CHAPTER 3

INSURANCE CLAIMS

Question – 1.

A fire engulfed the premises of a business of M/s Preet on the morning of 1st July 2018. The building, equipment and stock were destroyed and the salvage recorded the following:

Building – 4,000; Equipment – 2,500; Stock – 20,000. The following other information was obtained from the records saved for the period from 1st January to 30th June 2018:

Sales	*11,50,000*
Sales Returns	*40,000*
Purchases	*9,50,000*
Purchases Returns	*12,500*
Cartage inward	*17,500*
Wages	*7,500*
Stock in hand on 31st December, 2017	*1,50,000*
Building (value on 31st December, 2017)	*3,75,000*
Equipment (value on 31st December, 2017)	*75,000*
Depreciation provision till 31st December, 2017 on:	
Building	*1,25,000*
Equipment	*22,500*

No depreciation has been provided since December 31st 2017. The latest rate of depreciation is 5% p.a. on building and 15% p.a. on equipment by straight line method. Normally business makes a profit of 25% on net sales. You are required to prepare the statement of claim for submission to the Insurance Company.

Solution

Memorandum Trading Account for the Period from 1.1.2018 to 30.6.2018

Opening Stock (1.1.2018)	1,50,000	By Sales 1150000 *Less:* Sales Returns (40,000)	11,10,000
To Purchases 950000 *Less:* Returns 12500	9,37,500		
To Cartage Inwards	17,500	By Closing Stock (Bal. Fig.)	2,80,000
To Wages	7,500		
To Gross Profit (11,10,000 x 25%)	277500		

Stock Destroyed Account

To Trading Account	2,80,000	By Stock Salvaged Account	20,000
		By Balance c/d (for claim)	260000

Statement of Claim

Items	Cost	Depreciation	Salvage	Claim
A	**B**	**C**	**D**	**E**
Stocks	280000	-	20000	260000
Building	375000	125000 + 9375	4000	236625
Equipments	75000	22500 + 5625	2500	44375

Question – 2.

On 27th July, 2017, a fire occurred in the godown of M/s. Vijay Exports and most of the stocks were destroyed. However goods costing ` 5,000 could be salvaged. Their firefighting expenses were amounting to `1,300.

From the salvaged accounting records, the following information is available relating to the period from 1.4.2017 to 27.7.2017:

1.	*Stock as per balance sheet as on 31.3.2017*	*`63,000*
2.	*Purchases (including purchase of machinery costing `10,000*	*`2,92,000*
3.	*Wages (including wages paid for installation of machinery ` 3,000)*	*`53,000*
4.	*Sales (including goods sold on approval basis amounting to ` 40,000. No approval has been received in respect of 1/4th of the goods sold on approval)*	*`4,12,300*
5.	*Cost of goods distributed as free sample*	*`2,000*

Other Information:

(i) While valuing the stock on 31.3.2017, ` 1,000 had been written off in respect of certain slow moving items costing `4,000. A portion of these goods were sold in June, 2017 at a loss of `700 on original cost of `3,000. The remainder of these stocks is now estimated to be worth its original cost.

(ii) Past record shows the normal gross profit rate is 20%.

(iii) The insurance company also admitted firefighting expenses. The Company had taken the fire insurance policy of 55,000/- with the average clause.

You are required to compute the amount of claim of stock destroyed by fire, to be lodged to the Insurance Company. Also prepare Memorandum Trading Account for the period 1.4.2017 to 27.7.2017 for normal and abnormal items.

Question – 3.

The premises of Anmol Ltd. caught fire on 22nd January 2017, and the stock was damaged. The firm makes account up to 31st March each year. On 31st March, 2016 the stock at cost was Rs 6,63,600 as against Rs 4,81,100 on 31st March, 2015.

Purchases from 1st April, 2016 to the date of fire were Rs 17,41,350 as against Rs 22,62,500 for the full year 2015-16 and the corresponding sales figures were Rs 24,58,500 & Rs 26,00,000 respectively. You are given the following further information:

(i) ***In July, 2016, goods costing Rs 50,000 were given away for advertising purposes, no entries being made in the books.***

(ii) ***During 2016-17, a clerk had misappropriated unrecorded cash sales. It is estimated that the defalcation averaged Rs 1,000 per week from 1st April, 2016 until the clerk was dismissed on 18th August, 2016.***

(iii) ***The rate of gross profit is constant.***

You are required to calculate the value of stock in hand on the date of fire with the help of above information.

Solution

1. Ascertainment of rate of gross profit for the year 2015-16

Trading A/c for the year ended 31-3-2016

	Rs		**Rs**
To Opening stock To Purchases To Gross profit	4,81,100 22,62,500 5,20,000 **32,63,600**	By Sales By Closing stock	26,00,000 6,63,600 **32,63,600**

Rate of gross profit = GP ÷ Sales × 100

5,20,000 ÷ ×100 26,00,000 = 20%

Memorandum Trading A/c for the period from 1-4-2016 to 22-01-2017

	Rs	**Rs**		**Rs**	**Rs**
To Opening stock		6,63,600	By Sales		24,58,500
To Purchases Less: Goods used for	17,41,350		Add: Unrecorded cash sales (W.N.)	20,000	24,78,500
advertisement	(50,000)	16,91,350	By Closing stock		3,72,150
To Gross profit (20% of Rs 24,78,500)				4,95,700	
		28,50,650			28,50,650

Estimated stock in hand on the date of fire was Rs 3,72,150.

Working Note: Cash sales defalcated by the Accountant:

Defalcation period = 1.4.2016 to 18.8.2016= 140 days

Since, 140 days / 7 weeks = 20 weeks

Therefore, amount of defalcation = 20 weeks × Rs 1,000 = Rs 20,000.

Question – 4.

A fire occurred on 1st February, 20X2, in the premises of Pioneer Ltd., a retail store and business was partially disorganized upto 30th June, 20X2. The company was insured under a loss of profits for ` 1,25,000 with a six months period indemnity. From the following information, compute the amount of claim under the loss of profit policy.

Actual turnover from 1st February to 30th June, 20X2	***80,000***
Turnover from 1st February to 30th June, 20X1	***2,00,000***
Turnover from 1st February, 20X1 to 31st January, 20X2	***4,50,000***
Net Profit for last financial year	***70,000***
Insured standing charges for last financial year	***56,000***
Total standing charges for last financial year	***64,000***
Turnover for the last financial year	***4,20,000***

The company incurred additional expenses amounting to 6,700 which reduced the loss in turnover. There was also a saving during the indemnity period of 2,450 in the insured standing charges as a result of the fire.

There had been a considerable increase in trade since the date of the last annual accounts and it has been agreed that an adjustment of 15% be made in respect of the upward trend in turnover.

Solution

Computation of the amount of claim for the loss of profit

Reduction in Turnover	**Amount**
Turnover from 1st Feb X1 to 30th June X1	200000
Add – 15% Expected Increase	30000

	230000
Less Actual Turnover from 1 st Feb X2 to 30 th June X2	
Short Sales	150000
Gross Profit on Reduction in Turnover @ 30% on 150000 (see working note 1)	45000

Add: Additional Exp. Lower of

(1) Actual – 6700/-

(2) Additional Exp x $\frac{\text{GP on adjusted annual Turnover}}{\text{GP as above + Uninsured Standing Charges}}$

$6700 \times \frac{155250}{163250}$

6372/-

(3) G.P. on sales generated by additional expenses — not available

Therefore lower of above is 6372/-

Total Loss – 45000 + 6372 = 51372 – Saving in Insured Standing Charges

Amount of Claim before application of Avg. Clause – 48922

Avg Clause $= \frac{\text{Amount of Policy x Amount of Claim}}{\text{GP on Annual Turnover}}$

= 125000 x 48922/155250 = **39390/-**

Working Notes:

(1) Rate of Gross Profit for Last Financial Year:

Net Profit	70000
Add – Insured Standing Charges	56000
	126000
Turnover for the last FY	420000
Rate of GP	126 / 420 x 100 = 30%

(2) Annual Adjusted Turnover:

Turnover from 1st Feb 20x1 to 31st Jan 20x2	450000
Add – 15% Expected Increase	67500
	517500
GP on 517500 @ 30%	155250
Standing Charges not insured (64000 – 56000)	8000
Gross profit plus non – insured standing charges	**163250**

Question – 5.

S & M Ltd. give the following Trading and Profit and Loss Account for year ended 31st December, 20X1:

Trading and Profit and Loss Account for the year ended 31st December, 20X1

Opening Stock	*50000*	*Sales*	*800000*
Purchases	*300000*	*Closing Stock*	*70000*
Wages (20000 for Skilled Lab)	*160000*		
Manufacturing Exp	*120000*		
Gross Profit	***240000***		
Office Advertisement	*60000*	***Gross Profit***	***240000***
Advertising	*20000*		
Selling Exp	*40000*		
Commission on Sales	*48000*		

Carriage on Sales	16000		
Net Profit	**56000**		

The company had taken out policies both against loss of stock and against loss of profit, the amounts being 80,000 and 1,72,000. A fire occurred on 1st May, 20X2 and as a result of which sales were seriously affected for a period of 4 months. You are given the following further information:

(a) Purchases, wages and other manufacturing expenses for the first 4 months of 20X2 were 1,00,000, 50,000 and 36,000 respectively.

(b) Sales for the same period were 2,40,000.

(c) Other sales figures were as follows:

From 1st Jan X1 to 30th April 20X1	300000
From 1st May X1 to 30th August 20X1	360000
From 1st May X2 to 30th August 20X2	60000

(d) Due to rise in wages, gross profit during 20X2 was expected to decline by 2% on sales.

(e) Additional expenses incurred during the period after fire amounted to 1,40,000. The amount of the policy included 1,20,000 for expenses leaving 20,000 uncovered.

Ascertain the claim for stock and for loss of profit.

All workings should form part of your answers.

Solution:

Question – 6.

From the following particulars, you are required to calculate the amount of claim for Buildwell Ltd., whose business premises was partly destroyed by fire:

Sum insured (from 31st December 20X1)	***4,00,000***
Period of indemnity	***12 months***
Date of damage	***1st January, 20X2***
Date on which disruption of business ceased	***31st October, 20X2***

The subject matter of the policy was gross profit but only net profit and insured standing charges are included.

The books of account revealed:

(a) The gross profit for the financial year 20X1 was 3,60,000.

(b) The actual turnover for financial year 20X1 was 12,00,000 which was also the turnover in this case.

(c) The turnover for the period 1st January to 31st October, in the year preceding the loss, was 10,00,000.

During dislocation of the position, it was learnt that in November-December 20X1,

there has been an upward trend in business done (compared with the figure of the previous years) and it was stated that had the loss not occurred, the trading results for 20X2 would have been better than those of the previous years.
The Insurance company official appointed to assess the loss accepted this view and adjustments were made to the pre-damaged figures to bring them up to the estimated amounts which would have resulted in 20X2.

The pre-damaged figures together with agreed adjustments were:

Period	**Pre-damaged fig.**	**Adjustment to be added**	**Adjusted Standard Turnover**
January	*90000*	*10000*	*100000*
Feb to Oct.	*910000*	*50000*	*960000*
Nov. to Dec.	*200000*	*10000*	*210000*
	1200000	***70000***	***1270000***
Gross Profit	***360000***	***46400***	***406400***

Rate of Gross Profit 30% (actual for 20X1), 32% (adjust ed for 20X2).
Increased cost of working amounted to 1,80,000.
There was a clause in the policy relating to savings in insured standard charges during the indemnity period and this amounted to 28,000. Standing Charges not covered by insurance amounted to 20,000 p.a. The annual turnover for January was nil and for the period February to October 20X2 8,00,000

Solution:

Student Notes:-