amount
To Goods Sent on Consignment A/c (12,000*240)	28,80,000	By Goods Sent on Consignment A/c (Loading: 12,000*40)	4,80,000
To Bank A/c (Packing & Freight)	6,000	By Laxman Traders A/c (Sales) (10,000*250)	25,00,000
To Laxman Traders A/c (Expenses)	2,000	By Consignment Stock A/c	4,32,900
To Laxman Traders A/c (Commission)	1,45,000		
To Stock Reserve (Loading in Closing Stock) [4,80,000*2,000/12,000] – 10%	72,000		
To P&L A/c (Profit) – Bal. Fig.	3,07,900		
	34,12,900		**34,12,900**

LAXMAN TRADERS ACCOUNT

Particulars	Amount	Particulars	Amount
To Consignment A/c (Sales)	25,00,000	By Bank A/c	10,00,000
		By Consignment A/c (Expenses)	2,000
		By Consignment A/c (Commission)	1,45,000
		By Bank A/c (Bal. Fig.)	13,53,000
	25,00,000		**25,00,000**

W.N.-1 Commission = [25,00,000*5%] + [10,000*(250-240)*20%]
= 1,25,000+20,000 = 1,45,000

W.N.-2 Closing Stock

Particulars	Units	Amount (Invoice Price)
Goods sent on Consignment	12,000	28,80,000
Consignor Expenses	-	6,000
Consignee non recurring expenses	-	Nil
	12,000	**28,86,000**

Units Left unsold = 12000 – 10000 = 2000

Value of Closing Stock = 28,86,000/12000 * 2000 = 4,81,000

Less Decline @ 10% = (48,100)

Value = 4,32,900

NORMAL LOSS AND ABNORMAL LOSS

The words ''Normal Loss'' and ''Abnormal Loss'' refer basically to the **quantity of goods lost.**

Basis	**Normal Loss**	**Abnormal Loss**
Meaning	Loss that is expected/ unavoidable is called Normal Loss	Loss due to accident/unforeseen cause or avoidable, is called Abnormal loss
Example	While consigning liquids like oils, petrol, etc. any loss in quantity due to spilling or evaporation`	If the entire or a huge quantity of oil/petrol is lost due to lorry accident/ fire, etc.
Insurance claim	No recovery is possible from Insurance Company	Insurance Company may reimburse a suitable amount
Accounting Treatment	Total Cost Plus Expenses should be divided by the quantity available after Normal Loss	Abnormal loss should be valued in the same manner as Closing Stock, and credited to Consignment Account.
Journal Entry	There is no Journal Entry as such for Normal loss. It is adjusted by way of quantity deduction only. so Average cost per unit- $\dfrac{\text{Total Cost incurred}}{\text{Total Quantity} - \text{Normal Loss}}$	For recording Abnormal loss: Abnormal loss A/c Dr. To Consignment A/c

Table showing Computation of Loss & Closing Stock

TABLE

Particulars	Units	Amount
Goods sent on Consignment	✓	✓
+ Consignor Expenses	X	✓
	✓	✓
- Normal loss	(✓)	(X)
OR		
- Abnormal loss	(✓)	(✓)
	✓	✓
+ Consignee Non Recurring Exp.	X	✓
	✓	✓

Note:

It is important to value goods lost in transit & goods lost in consignee's godown. Both are abnormal loss & valuation will be as follows:

- If goods lost in Transit: Consignee's non recurring expenses are not to be included.
- If goods lost in Consignee's godown: Consignee's non recurring expenses are to be included.

Question 3

1,000 bicycles were consigned by X of Delhi to Y of Kanpur at Rs. 150 each. X paid freight Rs. 10,000 and insurance in transit Rs. 1,500. During transit 100 bicycles were totally damaged by fire. Y took delivery of the remaining bicycles and paid Rs. 1,530 for octroi.

Y sent a bank draft to X for Rs. 50,000 as advance payment and later sent an Account Sales showing that 800 bicycles were sold at Rs. 220 each. Expenses incurred by Y on godown rent and advertisement, etc. amounted to Rs. 2,000. Y is entitled to commission of 5%.

Prepare Consignment Account, Abnormal Loss Account & Y's Account in books of X assuming that a claim from insurance company was settled for Rs. 14,000.

Solution

BOOKS OF X

CONSIGNMENT ACCOUNT

Particulars	Amount	Particulars	Amount
To Goods Sent on Consignment A/c (1,000*150)	1,50,000	By Abnormal Loss	16,150
To Bank A/c Freight 10,000 Insurance in Transit 1,500	11,500	By Y's A/c (Sales) (800*220)	1,76,000
To Y's A/c Octroi 1,530 Godown Rent & Adv. 2,000	3,530	By Consignment Stock A/c	16,320
To Y's A/c (Commission) (1,76,000*5%)	8,800		
To P&L A/c (Profit) – Bal. Fig.	34,640		
	2,08,470		**2,08,470**

Y's ACCOUNT

Particulars	Amount	Particulars	Amount
To Consignment A/c (Sales)	1,76,000	By Bank A/c (Advance)	50,000
		By Consignment A/c (Expenses)	3,530
		By Consignment A/c (Commission)	8,800
		By Bank A/c (Bal. Fig.)	1,13,670
	1,76,000		**1,76,000**

ABNORMAL LOSS ACCOUNT

Particulars	Amount	Particulars	Amount
To Consignment A/c	16,150	By Bank A/c (Insurance Claim)	14,000
		By P&L A/c (Loss transferred)	2,150
	16,150		**16,150**

W.N.- Abnormal Loss and Closing Stock

Particulars	Units	Amount
Goods sent on Consignment	1,000	1,50,000
Consignor Expenses	-	11,500
	1,000	**1,61,500**
Less: Abnormal Loss	(100)	(16,150)
	900	1,45,350
Consignee non recurring expenses	-	1,530
	900	**1,46,880**

Units Left unsold = 900 – 800 = 100

Value of Closing Stock = 1,46,880/900 * 100 = 16,320

Question 4

Shri Ganpath of Nagpur consigns 500 cases of goods costing Rs. 1,500 each to Rawat of Jaipur. Shri Ganpath pays the following expenses in connection with the consignment:

Particulars	Amount
Carriage	15,000
Freight	45,000
Loading Charges	15,000

Shri Rawat sells 350 cases at Rs. 2,100 per case and incurs the following expenses

Clearing charges	18,000
Warehousing and Storage charges	25,000
Packing and selling expenses	7,000

It is found that 50 cases were lost in transit and another 50 cases were in transit. Shri Rawat is entitled to a commission of 10% on gross sales. Draw up the Consignment Account and Rawat's Account in the books of Shri Ganpath

Solution

BOOKS OF GANPATH
CONSIGNMENT ACCOUNT

Particulars	Amount	Particulars	Amount
To Goods Sent on Consignment A/c (1,500*500)	7,50,000	By Abnormal Loss*	82,500
To Bank A/c Carriage 15,000 Freight 45,000 Loading Charges 15,000	75,000	By Rawat's A/c (Sales) (350*2,100)	7,35,000
To Rawat's A/c Clearing Charges 18,000 Warehousing & Storage 25,000 Packing & Selling Exp. 7,000	50,000	By Consignment Stock A/c - In Transit - In Hand	 82,500 84,750
To Rawat's A/c (Commission) (7,35,000*10%)	73,500		
To P&L A/c (Profit) – Bal. Fig.	36,250		
	9,84,750		**9,84,750**

*Considered as abnormal loss.

Rawat's ACCOUNT

Particulars	Amount	Particulars	Amount
To Consignment A/c (Sales)	7,35,000	By Consignment A/c (Expenses)	50,000
		By Consignment A/c (Commission)	73,500
		By Balance c/d (Bal. Fig.)	6,11,500
	7,35,000		**7,35,000**

W.N.- Abnormal Loss and Closing Stock

Particulars	Units	Amount
Goods sent on Consignment	500	7,50,000
Consignor Expenses	-	75,000
	500	**8,25,000**
Less: Abnormal Loss	(50)	(82,500)
Less: Goods in Transit	(50)	(82,500)
	400	6,60,000
Consignee non recurring expenses	-	18,000
	400	**6,78,000**

Units Left unsold = 400 – 350 = 50

Value of Closing Stock = 6,78,000/400 * 50 = 84,750

Notes:

1) The goods in transit (50 cases) have not yet been cleared. Hence the proportionate clearing charges on those goods have not been included in their value
2) It has been assumed that balance of Rs. 6,11,500 is not yet paid

Question 5

Raj of Gwalior consigned 15,000 kgs of Ghee at Rs. 30 per kg to his agent Siraj at Delhi. He spent Rs. 5 per kg as freight and insurance for sending the Ghee at Delhi. On the way 100 kgs of Ghee was lost due to the leakage (which is to be treated as normal loss) and 400 kgs of Ghee was destroyed in consignee godown. Rs. 9,000 was paid to the consignor directly by the Insurance company as Insurance Claim. Siraj sold 7,500 kgs at Rs. 60 per kg. He spent Rs. 33,000 on advertisement and recurring expenses and 10,000 as non recurring expenses

Prepare Consignment account showing profit or loss on consignment, if Siraj is entitled to 5% commission on sales.

Solution

BOOKS OF Mr. RAJ

CONSIGNMENT ACCOUNT

Particulars	Amount	Particulars	Amount
To Goods Sent on Consignment A/c (15,000*30)	4,50,000	By Abnormal Loss A/c	14,362
To Bank A/c (Expenses-Freight & Insurance) (15,000*5)	75,000	By Siraj A/c (Sales) (7,500*60)	4,50,000
To Siraj A/c (Expenses)	43,000	By Consignment Stock A/c	2,51,342
To Siraj A/c (Commission)* (4,50,000*5%)	22,500		
To P&L A/c (Profit) – Bal. Fig.	1,25,204		
	7,15,704		**7,15,704**

ABNORMAL LOSS ACCOUNT

Particulars	Amount	Particulars	Amount
To Consignment A/c	14,362	By Bank A/c (Insurance Claim)	9,000
		By P&L A/c (Loss transferred)	5,362
	14,362		**14,362**

W.N.- Abnormal Loss and Closing Stock

Particulars	Units	Amount
Goods sent on Consignment	15,000	4,50,000
Consignor Expenses	-	75,000
	15,000	**5,25,000**
Less: Normal Loss	(100)	(-)
	14,900	**5,25,000**
Consignee non recurring expenses	-	10,000
	14,900	5,35,000
Less: Abnormal Loss	(400)	(14,362)
	14,500	**5,20,638**

Units Left unsold = 14,500 – 7,500 = 7,000

Value of Closing Stock = 5,20,638/14,500 * 7,000 = 2,51,342

Question 6

Anand of Bangalore consigned to Raj of pune, goods to be sold at invoice price which represents 125% of cost. Raj is entitled to a commission of 10% on sales at invoice price and 25% of any excess realised over invoice price. The expenses on freight and insurance incurred by Anand were Rs. 12,000. The account sales received by Anand shows that Raj has effected sales amounting to Rs. 1,20,000 in respect of 75% of the consignment. His selling expenses to be reimbursed were Rs. 9,600. 10% of consignment goods of the value of Rs. 15,000 were destroyed in fire at the Pune godown and the insurance company paid Rs. 12,000 net of salvage. Raj remitted the balance in favour of Anand.

You are required to prepare Consignment Account and the account of Raj in the books of Anand along with the necessary calculations.

Solution

Books of Anand

Dr. Consignment to Pune Account Cr.

Particulars	Amount	Particulars	Amount
To Goods Sent on Consignment A/c	1,50,000	By Goods sent on consignment A/c (Loading)	30,000
To Bank A/c (Frieght & Insurance)	12,000	By Abnormal Loss	13,200
To Raj's A/c (Expenses)	9,600	By Raj (Sales)	1,20,000
To Raj's (Commission)	13,125	By Consignment Stock A/c	24,300
To Inventories Reserve A/c	4,500	By Profit & Loss A/c (Bal. Fig.)	1,725
	1,89,225		**1,89,225**

Dr. Raj's Account Cr.

Particulars	Amount	Particulars	Amount
To Consignment A/c (Sales)	1,20,000	By Consignment A/c (Expenses)	9600
		By Consignment A/c (Commission)	13,125
		By Bank A/c (Bal. Fig.)	97,275
	1,20,000		**1,20,000**

Dr. Abnormal Account Cr.

Particulars	Amount	Particulars	Amount
To Consignment A/c (Sales)	13,200	By Bank A/c (Claim)	12,000
		By Profit & Loss (Loss)	1,200
	13,200		**13,200**

W.N.

(1) Calculation of Value of Goods sent on consignment :

Abnormal Loss at invoice price = 15000

Abnormal Loss as a percentage of total consignment = 10%

Hence, the value of Goods Sent on consignment = 15000×100/10 = 1,50,000

Loading of goods sent on consignment = 1,50,000×25/125 = 30,000

(2) Abnormal Loss and Closing Stock

Particulars	Invoice Value	Cost
Goods sent on Consignment	1,50,000	1,20,000
Consignor Expenses	12,000	12,000
	1,62,000	**1,32,000**
Less: Abnormal Loss (10%)	(16,200)	(13,200)
	1,45,800	**1,18,800**

Invoice Value of Closing Stock = 1,45,800/90 * 15 = 24,300
Loading in Closing Stock = 30,000 * 15% = 4,500
Cost of Closing Stock = 1,18,800/90 * 15 = 19,800

(3) Calculation of Commission :
Invoice price of Goods sold = 75% of 1,50,000 = 1,12,500
Excess of selling price over Invoice price = 1,20,000–1,12,500 = 7500
Total Commission = 10% of 1,12,500 + 25% of 7,500
= 11,250 + 1875
= 13,125

JOURNAL ENTRIES IN THE BOOKS OF THE CONSIGNEE

	Transactions	Journal Entry
1.	Advance sent as Cash/Cheque/ Bill of Exchange	Consignor A/c Dr. To Cash/Bank/Bill Payable A/c
2.	Expenses incurred by Consignee	Consignor A/c Dr. To Cash/ Bank A/c
3.	Own Acceptance(B/P) honoured on due date	Bills Payable A/c Dr. To Cash/ Bank A/c
4.	Sales made on Consignment Basis	Cash/ Bank/Sundry Debtor A/c Dr. To Consignor A/c
5.	Commission earned by Consignee	Consignor A/c Dr. To Commission Income A/c
6.	Bad debts	Bad Debts A/c Dr. To Sundry Debtors A/c
7.	Transfer of Bad Debts a) If borne by Consignor (Del-Credere Commission not given) b) If borne by Consignee (Del-Credere Commission given)	 Consignor A/c Dr. To Bad Debts A/c Commission A/c Dr. To Bad Debts A/c
8.	Final settlement amount paid to Consignor	Consignor A/c Dr. To Cash/ Bank A/c

CONSIGNOR ACCOUNT

Particulars	₹	Particulars	₹
To Cash/Bank/B/P Acc (Advance) To Cash/Bank A/c (Expenses) To Commission Income To Bad Debts (Debtors A/c) (if Del credere not given) To Cash/Bank A/c **(Bal. Fig.)**		By Cash/Bank/Debtors (Sales)	
Total		**Total**	

Question 7

A of Sonepat consigned 500 bicycles to B of Cochin to be sold on his account & at his risk. The cost of one bicycle was Rs. 200. A paid Rs. 5,500 as freight and insurance and received Rs. 40,000 as advance from B. B Paid Rs. 1,000 as octroi and carriage, Rs. 1,500 as rent and Rs. 1,200 as insurance. 410 bicycles were sold by B for Rs. 1,10,000. B was entitled to a commission of 5% on sale @ 250 per bicycle and 25% of any surplus realized.
Prepare A's Account in books of B.

Solution

BOOKS OF B
A's ACCOUNT

Particulars	Amount	Particulars	Amount
To Bank A/c (Advance)	40,000	By Bank A/c (Sales)	1,10,000
To Bank A/c (Expenses)	3,700		
To Commission A/c	7,000		
To Bank A/c (Bal. Fig.)	59,300		
	1,10,000		**1,10,000**

Commission = [(410 * 250)*5%] + [{1,10,000-(410*250)}*25%]
= (1,02,500 * 5%) + (7,500*25%)
= 5,125 + 1,875
= 7,000

SALE OF GOODS ON APPROVAL OR RETURN BASIS

CONCEPT

1. **Need:** In order to increase the sales of a product or to introduce a new product, a Firm may sell goods on approval or return basis.
   Generally, these transactions take place between the Manufacturer (or Wholesaler) and a Retailer.

2. **Effect:** In a Sale of Goods on Approval or Return basis, the goods will be delivered to the customers, with the option of either retaining them or returning them within a specified period.

3. **Possession Vs Ownership:** When goods are sold on Approval or Return basis, there is a change in possession of goods only, and not a transfer of ownership of goods.

4. **Transfer of Ownership:** As per the Sale of Goods Act, in respect of goods sent on approval or return basis, the transfer of ownership will take place only –
   (a) When the Buyer / Customer gives his approval, **<u>(Direct consent)</u>**.
   (b) When the Buyer / Customer does some act which denotes that he accepts the transaction, i.e. consumption or use of the goods involved, **<u>(Implied consent)</u>**
   (c) If the Buyer / Customer has not given his approval or acceptance to the Seller but retains the goods without giving the notice of rejection, on the expiry of the specified time (if a time has been fixed) or on the expiry of a reasonable time (if no time has been fixed) **<u>(Lapse of time)</u>**.

METHODS OF ACCOUNTING

ACCOUNTING TREATMENT

When transactions are **very less,** i.e. **casual** Sale or Return	When transactions are very **frequent, but not numerous** i.e. frequent Sale or Return	When transactions are very **frequent and numerous**
↓	↓	↓
Transaction is treated as Ordinary Sales.	Sale or Return Journal is prepared with 4 main columns.	Sale or Return Day Book and Sale or Return Ledger are prepared. These are regarded as Memorandum Books.

JOURNAL ENTRIES WHEN THE FIRM SENDS GOODS CASUALLY ON SALE OR RETURN BASIS (INFREQUENT)

	Transaction	Journal Entry	Remarks
1.	Goods dispatched on Approval or Return Basis	Sundry Debtors Dr. To Sales A/c	At Selling Price.

2.	Goods returned by customer within the specified period	Sales Returns or (Sales) A/c Dr. To Sundry Debtors A/c	At Selling Price.
3.	Goods accepted by Customer within specified period	No separate Journal Entry is required since it is already recorded as Normal Sales only.	Not Applicable
4.	Goods accepted at a price higher than the Invoice Price	Sundry Debtors A/c Dr. To Sales A/c	Difference in Price only.
5.	Goods accepted at a price lower than the Invoice Price	Sales A/c Dr. To Sundry Debtors A/c	Difference in price only.
6.	Goods pending approval at the end of the accounting period	Sales A/c Dr. To Sundry Debtors A/c	At Selling Price
7.	Recognition of Stock with customers at year – end	Stock with Customers A/c Dr. To Trading Account	Cost or NRV, whichever is less.

Casual Sale or Return

[Transactions are very less]

↓

To be treated as ordinary Sales

Dispatch of Goods → Debtors A/c - Dr

To Sales A/c

LATER ON

Return of Goods

Sales Return/Sales - Dr

To Debtors

Acceptance of Goods

Same Price

No Entry

Higher Price

Debtors A/c - Dr

To Sales

Lower Price

Sales A/c - Dr

To Debtors

Difference

Pending Approval At End

1. Sales A/c - Dr

To Debtors

2. Stock with Customers A/c - Dr

To Trading A/c

+20 D | +20 Days

1/4/20 | 1/5 | 25/3 | 31/3/21

Cost = 100000

SP = 125000

Cost = 200000

SP = 250000

Despatch (1/5)

Debtors 125000

To Sales 125000

Later on

Approved

No Entry

Rejected

Sales 125000

To Debtors 125000

Despatch (25/3)

Debtors 250000

To Sales 250000

Year End (31/3)

Sales 250000

To Debtors 250000

Stock with Customers 200000

To Trading A/c 200000

Question 1

X. Ltd. sends out its goods to dealers on Sale or Return basis. All such transactions are, however, treated as actual sales and are passed through the Day Book. Just before the end of the accounting year on 31.12.2021, 200 such goods have been sent to a dealer at Rs.250 each (cost Rs. 200 each) on sale or return basis and debited to his account. Of these goods, on 31.12.2021, 50 were returned and 70 were sold while for the other goods, date of return has not yet expired.
Pass necessary adjustment entries on 31.12.2021.

Solution

Journal Entries

Date	Particulars	L.F.	Dr.	Cr.
31.12.21	Sales/Sales Return A/c Dr. (250*50)		12,500	
	To Debtors A/c			12,500
	(Being adjustment for 50 units of goods returned by customers to whom goods sent on sale or return basis)			
31.12.21	Sales A/c Dr. (250*80)		20,000	
	To Debtors A/c			20,000
	(Being cancellation of entry for sale of goods not yet approved in respect of 80 units)			
31.12.21	Stock with Customers A/c Dr. (200*80)		16,000	
	To Trading A/c			16,000
	(Being inventories with customers recorded at cost)			

Note: No entry in respect of goods approved by the customers.
No. of units left = 200-50-70=80

Question 2

M Ltd. sends out its accounting machines costing Rs. 200 each to their customers on Sales or Return basis. All such transactions are, however, treated like actual sales and are passed through the Day Book. Just before the end of the financial year, i.e., on December 24, 2021, 300 such accounting machines were sent out at an invoice price of Rs. 280 each, out of which only 90 accounting machines are accepted by the customers Rs. 250 each and as to the rest no report is forthcoming.
Show the Journal Entries in the books of the company for the purpose of preparing Final Accounts for the year ended December 31, 2021.

Solution

Journal Entries

Date	Particulars	L.F.	Dr.	Cr.
31.12.21	Sales A/c Dr. (30*90)		2,700	
	To Debtors A/c			2,700
	(Being adjustment for reduction in selling price of 90 accounting machines @30 each)			
31.12.21	Sales A/c Dr. (280*210)		58,800	
	To Debtors A/c			58,800
	(Being cancellation of entry for sale of goods not yet approved in respect of 210 machines)			
31.12.21	Stock with Customers A/c Dr. (200*210)		42,000	
	To Trading A/c			42,000
	(Being inventories with customers recorded at cost)			

Question 3

Mr. Ganesh sends out goods on approval to few customers and includes the same in the Sales Account. On 31.3.2021, the Trade receivables balance stood at Rs.75,000 which included Rs.6,500 goods sent on

approval against which no intimation was received during the year. These goods were sent out at 30% over and above cost price and were sent to
Mr. Adhitya - Rs. 3,900 and Mr. Bakkiram - Rs. 2,600.
Mr. Adhitya sent intimation of acceptance on 25th April and Mr. Bakkiram returned the goods on 15th April, 2021.

Make the adjustment entries and show how these items will appear in the Balance Sheet on 31st March, 2021. Show also the entries to be made during April, 2021. Value of closing Inventories as on 31st March, 2021 was Rs.50,000.

Solution

Journal Entries

Date	Particulars	L.F.	Dr.	Cr.
31.03.21	Sales A/c Dr.		6,500	
	To Trade receivables A/c			6,500
	(Being the cancellation of original entry of sale in respect of goods on sale or return basis)			
31.03.21	Stock with Customers A/c Dr.		5,000	
	To Trading A/c (Note 1)			5,000
	(Being inventories with customers recorded at cost)			
25.04.21	Trade Receivables A/c Dr.		3,900	
	To Sales A/c			3,900
	(Being the goods sent to customers on sale or return basis in last financial year has been accepted)			

<u>Balance Sheet of A & Co. as on 31st March, 2021 (Extracts)</u>

Assets		
Trade receivables (75,000-6,500)		68,500
Inventories-in-trade	50,000	
Add: Inventories with customers on Sale or Return	5,000	55,000
		1,23,500

Notes:
(1) Cost of goods lying with customers = 100/130 x 6,500 = 5,000
(2) No entry is required on 15th April, 2021 for goods returned by Mr. Bakkiram. Goods should be included physically in the Inventories-in-trade.

ACCOUNTING TREATMENT WHEN SALE OF GOODS ON APPROVAL OR RETURN BASIS ARE FREQUENTLY DONE.

When Sale or Return transactions are very frequent, but not numerous, a separate Register/Day Book called "Sale or Return Journal" is maintained. The format of this Register is as under –

Goods sent on approval				Goods Returned				Goods Approved				Balance
1	2	3	4	5	6	7	8	9	10	11	12	13
Date	Particulars	LF	Amount	Date	Particulars	LF	Amount	Date	Particulars	LF	Amt	Amount
No entry in Financial Books				**No entry in Financial Books**				**Recorded as Sales**				**Treated as Stock**

Transaction	Treatment
Goods dispatched to Customers	➢ No entry in Financial Books. ➢ Record the dispatch in Columns 1 to 4 of the above Journal.
Goods returned by Customers	➢ No entry in Financial Books. ➢ Record the return in Columns 5 to 8 of the above Journal.
Goods approved by Customers	➢ Record the approval in Columns 9 to 12 of the above Journal. ➢ Record as Sales, by the following Journal Entry— Sundry Debtors A/c Dr. (At Selling Price) To Sales A/c (At Selling Price)
Stock at end of the period	➢ Recorded as Closing Stock (Column 13), by the following Journal Entry— Stock with Customers A/c Dr. (At lower of Cost or NRV) To Trading Account

Method: 2

Goods sent	Goods Returned	Goods Approved	Balance
500000	100000	280000	120000
No Entry in Financial Books	No Entry in Financial Books	Recorded as Sales	Treated as Stock

Method: 3

	Goods sent	Goods Returned	Goods Approved	Balance
A	300000	70000	110000	120000
B	200000	30000	170000	-

A

To Sale or Return	300000	By Sale or Return	70000
		By Sale or Return	110000
		By Bal c/d	120000

B

To Sale or Return	200000	By Sale or Return	30000
		By Sale or Return	170000

Sale or Return A/c

To Sundries (Return)	100000	By Sundries (Sale)	500000
To Sundries (Approval)	280000		
To Bal c/d	120000		

ACCOUNTING TREATMENT WHEN TRANSACTIONS RELATING TO SALE OF GOODS ON APPROVAL OR RETURN BASIS FREQUENT AND NUMEROUS

1. When Sale on Approval or Return transactions are frequent and numerous, there is a need to ensure proper control over the Sale or Return transactions. For this purpose, the Firm maintains –
   (a) Sale or return **Day Book**.
   (b) Sale or Return **Ledger** – containing the Ledger Accounts of Customers to whom goods are sent.
2. This Day Book & Ledger **are Memorandum Books**. They **do not** form part of the regular financial books.
3. The accounting process is explained below –

Transaction	Entry in		
	Sale or Return Day Book	**Sale or Return Ledger**	**Financial Books, i.e. Regular General Ledger**
Goods despatched to Customers	Record the despatch in Columns 1 to 4 of the S/R Day Book.	Customer A/c Dr. To Sale or Return A/c (Entry made at Selling Price)	No Entry in Financial Books.
Goods returned by Customers	Record the return in Columns 5 to 8 of the S/R Day Book.	Sale or Return A/c Dr. To Customer A/c (Entry made at Selling Price)	No Entry in Financial Books
Goods approved by Customers **(See Note below)**	Record the approval in Columns 9 to 12 of S/R Day Book.	Sale or Return A/c Dr. To Customer A/c (Entry made at Selling Price)	Customer A/c Dr. To Sales A/c (Entry made at Selling Price)
Stock at end of the period	Column 13 denotes Stock at Sale Price.	Balance in Sale or Return A/c is the value of Stock with Customers, at Sale Price.	Stock with Customers Dr. To Trading A/c (Entry made at Cost or NRV, whichever is lower)

Note: When goods are approved by customers, the earlier memorandum Sale entry in Sale or return Ledger is reversed, and the regular Sales Entry is recorded in the Financial Books.

Question 4

A firm sends goods on "Sale or Return basis". Customers have the choice of returning the goods within a month. During May 2021, the following are the details of goods sent:

Date (May)	2	8	12	18	20	27
Customers	P	B	Q	D	E	R
Value (Rs.)	17,000	22,000	25,000	5,500	2,000	28,000

Within the stipulated time, P and Q returned the goods and B, D and E signified that they have accepted the goods.

Show in the books of the firm, the Sale or Return Account and Customer-Q for Sale or Return Account as on 15th June 2021.

Solution

Dr. **Sale or Return Account** **Cr.**

Date	Particulars	Amount	Date	Particulars	Amount
2021 May,31	To Sundries : Sales	29,500	2021 May,31	By Sundries (Goods sent on sale or return basis)	99,500
June,15	To Sundries : Returned	42,000			
June,15	To Balance c/d	28,000			
		99,500			**99,500**
			June 16	By Balance b/d	28,000

Dr. **Q's Account** **Cr.**

Date	Particulars	Amount	Date	Particulars	Amount
2021 May,31	To Sale or Return A/c	25,000	2021 June,15	By Sale or Return A/c	25,000
		25,000			**25,000**

BANK RECONCILIATION STATEMENT

BANK PASS BOOK OR STATEMENT

Bank Pass Book (also known as Bank Statement) is an extract of the Ledger Account of the customer, as per the Bank's books of Accounts. It is a periodical statement of account in which all transactions, i.e, deposits and withdrawals made by the customer during the particular period is recorded.

Dr: +ve / Favourable Balance
Cr: -ve / Overdraft / Unfavourable

CUSTOMER
Cash Book

Date	Receipts	Cash	Bank	Date	Payments	Cash	Bank

Cr: +ve / Favourable Balance
Dr: -ve / Overdraft / Unfavourable

BANK
Pass Book [Bank statement / Ledger A/c of Customer]

Date	Particulars	Ref. No.	Withdrawals	Deposits	Dr./Cr.	Balance

BANK RECONCILIATION STATEMENT

1. **Bank Reconciliation Statement:** At periodical intervals, the customer/ business entity (i.e. Account Holder in the Bank), should compare the balance in Bank as shown by the Cash Book, with the Pass Book. In case of any differences between the two, they should be analyzed by listing out the various reasons for such difference. Such a statement is called **Bank reconciliation statement**.
2. **Advantages**: The advantages of Bank reconciliation statement are-
   (a) To record entries which have been missed out in the Cash Book, e.g. Interest charged/allowed by the bank, bank charges, and direct collection by bank etc.
   (b) To identify any errors that may been committed either in cash book in bank statement,
   (c) To identify any undue delay in the clearance of cheque and
   (d) To act as a deterrent against embezzlement frauds.

DIFFERENCES BETWEEN BANK STATEMENT AND CASH BOOK

Causes of Difference

Timing

Transaction recorded at 2 different times in cash book & Pass book

* Cheque issued but not presented
* Cheque deposited but not cleared

Transaction

Transactions which bank carries out itself without intimating the customer

* Interest allowed by bank
* Bank charges debited by bank

Error

Mistakes or errors in preparing accounts either in cash book or Pass book

PROCEDURE FOR BANK RECONCILIATION STATEMENT

BRS may be prepared in two ways-

(a) **Without** adjusting the Cash Book, i.e. Preparation of BRS only.

(b) **After** adjusting Cash Book for Items 3 to 10 given below, i.e. Preparation of Adjusted Cash Book and BRS.

METHOD 1: PREPARATION OF BRS ONLY (i.e. WITHOUT ADJUSTING CASH BOOK)

Prepare Bank Reconciliation Statement as under-

Starting Point	**Cash Book Balance**	**Pass Book Balance**
Balance as per Starting Point	Dr. Balance in Cash Book **(Favourable)**	Cr. Balance in Pass Book **(Favourable)**
1. Cheques issued but not yet presented for payment **(Item1)**	**Add**	**Subtract**
2. Cheques deposited into Bank but not yet credited/ cleared **(Item2)**	**Subtract**	**Add**
3. Interest allowed by Bank **(Item3)**	**Add**	**Subtract**
4. Interest & Dividends collected by Bank **(Item4)**	**Add**	**Subtract**
5. Direct payments into Bank by a customer **(Item5)**	**Add**	**Subtract**
6. Bills Receivable collected by bank on behalf of the customer **(Item6)**	**Add**	**Subtract**
7. Interest & Expenses charged by Bank **(Item7)**	**Subtract**	**Add**
8. Direct Payments by bank **(Item8)**	**Subtract**	**Add**
9. Dishonour of a bill discounted with the Bank **(Item9)**	**Subtract**	**Add**
10. Wrong Entries **(Item 10)**		
(a) Wrong Debit in Cash Book or in Pass Book, under-casting of Cr. Side of Cash Book, overcasting of Dr. side of cash book etc.	**Subtract**	**Add**
(b) Wrong Credit in Cash Book or Pass Book, overcasting of Cr. side of Cash book, under-casting of Dr. side of cash book	**Add**	**Subtract**
Balances as per End Point	**Pass Book Balance**	**Cash Book Balance**

METHOD 2: PREPARATION OF ADJUSTED CASH BOOK AND BRS

Step1: Prepare Adjusted Cash Book with the following Debits and Credits

Receipts	**Rs.**	**Payments**	**Rs.**
To balance b/d (in case of Favourable Balance as per Cash Book)		To balance b/d (in case of Overdraft Balance as per Cash Book)	
To Interest allowed by Bank	**Item 3**	By interest & expenses charged by bank	**Item 7**
To Interest & Dividends collected by Bank	**Item 4**	By Direct payments by bank as per SI	**Item 8**

To Direct Payments into Bank by firm's customers (being Firm's receipts)	**Item 5**	By dishonour of a bill discounted with the bank	**Item 9**
To Bill Receivable collected by bank on behalf of firm	**Item 6**		
To Rectification of Error in Cash Book, e.g. double credit posting, credit overcast, debit under cast, debit entry omission etc.	**Item 10**	By Rectification of error in cash book, e.g. double debit posting, debit overcast, credit undercast, credit entry omission etc.	**Item 10**
To balance c/d (in case of Overdraft balance as per Cash Book)		By balance c/d (in case of Favourable balance as per Cash Book)	
Total		**Total**	

Note:

- The closing balance in the above Adjusted Cash Book is called Adjusted Cash Balance. This will be taken to the BRS.
- In Item 10, Errors made in Cash Book will be adjusted, but errors made in Pass Book will not be given effect in Cash Book.

Step 2: Prepare Bank Reconciliation Statement as under-

Starting Point	**Cash Book Balance**	**Pass Book Balance**
Balance as per Starting Point	**Dr.** Balance in Cash Book **(Favourable)**	**Cr.** Balance in Pass Book **(Favourable)**
1. Cheques issued but not yet presented for payment (**Item1**)	**Add**	**Subtract**
2. Cheques deposited into Bank but not yet credited/cleared (**Item2**)	**Subtract**	**Add**
3. Wrong Cr. in Pass Book (**Item10**)	**Add**	**Subtract**
4. Wrong Dr. in Pass Book (**Item10**)	**Subtract**	**Add**
Balance as per End Point	**Pass Book Balance**	**Cash Book Balance**

Question 1

Prepare a Bank Reconciliation Statement from the following particulars as on 31st March, 2021:

Particulars	**Amount**
Debit balance as per bank column of the cash book	18,60,000
Cheque issued to creditors but not yet presented to the bank for payment	3,60,000
Dividend received by the bank but not entered in the Cash book	2,50,000
Interest allowed by the Bank	6,250
Cheques deposited into the bank for collection but not collected by bank upto this date	7,70,000
Bank Charges not entered in Cash Book	1,000
A cheque deposited into bank was dishonored but no intimation received	1,60,000
Bank paid house tax on our behalf but no intimation received from bank in this connection	1,75,000
Insurance premium paid by bank as per standing instruction not intimated	15,900
Cash sales wrongly recorded in the Bank column of the cash-book	2,55,000
Wrong credit given by the bank	1,50,000
Payments side of the Cash-book was under cast by	350
On 20th March, 2021 the debit balance as on the previous day, was brought forward as credit balance in Cash-book	2,500
A customer, who received a cash discount of 5% on his account of Rs. 2,000, paid cheque on 24th March, 2021. The cashier erroneously entered the gross amount in the Cash-Book.	2,000
Bank recorded a Cash deposit of Rs. 1,550 as Rs. 1,505	

Solution

Bank Reconciliation Statement

Particulars	**Amount**
Balance as per Cash book	18,60,000
Add : Cheque issued but not presented	3,60,000
Add : Dividend collected by the bank directly but not recorded in the cash book	2,50,000
Add : Interest allowed by bank	6,250
Less : Cheque deposited in bank but not yet credited	(7,70,000)
Less : Bank charges debited by the bank not entered in cash book	(1,000)
Less : Cheque deposited into bank was dishonored but no intimation received	(1,60,000)
Less : Bank paid house tax on our behalf but no intimation received from bank	(1,75,000)
Less : Insurance premium paid by bank as per standing instruction	(15,900)
Less: Cash sales wrongly recorded in the Bank column of the cash-book	(2,55,000)
Add: Wrong credit given by the bank	1,50,000
Less: Undercasting of payment side of cash book	(350)
Add: Debit balance brought forward as credit balance (2,500*2)	5,000
Less: Discount recorded in Bank column (2000*5%)	(100)
Less: Cash deposit wrongly recorded by bank (1550-1505)	(45)
Balance as per Pass Book	**12,53,855**

Question 2

On 30th November, 2020, the Bank Statement of Mr. Hari showed Rs. 3,200 overdrawn. An examination of the records showed the following errors:

(i) The debit side of the Cash Book was undercast by Rs. 400.

(ii) A cheque for Rs. 1,600 in favour of Y suppliers Ltd. was omitted by the bank from the statement, the cheque was debited to another customer's Account.

(iii) A cheque for Rs. 172 drawn for payment of telephone bill was recorded in the Cash Book as Rs. 127 but was shown correctly in the Bank Statement.

(iv) A cheque for Rs. 425 from Mr. Pal paid into bank was dishonoured and shown as such on the Bank Statement, although no entry relating to the dishonoured cheque was made in the Cash Book.

(v) The Bank had debited a cheque for Rs. 150 to Mr. Hari's Account by mistake, it should have been debited by them to Mr. Kar's Account.

(vi) A dividend of Rs. 100 was collected by the bank but not entered in the Cash Book.

(vii) Cheque for Rs. 1,200 deposited on 30th November was not credited by the Bank.

(viii) Interest amounting to Rs. 300 was debited by the Bank but yet to be entered in the Cash Book.

(ix) A cheque worth Rs. 400 directly deposited into Bank by customer but no entry was made in the Cash Book.

(x) Out of cheques issued worth Rs. 34,000, cheques amounting to Rs. 20,000 only were presented for payment till 30th Nov, 2020.

(xi) A cheque for Rs. 4,000 received and entered in the Cash Book but it was not sent to the Bank.

(xii) Cheques worth Rs. 20,000 had been sent to Bank for collection but the collection was reported by the Bank as under.

(1) Cheques collected before 30th Nov, 2020, Rs. 14,000

(2) Cheques collected on 10th Dec, 2020, Rs. 4,000

(3) Cheques collected on 12th Dec, 2020, Rs. 2,000.

(xiii) The Bank made a direct payment of Rs. 600 which was not recorded in the Cash Book.

You are required to prepare a Bank Reconciliation Statement on 30th November, 2020.

Solution

Bank Reconciliation Statement as on 30th November, 2020

	Particulars	Amount
	Bank Overdraft as per Bank Statement	(3,200)
Less:	Debit side of the Cash Book was undercast	(400)
Less:	Cheque issued but debited by the Bank to another customer's account by mistake	(1,600)
Add:	Cheque issued for 172 posted in the Cash Book as 127	45
Add:	Cheque dishonoured but not recorded in the Cash Book	425
Add:	Wrong debit by the Bank to Hari's A/c	150
Less:	Dividend directly collected by the Bank but not entered in the Cash Book	(100)
Add:	Cheque deposited but yet to be credited	1,200
Add:	Interest debited by Bank and yet to be entered in the Cash Book	300
Less:	Cheques deposited into the Bank by Customer but not entered in Cash Book	(400)
Less:	Cheques issued but not presented Rs. (34,000-20,000)	(14,000)
Add:	Cheques received, recorded in cash Book but not sent to the Bank	4,000
Add:	Cheques sent to the Bank but not collected	6,000
Add:	Direct payment made by the bank not recorded in the Cash book	600
	Bank overdraft as per the Cash Book (Cr.)	**(6,980)**

Question 3

On 30th September, 2021, the bank account of XYZ, according to the bank column of the cash book, was overdrawn to the extent of Rs. 8,062. An examination of the Cash book and Bank Statement reveals the following:

a) A cheque for Rs. 11,14,000 deposited on 29th September, 2021 was credited by the bank only on 3rd October, 2021.
b) A payment by cheque for Rs. 18,000 has been entered twice in the Cash book
c) On 29th September, 2021, the bank credited an amount of 1,15,400 received from a customer of XYZ, but the advice was not received by XYZ until 1st October, 2021.
d) Bank charges amounting to Rs. 280 had not been entered in the cash book.
e) On 6th September 2021, the bank credited Rs. 30,000 to XYZ in error.
f) A bill of exchange for Rs. 1,60,000 was discounted by XYZ with his bank. The bill was dishonoured on 28th September, 2021 but no entry had been made in the books of XYZ.
g) Cheques issued upto 30th September, 2021 but not presented for payment upto that date totalled Rs. 13,46,000.
h) A bill payable of Rs. 2,00,000 had been paid by the bank but was not entered in the cash book and bill receivable for Rs. 60,000 had been discounted with the bank at a cost of Rs. 1,000 which had also not been recorded in cash book.
i) A cheque for Rs. 70,000 had been dishonoured prior to 30th September, 2021, but no record of this fact appeared in the cash book.
j) A dividend of Rs. 1,80,000, paid direct to the bank had not been recorded in the cash book.
k) No entry had been made in the cash book for a trade subscription of Rs. 10,000 paid vide banker's order in August, 2021.
l) A cheque for Rs. 27,000 drawn by ABC had been charged to XYZ's bank account by mistake in September, 2021.

You are required:
To show the appropriate rectifications required in the cash book of XYZ, to arrive at the correct balance on 30th September, 2021 and to prepare a Bank Reconciliation Statement as on that date.

Solution

Cash Book (Adjusted/Revised)

Particulars	Amount	Particulars	Amount
To Party A/c (Twicely Credited, now rectify)	18,000	By Balance b/d	8,062
To Customers A/c	1,15,400	By Bank charges A/c	280
To Bills receivables A/c	59,000	By Customer (B/R dishonoured)	1,60,000
To Dividend Received	1,80,000	By Bills payable A/c	2,00,000
To Balance c/d (Bal. Fig.)	75,942	By Trade receivables (Cheque dishonoured)	70,000
		By Trade Subscription	10,000
	4,48,342		**4,48,342**

Bank Reconciliation Statement As on 30th September, 2021

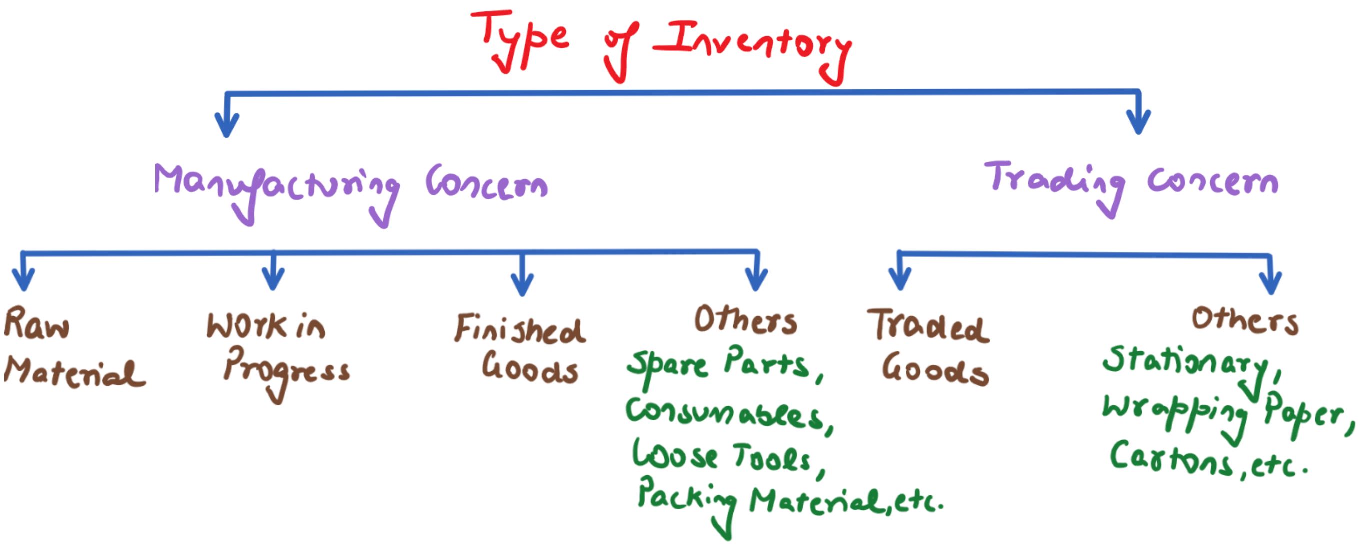
Particulars	Amount
Credit Balance (Overdraft) as per cash Book	(75,942)
Less: A cheque for Rs. 11,14,000 deposited on 29th Sep. 2021 was credited by the bank only on 3rd October, 2021	(11,14,000)
Add: On 6th Sep., 2021 the bank Credited Rs. 30,000 to XYZ in error	30,000
Add: Cheque issued up to 30th Sep., 2021 but not presented for payment up to that date totalled Rs. 13,46,000	13,46,000
Less: Cheque wrongly charged	(27,000)
Credit Balance (Favourable) as per pass book	**1,59,058**

INVENTORIES

DEFINITION

Inventories are Assets-

Nature of Inventory	Description
Held for sale in the ordinary course of business, or	**Finished goods**
In the process of production for such sale, or	**Work in progress**
In the form of materials or supplies to be consumed in the production process or in the rendering of services	**Raw Material**-including consumables & Loose Tools used in production process.



SIGNIFICANCE OF INVENTORY VALUATION

- To ascertain the **true income earned** by the entity during the accounting period
- To determine the **true financial position** of the **entity** as on the Balance sheet date.
- To analyze the **liquidity** of the enterprise.
- To ensure **compliance with disclosure requirements** under Accounting standard -2, and applicable Statutes like Companies Act, 2013

Note: Effect of wrong valuation of inventory on Profits and Balance Sheet position

Situation	Effect on Profit	Effect on Balance sheet	Effect on liquidity
Closing stock overstated	Overstated	Higher Current Assets	High
Closing stock understated	Understated	Lower Current Assets	Low
Opening stock overstated	Understated	-	-
Opening stock understated	Overstated	-	-

MEASUREMENT OR VALUATION OF INVENTORY

Principle: Inventories should be valued at – (a) Cost, or (b) Net Realizable Value**, whichever is lower.**

COMPONENTS OF COST

Meaning of Cost: The Cost of Inventories shall comprise **all-**

COST

- **Purchase Cost**
  - Purchase Price
  - + Non Refundable Taxes & Duties
  - + Freight Inwards
  - + Directly Attributable Expenditure [Eg. Transit Insurance, Buying Commission, etc.]
  - (–) Trade Discount / Rebate, etc.
- **Conversion Cost**
  - Direct Cost
    - Direct Labour
  - Indirect Cost (O/Hs)
    - Fixed Overheads
    - Variable Overheads
- **Other Costs**
  - Costs incurred in bringing inventories to their present location & condition [Eg. Design Costs]

NET REALIZABLE VALUE

Estimated Selling Price	XX
Less: Estimated selling expenses	(XX)
Less: Estimated cost of completion	(XX)
NRV	**XX**

➢ Inventories are usually written down to Net Realizable value on an item-by-item basis.

Example:

	Cost	NRV	Lower
Product A	50	40	40
Product B	60	80	60
			100

INVENTORY SYSTEMS

Inventory System refers to – (a) system of recording receipts and issues of inventory, and physical counting of actual stock available at the period end and (c) comparing physical stock as per books and records to ascertain discrepancies if any.

Periodic Inventory System	Perpetual Inventory System
This system is based on physical verification	It is based on book records.
This system provides information about inventory and cost of goods sold at a particular date	It provides continuous information about inventory and cost of sales.
This system determines inventory and takes cost of goods sold as residual figure.	It directly determines cost of goods sold and computes inventory as balancing figure.
Cost of goods sold includes loss of goods as goods not in inventory are assumed to be sold	Closing inventory includes loss of goods as all unsold goods are assumed to be in Inventory.
Under this method, inventory control is not possible	Inventory control can be exercised under this system.
This system is simple and less expensive.	It is costlier method.
Periodic system requires closure of business for counting of inventory.	Inventory can be determined without affecting the operations of the business.

Note:-

Periodic inventory system is used by small enterprises where is easy to control physical inventory. This system is not considered suitable for medium or larger enterprises which generally use Perpetual Inventory system.

TECHNIQUES / FORMULA FOR INVENTORY VALUATION

Techniques of Inventory Valuation

Historical Cost Methods

1) Specific Identification Method (Items not ordinarily interchangeable)
2) First in First Out (FIFO)
3) Last in First Out (LIFO)
4) Simple Average
5) Weighted Average

Non Historical Cost Methods

1) Adjusted Selling Price/ Retail Inventory Method
2) Standard cost Method

Question

A manufacturer has following record of a condenser, which he uses while manufacturing radio sets

Date	Quantity (units)	Price per unit
Dec. 4	900	50
Dec. 10	400	55
Dec. 11	300	55
Dec. 19	200	60
Dec. 28	800	47
	2,600	

Record of issues

Date	Quantity (units)
Dec. 5	500
Dec. 20	600
Dec. 29	500
	1,600

Find out value of inventory by following methods:

1) FIFO Method
2) LIFO Method
3) Simple Average Method
4) Weighted Average Cost Method

Also find inventory value if computed by Periodic inventory system.

Solution

a) First-in-First out basis (FIFO)

Calculation of the value of Inventory as on 31st December

Date	Particulars	Receipts			Issue			Balance		
		Qty.	Rate	Amt.	Qty.	Rate	Amt.	Qty.	Rate	Amt.
Dec 4	Purchase	900	50	45,000				900	50	45,000
Dec 5	Issue				500	50	25,000	400	50	20,000

Dec 10	Purchase	400	55	22,000				400	50	20,000
								400	55	22,000
Dec. 11	Purchase	300	55	16,500				400	50	20,000
								400	55	22,000
								300	55	16,500
Dec. 19	Purchase	200	60	12,000				400	50	20,000
								400	55	22,000
								300	55	16,500
								200	60	12,000
Dec 20	Issue				400	50	20,000	200	55	11,000
					200	55	11,000	300	55	16,500
								200	60	12,000
Dec 28	Purchase	800	47	37,600				200	55	11,000
								300	55	16,500
								200	60	12,000
								800	47	37,600
Dec 29	Issue				200	55	11,000	**200**	**60**	**12,000**
					300	55	16,500	**800**	**47**	**37,600**

Therefore, the value of Inventory as on 31 Dec: 1000 units = ₹ 49,600

b) <u>Last-in-First out basis (LIFO)</u>

c) Calculation of the value of Inventory as on 31st December

Date	**Particulars**	**Receipts**			**Issue**			**Balance**		
		Qty.	**Rate**	**Amt.**	**Qty.**	**Rate**	**Amt.**	**Qty.**	**Rate**	**Amt.**
Dec 4	Purchase	900	50	45,000				900	50	45,000
Dec 5	Issue				500	50	25,000	400	50	20,000
Dec 10	Purchase	400	55	22,000				400	50	20,000
								400	55	22,000
Dec. 11	Purchase	300	55	16,500				400	50	20,000
								400	55	22,000
								300	55	16,500
Dec. 19	Purchase	200	60	12,000				400	50	20,000
								400	55	22,000
								300	55	16,500
								200	60	12,000
Dec 20	Issue				200	60	12,000	400	50	20,000
					300	55	16,500	300	55	16,500
					100	55	5,500			
Dec 28	Purchase	800	47	37,600				400	50	20,000
								300	55	16,500
								800	47	37,600
Dec 29	Issue				500	47	23,500	**400**	**50**	**20,000**
								300	**55**	**16,500**
								300	**47**	**14,100**

Therefore, the value of Inventory as on 31 Dec: 1000 units valuing ₹ 50,600

a) <u>Simple Average Cost</u>

Simple Average per unit Cost = (50+55+55+60+47)/5 = 53.40

Closing Stock (in Units) = 1000 units

Value = 1000 * 53.40 = 53,400

b) **Weighted Average Cost**

Calculation of the value of Inventory as on 31st December

Date	Particulars	Receipts			Issue			Balance		
		Qty.	Rate	Amt.	Qty.	Rate	Amt.	Qty.	Rate	Amt.
Dec 4	Purchase	900	50	45,000				900	50	45,000
Dec 5	Issue				500	50	25,000	400	50	20,000
Dec 10	Purchase	400	55	22,000				800	52.50	42,000
Dec 11	Purchase	300	55	16,500				1100	53.18	58,500
Dec 19	Purchase	200	60	12,000				1300	54.23	70,500
Dec 20	Issue				600	54.23	32,538	700	54.23	37,962
Dec 28	Purchase	800	47	37,600				1500	50.37	75,562
Dec 29	Issue				500	50.37	25,185	**1000**	**50.37**	**50,377**

Therefore, the value of Inventory as on 31 Dec: 1000 units valuing ₹ 50,377

PERIODIC INVENTORY SYSTEM

1) FIFO
   Closing Stock = [(200*60)+(800*47)] = 49,600

2) LIFO
   Closing Stock = [(900*50)+(100*55)] = 50,500
3) Simple Average = Same value as earlier ie 53,400
4) Weighted Average
   Weighted average cost per unit = $\frac{(900*50)+(400*55)+(300*55)+(200*60)+(800*47)}{900+400+300+200+800}$
   $= \frac{1,33,100}{2,600}$
   $= 51.19$
   Closing Stock = 1,000*51.19 = 51,190

RETAIL METHOD

1. **Applicability:** This method is applicable in the following situations
   (a) Retail trade
   (b) Similar profit margins
   (c) Inventories of large numbers of rapidly changing items, and
   (d) Impracticable to use other costing methods
2. Retail Method may be used for **convenience** if the results approximate the actual cost.
3. **Measurement:** Cost of Inventory = **Sales Value of Inventory Less Appropriate Gross Margin %**

Note: Adjusted GP Percentage is used for inventories marked down to below its Original Selling Price. An average percentage for each Retail Departments is often used.

Cost + Profit = Sales	So, the relationship to be remembered is-
100% + 50% = 150%	(50÷100) = 1/2nd on Cost = 1/3rd on Sales = (50÷150)
100%+33 1/3%=133 1/3%	(33 1/3÷100) = 1/3rd on Cost = 1/4rd on Sales = (33 1/3÷133 1/3)
100% + 25% = 125%	(25÷100) = 1/4th on Cost = 1/5rd on Sales = (25÷125)
100% + 20% = 120%	(20÷100) = 1/5th on Cost = 1/6rd on Sales = (20÷120)

STANDARD COST METHOD

This method is used when there is frequent change in the price per unit of the goods and goods are purchased frequently by the business e.g. crude oil. Based on the experience a standard cost is determined on the basis of frequent changes in prices and inventory is valued on that price per unit.

Physical Stock v/s Book Stock

Wherever required the following adjustments are carried out in respect of value of Physical stock, to arrive at the value of Inventory as per the Balance sheet

	Value of **Physical Stocks** on the Closing Date	XXX
Add	Goods in Transit, i.e. goods in respect of which the Firm has the title and ownership, but lying with the Transporter/ Carrier, pending delivery.	XXX.
Add	Goods held by other Entities on our behalf (e.g. Our stock held by Agent, Sub-Contractor, Job Worker, etc.)	XXX
Add	Goods sent on approval for which confirmation not received from customer.	XXX
Less	Any goods sold in respect of title has been transferred to the Buyer, but delivery pending at Buyer's request.	(XXX)
Less	Goods held by us on behalf of other Entities (e.g. As agent, as Sub-Contractor, as Job Worker, etc)	(XXX)
Less	Adjustments required to mark-down defectives/Obsolete items etc, to their NRV, if any.	(XXX)
	Value of Stocks as per Balance sheet	XXX

Verification of Stock on other than balance sheet date

Generally, Physical Stock Verification and Valuation is done at the end of the last day of the accounting year. Sometimes, in big organizations, it may not be possible to verify the stocks exactly on the last date of the accounting period. In such cases, stock is taken either few days earlier or later, according to the situation. The following adjustments are carried out in order to arrive at the Stock Value on the Balance Sheet date-

1. Stock Taking after Balance Sheet date	2. Stock Taking before Balance Sheet date
Value of Stocks on verification date (e.g. 6th April)	Value of Stocks on verification date (e.g. 25th March)
(+) Cost of Sales made during the interim period	**(+)** Purchases made during the interim period
(+) Purchase Returns during the interim period	**(+)** Sales Return (at Cost price) during the period
(-) Purchases made during the interim period	**(-)** Cost of Sales made during the interim period
(-) Sales Return (at cost price) during the period	**(-)** Purchase Return during the interim period
Value of Stocks on B/S date i.e., 31st March	Value of Stocks on B/S date i.e., 31st March

Question

A trader prepared his accounts on 31st March, each year. Due to some unavoidable reasons, no inventory taking could be possible till 15th April, 2021 on which date the total cost of goods in his godown came to ₹ 5,00,000. The following facts were established between 31st March &15th April, 2021

a) Sales ₹ 4,10,000 (including cash sales ₹ 1,00,000)

b) Purchases ₹ 50,340 (including cash purchases ₹ 19,900)

c) Sales Return ₹ 10,000.

Goods are sold by the trader at a profit of 20% on sales.

You are required to ascertain the value of inventory as on 31st March, 2021.

Solution

Alternative 1:

Statement of valuation of Inventory on 31st March, 2021

Value of Inventory as on 15th April, 2021		5,00,000
Add: Cost of goods sold during the period between 31st March, 2021 to 15th April, 2021		
Sales (₹ 4,10,000 - ₹ 10,000)	4,00,000	
Less: Gross Profit (20% of ₹ 4,00,000)	(80,000)	3,20,000
		8,20,000
Less: Purchases during the period from 31st March, 2021 to 15th April, 2021		(50,340)
Stock as on 31.03.2021		**7,69,660**

Alternative 2:

Trading Account (01.04.2021 to 15.04.2021)

	Amount		Amount
To Opening Stock (Balancing Figure)	7,69,660	By Sales 4,10,000 Less: Returns (10,000)	4,00,000
To Purchases	50,340	By Closing Stock	5,00,000
To Gross Profit (4,00,000*20%)	80,000		
	9,00,000		**9,00,000**

Question

Raj Ltd. prepared their accounts financial year ended on 31st March 2021. Due to unavoidable circumstances actual stock has been taken on 10th April 2021, when it was ascertained at Rs. 1,25,000. It has been found that;

(i) Sales are entered in the Sales Book on the day of dispatch and return inwards in the Returns Inward Book on the day of the goods received back.

(ii) Purchases are entered in the Purchase Book on the day the Invoices are received.

(iii) Sales between 1st April 2021 to 9th April 2021 amounting to Rs. 20,000 as per Sales Day Book.

(iv) Free samples for business promotion issued during 1st April 2021 to 9th April 2021 amounting to Rs. 4,000 at cost.

(v) Purchases during 1st April 2021 to 9th April 2021 amounting to Rs. 10,000 but goods amounts to Rs. 2,000 not received till the date of stock taking.

(vi) Invoices for goods purchased amounting to Rs. 20,000 were entered on 28th March 2021 but the goods were not included in stock.

Rate of Gross Profit is 25% on cost. Ascertain the value of Stock as on 31st March 2021.

Solution

Statement of Valuation of Stock as on 31st March, 2021

	₹	₹
Value of stock as on 10th April, 2021		1,25,000
Add: Cost of sales during the intervening period		
Sales made between 1.4.2021 and 9.4.2021	20,000	
Less: Gross profit @20% on sales	(4,000)	16,000
Less: Purchases actually received during the intervening Period		
Purchases from 1.4.2021 to 9.4.2021	10,000	
Less: Goods not received upto 9.4.2021	(2,000)	
Less: Free Samples	(4,000)	(4,000)
Add: Purchases during March, 2021 but not recorded in stock		20,000
Value of Stock as on 31.3.2021		**1,57,000**

FINAL ACCOUNTS OF SOLE PROPRIETORS

FINANCIAL STATEMENTS

1. **Financial Statements** (also called General Purpose Financial Statements) consist of the following –
   (a) Statement of Performance - Profit and loss Account
   (b) Statement of Financial Position - Balance Sheet
2. **Meaning**: the above terms are explained below –

Item	Description
Statement of Performance	• This Statement / Account shows the **result of operations**, i.e. Profit or Loss of the entity for the period. • It is also called **"Performance Statement"**, or **"Income Statement"** • Consists of – (i) Manufacturing Account, (ii) Trading Account, and (iii) Profit and Loss Account.
Statement of Financial Position	• This Statement (not an Account) shows the **financial position,** i.e. Assets and Liabilities of the entity as on a particular date. • It is also called **"Position Statement"** or **"Balance Sheet"**

Final Accounts of Sole Proprietorship Entities

Non-Manufacturing / Trading Entities,

i.e. Entities engaged in purchase and sale of goods, without involving any production process

1. Trading account
2. Profit and Loss Account
3. Balance Sheet

Manufacturing Entities

i.e. Entities engaged in converting Raw Materials into Finished Goods through production process.

1. Manufacturing Account
2. Trading Account
3. Profit and Loss Account
4. Balance Sheet

TRADING ACCOUNT

The Trading Account shows the surplus of the Sale Value over the Cost of Goods Sold. This is called as the **Gross Profit.** Since the Gross Profit is the basic indicator of business profitability, the preparation of the Trading Account assumes significance

Trading Account of ……. For the year ended …….

Particulars	₹	Particulars	₹
To Opening Stock To Purchases (net of Returns) To Direct Expenses like Freight Inward, Octroi, Wages, etc. To Gross Profit c/d to P/L Account		By Sales (net of returns) By Closing Stock By Gross Loss c/d to P&L Account	
Total		**Total**	

Gross Profit = Sales - Cost of Goods Sold
Where Cost of Goods Sold = Opening Stock + Purchases + Direct Expenses – Closing Stock
GP (%) = Gross Profit/ Sales * 100

FORMAT OF PROFIT AND LOSS ACCOUNT

Profit and Loss Account of ……… for the year ended …………

Particulars	₹	Particulars	₹
To Gross Loss b/d (if any) To Administrative Expenses To Selling Expenses To Financing Expenses To Depreciation To Other Items, Adjustments & Prov. To Net Profit, transferred to Capital A/c		By Gross Profit b/d from Trading A/c By Other Income items By Net Loss, if any, transferred to Capital A/c	
Total		**Total**	

BALANCE SHEET

The Balance Sheet is a statement of financial position which sets out the Assets and liabilities of an enterprise as at a certain date.

Balance Sheet of ……… as at ………..

Liabilities	₹	Assets	₹
Capital **Reserves & Surplus** **Loans** **Current Liabilities:** Sundry Creditors Outstanding Expenses		**Fixed Assets** **Investments** **Current Assets:** Stock Debtors Cash at Bank, Cash in Hand	
Total		**Total**	

ARRANGEMENT OF ASSETS AND LIABILITIES

	Method 1: Permanence Approach	Method 2: Liquidity Approach
Assets	Assets which are to be used in the business for a longer span of time and which are not meant for sale, are shown first. 1. **Fixed Assets:** • Land and Building • Plant & Machinery • Furniture & Fixtures 2. **Current Assets** • Stock • Sundry Debtors • Bills Receivable • Other Investments • Government Securities • Cash at Bank • Cash in hand	Assets which are readily convertible into cash are shown first 1. **Current Assets** • Cash in hand • Cash at Bank • Government Securities • Other Investments • Bills Receivable • Sundry Debtors • Stock 2. **Fixed Assets** • Furniture & Fixtures • Plant & Machinery • Land and Building
Liabilities	• Capital • Reserves & Surplus • Loans • Trade Creditors • Bills Payable One way is to first show the capital, then long-term liabilities and then short-term	• Bills Payable • Trade Creditors • Loans • Reserves & Surplus • Capital Start with short-term liabilities and then long term liabilities and last of all capital

ADJUSTMENT ENTRIES IN FINAL ACCOUNTS

1. EXPENSES

Expenses

O/s Expenses

(Accrued but not paid)

Expense A/c - Dr.
    To O/s Expense A/c

Trading and P&L A/c

Dr.	Cr.
To Expense xx + O/s Exp. xx xx	

B/s

Liabilities	Assets
O/s Exp. xx	

Prepaid Expenses

(Paid but not accrued)

Prepaid Expense A/c - Dr
    To Expense A/c

Trading and P&L A/c

Dr.	Cr.
To Expense xx - Prepaid Exp. (xx) xx	

B/s

Liabilities	Assets
	Prepaid Exp. xx

2. INCOMES

Income

Accrued Income

(Accrued but not Received)

Accrued Income A/c - Dr
    To Income A/c

P&L A/c

Dr.	Cr.
	By Income xx + Accrued Income xx xx

B/s

Liabilities	Assets
	Accrued Income xx

Pre Received Income

(Received but not accrued)

Income A/c - Dr
    To Pre Received Income A/c

P&L A/c

Dr.	Cr.
	By Income xx - Pre Rec. Income (xx) xx

B/s

Liabilities	Assets
Pre Rec. Income xx	

Note:
If O/s Expense, Prepaid Expense, Accrued Income, Pre received income appearing in trial balance then effect only in balance sheet as entry has already been passed.

3. CLOSING STOCK

Closing Stock

Not Appearing in Trial Balance / Given in Adjustments
(Entry to be passed)

Closing Stock A/c – Dr.
    To Trading A/c
(2 Effects)

Trading A/c

	By Closing Stock xx

B/s

Liabilities	Assets
	Closing Stock xx

Appearing in Trial Balance
(Entry already passed)

Closing Stock A/c – Dr.
    To Purchases A/c
(1 Effect)

B/s

Liabilities	Assets
	Closing Stock xx

4. DEPRECIATION

Note:
If Depreciation appearing in trial balance then effect only in P&L Account

5. ABNORMAL LOSS

1) Abnormal loss A/c - Dr
    To Trading A/c

2) Insurance claim Rec. A/c - Dr
    P&L A/c (Loss) - Dr
    To Abnormal loss A/c

Trading A/c

	By Abnormal loss xx

P&L A/c

To Abnormal loss xx	

B/S

Liabilities	Assets
	Ins. claim Rec. xx

6. SALE OF GOODS ON APPROVAL OR RETURN BASIS PENDING CONFIRMATION

1) Sales A/c - Dr
    To Debtors A/c
    (At Selling Price)

2) Stock with customers A/c - Dr
    To Trading A/c
    (Lower of Cost or NRV)

Trading A/c

	By Sales xx	
	- Approval Basis (xx)	xx
	By Closing stock	
	In hand xx	
	With customers xx	xx

Balance sheet

Liabilities	Assets	
	Debtors xx	
	- Approval Basis (xx)	xx
	Closing Stock	
	In hand xx	
	With customers xx	xx

7. MANAGER COMMISSION

Manager Commission

1) Manager Commission A/c - Dr
    To O/s Manager Commission

Before charging

$$\text{Net Profit before comm.} \times \frac{\text{Rate}}{100}$$

After charging

$$\text{Net Profit before comm.} \times \frac{\text{Rate}}{100+\text{Rate}}$$

8. BAD DEBTS AND PROVISION FOR DOUBTFUL DEBTS

If a customer fails to pay the amount due from him, the uncollectible amount is called Bad Debts.

Method	Method1: General Treatment, i.e. Without having Provision for Bad & Doubtful Debts Account	Method 2: With Provision/Reserve for Bad & Doubtful Debts Account
Rule	Transfer Bad Debts as per TB, to the Debit Side of P&L A/c	• Transfer Bad Debts to Provision A/c. • Maintain provision upto desired amount
Bad Debts written off	Bad Debts A/c Dr. To Sundry Debtors (by name)	Bad Debts A/c Dr. To Sundry Debtors (by name)
Transfer of Bad Debts	Profit and Loss A/c Dr. To Bad Debts A/c	Provision for Bad & Doubtful debts Dr. To Bad Debts A/c
Provision at year-end	There is no such requirement	Profit and Loss A/c Dr. To Provision for Bad & Doubtful Debts
Treatment in B/sheet	Not Applicable	Closing Balance of Provision for Bad and Doubtful debts A/c is shown on Assets Side, as a reduction from Sundry Debtor

Bad Debts

1) Bad debts A/c - Dr
To Debtors A/c

2) P&L A/c - Dr
To Bad debts

P&L A/c

To Bad debts xx

B/s

Liabilities	Assets
	Debtors xx - Bad debts(xx) xx

9. DISCOUNT ALLOWED AND PROVISION FOR DISCOUNT ON DEBTORS

The different accounting treatments in respect of discount allowed to debtors is as under

Method	**Method 1: General Treatment**	**Method 2**
Description	**Without having Provision for Discount on Debtors A/c**	**With Provision on Discount on Debtors A/c**
Rule	Transfer discount allowed as per Tb, to the debit side of P&L A/c	Transfer discount allowed as per TB to the debit side of Provision A/c. Maintain Provision up to the desired amt.
Discount Allowed	Discount allowed A/c Dr. To Sundry Debtors	Discount allowed A/c Dr. To Sundry Debtors
Tfr of Dis Allowed	Profit & Loss A/c Dr. To Discount allowed A/c	Provision for discount on debtors Dr. To Discount allowed A/c
Creating Provision at year end	There is no such requirement	Profit and Loss A/c Dr. To Provision for discount on debtors
Treatment in Balance sheet	Not applicable	Closing balance of provision for discount allowed on debtors A/c is shown on the assets side as a reduction from debtors

Note: The provision for discount on debtors is calculated after deducting the provision for doubtful debts from debtors in order to determine the provision for discount on good debtors who make their payment promptly after getting the discount.

10. DISCOUNT RECEIVED AND RESERVE FOR DISCOUNT ON CREDITORS

The different accounting treatment in respect of discount received from supplier is as under:-

Method	**Without having Reserves for Discount on Creditors A/c**	**With Reserves for Discount on Creditors A/c**
Rule	Transfer discount received as per TB, to the credit side of P&L A/c	Transfer Discount received as per TB, to the reserve account. Maintain reserves up to desired amount
Discount received	Sundry Creditors A/c Dr. To Discount Received	Sundry Creditors A/c Dr. To Discount Received
Tfr of Disc received	Discount Received A/c Dr. To Profit and Loss A/c	Discount Received A/c Dr. To Reserve for discount on creditors
Creating reserves	There is no such requirement	Reserves for discount on creditors Dr. To Profit and Loss A/c
Treatment in Balance sheet	Not applicable	Closing balance of Reserve for discount on Creditors A/c is shown on liabilities side as reduction from sundry creditors.

<u>Note:</u> Provision for discount on creditors is often not provided in keeping with principle of conservatism.

11. GOODS USED OTHER THAN FOR SALE

	Situation	**Journal Entry**	**Treatment in financial Statement**
1.	Goods withdrawn by Proprietor for personal use	Drawings A/c Dr. To Purchases A/c	Reduce from capital in B/ sheet Purchases reduced in Trading A/c
2.	Goods given away as charity/ donation	Donation / Charity A/c Dr. To Purchases A/c	Add to donation / charity A/c Purchases reduced in Trading A/c
3.	Goods distributed as free sample	Sample/Advertisement A/c Dr. To Purchases A/c	Add to samples/advt. in P/L A/c Purchases reduced in Trading A/c

4.	Goods used for repairs and maintains of business premises or machinery	Repairs & Maintenance A/c Dr. To Purchases A/c	Add to repairs & maint. in P&L Purchases reduced in Trading A/c
5.	Goods used in business, for construction of building or machinery	Building/Machinery A/c Dr. To Purchases A/c	Add to Assets Cost in B/ sheet Purchases reduced in Trading A/c

12. OTHER MISC. ITEMS

	Adjustment	Journal entry	Treatment in Trading and P&L A/c	Treatment in Balance sheet
1.	Stock of stationery, advertisement Material, etc.	Stock of stationery, advertisement Material Dr. To Expenses A/c	Reduce from respective expense on debit side of P&L A/c	Assets side under ''current assets''
2.	Interest on capital	Interest on capital A/c Dr. To Capital	Show in debit side of P&L A/c	Add to capital A/c on the liabilities Side.
3.	Interest on drawings	Capital A/c Dr. To Interest on drawings	Show in credit side of P&L A/c.	Reduce from capital A/c on liabilities side

ACCOUNTING TREATMENT – INCOME –TAX

	Sole Proprietorship Firms	Partnership Firms
Nature of Expenses	Income –Tax is considered as a personal expense of the proprietor	Income Tax relating to the firm is considered just like any other expense
Treatment	Income Tax is debited to capital account	Income Tax is debited to P&L A/c
Journal Entry	(a) For payment of Tax during the year: Income –Tax A/c Dr. To Cash/ Bank (b) For transfer to Capital A/c at year end: Capital A/c Dr. To Income-Tax A/c	(a) For payment of Tax during the year: Firm Income –Tax A/c Dr. To Cash/ Bank (b) For provision for tax at year end: Profit & Loss A/c Dr. To Provision for taxation
Effect on Balance sheet	Capital account is reduced to the extent of Income-Tax paid.	If Tax Amount paid > Provision for Taxation:- The difference is shown as ''Receivable'', i.e., Current Asset If Provision for Taxation > Tax Amount paid:- The difference is shown as '' Payable'', i.e. Current Liability

Note: In case of partnership firms, if the partners' Personal Income tax is paid out of the firm's resources, it should be treated as drawings and should be debited to their capital account individually.

Question

Mr. Ravi gives you the following trial balance and some other information:

Trial Balance as on 31st March, 2021

Particulars	Debit (Rs.)	Credit (Rs.)
Capital Account		6,50,000
Sales		9,70,000
Purchases	4,30,000	
Opening Inventory	1,10,000	
Freights Inward	40,000	
Salaries	2,10,000	
Other Administration Expenses	1,50,000	
Furniture	3,50,000	
Trade receivables and Trade payables	2,10,000	1,90,000
Returns	20,000	12,000
Discounts	19,000	9,000
Bad Debts	5,000	
Investments in Government Securities	1,00,000	
Cash in Hand and Cash at Bank	1,87,000	
Total	**18,31,000**	**18,31,000**

(i) Closing Inventory was Rs. 1,80,000; (ii) Depreciate Furniture @ 10% p.a. Prepare final accounts & pass opening journal entry as on 01.04.2021

Solution

Books of Ravi

Trading Account for the year ended 31st March, 2021

Particulars	Amount	Amount	Particulars	Amount	Amount
To Opening Inventory		1,10,000	By Sales	9,70,000	
To Purchases	4,30,000		Less Return Inward	(20,000)	9,50,000
Less: Return Outward	(12,000)	4,18,000	By Closing Inventory		1,80,000
To Freight Inwards		40,000			
To Gross Profit (Bal. Fig.)		5,62,000			
		11,30,000			**11,30,000**

Profit & Loss Account for the year ended 31st March, 2021

Particulars	Amount	Particulars	Amount
To Salaries	2,10,000	By Gross Profit	5,62,000
To Administration expenses	1,50,000	By Discount received	9,000
To Discount allowed	19,000		
To Bad debts	5,000		
To Depreciation (3,50,000*10%)	35,000		
To Net Profit (Bal. Fig.)	1,52,000		
	5,71,000		**5,71,000**

Balance Sheet as on 31.03.2021

Liabilities	Amount	Amount	Assets	Amount	Amount
Capital	6,50,000		Furniture	3,50,000	
Add: Net profit	1,52,000	8,02,000	Less: Depreciation	(35,000)	3,15,000
Trade payables		1,90,000	Closing Inventory		1,80,000
			Trade receivables		2,10,000
			Investment in Govt Sec.		1,00,000
			Cash in Hand and Bank		1,87,000
		9,92,000			**9,92,000**

Opening Entry (01.04.2021)

Date	Particulars		L.F.	Debit	Credit
01.04	Furniture A/c	Dr.		3,15,000	
	Inventory A/c	Dr.		1,80,000	
	Trade receivables A/c	Dr.		2,10,000	
	Investment in Govt Sec. A/c	Dr.		1,00,000	
	Cash and Bank A/c	Dr.		1,87,000	
	To Trade Payables A/c				1,90,000
	To Capital A/c				8,02,000
	(Being the balances brought forward)				

Question

The following is the Trial Balance of Hari as at 31st December, 2021:

	Dr. (Rs.)	Cr. (Rs.)
Hari's Capital Account	-	76,690
Stock 1st January, 2021	46,800	-
Sales	-	3,89,600
Returns Inwards	8,600	-
Purchases	3,21,700	-
Returns Outwards	-	5,800
Carriages Inwards	19,600	-
Rent & Taxes	4,700	-
Salaries & Wages	9,300	-
Sundry Debtors	24,000	-
Sundry Creditors	-	14,800
Bank Loan @14% p.a.	-	20,000
Bank Interest	1,100	-
Printing and Stationary Expenses	14,400	-
Bank Balance	8,000	-
Discount Earned	-	4,440
Furniture & Fittings	5,000	-
Discount Allowed	1,800	-
General Expenses	11,450	-
Insurance	1,300	-
Postage & Telegram Expenses	2,330	-
Cash Balance	380	-
Travelling Expenses	870	-
Drawings	30,000	-
	5,11,330	**5,11, 330**

The following adjustments are to be made:

a) Included amongst the Debtors is Rs. 3,000 due from Ram and included among the Creditors Rs. 1,000 due to him.
b) Provision for Bad and Doubtful Debts be created at 5% and for Discount @ 2% on Sundry Debtors.
c) Depreciation on Furniture & Fittings @ 10% shall be written off.
d) Personal Purchases of Hari amounting to Rs. 600 had been recorded in the Purchases Day Book.
e) Interest on Bank Loan shall be provided for the whole year.
f) A quarter of the amount of Printing and Stationery Expenses is to be carried forward to the next year.
g) Credit Purchase Invoice amounting to Rs. 400 had been omitted from the Books.
h) Stock on 31.12.2021 was Rs. 78,600.

<u>Prepare:</u>

(i) Trading & Profit and Loss Account for the year ended 31.12.2021 and
(ii) Balance Sheet as on 31st December, 2021.

Solution

Trading and Profit and Loss Account of Mr. Hari

Particulars		Amount	Particulars		Amount
To Opening Stock		46,800	By Sales	3,89,600	
To Purchases	3,21,700		Less : Returns	(8,600)	3,81,000
Add: Omitted Invoice	400		By Closing Stock		78,600
Less: Returns	(5,800)				
Less: Drawing	(600)	3,15,700			
To Freight & Carriage		19,600			
To Gross Profit c/d		77,500			
		4,59,600			**4,59,600**
To Rent and taxes		4,700	By Gross Profit b/d		77,500
To Salaries and wages		9,300	By Discount		4,440
To Bank Interest	1,100				
Add: Due	1,700	2,800			
To Printing & Stationery	14,400				
Less: Prepaid	(3,600)	10,800			
To Discount allowed		1,800			
To General Expenses		11,450			
To Insurance		1,300			
To Postage & Telegram Expenses		2,330			
To Traveling Expenses		870			
To Provision for Bad Debts (New)		1,150			
To Provision for Discount on Debtors		437			
To Depreciation on Furniture & Fittings		500			
To Net Profit tfd. to Capital A/c		34,503			
		81,940			**81,940**

Balance Sheet of Hari
as at 31st December, 2021

Liabilities		Amount	Assets		Amount
Capital	76,690		Furniture and Fittings	5,000	
Add: Net Profit	34,503		Less: Dep.	(500)	4,500
Less: Drawings (Cash 30,000+Goods 600)	(30,600)	80,593	Sundry Debtors(24,000-1,000) Less: Prov. for D/D	23,000 (1,150)	
Bank Loan		20,000		21,850	
Bank Interest Due		1,700	Less: Provision for discount	(437)	21,413
Sundry Creditors [1]		14,200	Stock		78,600
			Prepaid: Printing & Stationery		3,600
			Bank Balance		8,000
			Cash Balance		380
		1,16,493			**1,16,493**

Working Note (1):

Sundry Creditors Balance as per Trial Balance	14,800
Less : Set off in respect of Ram	(1,000)
	13,800
Add : Purchases Invoice which were omitted	400
	14,200

Question

The following are the balances extracted from the books of Shri Raghuram as on 31.03.2021, who carries on business under the name and style of M/s Raghuram and Associates at Chennai:

	Dr. (Rs.)	Cr. (Rs.)
Capital A/c		14,11,400
Purchases	12,00,000	
Purchase Returns		18,000
Sales		15,00,000
Sales Returns	24,000	
Freight Inwards	62,000	
Carriage Outwards	8,500	
Rent of Godown	55,000	
Rates and Taxes	24,000	
Salaries	72,000	
Discount allowed	7,500	
Discount received		12,000
Drawings	20,000	
Printing and Stationery	6,000	
Insurance premium	48,000	
Electricity charges	14,000	
General expenses	11,000	
Bank charges	3,800	
Bad debts	12,200	
Repairs of Motor vehicle	13,000	
Interest on loan	4,400	
Provision for Bad-debts		10,000
Loan from Mr. Rajan		60,000
Sundry creditors		62,000
Motor vehicles	1,00,000	
Land and Buildings	5,00,000	
Office equipment	2,00,000	
Furniture and Fixtures	50,000	
Stock as on 31.03.2020	3,20,000	
Sundry debtors	2,80,000	
Cash at Bank	22,000	
Cash in Hand	16,000	
	30,73,400	**30,73,400**

Prepare Trading and Profit and Loss Account for the year ended 31.03.2021 and the Balance Sheet as at that date after making provision for the following:

(a) Depreciate Building by 5%, Furniture & Fixtures by 10%, Office Equipment by 15% and Motor Car by 20%.
(b) Value of stock at the close of the year was Rs. 4,10,000.
(c) One month rent for godown is outstanding.
(d) Interest on loan from Rajan is payable @ 10% per annum. This loan was taken on 01.07.2020
(e) Reserve for bad debts is to be maintained at 5% of Sundry debtors.
(f) Insurance premium includes Rs. 42,000 paid towards proprietor's life insurance policy and the balance of the insurance charges cover the period from 01.04.2020 to 30.06.2021.

Solution

M/s Raghuram & Associates

Trading and Profit and Loss Account for the year ended 31st March, 2021

Particulars		Amount	Particulars		Amount
To Opening Stock		3,20,000	By Sales	15,00,000	
To Purchases	12,00,000		Less: Return	(24,000)	14,76,000
Less: Returns	(18,000)	11,82,000	By Closing Stock		4,10,000
To Freight		62,000			
To Gross Profit c/d		3,22,000			
		18,86,000			**18,86,000**
To Salaries		72,000	By Gross Profit b/d		3,22,000
To Rent	55,000		By Discount Received		12,000
Add: O/s Rent	5,000	60,000			
To Provision for Doubtful Debts (WN-1)		16,200			
To Rent and Taxes		24,000			
To Discount Allowed		7,500			
To Carriage outwards		8,500			
To Printing and stationery		6,000			
To Electricity charges		14,000			
To Insurance premium (W.N. 1)		4,800			
To Depreciation (W.N. 2)		80,000			
To General expenses		11,000			
To Bank Charges		3,800			
To Interest on loan	4,400				
Add: O/s Interest	100	4,500			
To Motor car expenses (Repairs)		13,000			
To Net profit tfd to Capital Account		8,700			
		3,34,000			**3,34,000**

Balance Sheet of M/s Raghuram & Associates
(as at 31st March, 2021)

Liabilities		Amount	Assets		Amount
Capital Account			Land & Building	5,00,000	
Opening Balance	14,11,400		Less: Dep.	(25,000)	4,75,000
Add: Profit	8,700		Motor Vehicles	1,00,000	
Less: Drawings	(20,000)		Less: Dep.	(20,000)	80,000
Less: Prop. Ins Prem.	(42,000)	13,58,100	Office equipment	2,00,000	
Loan from Rajan	60,000		Less: Dep.	(30,000)	1,70,000
Add: O/s Interest	100	60,100	Furniture & Fixture	50,000	
Sundry Creditors		62,000	Less: Dep.	(5,000)	45,000
O/s Rent		5,000	Closing Stock		4,10,000
			Sundry Debtors	2,80,000	
			Less: Prov. for D/D	(14,000)	2,66,000
			Prepaid insurance (W.N. 1)		1,200
			Cash at Bank		16,000
			Cash in Hand		22,000
		14,85,200			**14,85,200**

Working Notes:

1. Insurance premium

Insurance premium as given in trial balance	48,000
Less: Personal premium	(42,000)
Less: Prepaid for 3 months (6,000*3/15)	(1,200)
Transfer to Profit and Loss A/c	**4,800**

2. Depreciation

On Building (5% of 5,00,000)	25,000
On Motor Vehicles (20% of 1,00,000)	20,000
On Furniture & Fittings (10% of 50,000)	5,000
On Office Equipment (15% of 2,00,000)	30,000
	80,000

3. Interest on Loan

Interest on Loan (60,000*10%*9/12)	4,500
Less: Interest as per Trial Balance	(4,400)
Amount Outstanding	**100**

4. Provision for Doubtful Debts Account

Particulars	Amount	Particulars	Amount
To Bad Debts A/c	12,200	By Balance b/d	10,000
To Balance c/d (2,80,000)*5%	14,000	By P&L A/c (Bal. Fig.)	16,200
	26,200		**26,200**

Question

From the following Trial Balance of Shri Shivam as on 31st March, 2021, you are required to prepare a Trading and Profit and Loss Account for the year ended 31st March, 2021 and Balance Sheet as on that date, after making the necessary adjustments as mentioned hereunder:

Particulars	Dr. (Rs.)	Cr. (Rs.)
Shivam's capital	-	1,60,000
Shivam's drawings	24,000	-
Furniture and Fixtures	8,000	-
Plant and Machinery	60,000	-
Patents (ten years from 1.4.2020)	40,000	-
Stock on 1.4.2020	40,000	-
Purchases	1,70,000	-
Salaries	14,800	-
Wages	30,000	-
Sundry debtors	20,400	-
Sales	-	2,64,000
Cash in Hand	13,250	-
Land	28,350	-
Loan from Shyam (at 6% from 1.10.2020)	-	20,000
Postage and Fax	3,000	-
Rent, rates and taxes	7,200	-
Bad debts	800	-
Sundry Creditors	-	24,000
Discount	-	1,200
Carriage Inward	400	-
Interest on loan	300	-
Insurance	1,600	-
Travelling expenses	1,000	-
Sundry Expenses	600	-
Cash at Bank	20,500	-
Bank overdraft	-	15,000
Total	**4,84,200**	**4, 84,200**

Adjustments:

a) Stock as on 31.3.2021 is valued at Rs. 30,000.
b) A new machine was installed on 1st April, 2020 for Rs. 3,000. No entry in this respect was passed in the books. Wages of Rs. 1,000 paid for installing the machine were debited to Wages account.
c) Of the Sundry debtors, Rs. 200 are bad and are to be written off. You are required to maintain a provision for doubtful debts @ 5% debtors and provision for discount on debtors @ 2%.
d) Goods costing Rs. 2,000 were given away as free samples for publicity.
e) Depreciate Plant and Machinery at 20% per annum and Furniture & Fixtures at 10% per annum.
f) On 1.4.2020, machinery of the value of Rs. 10,000 was destroyed by fire and the insurance claim settled at Rs. 8,000 was credited to Machinery account.
g) Goods costing Rs. 1,000 were sent to a customer for Rs. 1,200 on 30th March, 2021 on sale or return basis. This was recorded as actual sales.

Solution

In the books of Shri Shivam
Trading Profit & Loss A/c for the year ended 31.3.21

Particulars		Amount	Particulars		Amount
To Opening Stock		40,000	By Sales	2,64,000	
To Purchases		1,70,000	(-) Sale or Return basis	(1,200)	2,62,800
To Wages (30,000-1,000)		29,000	By Goods given as free sample		2,000
To Carriage Inward		400	By Closing Stock		
To Gross Profit		56,400	-Given	30,000	
			-With Customer	1,000	31,000
		2,95,800			**2,95,800**
To Depreciation:			By Gross Profit		56,400
Furniture & Fixtures	800		By Discount		1,200
Plant & Machinery	12,400	13,200			
To Loss by fire		2,000			
To Patent written-off		4,000			
To Salaries		14,800			
To Bad Debts	800				
(+) Additional	200	1,000			
To Prov. for Doubtful Debts		950			
To Prov. for Discount		361			
To Postage & Fax		3,000			
To Rent, Rates & Taxes		7,200			
To Interest on loan					
Paid	300				
(+) Outstanding	300	600			
To Insurance		1,600			
To Travelling exp.		1,000			
To Sundry Exp.		600			
To Advertisement(Goods as Sample)		2,000			
To Net profit transfer to Capital A/c		5,289			
		57,600			**57,600**

Balance Sheet as at 31.3.2021

Liabilities		Amount	Assets		Amount
Capital			Furniture & Fittings	8,000	
Op. Balance	1,60,000		(-) Depreciation (800)		7,200
(-) Drawings	(24,000)		Plant & Mach. (Note-1)	62,000	

(+) NP	5,289	1,41,289	(-) Depr. (12,400)		49,600
Creditor for Plant & Mach. [Note-]		3,000	Patent	40,000	
Loan from Shyam	20,000		(-) Written-off	(4,000)	36,000
(+) Interest	300	20,300	Land		28,350
Sundry Creditors		24,000	Stock (30,000+1,000)		31,000
Bank Overdraft		15,000	Debtors [Note-2]	19,000	
			(-) Prov. for D/D	(950)	
				18,050	
			(-) Prov. for discount	(361)	17,689
			Cash in hand		13,250
			Cash in Bank		20,500
		2,03,589			**2,03,589**

Working Notes:

(1) Computation of Plant & Machinery

Balance Given	60,000
(+) New Machinery (1.4.20) (3,000+1,000)	4,000
(-) Machinery Sold	(2,000)
	62,000

(2) Computation of Debtors

Balance	20,400
(-) Bad Debts	(200)
(-) Sale or return	(1,200)
	19,000

SIGNIFICANCE OF MANUFACTURING ACCOUNT

(a) The Manufacturing Account shows the total cost of manufacturing the finished products, with appropriate details and classifications of **Cost.**
(b) The debits to this account consist of the cost of materials consumed, Manufacturing Wages and Expenses incurred directly or indirectly on manufacture.
(c) This Account is relevant only for Manufacturing Entities, and is not applicable for Trading Entities.

MANUFACTURING ACCOUNT

Manufacturing Account of ....for the year ended.........

Particulars	Rs.	Particulars	Rs.
To Material consumed: Opening stock of raw materials **Add:** Purchases of Raw Materials **Less:** Closing Stock of Raw Materials To Direct Manufacturing Wages To Direct Expenses **(Note 1)** To Production Overheads **(Note 2)** To Opening Stock of WIP		By Closing stock of WIP By Net Factory Cost of Production Trfd to Trading A/c (bal. fig) By NRV/ Sale Value of By-Products, if any **(Note 3)**	
Total		**Total**	

Trading Account of ....for the year ended.........

Particulars	Rs.	Particulars	Rs.
To Opening stock of finished goods To Manufacturing account – Cost of Prodn To Gross Profit c/d to P&L Account		By Sales By Closing stock of finished goods	
Total		**Total**	

<u>Note:1</u>
Direct Manufacturing Expenses are costs, other than Materials and Wages, which are incurred for a specific product/ service.
Examples: (a) Royalty for use of license/ technology, (b) Hire Charges of Plant / Equipment, if based on units produced.

<u>Note:2</u>
These are called factory Overheads/ Production Overheads/ Works Overheads/ Manufacturing Overheads etc.
It is the Total **Indirect costs** (Indirect Materials + Indirect Labour + Indirect Expenses) which cannot be linked directly to units produced.
Examples: Factory Rent, Depreciation on Machinery, Supervisor's Salary, Consumables like Oils, Lubricants, etc.

<u>Note:3</u>
By-Product is an incidental product, arising during the production operations, having some saleable value.
Examples: Molasses is the by-product in sugar manufacturing
Net Realizable Value of By-product is credited to this account

Question

Mr. Sahil runs a factory which produces motor spares of export quality. The following details were obtained about his manufacturing expenses for the year ended on 31.3.2021.

W.I.P.	- Opening	3,90,000
	- Closing	5,07,000
Raw Materials	- Purchases	12,10,000
	- Opening	3,02,000
	- Closing	3,10,000
	- Returned	18,000
	- Indirect material	16,000
Wages	- direct	2,10,000
	- Indirect	48,000
Direct expenses	- Royalty on production	1,30,000
Indirect Expenses	- Repairs and maintenance	2,30,000
	- Depreciation on factory shed	40,000
	- Depreciation on plant & machinery	60,000
By-product at selling price		20,000

You are required to prepare Manufacturing Account of Mr. Sahil for the year ended on 31.3.2021.

Solution

Books of Mr. Sahil

Manufacturing Account for the year ended 31st March, 2021

Particulars	**Amount**	**Amount**	**Particulars**	**Amount**
To Opening W.I.P.		3,90,000	By Closing W-I-P	5,07,000
To Raw Material Consumed:			By- products (at S.P.)	20,000
Opening inventory	3,02,000		By Trading A/c-	17,81,000
Purchases	12,10,000		Cost of finished goods transferred (Bal. Fig.)	
Less: Return	(18,000)			
Less: Closing inventory	(3,10,000)	11,84,000		
To Direct Wages		2,10,000		
To Direct expenses:				
Royalty		1,30,000		
To Manufacturing Overhead:				
Indirect Material	16,000			
Indirect Wages	48,000			
Repairs & Maintenance	2,30,000			
Dep. on Factory Shed	40,000			
Dep. on Plant & Machinery	60,000	3,94,000		
		23,08,000		**23,08,000**

COMPANY ACCOUNTS

DEFINITION –COMPANY

Companies Act, 2013	A Company mean company which is formed and incorporated under the Companies Act, 2013 or an existing company formed and registered under any of the previous company laws.
Hanay	A Company is an Artificial Person created by law, having a Separate Entity, with a Perpetual Succession and a Common Seal.

CHARACTERISTIC/FEATURES OF A COMPANY

Feature	Explanation
Artificial Person	• A Company comes into existence by the operation of law. • By sanction of law, a Company is granted certain rights and obligations as that of a person. Thus, company is an artificial person, incorporated under law.
Separate Legal Entity	• A Company is a separate legal entity & artificial person known by its own name • A Company is distinct and separate from the members who constitute it. • A Company can contract, sue & be sued in its incorporated name & capacity.
Person, not Citizen	• A Company is not a citizen either under — (a) the Constitution of India or (b) the Citizenship Act • The Constitution provides certain fundamental rights to its citizens. A Company cannot enjoy the citizenship rights and duties as are enjoyed by natural citizens
Perpetual Succession	• A Company is an artificial person and has a separate legal entity. • The shares of a Company being transferable, members may change during the lifetime of the company. • Company goes on forever & continues to exist till it is wound up & dissolved.
Common Seal	• Common Seal is the official signature of a Company. The Company's name is engraved on the Seal. • The Articles of Association may provide for the documents that require the signature of the Company, i.e. the Common Seal. Where any document is affixed with the Common Seal, it amounts to being signed by the Company.
Ownership Vs Management	• The Board of Directors is the elected representative body of the Shareholders of the Company and manages the affairs of the Company. • Generally, every Shareholder / Member does not participate in the day-to-day affairs of working and administration of the Company. Hence, Ownership of Company is different from that of its Management.
Right of Access	The right of the shareholders of a company to inspect its books of account, with the exception of books open for inspection under the Statute, is governed by the AOA
Limited Liability	The liability of every shareholder of a company is limited to the amount he has agreed to pay to the company on the shares allotted to him. If such shares are fully paid-up, he is subject to no further liability.
Transferability of Shares	The capital is contributed by the shareholders through the subscription of shares. Such shares are transferable by its members except in case of a private limited company, which may have certain restrictions on such transferability.
Maintenance of Books	A limited company is required by law to keep a prescribed set of account books and any failure in this regard attracts penalties.
Periodic Audit	A company has to get its accounts periodically audited through the chartered accountants appointed for the purpose by the shareholders on the recommendation of board of director

TYPES OF COMPANIES

TYPE	EXPLANATION
Government Company	Any company in which not less than 51% of Paid -Up Capital of a Company is held by the Central Government, or State Government(s), or partly by Central Government and partly by one or more state Governments.
Foreign Company	Any company or body corporate incorporated outside India which – a) has a place of business in India whether by itself or through an agent physically or through electronic mode; and b) conducts any business activity in India in any other manner.
Private company	A company which by its articles— a) restricts the right to transfer its shares; b) except in case of One Person Company, limits the number of its members to 200 c) prohibits any invitation to the public to subscribe for any securities of the company. Shares of a Private Company are not listed on Stock Exchange
Public Company	A company which is not a private company; provided that a company which is a subsidiary of a company, not being a private company, shall be deemed to be public company for the purposes of this Act even where such subsidiary company continues to be a private company in its articles.
One Person Company	A company which has only one person as a member
Small Company	A company, other than a public company, - a) paid-up share capital of which does not exceed 50 lakh rupees or such higher amount as may be prescribed which shall not be more than 5 crore rupees; or b) turnover of which as per its last profit and loss account does not exceed 2 crore rupees or such higher amount as may be prescribed which shall not be more than 20 crore rupees
Listed Company	A company which has any of its securities listed on any recognised stock exchange.
Unlisted Company	The company, whose shares are not listed on any recognised stock exchange
Unlimited Company	A company not having any limit on the liability of its members
Company limited by Shares	Company having the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them.
Company limited by Guarantee	A company having the liability of its members limited by the memorandum to such amount as the members may respectively undertake to contribute to the assets of the company in the event of its being wound up.
Holding Company	In relation to one or more other companies, means a company of which such companies are subsidiary companies.
Subsidiary company	A company in which the holding company: a) controls the composition of the Board of Directors; or b) exercises or controls more than one-half of the total share capital either at its own or together with one or more of its subsidiary companies:

MAINTENANCE OF BOOKS OF ACCOUNTS (Sec 128 of Companies Act, 2013)

Every company shall prepare and keep at its ***registered office*** books of account and other relevant books and papers and financial statement for every financial year which give a ***true and fair view*** of the state of the affairs of the company, including that of its branch office or offices, if any, and explain the transactions effected both at the registered office and its branches and such books shall be kept on ***accrual basis*** and according to the ***double entry system*** of accounting:

PREPARATION OF FINANCIAL STATEMENTS

Under Section 129 of the Companies Act, 2013, the financial statements shall give a true and fair view of the state of affairs of the company or companies, comply with the notified accounting standards and shall be in the form or forms as may be provided for different class or classes of companies, as prescribed in Schedule III.

The Board of Directors of the company shall lay **financial statements** at every annual general meeting of a company which include:-

a) **Balance Sheet** as at the end of the period, and

b) **Profit and Loss Account** for that period.
[Note: For a Company not carrying on business for profit, an Income and Expenditure Account shall be laid at that AGM, instead of the P & L Account.]

c) **Cash flow statement** for the financial year

d) **Statement of changes in equity**, if applicable; and

e) **Any explanatory note** annexed to, or forming part of, any document referred above

Provided that the financial statement, with respect to One Person Company, small company and dormant company, may not include the cash flow statement.

Requisites of Financial Statements It shall give a true and fair view of the state of affairs of the company as at the end of the financial year.

Provisions Applicable

(1) Specific Act is Applicable

For instance any

a) Insurance company
b) Banking company or
c) Any company engaged in generation or supply of electricity or
d) Any other class of company for which a Form of balance sheet or Profit and loss account has been prescribed under the Act governing such class of company

(2) In case of all other companies

Balance Sheet as per Form set out in Part I of Schedule III and Statement of Profit and Loss as per Part II of Schedule III

PART I – BALANCE SHEET

Name of the Company…………………….

Balance Sheet as at ………………………

	PARTICULARS	Note No.	Figures as at the end of current Reporting period	Figures as at the end of previous reporting period
A.	**EQUITY AND LIABILITIES**			
1.	Shareholder's funds			
a	Share capital			
b	Reserves and surplus			
c	Money received against share warrants			
2.	Share application money pending allotment			
3.	Non-Current Liabilities			
a	Long-term borrowings			
b	Deferred tax liabilities (Net)			
c	Other long term liabilities			
d	Long-term provisions			
4.	Current Liabilities			
a	Short-term borrowings			
b	Trade payables			
c	Other current liabilities			
d	Short-term provisions			
	TOTAL			
B.	**ASSETS**			
1.	Non-Current Assets			
a	Property, Plant & Equipment			
i.	Tangible assets			
ii.	Intangible assets			
iii.	Capital work-in-Progress			
iv.	Intangible assets under development			
b	Non-current investments			
c	Deferred tax assets (net)			
d	Long-term loans and advances			
e	Other non-current assets			
2.	Current Assets			
a	Current investments			
b	Inventories			
c	Trade receivables			
d	Cash and cash equivalents			
e	Short-term loans and advances			
f	Other current assets			
	TOTAL			

SHARES- ISSUE, FORFEITURE AND RE-ISSUE

SHARE

Meaning	"Share" is the basic unit which the Capital of a Company is divided. *Example*: A company with a total Capital of Rs 1 crore is divided into 1 Lakh units of Rs 100 each. Each unit of Rs 100 is called a Share of the Company.

KINDS OF SHARES RECOGNIZED IN THE COMPANIES ACT, 2013

The Share Capital of a Company limited by Shares can only be of two kinds-

1. **Equity Share Capital –** (a) with Voting rights, or (b) with differential rights as to dividend, voting or otherwise in accordance with the prescribed Rules
2. **Preference Share Capital,** i.e. Priority for Dividend at Fixed Rate + Priority for repayment of Capital.

DIFFERENT TYPES OF PREFERENCE SHARE CAPITAL

1. Cumulative and Non-Cumulative Preference Shares

	Cumulative Preference Shares	Non-Cumulative Preference shares
a)	Dividend is at fixed rate, but keeps on accumulating until it is fully paid	Dividend is at a fixed rate, but does not accumulate for future years.
b)	Dividend is payable even out of future profits, if current year's profits are insufficient	If no dividend is declared in a year, the right to receive such dividend for that year expires
c)	Arrears of fixed Cumulative dividend shown in the Balance sheet as a Contingent Liability	There is no contingent liability

Note: Cumulative Preference shareholders will get voting rights if dividend remains in arrear for not less than 2 years

2. Redeemable and Irredeemable Preference Shares

	Redeemable Preference Shares	Irredeemable Preference Shares
a)	These are issued on the condition that the company will repay the same after a fixed period or even at company's discretion. This repayment is called Redemption	These are Preference shares, which are redeemable only at the time of winding up of the company
b)	Companies can issue only this category of preference shares. Also, the redemption period shall be a maximum of 20 years. Exception: Infrastructure Projects	No Company limited by shares shall issue – • Irredeemable Preference Shares, or • Preference Shares redeemable after the expiry of 20 years from the date of issue

3. Participating and Non-Participating Preference Shares

	Participating Preference Shares	Non-Participating Preference Shares
a)	In addition to a fixed dividend, the holders of these Shares have the right to participate in the surplus profits, if any, after the Equity Shareholders have been dividend at a stipulated rate.	Here, only a fixed rate of dividend is paid every year, without any additional rights in surplus profits.
b)	In the event of winding-up of the Company, the holders have the right to receive a pre-determined proportion of surplus, after the Equity Shareholders have been paid off towards their Capital.	In case of winding-up of the Company, the holders of these Shares are not entitled to any additional rights in the surplus on winding-up.

4. Convertible and Non-Convertible Preference Shares

	Convertible Preference Shares	Non-Convertible Preference Shares
a)	These Shares give the right to the holder to get them converted into Equity Shares **at their option,** and according to the terms and conditions of their issue.	There is no right to the holder, to get his holding converted into Equity Shares.

PREFERENCE SHARES AND EQUITY SHARES

BASIS	PREFERENCE SHARES	EQUITY SHARES
Definition	Shares that carry a Preferential Right as to payment of – (a) Dividend, and (b) Repayment of Capital.	Shares that are not Preference Shares are called Equity Shares.
Return	Fixed Rate	Based on profits available for distribution.
Dividend	Priority over Equity Dividend, i.e. paid first.	After Payment of Preference Dividend.
Repayment of Capital	Paid before repayment of Equity Capital.	Paid after entire Preference Capital is repaid.
Arrears of Dividend	Generally accumulates unless specifically said to be non-cumulative.	No accumulation of Unpaid Dividend. No Profits means no Dividend.
Redemption	Redeemable as per terms of issue and provisions of Act.	Not Redeemable till winding-up. Even in winding-up, will be repaid after Preference Shares.
Voting Rights	Generally restricted. Carries right to vote on all matters if dividend remains unpaid for the prescribed period.	Unrestricted, i.e. Holders can vote at any matters at any Meeting, or the Shares may be issued with varying voting rights.
Control/ Management	No right to take part in Management.	Equity Shareholders are the real owners, hence have a right to control the Management of Company.

DIFFERENT TYPES OF SHARE CAPITAL

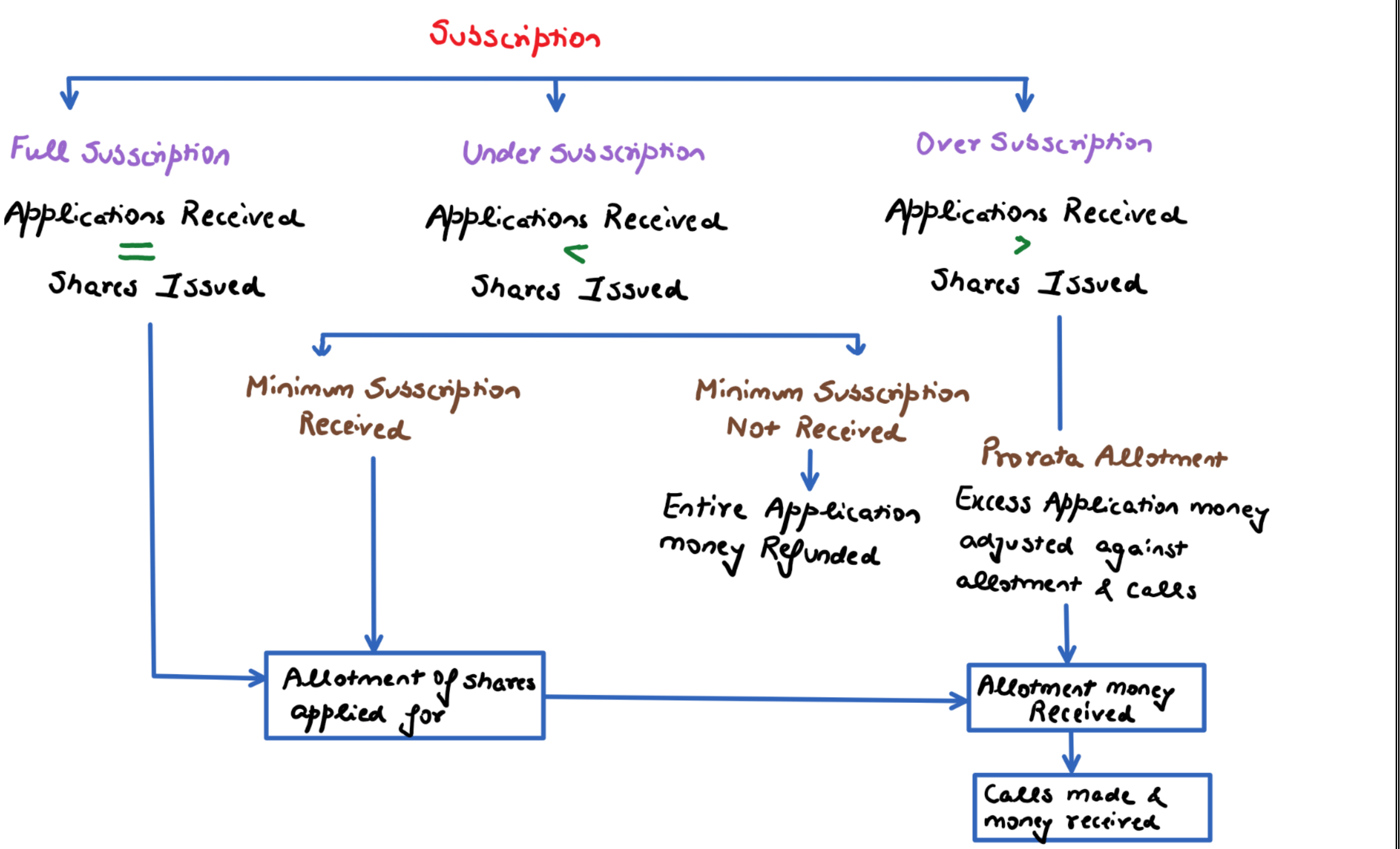
ITEM	EXPLANATION
Authorised Share Capital	• It is the amount of Share Capital which can be raised by the Company. • The Authorised Share Capital is also known as the "Registered Capital" or "Nominal Capital" and is given in the Memorandum of Association. • Authorised Capital is shown in the Balance Sheet at Nominal Value (Face Value). • *Example*: Authorised Capital=10,000 Shares of ₹ 100 each, Total=₹ 10,00,000.
Issued Share Capital	• It represents that part of Authorised Share Capital which has been given or issued or offered to Shareholders. • Issued Capital includes Shares issued for- (i) Cash, and (ii) Consideration other than cash, to Promoters and Others. • Issued Share Capital is shown in the Balance Sheet at Nominal Value (Face Value). • *Example*: Issued Capital= 9,000 Shares of ₹ 100, each, Total= ₹ 9,00,000 . **Note**: The remaining portion of Authorised Capital, which is not issued for cash or other consideration is called as Unissued Capital. It is not shown in the Balance Sheet.

Subscribed Share Capital	• Subscribed Capital is the part of Issued Capital which has been subscribed (i.e. applied for) by the public/ Shareholders, and allotted by the Company. • *Example*: Out of 9,000 Shares issued; 8,500 Shares are subscribed by public. **Note**: The remaining portion of Issued Capital, which is not subscribed, is not shown in the Balance Sheet.
Called up Share capital	• Companies generally receive the Issue Price of Shares in installments, e.g. Application stage, Allotment stage, First Call, Second Call, etc. • The portion of the Face Value of Shares which a Company has demanded or called from Shareholders is known as "Called-Up Capital". • The Balance portion which the Company has decided to call / demand in future is called as Uncalled Capital. • *Example*: Out of ₹ 100 per Share, the Company has called up ₹ 70 per Share. In such case, the Uncalled Capital is ₹ 30 per Share.
Paid-Up Capital	• It is that portion of called up capital which has been actually paid by shareholders • The unpaid portion is called "Unpaid Calls" or "Calls in Arrears". • So, Paid Up Capital = Called Up Capital Less Call in Arrears. • *Example*: If out of ₹ 70 per Share Called up, only ₹ 60 has been paid by some shareholders, the remaining ₹ 10 per Share constitutes Calls in Arrears.
Reserve Capital	• Company may decide by passing a resolution, that a certain portion of its Subscribed Uncalled Capital shall be called up only in the event of winding-up / liquidation of the Company. • That portion is called Reserve Capital. It is not shown in the Balance Sheet. • Reserve Capital is different from Capital reserve, Capital reserves (created out of capital profits) are part of 'Reserves and Surplus' and refer to those reserves which are not available for declaration of dividend

DISCLOSURE REQUIREMENTS - SHARE CAPITAL OF A COMPANY

Share Capital should be disclosed in a Company's Balance Sheet as under:

Particulars	Amount
Authorised: …. …. Shares of ₹ ... each	
Issued:… ... Shares of ₹ ... each	
Subscribed: ……... Shares of ₹ .. each (Various classes of capital should be distinguished while stating the above particulars)	
Called up & Paid Up: … … Shares of ₹ ... each [of the above Shares …. Shares are allotted as fully paid up for consideration other than cash, …. Shares are allotted as fully paid up by way of Bonus Shares] Less: Call unpaid: Add : Forfeited Shares (amount originally paid up)	



PROVISIONS RELATING TO MINIMUM SUBSCRIPTION

1. **Meaning:** Minimum Subscription is the minimum amount stated in the Prospectus, which must be raised by the issue of Share Capital to start with.

2. If the Company does not receive the Minimum Subscription of 90% of the issue, the entire subscription shall be refunded to the applicants within prescribed time period.

3. As per Section 39 of the Companies Act 2013, application money must be atleast 5% of the face value of shares. However, as per SEBI Regulations, the minimum application moneys to be paid by an applicant alongwith the application money shall not be less than 25% of the issue price.

ISSUE OF SHARES AT PREMIUM [SEC. 52]

1. **Meaning:** Premium refers to the excess of the Share Issue Price over its Face Value / Par Value. A Company can issue Shares at a premium, i.e. at a price above its Face Value.
   Example: If Share of Face Value Rs 100 is issued at a price of Rs 120, there is a premium of Rs 20
2. **Accounting Treatment:**
   The Premium Amount is credited to the **"Securities Premium Account".** This Account is shown on the Liabilities Side of the Company's Balance Sheet under the heading "Reserves and Surplus".
3. **Application of Securities Premium:** Securities Premium Account can be used only for —
   (a) Issuing **Fully Paid Bonus Shares** to Members.
   (b) Writing—off the **Preliminary Expenses** of the Company.
   (c) Writing off the — (i) Expenses Incurred, or (ii) Commission Paid, or (iii) Discount Allowed, on the Issue of Securities or Debentures of the Company.
   (d) Providing for the **premium payable** on redemption of a Redeemable Preference Shares or Debentures of the Company.
   (e) For the purchase of own shares or other securities.

PROVISIONS REGARDING THE ISSUE OF SHARES AT DISCOUNT [SEC. 53]

According to Section 53 of the Companies Act, 2013, a Company cannot issue shares at a discount except in the case of issue of sweat equity shares (issued to employees and directors). Thus any issue of shares at discount shall be void.

JOURNAL ENTRIES RELATING TO ISSUE OF SHARES

	TRANSACTION	JOURNAL ENTRY
1.	Receipt of Application Money	Bank A/c (Amount actually received) Dr. To Share Application A/c (Amount actually received)
2a.	Full/Under Subscription	Share Application A/c Dr. To Share Capital A/c [Shares allotted x Application Money] To Securities Premium A/c* (Share allotted x Premium / share) *(If Premium Amount is collected at the time of Application itself)
2b.	Oversubscription	Share Application A/c Dr. (Amount received) To Share Capital A/c [Shares allotted x Application Money] To Securities Premium A/c* (Share allotted x Premium /share) To Share Allotment A/c (Adjusted with Allotment) To Share Calls -in -Advance A/c (Adjusted with Calls) To Bank A/c (Refund) *(If Premium Amount is collected at the time of Application itself)
3.	Allotment money due	Share Allotment A/c Dr. To Share Capital A/c [Shares allotted x Allotment money due] To Securities Premium A/c* [Shares allotted x Premium / Share] *(If the Premium Amount is at the time of Allotment)
4.	Receipt of Share Allotment Money	Bank A/c (Amount received) Dr. To Share Allotment A/c
5.	Making Calls, i.e. Call Money due	Share ... (First or Second or Final)... Call A/c Dr. To Share Capital A/c [Shares allotted x Call Money due]
6.	Receipt of Share Call Money	Bank A/c (Amount received) Dr. To Share ...... Call A/c

Note: If question specifically asks preparation of Cash Book, then all the entries relating to Cash/Bank Account are not passed in journal and to be shown in Cash Book only.

CALLS IN ARREARS

1. **Meaning:** Calls in Arrears is the money remaining unpaid by the shareholder on the calls raised by the Company in respect of the shares held by him.
2. **Disclosure:** Calls in Arrears always have a Debit Balance and are shown as a deduction from called up capital to arrive at paid up value of the Share Capital on Liabilities Side of the Balance Sheet.
3. **Interest:** The Company can recover interest on the amount of calls in arrears from the date it became due till the when the call is received at the rate of 10% p.a. (Table F).
4. **Waiver of Interest:** The Directors may also be empowered to waive the Interest on Calls in Arrears, subject to certain conditions laid down in the Articles.

CALLS IN ADVANCE

1. **Meaning:** Calls in Advance is the surplus money received by the Company from the allottees, i.e. its Shareholders.
2. **Calls in Advance:** A Company, if permitted by its Articles, may accept from members either the whole or part of amount remaining unpaid on any shares held by him as Calls in Advance.
3. **No Voting Rights:** The Member shall not be entitled to any voting rights on Calls in Advance, until the same becomes presently payable and duly appropriated. Shareholders are not entitled for any dividend on calls in advance
4. **Disclosure:** Calls in Advance will always have a Credit Balance and will be shown under the Liabilities Side (Other Current Liabilities). It is not added to the amount of Paid -Up Capital.
5. **Interest:** The Company is liable to pay interest on the amount of Calls in Advance from the date of receipt till the when the Call is due for payment, at the rate of 12% p.a. (Table F)

JOURNAL ENTRIES

	CALLS -IN –ARREARS	
1.	Transfer of non - receipt of Share Allotment/ Call Money	Calls in Arrears A/c Dr. To Share Allotment / Share ...... Call A/c (This Journal Entry is optional. The amount may also be left in the Share Allotment/Share …..Calls A/c)
2.	Receipt of Calls in Arrears	Bank A/c Dr. To Calls in Arrears A/c (If this account was opened)
3.	Interest on Calls in Arrears	Shareholders' A/c Dr. To Interest on Calls -in -Arrears A/c
4.	Receipt of Interest on Calls -in –Arrears	Bank A/c Dr. To Shareholders' A/c
	CALLS -IN –ADVANCE	
1.	Receipt of Calls -in-Advance	Bank A/c Dr. To Calls -in -Advance A/c
2.	Adjusting Calls -in-Advance	Calls -in -Advance A/c Dr. To Particular Call A/c
3.	Interest on Calls- in –Advance	Interest on Calls -in -Advance A/c Dr. To Shareholders' A/c
4.	Payment of Interest on Calls -in- Advance	Shareholders' A/c Dr. To Bank A/c

FORFEITURE OF SHARES

1. **Meaning:** Forfeit = Taking away of property, on breach (non -fulfilment) of a condition. In the context of Shares, Forfeiture of Shares refers to the action taken by the Company, to cancel the Shares.
2. **Situation:** When Shareholders fail to pay Allotment or Call Money due, the Directors may forfeit the Shares in the bonafide interests of the Company, and in accordance with the Articles of Association. Proper Notice should be sent to the defaulting Shareholder, before forfeiture.
3. **Effect:** When Shares are forfeited, the title of such Shareholder is extinguished, but the amount paid by him till such forfeiture, is not refunded to him. The Shareholder has no further claim on the Company. The amount actually received from Shareholder is transferred to "Shares Forfeited A/c".
4. **Treatment:** Till Forfeited Shares are re -issued, the amount is shown as an addition to Share Capital, on the Liabilities Side of the Balance Sheet.

RE-ISSUE OF FORFEITED SHARES

1. **Sale, not Allotment:** Re -issue of Forfeited Shares is **not an allotment**, it is only a Sale. So, the Company need not file a Return of Allotment with the Registrar of Companies.
2. **Auction Sale:** After forfeiture, the Forfeited Shares vest in the Company in the Company, for the purpose of sale. The Company is under an obligation to dispose it off, generally by auction.
3. **Loss on Re -issue:** Loss on Re -issue shall be debited to "Forfeited Shares" A/c. Condition for Re -issue: Loss on Re -issue of Forfeited Shares should not exceed the Forfeited Amount, i.e. amount paid by Original Allottee, excluding premium, if any.)
4. **Surplus:** Surplus arising on Re -issue of Forfeited Shares (i.e. Forfeited Amount > Loss on Re -issue), should be transferred to Capital Reserve A/c.
5. **Re-issue at Premium:** When Forfeited Shares are re-issued at a price higher than its Face Value, the excess amount should be credited to Securities Premium A/c.

	TRANSACTION	JOURNAL ENTRY
	FORFEITURE OF SHARES	
1.	Forfeiture of Shares Issued at Par	Share Capital A/c (to the extent called) Dr. To Shares Forfeited A/c (to the extent amount received) To Calls in Arrears (to the extent amount called up & unpaid) (or alternatively Share Allotment A/c or Share ...... Call A/c)
2.	Forfeiture of Shares Issued at Premium - premium fully collected	Share Capital A/c (to the extent called - excluding Premium) Dr. To Shares Forfeited A/c (to the extent amount received) To Calls in Arrears (to the extent amount called up and unpaid (or alternatively Share Allotment A/c or Share ...... Call A/c)
3.	Forfeiture of Shares Issued at Premium - premium not fully collected	Share Capital A/c (to the extent called excluding Premium) Dr. Securities Premium A/c (Premium amount on Shares forfeited) Dr. To Shares Forfeited A/c (to the extent amount received) To Calls in Arrears (to the extent amount called up and unpaid (or alternatively Share Allotment A/c or Share ...... Call A/c)
	Note: When Shares are originally issued at a Premium, and the Premium has been collected in full, the Securities Premium A/c should not be reversed.	
	RE -ISSUE OF SHARES FORFEITED	
1.	Re -issue of Forfeited Shares	Bank A/c (Shares Reissued x Reissue Price) Dr. Shares Forfeited A/c (to the extent discount given) Dr. To Share Capital A/c (Shares Reissued x Paid up Value)
2.	Transfer of Share Forfeited A/c Balance on Reissued Shares	Shares Forfeited A/c Dr. To Capital Reserve A/c

SHARES ISSUED FOR CONSIDERATION OTHER THAN CASH

1. **Meaning:** A Company can issue shares for valuable Consideration other than Cash. For example, Shares may be issued to - (a) Vendors towards payment of Purchase Consideration, (b) Promoters towards reimbursement of Preliminary Expenses incurred by them for incorporation, (c) Underwriters towards payment of Underwriting Commission, etc.
2. **Disclosure:** Shares issued for Consideration other than Cash shall be separately disclosed in the Balance Sheet of Company, as required by Part I of Schedule III.
   Within specied time of allotment, the company must produce before the Registrar a written contract of sale of service in respect of which shares have been allotted.

JOURNAL ENTRIES

1.	Recording Purchase of Machinery, Assets etc.	Machinery / Assets A/c (in case of assets purchased) Dr. To Liabilities A/c To Vendor's A/c (Difference if any to be transferred to Goodwill/Capital Reserve A/c)
2.	Allotment of Shares to the Vendor	Vendor's A/c Dr. To Share Capital (Nominal Value of Shares issued) To Securities Premium (if issued at Premium)

Issue of shares for consideration other than cash

- Asset Purchased (A)
- Business Purchased (B)
  - Purchase Consideration not given (B1)
  - Purchase Consideration given (B2)

$$\text{No. of shares issued} = \frac{\text{Purchase Consideration}}{\text{Issue Price}}$$

Dividend

* Calculated on Paid up capital.

  Paid up Capital = Called up capital − Calls in Arrears.

* Calls in Advance not taken into Consideration.

Question

X Ltd. invited applications for 10 lakhs shares of Rs. 100 each payable as follows:

	Rs.
On Application	20
On Allotment (on 1st May, 2020)	30
On First Call (on 1st Oct., 2020)	30
On Final Call (on 1st Feb., 2021)	20

All the shares were applied for and allotted. A shareholder holding 20,000 shares paid the whole of the amount due along with allotment. Journalise the transactions, assuming all sums due were received. Interest was paid to the shareholder concerned on 1st February, 2021

Solution

Books of X Limited

Date	Particulars		L.F.	Debit (in Lakhs)	Credit (in Lakhs)
1.05.20	Bank A/c	Dr.		200	
	To Share Application A/c				200
	(Being Application money on 10 Lakh shares at Rs. 20 per share received)				
01.05.20	Share Application A/c	Dr.		200	
	To Share Capital A/c				200
	(Being amount transferred to Capital Account)				
01.05.20	Share Allotment A/c	Dr.		300	
	To Share Capital A/c				300
	(Being allotment money due)				
01.05.20	Bank A/c	Dr.		310	
	To Share Allotment A/c				300
	To Calls in Advance				10
	(Being allotment money and also the two calls (Rs. 30 and Rs.20) on 20,000 share received)				
01.10.20	Share First Call A/c	Dr.		300	
	To Share Capital A/c				300
	(Being first call money due)				
01.10.20	Bank A/c	Dr.		294	
	Calls in Advance A/c	Dr.		6	
	To Share First Call A/c				300
	(Receipt of the first call on 9.80 lakh shares)				
01.02.21	Share Final Call A/c	Dr.		200	
	To Share Capital A/c				200
	(Being final call money due)				
01.02.21	Bank A/c	Dr.		196	
	Calls in Advance A/c	Dr.		4	
	To Share Final Call A/c				200
	(Receipt of the moneys due on final call on 9.80 lakhs shares)				
01.02.21	Interest on Calls in Advance A/c	Dr.		0.66	
	To Shareholder A/c				0.66
	(Being interest on call in advance made due)				
01.02.21	Shareholder A/c	Dr.		0.66	
	To Bank A/c				0.66
	(Being interest paid)				

Working Note:

The interest on calls in advance paid @ 12% on

a) 6,00,000 (first call) from 1st May to 1st Oct., 2020–5 months = 6,00,000*12%*5/12 = 30,000
b) 4,00,000 (final call) from 1st May to 1st Feb., 2021–9 months = 4,00,000*12%*9/12 = 36,000

Total Interest Amount Due= **66,000**

Question

Y Ltd. forfeited 1,000 equity shares of Rs. 10 each, Rs. 7 called-up, issued at a premium of 20% (to be paid at the time of allotment) for non-payment of allotment money of Rs. 4 per share (including premium) and first call of Rs. 2 per share. Out of these, 600 shares were re-issued as fully paid-up for Rs. 8.50 per share.

Pass the journal entries for forfeiture and re-issue of shares.

Solution

Books of Y Ltd.

Date	Particulars		L.F.	Debit	Credit
-	Equity Share Capital A/c (1,000*7)	Dr.		7,000	
	Securities Premium A/c (1,000*2)	Dr.		2,000	
	(1,000*4) To Share Allotment A/c				4,000
	(1,000*2) To Share First Call A/c				2,000
	(1,000*3) To Share Forfeited A/c				3,000
	(Being the forfeiture of 1,000 shares Rs.7 each being called up for non-payment of allotment & first call)				
-	Bank A/c (600*8.50)	Dr.		5,100	
	Share Forfeited A/c (600*1.50)	Dr.		900	
	To Share Capital A/c				6,000
	(Being re-issue of 600 shares at Rs. 8.50 per share paid-up as Rs. 10)				
	Share Forfeited A/c	Dr.		900	
	To Capital Reserve A/c				900
	(Being profit on re-issue transferred to Capital Reserve)				

Working Note: Calculation of amount to be transferred to Capital Reserve

Forfeited amount per share = Rs. 3,000/1,000	3
Loss on re-issue = Rs. 10 – Rs. 8.50	(1.50)
Surplus per share re-issued	1.50
Transferred to capital Reserve Rs. 1.50 * 600	900

Question

B Limited issued 50,000 equity shares of Rs. 10 each payable as Rs. 3 per share on applications, Rs. 5 per share (including Rs. 2 as premium) on allotment and Rs. 4 per share on call. All these shares were subscribed.

Money due on all shares was fully received except from X, holding 1000 shares who failed to pay the allotment and call money and Y, holding 2000 shares, failed to pay the call money. All these 3,000 shares were forfeited. Out of forfeited shares, 2,500 shares (including whole of X's shares) were subsequently re-issued to Z as fully paid up at a discount of Rs. 2 per share.

Pass necessary journal entries in the books of B limited. Also prepare Balance Sheet and notes to accounts of the company.

Solution

Journal of B Ltd.

S. No.	Particulars	L.F	Debit	Credit
1	Bank A/c Dr.		1,50,000	
	To Equity Share Application A/c			1,50,000
	(Being application money received Rs.3 per share on 50,000 shares)			
2	Equity Share Application A/c Dr.		1,50,000	
	To Equity share Capital A/c			1,50,000
	(Being Application money transferred)			
3	Equity Share Allotment A/c Dr.		2,50,000	
	To Equity share capital A/c			1,50,000
	To Securities Premium A/c			1,00,000
	(Being allotment money due on 50,000 shares @ 5 including Rs.2 Premium)			
4	Bank A/c Dr.		2,45,000	
	To Equity Share Allotment A/c			2,45,000
	(Being Allotment received on 49,000 shares @ 5 each)			
5	Equity share call A/c Dr.		2,00,000	
	To Equity Share Capital A/c			2,00,000
	(Being Call money due on 50,000 shares @ 4 each)			
6	Bank A/c Dr.		1,88,000	
	To Equity share call A/c			1,88,000
	(Being call money received on 47000 shares @ 4 each)			
7	Equity share capital A/c Dr.		30,000	
	Securities Premium A/c Dr.		2,000	
	To Equity share Allotment A/c			5,000
	To Equity share Call A/c			12,000
	To Share forfeiture A/c			15,000
	(Being 3000 shares forfeited due to non payment or Allotment & Call)			
8	Bank A/c Dr.		20,000	
	Share Forfeiture A/c Dr.		5,000	
	To Equity share capital A/c			25,000
	(Being Reissued 2,500 shares @ 8 per share)			
9	Share forfeiture A/c Dr.		7,000	
	To Capital reserve A/c			7,000
	(Being excess forfeited amount on 2500 share transferred)			

W.N

(1) Calculation of Amount transferred to Capital Reserve :

Forfeited Amount on 2500 Shares.

X
Forfeited Amount
On 1,000 Shares @ 3 = 3,000

Y
Forfeited Amount on
1500 shares @ 6 = 9000

Total Forfeited Amount = 12,000
Less: Reissued Discount = (5,000)
Transfer to Capital Res. = 7,000

Example:

Prorata Allotment

Application Invited = 100000 shares

Received 300000 shares

Applied	Allotted
100000	3 for every 5
150000	1 for every 5
10000	Full
40000	Nil
300000	

Stages

Application : 3

Allotment : 5

Call : 2

Adjustment till allotment & balance refunded

Applied	Allotted	Money Rec.	Application	Allotment	Call	Refund
100000	60000	300000	180000	120000	-	-
150000	30000	450000	90000	150000	-	210000
10000	10000	30000	30000	-	-	-
40000	Nil	120000	-	-	-	120000
300000	100000	900000	300000	270000		330000

Share Forfeiture in Case of Prorata Allotment

Case 1:

Shares Applied = 1000

Shares Allotted = 600

Application = 2

Allotment = 3+1 (Sec. Prem.)

Call = 5

No Allotment & Call. Shares forfeited

Applied	Allotted	Money Rec.	Application	Allotment
1000	600	2000	1200	800

Forfeiture:

Share capital A/c —Dr		6000	(600X10)
Sec. Premium A/c - Dr		600	(600X1)
To Share Allotment		1600	(600 X4) - 800
To Share call		3000	600X5
To Share Forfeiture		2000	

Case 2:

Shares Applied = 1000 Application = 2

Shares Alloted = 600 Allotment = 1+1 (Sec. Prem.)

Call = 7

No Allotment & Call. Shares forfeited

Applied	Allotted	Money Rec.	Application	Allotment
1000	600	2000	1200	800

Forfeiture:

Share capital A/c —Dr

Sec. Premium A/c - Dr

To Share Allotment

To Share call

To Share Forfeiture