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CA FOUNDATION JUNE'24

Accounting

Paper - 1

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CAFC RS June 24 : Principles and Practice of Accounting

INDEX

Chapter		Page
No.	**Name**	**No.s**
1	Accounting Process (Journal / Subsidiary Books, Ledger, Trial Balance)	3 to 36
2	Bank Reconciliation Statement (BRS)	41 to 64
3	Rectification of Errors (ROE)	69 to 87
4	Bills of Exchange and Promissory Notes (Trade Bills and Accommodation Bills)	92 to 114
5	Depreciation and Amortisation	119 to 152
6	Inventories	157 to 178
7	Preparation of Final Accounts of Sole Proprietors (Non-Manufacturing Entities and Manufacturing Entities)	183 to 217
8	Accounts from Incomplete Records (Single Entry System) (Statement of Affairs Method and Conversion Method)	222 to 235
9	Financial Statements of Not-for-Profit Organisations (NPO)	240 to 258
10	**Partnership and LLP Accounts**	
a)	Introduction to Partnership and LLP Accounts	263 to 279
b)	Goodwill : Concept, Valuation and Accounting Treatment	284 to 299
c)	Admission of a Partner	304 to 314
d)	Retirement and Death of a Partner	319 to 338
e)	Dissolution of Partnership Firms and LLP	343 to 366
11	**Company Accounts**	
a)	Introduction : Issue, Forfeiture & Reissue of Shares	371 to 401
b)	Issue of Debentures	406 to 417
c)	Redemption of Preference Shares	422 to 431
d)	Accounting for Bonus Issue and Right Issue	436 to 452
e)	Redemption of Debentures	457 to 467
12	Theoretical Framework	472 to 523

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Introduction to Journal

Journal is the **Primary book of account** in which financial transactions are **first recorded** in a chronological order i.e. in the sequence they are entered into.

The basic book of accounting is called Journal. Precisely, it is the **book of prime entry** which means **Day Book**. Trader records his total daily transactions in it.

Transactions are recorded in the Journal book from **accounting vouchers** that are prepared on the basis of **source vouchers** / documents.

Journal is **sub-divided into** a number of subsidiary books which are as follows.

	Name of the Journal	Transactions to be recorded
I)	Cash Book	Cash, Bank & Discount (TCCB)
		Cash & Bank / Cash or Bank & Discount (DCCB)
		Simple Cash Book / Single Column Cash Book (SCCB)
II)	Purchases Book	**Credit** Purchases of Goods
	Sales Book	**Credit** Sales of Goods
	Purchases Return Book	Purchases Returns (out of **credit** purchases)
	Sales Return Book	Sales Returns (out of **credit** sales)
III)	Journal Proper	All other transactions

Notes :

1. **I)** Cash Book includes Petty Cash Book as well
2. **II)** are also called Goods Journals
3. **I) & II)** are called Special Journals, as specific transactions as defined are recorded in each of these.
4. **Besides above,** Bills Receivable Book & Bills Payable Book are also maintained if the volume of acceptances received & acceptances given is high.
5. **III)** Journal proper is also called General Journal , as it records all the remaining transactions which cannot be recorded in any of the above Special Journals.

These **are those transactions** for which separate Journal is **not** prepared as volume of such transactions is relatively low.

Cash Book

Cash Book is a **book of primary entry** in which cash and bank transactions of a business are recorded in chronological order, i.e. as they are entered into.

Recording of transactions in the cash book **takes form of a** ledger account.

In other words, cash books itself serves as cash account and bank account.

Hence, there is **no need to prepare** separate Cash A/c and Bank A/c in ledger.

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^ **Introduction to Ledger**

Ledger is Secondary book of account **or** Principal book of account **or** Book of Final Entry.

After recording the transaction in Journal(s), it is then posted into respective accounts maintained in ledger.

In Ledger, **all** accounts **(Personal, Real, Nominal)** are maintained i.e. A/c's of **all** Assets, Liabilities, Capital - Drawings, Expenses & Incomes are maintained.

The process of transfer of Journal entry to a ledger account is called **Posting**.

* **Ledger Accounts Balances**

1. **Personal Accounts**
   - If Account of any person **shows debit balance**, it means such person is **our Debtor** i.e. money / money's worth is receivable in future **(Assets)**
   - If Account of any person **shows credit balance**, it means such person is **our Creditor** i.e. money / money's worth is payable in future **(Liabilities)**

2. **Real Accounts**

   Real Accounts **shows Debit balance**, which indicates value of property / thing in hand as on date. **(Assets)**

3. **Nominal Accounts**
   - Account of Expenses / Losses **shows Debit balance**, which indicates Expense incurred / Loss suffered till the date in current period.
   - Account of Incomes / Gains **shows Credit balance**, which indicates Income / Profit earned till the date in current period.

** **Depending upon volume, for convenience, Ledger can be bifurcated into 3 parts :**
1) Sales (Debtors) Ledger **2)** Purchases (Creditors) Ledger **3)** General Ledger

^ **Introduction to Trial Balance**

After posting of all the transactions in the Ledger in respective accounts is completed and all accounts are balanced, it becomes necessary to **check the arithmetical accuracy** of the accounting work.

For this purpose, the balance of each and every account in the Ledger is put on a list.

The list so prepared **is called** Trial Balance (TB).

"A Trial balance is **the list** of debit and credit balances, taken out from the Ledger.

It also includes **the balances of Cash and Bank** taken from **the Cash Book**."

Q. 1 : Prepare a Triple Column Cash Book from the following transactions of M/s Raj Agencies and bring down the balance for the start of next month.

Mar-22		(₹)
1	Cash in hand	30,000
2	Cash at bank	1,20,000
2	Paid into bank	10,000
5	Bought Furniture and issued cheque	15,000
8	Purchased goods for cash	5,000
8	Received cash from Mohan	9,800
	Discount allowed to him	200
14	Cash sales	50,000
16	Paid to Lata by cheque	14,500
	Discount received	500
19	Paid into bank	5,000
23	Withdrawn from bank for private expenses	6,000
24	Received cheque from Gupta	14,300
	Allowed him discount	200
26	Deposited Gupta's cheque into bank	
28	Withdrew cash from bank for office use	20,000
30	Paid Rent by cheque	8,000

Q. 2 : The Rough Book of M/s Narain & Co. contains the following for 2022.

Feb-01	Purchased from Brown & Co. on credit:
	5 gross pencils @ ₹100 per gross,
	1 gross register @ ₹240 per doz.
	Less: Trade Discount @10%
Feb-12	Purchased for cash from the Stationery Mart;
	10 gross exercise books @ ₹300 per doz.
Feb-18	Purchased computer for office use from M/s office Goods Co. on credit for
	₹ 30,000
Feb-23	Purchased on credit from The Paper Co.
	5 reams of white paper @ ₹100 per ream
	10 reams of ruled paper @ ₹150 per ream
	Less: Trade Discount @10%
Feb-25	Purchased one dozen gel pens @ ₹15 each from M/s Verma Bros. on credit.

Make out the Purchase Book of M/s Narain & Co. & Show posting in ledger.

(Hint : 1 gross = 12 dozens ; 1 ream = 12 dozens)

^ **Q. 1 : In the books of Raj Agencies**

TRIPLE COLUMN

Date	Particulars (Receipts)	R. No.	L.F.	Discount Allowed	Cash ₹	Bank ₹

CASH BOOK

Date	Particulars (Payments)	V. No.	L.F.	Discount Received	Cash ₹	Bank ₹

^ **Q. 2 : PURCHASE BOOK**

Date	Particulars (Name of Supplier)	Inward Invoice No.	L. F.	Amount (₹)	Amount (₹)
2018					
April					

* **Notes :**

* **Dr.** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

* **Dr.** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

* **Dr.** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

* **Dr.** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

^ **Q. 3 :** The following are some of the transaction of M/s Kishore & Sons of the year 2022 as per their Waste Book. Make out their Sales Book & Post in ledger.

(1) Sold to M/s. Gupta & Verma on credit:
30 Shirt @ ₹ 800 per shirt.
20 trousers @ ₹ 1,000 per trouser.
Less: Trade Discount @ 10%

(2) Sold furniture to M/s. Sehgal & Co. on credit ₹8,000

(3) Sold 50 Shirts to M/s. Jain & Sons @ ₹ 800 per Shirt.

(4) Sold 13 Shirts to Cheap Stores @ ₹ 750 each for cash.

(5) Sold on credit to M/s. Mathur & Jain.
100 Shirts @ ₹ 750 per Shirt ; 10 overcoats @ ₹ 5,000 per overcoat
Less: Trade Discount @ 10%

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^ **Q. 3 :** **SALES BOOK**

Date	Particulars (Name of Customer)	Outward Invoice No.	L. F.	Amount (₹)	Amount (₹)
2018					
April					

* **Notes :**

* **Dr.** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

* **Dr.** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

* **Dr.** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

Dr. **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

^ **Q. 4 :** The following data is given by Mr. S, the owner, with a request to compile only the two personal accounts of Mr. H and Mr. R, in his ledger, for the month of April, 2022

1 Mr. S owes Mr. R ₹15,000; Mr. H owes Mr. S ₹20,000.

4 Mr. R sold goods worth ₹60 000 @ 10% trade discount to Mr. S.

5 Mr. S sold to Mr. H goods priced at ₹30,000.

17 Record a purchase of ₹ 25,000 net from R, which were sold to H at a profit of ₹ 15,000.

18 Mr. S rejected 10% of Mr. R's goods of 4th April.

19 Mr. S issued a cash memo for ₹ 10,000 to Mr. H who came personally for this consignment of goods, urgently needed by him.

22 Mr. H cleared half his total dues to Mr. S, enjoying a 1/2% cash discount (of the payment received, ₹ 20,000 was by cheque)

26 R's total dues (less ₹ 10,000 held back) were cleared by cheque, enjoying a cash discount of 1,000 on the payment made.

29 Close H's Account to record the fact that all but ₹ 5,000 was cleared by him, by a cheque, because he was declared bankrupt.

30 Balance R's Account.

^ **Q. 5 :** One of your clients, Mr. Singhania has asked you to finalise his accounts for the year ended 31st March, 2022. Till date, he himself has recorded the transactions in books of accounts. As a basis for audit, Mr. Singhania furnished you with the following statement. The closing inventory on 31st March, 2022 was valued at ₹ 574.

	Dr. Balance (₹)	Cr. Balance (₹)
Singhania's Capital		1,556
Singhania's Drawings	564	
Leasehold premises	750	
Sales		2,750
Due from customers		530
Purchases	1,259	
Purchases Return	264	
Loan from Bank		256
Trade payables	528	
Trade expenses	700	
Cash at Bank	226	
Bills Payable	100	
Salaries and Wages	600	
Inventories (1.4.2021)		264
Rent and Rates	463	
Sales Return		98
	5,454	**5,454**

Mr. Singhania Claims that he has recorded every transaction correctly as the trial balance is tallied. Check the accuracy of the above trial balance.

^ **Q. 6 : a)** Pass Journal Entries for following transactions in the books of Gamma Bros.

(i) Employees had taken inventory worth ₹ 1,00,000 (Cost price ₹ 75,000) on the eve of Deepawali & the same was deducted from their salaries in the subsequent month.

(ii) Wages paid for erection of Machinery ₹ 18,000.

(iii) Income tax liability of proprietor ₹ 17,000 was paid out of petty cash.

(iv) Purchase of goods from Naveen of the list price of ₹ 2,00,000. He allowed 10% trade discount, Rs. 5,000 cash discount was also allowed for quick payment.

^ **Q. 6 b)** Balance Sheet of Mr. Popatlal, a merchant on 31.03.22 stood as below :

	₹			₹
Capital	2,40,000	Fixed Assets		1,25,600
Trade payables	1,64,000	Inventories		2,06,400
Bank Overdraft	1,46,000	Trade Receivables	1,88,000	
		Less : Provision	(6,200)	1,81,800
		Cash		36,200
	5,50,000			**5,50,000**

Show opening journal entry on 1 st April, 2022 in the books of Mr. Popatlal.

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Q. 7 : Journalise the following transactions. Also state the nature of each account involved in the Journal entry. Following figures are given in ('00)

1. December 1, 2022, Ajit started business with capital ₹ 4,00,000
2. December 3, he withdrew cash for business from the Bank ₹ 2,000.
3. December 5, he purchased goods by making payment through bank ₹ 15,000.
4. December 8, he sold goods for ₹ 16,000 and received payment through bank.
5. December 10, he purchased furniture and paid by cheque ₹ 2,500.
6. December 12, he sold goods to Arvind ₹ 2,400.
7. December 14, he purchased goods from Amrit ₹ 10,000.
8. December 15, he returned goods to Amrit ₹ 500.
9. December 16, he received from Arvind ₹ 2,300 in full settlement.
10. December 18, he withdrew goods for personal use ₹ 1,000.
11. December 20, he withdrew cash from business for personal use ₹ 2,000.
12. December 24, he paid telephone charges ₹ 110.
13. December 26, amount paid to Amrit in full settlement ₹ 9,450.
14. December 31, paid for stationery ₹ 200, rent ₹5,000 and salaries to staff ₹ 2,000 from bank.
15. December 31, goods distributed by way of free samples ₹ 2,000.

Q. 8 : Journalise the following transactions.

i) Purchased goods from Sam for Rs. 40,000 at a trade discount of 10% plus CGST and SGST @ 9% each. Rs. 20,000 was paid immediately and balance payable after 3 months.

ii) Goods costing Rs. 20,000 withdrawn for personal use. Such goods were purchased by paying CGST and SGST @ 9% each.

iii) Paid rent to Gagandeep for Rs. 30,000 plus CGST and SGST 6% each.

iv) Goods costing Rs. 5,000 (before T.D. of 10%) returned to Sam. Such goods were purchased by paying CGST and SGST @ 9% each.

v) Purchased furniture for Rs. 44,800 including IGST @ 12%.

vi) Sold goods to Surjeet for Rs. 28,000 including CGST and SGST @ 6% each.

vii) Received Rs. 25,200 from Surjeet in full settlement of his account of Rs. 28,000.

viii) Sold goods to Kapil for Rs. 30,000 charged IGST @ 12%. Received Rs. 12,000 immediately and balance to be received after one month.

ix) Kapil was allowed rebate of Rs. 5,000 as goods supplied to him were defective. These goods were sold by charging IGST @ 12%.

x) Sold goods to Mukesh at the list price of Rs. 1,50,000 less 20% trade discount and 5% cash discount. Out of the amount due, 60% is received out of which three-fourth is received by cheque.

^ **Goods and Services Tax (GST)**

GST is an Indirect Tax (IDT) levied / charged at prescribed rate on **every supply** of goods & services, by the tax payers registered under GST.
(Supply : Sale of goods & rendering of services)

* GST is levied at the **same** rate on **similar** goods & services across all States & Union Territories. (**Union Territories** : Andaman & Nicobar Islands, Dadra & Nagar Haveli, Chandigarh, Lakshadweep, Daman & diu)
For eg. :
GST is applied on Electronic goods **across India** at the rate of 18%

* Goods & / or Services are grouped in **five categories** for the purpose of levy of GST.
GST is applied on goods &/or services at the **rates as specified** on that category.
The rates prescribed are : 0%, 5%, 12%, 18% & 28%
Rates and types of GST as prescribed by the government are subject to change.

* **Levy (charging) of GST**
GST is of following 3 types / categories
i) CGST : Central GST
ii) SGST : State GST (UTGST : Union Territory GST)
iii) IGST : Integrated GST

* Various relevant transactions are divided into 2 parts for the purpose of levy of GST.

1) GST on transactions with-in the same state (Intra state transactions)
When the supply (sale) of goods &/or services are with-in the same state, **both CGST & SGST**, each, are levied / charged **at half the prescribed rate** for such goods &/or service.
For eg. : If the prescribed rate of GST is 12%,
both CGST & SGST will be charged at 6% each on the value of supply (sale).
CGST will go the CG and SGST will go to the SG.

2) GST on transactions outside the state (Inter state transactions)
When the supply (sale) of goods &/or services are outside the state,
IGST is levied / charged at the prescribed rate for such goods &/or service.
For eg. : If the prescribed rate of GST is 12%, IGST will be charged at 12% on the value of supply (sale).
Though IGST is collected by the CG, Revenue collected under IGST will be divided between CG & SG as per the rates prescribed by the Government.

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* **GST Paid**

GST is paid on purchase of goods &/or services. It is called **Input GST**.

In most cases,
GST paid (Input GST) can be set-off against GST collected (Output GST),
it is accounted for **an Asset** and hence, **Input GST A/c is debited** when such goods &/or services are purchased.

* **GST Collected**

GST is received / collected on sale of goods &/or services. It is called **Output GST**.
Output GST can **never be treated** as our Income.
It is our **Liability** since it is collected by us on behalf of the Government.

Output GST A/c is credited when such goods are sold.

After setting off Input GST against Output GST [**after claiming** Input Tax Credit (ITC)],
excess Output GST is payable to the Government & hence,
it is **Liability** of the business.

* **Reversal / Cancellation of GST paid & debited to Input GST A/c**

i) GST paid & claimed as Input GST is reversed in case of **Purchase Returns**
as, in effect, purchases have reduced.

ii) When goods are **NOT sold further**
eg. Other outgoings of goods
(Goods withdrawn by proprietor for personal use,
Goods distributed as free samples, Goods lost by fire, theft etc.)

* **Reversal / Cancellation of GST received & credited to Output GST A/c**

GST received and credited to Output GST A/c is reversed in case of :
i) Sales Returns, as, in effect, sales have reduced.
ii) Rebate allowed for defective goods

Classification of Accounts

Traditional / English Approach		Account Balance	Modern / American / Accounting Equation Approach
1)	Real A/c's	Debit	1) Assets A/c
2)	Personal A/c's (debtors)		
	Personal A/c's (external creditors)	Credit	2) Liabilities A/c
	Capital A/c (proprietor)		3) Capital A/c
	Drawings A/c (proprietor)	Debit	Drawings A/c (Less from Capital)
3)	Nominal A/c's		
	Expenses and Losses	Debit	4) Expenses A/c
	Incomes and Gains	Credit	5) Incomes / Revenue A/c

Rules of Debit & Credit (Traditional / English Approach)

Personal A/c	Real A/c	Nominal A/c
Debit the Receiver	Debit what Comes in	Debit all Expenses & Losses
Credit the Giver	Credit what Goes out	Credit all Gains & Incomes

Rules of Debit and Credit : Modern / American / Accounting Equation Approach

		If Increase due to any transaction	If Decrease due to any transaction
I	Debit balances	Debit	Credit
	Assets A/c		
	Expenses A/c		
II	Credit balances	Debit	Credit
	Liabilities A/c (External)		
	Capital A/c (Internal)		
	Incomes / Revenue A/c		

Accounting Equation

An **Accounting Equation** (AE) is a mathematical expression which shows that the assets of a firm **are always equal to** Liabilities due to a firm & capital contributed by the owner.

Assets = Liabilities (External) + Capital (Internal Liability)

Any business transaction **will affect** both the sides of the AE in such a manner that **such equation will hold true** after any number **or** type of business transactions.

Q. 9 : Show the classification of the following Accounts under traditional and accounting equation / modern approach, fill the table below.

	Head of Account	Traditional Approach	Modern Approach
1	Building		
2	Purchases		
3	Sales		
4	Bank Fixed Deposit		
5	Rent		
6	Rent outstanding		
7	Cash		
8	Adjusted Purchases		
9	Closing inventory		
10	Investment		
11	Trade Receivables		
12	Sales Tax payables		
13	Discount Allowed		
14	Bad debts		
15	Capital		
16	Drawings		
17	Interest Receivable Account		
18	Rent received in advance		
19	Prepaid salary		
20	Bad debts recovered		
21	Depreciation		
22	Income Tax		
23	Interest on Provident Fund Invt.s		
24	Interest on Investments		
25	Life Insurance Premium		
26	Insurance claim		
27	Royalty		
28	Sales tax payable		
29	Bills Receivable		
30	Bills Payable		
31	Unexpired Insurance		
32	Loan taken		
33	Goodwill		
34	General Reserve		

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Q. 10 : Analyse transactions of M/s Sahil & Co. for the month of March, 2022 on the basis of double entry system by adopting the following approaches:

(A) Traditional Approach. (B) Accounting Equation Approach.

Transactions for the month of March, 2022 were as follows **(figures are in '000):**

1. Sahil introduced capital through bank of ₹ 4,000.
2. Cash withdrawn from the City Bank ₹ 200.
3. Loan of ₹ 500 taken from Mr. Y.
4. Salaries paid for the month of March, 2022, ₹ 300 and ₹ 100 is still payable for the month of March, 2022.
5. Furniture purchased ₹ 500.

Required : What conclusions one can draw from the above analysis?

Q. 10 : In the books of M/s Sahil & Co.

(figures are in '000)

A) Analysis of Transactions in Tabular form **(Traditional Approach)**

Sr. No.	Transactions	Accounts affected	Type of A/c	Debit (₹)	Credit (₹)	Rule
1	Sahil introduced capital through bank of ₹ 4,000.					
2	Cash withdrawn from the City Bank ₹ 200.					
3	Loan of ₹ 500 taken from Mr. Y.					
4a.	Salaries paid for the month of March, 2022, ₹ 300					
4b.	Salaries ₹ 100 is still payable for the month of Mar, 2022.					
5	Furniture purchased ₹ 500.					

B) Analysis of Transactions in Tabular form **(Accounting Equation Approach)**

Sr. No.	Transactions	Accounts affected	**Type of A/c**	Debit (₹)	Credit (₹)	**Rule**

^ **Conclusions drawn from the above analysis**

(**Comparison of** Traditional Approach and Accounting Equation / Modern Approach)

i) Classification of A/c's & Rules of debit credit **are different** under both the approches

ii) However, Accounts affected & accounts to be debited and credited **remains the same**

iii) Thus, recording of transactions on the basis of double entry system **is independent of** method of analysis followed by a business enterprise

iv) In other words, accounts to be debited & accounts to be credited to record the dual aspect of every transaction **remains the same** under both the approaches

Q. 11 : Calculate the missing amount for the following:

	Assets	Liabilities	Capital
a	15,00,000	?	2,50,000
b	?	1,50,000	75,000
c	57,00,000	-2,80,000	?

Q. 12 : Mr. Dravid has provided following details related to his financials. Find out the missing figures:

Particulars	(₹ in '000)
Profits earned during the year	5,000
Assets at the beginning of year	A
Liabilities at the beginning of year	12,000
Assets at the end of the year	B
Liabilities at the end of the year	C
Closing Capital	35,000
Total liabilities including capital at the end of the year	50,000

Q. 13 : Develop the accounting equation from following information available at the beginning of accounting period:

Particulars	(₹ in '000)
Capital	51,000
Loan	11,500
Trade payables	5,700
Fixed Assets	12,800
Inventory	22,600
Trade receivables	17,500
Cash and Bank	15,300

At the end of the accounting period, the balances appear as follows:

	(₹)
Capital	?
Loan	11,500
Trade payables	5,800
Fixed Assets	12,720
Inventory	22,900
Trade receivables	17,500
Cash and Bank	15,600

(a) Reset the equation and find out profit.

(b) Prepare Balance Sheet at the end of the accounting period.

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^ **Q. 14 :** Following is the information provided by Mr. Gopi pertaining to year ended 31st March 2022. Find the unknowns, showing computation to support your answer:

Particulars	₹	Particulars	₹
Machinery	12,00,000	Trade Receivables	B
Accounts Payable	1,00,000	Loans	C
Inventory	60,000	Closing Capital	D
Total Liabilities including capital	14,15,000	Opening Capital	10,00,000
Cash	A	Loss incurred during the year	35,000
Bank	80,000	**Capital Introduced during the year**	1,00,000

Additional Information: During the year sales of ₹ 15,55,000 was made of which ₹ 15,00,000 have been received

^ **Q. 15 :** Show the effect of increase = (+), decrease = (-) and no change = (0) on the assets of the following transactions:

(a) Purchased office furniture, payment to be made next month.
(b) Collected cash for repair services.
(c) Goods sold on credit.
(d) Withdrawal of cash by the owner for personal use.
(e) Hired an employee as sales manager of the north wing.
(f) Returned goods worth ₹50,000.
(g) One of our debtor agreed to pay his dues to Mr. C who is a creditor of the company with the same amount being due to him.
(h) Entered into an agreement with Mehta & Co. to purchase all raw materials from their company from next year.

Also give reasons for your answers.

^ **Introduction to Petty Cash Book**

In large business organisation, besides large payments, a number of **small payments** like coveyance, postage, stationery, carriage, refreshments, cleaning, xerox etc. have to be made by various departments regularly. If all these payments are made by the cashier and recorded in main cash book, the cashier will be over burdened with the work and cash book will also become voluminuos. To avoid this, it is usual to appoint **Petty Cashier** who is entrusted with the task of making **Petty / Small payments**. Such payments are recorded by petty cashier in separate book called **"Petty Cash Book"**

Advantages of Petty cash book includes saving in time of the main cashier, division of work, better control over small payments, convenience in ledger posting etc.

* **Petty / Small Payments**

Petty expenses (Nominal A/c's)		**Ledger A/c** (Real & Personal A/c's)	
(Specific groups / heads)		Examples	
1	Printing & Stationery A/c	1	Furniture A/c (chair purchased)
2	Postage & Courier Expenses A/c	2	Krishna's A/c (paid to krishna)
3	Travelling & Conveyance A/c	3	Advance to Arun A/c (advance paid)
4	Carriage & Cartage A/c		
5	Sundry / Miscellaneous Expenses A/c		
(Specific Expenses A/c's)			
6	Wages A/c		
7	Electricity A/c		
8	Advertisement A/c		
9	Repairs A/c **etc.**		

1) Printing & Stationery A/c

Eraser, Pen, Pencil, Sharpner, Files, Computer stationery, Envelopes, Inkpots, Stamp pad, Printing charges, Xerox charges, Photocopy charges, Note books, Photostating charges, Full scape papers etc

2) Postage & Courier Expenses A/c

Courier expenses, Speed post charges, **Postal stamps**, Post cards, Postage, Registered postal charges etc.

3) Travelling & Conveyance A/C

Auto fare, Taxi fare, Bus fare, Train fare etc.

4) Carriage & Cartage A/c

Carriage, Cartage, Loading charges, Unloading charges etc.

5) Sundry / Miscellaneous Expenses A/c

Refreshments, Lunch bill, Cleaning charges, Washing charges, Office sanitisation, Paid to sweeper, Gift to clerk, Tip to peon, Donation, Packing charges, Entertainment Exp.s, Newspaper subscription, Locks, Laundry expenses , Mobile charges, Telephone charges, Internet charges, **Revenue stamps** etc.

^ There are **two types** of Petty Cash Book

1) Analytical or Columnar Petty Cash Book **2)** Simple Petty Cash Book

^ **Q. 16 :** Mr. Sourabh the Petty Cashier of Raje Mobile Company, Latur, received Rs. 8,000 on 1 st June, 2019 from Head Cashier under Imprest System.

Details of petty payments for the month are as follows :

		Amt. (Rs.)
1	Auto fare	255
3	Courier Expenses	60
4	Postal stamps purchased	210
5	Eraser / Pen / Pencils purchased	525
6	Speed post charges	198
8	Taxi fare	390
8	Refreshment	850
10	Auto fare	310
12	Registered postal charges	142
13	Files purchased	45
14	Cartage	65
16	Computer stationery purchased	1,650
19	Bus fare	240
19	Mobile charges	270
20	Office sanitation charges paid	160
22	Refreshment	450
23	Wooden chair purchased	270
28	Courier Expenses	140
29	Unloading charges	170
30	Busfare	150

Prepare Analytical Petty Cash Book.

Also, pass relevant journal entries and show posting in relevant ledger accounts.

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* **Q. 26 :** In the books of Raje Mobile Company, Latur

ANALYTICAL / COLUMNAR PETTY

Receipts ₹	C. B. F.	Date	Particulars	V. No.	Payments ₹

CASH BOOK

Analysis of Payments									
Travelling & Conveyance A/c								L. F.	Ledger A/c

^	**Try Yourself : Objectives**
*	**State whether the following Statements are True or False with reasons.**
1	In accounting equation approach, equity + Long-term liabilities = fixed asset + current assets – current liabilities.
2	In the traditional approach, a debtor becomes receiver.
3	The rule of nominal account states that all expenses & losses are recorded on credit side.
4	Journal proper is also called a subsidiary book.
5	Capital account has a debit balance.
6	Purchase account is a nominal account.
7	All the personal & real account are recorded in P&L A/c.
8	Asset side of balance sheet contains all the personal & nominal accounts.
9	Capital account is a personal account.
10	Journal is also known as the book of original entry.
11	Trade discount is a reduction granted by a supplier from the list price of goods or services on business considerations for prompt payment.
12	A ledger is also known as the principal book of accounts.
13	Cash account has a debit balance.
14	Posting is the process of transferring the accounts from ledger to journal.
15	At the end of the accounting year, all the nominal accounts of the ledger book are balanced.
16	Ledger records the transactions in a chronological order.
17	If the total debit side is greater than the total of credit side, we get a credit balance as opening balance.
18	Ledger accounts of assets will always be debited when they are increased.
19	Preparing trial balance is the third phase of accounting process.
20	Trial balance forms a base for the preparation of Financial statement.
21	Agreement of trial balance is a conclusive proof of accuracy.
22	A trial balance will tally in case of compensating errors.
23	A trial balance can find the missing entry from the journal.
24	Suspense account opened in a trial balance is a permanent account.
25	The balance of purchase returns account has a credit balance.
26	Transactions recorded in the purchase book include only purchases of goods on credit transactions.
27	Transactions regarding the purchase of fixed asset are recorded in the purchase book.
28	Cash sales are recorded in the sales book.
29	Subsidiary books are also known as the books of original entry.
30	Bills receivable book is a subsidiary book.
31	Return inward book is also known as purchase return book.
32	Purchase of a second hand machinery will be recorded in purchase book.

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33	Total of sales return book may be posted to the debit side of sales account.
34	If the sales are on a frequent basis, the transactions are recorded in the sales book.
35	The Sales Book is kept to record both cash and credit sales.
36	Gauri purchased goods worth ₹ 75,800 at 5% trade discount and she paid half of the amount in cash. The amount appearing in the purchase book is ₹ 36,005.
37	The debit notes issued are used to prepare Sales Return Book.
38	Bills Receivable and Bills Payable books are type of subsidiary books.
39	Cash book is a subsidiary book as well as a principal book.
40	Two column cash book consists of two columns cash column & bank column.
41	Discount column of cash book is never balanced.
42	Contra entry is passed in a two column cash book.
43	If the bank column is showing the opening balance on credit side, it is an overdraft.
44	A cash book records cash transactions as well as credit transactions.
45	Discount column of cash book records the trade discount.
46	The balance of petty cash book represents an asset.

Answers:

1	**True** As per the modern accounting equation approach- it is the basic formula in the accounting process
2	**True** In the traditional approach, a debtor becomes receiver.
3	**False** The rule of nominal account states that all expenses & losses are recorded on debit side.
4	**True** It is one of the book where in the transactions not entered in the other books are entered in this book.
5	**False** Capital account has a credit balance.
6	**True** As it is considered as an expense.

7	**False**
	All the personal & real account are recorded in balance sheet.
8	**False**
	Asset side of balance sheet contains all the personal & real accounts.
9	**True**
	As it is in the name of the proprietor who is bringing in the capital to the business.
10	**True**
	As the transactions are entered first in this book as a first hand record.
11	**False**
	Trade discount is a reduction granted by a supplier from the list price of goods or services on business considerations other than for prompt payment.
12	**True**
	Since it classifies all the amounts related to a particular account and then it is used as the base for preparing the Trial balance, a ledger is also known as principal books of accounts.
13	**True**
	Being an asset under the modern equation approach, cash account has a debit balance.
14	**False**
	Posting is the process of transferring the balances from journal to ledger.
15	**False**
	At the end of the accounting year, all the nominal accounts of the ledger book are totaled and transferred to P&L A/c.
16	**False**
	Ledger records the transactions in analytical order. But journal records the transactions in a chronological order.
17	**False**
	If the total of debit side is greater than the total of credit side, we get a debit balance as the opening balance.

18	**True**
	The increase to an asset shall be debited since the original balance is also debit.
19	**True**
	Preparing trial balance is the third phase of accounting process which forms the base for the preparation of the final accounts.
20	**True**
	Based on trial balance only, we can prepare financial statement.
21	**False**
	Agreement of trial balance gives only arithmetical accuracy, there can still be errors in preparing the trail balance.
22	**True**
	Since compensating errors cancel out due to their compensating nature of the amounts, hence the Trial balance tallies.
23	**False**
	A trial balance cannot find the missing entry from the journal.
24	**False**
	Suspense account opened in a trial balance is a temporary account
25	**True**
	As purchases is debited, any returns shall be credited (treated in opposite way).
26	**True**
	Since cash purchases are taken to the cash book , it is only credit transactions that are recorded in the purchases book.
27	**False**
	Transactions regarding the purchase of fixed asset are not recorded in the purchase book, only the credit purchases of goods are recorded in it.
28	**False**
	Credit sales are recorded in the sales book.

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29	**True**
	Subsidiary books are maintained as an alternate to the journal.
30	**True**
	Bills receivable is one of the subsidiary book.
31	**False**
	Return inward book is also known as sales return book.
32	**False**
	Purchase of a second hand machinery will not be recorded in purchase book.
33	**True**
	Since sales return is reduction from the total sales value, it is debited in the sales A/c.
34	**True**
	When there are numerous transactions then there are subsidiary books like the sales book where there are recorded instead of regular journal entries.
35	**False**
	The Sales Book is a register specially kept to record credit sales of goods dealt in by the firm, cash sales are entered in cash book and not in the sales book.
36	**True**
	The trade discount is to be deducted from the total value of ₹ 75,800. The amount paid in cash includes cash purchases and only the credit purchase will be shown in the purchase book ₹ 36,005 (72,010 × 50%).
37	**False**
	The debit notes issued are used to prepare Purchase Return Book.
38	**True**
	Yes, they are types of subsidiary books which is alternate to the journals.
39	**True**
	Since the balance is directly taken to the Trial balance from cash book. Hence, it is a subsiadiary book as well as principal book.

40	**True**
	Two column cash book consists of two columns either cash column & discount column or cash column & bank column.
41	**True**
	Discount column is totalled and transferred to the discount allowed or received account.
42	**False**
	Contra entry is passed in a three column cash book which includes bank and cash columns.
43	**True**
	The debit side of opening balance shows a favourable balance, whereas the credit balance is an unfavourable balance and treated as overdraft.
44	**False**
	A cash book records only cash transactions.
45	**False**
	Discount column of cash book records the cash discount. Trade discount is not shown in the books of accounts.
46	**True**
	The balance represents the cash physically in existence and is therefore an asset.
*	**Multiple Choice Questions**
1	The rent paid to landlord is credited to
	(a) Landlord's account. (b) Rent account. (c) Cash account.
2	In case of a debt becoming bad, the amount should be credited to
	(a) Trade receivables account. (b) Bad debts account. (c) Cash account.
3	A Ltd. has a ₹ 35,000 account receivable from Mohan. On January, 22, Mohan makes a partial payment of ₹ 21,000 to A Ltd. The journal entry made on January, 22 by A Ltd. to record this transaction includes:
	(a) A credit to the cash received account of ₹ 21,000.
	(b) A credit to the Accounts receivable account of ₹ 21,000.
	(c) A debit to the cash account of ₹ 14,000.

4	Which financial statement represents the accounting equation -
	Assets = Liabilities + Owner's equity:
	(a) Income Statement (b) Statement of Cash flows (c) Balance Sheet.
5	Which account is the odd one out?
	(a) Office furniture & Equipment.
	(b) Freehold land and Buildings.
	(c) Inventory of materials.
6	The debts written off as bad, if recovered subsequently are
	(a) Credited to Bad Debts Recovered Account
	(b) Credited to Trade Receivables Account.
	(c) Debited to Profit and Loss Account.
7	In Double Entry System of Book-keeping every business transaction affects:
	(a) Two accounts
	(b) Two sides of the same account.
	(c) The same account on two different dates.
8	A sale of goods to Ram for cash should be debited to:
	(a) Ram (b) Cash (c) Sales
9	The process of transferring the debit and credit items from a Journal to their respective
	accounts in the ledger is termed as
	(a) Posting (b) Purchase (c) Balancing of an account
10	The technique of finding the net balance of an account after considering the totals of
	both debits and credits appearing in the account is known as
	(a) Posting (b) Purchase (c) Balancing of an account
11	Journal and ledger records transactions in
	(a) A chronological order and analytical order respectively.
	(b) An analytical order and chronological order respectively.
	(c) A chronological order only
12	Ledger book is popularly known as
	(a) Secondary book of accounts
	(b) Principal book of accounts (c) Subsidiary book of accounts

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13 At the end of the accounting year all the nominal accounts of the ledger book are

(a) Balanced but not transferred to profit and loss account

(b) Not balanced and also the balance is not transferred to the profit and loss account

(c) Not balanced and their balance is transferred to the profit and loss account.

14 A trial balance will not balance if

(a) Correct journal entry is posted twice.

(b) The purchase on credit basis is debited to purchases and credited to cash.

(c) ₹ 500 cash payment to creditor is debited to Trade payables for ₹ 50 and credited to cash as ₹ 500.

15 ₹ 1, 500 received from sub-tenant for rent and entered correctly in the cash book is posted to the debit of the rent account. In the trial balance

(a) The debit total will be greater by ₹ 3,000 than the credit total.

(b) The debit total will be greater by ₹ 1,500 than the credit total.

(c) Subject to other entries being correct the total will agree.

16 After the preparation of ledgers, the next step is the preparation of

(a) Trading accounts (b) Trial balance (c) Profit and loss account

17 After preparing the trial balance the accountant finds that the total of debit side is short by ₹ 1,500. This difference will be .

(a) Credited to suspense account

(b) Debited to suspense account

(c) Adjusted to any of the debit balance account

18

S.No.	Account heads	Debit (₹)	Credit (₹)
1	Sales		15,000
2	Purchases	10,000	
3	Miscellaneous expenses	2,500	
4	Salaries		2,500
	Total	12,500	17,500

The difference in trial balance is due to_____

(a) Wrong placing of sales account

(b) Wrong placing of salaries account

(c) Wrong placing of miscellaneous expenses account

19 In Purchases Book, the record is in respect of _____

(a) Cash purchase of goods.

(b) Credit purchase of goods dealt in.

(c) All purchases of goods.

20 The Sales Returns Book records _____

(a) The return of goods purchased.

(b) Return of anything purchased.

(c) Return of goods sold.

21 The Sales Book _____

(a) Is a part of journal.

(b) Is a part of the ledger.

(c) Is a part of the balance sheet.

22 The weekly or monthly total of the Purchase Book is _____

(a) Posted to the debit of the Purchases Account.

(b) Posted to the debit of the Sales Account.

(c) Posted to the credit of the Purchases Account.

23 The total of the Sales Book is posted to _____

(a) Credit of the Sales Account.

(b) Credit of the Purchases Account.

(c) Credit of the Capital Account.

24 In which book of original entry, will you record an allowance of ₹50 which was offered for an early payment of cash of ₹1,050 _____

(a) Sales Book (b) Cash Book (c) Journal Proper (General Journal)

25 A second hand motor car was purchased on credit from B Brothers for ₹10,000 will be recorded in_____.

(a) Journal Proper (General Journal)

(b) Sales Book

(c) Cash Book

(d) Purchase Book

26 In which book of original entry, will you record a bills receivable of ₹1,000, which was received from a debtor in full settlement for a claim of ₹1,100, is dishonoured_____

(a) Purchases Return Book

(b) Bills Receivable Book

(c) Journal Proper (General Journal)

27 The total of discounts column on the debit side of the cash book, recording cash discount deducted by customers when paying their accounts, is posted to the_____

(a) Credit of the discount allowed account.

(b) Debit of the discount allowed account

(c) Credit of the discount received account.

28 Cash book is a type of_____but treated as a_____of accounts.

(a) Subsidiary book, principal book

(b) Principal book, subsidiary book

(c) Subsidiary book, subsidiary book

29 Which of the following is not a column of a three-column cash book?

(a) Cash column (b) Bank column (c) Petty cash column

30 Contra entries are passed only when _____

(a) Double-column cash book is prepared

(b) Three-column cash book is prepared

(c) Simple cash book is prepared

31 The Cash Book records _____

(a) All cash receipts

(b) All cash payments

(c) All cash receipts and payments

32 The balance in the petty cash book is_____

(a) An expense (b) A profit (c) An asset

33 If Ram has sold goods for cash, the entry will be recorded _____

(a) In the Cash Book (b) In the Sales Book (c) In the Journal

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	Answers:
1	Cash account.
2	Trade receivables account.
3	A credit to the Accounts receivable account of ₹ 21,000.
4	Balance Sheet.
5	Inventory of materials.
6	Credited to Bad Debts Recovered Account
7	Two accounts
8	Cash
9	Posting
10	Balancing of an account
11	A chronological order and analytical order respectively.
12	Principal book of accounts
13	Not balanced and their balance is transferred to the profit and loss account.
14	₹ 500 cash payment to creditor is debited to Trade payables for ₹ 50 and credited to cash as ₹ 500.
15	The debit total will be greater by ₹ 3,000 than the credit total.
16	Trial balance
17	Debited to suspense account
18	Wrong placing of salaries account
19	Credit purchase of goods dealt in.
20	Return of goods sold.
21	Is a part of journal.
22	Posted to the debit of the Purchases Account.
23	Credit of the Sales Account
24	Cash Book
25	Journal Proper (General Journal)
26	Journal Proper (General Journal)
27	Debit of the discount allowed account
28	Subsidiary book, principal book
29	Petty cash column
30	Three-column cash book is prepared
31	All cash receipts and payments
32	An asset
33	In the Cash Book

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BHAVIK DOSHI



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



NETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

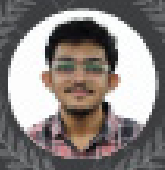
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June 22 & June 23



340/400

HARSH GULWANI
CA Foundation June'22



MEET SHAH
CA Foundation June'23
331



NISHIT KAPUR
CA Foundation June'23
328



PALAK JAJODIA
CA Foundation June'23
325



SWASTIKA SINGH
CA Foundation June'22
323



SUKUNJ GUPTA
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323



DURGASHRI VS
CA Foundation June'22
319



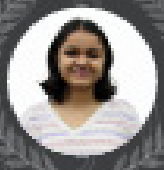
VARUN ADWANI
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319



KARTIK LADHANI
CA Foundation June'22
316



RIDHI PAREKH
CA Foundation Dec'22
314



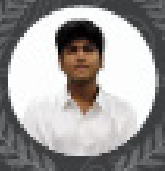
SMEET LADHANI
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313



TANMAY AGARWAL
CA Foundation June'23
311



GARV KHANDELWAL
CA Foundation June'22
308



DAKSH JAIN
CA Foundation June'23
308



DEEPAK GURNANI
CA Foundation June'22
305



PARIDHI JHAWAR
CA Foundation June'22
304



SATYA BHANUSHALI
CA Foundation June'23
304

and many more...

ALL INDIA RANKERS CA INTER | MAY'22 & MAY'23 NOV'23



JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
CA INTER MAY'23
AIR 34



HIMANSHI CHHAJED
CA INTER MAY'23
AIR 39



YUKTA SATPALKAR
CA INTER MAY'22
AIR 40



MARVI LODHA
CA INTER MAY'23
AIR 40



ARMAN HOSANGADY
CA INTER MAY'22
AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MUNDRA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHRUTI SHIVARAM
CA INTER NOV'23
AIR 47

ALL INDIA RANKERS CA FINAL | MAY'22 & NOV'23



SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHADRIA
CA FINAL NOV'23
AIR 32



PINAL KHETAN
CA FINAL NOV'23
AIR 35



SHOURYA TIBREWALA
CA FINAL MAY'22
AIR 39



DEEPAK LADHA
CA FINAL NOV'23
AIR 40



HIMANSHU KHATRI
CA FINAL MAY'22
AIR 41



SHRAVAN MUNDRA
CA FINAL NOV'23
AIR 45



DEEPTHI PACHIPULUSU
CA FINAL MAY'22
AIR 46



SHREY AGARWAL
CA FINAL MAY'22
AIR 48

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KANDIVALI (W)
9/82, Mahavir Nagar, Pragati CHS LTD, Kandivali (West), Mumbai :- 400 067
Ph. : 7784 873 873

GOREGAON (W)
202, 2nd floor, Azmi, 2nd floor, Opposite Ratna, Goregaon, Mumbai - 400104
Ph. : 9819 470 740

ANDHERI (E)
Crescent Plaza, 901, Teli Gali, opp. Imperial Palace Hotel, Bima Nagar, Andheri (E), Mumbai - 69
Ph. : 7273 895 895

VILE PARLE (W)
301/302,cosmos Court Premises Co Op Society Ltd Above Pethe Jewellers S V Road , Vile Parle West , Mumbai 400056
Ph. : 7273 895 895

DADAR (W)
Room No 36, 37, 38, 3rd Floor, Shree Bldg, Opp. Suvidha Showroom, Ranade Rd, Dadar (West)
Ph. : 9619 612 356

MIRA ROAD (E)
Shanti Shopping Centre, A 231, Shanti Shopping Center, Near Railway Station, Mira Road East - 401107
Ph. : 8652 644 767

VIRAR (W)
108,109 1st floor, Viva Mall, Puroshotam Parekh (PP) Market, Near Bus Depot, Opp. Anita Gas Agency, Virar Station (West)
Ph. : 9158 295 935

MULUND (W)
501, 5th Floor, Apt Plaza CTS, 787, JSD, Mulund West, Mumbai -80
Ph. : 7273 946 946

GHATKOPAR (W)
Shop Zone Building, 209/210, Mahatma Gandhi Rd, Ghatkopar West, Mumbai, 400086
Ph. : 7273 947 947

KALYAN (E)
101,Shivdarshan Apts, Near Kalyan Janta Sahakari Bank, Durga Mata Mandir Road,Kolsewadi, Kalyan (East)
Ph. : 859 111 5864

KALYAN (W)
212, Shreeji Solitaire, Khadakpada Circle, Above Bikaner, Kalyan (W)
Ph. : 70390 633 33

DOMBIVALI (W)
001, Vitthal Krupa Bldg, Shubhash Rd, Petrol Pump, Near Bhagshala Ground, Kagade Chowk, Dombivali (W).
Ph. : 9530 531 080

BHIWANDI
Shop No. 27, Prithvi Residency, Near Oswal School, Anjurphata.
Ph. : 7020 902 068

CHEMBUR (E)
19, Sunil Sadan, 3rd Floor, Central Avenue Road, Opp.of Grand Central Hotel, Above Monginis OR Yewle Tea, Chembur(E) - 400071
Ph. : 9870 780 524

AJMER
1, Parashnath Colony, Vaishali Nagar, Ajmer - 305001
Ph.: 8890 774 877

CHENNAI
S6, New No. 16, Old no 42, Govindan Road, West Mambalam, Chennai - 33
Ph.: 044 4860 3232

MATHURA
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Ph. : 8439 344 979

BHILWARA
CORE Junior College, G-409, Azadnagar, Bhilwara, Rajasthan - 311001
Ph. : 9001 390 017

7273 967 967

SCAN ME!

I. Transactions between Business firm and Bank

^ Usually, business firm opens a **Current account** with bank and all the transactions entered into with bank are recorded in **Bank column** of **Cash Book**.

Such bank column in cash book plays a dual role of Journal for recording bank transactions as well as Bank A/c.

Likewise, Bank opens a ledger account of every customer in its books and records all such transactions in such account. Periodically, bank supplies copy of the firm's A/c, in its ledger, to the firm for information and confirmation. This **copy of firm's account** in the books of bank is called **Pass Book** or **Bank Statement**.

^ **Receipts (bank balance increases)**

All receipts are recorded on debit side of cash book and credit side of pass book i.e. are said to be **debited** in cash book and **credited** in pass book

^ **Payments (bank balance decreases)**

All payments are recorded on credit side of cash book and debit side of pass book i.e. are said to be **credited** in cash book and **debited** in pass book

Cash Book (Bank Column)

Dr. **Bank A/c** in our books **Cr.**

Receipts (Bank balance Increases)	**Payments** (Bank balance Decreases)

Pass Book

Dr. **Our A/c** in the books of bank **Cr.**

Payments (Bank balance Decreases)	**Receipts** (Bank balance Increases)

^ **Regular Bank balance**

It indicates our money lying in bank account.

In our (firm's) books, Bank A/c will have Debit balance as Bank is our Debtor

In the books of Bank, Our A/c will have Credit balance as we are Creditor for Bank.

^ **Overdraft balance**

It indicates more amount withdrawn by us from bank than deposits

In our (firm's) books, Bank A/c will have Credit balance as Bank is our Creditor

In the books of Bank, Our A/c will have Debit balance as we are Debtor for Bank.

	Regular balance	Overdraft balance
Dr. balance as per Cash Book	●	
Cr. Balance as per Pass Book	●	
Cr. Balance as per Cash Book		●
Dr. balance as per Pass Book		●

II. Bank Reconciliation Statement (BRS)

Since all the transactions entered into by firm with the bank are recorded by both the parties, there should be no difference in balances shown by cash book and pass book.

Since all the entries recorded on Debit side of cash book are recorded on Credit side of pass book & vice versa, bank balance as per Cash Book & bank balance as per Pass book must tally, as on any date.

However,

sometimes it is possible that both the balances **as on particular date** does not tally.

It can be due to one or more of the following reasons

		Effect on **Bank balance** as per	
		Cash Book (Bank column)	Pass Book / Bank statement
I.	**Differences caused by** Time gap **in recording transactions**		
1	Cheque deposited but not cleared		
2	Cheque deposited & dishonoured but such dishonour not recorded in cash book		
3	Cheque issued but not presented for payment		
4	Cheque issued & dishonoured but such dishonour not recorded in cash book		
II.	**Transactions recorded by bank in pass book but** not recorded **in cash book**		
	as cashier had no information about the same till then		
1	Direct deposit by customer in our bank account		
2	Interest / dividends directly collected by the bank / credited in our bank account		
3	Bank interest allowed / credited by bank		
4	Utility bills / Insurance premium directly paid by the bank as per standing instructions		
5	Bank charges charged / debited by bank		
6	Bank interest charged / debited by bank		

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III.	**Error(s) committed** by either party		
	It can be error of complete omission by either party, error in posting, error in casting, error in balancing, error of principle (conceptual error) in following DES / principles of accounting etc.		
		Effect on **Bank Balance** as per	
		Cash Book (Bank column)	Pass Book / Bank statement
1	**Overcasting**		
	Debit (Receipts) side of C.B.		
	Credit (Payments) side of C.B.		
	Credit (Deposits) side of P.B.		
	Debit (Withdrawls) side of P.B.		
2	**Undercasting**		
	Debit (Receipts) side of C.B.		
	Credit (Payments) side of C.B.		
	Credit (Deposits) side of P.B.		
	Debit (Withdrawls) side of P.B.		
3	Cheque of ₹ 1,500 deposited into bank but wrongly recorded twice in Cash Book		
4	Cheque of ₹ 885 issued and presented to bank but recorded as ₹ 865 in pass book		
5	Cheque deposited and cleared but recorded in cash column of cash book		
6	Electricity bill paid by bank ₹ 3,000 was recorded twice in pass book		

^ **Difference in two bank balances** due to **Bills of Exchange** Transactions

		Effect on **Bank Balance** as per	
		Cash Book	Pass Book
		(Bank column)	/ Bank statement
I.	**Bills Receivable Transactions**		
1	A bill of ₹ 12,000 discounted with bank appears in cash book at full amount but bank has deducted ₹ 240 discounting charges		
2	A bill for ₹ 700 was retired by bank on our behalf under a rebate of ₹ 20. The full amount of the bill was credited in Cash Book.		
3	(BRS as on 31st August)) A bills receivable for ₹ 15,000 discounted with the bank dishonoured on 30th August but intimation was received on 3rd September		
4	(BRS as on 31.12.2018) A Bill of Exchange of ₹ 3,500 discounted with the bank in December 2018, returned dishonoured in January 2019		
5	Bills Receivable directly collected by the bank ₹ 30,000, not recorded in cash book		
II.	**Bills Payable Transactions**		
1	A Bills Payable amounting to ₹ 9,000 paid by bank has not been recorded in Cash Book		
2	Bill accepted in favour of our creditor for ₹ 10,000 honoured by bank but yet not recorded in Cash Book		

Hence, a statement is prepared at the **end of specified period**, to identify the reasons of difference & to reconcile the balances of two books.

Such a statement is called **'Bank Reconciliation Statement'**.

Thus, BRS is a statement prepared mainly **to reconcile** the difference between

i) Bank balance as per Cash Book and

ii) Bank balance as per Pass Book, **as on particular date**.

^ **Need and Importance of BRS**

1. Errors, if any, committed in recording transactions either by us in cash book or by bank in pass book are identified and can be rectified in time accordingly.
2. By preparing a BRS, firm becomes sure about the correctness of bank balance shown by CB. It helps in making further transactions with the bank, especially payments.
3. Undue delay in the clearance of cheques deposited is known from the BRS.
4. Regular prepararion of BRS reduces the chances of embezzlement by the staff. In large business organisations with high banking transactions, BRS is prepared at the end of every week or sometimes even at the end of every day.
5. BRS facilitates updation of cash book from time to time, by recording transactions which were recorded by bank only but not recorded in cash book.

^ It should be noted that it is neither compulsory to prepare BRS nor there is any fixed date / frequency for preparing BRS.

It is **not** even part of Double Entry System (DES) of Accounting.

It is **off the record statement**, prepared periodically, for reasons as stated.

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* **When starting point is regular / favourable balance**

^ **Q. 1 :** Messer's Tall & Short, Faiz Bazar, New Delhi-110002
in account with Punjab National Bank, Daryaganj, New Delhi-110002

PASS-BOOK

Date		Particulars	Withdrawal ₹	Deposits ₹	Dr. or Cr.	Balance ₹
2022						
Jan.	2	By Cash		4,00,000	Cr.	4,00,000
"	4	To Furniture Dealers Ltd.	60,000		Cr.	3,40,000
"	4	To Das & Co.	1,25,000		Cr.	2,15,000
"	10	By J. Johnson & Co.'s		35,000	Cr.	2,50,000
		cheque				
"	12	To Roy & James	1,00,000		Cr.	1,50,000
"	15	By B. Babu & Co's cheque		76,000	Cr.	2,26,000
"	16	By Cash		30,000	Cr.	2,56,000
"	20	To Cash	50,000		Cr.	2,06,000
"	26	By J. Rai & Bros cheque		43,000	Cr.	2,49,000
"	31	To Premium paid as per				
		standing instructions	25,000		Cr.	2,24,000
"	31	To Bank Charges	1,000		Cr.	2,23,000
"	31	By Interest collected on		20,000	Cr.	2,43,000
		Government Securities				

CASH-BOOK (Bank column only)

Date	Particulars	Amount	Date	Particulars	Amount
2022			2022		
Jan. 1	To Cash	4,00,000	Jan. 2	By Furniture Dealers	60,000
Jan. 2	To J. Johnson & Co.	35,000		Ltd.	
Jan. 8	To B. Babu & Co.	76,000	Jan. 2	By Roy & James	1,00,000
Jan. 10	To Cash	30,000	Jan. 2	By Das & Co.	1,25,000
Jan. 16	To J. Rai & Bros.	43,000	Jan. 4	By K. Nagpal & Co.	73,000
Jan. 20	To M. Mohan & Co.	1,05,000	Jan. 17	By Cash	50,000
Jan. 22	To N. Nandy & Sons	34,000	Jan. 20	By B. Babu & Co.	78,000
			Jan. 31	By Balance c/d	2,37,000
		7,23,000			7,23,000
Feb. 1	To Balance b/d	2,37,000			

Prepare BRS as on 31st January 2022 taking Cash Book balance as starting point and then taking Pass Book balance as starting point.

^ **Q. 1 : In the books of Messer's Tall & Short**

a) **If Bank Balance as per Cash Book is taken as starting point**

Bank Reconciliation Statement **as on** 31st January, 2022

Particulars			Amt. (₹)	Amt. (₹)

Workings :

Dr. Cash Book (Bank column) Cr.

	+		-

Dr. Pass Book Cr.

	-		+

b) If Bank Balance as per Pass Book is taken as starting point

Bank Reconciliation Statement **as on** 31st January, 2022

Particulars			Amt. (₹)	Amt. (₹)

Workings :

Dr.	Cash Book (Bank column)		Cr.
	+		-

Dr.	Pass Book		Cr.
	-		+

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^ **Q. 2 :** When Nikki & Co. received a Bank Statement showing a favourable balance of ₹ 10,39,200 for the period ended on 30th June, 2022, this did not agree with the balance in the cash book. An examination of the Cash Book and Bank Statement disclosed the following :

1. A deposit of ₹ 3,09,200 paid on 29th June, 2022 had not been credited by the Bank until 1st July, 2022.
2. On 30th March, 2022 the company had entered into hire purchase agreement to pay by bank order a sum of ₹ 3,00,000 on the 10th of each month, commencing from April, 2022. No entries had been made in Cash Book.
3. A customer of the firm, who received a cash discount of 4% on his account of ₹ 4,00,000 paid the firm a cheque on 12th June. The cashier erroneously entered the gross amount in the bank column of the Cash Book.
4. Bank charges amounting to ₹ 3,000 had not been entered in Cash-Book.
5. On 28th June, a customer of the company directly deposited the amount in the bank ₹ 4,00,000, but no entry had been made in the Cash Book.
6. ₹ 11,200 paid into the bank had been entered twice in the Cash Book.
7. A debit of ₹ 11,00,000 appeared in the Bank Statement for an unpaid cheque, which had been returned marked 'out of date'. The cheque had been re-dated by the customer and paid into Bank again on 5th July, 2022.

Prepare Bank Reconciliation Statement on 30 June, 2022.

^ **Q. 3 :** On 31st March 2018 bank Pass Book of Mr. Rajiv showed a credit balance of ₹ 6,300 but Cash Book showed a different balance. On comparing the two books the following differences were noticed. Prepare BRS as on 31st March 2018.

(i) Cheques sent to bank for collection ₹ 85,000 on 25th March 2018 but a cheque of ₹ 60,000 was only cleared by bank before 31st March 2018.

(ii) Out of cheques issued ₹ 58,500, cheques of ₹ 48,500 were not presented for payment before 31st March 2018.

(iii) A Bill of Exchange for ₹ 4,000 discounted with the bank was dishonoured on 30th March 2018. Intimation of the same was received on 5th April 2018.

(iv) Interest allowed by bank ₹ 820 appeared twice in the Cash Book.

(v) Pass Book debit side was overcast ₹ 200.

(vi) Cheque received from Akash ₹ 4,250 deposited into bank for collection was not yet collected. The entry was recorded in the cash column of Cash Book.

(vii) A bills payable amounting to ₹ 8,700 paid by bank has not been recorded in the Cash Book.

(viii) Mr. Aditya, our customer directly deposited ₹ 17,000 into our account through NEFT. It was not recorded in the Cash Book.

^ **Q. 4 :** Prepare a BRS as on 30th September, 2022 from the following particulars :

Particulars	₹
Bank balance as per pass-book	10,00,000
Cheque deposited in the bank, but no entry was passed in the Cash-Book	5,00,000
Cheque received, but not sent to bank	11,20,000
Credit side of the bank column cast short	2,000
Insurance premium paid directly by the bank under the standing advice	60,000
Bank charges entered twice in the cash book	2,000
Cheque issued, but not presented to the bank for payment	5,00,000
Cheque received entered twice in the cash book	10,000
Bills discounted dishonoured not recorded in the cash book.	5,00,000

^ **Q. 5 :** The following are the Cash Book (bank column) and Pass Book of Jain for the months of March, 2022 and April, 2022:

Cash Book (Bank Column only)

Date	Particulars	Amount	Date	Particulars	Amount
1.3.22	To Balance b/d	60,000	3.3.22	By Cash A/c	2,00,000
6.3.22	To Sales A/c	3,00,000	7.3.22	By Modi	60,000
10.3.22	To Ram	65,000	12.3.22	By Patil	30,000
18.3.22	To Singhal	2,70,000	18.3.22	By Suresh	40,000
25.3.22	To Goyal	33,000	24.3.22	By Ramesh	1,50,000
31.3.22	To Patel	65,000	30.3.22	By Balance c/d	3,13,000
		7,93,000			**7,93,000**

Pass Book

Date	Particulars	Amount Dr.	Amount Cr.	Dr. or Cr.	Balance
		₹	₹		₹
1/4/22	By Balance b/d		3,65,000	Cr.	3,65,000
3/4/22	By Goyal		33,000	Cr.	3,98,000
5/4/22	By Patel		65,000	Cr.	4,63,000
7/4/22	To Naresh	2,80,000		Cr.	1,83,000
12/4/22	To Ramesh	1,50,000		Cr.	33,000
15/4/22	To Bank Charges	200		Cr.	32,800
20/4/22	By Usha		17,000	Cr.	49,800
25/4/22	By Kalpana		38,000	Cr.	87,800
30/4/22	To Sunil	6,200		Cr.	81,600

Reconcile the balance of cash book on 31/3/2022

^ **When extract of Cash Book and Pass Book is given**

	Cash Book and Pass Book	Appearing in BRS
I	**Common** Period	**Uncommon** Transactions
II	**Uncommon** Period	**Common** Transactions

* **When starting point is overdraft / unfavourable balance**

^ **Q. 6 :** From the following information, prepare a bank reconciliation statement as at 31st December, 2022 for Messrs New Steel Limited :

Sr. No.	Particulars	₹
1	Bank overdraft as per Cash Book on 31st December, 2022	22,45,900
2	Interest debited by Bank on 26th December, 2022 but no advice received	2,78,700
3	Cheque issued before 31st December, 2022 but not yet presented to Bank	6,60,000
4	Transport subsidy received from the State Government directly by the Bank but not advised to the company	14,25,000
5	Draft deposited in the Bank, but not credited till 31st December, 2022	13,50,000
6	Bills for collection credited by the Bank till 31st December, 2022 but no advice received by the company	8,36,000
7	Amount wrongly debited to company account by the Bank, for which no details are available.	7,40,000

^ **Q. 7 :** On 30th November, 2018, the Cash Book of Mr. Hari showed an overdrawn position of ₹ 4,480 although his Bank Statement showed only ₹ 3,200 overdrawn. An examination of the two records showed the following errors:

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

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

(iv) A cheque for ₹ 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.

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(v) The Bank had debited a cheque for ₹ 150 to Mr. Hari's Account by mistake, it should have been debited by them to Mr. Kar's Account.
(vi) A dividend of ₹ 100 was collected by the bank but not entered in the Cash Book.
(vii) Cheques totalling ₹ 1,300 drawn on November was not presented for payment.
(viii) Cheque for ₹ 1,200 deposited on 30th November was not credited by the Bank.
(ix) Interest amounting to ₹ 300 was debited by the Bank but yet to be entered in the Cash Book.

You are required to prepare a Bank Reconciliation Statement on 30th November, 2018.

^ **Q. 8 :** The Bank Pass Book of Account No. 5678 of Mrs. Rani showed an overdraft of ₹ 33,575 on 31st March 2018. On going through the Pass Book, the accountant found the following:

(i) A Cheque of ₹ 1,080 credited in the pass book on 28th March 2018 being dishonoured is debited again in the pass book on 1st April 2018. There was no entry in the cash book about the dishonour of the cheque until 15th April 2018.
(ii) Bankers had credited her account with ₹ 2,800 for interest collected by them on her behalf, but the same has not been entered in her cash book.
(iii) Out of ₹ 20,500 paid in by Mrs. Rani in cash and by cheques on 31st March 2018 cheques amounting to ₹ 7,500 were collected on 7th April, 2018.
(iv) Out of Cheques amounting to ₹ 7,800 drawn by her on 27th March, 2018 a cheque for ₹ 2,500 was encashed on 3rd April, 2018.
(v) Bankers seems to have given here wrong credit for ₹ 500 paid in by her in account No. 8765 and a wrong debit in respect of a cheque for ₹ 300 against her account No. 8765.
(vi) A cheque for ₹ 1,000 entered in Cash Book but omitted to be banked on 31st March, 2018.
(vii) A Bill Receivable for ₹ 5,200 previously dishonoured (Discount ₹ 200) with the Bank had been dishounoured but advice was received on 1st April, 2018.
(viii) A Bill for ₹ 10,000 was retired /paid by the bank under a rebate of ₹ 175 but the full amount of the bill was credited in the bank column of the Cash Book.
(ix) A cheque for ₹ 2,400 deposited into bank but omitted to be recorded in Cash Book and was collected by the bank on 31st March, 2018.

Prepare Bank Reconciliation Statement as on 31st March, 2018.

Adjusted Cash Book

When the **balance in the cash book** is first adjusted for certain adjustments before taking it to the bank reconciliation statement,
then it is known as **adjusted cash book balance.**

While adjusting the cash-book,
the following adjustments are considered:-

(1) **All the errors in Cash Book** (like incorrect amount recorded in the cash-book, entry posted twice in the cash-book, over/undercasting of the balance etc.) and

(2) **Omissions in Cash Book** (like bank charges recorded in the pass-book only, interest debited by the bank, direct receipt or payment by the bank, dishonour of cheques/bills etc.) / by the cash-book are taken into care.

Remember

* **Adjusted** Cash Book balance **is taken to** BRS.
* Errors occuring in the P.B. are **not considered** in adjusted C.B.
* Any delay in recording in P.B. due to timing difference are **not considered** in adjusted C.B.

Adjusting the cash-book before preparing the bank reconciliation statement is completely optional, if reconciliation is done during different months.

But, if reconciliation is done at the end of the accounting year or financial year, the cash-book must be adjusted so as to reflect the correct bank balance in the balance sheet.

Q. 9 : According to the cash-book of Gopi, there was a balance of ₹ 44,50,000 in his bank on 30th June, 2022. On investigation you find that:

(1) Cheques amounting to ₹ 6,00,000 issued to creditors have not been presented for payment till the date.

(2) Cheques paid into bank amounting to ₹ 11,05,000 out of which cheques amounting to ₹ 5,50,000 only collected by the bank up to 30th June 2022.

(3) A dividend of ₹ 40,000 and rent amounting to ₹ 6,00,000 received by the bank and entered in the pass-book but not recorded in the cash book.

(4) Insurance premium (up to 31st December, 2022) paid by the bank ₹ 27,000 not entered in the cash book.

(5) The payment side of the cash book had been under casted by ₹ 5,000.

(6) Bank charges ₹ 1,500 shown in the pass book had not been entered in the cash book.

(7) A bill payable of ₹ 2,00,000 had been paid by the bank but was not entered in the cash book and bill receivable for ₹ 60,000 had been discounted with the bank at a cost of ₹ 1,000 which had also not been recorded in cash book.

Required :

(a) prepare BRS as on 30 th June, 2022 without adjusting the Cash Book

(a) to make the appropriate adjustments in the cash book, and

(b) to prepare a statement reconciling adjusted cash book balance with the pass book.

^ **Q. 10 :** On 30th September, 2022, the bank account of X, according to the bank column of the Cash- Book, was overdrawn to the extent of ₹ 4,062. On the same date the bank statement showed a credit balance of ₹ 20,758 in favour of X. An examination of the Cash Book and Bank Statement reveals the following:

1. A cheque for ₹ 13,14,000 deposited on 29th September, 2022 was credited by the bank only on 3rd October, 2022.
2. A payment by cheque for ₹ 16,000 has been entered twice in the Cash Book.
3. On 29th September, 2022, the bank credited an amount of ₹ 1,17,400 received from a customer of X, but the advice was not received by X until 1st October, 2022.
4. Bank charges amounting to ₹ 580 had not been entered in the Cash Book.
5. On 6th September, 2022, the bank credited ₹ 20,000 to X in error.
6. A bill of exchange for ₹ 1,40,000 was discounted by X with his bank. This bill was dishonoured on 28th September, 2022 but no entry had been made in the books of X.
7. Cheques issued upto 30th September, 2022 but not presented for payment upto that date totalled ₹ 13,26,000.

You are required :

(a) to show the appropriate rectifications required in the Cash Book of X, to arrive at the correct balance on 30th September, 2022 and

(b) prepare BRS with plus & minus columns

^ **Q. 11 :**

Mr. Manoj is employed by Century Rayon and Carpets Pvt Ltd. as their cashier.

The main responsibility of Mr. Manoj is to maintain the company's cash book and prepare a bank reconciliation statement at the end of each month.

The cash book (only bank column) is set out below together with a copy of the bank statement for the month of February 2022.

a) Make necessary entries to update the cash book.

b) Reconcile the cash book with the bank statement.

c) Start with the balance as per cash book, list any unpresented cheques and sub-total on the reconcliation statement.

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Cash Book (Bank Column only)

Date	Particulars	Dr. (₹)	Date	Particulars	Cr. (₹)
1-2-22	To Balance b/d	1,42,500	3-2-22	By Bhagwandas	1,980
1-2-22	To Blue and Co	1,570	7-2-22	By Maruti Ltd (400460)	1,500
4-2-22	To GM Ltd	2,430	12-2-22	By Jackson Ltd	54,000
8-2-22	To Robinson Ltd	910		(400461)	
13-2-22	To Donald	750	18-2-22	By PC computers	1,420
20-2-22	To Avenue Super mart	4,200		(400462)	
28-2-22	To Sleep Well Ltd	940	24-2-22	By Shiv garage	49,000
				(400463)	
			28-2-22	By Petty cash	1,500
				(400465)	
				By Shweta & Co	2,100
				(400464)	
				By AV Partners	5,200
				(400466)	
				By Balance c/d	36,600
		1,53,300			**1,53,300**

Customer: Century Rayon and Carpets Pvt Ltd

Account No – xxxxx0439

Account Statement for the month of February 2022

Date	Particulars	Dr. (₹)	Cr. (₹)	Dr. or Cr.	Balance (₹)
1.2.22	Balance b/d				1,42,500
3.2.22	Cheques		1,570	Cr.	1,44,070
5.2.22	Maruti Ltd	1,500		Cr.	1,42,570
7.2.22	Bhagwandas	1,980		Cr.	1,40,590
12.2.22	GM Ltd		2,430	Cr.	1,43,020
15.2.22	Robinson Ltd		910	Cr.	1,43,930
20.2.22	Premium of New India				
	Insurance Ltd	3,800		Cr.	1,40,130
24.2.22	Donald		750	Cr.	1,40,880
24.2.22	400463	49,000		Cr.	91,880
25.2.22	cheques		4,200	Cr.	96,080
26.2.22	Savita	1,030		Cr.	95,050
26.2.22	400465	1,500		Cr.	93,550
27.2.22	Shreya		2,200	Cr.	95,750
28.2.22	Bank charges	2,538		Cr.	93,212

^	**Try Yourself : Objectives**
*	**State whether the following statements are True or False with reasons :**
1	Cheques deposited into bank but not yet cleared appears in the Pass Book only.
2	Direct deposit made by debtors into businessman's bank account is recorded on the credit side of Pass Book.
3	Businessman can prepare Bank Reconciliation statement only with Cash Book Balance.
4	When overdraft as per Cash Book is given, bank charges debited in Pass Book only, is to be added.
5	Bank Statement is sent by Bank to businessman.
6	Bank Reconciliation Statement is prepared at the end of every month.
7	Bank Reconciliation Statement is prepared by the Bank.
8	Overdraft facility is allowed to Proprietor's Personal A/c.
9	Debit balance of Pass Book represents overdraft.
10	Bank charges debited by Bank increases bank balance as per Pass Book.
11	Interest credited in Pass Book is an income to the customer.
12	Bank Reconciliation Statement is prepared to detect the errors that take place in accounting.
13	Overdraft as per Cash Book means debit balance as per Cash Book.
14	Cheque deposited into Bank increases the Bank balance as per Cash Book.
15	Payments made by bank as per standing instructions are recorded on Debit balance of Pass Book.
16	Bank column in Cash Book represents Proprietor's Savings A/c.
17	Bank Reconciliation is the process of reconciling cash column of the cash book and bank column of the cash book.
18	There are 3 types of differences between cash book and pass book namely Timing, Transactions & Errors.
19	Adjusting the cash book for any errors and/or omissions before preparing bank reconciliation is optional when the reconciliation is done at the end of the financial year.
20	Debit balance in cash book is same as overdraft as per pass book.
21	Bank charges debited by the bank is an example of timing difference for the purposes of bank reconciliation.
22	Overcasting of the debit side of the cash book is an example of a difference that is due to error.
23	The bank charges charged by the bank should be deducted when bank reconciliation statement is being prepared starting from a credit balance of pass book.
24	When we start bank reconciliation with a debit balance in cash book, then cheques issued but not yet presented should be added back to arrive at the balance as per pass book.

25	When the causes of differences between pass book balance and cash book is not known, then the bank reconciliation statement can be prepared by matching the two books and identifying any unticked items in both sets.
26	While preparing the bank reconciliation statement starting with debit balance as per pass book or bank statement, the deposited cheques that are not yet cleared need not be adjusted.
27	Cash book shows a debit balance of ₹ 50,000 and the only difference from the balance as shown in pass book relates to cheques issued for ₹ 60,000 but not yet presented for payment. The balance as per pass book should be ₹ 1,10,000.
28	Overcasting of credit side of the cash book shall result in a higher bank balance in cash book when compared with pass book balance.
29	A cheque for ₹ 25,000 that was issued and was also presented for payment in same month but erroneously recorded on debit side of the cash book would cause a difference of ₹ 50,000 from the balance in pass book.
30	A direct debit by bank on account of any payment as may be instructed by customer should be recorded on credit side of cash book.
31	Bank Reconciliation Statement can be prepared in two formats – "Balance" presentation and "Plus & Minus" presentation.
32	The difference between cash book & pass book that relates to errors are those mostly made by Bank.
33	A cheque for ₹ 80,000 that was discounted from bank was dishonoured and the bank charged ₹ 1,600 as the charges on account of same. While starting with debit balance in cash book for preparing bank reconciliation statement, we need to deduct ₹ 78,400 to reconcile with pass book.
34	Interest on savings bank that is allowed or credited by bank is generally recorded in cash book prior to it being recorded by bank.
35	A regular bank reconciliation discourages the accountants to be involved in any kind of funds embezzlement.
36	Timing difference relates the transactions that are recorded in the same period in both cash book and also the bank pass book.
37	Bank reconciliation statement is prepared to arrive at the bank balance.

Answers

1 **False**

Cheques deposited into bank but not yet cleared appears in the cash book. only. Bank records entry in the pass book only after the cheque is cleared. So there is no entry for this transaction in the Pass Book.

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2	**True**
	Credit side of pass book means deposits made in the bank account. When direct deposits are made by debtors into businessman's bank account. It increases the bank balance and it is recorded on the credit side of Pass Book.
3	**False**
	Businessman can prepare Bank Reconciliation statement with the help of cash book, bank column and pass book. It is comparison between the two to show the differences. Both i.e. cash book and pass book / Bank statement is required to prepare Bank Reconciliation statement.
4	**True**
	Bank overdraft as per cashbook means negative bank balance. Businessman has to pay to the Bank. Bank charges are expenses for the business and this increases the amount payable to bank so bank charges debited in pass book only is to be added in the cash book.
5	**True**
	Bank statement is a statement issued by the bank to the current account holder informing about the bank transactions during a particular period of time. Generally it is issued every month. It gives details information about bank deposits and withdrawals etc.
6	**True**
	Monthly preparation of Bank Reconciliation Statement assists in the regular monitoring of cash flows of a business and identification of accounting error.
7	**False**
	A Bank Reconciliation statement shows the causes of disagreement between the balances shown by the bank pass book and bank balance shown by the cash book, for a particular period of time generally a month. It is prepared by the trader as he has both the books to compare and find the differences.
8	**False**
	Overdraft facility is allowed only to business current A/c & not to Proprietor's Personal A/c.

9	**True**
	Debit Column of a passbook means withdrawals from the bank, When withdrawala are more than deposits it means excess amount is withdrawn from the bank. It is a temporary loan payable by trader to the bank. So debit balance of Pass Book represents overdraft.
10	**False**
	Bank charges is expense for the business. Expenses decreases the bank balance as per Pass Book. Bank charges debited by the bank decreases Pass book balance.
11	**True**
	All incomes are shown on the credit side of passbook. It is a deposit. So Interest Credited in Passbook is an income to the customer.
12	**True**
	A businessman maintains a cash book with bank column to record his bank transactions where as bank also maintains a customer's ledger account and issues him a Bank statement. There could be differences as per the bank balance in the cash book and bank balance in the passbook. To detect the errors that take place in accounting Bank Reconciliation Statement is Prepared.
13	**False**
	Overdraft as per Cash Book means credit balance as per cash book. Cash book debit means deposits. When cash book debit balance is greater it means Bank Balance as per Cash Book.
14	**True**
	Debit side of cash book means deposits. So cheque deposited into the Bank increases the Bank Balance as per Cash Book.
15	**True**
	Debit side of passbook represents payments. So any payments made by the bank, Bank debits the customer's account and records on the Debit side of pass book.
16	**False**
	Cash book records only business transactions and not personal A/c of the trader. Bank column in Cash Book represents Business Current A/c and not the proprietors savings A/c.

17	**False**
	Bank Reconciliation Statement reconciles bank column of cash book with the balance in the pass book i.e. customer account in the books of bank.
18	**True**
	These are the three broad categories.
19	**False**
	Adjusting the cash book is mandatory when bank reconciliation is done at the end of the financial year.
20	**False**
	Debit balance as per cash book should be represented by credit or favourable balance in pass book.
21	**False**
	Bank charges are example of the transactions that bank carries out by itself and the same has not been recorded in the cashbook until statement is obtained from the bank.
22	**True**
	Overcasting is an example of an error.
23	**False**
	Bank charges should be added when we start with credit or favourable balance in pass book as bank would have debited the charges.
24	**True**
	Since the cheques issued would have been recorded as payments and bank balance was credited in cash book, we need to add it back as the same is not yet deducted from our bank balance.
25	**True**
	Since, we don't know the causes of difference, matching the two statements is only efficient way to identify the difference.
26	**False**
	Cheques deposited but not yet cleared should be subtracted from debit or unfavourable balance in pass book.

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27	**True**
	Cheques issued but not yet presented should be added back to a debit balance in cash book to arrive at pass book balance i.e. ₹ 50,000 + ₹ 60,000 = ₹ 1,10,000.
28	**False**
	Overcasting of credit side means excessive payments are recorded and hence would lower the bank balance.
29	**True**
	₹ 25,000 payment is recorded as a receipt and hence it will have to be adjusted twice (once to nullify and then once to record actual payment) hence causing the difference of double amount.
30	**True**
	It is an example of a payment instructed by customer to be directly debited by bank, and hence credited in the cash book.
31	**True**
	Reconciliation statement can be prepared in either of the two formats.
32	**False**
	Bank rarely makes mistakes, and hence differences that relate to errors are generally made in cash book.
33	**False**
	We need to deduct ₹ 81,600 (i.e. both cheque returned & charges) from debit balance in cash book to arrive at balance as per pass book.
34	**False**
	Interest allowed by bank is mostly recorded in cash book after the entry has been made in the pass book or bank statement.
35	**True**
	In absence of any reconciliation, the accountants can mis-utilize the funds temporarily by recording the entry without actual depositing the cash.

36	**False**
	Timing differences relate to the transactions that are recorded in cash book and pass book in two different periods.
37	**False**
	Bank reconciliation statement is prepared to reconcile and explain the causes of differences between bank balance as per cash book and the same as per bank statement as on a particular date.
*	**Multiple Choice Questions**
1	When the balance as per Cash Book is the starting point, direct deposits by customers are:
	(a) Added (b) Subtracted (c) Not required to be adjusted.
2	A debit balance in the depositor's Cash Book will be shown as:
	(a) A debit balance in the Bank Statement.
	(b) A credit balance in the Bank Statement.
	(c) An overdrawn balance in the Bank Statement.
3	When balance as per Pass Book is the starting point, interest allowed by Bank is
	(a) Added (b) Subtracted (c) Not required to be adjusted
4	A Bank Reconciliation Statement is prepared with the help of:
	(a) Bank statement and bank column of the Cash Book.
	(b) Bank statement and cash column of the Cash Book
	(c) Bank column of the Cash Book and cash column of the Cash Book.
5	When drawing up a Bank Reconciliation Statement, if you start with a debit balance as per the Bank Statement, the unpresented cheques should be:
	(a) Added (b) Deducted (c) Not required to be adjusted
6	The cash book showed an overdraft of ₹ 1,50,000, but the pass book made up to the same date showed that cheques of ₹ 10,000, ₹ 5,000 and ₹ 12,500 respectively had not been presented for payments; and the cheque of ₹ 4,000 paid into account had not been cleared. The balance as per the pass book will be:
	(a) ₹ 1,10,000 (b) ₹ 2,17,500 (c) ₹ 1,26,500

7	When drawing up a BRS if you start with a Dr. Balance as per Bank Statement, the following are added: 1. Cheque issued but not presented to bank 2. B/R collected directly by bank 3. Overcasting of the Dr. Side of bank A/c in the cash book. (a) only 1 (b) only 1& 2 (c) all of the above
8	A bank reconciliation statement is mainly prepared to: (a) Reconcile the cash balance of the cash book (b) Reconcile the difference between the bank balance shown by the cash book and bank passbook (c) both a & b
9	Overdraft means_____balance of Cash Book. (a) debit (b) credit (c) none
10	When a cheque is deposited and collected by bank Pass Book is_____. (a) dishonoured (b) debited (c) credited
11	A _____is a summary of financial transactions that take place over a period of time on a bank account. (a) withdrawal slip (b) bank advice (c) bank statement
12	Debiting an entry in Cash Book_____cash balance. (a) increases (b) decreases (c) nullifies
13	Bank Reconciliation Statement is prepared by_____. (a) student (b) businessman (c) bank
14	Bank balance as per Pass Book means balance of Pass Book. (a) debit (b) credit (c) none
15	Bank gives overdraft facility to_____account holder. (a) savings (b) recurring (c) current
16	Debit balance as per Cash Book is also known as_____balance. (a) favourable (b) abnormal (c) unfavourable

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17 When extracts of Cash Book and Pass Book are given for uncommon periods, only _____items are considered for preparation of Bank Reconciliation Statement.
(a) uncommon (b) normal (c) common

18 When extract of Cash Book and Pass Book are given for common period, only_____ items are considered for preparation of Bank Reconciliation Statement.
(a) uncommon (b) common (c) none

19 Pass Book is_____of account holders transactions with bank.
(a) an extract (b) mode (c) balance

20 When cheque is _____into bank Cash Book is debited.
(a) dishonoured (b) issued (c) deposited

21 Overdraft means_____balance of Pass Book.
(a) debit (b) credit (c) none

22 Interest on bank overdraft is recorded on_____side of Pass Book.
(a) debit (b) credit (c) none

23 Credit balance in the Pass Book represents .
(a) overdraft (b) bank balance (c) loan borrowed

24 Direct deposit by a customer will be recorded on _____side of Pass Book.
(a) debit (b) credit (c) any

25 Normally the Bank Reconciliation Statement is prepared at the end of a .
(a) month (b) week (c) year

26 Bank charges charged by bank are recorded on _____side of Pass Book.
(a) debit (b) credit (c) any

Answers :

1	(a)		**6**	(c)		**11**	(c)		**16**	(a)		**21**	(a)		**26**	(a)
2	(b)		**7**	(b)		**12**	(a)		**17**	(c)		**22**	(a)			
3	(b)		**8**	(b)		**13**	(b)		**18**	(a)		**23**	(b)			
4	(a)		**9**	(b)		**14**	(b)		**19**	(a)		**24**	(b)			
5	(a)		**10**	(c)		**15**	(c)		**20**	(c)		**25**	(a)			

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TARA MANGWANI
347



RIVA SINGH
346



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344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



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304



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302



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301



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300



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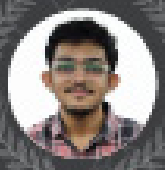
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328



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325



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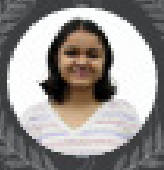
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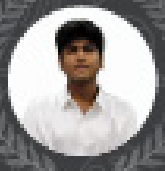
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308



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JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
CA INTER MAY'23
AIR 34



HIMANSHI CHHAJED
CA INTER MAY'23
AIR 39



YUKTA SATPALKAR
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AIR 46



PRANJAL MUNDRA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHRUTI SHIVARAM
CA INTER NOV'23
AIR 47

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SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
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AIR 6



SHRUTI PAROLIA
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AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
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AIR 22



PARTHIV CHADRIA
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SCAN ME!

^ **Process of Accounting / Accounting Cycle**

It includes various stages, which are as follows

1) Classification of various Events **between Transactions & Non- Transactions**

Non - Transactions, though could be very important for business and may affect business in long run, but, are **not recorded in** books of accounts since it doesn't affect any of the Personal, Real **or** Nominal Accounts as on today.
It's effect cann't be measured in terms of money.

2) Classification of Transactions between **Business & Personal Transactions**

Personal Transactions of proprietor which doesn't affect any of the Personal, Real or Nominal Accounts of business **are not recorded** in the books of accounts

3) **Various Business Transactions** as entered into throught the year **are :**

* **Firstly,** recorded in Primary Book of Account / Book of Original Entry called Journal or sub-division of such Journal called Subsidiary books.
Such recording is based on scientific principle called **Double Entry System** (DES) of book keeping, following dual aspect concept, as per which,
for every debit, there has to be **corresponding credit of the same amount**

* **Secondly**, such transactions are posted from Journal to Secondary / Principal book of account called Ledger.
It includes Posting, Casting & Balancing of various Ledger Accounts

Both the above steps (Journal & Ledger) includes Casting (totalling) & Carrying forward a total of one page to another page.

4) **At the end of Accounting period / year,**

* All Books & Ledger Accounts are closed, closing balance of each & every Account is put on a list called Trial Balance, to check the Arithmetical accuracy of accounting work.

DES of Accounting requires that for every debit, there is corresponding credit of the same amount. **If above principle is followed correctly**, throughout the period / year, for each & every transaction in books of accounts, Trial Balance (TB) tallies i.e. Total of debit column of TB is **equal to** total of credit column of TB.

* Then, **Final Accounts** are prepared consisting of :

1) Trading Account for the year ended …… (last day of year)

2) Profit & Loss Account for the year ended …… (last day of year)

Above two are prepared to find out **Operating results**

(Profit earned or Loss suffered during the year)

3) Balance Sheet as on …… (last day of year)

It is prepared to know the **Financial Position**

(Assets, Liabilities & Capital as on a particular date)

^ **Introduction**

Accounting is **often regarded as** a language of business.

Since the main aim of a language **is to serve as a** means of communication,

Accounting **communicates the result of business activities** to various interested parties like owners, management, creditors, lenders, government, employees etc.

These users **use accounting information** in order to satisfy some of their varied needs for information.

Hence,

it is very important that information provided by books of accounts is True & Fair and **it does not contain one or more errors**, thereby resulting into giving Incorrect / misleading information to various users of accounting information.

^ **Error**

Error can be defined as an unintentional mistake.

Such errors can be **at any stage** in accounting process.

It can be error in recording the transaction, error in posting, error in casting, error in balancing, error in carrying forward, error in writing balance in trial balance etc

Such errors **may not** affect tallying of Trial balance **or** may affect the trial triance, **depending upon** whether DES of accounting is followed properly or not.

Accordingly, **a particular error** can be **either** termed as :

1) Two sided error (If it doesn't affect tallying of the Trial balance) **or**

2) One sided error (If it affects tallying of the Trial balance)

^ **Rectification of Errors**

Errors, whether affecting the trial balance or not, **must be detected and corrected, to enable books of accounts giving** True & Fair view of operating results **(Profit or Loss)** and Financial Position **(Assets, External Liabilities & Capital)**.

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The procedure followed to rectify the errors & to set right accounting records is called **Rectification of Errors.**

Journal Entry passed to rectify any error is called a **Rectification Entry**.

Rectification Entries are recorded in **Journal Proper**.

Rectification of Errors can be :

* **Before** preparation of Trial Balance **or**
* **After** preparation of Trial Balance ;

depending upon at what stage such error is detected.

^ **Types of Errors**

I) **Errors of Principle**

Transactions recorded without following the accounting principles and rules are known as errors of principle. These errors are caused **due to the violation of** one or more fundamental accounting principles.

An error of principle may occur due to incorrect classification of expenditure or receipt between Capital and Revenue or due to any other violation of accounting rule(s).

These errors doesn't affect tallying of Trial balance **(two sided errors)** since DES of accounting is not violated.

II) **Errors of Omission**

a) **Errors of Complete Omission**

Such error occurs when a transaction is completely omitted to be recorded in books of accounts. These errors doesn't affect tallying of Trial balance **(two sided errors)** since DES of accounting is not violated.

b) **Errors of Partial Omission**

An error of omission other than error of complete omission is error of partial ommission.

These errors affects tallying of Trial balance **(one sided errors)** since DES of accounting is violated.

III) Errors of Commission

Types of Errors		One sided Errors	Two sided Errors
a)	**Error of recording**		
	This error arises when any transaction is recorded		
	incorrectly in the books of original entry		
	i.e. double effect given, but both effects are for		●
	wrong amount or recorded in wrong book		
	eg. Goods purchased on credit from Mohan for		
	₹ 500 recorded in Purchase Book as ₹ 5,000		
b)	**Error of casting**		
	This error arises when mistake is committed in	●	
	totalling the books of original entry		
c)	**Error in carrying forward**		
	This error arises when mistake is committed in	●	
	carrying forward a total of one page to another page		
d)	**Error in Posting**		
i)	**Errors of posting NOT affecting the TB**		
	eg. posting correct amount on correct side,		
	but in wrong account,		●
	posting wrong amount in both affected accounts		
	(from Journal proper)		
ii)	**Errors of posting affecting the TB**		
	Posting wrong amount from Special Journals,	●	
	posting on wrong side of the account,		
	posting twice in one account		
e)	**Error in balancing of an account**	●	

IV) Compensating Errors

These are the errors in which effect of one error is		
nullified by the effect of another error in such a way		
that trial balance tallies. **This is pure coincidence.**		
eg. Purchase book was undercast by ₹ 2,000 &		●
Sales Returns book was overcast by ₹ 2,000 ;		
Credit sales of ₹ 7,956 debited to Shyam's A/c		
as ₹ 7,965 and credit purchase of ₹ 2,412 credited		
to Ram's A/c as ₹ 2,421		

** **ROE I** : Rectification of Errors **before** Preparing **Trial Balance**

^ **Q. 1 :** The following errors, affecting the account for the year 2022 were detected in the books of Jain Brothers, Delhi:

(1) Sale of old Furniture ₹ 150 treated as sale of goods.

(2) Receipt of ₹ 500 from Ram Mohan credited to Shyam Sunder.

(3) Goods worth ₹ 100 brought from Mohan Narain have remained unrecorded so far.

(4) A return of ₹ 120 from Mukesh posted to his debit.

(5) A return of ₹ 90 to Shyam Sunder posted as ₹ 9 in his account.

(6) Rent of proprietor's residence, ₹ 600 debited to Rent A/c.

(7) A payment of ₹ 215 to Mohammad Sadiq posted to his credit as ₹ 125.

(8) Sales Book casted short by ₹ 900 .

(9) The total of Bills Receivable Book ₹ 1,500 left unposted.

You are required to pass the necessary rectifying entries and show how the trial balance would be affected by the errors.

^ **Q. 2 :** How would you rectify the following errors in the book of Rama & Co.?

1. The total to the Purchases Book has been undercast by ₹ 100.
2. The Returns Inward Book has been undercast by ₹ 50.
3. A sum of ₹ 250 written off as depreciation on machinery has not been debited to Depreciation Account.
4. A payment of ₹ 75 for salaries (to Mohan) has been posted twice to Salaries A/c.
5. The total of Bills Receivable Book ₹ 1,500 has been posted to the credit of Bills Receivable Account.
6. An amount of ₹ 151 for a credit sale to Hari, although correctly entered in the Sales Book, has been posted as ₹ 115.
7. Discount allowed to Satish ₹ 25 has not been entered in the Discount Column of the Cash Book. The amount has been posted correctly to the credit of his personal A/c.

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** **ROE II :** Rectification of Errors **after** Preparing **Trial Balance**

(When **Suspense A/c** is given)

DES of Accounting requires that for every debit, there is corresponding credit of the same amount. **If above principle is followed correctly**, throughout the year / period for each & every transaction in books of accounts, Trial Balance (TB) tallies i.e. Total of debit column of TB **is equal to** total of credit column of TB.

Hence, if TB prepared at the end of year / period doesn't tally, it means there are one or more errors occurred at any stage in the process of accounting till TB is prepared. Such errors affecting the Trial balance are called **One sided Errors**.

Certain steps can be followed like checking total of trial balance, verifying all A/c's balances are posted in correct column of TB, following trial & error method etc.
If still there is a difference in TB, a complete & detailed verification is necessary.

Meanwhile, till all errors are detected / identified and rectified,
the difference in Trial balance is temporarily transferred to Suspense A/c

If total of Dr. column of TB is more,
Suspense A/c is shown in Cr. column with differential amount.

If total of Cr. column of TB is more,
Suspense A/c is shown in Dr. column with differential amount.

The **rationale behind the opening of Suspense A/c** is to avoid delay in closure of books of accounts and consequently, avoid delay in preparation of Final Accounts.
Later the errors are identified and rectified.
When all the errors affecting the trial balance (one sided errors) are identified and rectified, balance in Suspense Account will become Nil.

^ **Rectification of Errors when there is Suspense A/c**

* **Rectification of Two sided errors :**
No change, follow usual process : pass Rectification entry

* **Rectification of One sided errors :**
Every one-sided error is rectified by passing a Journal entry through Suspense A/c

Q. 3 : Correct the following errors

(i) without opening a Suspense Account and

(ii) opening a Suspense Account:

(a) The Sales Book has been totalled ₹ 100 short.

(b) Goods worth ₹ 150 returned by Green & Co. have not been recorded anywhere.

(c) Goods purchased ₹ 250 have been posted to the debit of the supplier Gupta & Co.

(d) Furniture purchased from Gulab & Bros, ₹ 1,000 has been entered in Purchases Day Book.

(e) Discount received from Red & Black ₹ 15 has not been entered in the Discount Column of the Cash Book.

(f) Discount allowed to G. Mohan & Co. ₹ 18 has not been entered in the Discount Column of the Cash Book. The account of G. Mohan & Co. has, however, been correctly posted.

Q. 4 : The trial balance of Mr. W & H failed to agree and the difference ₹20,570 was put into suspense account pending the investigation which disclosed that:

(i) Purchase returns day book had been correctly entered and totalled at ₹ 6,160, but had not been posted to the ledger.

(ii) Discounts received ₹ 1,320 had been debited to discounts allowed.

(iii) The Sales account had been under added by ₹ 10,000.

(iv) A credit sale of ₹ 1,470 had been debited to a customer account at ₹ 1,740.

(v) A vehicle bought originally for ₹ 7,000 four years ago and depreciated to ₹ 1,200 had been sold for ₹ 1,500 in the beginning of the year but no entries, other than in the bank account had been passed through the books.

(vi) An accrual of ₹ 560 for telephone charges had been completely omitted.

(vii) A bad debt of ₹ 1,560 had not been written off and provision for doubtful debts should have been maintained at 10% of Trade receivables which are shown in the trial balance at ₹ 23,390 with a credit provision for bad debts at ₹ 2,320.

(viii) Tools bought for ₹ 1,200 had been inadvertently debited to purchases.

(ix) The proprietor had withdrawn, for personal use, goods worth ₹ 1,960. No entries had been made in the books.

You are required to give rectification entries without narration to correct the above errors before preparing annual accounts. Also, prepare Suspense A/c

^ **ROE III :** Correction in the **next Accounting Period** / Prior Period **Rectification**

(Rectification of Errors **After the Preparation of** Final Accounts)

Many a times, detection of all errors takes more time and hence, accountant may prepare final accounts, pending rectification of few errors, as it cannot be delayed beyond a point. In such a case, if one or more one sided errors are yet to be rectified, Suspense A/c will show some balance.

Such balance in Suspense A/c is **to be carried forward** to next accounting year.

Accordingly,

if there is debit balance in Suspense A/c, it will be shown on Asset side of BS and

if there is credit balance in Suspense A/c, it will be shown on Liability side of BS.

When such errors are located later on, after preparation of final accounts i.e. in next accounting period, such errors are to be rectified by passing Rectification Entry.

Such Rectification entry will involve Suspense A/c if it is for one sided error and will not involve Suspense A/c if it is for Two sided error. Once all one sided errors are located and rectified, Suspense A/c will tally.

** Such Prior Period Errors **rectification entries** should be **dated FIRST DAY** of the current accounting period. If such error **involves** Fixed Assets A/c, Debtors A/c etc. **it's corresponding effect** on Depreciation, R.D.D. etc. also should be considered.

^ If Rectification is **done after** preparation of Final A/c's **(Prior Period Rectification)**

Pass Usual Rectification entry for rectification of one sided & two sided errors,

except that,

if Usual Rectification Entry involves any Nominal Account ,

it should be replaced by "Profit & Loss Adjustment A/c".

Above is necessary **as otherwise** correction of errors will 'falsify' the P & L A/c of current year.

(If usual rectification entry involves **both** Nominal accounts **only**, no rectification entry to be passed, since rectification is post preparation of final accounts)

Balance in Profit & Loss Adjustment A/c represents change in Net Profit / Net Loss of last year & hence, it should be transferred to Capital A/c.

(where NP / NL of last year was transferred)

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Thus, correction of all amounts concerning nominal accounts, i.e., expenses and incomes should be through a special account styled as "**Prior Period Items**" or "**Profit and Loss Adjustment Account**". The balance in the account should be transferred to the Profit and Loss Account. **However**, these Prior Period Items should be charged **after deriving** the profit of the current year. **'Prior Period items'** are material income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods.

** **Prior Period Items** should be **separately disclosed** in the current year statement **together with** their nature and amount in a manner that **their impact on** current period profit or loss **can be perceived.**

^ **Q. 5 :** The following mistakes were located in the books of a concern after its books were closed and a Suspense Account was opened in order to get the Trial Balance agreed:

(i) Sales Day Book was overcast by ₹ 1,000.
(ii) A sale of ₹ 5,000 to X was wrongly debited to the Account of Y.
(iii) General expenses ₹ 180 was posted in the General Ledger as ₹ 810.
(iv) A Bill Receivable for ₹ 1,550 was passed through Bills Payable Book. The bill was given by P.
(v) Legal Expenses ₹ 1,190 paid to Mrs. Neetu was debited to her personal account.
(vi) Cash received from Ram was debited to Shyam ₹ 1,500.
(vii) While carrying forward the total of one page of the Purchases Book to the next, the amount of ₹ 1,235 was written as ₹ 1,325.

Find out the amount of the Suspense Account and pass entries (without narration) for the rectification of the above errors in the subsequent year's books.

^ **Q. 5 :** In the books of a concern

	ROE I	ROE II	ROE III
i)	Sales Day Book was overcast by Rs. 1,000 (**sided error**)		
ii)	Sales of Rs. 5,000 to X was wrongly debited to the A/c of Y (**sided error**)		
iii)	General expenses of Rs. 180 posted in the General Ledger as Rs. 810 (**sided**)		
iv)	A Bills Receivable of Rs. 1,550 was passed through Bills Payable Book. The bill was given by Mr. P		
v)	Legal expenses Rs. 1,190 paid to Mrs. Neetu debited to her Personal A/c		
vi)	Cash received from Ram was debited to Shyam Rs. 1,500		
vii)	While carrying forward the total of one page of the Purchase Book to the next, the amount of Rs. 1,235 was written off as Rs. 1,325		

Q. 5 : **In the books of a concern**

JOURNAL

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
i)				
ii)				
iii)				
iv)				
v)				
vi)				
vii)				
viii)				

Dr. **Suspense A/c** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

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^ **Q. 6 :** A merchant's trial balance as on June 30, 2022 did not agree. The difference was put to a Suspense Account. During the next trading period, the following errors were discovered:

(i) The total of the Purchases Book of one page, ₹4,539 was carried forward to the next page as ₹4,593.

(ii) A sale of ₹573 was entered in the Sales Book as ₹753 and posted to the credit of the customer

(iii) A return to a creditor, ₹510 was entered in the Returns Inward Book; however, the creditor's account was correctly posted.

(iv) Cash received from C. Dass, ₹620 was posted to the debit of G. Dass.

(v) Goods worth ₹840 were despatched to a customer before the close of the year but no invoice was made out.

(vi) Goods worth ₹1,000 were sent on sale or return basis to a customer and entered in the Sales Book. At the close of the year, the customer still had the option to return the goods. The sale price was 25% above cost.

You are required to give journal entries to rectify the errors in a way so as to show the current year's profit or loss correctly.

^ **Q. 7 :** M/s. Applied Laboratories were unable to agree the Trial Balance as on 31st March, 2020 and have raised a suspense account for the difference. Next year the following errors were discovered:

(i) Repairs made during the year were wrongly debited to the building A/c ₹ 12,500.

(ii) The addition of the 'Freight' column in the purchase journal was short by ₹ 1,500.

(iii) Goods to the value of ₹ 1,050 returned by a customer, Rani & Co., had been posted to the debit of Rani & Co. and also to sales returns.

(iv) Sundry items of furniture sold for ₹ 30,000 had been entered in the sales book, the total of which had been posted to sales account.

(v) A bill of exchange (received from Raja & Co.) for ₹ 20,000 had been returned by the bank as dishonoured and had been credited to the bank and debited to bills receivable account.

You are required to pass journal entries to rectify the above mistakes.

^ **Q. 8 :** Mr. Roy was unable to agree the Trial Balance last year and wrote off the difference to the Profit and Loss Account of that year. Next year, he appointed a Chartered Accountant who examined the old books and found the following mistakes:

(1) Purchase of a scooter was debited to conveyance account ₹3,000.

(2) Purchase account was over-cast by ₹10,000.

(3) A credit purchase of goods from Mr. P for ₹2,000 was entered as a sale.

(4) Receipt of cash from Mr. A was posted to the account of Mr. B ₹1,000.
(5) Receipt of cash from Mr. C was posted to the debit of his account, ₹500.
(6) ₹500 due by Mr. Q was omitted to be taken to the trial balance.
(7) Sale of goods to Mr. R for ₹2,000 was omitted to be recorded.
(8) Amount of ₹2,395 of purchase was wrongly posted as ₹2,593.

Mr. Roy used 10% depreciation on vehicles. Suggest the necessary rectification entries.

^ **Try Yourself : Objectives**

* **State whether the following statements are True or False with reasons.**

1	Trial Balance is prepared from the balance of ledger accounts.
2	A Trial Balance can agree in spite of certain errors.
3	Rectification entries are passed in Cash Book.
4	There is no need to open a Suspense Account if the Trial Balance agrees.
5	All the errors can be rectified only through Suspense Account.
6	Errors of principle is not disclosed by the Trial Balance.
7	Transaction not recorded in the books, is an error of principle.
8	If purchase book is undercasted, purchase account is debited in rectification.
9	When a transaction is not recorded according to the principles of book-keeping, the error is said to be an error of principle.
10	Error of omission is disclosed by the Trial Balance.
11	In case of error of complete omission, the trial balance does not tally.
12	When errors are detected after preparation of trial balance, suspense account is opened.
13	When purchase of an asset is treated as an expense, it is known as error of principle.
14	Trial balance agrees in case of compensating errors.
15	When amount is written on wrong side, it is known as an error of principle.
16	On purchase of old furniture, the amount spent on repairs should be debited to repairs account.
17	Rent paid to landlord of the proprietors house, must be debited to 'Rent account'.
18	If the errors are detected after preparing trial balance, then all the errors are rectified through suspense account.
19	The method of rectification of errors depends on the stage at which the errors are detected.
20	'Profit & Loss Adjustment Account' is opened to rectify the errors detected in the current accounting period.
21	Goods worth ₹ 600 taken by the proprietor for personal use should be credited to Capital Account.

22	If the effect of errors committed cancel out, the errors will be called compensating errors and the trial balance will disagree.
23	Prior period items need not be separately disclosed in the current statement of profit and loss.
24	If the amount is posted in the wrong account or it is written on the wrong side of the account, it is called error of principle.
25	Purchase of office furniture & fixtures of ₹ 2,500 has been debited to General Expense Account. It is an error of omission.
26	Under or over - casting of a subsidiary book is an example of error of commission.
27	The rationale behind the opening of a suspense account is to tally the trial balance.
*	**Answers:**
1	**True**
	A Trial balance is a statement of debit and credit balances extracted from the various accounts in the ledger. All business transactions are recorded first in Journal or in subsidiary books and subsequently they are posted to respective ledger accounts. At the end of the year, they are balanced and transferred to Trial balance.
2	**True**
	Error of principle or error of complete omission or compensatory error is not disclosed by the Trial Balance. It will be agreed with debit and credit balances but there may be certain error.
3	**False**
	Rectification entries are passed in Journal Proper. Cash book is used for recording monetary transactions and not for rectification of errors.
4	**True**
	When the Trial Balance does not tally, a temporary account called as Suspense A/c is opened to balance trial balance. So when trial balance agrees, there is no need to open Suspense Account.
5	**False**
	The errors of principle, errors of complete omission (two sided errors) can be rectified by passing entries. So all the errors can not be rectified through suspense account.

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6	**True**
	Error of Principle are those where some basic principle of book keeping and accountancy are not properly followed while recording a business transaction. Such errors can be rectified by passing journal entries.
	Eg. Capital expenditure shown as revenue expenditure or vice-a -versa. It won't affect Trial balance.
7	**False**
	Transaction not recorded in the books is an error of omission and not an error of principle.
8	**True**
	Purchase is an expense. All expenses are debited as per rule of nominal account. When purchase book is under casted, it can be corrected by debiting Purchase A/c.
9	**True**
	Error of Principle are those where some basic principle of book - keeping and accountancy are not properly followed while recording a business transaction.
	Eg. : Capital expenditure shown as revenue expenditure or Vice-a-Versa.
	They are called as an error of principle.
10	**False**
	Complete omission of a transaction will not be disclosed by the trial balance.
	In Trial balance, balances will be agree with such errors. So omission of transaction or an error of omission will not be disclosed by Trial Balance.
11	**False**
	In case of error of complete omission, the trial balance tallies.
12	**True**
	In order to balance the difference of balances in the trial balance suspense account is opened.
13	**True**
	Where the accounts being debited is principally incorrect it is termed as error of principle.

14	**True**
	Compensating errors cancel out each other when trial balance is prepared as the mistake pertains to the same amount being credited & later debited on account of two different mistakes.
15	**False**
	When amount is written on wrong side, it is known as an error of commission.
16	**False**
	On purchase of furniture, the amount spent on repairs should be debited to furniture account as it is a capital expense.
17	**False**
	Rent paid to land lord of the proprietors house, must be debited to 'Drawings account'.
18	**False**
	If the errors are detected after preparing trial balance, then all the errors are not rectified through suspense account. There may be principal errors, which can be rectified without opening a suspense account.
19	**True**
	There are 3 different stages when the mistakes are identified and then the rectification depends on the stage of identification of errors.
20	**False**
	'Profit & Loss adjustment account' is opened to rectify the errors detected in the next accounting period.
21	**False**
	Goods taken by the proprietor for personal use should be credited to Purchases Account as less goods are left in the business for sale.
22	**False**
	If the effect of errors committed cancel out, the errors will be called compensating errors and the trial balance will agree.

23	**False**
	Prior Period Items should be separately disclosed in the current statement of profit and loss together with their nature and amount in a manner that their impact on current profit or loss can be perceived.
24	**False**
	If an amount is posted in the wrong account or is written on the wrong side of the correct account, it is case of "errors of commission".
25	**False**
	When a transaction is recorded in contravention of accounting principles, like treating the purchase of an asset as an expense, it is an error of principle. Purchase of office furniture and fixtures is a capital expenditure, if debited to General Expenses account, is an error of principle and not an error of omission.
26	**True**
	If an amount is posted in the wrong account or it is written on the wrong side or the totals are wrong or a wrong balance is struck, it will be a case of "errors of commission." Thus, under or over casting of subsidiary books is an example of error of commission.
27	**False**
	The rationale behind the opening of a suspense account is to avoid delay in the preparation of financial statements.
*	**Multiple Choice Questions**
1	If a purchase return of ₹1,000 has been wrongly posted to the debit of the sales returns account, but has been correctly entered in the suppliers' account, the total of the
	(a) Trial balance would show the debit side to be ₹ 1,000 more than the credit.
	(b) Trial balance would show the credit side to be ₹ 1,000 more than the debit.
	(c) The debit side of the trial balance will be ₹ 2,000 more than the credit side.
2	If the amount is posted in the wrong account or it is written on the wrong side of the account, it is called
	(a) Error of omission. (b) Error of commission. (c) Error of principle
3	₹ 200 paid as wages for erecting a machine should be debited to
	(a) Repair account. (b) Machine account. (c) Capital account.

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4	On purchase of old furniture, the amount of ₹ 1,000 spent on its repair should be debited to
	(a) Repair account. (b) Furniture account. (c) Cash account.
5	Goods worth ₹ 50 given as charity should be credited to
	(a) Charity account. (b) Sales account. (c) Purchase account.
6	Goods worth ₹100 taken by proprietor for domestic use should be credited to
	(a) Sales account. (b) Proprietor's personal expenses. (c) Purchases account
7	Sales of office furniture should be credited to
	(a) Sales Account. (b) Furniture Account. (c) Purchase Account.
8	The preparation of a trial balance is for:
	(a) Locating errors of commission.
	(b) Locating errors of principle.
	(c) Locating clerical errors.
9	₹ 200 received from Smith whose account, was written off as a bad debt should be credited to:
	(a) Bad Debts Recovered account. (b) Smith's account. (c) Cash account.
10	Purchase of office furniture ₹ 1,200 has been debited to General Expense Account. It is :
	(a) A clerical error. (b) An error of principle. (c) An error of omission.
11	Goods purchased from A for ₹ 10,000 passed through the sales book. The error will result in :
	(a) Increase in gross profit
	(b) Decrease in gross profit
	(c) No effect on gross profit
12	Rectification entries are passed in_____.
	(a) Journal Proper (b) Ledger (c) Balance Sheet
13	The type of error for which journal entry is always required for rectification_____.
	(a) one sided error (b) two sided error (c) none

14 Error occurred due to wrong posting are called error of_____.

(a) principal (b) commission (c) compensating

15 If transaction is totally omitted from the books, it is called _____.

(a) Error of omission (b) Error of recording (c) Error of commission

16 Suspense Account is opened when _____does not tally.

(a) Balance sheet (b) Profit and loss Account (c) Trial Balance

17 Wages paid for installation of machinery wrongly debited to wages account is an error of _____.

(a) omission (b) principle (c) commission

18 If the trial balance shows a short credit the suspense account will have a_____balance.

(a) debit (b) zero (c) credit

19 If the trial balance does not agree the difference of the trial balance is placed in account.

(a) Personal (b) Suspense (c) Rectification

20 Errors which compensate the effect of each other are called _____errors.

(a) compensating (b) one sided (c) two sided

21 One sided errors are disclosed by_____.

(a) Trial Balance (b) Journal (c) Ledger Account

Answers :

1	(c)		**6**	(c)		**11**	(a)		**16**	(c)		**21**	(a)
2	(b)		**7**	(b)		**12**	(a)		**17**	(b)			
3	(b)		**8**	(c)		**13**	(b)		**18**	(c)			
4	(b)		**9**	(a)		**14**	(b)		**19**	(b)			
5	(c)		**10**	(b)		**15**	(a)		**20**	(a)			

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Dec'23



BHAVIK DOSHI

357/400



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



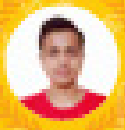
KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

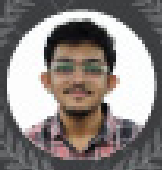
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June 22 & June 23



340/400

HARSH GULWANI
CA Foundation June'22



MEET SHAH
CA Foundation June'23
331



NISHIT KAPUR
CA Foundation June'23
328



PALAK JAJODIA
CA Foundation June'23
325



SWASTIKA SINGH
CA Foundation June'22
323



SUKUNJ GUPTA
CA Foundation June'22
323



DURGASHRI VS
CA Foundation June'22
319



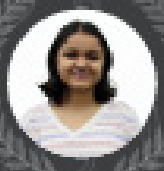
VARUN ADWANI
CA Foundation June'22
319



KARTIK LADHANI
CA Foundation June'22
316



RIDHI PAREKH
CA Foundation Dec'22
314



SMEET LADHANI
CA Foundation June'23
313



TANMAY AGARWAL
CA Foundation June'23
311



GARV KHANDELWAL
CA Foundation June'22
308



DAKSH JAIN
CA Foundation June'23
308



DEEPAK GURNANI
CA Foundation June'22
305



PARIDHI JHAWAR
CA Foundation June'22
304



SATYA BHANUSHALI
CA Foundation June'23
304

and many more...

ALL INDIA RANKERS CA INTER | MAY'22 & MAY'23 NOV'23



JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
CA INTER MAY'23
AIR 34



HIMANSHI CHHAJED
CA INTER MAY'23
AIR 39



YUKTA SATPALKAR
CA INTER MAY'22
AIR 40



MANVI LODHA
CA INTER MAY'23
AIR 40



ARYAN HOSANGADY
CA INTER MAY'22
AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MUNDRA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHRUTI SHIVARAM
CA INTER NOV'23
AIR 47

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AIR 6



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CA FINAL NOV'23
AIR 8



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AIR 17



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CA FINAL MAY'22
AIR 20



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CA FINAL MAY'22
AIR 22



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CA FINAL NOV'23
AIR 32



PINAL KHETAN
CA FINAL NOV'23
AIR 35



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CA FINAL MAY'22
AIR 39



DEEPAK LADHA
CA FINAL NOV'23
AIR 40



HIMANSHU KHATRI
CA FINAL MAY'22
AIR 41



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AIR 45



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SCAN ME!

Introduction

In modern times, large number of business transactions are made on credit basis.
When goods or services are obtained and payment will be made in future,
it is known as **credit transaction**.
Credit transactions **plays significant role** in the world of business.
Credit **motivates the customers** to increase the amount of their spending.
Moreover, business enterprises offer credit **to gain a competitive advantage** in the market.

To balance the potential for increased sales with the risk of decreased cash flow and large outstanding debts, the seller requires some sort of promise or commitment from the customer that he would pay the amount of goods due from him on a particular date in future.
In such a case, the seller would like to get a **written undertaking** from the buyer to get the payment after a fixed specified period.
As such, the seller **prepares a document** in which he puts in writing all the terms and conditions relating to sale of goods such as amount required to be paid, date of payment, place of payment and other relevant details.
Seller **signs such document** and sends it to buyer for **his acceptance (signature)**.
Buyer puts his signature on the document and it is known as **'Bill of Exchange'**

The bills of exchange are **instruments of credit** which facilitate the credit sale of goods.
BOE along with Promissory Note & Cheque are called **Negotiable Instruments** (NI) and are governed by the **Indian Negotiable Instruments Act, 1881**.
Such Act **has defined Negotiable Instrument** as follows
"Negotiable Instrument means a Bill of Exchange, Promissory Note or Cheque payable either to bearer or to order."

Bill of Exchange (BOE)

Section 5 of the Indian Negotiable Instruments Act, 1881 defines a BOE as follows.
A Bill of Exchange
* is an instrument in writing,
* containing an unconditional order,
* signed by the maker,
* directing a certain person to pay certain sum of money
* only to, or to the order of, a certain person
* or to the bearer of the instrument.

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* **Ex.** Prepare a bill of exchange from the following details.

(1) Drawer : Ms. Sucheta Gujarathi, Panama Apt., Dwarka, Nashik.
(2) Drawee : Vishal Bhardwaj, 506, Matange Colony, Satara.
(3) Period : 3 months
(4) Amount : ₹ 35,000
(5) Date of bill : 22nd August, 2022.
(6) Accepted on : 25th August, 2022.

BILL OF EXCHANGE

Ms. Sucheta Gujarathi,
STAMP — Panama Apt.,
Dwarka, Nashik.
₹ 35,000 — Date : 22nd August, 2022

Three months after date pay to me or my order the sum of Rupees Thirty Five Thousand only, for the value received.

Sd/-
(Ms. Sucheta Gujarathi)

To,
Vishal Bhardwaj,
506, Matange Colony,
Satara.

"Accepted"
Sd/-
(Vishal Bhardwaj)
Date : 25th August, 2022.

^ **Features of BOE**

1. It is drawn (prepared) and signed by the maker, called as **Drawer** of the bill.
He is the person who has granted credit to the person on whom the BOE is drawn.
In credit sales, seller of the goods draws the bill on buyer of the goods.
In above example, Mr. Prakash Rao is the drawer of the bill.

2. It must be **accepted** by the the person on whom such bill is drawn, to make it a legal document. Such person who accepts the bill drawn by the drawer is called the **Drawee** of the bill. In above example, Mr. Rahul Deo is the drawee of the bill.
Before acceptance of such bill by the drawee, it is called draft.
It becomes legal document (BOE) **only on its** acceptance by the drawee.

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3. A BOE is a written order.

4. It is an unconditional order to the drawee to pay the specified amount.

5. The specified amount is payable to the person named in the bill or to his order . or to the bearer. Such person to whom amount of the bill is to be paid is called **Payee**.

* Payee may be the drawer himself **or** a third person.

6. The last words in description **'for value received'** indicate that the bill is being drawn by the drawer on the drawee in consideration of the goods sold to the drawee on credit.

^ **Payee of the Bill**

= Holder of the bill on the due date of the bill.

Drawer of the bill has **following 4 options** to deal with the bill.

* **Option I**

He can **retain the bill** till maturity / due date with himself in which case he will be the **Payee**, as he is the holder of the bill on due date of the bill.

* **Option II**

He can **discount the bill** with the bank. BOE serves as a source of finance for the drawer. He need not wait till the due date of the bill to get the amount. If he needs money before the due date, he can get the bill discounted with the bank.
Bank deducts charges called as 'Discounting Charges' & gives balance amount to the drawer. Such charges depends upon the rate of interest & the period left for maturity.

In such case, bank will be the **Payee**, as bank will be the holder of the bill on due date of the bill.

* **Option III**

He can **endorse the bill** in favour of a creditor. The person who endorses the bill is called the **endorser**. The person in favour of whom bill is endorsed is called the **endorsee**. In such case, endorsee / creditor will be the **Payee**, as he will be the holder of the bill on due date of the bill.

* **Option IV**

He can send the bill to **bank for collection**.

In such case, bank will retain the bill in it's safe custody till the due date and present it for payment on due date. Bank will credit the amount in the account of the customer (drawer) after deduction of service charges, if any.

^ **Due date of the bill** or **Maturity Date**

* Due date is the date on which the payment of the bill is due.

It is the date on which drawee of the bill is liable to pay amount of the bill to the payee of the bill. It is also known as date of maturity.

* Due date calculation **depends upon** the type of bill.

Bill after date or **Bill after sight**

^ **Bill after date** is the bill in which the period is counted from the **date of drawing** of the bill.

^ **Bill after sight** is the bill in which the period is counted from the **date of acceptance** of the bill.

* In both the above cases,

3 Days of Grace are added to the period of bill to calculate the due date of the bill.

^ Following points to be remembered **while calculating** due date of the bill

* **When the period of the bill is stated in days,**

the calculation of maturity date will be in days.

Date of transaction to be excluded and date of payment to be included.

For eg. A bill dated 01.01.21 is payable 60 days after date.

Add 63 days (including 3 days of grace) to calculate the due date.

Due date = 30 days of Jan. + 28 days of Feb. + 5 days of Mar. = **5th March**

(**2021** : not leap year)

* **When the period of the bill is stated in months,**

the calculation of due date will be in months, ignoring the number of days in a month.

For eg. A bill dated 01.01.21 is payable 3 months after date.

Due date = 01.01.21 + 3 months = 01.04.21 + 3 days of grace = **04.04.21**

* If the maturity date falls on **sunday** or **public holiday,**
it should be taken as **immediately preceding** working day.

* If the maturity date is declared as **emergency holiday**,
it should be taken as **immediately following** working day.

* Date calculated **without adding** days of grace is called as **Nominal Due Date**.

* Date calculated **after adding** days of grace is called as **Due Date (Legal Due Date)**.

^ **Accounting for Bills of Exchange**

Books of Drawer (seller) (eg. Mr. A)	**Books of Drawee** (buyer) (eg. Mr. B)

* **Basic Transactions**

1 For **goods sold** by Mr. A to Mr. B on credit basis ₹ 50,000

2a) For **bill drawn** by Mr. A and sent to Mr. B for his acceptance

2b) For **bill accepted** by Mr. B and returned to Mr. A

* **Treatment of bill by the Drawer** (4 options / 4 cases)

3 **Case I :** Mr. A **retains the bill** with himself till the due date of the bill

3 **Case II :** Mr. A **discounts the bill** with the bank for ₹ 49,000

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3 **Case III** : Mr. A **endorses the bill** to his creditor Mr. C

3 **Case IV** : Mr. A sends the bill to **bank for collection**

* **Honour of the bill on due date**

When drawee of the bill **pays** the amount of the bill **on** the due date of the bill **to** the holder of the bill, bill is said to be **honoured**.

Books of Drawer (seller) (Mr. A)	**Books of Drawee** (buyer) (Mr. B)

4 **Case I** : Honour of **Retained Bill**

4 **Case II** : Honour of **Discounted Bill**

4 **Case III :** Honour of **Endorsed Bill**

4 **Case IV :** Honour of **B.F.C. Bill,** bank charges charged by bank ₹ 475

* **Retirement of the bill**

When drawee of the bill **pays** the amount of the bill **before** the due date of the bill, bill is said to be **retired**. If drawee wishes to pay the amount of the bill before due date, it is called **Retiring the bill**. Usually, the holder of the bill, in such case, would be willing to allow a reduction in amount, may be to the extent of interest, for early payment. Such reduction is called **Rebate**.

Books of Drawer (Mr. A)	Books of Drawee (Mr. B)
Retirement of **Retained Bill**	For **Payment of Liability** before due date
Retirement of **B.F.C. Bill**	

* **Dishonour of the bill on due date**

When drawee of the bill **does not pay** the amount of the bill on the due date of the bill, bill is said to be dishonoured.

Noting and Protesting of bill

To **establish the fact** that the bill was properly presented for payment to the drawee and was dishonoured, the bill is again presented for payment through a person called **Notary Public** (an official appointed under law). On drawee refusing to make the payment of bill, the notary public notes down the fact of dishonour of bill. Such act of notary public is called **"Noting"**. For rendering these services, notary public charges a small fee called **Noting Charges**. Noting charges is the fees paid to the notary public for authenticating the fact of dishonour of bill.

Noting will consist of the following

i) That the bill has been dishonoured
ii) The date of the dishonour
iii) The reason, if any, for the dishonour
iv) The fee charged by the notary public i.e. Noting charges

Thus, **Noting** is the process of recording the fact and reasons of dishonor by the notary public.

Protest is **a certificate** issued by a notary public **attesting the fact** of dishonour recorded upon the Instrument.

^ **Who pays the Noting Charges to the notary public ?**

^ **Is Holder of the bill liable to bear Noting Charges ?**

^ **Who finally bears Noting Charges ?**

^ **Noting Charges are expense for whom ?**

Books of Drawer (Mr. A)		Books of Drawee (Mr. B)		
	Dishonour of bill & noting charges	**1234**	**Dishonour of bill & noting charges**	
1234	**B's A/c (bill + noting charges) Dr.**		Bills Payable A/c (bill)	Dr.
1	To Bills Receivable A/c (bill amount)		Noting Charges A/c	Dr.
	To Cash / Bank A/c (noting charges)		**To A's A/c (bill + noting charges)**	
	or			
2	To Bank A/c (bill + noting charges)			
	or			
3	To C's A/c (bill + noting charges)			
	or			
4	To Bill sent for collection A/c (bill)			
	To Cash / Bank A/c (noting charges)			

^ **Q. 1 :** Pankaj purchased goods of ₹ 20,000 from Omprakash on credit on 15th April 2019. Omprakash draws After Sight bill for the amount due on Pankaj for 3 months which was accepted by Pankaj on 18th April, 2019. On 20th April, 2019, Omprakash endorsed the bill to his creditor Jagdish in full settlement of his amount ₹ 21,000. On the due date, the bill was dishonoured by Pankaj.
Give Journal Entries in the books of Omprakash, Pankaj and Jagdish.

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* Renewal of Bill

= Dishonour (cancellation) of existing bill (by mutual consent)

\+

Acceptance of new bill

An accepter of bill (drawee) may not be able to meet (honour) the bill on the due date and may request to renew the bill. **The purpose is to get extension of time.** If the drawer agrees, the old (existing) bill is cancelled and new bill is drawn & accepted by the drawee. This **process** is called **Renewal of the bill**.
In such case, bill may not be **noted** as drawee himself makes the request for cancellation of old bill.

Normally, drawer may agree for renewal of the bill, subject to one or more of the following terms.

i) New bill **may not be** for full amount due. Drawer may insist upon drawee to make part payment immediately & for balance amount due, new bill can be drawn & accepted.
ii) Drawer will charge **Interest** for the extension of time. Such Interest will depend on the amount of new bill, rate of interest and period of such new bill.
iii) **The amount of Interest** may be paid in cash immediately or may get added in new bill amount, as may be mutually decided between drawer and drawee.

^ Journal entries on renewal of the bill

	Books of Drawer (Mr. A)		Books of Drawee (Mr. B)
1	For dishonour / cancellation of old bill	1	For dishonour / cancellation of old bill
2	For Interest due / receivable	2	For Interest due / payable
3	For receipt of part amount	3	For payment of part amount
4	For receipt of B's acceptance (new bill)	4	For new bill accepted and returned to A

^ **Q. 2 :** On 12th May, 2020 A sold goods to B for ₹ 36,470 and drew upon the later two bills one for ₹ 16,470 at one month and the other for ₹ 20,000 at three months.
B accepted both the bills.
On 5th June, 2020 A sent both the bills to his banker for collection on the due dates.
The first bill was duly met. But due to some temporary financial difficulties, B failed to honour the second bill on the due date and the bank had to pay ₹ 20 as noting charges.
However, on 16th August, 2020 it was agreed between A & B that B would immediately pay ₹ 8,020 in cash and accept a new bill at 3 months for ₹ 12,480 which included interest for postponement of the part payment of the dishonoured bill. A immediately sent new acceptance to its bank for collection on the due date. On 1st October, 2020, B approached A offering ₹ 12,240 for retirement of his acceptance.
A accepted the request.
Pass journal entries of all the above transactions in the books of A.

^ **Q. 3 :** Journalise the following transactions in K. Katrak's books.

(i) Katrak's acceptance to Basu for ₹ 2,500 discharged by a cash payment of ₹ 1,000 and a new bill for the balance plus ₹ 50 for interest.

(ii) G. Gupta's acceptance for ₹ 4,000 which was endorsed by Katrak to M. Mehta was dishonoured. Mehta paid ₹ 20 noting charges. Bill withdrawn against cheque.

(iii) D. Dalal retires a bill for ₹ 2,000 drawn on him by Katrak for ₹ 10 discount.

(iv) Katrak's acceptance to Patel for ₹ 5,000 and Mody's acceptance to Katrak for a similar amount were duly discharged.

^ **Q. 4 :** Journalize the following in the books of Don :

(i) Bob informs Don that Ray's acceptance for ₹ 3,000 has been dishonoured and noting charges are ₹ 40. Bob accepts ₹ 1,000 cash and the balance as bill at three months at interest of 10%. Don accepts from Ray his acceptance at two months plus interest @ 12% p.a.

(ii) James owes Don ₹ 3,200; he sends Don's own acceptance in favour of Ralph for ₹ 3,160; in full settlement.

(iii) Don meets his acceptance in favour of Singh for ₹ 4,500 by endorsing John's acceptance for ₹ 4,450 in full settlement.

(iv) Ray's acceptance in favour of Don retired one month before due date, interest is taken at the rate of 6% p.a.

* **When Drawee is declared Insolvent / Bankrupt**

Books of Drawer (Mr. A)			Books of Drawee (Mr. B)		
1			1		
2	For final settlement		2	For final settlement	

^ **Q. 5 :** Mr. David draws two bills of exchange on 1.1.2022 for ₹ 6,000 and ₹ 10,000. The bills of exchange for ₹ 6,000 is for two months while the bill of exchange for ₹ 10,000 is for three months. These bills are accepted by Mr. Thomas. On 4.3.2022, Mr. Thomas requests Mr. David to renew the first bill with interest at 18% p.a. for a period of two months. Mr. David agrees to this proposal. On 20.3.2022, Mr. Thomas retires the acceptance for ₹ 10,000, the interest rebate i.e. discount being ₹ 100. Before the due date of the renewed bill, Mr. Thomas becomes insolvent and only 50 paise in a rupee could be recovered from his estate.
You are to give the journal entries in the books of Mr. David.

^ **Q. 6 :** Rita owed ₹ 1,00,000 to Siriman. On 1st October, 2021, Rita accepted a bill drawn by Siriman for the amount at 3 months. Siriman got the bill discounted with his bank for ₹ 99,000 on 3rd October, 2021. Before the due date, Rita approached Siriman for renewal of the bill. Siriman agreed on the conditions that ₹ 50,000 be paid immediately together with interest on the remaining amount at 12% per annum for 3 months and for the balance, Rita should accept a new bill at three months. These arrangements were carried out. But afterwards, Rita became insolvent and 40% of the amount could be recovered from her estate.
Pass journal entries in the books of Rita.

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Accommodation Bills

Bills of exchange are usually drawn to facilitate trade transaction, i.e. bills are meant to finance actual purchase and sale of goods. But the mechanism can be used to raise finance also.

An accommodation bill is a bill which is drawn and accepted or endorsed **not** in the ordinary course of business, but for the **specific purpose of temporary financial help** of one party or both the parties.

In case of an accommodation bill, the relationship between drawer and acceptor is not that of a creditor and debtor because an accommodation bill is **not** supported by any genuine transaction.

Q. 7 : Anil draws a bill of 3 months for ₹ 24,000 and Sunil accepts the same for mutual accommodation of both in the ratio of 2 : 1. Anil discounts the bill for ₹ 22,200 and remits 1/3 of the proceeds to Sunila. Before the due date Sunil draws another bill of 3 months for ₹ 36,000 on Anil in order to provide funds to meet the first bill.
The second bill is discounted for ₹ 34,800 and a sum of ₹ 7,200 is remitted to Anil after meeting the first bill. The second bill is duly met.
Show the Journal Entries in the book of Chanda and Usha.

Q. 8 : Anil draws a bill of Rs. 90,000 on Sanjay on 1 st April for 3 months.
After Sanjay's acceptance, Anil discounts it with his bank for Rs. 88,200 and remits 1/3 rd of the amount to Sanjay.
On the due date, Anil fails to remit the amount due to Sanjay, but he accepts a bill for Rs. 1,26,000 for 3 months, which Sanjay discounts for Rs. 1,23,300 and remits Rs. 38,640 to Anil.
Before the maturity of the new bill, Anil becomes insolvent and only 40% was realised from his estate on 15 th October. Pass necessary Journal entries in the books of Anil.

Q. 9 : On 1 st January, Vinod drew & Pramod accepted a bill at 3 months of Rs. 2,000.
Vinod discounted the bill with bank at 15% p.a. & remitted half the proceeds to Pramod.
On 1 st February, Pramod drew and Vinod accepted a bill at 4 months for Rs. 1,500.
On 4 th February, Pramod discounted the bill at 15% p.a. with his bank and remitted half of the proceeds to Vinod. They both agreed to share the discount equally.
At maturity, Vinod met his acceptance but Pramod dishonured & Vinod had to pay the bill.
Vinod drew and Pramod accepted a new bill at 3 months for the original bill plus interest at 18% p.a.
On 1 st July, Pramod became Insolvent and only 50 paise in a rupee was recovered.
Record the above transactions in Vinod's Journal.

^ **Q. 10 :** On 1st July, 2022 Gorge drew a bill for ₹ 1,80,000 for 3 months on Harry for mutual accommodation. Harry accepted the bill of exchange. Gorge had purchased goods worth ₹ 1,81,000 from Jack on the same date. Gorge endorsed Harry's acceptance to Jack in full settlement. On 1st September, 2022, Jack purchased goods worth ₹ 1,90,000 from Harry. Jack endorsed the bill of exchange received from Gorge to Harry and paid ₹ 9,000 in full settlement of the amount due to Harry. On 1st October, 2022, Harry purchased goods worth ₹ 2,00,000 from Gorge. Harry paid the amount due to Gorge by cheque.

Give the necessary Journal Entries in the books of Harry, Gorge and Jack.

* **Additional Theory**

^ Types of Bill of Exchange

(1) **Trade Bill :** A bill of exchange which is drawn by a creditor on his debtor with valuable consideration is known as trade bill. It is a bill drawn and accepted for genuine trade transactions.

(2) **Accommodation Bill :** A bill of exchange which has been drawn for mutual financial accommodation of parties involved in is known as accommodation bill. Such bills are drawn and accepted without any valuable consideration. The main objective of such bill is to oblige friends.

(3) **Inland Bill :** A bill of exchange which is drawn between two parties that are located or reside in the same country and thus, are made payable in the same country is known as inland bill of exchange.

(4) **Foreign Bill :** A bill which is drawn in one country and made payable in another country is known as foreign bill. For example, a bill drawn in India and is made payable in Australia or vice versa.

* **A further classification of Bill of Exchange are as follows**

(i) After Date Bill : After date bill is payable at a fixed period. The due date of this bill is calculated from the date of drawing. Grace period of three days are allowed on these bills.

ii) **After Sight Bill :** The due date of this bills calculated from the date of acceptance. Grace period of three days are allowed on these bills.

(iii) **Bill payable on Demand or At sight :** These bills are payable immediately on presentation to the Drawee. Time period is not mentioned for these bills. Also grace days are not allowed for such bills.

^ **Types of Acceptance :**

(1) **General Acceptance :** When the Drawee accepts the draft without any changes or condition, it is called general acceptance or unconditional acceptance.

(2) **Qualified Acceptance :** When Drawee accepts the bill with certain qualifications, to the order of the Drawer, it is called qualified acceptance.

^ **Following are the types of qualified Acceptance :**

(1) **Qualified as to time :** When Drawee accepts the bill subject to change in tenure or term of bill it is known as qualified acceptance as to time.

(2) **Qualified as to Place :** When the Drawee mentions that bill will be payable at a particular place only, it is known as qualified acceptance as to place.

(3) **Qualified as to amount :** When the Drawee accepts the bill, for a part of the amount of the bill it is known as qualified as to amount.

(4) **Qualified as to parties :** When the Drawee is not ready to pay the amount of bill to the payee named in the bill, it is known as qualified acceptance as to parties.

(5) **Qualified as to condition :** When the Drawee accepts the bill subject to certain conditions being fulfilled by the Drawer it is known as qualified acceptance as to conditions.

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^ **Promissory Notes**

A promissory note is an instrument in writing, not being a bank note or 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. Under Section 31(2) of the Reserve Bank of India Act a promissory note cannot be made payable to bearer.

A promissory note has the following characteristics:

1. It must be in writing.
2. It must contain a clear promise to pay. Mere acknowledgement of a debt is not a promissory note.
3. The promise to pay must be unconditional. "I promise to pay ₹ 50,000 as soon as I can" is not an unconditional promise.
4. The promiser or maker must sign the promissory note.
5. The maker must be a certain person.
6. The payee (the person to whom the payment is promised) must also be certain.
7. The sum payable must be certain. "I promise to pay ₹ 50,000 plus all fine" is not certain.
8. Payment must be in legal currency of the country.
9. It should not be made payable to the bearer.
10. It should be properly stamped.
11. It does not require any acceptance.

Specimen of promissory note :

A Promissory Note		
₹ 10,00,000/- only	Rohan 77, Sector-12, Ghaziabad March 01, 2022	
Three months after date I promise to pay Priya or her order the sum of ₹ Ten lakh only, for value received.		
To, Priya		
S-11, Rohini, Delhi.	Stamp	
	(Rohan)	

** **Note :**

Accounting Entries for Promissory Note **will be similar to** that of Bills of Exchange.

A party which **receives** a Promissory Note or **receives** an accepted Bill of Exchange will treat it as Bills Receivable.

A party which **issues** a Promissory Note or **accepts** a Bill of Exchange will treat it as **Bills Payable**.

^ **Differences -** Bill of Exchange and Promissory Note

	Bill of Exchange	Promissory Note
1	A bill contains an order to pay	A promissory note contains only a promise to pay certain sum of money
2	There are generally 3 parties (Drawer, Drawee and Payee) in bill of exchange	There are 2 parties (Maker and Payee) in promissory note
3	A bill is paid by acceptor	A promissory note is paid by maker
4	A bill is drawn by creditor	A promissory note is made by debtor
5	The drawer and payee may be same person in case of bill of exchange	In promissory note maker and payee cannot be same person
6	In a bill of exchange the liability of drawer is secondary and conditional. He will be liable only in case the acceptor does not honour the bill.	In a promissory note the liability of a maker is primary and absolute.
7	A bill of exchange can be accepted conditionally.	A promissory note cannot be made conditionally
8	In a bill of exchange, notice of dishonour must be given	Notice of dishonour is not required in case of promissory note
9	In case of dishonour, a bill of exchange must be noted and protested	Noting and protest is not required in case of dishonour of a promissory note.

Try Yourself : Objectives

* **State whether the following statements are True or False with reasons :**

1. Inland bill is one which is drawn in one country and payable in another country.
2. Retirement of bill means payment of the bill before due date.
3. Drawee can transfer the ownership of Bill.
4. Acceptance of bill without making any changes in the terms of bill is called qualified acceptance.
5. Discounting is a device to convert the bill into its present value.
6. A bill of exchange must be presented to the acceptor on the due date.
7. If a bill is discounted by the holder, no entry is passed in his book when bill is honoured on the due date.
8. Noting charges are to be borne by the drawer.
9. If a bill is drawn payable "on demand" no grace days are allowed.
10. There are three parties to a Promissory Note.
11. Honour of bill means payment in accordance with the apparent tenor of the bill.
12. Endorsement means transfer of title of bill from debtor to creditor.
13. Noting charges are payable to the Notary Public on honour of a bill.

14	Renewal is a request by drawee to extend the credit period of the bill.
15	A bill can't be deposited into bank for collection.
16	A bill of exchange is signed by the person on whom it is drawn.
17	Drawee has no right to discount the bill with the bank.
18	When the amount of the bill is paid on due date, it is said to be retired.
19	Bills payable account is a nominal account.
20	Promise to pay is included in a bill of exchange.
21	Days of rebate are added to the due date to arrive at the maturity date.
22	Discount at the time of retirement of a bill is a gain for the drawee.
23	Foreign bill is drawn in the country and payable outside the country.
24	Promissory note is different from bill of exchange because the amount is paid by the maker in case of former and by the acceptor in the later.
25	A has drawn a bill on B. B accepts the same and endorses the bill to C.
26	A bill given to a creditor is called bills payable.
27	In case of bill of exchange, the drawer and the payee may not be the same person but in case of a promissory note, the maker and the payee may be the same person.
	Answers
1	**False**
	Inland bill is one which is drawn in one country and payable in the same country.
2	**True**
	Retirement of bill means payment of bill before its due date at rebate.
3	**False**
	Drawee has no right to transfer the ownership of bill. Drawer or Holder of bill has right to discount or endorse the bill (transfer the ownership of bill).
4	**False**
	Acceptance of bill without making any changes in the terms of bill is called general acceptance and not qualified acceptance.
5	**True**
	Discounting is a device to convert the bill into its present value. Discounting means selling the bill to bank at discount to meet the present financial needs.
6	**True**
	A bills of exchange must be presented by holder to the accepter on due date for payment purpose. Acceptor of bill is supposed to make payment on due date.

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7	**True**
	Holder of the bill is not supposed to pass any entry in his books when discounted bill is honoured. Holder has already passed entry when the bill was discounted.
8	**False**
	Noting charges are paid by holder of the bill when it is dishonoured, but it is borne by drawee. Holder of the bill (bank or endorsee) will recover it from drawer who will eventually recover it from drawee.
9	**True**
	A demand bill or at sight bill is that bill which does not specify any period. It is presented by holder at any time and because of this, no days of grace are allowed to such bill.
10	**False**
	There are only two parties to a promissory note i.e. Maker / Promisor and Payee / Promisee. There are three parties to Bill of Exchange.
11	**True**
	Honour of bill means payment of bill on due date by the drawee to the holder of the bill. Drawee is supposed to honour the bill when the period of bill is expired.
12	**True**
	Endorsement means transfer of ownership of bill by signing on its back by the debtor to creditor in settlement of dues payable to creditors.
13	**False**
	Noting charges are payable to Notary public, a government officer for noting the fact of dishonour of bill. It is paid by holder and borne by drawee.
14	**True**
	In case of renewal of bill, the drawee is requesting to cancel the original bill and to extend its credit period by drawing new bill.
15	**False**
	A drawer of the bill can take the benefit of services provided by bank to collect the bill. A bill can be deposited into bank for collection purpose before its due date.

16	**False**
	A bill of exchange is signed by the drawer of the bill as the drawer gives order in writing to pay the amount of bill after certain period. Drawee is accepting the bill and not signing the bill.
17	**True**
	Holder of the bill can discount the bill before its due date in the bank. Drawee is a person who has to pay the bill and hence he has no right to discount the bill.
18	**False**
	When the amount of the bill is paid on due date, it is said to be honour of bill. Retirement means payment of bill before due date at rebate.
19	**False**
	The bills payable account is a personal account that represents a liability.
20	**False**
	Bill of exchange contains an order to pay the required amount and not a mere promise to pay.
21	**False**
	3 Days of grace are added to the due date to arrive at the maturity date.
22	**True**
	Discount at the time of retirement of a bill is a gain for the drawee and loss for the drawer.
23	**True**
	When a bill is drawn in the country and is payable outside the country it is termed as a foreign bill.
24	**True**
	In case of the promissory note, it is generally the maker who makes the payment, but in case of the bill of exchange, the person accepting the bill shall be liable to make the payment to the holder of the bill.
25	**False**
	B cannot endorse the bill to C as he is a drawee. Only A, the drawer can do so.

26 True

A bill given to a creditor is called Bills Payable as the debtor commits to pay by giving a bill to creditor.

27 False

The drawer and payee may be same person in case of bill of exchange whereas in promissory note maker and payee can't be same person.

* **Multiple Choice Questions**

1 On 1.1.2022, A draws a bill on B for ₹ 1,20,000 for 3 months' maturity date of the bill will be :

(a) 1.4.2022 (b) 3.4.2022 (c) 4.4.2022

2 On 16.6.2022 P draws a bill on Q for ₹ 1,25,000 for 30 days. 19th July is a public holiday, maturity date of the bill will be:

(a) 19th July (b) 18th July (c) 17th July

3 PQ draws a bill on XY for ₹ 1,30,000 on 1.1.2022. XY accepts the same on 4.1.2022 for period of 3 months after date. What will be the maturity date of the bill :

(a) 4.4.2022 (b) 3.4.2022 (c) 7.4.2022

4 A draws a bill on B. A endorsed the bill to C. The payee of the bill will be

(a) A (b) B (c) C

5 A bill of ₹ 1,20,000 was discounted by Saras with the banker for ₹ 1,18,800. At maturity, the bill returned dishonoured, noting charges ₹ 200. How much amount will the bank deduct from Saras's bank balance at the time of such dishonour?

(a) ₹ 1,20,000 (b) ₹ 1,18,800 (c) ₹ 1,20,200

6 X draws a bill on Y for ₹ 3,00,000 on 1.1.2022 for 3 months after sight, date of acceptance is 6.1.2022. Maturity date of the bill will be:

(a) 8.4.2022 (b) 9.4.2022 (c) 10.4.2022

7 X sold goods to Y for ₹ 5,00,000. Y paid cash ₹ 4,30,000. X will grant 2% discount on balance, and Y request X to draw a bill for balance, the amount of bill will be:

(a) ₹ 98,000 (b) ₹ 68,000 (c) ₹ 68,600

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8	On 1.1.2022, X draws a bill on Y for ₹ 5,00,000 for 3 months. X got the bill discounted 4.1.2022 at 12% rate. The amount of discount on bill will be:		
	(a) ₹ 15,000	(b) ₹ 16,000	(c) ₹ 18,000
9	Mr. Jay draws a bill on Mr. John for ₹ 3,00,000 on 1.1.2022 for 3 months. On 4.2.2022, John got the bill discounted at 12% rate. The amount of discount will be:		
	(a) ₹ 9,000	(b) ₹ 6,000	(c) ₹ 3,000
10	XZ draws a bill on YZ for ₹ 2,00,000 for 3 months on 1.1.2022. The bill is discounted with banker at a charge of ₹1,000. At maturity the bill return dishonoured. In the books of XZ, for dishonour, the bank account will be credited by:		
	(a) ₹ 1,99,000	(b) ₹ 2,00,000	(c) ₹ 2,01,000
11	On 1.1.2022, XA draws a bill on YB for ₹ 1,00,000. At maturity YB request XA to renew the bill for 2 months at 12% p.a. interest. Amount of interest will be:		
	(a) ₹ 2,000	(b) ₹ 1,500	(c) ₹ 1,800
12	A bill of exchange is drawn by a		
	(a) Creditor	(b) Debtor	(c) Debenture holder
13	At the time of drawing a bill, the drawer credits		
	(a) Bills Receivables A/c	(b) Bills Payable A/c	(c) Debtor's A/c
14	A promissory note is made by a		
	(a) Seller	(b) Purchaser	(c) Endorsee
15	A bill of exchange contains		
	(a) An unconditional order		
	(b) A promise		
	(c) A request to deliver the goods		
16	A promissory note contains		
	(a) An unconditional order		
	(b) A promise		
	(c) A request to deliver the goods		

17	The rebate on the bill shows that
	(a) It has been endorsed
	(b) It has been paid after the date of maturity
	(c) It has been paid before the date of maturity
18	Notary Public may charge his fee from the
	(a) Holder of bill of exchange
	(b) Drawer
	(c) None
19	The person on whom a bill is drawn is called
	(a) Drawee (b) Payee (c) Drawer
20	Before acceptance, the bill is called
	(a) Order (b) Request (c) Draft
21	When the due date of bill drawn falls due on a public holiday, the payment must be made on the_____day.
	(a) same (b) preceeding (c) next
22	The due date of the bill drawn for 2 months on 23rd Nov. 2019 will be
	(a) 23rd Jan. 2020 (b) 25th Jan. 2019 (c) 25th Jan. 2020
23	Noting charges are borne by _____.
	(a) Notary Public (b) Drawee (c) Drawer
24	There are_____parties to bill of exchange.
	(a) five (b) four (c) three
25	When a bill is drawn for 2 months after date on 3rd Jan. 2020, its due date will be .
	(a) 3rd Mar. 2020 (b) 5th Mar. 2020 (c) 6th Mar. 2020
26	Notary Public is _____.
	(a) Goverment Officer (b) Drawer (c) Payee
27	When Acceptor or Drawee does not pay the amount of bill to the holder on the due date, it is known_____as the bill.
	(a) honouring (b) discounting (c) dishonouring

28 The person who accepts the bill treats the bill as _____.
(a) Bills Payable (b) Promissory note (c) Bills Receivable

29 _____extra days are allowed over and above the period of bill.
(a) Two (b) Three (c) Five

30 is a person to whom the amount of a bill is payable.
(a) Drawer (b) Acceptor (c) Payee

31 A person who accepts the bill is called_____.
(a) drawer (b) acceptor (c) payee

32 The bill drawn on 12th June 2019 at two months, would be payable on _____.
(a) 15th August, 2019 (b) 16th August, 2019 (c) 14th August, 2019

33 _____means payment of bill before due date.
(a) Retirement of bill (b) Renewal of bill (c) Discounting of bill

34 _____means transfer of the title of a bill from debtors to creditors.
(a) Discounted (b) Renewal (c) Endorsement

35 A bill of one month drawn and accepted on 31st January will become due on_____.
(a) 28th February (b) 1st March (c) 3rd March

36 A bill drawn on 5th August for 45 days will be paid on_____.
(a) 19th September (b) 22nd September (c) 20th September

37 If drawee becomes insolvent, the bill is said to be _____.
(a) honoured (b) renewed (c) dishonoured

38 A bill drawn in Indian language is known as _____.
(a) Bills of Exchange (b) Hund i (c) Promissory note

Answers

1	(c)	5	(c)	9	(b)	13	(c)	17	(c)	21	(b)	23	(b)	27	(c)	31	(b)	35	(c)
2	(b)	6	(b)	10	(b)	14	(b)	18	(a)	22	(c)	24	(c)	28	(a)	32	(c)	36	(b)
3	(a)	7	(c)	11	(a)	15	(a)	19	(a)			25	(c)	29	(b)	33	(a)	37	(c)
4	(c)	8	(a)	12	(a)	16	(b)	20	(c)			26	(a)	30	(c)	34	(c)	38	(b)

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357/400

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347



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346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
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ALVITA KHAN
302



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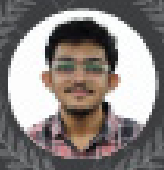
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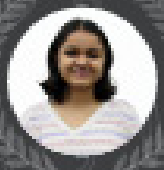
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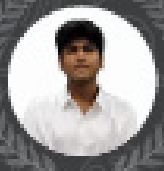
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SCAN ME!

Depreciation

The term 'Depreciation' is used **in relation to** Fixed Asset (FA) & **not** in relation to Goods.

The word 'depreciation' is derived from the **Latin word** 'Depretium', which means **reduction**.

All FA **except Freehold Land** has limited working Life and hence value of FA keeps on reducing with passage of time. Such reduction in the value of FA **mainly** due to its **use in the business** is called Depreciation.

Thus, it can be defined as follows :
Depreciation is **gradual**, **continuous** and **permanent** reduction in the value of fixed asset, mainly due to use of such fixed asset in the business.

Causes or Reasons of Depreciation (fall in value)

i) Normal & Natural Wear & Tear

As we keep on using such FA in business, its value will keep on reducing due to wear & tear. More we use it, more will be the wear & tear and faster its value will reduce.

ii) Passage of time :

FA gets depreciated due to passage / efflux of time, so it is necessary to depreciate them even if they are not in use.

Some assets have a definite life period like lease. On the expiry of life, asset will cease to exist. Other assets like plant and machinery may not have definite life. In their case, life is estimated.

iii) Obsolescence :

It means a state when an asset becomes obsolete due to product of better quality being available, due to technological developments etc.

If a better machine leading to lower cost of production comes in the market, value of old machines will fall down & old machines may have to be scrapped even though they are capable of being used.

iv) Accidents / Natural Calamities :

Loss in value of FA due to accidents or natural calamities is permanent, though it is not continuous and gradual. Such redcution in value is also accounted in the books of accounts.

^ **Original Cost of the FA**

Purchase Price of FA **Plus** Capital Expenditure on such FA

Any expenditure **incurred** at the time of purchase of such fixed asset, **before such asset is put to use**, is **called Capital Expenditure** and is to be **added** while arriving at the cost of such fixed asset.

eg. expenditure incurred on carriage and installation of machinery,
expenditure incurred on construction / renovation of building (raw materials, wages etc)
expenditure incurred on purchase of building (stamp duty, registration, brokerage etc)

Any Expenditure incurred on asset **after asset is put to use** like ^ periodic repairs, maintainance, Insurance premium etc is called **Revenue Expenditure**.
^ such expenses are incurred to maintain asset in proper working condition. It is regular business expense and should be **debited to Expense A/c** (& not FA a/c)

Note : GST paid on purchase of fixed asset is **not** the cost of purchase of FA
& it **cannot be added** while determining **Original Cost** of the FA.
(**If** such GST paid **can be set-off** against GST collected)
Hence, such GST paid is **debited to** Input GST A/c **and not to** Fixed Asset A/c

Journal Entries

			Debit	Credit
Date	**Particulars**	**L.F.**	₹	₹
1	**For Purchase of Fixed Asset**			
	Fixed Asset A/c Dr.			
	To Bank A/c **or** Cash A/c **or** Creditor for FA A/c			
2	**For Capital Expenditure on Fixed Asset**			
	Fixed Asset A/c Dr.			
	To Cash A/c **or** Bank A/c			
3	**For Depreciation on FA** at the end of period			
	Depreciation A/c Dr.			
	To Fixed Asset A/c			
4	**For Closure of Depreciation A/c at the end of period**			
	Profit & Loss A/c Dr.			
	To Depreciation A/c			

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^ **Estimated** useful or economic life **of the FA**

It refers to the **number of years** for which such FA is estimated to be useful in the business. It is usually lesser than the physical life of FA.

^ **Estimated** Scrap **or** Residual or Terminal **value of the FA**

It refers to the estimated scrap value **expected to be received** from the sale / scrap of such FA **at the end of its useful life**

** **O**riginal cost, **E**stimated useful life and **E**stimated scrap value **are the factors to be considered** while charging / deciding the amount depreciation every year

^ **Written Down Value / Book value of the FA**

It refers to the **reduced value of FA** in our books **after charging depreciation**.

^ **Methods of Calculating Depreciation**

Method I : Original Cost Method (OCM)

Under this method, depreciation is charged every year **on the OC** of the FA

It is also called Fixed Instalment Method (FIM) **or** Straight Line Method (SLM)

Calculation of Depreciation

It is calculated **either** at a specified % as given

or to be calculated if estimated useful life & scrap value is given

* **Straight Line Method**

$$\text{Depreciation p.a.} = \frac{\text{Cost of Asset - Estimated Scrap Value}}{\text{Estimated Useful Life (in years)}}$$

$$\text{Straight Line Depreciation Rate} = \frac{\text{Straight line depreciation}}{\text{Cost of Asset}} \times 100$$

Method II : Written Down Value Method (WDVM)

Under this method, depreciation is charged every year **on the WDV** of the FA. It is also called Reducing Balance Method (RBM) **or** Diminishing Balance Method (DBM).

Calculation of Depreciation

It is calculated at a specified %.

The rate of depreciation under this method may be determined by the following formula:

$$1 - \sqrt[n]{\frac{\text{Residual Value}}{\text{Cost of Assets}}} \times 100$$ **where, n = useful life**

When there is sale of fixed asset

Date	Particulars		L.F.	Debit ₹	Credit ₹
1	**For charging depreciation on SOLD fixed asset**				
	till the date of sale				
	Depreciation A/c	Dr.			
	To Fixed Asset A/c				
2	**For sale of fixed asset**				
	Bank A/c **or** Cash A/c	Dr.			
	To Fixed Asset A/c				
3	**For Profit on sale of fixed asset**				
	Fixed Asset A/c	Dr.			
	To Profit on Sale of Fixed Asset A/c				
4	**For closure of profit on ..... A/c** at the end of period				
	Profir on Sale of Fixed Asset A/c	Dr.			
	To Profit & Loss A/c				
OR					
3	**For Loss on sale of fixed asset**				
	Loss on Sale of Fixed Asset A/c	Dr.			
	To Fixed Asset A/c				
4	**For closure of loss on ..... A/c** at the end of period				
	Profit & Loss A/c	Dr.			
	To Loss on Sale of Fixed Asset A/c				

Depreciation : **'Standard Format'** per solution			
Page 1	Fixed Asset A/c	full page	Draw Journal for 2 pages if Journal entries asked
Page 2	Depreciation A/c	half page	
	Workings / Notes	half page	
Page 3	Workings / Notes	full page	

^ **Q. 1 :** Muskan Traders purchased four machines of ₹ 25,000 each on 1st July, 2016. on 30th Sept, 2017, the firm sold one of the machine purchased on 1st July, 2016 at a loss of ₹ 2,500. The firm sold another machine on 31st December, 2018 at a profit of ₹ 3,750. A new machine was purchased on 30th September, 2019, for ₹ 31,250. Prepare Machinery A/c and Machinery Disposal A/c for 4 years, if books of account are closed on 31st March each year and depreciation is charged @ 10% p.a. as per Straight Line Method.
CGST & SGST are charged at 6% each on purchase and sale of Machinery.

^ **Q. 2 :** On 1st January 2017 'Sai Industries, Nagpur' purchased a machine costing ₹ 1,65,000 and spent ₹ 15,000 for its installation charges. The estimated life of the machine is to be 10 years and the scrap value at the end of its life would be ₹ 30,000. On 1st October 2018 the entire Machine was sold for ₹ 1,50,000.
Show Machinery Account, Depreciation Account, for the years 2016-17, 2017-18 and 2018-19 assuming that the accounts are closed on 31st March every year.

Working / Notes :

1 Calculation of Depreciation per annum

2 Calculation of Profit or Loss on Sale of Machine

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In the books of Sai Industries, Nagpur

Dr. **Machinery Account** (y.e. 31 st March) **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

Dr. **Depreciation Account** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

Q. 3 : The Macinery Account of a factory showed a balance of ₹ 19,00,000 on 1st Jan., 2022. Its accounts were made up on 31st December each year and depreciation is written off at 10% on Diminishing Balance Method.

On 1st June, 2022, a new machinery was acquired at a cost of ₹ 2,80,000 and installation charges incurred in erecting the machine works out to ₹ 8,920 on the same date. On 1st June, 2022 a machine which had cost ₹ 4,37,400 on 1st Jan., 2020 was sold for ₹ 75,000. Another machine which had cost ₹ 4,37,000 on 1st Jan. 2021 was scrapped on the same date and it realised nothing.

Write a Machinery Account & Machinery Disposal Account for the year 2022, allowing the same rate of depreciation as in the past, calculating depreciation to the nearest multiple of a rupee.

Provision for Depreciation

This is the method of **accounting for depreciation** & not the method for calculation of depreciation.

Under this method, a separate Provision for Depreciation A/c is maintained and amount of depreciation is transferred to the credit of Provision for Depreciation A/c instead of credit to Assets A/c.

At the end of accounting period, Assets A/c and Provision for Depreciation A/c are balanced and balances carried forward to next period.

Under this method, Asset A/c shows the debit balance equal to original cost of asset at the end every of accounting period and Provision for Depreciation A/c shows total amount of depreciation written off on the concerned asset till that date.

Journal Entries

Date	Particulars		L.F.	Debit ₹	Credit ₹
1	**For charging depreciation**				
	Depreciation A/c	Dr.			
	To Provision for Depreciation A/c				
2	**For transfer of depreciation to Profit & Loss A/c**				
	Profit & Loss A/c	Dr.			
	To Depreciation A/c				

3	**For charging depreciation on SOLD fixed asset till the date of sale**					
	Depreciation A/c	Dr.				
	To Provision for Depreciation A/c					
4	**For transfer of cost from asset to Asset Disposal A/c**					
	Asset Disposal A/c	Dr.				
	To Asset A/c					
5	**For transfer of depreciation from provision for depreciation A/c**					
	Provision for depreciation A/c	Dr.				
	To Asset Disposal A/c					
	(Amount = Total Depreciation charged till the date of sale / disposal)					
6	**For sale of fixed asset**					
	Bank A/c **or** Cash A/c	Dr.				
	To Fixed Asset A/c					
7	**For Profit on sale of fixed asset**					
	Asset Disposal A/c	Dr.				
	To Profit on Sale of Fixed Asset A/c					
8	**For closure of profit on ……. A/c** at the end of period					
	Profit on Sale of Fixed Asset A/c	Dr.				
	To Profit & Loss A/c					
OR						
7	**For Loss on sale of fixed asset**					
	Loss on Sale of Fixed Asset A/c	Dr.				
	To Asset Disposal A/c					
8	**For closure of loss on ……. A/c** at the end of period					
	Profit & Loss A/c	Dr.				
	To Loss on Sale of Fixed Asset A/c					

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^ **Q. 4 :** On April 1, 2019 Shubra Ltd. purchased a machinery for ₹ 12,00,000. On Oct. 1, 2021, a part of the machinery purchased on April 1, 2019 for ₹ 80,000 was sold for ₹ 45,000 and a new machinery at a cost of ₹ 1,58,000 was purchased and installed on the same date. The company has adopted the method of providing 10% p.a. depreciation on the written down value of the machinery.

Required : Show the necessary Ledger A/c's for the years ended 31st March, 2020 to 2022 assuming that

(a) 'Provision for Depreciation Account' is not maintained

(b) Provision for Depreciation Account is maintained.

a) When 'Provision for Depreciation Account' is **NOT** maintained

Dr. **Machinery A/c** (10% p.a. W.D.V. 31/03) **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
2019				2020			
Apr. 1	To Bank A/c		12,00,000	Mar. 31	By Depreciation A/c		1,20,000
				Mar. 31	By Balance c/d		10,80,000
			12,00,000				**12,00,000**
2020				2021			
Apr. 1	To Balance b/d		10,80,000	Mar. 31	By Depreciation A/c		1,08,000
				Mar. 31	By Balance c/d		9,72,000
			10,80,000				**10,80,000**
2021				2021			
Apr. 1	To Balance b/d		9,72,000	Oct. 1	By Depreciation A/c		3,240
Oct. 1	To Bank A/c		1,58,000	Oct. 1	By Bank A/c		45,000
				Oct. 1	By Loss on sale of Machinery A/c		16,560
				2022			
				Mar. 31	By Depreciation A/c		98,620
				Mar. 31	By Balance c/d		9,66,580
			11,30,000				**11,30,000**

b) **When 'Provision for Depreciation Account' is maintained**

Dr. **Machinery Account** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

Dr. **Provision for Depreciation Account** **Cr.**

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

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Dr. **Machinery Disposal Account** Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹

Workings / Notes :

^ **Q. 5 :** A firm's plant and machinery account at 31st December, 2021 and the corresponding depreciation provision a/c, broken down by year of purchase are as follows :

Year of Purchase	Plant and Machinery at cost (₹)	Depreciation Provision
2005	2,00,000	2,00,000
2011	3,00,000	3,00,000
2012	10,00,000	9,50,000
2013	7,00,000	5,95,000
2020	5,00,000	75,000
2021	3,00,000	15,000
	30,00,000	**21,35,000**

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Depreciation is at the rate of 10% per annum on cost. It is the Company's policy to assume that all purchases, sales or disposal of plant occurred on 30th June in the relevant year for the purpose of calculating depreciation, irrespective of the precise date on which these events occurred.

During 2022 the following transactions took place :

1. Purchase of plant and machinery amounted to ₹ 15,00,000.
2. Plant that had been bought in 2011 for ₹ 1,70,000 was scrapped.
3. Plant that had been bought in 2012 for ₹ 90,000 was sold for ₹ 5,000.
4. Plant that had been bought in 2013 for ₹ 2,40,000 was sold for ₹ 15,000.

You are required to :

Calculate the provision for depreciation of plant and machinery for the year ended 31st December, 2022. In calculating this provision you should bear in mind that it is the company's policy to show any profit or loss on the sale or disposal of plant as a completely separate item in the Profit and Loss Account. You are also required to prepare the following ledger accounts during 2022.

(i) Plant and machinery at cost; (ii) Depreciation provision;

(iii) Sales or disposal of plant and machinery.

^ **Sum of the Years of Digits Method**

It is a variation of the "Reducing Balance Method". In this case, the annual depreciation is calculated by multiplying the original cost of the asset less its estimated scrap value by the fraction represented by:

$$\frac{\text{The number of years (including the present year) of remaining life of the asset}}{\text{Total of all digits of the life of the asset (in years)}}$$

This method is not yet in vogue; and its advantages are the same as those of the Reducing Balance Method.

^ **Q. 6 :** M Ltd. purchased an asset for ₹ 84,000 and estimated its life at 6 years. Show the Asset Account for the first three years if depreciation is charged under the sum of years digits method.

In the books of M Ltd.

Dr. Machinery Account Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
Year 1				**Year 1**			
Jan. 1	To Bank A/c			Mar. 31	By Depreciation A/c		
				Mar. 31	By Balance c/d		

Year 2				**Year 2**				
Apr. 1	To Balance b/d			Mar. 31	By Depreciation A/c			
				Mar. 31	By Balance c/d			
Year 3				**Year 3**				
Apr. 1	To Balance b/d			Mar. 31	By Depreciation A/c			
				Mar. 31	By Balance c/d			

^ **Machine Hour Method**

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 machine worked. The machine hour rate of the depreciation, is calculated after estimating the total number of hours that machine would work during its whole life; however, it may have to be varied from time to time, on a consideration of the changes in the economic and technological conditions which might take place, to ensure that the amount provided for depreciation corresponds to that considered appropriate in the changed circumstances. It would be observed that the method is a variation of the Straight Line Method under which depreciation is calculated per year. Under this method it is calculated for each hour the machine works.

Schedule II to the Companies Act 2013 which prescribes estimated useful life of different assets for companies also recognizes this method to some extent. It prescribes that depreciation should be charged using estimated useful life suggested in it; however, in certain category of plant and machinery it prescribes charging higher amount of depreciation if these assets are used for 2 shifts or 3 shifts. In a way, schedule II combines straight line method and machine hour method.

^ **Q. 7 :** A machine was purchased for ₹30,00,000 having an estimated total working of 24,000 hours. The scrap value is expected to be ₹2,00,000 and anticipated pattern of distribution of effective hours is as follows :

Year

1 – 3 3,000 hours per year

4 - 6 2,600 hours per year

7 - 10 1,800 hours per year

Required : Determine annual depreciation under Machine Hour Rate Method.

Production Units Method

Under this method depreciation of the asset is determined by comparing the annual production with the estimated total production. The amount of depreciation is computed by the use of following method:

$$\text{Depreciable Amount} \times \frac{\text{Production during the period}}{\text{Estimated total production}}$$

The method is applicable to machines producing product of uniform specifications.

Q. 8 : A machine is purchased for ₹20,00,000. Its estimated useful life is 10 years with a residual value of ₹2,00,000. The machine is expected to produce 1.5 lakh units during its life time. Expected distribution pattern of production is as follows:

Year	Production
1-3	20,000 units per year
4-7	15,000 units per year
8-10	10,000 units per year

Required : Determine the value of depreciation for each year using production units method.

Depletion Method

Depletion is the allocation of the cost of **wasting natural resources** such as oil, gas, timber, and minerals to the production process. This method is used in case of mines, quarries etc. containing only a certain quantity of product. The depreciation rate is calculated by dividing the cost of the asset by the estimated quantity of product likely to be available to be extracted. Annual depreciation will be the quantity extracted multiplied by the rate per unit.

Q. 9 : M/s Surya & Co. took lease of a quarry on 1-1-2019 for ₹1,00,00,000. As per technical estimate the total quantity of mineral deposit is 2,00,000 tonnes. Depreciation was charged on the basis of depletion method. Extraction pattern is given in the following table:

Year	Quantity of Mineral extracted
2019	2,000 tonnes
2020	10,000 tonnes
2021	15,000 tonnes

Required :

Show the Quarry Lease Account and Depreciation Account for each year from 2019 to 2021.

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In the books of M/s Surya & Co.

Dr. Quarry Lease Account Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
2019				2019			
Jan. 1	To Bank A/c			Mar. 31	By Depreciation A/c		
				Mar. 31	By Balance c/d		
2020				2020			
Apr. 1	To Balance b/d			Mar. 31	By Depreciation A/c		
				Mar. 31	By Balance c/d		
2021				2021			
Apr. 1	To Balance b/d			Mar. 31	By Depreciation A/c		
				Mar. 31	By Balance c/d		

Dr. Depreciation Account Cr.

Date	Particulars	J.F.	₹	Date	Particulars	J.F.	₹
2019				2019			
Dec. 31	To Quarry Lease A/c			Dec. 31	By Profit & Loss A/c		
2020				2020			
Dec. 31	To Quarry Lease A/c			Dec. 31	By Profit & Loss A/c		
2021				2021			
Dec. 31	To Quarry Lease A/c			Dec. 31	By Profit & Loss A/c		

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. Its effect needs to be quantified and disclosed separately. A change in an accounting estimate may affect the current period only or both the current period and future periods.

Q. 10 : A Firm purchased an old machinery for ₹37,000 on 1st January,2019 and spent ₹3,000 on its overhauling. On 1st July 2020, another machine was purchased for ₹10,000. On 1st July 2021, the machinery which was purchased on 1st January 2019, was sold for ₹28,000 and the same day a new machinery costing ₹25,000 was purchased. On 1st July,2022, the machine which was purchased on 1st July,2020 was sold for ₹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, 2020 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, 2019.

Q. 11 : M/s Anshul & Co. commenced business on 1st January 2017, when they purchased plant and equipment for ₹7,00,000. They adopted a policy of charging depreciation at 15% per annum on diminishing balance basis and over the years, their purchases of plant have been:

Date	Amt. (₹)
01-01-2018	1,50,000
01-01-2021	2,00,000

On 1-1-2021 it was decided to change the method and rate of depreciation to straight line basis. On this date remaining useful life was assessed as 6 years for all the assets purchased before 1.1.2021 with no scrap value and 10 years for the asset purchased on 1.1.2021.

Required :

Prepare Plant and Equipment Account for the year ending 31st December, 2021.

^ **Revision of the estimated useful life of Property, Plant and Equipment**

The residual value and the useful life of an asset should be reviewed at least at each financial year-end and, if expectations differ from previous estimates, the change(s) should be accounted for as a **change in an accounting estimate** in accordance with Accounting Standards.

Whenever there is a revision in the estimated useful life of the asset, the written down value or the balance depreciable amount should be charged over the revised remaining estimated useful life of the asset.

^ **Q. 12 :** A Machine costing ₹6,00,000 is depreciated on straight line basis, assuming 10 years working life and Nil residual value, for three years. The estimate of remaining useful life after third year was reassessed at 5 years.

Required : Calculate depreciation for the fourth year.

^ **Revaluation of Property, Plant and Equipment**

After recognizing an asset initially, the asset whose fair value could be reliably measured could be carried at the revalued amount, being the fair value at revaluation date and reduced by successively accumulated depreciation and successive accumulated impairment losses (permanent decline in value) (if any).

If an entity opts for revaluation:

(a) Revaluations must be made at adequate intervals (say yearly) for ensuring that carrying amount doesn't differ substantially from that which would be determined if fair value at end of the reporting period is used

(b) In case an item of PPE is revalued, whole class of such PPE to which such asset belongs should be revalued

(c) In case the carrying amount of an asset increases due to revaluation, such increase should be credited to revaluation surplus and should be accumulated in equity. However, such increase should be recognized in Profit and Loss statement to the extent of reversal of a previous decrease of that asset that was recognized in the Profit and Loss statement.

(d) In case the carrying amount of an asset is decreased due to revaluation, such decrease should be recognized in the Profit and Loss account. However, such decrease should be debited to the revaluation surplus to the extent of reversal of a previous increase that was recognized in revaluation surplus for that asset.

(e) The Revaluation Surplus may be transferred directly to retained earnings when the asset is derecognized. This may involve transferring the whole of the surplus when the asset is retired or disposed of. Such transfer from Revaluation Surplus to Retained Earnings cannot be made through the Profit or Loss.

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(f) Alternatively, where there is an upward revaluation, the excess depreciation on account of such upward revaluation may be transferred from Revaluation Surplus to Retained Earnings. Such transfer from Revaluation Surplus to Retained Earnings cannot be made through the Profit or Loss.

It may be pertinent to note that revaluation of Property, Plant and Equipment is an accounting policy choice, and not mandatory under the accounting standards or the Companies Act, 2013.

^ **Q. 13 :** A machine of cost ₹12,00,000 is depreciated straight-line assuming 10 year working life & zero residual value for three years. At the end of third year, the machine was revalued upwards by ₹60,000 the remaining useful life was reassessed at 9 years.

Required : Calculate depreciation for the fourth year.

^ **Q. 14 :** Amazing group had Property, Plant & Equipment (PP&E) with a book value of ₹35,00,000 on 31st December, 2022. The balance in Revaluation Surplus on that date was ₹3,00,000. As part of their practice of revaluing the assets on yearly basis, another revaluation was carried out on 31st December, 2022.

Evaluate the impact of Revaluation if the Fair Value as a result of Revaluation done on 31st December, 2022 was :

(a) ₹37,00,000

(b) ₹33,00,000 and

(c) ₹31,00,000.

Also, give the journal entries.

Answer :

(a) Fair Value : ₹37,00,000

Since this is an upward revaluation and the group had a balance in revaluation surplus (i.e. there was an upward movement earlier), hence this will result in an additional credit of ₹2,00,000 to Revaluation Surplus and hence the total Revaluation Surplus balance (part of other comprehensive income in Equity) shall increase to ₹5,00,000.

The Accounting journal entry shall be :

(b) Fair Value : ₹33,00,000

Since this is a downward revaluation and the group had a balance in revaluation surplus (i.e. there was an upward movement earlier), hence this will result in a reduction or a debit to Revaluation Surplus to the extent of balance therein and any excess shall be debited to Profit & Loss A/c. In this case, there is a reduction in fair value of ₹2,00,000 (35,00,000 – 33,00,000) and hence the entire amount shall be debited to Revaluation Surplus. Hence, the total Revaluation Surplus balance (part of other comprehensive income in Equity) shall decrease to ₹1,00,000.

The Accounting journal entry shall be:

(c) Fair Value : ₹31,00,000

Since this is also a downward revaluation and the group had a balance in revaluation surplus (i.e. there was an upward movement earlier), hence this will result in a reduction or a debit to Revaluation Surplus to the extent of balance therein and any excess shall be debited to Profit & Loss A/c. In this case, there is a reduction in fair value of ₹4,00,000 (35,00,000 – 31,00,000) and hence the Revaluation Surplus A/c shall be debited by ₹3,00,000 and the balance ₹1,00,000 shall be debited to Profit & Loss A/c. Hence, the total Revaluation Surplus balance (part of other comprehensive income in Equity) shall become Nil.

The Accounting journal entry shall be:

Amortisation

Q. 15 : Kumar R&D Co. registered a patent (the patent meets the criteria of an intangible asset) on 1st July, 2021 developed at a cost of ₹28,00,000 and spent ₹2,00,000 towards legal fees and registration. The patent is granted for a period of 10 years. The books are closed on 31st December every year.

Required :

Show the Patent Account and Amortisation Account for the year 2021 and 2022.

^ **Additional Theory**

* **Concept of Depreciation**

Tangible Assets are assets that have a physical substance i.e., they can be seen and touched, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.

Useful life of tangible asset is based on expected usage.

Property, **P**lant and **E**quipment 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 twelve months.

These are also called fixed assets in common parlance. When a fixed asset is purchased, it is recorded in books of account at its original or acquisition/purchase cost. However fixed assets are used to earn revenues or save costs for several accounting periods in future with the same acquisition cost until the concerned fixed asset is sold or discarded.

For example, acquisition of a machinery expected to be in use for 10 years in the production of finished goods will earn revenues over the next 10 years. Similarly, an ATM machine installed by a bank will result in cost savings over the expected life of such ATM machines for the bank in terms of not requiring to employ personnel to dispense cash for customers.

Since the life of such assets exceeds one year, it is therefore necessary that a part of the acquisition cost of such fixed assets be treated or allocated as an expense in each of the accounting period in which the asset is utilized. The amount or value of fixed assets allocated in such manner to respective accounting period is called depreciation. Value of such assets decreases with passage of time **mainly** due to following reasons :

1. Wear and tear due to its use in business
2. Efflux of time (even when it is not being used)
3. Obsolescence due to technological or other changes
4. Decrease in market value
5. Depletion mainly in case of mines and other natural reserves

It is important to account for value of portion of property, plant and equipment utilized for generating revenue during an accounting year to ascertain true income.

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In other words, against the income/cost savings generated during a period, it is essential to book a portion of the cost of the asset utilized in generating such income/ cost savings. **This portion of** cost of **Property, Plant & Equipment allocated** to an accounting year **is called depreciation.**

As per Schedule II under the Companies Act, 2013, Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life. The depreciable amount of an asset is the cost of an asset or other amount substituted for cost (i.e., in case of revaluation of assets, such revalued amount), less its residual value. The useful life of an asset is the period over which an asset is expected to be available for use by an entity, or the number of production or similar units expected to be obtained from the asset by the entity. Thus, there are 3 important factors for computing depreciation:

- Estimated useful life of the asset
- Cost of the asset
- Residual value of the asset at the end of the of its estimated useful life

Depreciation of an asset begins when it is available for use, i.e., when it is in the location and condition necessary for it to be capable of operating in the manner intended by management. Thus it is not necessary that an asset must be used to be depreciated. There is decrease in value of assets due to normal wear and tear or obsolescence even when these are not physically used. Accordingly, value of such wear and tear should be estimated and accounted for.

Depreciation is allocated so as to charge a fair proportion of the depreciable amount in each accounting period during the expected useful life of the asset. Depreciation for a period helps to charge that portion of the cost of the asset against the revenues earned, which is expired for that period and hence follows matching principle. In other words the total cost of the asset is reflected in form of a) Expired cost (depreciation) and b) Unexpired Cost which shall be the written down value of the asset being reflected in balance sheet. Also, charging depreciation every year reduces the distributable profits thereby ensuring the availability of funds whenever the replacement is required.
The depreciation is a type of loss in the value of assets employed for carrying on a business. Being an essential element of business expenditure, it is necessary to calculate the amount of such loss and to make a provision, and therefore, arrive at the amount of profit or loss made by the business.

Basically, the cost of an asset used for purpose of business has to be written off over its economic (not physical) life which must be estimated. A point to remember is that usually, at the end of the economic life, an asset has some value as scrap or otherwise. The amount to be written off in each year should be as such which will reduce the book value of the asset, at the end of its economic life, to its estimated scrap value.

* **Cost of Property, Plant and Equipment comprises :**

(a) its purchase price, including non-refundable import duties and purchase taxes, after deducting trade discounts and rebates.

(b) any cost directly attributable to bring the asset to the location and condition necessary for it to be capable of operating in a manner intended by the enterprise.

(c) the initial estimate of the costs of dismantling, removing, the item and restoring the site on which an asset is located.

Examples of directly attributable costs are :

(a) cost of employee benefits arising directly from acquisition or construction of an item of property, plant and equipment.

(b) cost of site preparation

(c) initial delivery and handling costs

(d) installation and assembly costs

(e) cost of testing whether the asset is functioning properly, after deducting the net proceeds from selling the items produced while testing (such as samples produced while testing)

(f) professional fees e.g. engineers hired for helping in installation of a machine.

Thus, all the expenses which are necessary for the asset to bring it in condition and location of desired use will become part of cost of the asset.

However, following expenses **should not** become part of cost of asset:

(a) costs of opening new facility or business, such as inauguration costs;

(b) cost of introducing new product or service (for example cost of advertisement or promotional activities).

(c) cost of conducting business in a new location or with a new class of customer (including cost of staff training); and

(d) administration and other general overhead costs.

Once an asset has been brought to its intended condition and location of use, no cost should be recognized as part of cost of the asset unless there is major repair or addition which increases the useful life of the asset or improves the production capacity of the asset. Accordingly, cost incurred while an item is capable of operating in intended manner but it is not yet put to use or is used at less than full capacity should not be capitalized as part of cost of the asset.

Similarly, cost of relocation of an asset should **not** be capitalized.

Any additions made to a particular item of property, plant and equipment after it is initially put to use are depreciated over the remaining useful life of the asset. Any addition or extension which has a separate identity and is capable of being used after the existing asset is disposed of, is accounted for separately. Therefore, it is important to maintain an asset register capturing asset wise details of cost, rate of depreciation, date of capitalization etc. All these details need to be captured for any additions to existing assets as well. In the absence of the adequate information, it will be very difficult to compute depreciation expense year on year. Also, at the time of disposal or discard of a particular asset, it will not be possible to compute gain or loss on such disposal / discard.

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* **Characteristics of depreciation :**

1. Depreciation is reduction in the book value of fixed assets (except freehold land)
2. It reduces the book value of the fixed asset.
3. Reduction in the book value of a fixed asset is permanent, gradual and of continuing nature.
4. Depreciation is a continuous process, i.e., provided every year because the book value is reduced either due to use or with the passage of time.
5. It occurs gradually unless there is a quick physical deterioration or obsolescence due to technological developments.
6. It is not a process of valuation of fixed asset. It is a process of allocation of cost of the fixed asset over its estimated useful life.
7. The term depreciation is used only for tangible fixed assets such as building, plant, machinery, etc. The term used in the case of Wasting Assets is depletion and in the case of Intangible Assets, the term is amortisation.
8. Depreciation is a non-cash expense. There is no outflow of cash when depreciation is charged.
9. Depreciation is an indirect expense, therefore, it is transferred to the debit of Profit & Loss Account.

* **Main reasons for providing Depreciation**

Depreciation is provided because of the following main reasons:

(i) To Determine Correct Profit or Loss.

Depreciation is an expenses of the business &, therefore, is a charge against revenue. If it is not accounted as an expense, correct profit earned or loss incurred for the accounting period will not be known.

(ii) To Show True and Fair View of the Financial Position.

Balance Sheet should give a true and fair view of the financial position of the entity. Depreciation, if not charged, would result in assets being stated at a higher value. As a result of this the Position Statement (Balance Sheet) would not present a true and fair view of the financial position of the entity.

(iii) To Comply with Legal Provisions.

It is necessary to charge depreciation to comply with the provision of the Companies Act and the Income Tax Act.

* **Intangible Assets**

An intangible asset is an identifiable non-monetary asset, without physical substance, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes. Examples of intangible assets include:

(a) Streaming rights of movies / TV shows / web series on platforms like Netflix, Disney Hot Star, Amazon Prime / Sony LIV etc.

(b) Broadcasting rights of events such as the Cricket World Cup, the Indian Premier League, the Pro Kabaddi League etc.

(c) Landing rights / time slots at airports which permit aircrafts to land or take-off during a particular time frame

(d) Patents

(e) Trademarks

(f) Copyrights

(g) Distribution rights for motion pictures in theatres

(h) Long-term customer contracts

(i) Customer data collected by the entities such as customer contact numbers / email IDs and spending data at stores like Pantaloons, Westside etc. could be a major intangible asset for these entities.

(j) Goodwill (purchased)

(k) Computer Software

Intangible assets comprise a major portion of the balance sheet. It may be noted that it can also be the case that intangible assets could make the entities far more valuable than the tangible assets. For instance, a multi-year customer contract guaranteeing more than 75% of the revenue for the company is a major asset, which on occasions could be more valuable than the tangible assets themselves. Similarly, when Air India was up for acquisition, the tangible assets comprised of several old planes which needed overhauling and maintenance. However, one of the major reasons that made Air India a desirable target was the prime landing slots (intangible asset) that it had at airports across the world Intangible assets can be recognized in the financial statements provided they meet the following conditions:

(i) The intangible asset is identifiable. Being identifiable means the entity could rent, sell, exchange or distribute the specific future economic benefits attributable to the asset without disposing of future economic benefits that flow from other assets used in the same revenue earning activity.

(ii) The enterprise can exercise control over such intangible asset. Control means the power available with the enterprise to obtain economic benefits from the asset and at the same time, can restrict access of others to those benefits.

(iii) It is probable that the future economic benefits attributable to the asset will flow to the enterprise; and

(iv) The cost of the intangible asset can be measured reliably.

An intangible asset acquired separately usually measured at cost, as cost can be measured reliably in such cases. The cost of the intangible asset would comprise of:

- Purchase price
- Any import duties and taxes (other than those subsequently recoverable by the enterprise from the tax authorities)
- Any directly attributable expenditure on making the asset ready for its intended use e.g., professional fees towards legal services. Any trade discounts and rebates are deducted in arriving at the cost.

As can be seen above, the cost of an intangible asset is similar to the manner in which the cost of a tangible asset is determined.

Intangible assets acquired as part of acquisition, government grants, internally generated goodwill / intangible assets, or on exchange of assets are dealt separately at the intermediate level.

An intangible asset should be derecognised (eliminated from the balance sheet) on disposal or when no future economic benefits are expected from its use and subsequent disposal.

Gains or losses arising from the retirement or disposal of an intangible asset should be determined as the difference between the net disposal proceeds and the carrying amount of the asset and should be recognised as income or expense in the statement of profit and loss.

Difference between Tangible and Intangible Assets

Tangible Assets	Intangible Assets
These are assets that have a physical substance i.e., they can be seen and touched, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.	These are identifiable assets that do NOT have a physical substance, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.
Tangible Assets have a finite life based on expected usage.	Intangible Assets have a finite life based on contractual terms. In some cases, intangible assets could also have an indefinite life e.g. purchased goodwill.
Useful life is based on expected usage, with no presumption laid down for the same.	Useful life of Intangible Assets is presumed not to exceed 10 years unless evidence exists to the contrary.

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Tangible Assets are depreciated over the useful life. In other words, writing off the value of tangible assets on an annual basis is known as depreciation.	Intangible Assets are amortised over the useful life. In other words, writing off the value of intangible assets on an annual basis is known as amortisation.
Examples include Property, Machinery, Vehicles etc.	Examples include software, streaming rights, landing rights, trademarks, patents etc.

* **Amortisation**

The concept of amortisation in case of intangible assets is similar to the concept of depreciation in case of tangible assets. In other words, 'depreciation of an intangible asset' is called **AMORTISATION.**

Amortisation can be defined as 'the systematic allocation of the depreciable amount of an intangible asset over its useful life'. Depreciable amount is the cost of an asset less its residual value.

Useful life is either:

(a) the period of time over which an asset is expected to be used by the enterprise; or

(b) the number of production or similar units expected to be obtained from the asset by the enterprise.

Residual value is the amount which an enterprise expects to obtain for an asset at the end of its useful life after deducting the expected costs of disposal.

The depreciable amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life. Amortisation should commence when the asset is available for use. It is presumed that the useful life of an intangible asset will exceed ten years from the date when the asset is available for use unless evidence not exists to the contrary. For instance, given the rapid changes in technology, computer software and many other intangible assets are susceptible to technological obsolescence. Therefore, it is likely that their useful life will be short. Similarly, intangible assets with contractual rights for a period exceeding ten years, will be amortised over such extended period rather than the presumed period of ten years.

Similar to depreciation, the amortisation method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise. If that pattern cannot be determined reliably, the straight-line method should be used. The amortisation charge for each period should be recognised as an expense unless permitted or required to be included in the carrying amount of another asset.

	Given the nature of intangible assets, the residual value of an intangible asset should be assumed to be zero unless:
	(a) there is a commitment by a third party to purchase the asset at the end of its useful life; or (b) there is an active market for the asset and:
	(i) residual value can be determined by reference to that market; and
	(ii) it is probable that such a market will exist at the end of the asset's useful life.
	The amortisation period and the amortisation method should be reviewed at least at each financial year end. If the expected useful life of the asset is significantly different from previous estimates, the amortisation period should be changed accordingly. If there has been a significant change in the expected pattern of economic benefits from the asset, the amortisation method should be changed to reflect the changed pattern.
^	**Try Yourself : Objectives**
*	**State True or False with reasons :**
1	Increase in market value of a fixed asset is one of the reasons for depreciation being charged.
2	Depreciation is a cash expenditure like other normal expenses..
3	Cost of property, plant and equipment includes purchase price, refundable taxes & import duties after deducting any discount or rebate.
4	Cost of fixed asset should also include cost of opening a new facility such as inauguration costs.
5	Depreciation is charged with a constant amount under straight line method and charged with a constant percentage under diminishing balance method.
6	In case an item of Property, Plant & Equipment is revalued, whole class of assets to which that asset being revalued belongs should be revalued.
7	In case the carrying amount of an asset is decreased due to revaluation, such decrease should always be recognized in the Profit and Loss account.
8	Akash purchased a machine for ₹12,00,000. Estimated useful life is 10 years and scrap value is ₹1,00,000. Depreciation for the first year using sum of the years digit method shall be ₹2,00,000.
9	Depreciation cannot be provided in case of loss, in a financial year.
10	Providing for depreciation also helps in providing for accumulation of funds to facilitate the replacement at the end of its useful life.
11	If the equipment account has a balance of ₹12,50,000 and the accumulated depreciation account has a balance of ₹4,00,000, the written down value of same shall be ₹16,50,000.
12	Sum of the years digit method is an example of accelerated method of charging depreciation.

13	Over the life of an asset subject to depreciation, the accelerated method will result in less depreciation expense in early years and more depreciation in later years of its life.
14	While depreciating land cost, Straight line method shall give more depreciation than the written down value.
15	Provision for depreciation account is debited at the time of recording the depreciation on an asset.
16	If adequate maintenance expenditure is incurred with relation to running repairs of an asset, we need not charge any depreciation.
17	When a property, plant or equipment is sold then provision for depreciation account is debited, asset account is credited and any gain or loss is recorded to profit and loss account.
18	While calculating the depreciation as per diminishing balance method, the salvage value of the asset at the end of its life is reduced from its cost.
19	Any change in the estimated useful life of an asset should be accounted for as a change in an accounting estimate in accordance with Accounting Standards.
20	An intangible asset is a non identifiable, non monetary asset.
21	Reducing balance method of depreciation is followed to have a uniform charge for depreciation and repairs and maintenance together.
22	Depreciation is a non-cash expense and does not result in any cash outflow.
	Answers :
1	**False**
	It is the decrease in market value as one of the reasons for depreciation. Increase in market value may result in Revaluation.
2	**False**
	Depreciation is not a cash expenditure like other normal expenses as it does not result in any cash outflow.
3	**False**
	Non refundable taxes & duties form part of the cost.
4	**False**
	Inauguration costs shouldn't be part of cost.
5	**True**
	SLM method results in same amount and diminishing method involves same rate of depreciation.

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6	**True**
	Revaluation should be done for the whole class of the asset.
7	**False**
	Any decrease in value of asset on account of revaluation should be first debited to Revaluation Reserve, if any, and then to Profit & Loss account.
8	**True**
	Sum of years digit method depreciation is calculated as
	10/55 x (12,00,000 – 1,00,000) = 2,00,000
9	**False**
	Depreciation is a charge against profit and not an appropriation of profit. Therefore, depreciation has to be provided for, even in case of loss in a financial year.
10	**True**
	Depreciation being non cash expense reduces the distributable profits and hence facilitates replacement of asset when required.
11	**False**
	WDV = ₹12,50,000 - ₹4,00,000 = ₹8,50,000
12	**True**
	Higher depreciation is charged in earlier years under sum of the years digit method.
13	**False**
	It is vice versa as under diminishing balance method; higher depreciation is charged in beginning.
14	**False**
	Land is not depreciated.
15	**False**
	Provision for Depreciation account is credited while charging the depreciation.
16	**False**
	Depreciation is allocation of the cost of an asset over its useful life. Regular repairs may be required during its life are expensed & depreciation has to be charged anyways.

17	**True**
	At the time of sale of an asset, respective asset account is credited with provision for depreciation account being debited and any resulting gain or loss being charged to profit & loss account.
18	**False**
	Under diminishing balance method, salvage value is not considered initially as it assumes that at the end of the asset's life the remaining value shall be its salvage value.
19	**True**
	Any change in useful life of an asset is accounted for as a change in estimate.
20	**False**
	An intangible asset is an identifiable non-monetary asset, held for use in production and supply of goods and services.
21	**True**
	In the early periods of useful life of a fixed assets, repairs and maintenance expenses are relatively low because the asset is new. Whereas in later periods, as the asset is new. Whereas in later periods, as the asset become old, repairs and maintenance expenses increase continuously. Under written down value method, depreciation charged is high in the initial period and reduces continuously in the later periods. Thus, depreciation and repair and maintenance expenses become more or less uniform throughout the useful life of the asset.
22	**True**
	Depreciation is a non-cash expense and unlike other normal expenditure (e.g. wages, rent, etc.) does not result in any cash outflow. Therefore depreciation is a non-cash expense and does not result in any cash outflow.
*	**Multiple Choice Questions**
1	Original cost = ₹12,60,000; Salvage value = Nil; Useful life = 6 years. Depreciation for the first year under sum of years digits method will be
	(a) ₹3,60,000 (b) ₹1,20,000 (c) ₹1,80,000
2	The number of production of similar units expected to be obtained from the use of an asset by an enterprise is called as
	(a) Unit life (b) Useful life (c) Production life

3	Obsolescence of a depreciable asset may be caused by:
	I. Technological changes.
	II. Improvement in production method.
	III. Legal or other restrictions.
	(a) Only (I) above
	(b) Both (I) and (II) above
	(c) All (I), (II), (III) and (IV) above
4	If a concern proposes to discontinue its business from March 2018 and decides to dispose of all its plants within a period of 4 months, the Balance Sheet as on March 31, 2018 should indicate the plants at their
	(a) Historical cost (b) Net realizable value (c) Cost less depreciation
5	In the case of downward revaluation of a plant which is for the first time revalued, the account to be debited is
	(a) Plant account (b) Revaluation Reserve (c) Profit & Loss a/c
6	The portion of the acquisition cost of the tangible asset, yet to be allocated is known as
	(a) Written down value (b) Accumulated value (c) Realisable value
7	The main objective of providing depreciation is to
	(a) Create secret reserve
	(b) Reduce the book value of assets
	(c) Allocate cost of the assets
8	Original cost of a machine was ₹25,20,000 salvage value was ₹1,20,000, useful life was 6 years. Annual depreciation under Straight Line Method
	(a) ₹4,20,000 (b) ₹4,00,000 (c) ₹3,00,000
9	The cost of a machine is ₹20,00,000. Two years later the book value is ₹10,00,000. The Straight-line percentage depreciation is
	(a) ₹50% (b) 33-1/3% (c) 25%
10	A machinery with original cost of ₹10,00,000 and Nil Salvage value acquired on 1st April 2019 with 4 years useful life was depreciated using Straight Line Method. It was decided to sell the machinery on 1st October 2021 for ₹1,20,000. What shall be the gain or (loss) on the sale of Machinery?
	(a) Loss of ₹1,30,000 (b) Gain of ₹1,20,000 (c) Loss of ₹5,000

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11 Which of the following assets does not depreciate?
(a) Machinery and equipment (b) Patents (c) Land

12 A company purchased a machinery on April 01, 2017, for 15,00,000. It is estimated that the machinery will have a useful life of 5 years after which it will have no salvage value. The depreciation charged during the year 2021-22 was
(a) ₹5,00,000 (b) ₹4,00,000 (c) ₹3,00,000

13 If the equipment account has a balance of 22,50,000 and the accumulated depreciation account has a balance of 14,00,000, the book value of the equipment is
(a) ₹36,50,000 (b) ₹8,50,000 (c) ₹14,00,000

14 A plant with original cost of 50,00,000 was revalued after 2 years resulting in credit to Revaluation Surplus account of ₹4,00,000. Towards the year end of 2019-20, due to COVID-19 the plan value had gone down by ₹5,00,000 and accordingly management decided to revalue the same. What shall be the impact of this downwards revaluation on the Profit & Loss Account ?
(a) Debit of ₹5,00,000 (b) Debit of ₹1,00,000 (c) Credit of ₹5,00,000

15 In respect of intangible assets, there is a presumption that the useful life of an intangible asset will not exceed
(a) 2 years (b) 3 years (c) 10 years

16 A company developed a technology to enhance the battery life of mobile phones. The cost of development have been capitalized as an intangible asset at ₹ 5,00,000. The company estimates the life of the technology developed to be 3 years. The company has forecasted that 50% of sales will be in year 1, 35% in year 2 and 15% in year 3. What should be the amortisation charge in third year?
(a) ₹2,50,000 (b) ₹75,000 (c) ₹1,75,000

17 An intangible asset is an asset
(a) with no physical existence
(b) generated internally by the business
(c) cannot be sold

Answers :

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

*	**Theory Questions**
1	Distinguish between Straight line method of depreciation and Written down value method of depreciation.
2	Write short note on Depletion method of depreciation.
3	What factors are considered for calculation of depreciation of a plant?
	Answers :
1	Under straight line method an equal amount is written off each year throughout the working life of the depreciable tangible asset so as to reduce the cost of the asset to nil or to its scarp value at the end. Under reducing balance method, a fixed percentage is charged on the diminishing balance of the asset each year so as to reduce the value of the asset to its scarp value at the end of useful life. The basic distinction between these two methods are as follows: Under straight line method, annual depreciation charge is equal throughout the life of the asset; but under reducing balance method, depreciation charge is reduced over the years as the asset grows old. Under straight-line method, the asset can be fully depreciated but under reducing balance method asset can never be fully depreciated. Under straight line method the charge for depreciation is constant while repair charges increase with the life of the asset, so the total charge throughout the life of the asset will not be uniform. To the contrary, under reducing balance method, depreciation charges become high in the initial years but generally repair remains low. As the asset grows old depreciation charge reduces but repair expenses increase. Thus under reducing balance method depreciation and repairs are more or less evenly distributed throughout the life of the asset.
2	Natural resources include physical assets like mineral deposits, oil and gas resources and timber. These natural resources exhaust by exploitation. Depletion per unit is calculated as $\frac{\text{Acquisition cost - Residual Value}}{\text{Estimate life in terms of production}}$
3	The factors considered for calculation of depreciation are as: (i) Cost of asset including expenses for installation, commissioning, trial run etc. (ii) Estimated useful life of the asset and (iii) Estimated scrap value (if any) at the end of useful life of the asset.

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357/400

BHAVIK DOSHI



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
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MEETALI MAHESHWARI
300

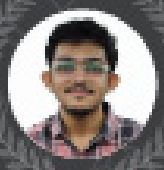
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340/400

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MEET SHAH
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331



NISHIT KAPUR
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328



PALAK JAJODIA
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325



SWASTIKA SINGH
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323



SUKUNJ GUPTA
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323



DURGASHRI VS
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319



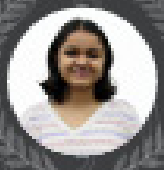
VARUN ADWANI
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319



KARTIK LADHANI
CA Foundation June'22
316



RIDHI PAREKH
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314



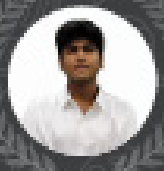
SMEET LADHANI
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313



TANMAY AGARWAL
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311



GARV KHANDELWAL
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308



DAKSH JAIN
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308



DEEPAK GURNANI
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305



PARIDHI JHAWAR
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304



SATYA BHANUSHALI
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and many more...

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JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
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AIR 33



PIYUSH KOTHARI
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AIR 34



HIMANSHI CHHAJED
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AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MUNDRA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHRUTI SHIVARAM
CA INTER NOV'23
AIR 47

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SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHADRIA
CA FINAL NOV'23
AIR 32



PINAL KHETAN
CA FINAL NOV'23
AIR 35



SHOURYA TIBREWALA
CA FINAL MAY'22
AIR 39



DEEPAK LADHA
CA FINAL NOV'23
AIR 40



HIMANSHU KHATRI
CA FINAL MAY'22
AIR 41



SHRAVAN MUNDRA
CA FINAL NOV'23
AIR 45



DEEPTHI PACHIPULUSU
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SHREY AGARWAL
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SCAN ME!

Meaning

Inventory can be defined as assets held

- for sale in the ordinary course of business, or
- in the process of production for such sale, or
- for consumption in the production of goods or services for sale, including maintenance supplies and consumables other than machinery spares, servicing equipment and standby equipment.

There can be different types of inventory based on nature of business of an enterprise.

In case of a trading concern, inventories primarily consist of products purchased for resale in their existing form. It may also have an inventory of supplies such as wrapping paper, cartons, and stationery.

The inventories of **manufacturing concern** consist of several types of inventories :
raw material (which will become part of the goods to be produced),
work-in-process (partially completed products in the factory) and
finished products.

In manufacturing concerns inventories will also include maintenance supplies, consumables, loose tools and spare parts. However, inventories do not include spare parts, servicing equipment and standby equipment which can be used only in connection with an item of fixed asset and whose use is expected to be irregular; such machinery spares are generally accounted for as fixed assets.

At the year-end (or any period for which books are closed) every business entity needs to ascertain the closing balance of inventory which comprise of inventory of raw material work in-progress, finished goods and other consumable items.

Value of closing inventory is put at : **Trading A/c Credit & Balance sheet, Asset side**

Inventory Valuation

A primary issue in accounting for inventories is the determination of the value at which inventories are carried in the financial statements until the related revenues are recognized. Inventory is generally the most significant component of the current assets held by a trading or manufacturing enterprise. Proper valuation of inventory has a very significant bearing on the authenticity of the financial statements. The significance of inventory valuation arises due to various reasons as explained in the following points :

(i) Determination of Income

The valuation of inventory is necessary for determining the true income earned by a business entity during a particular period. To determine gross profit, cost of goods sold is matched with revenue of the accounting period.

Cost of goods sold is calculated as follows :

Cost of goods sold = Opening Inventory + Purchases + Direct Expenses - Closing Inventory

Inventory valuation will have a major impact on the income determination. The effect of any over or under statement of inventory may be explained as :

If the value of	Then net income will be
Closing Inventory Overstated	Overstated
Closing Inventory Understated	Understated
Opening Inventory Overstated	Understated
Opening Inventory Understated	Overstated

(ii) Ascertainment of Financial Position

Inventories are classified as **current assets.** The value of inventory on the date of balance sheet is required to determine the financial position of the business.

In case the inventory is not properly valued, the balance sheet will not disclose the truthful financial position of the business.

(iii) Liquidity Analysis

Inventory is classified as a **current asset**, it is one of the components of net working capital which reveals the liquidity position of the business.

Current ratio which studies the relationship between current assets and current liabilities is significantly affected by the value of inventory. Bankers rely on the current ratio which is denoted as current assets divided by current liabilities. If inventory is a major part of the current assets then, naturally, the next set of questions that arise would be :

(a) Whether the inventory is properly valued based on consistently applied principles?

(b) Are there any items of inventory that are either slow-moving or non-moving?

(c) How often an external auditor has verified the inventories to make the valuation reliable?

Studies have shown that poor management of inventories, is one of the reasons of losses of small manufacturing enterprises which eventually leads to shutting down of such business units.

(iv) Statutory Compliance

Schedule III to the Companies Act, 2013 requires valuation of each class of goods i.e. raw material, work-in-progress and finished goods under broad head to be disclosed in the financial statements.

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As per the requirements of the Accounting Standards, the financial statements should disclose:

(a) the accounting policies adopted in measuring inventories, including the cost formula used, and

(b) the total carrying amount of inventories and its classification appropriate to the enterprise.

The common classification of inventories are raw materials; work-in-progress; finished goods; stores-in-trade (in respect of goods acquired for trading) and spares and loose tools.

^ **Basis of Inventory Valuation**

Inventories should be generally valued at the **lower of cost or net realizable value.**

This principle is governed by **'Principle of Conservative Accounting'** under which any expenses or losses from transactions entered or event occurred are to be recognized immediately, however, any gains or profits are not recognized until it becomes due or are actually realized.

Under the principle of 'lower of cost or net realizable value' any loss due to decrease in sales price of the inventory below its cost is recognized immediately as it is anticipated that the enterprise will make losses whenever it will sell.

^ **Methods to determine cost of Inventory**

* **Historical Cost Methods**

(i) **Specific Identification Method**

Pricing under this method is based on **actual physical flow of goods**.

It attributes specific costs to identified goods and requires keeping different lots purchased separately to identify the lot out of which units in inventories are left.

The historical costs of such specific purpose inventories may be determined on the basis of their specific purchase price or production cost.

This method is generally used to ascertain the cost of inventories of items that are not ordinarily interchangeable and their value is high like expensive medical equipment.

Ex. 1 : Surekha Ltd deals in 3 products P, Q & R, which are neither similar nor interchangeable. At the end of a financial year, the Historical Cost and NRV of items of closing stock are given below. Determine the value of closing stock.

Items	Historical Cost (in ₹Lakhs)	Net Realisable Value (in ₹Lakhs)
P	38	42
Q	29	29
R	17	14

Answer :

Inventories are to be valued at the **lower** of cost and Net Realisable Value (NRV).

Inventories are usually written down to NRV on an item-by-item basis. The value of closing stock is determined as under:

Items	Historical Cost (in ₹Lakhs)	Net Realisable Value (in ₹Lakhs)	Valuation = Least of Cost or NRV
P	38	42	38
Q	29	29	29
R	17	14	14
Total			**81**

(ii) **First In First Out (FIFO)**

This method assumes that the items of inventories which were purchased or produced first are consumed or sold first and consequently items remaining in the inventory at the end of the period are those most recently purchased or produced.

This assumption is in line with the good business practice to disposing goods in the order of their acquisition especially in the case of **perishable goods** and items with **frequent technological changes.**

It must be kept in mind that this assumption of cost flow or goods flow need not be true as a physical fact i.e. not necessary goods are physically also sold or issued in the chronological order of their purchase or production. It **relates only to** the method of accounting **and not** to the actual physical movement of goods.

(iii) **Last In Last Out (LIFO)**

Under this basis, goods issued are valued at the price paid for the latest lot of goods on hand which means inventory of goods in hand is valued at price paid for the earlier lot of goods.

LIFO method is based on an irrational assumption that inventories entering last in the stores are issued or consumed first. However, the flow of goods which is generally observed in business entities is contradictory to this assumption.

LIFO method is **no longer adopted** for valuing inventories.

Accounting Standards also **does not permit** the usage of LIFO Method.

Generally, in practice, FIFO and Weighted Average Price Method are popular among the business entities and both these methods are also permitted by Accounting Standards."

During periods of **rising prices or inflationary conditions,**

If FIFO is followed, cost of goods sold are valued at older and lower prices and consequently reported profits rise due to lower cost of goods sold.

Value of closing inventory will be high as closing inventories are valued at latest and higher purchase prices.

On the other hand, if LIFO is followed, cost of goods sold are valued at latest and higher prices and consequently reported profits are low due to higher cost of goods sold. Value of closing inventory will be low as closing inventories are valued at latest and higher purchase prices.

(iv) Simple Average Price Method

Simple Average price for computing value of inventory is a very simple approach. All the different prices are added together and then divided by the number of prices. The closing inventory is then valued according to the price ascertained. This method is generally followed by the entities using periodic inventory method as it does not require efforts of identifying that closing inventory belongs to which consignments or lots.

(v) Weighted Average Price Method

Simple average price does not consider quantities purchased in various lots. However, it is more logical to compute weighted average price using the quantities purchased in a lot as weights.

Under weighted average price method, cost of goods available for sale during the period is aggregated and then divided by number of units available for sale during the period to calculate weighted average price per unit. Thus

$$\text{Weighted average price per unit} = \frac{\text{Total cost of goods available for sale during the period}}{\text{Total number of units available for sale during the period}}$$

Closing inventory = No. of units in inventory × Weighted average price per unit

Cost of goods sold = No. of units sold × Weighted average price per unit.

^ **Q. 1 :** A manufacturer has the following record of purchases and issues of a condenser, which he uses while manufacturing radio sets:

Purchases			Issues	
Date	Quantity (units)	Price Per Unit (₹)	Date	Quantity (units)
Dec. 4	900	50	Dec. 5	500
Dec. 10	400	55	Dec. 20	600
Dec. 11	300	55	Dec. 29	500
Dec. 19	200	60		1,600
Dec. 28	800	47		
	2,600			

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Calculate the value of closing inventory using :

(i) First In First Out Method

(ii) Last In First Out Method

(iii) Weighted Average Method

(iv) Simple Average Method

Books of A Manufacturer

(i) Stock Ledger (First In First Out Method)

	Receipts			Issues			Balance		
Date	Quantity	Rate (₹)	Amt. (₹)	Quantity	Rate (₹)	Amt. (₹)	Quantity	Rate (₹)	Amt. (₹)

(ii) Stock Ledger (Last In First Out Method)

	Receipts			Issues			Balance		
Date	Quantity	Rate (₹)	Amt. (₹)	Quantity	Rate (₹)	Amt. (₹)	Quantity	Rate (₹)	Amt. (₹)

(iii) Stock Ledger (Weighted Average Method)

	Receipts			Issues			Balance		
Date	Quantity	Rate (₹)	Amt. (₹)	Quantity	Rate (₹)	Amt. (₹)	Quantity	Rate (₹)	Amt. (₹)

(iv) Simple Average Method

* **Non-Historical Cost Methods**

Non-historical cost methods do not consider the historical cost incurred to acquire the goods. Non- historical cost methods include :

(i) Adjusted Selling Price method and **(ii)** Standard Cost method.

(i) **Adjusted selling price method**

This method is also called retail inventory method. It is used widely in retail business or in business where the inventory comprises of items, the individual costs of which are not readily ascertainable.

The use of this method is appropriate for measuring inventories of large numbers of rapidly changing items that have similar margins and for which it is impracticable to use other costing methods.

The cost of the inventory is determined by reducing from the sales value of the inventory an appropriate percentage of gross margin.

^ **Q. 2 :** M/s X, Y and Z are in retail business, following information are obtained from their records for the year ended 31st March, 2022 :

Goods received from suppliers	₹15,75,500
(subject to trade discount and taxes)	
Trade discount 3% and GST 11%	
Packaging and transportation charges	₹87,500
Sales during the year	₹22,45,500
Sales price of closing inventories	₹2,35,000

Find out the non-historical cost of inventories using adjusted selling price method.

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(ii) **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.

^ **Sale of Goods on Approval or Return Basis**

Refer chapter 7, Final Accounts of Sole Proprietors ; post Q. 2 (Ganguli)

^ **Consignment**

To consign means to send.

It is a situation where one person (or firm) sends goods to another person (or firm) on the basis that the goods will be sold on behalf of and at the risk of the former.

The party which sends the goods (consignor) is called principal.

The party to whom goods are sent (consignee) is called agent.

The ownership of the goods, i.e., the property in the goods, remains with the consignor or the principal – the agent or the consignee does not become their owner even though goods are in his possession. On sale, of course, the buyer will become the owner.

It is the consignor who has to record the closing stock of the consigned goods since he is the owner of the goods.

^ **Inventories Taking**

Normally all operations are suspended for one or two days during the financial year and physical inventory is taken for everything in the godown or the store periodically. For the year-end inventory valuation, physical inventory taking is done during the last week of the financial year or during the first week of next financial year.

If inventory taking is finished on 26th March, whereas accounting year ends on 31st March, purchases and sales between 26th and 31st March are then separately adjusted.

Later, a value is put on each item. The principle of Cost or Net realizable value, whichever is lower, is applied either for the inventory as a whole or item by item.

Normally, enterprises prefer to perform inventory taking on the **closing day**, however, sometimes inventory taking cannot be carried out on the closing day. It is carried out a few days later or sometimes even a few days earlier. In such a case, the actual value of the inventory must be so adjusted as to relate it to the end of the year concerned.

For doing so, it will be necessary to take into account the goods that have come in (purchases and sales returns) and those that have gone out (sales and purchase returns) during the interval between the close of the year and the date of actual inventory taking. Further, the adjustment of all goods must be on the basis of cost or NRV whichever is lower.

^ **Q. 3 :** Physical verification of stock in a business was done on 23rd June, 2022. The value of the stock was ₹48,00,000. The following transactions took place between 23rd June to 30th June, 2022:

(i) Out of the goods sent on consignment, goods at cost worth ₹2,40,000 were unsold.

(ii) Purchases of ₹4,00,000 were made out of which goods worth ₹1,60,000 were delivered on 5th July, 2022.

(iii) Sales were ₹13,60,000, which include goods worth ₹3,20,000 sent on approval. Half of these goods were returned before 30th June, 2022.

(iv) Goods are sold at cost plus 25%. However, goods costing ₹2,40,000 had been sold for ₹1,20,000.

Determine the value of stock on 30th June, 2022.

^ **Q. 4 :** Sky Ltd. keeps no stock records but a physical inventory of stock is made at the end of each quarter and the valuation is taken at cost. The company's year ends on 31st March, 2018 and their accounts have been prepared to that date. The stock valuation taken on 31st March, 2018 was however, misleading and you have been advised to value the closing stocks as on 31st March, 2018 with the stock figure as on 31st December, 2017 and some other information is available to you :

(i) The cost of stock on 31st December, 2017 as shown by the inventory sheet was was ₹80,000.

(ii) On 31st December, stock sheet showed the following discrepancies :

(a) A page total of ₹5,000 had been carried to summary sheet as ₹6,000.

(b) The total of a page had been undercast by ₹200.

(iii) Invoice of purchases entered in the Purchase Book during the quarter from January to March, 2018 totalled ₹70,000. Out of this ₹3,000 related to goods received prior to 31st December, 2017. Invoices entered in April 2018 relating to goods received in March, 2018 totalled ₹4,000.

(iv) Sales invoiced to customers totalled ₹90,000 from January to March, 2018. Of this ₹5,000 related to goods dispatched before 31st December, 2017. Goods dispatched to customers before 31st March, 2018 but invoiced in April, 2018 totalled ₹4,000.

(v) During the final quarter, credit notes at invoiced value of ₹1,000 had been issued to customers in respect of goods returned during that period. The gross margin earned by the company is 25% of cost.

You are required to prepare a statement showing the amount of stock at cost as on 31st March, 2018.

Q. 5 : From the following particulars ascertain the value of inventories as on 31st March, 2022:

	(₹)		(₹)
Inventory as on 1.4.2021	1,42,500	Administrative Expenses	30,000
Purchases	7,62,500	Financial Charges	21,500
Manufacturing Expenses	1,50,000	Sales	12,45,000
Selling Expenses	60,500		

At the time of valuing inventory as on 31st March, 2021, a sum of ₹ 17,500 was written off on a particular item, which was originally purchased for ₹ 50,000 and was sold during the year for ₹ 45,000. Barring the transaction relating to this item, the gross profit earned during the year was 20 % on sales.

Q. 6 : The Profit and loss account of Hanuman showed a net profit of ₹ 6,00,000, after considering the closing stock of ₹ 3,75,000 on 31st March, 2022. Subsequently the following information was obtained from scrutiny of the books :

(i) Purchases for the year included ₹ 15,000 paid for new electric fittings for the shop.

(ii) Hanuman gave away goods valued at ₹ 40,000 as free samples for which no entry was made in the books of accounts.

(iii) Invoices for goods amounting to ₹ 2,50,000 have been entered on 27th March 2022, but the goods were not included in stock.

(iv) In March, 2022 goods of ₹ 2,00,000 sold and delivered were taken in the sales for April, 2022.

(v) Goods costing ₹ 75,000 were sent on sale or return in March, 2022 at a margin of profit of 33-1/3% on cost. Though approval was given in April, 2022 these were taken as sales for March, 2022.

Calculate the value of stock on 31st March, 2022 and the adjusted net profit for the year ended on that date.

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^ **Additional Theory**

* **Basis of Inventory Valuation**

Inventories should be generally valued at the **lower of cost or net realizable value.**

Cost : As per Accounting Standards, Cost of inventories should comprise

1. all cost of purchase,
2. costs of conversion (primarily for finished goods and work - in progress) and
3. other costs incurred in bringing the inventories to their present location and condition.

Cost of purchase consist of purchase price including duties and taxes (other than those subsequently recoverable by the enterprise from the taxing authorities), freight inwards and other expenditure directly attributable to the acquisition. Trade discounts, rebates, duty drawbacks and other similar items are deducted in determining costs of purchase. In other words, cost includes any amount paid to the seller reduced by any discounts / rebates given by the seller. Similarly, any duties paid to the supplier will be part of cost of the inventory unless the enterprises can recover these taxes duties from the authorities.

For example - Raw material required for making a product is bought at 100 per unit plus GST at 18%. 100 units of raw material are bought.

So, the amount that needs to be paid is -

100 units × ₹100 = ₹10,000 + GST at 18% = ₹11,800.

However, since the GST on purchase is available as credit, it won't be counted as the cost of purchase. Hence, the cost of purchase will be ₹10,000 only and not ₹11,800.

Costs of conversion of inventories include costs directly related to the units of production, such as direct labour. They also include a systematic allocation of fixed and variable overheads.

Continuing the above example – for the conversion of 100 units of raw material into finished goods, direct labour cost incurred is ₹3,000. Then, the cost of conversion will be ₹3,000 and thus the value of inventory at this stage is ₹13,000 (for 100 units).

Other Costs may include administrative overheads incurred to bring the inventory into present location and condition or any cost specifically incurred on inventory of a specified customer. Interest and other borrowing costs are generally not included in the cost of inventory. However, in some circumstances where production process is longer and it is required to carry inventory for a long period e.g. wine, rice and timber it may be appropriate to consider interest and other borrowing cost also part of cost of inventory.

In the same example let us assume that ₹200 is paid as unloading charges for the raw material from the truck to the storage place in the factory, in that case ₹200 shall NOT be accounted as unloading charges separately as expenses, but shall be accounted as other costs to bring the inventory to present location. And hence the cost of inventory of 100 units at this stage shall be ₹13,200.

Exclusions from cost of inventories : Following expenses are generally not included in the costs of inventories:

(a) abnormal amounts of wasted materials, labour or other production overheads:

(b) storage costs, unless those costs are necessary in the production process prior to further production stage;

(c) administrative overheads that do not contribute to bringing the inventories to their present location and condition; and

(d) selling and distribution costs

Brief explanation about the exclusions from the cost of inventories :

(a) Normal wastage of material or labour cost is included in the cost of inventory. However, abnormal wastage is excluded for the reason that it occurs either due to inefficiency or abnormal factors that won't justify considering those wastages as part of inventory cost.

(b) Storage costs are normally the cost of doing business. For example, rent of warehouse or storage area is considered as overheads already and hence not considered as cost of inventory. However, if special storage is required as part of the production process, then such storage cost is considered as cost of inventory. For example, in wine making process, requires the raw material is stored in a particular condition for fermentation for a long time (usually years together), such cost of storage is accounted as cost of inventory.

(c) Administrative overheads do not usually add any specific value to inventories and hence excluded.

(d) Selling and distribution costs are part of selling and general administration costs and hence excluded.

Net realizable value : This is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. In case of finished goods and traded goods net realizable value will generally mean selling price which is reduced by selling and distribution expenses. In case of work in progress, expenses and overheads required to be incurred to convert work -in progress into finished goods and making it ready for sale will also be reduced from selling price. In case of raw materials, replacement cost is generally considered as net realizable value.

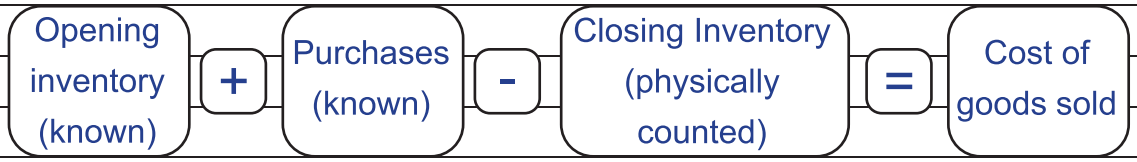
An assessment is made of as at each balance sheet date. Inventories are usually written down to net realizable value on an item-by-item basis. In some circumstances, however, it may be appropriate to group similar or related items e.g. in case of interchangeable items it may not be possible to identify cost and net realizable value of each item separately.

* Inventory Record Systems

There are **two** principal systems of determining the physical quantities and monetary value of inventories sold and in hand. One system is known as 'Periodic Inventory System' and the other as the 'Perpetual Inventory System'. The periodic system is less expensive to use than the perpetual method. But the useful information obtained from perpetual system is more than cost incurred on it. These systems are distinguished on the basis of the actual records kept to ascertain the cost of goods sold and the closing inventory valuations.

1 Periodic Inventory System

Periodic inventory system is a method of ascertaining inventory by taking an actual physical count (or measure or weight) of all the inventory items on hand at a particular date on which inventory is valued. It is because of actual physical count that the system is also called physical inventory system. The cost of goods sold is determined as shown below:



Periodic inventory system is simple and less expensive than the perpetual system. In this system, inventory account is adjusted at the end of the accounting period to determine cost of goods sold. This system suffers from various limitations :

(i) Physical inventory taking is required more than once a year for preparation of quarterly or half yearly financial statements thereby making this system more expensive.

(ii) Physical count of goods requires closure of normal operations of business.

(iii) As cost of goods sold is taken as residual figure, it is not possible to identify loss of goods due to pilferage, damage or even fraud.

(iv) Inventory control is not possible under this system.

(v) Books of accounts does not reflect inventory in hand and its value therefore, it is difficult to plan operations e.g. how much or when to order/manufacture.

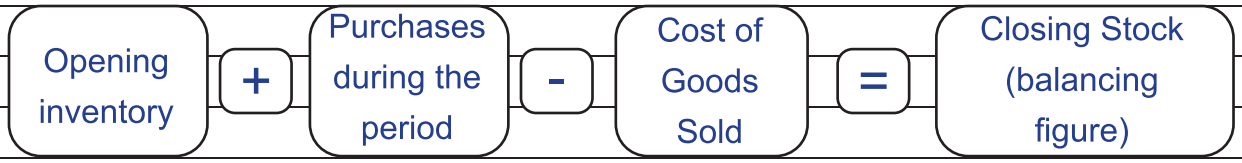
This system is used by small enterprises where it is easy to control physical inventory. This system is not considered suitable for medium or larger enterprises which generally use Perpetual Inventory system.

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2 **Perpetual Inventory System**

Perpetual inventory system is a system of recording inventory balances after each receipt and issue. In order to ensure accuracy of perpetual inventory records, physical inventory should be checked and compared with recorded balances. Under this system, cost of goods issued is directly determined and inventory of goods is taken as residual figure with the help of inventory ledger in which flow of goods is recorded on continuous basis. The basic feature of this system is the maintenance of inventory ledger to have records of goods on continuous basis.

Under perpetual inventory system, closing inventory is determined as follows :



Perpetual inventory system helps to overcome the limitations of periodic system. As inventory is taken as residual figure, it includes loss of goods. However, the main limiting factor is the high cost of using this system.

Distinction between Periodic Inventory System and Perpetual Inventory System

Both the systems - Periodic Inventory System and Perpetual Inventory System are not mutually exclusive and complementary in nature.

Distinction between both the systems can be explained as follows:

S. No.	Periodic Inventory System	Perpetual Inventory System
1	This system verification is based on physical verification.	It is based on book records.
2	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.
3	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.
4	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.
5	Under this method, inventory control is not possible.	Inventory control can be exercised under this system.

S. No.	Periodic Inventory System	Perpetual Inventory System
6	This system is simple and less expensive.	It is costlier method.
7	Periodic system requires closure of business for counting of inventory.	Inventory can be determined without affecting the operations of the business.

^ **Try Yourself : Objectives**

* **State True or False with reasons :**

1. Inventories are stocks of goods and materials that are maintained for mainly the purpose of revenue generation.
2. A building is considered inventory in a construction business.
3. Inventory is valued as carrying cost less percentage decreases.
4. Management has daily information about the quantity and valuation of closing stock under physical Inventory System.
5. Periodic Inventory System is more suitable for small enterprises.
6. When closing inventory is overstated, net income for the accounting period will be understated.
7. Closing inventory = Opening inventory + Purchases + Direct expenses + Cost of goods sold.
8. Cost of inventories should comprise all cost of purchase.
9. Inventory by-products, should be valued at net realisable value where cost of by products can be separately determined.
10. Abnormal amounts of wasted materials, labour or other production overheads expenses are included in the costs of inventories.
11. Perpetual system requires closure of business for counting of inventory.
12. Periodic inventory system is a method of ascertaining inventory by taking an actual physical count.
13. The value of closing inventory under simple average price method is realistic as compare to LIFO.
14. The value of stock is shown on the assets side of the balance-sheet as fixed assets.
15. Under inflationary conditions, FIFO will not show lowest value of cost of goods sold.
16. Under LIFO, valuation of inventory is based on the assumption that costs are charged against revenue in the order in which they occur.
17. Valuation of inventory, at cost or net realisable value, whichever less, is based on the principle of Conservatism.
18. Finished goods are normally valued at cost or market price whichever is higher.
19. Warehouse rent paid for storage of finished inventory should be included in the cost of finished inventory.

Answers :

1	**True**
	Inventories refers to stocks of goods and materials that are maintained in business for revenue generation.
2	**True**
	For a construction business, a building under construction will be inventory. The building is being built in the normal course of business and will eventually be sold as inventory.
3	**False**
	Inventory is valued at lower of cost or net realizable value.
4	**False**
	Under Perpetual Inventory System management have daily information of closing stock.
5	**True**
	A periodic inventory system is suitable to small and micro enterprises, where physical counting of inventory is not a tedious process.
6	**False**
	When closing inventory is overstated, net income for the accounting period will be overstated.
7	**False**
	Closing stock = Cost of goods sold - (Opening inventory + Purchases + Direct expenses).
8	**False**
	Cost of inventories should comprise all cost of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.
9	**False**
	Inventory by-products, should be valued at net realisable value where cost of by products cannot be separately determined. .
10	**False**
	Abnormal amounts of wasted materials, labour or other production overheads expenses are generally not included in the costs of inventories.

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11	**False**
	Periodic system requires closure of business for counting of inventory.
12	**True**
	Under Periodic inventory system actual physical count of inventory is taken of all the inventory on hand at a particular date.
13	**True**
	Value of Closing stock as per average method is more realistic then LIFO.
14	**False**
	The value of stock is shown on the assets side of the balance-sheet as current assets. As it is realisable within 12 months.
15	**False**
	Under inflationary conditions, LIFO and weighted average will not show lowest value of cost of goods sold.
16	**False**
	Under FIFO, valuation of inventory is based on the assumption that costs are charged against revenue in the order in which they occur.
17	**True**
	The conservatism concept states that one shall not account for anticipated profits but shall provide all prospective losses. Valuing inventory at cost or net realisable value whichever is less, therefore is based on principle of Conservatism.
18	**False**
	Finished goods are normally valued at cost or market price whichever is lower.
19	**False**
	Warehousing costs related to finished goods are expensed when incurred and are not included in inventory costs unless storage is incurred for getting the inventory ready for sale i.e. until and unless storage is required as a part of process of production of inventory like in case of wine.

*	**Multiple Choice Questions**
1	The amount of purchase if Cost of goods sold is ₹80,700 Opening Inventory ₹5,800
	Closing Inventory ₹6,000
	(a) ₹80,500 (b) ₹74,900 (c) ₹80,900.
2	Average Inventory = ₹12,000. Closing Inventory is ₹3,000 more than opening Inventory.
	The value of closing Inventory =_____.
	(a) ₹12,000 (b) ₹24,000 (c) ₹13,500
3	While finalizing the current year's profit, the company realized that there was an error in
	the valuation of closing Inventory of the previous year. In the previous year, closing
	Inventory was valued more by ₹50,000. As a result
	(a) Previous year's profit is overstated and current year's profit is also overstated
	(b) Previous year's profit is overstated and current year's profit is understated
	(c) Previous year's profit is understated and current year's profit is also understated
4	Consider the following for Q Co. for the year 2021-22:
	Cost of goods available for sale ₹1,00,000
	Total sales ₹80,000
	Opening inventory of goods ₹20,000
	Gross profit margin on sales 25%
	Closing inventory of goods for the year 2021-22 as
	(a) ₹80,000 (b) ₹60,000 (c) ₹40,000
5	If the profit is 25% of the cost price then it is
	(a) 25% of the sales price (b) 33% of the sales price (c) 20% of the sales price
6	Goods purchased ₹1,00,000. Sales ₹90,000. Margin 20% on cost. Closing Inventory =?
	(a) ₹20,000 (b) ₹10,000 (c) ₹25,000
7	A company is following weighted average cost method for valuing its inventory.
	The details of its purchase and issue of raw-materials during the week are as follows:
	1.12.2022 opening Inventory 50 units value ₹2,200.
	2.12.2022 purchased 100 units @ ₹47.
	4.12.2022 issued 50 units.
	5.12.2022 purchased 200 units @ ₹48.
	The value of inventory at the end of the week and the unit weighted average costs is
	(a) ₹14,200 – ₹47.33 (b) ₹14,300 – ₹47.67 (c) ₹14,000 – ₹46.66

8 The cost of sales is equal to
(a) Opening stock plus purchases
(b) Purchases minus Closing stock
(c) Opening stock plus purchases minus closing stock

9 Inventory is disclosed in financial statements under:
(a) Fixed Assets (b) Current Assets (c) Current Liabilities

10 Accounting Standards do not permit following method of inventory valuation
(a) FIFO (b) Average cost (c) LIFO

11 Which inventory costing formula calculates value of closing inventory considering that inventory most recently purchased has not been sold?
(a) FIFO (b) LIFO (c) Weighted average cost

12 Valuing inventory at cost or net releasable value is based on which principle
(a) Consistency (b) Conservatism (c) Going concern

13 Under inflationary trend, which of the methods will show highest value of inventory?
(a) FIFO (b) Weighted average cost (c) LIFO

14 Which of the following methods does not consider historical cost of inventory?
(a) Weighted average (b) FIFO (c) Retail price method

Answers :

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

^ **Theoretical Questions**

1 Write short notes on:
(i) Adjusted Selling Price method of determining cost of stock.
(ii) Principal methods of ascertainment of cost of inventory.

2 Distinguish between:
(i) LIFO and FIFO basis of costing of stock.
(ii) FIFO and weighted average price method of stock costing.

3 Define inventory. Explain the importance of proper valuation of inventory in the preparation of statements of the business entity.

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Answers :

1 (i) Adjusted selling method is also called retail inventory method. It is used widely in retail business or in business where the inventory comprises of items, the individual costs of which are not readily ascertainable. The historical cost of inventory is estimated by calculating it in the first instance at selling price and then deducting an amount equal to the estimated gross margin of profit on such stocks.

(ii) The specific identification method, First-In–First-Out (FIFO) and weighted average cost formulae are the principal methods of ascertaining the cost of inventory.

The cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects should be assigned by specific identification of their individual costs under the specific identification method.

2 (i) Under FIFO method of inventory valuation, inventories purchased first are issued first. The closing inventories are valued at latest purchase prices and inventory issues are valued at corresponding old purchase prices. In other words, under FIFO method, costs are assigned to the units issued in the same order as the costs entered in the inventory. During periods of rising prices, cost of goods sold are valued at older and lower prices if FIFO is followed and consequently reported profits rise due to lower cost of goods sold.

On the other hand, under LIFO method of inventory valuation, units of inventories issued should be valued at the prices paid for the latest purchases and closing inventories should be valued at the prices paid for earlier purchases. In other words, closing inventories are valued at old purchase prices and issues are valued at corresponding latest purchase prices.

(ii) Under the First-In-First-Out (FIFO) method of valuation of stock, the actual issue of goods is usually the earliest lot on hand. Hence, the stock in hand will therefore consist of the latest consignments. The closing stock is valued at the price paid for such consignments.

The weighted average price method is not a simple average price method. Under this method of valuation of stock, a stock ledger is maintained, recording receipts and issues on daily basis. A new average would be calculated on receiving fresh consignment. The average price thus calculated after considering arrival of new consignment with the previous value of stock and dividing the preceding stock value and the cost of new arrival with the total units of preceding and new arrival will give the weighted average price.

3 Inventory can be defined as assets held

- for sale in the ordinary course of business, or
- in the process of production for such sale, or
- for consumption in the production of goods or services for sale, including maintenance supplies and consumables other than machinery spares.

The significance of inventory valuation arises due to the following reasons:

(i) Determination of Income

(ii) Ascertainment of Financial Position

(iii) Liquidity Analysis

(iv) Statutory Compliance

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357/400

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TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



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308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
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SORABH MOHATA
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SANA DESHPANDE
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MEETALI MAHESHWARI
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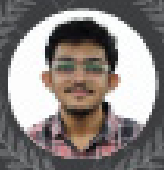
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DURGASHRI VS
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319



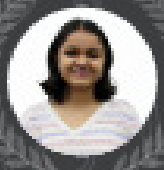
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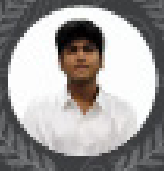
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305



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and many more...

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AIR 13



MANAN SHAH
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AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHRUTI SHIVARAM
CA INTER NOV'23
AIR 47

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CA FINAL NOV'23

AIR 2



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AIR 6



SHRUTI PAROLIA
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AIR 8



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AIR 17



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RITIK SANGHAVI
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SCAN ME!

a. Final Accounts of Non-Manufacturing Entities

^ **Introduction**

After the Trial Balance is prepared,

next step in the accounting process is preparation of Final Accounts, which includes :

(To know **Financial Performance** during the year)

I) Trading A/c for the year ended ……..

(To find out **Gross Profit** earned during the year)

II) Profit & Loss A/c for the year ended ……..

(To find out **Net Profit** earned / Net Loss suffered during the year)

(To know **Financial Position** as on date)

III) Balance Sheet as on ……..

(Assets, Liabilities & Capital as on the date)

^ **Trial Balance** (summarised effect of **all recorded transactions** during the year)

TRIAL BALANCE as on (last day of the accounting year)

Sr. No.	Head of Accounts	L.F.	Debit ₹	Credit ₹
I)	**Accounts** to be transferred to **Trading A/c**			
1	**Opening Stock**		●	
	(Stock of unsold goods in hand at the **start** of the year)			
2	**Purchases**		●	
	(Total goods purchased by us from suppliers during the year,			
	on cash & credit, both)			
3	**Purchase Returns / Returns Outwards**			●
	(Goods returned by us to suppliers)			
4	**Sales**			●
	(Total goods sold by us to customers during the year,			
	on cash & credit, both)			
5	**Sales Returns / Returns Inwards**		●	
	(Goods returned by customers to us)			

6	**Direct Expenses**			
	a) Expenses incurred **on purchase** of goods		●	
	Carriage / Freight Inwards (Transportation expenses)			
	Insurance during transit, Customs (Import) duty,			
	Clearing charges, Demurrage (charges paid for the use of			
	container outside the terminal or depot, beyond the free time			
	period) etc.			
	b) Expenses incurred **on production** of goods		●	
	Wages, Coal, Gas, Water, Power & Fuel, Factory Rent,			
	Consumable stores (used in production to keep machine			
	in proper working condition) (engine oil, cotton waste, soft			
	soap, oil & grease consumed in factory etc), Royalties etc.			

^ **Calculation of Gross Profit**

Trading Account is prepared, at the end of the period, to determine Gross profit for that accounting period (usually a year). It is a **Nominal Account**.

It is **based on the matching concept**, where in Revenue from sale of goods and cost of goods sold are recognised in the same period.

It is calculated by preparing Trading A/c, as follows

Dr. **Trading A/c for the year ended** …. (last day of the year) **Cr.**

Particulars	₹	₹	Particulars	₹	₹
To Opening Stock		xxx	By Sales	xxx	
To Purchases	xxx		Less : Sales Returns	(xx)	xxx
Less : Purchase Returns	(xx)	xxx			
			By Closing Stock *		**xxx**
To Direct Expenses		xxx			
To Gross Profit c/d		xxx			
		XXX			**XXX**

Note :

* **2nd effect of Closing Stock : Show it seperately, B A**

* **Adjustment**

= Unrecorded Transaction (**or** Wrongly Recorded Transaction)

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^ **TRIAL BALANCE** as on ..... (last day of the accounting year)

Sr. No.	Head of Accounts	L.F.	Debit ₹	Credit ₹
II)	**Accounts** to be transferred to **Profit & Loss A/c**			
	Indirect Expenses (& losses)		●	
	Sundry Incomes (& gains)			●

* **Indirect Expenses**

Indirect Expenses are those expenses **which are not** direct expenses
i.e. which are **neither** incurred on purchase of goods **nor** incurred on production of goods.

Examples of Indirect Expenses (& losses)

Salaries, Electricity, Printing & stationery, Postage & telegram, Conveyance,
Travelling expenses, Telephone expenses, Internet charges, Audit fees, Advertisement,
Sales promotion expenses, Commission, Discount allowed, Rebate, Depreciation,
Rent, Repairs & maintenance, Carriage / Freight outward, Insurance, Legal expenses,
Accounting charges, Staff welfare expenses, Bad debts, Bank charges
General / Sundry / Miscellaneous / Trade expenses, Charity, Donation,
Interest on loans taken, Loss on sale of fixed assets, loss by fire, loss by theft **etc.**

* **Examples of Sundry Incomes (& gains)**

Discount received, Commission received, Rent received, Interest received,
Baddebts Recovered, Dividend on shares, Interest on Investments,
Profit on sale of fixed assets, Profit on sale of Investments **etc.**

^ **Calculation of Net Profit (or Net Loss)**

Profit & Loss A/c is prepared to find out Net Profit (or Net Loss) for the period.
It is a **Nominal Account**.

Dr. Profit & Loss A/c for the year ended ...(last date of the year) Cr.

Particulars	₹	₹	Particulars	₹	₹
			By Gross Profit b /d		xxx
To Indirect Expenses		xxx	By Sundry Incomes		xxx
(& Losses)			(& Gains)		
To Net Profit		xxx			
		XXX			**XXX**

^ **TRIAL BALANCE** as on.... (last day of the accounting year)

Sr. No.	Head of Accounts	L.F.	Debit ₹	Credit ₹
III)	**Accounts** to be written in **Balance Sheet**			
	Real Accounts		●	
	Personal Accounts of Debtors		●	
	Personal Accounts of Creditors			●
	Capital A/c			●
	Drawings A/c		●	

^ **Balance Sheet as on ....** (last day of the year)

Liabilities	₹	₹	Assets	₹	₹
Capital			**Fixed Assets**		
(Personal A/c of proprietor)			(Real Accounts)		
Borrowed Funds			**Investments**		
(Personal A/c of creditors)			(Real Accounts)		
Current Liabilities			**Current Assets**		
(Personal A/c of creditors)			(Real Accounts)		
			(Personal A/c's of debtors)		

Assets

It includes **Debit Balances** of : All Real Accounts **&** Personal Accounts of Debtors

Liabilities (External Liabilities + Internal Liability)

It includes **Credit Balances** of Personal Accounts of Creditors

All Nominal accounts **are closed** at the end of period.

Generally , balances of Nominal accounts is not carried forward to next year and hence, doesn't appear in Balance Sheet.

^ **Summary : Trial Balance items** (various Ledger Accounts balances)

* **I) Accounts relating to Goods**

		Debit	Credit	
1	Opening stock	xxx		**TD**
2	Purchases	xxx		**TD**
3	Pur Ret. / Ret. O.		xxx	**TD** : Less from Purchases
4	Sales		xxx	**TC**
5	Sales Ret. / Ret. I.	xxx		**TC** : Less from Sales

* **II) Other Nominal Accounts**

		Debit	Credit	
1	Direct Expenses	xxx		**TD** (Exp.s on purchase or production of goods)
2	Indirect expenses			
	& Losses	xxx		**PD**
3	Incomes, Gains /			
	Profits		xxx	**PC**

* **III) Other Real Accounts**

		Debit	Credit	
1	Tangible Fixed assets	xxx		**BA**
2	Intangible Fixed assets	xxx		**BA**
3	Investments	xxx		**BA**
4	Other assets	xxx		**BA**
	(eg. Cash)			

* **IV) Personal Accounts**

		Debit	Credit	
1	Capital	xxx	xxx	Capital A/c : Opening Balance
2	Drawings	xxx		Capital A/c : Dr. Side
3	various Debtors	xxx		(money or moneys worth **receivable** in future) **BA**
4	various Creditors		xxx	**BL** (money or moneys worth **payable** in future)

* **Trial Balance Item : One effect**

Debit balances : Debit side (T D / P D / B A) **or** deduct from credit side

Credit balances : Credit side (T C / P C / B L) **or** deduct from debit side

* **Adjustment : Two effects,**

One **DEBIT** effect **&** Other **CREDIT** effect

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Ex. 1 : The following is the Trial Balance of C. Wanchoo on 31st March, 2022.

Particulars	₹	₹
Capital Account		10,50,000
Drawings	50,000	
Inventories as on 1st April, 2021	2,00,000	
Cash in hand	1,44,000	
Machinery Account	7,36,000	
Purchases Account	18,20,000	
Wages Account	10,00,000	
Salaries Account	10,00,000	
Discount Allowed A/c	50,000	
Discount Received A/c		30,000
Sundry Office Expenses Account	6,00,000	
Sales Account		50,00,000
Sums owing by customer (Trade receivables)	8,50,000	
Trade payables (sums owing to suppliers)		3,70,000
Total	**64,50,000**	**64,50,000**

Value of closing inventory on 31st March, 2022 was ₹ 2,70,000.

Pass closing entries for the above items and prepare Trading and Profit and Loss A/c.

In the books of C. Wanchoo

Dr. Trading A/c for the year ended 31st March 2022 Cr.

Particulars	₹	₹	Particulars	₹	₹
To Opening Inventory		2,00,000	By Sales		50,00,000
To Purchases		18,20,000			
To Wages		10,00,000	By Closing Inventory		2,70,000
To Gross Profit c/d		22,50,000			
		52,70,000			**52,70,000**

Dr. Profit and Loss A/c for the year ended 31st March 2022 Cr.

Particulars	₹	₹	Particulars	₹	₹
To Salaries		10,00,000	By Gross Profit b/d		22,50,000
To Discount Allowed		50,000	By Discount Received		30,000
To Sundry Office Expenses		6,00,000			
To Net Profit		6,30,000			
		22,80,000			**22,80,000**

Journal Proper

Date	Particulars	L.F.	Debit (₹)	Credit (₹)

Date	Particulars	L.F.	Debit (₹)	Credit (₹)

Valuation of Closing Stock

Closing stock indicates value of goods in hand **at the end** of the period.

Generally, Closing stock is **not** part of Trial balance.

It is being given effect in books of accounts after Trial Balance is extracted, it is **part of Adjustments** while preparing Final Accounts.

According to the Concept of Conservatism (Prudence),
Closing stock is **valued at** cost price or net realizable value (market value),
whichever is lower.

	Adjustment (Journal entry)	Effects in Final A/c's					
1	**Closing Stock of Goods**						
	Closing Stock A/c Dr.		BA	D			
	To Trading A/c **or** Pur. A/c					TC	C
2	**Depreciation on Fixed Asset**						
	Depreciation A/c Dr.		PD	D			
	To FA / PFD A/c				Less from FA	BA	C
3	**Outstanding Expenses**						
4	**Outstanding Incomes**						
5	**Prepaid Expenses**						
6	**Pre received Incomes**						
7	**Goods distributed as free samples**						

	Adjustment (Journal entry)	Effects in Final A/c's
8	**Goods withdrawn by proprietor for personal use**	
9	**Baddebts written off**	
10	**Reserve / Provision for Doubtful Debts (R.D.D.)**	
11	**Interest on Capital (I.O.C.)**	
12	**Interest on Drawings (I.O.D.)**	
13	**Reserve** / Provision **for Discount on Debtors (R.F.D.D.)**	
14	**Reserve / Provision for Discount on Creditors (R.F.D.C.)**	
15	**Wages paid for installation of plant and machinery included in wages**	

	Adjustment (Journal entry)	Effects in Final A/c's
16	**Purchases include purchase of furniture**	
17	**Credit purchases omitted to be recorded in purchase day book (unrecorded purchases)**	
18	**Credit sales omitted to be recorded in sales day book (unrecorded sales)**	
19	**Included in debtors is ₹ 3,000 due from Ram and included in creditors ₹ 1,000 due to him**	

^ **Effect of** few **Trial Balance A/c's** (usually part of adjustments)

	Account	Balance	Effect in Final Accounts
1	Outstanding Expense	Credit	
2	Outstanding / Accrued Income	Debit	
3	Prepaid Expense	Debit	
4	Pre received Income	Credit	
5	Depreciation	Debit	
6	Closing Stock	Debit	

^ Final Accounts : **'Standard Format'** per solution

Page 1	Trading A/c	approx 20 lines
Page 2	Profit & Loss A/c	full page
Page 3	Balance Sheet	full page
Page 4	Capital A/c, Provision for Doubtful Debts A/c, Provision for Discount on Debtors A/c & Other Workings	

TD	**Trading A/c, Dr. side**	**TC**	**Trading A/c, Cr. side**
PD	**Profit & Loss A/c, Dr. side**	**PC**	**Profit & Loss A/c, Cr. side**
BL	**Balance Sheet, Liabilities side**	**BA**	**Balance Sheet, Assets side**

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^ **Q. 1 :** The following is the schedule of balances as on 31.3.22 extracted from the books of Shri Gavaskar, who carries on business under the same name and style of Messrs Gavaskar Viswanath & Co., at Mumbai:

Particulars	Dr. (₹)	Cr. (₹)
Cash in hand	14,000	
Cash at bank	26,000	
Sundry Debtors	8,60,000	
Stock on 1.4.2021	6,20,000	
Furniture & fixtures	2,14,000	
Office equipment	1,60,000	
Buildings	6,00,000	
Motor Car	2,00,000	
Sundry Creditors		4,30,000
Loan from Viswanath		3,00,000
Provision for bad debts		30,000
Purchases	14,00,000	
Purchase Returns		26,000
Sales		23,00,000
Sales Returns	42,000	
Salaries	1,10,000	
Rent for Godown	55,000	
Interest on loan from Viswanath	27,000	
Rates & Taxes	21,000	
Discount allowed to Debtors	24,000	
Discount received from Creditors		16,000
Freight on purchases	12,000	
Carriage Outwards	20,000	
Drawings	1,20,000	
Printing and Stationery	18,000	
Electricity Charges	22,000	
Insurance Premium	55,000	
General office expenses	30,000	
Baddebts	20,000	
Bank charges	16,000	
Motor car expenses	36,000	
Capital A/c		16,20,000
TOTAL	**47,22,000**	**47,22,000**

Prepare Trading and Profit and Loss Account for the year ended 31st March, 2022 and the Balance Sheet as at that date after making provision for the following:

(i) Depreciate:
- (a) Building used for business by 5 percent;
- (b) Furniture and fixtures by 10 percent; One steel table purchased during the the year for ₹14,000 was sold for same price but the sale proceeds were wrongly credited to Sales Account;
- (c) Office equipment by 15 percent; Purchase of a typewriter during the year for ₹40,000 has been wrongly debited to purchase; and
- (d) Motor car by 20%.

(ii) Value of stock at the close of the year was ₹4,40,000

(iii) Two month's rent for godown is outstanding.

(iv) Interest on loan from Viswanath is payable at 12 percent per annum, this loan was taken on 1.5.2021.

(v) Provision for bad debts is to be maintained at 5 percent of Sundry Debtors.

(vi) Insurance premium includes ₹40,000 paid towards proprietor's life insurance policy and the balance of the insurance charges cover the period from 1.4.2021 to 30.6.2022.

^ **Q. 2 :** From the following particulars extracted from the books of Ganguli, prepare trading and profit and loss account and balance sheet as at 31st March, 2022 after making the necessary adjustments:

	Amt. (₹)		Amt. (₹)
Ganguli's capital account (Cr.)		Interest received	7,250
as on 1.4.2021	5,40,500	Cash with Traders Bank Ltd.	40,000
Stock on 1.4.2021	2,34,000	Discounts received	14,950
Sales	14,48,000	Investments (at 5%) as on	
Sales return	43,000	1.4.2021	25,000
Purchases	12,15,500	Furniture as on 1-4-2021	9,000
Purchases return	29,000	Discounts allowed	37,700
Carriage inwards	93,000	General expenses	19,600
Rent	28,500	Audit fees	3,500
Salaries	46,500	Fire insurance premium	3,000
Sundry debtors	1,20,000	Travelling expenses	11,650
Sundry creditors	74,000	Postage and telegrams	4,350
Loan from Dena Bank Ltd.		Cash in hand	1,900
at 12%	1,00,000	Deposits at 10% as on	
Interest paid	4,500	1-4-2021 (Dr.)	1,50,000
Printing and stationery	17,000	Drawings	50,000
Advertisement	56,000		

Adjustments:

(1) Value of stock as on 31st March, 2022 is ₹3,93,000. This includes goods returned by customers on 31st March, 2022 to the value of ₹15,000 for which no entry has been passed in the books.

(2) Purchases include furniture purchased on 1st January, 2022 for ₹10,000.

(3) Depreciation should be provided on furniture at 10% per annum.

(4) The loan account from Dena bank in the books of Ganguli appears as follows :

		₹			₹
31.3.2022	To Balance c/d	1,00,000	1.4.2021	By Balance b/d	50,000
			31.3.2022	By Bank	50,000
		1,00,000			**1,00,000**

(5) Sundry debtors include ₹20,000 due from Robert and sundry creditors include ₹ 10,000 due to him.

(6) Interest paid include ₹3,000 paid to Dena bank.

(7) Interest received represents ₹1,000 from the sundry debtors (due to delay on their part) and the balance on investments and deposits.

(8) Provide for interest payable to Dena bank and for interest receivable on investments and deposits.

(9) Make provision for doubtful debts at 5% on the balance under sundry debtors. No such provision need to be made for the deposits.

^ **Sale of Goods on Approval or Return Basis**

When a businessman wants to increase his sales or introduce a new product in the market, he usually faces hardship due to competition prevailing in the market. To counter it, goods are sometimes sent to the customers on sale or return basis. Here, goods sent on 'approval' **or** 'on return' basis means goods are delivered to the customers with the **option** to **retain** or **return** them **with in a specified period**. Generally, these transactions take place between a manufacturer (or a wholesaler) and a retailer. In current scenario, this practice is prevalent in case of online sales, where the buyer is given time of few days to return the goods if the buyer believes that the specifications of goods are different from the same mentioned on website at the time of sale. There may be certain terms and conditions to administrate the return of goods. Following are essentially the features of sale of goods on approval or return basis :

(a) There is a **change in the possession of goods** from one person to another.

(b) It **does not involve transfer of ownership of goods**. The ownership is passed only when the buyer gives his approval or if the goods are not returned within that specified period.

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(c) The **customer does not incur any liability** when the goods are merely sent to him. In case of online transactions, sometimes customers are given choice to pay on receipt of goods and in some cases they are required to pay in advance and then seller ships the goods to buyer. Even in case the buyer has paid in advance, it retains the right of refund if the goods are returned as per the terms & conditions agreed between seller and buyer.

Accounting Treatment

When the transactions are few, the seller on sending the goods, treats them as an **ordinary sale.**

If the goods are accepted or not returned or the business receives no intimation within the specified time limit, **no extra entry** is required to be passed because the entry for sale (passed at the time of sending goods) becomes the usual entry after the expiry of the specified period.

If the goods are returned within a specified time limit, a **reverse entry** is passed to cancel the previous transaction.

If, at the year-end, goods are still lying with the customers and the specified time limit is yet to expire, the entry for sales made earlier is cancelled and the value of the goods lying with the customers must be reduced from the selling price to the cost price, and treated as part of closing inventories for Balance Sheet purposes.

Journal Entries

I. During the year

1 When goods are sent on sale or return basis

Trade receivables / Customers Account	Dr.		**(At Invoice Price)**
To Sales Account			

2 When goods are rejected or returned within the specified time

Sales / Return Inwards Account	Dr.		**(At Invoice Price)**
To Customers / Trade receivables Account			

3 When goods are accepted at invoice price / no reply is received from customer within specified time

No Entry

II. At the year-end, When goods are lying with customers and the specified time limit is yet to expire

1 Reversal of sale

Sales Account	Dr.	**(At Invoice Price)**
To Customers / Trade receivables Account		

2 These goods should be considered as inventories lying with customers

Add to Closing stock and then usual journal entry	Dr.	**(Cost price or Market price, whichever is less)**
should be passed for recording total closing stock in the		
books of accounts including goods lying with customers.		

Note :

After the end of accounting period,

No entry is to be passed for goods returned by the customers on a subsequent date. If the goods are accepted or not returned or the business receives no intimation within the specified time limit, **entry for normal sale** is required to be passed.

20 Goods costing ₹10,000 sent to a customer on Sale or Return / Approval basis for ₹12,000 included in sales

a)	**Sales Value ₹12,000**						
	Sales A/c Dr.	Less from Sales	TC	D			
	To Debtors A/c				Less from Debtors	BA	C
b)	**Cost ₹10,000**						
	Add to Closing Stock						

^ **Q. 3 :** From the following trial balance and additional information of Mr. H, prepare Trading and Profit and Loss Account for the year ended March 31, and Balance Sheet as on that date

Particulars	Amt. (₹)	Particulars	Amt. (₹)
Bad debts	23,000	Rent received	65,000
Rent	1,10,000	Discount received	10,000
Wages	2,09,000	Sales	10,07,000
Building	6,00,000	Capital	13,83,000
Machinery	1,60,000	Commission received	30,000
Salaries	4,16,000	Creditors	1,90,000

Debtors (includes Shyam's	3,37,000			
dishonoured bills receivable				
of ₹8,000)				
Discount allowed	10,000			
Purchases	6,74,000			
Printing and Stationery	1,46,000			
	11,67,000			**0**

Additional Information:

1. Wages include the following amounts
   (a) ₹40,000 spent on additions to Building during the year.
   (b) ₹20,000 for erection of new machine during the year.
2. Provide 10% depreciation on Machine and Building.
3. Discount of ₹10,000 was initially allowed to a customer and was then reversed since he had not satisfied the conditions relating to discount allowance. The reversal of discount was posted to the credit of Discount Received A/c.
4. Remuneration of ₹20,000 paid to an employee stands posted to his Personal A/c.
5. Creditors include ₹55,000 received from Mr. K and credited to his account. This amount was written off as bad debts last year.
6. Goods costing ₹5,000 was taken by proprietor for personal use.
7. Goods costing ₹6,000 were sent to a customer on sale or return basis for ₹7,000 on 30th March.
8. Loss of stock due to fire on 25th March in the godown was ₹10,000. Insurance company admitted the claim at 60%.
9. Half the amount of Shyam's dishonoured bills receivable is irrecoverable.
10. Create provision of 5% on other debtors.
11. 50% of printing and stationery is to be carried forward for next year.
12. One third of the commission received is in respect of work to be done next year.
13. Rent has been paid for 11 months but has been received for 13 months.
14. Included in debtors is ₹30,000 due from Om and included in creditors ₹10,000 due to him.
15. Stock in hand is ₹4,88,880.
16. Manager is given commission of 20% of net profit after charging his commission.

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Q. 4 : From the particulars, prepare Trading and Profit and Loss Account and Balance Sheet of Mr. R -

Particulars	Dr. (₹)	Cr. (₹)
Building	5,00,000	
Machinery	2,00,000	
Furniture	1,00,000	
Cash at Bank	90,000	
Cash in Hand	10,000	
18% p.a. Loan obtained from Mr. S (taken on 1st June)		3,00,000
R's Capital		5,20,000
Sundry Debtors / Sundry Creditors	5,00,000	4,00,000
Opening Stock	1,20,000	
Purchases / Sales	25,00,000	32,20,000
Sales Return / Purchase Return	1,20,000	1,00,000
Rent	60,000	
Establishment expenses	1,80,000	
Electricity charges	15,000	
Telephone charges	10,000	
Commission on sales	30,000	
Insurance premium	10,000	
Bad debts	20,000	
Bills Receivable	75,000	
	45,40,000	**45,40,000**

Additional Information :

1. Provide for depreciation on Buildings at 5% p.a., on Machinery at 25% p.a., on Furniture at 10% p.a. Provision for bad debts is to be made at 5% on Sundry Debtors.
2. Mr. R's manager is entitled to a commission of 10% on the net profit after charging his commission.
3. Closing stock was not taken on March 31 but only on 7th April.
   Following transactions had taken place during the period from 1st April to 7th April :
   Sales ₹2,50,000, Purchases ₹1,50,000, Stock on 7th April was ₹1,80,000
   The rate of gross profit on sales was 20%.
4. Insurance premium mentioned in the trial balance was in respect of Building and Machinery.
5. Interest on loan is to be provided up to March 31.

Q. 5 : The following are the balances as at 31st March, 2017 extracted from the books of Mr. XYZ.

Particulars	Amt. (₹)	Particulars	Amt. (₹)
Plant and Machinery	19,550	Bad debts recovered	450
Furniture and Fittings	10,250	Salaries	22,550
Bank Overdraft	80,000	Salaries payable	2,450
Capital Account	65,000	Prepaid rent	300
Drawings	8,000	Rent	4,300
Purchases	1,60,000	Carriage inward	1,125
Opening Stock	32,250	Carriage outward	1,350
Wages	12,165	Sales	2,15,300
Provision for doubtful debts	3,200	Advertisement Expenses	3,350
Provision for discount on		Printing and Stationery	1,250
debtors	1,375	Cash in hand	1,450
Sundry Debtors	1,20,000	Cash at bank	3,125
Sundry Creditors	47,500	Office Expenses	10,160
Bad debts	1,100	Interest paid on loan	3,000

Additional Information:

1. Purchases include sales return of ₹2,575 and sales include purchases return of ₹ 1,725.
2. Goods withdrawn by Mr. XYZ for own consumption ₹3,500 included in purchases.
3. Wages paid in the month of April for installation of plant and machinery amounting to ₹450 were included in wages account.
4. Free samples distributed for publicity costing ₹825.
5. Create a provision for doubtful debts @ 5% and provision for discount on debtors @ 2.5%.
6. Depreciation is to be provided on plant and machinery @ 15% p.a. and on furniture and fittings @ 10% p.a.
7. Bank overdraft is secured against hypothecation of stock. Bank overdraft outstanding as on 31.3.2017 has been considered as 80% of real value of stock (deducting 20% as margin) and after adjusting the marginal value 80% of the same has been allowed to draw as an overdraft.

Prepare a Trading and Profit and Loss Account for the year ended 31st March, 2017, and a Balance Sheet as on that date. **Also show the rectification entries.**

^ **Q. 6 :** Karuna decided to start business of fashion garments under the name of M/s. Designer Wear on 1st April, 2020. She had a saving of about ₹10,00,000. She invested ₹3,00,000 out of her savings and borrowed equal amount from bank. She purchased a commercial space for ₹5,00,000 and further spent ₹1,00,000 on its renovation to make it ready for business.

Loan and interest repaid by her in the first year are as follows:

30th June, 2020 : ₹15,000 principal + ₹9,000 interest

30th September, 2020 : ₹15,000 principal + ₹8,550 interest

31st December, 2020 : ₹15,000 principal + ₹8,100 interest

31st March, 2021 : ₹15,000 principal + ₹7,650 interest.

In view of further capital requirement, she transferred ₹2,00,000 from her saving bank account to the bank account of the business. She paid security deposit of ₹7,000 for telephone connection. Furniture of ₹10,000 was purchased, All payments were made by cheque and all receipts in cash were deposited in the bank.

At the end of the year, her business showed the following results:

Particulars	Amt. (₹)	Particulars	Amt. (₹)
Total Sales	20,00,000	Total Purchases	17,00,000
Electricity Expenses paid	40,000	Telephone Charges	50,000
Cartage Outwards	60,000	Travelling Expenses	45,000
Entertainment Expenses	5,000	Maintenance Expenses	25,000
Misc. Expenses	15,000	Electricity Expenses Payable	20,000

Other Information:

(i) She withdrew ₹5,000 by cheque each month for her personal expenses.

(ii) Depreciation on building @ 5% p.a. and on furniture @ 10% p.a.

(iii) Closing stock in hand as on 31st March, 2021 : ₹5,50,000

Prepare trading account, profit and loss account for the year ended 31-3-2021 and Balance Sheet as on that date.

^ **Set off / adjustment of Input GST against Output GST**

		Set off against		
Debit Balance		1)	2)	3)
I	Input **IGST**	Output **IGST**	Output CGST	Output SGST
II	Input **CGST**	Output **CGST**	Output IGST	~
III	Input **SGST**	Output **SGST**	Output IGST	~

* **Excess Output GST,** if any, to be paid off

Till it is paid off, it will appear on **Liability side** of Balance Sheet

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* **Excess Input GST**, if any

Excess Input GST, if any, is called as **Input Tax Credit (ITC)**.

ITC is **to be carried forward** & to be shown on the **Asset side** of the Balance Sheet.

It is to be set off against Output GST of next period.

^ **Q. 7 :** Mr. Mohan gives you the following trial balance and some other information :

Trial Balance as on 31st March, 2022

Particulars	₹	₹
Capital		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	1,89,000	
Input CGST	10,000	
Input SGST	10,000	
Output CGST		8,000
Output SGST		8,000
Output IGST		6,000
	18,53,000	**18,53,000**

Other Information:

(i) Closing Inventory was ₹1,80,000;

(ii) Depreciate Furniture @ 10% p.a.

Required : Prepare Trading and Profit and Loss Account for the year ended on 31.3.2022 and Balance Sheet of Mr. Mohan as on that date.

b. Final Accounts of Manufacturing Entities

^ **Introduction**

The manufacturing entities generally prepare a separate **Manufacturing Account**, as a part of Final accounts in addition to Trading Account, Profit and Loss A/c and Balance Sheet.

The objective of preparing Manufacturing Account is to determine **manufacturing costs of finished goods** for assessing the cost effectiveness of manufacturing activities. Manufacturing costs of finished goods are then transferred from the Manufacturing A/c to Trading A/c.

^ **Purpose**

1) It shows the total cost of manufacturing the finished products and sets out in detail, with appropriate classifications, the constituent elements of such cost. It is, therefore, **debited with** the cost of materials, manufacturing wages and expenses incurred directly or indirectly on manufacture.

2) It provides details of factory cost and facilitates **reconciliation** of financial books with cost records and also serves as a basis of **comparison** of manufacturing operations from year to year.

3) The Manufacturing A/c may also be used for various purposes. For example, if the output is carried to the Trading Account at market prices, it discloses the profit or loss on manufacture. Similarly, it may also be used to fix the amount of production linked bonus when such schemes are in force.

^ **Manufacturing Costs**

Particulars	₹
Raw material consumed	xxx
Add : Direct manufacturing wages	xxx
Add : Direct manufacturing expenses	xxx
Add : Indirect manufacturing expenses or **manufacturing overheads**	xxx
Total Manufacturing Costs	**xxx**

* **Raw material consumed**

= Opening stock of raw materials + Purchase of raw material + Expenses on Pur. of R/M - Closing stock of raw material

* If there remains unfinished goods at the beginning &/or end of the accounting period, cost of such unfinished goods i.e. work-in-progress is shown in Manufacturing A/c.

Opening inventory of work-in-progress is posted on the **debit** of Manufacturing Account.

Closing inventory of work-in-progress is posted on the **credit** of Manufacturing Account.

* **Direct Manufacturing Expenses**

Direct manufacturing expenses are costs, other than material or wages, which are incurred for a **specific** product or saleable service.

Examples :

(i) Royalties for using license or technology if based on units produced,

(ii) Hire charge of plant and machinery used on hire, if based on units produced, etc.

When royalty or hire charges are based on units produced, these expenses directly vary with production

* **Indirect Manufacturing Expenses or Overhead Expenses**

These are also called Manufacturing overheads or Production overheads or Works overheads.

Overhead = Indirect material + Indirect wages + Indirect expenses.

Indirect material means materials which cannot be linked directly with the units produced, for example, stores consumed for repair and maintenance work, small tools, fuel and lubricating oil, etc.

Indirect wages are those which cannot be directly linked to the units produced, for example, wages for maintenance works, holding pay, etc.

Indirect expenses are those which cannot be directly linked to the units produced, for example, training expenses, depreciation of plant and machinery, depreciation of factory shed, insurance premium for plant and machinery, factory shed, etc.

^ **By-Products**

In most manufacturing operations, the production of the main product is accompanied by the production of a subsidiary product which has a value, on sale.

The subsidiary product is termed as a by-product because its production is not consciously undertaken but results out of the production of the main product.

It is usually very difficult to ascertain the cost of the product. Moreover, its value usually forms a very small percentage of the main product.

By-product is a secondary product. This is produced from the same raw materials, which are used for producing the main product and without incurring any additional expenses from the same production process in which the main product is produced.

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Examples of by-product are given below :

(i) Molasses is the by-product in sugar manufacturing;

(ii) Butter milk is the by-product of a dairy which produces butter and cheese, etc.

By-products generally have **insignificant value** as compared to the value of main product. They are generally valued at **net realizable value**, if their costs cannot be separately identified. It is often treated, as miscellaneous income but the correct treatment would be to **credit the sale value of the by-product to Manufacturing Account** so as to reduce to that extent, the cost of manufacture of main product.

FORMAT OF A MANUFACTURING ACCOUNT

Dr. Manufacturing Account for the year ended ..... Cr.

Particulars	₹	₹	Particulars	₹	₹
To Opening work-in-progress		xx	By By-products at Net Realisable Value		xx
To Raw Materials Consumed			By Closing work-in-progress		xx
Opening Stock	xx				
Add : Purchases (Net)	xx				
Add : Carriage etc.	xx				
Less : Closing Stock	(xx)	xxx			
To Direct Wages		xxx			
To Direct Expenses		xx	**By Cost of Goods**		
Prime Cost		xxx	**Manufactured**		
To Factory Overheads (indirect manufacturing expenses)		xxx	transferred to Trading A/c		**xxx**
		xxx			**xxx**

Q. 8 : On 31st March, 2022 the Trial Balance of Mr. White were as follows:

Trial Balance as on 31st March, 2022

Particulars	Dr. (₹)	Particulars	Cr. (₹)
Stock on 1st April 2021		Sundry Creditors	15,000
Raw Materials	21,000	Bills Payable	7,500
Work in Progress	9,500	Sale of Scrap	2,500
Finished Goods	15,500	Commission Received	450
Sundry Debtors	24,000	Provision for doubtful debts	1,650
Carriage on Purchases	1,500	Capital Account	1,00,000
Bills Receivable	15,000	Sales	1,67,200
Wages	13,000	Bank Overdraft	8,500
Salaries	10,000		
Telephone, Postage etc.	1,000		
Repairs to Office Furniture	350		
Cash at Bank	17,000		
Office Furniture	10,000		
Repairs to Plant	1,100		
Purchases	85,000		
Plant and Machinery	70,000		
Rent	6,000		
Lighting	1,350		
General Expenses	1,500		
	3,02,800		**3,02,800**

The following additional information is available :

Stocks on 31st March, 2022 were :

Raw Materials ₹16,200

Finished goods ₹18,100

Semi-finished goods ₹7,800

Salaries and wages unpaid for March 2022 were respectively, ₹900 and ₹2,000.

Machinery is to be depreciated by 10% and office furniture by 7.5%.

Provision for doubtful debts is to be maintained @ 1% of sales.

Office premises occupy 1/4 of total area.

Lighting is to be charged as to 2/3 to factory and 1/3 to office.

Prepare the Manufacturing Account, Trading Account, Profit and Loss Account and the Balance Sheet relating to 31st March 2022.

Q. 9 : The following is the trial balance of Mr. Pandit for the year ended 31.03.2022.

Particulars	Dr. (₹)	Particulars	Cr. (₹)
Opening Stock :		Sundry Creditors	50,000
Raw Materials	1,50,000	Purchase Returns	5,000
Finished goods	75,000	Capital	1,00,000
Purchase of Raw Materials	5,00,000	Bills Payable	24,000
Land & Building	1,00,000	Long-Term Loan	2,00,000
Loose tools	30,000	Provision for Bad and	
Plant & Machinery	30,000	Doubtful Debts	2,000
Investments	25,000	Sales	8,50,000
Cash in Hand	20,000	Bank Overdraft	23,000
Cash at Bank	5,000		
Furniture & Fixtures	15,000		
Bills Receivable	15,000		
Sundry Debtors	40,000		
Drawings	20,000		
Salaries	20,000		
Coal and Fuel	15,000		
Factory rent & rates	20,000		
General Expenses	4,000		
Advertisement	5,000		
Sales Return	10,000		
Bad Debts	4,000		
Direct Wages (Factory)	80,000		
Power	30,000		
Interest Paid	7,000		
Discount Allowed	3,000		
Carriage Inwards	15,000		
Carriage Outwards	7,000		
Commission Paid	9,000		
	12,54,000		**12,54,000**

1. Stock of finished goods at the end of the year ₹1,00,000.
2. A provision for doubtful debts is to be created at 5% on Sundry Debtors.
3. Depreciation on building ₹1,000 and ₹3,000 on Plant & Machinery to be provided.
4. Accrued commission of ₹12,500 is to be received for the year.
5. Interest has accrued on investment ₹15,000.
6. Salary Outstanding ₹2,000 and Prepaid Interest ₹1,500.

Prepare Manufacturing, Trading and Profit and Loss Account for the year ended 31.03.2022

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^	**Try Yourself : Objectives**
*	**State True or False with reasons :**
1	The income statement shows either net profit or net loss for a particular period.
2	Gains from the sale or exchange of assets are not considered as the revenue of the the business.
3	The salary paid in advance is not an expense because it neither reduces assets or nor increase liabilities.
4	A loss is an expenditure which does not bring any benefit to the concern.
5	All liabilities which become due for payment within the year are classified as long-term liabilities.
6	The term current asset is used to designate cash and other assets or resources which are reasonably expected to be realized or sold or consumed within one year.
7	An asset gives rise to expenditure when it is acquired and to an expense when it is consumed.
8	If the balance of an account on the debit side of the trial balance where the benefit has already expired then it is treated as an expense.
9	Sales less cost of goods sold = gross profit.
10	If the debit side of the trading account exceeds its credit side then the balance is termed as gross profit.
11	The provision for bad debts is debited to Sundry Debtors Account.
12	The provision for discount on creditors is often not provided in keeping with the principle of conservatism.
13	The debts written off as bad, if recovered subsequently are credited to Debtors Account.
14	The adjustment entry in respect of income received in advance is debit Income received in advance account and credit income account.
15	Premium paid on the life policy of a proprietor is debited to profit and loss account.
16	Depreciation account appear in the trial balance is taken only to profit and loss account.
17	Personal purchases included in the purchases day book are added to the sales account in the Trading account.
18	Medicines given to the office staff by a manufacturer of medicines will be debited to salaries account.
19	Goods worth 600 taken by the proprietor for personal use should be credited to Capital Account.
20	If closing stock appears in the trial balance, the closing inventory is then not entered in Trading Account. It is only shown in the Balance Sheet.
21	By-products valued at cost or net realisable value whichever is lower.
22	The manufacturing account is prepared to ascertain the profit or loss on the goods produced.

23	Raw Material Consumed = Opening inventory of Raw Materials + Purchases – Closing inventory of Raw Materials.
24	If there remain unfinished goods at the beginning and at the end of the accounting period, cost of such unfinished goods is shown in the Manufacturing Account.
25	The Trading Account will show the quantities of finished goods, raw materials and work-in-progress.
26	Overhead is defined as total cost of direct material, direct wages and direct expenses.
27	Manufacturing A/c is prepared by an enterprise engaged in trading activities.
28	A withdrawal of cash from the business by the proprietor should be charged to profit and loss account as an expense.
29	Stock at the end, if appears in the Trial Balance, is taken only to the Balance Sheet.
30	"Salary paid in advance" is not an expense because it neither reduces assets nor increases liabilities.
31	The results and position disclosed by final accounts are not exact.
32	The value of human resources is generally shown as assets in the Balance Sheet.
33	All the personal & real accounts are recorded in P&L A/c.
34	When closing inventory is overstated, net income for the accounting period will be understated.
35	Sale of office furniture should be credited to Profit and Loss Account.
36	Depreciation is a non-cash expense and does not result in any cash outflow.
37	The sale value of by-product is credited to Trading Account.
38	The provision for bad debts is debited to sundry debtors account.
	Answers :
1	**True**
	Profit and loss account shows either net profit or net loss for a particular period.
2	**False**
	Gains from the sale or exchange of assets are considered as the revenue of the business. But this revenue not in the ordinary course of business so it is capital receipts.
3	**True**
	The salary paid in advance is an asset it is not an expense because it neither reduces assets or nor increase liabilities.
4	**True**
	A loss is an expenditure of the business which does not bring any gain to the business.

5	**False**
	All liabilities which become due for payment within one year are classified as current liabilities.
6	**True**
	Current assets are all the assets which are expected to be realized or sold or consumed within one year.
7	**True**
	When an asset is purchase capital expenditure is incurred and when the asset is put to use expenses are incurred in consumption.
8	**True**
	Debit balance of accounts are treated as expenses whose benefit is already received or expired.
9	**True**
	Gross profit is obtained by deducting cost of goods sold from sales.
10	**False**
	If the debit side of the trading account exceeds its credit side then the balance is termed as gross loss.
11	**False**
	The provision for bad debts is debited to debited to Profit and loss Account, in Balance Sheet it is shown either on liability side or deducted from the head Debtors.
12	**True**
	According to the provision of conservatism provision is maintained for the losses to be incurred in future. Discount on creditors is an income so provision in not maintained.
13	**False**
	The debts written off as bad, if recovered subsequently are credited to Bad Debts Recovered Account and becomes an income.
14	**False**
	Income received in advance is reduced from the concerned income in profit and loss account & it is shown as a liability in balance sheet under the head Current Liabilities

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15	**False**
	Premium paid on the life policy of a proprietor is to be debited to capital account, as it is personal expense.
16	**True**
	Depreciation is charge on each of the asset on a certain percentage. Depreciation is a charge to profit and loss account and should be debited to profit & loss account by crediting the respective assets. If it appears in trial balance then it is taken only to profit and loss account.
17	**False**
	Personal purchases included in the purchases day book are deducted from the purchases account in the Trading account.
18	**True**
	Any benefit given to the staff is debited to the salary account.
19	**False**
	Goods taken by the proprietor for personal use should be credited to Purchase Account as less goods are left in the business for sale.
20	**True**
	The closing Stock appears in the trial balance only when it is adjusted against purchases by passing the entry. In this case, closing stock is not entered in Trading Account and is shown only in Balance Sheet.
21	**False**
	By-products generally have insignificant value as compared to the value of main product. Therefore, they are generally valued at net realisable value.
22	**False**
	The objective of preparing Manufacturing Account is to determine manufacturing costs of finished goods for assessing the cost effectiveness of manufacturing activities.
23	**True**
	Raw Material consumed is arrived at after adjustment of opening and closing inventory of raw materials and purchases.

24	**True**
	Manufacturing account deals with the raw material and work in progress.
25	**False**
	The Trading Account will show the quantities of finished goods manufactured and sold and the opening and closing inventory. It will not show the quantity of raw materials or work-in-progress.
26	**False**
	Overhead is defined as total cost of indirect material, indirect wages and indirect expenses.
27	**False**
	Manufacturing A/c is prepared by the entities engaged in manufacturing activities.
28	**False**
	Cash withdrawal by the proprietor from his business should be treated as his drawings and not a business expense chargeable to profit and loss account. Such drawings should be deducted from the proprietors capital.
29	**True**
	Because it depicts that one aspect of the double entry has been completed.
30	**True**
	Salary paid in advance relates to the coming accounting period. It has nothing to do with the current period. Hence it is not taken in the Profit and Loss Account as an expense. It is shown as a Current Asset in the Balance Sheet.
31	**True**
	They are prepared on the basis of assumptions, conventions, concepts and p ersonal judgements of the person who prepare them.
32	**False**
	The value of human resources cannot be measured in monetary terms, thus it will not be shown in the balance sheet.
33	**False**
	All the personal & real account are recorded in balance sheet.

34	**False**
	When closing inventory is overstated, net income for the accounting period will be overstated.
35	**False**
	Sale of office furniture should be credited to Furniture account since it is a capital receipt.
36	**True**
	Depreciation is a non-cash expense and unlike other normal expenditure (e.g. wages, rent, etc.) does not result in any cash outflow. Therefore depreciation is a non-cash expense and does not result in any cash outflow.
37	**False**
	The sale value of the by-product is credited to Manufacturing Account so as to reduce to that extent, the cost of manufacture of main product.
38	**False**
	The provision for bad debts is debited to Profit and loss Account, in Balance Sheet it is shown either on liability side or deducted from the head debtors.
*	**Multiple Choice Questions :**
1	A debit to an account may
	(a) increase expense (b) decrease an asset. (c) increase a liability.
2	Prepayment of insurance premium will appear in the Balance Sheet and in the Insurance Account respectively as:
	(a) a liability and a debit balance.
	(b) an asset and a debit balance.
	(c) an asset and a credit balance.
3	Gross profit is the difference between:
	(a) sales and purchases (b) sales and cost of sales. (c) sales and total expenses.
4	Payment made to a creditor subject to cash discount will :
	(a) reduce a liability, reduce an asset and add to expenses.
	(b) reduce a liability, add to an asset, and add to revenue.
	(c) reduce an asset, reduce a liability, and add to revenue.

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5	A customer returns goods already charged to him. We should: (a) debit his account. (b) credit his account. (c) make no entry on his account.
6	Capital is the difference between (a) Income and expenses (b) Sales and Cost of goods sold (c) Assets and liabilities
7	The capital of a sole trader would change as a result of: (a) A creditor being paid his account by cheque. (b) Raw materials being purchased on credit. (c) Wages being paid in cash.
8	A decrease in the provision for doubtful debts would result in: (a) An increase in liabilities. (b) A decrease in working capital. (c) An increase in net profit.
9	A Company wishes to earn a 20% profit margin on selling price. Which of the following is the profit mark up on cost, which will achieve the required profit margin? (a) 33% (b) 25% (c) 20%
10	If sales is ₹2,000 and the rate of gross profit on cost of goods sold is 25%, then the cost of goods sold will be (a) ₹2,000. (b) ₹1,500. (c) ₹1,600.
11	Sales for the year ended 31st March, 2022 amounted to ₹10,00,000. Sales included goods sold to Mr. A for ₹50,000 at a profit of 20% on cost. Such goods are still lying in the godown at the buyer's risk. Therefore, such goods should be treated as part of (a) Sales. (b) Closing Inventory. (c) Goods in transit.
12	If sales revenues are ₹4,00,000; cost of goods sold is ₹3,10,000 and expenses are ₹ 60,000, the gross profit is (a) ₹30,000. (b) ₹90,000. (c) ₹3,40,000.
13	Under-statement of closing work in progress in the period will (a) Understate cost of goods manufactured in that period. (b) Overstate current assets. (c) Understate net income in that period. (d) None of the three.

14 Sales is equal to

(a) Cost of goods sold – Gross profit.

(b) Cost of goods sold + Gross profit.

(c) Gross profit – Cost of goods sold.

15 Indirect Manufacturing expenses are also called

(a) Manufacturing overhead. (b) Production overhead.

(c) Works overhead. (d) All the three.

16 Sale value of the by-product is credited to

(a) Manufacturing account. (b) Capital account.

(c) Overheads account. (d) Trading account.

17 Manufacturing account shows

(a) Total cost of manufacturing the finished products.

(b) It provides details of factory cost.

(c) It facilitates reconciliation of financial books with cost records.

(d) All the three.

Answers :

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

* **Theoretical Questions**

1 Write shorts notes on:

(a) Balance sheet.

(b) Trading account

(c) Closing entries

2 Distinguish between Provision and reserve fund.

3 Write short note on by-products.

4 Differentiate between Direct Manufacturing Expenses and Indirect Manufacturing expenses.

Answers :

1 (a) The balance sheet may be defined as "a statement which sets out the assets and liabilities of a firm or an institution as at a certain date." Since even a single transaction will make a difference to some of the assets or liabilities, the balance sheet is true only at a particular point of time. That is the significance of the word "as at."

(b) At the end of the year, it is necessary to ascertain the net profit or the net loss. For this purpose, it is first necessary to know the gross profit or gross loss with the helps to Trading A/c. Gross Profit is the difference between the selling price and the cost of the goods sold.

(c) Closing entries: The entries that have to be made in the journal for preparing the Trading and the Profit and Loss Account that is for transferring the various accounts to these two accounts are known as closing entries.

2 Provision means "any amount written off or retained by way of providing for depreciation, renewal or diminution in the value of assets or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy".

Reserve Fund: It signifies the amount standing to the credit of the reserve that is invested outside the business in securities which are readily realisable e.g., when the amounts set apart for replacement of an asset are invested periodically, in government securities or shares. The account to which these amounts are annually credited is described as the Reserve Fund.

3 By-products generally have insignificant value as compared to the value of main product. They are **generally valued at net realisable value**, if their costs cannot be separately identified. It is often treated, as "Miscellaneous income" but the correct treatment would be to credit the sale value of the by-product to Manufacturing Account so as to reduce to that extent, the cost of manufacture of main product.

4 **Direct manufacturing expenses** are costs, other than material or wages, which are incurred for a specific product or saleable service.

Indirect Manufacturing expenses are also called Manufacturing overhead, Production overhead, Works overhead, etc. Overhead is defined as total cost of indirect material, indirect wages and indirect expenses.

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TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
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SOHAM SHAH
307



GAURANG SHAH
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NEMIL SATUNDA
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ESAKKIMUTHU DAS
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SHASHI PALOD
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ALVITA KHAN
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SORABH MOHATA
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SANA DESHPANDE
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MEETALI MAHESHWARI
300

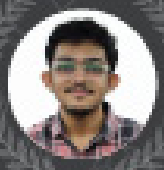
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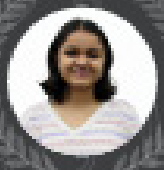
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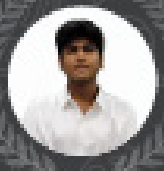
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SCAN ME!

^ Introduction

In all the chapters studied, we have discussed how to prepare Books of Accounts following the Double Entry System (DES) of accounting.

Accounting records which are **not prepared** in accordance with the DES are known as **Incomplete Records.**

In other words, any accounting records which falls short of DES (i.e. under which both the aspects of each & every transaction is not recorded) are called Incomplete records.

Sometimes, it is termed as **Single Entry System** (SES) of accounting.

It should be noted that there are **no set rules** to be followed under SES of accounting, even books of accounts to be maintained are **not certain**.

It can simply be termed as **absence of DES** of accounting.

* Features of Single Entry System

1. It is an inaccurate, unscientific & unsystematic system of recording business transactions.
2. There is generally no record of real and nominal Accounts.
   It is either **Pure SES** in which only Personal A/c's are maintained
   or **Simple SES** in which Personal A/c's & Cash Book are maintained
   or **Quasi SES** in which Personal A/c's, Cash Book & Subsidiary Books are maintained
3. Cash Book mixes up business and personal transactions of the owners
4. There is no uniformity in maintaining the records and system differs from firm to firm, depending upon the requirement and convenience of each firm.
5. Profitability & Financial Position under this system is only an estimate based.

II. Ascertainment of Profit from Incomplete records

Despite the records being incomplete, the business owner would like to know profits earned or loss incurred at periodic intervals, generally a year.

Also, he would like to know financial position at the end of the period.

Final A/c's **cannot be prepared in the usual manner** , since all the required information is not available.

In such a situation, there are **two methods** used for ascertaining profits of the business.

1. Statement of Affairs Method **or** Net Worth Method **or** Capitals Comparision Method

2. Conversion Method (Conversion **of** Single Entry **into** Double Entry)

^ Statement of Affairs Method or Net Worth Method

Closing Capital = Opening Capital + Capital Introduced - Drawings + Profit

Hence, Profit = Closing Capital + Drawings - Opening Capital - Capital Introduced

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Q. 1 : Assets and Liabilities of Mr. X as on 31-03-2021 and 31-03-2022 are as follows:

Particulars	31-03-2021	31-03-2022
	(₹)	(₹)
Assets		
Building	1,00,000	?
Furniture	50,000	?
Inventory	1,20,000	2,70,000
Sundry debtors	40,000	90,000
Cash at bank	70,000	85,000
Cash in hand	1,200	3,200
Liabilities		
Loans	1,00,000	80,000
Sundry creditors	40,000	70,000

Decided to depreciate Building by 2.5%p.a. and Furniture by 10% p.a. One Life Insurance Policy of the Proprietor was matured during the period and the amount 40,000 is retained in the business. Proprietor took @ 2,000 p.m. for meeting family expenses. Prepare S.O.A. as on 31-03-2021 & 31-03-2022 and also find out profit.

Q. 2 : The Income Tax Officer, on assessing the income of Shri Moti for the financial years 2020-2021 and 2021-2022 feels that Shri Moti has not disclosed the full income. He gives you the following particulars of assets and liabilities of Shri Moti as on 1st April, 2020 and 1st April, 2022.

			₹
01-04-2020	**Assets:**	Cash in hand	25,500
		Inventory	56,000
		Sundry debtors	41,500
		Land and Building	1,90,000
		Wife's Jewellery	75,000
	Liabilities:	Owing to Moti's Brother	40,000
		Sundry creditors	35,000
01-04-2022	**Assets:**	Cash in hand	16,000
		Inventory	91,500
		Sundry debtors	52,500
		Land and Building	1,90,000
		Motor Car	1,25,000
		Wife's Jewellery	1,25,000
		Loan to Moti's Brother	20,000
	Liabilities:	Sundry creditors	55,000

During the two years the domestic expenditure was ₹4,000 p.m. The declared incomes of the financial years were ₹1,05,000 for 2020-2021 and ₹1,23,000 for 2021-2022 respectively. State whether the Income-tax Officer's contention is correct. Explain by giving your workings.

^ **Q. 3 :** Raju does not maintain his book of accounts under the Double Entry System, but keeps slips of papers from which he makes up his annual accounts. He has borrowed moneys from a Bank to whom he has to render figures of profits every year. He has given the Bank the following profit figures -

Year ending 31st Dec.	2019	2020	2021	2022	2023
Profit in (₹)	20,000	32,000	35,000	48,000	55,000

The Bank appoints you to audit the statements and verify whether the figures of profits reported are correct or not. For this purpose the following figures are made available to you:

(a) Position as on 31.12.2018 : Sundry Debtors ₹20,000,
Stock in Trade (at 95% of Cost) ₹47,500, Cash on Hand and at Bank ₹12,600,
Trade Creditors ₹6,000, Expenses Due - ₹1,600.

(b) He had borrowed ₹5,000 from his wife on 30.9.2018 on which he had agreed to pay simple interest at 12% p.a. The loan was repaid along with interest on 31.3.2020.

(c) In December 2019, he had advanced ₹8,000 to Raghav for purchase of a vacant land. The property was registered in March 2021 after payment of balance consideration of ₹32,000. Cost of registration incurred for this were ₹7,500.

(d) Raju purchased jewellery for ₹15,000 for his daughter in October 2021. Marriage expenses incurred in January 2022 were ₹24,000.

(e) A new DVD Player was purchased by him in March 2022 for ₹18,000 & presented by him to his friend in November 2023.

(f) His annual household expenses amounted to a minimum of ₹ 24,000.

(g) The position of Assets and Liabilities as on 31.12.2023 was found to be :
Overdraft with Bank (Secured against property) ₹12,000
Trade Creditors ₹10,000, Expenses payable ₹600
Sundry Debtors ₹28,800 (including ₹600 due from a person declared insolvent)
Stock in Trade (at 125% of cost to reflect market value) ₹60,000,
Cash-in-Hand - ₹250.

(h) It is found that the rate of profit has been uniform throughout the period and the proportion of sales during the years to total sales for the period was in the ratio of 3 : 4 : 4 : 6 : 8.

Ascertain the annual profits and indicate differences, if any, with those reported by Raju to the Bank earlier. All workings are to form part of your answer.

^ **Conversion Method**

This method can be followed when, though complete DES is not followed, substantial information / records are available / kept, such that missing informations / transactions can be found out as a **Balancing Figure** by preparing relevant accounts, thereby **converting it** into DES of accounting.

Final Accounts consists of :

1) Trading A/c for the year ended…….
2) Profit & Loss A/c for the year ended……
3) Balance Sheet as on ……

In addition,
one or more of the following **may be** required be prepared **to get missing figures**

1) **(Opening) Balance Sheet at the start of the year**
(To get opening capital or cash / bank or any other opening balance)

2) **Cash & Bank A/c** or **Columner Cash Book : separate column for Cash & Bank**
(To get closing balance or cash sales or collection from debtors
or payment to creditors or any other missing information)

3) Total Debtors A/c
4) Total Creditors A/c
5) Bills Receivable A/c
6) Bills Payable A/c **etc.**

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^ **Total Debtors A/c**

Particulars	₹	Particulars	₹
To Balance b/d	**xxx**		
(Opening Dr. Balance)			
To Sales A/c	**xxx**	**By Sales Returns A/c**	**xxx**
(Credit Sales)		(Returns Inward)	
To Bank A/c	**xxx**	**By Cash / Bank A/c**	**xxx**
(dishonour of cheque)		(Collection from Debtors)	
To (dishonour of B/R) A/c	**xxx**	**By Bills Receivable A/c**	**xxx**
(with noting charges)		(acceptances received)	
To Cash / Bank A/c	**xxx**	**By Discount Allowed A/c**	**xxx**
(Expense paid / charged)		(for receipt before due date)	
		By Baddebts A/c	**xxx**
		(on insolvency / otherwise)	
		By Balance c/d	**xxx**
		(Closing Dr. Balance)	
	XXXX		**XXXX**

* Above A/c is prepared **to find out** Credit Sales / Collection / Closing balance **or** any other missing figure

^ **Total Creditors A/c**

Particulars	₹	Particulars	₹
		By Balance b/d	**xxx**
		(Opening Cr. Balance)	
To Purchase Returns A/c	**xxx**	**By Purchases A/c**	**xxx**
(Returned Outward)		(Credit Purchases)	
To Cash / Bank A/c	**xxx**	**By Bank A/c**	**xxx**
(Payment to Creditors)		(Cheque issued dishonoured)	
To Bills Payable A/c	**xxx**	**By Bills Payable A/c**	**xxx**
(acceptances given)		(Dishonour)	
To Discount Received A/c	**xxx**	**By Expense A/c**	**xxx**
(for payment before due date)		(charged / paid on our behalf)	
To Bills Receivable A/c		**By Debtors A/c**	**xxx**
(B/R endorsed)		(Endorsed B/R dishonoured)	
To Balance c/d	**xxx**		
(Closing Cr. Balance)			
	XXXX		**XXXX**

* Above A/c is prepared **to find out** Credit Purchases / Payment / Closing balance **or** any other missing figure

^ **Bills Receivable A/c**

Particulars	₹	Particulars	₹
To Balance b/d	**xxx**	**By Cash / Bank A/c**	**xxx**
(Opening Dr. Balance)		(Honour / Retirement of B/R)	
To Total Debtors A/c	**xxx**	**By Rebate A/c**	**xxx**
(acceptances received)		(on retirement of bill)	
		By Bank A/c	**xxx**
		By Discount A/c	**xxx**
		(Bills discounted)	
		By Total Creditors A/c	**xxx**
		(Bills endorsed)	
		By Bill sent for Collection A/c	**xxx**
		(Bills sent for B.F.C.)	
		By Total Debtors A/c	**xxx**
		(Retained bill dishonoured)	
		By Balance c/d	**xxx**
		(Closing Dr. Balance)	
	XXXX		**XXXX**

* Above A/c is prepared **to find out** acceptances received / closing balance **or** any other missing figure

^ **Bills Payable A/c**

Particulars	₹	Particulars	₹
To Cash / Bank A/c	**xxx**	**By Balance b/d**	**xxx**
(Honour / Retirement)		(Opening Cr. Balance)	
To Rebate A/c	**xxx**	**By Total Creditors A/c**	**xxx**
(on retirement of bill)		(acceptances given)	
To Total Creditors A/c	**xxx**		
(Dishonour)			
To Balance c/d	**xxx**		
(Closing Cr. Balance)			
	XXXX		**XXXX**

* Above A/c is prepared **to find out** acceptances given / closing balance **or** any other missing figure

Q. 4 : Ram carried on business as retail merchant. He has not maintained regular account books. However, he always maintained ₹ 10,000 in cash and deposited the balance into the bank account. He informs you that he has sold goods at profit of 25% on sales.

Following information is given to you :

Assets and Liabilities	As on 1.4.2021	As on 31.3.2022
Cash in Hand	10,000	10,000
Sundry Creditors	40,000	90,000
Cash at Bank	50,000 (Cr.)	80,000 (Dr.)
Sundry Debtors	1,00,000	3,50,000
Stock in Trade	2,80,000	?
Ram's capital	3,00,000	?

Analysis of his bank pass book reveals the following information:

(a) Payment to creditors ₹7,00,000

(b) Payment for business expenses ₹ 1,20,000

(c) Receipts from debtors ₹7,50,000

(d) Loan ₹ 1,00,000 taken on 1.10.2021 at 10% per annum

(e) Cash deposited in the bank 1,00,000

He informs you that he paid creditors for goods ₹ 20,000 in cash and salaries ₹ 40,000 in cash. He has drawn ₹ 80,000 in cash for personal expenses. During the year Ram had not introduced any additional capital. Surplus cash if any, to be taken as cash sales. All purchases are on credit basis.

You are required to prepare Trading and Profit and Loss Account for the year ended 31.3.2022 and Balance Sheet as at 31st March, 2022.

Q. 5 : Mr. A runs a business of readymade garments. He closes the books of accounts on 31st March. The Balance Sheet as on 31st March, 2021 was as follows:

Liabilities	(₹)	Payments	(₹)
A's capital a/c	4,04,000	Furniture	40,000
Creditors	82,000	Stock	2,80,000
		Debtors	1,00,000
		Cash in hand	28,000
		Cash at bank	38,000
	4,86,000		**4,86,000**

You are furnished with the following information :

(1) His sales, for the year ended 31st March, 2022 were 20% higher than the sales of previous year, out of which 20% sales was cash sales.
Total sales during the year 2020-21 were ₹ 5,00,000.

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(2) Payments for all the purchases were made by cheques only.
(3) Goods were sold for cash and credit both. Credit customers pay by cheques only.
(4) Deprecation on furniture is to be charged 10% p.a.
(5) Mr. A sent to the bank the collection of the month at the last date of the each month after paying salary of ₹ 2,000 to the clerk, office expenses ₹ 1,200 and personal expenses ₹ 500.

Analysis of bank pass book for the year ending 31st March 2022 disclosed the following

	(₹)
Payment to creditors	3,00,000
Payment of rent up to 31st March, 2022	16,000
Cash deposited into the bank during the year	80,000

The following are the balances on 31st March, 2022 :

	(₹)
Stock	1,60,000
Debtors	1,20,000
Creditors for goods	1,46,000

On the evening of 31st March 2022, the cashier absconded with the available cash in the cash book.

You are required to prepare Trading and Profit and Loss A/c for the year ended 31st March, 2022 and Balance Sheet as on that date. All the workings should form part of the answer.

^ **Q. 6 :** Mr. Anup runs a wholesale business where in all purchases and sales are made on credit. He furnishes the following closing balances:

	31st March 2021	31st March 2022
Sundry Debtors	70,000	92,000
Bills Receivable	15,000	6,000
Bills Payable	12,000	14,000
Sundry Creditors	40,000	56,000
Inventory	1,10,000	1,90,000
Bank	90,000	87,000
Cash	5,200	5,300

Summary of cash transactions during the year 2021-2022 :

(i) Deposited to bank after payment of shop expenses @ ₹600 p.m., salary @ ₹9,200 p.m. and personal expenses @1,400 p.m. ₹7,62,750.
(ii) Cash withdrawn from bank ₹1,21,000.
(iii) Cash payment to suppliers ₹77,200 for supplies and ₹25,000 for furniture.

(iv) Cheques collected from customers but dishonoured ₹5,700.
(v) Bills accepted by customers ₹40,000.
(vi) Bills endorsed ₹10,000.
(vii) Bills discounted ₹20,000, discount ₹750.
(viii) Bills matured and duly collected ₹16,000.
(ix) Bills accepted ₹24,000.
(x) Paid suppliers by cheque ₹3,20,000.
(xi) Received ₹20,000 on maturity of one LIC policy of the proprietor by cheque.
(xii) Rent received ₹14,000 by cheque for the premises owned by proprietor.
(xiii) A building was purchased on 30-11-2021 for opening a branch for ₹3,50,000 and some expenses were incurred on this building, details of which are not maintained.
(xiv) Electricity and telephone bills paid by cash ₹18,700, due ₹2,200.

Other transactions :

(i) Claim against the firm for damage ₹1,55,000 is under legal dispute. Legal expenses ₹17,000. The firm anticipates defeat in the suit.
(ii) Goods returned to suppliers ₹4,200.
(iii) Goods returned by customers ₹1,200.
(iv) Discount offered by suppliers ₹2,700.
(v) Discount offered to the customers ₹2,400.
(vi) The business is carried on at the rented premises for an annual rent of ₹20,000 which is outstanding at the year end.

Prepare Trading and Profit & Loss Account of Mr. Anup for the year ended 31st March 2022 and Balance Sheet as on that date.

^ **Q. 7 :** 'A' and 'B' are in partnership, sharing profits and losses equally. They keep their books by Single Entry System. The following balances are available from their books :

Particulars	Opening (₹)	Closing (₹)
Building	1,50,000	1,50,000
Equipments	2,40,000	2,72,000
Furniture	25,000	25,000
Debtors	?	1,00,000
Creditors	65,000	?
Stock	?	70,000
Bank Loan	45,000	35,000
Bills Payable	60,000	?

The transactions during the year were the following :

Particulars	(₹)
Collection from Debtors	3,80,000
Payment to Creditors	2,50,000
Cash Purchases	65,000
Expenses paid	40,000
Drawings by 'A'	30,000

1. On 1st April, an Equipment of book value ₹20,000 was sold for ₹15,000. On 1st October, some more extra equipments were purchased.
2. Cash Sales amounted to 10% of Sales.
3. Credit Sales amounted to ₹ 4,50,000.
4. Credit Purchases were 80% of Total Purchases.
5. The Firm sells goods at cost plus 25%.
6. Discount Allowed ₹5,500 during the year.
7. Discount Earned ₹4,800 during the year.
8. Outstanding Expenses ₹3,000 as at year end.
9. Capital of 'A' as at the beginning of the year was ₹15,000 more than the Capital of 'B',
10. Equipments and Furniture to be depreciated at 10% p.a. and Building at 2% p.a.

Prepare the Trading and Profit and Loss Account for the year ended 31st March and a Balance Sheet as on that date.

Q. 8 : The following is the Balance Sheet of M/s Care Traders as on 1st April -

Sources of Funds	Amt. (₹)	Application of Funds	Amt. (₹)
Share Capital	10,00,000	Machinery	8,25,500
Profit and Loss	1,47,800	Furniture	1,28,700
Unsecured Loan at 10%	1,75,000	Inventory	1,72,000
Trade Payables	45,800	Trade receivables	2,29,600
		Bank balance	12,800
	13,68,600		**13,68,600**

A fire broke out in the premises on 31st March and destroyed the books of accounts. The Accountant could however provide the following information :

1. Sales for the year was ₹18,60,000. Sales for the current year was 20% higher than the last year.
2. 25% sales were made in cash and the balance was on credit.
3. Gross Profit on sales is 30%.
4. Terms of Credit : Debtors - 2 Months, Creditors - 1 month. All creditors are paid by cheque & sales are collected in cheque.

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5. The Bank Pass Book has the following details (other than payment to Creditors and collection from Debtors)

Machinery purchased	1,14,000
Rent paid	1,32,000
Advertisement expenses	80,000
Travelling expenses	78,400
Repairs	36,500
Sales of Furniture	9,500
Cash withdrawn for petty expenses	28,300
Interest paid on Unsecured Loan	8,750

6. Machinery was purchased on 1st October.
7. Rent was paid for 11 months only and 25% of the advertisement expenses relates to the next year.
8. Travelling expenses of ₹7,800 for which cheques were issued but not presented in bank.
9. Furniture was sold on 1st April at a loss of ₹2,900 on book value.
10. Physical Verification as on 31st March ascertained the stock position at ₹1,81,000 and Petty Cash Balance at Nil.
11. There was no change in Unsecured Loans during the year.
12. Depreciation is to be provided at 10% on Machinery and 20% on Furniture.

Prepare Bank A/c, Trading and Profit & Loss A/c for the year, in the books of M/s. Care Traders & a Balance Sheet as on that date. Make assumptions wherever necessary.

^ **Try Yourself : Objectives**

* **State True or False with reasons :**

1 A Trial Balance cannot be drawn up from books kept under Single Entry.

2 Nominal Accounts are kept under Single Entry System.

3 Single Entry System can be adopted by small firms.

4 Profit under single entry system is always correct and accurate.

5 Profits computed under single entry system by different business entities are not comparable.

Answers :

1 **True**

Since incomplete records are maintained, trial balance cannot be prepared.

2 **False**

Under the single entry system of bookkeeping, generally cash book and personal accounts of creditors and debtors are maintained, and no other ledger is maintained.

3	**True**
	A single entry system is the one where financial transactions are recorded as a single entry in a log and is usually used by new small businesses.
4	**False**
	Profit under single entry system is only an estimate based on available information and correct profits cannot be determined.
5	**True**
	Since entry system has no fixed set of principles for recording the financial transaction, different organisations maintain records as per their needs. Hence their accounts are not comparable.
*	**Multiple Choice Questions**
1	In case of net worth method, profit is determined by
	(a) Preparing a trading and profit and loss account.
	(b) Comparing the capital in the beginning with the capital at the end of the accounting perio
	(c) Comparing the net assets in the beginning with the net assets at the end of the accounting period.
2	Single entry system can be followed by
	(a) Small firms. (b) Joint stock companies. (c) Co-operative societies.
3	Closing capital is calculated as
	(a) Opening capital + Additional capital – Drawings.
	(b) Opening capital + Additional capital – Drawings + Profit.
	(c) Opening capital + Additional capital + Drawings – Profit.
4	Under single entry system, only personal accounts are kept and, in some cases,
	(a) Cash book is maintained
	(b) Fixed assets' accounts are maintained
	(c) Liabilities' accounts are maintained.
5	The closing capital of Mr. B as on 31.3.2022 was ₹4,00,000. On 1.4.2021 his capital was ₹3,50,000. His net profit for the year ended 31.3.2022 was ₹1,00,000. He introduced ₹30,000 as additional capital in February, 2022 Find out the amount drawn by Mr. B for his domestic expenses.
	(a) 1,00,000 (b) 80,000;. (c) 1,20,000;

6	Given information:	
	Opening capital:	₹60,000
	Drawings:	₹5,000
	Capital introduced during the period: 10,000 Closing capital:	₹90,000
	Profit earned during the period	?
	(a) ₹20,000 (b) ₹25,000;. (c) ₹30,000;	

Answers :

1	(b)		**2**	(a)		**3**	(b)		**4**	(a)		**5**	(b)		**6**	(b)	

^ **Theoretical Questions**

1 What is meant by Single entry System? What are the types of procedures adopted for this system?

2 Differentiate between Statement of Affairs and Balance Sheet.

Answers :

1 Single entry system is an inaccurate and unsystematic method of recording business transactions. The procedures adopted are : Pure single entry; Simple entry and Quasi single entry.

(i) **Pure single entry** : In this, only personal accounts are maintained with the result that no information is available in respect of cash and bank balances, sales and purchases, etc. In view of its failure to provide even the basic information regarding cash etc., this method exists only on paper and has no practical application.

(ii) **Simple single entry** : In this, only: (a) personal accounts, and (b) cash book are maintained. Although these accounts are kept on the basis of double entry system, postings from cash book are made only to personal accounts with no other account to be found in the ledger. Cash received from debtors or cash paid to creditors is simply noted on the bills issued or received as the case may be.

For example, M/s Small shop runs a retail shop. It keeps a register of amount receivable from people for items sold (bread, butter, milk etc). as under:

Mr. A – ₹300 Mr. B – ₹450 Mr. C – ₹260.

The business does not maintain a record of what item has been sold. It is only concerned about the amount receivable (personal account balance) from its customers.

(iii) **Quasi single entry** : In this: (a) personal accounts, (b) cash book, and (c) some subsidiary books are maintained. The main subsidiary books kept under this system are Sales book, Purchases book and Bills book. No separate record is maintained for discounts, which are entered into the personal accounts. In addition, some scattered information is also available in respect of few important items of expenses

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like wages, rent, rates, etc. In fact, this is the method which is generally adopted as a substitute for double entry system.

Some businesses may also maintain additional records like Bills book or Sales book. This might be required for tax or other purposes. For example, a shop selling t-shirts may want to issue a bill to each customer for the sales made to them. This will help them validate any returns of goods within reasonable time. In addition, they may keep a purchase book to record all purchases.

Also, organisations employing workers keep records of cash wages paid and take acceptance from the workers for the amount paid to them.

2 Difference between Statement of Affairs and Balance Sheet

Basis	Statement of affairs	Balance sheet
Source	It is prepared on the basis of transactions partly recorded under the double entry book keeping and partly under the single entry. Most of the assets are recorded based on the estimates, assumptions, information gathered from memory rather from the records.	It is based on transactions recorded strictly on the basis of double entry book keeping; each item in the balance sheet can be verified from the relevant subsidiary books, ledger and documentary evidences.
Capital	In this statement, capital is merely a balancing figure being excess of assets over liabilities. Hence assets need not be equal to liabilities.	Capital is derived from the capital account in the ledger and therefore the total of assets side will always be equal to the total of liabilities side.
Omission	Since this statement is prepared from incomplete records, it is very difficult, to identify and record those assets and liabilities, if omitted from the books.	There is no possibility of omission of any item of asset and liability since all items are properly recorded. Moreover, it is easy to locate the missing items since the balance sheet will not agree.
Basis of Valuation	The valuation of assets is generally done in an arbitrary manner; therefore, no method of valuation is disclosed.	The valuation of assets is done on scientific basis, fixed assets are shown at the original costs less depreciation till date. Any change in the method of valuation is properly disclosed.
Objective	The objective of preparing this statement is to identify the capital figures in the beginning and at the end of the accounting period respectively.	The objective of preparing the balance sheet is to ascertain the financial position on a particular date.

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Dec'23



357/400

BHAVIK DOSHI



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

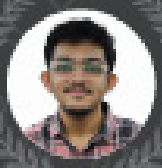
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340/400

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CA Foundation June'23
331



NISHIT KAPUR
CA Foundation June'23
328



PALAK JAJODIA
CA Foundation June'23
325



SWASTIKA SINGH
CA Foundation June'22
323



SUKUNJ GUPTA
CA Foundation June'22
323



DURGASHRI VS
CA Foundation June'22
319



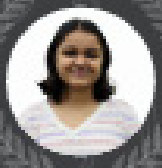
VARUN ADWANI
CA Foundation June'22
319



KARTIK LADHANI
CA Foundation June'22
316



RIDHI PAREKH
CA Foundation Dec'22
314



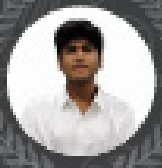
SMEET LADHANI
CA Foundation June'23
313



TANMAY AGARWAL
CA Foundation June'23
311



GARV KHANDELWAL
CA Foundation June'22
308



DAKSH JAIN
CA Foundation June'23
308



DEEPAK GURNANI
CA Foundation June'22
305



PARIDHI JHAWAR
CA Foundation June'22
304



SATYA BHANUSHALI
CA Foundation June'23
304

and many more...

ALL INDIA RANKERS CA INTER | MAY'22 & MAY'23 NOV'23



JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
CA INTER MAY'23
AIR 34



HIMANSHI DHAIJEE
CA INTER MAY'23
AIR 39



YUKTA SATPALKAR
CA INTER MAY'22
AIR 40



MARVI LODHA
CA INTER MAY'23
AIR 40



ARMAN HOSANGADY
CA INTER MAY'22
AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MEHDIRATTA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

ALL INDIA RANKERS CA FINAL | MAY'22 & NOV'23



SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHABRIA
CA FINAL NOV'23
AIR 32



PINAL KHETAN
CA FINAL NOV'23
AIR 35



SHOURYA TIBREWALA
CA FINAL MAY'22
AIR 39



DEEPAK LADHA
CA FINAL NOV'23
AIR 40



HIMANSHU KHATRI
CA FINAL MAY'22
AIR 41



SHRAVAN MUNDRA
CA FINAL NOV'23
AIR 45



DEEPTHI PACHIPULUSU
CA FINAL MAY'22
AIR 46



SHREY AGARWAL
CA FINAL MAY'22
AIR 48

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GHATKOPAR (W)
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KALYAN (E)
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KALYAN (W)
212, Shreeji Solitaire, Khadakpada Circle, Above Bikaner, Kalyan (W)
Ph. : 70390 633 33

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Ph. : 9530 531 080

BHIWANDI
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Ph. : 7020 902 068

CHEMBUR (E)
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Ph.: 8890 774 877

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SCAN ME!

^ **Introduction**

There are two types of organisations

1) Trading organisations **or** Profit making organisations

2) Non Trading Organisations (NTO) **or** Not for Profit Organisations (NPO).

* **Characteristics** or **Features of NPO**

i) **Purpose :**

A non-profit organisation is a **legal accounting entity** that is operated for the benifit of society as a whole, rather than for the benefit of a sole proprietor or a group of partners or group of shareholders.

The **main motive** behind such organisation is **to render service** to the society or the members of the organisation.

These are not business organisations operating with an intention to earn profits. These are set up with the **main objective** to provide qualitative service to its members and society at minimum charges and to promote art, culture, sports, education, charity, health etc. **Examples of NPO are** : Public Educational Institutions, Sports clubs, Public Hospitals, Religious Concerns (Temples, Churches etc), Trusts, Social Welfare Associations, Libraries etc. Such Not for profit organisations are **managed by** a group of individuals often called Trustees or Managing Committee.

ii) **Profit, not the Objective :**

Though NPO doesnot function with the objective to earn profit, it doesn't mean that it cannot earn profits. It also earns profits, termed as **surplus**, which is necessary to maintain its assets and also operations. Surplus is used for the objects for which it is set up and is not distributed amongst its members.

iii) **Financial Statements :**

NPO **prepares** its **final accounts** / financial statements annually showing the summary of financial transactions for its members, government departments, donors **etc.**

a) to comply with the statutory requirements,

b) for seeking grants from the government **and**

c) for getting confidence of donors and public at large.

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^ **Final Accounts of NPO :**

* **Usually given**

a) Receipts and Payments A/c (**summarised** Cash & Bank A/c)

It records **ALL** Receipts and Payments of money **during the year**, **whether**

Capital or Revenue **OR** whether relating to Current Year, Past Years or Next Years

b) Other relevant informations and adjustments

* **Usually to be prepared**

1. Income and Expenditure A/c (similar to Profit & Loss A/c)

2. Balance Sheet

Such final accounts are prepared more or less in **usual way**, following **accrual concept**.

^ **Incomes received by such NPO**

A. **If such Income** is for **general purpose (NOT specified** to be for **specific purpose)**

It includes various receipts which are either recurring or non recurring in nature

	Main sources of Incomes	**Treatment, unless otherwise given** or **warranted** due to nature of organisation
1	**Periodic Subscriptions**	I & E A/c, Income side
	amount paid by the members of NPO periodically to keep membership alive	
2	**Donations**	I & E A/c, Income side
3	**Grants received from Govt.**	I & E A/c, Income side
4	**Sundry Other Incomes**	I & E A/c, Income side
	Sale of old news papers, Interest received, Rent received, Profit on sale of FA etc	
5	**Corpus Donations**	Add to Capital Fund, Liability side
	Contributions by different parties for commencement & expansion of NPO	
6	**Entrance / Admission Fees**	Add to Capital Fund, Liability side
	amount paid by a person at the time of becoming member of a NPO	
7	**Life Membership Fees**	Add to Capital Fund, Liability side
	Lumpsum amount paid by a member **instead of** periodic subscription	
8	**Legacy**	Add to Capital Fund, Liability side
	the amount received as donation **under WILL** of a deceased person	

Note : Capital Fund, also known as General Fund / **Accumulated Fund**,
is an unrestricted fund which can be used by the management for any purpose of such NPO as may be considered appropriate.
Surplus or Deficit **from I & E A/c** every year is also transferred to Capital Fund.

B. If **such Income** is for a **Specific Purpose**

* **If it is for a Specific Event**, for which NO seperate / specific fund is to be created

These are the contributions of amount for a specific event like annual dinner, cultural program, exhibition, entertainment show, tournament etc.
Such receipt is to be **compared with** related expenses of such event and it may result into some (**net**) surplus **or** deficit from such event, which is to be **transferred to** I & E A/c.

* **If Seperate / Specific Fund is to be created for such purpose**

In such case, all the Incomes received for such purpose are to be **added to such fund** and such specific fund is shown on the **Liability side of the Balance Sheet**.
Such Incomes includes Donations - Legacy - Government Grants received etc. **for a specific purpose**.
Fund means amount received **or** set aside by a NPO for a specific purpose.
In such case, Fund amount, along with the income earned on the fund (**Income from Investments** made from **such fund**), cannot be used for purposes other than those for which such fund is created.
Use of such fund is restricted for a specific purpose **either** by the management **or** by the donor / government.
Purpose of such specific funds can be **Revex** or **Capex** to be incurred in future.

* **Funds created for Revex to be incurred in future**

Prize Fund, Sports Fund, Tournament Fund, Endowment Fund, Annuity Fund etc.
Contributions received towards such fund & Income earned on such fund Investments is to be **added to the** respective fund, where as related expenses (Revex) incurred during the year is to be **deducted from** such fund.

* **Funds created for Capex to be incurred in future**

eg. Building Fund
Contributions received towards such fund & Income earned on such fund Investments is to be **added to** the respective fund.
Amount spent on Purchase / Construction of FA during the year is to be **deducted** from such fund & **added** to the Capital fund.

Q. 1 : The Sportwriters Club gives the following Receipts and Payments Account for the year ended March 31, 2022 :

Receipts and Payments Account

Receipts	(₹)	Payments	(₹)
To Balance b/d	4,820	By Salaries	12,000
To Subscriptions	28,600	By Rent and electricity	7,220
To Miscellaneous income	700	By Library books	1,000
To Interest on fixed deposit	2,000	By Magazines and	
		newspapers	2,172
		By Sundry expenses	10,278
		By Sports equipments	1,000
		By Balance c/d	2,450
	36,120		**36,120**

Figures of other assets and liabilities are furnished as follows:

	As at March 31	
	(₹)	(₹)
	2021	**2022**
Salaries outstanding	710	170
Outstanding rent and electricity	864	973
Outstanding for magazines and newspapers	226	340
Fixed Deposit (10%) with bank	20,000	20,000
Interest accrued thereon	500	500
Subscription receivable	1,263	1,575
Prepaid expenses	417	620
Furniture	9,600	
Sports equipments	7,200	
Library books	5,000	

The closing values of furniture and sports equipments are to be determined after charging depreciation at 10% and 20% p.a. respectively inclusive of the additions, if any, during the year. The Club's library books are revalued at the end of every year and the value at the end of March 31, 2022 was ₹ 5,250.

Required :

From the above information you are required to prepare:

(a) The Club's Balance Sheet as at March 31, 2021;

(b) The Club's Income and Expenditure Account for the year ended March 31, 2022.

(c) The Club's Closing Balance Sheet as at March 31, 2022.

(d) Prepare Subscription A/c

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Q. 2 : From the following information supplied by XYZ Club, prepare Receipts and Payments Account and Income and Expenditure Account for the year ended 31st March, 2022. Also prepare Subscription Account.

	01.04.2021	31.03.2022
	₹	₹
Outstanding subscription	8,40,000	12,00,000
Advance subscription	1,50,000	1,80,000
Outstanding salaries	90,000	1,08,000
Cash in Hand and at Bank	6,60,000	?
10% Investment	8,40,000	4,20,000
Furniture	1,68,000	84,000
Machinery	60,000	1,20,000
Sports goods	90,000	1,50,000

Subscription for the year amount to ₹ 18,00,000. Salaries paid ₹ 3,60,000. Face value of the Investment was ₹ 10,50,000, 50% of the Investment was sold at 80% of face value. Interest on investments was received ₹ 84,000. Furniture was sold for ₹ 48,000 at the beginning of the year. Machinery and Sports Goods purchased and put to use at the last date of the year. Charge depreciation @ 15% p.a. on Machinery and Sports goods and @ 10% p.a. on Furniture.

Following expenses were made during the year :

Sports Expenses: ₹ 3,00,000

Rent: ₹ 1,44,000 out of which ₹ 12,000 outstanding

Misc. Expenses: ₹ 30,000

Q. 3 : From the following data, prepare an Income and Expenditure Account for the year ended 31st December 2019, and Balance Sheet as at that date of the Jeevan Hospital:

Receipts and Payments Account for the year ended 31 December, 2019

Receipts		(₹)	Payments	(₹)
To Balance b/d			By Salaries:	
Cash	800		(₹7,200 for 2018)	31,200
Bank	5,200	6,000	By Hospital Equipment	17,000
To Subscriptions:			By Furniture purchased	6,000
For 2018		5,100	By Additions to Building	50,000
For 2019		24,500	By Printing and Stationery	2,400
For 2020		2,400	By Diet expenses	15,600

To Government Grant:		By Rent and rates		
For building	80,000	(₹ 300 for 2020)		2,000
For maintenance	20,000	By Electricity and water		
Fees from sundry		charges		2,400
patients	4,800	By Office expenses		2,000
To Donations (not to be		By Investments		20,000
capitalized)	8,000	By Balances:		
To Net collections from		Cash	1,400	
benefit shows	6,000	Bank	6,800	8,200
	1,56,800			**1,56,800**

Additional information:	₹
Value of building under construction as on 31.12.2019	1,40,000
Value of hospital equipment on 31.12.2019	51,000
Building Fund as on 1.1.2019	80,000
Subscriptions in arrears as on 31.12.2018	6,500
Investments in 8% Govt. securities were made on 1st July, 2019.	

^ **Q. 4 :** The following was the Receipts and Payments Account of Exe Club for the year ended March 31, 2022

All figures are in thousands

Receipts	Amt. (₹)	Payments	Amt. (₹)
Cash in hand	100	Groundsman's Fee	750
Balance at Bank as per		Moving Machine	1,500
Pass Book :		Rent of Ground	250
Deposit Account	2,230	Cost of Teas	250
Current Account	600	Fares	400
Bank Interest	30	Printing & Office Expenses	280
Donations and Subscriptions	2,600	Repairs to Equipment	500
Receipts from teas	300	Honorarium to Secretary and	
Contribution to fares	100	Treasurer of 2021	400
Sale of Equipment	80	Balance at Bank as per	
Net proceeds of Variety		Pass Book :	
Entertainment	780	Deposit Account	3,090
Donation for forth coming		Current Account	150
Tournament	1,000	Cash in hand	250
	7,820		**7,820**

You are given the following additional information :

	April, 1, 2021	March, 31, 2022
	(₹)	(₹)
Subscription due	150	100
Amount due for printing etc.	100	80
Cheques unpresented being payment for repairs	300	260
Estimated value of machinery and equipment	800	1,750
Interest not yet entered in the Pass Book		20
Bonus to Groundsman outstanding		300

For the year ended March 31, 2022, the honorarium to the Secretary & Treasurer are to be increased by a total of ₹ 200. Prepare the Income and Expenditure Account and Balance Sheet for period ending 31st March, 2022 .

^ **Q. 5 :** The following is the Receipts and Payments Account of Lion Club for the year ended 31st March, 2022.

Receipts	Amt. (₹)	Payments	Amt. (₹)
Opening balance :		Salaries	1,20,000
Cash	10,000	Creditors	15,20,000
Bank	3,850	Printing and stationary	70,000
Subscription received	2,02,750	Postage	40,000
Entrance donation	1,00,000	Telephones and telex	52,000
Interest received	58,000	Repairs and maintenance	48,000
Sale of assets	8,000	Glass and table linen	12,000
Miscellaneous income	9,000	Crockery and cutlery	14,000
Receipts at		Garden upkeep	8,000
Coffee room	10,70,000	Membership fees	4,000
Soft drinks	5,10,000	Insurance	5,000
Swimming pool	80,000	Electricity	28,000
Tennis court	1,02,000	Closing balance :	
		Cash	8,000
		Bank	2,24,600
	21,53,600		**21,53,600**

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The assets and liabilities as on 1.4.2021 were as follows :

	₹
Fixed assets (net)	5,00,000
Stock	3,80,000
Investment in 12% Government securities	5,00,000
Outstanding subscription	12,000
Prepaid insurance	1,000
Sundry Creditors	1,12,000
Subscription received in advance	15,000
Entrance donation received pending membership	1,00,000
Gratuity fund	1,50,000

The following adjustments are to be made while drawing up the accounts :

(i) Subscription received in advance as on 31st March, 2022 was ₹ 18,000.

(ii) Outstanding subscription as on 31st March, 2022 was ₹ 7,000.

(iii) Outstanding expenses are salaries ₹ 8,000 and electricity ₹ 15,000.

(iv) 50% of the entrance donation was to be capitalized. There was no pending membership as on 31st March, 2022.

(v) The cost of assets sold net as on 1.4.2021 was ₹ 10,000.

(vi) Depreciation is to be provided at the rate of 10% on assets.

(vii) A sum of ₹ 20,000 received in October 2021 as entrance donation from an applicant was to be refunded as he has not fulfilled the requisite membership qualifications. The refund was made on 3.6.2022.

(viii) Purchases made during the year amounted ₹ 15,00,000.

(ix) The value of closing stock was ₹ 2,10,000.

(x) The club as a matter of policy, charges off to income and expenditure account all purchases made on account of crockery, cutlery, glass and linen in the year of purchase.

You are required to prepare an Income and Expenditure Account for the year ended 31st March, 2022 and the Balance Sheet as on 31st March, 2022 along with necessary workings.

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Q. 6 : From the following balances and particulars of Republic College, prepare Income & Expenditure Account for the year ended March, 2022 and a Balance Sheet as on the date :

	(₹)	(₹)
Seminars & Conference Receipts		4,80,000
Consultancy Receipts		1,28,000
Security Deposit - Students		1,50,000
Capital Fund		16,06,000
Research Fund		8,00,000
Building Fund		25,00,000
Provident Fund		5,10,000
Tuition Fee Received		8,00,000
Government Grants		5,00,000
Donations		50,000
Interest & Dividends on Investments		1,85,000
Hostel Room Rent		1,75,000
Mess Receipts (Net)		2,00,000
College Stores - Sales		7,50,000
Outstanding expenses		2,25,000
Stock of - Stores and Supplies (opening)	3,00,000	
Purchases - Stores & Supplies	8,00,000	
Salaries - Teaching	8,50,000	
Research	1,20,000	
Scholarships	80,000	
Students Welfare expenses	38,000	
Repairs & Maintenance	1,12,000	
Games & Sports Expenses	50,000	
Misc. Expenses	65,000	
Research Fund Investments	8,00,000	
Other Investments	18,50,000	
Provident Fund Investment	5,10,000	
Seminar & Conference Expenses	4,50,000	
Consultancy Expenses	28,000	
Land	1,00,000	
Building	16,00,000	
Plant and Machinery	8,50,000	
Furniture and Fittings	6,00,000	
Motor Vehicle	1,80,000	

Provision for Depreciation:		
Building		4,80,000
Plant & Equipment		5,10,000
Furniture & Fittings		3,36,000
Cash at Bank	6,42,000	
Library	3,60,000	
	1,03,85,000	1,03,85,000

Adjustments:

		(₹)
(1)	Materials & Supplies consumed: (From college stores)	
	Teaching	50,000
	Research	1,50,000
	Students Welfare	75,000
	Games or Sports	25,000
(2)	Tuition fee receivable from Government for backward class Scholars	80,000
(3)	Stores selling prices are fixed to give a net profit of 10% on selling price	
(4)	Depreciation is provided on straight line basis at the following rates:	
	(1) Building	5%
	(2) Plant & Equipment	10%
	(3) Furniture & Fixtures	10%
	(4) Motor Vehicle	20%

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Q. 7 : From the following Income and Expenditure account and the Balance sheet of a club, prepare its Receipts and Payments Account and subscription account for the year ended 31st March, 2019 :

Income & Expenditure Account for the year 2018-19

Particulars	(₹)	Particulars	(₹)
To Upkeep of ground	11,000	By Subscriptions	19,052
To Printing	1,100	By Sale of Newspapers (Old)	286
To Salaries	11,100	By Lectures (Fee)	1,650
To Depreciation on furniture	1,100	By Entrance Fee	2,145
To Rent	1,660	By Misc. Income	440
		By Deficit	2,387
	25,960		**25,960**

Balance sheet as at 31st March 2019

Liabilities		(₹)	Assets	(₹)
Subscription in advance		110	Furniture	9,900
(2019-20)			Ground and Building	51,700
Prize fund:			Prize Fund Investment	22,000
Opening balance	27,500		Cash in Hand	2,530
Add: Interest	1,100		Subscription (outstanding)	770
	28,600		(2018-2019)	
Less: Prizes given	2,200	26,400		
General Fund:				
Opening balance	62,062			
Less: Deficit	2,387			
	59,675			
Add: Entrance Fee	715	60,390		
		86,900		**86,900**

The following adjustments have been made in the above accounts:

(i) Upkeep of ground ₹ 660 and printing ₹ 264 relating to 2017-18 were paid in 2018-19

(ii) One fourth of entrance fee has been capitalized by transfer to General Fund.

(iii) Subscription outstanding in 2017-18 was ₹ 880 and for 2018-19 ₹ 770.

(iv) Subscription received in advance in 2017-18 was ₹ 220 and in 2018-19 for 2019-20 was ₹ 110.

(v) Furniture was purchased during the year.

^	**Try Yourself : Objectives**
*	**State whether the following statements are True or False with reasons :**
1	The Receipts and payment account for a non-profit organization follows the accrual concept of accounting.
2	Both the revenue and capital nature transactions are recorded in the Income and expenditure account.
3	Sale of grass by a sports club is to be treated as sale of an asset.
4	Subscriptions outstanding for the current year are disclosed under the Fixed assets side of the Balance sheet.
5	Receipts and payments account gives the details about the expenses outstanding for the year.
6	Adjustments in the form of additional information shall be adjusted in the final accounts of a Non- profit organisation only in one place.
7	Tournament expenses incurred are more than the Tournament fund, then the excess to be shown as an asset in the closing Balance sheet.
8	For Non-profit organisation, Excess of income over expenditure in the Income and Expenditure account is termed as profit.
9	Surplus of non-profit organizations is distributed among its members.
10	Tournament fund, building fund, library fund is based on the fund based accounting.
11	Subscription fees refers to the one-time fees paid by the members to get admission for the benefits of the club.
12	Token payment made to a person, who voluntarily undertakes a service which would normally be paid in case of profitable organization is termed as Honorarium.
13	An Insurance company is an example of non-profit organization.
14	Part amount of entrance fees which is to be capitalized shall be disclosed in the income and expenditure account.
15	Both the income and expenditure of the current and the previous year are recorded in the Income and Expenditure account.
16	Amount received as donation by an Non-profit organisation under the will of a deceased person is termed as legacy.
17	Where a Non-profit organisation has a separate trading activity, the profit/loss from the trading account shall be transferred to Income and Expenditure Account at the time of consolidation.
18	Not for profit concerns concentrate their efforts to maximize the profit earning avenues.
19	All the receipts are of revenue nature in case of Non-profit organisation.
20	There is opening balance of Income and expenditure account.
21	Receipts and Payments Account highlights total income and expenditure.

22	Net income in case of persons practicing vocation is determined by preparing profit and loss account.
23	In case a Sports Fund is kept, expenses on account of sports events should be charged to Sports Fund.
24	Laboratory & library Deposits taken from the students in case of an Educational Institution are shown on the liabilities side of the Balance Sheet.
25	Fees received for Life Membership is a revenue receipt as it is of recurring nature.
26	Not for Profit Concerns do not have profit motive.
27	Charitable Institutions prepare Profit and Loss Account at the end of every financial year.
28	There is no difference between Receipts and Payments Account and Income and Expenditure Account
29	Income and Expenditure Account represents either surplus or deficit.
30	Receipts and Payments Account do not have any opening balance.
31	Not for profit Concerns do not prepare Balance Sheet.
32	Purchases of Sports Equipment is a Capital Expenditure.
33	Income and Expenditure Account is Real Account.
34	Receipts and Payments Account contains only the transactions relating to current year.
35	Excess of Assets over Liabilities is called Capital Fund.
	Answers :
1	**False**
	It depicts the cash system of accounting rather than the accrual system, as the cash receipts and payments pertaining to any year are entered in the Receipts and payments account. The principle of accrual is not followed with regard to the receipts and payments account of a non-profit organization.
2	**False**
	The income and expenditure account records only the revenue income and expenditure. The capital transactions are being recorded in the Balance sheet.
3	**False**
	The grass for a sports club is not a capital item, hence the sale of such grass shall be treated as a revenue receipt.
4	**False**
	They are disclosed under the current assets of the Balance sheet as they will be paid within the next year and not to be treated as non-current assets.

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5	**False**
	Receipts and payments account gives information about the expenses paid in cash for the current year, previous or the next year. It is only from the additional information we identify the outstanding expenses.
6	**False**
	Additional information means that information which has been identified just before the preparation of the final accounts. As NPO follows the double entry system of book keeping, there shall be 2 effects for each of the additional information.
7	**False**
	The excess of expenditure over the tournament fund shall be debited to the income and expenditure account and not taken to the closing balance sheet.
8	**False**
	The excess of the income over the expenditure is called as Surplus and not profit for an Non-profit organisation.
9	**False**
	The Non-profit organisation credits the surplus earned in a year to the general fund maintained by it.
10	**True**
	It is Fund based accounting that records the fund balances in the balance sheet.
11	**False**
	Subscription is a regular fees paid by the members to keep the membership alive.
12	**True**
	Honorarium refers to the nominal amount paid for the services with a non-commercial intent.
13	**False**
	Insurance Company has a profit motive, hence it is not a non-profit organization.
14	**False**
	It shall be shown in the Balance sheet- where it is to be capitalized.

15	**False**
	It is only the current year income and expenditure which is recorded in the Income and Expenditure account as per the accrual concept.
16	**True**
	While on the death bed, if there is any will written that the assets of a person shall be donated to any NPO - then such a donation to the NPO, is termed as Legacy.
17	**True**
	Where in case of the trading activities, the profit /loss from such activity to be transferred to the Income and expenditure account in case of consolidated accounts.
18	**False**
	The Non-profit organisation has its very existence to serve the members and the society. Profit earning shall never be its motive.
19	**False**
	Receipts can be both of revenue as well as capital nature. Receipts of both the nature are recorded in the receipts and payments account.
20	**False**
	It represents a nominal account and is prepared in accordance with the accrual concept, hence there can be no opening balances.
21	**False**
	Receipts and payments account is a classified summary of cash receipts and payments over a certain period together with cash and bank balances at the beginning and close of the period.
22	**False**
	Net income is determined by preparing income and expenditure in case of persons practicing vocation.
23	**True**
	Institutions sometimes keep special funds for some special purposes. In such a case the income related to such funds should be added to these funds and expenses should be deducted from such funds.

24	**True**
	Because the laboratory and library deposits are of the nature of security deposits to be refunded to the students on their leaving the College or University.
25	**False**
	Life Membership Fee received for life membership is a capital receipt as it is of non-recurring nature. It is directly added to capital fund or general fund.
26	**True**
	The organisations which are not engaged in trading activities but established with a service motive are called as 'not for profit concerns.
27	**False**
	Income and Expenditure account is prepared by not for profit concern instead of Profit and Loss Alc.
28	**False**
	Receipts and Payments Account is a summary of cash and bank transactions for a particular period it contains all receipts and payments for current year, past year and future years. Where has Income and Expenditure Account shows Income and Expenditure for current year only.
29	**True**
	Income and Expenditure Account is a summary of revenue income and revenue expenses of a particular period (year). It is similar to profit and loss account all revenue expenses / losses of current year are debited to find surplus or deficit.
30	**False**
	Receipts and Payments Account do have opening balance of cash and bank or bank overdraft.
31	**False**
	Not for Profit concern do prepare Balance sheet to know their financial position on particular date i.e. financial year (31st March).
32	**False**
	Purchase of Sports Equipment is a Revenue Expenditure is used day to day and its life is short (Less than a year).

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33	**True**
	Income and Expenditure account is a Nominal Alc. It shows current year income/gains and current year expenses/losses. It is similar to Profit and Loss Account.
34	**False**
	Receipts and Payments Account contains all cash and bank transactions relating to current year, past year and future years. It is as goods as cash back with cash and bank balance
35	**True**
	The excess of assets over liabilities of not for profit concern represents capital fund. It is similar to capital account. Every year surplus of Income and Expenditure Account is added to this fund and deficit is subtracted. Entrance fees. Life membership fees and Legacies are added to this fund.
*	**Select the most appropriative alternatives from those given below.**
1	Scholarship greanted to students out of specific funds provided by Government will be debited to
	(a) Income and Expenditure Account
	(b) Receipts and Payment Account
	(c) Fees Granted for Scholarship Account
2	In case of NPO, excess of total assets over liabilities is known as
	(a) Profits (b) Surplus (c) Capital Fund
3	General donations and legacies are credited to
	(a) Receipts and Payments Account.
	(b) Income and Expenditure Account.
	(c) Capital Fund.
4	Interest on prize funds is
	(a) Credited to Income and Expenditure Account.
	(b) Credited to Receipts and Payments Account.
	(c) Added to prize fund.
5	Not for Profit Concern renders_____services to public at large.
	(a) Commercial (b) Social (c) Individual

6	Special aids are
	(a) Treated as capital receipts.
	(b) Treated as revenue receipts.
	(c) Both (a) and (c).
7	If there exist a specific sports fund, the expenses incurred in relation to sports activities will be taken to
	(a) Income and Expenditure Account
	(b) Receipt and Payment Account
	(c) Sports fund
8	Donation for Scholarship Fund is _____
	(a) Capital Receipt (b) Revenue Receipt (c) None
9	Income and Expenditure Account is a_____Account.
	(a) Personal (b) Real (c) Nominal
10	Outstanding subscription at the end of the accounting year represents_____
	(a) Liability (b) Capital Fund (c) An Asset
11	Subscription received in advance during the accounting year is_____.
	(a) Liability (b) Capital Fund (c) An Asset
12	Excess of Income over Expenditure is termed as_____
	(a) Deficit (b) Profit (c) Surplus
13	Not for Profit Concerns prepares_____account instead of Profit and Loss account to know the result.
	(a) Trading (b) Income and Expenditure (c) Receipts and Payments
14	The closing balance of Receipts and Payments account usually represent
	(a) Closing stock (b) Cash and Bank balance (c) Surplus
15	Not for Profit Organization is also called_____organization.
	(a) Service (b) Trading (c) Profit making

16 Expenditure on Purchase of Building is a_____Expenditure.

(a) Capital (b) Revenue (c) General

Answers

1	(c)		9	(c)
2	(c)		10	(c)
3	(b)		11	(a)
4	(c)		12	(c)
5	(b)		13	(b)
6	(c)		14	(b)
7	(c)		15	(a)
8	(a)		16	(a)

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BHAVIK DOSHI



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

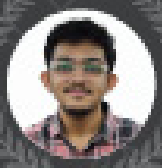
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328



PALAK JAJODIA
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325



SWASTIKA SINGH
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SUKUNJ GUPTA
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DURGASHRI VS
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319



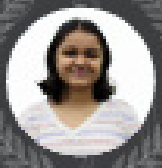
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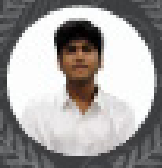
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TANMAY AGARWAL
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311



GARV KHANDELWAL
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308



DAKSH JAIN
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DEEPAK GURNANI
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305



PARIDHI JHAWAR
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SATYA BHANUSHALI
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and many more...

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CA INTER MAY'22

AIR 13



MANAN SHAH
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AIR 14



PRACHI NANDU
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AIR 24



VATSAL MEHTA
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AIR 46



PRANJAL MEHDIRA
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AIR 46



SANJEEV JAIN
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AIR 47



RISHABH JAIN
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AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

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SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHABRIA
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AIR 32



PINAL KHETAN
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AIR 35



SHOURYA TIBREWALA
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AIR 39



DEEPAK LADHA
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AIR 40



HIMANSHU KHATRI
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SCAN ME!

^ **Meaning / Definition and Features of Partnership**

"Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all". (**Section 4** of the IPA, 1932)

In India, partnership is regulated by **the Indian Partnership Act, 1932.** (IPA, 1932)

The persons who have entered into partnership are individually known as **partners** and collectively as a **firm.**

The name under which the business is conducted is known as **firm's name.**

^ **Features / Characteristics of Partnership**

i) **Association of two or more persons**

Partnership is an association of two or more persons.
Minimum 2 partners are required to form a partnership.
Maximum 50 partners are allowed in a firm, as prescribed by The Companies Act, 2013 vide section 464 and as specified in Rule 10 of the Companies Rules, 2014.

ii) **Existence of an agreement :** As per section 5 of the Indian Partnership Act, 1932, The relation of partnership arises from contract between parties and not from status as it happens in case of HUF (Hindu Undivided Family).
A formal **or** written agreement is **not necessary** to create a partnership.

Partnership comes into existence by an agreement, **either** written **or** oral.
The terms & conditions of the agreement amongst partners is the basis of their relationship.

* **Contents of the Partnership Deed** usually may include **:**

1) Name and adress of the firm and its main business
2) Name and adress of all partners
3) Duration of the partnership
4) Rights, duties and liabilities of partners
5) Capital contribution by partners
6) Ratio in which profits (& losses) are to be shared amongst partners
7) Rate of interest (if any) on capital, loan, drawings etc.
8) Salary, Commission etc (if any) payable to partners.
9) Provisions relating to admission, retirement and death etc. of a partner
10) Settlement of accounts on dissolution of firm

11) Method of settlement of disputes amongst partners

12) Any other matter relating to the conduct of business

It is advisable to have a **registered** written agreement i.e. partnership deed, to avoid disputes in the future amongst the partners.

iii) **Sharing of Profit** : The persons concerned must agree to share the profits of the business because no person is a partner unless he or she has the right to share the profits of the business. Section 4 of Indian Partnership Act, 1932 does not insist upon sharing of losses. Thus, a provision for sharing of loss is not necessary.

iv) **Minor as a partner** : A minor can be added in partnership firm, but the condition is that he can be admitted to share profit only. He cannot be made to share losses of the firm. If the partnership firm suffers loss than it will be borne by other major partners is their profit-sharing ratio.

v) **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.
Section 2 (b) of Indian Partnership Act, 1932 only states that business includes every trade, occupation and profession.
Business of the partnership should be **Lawful** & such business may be carried on by all or any of them acting for all. Such **Principle of mutual agency** means partners are principals and also agents of each other.
It means each partner is bound by the acts of other partner(s).

vi) **Mutual agency :** It means that the business is to be carried on by all or any of them acting for all. Thus, if the person carrying on the business acts not only for himself but for others also so that they stand in the positions of principals and agents, they are partners.

vii) **Unlimited Liability :**
From accounting point of view, partnership firm is a separate business entity.
However, **Liability of partners is unlimited.**
Partners are **jointly & severally** liable for the debts of the business, in case firm is unable to meet its liabilities, due to its bankruptcy / insolvency.
In such case,
net private assets of a partner can be used to pay firm's balance debts.

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^ **Appropriations out of Profits**

It means **distribution** of Profit amongst the Partners (Owners of business)

a) **Transfer to Reserves**

Reserves are undistributed / accumulated profits.

These are past profits which are **yet not** distributed to the owners / partners, but are kept in the business for future uncertainities / requirements.

In order to strengthen the financial position of the business and with a view to meet all eventualities, it is desirable that entire profits should not be distributed amongst the owners of the business. Some portion of profit should be kept in the business for meeting unknown liabilities / losses in future.

This is done by **creating Reserves** at the time of preparing Final accounts.

* **Journal Entry** for creation of **Reserves out of Profits**

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

To Reserves A/c

Reserves means the amounts **set aside out of profits** & other surpluses, **which are not earmarked in any way** to meet any particular liability known to exist on the date of the Balance Sheet.

The Reserves may be created for

Expansion of business (ploughing back of the profits), better financial position, meeting unforeseen contingencies etc.

Examples of Reserves

i) General Reserve
ii) Reserve Fund
iii) Profit & Loss A/c (credit balance)
iv) Investment Fluctuation Fund
v) Workmen Compensation Fund
vi) Capital Reserve **etc.**

It should be clearly understood that the amount of Reserve **does not represent** any expense / loss / liability.

It represents undistributed profits, **belonging to** the owners of the business.

b) **Interest on Capital (IOC)** / Salary / Remuneration / Commission **etc**
Payable **by** the Firm **to** Partners, **as** may have been **agreed amongst partners**

i) **For IOC** etc **Allowed / Payable**

IOC / S / R / C etc A/c **Dr.**
To Partners Capital A/c's

ii) To close **IOC** etc **A/c**

Profit & Loss Appropriation A/c **Dr.**
To IOC / S / R / C etc A/c

c) **Interest on Drawings (IOD)** Charged / Payable **by** Partners **to** the Firm,
as may have been **agreed amongst partners**

i) **For IOD Charged / Receivable**

Partners Capital A/c's **Dr.**
To Interest on Drawings A/c

ii) To close **IOD A/c**

Interest on Drawings A/c **Dr.**
To Profit & Loss Appropriation A/c

d) Balance **Profit to be distributed** to the Partners **in agreed P.S.R.**

Profit & Loss Appropriation A/c **Dr.**
To Partners Capital A/c's

Dr. **Profit & Loss Appropriation A/c** for the year ended ..... **Cr.**

	₹	₹		₹	₹
			By Net Profit b/d		xxx
To Reserves A/c		xxx	**By IOD A/c**		
(% of N.P. **or** as given)			A	xx	
			B	xx	xxx
To IOC / S/R/C etc A/c					
A	xx				
B	xx	xxx			
To Partners Capital A/c's					
A	xx				
B	xx	xxx			
(Balance Profit)					
		XXX			**XXX**

^ **Key Points**

1) Appropriations means **distribution** of Profit amongst the Partners / Owners.
Hence, existence of profits is **MUST** for appropriations.
In any case,
appropriations **cannot exceed** profits, unless otherwise agreed amongst partners.

2) Rent payable by the firm to Partner & **Interest on Partners Loan**
These are **Charge against Profits**, NOT appropriations and hence,
will be recorded in Profit & Loss A/c, **NOT in** P & L Appropriation A/c

^ **Provisions of IPA, 1932**

When there is **NO** oral / written agreement amongst partners (**NO** Partnership deed)
OR such deed doesn't have a clause (deed is silent) on a particular matter,
then, the Provisions of **IPA 1932 shall apply,** as follows.

Provisions of the IPA, 1932 (to be followed, **only if** problem is silent)

* **Provisions of the IPA, 1932** (to be followed, **only if** problem is silent)

1	Sharing of Profits & Losses : **P.S.R.**	**EQUAL** amongst all partners
	Payable **by** Firm **to** Partner	
2	Interest on Partners Capital / Current A/c's	**NOT** allowed
	Salary / Remuneration / Commission to Partners	
	Interest on Loan **by** Partner **to** the Firm	allowed at **6% p.a.**
3	Payable **by** Partner **to** the Firm	
	Interest on Partners Drawings	**NOT** charged
	Interest on Loan **by** the Firm **to** Partner	

^ **Q. 1 :** A and B commenced business in partnership on 1 January 2022. No partnership agreement was made either oral or written. They contributed ₹ 40,000 and ₹ 10,000 respectively as capital. In addition, A also advanced ₹ 20,000 on 1 July 2022. A met with an accident on 1 April 2022 and could not attend to the partnership business upto 30 June 2022. The profits for the year ended on 31 December 2022 amounted to ₹ 50,600. Disputes having been arisen between them for sharing the profits.
A claims: (i) He should be given interest at 10% p.a. on capital & loan (ii) Profit should be distributed in proportion of capital.
B claims: (i) Net profit should be shared equally (ii) He should be allowed remuneration of ₹ 1,000 p.m. during the period of A's illness (iii) Interest on capital and loan should be given @ 6% p.a. You are required to settle the dispute between them and distribute the profits according to law. State reasons for your answer.

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^ **Q. 2 :** Shilpa and Sanju are partners with a capital of ₹1,00,000 and ₹1,60,000 on January 1,2022 respectively. Shilpa introduced additional capital of ₹30,000 on July 1, 2022 and another ₹20,000 on October 31, 2022. Calculate interest on capital for the year ending 2022. The rate of interest is 9% p.a.

^ **Q. 3 :** X, a partner, has drawn the following sum of money :

On 29 th February, 2022 ₹ 500 ; On 31 st March, 2022 ₹ 400

On 30 th June, 2022 ₹ 600 ; On 31 st October, 2022 ₹ 800

Accounts are closed on 31 st December every year.

Interest is chargeable on drawings at 6% p.a. calculate interest on drawings.

^ **Calculation of Interest on Partners Capital A/c's (IOC)**

* It is allowed / payable only if specifically **agreed** amongst the partners
* It is **appropriation out of profits** and hence, payable only if there are profits
* Following **should be taken into account** while calculating IOC

i) Opening Capital **ii)** Further Capital Introduced

iii) Drawings **out of** Capital (as clearly specified)

(Drawings should be assumed to be out of profits, if no information given)

^ **Calculation of Interest on Partners Drawings (IOD)**

* Interest on drawings is charged only if specifically **agreed** amongst the partners

It is charged on drawings out of profits (& **not on** drawings out of capital)

Drawings by partners should be assumed to be out of profits, if no information given.

* **When** amount of drawings **&/or** time interval between the 2 drawings is **NOT** uniform.

IOD is to be calculated at agreed rate, on each drawings seperately,

for a period depending upon actual date of each drawings.

* **When** amount of drawings **&** time interval between the 2 drawings **is uniform**,

average method can be followed as follows.

	If drawings are made	Interest on total drawings to be for
2	uniformly throughout the period	6 months (half of total period)
	in the middle of every month	
	no info is given in the problem	
2	At the beginning of every month	6 1/2 months [(12 + 1) / 2]
3	At the end of every month	5 1/2 months [(11 + 0) / 2]
4	At the beginning of every quarter	7 1/2 months [(12 + 3) / 2]
5	At the end of every quarter	4 1/2 months [(9 + 0) / 2]

^ **Q. 4 :** Drawings by Partners A and B for the year ended 31 st March 2023 is as follows. Calculate IOD @ 8% p.a. in each of the following cases.

Case	Drawings p.a.		
	A	B	
1	1,20,000	1,80,000	on 1 st July and 1 st Dec. 2022 respectively
2	1,20,000	1,80,000	no information is given in the problem
3	1,20,000	1,80,000	on first day of every month
4	1,20,000	1,80,000	on last day of every month
5	1,20,000	1,80,000	on first day of every quarter
6	1,20,000	1,80,000	on last day of every quarter

^ **Partners Capital Accounts**

* Partners introduces capital in the business when the business is started and also in future as and when needed.
* Partners may withdraw capital in future or total capital of the firm may be increased or decreased, as per mutual consent of partners.
* Capitals of partners may not be in equal proportion or in their P.S.R.
* Capital may be contributed by partner in cash or in kind.
  Capital brought in in kind is recorded in books of accounts at agreed values.

* **Methods** of maintaining **Partners Capital A/c's**

Capital account for each partner is maintained seperately.
Such Capital account of each partner can be maintained following
either
Fluctuating Capital Accounts Method
or
Fixed Capital Accounts Method

Under both the methods,
Loan given by partner to firm & Interest due on such loan is recorded in **Loan by Partner A/c** and is shown seperately on the Liability side.

* **a) Fluctuating Capital Accounts Method**

Under this method,
only Capital account is maintained for each partner and hence,
all transactions of a partner are shown in the Capital account of the partner.
As a result,
balance in capital account keeps **Fluctuating** with every transaction.

Capital account balance :

increases due to

i) additional capital introduced by the partner

ii) rent due to the partner

iii) Interest on capital due to the partner

iv) salary / commission due to the partner

v) share in profit and it

decreases due to

i) drawings out of capital by partner

ii) drawings out of profits by partner

iii) Interest on drawings payable by partner

iv) Interest on loan by firm to partner payable by partner

v) share in loss

As a result,

Capital A/c under this method can have credit balance **or** debit balance.

Credit balance is shown on the **Liability side** indicating amount payable to the partner.

Debit balance is shown on the **Asset side** indicating amount receivable from the partner.

Note : In the absence of any information,
Fluctuating Capital Accounts method is followed.

* **b) Fixed Capital Accounts Method**

Under this method, two accounts are maintained for each partner

i) Partners Capital Account ii) Partners Current Account

Under this method, Capital accounts of partners is intended to be kept **Fixed**.

It shows same balance year after year, **except when**

additional capital is introduced **or** part capital is withdrawn by the partner.

Hence, all transactions relating to partner, **except** introduction or withdrawl of capital,

are recorded in the separate account for each partner called Partners Current A/c.

As a result, Capital A/c under this method will have credit balance **(Liability side)**

Current A/c under this method can have credit balance **or** debit balance.

Credit balance is shown on the **Liability side** indicating amount payable to the partner.

Debit balance is shown on the **Asset side** indicating amount receivable from the partner.

Note: Fixed Capital Method is followed **only when** it is specifically given in the problem,

either directly or indirectly (by giving Partners Current A/c's balances).

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Capital Ratio

Partners may agree to share profits and losses in the capital ratio.

When capitals are fixed, profits will be shared in the ratio of given capitals.

But if capitals are fluctuating & partners introduce or withdraw capitals during the year, the capitals for the purpose of ratio would be determined with reference to time on the basis of weighted average method.

Q. 5 : A and B are partners sharing profits and losses in the ratio of their effective capital. They had ₹ 1,00,000 & ₹ 60,000 respectively in their Capital A/c's on 1.1.2022. A introduced a further capital of ₹ 10,000 on 1st April, 2022 and another ₹ 5,000 on 1st July, 2022. On 30th September, 2022 A withdrew ₹ 40,000. On 1st July, 2022, B introduced further capital of ₹ 30,000. The partners drew the following amounts in anticipation of profit. A drew ₹ 1,000 per month at the end of each month beginning from January, 2022. B drew ₹ 1,000 on 30th June and ₹ 5,000 on 30th September, 2022. 12% p.a. interest on capital is allowable and 10% p.a. interest on drawings is chargeable. Date of closing 31.12.2022. Calculate: (a) Profit-sharing ratio; (b) Interest on capital; and (c) Interest on drawings.

Q. 6 : Ram and Rahim start business with capital of ₹ 50,000 and ₹ 30,000 on 1st January, 2022. Rahim is entitled to a salary of ₹ 400 per month. Interest is allowed on capitals and is charged on drawings at 6% per annum. Profits are to be distributed equally after the above noted adjustments. During the year, Ram withdrew ₹ 8,000 and Rahim withdrew ₹ 10,000. The profit for the year before allowing for the terms of the Partnership Deed came to ₹ 30,000. Assuming the capitals to be fixed, prepare the Profit & Loss Appropriation A/c and the Capital & Current A/c's relating to the partners.

Q. 7 : Weak, Able & Lazy are in partnership sharing profits and losses in the ratio of 2:1:1. It is agreed that interest on capital will be allowed @ 10% per annum & interest on drawings will be charged @ 8 % per annum. (No interest will be charged/allowed on Current Accounts).

The following are the particulars of the Capital and Drawings Accounts of the partners

	Weak	Able	Lazy
	(₹)	(₹)	(₹)
Capital (1.1.2022)	75,000	40,000	30,000
Current Account (1.1.2022)	10,000	5,000	(Dr.) 5,000
Drawings	15,000	10,000	10,000

The draft accounts for 2022 showed a net profit of ₹ 60,000 before taking into account

(a) Life Insurance premium of Weak amounting to ₹ 750 paid by the firm on 30th June, 2022 has been charged to Miscellaneous Expenditure A/c.

(b) Repairs of Machinery amounting to ₹ 10,000 has been debited to Plant Account and depreciation thereon charged @ 20%.

(c) Travelling expenses of ₹ 3,000 of Able for a pleasure trip to U.K. paid by the firm on 30th June, 2022 has been debited to Travelling Expenses Account.

You are required to prepare the Profit and Loss Appropriation Account, Current Accounts of partners Weak, Able and Lazy for the year ended 31st December, 2022.

^ **Q. 8 :** Ram and Rahim are in partnership sharing profits and losses in the ratio of 3:2. As Ram, on account of his advancing years, feels he cannot work as hard as before, the chief clerk of the firm, Ratan, is admitted as a partner with effect from 1st January, 2022, and becomes entitled to 1/10th of the net profits and nothing else, the mutual ratio between Ram and Rahim remaining unaltered.

Before becoming a partner, Ratan was getting a salary of ₹ 500 p.m. together with a commission of 4% on the net profits after deducting his salary and commission.

It is provided in the partnership deed that the share of Ratan's profits as a partner in excess of the amount to which he would have been entitled if he had continued as the chief clerk, should be taken out of Ram's share of profits.

The net profit for the year ended December 31, 2022 is ₹ 1,10,000.

Show the distribution of net profit amongst the partners.

^ **Guarantee of Minimum Profit**

Sometimes, one partner can enjoy the right to have minimum amount of profit in a year as per the terms of the partnership agreement.

In such case, allocation of profit is done in a normal way if the share of partner, who has been guaranteed minimum profit, is more than the amount of guaranteed profit.

However, if share of the partner is less than the guaranteed amount, he takes minimum profit & the excess of guaranteed share of profit over actual share is borne by the remaining partners as per the agreement.

There are **3 possibilities** as far as share of deficiency by other partners is concerned.

These are as follows:

- Excess is payable by one of the remaining partners.
- Excess is payable by at least two or all the partners in an agreed ratio.
- **Excess is payable by remaining partners in their mutual profit sharing ratio.**

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If the question is silent about the nature of guarantee,
the burden of guarantee is borne by the remaining partners in their mutual P.S.R.

Note :
If guarantee is given to newly admitted partner & such partner is admitted during year, Guaranteed amount should be calculated on proportionate basis from the date of admission of guaranteed partner till the closing date of accounting period.

^ **Q. 9 :** A and B were partners in a firm sharing profits and losses in the ratio of 3:2. They admit C for 1/6th share in profits and guaranteed that his share of profits will not be less than ₹ 250,00,000. Total profits of the firm for the year ended 31st March, 2022 were ₹ 900,00,000. Calculate share of profits for each partner when:
1. Guarantee is given by firm.
2. Guarantee is given by A
3. Guarantee is given by A and B equally.

^ **Q. 10 :** A, B and C are partners in a firm sharing profits and losses in the ratio of 2:3:5. Their fixed capitals were ₹ 15,00,000, ₹ 30,00,000 and ₹ 60,00,000 respectively. For the year 2022 interest on capital was credited to them @ 12% instead of 10%. Pass the necessary adjustment entry.

^ **Distinction between an ordinary Partnership Firm and LLP**

	Basis	LLP	Partnership firm
1	Regulating Act	The Limited Liability Partnership Act, 2008.	The Indian Partnership Act, 1932
2	Body corporate	It is a body corporate.	It is not a body corporate,
3	Separate legal entity	It is a legal entity separate from its members.	It is a group of persons with no separate legal entity.
4	Creation	It is created by a legal process called registration under the LLP Act, 2008.	It is created by an agreement between the partners.
5	Registration	Registration is mandatory. LLP can sue and be sued in its own name.	Registration is voluntary. Only the registered partnership firm can sue the third parties.
6	Perpetual succession	The death, insanity, retirement or insolvency of the partner(s) does not affect its existence of LLP. Members may join or leave but its existence continues forever.	The death, insanity, retirement or insolvency of the partner(s) may affect its existence. It has no perpetual succession.

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7	Name	Name of the LLP to contain the word limited liability partners (LLP) as suffix.	No guidelines. The partners can have any name as per their choice.
8	Liability	Liability of each partner limited to the extent to agreed contribution except in case of willful fraud.	Liability of each partner is unlimited. It can be extended upto the personal assets of the partners.
9	Mutual agency	Each partner can bind the LLP by his own acts but not the other partners.	Each partner can bind the firm as well as other partners by his own acts.
10	Designated partners	At least two designated partners and atleast one of them shall be resident in India.	There is no provision for such partners under the IPA, 1932
11	Number of Partners	Minimum 2 but no maximum limit	Minimum 2 and maximum 50.
12	Legal compliances	Only designated partners are responsible for all the compliances and penalties under this Act.	All partners are responsible for all the compliances and penalties under the Act.
13	Foreign partnership	Foreign nationals can become a partner in a LLP.	Foreign nationals cannot become a partner in a partnership firm.
14	Minor as partner	Minor cannot be admitted to the benefits of LLP.	Minor can be admitted to the benefits of the partnership with the prior consent of the existing partners.

^ Final Accounts of a Partnership Firm includes the following :

1) Trading A/c for the year ended ……..

(To find out Gross Profit earned during the year)

2) a) **Profit & Loss A/c** for the year ended ……..

(To find out Net Profit earned / Net Loss suffered during the year)

b) **Profit & Loss Appropriation A/c** for the year ended ……..

(It is an extention of Profit & Loss A/c.

It shows distribution of Net Profit amongst the partners)

[**1)** & **2)** collectively are called Income Statement and are prepared to know **Financial Performance** during the year]

3) **Balance Sheet** as on ……..

(To know **Financial Position** i.e. Assets, Liabilities & Capital as on the date)

^ **Try Yourself : Objectives**

* **True and False**

1 In absence of any agreement partners share profits of the business in the ratio of their capital contribution.

2 Profit sharing ratio and capital contribution ratio need not be same.

3 Every partnership firm must register itself with Registrar of firms.

4 A partner can advance loan to the partnership firm in addition to capital contributed by him.

5 A partner can demand interest on capital even if it is not provided in the partnership deed.

6 If a partner does not take part in day to day business activities of the firm then he is not entitled to any share of profit.

7 Interest should be paid @ 6% p.a. on partners' loan even if it is not provided in the partnership deed.

8 Husband and wife cannot be partners in the same firm.

9 One senior partner is Principal and other partners are his agents.

10 Partners are the agents of the firm and each other.

Answers:

1 **False**

In absence of any agreement, partners share profits equally and not in capital contribution ratio.

2 **True**

Profit sharing can be different from the that of the capital introduced by each of the partner. Not necessary that partner contributing more capital should have a higher profit sharing ratio and vice versa.

3 **False**

Registration of firms is not compulsory under Indian Partnership Act, 1932.

4 **True**

Where the partnership deed is absent, then the interest shall be paid at 6% per annum. So the interest on the loan to be paid to the partner.

5 **False**

Interest on capital can be paid only if it is provided in the partnership deed.

6	**False**
	Every partner need not take part in the business. Even if a partner does not take part in the business he is entitled for his share of profit.
7	**True**
	In absence of Partnership deed, Interest at the rate of 6% p.a. is to be allowed on a partner's loan to the firm.
8	**False**
	Husband and wife can be partners in the same firm.
9	**False**
	There is no senior or junior partner. Every partner is agent/principal of other partners.
10	**True**
	Concept of agency applies to every partner and the firm as well. So each partner is a principal to and agent of every other partner and to the firm.
*	**Multiple Choice Questions**
1	If a firm prefers Partners' Capital Accounts to be shown at the amount introduced by the partners as capital in firm then entries for salary, interest, drawings, interest on capital and drawings and profits are made in
	(a) Trading Account
	(b) Profit and Loss Account
	(c) Partners' Current Account
2	In the absence of any agreement, partners are liable to receive interest on their Loans @
	(a) 12% p.a. (b) 10% p.a. (c) 6% p.a.
3	The relationship between persons who have agreed to share the profit of a business carried on by all or any of them acting for all is known as ……
	(a) Partnership. (b) Joint Venture (c) Association of Persons.
4	Firm has earned exceptionally high profits from a contract which will not be renewed.
	In such a case the profit from this contract will not be included in ……
	(a) Profit sharing of the partners.
	(b) Calculation of the goodwill.
	(c) Both.

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5	In the absence of an agreement, partners are entitled to
	(a) Interest on Loan and Advances.
	(b) Commission.
	(c) Salary.
6	Partners are supposed to pay interest on drawings only when …… by the ……
	(a) Provided, Agreement. (b) Agreed, Partners (c) Both (a) & (b) above.
7	When a partner is given a guarantee by the other partner, loss on such guarantee will be borne by
	(a) Partner who gave the guarantee
	(b) All the other partners.
	(c) Partnership firm.
8	A, B and C had capitals of ₹ 50,000; ₹ 40,000 and ₹ 30,000 respectively for carrying on business in partnership. The firm's reported profit for the year was ₹ 80,000. As per provisions of the Indian Partnership Act, 1932, find out the share of each partner in the above amount after taking into account that no interest has been provided on an advance by A of ₹ 20,000, in addition to his capital contribution.
	(a) ₹ 26,267 for Partner B and C & ₹ 27,466 for partner A.
	(b) ₹ 26,667 each partner.
	(c) ₹ 33,333 for A, ₹ 26,667 for B and ₹ 20,000 for C.
9	X, Y and Z are partners in a firm. At the time of division of profit for the year there was dispute between the partners. Profits before interest on partner's capital was ₹ 6,000 and X wanted interest on capital @ 20% as his capital contributions was ₹ 1,00,000 as compared to that of Y and Z which was ₹ 75,000 and ₹ 50,000 respectively.
	(a) Profits of ₹ 6,000 will be distributed equally with no interest on either Capital.
	(b) X will get the interest of ₹ 20,000 and the loss of ₹ 14,000 will be shared equally.
	(c) All the partners will get interest on capital and the loss of ₹ 39,000 will be shared equally.
10	X, Y and Z are partners in a firm. At the time of division of profit for the year there was dispute between the partners. Profits before interest on partner's capital was ₹ 6,000 and Y determined interest @ 24% p.a. on his loan of ₹ 80,000. There was no agreement on this point. Calculate the amount payable to X, Y and Z respectively.
	(a) ₹ 2,000 to each partner
	(b) Loss of ₹ 4,400 for X & Z and Y will take home ₹ 14,800.
	(c) ₹ 400 for X, ₹ 5,200 for Y and ₹ 400 for Z.

11 X, Y and Z are partners in a firm. At the time of division of profit for the year there was dispute between the partners. Profits before interest on partner's capital was ₹ 6,000 and Z demanded minimum profit of ₹ 5,000 as his financial position was not good. However, there was no written agreement. Profits to be distributed to X, Y and Z will be

(a) Other partners will pay Z the minimum profit and will suffer loss equally.

(b) Other partners will pay Z the minimum profit and will suffer loss in capital ratio.

(c) ₹ 2,000 to each of the partners.

Answers:

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

^ **Theory questions**

1 Write short notes on:

(a) Features of Partnership

(b) Powers of Partners

2 Distinguish between fixed capital and fluctuating capital.

3 What are the liabilities of designated partners in case of LLP.

Answers:

1 **(a)** The following four essential features of a partnership, namely:

(i) Partnership is the result of an agreement: It means that the relation of partnership arises from contract and not from status.

(ii) Business: A partnership can exist only in business.

(iii) Sharing of profit: The persons concerned must agree to share the profits of the business.

(iv) Mutual agency: It means that the business is to be carried on by all or any of them acting for all. Thus, if the person carrying on the business acts not only for himself but for others also so that they stand in the positions of principals and agents, they are partners.

(b) Powers of partners are the following:

(i) Buying and selling of goods;

(ii) Receiving payments on behalf of the firm and giving valid receipt;

(iii) Drawing cheques and drawing, accepting and endorsing bills of exchange and promissory notes in the name of the firm;

(iv) Borrowing money on behalf of the firm with or without pledging the inventories-in-trade;

(v) Engaging servants for the business of the firm.

2	In fixed capital method, generally initial capital contributions by the partners are credited to partners' capital accounts and all subsequent transactions and events are dealt with through current accounts, Unless a decision is taken to change it, initial capital account balance is not changed. In fluctuating capital method, no current account is maintained. All such transactions & events are passed through capital accounts. Naturally, capital account balance of the partners fluctuates every time. So in fixed capital method a fixed capital balance is maintained over a period of time while in fluctuating capital method capital account balances fluctuates all the time.
3	As per LLP Act, unless expressly provided otherwise in this Act, a designated partner should be- (a) responsible for the doing of all acts, matters, and things as are required to be done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement, and the like report pursuant to the provisions of this Act and as may be specified in the limited liability partnership agreement; and. (b) liable to all penalties imposed on the limited liability partnership for any contravention of those provisions.

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357/400

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347



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346



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344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



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302



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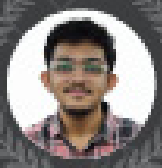
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328



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325



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319



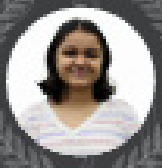
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316



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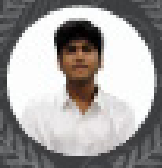
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313



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311



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308



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305



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MANAN SHAH
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AIR 8



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SCAN ME!

^ **Introduction**

* Goodwill is **reputation** of business **expressed in terms** of money.

* If a firm is **expected to earn** more profits in future (super profits) **than** normal profits due to efforts made by the existing (old) partners in past, it is said to have **Goodwill**.
The goodwill so generated is called **self- generated goodwill** .

It is the goodwill which is **not purchased** for a consideration.

It is earned / internally created by the consistent efforts of the old partners over long period of time, due to which business firm is **able to earn** higher profits than normal.

* Goodwill is an **Intangible Asset**.
Though it can not be touched, can not be seen, can not be transported physically, it is very much **Real Asset** since it has monetary / saleable value.

* **Super profits** implies excess profits earned by the firm over and above normal profits earned by similar firms in the same locality.
It is **future capability** of the business to earn more profit **than the** normal profit.
It may be **due to** locational advantage, quality of goods sold, personal reputation of owners / partners to attract more customers, better customer service, presence of managerial skill, possession of special contracts to get quality materials at cheaper prices etc.

* **Features / Characteristics of Goodwill**

1. Goodwill is an **intangible asset** i.e. an asset which cannot be touched or seen.

2. Though it cannot be touched or seen, it is a **Real Asset** (not fictitious asset), since it can be sold off in future and converted into money or moneys worth.
However, (generally) Goodwill cannot be sold in isolation as it does not have an existence separate from that of an enterprise (business firm).
Hence, it can be sold / generally have realisable value when the business firm is sold.

3. It comes into existence **due to various factors** like efficient management, favourable location, consistently good quality of goods &/or services etc.

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4. Goodwill helps the firm **to earn higher profits** as compared to new / other firms in the same line of business. Strictly, there is no goodwill, if firm is able to earn the same profits as other similar firms.

5. Value of goodwill is **subjective**. It depends upon the purpose of valuation and judgement / assessment of the Valuer. Value of goodwill is **not constant** throughout the life of the business. It fluctuates with the change in the fortunes of the firm.

^ **Situations**, which may involve valuation of goodwill in case of **Partnership Firms**

(Need for valuation of Goodwill)

The following are the **situations warranting valuation** of Goodwill in case of partnership firms

1. When there is a change in PSR (Profit Sharing Ratio) amongst the partners
2. When a new partner is admitted.
3. When an existing partner retires **or** dies.

In all the above cases, there is change in P.S.R. amongst the partners in future, due to which one or more partner sacrifices and one or more partners **gains**.
Hence, gaining partners **will have to compensate** sacrifing partners for Goodwill.

4. When partnership firm is dissolved / sold as a going concern
5. When there is amalgamation of two or more firms
6. When a partnership firm is converted into a company

^ **Steps** to be followed for **Valuation** of Goodwill

Valuation based on F.M.P.

I Calculation of Future Maintainable Profit (FMP)
** Valuation of Goodwill based on F.M.P.

Valuation based on Super Profit

I Calculation of Future Maintainable Profit (FMP)
II Calculation of Normal Profit
III Calculation of Super Profit
** Valuation of Goodwill based on Super Profit

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I Calculation of Future **M**aintainable **P**rofit (FMP)

* FMP is **estimated** normal business profits **expected to be earned in future**.

* Such estimation of future maintainable profit is **based on** profits of past few years, **adjusted for** known changes in future.

* Profits of each of the past few years (eg. 3 years) is adjusted as follows

		Past years	1	2	3
		Profits as given	**xxx**	**xxx**	**xxx**
		(Rectification of errors)			
i)		Purchase of machinery debited to purchases			
		Depreciation on machinery, yet not provided			
ii)		Repairs to car debited to vehicles			
		Depreciation on repairs to car wrongly capitalised			
iii)		Under valuation of closing stock			
		Under valuation of opening stock			
iv)		Over valuation of closing stock			
		Over valuation of opening stock			
v)		IOC, salary to partner etc. yet not provided			
		IOD yet not provided			
		(Adjust for known changes in future)			
i)		Non recurring expenses, Non operating expenses,			
		Abnormal losses etc **incurred in past**,			
		not expected to be incurred in future			
		eg. Loss by fire / theft, Loss on sale of FA etc			
ii)		Non recurring Incomes, Non operating incomes,			
		Abnormal gains **earned in past**,			
		not expected to be earned in future			
		eg. Profit on sale of FA / Invt.s etc			
iii)		Expenses, **not incurred in past,**			
		expected to be incurred in future			
iv)		Incomes, **not earned in past,**			
		expected to be earned in future			
		Adjusted Profits	**xxx**	**xxx**	**xxx**

FMP **= Average** adjusted profits of past few years

Such **average** can be **simple / normal** average or **weighted** average

Simple average is suitable when there is **no clear trend** in past years profits, in which case equal weight is given to profits of each past year

If there is noticeable **clear trend** in past profits, then **weighted average** may be used **assigning** more weight to the profit of recent year as it indicates the most likely profits in future.

** Valuation of Goodwill **based on F.M.P.**

This method is **based on the assumption** that a newly started business will not earn any profit during the initial years of its operations.

Hence, one who purchases a running business or becomes a partner in existing business pays for goodwill for being in a position to earn profit in the initial years of business.

* **Method 1 : Number of Years of Purchase Method**

Number of years of purchase **means** the number of years for which the firm is likely to earn same amount of profit because of efforts put in the past.

Goodwill = Number of years of purchase * FMP

^ **Q. 1 :** Cu and Au were in partnership sharing profits and losses in the ratio 5:3.

On 1st April 2022, they decided to admit Ag the partnership on the following terms:

1. Ag will bring ₹ 2,00,000/- as capital for ¼ share.
2. New profit sharing ratio shall be 2:1:1 among Cu, Au and Ag.
3. Cu was entitled to salary of ₹ 2,000/- p.m., it was revised to ₹ 3,000 p.m. from 1st October 2020.
4. Interest on capital was paid at 8% p.a.
5. Capitals as on 31st March 2022 were Cu ₹ 4,00,000 Au ₹ 3,00,000, which had remained unchanged since last four years.
6. Goodwill was to be valued on the basis of 3 years purchase of average adjusted weighted average profits of past 4 years. The profits of previous four years, before charging interest on capital and salary to Cu were as follows:

Year	Profit
2018-19	2,10,000
2019-20	2,60,000
2020-21	2,10,000
2021-22	3,05,000

These profits were subject to following rectification

(a) A machine costing ₹ 40,000 purchased on 1st October, 2020 was wrongly charged to revenue. The machinery was depreciated at 20% p.a. on written down value method

(b) Stock on 31st March 2020 was over valued by ₹ 20,000.

(c) There was a loss by fire amounting to ₹ 10,000/- in the year 2018-19 which was not considered in trading account but correctly debited in the Profit & Loss a/c for that year.

(d) Debtors as on 31st March 2022 included bad debts of ₹ 5,800/-

7. Ag shall bring his share of goodwill in cash.

You are required to calculate amount of goodwill Ag is supposed to bring.

*

Ratio's	5 : 3	2 : 1 : 1		
			Sacrifice	**Gain**
	Old Share	**New Share**	**(Old - New)**	**(New - Old)**
Cu				
Au				
Ag				

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^ **Q. 2 :** Antoo, Bantoo and Chintoo were in partnership sharing profits and losses 3:4:3 respectively. The accounts of the firm are made up to 31st March every year. The partnership provided, interalia, that: On the retirement of a partner the goodwill was to be valued at three years' purchase of average profits of the past four years upto the date of the retirement after deducting interest @12%p.a. on capital employed and remuneration of ₹ 2,000 p.m. to each partner. On 1st April 2022, Antoo retired & it was agreed on his retirement to adjust goodwill in the capital accounts without showing any amount of goodwill in the Balance Sheet. It was agreed that the capital employed would be ₹ 6,50,000. Bantoo and Chintoo were to continue the partnership, sharing profits and losses equally after the retirement of Antoo. The following were the amounts of profits of earlier years before charging salary to partners and interest on capital employed.

Year	Profit
2018-19	2,60,000
2019-20	2,75,000
2020-21	2,65,000
2021-22	2,80,000

You are required to compute the value of goodwill.

^ **Q. 3 :** Wise, Clever & Dull were trading in partnership sharing profits and losses 4:3:3 respectively. The accounts of the firm are made upto 31st December every year.
The partnership provided, interalia, that:
On the death of a partner the goodwill was to be valued at three years' purchase of average profits of the three years upto the date of the death after deducting interest @ 8 percent on capital employed and a fair remuneration of each partner. The profits are assumed to be earned evenly throughout the year.
On 30th June, 2022, Wise died and it was agreed on his death to adjust goodwill in the capital accounts without showing any amount of goodwill in the Balance Sheet.
It was agreed for the purpose of valuation of goodwill that the fair remuneration for work done by each partner would be ₹15,000 per annum and that the capital employed would be ₹ 1,56,000. Clever and Dull were to continue the partnership, sharing profits and losses equally after the death of Wise.
The following were the amounts of profits of earlier years before charging interest on capital employed.

2019	67,200
2020	75,600
2021	72,000
2022	62,400

You are required to compute the value of goodwill.

II **Calculation of Normal Profit**

Normal Profit = NRR x Capital Employed
100

a. Capital Employed

Capital employed means capital invested in the firm to carry on the business.

If Opening C.E. is given, Average C.E. = (Op. C.E + Cl. C.E.)
2

b. Normal Rate of Return (NRR)

It is the rate at which profit is earned by similar business entities in the industry under normal circumstances. It is usually given in the problem.

c. Normal Profit = NRR x Capital Employed
100

III **Calculation of Super Profit**

Super Profits are excess (surplus) profit expected to be earned by a firm, in comparision to average profit normally earned by other comparable firms.

Super Profit = FMP - Normal Profit

IV Valuation of Goodwill **based on Super Profit**

* **Method 1 : Number of Years of Purchase Method**

Goodwill = Number of years of purchase * Super Profit

^ **Q. 4 :** The following particulars are available in respect of business carried on by Rathore

			(₹)
(1)	Capital Invested		1,50,000
(2)	Trading Results:		
	2019	Profit	40,000
	2020	Profit	36,000
	2021	Loss	6,000
	2022	Profit	50,000
(3)	Market Rate of interest on investment	10%	
(4)	Rate of risk return on capital invested in business	2%	
(5)	Remuneration from alternative		
	employment of the proprietor	₹ 6,000	
	(if not engaged in business)	per annum	

You are required to compute the value of goodwill on the basis of 5 years purchase of super profit of the business calculated on the average profits of the last four years.

* **Method 2 : Capitalisation Method**

When super profits are expected to earn for many more number of years in future because of the efforts put in the past, this method may be followed.

$$\text{Goodwill} = \frac{\text{Super Profit}}{\text{NRR}} \times 100$$

OR

$$\text{Goodwill} = \frac{\text{FMP}}{\text{NRR}} \times 100 - \text{Capital Employed}$$

(Total capitalised value of the business / firm **Less** Capital employed)

^ **Q. 5 :** The net tangible assets of a firm are worth ₹ 4,10,000 and the average profit of last four years amounts to ₹ 60,000. Find out the value of Goodwill under capitalisation method if the reasonable return on capital invested is 12%.

* **Method 3 : Annuity Method**

The **major drawback** of number of years of purchase method **is that time value of money** is not considered.

Hence, discounted value of super profits for certain no of years is considered for calculating value of Goodwill under Annuity Method.

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^ **Q. 6 :** Calculate the goodwill by annuity method of super profit from the following facts.

a) Annual maintainable profit after tax ₹ 65,000

b) Capital employed is ₹ 4,00,000

c) Normal rate of return is expected at 12% p.a.

d) Present value of an annuity of Rs. 1 for five years @ 12% interest is 3.604776.

Also find out the value of goodwill under capitalisation method.

^ **Q. 7 :** Lee and Lawson are in equal partnership. They agreed to take Hicks as one-fourth partner. For this it was decided to find out the value of goodwill. M/s. Lee and Lawson earned profits during 2019-2022 as follows:

Year	Profits (₹)
2019	1,20,000
2020	1,25,000
2021	1,30,000
2022	1,50,000

On 31.12.2022 capital employed by M/s. Lee and Lawson was ₹ 5,00,000.

Rate of normal profit is 20%.

Required

Find out the value of goodwill following various methods.

Write assumptions clearly wherever required.

^ **Accounting Treatment of Goodwill**

Goodwill is of two types

1. Self - generated Goodwill (non-purchased goodwill)

2. Purchased Goodwill

* **Self generated or Internally generated or Inherent Goodwill**

It is the goodwill which is not purchased for a consideration.

It is earned / internally created by the consistent efforts of the management over long period of time, due to which business firm is able to earn higher profits than normal.

* Recommendation of Accounting Standard

Accounting Standards require an enterprise to recognize an intangible asset, only **if and only if,** certain conditions are satisfied, namely:

(i) An intangible asset must have the **characteristics of an asset.** It means that it must have some value and must be clearly identifiable, so that it can be sold without disposing other assets or future benefits flowing from other assets.

(ii) An intangible asset should be recognized only if the **future probable economic** benefits (i.e., increased revenue from sales) will flow to the business enterprise and not to others. It means that management can make reasonable estimates of future benefits.

(iii) The cost of the intangible asset can **be measured reliably**, that is, the cost is objectively verifiable. If the cost cannot be measured reliably, then it cannot be recognized as an asset.

It is thus clear that none of the conditions is satisfied by internally generated goodwill or inherent goodwill. The reasons are simple to explain. **First,** it is not an identifiable resource like patent, trademark or copyright. **Second**, it is very difficult to assess its future benefits. **Finally,** the cost of internally generated goodwill cannot be reliably measured in the absence of any consideration in money or money' worth. There is no documentary evidence to support the value of goodwill as a resource.

Goodwill should be recorded in the books only when some consideration in money or money' worth has been paid for it. Accordingly, on admission **or** retirement/death of a partner **or** even when there is a change in profit sharing ratio amongst the existing partners, goodwill should not be raised in the books of account of the partnership firm because no consideration in money or money' worth has been paid for it.
The conclusion is that only purchased goodwill should be recorded in the books of account whether the payment is made directly in cash or money' worth.

Hence, **As per Accounting Standards,**
Self-generated goodwill is not recognised / **cannot be recorded** as an asset in the books of accounts because consideration in terms of money or moneys worth is not paid for acquiring such goodwill.
Its valuation is subjective assessment of the valuer, being not based on the evidence.
True cost of such goodwill cannot be reliably measured.

* **Purchased Goodwill**

* It is that goodwill which is acquired / purchased by a firm for a consideration, such consideration can be paid in cash &/or in kind.
* Goodwill can be purchased at the time of purchase of running business of some other firm. Such purchase of running business will consist of takeover of other assets and liabilities of other firm along with purchase of goodwill.
* Value of goodwill is determined at a price as agreed between the buyer and seller.

* **AS 26** prescribes that purchased goodwill may be recognised / **recorded** in the books of accounts since consideration is paid for the same. It is shown as an **Asset** in the Balance sheet. It is to be amortised / written-off at the earliest, **but not later than** its estimated useful life.

Ex. : A and B purchase the net assets (assets minus liabilities) of C amounting to ₹ 2,50,000 for ₹ 3,00,000 which is paid in cash. In such case, additional payment made for ₹ 50,000 is said to be paid for goodwill. It is a case of purchased goodwill (an asset) and can be validly recorded as asset in the books of A and B.

* **Accounting treatment of Goodwill**

1. When there is a change in PSR (Profit Sharing Ratio) amongst the partners
2. When a new partner is admitted.
3. When an existing partner retires **or** dies.

In all the above cases, there is change in P.S.R. amongst the partners in future, due to which one or more partner sacrifices and one or more partners **gains**.
Hence, gaining partners **will have to compensate** sacrifing partners for Goodwill.
However,
since such internally generated goodwill cannot be raised / recorded in the B.O.A., adjustment for such goodwill **should be made** directly through **Partners Capital A/c's**, **without** raising the goodwill or bringing such goodwill in books of accounts.

Sacricing Partners should be allowed / given their **share** in Total Goodwill of firm and **Gaining Partners** should be charged for their **share** in Total Goodwill of firm

Accordingly, **Journal Entry** for the same will be as follows :

Note : Old Goodwill, if any, appearing in Balance sheet should be **written off** immediately amongst **Old** Partners in **Old** Ratio **(O O)**

^ **Q. 8 :** What will be the journal entry for Goodwill in :
a) Q. 1 (Cu, Au & Ag)
b) Q. 2 (Antoo, Bantoo and Chintoo)
c) Q. 3 (Wise, Clever and Dull)

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^ **Q. 9 :**

a) A, B & C are equal partners. They wanted to change the P.S.R. into 4:3:2. Goodwill of the firm is valued at ₹ 90,000. Make the necessary journal entries.

b) A, B and C are in partnership sharing profits & losses in the ratio of 4:3:3. They decided to change the profit sharing ratio to 7:7:6. Goodwill of the firm is valued at ₹20,000. Calculate the sacrifce / gain by the partners and make the necessary journal entry.

c) A, B, C & D are in partnership sharing profits and losses equally. They mutually agreed to change the P.S.R. to 3:3:2:2. Goodwill of the firm is valued at ₹ 20,000. Give necessary journal entry.

d) M, K & B are in partnership sharing profits and losses as 2/5 th, 3/10 th and 3/10 th. K retired. M and B will share future profits and losses of the new firm in the ratio 1:2. Goodwill of the firm is valued at ₹36,000. Give necessary journal entry.

^ **Q. 10 :**

A, B & C are sharing profits and losses in the ratio 5:3:2. Calculate new profit sharing ratio and sacrificing ratio in following case.
A, B and C decide that the future P.S.R. between B and C shall be the same as existing between A and B.

^ **Q. 11 :**

Nigam and Dhameja are in partnership sharing profits and losses equally. They agreed to take Ghosh as one third partner. The new profit sharing ratio will be 4:2:3. Goodwill of the firm is valued at ₹ 27,000. Pass necessary journal entry.

^	**Try Yourself : Objectives**
*	**True and False**
1	Goodwill is intangible asset therefore it cannot be valued.
2	Goodwill is valued whenever there is change in the profit sharing ratio among the partners.
3	Goodwill is the value of reputation of a firm in respect of profits expected in future over and above the normal rate of profits.
4	At the time of admission or retirement of a partner, goodwill can be raised in the books of accounts and shown as an asset.
5	Only simple average method can be used for valuation of goodwill.
6	Super profit means excess of actual average profit over normal profit.
7	Normal profit means profit earned by similar companies in the same industry.
8	Normal profit depends upon Normal Rate of Return and past profits.
9	At the time of admission/retirement of a partner, since goodwill can not be raised in the books of accounts is recorded through capital accounts of the partners.
10	At the time of admission of a partner, goodwill brought in by the new partner is shared equally by old partners.
	Answers:
1	**False**
	Even though Goodwill is intangible asset, it can be valued in terms of money.
2	**True**
	Goodwill has to be valued every time whenever there is a reconstitution.
3	**True**
	Goodwill is the brand image the firm has in the market due to which it enjoys an advantageous position over the other players in the market.
4	**False**
	At the time of admission or retirement of a partner, goodwill should not be raised in the books of account of partnership firm because no consideration in money or money worth has been paid for it.
5	**False**
	Weighted average profit method, capitalisation method, super profits methods also can be used for valuation of Goodwill.

6	**True**
	Super profit means excess profit that can be earned by the firm over and above the normal profit usually earned by similar firms under similar circumstances.
7	**True**
	The rate of return is considered as an average for the industry, which is applied to the capital employed in the concerned firm.
8	**False**
	Normal profit depends upon Normal rate of return only and not on past profits.
9	**True**
	Generally, the goodwill at the time of admission is adjusted through the capital accounts and not shown in the books of the firm.
10	**False**
	Goodwill brought in by new partner is shared by old partners in sacrificing ratio and not equally.
*	**Multiple Choice Questions**
1	Goodwill brought in by incoming partner in cash for joining in a partnership firm is taken away by the old partners in their……ratio.
	(a) Capital (b) New Profit Sharing (c) Sacrificing
2	A & B are partners sharing profits and losses in the ratio 5:3. On admission, C brings ₹ 70,000 cash and ₹ 48,000 against goodwill. New profit sharing ratio between A, B and C are 7:5:4. Find the sacrificing ratio of A:B.
	(a) 3:1. (b) 4:7. (c) 5:4.
3	Following are the factors affecting goodwill except:
	(a) Nature of business.
	(b) Efficiency of management.
	(c) Location of the customers.
4	Weighted average method of calculating goodwill should be followed when:
	(a) Profits has increasing trend.
	(b) Profits has decreasing trend.
	(c) Either 'a' or 'b'.

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5	In the absence of any provision in the partnership agreement, profits and losses are shared
	(a) In the ratio of capitals.
	(b) Equally.
	(c) In the ratio of loans given by them to the partnership firm.
6	The profits and losses for the last 4 years are 2018-19 Losses ₹ 10,000; 2019-20 Losses ₹ 2,500; 2020-21 Profits ₹ 98,000 & 2021-22 Profits ₹ 76,000. The average capital employed in the business is ₹ 2,00,000. The rate of interest expected from capital invested is 12%.
	The remuneration of partners is estimated to be ₹ 1,000 per month not charged in the above losses/profits. Calculate the value of goodwill on the basis of two years purchase of super profits based on the average of four years.
	(a) ₹ 9,000. (b) ₹ 8,750. (c) ₹ 8,250.
7	A, B and C are partners sharing profits and losses in the ratio 3:2:1. They decide to change their profit sharing ratio to 2:2:1. To give effect to this new profit sharing ratio they decide to value the goodwill at ₹ 30,000. Pass the necessary journal entry if Goodwill not appearing in the old balance sheet and should not appear in the new balance sheet.
	(a) B's Capital Account Dr. ₹ 2,000
	C's Capital Account Dr. ₹ 1,000
	To A's Capital Account ₹ 3,000
	(b) Goodwill Account Dr. ₹ 30,000
	To A's Capital Account ₹ 15,000
	To B's Capital Account ₹ 10,000
	To C's Capital Account ₹ 5,000
	(c) A's Capital Account Dr. ₹ 12,000
	B's Capital Account Dr. ₹ 12,000
	C's Capital Account Dr. ₹ 6,000
	To Goodwill Account ₹ 30,000

Answers:

1. Sacrificing
2. 3:1
3. Location of the customers
4. Either 'a' or 'b'
5. Equally
6. Rs. 8,750
7. B's Capital Account Dr. ₹ 2,000
C's Capital Account Dr. ₹ 1,000
To A's Capital Account ₹ 3,000

^ **Theory questions**

1 Write short note on methods for valuation of goodwill.
2 Explain Accounting treatment of goodwill in case of change in profit sharing ratio.
3 Distinguish between Super profit basis and Capitalisation Basis.

Answers:

1 Methods for Valuation of Goodwill of Firm / Business
1) No. of Years of Purchase Method **2)** Capitalisation Method **3)** Annuity Method
In above methods, Goodwill can be valued :
based on Future Maintainable Profits (F.M.P.)
(Simple Average Profits **or** Weighted Average Profits) **or** based on Super Profits
(Write short note on each method from theory notes already given in the chapter)

2 In case of change in profit sharing ratio, the value of goodwill should be determined and preferably adjusted through capital accounts of the partners on the basis of profit sacrificing ratio & gain ratio.

3 **Super Profit Basis:** In case of average profit basis, goodwill is calculated on the basis of average profit multiplied by certain number of years.
Super Profit = Actual Profit - Normal Profit
Actual Profit is average profit and Normal Profit = Normal rate of Return (NRR) * C.E.

Capitalization Basis: Under this basis, value of whole business is determined applying normal rate of return. If such value (arrived at by applying normal rate of return) is higher than the capital employed in the business, then the difference is goodwill.

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TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



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301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

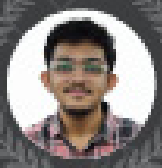
Toppers CA Foundation

June 22 & June 23



340/400

HARSH GULWANI
CA Foundation June'22



MEET SHAH
CA Foundation June'23
331



NISHIT KAPUR
CA Foundation June'23
328



PALAK JAJODIA
CA Foundation June'23
325



SWASTIKA SINGH
CA Foundation June'22
323



SUKUNJ GUPTA
CA Foundation June'22
323



DURGASHRI VS
CA Foundation June'22
319



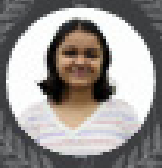
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CA Foundation June'22
319



KARTIK LADHANI
CA Foundation June'22
316



RIDHI PAREKH
CA Foundation Dec'22
314



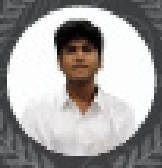
SMEET LADHANI
CA Foundation June'23
313



TANMAY AGARWAL
CA Foundation June'23
311



GARV KHANDELWAL
CA Foundation June'22
308



DAKSH JAIN
CA Foundation June'23
308



DEEPAK GURNANI
CA Foundation June'22
305



PARIDHI JHAWAR
CA Foundation June'22
304



SATYA BHANUSHALI
CA Foundation June'23
304

and many more...

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JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
CA INTER MAY'23
AIR 34



HIMANSHI DHAIJEE
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AIR 39



YUKTA SATPALKAR
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AIR 40



MARVI LODHA
CA INTER MAY'23
AIR 40



ARMAN HOSANGADY
CA INTER MAY'22
AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MEHDIRATTA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

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SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHABRIA
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AIR 32



PINAL KHETAN
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AIR 35



SHOURYA TIBREWALA
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AIR 39



DEEPAK LADHA
CA FINAL NOV'23
AIR 40



HIMANSHU KHATRI
CA FINAL MAY'22
AIR 41



SHRAVAN MUNDRA
CA FINAL NOV'23
AIR 45



DEEPTHI PACHIPULUSU
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AIR 46



SHREY AGARWAL
CA FINAL MAY'22
AIR 48

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ANDHERI (E)
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GHATKOPAR (W)
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KALYAN (E)
101,Shivdarshan Apts, Near Kalyan Janta Sahakari Bank, Durga Mata Mandir Road,Kolsewadi, Kalyan (East)
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KALYAN (W)
212, Shreeji Solitaire, Khadakpada Circle, Above Bikaner, Kalyan (W)
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CHEMBUR (E)
19, Sunil Sadan, 3rd Floor, Central Avenue Road, Opp.of Grand Central Hotel, Above Monginis OR Yewle Tea, Chembur(E) - 400071
Ph. : 9870 780 524

AJMER
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Ph.: 8890 774 877

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Ph. : 9001 390 017

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SCAN ME!

^ **Introduction**

Admission of a Partner **means** a new partner is admitted in the firm for the benefit of the partnership firm.

* A person can be admitted as a new partner **either** as per the terms of partnership deed **or** only with the consent of all existing partners.

* Admission of a partner is a **mode of reconstituting the firm**

under which

old partnership relation comes to an end

and

new partnership relation amongst all the partners including **Incoming (newly admitted) partner** begins.

However, **Partnership firm** continues, **DOES NOT** get dissolved.

* A new partner can be admitted in the firm for **one or more reasons** like more capital requirement, expansion of business, special skill possessed by incoming partner, strengthening the management of the firm etc.

^ **Q. 1 :**

Calculate Missing ratios in each of the following.

a) A and B are partners sharing profits in the ratio 3:2. They admit C as the new partner. A surrenders 1/3 rd of his share and B surrenders 2/3 rd of his share in favour of C.

b) A and B are partners sharing profits in the ratio 3:2. They admit C as a new partner for 1/3 rd share in future profits which he gets 1/9 from A and 2/9 from B.

c) A and B are partners sharing profits in the ratio 3:2. They admit C as a new partner for 1/3 rd share in future profits.

^ **Usually given**

1. Balance Sheet of the firm before the admission of a partner

2. Other Relevant details / information

Usually required

1. Pass Journal entries **& / or** Prepare relevant Ledger accounts

2. Balance Sheet of the firm after the admission of a partner

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^ Admission of Partner : **'Standard Format'** per solution **(Ledger Accounts)**

Page 1	Revaluation A/c (**or** Profit & Loss Adjustment A/c)	half page
	Partners Capital A/c's	half page
Page 2	Balance Sheet of the firm after the admission	15 to 18 lines
	Bank A/c **or** Cash A/c	balance page
Page 3	blank page for workings / notes	full page

^ **Summary** of Steps to be followed

I	Calculate **Missing Ratio's** and Write **Opening balances** in Ledger Accounts
	(Accounts prepared as asked **or** prepared in working notes)
II	**Distribute** Reserves and **Write off** Accumulated Losses **(O O)**
	(even if problem is silent on this matter)
III	Record **Revaluation** of Assets (excluding Goodwill) & Reassessment of Liabilities
	(**including recording** unrecorded assets and liabilities)
	Note :
	Final Profit or Loss to be distributed amongst **Old** Partners in **Old** Ratio **(O O)**
IV	Record **Capital brought in** by newly admitted partner
V	Adjustment / Treatment of **Goodwill**
VI	Record **Sundry Other Transactions**, if any
VII	Adjustment of **Partners Capitals in New Ratio**, as specified in the problem
VIII	**Closing Steps**

^ **Q. 1 :** Alpha and Beeta were partners in a LLP namely Meta-Chem LLP sharing profits and losses equally.

Balance Sheet of Meta-Chem LLP as on 31st March, 2022

Liabilities	(₹)	Assets	(₹)
Capital :		Factory Building	4,78,000
Alpha 3,00,000		Plant & Machinery	3,41,000
Beeta 2,00,000	5,00,000	Office Furniture	55,850
General Reserve	1,80,000	Inventory	77,740
Workmen compensation fund	60,000	Trade Receivables	1,43,210
Term loan from IDFC bank	2,78,000	Bank	44,200
Trade payables	1,22,000		
	11,40,000		**11,40,000**

They agreed to admit Gyama as partner from 1st April 2022 on the following terms:

1. He shall have one-sixth share in future profits.
2. New profit sharing ratio would be 3:2:1

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3. He shall bring ₹ 2,50,000 as his capital.
4. Goodwill of the firm is valued at ₹ 3,00,000
5. Factory Building is to be appreciated by 20% and inventory is revalued at ₹ 70,000.
6. Machinery to be appreciated by 20% and Office furniture to be revalued at ₹ 50,000
7. Of the trade receivables ₹ 3,210 are bad and 5% be provided for bad & doubtful debts.
8. There is no actual liability towards workman.

You are required to prepare necessary a/c's and Balance sheet after admission.

Q. 2 : Gopal and Govind are partners sharing profits and losses in the ratio 60:40.

The firms balance sheet as on 31.03.2022 was as follows:

Liabilities	(₹)	Assets	(₹)
Capital accounts:		Fixed assets	3,00,000
Gopal	1,20,000	Investments	50,000
Govind	80,000	Current assets	2,00,000
Long term loan	2,00,000	Loans and advances	1,00,000
Current liabilities	2,50,000		
	6,50,000		**6,50,000**

Due to financial difficulties, they have decided to admit Guru as partner in the firm from 01.04.2022 on the following terms : Guru will be paid 40% of the profits.

Guru will bring in cash ₹ 1,00,000 as capital. It is agreed that goodwill of the firm will be valued at 2 years' purchase of 3 years' normal average profits of the firm and Guru will bring in cash his share of goodwill. It was also decided that the partners will not withdraw their share of goodwill nor will the goodwill appear in the books of account.

The profits of the previous three years were as follows:

For the year ended 31.3.2020: profit ₹ 20,000 (includes insurance claim received of ₹40,000).

For the year ended 31.3.2021: loss ₹ 80,000 (includes voluntary retirement compensation paid ₹ 1,10,000).

For the year ended 31.3.2022: profit of ₹ 1,05,000 (includes a profit of ₹ 25,000 on the sale of assets).

It was decided to revalue the assets on 31.03.2022 as follows:

	(₹)
Fixed assets (net)	4,00,000
Investments	Nil
Current assets	1,80,000
Loans and advances	1,00,000

The new profit sharing ratio after the admission of Guru was 35:25:40.

Show goodwill calculation and prepare revaluation account, partners' capital accounts and balance sheet as on 01.04.2022 after the admission of Guru.

** Adjustment of **Partners Capitals in N.R**, taking Incoming Partners Capital **as Base**

^ **Q. 3 :** The B / S of Adil and Sameer who share profits in ratio of 2:1 as on 31.03.18

Balance Sheet As on 31st March 2018

Liabilities	(₹)	Assets	(₹)
Capitals:		Land & Building	75,000
Adil	90,000	Investment	1,08,000
Sameer	48,600	Debtors	39,000
Investment Fluctuation		Goodwill	12,000
Reserve	15,000	Profit and Loss A/c	12,000
General Reserve	12,000	Advertisement Suspense	12,000
Sundry Creditors	63,000	Cash	30,600
Bills Payable	60,000		
	2,88,600		**2,88,600**

On 1.4.2018, Raju was admitted into partnership on the following terms :

1. Raju pays ₹ 30,000 as his capital for 1/4th share.
2. Raju pays ₹ 15,000 for Goodwill. Half of the sum is to be withdrawn by Adil & Sameer
3. RDD is created @ 10%.
4. The value of land and building is appreciated by ₹ 30,000.
5. Investments were reduced by ₹ 22,500.
6. Sundry creditors are to be valued at ₹ 62,250.
7. Capitals of Adil and Sameer to be adjusted taking Raju's capital as the base.
   Adjustment of capitals is to be made through cash.

Prepare Revaluation Account, Partner's Capital Account and Balance Sheet of the New Firm as on 1st April, 2018

** **When** Capital brought in by **Incoming Partner** is **NOT** given

^ **Q. 4 :** The Balances sheet of Bhavesh and Chandra who share profit and losses in the ratio of 3:1 as at 31st March 2018 was as under :

Balance Sheet As on 31st March, 2018

Liabilities	Amt (₹)	Assets		Amt (₹)
Creditors	20,000	Bank		20,000
Workmen's Compensation		Debtors	13,000	
Reserve	30,000	Less : Provision	1,000	12,000
General Reserve	24,000	Bills Receivable		10,000
Bhavesh's Capital	32,000	Stock		20,000
Chandra's Capital	28,000	Land & Building		30,000
		Goodwill		42,000
	1,34,000			**1,34,000**

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Alia was admitted on 1.4.2018 for 1/5th share on the following terms :

1. Alia shall bring ₹ 20,000 for her share of goodwill and necessary amount for her share of capital in cash.
2. Anju, an old customer whose account was written off as bad, has paid ₹ 400 in cash in full settlement of his dues.
3. The market value of Land and Building be taken as ₹ 40,000.
4. Workmen's Compensation Reserve is to be increased by ₹ 10,000.
5. Unaccounted Accrued Incomes of ₹ 200 to be accounted for.
6. The capitals of all partners are to be in new profit sharing ratio taking old partners total capital as base after adjustment. Actual cash is to be paid off or brought in by the partners for adjusting their capital accounts.

Prepare Revaluation Account, Partner's Capital Account and Balance Sheet after Alia's admission.

^ **Valuation of Goodwill, TYPICAL / Hidden or Inferred Goodwill**

When amount of Goodwill is **to be calculated** on the basis of an **Inferred Method**

i.e. Goodwill of the firm to be calculated **based on**

Capital brought in by an Incoming Partner and **his share** in future profits.

Steps for Calculation of Goodwill

I **Net Worth** including **Goodwill**

= Incoming partners capital * reciprocal of share of Incoming partner

eg. Incoming partner brings Rs. 60,000 as capital and his share in profits is 1/5 th

In such case, Total net worth of the firm = 60,000 * 5/1 = Rs. 3,00,000

II **Net worth** excluding **Goodwill**

= Agreed values of all real assets **Less** Agreed values of all outsiders liabilities

OR

= Capital of old partners + Reserves - Fictitious assets (accumulated losses)

+ / - Profit / Loss on Revaluation of Assets and Reassessment of Liabilities

Plus

Capital of Incoming Partner

III **Goodwill = I - II**

^ **Q. 5 :** A and B are partners in a firm, sharing profits and losses in the ratio of 3 : 2.

The Balance Sheet of A and B as on 1.1.2022 was as follows:

Liabilities		Amt. (₹)	Assets		Amt. (₹)
Trade payables		17,000	Building		26,000
			Furniture		5,800
Bank overdraft		9,000	Inventories		21,400
Capital accounts:			Trade receivables	35,000	
A	44,000		Less: Provision	(200)	34,800
B	36,000	80,000	Investment		2,500
			Cash		15,500
		1,06,000			**1,06,000**

'C' was admitted to the firm on the above date on the following terms:

(i) C is admitted for 1/6 share in the future profits and to introduce a capital of ₹ 25,000.

(ii) The new profit sharing ratio of A, B and C will be 3:2:1 respectively.

(iii) 'C' is unable to bring in cash for his share of goodwill, they decide to calculate goodwill on the basis of C's share in the profits and the capital contribution made by him to the firm.

(iv) Furniture is to be written down by ₹ 870 and Inventory to be depreciated by 5%. A provision is required for trade receivables @ 5% for bad debts. A provision would also be made for outstanding wages for ₹ 1,560. The value of buildings having appreciated be brought upto ₹ 29,200. The value of investments is increased by ₹450.

(v) It is found that the trade payables included a sum of ₹ 1,400, which is not to be paid off. Prepare Revaluation account & Partners' capital accounts.

^ When the **revised values are NOT TO BE recognised in the books**

i.e. when all the partners have decided to that **revalued figures** of assets & liabilities **are not to be shown** in the new Balance sheet, but they **should appear** at old values

The partners may decide that the values of assets and liabilities are not to change i.e. shall continue to appear in the books at their old values.

If it is so, they may decide to open **Memorandum Revaluation A/c**

^ **Q. 6 :** A and B are partners sharing profits and losses in the ratio of 3:2.

On 1.4.2022, they admit C on the following terms:

(1) C will bring ₹ 50,000 as a capital and ₹ 10,000 for goodwill for 1/5 share;

(2) Provision for doubtful debts is to be made on Trade receivables @ 2%

(3) Inventory to be written down by 10%.

(4) Freehold premises is to be revalued at ₹ 2,40,000, plant at ₹ 35,000, furniture ₹ 25,000 and office equipment ₹ 27,500.

(5) Partners agreed that the values of the assets and liabilities remain the same and, as such, there should not be any change in their book values as a result of the above mentioned adjustments.

Their Balance Sheet as on 31.3.2022 is given below:

Liabilities	Amt (₹)	Assets	Amt (₹)
Trade payables	50,000	Freehold premises	2,00,000
Capital Accounts:		Plant	40,000
A	2,00,000	Furniture	20,000
B	1,00,000	Office equipment	25,000
		Inventories	30,000
		Trade receivables	25,000
		Bank	10,000
	3,50,000		**3,50,000**

You are required to make necessary adjustment in the Capital Accounts of the partners and show the Balance Sheet of the New Firm.

^ **Q. 7 :** The following was the balance sheet of A, B and C who were equal partners on January 1, 2022

Liabilities	Amt (₹)	Assets	Amt (₹)
Bills Payable	3,000	Cash	1,000
Creditors	6,000	Debtors	10,000
Capital Accounts		Stock	12,000
A	20,000	Furniture	5,000
B	15,000	Buildings	25,000
C	10,000	Bills Receivable	1,000
	54,000		**54,000**

They agree to take D into partnership and give him a 1/4 share in the profits on the following terms:

(1) D should bring in ₹ 6,000 for goodwill and ₹ 10,000 as capital;

(2) one-half of the goodwill shall be withdrawn by old partners;

(3) stock and furniture be depreciated by 10%.

(4) a liability of ₹ 1,300 be created against bills discounted;

(5) the building be valued at ₹ 40,000;

(6) the values of liabilities and assets other than cash are not to be altered.

Give the necessary entries to give effect to the above arrangement; prepare revaluation account and opening balance sheet of the firm as newly constituted.

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^	**Try Yourself : Objectives :**
*	**True or False**
1	A newly admitted partner does not have same rights as old partners.
2	When a new partner is admitted, old partners have to forego certain share in profits of the firm, this is called as sacrifice ratio.
3	Revaluation account is also called as Profit and Loss Adjustment Account.
4	Any appreciation in the value of an asset is credited to Revaluation account.
5	All the partners may decide not to change the values of assets and liabilities in the books of accounts.
6	New partner is entitled to have share in reserves appearing in the balance sheet prior to his admission.
7	If revaluation account shows credit balance then it represents profit and therefore it is credited to all partners equally.
8	New partner brings necessary amount as his capital.
9	New partner is entitled to share in revaluation profit.
	Answers:
1	**False**
	All the partners have same rights at all times, unless contrary is provided in the partnership deed/or agreed by the partners.
2	**True**
	With every new partner, remaining old partners have to forgo a proportion in their share which is called as sacrificing ratio.
3	**True**
	Revaluation account is also called as profit and loss adjustment account.
4	**True**
	Increase in asset is an income hence credited to revaluation account.
5	**True**
	This can be done by opening Memorandum Revaluation Account.
6	**False**
	New partner is not entitled to have any share in the reserves of the firm prior to his admission. Such reserves are distributed to old partners in their old profit sharing ratio.

7	**False**
	If revaluation account shows credit balance then it represents profit and therefore it is credited to only old partners in their profit sharing ratio and not equally.
8	**True**
	Every incoming partner shall bring in some amount of capital for the firm.
9	**False**
	New partner is not entitled to profit on revaluation, it belongs to old partners in their old profit sharing ratio.
*	**Multiple Choice Questions**
1	A and B are partners sharing profits and losses in the ratio 5:3. They admitted C and agreed to give him 3/10th of the profit. What is the new ratio after C's admission?
	(a) 35:42:17. (b) 35:21:24. (c) 49:22:29
2	A and B are partners sharing profits in the ratio 5:3, they admitted C giving him 3/10th share of profit. If C acquires 1/5 from A and 1/10 from B, new profit sharing ratio will be:
	(a) 5:6:3 (b) 2:4:6. (c) 17:11:12
3	C was admitted in a firm with 1/4th share of the profits of the firm. C contributes ₹ 15,000 as his capital, A and B are other partners with the profit sharing ratio as 3:2. Find the required capital of A and B, if capital should be in profit sharing ratio taking C's as base capital:
	(a) ₹ 27,000 and ₹ 16,000 for A and B respectively
	(b) ₹ 27,000 and ₹ 18,000 for A and B respectively.
	(c) ₹ 32,000 and ₹ 21,000 for A and B respectively.
4	A, B and C are partners sharing profits and losses in the ratio 6:3:3, they agreed to take D into partnership for 1/8th share of profits. Find the new profit sharing ratio.
	(a) 12:27:36:42. (b) 14:7:7:4. (c)1:2:3:4.
5	A and B are partners sharing profits and losses in the ratio of 3:2 (A's Capital is ₹ 30,000 and B's Capital is ₹ 15,000). They admitted C and agreed to give 1/5th share of profits to him. How much C should bring in towards his capital?
	(a) ₹ 9,000. (b) ₹ 12,000. (c) ₹ 11,250.

6	A and B are partners sharing the profit in the ratio of 3:2. They take C as the new partner, who brings in ₹ 25,000 against capital and ₹ 10,000 against goodwill. New profit sharing ratio is 1:1:1. In what ratio will this amount will be shared among the old partners A & B.
	(a) ₹ 8,000: ₹ 2,000.
	(b) ₹ 5,000: ₹ 5,000.
	(c) Old partners will not get any share in the goodwill brought in by C.
7	A and B are partners sharing the profit in the ratio of 3:2. They take C as the new partner, who is supposed to bring ₹ 25,000 against capital & ₹ 10,000 against goodwill. New profit sharing ratio is 1:1:1. C brought cash for his share of Capital and agreed to compensate to A & B outside the firm. How this will be treated in the books of the firm.
	(a) Cash brought in by C will only be credited to his capital account.
	(b) Goodwill will be raised to full value in old ratio.
	(c) Goodwill will be raised to full value in new ratio.
8	X and Y are partners sharing profits in the ratio of 3: 1. They admit Z as a partner who pays ₹ 4,000 as Goodwill the new profit sharing ratio being 2:1: 1 among X, Y and Z respectively. The amount of goodwill will be credited to:
	(a) X and Y as ₹ 3,000 and ₹ 1,000 respectively.
	(b) X only
	(c) Y only.
9	P and Q are partners sharing Profits in the ratio of 2:1. R is admitted to the partnership with effect from 1st April on the term that he will bring ₹ 20,000 as his capital for 1/4th share and pays ₹ 9,000 for goodwill, half of which is to be withdrawn by P and Q. If profit on revaluation is ₹ 6,000 and opening capital of P is ₹ 40,000 and of Q is ₹ 30,000, find the closing balance of each capital.
	(a) ₹ 47,000: ₹ 33,500: ₹ 20,000
	(b) ₹ 50,000: ₹ 35,000: ₹ 20,000.
	(c) ₹ 40,000: ₹ 30,000: ₹ 20,000

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BHAVIK DOSHI



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

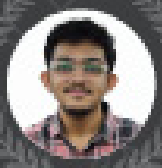
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331



NISHIT KAPUR
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328



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325



SWASTIKA SINGH
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323



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323



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319



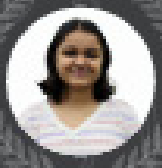
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319



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316



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314



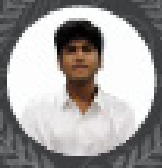
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313



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311



GARV KHANDELWAL
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308



DAKSH JAIN
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308



DEEPAK GURNANI
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305



PARIDHI JHAWAR
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304



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and many more...

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CA INTER MAY'22

AIR 13



MANAN SHAH
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AIR 14



PRACHI NANDU
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AIR 24



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AIR 46



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AIR 46



SANJEEV JAIN
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RISHABH JAIN
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AIR 47



SHREYA SHIVARAM
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AIR 47

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AIR 2



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AIR 8



MAYANK HOLANI
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AIR 17



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AIR 20



RITIK SANGHAVI
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AIR 22



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AIR 35



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SCAN ME!

^ Retirement of a partner **means** that the partner does not remain a partner i.e. **ceases to be a partner** of the firm and the **remaining partners continue** to carry on the business of the firm.

Partner may retire due to old age, misunderstandings amongst the partners, loss in business or want to start business venture etc.

* A partner **may retire** from the firm
1) By giving notice as required, to the other partners of his / her intention to retire, in the case of partnership at will.
2) In accordance with the existing agreement to that effect.
3) With the consent of all the partners.

^ A partner will cease to be a partner on his / her death and hence death is considered as **Compulsory Retirement.**

* Retirement or Death of a partner is a **mode of reconstituting the firm under which**
old partnership relation comes to an end
and
new partnership relation amongst remaining partners (**minimum 2**), **excluding retiring / deceased (outgoing) partner**, begins.

^ **Does** Partnership Firm **gets dissolved** on Retirement **or** Death ?

* **Retirement of a partner**
Usually, Partnership firm continues, DOES NOT get dissolved.

* **Death of a partner**
Unless otherwise agreed by the partners in the Partnership Deed, a firm is dissolved on the death of a partner **(IPA, 1932)**
In most cases, partners will have such clause in the partnership deed **such that** firm doesn't get dissolved on death of a partner and remaining partners (minimum 2) can continue the business post death of a partner.

^ **In case of Retirement,**

Payment of the amount due is made to the retiring partner,

whereas in case of death,

amount due is payable to the Executors **or** Legal heirs of the deceased partner

and hence,

it is to be transferred to Deceased Partners **Executors / Legal heirs Loan A/c**

^ **Retirement**, in most cases, can be planned on the date of Balance Sheet,

but sometimes, it can happen during the year as well

Death, in almost all cases, can happen on any day during the year,

but rarely (pure coincidence), it can happen on the date of Balance Sheet as well

^ Retirement / Death on the date of **Balance Sheet**

Accounting Procedure is **VERY SIMILAR** to that on Admission

Usually given

1. Balance Sheet of the firm before the retirement of a partner

2. Other Relevant details / information

Usually required

1. Pass Journal entries **& / or** Prepare relevant Ledger accounts

2. Balance Sheet of the firm after the retirement of a partner

* **Standard Format'** per solution **(Ledger Accounts)**

Page 1	Revaluation A/c (**or** Profit & Loss Adjustment A/c)	half page
	Partners Capital A/c's	half page
Page 2	Balance Sheet of the firm after retirement / death	15 to 18 lines
	Bank A/c **or** Cash A/c	balance page
Page 3	blank page for workings / notes	full page

* **Summary** of Steps to be followed

Step I , II & III very similar to those on Admission of a Partner	
IV	Adjustment / Treatment of **Goodwill**
V	Record **Sundry Other Transactions**, if any
VI	Treatment of **final amount payable** to Retiring / Deceased Partner
VII	Adjustment of remaining **Partners Capitals in New Ratio**, as specified.
VIII	**Closing Steps**

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^ **Q. 1** : F, G & K were partners in LLP sharing profits and losses at the 2:2:1. K wants to retire on 31.12.2022.

Balance Sheet as on 31.12.2022

Liabilities	(₹)	Assets	(₹)
Capital A/cs		Sundry Fixed Assets	1,50,000
F	1,20,000	Inventories	50,000
G	80,000	Trade receivables	70,000
K	60,000	(Including Bills Receivable	
Reserve	10,000	20,000)	
Trade payables	50,000	Bank	50,000
	3,20,000		**3,20,000**

F and G agree to share profits & losses at the ratio of 3: 2 in future. Value of Goodwill is taken to be ₹ 50,000. Sundry Fixed Assets are revalued upward by ₹ 30,000 and Inventories by ₹ 10,000. Bills Receivable dishonoured ₹ 5,000 on 31.12.2022 but not recorded in the books. Dishonour of bill was due to insolvency of the customer. F and G agree to bring sufficient cash to discharge claim of K and to make their capital proportionate. Also they wanted to maintain ₹ 75,000 bank balance for working capital. Pass necessary journal entries and draft the Balance Sheet of M/s F & G LLP after K's retirement. Also prepare capital accounts of partners.

^ **Q. 2** : K, L & M are partners sharing profits and losses in the ratio 5:3:2. Due to illness, L wanted to retire from the firm on 31.3.2022 and admit his son N in his place.

Balance Sheet of K, L and M as on 31.3.2022

Liabilities		(₹)	Assets	(₹)
Capital:			Furniture	20,000
K	40,000		Trade receivables	50,000
L	60,000		Inventory in Trade	50,000
M	30,000	1,30,000	Cash and Bank balances	80,000
Reserve		50,000		
Trade payables		20,000		
		2,00,000		**2,00,000**

On retirement of L assets were revalued: Furniture ₹ 10,000 and Inventory in trade ₹ 30,000. 50% of the amount due to L was paid off in cash and the balance was retained in the firm as capital of N. On admission of the new partner, goodwill was valued at ₹ 50,000. Partners are being paid off their extra balances to make capital proportionate by keeping N's capital as base. You are required to give:
(i) Necessary journal entries; (ii) balance sheet of M/s K, M and N as on 1.4.2022;
(iii) capital accounts of partners.

^ **Q. 3** : A, B & C were in partnership sharing profits in the proportions of 5:4:3. The balance sheet of the firm as on 31st March, 2022 was as under:

Liabilities	(₹)	Assets	(₹)
Capital accounts:		Fixtures	8,200
A	1,35,930	Inventories	1,57,300
B	95,120	Trade receivables	93,500
C	61,170	Cash	74,910
Trade payables	41,690		
	3,33,910		**3,33,910**

A had been suffering from ill-health and gave notice that he wished to retire. An agreement was, therefore, entered into as on 31st March, 2022, the terms of which were as follows:

(i) The profit and loss account for the year ended 31st March, 2022 which showed a net profit of ₹ 48,000 was to be re-opened. B was to be credited with ₹ 4,000 as bonus, in consideration of the extra work which had devolved upon him during the year. The profit sharing was to be revised from 1st April, 2021, as 3:4:4.

(ii) Goodwill was to be valued at two years' purchase of the average profits of the preceding five years. The fixtures were to be valued by an independent valuer. The valuations arising out of the above agreement were goodwill ₹ 56,800 and fixtures ₹ 10,980. A provision of 2% was to be made for doubtful debts and the remaining assets were to be taken at their book values.

B and C agreed, as between themselves, to continue the business, sharing profits in the ratio of 3:2 and decided to retain the fixtures on the books at the revised value, and to increase the provision for doubtful debts to 6%.

Required:

Prepare necessary accounts and Balance sheet of the firm after retirement.

** If **Retiring Partners Loan** is to be paid **in Instalments** along with Interest

^ **Q. 4 :** On 1 st Jan. 2021 (retirement date), Retiring Partner C's Loan is standing in the books at ₹30,000 & it is to be paid in 4 equal annual instalments on 31.12 every year. Such loan to carry interest @ 6% p.a.. Prepare C's Loan A/c till it is fully paid off.

^ **JOINT LIFE POLICY (JLP)**

* A partnership firm may decide to take a **Joint Life Insurance Policy** on the lives of **all** partners and **premium of such policy** is paid by the firm.

* The **objective** of taking such a policy is to minimize the financial hardships in the event of **payment of large sum** to the retiring partner (in case of retirement) **or** to the legal representatives of a deceased partner (in case of death).

* Such policy can **mature** (amount of such policy is **received**) **either** on the maturity of the policy
or on surrender of such policy at its surrender value (in case of retirement)
or on the death of any partner, whichever is earlier.

* **Accounting Treatment**

There are **3 methods**

I Premium Method (When premium paid is treated as an **expense**)

II Surrender Value Method (When premium paid is treated as an **asset**)

III Joint Life Policy Reserve Method (When premium paid is treated as an **asset** & also, **Joint Life Policy Reserve A/c** is created)

I Premium Method

a) On **payment of premium** by the firm

Joint Life Policy Insurance Premium A/c	Dr.			
To Bank A/c				

b) On treating such premium as **expense** at the end of accounting year

Profit & Loss A/c	Dr.			
To Joint Life Policy Insurance Premium A/c				

Note : Above 2 entries are repeated every year

c) On **maturity** of such policy

Bank A/c or Insurance Company A/c	Dr.			
To Partners Capital A/c's **(O O)**				

Note : Amount received or receivable on maturity of such JLP can be :
either credited to **Partners Capital A/c's (O O)**
or credited to JLP A/c and then, to **Partners Capital A/c's (O O)**
or credited to Revaluation A/c and then,
final difference of such A/c will go to **Partners Capital A/c's (O O)**

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^ **Q. 5** : Red, White and Black shared profits and losses in the ratio of 5:3:2. They took out a joint life Policy in 2018 for ₹ 50,000, a premium of ₹ 3,000 being paid annually on 10th June. The surrender value of the policy on 31st December of various years was as follows: 2018 nil; 2019 ₹ 900; 2020 ₹ 2,000; 2021 ₹ 3,600.
Black retires on 15th April, 2022.
Prepare ledger accounts assuming no Joint Life Policy Account is maintained.

^ **Q. 6** : A, B and C are in partnership sharing profits and losses in the ratio of 5:3:2. They took a joint life policy of ₹1,00,000. A dies and firm receives ₹ 1,00,000 from the insurance company. Pass journal entries.

II **Surrender Value Method**

a) **On payment of premium** by the firm

Joint Life Policy A/c	Dr.			
To Bank A/c				

b) On treating amount **in excess of surrender value** at the end of the year as **loss**

Profit & Loss A/c	Dr.			
To Joint Life Policy A/c				

Note : 1) Above 2 entries are repeated every year
2) In such case, JLP A/c every year will appear in B S at its current surrender value

c) On **maturity** of such policy

i) **For policy amount received / receivable**

Bank A/c **or** Insurance Company A/c	Dr.			
To Joint Life Policy A/c				

ii) **For closing Joint Life Policy A/c** (gain on the policy)

Joint Life Policy A/c	Dr.			
To Partners Capital A/c's **(O O)**				

^ **Q. 7 :** Red, White & Black shared profits and losses in the ratio of 5: 3: 2. They took out a Joint Life Policy in 2018 for ₹ 50,000, a premium of ₹ 3,000 being paid annually on 10th June. The surrender value of the policy on 31st December of various years was as follows: 2018 nil; 2019 ₹ 900: 2020 ₹ 2,000; 2021 ₹ 3,600.
Black retires on 15 th April, 2022 and JLP was surrendered for ₹4,000
Prepare JLP A/c assuming Joint Life Policy A/c is maintained on surrender value basis.

^ **Q. 8 :** A, B and C are in partnership sharing profits and losses in the ratio of 5:3:2. They took a joint life policy of ₹1,00,000 which is appearing in the Balance Sheet at the surrender value of ₹ 10,000. A dies, the firm receives ₹ 1,00,000 from the Insurance company. Pass journal entries.

III **Joint Life Policy Reserve Method**

a) On **payment of premium** by the firm

Joint Life Policy A/c	Dr.			
To Bank A/c				

b) For **creation of JLP Reserve** at the end of the year

Profit & Loss Appropriation A/c	Dr.			
To JLP Reserve A/c				

c) On treating amount **in excess of surrender value** at the end of the year as **loss**

JLP Reserve A/c	Dr.			
To Joint Life Policy A/c				

Note : 1) Above 3 entries are repeated every year

2) In such case, JLP A/c & JLP Reserve A/c, **both**, will appear in Balance Sheet at its current surrender value, at the end of every year.

d) On **maturity** of such policy

i) **For policy amount received / receivable**

Bank A/c **or** Insurance Company A/c	Dr.			
To Joint Life Policy A/c				

ii) **For closing JLP Reserve A/c**

JLP Reserve A/c	Dr.			
To Joint Life Policy A/c				

iii) **For closing Joint Life Policy A/c** (gain on the policy)

Joint Life Policy A/c	Dr.			
To Partners Capital A/c's **(O O)**				

^ **Q. 9 :** A, B and C are in partnership sharing profits and losses in the ratio of 5:3:2. They took a joint life policy of ₹1,00,000 which is appearing in the Balance Sheet at the surrender value of ₹ 10,000, along with JLP Reserve. A dies, the firm receives ₹ 1,00,000 from the Insurance company. Pass journal entries.

^ **Q. 10 :** A, B and C are in partnership sharing profits and losses at the ratio of 5:3: 2.

The balance sheet of the firm on 31.12.2021 was as follows:

Liabilities	(₹)	Assets	(₹)
Capital A/cs:		Sundry Fixed Assets	80,000
A	50,000	Inventories	50,000
B	40,000	Trade receivables	30,000
C	30,000	Joint Life Policy	20,000
Bank Loan	40,000	Bank	10,000
Trade payables	30,000		
	1,90,000		**1,90,000**

On 1.1.2022, A wants to retire, B & C agreed to continue at 2:1. Joint Life Policy was taken on 1.1.2017 for ₹ 1,00,000 and its surrender value as on 31.12.2021 was ₹ 25,000. For the purpose of A's retirement, goodwill was raised for ₹ 1,00,000. Sundry Fixed Assets was revalued for ₹ 1,10,000. Also they agreed to bring necessary cash to discharge 50% of the A's claim, to make the bank balance ₹ 25,000 and to make their capital proportionate. Prepare journal entries to give effect in capital A/c's of partners.

^ **SEPARATE / INDIVIDUAL LIFE POLICY** of each partner

* Instead of taking joint life policy in the names of all the partners, the firm may take individual policies on the lives of respective partners.

* **Premium paid** by the firm is treated **as expense** and charged to **Profit & Loss A/c**

* **In the event of retirement of partner**, retiring partner is **entitled to his / her share** in total surrender value of all the policies on the date of retirement.

Ex. : Sona, Gabbu and Amit are partners sharing profits in the ratio of 3:1:1.

	SONA	GABBU	AMIT
Policy	1,00,000	2,00,000	3,00,000
Surrender Value	10,000	20,000	30,000

If Amit retires, Amit will get 1/5 * 60,000 = Rs. 12,000

* **In the event of death of partner,** deceased partner is **entitled to his / her share in** :

i) amount received / receivable from insurance company on deceased partners policy &

ii) total surrender value of remaining partners policies on the date of death.

If Amit dies, then, Amit's executors will get :

[1/5 x 3,00,000] + [1/5 (10,000 + 20,000)] = 60,000 + 6,000 = Rs. 66,000

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^ **Death (or retirement) anytime during the year**

Accounting Process is same.

One or more of the following **additional entries** may also be required to be passed.

*	1)	**Capital Introduced** by **Deceased Partner** (D.P.) from **the date of Last B S** upto **the date of death**				
*	2)	**Drawings** by **Deceased Partner** from **the date of Last B S** upto **the date of death**				
	a)					
	b)					
*	3)	**Share of Deceased Partner in estimated profit** from **the date of Last B S** upto **the date of death**				
*	4)	I.O.C. / Salary / Commision **etc. due to** the D. P. from **the date of Last B S** upto **the date of death**				
	a)					
	b)					

	5)	I.O.D. **due from** the Deceased Partner				
		from **the date of Last B S** upto **the date of death**				
	a)					
	b)					
	6)	**Close** Deceased Partners **Capital A/c**				
	7)	**Deceased Partners** Executors / Legal heirs **Loan paid**				

^ **USUAL Solution Format** when Ledger A/c's & Balance Sheet is asked

Solution Page No.		approx. page area
Page 1	Revaluation A/c **or** Profit & Loss Adjustment A/c	50%
	Partners Capital A/c's **or** Partners Current A/c's	50%
Page 2	New Balance Sheet	50%
	1) Bank A/c **or** Cash A/c	25%
	2) Profit & Loss Suspense A/c	25%
Page 3	**Blank page for other workings** : Ratio's, Goodwill, Share in Profit, I.O.C., I.O.D. etc.	full

^ **Dr. (Receivable) Deceased Partner's Capital A/c (Payable) Cr.**

Particulars	₹	Particulars	₹
		By Balance b/d (Op. Bal.)	xxx
To Accumulated Losses A/c	xxx	**By** Reserves A/c	xxx
To Revaluation A/c (loss)	xxx	**By** Revaluation A/c (profit)	xxx
To Drawings A/c	xxx	**By** Cash or Bank A/c	xxx
		(Capital Introduced)	
To Goodwill A/c (old Goodwill)	xxx	**By**.....A/c	xxx
(method II & III)		(share of Goodwill)	
		By Profit & Loss Suspense A/c	xxx
		(Share in Profit)	
To Interest on Drawings A/c		**By** I.O.C. / Salary **etc**. A/c	xxx
To Deceased Partners			
Executors / Legal heirs			
Loan A/c	xxx		
	xxx		**xxx**

^ **Profit & Loss Suspense A/c**

Particulars	₹	₹	Particulars	₹	₹
To Deceased Partners			**By** I.O.D. A/c		xxx
Capital A/c		xxx			
(Share in Profit)			**By** Balance c/d **		**xxx**
To I.O.C. / Salary etc. A/c		xxx	(closing **Dr.** balance)		
		xxx			**xxx**

** Such closing **Dr. balance** will appear temporarily on the **Asset side** of the B S.

* **At the end of Accounting Year**

	Close Profit & Loss Suspense A/c			

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Q. 11 : Diya, Riya & Kiya are partners of M/s. DRK Fabrics sharing profits and losses in the ratio of 2:1:2. On 31st March 2022 their Balance Sheet was as under:

Liabilities	(₹)	Assets	(₹)
Capitals :		Land & Building	1,65,000
Diya	1,50,000	Furniture	75,000
Riya	1,80,000	Joint life Policy	60,000
Kiya	70,000	Inventory	88,740
General Reserve	1,40,000	Trade Receivable	96,750
Trade payables	60,000	Bank	1,14,510
	6,00,000		**6,00,000**

Kiya died on 30th September, 2022.

The partnership deed provides as follows:

(a) That partners be allowed interest at 12% p.a. on their capitals, but no interest be charged on drawings.

(b) Upon the death of a partner, the goodwill of the firm be valued at one years' purchase of the average net profits (after charging interest on capital) for the four years to 31st March preceding the death of a partner.

The profits of the firm before charging interest on capitals were :

2018-19	1,62,000	2019-20	1,99,000
2020-21	1,87,000	2021-22	1,96,000

Average capital during preceding four years may be assumed as ₹ 3,00,000

(c) Profits till the date of death to be ascertained on the basis of average profit of previous four years.

(d) Upon the death of a partner, she is to be credited with her share of the profits, interest on capitals etc. calculated till the date of death

After the death of Kiya,

1. ₹ 2,00,000 was received from insurance company against Joint life Policy.
2. Land & Building was appreciated by 20%, Furniture to be depreciated by 10%, inventory to be revalued at ₹ 80,000. Bad debts amounted ₹ 1760.
3. Amount payable to Kiya was paid in cash.

You are required to prepare :

1. Revaluation A/c 2. Partners' Capital A/c
3. Balance Sheet as on 30th September 2022, assuming other Assets and liabilities remaining the same.

^ **Q. 12 :** Peter, Paul and Prince were partners sharing profits and losses in the ratio 2:1:1. It was provided in the partnership deed that in the event of retirement /death of a partner, he/his legal representatives would be paid:

(i) The balance in the capital Account

(ii) His share of goodwill of the firm valued at two years purchase of normal average profits (after charging interest on fixed capital) for the last three years to 31st December preceding the retirement or death.

(iii) His share of profits from the beginning of the accounting year to the date of retirement or death, which shall be taken on proportionate basis of profits of the previous year as increased by 25%

(iv) Interest on fixed capital at 10% p.a. though payable to the partners will not be payable in the year of death or retirement.

(v) All the asset are to be revalued on the date of retirement or death and the profit and loss be debited/credited to the Capital Accounts in the profit sharing ratio.

Peter died on 30th September, 2022. The books of Account are closed on calendar year basis from 1st January to 31st December.

The balance in the Fixed Capital Accounts as on 1st January, 2022 were Peter ₹ 10,000, Paul ₹ 5,000 and Prince ₹ 5,000. The balance in the Current Account as on 1st January, 2022 were Peter ₹ 20,000, Paul ₹ 10,000 and Prince ₹ 7,000. Drawings of Peter till 30th September, 2022 were ₹ 10,000. The profits of the firm before charging interest on capital for the calendar years 2019, 2020 and 2021 were ₹ 1,00,000, ₹ 1,20,000 and ₹ 1,50,000 respectively. The profits include the following abnormal items of credit:

	2019	2020	2021
	(₹)	(₹)	(₹)
Profit on sale of assets	5,000	7,000	10,000
Insurance claim received	3,000		12,000

The firm has taken out a Joint Life Policy for ₹ 1,00,000. Besides the partners had severally insured their lives for ₹ 50,000 each, the premium in respect thereof being charged to the Profit and Loss account. The surrender value of the Policies were 30% of the face value. On 30th June, 2022 the firm received notice from the insurance company that the insurance premium in respect of fire policy had been undercharged to the extent of ₹ 6,000 in the year 2021 and the firm has to pay immediately. The revaluation of the assets indicates an upward revision in value of assets to the extent of ₹ 20,000. Prepare an account showing the amount due to Peter's Legal representatives as on 30th September, 2022 along with necessary workings.

^	**Try Yourself : Objectives**
*	**True and False**
1	Business of a partnership has to be closed if any one of the partners retires.
2	At the time of retirement of a partner no special treatment is required for any reserves appearing in the Balance Sheet.
3	After retirement of a partner, profit sharing ratio of continuing partners remains the same.
4	If any partner wants to retire from the business, he must retire on 1st day of the accounting year.
5	Retiring partner has to forego his share of goodwill in the firm.
6	If a partner retires in between the accounting year then he is not entitled to any profit from the date of beginning of the year till his date of retirement.
7	If the firm has taken any joint life policy then it is to be surrendered at the time of retirement of a partner.
8	Any joint life policy reserve appearing in the Balance Sheet is credited to all the partners in their old profit sharing ratio.
9	No revaluation account is necessary on retirement of a partner.
10	Profit on revaluation is credited to continuing partners, retiring partner is not entitled to any profit on revaluation.
11	Business of partnership comes to an end on death of a partner.
12	Legal heir of a deceased partner automatically becomes partner in the firm.
13	A revaluation account is opened in the books of accounts on death of a partner.
14	Any reserve appearing in the balance sheet on the date of death of a partner is transferred to all partners capital account in their profit sharing ratio.
15	Legal heirs of a deceased partner are entitled to his capital account balance only.
16	It is not necessary to adjust goodwill on death of a partner.
17	On death of a partner continuing partners can agree to change their capital contribution and profit sharing ratio.
18	On death of a partner, the firm gets surrender value of the joint life policy.
19	Only legal heirs of deceased partner are entitled to amount received from joint life policy.
	Answers :
1	**False**
	Business of a partnership is not closed if any one of the partners retires, remaining partners can continue to carry on the business.
2	**False**
	At the time of retirement of a partner, all the reserves appearing in the balance sheet are transferred to all the partners in their old profit sharing ratio.

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3	**False**
	After retirement of a partner, profit sharing ratio of continuing partners does not remain the same.
4	**False**
	A partner can retire on any day as per his own wish.
5	**False**
	Retiring partner is entitled to his share of goodwill in the firm.
6	**False**
	If a partner retires in between the accounting year then he is certainly entitled to the profit from the date of beginning of the year till his date of retirement.
7	**True**
	The firm is eligible for the surrender value on the Joint Life Policy taken on the partners at the time of their retirement.
8	**True**
	As per the surrender policy method, the JLP reserve is distributed to the partners in their profit sharing ratio through capital account.
9	**False**
	Revaluation account is necessary on retirement of a partner.
10	**False**
	Profit on revaluation is credited to all the partners in their profit sharing ratio.
11	**False**
	Surviving partners can continue to carry on the business.
12	**False**
	Legal heirs of deceased partners are entitled to dues of the deceased partner.
13	**True**
	To find out profit or loss on revaluation of assets and liabilities and to bring actual values of the assets and liabilities in books, revaluation account is prepared.

14	**True**
	Reserves belong to the partners in the same manner the capital contributed by them.
	Hence, it is distributed to them through the capital account.
15	**False**
	Legal heirs of a deceased partner are entitled to all the dues of deceased partner.
16	**False**
	It is very much necessary to adjust goodwill on death of a partner.
17	**True**
	Yes, it can be continued in the earlier share or in new share, in either case it leads to computing a new profit sharing ratio.
18	**False**
	On death of a partner, the firm gets full value of sum assured of the joint life policy.
19	**False**
	All the partners are entitled to amount received from joint life policy.
*	**MULTIPLE CHOICE QUESTIONS**
1	C, D and E are partners sharing profits and losses in the proportion of 1/2, 1/3 and 1/6. D retired and the new profit sharing ratio between C and E is 3:2 and the Reserve of ₹ 12,000 is divided among the partners in the ratio:
	(a) ₹ 2,000: ₹ 4,000: ₹ 6,000.
	(b) ₹ 5,000: ₹ 5,000: ₹ 2,000.
	(c) ₹ 6,000: ₹ 4,000: ₹ 2,000.
2	A, B and C takes a Joint Life Policy, after five years B retires from the firm. Old profit sharing ratio is 2:2:1. After retirement, A and C decides to share profits equally. They had taken a Joint Life Policy of ₹ 2,50,000 with the surrender value ₹ 50,000. What will be the treatment in the partner's capital account on receiving the JLP amount if joint life policy premium is fully charged to revenue as and when paid?
	(a) ₹ 50,000 credited to all the partners in old ratio.
	(b) ₹ 2,50,000 credited to all the partners in old ratio.
	(c) ₹ 2,00,000 credited to all the partners in old ratio.

3	A, B and C take a Joint Life Policy, after five years, B retires from the firm. Old profit sharing ratio is 2:2:1. After retirement A and C decides to share profits equally. They had taken a Joint Life Policy of ₹ 2,50,000 with the surrender value ₹ 50,000. What will be the treatment in the partner's capital account on receiving the JLP amount if joint life policy is maintained at the surrender value?
	(a) ₹ 50,000 credited to all the partners in old ratio.
	(b) ₹ 2,50,000 credited to all the partners in old ratio.
	(c) No treatment is required.
4	A, B and C are partners sharing profits in the ratio 2:2:1. On retirement of B, goodwill was valued as ₹ 30,000. Find the contribution of A and C to compensate B.
	(a) ₹ 20,000 and ₹ 10,000.
	(b) ₹ 8,000 and ₹ 4,000.
	(c)They will not contribute anything.
5	A, B and C were partners in a firm sharing profits and losses in the ratio of 2:2:1 respectively with the capital balance of ₹ 50,000 for A and B, for C ₹ 25,000. B declared to retire from the firm and balance in reserve on the date was ₹ 15,000. If goodwill of the firm was valued as ₹ 30,000 & profit on revaluation was ₹ 7,050 then what amount will be transferred to the loan account of B.
	(a) ₹ 70,820. (b) ₹ 50,820. (c) ₹25,820.
6	A, B and C are partners sharing profits and losses in the ratio of 3:2:1. C retires on a decided date and Goodwill of the firm is to be valued at ₹ 60,000. Find the amount payable to retiring partner on account of goodwill.
	(a) ₹ 30,000. (b) ₹ 20,000 (c) ₹10,000
7	A, B and C were partners sharing profits and losses in the ratio of 3:2:1. A retired and Goodwill of the firm is to be valued at ₹ 24,000. What will be the treatment for goodwill?
	(a) Credited to Revaluation Account at ₹ 24,000.
	(b) Adjusted through partners' capital accounts in gaining/sacrificing ratio.
	(c) Only A's capital account credited with ₹ 12,000.
8	Balances of A, B and C sharing profits and losses in proportionate to their capitals, stood as A - ₹ 2,00,000; B - ₹ 3,00,000 and C - ₹ 2,00,000. A desired to retire from the firm, B and C share the future profits equally, Goodwill of the entire firm be valued at ₹ 1,40,000 and no Goodwill account being raised.

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(a) Credit Partner's Capital Account with old profit sharing ratio for ₹ 1,40,000.
(b) Credit Partner's Capital Account with new profit sharing ratio for ₹ 1,40,000.
(c) Credit A's Account with ₹ 40,000 and debit B's Capital Account with ₹ 10,000 and C's Capital Account with ₹ 30,000.

9 In the absence of proper agreement, representative of the deceased partner is entitled to the Dead partner's share in
(a) Profits till date, goodwill, joint life policy, share in revalued assets and liabilities.
(b) Capital, goodwill, joint life policy, interest on capital, share in revalued assets and liabilities.
(c) Capital, profits till date, goodwill, joint life policy, share in revalued assets and liabilities.

10 A, B and C are the partners sharing profits and losses in the ratio 2:1:1. Firm has a joint life policy of ₹ 1,20,000 and in the balance sheet it is appearing at the surrender value i.e. ₹ 20,000. On the death of A, how this JLP will be shared among the partners.
(a) ₹ 50,000: ₹ 25,000: ₹ 25,000.
(b) ₹ 60,000: ₹ 30,000: ₹ 30,000.
(c) ₹ 40,000: ₹ 35,000: ₹ 25,000.

11 R, J and D are the partners sharing profits in the ratio 7:5:4. D died on 30th June 2022 It was decided to value the goodwill on the basis of three year's purchase of last five years average profits. If the profits are ₹ 29,600; ₹ 28,700; ₹ 28,900; ₹ 24,000 and ₹ ₹ 26,800. What will be D's share of goodwill?
(a) ₹ 20,700. (b) ₹ 27,600.. (c) ₹82,800.

12 R, J and D are the partners sharing profits in the ratio 7:5:4. D died on 30th June 2022 and profits for the accounting year 2021-2022 were ₹ 24,000. How much share in profits for the period 1st April 2022 to 30th June 2022 will be credited to D's Account.
(a) ₹ 6,000. (b) ₹ 1,500. (c) ₹2,000

13 Revaluation account is prepared at the time of
(a) Admission and retirement of a partner
(b) Death of a partner
(c) All of the above

14 If three partners A, B & C are sharing profits as 5:3:2, then on the death of a partner A, how much B & C will pay to A's executer on account of goodwill. Goodwill is to be calculated on the basis of 2 years purchase of last 3 years average profits. Profits for last three years are: ₹ 3,29,000; ₹ 3,46,000 and ₹ 4,05,000.

(a) ₹ 2,16,000 & ₹ 1,42,000.

(b) ₹ 2,44,000 & ₹ 2,16,000.

(c) ₹ 2,16,000 & ₹ 1,44,000.

Answers:

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

^ **Theoretical Questions**

1 Write short notes on:

(i) Calculation of gaining ratio.

(ii) Final payment of a retiring partner.

2 What is joint life policy? What is the objective of taking such a policy?

3 Explain distinction between retirement and death of a partner as relating to finalisation of amount payable.

4 What amount is payable to legal representatives of dead partner?

5 State the relevant provisions briefly, when settlement with retired partner or executors of deceased partner is delayed ?

Answers

1 (a) On retirement of a partner, the continuing partners will gain in terms of profit sharing ratio. For example, if A, B and C were sharing profits and losses in the ratio of 5:3:2 and B retires, then A and C have to decide at which ratio they will share profits and losses in future. If it is decided that the continuing partners will share profits and losses in future at the ratio of 3:2, then A gains 1/10th [(3/5)-(5/10)] & C gains 2/10 [(2/5)-(2/10)]. So the gaining ratio between A and C is 1:2. If A & C decide to continue at the ratio 5:2, this indicates that they are dividing the gained share in the previous profit sharing ratio.

(b) The following adjustments are necessary in the Capital A/c: (i) Transfer of reserve, (ii) Transfer of goodwill, (iii)Transfer of profit/loss on revaluation. After adjustment of these items, the Capital Account balance standing to the credit of the retiring partner represents amount to be paid to him. The continuing partners may discharge the whole claim at the time of retirement.

2 A partnership firm may decide to take a Joint Life Insurance Policy on the lives of all partners. The firm pays the premium and the amount of policy is payable to the firm on the death of any partner or on the maturity of policy whichever is earlier. The objective of taking such a policy is to minimize the financial hardships on the event of payment of a large sum to the legal representatives of a deceased partner or to the retiring partner.

3 The basic distinction between retirement and death of a partner relates to finalisation of amount payable to the Executor of the deceased partner. Although, revaluation of goodwill is done in the same way as it has been done in case of retirement, in addition, the executor of the deceased partner is entitled to share of profit upto the date of death

4 When the partner dies the amount payable to him/her is paid to his/her legal representatives. The representatives are entitled to the followings :
(a) The amount standing to the credit to the capital account of the deceased partner;
(b) Interest on capital, if provided in the partnership deed upto the date of death;
(c) Share of goodwill of the firm;
(d) Share of undistributed profit or reserves;
(e) Share of profit on the revaluation of assets and liabilities;
(f) Share of profit upto the date of death;
(g) Share of Joint Life Policy.

5 As per Section 37 of the IPA, 1932, if full or part amount of the outgoing partner still remain unpaid, then retired partner or executors / legal heirs of deceased partner will be entitled to get (unless otherwise agreed / specified) :

a) Interest at the agreed rate or at 6% p.a. if nothing is agreed

or

b) Proportionate attributable share in profits of the firm, **whichever is higher**

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347



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346



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344



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338



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329



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326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



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313



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310



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308



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307



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307



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304



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304



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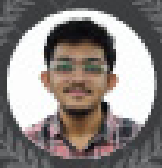
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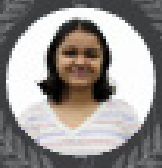
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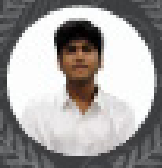
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SCAN ME!

^ **Introduction**

"Dissolution of the firm means dissolution of partnership amongst all the partners in the firm." (Section 39 of the IPA, 1932)

Dissolution of the firm means relationship amongst all the partners coming to an end **which leads to** closure of business and also the firm.

* **Circumstances leading to Dissolution**

(Reasons for which a partnership could be dissolved)

a) On the expiry of the term, where the firm is constituted for a fixed term.

b) On completion of the specific venture, where the firm is constituted to carry out one or more ventures or undertaking.

c) On the death of a partner (unless otherwise agreed amongst the partners)

d) On the adjudication of a partner as an insolvent (unless otherwise agreed)

* A firm **stands dissolved** in the following cases

(Reasons when a firm stands dissolved)

i) The partners agree that the firm should be dissolved

ii) Dissolution by notice, in case partnership is at Will

iii) When all the partners or all except one become insolvent.

iv) When business becomes unlawful / illegal on happening of some event.

v) Dissolution with the Court order

The court has the option to order dissolution of a firm in the following circumstances

a) When a partner has become of unsound mind

b) When a partner suffers from permanent incapacity

c) Where a partner is guilty of misconduct of the business

d) Where a partner persistently disregards the partnership agreement

e) Where a partner transfers his interest or share to a third party

f) Where the business cannot be carried on except at a loss

d) Where it appears to be just and equitable

* Dissolution of Partnership **may** or **may not** result into Dissolution of Firm.

In Dissolution of Partnership, business may continue.

However, it will lead to reconstitution of partnership (Admission of a Partner, Retirement of a Partner, Death of a Partner).

* Distinction between **Dissolution of Partnership** and **Dissolution of Firm**

Dissolution of Partnership	Dissolution of Partnership Firm
Dissolution of a partnership refers to the discontinuance of the relation between the partners of the firm.	Dissolution of the firm implies that the entire firm ceases to exist, including the relation among all the partners.
There can be change in profit sharing ratio or admission/death/retirement of a partner.	Dissolution of partnership firm occurs.
In event of dissolution of the partnership, the business continues as usual, but the partnership is reconstituted.	In event of the dissolution of the firm, the business ceases to end.
There is no intervention by the court.	Court has the inherent power to intervene. By its order, a firm can be dissolved.
Economic relationships among partners may remain same or change.	Economic relationship among partners . comes to an end
Assets and liabilities are revalued.	Assets are sold and realized.
New balance sheet is prepared.	Liabilities are paid off.
Revaluation account is prepared.	Realization account is prepared.
Assets and liabilities are revalued after winding up of the existing partnership.	Assets and liabilities are settled on winding up of a firm.
Books of accounts are not closed.	Books of accounts are closed.

* **On Dissolution of Firm,**

1) Real Assets **(Recorded & Unrecorded)** are disposed off at their current values
2) Outsiders Liabilities **(Recorded & Unrecorded)** are paid off / settled at agreed values
3) Loan taken from Partner is paid off / settled at agreed value
4) Final balance in Partners Capital A/c's is paid to / received from Partner.

^ **Steps to be followed** (Accounting Procedure on Dissolution)

Following Ledger Accounts are to be **kept open for a while**, to record dissolution transactions.

Dissolution : **'Standard Format'** per solution **(Ledger Accounts)**		
Page 1	Realisation A/c	full page
Page 2	Partners Capital A/c's	12 lines
	Loan from Partner A/c	6 lines
	Cash A/c **or** Bank A/c	10 lines

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I	**CLOSE** All Other Ledger Accounts **(except above)**, as appearing in the Balance Sheet on the date of dissolution, at its **BOOK VALUE'S**		
a)	Write **opening balances** in the respective accounts (Page 2 as above) (No Journal Entry required for the same)		
b)	Distribute **Reserves** & Write off **Accumulated Losses**, amongst Partners in P.S.R.		
c)	**Close** All Other Accounts, **Transfer** their balances to Realisation A/c at **B.V.**		
	i) Close **All Real Assets A/c's** & transfer to **Realisation A/c**		
	ii) Close **Provision** / Reserve / Fund **against Assets** A/c's & transfer to **Realisation A/c** Examples : R.D.D, R.F.D.D., Provision for depreciation, Investment Fluctuation Fund, Joint Life Policy Fund / Reserve etc.		
	iii) Close **Sundry Outsiders Liabilities A/c's** and transfer to **Realisation A/c**		
II	**Record** disposal of **various recorded** & unrecorded **assets** **(at CURRENT Values)**		
	i) If realised / disposed off		

ii) If taken over by any partner

III **Record** settlement of **various recorded** & unrecorded **Liabilities** (at CURRENT Values)
(including Realisation / Dissolution expenses)

i) If paid off

ii) If taken over by any partner / partner undertakes to settle a liability

Notes :

1. If the realised amount of any asset is **not** given,
it is assumed that the asset has **not realised** any amount.

2. If the amount paid to any liability is **not** given,
it is assumed to be **fully paid off (at book value)**.

3. If **Bank Overdraft** is given on the **Liability side** (& no further information is given)

4. Profit or Loss on Disposal of **each** Real Asset & Settlement of **each** Outsiders Liability
What Journal entry to be passed ?

5. If any **Asset** is taken over by any **Liability** (Transfer of Asset to pay Liability)
What Journal entry to be passed ?

IV **Settlement / Payment of Loan from Partner**

Note :

Difference, if any, should be transferred to Realisation A/c.

(**If settled for more**, it is Loss for the firm & **if settled for less**, it is Profit for the firm)

V **Close Realisation A/c**

and distribute the Profit or Loss on Dissolution / Realisation amongst partners in their Profit sharing ratio (P.S.R.)

i) If Profit on dissolution

ii) If Loss on dissolution

VI **Settlement of Partners Capitals**

i) If final Cr. Balance (payable to partner), **Pay to such partner**

ii) If final Dr. balance (receivable from partner), **Receive from such partner**

***** Cash A/c or Bank A/c will TALLY.**

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Summary : Steps to be followed

I	Close / Transfer all Balance Sheet A/c's (at **BOOK values**)
II	Record disposal of various recorded & unrecorded assets (at **CURRENT Values**)
III	Record settlement of various recorded & unrecorded Liabilities (at **CURRENT Values**)
	(Including Realisation / Dissolution expenses)
IV	Settlement / Payment of Loan from Partner
V	Close Realisation A/c
VI	Settlement of Partners Capitals
	*** **Cash A/c or Bank A/c will TALLY.**

Dr. **Realisation A/c** **Cr.**

	Particulars	₹	₹	Particulars	₹	₹
I	To Sundry Assets A/c			By Sundry Liabilities A/c		
	(Book Values)	xxx		**(Book Values)**	xxx	
		xxx			xxx	XXX
		xxx		By Provision / Reserve /		
		xxx		Fund against Asset A/c		XXX
		xxx		**(Book Values)**		
		xxx	XXX			
II & III	To Cash or Bank A/c			By Cash or Bank A/c		
	or Partners Capital A/c			or Partners Capital A/c		
	(Current Values)	xxx		**(Current Values)**	xxx	
		xxx	XXX		xxx	
					xxx	
					xxx	XXX
IV	To Loan from Partner A/c		XXX	By Loan from Partner A/c		XXX
	(If settled for more)			(If settled for less)		
V	To Partners Capital A/c's			By Partners Capital A/c's		
	A	xxx		A	xxx	
	B	xxx	XXX	B	xxx	XXX
	(Dissolution Profit)			**(Dissolution Loss)**		
			XXX			XXX

Q. 1 : Amit, Sumit, and Kumar are partners sharing profit and losses in the ratio 2:2:1. The partners decided to dissolve the partnership on 31st March 2022 when their Balance Sheet was as under:

Liabilities	Amt. (₹)	Assets		Amt. (₹)
Capital accounts		Land & Building		1,35,000
Amit	55,200	Plant & Machinery		45,000
Sumit	55,200	Furniture		25,500
General Reserve	61,500	Investments		15,000
Kumar's Loan A/c	15,000	Book Debts	60,000	
Loan from D	1,20,000	Less:Prov. for bad debts	-6,000	54,000
Trade Creditors	30,000	Stock		36,000
Bills Payable	12,000	Bank		13,500
Outstanding Salary	7,500	Capital Withdrawn:		
		Kumar		32,400
	3,56,400			**3,56,400**

The following information is given to you:

(i) Realisation expenses amounted to ₹ 18,000 out of which ₹ 3,000 was borne by Amit.

(ii) A creditor agreed to takeover furniture of book value ₹ 12,000 at ₹ 10,800. The rest of the creditors were paid off at a discount of 6.25%.

(iii) The other assets realized as follows:

Furniture - Remaining taken over by Kumar at 90% of book value

Stock - Realized 120% of book value

Book Debts - ₹ 12,000 of debts proved bad, remaining were fully realized

Land & Building - Realized ₹ 1,65,000

Investments -Taken over by Amit at 15% discount

(iv) For half of his loan, D accepted Plant & Machinery and ₹ 7,500 cash. The remaining amount was paid at a discount of 10%.

(v) Bills payable were due on an average basis of one month after 31st March 2022, but they were paid immediately on 31st March @ 6% discount "per annum".

Prepare the Realization Account, Bank Account and Partners' Capital Accounts in the books of Partnership firm.

FIXED CAPITAL METHOD

(When there are **Partners Current A/c's also**, apart from Capital A/c's)

After all adjustments are done in Partners Current A/c's (instead of Capital A/c's), then,

transfer Current A/c's balances to respective Capital A/c's

& then, settle Partners Capitals.

^ **Q. 2 :** P and Q were partners sharing profits equally in LLP. Their Balance Sheet as on March 31, 2022 (dissolution date) was as follows:

Balance Sheet as on 31st March, 2022

Equity and Liabilities		Amt. (₹)	Assets	Amt. (₹)
Capital accounts			Bank	30,000
P	1,00,000		Debtors	25,000
Q	50,000	1,50,000	Stock	35,000
Creditors		20,000	Furniture	40,000
Q's current account		10,000	Machinery	60,000
Reserves		15,000	P's current account	10,000
Bank overdraft		5,000		
		2,00,000		**2,00,000**

P took over 50% of the stock at 10% less on its book value, and the remaining stock was sold at a gain of 15%. Furniture and Machinery realized for ₹ 30,000 and ₹ 50,000 respectively; There was an unrecorded investment which was sold for ₹ 25,000; Debtors realized 90% only and ₹ 1,245 were recovered for bad debts written off last year. There was an outstanding bill for repairs which had to be paid for ₹ 2,000. You are required to prepare Realization Account, Partners' capital accounts (including transfer of current account balances) and Bank Account in the books of the firm.

^ **When** ONE or more Partners **become Insolvent**

If any partner is unable to pay his dues to the firm (due to his / her insolvency), such Partner's **Capital Deficiency** is borne by other partners in their P.S.R. **(XII th Board)**

* **Garner v/s Murray Rule** (CAFC)

1. It was laid down in famous English case in 1904 & is applicable in India as well, as there has been no case law in India to deal with such situation.
2. It is applicable **only when** there is no agreement between the partners for sharing the **Insolvency Loss** or **Capital Deficiency** in the A/c of Insolvent Partner.
3. Such Loss arises when there is **Debit balance** in Insolvent Partners Capital A/c which such partner is **unable to** pay / bring money in the firm.

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* **KEY POINTS : Garner v/s Murray Rule** (CAFC)

1 Such Loss, being capital loss, to be beared by Solvent Partners in their **Capital Ratio**, such capital being capital **on the** date of dissolution.
Since such Loss is to be beared in Capital Ratio ,
Solvent Partner having **Debit balance** in Capital on the date of dissolution **will not share** Insolvency Loss.
It should be noted that if capital on the date of dissolution contains **one or more error**, it must be **rectified first**, to get correct amout of capital on the date of dissolution, **before determining Capital Ratio**.

2 **Under Fixed Capital Method,**
It should be in Fixed Capitals Ratio **on the** date of dissolution

3 **Under Fluctuating Capital Method**,
It should be in **adjusted Capital Ratio** on the date of dissolution
(Capitals + Reserves - Accumulated Losses)

4 **ALL** Solvent Partners should **bring in** Cash equal to Realisation Loss, **if any**
Cash or Bank A/c Dr.
To **Solvent** Partners Capital A/c's

^ **Q. 3 :** M/s X, Y, and Z who were in partnership sharing profits and losses in the ratio of 2:2:1 respectively, had the following Balance Sheet as on December 31, 2022:

Liabilities			Amt. ₹	Assets		Amt. ₹
Capital:	X	29,200		Fixed Assets		40,000
	Y	10,800		Stock		25,000
	Z	10,000	50,000	Book Debts	25,000	
Z's Loan			5,000	Less: Provision	(5,000)	20,000
Loan from Mrs. X			10,000	Cash		1,000
Sundry Trade Creditors			25,000	Advance to Y		4,000
			90,000			**90,000**

The firm was dissolved on the date mentioned above due to continued losses. After drawing up the balance sheet given above, it was discovered that goods amounting to ₹ 4,000 have been purchased in November, 2022 and had been received but the purchase was not recorded in books. Fixed assets realized ₹ 20,000; Stock ₹ 21,000 and Book Debt ₹ 20,500. Similarly, the creditors allowed a discount of 2% on average. The expenses of realization come to ₹ 1,080. X agreed to take over the loan of Mrs. X. Y is insolvent, and his estate is unable to contribute anything.
Give accounts to close the books; work according to the decision in Garner vs. Murray.

^ **Q. 4 :** 'Thin', 'Short' and 'Fat' were in partnership sharing profits and losses in the ratio of 2:2:1. On 30th September, 2022 their Balance Sheet was as follows:

Liabilities		Amt. ₹	Assets	Amt. ₹
Capital Accounts:			Premises	50,000
Thin	80,000		Fixtures	1,25,000
Short	50,000		Plant	32,500
Fat	20,000	1,50,000	Stock	43,200
Current Accounts:			Debtors	54,780
Thin	29,700		Current Account	
Short	11,300	40,000	Fat	14,500
Sundry Creditors		84,650		
Bank Overdraft		44,330		
		3,18,980		**3,19,980**

'Thin' decides to retire on 30th September, 2022 and as 'Fat' appears to be short of private assets, 'Short' decides that he does not wish to take over Thin's share of partnership, so all three partners decide to dissolve the partnership with effect from 30th September, 2022. It then transpires that 'Fat' has no private assets whatsoever. The premises are sold for ₹ 60,000 and the plant for ₹ 1,07,500. The fixtures realize ₹ 20,000 and the stock is acquired by another firm at a book value less 5%. Debtors realize ₹ 45,900. Realization expenses amount to ₹ 4,500. The bank overdraft is discharged and the creditors are also paid in full.

You are required to write up the following ledger accounts in the partnership books following the rules in Garner vs. Murray:

(i) Realization Account;

(ii) Partners' Current Accounts;

(iii) Partners' Capital Accounts showing the closing of the firm's books.

^ **Insolvency of ALL Partners**

a) Prepare **Separate A/c** for each & every **outsider Liability** and also Deficiency A/c
(It means outsiders liabilities **NOT to be** transferred to Realisation A/c)

b) Available money (after payment of dissolution expenses)
to be be paid to outsiders Liabilities in their **Liability Ratio**

c) Close each outsiders Liability A/c & balance to be transferred to **Deficiency A/c**

d) Close Partners Capital A/c's & balance to be transferred to **Deficiency A/c**

*** **Deficiency A/c will TALLY.**

^ **Q. 5 :** Following is the Balance Sheet as on 31st March, 2019 of a firm having Three equal partners Priti, Priya and Prachi.

Balance Sheet as on 31st March 2019.

Liabilities	Amt. ₹	Assets	Amt. ₹
Capital		Machinery	23,000
Priti	40,000	Furniture	16,000
Priya	35,000	Stock	47,000
Prachi	25,000	Cash at Bank	10,000
Trade Creditors	50,000	Profit and Loss Account	84,000
Loan (secured by Machinery)	30,000		
	1,80,000		**1,80,000**

The firm was dissolved due to insolvency of all the partners. Machinery was sold for ₹ 18,000, while Furniture fetched ₹ 14,000, Stock realised ₹ 35,000. Realisation expenses amounted to ₹ 2,000. Nothing could be recovered from Priya and Prachi, but ₹ 3,400 could be collected from Priti's private estate.
Close the books of accounts of the firm.

Piecemeal Distribution

^ **Piecemeal Distribution**

Generally, on dissolution of firm, assets of the firm are realised, **piece by piece**, in instalments, over a period of few months.
In such a case,
there are two options for payment of liabilities.

* **Option I :**
Distribute cash available also, **piece by piece**, in instalments, to various liabilities in the **prescribed order of payment**, as soon as collected from realisation of assets.

* **Option II :**
Wait for the whole amount to be collected from realisation of all assets and then pay all liabilities together in the prescribed order.

In most cases, the **first option** is preferred.

^ **Prescribed Order of Payment**

The amount realised from the disposal of assets of the firm on dissolution of the firm should be applied / used in the following manner.

I **Realisation / Dissolution Expenses**

There are 3 possibilities

a **If Total Realisation expenses are given / known**

Pay it fully out of available Cash / Bank balance or out of first realisation

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b	**Estimated Realisation expenses are given**
i)	Keep aside amount equal to **estimated** total realisaion expenses,
	out of available Cash / Bank balance **or** out of first realisation
ii)	**Compare** estimated realisation expenses **with** actual realisation expenses at the end
	and **difference** to be added to / deducted from **last realisation** amount.
c	**When Realisation expenses are given at each stage of realisation**
	Since realisation of assets is piece by piece in instalments, expenses also might be
	given / incurred at each stage of realisation.
	In such case, **net** realisation only should be used for repayment of liabilities.
II	**Secured Loans** should be paid out of amount realised from sale of such security.
	If excess amount is realised, balance amount to be utilised for payment of other liabilities.
	If lesser amount is realised, treat balance secured loan as unsecured, at par with
	other unsecured liabilities.
III	**Other Outsiders Liabilities**
*	Preferential Liabilities like Government dues, Employees dues to be paid off first
*	Other unsecured liabilities should be paid in Liability Ratio.
IV	**Loan given by Partner to the firm**
	It can be paid off only after ALL outsiders liabilities are paid off fully.
V	**Adjusted** Capitals of Partners
	Finally, payment can made to partners towards their Capitals, which can be
	calculated **after adjusting it for** i) Current A/c balances, ii) Loan by firm to the partner,
	iii) Reserves and iv) Accumulated Losses, **on the date of dissolution**.
*	**Adjusted Capitals** of Partners can be paid off by following any one of the following
	two methods, as may be decided / given in the problem
1	Excess/Surplus Capital Method or Highest Relative Capital Method or Quotient Method
2	Maximum or Notional Loss Method
1	**Excess / Surplus Capital Method**
	When Actual adjusted Capital of any partner is more than Proportionate Capital,
	such partner is said to be having **Excess** or **Surplus capital**.
	Such excess / surplus capital should be **paid off first**, so that, post that,
	all partners capitals comes in P.S.R. **& then**, all partners can be paid off in their P.S.R.

Q. 6 : The Firm of LMS was dissolved on 31st March, at which date its Balance Sheet stood as follows :

Capital and Liabilities	Amt. (₹)	Properties and Assets	Amt. (₹)
Creditors	2,00,000	Fixed Assets	45,00,000
Bank Loan	5,00,000	Cash & Bank	2,00,000
Laxman's Loan	10,00,000		
Laxman Capital A/c	15,00,000		
Mukund Capital A/c	10,00,000		
Srinivas Capital A/c	5,00,000		
	47,00,000		**47,00,000**

Partners share profits equally. A Firm of Chartered Accountants is retained to realise the assets and distribute the cash after discharge of liabilities. Their fees which are to include all expenses is fixed at ₹ 1,00,000. No loss is expected on realisation since fixed assets include valuable Land and Building. Realisations are as under:

Stage	1	2	3	4	5
₹	5,00,000	15,00,000	15,00,000	30,00,000	30,00,000
	(including cash balance)				

The Chartered Accountant Firm decided to pay off the Partners in 'Higher Relative Capital Method'. You are required to prepare a statement showing distribution of cash with necessary workings.

Q. 6 : **In the books of the firm of LMS**

Statement showing **Piecemeal distribution of Cash**

	Particulars	Available Cash	Bank Loan	Creditors	

Q. 6 : **(Figures in ₹)**

under Highest **Relative Capital Method**

Laxman's	Adjusted Partners Capitals			Total
Loan	Laxman	Mukund	Srinivas	Liabilities

^ **Q. 6 :** **In the books of the firm of LMS**

* **Statement showing calculation of Excess Capital**

			Laxman	Mukund	Srinivas
			(₹)	(₹)	(₹)
1	Capitals as given = **Adjusted Capitals**		**15,00,000**	**10,00,000**	**5,00,000**
10	**Payment towards Partners Capitals**				

^ **Q. 7 :** The Firm of Trinity has presented you with the following Balance Sheet drawn as at 31st March:

Capital and Liabilities	Amt. (₹)	Properties and Assets	Amt. (₹)
Sundry Creditors	37,000	Cash in Hand	3,000
Partners' Capital A/c :		Sundry Debtors	34,000
Iris	40,000	Stock-in-Trade	39,000
Kris	30,000	Plant & Machinery	51,000
Sris	27,000	Current A/c : Kris	4,000
		Sris	3,000
	1,34,000		**1,34,000**

Partners shared profits and losses in the ratio of 4:3:3. Due to differences among the partners, it was decided to wind up the Firm, realise the assets and distribute the cash among the partners at the end of each month.

The following realisations were made :

1. May - ₹ 15,000 from Debtors and ₹ 20,000 by sale of Stock.
   Expenses on Realisation were ₹ 500.
2. June - Balance of Debtors realised ₹ 10,000. Balance of Stock fetched ₹ 24,000.
3. August - Part of Machinery was sold for ₹ 18,000. Expenses incidental to sale were ₹ 600.
4. September - Part of a Machinery valued in the books at ₹ 5,000 was taken by Iris in part discharge at an agreed value of ₹ 10,000. Balance of Machinery was sold for ₹ 30,000 (Net). Partners decided to keep minimum cash balance of ₹ 2,000 in the first 3 months and ₹ 1,000 thereafter.

Show how the amounts due to partners will be settled. All working should form part your answer.

^ **Q. 8 :** The partners P, Q & R (sharing profits and losses in the ratio of 4 : 3 : 2), have called you to assist them in winding up the affairs of their partnership on 31st December. Their Balance Sheet as on the date is given below :

Capital and Liabilities	Amt. (₹)	Properties and Assets	Amt. (₹)
Capital Accounts : P	65,000	Land & Building	50,000
Q	50,500	Plant & Machinery	46,000
R	32,000	Furniture & Fixtures	10,000
Sundry Creditors	16,000	Debtors	14,500
		Stock	14,000
		Cash at Bank	9,000
		Loan P	13,000
		Loan Q	7,000
	1,63,500		**1,63,500**

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Summary of Liquidation Transactions are as follows: (Cash is distributed to the Partners at the end of each month)

January	February	March
• ₹ 9,000 Collected from Debtors, balance is Uncollectable. • ₹ 8,000 - Received from the sale of entire Furniture. • ₹ 1,000 - Liquidation expenses paid. • ₹ 6,000 - Cash retained in the business at the end of month.	• ₹ 1,000 - Liquidation expenses paid. • As part payment of his capital, R accepted a Machinery for ₹ 9,000 (Book Value ₹ 3,500) • ₹ 2,000 - Cash retained in the business at the end of month.	• ₹ 38,000 - Received on the sale of remaining Plant and Machinery. • ₹ 10,000 - Received from the sale of entire Stock. • ₹ 1,700 - Liquidation expenses paid. • ₹ 41,000 - Received on sale of Land & Building. • No cash is retained in the business.

You are required to prepare a Schedule of Cash Payments amongst the Partners by "Higher Relative Capital Method".

^ **Q. 9 :** X, Y and Z are in partnership sharing profits and losses in the ratio of 5:4:4. The Balance Sheet of the Firm as on 31st March 2021 is as below :

Capital and Liabilities	Amt. (₹)	Properties and Assets	Amt. (₹)
X's Capital	60,000	Factory Building	96,640
Y's Capital	40,000	Plant & Machinery	65,100
Z's Capital	50,000	Trade Receivables	21,600
Y's Loan A/c	18,000	Inventories	49,560
Trade Payables	66,000	Cash at Bank	1,100
	2,34,000		**2,34,000**

On the Balance Sheet date, all the three partners have decided to dissolve their partnership. Since the realisation of assets was protracted, they decided to distribute amounts as and when feasible, and for this purpose they appoint Z who was to get as his remuneration 1% of the value of the assets realised other that Cash at Bank, and 10% of the amount distributed to the Partners. Assets were realised piecemeal as under:

First Instalment	Second Instalment	Third Instalment	Last Instalment
₹ 74,600	₹ 69,301	₹ 40,000	₹ 28,000

Dissolution expenses were provided for estimated amount of ₹ 12,000. The Creditors were settled finally for ₹ 63,600.

Prepare a statement showing distribution of Cash amongst the Partners by "Higher Relative Capital Method".

Q. 10 : Daksh Associates is a reputed Firm. On account of certain misunderstanding between the partners, it was decided to dissolve the Firm as on 31st December.

Their Balance Sheet as on 31st December was follows:

Capital and Liabilities		Amt. (₹)	Properties and Assets	Amt. (₹)
Capitals :			Land & Buildings	7,00,000
Daksh	3,00,000		Other Fixed Assets	3,00,000
Yash	2,00,000		Stock-in-Trade	2,00,000
Raj (Minor)	1,00,000	6,00,000	Debtors	4,00,000
Trade Loans		3,00,000	Bills Receivable	1,50,000
Bank Overdraft		3,00,000	Goodwill	30,000
Other Loans		2,00,000	Cash	20,000
Creditors		2,00,000		
Raj's Loan		2,00,000		
		18,00,000		**18,00,000**

It was decided that Mr. Daksh shall be in-charge of realisation. He shall set apart ₹ 10,000 towards expenses. He shall be paid a remuneration of 5% on the amounts distributed to the partners towards their contribution other than Loans.

Assets realised are as follows : (The Final Dissolution is made on 15th March)

Date	1st January	15th January	1st February	15th February	1st March	15th March
Assets	Debtors	Fixed Assets	Debtors	Bills Receivable	Other Fixed Assets	Land and Buildings
(₹)	3,50,000	4,00,000	50,000	1,40,000	50,000	8,00,000

Prepare a statement showing how the money received on various dates will be distributed assuming :

1. The actual expenses of realisation amounted to ₹ 20,005 and the Firm is solvent.
2. Profit sharing ratio for Daksh, Yash & Raj being - (a) Profit 2:2:1, (b) Loss 1:1:Nil.

2 Maximum or Notional Loss Method

* **Pay** till Partners Loan (Loan from Partner) **in usual way**.

* **For payment to Partners** towards their **Adjusted Capitals,**
following steps should be followed under this method, on every realisation.

a) **Assume** cash available / current instalment as final / last realisation.

b) Accordingly,
calculate **Realisation Loss** & distribute the same amongst partners in their **P.S.R.**

c) If any partners **capital** shows **negative balance**,
assume such partner to be Insolvent, unable to contribute anything and accordingly,
distribute **Capital Deficiency / Insolvency Loss** following **Garner v/s Murray**.

* Repeat the process till no partner is having negative capital balance.

* **At this stage**, Capital balances and cash available will be the same.

d) **Pay** available cash to partners towards their capitals.

e) **Balance Capital** = Capital balance before this realisation **Less** payment made

^ **Q. 11 :** Amar, Akbar & Antony are in partnership. The following is their Balance Sheet as on 31st March on which date they dissolve partnership. They share Profit in the ratio of 5: 3: 2.

Capital and Liabilities	Amt. (₹)	Properties and Assets	Amt. (₹)
Creditors	80,000	Plant and Machinery	60,000
Loan A/c - Amar	20,000	Premises	80,000
Capital A/c		Stock	60,000
Amar	1,00,000	Debtors	1,20,000
Akbar	30,000		
Antony	90,000		
	3,20,000		**3,20,000**

It was agreed to repay the amounts due to the partners as and when the assets were realised, viz. 15th April - ₹ 60,000 1st May - ₹ 1,46,000 31st May - ₹ 94,000
Prepare a statement showing how the distribution should be made under Maximum Loss Method & write up the Cash Account and Partner's Capital Account.

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Q. 12 : E, F and G were partners in a Firm, sharing profits and losses in the ratio of 3:2:1 respectively. Due to extreme competition, it was decided to dissolve the Partnership on 31st December. The Balance Sheet on that date was as followsv:

Liabilities			Amt. (₹)	Assets	Amt. (₹)
Capital A/c's :	E	1,13,100		Machinery	1,54,000
	F	35,400		Furniture & Fittings	25,800
	G	31,500	1,80,000	Investments	5,400
Current A/c's :	E	26,400		Stock	97,700
	G	6,000	32,400	Debtors	56,400
Reserves			1,08,000	Bank	29,700
Loan Account : G			15,000	Current Account : F	18,000
Creditors			51,600		
			3,87,000		**3,87,000**

The realization of assets is spread over the next few months as follows:
February : Debtors ₹ 51,900;
March : Machinery ₹ 1,39,500;
April : Furniture etc. ₹ 18,000
May : G agreed to take over Investment at ₹ 6,300;
June : Stock ₹ 96,000.
Dissolution Expenses, originally provided were ₹ 13,500, but actually amounted to ₹ 9,600 and were paid on 30th April. The partners decide that after Creditors were settled for ₹ 50,400, all cash received should be distributed at the end of each month in the most equitable manner.
Prepare a statement of actual cash distribution as received using "Maximum Loss basis".

^ **Try Yourself : Objectives**

* **State whether the following Statements are True or False with reasons.**

1 Books of accounts are closed in dissolution of partnership.

2 On the dissolution of a partnership firm, firstly, the assets of the firm are realized. Then the amount realized, is applied first towards repayment of liabilities to outsiders.

3 In event of the dissolution of the firm, the business ceases to end. In event of dissolution of the partnership, the partnership is reconstituted and the business continues.

4 Expenses of dissolution on realization of assets are credited to the Realization A/c.

5 Revaluation Account is prepared at the time of dissolution of partnership but Realization Account is prepared at the time of dissolution of partnership firm.

Answers:

1 **False.**

Books of accounts are not closed in dissolution of partnership but are closed in case of dissolution of partnership firm.

2 **True.**

On the dissolution of a partnership firm, firstly, the assets of the firm are realized. Then the amount realized, is applied first towards repayment of liabilities to outsiders & loans taken from partners; afterwards, the capital contributed by partners is repaid.

3 **True.**

In event of the dissolution of the firm, the business ceases to end. However, in event of dissolution of the partnership, the business continues as usual, but the partnership is reconstituted.

4 **False.**

Expenses of dissolution on realization of assets are debited to the Realization Account.

5 **True.**

Revaluation Account is prepared at the time of dissolution of partnership, but Realization Account is prepared at the time of dissolution of partnership firm.

*	**Multiple Choice Questions**
1	Partnership could be dissolved because of
	(a) Death of a partner. (b) Insolvency of a partner. (c) Either (a) or (b).
2	On the dissolution of partnership, profit or loss on realization of assets and liabilities
	should be divided among partners
	(a) In the ratio of their capitals.
	(b) In the same ratio in which they share profits.
	(c) Equally.
3	An unrecorded asset realized at the time of dissolution is credited to
	(a) Realization account.
	(b) Revaluation account.
	(c) Capital accounts.
4	A liability taken over by a partner at the time of dissolution is credited to
	(a) Profit and loss account.
	(b) Partners' capital accounts.
	(c) Realization account.
5	Realization account is a
	(a) Nominal account. (b) Real account. (c) Personal account.
6	Which of the following method/methods is adopted to ensure that distribution of cash
	among partners is in proportion to their interest in partnership?
	(a) Maximum loss method.
	(b) Highest relative capital method.
	(c) Either (a) or (b).
	Answers:
1	Either (a) or (b).
2	In the same ratio in which they share profits.
3	Realization account.
4	Partners' capital accounts.
5	Nominal account.
6	Either (a) or (b).

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^ **Theoretical Questions**

1 State the circumstances when Garner V/S Murray rule not applicable.

2 W paid a premium to other partners of the firm at the time of his admission to the firm, with a condition that they will not be dissolved before the expiry of five years. The firm is dissolved after three years. W claims refund of premium.

(i) List the criteria for the calculation of the amount of refund.

(ii) Also list any two conditions when no claim in this respect will arise.

Answers:

1 Non-Applicability of Garner vs Murray rule:

(i) When the solvent partner has a debit balance in the capital account.
Only solvent partners will bear the loss of capital deficiency of insolvent partner in their capital ratio. If incidentally, a solvent partner has a debit balance in his capital account, he will escape the liability to bear the loss due to insolvency of another partner.

(ii) When the firm has only two partners.

(iii) When there is an agreement between the partners to share the deficiency in capital account of the insolvent partner.

(iv) When all the partners of the firm are insolvent.

2 If the firm is dissolved before the term expires, as is the case, W being a partner who has paid a premium on admission will have to be repaid/refunded

The criteria for calculation of refund amount are:

(i) Terms upon which admission was made,

(ii) The time period for which it was agreed that the firm will not be dissolved,

(iii) The time period for which the firm has already been in existence.

No claim for refund will arise if:

(i) The firm is dissolved due to the death of a partner,

(ii) If the dissolution of the firm is basically because of misconduct of W,

(iii) If the dissolution is through an agreement and such an agreement does not have a stipulation for a refund of premium.

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BHAVIK DOSHI



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

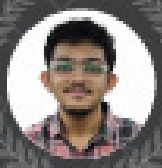
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MEET SHAH
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NISHIT KAPUR
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328



PALAK JAJODIA
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325



SWASTIKA SINGH
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323



SUKUNJ GUPTA
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DURGASHRI VS
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319



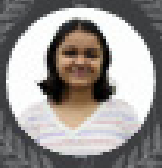
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KARTIK LADHANI
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RIDHI PAREKH
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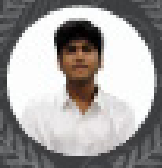
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305



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and many more...

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JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
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AIR 34



HIMANSHI CHHAJED
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AIR 39



YUKTA SATPALKAR
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AIR 40



MARVI LODHA
CA INTER MAY'23
AIR 40



ARMAN HOSANGADY
CA INTER MAY'22
AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MEHDIRA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

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SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHABRIA
CA FINAL NOV'23
AIR 32



PINAL KHETAN
CA FINAL NOV'23
AIR 35



SHOURYA TIBREWALA
CA FINAL MAY'22
AIR 39



DEEPAK LADHA
CA FINAL NOV'23
AIR 40



HIMANSHU KHATRI
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AIR 41



SHRAVAN MUNDRA
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AIR 45



DEEPTHI PACHIPULUSU
CA FINAL MAY'22
AIR 46



SHREY AGARWAL
CA FINAL MAY'22
AIR 48

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KANDIVALI (W)
9/82, Mahavir Nagar, Pragati CHS LTD, Kandivali (West), Mumbai :- 400 067
Ph. : 7784 873 873

GOREGAON (W)
202, 2nd floor, Azmi, 2nd floor, Opposite Ratna, Goregaon, Mumbai - 400104
Ph. : 9819 470 740

ANDHERI (E)
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KALYAN (W)
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SCAN ME!

Introduction

The word **'Company'** is defined as a company formed and registered / incorporated under **the Companies Act, 2013** **or** an existing company which is formed & incorporated under any of the previous company laws.

As per the definition, there must be group of persons who agree to form a company under the law **and once so formed,** it becomes a **separate legal entity** having **perpetual succession** with a distinct name of its own and a **common seal**.
Its **existence** is **not affected** by the change of members.
A company (Joint stock company) is an entity created by a group of persons **through the process of law** for usually undertaking a business.
It is **an artificial person** separate from its members / shareholders / owners.
A company is an **artificial person** created by law having common seal and perpetual succession.

Salient Features of a Company

1) Incorporated Association
2) Separate Legal Entity
3) Common Seal
4) Perpetual Existence
5) Limited Liability
6) Distinction between Ownership and Management
7) Transferability of Shares
8) Not a citizen
9) Maintenance of Books
10) Periodic Audit
11) Right of Access to Information

Issue of Shares

* **Capital** refers to money or money's worth invested in the business **by the proprietor** of the business. For the Business Organization / Entity, Capital is treated as **liability towards** the proprietor of the business.
It can be viewed as amount due to / payable by the business to the proprietor of the business. Hence, Capital is Internal **Liability** of the business.

* Capital, **in case of a company**, is called as **Share Capital**.

Capital of a company is divided into units of smaller denominations (say ₹ 1, 2, 5, 10, 50 or 100) and each such unit is called a **Share**.

For example, in a company, total capital of ₹ 50,00,000 is divided into 5,00,000 shares of ₹ 10 each, then each such unit of ₹ 10 each is called a Share.

₹ 10 in above case is known as **face value** or **nominal value** of the share.

Share simply means a share in the share capital of a company.

The persons who **owns** the shares are called **shareholders**

*

Business Organisation	Ownership	Type of Capital	Liability of Owners
Sole Proprietorship	Single Proprietor	Capital	Unlimited
Partnership	Partners	Partners Capital	Unlimited
Company	Shareholders	Share Capital	Limited to the issue price of shares held

^ **Types of Share Capital**

The different types of share capital are as follows :

i) **Authorised** or **Nominal** or **Registered Capital**

A company estimates its **maximum** capital requirements.

This amount of capital is mentioned in **'Capital Clause'** of **'Memorandum of Association'** registered with the Registrar of Companies.

It puts a limit on the amount of capital, **which a company is authorised** to raise during its life time and is called **Authorised Capital**. The Authorised Capital can be increased or decreased by adopting the prescribed legal procedure.

ii) **Issued Capital**

Issued Capital is a **part of the Authorised Capital** that is issued for subscription.

It should be noted that total Issued Capital (all inclusive) **cannot exceed** the Company's Authorised Share Capital.

The part of Authorised capital which is not issued till date is known as Unissued capital.

iii) **Subscribed Capital**

means such part of the issued capital which is subscribed by the members of a company. **When shares issued for subscription are wholly subscribed**, Issued capital and Subscribed capital would be the same.

In case of under subscription, the part of the issued capital which is not subscribed by the public are known as Unsubscribed capital.

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iv) Called up Capital

It is that part of the subscribed capital which is actually called up / demanded from the shareholders till the date.

The part of subscribed capital which is not called up till the date is called Uncalled Capital.

v) Paid up Capital

It is that portion of called up capital which is actually been paid by the shareholders.

Paid up capital = Called up capital **less** calls in arrears.

vi) Reserve Capital

Reserve Capital is that part of the subscribed capital remaining uncalled, that a company resolves, by a Special Resolution, **not to call** except in the event of winding up of the company. The term Reserve Capital and **Capital Reserve** are two different terms. **Capital Reserve** is a reserve created out of capital profits and is shown under the head **Reserves and Surplus** .

^ **A/c's in the Balance Sheet of a Company**

	Account	Balance		Balance Sheet
1	Share Capital	Credit	L	Called up & Paid up Share Capital
2	Calls in Arrears	**Debit**	L	**Deduct from** Called up Capital
	(if overdue money **yet not** received & also, shares **yet not** cancelled / forfeited)			
3	Share Forfeiture	Credit	L	**Add to** Paid up Capital
	(if shares are forfeited **but yet not** reissued)			
4	Securities Premium Capital Reserve	Credit	L	Reserves & Surplus
5	Calls in Advance	Credit	L	Current Liabilities
	(if **yet not** adjusted against respective call)			
6	Bank	**Debit**	A	Current Assets
7	Expenses on Issue of Shares Discount on Issue of Shares	**Debit**	A	Current Assets
	(if **yet not** written off) (These are fictitious assets)			

* Accounts **NOT shown** in the Balance Sheet, **NIL balance**

1) Share Application / Allotment / Call A/c, generally gets cancelled

2) Calls in Arrears A/c, if overdue money already received **or** shares already forfeited

3) Calls in Advance A/c, if already adjusted against respective call

4) Share Forfeiture A/c, if forfeited shares are already reissued

Name of the Company …

Balance Sheet as at ……. (₹ in ……)

Sr. No.	Particulars	Note No.	Figures at the end of Current Reporting Period	Figures at the end of Previous Reporting Period
I.	**EQUITY AND LIABILITIES**			
1	Shareholders Funds			
	(a) Share Capital		xxx	
	(b) Reserves and Surplus		xxx	
	(c) Money received against Share warrants		xxx	
2	**Share Application money pending Allotment**		xxx	
3	**Non-Current Liabilities**			
	(a) Long-term Borrowings		xxx	
	(b) Deferred Tax Liabilities (net)		xxx	
	(c) Other Long Term Liabilities		xxx	
	(d) Long-term Provisions		xxx	
4	**Current Liabilities**			
	(a) Short-term Borrowings		xxx	
	(b) Trade Payables		xxx	
	(c) Other Current Liabilities		xxx	
	(d) Short-term Provisions		xxx	
	Total		**XXX**	
II.	**ASSETS**			
1	**Non-Current Assets**			
	(a) i) Property, Plant and Equipment		xxx	
	ii) Intangible Assets		xxx	
	iii) Capital Work-in-Progress		xxx	
	iv) Intangible Assets under Development		xxx	
	(b) Non-Current Investments		xxx	
	(c) Deferred Tax Assets (net)		xxx	
	(d) Long-term Loans and Advances		xxx	
	(e) Other Non-Current Assets		xxx	
2	**Current Assets**			
	(a) Current Investments		xxx	
	(b) Inventories		xxx	
	(c) Trade Receivables		xxx	
	(d) Cash and Cash Equivalents		xxx	
	(e) Short-term Loans and Advances		**xxx**	
	(f) Other Current Assets		**xxx**	
	Total		**XXX**	

^ **Schedule III, Part I** (of the Companies Act, 2013)

As per Section 129 of the Companies Act, 2013, Financial statements shall give a true and fair view of the state of affairs of the company or companies and comply with the accounting standards notified under Section133 and shall be in the form or forms as may be provided for different class or classes of companies in Division I of Schedule III under the Act.

* **Classes / kinds / types of shares**

Shares of a company can be of two types

1. Preference Shares

2. Equity Shares

Preference shares are the shares which carry the following **two preferential rights** ;

first regarding payment of dividend at fixed % and

second regarding repayment of capital, in case of winding up / liquidation of the company.

Equity shares are those shares which **are not** preference shares.

Equity shares are the **most commonly issued** type of shares which carry the maximum risks & rewards of the business.

The **risks** being losing part or all of the value of shares if business incurs losses ;

the **rewards** being payment of higher dividends and appreciation in the market value of shares, if there is profitable growth of business.

* **A company may Issue shares**

i) for cash **or**

ii) for consideration other than cash

* **Issue of shares for cash consideration**

Shares are said to be issued for cash when the company receives amount by cheque or any other banking instrument / mode against shares issued.

The amount of shares may be payable

either in lumpsum along with the application

or in instalments at different stages

i.e. partly on application, partly on allotment and balance on one or more calls.

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^ Such shares can be issued at Par **or** at Premium **or** at Discount.

* **At Par** :

When shares are issued at its face value, it is said to be an issue at par.

* **At Premium** :

When shares are issued at a price more than the face value,
it is said to be an issue at premium.

* **At Discount** :

When shares are issued at a price less than the face value,
it is said to be an issue at discount.

^ **Accounting Treatment** of Issue of **Equity Shares** for cash by **Public Company**

Public companies issues a 'Prospectus' and invites general public to subscribe for its shares.

^ **Calls - in - Arrears**

Amount **called** by the company towards issue price of shares (either as allotment or as call money) **but yet not received** by the company from one or more shareholders is called **Calls in Arrears.**

Such amount is receivable from such defaulting shareholder(s) in future, hence such defaulting shareholders becomes debtor for the company & hence their A/c is debited.

Calls-in-Arrears A/c is a **Representative Personal A/c** of all defaulting shareholders.

^ **Over-subscription of shares**

means applications received for shares are more than the shares offered (issued) for subscription. A company, usually, cannot allot shares more than the shares it has issued / offered for subscription.

In such case,

company can allot shares in **any of** the following **3 ways**.

i) company can **reject** excess applications and **refund** application money received on such rejected applications

or

ii) company can do **pro-rata (proportionate) allotment** to all the applicants

or

iii) company can accept some applications in full, reject some applications and do pro-rata allotment on balance.

Issue of Equity shares AT PAR - basic entries

	For Receipt of Share Applications		For Disposal of Share Applications	
I	Bank A/c	Dr.	Equity Share Application A/c	Dr.
	To Equity Share Application A/c		To Equity Share Capital A/c	
			To Bank A/c	
			To Equity Share Allotment A/c	
II	**For Allotment moneys due / receivable**		**For Allotment moneys received**	
	Equity Share Allotment A/c	Dr.	Bank A/c	Dr.
	To Equity Share Capital A/c		Calls in Arrears A/c	Dr.
			To Equity Share Allotment A/c	
	At any stage		**For Receipt of Calls in Advance**	
			Bank A/c	Dr.
			To Calls in Advance A/c	
III IV etc.	**For Call moneys due / receivable**		**For Call moneys received**	
	Equity Share..... Call A/c	Dr.	Bank A/c	Dr.
	To Equity Share Capital A/c		Calls in Arrears A/c	Dr.
			Calls in Advance A/c	Dr.
			To Equity Share.....Call A/c	
	For Receipt of Calls in Arrears		**For Expenses on Issue of Shares**	
	Bank A/c	Dr.	Expenses on Issue of Shares A/c	Dr.
	To Calls in Arrears A/c		To Bank A/c	

Issue of Preference Shares

Journal entries for issue of preference shares are very similar to that of equity shares.

Undersubscription of Shares

means applications received by the company are for shares **less than** the shares issued / offered for subscription.

In this case,

journal entries are to be passed for number of shares applied & allotted only,

not for shares issued / offered for subscription.

Minimum Subscription

A public limited company cannot make any allotment of shares unless the amount of **minimum subscription** stated in the prospectus has been subscribed and the sum payable as application money for such shares has been paid to & received by the company.

Every company offering shares to public for subscription is required to state in its prospectus the **minimum subscription**. The Companies Act, 2013 allows the company to decide minimum subscription. **SEBI** (Securities & Exchange Board of India) has prescribed minimum subscription to be **90% of the issue of shares.**
It means, companies issuing shares to public should receive atleast 90% of the application money payable on shares issued for subscription before alloting any shares.

Q. 1 : Gulab Ltd. was registered with a capital of ₹ 10,00,000 divided into 1,00,000 equity shares of ₹ 10 each. The company invited applications for 55,000 shares in July 2021. The amount payable was as follows :

On Application	₹ 3
On Allotment	₹ 2 (24.08.2021)
On First call	₹ 4 (24.11.2021)
On Second & Final call	₹ 1 (24.02.2022)

Applications were received for 90,000 shares.
It was decided :
i) To refuse allotment to the applicants for 15,000 shares,
ii) To allot in full to Mehul who had applied for 5,000 shares
iii) To allot balance of available shares on pro rata basis among the other applicants.
All the calls were made and all the amounts were duly received except both call money on 1,000 shares allotted to Mr. Garib.
Mr. Amir, who had applied for 700 shares, paid both the call money at the time of allotment itself.
Pass journal entries in the books of Gulab Ltd. and show how relevant accounts out of above will appear in the Balance Sheet of the Company.

(Balance sheet format next page)

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M/s Gulab Ltd.

Balance Sheet as at …….

Sr. No.	Particulars	Note No.	Rs.
I.	**EQUITY AND LIABILITIES**		
1	**Shareholders Funds**		
	Share Capital	1	
II.	**ASSETS**		
2	**Current Assets**		
	Cash and Cash Equivalents	2	

Notes to Accounts

Sr. No.	Particulars	Rs.	Rs.
1	**Share Capital**		
	Authorised Share Capital		
	Issued Share Capital		
	Subscribed, Called up and Paid up Share Capital		
2	**Cash and Cash Equivalents**		
	Bank Balance		

^ **Forfeiture / Cancellation of Shares**

Forfeiture of shares means cancellation of shares and forfeiting the amount received against these shares.

If any shareholder(s) does not pay the allotment &/or call(s) money, directors can forfeit such shares as per the provisions of Articles of Association of a company, if such money is not received till the specified date despite of giving reminders.

For forfeiture of shares originally issued **at par**

Equity Share Capital A/c	Dr.	xxx	
(shares forfeited * **called up** value per share)			
To Calls-in-Arrears A/c			xxx
(shares forfeited * **unpaid** value per share)			
To Shares Forfeited A/c			xxx
(shares forfeited * **paid up** value per share)			

^ **Re-issue of all or few of such forfeited shares**

Re-issue of forfeited shares means selling the forfeited shares on the terms as decided by the company. Such shares **can be re-issued** at par, premium or even at discount.

Re-issue is a **sale** of forfeited shares & not an allotment of shares.

Re-issue of forfeited shares **can be** at discount, **but** the amount of discount allowed cannot exceed the amount forfeited on these shares

i.e. Loss on re-issue (discount) cannot be more than profit on forfeiture.

For Re-issue at par

Bank A/c	Dr.	xxx	
(shares re-issued * receipt per share)			
To Equity Share Capital A/c			xxx
(shares re-issued * **Called up** value per share)			

or

For Re-issue at premium

Bank A/c	Dr.	xxx	
(shares re-issued * receipt per share)			
To Equity Share Capital A/c			xxx
(shares re-issued * **Called up** value per share)			
To Securities Premium A/c			xxx
(shares re-issued * Premium per share)			

or

For Re-issue at discount

Bank A/c	Dr.	xxx	
(shares re-issued * receipt per share)			
Shares Forfeited A/c	**Dr.**	xxx	
(shares re-issued * discount per share)			
To Equity Share Capital A/c			xxx
(shares re-issued * **Called up** value per share)			

For Net Profit post re-issue

Shares Forfeited A/c	Dr.	xxx	
(shares **re-issued** * net profit per share)			
To Capital Reserve A/c			xxx

^ **Issue of Shares at Discount**

When a company issues shares at a price less than the face value of the shares, it is known as issue of shares at discount.

According to **Section 53** of the Companies Act, 2013, a company **cannot issue shares** at discount to the public, **except** sweat equity shares (issued to employees and directors), which can be issued at discount.

Also, re-issue of forfeited shares can be at discount, but the amount of discount allowed cannot exceed the amount forfeited on these shares.

^ **Q. 2 :** Fashion Garments Ltd. invited applications for issuing 10,000 equity shares of ₹ 10 each. The amount was payable as follows :

(i) On Application ₹ 1 per share
(ii) On Allotment ₹ 2 per share
(iii) On First Call ₹ 3 per share
(iv) On Second and Final Call ₹ 4 per share

The issue was fully subscribed. Ram to whom 100 shares were allotted, failed to pay the allotment money and his shares were forfeited immediately after the allotment. Shyam to whom 150 shares were allotted, failed to pay the first call. His shares were also forfeited after the first call. Afterwards the second and final call was made. Mohan to whom 50 shares were allotted failed to pay the second and final call. His shares were also forfeited. All the forfeited shares were re-issued at ₹ 9 per share fully paid-up.

Pass necessary journal entries in the books of Fashion Garments Ltd.

^ **Issue of Shares at Premium**

i) When issue price of shares **is higher than** its face value, amount in excess of face value is termed as Securities Premium.

ii) Such premium can be collected by a company either with application money and/or allotment money and/or with one or more call money, as per the terms of issue. (if question is silent, **assume it with** allotment money)

iii) Such Premium is a Capital Receipt / Profit for the company and is to be **credited** to **"Securities Premium A/c"**

iv) Such Securities Premium is shown under the main head **Shareholders Funds** and sub-head **Reserves and Surplus** in the Balance Sheet of the company.

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^ **Forfeiture of shares originally issued at premium**

* **Case I : If premium on such shares is already received**

In such case, premium already collected cannot be cancelled / debited on forfeiture, since premium once received and credited to Securities Premium can be utilised **only for** the purposes specified in Section 52(2) of the Companies Act, 2013 **and hence**, it cannot be cancelled on forefeiture once collected.

* **Case II** : If premium on such shares is **NOT received** (it is **part of** calls-in-arrears)

Equity Share Capital A/c	Dr.	xxx	
(shares forfeited * **called up** value per share)			
Securities Premium A/c	Dr.	xxx	
(shares forfeited * **called up & uncollected premium**)			
To Calls-in-Arrears A/c			xxx
(shares forfeited * **unpaid** value per share)			
To Shares Forfeited A/c			xxx
(shares forfeited * **paid up** value per share)			

^ **Q. 3 :** BP Limited issued a prospectus inviting applications for 1,20,000 equity shares of ₹ 10 each at a premium of ₹ 2 per share payable as follows :

On Application ₹ 3 per share

On Allotment ₹ 5 per share (including premium)

On First and Final Call ₹ 4 per share

Applications were received for 3,60,000 equity shares. Applications for 80,000 shares were rejected and the money refunded. Shares allotted to remaining applications as follows :

Category	No. of shares applied	No. of shares allotted
I	1,60,000	80,000
II	1,20,000	40,000

Excess money received with applications was adjusted towards sums due on allotment and the balance amount returned to the applicants. All calls were made duly received except the final call by a shareholder belonging to Category I who has applied for 680 shares. His shares were forfeited. The forfeited shares were reissued at ₹ 13 per share fully paid-up.

Pass necessary journal entries for the above transactions in the books of BP Ltd, open call in arrears account whenever required.

^ **Q. 4 :** A Company issued 50,000 equity shares of Rs. 100 each at premium of 25%, received applications for 1,10,000 shares and allotment was made as follows :

Allotment Table

	Category	Applied	Allotted	Rejected
1	Fully Rejected	10,000	0	10,000
2	Fully Allotted	20,000	20,000	0
3	Pro Rata (all remaining applications)	80,000	30,000	50,000
		1,10,000	**50,000**	**60,000**

Amount payable per share 30, 60 & balance on call.

Mr. A who was allotted 300 shares on 800 shares he had applied for failed to pay any money after application.

His shares were forfeited after call and subsequently 60% of his shares were reissued at a discount of 10%.

Pass Journal entries to record all the above transactions.

^ **Q. 5 :** PQR Limited issued 2,00,000 equity shares of, ₹ 10 each payable as ₹ 3 per share on application & ₹ 5 per share (including ₹ 2 as premium) on allotment and ₹ 4 per share on call. All these shares were subscribed. Money due on all shares was fully received except from Mr. A, holding 5,000 shares who failed to pay the allotment and call money and Mr. B, holding 10,000 shares, who failed to pay the call money. All these 15,000 shares were forfeited. Out of the forfeited shares, 10,000 shares (including whole of A's shares) were subsequently re-issued to Mr. C as fully paid up at a discount of ₹ 1 per share.

Pass necessary journal entries in the books of PQR Limited, assuming calls in arrears A/c is not to be opened.

^ **Interest on calls-in-arrears and calls-in-advance**

Interest on calls in arrears is recoverable and that in respect of calls in advance is payable, according to provisions in this regard in the articles of the company, at the rates mentioned therein or those to be fixed by the directors, within the limits prescribed by the Articles.

Table F prescribes the **maximum** rates as :

Charge 10% p.a. Int. on calls in arrears and

Allow 12% p.a. Int. on calls in advance.

Interest on calls-in-arrears	Interest on calls-in-advance
It is payable by shareholders to company on the calls due but remaining unpaid.	It is payable by the company to shareholders on the call money received in advance but not yet due.
As per Table F,	As per Table F,
maximum prescribed rate is 10%.	maximum prescribed rate is 12%.
Period considered : From the date call money was due to the date money is finally received.	Period considered : From the date money was received to the day call was finally made due.
Directors have a right to waive off such interest in individual cases at their own discretion.	Shareholders are not entitled for any dividend on calls in advance.
It is a nominal account in nature and is credited to statement of profit and loss as an income.	It is a nominal account in nature with interest being an expense for the company.

^ **Interest on Calls - in - Arrears**

i) For receipt of such Interest, along with calls in arrears

Bank A/c	Dr.	xxx		
To Calls in Arrears A/c		xxx	xxx	
To Interest on calls-in-arrears A/c		xxx		

ii) When Interest on calls-in-arrears is due / receivable (at year end)

Sundry shareholders A/c	Dr.	xxx	
To Interest on calls-in-arrears A/c		xxx	xxx

iii) For transfer of interest on calls-in-arrears

Interest on calls-in-arrears A/c	Dr.	xxx	
To Profit & Loss A/c		xxx	xxx

^ **Interest on Calls - in - Advance**

i) When Interest on calls-in-advance is due / payable

Interest on calls-in-advance A/c	Dr.	xxx	
To Sundry shareholders A/c		xxx	xxx

ii) For payment of such Interest

Sundry shareholders A/c	Dr.	xxx	
To Bank A/c			xxx

iii) For transfer of interest on calls-in-advance

Profit & Loss A/c	Dr.	xxx	
To Interest on calls-in-advance A/c		xxx	xxx

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^ **Q. 6 :** A Limited issued 20,000 equity shares of, 10 each at a premium of 10%, payable ₹ 2 on application; ₹ 4 on allotment (including premium); ₹ 2 on first call and balance on the final call. All the shares were fully subscribed. Mr. M who held 2,000 shares paid full remaining amount on first call itself. The final call which was made after 4 months from the first call was fully paid except a shareholder having 200 shares and one another shareholder having 100 shares. They paid their due amount after 3 months and 4 months respectively alongwith interest on calls in arrears, Company also paid interest on calls in advance to Mr. M. The Company maintains Calls in Arrear and Calls in Advance A/c. Give journal entries to record these transactions.
Show workings of interest calculation. (Ignore dates).

^ **Issue of Shares for Consideration OTHER THAN cash**

i) For Purchase of Business (taking over assets and liabilities)

	Assets A/c (each seperately)	Dr.	xxx		
	To Liabilities A/c (each seperately)		xxx	xxx	
	To Vendor's A/c		xxx	xxx	

ii) For Issue of shares at par

	Vendor's A/c	Dr.	xxx		
	To Equity Share Capital A/c			xxx	

^ **Q. 7 :** R Ltd. took over assets worth ₹ 4,00,000 & liabilities worth ₹ 1,30,000 of Akshya Enterprise. The vendors were issued fully paid equity shares of ₹ 10 each.
Pass journal entries in the following cases :
a) if such shares were issued at par
b) if such shares were issued at 20% premium

^ **Q. 8 :** X Co. Ltd. was incorporated with an authorized share capital of 90,000 equity shares of ₹ 10 each. The company purchased land and buildings from Y Co. Ltd. for ₹ 4,00,000 payable in fully paid-up shares of the company. The balance of the shares were issued to the public, which were fully subscribed and paid for.
You are required to pass Journal Entries and to prepare the Balance Sheet.

^ **Additional Theory**

* **Types of Companies**

1 **Government Company**

According to Section 2(45) of the Companies Act, 2013, "Government company" means any company in which not less than fifty-one per cent of the paid-up share capital is held by the Central Government, or by any State Government or Governments, or partly by the Central Government and partly by one or more State Governments, and includes a company which is a subsidiary company of such a Government company.

2 **Foreign Company**

According to Section 2 (42) of the Companies Act, 2013, "Foreign company" means 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.

3 **Private Company**

Section 2(68) of the Companies Act, 2013 defines 'Private company' as a company which by its articles,

(i) Restrict the right to transfer its shares;

(ii) Except in case of One Person Company limits the number of its members to two hundred:

Provided that where two or more persons hold one or more shares in a company jointly, they shall, for the purposes of this sub-clause, be treated as a single member:

Provided further that

(A) persons who are in the employment of the company; and

(B) persons who, having been formerly in the employment of the company, were members of the company while in that employment and have continued to be members after the employment ceased,

shall not be included in the number of members; and

(iii) 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.

4 **Public Company**

Section 2(71) of the Companies Act, 2013 defines Public Company as a company which -

(a) is not a private company; and

(b) has a minimum paid-up share capital as may be prescribed

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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;

A company which is a listed public company if it gets unlisted continues to be a public company.

No Minimum Paid-up Share Capital : The minimum paid-up share capital requirement of ₹ 1,00,000 (in case of a private company) and ₹ 5,00,000 (in case of a public company) has been done away with under Companies Act, 2013.

Accordingly, no minimum paid-up capital requirements will now apply for incorporating private as well as public companies in India.

5 One Person Company

Section 2 (62) of the Companies Act, 2013 defines "One Person Company" as a company which has only one person as a member.

6 Small Company

Section 2(85) of the Companies Act, 2013 defines "Small company" means a company, other than a public company

(i) paid-up share capital of which does not exceed four crores rupees or such higher amount as may be prescribed which shall not be more than ten crore rupees; and

(ii) turnover of which as per its last profit & loss account for the immediately preceding financial year does not exceed forty crore rupees or such higher amount as may be prescribed which shall not be more than hundred crore rupees:

Provided that nothing in this clause should apply to:

(A) a holding company or a subsidiary company

(B) a company registered under section 8

(C) a company or body corporate governed by any special Act

7 Listed Company

As per Section 2 (52) of the Companies Act, 2013,"listed company" means a company which has any of its securities listed on any recognised stock exchange.

The company, whose shares are not listed on any recognised stock exchange is called ''Unlisted Company''.

An unlisted company can be a public company or a private company.

8 Unlimited Company

Section 2 (92) of the Companies Act, 2013 defines "Unlimited company" means a company not having any limit on the liability of its members.

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9	**Company limited by Shares**
	As per Section 2(22) of the Companies Act, 2013, "Company limited by shares" means a company having the liability of its members limited by the memorandum to the amount, if any, unpaid on the shares respectively held by them.
10	**Company limited by Guarantee**
	As per Section 2(21) of the Companies Act, 2013, "company limited by guarantee" means 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.
11	**Holding Company**
	According to Section 2 (46) of the Companies Act, 2103, "Holding company", in relation to one or more other companies, means a company of which such companies are subsidiary companies.
12	**Subsidiary Company**
	Section 2(87) of the Companies Act, 2013 defines "subsidiary company" as a company in which the holding company:
	(i) Controls the composition of the Board of Directors; or
	(ii) 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.
	A company shall be deemed to be a subsidiary company of the holding company even if there is indirect control through the subsidiary company (ies). The control over the composition of a subsidiary company's Board of Directors means exercise of some power to appoint or remove all or a majority of the directors of the subsidiary company.
*	**Maintenance of Books of Accounts**
	As per Section 128 of the 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 & such books shall be kept on accrual basis and according to the double entry system of accounting :
	Provided further that the company may keep such books of account or other relevant papers in electronic mode in such manner as may be prescribed.

* **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.

Financial Statements as per Section 2(40) of the Companies Act, 2013, inter-alia include -

i. A balance sheet as at the end of the financial year;

ii. A profit & loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;

iii. cash flow statement for the financial year;

iv. A statement of changes in equity, if applicable; and

v. (any explanatory not annexed to, or forming part of, any document referred to in sub clause (i) to sub-clause (iv):

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.

* **Compliance with Accounting Standards**

As per Section 129 of the Companies Act, it is mandatory to comply with accounting standards notified by the Central Government from time to time.

* **Schedule III, Part II** (of the Companies Act, 2013)

Name of the Company ...

Profit and Loss Statement for the year ended ..... (₹ in .....)

Sr. No.	Particulars	Note No.	Figures at the end of Current Reporting Period	Figures at the end of Previous Reporting Period
I	Revenue from operations		xxx	
II	Other income		xxx	
III	Total Revenue (I + II)		xxx	
IV	Expenses			
	Cost of materials consumed		xxx	
	Purchases of Stock-in-Trade		xxx	
	Changes in inventories of finished goods,			
	Work-in-Progress and Stock-in-Trade		xxx	
	Employee benefits expense		xxx	
	Finance costs		xxx	
	Depreciation and amortization expense		xxx	
	Other expenses		xxx	
	Total expenses		xxx	
V	Profit before exceptional and extraordinary items			
	and tax (III - IV)		xxx	
VI	Exceptional items		xxx	
VII	Profit before extraordinary items and tax (V - VI)		xxx	
VIII	Extraordinary Items		xxx	
IX	Profit before tax (VII - VIII)		xxx	
X	Tax expense :			
	(1) Current tax		xxx	
	(2) Deferred tax		xxx	
			xxx	
XI	Profit / (Loss) for the period from continuing			
	operations (VII - VIII)		xxx	
XII	Profit / (Loss) from discontinuing operations		xxx	
XIII	Tax expense of discontinuing operations		xxx	
XIV	Profit / (Loss) from discontinuing operations		xxx	
	(after tax) (XII - XIII)			
XV	Profit / (Loss) for the period (XI + XIV)		xxx	
XVI	Earnings per equity share :			
	(1) Basic		xxx	
	(2) Diluted		xxx	

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^	**Try Yourself : Objectives**
*	**State whether the following statements are True or False with reasons :**
1	Every public company is a listed company.
2	Shares of a private company are not listed on stock exchange.
3	It is not mandatory to incorporate a company under the companies act.
4	Company is an artificial, legal person created by law.
5	Death, insolvency or change of members affects the existence of a company.
6	If the shares are fully paid-up by the shareholder, he is subject to no further liability.
7	Public limited company has restrictions on transferability of shares.
8	Financial statements of company show the financial position of the business.
9	Schedule I gives proforma of Balance Sheet.
10	Schedule III prescribes the format of Directors' Report.
11	Financial statements need to be true and correct as per Companies Act.
12	Every public company is a listed company.
13	Once the application money is received, directors can immediately proceed for allotment of shares.
14	Joint stock company form of business organisation came into existence after industrial revolution.
15	Equity shareholders get guaranteed rate of dividend every year.
16	Face value of shares and market value of shares is always same.
17	Sweat shares are issued to public.
18	The liability of a shareholder of public limited company is limited.
19	Equity shareholders enjoy preferential rights.
20	Shares are always issued at par.
21	Shares are issued for cash only.
22	Share capital is borrowed capital.
23	Entire profit is distributed among the share holders as dividend.
24	In public issue, whole amount of share capital is called at once.
25	A public company can issue shares only at discount.
26	In private placement, shares are issued to public through prospectus.
27	Authorised capital appears in the balance sheet at face value.
28	Liability of a holder of shares is limited to the face value of shares acquired by them.
29	The rate of dividend on preference shares may vary from year to year.
30	A company may issue shares at a discount to the public in general.
31	Sweat equity shares are those which are issued to employees & directors at a discount.
32	As per table F, rate of interest on calls in arrears is 12%.
33	As per Table F, rate of interest on calls in advance is 10%.
34	Non-participating preference shareholders enjoy voting rights.

35	Forfeited shares are available to the company for the purpose of resale.
36	Loss on reissue should exceed the forfeited amount.
37	When shares are forfeited, the share capital account is debited with called up capital of shares forfeited and the share forfeiture account is credited with calls in arrears of shares forfeited.
38	Re-issue of forfeited shares is allotment of shares but not a sale.
39	Interest on calls in arrears is payable by company to shareholders.
40	"Listed company" means a company which has its securities only listed with National stock exchange.
41	Since company has existence independent of its members, it continues to be in existence despite the death, insolvency or change of members.
42	A person holding preference shares of a company cannot hold equity shares of the same company.
	Answers :
1	**False**
	Listed companies are those which are listed on the stock exchange. Shares of listed companies are open to general public. Every listed company is a public company but every public company is not a listed company.
2	**True**
	Only the shares of public company are listed on stock exchange. Every listed company is a public company.
3	**False**
	It is mandatory to incorporate a company under the Companies Act. Without such incorporation, a company cannot come into existence.
4	**True**
	Company comes into existence through the operation of law. It is a separate entity distinct from it's members.
5	**False**
	Company is a separate legal entity created by law. Death, insolvency or change of member does not affect it's existence.
6	**True**
	Liability of shareholders is limited to the extent of the unpaid share capital. So, if shares are fully paid-up, he is subject to no further liability.

7	**False**
	Shares of public company are freely transferable. Transferability of shares is restricted in a private limited company.
8	**True**
	Financial statements give a true & fair view of the state of affairs of the company.
	Financial statements include profit and loss account, balance sheet, etc.
9	**False**
	Schedule III Part I explains proforma of Balance Sheet.
10	**False**
	Schedule III Part I explains proforma of Balance Sheet and Profit and Loss.
11	**False**
	As per Section 128, every company shall prepare financial statement for every financial year which give a true and fair view of the state of the affairs of the company.
12	**False**
	Directors of company cannot forfeit the shares except in case the calls are in arrears.
	Shares are forfeited after serving call reminder and warning notice to defaulters.
13	**False**
	Once the application money is received, the directors cannot proceed to allot the shares.
	They have to confirm that minimum amount has been subscribed as stated in prospectus and other legal requirement are also completed.
14	**True**
	Joint stock company form of business organisation came into existence after Industrial Revolution. This is because after Industrial Revolution there was a need for large size business units due to limited sole trading concerns and partnership firms.
15	**False**
	Equity shareholders do not get guaranteed rate of dividend every year. Equity shareholders get fluctuating rate of dividend depending upon the profit to the company.
	If company suffers loss they are not paid any dividend.

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16	**False**
	Face value of shares and market value of shares is not always the same, face value of shares is fixed but market value of shares always fluctuates depending upon market fluctuations.
17	**False**
	Sweat shares are not issued to public. Such shares are issued to directors or employees at discount or for consideration other than cash for providing their know-how or making available rights in the nature of intellectual property rights.
18	**True**
	The liability of a shareholder of public limited company is limited. This is as per the liability clause of memorandum of Association that the liability of shareholders is limited to the extent of their investment only.
19	**False**
	Equity share holders do not enjoy preferential rights. Preferential rights are enjoyed by preference shareholders. Equity shares are risky shares and they are the last persons to be paid in case of liquidation pf company.
20	**False**
	Shares are not always issued at par. Shares can be issued at par or at premium and at discount as per the requirement of company.
21	**False**
	Shares are not only issued for cash. Shares are also issued for consideration other than cash to vendor for purchase of assets by company and to promoters for their services.
22	**False**
	Share capital is not borrowed capital, it is owned capital. Equity shareholders are the owners of the company therefore, equity capital is owned capital. Issue of debenture or bonds is termed as borrowed capital.
23	**False**
	Entire profit is not distributed as dividend to shareholders. As per the provisions of companies act directors are supposed to create reserves out of profit to certain extent and the balance profit is distributed as dividend.

24	**False**
	Generally when shares are offered to public the whole amount is not called at once. Company asks to pay application money first, then allotment money and then calls on shares.
25	**False**
	A public company can issue shares at premium or at par.
26	**False**
	In private placement, shares are not issued to public through prospectus. In private placement, shares are issued to friends, relatives, directors, financial institutes etc. and company gets relief of complicated procedures of public issue.
27	**True**
	Authorised capital is the amount of capital mentioned in 'capital clause' of the 'Memorandum of Association'. Authorised capital is considered only as presentation and not considered in total of balance sheet.
28	**False**
	Liability of the holder of shares is limited to the issue price of shares acquired by them.
29	**False**
	Rate of preference dividend is always fixed.
30	**False**
	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.
31	**True**
	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).
32	**False**
	As per table F, rate of interest on calls in arrears is 10%.

33	**False**
	As per Table F, rate of interest on calls in advance is 12%.
34	**False**
	A share on which only a fixed rate of dividend is paid every year, without any accompanying additional rights in profits and in the surplus on winding-up, is called Non-participating Preference Shares. Non-participating preference shareholders do not enjoy voting rights.
35	**True**
	Reissue of forfeited shares is not allotment of shares but only a sale.
36	**False**
	Loss on re-issue should not exceed the forfeited amount.
37	**False**
	When shares are forfeited, the share capital account is debited with called up capital of shares forfeited and the share forfeiture account is credited with amount received on shares forfeited.
38	**False**
	A forfeited share is merely a share available to the company for sale and remains vested in the company for that purpose only. Reissue of forfeited shares is not allotment of shares but only a sale as they have already been allotted earlier.
39	**False :** Interest on calls in arrears is payable by shareholders to company.
40	**False**
	As per Section 2 (52) of the Companies Act, 2013,"listed company" means a company which has any of its securities listed on any recognised stock exchange.
41	**True**
	As per Perpetual Existence company has existence independent of its members, it continues to be in existence despite the death, insolvency or change of members.
42	**False**
	Preference share holder can hold both Equity shares and Preference shares of the company. Any person can hold both kinds of shares.

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*	**Multiple Choice Questions**
1	Which of the following statement is not a feature of a Company?
	(a) Separate legal entity
	(b) Perpetual Existence
	(c) Members have unlimited liability
2	In a Government Company, the holding of the Central Government in paid-up capital should not be less than
	(a) 25% (b) 50% (c) 51%
3	Which of the following statement is true in case of a Foreign Company?
	(a) A Company incorporated in India and has place of business outside India.
	(b) A Company incorporated outside India and has a place of business in India.
	(c) A Company incorporated in India and has a place of business in India.
4	Cash flow statements are not required for
	(a) Private company (b) One person company (c) Public company
5	Which of the following statements is not a feature of a private company?
	(a) Restricts the rights of members to transfer its shares.
	(b) Does not restrict on the number of its members to any limit.
	(c) Does not involve participation of public in general.
6	Under Schedule III of the Companies Act, assets and liabilities are to be disclosed based on:
	(a) Current / non-current
	(b) Financial / non-financial
	(c) Owned / not-owned.
7	Schedule III of the Companies Act prescribes the format and content of
	(a) Balance sheet and statement of profit and loss
	(b) Auditors' report
	(c) Directors' report.
8	A company is required to maintain its books of accounts at
	(a) its registered office
	(b) its largest branch office
	(c) Managing Director's residence.

9	The presentation and disclosure requirements of a company are prescribed by
	(a) Schedule III (b) Schedule II (c) Schedule I
10	Following is an example of current assets
	(a) Inventories
	(b) Property, Plant & Equipment
	(c) Intangible Assets.
11	Earnings per share (EPS) is to be disclosed in which of the following section of the financial statement
	(a) Balance Sheet
	(b) Statement of Profit and Loss
	(c) Cash Flow Statements.
12	Following is NOT an example of a company under Companies Act, 2013
	(a) Small company (b) Private company (c) Large company
13	The balance of Share Forfeiture A/c is transferred to_____account after re-issue of these share.
	(a) Reserve Capital (b) Capital Reserve (c) Profit & Loss
14	Premium received on issue of shares is shown to
	(a) Liability side of Balance Sheet
	(b) Asset side of Balance Sheet
	(c) Profit & Loss A/c credit side
15	Shareholders get_____on shares.
	(a) Interest (b) Commission (c) Dividend
16	The document inviting to subscribe the shares of a company is
	(a) Prospectus
	(b) Share certificate
	(c) Memorandum of Association
17	As per SEBI guidelines minimum amount payable on share application should be _____of Issue price of of shares.
	(a) 10% (b) 15% (c) 25%

18 When shares are forfeited the Share Capital Account is_____.
(a) credited (b) debited (c) None

19 The Share Capital which a company is authorised to issue by its Memorandum of Association is_____.
(a) Authorised capital (b) Issued capital (c) Paid up capital

20 The unpaid amount on allotment and calls may be transferred to_____account.
(a) calls in advance (b) calls in arrears (c) calls

21 There must be provision in_____for forfeiture of shares.
(a) Articles of Association
(b) Memorandum of Association
(c) Prospectus

22 If shares are issued at its face value it is called as issue at_____.
(a) premium (b) par (c) discount

23 A share of ₹ 10 issued for ₹ 11 is known as issue of shares
(a) at premium (b) at par (c) at discount

24 The amount of capital which is actually subscribed by the public is known as
(a) Issued capital (b) Paid up capital (c) Subscribed capital

25 A shareholder is a_____of a joint stick company.
(a) owner (b) creditor (c) donor

26 is deducted from the share capital to know paid up value of shares.
(a) calls-in-advance (b) calls-in-arrears (c) forfeited shares

27 Interest on call-in-arrears isfor the company.
(a) income (b) expense (c) asset

28 The excess price received over the par value of shares should be credited to_____.
(a) Calls-in-advance account
(b) Share capital account
(c) Securities premium account

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29 The Securities Premium amount may be utilized by a company for .

(a) Writing off any loss on sale of fixed asset

(b) Writing off any loss of revenue nature

(c) Writing off the expenses/discount on the issue of debentures

30 When shares are forfeited, the share capital account is debited with_____and the share forfeiture account is credited with .

(a) Paid-up capital of shares forfeited; Called up capital of shares forfeited

(b) Called up capital of shares forfeited; Calls in arrear of shares forfeited

(c) Writing off the expenses/discount on the issue of debentures

31 T Ltd. proposed to issue 6,000 equity shares of ₹ 100 each at a premium of 40%. The minimum amount of application money to be collected per share as per the Companies Act, 2013

(a) ₹ 5.00 (b) ₹ 6.00 (c) ₹ 7.00

32 Securities Premium is presented as a part of

(a) Reserves & Surplus (b) Share Capital (c) Asset

33 Dividends are usually paid as a percentage of_____.

(a) Authorized share capital

(b) Net profit

(c) Paid-up capital

34 As per the SEBI guidelines, on issue of shares, the application money should not be less than

(a) 2.5% of the nominal value of shares

(b) 2.5% of the issue price of shares

(c) 25.0% of the issue price of shares

35 G Ltd. acquired assets worth ₹ 7,50,000 from H Ltd. by issue of shares of ₹ 100 at a premium of 25%. The number of shares to be issued by G Ltd. to settle the purchase consideration = ?

(a) 6,000 shares (b) 7,500 shares (c) 9,375 shares

36 Schedule III of Companies Act 2013 prescribes the format for

(a) Financial statements (b) Directors' Report (c) Auditors' Report

37 Dividend on_____shares have to be paid before dividend on_____shares.

(a) Equity, Preference

(b) Preference, Equity

(c) Convertible, Non-Cumulative

38 Preference shares are_____unless expressly stated otherwise.

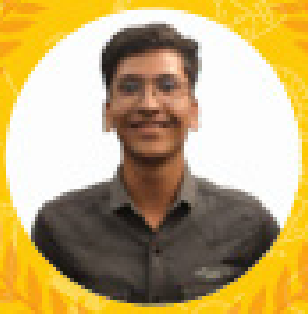
(a) Non-participating (b) Convertible (c) Interest-bearing

Answers :

1	(c)		8	(a)		15	(c)		22	(b)		29	(c)		36	(a)	
2	(c)		9	(a)		16	(a)		23	(a)		30	(c)		37	(b)	
3	(b)		10	(a)		17	(c)		24	(c)		31	(a)		38	(a)	
4	(b)		11	(b)		18	(b)		25	(a)		32	(a)				
5	(b)		12	(c)		19	(a)		26	(b)		33	(c)				
6	(a)		13	(b)		20	(b)		27	(a)		34	(c)				
7	(a)		14	(a)		21	(a)		28	(c)		35	(a)				

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BHAVIK DOSHI



TARA MANGWANI
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RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



HEMIL SATUNDA
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ESAKKIMUTHU DAS
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SHASHI PALOD
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ALVITA KHAN
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SORABH MOHATA
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SANA DESHPANDE
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MEETALI MAHESHWARI
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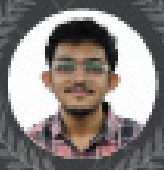
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NISHIT KAPUR
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PALAK JAJODIA
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SWASTIKA SINGH
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SUKUNJ GUPTA
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DURGASHRI VS
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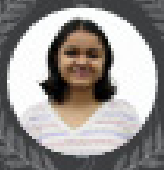
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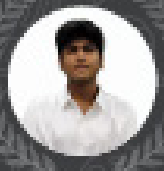
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GARV KHANDELWAL
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DAKSH JAIN
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DEEPAK GURNANI
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PARIDHI JHAWAR
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SATYA BHANUSHALI
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and many more...

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AIR 13

JUHI KAJARIA
CA INTER MAY'22



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
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AIR 34



HIMANSHI CHHAJED
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AIR 39



YUKTA SATPALKAR
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AIR 40



MARVI LODHA
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AIR 40



ARMAN HOSANGADY
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AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MUNDRA
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AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

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AIR 2

SANKRUTI PAROLIA
CA FINAL NOV'23



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHABRIA
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AIR 32



PINAL KHETAN
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AIR 35



SHOURYA TIBREWALA
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AIR 39



DEEPAK LADHA
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SCAN ME!

^ **Debentures**

A debenture is a bond issued by a company under its seal, **acknowledging a debt** and containing **provisions as regards** repayment of the principal and interest.
If a **charge** has been created on any or on the entire assets of the company, the nature of the charge and the assets charged are described therein.
Such charge is **registered with the Registrar** & the certificate registering the charge is printed on the bond.

Section 2(30) of the Companies Act, 2013 **defines debentures as** :
"Debenture" includes debenture stock, bonds, or any other instrument of the company **evidencing a debt**, whether constituting a charge on the assets of the company or not.

* **Features of Debentures**

1. It is document which **evidences** a loan made / given to a company
2. It is a fixed **interest** bearing security where interest falls due on specific dates. Such interest is payable at **fixed rate** on **fixed date**, regardless of profit or loss.
3. Such debentures can be **issued** at par, premium **or** discount and **are redeemable** at future date at par, premium **or** discount.
4. Amount due can be repaid **or** is converted into shares **or** other debentures **or** any combination of above, as pre-decided.
5. It may **or** may not create charge on the assets of the company as security (debentures may be secured debentures or unsecured debentures)
6. No Company **shall issue any debentures** carrying any voting rights.
7. Debentures are generally bought or sold **through the stock exchange** and it might be traded at a price above or below its face value.

^ **Journal entries** for Issue of **Redeemable** Debentures **(in Lumpsum)**

It can be divided into 6 categories as follows

	Issue at	Redeemable at	
1	Par	Par / Discount *	* Redemption at discount is **very rare** in practical life
2	Premium		
3	Discount		
4	Par	Premium	
5	Premium		
6	Discount		

^ **Q. 1 :** Koinai Chemicals Ltd. issued 40,00,000, 11% debentures of ₹50 each, redeemable anytime after 3 years from the date of issue.

Pass Journal entries in each of the following cases :

1) Issue at par redeemable at par
2) Issue at 8% premium redeemable at par
3) Issue at 3% discount redeemable at par
4) Issue at par redeemable at 2% premium
5) Issue at 8% premium redeemable at 2% premium
6) Issue at 3% discount redeemable at 2% premium

^ **Q. 2 :** Modern Equipments Ltd. issued 4,00,000, 12% debentures of ₹100 payable as follows :

On application	₹ 30
On allotment	₹ 70

The debentures were fully subscribed and all the money was duly received. As per the terms of issue, debentures are redeemable at ₹110 per debenture.

Record necessary entries regarding issue of debentures.

^ **Issue of Debentures as Collateral Security**

Collateral security means secondary or supporting security for a loan, which can be realised by the lender in the event of the original loan not being repaid on the due date. Under this arrangement, the borrower agrees that a particular asset or a group of assets will be realized and the proceeds there from will be applied to repay the loan in the event that the amount due, cannot be paid.

Sometimes companies issue their own debentures as collateral security for a loan or a fluctuating overdraft. When the loan is repaid on the due date, these debentures are at once released with the main security. In case, the company cannot repay its loan and the interest thereon on the due date, the lender becomes the debenture holder who can exercise all the rights of a debenture holder.

In such cases, the holder of such debentures is **entitled to interest only on the amount of loan**, but not **on the debentures.**

^ **Accounting Entries**

There are two methods of showing these types of debentures in the accounts of a company.

I Under this method, no entry is made in the books of account of the company at the time of making issue of such debentures.

In the 'Notes to Accounts' of Balance Sheet, the fact of the debentures being issued and outstanding is shown by a note under the liability secured.

Q. 3 : X Ltd. obtains a loan from IDBI of 1,00,00,000, giving as collateral security ₹1,50,00,000 (of ₹10 each), 14%, First Mortgage Debentures.

Answer : In the Notes to Accounts of Balance Sheet of X Ltd., it is shown as follows :

Notes to Accounts of X Limited as at…(includes)

Long Term Borrowings	₹
Secured Loan	
IDBI Loan	1,00,00,000
(Collaterally secured by issue of 1,50,00,000 14% First Mortgage Debentures)	

II Under this method, the following entry is made to record the issue of such debentures:

Debentures Suspense Account Dr.
To % Debentures Account

The Debentures Suspense A/c will appear on the assets side of the Balance Sheet under Other Non-Current Assets and Debentures on the liabilities side of the Balance Sheet. When the loan is repaid, the entry is reversed in order to cancel it.

Taking the same Q.8. above, the entry on issue will be as follows :

Journal in the books of X Ltd.

Date	Particulars		(₹)	(₹)
	Debentures Suspense A/c	Dr.	1,50,00,000	
	To 14% First Mortgage Debentures A/c			1,50,00,000
	(Being the issue of ₹ 15,00,000 debentures @			
	₹ 10 collaterally as per Board's Resolution			
	No…dated…)			

Balance Sheet of X Limited as at…. (Extracts)

Particulars	Notes No.	(₹)	(₹)
EQUITY AND LIABILITIES			
1. Non-Current Liabilities			
Long Term Borrowings	1	2,50,00,000	
Total		**2,50,00,000**	
ASSETS			
2. Non-current Assets			
Other non-current asset	2	1,50,00,000	
3. Current Assets			
Cash and cash equivalent		1,00,00,000	
Total		**2,50,00,000**	

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Notes to accounts			
		(₹)	(₹)
1. Long Term Borrowings			
Secured Loan			
IDBI Loan		1,00,00,000	
14% First Mortgage Debentures		1,50,00,000	2,50,00,000
2. Other non-current asset			
Debenture Suspense Account			1,50,00,000
(issue of ₹15,00,000 14% First Debentures as			
collateral security as per contra)			

Method 1 is much more logical **from the accounting point of view.**

^ **Issue of Debentures in Consideration Other Than For Cash**

^ **Q. 4 :** A Limited issued 14% Debentures of the nominal value of ₹10 each as follows:

(a) To sundry persons 1,00,000 Debentures for cash at 10% discount.

(b) To a vendor for purchase of Inventory worth ₹1,00,000, 8,000 debentures at 25% premium.

(c) To the banker as collateral security for a loan of ₹1,00,000 – ₹1,50,000 nominal value.

Pass necessary Journal Entries.

^ **Treatment of Discount / Loss on Issue of Debentures**

^ **Q. 5 :** HDC Ltd issues 1,00,000, 12% Debentures of ₹100 each at ₹94 on 1-1-2022. Under the terms of issue, the debentures are redeemable at the end of 5 years from the date of the issue. Calculate the amount of discount to be written-off in each of the 5 years.

^ **Q. 6 :** HDC Ltd. issues 2,00,000, 12% Debentures of ₹10 each at ₹9.40 on 1-1-2022. Under the terms of issue, 1/5th of the debentures are annually redeemable by drawings, the first redemption occurring on 31st December, 2022. Calculate the amount of discount to be written-off from 2022 to 2026.

^ **Interest on Debentures**

^ **Q. 7 :** A company issued 12% debentures of the face value of ₹10,00,000 at 10% discount on 1-1-2022. Debenture interest after deducting tax at source @ 10% was payable on 30th June and 31st of December every year. All the debentures were to be redeemed after the expiry of five year period at 5% premium.

Pass journal entries for the accounting year 2022.

^ **Q. 8 :** Journalise the following issues of debentures in the books of the Issuing Company (each situation is independent)

(a) 25,000 nos. of 8% Debentures of ₹100 each, issued at a premium of ₹15 per Debenture, the total amount is collected at the time of application itself.

(b) Machinery worth ₹38 lakhs was purchased. The amount due to the Vendor was settled by way of issue of 6% Debentures of ₹400 each, issued at a discount of 5%.

(c) 50,000 nos. 9% Fully Convertible Debentures issued at face value of ₹ 50 each, the entire amount being collected at the time of application.

^ **Q. 9 :** On 1st January, Ankit Ltd. issued 10% debentures of the face value of ₹ 20,00,000 at 10% discount. Debenture interest after deducting tax at source @ 10% was payable on 30th June and 31st December every year. All the debentures were to be redeemed after the expiry of five year period at 5% premium. Pass necessary journal entries for the accounting year, being calendar year.

^ **Try Yourself**

* **Shares vs Debentures**

Basis	Share	Debenture
1. Meaning	A Share is the share in the **Share Capital** of the Company.	A Debenture is the acknowledgment of **Debt.**
2. Nature	Share Capital is the part of the **Capital** of the company.	Debentures constitute the **Loan** of the company.
3. Holders	Shareholders are the **Owners** of the company.	Debentureholders are the **Creditors.**
4. Kinds	There are only two basic kinds of shares (a) Equity shares, and (b) Preference shares.	Debentures can be classified in different ways.
5. Voting	Shareholders generally enjoy **voting** rights.	Debentures **do not** have any voting rights.
6. Return	Dividend is paid only **out of the** profits of the company.	Interest on debentures is paid **even if** there are **no profits.**
7. Variation in return	Dividend on equity shares may **vary** from year to year. [However, dividend on preference shares is paid at a fixed rate.]	Rate of interest on debentures is **fixed.**

8. Nature of Payment	Dividend is an **appropriation** of profits of the company. Hence, it is not deductible as **an expense** for tax purposes.	Interest on debentures is a **"charge"** on the profits of the company. Interest payment gives tax savings to the company.
9. Disclosure	Shares are shown under **"Share Capital"** on the Liabilities Side of the Balance Sheet.	Debentures are shown under **"Secured Loans"** on the Liabilities Side of the Balance Sheet.
10. Conversion	Shares **cannot** be converted into debentures under any circumstances.	Debentures **may be** converted into shares (partly or fully) as per the terms of issue.
11. Forfeiture	Shares **can be** forfeited for non-payment of allotment or call moneys, as per AOA.	Debentures **cannot** be forfeited for non-payment of call money.
12. Charge on Assets	Shares **do not** carry any charge on assets.	Debentures generally **have** a charge on the assets of the company.
13. Priority of repayment	Upon winding-up, they are paid after Debentureholders are settled.	They are paid **before** shareholders, since they are the creditors of the company.
14. Risk	**Higher** risk than debentureholders.	**Lower** risk than equity shareholders.
15. Control	**Higher** degree of control over the company.	**Minimum / No control.**

* **Different kinds of Debentures**

Kinds of Debentures - Based on

Priority	Negotiability	Redeemability	Security	Convertibility
(a) First Mortgage Debentures	(a) Bearer or Unregistered Debentures	(a) Redeemable Debentures	(a) Secured Debentures	(a) Convertible Debentures
(b) Second Mortgage Debentures	(b) Registered Debentures	(b) Irredeemable or Perpetual Debentures	(b) Unsecured or Naked Debentures	(b) Non-Convertible Debentures

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1. Based on Priority

	First Mortgage Debentures	Second Mortgage Debentures
(a)	They are ranked first and are to be **paid first in priority** to other debentures which may be issued later or subsequently by the company.	They are issued **subsequent to First Debentures** and rank next in matters of repayment, i.e. they can be repaid or redeemed only after first debentures are repaid / redeemed.
(b)	These constitute first priority in repayment.	These constitute second priority in repayment.

2. Based on Negotiability

	Bearer or Unregistered Debentures	Registered Debentures
(a)	These are payable to **Bearer**. Interest is paid through coupons attached to Certificate. On maturity, principal is paid to the Bearer.	These are payable to **Registered Holders**, i.e. whose names appear on the Certificate and are entered as a Holder in the Register of Debenture Holders of the Company.
(b)	These are similar to Negotiable Instruments, and are freely transferable, by mere delivery, ensure good title.	They are transferable only as per conditions endorsed in it, i.e. by way of execution of transfer deed and registration with the Company.
(c)	Stamp duty is not paid on transfer.	Stamp duty is paid on transfer.

3. Based on Permanence / Redeemability

	Redeemable Debentures	Irredeemable Debentures
(a)	They are issued for a specified period of time upon whose expiry, Company has the right to pay back the Holders and have its properties released from charge.	It is a Debenture which contains no clause as to payment, or which contains a clause that it shall not be paid back.
(b)	Payment / Redemption is made at the end of the specified period.	Payment / Redemption is only upon winding-up or a very long period of time, or happening of such other event as specified in the terms of issue.

4. Based on Security

	Secured Debentures	Unsecured / Naked Debentures
(a)	These are secured by a charge on the assets / part of the assets of the company.	These are issued without any security. They do not create any charge on the company's assets.
(b)	The charge may either be fixed or floating. (See Note below.)	Holders are like ordinary unsecured creditors and may sue the company for recovery.
(c)	Holders of such debentures have lower risk.	These type of debentures are very risky from the viewpoint of Investors.

Note : A Fixed Charge is a mortgage on specific assets, e.g. Machinery, Land and Building, etc. These assets cannot be sold without the consent of the Debentureholders. The sale proceeds of these assets are utilized first for repaying Debentureholders.
A Floating Charge generally covers all assets of the Company, including future assets, e.g. Stock, Receivables, Debtors, etc.

5. Based on Convertibility

	Convertible Debentures	Non Convertible Debentures
(a)	They are issued with an option that they can be converted into Equity or Preference Shares (at par or premium or discount), after a certain period.	They do not have any option as to convertibility.
(b)	They can be fully convertible or partly convertible. It shall be approved by a special resolution passed at a general meeting [Sec.71(1)]	They become fully payable on maturity, as specified in the terms of issue. Special resolution not required.

^ **Try Yourself : Objectives**

* **State True or False with reasons**

1. Debenture holder are the owners of the company.
2. Perpetual debentures are payable at the time of liquidation of the company.
3. Registered debentures are transferable by delivery.
4. When companies issue their own debentures as collateral security for a loan, the holder of such debenture is entitled to interest only on the amount of loan and not on the debentures
5. Debentures suspense account appears on liability side of balance sheet.
6. If a company incurs loss, then it does not pay interest to the debenture holders.

7	At the time of liquidation, debenture holders are paid off after the shareholders.
8	Convertible debentures can be converted into equity shares.
9	Redeemable debentures are not payable during the life time of the company.
10	Debentures can be issued for a consideration other than for cash, such as for purchasing land, machinery etc.
11	Debenture interest is payable after the payment of preference dividend but before the payment of equity dividend.
12	Debenture holders enjoy the voting rights in the company.
13	A fixed charge generally covers all the assets of the company including future one.
	Answers :
1	**False**
	Debenture holder are the creditors of the company.
2	**True**
	Perpetual debentures, also known as irredeemable debentures are not repayable during the life time of the company.
3	**False**
	Registered debentures are not easily transferable by delivery. Bearer debentures are transferrable by delivery.
4	**True**
	In case the company cannot repay its loan & the interest thereon on the due date, the lender becomes debenture holder & then only he is entitled to interest on debentures.
5	**False**
	Debentures suspense account appears on asset side of balance sheet under non-current asset.
6	**False**
	Even if the company incurs loss or earns profit, it has to pay the interest on debentures.
7	**False**
	At the time of liquidation, debenture holders are paid off before shareholders on priority basis.

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8	**True**
	Convertible debentures can be converted into equity share after a certain period of time from the date of its issue.
9	**False**
	These debentures are repayable as per the terms of issue, for example, after 8 years from the date of issue.
10	**True**
	Debentures can be issued for a consideration other than for cash, such as for purchasing land, machinery etc.
11	**False**
	Debenture interest is payable before the payment of any dividend on s hares.
12	**False**
	Debenture holder does not enjoy voting rights in company. He is only a creditor of the company.
13	**False**
	A fixed charge is a mortgage on specific assets. A floating charge generally covers all the assets of the company including future one.
*	**Multiple Choice Questions**
1	Premium on redemption of debentures account appearing in the balance sheet is
	(a) A nominal account – expenditure
	(b) A nominal account - income
	(c) A personal account.
2	Debenture interest
	(a) Is payable before the payment of any dividend on shares
	(b) Accumulates in case of losses or inadequate profits
	(c) Is payable after the payment of preference dividend but before the payment of equity dividend.

3 F Ltd. purchased machinery from G Company for a book value of ₹4,00,000. The consideration was paid by issue of 10% debentures of ₹100 each at a premium of 25%. The debenture account was credited with :

(a) ₹4,00,000 (b) ₹5,00,000 (c) ₹3,20,000

4 Which of the following is not a characteristic of Bearer Debentures?

(a) They are treated as negotiable instruments

(b) Their transfer requires a deed of transfer

(c) They are transferable by mere delivery

5 When debentures are issued as collateral security, the final entry for recording the collateral debentures in the books is .

(a) Credit Debentures A/c and debit Cash A/c.

(b) Debit Debenture suspense A/c and credit Cash A/c.

(c) Debit Debenture suspense A/c and credit Debentures A/c.

6 When debentures are redeemable at different dates, the total amount of discount on issue of debentures should be written off

(a) Every year by applying the sum of the year's digit method

(b) Every year by applying the straight line method

(c) To profit and loss account in full in the year of final or last redemption

7 Debentures are issued at discount when

(a) Market interest rate is higher than debenture interest rate

(b) Market interest rate is lower than debenture interest rate

(c) Market interest rate is equal debenture interest rate

8 Interest payable on Debentures attract

(a) Tax deducted at source

(b) Goods and Service tax

(c) Fringe benefit tax

Answers :

1	(c)		**2**	(a)		**3**	(c)		**4**	(b)		**5**	(c)		**6**	(a)
7	(b)		**8**	(a)												

*	**Theoretical Questions**
1	Distinguish between debentures and shares.
2	Explain the purpose for raising of debenture by the company. Also give the main features of debentures.
	Answers:
1	Refer previous pages (post Q. 9) for the distinction between Shares & Debentures.
2	Debenture is one of the most commonly used debt instrument issued by the company to raise funds for the business. The most common method of supplementing the capital available to a company is to issue debentures which may either be simple or naked carrying no charge on assets, or mortgage debentures carrying either a fixed or a floating charge on some or all of the assets of the company.

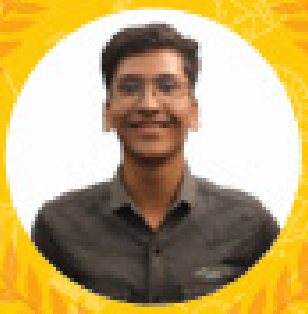
Features of Debentures

1. It is a document which evidences a loan made to a company.
2. It is a fixed interest-bearing security where interest falls due on specific dates.
3. Interest is payable at a predetermined fixed rate, regardless of the level of profit.
4. The original sum is repaid at a specified future date or it is converted into shares or other debentures.
5. It may or may not create a charge on the assets of a company as security.
6. It can generally be bought or sold through the stock exchange at a price above or below its face value.

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346



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344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
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RAVI RAO
313



PRISHITA SETHI
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308



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ESAKKIMUTHU DAS
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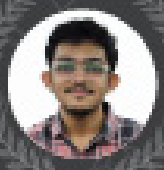
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DURGASHRI VS
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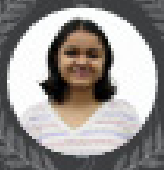
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316



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314



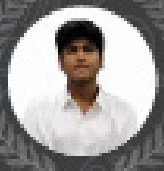
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311



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308



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305



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and many more...

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AIR 13

JUHI KAJARIA
CA INTER MAY'22



MANAN SHAH
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AIR 14



PRACHI NANDU
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AIR 24



VATSAL MEHTA
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AIR 34



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RISHABH JAIN
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AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

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AIR 2

SANKRUTI PAROLIA
CA FINAL NOV'23



MAHESH TAPADIYA
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AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
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AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
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AIR 22



PARTHIV CHABRIA
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AIR 32



PINAL KHETAN
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AIR 35



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SCAN ME!

^ **R**edemption of **P**reference Shares **(RPS)**

Redemption = Repayment

Redemption of PS means **R**edemption of **P**reference **S**hare Capital (**RPSC**)

RPSC means repaying the Capital back to the preference shareholders, **at an** agreed amount, **at an** agreed rate.

Redemption period / maturity date and amount is **known** to all concerned **at the time of** Issue of such securities, so that it is easy to attract Investors.

Company **cannot issue** Irredeemable PS. Maximum time limit for RPS is 20 years, which can be extended upto 30 years for companies engaged in setting up and dealing with of Infrastructural projects.

PS are redeemed **either** at par **or** at premium, but not at discount.

^ **Conditions for Redemption of PSC**

1 **ONLY fully paid up** PS can be redeeemd

Partly paid up preference shares cannot be redeemed.

If company has partly paid up PS, it must be first converted into fully paid up and then only such PS can be redeemed.

* **If final call is yet not made**, make final call and receive all money.

* **If there are calls in arrears**, either receive calls in arrears or forfeit such shares.

Reissue such forfeited shares, if given in the problem.

2 Redemption of **PSC MUST NOT** result into **Reduction of Capital**

* **Option I** : Fresh Issue of shares for this (Capital **to be replaced by** Capital)

In such case, **either** fresh equity shares **or** preference shares can be issued.

Issue of debentures etc **not allowed** for this purpose.

Also, if such fresh shares are issued at premium, securities premium **cannot be** considered for replacement, as capital must be replaced by capital.

* **Option II** : **Create** Capital Redemption Reserve (CRR) **out of** Divisible Profits

CRR = Face value of PS to be redeemed **Less** Face value of fresh issue of shares

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Divisible Profits / Distributable Profits

= Profits otherwise **available for distribution** as dividend to shareholders

Examples of Divisible Profits

General **R**eserve, **R**eserve **F**und, **R**evenue Reserves,

Dividend Equilisation Reserve etc.

Profit & Loss A/c (Surplus in P & L A/c)

** CRR can be **used** in the future, **ONLY FOR**, Issue of **Fully paid up Bonus Shares** and no other purpose. The provisions of the Act relating to reduction of capital shall apply to CRR also, as if the CRR were Paid-Up Capital of the Company.

3 Premium on Redemption of PS, if any, must be **written off immediately out of** Divisible Profits (use Securities Premium, only if, specified in the problem)

^ **Journal Entries**

1 **PS final call due and received**

2 **Receipt of Calls in Arrears on PS**

3 **Forfeiture of PS**

4 **Reissue of PS** (if still time for RPS)

5	**Transfer to Capital Reserve** (even if no re-issue)					
	Note : Replacement of PSC (when no reissue)					
	Full Capital including forfeited shares which are not re-issued					
6	Replacement of PSC to be redeemed					
a	**Fresh Issue of Shares at Par**					
or						
b	**Fresh Issue of Shares at Premium**					
c	**Creation of CRR out of Divisible Profits**					
7	Sundry Other Transactions					
a	**Sale of Investments**					
b	**Loss on Sale of Investments**					
or						
b	**Profit on Sale of Investments**					

8 Redemption of PSC

a **Redemption** due / payable to **Preference share holders**

b **Write off Premium on RPS,** if any, **immediately**

c **Payment to** Preference share holders

^ **Q. 1 :** X Ltd. gives you the following information as at 31st March, 2023:

	Particulars	(₹)
	EQUITY AND LIABILITIES	
1	**Shareholders' funds**	
	a. Share capital	2,90,000
	b. Reserves and Surplus	48,000
2	**Current liabilities**	
	Trade Payables	56,500
	ASSETS	
1	**Property, Plant and Equipment**	3,45,000
2	**Non-current investments**	18,500
3	**Current Assets** Cash and cash equivalents (bank)	31,000

The share capital of the company consists of ₹ 50 each equity shares of ₹ 2,25,000 & ₹ 100 each Preference shares of ₹ 65,000 (issued on 1.4.2021). Reserves & Surplus comprises Profit and Loss Account only.

In order to facilitate the redemption of preference shares at a premium of 10%, the Company decided:

(a) to sell all the investments for ₹ 15,000.

(b) to finance part of redemption from company funds, subject to, leaving a bank balance of ₹ 12,000.

(c) to issue minimum equity share of ₹ 50 each share to raise the balance of funds required.

Pass the necessary journal entries to record the above transactions.

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^ **Q. 2 :** The capital structure of a company consists of 20,000 equity shares of ₹ 10 each fully paid up and 1,000 8% Redeemable Preference Shares of ₹ 100 each fully paid up (issued on 1.4.2021).

Undistributed reserve and surplus stood as : General Reserve ₹ 80,000; Profit & Loss Account ₹ 20,000; Investment Allowance Reserve (out of which ₹ 5,000 not free for distribution as dividend) ₹ 10,000; Securities Premium ₹ 2,000, Cash at bank amounted to ₹ 98,000. Preference shares are to be redeemed at a premium of 10% and for the purpose of redemption, the directors are empowered to make fresh issue of equity shares at par after utilising the undistributed reserve and surplus, subject to the conditions that a sum of ₹ 20,000 shall be retained in general reserve and which should not be utilised.

Pass journal entries to give effect to the above arrangements.

^ **Q. 3 :** The Balance Sheet of XYZ Ltd. as at 31st December, 2021 inter alia includes the following information:

	(₹)
50,000, 8% Preference Shares of ₹ 100 each, ₹ 70 paid up	35,00,000
1,00,000 Equity Shares of ₹ 100 each fully paid up	1,00,00,000
Securities Premium	5,00,000
Capital Redemption Reserve	20,00,000
General Reserve	50,00,000
Bank	15,00,000

Under the terms of their issue, the preference shares are redeemable on 31st March, 2022 at 5% premium. In order to finance the redemption, the company makes a rights issue of 50,000 equity shares of ₹ 100 each at ₹ 110 per share, ₹ 20 being payable on application, ₹ 35 (including premium) on allotment & the balance on 1st January, 2023. The issue was fully subscribed & allotment made on 1st March, 2022. The money due on allotment were duly received by 31st March, 2022. The preference shares were redeemed after fulfilling the necessary conditions of Section 55 of the Companies Act, 2013.

You are asked to pass necessary journal entries assuming that preference shareholder holding 2,000 shares failed to pay the final call and hence such shares are forfeited after giving proper notices (Ignore date column).

Also, show relevant extracts from the Balance Sheet as at end of the year with the corresponding figures.

^ **Q. 4 :** Following is the Balance Sheet of Ms Nataraja Ltd as on 31st March

Equity and Liabilities	(₹)	Assets	(₹)
80,000, 6% Red. Pref. Shares		Sundry Assets	16,80,000
of ₹ 10 each ₹ 9 paid up	7,20,000	Cash	5,20,000
40,000 Equity Shares of ₹ 10			
each fully paid	4,00,000		
Securities Premium	60,000		
Profit and Loss Account	5,00,000		
General Reserve	1,00,000		
Sundry Creditors	4,20,000		
	22,00,000		**22,00,000**

By the terms of their issue, the preference shares were redeemable at a premium of ₹ 50 paise per share on 1st April, and it was decided to arrange for this, as far as possible, out of the company's resources subject to leaving a credit balance of ₹ 24,000 in the P&L A/c. It was also decided to raise the balance of funds required by the issue of sufficient number of equity shares at a premium of 10%. Assume that Securities Premium A/c is usable for providing the premium on redemption of Preference Shares. Show the journal entries giving effect to the above transactions & Balance Sheet thereafter.

^ **Q. 5 :** Calculate the number of equity shares to be issued for redemption in the following independent cases -

A. H Ltd. had 5,000 8% Redeemable Preference Shares of ₹100 each, fully paid up. The company decided to redeem these preference shares at par by the issue of sufficient number of equity shares of ₹10 each fully paid up at par.

B. C Ltd. had 10,000, 10% R. Preference Shares of ₹ 100 each, fully paid up. The company decided to redeem these shares at par, by issue of sufficient number of equity shares of ₹10 each at a premium of 2 per share as fully paid up.

C. G Ltd. had 9,000 10% Redeemable Preference Shares of ₹10 each, fully paid up. The company decided to redeem these preference shares at par by the issue of sufficient number of equity shares of ₹ 9 each fully paid up.

^ **Try Yourself : Objectives**

* **State True or False with reasons :**

1 When shares are redeemed by utilising distributable profit, an amount equal to the face value of shares redeemed is transferred to Capital Reserve account by debiting the distributable profit.

2 A company who prepares financial statements in compliance with Accounting Standards under Section 133 of the Companies Act, 2013, it cannot utilize securities premium for the purpose of providing for premium on the redemption of Redeemable Preference shares of the Company.

3 The balance in forfeited shares account can be used for transfer to capital redemption reserve account.

4 Capital redemption reserve cannot be used for writing off miscellaneous expenses and losses.

Answers :

1 **False**

When shares are redeemed by utilising distributable profit, an amount equal to the face value of shares redeemed is transferred to Capital Redemption Reserve account by debiting the distributable profit.

2 **True**

A company who prepares financial statements in compliance with Accounting Standards under Section 133 of the Companies Act, 2013, it cannot utilize securities premium for the purpose of providing the premium on the redemption of redeemable preference shares.

3 **False**

The balance in Forfeited Shares account cannot be used for transfer to capital redemption reserve account.

4 **True**

Capital redemption reserve cannot be used for writing off miscellaneous expenses and losses.

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* **Multiple Choice Questions**

1 Securities premium cannot be used to_____.

(a) Issue bonus shares

(b) Redeem preference shares

(c) Write-off preliminary expenses

2 S Ltd. issued 2,000, 10% Preference shares of ₹ 100 each at par on 1.4.2021, which are redeemable at a premium of 10%. For the purpose of redemption, the company issued 1,500 Equity Shares of ₹ 100 each at a premium of 20% per share. At the time of redemption of Preference Shares, the amount to be transferred by the company to the Capital Redemption Reserve Account = ?

(a) ₹ 50,000 (b) ₹ 40,000 (c) ₹ 2,00,000

3 Which of the following cannot be used for the purpose of creation of capital redemption reserve account?

(a) Profit and loss account (credit balance)

(b) General reserve account

(c) Unclaimed dividend account

4 According to Section 52 of the Companies Act, 2013, the amount in the Securities Premium A/c cannot be used for the purpose of

(a) Issue of fully paid bonus shares

(b) Writing off losses of the company

(c) For purchase of own securities

5 Which of the following can be utilized for redemption of preference shares?

(a) The proceeds of fresh issue of equity shares

(b) The proceeds of issue of debentures

(c) The proceeds of issue of fixed deposit

6 Preference shares amounting to ₹ 2,00,000 (already issued on 1.4.2021) are redeemed at a premium of 5%, by issue of shares amounting to ₹ 1,00,000 at a premium of 10%. The amount to be transferred to capital redemption reserve = ?

(a) ₹ 1,05,000 (b) ₹ 1,00,000 (c) ₹ 2,00,000

Answers :

1	(b)		**2**	(a)		**3**	(c)		**4**	(b)		**5**	(a)		**6**	(b)

^ **Theoretical Questions**

1 What is the purpose of issuing redeemable preference shares?

2 What are the provisions of the Companies Act, 2013 related with redemption of preference shares? Explain in brief.

Answers :

1 A company may issue redeemable preference shares to raise finance in a dull primary market. Preference shares may be redeemed when there is a surplus of capital and the surplus funds cannot be utilised in the business for profitable use.

Purpose of issuing Redeemable Preference Shares

1 It is a proper way of raising finance in a dull primary market.

2 A company may face difficulty in raising share capital, as its shares are not traded on the stock exchange. Potential investors who may, hesitate in putting money into shares that cannot easily be sold may be encouraged to invest if the shares are redeemable by the company

3 The preference shares may be redeemed when there is a surplus of capital and the surplus funds cannot be utilised in the business for profitable use.

4 No dividend is required to be paid, if there is loss or no profit, whereas interest is payable on debentures or loans even in case of loss. In other words, preference dividend declared / paid continues to be regarded as an appropriation of profits (similar treatment is given for equity shares), as against interest on debentures, which is a charge against profits.

2 Section 55 of the Companies Act, 2013, deals with provisions relating to redemption of preference shares. It ensures that there is no reduction in shareholders' funds due to redemption and, thus, the interest of outsiders is not affected.

Provisions of The Companies Act, 2013 (Section 55)

A company limited by shares if so authorised by its Articles, may issue preference shares which at the option of the company, are liable to be redeemed within a period, normally not exceeding 20 years from the date of their issue. It should be noted that :

(a) no shares can be redeemed except out of divisible or distributable profit, (i.e. out of the profit of the company which would otherwise be available for dividend) or out of proceeds of fresh issue of shares made for the purpose of redemption;

(b) no such shares can be redeemed unless they are fully paid;

(c) (i) in case of such class of companies, as may be prescribed and whose financial statement comply with the accounting standards prescribed for such class of companies under Section 133, the premium, if any, payable on redemption shall be provided for out of the profits of the company, before the shares are redeemed: Provided also that premium, if any, payable on redemption of any preference shares issued on or before the commencement of this Act by any such company shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.

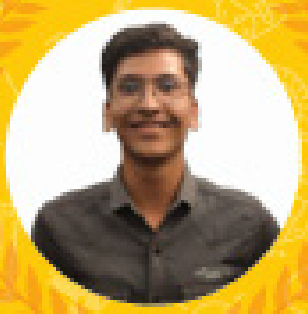
(ii) in case of other companies (not falling under (i) above), the premium, if any payable on redemption shall be provided for out of the profits of the company or out of the company's securities premium account, before such shares are redeemed.

(d) where any such shares are proposed to be redeemed out of the profits of the company, there shall, out of the divisible profits, i.e. the profits which would otherwise have been available for dividends, be transferred to a reserve account to be called Capital Redemption Reserve Account, a sum equal to the nominal amount of the shares redeemed; and the provisions of the Act relating to the reduction of the share capital of a company shall, except as provided in the Section, apply as if the Capital Redemption Reserve (CRR) Account were the paid-up share capital of the company. The utilisation of CRR Account is further restricted to issuance of fully paid-up bonus shares only.

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357/400

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347



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346



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344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



HEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
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ALVITA KHAN
302



SORABH MOHATA
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SANA DESHPANDE
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MEETALI MAHESHWARI
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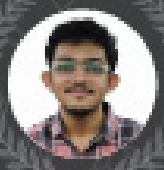
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328



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325



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323



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319



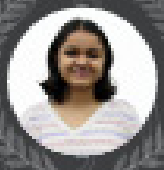
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316



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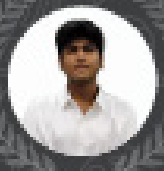
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313



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308



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212, Shreeji Solitaire, Khadakpada Circle, Above Bikaner, Kalyan (W)
Ph. : 70390 633 33

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Ph. : 7020 902 068

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SCAN ME!

^ **Issue of Bonus Shares**

* It is **appropriation out of profits** i.e. one of the way of distribution of profits to the existing shareholders.

It is done by **capitalising profits** i.e. Converting Reserves into Share Capital

* It can be done in **any one** of the following two or **both** ways

A) Bonus Dividend

Conversion of partly paid up shares into fully paid up,
without shareholders being required to pay for the same.

^ **Ex. 1 :** A Limited company with subscribed capital of ₹5,00,000 consisting of 50,000 equity shares of ₹10 each; called up capital of ₹7.50 per share. A bonus was declared out of reserves to be applied in making the existing shares fully paid up.

JOURNAL

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
1				
	(Being equity share final call due on 50,000 equity			
	shares @ ₹2.50 per share as per board's resolution			
	No. …… dated ……)			
2				
	(Being bonus declared for making partly paid up equity			
	shares into fully paid up as per share as per			
	shareholders resolution no.....dated ……)			
3				
	(Being bonus applied for making partly paid up equity			
	shares fully paid up)			

B) Issue of Fully paid up Bonus shares to the existing shareholders

These are additional shares issued to existing shareholders, free of cost i.e. without shareholders being required to pay for the same.

Ex. 2 : A Limited company having fully paid capital of 50,00,000 consisting of Equity shares of ₹10 each, had Reserves of ₹9,00,000. It was resolved to capitalise part of the reserves by issuing fully paid up bonus shares at the rate of one share for every ten shares held.

JOURNAL

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
1				
	(Being bonus declared for issuing fully paid up equity			
	shares, at one share for every ten shares held, as per			
	shareholders resolution no..... dated....)			
2				
	(Being 15,000 equity shares of 10 each fully paid up			
	issued as bonus shares)			

** as per SEBI Regulations for listed companies		Bonus Dividend	Fully paid up Bonus shares
Reserves that **can be utilised** (in that order)			
1	Capital Redemption Reserve	NO	Yes
2	Securities Premium (**only if** realised in cash) **		
	Free Reserves (Divisible Profits) **(Note 1)**		
	Profit on Sale of Investments	Yes	
3	Capital Reserve (Profit on sale of Fixed Assets) **(Note 2)**		
	General Reserve, **R**eserve Fund, **R**evenue Reserves,		
	Dividend Equilisation Reserve etc.		
	Profit & Loss A/c (Surplus in P & L A/c)		
Reserves that **cannot be utilised**			
1	Capital Reserve **(Note 3)**	NO	
2	Revaluation Reserve		
3	Development Rebate Reserve, Investment Allowance		
	Reserve, Export Profit Reserve		

Note 1 : Free Reserves

Free Reserves means, such Reserves, which as per the latest audited balance sheet of a company, are **available for distribution as dividend**. Unrealised Gains / Notional Gains / Gains on Revaluation of assets etc. **shall not be** treated as Free Reserves.

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*	**Note 2** : Capital Reserve, **being Capital Profit on sale of Fixed Assets**
	These are **NOT** available for distribution as dividend (**NOT** Free Reserve)
	in the circumstances given below :
1	When Such Profit on Sale of Fixed Assets is **NOT realised**
2	When Such Profit on Sale of Fixed Assets though realised,
	is likely to be wiped out by the deficiency on revaluation of other assets
3	Where the Articles of Association of the company **do not permit** distribution of such
	profit as dividend
*	**Note 3 : Capital Reserve**
	Capital Reserve is a Reserve which **does not include** any amount regarded as free
	for distribution.
	Generally,
	only Profits or Surplus **of a capital nature** can be created as capital Reserve.
	Examples
1	Profits **Prior to Incorporation**
2	**(net)** Profit on **Re-issue** of Forfeited shares
3	**Excess of** Value of Net Assets Taken Over **(NATO)**
	over Purchase Consideration **(PC)** Paid for the **acquision of a business**.
4	Credit Balance in Capital Reduction A/c, when there has been a Reduction of Capital
	(**Internal Reconstruction**), with the consent of the court / NCLT.
5	Profits on **Redemption of Debentures,**
	where the distribution of such profits is **not permitted** by the A-O-A.
^	**Other conditions for Issue of Bonus Shares**
1	**Partly paid up shares**, if any, MUST be **made fully paid** up first
2	It is authorised by A-O-A of the company
3	It is, on recommendation of the Board, authorised in the general meeting of the company.
4	**Company has NOT defaulted in respect of the payment of**
	a) interest or principal in respect of Fixed deposits or debts issued by the company
	b) statutory dues of the employees (contribution to provident fund, gratuity, bonus)
5	Bonus, once announced / approved, shall not be withdrawn by the company.
6	Such other conditions as may be prescribed

Q. 1 : Following notes pertain to the Balance Sheet of Solid Ltd. as at 31st March, 2022:

	(₹)
Authorised Capital :	
10,000 12% Preference Shares of ₹10 each	1,00,000
1,00,000 Equity Shares of ₹10 each	10,00,000
	11,00,000
Issued and Subscribed Capital :	
8,000 12% Preference Shares of ₹10 each fully paid	80,000
90,000 Equity Shares of ₹10 each, ₹8 paid up	7,20,000
Reserves and Surplus :	
General reserve	1,60,000
Revaluation reserve	35,000
Securities premium (collected in cash)	20,000
Profit and Loss Account	2,05,000
Secured Loan:	
12% Debentures @ ₹100 each	5,00,000

On 1st April, 2022 the company has made final call @ ₹2 each on 90,000 equity shares. The call money was received by 20th April, 2022. Thereafter the company decided to capitalise its reserves by way of bonus at the rate of one share for every four shares held. Show necessary entries in the books of the company and prepare the extract of the Balance Sheet immediately after bonus issue assuming that the company has passed necessary resolution at its general body meeting for increasing the authorised capital.

Q. 2 : The following notes pertain to Jayaram Ltd's Balance Sheet as at 31st March :

Notes	(₹) in Lakhs
(1) Share Capital	
Authorised :	
20 crore shares of ₹10 each	20,000
Issued and Subscribed :	
10 crore Equity Shares of ₹10 each	10,000
2 crore 11% Cumulative Preference Shares of ₹10 each	2,000
Called and paid up:	
10 crore Equity Shares of ₹10 each, ₹8 per share called & paid up	8,000
2 crore 11% Cumulative Preference Shares of ₹10 each, fully called and paid up	2,000

	10,000
(2) Reserves and Surplus :	
Capital Reserve	485
Capital Redemption Reserve	1,000
Securities Premium	2,000
General Reserve	1,040
Surplus i.e. credit balance of Profit & Loss (Appropriation) A/c	273
	4,798

On 2 nd April, the Company made Final Call on Equity Shares at Rs. 2 per Share. The entire money was received in the month of April.

On 1 st June, the Company decided to issue Equity Shareholders Bonus Shares at the rate of 2 Shares for every 5 Shares held and for this purpose, it decided to utilise the Capital Reserves to the maximum possible extent.

Pass Journal entries for all the above mentioned transactions.

Also prepare the notes on Share Capital and Reserves and Surplus relevant to the Balance Sheet of the Company immediately after the issue of Bonus Shares.

^ **Q. 3 :** The Balance Sheet of Harihara Ltd.as at 31st March, having Net Assets 17,00,000 contained the following :

Liabilities	(₹)
Share Capital :	
Authorised Capital :	
1,50,000 Equity Shares of 10 each	15,00,000
Issued, Subscribed & Paid up:	
80,000 Equity Shares of ₹ 7.50 each called up & paid-up	6,00,000
Reserves :	
Capital Redemption Reserve	1,50,000
Plant Revaluation Reserve	20,000
Securities Premium	1,50,000
Development Rebate Reserve	2,30,000
Investment Allowance Reserve	2,50,000
General Reserve	3,00,000
	17,00,000

The Company wanted to issue bonus shares to its shareholders at the rate of one share for every two shares held. Necessary resolutions were passed, requisite legal requirements were complied with.

You are required to -

(a) Give effect to the proposal by passing journal entries in the books of the company,

(b) Show the amended Balance Sheet.

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^ **Q. 4 :** The following is the Balance Sheet of Indra Limited as at 31st March -

Sources of Funds	(₹)	Application of Funds:	(₹)
Authorized Capital :		Property, Plant & Equipment	7,80,000
50,000 Equity Shares of		Investments	4,90,000
₹ 10 each	5,00,000	(Market Value ₹ 5,80,000)	
10,000 Preference Shares		Deferred Tax Assets	4,80,000
of ₹ 100 each	10,00,000	Sundry Debtors	6,20,000
Issued and Paid Up :		Cash & Bank Balances	2,80,000
30,000 Equity Shares of			
₹ 10 each	3,00,000		
5,000 8% Preference Shares			
of ₹ 100 each	5,00,000		
Reserves & Surplus :			
Securities Premium	6,00,000		
General Reserve	6,50,000		
Profit & Loss A/c	1,80,000		
2,500 9% Debentures of			
₹ 100 each	2,50,000		
Sundry Creditors	1,70,000		
	26,50,000		**26,50,000**

In the Annual General Meeting held on 20th June, the Company passed the following resolutions:

(a) To split equity share of ₹10 each into 5 equity shares of ₹2 each from 1st July.

(b) To redeem 8% Preference Shares at a premium of 5%.

(c) To redeem 9% Debentures by making offer to Debentureholders to convert their holdings into equity shares at ₹10 per share or accept cash on redemption.

(d) To issue fully paid bonus shares in the ratio of one equity share for every 3 shares held on record date.

On 10th July, Investments were sold for ₹5,55,000 and Preference Shares were redeemed. 40% of Debenture holders exercised their option to accept cash and their claims were settled on 1st August. The Company fixed 5th September as Record Date, and Bonus Issue was concluded by 12th September.

Journalize the above transactions including cash transactions and prepare Balance Sheet Extract as at 30th September.

Q. 5 : The provisional Balance Sheet of Lavanya Ltd as at 31st March was as under:

Particulars	₹	₹	Particulars	₹	₹
Share Capital :			Property, Plant &		
50,000 Equity Shares of			Equipment		7,00,000
₹ 10 each, ₹ 7 per share			Cash and Bank		
called up	**3,50,000**		balances		2,00,000
Less : Calls in arrears on			Other Current		
10,000 shares at ₹2 per share	(20,000)		Assets		6,00,000
Add : Calls in advance on					
40,000 shares at ₹3 per share	1,20,000	4,50,000			
20,000 10% Redeemable					
Preference Shares of					
₹ 10 each		2,00,000			
Reserves and Surplus :					
General Reserve		3,00,000			
Profit and Loss A/c		2,70,000			
Current Liabilities		2,80,000			
		15,00,000			**15,00,000**

Calls in arrears are outstanding for 6 months. Calls in advance were received 6 months back. Interest at 10% p.a. on calls in advance and 12% p.a. on calls in arrears are allowed / charged. The Board of Directors have recommended that -

1. Dividend for the year be allowed at 20% on equity shares and paid immediately.
2. Calls in Advance be refunded and partly paid equity shares be converted as fully paid up by declaring bonus dividend to shareholders.
3. Preference Shares, which are redeemable at a premium of 10%, may be redeemed by issue of 10% Debentures of ₹ 100 each. Preference Dividend is paid immediately and prior to redemption.

Show Journal Entries to give effect to the above proposals including payment and receipt of cash and re-draft the Profit and Loss A/c and Balance Sheet of the Company. (Ignore taxation)

Q. 6 : The following is the Balance Sheet of Maheswar Ltd at the beginning of a financial year -

Equity and Liabilities	(₹)	Assets	(₹)
Authorised Capital :		**Tangible Assets**	
10,000 10% Redeemable		Gross Block 3,00,000	
Pref. Shares of ₹ 10 each	1,00,000	Less: Depreciation (1,00,000)	
90,000 Equity Shares of		Net Block	2,00,000
₹ 10 each	9,00,000	**Investments**	1,00,000
	10,00,000	**Current Assets, Loans and**	
Paid Up Capital :		**Advances:**	
10,000 10% Redeemable		Inventory	45,000
Pref. Shares of ₹ 10 each	1,00,000	Debtors	25,000
10,000 Equity Shares of		Cash and Bank balances	50,000
₹ 10 each	1,00,000		
	2,00,000		
Reserves and Surplus :			
General Reserve	1,20,000		
Securities Premium	70,000		
Profit and Loss A/c	18,500		
CL and Provisions	11,500		
	4,20,000		**4,20,000**

For the current financial year, the company made a net profit of ₹ 15,000 after providing ₹40,000 depreciation. The following additional information is available with regard to company's operations -

1. Preference Dividend for the current year ended 31st March was paid before the end of the year.
2. Except Cash and Bank, other Current Assets and Current Liabilities as at the end of the year was the same as at the beginning of the year.
3. The Company redeemed the Preference Shares at a premium of 10%. Assume that Securities Premium A/c is usable for providing the premium on redemption of preference shares.
4. The Company issued bonus shares of one share for every equity share held as at the end of the year.
5. To meet the cash requirements of redemption, the Company sold a portion of the Investments, so as to leave a minimum balance of ₹30,000 after such redemption.
6. Investments were sold at 90% of cost as at the end of the year.

You are required to :

1. Prepare necessary journal entries to record redemption and issue of bonus shares.
2. Prepare the Cash and Bank A/c.
3. Prepare the Balance Sheet as at the end of the year incorporating the above.

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Q. 7 : The following is the Balance Sheet of R Limited as at 31st March -

Sources of Funds	(₹)	Application of Funds	(₹)
Authorized Capital :		Property, Plant & Equipment	31,60,000
1,50,000 Equity Shares of		Investments	14,70,000
₹10 each	15,00,000	(Market Value ₹ 17,40,000)	
30,000 Preference Shares of		Sundry Debtors	17,60,000
₹ 100 each	30,00,000	Cash & Bank Balances	5,42,500
Issued and Paid Up Capital :			
90,000 Equity Shares of			
₹ 10 each	9,00,000		
15,000 Preference Shares of			
₹ 100 each	15,00,000		
Reserves & Surplus :			
Securities Premium	18,00,000		
General Reserve	16,50,000		
Profit & Loss A/c	1,20,000		
7,500 9% Debentures of			
₹ 100 each	7,50,000		
Sundry Creditors	2,12,500		
	69,32,500		**69,32,500**

In the Annual General Meeting held on 15th May, the Company passed the following resolutions :

(a) To redeem 10% Preference Shares at a premium of 5%.

(b) To redeem 9% Debentures by making offer to debenture holders to convert their holdings into equity shares at ₹40 per share or accept cash on redemption.

(c) To issue fully paid bonus shares in the ratio of one equity share for every 3 shares held on 31st March.

(d) Redemption of preference shares and debentures will be paid through company's cash & bank balance subject to leaving a minimum cash & bank balance of ₹ 2,00,000.

(e) To issue sufficient number of equity shares @ ₹40 per share as required to finance redemption of Preference Shareholders and Debenture holders.

On 5 June, Investments were sold for 16,80,000 & preference shares were redeemed. 30% of Debenture holders exercised their option to accept cash and their claims were settled on 1st August. The bonus issue was concluded by 10th August.

You are required to journalize the above transactions including cash transactions and Balance Sheet as at 30th September.

All working notes should form part of your answer.

Right Issue of Shares

^ **When a company intends to issue new shares**, since it needs additional capital for business, Companies Act, 2013 allows existing shareholders (except few exceptions) to preserve their position (financial & governance interest in the company), by offering those newly issued shares at the first instance to them.

The existing shareholders **are given a right** to subscribe these shares, if they like so, **so that** voting and governance rights of the existing shareholders is not diluted.

Such **right** to subscribe new shares is in **proportion** to their existing holding for shares.

Normally, such right issue of shares **is at discounted price** from the current market price, to evoke positive response as well as to reward the existing shareholders.

Unless the A-O-A of the company specifically prohibits, they have an implicit right to renounce (transfer) this right in favour of anyone else.

In other words, the existing shareholders have right of first refusal, i.e. they have a right to **either** subscribe for these shares **or** sell their rights **or** reject the offer.

^ **Accounting** for Right Issue **is exactly same** as that of Issue of Shares to Public.

^ **Right of Renunciation**

It refers to the right of the shareholder to surrender his right to buy the securities and transfer such right to any other person (by selling it to such other person).

* **Value of right**

The renunciation of the right is valuable & can be monetised by the existing shareholders in well-functioning capital market.

The monetised value available to the existing shareholders due to the right issue is known as **'value of right'**

Ex. 3 : Existing Issued and Subscribed capital of the company is 1,00,000 shares. Company makes a right issue of 10,000 shares (1 share for every 10 shares held). Hence, Mr. X, an existing shareholder, holding 1,000 shares **may subscribe** to this 100 shares **as matter of right**, in which case his % holding will remain same at 1%. **If X doesn't want to subscribe for this right shares**, he may renounce the right in favour of anyone else, say Mr. Y, in which case such 100 shares will be issued to Y, at the insistence of X. X **may** charge Y for this privilege, which is technically termed as the **value of right**.

* **Cum-right Market Price**

The market price, which exists before the right issue, is termed as Cum-right M.P.

* **Ex-right Market Price**

The market price of the shares after the right issue of shares is termed as Ex-right M.P.

* **Value of Right**

= Cum-right Market Price per share **Less** Ex-right Market Price per share

* **Theoratically** (in well functioning capital market),

the value of company's shares after a rights issue

must be equal to

the sum of market capitalisation prior to rights issue

and the cash inflows generated from the rights issue.

* **Continuing Ex. 3**

Existing Capital : 1,00,000 shares × 10 (face value) = ₹10,00,000

Right Issue : 10,000 shares at ₹14 per share

Cum-right Market Price per share = ₹25

Current holding of Mr. X = 1,000 shares

Cum-right market value of all shares = 1,00,000 × 25 = ₹25,00,000

Ex-right value of all shares = 25,00,000 + (10,000 × 14) = ₹26,40,000

Ex-right value per share = 26,40,000 / 1,10,000 = ₹24 per share.

Value of right = 25 - 24 = **₹1 per share**

^ **Q. 8 :** A company offers new shares of ₹100 each at 25% premium to existing shareholders on one for four basis. The cum-right market price of a share is ₹150. Calculate the value of a right. What should be the ex-right market price of a share?

^ **Q. 9 :** A company has decided to increase its existing share capital by making rights issue to its existing shareholders. The company is offering one new share for every two shares held by the shareholder. The market value of the share is ₹240 and the company is offering one share of ₹120 each. Calculate the value of a right. What should be the ex-right market price of a share?

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^ **Q. 10 :** A Ltd company having share capital of 25,000 equity shares of ₹10 each decides to issue rights share at the ratio of 1 for every 4 shares held at par value. Assuming all the share holders accepted the rights issue and all money was duly received, pass journal entries in the books of the company.

^ **Q. 11 :** Following notes pertain to the Balance Sheet of Mars Company Limited as at 31st March 2022:

	(₹)
Authorised Capital :	
50,000 12% Preference Shares of ₹10 each	5,00,000
5,00,000 Equity Shares of ₹10 each	50,00,000
	55,00,000
Issued and Subscribed Capital :	
50,000 12% Preference shares of ₹10 each fully paid	5,00,000
4,00,000 Equity shares of ₹10 each, ₹8 paid up	32,00,000
Reserves and Surplus :	
General Reserve	1,60,000
Capital Redemption Reserve	2,40,000
Securities premium (collected in cash)	2,75,000
Revaluation Reserve	1,00,000
Profit and Loss Account	16,00,000

On 1st April, 2022, the Company has made final call @ ₹2 each on 4,00,000 equity shares. The call money was received by 25th April, 2022. Thereafter, on 1st May 2022 the company decided to capitalise its reserves by way of bonus at the rate of one share for every four shares held, it decided that there should be minimum reduction in free reserves. On 1st June 2022, the Company issued Rights shares at the rate of two shares for every five shares held on that date at issue price of ₹12 per share. All the rights shares were accepted by the existing shareholders and the money was duly received by 20th June 2022. Show necessary journal entries in the books of the company for bonus issue and rights issue.

^ **Q. 12 :** The share of Galaxy Ltd of a face value of ₹10 is being quoted at ₹24. The company has a plan to make a rights issue of one equity share for every four shares currently held at a premium of 40% per Share. You are required to -

1. Determine the Minimum Price that can be expected of share after the issue.
2. Calculate the Theoretical Value of the Rights alone.
3. Show the effect of the right issue on the wealth of a shareholder who has 1,500 Shares, if (a) He sells the entire rights, and (b) He ignores the rights.

^ **Try Yourself : Objectives**

* **State True or False with reasons**

1 Earning per share gets increased after bonus issue.

2 Issued share capital including issue of rights shares and bonus shares may be more than the Authorised Capital.

3 Rights issue of shares results in decrease of market value of per share in comparison to market price before rights issue.

4 Right shares are normally offered at a price more than the cum-right value of the hare, causing dilution in its value post-right issue.

Answers :

1 **False**

Earnings per share gets decreased after bonus issue.

2 **False**

Issued share capital including issue of rights shares and bonus shares is always less than or equal to Authorised capital.

3 **True**

Rights issue of shares results in decrease of market value of per share in comparison to market price before rights issue.

4 **False**

Right shares are normally offered at a price less than the cum-right value of the share, causing dilution in its value post-right issue.

* **Multiple Choice Questions**

1 Which of the following cannot be used for issue of bonus shares as per the Companies Act?

(a) Securities premium account

(b) Revaluation reserve

(c) Capital redemption reserve

2 Which of the following statements is true with regard to declaring and issuing of Bonus Shares?

(a) Assets are transferred from the company to the shareholders.

(b) A Bonus issue results in decrease in reserves and surplus.

(c) A Bonus issue is same as declaration of dividends.

3	Which of the following statement is true in case of bonus issue?
	(a) Convertible debenture holders will get bonus shares in same proportion as to the existing shareholders.
	(b) Bonus shares may be issued to convertible debenture holders at the time of conversion of such debentures into shares.
	(c) Both (a) and (b).
4	Bonus issue is also known as
	(a) Scrip issue. (b) Capitalisation issue. (c) Both (a) and (b).
5	The bonus issue is not made unless
	(a) Partly paid shares are made fully paid up.
	(b) It is provided in its articles of association
	(c) Both (a) and (b).
6	Bonus issue has the following effect
	(a) Market price gets adjusted on issue of bonus shares.
	(b) Effective Earnings per share, Book Value and other per share values stand increased.
	(c) Markets generally take the action as an unfavourable act.
7	ABC Co. Ltd resolved to issue bonus shares. Which of the following is not a pre-requisite for issuance of bonus shares?
	(a) Authorization in Articles of Association.
	(b) Timely Payment of statutory dues of employees such as PF, Gratuity etc.
	(c) Sufficient balance in bank account of company.
8	In case of further issue of shares, the right to renounce the shares in favour of a third party
	(a) Must include a right exercisable by the person concerned to renounce the shares;
	(b) Should include a right exercisable by the person concerned to renounce the shares;
	(c) Is deemed to include a right exercisable by the person concerned to renounce the shares (subject to the provisions under the articles of the company).
9	A company's share's face value is ₹10, book value is ₹20, Right issue price is ₹30 and Market price is ₹40, while recording the issue of right share, the securities premium will be credited with
	(a) ₹10 (b) ₹20 (c) ₹30

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10 A. Right shares enable existing shareholders to maintain their proportional holding in the company.

B. Right share issue does not cause dilution in the market value of the share.

Which of the option is correct?

(a) A-Correct; B Correct (b) A – Incorrect; B Correct (c) A - Correct; B – Incorrect

11 Ex-Rights price can be calculated by which of these formulas?

(a) (Cum rights value of the existing shares + Rights share issue proceeds)/ (existing number of shares + No. of right shares).

(b) (Cum rights value of the existing shares + Rights share issue proceeds) X (existing number of shares + No. of right shares).

(c) (Cum rights value of the existing shares - Rights share issue proceeds)/ (existing number of shares – No. of right shares).

Answers :

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

^ **Theoretical Questions**

1 What is meant by Bonus issue? Explain its related provisions as per the Companies Act, 2013.

2 Explain the financial effects of a further issue of equity shares on the market value of the share.

3 What are the advantages and disadvantages of a rights issue?

4 What is meant by renunciation of rights shares by existing shareholder?

Answers :

1 Bonus Issue means an offer of free additional shares to existing shareholders.

A company may decide to distribute further shares as an alternative to increase the dividend pay-out.

A bonus share may be defined as issue of shares at no cost to current shareholders in a company, based upon the number of shares that the shareholder already owns. In other words, no new funds are raised with a bonus issue. While the issue of bonus shares increases the total number of shares issued and owned, it does not increase the net worth of the company. Although the total number of issued shares increases, the ratio of number of shares held by each shareholder remains constant.

Bonus issue is also known as 'capitalisation of profits'. Capitalisation of profits refers to the process of converting profits or reserves into paid up capital. A company may

capitalise its profits or reserves which otherwise are available for distribution as dividends among the members by issuing fully paid bonus shares to the members.

Provisions of the Companies Act, 2013

Section 63 of the Companies Act, 2013 deals with the issue of bonus shares.

According to Sub-section (1) of Section 63, a company may issue fully paid-up bonus shares to its members, in any manner whatsoever, out of -

(i) its free reserves;

(ii) the securities premium account; or

(iii) the capital redemption reserve account:

Provided that no issue of bonus shares shall be made by capitalising reserves created by the revaluation of assets.

Sub-section (2) of Section 63 provides that no company shall capitalise its profits or reserves for the purpose of issuing fully paid-up bonus shares under sub-section (1), unless -

(a) it is authorised by its articles;

(b) it has, on the recommendation of the Board, been authorised in the general meeting of the company;

(c) it has not defaulted in payment of interest or principal in respect of fixed deposits or debt securities issued by it;

(d) it has not defaulted in respect of the payment of statutory dues of the employees, such as, contribution to provident fund, gratuity and bonus;

(e) the partly paid-up shares, if any outstanding on the date of allotment, are made fully paid-up.

(f) it complies with such conditions as may be prescribed

The company which has once announced the decision of its Board recommending a bonus issue, shall not subsequently withdraw the same.

Sub-section (3) of the Section also provides that the bonus shares shall not be issued in lieu of dividend.

2 The financial position of a business is contained in the balance sheet. Further issue of shares increases the amount of share capital as well as the liquid resources (Bank). The amount of share capital issued is the product of further number of shares issued multiplied by issue price. The issue price may be higher than the face value (issue at a premium).

3 Rights issue is an issue of rights to a company's existing shareholders that entitles them to buy additional shares directly from the company in proportion to their existing holdings, within a fixed time period.

Advantages of Right Issue

1. Right issue enables the existing shareholders to maintain their proportional holding in the company and retain their financial and governance rights. It works as a deterrent to the management, which may like to issue shares to known persons with a view to have a better control over the company's affairs.
2. In well-functioning capital markets, the right issue necessarily leads to dilution in the value of share. However, the existing shareholders are not affected by it because getting new shares at a discounted value from their cum-right value will compensate decrease in the value of shares. The cum-right value is maintained otherwise also, if the existing shareholders renounce their right in favour of a third party.
3. Right issue is a natural hedge against the issue expenses normally incurred by the company in relation to public issue.
4. Right issue has an image enhancement effect, as public and shareholders view it positively.
5. The chance of success of a right issue is better than that of a general public issue and is logistically much easier to handle.

Disadvantages of Right Issue

1. The right issue invariably leads to dilution in the market value of the share of the company.
2. The attractive price of the right issue should be objectively assessed against its true worth to ensure that you get a bargained deal.

4 In a situation where existing shareholder does not intend to subscribe to the rights issue of a company, he may give up his right in favour of another person for a consideration. Such giving up of rights is called renunciation of rights.

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347



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346



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344



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338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



NEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
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SORABH MOHATA
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SANA DESHPANDE
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MEETALI MAHESHWARI
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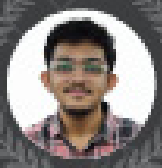
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328



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325



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323



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319



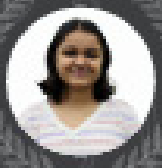
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319



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316



RIDHI PAREKH
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314



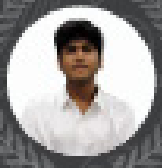
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313



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311



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308



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305



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JUHI KAJARIA
CA INTER MAY'22

AIR 13



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
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AIR 46



PRANJAL MEHDIRA
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AIR 46



SANJEEV JAIN
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AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

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SANKRUTI PAROLIA
CA FINAL NOV'23

AIR 2



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHABRIA
CA FINAL NOV'23
AIR 32



PINAL KHETAN
CA FINAL NOV'23
AIR 35



SHOURYA TIBREWALA
CA FINAL MAY'22
AIR 39



DEEPAK LADHA
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AIR 40



HIMANSHU KHATRI
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AIR 41



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^ **Redemption of** Redeemable **Debentures (ROD)**

Based on the **Terms of the IOD**,
Debentures are usually redeemable (Liability on debentures can be settled)
in any of the following ways

1) At the end of the stipulated period **i.e.** after a fixed number of years
2) Anytime after a certain number of years has elapsed since their issue
3) In equal annual instalments (redemption by annual drawing)

Such debentures can be redeemable
either by payment in cash or by conversion into shares or combination of both

* **Note :** A Company may **purchase its own debentures** from the open market,
when such debentures are **quoted at a discount** on the stock exchange.
It may be profitable for company **to purchase and cancel** them.
ROD by purchase of own debentures is **specifically excluded** at Foundation level.

^ **Debenture Redemption Reserve (DRR)**

A Company issuing debentures **may be** required to create DRR **out of** Divisible Profits.
An appropriate amount is transferred from profits every year to DRR and then,
is invested in specified earmarked securities. **This is repeated every year.**
Such Investments are called : Debenture Redemption Reserve Investment **(DRRI).**

In the last year or **at the time of ROD,**
DRRI are encashed and amount so obtained is used for ROD.

^ **Journal Entries** for ROD through creation of DRR

* At the end of first year

1 **Annual appropriation / creation of DRR**

2 **For Investing in earmarked securities**

*	At the end of second & subsequent years					
1	**For receipt of Interest on DRRI**					
2	**For transfer of Interest on DRRI**					
	Note : In the absence of information, assume fund to be non-cumulative.					
3	**Annual appropriation / creation of DRR**					
4	**For Investing in earmarked securities**					
*	At the end of second & subsequent years					
1	**For receipt of Interest on DRRI**					
2	**For transfer of Interest on DRRI**					
3	**For Sale / Disposal / Encashment of DRRI**					
4	**Transfer of Profit on sale**					

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OR						
4	**Transfer of Loss on sale**					
5	**For ROD due / payable**					
6	**To write off Premium on ROD,** if not recorded **at the time of IOD**					
7	**For Payment to Debenture holders**					
8	**Close DRR A/c**					

^ **Adequacy of DRR**

Companies, except exempt companies, are required to ensure DRR shall be **atleast 10% of value of Outstanding Debentures**

^ **Investment in Earmarked / Specified Securities**

Companies, except exempt companies, **must invest** or **deposit**, on or before 30th April each year, **atleast 15%** of the Nominal / Face value of its debentures **maturing during** the year ending on the **31 st March of the next year**

** Provided that the amount remaining deposited or invested, shall not at anytime fall below 15% of the amount of Debentures maturing during the 31 st day of March of next year.

		DRR	DRRI
I	All India Financial Institutions (AIFIs)	Exempt	Exempt
	Banking Companies		
	Other Financial Institutions		
II	Listed registered NBFC's		Yes
	Listed registered HFC's		
	Other Listed Companies		
III	Unlisted registered NBFC's		Exempt
	Unlisted registered HFC's		
	Other Unlisted Companies	Yes	

In case of **Partly** Convertible Debentures,

DRR shall be created in respect of **non-convertible** portion of Debenture Issue.

^ **Q. 1 :** Libra Limited (a listed company) recently made a public issue in respect of which the following information is available :

(a) No. of partly convertible debentures issued - 2,00,000;
face value and issue price - ₹100 per debenture.

(b) Convertible portion per debenture - 60%, date of conversion - on expiry of 6 months from the date of closing of issue.

(c) Date of closure of subscription lists - 1.5.2021, date of allotment - 1.6.2021, rate of interest on debenture - 15% payable from the date of allotment, value of equity share for the purpose of conversion - 60 (Face Value 10).

(d) No. of debentures applied for - 1,50,000.

(e) Interest payable on debentures half-yearly on 30th September and 31st March.

Write relevant journal entries for all transactions arising out of the above during the year ended 31st March, 2022 (including cash and bank entries).

Q. 2 : Case Ltd. (unlisted company other than AIFI, Banking company, NBFC and HFC) provides the following information as at 31st March, 2022:

Particulars	(₹)
Shareholder's Funds	
(a) Share Capital	
Authorized share capital:	
45,000 equity shares of ₹10 each fully paid	4,50,000
Issued and subscribed share capital:	
30,000 equity shares of ₹10 each fully paid	3,00,000
(b) Reserves and Surplus	
Profit & Loss Account	1,62,000
Debenture Redemption Reserve	18,000
Non-current liabilities	
(a) Long term borrowings	
12% Debentures	1,80,000
Current Liabilities	
(a) Trade payables	1,72,500
Non-current assets	
(a) Property, Plant and Equipment (Freehold property)	1,72,500
(b) Non-current Investment : DRR Investment	27,000
Current assets	
(a) Inventories	2,02,500
(b) Trade receivables	1,12,500
(c) Cash and bank balances:	
Cash at bank	2,73,000
Cash in hand	45,000

At the Annual General Meeting on 1.4.2022, it was resolved:

(a) To give existing shareholders the option to purchase one ₹10 share at ₹15 for every four shares (held prior to the bonus distribution). This option was taken up by all the shareholders.

(b) To issue one bonus share for every five shares held.

(c) To repay the debentures at a premium of 3%.

Give the necessary journal entries for these transactions.

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Q. 3 : The Balance Sheet of BEE Co. Ltd. (unlisted company other than AIFI, Banking company, NBFC and HFC) as at 31st March, 2021 is as under:

Particulars	Note No	(₹)
I. Equity and liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,00,000
(b) Reserves and Surplus	2	1,20,000
(2) Non-current liabilities		
(a) Long term borrowings	3	1,20,000
(3) Current Liabilities		
(a) Trade payables		1,15,000
		5,55,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	4	1,15,000
(2) Current assets		
(a) Inventories		1,35,000
(b) Trade receivables		75,000
(c) Cash and bank balances	5	2,30,000
		5,55,000

Notes to Accounts

			(₹)
1	**Share Capital**		
	Authorised share capital		
	30,000 shares of ₹10 each fully paid		3,00,000
	Issued and subscribed share capital		
	20,000 shares of ₹10 each fully paid		2,00,000
2	**Reserve and Surplus**		
	Profit & Loss Account		1,20,000
3	**Long term borrowings**		
	12% Debentures		1,20,000
4	**Property, Plant and Equipment**		
	Freehold property		1,15,000
5	**Cash and bank balances**		
	Cash at bank	2,00,000	
	Cash in hand	30,000	2,30,000

At the Annual General Meeting, it was resolved:

(a) To give existing shareholders the option to purchase one ₹10 share at ₹15 for every four shares (held prior to the bonus distribution). This option was taken up by all the shareholders.

(b) To issue one bonus share for every five shares held.

(c) To repay the debentures at a premium of 3%.

Give the necessary journal entries for these transactions.

^ **Q. 4 :** The following balances appeared in the books of Paradise Ltd (unlisted company other than AIFI, Banking company, NBFC and HFC) as on 1-4-2021:

(i) 12% Debentures ₹ 7,50,000

(ii) Balance of DRR ₹25,000

(iii) DRR Investment ₹1,12,500 represented by 10% ₹1,125 Secured Bonds of the Government of India of ₹100 each.

Annual contribution to the DRR was made on 31st March every year. On 31-3-2022, balance at bank was ₹7,50,000 before receipt of interest. The investment were realised at par for redemption of debentures at a premium of 10% on the above date.

You are required to prepare the following accounts for the year ended 31st March, 2022:

(1) Debentures Account

(2) DRR Account

(3) DRR Investment Account

(4) Bank Account

(5) Debenture Holders Account.

^ **Q. 5 :** The following balances appeared in the books of a company (unlisted company other than AIFI, Banking company, NBFC and HFC) as on December 31, 2021 :

6% Mortgage 10,000 debentures of ₹100 each; Debenture Redemption Reserve (for redemption of debentures) ₹50,000; Investments in deposits with a scheduled bank, free from any charge or lien ₹1,50,000 at interest 4% p.a. receivable on 31st December every year. Bank balance with the company is ₹9,00,000.

The Interest on debentures had been paid up to December 31, 2021.

On February 28, 2022, the investments were realised at par and the debentures were paid off at ₹101, together with accrued interest.

Write up the concerned ledger accounts.

Q. 6 : The summarized Balance Sheet of Krishna Ltd (Listed) as on 31st March is as under :

Liabilities	(₹)	Assets	(₹)
4,00,000 Equity Shares of		Property, Plant & Equipment	
₹ 10 each fully paid up	40,00,000	(at Cost less Depreciation)	1,50,00,000
General Reserve	50,00,000	Debenture Redemption	
Debenture Redemption Reserve	35,00,000	Reserve Investments	30,00,000
12% Convertible Debentures,		Cash and Bank Balances	40,00,000
80,000 Debentures of ₹100	80,00,000	Other Current Assets	1,20,00,000
Other Loans	45,00,000		
Current Liabilities and			
Provisions	90,00,000		
	3,40,00,000		**3,40,00,000**

The Debentures are due for redemption on 1st April. The terms of issue of debentures provided that they were redeemable at a premium 5% and also conferred option to the Debentureholders to convert 25% of their holding into equity shares at a pre-determined price of ₹11.90 per share, and the balance payment in cash. Assuming that:

(i) Except for Debentureholders holding 12,000 Debentures in aggregate, the rest of them exercised the option for maximum conversion,

(ii) The Investments realized ₹ 32,00,000 on sale,

(iii) All the transactions were taken place in 1st April, without any lag, and

(iv) Premium on redemption of debentures is to be adjusted against General Reserve.

Redraft the Balance Sheet of Krishna Ltd as on 1st April after giving effect to the redemption. Show your calculations in respect of the number of equity shares to be allotted and the cash payment necessary.

Q. 7 : The Balance Sheet of Ram Limited on 31st March, was as follows:

Equity & Liabilities	(₹)	Assets	(₹)
Share Capital :		Property, Plant & Equipment	8,00,000
Authorised Capital :		Debenture Redemption	
50,000 Equity Shares of		Investments	2,00,000
₹10 each	5,00,000		
Issued Capital :		Cash Balance	2,50,000
25,000 Equity Shares of		Other Current Assets	10,00,000
₹10 fully paid up	2,50,000		
Reserves and Surplus :			
General Reserve	2,75,000		
Profit & Loss A/c	1,00,000		

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Debenture Redemption				
Reserve	2,50,000			
Secured Loans :				
Other Secured Loans	2,50,000			
12% Convertible Debentures	5,00,000			
(5,000 Deb. of ₹ 100 each)				
Current Liabilities and				
Provisions	6,00,000			
Dividend	25,000			
	22,50,000			**22,50,000**

At the General Meeting, it was resolved to -

1. Pay dividend of 10% in cash.
2. Give existing shareholders, the option to purchase one share of ₹ 10 each at ₹15 for every five shares held. This option was taken up by all the shareholders.
3. Redeem the debentures at a premium of 5% and also confer option to the Debentureholders to convert 50% of their holding into equity shares at a pre-determined price of ₹15 per share and balance payment to be made in cash.
4. Holders of 3,000 Debentures opted to get their debentures redeemed in cash only while the rest opted for getting the same converted into equity shares as per the terms of issue. Debenture Redemption Investments realized ₹1,80,000 on sales.

You are required to redraft the Balance Sheet after giving effects to the Rights Issue and Redemption of Debentures. Also show the calculations in respect of number of equity shares issued and cash payment.

^ **Q. 8 :** M Limited recently made a public issue of Debentures. The following information is available in respect of the issue -

(i) 3,00,000 Partly Convertible Debentures of face value and issue price of ₹ 100 per debenture were issued.
(ii) Conversion of 50% of each debenture is to be done on expiry of 6 months from date of close of issue.
(iii) Date of closure of subscription list is 1st June. Date of allotment is 1st July.
(iv) Interest on Debentures at the rate of 12% is payable from the date of allotment.
(v) Equity Share of ₹ 10 each are issued at 50 per share for the purpose of conversion.
(vi) Underwriting Commission is 2%.
(vii) 2,25,000 Debentures were applied for.
(viii) Interest on Debentures is payable half-yearly on 30th September and 31st March.

Give journal entries for all transactions relating to above, including Cash & Bank entries for the year ended 31st March.

^	**Try Yourself : Objectives**
*	**State True or False with reasons**
1	Amounts credited to the debenture redemption reserve may be utilised by the company for any purpose.
2	All India Financial Institutions (AIFIs) regulated by Reserve Bank of India and Banking Companies for both public as well as privately placed debentures need not create any Debenture Redemption Reserve (DRR).
3	Under payment in instalments method, the payment of entire debenture is made in one lot.
4	At redemption of debentures, DRR should be transferred to general reserve.
	Answers :
1	**False**
	Amounts credited to the debenture redemption reserve should not be utilised by the company for any purpose except for the purpose other than for redemption of debentures.
2	**True**
	All India Financial Institutions (AIFIs) regulated by Reserve Bank of India and Banking Companies for both public as well as privately placed debentures need not create any DRR.
3	**False**
	under payment in instalments method, the payment of specified portion of debentures are made in instalments at specified intervals.
4	**True**
	DRR is transferred to general reserve at the time of redemption of debentures.
*	**Multiple Choice Questions**
1	Which of the following statements is true?
	(a) A debenture holder is an owner of the company.
	(b) A debenture holder can get his money back only on the liquidation of the company.
	(c) A debenture issued at a discount can be redeemed at a premium.
2	Which of the following statements is false?
	(a) Debentures can be redeemed by payment in lump sum at the end of a specified period.
	(b) Debentures cannot be redeemed during the life time of the company.
	(c) Debentures can be redeemed by payments in annual instalments.

3 For debentures issued by unlisted companies (other than AIFIs, Banking companies, NBFCs and HFCs), Debentures Redemption reserve will be considered adequate if it is:

(a) 25% of the value of debentures issued through public issue.

(b) 10% of the value of debentures issued through public issue.

(c) 5% of the value of debentures issued through public issue.

Answers :

1	(c)		2	(b)		3	(b)

* **Theoretical Questions**

1 What is meant by redemption of debentures? Explain.

2 Write short note on Debenture Redemption Reserve.

Answers :

1 Debentures are usually redeemable i.e. either redeemed in cash or convertible after a time period.

Redeemable debentures may be redeemed :

- after a fixed number of years; or
- any time after a certain number of years has elapsed since their issue; or
- on giving a specified notice; or
- by annual drawing.

A company may also purchase its debentures, as and when convenient, in the open market. When the debentures are quoted at a discount on the Stock Exchange, it may be profitable for the company to purchase and cancel them.

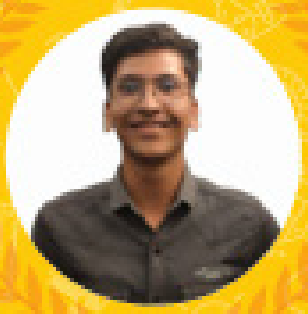
2 A company issuing debentures may be required to create a debenture redemption reserve account out of the profits available for distribution of dividend and amounts credited to such account cannot be utilised by the company except for redemption of debentures. Such an arrangement would ensure that the company will have sufficient liquid funds for the redemption of debentures at the time they fall due for payment.

An appropriate amount is transferred from profits every year to Debenture Redemption Reserve and its investment is termed as Debenture Redemption Reserve Investment (or Debenture Redemption Fund). In the last year or at the time of redemption of debentures, Debenture Redemption Reserve Investments are encashed and the amount so obtained is used for the redemption of debentures.

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CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



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321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



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310



LOKESH PAWAR
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SOHAM SHAH
307



GAURANG SHAH
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HEMIL SATUNDA
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ESAKKIMUTHU DAS
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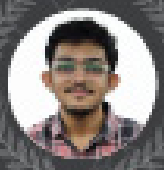
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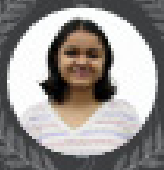
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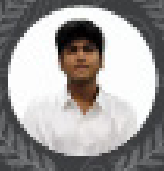
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SCAN ME!

^ MEANING AND SCOPE OF ACCOUNTING

* Meaning of Accounting :

The Committee on Terminology set up by the American Institute of Certified Public Accountants formulated the following definition of accounting in 1961 :

"Accounting is the art of recording, classifying, and summarising in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the result thereof."

The American Accounting Association in 1966 treated accounting as :

"The process of identifying, measuring and communicating economic information to permit informed judgments and decisions by the users of accounts."

In 1970, the Accounting Principles Board (APB) of American Institute of Certified Public Accountants (AICPA) enumerated the functions of accounting as follows :

"The function of accounting is to provide quantitative information, primarily of financial nature, about economic entities, that is needed to be useful in making economic decisions."

Thus, accounting may be defined as the process of recording, classifying, summarising, analysing and interpreting the financial transactions and communicating the results thereof to the persons interested in such information.

* Procedural aspects of Accounting

On the basis of the above definitions, procedure of accounting can be basically divided into two parts :

(i) Generating financial information and

(ii) Using the financial information.

Generating financial information

1. Recording
2. Classifying
3. Summarising
4. Analysing
5. Interpreting
6. Communicating

Using the financial information

Accounting is **often regarded as** a language of business.

Since the main aim of a language is **to serve as a** means of communication, accounting communicates the result of business activities to various interested parties like owners (present investors), management, creditors, lenders, government etc.

Accounting information is **used by different groups** of people having vested interests in a business organization. They use accounting information in order to satisfy some of their varied needs for information. They are called **Users** of accounting information.

Such users can be classified into two groups

1. Internal users (owners & management)
2. External users (creditors / lenders, potential investors, employees, government agencies, tax authorities, researchers, competitors, social responsibility groups like environment protection groups)

Different users may need accounting information for different purposes.

* **Evolution of Accounting**

In ancient times, Barter system was followed in trade.

Gradually, Hundis replaced barter system and later money came into existence.

As the money became the medium of trade settlements, accounting came into existence.

In India, Chanakya, also known as Kautilya, the Chief Minister in the court of Chandragupta Maurya, the first emperor of India, wrote the manuscript similar to Financial Management Book, titled 'Arthshastra'. It had detailed aspects of maintaining books of account of a Sovereign State. It is considered to be the first Indian authentic manuscript on accounting.

The first phase of accounting can be attributed to 15th century although it is believed that in 14th century, double entry book keeping was widely used in Italy.

Fra Luca Pacioli is considered to be the architect of **Double Entry Book Keeping,** who laid the foundation of Double Entry system of Book keeping / Accounting which is widely used today. The method developed by Pacioli was widely used in western Europe and became an accepted standard system of accounting.

The second phase of accounting can be attributed to the era when owners began conducting business through managers. Owners provided capital for the business

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and appointed managers to manage the business under their supervision and directions. Controls were exercised on managers through accounting and reporting.

The third phase & present stage of accounting is attributed to the development of Joint Stock Companies from about the year 1600 as the requirement of capital increased. It built wider stakeholders seeking financial information. This led to accounting for Internal (management accounting) and external (financial accounting) purposes.

Subsequently, as business grew and also the stakeholders, accounting and disclosure requirements set in along with external attestation i.e. Audit and later Accounting Standards (guidelines) were formulated.

* **Objectives of Accounting**

1. **Systematic recording of transactions –** Basic objective of accounting is to systematically record the financial aspects of business transactions, i.e., book-keeping. These recorded transactions are later on classified and summarized logically for the preparation of financial statements and for their analysis and interpretation.

2. **Ascertainment of results of above recorded transactions** – Accountant prepares profit and loss account to know the results of business operations for a particular period of time. If revenue (sales) exceeds expenses then it is said that business is running profitably but if expenses exceed revenue, then it can be said that business is running under loss. The profit and loss account helps the management and different stakeholders in taking rational decisions. For example, if business is not proved to be remunerative or profitable, the cause of such a state of affair can be investigated by the management for taking remedial steps.

3. **Ascertainment of the financial position of the business –** A businessman is not only interested in knowing the results of the business in terms of profits or loss for a particular period but is also anxious to know that what he owes (liability) to the outsiders and what he owns (assets) on a certain date. To know this, accountant prepares a financial position statement popularly known as Balance Sheet. The balance sheet is a statement of assets and liabilities of the business point of time and helps in ascertaining the financial health of the business.

4. **Providing information to the users for rational decision-making –** Accounting as a 'language of business' communicates the financial results of an enterprise to various stakeholders by means of financial statements. Accounting aims to meet the information needs of the decision-makers and helps them in rational decision-making.

5. **To know the solvency position –** By preparing the balance sheet, management not only reveals what is owned and owed by the enterprise, but also it gives the information regarding concern's ability to meet its liabilities in the short run (liquidity position) and also in the long-run (solvency position) as and when they fall due.

* Functions of Accounting

The main functions of accounting are as follows:

(a) **Measurement :** Accounting measures past performance of the business entity and depicts its current financial position.

(b) **Forecasting :** Accounting helps in forecasting future performance and financial position of the enterprise using past data and analysing trends.

(c) **Decision-making :** Accounting provides relevant information to the users of accounts to aid rational decision-making.

(d) **Comparison & Evaluation :** Accounting assesses performance achieved in relation to targets and discloses information regarding accounting policies and contingent liabilities which play an important role in predicting, comparing and evaluating the financial results.

(e) **Control :** Accounting also identifies weaknesses of the operational system and provides feedbacks regarding effectiveness of measures adopted to check such weaknesses.

(f) **Government Regulation and Taxation :** Accounting provides necessary information to the government to exercise control on the entity as well as in collection of tax revenues.

* Book Keeping (BK)

BK is an **art** of recording business transactions in the s**cientific** manner so that up-to-date information is available at any point of time.

BK, **as part of Accounting**, means recording of financial transactions & events in a systematic manner in the books of accounts (i.e. Journal & Ledger).

BK is the **science** & **art** of recording correctly in the books of accounts all those business transactions that result in transfer of money or money's worth.

Thus, **BK is concerned with**

i) Identifying financial transactions & events

ii) Measuring them in terms of money

iii) Recording them in **Primary Book of Account** called Journal

iv) Posting them in **Secondary Book of Account called** Ledger

Objectives of Book-keeping

1. **Complete recording of transactions –** It is concerned with complete and permanent record of all transactions in a systematic and logical manner to show its financial effect on the business.
2. **Ascertainment of financial effect on the business –** It is concerned with the combined effect of all the transactions made during the accounting period upon the financial position of the business as a whole.

* **Distinction between Book-Keeping and Accounting**

No.	Book-keeping	Accounting
1	It is a process concerned with recording of transactions.	It is a process concerned with summarising of the recorded transactions.
2	It constitutes as a base for accounting.	It is considered as a language of the business.
3	Financial statements do not form part of this process.	Financial statements are prepared in this process on the basis of book-keeping records.
4	Managerial decisions cannot be taken with the help of these records.	Management takes decisions on the basis of these records.
5	There is no sub-field of book- keeping.	It has several sub-fields like financial accounting, management accounting cost accounting etc.
6	Financial position of the business cannot be ascertained through book-keeping records.	Financial position of the business is ascertained on the basis of the accounting reports.

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Sub-fields of Accounting

The various sub-fields of accounting are :

(i) **Financial Accounting** – It covers the preparation and interpretation of financial statements and communication to the users of accounts. It is historical in nature as it records transactions which had already been occurred. The final step of financial accounting is the preparation of Profit and Loss Account and the Balance Sheet. It primarily helps in determination of the net result for an accounting period and the financial position as on the given date.

(ii) **Management Accounting –** It is concerned with internal reporting to the managers of a business unit. To discharge the functions of stewardship, planning, control and decision- making, the management needs variety of information. The different ways of grouping information and preparing reports as desired by managers for discharging their functions are referred to as management accounting. A very important component of the management accounting is cost accounting which deals with cost ascertainment and cost control. Management Accounting will be dealt with at higher levels of the Chartered Accountancy Course.

(iii) **Cost Accounting –** The terminology of Cost Accounting published by the Institute of Cost and Management Accountants of England defines cost accounting as: "the process of accounting for cost which begins with the recording of income and expenditure or the bases on which they are calculated and ends with the preparation of periodical statements and reports for ascertaining and controlling costs."

(iv) **Social Responsibility Accounting** – The demand for social responsibility accounting stems from increasing social awareness about the undesirable by products of economic activities. As already discussed earlier, social responsibility accounting is concerned with accounting for social costs incurred by the enterprise and social benefits created.

(v) **Human Resource Accounting** – Human resource accounting is an attempt to identify, quantify and report investments made in human resources of an organisation that are not presently accounted for under conventional accounting practice.

* Basis of Accounting or Methods of Accounting

One of the main objective of Accounting is to find out Profit or Loss of a business enterprise at the end of accounting period.

Profit or Loss **for a particular period** can be calculated **by comparing** Incomes & Expenses

Profit = Incomes less Expenses
Loss = Expenses less Incomes

It is quite possible that **particular income** becomes due (legally becomes receivable) in one accounting period **but money is actually received** in other accounting period.

Likewise, **particular expense** becomes due (obligation to pay arises) in one accounting period **but money is actually paid** in other accounting period.

So, the question arises as to **in such cases**,

Income and Expense should be considered / recorded in which accounting period ?

It **depends upon** the basis of accounting followed by the enterprise.

There are, mainly, two basis of accounting (methods to find out Profit or Loss)

1. Cash Basis of Accounting
2. Accrual Basis of Accounting (Mercantile Basis of Accounting)

1 Cash Basis of Accounting

Under this method / basis of accounting,
transactions are recorded in books of accounts on cash basis
i.e. receipt and payment basis.

It means Revenues (Incomes) are recognised as Incomes in the year in which money is received.
Likewise, Expenses are recognised as expenses in the year in which money is paid.

Advantages of Cash basis of Accounting

1. This basis of accounting is simple, as no adjustments are required to be made for prepraring final accounts.
2. This method is more objective as very few estimates and personal judgements are required.
3. It is suitable for those enterprises where most of the transactions are on cash basis.

Disadvantages of Cash basis of Accounting

1. It **does not give** True and Fair view of the profit or loss and the financial position of an enterprise because **it ignores** one of the fundamental accounting assumption i.e. accrual concept. This method **completely ignores** outstanding expenses, outstanding incomes, prepaid expenses and pre received incomes
2. It does not follow Matching Concept of accounting
   It does not make distinction between Capital and Revenue items.
   As a result, there is no consistency in profits of two years.
   Hence, not suitable for Intra firm and Inter firm comparisions.
3. There is great possibility of profits manipulation, by preponing or postponing payments &/or receipts.

Disadvantages of this basis **far overweighs** its advantages,

Hence, this basis is **not recognised by** The Companies Act, 2013 since it is not reliable basis of accounting.

Some professional people, small ventures of temporary period, some non-trading organisations or institutions with service motive, small traders etc maintains their books of accounts by following cash basis of accounting.

2 Accrual Basis of Accounting

Under this method / basis of accounting,
transactions are recorded in books of accounts on accrual basis i.e. due basis

It means Revenues (Incomes) are recognised as Incomes in the year in which it becomes due i.e. when goods are sold &/or services are rendered (we get legal right to receive such amount)

Likewise, Expenses are recognised as expenses in the year in expenses becomes due i.e. amount becomes legally payable

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Advantages of Accrual basis of Accounting

1. It is more scientific and comprehensive method of accounting and hence is preferred by most accountants.
2. This method discloses correct profit or loss for a particular period & also exhibits true financial position, as it follows accrual concept, matching concept, makes distinction between capital & revenue items.
3. This method is consistent in computation of profit & hence is suitable for intra firm & Inter firm comparision.

Disadvantages of Accrual basis of Accounting

1. This basis of accounting is technical / comparatively complicated, as various adjustments are required to be made while preparing final accounts.
2. This method requires the use of estimates and personal judgements.

Since its advantages **far overweighs** its drawbacks, it has **wider acceptability** and followed virtually by all commercial establishments (business enterprises with profit motive)

Also, this basis **is recognised** by the Companies Act, 2013

3 **Hybrid or Mixed Basis of Accounting**

This method is combination of above 2 methods, it can be considered as third method. Cash basis of accounting is simple whereas the accrual basis of accounting is scientifc and reliable. So, accountants have tried to club these advantages of the two systems and have come up with mixed or hybrid basis of accounting.

Under this method, both cash basis and accrual basis are followed.
Incomes are recorded on Cash basis where as
Expenses are recorded on Accrual basis.

This is the **most conservative basis** of ascertaining profit because all expenses relating to the period are considered whether actually paid or not where as Incomes are recorded only when actually received. Usually, professionals like doctors, lawyers etc. follows this method, **though not widely used**.

It is advisable to follow basis of accounting regularly & consistently, every year.

^ **ACCOUNTING CONCEPTS, CONVENTIONS AND PRINCIPLES**

Accounting is an **information system** and its main aim is to provide **financial information**. Unlike in past when such financial information was largely needed by the proprietor(s) of the business, these days such information is also needed / useful to various Internal & External users, who have vested interest in the business. Such users includes Proprietor(s) / Owners, Management, Investors, Creditors / Lenders, Employees, Government & Others.

Business **communicates through** financial statements, which are prepared following **GAAP / Accounting Policies / Accounting Concepts,** so that they are understood in uniform manner by all the users.
(**GAAP** : Generally Accepted Accounting Principles)

* **GAAP / Accounting Policies / Accounting Concepts**

These are set of rules / guidelines **which are to be followed** for preparing financial statements / Books of Accounts.

These are the **guidelines developed** over a period of time to bring **Uniformity**, **Consistency / Comparability & Reliability** to the process of accounting (preparation & presentation of financial statements) in order to enhance its utility to various users of accounting information.

In order to make Accounting / Financial statements / information meaningful to various users, it is significant that such information is **reliable** as well as **comparable**. It is therefore necessary that such statements should be prepared according to some **standard language & set rules**. These rules are usually called as **GAAP**.

GAAP are combination of

i) Accounting Standards (issued by the Institute of Chartered Accountants of India) &
ii) Commonly accepted practices

* **Importance of Accounting Concepts**

1) Reliable financial statements
2) Uniformity in presentation
3) Generally acceptable basis of measurement
4) Proper information to all concerned
5) Valid and appropriate assumptions

1) **Entity Concept :**

Business is an Accounting Entity & transactions are recorded in the books from the point of view of business. According to this concept, business is always considered as **distinct & separate** from the owners of the business. Business unit should have completely separate set of books and we have to record business transactions from firm's (businesses) point of view & not from the point of view of proprietor of the business. The financial position & performance (profit or loss) of a business **cannot be known** in the absence of this concept.

Because of this concept of separate entity,
the proprietors personal assets, liabilities, expenses & incomes are kept separate from the accounts of the business.

If the proprietor has **some other business entity** doing similar business in some other area or some other business, the records / accounts of that business should also be kept separate. This concept applies to **all forms of business organizations** i.e. Sole Proprietorship, Partnership or a Company.

2) **Money Measurement Concept**

According to this concept,
Only those transactions are recorded in the books which are capable of being expressed in terms of money.
To make accounting records relevant, simple, understandable & homogeneous, they are expressed in **common unit of measurement** i.e. money.

Since money serves as the medium of exchange, transactions expressed in money are recorded and the ruling currency of a country is the measuring unit for accounting.

Events like resignation / death of a key personnel, strike, quarrel with in the organization, launch of a better product by competitor etc. cannot be recorded in the books since it cannot be expressed in terms of money. **Despite of these events being important & may adversely impact business in long term if not dealt with properly,** they cannot be recorded in the books since these facts or happenings cannot be expressed in terms of money.

3) **Periodicity Concept**

This is also called the concept of **definite accounting period**. As per going concern concept an **indefinite life of the entity is assumed**. For a business entity it causes

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inconvenience to measure performance achieved by the entity in the ordinary course of business.

If a textile mill lasts for 100 years, it is not desirable to measure its performance as well as financial position only at the end of its life.

So, a small but workable fraction of time is chosen out of infinite life cycle of the business entity for measuring performance and looking at the financial position.

Generally, one year period is taken up for performance measurement and appraisal of financial position. However, it may also be 6 months or 9 months or 15 months.

According to this concept accounts should be prepared after every period & not at the end of the life of the entity. Usually, this period is one calendar year. We generally follow from 1st April of a year to 31st March of the immediately following year.

Thus, for performance appraisal it is not necessary to look into the revenue and expenses of an unduly long time-frame. This concept makes the accounting system workable and the term 'accrual' meaningful. If one thinks of indefinite time-frame, nothing will accrue. There cannot be unpaid expenses and non-receipt of revenue.

Accrued expenses or accrued revenue is only with reference to a finite time-frame which is called accounting period.

Thus, the periodicity concept facilitates in :

(i) Comparing of financial statements of different periods

(ii) Uniform and consistent accounting treatment for ascertaining the profit and assets of the business

(iii) Matching periodic revenues with expenses for getting correct results of the business operations

4) Accrual Concept

As per this concept,

Incomes are recognised / recorded as income as soon as they are earned / **accrued** (becomes receivable), irrespective of whether they are received in the current accounting period / year or not.

Likewise,

Expenses are recorded as expense as soon as they are **accrued** (becomes payable), irrespective of whether they are paid in the current period or not.

On the basis of this concept,

adjustments are made in books of accounts for Outstanding and Pre-paid expenses, Outstanding and Pre-received Incomes.

Also, due provisions are made for depreciation of the fixed assets, bad debts etc. relating to the accounting period.

5) Matching Concept

This concept is very important **for correct determination** of **net profit** for a particular accounting period.

According to this concept,

First, Revenues / Incomes are recognized for a particular accounting period

& then, all the costs incurred for generating such revenues should be recognized.

It means Revenues & Related costs **should be recognized in the same period.**

Since the accounts are usually prepared on accrual basis (accrual concept), the expenses incurred in a particular period are **matched** with the revenues recognized in that period.

In brief, Matching concept (principle) requires that **all the Revenues** earned during an accounting period, whether received in the same period or not and all the related costs incurred, whether paid in the same period or not, have to be taken into account while preparing Profit & Loss account for that period.

Similarly,

all the amounts **received or paid** during the current period but relating to next period or last period, should be **excluded from** current period's Revenues & Costs.

6) Going Concern Concept

As per this concept, the enterprise is **normally viewed** as a going concern i.e. as continuing in operation for the foreseeable future.

It is **assumed that** the enterprise has **neither** the intention **nor** the necessity of liquidation or of curtailing materially / substantially the scale of operations.

Going concern concept influences accounting practices in relation to valuation of assets and liabilities, depreciation of fixed assets etc.

For eg. assets are generally valued at historical cost. Any increase or decrease in the value of assets in the short period is ignored.

7) Cost Concept

According to this concept, an asset is ordinarily recorded in the books of account at the price at which it was acquired. This cost becomes the basis of all subsequent accounting for that asset. Since such acquisition cost **relates to past**, it is referred to as Historical cost.

For example

If a business entity purchases a building for total cost of ₹ 20,00,000 ; it will be recorded in the books of accounts at this figure. Subsequent increase or decrease in the market value would not be ordinarily recorded in the books of accounts since such building is intended to be used for longer period in the business.

Historical cost concept **doesn't mean** that assets will continue to be shown at its acquisition cost every year. Their cost is **systematically reduced** from year to year **by charging depreciation** & the assets are shown in the balance sheet at cost less depreciation i.e. at **Book values**.

8) **Realisation Concept** (covered by Accrual concept)

eg. A company gets an order for sale of goods ₹ 1,00,000 in May 2017.
Goods of only ₹ 60,000 are sold and delivered in June 2017.
Cash received ₹ 60,000 in Sept. 2017.
As per this concept, sale is to be recorded as Income in June 2017.

^ **Ex. 1 :** Mr. X purchased a piece of land on 1.1.1995 paying ₹ 2,000. Its current market value is ₹ 1,02,000 on 31.12.2022. Should the accountant show the land at ₹ 2,000 following cost concept and ignoring ₹1,00,000 value increase since it is not realised? If he does so, the financial position would be:

BALANCE SHEET

Liabilities	(₹)	Assets	(₹)
Capital	2,000	Land	2,000
	2,000		**2,000**

Is it not proper to show it in the following manner?

BALANCE SHEET

Liabilities	(₹)	Assets	(₹)
Capital	2,000	Land	1,02,000
Unrealised Gain	1,00,000		
	1,02,000		**1,02,000**

Now-a-days the revaluation of assets has become a widely accepted practice when the change in value is of permanent nature. Accountants adjust such value change through creation of revaluation (capital) reserve.

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9) Dual Aspect Concept

An **Accounting Equation** (AE) is a mathematical expression which shows that the assets of a firm are **always equal to** Liabilities due to a firm & capital contributed by the owner.

Assets = Liabilities (External) + Capital (Internal Liability)

AE signifies that the Assets of the business are always equal to the total of Liabilities & Capital. Any business transaction **will affect** both the sides of the AE **in such a way that** such equation will hold true after any number / type of business transactions.

This AE is based on **'Dual Aspect Concept'** which says that every business transaction affects minimum 2 A/c's, one A/c is debited & other A/c is credited i.e. for every debit, there is corresponding credit of the same amount.

It is the basis for Double Entry System (DES) of Accounting, i.e. system of recording transactions based on this concept / principle is called D.E.S. of Accounting.

Ex. 2 : **BALANCE SHEET**

Liabilities	(₹)	Assets	(₹)
Capital	1,50,000	Machinery	2,00,000
Bank Loan	75,000	Cash	1,00,000
Other Loan	75,000		
	3,00,000		**3,00,000**

Transactions:

(a) A new machine is purchased paying ₹ 50,000 in cash.

(b) A new machine is purchased for ₹ 50,000 on credit, cash is to be paid later on.

(c) Cash paid to repay bank loan to the extent of ₹ 50,000.

(d) Raised bank loan of ₹ 50,000 to pay off other loan.

Effect of the Transactions:

(a) Increase in machine value and decrease in cash balance by ₹ 50,000.

BALANCE SHEET

Liabilities	(₹)	Assets	(₹)
Capital	1,50,000	Machinery	2,50,000
Bank Loan	75,000	Cash	50,000
Other Loan	75,000		
	3,00,000		**3,00,000**

(b) Increase in machine value and increase in creditors by ₹ 50,000

BALANCE SHEET

Liabilities	(₹)	Assets	(₹)
Capital	1,50,000	Machinery	2,50,000
Creditors for machinery	50,000	Cash	1,00,000
Bank Loan	75,000		
Other Loan	75,000		
	3,50,000		**3,50,000**

(c) Decrease in bank loan and decrease in cash by ₹ 50,000.

BALANCE SHEET

Liabilities	(₹)	Assets	(₹)
Capital	1,50,000	Machinery	2,00,000
Bank Loan	25,000	Cash	50,000
Other Loan	75,000		
	2,50,000		**2,50,000**

(d) Increase in bank loan and decrease in other loan by ₹ 50,000.

BALANCE SHEET

Liabilities	(₹)	Assets	(₹)
Capital	1,50,000	Machinery	2,00,000
Bank Loan	1,25,000	Cash	1,00,000
Other Loan	25,000		
	3,00,000		**3,00,000**

We may conclude that every transaction and event has two aspects.

This gives basic accounting equation :

Equity (E) + Liabilities (L) = Assets (A) or

Equity (E)= Assets (A) – Liabilities(L)

Or, Equity + Long Term Liabilities + Current Liabilities = Fixed Assets + Current Assets

Or, Equity + Long Term Liabilities = Fixed Assets + (Current Assets – Current Liabilities)

Or, Equity = Fixed Assets + Working Capital – Long Term Liabilities

Ex: 3 : Develop the accounting equation from the following information:

Particulars	March 31, 2021	March 31, 2022
	(₹)	(₹)
Capital	1,00,000	?
12% Bank Loan	1,00,000	1,00,000
Trade Payables	75,000	70,000
Fixed Assets	1,25,000	1,10,000
Trade Receivables	75,000	80,000
Inventory	70,000	80,000
Cash & Bank	5,000	6,000

Required :

Find the profit for the year & prepare the Balance Sheet as on 31/3/2022.

Answers :

For the year ended March 31, 2021:

Equity = Capital ₹ 1,00,000

Liabilities = Bank Loan + Trade Payables

= ₹ 1,00,000 + ₹ 75,000

= ₹ 1,75,000

Assets = Fixed Assets + Trade Receivables + Inventory + Cash & Bank

= 1,25,000 + 75,000 + 70,000 + 5,000

= ₹ 2,75,000

Equity + Liabilities = Assets

₹ 1,00,000 + ₹ 1,75,000 = ₹ 2,75,000

For the year ended March 31, 2022:

Assets = ₹ 1,10,000 + ₹ 80,000 + ₹ 80,000 + ₹ 6,000 = ₹ 2,76,000

Liabilities = ₹ 1,00,000 + ₹ 70,000 = ₹ 1,70,000

Equity = Assets – Liabilities

= ₹ 2,76,000 – ₹ 1,70,000

= ₹ 1,06,000

Profits = New Equity – Old Equity

= ₹ 1,06,000 – ₹1,00,000

= ₹ 6,000

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10) Conservatism or Prudence Concept

According to this concept, all expected expenses & anticipated losses should be recorded in the books of accounts but all anticipated / unrealized gains should be ignored. This concept is many a times described by using the phrase

" Do not anticipate a profit but provide for all possible losses "

In other words, conservatism is the policy of playing safe.

Provision is made for all known liabilities & losses even though the amount can not be determined with certainty.

Examples of application of such concept

i) Closing stock is valued at cost price or net realizable value, whichever is lower.

ii) Provision for doubtful debts is created in anticipation of actual bad debts.

iii) Joint Life policy is shown only at surrender value as against the amount paid.

Effect of Concept of Conservatism

Such concept **should be used very cautiously** otherwise it will have two effects.

i) Profit & Loss A/c will show lower profits than actuals.

ii) Balance Sheet will disclose understated values of assets and overstated values of liabilities, in comparison to its actual values.

The above mentioned effects **will result in** creation of **Secret Reserves**, which is in direct conflict with the Concept of full disclosure.

11) Consistency Concept

As per this concept,

it is assumed that the **accounting policies** are consistent from one period to another.

Any policy adopted for accounting should be continuous or consistent and it need not be changed generally unless and until circumstances demand.

eg. Method followed for charging depreciation on fixed assets

Any change in the accounting policies which has **material effect** in the current period or which is reasonably expected to have material effect in later periods should be disclosed.

12) **Materiality Concept**

According to this convention,
financial statements (final accounts) should disclose all material items which might influence the decisions of the users of financial statements.
According to this concept, items having an insignificant impact or being irrelevant to the user **need not** be disclosed. The unimportant items are either being left out or **mostly** are to be merged with other items so that accounting statements are not unnecessarily over burdened.

The term materiality is subjective in nature. Materiality depends on the amount involved in the transaction, size of the business, nature of information etc.
An item material to one person or one business may be immaterial to another person.

* **Fundamental Accounting Assumptions**

Certain fundamental accounting assumptions underlie the preparation and presentation of financial statements. They are usually not specifically stated because their acceptance and use are assumed. Disclosure is necessary if they are not followed.

The following have been generally accepted as fundamental accounting assumptions :

(a) **Going Concern :** The enterprise is normally viewed as a going concern, that is, as continuing in operation for the foreseeable future. It is assumed that the enterprise has neither the intention nor the necessity of liquidation or of curtailing materially the scale of the operations.

(b) **Consistency :** It is assumed that accounting policies are consistent from one period to another.

(c) **Accrual :** Revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate.

* **Financial Statements (FS) / Accounting Statements**

Accounting is an **Information system** and its main aim is to provide **financial information**. **Unlike in past** when such financial information was largely needed by the proprietor(s) of the business, these days such information is also needed / useful to various Internal & External users, who have vested interest in the business. Such users includes Proprietor(s) / Owners, Management, Investors, Creditors / Lenders, Employees, Government & Others.

Such financial information is provided through set of **financial statements**, namely, **Profit & Loss A/c and Balance Sheet**. These are also called **Final Accounts**.

* **Qualitative characteristics of financial statements**

1. Understandability
2. Relevance
3. Reliability
4. Comparability
5. Materiality
6. Faithful Representation
7. Substance over Form
8. Neutrality
9. Prudence
10. Full, fair and adequate disclosure
11. Completeness

The four principal qualitative characteristics are understandability, relevance, reliability and comparability.

^ **CAPITAL AND REVENUE EXPENDITURES AND RECEIPTS**

* **Capital Expenditure**

This expenditure is incurred to acquire fixed asset **or** to increase the value of fixed asset. It gives the benefit for a long period of time and it is generally non recurring in nature.

eg. Purchase of Machinery, Extention of Building, Immediate repairs to second hand Motor car purchased etc.

* **Revenue Expenditure**

These are those expenses whose benefit is exhausted fully in the same accounting period in which it is incurred. It doesn't increase profit earning capacity of business. These are normal day to day business expenses and are shown on the debit side of Trading or Profit & Loss A/c. Such expenses doesn't have disposal / saleable value.

eg. Salary, Rent, Commission, Audit fees, Repairs etc.

* **Considerations in determining capital and revenue expenditures**

The basic considerations in distinction between capital and revenue expenditures are:

(a) **Nature of business** : For a trader dealing in furniture, purchase of furniture is revenue expenditure but for any other trade, the purchase of furniture should be treated as capital expenditure and shown in the balance sheet as asset. Therefore, the nature of business is a very important criteria in separating an expenditure between capital and revenue.

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(b) **Recurring nature of expenditure :** If the frequency of an expense is quite often in an accounting year then it is said to be an expenditure of revenue nature while non-recurring expenditure is infrequent in nature and do not occur often in an accounting year. Monthly salary or rent is the example of revenue expenditure as they are incurred every month while purchase of assets is not the transaction done regularly therefore, classified as capital expenditure unless materiality criteria defines it as revenue expenditure.

(c) **Purpose of expenses :** Expenses for repairs of machine may be incurred in course of normal maintenance of the asset. Such expenses are revenue in nature. On the other hand, expenditure incurred for major repair of the asset so as to increase its productive capacity is capital in nature. However, determination of the cost of maintenance and ordinary repairs which should be expensed, as opposed to a cost which ought to be capitalised, is not always simple.

(d) **Effect on revenue generating capacity of business :** The expenses which help to generate income/ revenue in the current period are revenue in nature and should be matched against the revenue earned in the current period. On the other hand, if expenditure helps to generate revenue over more than one accounting period, it is generally called capital expenditure.

When expenditure on improvements and repair of a fixed asset is done, it has to be charged to Profit and Loss Account if the expected future benefits from fixed assets do not change, and it will be included in book value of fixed asset, where the expected future benefits from assets increase.

(e) **Materiality of the amount involved :** Relative proportion of the amount involved is another important consideration in distinction between revenue and capital.

* **Key differences between Capital and Revenue Expenditures**

Key Differences	Capital Expenditure	Revenue Expenditure
Period of benefit	Any expenditure incurred to provide a benefit over a long- term period is capital expenditure.	Any expenditure incurred to provide a benefit during the current period is revenue expenditure.
Enhancement vs Maintenance	Capital expenditure is incurred for the purpose of **increasing the capacity** of the business. Alternatively, it also includes	Revenue expenditure is incurred to **maintain the earning capacity** of the business.

	an expenditure to **reduce** the	
	costs of the business.	
Examples	Purchase of machine, car,	Repairs and maintenance, salary
	furniture, etc.	of accounting staff, etc.

^ **Q. 1 :** Good Pictures Ltd., constructs a cinema house and incurs the following expenditure during the first year ending 31st March, 2022.

(1) Second-hand furniture worth ₹ 9,000 was purchased; repainting of the furniture costs ₹ 1,000. The furniture was installed by own workmen, wages for this being ₹ 200.

(2) Expenses in connection with obtaining a license for running the cinema worth ₹ 20,000. During the course of the year the cinema company was fined ₹ 1,000, for contravening rules. Renewal fee ₹ 2,000 for next year also paid.

(3) Fire insurance, ₹ 1,000 was paid on 1st October, 2021 for one year.

(4) Temporary huts were constructed costing ₹ 1,200. They were necessary for the construction of the cinema. They were demolished when the cinema was ready.

Point out how you would classify the above items.

Answers :

(1) The total cost of the furniture should be treated as ₹ 10,200 i.e., all the amounts mentioned should be capitalised since without such expenditure the furniture would not be available for use. If ₹ 1,000 and ₹ 200 have been respectively debited to the Repairs Account and the Wages Account, these accounts will be credited to the Furniture Account.

(2) License for running the cinema house is necessary, hence its cost should be capitalised. But the fine of ₹ 1,000 is revenue expenditure. The renewal fee for the next year is also revenue expenditure but pertains to the next year; hence, it is a prepaid expense.

(3) Half of the insurance premium pertains to the year beginning on 1st April, 2021. Hence such amount should be treated as prepaid expense. The remaining amount is revenue expense for the current year.

(4) Since the temporary huts were necessary for the construction, their cost should be added to the cost of the cinema hall and thus capitalised.

^ **Q. 2 :** State with reasons, how you would classify the following items of expenditure:

(1) Overhauling expenses of ₹ 25,000 for the engine of a motor car to get better fuel efficiency.

(2) Inauguration expenses of ₹ 25 lacs incurred on the opening of a new manufacturing unit in an existing business.

(3) Compensation of ₹ 2.5 crores paid to workers, who opted for voluntary retirement.

Answers :

(1) Overhauling expenses are incurred for the engine of a motor car to derive better fuel efficiency. These expenses will reduce the running cost in future and thus the benefit is in form of endurable long-term advantage.
So this expenditure should be capitalised.

(2) Inauguration expenses incurred on the opening of a new unit may help to explore more customers This expenditure is in the nature of revenue expenditure, as the expenditure may not generate any enduring benefit to the business over more than one accounting period.

(3) The amount paid to workers on voluntary retirement is in the nature of revenue expenditure. Since the magnitude of the amount of expenditure is very significant, it may be better to defer it over future years.

^ **Q. 3 :** State with reasons whether the following are Capital or Revenue Expenditure:

(1) Expenses incurred in connection with obtaining a license for starting the factory for ₹ 10,000.

(2) ₹ 1,000 paid for removal of inventory to a new site.

(3) Rings and Pistons of an engine were changed at a cost of ₹ 5,000 to get fuel efficiency.

(4) Money paid to Mahanagar Telephone Nigam Ltd. (MTNL) ₹ 8,000 for installing telephone in the office.

(5) A factory shed was constructed at a cost of ₹ 1,00,000. A sum of ₹ 5,000 had been incurred in the construction of temporary huts for storing building material.

Answers :

(1) Money paid ₹ 10,000 for obtaining license to start a factory is a capital expenditure.
This is an item of expenditure incurred to acquire the right to carry on business.

(2) ₹ 1,000 paid for removal of inventory to a new site is revenue expenditure.
This is neither bringing enduring benefit nor enhancing the value of the asset.

(3) ₹ 5,000 spent in changing Rings and Pistons of an engine to get fuel efficiency is capital expenditure. This is an expenditure on improvement of a fixed asset. It results in increasing profit-earning capacity of the business by cost reduction.

(4) Money deposited with MTNL for installation of telephone in office is not expenditure.
This is treated as an asset and the same is adjusted over a period of time against actual telephone bills.

(5) Cost of construction of building including cost of temporary huts is capital expenditure.
Building is fixed asset which will generate enduring benefit to the business over more than one accounting period. Construction of temporary huts is incidental to the main construction. Such cost is also capitalised with the cost of building.

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Q. 4 : State with reasons whether the following statements are 'True' or 'False'.

(1) Overhaul expenses of second-hand machinery purchased are Revenue Expenditure.

(2) Money spent to reduce working expenses is Revenue Expenditure.

(3) Legal fees to acquire property is Capital Expenditure.

(4) Amount spent as lawyer's fee to defend a suit claiming that the firm's factory site belonged to the plaintiff's land is Capital Expenditure.

(5) Amount spent for replacement of worn out part of machine is Capital Expenditure.

(6) Expense incurred on the repairs and white washing for the first time on purchase of an old building are Revenue Expenses.

(7) Expenses in connection with obtaining a license for running the cinema is Capital Expenditure.

(8) Amount spent for the construction of temporary huts, which were necessary for construction of the Cinema House and were demolished when the cinema house was ready, is Capital Expenditure.

Answers :

(1) **False:** Overhaul expenses are incurred to put second-hand machinery in working condition to derive endurable long-term advantage. So it should be capitalised.

(2) **False:** It may be reasonably presumed that money spent for reducing revenue expenditure would have generated long-term benefits to the entity. So this is capital expenditure.

(3) **True:** Legal fee paid to acquire any property is part of the cost of that property. It is incurred to possess the ownership right of the property and hence a capital expenditure.

(4) **False:** Legal expenses incurred to defend a suit claiming that the firm's factory site belongs to the plaintiff is maintenance expenditure of the asset. By this expense, neither any endurable benefit can be obtained in future in addition to that what is presently available nor the capacity of the asset will be increased. Maintenance expenditure in relation to an asset is revenue expenditure.

(5) **False:** Amount spent for replacement of any worn out part of a machine is revenue expense since it is part of its maintenance cost.

(6) **False:** Repairing and white washing expenses for the first time of an old building are incurred to put the building in usable condition. These are the part of the cost of building. Accordingly, these are capital expenditure.

(7) **True:** The Cinema Hall could not be started without license. Expenditure incurred to obtain the license is pre-operative expense which is capitalised. Such expenses are amortised over a period of time.

(8) **True:** Cost of temporary huts constructed which were necessary for the construction of the cinema house is part of the construction cost of the cinema house. Therefore such costs are to be capitalised.

Q. 5 : Are the following expenditures capital in nature?

(1) M/s ABC & Co. run a restaurant. They renovate some of the old cabins. Because of this renovation some space was made free and number of cabins was increased from 10 to 13. The total expenditure was ₹ 20,000.

(2) M/s New Delhi Financing Co. sold certain goods on installment payment basis. Five customers did not pay installments. To recover such outstanding installments, the firm spent ₹ 10,000 on account of legal expenses.

(3) M/s Ballav & Co. of Delhi purchased a machinery from M/s Shah & Co. of Ahmedabad. M/s Ballav & Co. spent ₹ 40,000 for transportation of such machinery. The year ending is 31st Dec, 2022.

Answers :

(1) Renovation of cabins increased the number of cabins. This has an effect on the future revenue generating capability of the business. Thus, the renovation expense is capital expenditure in nature.

(2) Expense incurred to recover installments due from customer do not increase the revenue generating capability in future. It is a normal recurring expense of the business. Thus, the legal expenses incurred in this case is revenue expenditure in nature.

(3) Expenses incurred on account of transportation of fixed asset is capital expenditure in nature.

Try Yourself : Q. 6 :

State with reasons, how you would classify the following items of expenditure:

(1) Overhauling expenses of ₹ 25,000 for the engine of a motor car to get better fuel efficiency.

(2) Inauguration expenses of ₹ 25 lacs incurred on the opening of a new manufacturing unit in an existing business.

(3) Compensation of ₹ 2.5 crores paid to workers, who opted for voluntary retirement.

Answers :

(1) Overhauling expenses are incurred for the engine of a motor car to derive better fuel efficiency. These expenses will reduce the running cost in future and thus the benefit is in form of endurable long-term advantage. So this expenditure should be capitalised.

(2) Inauguration expenses incurred on the opening of a new unit may help to explore more customers This expenditure is in the nature of revenue expenditure, as the expenditure may not generate any enduring benefit to the business over more than one accounting period.

(3) The amount paid to workers on voluntary retirement is in the nature of revenue expenditure. Since the magnitude of the amount of expenditure is very significant, it may be better to defer it over future years.

^ **Try Yourself : Q.7 :**

Classify the following expenditures as capital or revenue expenditure

1. Amount spent on making a few more exists in a Cinema Hall to comply with Government orders.
2. Cost of repairs on second-hand car purchased to bring it into working condition.
3. Complete repaint of existing building.
4. Installation of a new central heating system.
5. Repainting of a delivery van.
6. Providing drainage for a new piece of water-extraction equipment.
7. Legal fees on the acquisition of land.
8. Carriage costs on a replacement part for a piece of machinery.
9. ₹ 10,000 spent as import duty on machinery purchased.
10. Cost of testing whether the equipment is functioning properly.
11. An extension of railway tracks in the factory area.
12. Amount spent on painting the factory.
13. Payment of wages for building a new office extension.
14. Expenses incurred to keep the machine in working condition.
15. Registration fees paid at the time of purchase of a building.
16. Expenses incurred for advertisement in newspaper.
17. Amount spent on renewal fee of patent rights.

Answers :

1. Revenue Expenditure
2. Capital Expenditure
3. Revenue Expenditure
4. Capital Expenditure
5. Revenue Expenditure
6. Capital Expenditure
7. Capital Expenditure
8. Revenue Expenditure
9. Capital Expenditure
10. Capital Expenditure
11. Capital Expenditure **(because it will yield benefit for more than one accounting period)**
12. Revenue Expenditure **(because it has been incurred to maintain the factory building)**
13. Capital Expenditure
14. Revenue Expenditure

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15. Capital Expenditure
16. Revenue Expenditure
17. Revenue Expenditure

* **Capital Receipts and Revenue Receipts**

Just as a clear distinction between capital and revenue expenditure is necessary, in the same manner capital receipts must be distinguished from revenue receipts. Receipts which are obtained in course of normal business activities are revenue receipts (e.g., receipts from sale of goods or services, interest income etc.). On the other hand, receipts which are not revenue in nature are capital receipts (e.g., receipts from sale of fixed assets or investments, secured or unsecured loans, owners' contributions etc.). Revenue and capital receipts are recognised on accrual basis as soon as the right of receipt is established. Revenue receipts should not be equated with the actual cash receipts. Revenue receipts are credited to the Profit and Loss Account. On the other hand, Capital receipts are not directly credited to Profit and Loss Account.

^ **Q. 8 :** State with reasons whether the below items relating to the business of AB Ltd are capital or revenue receipts?

(a) A machine with a book value of ₹ 10 lakh is sold for ₹ 12 lakh.
(b) Premium amounting to ₹ 1 Lakh received on issue of shares
(c) An amount of ₹ 20,000 received from goods sold in cash.
(d) An amount of ₹ 5 lahhs received on the maturity of fixed deposit from bank. Also, an interest of ₹ 40,000 was received in addition to the maturity amount of the fixed deposits.

Answers :

(a) The amount of ₹ 12 lac is a capital receipt. There is a profit on sale of the machine to the extent of ₹ 2 lakhs (12 – 10).
(b) Premium received on issue of shares is an example of capital receipt.
(c) Amount received from cash sale is a revenue receipt.
(d) Amount received on the maturity of fixed deposit is the recovery of the deposit amount, and is a capital receipt. Interest income is an example of revenue receipt.

^ **Q. 9 :** Classify the following expenditures and receipts as capital or revenue:

(a) ₹ 10,000 spent as travelling expenses of the directors on trips abroad for purchase of capital assets.
(b) Amount received from Trade receivables during the year.
(c) Amount spent on demolition of building to construct a bigger building on the same site.
(d) Insurance claim received on account of a machinery damaged by fire.

SOLUTION

(a) Capital expenditure.

(b) Revenue receipt.

(c) Capital expenditure.

(d) Capital receipt.

^ **Try Yourself : Q.10 :** Classify the following as capital or revenue receipts:

1. Amount received from debtors during the year.
2. Insurance claim received on account of inventory damaged by fire.
3. Dividend received from XYZ limited during the year.
4. Subsidy received from the government for working capital by a manufacturing concern.

Answers :

1. Revenue Receipt
2. Revenue Receipt
3. Revenue Receipt
4. Revenue Receipt

^ **CONTINGENT ASSETS AND CONTINGENT LIABILITIES**

* **Contingent Asset**

A contingent asset is a **possible asset** that arises from **past events** the existence of which will be confirmed only by the **occurrence or non-occurrence** of one or more **uncertain future events** not wholly within the control of the enterprise.

An enterprise **should not recognise** a contingent asset.

Contingent assets usually arise from unplanned or other unexpected events that give rise to the possibility of an inflow of economic benefits to the enterprise. An example is a claim that an enterprise is pursuing through legal processes, where the outcome is uncertain.

Contingent assets are not recognised in financial statements since this may result in the recognition of income that may never be realised. However, when the realisation of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate.

A contingent asset is not disclosed in the financial statements. It is usually disclosed in the report of the approving authority (Board of Directors in the case of a company, and, the corresponding approving authority in the case of any other enterprise), where an inflow of economic benefits is probable.

Contingent assets are assessed continually and if it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs.

* Contingent Liabilities

The term 'Contingent liability' can be defined as

"(a) a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or

(b) a present obligation that arises from past events but is not recognised because :

(i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

(ii) a reliable estimate of the amount of the obligation cannot be made."

A contingent liability is a possible obligation arising from past events and may arise in future depending on the occurrence or non-occurrence of one or more uncertain future events. A contingent liability may also be a present obligation that arises from past events.

An enterprise should not recognise a contingent liability in balance sheet, however it is required to be disclosed in the notes to accounts, unless possibility of outflow of a resource embodying economic benefits is remote.

These liabilities are assessed continually to determine whether an outflow of resources embodying economic benefits has become probable. If it becomes probable that an outflow or future economic benefits will be required for an item previously dealt with as a contingent liability,

a provision is recognised in financial statements of the period in which the change in probability occurs except in the extremely rare circumstances where no reliable estimate can be made.

* Distinction between Contingent Liabilities and Provisions

Provision means "any amount written off or retained by way of providing for depreciation, enewal or diminution in the value of assets or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy".

It is important to know the difference between provisions and contingent liabilities.

The distinction between both of them can be explained as follows:

	Provision	Contingent liability
1	Provision is a present liability of uncertain amount, which can be measured reliably by using a substantial degree of estimation.	A Contingent liability is a possible obligation that may or may not crystallise depending on the occurrence or non- occurrence of one or more uncertain future events.
2	A provision meets the recognition criteria.	A contingent liability fails to meet the same.

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3	Provision is recognised when (a) an enterprise has a present obligation arising from past events; an outflow of resources embodying economic benefits is probable, and (b) a reliable estimate can be made of the amount of the obligation.	Contingent liability includes present obligations that do not meet the recognition criteria because either it is not probable that settlement of those obligations will require outflow of economic benefits, or the amount cannot be reliably estimated.
4	If the management estimates that it is probable that the settlement of an obligation will result in outflow of economic benefits, it recognises a provision in the balance sheet.	If the management estimates, that it is less likely that any economic benefit will outflow the firm to settle the obligation, it discloses the obligation as a contingent liability.

		Existence of Liability	Amount of Liability
1	**Contingent Liability**	**Uncertain**	
2	**Provision**	**Certain**	**Uncertain**
3	**Liability**	**Certain**	

ACCOUNTING POLICIES

The accounting policies refer to the specific accounting principles and the methods of applying those principles adopted by the enterprise in the preparation and presentation of financial statements.

There is no single list of accounting policies which are applicable to all circumstances. The differing circumstances in which enterprises operate in a situation of diverse and complex economic activity make alternative accounting principles and methods of applying those principles acceptable. The choice of the appropriate accounting principles and the methods of applying those principles in the specific circumstances of each enterprise calls for considerable judgement by the management of the enterprise.

The following are examples of the areas in which different accounting policies may be adopted by different enterprises:

(a) Methods of depreciation, depletion and amortisation
(b) Valuation of inventories
(c) Treatment of goodwill
(d) Valuation of fixed assets
(e) Treatment of contingent liabilities etc.

* Selection of Accounting Policies

The primary consideration in the selection of accounting policies by an enterprise is that the financial statements prepared and presented on the basis of such accounting policies should represent a true and fair view of the state of affairs of the enterprise as at the balance sheet date and of the profit or loss for the period ended on that date.

For this purpose, the major considerations governing the selection and application of accounting policies are :

(a) Prudence :

In view of the uncertainty attached to future events, profits are not anticipated but recognised only when realised though not necessarily in cash. Provision is made for all known liabilities and losses even though the amount cannot be determined with certaintyand represents only a best estimate in the light of available information.

(b) Substance over Form :

The accounting treatment and presentation in financial statements of transactions and events should be governed by their substance and not merely by the legal form.

(c) Materiality :

Financial statements should disclose all "material" items, i.e. items the knowledge of which might influence the decisions of the user of the financial statements.

* Change in Accounting Policy

A change in accounting policies should be made only if :

(a) the adoption of a different accounting policy is required by statute or for compliance with an accounting standard, or

(b) it is considered that the change would result in a more appropriate presentation of the financial statements of the enterprise.

Any change in an accounting policy which has a material effect should be disclosed. The amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. If a change is made in the accounting policies which has no material effect on the financial statements for the current period but which is reasonably expected to have a material effect in later periods, the fact of such change should be appropriately disclosed in the period in which the change is adopted.

^ **ACCOUNTING AS A MEASUREMENT DISCIPLINE – VALUATION PRINCIPLES**

ACCOUNTING ESTIMATES

* **Meaning of Measurement**

Measurement is vital aspect of accounting. Primarily transactions and events are measured in terms of money.

The three elements of measurement are :

(1) Identification of objects and events to be measured;

(2) Selection of standard or scale to be used;

(3) Evaluation of dimension of measurement standard or scale.

Objects or Events to be measured

Accounting as the process of identifying, measuring and communicating economic information to permit informed judgements and decisions by the users of the information. So accounting essentially includes measurement of 'information'.

Decision makers need past, present and future information. For external users, generally the past information is communicated. There is no uniform set of events and transactions in accounting which are required for decision making.

The past and present objects and events can be measured with some degree of accuracy but future events and objects are only predicted, not measured. Prediction is an essential part of accounting information. Decision makers have to take decisions about the unseen future for which they need suitable information.

Standard or Scale of Measurement

In accounting, money is the scale of measurement (money measurement concept), although now-a- days quantitative information is also communicated along with monetary information. It takes the shape of currency ruling in a country. For example, in India the scale of measurement is Rupee, in the U.K. Pound-Sterling (£), in the United States Dollar ($) and so on. Also there is no constant exchange relationship among the currencies.

Dimension of Measurement Scale

An ideal measurement scale should be stable over time.

Money as a scale of measurement is not stable. There occurs continuous change in the input output prices. The same quantity of money may not have the ability to buy same quantity of identical goods at different dates. Thus information of one year measured in money terms may not be comparable with that of another year.

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* Valuation Principles

There are four generally accepted measurement bases or valuation principles.

These are:

(i) Historical Cost;

(ii) Current Cost;

(iii) Realizable Value;

(iv) Present Value.

(i) Historical Cost

It means acquisition price. According to this base -

(a) Assets are recorded at an amount of cash or cash equivalent paid at the time of acquisition.

(b) Liabilities are recorded at the amount of proceeds received in exchange for the obligation.

In some circumstances a liability is recorded at the amount of cash or cash equivalent expected to be paid to satisfy it in the normal course of business.

Companies usually apply historical cost method in case of long-term assets like machinery, furniture, licenses etc.

(ii) Current Cost

(a) Assets are carried out at the amount of cash or cash equivalent that would have to be paid if the same or an equivalent asset was acquired currently.

(b) Liabilities are carried at the undiscounted amount of cash or cash equivalents that would be required to settle the obligation currently.

(iii) Realizable Value

(a) Assets are carried at the amount of cash or cash equivalents that could currently be obtained by selling the assets in an orderly disposal.

Haphazard disposal may yield something less.

(b) Liabilities are carried at their settlement values; i.e. the undiscounted amount of cash or cash equivalents expressed to be paid to satisfy the liabilities in the normal course of business.

(iv) Present Value

(a) An asset is carried at the present discounted value of the future net cash inflows that the item is expected to generate in the normal course of business.

(b) Liabilities are carried at the present discounted value of future net cash outflows that are expected to be required to settle the liabilities in the normal course of business.

The concept of Present Value is common in case of accounting for investments and loans.

* **Accounting Estimates**

There are certain items, which have not occurred therefore cannot be measured using valuation principles still they are necessary to record in the books of account, for eg. doubtful debts. For such items, we need some value. In such a situation, reasonable estimates based on the existing situation and past experiences are made.

The measurement of certain assets and liabilities is based on estimates of uncertain future events. As a result of the uncertainties inherent in business activities, many financial statement items cannot be measured with precision but can only be estimated. Therefore, the management makes various estimates and assumptions of assets, liabilities, incomes and expenses as on the date of preparation of financial statements. Such estimates are made in connection with the computation of depreciation, amortisation and impairment losses as well as, accruals, provisions and employee benefit obligations. Also estimates may be required in determining the bad debts, useful life and residual value of an item of plant and machinery and obsolescence. The process of estimation involves judgements based on the inventory latest information available.

An estimate may require revision if changes occur regarding circumstances on which the estimate was based, or as a result of new information, more experience or subsequent developments. Change in accounting estimate means difference arises between certain parameters estimated earlier and re-estimated during the current period or actual result achieved during the current period.

^ **ACCOUNTING STANDARDS**

Introduction

To ensure transparency, consistency, comparability, adequacy and reliability of financial reporting, it is essential to standardize the accounting principles and policies. Accounting Standards (ASs) provide framework and standard accounting policies for treatment of transactions and events so that the financial statements of different enterprises become comparable.

Accounting standards are written policy documents issued by the expert accounting body (ICAI) or by the government or other regulatory body covering the aspects of recognition, measurement, presentation and disclosure of accounting transactions and events in the financial statements. The accounting standards deal with the issues of -

(i) recognition of events and transactions in the financial statements;

(ii) measurement of these transactions and events;

(iii) presentation of these transactions and events in the financial statements in a manner that is meaningful and understandable to the reader; and

(iv) the disclosure requirements which should be there to enable the public at large and the stakeholders and the potential investors in particular, to get an insight into what these financial statements are trying to reflect and thereby facilitating them to take prudent and informed business decisions.

* **Objectives of Accounting Standards**

(i) eliminate the non-comparability of financial statements and thereby improving the reliability of financial statements; and

(ii) provide a set of standard accounting policies, valuation norms and disclosure requirements.

* **Benefits and Limitations of Accounting Standards**

By setting the accounting standards, the accountant has following benefits:

(i) Standards reduce to a reasonable extent or eliminate altogether confusing variations in the accounting treatments used to prepare financial statements.

(ii) There are certain areas where important information are not statutorily required to be disclosed. Standards may call for disclosure beyond that required by law.

(iii) The application of accounting standards would, to a limited extent, facilitate comparison of financial statements of companies situated in different parts of the world and also of different companies situated in the same country. However, it should be noted in this respect that differences in the institutions, traditions and legal systems from one country to another give rise to differences in accounting standards adopted in different countries.

However, there are some limitations of accounting standards:

(i) Difficulties in making choice between different treatments : Alternative solutions to certain accounting problems may each have arguments to recommend them. Therefore, the choice between different alternative accounting treatments may become difficult.

(ii) Restricted scope : Accounting standards cannot override the statute. The standards are required to be framed within the ambit of prevailing statutes.

* **List of Accounting Standards in India**

The 'Accounting Standards' issued by the Accounting Standards Board establish standards which have to be complied by the business entities so that the financial statements are prepared in accordance with generally accepted accounting principles. Following is the list of applicable Accounting Standards:

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* Following is the list of applicable Accounting Standards:

List of Accounting Standards

Sr. No.	Number of the Accounting Standard (AS)	Title of the Accounting Standard
1	AS 1	Disclosure of Accounting Policies
2	AS 2 (Revised)	Valuation of Inventories
3	AS 3 (Revised)	Cash Flow Statements
4	AS 4 (Revised)	Contingencies and Events Occurring after the Balance Sheet Date
5	AS 5 (Revised)	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
6	AS 7 (Revised)	Accounting for Construction Contracts
7	AS 9	Revenue Recognition
8	AS 10	Property, Plant and Equipment
9	AS 11 (Revised)	The Effects of Changes in Foreign Exchange Rates
10	AS 12	Accounting for Government Grants
11	AS 13	Accounting for Investments
12	AS 14	Accounting for Amalgamations
13	AS 15 (Revised)	Employee Benefits
14	AS 16	Borrowing Costs
15	AS 17	Segment Reporting
16	AS 18	Related Party Disclosures
17	AS 19	Leases
18	AS 20	Earnings Per Share
19	AS 21	Consolidated Financial Statements
20	AS 22	Accounting for Taxes on Income
21	AS 23	Accounting for Investments in Associates in Consolidated Financial Statements
22	AS 24	Discontinuing Operations
23	AS 25	Interim Financial Reporting
24	AS 26	Intangible Assets
25	AS 27	Financial Reporting of Interests in Joint Ventures
26	AS 28	Impairment of Assets
27	AS 29	Provisions, Contingent Liabilities & Contingent Assets

Note: The list of accounting standards given above **does not form** part of syllabus. It has been given here for the knowledge only.

^	**Try Yourself : Objectives**
*	**State whether the following statements are True or False with reasons**
1	There is no difference between book keeping and accounting, both are same.
2	Management Accounting covers the preparation and interpretation of financial statements and communication to the users of accounts.
3	Financial accounting is concerned with internal reporting to the managers of a business unit.
4	Customers of business should not be considered as users of accounts prepared by business. They are not interested to know performance of the business.
5	Summarising is the basic function of accounting. All business transactions of a financial characters evidenced by some documents such as sales bill, pass book, salary slip etc. are recorded in the books of account.
6	Balance sheet shows the position of the business on the day of its preparation and not on the future date.
7	Objectives of book-keeping are complete recording of transactions & ascertainment of financial effect on the business.
8	Accounting can be viewed as an information system which has its input processing methods and output.
9	The financial statements are not prepared on the assumption that an enterprise is a going concern and will continue its operation for the foreseeable future.
10	The concept helps in keeping business affairs free from the influence of the personal affairs of the owner is known as the matching concept.
11	Entity concept means that the enterprise is liable to the owner for capital investment made by the owner.
12	Accrual means recognition as money is received or paid and not of revenue and costs as they are earned or incurred.
13	The Conservatism Concept states that no change should be counted unless it has materialized.
14	The concept of consistency implies non-flexibility as not to allow the introduction of improved method of accounting.
15	The materiality depends only upon the amount of the item and not upon the size of the business, nature and level of information, level of the person making the decision etc.
16	Accrual basis of accounting is the method of recording transactions by which revenues and costs and assets and liabilities are reflected in the accounts in the period in which actual receipts or actual payments are made.
17	Accrual concept implies accounting on cash basis.
18	The provision for discount on creditors is often not provided in keeping with the principle of conservatism.

19	As per concept of conservatism the accountant should provide for all possible losses but should not anticipate income.
20	The nature of business is not an important criteria in separating an expenditure between capital and revenue.
21	Expenditure incurred for major repair of the asset so as to increase its productive capacity is revenue in nature.
22	Amount spent as lawyer's fee to defend a suit claiming that the firm's factory site belonged to the plaintiff's land is Capital Expenditure.
23	Amount spent for replacement of worn-out part of machine is Capital Expenditure.
24	Legal fees to acquire property is Capital Expenditure.
25	Amount spent for the construction of temporary huts, which were necessary for construction of the cinema house and were demolished when the cinema house was ready, is Capital Expenditure.
26	Amount paid to Management Company for consultancy to reduce the working expenses is capital expenditure if the reduced working expenses will generate long term benefits to the entity.
27	M/s Raj Yog & Co. runs a cafe. They renovated some of the old cabins. Because of this renovation some space was made free and number of cabins was increased from 25 to 28. The total expenditure incurred was ₹ 50,000 and was treated as a revenue expenditure.
28	A contingent liability need not be disclosed in the financial statements.
29	A Provision fails to meet the recognition criteria.
30	A claim that an enterprise is pursuing through legal process, where the outcome is uncertain, is a contingent liability.
31	When it is probable that the firm will need to pay off the obligation, this gives rise to contingent liability.
32	Present financial obligation of an enterprise, which arises from past event is termed as contingent liability.
33	There is a single list of accounting policies, which are applicable to all enterprises in all circumstances.
34	Selection of accounting policy doesn't impact financial performance and financial position of the business
35	A change in accounting policies should be made as and when business like to show result as per their choice.
36	Choosing FIFO or weighted average method for inventory valuation is selection of accounting policy.
37	Selection of an inappropriate accounting policy decision will overstate the performance and financial position of a business entity every time.

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38	There are four generally accepted measurement bases.
	(i) Historical Cost;
	(ii) Current Cost;
	(iii) Realizable Value;
	(iv) Future Value.
39	Historical Cost means price paid at time acquisition.
40	As per future value, assets are carried at the amount of cash or cash equivalents that could currently be obtained by selling the assets in an orderly disposal.
41	At Present Value, liabilities are carried at the value of future net cash outflows that are expected to be required to settle the liabilities in the normal course of business.
42	ABC purchased a machinery amounting ₹ 10,00,000 on 1st April, 2001. On 31st March, 2022, similar machinery could be purchased for ₹ 20,00,000. Historical cost of machine is ₹ 20,00,000.
43	ABC purchased a machinery amounting ₹ 10,00,000 on 1st April, 2001. On 31st March, 2022, similar machinery could be purchased for ₹ 20,00,000. Current cost of machine is ₹ 20,00,000.
44	Change in accounting estimate has to be given retrospective effect.
45	A concern proposes to discontinue its business from December 2020 and decides to dispose off all its plants within a period of 3 months. The Balance Sheet as on 31st December, 2020 should continue to indicate the plants at its historical costs as the assets will be disposed off after the Balance Sheet date.
46	Accounting standards are written policy documents issued by the expert accounting body or by the government or other regulatory body covering the aspects of recognition, measurement, presentation and disclosure of accounting transactions and events in the financial statements.
47	Accounting standards can override the statute.
48	Difficulties in making choice between different treatments is one of the benefits of accounting standards.
49	Requirements for additional disclosures is limitation of accounting standards.
50	ASB stands for Accounting standardisation benchmarking.
51	There are no limitation to accounting standards.
52	Accounting Standards for non-corporate entities in India are issued by the Central Government.
	Answers:
1	**False**
	Book-keeping and accounting are different from each other. Accounting is a broad subject. It calls for a greater understanding of records obtained from book-keeping and anability to analyse and interpret the information provided by book-keeping records.

	Book-keeping is the recording phase while accounting is concerned with the summarizing phase of an accounting system.
2	**False**
	Financial accounting covers the preparation and interpretation of financial statements and communication to the users of accounts.
3	**False**
	Management accounting is concerned with internal reporting to the managers of a business unit.
4	**False**
	Customers are also concerned with the stability and profitability of the enterprise because their functioning is more or less dependent on the supply of goods.
5	**False**
	Recording is the basic function of accounting. Summarising is concerned with the preparation and presentation of the classified data in a manner useful to the internal as well as the external users of financial statements.
6	**True**
	Balance Sheet is a statement of the financial position of an enterprise at a given date.
7	**True**
	Book-keeping is concerned with complete recording and combined effect of transactions made during the accounting period.
8	**True**
	Accounting is a process of identifying, measuring and communicating information to permit informed judgement and decisions. It covers the preparation of financial statements and communication to the users of accounts.
9	**False**
	The financial statements are normally prepared on the assumption that an enterprise is a going concern and will continue in operation for the foreseeable future.
10	**False**
	Under matching concept all expenses matched with the revenue of that period should only be taken into consideration. In the financial statements of the organization if any

revenue is recognized then expenses related to earn that revenue should also be recognized.

11 **True**

Since the owner invested capital, he has claim on the profits of the enterprise.

12 **False**

Under accrual concept, the effects of transactions and other events are recognised on mercantile basis i.e., when they occur (and not as cash or a cash equivalent is received or paid) and they are recorded in the accounting records and reported in the financial statements of the periods to which they relate.

13 **False**

The Realisation Concept states that no change should be counted unless it has materialised.

14 **False**

The concept of consistency does not imply non-flexibility as not to allow the introduction of improved method of accounting.

15 **False**

As per materiality principle, all the items having significant economic effect on the business of the enterprise should be disclosed in the financial statements.

16 **False**

Cash Basis of Accounting is the method of recording transactions by which revenues and costs and assets and liabilities are reflected in the accounts in the period in which actual receipts or actual payments are made.

17 **False**

Accrual concept implies accounting on 'due' or 'accrual' basis. Accrual basis of accounting involves recognition of revenues and costs as and when they accrue irrespective of actual receipts or payments.

18 **True**

According to the principle of conservatism provision is maintained for the losses to be incurred in future. Discount on creditors is an income so provision in not maintained.

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19	**True**
	Conservatism states that the accountant should not anticipate any future income, however, they should provide for all possible losses.
20	**False**
	The nature of business is a very important criteria in separating an expenditure betweencapital and revenue. For example- For a trader dealing in furniture, purchase of furniture is revenue expenditure but for any other trade, the purchase of furniture should be treated as capital expenditure and shown in the balance sheet as asset. .
21	**False**
	Expenditure incurred for major repair of the asset so as to increase its productive capacity is capital in nature.
22	**False**
	Legal expenses incurred to defend a suit claiming that the firm's factory site belongs to the plaintiff is maintenance expenditure of the asset. By this expense, neither any endurable benefit can be obtained in future in addition to that what is presently available nor the capacity of the asset will be increased. Maintenance expenditure in relation to an asset is revenue expenditure.
23	**False**
	Amount spent for replacement of any worn out part of a machine is revenue expense since it is part of its maintenance cost.
24	**True**
	Legal fee paid to acquire any property is a part of cost of that property. It is incurred to possess the ownership right of the property and hence a capital expenditure.
25	**True**
	Since temporary huts were necessary for the construction, their cost should be added to the cost of the cinema hall and thus capitalised.
26	**True**
	Amount paid to management company for consultancy to reduce the working expenses is capital expenditure as this expenditure will generate long-term benefit to the entity.

27	**False**
	Renovation of cabins increased the number of cabins. This has an effect on the future revenue generating capability of the business. Thus, this renovation expense is capital expenditure in nature.
28	**False**
	A Contingent liability is required to be disclosed unless possibility of outflow of a resource embodying economic benefits is remote.
29	**False**
	A contingent liability fails to meet the recognition criteria.
30	**False**
	A claim that an enterprise is pursuing through legal process, where the outcome is uncertain, is a contingent asset.
31	**False**
	When it is probable that the firm will need to pay off the obligation, this gives rise to provision.
32	**False**
	Present Financial obligation of an enterprise, which arises from past events is termed as liability.
33	**False**
	There cannot be single list of accounting policies, which are applicable to all enterprises in all circumstances. There would always be different policies chosen by different industries under different circumstances.
34	**False**
	Accounting policy has big impact on value of items goes under financial statements, hence it impacts financial performance and financial position of the business.
35	**False**
	A change in accounting policies should be made in the following conditions: (a) It is required by some statute or for compliance with an Accounting Standard. (b) Change would result in more appropriate presentation of financial statement.

36	**True**
	An enterprise may adopt FIFO or weighted average method for inventory valuation and the method selected for valuation is called an accounting policy.
37	**False**
	It could understate/overstate the performance and financial position of a business entity.
38	**False**
	There are four generally accepted measurement bases . (i) Historical Cost; (ii) Current Cost; (iv) Realizable Value; (iv) Present Value
39	**True**
	Historical cost means the acquisition price.
40	**False**
	At Realisable value, assets are carried at the amount of cash or cash equivalents that could currently be obtained by selling the assets in an orderly disposal.
41	**False**
	Liabilities are carried at the present discounted value of future net cash outflows that are expected to be required to settle the liabilities in the normal course of business.
42	**False**
	Historical cost is ₹10,00,000.
43	**True**
	Since similar machine is purchased at ₹ 20,00,000, the current cost of machine is ₹ 20,00,000.
44	**False**
	Change in accounting estimate has not to be given retrospective effect.
45	**False**
	If the fundamental accounting assumption of going concern is not followed, then the assets and liabilities should be stated at realizable value not historical cost.

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46	**True**
	Accounting standards are documents covering recognition, measurement, presentation and disclosure of accounting transactions and events in the financial statements.
47	**False**
	Accounting standards can never override the statute. The standards are required to be framed within the ambit of prevailing statutes.
48	**False**
	Difficulties in making choice between different treatments is one of the limitation of accounting standard.
49	**False**
	Benefits of accounting standards are: • Standardisation of alternative accounting treatments • Comparability of financial statements • Requirements for additional disclosures.
50	**False**
	ASB stands for Accounting Standard Board.
51	**False**
	Limitations of accounting standards • Difficulties in making choice between different treatments • Restricted scope
52	**False**
	Accounting Standards for non-corporate entities in India are issued by the Institute of Chartered Accountants of India (ICAI).
*	**Multiple Choice Questions**
1	Which of the following is not a subfield of accounting? (a) Management accounting (b) Cost accounting (c) Book-keeping
2	Purposes of an accounting system include all the following except (a) Interpret and record the effects of business transaction. (b) Classify the effects of transactions to facilitate the preparation of reports. (c) Dictate the specific types of business enterprise transactions that the enterprises may engage in.

3	Book-keeping is mainly concerned with
	(a) Recording of financial data.
	(b) Designing the systems in recording, classifying and summarising the recorded data.
	(c) Interpreting the data for internal and external users.
4	All of the following are functions of Accounting except
	(a) Decision making. (b) Ledger posting. (c) Forecasting.
5	Financial statements are part of
	(a) Accounting. (b) Book-keeping. (c) Management Accounting.
6	Financial position of the business is ascertained on the basis of
	(a) Records prepared under book-keeping process.
	(b) Trial balance.
	(c) Balance Sheet.
7	Users of accounting information include
	(a) Creditors/Suppliers (b) Lenders / Customers (c) Both (a) and (b)
8	Financial statements do not consider
	(a) Assets expressed in monetary terms.
	(b) Liabilities expressed in monetary terms.
	(c) Assets and liabilities expressed in non-monetary terms
9	On January 1, Sohan paid rent of ₹ 5,000. This can be classified as
	(a) An event.
	(b) A transaction.
	(c) A transaction as well as an event.
10	On March 31, 2022 after sale of goods worth ₹ 2,000, he is left with the closing
	inventory of ₹ 10,000. This is
	(a) An event. (b) A transaction. (c) A transaction as well as an event.
11	Which of the following is not a business transaction?
	(a) Bought a machine of ₹ 10,000 for business
	(b) Paid towards salaries of employees ₹ 5,000
	(c) Paid son's fees from her personal bank account ₹ 8,000

12 Which qualitative characteristics of accounting information is reflected when accounting information is clearly presented?
(a) Understandability (b) Relevance (c) Comparability

13 All the following items are classified as fundamental accounting assumptions except
(a) Consistency. (b) Business entity. (c) Going concern.

14 Two primary qualitative characteristics of financial statements are
(a) Understandability and materiality.
(b) Relevance and reliability.
(c) Neutrality and understandability.

15 Kanika Enterprises follows the written down value method of depreciating machinery year after year due to
(a) Comparability. (b) Convenience. (c) Consistency.

16 A purchased a car for ₹ 5,00,000, making a down payment of ₹ 1,00,000 and signing a ₹ 4,00,000 bill payable due in 60 days. As a result of this transaction
(a) Total assets increased by ₹ 5,00,000.
(b) Total liabilities increased by ₹ 4,00,000.
(c) Total assets increased by ₹ 4,00,000 with corresponding increase in liabilities by ₹ 4,00,000.

17 Mohan purchased goods for ₹ 15,00,000 and sold 4/5th of the goods amounting ₹ 18,00,000 and met expenses amounting ₹ 2,50,000 during the year, 2022. He counted net profit as ₹ 3,50,000. Which of the accounting concept was followed by him?
(a) Entity (b) Periodicity. (c) Matching.

18 A businessman purchased goods for ₹ 25,00,000 and sold 80% of such goods during the accounting year ended 31st March, 2022. The market value of the remaining goods was ₹ 4,00,000. He valued the closing inventory at cost. He violated the concept of
(a) Money measurement. (b) Conservatism. (c) Cost.

19 Capital brought in by the proprietor is
(a) Increase in asset and increase in liability
(b) Increase in liability and decrease in asset
(c) Increase in asset and decrease in liability

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20	During the life-time of an entity, accounting provides financial statements in accordance with which basic accounting concept: (a) Conservatism (b) Matching (c) Accounting period
21	A concept that a business enterprise will not be liquidated in the near future is known as (a) Going concern (b) Economic entity (c) Monetary unit
22	Assets are held in the business for the (a) Resale. (b) Conversion into cash (c) Earning revenue.
23	Revenue from sale of products, is generally, realised in the period in which (a) Cash is collected. (b) Sale is made (c) Products are manufactured
24	The concept of conservatism when applied to the balance sheet results in (a) Understatement of assets. (b) Overstatement of assets. (c) Overstatement of capital.
25	Decrease in the amount of trade payables results in (a) Increase in cash. (b) Decrease in bank over draft account. (c) Decrease in assets.
26	The determination of expenses for an accounting period is based on the principle of (a) Objectivity. (b) Materiality. (c) Matching.
27	Economic life of an enterprise is split into the periodic interval to measure its performance is as per (a) Entity. (b) Matching. (c) Periodicity.
28	If an individual asset is increased, there will be a corresponding (a) Increase of another asset or increase of capital. (b) Decrease of another asset or increase of liability. (c) Decrease of specific liability or decrease of capital.
29	Purchase of machinery for cash (a) Decreases total assets. (b) Increases total assets. (c) Retains total assets unchanged.

30 Consider the following data pertaining to Alpha Ltd.:

Particulars	₹
Cost of machinery purchased on 1st April, 2021	10,00,000
Installation charges	1,00,000
Market value as on 31st March, 2022	12,00,000

While finalizing the annual accounts, if the company values the machinery at ₹ 12,00,000. Which of the following concepts is violated by the Alpha Ltd.?

(a) Cost. (b) Matching. (c) Accrual.

31 Money spent ₹ 10,000 as traveling expenses of the directors on trips abroad for purchase of capital assets is

(a) Capital expenditures

(b) Revenue expenditures

(c) Prepaid revenue expenditures

32 Amount of ₹ 5,000 spent as lawyers' fee to defend a suit claiming that the firm's factory site belonged to the plaintiff's land is

(a) Capital expenditures

(b) Revenue expenditures

(c) Prepaid revenue expenditures

33 Entrance fee of ₹ 2,000 received by Ram and Shyam Social Club is

(a) Capital receipt (b) Revenue receipt (c) Capital expenditures

34 4. Subsidy of ₹ 40,000 received from the government for working capital by a manufacturing concern is

(a) Capital receipt (b) Revenue receipt (c) Capital expenditures

35 Insurance claim received on account of

(a) Capital receipt (b) Revenue receipt (c) Capital expenditures

36 Interest on investments received from

(a) Capital receipt (b) Revenue receipt (c) Capital expenditures

37 Amount received from IDBI as a medium term loan for augmenting working capital is

(a) Capital expenditures (b) Revenue expenditures (c) Capital receipt

38 Revenue from sale of products, ordinarily, is reported as part of the earning in the period in which
(a) The sale is made.
(b) The cash is collected.
(c) The products are manufactured.

39 If repair cost is ₹ 25,000, whitewash expenses are ₹ 5,000, (both these expenses relate to presently used building) cost of extension of building is ₹ 2,50,000 and cost of improvement in electrical wiring system is ₹19,000; the amount to be expensed is
(a) ₹ 2,99,000. (b) ₹ 44,000. (c) ₹ 30,000.

40 Contingent asset usually arises from unplanned or unexpected events that give rise to
(a) The possibility of an inflow of economic benefits to the business entity.
(b) The possibility of an outflow of economic benefits to the business entity.
(c) Either (a) or (b).

41 If an inflow of economic benefits is probable then a contingent asset is disclosed
(a) In the financial statements.
(b) In the report of the approving authority (Board of Directors in the case of a company, and the corresponding approving authority in the case of any other enterprise).
(c) In the cash flow statement.

42 In the case of , either outflow of resources to settle the obligation is not probable or the amount expected to be paid to settle the liability cannot be measured with sufficient reliability.
(a) Liability (b) Provision (c) Contingent liabilities

43 Present liability of uncertain amount, which can be measured reliably by using a substantial degree of estimation is termed as .
(a) Provision. (b) Liability. (c) Contingent liability.

44 In the financial statements, contingent liability is
(a) Recognised. (b) Not recognised. (c) Adjusted

45 A change in accounting policy is justified
(a) To comply with accounting standard and law.
(b) To ensure more appropriate presentation of the financial statement of the enterprise.
(c) Both (a) and (b).

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46 Accounting policy for inventories of Xeta Enterprises states that inventories are valued at the lower of cost determined on weighted average basis or net realizable value. Which accounting principle is followed in adopting the above policy?
(a) Materiality. (b) Prudence. (c) Substance over form.

47 The areas wherein different accounting policies can be adopted are
(a) Providing depreciation. (b) Valuation of inventories. (c) Both the option.

48 Selection of an inappropriate accounting policy decision may
(a) Overstate the performance and financial position of a business entity.
(b) Understate/overstate the performance and financial position of a business entity.
(c) Overstate the performance of a business entity.

49 Accounting policies refer to specific accounting
(a) Principles.
(b) Methods of applying those principles.
(c) Both (a) and (b).

50 Measurement discipline deals with
(a) Identification of objects and events.
(b) Selection of scale.
(c) Both (a) and (b)

51 All of the following are valuation principles except
(a) Historical cost. (b) Present value. (c) Future value

52 Book value of machinery on 31st March, 2022 ₹ 10,00,000
Market value as on 31st March, 2022 if sold ₹ 11,00,000
As on 31st March, 2022, if the company values the machinery at ₹ 11,00,000, which of the following valuation principle is being followed?
(a) Historical Cost. (b) Present Value. (c) Realisable Value.

53 Mohan purchased a machinery amounting ₹ 10,00,000 on 1st April, 2001. On 31st March, 2022, similar machinery could be purchased for ₹ 20,00,000 but the realizable value of the machinery (purchased on 1.4.2001) was estimated at ₹ 15,00,000. The present discounted value of the future net cash inflows that the machinery was expected to generate in the normal course of business, was calculated as ₹ 12,00,000.

(i) The current cost of the machinery is

(a) ₹ 10,00,000. (b) ₹ 20,00,000. (c) ₹ 15,00,000.

(ii) The present value of machinery is

(a) ₹ 10,00,000. (b) ₹ 20,00,000. (c) ₹ 12,00,000.

(iii) The historical cost of machinery is

(a) ₹ 10,00,000. (b) ₹ 20,00,000. (c) ₹ 15,00,000.

(iv) The realizable value of machinery is

(a) ₹ 10,00,000. (b) ₹ 20,00,000. (c) ₹ 15,00,000.

54 Accounting Standards for Non-Corporate entities in India are issued by

(a) Central Govt.

(b) State Govt.

(c) Institute of Chartered Accountants of India.

55 Accounting Standards

(a) Harmonise accounting policies.

(b) Eliminate the non-comparability of financial statements.

(c) Both the above.

56 It is essential to standardize the accounting principles and policies in order to ensure

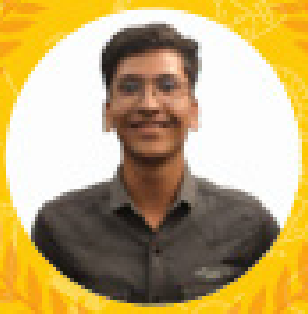
(a) Transparency. (b) Consistency. (c) Both the above.

Answers:

1	(c)		**13**	(b)		**25**	(c)		**37**	(c)		**49**	(c)
2	(c)		**14**	(b)		**26**	(c)		**38**	(a)		**50**	(c)
3	(a)		**15**	(c)		**27**	(c)		**39**	(c)		**51**	(c)
4	(b)		**16**	(c)		**28**	(b)		**40**	(a)		**52**	(c)
5	(a)		**17**	(c)		**29**	(c)		**41**	(b)		**53**	
6	(c)		**18**	(b)		**30**	(a)		**42**	(c)		**i.**	(b)
7	(c)		**19**	(a)		**31**	(a)		**43**	(a)		**ii.**	(c)
8	(c)		**20**	(c)		**32**	(b)		**44**	(b)		**iii.**	(a)
9	(b)		**21**	(a)		**33**	(a)		**45**	(c)		**iv.**	(c)
10	(a)		**22**	(c)		**34**	(b)		**46**	(b)		**54**	(c)
11	(c)		**23**	(b)		**35**	(a)		**47**	(b)		**55**	(c)
12	(a)		**24**	(a)		**36**	(b)		**48**	(b)		**56**	(c)

Toppers CA Foundation

Dec'23



357/400

BHAVIK DOSHI



TARA MANGWANI
347



RIVA SINGH
346



AMRUTANSHU
344



MANYA JAIN
338



SWAPNIL GUPTA
329



CHHAVI KHANDELWAL
326



HETA SAVALIYA
324



VANSHITA CHATURVEDI
323



YASH PRABHU
321



SHORIYAN TRIVEDI
319



KASAK JAIN
319



RAVI RAO
313



PRISHITA SETHI
310



LOKESH PAWAR
308



SOHAM SHAH
307



GAURANG SHAH
307



HEMIL SATUNDA
304



ESAKKIMUTHU DAS
304



SHASHI PALOD
304



ALVITA KHAN
302



SORABH MOHATA
301



SANA DESHPANDE
300



MEETALI MAHESHWARI
300

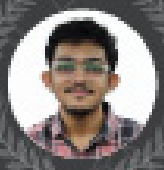
Toppers CA Foundation

June 22 & June 23



340/400

HARSH GULWANI
CA Foundation June'22



MEET SHAH
CA Foundation June'23
331



NISHIT KAPUR
CA Foundation June'23
328



PALAK JAJODIA
CA Foundation June'23
325



SWASTIKA SINGH
CA Foundation June'22
323



SUKUNJ GUPTA
CA Foundation June'22
323



DURGASHRI VS
CA Foundation June'22
319



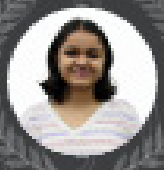
VARUN ADWANI
CA Foundation June'22
319



KARTIK LADHANI
CA Foundation June'22
316



RIDHI PAREKH
CA Foundation Dec'22
314



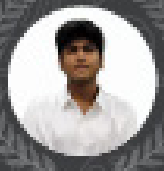
SMEET LADHANI
CA Foundation June'23
313



TANMAY AGARWAL
CA Foundation June'23
311



GARV KHANDELWAL
CA Foundation June'22
308



DAKSH JAIN
CA Foundation June'23
308



DEEPAK GURNANI
CA Foundation June'22
305



PARIDHI JHAWAR
CA Foundation June'22
304



SATYA BHANUSHALI
CA Foundation June'23
304

and many more...

ALL INDIA RANKERS CA INTER | MAY'22 & MAY'23 NOV'23



AIR 13

JUHI KAJARIA
CA INTER MAY'22



MANAN SHAH
CA INTER MAY'22
AIR 14



PRACHI NANDU
CA INTER MAY'23
AIR 24



VATSAL MEHTA
CA INTER MAY'23
AIR 33



PIYUSH KOTHARI
CA INTER MAY'23
AIR 34



HIMANSHI CHHAJED
CA INTER MAY'23
AIR 39



YUKTA SATPALKAR
CA INTER MAY'22
AIR 40



MARVI LODHA
CA INTER MAY'23
AIR 40



ARMAN HOSANGADY
CA INTER MAY'22
AIR 41



VANSHIKA LOHANA
CA INTER MAY'22
AIR 46



PRANJAL MUNDRA
CA INTER MAY'23
AIR 46



SANJEEV JAIN
CA INTER MAY'22
AIR 47



RISHABH JAIN
CA INTER MAY'23
AIR 47



SHREYA SHIVARAM
CA INTER NOV'23
AIR 47

ALL INDIA RANKERS CA FINAL | MAY'22 & NOV'23



AIR 2

SANKRUTI PAROLIA
CA FINAL NOV'23



MAHESH TAPADIYA
CA FINAL MAY'22
AIR 6



SHRUTI PAROLIA
CA FINAL NOV'23
AIR 8



MAYANK HOLANI
CA FINAL NOV'23
AIR 17



KUSHAGRA AGARWAL
CA FINAL MAY'22
AIR 20



RITIK SANGHAVI
CA FINAL MAY'22
AIR 22



PARTHIV CHABRIA
CA FINAL NOV'23
AIR 32



PINAL KHETAN
CA FINAL NOV'23
AIR 35



SHOURYA TIBREWALA
CA FINAL MAY'22
AIR 39



DEEPAK LADHA
CA FINAL NOV'23
AIR 40



HIMANSHU KHATRI
CA FINAL MAY'22
AIR 41



SHRAVAN MUNDRA
CA FINAL NOV'23
AIR 45



DEEPTHI PACHIPULUSU
CA FINAL MAY'22
AIR 46



SHREY AGARWAL
CA FINAL MAY'22
AIR 48

MUMBAI'S NO 1 COMMERCE COACHING

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OUR PRESENCE

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KANDIVALI (W)
9/82, Mahavir Nagar, Pragati CHS LTD, Kandivali (West), Mumbai :- 400 067
Ph. : 7784 873 873

GOREGAON (W)
202, 2nd floor, Azmi, 2nd floor, Opposite Ratna, Goregaon, Mumbai - 400104
Ph. : 9819 470 740

ANDHERI (E)
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Ph. : 7273 895 895

VILE PARLE (W)
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Ph. : 7273 895 895

DADAR (W)
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MIRA ROAD (E)
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VIRAR (W)
108,109 1st floor, Viva Mall, Puroshotam Parekh (PP) Market, Near Bus Depot, Opp. Anita Gas Agency, Virar Station (West)
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Ph. : 7273 947 947

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101,Shivdarshan Apts, Near Kalyan Janta Sahakari Bank, Durga Mata Mandir Road,Kolsewadi, Kalyan (East)
Ph. : 859 111 5864

KALYAN (W)
212, Shreeji Solitaire, Khadakpada Circle, Above Bikaner, Kalyan (W)
Ph. : 70390 633 33

DOMBIVALI (W)
001, Vitthal Krupa Bldg, Shubhash Rd, Petrol Pump, Near Bhagshala Ground, Kagade Chowk, Dombivali (W).
Ph. : 9530 531 080

BHIWANDI
Shop No. 27, Prithvi Residency, Near Oswal School, Anjurphata.
Ph. : 7020 902 068

CHEMBUR (E)
19, Sunil Sadan, 3rd Floor, Central Avenue Road, Opp.of Grand Central Hotel, Above Monginis OR Yewle Tea, Chembur(E) - 400071
Ph. : 9870 780 524

AJMER
1, Parashnath Colony, Vaishali Nagar, Ajmer - 305001
Ph.: 8890 774 877

CHENNAI
S6, New No. 16, Old no 42, Govindan Road, West Mambalam, Chennai - 33
Ph.: 044 4860 3232

MATHURA
Near Masani Petrol Pump, Opp Kiran Palace, Agrsen Chowk, Mathura, U.P.- 281001
Ph. : 8439 344 979

BHILWARA
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Ph. : 9001 390 017

7273 967 967

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