FINANCIAL ACCOUNTING

Study Material Prepared By

INSTITUTE OF COST AND WORKS ACCOUNTANTS OF INDIA

for

Junior Accounts Officer(Civil) Examination

Conducted By

CONTROLLER GENERAL OF ACCOUNTS
1.0 INTRODUCTION TO FINANCIAL ACCOUNTING

Accounting is a social science. The nature of accounting information has been dictated from time immemorial by the needs of the users of the day. The history of accounting reflects the pattern of social developments and the forces which necessitate the changes in accounting system from time to time.

Over the years accountancy has made tremendous progress in the field of commerce and industry. Accounting can be described as being concerned with measurement and management. Measurement of recording transactions and management with the use of data for making decisions are the two fundamental aspects.
Financial Accounting Fundamentals

Accounting function is vital for every entity of the society whether individuals, housewives, business entity, nonprofit making organisations like municipalities, panchyats, clubs, etc. All are required to maintain accounts.

Accounting is commonly referred to as the “language of the business” as it is effectively employed to communicate the financial performance of business to various interested parties or stakeholders. It is concerned with the measurement and communicating financial data.

Financial Accounting is based on double entry system of accounting which comprises of

(i) recording of business transactions in the books of prime entry,
(ii) posting into respective ledger accounts,
(iii) striking balance, and
(iv) preparing the performance statement (profit and loss statement) and position statement (balance sheet).

Financial Accounting is concerned with the collection, recording, classification and presentation of financial data to serve the purposes of the management, shareholders and stakeholders, such as, creditors, bankers, Government, etc.

The nature and purpose of accounting

The basic aim of accounting in a business entity is to provide financial information for making decisions on its activities. Managers of an economic entity at various levels require analysed financial information for planning and programming, for controlling expenditure, for ascertaining the extent of profitability or otherwise of a department – even of each production item for undertaking new jobs, etc.

Financial information in tabular forms and with graphs and charts are also required by the outsiders, namely, bankers, financial institutions, creditors, investors, government agencies and even by the labour unions and the general public who have some interest in the particular business concern.

Definition of Accounting

A widely accepted definition of accounting has been provided by the American Accounting Association. According to this definition accounting is the process of identifying, measuring and communicating information to permit judgement and decisions by the users of accounts. This definition implies that –

(1) there should be users of accounts who need relevant information,
(2) the information should enable the users to make judgement and decisions, and
(3) transactions and events are measured and the data are processed and then communicated to the users through accounting.
Basics of Financial Accounting

Objectives of Accounting

The basic objectives of accounting are to provide financial information to the managers, owners and the stakeholders i.e. the parties who are interested in an organisation. To attain such objectives various financial statements are prepared.

The users of financial statements may be broadly classified in the following groups –

(a) *The investor* – This group includes both existing and potential owners of shares in companies. They are broadly interested in the performance of the entity and the dividend declared by such entity. They also measure the social and economic policies of the company to decide whether they will remain associated with such entity.

(b) *The lender* – This group includes both secured and unsecured lenders. Such creditors may be financing long term or short term loans. The financial statements are analysed to determine an organisation’s ability as to

(i) pay the interest on due date,
(ii) the growth and stability of the organisation,
(iii) capability of repaying the loan as agreed upon, and.
(iv) the book value of assets offered as security by the organisation.

(c) *The customers and suppliers* – While customers are interested in the ability of the organisation to provide goods/services, the suppliers are interested in the capability of the organisation to pay their dues as and when due.

(d) *The government* – This group includes various taxation authorities viz. Income tax, Excise department, Sales tax department etc. and also various other government authorities for statistical purposes and for framing various economic and planning policies.

(e) *The employee group* – The employees are concerned with the capability of an organisation to pay their present emoluments and future retirement benefits. Moreover, financial statements help them to asses job security.

(f) *The analyst* – Advisors to the management, investors, employees or public at large collect various data from financial statements to advise their clients.

(g) *The Management* – Financial statements provide required information to different levels of management to assist them in making decisions at each appropriate level.
1.1 SUBDIVISION OF ACCOUNTING

Generally, accounting is subdivided as follows:

a) Book-keeping
b) Measuring working results and capital of the economic entity and reporting.

(a) Book-keeping: Book-keeping is the art and science of recording transactions of a business enterprise or an organisation carrying out non-business activities in a systematic and appropriate manner to measure the working results and capital at periodical interval depending upon needs of an entity.

(b) Measuring working results and capital of the economic entity and reporting: The most important aspect of accounting records is to measure the working results and the capital of the economic entity and interpreting and reporting of results.

1.2 CONCEPTS AND CONVENTIONS IN ACCOUNTING

Basic concepts:

Accounting principles are built on a foundation of a few basic concepts. These concepts are so basic that most accountants do not consciously think of them; they are regarded as being self-evident. Non-accountants will not find these concepts to be self-evident. Some accounting theorists argue that certain of the present concepts are wrong and should be changed. But in order to understand accounting, as it now exists, one must understand what the underlying concepts currently are. The different aspects are:—

1. Business Entity Concept
2. Money Measurement Concept
3. Cost Concept
4. Going Concern Concept
5. Dual-aspect Concept
6. Realisation Concept
7. Accrual Concept
8. Accounting Period Concept

1. Business Entity Concept:

The business is treated as a distinct (and separate) entity from the individuals who own it and accordingly accountants record transactions. For example, if the owner of a shop withdraws Rs. 10,000 for personal use, from the business entity point of view, the entity has less cash though it belongs to the owners. Therefore, this amount is shown as a reduction in owner’s capital, which in view of business entity concept appears as a liability in the balance sheet of the business. Without such a distinction the affairs of the shop will be
Basics of Financial Accounting

mixed with the personal affairs of the owner. For a company the distinction is easier as legally the company is a distinct entity from the persons who own it. Therefore, an entity is a business organisation or activity in relation to which accounting reports are compiled. It may include universities, voluntary organisations, government and non-business units. What we have stated above is just a superficial discussion of the concept, though the central point has been brought out clearly. But we have to go at least a little deeper because out of this basic concept, a large number of very important sub-concepts emerge, dealing with ownership equities, without which we cannot understand properly many of the modern accounting practices.

Pure Accounting Viewpoint: We will start from the fundamental accounting equation, that is:

Debit = Credit (i)
And, Assets = Liabilities (ii)
And, Assets = Internal Liabilities + External Liabilities (iii)
And finally, Assets = Capital + Liabilities; or A = C + L (iv)

2. Money Measurement Concept:

A record is made only of the information that can be expressed in monetary terms for accounting purposes. The advantage of doing this is that money provides common denominators by means of which variety of facts can be expressed as numbers that can be added and subtracted. This enables addition and subtraction of varied items since money provides the common denominator. An event even though important like the loyalty of the workers will not be recorded unless it can be expressed in monetary terms. The changing price level also creates difficulties in the monetary value.

If we look at financial accounting purely from the point of view of Fundamental Accounting Equation:

Assets = Capital + Liabilities,

then it would be evident that it had virtually no option but to adopt monetary values of assets and liabilities and capital to apply the equation in day-to-day business affairs. This concept is basically concerned with the problem of measuring items of the accounting equation. Such items may be plant and machinery (assets), liability for loan taken – all these are object of some kind of the other. Other items represent events (transactions) such as expenses and income. Basically, double entry system is additive (say, when finding the aggregate of assets) or subtractive (say when total liabilities are deducted from total assets to find capital, or deducting expenses from income to estimate profit). But only the "like" can be added with the "like" and the "like" can be deducted from the "like", when the word "like" means that the items involved are expressed in the same unit. But in real-world affairs, physical assets may have to be expressed in several ways, like numbers of units, weight, volume, etc. Likewise wages may have to be expressed in man-hours or simply in hours. Apart from ensuring feasibility of making addition and subtraction, which is inherent in the accounting equation, the sign of equality (actually the sign of "identity") needs use of the
Financial Accounting Fundamentals

same units in describing such items. In accounting the description is finally expressed quantitatively in terms of money. In modern business it is essential link to accounting to a market system in an exchange economy a valuable source of quantitative data. Since goods and service are generally exchanged in terms of money, a monetary measurement of economics data can be assumed to be useful in decision-making, particularly for that decision relating to wealth and the production of goods and services.

3. Cost Concept:

The cost concept and the money measurement concept go hand in hand. Transactions are recorded in the books at the price paid that is the cost. This avoids an arbitrary value being placed on the asset and all subsequent accounting is in relation to the cost. Therefore, the recording of the assets is at cost figures and this may not reflect the current market value especially in the case of the older assets. The value of an asset in the accounting records does not remain at the original cost because it is diminished systematically by virtue of its use called expired cost and then shown at its depreciated value e.g. an asset of Rs. 1,00,000 is depreciated at 10%. Therefore, closing value will be Rs. 90,000 in the Balance Sheet. An expired cost is an expenditure of money, the economic value of which has been made use of during a particular year (or lost without accruing any benefit to the entity, like machinery destroyed by flood). Every cost has to be recovered from the market through sales, otherwise, the entity will suffer loss, that is, lose its capital. Depreciation, looked at from this viewpoint, is nothing but gradual recovery of cost incurred, that is, money paid at a time during a particular year for acquiring a fixed asset, during the subsequent years (during which the asset is assumed to remain serviceable) on some estimated basis, by treating the expired cost pertaining to a particular year, calculated on some approved and selected estimated basis, by including such expired cost, called an expense, in the cost of production of that particular accounting year. Linking annual depreciation with the expected service life of a fixed asset does not endow any scientific logic on any estimated basis of depreciation. In accounting, depreciation is nothing more and nothing less than a process of allocation of some specific costs (cost of acquiring fixed assets) on some generally accepted (may or may not be legally approved) estimated basis. An expired cost is not a money measure of the wear and tear obsolescence (passage of time) etc. of any fixed assets. It is just a reasonable basis for recovery of cost of fixed asset in a gradual manner. Money value of wear and tear would need engineering analysis, which is not the domain of financial accounting.

In essence, in a little more technical sense, cost represents the exchange price agreed upon by the buyer and the seller in a relatively free economy. Cost has been the most common valuation concept in the traditional accounting structure.

Therefore, cost is the exchange price of goods and services at the time they are acquired. So, cost is also the economic sacrifice expressed in monetary terms required to obtain a specific asset or a group of assets. Very often cost is not represented by a single exchange price, but it includes many sacrifices of economic resources necessary to obtain the asset in the form, location and time in which it can be useful to the operating activities of the firm.
4. **Going Concern Concept:**

Accounting assumes that the business will exist indefinitely into future and accordingly transactions are recorded. If however, there is evidence that the firm will be liquidated then market value of the assets and liabilities will be ascertained and necessary accounting considered. In other cases where the business is an on-going activity resale value of assets is irrelevant. The whole accounting is done based on this assumption.

The present concept as well as the earlier Business Entity concept belongs to the category of "Environmental Postulates of Accounting". It is important to know the precise meaning of this expression, for which purpose we have to know what an accounting postulate is and what is environmental in accounting. In order to avoid a lengthy discussion, we may summarise, by stating that postulates are basic assumption or fundamental propositions concerning the economic, political and sociological environment in which accounting must operate. Thus, it is clear that certain economic, political and sociological events do affect the thinking and actions of accountants and we must also clearly understand that every such event does not affect accounting concepts and practice. The basic criteria for any such postulates are:

1. They must be relevant to the development of accounting logic, that is, they must serve as a foundation for the logical derivation of further propositions; and
2. They must be accepted as valid by the participants in the discussion as either being true or providing a useful starting point as an assumption in the development of accounting logic.

5. **Dual Aspect Concept:**

The economic resources of an entity are assets and the acquisition of an asset must be on account of:

- (a) some other assets being sold; or
- (b) the creation of an obligation to pay; or
- (c) there has been a profit owed to proprietor; or
- (d) the owner has contributed.

On the other hand, an increase in liability is on account of an increase in asset or a loss. Therefore, at any time –

\[
\text{Assets} = \text{Liabilities} + \text{Capital} \\
\text{Capital} = \text{Assets} – \text{Liabilities}
\]
The owner’s share is what is left after paying outsiders. This is the accounting equation. Every transaction has dual impact and accounting systems record both the aspects and are called the double entry system. e.g. X starts a business with a capital of Rs.20,000. There are two aspects of the transaction. On the one hand the business has assets of Rs. 20,000 while on the other hand it has to pay the proprietor Rs. 20,000, therefore: –

\[
\text{Capital (Equities)} = \text{Assets (Cash)} \\
Rs. 20,000 = Rs. 20,000
\]

What has been stated above is an oversimplified version of the concept and its application, since this is the form of the concept with which we are familiar as beginners. But we have to go a little deeper in order to have a more meaningful understanding of the concept because it is the bedrock on which double entry book keeping has built its gigantic edifice and is still flourishing as a very important discipline all over the world. There must be something deeper than what has been stated above which caught the imagination of an Italian priest and mathematician and prompted him to codify if not invent the double-entry system in 1495 which explained logically and systematically what happens in the economic world, in terms of money when goods are manufactured and sold at the market place through financial transactions. This could be applied to sale of services equally logically, and systematically. In course of time it also exposed other related concepts, especially the first two concepts already discussed, namely the Business Entity concept and the Money Measurement concept.

6. Realisation Concept:

The realisation concept indicates the amount of revenue that should be considered from a given transaction. Realization refers to inflows of cash or claims to cash. It states that the amount recognized as revenue is the amount that is reasonably certain to be realised. Sometimes there is scope for difference of judgement as to how to ascertain "reasonably certain". A situation arises when a company makes a credit sale and expects that the customer will pay their bill. Experience shows that not all customers pay their bill. In measuring the revenue for a period, the amount of credit sales that will not be realised should be reduced by the estimated amount of credit sales that will never be realised i.e. by estimated amount of bad debts. Example: If a company makes a credit sale of Rs 100,000 during a period and experience indicates that 2% of credit sales will become bad debt, the amount of revenue for the period is Rs 98,000 and not Rs 100,000. It does not anticipate events and stops the business from inflating their profits by recording sales and incomes likely to accrue. Unless money has been realised as cash or legal obligation to pay on sale, profit or income is considered e.g. M places an order with N for supply of certain goods yet to be manufactured. On receipt of order N purchases raw materials, employs workers, produces goods and delivers to M. M makes payment on receipt of goods. In this case the sale is not at the time of receipt of order but at the time when goods are delivered to M.
Basics of Financial Accounting

7. Accrual Concept:

Profit arises only out of business operation when there is an increase in the owner’s share of the business and not due to his contribution to the business. Any increase in owner’s equity is called revenue and any reduction in it termed as a loan. In fact, it is the direct outcome of Realisation Concept (already discussed) and the Accounting Period concept (to be discussed). In a way, realisation concept has been split up into two parts, namely, production of economic goods or rendering of economic services, and realisation of due revenue. Any uncertainty about any of the two elements beyond what is considered uncontrollable will not permit the accountant to treat the money value or cash equivalent of the sale price to be considered as realised income. Another very vital element is involved in between, that is, a third one, namely acquiring legal right to claim the price of the goods delivered or fees for services rendered. Acquiring the legal right to claim the consideration for goods/services is called accrual of revenue, which usually precedes collection. However, in case of cash transactions, under the accrual method P/L A/c and Balance Sheet are prepared on the accrual basis, in the absence of any uncertainty about collection. This does not mean that collection has been given less importance than economic value adding and the right to claim the purchase consideration. With uncertainty about collection, it is meaningless and dangerous to take income into account as having been realised. In fact, ability to pay, is considered by the supplier of goods and services before one decides to sell his products or render his services to another. Then after the deal is finalised, goods have been delivered or services rendered and legal right to claim the purchase consideration has been acquired, collection is taken up as a specialised process to ensure return of capital and earning of profit. The other pressure comes from the Accounting Period convention. Production is a continuous process. True profit is cash profit during the entire lifetime of an enterprise. Then and then only we know total money collected and spent by it during its lifetime. But the way our culture has bound us up with annual profit, annual income and other periodic results, we have divided the entire life-span of our organisation into several chapters, each chapter being an accounting period or an accounting year. A year consists of 12 months. This is very significant, because each period being equal in terms of time frame, it facilitates comparison of performances. Because of this Cost Accountants divide a year in 13 months, each period consisting of 4 weeks. The process of dividing the life span of a company into time-chapters which is an artificial man-made process, though production follows a continuous flow, gives rise to certain accounting problems. For example, at the time of closing of period/annual accounts, production and sale might have been completed, local right to claim the sales value have been acquired, but payment has not yet come through.

8. Accounting Period Concept:

The accounting reports measure activities for a specified interval of time called the accounting period, which is usually one year and therefore termed as annual reports. Interim reports in between may be compiled especially for internal users. Except for those ventures which are predetermined to end on the completion of a specific task or a specific time-frame, every enterprise, profit-oriented or not, desires to enjoy perpetual existence as a going (running)
Financial Accounting Fundamentals

Concern, making profits, grow and distribute profits judiciously. This calls for recognition and measurement of incomes and expenses and to match them to ascertain profit. But, the concept of profit is time-related. Hence, the question: profit for what length of time? Theoretically, the most correct reply would be the entire life-time of an enterprise. That means no measurement of income until an enterprise is wound up. But human beings inherently, desire to know, periodic performances mainly for the purpose of comparison, which would not be possible, different firms wind up after different lengths of time. Moreover, from the practical point of view, some firms may not close down during a number of successive generations. Hence no income tax for ages, too. Let us not extend the list of such fanciful but important (academically) possibilities. Thus, out of practical considerations, businessmen, sided by accountants, divide the life span of an entity into a number of chapters of equal duration, usually a twelve-month period. Thus one phase of activities of an enterprise is deemed to have passed – one chapter is closed. Such a 12-month chapter is called accounting period. And financial accountants prepare a P/L A/c. for that period to estimate its operating result, that is, profit or loss and the financial position as at the end of the period in terms of assets, liabilities (external) and owners’ equity (internal liability).

Conventions:

The term "accounting conventions" refer to the customs or traditions, which are used as a guide in the preparation of meaningful financial records in the form of the income statement (Profit and Loss Account) and the position statement (Balance Sheet).

These are as follows.

1. Conservatism:

Financial statements are drawn on a conservatism basis where better evidence is required of losses. This is necessary as Management and ownership are in different hands and a cut is needed on management to show overoptimistic, favourable performance results. For example, inventories are valued at the cost or market price whichever is lower. Revenues are recognised when they are certain but expenses as soon as they are reasonably possible e.g. it encourages the accountant to create provisions for bad and doubtful debts.

Since inception, it has come to mean the following:

a) delay in recognition of income;
b) expedite recognition of income;

Note: This obviously affects the reliability of the process of matching cost against revenue.

c) if in doubt, understate assets and income;
d) if in doubt, overstate liabilities and expenses.

Note: (c) and (d) above violate the postulates of consistency and therefore comparability.
Basics of Financial Accounting

It may result in creation of Secret Reserves if overdone, which vitiates reliabilities of financial statement as the opposite operation, namely, window-dressing. Today’s accountants condemn both the practices. The driving-force behind conservatism is: it is better to be wrong on the minus side than on the plus side of financial statements. This is pessimism and not sceptics. An accountant should be sceptic and not a pessimist; the former can be convinced by sound logic while the latter can be made to change her/his mindset. Moreover, there is no standard by which the degree of conservatism may be standardised. Hence, it becomes highly subjective and may even go to the length of seriously affecting the doctrine of disclosure.

2. Consistency:

This concept states that once the organisation has decided on a method, it should use the same method subsequently unless there is a valid reason for a change of method. If frequent changes are made it is not possible to carry out comparisons on an inter-period or inter-firm basis. If a change is necessary it has to be highlighted. e.g. if depreciation is charged on diminishing balance method, it should be done year after year.

It is an accounting postulate since it develops the growth of the subject of accountancy with only a few constraints. By this standard, it is difficult to call conservatism an accounting postulate since it acts as constraints in many cases, as we have seen above. The basic prerequisite of the postulate of consistency is that the same accounting procedure, treatments, approaches, techniques, tools, concepts and principles should be applied from year to year within the firm; and also to the extent it is possible to ensure the same in all other organisations. But there are difficulties in having uniform principles and concepts and tools and procedures to be used by all the firm within a country, if not globally, mainly because of the following reasons:

a) Local custom, economic, social and political environments may differ from place to place.

b) The different nature of business of different kinds and size.

c) Presence of valid alternatives, accepted by law and standard setting bodies consistency serves two purposes, one directly and the other indirectly. Directly, it facilitates comparison, which is a vital tool for complex decision-making. Indirectly, when used over a considerable length of time it reduces risks surrounding operating enterprises.

3. Matching:

When an event affects both revenues and expenses, the effect on each period should be recognised in the same accounting period. This leads to matching concepts. The matching concepts is applied by first determining the items that constitute revenues for the period and their amounts in accordance with the conservatism concepts and than matching costs to these revenues. Thus both the aspects of an event are recorded in terms of revenue and expense in the same accounting period.
4. Disclosure:

Apart from legal requirements all significant information should be disclosed. The matching concept states that all significant information should be disclosed and all insignificant information should be disregarded. However, there are no definite rules to separate the two. For recording purposes also only significant events are recorded in detail taking into consideration the cost of detailed record keeping.

5. Materiality:

The accountant should attach importance to material details and ignore insignificant details. The question what constitutes a material detail is left to the discretion of the accountant. An item is material if there is reason to believe that knowledge of it would influence the decision of the informed investor. This has already been referred to above in connection with Disclosure. In addition to what has already been discussed, the reader is to note the following points:

a) Materiality of information  
b) Materiality of amount  
c) Materiality of procedure  
d) Materiality of nature

Materiality of Information: Misdescription of assets, liabilities, receipts and expenditures. Likewise, wrong classification between Capital and Revenue would also come under this category.

Materiality of Amount: This is a highly relative term. A fraud or an error of Rs. 5,000 may be material in a small organisation while not so in a large organisation. Which is why, the Companies Act 1956 and MAOCARO, 1988 have indicated at different places as to the degree (relatively) of tolerance. For example, an item of expense should be shown separately if it constitutes a certain percentage of the total expenses for the period.

Materiality of Procedure: Every accountant knows that some procedures are superior to others for certain purposes. For example, the various methods of depreciation, treating liability for gratuity on Cash Basis and on Actuarial Basis, etc.

Materiality of Nature: Some items are material by nature regardless of the amount involved and any other factor. A small error in such items will be considered as material always. For example, Director’s Fees, Audit Fees, amount due from directors etc.

1.3 GOLDEN RULE OF ACCOUNTING

Duality concept provides that every transaction has two sides to it – (1) the debit and (2) the credit. In other words every financial transaction involves the simultaneous receiving and giving the value.

For the purpose of making accounting entries, it is necessary to understand the nature of account. Accounting transactions involves recording of assets, debtors, expenses and capital, creditors and incomes. Incomes and expenses are known as Nominal Accounts, Assets and Capital are known as Real Accounts. In between these two groups, personal accounts like debtors and creditors are also recorded in financial books.
**Basics of Financial Accounting**

The Golden Rule of accounting provides how the duality aspect of transactions is to be recorded in the books of accounts. These rules are –

<table>
<thead>
<tr>
<th>Nature of Account</th>
<th>Rule</th>
</tr>
</thead>
</table>
| Nominal Account   | Debit all expenses and losses  
       | Credit all incomes and profits |  
| Real Account      | Debit what comes in and  
       | Credit what goes out |  
| Personal Account  | Debit the receiver and  
       | Credit the giver. |

The above rules are explained in the following transactions.

**Illustration 1 :**

During the month of January 2001, ABC Ltd. has made the following transactions –

<table>
<thead>
<tr>
<th>Item No.</th>
<th>Date</th>
<th>Transactions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>January 1</td>
<td>Issued 10,000 shares of Rs. 10 each in cash</td>
</tr>
<tr>
<td>2.</td>
<td>2</td>
<td>Purchased machinery costing Rs. 50,000 from Y Ltd.</td>
</tr>
<tr>
<td>3.</td>
<td>3</td>
<td>Purchased raw materials from Z Ltd. worth Rs. 10,000</td>
</tr>
<tr>
<td>4.</td>
<td>15</td>
<td>Paid wages in cash Rs. 15,000</td>
</tr>
<tr>
<td>5.</td>
<td>17</td>
<td>Sold goods to PQR Ltd. for Rs. 25,000</td>
</tr>
<tr>
<td>6.</td>
<td>18</td>
<td>Paid cash to Y Ltd. Rs. 20,000</td>
</tr>
<tr>
<td>7.</td>
<td>19</td>
<td>Received from PQR Ltd. Rs. 20,000</td>
</tr>
</tbody>
</table>

**Analysis of Transactions**

*Item No. 1 :* ABC Ltd. received cash from its shareholders. Cash is an asset, a real account. Cash is given by shareholders. Cash comes in — Cash A/c is debited and shareholders giving the cash is debited.

*Item No. 2 :* Machinery is a real account and it comes in, Y Ltd. gives the machinery. Therefore, Machinery A/c is debited and Y’s Ltd. A/c is credited.

*Item No. 3 :* Purchasing of goods is an expense. It is a nominal A/c and therefore should be debited, Z Ltd. gives the goods, therefore, Z Ltd. A/c should be credited.

*Item No. 4 :* Wages is an expense, a nominal account, therefore, it should be debited. Cash a real account which goes out and it should be credited.

*Item No. 5 :* Sale of goods resulted in an income, hence, credited. PQR Ltd. received the goods hence PQR Ltd. A/c should be debited.

*Item No. 6 :* Y Ltd. is a personal account who receives the cash and thus Y Ltd. is debited; cash a real account which goes out and is therefore credited.
Financial Accounting Fundamentals

Item No. 7: Cash comes in. Cash is a real A/c hence debited. PQR Ltd. gives the cash, hence it is credited.

The entries relating to above transactions are given below:

<table>
<thead>
<tr>
<th>Item no.</th>
<th>Accounts involved</th>
<th>Nature of A/c</th>
<th>Dr.(Rs.)</th>
<th>Cr.(Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Cash</td>
<td>Real</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Shareholders</td>
<td>Personal A/c</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Machinery</td>
<td>Real</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Y Ltd.</td>
<td>Personal</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Purchases</td>
<td>Nominal</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Z Ltd.</td>
<td>Personal</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Wages</td>
<td>Nominal</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cash</td>
<td>Real</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>PQR Ltd.</td>
<td>Personal</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sales</td>
<td>Nominal</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Y Ltd.</td>
<td>Personal</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cash</td>
<td>Real</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>7.</td>
<td>Cash</td>
<td>Real</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>PQR Ltd.</td>
<td>Personal</td>
<td>20,000</td>
<td></td>
</tr>
</tbody>
</table>

1.4 ACCOUNTING RECORDS

Accounting Records are maintained on the dual concept basis which states that –

Assets = Liabilities + Capital.

The above terms mean: –

i) Asset is a resource used to derive income in the future.

Assets are mainly classified as tangible or intangible. Tangible assets are those assets which can be physically seen, such as land, building, plant, cash etc. Intangible assets are those assets which cannot be physically seen e.g. goodwill, patent, copyright, etc. Again, assets can be classified as fixed and current assets. Fixed Assets are those assets which are held for a longer period of use e.g. land, building, plant, goodwill, copyright, etc. Current Assets are those assets which are held for a shorter period, generally not exceeding one year, such as cash, debtors, stock, short term investments etc.
Basics of Financial Accounting

ii) **Liability** is an amount owed by a business or organisation, e.g. creditors, loans received, bank overdraft, etc. Capital is the amount owed by the proprietor, partners or shareholders of a business or organisation.

Thus the equation states that Assets are created by owing money to the owners of the business (Capital) and other persons who owed money from the business (Liabilities).

The equation is explained by the following illustration.

**Illustration 1:**

On 31st March 2001 Mr. PQR resigned from his employment. On that date he receives from his employer Rs. 15,000. On 1st April 2001, he started a business with Rs. 15,000. On 2nd April he opened a Bank A/c by depositing Rs. 10,000; on 6th April he purchased 100 units of L at Rs. 10,000. He paid Rs. 5,000 in cash and agreed to pay balance amount after one month. On 7th April he sold 60 units of L for cash and 30 units of L on 2 months credit term. Selling price per unit Rs. 120.

April 1: Cash introduced in business Rs. 15,000

\[ \text{Cash Rs. 15,000} = \text{Proprietor’s Capital A/c 15,000} \]

Asset (cash) = Capital + Liabilities

\[ 15,000 = 15,000 + 0 \]

April 2: Opened Bank A/c by depositing Rs. 10,000

\[ \text{Cash (15,000 – 10,000) + Bank (10,000) = Capital (15,000)} \]

\[ 15,000 = 15,000 + 0 \]

April 6: Goods purchased for Rs. 10,000 paid Rs. 5,000 in cash; by the transaction as on that his stock of goods amounted to Rs. 10,000. As he paid cash Rs. 5,000, cash balance was nil and liability for goods purchased was Rs. 5,000

\[ \text{Asset (Cash + Bank) 15,000} = \text{Capital (15,000) + Liability (0)} \]

\[ 15,000 = 15,000 + 0 \]

April 7: He sold 60 units of L for cash @ Rs. 120. He therefore received Rs. 7,200 in cash and 30 units of L for credit @ 120, therefore Rs. 3,600 becomes amount receivable. He thus withdrew 90 units of L costing Rs. 9,000 which he sold at Rs. 10,800 (Rs. 7,200 + Rs. 3,600). He therefore earned an income of Rs. 1,800 which would increase his capital. The above transactions would affect the following Accounts:

\[ \text{Asset (Cash + Bank + Debtors) 20,000} = \text{Capital (15,000 + 1,800) + Liability (5,000)} \]

\[ 20,000 = 20,000 \]

\[ \text{April 7: He sold 60 units of L for cash @ Rs. 120. He therefore received Rs. 7,200 in cash and 30 units of L for credit @ 120, therefore Rs. 3,600 becomes amount receivable. He thus withdrew 90 units of L costing Rs. 9,000 which he sold at Rs. 10,800 (Rs. 7,200 + Rs. 3,600). He therefore earned an income of Rs. 1,800 which would increase his capital. The above transactions would affect the following Accounts:} \]

\[ \text{Assets = Cash (0 + 7,200), Bank (10,000), Debtors 3,600 Stock (10,000 – 9,000)} \]

\[ \text{Asset (Cash + Bank + Debtors) 20,000} = \text{Capital (15,000 + 1,800) + Liability (5,000)} \]

\[ \text{Total Assets (21,800) = Capital (16,800) + Liability (5,000)} \]
### 1.5 BOOKS OF ACCOUNT

**Journal:**

The word *journal* means a diary or a day book. In older days all monetary transactions were recorded in chronological order in the journal book based on golden rule of accounting. The entries in journal in our *earlier illustration* would have been as follows:

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>April 1</td>
<td>Cash</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To PQR’s Capital A/c</td>
<td></td>
<td>15,000</td>
</tr>
<tr>
<td>April 2</td>
<td>Bank</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Cash</td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td>April 6</td>
<td>Goods/stock</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Cash</td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>To Creditors</td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td>April 7</td>
<td>Cash</td>
<td>7,200</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Debtors</td>
<td>3,600</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Goods/Stock</td>
<td></td>
<td>9,000</td>
</tr>
<tr>
<td></td>
<td>To Capital A/c</td>
<td></td>
<td>1,800</td>
</tr>
</tbody>
</table>

However in modern accounting systems the journal is mainly divided into three parts –

1. The **General Journal**.
2. Sales and Purchase Day Books or Journals

1. The **General Journal** is used for recording —
   
   (a) Opening Entries
   (b) Closing Entries, and
   (c) Transaction of a special nature

In the general journal the following columns are normally provided.
Basics of Financial Accounting

At the foot of each entry the narration is given which shows the nature of and where necessary the authority for the entry passed.

The amount shown in the debit column of the journal entered on the debit side of the ledger and the amount shown in the credit column of the journal are entered on the credit side of the ledger.

2. Sales and Purchase Day Books or Journals.

Each credit sale (i.e. other than cash sales) are entered in the Sales Day Book or Journal with such details as are required e.g. date, name, invoice no., amount, discount allowed etc. At periodical intervals say, monthly, quarterly, half yearly or yearly additions of all entries in the Sales Day Book are made. The personal account of buyers are posted to the debit side of each buyer’s account and the total amount of sale for the respective period is credited to sales following the golden rules to debit the receiver and credit what goes out.

In case of credit purchase (i.e., other than cash purchase) purchases made by an enterprise are similarly recorded and posted to the credit of the suppliers’ account in the ledger (Personal A/c. credit the giver) and Purchase A/c is debited (Debit what comes in).

3. Sales Returns and Purchase Returns Day Books or Journals

These books or journals record sales and purchase returns. When goods already sold are returned by the buyer, they are recorded in Sales Return Day Book. Similarly when good purchased are returned to the buyer they are recorded in Purchase Return Day Book.

These journals occupy the converse position to the Day Books or Journals. Thus in case of Sales Return Day Book, Sales or Return Inward A/c. is debited and the Personal A/c. is credited. Similarly, when purchases are returned Purchase A/c is credited & Personal A/c is debited.

Ledger

Ledger is defined as a “Book which contains in a summarised and classified form of permanent record of all transactions. Ledger is called the principal book of account as final information pertaining to financial position of a business emerges from this book. The form of an account in the ledger is given below:

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Amount Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Amount Rs.</th>
</tr>
</thead>
</table>

Every account has a debit side and a credit side; Journal Folio or J.F. indicates the number of the page of the journal where the other affected account appears.
Financial Accounting Fundamentals

Sometimes ledger is also maintained in a “running account format” as follows –

### Title of the Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Folio</th>
<th>Dr. Rs.</th>
<th>Cr. Rs.</th>
<th>Balance Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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**Posting of Entries**

Consider the following Journal Entry:

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Rs.(Dr.)</th>
<th>Rs.(Cr.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 18</td>
<td>Purchases A/c</td>
<td>Dr.</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bank A/c</td>
<td></td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>(Being goods purchased).</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The above journal entry when posted to the ledger accounts would appear as follows:

**Dr. Purchases Account**

<table>
<thead>
<tr>
<th>Date (2003)</th>
<th>Particulars</th>
<th>JF</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 18</td>
<td>To Bank A/c</td>
<td>JF</td>
<td>5,000</td>
</tr>
</tbody>
</table>

[The debit side of the Purchase A/c is greater. To maintain symmetry the balance is carried down (c/d) at the end of the month to the credit side and brought down again at the beginning of the following month i.e., June 1st to the debit side. Thus it can be seen that the Purchase A/c has a debit balance.]

**Cr. Bank Account**

<table>
<thead>
<tr>
<th>Date (2003)</th>
<th>Particulars</th>
<th>JF</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 18</td>
<td>By Purchases</td>
<td>JF</td>
<td>5,000</td>
</tr>
</tbody>
</table>

**Subdivision of the Journal**

Where the number of transactions are many it would be time consuming and cumbersome if each and every transaction were to be entered in a single Journal. Usually firms maintain subsidiary books to record transactions. These books are
Basics of Financial Accounting

1. Cash Book (to record cash and bank transactions)
2. Petty Cash Book (to record cash payments involving small amounts)
3. Sales Book (to record credit sales)
4. Purchase Book (to record credit purchases)
5. Sales Return Book (to record return from customers)
6. Purchase Returns Book (to record return to suppliers)
7. Bills Receivable Book (to record acceptances received)
8. Bills Payable Book (to record acceptances given)
9. Journal Proper (to record transactions which cannot be entered in any of the above specialised Journals)

1. Cash Book

All transactions relating to each cash are recorded in the cash book, and on the basis of such a record ledger accounts are prepared. The different types of cash book are:

1. Simple Cash Book containing Cash Column only
2. Two Column Cash Book containing both Cash Column and Bank Column
3. Three Column Cash Book containing Cash, Bank and Discount columns.

(1) Simple Cash Book

The simple cash book is maintained strictly for cash transactions, a bank book being maintained separately for bank transactions. The form of a simple cash book is like that of any other account and is as follows:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Receipts</th>
<th>Payments</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>LF</td>
<td>Amount</td>
</tr>
</tbody>
</table>

(2) Two Column Cash Book

Unlike the simple cash book the Two Column Cash Book combines both bank and cash transactions for the sake of convenience due to the ever increasing bank transactions. The ruling of this book is –

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Receipts</th>
<th>Payments</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>LF</td>
<td>Cash</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

The cash book is so ruled that the debit column of cash and bank are placed alongside each other likewise with the credit column of cash and bank. The bank column contains details of payment made by cheques and money received and paid into the bank A/c.

In the folio columns the letter “C” is used whenever cash is being paid into the bank or there is a receipt from the bank, “C” means contra item and described transaction affecting only cash and bank accounts.

Illustration 2:

Enter the following transactions in a two column cash book:

1997
- Jan 1 Balances brought down – bank Rs. 5,000 and cash Rs. 450
- 3 Withdrew Rs. 2,000 from bank
- 5 Bought goods for Rs. 1,500 paying by cheque
- 8 Purchased stationery by cash Rs. 50
- 11 Paid electricity bill Rs. 100 by cheque
- 15 Sold goods for Rs. 2,000 and received cheque
- 20 Paid into bank Rs. 150

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Cash (Rs)</th>
<th>Bank (Rs)</th>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Cash (Rs)</th>
<th>Bank (Rs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan 1</td>
<td>To Balance b/d</td>
<td></td>
<td>450</td>
<td>5,000</td>
<td>Jan 3</td>
<td>By Cash</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jan 3</td>
<td>To Bank</td>
<td>C</td>
<td>2,000</td>
<td></td>
<td>Jan 5</td>
<td>by Purchases</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jan 15</td>
<td>To Sales</td>
<td></td>
<td>2,000</td>
<td></td>
<td>Jan 8</td>
<td>By Stationery</td>
<td></td>
<td></td>
<td>50</td>
</tr>
<tr>
<td>Jan 20</td>
<td>To Cash</td>
<td>C</td>
<td>150</td>
<td></td>
<td>Jan 11</td>
<td>By Electricity</td>
<td></td>
<td></td>
<td>100</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Jan 20</td>
<td>By Bank</td>
<td>C</td>
<td>150</td>
<td>2,250</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Jan 31</td>
<td>By Balance</td>
<td></td>
<td>2,450</td>
<td>3,550</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2,450</td>
<td>7,150</td>
<td></td>
<td></td>
<td></td>
<td>2,450</td>
<td>7,150</td>
</tr>
<tr>
<td>Feb 1</td>
<td>To Balance b/d</td>
<td></td>
<td>2,250</td>
<td>3,550</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Payments can easily be identified as either cash or bank payments. If a payment is made directly from bank account e.g., by a standing order it appears in the bank account column. Payments of cash are entered in the cash column. When an amount is received by cheque it should be recorded directly in the bank column. The banking on any cash is a separate transaction.
(3) Three Column Cash Book

The three column cash book has the cash and bank discount column. Cash discount is an incentive given to customers to pay before the date specified. It encourages early payment and when given to a customer is a loss and when received from a supplier is a gain. Since this discount arises only when cash is received or paid it is recorded in the cash book, discount allowed on the debit side and discount received on the credit side of the cash book. The discount columns are totalled and not balanced. The form of a three column cash book is illustrated with the following example:

**Illustration 3:**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Disc.</th>
<th>Cash</th>
<th>Bank</th>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Disc.</th>
<th>Cash</th>
<th>Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 1</td>
<td>To Balance b/d</td>
<td>709</td>
<td>3080</td>
<td>3080</td>
<td>709</td>
<td>May 2</td>
<td>By Wages</td>
<td>218</td>
<td>218</td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 4</td>
<td>To Kiran</td>
<td>13</td>
<td>177</td>
<td>177</td>
<td>13</td>
<td>May 6</td>
<td>By Ravi</td>
<td>12</td>
<td>12</td>
<td>188</td>
<td>188</td>
</tr>
<tr>
<td>May 8</td>
<td>To Ali</td>
<td>15</td>
<td>485</td>
<td>485</td>
<td>15</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 10</td>
<td>To Joshi</td>
<td>4.50</td>
<td>145.50</td>
<td>145.50</td>
<td>4.50</td>
<td>May 11</td>
<td>By Balance c/d</td>
<td>813.50</td>
<td>813.50</td>
<td>3377</td>
<td>3377</td>
</tr>
<tr>
<td></td>
<td></td>
<td>32.50</td>
<td>1031.50</td>
<td>1031.50</td>
<td>32.50</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>3565</td>
<td>3565</td>
</tr>
<tr>
<td>May 11</td>
<td>To Balance b/d</td>
<td>813.50</td>
<td>3377</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The total of the debit discount column i.e., discount allowed is transferred to the discount allowed account in the ledger. Similarly, discount received (credit discount column) is transferred to the discount received account in the ledger.

Petty Cash Book

In any business there will be numerous small cash payments. It would be advantageous if these payments could be kept separate from the main cash book. This separate book is called Petty Cash Book.

Advantages of maintaining a Petty Cash Book are:

(i) It saves the time of the General Cashier.

(ii) As the record of Petty Cash is checked by the cashier periodically, so the mistake is rectified immediately.

(iii) Under Imprest System, the Petty Cashier is not allowed to keep idle cash with him.
(iv) The chance of misappropriation is less.
(v) It trains the staff to handle money with responsibility.
(vi) It reduces the work load of general Cashier and the volume of General Cash Book becomes small.

The Imprest System

In this system the cashier gives the petty cashier a fixed amount of cash to meet his needs for the ensuing period. At the end of the period the cashier ascertains the amount spent by the petty cashier and reimburses the same to him. The petty cash in hand will then be equal to the original amount at the beginning of the period.

| Amount given by cashier at the beginning | Rs. 200 |
| Expenses during the period               | Rs. 142 |
| Petty cash in hand                       | Rs. 58  |
| Reimbursement from cashier               | Rs. 142 |
| Petty cash at the end of the period      | Rs. 200 |

Illustration 4:

2003
July 1 The cashier of a firm gives Rs. 200 as imprest to the petty cashier.
Payments of petty cash during July are:
2 Postage stamps purchased Rs. 10
3 Pencils bought Rs. 3
4 Busfare Rs. 3
5 Cleaning charges Rs. 15
6 Wages to coolie for shifting furniture Rs. 15
9 Taxi fare paid Rs. 10
10 Refreshments bought for customers for Rs. 17
14 Telegram charges Rs. 7
15 Stationery bought Rs. 9
17 Repair of chair Rs. 12
18 Battery for clock purchased Rs. 6
21 Stamps bought Rs. 8
23 Spare keys made for manager’s cabin Rs. 5
24 Busfare Rs. 2
26 Casual labour Rs. 9
27 Carbon paper Rs. 5
29 Newspaper (special edition) Rs. 3
30 Busfare Rs. 3

Write up the petty cash book, cash book and the necessary ledger accounts.
### Basics of Financial Accounting

#### Petty Cash Book

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>July 1</td>
<td>To Cash Book</td>
<td>200</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jul 2</td>
<td>By Postage</td>
<td>10</td>
<td>Jul 3</td>
<td>By Stationary</td>
<td>3</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td>Jul 4</td>
<td>By Travelling</td>
<td>3</td>
<td></td>
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<td></td>
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<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Jul 5</td>
<td>By Cleaning</td>
<td>15</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Jul 6</td>
<td>Other Expns.</td>
<td>15</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td>By Travelling</td>
<td>10</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td>By other Expns.</td>
<td>17</td>
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<td>By Postage</td>
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<td>By Stationery</td>
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<td>By other Expns.</td>
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<td>By other Expns.</td>
<td>6</td>
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<td>By Postage</td>
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<td></td>
<td></td>
<td>By Other Expns.</td>
<td>5</td>
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<td>By Travelling</td>
<td>2</td>
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<td></td>
<td>By Other Expns.</td>
<td>9</td>
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<td>By Stationery</td>
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<td></td>
<td>By Other Expns.</td>
<td>3</td>
<td></td>
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<td></td>
<td>By Travelling</td>
<td>3</td>
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<td></td>
<td></td>
<td>By Travelling</td>
<td>3</td>
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<tr>
<td>Aug 1</td>
<td>To Balance b/d</td>
<td>58</td>
<td></td>
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<td></td>
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<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug 1</td>
<td>To Cash</td>
<td>142</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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</tbody>
</table>

#### Cash Book

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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>July 1</td>
<td>By Petty Cash</td>
<td>200</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

GENERAL LEDGER

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Travelling Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 31</td>
<td>To Petty Cash</td>
<td>18</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Printing &amp; Stationery Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 31</td>
<td>To Petty Cash</td>
<td>17</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Postage &amp; Telegram Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 31</td>
<td>To Petty Cash</td>
<td>25</td>
</tr>
</tbody>
</table>

Similarly there will be Clearing Expenses and Other Expenses Accounts.

3. Sales Book

The sales book records all credit sales of goods of business, cash sales are recorded in cash book. The form of a sales book can be explained with the following example:

*Transactions of Beauty Ltd.*

2003

June 1  
Sold to P Ltd. 25 jars of cream @ Rs. 37 and 200 packets of powder @ Rs. 9.50 each less T.D. @ 10%.

2  
Sold old books to B Ltd. on credit Rs. 750

4  
Sold to S stores 35 packets of powder @ Rs. 9.50 for cash.

7  
Sold to A departmental stores 310 packets of powder @ Rs. 9.50 and 40 jars of cream @ Rs. 36 each less T.D. @ 10%.
Basics of Financial Accounting

Sales Book

<table>
<thead>
<tr>
<th>Date (2003)</th>
<th>Particulars</th>
<th>LF</th>
<th>Invoice No</th>
<th>Amount Rs.</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jun 1</td>
<td>P. Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>– 25 jars of cream @ Rs. 37</td>
<td></td>
<td></td>
<td>925.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>– 200 packets of powder @ Rs. 9.50</td>
<td></td>
<td></td>
<td>1,900.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Less : T.D. @ 10%</strong></td>
<td></td>
<td></td>
<td>282.50</td>
<td>2,542.50</td>
</tr>
<tr>
<td>Jun 7</td>
<td>A Departmental Stores</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>– 40 jars of cream @ Rs. 36</td>
<td></td>
<td></td>
<td>1,440.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>– 310 packets of powder @ Rs. 9.50</td>
<td></td>
<td></td>
<td>2,945.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Less : T.D. @ 10%</strong></td>
<td></td>
<td></td>
<td>438.50</td>
<td>3,946.50</td>
</tr>
</tbody>
</table>

Note. Cash sales and sale of the old books (asset) in cash are not entered in the sales book. Trade discount is allowed where a customer purchases goods above a certain quantity or amount. Only the net amount i.e., after deduction of trade discount is considered. No entry is made in the ledger accounts.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Sales Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>June 01</td>
<td>To Balance c/d</td>
<td>6821.50</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>6821.50</td>
</tr>
</tbody>
</table>

Difference between Trade discount and Cash discount

<table>
<thead>
<tr>
<th>Cash Discount</th>
<th>Trade Discount</th>
</tr>
</thead>
<tbody>
<tr>
<td>When payment is made earlier than the stipulated date.</td>
<td>It is normally allowed on purchases.</td>
</tr>
<tr>
<td>Cash discounts allowed/ received are accounted for in the ledger.</td>
<td>Trade discount is not entered in ledger.</td>
</tr>
<tr>
<td>It is not deducted from the invoice.</td>
<td>The amount of trade discount is deducted from the invoice.</td>
</tr>
</tbody>
</table>
4. Purchase Book

The purchase book records all credit purchases of goods of business, cash purchases and credit purchases of assets are not entered in this book. The form of a purchase book can be explained with the following illustration.

**Illustration 5 :**

**Transaction of M/s Sporting Ltd.**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 1</td>
<td>Indian Sports Co. 75 Cricket bats @ Rs. 100 each</td>
<td>7,500.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>90 Footballs @ Rs. 80 each</td>
<td>7,200.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Less : Trade Discount 10 %</strong></td>
<td>1,470.00</td>
<td>13,230.00</td>
</tr>
<tr>
<td>July 8</td>
<td>Wicket Pvt. Ltd. 40 Cricket bats @ Rs. 105 each</td>
<td>4,200.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>70 Footballs @ Rs. 82 each</td>
<td>5,740.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Less : Trade Discount 10%</strong></td>
<td>994.00</td>
<td>8,946.00</td>
</tr>
<tr>
<td>July 9</td>
<td>Green and Company 15 Hockey Sticks @ Rs. 75 each</td>
<td>1,125.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td></td>
<td>23,301.00</td>
</tr>
</tbody>
</table>

Cash purchases of goods and purchase of assets (i.e., vacuum cleaner) are not entered in the purchase book. From the purchase book a purchase account is prepared.

**Note.** The Purchase account records the cash purchases also.
Basics of Financial Accounting

**Dr. Purchase Account**

<table>
<thead>
<tr>
<th>Date (Jul '03)</th>
<th>Particulars</th>
<th>JF</th>
<th>Amount</th>
<th>Date (Jul, '03)</th>
<th>Particular</th>
<th>JF</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>3</td>
<td>To Cash</td>
<td>3825.00</td>
<td>Oct 9</td>
<td>By Balance c/d</td>
<td>27126.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>9</td>
<td>To Purchases as per purchase book</td>
<td>23301.00</td>
<td>27126.00</td>
<td></td>
<td>27126.00</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Dr. Purchase Ledger**

<table>
<thead>
<tr>
<th>Date (Jul '03)</th>
<th>Particulars</th>
<th>Amount</th>
<th>Date (Jul, '03)</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>By Purchases A/c Wicket Pvt. Ltd.</td>
<td>8946.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>By Purchases A/c</td>
<td>23301.00</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**5. Sales Return Book**

The sales return book is also known as Returns Inward Book.

Where customers frequently return the goods sold to them, it would be convenient to record the returns in a separate book called the Sales Return Book. Where goods are returned by customers, a document known as credit note will be sent to them, showing the amount of allowance given in respect of the returns. The term credit note takes its name from the fact that the customer’s account will be credited with the amount of the allowance, so as to show the reduction in the amount owed by him. The Sales Return Book is illustrated below with assumed figures:

**Sales Returns Book**

<table>
<thead>
<tr>
<th>Date (July 2003)</th>
<th>Particulars</th>
<th>JF</th>
<th>Amt. Rs.</th>
<th>Amt. Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>5</td>
<td>Indian Glassware Co.</td>
<td>160.00</td>
<td></td>
<td>144.00</td>
</tr>
<tr>
<td></td>
<td>20 Glass Cups @ Rs. 8</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Less : Trade Discount @ 10%</td>
<td>16.00</td>
<td>144.00</td>
<td></td>
</tr>
<tr>
<td>27</td>
<td>Hindustan Dept. Stores</td>
<td>150.00</td>
<td></td>
<td>135.00</td>
</tr>
<tr>
<td></td>
<td>15 Coffee Cups @ Rs. 10</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Less : Trade Discount @ 10%</td>
<td>15.00</td>
<td>135.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>279.00</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

The form of credit note is illustrated below:

Indian Glassware Co.
15, N.S.C. Road
Chennai - 600 052

To,

Bric - A - Brac Co. Ltd.
19, Lal Street,
Delhi - 110 103

Credit Note No. 8/83
Per unit
Rs.

<p>| | | |</p>
<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td></td>
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<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

20 Glass Cups 8.00 160.00
Less : Trade discount 10% 16.00
Total 144.00

The total of the Sales Return Book is transferred to the sales returns account.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Sales Return Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>-----</td>
<td>--------------</td>
<td>-------------</td>
</tr>
<tr>
<td>Jul 31</td>
<td>To Sales returns as per sales return book</td>
<td>279.00</td>
</tr>
<tr>
<td>Aug 1</td>
<td>To Balance b/d</td>
<td>279.00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Indian Glassware Co. Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Date</td>
<td>Particulars</td>
</tr>
<tr>
<td>-----</td>
<td>------</td>
<td>-------------</td>
</tr>
<tr>
<td>Jul 5</td>
<td>To Balance c/d</td>
<td>144.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>144.00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Hindustan Departmental Store</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Date</td>
<td>Particulars</td>
</tr>
<tr>
<td>-----</td>
<td>------</td>
<td>-------------</td>
</tr>
<tr>
<td>Jul 27</td>
<td>To Balance c/d</td>
<td>135.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>135.00</td>
</tr>
</tbody>
</table>
6. Purchases Returns Book

When goods are returned to suppliers these are recorded in the Purchases Returns or Returns Outward Book. A debit note is sent to the supplier stating the amount of allowance to which the firm returning the goods is entitled. The term Debit Note stems from the fact that as the liabilities to the supplier is accordingly reduced and his personal account must be debited to record this. The Return Outward book is illustrated below.

### Returns Outward Book

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 15</td>
<td>Travel Luggage Co. 2 40” Suitcases @ Rs. 500</td>
<td>1,000.00</td>
<td>100.00</td>
<td>900.00</td>
</tr>
<tr>
<td>May 26</td>
<td>Bags &amp; Bags Co One 24” travel bag</td>
<td>200.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td><strong>1,100.00</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The total of the Returns Outward Book is transferred to the Returns Outwards account.

### Dr. Return Outward Account Cr.

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 31</td>
<td>To Balance c/d</td>
<td>1,100.00</td>
<td>May 31</td>
<td>By Returns Less : Outwards as per Returns Outwards Book</td>
<td>1,100.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>June 1</td>
<td>By Balance b/d</td>
<td>1,100.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Dr. Travel Luggage Co. Cr.

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 15</td>
<td>To Returns Outward</td>
<td>900.00</td>
<td>May 15</td>
<td>By Balance c/d</td>
<td>900.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>900.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 16</td>
<td>To Balance c/d</td>
<td>900.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Dr. Bags & Bags Co. Cr.

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 26</td>
<td>To Returns Outward</td>
<td>200.00</td>
<td>May 26</td>
<td>By Balance c/d</td>
<td>200.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>200.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 27</td>
<td>To Balance b/d</td>
<td>200.00</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
7. Bills Receivable Books

When the number of bills or promissory notes received is large, instead of journalising each receipt of bills, which would be cumbersome, a register to record all receipts of bill is maintained. Every month this register are totalled. Receipts of cash in respect of bills will be recorded in the cash book. Only the endorsement of bills in favour of other parties or dishonour will be journalised. The Bill Receivable Book can be illustrated with the following example:

**Illustration**

X received the following bills:

- Sept 5: Drew on A a bill of exchange at 3 months which was accepted and returned by him on 5th Sept. 2002. The amount being Rs. 1,500.
- Sept 20: Drew on C a bill of exchange for Rs. 2,500 at 2 months which was accepted on the same day. The bill was payable at Union Bank of India.

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>From whom received</th>
<th>Acceptor</th>
<th>Date of bill</th>
<th>Term</th>
<th>Date of maturity</th>
<th>Amount</th>
<th>How disposed of</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>A</td>
<td>A</td>
<td>Sept 5</td>
<td>3 mths</td>
<td>Dec. 8</td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>C</td>
<td>C</td>
<td>Sept 20</td>
<td>2 mths</td>
<td>Nov 23</td>
<td>2,500</td>
<td></td>
</tr>
</tbody>
</table>

The total of the Bills Receivable is transferred to the Bills Receivable A/c.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Bills Receivable Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>JF</td>
</tr>
<tr>
<td>1996</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sep 30</td>
<td>To Sundries as per Bills Receivable Book</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>A’s Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>JF</td>
</tr>
<tr>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sep 5</td>
<td>By Bills Receivable A/c</td>
<td></td>
</tr>
</tbody>
</table>
8. The Bills Payable Book

The Bills Payable Book recording the acceptances given can be illustrated with the following example.

**Illustration 7**: 
M accepted the following bills.

2002
Aug 13 Accepted P’s bill for Rs. 3,000 due in one month.
Aug 17 Accepted Q’s bill for Rs. 5,000 due in two months payable at Canara Bank

<table>
<thead>
<tr>
<th>Sr. No.</th>
<th>Date of issue</th>
<th>To whom given</th>
<th>Term</th>
<th>Date of maturity</th>
<th>Where maturity</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Aug 13</td>
<td>P</td>
<td>1 mth</td>
<td>Sep 16</td>
<td></td>
<td>3,000</td>
</tr>
<tr>
<td>2</td>
<td>Aug 17</td>
<td>Q</td>
<td>2 mth</td>
<td>Nov 20</td>
<td>Canara Bank</td>
<td>5,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aug 31</td>
<td>By Sundries</td>
<td></td>
<td>8,000.00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aug 13</td>
<td>To Bills Payable A/c</td>
<td></td>
<td>3,000.00</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>JF</th>
<th>Rs. P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aug 17</td>
<td>To Bills Payable A/c</td>
<td></td>
<td>5,000.00</td>
</tr>
</tbody>
</table>

9. Journal Proper

All transactions which do not find place in the subsidiary books find place in the journal proper. Opening entries, closing entries, adjustment entries, rectification entries etc. appear in the journal proper. [All these entries are explained in detail in subsequent Study Notes].
Financial Accounting Fundamentals

e.g. Purchase of fixed asset on credit:

Asset A/c Dr.  
To Creditor’s A/c 

e.g. Drawings made by the proprietor

a) Cash drawn

Drawings A/c Dr.  
To Bank/Cash A/c 

b) Goods withdrawn at sale or purchase price for personal use:

Drawings A/c Dr.  
To Purchase/Sale A/c 

1.6 TRIAL BALANCE

In the double entry system every entry has its corresponding credit and debit. It follows, that at any given point of time, the posting from Journal, day books and cash book to the ledger is completed, the debit balances standing in all the ledgers including the cash book will equal the credit balances. At the end of the financial period (or at some other date) these balances are extracted and a schedule is prepared in journal form is called a Trial Balance. Thus the total of debit balances appearing in the Trial Balance must agree with the total of credit balances of appearing in the Trial Balance.

The next stage after posting accounts to the ledger is the preparation of a Trial Balance. The debit and credit balances of accounts are entered in this statement. The total of the debit and the total of the credit side must agree. An agreement indicates reasonable accuracy of the accounting work.

The trial balance helps in ascertaining arithmetical accuracy of the ledger accounts, location of errors and in the preparation of financial statements.

Objects of preparing Trial Balance:

1. It forms the very basis on which final accounts are prepared.
2. It helps in knowing the balance on any particular account in the ledger.
3. It is used as a test of arithmetical accuracy.

However, a Trial Balance is not a conclusive proof of absolute accuracy of the accounts. It does not indicate the absence of an error. Thus, a non-tallied Trial Balance indicates the presence of book-keeping errors.
Errors disclosed by the Trial Balance:

A Trial Balance will not agree on account of the following errors:

(i) Wrong posting of entries i.e. A debit entry of Rs. 1,000 for purchase of furniture wrongly posted as Rs. 100 in the account.
(ii) Omission of posting of debit or credit e.g. A debit entry of Rs. 1,000 for purchase of furniture is not posted at all.
(iii) Duplication of posting e.g. when debit entry of Rs. 1000 for purchase of furniture has been posted twice in the account.
(iv) Wrong side of posting e.g. when debit entry is posted on the credit side or credit entry is posted on the debit side, e.g. when a debit entry of Rs. 1000 is posted on the credit side, i.e. when debit entry of Rs. 1000 is posted on the credit side and vice versa.
(v) Errors in casting the totals of debit or credit side of the Trial Balance.
(vi) Wrong transfer of balances in the Trial Balance.
(vii) Omission of entering the balance of account in the Trial Balance.
(viii) Balance of cash book omitted to be recorded in the Trial Balance.
(ix) Wrong balancing of account.
(x) Errors in the total or posting or entries of subsidiary book.
(xi) Wrong carry forward of balance in the various books, i.e. day books, cash book, etc.

Errors not disclosed by Trial Balance

The following errors do not affect the agreement of the Trial Balance:

(i) Errors or omission; omission to record any transaction
(ii) Posting of wrong amount both debit and credit side of the account
(iii) Error made in posting of debit or credit entry is compensated by an identical error of equal amount. These errors are known as compensating errors.
(iv) Errors made in posting a transaction on the correct side of wrong account.
(v) Recording a transaction twice erroneously. These are known as errors of duplication.
(vi) Errors of principle – when the accounting principle is disregarded e.g. a capital item as revenue item and vice versa, i.e. purchase of furniture posted to Purchases Account.
Methods of locating errors in Trial Balance:

The following are some of the ways of detecting errors in the Trial Balance –

(i) When digits are wrongly interchanged — it causes the error to occur in multiples of 9. Therefore the difference is a multiple of 9, there are good chances of error occurring in transposition of digits, i.e. when 97 is recorded as 79.

(ii) When the difference is an even number divide by 2 and check whether such an amount is wrongly entered on the wrong side of debit or credit.

(iii) If the difference is a multiple of 10 or 100 or 1000, then there are chances of the error occurring in the totalling.

(iv) Ensure that all the balances of ledger accounts have been considered in the Trial Balance.

(v) Ensure that there is no omission of recording the balances from the subsidiary books or cash book.

(vi) Check all the postings and totals.

If the difference still persists, it should be transferred temporarily to Suspense Account and on locating the errors at a future date, the Suspense Account can be closed.

The format of a trial balance is as follows:

<table>
<thead>
<tr>
<th>Trial Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Ledger Accounts</strong></td>
</tr>
</tbody>
</table>

Where the debit and the credit totals of the trial balance do not agree it is an indication that one or more errors have been made. (These errors are discussed in detail in ). The trial balance is the stepping stone for the preparation of financial statements.

Illustration 1:

From the following particulars prepare a Trial Balance as on 30th September 2001:

Stock 1st October 2000 Rs. 1,380, Debtors Rs. 2,960, Creditors Rs. 1,580, Capital Account 1st Oct. 2000 Rs. 4,100, Drawings Rs. 1,200, Bills Receivable Rs. 770, Bad Debt written off Rs. 190, Provision for Bad and Doubtful Debts Rs. 160, Bills Payable Rs. 470, Wages & Salaries Rs. 1,920, Purchases Rs. 6,580, Sales Rs. 10,670, Bank Rs. 580, Cash Rs. 40, Rent, Rates & Insurance Rs. 330, Sales Returns Rs. 410, Purchases Returns Rs. 280, Fixtures & Fittings Rs. 550, General Expenses Rs. 200, Discounts allowed Rs. 520, Discounts Recd. Rs. 370.
**Basics of Financial Accounting**

**Trial Balance as on 30th Sept. 2001**

<table>
<thead>
<tr>
<th></th>
<th><strong>Dr.</strong></th>
<th><strong>Cr.</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(Rs.)</td>
<td>(Rs.)</td>
</tr>
<tr>
<td>Stock 1st Oct. 2000</td>
<td>1,380</td>
<td></td>
</tr>
<tr>
<td>Debtors and Creditors</td>
<td>2,960</td>
<td>1,580</td>
</tr>
<tr>
<td>Capital Account 1st Oct.2000</td>
<td></td>
<td>4,100</td>
</tr>
<tr>
<td>Drawings</td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td>Bills Receivable</td>
<td></td>
<td>770</td>
</tr>
<tr>
<td>Bad Debt written off</td>
<td>770</td>
<td>190</td>
</tr>
<tr>
<td>Provision for Bad &amp; Doubtful Debts</td>
<td></td>
<td>160</td>
</tr>
<tr>
<td>Bills Payable</td>
<td></td>
<td>470</td>
</tr>
<tr>
<td>Wages and Salaries</td>
<td>1,920</td>
<td></td>
</tr>
<tr>
<td>Purchases &amp; Sales</td>
<td>6,580</td>
<td>10,670</td>
</tr>
<tr>
<td>Bank</td>
<td>580</td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>40</td>
<td></td>
</tr>
<tr>
<td>Rent, Rates &amp; Insurance</td>
<td>330</td>
<td></td>
</tr>
<tr>
<td>Sales &amp; Purchases Returns</td>
<td>410</td>
<td>280</td>
</tr>
<tr>
<td>Fixtures &amp; Fittings</td>
<td>550</td>
<td></td>
</tr>
<tr>
<td>General Expenses</td>
<td>200</td>
<td></td>
</tr>
<tr>
<td>Discounts</td>
<td>520</td>
<td>370</td>
</tr>
<tr>
<td></td>
<td>17,630</td>
<td>17,630</td>
</tr>
</tbody>
</table>

**Illustration 2** : Journalise the following transactions and post them to Ledger and balance the accounts. Also prepare a Trial Balance as on 30th April 2003.

2003.

April 1  Ravi started business with Rs. 15,000 of which Rs. 4,000 were borrowed at 15% p.a. from Shri Sashi.
2  Purchased goods worth Rs. 4,000 from Anant at 2% trade discount.
3  Cash sales to Madan Rs. 1,200.
6  Credit sales to Salvi Rs. 2,000 less trade discount 2%.
9  Paid cash Rs. 1,950 to Anant and received discount of Rs. 10
12  Received Rs. 1,950 from Salvi in full settlement of his dues.
14  Returned goods of the price of Rs. 100 to Anant.
16  Paid into bank Rs. 5,000.
18  Issued a cheque for Rs. 1,000 to Anant on account.
19  Purchased goods of Rs. 2,000 from Anant.
22  Sold foods costing Rs. 1,000 at 25% profit to Ratan.
22  Received commission Rs. 800 from S & Co.
24  Received a cheque for Rs. 395 from Ratan & he was allowed discount Rs. 5.
**Financial Accounting Fundamentals**

25 Ratan returned goods of Rs. 50.
30 Paid Interest on loan Rs. 50 to Sashi.
30 Paid Salaries Rs. 2,000 out of which Rs. 1,200 paid by cheque.
30 Paid into Bank Rs. 500.
30 Paid Office Rent by cheque Rs. 300.

**Solution:**

**JOURNAL**

<table>
<thead>
<tr>
<th>Date (2003)</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apr 1</td>
<td>Cash A/c</td>
<td></td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Capital A/c</td>
<td></td>
<td>11,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Sashi’s Loan A/c</td>
<td></td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Cash brought into business and loan taken from Sashi @ 15% to start the business)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apr 1</td>
<td>Purchases A/c</td>
<td></td>
<td>3,920</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Anant’s A/c</td>
<td></td>
<td>3,920</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Credit purchases from Anant)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apr 3</td>
<td>Cash A/c</td>
<td></td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Sales A/c</td>
<td></td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Cash sales)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apr 6</td>
<td>Salvi’s A/c</td>
<td></td>
<td>1,960</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Sales A/c</td>
<td></td>
<td>1,960</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Credit Sales to Salvi)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apr 9</td>
<td>Anant’s A/c</td>
<td></td>
<td>1,950</td>
<td>98</td>
</tr>
<tr>
<td></td>
<td>To Cash A/c</td>
<td></td>
<td>1,950</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Discount A/c</td>
<td></td>
<td>10</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Paid cash to &amp; received discount from Anant.)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apr 12</td>
<td>Cash A/c</td>
<td></td>
<td>1,950</td>
<td>1,960</td>
</tr>
<tr>
<td></td>
<td>Discount A/c</td>
<td></td>
<td>10</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Salvi’s A/c</td>
<td></td>
<td>1,960</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Received cash from &amp; allowed discount to Salvi)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apr 14</td>
<td>Anant’s A/c</td>
<td></td>
<td>98</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Returns Outwards A/c</td>
<td></td>
<td>98</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Returned goods to Anant)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Apr 16</td>
<td>Bank A/c</td>
<td></td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Cash A/c</td>
<td></td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Paid cash into Bank)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Basics of Financial Accounting

Apr 18  Anant A/c
          Dr.  1,000
To Bank A/c  1,000
(Issued a cheque to Anant)

Apr 19  Purchase A/c
          Dr.  2,000
To Anant A/c  2,000
(Credit purchases from Anant)

Apr 22  Ratan’s A/c
          Dr.  1,250
To Sales A/c  1,250
(Credit sales to Ratan)

Apr 22  Cash A/c
          Dr.  800
To Commission A/c  800
(Received commission)

Apr 24  Cash A/c
          Dr.  395
Discount A/c  5
To Ratan’s A/c  400
(Received a cheque from & allowed discount to Ratan)

Apr 25  Returns Inwards A/c
          Dr.  50
To Ratan’s A/c  50
(Received goods returned by Ratan)

Apr 30  Interest A/c
          Dr.  50
To Cash A/c  50
(Paid interest for April 1993, to Sashi on loan taken from him)

Apr 30  Salaries A/c
          Dr.  2,000
To Cash A/c  800
To Bank A/c  1,200
(Paid salary Rs. 800 in cash and Rs. 1,200 by cheque)

Apr 30  Bank A/c
          Dr.  500
To Cash A/c  500
(Paid cash into bank)

Apr 30  Rent A/c
          Dr.  300
To Bank A/c  300
(Issued a cheque for office rent for April, 1993)
**Financial Accounting Fundamentals**

**LEDGER**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cash Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Amount</td>
</tr>
<tr>
<td>2003</td>
<td></td>
<td>Rs.</td>
</tr>
<tr>
<td>Apr 1</td>
<td>To Capital A/c</td>
<td>11,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td>To Sashi’s Loan A/c</td>
<td>4,000</td>
</tr>
<tr>
<td>Apr 3</td>
<td>To Sales A/c</td>
<td>1,200</td>
</tr>
<tr>
<td>Apr 12</td>
<td>To Salvi’s A/c</td>
<td>1,950</td>
</tr>
<tr>
<td>Apr 22</td>
<td>To Commission A/c</td>
<td>800</td>
</tr>
<tr>
<td>Apr 24</td>
<td>To Ratan’s A/c</td>
<td>395</td>
</tr>
<tr>
<td></td>
<td></td>
<td>19,345</td>
</tr>
<tr>
<td>May 1</td>
<td>To Balance b/d</td>
<td>11,045</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Bank A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Amount</td>
</tr>
<tr>
<td>2003</td>
<td></td>
<td>Rs.</td>
</tr>
<tr>
<td>Apr 16</td>
<td>To Cash A/c</td>
<td>5,000</td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Cash A/c</td>
<td>500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>5,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 1</td>
<td>To Balance b/d</td>
<td>3,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Salaries A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Amount</td>
</tr>
<tr>
<td>2003</td>
<td></td>
<td>Rs.</td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Cash A/c</td>
<td>800</td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Bank A/c</td>
<td>1,200</td>
</tr>
<tr>
<td>May 1</td>
<td>To Balance b/d</td>
<td>2,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Rent A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Amount</td>
</tr>
<tr>
<td>2003</td>
<td></td>
<td>Rs.</td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Bank A/c</td>
<td>300</td>
</tr>
<tr>
<td></td>
<td></td>
<td>300</td>
</tr>
<tr>
<td>May 1</td>
<td>To Balance b/d</td>
<td>300</td>
</tr>
</tbody>
</table>
### Basics of Financial Accounting

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Commission A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong>&lt;br&gt;2003</td>
<td><strong>Particulars</strong></td>
<td><strong>Amount Rs.</strong></td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Balance c/d</td>
<td>800</td>
</tr>
<tr>
<td></td>
<td></td>
<td>800</td>
</tr>
<tr>
<td></td>
<td>May 1</td>
<td>By Balance b/d</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Interest A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong>&lt;br&gt;2003</td>
<td><strong>Particulars</strong></td>
<td><strong>Amount Rs.</strong></td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Cash A/c</td>
<td>50</td>
</tr>
<tr>
<td></td>
<td></td>
<td>50</td>
</tr>
<tr>
<td>May 1</td>
<td>To Balance b/d</td>
<td>50</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Discount A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong>&lt;br&gt;2003</td>
<td><strong>Particulars</strong></td>
<td><strong>Amount Rs.</strong></td>
</tr>
<tr>
<td>Apr 12</td>
<td>To Salvi’s A/c</td>
<td>10</td>
</tr>
<tr>
<td>Apr 24</td>
<td>To Ratan’s A/c</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>15</td>
</tr>
<tr>
<td>May 1</td>
<td>To Balance b/d</td>
<td>5</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Capital A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong>&lt;br&gt;2003</td>
<td><strong>Particulars</strong></td>
<td><strong>Amount Rs.</strong></td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Balance c/d</td>
<td>11,000</td>
</tr>
<tr>
<td></td>
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<td>11,000</td>
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<td></td>
<td>May 1</td>
<td>By Balance b/d</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Sashi’s Loan A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong>&lt;br&gt;2003</td>
<td><strong>Particulars</strong></td>
<td><strong>Amount Rs.</strong></td>
</tr>
<tr>
<td>Apr 30</td>
<td>To Balance c/d</td>
<td>4,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>4,000</td>
</tr>
<tr>
<td></td>
<td>May 1</td>
<td>By Balance b/d</td>
</tr>
</tbody>
</table>
### Financial Accounting Fundamentals

#### Salvi’s A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>Apr 6 To Sales A/c</td>
<td>1,960</td>
<td>Apr 12</td>
<td>By Cash A/c</td>
<td>1,950</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Apr 12</td>
<td>By Discount A/c</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1,960</td>
</tr>
</tbody>
</table>

#### Anant’s A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>Apr 9 To Cash A/c</td>
<td>1,950</td>
<td>Apr 2</td>
<td>By Purchases A/c</td>
<td>3,920</td>
</tr>
<tr>
<td></td>
<td>Apr 9 To Discount A/c</td>
<td>10</td>
<td>Apr 19</td>
<td>By Purchases A/c</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td>Apr 14 To Returns Outwards A/c</td>
<td>98</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Apr 18 To Bank A/c</td>
<td>1,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Apr 30 To Balance c/d</td>
<td>2,862</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>5,920</td>
<td>May 1</td>
<td>By Balance b/d</td>
<td>2,862</td>
</tr>
</tbody>
</table>

#### Ratan’s A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>Apr 22 To Sales A/c</td>
<td>1,250</td>
<td>Apr 24</td>
<td>By Cash A/c</td>
<td>395</td>
</tr>
<tr>
<td></td>
<td>Apr 24 To Discount A/c</td>
<td>5</td>
<td>Apr 25</td>
<td>By Returns Inwards A/c</td>
<td>50</td>
</tr>
<tr>
<td></td>
<td>Apr 25 To Bank A/c</td>
<td>800</td>
<td>Apr 30</td>
<td>By Balance c/d</td>
<td>1,250</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,250</td>
<td>May 1</td>
<td>By Balance b/d</td>
<td>800</td>
</tr>
</tbody>
</table>

#### Purchases A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>Apr 2 To Anant</td>
<td>3,920</td>
<td>Apr 19</td>
<td>To Anant</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Apr 30</td>
<td>By Balance c/d</td>
<td>5,920</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>5,920</td>
<td></td>
<td>5,920</td>
</tr>
<tr>
<td></td>
<td>May 1 To Balance b/d</td>
<td>5,920</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Basics of Financial Accounting

#### Sales A/c

<table>
<thead>
<tr>
<th>Date 2003</th>
<th>Particulars</th>
<th>Amount</th>
<th>Date 2003</th>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Apr 3 By Cash A/c</td>
<td>1,200</td>
<td></td>
<td>Apr 6 By Salvi A/c</td>
<td>1,960</td>
</tr>
<tr>
<td>Apr 30 To Balance c/d</td>
<td>4,410</td>
<td>Apr 22 By Ratan A/c</td>
<td>1,250</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,410</td>
<td></td>
<td></td>
<td>May 1 By Balance b/d</td>
<td>4,410</td>
</tr>
</tbody>
</table>

#### Returns Outward A/c

<table>
<thead>
<tr>
<th>Date 2003</th>
<th>Particulars</th>
<th>Amount</th>
<th>Date 2003</th>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Apr 30 To Balance c/d</td>
<td>98</td>
<td>Apr 14 By Anant</td>
<td>98</td>
<td></td>
</tr>
<tr>
<td></td>
<td>98</td>
<td></td>
<td></td>
<td>May 1 By Balance b/d</td>
<td>98</td>
</tr>
</tbody>
</table>

#### Returns Inwards A/c

<table>
<thead>
<tr>
<th>Date 2003</th>
<th>Particulars</th>
<th>Amount</th>
<th>Date 2003</th>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apr 25 To Ratan’s A/c</td>
<td>50</td>
<td>Apr 30 By Balance c/d</td>
<td>50</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>50</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>May 1 To Balance b/d</td>
<td>50</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### TRIAL BALANCE as on 30th April, 2003.

<table>
<thead>
<tr>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash A/c</td>
<td>11,045</td>
</tr>
<tr>
<td>Bank A/c</td>
<td>3,000</td>
</tr>
<tr>
<td>Salaries A/c</td>
<td>2,000</td>
</tr>
<tr>
<td>Rent A/c</td>
<td>300</td>
</tr>
<tr>
<td>Commission A/c</td>
<td>800</td>
</tr>
<tr>
<td>Interest A/c</td>
<td>50</td>
</tr>
<tr>
<td>Discount A/c</td>
<td>5</td>
</tr>
<tr>
<td>Capital A/c</td>
<td>11,000</td>
</tr>
<tr>
<td>Sashi’s Loan A/c</td>
<td>4,000</td>
</tr>
<tr>
<td>Creditor (Anant)</td>
<td>2,862</td>
</tr>
<tr>
<td>Debtor (Ratan)</td>
<td>800</td>
</tr>
<tr>
<td>Purchases A/c</td>
<td>5,920</td>
</tr>
<tr>
<td>Sales A/c</td>
<td>4,410</td>
</tr>
<tr>
<td>Returns Outwards A/c</td>
<td>98</td>
</tr>
<tr>
<td>Returns Inwards A/c</td>
<td>50</td>
</tr>
<tr>
<td></td>
<td>23,170</td>
</tr>
</tbody>
</table>
Illustration 3:

Enter the following transactions in the subsidiary books and post them into ledger and prepare a Trial Balance.

2002

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Cash</th>
<th>Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Dec.</td>
<td>Mr. X started a business</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>5 Dec.</td>
<td>Purchased furniture from Vikram Furniture for</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>7 Dec.</td>
<td>Purchased goods for cash</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>10 Dec.</td>
<td>Purchased goods from AB &amp; Co. for Rs. 30,000. Trade Discount 20%</td>
<td></td>
<td>15,000</td>
</tr>
<tr>
<td>12 Dec.</td>
<td>Opened a bank account by depositing</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>14 Dec.</td>
<td>Sold goods for cash</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>15 Dec.</td>
<td>Purchased Stationery for Rs. 1,000 from Sayyed Stationery Mart</td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td>18 Dec.</td>
<td>Sold goods to Yusuf</td>
<td>400</td>
<td></td>
</tr>
<tr>
<td>20 Dec.</td>
<td>Goods returned by Yusuf</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>21 Dec.</td>
<td>Payment to AB &amp; Co. by cheque</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>22 Dec.</td>
<td>Purchased goods on Credit from Ramesh &amp; Co. for</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>23 Dec.</td>
<td>Returned goods to Ramesh &amp; Co. worth</td>
<td>400</td>
<td></td>
</tr>
<tr>
<td>23 Dec.</td>
<td>Paid Electricity Bill for</td>
<td>18,000</td>
<td></td>
</tr>
<tr>
<td>29 Dec.</td>
<td>Cash Sale for</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>30 Dec.</td>
<td>Withdraw Rs. 2,000 for private use from Bank.</td>
<td>18,000</td>
<td></td>
</tr>
</tbody>
</table>

Solution:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cash Book (with Bank Column)</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Date 2002</td>
<td>Particulars</td>
</tr>
<tr>
<td>Dec 1</td>
<td>To Capital</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Dec 12</td>
<td>To Cash A/c (Opening A/c)</td>
<td>25,000</td>
</tr>
<tr>
<td>Dec 14</td>
<td>To Sales</td>
<td>15,000</td>
</tr>
<tr>
<td>Dec 23</td>
<td>To Sales</td>
<td>2,000</td>
</tr>
<tr>
<td>Dec 30</td>
<td>To Sales</td>
<td>79,600</td>
</tr>
<tr>
<td>Jan 1</td>
<td>To Balance b/d</td>
<td>79,600</td>
</tr>
</tbody>
</table>
### BASICS OF FINANCIAL ACCOUNTING

#### Purchase Day Book

<table>
<thead>
<tr>
<th>Date (2002)</th>
<th>Particulars</th>
<th>L.F</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 10</td>
<td>AB &amp; Co.</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Less: Trade Discount</td>
<td>6,000</td>
<td>24,000</td>
</tr>
<tr>
<td>Dec 22</td>
<td>Ramesh &amp; Co.</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Purchases A/c</td>
<td></td>
<td>44,000</td>
</tr>
</tbody>
</table>

#### Sales Day Book

<table>
<thead>
<tr>
<th>Date (2002)</th>
<th>Particulars</th>
<th>L.F</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 18</td>
<td>Yusuf</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sales A/c</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Purchase Return Book

<table>
<thead>
<tr>
<th>Date (2002)</th>
<th>Particulars</th>
<th>L.F</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 23</td>
<td>Ramesh &amp; Co.</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Purchase Return A/c</td>
<td></td>
<td>2,000</td>
</tr>
</tbody>
</table>

#### Sales Return Book

<table>
<thead>
<tr>
<th>Date (2002)</th>
<th>Particulars</th>
<th>L.F</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 20</td>
<td>Yusuf</td>
<td>400</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Sales Return A/c</td>
<td></td>
<td>400</td>
</tr>
</tbody>
</table>

#### Journal Proper

<table>
<thead>
<tr>
<th>Date (2002)</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit (Rs.)</th>
<th>Credit (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec 5</td>
<td>Furniture A/c</td>
<td>Dr.</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Vikram Furniture A/c</td>
<td>Cr.</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being furniture purchased on credit)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec 13</td>
<td>Stationery A/c</td>
<td>Dr.</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Sayyed Stationary Mart</td>
<td>Cr.</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being purchase of stationery)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

**LEDGER of X**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec 31</td>
<td>To Balance c/d</td>
<td>1,00,000</td>
<td>Dec 1</td>
<td>By Cash A/c</td>
<td>1,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,00,000</td>
<td></td>
<td></td>
<td>1,00,000</td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td></td>
<td></td>
<td>By Balance b/d</td>
<td>1,00,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec 5</td>
<td>To Vikram Furniture A/c</td>
<td>20,000</td>
<td>Dec 31</td>
<td>By Balance c/d</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>20,000</td>
<td></td>
<td></td>
<td>20,000</td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td></td>
<td></td>
<td>By Balance b/d</td>
<td>20,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec 31</td>
<td>To Balance c/d</td>
<td>20,000</td>
<td>Dec 5</td>
<td>By Furniture A/c</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>20,000</td>
<td></td>
<td></td>
<td>20,000</td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td></td>
<td></td>
<td>By Balance b/d</td>
<td>20,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 9</td>
<td>To Cash A/c</td>
<td>15,000</td>
<td>Dec. 31</td>
<td>By Balance c/d</td>
<td>59,000</td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To Purchase day book</td>
<td>44,000</td>
<td></td>
<td></td>
<td>59,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>59,000</td>
<td></td>
<td></td>
<td>59,000</td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td></td>
<td></td>
<td>By Balance b/d</td>
<td>59,000</td>
</tr>
</tbody>
</table>
## Basics of Financial Accounting

### Sales Account

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Dec. 14</td>
<td>By Cash A/c</td>
<td>15,000</td>
<td>Dec. 29</td>
<td>By Cash A/c</td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To Balance c/d</td>
<td>25,000</td>
<td>Dec. 31</td>
<td>By Sales Day Book</td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>25,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td>To Balance b/fd</td>
<td>25,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Stationery Account

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 15</td>
<td>To Sayyed Stationery Mart</td>
<td>1,000</td>
<td>Dec. 31</td>
<td>By Balance c/d</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td>By Balance b/d</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Sayyed Stationery Mart

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To Balance c/d</td>
<td>1,000</td>
<td>Dec. 15</td>
<td>By Stationery A/c</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td>By Balance b/d</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Electricity Account

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 23</td>
<td>To Cash</td>
<td>400</td>
<td>Dec. 31</td>
<td>By Balance c/d</td>
<td>400</td>
</tr>
<tr>
<td></td>
<td></td>
<td>400</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td>To Balance b/d</td>
<td>400</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Drawings Account

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td></td>
<td></td>
<td>2002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 30</td>
<td>To Bank</td>
<td>2,000</td>
<td>Dec. 31</td>
<td>By Balance c/d</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td>To Balance b/d</td>
<td>2,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Financial Accounting Fundamentals

#### Purchases Return Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>To Balance c/d</td>
<td>2,000</td>
<td>2002</td>
<td>By Purchase Returns</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,000</td>
<td></td>
<td></td>
<td>2,000</td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td></td>
<td>2003</td>
<td>By Balance b/d</td>
<td>2,000</td>
</tr>
</tbody>
</table>

#### Sales Return Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>To Sales Return Book</td>
<td>400</td>
<td>2002</td>
<td>By Balance c/d</td>
<td>400</td>
</tr>
<tr>
<td></td>
<td></td>
<td>400</td>
<td></td>
<td></td>
<td>400</td>
</tr>
<tr>
<td>2003</td>
<td>Jan 1</td>
<td></td>
<td>2003</td>
<td>To Balance b/d</td>
<td>400</td>
</tr>
</tbody>
</table>

#### A B & Co. Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>To Bank A/c</td>
<td>5,000</td>
<td>2002</td>
<td>By Purchases A/c</td>
<td>24,000</td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To Balance c/d</td>
<td>19,000</td>
<td>2003</td>
<td></td>
<td>24,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>24,000</td>
<td>Jan. 1</td>
<td>By Balance b/d</td>
<td>19,000</td>
</tr>
</tbody>
</table>

#### Ramesh & Co. Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>To Purchases Returns A/c</td>
<td>2,000</td>
<td>2002</td>
<td>By Purchases A/c</td>
<td>20,000</td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To Balance c/d</td>
<td>18,000</td>
<td>2003</td>
<td></td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>20,000</td>
<td>Jan. 1</td>
<td>By Balance b/d</td>
<td>18,000</td>
</tr>
</tbody>
</table>
Basics of Financial Accounting

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>To Sales A/c</td>
<td>5,000</td>
<td>Dec. 18</td>
<td>By Sales Return</td>
<td>400</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>4,600</td>
</tr>
<tr>
<td></td>
<td></td>
<td>5,000</td>
<td></td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td>2003</td>
<td>To Balance b/d</td>
<td>4,600</td>
<td>Jan. 1</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

TRIAL BALANCE of X as on 31st December, 2002.

<table>
<thead>
<tr>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Account</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Furniture Account</td>
<td>20,000</td>
</tr>
<tr>
<td>Vikram Furniture Account</td>
<td>20,000</td>
</tr>
<tr>
<td>Purchases Account</td>
<td>59,000</td>
</tr>
<tr>
<td>Sales Account</td>
<td>25,000</td>
</tr>
<tr>
<td>Stationery Account</td>
<td>1,000</td>
</tr>
<tr>
<td>Sayyed Stationery Mart</td>
<td>1,000</td>
</tr>
<tr>
<td>Electricity Account</td>
<td>400</td>
</tr>
<tr>
<td>Drawings Account</td>
<td>2,000</td>
</tr>
<tr>
<td>Purchases Return Account</td>
<td>2,000</td>
</tr>
<tr>
<td>Sales Return Account</td>
<td>400</td>
</tr>
<tr>
<td>AB &amp; Co. Account</td>
<td>19,000</td>
</tr>
<tr>
<td>Ramesh &amp; Co. Account</td>
<td>18,000</td>
</tr>
<tr>
<td>Yusuf Account</td>
<td>4,600</td>
</tr>
<tr>
<td>Cash Account</td>
<td>79,600</td>
</tr>
<tr>
<td>Bank Account</td>
<td>18,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,85,000</strong></td>
</tr>
</tbody>
</table>
1.7 SPECIMEN QUESTIONS WITH ANSWERS

Question 1:

The following details were available from the books of Robin Singh in respect of Petty Cash Account for the year 2002-2003:

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Balance</td>
<td>10.20</td>
</tr>
<tr>
<td>Total sums debited to Petty Cash Account</td>
<td>1,112.80</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Postage</td>
<td>220.30</td>
</tr>
<tr>
<td>Stationery</td>
<td>334.65</td>
</tr>
<tr>
<td>Conveyance</td>
<td>167.30</td>
</tr>
<tr>
<td>Tea</td>
<td>90.35</td>
</tr>
<tr>
<td>Coolly and cartage</td>
<td>134.80</td>
</tr>
<tr>
<td>Miscellaneous expenses</td>
<td>125.60</td>
</tr>
<tr>
<td></td>
<td>1,073.00</td>
</tr>
</tbody>
</table>

Expenses have not been charged to the respective accounts.

Pass necessary entries at the time of finalisation and show the Petty Cash Account in the ledger.

Answer:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.(Rs.)</th>
<th>Cr.(Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundries</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Postage A/c</td>
<td>Dr.</td>
<td>220.30</td>
</tr>
<tr>
<td>Stationery A/c</td>
<td>Dr.</td>
<td>334.65</td>
</tr>
<tr>
<td>Conveyance A/c</td>
<td>Dr.</td>
<td>167.30</td>
</tr>
<tr>
<td>Tea A/c</td>
<td>Dr.</td>
<td>90.35</td>
</tr>
<tr>
<td>Coolly &amp; Cartage A/c</td>
<td>Dr.</td>
<td>134.80</td>
</tr>
<tr>
<td>Miscellaneous Expenses A/c</td>
<td>Dr.</td>
<td>125.60</td>
</tr>
<tr>
<td>To Petty Cash</td>
<td>Cr.</td>
<td>1,073.00</td>
</tr>
</tbody>
</table>

(Being petty expenses during the year as per Summary from Petty Book)
Basics of Financial Accounting

LEDGER

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Petty Cash Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To</td>
<td>Balance b/d</td>
<td>10.20</td>
</tr>
<tr>
<td></td>
<td>Cash (Total)</td>
<td>1,112.80</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,123.00</td>
</tr>
</tbody>
</table>

Question 2:

Samson furnishes you with his statement of affairs (in Rs.) as on 30th Nov., 2000 and 1999:

<table>
<thead>
<tr>
<th></th>
<th>30.11.2000</th>
<th>30.11.1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets owned:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fixed assets : Cost</td>
<td>8,00,000</td>
<td>7,00,000</td>
</tr>
<tr>
<td>Less : Depreciation provision</td>
<td>3,50,000</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Inventory at cost</td>
<td>4,50,000</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Customers dues</td>
<td>6,10,000</td>
<td>5,40,000</td>
</tr>
<tr>
<td>Bank</td>
<td>50,000</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>11,50,000</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Less : Liabilities owned:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Creditors</td>
<td>2,00,000</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Bank</td>
<td>—</td>
<td>75,000</td>
</tr>
<tr>
<td>Loan from Goliath</td>
<td>2,00,000</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>4,00,000</td>
<td>3,75,000</td>
</tr>
<tr>
<td>Net worth</td>
<td>7,50,000</td>
<td>6,25,000</td>
</tr>
</tbody>
</table>

His revenue statement for the year ended 30th November, 2000 was as under:

|                               | Rs. | Rs. | Rs. |
| Sales                        | 39,00,000 |     |     |
| Less :                       |  |     |     |
| Opening stock                | 60,000 |     |     |
| Purchases                    | 34,90,000 |     |     |
|                               | 35,50,000 |     |     |
| Less : Closing stock         | 40,000 | 35,10,000 |     |
| Gross margin                 | 3,90,000 |     |     |
### Financial Accounting Fundamentals

**Less : Expenses**  
- Interest to: Bank 16,000
- Goliath 24,000  

**Less : Depreciation**  
Net profit 1,40,000

Cash profit 2,00,000

Samson asks you to show his ledger accounts for the year ended 30th November, 2000.

**Answer :**  
Samson’s ledger for the year ended 30th November, 2000. *(Figures in Rs.)*

<table>
<thead>
<tr>
<th></th>
<th>Dr.</th>
<th>Cr.</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fixed Assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec 01, 1999</td>
<td>To Balance b/d 7,00,000</td>
<td>Dr. 7,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bank *1,00,000</td>
<td>Dr. 8,00,000</td>
<td></td>
</tr>
<tr>
<td>Nov 30, 2000</td>
<td>By Balance c/d 8,00,000</td>
<td>8,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Provision for depreciation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec 01, 1999</td>
<td>By Balance b/d 3,00,000</td>
<td>Cr. 3,00,000</td>
<td></td>
</tr>
<tr>
<td>Nov. 30, 2000</td>
<td>By Depreciation *50,000</td>
<td>Cr. 3,50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Balance c/d 3,50,000</td>
<td>3,50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Depreciation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nov. 30, 2000</td>
<td>To Provision for Deprn. 50,000</td>
<td>Dr. 50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>By Profit &amp; Loss A/c 50,000</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Inventory</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 01, 1999</td>
<td>To Balance b/d 60,000</td>
<td>Dr. 60,000</td>
<td>Nil</td>
</tr>
<tr>
<td></td>
<td>By Trading A/c 60,000</td>
<td>Dr. 60,000</td>
<td>Nil</td>
</tr>
<tr>
<td>Nov. 30, 2000</td>
<td>To Trading A/c 40,000</td>
<td>Dr. 40,000</td>
<td>Nil</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d 1,00,000</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Customers</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 01, 1999</td>
<td>To Balance b/d 5,40,000</td>
<td>Dr. 5,40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Sales 39,00,000</td>
<td>Dr. 44,40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>By Bank *38,30,000</td>
<td>Dr. 6,10,000</td>
<td></td>
</tr>
<tr>
<td>Nov. 30, 2000</td>
<td>By Balance c/d 44,40,000</td>
<td>44,40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>Suppliers</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dec. 01, 1999</td>
<td>By Balance c/d 3,00,000</td>
<td>Cr. 3,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>By Purchases 34,90,000</td>
<td>Cr. 37,90,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bank *35,90,000</td>
<td>Cr. 2,00,000</td>
<td></td>
</tr>
<tr>
<td>Nov. 30, 2000</td>
<td>To Balance c/d 2,00,000</td>
<td>37,90,000</td>
<td>37,90,000</td>
</tr>
</tbody>
</table>
### Basics of Financial Accounting

#### Goliath’s loan
- **By** Bank  
  - *  
  - 2,00,000  
  - Cr. 2,00,000

Nov. 30, 2000
- **To** Balance c/d  
  - 2,00,000  
  - 2,00,000

#### Sales A/c
- **By** Customers  
  - 39,00,000

Nov. 30, 2000
- **To** Trading A/c  
  - 39,00,000  
  - 39,00,000

#### Purchases A/c
- **To** Suppliers  
  - 34,90,000

Nov. 30, 2000
- **To** Trading A/c  
  - 34,90,000  
  - 34,90,000

#### Expenses A/c
- **To** Bank  
  - 1,00,000  
  - Dr. 1,00,000

Nov. 30, 2000
- **By** Profit & Loss A/c  
  - 1,00,000  
  - 1,00,000

#### Interest A/c
- **To** Bank - Bank  
  - *16,000  
  - Dr. 16,000

To Bank - Goliath  
- 24,000  
- Dr. 40,000

Nov. 30, 2000
- **By** Profit & Loss A/c  
  - 40,000  
  - 40,000

#### Capital A/c
- **Dec. 01, 1999**
  - **By** Balance b/d  
    - 6,25,000  
    - Cr. 6,25,000

By Net Profit  
- 2,00,000  
- Cr. 8,25,000

To Drawings - Bank  
- *75,000  
- Cr. 7,50,000

Nov. 30, 2000
- **To** Balance c/d  
  - 7,50,000  
  - 8,25,000

#### Bank A/c
- **Dec. 01, 1999**
  - **By** Balance b/d  
    - 75,000  
    - Cr. 75,000

By Fixed Assets  
- 1,00,000  
- Cr. 1,75,000

To Customers  
- 38,30,000  
- Dr. 36,55,000

By Suppliers  
- 35,90,000  
- Dr. 65,000

To Goliath’s Loan A/c  
- 2,00,000  
- Dr. 2,65,000

By Expenses  
- 1,00,000  
- Dr. 1,65,000

By Interest - Bank  
- 16,000  
- Dr. 1,49,000

By Interest - Goliath  
- 24,000  
- Dr. 1,25,000

By Capital - Drawings  
- 75,000  
- Dr. 50,000

Nov. 30, 2000
- **By** Balance c/d  
  - 50,000  
  - 40,30,000

#### Trading A/c
- **To** Opening stock  
  - 60,000  
  - Dr. 60,000

By Closing stock  
- 40,000  
- Dr. 20,000

To Purchases  
- 34,90,000  
- Dr. 35,10,000

By Sales  
- 39,00,000  
- Cr. 3,90,000

To P & L A/c – Gross Profit  
- 3,90,000  
- 39,40,000

- 39,40,000  
- 39,40,000
1.8 SELF-EXAMINATION QUESTIONS

1. State the nature and purpose of accounting.

2. Indicate briefly the concepts and conventions in accounting.


4. What is a Journal? Indicate the different types of Journals or Subsidiary Books.

5. What is a Ledger? Draw two alternative types of Ledgers.


7. What is a Trial Balance? What errors are not detected by Trial Balance?

From the following particulars prepare Journal, Ledger accounts and trial balance of “P” as on 30th June 2002 –

2002 June

   1  Started business with cash Rs. 10,000.
   7  Paid rent by cheque Rs. 550, purchased furniture Rs. 420, sold goods for cash Rs. 3,500.
   15 Purchased goods on credit from A Rs. 6,000, sold goods on credit Rs. 10,000.
   21 Deposited cash into bank Rs. 500. Received from B Rs. 6,000 & paid to A Rs. 600.
   23 Returned goods to A Rs. 500 and Returns from B Rs. 600.
   27 Received bill from B Rs. 1,000 accepted bill of A Rs. 1,500.

---

Profit & Loss A/c

<table>
<thead>
<tr>
<th>By</th>
<th>Profit (Cr.)</th>
<th>By</th>
<th>Profit (Cr.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trading A/c - Gross Profit</td>
<td>3,90,000</td>
<td>Expenses</td>
<td>2,90,000</td>
</tr>
<tr>
<td>To</td>
<td></td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>To Interest to bank</td>
<td>16,000</td>
<td>Interest to Goliath</td>
<td>2,50,000</td>
</tr>
<tr>
<td>To Interest to Goliath</td>
<td>24,000</td>
<td>Depreciation</td>
<td>2,00,000</td>
</tr>
<tr>
<td>To</td>
<td>50,000</td>
<td>Capital A/c</td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

* Balancing figures
2.0 ELEMENTS OF FINANCIAL STATEMENTS

The elements which are directly related to the measurement of financial position are assets, liabilities and equity. The elements which are directly related to the measurement of profit are income and expenses.

Asset: An asset is a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise.

Liability: A liability is a present obligation of the enterprise arising from past events the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

There is a distinction between a present obligation and future commitment. A decision by the management of an enterprise to acquire assets in future does not of itself give the rise to a present obligation.
**Financial Accounting Fundamentals**

**Equity:** In a corporate enterprise equity is classified in the Balance Sheet as Share Capital and Reserve and Surplus. Normally Equity is shown at its paid up value.

**Income and Expenses:** Income is increase in economic benefits during the accounting period in the form of inflows or enhancement of assets or decrease of liability that result in increase of equity. Whereas expenses are decreases in economic benefits during the accounting period in the form of outflows or depletion of assets or increases in liabilities that result in decrease in equity other than those relating to distribution to equity participants.

**Measurement of elements of financial statements**

Measurement is the process of determining the monetary amounts at which the elements of the financial statement are to be recognised and carried in the Balance Sheet and Income Statement. A number of different measurements are employed to define degrees in financial statements. They are as follows:

- a) Historical cost
- b) Current cost
- c) Realistic value
- d) Present value.

The commonly adopted basis is historical cost.

**Concept of Capital**

The financial concept of capital is adopted by most enterprises in preparing their financial statements. Capital is synonymous with the net assets or equity of the enterprise under a financial concept such as invested money or invested purchasing power.

**Fundamental accounting assumptions**

Certain fundamental accounting assumptions underlie preparation and presentation of financial statements. They are stated as follows:

- (a) **Going Concern:** The enterprise is normally viewed as a going concern i.e. as continuing its operation for unforeseeable future.
- (b) **Consistency:** Application of same set of accounting policies over the years in preparation of financial statements is assumed.
- (c) **Accrual:** Revenues and costs are recognized in the year to which they are related and not as paid or received.

**Disclosure of Accounting Policies**

Students should refer from any recommended Text Book:

- (a) International Accounting Standards
- (b) Indian Accounting Standards
2.1 CAPITAL AND REVENUE EXPENDITURE

**Capital expenditure** is the expenditure incurred for acquisition of assets the benefits of which are enjoyed over the years. The benefits of revenue expenditures are exhausted in the year of incurrence.

Thus it is seen that utilisation of business capital is made for two distinct purposes:

1) Expenses yielding benefits over the years termed – capital expenditure.
2) Expenditures yielding benefits during the current accounting year – termed as revenue expenditure.

Where the benefits of a revenue expenditure are extended beyond the accounting year of incurrence it is called a deferred revenue expenditure.

Suppose a company incurred an expenditure of Rs. 100000 for advertisement before marketing of a new product. If the whole amount is charged in the current year, the profit of the company would not reflect a true picture as the benefits are likely to spread over three to four years. So 1/3 or 1/4 of the expenditure will be charged to current P/L Account and the balance should be carried forward for remaining years. This will be shown on the assets side of the balance sheet as deferred revenue expenditure.

### Difference between Capital and Revenue Expenditure

<table>
<thead>
<tr>
<th>Capital Expenditure</th>
<th>Revenue Expenditure</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. It is incurred for acquiring fixed assets in use and for increasing earning capacity of the business.</td>
<td>It is incurred to run the business but does not increase the capacity of the business.</td>
</tr>
<tr>
<td>2. Benefits of such expenditure extend to years beyond which it is incurred.</td>
<td>Usually the benefit is consumed in the period in which it is incurred</td>
</tr>
<tr>
<td>3. It is shown in the Balance Sheet.</td>
<td>It is taken to the Trading / P&amp;L A/c of the concern.</td>
</tr>
</tbody>
</table>

**Illustration 1 :**

An old building which originally costs stands in the book is at Rs. 3, 00,000 is pulled down and a new one is erected in its place. Rs. 1,500 worth of material out of the old building is sold and Rs. 5,000 worth is used in new building. In addition to this Rs.5.50 lakhs is spent under a contract for its construction, Rs. 2.25 lakhs had been set aside by firm for the depreciation on the old building and is now appropriated. What addition to the Building Account will legitimately arise out of the rebuilding?
Solution:

Book value of old building 3,00,000
Less: Provision for Deprn. 2,25,000
Sale of old Materials 1,500
Old Material used in new building 5,000

2,31,500
68,500

The cost of new building should be shown as Rs. 5,50,000 + 68,500 = Rs. 6,18,500

Illustration 2:

An agricultural land was purchased for a mill was Rs. 1,00,000. Rs. 10,000 was paid for land revenue.

Solution:

Cost of land amounting to Rs. 1,00,000 will be treated as Capital Expenditure and Land revenue of Rs. 10,000 will be treated as Revenue Expenditure.

Illustration 3:

Rs. 50,000 was spent on advertising for the introduction of a new product in the market, the benefit of the market which will be divided for four years.

Solution:

Rs. 50,000 spent on advertising is to be treated as deferred revenue expenditure considering the benefit attributable for four years to come. Rs. 12,500 is to be written off every year.

Illustration 4:

Rs. 10,000 spent as lawyer's fee to defend a suit claiming that the firm's factory site belonged to the plaintiff. The suit was not successful.

Solution:

Rs. 10,000 incurred for defending the title to the firm's assets is a revenue expenditure. If, however any expenditure incurred for rectifying the title is a capital expenditure.
2.2 OPENING, CLOSING AND ADJUSTMENT ENTRIES

Opening Entries

At the end of each accounting period a firm closes its books of accounts opens new hooks at the beginning of each accounting period. The first entry in the journal is to record the closing balance of various assets and liabilities at the end of the previous year or the opening balances in the beginning of the new year. The balance sheet prepared at the end of each year records these balances. It is from these balances that the first entry is passed which is known as the “Opening Entry” e.g.

Balance Sheet as on 31st March, 1994

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital 44,200</td>
<td>Plant &amp; Machinery 50,000</td>
</tr>
<tr>
<td>Sundry Creditors 25,000</td>
<td>S. Debtors 7,500</td>
</tr>
<tr>
<td>Closing stock 5,000</td>
<td>Cash at bank 6,000</td>
</tr>
<tr>
<td>Cash in hand 700</td>
<td>69,200</td>
</tr>
</tbody>
</table>

Journal

<table>
<thead>
<tr>
<th>Dt.</th>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1994 Apr. 1</td>
<td>Cash in hand</td>
<td>Dr.</td>
<td>700</td>
</tr>
<tr>
<td></td>
<td>Cash at bank</td>
<td>Dr</td>
<td>6000</td>
</tr>
<tr>
<td></td>
<td>Stock A/c</td>
<td>Dr</td>
<td>5000</td>
</tr>
<tr>
<td></td>
<td>S. Debtors A/c</td>
<td>Dr</td>
<td>7500</td>
</tr>
<tr>
<td></td>
<td>Plant &amp; Machinery A/c</td>
<td>Dr</td>
<td>50000</td>
</tr>
<tr>
<td></td>
<td>To S. Creditors 25000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Capital 44200</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(Balances brought forward)

The above entries will then be posted to the ledger accounts as follows:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cash account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Cash</td>
</tr>
<tr>
<td></td>
<td></td>
<td>700</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Stock account</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1994</td>
<td>To Balance b/d</td>
<td>5000</td>
</tr>
</tbody>
</table>
# Financial Accounting Fundamentals

## Sundry Debtors account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apr 1</td>
<td>To Balance b/d</td>
<td>7500</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## Plant & Machinery account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apr 1</td>
<td>To Balance b/d</td>
<td>50000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## Sundry Creditors account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apr 1</td>
<td>By Balance b/d</td>
<td>25000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## Capital account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Apr 1</td>
<td>By Balance b/d</td>
<td>44200</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## Closing Entries

*In respect of Trading A/c:*

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trading A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Stock (Opening) A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Purchases A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Factory fuel &amp; power A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Factory rent &amp; rates A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Freight on purchases A/c etc.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Purchases are net purchases i.e. purchases less purchases returns)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stock (closing) A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Trading A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Sales are net sales i.e. sales less sales returns.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trading A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To P &amp; L A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>L A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(for transfer of gross profit)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Final Accounts

In respect of Profit & Loss A/c:

Items of expenses etc.

P & L A/c Dr.
To Salaries A/c
To Rent A/c
To Interest A/c

Items of gain:

Interest received A/c Dr.
Miscellaneous income A/c Dr
To P & L A/c
(The above entries will close all nominal accounts.)
P & L A/c Dr.
To Capital A/c
(transfer of net profit)
Capital A/c Dr.
To P& L A/c
(transfer of net loss)

Adjustment Entries

Adjustment means putting things in order. Adjustment entries are entries made for putting everything in order. The examples are:

i) Accrued/outstanding expenses and prepaid expenses

ii) Accrued Income and Income received in advance

iii) Depreciation

iv) Bad Debts, Provision for bad and doubtful debts, Provision for discount on debtors;
v) Commission on profits

2.3 RECTIFICATION ENTRIES

Errors may be divided into two types:
   i) Errors not affecting the trial balance.
   ii) Errors affecting the trial balance.

Errors not affecting the trial balance may be further divided into the following:
   a) Omission of an entry in the subsidiary book.
   b) Wrong entry made in the subsidiary book.
   c) Errors of principle.
   d) Posting an amount in the wrong account but on the correct side
   e) Entry made in the wrong subsidiary book.
   f) Compensating errors.

**Omission of an entry in the subsidiary book**

Here a transaction is completely omitted to be recorded in the books of accounts. For example, a credit sale to A for Rs. 2000 was omitted to be recorded in the sales book.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>A's A/c</td>
<td></td>
<td>2000</td>
</tr>
<tr>
<td>To Sales A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Rectification entry passed for omission of credit sales to A being omitted to be recorded in the sales book)</td>
</tr>
</tbody>
</table>

**Wrong entry made in the Subsidiary Book**

For example, credit purchases from Q for Rs. 3000 have been wrongly entered in the purchases book as Rs. 3300.

Purchases book has an excess debit of Rs. 300 and Q's account has an excess credit for the same amount.

Therefore, the rectifying entry will be

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q's A/c</td>
<td>300</td>
<td></td>
</tr>
<tr>
<td>To Purchases A/c</td>
<td></td>
<td>300</td>
</tr>
</tbody>
</table>

**Errors of principle**

These arise when a revenue expenditure is treated as a capital expenditure or vice versa. For example, furniture purchased from X for Rs. 4000 was entered in the purchase book.
### Final Accounts

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Wrong entry</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase A/c</td>
<td>4000</td>
<td></td>
</tr>
<tr>
<td>To X's A/c</td>
<td></td>
<td>4000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Correct entry</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Furniture A/c</td>
<td>4000</td>
<td></td>
</tr>
<tr>
<td>To X's A/c</td>
<td></td>
<td>4000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Rectifying Entry</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Furniture A/c</td>
<td>4000</td>
<td></td>
</tr>
<tr>
<td>To Purchase A/c</td>
<td></td>
<td>4000</td>
</tr>
</tbody>
</table>

Purchase A/c has been debited wrongly, therefore it has been credited [rectifying entry] in order to cancel the debit. However, X's Account has been credited correctly. As furniture A/c has to be debited in the first place it is done through the rectifying entry.

**Posting an amount in the wrong A/c but on the correct side**

e.g. Credit sales to Ramanathan for Rs. 1500 has been posted to Ramamurthy's A/c

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Wrong entry</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ramamurthy's A/c</td>
<td>1500</td>
<td></td>
</tr>
<tr>
<td>To Sales A/c</td>
<td></td>
<td>1500</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Correct entry</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ramanathan A/c</td>
<td>1500</td>
<td></td>
</tr>
<tr>
<td>To Sales A/c</td>
<td></td>
<td>1500</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Rectifying entry</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ramanathan A/c</td>
<td>1500</td>
<td></td>
</tr>
<tr>
<td>To Ramamurthy A/c</td>
<td></td>
<td>1500</td>
</tr>
</tbody>
</table>
Entry made in the wrong Subsidiary Book

e.g. Credit sales to Y Rs. 2500 was wrongly entered in the Purchases Book.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wrong entry</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase A/c Dr.</td>
<td>2500</td>
<td></td>
</tr>
<tr>
<td>To Y's A/c Cr.</td>
<td></td>
<td>2500</td>
</tr>
<tr>
<td>Correct entry</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Y's A/c Dr.</td>
<td>2500</td>
<td></td>
</tr>
<tr>
<td>To Sales A/c Cr.</td>
<td></td>
<td>2500</td>
</tr>
<tr>
<td>Rectifying Entry</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Y's A/c Dr.</td>
<td>5000</td>
<td></td>
</tr>
<tr>
<td>To Purchase A/c Cr.</td>
<td>2500</td>
<td></td>
</tr>
<tr>
<td>To Sales A/c Cr.</td>
<td>2500</td>
<td></td>
</tr>
</tbody>
</table>

Compensating Errors

If the effect of one error is multiplied by the effect of some other errors the trial balance will agree, e.g. an amount of Rs.25 received by M is not credited to his A/c and the total of the sales books is overcast by Rs. 25. The omission of credit to M's A/c is offset by the increased credit to the Sales A/c and hence the Trial Balance will agree.

Errors affecting the Trial Balance

As already discussed these errors are:

a) Omission to post to the ledger from the subsidiary book.
b) Posting the wrong amount in the ledger.
c) Posting an amount to the wrong side.
d) Wrong casting of the subsidiary book.
e) Posting wrong amount to the wrong side.
f) Posting a wrong amount to a wrong account
g) Posting a wrong amount to the wrong side of a wrong account.

Omission of posting from a subsidiary book

Goods returned to D Rs. 300 entered in the Purchases Returns Book omitted to he posted to D's A/c. D's A/c has not been debited. Therefore his A/c should be debited with Rs. 300.
Final Accounts

Posting the wrong amount in the ledger
Credit sales to Z for Rs. 120 was correctly entered in the sales book but posted to Z's A/c as Rs. 102. Z's A/c is debited short by Rs. 18(120-102). Therefore debit his A/c with Rs. 18.

Posting an amount to the wrong side
Credit purchases from U for Rs. 500 was correctly entered in the purchases book but wrongly debited to U’s A/c has to be credited with Rs. 1000.
U’s A/c is wrongly debited with Rs. 500. To Cancel this debit of Rs. 500 a credit of Rs. 500 must be given. Another credit of Rs. 500 must be given to incorporate the correct entry. Therefore a total credit of Rs. 1,000 has been given.

Wrong casting of the subsidiary book
Sales book has been totaled as Rs. 4000 the correct being Rs. 4400. Sales A/c has short credit of Rs. 400. Therefore credit sales A/c by Rs. 400.

Posting wrong amount to wrong side
Sold goods to K for Rs. 136 entered in the sales book correctly but credited to K’s a/c for Rs. 163.
K's A/c has to be debited with Rs. 299. K’s A/c has been credited wrongly for Rs. 163. To cancel this credit a debit of Rs. 163 is given. Further a debit of Rs. 136 has to be given the accommodate the correct entry. Therefore a total debit of Rs. 299 (163 + 136) has to be given.

Posting a wrong amount to the wrong account
Credit purchases from Akila for Rs. 155 was posted to the credit Akila for Rs. 165.
Debit Akila's A/c with Rs. 165.
Credit Akila's A/c with Rs. 155.
Akila's A/c has been wrongly credited therefore it should be debited to cancel the credit. Akila's A/c has not been credited.
So credit her A/c now with the correct amount Rs. 155.

Posting the wrong amount to the wrong side of a wrong account
A credit sales to W for Rs. 153 was credited to V's A/c for Rs. 135.
Debit V's A/c with Rs. 135.
Credit W's A/c with Rs. 153.
V's A/c has been credited wrongly, so his A/c is debited to cancel the wrong credit. W's A/c should have been debited in the first place.
Therefore, his A/c is now debited with Rs. 153, being the correct amount.
Financial Accounting Fundamentals

Illustration 5:
Correct the following entries.

a) Sale or goods Rs.1200 to Mr. Kumar has been entered in the sales book as Rs. 1100.

b) Machinery purchased for Rs. 11500 from XYZ Co. Ltd has been entered in the Purchases book.

c) Payment of the proprietor's personal expenses Rs. 450 has been debited to the General Expenses A/c.

d) The Returns Inwards book has been overcast by Rs. 150.

e) Discount allowed to M/s ABC Rs. 35 has not been entered in the cash book but the full amount (including discount) has been credited to M/s ABC

f) Sale of old typewriter Rs. 275 has been passed through the sales book.

Solution:

<table>
<thead>
<tr>
<th>Journal Entries</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) Kumar's A/c</td>
<td>Dr  100</td>
<td></td>
</tr>
<tr>
<td>To Sales A/c</td>
<td></td>
<td>100</td>
</tr>
<tr>
<td>(Rectifying entry passed for short credit-sales A/c and short debit to Kumar's A/c)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b) Plant &amp; Machinery A/c</td>
<td>Dr  11500</td>
<td></td>
</tr>
<tr>
<td>To Purchases A/c</td>
<td></td>
<td>11500</td>
</tr>
<tr>
<td>(Rectifying entry passed to correct machinery purchased charged to Purchases A/c)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>c) Drawing A/c</td>
<td>Dr  450</td>
<td></td>
</tr>
<tr>
<td>To General Expense A/c</td>
<td></td>
<td>450</td>
</tr>
<tr>
<td>(Rectifying entry passed to correct drawings charged to Gen. Exp. A/c)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>d) Credit Returns Inwards A/c by Rs. 150.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>e) Debit Discount allowed A/c Rs. 35.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(As the amount has not been entered in the cash book there is a short debit in the Discount Allowed A/c. Therefore the additional debit)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>f) Sales A/c</td>
<td>Dr  275</td>
<td></td>
</tr>
<tr>
<td>To Office Equipment A/c</td>
<td></td>
<td>275</td>
</tr>
<tr>
<td>(Rectifying entry passed to correct sale of old typewriter erroneously credited to Sales A/c instead of Office Equipment A/c)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Final Accounts

Suspense Account

The difference in the Trial Balance may be put in an account known as the Suspense Account, where the error causing difference cannot be located immediately and the books of accounts have to be closed. Suspense account is an account to which the difference in the trial balance has been put temporarily. If the debit side is short this account is debited and if the credit side is short it will be credited. However the opening of a suspense account does not mean that the errors need not be found out.

All errors affecting the trial balance (these were discussed earlier) are corrected through the suspense account as these are one-sided errors. Previously one sided errors have been corrected by making a correcting entry in the account concerned without making an entry in any other account. Double entry will be complete where a suspense account is opened with a difference in the trial balance.

Illustration 6:
Correct the following errors –

i) Without opening a Suspense Account, and
ii) Opening a Suspense Account

a) The Purchases Returns Book has been totalled Rs. 80 short.
b) Goods returned by M/s Amar & Sons Rs. 150 have not been recorded anywhere.
c) Goods bought from M/s Devi Bros Rs. 250 have been posted to their debit as Rs. 205.
d) Discount received from Hi-Fi Bros Rs. 25 has not been entered in the discount column of the cash book.
e) A sale to Mr. Dubey Rs. 450 was wrongly credited to his account.

Solution:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>i) Without opening a Suspense Account :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>a) Credit Purchases Returns A/c with Rs. 80.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>b) Sales Returns A/c</td>
<td>Dr 150</td>
<td></td>
</tr>
<tr>
<td>To M/s Amar &amp; Sons A/c</td>
<td></td>
<td>150</td>
</tr>
<tr>
<td>(Entry passed for goods returned as it was omitted from the Sales Returns Book)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>c) Credit M/s Devi Bros with Rs. 455.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>M/s Devi Bros have been debited Rs. 205 instead of being credited.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Therefore a credit of Rs. 205 is given to remove the wrong debit and a further credit of Rs. 250 is given to record the correct credit.)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

d) Credit Discount Received A/c Rs. 25.
(There is a short credit in the Discount Received A/c by Rs. 25. Hence an additional
credit is given to the account.)

e) Debit Mr. Dubey’s A/c with Rs. 900.
(Mr. Dubey’s A/c has been credited with Rs. 450 instead of being debited. This account is
now debited with Rs. 900 to remove the wrong credit and given the correct debit.)

ii) Opening a Suspense Account

a) Suspense A/c Dr 80
   To Purchase Returns A/c 80
   (Correction arising from undercasting of Purchases
   Returns Book)

b) Sales Returns A/c Dr 150
   To M/s Amar & Sons A/c 150
   (Recording an entry omitted earlier)

c) Suspense A/c Dr 455
   To M/S Devi Bros A/c 455
   (Correction of entry by which M/s Devi Bros were
debited Rs. 205 instead of being credited with Rs. 250)

d) Suspense A/c Dr 25
   To Discount Received A/c 25

e) Mr. Dubey’s A/c Dr 900
   To Suspense A/c 900
   (Correction of entry by which Mr. Dubey’s A/c was
credited with Rs. 450 instead of being debited)

Effect of errors and their rectification on profit or loss:

Certain errors affect the profit or loss of the firm. If the error is in the nominal account the
profit and loss account will be affected but if it is in a personal or real account there will be
no change on the profit or loss. Rectification of an error in a nominal account will change
the figure of profit or loss previously arrived at.
Illustration 7:

The Trial Balance of M/s Soles & Soles extracted on 31st March, 1997 was Rs. 1595 short on the debit side. A suspense account is opened to tally the trial balance. On examination of the books of accounts the following errors were noticed:

- a) Credit Purchases from M/s Toepuf Rs. 200 was posted as Rs. 20 in the ledger.
- b) Miser the landlord was debited Rs. 250 for payment of rent.
- c) Cash purchase of Rs.125 was not posted to the ledger.
- d) Discount allowed column in the cash book was posted to Gen. Exps are Rs.20.
- e) Payment made to Insole & Sons Rs.1500 was posted to their credit Rs.150.
- f) Received Rs.250 from Tom but posted to Thompson's A/c.
- g) Credit sale of Rs.750 to Shoes & Socks Ltd entered in the Returns Outwards Book.

Pass necessary rectifying entries. Prepare the Suspense A/c and show the effect of the rectifying entries on the profit of business.

Solution:

<table>
<thead>
<tr>
<th>S.No.</th>
<th>Particulars</th>
<th>LF</th>
<th>Dr(Rs)</th>
<th>Cr(Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>a)</td>
<td>Suspense A/c</td>
<td>Dr</td>
<td>180</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To M/s Toepuf A/c</td>
<td></td>
<td>180</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(rectification of posting of wrong amount)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>b)</td>
<td>Rent A/c</td>
<td>Dr</td>
<td>250</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Miser's A/c</td>
<td></td>
<td>250</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(rectification of payment of rent posted to Miser's (landlord) A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>c)</td>
<td>Purchases A/c</td>
<td>Dr</td>
<td>125</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Suspense A/c</td>
<td></td>
<td>125</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(cash purchases not posted rectified)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>d)</td>
<td>Discount allowed A/c</td>
<td>Dr</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Gen. Expense A/c</td>
<td></td>
<td>20</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(posting of discount allowed to Gen Exp. rectified)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>e)</td>
<td>Insole &amp; Sons A/c</td>
<td>Dr</td>
<td>1650</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Suspense A/c</td>
<td></td>
<td>1650</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(rectification of posting wrong amount i.e. Rs. 150 instead of Rs. 1500 to the credit side instead of the debit side)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
**Financial Accounting Fundamentals**

f) Thompson's A/c  
   Dr 250  
   To Tom's A/c 250  
   (receipt from Tom posted to Thompson rectified)

g) Returns Outwards A/c  
   Dr 750  
   To Sales A/c 750  
   (Credit sales recorded in Returns Outwards Book rectified)

<table>
<thead>
<tr>
<th>Dr. Particulars</th>
<th>Rs</th>
<th>Cr. Particulars</th>
<th>Rs</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Difference in Trial Balance</td>
<td>1595</td>
<td>By Purchases</td>
<td>125</td>
</tr>
<tr>
<td>To M/s Toepuf</td>
<td>180</td>
<td>By Insole &amp; Sons</td>
<td>1650</td>
</tr>
<tr>
<td></td>
<td>1775</td>
<td></td>
<td>1775</td>
</tr>
</tbody>
</table>

**Effect of rectifying entries on profit**

   a) No effect  
   b) Profit reduced by Rs. 250  
   c) Profit reduced by Rs. 125  
   d) No effect  
   e) No effect  
   f) No effect  
   g) No effect

**Rectification in the next trading period:**

   In order to ascertain the profit or loss of each period separately errors should be rectified in such a manner that the current year's income, expenses or loss are not affected.

   An error committed in 2001-02 is rectified in 2002-03. By rectifying Sales A/c would mean that it is treated as an income of 2002-03 when it actually pertains to 2001-02. Therefore the proper thing to do should be to open a separate account called the Profit & Loss Adjustment account and pass all debits and credits in respect of nominal accounts for errors committed in the previous period through this account. The balance of this account is transferred to the Capital A/c.

   Only when rectification is carried out in the next trading period and if it pertains to the nominal accounts alone this procedure be adopted. Rectification in the current period is made in the usual manner.
Illustration 8:

On 31st March, 2003, the Trial Balance of Mr. Good did not agree. The difference was transferred to a Suspense Account. In May 2003, the errors of March 1997 were discovered. They are:

1) The Returns Outwards Book was overcast by Rs. 700.
2) Purchase of furniture Rs. 2000 was passed through the Purchases Book.
3) Wages to workmen for installation of machinery Rs.1250 was charged to Wages A/c.
4) Payment of rent of Mr. Goods house Rs. 750 was charged to Rent A/c.
5) Goods returned by a customer amounted to Rs. 950 were taken into stock but no entry was made in the book.
6) Sale of goods worth Rs. 1700 has been passed through Purchases book. The Customer's A/c has been however debited correctly.
7) Sale of Rs. 2250 to M/s Wye Ltd was credited to their A/c.
8) Sales Book total while being carried forward to the next page was written as Rs. 219431 instead Rs. 291341.
9) A sale of Rs. 760 has been posted to the credit of the customer's Mr. Zed A/c as Rs. 670.
10) A cheque for Rs. 1500 received from M/s Sky Bros was dishonoured and posted to the debit of Allowances A/c.

Give journal entries to rectify the above errors without affecting the current year's Profit and Loss Adjustment A/c

Prepare the Profit & Loss Adjustment A/c.

Solution:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) P &amp; L Adjustment A/c</td>
<td>Dr 700</td>
<td></td>
</tr>
<tr>
<td>To Suspense A/c</td>
<td></td>
<td>700</td>
</tr>
<tr>
<td>2) Furniture A/c</td>
<td>Dr 2000</td>
<td></td>
</tr>
<tr>
<td>To P &amp; L Adjustment A/c</td>
<td></td>
<td>2000</td>
</tr>
<tr>
<td>3) Machinery are</td>
<td>Dr 1250</td>
<td></td>
</tr>
<tr>
<td>To P &amp; L Adjustment A/c</td>
<td></td>
<td>1250</td>
</tr>
</tbody>
</table>
### Financial Accounting Fundamentals

4) **Drawings A/c**  
   Dr. 750  
   To P & L Adjustment A/c  
   Rs. 750

5) **P&L Adjustment A/c**  
   Dr. 950  
   To Customer’s A/c  
   Rs. 950

6) **Suspense A/c**  
   Dr. 3400  
   P&L Adjustment A/c  
   Rs. 3400

7) **M/s Wye Ltd. A/c**  
   Dr. 4500  
   To Suspense A/c  
   Rs. 4500

8) **Suspense A/c**  
   Dr. 71910  
   To P&L Adjustment A/c  
   Rs. 71910

9) **Suspense A/c**  
   Dr. 1430  
   To Mr. Z’s A/c  
   Rs. 1430

10) **M/s Sky Bros. A/c**  
    Dr. 1500  
    To P&L Adjustment A/c  
    Rs. 1500

   **P&L Adjustment A/c**  
   Dr. 79160  
   To Capital A/c  
   Rs. 79160

---

<table>
<thead>
<tr>
<th>Dr. Profit And Loss Adjustment Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong></td>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>To Suspense A/c</td>
<td>700</td>
</tr>
<tr>
<td>&quot; Customer’s A/c</td>
<td>950</td>
</tr>
<tr>
<td>&quot; Capital A/c (Bal. fig)</td>
<td>79160</td>
</tr>
<tr>
<td>&quot; Suspense</td>
<td>3400</td>
</tr>
<tr>
<td>&quot; M/s Sky Bros.</td>
<td>1500</td>
</tr>
</tbody>
</table>
Illustration 9:

The books of accounts of B. Quick for the year ending 31st March, 2003 were closed with a difference in books carried forward. The following errors were detected subsequently:

(i) Goods Rs. 125 returned to Mita Bros. were recorded in the Returns Inward Book as Rs. 251 and from there it was posted to the debit of Mita Bros. Account.

(ii) A credit sale of Rs. 760 was wrongly posted as Rs. 670 to the customers account in the Sales Ledger.

(iii) Closing Stock was overstated by Rs. 5,000 being casting error in the schedule of inventory.

(iv) Paid acceptance to Bala Ram for Rs. 7,600 was posted to the debit of Sita Ram as Rs. 6,700.

(v) Goods purchased from A & Co. Rs. 3,250 entered in the Sales Day Book for Rs. 3,520.

(vi) Rs. 1,500 being the total of the discount column on the credit side of the Cash Book was not posted. Pass rectification entries in the next year.

Solution:

In the books of B. Quick

<table>
<thead>
<tr>
<th>JOURNAL ENTRIES</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>LF</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>i)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Suspense A/c (251×2)</td>
<td>Dr.</td>
<td>502</td>
<td></td>
</tr>
<tr>
<td>To Mita Bros. (251 – 125)</td>
<td></td>
<td>126</td>
<td></td>
</tr>
<tr>
<td>To Profit &amp; Loss Adjustment A/c</td>
<td></td>
<td>376</td>
<td></td>
</tr>
<tr>
<td>(Being the amount of purchase return to Mita Bros. Rs. 125 wrongly recorded in return inward book as Rs. 251 and posted to the debit of Mita Bros. A/c — now rectified)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ii)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors A/c</td>
<td>Dr.</td>
<td>90</td>
<td></td>
</tr>
<tr>
<td>To Suspense account (760 – 670)</td>
<td></td>
<td>90</td>
<td></td>
</tr>
<tr>
<td>(Being credit sale of Rs. 760 wrongly posted to the customers account as Rs. 670 — now rectified).</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>iii)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Suspense A/c</td>
<td>Dr.</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>To P&amp;L adjustment A/c</td>
<td></td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>(Being Closing Stock amount was wrongly overcast — now rectified).</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
iv) Bala Ram’s A/c Dr. 7,600  
   To Sita Ram’s A/c 6,700  
   To Suspense A/c 900  
   (Being acceptance paid to Bala Ram Rs. 7,600 wrongly posted to the debit of Sita Ram as Rs. 6,700 — now rectified).

v) Profit & Loss Adjustment A/c Dr. 6,770  
   To M/s A. & Co. A/c 6,770  
   (Being goods purchased from A & Co. Rs. 3,250 entered wrongly in Sales Day Book as Rs. 3,520 — now rectified).

vi) Suspense A/c Dr. 1,500  
    To Profit & Loss Adjustment account 1,500  
    (Being the amount of discount column on the Credit side of Cash Book was not posted — now rectified).

Illustration 10 :

Following mistakes occurred in a computerised accounting system :–

(a) Payment of Rs. 10,000 to a party by cheque was recorded through the receipt column of the bank account;

(b) Receipt of Rs. 25,000 from a customer was entered through the payment column of the bank account;

(c) Purchase invoice of Rs. 51,000 was entered through the sales journal as Rs. 15,000;

(d) Sales bill of Rs. 46,000 was entered through the purchase journal as Rs. 64,000;

(e) Returns inwards of Rs. 6,000 was entered through the purchase journal as Rs. 60,000;

(f) Returns outwards of Rs. 5,000 was entered through the sales journal as Rs. 500.

What will be the changes in final accounts on rectification of the above mistakes? Pass the rectification entries and pinpoint the changes.

Solution :

Rectification and effects

a) Sundry Debtors Dr. 20,000  
   To Bank Account 20,000  
   *Effect : Liability to suppliers-reduced by Rs. 20,000;  
    Bank balance-reduced by Rs. 20,000;  
    (No impact on Profit/loss)*
Final Accounts

b) Bank Account
   To Sundry Creditors Account 25,000
   To Sundry Debtors Account 25,000
   \(\text{(assuming the supplier party wrongly debited)}\)
   \textit{Effects:} Dues from customers-reduced by Rs. 25,000;
   Bank balance -increased by Rs. 50,000
   Dues to supplier party-increased by Rs. 25,000; No impact on Profit/loss.

c) Purchases Account Dr. 51,000
   Sales Account 15,000
   To Party Account 51,000
   To Sundry Account 15,000
   \textit{Effect:} Liabilities to suppliers-increased by Rs. 51,000;
   Purchases-increased by Rs. 51,000;
   Sundry debtors-reduced by Rs. 15,000
   Sales reduced by Rs. 15,000
   Profit reduced by Rs. 66,000

d) Sundry Creditors Account Dr. 64,000
   Sundry Debtors Account Dr. 46,000
   To Purchases Account 64,000
   To Sales Account 46,000
   \textit{Effect:} Personal account of the party reduced by Rs. 64,000;
   Sales-increased by Rs. 46,000;
   Sundry debtors-increased by Rs. 46,000;
   Profit-increased by Rs. 1,10,000

e) Returns Inwards Account Dr. 6,000
   Sundry creditors Account Dr. 60,000
   To Sundry Debtors Account 6,000
   To Purchases Account 60,000
   \textit{Effect:} Amount due to supplier party-reduced by Rs. 60,000;
   Purchase-reduced by Rs. 6,000;
   Sundry debtors-reduced by Rs. 6,000;
   Profit-goes up by Rs. 54,000.
Illustration 11:
The trial balance of M/s Ganguly & Co. as at 31.03.2003 did not agree. In order to close the books the accountant transferred the difference to the Suspense A/c newly opened and carried forward the difference to the next period for necessary adjustments. Later, the following errors, arising in 2002-03 were detected —

(a) Sales Day book was overcast by Rs. 100 in January, 2003.
(b) Furniture purchased for Rs. 2,500 cash was posted to the purchase account in the Ledger.
(c) Credit Sale of Rs. 97 was posted to the credit of the Customer's Account as Rs. 79.
(d) Rs. 50 allowed as Cash discount to a Trade Debtor was not debited to the Discount Account.
(e) An item of purchase of Rs. 162 was recorded in the Purchase Day Book as Rs. 62 and posted to the debit of the Supplier's Account as Rs. 26. Show the necessary journal entries to rectify these errors and show Suspense Account; and Profit and Loss Adjustment Account and state the ultimate effect of these correcting entries in the books for 2003-04.

Solution:

In the books of M/s GANGULY & CO.

<table>
<thead>
<tr>
<th>Date (2003)</th>
<th>Particulars</th>
<th>L/F</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>April 1</td>
<td>Profit &amp; Loss Adjustment A/c</td>
<td>Dr.</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Suspense A/c</td>
<td></td>
<td></td>
<td>100</td>
</tr>
</tbody>
</table>

(Being Sales day book overcast by Rs. 100, now rectified)
Final Accounts

b) Furniture A/c
To Profit & Loss Adjustment A/c
Dr. 2,500
(Being furniture purchased has been posted to the purchase A/c, now rectified)

c) Customers A/c
To Suspense A/c
Dr. 176
(Being credit sale of Rs.97 wrongly posted to the credit of Customer's A/c, as Rs. 79)

d) Profit & Loss Adjustment A/c
To Suspense A/c
Dr. 50
(Being discount allowed not posted to discount allowed A/c, now rectified)

e) Profit & Loss Adjustment A/c
Suspense A/c
To Supplier A/c
Dr. 100
Dr. 88
188
(Being purchase of Rs. 162 entered in the purchase book as Rs. 62 but posted to the debit of supplier A/c as Rs. 26, now rectified)

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Suspense Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>L/F</td>
</tr>
<tr>
<td>To Balance b/f (Bal. Fig.)</td>
<td>238</td>
<td>By Profit &amp; Loss Adj. A/c</td>
</tr>
<tr>
<td>To Supplier A/c</td>
<td>88</td>
<td>By Customer A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Profit &amp; Loss Adj. A/c</td>
</tr>
<tr>
<td></td>
<td>326</td>
<td>326</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Profit &amp; Loss Adjustment Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>L/F</td>
</tr>
<tr>
<td>To Supplier's A/c</td>
<td>100</td>
<td>By Furniture A/c</td>
</tr>
<tr>
<td>To Suspense A/c</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>To Suspense A/c</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>To Partner's Capital A/c</td>
<td>2,250</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,500</td>
<td>2,500</td>
</tr>
</tbody>
</table>

2.4 ADJUSTED TRIAL BALANCE

A Trial Balance should be prepared before the adjusting entries are recorded in order to ensure that the debits are equal to the credits. In addition another Trial Balance prepared after recording the adjusting entries. This Trial Balance is called an Adjusted Trial Balance which provides a convenient source of information for the preparation of final accounts.
Illustration 12:

From the following details prepare an Adjusted Trial Balance after passing the necessary adjustment entries:

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase</td>
<td>65,000</td>
</tr>
<tr>
<td>Carriage Inward</td>
<td>1,000</td>
</tr>
<tr>
<td>Wages</td>
<td>6,000</td>
</tr>
<tr>
<td>Salaries</td>
<td>10,000</td>
</tr>
<tr>
<td>Rent, rates and taxes</td>
<td>1,800</td>
</tr>
<tr>
<td>Insurance</td>
<td>1,500</td>
</tr>
<tr>
<td>interest paid</td>
<td>1,000</td>
</tr>
<tr>
<td>Sales</td>
<td>95,000</td>
</tr>
<tr>
<td>Cash and Bank</td>
<td>21,500</td>
</tr>
<tr>
<td>Bills Payable</td>
<td>5,800</td>
</tr>
</tbody>
</table>

Notes –

1. Salaries and wages due to be paid Rs. 2,000 and Rs. 1,500 respectively.
2. Insurance was paid to the extent of Rs. 300 advance.
3. A sum of Rs. 500 to be written off as bad debt out of sundry debtors and a provision of 5% to be created for doubtful debts.
4. Sundry expenses include Rs. 2,000 spent for the personal purpose of the proprietor.
5. Sales for the period include Rs. 500 worth of goods (cost price) taken by the proprietor for personal consumption. He has also taken goods worth Rs. 1,000 (cost price) for personal consumption which has not been recorded in the books.
6. Depreciation to be provided as follows:–
   - Plant and Machinery 10%
   - Building 5%
   - Furniture 10%
7. Closing Stock Rs. 20,000

Solution:

| JOURNAL ENTRIES |
|-----------------|---|---|
| Particulars     | L.F. | Dr. | Cr. |
| Salaries A/c    |     | 2,000 |     |
| To Outstanding Salaries A/c  | Dr. | 2,000 |     |
| (Outstanding salaries adjusted) |     |     |     |
**Final Accounts**

<table>
<thead>
<tr>
<th>Account</th>
<th>Dr</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wages A/c</td>
<td>1500</td>
<td>To Outstanding Wages A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Outstanding wages adjusted)</td>
</tr>
<tr>
<td>Drawings A/c</td>
<td>2000</td>
<td>To Sundry Expenses A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Sundry Exp. A/c now adjusted)</td>
</tr>
<tr>
<td>Sales A/c</td>
<td>500</td>
<td>To Sundry Debtors A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Goods taken by the proprietor for personal consumption and included in sales now cancelled)</td>
</tr>
<tr>
<td>Drawings A/c</td>
<td>1500</td>
<td>To Purchase A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Goods taken by the proprietor at cost price for personal consumption)</td>
</tr>
<tr>
<td>Prepaid Insurance A/c</td>
<td>300</td>
<td>To Insurance A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Insurance premium paid in advance adjusted)</td>
</tr>
<tr>
<td>Bad Debts A/c</td>
<td>500</td>
<td>To Sundry Debtors A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Amount written off as bad debt)</td>
</tr>
<tr>
<td>Bad Debts A/c</td>
<td>1950</td>
<td>(5% on (40000-500-500)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>To Provision for Bad Debts a/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Provision for Bad Debts created @ 5% on Debtors)</td>
</tr>
<tr>
<td>Depreciation A/c</td>
<td>1550</td>
<td>To Plant &amp; Machinery</td>
</tr>
<tr>
<td></td>
<td></td>
<td>To Buildings</td>
</tr>
<tr>
<td></td>
<td></td>
<td>To Furniture</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Depreciation provided on various assets)</td>
</tr>
<tr>
<td>Closing Stock A/c</td>
<td>20000</td>
<td>To Purchases</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Closing stock adjusted to purchases)</td>
</tr>
</tbody>
</table>

*Note:* Since here provisions for Doubtful Debts is to be created before preparing final accounts Bad Debts A/c has been debited instead of P & L A/c.
### Financial Accounting Fundamentals

#### Trial Balance as at ........

<table>
<thead>
<tr>
<th>Account</th>
<th>Dr</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Purchases (65000 - 1500 - 20000)</td>
<td>43500</td>
<td></td>
</tr>
<tr>
<td>Carriage Inward</td>
<td>1000</td>
<td></td>
</tr>
<tr>
<td>Wages (6000 +1000)</td>
<td>7000</td>
<td></td>
</tr>
<tr>
<td>Salaries (10000 +2000)</td>
<td>12000</td>
<td></td>
</tr>
<tr>
<td>Rent, Rates &amp;Taxes</td>
<td>1800</td>
<td></td>
</tr>
<tr>
<td>Interest (1500 - 300)</td>
<td>1200</td>
<td></td>
</tr>
<tr>
<td>Interest Paid</td>
<td>1000</td>
<td></td>
</tr>
<tr>
<td>Sales (95000 - 500)</td>
<td></td>
<td>94500</td>
</tr>
<tr>
<td>Cash &amp; Bank</td>
<td>21500</td>
<td></td>
</tr>
<tr>
<td>Bills Payable</td>
<td></td>
<td>5800</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td></td>
<td>35000</td>
</tr>
<tr>
<td>Plant &amp; Machinery (10000 - 1000)</td>
<td>9000</td>
<td></td>
</tr>
<tr>
<td>Buildings (5000 - 250)</td>
<td>4750</td>
<td></td>
</tr>
<tr>
<td>Furniture (3000 - 300)</td>
<td>2700</td>
<td></td>
</tr>
<tr>
<td>Bills Receivable</td>
<td>10000</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors (40000 – 500 - 500)</td>
<td>39000</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td></td>
<td>66000</td>
</tr>
<tr>
<td>Sundry Expenses (5000 – 2000)</td>
<td>3000</td>
<td></td>
</tr>
<tr>
<td>Opening Stock</td>
<td>21000</td>
<td></td>
</tr>
<tr>
<td>Outstanding Salaries</td>
<td></td>
<td>2000</td>
</tr>
<tr>
<td>Outstanding Wages</td>
<td></td>
<td>1000</td>
</tr>
<tr>
<td>Drawings (2000 +1500)</td>
<td>3500</td>
<td></td>
</tr>
<tr>
<td>Prepaid Insurance</td>
<td>300</td>
<td></td>
</tr>
<tr>
<td>Bad-Debts (500 +1950)</td>
<td>2450</td>
<td></td>
</tr>
<tr>
<td>Provision for Bad Debts</td>
<td></td>
<td>1950</td>
</tr>
<tr>
<td>Depreciation</td>
<td>1550</td>
<td></td>
</tr>
<tr>
<td>Closing Stock</td>
<td>20000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>206250</td>
<td>206250</td>
</tr>
</tbody>
</table>

#### Balance Sheet

The Balance Sheet is a statement which sets out the Assets and Liabilities as on a certain date. It is prepared with a view to measure the true financial position at a particular point of time. The Balance Sheet has the following form.
**Final Accounts**

**Balance Sheet as on ..........**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Amount</th>
<th>Assets</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry on Trade</td>
<td>Cash in hand</td>
<td>Cash at hank</td>
<td></td>
</tr>
<tr>
<td>Creditors [including petty cash]</td>
<td></td>
<td>Bills payable</td>
<td></td>
</tr>
<tr>
<td>Bills payable</td>
<td></td>
<td>Loans (Dr)</td>
<td></td>
</tr>
<tr>
<td>Loans</td>
<td></td>
<td>Mortgage</td>
<td></td>
</tr>
<tr>
<td>Reserve or Reserve Fund</td>
<td>Investments</td>
<td>Reserve or Reserve Fund</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>Furniture &amp; Fittings</td>
<td>Add: Interest on capital</td>
<td></td>
</tr>
<tr>
<td>Add: Interest on capital</td>
<td>Loose Tools</td>
<td>Add: New profit</td>
<td></td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>Plant &amp; Machinery</td>
<td>Less: Interest on Drawings</td>
<td></td>
</tr>
<tr>
<td>Less: Income tax</td>
<td>Freehold &amp; leasehold Land</td>
<td>Less: Income tax</td>
<td></td>
</tr>
<tr>
<td>Goodwill</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

A **Balance Sheet** has the following characteristics:

a) It is prepared at a particular date and not for a period.

b) It is prepared only after preparation of the Trading and Profit & Loss A/c. Without the Profit & Loss A/c it will not give the financial position of the firm adequately.

c) Capital is equal to the difference of assets and liabilities. Therefore the two sides of the balance sheet must have the same totals otherwise it is an indication of the presence of errors.

d) It is not an account but only a statement of assets and liabilities.

e) The balance sheet shows the financial position of a business at going concern concept.

**Difference between a Trial Balance and a Balance Sheet**

<table>
<thead>
<tr>
<th>Trial Balance</th>
<th>Balance Sheet</th>
</tr>
</thead>
<tbody>
<tr>
<td>The purpose of a trial balance is to establish the arithmetical accuracy of the books of accounts.</td>
<td>The Balance Sheet aims at reflecting the financial position of the business.</td>
</tr>
<tr>
<td>No information about profits can be obtained from the trial balance.</td>
<td>Information about profit can be obtained from the balance sheet.</td>
</tr>
<tr>
<td>It may be possible to dispense with the preparation of the trial balance though its preparation is desirable.</td>
<td>To complete the accounting process the balance must be essentially be prepared.</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

All accounts personal, real and only personal and real accounts find place in the balance sheet.

Normally Trial balances are prepared monthly. Balance sheet is prepared at the end of the trading period.

A trial balance can be prepared with or without adjustment. A trial balance incorporating adjustments is known as the adjusted trial balance.

Closing stock does not appear in the trial balance however it may appear where an adjusted trial balance is prepared.

Assets & Liabilities Arrangement

Assets may be grouped as follows:

<table>
<thead>
<tr>
<th>In order of Liquidity</th>
<th>In order of Performance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in hand</td>
<td>Goodwill</td>
</tr>
<tr>
<td>Cash at bank</td>
<td>Patents</td>
</tr>
<tr>
<td>Investments</td>
<td>Land &amp; Buildings</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>Machinery</td>
</tr>
<tr>
<td>Stock of finished goods</td>
<td>Furniture</td>
</tr>
<tr>
<td>Stock of partly finished goods</td>
<td>Stock of partly finished goods</td>
</tr>
<tr>
<td>Stock of raw materials</td>
<td>Stock of raw materials</td>
</tr>
<tr>
<td>Furniture</td>
<td>Stock of finished goods</td>
</tr>
<tr>
<td>Machinery</td>
<td>Sundry Debtors</td>
</tr>
<tr>
<td>Land and Buildings</td>
<td>Investment</td>
</tr>
<tr>
<td>Patents</td>
<td>Cash at bank</td>
</tr>
<tr>
<td>Goodwill</td>
<td>Cash in hand</td>
</tr>
</tbody>
</table>

Liquidity: Liquidity means the case with which assets may be converted into cash. Assets which are most difficult in this respect are written last.

Permanence: Assets which are to be used permanently in the business and are meant to be sold are written first.

Liabilities: Liability may be shown according to the urgency with which payment has to be made. Short term liabilities such as bills payable, and sundry creditors for supply of goods may be shown first, then long term liabilities and lastly capital. Another way is to show capital, long term liabilities and last short term liabilities.
Assets and Liabilities-Classification :-

Assets may be classified as –

a) Fixed Assets
   i) Tangible fixed assets.
   ii) Intangible fixed assets.
   iii) Investments (longterm)

b) Current Assets

Fixed Assets : Fixed asset is an asset acquired for continuing use within the business with a view to earning income or making profits from its use either directly or indirectly. A fixed asset is not acquired for sale to a customer.

A tangible fixed asset is a physical asset, i.e. One that has real solid existence, e.g. Plant & Machinery.

An intangible fixed asset is an asset which does not have a physical existence, e.g. Goodwill.

An investment might also be a fixed asset, investment purchased with a view to holding them for more than a year are classified as fixed assets.

Current Assets : Current assets are either items owned by the business with the intention of their resale or cash including cash at bank deposited by the business. These assets are "Current" in the sense that they are continuously flowing.

Other current Assets are :-

Short term investment. This includes short term trade investment.

Prepayments :
These are amounts which are already paid by the business for benefits which have not yet been consumed.

Trade Debtors :
These are debtors to the business for supply of goods to them.

Liabilities :
These are debts of the business that must be paid within one year. They are –

   i) Loans payable within a year.
   ii) Bank Overdraft.
   iii) Trade creditors for supply of goods.
   iv) Bills of exchange.
   v) Outstanding payments.
   vi) Interest on loans due and accrued but not paid.
Financial Accounting Fundamentals

Long term liabilities:
Long term liability is a debt which is not payable within one year.

Owners equity or capital.
The amount owing to the proprietors as capital is shown separately.

Illustration 13:
The following Trial Balances as on 31st May, 2000 and 31st May, 2001 are furnished to you by Ashar and Sons:

<table>
<thead>
<tr>
<th></th>
<th>31st May, 2001</th>
<th></th>
<th>31st May, 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Dr. Rs.</td>
<td>Cr. Rs.</td>
<td>Dr. Rs.</td>
</tr>
<tr>
<td>Fixed capitals:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ashar</td>
<td>—</td>
<td>6,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Bismilla</td>
<td>—</td>
<td>4,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Cawasji</td>
<td>—</td>
<td>2,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Current accounts:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ashar</td>
<td>—</td>
<td>10,000</td>
<td>5,000</td>
</tr>
<tr>
<td>Bismilla</td>
<td>—</td>
<td>60,000</td>
<td>—</td>
</tr>
<tr>
<td>Cawasji</td>
<td>10,000</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Customers dues</td>
<td>11,00,000</td>
<td>—</td>
<td>9,00,000</td>
</tr>
<tr>
<td>Suppliers</td>
<td>—</td>
<td>80,000</td>
<td>—</td>
</tr>
<tr>
<td>Fixed assets (cost)</td>
<td>3,00,000</td>
<td>—</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Provision for depreciation</td>
<td>—</td>
<td>1,30,000</td>
<td>—</td>
</tr>
<tr>
<td>Stock</td>
<td>65,000</td>
<td>—</td>
<td>1,05,000</td>
</tr>
<tr>
<td>Cash</td>
<td>10,000</td>
<td>—</td>
<td>10,000</td>
</tr>
<tr>
<td>Bank</td>
<td>20,000</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>20,000</td>
<td>—</td>
<td>15,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>—</td>
<td>45,000</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>15,25,000</td>
<td>15,25,000</td>
<td>12,35,000</td>
</tr>
</tbody>
</table>

You are asked to interpret the above trial balances.

Solution:

Working Note.
For interpretation of the Trial Balances it should be redrafted in the following format to find out the changes occurred in the two financial years i.e. 1999-2000 and 2000-2001.
Final Accounts

<table>
<thead>
<tr>
<th>Items</th>
<th>As at 31.5.2001</th>
<th>As at 31.5.2000</th>
<th>Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liabilities:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital A/c — Ashar</td>
<td>6,00,000</td>
<td>7,00,000</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Capital A/c — Bismilla</td>
<td>4,00,000</td>
<td>2,00,000</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Capital A/c — Cawasji</td>
<td>2,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current A/c — Ashar</td>
<td>10,000</td>
<td>5,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Current A/c — Bismilla</td>
<td>60,000</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Suppliers</td>
<td>80,000</td>
<td>1,50,000</td>
<td>70,000</td>
</tr>
<tr>
<td>Outstanding Expenses</td>
<td>45,000</td>
<td>25,000</td>
<td>20,000</td>
</tr>
<tr>
<td>Provision for Depreciation</td>
<td>1,30,000</td>
<td>90,000</td>
<td>40,000</td>
</tr>
<tr>
<td></td>
<td>15,25,000</td>
<td>12,10,000</td>
<td>1,70,000</td>
</tr>
<tr>
<td>Assets:</td>
<td></td>
<td></td>
<td>4,95,000</td>
</tr>
<tr>
<td>Fixed Assets</td>
<td>3,00,000</td>
<td>2,00,000</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Customers</td>
<td>11,00,000</td>
<td>9,00,000</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Current A/c — Cawasji</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stock</td>
<td>65,000</td>
<td>1,05,000</td>
<td>40,000</td>
</tr>
<tr>
<td>Cash</td>
<td>10,000</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Bank</td>
<td>20,000</td>
<td>(30,000)</td>
<td>50,000</td>
</tr>
<tr>
<td>Prepaid Expenses</td>
<td>20,000</td>
<td>15,000</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>15,25,000</td>
<td>12,00,000</td>
<td>3,65,000</td>
</tr>
</tbody>
</table>

Interpretation of Trial Balance:

1. The trial balances of both the years are prepared after preparation of Profit and Loss Account. The net profits or losses, if any, are adjusted to the current account of the partners.

2. Cawasji was admitted as partner during the financial year 2000-2001. The treatment of goodwill, if any, had not been shown in the accounts. However, it appears from the movement of fixed capital accounts that Ashar had sacrificed his share of profit in the business which was acquired by both Bismilla and Cawasji which had the effect of bringing in cash by them and withdrawal of cash by Ashar. The capital accounts being in the nature of fixed capital, normally no profit and/or drawings have been transacted through these accounts. However, in the absence of any information as to goodwill of the firm and profit sharing ratios of the partners, it is not possible to state about the movement of funds.

3. The changes in the current accounts of the partners is due to transactions relating to sharing of profits according to profit sharing ratios and credits on account of interest in capital in the one hand and correspondingly the drawings and debit of interest on drawings (if any) on the other hand. However, the debit of Rs. 10,000 in the new partner Cawasji may be on account of adjustment of goodwill which might have been debited to maintain a current account balance of Rs. 2,00,000 as may be agreed by the partners. In absence of relevant information the exact position could not be ascertained.
4. The net current assets of the firm and changes therein during the financial year is stated below:

<table>
<thead>
<tr>
<th></th>
<th>As at 31.5.2001</th>
<th>As at 31.5.2000</th>
<th>Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Increase</td>
</tr>
<tr>
<td>Stock</td>
<td>65,000</td>
<td>1,05,000</td>
<td>—</td>
</tr>
<tr>
<td>Customers</td>
<td>11,00,000</td>
<td>9,00,000</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Cash</td>
<td>10,000</td>
<td>10,000</td>
<td>—</td>
</tr>
<tr>
<td>Bank</td>
<td>20,000</td>
<td>—</td>
<td>20,000</td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>20,000</td>
<td>15,000</td>
<td>5,000</td>
</tr>
<tr>
<td>Total current assets (A)</td>
<td>12,15,000</td>
<td>10,30,000</td>
<td>2,25,000</td>
</tr>
</tbody>
</table>

Less:

|                      |                 |                 | Decrease      |
| Suppliers            | 80,000          | 1,50,000        | —             |
| Expenses             | 45,000          | 25,000          | 20,000        |
| Bank overdraft       | —               | 30,000          | —             |
| Total current liabilities (B) | 1,25,000 | 2,05,000 | 20,000 |

Net current assets (A) - (B) | 10,90,000 | 8,25,000 | 2,65,000 |

The above statement reveals:

(a) There is overall increase in the net current assets by Rs. 2,65,000.

(b) Current assets to current liabilities ratios

- For the year 2000-2001 — Rs. 9.72 to Re. 1
- For the year 1999-2000 — Rs. 5.02 to Re. 1

which shows an improvement of Rs. 4.70 to Re. 1

The changes in the ratios are due to:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase in debtors A/c</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>Increase in bank balance</td>
<td></td>
<td>20,000</td>
</tr>
<tr>
<td>Decrease in suppliers A/c</td>
<td>70,000</td>
<td></td>
</tr>
<tr>
<td>Decrease in bank A/c</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Decrease in Prepaid Expenses</td>
<td>5,000</td>
<td>3,25,000</td>
</tr>
</tbody>
</table>

Less:

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Decrease in stock</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Increase in liability for expenses</td>
<td>20,000</td>
<td>60,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,65,000</td>
</tr>
</tbody>
</table>
Final Accounts

Increases in bank balances, repayment of bank overdraft and reduction in stock are signs of good and positive sound position of firm’s/company’s trading activities. However, there is no change in the cash balance. It is assumed that cash balance represents petty cash.

In the absence of sales and purchase figures, the changes in debtors by Rs. 2,00,000 and reduction in creditors by Rs. 70,000 could not be properly explained.

Prepaid expenses have gone by up by Rs. 5,000 which may be considered as normal.

Outstanding expenses have gone up by Rs. 20,000. However, the firm possesses a cash and bank balances of Rs. 30,000 which is sufficient to repay them on due dates of payment.

5. Cost of fixed assets has gone up by Rs. 1,00,000; similarly accumulated depreciation by Rs. 40,000. No information has been provided for any sale or discard of any fixed assets. In the absence of such information exact outflow of fund in this regard could not be ascertained.

Illustration 14:

From the following transactions pass journal entries and show ledger accounts in the Books of S. Banerjee and prepare a Trial Balance.

Started business with cash Rs. 1,50,000, Goods worth Rs. 80,000, Office Equipment Rs. 70,000 and his private car worth Rs. 1,20,000 which will henceforth be used solely for business purpose.

Bought furniture worth Rs. 40,000 of which those worth Rs. 10,000 are for office use and the balance for stock. Purchased 3 motor cars worth Rs. 1,50,000 each from Ganguly & Co. for stock.

Purchased 2 motor cars worth Rs. 80,000 each from Ganguly & Co. for business use.

Purchased for cash 1 motor car worth Rs. 70,000 for private use.

Returned motor cars worth Rs. 1,50,000 from stock and that worth Rs. 80,000 for business use to Ganguly & Co.

Sold office equipment for Rs. 40,000

Sold one of the motor cars for stock for Rs. 2,00,000; paid landlord Rs. 12,000 for rent. One-third of the premises is occupied by the proprietor for his own residence.

Sold the third car for Rs. 3,50,000.
**Financial Accounting Fundamentals**

**Solution:**

**In the books of Mr. S. Banerjee**

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) Cash A/c</td>
<td>150000</td>
<td></td>
</tr>
<tr>
<td>Stock A/c</td>
<td>80000</td>
<td></td>
</tr>
<tr>
<td>Office Equipment A/c</td>
<td>70000</td>
<td></td>
</tr>
<tr>
<td>Motor car Q/c</td>
<td>120000</td>
<td>420000</td>
</tr>
<tr>
<td>To capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>(Sundry Assets introduced as Capital to start business)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>b) Furniture A/c</td>
<td>1000</td>
<td></td>
</tr>
<tr>
<td>Purchase A/c</td>
<td>3000</td>
<td>40000</td>
</tr>
<tr>
<td>To cash A/</td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>(Purchase of furniture worth Rs. 40000 out of which Rs.10000 for office decoration and Rs. 30000 for stock)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>c) Purchase A/c</td>
<td>450000</td>
<td>450000</td>
</tr>
<tr>
<td>To Ganguli &amp; Co.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>(Purchased 3 motor cars for stock purpose)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>d) Motor Car A/c</td>
<td>160000</td>
<td>160000</td>
</tr>
<tr>
<td>To Ganguli &amp; Co.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>(Purchased 2 motor cars for office use)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>e) Drawings A/c</td>
<td>70000</td>
<td></td>
</tr>
<tr>
<td>To Cash A/c</td>
<td></td>
<td>70000</td>
</tr>
<tr>
<td><em>(Bought 1 office car for private use)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>f) Ganguli &amp; Co.</td>
<td>230000</td>
<td></td>
</tr>
<tr>
<td>To Return outward A/c</td>
<td></td>
<td>150000</td>
</tr>
<tr>
<td>To Motor car A/c</td>
<td></td>
<td>80000</td>
</tr>
<tr>
<td><em>(Motor car worth Rs. 150000 from stock and Rs.80000 from business use returned to Ganguli &amp; Co.)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>g) Cash A/c</td>
<td>40000</td>
<td>40000</td>
</tr>
<tr>
<td>To Office Equipment A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>(Office equipment worth Rs. 40000 sold)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>h) Cash A/c</td>
<td>200000</td>
<td>200000</td>
</tr>
<tr>
<td>To Sales A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>(Being one motor car from stock sold)</em></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Final Accounts

**i)** Rent A/c  
Dr. 8000  
Drawings A/c  
Dr. 4000  
To Cash A/c 12000  
(Rent paid to landlord, 1/3 of the premises occupied by the proprietor for personal residence)

**j)** Cash A/c  
Dr. 350000  
To Sales A/c 350000  
(Sold the third car for cash)

<table>
<thead>
<tr>
<th>Dr. Cash Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td>Rs.</td>
</tr>
<tr>
<td>To Capital</td>
<td>1,50,000</td>
</tr>
<tr>
<td>To Office Equipment</td>
<td>40,000</td>
</tr>
<tr>
<td>To Sales</td>
<td>2,00,000</td>
</tr>
<tr>
<td>To Sales</td>
<td>3,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,40,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr. Stock Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td>Rs.</td>
</tr>
<tr>
<td>To Capital</td>
<td>80000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr. Office Equipment A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td>Rs.</td>
</tr>
<tr>
<td>To Capital</td>
<td>70000</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>70000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr. Motor Car A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td>Rs.</td>
</tr>
<tr>
<td>To Capital</td>
<td>120000</td>
</tr>
<tr>
<td>&quot; Ganguli &amp; Co.&quot;</td>
<td>160000</td>
</tr>
<tr>
<td></td>
<td>280000</td>
</tr>
</tbody>
</table>
### Financial Accounting Fundamentals

#### Dr. Furniture A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash</td>
<td>10000</td>
<td>By Balance c/d</td>
<td>10000</td>
</tr>
</tbody>
</table>

#### Dr. Purchase A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash</td>
<td>30000</td>
<td>By Balance c/d</td>
<td>480000</td>
</tr>
<tr>
<td>To Ganguli &amp; Co.</td>
<td>450000</td>
<td>480000</td>
<td></td>
</tr>
</tbody>
</table>

#### Dr. Return Outward A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance c/d</td>
<td>150000</td>
<td>By Ganguli &amp; Co.</td>
<td>150000</td>
</tr>
</tbody>
</table>

#### Dr. Ganguli & Co. A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Return Outward</td>
<td>150000</td>
<td>By Purchase</td>
<td>450000</td>
</tr>
<tr>
<td>To Motor Car</td>
<td>80000</td>
<td>By Motor Car</td>
<td>160000</td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>380000</td>
<td>610000</td>
<td></td>
</tr>
</tbody>
</table>

#### Dr. Drawings A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash</td>
<td>70000</td>
<td>By Balance c/d</td>
<td>74000</td>
</tr>
<tr>
<td>To Cash</td>
<td>4000</td>
<td>74000</td>
<td>74000</td>
</tr>
</tbody>
</table>

#### Dr. Sales A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance c/d</td>
<td>550000</td>
<td>By Cash</td>
<td>200000</td>
</tr>
<tr>
<td>550000</td>
<td></td>
<td>350000</td>
<td>550000</td>
</tr>
</tbody>
</table>
Final Accounts

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Rent A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>To Cash</td>
<td>8000</td>
<td>By Balance c/d</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Capital A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>420000</td>
<td>By Cash</td>
</tr>
<tr>
<td>To Stock</td>
<td>80000</td>
<td></td>
</tr>
<tr>
<td>To Office Equipment</td>
<td>70000</td>
<td>By Motor Car</td>
</tr>
<tr>
<td></td>
<td>420000</td>
<td></td>
</tr>
</tbody>
</table>

Trial Balance

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Rs.</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>Cash</td>
<td>618000</td>
</tr>
<tr>
<td>Stock</td>
<td>80000</td>
</tr>
<tr>
<td>Office Equipment</td>
<td>30000</td>
</tr>
<tr>
<td>Motor Car</td>
<td>200000</td>
</tr>
<tr>
<td>Furniture</td>
<td>10000</td>
</tr>
<tr>
<td>Purchase</td>
<td>480000</td>
</tr>
<tr>
<td>Ganguli &amp; Co.</td>
<td>380000</td>
</tr>
<tr>
<td>Drawings</td>
<td>74000</td>
</tr>
<tr>
<td>Return outward</td>
<td>150000</td>
</tr>
<tr>
<td>Sales</td>
<td>550000</td>
</tr>
<tr>
<td>Rent</td>
<td>8000</td>
</tr>
<tr>
<td>Capital</td>
<td>420000</td>
</tr>
<tr>
<td></td>
<td>1500000</td>
</tr>
</tbody>
</table>

2.5 DEPRECIATION

Depreciation is the diminution in the value of assets due to use, wear and tear and efflux of time. It is an estimated charge against profit for use of fixed assets. The provision for depreciation is to create funds for replacement of assets. It may either be written off against asset accounts or it may be Depreciation Provision Account keeping Asset Account at cost. There are various methods of depreciation, such as,—

1) **Straight-line method or Fixed Instalment method** - This is simple and most widely used method. An equal portion of the cost of the asset is allocated to each period of use.

2) **Diminishing/reducing value method**
Financial Accounting Fundamentals

3) Annuity method
4) Insurance Policy
5) Revaluation
6) Unit charging system.
   i) Production unit.
   ii) Time unit
7) Machine Hour Rate.
8) Sum of the digits method.

The entry for depreciation will be :-
Depreciation A/c Dr. 
To Respective Asset A/c

The most commonly methods of depreciation are –
1) Straight line method and
2) Reducing / Diminishing value method.

For depreciation, Students are advised to go thorough
i) International Accounting Standard - 4, and
ii) Indian Accounting Standard - 6 for a thorough knowledge on the subject.

Methods of Calculating Depreciation

There are a number of methods of calculating depreciation on the original cost or on the
replacement cost of the assets. Each method adopts one or more of the following principles —
(a) depreciation is a function of time;
(b) depreciation is a function of use;
(c) depreciation is a function of time and use;
(d) depreciation is a function of time and maintenance; and
(e) depreciation is a function of time and interest.

Whatever method is applied in the accounts, it must be suitable to the circumstances prevailing
in the organisation. The different methods are discussed as follows :

1) **Straight line method** : This is the method of providing for depreciation by means
   of periodic charges over the assumed or anticipated life of the asset.

   *Example :*
   If, C = Cost of the asset depreciated = Rs. 10,000.
   R = Residual value of the asset = Rs. 500.
   n = Life of the asset = 4 years.
Final Accounts

Then,

\[ D = \text{Proportion of cost of asset depreciated under this method} \]

\[
= \frac{C - R}{n \times C} = \frac{10,000 - 500}{4 \times 10,000} = 0.2375 \text{ or } 23.75\%
\]

So, amount of depreciation is 23.75% of Rs. 10,000 = Rs. 2,375 each year.

\textbf{Proof :}

<table>
<thead>
<tr>
<th>Year</th>
<th>Cost and balance b/d Rs.</th>
<th>Depreciation Rs.</th>
<th>Balance c/f Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>10,000</td>
<td>2,375</td>
<td>7,625</td>
</tr>
<tr>
<td>2</td>
<td>7,625</td>
<td>2,375</td>
<td>5,250</td>
</tr>
<tr>
<td>3</td>
<td>5,250</td>
<td>2,375</td>
<td>2,875</td>
</tr>
<tr>
<td>4</td>
<td>2,875</td>
<td>2,375</td>
<td>500</td>
</tr>
</tbody>
</table>

(Depreciation has been calculated to the nearest Rupee.)

Thus, by using this method an equal amount of depreciation is charged during each period, irrespective of its use. This method is simple and is usefully applied to all types of fixed assets, particularly in connection with patents, leasehold and similar assets having definite life. Its use in cost accounts affords a better comparative costs for its uniform charge. However, the total cost of depreciation and repair and maintenance costs of assets increase progressively.

(2) \textbf{Reducing balance method :} This is the method of providing for depreciation by means of periodic charges calculated as a constant proportion of the balance of the asset after deducting the amounts previously provided. This is also called written down value method.

\textbf{Example :}

Assuming the same data as before,

\[ D = \text{Proportion of reducing balance of cost of asset depreciated in each period.} \]

\[
= 1 - \sqrt{\frac{R}{C}} = 1 - \sqrt{\frac{500}{10,000}}
\]

\[
= 1 - 0.4729
\]

\[
= 0.5271 \text{ or } 52.71\%
\]

(if the residual value is nil, assume R = 1)
Financial Accounting Fundamentals

Proof :

<table>
<thead>
<tr>
<th>Year</th>
<th>Cost and balance b/d Rs.</th>
<th>Depreciation @ 52.71% Rs.</th>
<th>Balance c/f Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>10,000</td>
<td>5,271</td>
<td>4,729</td>
</tr>
<tr>
<td>2</td>
<td>4,729</td>
<td>2,493</td>
<td>2,236</td>
</tr>
<tr>
<td>3</td>
<td>2,236</td>
<td>1,179</td>
<td>1,057</td>
</tr>
<tr>
<td>4</td>
<td>1,057</td>
<td>557</td>
<td>500</td>
</tr>
</tbody>
</table>

Because of its simplicity, this method is popular and is extensively used for taxation purposes. It is observed that a heavier depreciation is borne in the earlier years when repairs are lighter, and that the increasing repair cost is counterbalanced, in later years, by the reduced annual charge for depreciation. The use of this method for costing purposes is justifiable only if its effect is to provide a uniform charge for the services of the asset throughout its life; otherwise, the cost of production in subsequent years appears to decrease, although they are produced under identical conditions.

(3) Production unit method: This is the method of providing for depreciation by means of a fixed rate per unit of production calculated by dividing the value of the asset by the estimated number of units to be produced during its life.

Example:

Assuming C and R to have the same value as before and \( N_U = \) Estimated units to be produced during its life = 38,000 units.

Then, \( D = \frac{C-R}{N_U} = \frac{10,000-500}{38,000} = \frac{9500}{38000} \)

= Re. 0.25 per unit.

Thus, if 4,000 units are produced in a certain period, Rs. 1,000 will be charged as depreciation.

This method gives emphasis on usage and ignores time factor. The depreciation charge is high in periods of abnormal activity and low when machines are idle. This method is suitable for wasting assets such as mines and quarries. If estimated production during the life can be determined, this method satisfies the costing requirement that the cost of an asset should be evenly spread over the work done by it. However, the main disadvantage of this method is that a separate record of output of each of the assets has to be maintained and this method cannot be applied were output are of different types.
Final Accounts

(4) **Production hour method**: This is the method of providing for depreciation by means of a fixed rate per hour of production calculated by dividing the value of the asset by the estimated number of hours of its life.

*Example:*

Assuming C and R to have the same value, and

\[ N_H = \text{Estimated number of working hours of its life} = 19,000 \text{ hrs.} \]

Then, \( D = \text{Depreciation per hour} \)

\[
D = \frac{C-R}{N_H} = \frac{10,000-500}{19,000} = \text{Re. 0.50 per hour}
\]

Thus, for a work of 1,000 hours in a certain period, depreciation charge will be:

\[ \text{Rs. } 1,000 \times \text{Re. 0.50} = \text{Rs. } 500.\]

This method is usefully applied in cases of costly automatic machines having a limited but definite working life. This method is similar to production unit method. However, under this method, there is no need for all the units to be produced to be one type or even similar to one another as the charge is based upon the time involved in their production, and not on their number.

(5) **Annuity method**: This is the method of providing for depreciation by means of periodic charges, each of which is a constant proportion of the aggregate of the cost of the asset depreciated and interest at a given rate per period on the written down value of the asset at the beginning of each period.

*Example:*

If \( C = \text{Rs. } 10,000; \ n = 4 \text{ years}; \ r = \text{rate of interest } 4\% \text{ per annum}; \)

\( a_n = \text{present value of an annuity certain of } 1 \text{ per year.} \)

\[
a_n = \frac{1}{r} \left(1 - \frac{1}{(1+r)^n}\right)
\]

Then, \( D = \text{amount of periodic depreciation charge under this method} \)

\[
D = \frac{C}{a_n} = \frac{C \times r}{1-\frac{1}{(1+r)^n}} = \frac{10,000 \times 0.04}{1-\left(\frac{1}{1.04}\right)^4} = \frac{400}{1-1.04^{-4}} = \frac{400}{1-169859} = \text{Rs. 2,755}
\]
### Financial Accounting Fundamentals

**Proof:**

<table>
<thead>
<tr>
<th>Year</th>
<th>Cost and balance b/f (nearest rupee)</th>
<th>Interest @ 4% (nearest rupee)</th>
<th>Total provision</th>
<th>Annual provision</th>
<th>Balance c/f</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>10,000</td>
<td>400</td>
<td>10,400</td>
<td>2,755</td>
<td>7,645</td>
</tr>
<tr>
<td>2</td>
<td>7,645</td>
<td>306</td>
<td>7,951</td>
<td>2,755</td>
<td>5,196</td>
</tr>
<tr>
<td>3</td>
<td>5,196</td>
<td>208</td>
<td>5,404</td>
<td>2,755</td>
<td>2,649</td>
</tr>
<tr>
<td>4</td>
<td>2,649</td>
<td>106</td>
<td>2,755</td>
<td>2,755</td>
<td>Nil</td>
</tr>
</tbody>
</table>

The amount of depreciation is heavy in this method and is intended to cover the cost of opportunity lost by not investing the capital elsewhere.

This method is based on the concept that money invested in an asset earns interest. This method is suitably used for the redemption of leases over a fairly long period. It is a scientific method where investment funds outside a business is not required.

(6) **Revaluation method:** This is the method of providing for depreciation by means of periodic charges each of which is equivalent to the difference between the values assigned to the asset at the beginning and the end of the period.

*Example:*

If, \( C = \text{Cost of the asset} = Rs. 10,000; \)
\[ V = \text{Value of asset at the end of one year} = Rs. 7,000 \]

Then, \( D = \text{Amount of depreciation under this method} = C - V = 10,000 - 7,000 = Rs. 3,000. \)

This method is commonly used for depreciation of loose tools, livestock, patents, patterns, etc., which depreciate rapidly. This method is also used for use of assets in contracts.

(7) **Sum of the digits method:** This is the method of providing for depreciation by means of differing periodic rates which is computed by taking a reduced proportion of the sum of an arithmetical progression in respect of the years of life of the asset, multiplied by the cost, less residual value, of the asset.

*Example:*

If, \( C = \text{cost of asset} = Rs. 10,000; \quad R = \text{residual value} = Rs. 400; \quad n = 4\text{yrs.} \)

Then, \( S = \text{sum of years} = 1 + 2 + 3 + 4 = 10 \)
**Final Accounts**

Then, depreciation charge:

<table>
<thead>
<tr>
<th>Year</th>
<th>Percentage</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>4/10</td>
<td>3,840</td>
</tr>
<tr>
<td>2</td>
<td>3/10</td>
<td>2,880</td>
</tr>
<tr>
<td>3</td>
<td>2/10</td>
<td>1,920</td>
</tr>
<tr>
<td>4</td>
<td>1/10</td>
<td>960</td>
</tr>
</tbody>
</table>

This method is suitable for depreciation of motor vehicle and other assets which drop in value immediately after purchase. Thus the advantage of this method is that it takes into account of such drop in value of new asset and makes the decision to sell and repurchase before the estimated time an easier one.

The following should be noted for depreciation of the following types of fixed assets:

(a) **Goodwill**: No depreciation arises unless the firm’s profits are decreasing. Prudent firms try to write off goodwill over a number of years.

(b) **Freehold Land**: In this case also no depreciation arises. Amounts written off should be shown separately.

(c) **Loose tools, Jigs and Patterns**: Depreciation should be calculated on revaluation method.

(d) **Patents, Trade Marks, etc.**: There is a maximum legal life of such assets but the commercial life may be shorter. The asset should be depreciated by straight line method so that it is written off within the legal or commercial life whichever is shorter.

(e) **Mines, Oil wells, Quarries, etc.**: Depreciation should be charged on depletion method.

**Illustration 15**:

A company purchased a machine for Rs. 20,000 and paid cost of installation Rs. 1,000. At the date of purchase, the life of the machine was estimated at 15 years and hence it was decided to create a depreciation fund to be invested in Government Securities to provide for replacement of the machine.

Before expiration of the estimated life it was decided to dismantle the machine and replace it with a modern one. The cost of dismantling was Rs. 200 and the cost of purchase and installation of new machine was Rs. 23,000. Parts of the old machine estimated to be worth Rs. 500, were retained and the remainder sold as scrap for Rs. 750.

At the date of dismantling the old machine, the depreciation fund stood in the books at Rs. 16,500 and was represented by Government Securities costing the same amount. These securities were sold for Rs. 15,600.

You are required to write up the ledger accounts concerned.
Financial Accounting Fundamentals

Solution:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Machinery A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To</td>
<td>Cash A/c</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cost of Machine</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td>Installation</td>
<td>1,000</td>
</tr>
<tr>
<td>To</td>
<td>Cash A/c</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Cost of new Machine</td>
<td>23,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Depreciation Fund A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To</td>
<td>Cash A/c – Cost of dismantling Depreciation Fund</td>
<td>200</td>
</tr>
<tr>
<td></td>
<td>Investment A/c – transferred</td>
<td>900</td>
</tr>
<tr>
<td></td>
<td>Machinery A/c (Balancing figure)</td>
<td>15,400</td>
</tr>
<tr>
<td></td>
<td>16,500</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Depreciation Fund A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To</td>
<td>Balance b/d</td>
<td>16,500</td>
</tr>
<tr>
<td></td>
<td>— Sale of securities</td>
<td>15,600</td>
</tr>
<tr>
<td></td>
<td>— Depreciation Fund A/c</td>
<td>900</td>
</tr>
<tr>
<td></td>
<td>— Loss tfd..</td>
<td></td>
</tr>
<tr>
<td></td>
<td>16,500</td>
<td>16,500</td>
</tr>
</tbody>
</table>

Working to find out loss on dismantling the old machine.

Cost of old machine Rs. 21,000

Less: Parts retained from Old machine 500
Sale of Scrap 750 1,250

Less: Amount available from the balance of Depreciation Fund A/c 15,400
Loss 4,350
**Final Accounts**

**Illustration 16:**

A firm is willing to change the system of providing for depreciation from Diminishing Balance Method to Straight Line Method with retrospective effect from 1st April, 1995. On 1st April, 1997, Machinery Account in the Ledger had a debit balance of Rs. 5,67,000. The rate of depreciations would, however, remain unchanged. Necessary adjustments for depreciations due to change in method should be made in the year 1997-98. Rate of Depreciation 10% p.a.

You are further informed that new machinery were purchased on 1st October, 1997 at a cost of Rs. 60,000.

Show the Machinery Account from 1995-96 to 1997-98.

**Solution:**

Cost of Machinery on 1st April, 1995

\[
Rs. \frac{5,67,000 \times 100}{90} \times \frac{100}{90} = Rs. 7,00,000.
\]

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Machinery Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>1.4.95–31.3.96</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Balance</td>
<td>7,00,000</td>
<td>By Depreciation (on Rs. 7,00,000 @ 10%) 70,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Balance c/d 63,000</td>
</tr>
<tr>
<td></td>
<td>7,00,000</td>
<td></td>
</tr>
<tr>
<td>1.4.96–31.3.97</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Balance b/d.</td>
<td>63,000</td>
<td>By Depreciation (on Rs. 63,000 @ 10%) 63,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d 5,67,000</td>
</tr>
<tr>
<td></td>
<td>63,000</td>
<td></td>
</tr>
<tr>
<td>1.4.97–31.3.98</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Balance b/d.</td>
<td>5,67,000</td>
<td>By Depreciation (due to change in Method) 7,000</td>
</tr>
<tr>
<td>1.10.97 To Bank (Addition)</td>
<td>60,000</td>
<td>By Depreciation:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(i) On Rs. 7,00,000 @ 10% p.a. 70,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(ii) On 60,000 for 6 months @ 10% p.a. 3,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d 5,47,000</td>
</tr>
<tr>
<td></td>
<td>6,27,000</td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Depreciation provided on reducing system:

<table>
<thead>
<tr>
<th>Year</th>
<th>Depreciation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995-96</td>
<td>Rs. 70,000</td>
</tr>
<tr>
<td>1996-97</td>
<td>Rs. 63,000</td>
</tr>
<tr>
<td></td>
<td><strong>Rs. 1,33,000</strong></td>
</tr>
</tbody>
</table>

Depreciation to be provided on Straight Line Method:

<table>
<thead>
<tr>
<th>Year</th>
<th>Depreciation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995-96</td>
<td>Rs. 70,000</td>
</tr>
<tr>
<td>1996-97</td>
<td>Rs. 70,000</td>
</tr>
<tr>
<td></td>
<td><strong>Rs. 1,40,000</strong></td>
</tr>
</tbody>
</table>

Deprn. short to be provided for
(Rs. 1,40,000 – Rs. 1,33,000) Rs. **7,000**

Illustration 17:

Depreciation has been charged for the years 1998 to 2001 at 10% on reducing balance method on opening balance of each item of plant and machinery in use. The balance of Plant and Machinery Account on 31st December, 2001 was Rs. 54,000. There were no sales during these years but purchases were Rs. 16,800 on September, 1998 and Rs. 11,400 in December, 2000.

The management decided that depreciation should be charged at 20% on the same method but calculated on the closing balance of each year with retrospective effect from 1998.

You are required to pass Journal Entry for giving effect to the revised basis at the end of 2001, and prepare Plant and Machinery Account and Revised Plant and Machinery Account for all the years.

Solution:

The balance of Plant and Machinery Account as on January, 1998 is not given. This balance is to be ascertained by working reverse way from 2001.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Plant and Machinery Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Date</strong></td>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>1998</td>
<td>1998</td>
<td></td>
</tr>
<tr>
<td>1-Jan</td>
<td>To Balance b/d</td>
<td>48,000</td>
</tr>
<tr>
<td></td>
<td>To Bank A/c</td>
<td>16,800</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Final Accounts

1999

1-Jan To Balance b/d 60,000 31-Dec By Depreciation (1/9 of Rs. 54,000) 6,000
   By Balance c/d 54,000

2000

1-Jan To Balance b/d 54,000 31-Dec By Depreciation (1/9 of Rs. 60,000)
   – Rs. 11,400) 5,400
   By Balance c/d 60,000

2001

1-Jan To Balance b/d 60,000 31-Dec By Depreciation (1/9 of Rs. 54,000) 6,000
   By Balance c/d 54,000

When deprn. is calculated on the revised basis, the Plant and Machinery Account will be as under:

<table>
<thead>
<tr>
<th>Date</th>
<th>Dr.</th>
<th>Revised Plant and Machinery</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Date</td>
<td>Rs.</td>
</tr>
<tr>
<td>1998</td>
<td>1-Jan To Balance b/d</td>
<td>48,000</td>
<td>12,960</td>
</tr>
<tr>
<td>1-Sep</td>
<td>To Bank A/c</td>
<td>16,800</td>
<td>51,840</td>
</tr>
<tr>
<td></td>
<td></td>
<td>64,800</td>
<td>64,800</td>
</tr>
<tr>
<td>1999</td>
<td>1-Jan To Balance b/d</td>
<td>51,840</td>
<td>10,368</td>
</tr>
<tr>
<td></td>
<td></td>
<td>31-Dec</td>
<td>41,472</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Deprn. (20% on 51,840)</td>
<td>41,472</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>51,840</td>
</tr>
<tr>
<td>2000</td>
<td>1-Jan To Balance b/d</td>
<td>41,472</td>
<td>10,574</td>
</tr>
<tr>
<td>Dec</td>
<td>To Bank A/c</td>
<td>11,400</td>
<td>42,298</td>
</tr>
<tr>
<td></td>
<td></td>
<td>52,872</td>
<td>52,872</td>
</tr>
<tr>
<td>2001</td>
<td>1-Jan To Balance b/d</td>
<td>42,298</td>
<td>8,460</td>
</tr>
<tr>
<td></td>
<td></td>
<td>31-Dec</td>
<td>33,838</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Deprn. (20% on 42,298)</td>
<td>8,460</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>33,838</td>
</tr>
</tbody>
</table>

The resultant impact on P & L A/c of Rs. 20,162 to be disclosed in notes on Accounts.
**Financial Accounting Fundamentals**

<table>
<thead>
<tr>
<th>Date</th>
<th>Depn. @ 10%</th>
<th>Residual value</th>
<th>Deprn. @ 20%</th>
<th>Residual value</th>
</tr>
</thead>
<tbody>
<tr>
<td>31-Dec-01</td>
<td>6,000</td>
<td>54,000</td>
<td>8,460</td>
<td>33,838</td>
</tr>
<tr>
<td>31-Dec-00</td>
<td>5,400</td>
<td>60,000</td>
<td>10,574</td>
<td>42,298</td>
</tr>
<tr>
<td>31-Dec-99</td>
<td>6,000</td>
<td>54,000</td>
<td>10,368</td>
<td>41,472</td>
</tr>
<tr>
<td>31-Dec-98</td>
<td>4,800</td>
<td>60,000</td>
<td>12,960</td>
<td>51,840</td>
</tr>
<tr>
<td>31-Sep-98</td>
<td></td>
<td>64,800</td>
<td></td>
<td></td>
</tr>
<tr>
<td>01-Jan-98</td>
<td></td>
<td>48,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Difference</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>22,200</td>
</tr>
<tr>
<td>Difference</td>
<td>Rs.</td>
</tr>
<tr>
<td></td>
<td>20,162</td>
</tr>
</tbody>
</table>

**Journal Entry**

31-Dec-01 Depreciation A/c Dr. 2,460

Prior period Adj. A/c Dr. 17,702

(Deprn. for previous years)

To Plant & Machinery A/c 20,162

(Being arrear provision of depreciation chargeable at the revised rate of 20% and charged @ 10% for the years 1998 to 2000 and (Rs.33,902 – Rs.16,200) for the year 2001 (Rs. 8,460 – Rs. 6,000) already charged)

**Illustration 18 :**

(a) What are the different methods of providing depreciation? Is it necessary to provide depreciation? If yes, then what are the reasons?

(b) XYZ Limited purchased on 1st January, 1990 second hand plant for Rs.90,000 and immediately spent Rs.60,000 in overhauling it. On 1st July 1990 additional machinery at a cost of Rs.75,000 was purchased. On 1st July 1992 the plant purchased on 1st January 1990 became obsolete and was sold for Rs.30,000. On that date new machinery was purchased at a cost of Rs.1,80,000. Depreciation was provided annually on 31st December at 10% per annum on the original cost of asset. In 1993 however the company changed this method for depreciation and adopted the method of writing off 15% on the diminishing value. Show the Plant & Machinery Account as it would appear in the books of the company for the year 1990 to 1995.
Solution (a):

There are various methods of providing depreciation, these are —

i) Straight Line Method or Fixed Installment Method.
ii) Diminishing/Reducing value Method.
iii) Annuity Method.
iv) Insurance Policy Method.
v) Revaluation Method.
vi) Unit Charging System Method.
vii) Machine Hour Rate Method.

Yes, it is necessary to provide depreciation on fixed assets the lives of which are extinguished gradually owing to wear and tear, efflux of time, etc.

The capital expenditure incurred on acquisition of fixed asset is not charged as such in the revenue account in the concern in any year. Since the concern is utilising the asset for its business purpose, the revenue account for a year should share reasonably chargeable proportionate cost thereof. Depreciation is that reasonable charge on the profit and it is not appropriation of the profit. The Companies Act also stipulates that depreciation should be provided. If depreciation is not provided by a concern the true and fair picture of the working results will be vitiated and the Auditor will have to make a comment on that in his report.

Solution (b):

Books of XYZ Ltd.

Plant & Machinery Account

<table>
<thead>
<tr>
<th>Year</th>
<th>Particulars</th>
<th>Amount (1)</th>
<th>Amount (2)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>Jan. 1 To Bank A/c</td>
<td>90,000</td>
<td>Dec. 31 By Depreciation</td>
</tr>
<tr>
<td></td>
<td>&quot; Bank A/c- overhauling</td>
<td>60,000</td>
<td>&quot; Balance c/d</td>
</tr>
<tr>
<td></td>
<td>July 1 &quot; Bank A/c</td>
<td>75,000</td>
<td>2,25,000</td>
</tr>
<tr>
<td>1991</td>
<td>Jan. 1 To Balance c/d</td>
<td>2,06,250</td>
<td>Dec. 31 &quot; Balance c/d</td>
</tr>
<tr>
<td></td>
<td>July 1 &quot; Bank A/c</td>
<td>1,80,000</td>
<td>Dec. 31 &quot; Depreciation A/c</td>
</tr>
<tr>
<td></td>
<td>&quot; Profit &amp; Loss A/c</td>
<td>82,500</td>
<td>&quot; Balance c/d</td>
</tr>
<tr>
<td></td>
<td>3,63,750</td>
<td>3,63,750</td>
<td>3,63,750</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

1993

July 1 To Bank c/d 2,27,250 1993

Dec. 31 By Depreciation A/c 34,089

" Balance c/d 1,93,161 1993

2,27,250 2,27,250

1994

Jan. 1 To Balance b/d 1,93,161 1994

Dec. 31 By Depreciation A/c 28,974

" Balance c/d 1,64,187 1994

1,93,161 1,93,161

1995

Jan. 1 To Balance b/d 1,64,187 1995

Dec. 31 By Depreciation 24,628

" Balance c/d 1,39,559 1995

1,64,187 1,64,187

Working Notes: —

(1) Depreciation for the year 1990 (Rs. 18,750):

On cost of Plant:
90,000 @ 10% for full year 9,000
60,000 @ 10% for full year 6,000
75,000 @ 10% for 1/2 of year 3,750
18,750

(2) Depreciation for the year 1992:

On plant sold 1,50,000 @ 10% for 1/2 of year 7,500
On plant purchased 75,000 for full year 7,500
On plant purchased 1,80,000 for 1/2 year 9,000
24,000

(3) Loss on sale of plant (Rs. 82,500):

Cost of plant 90,000
Add: Overhauling 60,000 1,50,000
Less: Depreciation -
For the year 1990 15,000
For the year 1991 15,000
For the year 1992(1/2) 7,500 37,500 1,12,500
Less: Amount realised on Sale 30,000 82,500

NOTE: Regarding the change in the method of calculating depreciation reference may be made to AS - 6.

Illustration 19:

On 1.1.93 Machinery was purchased by X for Rs. 50,000. On 1.7.94 additions were made to the extent of Rs. 10,000. On 1.4.95 further additions of Rs. 6,400 were made on 30th June 1996. Machinery original value of which was Rs. 8,000 on 1.1.93 was sold for Rs. 6,000. Depreciation is charged at 10% p.a. on original cost.

Show the Machinery Account for the years 1993 to 1996 in the books of X who closes his books on 31st December every year.
### Final Accounts

**Solution:**

In the Books of X

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1.93</td>
<td>To Bank A/c-Purchase</td>
<td>50,000</td>
<td>31.12.93</td>
<td>By Depreciation A/c</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>50,000</td>
</tr>
<tr>
<td>1.1.94</td>
<td>To Balance b/d</td>
<td>45,000</td>
<td>31.12.94</td>
<td>By Depreciation A/c</td>
<td>5,500</td>
</tr>
<tr>
<td>1.7.94</td>
<td>To Bank-Purchase</td>
<td>10,000</td>
<td></td>
<td>By Balance c/d</td>
<td>49,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>55,000</td>
</tr>
<tr>
<td>1.1.95</td>
<td>To Balance b/d</td>
<td>49,500</td>
<td>31.12.95</td>
<td>By Depreciation A/c</td>
<td>6,480</td>
</tr>
<tr>
<td>1.4.95</td>
<td>To Bank-Purchase</td>
<td>6,400</td>
<td></td>
<td>By Balance c/d</td>
<td>49,420</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>55,900</td>
</tr>
<tr>
<td>1.1.96</td>
<td>To Balance b/d</td>
<td>49,420</td>
<td>30.6.96</td>
<td>By Bank A/c (Sale)</td>
<td>6,000</td>
</tr>
<tr>
<td>30.6.96</td>
<td>To P/L A/c-Profit on Sale</td>
<td>800</td>
<td>31.12.96</td>
<td>By Depreciation A/c</td>
<td>6,240</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>37,980</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>50,220</td>
</tr>
<tr>
<td>1.1.97</td>
<td>To Balance b/d</td>
<td>37,980</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Working Notes:**

1. Annual depreciation —
   a. For 1993
      Depreciation @ 10% on Rs. 50,000 = Rs. 5,000
   b. For 1994
      1st Machine @ 10% on Rs. 50,000 = Rs. 5,000
      2nd Machine @ 10% on Rs. 10,000 for 6 mths = Rs. 500
   c. For 1995
      1st Machine @ 10% on Rs. 50,000 = Rs. 5,000
      2nd Machine @ 10% on Rs. 10,000 = Rs. 1,000
      3rd Machine @ 10% on Rs. 6,400 for 9 months = Rs. 480
   d. 1st M/c @ 10% on (50,000 – 8,000) = Rs. 42,000 = Rs. 4,200
      2nd Machine @ 10% on Rs. 10,000 = Rs. 1,000
      3rd Machine @ 10% on 6,400 = Rs. 640
      On selling Machine at Rs. 8,000 for 6 mths.
      Rs. 8,000 × 10/100 × 1/2 = Rs. 400
      Total depreciation for 1994 = Rs. 8,500
      Total depreciation for 1995 = Rs. 10,720
      Total depreciation for 1996 = Rs. 6,240
      Total depreciation for 1997 = Rs. 6,240

STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION
2. Profit or loss on sale —

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Original cost of Machine as on 1.1.93</td>
<td>8,000</td>
</tr>
<tr>
<td>Less : Deprn. @ 10% for 3×1/2 years</td>
<td>2,800</td>
</tr>
<tr>
<td>Value as on Selling date i.e. 30.6.96</td>
<td>5,200</td>
</tr>
<tr>
<td>Sales Value</td>
<td>6,000</td>
</tr>
<tr>
<td>So Profit on Sale (6,000 – 5,200)</td>
<td>800</td>
</tr>
</tbody>
</table>

2.6 PROVISIONS AND RESERVES

Reserves or Reserve Funds mean amounts set aside out of profits (as ascertained by the Profit and Loss Account) or other surpluses which are not meant to cover any liability, contingency, commitment or depreciation in the value of assets.

Capital Reserves:

These reserves are not available for distribution among shareholders as dividend in the case of companies. They are built out of capital profits as against ordinary trading or revenue profits. In case of a limited company, the following are capital profits:

(a) Profits prior to incorporation;
(b) Premium on issue of shares or debentures;
(c) Profits on redemption of debentures;
(d) Amount utilised out of profits to redeem redeemable preference share;
(e) Profit on forfeiture of shares;
(f) Profits on sale of fixed assets over the original cost; and
(g) Profit on revaluation of fixed assets or liabilities.

Secret Reserves:

Secret Reserves are reserves which are not known to the members of the company. When secret reserves exit, the financial position of the company is better than what appears from the balance sheet. In some businesses, for example banks, the existence of secret reserves is necessary. Such businesses, depending upon public confidence, cannot afford to show a loss in any trading period. Secret reserves enable them to show a profit even when there is a loss. Secret reserves are created by the simple method of showing profit at a figure much lower than the actual.
Final Accounts

Illustration 20:

A company maintains its Reserve for discounts on Sundry Creditors @ 4%. On 1st April, 1995 Reserve for discounts on Sundry Creditors stood in the books for Rs. 9,500. On 31st March, 1996 and 31st March, 1997 Sundry Creditors (before adjustment of Discount received) amounted to Rs. 1,30,000 and Rs. 1,80,000 respectively.

Discounts received

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995-96</td>
<td>4,500</td>
</tr>
<tr>
<td>1996-97</td>
<td>12,000</td>
</tr>
</tbody>
</table>


Solution:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Reserve for Discount A/c on Sundry Creditors</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>01.4.95 To Balance b/d</td>
<td>9,500</td>
<td>31.3.96 By Discount Received 4,500</td>
</tr>
<tr>
<td>31.3.96 To Profit &amp; Loss A/c — transferred</td>
<td>20</td>
<td>31.3.96 By Balance c/d (4% on Rs. 1,25,500) 5,020</td>
</tr>
<tr>
<td></td>
<td>9,520</td>
<td>31.3.96 By Discount Received 9,520</td>
</tr>
<tr>
<td>01.4.96 To Balance b/d</td>
<td>5,020</td>
<td>31.3.97 By Discount Received 12,000</td>
</tr>
<tr>
<td>31.3.97 To Profit &amp; Loss A/c — trfd.</td>
<td>13,700</td>
<td>31.3.97 By Balance c/d 6,720</td>
</tr>
<tr>
<td></td>
<td>18,720</td>
<td>31.3.97 By Balance c/d 18,720</td>
</tr>
</tbody>
</table>

Illustration 21:

R. Sing, a trader makes provision for doubtful debts at the end of each year against specific debtors. On 31st March, 1997 the following debtors’ balances were considered doubtful and provided for B Rs. 3,000, C Rs. 800, D Rs. 500.

Following are the particulars for the year ended 31st March, 1998:

(i)  Bad Debts 00, S - Rs. 1,200, N - Rs. 1,000;
(ii) Bad Debts considered doubtful at the end of the year : G - Rs. 1,600, H - Rs. 1,800, K - Rs. 2,000.

Debts considered doubtful at the commencement of the year were either realised or written off as Bad Debts.

Write up the Bad Debts A/c and Provision for Doubtful Debts A/c for the year ended 31st March, 1998.
Financial Accounting Fundamentals

Solution :

R Singh

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Bad Debts Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>31.3.98</td>
<td>To Sundry Debtors</td>
<td>3,400</td>
</tr>
<tr>
<td>(2,400+500+500)</td>
<td>By Provisions for Bad Debts A/c</td>
<td>3,400</td>
</tr>
<tr>
<td>31.3.98</td>
<td>3,400</td>
<td>3,400</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Provision For Bad Debts Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>31.3.98</td>
<td>To Bad Debts A/c</td>
<td>3,400</td>
</tr>
<tr>
<td>To Balance (1,600+1,800+2,000)</td>
<td>5,400</td>
<td>31.3.98</td>
</tr>
<tr>
<td>(1,400+1,200+1,000)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>8,800</td>
<td></td>
<td>8,800</td>
</tr>
</tbody>
</table>

Note : Amount realised against bad debts previously written off should be credited to Provision for Bad & Doubtful Debts A/c.

Illustration 22 :

(a) The following is the agewise analysis of customers dues not yet written off as bad as at the end of each of the 3 years ended 31st March, 2000:

<table>
<thead>
<tr>
<th></th>
<th>Over 3 years</th>
<th>Outstanding for 3 years upto one year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>31-3-1998</td>
<td>40,000</td>
<td>1,00,000</td>
</tr>
<tr>
<td>31-3-1999</td>
<td>50,000</td>
<td>1,20,000</td>
</tr>
<tr>
<td>31-3-2000</td>
<td>60,000</td>
<td>1,50,000</td>
</tr>
</tbody>
</table>
Final Accounts

(b) The business carried forward a “provision” for doubtful debts and a “reserve” for doubtful debts at the end of each year with reference to year end debtors:

<table>
<thead>
<tr>
<th>Debts due</th>
<th>Provision</th>
<th>Reserve</th>
</tr>
</thead>
<tbody>
<tr>
<td>Over 3 years</td>
<td>100%</td>
<td>Nil</td>
</tr>
<tr>
<td>Over 2 years less than 3 years</td>
<td>75%</td>
<td>25%</td>
</tr>
<tr>
<td>Over 1 year less than 2 years</td>
<td>50%</td>
<td>10%</td>
</tr>
<tr>
<td>Less than 1 year</td>
<td>4%</td>
<td>6%</td>
</tr>
</tbody>
</table>

(c) The actual bad debts written off before arriving at the figures of debtors in (a) above during the year were:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997-1998</td>
<td>50,000</td>
</tr>
<tr>
<td>1998-1999</td>
<td>75,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>1,00,000</td>
</tr>
</tbody>
</table>

You are asked to show for each of the 3 years ended 31-3-2000 accounts relating to

(i) bad debts,
(ii) provision for doubtful debts,
(iii) reserve for doubtful debts.

You are informed that the balance on 31-3-1997 in “provision” for doubtful debts account is Rs. 60,000 and in “reserve” for doubtful debts account is Rs. 1,00,000.

Show your working.

Solution:

<table>
<thead>
<tr>
<th>Working</th>
<th>31.3.97</th>
<th>31-3-98</th>
<th>31-3-99</th>
<th>31-3-2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td></td>
</tr>
<tr>
<td>Bad debts written off.</td>
<td>?</td>
<td>50000</td>
<td>75000</td>
<td>100000</td>
</tr>
<tr>
<td>Provision for doubtful debts:</td>
<td>60,000</td>
<td>40,000</td>
<td>50,000</td>
<td>60,000</td>
</tr>
<tr>
<td>at 100%</td>
<td>75%</td>
<td>90,000</td>
<td>1,12,500</td>
<td>1,35,000</td>
</tr>
<tr>
<td>at 50%</td>
<td>1,00,000</td>
<td>1,12,500</td>
<td>1,35,000</td>
<td>1,35,000</td>
</tr>
<tr>
<td>at 4%</td>
<td>40,000</td>
<td>48,000</td>
<td>60,000</td>
<td>60,000</td>
</tr>
<tr>
<td>Closing balance.</td>
<td>60,000</td>
<td>2,55,000</td>
<td>3,00,500</td>
<td>3,67,500</td>
</tr>
<tr>
<td>Reserve for doubtful debts:</td>
<td>1,00,000</td>
<td>25,000</td>
<td>30,000</td>
<td>37,500</td>
</tr>
<tr>
<td>at 25%</td>
<td>20,000</td>
<td>22,500</td>
<td>27,000</td>
<td>27,000</td>
</tr>
<tr>
<td>at 10%</td>
<td>60,000</td>
<td>72,000</td>
<td>90,000</td>
<td>90,000</td>
</tr>
<tr>
<td>at 6%</td>
<td>1,05,000</td>
<td>1,24,500</td>
<td>1,24,500</td>
<td>1,24,500</td>
</tr>
</tbody>
</table>
### Bad Debts A/c.

<table>
<thead>
<tr>
<th>Year</th>
<th>To</th>
<th>Dr.</th>
<th>By</th>
<th>Cr.</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997-98</td>
<td>Customers A/c.</td>
<td>50,000</td>
<td>Provision for bad debts</td>
<td>.</td>
<td>50,000 Dr.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>50,000</td>
<td>Nil</td>
</tr>
<tr>
<td>1998-99</td>
<td>Customers A/c.</td>
<td>75,000</td>
<td>Provision for bad debts</td>
<td>.</td>
<td>75,000 Dr.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>75,000</td>
<td>Nil</td>
</tr>
<tr>
<td>1999-2000</td>
<td>Customers A/c.</td>
<td>1,00,000</td>
<td>Provisions for bad debts.</td>
<td>.</td>
<td>1,00,000 Nil.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1,00,000</td>
<td></td>
</tr>
</tbody>
</table>

### Provision for Doubtful Debts

<table>
<thead>
<tr>
<th>Year</th>
<th>To</th>
<th>Dr.</th>
<th>By</th>
<th>Cr.</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997-98</td>
<td>Balance b/fd</td>
<td></td>
<td>Balance b/fd</td>
<td>60,000</td>
<td>Cr.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Profit and loss A/c.</td>
<td>2,45,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Balance c/fd</td>
<td>2,55,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>3,05,000</td>
<td></td>
</tr>
<tr>
<td>1998-99</td>
<td>Balance b/fd</td>
<td></td>
<td>Balance b/fd</td>
<td>2,55,000</td>
<td>Cr.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Profit and loss A/c.</td>
<td>1,20,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Balance c/fd</td>
<td>3,00,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>3,75,500</td>
<td></td>
</tr>
<tr>
<td>1999-2000</td>
<td>Balance b/fd</td>
<td></td>
<td>Balance b/fd</td>
<td>3,00,500</td>
<td>Cr.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Profit and loss A/c.</td>
<td>1,67,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Balance c/fd</td>
<td>3,67,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>4,67,500</td>
<td></td>
</tr>
</tbody>
</table>
2.7 SPECIMEN QUESTION WITH ANSWERS

Question 1:

S. Ltd. keeps no running stock records but a physical inventory of stock is made at the end of each quarter and evaluated at cost. The company's year ends on 31st March, 1997 and draft accounts have been prepared to that date. The stock inventory taken on 31st March, 1997 was accidentally destroyed before the items had been evaluated, the closing stock figure used in the draft accounts being that shown by the inventory taken on 31st December, 1996. The gross margin earned by company is 25% of cost. During your audit you discovered the following:

(a) The cost of the stock on 31st December, 1996 as shown by the inventory was Rs. 40,525.

(b) On 31st December, 1996 stock sheets showed the following discrepancies:
   (i) A page total of Rs. 5,059 had been carried to the summary as Rs. 5,509.
   (ii) The total of a page had been undercast by Rs. 98.
   (iii) 100 items which had cost Rs. 5 each had been taken at 25 paise each.

(c) Invoice for purchases entered in the Purchases Book during the month of January, February and March, 1997 totalled Rs. 38,560. Of this total Rs. 2,800 related to goods received on or prior to 31st December, 1996. Invoices entered in April, 1997 relating to goods received in March, 1997 totalled Rs. 3,700.
Financial Accounting Fundamentals

(d) Sales invoiced to customers in January, February and March, 1997 totalled Rs. 51,073. Of this total Rs. 3,824 related to goods despatched on or before 31st December, 1996. Goods despatched to customers before 31st March, 1997 but invoiced in April, 1997 totalled Rs. 5,241.

(e) During the final quarter to the company's year, credit notes at invoiced value of Rs. 1,280 had been issued to customers in respect of goods returned during that period. You are required to prepare a statement showing the amount of the stock at cost as on 31st March, 1997.

Answer:

Statement showing the amount of Physical Stock at Cost as on 31st March, 1997.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>a) Adjusted Stock as on 31.12.96</strong></td>
<td>Rs. 40,525</td>
</tr>
<tr>
<td>Stock at cost as on 31.12.96</td>
<td></td>
</tr>
<tr>
<td>Add : Cost of 100 items wrongly undercast by Rs. 4.75 (5.00 – 0.25) each 100×4.75</td>
<td>475</td>
</tr>
<tr>
<td>Under cast in total of a page by Rs. 98</td>
<td>98</td>
</tr>
<tr>
<td>Less : Errors in carry forward of a page total by Rs. 450 (Rs. 5509 – Rs. 5059) – overcast</td>
<td>450</td>
</tr>
<tr>
<td></td>
<td>41,098</td>
</tr>
<tr>
<td><strong>b) Adjusted cost of sales as on 31.3.97.</strong></td>
<td></td>
</tr>
<tr>
<td>Sales from 1.1.97 to 31.3.97</td>
<td>Rs. 51,073</td>
</tr>
<tr>
<td>Add : Goods despatched before 31.3.97 but invoice raised in April, 97</td>
<td>5,241</td>
</tr>
<tr>
<td>Less : Goods despatched before 31.12.96 included in sales of Rs. 51,073</td>
<td>3,824</td>
</tr>
<tr>
<td>Less : Credit Note issued to customers for sales return during final quarter i.e. January to March, '97</td>
<td>1,280</td>
</tr>
<tr>
<td>Less : Gross margin @ 25% on cost i.e., 20% on sale Rs. 51,210</td>
<td>10,242</td>
</tr>
<tr>
<td></td>
<td>40,968</td>
</tr>
<tr>
<td><strong>c) Adjusted Purchase as on 31.3.97.</strong></td>
<td></td>
</tr>
<tr>
<td>Purchase from 01.01.97 to 31.3.97</td>
<td>Rs. 38,560</td>
</tr>
<tr>
<td>Add : Goods purchased before 31.3.97 but recorded in April, '97</td>
<td>3,700</td>
</tr>
<tr>
<td>Less : Goods received before 31.12.96 included in purchase of Rs. 38,560</td>
<td>2,800</td>
</tr>
<tr>
<td></td>
<td>39,460</td>
</tr>
</tbody>
</table>
Final Accounts

d) Stock (Physical) as on 31.3.97
   Adjusted Stock as on 31.12.96 — (a) 40,648
   Add : Adjusted purchase as on 31.3.97 — (c) 39,460
   Less : Adjusted cost of sales as on 31.3.97 — (b) 40,968
   Physical stock balance as on 31.3.97 at Cost 39,140

Question 2:

The Balance in Profit & Loss Account as per Balance Sheet as at 31st March, 1997 is Rs. 32,600, whereas the balance on Balance Sheet as at 31st March, 1998 is Rs. 38,100. The following facts are ascertained:

   (i) Rs. 8,500 depreciation has been charged;
   (ii) Provision for dividend Rs. 15,000 has been made;
   (iii) Rs. 4,500 has been transferred to General Reserve;
   (iv) Rs. 1,000 Dividend (gross) has been credited;
   (v) Rs. 2,300 Loss on Sale and Fixed Assets has been debited;
   (vi) Indirect Expenses debited amount to Rs. 30,500 in total.

Find out Gross Profit, Trading Profit and Net Profit.

Answer:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Profit &amp; Loss Account (Includes)</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Indirect expenses</td>
<td>30,500</td>
<td></td>
</tr>
<tr>
<td>To Trading Profit c/d (2)</td>
<td>34,800</td>
<td>65,300</td>
</tr>
<tr>
<td></td>
<td>65,300</td>
<td>65,300</td>
</tr>
<tr>
<td>To Loss on sale of Fixed Assets</td>
<td>2,300</td>
<td>34,800</td>
</tr>
<tr>
<td>To Depreciation</td>
<td>8,500</td>
<td>1,000</td>
</tr>
<tr>
<td>To Net Profit c/d (1)</td>
<td>25,000</td>
<td>35,800</td>
</tr>
<tr>
<td></td>
<td>35,800</td>
<td>35,800</td>
</tr>
<tr>
<td>To Provision for dividend</td>
<td>15,000</td>
<td>32,600</td>
</tr>
<tr>
<td>To General Reserve</td>
<td>4,500</td>
<td>25,000</td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>38,100</td>
<td>57,600</td>
</tr>
<tr>
<td></td>
<td>57,600</td>
<td>57,600</td>
</tr>
</tbody>
</table>

Note: The missing figures marked 1, 2 and 3 have been found out in the same order.
Financial Accounting Fundamentals

Question 3:

P.K. commenced business in a retail shop on 1st July, 1997 in premises for which he paid a rent of Rs. 320 per month. The only records he kept, apart from his bank statements, were files of paid invoices and unpaid invoices for goods purchased, together with a notebook in which he recorded a few sales on credit to special customers who paid him by cheques. Cash received from cash sale was paid into the till out which he paid certain amounts, of which he kept a rough record, and he made weekly bankings out of the balance in the till. He paid all suppliers for goods purchased by cheque.

An analysis of the bank statements for the six months ended 31st December, 1997 was as follows:

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital paid in</td>
<td>6,400</td>
</tr>
<tr>
<td>Loan (interest free)</td>
<td>3,200</td>
</tr>
<tr>
<td>Suppliers cheque for goods returned</td>
<td>448</td>
</tr>
<tr>
<td>Special customers</td>
<td>480</td>
</tr>
<tr>
<td>Total of weekly cash bankings</td>
<td>19,088</td>
</tr>
<tr>
<td>Shop fixtures and fittings</td>
<td>3,200</td>
</tr>
<tr>
<td>Household furniture</td>
<td>2,880</td>
</tr>
<tr>
<td>Suppliers (for purchases)</td>
<td>15,744</td>
</tr>
<tr>
<td>Rates</td>
<td>480</td>
</tr>
<tr>
<td>Rent</td>
<td>1,600</td>
</tr>
<tr>
<td>Insurance on stocks</td>
<td>320</td>
</tr>
<tr>
<td>Electricity</td>
<td>288</td>
</tr>
<tr>
<td>Balance on 31st December, 1997</td>
<td>5,104</td>
</tr>
<tr>
<td>Balance on 31st December, 1997</td>
<td>29,616</td>
</tr>
</tbody>
</table>

P.K. estimates that the total amounts paid out of the till before making the weekly bankings for the six months were:

Drawings - Rs. 3,200, Wages - Rs. 2,240 and Sundry shop expenses - Rs. 1,280.

You ascertain that as on 31st December, 1997:

1. Stocks, correctly taken at cost, were Rs. 2,752.
2. The balance in the till was Rs. 416, including a post dated cheque for Rs. 200, cashed for a customer.
3. Cheques for Rs. 272 from special credit customers paid into the bank have not been cleared. One for Rs. 112 was cleared on 3rd January, 1998 and the other for Rs. 160 was returned dishonoured and the customer could not be traced. This sum is considered as bad. Other special customers owned Rs. 384.
4. The following cheques had been issued but had not been presented—rent for December Rs. 320 and lighting charges Rs. 240.
5. The cash paid into the bank included Rs. 480 from a sale of surplus shop fittings. There was no profit or loss on this transaction.
6. Suppliers’ unpaid invoices amounted to Rs. 3,584 and there was Rs. 64 owing for electricity.

You are required to prepare the Balance Sheet as at 31st December, 1997 and the Trading and Profit and Loss Account for the half-year ended on that date.
**Final Accounts**

**Answer:**

**Trading and Profit & Loss Account for the half year ended 31st December, 1997**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Purchases</td>
<td>19,328</td>
<td></td>
<td>By sales —</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less : Returns</td>
<td>448</td>
<td>18,880</td>
<td>Cash sales</td>
<td>25,744</td>
<td></td>
</tr>
<tr>
<td>&quot; Wages</td>
<td>2,240</td>
<td></td>
<td>By Closing Stock</td>
<td>2,752</td>
<td></td>
</tr>
<tr>
<td>&quot; Gross Profit c/d</td>
<td>8,512</td>
<td>29,632</td>
<td>Gross Profit c/d</td>
<td>8,512</td>
<td></td>
</tr>
<tr>
<td>To Shop Expenses</td>
<td>1,280</td>
<td></td>
<td>By Gross Profit b/d</td>
<td>8,512</td>
<td></td>
</tr>
<tr>
<td>&quot; Rent (1600+320)</td>
<td>1,920</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Rates</td>
<td>480</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Insurance</td>
<td>320</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Electricity (Rs.288+64)</td>
<td>352</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Reserve for Bad debts</td>
<td>160</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Lighting charges</td>
<td>240</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Net Profit transferred to Capital A/c</td>
<td>3,760</td>
<td>8,512</td>
<td>Net Profit transferred to Capital A/c</td>
<td>3,760</td>
<td>8,512</td>
</tr>
</tbody>
</table>

**Balance Sheet as at 31st December, 1997**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Creditors for expenses—Electricity</td>
<td>64</td>
<td></td>
<td>Cash in hand</td>
<td>416</td>
<td></td>
</tr>
<tr>
<td>Trade Creditors</td>
<td>3,584</td>
<td></td>
<td>Cash at Bank</td>
<td>4,816</td>
<td></td>
</tr>
<tr>
<td>Loan Account</td>
<td>3,200</td>
<td></td>
<td>Sundry Debtors</td>
<td>384</td>
<td></td>
</tr>
<tr>
<td>Capital Account —</td>
<td></td>
<td></td>
<td>Less : Reserve for B.D.</td>
<td>160</td>
<td>224</td>
</tr>
<tr>
<td>Amount deposited</td>
<td>6,400</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add : Profit</td>
<td>3,760</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>10,160</td>
<td></td>
<td>Stock</td>
<td>2,752</td>
<td></td>
</tr>
<tr>
<td>Less : Drawings</td>
<td></td>
<td></td>
<td>Shop, fixture and fittings</td>
<td>3,200</td>
<td></td>
</tr>
<tr>
<td>(Household furniture)</td>
<td></td>
<td></td>
<td>Less : Sold</td>
<td>480</td>
<td>2,720</td>
</tr>
<tr>
<td>Cash drawing</td>
<td>2,880</td>
<td>4,080</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,200</td>
<td>10,928</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
**Working Notes:**

1) **Cash Sales:**

   - Total of weekly cash bankings: Rs. 19,088
   - Add: Payments made out of till:
     - Drawings: 3,200
     - Wages: 2,240
     - Shop expenses: 1,280
   - Balance on hand: 416

   Less: Sale of surplus shop fittings included in weekly bankings: 480

   Balance on hand: 26,224

2) **Sales to special customers:**

   - Cheques received from special customers and banked: 480
   - Add: Chqs. recd. from sp. customers paid in but not collected: 272
   - Amount due from special customers: 384
   - Total: 1,136

3) **Purchases:**

   - Payment to suppliers (for purchases): Rs. 15,744
   - Add: unpaid invoices: 3,584
   - Total: 19,328

4) **Bank balance as per Cash Book:**

   - Balance as per Pass Book: 5,104
   - Add: Cheques paid in but not credited: 272
   - Total: 5,376

   Less: Cheques issued but not yet presented for payment:
     - Rent: 320
     - Lighting: 240
   - Total: 560

   Bank balance as per Cash Book: 4,816

   Since the cheque in the till is a postdated cheque, it is not considered and is treated as cash.

5) The cheque for Rs. 160 received from special customers which was dishonoured subsequently can not be considered as bad debts during the current accounting period. Assuming that P.K. had the knowledge of the cheque being dishonoured at the time of preparing the accounts, provision for bad debts is made so that during the next accounting period, this can be written off against the Reserve.
Final Accounts

Question 4:

The Profit and Loss Account of Sampat for the year ended 31st March, 1998 showed a Net Profit of Rs. 2,500 after taking into account the closing Stock of Rs. 4,720.

On a scrutiny of the books the following information could be obtained:

(i) Purchases of the year included Rs. 500 spent on acquisition of a ceiling fan for his shop.

(ii) Sampat has taken goods valued at Rs. 1,800 for his personal use without making entry in the books.

(iii) Invoices for goods amounting to Rs. 4,000 have been entered on 29th March, 1998 but such goods were not included in stock.

(iv) Sale of goods amounting to Rs. 700 sold and delivered in March, 1998 had been entered in April, 1998 sales.

(v) Rs. 500 had been included in closing stock in respect of goods purchased and invoiced on 28th March, 1998 but included in purchase for April, 1998.

You are required to ascertain the correct amount of Closing Stock as on 31st March, 1998 and the adjusted Net Profit for the year ended on that date.

Answer:

In the Books of Sampat:

(i) Calculation of stock as on 31st March, 1998:

<table>
<thead>
<tr>
<th>Stock as already given</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>4,720</td>
<td></td>
</tr>
</tbody>
</table>

Add : Purchases not included

| 4,000 | 8,720 |

(ii) Profit & Loss Adjustment Account

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Profit &amp; Loss Adjustment Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To</td>
<td>Suppliers A/c</td>
<td>500</td>
</tr>
<tr>
<td>&quot;</td>
<td>Net Profit (Balancing figure)</td>
<td>9,000</td>
</tr>
<tr>
<td>&quot;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>9,500</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Question 5:

Mr. Clarence starts a business on 1.1.98 with Rs. 10,000 and purchases furniture and equipments for Rs. 1,000 and starts a Current Account with the balance.

He employs one salesman for Rs. 100 p.m. payable in the first week of the month following. He also rents a house at Rs. 70 p.m. payable in the last week of the month concerned.

He cannot stand paper work and he does not maintain any books of account, whatsoever. He prepares challans which are handed over on payment. All purchases are paid for by bearer or crossed cheques from Current Account. All collections are deposited intact in Current Account.

Rs. 500 p.m. is transferred to a Saving Account wherefrom other expenses and drawings @ Rs. 250 p.m. are made.

He keeps petty cash box from which direct charges on purchase as carriage, etc. are met and periodically it is reimbursed from Current Account.

On 31.12.98 the following balances are there: Stock Rs. 5,000; Current Account Rs. 7,000; Saving Account Rs. 300; Petty Cash Box Rs. 20; Cash Rs. 500 collected and to be deposited, already entered in pay-in-slips; Challans in hand Rs. 1,000.

It is found that Rs. 10 has been credited as interest in Savings Account. A challan showing Rs. 50 is not recoverable. Prepare Profit and Loss Account for the year and Balance Sheet as on 31.12.98 taking the following points into consideration:

(a) Depreciation @10% p.a. on Furniture and Fixture is to be provided.
(b) 10% Reserve for Bad Debt is to be created.

Answer:

<table>
<thead>
<tr>
<th>Dr. Particulars</th>
<th>Profit and Loss Account for the year ended 31st December, 1998 Rs.</th>
<th>Cr. Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Salary (1,100+100)</td>
<td>1,200</td>
<td>By Gross Profit</td>
<td>10,520</td>
</tr>
<tr>
<td>&quot; Rent</td>
<td>840</td>
<td>&quot; Bank Interest</td>
<td>10</td>
</tr>
<tr>
<td>&quot; Petty Expenses</td>
<td>770</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Depreciation</td>
<td>100</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Bad Debts</td>
<td>50</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Provn. for Bad Debts on Rs. 950</td>
<td>95</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Net Profit</td>
<td>7,475</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>10,530</td>
</tr>
</tbody>
</table>

10,530

10,530
Final Accounts

**Balance Sheet as at 31st December, 1998**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outstanding Salary</td>
<td>100</td>
<td></td>
<td>Furniture &amp; Equipments</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>10,000</td>
<td></td>
<td>Less : Depreciation</td>
<td>100</td>
<td>900</td>
</tr>
<tr>
<td>Add : Profit for the year</td>
<td>7,475</td>
<td></td>
<td>Closing Stock</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>17,475</td>
<td></td>
<td>Debtors</td>
<td>950</td>
<td></td>
</tr>
<tr>
<td>Less : Drawings</td>
<td>3,000</td>
<td>14,475</td>
<td>Less : Provision for B. Debts</td>
<td>95</td>
<td>855</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Cash at Banks :</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Current Account</td>
<td>7,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Savings Account</td>
<td>300</td>
<td>7,300</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Cash in Hand :</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Petty Cash</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Cash (for depositing)</td>
<td>500</td>
<td>520</td>
</tr>
<tr>
<td></td>
<td></td>
<td>14,575</td>
<td>14,575</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Working Note :**

1) Statement for finding out Gross profit (From Current Account and allied items)

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Savings Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To Total Deposits into Savings A/c</td>
<td>6,000</td>
<td>By</td>
</tr>
<tr>
<td>(Rs.500×12)</td>
<td></td>
<td>”</td>
</tr>
<tr>
<td></td>
<td></td>
<td>”</td>
</tr>
<tr>
<td></td>
<td></td>
<td>”</td>
</tr>
<tr>
<td></td>
<td></td>
<td>”</td>
</tr>
<tr>
<td></td>
<td>6,010</td>
<td></td>
</tr>
</tbody>
</table>

The Petty Expenses from Savings Accounts are found from an analysis of Savings Account.
Question 6:

From the following details of a partnership firm prepare Manufacturing, Trading and Profit and Loss Account and P/L Appropriation Account for the year ending 31st March, 1998, and a Balance Sheet as on 31st March, 1998.

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Stock:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Raw Material</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Work-in-Progress</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Finished Goods</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>Purchases:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Raw Material</td>
<td>2,10,000</td>
<td></td>
</tr>
<tr>
<td>Finished Goods</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Factory Rent</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td>Office Rent, Rate and Taxes</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>Factory Salary</td>
<td>18,000</td>
<td></td>
</tr>
<tr>
<td>Office Salary</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td>Debtors and Creditors</td>
<td>78,000</td>
<td>56,000</td>
</tr>
<tr>
<td>Sales</td>
<td>3,30,000</td>
<td></td>
</tr>
<tr>
<td>Selling Expenses</td>
<td>8,000</td>
<td></td>
</tr>
<tr>
<td>Interest on Loan paid</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Discount Allowed</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>Discount Received</td>
<td>1,100</td>
<td></td>
</tr>
<tr>
<td>Capital and Partnership Salary (drawn):</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sita</td>
<td>6,000</td>
<td>68,000</td>
</tr>
<tr>
<td>Gita</td>
<td>3,000</td>
<td>30,000</td>
</tr>
<tr>
<td>Loan</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Wages</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Interest on Partner’s Capital (drawn):</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sita</td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>Gita</td>
<td>600</td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>45,000</td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>5,35,100</td>
<td>5,35,100</td>
</tr>
</tbody>
</table>

(a) Provide 10% depreciation on Machinery and Furniture.
(b) Loan carries 10% interest and the amount is brought forward from earlier year.
(c) Provide 6% interest on Partners’ Capital.
Final Accounts

(d) Closing Stocks are:

<table>
<thead>
<tr>
<th>Item</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Materials</td>
<td>50,000</td>
</tr>
<tr>
<td>Work-in-Progress</td>
<td>10,000</td>
</tr>
<tr>
<td>Finished Goods</td>
<td>35,000</td>
</tr>
</tbody>
</table>

(e) Salary Outstanding as on 31st March, 1998:

<table>
<thead>
<tr>
<th>Item</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Factory</td>
<td>2,000</td>
</tr>
<tr>
<td>Office</td>
<td>1,000</td>
</tr>
</tbody>
</table>

(f) Sita and Gita share profits and losses as 3:2 after charging salary @ Rs. 500 and Rs. 250 p.m. to Sita and Gita respectively.

(g) Outstanding Factory Rent Rs. 1,000.

Answer:

Dr. Manufacturing Account for the year ended 31st March, 1998

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Raw Materials</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Work-in-progress</td>
<td>5,000</td>
<td>65,000</td>
</tr>
<tr>
<td>To Purchases — Raw Materials</td>
<td>2,10,000</td>
<td></td>
</tr>
<tr>
<td>To Wages</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>To Factory Expenses and charges:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Factory Salary (18,000+2,000)</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>Factory Rent (12,000+1,000)</td>
<td>13,000</td>
<td></td>
</tr>
<tr>
<td>Deprn. on Machinery (10%)</td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,42,500</td>
<td></td>
</tr>
<tr>
<td>By Closing Stock:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Raw Materials</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Work-in-progress</td>
<td>10,000</td>
<td>60,000</td>
</tr>
</tbody>
</table>

Cr. Trading Account for year ended 31st March, 1998

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock of Finished Goods</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>To Purchase of Finished Goods</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>To Cost of Prod.-b/d from Mfg. A/c</td>
<td>2,82,500</td>
<td></td>
</tr>
<tr>
<td>To Balance – Gross Profit c/d</td>
<td>52,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,65,000</td>
<td></td>
</tr>
<tr>
<td>By Sales</td>
<td></td>
<td>3,30,000</td>
</tr>
<tr>
<td>By Closing Stock of Finished Goods</td>
<td></td>
<td>35,000</td>
</tr>
</tbody>
</table>
### Profit and Loss Account for the year ended 31st March, 1998

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Office Salaries (12,000 + 1,000)</td>
<td>13,000</td>
<td></td>
<td>By Balance b/d - Gross Profit</td>
<td>52,500</td>
<td></td>
</tr>
<tr>
<td>To Office Rent, Rates and Taxes</td>
<td>3,000</td>
<td></td>
<td>By Discount Received</td>
<td>1,100</td>
<td></td>
</tr>
<tr>
<td>To Selling Expenses</td>
<td>8,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Discount Allowed</td>
<td>3,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest on loan: 10% of Rs. 50,000</td>
<td>5,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Depreciation on Furniture 10%</td>
<td>500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Balance-Net Profit c/d</td>
<td>21,100</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>53,600</td>
<td></td>
<td></td>
<td></td>
<td>53,600</td>
</tr>
</tbody>
</table>

### Profit & Loss Appropriation Account for the year ended 31st March, 1998

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Interest of Capital :</td>
<td></td>
<td></td>
<td>By Balance b/d - Net Profit</td>
<td>21,100</td>
<td></td>
</tr>
<tr>
<td>Sita</td>
<td>4,080</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gita</td>
<td>1,800</td>
<td>5,880</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Partner’s Salary :</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sita</td>
<td>6,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gita</td>
<td>3,000</td>
<td>9,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Share of Profit :</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sita (3)</td>
<td>3,732</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gita (2)</td>
<td>2,488</td>
<td>6,220</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>21,100</td>
<td></td>
<td></td>
<td></td>
<td>21,100</td>
</tr>
</tbody>
</table>

### Balance Sheet as at 31st March, 1998

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Accounts :</td>
<td></td>
<td></td>
<td>Machinery</td>
<td>45,000</td>
<td></td>
</tr>
<tr>
<td>Sita :</td>
<td>68,000</td>
<td></td>
<td>Less : Depreciation</td>
<td>4,500</td>
<td>40,500</td>
</tr>
<tr>
<td>Add : Salary</td>
<td>6,000</td>
<td></td>
<td>Furniture</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Interest on Capital</td>
<td>4,080</td>
<td></td>
<td>Less : Depreciation</td>
<td>500</td>
<td>4,500</td>
</tr>
<tr>
<td>Share of Profit</td>
<td>3,732</td>
<td></td>
<td>Stock :</td>
<td>81,812</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>75,312</td>
<td></td>
</tr>
<tr>
<td>Less : Drawings (6000+500)</td>
<td>6,500</td>
<td>75,312</td>
<td></td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Gita :</td>
<td>37,288</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add : Salary</td>
<td>3,000</td>
<td></td>
<td>Debtors</td>
<td>78,000</td>
<td></td>
</tr>
<tr>
<td>Interest on Capital</td>
<td>1,800</td>
<td></td>
<td>Cash</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Share of profit</td>
<td>2,488</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>33,688</td>
<td></td>
<td></td>
<td></td>
<td>10,000</td>
</tr>
</tbody>
</table>

Less : Drawings (3000+600)
Final Accounts

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan</td>
<td>50,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>56,000</td>
</tr>
<tr>
<td>Liabilities for Expenses:</td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>3,000</td>
</tr>
<tr>
<td>Interest on Loan (5000–4000)</td>
<td>1,000</td>
</tr>
<tr>
<td>Factory Rent</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>2,20,000</td>
</tr>
</tbody>
</table>

Question 7:

Arvind operates a warehouse selling wall papers direct to the public on a strictly cash basis. On 1st April 1999, a serious fire at his premises destroyed or damaged all his stock and most of his accounting and stock records. He has asked you to calculate the cost of stocks so that he can make an insurance claim. He has also asked you to establish whether he has trading profitability in the period from 1st October 1998 to the date of fire, so that he can decide whether to start trading again in this line.

You obtain the following information in connection with his trading activities:

1. Arvind obtains supplies of wall papers from two companies only Tee Ltd. and Dee Ltd. Both the companies supply Arvind with goods at recommended retail price(R.R.P.) less 331/3%. A cash discount of 10% is given on this net price for payment within two weeks, which Arvind always takes.

2. Both suppliers give an extra bulk rebate based on the value of goods purchased over the winter months from 1st October to 31st March. The rebate from Tee Ltd. amount to 5% R.R.P. for goods purchased excluding the first Rs. 25,000 in the winter months. Dee Ltd. gives a rebate of 8% on R.R.P. for goods purchased excluding the first Rs. 37,500 in those months.

3. The bulk rebate for the six months to 31st March 1999 was received in April 1999 and amounted to Rs. 4,100 in respect of purchases from Tee Ltd. and Rs. 3,800 in respect of purchases from Dee Ltd.

4. Arvind sells all goods at a price which gives a gross profit equal to 25% of the cost of goods, before deducting either the cash discount or the bulk rebate.

5. General expenses paid out of cash sales prior to banking are estimated at the following monthly amounts:–

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wages &amp; salaries</td>
<td>1,470</td>
</tr>
<tr>
<td>Motor expenses</td>
<td>218</td>
</tr>
<tr>
<td>Sundry expenses</td>
<td>105</td>
</tr>
<tr>
<td>Drawings by Arvind</td>
<td>150</td>
</tr>
</tbody>
</table>
(6) Information obtained from paid cheques and bank statements showed bank deposits from sale of Rs. 1,62,362, general overheads of Rs. 27,452 and two quarterly rent payments of Rs. 1,500 each.

(7) Fixtures which cost Rs. 8,000 and vehicles which cost Rs. 7,600 are to be depreciated at the rate of 15% and 25 % per annum respectively.

(8) In January 1999 Arvind used wall paper which cost before deducting either the bulk rebate or the cash discount Rs. 180 in decorating his own house.

(9) The stock held by Arvind on 30th September 1998 had a cost before deduction of any rebates or discounts of Rs. 56,807.

You are required to :-

(a) calculate the cost before deduction of any rebate or discounts of Arvind’s stock on 31.3.99.

(b) prepare a trading and profit and loss account for the six months to 31.3.1999.

**Answer :**

**In the books of ARVIND**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Trading and profit and loss account for the period ended 31.03.99</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To</td>
<td>Opening stock</td>
<td>56,807</td>
</tr>
<tr>
<td>To</td>
<td>Purchases</td>
<td>1,28,000</td>
</tr>
<tr>
<td>To</td>
<td>Gross profit (20% on sales)</td>
<td>34,804</td>
</tr>
<tr>
<td></td>
<td>2,19,611</td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Wages &amp; salaries (1,470×6)</td>
<td>8,820</td>
</tr>
<tr>
<td>To</td>
<td>Motor expenses (218×6)</td>
<td>1,308</td>
</tr>
<tr>
<td>To</td>
<td>Sundry expenses (105×6)</td>
<td>630</td>
</tr>
<tr>
<td>To</td>
<td>General overhead</td>
<td>27,452</td>
</tr>
<tr>
<td>To</td>
<td>Rent (1,500×2)</td>
<td>3,000</td>
</tr>
<tr>
<td>To</td>
<td>Depreciation</td>
<td>600</td>
</tr>
<tr>
<td></td>
<td>Vehicles</td>
<td>950</td>
</tr>
<tr>
<td>To</td>
<td>Net Profit c/d</td>
<td>12,744</td>
</tr>
<tr>
<td></td>
<td>Net Profit c/d</td>
<td>55,504</td>
</tr>
</tbody>
</table>
**Final Accounts**

**Working Notes:** Calculation of purchases —

<table>
<thead>
<tr>
<th></th>
<th>Tee Ltd.</th>
<th>Dee Ltd.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bulk rebate</td>
<td>4,100</td>
<td>3,800</td>
</tr>
<tr>
<td>Rebate rate (on M.R.P.)</td>
<td>5%</td>
<td>8%</td>
</tr>
<tr>
<td>Bulk purchase</td>
<td>82,000</td>
<td>47,500</td>
</tr>
<tr>
<td>Basic purchase</td>
<td>25,000</td>
<td>37,500</td>
</tr>
<tr>
<td>Total purchase</td>
<td>1,07,000</td>
<td>85,000</td>
</tr>
</tbody>
</table>

Total purchases at R.R.P.— 1,92,000
Less : Trade discount (1/3) 64,000
Purchase cost 1,28,000
Cash Sales —
Amount deposited in the bank 1,62,362
Wages & salaries 8,820
Motor car expenses 1,308
Sundry expenses 630
Drawings 900

1,74,020

**Question 8:**

On 30th November 1999 the balance sheet of Colourful & Co., a firm, is as under :-

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Creditors</td>
<td>60,000</td>
<td>Cash/bank</td>
</tr>
<tr>
<td>Reserves</td>
<td>40,000</td>
<td>Customers</td>
</tr>
<tr>
<td>Capitals:</td>
<td></td>
<td>Inventories</td>
</tr>
<tr>
<td>Green</td>
<td>12,00,000</td>
<td>Fixed assets WDV</td>
</tr>
<tr>
<td>Yellow</td>
<td>12,00,000</td>
<td>Investments at cost</td>
</tr>
<tr>
<td>Blue Ltd.</td>
<td>25,00,000</td>
<td>(market value Rs.15,00,000)</td>
</tr>
<tr>
<td></td>
<td>50,00,000</td>
<td>50,00,000</td>
</tr>
</tbody>
</table>

Green, Yellow and Blue Ltd. shared profit and losses in the ratio of 1:1:2.

On 1st December 1999 Green and Yellow retired and Blue Ltd. continued the business.

Blue Ltd. paid Rs. 18,00,000 to Green and Rs. 18,00,000 to Yellow in full and final discharge of their claim in the partnership. This amount was brought in by Blue Ltd. for the purpose of payment to the retiring partners. None of the asset and liabilities are to be revalued.
Financial Accounting Fundamentals

You are asked to:

(a) pass accounting entries in relation to the above in the books of the business unit.
(b) prepare the balance sheet of the business unit after the above transactions are recorded.

Answer:

Entries in the books of the Business Unit

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec. 1</td>
<td>Bank A/c</td>
<td>Dr. 36,00,000</td>
<td>36,00,000</td>
</tr>
<tr>
<td>1999</td>
<td>To Blue Ltd.’s Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being capital brought in by Blue Ltd. for payment to Green and Yellow.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Green’s Capital A/c</td>
<td>Dr. 18,00,000</td>
<td>36,00,000</td>
</tr>
<tr>
<td></td>
<td>Yellow’s Capital A/c</td>
<td>Dr. 18,00,000</td>
<td>36,00,000</td>
</tr>
<tr>
<td></td>
<td>To Bank A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being capitals paid off on retirement.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Blue Ltd.’s Capital A/c</td>
<td>Dr. 12,00,000</td>
<td>6,00,000</td>
</tr>
<tr>
<td></td>
<td>To Green’s Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Yellow’s Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being purchase by Blue Ltd. of shares of goodwill, unrecorded increase in value of assets and reserves from Green and Yellow on their retirement.)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Balance sheet of Business Unit after retirement of Green and Yellow (Rs. ’000)

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net worth being excess of assets</td>
<td>Fixed assets W.D.V.</td>
</tr>
<tr>
<td>over liabilities comprising of</td>
<td>Investment at cost</td>
</tr>
<tr>
<td>Blue Ltd.’s capital contribution</td>
<td>(Market value Rs. 15,00,000)</td>
</tr>
<tr>
<td>Reserves</td>
<td>Current assets</td>
</tr>
<tr>
<td>4900</td>
<td>Inventories</td>
</tr>
<tr>
<td>40</td>
<td>Customers dues</td>
</tr>
<tr>
<td>4940</td>
<td>Cash/bank</td>
</tr>
<tr>
<td>Current liabilities :</td>
<td></td>
</tr>
<tr>
<td>Creditors</td>
<td></td>
</tr>
<tr>
<td>60</td>
<td></td>
</tr>
<tr>
<td>5000</td>
<td></td>
</tr>
</tbody>
</table>

STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION
Question 9:

Ashoka Ltd. was incorporated on 1.1.1999 with an authorised capital of Rs. 25 crores. The subscribers to the memorandum and articles of association subscribed for 1000 equity shares of Rs. 10 each. The promoters and well wishers subscribed and paid for Rs. 4,99,000 equity shares of Rs. 10 each. The company took over running business of Magadha Bros. and allotted 15,00,000 equity shares of Rs. 10 each at par. The company made a public issue of 80,00,000 equity shares of Rs. 10 each at par, Rs. 5 being payable on application, Rs. 3 on allotment and Rs. 2 on call. Application monies were receivable by 28.2.1999, allotment was made on 31.3.1999, allotment moneys were due by 30.4.99, first call was made on 31.5.1999; first call was due by 30.6.1999.

Public applied for in full. Allotment monies were received from all members except holders of 500 shares. Call monies were received from all members except holders of 800 shares (including those who had not paid allotment monies).

After due notice, the 800 shares were forfeited on 30.9.1999. They were reissued on 31.10.1999 at Rs. 11 per share.

Your are asked to:

(a) record all the above transactions through the journal of Ashoka Ltd.

(b) show the presentation in the balance sheet as on 30.11.1999 of the company.

Answer:

**JOURNAL ENTRIES (in Rs. '000)**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being cheques received from the subscribers to</td>
<td></td>
<td></td>
</tr>
<tr>
<td>memorandum and articles of association in respect of 1000 equity shares no. 1 to 1000 agreed to be taken by them)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being application money received from promoters and well wishers)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity Share Application A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Equity Shares Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being allotment at par of 499000 equity shares vide board resolution dtd. ....)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Business Purchases A/c                      Dr. 15000
                                        To Equity Share Capital A/c 15000
                                        (Being allotment at par of 15,00,000 equity shares to
                                        Magadha Bros. on take over to their business vide
                                        board resolution dtd. .... )

Feb. 28   Bank A/c                          Dr. 40000
                                        To Equity Share Application A/c 40000
                                        (Being application monies at Rs. 5 per share received
                                        from applicants for 80,00,000 equity shares as per
                                        details in the application and allotment register.)

Mar. 31   Equity Share Application A/c      Dr. 40000
                                        Equity Share Allotment A/c 24000
                                        To Equity Share Capital A/c 64000
                                        (Being allotment of 80,00,000 equity shares and
                                        recording of allotment money due at Rs. 3 per share
                                        vide board resolution dtd. 31.03.1999)

Apr. 30   Bank A/c                          Dr. 23998.5
                                        To Equity Share Allotment A/c 23998.5
                                        (Being allotment moneys received from members
                                        except those owning 1500 shares)

May 31    Equity Share First Call A/c       Dr. 16000
                                        To Equity Share Capital A/c 16000
                                        (Being first call at Rs. 2 per share made from members
                                        holding 80,00,000 equity shares vide board resolution
                                        dtd. May, 31, 1999)

Sept. 30  Equity Share Capital A/c          Dr. 8.0
                                        To Equity Share Allotment A/c 1.5
                                        To Equity Share First call A/c 1.6
                                        To Forfeited Shares A/c 4.9
                                        (Being forfeiture of 800 shares for nonpayment of
                                        allotment & call monies as per details given : 500 shares
                                        for nonpayment of allotment, call 300 shares for
                                        nonpayment of call vide res. dtd. 30.9.99)
Final Accounts

Oct. 31

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank A/c</td>
<td>8.8</td>
</tr>
<tr>
<td>Forfeited Shares A/c</td>
<td>4.9</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td>8.0</td>
</tr>
<tr>
<td>To Capital Reserve A/c</td>
<td>5.7</td>
</tr>
</tbody>
</table>

(Being allotment on reissue of 800 equity shares no. ...) on receipt of Rs. 11 per share, vide board resolution dated dt.31.10. 1999)

Extracts from Balance Sheet as at 30.11.1999 (Rs. in crores)

<table>
<thead>
<tr>
<th>Share Capital :</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorised</td>
<td>25.00</td>
</tr>
<tr>
<td>Issued and subscribed :</td>
<td></td>
</tr>
<tr>
<td>For cash: 85,00,000 equity shares of Rs. 10 each fully paid</td>
<td>8.50</td>
</tr>
<tr>
<td>For consideration other than cash:</td>
<td></td>
</tr>
<tr>
<td>15,00,000 equity shares of Rs. 10 each fully paid on purchase of business</td>
<td>1.50 10.00</td>
</tr>
<tr>
<td>Reserves and surplus :</td>
<td></td>
</tr>
<tr>
<td>Capital reserve (Rs. 5,700)</td>
<td>0.00</td>
</tr>
</tbody>
</table>

Question 10:

King, Queen and Jack are sharing profits and losses in the ratio of 3 : 2 : 1. They are also entitled to interest on loan at 10% p.a., but not interest on capital.

The partners decided to dissolve the firm on 31.03.2000. Balance Sheet was drawn up to 31.12.1999 which is reproduced below:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital of King</td>
<td>1,68,000</td>
<td>Building</td>
<td>2,10,000</td>
</tr>
<tr>
<td>Queen</td>
<td>1,15,500</td>
<td>Furniture</td>
<td>35,000</td>
</tr>
<tr>
<td>King’s loan</td>
<td>77,000</td>
<td>Motor cycle</td>
<td>1,40,000</td>
</tr>
<tr>
<td>Sundry creditors</td>
<td>2,80,000</td>
<td>Stock</td>
<td>1,92,500</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>1,05,000</td>
<td>Sundry debtors</td>
<td>1,40,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Jack’s Capital A/c</td>
<td>28,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>7,45,500</td>
</tr>
</tbody>
</table>

Between the balance sheet date and the date of dissolution purchases amounted to Rs. 1,05,000 and sales Rs. 1,57,500. In addition to payments made to creditors, a sum of Rs. 42,000 and Rs. 21,000 were paid on account of salaries and general expenses.

Each partner withdrew Rs. 2,800 per month. On 31.03.2000 debtors, creditors and stock amounted to Rs. 2,10,000, Rs. 2,45,000 and Rs. 1,57,500 respectively.
In course of proceedings the partners decided to transfer the entire business to a private limited company with all assets, liabilities and partners loan for a consideration of Rs. 3,15,000. Dissolution expenses amounted to Rs. 9,800 was borne by King.

You are advised to present the Balance Sheet as at 31.03.2000 along with necessary ledger accounts of the firm viz. KQJ & Co.

**Answer :**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Sundry Debtors A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To</td>
<td>Balance b/d</td>
<td>1,40,000</td>
</tr>
<tr>
<td></td>
<td>Sales</td>
<td>1,57,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,97,500</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Sundry Creditors A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To</td>
<td>Bank</td>
<td>1,40,000</td>
</tr>
<tr>
<td></td>
<td>(balancing figure)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Balance c/d</td>
<td>2,45,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3,85,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Bank A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To</td>
<td>Sundry Debtors</td>
<td>87,500</td>
</tr>
<tr>
<td></td>
<td>Balance c/d</td>
<td>2,45,700</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Profit and Loss A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To</td>
<td>Opening Stock</td>
<td>1,92,500</td>
</tr>
<tr>
<td></td>
<td>Purchases</td>
<td>1,05,000</td>
</tr>
<tr>
<td></td>
<td>Salaries</td>
<td>42,000</td>
</tr>
<tr>
<td></td>
<td>General expenses</td>
<td>21,000</td>
</tr>
</tbody>
</table>
### Final Accounts

<table>
<thead>
<tr>
<th>To</th>
<th>Balance c/d</th>
<th>45,500</th>
<th>By</th>
<th>Net loss :</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Interest on loan</td>
<td>1,925</td>
<td></td>
<td>King</td>
</tr>
<tr>
<td></td>
<td>Queen</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Jack</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>47,425</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Note:** Profit on realisation

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total consideration</td>
</tr>
<tr>
<td>Less : Net assets</td>
</tr>
<tr>
<td>Less : Realisation expenses</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Partners’ Capital Accounts</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>King</td>
<td>Queen</td>
</tr>
<tr>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>----</td>
<td>------</td>
<td>-------</td>
</tr>
<tr>
<td>To</td>
<td>Balance c/d</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Profit &amp; Loss A/c (share of loss)</td>
<td>23,712</td>
</tr>
<tr>
<td></td>
<td>Drawings</td>
<td>8,400</td>
</tr>
<tr>
<td></td>
<td>Balance c/d</td>
<td>1,35,888</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,68,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,68,000</td>
</tr>
</tbody>
</table>

**KQJ & Co.**

### Balance Sheet as at 31-03-2000

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital A/cs :</td>
<td></td>
<td>Building</td>
<td>2,10,000</td>
</tr>
<tr>
<td>King</td>
<td>1,35,888</td>
<td>Furniture</td>
<td>35,000</td>
</tr>
<tr>
<td>Queen</td>
<td>91,292</td>
<td>Motorcycle</td>
<td>1,40,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>2,45,000</td>
<td>Stock-in-trade</td>
<td>1,57,500</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>2,45,700</td>
<td>Sundry Debtors</td>
<td>2,10,000</td>
</tr>
<tr>
<td>King’s loan A/c</td>
<td>77,000</td>
<td>Capital A/c :</td>
<td></td>
</tr>
<tr>
<td>Add : Interest on loan</td>
<td>1,925</td>
<td>78,925</td>
<td>Jack</td>
</tr>
<tr>
<td></td>
<td>7,96,805</td>
<td>7,96,805</td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Question 11:

From the information supplied below by Vinay Ventures, prepare Profit and Loss Account for the year ended 31-12-1999 and a Balance Sheet as on the date:

<table>
<thead>
<tr>
<th>Item</th>
<th>1-1-1999</th>
<th>31-12-1999</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Fixed Assets</td>
<td>1,80,000</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Stock-in-hand</td>
<td>1,40,000</td>
<td>1,90,000</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>82,000</td>
<td>48,000</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>22,000</td>
<td>80,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>?</td>
<td>2,60,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>1,20,000</td>
<td>98,000</td>
</tr>
<tr>
<td>Outstanding Expenses</td>
<td>10,000</td>
<td>6,000</td>
</tr>
</tbody>
</table>

During the year the following transactions took place:

1. Collection from Debtors and discount allowed to them Rs. 24,50,000
2. Return Inward Rs. 60,000
3. Bad Debts Rs. 10,000
4. Sales (cash and credit) Rs. 30,00,000
5. Return outward Rs. 30,000
6. Paid to suppliers by cheque Rs. 23,62,000
7. Collection from debtors and deposited into the bank Rs. 24,30,000
8. Cash Purchases Rs. 1,00,000
9. Salaries and wages paid by cheque Rs. 1,80,000
10. Miscellaneous cash expenses Rs. 50,000
11. Drawings in cash Rs. 94,000
12. Assets purchased by cheque Rs. 20,000
13. Cash withdrawals from bank Rs. 2,10,000
14. Cash sales deposited into bank Rs. ?
15. Discount received Rs. 40,000
**Final Accounts**

**Answer:**

In the Books of Vinay Ventures Limited.

Trading and Profit and Loss Account for the period ended on 31.12.1999

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount</th>
<th>Amount</th>
<th>Particulars</th>
<th>Amount</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock.</td>
<td>1,40,000</td>
<td></td>
<td>By Sales</td>
<td>4,00,000</td>
<td></td>
</tr>
<tr>
<td>&quot; Purchases :</td>
<td></td>
<td></td>
<td>Cash</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>1,00,000</td>
<td></td>
<td>Credit</td>
<td>26,00,000</td>
<td></td>
</tr>
<tr>
<td>Credit</td>
<td>24,10,000</td>
<td></td>
<td></td>
<td>30,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>25,10,000</td>
<td></td>
<td>Less : Return</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Inwards</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>By Closing stock.</td>
<td></td>
<td>29,40,000</td>
</tr>
<tr>
<td>&quot; Salary &amp; Wages.</td>
<td>1,80,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Misc. expenses.</td>
<td>46,000</td>
<td></td>
<td>By discount received</td>
<td></td>
<td>40,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(50000 + 6000 - 10000)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Discount allowed.</td>
<td>20,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Bad debt.</td>
<td>10,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot; Net Profit transferred to Capital A/c</td>
<td>2,94,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>31,70,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Balance Sheet as on 31.12.1999

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Amount</th>
<th>Amount</th>
<th>Assets</th>
<th>Amount</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Account :</td>
<td>4,74,000</td>
<td></td>
<td>Sundry assets</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>Opening balance.</td>
<td></td>
<td></td>
<td>(180000+20000)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add: Net Profit</td>
<td>2,94,000</td>
<td></td>
<td>Stock in trade</td>
<td>1,90,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,68,000</td>
<td></td>
<td>Sundry debtors</td>
<td>2,60,000</td>
<td></td>
</tr>
<tr>
<td>Less : Drawings.</td>
<td>94,000</td>
<td></td>
<td>Cash at Bank</td>
<td>80,000</td>
<td></td>
</tr>
<tr>
<td>Sundry creditors</td>
<td>98,000</td>
<td></td>
<td>Cash in hand</td>
<td>48,000</td>
<td></td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>6,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,78,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Opening Balance Sheet

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Amount</th>
<th>Amount</th>
<th>Assets</th>
<th>Amount</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>1,20,000</td>
<td></td>
<td>Sundry Assets</td>
<td>1,80,000</td>
<td></td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>10,000</td>
<td></td>
<td>Sundry debtors</td>
<td>1,80,000</td>
<td></td>
</tr>
<tr>
<td>Capital Account (balancing figure)</td>
<td>474,000</td>
<td></td>
<td>Stock in trade</td>
<td>1,40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>6,04,000</td>
<td></td>
<td>Rent</td>
<td>22,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Cash in hand</td>
<td>82,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>6,04,000</td>
</tr>
</tbody>
</table>

STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION
Financial Accounting Fundamentals

### Sundry Debtors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount</th>
<th>Particulars.</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d.</td>
<td>1,80,000</td>
<td>By Bank</td>
<td>24,30,000</td>
</tr>
<tr>
<td>balancing figure</td>
<td></td>
<td>By Discount allowed</td>
<td>20,000</td>
</tr>
<tr>
<td>To Credit sales.</td>
<td>26,00,000</td>
<td>By Return inward</td>
<td>60,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Bad debt</td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance b/d</td>
<td>2,60,000</td>
</tr>
<tr>
<td></td>
<td>27,80,000</td>
<td></td>
<td>7,80,000</td>
</tr>
</tbody>
</table>

### Sundry Creditors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount</th>
<th>Particulars.</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Bank</td>
<td>23,62,000</td>
<td>By Balance b/d</td>
<td>1,20,000</td>
</tr>
<tr>
<td>&quot; Discount</td>
<td>40,000</td>
<td>By Credit purchases</td>
<td>24,10,000</td>
</tr>
<tr>
<td>&quot; Returns</td>
<td>30,000</td>
<td>(balancing fig)</td>
<td></td>
</tr>
<tr>
<td>&quot; Balance c/d.</td>
<td>98,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>25,30,000</td>
<td></td>
<td>25,30,000</td>
</tr>
</tbody>
</table>

### Cash & Bank Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount</th>
<th>Particulars.</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d.</td>
<td>82,000</td>
<td>22,000</td>
<td>23,62,000</td>
</tr>
<tr>
<td>To Sundry Debtors</td>
<td>24,30,000</td>
<td>By Purchases</td>
<td>1,00,000</td>
</tr>
<tr>
<td>To Cash sales</td>
<td>4,00,000</td>
<td>By Salary &amp; Wages</td>
<td>1,80,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Misc. exp.</td>
<td>50,000</td>
</tr>
<tr>
<td>To Bank</td>
<td>2,10,000</td>
<td>By Drawings</td>
<td>94,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Cash</td>
<td>2,10,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Fixed Assets.</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance B/D.</td>
<td>48,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>80,000</td>
</tr>
<tr>
<td></td>
<td>2,92,000</td>
<td>28,52,000</td>
<td>2,92,000</td>
</tr>
</tbody>
</table>

**Question 12:**

Jamnadas furnishes you with the following trial balance as on 31st May, 2001:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Rs.</td>
</tr>
</tbody>
</table>

- Stock on 31.5.2000 (at cost) 35,000
- Depreciation 5,000
- Provision for depreciation — 40,000
- Fixed assets (at cost) 50,000
- Profit/loss on sale of fixed assets 8,000
- Investments at cost 1,25,000
- Profit/loss on sale of investments — 80,000
- Sale (at 20% gross profit margin) — 8,00,000
**Final Accounts**

Purchases 7,50,000 —  
Balances in customers’ accounts 1,00,000 20,000  
Balances in suppliers’ accounts 5,000 60,000  
Expenses 42,000 —  
Discount 18,000 12,000  
Commission 50,000 80,000  
Amounts due to principals — 8,000  
Amounts due from consignees 75,000 —  
Deposits with consignors 1,00,000 —  
Deposits from consignees — 1,50,000  
Cash 7,000 —  
Income on investments — 5,000  
Interest on deposits:  
with consignors — 12,000  
from consignees 18,000 —  
Prepaid/outstanding expenses:  
as on 31.5.2000 7,000 13,000  
as on 31.5.2001 9,000 6,000  
Fixed deposits with bank 2,00,000 —  
Interest on bank fixed deposit — 20,000  
Drawing/Capital 60,000 3,00,000  
Bank — 58,000  

Rs. 16,64,000 16,64,000

You find that the cost of fixed assets sold was Rs. 30,000, the accumulated depreciation up to the date of sale was Rs. 9,000.

Jammadas asks you to:

(a) Show the following ledger accounts for the year ended 31st May, 2001:
   (i) provision for depreciation
   (ii) expenses
   (iii) trading account
   (iv) profit and loss account
   (v) capital account

(b) Prepare the balance sheet as on 31st May, 2001.
Financial Accounting Fundamentals

**Answer (a):**

**In the Ledger book of JAMNADAS**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>31.5.01</td>
<td>To Assets sold A/c</td>
<td>9,000</td>
<td>1.6.00</td>
<td>By Balance b/d</td>
<td>44,000</td>
</tr>
<tr>
<td>31.5.01</td>
<td>To Balance c/f</td>
<td>40,000</td>
<td>31.5.01</td>
<td>By Depreciation A/c</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>49,000</td>
<td></td>
<td></td>
<td>49,000</td>
</tr>
</tbody>
</table>

**Opening balance is the balancing figure**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.6.00</td>
<td>To Prepaid A/c</td>
<td>7,000</td>
<td>1.6.00</td>
<td>By Outstanding liabilities A/c</td>
<td>13,000</td>
</tr>
<tr>
<td></td>
<td>To Cash/Bank A/c</td>
<td>45,000</td>
<td>31.5.01</td>
<td>By Prepaid A/c</td>
<td>9,000</td>
</tr>
<tr>
<td>31.5.01</td>
<td>By Outstanding liability A/c</td>
<td>6,000</td>
<td>31.5.01</td>
<td>By Profit &amp; Loss A/c</td>
<td>36,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>58,000</td>
<td></td>
<td></td>
<td>58,000</td>
</tr>
</tbody>
</table>

Cash/Bank A/c is the balancing figure.

**JAMNADAS**

**Trading Account for the year ended 31st May 2001**

<table>
<thead>
<tr>
<th>P.Y.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>P.Y.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>To Opening stock</td>
<td>35,000</td>
<td></td>
<td>By Sales</td>
<td>8,00,000</td>
</tr>
<tr>
<td></td>
<td>To Purchases</td>
<td>7,50,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Gross profit</td>
<td></td>
<td></td>
<td>Transferred to P &amp; L A/c</td>
<td>1,60,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Closing stock</td>
<td>1,45,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>9,45,000</td>
</tr>
</tbody>
</table>

**Profit & Loss Account for the year ended 31st May 2001**

<table>
<thead>
<tr>
<th>P.Y.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>P.Y.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>To Expenses</td>
<td>36,000</td>
<td></td>
<td>By Gross Profit b/d</td>
<td>1,60,000</td>
</tr>
<tr>
<td></td>
<td>To Discount</td>
<td>18,000</td>
<td></td>
<td>By Discount</td>
<td>12,000</td>
</tr>
<tr>
<td></td>
<td>To Interest</td>
<td>18,000</td>
<td></td>
<td>By Commission</td>
<td>80,000</td>
</tr>
<tr>
<td></td>
<td>To Loss on sale of fixed assets</td>
<td>8,000</td>
<td></td>
<td>By Interest</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Commission</td>
<td>50,000</td>
<td>(i)</td>
<td>On deposit</td>
<td>12,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(ii)</td>
<td>From bank</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td>To Depreciation</td>
<td>5,000</td>
<td></td>
<td>By Income form investment</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>To Net profit transferred to Capital A/c</td>
<td>2,34,000</td>
<td></td>
<td>By Profit on sale of investment</td>
<td>80,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3,69,000</td>
<td></td>
<td></td>
<td>3,69,000</td>
</tr>
</tbody>
</table>
**Final Accounts**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Capital A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Amount (Rs.)</td>
</tr>
<tr>
<td>31.5.00</td>
<td>To Drawings A/c</td>
<td>60,000</td>
</tr>
<tr>
<td>31.5.01</td>
<td>To Balance c/d</td>
<td>4,74,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>5,34,000</td>
</tr>
</tbody>
</table>

**Answer (b) :**

**Jamandas**

Balance Sheet *as at 31st May 2001*

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital A/c</td>
<td></td>
<td>Fixed Assets :</td>
<td></td>
</tr>
<tr>
<td>Balance as per last A/c</td>
<td>3,00,000</td>
<td>At cost</td>
<td></td>
</tr>
<tr>
<td>Add : Profit for the year</td>
<td>2,34,000</td>
<td>As per last A/c</td>
<td>80,000</td>
</tr>
<tr>
<td>Less : Drawings</td>
<td>60,000</td>
<td>Less : Cost of assets sold</td>
<td>30,000</td>
</tr>
<tr>
<td></td>
<td>4,74,000</td>
<td>Less : Depreciation</td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>As per last A/c</td>
<td>44,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Less : For assets sold</td>
<td>9,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>35,000</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>58,000</td>
<td>Add : For the year</td>
<td>5,000</td>
</tr>
<tr>
<td>Advances from consignees</td>
<td>1,50,000</td>
<td></td>
<td>40,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>94,000</td>
<td>Investments (At cost)</td>
<td>1,25,000</td>
</tr>
<tr>
<td>For goods</td>
<td>60,000</td>
<td>Current Assets</td>
<td></td>
</tr>
<tr>
<td>For expenses</td>
<td>6,000</td>
<td>Stock (At cost)</td>
<td>1,45,000</td>
</tr>
<tr>
<td>For others -</td>
<td>8,000</td>
<td>Cash-in-hand</td>
<td>7,000</td>
</tr>
<tr>
<td>Principals</td>
<td>20,000</td>
<td>Fixed deposit with bank</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Customers</td>
<td></td>
<td>— Customers</td>
<td>1,00,000</td>
</tr>
<tr>
<td></td>
<td>94,000</td>
<td>Loans &amp; Advances</td>
<td>4,52,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Amount due from</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Consignees</td>
<td>75,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Suppliers</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Deposit with consignors</td>
<td>80,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Prepaid expenses</td>
<td>1,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>9,000</td>
</tr>
<tr>
<td></td>
<td>7,76,000</td>
<td></td>
<td>7,76,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Question 13:

Vijay Stores submits you with the following information:

(a) Assets as on 31st May

<table>
<thead>
<tr>
<th></th>
<th>2001 (Rs.)</th>
<th>2000 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>4,000</td>
<td>5,000</td>
</tr>
<tr>
<td>Dues from customers</td>
<td>60,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>5,000</td>
<td>3,000</td>
</tr>
<tr>
<td>Stock at cost</td>
<td>40,000</td>
<td>35,000</td>
</tr>
<tr>
<td>Bank balance (as per pass book)</td>
<td>15,000</td>
<td>20,000</td>
</tr>
<tr>
<td>Fixed assets (cost as on 1.6.1996)</td>
<td>75,000</td>
<td>75,000</td>
</tr>
</tbody>
</table>

(b) Liabilities as on 31st May

<table>
<thead>
<tr>
<th></th>
<th>2001 (Rs.)</th>
<th>2000 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suppliers of goods</td>
<td>37,000</td>
<td>43,000</td>
</tr>
<tr>
<td>Loan from Desouza</td>
<td>—</td>
<td>25,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>3,000</td>
<td>2,000</td>
</tr>
</tbody>
</table>

(c) On checking the bank pass book, you find that:

(i) cheques received from customers on or before 31st May, but realised after 31st May, were 55,000 45,000

(ii) cheques issued by 31st May, but presented for payment to the bank after 31st May, were 23,000 27,000

(d) During the year ended 31st May, you find that:

|                                | Rs.       | Rs.       |
| (i) cash withdrawn from bank amounted to | 1,50,000   | 1,35,000   |
| of which cash taken for personal use was | 1,00,000   | 90,000     |
| (ii) cash deposited in bank out of collection from customers — cash sales | 60,000     | 55,000     |
| (iii) cash & cheques deposited in bank — collections from credit customers | 4,50,000   | 4,00,000   |
| (iv) cheques issued to suppliers amounted to | 3,00,000   | 2,80,000   |
| (v) cheques issued for expenses | 25,000     | 30,000     |
| (vi) discount allowed to customers | 7,000      | 6,000      |
| (vii) discount allowed by suppliers | 8,000      | 5,000      |
| (viii) cost of goods taken for personal use from stock | 6,000      | 4,000      |
Final Accounts

(e) The cost of fixed assets was to be written off over 10-year period under straight line method.

(f) Vijay Stores donated to Gujarat Earthquake Relief Fund by cheque Rs. 26,000.

(g) Payment made to Desouza out of personal funds was Rs. 29,500 against Rs. 4,500 similarly paid in 1999-2000.

Vijay Stores asks you to prepare:

Either,

(i) Statement of affairs as on 31st May, 2000-2001, and
(ii) Statement of profit or loss during the year ended 31st May, 2001.

Or,

(iii) Trading and profit and loss account for the year ended 31st May, 2001, and
(iv) Balance sheet as on 31st May, 2001

Show your working.

Answer:

Working Notes.


   Cost of Fixed Asset  Rs. 75,000
   Date of purchase  1.6.1996
   Depreciation Method  Straight line
   Useful Life  10 years
   Rate of Depreciation  10%
   Amount of Depreciation  Rs. 7,500

   Accumulated Depreciation upto 31.5.2000 = (Rs. 7500)×4 = Rs. 30,000
   Deprn. for the F.Y.2000-20001  Rs. 7,500
   Accumulated Deprn. upto 31.5.2001  Rs. 37,500

2. Bank Reconciliation Statement

   For the year ended 31.5.2001  31.5.2000

   Balance as per Pass Book  15,000  20,000
   Add: Cheques deposited but not credited by bank  55,000  45,000
   70,000  65,000
   Less : Cheques issued but not presented for payment  23,000  27,000
   Balance as per Book  47,000  38,000
### Alternative (i):

**Vijay Stores**

**Statement of Affairs as on 31st May 2001**

<table>
<thead>
<tr>
<th>Assets owned:</th>
<th>Current Year</th>
<th>Previous Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>4,000</td>
<td>5,000</td>
</tr>
<tr>
<td>Bank</td>
<td>47,000</td>
<td>38,000</td>
</tr>
<tr>
<td>Debtors</td>
<td>60,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Prepaid Expenses</td>
<td>5,000</td>
<td>3,000</td>
</tr>
<tr>
<td>Stock at cost</td>
<td>40,000</td>
<td>35,000</td>
</tr>
<tr>
<td><strong>Fixed Assets —</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>At cost</td>
<td>75,000</td>
<td>75,000</td>
</tr>
<tr>
<td>Less: Accumulated Deprn.</td>
<td>37,500</td>
<td>30,000</td>
</tr>
<tr>
<td><strong>Total (A)</strong></td>
<td>1,93,500</td>
<td>1,76,000</td>
</tr>
<tr>
<td>Less : Liabilities owed – Loan from De Souza</td>
<td>—</td>
<td>25,000</td>
</tr>
<tr>
<td>Creditors: for goods</td>
<td>37,000</td>
<td>43,000</td>
</tr>
<tr>
<td>for Expenses</td>
<td>3,000</td>
<td>2,000</td>
</tr>
<tr>
<td><strong>Total (B)</strong></td>
<td>40,000</td>
<td>70,000</td>
</tr>
<tr>
<td><strong>Capital (A) – (B)</strong></td>
<td>1,53,500</td>
<td>1,06,000</td>
</tr>
</tbody>
</table>

(b) Statement of Profit/Loss for the year ended 31.05.2001

| Capital at the end of the year | Rs. 1,53,500 |
| Add: Drawings during the year |               |
| Cheque                        | 1,00,000      |
| Goods                         | 6,000         |
| **Less: Business Liabilities paid out of personal funds :** | | |
| Loan from Desouza             | 25,000        |
| Interest thereon              | 4,500         |
| **Deduct: Capital at the commencement of the year** | 1,06,000 |
| **Profit earned during the year** | 1,24,000 |
Final Accounts

Alternative (ii) :

Working Note No. 1 :

Cash and Bank Abstract.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Cash</th>
<th>Bank</th>
<th>Particulars</th>
<th>Cash</th>
<th>Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Balance</td>
<td>5,000</td>
<td>38,000</td>
<td>By Drawings</td>
<td>—</td>
<td>1,00,000</td>
</tr>
<tr>
<td>To Bank (contra)</td>
<td>50,000</td>
<td></td>
<td>By Cash (contra)</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>To Cash sales</td>
<td>60,000</td>
<td></td>
<td>By Bank (contra)</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>To Cash (contra)</td>
<td>60,000</td>
<td></td>
<td>By Creditors</td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td>To Debtors</td>
<td>4,50,000</td>
<td></td>
<td>By Expenses</td>
<td>51,000</td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>By Donation</td>
<td>—</td>
<td>26,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>By Closing balance</td>
<td>4,000</td>
<td>47,000</td>
</tr>
<tr>
<td></td>
<td>1,15,000</td>
<td>5,48,000</td>
<td></td>
<td>1,15,000</td>
<td>5,48,000</td>
</tr>
</tbody>
</table>

Working Note No. 2 :

Dr. Expenses A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Prepaid A/c</td>
<td>3,000</td>
<td>By Outstanding expenses</td>
<td>2,000</td>
</tr>
<tr>
<td>To Cash</td>
<td>51,000</td>
<td>By Closing Prepaid</td>
<td>5,000</td>
</tr>
<tr>
<td>To Bank</td>
<td>25,000</td>
<td>By Profit &amp; Loss A/c</td>
<td>75,000</td>
</tr>
<tr>
<td>To Outstanding expenses</td>
<td>3,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>82,000</td>
<td></td>
<td>82,000</td>
</tr>
</tbody>
</table>

Working Note No. 3 :

Dr. Sundry Debtors A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance</td>
<td>50,000</td>
<td>By Bank</td>
<td>4,50,000</td>
</tr>
<tr>
<td>To Sales</td>
<td>4,67,000</td>
<td>By Discount</td>
<td>7,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Closing balance</td>
<td>60,000</td>
</tr>
<tr>
<td></td>
<td>5,17,000</td>
<td></td>
<td>5,17,000</td>
</tr>
</tbody>
</table>

Working Note No. 4 :

Dr. Sundry Creditors A/c Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Bank</td>
<td>3,00,000</td>
<td>By Opening balance</td>
<td>43,000</td>
</tr>
<tr>
<td>To Discount Recd.</td>
<td>8,000</td>
<td>By Purchase A/c</td>
<td>3,02,000</td>
</tr>
<tr>
<td>To Balance (Closing)</td>
<td>37,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,45,000</td>
<td></td>
<td>3,45,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Alternative (iii) :

Vijay Stores

Trading and Profit & Loss A/c for the year ended 31st May 2001

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>35,000</td>
<td>By Sales</td>
<td>60,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>3,02,000</td>
<td>Cash</td>
<td>4,67,000</td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>2,36,000</td>
<td>Credit</td>
<td>5,27,000</td>
</tr>
<tr>
<td>By Capital A/c – cost of</td>
<td>By Capital A/c – cost of goods withdrawn</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>By Closing stock</td>
<td>40,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Expenses</td>
<td>75,000</td>
<td>By Gross Profit b/d</td>
<td>2,36,000</td>
</tr>
<tr>
<td>To Discount</td>
<td>7,000</td>
<td>By Discount earned</td>
<td>8,000</td>
</tr>
<tr>
<td>To Interest</td>
<td>4,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Depreciation</td>
<td>7,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Donation</td>
<td>26,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net profit for the year</td>
<td>1,24,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>transferred to Capital A/c</td>
<td>2,44,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Alternative (iv) :

Vijay Stores

Balance Sheet as at 31st May 2001

<table>
<thead>
<tr>
<th>Capital &amp; Liabilities</th>
<th>Rs.</th>
<th>Property &amp; Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital A/c</td>
<td></td>
<td>Fixed Assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>As per last A/c</td>
<td>1,06,000</td>
<td>As cost</td>
<td>75,000</td>
<td></td>
</tr>
<tr>
<td>Add :</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1) Amt. introduced</td>
<td>29,500</td>
<td>Less : Deprn. to date</td>
<td>37,500</td>
<td>37,500</td>
</tr>
<tr>
<td>2) Net profit</td>
<td>1,24,000</td>
<td>Stock</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,59,500</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less :</td>
<td></td>
<td>Sundry debtors</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td></td>
<td>Prepaid expenses</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Cheque</td>
<td>1,00,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Goods</td>
<td>6,000</td>
<td>Cash-in-hand</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,06,000</td>
<td>Cash-at-bank</td>
<td>47,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,53,500</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>For goods</td>
<td>37,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>For expenses</td>
<td>3,000</td>
<td></td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,93,500</td>
<td></td>
<td>1,93,500</td>
<td></td>
</tr>
</tbody>
</table>
**Final Accounts**

**Question 14:**

Bhola submits the following trial balance as on 31st May, 2001:

<table>
<thead>
<tr>
<th></th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital: Opening</td>
<td></td>
<td>3,00,000</td>
</tr>
<tr>
<td>Drawings</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Fixed assets — WDV — Opening</td>
<td>70,000</td>
<td></td>
</tr>
<tr>
<td>Fixed assets — purchased during the year</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Stock on 1st June, 2000</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Purchase</td>
<td>8,00,000</td>
<td></td>
</tr>
<tr>
<td>Purchase returns</td>
<td></td>
<td>35,000</td>
</tr>
<tr>
<td>Sales</td>
<td></td>
<td>9,00,000</td>
</tr>
<tr>
<td>Sales returns</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Customers dues</td>
<td>1,25,000</td>
<td></td>
</tr>
<tr>
<td>Creditors for:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fixed assets purchased</td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td>Goods purchased</td>
<td></td>
<td>1,00,000</td>
</tr>
<tr>
<td>Expenses</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Fixed deposit with bank</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Interest on bank fixed deposit</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td></td>
<td>4,000</td>
</tr>
<tr>
<td>Bank balance in current account</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Suspense (difference in trial balance)</td>
<td></td>
<td>1,000</td>
</tr>
</tbody>
</table>

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Rs. 13,60,000</td>
</tr>
</tbody>
</table>

Bhola informs you that:

(a) Stock on 31.5.2001 is worth Rs.60,000 at sales price and Rs.50,000 at cost price.

(b) Depreciation of Rs. 9,000 is to be provided for the year.

Bhola asks you to check up his books and pass necessary entries to correct the mistakes (if any).

On your checking you find that:

(i) A sum of Rs. 10,000 drawn from the bank on 1.1.2001 was debited to drawings account in full although Rs. 6,000 out of the said withdrawal was used in the business for meeting day to day expenses and payment, which were also entered in the cash book.

(ii) Purchases of goods worth Rs. 8,000 made on 28th May, 2001 was not recorded in the books; although the sale thereof on 30th May, 2001 at Rs. 9,000 was properly recorded.

(iii) Purchase returns of Rs. 500 was recorded through sales returns journal. However the posting to the Party’s account in the ledger was for the correct amount and on the correct side.

(iv) Expenses paid include Rs. 3,000 in respect of period after 31st May, 2001.

Bhola wants you to prepare his final accounts for the year ended 31st May, 2001.
Financial Accounting Fundamentals

Answer:

Note: Entries passed in the books in respect of Item Nos. (i) and (iii)

Re: Item No. (i)

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>10,000</td>
</tr>
<tr>
<td>To Bank</td>
<td>10,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Drawings</td>
<td>10,000</td>
</tr>
<tr>
<td>Expenses</td>
<td>6,000</td>
</tr>
<tr>
<td>To Cash</td>
<td>16,000</td>
</tr>
</tbody>
</table>

Thus there was a negative cash balance of Rs. 6,000

Re: Item No. (iii)

In this case purchase returns were passed through sales return. The effect of this was instead of crediting the Purchase Returns the same was debited to Sales Return. In the result there was a difference of Rs. 1000 which was shown in the trial balance under the head Suspense A/c.

Rectification Entries to be passed

Re: Item No. (I)

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>6000</td>
</tr>
<tr>
<td>To Drawings</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being rectification of debit given on 01-01-2001 to Drawings A/c as it is overstated by Rs. 6000, actual drawing being Rs. 4000)</td>
</tr>
</tbody>
</table>

Re: Item No. 2

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase</td>
<td>8000</td>
</tr>
<tr>
<td>To Suppliers</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being the passed to record the purchase on 28.5.2001)</td>
</tr>
</tbody>
</table>

Re: Item No. 3

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Suspense</td>
<td>1000</td>
</tr>
<tr>
<td>To Purchase Returns</td>
<td></td>
</tr>
<tr>
<td>To Sales Returns</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being rectification of Purchase Return wrongly entered in the Sales Return Day Book)</td>
</tr>
</tbody>
</table>

Re: Item No. 4

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prepaid Expenses</td>
<td>3000</td>
</tr>
<tr>
<td>To Expenses</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being prepaid expenses wrongly debited to expenses A/c)</td>
</tr>
</tbody>
</table>
Final Accounts

Working Note No. 2 : Effect of Entries in the Final A/cs

<table>
<thead>
<tr>
<th></th>
<th>As per Trial Balance</th>
<th>Adjustment</th>
<th>Adjusted figures</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Drawings</td>
<td>Dr Rs.10,000</td>
<td>Cr 6,000</td>
<td>Dr 4,000</td>
</tr>
<tr>
<td>2. Cash</td>
<td>Cr 4,000</td>
<td>Dr 6,000</td>
<td>Dr 2,000</td>
</tr>
<tr>
<td>3. Purchase</td>
<td>Dr 8,00,000</td>
<td>Dr 8,000</td>
<td>Dr 8,08,000</td>
</tr>
<tr>
<td>4. Suppliers</td>
<td>Cr 1,00,000</td>
<td>Cr 8,000</td>
<td>Cr 1,08,000</td>
</tr>
<tr>
<td>5. Purchase Returns</td>
<td>Cr 35,000</td>
<td>Cr 500</td>
<td>Cr 35,500</td>
</tr>
<tr>
<td>6. Sales Returns</td>
<td>Dr 50,000</td>
<td>Cr 500</td>
<td>Dr 49,500</td>
</tr>
<tr>
<td>7. Suspense</td>
<td>Cr 1,000</td>
<td>Dr 1,000</td>
<td>—</td>
</tr>
<tr>
<td>8. Expenses</td>
<td>Dr 25,000</td>
<td>Cr 3,000</td>
<td>Dr 22,000</td>
</tr>
<tr>
<td>9. Prepaid Expenses</td>
<td>Dr —</td>
<td>Dr 3,000</td>
<td>Dr 3,000</td>
</tr>
</tbody>
</table>

Bhola

Trading and Profit & Loss Account for the year ended 31.05.2001

<table>
<thead>
<tr>
<th></th>
<th>To Opening Stock 30,000</th>
<th>By Sales 9,00,000</th>
<th>Less: Returns 49,500</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less: Returns</td>
<td>35,500</td>
<td>7,72,500</td>
<td>50,000</td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>98,000</td>
<td></td>
<td>90,050</td>
</tr>
<tr>
<td>Total</td>
<td>90,050</td>
<td></td>
<td>90,050</td>
</tr>
<tr>
<td>To Expenses</td>
<td>22,000</td>
<td>By Gross Profit b/d 98,000</td>
<td></td>
</tr>
<tr>
<td>To Depreciation</td>
<td>9,000</td>
<td>By Interest on Bank Deposit 10,000</td>
<td></td>
</tr>
<tr>
<td>To Net Profit transferred to Capital A/c</td>
<td>77,000</td>
<td>1,08,000</td>
<td></td>
</tr>
</tbody>
</table>

BHOLA

Balance Sheet as at 31st May, 2001

<table>
<thead>
<tr>
<th></th>
<th>Sundry Creditors 1,18,000</th>
<th>Cash 2,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>For Goods</td>
<td>1,08,000</td>
<td>Bank-Current A/c 50,000</td>
</tr>
<tr>
<td>For Others</td>
<td>10,000</td>
<td>Fixed Deposit with Bank 1,00,000</td>
</tr>
<tr>
<td></td>
<td>1,18,000</td>
<td>Stock (At Cost) 50,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>1,25,000</td>
<td></td>
</tr>
<tr>
<td>Prepaid Expenses</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>3,23,000</td>
<td>Fixed Assets :</td>
</tr>
<tr>
<td>As per Last A/c</td>
<td>3,00,000</td>
<td>Opening WDV 70,000</td>
</tr>
<tr>
<td>Add : Profit for the year</td>
<td>77,000</td>
<td>Addition during the year 50,000</td>
</tr>
<tr>
<td></td>
<td>3,77,000</td>
<td>1,20,000</td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>54,000</td>
<td>Less: Depreciation 9,000</td>
</tr>
<tr>
<td></td>
<td>3,23,000</td>
<td>1,11,000</td>
</tr>
<tr>
<td>Total</td>
<td>4,41,000</td>
<td>Total 4,41,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Question 15:

On 31st March, 2001 James owned

(i) a shop which had cost him Rs. 40,000;
(ii) furniture and fittings whose cost was Rs. 30,000 and on which depreciation of Rs. 28,000 was provided over the last 28 years;
(iii) a delivery van which had cost him Rs. 150,000 on which depreciation of Rs. 120,000 was provided over the last 8 years;
(iv) An inventory which cost him Rs. 13,000 and which was expected to be sold for Rs. 15,000.

As on that date :

(a) his customers owed him Rs. 40,000;
(b) his unpaid suppliers for goods amounted to Rs. 15,000;
(c) he had given advance of Rs. 8,000 to his suppliers against orders to be executed after March 31, 2001;
(d) he had received advance of Rs. 11,000 from his customers against orders to be executed after March 31, 2001;
(e) expenses already paid for the period after March, 2001 were –
   (i) insurance for the year to end on 31st January, 2002 at Rs. 600 per month,
   (ii) subscription to periodicals for the year to end on June 30, 2001 at Rs. 30 per month;
(f) expenses incurred during the year ended March 31, 2001 but not yet paid amounted to Rs. 2,000;
(g) he had Rs. 1,300 in his cash box; fixed deposit of Rs. 100,000 with Union Bank of India carrying interest at 10% per annum payable on 31st December and 31st March every year; the bank owed him Rs. 3,000 in his business cash credit account. The cash credit account had drawing power of 80% of the amount of fixed deposit;
(h) during the year ended March 31, 2001 James had withdrawn Rs. 48,000 for personal use and had earned a net profit of Rs. 63,390.

James asks you to –

(i) prepare the balance sheet as at March 31, 2001
(ii) open his accounts for the year starting on April, 2001.
**Final Accounts**

**Answer:**

**i)**

**James**

**Balance sheet** as at March 31, 2001

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry creditors for:</td>
<td></td>
<td></td>
<td>Cash and bank balances:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Goods</td>
<td>15,000</td>
<td></td>
<td>Cash</td>
<td>1,300</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Services</td>
<td>2,000</td>
<td></td>
<td>Balance with union</td>
<td>17,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Advance from customers</td>
<td>11,000</td>
<td></td>
<td>Bank of India in</td>
<td>1,04,300</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening balance</td>
<td>2,00,000</td>
<td></td>
<td>Customer’s dues</td>
<td>40,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net profit</td>
<td>63,390</td>
<td></td>
<td>Advance to suppliers of:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,63,390</td>
<td></td>
<td>Goods</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less : Drawings</td>
<td>48,000</td>
<td></td>
<td>Prepaid expenses ::</td>
<td>2,15,390</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Inventory at cost</td>
<td>6,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Delivery van cost</td>
<td>1,50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less : Provision for depreciation</td>
<td>1,20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Furniture and fittings at cost</td>
<td>30,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less : Provision for depreciation</td>
<td>28,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Shop at cost</td>
<td>40,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>243,390</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**ii)**

**James** Ledger for 2001-2002

**Sundry creditors for goods**

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td></td>
<td>Opening balance</td>
<td>15,000</td>
</tr>
</tbody>
</table>

**Sundry creditors for services**

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td></td>
<td>Opening balance</td>
<td>2,000</td>
</tr>
</tbody>
</table>
**Financial Accounting Fundamentals**

### Advance from customers

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>11,000</td>
<td></td>
</tr>
</tbody>
</table>

### Capital

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>215,390</td>
<td></td>
</tr>
</tbody>
</table>

### Cash

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>1,300</td>
<td></td>
</tr>
</tbody>
</table>

### Union Bank of India – Cash Credit A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>3,000</td>
<td></td>
</tr>
</tbody>
</table>

### Fixed deposit with Union Bank of India

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>100,000</td>
<td></td>
</tr>
</tbody>
</table>

### Customer’s A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>40,000</td>
<td></td>
</tr>
</tbody>
</table>

### Advance to suppliers of Goods

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>8,000</td>
<td></td>
</tr>
</tbody>
</table>

### Advance to suppliers of services of Insurance & Periodicals

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance Insurance</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Periodicals</td>
<td>90</td>
<td></td>
</tr>
</tbody>
</table>

### Inventory

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>13,000</td>
<td></td>
</tr>
</tbody>
</table>
Final Accounts

Delivery van

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>1,50,000</td>
<td></td>
</tr>
</tbody>
</table>

Furniture and Fittings

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>30,000</td>
<td></td>
</tr>
</tbody>
</table>

Shop

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>40,000</td>
<td></td>
</tr>
</tbody>
</table>

Provision for depreciation on Delivery van

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>1,20,000</td>
<td></td>
</tr>
</tbody>
</table>

Furniture and fittings

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4-2001</td>
<td>Opening balance</td>
<td>28,000</td>
<td></td>
</tr>
</tbody>
</table>

Question 16:

Mr. Reddy, a retired Government Officer who started business as Stationery Merchant in Pune on 1st April 1994, gives you the following balances relating to the year ending 31st March, 2002. He also acts as a selling agent of Mr. Sharma and for this he is given a commission at the rate of 10% on sales.

Trial Balance as at 31.03.2002

<table>
<thead>
<tr>
<th>Debit Balance</th>
<th>Credit Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening stock</td>
<td>Rs. 80,000</td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>Rs. 1,75,000</td>
</tr>
<tr>
<td>Furniture and fittings</td>
<td>36,000</td>
</tr>
<tr>
<td>Bills receivable</td>
<td>Rs. 40,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>Rs. 5,20,000</td>
</tr>
<tr>
<td>Wages</td>
<td>Rs. 5,000</td>
</tr>
<tr>
<td>Salaries</td>
<td>Rs. 25,000</td>
</tr>
<tr>
<td>Sales return</td>
<td>Rs. 3,000</td>
</tr>
<tr>
<td>Printing and advertising</td>
<td>12,000</td>
</tr>
<tr>
<td>Postage</td>
<td>Rs. 4,500</td>
</tr>
<tr>
<td>Sales</td>
<td>Rs. 7,65,000</td>
</tr>
<tr>
<td>Capital</td>
<td>Rs. 1,90,000</td>
</tr>
<tr>
<td>Purchase return</td>
<td>Rs. 2,000</td>
</tr>
<tr>
<td>Discount received</td>
<td>Rs. 2,000</td>
</tr>
<tr>
<td>Sundry creditors</td>
<td>Rs. 73,64C</td>
</tr>
<tr>
<td>Consignor’s balance (01.04.01)</td>
<td>30,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Discount allowed 2,500  
Building rent 9,600  
Insurance 1,040  
Other trade expenses 10,000  
Cash sent to consignor 75,000  
Suspense account 3,000  
Drawings 15,000  
Cash in hand 10,000  
Balance with scheduled bank in current account 11,000  
In fixed deposit account 25,000  
10,62,640 10,62,640

Additional information:

1. Stock on 31.03.2002 valued at cost Rs. 64,000.
2. Business is carried on in a rented house. The ground floor, 50% of the accommodation, is used for business. Mr. Reddy lives with his family on the first floor.
3. The effect of advertising is expected to last for coming year also and as such half of printing and advertising is to be carried forward.
4. Provide depreciation on furniture and fittings @ 10% p.a.
5. A cheque of Rs. 5,000 received from a customer was returned dishonoured by bank but the same has not been recorded in the books. The customer has become insolvent and 60% is expected to be realized from his estate.
6. Furniture appearing in the books on 01.04.01 at Rs. 6,000 was disposed off on 30.09.01 at Rs. 3,500 in part exchange for a new furniture costing Rs. 5,000. A net invoice for Rs. 1,500 was passed through purchase day book.
7. Sales include Rs. 75,000 for goods sold in cash on behalf of Mr. Sharma. Trade expenses also include Rs. 4,000 as expenses in connection with this sale.
8. Suspense account represents money advanced to Sales Manager who was sent to Delhi in August 2001, for sales promotion. On returning to Pune, he submitted a statement disclosing that Rs. 1,200 was incurred for travelling, Rs. 500 for legal expenses and Rs. 900 for miscellaneous expenses. The balance lying with him is yet to be refunded.
9. Insurance premium covers a period of one month advance.
10. Opening stock has been valued at 20% below cost but final accounts should be prepared by taking stock at cost.

Prepare Mr. Reddy's Trading and Profit and Loss Account for the year ended 31st March 2002 and a Balance Sheet as on that date after taking into consideration the above mentioned information.
Answer:

Workings Notes.

(1) Valuation of opening stock 80000 × 100/80 = Rs.100000

(2) Net invoice of furniture Rs.(5000 – 3500) i.e 1500 passed through purchase day book. Rs.

(3) Cheque dishonoured by customer 5,000
   Less: 60% expected realisation from estate 3,000
   Provision for bad & doubtful debt 2,000

(4) Book value of furniture on 1.04.01 - 6,000
   Less: Depreciation from 1.04.01 to 30.09.01 300
   W.D.V as on 30.09.01 5,700
   Less: Sale value of furniture 3,500
   Loss on sale of furniture 2,200

(5) Depreciation on furniture
   Furniture & fittings as per Trial Balance as 31-03-02 36,000
   Less: Book value of furniture sold on 30.09.01 6,000
   Value of old furniture & fittings 30,000
   Depreciation on old furniture @ 10% of Rs.30000 3,000
   Depreciation on furniture sold for 6 months @ 10% on Rs.6000 300
   Depreciation on new furniture for 6 months @ 10% on Rs.5000 250
   3,550

(6) Insurance for 13 months
   Prepaid Rent = 1040/13 80

(7) Advanced to sales manager shown as suspense account 3,000
   Less: Expense Sheet submitted
   Travelling 1,200
   Legal expenses 500
   Misc. expenses 900
   2,600
   Balance suspense A/c as on 31-03-02 400

(8) Consignors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash sent</td>
<td>75,000</td>
<td>To Balance c/d</td>
<td>18,500</td>
</tr>
<tr>
<td>To Expenses</td>
<td>4,000</td>
<td>To Consignment sales</td>
<td>75,000</td>
</tr>
<tr>
<td>To Commission</td>
<td>7,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>105,000</td>
<td></td>
<td>105,000</td>
</tr>
</tbody>
</table>
### Financial Accounting Fundamentals

#### In the Books of Mr. Reddy

**Trading and Profit and Loss account** for the year ended 31-03-02

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount (Rs)</th>
<th>Amount (Rs)</th>
<th>Amount (Rs)</th>
<th>Particulars</th>
<th>Amount (Rs)</th>
<th>Amount (Rs)</th>
<th>Amount (Rs)</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td></td>
<td></td>
<td></td>
<td>By Sales</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Note 1)</td>
<td>100,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Purchases</td>
<td>520,000</td>
<td></td>
<td></td>
<td>Less: Returns</td>
<td></td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>Less: Purchase of furniture</td>
<td></td>
<td></td>
<td></td>
<td>On behalf of consignor</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Note 2)</td>
<td>1,500</td>
<td>3,500</td>
<td>516,500</td>
<td>By Closing stock</td>
<td></td>
<td></td>
<td>64,000</td>
</tr>
<tr>
<td>Less: Returns</td>
<td>2,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Wages</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Gross profit c/d</td>
<td>129,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>751,000</td>
</tr>
<tr>
<td>To Salaries</td>
<td>25,000</td>
<td></td>
<td></td>
<td>By Gross profit c/d</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Printing &amp; Adv.</td>
<td></td>
<td>12,000</td>
<td></td>
<td>b/d</td>
<td></td>
<td></td>
<td>129,500</td>
</tr>
<tr>
<td>Less: Pre-paid</td>
<td></td>
<td>6,000</td>
<td></td>
<td>By Discount</td>
<td></td>
<td></td>
<td>2,000</td>
</tr>
<tr>
<td>To Postage</td>
<td></td>
<td></td>
<td></td>
<td>By Comm.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Disc. Allowed</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Trade Expenses</td>
<td></td>
<td></td>
<td></td>
<td>By Consignment</td>
<td></td>
<td></td>
<td>7,500</td>
</tr>
<tr>
<td>Less: Expns. for Consignment</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Provn for bad &amp; doubtful debts</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Note 3)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Loss on sale of furniture</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Note 4)</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Depn. on furniture</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Note 5)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Rent</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Drawings</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Insurance</td>
<td></td>
<td>9,600</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Prepaid</td>
<td></td>
<td>1,040</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Note 6)</td>
<td></td>
<td>80</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>960</td>
</tr>
<tr>
<td>To Travelling &amp; Conveyance</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Legal Expenses</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Misc. Expenses</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net profit trfd. to Capital A/c</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>78,890</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>139,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>139,000</td>
</tr>
</tbody>
</table>
### Final Accounts

#### Balance Sheet as at 31-03-02

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Amount (Rs.)</th>
<th>Amount (Rs.)</th>
<th>Assets</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital A/c opening bal.</td>
<td>190,000</td>
<td></td>
<td>Furniture &amp; Fittings (old)</td>
<td>36,000</td>
</tr>
<tr>
<td>Add: Understatement</td>
<td></td>
<td></td>
<td>Less: Furniture sold</td>
<td>6,000</td>
</tr>
<tr>
<td>of Net Profit in last yr</td>
<td></td>
<td></td>
<td>Less: Deprn. @ 10%</td>
<td>3,000</td>
</tr>
<tr>
<td>due to undervaluation</td>
<td>20,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Closing stock</td>
<td>210,000</td>
<td></td>
<td>Add: New furniture purchased</td>
<td>5,000</td>
</tr>
<tr>
<td>Add: Profit for the year</td>
<td>78,890</td>
<td></td>
<td></td>
<td>32,000</td>
</tr>
<tr>
<td></td>
<td>288,890</td>
<td></td>
<td>Less: Deprn. For 6 mths @ 10%</td>
<td>250</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>31,750</td>
</tr>
<tr>
<td>Less: Drawings</td>
<td></td>
<td></td>
<td>Sundry debtors</td>
<td>175,000</td>
</tr>
<tr>
<td>Cash</td>
<td>15,000</td>
<td></td>
<td>Add: Cheque dishonoured</td>
<td>5,000</td>
</tr>
<tr>
<td>Rent</td>
<td>4,800</td>
<td>19,800</td>
<td>269,090</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less: Pro. for bad debt</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>178,000</td>
</tr>
<tr>
<td>Bills Receivables</td>
<td></td>
<td></td>
<td></td>
<td>40,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>73,640</td>
<td></td>
<td>Closing Stock</td>
<td>64,000</td>
</tr>
<tr>
<td>Consignors Balance (Note 8)</td>
<td>18,500</td>
<td></td>
<td>Cash at Bank</td>
<td>11,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less: Cheque dishonoured</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>6,000</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>10,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prepaid Expenses</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Printing &amp; Advt.</td>
<td></td>
<td></td>
<td></td>
<td>6,000</td>
</tr>
<tr>
<td>Insurance</td>
<td></td>
<td></td>
<td></td>
<td>80</td>
</tr>
<tr>
<td>Sales Managers</td>
<td></td>
<td></td>
<td></td>
<td>6,080</td>
</tr>
<tr>
<td>Suspenses A/c (Note 7)</td>
<td></td>
<td></td>
<td></td>
<td>400</td>
</tr>
<tr>
<td></td>
<td>361,230</td>
<td></td>
<td></td>
<td>361,230</td>
</tr>
</tbody>
</table>

#### Question 17:

The following is the Trial Balance extracted from the Books of Halder & Co. as at 31.12.96. You are asked to prepare the Trading A/c and Profit & Loss A/c for the year ended on 31st December, 1996 and a Balance Sheet as at that date taking into consideration the following:

- Closing Stock has been valued at Rs. 38,000.
- Outstanding Wages Rs. 200.
- Prepaid Rates and Taxes Rs. 25
- Depreciate Buildings @ 2.5%, Machinery @ 5% and Loose Tools @ 25% p.a.
- Adjust the provision for doubtful Debts @ 5% on Debtors and make a provision for discount on Debtors @ 5%.
- Make a Provision for Discount on Creditors @ 5%.
- Allow 5% p.a. interest on capital and charge 4% p.a. interest on Drawings.
- Interest on Investment received in advance Rs. 20.
- Misc. Receipts accrued due but not received Rs. 10.
### Trial Balance as at 31st December, 1996

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr. Amt.</th>
<th>Cr. Amt.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Capital A/c of Mr. Halder</td>
<td>—</td>
<td>16,000</td>
</tr>
<tr>
<td>Drawings A/c</td>
<td>600</td>
<td>—</td>
</tr>
<tr>
<td>Building</td>
<td>25,000</td>
<td>—</td>
</tr>
<tr>
<td>Machinery</td>
<td>8,000</td>
<td>—</td>
</tr>
<tr>
<td>Furniture and Fittings</td>
<td>2,000</td>
<td>—</td>
</tr>
<tr>
<td>Goodwill</td>
<td>8,000</td>
<td>—</td>
</tr>
<tr>
<td>Stock (01.01.96)</td>
<td>5,500</td>
<td>—</td>
</tr>
<tr>
<td>Purchases</td>
<td>28,600</td>
<td>—</td>
</tr>
<tr>
<td>Carriage Inward</td>
<td>300</td>
<td>—</td>
</tr>
<tr>
<td>Sales</td>
<td>—</td>
<td>59,800</td>
</tr>
<tr>
<td>Returns</td>
<td>250</td>
<td>135</td>
</tr>
<tr>
<td>Carriage outward</td>
<td>100</td>
<td>—</td>
</tr>
<tr>
<td>Wages</td>
<td>4,300</td>
<td>—</td>
</tr>
<tr>
<td>Motive Power</td>
<td>230</td>
<td>—</td>
</tr>
<tr>
<td>Salaries</td>
<td>1,300</td>
<td>—</td>
</tr>
<tr>
<td>Rent, Rates &amp; Taxes</td>
<td>340</td>
<td>—</td>
</tr>
<tr>
<td>Apprenticeship Premium (for the year)</td>
<td>—</td>
<td>200</td>
</tr>
<tr>
<td>Insurance</td>
<td>50</td>
<td>—</td>
</tr>
<tr>
<td>Advertisement</td>
<td>500</td>
<td>—</td>
</tr>
<tr>
<td>Printings and Stationery</td>
<td>45</td>
<td>—</td>
</tr>
<tr>
<td>Bad Debt</td>
<td>100</td>
<td>—</td>
</tr>
<tr>
<td>Discounts</td>
<td>130</td>
<td>160</td>
</tr>
<tr>
<td>Miscellaneous Receipts</td>
<td>—</td>
<td>300</td>
</tr>
<tr>
<td>Investments</td>
<td>3,000</td>
<td>—</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>2,000</td>
<td>—</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>—</td>
<td>5,000</td>
</tr>
<tr>
<td>Loose Tools</td>
<td>1,000</td>
<td>—</td>
</tr>
<tr>
<td>Loan</td>
<td>—</td>
<td>7,400</td>
</tr>
<tr>
<td>Interest on Loan</td>
<td>370</td>
<td>—</td>
</tr>
<tr>
<td>Interest on Investments</td>
<td>—</td>
<td>150</td>
</tr>
<tr>
<td>Provision for Doubtful Debts</td>
<td>—</td>
<td>140</td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>—</td>
<td>2,500</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>70</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>91,785</td>
<td>91,785</td>
</tr>
</tbody>
</table>
Final Accounts

**Answer:**

**HALDER & CO.**

**Trading Account for the year ended on 31st December, 1996**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Stock</td>
<td>5,500</td>
<td>By</td>
<td>Sales</td>
<td>59,800</td>
<td></td>
</tr>
<tr>
<td>To Purchase</td>
<td>28,600</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Less : Return</strong></td>
<td>135</td>
<td>28,465</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Carriage Inward</td>
<td>300</td>
<td>By</td>
<td>Stock (closing)</td>
<td>38,000</td>
<td></td>
</tr>
<tr>
<td>To Wages</td>
<td>4,300</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Add : Outstanding</strong></td>
<td>200</td>
<td>4,500</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Motive Power</td>
<td></td>
<td></td>
<td></td>
<td>230</td>
<td></td>
</tr>
<tr>
<td>To Profit &amp; Loss A/c</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Gross Profit transferred)</td>
<td>58,555</td>
<td></td>
<td></td>
<td>97,550</td>
<td>97,550</td>
</tr>
</tbody>
</table>

**Halder & Co.**

**Profit & Loss Account for the year ended on 31st December, 1996**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Carriage Outward</td>
<td>100</td>
<td>By</td>
<td>Trading A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Salaries</td>
<td>1,300</td>
<td>—</td>
<td>Gross Profit</td>
<td>58,555</td>
<td></td>
</tr>
<tr>
<td>To Rent, Rates &amp; Taxes</td>
<td>340</td>
<td>By</td>
<td>Apprenticeship Premium A/c</td>
<td>200</td>
<td></td>
</tr>
<tr>
<td><strong>Less : Prepaid</strong></td>
<td>25</td>
<td>315</td>
<td>By Discount received</td>
<td>160</td>
<td></td>
</tr>
<tr>
<td>To Insurance</td>
<td>50</td>
<td>By</td>
<td>Misc. Receipts</td>
<td>300</td>
<td></td>
</tr>
<tr>
<td>To Advertisement</td>
<td>500</td>
<td><em>Add :</em></td>
<td></td>
<td>10</td>
<td>310</td>
</tr>
<tr>
<td>To Printing &amp; Stationery</td>
<td>45</td>
<td>By</td>
<td>Interest on</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Bad Debt</td>
<td>100</td>
<td></td>
<td>Investment</td>
<td>150</td>
<td></td>
</tr>
<tr>
<td>To Discount (allowed)</td>
<td>130</td>
<td><em>Less :</em></td>
<td>Received in</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest on Loan</td>
<td>370</td>
<td></td>
<td>advance</td>
<td>20</td>
<td>130</td>
</tr>
<tr>
<td>To Depreciation :</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Building @ 231%</td>
<td>625</td>
<td>By Provision for Doubtful Debts :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Machinery @ 5%</td>
<td>400</td>
<td>Old Provision</td>
<td>140</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Less : New Provision</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loose Tools @ 25%</td>
<td>250</td>
<td>1,275</td>
<td>@ 5% on Rs.2000</td>
<td>100</td>
<td>40</td>
</tr>
<tr>
<td>To Provision for Discount @ 5% on Debtors on (2000–100)</td>
<td>95</td>
<td>By Provision for</td>
<td>discount on Creditors</td>
<td>250</td>
<td></td>
</tr>
<tr>
<td>To Interest on Capital @ 5%</td>
<td>800</td>
<td>By Interest on drawings @ 4%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Capital A/c</td>
<td>54,577</td>
<td></td>
<td>(for 6 months on average)</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td></td>
<td>59,657</td>
<td></td>
<td></td>
<td>59,657</td>
<td></td>
</tr>
</tbody>
</table>
### Balance Sheet as at 31st December, 1996

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital A/c : Building</td>
<td>25,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening balance</td>
<td>16,000</td>
<td>Less : Depreciation @ 2.5%</td>
<td>625</td>
</tr>
<tr>
<td>Add : Net Profit</td>
<td>54,577</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add : Interest on Capital</td>
<td>800</td>
<td>Machinery</td>
<td>8,000</td>
</tr>
<tr>
<td>Less : Drawings</td>
<td>71,377</td>
<td>Less : Depreciation @ 5%</td>
<td>400</td>
</tr>
<tr>
<td>Loan A/c</td>
<td>7,400</td>
<td>Stock (closing)</td>
<td>38,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>5,000</td>
<td>Sundry Debtors</td>
<td>2,000</td>
</tr>
<tr>
<td>Less : Provision for</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>discount @ 5%</td>
<td>250</td>
<td>Less : Provision for</td>
<td>10c</td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>2,500</td>
<td>doubtful Debts</td>
<td></td>
</tr>
<tr>
<td>Outstanding Wages</td>
<td>200</td>
<td>@ 5%</td>
<td>1,90c</td>
</tr>
<tr>
<td>Interest received in advance</td>
<td>20</td>
<td>Less : Prov. for discount</td>
<td>95</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash in hand</td>
<td>70</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Accrued Misc. Receipts</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Prepaid Rates and Taxes</td>
<td>25</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>85,635</td>
</tr>
</tbody>
</table>

#### Question 18:

Prepare the final accounts from the following information:

Mr. T. Dutta is the proprietor of a large business of Silk Piece Goods. The following Trial Balance is prepared from his books as on 31.03.97.

<table>
<thead>
<tr>
<th>Debit Balance</th>
<th>Rs.</th>
<th>Credit Balance</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land &amp; Building</td>
<td>40,000</td>
<td>Sales</td>
<td>4,68,100</td>
</tr>
<tr>
<td>Purchases</td>
<td>3,26,700</td>
<td>Income from investment</td>
<td>990</td>
</tr>
<tr>
<td>Return Inward</td>
<td>2,500</td>
<td>12% Bank Loan</td>
<td></td>
</tr>
<tr>
<td>Travelling Expenses</td>
<td>6,900</td>
<td>secured on Fixed Assets</td>
<td>40,000</td>
</tr>
<tr>
<td>Printing &amp; Stationery</td>
<td>1,600</td>
<td>(no movements during the year)</td>
<td></td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>30,795</td>
<td>Capital A/c</td>
<td>80,000</td>
</tr>
<tr>
<td>Discount Allowed</td>
<td>1,800</td>
<td>Sundry Creditors</td>
<td>63,100</td>
</tr>
<tr>
<td>Misc. Expenses</td>
<td>18,620</td>
<td>Bills Payable</td>
<td>2,600</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>64,000</td>
<td>Returns Outward</td>
<td>3,700</td>
</tr>
<tr>
<td>Postage</td>
<td>800</td>
<td>Discount Received</td>
<td>1,200</td>
</tr>
<tr>
<td>Furniture</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Final Accounts

Cash in hand 5,900
Motor Car 16,000
Investment 12,000
Drawings 10,000
Bills Receivable 4,800
Stock (1.4.96) 63,680
Interest on Bank Loan 3,000
Salaries (Including an
advance of Rs. 1, 500) 22,000
Carriage Inwards 3,000
Establishment Expenses 1,595
Advertisement 16,000

6,59,690 6,59,690

a) Stock as on 31.03.97 was Rs. 1,20,000,
b) Sundry Debtors include a sum of Rs. 3,000 due from Mr. B. and Sundry Creditors include a sum of Rs. 4,000 due to Mr. B.
c) The Reserve for Doubtful Debts is to be maintained @ 10% on Sundry Debtors and Reserve for Discount on Debtors and Discount on Creditors are to be created @ 5%.
d) Bills Receivable include dishonoured bill for Rs. 600.
e) Stock worth Rs. 10,000 was destroyed by Fire in respect of which the Insurance Company admits a claim for only Rs. 7, 500.

f) The Manager of Mr. T. Dutta is entitled to a Commission of 10% of Net Profit calculated after charging such Commission.
g) 3/4th of the advertisement expenses are to be carried forward.
h) 2.5% of the Net Profit is to be transferred to Reserve Fund.

i) Depreciation is to be charged on --
   (i) Land & Building @ 2.5 %;
   (ii) Furniture @ 10% ; and
   (iii) Motor Car @ 20%
**Financial Accounting Fundamentals**

**Answer:**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Trading Account for the year ended 31.03.1997</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To Opening Stock</td>
<td>63,680</td>
<td>By Sales</td>
</tr>
<tr>
<td>To Purchases</td>
<td>3,26,700</td>
<td>Less : Returns</td>
</tr>
<tr>
<td>less : Returns</td>
<td>3,700</td>
<td>By Closing Stock</td>
</tr>
<tr>
<td>To Carriage Inwards</td>
<td>3,000</td>
<td>By Stock Destroyed on fire</td>
</tr>
<tr>
<td>To Gross Profit (transferred to Profit &amp; Loss A/c)</td>
<td>2,05,920</td>
<td></td>
</tr>
<tr>
<td></td>
<td>5,95,600</td>
<td>5,95,600</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Profit &amp; Loss A/c for the year ended 31.03.1997</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To Travelling Expenses</td>
<td>6,900</td>
<td>By Gross Profit (Transferred)</td>
</tr>
<tr>
<td>To Printing &amp; Stationary</td>
<td>1,600</td>
<td>from Trading A/c</td>
</tr>
<tr>
<td>To Discount allowed</td>
<td>1,800</td>
<td>By Income on Investment</td>
</tr>
<tr>
<td>To Misc. Expenses</td>
<td>18,620</td>
<td>By Discount Received</td>
</tr>
<tr>
<td>To Postage</td>
<td>800</td>
<td>By Discount on</td>
</tr>
<tr>
<td>To Interest on Bank Loan</td>
<td>3,000</td>
<td>Creditors (New)</td>
</tr>
<tr>
<td>Add : Due [(40,000×12%)-3000]</td>
<td>1,800</td>
<td>4,800</td>
</tr>
<tr>
<td>To Salaries</td>
<td>22,000</td>
<td></td>
</tr>
<tr>
<td>Less : Advance</td>
<td>1,500</td>
<td>20,500</td>
</tr>
<tr>
<td>To Establishment Expenses</td>
<td>1,595</td>
<td></td>
</tr>
<tr>
<td>To Advertisement</td>
<td>16,000</td>
<td></td>
</tr>
<tr>
<td>Less : Transferred to Balance Sheet</td>
<td>12,000</td>
<td>4,000</td>
</tr>
<tr>
<td>To Loss on Stock destroyed [10,000 - 7,500]</td>
<td>2,500</td>
<td></td>
</tr>
<tr>
<td>To Provision for Doubtful Debts (New) [64,000 - 3,000] = 61,000+600=61,600×10/100]</td>
<td>6,160</td>
<td></td>
</tr>
<tr>
<td>To Provision for Discount on Debtors (New) [61,600 - 6,160] = 55,440 x 5/100]</td>
<td>2,772</td>
<td></td>
</tr>
</tbody>
</table>
Final Accounts

To Depreciation:
- Land & Building – 5% 1,000
- Furniture – 10% 800
- Motor Car – 20% 3,200

To Commission (due) 12,188
To Reserve Fund 3,352
To Net Profit (to be added with Capital A/c) 1,18,528.

2,11,115 2,11,115

Question 19:

The following is the Trial Balance of Mr. Nayan Bhattacharjee as on 31.12.98. Prepare a Trading & Profit & Loss account for the year 1998 and the Balance Sheet as on 31.12.98 from it.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>(Dr.) Rs.</th>
<th>(Cr.) Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchase (Adjusted)</td>
<td>1,60,000</td>
<td></td>
</tr>
<tr>
<td>Opening Stock</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>Salary less Provident Fund</td>
<td>15,400</td>
<td></td>
</tr>
<tr>
<td>Rent @ 500 p.m.</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>P. F. remittance incl. proprietor’s contribution @ 50%</td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>45,000</td>
<td></td>
</tr>
<tr>
<td>Wages</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Furniture &amp; Fittings</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Electricity</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Trade Expenses</td>
<td>1,550</td>
<td></td>
</tr>
<tr>
<td>Debtors</td>
<td>25,500</td>
<td></td>
</tr>
<tr>
<td>Interest on Loan</td>
<td>400</td>
<td></td>
</tr>
<tr>
<td>Commission</td>
<td>200</td>
<td></td>
</tr>
<tr>
<td>10% Bank Loan</td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td>Creditors</td>
<td></td>
<td>15,000</td>
</tr>
<tr>
<td>Building</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td></td>
<td>1,00,000</td>
</tr>
<tr>
<td>Drawings</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Closing Stock</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>Prepaid Wages</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>14,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td></td>
<td>2,72,250</td>
</tr>
<tr>
<td>Suspense A/c</td>
<td></td>
<td>7,000</td>
</tr>
</tbody>
</table>

4,04,250 4,04,250
Financial Accounting Fundamentals

Adjustments :
1. Wages include Rs. 1,000 paid for machinery erection charge.
2. Goods costing Rs. 5,000 were destroyed by fire and insurance claim was received for Rs. 4,000.
3. Sundry Debtors include Rs. 500 proved to be bad and provide @ 10% as Reserve for Bad Debt.
4. Goods costing Rs. 5,000 were sent to a customer on “sale on approval” basis on 31.12.98. These were recorded as sales. The rate of gross profit was 1/6th of sale.
5. Two cheques of Rs. 1,000 and Rs. 1,200 were deposited into bank on 29.12.98 but not cleared by the bank till 31.12.98.
6. Goods withdrawn by the proprietor for personal use but no entry was passed Rs. 2,500.
7. Discount allowed amounting to Rs. 3,500 had been posted to the debit of Sundry Debtors.
8. Sales had been overcast on the credit side by Rs. 2,000.
9. Cash withdrawn from bank Rs. 4,000 had been entered in the bank column of the cash book.
10. Provide depreciation @ 10% p.a. on all fixed assets.

Answer :

IN THE BOOKS OF NAYAN BHATTACHARJEE

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Trading Account and Profit &amp; Loss Account for the year ended 31.12.98</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To</td>
<td>Opening Stock</td>
<td>20,000</td>
</tr>
<tr>
<td>To</td>
<td>Purchase 1,60,000</td>
<td>Less : Sale on App. basis</td>
</tr>
<tr>
<td>Less</td>
<td>Drawings</td>
<td>2,500</td>
</tr>
<tr>
<td>To</td>
<td>Wages</td>
<td>15,000</td>
</tr>
<tr>
<td>Less</td>
<td>Erection Charge</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,62,250</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Salary A/c</td>
<td>15,400</td>
</tr>
<tr>
<td>Add:</td>
<td>P.F. Deduc. (50% of Rs.600)</td>
<td>600</td>
</tr>
<tr>
<td>To</td>
<td>Rent A/c 5,000</td>
<td>1,000</td>
</tr>
</tbody>
</table>
**Final Accounts**

To Contribution to P.F. (50% of Rs.1,200) 600
To Electric Charge 4,000
To Trade Expenses 1,550
To Interest on loan 400
Add : Outstanding 100 500
To Commission 200
To Loss by Fire 1,000
To Prov. for Bad Debt 1,200
To Bad debt 500
To Deprn. On :
  Machinery 4,600
  Building 3,000
  Furniture 4,000 11,600
To Capital A/c (N.P. transferred) 37,600.

80,750 80,750

**Balance Sheet as at 31.12.98**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Add : Net Profit</td>
<td>37,600</td>
<td>45,000</td>
</tr>
<tr>
<td>Less : Drawings (5,000+2,500)</td>
<td>7,500</td>
<td>1,30,100</td>
</tr>
<tr>
<td>10% Bank Loan</td>
<td>10,000</td>
<td>30,000</td>
</tr>
<tr>
<td>Outstanding Rent</td>
<td>1,000</td>
<td>3,000</td>
</tr>
<tr>
<td>Outstanding Interest on Bank Loan</td>
<td>100</td>
<td>40,000</td>
</tr>
<tr>
<td>Creditors</td>
<td>15,000</td>
<td>4,000</td>
</tr>
<tr>
<td>Less : Closing Stock (20,000 + 5,000)</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Less : Prepaid Wages</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Cash at bank</td>
<td>14,000</td>
<td></td>
</tr>
<tr>
<td>Less : Withdrawal</td>
<td>4,000</td>
<td>10,000</td>
</tr>
<tr>
<td>Debtors</td>
<td>25,500</td>
<td></td>
</tr>
<tr>
<td>Less : Unapproved Sales</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>19,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less : Bad Debt</td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>19,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less : wrong debit</td>
<td>7,000</td>
<td>12,000</td>
</tr>
<tr>
<td>1,200</td>
<td>10,800</td>
<td></td>
</tr>
<tr>
<td>Insurance Claim</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>1,56,200</td>
<td>1,56,200</td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Working Notes:

1. **For Adjustment No. 4**:
   Goods are not actually sold when sent for approval unless these are approved on & before the closing date (here 31.12.98) the selling price of the goods (here cost + 1/6th of sale or 1/5th of cost = 5,000 + 1/5 × 5,000 = Rs. 6,000) should be deducted from a Sale and Debtors.

   b. Added with closing stock

2. **For adjustment No. 5**:
   Two cheques of Rs. 1,000 and Rs.1,200 were deposited but not cleared by Bank has not affected as per balance of Cash Book.

3. **For Adjustment No. 7, 8 & 9**:
   Sundry debtors have credited by Rs. 7,000 to rectify wrong debit of discount of Rs. 3,500. Cash at bank has been reduced by Rs. 4,000 for omission of posting of withdrawal. Sales have been decreased by Rs. 4,000 due to overcosting.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Suspense Account</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>----------------------</td>
<td>-----------------------------------</td>
</tr>
<tr>
<td>To Sundry Debtors</td>
<td>(Rs.3,500 × 2)</td>
</tr>
<tr>
<td>To Bank A/c (Cash Withdrawal)</td>
<td>4,000</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

4. In absence of any information regarding date of Bank Loan taken, Interest on Loan is Calculated for 6 months. So interest on Loan should be 10% of Rs.10,000 × 1/2 = 500.

**Question 20**:

Mr. Salil Ghosh closes his Books on 31st December every year. The following matters are to be taken into consideration while preparing final accounts for the year ended 31.12.98:

(i) Goods costing Rs. 3,000 were taken by the proprietors for his personal use.

(ii) Goods costing Rs. 3,500 were destroyed by fire, but Insurance Company admitted a claim for Rs. 3,000 only.

(iii) Rs. 1,200 was paid for Insurance premium on 1.9.98 for the year ended 31.8.99.

(iv) Sales for the period included Rs. 1,500 worth of goods (at cost price) also taken by the proprietor for personal consumption.
**Final Accounts**

**Answer:**

**In the Books of SALIL GHOSH**

<table>
<thead>
<tr>
<th>JOURNAL ENTRIES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
</tr>
<tr>
<td>1.</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>2.</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>3.</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>4.</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

**Question 21:**

The following is the schedule of balances as on 31.03.98 extracted from the books of Kalidas Gupta:

<table>
<thead>
<tr>
<th>Dr.(Rs.)</th>
<th>Cr.(Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in Hand</td>
<td>2,800</td>
</tr>
<tr>
<td>Cash at flank</td>
<td>5,200</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>172,000</td>
</tr>
<tr>
<td>Stock as on 01.04.97</td>
<td>124,000</td>
</tr>
<tr>
<td>Furniture &amp; Fixture</td>
<td>42,800</td>
</tr>
<tr>
<td>Office Equipment</td>
<td>32,200</td>
</tr>
<tr>
<td>Building</td>
<td>120,000</td>
</tr>
<tr>
<td>Motor Car</td>
<td>40,000</td>
</tr>
</tbody>
</table>
### Readling and Profit & Loss Account for the year ended 31.03.98 and the Balance Sheet as on that date after making provision for the following —

1. **Depreciation:**
   - (a) Building used for business by 5%
   - (b) Furniture and Fitting by 10% – one steel table purchased during the year for Rs. 2,800 was sold for the same price but the sale proceeds were wrongly credited to Sales Account.
   - (c) Office Equipment by 15% – A type writer purchased during the year for Rs. 8,000 has been wrongly debited to Purchase Account.
   - (d) Motor Car by 20%.
2. Value of stock at the close of the year Rs. 88,000.
3. One month’s Rent for godown is outstanding.
4. One month’s salary is outstanding.
Final Accounts

5. Interest on loan from Mr. Goel is 12% per annum. This loan was taken on 01.05.97.
6. Reserve for bad debt to be maintained at 5% on Sundry Debtors.
7. Insurance premium includes Rs. 8,000 paid towards proprietor’s Life Insurance Policy and the balance of the insurance charges cover the period from 01.04.97 to 01.07.98.
8. Half of the building is used for residential purposes of Kalidas Gupta.

Answer:

Trading Account for the year ended 31.03.1998

<table>
<thead>
<tr>
<th>To</th>
<th>Opening Stock 124000</th>
<th>By Sales 460000</th>
<th>Less : Sale</th>
</tr>
</thead>
<tbody>
<tr>
<td>&quot;</td>
<td>Purchases 280000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Less : Purchase of</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Office Equipment</td>
<td>8000</td>
<td>457200</td>
</tr>
<tr>
<td>&quot;</td>
<td>Less : Returns</td>
<td>5200</td>
<td>266800</td>
</tr>
<tr>
<td>&quot;</td>
<td>Freight</td>
<td>2400</td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Gross Profit c/d</td>
<td>143600</td>
<td>Closing Stock 88000</td>
</tr>
<tr>
<td>&quot;</td>
<td></td>
<td>536800</td>
<td>536800</td>
</tr>
</tbody>
</table>

Profit and Loss Account for the ended 31.03.98

<table>
<thead>
<tr>
<th>To</th>
<th>Salaries 22000</th>
<th>By Gross Profit c/d 143600</th>
<th>Add : Outstanding 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td>&quot;</td>
<td>Rent for godown 11000</td>
<td>Discount Received 3200</td>
<td>24000</td>
</tr>
<tr>
<td>&quot;</td>
<td>Interest on Loan 5400</td>
<td>Gross Profit c/d 143600</td>
<td>12000</td>
</tr>
<tr>
<td>&quot;</td>
<td>Rates &amp; Taxes 4200</td>
<td></td>
<td>6600</td>
</tr>
<tr>
<td>&quot;</td>
<td>Discount Allowed 4800</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Carriage Outward 4000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Printing &amp; Stationery 3600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Electric Charges 4400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Insurance Premium 11000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>&quot;</td>
<td>Less : Premium on own life policies 8000</td>
<td>2400</td>
<td>600</td>
</tr>
<tr>
<td>&quot;</td>
<td>Less : Prepaid 3/15 x 3000 600</td>
<td>2400</td>
<td>600</td>
</tr>
<tr>
<td>&quot;</td>
<td>General Office Expenses 6000</td>
<td>8600</td>
<td>12600</td>
</tr>
<tr>
<td>&quot;</td>
<td>Res. for bad debt (5%) 8600</td>
<td>12600</td>
<td>8600</td>
</tr>
<tr>
<td>&quot;</td>
<td>Add: Bad debts 4000</td>
<td>12600</td>
<td>8600</td>
</tr>
<tr>
<td>&quot;</td>
<td>Less: Existing Res. 6000</td>
<td>8600</td>
<td>6600</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

“Bank Charges” 3200
“Motor Car Expenses” 7200
“Depreciation —
  Building 3000
  Furniture 4000
  Office Equipment 6000
  Motor Car 8000 21000
“Net Profit transferred to Balance Sheet” 36800

Balance Sheet of Kalidas Gupta as at 31.03.98

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital A/c Balance</td>
<td>324000</td>
<td>Building</td>
<td>120000</td>
</tr>
<tr>
<td>Add : Net Profit</td>
<td>36800</td>
<td>Less : Depreciation</td>
<td>6000</td>
</tr>
<tr>
<td></td>
<td>360800</td>
<td>Furniture &amp; Fittings</td>
<td>42800</td>
</tr>
<tr>
<td>Less : Drawings</td>
<td>35000</td>
<td>Less : Sales</td>
<td>2800</td>
</tr>
<tr>
<td>(24000 + 8000 + 3000)</td>
<td>325800</td>
<td>Less : Sales</td>
<td>2800</td>
</tr>
<tr>
<td>Loan from Mr. Goel</td>
<td>60000</td>
<td>Office Equipment</td>
<td>32000</td>
</tr>
<tr>
<td>Interest accrued</td>
<td>1200</td>
<td>Add : Purchase</td>
<td>8000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Less : Depreciation</td>
<td>4000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Motor Car</td>
<td>40000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Less : Depreciation</td>
<td>8000</td>
</tr>
<tr>
<td>Current Liabilities :</td>
<td></td>
<td>Current Assets :</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>86000</td>
<td>Stock in Trade</td>
<td>88000</td>
</tr>
<tr>
<td>Outstanding Expenses —</td>
<td></td>
<td>Sundry Debtors</td>
<td>172000</td>
</tr>
<tr>
<td>Salaries</td>
<td>2000</td>
<td>Less : Res. for B/Debt</td>
<td>8600</td>
</tr>
<tr>
<td>Godown</td>
<td>1000</td>
<td>Cash at Bank</td>
<td>5200</td>
</tr>
<tr>
<td></td>
<td>89000</td>
<td>Cash in hand</td>
<td>2800</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Prepaid Insurance</td>
<td>600</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>476000</td>
</tr>
</tbody>
</table>

Working :
- Drawings as per Trial Balance 24000
  Add : Insurance Policy on own life 8000
  32000
  Add : Depreciation of Building used for own life 35000

STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION
2.8 SELF-EXAMINATION QUESTIONS

1. Define Capital Expenditure, Revenue Expenditure and Deferred Revenue Expenditure.

2. Explain the basic principles in allocating expenditure between capital and revenue.

3. Distinguish, giving examples, between Trial Balance and Balance Sheet.

4. Pass entries to adjust the following:
   a) Salary paid Rs. 15,000; opening and closing outstanding salaries are Rs. 1,000 and Rs. 3,000 respectively.
   b) Consumption of materials at cost not recorded.
   c) Provide 5% on sundry debtors and 2% Reserve for discount allowable, closing balance of Sundry Debtors Rs. 60,000, from which Rs. 2,000 is to be written off.

5. A Company prepared its financial statement for the year ended 31st March, 1994, after transferring the difference in Trial Balance to a Suspense Account which was carried to the Balance Sheet.

   In the next year the following errors were discovered relating to the year 1993-94:
   (a) Wages included Rs. 8,000 towards installation of a new plant on 1st April 1993. The company charges depreciation on plant and machinery @ 15% p.a.
   (b) A cheque of Rs. 10,800 was paid to a creditor who allowed 10% cash discount but the payment was wrongly posted to purchase account Rs. 1,080 only without any other entry.
   (c) Sundry Debtors include Rs. 1,500 which proved irrecoverable but was not written off. A Reserve for Bad Debt was created only on closing debtors.
   (d) A Bills receivable amount Rs. 6,000 was discounted for Rs. 5,800, but the proceeds was posted to Sales Account as Rs. 580 and no other entry was made in this respect.

   Give the appropriate Journal entries to rectify the above errors.

6. (a) What is depreciation? What are causes of depreciation?
   (b) Bajaj & Co. close their account on 31st March every year. They purchased the machineries as follows:
      (i) Purchased the machineries costing Rs. 1,20,000 on 1.7.90.
      (ii) On 1.1.91, some machines were purchased costing Rs. 1,20,000.
      (iii) On 1.10.91, again purchased some machinery costing Rs. 20,000.
Financial Accounting Fundamentals

(iv) On 1.1.92, purchased a new machine for Rs. 60,000.

(v) One machine costing Rs. 40,000 which was purchased on 1.7.90, was sold for Rs. 12,000 on 1.4.92.

(vi) They charge depreciation @ 33\%\over 3 \% on the written-down value method.

(vii) They have the practice to charge depreciation for the full year even if the machinery is used for a part of the year.


[Ans. : Balance on 31.3.91 Rs. 1.6L ; 31.3.92 Rs. 1.6L and 31.3.93 Rs. 0.94815L]

7. A Ltd. provides for doubtful debts @ 5\% and for discount on debtors @ 2\%.

From the following details you are required to show the journal entries in the books of A Ltd.

Debtors as on 31.12.94 were Rs. 25,600 including bad debts of Rs. 600. Debts written off during the year excluding this Rs. 600 amounted to Rs. 1,330. Discount allowed during the year was Rs. 400. Provision for doubtful debts and that for discount on 1.1.94 were Rs. 2,740 and Rs. 380 respectively.

[Ans. : Provision for doubtful debts Rs. 440 ; Prov. for discount on debtors Rs. 475]

8. The financial year of Mr. X ends on 31st March 1995 but the stock on hand was physically verified only on 7th April 1995. You are required to ascertain the value of closing stock (at cost) as on 31st March 1995 from the following information :–

(a) The stock (valued at cost) as verified on 7th April 1995 was Rs. 1,54,000.

(b) Sales have been entered in the Sales day book only after the despatch of goods and sales return only on receipt of the goods.

(c) Purchases have been entered in the Purchase day book on receipt of the purchase invoice irrespective of the date of receipt of the goods.

(d) Sales as per sales day book for the period 1st April 1995 to 7th April 1995 (before the actual verification) amounted to Rs. 68,800 of which goods of a sale value of Rs. 12,000 had not been delivered at the time of verification.

(e) Purchases as per Purchase day book for the period 1st April 1995 to 7th April 1995 (before the actual verification) amounted to Rs. 58,000 of which goods for purchases of Rs. 15,000 had not been received at the date of verification and goods for purchases of Rs. 20,000 had been received prior to 31st March 1995.

(f) In respect of goods costing Rs. 50,000 received prior to 31st March 1995, invoices had not been received up to the date of verification of stocks.

(g) The gross profit is 25\% on sales.

[Ans. : Value of Closing Stock on 31.3.1995 Rs. 1,03,600]
9. (a) The net income of Mr. A. K. Bose for the year ended 31st December, 1994 under cash basis was Rs. 10,875. From the following particulars, pass Journal entries, to convert his income from cash basis to accrual basis and ascertain his income under accrual basis:

<table>
<thead>
<tr>
<th>Date</th>
<th>Depreciation</th>
<th>1-1-1994 (Rs.)</th>
<th>31-12-94 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accrued fees</td>
<td>350</td>
<td>450</td>
<td></td>
</tr>
<tr>
<td>Fees received in advance</td>
<td>100</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>Expenses outstanding</td>
<td>200</td>
<td>150</td>
<td></td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>100</td>
<td>175</td>
<td></td>
</tr>
</tbody>
</table>

[Ans. : Income under Accrual basis Rs. 11,150]

(b) A manager is entitled to a commission at a certain percentage of net profit (such commission to be charged in arriving at the net profit).

The commission is to be allowed on the following rates:

- First Rs. 10,000 of the net profit Nil
- Next Rs. 20,000 " " @ 10%
- Next Rs. 30,000 " " @ 15%
- Next Rs. 60,000 " " @ 20%
- Balance " " @ 30%

The net profit before charging the manager’s commission is Rs. 1,45,000. Compute the amount of manager’s commission.

[Ans. : Manager's commission Rs. 18,500 + Rs. 1,500 = Rs. 20,000]

10. Discuss how the following items shall be treated in the Final Accounts:

(a) Wages for extension of buildings;
(b) Carriage on new machinery;
(c) Preliminary expenses;
(d) Interest paid on capital during constructions;
(e) Advertisement expenditure in special advertisement drive.
11. The following is the Balance Sheet of the retail business of Mr. Padamsi as on 31.12.1995:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mr. Padamsi’s Capital Account</td>
<td>1,25,000</td>
<td>Furniture &amp; Fittings</td>
<td>25,000</td>
</tr>
<tr>
<td>Creditors for goods</td>
<td>30,000</td>
<td>Stock</td>
<td>75,000</td>
</tr>
<tr>
<td>Outstanding expenses (rent)</td>
<td>1,000</td>
<td>Sundry Debtors</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash at bank</td>
<td>35,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash in hand</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>1,56,000</td>
<td></td>
<td>1,56,000</td>
</tr>
</tbody>
</table>

You are furnished with the following information:

1. Mr. Padamsi always sells his goods at a profit of 25% on sales.
2. Goods are sold for cash and credit. Credit customers pay by cheque only.
3. Payments for purchases are always made by cheque.
4. It is Mr. Padamasí’s practice to bank his takings at the end of every week after paying the weekly expenses, viz., salaries to clerk Rs. 250, sundry expenses Rs. 50, and personal expenses Rs. 100.

Analysis the bank pass book for the period ended 31.3.1996 disclosed the following:

- Payments to creditors Rs. 75,000
- Payment of rent 4,000
- Amount remitted to the bank Rs. 1,35,000 (including cheques for Rs. 10,000 received from customers to whom the goods were sold on credit).

The following are the balances as on 31.3.1996:

- Stock Rs. 32,500
- Creditors for goods 32,500
- Sundry Debtors 30,000

In the evening of 31.3.1996, the cashier absconded with the available cash in the cash box. You are required to prepare a statement, showing the amount of cash defalcated by the cashier, and also a profit and Loss Account for the year ended 31.3.1996.

[Ans.: Cash defalcated by the cashier Rs. 10,800; Net Profit Rs. 22,300; Balance Sheet total Rs. 1,78,500 and Cash sales Rs. 1,40,000]
3.0  INTRODUCTION

Some organisations like clubs, hospitals, educational institutions are established not for making profit but for the purpose of providing services to members and beneficiaries. Receipts and Payments A/c Income and Expenditure A/c and Balance Sheet form part of their final accounts.

3.1  TREATMENT OF CERTAIN ITEMS

1) Entrance Fees : Such fees are received by non profit seeking organisations at the time of admitting new members. For the incoming member it is a one time payment. Entrance Fees can be capitalised or charged to Income Expenditure A/c as per rules of the organization.

2) Donations : Donation can be utilised for meeting capital or revenue expenses. When received for a special purpose, the amount of donation is credited to a special fund, which may be invested in specific securities. Interest, Dividend, etc. received from such investments are credited to Fund A/c expenses for performing the purpose of Fund is charged to Fund A/c.
3) **Life membership subscriptions:** This can be treated in the following ways in the Accounts:

   i) The entire amount is transferred to a special account on death of the member and it is transferred to the Accumulated Fund.

   ii) An amount equal to normal yearly membership subscription is charged to Income and Expenditure A/c and the balance is carried forward until exhausted. In case of death of a member the unexhausted portion is charged to Accumulated Fund on the date of death.

   iii) An amount calculated according to age and average life of the member may annually be transferred to the credit of Income and Expenditure A/c

4) **Subscription:** This is one of the main sources of income and has to be accounted for on accrual basis. The amount of subscription chargeable to Income and Expenditure A/c can be determined by opening a Subscription A/c in the following way:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Subscription A/c</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td><strong>Explanation</strong></td>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>To Balance b/d</td>
<td>Subscription A/c Opening balance of accrued subscription</td>
<td>By balance b/d</td>
</tr>
<tr>
<td>To Income and Expenditure A/c</td>
<td>Balancing figure</td>
<td>By Bank A/c</td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>Closing balance of advance subscription</td>
<td>By Balance c/d</td>
</tr>
</tbody>
</table>

5) **Sale of News papers & used sports materials:**

   Sale proceeds are credited to Income & Expenditure A/c

6) **Sale of Assets:** Sale proceeds are debited in Receipts & Payments A/c and the Profit/Loss on sale is taken to Income/Expenditure A/c.

**Illustration 1:**

A summary of Receipts and Payments Account of Calcutta Club for the year ended 31.03.97 is given below:
Receipts | Rs. | Rs. | Payments | Rs.
---|---|---|---|---
Cash in hand (1.4.96) | 4,740 | Wages | 13,380 |
Subscription :
1995-96= | 700 | Restaurant Purchase | 50,400 |
1996-97= | 28,620 | Rent | 7,500 |
1997-98= | 400 | Rates | 2,200 |
| 29,720 | Secretary's Salary | 3,120 |
Entrance Fees | 3,200 | Lighting & Other Services | 7,700 |
Restaurant Receipts | 56,800 | Competition Prizes | 4,000 |
Tournament Receipts | 13,640 | Printing & Stationary | 6,000 |
Due to Secretary for Fixed Deposits | 8,000 |
Petty Expenses | 80 | Balance in hand and at Bank | 5,880 |
| 1,08,180 | | 1,08,180 |

On April 1, 1996, the Club's Assets were: Furniture and Equipment Rs. 48,000; Restaurant Stocks Rs. 2,600; stock of Prizes Rs. 800; Rs. 5,200 was owing for supplies to the Restaurant.

On March 31, 1997 the Restaurant Stocks were Rs. 3,000 and Prizes in hand were Rs. 5,600 while the Club owed Rs. 5,600 for Restaurant supplies.

It was also found that member's subscriptions unpaid at March 31, 1997 amounted to Rs. 1,000.

Rent was paid upto June 30, 1997. Prepare an account showing the Profit or Loss made on the Restaurant and a General Income and Expenditure account for the year ended 31.03.97 together with a Balance Sheet at that date, after writing 10% off the Furniture and Equipment.

Solution:

In the books of CALCUTTA CLUB

Dr. | Restaurant Trading for the year ended 31.3.1997 | Cr.
---|---|---
Particulars | Rs. | Particulars | Rs.
To Opening Stock | 2,600 | By Restaurant Receipts | 56,800 |
To Purchase | 50,800 | By Closing Stock | 3,000 |
To Profit (transferred to Income & Exp. A/c) | 6,400 |
| 59,800 | 59,800 |
Financial Accounting Fundamentals

Dr. Income & Expenditure Account for the year ended 31.3.97 Cr.

<table>
<thead>
<tr>
<th>Expenditure</th>
<th>Rs.</th>
<th>Income</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Wages - Outdoor Staff</td>
<td>13,380</td>
<td>By Member's Subscription</td>
<td>29,620</td>
</tr>
<tr>
<td>To Rent</td>
<td>5,000</td>
<td>By Games competition receipts</td>
<td>13,640</td>
</tr>
<tr>
<td>To Rates</td>
<td>2,200</td>
<td>By Restaurant Profit</td>
<td>6,400</td>
</tr>
<tr>
<td>To Secretary's Salary</td>
<td>3,120</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Lighting, cleaning and Sanitary services</td>
<td>7,700</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Competition Prizes</td>
<td>4,300</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Printing, Postage and Sundries</td>
<td>6,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Depreciation on Furniture &amp; Equipment 10%</td>
<td>4,800</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Excess of Income over Expenditure</td>
<td>3,160</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>49,660</td>
<td></td>
<td>49,660</td>
</tr>
</tbody>
</table>

Balance Sheet as at 31.3.1997

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Fund :</td>
<td></td>
<td>Furniture &amp; Equipment</td>
<td>48,000</td>
</tr>
<tr>
<td>Opening Balance</td>
<td>50,390</td>
<td>Less: 10% Depreciation</td>
<td>4,800</td>
</tr>
<tr>
<td>Add : Entrance Fees</td>
<td>3,200</td>
<td>Restaurant Stock</td>
<td>3,000</td>
</tr>
<tr>
<td>Add : Excess of Income</td>
<td></td>
<td>Prizes in hand</td>
<td>500</td>
</tr>
<tr>
<td>over Expenditure</td>
<td>3,160</td>
<td>Fixed Deposit with Bank</td>
<td>8,000</td>
</tr>
<tr>
<td>Subscription Received in advance</td>
<td>400</td>
<td>Cash in hand and at Bank</td>
<td>5,880</td>
</tr>
<tr>
<td>Creditors for Restaurant supply</td>
<td>5,600</td>
<td>Prepaid Rent (April to June, 1997)</td>
<td>1,250</td>
</tr>
<tr>
<td>Due to Secretary</td>
<td>80</td>
<td>Subscription Outstanding</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>62,830</td>
<td></td>
<td>62,830</td>
</tr>
</tbody>
</table>

Illustration 2:

From the following balances in the books and other details of Dancing Club, prepare Trading Account and Income and Expenditure Account for the year and a Balance Sheet as at 31.03.2002:

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bar Collections</td>
</tr>
<tr>
<td>Restaurant collections</td>
</tr>
<tr>
<td>Furniture on 31.03.2001</td>
</tr>
<tr>
<td>Tennis Accessories on 31.03.2001</td>
</tr>
<tr>
<td>Tennis Receipts</td>
</tr>
<tr>
<td>Furniture Purchased</td>
</tr>
<tr>
<td>Subscription</td>
</tr>
<tr>
<td>Interest</td>
</tr>
<tr>
<td>Capital Fund Balance as on 31.03.2001</td>
</tr>
<tr>
<td>Stock in Bar on 31.03.2001</td>
</tr>
</tbody>
</table>
Stock in Restaurant on 31.03.2001  510
Rent and Rates  6,700
Purchases for Bar  14,365
Purchases for Restaurant  11,735
China, Cutlery, Linen on 31.03.2001  2,400
Electric Charges  1,720
Establishments :
   Bar  4,960
   Restaurant  3,540
   General  4,260
Outstanding Subscription on 31.03.2002  3,650
Creditors on 31.03.2002  5,000
Purchase of China, Cutlery, Linen  1,200
Cash and Bank balances on 31.03.2002  10,560
Investments  4,000

Stock in Bar on 31.03.2002 — Rs. 4,000; Stock in Restaurant on 31.03.2002 — Rs. 1,230.
Provide depreciation on opening balances; Furniture @ 20% (50% to be charged to Bar and Restaurant on collection basis); Tennis Accessories 20%; China, Cutlery, Linen 20% (to be charged on collection basis).

Solution :

**DANCING CLUB**

Trading Account for the year ended 31st March, 2002

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Bar</th>
<th>Restaurant</th>
<th>Particulars</th>
<th>Bar</th>
<th>Restaurant</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>1,560</td>
<td>510</td>
<td>By Collection</td>
<td>21,250</td>
<td>14,360</td>
</tr>
<tr>
<td>To Purchases</td>
<td>14,365</td>
<td>11,735</td>
<td>By Closing Stock</td>
<td>4,000</td>
<td>1,230</td>
</tr>
<tr>
<td>To Establishment</td>
<td>4,960</td>
<td>3,540</td>
<td>By Income &amp; Expenditure A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Depreciation :</td>
<td></td>
<td></td>
<td></td>
<td>1,083</td>
<td></td>
</tr>
<tr>
<td>on furniture</td>
<td>900</td>
<td>600</td>
<td></td>
<td>1,083</td>
<td></td>
</tr>
<tr>
<td>on Cutlery, Linen, etc.</td>
<td>432</td>
<td>288</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Income &amp; Expenditure A/c</td>
<td></td>
<td></td>
<td></td>
<td>3,033</td>
<td></td>
</tr>
<tr>
<td></td>
<td>25,250</td>
<td>16,673</td>
<td></td>
<td>25,250</td>
<td>16,673</td>
</tr>
</tbody>
</table>

**Notes**: Depreciate furniture by 20% (i.e., Rs. 3,000) out of which 50% of Rs. 3,000 distributed and the ratio of 3 : 2 as rounded off on 21,250 : 14,360. Depreciate China, Cutlery & Linen by 20% (i.e., Rs. 720) and distributed as 3 : 2 as above.
Financial Accounting Fundamentals

**Income & Expenditure Account** for the year ended 31st March, 2002

<table>
<thead>
<tr>
<th>Expenditure</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Income</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Establishment</td>
<td>4,260</td>
<td>By Subscription</td>
<td>25,730</td>
<td></td>
</tr>
<tr>
<td>To Rent &amp; Rates</td>
<td>6,700</td>
<td>By Tennis Receipts</td>
<td>7,620</td>
<td></td>
</tr>
<tr>
<td>To Electric Charges</td>
<td>1,720</td>
<td>By Interest</td>
<td>480</td>
<td></td>
</tr>
<tr>
<td>To Depreciation :</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>1500</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tennis Accessories</td>
<td>1100</td>
<td>2,600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Excess of Income over</td>
<td></td>
<td></td>
<td>Less: Loss in Restaurant</td>
<td>1,950</td>
</tr>
<tr>
<td>Expenditure A/c</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Surplus transferred</td>
<td>20,500</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>35,780</td>
<td>35,780</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Notes:** 50% of depreciation on furniture (i.e., of Rs. 3,000). Ledger balance after adjustment with outstanding subscription.

**Balance Sheet** as at 31st March, 2002

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Fund :</td>
<td></td>
<td></td>
<td>Furniture</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Balance on 1.4.2001</td>
<td>17720</td>
<td></td>
<td>Less: Depreciation</td>
<td>3,000</td>
<td>12000</td>
</tr>
<tr>
<td>Add: Excess of Income over Expenditure</td>
<td>20,500</td>
<td>38,220</td>
<td>Add: during the year</td>
<td>500</td>
<td>12,500</td>
</tr>
<tr>
<td>Creditors</td>
<td>5,000</td>
<td></td>
<td>Tennis Accessories</td>
<td>5500</td>
<td>1100</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less: Deprn.</td>
<td></td>
<td>1200</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>China, Cutlery, Linen</td>
<td>2400</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Add: During the year</td>
<td>1200</td>
<td>3600</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less: Depreciation</td>
<td>720</td>
<td>2,880</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Investments</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Stock in Bar</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Stock in Restaurant</td>
<td>1,230</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Outstanding Subscription</td>
<td>3,650</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Cash &amp; Bank Balances</td>
<td>10,560</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>43,220</td>
<td>43,220</td>
<td></td>
</tr>
</tbody>
</table>
### 3.2 SPECIMEN QUESTIONS WITH ANSWERS

**Question 1:**

The following is the Receipt and Payment Account of Jayshree Sangha Club in respect of the year to 31.12.98.

<table>
<thead>
<tr>
<th>Receipt</th>
<th>Rs.</th>
<th>Payment</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1.98</td>
<td>31.12.98</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Balance b/d</td>
<td>25,000</td>
<td>By Salaries</td>
<td>24,000</td>
</tr>
<tr>
<td>31.12.98</td>
<td></td>
<td>By Stationery</td>
<td>5,000</td>
</tr>
<tr>
<td>To Subscription</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1997</td>
<td>800</td>
<td>By Telephone Charges</td>
<td>2,000</td>
</tr>
<tr>
<td>1998</td>
<td>40,000</td>
<td>By Investment</td>
<td>40,000</td>
</tr>
<tr>
<td>1999</td>
<td>1,500</td>
<td>By Sundry Expenses</td>
<td>9,000</td>
</tr>
<tr>
<td>To Sales of Newspaper</td>
<td>1,200</td>
<td>By Balance c/d</td>
<td>9,500</td>
</tr>
<tr>
<td>To Dividend on Investment</td>
<td>25,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Donation</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,01,500</td>
<td></td>
<td>1,01,500</td>
</tr>
</tbody>
</table>

**Additional information available:**

(a) There are 500 members each paying as annual subscription of Rs. 100; Rs. 1,000 being in arrear for 1997 at the beginning of 1998.

(b) Stock of stationery on 31. Dec. 1997 was Rs. 2000 and on 31st Dec. 1998 Rs. 1500

(c) At 31st Dec. 1998, the rates were prepaid to the following 31st March, the yearly charges being Rs. 12,000. A Quarter’s charge for telephone is outstanding for Rs. 500. Sundry Expenses outstanding on 31st Dec. 1997 was Rs. 1200.

(d) At 31st Dec. 1997 the Building stood in the book at Rs. 1,50,000 on which depreciation is to be provided at 5% per annum. Investment on 31.12.1997 were Rs. 3,50,000.

Prepare an Income & Expenditure Account for the year ended 31st Dec. 1998 and a Balance Sheet as on that date.
**Financial Accounting Fundamentals**

**Answer:**

**In the books of Jayshree Sangh Club**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Income and Expenditure Account for the year ended 31.12.98</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>Expenditure</strong></td>
<td><strong>Rs.</strong></td>
</tr>
<tr>
<td>To Salary</td>
<td>24,000</td>
<td>By Subscription</td>
</tr>
<tr>
<td>To Stationery used:</td>
<td>Add: Outstanding</td>
<td>10,000</td>
</tr>
<tr>
<td>– Opening stock</td>
<td>20,000</td>
<td>Add: Purchase</td>
</tr>
<tr>
<td></td>
<td>7,000</td>
<td>Less: Closing Stock</td>
</tr>
<tr>
<td>To Rates</td>
<td>12,000</td>
<td>By Donation</td>
</tr>
<tr>
<td>Less: Prepaid (3/12×12,000)</td>
<td>3,000</td>
<td>9,000</td>
</tr>
<tr>
<td>To Telephone Charge</td>
<td>2,000</td>
<td>Add: Outstanding</td>
</tr>
<tr>
<td>To Sundry Exp.</td>
<td>9,000</td>
<td>Less: Outstanding for ‘97</td>
</tr>
<tr>
<td>To Deprn. on Building</td>
<td>7,500</td>
<td></td>
</tr>
<tr>
<td>Expenditure transfer to Capital Fund</td>
<td>27,900</td>
<td></td>
</tr>
<tr>
<td></td>
<td>84,200</td>
<td>84,200</td>
</tr>
</tbody>
</table>

**Jayshree Sangha Club**

**Balance Sheet as at 31.12.98**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>5,26,800</td>
<td>1,50,000</td>
<td>Building</td>
<td>5,54,700</td>
<td></td>
</tr>
<tr>
<td>Add: Surplus</td>
<td>27,900</td>
<td>7,500</td>
<td>Less: Deprn. @ 5%</td>
<td>1,42,500</td>
<td></td>
</tr>
<tr>
<td>Subscription received in advance</td>
<td>1,500</td>
<td>3,50,000</td>
<td>Investment</td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td>Add: Purchase</td>
<td>40,000</td>
<td>3,90,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Outstanding Telephone Charge</td>
<td>500</td>
<td>1,500</td>
<td>Stock of stationery</td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td>ACCRUED SUBSCRIPTION:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1997</td>
<td>200</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1998</td>
<td>10,000</td>
<td>10,200</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prepaid Rates</td>
<td>3,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>9,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>5,56,700</td>
<td>5,56,700</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Accounting for Non-Profit Organisations

Working Notes :

1. **Analysis of Subscriptions :**
   (a) For 1997
      - Total Amount due on 31.12.97: Rs. 1,000
      - Less: Received in 1998 on A/c: Rs. 800
      - Outstanding on 31.12.98: Rs. 200
   (b) For 1998
      - Annual subscription times 500 × Rs. 100: Rs. 50,000
      - Less: Received in 1998 on Account: Rs. 40,000
      - Outstanding on 31.12.98: Rs. 10,000
   (c) For 1999
      - Received in advance: Rs. 1,500

2. **Opening Capital on 31.12.97 or 1.1.98**

   **Balance Sheet as on 1.1.98**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital (Balancing figure)</td>
<td>5,26,800</td>
<td>Cash</td>
<td>25,000</td>
</tr>
<tr>
<td>Outstanding Sundry Expenses</td>
<td>1,200</td>
<td>Outstanding Subscription</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stock of Stationery</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Building</td>
<td>1,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Investment</td>
<td>3,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>5,28,000</td>
<td></td>
<td>5,28,000</td>
</tr>
</tbody>
</table>

**Question 2:**

On 31st March, 1999 Writers Club, a cultural association had the following assets and liabilities:

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust fund: 5,00,000 Cash: 3,000</td>
<td></td>
</tr>
<tr>
<td>Accumulated surplus in income and expenditure A/c: 1,05,000 Canara Bank: Savings A/c: 7,000</td>
<td></td>
</tr>
<tr>
<td>Membership fee received in advance for 1999-2000: 10,000 Fixed deposit: 2,00,000</td>
<td></td>
</tr>
<tr>
<td>Outstanding expenses: 10,000 Investments in: Government securities: 3,00,000 Fixed assets: 95,000</td>
<td></td>
</tr>
<tr>
<td>Membership fee receivable: 15,000 Prepaid expenses: 5,000</td>
<td></td>
</tr>
<tr>
<td>6,25,000</td>
<td>6,25,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

The following is the receipt and payment account for the year ended 31st March, 2000:

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening balance:</td>
<td>Administrative expenses</td>
</tr>
<tr>
<td>Cash</td>
<td>3,000</td>
</tr>
<tr>
<td>Savings with Canara Bank</td>
<td>7,000</td>
</tr>
<tr>
<td>10,000</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Membership fee received up to 31/3/1999</td>
<td>Investments in ICICI Bond</td>
</tr>
<tr>
<td>for 1999-2000</td>
<td>14,000</td>
</tr>
<tr>
<td>for 2000-2001</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Sale of tickets - programme</td>
<td>Cash</td>
</tr>
<tr>
<td>Advertisements in program souvenir</td>
<td>Savings with Canara Bank</td>
</tr>
<tr>
<td>25,000</td>
<td>7,700</td>
</tr>
<tr>
<td>Fixed deposits with Canara Bank</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Interest on bank A/c: Savings</td>
<td>700</td>
</tr>
<tr>
<td>Fixed deposit</td>
<td>22,000</td>
</tr>
</tbody>
</table>

| Amount received on maturity of government security inclusive of interest Rs. 8,000 (cost Rs. 80,000) | |
| 1,00,000 | 9,1,2,700 |

The club informs you that:

(i) Membership fee for 1999-2000 due is Rs. 25,000; it includes Rs. 1,000 due from the member who has not yet paid also for 1998-99; provision for irrecoverable membership is to be made in respect of this member.

(ii) Income receivable on 31-3-2000 on ICICI bond is Rs. 30,000 and on government securities is Rs. 24,000.

(iii) Prepaid expenses on 31-3-2000 amount to Rs. 7,000.

(iv) Outstanding expenses on 31-3-2000 amount to Rs. 8,000.

(v) Depreciation provision is to be Rs. 12,500.

(vi) Programme is an annual feature.
The club asks you to prepare

(a) Income and expenditure account for the year ended 31st March, 2000.
(b) Balance sheet as at 31st March, 2000.

**Answer:**

**WRITERS CLUB:**

**Income and Expenditure A/c for the year ended 31st March, 2000.**

<table>
<thead>
<tr>
<th>Expenditure</th>
<th>Rs.</th>
<th>Income</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Administration expenses</td>
<td>1,21,000</td>
<td>By Membership fee (Working 1)</td>
<td>1,85,000</td>
</tr>
<tr>
<td>(Working 3)</td>
<td></td>
<td>&quot; Interest Income :&quot;</td>
<td></td>
</tr>
<tr>
<td>&quot; Depreciation.</td>
<td>12,500</td>
<td>(Working 4)</td>
<td>84,700</td>
</tr>
<tr>
<td>&quot; Provision for doubtful memberships</td>
<td>2,000</td>
<td>&quot; Surplus from programme</td>
<td></td>
</tr>
<tr>
<td>(Working 2)</td>
<td></td>
<td>(Working 7)</td>
<td>2,50,000</td>
</tr>
<tr>
<td>&quot; Surplus for the year</td>
<td>3,96,200</td>
<td>&quot; Profit on disposal of</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>government securities</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Working 6)</td>
<td>12,000</td>
</tr>
<tr>
<td></td>
<td>5,31,700</td>
<td>5,31,700</td>
<td>5,31,700</td>
</tr>
</tbody>
</table>

**Writers Club**

**Balance Sheet as at 31st March, 2000**

<table>
<thead>
<tr>
<th>Liabilities :</th>
<th>Rs.</th>
<th>Assets :</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust Fund :</td>
<td></td>
<td>Cash</td>
<td>2,700</td>
</tr>
<tr>
<td>As per last balance sheet.</td>
<td>5,00,000</td>
<td>Canara Bank : Fixed deposit</td>
<td>5,000</td>
</tr>
<tr>
<td>Income and expenditure A/c</td>
<td>1,05,000</td>
<td>(Working 8)</td>
<td>2,50,000</td>
</tr>
<tr>
<td>– As per last balance Sheet</td>
<td></td>
<td></td>
<td>2,55,000</td>
</tr>
<tr>
<td>Surplus for the year</td>
<td>3,96,200</td>
<td>Investments in :</td>
<td>5,20,000</td>
</tr>
<tr>
<td>Membership fee received</td>
<td>5,01,200</td>
<td>Government Securities</td>
<td></td>
</tr>
<tr>
<td>in advance</td>
<td></td>
<td>(Working 5)</td>
<td>2,20,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>8,000</td>
<td>ICICI Ltd. Bonds</td>
<td>3,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Interest income receivable on :</td>
<td>5,20,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Government securities</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Working 4)</td>
<td>24,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>ICICI Ltd. bonds</td>
<td>30,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>54,000</td>
</tr>
</tbody>
</table>
## Financial Accounting Fundamentals

### Membership Fees due for

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>1,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td>26,000</td>
</tr>
</tbody>
</table>

Less: Provision for doubtful dues

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>2,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>7,000</td>
</tr>
</tbody>
</table>

Prepaid expenses

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>2,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>7,000</td>
</tr>
</tbody>
</table>

Fixed assets: (Working 9)

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>1,62,500</td>
</tr>
<tr>
<td>1999-2000</td>
<td>1,62,500</td>
</tr>
</tbody>
</table>

Total: 10,25,200

### Prepaid expenses

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>7,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>7,000</td>
</tr>
</tbody>
</table>

Total: 14,000

### Income & expenditure A/c

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>14,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>16,000</td>
</tr>
</tbody>
</table>

Closing receivable for:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>1,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>25,000</td>
</tr>
</tbody>
</table>

Total: 2,16,000

### Provision for Doubtful Recovery

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-99</td>
<td>1,000</td>
</tr>
<tr>
<td>1999-2000</td>
<td>1,000</td>
</tr>
</tbody>
</table>

Closing balance: 2,000

### Expenses A/c

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening prepaid Bank</td>
<td>5,000</td>
</tr>
<tr>
<td>Income &amp; expenditure A/c</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Closing outstanding (balancing figure)</td>
<td>8,000</td>
</tr>
<tr>
<td>Closing prepaid.</td>
<td>7,000</td>
</tr>
</tbody>
</table>

Total: 1,38,000

---

### Working:

1) **Membership Fees**

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening receivable.</td>
<td>15,000</td>
</tr>
<tr>
<td>Income &amp; expenditure A/c. (balancing figure)</td>
<td>1,85,000</td>
</tr>
<tr>
<td>Closing receipt in advance</td>
<td>16,000</td>
</tr>
<tr>
<td>Opening receipt in advance Bank for 1998-99</td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td>14,000</td>
</tr>
<tr>
<td></td>
<td>1,50,000</td>
</tr>
<tr>
<td></td>
<td>16,000</td>
</tr>
<tr>
<td></td>
<td>1,80,000</td>
</tr>
<tr>
<td>Closing receivable for: 1998-99</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td>26,000</td>
</tr>
<tr>
<td></td>
<td>2,16,000</td>
</tr>
</tbody>
</table>

2) **Provision for Doubtful Recovery**

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,000</td>
</tr>
<tr>
<td>1,000</td>
</tr>
<tr>
<td>2,000</td>
</tr>
</tbody>
</table>

3) **Expenses A/c**

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening prepaid Bank</td>
<td>5,000</td>
</tr>
<tr>
<td>Income &amp; expenditure A/c</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Closing outstanding (balancing figure)</td>
<td>8,000</td>
</tr>
<tr>
<td>Closing prepaid.</td>
<td>7,000</td>
</tr>
</tbody>
</table>

Total: 1,38,000
### Interest income:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank accounts</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Savings</td>
<td>700</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fixed deposit</td>
<td>22,000</td>
<td>22,700</td>
<td></td>
</tr>
<tr>
<td>Investments</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government securities</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>received</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>receivable</td>
<td>24,000</td>
<td>32,000</td>
<td></td>
</tr>
<tr>
<td>ICICI Ltd. Bond</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Receivable</td>
<td>30,000</td>
<td>62,000</td>
<td>84,700</td>
</tr>
</tbody>
</table>

5) Investments in government securities:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening cost</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Less: Realised</td>
<td>80,000</td>
</tr>
<tr>
<td>Closing cost</td>
<td>2,20,000</td>
</tr>
</tbody>
</table>

6) Profit on disposal of government securities:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount received</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Less: Interest</td>
<td>8,000</td>
</tr>
<tr>
<td>Cost</td>
<td>80,000</td>
</tr>
<tr>
<td>Profit</td>
<td>12,000</td>
</tr>
</tbody>
</table>

7) Surplus from programme:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advertisements in souvenir</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Sale of tickets</td>
<td>25,000</td>
</tr>
<tr>
<td>Less: Programme expenses</td>
<td>2,75,000</td>
</tr>
</tbody>
</table>

8) Fixed deposit with Canara Bank:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening balance</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Add: Fresh deposit</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Less: Maturity</td>
<td>75,000</td>
</tr>
<tr>
<td>Closing balance</td>
<td>2,50,000</td>
</tr>
</tbody>
</table>

9) Fixed assets:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening balance</td>
<td>95,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>80,000</td>
</tr>
<tr>
<td>Less: Depreciation</td>
<td>12,500</td>
</tr>
<tr>
<td>Total</td>
<td>1,62,500</td>
</tr>
</tbody>
</table>
5.14

Financial Accounting Fundamentals

**Question 3:**

Paresh runs a circulating library and his accounts are in a mess. One Bank Account has been used for both the business as well as his personal transactions. After looking into his records you gather the following information:

3. Payment of other expenses for the year ended 31st March, 2002 – Rs. 3,080.
4. Subscription collected – Rs. 21,695.
5. He has taken Rs. 500 per month in cash from the subscription collection to pay to his wife for their household and personal expenses, depositing the balance of the collections into the Bank.
6. During the year he bought a second hand car (not used for the business) from a friend for Rs. 4,000. However, as the friend owed him Rs. 250 for subscription, the matter was settled by a cheque for the difference.
7. An assurance policy on his life matured during the year and realised Rs. 7,000.
8. Paresh issued a cheque for Rs. 1,200 to a friend as loan. The friend is repaying by instalments in cash, and owes Rs. 500 on 1st March, 2002.
9. Magazine subscription for the year amounting to Rs. 400 had to be written off by Paresh as irrecoverable.
10. Other personal payments by cheques total Rs. 2,350.
11. The cash collected includes Rs. 600 in respect of magazine subscription written off as irrecoverable in a previous year.
12. Paresh runs the business from his flat for which a rent of Rs. 90 per month is included in the payments for other expenses Rs. 3,080. The living accommodation may be regarded as two-thirds of the whole.
13. The following balances may be accepted as correct:

<table>
<thead>
<tr>
<th></th>
<th>31st March 2001 (Rs.)</th>
<th>31st March 2002 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in Hand</td>
<td>115</td>
<td>70</td>
</tr>
<tr>
<td>Bank Balance</td>
<td>4,720</td>
<td>5,880</td>
</tr>
<tr>
<td>Subscription receivable (Debtors) considered good</td>
<td>1,830</td>
<td>2,105</td>
</tr>
<tr>
<td>Creditors for purchase of Magazine</td>
<td>900</td>
<td>840</td>
</tr>
<tr>
<td>Stock of Magazine, at cost</td>
<td>2,450</td>
<td>830</td>
</tr>
</tbody>
</table>

You are required to prepare:

(a) A Cash and Bank Account for the year;
(b) Paresh (Proprietor’s) Account for the year;
(c) An income and Expenditure Account of the circulating Library for the year ended 31st March, 2002; and
(d) A Balance Sheet of the Business as at 31st March, 2002.

Show your workings.
Answer:

**In the Books of Paresh**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Receipts</th>
<th>Cash</th>
<th>Bank</th>
<th>Payments</th>
<th>Cash</th>
<th>Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002, April 1</td>
<td>To Balance b/d</td>
<td>115</td>
<td>4720</td>
<td>By Creditors (Magazine)</td>
<td>9700</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Subscription</td>
<td>6000</td>
<td>15095</td>
<td>By Other Expenses</td>
<td>2000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Subscription w/o in previous year now recovered</td>
<td>600</td>
<td></td>
<td>By Rent of Premises</td>
<td>1080</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Capital A/c (Proprietor’s Policy money)</td>
<td>7000</td>
<td></td>
<td>By Wages (Cash bal. figure)</td>
<td>1345</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Drawings (Refund of loan)</td>
<td>700</td>
<td></td>
<td>By Drawings (for Loan to friend)</td>
<td>1200</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Drawings (Personal payments)</td>
<td>2350</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>70</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Total</td>
<td>7415</td>
<td>26815</td>
</tr>
</tbody>
</table>

* Out of Rent Rs. 1080, share of Paresh is Rs. 720.

**Dr. Paresh (Proprietor’s) Account**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Drawings</td>
<td>13570</td>
<td>By Balance b/d</td>
<td>8,215</td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>8045</td>
<td>By Bank (Policy money)</td>
<td>7,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Income and Expenditure A/c</td>
<td>6,400</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>21615</td>
<td></td>
</tr>
</tbody>
</table>

**Mr. Paresh Income and Expenditure Account** for the year ended 31st March, 2002

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Stock of magazine</td>
<td>2450</td>
<td>By Subscription</td>
<td>22,020</td>
</tr>
<tr>
<td>To Purchase (magazine)</td>
<td>9640</td>
<td>By Subscription recovered for previous yr.</td>
<td>600</td>
</tr>
<tr>
<td>To Delivery Peon’s Wages</td>
<td>2200</td>
<td>By Stock of Magazine</td>
<td>830</td>
</tr>
<tr>
<td>To Other Expenses</td>
<td>2000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Rent</td>
<td>1080</td>
<td>Less: Proprietor’s Rent</td>
<td>720</td>
</tr>
<tr>
<td></td>
<td></td>
<td>360</td>
<td></td>
</tr>
<tr>
<td>To Bad debts (Subscription W/O)</td>
<td>400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Excess of Income over Expenditure – transfer to Capital A/c</td>
<td>6400</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>23,450</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Balance Sheet of Paresh as at 31st March, 2002

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trade Creditors (Re. Magazine)</td>
<td>840</td>
<td></td>
<td>Cash in hand</td>
<td>70</td>
</tr>
<tr>
<td>Capital</td>
<td></td>
<td></td>
<td>Cash at Bank</td>
<td>5880</td>
</tr>
<tr>
<td>Opening</td>
<td>8215</td>
<td></td>
<td>Sundry Debtors – Subscription receivable (considered good)</td>
<td>2105</td>
</tr>
<tr>
<td>Add: Additions</td>
<td>7000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Excess of Income over Expenditure</td>
<td>6400</td>
<td>8045</td>
<td>Stock of Magazine</td>
<td>830</td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>(13570)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

8885 8885

Balance Sheet of Paresh as at 31st March, 2001

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Creditors (Re- Magazines)</td>
<td>900</td>
<td>Cash at Bank</td>
<td>4720</td>
</tr>
<tr>
<td>Capital (Balance Figure)</td>
<td>8215</td>
<td>Cash in Hand</td>
<td>115</td>
</tr>
<tr>
<td>Subscription Receivable</td>
<td></td>
<td>Stock</td>
<td>2450</td>
</tr>
</tbody>
</table>

9115 9115

Working Notes:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Drawings Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
<td>Particulars</td>
</tr>
<tr>
<td>To Cash (Monthly Exp.)</td>
<td>6000</td>
<td>By Capital A/c (Transfer)</td>
</tr>
<tr>
<td>To Bank (Loan to friend)</td>
<td>1200</td>
<td>By Cash (Refund)</td>
</tr>
<tr>
<td>To Bank (Car)</td>
<td>3750</td>
<td></td>
</tr>
<tr>
<td>To Bank (Personal Payment)</td>
<td>2350</td>
<td></td>
</tr>
<tr>
<td>To Other Expenses (Rent)</td>
<td>720</td>
<td></td>
</tr>
<tr>
<td>To Subscriptions (Car)</td>
<td>250</td>
<td></td>
</tr>
</tbody>
</table>

14270 14270

Dr.                  | Debtors (Re-Subscriptions) Account | Cr.          |
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
<td>Particulars</td>
</tr>
<tr>
<td>To Balance b/d</td>
<td>1830</td>
<td>By Cash</td>
</tr>
<tr>
<td>To Subscriptions A/c (bal. fig.)</td>
<td>22020</td>
<td>By Bank</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Bad Debts (Subscriptions – W/O)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Drawings (Re. Car)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d</td>
</tr>
</tbody>
</table>

23850 23850
### Question 4:

From the following details prepare **Balance Sheet of Ever Green Club** as at 31.3.2003:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fixed Assets</strong></td>
<td></td>
<td><strong>Swimming Pool</strong></td>
<td>40,000</td>
</tr>
<tr>
<td><strong>Capital Fund</strong></td>
<td></td>
<td><strong>Equipments</strong></td>
<td>20,000</td>
</tr>
<tr>
<td>Balance</td>
<td>60,000</td>
<td><strong>Furniture</strong></td>
<td>8,000</td>
</tr>
<tr>
<td><strong>Add : Capital Grants</strong></td>
<td>10,000</td>
<td><strong>Less : Deprn.</strong></td>
<td>800</td>
</tr>
<tr>
<td><strong>Legacies</strong></td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Entrance Fees (50%)</strong></td>
<td>2,000</td>
<td><strong>General Fund</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Balance</strong></td>
<td>10,000</td>
<td><strong>Prize Fund</strong></td>
<td>36,000</td>
</tr>
<tr>
<td><strong>Add : Excess of Income</strong> over Expenditure</td>
<td>20,000</td>
<td><strong>Cash &amp; Bank Balances</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Building Fund</strong></td>
<td>30,000</td>
<td><strong>Fixed Deposit</strong></td>
<td>20,000</td>
</tr>
<tr>
<td><strong>Balance</strong></td>
<td>32,000</td>
<td><strong>Current Account</strong></td>
<td>10,000</td>
</tr>
<tr>
<td><strong>Add : Income</strong></td>
<td>1,000</td>
<td><strong>Cash</strong></td>
<td>800</td>
</tr>
<tr>
<td><strong>(800)</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Prize Fund</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Balance</strong></td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Add : Income</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Current Liabilities</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Allowances outstanding</td>
<td>800</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Printers’ Bill outstanding</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Subscription Outstanding</strong></td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Answer:**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Balance Sheet of Evergreen Club <strong>as at 31.3.03</strong></th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Liabilities</strong></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td><strong>Funds</strong></td>
<td></td>
<td><strong>Fixed Assets</strong></td>
</tr>
<tr>
<td>Capital Fund</td>
<td></td>
<td><strong>Swimming Pool</strong></td>
</tr>
<tr>
<td>Balance</td>
<td>60,000</td>
<td>40,000</td>
</tr>
<tr>
<td><strong>Add : Capital Grants</strong></td>
<td>10,000</td>
<td><strong>Equipments</strong></td>
</tr>
<tr>
<td><strong>Legacies</strong></td>
<td>8,000</td>
<td>20,000</td>
</tr>
<tr>
<td><strong>Entrance Fees (50%)</strong></td>
<td>2,000</td>
<td><strong>Furniture</strong></td>
</tr>
<tr>
<td><strong>General Fund</strong></td>
<td></td>
<td>8,000</td>
</tr>
<tr>
<td><strong>Balance</strong></td>
<td>10,000</td>
<td><strong>Less : Deprn.</strong></td>
</tr>
<tr>
<td><strong>Add : Excess of Income</strong> over Expenditure</td>
<td>20,000</td>
<td>800</td>
</tr>
<tr>
<td><strong>Building Fund</strong></td>
<td></td>
<td><strong>General Fund</strong></td>
</tr>
<tr>
<td><strong>Balance</strong></td>
<td>30,000</td>
<td><strong>Prize Fund</strong></td>
</tr>
<tr>
<td><strong>Add : Income</strong></td>
<td>2,000</td>
<td>36,000</td>
</tr>
<tr>
<td><strong>(800)</strong></td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td><strong>Prize Fund</strong></td>
<td></td>
<td><strong>Cash &amp; Bank Balances</strong></td>
</tr>
<tr>
<td><strong>Balance</strong></td>
<td>10,000</td>
<td><strong>Fixed Deposit</strong></td>
</tr>
<tr>
<td><strong>Add : Income</strong></td>
<td>1,000</td>
<td><strong>Current Account</strong></td>
</tr>
<tr>
<td><strong>(800)</strong></td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td><strong>Current Liabilities</strong></td>
<td></td>
<td><strong>Cash</strong></td>
</tr>
<tr>
<td>Allowances outstanding</td>
<td>800</td>
<td></td>
</tr>
<tr>
<td>Printers’ Bill outstanding</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td><strong>Subscription Outstanding</strong></td>
<td>10,000</td>
<td></td>
</tr>
</tbody>
</table>

| Total                                         | 1,54,000                                           | 1,54,000              |
**Financial Accounting Fundamentals**

**Question 5:**

Surya Trust runs a charitable hospital and a dispensary and for the year ended 31.3.98, the following balances were extracted from its books:

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Fund</td>
<td>18,00,000</td>
<td></td>
</tr>
<tr>
<td>Donation received in the year</td>
<td>12,00,000</td>
<td></td>
</tr>
<tr>
<td>Fees received from patients</td>
<td>6,00,000</td>
<td></td>
</tr>
<tr>
<td>Recovery for amenities — rent etc.</td>
<td>5,50,000</td>
<td></td>
</tr>
<tr>
<td>Recovery for food supplies</td>
<td>2,80,000</td>
<td></td>
</tr>
<tr>
<td>Surgical equipments</td>
<td>9,10,000</td>
<td></td>
</tr>
<tr>
<td>Buildings, theatres etc.</td>
<td>6,40,000</td>
<td></td>
</tr>
<tr>
<td>Consumption of —</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medicines</td>
<td>2,40,000</td>
<td></td>
</tr>
<tr>
<td>Foodstuffs</td>
<td>1,80,000</td>
<td></td>
</tr>
<tr>
<td>Chemicals etc.</td>
<td>60,000</td>
<td>4,80,000</td>
</tr>
<tr>
<td>Closing Stock of:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medicines etc.</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Foodstuffs</td>
<td>8,000</td>
<td></td>
</tr>
<tr>
<td>Chemicals etc.</td>
<td>2,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Sales of Medicines (dispensary)</td>
<td></td>
<td>6,20,000</td>
</tr>
<tr>
<td>Opening Stock of Medicines (dispensary)</td>
<td>1,10,000</td>
<td></td>
</tr>
<tr>
<td>Purchases of medicines (dispensary)</td>
<td>6,00,000</td>
<td></td>
</tr>
<tr>
<td>Salaries:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Administrative staff</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Doctors, nurses, etc.</td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td>Assistants at dispensary</td>
<td>30,000</td>
<td>3,90,000</td>
</tr>
<tr>
<td>Electricity and power charges etc.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hospital</td>
<td>2,10,000</td>
<td></td>
</tr>
<tr>
<td>Dispensary</td>
<td>4,000</td>
<td>2,14,000</td>
</tr>
<tr>
<td>Furniture, fittings and equipments</td>
<td>1,60,000</td>
<td></td>
</tr>
<tr>
<td>Ambulance</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Postage, telephone charges etc. less recovery</td>
<td>52,000</td>
<td></td>
</tr>
<tr>
<td>Subscription to medical journals</td>
<td>42,000</td>
<td></td>
</tr>
<tr>
<td>Ambulance maintenance charges less recoveries</td>
<td></td>
<td>1,600</td>
</tr>
<tr>
<td>Consumption of linen, bedsheets, etc.</td>
<td>1,80,000</td>
<td></td>
</tr>
<tr>
<td>Fixed Deposit (made on 10.8.96 for 3 yrs. at @ 11%p.a. interest)</td>
<td>10,00,000</td>
<td></td>
</tr>
<tr>
<td>Cash in hand</td>
<td>12,100</td>
<td></td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>70,500</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors (dispensary)</td>
<td>1,21,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors (dispensary)</td>
<td></td>
<td>82,000</td>
</tr>
<tr>
<td>Remuneration to trustees, trust office expenses etc.</td>
<td>42,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>51,33,600</td>
<td>51,33,600</td>
</tr>
</tbody>
</table>
Accounting for Non-Profit Organisations

Additional information:

(i) The dispensary supplies medicines to Hospital on requisitions and delivery notes; for which no adjustment has been made in the books. Cost of such supplies in the year was Rs. 1,20,000.

(ii) Stock of medicines at close at dispensary was Rs. 80,000;

(iii) Donations were received towards the corpus of the trust;

(iv) Stock of medicines on 31st March, 1998 at the Hospital included Rs. 8,000 worth of medicines belonging to patients; this has not been considered in arriving of the figure of consumption of medicines;

(v) One of the well-wishers donated Surgery Equipment, whose market value was Rs. 80,000 on 15th August, 1997;

(vi) The Hospital is to receive a grant of 25% of the amount spent on treatment of poor patients from the local branch of the Red Cross Society. Such expenditure in the year was Rs. 1 lakh.

(vii) Out of the fees recovered from the patients, 10% is to given to specialists as retained.

(viii) Depreciations on assets, on closing balances, is to be provided on:

- Surgical Equipments 20%
- Buildings 5%
- Furniture and fittings 10%
- Ambulance 30%

Prepare the Income and Expenditure Account of the dispensary, Trust and the Hospital for the year ended 31st March, 1998 and statement of affairs of the Trust as at that date.

Answer:

### SURYA TRUST

**Income & Expenditure Account for the year ended 31st March, 1998**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr. Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To</td>
<td>Opening stock</td>
<td>1,10,000</td>
<td>By Sales</td>
<td>6,20,000</td>
</tr>
<tr>
<td>To</td>
<td>Purchases</td>
<td>6,00,000</td>
<td>By Issues to Hospital</td>
<td>1,20,000</td>
</tr>
<tr>
<td>To</td>
<td>Gross Profit</td>
<td>1,10,000</td>
<td>By Closing stock</td>
<td>80,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>8,20,000</td>
<td></td>
<td>8,20,000</td>
</tr>
<tr>
<td>To</td>
<td>Salaries</td>
<td>30,000</td>
<td>By Gross Profit</td>
<td>1,10,000</td>
</tr>
<tr>
<td>To</td>
<td>Electric charges</td>
<td>4,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Net Profit t/d to General Trust Income &amp; Expenditure A/c</td>
<td>76,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,10,000</td>
<td></td>
<td>1,10,000</td>
</tr>
</tbody>
</table>
### Financial Accounting Fundamentals

#### DR. General Trust A/c CR.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Deficit in Hospital A/c</td>
<td>2,67,400</td>
<td>By Profit from Dispensary</td>
<td>76,000</td>
</tr>
<tr>
<td>To Postage, Telephone charges, etc</td>
<td>52,000</td>
<td>By Interest due on</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Fixed Deposit</td>
<td>1,10,000</td>
</tr>
<tr>
<td>To Trustees &amp; Remuneration expns., etc</td>
<td>42,000</td>
<td>By Net Deficit for the year</td>
<td>1,75,400</td>
</tr>
<tr>
<td></td>
<td>3,61,400</td>
<td></td>
<td>3,61,400</td>
</tr>
</tbody>
</table>

#### DR. Hospital A/c CR.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Consumption of:</td>
<td></td>
<td>By Fees recovered from patients</td>
<td>6,00,000</td>
</tr>
<tr>
<td>Medicines</td>
<td>3,68,000</td>
<td>By Recovery for room rent etc.</td>
<td>5,50,000</td>
</tr>
<tr>
<td>Food stuffs</td>
<td>1,80,000</td>
<td>By Recovery from Food supplied</td>
<td>2,80,000</td>
</tr>
<tr>
<td>Chemicals etc.</td>
<td>60,000</td>
<td>By Ambulance receipts (Net)</td>
<td>1,600</td>
</tr>
<tr>
<td></td>
<td>6,08,000</td>
<td>By Grants receivable from Red Cross</td>
<td>25,000</td>
</tr>
<tr>
<td>To Salaries to:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Doctors, Nurses etc.</td>
<td>3,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Administrative Staff</td>
<td>60,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Returns due to specialists</td>
<td>60,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Electricity &amp; Power charges</td>
<td>2,10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Subscription to Medical Journals</td>
<td>42,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Consumption of linen</td>
<td>1,80,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Depreciation of: —</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Surgical equipments @ 20%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>on Rs. 9,90,000</td>
<td>1,98,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Building @ 5%</td>
<td>32,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Furniture &amp; fits. @ 10%</td>
<td>16,000</td>
<td>By Excess of Expenditure</td>
<td></td>
</tr>
<tr>
<td>Ambulance @ 30%</td>
<td>18,000</td>
<td>over Income</td>
<td>2,67,400</td>
</tr>
<tr>
<td></td>
<td>2,64,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>17,24,000</td>
<td></td>
<td>17,24,000</td>
</tr>
</tbody>
</table>

### STATEMENT OF AFFAIRS as at 31.3.98  
(figures in Rs. ’000)

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capital Fund:</strong></td>
<td></td>
</tr>
<tr>
<td>As on 1.7.97</td>
<td>1800</td>
</tr>
<tr>
<td>Add: Donation received</td>
<td>1200</td>
</tr>
<tr>
<td>Add: Market value of gift of Equipment</td>
<td>80 3080</td>
</tr>
<tr>
<td>Less: Deficit for the year</td>
<td>175.4 121</td>
</tr>
<tr>
<td></td>
<td>2904.6 Grant due from Red Cross</td>
</tr>
<tr>
<td><strong>Cash in hand:</strong></td>
<td>12.1</td>
</tr>
<tr>
<td><strong>Cash at Bank:</strong></td>
<td></td>
</tr>
<tr>
<td>On Current A/c</td>
<td>70.5</td>
</tr>
<tr>
<td>On Fixed Deposit</td>
<td>1070.5</td>
</tr>
<tr>
<td>Interest accrued on F. D.</td>
<td>110</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>121</td>
</tr>
</tbody>
</table>

---

**STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION**
Accounting for Non-Profit Organisations

Sundry Creditors :
- For Medicine supplied 82
- For retainer due to specialists 60

Stocks of goods –
- Medicines (Dispensary) 80

Hospital :
- Medicines 32
- Food 8
- Chemicals 2

Surgical Equipments :
- (as on 1.4.97) 910
- Gift received 80
- Gift received 990

Less : Depreciation 198 792

Building, Theatre etc :
- as on 1.4.97 640
- Less : Depreciation 32 608

Furniture & Fittings etc. :
- as on 1.4.97 160
- Less : Depreciation 16 144

Ambulance :
- as on 1.4.97 60
- Less : Depreciation 18 42.0

3046.6 3046.6

3.3 SELF-EXAMINATION QUESTIONS

1. Distinguish, giving examples, between Receipts and Payment Account and Income and Expenditure Accounts.

2. Do you consider the following to be Capital or Revenue item? Give reasons.
   (i) A motor car, whose book value is Rs. 10,000 and was sold for Rs. 15,000, thus making a gain of Rs. 5,000.
   (ii) Legal expenses incurred in raising a debenture loan.
   (iii) Rs. 15,000 was paid as compensation to a discharged employee.
   (iv) The removal of stock from old works to new works costed Rs. 5,000.
Financial Accounting Fundamentals

3. The Secretary of the Systematic Club has prepared the following draft Balance Sheet of the club as at 30.9.1995:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capital Account:</strong></td>
<td></td>
<td><strong>Fixtures &amp; Fittings:</strong></td>
<td></td>
</tr>
<tr>
<td>Balance as on 30.9.95</td>
<td>14,300</td>
<td>As on 30.09.95</td>
<td>10,600</td>
</tr>
<tr>
<td>Less: Loss for the year</td>
<td>2,100</td>
<td>Less: Depreciation for the year</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>12,200</td>
<td></td>
<td>9,600</td>
</tr>
<tr>
<td>Subscription in advance</td>
<td>600</td>
<td>Stock</td>
<td>3,200</td>
</tr>
<tr>
<td>Creditors</td>
<td>2,400</td>
<td>Debtors</td>
<td>1,400</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Balance at bank</td>
<td>950</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash in hand</td>
<td>50</td>
</tr>
<tr>
<td></td>
<td>15,200</td>
<td></td>
<td>15,200</td>
</tr>
</tbody>
</table>

You ascertain the following:

1. The amount of loss was only a balancing figure as the books had been kept on a single entry basis.
2. The balance at bank was that shown by the bank statement at the close of the business on 30.9.95.
3. The following amounts had been paid into bank on 30.09.95 but had not been credited by the bank:
   (i) Two cheques of Rs. 50 each had been cashed for a member - one had since been duly honoured but the other had been returned marked “refer to drawer” and, on being approached, the member repaid Rs. 50 in cash;
   (ii) A member’s subscription of Rs. 80 for the year 1995-96.
4. The following cheques had been drawn in September but had not been presented until October:
   (i) Rs. 480 for bar supplies which had been delivered but had not been included in stock;
   (ii) Rs. 350 for additional typewriter received on October 2;
   (iii) Rs. 100 as bonus of the professional included under the creditors;
   (iv) Rs. 140 for fuel which had been included in the stock figure but not in the creditors and this cheque was dated October 1.

You are required to prepare:

(a) a bank reconciliation statement as on 30.9.95, and
(b) a revised Balance Sheet as on the date to give effect to the consequential adjustments, assuming that otherwise the items in the draft Balance sheet were correct.
**COMPANY ACCOUNTS**

### 4.0 INTRODUCTION TO COMPANY ACCOUNTS

#### 4.1 CONCEPT OF SHARE CAPITAL

Money required by a company to commence and carry on its operations is raised by issuing shares and debentures. Although there are other sources of raising funds (like acceptance of public deposits, taking bank loans, etc.), issue of shares is the bulk of fund requirement by a company.
The term ‘Share Capital of a company’ can be used in the following concepts :-

1. **Authorised Capital**: This presents the value of shares with which a company is registered.

2. **Issued Capital**: This means the portion of authorised capital that is being offered for public subscription.

3. **Subscribed Capital**: This presents that portion of issued Capital that is being taken up by public.

4. **Called up Capital**: This represents that part of subscribed capital that the directors have decided to call up from the subscriber to satisfy the monetary needs of the company.

5. **Paid up Capital**: That portion of called up capital that is being actually paid in cash by the shareholders.

**Types of Shares**

A company can issue two types of shares :-

1. **Preference shares** :

   Preference shares carry a fixed rate of dividend which is to be paid before distribution of Equity Dividend. At the time of winding up of the company the claim of preference shares towards repayment of capital has to be satisfied before satisfying claim of Equity Shareholders. Preference share holders can neither get the Notice of A.G.M nor they are able to take part in deliberation of the meeting except when their dividend has remained unpaid for a specified number of years.

   Preference shares can be cumulative or noncumulative. In the first case the unpaid preference dividend accumulates over the years and has to be paid in later years when there is adequate profit. This condition does not exists in case of noncumulative preference shares.

   Under the Companies (Amendment) Act, 1988, preference shares issued by a company has to be redeemed within 10 years from the date of issue.

2. **Equity shares**:

   Equity shares are those which are not preference shares. They do not carry any specific rate of dividend; i.e. the rate of dividend can vary over the years depending on the sufficiency of profit. They are allowed to get notice and attend the A.G.M. of the company.
Company Accounts

Books of Account of a Company

According to Section 209 of the Companies Act, 1956:

— Every Company shall keep at its registered Office proper books of account with respect to:
  (a) all sums of money received and expended by the Company and the matters in respect of which the receipt and expenditure take place;
  (b) all sales and purchases of goods by the Company;
  (c) the Assets and Liabilities of the Company;
  (d) in the case of a Company pertaining to any class of Companies engaged in production, processing, manufacturing or mining activities, such particulars relating to utilisation of materials or labour or to other items of cost as may be prescribed, if such class of Companies is required by the Central Government to include such particulars, in the books of account.

Provided that all or any of the books of account aforesaid may be kept at such other place in India as the Board of Directors may decide and the company shall, within 7 days of the decision, file with the Registrar a Notice in writing giving the full address of that other place.

— If proper books of account relating to the transactions effected at the branch office are kept at that Office and proper summarised returns, made up to date at intervals of not more than 3 months are sent by the branch office or the other place as decided upon.

— Proper books of account shall not be deemed to be kept with respect to the matters specified therein:
  (a) if there are not kept such books as are necessary to give a true and fair view of the state of affairs of the Company or branch office, as the case may be and to explain its transactions.
  (b) if such books are not kept on accrual basis and according to the double entry system of accounting.

— The books of account and other papers shall be open to inspection by any director during business hours.

— The books of account of every Company relating to a period of not less than 8 years immediately preceding the current year together with the vouchers shall be preserved in good order.
4.2 ISSUE OF SHARES

Issue of shares involves the following steps:

1. Issue of prospectus including people to take up shares
2. Receiving applications along with application money.
3. Allotment of shares
4. Making calls on shares as decided by the Board of Directors.
5. Issue and despatch of share certificate.

Journal Entries for issue of Shares

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr. (reason)</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) on receipt of application money:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank A/c</td>
<td>Dr.</td>
<td></td>
</tr>
<tr>
<td>To Share Application A/c</td>
<td>[No. of shares applied × Rate]</td>
<td></td>
</tr>
<tr>
<td>2) on allotment of shares:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Application A/c</td>
<td>Dr.</td>
<td></td>
</tr>
<tr>
<td>[No. of shares applied × Rate]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Share Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3) For rejection of some applications:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Application A/c</td>
<td>Dr.</td>
<td></td>
</tr>
<tr>
<td>[No. of shares rejected × Rate]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Share Capital A/c</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: Shares can be issued at premium which may be receivable either at the time of application or allotment; the Journal Entries then will be:

a) When Premium is receivable along with application:
   i) Bank A/c  [Total receipt including premium]  Dr.
      To Share Application
   ii) Share Application A/c  [No. of shares issued × Rate]  Dr.
      To Share Capital  [No. of shares issued × Rate towards face value]
      To Share Premium  [premium / share × No. of shares issued]

b) When premium is receivable at the time of allotment.
   i) Share Allotment A/c  Dr.
      To Share Capital
      To Share Premium.
   ii) Bank A/c  Dr.
      To Share Allotment
5) **Making and Receipt of Calls**: The Balance due towards face value of shares after receiving application and allotment money can be recovered by making as many calls as the directors decide. The entries should be:

1) **For Call Money due:**

   Share Call A/c \( [\text{No. of shares Issued} \times \text{Rate}] \) Dr.

   To Share Capital.

2) **For Call money received**

   Bank A/c Dr.

   To Share Call A/c

6) **Treatment of calls-in-arrear**: The terms denote failure on part of some shareholders to make payment of any call due on the shares taken up by him. The following entry should be passed in every case of such default.

   Call-in-arrear A/c \( [\text{No. of defaulted shares} \times \text{Rate}] \) Dr.

   To (Respective) Call A/c.

   In case shares are not forfeited the Total balance of call-in-arrear A/c should be deducted from Share Capital A/c in the Balance Sheet.

**Treatment of call-in-advance**

When some shareholders make excess payment in respect of any instalment due on his shares the excess amount may be retained by the company and adjusted against subsequent calls. The Journal Entries would be:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>(reason)</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Share Call (1) ( [\text{No. of shares Issued} \times \text{Rate}] ) Amount due on call/share</td>
<td>Dr.</td>
<td>(reason)</td>
<td>Share Capital (original call made).</td>
</tr>
<tr>
<td>2) Bank A/c Dr. (Total receipt)</td>
<td>To Share Call (1) A/c ( [\text{No. of shares} \times \text{Due on call/per share}] ) To Calls-in-advance ( [\text{Excess amount received}] )</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3) Share Call (2) A/c ( [\text{No. of shares issued} \times \text{Amount due on call/per share}] )</td>
<td>Dr.</td>
<td></td>
<td>Share Capital</td>
</tr>
<tr>
<td>4) Bank A/c (Balance)</td>
<td>Dr.</td>
<td></td>
<td>Calls-in-advance A/c ( [\text{Excess amount received on prior call}] ) Dr.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>To share call (2) A/c ( [\text{No. of shares issued} \times \text{amount due/per Share}] )</td>
</tr>
</tbody>
</table>

Unadjusted calls in advance should be shown on Liability side of Balance Sheet.
Financial Accounting Fundamentals

Issue of shares at a discount

For issuing shares at discount the following conditions are to be satisfied: (u/s 79 of Companies Act)

1) Discount should be given on such classes of shares already issued by the Company.
2) The decision to issue shares at discount will be taken by passing a resolution at the A.G.M.
3) The company must be at least one year of age.
4) Without approval of CLB the maximum rate of discount must not exceed 10% of face value.
5) Sanction of CLB to such discounted issue must be obtained within two months after such issue or within two months after such issue or within such extended period as may be granted by the CLB.

JOURNAL ENTRY

<table>
<thead>
<tr>
<th>Share Allotment A/c</th>
<th>Dr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discount on Issue of Share A/c</td>
<td>Dr.</td>
</tr>
<tr>
<td>To Share Capital</td>
<td></td>
</tr>
</tbody>
</table>

Note: The above entry assumes the adjustment of discount at the time of allotment.

Illustration 1:

Bat and Ball Ltd. issued 50,000 Equity Shares of Rs. 100 each. These were payable as to Rs. 20 on Application, Rs. 30 on Allotment and the balance will be paid as and when called for by Directors. Applications were received for 70,000 shares. The Directors made the allotment as follows:

- To applicants of 30,000 shares — Full allotment
- To applicants of 30,000 shares — 20,000 shares
- To applicants of 10,000 shares — Application money refunded

Give journal entries for the above assuming all the money due on allotment has been received and no call has been made.
### Company Accounts

**Solution** :

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank Account Dr. 14,00,000</td>
<td></td>
<td>14,00,000</td>
</tr>
<tr>
<td>To Share Application A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being Application money received on 70,000 shares @ Rs. 20 per share)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Application A/c Dr. 10,00,000</td>
<td></td>
<td>10,00,000</td>
</tr>
<tr>
<td>To Share Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being Application money transferred to Share Capital Account as per Board’s Resolution Dated.........)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Application A/c Dr. 2,00,000</td>
<td></td>
<td>2,00,000</td>
</tr>
<tr>
<td>To Bank Account</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being the application money on 10,000 shares @ Rs. 20 per Share refunded as Shares were not allotted as per Board’s Resolution No. Dated.........)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Allotment Account Dr. 15,00,000</td>
<td></td>
<td>15,00,000</td>
</tr>
<tr>
<td>To Share Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being the Capital Account money due on 50,000 shares @ Rs.30 per share as per Board’s Resolution dated...........)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Application Account Dr. 2,00,000</td>
<td></td>
<td>2,00,000</td>
</tr>
<tr>
<td>To Share Allotment A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being surplus Application money on 10,000 shares transferred to Share Allotment A/c as per Board’s Resolution dated...........)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank A/c Dr. 13,00,000</td>
<td></td>
<td>13,00,000</td>
</tr>
<tr>
<td>To Share Allotment A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Being the receipt of the amount due on allotment Rs. 15,00,000 – 2,00,000)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
4.3 FORFEITURE AND REISSUE OF SHARES

Forfeiture of shares:
The shares allotted to a subscriber who has defaulted in paying any call due on his shares can be forfeited by decision of the Board of Directors if empowered by the articles of the company after giving due notice to the defaulting shareholders. This power of Board of Directors has to be applied bonafide and in the interest of the company.

Journal Entries for Forfeiture
Share Capital A/c Dr. 
[No. of share forfeited ‘×’ Amount called up per share]
To Calls in Arrear [total amount of dues not collected on forfeited shares]
To Share Forfeiture A/c [amount collected on forfeited shares]

If forfeited shares are issued at a premium and such premium is not received then the entry should be:
Share Capital A/c Dr.
Share Premium A/c Dr.
To Calls-in-arrear A/c
To Share Forfeiture A/c


1) Bank A/c Dr. (Amount actually received)
   Share Forfeiture A/c Dr. (Discount on Reissue)
   To Share Capital A/c (Face value of share)

2) If balance of Share Forfeiture A/c exceeds discount on Reissue, the Balance should be treated as a Capital profit which is computed on follows :-
   Amount forfeited × No. of shares reissued - Discount on No. of forfeited shares reissued. × no. of shares.

The Journal Entry will be:
1) Share Forfeited A/c Dr.
To Capital Reserve

Note:
The forfeited amount on unissued shares will be shown in Balance Sheet as an addition to share capital.
Company Accounts

Prorata Allotment

In case of over subscription the company can either reject the excess applications or make proportionate allotment to all applicants. The second case is called prorata allotment. The excess money received on application is adjusted against subsequent calls:

Entries

Share Application A/c Dr.
To Subsequent Calls A/c

Illustration 2:

Kamnasib Ltd. issued 400000 equity shares of Rs. 10 each at a premium of Rs. 20 per share. The amounts were receivable as follows:

<table>
<thead>
<tr>
<th>On</th>
<th>Capital Rs.</th>
<th>Premium Rs.</th>
<th>Total Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Application</td>
<td>1</td>
<td>9</td>
<td>10</td>
</tr>
<tr>
<td>Allotment</td>
<td>2</td>
<td>8</td>
<td>10</td>
</tr>
<tr>
<td>Final call</td>
<td>7</td>
<td>3</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>10</td>
<td>20</td>
<td>30</td>
</tr>
</tbody>
</table>

All members except Mr. Unfortunate paid the amounts due to allotment and call. Mr. Unfortunate who was allotted 300 shares failed to pay call money. His shares were forfeited after due compliance with law.

These shares were reissued to Hopeful at a price of Rs. 25 per share.

You are asked to pass the journal entries on:

(a) Forfeiture
(b) Reissue

Also show the presentation in balance sheet before and after forfeiture and after reissue.
### Solution:

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1) Equity Share Capital (at Rs. 10/-)</strong></td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>Share Premium (at Rs. 3)</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td>To Share Final Call (at Rs. 10)</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>To Forfeited Shares A/c.</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td>(Being forfeiture of 300 shares numbered... held by Unfortunate for non payment of final call of Rs. 10, the amount received on capital account on application (Rs. 1) and allotment (Rs. 2) being credited to Forfeited Shares A/c vide Board Resolution dt.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>2) Bank.</strong></td>
<td>7,500</td>
<td></td>
</tr>
<tr>
<td>Forfeited Shares</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>” Share Premium</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td>” Capital Reserve</td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td>(Being reissue at Rs. 25 per share of 300 Equity Shares numbered to Hopeful vide board resolution dt....)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Extract from Balance Sheet (before forfeiture)

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Equity Share Capital</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issued : For cash</td>
<td>40,00,000</td>
<td></td>
</tr>
<tr>
<td>400000 Equity Shares of Rs. 10 each fully Called up.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less : Calls-in-arrear</td>
<td>2,100</td>
<td></td>
</tr>
<tr>
<td>39,97,900</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Reserves and Surplus :</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Premium.</td>
<td>80,00,000</td>
<td></td>
</tr>
<tr>
<td>Less : Calls in-arrear</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td>79,99,100</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Extract from balance sheet (after forfeiture)

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Equity Share Capital :</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issued : For Cash.</td>
<td>39,97,000</td>
<td></td>
</tr>
<tr>
<td>399700 Equity Shares of Rs. 10 each fully paid</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add : Forfeited shares.</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td>39,97,900</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Company Accounts

Reserve and surplus:
Share Premium:
As per last Balance Sheet. 79,99,100

Rs. Rs.

Extract from balance sheet (after reissue)

Equity Share Capital:
Issued: For cash.
400000 Equity Shares of Rs. 10 each fully paid. 40,00,000

Reserve and surplus:
Capital Reserve:
Profit on reissue of forfeited equity shares. 4,500
Share Premium:
As per last Balance Sheet. 79,99,100
Add: Received on reissue of forfeited shares. 900
80,04,500

Illustration 3:

ABC Limited offered for public subscription 2,000 Equity shares of Rs. 100 each at a premium of Rs. 20 per share on the following terms:

(a) Applications money to be paid before 30th June, 2000; Rs. 40 per share.
(b) Allotment money to be paid before 20th September, 2000; Rs. 50 per share including Rs. 20 premium.
(c) First and final call money to be paid before 31st December, 2000; Rs. 30 per share.

Applications for 4,000 shares were received, the Company decided to:

(i) Allot in full 200 shares to 4 applicants who had applied for the same.
(ii) Reject the application for 1,400 shares applied for by persons suspected to be agents of a rival company.
(iii) Allot the balance number of shares proportionately, to the remaining applicants, and to apply the excess money paid towards the allotment money dues.

Ravi who had applied for 100 shares and who was allotted all the shares applied for could not pay allotment money. Ruby who was allotted 60 shares on the proportion basis could not pay the final call. After due notices all such shares were forfeited and reissued at a discount of 20% of the face value of the share of Mr. Reddy.

Pass the necessary journal entries to record the above transactions in the books of the Company.
Solution:

Working Notes:

1. Issue of 2,000 equity shares of Rs. 100 each at Rs. 20 premium.
   For application of Rs. 40
   Amount received = 4000 × Rs. 40 = Rs. 1,60,000
   
<table>
<thead>
<tr>
<th>Application</th>
<th>Allotment</th>
</tr>
</thead>
<tbody>
<tr>
<td>200</td>
<td>200</td>
</tr>
<tr>
<td>1,400</td>
<td>Rejected</td>
</tr>
<tr>
<td>2,400 (4:3)</td>
<td>1,800</td>
</tr>
<tr>
<td>4,000</td>
<td>2,000</td>
</tr>
</tbody>
</table>

2. For Allotment:
   Refund of application = 1,400 × Rs. 40 = Rs. 56,000
   Excess application amount = 600 × Rs. 40 = Rs. 24,000
   Amount due = 2,000 × Rs. 50 = Rs. 1,00,000
   Amount received:
   
<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount due</td>
</tr>
<tr>
<td>Less : Already received</td>
</tr>
<tr>
<td>Less : Calls in arrears (Ravi) (100×50)</td>
</tr>
<tr>
<td>Amount received</td>
</tr>
</tbody>
</table>

3. For first and final call: (Rs. 30)
   Amount due = 2,000 × 30 = Rs. 60,000
   Amount received:
   
<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount due</td>
</tr>
<tr>
<td>Less : Calls in arrears :</td>
</tr>
<tr>
<td>Ravi (100×30)</td>
</tr>
<tr>
<td>Ruby (60×30)</td>
</tr>
<tr>
<td>Amount received</td>
</tr>
</tbody>
</table>
**Company Accounts**

In the books **ABC Ltd.**

<table>
<thead>
<tr>
<th>JOURNAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
</tr>
<tr>
<td>1. Cash/Bank A/c</td>
</tr>
<tr>
<td>To Share Application A/c</td>
</tr>
<tr>
<td>(Being application money received)</td>
</tr>
<tr>
<td>2. Share Application A/c</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
</tr>
<tr>
<td>To Cash/Bank A/c</td>
</tr>
<tr>
<td>To Share Allotment A/c</td>
</tr>
<tr>
<td>(Being application money received transferred to various latter A/c as per Board Resolution No. ...., dated .......)</td>
</tr>
<tr>
<td>3. Share Allotment A/c</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
</tr>
<tr>
<td>To Security Premium A/c</td>
</tr>
<tr>
<td>(Being allotment of shares as per Board Resolution No. ..... dated .......)</td>
</tr>
<tr>
<td>4. Cash/Bank A/c</td>
</tr>
<tr>
<td>Calls in-arrear A/c</td>
</tr>
<tr>
<td>To Share Allotment A/c</td>
</tr>
<tr>
<td>(Being allotment received on allotment and calls in arrear on allotment of shares)</td>
</tr>
<tr>
<td>5. First and Final Call A/c</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
</tr>
<tr>
<td>(Being first and final call made as per Board Resolution No. ..... dated .......)</td>
</tr>
<tr>
<td>6. Cash/Bank A/c</td>
</tr>
<tr>
<td>Calls in-arrear A/c</td>
</tr>
<tr>
<td>To First and final call A/c</td>
</tr>
<tr>
<td>(Being amount received and calls in arrears on first and final call)</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

7. Equity Share Capital A/c Dr. 16,000
   To Calls in arrears A/c 9,800
   To Share Forfeiture A/c 6,200
   (Being entry for forfeiture of 160 shares as per Board Resolution No.... dated ...)

8. Cash/Bank A/c Dr. 12,800
   Share Forfeiture A/c Dr. 3,200
   To Equity share capital A/c 16,000
   (Being forfeited shares reissued at a discount of Rs.20 as per Board’s Resolution No. Dated....)

9. Share Forfeiture A/c Dr. 3,000
   To Capital Reserve A/c 3,000
   (Being profit on reissue transferred to Capital Reserve account)

Illustration 4:
The following particulars are given for the books and records of M/s Arati Ltd. relating to issue and forfeiture of shares and payable as follows:

- on application Rs. 3 per share
- on allotment Rs. 5 per share (including premium)
- on first and final call Rs. 4 per share

<table>
<thead>
<tr>
<th>Category</th>
<th>No. of shares allotted</th>
<th>No. of shares applied for</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category I</td>
<td>20,000</td>
<td>30,000</td>
</tr>
<tr>
<td>Category II</td>
<td>10,000</td>
<td>10,000</td>
</tr>
<tr>
<td>Category III</td>
<td>Nil</td>
<td>5,000 (Money refunded)</td>
</tr>
</tbody>
</table>

The book value of each share is Rs. 10. Allotment were made prorata in Category I. Mr. Malay Das who applied for 450 shares in Category I failed to pay allotment and call money and his shares were forfeited by directors. Subsequently 200 forfeited shares were reissued to Mr. Badal as fully paid for Rs. 9 per share.

Show the Journal Entries and Cash Book to record the above transactions. Also prepare the Balance Sheet.
Company Accounts

**Solution:**

In the books of Arati Ltd.

**Journal Entries**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Equity Share Application A/c Dr. 1,20,000 To Equity Share Capital A/c 90,000 To Equity Share Allotment A/c 30,000 (Being Application money on 30,000 equity share were transferred and excess 10,000 application money were adjusted with Allotment as per Board Resolution No. &amp; Dated.....)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Equity Share Allotment A/c Dr. 1,50,000 To Equity Share Capital A/c 90,000 To Share Premium A/c 60,000 (Being Allotment money due on 30,000 equity share of Rs. 5 each including Rs. 2 as premium as per Board Resolution No. Dated.....)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Equity Share 1st Call &amp; Final Call A/c Dr. 1,20,000 To Equity Share Capital A/c 1,20,000 (Being Call money due on 30,000 Equity Share @ Rs. 4 per share as per Board Resolution No. Dated.....)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Equity Share Capital A/c Dr. 3,000 Share Premium A/c Dr. 600 To Share Forfeiture A/c 1,350 To Share Allotment A/c 1,050 To Share First &amp; Final Call A/c 1,200 (Being 450 Equity shares were forfeited after nonpayment of Allotment and call money as per Board Resolution No. Dated.....)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Forfeited Share A/c Dr. 200 To Equity Share Capital A/c 200 (Being Discount on Reissue were adjusted)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Forfeited Share A/c Dr. 700 To Capital Reserve A/c 700 (Being Profit on reissue were transferred)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Financial Accounting Fundamentals

#### CASH BOOK (BANK COLUMN)

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Rs.</th>
<th>Cr.</th>
<th>L.F.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>To Equity Share Application A/c</td>
<td>1,35,000</td>
<td></td>
<td>By Equity Share Application</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(45,000 share @ Rs.3 each)</td>
<td></td>
<td></td>
<td>(Excess appl. on 5,000 share refunded)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Sh. Allotment A/c (Note No.1)</td>
<td>1,18,950</td>
<td></td>
<td>By Balance c/d</td>
<td>3,59,550</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share 1st &amp; Final Call A/c</td>
<td>1,18,800</td>
<td></td>
<td></td>
<td>3,74,550</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(29,700 share @ 4 each)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Capital A/c</td>
<td>1,800</td>
<td></td>
<td></td>
<td>3,74,550</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3,74,550</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Balance B/d</td>
<td>3,59,550</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### ARATI LTD.

**Balance Sheet as on .....**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Share Capital</strong></td>
<td></td>
<td><strong>Current Asset</strong></td>
<td></td>
</tr>
<tr>
<td>Issued and paid up Capital</td>
<td>29,90-</td>
<td>Equity share @ Rs. 10 each</td>
<td>3,59,550</td>
</tr>
<tr>
<td>Reserve &amp; Surplus</td>
<td>59,400</td>
<td>Cash at Bank</td>
<td></td>
</tr>
<tr>
<td>Share Premium (60,000–600)</td>
<td>700</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital Reserve</td>
<td>450</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Forfeiture A/c (1,350–900)</td>
<td>3,59,550</td>
<td></td>
<td>3,59,550</td>
</tr>
</tbody>
</table>

**Working Notes :**

1. **Amount Received on Allotment :**
   - Amount due on Allotment 30,000 Share @ 5 each $1,50,000$
   - Less : Amount already adjusted $30,000$
   - Less : Non Receipt of Allotment $1,20,000$
   - Less : Non Receipt of Allotment $1,18,950$

2. **Non Receipt of Allotment :**
   - Amount due on 300 shares (2/3×450) @ 5 each $1,500$
   - Less : Amount paid in excess on Application (150×3) $450$
   - Less : Amount utilised (200×1) $700$

3. **Capital Reserve :**
   - Amount Credited from 200 shares (1,350/300×200) $900$
   - Less : Amount utilised (200×1) $200$

**Note :** Balance amount in Share Forfeiture A/c i.e. (1,350–900) = Rs. 450 kept for further reissue of Balance 100 Equity Shares.
4.4 ISSUE OF BONUS SHARES

Companies with substantial reserve may decide to capitalise a part or whole of such reserves by issuing fully paid up, instead of paying dividend to its share holders.

Sources of Bonus Issue

1. For fully paid up Bonus Shares:
   (a) P/L Account,
   (b) General Reserve,
   (c) Capital Redemption Reserve,
   (d) Share Premium A/c,
   (e) Other free reserves.

2. For partly paid up bonus shares:
   (a) P/L A/c,
   (b) General Reserve,
   (c) Other free Reserves.

Note:

1) Revaluation Reserve is not available for issue of Bonus Shares.
2) Share Premium and Capital Redemption Reserves are not available for issuing partly paid up Bonus shares.

JOURNAL ENTRIES.

For fully paid up Bonus Share issue

1) Reserve A/c Dr. To Bonus to Shareholders
   (Declaration of Bonus as per share holders Resolution No........dated......)

2) Bonus to Shareholders A/c Dr. To Equity Share Capital
   (Issue of ......(no.) of Bonus shares as per Share Holder Resolution No......dated.....)

For issuing partly paid up Bonus shares

a) Share ......CallA/c Dr. To Share Capital
   (Call money due on ......shares @ Rs......)
Financial Accounting Fundamentals

b) Reserves A/c  
To Bonus to Shareholder A/c  
(Declaration of Bonus as per Shareholder resolutions no....dated..)

c) Bonus to Shareholders A/c  
To Share Call A/c  
(Utilisation of Reserves for making partly paid up shares into fully paid up)

Procedure for Issue of Bonus share:
Students are advised to refer to the SEBI Guidelines issued from time to time in this respect. Behind bonus issue

1. Reflection of true earning rate to shareholders funds.
2. Avoidance of monetary outflow involved in distribution of dividend.
3. Improvement of company reputation in the market.

Redemption of Preference shares:
One should refer to Section 80 of Companies Act in this respect which is reproduced below:

1. Only fully paid up shares can be redeemed.
2. Such redemption should be affected either out of the funds obtained from fresh issue of shares or out of the nonspecific reserves of the company.
3. Premium (if any) on redemption shall be paid out of companies past profit or Share Premium A/c.
4. Where such redemption is affected otherwise than out of the proceeds of the fresh issue an amount equal to the nominal value of the shares so redeemed will be transferred termed "Capital Redemption Reserve".

JOURNAL ENTRIES.

1. Preference Share Capital A/c  
[Face value of shares to be redeemed]  
Premium on Redemption A/c  
To Preference Shareholders A/c  
(Amount due on Redemption as well as premium thereon transferred to preference share holders A/c)

2. Bank A/c  
To Share Capital  
(Fresh issue made on finance Redemption).
Company Accounts

**Note:**

1. This entry should be made only when fresh shares are issued.
2. Premium or discount on such issue shall be adjusted in the manner mentioned earlier while discussing issue of shares.
3. **Bank A/c Dr.**
   **To Assets A/c**
   (Sale of Assets to finance redemption)
   **Note:** Any profit or loss on such sale should be adjusted in P/L A/c
4. **Reserve A/c Dr.**
   **To Capital Redemption Reserve**
   \[\text{Face value of shares redeemed} - \text{Face Value of new issue}\]
   (Provision of Sec. 80 of Companies Act)
5) **Preference Shareholders A/c Dr.**
   **To Bank**
   (payment made to preference share holders)
   **Note:** In case some of shareholders could not be found amount due to them should be shown on liability in the Balance Sheet.
6) **Reserve A/c Dr.**
   **To Premium of Redemption A/c**
   \[\text{Premium on redemption adjusted}\]

**Illustration 5:**

The Bharat Steel Co. whose issued share capital on 31st March, 1994, consisted of 6,000 8% redeemable preference shares of Rs. 100 each fully paid and 20,000 equity shares of Rs. 100 each, Rs. 80 paid up, decided to redeem preference shares at a premium of Rs. 10 per share. The Co.’s Balance Sheet as at 31st March, 1994, showed a General Reserve of Rs. 9,00,000 and a Capital Reserve of Rs. 85,000. The redemption was effected partly out of profits and partly out of the proceeds of a new issue of 3,000 7.5% cumulative preference shares of Rs. 100 each at a premium of Rs. 25 per share. The premium payable on redemption met out of the premium received on the new issue. On 1st July, 1994 the company at its General Meeting resoloved that all the capital reserves be applied in the following manner:

(a) The declaration of bonus at the rate of Rs. 20 per share on equity shares for the purpose of making the said shares fully paid; and

(b) The issue of bonus shares to the equity shareholders in the ratio of 1 share for every four shares held.

You are required to pass necessary journal entries.
Solution:

Books of Bharat Steel Co. Ltd.

**JOURNAL**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>31.3.94</td>
<td>8% Preference Share Capital A/c</td>
<td>Dr. 6,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Preference Shareholders A/c</td>
<td></td>
<td>6,00,000</td>
</tr>
<tr>
<td></td>
<td>(Redemption of 6,000 shares due)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.3.94</td>
<td>Premium on Redemption A/c</td>
<td>Dr. 60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To preference Shareholders A/c</td>
<td></td>
<td>60,000</td>
</tr>
<tr>
<td></td>
<td>(Premium due on redemption)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.3.94</td>
<td>Bank A/c</td>
<td>Dr. 3,75,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To 7.5% Preference Share Capital A/c</td>
<td></td>
<td>3,00,000</td>
</tr>
<tr>
<td></td>
<td>To Share Premium A/c</td>
<td></td>
<td>75,000</td>
</tr>
<tr>
<td></td>
<td>(Issue of Preference shares at 25% premium)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.3.94</td>
<td>General Reserve A/c</td>
<td>Dr. 3,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Capital Redemption Reserve A/c</td>
<td></td>
<td>3,00,000</td>
</tr>
<tr>
<td></td>
<td>(Provision of s. 80 of Companies Act met)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.3.94</td>
<td>Preference Shareholders A/c</td>
<td>Dr. 6,60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bank A/c</td>
<td></td>
<td>6,60,000</td>
</tr>
<tr>
<td></td>
<td>(Payments to Preference Shareholders)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.3.94</td>
<td>Share Premium A/c</td>
<td>Dr. 60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Premium on Redemption A/c</td>
<td></td>
<td>60,000</td>
</tr>
<tr>
<td></td>
<td>(Transfer entry)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1.7.94</td>
<td>Equity Share Final Call A/c</td>
<td>Dr. 4,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Capital A/c</td>
<td></td>
<td>4,00,000</td>
</tr>
<tr>
<td></td>
<td>(Call made on 20,000 shares @ Rs. 20 per share)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1.7.94</td>
<td>General Reserve A/c</td>
<td>Dr. 4,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bonus Dividend A/c</td>
<td></td>
<td>4,00,000</td>
</tr>
<tr>
<td></td>
<td>(Bonus issued @ Rs. 20 per share)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1.7.94</td>
<td>Bonus Dividend A/c</td>
<td>Dr. 4,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Final Call A/c</td>
<td></td>
<td>4,00,000</td>
</tr>
<tr>
<td></td>
<td>(Issue of Bonus Share by conversion of partly paid up shares into fully paid up.)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Company Accounts

1.7.94 Capital Redemption Reserve A/c Dr. 3,00,000
  Share Premium A/c Dr. 15,000
  Capital Reserve A/c Dr. 85,000
  General Reserve A/c Dr. 1,00,000
  
  To Bonus Dividend A/c 5,00,000
  (Declaration of bonus as per Shareholders Resolution
  No.....dated.....)

1.7.94 Bonus Dividend A/c Dr. 5,00,000
  To Equity Share Capital A/c 5,00,000
  (Issue of 5,000 Equity shares as bonus)

Illustration 6:

The following is the Balance Sheet of TOM Ltd. as at 31.03.1997:

TOM Ltd.
Balance Sheet as at 31st March, 1997

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital – Fixed Assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Authorised 5000 10% Redeemable</td>
<td></td>
<td></td>
<td>Gross Block</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>Preference Share of Rs. 10 each</td>
<td>50,000</td>
<td></td>
<td>Less : Depreciations</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>45,000 Equity Shares of Rs. 10 each</td>
<td>4,50,000</td>
<td></td>
<td>Investments</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>5,00,000</td>
<td></td>
</tr>
<tr>
<td>Issued, Subscribed and paid-up Capital</td>
<td></td>
<td></td>
<td>Inventory</td>
<td>12,500</td>
<td></td>
</tr>
<tr>
<td>5000 10% Redeemable</td>
<td></td>
<td></td>
<td>Debtors</td>
<td>12,500</td>
<td></td>
</tr>
<tr>
<td>Preference Shares of Rs. 10 each</td>
<td>50,000</td>
<td></td>
<td>Cash and Bank Balances</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>5000 Equity Shares of Rs. 10 each</td>
<td>50,000</td>
<td></td>
<td>Misc. Expenditure to the extent not written off</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Reserves and surplus</td>
<td></td>
<td></td>
<td>General Reserve</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Share Premium</td>
<td>35,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Profit &amp; Loss A/c</td>
<td>9,250</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1,04,250</td>
<td></td>
</tr>
<tr>
<td>Current Liabilities and Provisions</td>
<td></td>
<td></td>
<td>Sundry Creditors</td>
<td>5,750</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2,10,000</td>
<td></td>
</tr>
</tbody>
</table>

STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION
Financial Accounting Fundamentals

For the year ended 31.3.1998, the company made a net profit of Rs. 7,500 after providing Rs. 10,000 depreciation and writing off the miscellaneous expenditure of Rs. 10,000.

The following additional information is available with regard to company’s operation:

(i) The preference dividend for the year ended 31.3.1998 was paid before 31.3.1998.
(ii) The company redeemed the preference shares at a premium of 10%.
(iii) To meet the cash requirements of redemption, the company sold a portion of the investments, so as to leave a minimum balance of Rs. 15,000 after such redemption.
(iv) Except cash and bank balances other current assets and current liabilities as on 31.3.1998 was the same as on 31.3.1997.
(v) The company issued bonus shares in the ratio of one share for every equity share held as on 31.3.1998.
(vi) Investments were sold at 90% of cost on 31.3.1998.

You are required to:

(a) prepare necessary Journal Entries to record redemptions and issue of bonus shares;
(b) prepare the Cash and Bank Account;
(c) prepare the Balance Sheet as at 31.3.1998 incorporating the above transactions.

Solution:

**JOURNAL ENTRIES in the Books of TOM LTD.**

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>10% Redeemable Preference Capital A/c</td>
<td></td>
<td>50,000</td>
</tr>
<tr>
<td>Premium on Redemption of Preference Shares</td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td>To Preference Shareholders</td>
<td></td>
<td>55,000</td>
</tr>
<tr>
<td>(Being amount payable to Pref. shareholder on redemption)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Reserve A/c</td>
<td></td>
<td>50,000</td>
</tr>
<tr>
<td>To Capital Redemption Reserve</td>
<td></td>
<td>50,000</td>
</tr>
<tr>
<td>(Being transfer to the Latter A/c on redemption of shares)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank A/c.</td>
<td></td>
<td>22,500</td>
</tr>
<tr>
<td>Profit &amp; Loss A/c</td>
<td></td>
<td>2,500</td>
</tr>
<tr>
<td>To Investments</td>
<td></td>
<td>25,000</td>
</tr>
<tr>
<td>(Being amount realised on sale of Investments and loss thereon adjusted)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Company Accounts

Preference Shareholders A/c Dr. 55,000
To Bank 55,000
(Being payment made to Preference Shareholders)

Share Premium A/c Dr. 5,000
To Premium on Redemption of Preference Shares 5,000
(Being amount of Premium payable on redemption of Preference shares)

Capital Redemption Reserve A/c Dr. 50,000
To Bonus to Shareholders 50,000
(Amount adjusted for issuing bonus shares in ratio of 1:1)

Bonus to Shareholders A/c. Dr. 50,000
To Equity Share Capital 50,000
(Balance of former account transferred to Latter)

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cash and Bank Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>To Balance B/F.</td>
<td>25,000</td>
<td>By Preference Dividend</td>
</tr>
<tr>
<td>To Cash from operations</td>
<td>7,500</td>
<td>By Preference Shareholders</td>
</tr>
<tr>
<td>Add : Deprn.</td>
<td>10,000</td>
<td>Balance C/f.</td>
</tr>
<tr>
<td>Add : Misc. Expenditure</td>
<td>10,000</td>
<td>27,500</td>
</tr>
<tr>
<td>To Investments</td>
<td>22,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>75,000</td>
</tr>
</tbody>
</table>

Working Notes:

Sale of Investments:

Cost of Investments 25,000
Less : Cash received 22,500
Loss on sale of Investment 2,500
Total Investment 50,000
Less : Cost of Investment sold 25,000
Cost of Investment in hand 25,000
Market value 90% of 25000 22,500
Balance Sheet of Tom Ltd.  
_as at 31st March, 1998_  
(After Redemption)

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Share Capital</strong></td>
<td></td>
<td><strong>Fixed Assets</strong></td>
<td></td>
</tr>
<tr>
<td>Authorised Capital :</td>
<td>5,00,000</td>
<td>Gross Block</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Issued, Subscribed &amp; Paid up :</td>
<td></td>
<td>Less : Depreciation</td>
<td></td>
</tr>
<tr>
<td>10,000 Equity Shares of Rs. 10/-</td>
<td></td>
<td>As per last A/c</td>
<td>50,000</td>
</tr>
<tr>
<td>each fully paid (5000, Shares</td>
<td></td>
<td>For the year</td>
<td>10,000</td>
</tr>
<tr>
<td>have been allotted as Bonus</td>
<td></td>
<td>Investments : (Market value Rs. 22,500)</td>
<td>25,000</td>
</tr>
<tr>
<td>Shares for Capitalising</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital Redemption Reserve)</td>
<td>1,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Reserve &amp; Surplus</strong></td>
<td></td>
<td><strong>Current Assets, Loans &amp; Advances</strong></td>
<td></td>
</tr>
<tr>
<td>General Reserve</td>
<td>10,000</td>
<td>Inventory</td>
<td>12,500</td>
</tr>
<tr>
<td>Share Premium A/c</td>
<td>30,000</td>
<td>Debtors</td>
<td>12,500</td>
</tr>
<tr>
<td>Profit &amp; Loss A/c</td>
<td><strong>9,250</strong></td>
<td>Cash &amp; Bank Balance</td>
<td><strong>49,250</strong></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Current Liabilities &amp; Provisions</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>5,750</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| Working Notes :                     |        |                                |        |
| Profit & Loss A/c –                 |        |                                |        |
| Balance as per last A/c             |         | 9,250                          |        |
| Add : Profit for the year           |         | 7,500                          |        |
|                                     |         | 16,750                         |        |
| Less : Pref. dividend               | 5,000   |                                |        |
| Sale of Investment                  | 2,500   | 7,500                          |        |
|                                     |         | 9,250                          |        |

4.5 **UNDERWRITING**

Underwriting in the context of a company means undertaking a responsibility or giving a guarantee that the shares or debentures offered to the public will be subscribed for. There are firms which undertake this sort of work and are very useful to companies which want to raise funds by the issue price of the whole of the shares or debentures underwritten. A company cannot pay commission on issue of shares unless it is provided for in its Articles. Commission cannot be paid to any person on shares or debentures which are not offered to the public for subscription [sec. 76(4A)].

The law limits the commission on issue of share to 5% for shared and 2 1/2% for debentures. This has to be disclosed in the prospectus.
Sub-underwriters:

These are underwriters who work under other underwriters. For subscriptions procured by them, the underwriter gets a small commission called **overall commission**.

Brokerage:

It is merely the act of procuring subscriptions for shares or debentures without undertaking any responsibility.

Marked Applications:

Underwriters issue application forms stamped with their name for shares and debentures to the public.

Underwriting commission:

The entry for underwriting commission is:

```
Underwriting commission on Issue of Shares A/c  Dr.
To Underwriter A/c
```

The underwriter can also take part responsibility. In such a case his liability will have to be calculated accordingly.

Illustration 7:

Dale Ltd. has Authorised Capital of Rs. 8,00,000. The company issues 20,000 equity shares of Rs. 10 each at a premium of Rs. 5 per share payable as:

- On application — Rs. 6 (including premium Rs. 3)
- On allotment — Rs. 5 (including balance of premium)

Balance in two calls.

Applications were received for 35,000 shares. The applicants were divided in the following groups:

- **Group A** — Applying for 5,000 shares allotted fully.
- **Group B** — Applying for 20,000 shares are made prorata allotment for 15,000 shares.
- **Group C** — Applying for total 10,000 shares are refunded.

Directors while making allotment adjust the excess amount received on application against allotment money due. When second and final calls were made, shareholders holding 500 shares failed to pay the final call money. The directors forfeited these shares. All the forfeited shares were reissued at Rs. 9 per share.
Financial Accounting Fundamentals

It is agreed that brokerage @ 3% and underwriting commission @ 3% will be paid for this issue. Claims of brokers and underwriters are satisfied by issuing to them additional equity shares of Rs. 10 each at a premium of Rs. 5 per share (without any cash payment).

Show Journal Entries and the Balance Sheet of the company in the books of the company.

Solution:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank Account</td>
<td>2,10,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Application Account</td>
<td></td>
<td>2,10,000</td>
</tr>
<tr>
<td>(application money recd. on 35000 shares @ Rs.6 share)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity Share Application Account</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>To Bank Account</td>
<td></td>
<td>60,000</td>
</tr>
<tr>
<td>(being application money on 10,000 shares refunded)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity share Application Account</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td></td>
<td>60,000</td>
</tr>
<tr>
<td>To Security Share Premium A/c</td>
<td></td>
<td>60,000</td>
</tr>
<tr>
<td>(being application money on 20000 shares transferred to share premium and share capital)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity Share Application A/c</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Allotment A/c</td>
<td></td>
<td>30,000</td>
</tr>
<tr>
<td>(Excess application money received on application transferred to share allotment account as per board’s resolution No.------- Dated-------)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity Share Allotment A/c</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td></td>
<td>60,000</td>
</tr>
<tr>
<td>To Security Premium A/c</td>
<td></td>
<td>40,000</td>
</tr>
<tr>
<td>(Amount due on allotment A/c @ Rs. 5 per share including a premium of Rs. 2 as per board’s resolution No.------- Dated-------)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank Account</td>
<td>70,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Allotment A/c</td>
<td></td>
<td>70,000</td>
</tr>
<tr>
<td>(being balance of allotment money recd. in full)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
**Company Accounts**

<table>
<thead>
<tr>
<th>Account</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity Share First Call A/c</td>
<td>40,000</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td>40,000</td>
</tr>
<tr>
<td>(being call money due on 20000 shares @ Rs.2/share)</td>
<td></td>
</tr>
<tr>
<td>Bank Account</td>
<td>40,000</td>
</tr>
<tr>
<td>To Equity Share First Call A/c</td>
<td>40,000</td>
</tr>
<tr>
<td>(being first call money recd.)</td>
<td></td>
</tr>
<tr>
<td>Equity Share Final Call A/c</td>
<td>40,000</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td>40,000</td>
</tr>
<tr>
<td>(being call money due on 20000 shares @ Rs.2/share)</td>
<td></td>
</tr>
<tr>
<td>Bank Account</td>
<td>39,000</td>
</tr>
<tr>
<td>To Equity Share Final Call A/c</td>
<td>39,000</td>
</tr>
<tr>
<td>(being call money on 19500 share received)</td>
<td></td>
</tr>
<tr>
<td>Equity Share Capital Account</td>
<td>5,000</td>
</tr>
<tr>
<td>To Equity Share Final Call A/c</td>
<td>1,000</td>
</tr>
<tr>
<td>To share forfeiture account</td>
<td>4,000</td>
</tr>
<tr>
<td>(being 500 shares forfeited)</td>
<td></td>
</tr>
<tr>
<td>Bank Account</td>
<td>4,500</td>
</tr>
<tr>
<td>Share Forfeiture Account</td>
<td>500</td>
</tr>
<tr>
<td>To Equity Share Capital Account</td>
<td>5,000</td>
</tr>
<tr>
<td>(being 500 shares reissued @Rs. 9/share)</td>
<td></td>
</tr>
<tr>
<td>Share Forfeiture A/c</td>
<td>3,500</td>
</tr>
<tr>
<td>To Capital Reserve A/c</td>
<td>3,500</td>
</tr>
<tr>
<td>(being profit on forfeiture transferred to capital reserve)</td>
<td></td>
</tr>
<tr>
<td>Brokerage Account</td>
<td>6,000</td>
</tr>
<tr>
<td>Commission Account</td>
<td>6,000</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td>8,000</td>
</tr>
<tr>
<td>To Security Premium Account</td>
<td>4,000</td>
</tr>
<tr>
<td>(Commission and Brokerage paid)</td>
<td></td>
</tr>
</tbody>
</table>
Balance Sheet of Dale Ltd.

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td></td>
<td>Fixed Assets</td>
<td></td>
</tr>
<tr>
<td>Authorised (80000 share of Rs. 10 each)</td>
<td>8,00,000</td>
<td>Investments</td>
<td></td>
</tr>
<tr>
<td>Issued, subscribed and paid</td>
<td></td>
<td>Current Assets, Loans &amp; Advances</td>
<td></td>
</tr>
<tr>
<td>20800 equity shares of Rs. 10 each</td>
<td></td>
<td>Bank balance</td>
<td>3,03,500</td>
</tr>
<tr>
<td>(800 shares issued for consideration other than cash)</td>
<td>2,08,000</td>
<td>Miscellaneous Expenditure</td>
<td>6,000</td>
</tr>
<tr>
<td>Reserves &amp; Surplus</td>
<td></td>
<td>Brokerage on issue of shares</td>
<td></td>
</tr>
<tr>
<td>Security premium</td>
<td>1,04,000</td>
<td>Commission on issue of shares</td>
<td>6,000</td>
</tr>
<tr>
<td>Capital reserves</td>
<td>3,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,15,500</td>
<td></td>
<td>3,15,500</td>
</tr>
</tbody>
</table>

4.6 DEBENTURE — ISSUE AND REDEMPTION

A debenture may be defined as an acknowledgment (mostly under seal of the company) of a debt or loan raised by the company. Just as the share capital of a company is divided in a large number of parts, each part being called a share, the loan may be divided into a number of parts called Debentures. They enable a company to raise a loan easily by enabling investors to buy as many debentures as they want.

Debenture is a creditorship security. Company has to pay interest to debenture holders at the agreed rate. It is usual to prefix “Debentures” with annual rate of interest.

Distinction between Debentures and Shares.

<table>
<thead>
<tr>
<th>Debentures</th>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>i) Security</td>
<td>It is a creditorship Security</td>
</tr>
<tr>
<td>ii) Return</td>
<td>A debenture holder is certain of return on his investment and of interest payments.</td>
</tr>
<tr>
<td>iii) Order of repayment on winding up.</td>
<td>They are paid first</td>
</tr>
<tr>
<td>iv) Issue at a discount</td>
<td>No legal conditions</td>
</tr>
<tr>
<td>v) Mortgage</td>
<td>There can be mortgage Debentures</td>
</tr>
<tr>
<td>vi) Convertibility</td>
<td>Can be converted into shares at the option of the debenture holder.</td>
</tr>
</tbody>
</table>
Company Accounts

CLASSES OF DEBENTURES

<table>
<thead>
<tr>
<th>Convertible Debentures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Redeemable</td>
</tr>
<tr>
<td>Irredeemable</td>
</tr>
</tbody>
</table>

**Issue of Debentures:**

The company issues the prospectus inviting applications along with a sum of money called Application money. After scrutiny, the Board of Directors make allotment.

**Entries:**

1) When applications are received:
   - Bank A/c Dr.
     - To Debenture Application A/c

2) Debenture Application A/c Dr.
   - To Debenture A/c

3) Rejection to applications:
   - Debenture Application A/c Dr.
     - To Debenture Allotment A/c

4) Surplus allotment money:
   - Debenture Application A/c Dr.
     - To Debenture Allotment A/c

5) Amount due on allotment of debentures:
   - Debenture Allotment A/c Dr.
     - To Debentures A/c

Like shares debentures may be issued at par, at a premium or at a discount. But the law does not lay down any maximum limit for discount on issue of debentures. The sanction of the CLB is also not needed. If a company issues debentures on the condition that they would be redeemed at a premium, this additional liability should be recorded in a separate account called “Premium on Redemption of Debentures A/c” and should be shown along with the liability “Debentures” on the liabilities side of the Balance Sheet.
Entries:

i) When debentures are issued at par and are also redeemed at par:

\[
\text{Bank A/c Dr.} \quad \text{To Debenture A/c}
\]

ii) When debentures are issued at a discount, but redeemable at par:

\[
\text{Bank A/c Dr.} \\
\text{Discount of Issue of Debentures A/c Dr.} \\
\text{To Debenture A/c}
\]

iii) When debentures are issued at a premium and redeemable at par:

\[
\text{Bank A/c Dr.} \\
\text{To Debenture A/c} \\
\text{To Premium on Issue of Debentures A/c}
\]

iv) When debentures are issued at par and redeemable at a premium:

\[
\text{Bank A/c Dr.} \\
\text{Loss of Issue of Debentures A/c Dr.} \\
\text{To Debenture A/c} \\
\text{To Premium on Redemption of debentures A/c}
\]

v) When debentures are issued at a discount and redeemable at a premium:

\[
\text{Bank A/c Dr.} \\
\text{Discount on Issue of Debentures A/c Dr.} \\
\text{Loss on issue of Debentures A/c Dr.} \\
\text{To Debentures A/c} \\
\text{To Premium on Issue of Debentures A/c}
\]

vi) Expenses, Discount, and loss on Issue of debentures are transferred to an account called Cost of Issue of debentures A/c and shown as "Miscellaneous Expenditure" in the Balance Sheet.

vii) Premium on Issue of debentures is transferred to Capital Reserve A/c.

Redemption of Debentures:

Debentures are invariably redeemable. Debentures may be redeemed

(i) In one lot,

(ii) In instalments or drawing by lots,

(iii) By purchase of debentures in the open market.

Cancellation of debentures may take place in one of two ways :-

(i) Immediate cancellation i.e. immediately after purchase in the open market, and

(ii) Cancellation after holding them for some time as "own debentures". After cancellation the debentures cannot be resold as they stand redeemed.
### Company Accounts

**Entries:**

1) **When the debentures are redeemed at par:**
   - **i)** Debentures A/c Dr. To Sundry Debentureholders A/c Dr.
   - **ii)** Sundry debentureholders A/c To Bank A/c

2) **When the debentures are redeemed at a premium:**
   - **i)** Debentures A/c Dr. Premium on Redemption A/c Dr. To Sundry Debentureholders A/c Dr.
   - **ii)** Sundry Debentureholders A/c To Bank A/c

When the debentures are redeemed by cancelling them immediately after their purchase in the open market, redemption will be recorded as follows –

1) **When purchase prices is equal to the face value of debentures:**
   - Debentures A/c Dr. To Bank A/c

2) **When purchase price is higher than the face value of debentures:**
   - **i)** Debentures A/c Dr. Loss on Redemption of Debentures A/c Dr. To Bank A/c
   - **ii)** Share Premium A/c Dr. 
     - or Profit & Loss A/c Dr. To Loss on Redemption of Debentures A/c

3) **When purchase price is lower than the face value of the debentures:**
   - **i)** Debenture A/c Dr. To Bank A/c To Profit on Redemption of Debentures A/c Dr.
   - **ii)** Profit on Redemption of Debentures A/c Dr. To Capital Reserve A/c
A company may buy its own debentures, hold them as investments for some time and then redeem them by cancellation. Entries will be as follows:

<table>
<thead>
<tr>
<th>When own debentures are purchased as investments:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Own Debentures A/c Dr.</td>
</tr>
<tr>
<td>To Bank A/c</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>When &quot;own debentures&quot; held as investments are cancelled:</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) When purchase price is equal to the face value of debentures:</td>
</tr>
<tr>
<td>Debit: Debentures A/c Dr.</td>
</tr>
<tr>
<td>Credit: To Own Debentures A/c</td>
</tr>
<tr>
<td>2) When purchase price is higher than the face value of debentures:</td>
</tr>
<tr>
<td>i) Debit: Debentures A/c Dr.</td>
</tr>
<tr>
<td>Credit: Loss of Redemption of own debentures A/c Dr.</td>
</tr>
<tr>
<td>Credit: To Own Debentures A/c</td>
</tr>
<tr>
<td>ii) Debit: Share premium A/c Dr.</td>
</tr>
<tr>
<td>or</td>
</tr>
<tr>
<td>Credit: Profit &amp; Loss A/c Dr.</td>
</tr>
<tr>
<td>Credit: To Loss on Cancellation of Own Debentures A/c</td>
</tr>
<tr>
<td>3) When purchase price is lower than the face value of debentures:</td>
</tr>
<tr>
<td>i) Debit: Debentures A/c Dr.</td>
</tr>
<tr>
<td>Credit: To Own Debentures A/c</td>
</tr>
<tr>
<td>Credit: Profit on cancellation of own debentures A/c</td>
</tr>
<tr>
<td>ii) Debit: Profit on Cancellation of Own Debenture A/c</td>
</tr>
<tr>
<td>Credit: To Capital Reserve A/c</td>
</tr>
</tbody>
</table>

**Sinking Fund method:**

Under this method the amount is invested in first class securities which when allowed to accumulate with compound interest produce the amount required to redeem the debentures on the due date. This method of providing for funds is known as Sinking fund method. Accounting entries for making the provision for the redemption of debentures are as follows:

<table>
<thead>
<tr>
<th>First year on 31st December (date of closing) :</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Profit &amp; Loss Appropriation A/c Dr.</td>
</tr>
<tr>
<td>To Sinking Fund A/c</td>
</tr>
<tr>
<td>(for setting aside the amount which is calculated after consulting the sinking fund tables).</td>
</tr>
<tr>
<td>2. Sinking Fund Investment A/c Dr.</td>
</tr>
<tr>
<td>To Bank A/c</td>
</tr>
<tr>
<td>(for investing the amount set aside)</td>
</tr>
</tbody>
</table>
Company Accounts

For second and subsequent years:
1. Bank A/c Dr. To Interest on Sinking Fund Investment A/c (for receiving interest on the investment made in the past years)
2. Interest on Sinking Fund Investment A/c Dr. To Sinking Fund A/c (for transferring interest to Sinking Fund)

For Last Year
1. Bank A/c Dr. To Interest on Sinking Fund Investment A/c (for receiving interest on the investment made in the past years)
2. Profit and Loss Appropriation A/c Dr. To Sinking Fund A/c (for setting aside the amount)
3. Interest on Sinking Fund Investment A/c Dr. To Sinking Fund A/c (for transferring Interest Account to Sinking Fund)

It may be noted that in the final year the amount appropriated from the profits of the company and the amount received as interest on sinking fund investment are not invested as the amount would be needed on the following day for the redemption of debenture.

Concept of Cum and Ex-interest

The word "Cum" means "inclusive" and "Ex" means exclusive. When debentures are quoted on "cum-interest" basis it means that the quotation in addition to covering the cost also includes accrued interest upto the date of purchase/sale.

In case of Ex-interest quotation only cost element is covered.

Redemption of Debentures by purchase in open market purchase for immediate cancellation. The company at its will can purchase own debentures for market and cancel them. The Accounting Entries will be:

i) For purchase of debentures (Quoted price × No. of debenture purchased) – Accrued interest.
   Debenture Redemption A/c Dr. (Cost)
   Debenture Interest A/c Dr. (Accrued Interest)
   To Bank A/c Total payment.

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Financial Accounting Fundamentals

b) When debentures are purchased (Ex-interest)
   Debenture redemption A/c Dr.  
   (Quoted price × No. of Debentures purchased)  
   Debenture Interest A/c Dr.  
   (Accrued Interest)  
   To Bank  *(Total payment)*

c) Sale of Sinking Fund Investment
   Bank A/c Dr.  
   To S.F. Investment A/c
   Note: Profit/Loss on sale will be adjusted in Sinking Fund A/c.

d) For cancellation:
   Debentures A/c Dr.  
   (Face value of Debenture Redeemed)  
   To Debenture Redemption A/c

Any balance in Debenture Redemption A/c will be adjusted against Sinking Fund A/c.

Purchase of Debentures in open market as Investment
Sometimes a company purchases its debentures and hold them as investment. The accounting entries are stated as follows:

1. When debentures are purchased
   1. At cum Interest
      Own Debenture Investment A/c Dr.  
      (Quoted price – Accrued debentures purchased)  
      Debenture Interest A/c Dr.  
      (Accrued Interest)  
      To Bank A/c
   b. At Exinterest:
      Own Debenture Investment A/c Dr.  (Quoted price Accrued debentures purchased)  
      Debenture Interest A/c Dr.  (Accrued interest)  
      To Bank
   c. For sale of Sinking Fund Investment
      Bank A/c Dr.  
      To Sinking Fund Investment A/c
      *Any Profit & Loss will be adjusted in Sinking Fund A/c*

4. For Cancellation:
   Debentures A/c Dr.  *(Face value)*  
   To Own Debenture investment A/c [Cost]  
   To Profit/Loss on Cancellation will be charged to Sinking Fund A/c
Illustration 8:

You are required to set out the Journal Entries relating to the issue of the following Debentures in the books of X Ltd:

(a) 8%, 120 Rs. 1,000 Debentures are issued at 5% discount and are repayable at par.
(b) Another 7%, 150 Rs. 1,000 Debentures are issued at 5% discount and repayable at 10% premium.
(c) Further 80, 9% Rs. 1,000 Debentures are issued at 5% premium.
(d) In addition another 400, 8% Rs. 100 Debentures are issued at collateral security against a loan of Rs. 40,000.

Solution:

<table>
<thead>
<tr>
<th>Journal</th>
<th>Dr.(Rs.)</th>
<th>Cr.(Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Bank Account</td>
<td>Dr. 1,14,000</td>
<td></td>
</tr>
<tr>
<td>Debenture Discount A/c.</td>
<td>Dr. 6,000</td>
<td></td>
</tr>
<tr>
<td>To 8% Debentures A/c.</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td>(Issue of 8%, 120 Rs. 1,000 Debentures of 5% discount and repayable at par as per Board’s resolution dated...)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(ii) Bank Account</td>
<td>Dr. 1,42,500</td>
<td></td>
</tr>
<tr>
<td>Loss on issue</td>
<td>Dr. 22,500</td>
<td></td>
</tr>
<tr>
<td>To 7% Debentures</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>To Premium on Redemption</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>(Issue of 7%, 150 Rs. 1,000 Debentures at a Discount of 5% and repayable at 10% premium as per Boards’ Resolution dated ..... )</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(iii) Bank Account</td>
<td>Dr. 84,000</td>
<td></td>
</tr>
<tr>
<td>To 9% Debenture</td>
<td>80,000</td>
<td></td>
</tr>
<tr>
<td>To Debentures Premium</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>(Issue of 9%, 80 Rs. 1,000 Debentures at 5% premium as per Boards’ Resolution dated .... )</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(iv) Debenture Suspense (or) (8% Collateral Debentures)</td>
<td>Dr. 40,000</td>
<td></td>
</tr>
<tr>
<td>To 8% Debentures</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>(Issue of 400, 8% Debentures of Rs. 100 each as collateral security to against Rs. 40,000/- loan as per agreement and Board’s Resolution dated.... )</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Notes:

1. Discount Account may also be termed as Loss on Issue Account. But loss on issue is better used in second case as it indicates loss due to discount and also loss arising as a result of the term to pay premium on redemption.

2. Collateral Debenture will be shown in Asset side or by way of deductions from Debentures. In the alternative, no entry may be passed and a note to that effect in the Balance Sheet will serve the purpose.

Illustration 9:

The Summarised Balance Sheet of Nipa Ltd. on March 31, 1997 was as follows:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Amount</th>
<th>Assets</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share capital:</td>
<td></td>
<td>Fixed assets at cost less :</td>
<td>4,12,000</td>
</tr>
<tr>
<td>6% Redeemable preference shares of</td>
<td></td>
<td>Goodwill</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Rs. 10 each</td>
<td>2,00,000</td>
<td>Stock</td>
<td>4,50,000</td>
</tr>
<tr>
<td>Equity shares of Rs. 10 each</td>
<td>4,00,000</td>
<td>Sundry Debtors</td>
<td>2,15,000</td>
</tr>
<tr>
<td>Profit &amp; loss A/c</td>
<td>2,50,000</td>
<td>Discount on Debentures</td>
<td>12,000</td>
</tr>
<tr>
<td>5% Debentures</td>
<td>3,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank Loan</td>
<td>50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>89,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>12,89,000</td>
<td></td>
<td>12,89,000</td>
</tr>
</tbody>
</table>

Wanting to redeem the Preference Shares and the Debentures the company offered to the Redeemable Preference Shareholders and the Debenture holders the option to convert their holding into Equity Shares to be issued at a premium of Rs. 2.50 per share. Half of the Preference Shareholders and one-third of the Debenture holders agreed to do this. The company issued 30000 Equity Share at Rs. 12.50 to the public for cash and with the funds available paid off the bank loan and redeemed the remaining redeemable Preference Shares and Debentures.

Journalise the transaction and show how the balance sheet will appear after the transactions have been completed.

Solution:

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>31st March, 1997</td>
<td>i) 6% Redeemable Preference Share Capital A/c</td>
<td></td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Capital (8000×Rs.10)</td>
<td></td>
<td>80,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Share Premium A/c (8000×Rs. 2.50)</td>
<td></td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Being 50% of Redeemable Preference Shares converted into Equity Shares @ 10 each with Premium, Rs. 2.50 each.)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Company Accounts

ii) 5% Debentures A/c Dr. 1,00,000
   To Equity Share Capital A/c (8000×Rs.10) 80,000
   To Share Premium A/c (8000×Rs.2.50) 20,000
   (Being 1/3rd Debenture converted into Equity Share at Rs. 10 each with Premium of Rs. 2.50 each.)

iii) Bank A/c (30,000 × Rs. 12.50) Dr. 3,75,000
     To Equity Share Capital A/c (30,000×Rs. 2.50) 3,00,000
     To Share Premium A/c (30,000×Rs. 2.50) 75,000
     (Being 30,000 Equity Shares @ Rs. 10 with Premium Rs. 2.50 each issued for Cash as per Board Resolution No. ...... Dt. ...... .)

iv) 6% Redeemable Preference Share Capital A/c Dr. 1,00,000
    5% Debentures A/c Dr. 2,00,000
    To Preference Share Holders A/c 1,00,000
    To Debenture Holders A/c 2,00,000
    (Being the balance amount of Redeemable Preference Share and Debentures redeemable.)

v) Preference Share Holders A/c Dr. 1,00,000
   Debenture Holders A/c Dr. 2,00,000
   Bank Loan A/c Dr. 50,000
   To Bank A/c 3,50,000
   (Being the amount paid to Share Holders and Debenture Holders in full and Bank Loan repaid.)

vi) Share Premium A/c Dr. 12,000
    To Discount on debenture A/c 12,000
    (Being the amount of discount on debenture is written off after utilising the amount of Share Premium A/c.)

NIPA Limited.

Balance Sheet as at 31.03.1997

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital:</td>
<td></td>
<td>Goodwill</td>
<td>2,00,00</td>
</tr>
<tr>
<td>Equity Shares @ Rs. each</td>
<td>8,60,00</td>
<td>Fixed Assets at cost</td>
<td></td>
</tr>
<tr>
<td>Reserve &amp; Surplus :</td>
<td></td>
<td>Less : Depreciation</td>
<td>4,12,00</td>
</tr>
<tr>
<td>Profit &amp; Loss A/c</td>
<td>2,50,00</td>
<td>Current Assets :</td>
<td></td>
</tr>
<tr>
<td>Share Premium A/c</td>
<td>1,03,00</td>
<td>Stock</td>
<td>4,50,00</td>
</tr>
<tr>
<td>Current Liabilities &amp; Provisions :</td>
<td></td>
<td>Sundry Debtors</td>
<td>2,15,00</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>89,000</td>
<td>Cash at Bank</td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td>13,02,00</td>
<td></td>
<td>13,02,00</td>
</tr>
</tbody>
</table>
Illustration 10:

The following balances appeared in the books of Royco Ltd. on 1.4.2001:

(a) Debenture Redemption Fund Rs. 60,000 represented by investments of an equal amount (nominal value Rs. 75,000).

(b) The 12% debentures stood at Rs. 90,000.

The company sold required amount of investments at 90% for redemption of Rs. 30,000 Debentures at a premium of 20% on the above date.

Show the:

(i) 12% Debenture Account;

(ii) Debenture Redemption Fund Account;

(iii) Debenture Redemption Fund Investments Accounts;

(iv) Debenture-holders account

Solution:

In the books of the Royco Ltd.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>12% Debentures A/c Rs.</th>
<th>Date</th>
<th>Particulars Rs.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1/4/01</td>
<td>To Deb. holders A/c</td>
<td>30,000</td>
<td>1/4/01</td>
<td>By Balance b/d</td>
<td>90,000</td>
</tr>
<tr>
<td>31/3/02</td>
<td>To Balance c/d</td>
<td>60,000</td>
<td>90,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Debenture Redemption Fund A/c Rs.</th>
<th>Date</th>
<th>Particulars Rs.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>31/3/02</td>
<td>To Premium on redemption</td>
<td>1/4/01</td>
<td>By Balance b/d</td>
<td>60,000</td>
</tr>
<tr>
<td>31/3/02</td>
<td>of debenture A/c</td>
<td>1/4/01</td>
<td>By Debenture Redemption</td>
<td></td>
</tr>
<tr>
<td>31/3/02</td>
<td>To General Reserve</td>
<td>30,000</td>
<td>Fund investment A/c</td>
<td>4,000</td>
</tr>
<tr>
<td>31/3/02</td>
<td>To Balance c/d</td>
<td>28,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31/3/02</td>
<td></td>
<td>64,000</td>
<td></td>
<td>64,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Debenture Redemption Fund Investment A/c Rs.</th>
<th>Date</th>
<th>Particulars Rs.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1/4/001</td>
<td>To Balance b/d</td>
<td>60,000</td>
<td>1/4/01</td>
<td>By Bank A/c</td>
</tr>
<tr>
<td>31/3/02</td>
<td>To Debenture Redemption Fund A/c</td>
<td>4,000</td>
<td>31/3/02</td>
<td>By Balance c/d</td>
</tr>
<tr>
<td>1/4/02</td>
<td>To Balance b/d</td>
<td>28,000</td>
<td>64,000</td>
<td></td>
</tr>
</tbody>
</table>
Company Accounts

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1/4/01</td>
<td>To Bank</td>
<td>36,000</td>
<td>31/3/02</td>
<td>By 12% Debentures A/c</td>
<td>30,000</td>
</tr>
<tr>
<td>,</td>
<td>,</td>
<td>36,000</td>
<td>,</td>
<td>By Premium on Redm. of Debenture A/c</td>
<td>6,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>36,000</td>
<td></td>
<td></td>
<td>36,000</td>
</tr>
</tbody>
</table>

Notes:

1. Debentures of Rs. 30000 is to be redeemed at a premium of 20%. Therefore, the amount payable to the debentureholders is Rs. 30000 x 120% = Rs. 36000. To get Rs. 36000 investments worth Rs. 40000 is to be sold at 90% = Rs. 40000

2. Sale proceeds from investments 36,000

\[ \text{Less: Cost of investment sold} = \left( \frac{60,000}{75,000} \right) \times 40,000 = 32,000 \]

\[ \text{Profit on sale of investments} = 4,000 \]

Illustration 11:

You are requested to pass the Journal Entries to the issue of the following debentures in the books of Damodar Valley Corporation.

(i) 2000, 5% Debentures of Rs. 100 each at a premium of Rs. 10 per debenture, redeemable at par.

(ii) 1000, 8% Debentures Rs. 150 each at a discount of Rs. 20 per debenture.

(iii) 2000, 12% Debentures of Rs. 200 each at par, redeemable at a premium of 10%.

(iv) 1500, 11% Debentures of Rs. 250 each at a discount of 10% redeemable at a premium of 10%.

Solution:

In the books of DVC

<table>
<thead>
<tr>
<th>Journal Entries</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Bank A/c</td>
<td>Dr. 2,20,000</td>
<td></td>
</tr>
<tr>
<td>To 5% Debentures A/c</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>To Premium on issue of Debentures A/c</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>( \text{(Being issue of 2000 debentures of Rs. 100 each at premium, redeemable at per)} )</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Bank A/c</td>
<td>Dr. 1,30,000</td>
<td></td>
</tr>
<tr>
<td>Discount on issue of Debentures A/c</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>To 8% Debenture A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>( \text{(Being issue of 1000 debentures of Rs. 150 each at a discount but redeemable at per)} )</td>
<td>1,50,000</td>
<td></td>
</tr>
</tbody>
</table>
Illustration 12:

ABC Limited issued 4000 10% debentures of Rs.100 each at par in January 1988 redeemable at par on December 1997. Interest was payable on debentures on 30th June and 31st December in each year. For redemption, the company has set up Sinking Fund by appropriating a sum of Rs.32,000 and the amount was invested. As per the terms of the issue the company is empowered to purchase its own debentures in the market and to keep them available for reissue. On December 1996 the following balances were extracted from the company’s book:

Sinking Fund Investments in Govt. Securities at cost

(a) Sinking Fund Investments in Govt. Securities at cost  Rs. 3,27,520
(b) 10% debenture Stock  4,00,000
(c) Sinking Fund Account  3,72,000

The transactions during the year ended 31st December ’97 included the following —

January 1 : Government securities at par value of Rs.32,000 were purchased for Rs. 31,680.
February 1 : 120 own debentures were purchased cum-interest at a cost of Rs. 11,760.
September 1 : Government securities worth Rs. 12,000 were disposed of at Rs.11,800 ex-interest.
September 1 : 120 own debentures were purchased ex-interest for Rs.11,800 with the proceeds of investment sold.
December 22 : The balance of the Sinking fund investment sold cum-interest at 99%.

The debenture stock was redeemed and cancelled in accordance with the terms of issue.
Company Accounts

Appropriate for the year from the Profit & Loss Account to Sinking Fund to the extent of amount actually required for redemption.

You are required to prepare the following accounts in the books of the company for the year ended 31st December, 1997 (workings should form part of your Answer):

(a) Sinking Fund Account.
(b) Sinking Fund Investment Account.

Solution:

**ABC Limited**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Nominal</th>
<th>Interest</th>
<th>Cost</th>
<th>Date</th>
<th>Particulars</th>
<th>Nominal</th>
<th>Interest</th>
<th>Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1997</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jan.1</td>
<td>To Bal b/d</td>
<td>327520</td>
<td>—</td>
<td>327520</td>
<td>Jun30</td>
<td>By Bank</td>
<td>—</td>
<td>17,976</td>
<td>—</td>
</tr>
<tr>
<td>Jan.1</td>
<td>To Bank</td>
<td>32000</td>
<td>—</td>
<td>31680</td>
<td>Sept.1</td>
<td>By Bank</td>
<td>12000</td>
<td>200</td>
<td>11800</td>
</tr>
<tr>
<td>Dec.31</td>
<td>Sinking Fund A/c (Transfer)</td>
<td>—</td>
<td>34838</td>
<td></td>
<td>Sept.1</td>
<td>By Sinking Fund A/c (Loss)</td>
<td>200</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Dec.22</td>
<td>By Bank</td>
<td>347520</td>
<td>16662</td>
<td>327383</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Dec.31</td>
<td>By Sinking F. A/c (loss)</td>
<td>19817</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>359520</td>
<td>34838</td>
<td>359200</td>
<td></td>
<td></td>
<td>359520</td>
<td>34838</td>
<td>359200</td>
</tr>
</tbody>
</table>

**10% Sinking Fund Investment Account (Government Securities)**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Nominal</th>
<th>Interest</th>
<th>Cost</th>
<th>Date</th>
<th>Particulars</th>
<th>Nominal</th>
<th>Interest</th>
<th>Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1997</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Feb.1</td>
<td>To Bank</td>
<td>12000</td>
<td>100</td>
<td>11660</td>
<td>Jun30</td>
<td>By Debenture Interest A/c</td>
<td>—</td>
<td>600</td>
<td>—</td>
</tr>
<tr>
<td>Sept.1</td>
<td>To Bank</td>
<td>12000</td>
<td>200</td>
<td>11800</td>
<td>Dec.31</td>
<td>By Deb. Int A/c</td>
<td>—</td>
<td>1200</td>
<td>—</td>
</tr>
<tr>
<td>Dec.31</td>
<td>Sinking Fund A/c (Transfer)</td>
<td>—</td>
<td>1500</td>
<td>540</td>
<td>Dec.31</td>
<td>By 10% Debenture Stock A/c</td>
<td>24000</td>
<td>24000</td>
<td>24000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>24000</td>
<td>1800</td>
<td>24000</td>
<td></td>
<td></td>
<td>24000</td>
<td>1800</td>
<td>24000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Sinking Fund Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td>To Sinking Fund Inv. A/c (Gross on sale of Govt. Sec.)</td>
<td>200</td>
<td>Jan. 1</td>
<td>By Balance b/d</td>
<td>3,72,000</td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To Sinking Fund Inv. A/c (Loss on sale of Govt. Sec.)</td>
<td>19,817</td>
<td>Dec. 31</td>
<td>By Sinking Fund Inv. A/c (Int. on Govt. Securities)</td>
<td>34,838</td>
</tr>
<tr>
<td></td>
<td>Dec. 31</td>
<td></td>
<td>By Sinking Fund Inv. A/c — (Own Debentures)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>— Interest</td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To General Reserve</td>
<td>4,00,000</td>
<td>Dec. 31</td>
<td>By Profit &amp; Loss A/c- (Apprn. for redemption)</td>
<td>11,139</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4,20,017</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

10% Debenture Stock Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec. 31</td>
<td>To Sinking Fund Inv. A/c (Own debenture cancellation)</td>
<td>24,000</td>
<td>Jan. 1</td>
<td>By Balance b/d</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Dec. 31</td>
<td>To Bank</td>
<td>3,76,000</td>
<td></td>
<td></td>
<td>4,00,000</td>
</tr>
</tbody>
</table>

Working Notes —

1. Interest : \[3,47,520 \times \frac{10}{100} \times \frac{175}{365} = 16,661.90\] (= 16662 say)
2. It is assumed in respect of Government Securities
   (a) Rate of interest is 10%
   (b) Interest is payable on 30th June and 31st December every year
   (c) Face value of Securities as on 31st December, 1996 is taken at Rs. 3,27,520.

4.7 PROFIT OR LOSS PRIOR TO INCORPORATION

Business is very often taken over by a company from a date earlier than the date of its incorporation or date of commencement of business. The profit of the company up to the date of its incorporation/commencement of business, cannot be treated as Trading Profit of the company. Thus, the profit arising to the company from the date of purchase, up to the date of incorporation/commencement of business is known as pre-incorporation profit. This pre-incorporation profit being considered as capital profit is transferred to Capital Reserve or adjusted with Goodwill. When a business is taken over and working continued, usually same set of books is used and ultimately, the total profit for the year is divided between pre and post incorporation periods. At times, this division is made on some estimation.
Company Accounts

The usual practice is to prepare the profit and loss account only at the end of the year and then to allocate the profits between the two periods in the following manner:

(a) Gross profit and expenses connected with sales to be apportioned according to the ratio of sales for the two periods.

(b) Salaries, rent, interest etc. should be apportioned on the basis of ratio of time before incorporation and after.

(c) Expenses solely incurred for the company on and after its incorporation e.g. preliminary expenses, directors’ fees, etc. should be charged wholly to the post-incorporation period.

Illustration 13:

The Sai Deep Ltd. was incorporated on 1st August 1996, to take over the running business of Krishna Bros. with effect from 1st April 1996. The company received the certificate for commencement of business on 1st October 1996. The following P&L A/c was prepared for the year ended 31.3.1997.

Profit and Loss Account for the year ended 31.03.1997

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amt. (Rs.)</th>
<th>Particulars</th>
<th>Amt. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Office Salaries</td>
<td>21,000</td>
<td>By Gross Profit b/d</td>
<td>80,000</td>
</tr>
<tr>
<td>To Partners Salaries</td>
<td>6,000</td>
<td>By Share Transfer Fee</td>
<td>1,000</td>
</tr>
<tr>
<td>To Advertisement</td>
<td>4,400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Printing &amp; Stationery</td>
<td>1,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Travelling expenses</td>
<td>4,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Office Rent</td>
<td>9,600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Electricity Charges</td>
<td>900</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Auditors Charges</td>
<td>600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Directors Charges</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Bad Debts</td>
<td>1,200</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Commission on Sales</td>
<td>4,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Preliminary Expenses</td>
<td>700</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Debenture Interest</td>
<td>1,600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest on Capital</td>
<td>1,800</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Depreciation</td>
<td>2,100</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>20,600</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Additional information:

(1) Total Sales for the year, which amounted to Rs. 8,00,000 arose evenly up to the date of certificate of commencement, whereafter they recorded an increase of 2/3 during the year. Gross profit was at an uniform rate of 10% of selling price throughout the year and a commission of 0.5% was paid on sales.
Financial Accounting Fundamentals

(2) Office Rent was paid @ Rs. 8,400 p.a. up to 30th September 1996, and thereafter it was paid @ Rs. 10,800 p.a.

(3) Travelling Expenses include Rs. 1,600 towards sales promotion

(4) Bad Debts written off –
   (a) A debt of Rs. 400 taken over from the vendor.
   (b) A debt of Rs. 800 in respect of goods sold in September 1996

Depreciation includes Rs. 600 for assets acquired in the post-incorporation period.

Show the “pre” and “post” incorporation results and also state how the results of pre- and post-incorporation is dealt with.

Solution:

M/S SAIDEEP LIMITED.

<table>
<thead>
<tr>
<th>Dr. Expenses</th>
<th>Profit and Loss account for the year ended 31.3.96</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Basis</td>
<td>Pre</td>
</tr>
<tr>
<td>To Office salary</td>
<td>Time 7,000</td>
<td>14,000</td>
</tr>
<tr>
<td>To Partners’ salary</td>
<td>Actual 6,000</td>
<td>–</td>
</tr>
<tr>
<td>To Advertisement</td>
<td>Sales 1,100</td>
<td>3,300</td>
</tr>
<tr>
<td>To Printing &amp; Stationery</td>
<td>Time 500</td>
<td>1,000</td>
</tr>
<tr>
<td>To Sales promotion</td>
<td>Sales 400</td>
<td>1,200</td>
</tr>
<tr>
<td>To Travelling exp.</td>
<td>Time 800</td>
<td>1,600</td>
</tr>
<tr>
<td>To Office rent</td>
<td>Time 2,800</td>
<td>6,800</td>
</tr>
<tr>
<td>To Electricity chgs.</td>
<td>Time 300</td>
<td>600</td>
</tr>
<tr>
<td>To Director’s fees</td>
<td>Actual –</td>
<td>1,000</td>
</tr>
<tr>
<td>To Auditors’s fees</td>
<td>Time 200</td>
<td>400</td>
</tr>
<tr>
<td>To Bad debts</td>
<td>Time 400</td>
<td>800</td>
</tr>
<tr>
<td>To Commission on sales</td>
<td>Sales 1,000</td>
<td>3,000</td>
</tr>
<tr>
<td>To Preliminary Exp.</td>
<td>Actual –</td>
<td>700</td>
</tr>
<tr>
<td>To Debenture int.</td>
<td>Actual –</td>
<td>1,600</td>
</tr>
<tr>
<td>To Int. on Capital</td>
<td>Actual 1,800</td>
<td>–</td>
</tr>
<tr>
<td>To Depreciation</td>
<td>Time 500</td>
<td>1,600</td>
</tr>
<tr>
<td>To Bal. b/d</td>
<td>–</td>
<td>23,400</td>
</tr>
</tbody>
</table>

22,800  61,000  22,800  61,000
Company Accounts

Working Notes:

1. **Pre-incorporation loss** – It has been transferred to Goodwill A/c.

2. **Sales ratio** —

<table>
<thead>
<tr>
<th>Apr</th>
<th>May</th>
<th>June</th>
<th>July</th>
<th>Aug</th>
<th>Sept</th>
<th>Oct</th>
<th>Nov</th>
<th>Dec</th>
<th>Jan</th>
<th>Feb</th>
<th>Mar</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>12/3</td>
<td>12/3</td>
<td>12/3</td>
<td>12/3</td>
<td>12/3</td>
<td>12/3</td>
<td>12/3</td>
</tr>
</tbody>
</table>

Pre-incorporation sales = 4. Post incorporation sales = 12;
Hence, Sales ratio = 4:12 i.e. 1:3
Let average sales of first six months be Rs. 3 per month —
So, average sales of remaining six months (Rs. 3 + 2/3 of Rs. 3, i.e., Rs. 3+2 = Rs. 5 p.m.
Sales ratio = 12 : 36
4 months = Rs. 3 per month = \( A \times 3 = 12 \)
8 months = Rs. 3 per month = i.e. 2 × 3 = 6 @ Rs. 5 p.m. = i.e. , 6 × 5 = 30 that is
30 + 6 = 36
12 : 36 = 1 : 3

3. **Allocation of office rent** —

   Pre-incorporation | Post-incorporation
   | April to July | 8,400 × 4 ÷ 12 = 2,800 | 10,800 × 6 ÷ 12 = 5,400 Oct. to Mar.
   | Aug. to March | 8,400 × 2 ÷ 12 = 1,400 Aug. to Sept.
   | Aug. to Mar.  | 6,800

4. **Allocation of depreciation** —

On post inc. assets | Pre-inc. | Post-inc.
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Bal. Rs. 1,500 on time ratio 4 : 12</td>
<td>500</td>
<td>1,000</td>
</tr>
</tbody>
</table>

4.8 **SPECIAL POINTS IN RESPECT OF CERTAIN ITEMS**

1. **Income-tax** : For provisions relating to advance tax, provision for income-tax refer any recommended Text Book. The following is an example –

   **Illustration 14** :  
   
   Trial Balance of Soma Ltd. as on 31st March, 1997 [extract]

<table>
<thead>
<tr>
<th>Name of Account</th>
<th>Dr.(Rs.)</th>
<th>Cr.(Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advance income tax for 1995-96</td>
<td>2,20,000</td>
<td></td>
</tr>
<tr>
<td>Advance income tax for 1996-97</td>
<td>2,30,000</td>
<td></td>
</tr>
<tr>
<td>Provision for income tax 1995-96</td>
<td></td>
<td>2,00,000</td>
</tr>
</tbody>
</table>
Adjustments:

(i) The income tax assessment for 1995-96 completed during the year showed gross tax demand of Rs. 2,40,000 but no effect has been given for this in the account.

(ii) Provision for income tax is to be made for Rs. 2,10,000 for 1996-97.

Show Journal Entries and relevant extract in the Final Account.

Solution:

Journal Entries of Soma Limited.

<table>
<thead>
<tr>
<th>Date (1997)</th>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>31.3</td>
<td>Profit &amp; Loss A/c</td>
<td>Dr. 2,10,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Provision for Income-tax A/c</td>
<td></td>
<td>2,10,000</td>
</tr>
<tr>
<td></td>
<td>(Being the amount of provision for Income-tax for the year 1996-97 charged to P/L Account)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.3</td>
<td>Profit &amp; Loss Appropriation A/c</td>
<td>Dr. 40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Provision for Income-tax A/c</td>
<td></td>
<td>40,000</td>
</tr>
<tr>
<td></td>
<td>(Being the amount of less provision for Income-tax for 1995-96 charged to P/L A/c of this year 1996-97)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31.3</td>
<td>Provision for Income-tax A/c</td>
<td>Dr. 2,20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Advance Income-tax A/c</td>
<td></td>
<td>2,20,000</td>
</tr>
<tr>
<td></td>
<td>(Being the amount of advance income-tax for earlier year 1995-96 adjusted with provision for tax.)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Dr. Profit & Loss Account for the year ended 31.3.97 (Extract)

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Provision for Tax (1996-97)</td>
<td>2,10,000</td>
<td>By Gross Profit b/d</td>
<td>?</td>
</tr>
<tr>
<td>To Net Profit c/d</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Provision for Tax</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Less: Provision for 1995-96)</td>
<td>40,000</td>
<td>By Balance b/d</td>
<td>?</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Net Profit during the year</td>
<td>?</td>
</tr>
</tbody>
</table>
Company Accounts

SOMA Limited
Balance Sheet as on 31.03.1997 (Extract)

<table>
<thead>
<tr>
<th>Liabilities &amp; Provisions</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>?</td>
<td>Fixed Assets</td>
<td>?</td>
</tr>
<tr>
<td>Reserves &amp; Surplus</td>
<td>?</td>
<td>Current Assets, Loan and Advances</td>
<td>?</td>
</tr>
<tr>
<td>Current Liabilities &amp; Provisions</td>
<td></td>
<td>Current Assets</td>
<td>?</td>
</tr>
<tr>
<td>Provision for Tax</td>
<td></td>
<td>Loans &amp; Advances</td>
<td></td>
</tr>
<tr>
<td>1995 - 96</td>
<td>20,000</td>
<td>Advance Income Tax for 1996-97</td>
<td>2,30,000</td>
</tr>
<tr>
<td>1996 - 97</td>
<td>2,10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

2. **Sundry Debtors**: Sundry debtors should be segregated agewise, namely, debts outstanding for a period exceeding six months, and other debts.

In regard to Sundry Debtors particulars to be given separately of –

(a) debts considered good and in respect of which the company is fully secured:

(b) debts considered good for which the company holds no security other than the debtor’s personal security; and

(c) debts considered doubtful or bad.

3. **Bank Balances**: Bank balances should be shown as follows –

(a) Bank balance with Scheduled Banks, and

(b) Bank balance with others.

For detail, Students are required to refer **Schedule VI of Part I** of the Companies Act, 1956 relating to the Form of Balance Sheet.
4.9 COMPANY FINAL ACCOUNTS

Illustration 15:

From the following particulars furnished by Printex Ltd., prepare the Balance Sheet as at 31st March, 2002 as required by Part I, Schedule VI of the Companies Act. Give notes at the foot of the Balance Sheet as may be found necessary:

<table>
<thead>
<tr>
<th>Debit (Rs.)</th>
<th>Credit (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity Capital (face value of Rs. 100)</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Land</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Building</td>
<td>3,50,000</td>
</tr>
<tr>
<td>Plant and Machinery</td>
<td>5,25,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>50,000</td>
</tr>
<tr>
<td>Calls in Arrears</td>
<td>1,000</td>
</tr>
<tr>
<td>General Reserve</td>
<td>2,10,000</td>
</tr>
<tr>
<td>Loan from State Financial Corporation</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Stock:</td>
<td></td>
</tr>
<tr>
<td>Finished</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Raw Materials</td>
<td>50,000</td>
</tr>
<tr>
<td>Sundry Creditors (for goods and expenses)</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Loans (unsecured)</td>
<td>1,21,000</td>
</tr>
<tr>
<td>Preliminary expenses</td>
<td>13,300</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>2,47,000</td>
</tr>
<tr>
<td>Cash Balance</td>
<td>30,000</td>
</tr>
<tr>
<td>Profit &amp; Loss Account</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Proposed Dividend</td>
<td>60,000</td>
</tr>
<tr>
<td>Advances</td>
<td>42,700</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Provision for Taxation</td>
<td>68,000</td>
</tr>
<tr>
<td></td>
<td>19,09,000</td>
</tr>
</tbody>
</table>

The following additional information is also provided:

(a) Miscellaneous expenses included Rs. 5,000 audit fees and Rs. 700 for out of pocket expenses paid to the auditors.
(b) 2000 Equity Shares were issued for consideration other than cash.
(c) Debtors of Rs. 52,000 are due for more than six months.
(d) The Cost of Assets:
    - Building Rs. 4,00,000
    - Plant and Machinery Rs. 7,00,000
    - Furniture Rs. 62,500
Company Accounts

(e) The balance of Rs. 1,50,000 in the loan account with State Finance Corporation is inclusive of Rs. 7,500 for interest accrued but not due. The Loan is secured by hypothecation of the Plant & Machinery.

(f) Balance at Bank includes Rs. 2,000 with Simplex Bank Ltd., which is not a scheduled Bank.

(g) Bills Receivable for Rs. 2,75,000 maturing on 30th June, 2002 have been discounted.

(h) The company had contract for the erection of machinery at Rs. 2,50,000 which still incomplete.

Solution :

PRINTEX LTD.

Balance Sheet as at 31st March, 2002 (drawn as per Part-I Schedule - VI)
(Section 211 of the Companies Act)

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>As at 31.3.2002</th>
<th>Assets As at 31.03.2002</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Share Capital</strong></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Authorized</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity Shares of Rs. ...... each</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issued and Subscribed 10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity Shares of Rs. 100 each fully called up</td>
<td>100000</td>
<td></td>
</tr>
<tr>
<td>(of the above, 200 equity share of Rs. 100 each have been issued for consideration other than cash)</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Less:</strong> Calls in arrear</td>
<td>1000</td>
<td>9,99,000</td>
</tr>
<tr>
<td><strong>Reserves &amp; Surplus</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Reserve</td>
<td>2,10,000</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Profit &amp; Loss A/c</td>
<td>1,00,000</td>
<td>2,50,000</td>
</tr>
<tr>
<td><strong>Secured Loans</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loan from State Financial Corporation (secured by hypothecation of Plant &amp; Machinery)</td>
<td>1,42,500</td>
<td>1,48,000</td>
</tr>
<tr>
<td><strong>Unsecured Loans</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unsecured Loans</td>
<td>1,21,000</td>
<td>2,45,000</td>
</tr>
<tr>
<td><strong>Current Liabilities and Provisions</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>A. Current Liabilities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors for goods and Expenses</td>
<td>2,00,000</td>
<td>42,700</td>
</tr>
<tr>
<td>B. Loans &amp; Advances</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Advances</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Miscellaneous Expenditure</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Interest Accrued but not due (S.F.C) (to the extent not written off or adjusted) 13,300

B. Provisions:
- Provision for Taxation 68,000
- Proposed Dividend 60,000

19,08,000 19,08,000

Contingent Liability: Estimated amount of contract remaining to be executed on Capital Account and not provided for Rs. 1,50,000

Notes:
1. Maturing on 30th June, 2002 amounting to Rs. 2,75,000 discounted.
2. Miscellaneous Expenditure included:
   - Audit fees Rs. 5,000
   - Expenses (Out of Pocket) Rs. 700
   - Rs. 5,700
3. The information required to be given under any of the items or sub-items, if it cannot be conveniently included in the Balance Sheet itself, shall be furnished in separate schedule to be annexed to and to form part of the Balance Sheet, specially in case of Balance Sheet drawn vertically.

Illustration 16:

The following balances and particulars are extracted from the books of Pant Co. Pvt. Ltd., for the year ended 31st December 1994:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital: Authorised, issued &amp; fully paid up (50,000 equity shares)</td>
<td>5,00,000</td>
</tr>
<tr>
<td>General Reserve (as at 1.1.94)</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Furniture (including addition of Rs. 5,000)</td>
<td>35,000</td>
</tr>
<tr>
<td>Office equipments (as at 1.4.94)</td>
<td>22,000</td>
</tr>
<tr>
<td>Motor car (purchased on 30.12.94)</td>
<td>30,000</td>
</tr>
<tr>
<td>Sundry debtors (unsecured)</td>
<td>8,50,000</td>
</tr>
<tr>
<td>Advance to staff</td>
<td>10,000</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>2,000</td>
</tr>
<tr>
<td>Balance with Bank of India (including fixed deposits of Rs. 1,00,000)</td>
<td>1,40,000</td>
</tr>
<tr>
<td>Loans from Directors</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Liability for expenses and goods</td>
<td>2,67,000</td>
</tr>
<tr>
<td>Provision for tax (as on 1.1.94)</td>
<td>1,00,000</td>
</tr>
</tbody>
</table>
Company Accounts

Profit & Loss A/c (as on 1.1.94) 3,000
Closing stock (20,000 metres) 3,00,000
Advance Tax paid 1,90,000
Depreciation written off up to 31.12.94
(Furniture : Rs.5,000, Office eqpt : Rs.2,000) 7,000
Opening Stock (10,000 metres) 1,50,000
Legal charges including Rs. 3,000 paid to
auditors for tax representation 10,000
Salaries to staff 50,000
Miscellaneous expenses (including Rs. 4,000 for
tour within India, Rs.36,000 for foreign tour) 2,00,000
Purchase of cloth (2.10 lakh metres) 30,39,000
Audit fees 4,000
Interest on fixed deposit with bank 5,000
Sales (2 lakhs metres) (including export sales
of Rs. 10 lakhs) 35,00,000

Further information :

(a) Rate of depreciation – Furniture 10%, Office equipment 15% and Motor car 20%
(b) M.D. is entitled to commission @ 10% of net profits after providing such
commission subject to maximum of Rs. 36,000 p.a.
(c) Debtors include Rs. 1,50,000 outstanding of more than 6 months. Out of this Rs.
20,000 is considered doubtful for which provision is to be made in the accounts.
(d) Tax liability for 1994 is estimated at Rs. 2,00,000 for which provision is to be made.
(e) Transfer to General Reserve Rs. 50,000 out of net profits and proposed dividend is
@ 6% on equity shares.

Prepare the Balance Sheet, and Profit & Loss Account for the year ended 31st December,
1994, in accordance with the requirements of Companies Act, 1956.
**Financial Accounting Fundamentals**

**Solution:**

**PANT CO. (P) LTD.**

**Balance Sheet as at 31.03.94**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Share Capital:</strong></td>
<td></td>
<td></td>
<td><strong>Fixed Assets:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Authorised, issued, subscribed &amp; fully paid up (50,000 Equity shares)</td>
<td></td>
<td></td>
<td>Furniture</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Rs. 10 fully paid up)</td>
<td>50,000</td>
<td></td>
<td>Addition during year</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Rs. 10 fully paid up)</td>
<td>35,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Reserves and Surplus:</strong></td>
<td></td>
<td></td>
<td><strong>Less : Depreciation</strong></td>
<td>5,000</td>
<td>30,000</td>
</tr>
<tr>
<td>General Reserve</td>
<td>1,50,000</td>
<td></td>
<td>Office equipment</td>
<td>22,000</td>
<td></td>
</tr>
<tr>
<td><strong>Add : Appropriations during the year</strong></td>
<td>50,000</td>
<td>20,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit and Loss A/c</td>
<td>23,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Secured Loan:</strong></td>
<td></td>
<td></td>
<td><strong>Current Assets, Loans/Advances:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loan from Directors</td>
<td>2,00,000</td>
<td></td>
<td>Stock in trade</td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td><strong>Unsecured Loan:</strong></td>
<td></td>
<td></td>
<td>S/D due for more than 6 months</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>— Others</td>
<td>7,00,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Current Liabilities &amp; Provisions :</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liab. for goods and expenses</td>
<td>2,67,000</td>
<td></td>
<td><strong>Less : Prov. for B/D</strong></td>
<td>20,000</td>
<td>8,30,000</td>
</tr>
<tr>
<td>Remuneration to M.D.</td>
<td>32,000</td>
<td>2,99,000</td>
<td>Cash in hand</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Provision for taxation (net of advance tax)</td>
<td>1,10,000</td>
<td></td>
<td>Cash at bank</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Proposed dividend</td>
<td>30,000</td>
<td>1,40,000</td>
<td>Fixed Deposit</td>
<td>1,00,000</td>
<td>1,42,000</td>
</tr>
<tr>
<td></td>
<td>1,42,000</td>
<td></td>
<td>Advances to staff</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>13,62,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Pant Co. (P) Ltd.**

**Trading and Profit and Loss Account for the year ended 31.03.1994**

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td>1,50,000</td>
<td>By Sales :</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Purchases</td>
<td>30,39,000</td>
<td>– Domestic</td>
<td>25,00,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Travelling expenses :</td>
<td></td>
<td>– Export</td>
<td>10,00,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Within India</td>
<td>4,000</td>
<td></td>
<td>35,00,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Outside India</td>
<td>36,000</td>
<td>40,000</td>
<td>By Closing stock</td>
<td>3,00,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Paid to Auditors</td>
<td>4,000</td>
<td>By Interest on fixed deposit</td>
<td>5,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Audit fees</td>
<td>3,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Tax representation fees</td>
<td>7,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Company Accounts

To Legal charges 7,000
To Salaries to staff 50,000
To Provision for bad debts 20,000
To Misc. expenses 1,60,000
To M. D.'s remuneration 32,000
To Provision for taxation 2,00,000
To Net profit c/d 1,00,000

38,05,000 38,05,000
To Proposed dividend 30,000 By Balance b/d (previous year) 3,000
To General Reserve 50,000 By Net Profit b.d 1,00,000
To Balance cd 23,000

1,03,000 1,03,000

(a) Computation of M.D’s Remuneration:

Net profit after taxation provision Rs.
As per profit and loss A/c 1,32,000
Add : Provision for taxation 2,00,000
Add : Provision for bad debt 20,000

3,52,000
M.D.’s Remuneration = 3,52,000 × (10/110) = Rs. 32,000

(b) According to Companies Act where during any financial year any addition has been made to an asset, the depreciation on such asset will be calculated on a prorata basis from the date of such addition. As the Motor Car has been acquired on the last day of the Accounting year no depreciation on the same is chargeable.

Illustration 17:

The Trial Balance of T.V. Ltd. (having authorised capital of Rs. 8,00,000) was at 31.12.96 as under:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital (Share of Rs. 100 each fully paid)</td>
<td>5,00,000</td>
<td></td>
</tr>
<tr>
<td>Share Premium Account</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Land and Building (Cost Rs. 3,00,000)</td>
<td>2,50,000</td>
<td></td>
</tr>
<tr>
<td>Plant and Machinery (Cost Rs. 4,00,000)</td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td>Live Stock</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>Gross Profit Earned during 1996</td>
<td>1,30,000</td>
<td></td>
</tr>
<tr>
<td>General Reserve</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>6% Debentures (Issued on 1st January 1989 secured by mortgage on land and redeemable on 31.12.98)</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors and Creditors</td>
<td>60,000</td>
<td>30,000</td>
</tr>
</tbody>
</table>
### Stock as at 31.12.96 (At cost or market value whichever is lower)

- Stocks: 50,000
- Salaries: 19,000
- Directors’ fees: 10,000
- General Expenses: 15,000
- Cash at Bank: 6,400
- Cash in hand: 600
- Bills Receivables: 20,000
- Discount on issue on debentures: 4,000
- Profit and Loss b/f: 10,000
- Investment (4% Government Securities, Face value Rs. 1,00,000 purchased on 1.1.96): 95,000
- Investments in Eq. Shares (10,000 shares @ Rs. 25 per share, Rs. 20 paid up): 1,70,000

**Total:** 10,20,000

### Further information:

1. Of the shares allotted 2,000 shares worth Rs. 2,00,000 were allotted as fully paid to vendor from whom a running business was acquired.
2. Of the Debtors Rs. 10,000 were outstanding but are considered good except a debt of Rs. 5,000 doubtful to be provided.
3. A provision of Rs. 25,000 is to be made for Income Tax.
4. The Market Value of Government Securities on the date of the Balance Sheet was Rs. 93,000 and that of equity shares was Rs. 1,60,000.
5. Auditor’s fee Rs. 3,000 should be provided for. Included in General Expenses is six months Insurance Rs. 1,500 paid for the year to end on 30th June 1997.
6. Interest on Debentures issued and on Investment in Government Securities should be taken into account.
7. Depreciation is to be provided for @ 6% Original cost of Machinery and 2% on the Original Cost of land and building.
8. Provide for a dividend of 5% on shares.

Prepare Profit and Loss A/c, Profit and Loss Adjustment A/c and the Balance Sheet as on 31st December, 1996.
### Company Accounts

#### Solution:

**T.V. LTD.**

**Profit and Loss Account for the year ended 31.3.96**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To</td>
<td>Salaries</td>
<td>19,000</td>
<td>By Gross profit b/d</td>
</tr>
<tr>
<td>To</td>
<td>Directors’s fees</td>
<td>10,000</td>
<td>By Interest on Govt. securities</td>
</tr>
<tr>
<td>To</td>
<td>General expenses</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Less: Prepaid insurance (6mts.)</td>
<td>750</td>
<td>14,250</td>
</tr>
<tr>
<td>To</td>
<td>Provision for doubtful debt</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Interest on debentures @ 6%</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Depreciation on assets (Note)</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Audit fees</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Net Profit c/d</td>
<td>46,750</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>1,34,000</strong></td>
<td><strong>1,34,000</strong></td>
<td></td>
</tr>
</tbody>
</table>

**Profit & Loss Adjustment A/c for the year ended 31.3.96**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To</td>
<td>Provision for tax</td>
<td>25,000</td>
<td>By Balance b/d</td>
</tr>
<tr>
<td>To</td>
<td>Proposed dividend</td>
<td>25,000</td>
<td>By Net profit during the year</td>
</tr>
<tr>
<td>To</td>
<td>Balance c/d transferred to B/S</td>
<td>6,750</td>
<td></td>
</tr>
<tr>
<td></td>
<td><strong>56,750</strong></td>
<td><strong>56,750</strong></td>
<td></td>
</tr>
</tbody>
</table>

**Balance Sheet as at 31.12.96**

<table>
<thead>
<tr>
<th>Assets</th>
<th>Rs.</th>
<th>Liabilities</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorised Capital:</td>
<td>8,00,000</td>
<td>Fixed Assets: (W.D.V.)</td>
<td>2,44,000</td>
</tr>
<tr>
<td>8,000 equity shares @ Rs. 100 each</td>
<td>8,00,000</td>
<td>Land and Building (cost Rs.3,00,000)</td>
<td>2,26,000</td>
</tr>
<tr>
<td>Issued, Subscribed &amp; paid up Capital:</td>
<td>5,00,000</td>
<td>Plant and Machinery (cost Rs.4,00,000)</td>
<td>2,76,000</td>
</tr>
<tr>
<td>5,000 Eq. sh. @ Rs.100 each, fully paid</td>
<td>5,00,000</td>
<td>Live stock</td>
<td>20,000</td>
</tr>
<tr>
<td>Reserves and Surplus:</td>
<td>2,00,000</td>
<td>Investments:</td>
<td>1,70,000</td>
</tr>
<tr>
<td>General Reserve</td>
<td>2,00,000</td>
<td>Investments 4% Govt. securities</td>
<td></td>
</tr>
<tr>
<td>Profit &amp; Loss (Cr.)</td>
<td>6,750</td>
<td>(face value Rs. 1,00,000)</td>
<td>95,000</td>
</tr>
<tr>
<td>Share premium</td>
<td>50,000</td>
<td>Investment in shares</td>
<td>1,70,000</td>
</tr>
<tr>
<td>Secured Loans:</td>
<td></td>
<td>Current Assets, Loans &amp; Advances:</td>
<td></td>
</tr>
<tr>
<td>6% Debenture (mortgage on land)</td>
<td>1,00,000</td>
<td>Current Assets:</td>
<td></td>
</tr>
<tr>
<td>Unsecured Loans:</td>
<td>Nil</td>
<td>Debt. more than 6 months</td>
<td>10,000</td>
</tr>
<tr>
<td>Current Liabilities and Provisions:</td>
<td></td>
<td>Others</td>
<td>50,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>30,000</td>
<td>Interest on debenture</td>
<td>6,000</td>
</tr>
<tr>
<td>Interest on debenture</td>
<td>6,000</td>
<td>Less : Prov. for B/D</td>
<td>5,000</td>
</tr>
<tr>
<td>Auditor’s fees</td>
<td>3,000</td>
<td>55,000</td>
<td></td>
</tr>
</tbody>
</table>
**Financial Accounting Fundamentals**

| Proposed dividend   | 25,000 | Cash in hand  | 600    
|---------------------|--------|---------------|--------
| Provision for tax   | 25,000 | Cash at bank  | 6,400  
| Bills receivables   | 20,000 |               | 0      

**Loans and Advances :**  
- Interest on Government securities 4,000  
- Prepaid insurance 750  

**Miscellaneous Expenditure :**  
- Discount on debenture 4,000  

| Total                | 9,45,750 | Total                | 9,45,750 |

**Notes :**  
* Depreciation on assets:  
  - Plant & Machinery = 6% on 4,00,000 = Rs. 24,000  
  - Land & Building = 2% on 3,00,000 = Rs. 6,000  
* Market value of investment has not been considered.

**Illustration 18 :**

The Balance Sheet of PQR Ltd. as at 31st March, 1998 is given below:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital Authorised:</td>
<td>30,000</td>
<td>Fixed Assets:</td>
<td>1,15,000</td>
</tr>
<tr>
<td>30,000 Eq. Sh. of Rs. 10 each</td>
<td>3,00,000</td>
<td>Freehold Property</td>
<td>1,15,000</td>
</tr>
<tr>
<td>Issued and Subscribed:</td>
<td>20,000</td>
<td>Current Assets, Loans and Advances:</td>
<td>1,35,000</td>
</tr>
<tr>
<td>20,000 Eq. Sh. of Rs. 10 each fully paid</td>
<td>2,00,000</td>
<td>Stock in Trade</td>
<td>1,35,000</td>
</tr>
<tr>
<td>Reserve and Surplus:</td>
<td></td>
<td>Sundry Debtors</td>
<td>75,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash and Bank Balances</td>
<td>30,000</td>
</tr>
<tr>
<td>Profit and Loss Account</td>
<td>1,20,000</td>
<td>Cash in Hand</td>
<td>2,20,000</td>
</tr>
<tr>
<td>Secured Loan:</td>
<td>1,20,000</td>
<td>Cash at Bank</td>
<td></td>
</tr>
<tr>
<td>12% Debentures</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current Liabilities and Provisions:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>1,15,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proposed Dividend</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>5,75,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

At the Annual General Meeting it was resolved:

(i) To pay the proposed Dividend of 10% in cash.
(ii) To issue one Bonus share for every four shares held.
(iii) To give existing shareholders the option to purchase one Rs. 10 share at Rs. 15 for every four shares held prior to bonus distribution, this option being taken up by all the shareholders.
(iv) To repay the debentures at a premium of 3 per cent.

Give the necessary journal entries and the company’s Balance Sheet after the completion of all these transactions.
**Solution:**

*Journal of PQR Ltd.*

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank Account</td>
<td>75,000</td>
<td>75,000</td>
</tr>
<tr>
<td>To Equity Shareholders Account</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Application money received on 5,000 Shares @ Rs. 15 per share to be issued as rights shares in the ratio of 1:4)</td>
<td>75,000</td>
<td>75,000</td>
</tr>
<tr>
<td>Equity Shareholders Account</td>
<td>75,000</td>
<td>50,000</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Share Premium Account</td>
<td>50,000</td>
<td>25,000</td>
</tr>
<tr>
<td>(Share application money on 5,000 Shares @ Rs. 10 per share transferred to Share Capital Account and Rs. 5 per share to Share Premium Account, vide Board’s Resolution dated......)</td>
<td>75,000</td>
<td>75,000</td>
</tr>
<tr>
<td>Proposed Dividend A/c</td>
<td>20,000</td>
<td>20,000</td>
</tr>
<tr>
<td>To Bank A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Proposed dividend paid to existing shareholders @ 10%)</td>
<td>25,000</td>
<td>25,000</td>
</tr>
<tr>
<td>Share Premium A/c</td>
<td>25,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Profit and Loss A/c</td>
<td>25,000</td>
<td>50,000</td>
</tr>
<tr>
<td>To Bonus to Shareholders A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Amount transferred for issue of bonus shares to existing shareholders in the ratio of 1 : 4 vide General Body’s Resolution dated......)</td>
<td>50,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Bonus to Shareholders A/c</td>
<td>50,000</td>
<td>50,000</td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Issue of bonus shares in the ratio of 1 for 4 vide Board’s Resolution dated......)</td>
<td>1,20,000</td>
<td>1,20,000</td>
</tr>
<tr>
<td>12% Debentures A/c</td>
<td>1,20,000</td>
<td>1,20,000</td>
</tr>
<tr>
<td>Premium Payable on Redemption A/c</td>
<td>3,600</td>
<td>3,600</td>
</tr>
<tr>
<td>To Debentureholders A/c</td>
<td>1,23,600</td>
<td>1,23,600</td>
</tr>
<tr>
<td>(Amount payable to Debentureholders on redemption, at a premium of 3%, transferred to Debentureholders A/c)</td>
<td>1,23,600</td>
<td>1,23,600</td>
</tr>
</tbody>
</table>
**Balance Sheet of PQR Limited as on ....(After completion of transactions) :**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shares Capital:</td>
<td></td>
<td>Fixed Assets:</td>
<td></td>
</tr>
<tr>
<td>Authorised, Issued &amp; Subscribed:</td>
<td></td>
<td>Property</td>
<td>1,15,000</td>
</tr>
<tr>
<td>30,000 Shares of Rs. 10 each fully paid</td>
<td>3,00,000</td>
<td>Investments</td>
<td>—</td>
</tr>
<tr>
<td>(5,000 Shares of Rs.10 each fully paid issued as bonus shares out of share premium and P &amp; L A/c)</td>
<td></td>
<td>Current Assets:</td>
<td></td>
</tr>
<tr>
<td>Reserve &amp; Surplus:</td>
<td></td>
<td>Stock in trade</td>
<td>1,35,000</td>
</tr>
<tr>
<td>Profit &amp; Loss A/c</td>
<td>91,400</td>
<td>Sundry Debtors</td>
<td>75,000</td>
</tr>
<tr>
<td>Secured Loans</td>
<td>—</td>
<td>Cash at Bank</td>
<td>1,51,400</td>
</tr>
<tr>
<td>Unsecured Loans</td>
<td>—</td>
<td>Cash in hand</td>
<td>30,000</td>
</tr>
<tr>
<td>Current Liabilities &amp; Provisions:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>1,15,000</td>
<td></td>
<td>5,06,400</td>
</tr>
<tr>
<td></td>
<td>5,06,400</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Note :**  
The number of bonus shares issued has been calculated on the basis of issued capital before rights issue, i.e., 20,000 shares (and not 25,000 shares after rights issue).

**Illustration 19 :**

The following is the trial balance on 31st March 1999 of Ramesh Ltd.:

<table>
<thead>
<tr>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity capital: Equity shares of Rs. 10 each fully paid</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Reserves and surplus: 31.3.1998</td>
<td>15,00,000</td>
</tr>
<tr>
<td>Bank overdraft (secured against working capital)</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Deposits from directors</td>
<td>6,00,000</td>
</tr>
<tr>
<td>Suppliers A/c</td>
<td>2,50,000</td>
</tr>
<tr>
<td>Customers A/c</td>
<td>28,00,000</td>
</tr>
<tr>
<td>Stock on 31.3.1998</td>
<td>25,000</td>
</tr>
<tr>
<td>Expenses paid</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>
Company Accounts

Prepaid expenses 31.3.1998 4,000
Outstanding expenses 31.3.1998 14,000
Purchases and sales 130,00,000 135,00,000
Returns in and out 1,56,000 1,46,000
Fixed assets: 31.3.1998:
Cost 14,50,000
Provision for depreciation 4,50,000
Interest on loans and overdraft 1,00,000
180,85,000 180,85,000

On 31st March 1999 value of stock was Rs. 75,000; prepaid expenses were Rs. 16,000 and outstanding expenses were Rs. 6,000. Depreciation is to be provided on fixed assets at 15% on reducing balance method.

Ramesh Ltd. asks you to prepare:

(a) revenue statement for the year ended 31.3.99.
(b) balance sheet as at 31.3.99.

Solution:

Working Notes:

1. Dr. Expenses A/c Cr.
   Particulars Rs. Particulars Rs.
   Opening prepaid 4,000 Opening outstanding 14,000
   Expenses paid 3,00,000 Expenses to profit and loss A/c 2,80,000
   Closing outstanding 6,000 Closing prepaid 16,000
   3,10,000 3,10,000

2. Depreciation
   Cost 14,50,000
   Less: Provision for depreciation 4,50,000
   Opening written down value 10,00,000
   Depreciation thereon at 15% 1,50,000

3. Sales
   Gross 1,35,00,000
   Less: Returns inwards 1,56,000
   1,33,44,000

4. Purchases
   Gross 1,30,00,000
   Less: Returns outwards 1,46,000
   1,28,54,000
Financial Accounting Fundamentals

5. Cost of sales
   Opening stock 25,000
   Net purchases 1,28,54,000
   Less : Closing stock 75,000
   1,28,04,000

6. Reserves and surplus
   As per last balance sheet 15,00,000
   Add : Surplus during the year 10,000
   15,10,000

Fixed assets :
   Cost 14,50,000
   Less : Accumulated deprn. up to last year 4,50,000
   for this year 1,50,000
   6,00,000
   8,50,000

Current assets :
   Inventory at cost 75,000
   Customers sued – considered good 28,00,000
   Advance to suppliers 2,50,000
   Prepaid expenses 16,000
   Less : Current liabilities –
   Creditors for goods 9,00,000
   Outstanding expenses 6,000
   Amounts due to customers 75,000
   9,81,000
   21,60,000
   30,10,000

Note : In the absence of information :-
   i) corresponding figures of last financial statement are not furnished
   ii) all information required to be disclosed under Company Law has not been disclosed.

Revenue statement for the year ended 31. 3. 1999

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>1,33,44,000</td>
<td></td>
</tr>
<tr>
<td>Less : Cost of sales</td>
<td>1,28,04,000</td>
<td>5,40,000</td>
</tr>
<tr>
<td>Less : Expenses</td>
<td>2,80,000</td>
<td></td>
</tr>
<tr>
<td>Interest</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Depreciation</td>
<td>1,50,000</td>
<td>5,30,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>10,000</td>
</tr>
</tbody>
</table>
Company Accounts

**Balance Sheet as at 31.3.1999**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sources of funds :–</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Shareholders' funds :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share capital :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issued : 50000 equity shares of Rs. 10 each</td>
<td>5,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>15,10,000</td>
<td>20,10,000</td>
</tr>
<tr>
<td>Loan funds :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Secured : from bank – against working capital</td>
<td>4,00,000</td>
<td></td>
</tr>
<tr>
<td>Unsecured : from directors</td>
<td>6,00,000</td>
<td>10,00,000</td>
</tr>
<tr>
<td></td>
<td>30,10,000</td>
<td></td>
</tr>
</tbody>
</table>

4.10 SPECIMEN QUESTIONS WITH ANSWERS

**Question 1:**

D Ltd. has authorised capital of Rs. 4,00,000. The company issues 20,000 equity shares of Rs. 10 each at a premium of Rs. 5 per share payable as:

- On application — Rs. 6 (including premium Rs. 3)
- On allotment — Rs. 5 (including balance of premium)
- Balance in two calls.

Applications were received for 35,000 shares. The applicants were divided in the following groups:

- Group A — Applying for 5,000 shares allotted fully.
- Group B — Applying for 20,000 shares are made prorata allotment for 15,000 shares.
- Group C — Applying for total 10,000 shares are refunded.

Directors while making allotment adjust the excess amount received on application against allotment money due. When second and final calls were made shareholders holding 500 shares failed to pay the final call money. The directors forfeited these shares. All the forfeited shares were reissued at Rs. 9 per share. It is agreed that brokerage @ 3% and underwriting commission @ 3% will be paid for this issue. Claims of brokers and underwriters are satisfied by issuing to them additional equity shares of Rs. 10 each at a premium of Rs. 5 per share (without any cash payment).

Show Journal Entries and the Balance Sheet of the company in the books of the company.
**Financial Accounting Fundamentals**

**Answer:**

In the books of D Ltd.

**JOURNAL ENTRIES**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Rs.(Dr.)</th>
<th>Rs.(Cr.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bank Account</td>
<td>Dr.</td>
<td>2,10,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Capital Account</td>
<td></td>
<td>2,10,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(being the application money received on 35,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>shares @ Rs. 6 per share)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Equity Share Application Account</td>
<td>Dr.</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bank Account</td>
<td></td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(being the application on 10,000 shares refunded)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Equity Share Application Account</td>
<td>Dr.</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Capital</td>
<td></td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share premium</td>
<td></td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(being the application money on 20,000 shares</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>transferred to share premium and share capital)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Equity Share Application Account</td>
<td>Dr.</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Allotment Account</td>
<td></td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(being excess of application money adjusted against</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>allotment money due)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Equity Share allotment account</td>
<td>Dr.</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Capital Account</td>
<td></td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Share Premium Account</td>
<td></td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(being the amount due on allotment @ Rs. 5 per share</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>including a premium of Rs. 2 as per board’s resolution</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>no. ...... dated....)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Bank Account</td>
<td>Dr.</td>
<td>70,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Allotment Account</td>
<td></td>
<td>70,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(being balance of allotment money received in full</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>for 14,000 shares)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Equity Share First Call Account</td>
<td>Dr.</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Equity Share Capital Account</td>
<td></td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(being the call money due on 20,000 shares @ Rs. 2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>per share)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Company Accounts

Bank Account
- Dr. 40,000
  - To Equity Share First Call Account 40,000
    (being the first call money received)

Equity Share Final Call Account
- Dr. 40,000
  - To Equity Share Capital Account 40,000
    (being the call money due on 20,000 shares @ Rs. 2 per share)

Bank Account
- Dr. 39,000
  - To Equity Share Final Call Account 39,000
    (being the call money on 19,500 shares received)

Equity Share Capital Account
- Dr. 5,000
  - To Equity Share Final Call Account 1,000
  - To Share Forfeiture Account 4,000
    (being 500 shares forfeited)

Bank Account
- Dr. 4,500
  - Share Forfeiture Account 500
    (being 500 shares reissued @ Rs. 9 per share)

Share Forfeiture Account
- Dr. 3,500
  - To Capital Reserve Account 3,500
    (being profit on forfeiture transferred to capital reserve account)

Brokerage Account
- Dr. 6,000
  - To Equity Share Capital Account 8,000
  - To Share Premium Account 4,000
    (being brokerage and commission paid)
### Financial Accounting Fundamentals

#### Balance Sheet of D Ltd.

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital –</td>
<td></td>
<td>Fixed Assets –</td>
<td></td>
</tr>
<tr>
<td>Authorised Capital :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>40,000 shares on Rs. 10 each</td>
<td>4,00,000</td>
<td>Investments :</td>
<td></td>
</tr>
<tr>
<td>Issued, Subscribed and Paid-up Capital</td>
<td></td>
<td>Current Assets, Loans and Advances :</td>
<td></td>
</tr>
<tr>
<td>20,800 Equity Shares of Rs. 10 each</td>
<td>3,03,500</td>
<td>Bank</td>
<td>3,03,500</td>
</tr>
<tr>
<td>(800 shares issued for consideration</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>other than cash)</td>
<td>2,08,000</td>
<td>Miscellaneous expenditure :</td>
<td></td>
</tr>
<tr>
<td>Reserve &amp; Surplus :</td>
<td>3,500</td>
<td>Brokerage on issue of shares</td>
<td>6,000</td>
</tr>
<tr>
<td>Capital Reserve</td>
<td>1,04,000</td>
<td>Commission on issue of shares</td>
<td>6,000</td>
</tr>
<tr>
<td>Share Premium</td>
<td>3,15,500</td>
<td>Commission on issue of shares</td>
<td>3,15,500</td>
</tr>
</tbody>
</table>

#### Question 2:

Sun Ltd. issued 20,000 Equity Shares of Rs. 10 each payable as follows:

- **On Application** Rs. 5 (including Rs. 2 as premium)
- **On Allotment** Rs. 5
- **On Call** Rs. 2

Applications were received for 36,000 Shares of which the application money on 6,000 Shares were refunded and allotment was made to the rest of the applicants on pro-rata basis. All the money due on Shares was received in full with the exception of allotment money on 200 Shares and Call Money on 500 Shares (including those on which allotment money was due). These 500 Shares were forfeited by the Company. Subsequently, 400 of these shares of which 200 were those Shares on which allotment money was not paid, were reissued at Rs. 7 per Share.

Show the Journal entries (including the Cash transactions) relating to the forfeiture and reissue of the Shares.
**Answer:**

In the books of Sun Ltd.

**JOURNAL**

*(All figures are in Rs.)*

<table>
<thead>
<tr>
<th>Particulars</th>
<th>L/F</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>i) Bank A/c</td>
<td></td>
<td></td>
<td>1,80,000</td>
</tr>
<tr>
<td>To Share Application A/c (36,000×5)</td>
<td></td>
<td>1,80,000</td>
<td></td>
</tr>
<tr>
<td><em>(Being application money received)</em></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ii) Share Application A/c</td>
<td></td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>To Bank (6000×5)</td>
<td></td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td><em>(Being application money refunded)</em></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>iii) Share application A/c</td>
<td></td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital</td>
<td></td>
<td></td>
<td>60,000</td>
</tr>
<tr>
<td>To Equity Share Premium A/c</td>
<td></td>
<td></td>
<td>40,000</td>
</tr>
<tr>
<td>To Equity Share Allotment A/c</td>
<td></td>
<td></td>
<td>50,000</td>
</tr>
<tr>
<td><em>(Being application money transferred to Capital A/c and Premium A/c after adjusting excess application money with allotment as per Bond Resolution No. ...... dt. ......)</em></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>iv) Share Allotment A/c</td>
<td></td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital (20,000×5)</td>
<td></td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td><em>(Being allotment money due for 20,000 equity shares as per Bond Resolution No. ...... dt. ......)</em></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>v) Bank A/c</td>
<td></td>
<td>49,500</td>
<td></td>
</tr>
<tr>
<td>Call in Arrear A/c</td>
<td></td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Allotment A/c</td>
<td></td>
<td></td>
<td>50,000</td>
</tr>
<tr>
<td><em>(Being allotment money received except 200 shares)</em></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>vi) Share Call Money A/c</td>
<td></td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital (20,000×2)</td>
<td></td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td><em>(Being Call money due as per Board's Resolution No. ...... dt. ......)</em></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>vii) Bank A/c</td>
<td></td>
<td>39,000</td>
<td></td>
</tr>
<tr>
<td>Call in Arrear A/c</td>
<td></td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>To Share Call Money</td>
<td></td>
<td></td>
<td>40,000</td>
</tr>
<tr>
<td><em>(Being Call money received except 500 Shares)</em></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

viii) Equity Share Capital A/c Dr. 5,000
    To Call in Arrear A/c 1,500
    To Share Forfeiture A/c (1100 + 2400) 3,500
    (Being 500 Non payment shares forfeited as per
    Board's Resolution No. ...... dt. ......)

ix) Bank A/c (400×7) Dr. 2,800
    Share Forfeiture A/c Dr. 1,200
    To Share Capital A/c 4,000
    (Being 400 Forfeiture shares revised @ Rs. 7 per share
    as per Board's Resolution No. ...... dt. ......)

x) Share Forfeiture A/c Dr. 1,500
    To Capital Reserve A/c 1,500
    (Being Profit on revised transferred to Capital
    Reserve as per Board's Resolution No. ...... dt. ......)

Working Note :

1) Due on allotment money for 200 shares.
   Shares applied for  =  200 x 30,000 / 20,000  =  300 Shares.
   Application Money Received Rs. 1,500
   Excess Money received in application  =  (300 – 200)×5  =  500
   Due for allotment ...... Rs.200×5 = 1,000
   Less : Excess Received (-500)
   Allotment money failed to pay (200×2.50)  500
   Out of application money Rs.1500. Amount of Premium is Rs.400 for 200 Shares
   allotted and Balance 1100 for application and Partly allotment.

2) Profit on Reissue 400 shares.
   For 200 Share forfeiture amount  =  Rs. 1,100
   Now For 300 Share forfeiture amount  =  Rs. 2,400
   For 200 Share forfeiture amount is  =  2,400 x 200 /300  =  1,600
   Profit on Reissue = (2700 – 1200)  =  1,500
   Balance of Forfeiture A/c will be  = (3500 – 2700)  =  Rs. 800.
Company Accounts

Question 3:

The following Ledger balances are extracted from the books of QR Ltd. as on 30.9.98:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>9% Debenture issued @ Rs. 95</td>
<td>9,50,000</td>
</tr>
<tr>
<td>Debenture Redemption Reserve Fund A/c</td>
<td>9,37,000</td>
</tr>
<tr>
<td>Discount on issue of Debentures</td>
<td>26,000</td>
</tr>
<tr>
<td>Investment against Debenture Redemption Reserve Fund</td>
<td>9,37,000</td>
</tr>
</tbody>
</table>

Following further information is given:

(a) Investments include debentures of the face value of Rs. 2,00,000 purchased on 1.8.98 @ Rs. 99.
(b) Interest on debentures is payable on 30th June and 31st December.
(c) All debentures are redeemable at par on 31st December.
(d) Income from outside investments of Redemption Fund from 30.9.98 to 31.12.98 is Rs. 45,000

Show ledger accounts assuming that the above transactions have been carried out and all outside investments were sold at a gain of 10% over cost.

Solution:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Debit</th>
<th>Cr.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td></td>
<td>1998</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Oct. 1st</td>
<td>To Balance</td>
<td>Dec 31st</td>
<td>To Sinking Fund (Profit on Sales)</td>
<td>73,900</td>
<td>Dec 31st</td>
<td>By Bank</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(Transfer to separate A/c)</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>9,37,000</td>
<td>Oct 1st</td>
<td>By (own Debenture Inv. A/c)</td>
</tr>
<tr>
<td>10,10,900</td>
<td></td>
<td>10,10,900</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## Financial Accounting Fundamentals

### Debenture Redemption Fund (Own Debentures) Investment A/c

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To D.R.F. Investment A/c (Transfer)</td>
<td>1,98,000</td>
<td>By 9% Debenture A/c</td>
<td>2,00,000</td>
</tr>
<tr>
<td>&quot; D.R.R.F. (Profit on cancellation)</td>
<td>2,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,00,000</td>
<td></td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

### Debenture Redemption Reserve Fund

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Discount on issue of Debentures</td>
<td>26,000</td>
<td>By Balance b/d</td>
<td>9,37,000</td>
</tr>
<tr>
<td>&quot; Capital Reserve (Profit on cancellation of Debentures)</td>
<td>2,000</td>
<td>By Debenture A/c (on Rs. 2,00,000 for 5 months)</td>
<td>7,500</td>
</tr>
<tr>
<td>&quot; General Reserve</td>
<td>10,37,400</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>10,65,400</td>
<td></td>
<td>10,65,400</td>
</tr>
</tbody>
</table>

### Discount on Issue of Debentures

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec. 31st 1998 To Balance B/D</td>
<td>26,000</td>
<td>Dec. 31st 1998 By D.R.F.</td>
<td>26,000</td>
</tr>
<tr>
<td></td>
<td>26,000</td>
<td></td>
<td>26,000</td>
</tr>
</tbody>
</table>

### 9% Debentures A/c

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To DRF (own Debentures Inv. A/c)</td>
<td>2,00,000</td>
<td>By Balance b/d</td>
<td>9,50,000</td>
</tr>
<tr>
<td>&quot; Bank</td>
<td>7,50,000</td>
<td></td>
<td>9,50,000</td>
</tr>
<tr>
<td></td>
<td>9,50,000</td>
<td></td>
<td>9,50,000</td>
</tr>
</tbody>
</table>
Company Accounts

Question 4:

Rajesh Ltd. furnishes you with the following balance sheet as at 31st March, 2001:

(Rs. in crores)

Sources of Funds:
Share Capital
Authorised
Issued 100
10% Redeemable preference shares of Rs.100 each fully paid 75
Equity shares of Rs. 10 each fully paid 25 100
Reserve and surplus
Capital reserves 15
Share premium 25
Revenue reserves 260 300 400

Funds employed in:
Fixed assets (cost) 100
Less Provision for depreciation 100 Nil
Investment (at cost) (Market value Rs. 400 crores) 100
Current assets 340
Less Current liabilities 40 300 400

The company redeemed preference shares on 1st April, 2001. It also bought back 50 lakh equity shares of Rs.10 each at Rs. 50 per share. The payments for the above were made out of the huge bank balances, which appeared as part of current assets.

You are asked to:

(i) Pass journal entries to record the above and
(ii) prepare balance sheet.

Answer (i):

Note: As regards redemption of redeemable preference shares and buy back of shares, section 80 of the Companies Act is on redemption of redeemable preference share and Section 77A, introduced by the Companies (Amendment) Act, 1999 is on buy back of shares. While section 80 provides that redemption of redeemable preference shares can be made either out of proceeds of fresh issue or out of profits available for distribution. Section 77A provides that buy back of shares can be made –
Financial Accounting Fundamentals

(a) out of free reserves or
(b) security premium A/c or
(c) out of proceeds of fresh issue of capital.

However, section 80 provides that premium on redemption can be provided either out of profits or out of security premium account.

In the given problem the company redeemed the preference shares at par, but buy-back of equity shares at a premium. The company bought back 50 lakh equity shares @ Rs. 50 per share which is equal to security premium account. It is, therefore, presumed that the buy back of shares have been made out of security premium account and redemption of preference shares out of profit available for dividend. There can be other presumptions too, like both redemption of redeemable preference shares and buy back of shares have been made out of profit or out of free reserves as the case may be.

SEBI Guidelines and Rules framed by Company Law Board further requires that in case of buy back of shares, the company must open an escrow account by depositing the requisite amount to a designated bank or by giving guarantee of payment during the book building procedure and also open a separate designated account with its bankers for payment of shareholders.

Journal Entries

(Rs. in lakhs)

Re. Redeemable Preference Shares :

10% Redeemable Preference shares A/c Dr. 75
To Redeemable Preference Shareholders A/c 75
(Being the amount transferred to latter A/c as per Board resolution dated ……)

Redeemable Preference Shareholders A/c Dr. 75
To Bank 75
(Being the payment made to redeemable Preference shareholders)

Revenue Reserve A/c Dr. 75
To Capital Redemption Reserve Account 75
(Being the amount transferred from Revenue Reserve as per Board Resolution dated ……in terms of s.80 of the Companies Act, 1956)
Company Accounts

Re. Buy Back of Equity Shares:

Escrow Bank A/c Dr. 5
To Bank A/c 5
(Being amount transferred to Escrow Bank A/c opened as per Board Resolution dated .... and for buy back of equity shares along with authorisation of payment to be made by merchant bankers for payment.)

Equity Share Capital A/c Dr. 5
Premium on buy back of Equity Shares Dr. 20
To Shareholders A/c 25
(Being the amount of equity share capital bought back at premium of Rs. 40 per share as per special resolution dated ..... passed on extra ordinary General Meeting held on .......)

Bank A/c for Buy-back of shares Dr. 25
To Escrow Bank A/c 5
To Bank A/c 20
(Being the amount transferred from latter accounts to former A/c as per Board Resolution dated .....)

Shareholders A/c Dr. 25
To Bank A/c for buy back of shares 25
(Being the payment made to equity shareholders on buy back of shares as per special resolution passed on extra ordinary General Meeting dated ...... held on.........)

Security Premium A/c Dr. 5
To Capital Redemption Reserve 5
(Being the transfer of security premium account to Capital Redemption Reserve A/c for the purpose of buy-back of 50 lakhs equity shares of Rs. 10 each.)

General Reserve A/c Dr. 20
To Premium on buy back of equity shares 20
(Being the premium on buy back of equity shares transferred to General Reserve Account)
Financial Accounting Fundamentals

Note:
Section 77A, unlike section 80, is silent about treatment of Premium on buy-back of equity shares. No authoritative pronouncement is made available. One school of thought is that the premium may be adjusted against security premium account while other school of thought that it may be adjusted against revenue reserve or may be treated as Deferred Revenue Expenditure account. Accordingly the entry may be passed.

Answer (ii):

Rajesh Ltd.
Balance Sheet as on 1.4.2001

(Rs. in crores)

I. Sources of Funds:

<table>
<thead>
<tr>
<th>Shareholders Funds</th>
<th>Schedule</th>
<th>(Rs. in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Capital</td>
<td>1</td>
<td>20</td>
</tr>
<tr>
<td>(b) Reserves &amp; Surplus</td>
<td>2</td>
<td>280</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>300</td>
</tr>
</tbody>
</table>

II. Application of Funds:

<table>
<thead>
<tr>
<th>Fixed Assets</th>
<th>Gross Block</th>
<th>100</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less : Depreciation</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Investments (Market value Rs. 400 crores)</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Current Assets</td>
<td>240</td>
<td></td>
</tr>
<tr>
<td>Less : Current liabilities</td>
<td>40</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>300</td>
<td></td>
</tr>
</tbody>
</table>

Schedules:

Schedule 1:
Share Capital —
Authorised Share Capital –
Authorised ?
Issued, Subscribed and Paid up 20
7,50,000, 10% Redeemable Preference shares of Rs. 100 each fully paid redeemed at par as per terms and conditions of issue on 1.4.2001 —
20,00,000 (P.Y. 25,00,000) Equity shares of Rs. 10 each fully called and paid up 20
20
Schedule 2:

(1) Capital Reserve (As per last A/c) 15
(2) Capital Redemption Reserve –
   Transferred from Security Premium 5
   Transferred from Revenue Reserve 75 80
(3) Security Premium A/c—
   As per last A/c 25
   Less : Transferred to Capital Redemption Reserve on
   account of Buy Back of Equity Shares 5 20
(4) Revenue Reserve —
   As per last A/c 260
   Less: Premium on Buy-back of Equity Shares 20
   Less: Transferred to Capital Redemption Reserve
   on redemption of Redeemable Preference Shares 240 165

280

Question 5:

On 1st December, 1999 Mehul Ltd. was incorporated with authorised capital of Rs. 1 core. On 30th November, 2000 the following is its Trial Balance:

<table>
<thead>
<tr>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity share capital (fully paid up shares of Rs. 10 each of which 1,00,000 shares are issued for consideration other than cash Rs. 10,00,000)</td>
<td>25,00,000</td>
</tr>
<tr>
<td>Capital reserve</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Fixed assets — cost</td>
<td>8,00,000</td>
</tr>
<tr>
<td>Purchases (net)</td>
<td>60,00,000</td>
</tr>
<tr>
<td>Sales (net)</td>
<td>75,00,000</td>
</tr>
<tr>
<td>Expenses</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Provision for depreciation</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Bank — current account — scheduled bank</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Interim dividend</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Liability for interim dividend</td>
<td>1,80,000</td>
</tr>
<tr>
<td>Creditors for goods</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Creditors for expenses</td>
<td>20,000</td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>50,000</td>
</tr>
<tr>
<td>Advance from customers</td>
<td>1,00,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Advance to suppliers 1,50,000
Customers dues 32,00,000
Tax payment 4,00,000

1,16,00,000 1,16,00,000

On 30th November, 2000, the cost of unsold stock is Rs. 3,50,000. Customers dues are unsecured but considered good and are due for less than six months. Provide for taxation at 35%. Directors have proposed final dividend of Rs. 2,00,000 and appropriation to general reserve of Rs. 2,50,000.

Prepare the final accounts.

Answer:

Mehul Ltd Revenue statement for the year ended 30th November, 2000

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>75,00,000</td>
</tr>
<tr>
<td>Cost of sales :</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>60,00,000</td>
</tr>
<tr>
<td>Less : Inventory-year end</td>
<td>3,50,000</td>
</tr>
<tr>
<td></td>
<td>56,50,000</td>
</tr>
<tr>
<td>Expenses</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Profit before tax</td>
<td>13,50,000</td>
</tr>
<tr>
<td>Provision for tax @ 35%</td>
<td>4,72,500</td>
</tr>
<tr>
<td>Profit after tax</td>
<td>8,77,500</td>
</tr>
<tr>
<td>Less : Appropriation to :</td>
<td></td>
</tr>
<tr>
<td>General reserve</td>
<td>2,50,000</td>
</tr>
<tr>
<td>Interim dividend</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Proposed dividend</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Balance carried forward</td>
<td>1,27,500</td>
</tr>
</tbody>
</table>

Mehul Ltd.

Balance Sheet as at 30th November 2000

<table>
<thead>
<tr>
<th>Schedule</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sources of funds :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Shareholder’s fund :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Capital</td>
<td>A</td>
<td>25,00,000</td>
</tr>
<tr>
<td>Reserves and surplus :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital reserve</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>General reserve</td>
<td>2,50,000</td>
<td></td>
</tr>
<tr>
<td>Surplus</td>
<td>1,27,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>5,77,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>30,77,500</td>
<td></td>
</tr>
</tbody>
</table>
## Company Accounts

### Funds employed in:

- **Fixed assets**: Cost 8,00,000
- **Less**: Provision for depreciation 1,00,000 7,00,000

### Current assets:

- **Inventory at cost**: 3,50,000
- **Dues from customers-unsecured but considered good for less than 6 mths**: 32,00,000
- **Balance with scheduled bank in current account**: 2,00,000
- **Advances recoverable in cash or in kind (50,000 + 1,50,000)**: 2,00,000
- **Tax payment pending assessment**: 4,00,000

### Less: Current liabilities and provisions

- **Creditors for goods**: 10,00,000
- **Creditors for expenses**: 20,000
- **Advances from customers**: 1,00,000
- **Interim dividend**: 1,80,000
  
  **Total**: 13,00,000

- **Provision for taxation**: 4,72,500
- **Proposed dividend**: 2,00,000

### Schedule A: Schedule Capital:

- **Authorised**:
  - 10,00,000 equity shares of Rs. 10 each 1,00,00,000
- **Issued**: 2,50,000 equity shares of Rs. 10 each fully paid – 25,00,000
  - including 1,00,000 equity shares of Rs. 10 each issued for consideration other than cash.

### Question 6:

On 30th November, 2001 the following was the balance sheet of XY and Co. a partnership firm where X Ltd. and Y Ltd. were partners sharing profits and losses in the ratio of 3 : 2 after payment of interest on fixed capitals at 12% per annum.
### Financial Accounting Fundamentals

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs. (in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Fixed assets</strong></td>
<td><strong>60</strong></td>
</tr>
<tr>
<td>Less: Accumulated depreciation</td>
<td><strong>40</strong></td>
</tr>
<tr>
<td>Investments at cost in equity shares of: A Ltd. (market value Rs. 80 Cr.)</td>
<td><strong>30</strong></td>
</tr>
<tr>
<td>B Ltd. (market value of Rs. 70 Cr.)</td>
<td><strong>25</strong></td>
</tr>
<tr>
<td><strong>Current assets</strong></td>
<td><strong>140</strong></td>
</tr>
<tr>
<td>Less: Current liabilities</td>
<td><strong>65</strong></td>
</tr>
<tr>
<td><strong>150</strong></td>
<td></td>
</tr>
<tr>
<td><strong>Financed by:</strong></td>
<td></td>
</tr>
<tr>
<td>Loan from Zed Ltd. carrying interest at 15% p.a.</td>
<td><strong>40</strong></td>
</tr>
<tr>
<td>Reserves</td>
<td><strong>30</strong></td>
</tr>
<tr>
<td>Current accounts of partners: X Ltd.</td>
<td><strong>3</strong></td>
</tr>
<tr>
<td>Y Ltd.</td>
<td><strong>2</strong></td>
</tr>
<tr>
<td><strong>Capital accounts of partner(s):</strong></td>
<td></td>
</tr>
<tr>
<td>X Ltd.</td>
<td><strong>40</strong></td>
</tr>
<tr>
<td>Y Ltd.</td>
<td><strong>35</strong></td>
</tr>
<tr>
<td><strong>150</strong></td>
<td></td>
</tr>
</tbody>
</table>

On 1st December, 2001 they decided to admit Z Ltd. as a partner. The following terms were agreed upon:

1. Zed Ltd.’s loan is to be converted into fixed capital.
2. The goodwill of the firm is considered to be worth Rs. 50 crores; however the necessary adjustment should be recorded through fixed capital accounts of the partners.
3. The fixed assets are considered to be worth Rs. 50 crores. However they are to continue to appear in the books at the present cost of Rs. 60 crores and the present accumulated provision for depreciation of Rs. 40 crores. The necessary adjustment is to be done through fixed capital accounts.
4. There is no change in the valuations of current assets and current liabilities.
5. Reserves are to continue to appear at the balance sheet figures. However necessary adjustment is to be done through fixed capital accounts.
6. The investments in A Ltd. are to be taken over by X Ltd. at Rs. 70 crores. The investments in B Ltd. are to be taken over by Y Ltd. at Rs. 60 crores.
7. X Ltd., Y Ltd. and Z Ltd. are to bring in such amounts as fixed capital as would enable combined balance of Rs. 120 crores in the fixed capital accounts carried forward in revised profit sharing ratio.
(viii) Interest at 1% per month is to be calculated on the fixed capitals and credited to partner’s current accounts.

(ix) 10% of annual profit (after considering interest on fixed capitals) is to be credited to reserves.

(x) The balance 90% of annual profit is to be shared by X Ltd., Y Ltd. and Z Ltd. in the ratio of 5:3:2. The same is to be credited to current accounts.

(xi) Drawings of the partners during the year are to be within the upper ceiling of credit to current accounts. The same is to be credited to current accounts.

You are asked to pass necessary accounting entries through the journal of the firm on the morning of December 1, 2001 and prepare the balance sheet before any other transaction takes place on December 1, 2001. The balance sheet should also show the comparative position before admission of Zed Ltd.

**Answer:**

**JOURNAL**

**(Rs. in Crores)**

<table>
<thead>
<tr>
<th>Date</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001 Dec. 1</td>
<td>Zed Ltd. Loan</td>
<td>40</td>
</tr>
<tr>
<td></td>
<td>To Zed Ltd. – Capital</td>
<td>40</td>
</tr>
<tr>
<td></td>
<td>(Being transfer of loan balance into fixed capital on admission of Zed Ltd. as a partner)</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Zed Ltd. – Capital</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>To X Ltd. – Capital</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>To Y Ltd. – Capital</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>(Being 1/5th share of goodwill purchased by incoming partner Zed Ltd. from the old partners X Ltd. and Y Ltd.)</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Zed Ltd. Capital</td>
<td>6</td>
</tr>
<tr>
<td></td>
<td>To X Ltd. – Capital</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>To Y Ltd. – Capital</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>(Being the purchase of 20% share of latent increase in the value of fixed assets by Zed Ltd. from X Ltd. and Y Ltd. on admission as a partner)</td>
<td></td>
</tr>
</tbody>
</table>
4. **Zed Ltd. – Capital**
   - Dr. 6
   - To X Ltd. – Capital 3
   - To Y Ltd. – Capital 3
   (Being 20% share in existing reserves purchased by incoming partner Zed Ltd. from X Ltd. and Y Ltd.)

5. **X Ltd. – Capital**
   - Dr. 70
   - To Investment in A Ltd. 30
   - To Realisation A/c 40
   (Being investments in A Ltd. taken over by X Ltd.)

6. **Y Ltd. – Capital**
   - Dr. 60
   - To Investments in B Ltd. 25
   - To Profit on take over 35
   (Being investments in B Ltd. taken over Y Ltd.)

7. **Realisation A/c**
   - Dr. 75
   - To Capital A/cs
     - X Ltd. 45
     - Y Ltd. 30
   (Being profit on take over of investments credited to partners’ capitals in old profit sharing ratio.)

8. **Bank A/c (Current asset)**
   - Dr. 60
   - To Fixed capitals:
     - X Ltd. 34
     - Y Ltd. 20
     - Z Ltd. 6
   (Being fixed capital introduced by the three partners in pursuance of clause of partnership deed dated Dec. 1, 2001)

**Working Notes:**

(A) Change in Partners’ Profit Sharing Ratio on admission of Z Ltd.:

<table>
<thead>
<tr>
<th></th>
<th>Old Ratio</th>
<th>New Ratio</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>X Ltd.</td>
<td>3/5</td>
<td>5/10</td>
<td>(−) 1/10</td>
</tr>
<tr>
<td>Y Ltd.</td>
<td>2/5</td>
<td>3/10</td>
<td>(−) 1/10</td>
</tr>
<tr>
<td>Z Ltd.</td>
<td></td>
<td>2/10</td>
<td>+ 2/10</td>
</tr>
<tr>
<td></td>
<td>1</td>
<td>1</td>
<td>0</td>
</tr>
</tbody>
</table>
### Company Accounts

**B) Adjustment in Fixed Capital of Partners on account of goodwill:**

<table>
<thead>
<tr>
<th></th>
<th>X Ltd.</th>
<th>Y Ltd.</th>
<th>Z Ltd.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goodwill raised</td>
<td>Rs. 30 (CR)</td>
<td>Rs. 20 (CR)</td>
<td>–</td>
</tr>
<tr>
<td>Goodwill w/off</td>
<td>Rs. 25 (DR)</td>
<td>Rs. 15 (DR)</td>
<td>10 (DR)</td>
</tr>
<tr>
<td>Net effect</td>
<td>5 (CR)</td>
<td>5 (CR)</td>
<td>10 (DR)</td>
</tr>
</tbody>
</table>

**C) Adjustment in Fixed Capital due to revaluation of Fixed Assets:**

<table>
<thead>
<tr>
<th></th>
<th>X Ltd.</th>
<th>Y Ltd.</th>
<th>Z Ltd.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Difference</td>
<td>18</td>
<td>12</td>
<td>–</td>
</tr>
<tr>
<td>Written Back to book value</td>
<td>15</td>
<td>9</td>
<td>6</td>
</tr>
<tr>
<td>3 (CR)</td>
<td>3 (CR)</td>
<td>6 (CR)</td>
<td></td>
</tr>
</tbody>
</table>

**D) Adjustment on A/c of Reserves due to admission of Z Ltd.:**

<table>
<thead>
<tr>
<th></th>
<th>X Ltd.</th>
<th>Y Ltd.</th>
<th>Z Ltd.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reserves as per old Ratio</td>
<td>18</td>
<td>12</td>
<td>–</td>
</tr>
<tr>
<td>Reversal as per new Ratio</td>
<td>15</td>
<td>9</td>
<td>6</td>
</tr>
<tr>
<td>3 (CR)</td>
<td>3 (CR)</td>
<td>6 (CR)</td>
<td></td>
</tr>
</tbody>
</table>

**E) Adjustment on A/c of takeover of Investment:**

<table>
<thead>
<tr>
<th></th>
<th>X Ltd.</th>
<th>Y Ltd.</th>
<th>Z Ltd.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit on sale of Investment in A Ltd. (Rs. 70 – 30)</td>
<td>40</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit on sale of Investment in B Ltd. (Rs. 60 – 25)</td>
<td>35</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
| This profit will be allocated amongst the erstwhile partners i.e. X Ltd. and Y Ltd. in their old profit sharing ratio i.e. 3 : 2, Rs. 45 and Rs. 30.
Financial Accounting Fundamentals

(F) Net effect of changes:

<table>
<thead>
<tr>
<th></th>
<th>X Ltd.</th>
<th>Y Ltd.</th>
<th>Z Ltd.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>DR</td>
<td>CR</td>
<td>DR</td>
</tr>
<tr>
<td>Goodwill</td>
<td>5</td>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td>Fixed Assets</td>
<td>3</td>
<td>3</td>
<td>6</td>
</tr>
<tr>
<td>Reserve</td>
<td>3</td>
<td>3</td>
<td>6</td>
</tr>
<tr>
<td>Sale of investment</td>
<td>70</td>
<td>45</td>
<td>60</td>
</tr>
<tr>
<td></td>
<td>70</td>
<td>56</td>
<td>60</td>
</tr>
<tr>
<td>Capital before changes</td>
<td>40</td>
<td>35</td>
<td>40</td>
</tr>
<tr>
<td>Capital after changes</td>
<td>26</td>
<td>16</td>
<td>18</td>
</tr>
<tr>
<td>Capital as per partnership deed</td>
<td>60</td>
<td>36</td>
<td>24</td>
</tr>
<tr>
<td>Amount to be brought in</td>
<td>34</td>
<td>20</td>
<td>6</td>
</tr>
</tbody>
</table>

*XY and Co.*

Balance sheet as on the morning of 1st Dec. 2001

<table>
<thead>
<tr>
<th></th>
<th>After admission (in crores)</th>
<th>Before admission (in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Fixed assets:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost</td>
<td>60</td>
<td>60</td>
</tr>
<tr>
<td>Less: Accumulated depreciation</td>
<td>40</td>
<td>40</td>
</tr>
<tr>
<td></td>
<td>20</td>
<td>20</td>
</tr>
<tr>
<td>Investment at cost in equity shares of:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>A Ltd.</td>
<td>–</td>
<td>30</td>
</tr>
<tr>
<td>B Ltd.</td>
<td>–</td>
<td>25</td>
</tr>
<tr>
<td></td>
<td></td>
<td>55</td>
</tr>
<tr>
<td>Current assets:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank</td>
<td>60</td>
<td>–</td>
</tr>
<tr>
<td>Other</td>
<td>140</td>
<td>140</td>
</tr>
<tr>
<td></td>
<td>200</td>
<td>140</td>
</tr>
<tr>
<td>Less: Current liabilities</td>
<td>65</td>
<td></td>
</tr>
<tr>
<td></td>
<td>135</td>
<td>155</td>
</tr>
<tr>
<td>Financed by:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Borrowing:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loan from</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Zed Ltd.</td>
<td>Nil</td>
<td></td>
</tr>
</tbody>
</table>
Question 7:

X Co. Ltd. was registered with an authorised Capital of Rs. 10,00,000 divided into shares of Rs. 10 each, of which 40,000 shares had been issued and fully paid.

The following is the Trial Balance extracted on 31st March 2002:

<table>
<thead>
<tr>
<th>Description</th>
<th>Dr</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock (1.4.2004)</td>
<td>1,86,420</td>
<td></td>
</tr>
<tr>
<td>Returns</td>
<td>12,680</td>
<td>9,850</td>
</tr>
<tr>
<td>Sundry manufacturing expenses</td>
<td>19,240</td>
<td></td>
</tr>
<tr>
<td>18% Bank Loan (secured)</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Office salaries and Expenses</td>
<td>17,870</td>
<td></td>
</tr>
<tr>
<td>Directors’ Remuneration</td>
<td>26,250</td>
<td></td>
</tr>
<tr>
<td>Freehold premises</td>
<td>1,64,210</td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Debtors and Creditors</td>
<td>1,05,400</td>
<td>62,220</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>96,860</td>
<td></td>
</tr>
<tr>
<td>Profit and Loss Account on 1.4.2001</td>
<td></td>
<td>38,640</td>
</tr>
<tr>
<td>Share Capital</td>
<td></td>
<td>4,00,000</td>
</tr>
<tr>
<td>Purchases and sales</td>
<td>7,18,210</td>
<td>11,69,900</td>
</tr>
<tr>
<td>Manufacturing Wages</td>
<td>1,09,740</td>
<td></td>
</tr>
<tr>
<td>Carriage Inwards</td>
<td>4,910</td>
<td></td>
</tr>
<tr>
<td>Interest on bank loan</td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td>Auditors’ Fees</td>
<td>8,600</td>
<td></td>
</tr>
<tr>
<td>Preliminary Expenses</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>Plant and machinery</td>
<td>1,28,400</td>
<td></td>
</tr>
<tr>
<td>Loose Tools</td>
<td>12,500</td>
<td></td>
</tr>
<tr>
<td>Cash in hand</td>
<td>19,530</td>
<td></td>
</tr>
<tr>
<td>Advance payment of Tax</td>
<td>84,290</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>17,30,610</td>
<td>17,30,610</td>
</tr>
</tbody>
</table>
You are required to prepare Profit and Loss Account for the year ended 31st March 2002 and a Balance Sheet as at that date after taking into consideration the following adjustments:

(i) On 31st March 2002, outstanding manufacturing wages and outstanding office salaries stood at Rs. 1,890 and Rs. 1,200 respectively. On the same date stock was valued at Rs. 1,24,840 and loose tools at Rs. 10,000.

(ii) Provide for interest on bank loan for 6 months.

(iii) Depreciation on plant and machinery is to be provided @ 15% while on office furniture it is to be @ 10%.

(iv) Write-off one-third of balance of preliminary expenditure.

(v) Make a provision for income tax @ 50%.

(vi) The directors recommended dividend @ 15% for the year ending 31st March 2002 after a transfer of 5% of the profits to general reserve.

Answer:

In the books of X Co. Ltd.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Profit and Loss A/c for the year ended 31.3.2002</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>Opening Stock</td>
<td>1,86,420</td>
<td>By Sales</td>
</tr>
<tr>
<td></td>
<td></td>
<td>11,69,900</td>
</tr>
<tr>
<td>Purchase</td>
<td>7,18,210</td>
<td>Less:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Return</td>
</tr>
<tr>
<td>Less : Returns</td>
<td>9,850</td>
<td>7,08,360</td>
</tr>
<tr>
<td>Wages</td>
<td>1,09,740</td>
<td>By Closing Stock</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,24,840</td>
</tr>
<tr>
<td>Add : Outstanding wages</td>
<td>1,890</td>
<td>1,11,630</td>
</tr>
<tr>
<td>Sundry Mfg. expenses</td>
<td></td>
<td>19,240</td>
</tr>
<tr>
<td>Carriage inward</td>
<td></td>
<td>4,910</td>
</tr>
<tr>
<td>Gross Profit c/d</td>
<td>2,51,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>12,82,060</td>
<td></td>
</tr>
<tr>
<td>Int. on Bank loan</td>
<td>4,500</td>
<td>By Gross Profit b/d</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,51,500</td>
</tr>
<tr>
<td>Add : Outstanding</td>
<td>4,500</td>
<td>9,000</td>
</tr>
<tr>
<td>Office salaries &amp; expenses</td>
<td>17,870</td>
<td></td>
</tr>
<tr>
<td>Add : Outstanding</td>
<td>1,200</td>
<td>19,070</td>
</tr>
<tr>
<td>Auditors’ Fees</td>
<td></td>
<td>8,600</td>
</tr>
<tr>
<td>Directors’ remuneration</td>
<td></td>
<td>26,250</td>
</tr>
<tr>
<td>Provisions for depreciation</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Plant and Machinery</td>
<td>19,260</td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>Loose tools</td>
<td>2,500</td>
<td>22,260</td>
</tr>
<tr>
<td>Preliminary expenses</td>
<td></td>
<td>2,000</td>
</tr>
<tr>
<td>Income Tax</td>
<td></td>
<td>82,160</td>
</tr>
<tr>
<td>Net Profit c/d</td>
<td></td>
<td>82,160</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,51,500</td>
</tr>
</tbody>
</table>

STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION
## Company Accounts

Directors’ Fees (15% of 400000) 60000 By Balance b/d 38640  
General Reserve (5% of 82160) 4108 By Net profit b/d 82160  
Balance c/d 56692  
1,20,800 1,20,800

### Balance Sheet of X Co. Ltd as at 31.3.2002

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Share Capital</strong></td>
<td></td>
<td></td>
<td><strong>Fixed Assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Authorised, issued, subscribed and Paid up: Freehold Premises 1,64,210</td>
<td></td>
<td></td>
<td>Plant and Machinery 1,28,400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rs.10 each, fully paid up 4,00,000</td>
<td></td>
<td></td>
<td>Less: Provision for deprn. 19,260</td>
<td></td>
<td>1,09,140</td>
</tr>
<tr>
<td><strong>Reserves and Surplus</strong></td>
<td></td>
<td></td>
<td>Furniture 500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Reserve 4,108</td>
<td></td>
<td></td>
<td>Investments NIL</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit and Loss Account 56,692</td>
<td></td>
<td></td>
<td>Current Assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Secured loans</strong></td>
<td></td>
<td></td>
<td>Loose Tools 10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>18% Bank loan 50,000</td>
<td></td>
<td></td>
<td>Debtors 1,24,840</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Unsecured loans</strong></td>
<td></td>
<td></td>
<td>Outstanding for</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nil</td>
<td></td>
<td></td>
<td>More than 6 months ?</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Current Liabilities and Provisions</strong></td>
<td></td>
<td></td>
<td>Others ? 1,05,400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Creditors 62,220</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manufacturing Wages 1,890</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Office Salaries 1,200</td>
<td></td>
<td></td>
<td>Cash at Bank 96,860</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest on Bank loan 4,500</td>
<td></td>
<td></td>
<td>Cash in hand 19,530</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Provisions</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Provision for Taxation 82,160</td>
<td></td>
<td></td>
<td>Advance payment of 84,290</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proposed Dividend 60,000</td>
<td></td>
<td></td>
<td>Income tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Miscellaneous Expenditure</strong></td>
<td></td>
<td></td>
<td>Preliminary Exp.(Rs.6000 – 2000)</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,22,770</td>
<td>7,22,770</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION
Financial Accounting Fundamentals

Question 8:

The Balance Sheet of X & Y Ltd. as on 31st December, 1999 is given below:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>Fixed Assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>a) Authorised :</td>
<td>Land &amp; Building</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>50,000 Eq. Sh. @ Rs. 10 each</td>
<td>5,00,000</td>
<td>Current Assets, Loans &amp; Advances</td>
<td></td>
</tr>
<tr>
<td>b) Issued &amp; Paid up Capital :</td>
<td>Stock in Trade</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>40,000 Eq. Sh. of Rs. 10 each</td>
<td>Sundry Debtors</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Reserve &amp; Surplus</td>
<td>Cash and Bank Balance</td>
<td>2,40,000</td>
<td></td>
</tr>
<tr>
<td>Reserve</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit &amp; Loss A/c</td>
<td>1,30,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Secured Loan</td>
<td>7% Debenture</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Current Liabilities &amp; Provisions</td>
<td>Sundry Creditors</td>
<td>50,000</td>
<td></td>
</tr>
</tbody>
</table>

7,00,000 | 7,00,000

At the Annual General Meeting it is resolved:

(i) to pay a dividend of 15%.
(ii) to issue one bonus share for every five shares held.
(iii) to give existing shareholders the option to purchase one of Rs. 10 share at Rs. 14 for every five shares held prior to the Bonus distribution.

Pass the appropriate Journal Entries to record the above transactions and also draw up Balance Sheet. 10+10

Answer:

IN THE BOOKS OF X & Y LTD.
JOURNAL ENTRIES

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit &amp; Loss Appropriation A/c</td>
<td>Dr.</td>
<td>60,000</td>
<td></td>
</tr>
</tbody>
</table>
To Equity Dividend A/c | | 60,000 |
(Being a dividend @15% declared as per share holder’s resolution No...... Dated......)

Equity Dividend A/c | Dr. | 60,000 |
To Bank A/c | | 60,000 |
(Being equity dividend paid off)
Company Accounts

P/L A/c Dr. 70,000
Reserve A/c Dr. 10,000
To Bonus Dividend A/c 80,000
(Being bonus declared as per member’s Resolution Dated......)

Bonus Dividend A/c Dr. 80,000
To Equity Share Capital A/c 80,000
(Being Bonus utilized for the issue of 8,000 Equity Shares of Rs. 10 each distributed in the ratio of one share for every 5 share held)

Bank A/c Dr. 1,12,000
To Equity Share Capital A/c 80,000
To Share Premium A/c 32,000
(Being amount received on issue of 8,000 Equity Share @ Rs. 10 each at a premium Rs. 4 per share as per members Resolution Dated......)

Dr. X&Y Ltd. Cr.

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td></td>
<td>Fixed Assets</td>
<td></td>
</tr>
<tr>
<td>a. Authorised :</td>
<td></td>
<td>Land &amp; Building</td>
<td>2,00,000</td>
</tr>
<tr>
<td>50,000 Equity Shares @ Rs. 10 each</td>
<td>5,00,000</td>
<td>Current Assets</td>
<td>2,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stock in Trade</td>
<td>60,000</td>
</tr>
<tr>
<td>b. Issued &amp; Paid up Capital :</td>
<td></td>
<td>Sundry Debtors</td>
<td></td>
</tr>
<tr>
<td>48,000 Equity Share @ Rs. 10 each</td>
<td>4,80,000</td>
<td>Cash &amp; Bank Balance</td>
<td>1,80,000</td>
</tr>
<tr>
<td>Reserve &amp; Surplus :</td>
<td></td>
<td>(2,40,000 – 60,000)</td>
<td></td>
</tr>
<tr>
<td>Reserve (20,000 – 10,000)</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>P/L A/c (1,30,000 – 60,000 – 70,000)</td>
<td>Nil</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Secured Loan :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7% Debentures</td>
<td>1,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current Liabilities :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>6,40,000</td>
<td></td>
<td>6,40,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

Working Notes:

1. **Amount required for Dividend**
   (a) Cash Dividend = 15% of Subscribed Capital = Rs. 60,000
   (b) Bonus Dividend = $\frac{1}{5} \times 40,000 \times 10 = Rs. 80,000$

2. **Utilization of Profits/Reserve**
   (a) Cash Dividend should be declared out of P/L A/c
   (b) Bonus Dividend should be declared out of – :
      i. Rs. 70,000 from P/L A/c
      ii. Rs. 10,000 for Reserve A/c.

**Question 9:**

The Balance Sheet of Sayan Ltd. as on 31.12.98 is given below :

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>12% Pref. sh. of Rs.100 each, fully paid up</td>
<td>6,50,000</td>
<td>Sundry Assets</td>
<td>8,50,000</td>
</tr>
<tr>
<td>30,000 eq. sh. of Rs.5 each fully paid</td>
<td>1,50,000</td>
<td>Investment</td>
<td>3,75,000</td>
</tr>
<tr>
<td>General Reserve</td>
<td>1,60,000</td>
<td>Sundry Debtors</td>
<td>47,500</td>
</tr>
<tr>
<td>Profit &amp; Loss Account</td>
<td>3,00,000</td>
<td>Bills Receivable</td>
<td>60,000</td>
</tr>
<tr>
<td>10% Debenture</td>
<td>1,00,000</td>
<td>Cash at Bank</td>
<td>67,500</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>40,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>14,00,000</strong></td>
<td><strong>Sundry Debtors</strong></td>
<td><strong>14,00,000</strong></td>
</tr>
</tbody>
</table>

The preference shares are to be redeemed on 1st January 1999 at a premium of 7.5%. In order to facilitate redemption of the company has decided —

(i) To sell the investment for Rs. 3,60,000.
(ii) To finance part of the Company’s fund and to issue sufficient Equity shares at a premium of Re. 1 per share to raise the balance of funds required.
(iii) Minimum bank balance to be retained at Rs. 5,127.
(iv) The investments were sold, the equity shares were fully subscribed and all payments were made except to holders of 50 shares who could not be traced.

Give the necessary entries and the new Balance Sheet as on 1.1.1999.
**Company Accounts**

**Answer:**

In the Book of Sayan Ltd.

**Journal Entries**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>L.F.</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank A/c</td>
<td>Dr.</td>
<td>3,60,000</td>
<td></td>
</tr>
<tr>
<td>P/L A/c</td>
<td>Dr.</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>To Investment A/c</td>
<td></td>
<td></td>
<td>3,75,000</td>
</tr>
<tr>
<td>(Being investment sold and transferred the loss on sale to P/L A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>12% Pref. Share Capital A/c</td>
<td>Dr.</td>
<td>6,50,000</td>
<td></td>
</tr>
<tr>
<td>Premium on Redemption of Pref. Share</td>
<td>Dr.</td>
<td>48,750</td>
<td></td>
</tr>
<tr>
<td>To 12% Pref. Share Holder A/c</td>
<td></td>
<td></td>
<td>6,98,750</td>
</tr>
<tr>
<td>(Being amount payable on Redemption of 6,500, 12% Pref. Share with a premium of 7 &amp; 1/2 %)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank A/c</td>
<td>Dr.</td>
<td>2,71,002</td>
<td></td>
</tr>
<tr>
<td>To Equity Share Capital A/c</td>
<td></td>
<td></td>
<td>2,25,835</td>
</tr>
<tr>
<td>To Share Premium A/c</td>
<td></td>
<td></td>
<td>45,167</td>
</tr>
<tr>
<td>(Being 45,767 equity share of Rs. 5 each were issued at a premium of Rs. 1 per share as per Board resolution No........ Dated........)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>12% Pref. Shareholder A/c</td>
<td>Dr.</td>
<td>6,93,375</td>
<td></td>
</tr>
<tr>
<td>To Bank</td>
<td></td>
<td></td>
<td>6,93,375</td>
</tr>
<tr>
<td>(Being amount due to preference share holders paid off except to the holders of 50 shares)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Reserve A/c</td>
<td>Dr.</td>
<td>1,60,000</td>
<td></td>
</tr>
<tr>
<td>P/L A/c</td>
<td>Dr.</td>
<td>2,64,165</td>
<td></td>
</tr>
<tr>
<td>To Capital Redemption of Pref. Share</td>
<td></td>
<td></td>
<td>4,24,165</td>
</tr>
<tr>
<td>(Being necessary amounts transferred out of profit and Reserve for Capital Redemption)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share Premium A/c</td>
<td>Dr.</td>
<td>45,167</td>
<td></td>
</tr>
<tr>
<td>P/L A/c</td>
<td>Dr.</td>
<td>3,583</td>
<td></td>
</tr>
<tr>
<td>To Premium on Redemption of Pref. Share</td>
<td></td>
<td></td>
<td>48,750</td>
</tr>
<tr>
<td>(Being premium payable on redemption were adjusted)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
# Balance Sheet as on 1.1.99

**Liabilities** | **Rs.** | **Assets** | **Rs.**
---|---|---|---
Share Capital | | Sundry Assets | 8,50,000
Issued and Subscribed | | 75,167 Equity Share of Rs. each | 3,75,835
RESERVE AND SURPLUS | | Bills Receivable | 60,000
P/L A/c | | Cash at Bank | 5,127
(3,00,000 – 2,64,165 – 15,000 – 3,583) | | | |
Capital Redemption Reserve | | | 4,24,165
Secured Loan | | 10% Debenture | 1,00,000
Current Liabilities | | Sundry Creditors | 40,000
| | 12% Red. Pref. Share Holder | 5,375
| | | 9,62,627 |

## Working Notes:

1) Cash to be raised through issue of Equity Share.

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Bank Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Particulars</strong></td>
<td><strong>Rs.</strong></td>
<td><strong>Particulars</strong></td>
</tr>
<tr>
<td>To Balance b/d</td>
<td>67,500</td>
<td>By Preference Shareholder A/c</td>
</tr>
<tr>
<td>To Investment</td>
<td>3,60,000</td>
<td>(6,98,750 – 50/6,500 × 6,98,750)</td>
</tr>
<tr>
<td>To Eq. Sh. Holder A/c (Balancing Figure)</td>
<td>2,71,002</td>
<td>By Balance c/f</td>
</tr>
<tr>
<td></td>
<td>6,98,502</td>
<td></td>
</tr>
</tbody>
</table>

2) Equity Shares of Rs.5 each to be issued to a Premium of Re.1 per share. So No. of Equity Shares to be issued = Rs.2,71,002/6 = 45,167

3) Arrangement of funds:

<table>
<thead>
<tr>
<th>Payable on Redemption</th>
<th>New Issue</th>
<th>Reserve &amp; Surplus</th>
</tr>
</thead>
<tbody>
<tr>
<td>Preference Share Capital</td>
<td></td>
<td>Amount Required</td>
</tr>
<tr>
<td>Capital = Rs. 6,50,000</td>
<td>Equity Share Capital</td>
<td>45,167 × 5 = 2,25,835</td>
</tr>
<tr>
<td>Premium on Redemption</td>
<td></td>
<td>6,50,000 – 2,25,835 = Rs.4,24,165</td>
</tr>
<tr>
<td>@7 &amp; 1/2% = Rs.48,750</td>
<td></td>
<td>1,60,000</td>
</tr>
<tr>
<td></td>
<td>Share Premium</td>
<td>General Reserve</td>
</tr>
<tr>
<td></td>
<td>47,167 × 1 = 45,167</td>
<td>P/L A/c</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,64,165</td>
</tr>
<tr>
<td></td>
<td></td>
<td>4,24,165</td>
</tr>
<tr>
<td></td>
<td></td>
<td>P/L A/c = Rs.3,583</td>
</tr>
</tbody>
</table>
Company Accounts

Question 10:

Ram and Shyam are partners of Ram Shyam & Co. sharing profits and losses in the ratio of 3:2. Sita and Gita are partners of Sita Gita & Co. sharing profits and losses in the ratio of 5:3.

The balance sheets of the two firms as on 31st May, 2001 was as under:

<table>
<thead>
<tr>
<th></th>
<th>Ram Shyam &amp; Co.</th>
<th>Sita Gita &amp; Co.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Capitals</strong></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Ram</td>
<td>5,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Shyam</td>
<td>3,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Sita</td>
<td>—</td>
<td>6,00,000</td>
</tr>
<tr>
<td>Gita</td>
<td>—</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Loan from Sita Gita &amp; Co.</td>
<td>2,00,000</td>
<td>—</td>
</tr>
<tr>
<td><strong>Fixed assets</strong></td>
<td>Rs. 10,00,000</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Cost</td>
<td>4,00,000</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Less: Depreciation to date</td>
<td>3,00,000</td>
<td>4,00,000</td>
</tr>
<tr>
<td></td>
<td>1,00,000</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Loan to Ram Shyam &amp; Co.</td>
<td>—</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Current assets</td>
<td>21,00,000</td>
<td>7,50,000</td>
</tr>
<tr>
<td>Less: Current liabilities</td>
<td>12,00,000</td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td>9,00,000</td>
<td>7,00,000</td>
</tr>
<tr>
<td><strong>Rs.10,00,000</strong></td>
<td>10,00,000</td>
<td></td>
</tr>
</tbody>
</table>

Kuber Ltd. was incorporated on 1st April, 2001 with an authorised capital of Rs. 1 crore. The subscribers to the memorandum and articles of association took up 3,00,000 equity shares of Rs. 10 each and paid for same on formation of the company. Formation expenses amounted to Rs. 1,00,000 and were paid off.

Kuber Ltd. decided to take over the net assets of Ram Shyam & Co. at a valuation of Rs. 12,50,000 and the net assets of Sita Gita & Co. at a valuation of Rs. 14,00,000. Equity shares of Rs. 10 each were allotted at par in discharge of the consideration on 1st June, 2001.

The directors of Kuber Ltd. decided to revalue only the fixed assets taken over at Rs. 2,50,000 in respect of Ram Shyam & Co. and Rs. 3,00,000 in respect of Sita Gita & Co.

The directors of Kuber Ltd. ask you to show the ledger accounts in respect of the above transactions and extract the trial balance.
**Financial Accounting Fundamentals**

**Answer:**

**In the books of Kuber Ltd.**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Bank A/c</strong></td>
<td></td>
<td></td>
<td></td>
<td><strong>Cr.</strong></td>
<td></td>
</tr>
<tr>
<td>1.4.01</td>
<td>To Equity share capital</td>
<td>30,00,000</td>
<td>1.4.01</td>
<td>By Formation exp</td>
<td>1,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>30.6.01</td>
<td>By Balance</td>
<td>29,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>30,00,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Equity Share Capital A/c</strong></td>
<td></td>
<td></td>
<td></td>
<td><strong>Cr.</strong></td>
<td></td>
</tr>
<tr>
<td>Date</td>
<td>Particulars</td>
<td>Amount (Rs.)</td>
<td>1.4.01</td>
<td>By Bank</td>
<td>30,00,000</td>
</tr>
<tr>
<td></td>
<td>30.6.01</td>
<td>To Balance</td>
<td>56,50,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Ram Shyam A/c</strong></td>
<td></td>
<td></td>
<td></td>
<td><strong>Cr.</strong></td>
<td></td>
</tr>
<tr>
<td>1.6.01</td>
<td>To Current liabilities</td>
<td>12,00,000</td>
<td>1.6.01</td>
<td>By Fixed assets</td>
<td>2,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2,00,000</td>
<td>By Current assets</td>
<td>21,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>To Business purchase A/c</td>
<td>9,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>23,50,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sita Gita &amp; Co. A/c</strong></td>
<td></td>
<td></td>
<td></td>
<td><strong>Cr.</strong></td>
<td></td>
</tr>
<tr>
<td></td>
<td>50,000</td>
<td>1.6.01</td>
<td>By Fixed assets</td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>12,00,000</td>
<td>To Business purchase</td>
<td>12,50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2,00,000</td>
<td>By Loan</td>
<td>7,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>12,00,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Business Purchase A/c</strong></td>
<td></td>
<td></td>
<td></td>
<td><strong>Cr.</strong></td>
<td></td>
</tr>
<tr>
<td>1.6.01</td>
<td>To Equity Capital A/c</td>
<td>26,50,000</td>
<td>1.6.01</td>
<td>By Ram Shyam &amp; Co.</td>
<td>9,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>12,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>5,00,000</td>
</tr>
</tbody>
</table>

**STUDY MATERIAL PREPARED BY ICWAI FOR J.A.O (CIVIL) EXAMINATION**
## Company Accounts

### Fixed Assets A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.6.01</td>
<td>To Ram Shyam &amp; Co.</td>
<td>2,50,000</td>
<td>1.6.01</td>
<td>By Balance</td>
<td>5,50,000</td>
</tr>
<tr>
<td></td>
<td>To Sita Gita &amp; Co.</td>
<td>3,00,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>5,50,000</td>
<td></td>
<td></td>
<td>5,50,000</td>
</tr>
</tbody>
</table>

### Current Assets A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.6.01</td>
<td>To Ram Shyam &amp; Co.</td>
<td>21,00,000</td>
<td>30.6.01</td>
<td>By Balance</td>
<td>28,50,000</td>
</tr>
<tr>
<td></td>
<td>To Sita Gita &amp; Co.</td>
<td>7,50,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>28,50,000</td>
<td></td>
<td></td>
<td>28,50,000</td>
</tr>
</tbody>
</table>

### Current Liabilities A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>30.6.01</td>
<td>To Balance</td>
<td>12,50,000</td>
<td>1.6.01</td>
<td>By Ram Shyam &amp; Co.</td>
<td>12,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Sita Gita &amp; Co.</td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>12,50,000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Goodwill A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.6.01</td>
<td>To Business Purchase</td>
<td>5,00,000</td>
<td>30.6.01</td>
<td>By Balance</td>
<td>5,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>5,00,000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Formation Exps. A/c

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
<th>Date</th>
<th>Particulars</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.6.01</td>
<td>To Bank</td>
<td>1,00,000</td>
<td>30.6.01</td>
<td>By Balance</td>
<td>1,00,000</td>
</tr>
</tbody>
</table>

### Trial Balance for the period 1.4.01 to 30.6.01

<table>
<thead>
<tr>
<th></th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank</td>
<td>29,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Equity Share Capital</td>
<td>—</td>
<td>56,50,000</td>
</tr>
<tr>
<td>Formation Expenses</td>
<td>1,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Fixed Assets</td>
<td>5,50,000</td>
<td>—</td>
</tr>
<tr>
<td>Current Assets</td>
<td>28,50,000</td>
<td>—</td>
</tr>
<tr>
<td>Goodwill</td>
<td>5,00,000</td>
<td>—</td>
</tr>
<tr>
<td>Current Liabilities</td>
<td>12,50,000</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>69,00,000</td>
<td>69,00,000</td>
</tr>
</tbody>
</table>
Financial Accounting Fundamentals

4.11 SELF-EXAMINATION QUESTIONS

1. Distinguish between a company and a partnership firm.

2. What are the guidelines issued by SEBI regarding Issue of Bonus and Right Shares?

3. Discuss provisions of Companies Act regarding premium of redemption of preference shares.

4. A Public Co. Ltd. invited applications for the issue of 2,00,000 equity shares of Rs. 10 each at a premium of Re. 1 per share. The shares were payable as under:

   - Rs. 2 with application;
   - Rs. 4 on allotment (including premium);
   - Rs. 3 on 1st call; and
   - Rs. 2 on final call.

   The applications were received for 2,60,000 shares. The company decided to reject 40,000 share applications and allotted the rest proportionately. All the calls were made and an applicant holding 6,000 shares could not pay the dues on final. Consequently these shares were forfeited and subsequently re-issued @ Rs. 9 per share.

   Pass journal entries relating to the issue of the shares and also show the Bank Account in the books of the company.

5. Fairgrowth Ltd. had 6% Rs. 1,00,000 debentures. It had not created any Sinking fund. Debenture interest date is 31st December. On 1.4.95, it purchased Rs. 10,000 own debentures for immediate cancellation @96. On 1.12.95 it purchased Rs. 6,000 such debentures @94 exinterest which were also for cancellation.

   Show the ledger accounts in the books of Fairgrowth Ltd. Ignore Income Tax.
Company Accounts

6. Growquick Ltd. was incorporated on 1st May 1994 and was entitled to commence business on 1st June 1994. It had acquired a running business as from 1st January 1994. The profit & loss account for 1994 was as under:

<table>
<thead>
<tr>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Salaries</td>
<td>40,000</td>
</tr>
<tr>
<td>To General expenses</td>
<td>10,000</td>
</tr>
<tr>
<td>To Carriage</td>
<td>15,000</td>
</tr>
<tr>
<td>To Advertising</td>
<td>20,000</td>
</tr>
<tr>
<td>To Debenture interest</td>
<td>6,000</td>
</tr>
<tr>
<td>To Director's fees</td>
<td>5,000</td>
</tr>
<tr>
<td>To Audit fees</td>
<td>4,000</td>
</tr>
<tr>
<td>To Depreciation</td>
<td>20,000</td>
</tr>
<tr>
<td>To Interest to vendor (up to 30th June '94)</td>
<td>10,000</td>
</tr>
<tr>
<td>To Net profit</td>
<td>70,000</td>
</tr>
<tr>
<td></td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

Ascertain the profit prior to incorporation. Sales up to 1st May 1994 were Rs. 2,00,000 and after 1st May 1994, Rs. 8,00,000.

7. JALAJOGA Ltd. was incorporated as private limited company on 31.8.1995 to take over a business as a going concern as from 1.1.1995. Vendors would get 75% of the profits earned prior to 31.8.95. Trading and profit and Loss Accounts for the year ended 31.12.95 were as under:

(Figures in Rs.)

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Materials consumed</td>
<td>1,80,000</td>
</tr>
<tr>
<td>&quot; Manufacturing wages</td>
<td>48,000</td>
</tr>
<tr>
<td>&quot; Manufacturing expenses</td>
<td>12,200</td>
</tr>
<tr>
<td>&quot; Carriage inwards</td>
<td>7,000</td>
</tr>
<tr>
<td>&quot; Gross profit C/d</td>
<td>52,800</td>
</tr>
<tr>
<td></td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

| To Salaries & establishment | 15,000 |
| Office expenses             | 6,000  |
| " Director’s fees           | 1,800  |
| " Bad debts                 | 2,300  |
| " Debenture interest        | 1,150  |
| " Commission & discount     | 8,000  |
| " Carriage outwards         | 1,600  |
| " Depreciation              | 10,200 |
| " Net profit for the year   | 6,750  |
|                   | 52,800   |

2,00,000 2,00,000
Sales for March & April are 1.5 times the average monthly sales. Sales for Sept. & Oct. are twice the average monthly sales. Bad debts of Rs. 1,100 were written off in June. Prepare a statement showing pre-incorporation profits. Also indicate the disposal of such profits.

8. The following balances and particulars are extracted from the books of Pant Co. Pvt. Ltd. for the year ended 31st December 1994:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital : Authorised, issued &amp; fully paid up (50,000 equity shares)</td>
<td>5,00,000</td>
</tr>
<tr>
<td>General Reserve (as at 1.1.94)</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Furniture (including addition of Rs. 5,000)</td>
<td>35,000</td>
</tr>
<tr>
<td>Office equipments (as at 1.1.94)</td>
<td>22,000</td>
</tr>
<tr>
<td>Motor car (purchased on 30.12.94)</td>
<td>30,000</td>
</tr>
<tr>
<td>Sundry debtors (unsecured)</td>
<td>8,50,000</td>
</tr>
<tr>
<td>Advance to staff</td>
<td>10,000</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>2,000</td>
</tr>
<tr>
<td>Balance with Bank of India (including fixed deposits of Rs. 1,00,000)</td>
<td>1,40,000</td>
</tr>
<tr>
<td>Loans from Directors</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Liability for expenses and goods</td>
<td>2,67,000</td>
</tr>
<tr>
<td>Provision for tax (as on 1.1.94)</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Profit &amp; Loss A/c (as on 1/1/94)</td>
<td>3,000</td>
</tr>
<tr>
<td>Closing stock (20,000 metres)</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Advance Tax paid</td>
<td>1,90,000</td>
</tr>
<tr>
<td>Depreciation written off up to 31.12.94 (Furniture : Rs. 5,000, Office equipment : Rs. 2,000)</td>
<td>7,000</td>
</tr>
<tr>
<td>Opening Stock (10,000 metres)</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Legal charges including Rs. 3,000 paid to auditors for tax representation</td>
<td>10,000</td>
</tr>
<tr>
<td>Salaries to staff</td>
<td>50,000</td>
</tr>
<tr>
<td>Miscellaneous expenses (including Rs. 4,000 for tour within India, Rs. 36,000 for foreign tour)</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Purchase of cloth (2.10 lakh metres)</td>
<td>30,39,000</td>
</tr>
<tr>
<td>Audit fees</td>
<td>4,000</td>
</tr>
<tr>
<td>Interest on fixed deposit with bank</td>
<td>5,000</td>
</tr>
<tr>
<td>Sales (2 lakh metres) (including export sales of Rs. 10 lakhs)</td>
<td>35,00,000</td>
</tr>
</tbody>
</table>
Company Accounts

Further information:

(a) Rate of depreciation – Furniture 10%, Office equipment 15% and Motor car 20%.

(b) M.D. is entitled to commission @ 10% of net profits after providing such commission subject to maximum of Rs. 36,000 p.a.

(c) Debtors include Rs. 1,50,000 outstanding for more than 6 months. Out of this Rs. 20,000 is considered doubtful for which provision is to be made in the accounts.

(d) Tax liability for 1994 is estimated at Rs. 2,00,000 for which provision is to be made.

(e) Transfer to General Reserve Rs. 50,000 out of net profits and proposed dividend is @ 6% on equity shares.

Prepare the Balance Sheet, and Profit & Loss Account for the year ended 31st December 1994, in accordance with the requirements of Companies Act, 1956.

[Ans. : Net profit Rs. 1,00,000 ; Balance Sheet total Rs. 13,62,000]

9. Mr. Sharma, proprietor of a large business of textiles and readymade goods maintained a provision for doubtful debts @ 10%, a provision for discount @ 4% on debtors and a reserve for discount @ 4%, on creditors which on 1st December, 1999 amounted to Rs. 4,800, Rs. 1,600 and Rs. 1,280 respectively. His balances on 30th November 2000, 2001 and 2002 were as follows:

<table>
<thead>
<tr>
<th></th>
<th>30th November 2000 (Rs.)</th>
<th>30th November 2001 (Rs.)</th>
<th>30th November 2002 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bad debts written off</td>
<td>4,760</td>
<td>960</td>
<td>3,840</td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>32,000</td>
<td>9,600</td>
<td>48,000</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>960</td>
<td>320</td>
<td>1,280</td>
</tr>
<tr>
<td>Sundry creditors</td>
<td>48,000</td>
<td>32,000</td>
<td>64,000</td>
</tr>
<tr>
<td>Discount received</td>
<td>960</td>
<td>160</td>
<td>1,120</td>
</tr>
</tbody>
</table>

You are asked to prepare the necessary accounts in the ledger; also show how the items would appear in the final accounts of each of the three years.
10. The Balance Sheet of M/s RAMAN Ltd. as at 31st December, 2001, inter alia includes the following :

\[
\begin{align*}
\text{Rs.} & \\
50,000 & \text{8% preference shares of Rs. 100 each, Rs. 70 paid up} & 35,00,000 \\
1,00,000 & \text{equity shares of Rs. 100 each, fully paid up} & 1,00,00,000 \\
\text{Securities premium} & & 5,00,000 \\
\text{Capital redemption reserve} & & 25,00,000 \\
\text{General reserve} & & 45,00,000
\end{align*}
\]

The Board decided to redeem the entire preference share capital at a premium of 5% on 31.03.2002. In order to finance the redemption, the Company makes a right issue of 50,000 equity shares of Rs. 100 each at Rs. 110 per share, Rs. 20 being payable on application, Rs. 35 (including premium) on allotment and the balance on January 1, 2003. The issue was fully subscribed and allotment made on March 1, 2002. The monies due on allotment were received by March 30, 2002.

The preference shares were redeemed after fulfilling the necessary conditions of section 80 of the Companies Act, 1956. The Company decided to make the minimum utilisation of general reserve.

Show the journal entries in the books of the Company and prepare the relevant extracts from the Balance Sheet as on March 31, 2002 with the corresponding figures as on 31st Dec., 2001.
5.1 ACCOUNTING PRINCIPLES, CONCEPTS AND CONVENTIONS

Introduction and Definition:

The business house employs the scarce economic resources – material, labour, building, equipment and different types of services, which have to be financed. The work is done through joint stock companies where groups of individuals work together for some common goals. The groups of people need information about the amounts and usage of resources, the means of financing them and the results of operating activities and may be broadly termed internal users. External users (such as lenders, creditors, shareholders, employee, public, etc) need similar information for the performance evaluation of the company. A systematic record of the events of the business leading to a presentation of a complete financial picture is known as accounting. Information requirements of external users are served through financial statements. These are balance sheet and profit and loss account for the period along with schedules and notes on account. Non-profit organisations need to know the details of income and expenditure. Therefore, accounting is similar in profit as well as non-profit organisations.
Accounting is aptly termed as the language of business. The American Institute of Certified Public Accountants have defined "Accounting is the art of recording, classifying and summarising in significant manner and in terms of money transactions and events which are, in part, at least of a financial character and interpreting the results thereof. " Affairs of a business unit are communicated to outsiders, owners, lenders and managers through accounting information, which has to be suitably recorded, classified, summarised and presented. In order to convey a uniform meaning to all people as far as possible and to make it meaningful, it is necessary that it should be based on certain uniform scientifically laid down standards. These standards are termed as accounting principles. These accounting principles/guidelines are to establish standards for sound accounting practices and procedures in reporting the financial status and periodic performance of a business. These principles are classified in two categories:

1. Accounting concepts; and
2. Accounting convention.

The best way to understand the underlying principles, concepts and conventions is to acquire genuine insight into the general body of accounting theory comprising the generally accepted accounting principles/standards whether they are as per law or on the strength of standard guidelines issued by authoritative accounting bodies like the ICWAI, ICAI etc. or on the basis of local custom. Students will find it profitable to study those principles/concepts, which are still at research level. For this purpose, the students are advised to be abreast of the latest developments in the fields of accounting theory, to the extent possible, by going through at least some of the available literature on the subject like the Management Accountant issued by the ICWAI and the Chartered Accountant issued by the ICAI. As regards accounting theory, the students are advised to go through at least some above average textbooks, such as Accounting Theory by E. S. Hendriksen. The origin of double entry during 15th century can be taken as the starting point for a study of the development of the accounting theory. The basic accounting principles developed during the 19th century and early 20th century. According to Prof Hendriksen "The main influence on accounting theory during the period 1800 to 1930 can be classified as follows:

1. The textbook presentation of bookkeeping and the development of newer methods of teaching accounting;
2. The Industrial revolution with its influence on cost accounting and accounting for depreciation;
3. Government regulations of business;
4. The taxation of business;
5. The development of the corporation and growth of industrial and financial giants through managers; and
6. The influence of economic theory.

It is beyond the scope of these Study Notes to deal with accounting theory in detail. However, a very brief outline of the subject is given below only to kindle interest among the students to take up a detailed study of the subject as suggested above.
Accounting Principles and Accounting Standards

Theoretically, the most important goal of accounting theory should be to provide a coherent set of logical principles that form the general frame of reference for the evaluation and development of sound accounting practices. According to Hendriksen probably the most relevant definition of accounting theory is that it represents the coherent set of hypothetical, conceptual and pragmatic principles. Hence Accounting Theory, should provide the following:

a) A general frame of reference by which accounting practices can be evaluated.

b) Guidance for the development of new practices and procedures.

However, a single general theory of accounting though highly desirable, yet accounting as a logical and empirical (social) science is still in too primitive a stage for such a development. The best that can be accomplished at this stage is a set of theories (models) and sub-theories that may be complementary or competing. By definition, each theory consists of a set of statements or propositions connected by rules of logic or inferential reasoning. In any event, we should always bear in mind that all theories are subject to modification or abandonment with the development of new information or new theories that permit better predictions. To avoid confusion now and later on, it is necessary to classify accounting theories. There are several ways in which it can be done. Here again we are handicapped by the limited scope to discuss this point elaborately. So we give below a short classification of accounting theories according to predictive levels, because predictability is one of the main features of any theory, including accounting theory. The three main levels of accounting theory are as follows:

1. Theories that attempt to explain accounting practices and predict how accountants would react to certain situations or how they would report specific events. These theories relate to the structure of the data collection process and financial reporting. Which is why they are called syntactical theories (syntax in literature means the correct Arrangement of words in sentences). Examples of this kind of theories are:

   a) Valuation of Fixed Assets of a going concern at historical cost less depreciation.

   b) Valuation of current assets at cost or market price whichever is lower, barring a few exceptions.

   c) Whether raw materials issued to production should be valued at cost or market price or at standard cost. Again, within the cost price bases whether it should be FIFO or LIFO or Weighted Average Cost.

   d) While valuing Goodwill, the assets of the Vendor company should preferably be valued at replacement cost.

Theories concentrate on the relationship between a phenomenon (object or event) and the term or symbol representing it. These can be referred to as interpretational theories. This is the reason why these theories are called semantical theory (in literature semantics mean study of meanings). Particular care must be taken to assure that the interpretations of concepts by the accountants are the same interpretations made by the users of accounting reports. For example, the word "Profit" means something else in economics. This confusion is mainly due to the fact that particularly by borrowing from economics, accountants have long attempted to find a correspondence between accounting (money) measurements and
economic or physical concepts or real-world phenomena. This search has been necessary in order to give some meaning to accounting theory and practice. Without interpretational support no accounting structure can be meaningful and useful. Examples are:

Method of assets valuation, methods of profit estimation, etc. These are all artificial concepts peculiar to accounting. Hence, for the users to financial reports/information, they should be interpreted in a specific manner. But, on many occasions real difficulty will arise. For example, the word "value" has no specific interpretations, as we see later on. The word cash/bank balances does not need any interpretation. But terms like deferred revenue expenditure, intangible assets, fictitious assets etc. need clear accounting interpretation in a standard manner, to the extent now possible.

Behavioural (Pragmatic) Theories : These theories emphasise the behavioural or decision-oriented effects of accounting information/reports/statements. The most commonly used dictionary meaning of the word "pragmatic" is "practical". This kind of accounting theories is called "practical" because to whom the periodic financial statement (Balance Sheet and the Profit and Loss Account) are sent, use them for the most practical use, that is, taking decisions on the basis of such financial statements. In this category the focus is on the relevance of information being communicated to decision-makers and the "behaviour" of different individuals or groups as a result of the presentation of accounting information. The literal meaning of the word "behaviour" is the manner in which an individual (or a group) reacts. In the present context, behaviour would mean how an individual (or a group) reacts on receiving and studying communicated accounting information for example individual; reaction on seeing the bottom line (net profit) as compared to the last year. Likewise, reaction on examining the financial condition is revealed by the Balance Sheet. Finally, helping the user of the financial statements to decide whether he would like to hold on the shares or dispose them of. Of course, before taking a final decision, the user may need much more and complex information like Ratio Analysis, Fundamental Analysis. Fundamental Analysis, studies with Technical Analysis (methods employed to study and forecast trends in stock exchange operations).

This category of accounting theories is still in its infancy. The issue is rendered more complicated because our knowledge of human psychology, which differs from person to person, is imprecise, incomplete, controversial and highly subjective in many cases. In spite of all these practical handicaps researchers are busy acquiring more dependable insight into the human psychology, both individual and group. The result is the emergence of new concepts like Human Information Processing, Agency Theory, etc. The basic contention of Human Information Processing is that individuals have been found to be limited in their ability to process information in a complex setting. To overcome the complexity, they will mostly attempt to simplify the information and reduce the uncertainty, as they perceive it.

Basic concepts:

Accounting principles are built on a foundation of a few basic concepts. These concepts are so basic that most accountants do not consciously think of them; they are regarded as being self-evident. Non-accountants will not find these concepts to be self-evident. Some accounting theorists argue that certain of the present concepts are wrong and should be
changed. But in order to understand accounting, as it now exists, one must understand what the underlying concepts currently are. The different aspects are:

1. Business Entity Concept
2. Money Measurement Concept
3. Cost Concept
4. Going Concern Concept
5. Dual-aspect Concept
6. Realisation Concept
7. Accrual Concept
8. Accounting Period Concept

1. BUSINESS ENTITY CONCEPT:

The business is treated as a distinct entity from the individuals who own it and accordingly accountants record transactions. For example, if the owner of a shop withdraws Rs. 10,000 for personal use, from the business entity point of view, the entity has less cash though it belongs to the owners. Therefore, this amount is shown as a reduction in owner’s capital, which in view of business entity concept appears as a liability in the balance sheet of the business. Without such a distinction the affairs of the shop will be mixed with the personal affairs of the owner. For a company the distinction is easier as legally the company is a distinct entity from the persons who own it. Therefore, an entity is a business organisation or activity in relation to which accounting reports are compiled. It may include universities, voluntary organisations, government and non-business units. What we have stated above is just a superficial discussion of the concept, though the central point has been brought out clearly. But we have to go at least a little deeper because out of this basic concept, a large number of very important sub-concepts emerge, dealing with ownership equities, without which we cannot understand properly many of the modern accounting practices. Constrained by the limited scope of Study Notes to deal exhaustively with a particular concept, the discussion that follows in this regard will touch upon the basic outlines of the sub concepts related to the Business Entity Concept.

But before we take up the specific sub-concepts, let us turn to the factors, which compelled the emergence of the basic concept of Business Entity.

There are two ways in which we may look at it. Namely, the pure accounting angle and the legal viewpoint. Let us consider the pure accounting viewpoint first.

Pure Accounting Viewpoint: We will start from the fundamental accounting equation, that is:

\[
\text{Debit} = \text{Credit} \quad (i)
\]
\[
\text{And, Assets} = \text{Liabilities} \quad (ii)
\]
\[
\text{And, Assets} = \text{Internal Liabilities} + \text{External Liabilities} \quad (iii)
\]
\[
\text{And finally, Assets} = \text{Capital} + \text{Liabilities}; \text{ or } A = C + L \quad (iv)
\]
Advanced Financial Accounting

The above equation/s epitomises the logic of the double-entry system of bookkeeping. There was interna
tly no difficulty in recording all financial transactions, except the entry for introduction of capital by the owner. The matter was further compounded by the fact that an owner may be owning a number of business enterprises besides his personal financial affairs. Practical accounting is organisation-specific, meaning that accounting entries are passed with reference to a particular business (or non-business) organisation (enterprise). From the non-accounting point of view when an owner introduces capital into a particular business, it seems "as if" the owner is giving money to himself. Double-entry system, cannot record such a nondual transaction. It can record a financial transaction when one distinct person gives money to another distinct person. Accountants cannot afford to ignore to record introduction of capital by the owner, since in reality the business is receiving money from "somebody". Hence they were compelled to invent another person who was receiving money from the owner as capital. It was logical to assume the business itself, as the much needed "invented" person. There is no difficulty in debiting the Cash/Bank, which is coming in. But to credit Whom? After the business came to be considered as separate from the owner, his name was made secondary to the new status "Capital". This is the accounting angle. Now let us turn to the legal Angle.

Legal Angle:

When the Industrial Revolution became a grand reality nearly 250 years ago, formation of company type of business Organisation became an inevitable event, to raise huge capitals, which is possible only with a large number of co-owners, need to finance production on hitherto unknown scales of production. Prior to the centre-stage appearance of the companies, partnership was the predominant form of doing large-scale (by the then the standard) business form. But partnership was risky affair for the partners with unlimited liability.

It was risky, for the unsecured creditors due to dissolution of partnership on any change in the ownership, particularly due to the death of a partner/s. Company type of business would have failed to win the confidence of a large number of investors of large amounts as capital as well as the unsecured creditors now with bigger stakes due to much larger scales of operations, if those two characteristic features of partnership had persisted. Hence the emergence of the concepts of limited liability and perpetual succession. But these two concepts could not be put into practice until the business was endowed with an entity, that is, existence independently of and separate from its owners. This is the main point about legal recognition of the separateness of business as an entity from that of its owners. But this was no surprise to the accounting community since they had already realised the significance of (his concept under the inevitable compulsion of the rigour of double entry system of book-keeping for recording capital contributed by the owner/s.

Now let us turn to the important intimate relationship between the Entity Concept and the Equity Concept.
**Entity and Equities:**

An entity means an Organisation, whether a company or not, big or small or profit oriented or not, having a separate existence (entity) from the owner. Equity means any right, claim or interest in an asset (in accounting, as it could relate to things other than assets in the other departments of life) recognised as valid under any law based on impartial justice.

**Note:** The separate existence may be recognised under law as well as in accounting only.

In order to have close touch with real-world affairs, we shall henceforth discuss the present issue with regard to a big company unless otherwise stated specifically. From the description of what constitutes the concept of "equity". As stated above, there is no bar to admitting that all the items on the liabilities side of a Balance Sheet can be described as items of equity, which can be broadly classified as follows:

a) Shareholders’ equity comprising different kinds of Shares plus all kinds of Reserves plus all kinds of Retained Earnings less Expenditure/s to the extent not written off, such as Preliminary Expenses, Deferred Revenue Expenditure, etc.

**Note:** In India at present there can be only, two kinds of shares, namely Equity and Preference Shares. As regards share Capital, Preference Shareholders’ claim is restricted to the paid up amount only.

b) Long-term creditors/lenders

c) Current Liabilities.

**Note:** The claim of any category of creditors, whether long-term or current is restricted to the amount of credit legally admitted at the point of time when it is materialised.

Equities are treated differently for a going-concern from a company, which is going, or gone into liquidation. A going-concern is one, which has not contemplated going into liquidation even in the remotest future at the time of preparing its latest financial statements, consisting primarily of the Balance Sheet and the P/L A/c. The main point of difference is that the residue of money received from sale of the business less all liabilities are due for return to the Equity Shareholders, while liabilities and Preference shareholders are paid off only, the legally prior-committed amount. In liquidation, the Equity Shareholders may get less than their book-value of claims. The equities can be looked at from different angles, depending on how the equity holders, mainly the shareholders, look at the business entity’s assets. At present, however, the ways in which the employees, the community as well as the rest of the society at large, meaning the country as a whole, look at the Organisation. This has given rise to the modern concept of Social Accounting; this is, however, outside the scope of the present Study Notes. The ways in which the different kinds of equity-holders view their claims on the assets of the entity and their relative strengths among themselves determine a lot of accounting and social issues. In accounting, these factors are responsible for the format and the other aspects of what is known as the "Design of Accounts", Disclosure and Transparency of Accounts, etc. But an accountant today will have to consider every aspect of traditional accounting from the formal angle of the "structure" of the Fundamental Accounting Equation, which has already been referred to. From such an angle, certain theories of equity have been evolved. We are now going to discuss some major theories as briefly as possible.
Advanced Financial Accounting

Proprietary Theory:
Here the owner/s is the focal point of all the activities of the entity. He is concerned with his claim on the entity’s assets. As a result, the fundamental accounting equation is changed from Assets = Liabilities + Capital [Capital because it includes share capital + all Reserves + all Retained Earnings – Fictitious Assets] to Capital = Assets – Liabilities. As a result of rearranging the fundamental equation in this fashion, the emphasis on Capital is heightened.

Entity Theory:
Here equal importance is given to all equity holders, whether owner or lender or creditor. As a result, the fundamental equation, Assets = Liabilities + Capital (Capital because it includes share capital + all Reserves + all Retained Earnings – Fictitious Assets) to Capital = Assets – Liabilities is either retained as it is or to focus attention on the equity holders as a whole; it may be written as: Liabilities + Capital = Assets.

Enterprise Theory:
Here the shift is from Entity to Enterprise because it is intended to include among equity holders not only those who have directly provided funds to the enterprise, but also employees, community and the state who have provided with intangible resources like human resource (by employees) co-operation (by the community) and infrastructure (by the State). Hence, the fundamental equation is viewed from two angles as shown below Tangible Form: Liabilities + Capital = Assets
Intangible Form: Liabilities (legal + contractual) + Liabilities (non-contractual but social, comprising Employees, community members and the state).

Note: At the present moment the Entity Theory is the leading most theory for companies and the point of view of the Proprietary Theory may still be used in the context of Sole-traderships and Partnership firms. The Enterprise theory is the accounting equation form of Social Accounting, which is yet to have Universal application.

Residual Equity Theory:
In this approach, the Equity Shareholders are shown separately from other equity holders like lenders. Creditors and preference shareholders, because changes in the values of assets will not affect the legal and contractual claims of those equity holders who are not equity shareholders. The fact that the equity shareholders are entitled to the residue of assets after meeting the claims of lenders, creditors and preference shareholders is highlighted by altering the fundamental equation into:
Assets – Specific Equities = Residual Equities.

Note: Specific Equities include creditors, lenders and preference shareholders.
This theory, therefore, stands halfway between proprietary Theory and Entity Theory.
Fund Theory:

This theory calls for a very critical analysis of the concept involved since it tends to violate, though conceptually only, the separateness of the owner/s entity (existence) from that of the business. It does not affect the mechanical aspect of double entry book-keeping, which will be carried out in the same manner, regardless of the equity theory, which a specific entity is following, in so far as what is to be debited and credit different situations which give rise to financial transactions. The focus on the separateness of entities is withdrawn as repositioned on the operational and activity aspects of an Organisation. This new area under focus is called the "Fund" which is nothing but a conglomeration of assets and related obligations and restrictions denoting specific economic (hence financial also in most of the cases) operation/activity undertaken by the Organisation. This Fund theory is, therefore, based on the modified equation:

\[
\text{Assets} = \text{Restrictions on the use of Assets}
\]

Assets represent prospective services to the Fund, that is a specific operational unit, say, Governmental expenditure on Education. Liabilities represent restrictions against specific or general assets of the fund, that is the invested capital, say, Government’s allocation of money for expenditure on education, must be maintained unless specific authority has been obtained, which means that money allocated for expenditure on education must be spent only, on education. However, in very special cases some exceptions are allowed. This is primarily meant for ensuring strict adherence to planned expenditure on specific areas of activities, for various reasons, such as, social, political, economic, ethical, etc. This automatically gets involved with rigid rules of accounting and administrative accountability on the part of those who have been authorised to dispose of fund-specific assets. Naturally, therefore, this theory is found extremely suitable and useful for social organisations, political and charitable organisations, including educational institution, social welfare institutions, political parties, clubs, charitable trusts and the like. Since a Government is concerned with all the above activities, it goes without saying that by and large, Government Accounting is Fund Theory-oriented.

Commander Theory:

Fairly recently some experts have criticised the Proprietary, Entity and related theories on the ground that none puts emphasis on the correct economic aspect of an entity. On the contrary undue emphasis is put on the legal and/or accounting feature of a personified entity to the exclusion of people who carry out economic, managerial accounting and social functions on behalf of an artificially created person devoid of any human characteristics of its own. Undue emphasis is also put on ownership that is equity and today the question of ownership is vague and complicated and difficult to understand logically. Ownership is a legal matter, but "Control" is intrinsically an economic hence human agency-related. Those who control are commanders. There are different kinds of commanders. For that matter, shareholders as well as members of the management team are commanders since they can take decisions about the source and application of fund as well as exercise specific control functions. Command guide commanders. Commander communicates with commander.
Commander reports to commanders. Hence, finally the Balance sheet should be construed as reporting of one-group commanders (the management) to the group of commanders (the owners). Management is entrusted with initiating action pertaining to source and application of funds. The owners are authorised to appoint, remove and guide the management, rather, allocate responsibility to management and the exercise control on the management by demanding accountability reports in the form of Balance Sheet and the P/L A/c, though they (the owner) do not enjoy day-to-day control right. On the other hand, the management enjoys the right to exercise day to day control but not ownership-related control, such as, adoption of accounts, appointment or reappointment of auditors are directors and declaring dividends in the advice of management (basically a staff and not an executive function). To project this view point in the correct perspective, the fundamental equation is expressed as:

\[
\text{Liabilities} = \text{Assets} \quad \text{to signify} \quad \text{Source of Funds} = \text{Application of Funds.}
\]

**In other words:** Most economically and judiciously controlled raising of funds = Most economically and judiciously controlled application of funds.

**Note:** A parallel economics theory known as Agency Theory is fast approaching the Centre stage in the theory and practice of management of economics organisations and related accounting aspects. Though this theory is outside the scope of the study Notes, yet it would be useful to note its basics theme which claim that the management will first take care of its personal aspect/s out of self-interest and maximisation of shareholder’s funds entrusted to it for enlargement through profit maximum will assume a position of secondary importance to it (the management). This theory is still now well founded. But the fact remains that human psychology, whether operation through an individual or a group, has yet been established on sound logical and scientific foundation. Hence the psychological aspects of human behaviour will continue to be a debatable issue at least for quite some time into the foreseeable future.

### 2. MONEY MEASUREMENT CONCEPT:

A record is made only of the information that can be expressed in monetary terms for accounting purposes. The advantage of doing this is that money provides common denominators by means of which variety of facts can be expressed as numbers that can be added and subtracted. This enables addition and subtraction of varied items since money provides the common denominator. An event even though important like the loyalty of the workers will not be recorded unless it can be expressed in monetary terms. The changing price level also creates difficulties in the monetary value.

If we look at financial accounting purely from the point of view of Fundamental Accounting Equation:

\[
\text{Assets} = \text{Capital} + \text{Liabilities.}
\]

Then it would be evident that it had virtually no option but to adopt monetary values of assets and liabilities and capital to apply the equation day-to-day business affairs. This concept is basically concerned with the problem of measuring items of the accounting
Accounting Principles and Accounting Standards

equation. Such items may be, plant and machinery (an assets), liability for loan taken – all these are object of some kind of the other. Other items represent events (transaction) such as expenses and income. Basically, double entry system is additive (say, when finding the aggregate of assets) or subtractive (say when total liabilities are deducted from total assets to find capital, or deducting expenses from income to estimate profit). But only the "like" can be added with the "like" and the "like" can be deducted from the "like", when the word "like" means that the items involved are expressed in the same unit. But in real-world affairs, physical assets may have to be expressed in several ways, like numbers of units, weight, volume, etc. Likewise wages may have to be expressed in man-hours or simply in hours. Apart from ensuring feasibility of making addition and subtraction, which is inherent in the accounting equation, the sign of equality (actually the sign of "identity") needs use of the same units in describing such items. In accounting the description is finally expressed quantitatively in terms of money. In modern business it is essential link to accounting to a market system in an exchange economy a valuable source of quantitative data. Since goods and service are generally exchanged in terms of money, a monetary measurement of economics data can be assumed to be useful in decision-making, particularly for that decision relating to wealth and the production of goods and services.

At first you may wonder, how items other than assets, liabilities and capital, such as expense and income may appear in the fundamental accounting equation:

\[
\text{Assets} = \text{Liabilities} + \text{Capital}
\]

Well, during the year/period, transaction relating to expense and income usually referred to as "nominal accounts" are recorded until they are summarised at the end of the year (in the form of a Balance Sheet, as the P/L A/c only provide details of periodic profit or loss). The following illustration will clarify this, assuming a profit - earning year.

Accounting Equation as at the beginning of the year:

\[
\text{Assets}_1 = \text{Liabilities}_1 + \text{Capital}_1
\]

Recording of expenses and income during the year:

\[
\text{Assets}_1 + \text{Expenses} = \text{Liabilities}_1 + \text{Income} + \text{Capital}_1
\]

Arriving at profit at the end of the year:

\[
\text{Assets}_2 = \text{Liabilities}_2 + \text{Capital}_2 + (\text{Income} - \text{Expenses} = \text{Profit})
\]

From equation (3) above, we now get:

\[
\text{Assets}_1 = \text{Liabilities}_1 + \text{Capital}_1 + \text{Profit} = \text{Liabilities}_1 + \text{Capital}_1
\]

Notes:

a) At the end of the year : \( \text{Capital}_1 + \text{Profit} = \text{Capital}_2 \)

b) Every transaction of expenses or income is related to either flow of an assets or the incurring of a liabilities or change in the capital. As a result, at the end of the year, we get :

\[
\text{Assets}_1 + \text{liabilities (net) assumed during the year} = \text{Liabilities}_2
\]
In fact, Capital\textsubscript{2}

\[ = \text{Capital}_{1} + \text{Profit} + \text{Net change in capital due to capital related transactions during the year, like issue/ redeeming of ownership capital.} \]

Hence the Final Accounting equation as at the of the year would be:

\[ \text{Assets}_{2} = \text{Liabilities}_{2} + \text{Capital}_{2} \]

Valuation, strictly speaking is barter-oriented. But the barter system has the following practical drawbacks:

a) Every person having a surplus item to exchange has to look for another person who has a surplus to exchange for the surplus of the former, which may be quite difficult on most of the occasions.

b) Barter of perishable goods is a constant source of worry and anxiety to the holder of such goods.

c) Carrying bulky goods would cause as much problem of carrying livestock.

d) The subtlety of barter value of services to be bartered poses real difficulties.

e) The combinations of a large number of barterable items would create a lot of computational problems. For example, if ‘n’ number of items are to be bartered, the possible combinations would be n^{c_2}. However. The emergence of money as a medium of exchange as well as a temporary ‘abode of purchasing power’ (that is, its storage value) solved all the above problems. But, at the same time, the process of measurement itself became as undependable affair due to fluctuation in the value of money itself, which has been used as a unit of measurement. This becomes a gigantic problem when prices fluctuate violently as in hyperinflation. However, researches are at work to find out practical ways and means to combat this problem. Current Purchasing Power Accounting (CPPA) and Current Cost Accounting and the like are some such attempts. In certain cases they have succeeded in tackling the problem, but their overall track record is far from "satisfactory". Money measurement imposes a severe limitation on the scope of accounting report; as it excludes non-monetary facts like quality of the product, labour strike, rift between production and sales manager, management calibre, economic climate, etc. However, researchers are still busy in finding out a more acceptable and successful approach to the problem. The criteria of a good measurement system should possess at least the following attributes:

a) **Objectivity:**

This means that the same items measured by different competent persons should produce the same value, subject to some conditions. Objectivity enhances the verifiability of the value of an item measured.

b) **Uncertainty:**

One of the most important uses of current financial data is to estimate the future as correctly as possible. Such predictability is an important aspect of any decision making process. Hence, it is most desirable that the predicted
Accounting Principles and Accounting Standards

future value on the basis of present value, mainly, should not be distorted by any measurement related disturbing factor.

c) Freedom from bias:
Bias is another name in accounting measurement for palpable subjectivity. This becomes a really difficult problem to solve if such bias is inherent in the measurement process. Statistically, it can be measured by measuring standard deviations of observed data with reference to some "true" or "near true" value. For example replacing historical cost by current cost may go a long way towards removing or controlling bias, but that would be at the expense of verifiability, in the presence of violent price fluctuation. Sooner or later, we will have to find out a better solution.

Note:
1. For decision making sometimes non-monetary information may be acutely needed. Hence, this may be provided along with monetary value, disregarding the principle of double entry accounting.
2. The emergence and rapid development of Management Accounting has greatly facilitated decision-making by appropriately co-relating monetary data to non-monetary data.

3. COST CONCEPT
Transactions are recorded in the books at the price paid that is the cost. This avoids an arbitrary value being placed on the asset and all subsequent accounting is in relation to the cost. Therefore, the recording of the assets is at cost figures and this may not reflect the current market value especially in the case of the older assets. The value of an asset in the accounting records does not remain at the original cost because it is diminished systematically by virtue of its use called expired cost and then shown at its depreciated value e.g. an asset of Rs. 1,00,000 is depreciated at 10%. Therefore, closing value will be Rs. 90,000 in the Balance Sheet. An expired cost is an expenditure of money, the economic value of which has been made use of during a particular year (or lost without accruing any benefit to the entity, like machinery destroyed by flood). Every cost has to be recovered from the market through sales, otherwise, the entity will suffer loss, that is, lose its capital. Depreciation, looked at from this view-point, is nothing but gradual recovery of cost incurred, that is, money paid at a time during a particular year for acquiring a fixed asset, during the subsequent years (during which the asset is assumed to remain serviceable) on some estimated basis, by treating the expired cost pertaining to a particular year, calculated on some approved and selected estimated basis, by including such expired cost, called an expense, in the cost of production of that particular accounting year. Linking annual depreciation with the expected service life of a fixed asset does not endow any scientific logic on any estimated basis of depreciation. In accounting, depreciation is nothing more and nothing less than a process of allocation of some specific costs (cost of acquiring fixed assets) on some generally accepted (may or may not be legally approved) estimated basis. An expired cost is not a money measure of the wear and tear obsolescence (passage of time) etc. of any fixed assets. It is just a reasonable basis for recovery of cost of fixed asset in a gradual manner. Money value
of wear and tear would need engineering analysis, which is not the domain of financial accounting.

In essence, in a little more technical sense, cost represents the exchange price agreed upon by the buyer and the seller in a relatively free economy. Cost has been the most common valuation concept in the traditional accounting structure.

Therefore, Cost is the exchange price of goods and services at the time they are acquired. So, cost is also the economic sacrifice expressed in monetary terms required to obtain a specific asset or a group of assets. Very often cost is not represented by a single exchange price, but it includes many sacrifices of economic resources necessary to obtain the asset in the form, location and time in which it can be useful to the operating activities of the firm. Thus, all of these sacrifices should be included in the concept of cost valuation. For example, the cost of a plant or machinery should include: original exchange price, import duty, transportation charges, handling charges, erecting and installation charges, etc. depending upon the circumstances of each particular case, until the plant becomes satisfactorily operational. It is also assumed that cost represents the value of the asset to the firm at the time of acquisition, but this cannot be proved, since all factors of the enterprise are used jointly (and preferably in desirable co-ordination) improving the cash available, by realised profit or surplus. To be more specific, we pay exchange prices separately for acquiring different types of assets. But, for a manufacturing enterprise, it is no use simply acquiring assets after another unless they are properly utilised in harmony to the product, which the enterprise wants to be sold at a realised profit. Hence, from the point of view of utility, it becomes very difficult to value each of those assets individually. It is because of the teamwork of a group of mutually useful assets, for example, when a team playing well, it is very difficult to assess the contribution even of a so-called mediocre player, to the team performance. It follows from cost based accounting that if nothing is paid in acquiring an item, the same will not be normally recorded as an asset. Thus a favourable business location, which becomes of increasing importance as time goes on, a good reputation with its customers (goodwill) will not be recorded as an assets in the accounts of the company although they have monetarily value. One of main disadvantages of historical cost valuation is that the value of the asset to the firm may change over time, after long period of time it may have no significance whatever as a measure of the quantity of resource available to the enterprise. Historical cost valuation is also disadvantageous because it fails to the permit the recognition of gain and losses in which they may actually occur (this point will become more clear when the concept of matching cost against revenue will be discussed later on). Also because of change over time, costs of assets acquired in different time period cannot be added together in the Balance Sheet to provide interpretable sums.

Discounting Future Costs:

Most non-monetary assets represent goods or service acquired in advance. There are many reasons for which such advance acquisitions are made. For example, it is less costly (because of trade discount on bulk purchase or before anticipated price rises). In those cases, the equivalent cost of the assets-linked service at the time of actual use may be the most
relevant valuation concept. In this context, the present value of these service (the asset) is
the discounted value of costs. However, no discounting, that is, recognising the time value
of money, would be necessary where the service will be available in the near future, as in
the case of prepaid expenses temporarily assetised (in the "current asset" category), at the
end of year when the cost was yet to expire. But, in other cases, the cost price (since
bought at a cheaper rate in advance) may be less than the amount that would have been
required if the service had been acquired when needed. In part, this difference is due to
the interest factor, and in part to other factors (like inflation). At this stage, we need not go
further into the detail of the cost concept. However, being aware of the impact of the time
value of money, up to understand properly the related literature, since tremendous amount
of research work is going on in this regard to make decision-making more relevant in the
face of fast-changing scenario.

4. **GOING CONCERN CONCEPT**

Accounting assumes that the business will exist indefinitely into future and accordingly
transactions are recorded. If however, there is evidence that the firm will be liquidated then
market value of the assets and liabilities will be ascertained and necessary accounting
considered. In other cases where the business is an on-going activity resale value of assets
is irrelevant. The whole accounting is done based on this assumption.

The present concept as well as the earlier Business Entity concept belongs to the category
of "Environmental Postulates of Accounting". It is important to know the precise meaning
of this expression, for which purpose we have to know what an accounting postulate is and
what is environmental in accounting. In order to avoid a lengthy discussion, we may
summarise, by stating that postulates are basic assumption or fundamental propositions
concerning the economic, political and sociological environment in which accounting must
operate. Thus, it is clear that certain economic, political and sociological events do affect
the thinking and actions of accountants and we must also clearly understand that every
such event does not affect accounting concepts and practice. The basic criteria for any
such postulates are:

1. They must be relevant to the development of accounting logic, that is, they must
   serve as a foundation for the logical derivation of further prepositions; and

2. They must be accepted as valid by the participants in the discussion as either
   being true or providing a useful starting point as an assumption in the development
   of accounting logic.

It is not necessary, that the postulates be true or even realistic. For example, the assumption
in economics of a perfectly competitive society has never been true, but it has provided
useful insights into the working of the economic system. On the other hand, an assumption
of a monopolistic society leads to different conclusions that may also be useful in an evaluation
of the economy. The assumptions that provide the greatest degree of prediction may be
more useful than those that are most realistic. The environmental of accounting has a direct
bearing on the objectives and on the logical derivation principles and rules. You may recall
that accounting environment comprises economic, political and sociological factors. But
not all aspects of society are relevant to accounting, some are clearly, irrelevant. Others are only indirectly relevant, and many social, political and economic are directly relevant. What may be relevant during one period of time may be irrelevant during another and vice versa. For example, the development of the railways and the proximity of a factory to a railway may have been much more important to some enterprises before the construction of high-speed highways. Even a few decades ago pollution, ecology etc. had no bearing on accounting. But today they have become compulsive forces on current thinking on accounting. The objective of stating environment postulates (those which are directly or indirectly influenced by the accounting "milieu" – environment) is to point out what aspects of a society are relevant to accounting and to decide which of conflicting situations or of several institutions are more significant for providing a framework for broad generalisation. Most statements of environmental postulates include in assumption that exchanges in the economy take place in markets and that market prices leave significant implications for accounting. However, there is no agreement regarding which prices are relevant. These differences arise because of different objectives of different authors of accounting postulates based on accounting environment.

**Going concern or Continuity Concept:**

In addition to the "accounting entity concept", a further observation made regarding the nature of the relevant accounting entity is that most economic units are organised to operate over an indefinite period of time. Therefore, it is frequently argued that it is a logical step to recognise that the entity should be viewed as remaining in operation indefinitely under normal circumstances – this is the traditional going concern postulate. But, we must know that all accountants do not agree to this. This postulate includes among the classification of imperatives (compulsory practices), apparently, because accounting practice does not generally, recognise this assumption throughout the entire accounting process. However, so far as we are concerned we should follow this postulate. If there is evidence that it will not continue in existence long enough (for instance, where there are large and persistent losses or where it appears that the enterprise cannot continue at a profitable level) general accounting principles would not apply and the accountant has the professional responsibility of informing through proper channel the users/readers accordingly. The reason for including the continuity postulate is generally to support the benefit theory of valuation (like the opportunity of spreading the cost of fixed assets over a number of years, uniformity in accounting to ensure more meaningful comparisons because of the opportunity to adopt accrual basis of accounting, etc.) or in some cases to support the use of historical costs as opposed to liquidation values. Another interesting view is offered by some researchers who do not accept the usual meaning of the going concern postulates by stating that a going concern is an enterprise that adopts itself by the sale of its assets in the ordinary course of business, that is in orderly liquidation as opposed to forced liquidation. This assumption thus supports the proposition regarding the relevance of current cash equivalents. Some experts assume an expected life span of the entity without necessarily assuming that it will be indefinite. Logically, this would include an expected life of zero (i.e., in finding liquidation situation). Another expert holds the view that the continuity concept is not an assumption,
but a condition—one that is at least to a large extent a verifiable attribute of the business system. He contends that it is a "status quo" assumption that is really an extension of the measurement process. But the opponents of this view argue that the status quo assumptions are falsifiable and misleading. They propose that rather than making continuity an assumption, it should be a prediction. They further argue that the going concern concept does not automatically justify valuation on historical costs since there may we believe that postulates should basically be predictive to help make future prediction. Hence there is no need to interpret the going concern concept either as a status quo concept or as a justification for valuation on historical costs or even the benefit concept of accounting (as already explained). However it is relevant postulates, leading to the presentation of accounting information regarding resources and commitments and operational activity (such as sales of goods and services over several years), on the ground that such information may aid in the prediction of future operational activity. Continuity assumes some connection between the past and the future, although not necessarily that the future will be repetition of the past. In the case of discontinuity, such as a forced liquidation, the usual accounting procedures would not apply, and the accountant should disclose the nature of the discontinuity and then its resources would be reported at their liquidation value. Such circumstances are uncommon.

This concept will come out in bolder relief in our subsequent discussion of the concept of matching cost against revenue.

5. Dual Aspect Concept

The economic resources of an entity are assets and the acquisition of an asset must be on account of: –

(a) Some other assets being sold: or (b) the creation of an obligation to pay; or (c) there has been a profit owed to proprietor; or (d) The owner has contributed.

On the other hand, an increase in liability is on account of an increase in asset or a loss. Therefore, at any time –

\[
\text{Assets} = \text{Liabilities} + \text{Capital}
\]

\[
\text{Capital} = \text{Assets} - \text{Liabilities}
\]

The owner’s share is what is left after paying outsiders. This is the accounting equation. Every transaction has dual impact and accounting systems record both the aspects and are called the double entry system. e.g. X starts a business with a capital of Rs.20,000. There are two aspects of the transaction. On the one hand the business has assets of Rs. 20,000 while on the other hand it has to pay the proprietor Rs. 20,000, therefore: –

\[
\text{Capital (Equities)} = \text{Assets (Cash)}
\]

\[
\text{Rs. 20,000} = \text{Rs. 20,000}
\]

What has been stated above is an oversimplified version of the concept and its application, since this is the form of the concept with which we are familiar as beginners. But we have to go a little deeper in order to have a more meaningful understanding of the concept because it is the bedrock on which double entry book keeping has built its gigantic edifice
and is still flourishing as a very important discipline all over the world. There must be something deeper than what has been stated above which caught the imagination of an Italian priest and mathematician and prompted him to codify if not invent the double-entry system in 1495 which explained logically and systematically what happens in the economic world, in terms of money when goods are manufactured and sold at the market place through financial transactions. This could be applied to sale of services equally logically, and systematically. In course of time it also exposed other related concepts, especially the first two concepts already discussed, namely the Business Entity concept and the Money Measurement concept. The two basic economic phenomena which constitute the foundation of the Dual Aspect Concept are as follows:

No financial/commercial/transaction as distinct from gifts is unilateral. In a financial transaction, each party receives as well as gives up things, which have economic value, of matching amount when a deal is finalised. Otherwise, why should one knowingly, pay in value (money value) more than that one perceives to be the value (in money) of what one receives in exchange? Hence, when one receives something of an agreed money value one's resources go up by that amount only to be reduced by the same amount, which is the agreed money value of what one gives up. This is now being interpreted as an event in which each party, to a financial transaction is affected in equal amount on two accounts, one account represents the money value of what the person receives while the other account represents the money value of what the person has to give up in exchange. If money or its equivalent is perceived to flow in when it comes in and flows out when it goes out then "coming in" and "going out" would represent opposite directions, but of equal money-value, otherwise the transaction would not have materialised. Which is why today’s accountants explain that when a transaction (financial) takes place, each party is affected equally on two fronts, that is, two accounts, but in opposite conceptual directions. But, how to equate “going out” and “coming in”? This can be solved if we look at each asset as a property, (wealth) as well as a claim on such property. Hence, the value of the property has got to be equal to the value of the claim on it, both in monetary terms, of course. If a property holds some reasonable promise of yielding some financial benefit in future, then every claim should be holding a prospective “threat” to give up something. This concept can be very elegantly and precise but forth if we describe a claim as a liability and a property as an asset.

Hence : Property = Claims on property. (i)
Or, Asset = Liability. (ii)

Now, a liability is internal if the owner of the business has claim over an asset, This has to be distinguished from a claim in favour of a person other than the owner. Hence owner’s claim is called the capital and others’ claims as liabilities.

Hence, we get, Assets = Internal Liabilities + External Liability. (iii)
Or, Assets = Capital+ Liability. (iv)

We have already explained how from the opening Balance Sheet for a year, that is opening Accounting Equation; Assets = Capital + Liability, is changed into Assets = Capital + Liability as at the end of the year, that is closing Balance Sheet. We have explained, how the various
Accounting Principles and Accounting Standards

financial transactions entered into during the year, keep altering the initial equation for every transaction, caused by receipts and payments of money, goods, and services, unwiring expenses and earning income in our discussion of Money Measurement Concept.

Note: The notation of summation "S" has been omitted and the present discussion has been restricted to one "Asset" one "Liability" and one Capital for the sake of simplicity.

For a better understanding of the Dual Aspect Concept the following points should be borne in mind:

(a) The liabilities side of a Balance Sheet represents all the providers of the business fund, whether obtained from the owner/s or others. Hence this side represents the "Sources of Funds". Similarly, as assets are obtained by utilising fund, the Asset side represents the "Application of Funds".

(b) We are familiar with the "golden rule of accounting/Book keeping". This rule requires us first to classify accounts into Real, Nominal and Personal categories, and then apply the conventional rules as to which account is to be debited while which account is to be credited with for each transaction. There is nothing wrong with this system. But it does not very clearly highlight that for, whatever having a money value, we have to give up something of equal money value to the other party to the financial transaction.

In order to clearly associate this process of equality of opposite direction-oriented giving up and receiving of goods/services, we may consider a new approach which is known as the "Input-Output Concept" of equality of each financial transaction's two constituents of giving and receiving. According to this concept, the giving up and receiving of what constitutes the two components must belong to any one of the following categories:

i) Goods of all kinds ranging form nails to ships;

ii) Services of all kinds ranging from those rendered by sweepers to what are rendered by the world's topmost scientist.

iii) Facilities of all kinds which are akin to services but differ from the later in the sense that they do not include the exertion of an individual’s physical or intellectual energy. Examples of facilities are – letting out of land, building, plant and machinery, equipment, etc.

iv) Money itself, for example, a banker’s main business is lending out and getting back the let out money.

v) A promise to pay some definite person a definite amount on or by definite date. Such promise may be oral or by conduct or in black and white. To illustrate let us take the case of sale of goods on credit. From the seller's point of view, he/she parts with goods of agreed monetary value. But, what does he/she concurrently get in exchange therefore so as to establish the universal applicability of the double- entry principle of bookkeeping? He/she immediately gets a promise from the buyer to pay him/her in future.
Hence strictly and academically speaking, the seller would pass the following entry :-

Promise to Receive money from :
Mr./Mrs.……..A/c (Receipt of something)………..Dr.

The language of bookkeeping has an inherent tendency to get as much symbolic as possible. As a result, in actual practice, instead of receiving a promise to get money in future from Mr./Ms. "so and so". Mere Mr./Ms. so and so’s A/c is considered sufficient for getting a debit entry likewise, suffice it to write merely Sales A/c instead of Sale of Goods A/c. According to the same logic, when eventually the debtor pays up, the seller receives cash and gives up the promise received earlier. Hence Cash/Bank A/c. is debited while Mr./Ms. So and so, A/c is credited. The same logic will also hold good from the point of view of the buyer on credit. First, he receives goods which is indicated by Purchase A/c. (in fact Purchase of Goods A/c) and gives up a" Promise to pay to Mr./Mrs. So and So", for which merely Mr./Mrs. So and So’s A/c. is credited. When he/she meets his/her past commitment, what comes in is the promise to pay given earlier and what goes out is Cash/Bank A/c. It may be observed that, in every case what goes out or comes in belongs to one of the five above referred to categories of things.

To sum up every transaction recorded in the accounts effects at least two items. There cannot be a transaction, which will result in only a single change in the accounts.

Note : The P/L A/c is something not directly connected with the fundamental accounting equation. It is a convenient and informative means by which accumulated periodic expenses are matched against periodic incomes to estimate the outcome of carrying out normal business activities during the said period, to find out if as a result thereof capital has undergone an increase or a decrease.

6. Realisation Concept

The realisation concept indicates the amount of revenue that should be considered from a given transaction. Realization refers to inflows of cash or claims to cash. It states that the amount recognized as revenue is the amount that is reasonably certain to be realised. Sometimes there is scope for difference of judgement as to how to ascertain" reasonably certain". A situation arises when a company makes a credit sale and expects that the customer will pay their bill. Experience shows that not all customers pay their bill. In measuring the revenue for a period, the amount of credit sales that will not be realised should be reduced by the estimated amount of credit sales that will never be realised i.e. by estimated amount of bad debts. Example: If a company makes a credit sale of Rs 100,000 during a period and experience indicates that 2% of credit sales will become bad debt, the amount of revenue for the period is Rs 98,000 and not Rs 100,000. It does not anticipate events and stops the business from inflating their profits by recording sales and incomes likely to accrue. Unless money has been realised as cash or legal obligation to pay on sale, profit or income is considered. e.g. M places an order with N for supply of certain goods yet to be manufactured.
On receipt of order N purchases raw materials, employs workers, produces goods and delivers to M. M makes payment on receipt of goods. In this case the sales is not at the time of receipt of order but at the time when goods are delivered to M.

The modern concept of Revenue Income is that it is the product of an enterprise or services rendered by it which has been measured by an exchange value or cash equivalent. This definition does not solve the problem of deciding the point/s in time when we should measure record and report the revenue. According to Economics, value added is a continuous process. In very simple terms Value added = Sale value of a product – the cost of raw materials and other goods (components) bought from outsiders (suppliers). This involves acquisition and assembling raw materials and changing them from or processed by the application of labour and fixed assets. Revenue reporting entails not only the acknowledgement that an entity has produced economic value in the form of goods or services, but also the measurement of that value. The product or services can be measured best by the money or money equivalent expected to be received for the products/services at some time in the future. It is the uncertainty of this expected receipt and the search for variable measurements that have led accountants to the adoption of specific rules for the timing of revenue. Sprouse and Moonitz stated that revenue should be identified with the period during which the major economic activities necessary to the creation and disposition of goods and services have been accomplished, provided objective measurements of the results of those activities are available. These two conditions, namely, accomplishment of major economic activity and objectivity of measurement, are fulfilled at different stages of activity in different cases, sometimes as late as time of delivery of product or rendering of services, in other cases at an earlier point of time.

An alternative to the reporting of revenue at the time of accomplishment of the major economic activity is the critical event (or crucial event) concept of revenue reporting. In most cases, the value added by the enterprise (reported as net income, that is, net profit) is jointly associated with the entire process of planning, producing, providing the goods or services for customers and the final collection of cash, and, in some cases, the providing of services (such as repairs under warranties), beyond the collection process. Because of the jointness of this value added over time, it is impossible to make a logical allocation to the several processes. Therefore, an expedient method is to report the value added by the enterprise at a single point in time. The critical event concept suggests that the most appropriate moment of time is when the most critical decision is made or when the most difficult task is performed. This could be at the point when the contract is signed, the time when the services are performed, when cash is collected (as in the hybrid system of accounting, under which professional men like doctors and lawyers keep accounts on "accrual" basis for expenses but incomes like professional fees are recorded on "cash" basis) or at some other time.
The Reporting of Revenue During Production:

The traditional accrual basis of accounting recognises revenue as earned if there is a simultaneous increase in the claim against the customer or client. This is the general practice with services. The product of the enterprise emerges as the services are provided. The amount of the claim is usually determined by prior agreement (contract), or often by established trade practices, even though the client or tenant may not be required to make payment until at later date or at least until a determinable amount of service has been provided. Examples are: rent, interest, commission, personal services rendered on a time basis. In each of these cases the basic criteria for revenue reporting are met. The services are usually performed on a time basis and the performing of services may be crucial. The amount of the revenue has been established by prior contract/agreement. In addition a valid claim arises against the customer, client or tenant even though the amount is not billed and payment is not required until a later date.

Long-term contracts:

The generally accepted practice in this case is based on pragmatic grounds and supported by theory. An individual or a firm would usually object to publication of financial statements showing no income for a year during which the organisation had spent considerable efforts in obtaining partial completion of a contract (as in contractual jobs) that would have permitted a reasonable profit with a fair degree of certainty. If contracts are completed at irregular intervals, the reporting of profit only when the contracts are completed could result in hardship or injustice to the shareholders who wish to see their interests before the completion of major contracts because of lack of information. The annual P/L might have less meaning also from either a managerial or a financial point of view. The most important consideration is that the total price of the contract is determined in advance or is determinable. Uncertainty regarding the selling price is minimised and uncertainty regarding collection is usually not very great, if any Government is the contractee and other renowned private sector companies. Two areas of uncertainty remain, however: (1) At any particular point, it may be difficult to determine the sale price of the product produced to date, (2) The total costs of the project may be difficult to estimate with accuracy. If the total costs of completion differ from the estimated costs, the net profit of each period will have been affected. Uncertainty, however, should not be cause for the failure to report revenue when the value increase can be measured. Reasonable estimates based on contract prices and expert judgement regarding costs may provide better information regarding the progress of the firm than on insisting on the narrow realisation concept. The actual treatment can be found in any textbook on Cost Accountancy. For example, if the progress of the contracted job is neither 100 per cent nor nearing completion, accountants usually taken into the P/L A/c of the concerned year, the following amount:

\[ \text{Book profit} \times \frac{2}{3} \times \frac{\text{Cash received}}{\text{Value of work certified}} \]

The above amount is conservative and at the time report progress to external users, without bookishly following the age-old criteria for the realisation concept, though two uncertainties still persist.
The discussion of the topic would be incomplete without a reference to Accounting Standard – 9 (AS–9) issued by the Chartered Accountants of India (ICAI), which is titled:

Revenue Recognition: The following is an extract from AS–9:

“11. In a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

(i) the seller of the goods has transferred to buyer the property in the goods for a price or all significant risks and reward of ownership have been transferred to the buyer and the seller retains no effective control of goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

12. In a transaction involving the rendering of services, performance should be measured either under the transaction involving the rendering of services, performance should be measured either under the complete service contract method or the proportionate completion method, whichever related the revenue to the work accomplished. Such performance should be regarded as having been achieved when no significant uncertainty exists regarding the amount of the consideration that will be derived from rendering the service.

13. Revenue arising from the use by other of enterprise resources yielding interest, royalties and dividend, should only be recognised on the following basis:

i) Interest: On a time proportional basis taking into account the amount outstanding and the rate applicable.

ii) Royalties: On an accrual basis in accordance with the term of the relevant agreement.

iii) Dividends from Investment in share: When the owner’s right to receive payment is established.

Disclosure:

In addition to the disclosures required by AS–1 on Disclosure of Accounting Policies, an enterprise should also disclose the circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties.”.

7. Accrual Concept

Profit arises only out of business operation when there is an increase in the owner’s share of the business and not due to his contribution to the business. Any increase in owner’s equity is called revenue and any reduction in it termed as a loan. In fact, it is the direct outcome of Realisation Concept (already discussed) and the Accounting Period concept (to be discussed). In a way, realisation concept has been split up into two parts, namely, production of economic goods or rendering of economic services, and realisation of due
Advanced Financial Accounting

revenue. Any uncertainty about any of the two elements beyond what is considered uncontrollable will not permit the accountant to treat the money value or cash equivalent of the sale price to be considered as realised income. Another very vital element is involved in between, that is, a third one, namely acquiring legal right to claim the price of the goods delivered or fees for services rendered. Acquiring the legal right to claim the consideration for goods/services is called accrual of revenue, which usually precedes collection. However, in case of cash transactions, under the accrual method P/L A/c and Balance Sheet are prepared on the accrual basis, in the absence of any uncertainty about collection. This does not mean that collection has been given less importance than economic value adding and the right to claim the purchase consideration. With uncertainty about collection, it is meaningless and dangerous to take income into account as having been realised. In fact, ability to pay, is considered by the supplier of goods and services before one decides to sell his products or render his services to another. Then after the deal is finalised, goods have been delivered or services rendered and legal right to claim the purchase consideration has been acquired, collection is taken up as a specialised process to ensure return of capital and earning of profit. The other pressure comes from the Accounting Period convention. Production is a continuous process. True profit is cash profit during the entire lifetime of an enterprise. Then and then only we know total money collected and spent by it during its lifetime. But the way our culture has bound us up with annual profit, annual income and other periodic results, we have divided the entire life-span of our organisation into several chapters, each chapter being an accounting period or an accounting year. A year consists of 12 months. This is very significant, because each period being equal in terms of time frame, it facilitates comparison of performances. Because of this Cost Accountants divide a year in 13 months, each period consisting of 4 weeks. The process of dividing the life span of a company into time – chapters which is an artificial man-made process, though production follows a continuous flow, gives rise to certain accounting problems. For example, at the time of closing of period/annual accounts, production and sale might have been completed, local right to claim the sales value have been acquired, but payment has not yet come through. Yet, the sale will be included in the year of sale, though collection of dues has not yet taken place. However there is no material uncertainty about collection. Ascertaining revenue for a specific period automatically invites the question of matching cost against such revenue to estimate periodic profit. But modern experts have brought out certain inconsistencies and arbitrariness in such matching process. The most glaring example is charging depreciation to revenue. Despite a number of alternative treatments none is fully satisfactory logically. The only way to rationalise depreciation is a generally accepted principle of allocating costs of fixed assets for ultimate recovery through sales. Despite some shortcomings, accrual concept has become one of the fundamental assumptions of accounting mainly as a measure of periodic performance, which facilitates comparisons. According to the ICAI, this assumption is so basic that it need not be disclosed in the accounting policy of the enterprise, unless there has been deliberate departure. For example, logically speaking provision for gratuity should be made on accrual basis. But that would require actuarial valuation, which every organisation may not be able to afford. As a result, in India at least charging gratuity on cash basis has been an accepted accounting practice. Similarly, we have already referred
to the hybrid system of accounting followed by some professional persons who prepare P/L A/c with expenses on accrual basis but revenue only on Cash basis due to social and professional reasons. The system that is based on accrual concept is called the mercantile system. Section 209(3)(b) of the Companies Act, 1956 requires that books of account shall not be deemed to be kept if they are not kept on accrual basis and according to the double entry book-keeping in respect of a company. Thus the financial statements except cash flow statement are to be prepared on accrual basis.

8. **Accounting Period Concept**

The accounting reports measure activities for a specified interval of time called the accounting period, which is usually one year and therefore termed as annual reports. Interim reports in between may be compiled especially for internal users. Except for those ventures which are predetermined to end on the completion of a specific task or a specific time-frame, every enterprise, profit-oriented or not, desires to enjoy perpetual existence as a going (running concern), making profits, grow and distribute profits judiciously. This calls for recognition and measurement of incomes and expenses and to match them to ascertain profit. But, the concept of profit is time-related. Hence, the question: profit for what length of time? Theoretically, the most correct reply would be the entire life – time of an enterprise. That means no measurement of income until an enterprise is wound up. But human beings inherently, desire to know, periodic performances mainly for the purpose of comparison, which would not be possible, different firms wind up after different lengths of time. Moreover, from the practical point of view, some firms may not close down during a number of successive generations. Hence no income tax for ages, too. Let us not extend the list of such fanciful but important (academically) possibilities. Thus, out of practical considerations, businessmen, sided by accountants, divide the life span of an entity into a number of chapters of equal duration, usually a twelve-month period. Thus one phase of activities of an enterprise is deemed to have passed – one chapter is closed. Such a 12-month chapter is called accounting period. And financial accountants prepare a P/L A/c. for that period to estimate its operating result, that is, profit or loss and the financial position as at the end of the period in terms of assets, liabilities (external) and owners’ equity (internal liability).

This gives rise to a number of problems. Some of the major problems are discussed below:

a) **Cash Basis or Accrual Basis** – This question has already been discussed and we are convinced about the superiority of the accrual basis over cash basis, barring a few exceptions, like the preparation of hybrid accounts (already discussed) – by some professional persons.

b) **Matching cost against Revenue** – Sometimes it gives rise to allocation-related problems. For example, if substantial (but not unusually high) expenditure has been spent on advertisement in the last week of the accounting year, should not some part at least be carried over to the next year where it will get the benefit of the expenditure? Will it be correct to treat the whole of the expenditure as revenue expense (expired cost) for the year of payment and matched against the revenue for the year?
c) *Capital-Revenue Conflict* – We define a Fixed (Capital) Asset as one which is acquired/ not for immediate resale and it would give us benefits beyond the year of expenditure, that is, for over 12 months? We are so intimately concerned with a 12 month period, almost constantly, that an asset having an expected life-span of five years, is almost intuitively, treated as a fixed asset. But if we prepare a five–year P/L A/c., then the entire cost of the asset would be treated as the cost of one accounting period, though of 5 – year duration.

d) *Road Blocks to Company* – Besides estimating fairly and properly periodic profit/loss and period-end financial condition, another important use of annual closing of accounts is to facilitate comparison within the firm and outside the firm. Fixed Accounting Periods ensure comparability of equal time frames, but the accounting policies may differ from year to year and/or from firm to firm. This reduces the usefulness of periodic performance results. Hence uniformly of time-span of each business chapter should be supported by uniformity of accounting policies. If not so done prime facie, necessary adjustments should be made to facilitate comparability. Despite the above constraints, dedicated, experienced and enterprising accountants have succeeded in producing meaningful and useful financial information, without any respite, since a large number of accountants are engaged in a constant research work to improve upon existing concepts/practices, developing new ones to meet new challenges and to give more useful information. Accounting period assessment of income, expense, asset and liabilities can be compared with education, which is a continuous Process. To assess it we should consider the entire life span of an individual. But we artificially divide it into several man-made phases like: school leaving examination, undergraduate and post graduate examinations and doctoral assessment, etc.

**Conventions:**

The term "accounting conventions" refer to the customs or traditions, which are used as a guide in the preparation of meaningful financial records in the form of the income statement (profit and Loss Account) and the position statement (Balance Sheet).

These are as follows.

1. **Conservatism**

Financial statements are drawn on a conservatism basis where better evidence is required of losses. This is necessary as Management and ownership are in different hands and a cut is needed on management to show over-optimistic, favourable performance results. For example, inventories are valued at the cost or market price whichever is lower. Revenues are recognised when they are certain but expenses as soon as they are reasonably possible e.g. it encourages the accountant to create provisions for bad and doubtful debts.

Since inception, it has come to mean the following:
Accounting Principles and Accounting Standards

a) delay recognition of income;
b) Expedite recognition of income;

Note: This obviously affects the reliability of the process of matching cost against revenue.

c) if in doubt, understate assets and income;
d) If in doubt, overstate liabilities and expenses

Note: (c) and (d) above violate the postulates of consistency and therefore comparability.

It may result in creation of Secret Reserves if overdone, which vitiates reliabilities of financial statement as the opposite operation, namely, window-dressing. Today’s accountants condemn both the practices. The driving-force behind conservatism is: it is better to be wrong on the minus side than on the plus side of financial statements. This is pessimism and not sceptics. An accountant should be sceptic and not a pessimist; the former can be convinced by sound logic while the latter can be made to change her/his mindset. Moreover, there is no standard by which the degree of conservatism may be standardised. Hence, it becomes highly subjective and may even go to the length of seriously affecting the doctrine of disclosure.

At best, conservatism was and still is a very crude way to take financial guard against a world of uncertainty in which a business operates. But today’s accountant is quite well comparatively to assess risks. In fact, he is, in many cases, more competent than the user of financial statements. But subjectively cannot be fully avoided in assessing risks. Basically, in the present context, there are two kinds of risks, namely, (i) not happening what has been reported (statistically, the: "alpha risk") and (ii) happening of what has not been reported (statistically, the "beta risk"). Decades ago, accountant felt that for rejection of what might be true is more than what is untrue for favourable items. And vice versa for unfavourable items. Today accountants have realised that a true accountant should not indulge in such a practice what she/he should actually do is: to strike a realistic balance between the two kinds of risk – and provide information for a proper evaluation of the risk whenever possible; to be done by the user and not by herself/himself, even though he may be better equipped to do normally.

According to some experts, the only occasion which conservatism may be justified is when the accountant has to report on some thing which itself is highly subjective, enigmatic and elusive, like goodwill. Then the opposing camp would immediately question. Why bother to bring into accounting such capricious items?

2. Consistency:

This concept states that once the organisation has decided on a method, it should use the same method subsequently unless there is a valid reason for a change of method. If frequent changes are made it is not possible to carry out comparisons
on an inter-period or inter-firm basis. If a change is necessary it has to be highlighted. e.g. if depreciation is charged on diminishing balance method, it should be done year after year.

It is an accounting postulate since it develops the growth of the subject of accountancy with only a few constraints. By this standard, it is difficult to call conservatism an accounting postulate since it acts as constraints in many cases, as we have seen above. The basic prerequisite of the postulate of consistency is that the same accounting procedure, treatments, approaches, techniques, tools, concepts and principles should be applied from year to year within the firm; and also to the extent it is possible to ensure the same in all other organisations. But there are difficulties in having uniform principles and concepts and tools and procedures to be used by all the firm within a country, if not globally, mainly because of the following reasons:

a) local custom, economic, social and political environments may differ from place to place.
b) The different nature of business of different kinds and size.
c) Presence of valid alternatives, accepted by law and standard – setting bodies consistency serves two purposes, one directly and the other indirectly. Directly, it facilitates comparison, which is a vital tool for complex decision-making. Indirectly, when used over a considerable length of time it reduces risks surrounding operating enterprises.

Only in the following cases, change in existing practice should be permitted:

(a) when law or standards set by competent bodies require a change to be introduced, or
(b) when the change is to ensure better accounting system.

The importance of maintaining consistency is so acute today that the ICAI has treated this as a fundamental accounting assumption; its compliance need not be disclosed. Only deviation from it has to be fully disclosed. After many deliberations, standard-setting bodies, local, regional and international have failed to prescribe compliance with the same concepts and procedures and have been compelled to prescribe alternatives. Hence, this is not standardisation, critically speaking, it is harmonising, that is, reducing the areas of applicability and the number of alternatives.

3. Matching:

When an event affects both revenues and expenses, the effect on each period should be recognised in the same accounting period. This leads to matching concepts. The matching concepts is applied by first determining the items that constitute revenues for the period and their amounts in accordance with the conservatism concepts and than matching costs to these revenues. Thus both the aspects of an event are recorded in terms of revenue and expense in the same accounting period.
Accounting Principles and Accounting Standards

Theoretically it is an elegant postulate. But, in the practical field, it has number of limitations. The following are the main reasons why this convention fails in so many situations:

a) The persisting fetish of adherence to the doctrine of conservatism and its frequent over application.

b) Dispute and difficulty in arriving at a consensus as regards timing for recognising expense and revenue,

c) Dispute and differences as to the clear-cut distinction between capital and revenue,

d) Extreme crudity and law of minimum of logic in allocating a number of costs over a number of years.

e) Changes in Accounting Policies with prospective and retrospective effects,

f) Delay in recognising incomes but hurry in recognising expense.

g) Matching presupposes an association between expenses and revenues. ‘It necessarily does not follow that all expenses result in revenues. But, it is true that no revenue can be generated without incurring expenses. These basic factors have made it very difficult to find some logical association between expenses and revenues. Any failure to detect such association is bound to introduce arbitrariness in the matching process, because the businessman has to recover money invested by him from sale proceeds. However, this has been mitigated to some extent by classifying costs between product costs and period costs. Direct costs are reported as soon as goods and services are consumed. But they are matched against revenue only when sales take place either in the year of production or afterwards. This match gives rise to conceptual problems. On the other hand, period costs are charged to revenue of the year in which they have been incurred. The logic here is also no sound enough.

h) Taking revenue for the year does usually matching and then expenses incurred for earning such revenues are identified and matched with it. The alternative procedure of identifying expenses for the period and then matching them with the revenue they have produced, has hardly been tried. We come across it in Contract Cost Accounting where the amount of realised profit is estimated on the basis of degree of work done (cost incurred) and certified by the contractee.

This is also not a very sound principle, according to some experts.

4. Disclosure

Apart from legal requirements all significant information should be disclosed. The matching concept states that all significant information should be disclosed and all insignificant information should be disregarded. However, there are no definite rules to separate the two. For recording purposes also only significant events are recorded in detail taking into consideration the cost of detailed record keeping.
Advanced Financial Accounting

The society directly through legislation and indirectly through regulatory bodies cast a duty on the accounting profession to ensure that all financial statements and related books of account and documents are scrupulously correct and that it must ensure that proper disclosure has been made of all material facts. Hence, disclosure leads us to the following basic questions:

a) how to ensure proper adequate disclosure?
b) what is a material fact?

If we study the provisions of the Companies Act, 1956 relating to the preparation of financial statements (Part I, II and III of schedule VI of the Act, specially) along with MAOCARO, 1988, we will realise that the emphasis is one or more disclosure of material facts. Disclosure, therefore, has the following constituents:

a) Break-up details where totals have been reported *prima facie*.
b) Description of each item should be conventional, unless otherwise explained. For example, depreciation should be described as depreciation and not by any unfamiliar description.
c) Disclosure, explanations and remarks should be unambiguous. For example, bad debts should be described as bad debts and not in any clever way to reduce the impact of the expression: Bad Debts.
d) The basis of computation. For example, the basis on which different categories of closing stocks has been valued.
e) Disclosure of Accounting Policy. An Accounting Policy of an organisation deals with the alternative accounting practices and concepts and principles which the particular organisation has selected from among prescribed alternatives. Hence, any change in the Accounting Policy and its impact on the accounts should be properly disclosed. For example, if a company changes its depreciation policy from the SLM to the Reducing Balance Method. The ICAI has attached great importance to it. Hence, ASI deals with Accounting Policy and its disclosure.
f) Some unusual and prior period items should be shown clearly and separately so that current year’s operation result is not impaired.

**Material Fact :** A fact is material in the context of accounting if a person had known the actual fact and not what has been disclosed would have most probably made a different decision. For example, due to several factors, like estimating, every financial statement set is bound to have some degree to Secret Reserve, and Window Dressing. But, when the amount involved exceeds a certain limit, the situation becomes grave, and then the auditor is expected to report upon such secret reserves and window—dressings. Materiality, however, is a relative term. Some are material by nature, others by relative importance.
5. **Materiality**:

The accountant should attach importance to material details and ignore insignificant details. The question what constitutes a material detail is left to the discretion of the accountant. An item is material if there is reason to believe that knowledge of it would influence the decision of the informed investor. This has already been referred to above in connection with Disclosure. In addition to what has already been discussed, the reader is to note the following points:

- **Materiality of information**
- **Materiality of amount**
- **Materiality of procedure**
- **Materiality of nature**

**Materiality of Information**: Misdescription of assets, liabilities, receipts and expenditures. Likewise, wrong classification between Capital and Revenue would also come under this category.

**Materiality of Amount**: This is a highly relative term. A fraud or an error of Rs. 5,000 may be material in a small organisation while not so in a large organisation. Which is why, the Companies Act 1956 and MAOCARO, 1988 have indicated at different places as to the degree (relatively) of tolerance. For example, an item of expense should be shown separately if it constitutes a certain percentage of the total expenses for the period.

**Materiality of Procedure**: Every accountant knows that some procedures are superior to others for certain purposes. For example, the various methods of depreciation, treating liability for gratuity on Cash Basis and on Actuarial Basis, etc.

**Materiality of Nature**: Some items are material by nature regardless of the amount involved and any other factor. A small error in such items will be considered as material always. For example, Director’s Fees, Audit Fees, amount due from directors etc.

5.2 **ACCOUNTING STANDARDS – INTERNATIONAL, US GAAP AND NATIONAL**

**INTERNATIONAL ACCOUNTING STANDARDS**

The International Accounting Standard Committee (IASC) came into existence on June 29, 1973 when sixteen accounting bodies from nine nations (designated as founder members) signed the agreement and constitution for its formation with headquarters at London.

The objective of the committee is "to formulate and publish in the public interest standards to be observed in the presentation of audited financial statements and to promote their worldwide acceptance and observance". This would facilitate flow and communication of financial information and in turn investment. The committee has so far laid down standards regarding the following areas:
### Advanced Financial Accounting

<table>
<thead>
<tr>
<th>IAS NO.</th>
<th>Title</th>
</tr>
</thead>
<tbody>
<tr>
<td>IAS 1</td>
<td>Presentation of Financial Statements (Revised 1997)</td>
</tr>
<tr>
<td>IAS 2</td>
<td>Inventories (Revised 1993)</td>
</tr>
<tr>
<td>IAS 4</td>
<td>Depreciation Accounting (Reformatted)</td>
</tr>
<tr>
<td>IAS 5</td>
<td>Information to be disclosed in financial statements</td>
</tr>
<tr>
<td>IAS 7</td>
<td>Cash Flow Statement (Revised 1992)</td>
</tr>
<tr>
<td>IAS 8</td>
<td>Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies (Revised 1993)</td>
</tr>
<tr>
<td>IAS 9</td>
<td>Research &amp; Development Cost</td>
</tr>
<tr>
<td>IAS 10</td>
<td>Events after the Balance Sheet Date (Revised 1999)</td>
</tr>
<tr>
<td>IAS 11</td>
<td>Construction Contracts (Revised 1993)</td>
</tr>
<tr>
<td>IAS 12</td>
<td>Income Taxes (Revised 1996)</td>
</tr>
<tr>
<td>IAS 13</td>
<td>Presentation of Current Assets and Liabilities</td>
</tr>
<tr>
<td>IAS 14</td>
<td>Segment Reporting (Revised 1997)</td>
</tr>
<tr>
<td>IAS 15</td>
<td>Information reflecting the effects of changes in prices</td>
</tr>
<tr>
<td>IAS 16</td>
<td>Property, Plant &amp; Equipment (Revised 1998)</td>
</tr>
<tr>
<td>IAS 17</td>
<td>Leases (Revised 1997)</td>
</tr>
<tr>
<td>IAS 18</td>
<td>Revenue (Revised 1993)</td>
</tr>
<tr>
<td>IAS 19</td>
<td>Employee Benefits (Revised 1998)</td>
</tr>
<tr>
<td>IAS 21</td>
<td>The Effects of Changes in Foreign Exchange Rates (Revised 1993)</td>
</tr>
<tr>
<td>IAS 22</td>
<td>Business Combinations (Revised 1998)</td>
</tr>
<tr>
<td>IAS 23</td>
<td>Borrowing Costs (Revised 1993)</td>
</tr>
<tr>
<td>IAS 24</td>
<td>Related Party Disclosures (Reformatted 1994)</td>
</tr>
<tr>
<td>IAS 25</td>
<td>Accounting for Investments</td>
</tr>
<tr>
<td>IAS 26</td>
<td>Accounting and Reporting by Retirement Benefit Plans</td>
</tr>
<tr>
<td>IAS 27</td>
<td>Consolidated Financial Statements and Accounting for Investments in Subsidiaries (Reformatted 1994)</td>
</tr>
<tr>
<td>IAS 28</td>
<td>Accounting for Investments in Associates (Revised 1998)</td>
</tr>
<tr>
<td>IAS 29</td>
<td>Financial Reporting in Hyperinflationary Economics (Reformatted 1994)</td>
</tr>
<tr>
<td>IAS 31</td>
<td>Financial reporting of Interests in Joint Ventures (Revised 1998)</td>
</tr>
<tr>
<td>IAS 32</td>
<td>Financial Instruments: Disclosure and Presentation (Revised 1998)</td>
</tr>
<tr>
<td>IAS 33</td>
<td>Earning per share (1997)</td>
</tr>
<tr>
<td>IAS 38</td>
<td>Intangible Assets (1998)</td>
</tr>
<tr>
<td>IAS 39</td>
<td>Financial Instruments; Recognition and Measurement (1998)</td>
</tr>
<tr>
<td>IAS 40</td>
<td>Investment property</td>
</tr>
<tr>
<td>IAS 41</td>
<td>Agriculture</td>
</tr>
</tbody>
</table>
Accounting Principles and Accounting Standards

The International Accounting Standards Committee (IASC) announced in January 1975, the following standards regarding disclosure of fundamental accounting assumptions and policies. Fundamental Accounting Assumptions refer to those accounting standards whose acceptance and use are assumed in the preparation of financial statements.

The fundamental accounting assumptions enumerated by the International Accounting Standards Committee are as follows:

- Going concern,
- Consistency,
- Accrual.

If any of the above accounting assumption is not followed it should be disclosed with reasons. The assumptions already explained are applicable.

International accounting standards are being used as national standards in some developing countries. These standards are also forming the basis of research for national standards.

IASC is permitting alternatives in many areas of reporting practice, but the Board of the IASC believes that the time is ripe to reduce the alternatives. As a step in this direction, the Board set up a Special Steering Committee in March 1987 to find ways of reducing or eliminating alternatives. If all the countries follow the policy as being followed in UK, and some other countries that departures from the international standards be disclosed in the financial statement, international accounting standards will be harmonised throughout the world and the real purpose of developing IAS will be achieved.

The IAASC Board has set up a Standing Interpretation Committee (SIC) to consider on a timely basis accounting issues that are likely to receive divergent or unacceptable treatment in the absence of authoritative guidance. The SIC reviews accounting issues within the context of existing International Accounting Standards and IASC framework. SIC have issued 17 interpretations on various issues such a consistency on different cost formulas for inventories, Introduction to Euro, Primary basis of accounting, alternative methods, etc.

Problem Area: However, there is a problem area. International accounting standards do not have any statutory authority so they do not acquire a compulsiveness associated with legislation. They do not impose any legal obligations on companies preparing financial statements for presentation to the shareholders.

Important IAS are discussed in the Appendix.

US GAAP

During the past 50 years the contribution of the United States to accounting theory has been tremendous. Different committees, associations and institutes have based upon researches conducted, made pronouncements from time to time to develop and improve the principles which are commonly known as Generally Accepted Accounting Principles (GAAP) in the United States. These include broad concepts, guidelines, conventions, rules and procedure at any given time. An underlying structure of concepts, techniques and conventions provides a basis for accounting practice. Three major measurement conventions are realisation,
Advanced Financial Accounting

matching and stable monetary unit. The accrual basis is the heart of accounting whereby revenues are recognized as earned and expenses as incurred rather than as related cash is received or disbursed.

Every business enterprise in USA prepares its financial statements in accordance with the GAAP. The GAAP are guidelines for specific accounting issues, which are to be followed for the preparation of financial statements. These financial statements are audited by the auditors who certify that the financial statements have been prepared in accordance with GAAP.

US GAAP are more prescriptive and detailed than accounting standards in other countries. The volume and complexity of different standards under GAAP is very large as indicated below:

- FASB Interpretations – 44 Nos.
- FASB Technical Bulletins – about 100 Nos.
- Opinions of the Accounting Principle Board
- Research Bulletins of the American Institute of Certified Public Accountants (AICPA) – 51 Nos.
- AICPA Industry Audit and Accounting Guidelines.
- AICPA Statement of position
- AICPA Accounting Interpretations – 30 Nos.

Financial Statements as per US GAAP comprised of income statement, balance sheet, earning per share statement, and statement of shareholders’ equity and cash flow statement. These statements are prepared on consolidated basis for a parent company. Comparative information is provided in the balance sheet for preceding two financial periods and in the income statement, cash flow statement and statement of shareholders’ equity for one preceding financial period.

The balance sheet prepared showing separate classifications of current assets and current liabilities is commonly referred to as classified balance sheet. An enterprise preparing a classified balance sheet shall segregate current assets and current liabilities separately from other assets and liabilities. The current classification applies to those assets, which will be realized in cash, sold or consumed within one year (or operating cycle, if longer) and those liabilities that will be discharged by use of current assets or the creating of other current liabilities within one year (or operating cycle, if longer).

To sum US GAAP requires presenting fairly the results of operation for the period or period under report. Cost of sales and expenses should be appropriately matched against the periodic sales and revenue.

The students are advised to have recourse to the text and study them.
### Accounting Principles and Accounting Standards

#### The Standards at the National Level

The Institute of Chartered Accountants of India and the Institute of Cost and Works Accountants of India are both members of International Accounting Standards Committee. On 22nd April 1977, the Council of The Institute of Chartered Accountants of India established an Accounting Standards Board (ASB). The main function of this Board is to formulate standards with due consideration of the prevalent laws, customs, and business environment.

The ASB has already announced the following standards.

<table>
<thead>
<tr>
<th>AS No.</th>
<th>Title</th>
</tr>
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<tbody>
<tr>
<td>AS–1</td>
<td>Disclosure of Accounting Policies</td>
</tr>
<tr>
<td>AS–2</td>
<td>Valuation of Inventories, (Revised –Mandatory)</td>
</tr>
<tr>
<td>AS–3</td>
<td>Cash Flow Statement</td>
</tr>
<tr>
<td>AS–4</td>
<td>Contingencies and Events Occurring After the Balance Date (Revised –Mandatory)</td>
</tr>
<tr>
<td>AS–5</td>
<td>Net Profit or Loss for the Period, Prior Period and extraordinary Items and Changes in Accounting Policies (Revised –Mandatory)</td>
</tr>
<tr>
<td>AS–6</td>
<td>Depreciation Accounting (Revised)</td>
</tr>
<tr>
<td>AS–7</td>
<td>Accounting for Construction Contracts</td>
</tr>
<tr>
<td>AS–8</td>
<td>Accounting for Research and Development</td>
</tr>
<tr>
<td>AS–9</td>
<td>Revenue Recognition</td>
</tr>
<tr>
<td>AS–10</td>
<td>Accounting for Fixed Assets</td>
</tr>
<tr>
<td>AS–11</td>
<td>Accounting for the Effects of Changes in Foreign Exchange Rates</td>
</tr>
<tr>
<td>AS–12</td>
<td>Accounting for Government Grants (Mandatory)</td>
</tr>
<tr>
<td>AS–13</td>
<td>Accounting for Investments</td>
</tr>
<tr>
<td>AS–14</td>
<td>Accounting for Amalgamations (Mandatory)</td>
</tr>
<tr>
<td>AS–15</td>
<td>Accounting for Retirement Benefits in the Financial Statements of Employers</td>
</tr>
<tr>
<td>AS–16</td>
<td>Borrowing Costs (Mandatory)</td>
</tr>
<tr>
<td>AS–17</td>
<td>Segmental Reporting</td>
</tr>
<tr>
<td>AS–18</td>
<td>Related Party Disclosures</td>
</tr>
<tr>
<td>AS–19</td>
<td>Leases</td>
</tr>
<tr>
<td>AS–20</td>
<td>Earnings Per Share (Mandatory)</td>
</tr>
<tr>
<td>AS–21</td>
<td>Consolidated Financial Statements</td>
</tr>
<tr>
<td>AS–22</td>
<td>Accounting for Taxes on Income</td>
</tr>
<tr>
<td>AS–23</td>
<td>Accounting for Investments in Associates in consolidated Financial Statements.</td>
</tr>
</tbody>
</table>

The accounting standards which have been made mandatory are indicated above in the table.
Compliance with Accounting Standards:

A new sub-section 3A to Section 211 of the Companies Act, 1956 was inserted in 1999. This sub-section requires that every profit and loss account and Balance sheet shall comply with accounting standards. Accounting Standards mean the standards issued by the Institute of Chartered Accountants of India (ICAI) and prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standards (NACAS) constituted under Section 210(a)(1) of the Companies Act, 1956. Until the Central Government prescribes accounting standards under this section, accounting standards issued by the ICAI shall be deemed to be the accounting standards.

NACAS shall consist of the following 12 members:

- A chairman, who shall be a person of eminence well versed in accountancy, finance, business administration, business law, economics or similar discipline;
- One member each nominated by the Institute of Chartered Accountants of India, Institute of Cost & Works Accountants of India and Institute of Company Secretaries of India;
- One representative of the Central Government to be nominated by it;
- One representative of the Reserve Bank of India to be nominated by it;
- One representative of the Comptroller and Auditor General of India to be nominated by him;
- A person whole holds, or has held the office of Professor in accountancy, finance or business management in any University or deemed university;
- The chairman of the Central Board of Direct Taxes, constituted under Central Board of Revenue Act, 1963 or his nominee;
- Two members to represent the chambers of commerce and industry to be nominated by the Central Government;
- One representative of the Securities Exchange Board to be nominated by it.

Deviation from accounting standards:

Section 211(3B) of the Companies Act, 1956 requires that in case the profit and loss account and balance sheet of company do not comply the requirements of the accounting standards, disclosure should be made stating:

a) Deviation from the accounting standards;

b) Reasons for such deviations; and

c) The financial effect, if any, due to such deviations.

It is beyond the scope the Study Notes to include the texts of all such above standards. The students are advised to have recourse to the texts and study them (both International Accounting Standards and National Accounting standards). Some of the standards are discussed in brief as under:
Accounting Principles and Accounting Standards

AS 1: Disclosure of Accounting Policies

The prominent feature of Accounting Standard AS 1 announced by the ASB, regarding disclosure is as follows:

1) Fundamental Accounting Assumptions:
   Certain fundamental accounting assumptions undertake the preparation and presentation of financial statements. They are usually not specifically stated because their acceptance and use are assumed.
   Fundamental accounting assumptions are:
   - going concern
   - consistency
   - accrual.
   If any assumption is not followed the fact should be disclosed.

2) Accounting Policies:
   Accounting policies refer to the specific accounting principles and the methods of applying those principles by enterprises in the compilation and presentation of financial statements. There is not exhaustive list of policies applicable under all circumstances. The varying circumstances under which enterprises operate necessitate the choice of appropriate principles and require considerable expertise of management.
   The following are the areas in which a choice with regard to policy is made by the enterprise:
   - Method of depreciation, depletion and amortisation
   - Treatment of expenditure, during the construction
   - Conversion or translation of foreign currency items,
   - Valuation of inventories
   - Treatment of goodwill
   - Valuation of investments
   - Treatment of retirement benefits
   - Recognition of profit on long-term contracts
   - Valuation of fixed assets
   - Treatment of contingent liabilities.
   This list is not exhaustive.

The objective of the accounting policies is to present 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.

The major considerations while selecting accounting policies are: –
   - Prudence
   - substance over form, and
   - materiality.
To ensure proper understanding of financial statements, all significant accounting policies adopted in the preparation should be disclosed.

The disclosure of the significant accounting policies as such should form a part of the financial statements and the significant accounting policies should normally be disclosed at one place.

Any change in the accounting policy which has material effect in the current period or which will have a reasonable effect in future should be disclosed. In case a change in the current period policy is there the measurable impact should be disclosed on the item concerned. Where the impact is not quantifiable wholly or partially, the fact should be indicated.

The effort of the ASB will therefore definitely improve the financial information presented in the country.

**AS 2 : Valuation of Inventories**

AS 2 HAS BEEN REVISED AND IS MANDATORY IN NATURE. This is effective for the period commencing on or after 1.4.99. As per AS2 inventories should be valued at the lower of cost and net realisable value. The cost of inventories should comprise of all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. The allocation of fixed production overhead in the cost of conversion is to be based on the normal capacity. The following costs are to be excluded from the cost of inventories and recognized as expense in the period of incurrence: -

- a) Abnormal amounts of waste material, labour or other production costs;
- b) storage costs unless those costs are necessary in the production process prior to a further production stage;
  - a) Administrative overheads that do not contribute to bringing the inventories to their present location and condition; and
  - b) Selling and distribution costs.

The cost of inventories should be determined by using FIFO or weighted average formulae. The accounting policy adopted in measuring inventories, cost formula used and total carrying amount of inventories and its classification appropriate to the enterprise shall be disclosed.

**AS 3 : Cash Flow Statements**

This standard provides that an enterprise should present Cash Flow Statement for each period for which financial statements are presented. The cash flow statement should report cash flows during the period classified by operating, investing and financing activities on a net basis. It should also disclose the components of cash and cash equivalents and should present a reconciliation of amounts in its cash flow statements with equivalent items reported in the balance sheet.
This revised standard comes into effect for the accounting period commencing on or after 1.4.1995 and is mandatory in nature. The amount of a contingent loss should be provided for by a charge in the statement of profit and loss if future events will confirm that after taking into accountancy related probable recovery, as asset has been impaired or a liability has been incurred as at the balance sheet date; and a reasonable estimate of amount of loss can be made. The existence of a contingent loss should be disclosed in the financial statements. Contingent gains should not be recognized in the financial statements.

The following information should be provided in the financial statements:

a) the nature of the contingency cover;
b) the uncertainties which may affect the future outcome; and
c) an estimate of the financial effect or a statement that such an estimate cannot be made.

This Standard has been revised and is mandatory in nature. This standard deals with classification and disclosure of extraordinary and prior period items within profit or loss from ordinary activities. It also specifies the accounting treatment for changes in accounting estimates and disclosures to be made in the financial statements regarding changes in accounting policies.

This standard requires that the depreciable amount of a depreciable asset should be allocated on a systematic basis to accounting period during the useful life of the asset. The following information regarding depreciation should be disclosed in the financial statements:

a) the historical cost of each depreciable assets;
b) total depreciation for the period for each class of assets;
c) the related accumulated depreciation;
d) depreciation rates or the useful lives of the assets; and
e) effect of change in depreciation policy.

This statement deals with accounting for construction contracts in the financial statement of the enterprise. Various aspects of AS 7 have been discussed in Study Note 4.

According to the standard, financial statement should disclose :-
Advanced Financial Accounting

(a) the amount of construction work-in-progress;
(b) progress payments received and advances and retentions on account of contracts included in construction work-in-progress; and
(c) the amount receivable in respect of income accrued under cost-plus contracts not included in construction work-in-progress.

If both the percentage of completion method and the completed contract method are simultaneously used by the contract, the amount of contract work described in (i) above should be analysed to disclose separately the amount attributable to contracts accounted for under each method. If accounting policy in this regard is changed, the effect of the change and its amount is to be disclosed in the financial statement.

AS 8 : Research and Development

This standard deals with accounting treatment of research and development. This standard does not apply to:

a) Research and development activities conducted for other under a contract;
b) Exploration for oil, gas and mineral deposits;
c) Research and development activities at the construction stage.

The cost of research and development includes the following:

a) Salaries, wages and other related cost of personnel;
b) costs of materials and services consumed;
c) Depreciation of building, equipment and facilities to the extent they are used for research and development;
d) An appropriate amortisation of cost of building equipment, etc, exclusively used for the project;
e) A reasonable allocation of overhead;
f) Other costs such as amortisation of patents and licences and charges paid to outside bodies for research.

Amount of research and development cost should be charged as an expense of the period in which they are incurred except where such costs may be deferred if criteria are satisfied:

1) the product or process is clearly defined and the costs attributable to future periods or process can be separately identified.
2) technical feasibility of the production or process has been demonstrated;
3) intention to provide and market or use the product or process;
4) there is a reasonable indication that current and future development costs to be incurred on the project together with expected production selling and administration cost is likely to be more than covered by related future revenue.
Accounting Principles and Accounting Standards

5) adequate resources exist or are reasonably expected to be available to complete project and market the product or process.

The total of research and development costs including the amortised portion of deferred costs charged as expense should be disclosed in the profit and loss account of the period. Deferred research and development expenditure should be separately disclosed in the balance sheet under the head Misc. Expenditure.

AS 9 : Revenue Recognition

This standard deals with bases for recognition of revenue in the profit and loss account for revenue arising in the course or ordinary activities of the enterprise from a) the sale of goods; b) the rendering of services; and c) use by others of enterprise resources yielding interest royalties and dividends. It does not apply to following aspects of revenue recognition involving special consideration:

a) Revenue arising from construction contracts;

b) Revenue arising from hire purchase, lease agreements;

c) Revenue arising from Govt grants and other similar subsidies;

d) Revenue of insurance companies arising from revenue contracts.

This also does not apply to :

(a) Realised and unrealised gains in relation to fixed assets;

(b) realised and unrealised gains in relation to current assets;

(c) realised and unrealised gains due to fluctuations in foreign currency;

(d) realised gains resulting from the discharge of an obligation at less than its carrying amount; and

(e) unrealised gains resulting from the restatement of the carrying amount of an obligation.

Various aspect of accounting revenue has been discussed earlier under principles of account and Accounting Standard on Disclosure Policy.

Appendix to the Standard lists various illustrations of revenue recognition and the same may be studied.

Other Accounting standards are AS 10 for Fixed Assets, As 11 Accounting for the effect of changes in Foreign Exchange rates; AS 12 Accounting for Government grants, etc. numbering up to AS 23. The various aspect of AS 14 and AS 23 relating to amalgamation/consolidation of financial statement have been discussed under relevant study note.
5.3 QUESTIONS

1. Explain each of the following concepts/conventions:
   - Money Measurement Concept
   - Business Entity Concept
   - Going Concern Concept
   - Realisation Concept
   - Materiality Concept

2. Distinguish briefly cash basis and accrual basis of accounting. Also discuss the provisions of Companies Act relating to accrual basis of accounting.

3. Discuss the requirement of good design of account.


5. Discuss conventions regarding financial statement and limitations of financial statement.

6. Explain the difference between concepts and conventions.
6.1 ACCOUNTING OF BANKING COMPANIES

Definition of Banking:

Section 5(h) of the Banking Companies Act defines banking as "The accepting for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise and withdrawable by cheque, draft, order or otherwise". Till 1949 there was no special legislation to regulate banking companies but since that year the provisions of Banking Regulation Act and Companies Act, 1956 applies to corporation entities carrying on banking business including the nationalised banks. Section 6 of the Act lays down that in addition to the usual business, the following business may also be carried on by a banking company —

(a) acting as agents for any Government or local authority or any other person or persons,
(b) carrying on and transacting every kind of guarantee and indemnity business, and
(c) undertaking and executing trusts.
Other types of business are prohibited for a banking company. No banking company can directly or indirectly deal in the buying or selling or bartering of goods, except in connection with the realisation of security given to or held by it or engage in any trade or buy or sell or barter goods for others otherwise than in connection with bills of exchange. Immovable property, except that required for its own use, however acquired, must be disposed of within seven years from the date of acquisition.

**Non-banking Assets:**

A bank cannot acquire certain assets but it can always lend against the security of such assets. This means that sometimes, in case of failure on the part of the loanee to repay the loans, the bank may have to take possession of such assets. In that case, the assets will be shown in the balance sheet as "non-banking assets". These must be disposed of within seven years. Income from or profit on sale and loss on sale of such assets has to be separately shown in Profit and Loss Account of the bank.

It may be noted that should the bank lend against such assets as are allowed to be held by a bank, say, government security, it can continue to hold them if the loanee fails to meet his obligations. Such assets cannot be treated as non-banking assets.

**Management:**

The Act has been recently amended by the Banking Regulation (Amendment) Ordinance, 1994 w.e.f. 31st January, 1994. Provision has been made for the appointment of a whole time or part-time Chairman for a banking company in place of only a whole time Chairman earlier. However, where a chairman is appointed on a part time basis, the management of the whole of the affairs of the banking company shall be entrusted to a Managing Director.

The Reserve Bank of India has the power to order the removal of a director or the chairman.

**Minimum Share Capital and Reserve:**

Section 11 lays down the following as the minimum limit of paid-up capital & reserves:

(a) Banking companies incorporated outside India :-

If it has places of business in Bombay or Calcutta Rs. 20 lakhs

If the places of business are elsewhere Rs.15 lakhs

Further every year 20% of the profits earned in India must be added to the sums specified above.

The sum must be kept deposited with the Reserved Bank either in cash or in the form of unencumbered securities.
Banking companies incorporated in India :-

(i) If the places of business are in more than one State and if any places of business are in Bombay or Calcutta.

Rs. 10 lakhs

(ii) If the places of business are in more than one State but none of the places of business are in Bombay or Calcutta

Rs. 5 lakhs

(iii) If the places of business are only in one State, none of the places of business being in Bombay or Calcutta

Rs. 10 lakhs

for the principal place plus

Rs. 10,000 for each additional place of business in the same district and

Rs. 25,000 for a place of business outside the district.

The total need not exceed Rs. 5 lakhs, or Rs. 50,000 in case there is only one place of business.

But companies which commence business after the commencement of the Banking (Companies) Amendment Act of 1962, a minimum of rupees five lakhs is required.

(iv) If the places of business are only in one State and if the place of business are also in Bombay, or Calcutta.

Rs. 5 lakhs plus.

for each place of business situated outside Bombay, and Calcutta. The total need not exceed Rs. 10 lakhs.

Banking companies carrying on business in India must see to it that :-

(a) the subscribed capital is not less than half the authorised capital;
(b) the paid up capital is not less than half the subscribed capital; and
(c) the capital of the company consists only of ordinary or equity shares and such preference shares as may have been issued before July 1, 1964.

A shareholder cannot exercise more than ten percent of the total voting rights of the company. This was increased from 1% to 10% by Banking Regulation Amendment Ordinance, 1994 w.e.f 31st January, 1994. A chairman, managing director or chief executive of a banking
company must declare his full holdings in the capital of the company. Underwriting commission or brokerage or discount on shares issued by a banking company cannot exceed 2.5 % of the paid up value of the shares. A charge on unpaid capital cannot be created. No dividend can be declared unless expenses not represented by tangible assets have been completely written off. The limits as to share capital given above were fixed a long time back. These limits have been found to be quite inadequate. In order to strengthen the capital base of the banks, the Reserve Bank on the recommendations of the Narasimhan Committee introduced in April, 1992 risk weighted asset ratio system. According to the system, paid-up capital and reserves of a bank (after writing off bad debts) should form an adequate percentage of the assets of the bank, their investment, loans and advances. All these items have been assigned weights according to the prescribed risk. Ratio so computed is known as capital adequacy ratio. All banks operating in India should have 8% latest by, March, 1996.

Moreover, the Reserve Bank has now finally, decided to allow private banks to be set up after almost 20 years of nationalisation of banks. Such a private bank shall be registered as a public limited company under the Companies Act, 1956 and shall have a minimum paid up capital of Rs. 100 crores.

Floating Charge:
Section 14 A lays down that a banking company shall not create a floating charge on the undertaking or any property of the company or any part thereof except upon a certificate from the Reserve Bank that such a charge is not detrimental to the interests of the depositors of the company. A floating charge created without such a certificate in invalid. A charge on uncalled capital is invalid.

Restrictions on Dividend :
According to Section 15, a banking company cannot pay dividends unless all of its capitalised expenses (including preliminary expenses, share selling commission, brokerage, amount of losses incurred and any other item of expenditure not represented by tangible assets) have been completely written off.

But a banking company need not -

(a) write off depreciation in the value of its investments in approved securities in any case where such depreciation has not actually been capitalised or otherwise accounted for as a loss;
(b) write off depreciation in the value of its investments in shares, debentures, or bonds (other than approved securities) in any case where adequate provision for such depreciation has been made to the satisfaction of the auditor;
(c) write off bad debts in any case where adequate provision for such debts has been made to the satisfaction of the auditors of the banking company.
Statutory Reserve:
Section 17 of the Act lays down that at least 20% of the profits prior to declaration of dividend must be transferred to the Reserve Fund. It is only with the permission of the Reserve Bank that a bank can stop such transfer. The Reserve Fund thus built up should be shown separately from other reserves.

Cash Reserves (Section 18):
A scheduled bank (i.e. a bank included in the schedule maintained by the Reserve Bank of India) has to maintain with the Reserve Bank a balance equal to 3% of its time liabilities (i.e. deposits received for fixed terms) as well as of its demand liabilities. The Reserve Bank has the power to increase the percentage to 20% by a notification in the office gazette. Every non-scheduled bank is also required to maintain in India by way of cash reserve with itself or in any current account opened with the Reserve Bank of India or State Bank of India or partly in cash with itself and partly in such accounts a sum equivalent to at least 3% of the total of its time and demand liabilities in India.

Statutory Liquidity Ratio (SLR):
Over and above the cash reserve, every banking company is required to maintain in India in cash, gold and unencumbered securities, an amount which shall not be less than 25 percent of its time and demand liabilities in India. This is known as "Statutory Liquidity Ratio" or SLR. The Reserve Bank has the power to increase this ratio up to 40 percent. It now stands at 33.75% w.e.f. September 17, 1994. The Reserve Bank has decided to gradually reduce it to 25% over a three years period.

Restrictions on Loans and Advance:
After the amendment of the law in 1968, a bank cannot: (i) grant loans or advances on the security of its own shares, and (ii) grant or agree to grant a loan or advance to or on behalf of (a) any of its directors (b) any firm in which any of its directors is interested as partner, manager or guarantor; (c) any company of which any of its director is a director, manager, employee or guarantor or in which he holds substantial interest, or (d) any individual in respect of whom any of its directors is a partner or guarantor.

Note: (ii) (c) does not apply to subsidiaries of the banking company, registered under section 25 of the Companies Act or a government company.

Subsidiary Companies:
A banking company is allowed to form subsidiary companies only for the purpose of (a) undertaking and executing trusts, (b) the undertaking of the administration of estates as executors, trustee or otherwise, (c) the providing of safe deposit vaults; and (d) such other purposes as are incidental to the business of banking with the permission of the Reserve Bank.
Advanced Financial Accounting

Control:

The Reserve Bank of India is now authorised to exercise general supervision on the working of banks and to conduct investigation into the affairs of any bank. The Reserve Bank may order a bank not to accept further deposits. Every bank has to obtain a license from the Reserve Bank and permission to open a branch.

Accounting Record In The Books Of Bank:

In the book of bank, accounting record is made according to Slip System. Following books are mostly used in Bank accounting:

1. General Cash Book;
2. Sectional Cash Book;
3. Customer's Receipts Book;
4. Counter Payment Books;
5. Cash Balance Books;
6. Bills Payable Register;
7. Bills Discounting Register;
8. Transfer Journal;
9. General Ledger;
10. Current Account Ledger;
11. Saving Account Ledger;
12. Fixed Deposits Ledger;
13. Investment Ledger;
14. Loan Ledger;
15. Safe Deposits Vault Register;
16. Bills Register;
17. Securities Register.

Slip System:

Double entry system of Book-Keeping is adopted in a bank. For accounting Slip System is very popular in banks. Records in accounting books are made only on the basis of slips. When a person deposits amount in a bank, he has to fill in pay-in-slip. The concerned officer signs on its counterfoil and returns it back to the person concerned. The portion of pay-in-slip which is retained by the officer is sent to the cashier. Cashier makes record in the cash book in its basis. From cashier this slip is sent to ledger-keeper. There customer's account is credited on the basis of this slip. Ledger-keeper sends this slip to the clerk who makes entries in the Pass Book. This method is also adopted for transferring the amount from one account to another. Slip system of accounting is also called Unit Media of Posting.
**Final Accounts of Banking Companies - Preparation of Profit and Loss Account**

The Profit & Loss Account of a banking company has to be prepared in Form B of Schedule III, attached to the Banking Regulation Act. As stated earlier the form has been revised w.e.f. 1st April, 1992 and the Profit & Loss Account of a banking company for the year ending March 31, 1991, and onwards has to be prepared in the prescribed new form as given below:

**FORM 'B'
THIRD SCHEDULE
FORM OF PROFIT AND LOSS ACCOUNT**

Profit & Loss Account for the year ended 31st March, 19...

<table>
<thead>
<tr>
<th>Schedule No.</th>
<th>Current year</th>
<th>Previous year</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. INCOME:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest Earned</td>
<td>13</td>
<td>—</td>
</tr>
<tr>
<td>Other Income</td>
<td>14</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. EXPENDITURE:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest Expended</td>
<td>15</td>
<td>—</td>
</tr>
<tr>
<td>Operating Expenses</td>
<td>16</td>
<td>—</td>
</tr>
<tr>
<td>Provision and Contingencies</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. PROFIT/LOSS:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net Profit / (Loss) for the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>IV APPROPRIATIONS:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transfer to Statutory Reserves</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Transfer to other Reserves</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Transfer to Govt./Proposed Dividend</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Balance carried over to Balance Sheet</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

*Notes:*

(a) Total income includes income of foreign branches at Rs. ____
(b) Total expenditure includes expenditure of foreign branches at Rs. ____
(c) Surplus/Deficit of foreign branches at Rs. ____
Advanced Financial Accounting

Schedules to be annexed with Profit and Loss Account

**SCHEDULE 13: INTEREST EARNED**

<table>
<thead>
<tr>
<th></th>
<th>Current year</th>
<th>Previous year</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Interest Discount on Advances/Bills</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Income on Investments</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. Interest on balances with RBI and other inter-bank funds</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>IV. Others</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

**SCHEDULE 14: OTHER INCOME**

<table>
<thead>
<tr>
<th></th>
<th>Current year</th>
<th>Previous year</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Commission, Exchange, Brokerage</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Profit on sale of investments</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><em>Less:</em> Loss on sale of Investments</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. Profit on revaluation of Investments</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><em>Less:</em> Loss on Revaluation of Investments</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>IV. Profit on Sale of Land/Building and other Assets</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><em>Less:</em> Loss on sale of land, Bldg. &amp; other Assets</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>V. Profit on Exchange transactions</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><em>Less:</em> Loss on Exchange transactions</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>VI. Income earned by way of dividends etc. from subsidiaries/companies and/or joint ventures/abroad/in India</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>VII. Misc. Income</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

*Note:* Under Item II to V loss figures may be shown in brackets.

**SCHEDULE 15: INTEREST EXPENDED**

<table>
<thead>
<tr>
<th></th>
<th>Current year</th>
<th>Previous year</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Interest on Deposits</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Interest on RBI/Inter-bank Borrowings</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. Others</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>
Banking, Electricity, Insurance and Consequential Loss

SCHEDULE 16: OPERATING EXPENSES

| I. Payments to and Provisions for Employees | — | — |
| II. Rent, Taxes and Lighting | — | — |
| III. Printing and Stationery | — | — |
| IV. Advertisement and Publicity | — | — |
| V. Depreciation on Bank's Property | — | — |
| VI. Directors' Fees, Allowances & Expenses | — | — |
| VII. Auditors' Fees and Expenses (Including Branch Auditors) | — | — |
| VIII. Law Charges | — | — |
| IX. Postages, Telegrams, Telephones etc. | — | — |
| X. Repairs and Maintenance | — | — |
| XI. Insurance | — | — |
| XII. Other Expenditure | — | — |
| TOTAL | — | — |

Note: Corresponding figures for the immediately preceding financial year should be shown in separate columns.

COMMENTS ON PROFIT AND LOSS ACCOUNT ITEMS:

(A) Interest Earned (Schedule 13)

I. Interest/Discount on Advances/Bills: Includes interest and discount on all types of loans and advances like cash credit, demand, loans, overdrafts, export loans, term loans, domestic and foreign bills purchased and discounted, (including those rediscounted), overdue interest and also interest subsidy, if any, relating to such advances/bills.

II. Income on Investments: Includes all income derived from the investment portfolio by way of interest and dividend.

III. Interest on Balances with Reserve Bank of India and other Inter-bank Funds: Includes interest on balance with Reserve Bank and other banks, call loans, money market placement, etc.

IV. Others: Includes any other interest/discount income not included in the above heads.

(B) Other Income (Schedule 14):

I. Commission, Exchange and Brokerage: Includes all remuneration on services such as collections, commission/exchange on remittances and transfers, commission on letters of credit, letting out of lockers and
guarantees, commission on Government Business, commission on other permitted agency, business including consultancy and other services, brokerage, etc. on securities. It does not include foreign exchange income.

II. Profit on Sale of investments; Less: Loss on Sale of Investments;

III. Profit on Revaluation of Investments; Less: Loss on Revaluation of Investments;

IV. Profit on Sale of Land, Buildings and Other Assets; Less: Loss on sale of land, buildings and other assets. Includes profit/loss on sale of securities, land and buildings, motor vehicle, gold, silver etc. Only, the net position should be shown. If the net position is a loss, the amount should be shown as a deduction. The Net Profit/ Loss on revaluation of assets may also be shown under this item

V. Profit on Exchange transactions; Less: Loss on Exchange Transactions: Includes profit / loss on dealing in foreign exchange, all income carried by way of foreign exchange, commission and charges on foreign exchange transactions excluding interest which will be shown under interest. Only the net position should be shown. If the net position is a loss, it is to be shown as a deduction.

VI. Income earned by way of dividends etc. from subsidiaries, companies, joint ventures abroad/in India.

VII. Miscellaneous Income: Includes recoveries from constituents for godown rents, income from bank's properties, security charges, insurance etc. and any other miscellaneous income. In case any item under this head exceeds one percentage of the total income, particulars may be given in the notes.

(C) Interest Expended (Schedule 15):

I. Interest on Deposits: Includes interest paid on all types of deposits including deposits from banks and other institutions.

II. Interest on RBI/Inter-Bank borrowings: Includes discount/interest on all borrowings and refinancing from Reserve Bank of India and other banks.

III Others: Includes discount/interest on all borrowings/refinancing from financial institutions. All other payments like interest on participation certificates, penal interest paid, etc. may also be included here.

(D) Operating Expenses (Schedule 16):

I. Payments to and Provisions for employee: Includes staff salaries/wages, allowances, bonus, other staff benefits like provident fund, pension, gratuity, liveries to staff, leave fare concessions, staff welfare, medical allowance to staff etc.
II. **Rent, Taxes and Lighting:** Including rent paid by the banks on building and other municipal and other taxes paid (excluding income tax and interest tax) electricity and other similar charges and levies. House rent allowance and other similar payments to staff should appear under the head "Payments to and Provisions for Employees."

III. **Printing & Stationery:** Includes books and forms and stationery used by the bank and other printing charges which are not incurred by way of publicity expenditure.

IV. **Advertisement and Publicity:** Includes expenditure incurred by the bank for advertisement and publicity purposes including printing charges of publicity matter.

V. **Depreciation on Bank's Property:** Includes depreciation on bank's own property, motor cars and other vehicles, furniture, electric fittings, vaults, lifts, leasehold properties, non-banking assets, etc.

VI. **Directors Fees, Allowances and Expenses:** Includes sitting fees and all other items of expenditure incurred on behalf of directors. The daily allowance, hotel charges, conveyance charges, etc. which though in the nature of reimbursement of expenses incurred may be included under this head. Similar expenses of Local Committee members may also be included under this head.

VII. **Auditors' Fees & Expenses (including branch auditors' fee and expenses):** Includes the fee paid to the statutory auditors and branch auditors for professional services rendered and all expenses for performing their duties, even though they may be in the nature of reimbursement of expenses. If external auditors have been appointed by banks themselves for internal inspection and audits and other services, the expenses incurred in that context including fees may not be included under this head but shown under 'other expenditure'.

VIII. **Law Charges:** All legal expenses and reimbursement of expenses incurred in connection with legal services are to be included here.

IX. **Postage, Telegraphs, Telephones, etc.** Includes insurance charges on bank's property, their maintenance charges, etc.

X. **Repairs and maintenance:** Includes insurance charges on bank's property, their maintenance charges etc.

XI. **Insurance:** Includes insurance charges on bank's property, insurance premium paid to Deposit Insurance & Credit Guarantee Corporation (DICGC) etc. to the extent they are not recovered from the concerned parties.

XII. **Other Expenditure:** All expenses other than those not included in any of the other heads, like license fees, donations, subscriptions to papers, periodicals, entertainment expenses, travel expenses, etc. may be included under this head. In case any particular item under this head exceeds one percentage of the total income particulars may be given in the notes.
(E) **Provisions and Contingencies : (Form B)**

Includes any provision made for bad and doubtful debts, provisions for taxation, provisions for diminution in the value of investments, transfers to contingencies and other similar items.

**PREPARATION OF BALANCE SHEET:**

The Balance Sheet of a banking company has to be prepared in Form A of Schedule III attached to the Banking Regulation Act. The form of balance sheet, as stated earlier, has been revised w.e.f. April 1, 1991. The Balance Sheet of a banking company has to be prepared in the prescribed new form for the year ending 31st March, 1992 and onwards as given below:

**THE THIRD SCHEDULE: FORM ‘A’**

**FORM OF BALANCE SHEET**

Balance Sheet as on 31st March.....

<table>
<thead>
<tr>
<th>Schedule</th>
<th>Current year Rs.</th>
<th>Previous year Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>CAPITAL &amp; LIABILITIES</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Reserves and Surplus</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Deposits</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Borrowings</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>Other Liabilities and Provisions</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ASSETS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and Balance with RBI</td>
<td>6</td>
<td></td>
</tr>
<tr>
<td>Balance with banks &amp; Money at Call &amp; Short Notice</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>Investments</td>
<td>8</td>
<td></td>
</tr>
<tr>
<td>Advances</td>
<td>9</td>
<td></td>
</tr>
<tr>
<td>Fixed Assets</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>Other Assets</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contingent Liabilities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bills for Collection</td>
<td>12</td>
<td></td>
</tr>
</tbody>
</table>

The following schedules are required to be furnished with the Balance Sheet.
### SCHEDULE 1 : CAPITAL

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>I. NATIONALISED BANKS:</strong></td>
<td></td>
</tr>
<tr>
<td>Capital (Fully owned by Central Government)</td>
<td>—</td>
</tr>
<tr>
<td>(a) FOR BANKS INCORPORATED OUTSIDE INDIA:</td>
<td></td>
</tr>
<tr>
<td>(i) Capital (the amount brought in by banks by way of start-up capital as prescribed by RBI should be shown under this head)</td>
<td>—</td>
</tr>
<tr>
<td>(ii) Amount of Deposit kept with RBI under Section 11(2) of the Banking Regulation Act, 1949.</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>—</td>
</tr>
<tr>
<td><strong>III. FOR OTHER BANKS:</strong></td>
<td></td>
</tr>
<tr>
<td>Authorised Capital (shares of Rs each)</td>
<td>—</td>
</tr>
<tr>
<td>Issued Capital (shares of Rs each)</td>
<td>—</td>
</tr>
<tr>
<td>Subscribed Capital (shares of Rs each)</td>
<td>—</td>
</tr>
<tr>
<td>Called up Capital (shares of Rs. each)</td>
<td>—</td>
</tr>
<tr>
<td>Less: Calls unpaid</td>
<td>—</td>
</tr>
<tr>
<td>Add: Forfeited Shares</td>
<td>—</td>
</tr>
</tbody>
</table>

### SCHEDULE 2 : RESERVES AND SURPLUS

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>I. Statutory Reserves:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening Balance</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Additions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Deductions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>II. Capital Reserves:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening Balance</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Additions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Deductions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>III. Share Premium</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening Balance</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Additions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Deductions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>IV. Revenue and Other Reserves</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening Balance</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Additions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Deductions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>V. Balance in Profit &amp; Loss Account:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>TOTAL (I + II + III + IV + V)</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>
### SCHEDULE 3: DEPOSITS

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. I. Demand Deposits</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) From Banks</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) From Others</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Savings Bank Deposits</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. Term Deposits:</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) From Banks</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) From Others</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL (I, II &amp; III)</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

B. (i) Deposits of Branches in India | —   | —   |
| (ii) Deposits of Branches Outside India | —   | —   |
| TOTAL | —   | —   |

### SCHEDULE 4: BORROWINGS

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Borrowings in India.</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) Reserve Bank of India</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) Other Banks</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(iii) Other Institutions and Agencies</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Borrowings Outside India</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL (I and II)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Secured Borrowing in 1, II above</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

### SCHEDULE 5: OTHER LIABILITIES & PROVISIONS

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Bills Payable</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Inter-office Adjustments (net)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. Interest Accrued</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>IV Other (including Provisions)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>
Banking, Electricity, Insurance and Consequential Loss

**SCHEDULE 6 : CASH AND BALANCE WITH RBI**

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Cash in Hand (including foreign currency notes)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Balances with RBI in:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(i) In Current Account</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) In Other Accounts</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL (I &amp; II)</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

**SCHEDULE 7 : BALANCE WITH BANKS & MONEY AT CALL AND SHORT NOTICE**

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. In India</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) Balance with Banks</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) in Current Accounts</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(b) in Other Deposit Accounts</td>
<td></td>
<td>—</td>
</tr>
<tr>
<td>(ii) Money at Call &amp; Short Notice</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(a) With Banks</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(b) With other Institutions</td>
<td></td>
<td>—</td>
</tr>
<tr>
<td>TOTAL (I &amp; II)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Outside India</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) In Current Accounts</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) In other Deposit Accounts</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(iii) Money at Call and Short Notice</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Grant Total (I &amp; II)</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

**SCHEDULE 8 : INVESTMENTS**

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Investments in India in Rs.</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) Govt. Securities</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) Other Approved Securities</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(iii) Shares</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(iv) Debentures and Bonds</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(v) Subsidiaries and/or Joint Ventures</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Other (to be specified)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Investments outside India in</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) Govt. Securities (incl. local authorities)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) Subsidiaries and/or Joint Ventures abroad</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(iii) Other Investment (to be specified)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>GRAND TOTAL</strong></td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>
### SCHEDULE 9: ADVANCES

<table>
<thead>
<tr>
<th>A.</th>
<th>Bills Discounted and Purchased</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Cash Credits, Overdrafts and Loans repayable on Demand</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Term Loans</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>B.</td>
<td>Secured by Tangible Assets</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Covered by Bank/Govt. Guarantees</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Unsecured</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>C. I.</td>
<td>Advances in India:</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Priority Sectors</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Public Sector</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Banks</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Others</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II.</td>
<td>Advances Outside India:</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Due from Banks</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Due from Others:</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Bills purchased and discounted</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Syndicated Loans</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td></td>
<td>Others</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

**GRAND TOTAL (C. I and C. II)**

### SCHEDULE 10: FIXED ASSETS

<table>
<thead>
<tr>
<th>I. Premises:</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>At cost as on 31st March of the preceding year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Additions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Deductions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Depreciation to date</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>II. Other Fixed Assets (incl. Furniture &amp; Fixture):</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>At cost as on 31st March of the preceding year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Additions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Deductions during the year</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Depreciation to date</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>TOTAL (I &amp; II)</td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>
Banking, Electricity, Insurance and Consequential Loss

### SCHEDULE 11: OTHER ASSETS

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Inter-office Adjustments (net)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Interest Accrued</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. Tax paid in Advance/Tax Deducted at Source</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>IV. Stationery and Stamps</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>V. Non-banking Assets acquired in satisfaction of claims</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>VI. Others (in case there is any unadjusted balance of loss. The same may be shown under this item with appropriate footnote)</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>

### SCHEDULE 12: CONTINGENT LIABILITIES

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Claims against the Bank not acknowledged as debts</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>II. Liability for part paid Investments</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>III. Liability on account of outstanding forward exchange contracts</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>IV. Guarantees given on behalf of constituents</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(i) In India</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(ii) Outside India</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>V. Acceptances, Endorsements and other Obligations</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>VI. Other items for which the bank is contingently liable</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>—</td>
<td>—</td>
</tr>
</tbody>
</table>
COMMENTS ON BALANCE SHEET ITEMS:

1. **Capital (Schedule 1)**

   (I) **Nationalised Banks:**

   (a) **Capital (fully owned by Central Government):** The capital owned by Central Government as on the date balance sheet including contribution from Government, if any, for participating in World Bank Projects should be shown.

   (b) **Banking Companies incorporated outside India:**

      (i) The amount brought in by banks by way of start-up capital as prescribed by RBI should be shown under this head.

      (ii) The amount of deposit kept with RBI, under sub-section 2 of section II of the Banking Regulation Act. 1949 should also be shown.

   (II) **Other Banks (Indian)**

      Authorised, Issued, Subscribed, Called-up Capital should be given separately. Calls-in-arrears will be deducted from Called up capital while the paid-up value of forfeited shares should be added thus arriving at the paid-up capital. Where necessary, items which can be combined should be shown under one head for instance 'Issued and Subscribed Capital'.

   *Note:* The changes in the above items, if any, during the year, say, fresh contribution made by Government, fresh issue of capital, capitalisation of reserves, etc. may be explained in the notes.

2. **Reserves & Surplus (Schedule 2)**

   I. **Statutory Reserves:** Reserves created in terms of Section 17 or any other section of Banking Regulation Act must be separately disclosed.

   II. **Capital Reserves:** The expression 'Capital Reserves' shall not include any amount regarded as free for distribution through the Profit & Loss Account. Surplus on revaluation should be treated Reserve. Surplus on translation of the financial statements of foreign branches (which includes fixed assets also) is not a revaluation reserve.

   III. **Share Premium:** Premium on issue of share capital may be shown separately under this head.

   IV. **Revenue and Other Reserves:** The expression 'Revenue Reserve' shall mean any reserve other than capital reserve. This items will include all reserves, other than those separately classified. The expression 'reserve' shall not include any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets or retained by way of providing for any known liability.

   V. **Balance of Profit:** Includes Balance of Profit after appropriations. In case of loss the balance may be shown as a deduction.

   *Note:* Movement in various categories of reserves should be shown as indicated in the schedule.
3. Deposits (Schedule3):
   A. I. Demand Deposits :
      (i) From Banks:
      (ii) From Others: Includes all bank deposits repayable on demand. Includes all demand deposits of the non-bank sectors. Credit balance in overdrafts, cash credit account, deposits, payable at call, overdue deposits, inoperative current accounts, matured time deposits and cash certificates, certificates of deposits, etc. are to be included under this category.

   A. II. Savings Bank Deposits :
      Includes all savings bank deposits (including inoperative savings bank accounts),

   A. III. Term Deposits
      (a) From Banks: Includes all types of bank deposits repayable after a specified term.
      (b) From Others: Includes all types of deposits of the non-bank sector repayable after a specified term. Fixed deposits, cumulative and recurring deposits, cash certificates, certificates of deposits, annuity deposits, deposits mobilised under various schemes, ordinary staff deposits, foreign currency non-resident deposits accounts, etc. are to be included under this category.

   B. (I) Deposits of Branches in India, and
      (II) Deposits of Branches outside India :
      The total of these two items will agree with the total deposits.

Notes: A. Interest payable on deposits which is accrued but not due should not be included but shown under other liabilities.
B. Matured time deposits and cash certificates, etc. should be treated as demand deposits.
C. Deposits under special schemes should be included under term deposits if they are not payable on demand. When such deposits have matured for payment they should be shown under demand deposits.
D. Deposits from banks will include deposits from the banking system in India. Cooperative banks, foreign banks which may or may not have a presence in India.

4. Borrowings (Schedule 4)
   I. Borrowings in India:
      (a) Reserve Bank of India: Includes borrowings / refinance obtained from Reserve Bank of India.
Advanced Financial Accounting

(b) Other Banks: Includes borrowings / refinance obtained from commercial banks (including cooperative banks).

(c) Other Institutions and Agencies: Includes borrowing / refinance obtained from Industrial Development bank of India, Export-Import bank of India, national Bank for Agriculture and Rural Development and other institutions, agencies (including liability against participation certificates, if any).

II. Borrowings outside India:

Includes borrowings of India branches abroad as well as borrowing of foreign branches.

Secured borrowing included above. This item will be shown separately.

Includes secured borrowings / refinance in India and outside India.

Notes:

(i) The total of I & II will agree with the total borrowings shown in the Balance Sheet.

(ii) Inter-office transactions should not be shown as borrowings.

(iii) Funds raise by, foreign branches by way of certificate of deposits, bonds etc. should be classified depending upon documentation, as "deposits" "borrowings",

(iv) Refinance obtained by banks from Reserve Bank of India and various Institutions are being brought under the head 'borrowings'. Hence, advances will be shown at the gross amount on the assets side.

5. Other Liabilities & Provisions (Schedule 5):

I. Bill Payable:

The bank provide the facility of remitting funds from one place to another by means of bank drafts, telegraphic transfer, circular notes, pay orders etc. The person intending to remit the money has to deposit the money with the bank and get a pay order or bank draft in exchange for the money deposited. Alternatively, he may request the bank for making a telegraphic transfer from his account to the account of the person to whom he wants to remit the money. The paying bank is reimbursed by the bank who issues such draft or instructions. The banks also issues travellers and gift cheques for carrying or remitting money. If any such drafts, cheques etc. remain uncashed on the day of preparation of final accounts, they are shown under the heading "Bills Payable" in the balance sheet.

A. Inter Office (or Branch) Adjustments (Net): This item represents the difference on account of incomplete recording of transactions between one branch and another branch or between one branch and the head office. It may have a debit or a credit balance. In case of a credit balance, it should be shown under this head. It may be noted that only net portion is to be shown of inter office account, inland as well as foreign.
B. **Interest Accrued:** Includes interest accrued but not due on deposits and borrowings.

C. **Others (Including Provisions):** Includes net provision for income tax and other taxes like interest tax (less advance payment, tax deducted at source, etc.), surplus in aggregate in provisions for bad debts provision account, surplus in aggregate in provisions for depreciation in securities, contingency funds which are not disclosed as reserves but are actually in the nature of reserves, proposed dividend / transfer to Government, other liabilities which are not disclosed under any of the major heads such unclaimed dividend provisions and funds kept for specific purposes, unexpired discount, outstanding charges like rent, conveyance, etc. Certain types of deposits like staff security deposits, margin deposits, etc. where the repayment is not free, should also be included under this head.

**Notes:**

(i) For arriving at the net balance of inter-office adjustments all connected inter office account should be aggregated and the net balance only will be shown, representing mostly, items in transit and unadjusted items.

(ii) The interest accruing on all deposits, whether the payment is due or not, should be treated as liability.

(iii) It is proposed to show only pure deposits under this head 'deposits' and hence all surplus provisions for bad and doubtful debts contingency funds, Secret reserves, etc. which are not netted off against the relative assets, should be brought under the head 'Other (including provision)'.

6. **Cash and Balance with the Reserve Bank of India (Schedule 6):**

   I. **Cash in hand (including foreign currency notes);**

   II. **Balance with RBI**

      (a) in current account,

      (b) in other accounts.

      Includes cash in hand including foreign currency notes and also of foreign branches in the case of banks having such branches.

7. **Balances with Banks and Money at Call and Short Notice (Schedule 7):**

   I. **In India:**

      a. **Balance with Banks :**

         (a) **Current Accounts.**

         (b) **In other Deposit Accounts :** including all balances with banks in India (including cooperative banks). Balances in current account and deposit accounts should be shown separately.
b. **Money at call and short notice:**

(i) *With Banks;*

(ii) *With Other Institutions.* This item mainly represents the loans given by one bank to another for a short period. Call loans are repayable at any time the banker recalls them while short notice advances are repayable within a short notice of (say) 24 hours. The maximum notice period is usually of two weeks.

This includes deposits repayable within 15 days or less than 15 days notice lent in the inter-bank call money market.

II. **Outside India:**

(i) *Current Accounts* and

(ii) *Deposits Accounts:* Includes balances held by foreign branches and balance held by Indian Branches of the banks outside India. Balance held with foreign branch and by other branches of the bank should not be shown under this head but should be included in inter-branch account. The amounts held in ‘current account’ should be shown separately.

(iii) *Money at Call and Short Notice:* Includes deposits usually classified in foreign currencies as money at call and short notice.

8. **Investments (Schedule 8):**

1. **Investments in India in**

   (i) *Government Securities:* Includes Central and State Government securities and government treasury bills. These securities should be shown at the book value. However, the difference between the book value and market value should be given in the notes to the balance sheet.

   (ii) *Other Approved Securities:* Securities other than Government Securities which according to the Banking Regulation Act, 1949 are treated as approved securities, should be included here.

   (iii) *Shares:* Investments in shares of companies and corporations not included in item (ii) above should be included here.

   (iv) *Debentures and Bonds:* Investments in debentures and bonds of companies and corporations not included in items (ii) should be included here.

   (v) *Investments in Subsidiaries/Joint Ventures:* Investments in Subsidiaries/Joint Ventures (including RRBs) should be included here.

   (vi) *Others:* Includes residual investment, if any, like gold, commercial paper and other instruments in the nature of share/debentures/bonds.
Banking, Electricity, Insurance and Consequential Loss

II. Investments outside India -

(i) Government Securities (including local authorities): All foreign Government securities including securities issued by local authorities may be classified under this head.

(ii) Subsidiaries and/or joint ventures abroad: All investments made in the share capital of subsidiaries floated outside India and/or joint ventures abroad should be classified under this head.

(iii) Others: All other investments outside India may be shown under this head.

9. Advances (Schedule 9):

A.

(i) Bills discounted and purchased. The banks also give advances to their customers by discounting their bills. Net amount after deducting the amount of discount is credited to the account of customer. The bank may discount the bills with or without any security from the debtor in addition to one or more persons already liable on the bill.

(ii) Cash Credits, Overdrafts and Loans repayable on demand:

Cash Credits. A cash credit is an arrangement by which a banker allows his customer to borrow money up to a certain limit. Cash credit arrangements are usually made against the security of commodities hypothecated or pledged with the bank.

In case of a cash credit facility the borrower need not borrow at once the whole of the amount he is likely to require, but draw such amounts as and when required. He can put back any surplus amount which he may find with him for the time being. Interest on cash credit has to be paid on the amount actually drawn at any time and not on the full amount of credit allowed overdrafts. The customer may be allowed to overdraw his current account with or without security if he requires temporary accommodation. This arrangement like cash credit is advantageous from the customer's point of view as he is required to pay interest on the actual amount used by him.

Loans. A loan is a kind of advance made with or without security. In case of loan the bank makes a lump sum payment to the borrower or credits his deposit account with the money advanced. Repayments may be made in instalments or at the expiry of a certain period. The customer has to pay interest on the total advance whether he withdraws the money from his account (credited with the loan). A loan once repaid in full or in part cannot be drawn again by the borrower unless the banker sanctions a fresh loan.
(iii) **Terms Loans:** A loan may be in the form of a demand loan. Demand loan is payable on demand. It is usually for a short period not exceeding a year, while the term loan is given for a fixed term usually exceeding a year.

In classification under section 'A' all outstanding in India as well as outside less provisions made, will be classified under three heads indicated above and both secured and unsecured advances will be included under these heads. Term loans should be mentioned including overdue instalments.

**B.**

(i) **Secured by Tangible Assets:** All advances or part of advances which are secured by tangible assets may be shown here. The item will include advances in India and outside India.

(ii) **Covered by Bank/Government Guarantee:** Advances in India to the extent they are covered by guarantees of Indian and foreign governments and Indian and foreign banks and DICGC and ECGC are to be included.

(iii) **Unsecured:** All advances not classified under (i) and (ii) will be included here. Total of 'A' should tally with total of 'B'.

**C.**

1. **Advances in India (Priority Sectors; Public Sector; Banks and Others):** Advances should be broadly classified into 'Advances in India' and 'Advances outside India'. Advances in India will be further classified on the sectorial basis as indicated. Advances to sectors which for the time being are classified as priority sectors according to the instructions of the Reserve Bank are to be classified under the head 'Priority Sectors'. Such advances should be excluded from item (ii) i.e. advances to public sector. Advances to Central and State Governments and other Government undertakings including Government Companies and Corporation which are, according to the statutes, to be treated as public sector companies are to be included in the category "Public Sector". All advances to the banking sector including cooperative bank will come under the head "Banks". All the remaining advances will be included under the head "Others" and typically this category will include non-priority advances to the private, joint and cooperative sectors.

**Notes:**
(i) The gross amount of advances including refinance and rediscounts but excluding provision made to the satisfaction of auditors should be shown as advances.

(ii) Term loans will be loans not repayable on demand.

(iii) Consortium advances would be shown net of share from other participating banks/institutions.
Banking, Electricity, Insurance and Consequential Loss

10. Fixed Assets (Schedule 10):

I. Premises:
   (i) At cost as on 31 March of the preceding year
   (ii) Additions during the year,
   (iii) Deductions during the year,
   (iv) Depreciation to date.

Premises wholly or partly, owned by the banking company for the purpose of business including residential premises should be shown against 'Premises'. In the case of premises and other fixed assets, the previous balance, additions thereto and deductions there from during the year as also the total depreciation written off should be shown. Where sums have been written off on reduction of capital or revaluation of assets, every balance sheet after the first balance sheet subsequent to the reduction should show the revised figures for a period of five years with the date and amount of revision made.

II. Other Fixed Assets (including Furniture and Fixtures):
   (i) At cost on 31st March of the preceding year;
   (ii) Additions during the year;
   (iii) Deductions during the year;
   (iv) Depreciation to date.

Motor vehicle and all other fixed assets other than premises but including furniture and fixtures should be shown under this head.

11. Other Assets (Schedule 11): They, include the following –

I. Inter/Office Adjustments (Net):

   The inter-office adjustments balance, if in debit, should be shown under this head. Only net position of inter-office accounts, inland as well as foreign, should be shown here. For arriving at the net balance of inter-office accounts should be aggregated and the net balance, if in debit, only should be shown representing mostly items in transit and unadjusted items.

II. Interest Accrued:

   Interest accrued but not due on investment and advances and interest due but not collected on investments will be the main components of this item. As banks normally debit the borrowers' account with interest due on the balance sheet date, usually there may not be any amount of interest due on advance. Only such interest as can be realised in the ordinary course should be shown under this head.

III. Tax paid in advance/deducted at source:

   The amount of tax deducted at source on securities, advance tax paid etc. to the extent that these items are not set off against relative tax provisions should be shown under this head.
Advanced Financial Accounting

IV. **Stationery and Stamps:**
Only exceptional items of expenditure on stationery like bulk purchase of security paper, loose leaf or other ledgers, etc. which are shown as quasi-asset to be written off over a period of time should be shown here. The value should be on a realistic basis and cost escalation should not be taken into account as these items are for internal use.

V. **Non-banking assets acquired in satisfaction of claims:**
Immovable properties/tangible assets acquired in satisfaction of claims are to be shown under this head.

VI. **Others:**
This will include items like claims which have not been met, for instance, clearing items, debit items representing addition to assets or reduction in liabilities which have not been adjusted for technical reasons, want of particulars, etc. advances given to staff by a bank as employer and not as a bank, etc. Items which are in the nature of expenses are pending adjustments should be provided for and the provision netted against this item so that only realisable value is shown under this head. Accrued income other than interest may also be included here.

12. **Contingent Liabilities (Schedule 12):**
   I. Claims against the bank not acknowledged as debts.
   II. Liability for partly paid investments: Liabilities on partly paid shares, debentures, etc. will be included in this head.
   III. Liability on account of outstanding forward exchange contracts.
   IV. Guarantees given on behalf of constituents (i) in India (ii) Outside India.
   V. Acceptances, endorsements and other obligations: This item will include letters of credit and bill accepted by the bank on behalf of customers. In such cases the bank takes upon itself the responsibility for payment. In order to keep a proper record of such liability the bank maintains a customers acceptances, endorsements and guarantee register. All obligations undertaken by the bank as a result of guarantees, endorsements, acceptances etc. are recorded here. At the end of the accounting year, if some of these obligations remain undisbursed, they are to be shown as contingent liabilities under this head.
   VI. Other items for which the Bank is contingently liable: Arrears of cumulative dividends, bills rediscounted under writing contracts, estimated amounts of contracts remaining to be executed on capital account and not provided for, etc. are to be included here.
Bills for Collection:

A banking company receives a large number of bills of exchange for collection purposes. In order to keep a systematic record of such bills it maintains a book called "Bills for Collection Register". On receipt of a bill for collection the entry is made in this register. On collection of the bill of exchange, besides making a note of this fact in the bills for collection register, the following accounting entry is also passed by the banker:

\[
\begin{align*}
\text{Cash Account Dr.} & : \quad \text{(With the amount of bill collected)} \\
\text{To Customer's Account} & : \quad \text{(With the amount of Bill collected less commission charges)} \\
\text{To Commission Account} & : \quad \text{(Commission charges)}
\end{align*}
\]

At the end of the accounting period, the amount of bills yet to be collected is ascertained from the bills for collection register. The total amount of such bills is shown here.

Compulsory Deposits: In case certain persons are required to make compulsory deposits with a bank as per income tax, excise rules etc. these deposits have been received by the concerned bank on behalf of the concerned authority. They may be included in the category of Demand Deposits and shown in the Balance Sheet accordingly.

NOTES AND INSTRUCTION FOR COMPILATION

General Instructions:

1. The formats of balance sheet and profit & loss account cover all items likely to appear in these statements. In case a bank does not have any particular item to report, it may be omitted from the formats.

2. Corresponding comparative figures for the previous year are to be disclosed as indicated in the formats. The words 'current year' and 'previous year' used in the formats are only, to indicate the order of presentation and may not appear in the account.

3. Figures should be rounded off to the nearest thousand rupees. Thus, a sum of Rs. 19,75,921.20 will appear in the balance as Rs. 19.76.

4. Unless otherwise indicated, the term 'bank/s' in these statements will include banking companies, nationalised banks, State Bank of India, Associate banks and all the institutions including cooperatives carrying on the business of banking whether or not incorporated or operating in India. The Hindi version of the Balance Sheet will be a part of the annual report.
Advanced Financial Accounting

**Accounting Policies for Banking Sector:**

On recommendations of the Ghosh Committee, the Reserve Bank of India has issued a directive to all scheduled commercial banks to disclose the Accounting Policies adopted by them in the financial statements for the year ending 31st March, 1991, and later. A specimen form in which accounting policies may be disclosed in the financial statements is given below:

**Principal Accounting Policies:**

1. General: The accompanying financial statements have been prepared on the historical cost basis and conform to the statutory provisions and practices prevailing in the country.

2. Transaction involving foreign exchange: (a) Monetary assets and liabilities have been translated at the exchange rates prevailing at the close of the year. Non-Monetary assets have been carried in the books at the historical cost. (b) Income expenditure items in respect of Indian Branches have been translated at the exchange rates ruling on the date of transaction and in respect of overseas branches at the exchange rates prevailing at the close of the year. (c) Profit or loss on pending forward contracts has been accounted for.

3. Investments: (a) Investments in Government and other approved securities in India are valued at the lower of cost or market value. (b) Investments in subsidiary companies and associate companies (i.e. companies in which the bank hold at least 35% of the share capital) have been accounted for on the historical cost basis.

4. Advances: (a) Provisions for doubtful advances have been made to the satisfaction of the auditors: (i) in respect of identified advances, based on a periodic reviews of advances and after taking into account the portion of advance guaranteed by the Deposit Insurance and Credit Guarantee Corporation, the export credit and guarantee corporation and similar statutory bodies; (ii) in respect of general advances as percentage of total advances taking into account guidelines issued by the Government of India and the Reserve Bank of India. (b) Provisions in respect of doubtful advances have been deducted from advances to the extent necessary and the excess has been included under "other liabilities and provisions". (c) Provisions have been made on a gross basis. Tax relief which will be available when the advance is written off will be accounted for in the year for write off.

5. Fixed Assets: (a) Premises and other fixed assets have been accounted for at their historical cost. Premises which have been revalued are accounted for at the values determined on the basis of such revaluation made by professional valuers. Profit arising on revaluation has been credited to Capital Reserve. (b) Depreciation has been provided for on the straight line/diminishing balance method. (c) In respect of revalued assets, depreciation is provided for on the revalued figures and an amount equal to the additional depreciation consequent on revaluation is transferred annually from the Capital Reserve to the General Reserve/ Profit and Loss Account.
Banking, Electricity, Insurance and Consequential Loss

(6) Staff Benefits made provisions for gratuity/pension benefits to staff has been on an accrual/cash basis and bonus to staff as per statutory requirement have been made. Separate funds for gratuity/pension have been created.

(7) Net Profit

(a) The net profit disclosed in the profit and loss account is after:

   (i) Provisions for taxes and (income, wealth tax) on income in accordance with statutory requirements.

   (ii) Provisions for doubtful advances.

   (iii) Adjustments to the value of "current" investments in Government and other approved securities in India valued at lower of cost or market value.

   (iv) Transfers to contingency.

   (v) Other usual or necessary provision.

(b) Contingency funds have been grouped in the balance sheet under the head "Other Liabilities and Provisions".

Accounting Treatment:

Accounting treatment of some specific items in the Profit & Loss Account and Balance Sheet is being explained as follows:

1. Income Recognition:

   The banks have been recently advised by the Reserve bank of India that they should identify the non-performing assets and ensure that interest on such non-performing assets (NPA) is not recognised as income and taken to the profit and loss account w.e.f financial year 1992-93. The term non-performing assets means a credit facility in respect of which the interest/installment remains 'past due' for a period of two quarters i.e. six months. An amount under any of the credit facilities is to be treated as 'past due', when it has remained outstanding for thirty days beyond the due date. Moreover, if one of the accounts under the new norms is an NPA, all the accounts of the borrowers (other than loans with a liability of less than Rs.25,000) will be treated as NPAs.

2. Bad Debts and Provisions for Doubtful Debts:

   The business of a banking depends on public confidence. In order to ensure that this confidence is not impaired, the banks till recently were given a special privilege permitting them not to show in their published account bad debts and provisions for doubtful debts. They could show income after making deductions for such losses. In the Profit and Loss account the income from 'interest and discount' was usually shown after meeting such losses. In the Balance Sheet, the amount of advances was shown after deducting bad and doubtful debts.
However, with effect from April 1, 1991, this practice has undergone a change. The amount of bad debts and provision for bad debts has to be charged under the heading "Provisions & Contingencies" in the Profit & Loss Account. In the Balance Sheet, the advances are shown after deducting both bad debts and provision for bad debts. It may be noted that the banks collect from their branches information regarding bad and doubtful debts also. The Schedule of Advance is to be filled in by the branches containing separate columns regarding doubtful debts in respect of bills purchased and discounted, cash credits, and overdrafts, and unsecured loans. However, while consolidating the Schedule of Advances at the Head Office level for Balance Sheet purposes, the advances are shown net of any bad or doubtful debts.

Any surplus provision for doubtful debts has not to be deducted from advances but to be shown under the heading other liabilities and provisions in the Balance Sheet.

As per recent directive of the Reserve Bank, provision for doubtful debts has to be created on the various advances on the following basis:

(i) **Standard Assets**: These include advances which are not non-performing assets. No provision is required for such advances.

(ii) **Sub-Standard Assets**: These are advances which have been classified as non-performing assets and are outstanding for a period not exceeding two years. A provision of 10% is required for such advances.

(iii) **Doubtful assets**: These are advances which remain classified as non-performing assets for more than two years. A provision for doubtful debts against such advances has to be created as follows:

   (a) First year: Unsecured portion + 20% of secured portion
   (b) Second and Third year: Unsecured Portion + 30% of secured portion

(iv) **Loss Assets**: These include advances which are fully and substantially non-recoverable and the security value in respect of them is negligible. 100% provision is required for such assets.

(v) Assets for which borrowers' liability is less than Rs. 25,000: 5% of the aggregate liability has to be provided as a general provision.

**Illustration 1:**

Compute the amount of provision for doubtful debts from the following details of advances of National Bank Ltd. (Rs in lakhs)

1. Total Loans and Advances 50
2. Fully secured advances without any default by the borrowers 30
3. Advances overdue for 15 months 10
4. Advances overdue for more than 30 months (secured by mortgage of plant worth Rs. 3 lakhs) 5
5. Non-recoverable unsecured advances 3
6. Small advances not exceeding Rs. 25,000 to each borrower 2
Solution:

**Computation of Provision for Doubtful Debts**

<table>
<thead>
<tr>
<th>SI. No.</th>
<th>Category of advances</th>
<th>Amount (Rs. Lakhs)</th>
<th>Prov. % Debts</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Standard Assets</td>
<td>30</td>
<td>–</td>
</tr>
<tr>
<td>2.</td>
<td>Sub-Standard Assets</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>3.</td>
<td>Doubtful Assets</td>
<td>5</td>
<td>Unsecured</td>
</tr>
<tr>
<td></td>
<td>Unsecured Rs. 2.00</td>
<td></td>
<td>Portion + 30% of secured portion</td>
</tr>
<tr>
<td></td>
<td>Secured Rs. 3.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Loss Assets</td>
<td>3</td>
<td>100</td>
</tr>
<tr>
<td>5.</td>
<td>Small Advances</td>
<td>2</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td></td>
<td>50</td>
<td></td>
</tr>
</tbody>
</table>

**3. Provisions for Taxation:**

Its treatment till recently was on the pattern of bad and doubtful debts. The amount of Provision for Taxation was quietly deducted from Interest and Discount Income. In the Balance Sheet, the amount was merged with "Current and Contingencies Account" on the Liabilities side. However, with effect from 1.4.1991, the above practice has undergone a change. In the revised formats, effective from 1.4.1991, the item has to be shown as under:

The amount of Provision for Taxation has to be charged to the Profit & Loss Account under the heading "Provision & Contingencies" in the Balance Sheet, it will be shown under the heading "Other Liabilities & Provisions", on the Liabilities side.

It will be useful here to know the provisions of the Income Tax Act regarding treatment of Provision for Doubtful Debts while creating provision for Taxation. Section 36(I)(VII) (a) of the Income Tax Act, 1961, permits banking companies to make adequate provisions form their current profits to provide for risk in relation to their rural advances. The amount of deduction in respect of Bad & Doubtful Debts for the assessment year 1995-96 onwards is as follows:

(i) 5 per cent of the total income of the banking company before making such deduction; or

(ii) 4 per cent of aggregate average rural advances made by the banking company.

Tutorial Note. In the absence of any specific details about the rural advances, the students may create Provision for Taxation on Net Profits left after charging Provision for Doubtful Debts.
4. **Rebate on Bill Discounted:**

This refer to unexpired discount. A banking company charges discount in advance for the full period of the bill of exchange or promissory note discounted with it. The accounting entry made is as follows:

Bill Discounted and Purchased A/c Dr.
To Customer's A/c
To Discount A/c

Customer's account is credited with the net amount remaining after deducting the amount of discount. The amount credited to the discount account represents the earning of the bank. However, it may be possible that the bills discounted may mature after the close of the financial year. It will not be appropriate to the credit of the profit and loss account that part of the discount charged which relates to the next year. An accounting entry is, therefore, passed for unearned discount in the following manner:

Discount A/c Dr.
To Rebate on Bill Discounted
(with the amount of unearned discount relating to the next period)

Rebate on bills discounted, if already appears in the trial balance is taken to the balance sheet on the "liabilities side". However, if adjustment has to be done after preparation of the trial balance in respect of rebate on bills discounted, the amount of such rebate (i.e. the unearned discount) will be deducted from the total discount in the profit and loss account and will also appear in the balance sheet.

5. **Interest on Doubtful Debts**

Interest earned by a banking company on doubtful debts can be treated in any of the following ways in the account of a banking company

(a) **Interest Suspense Method.** The interest earned may be credited to Interest Suspense Account opened for this purpose.

(b) **Cash Method.** No entry is passed for such interest till it is actually received.

(c) **Accrual Method.** Interest Account may be credited with the full amount of interest due on doubtful debts and simultaneously an adequate provision for bad and doubtful debts may be created.

It may not be noted, as discussed earlier, that the doubtful debts come within the category of non-performing assets and therefore interest income on such doubtful advances should not be recognized and taken to the profit and loss account. The method (b) is therefore best under the present circumstances.
**Illustration 2:**

Following are the balance sheets of A Bank Ltd. for the year ended on 31st March, 1999 and 31st March, 1998:

<table>
<thead>
<tr>
<th>1999 (Rs.)</th>
<th>1998 (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest on Loans</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Interest on Cash Credit</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Interest on Overdraft</td>
<td>50,000</td>
</tr>
<tr>
<td>Commission Received</td>
<td>5,000</td>
</tr>
<tr>
<td>Rent</td>
<td>40,000</td>
</tr>
<tr>
<td>Interest on Fixed Deposit</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Discount on Bills Discounted</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Law Charges</td>
<td>30,000</td>
</tr>
<tr>
<td>Brokerage received</td>
<td>30,000</td>
</tr>
<tr>
<td>Interest on Saving Bank Deposit</td>
<td>80,000</td>
</tr>
<tr>
<td>Insurance</td>
<td>18,000</td>
</tr>
<tr>
<td>Printing and Stationery</td>
<td>4,000</td>
</tr>
<tr>
<td>Auditor's Fees</td>
<td>2,000</td>
</tr>
<tr>
<td>Directors’ Fees</td>
<td>4,000</td>
</tr>
<tr>
<td>Rebate on Bills Discounted</td>
<td>40,000</td>
</tr>
<tr>
<td>Salaries</td>
<td>50,000</td>
</tr>
<tr>
<td>Postage expenses</td>
<td>1,000</td>
</tr>
<tr>
<td>Interest on Investment</td>
<td>7,00,000</td>
</tr>
<tr>
<td>Interest on balance with RBI</td>
<td>10,000</td>
</tr>
</tbody>
</table>

Prepare Profit and Loss Account of A Ltd. from the above particulars.

**Solution:**

(000s omitted)

**PROFIT AND LOSS ACCOUNTS OF A BANK LTD.** for the year ended 31st March, 1999

<table>
<thead>
<tr>
<th>No.</th>
<th>Schedule</th>
<th>Year ended 31.3.99</th>
<th>Year ended 31.3.98</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>(Current year) Rs.</td>
<td>(Previous year) Rs.</td>
</tr>
<tr>
<td>I.</td>
<td>INCOME</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Interest earned</td>
<td>13 1210.00 849.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Other income</td>
<td>14 35.00 30.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>TOTAL</td>
<td>1245.00 879.00</td>
<td></td>
</tr>
<tr>
<td>II.</td>
<td>EXPENDITURE</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Interest expended</td>
<td>15 380.00 320.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Operating expenses</td>
<td>16 149.00 106.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Provision and Contingencies</td>
<td>— —</td>
<td></td>
</tr>
<tr>
<td></td>
<td>TOTAL</td>
<td>529.00 426.00</td>
<td></td>
</tr>
</tbody>
</table>
Advanced Financial Accounting

III. PROFIT/LOSS

Net Profit/Loss for the year 716.00\(^1\) 453.00\(^2\)
Profit/Loss (-) brought forward — —
TOTAL 716.00 453.00

IV. APPROPRIATIONS

Transfer to statutory reserves 143.20\(^3\) 90.60\(^4\)
Transfer to other reserves — —
Transfer to govt./proposed dividend — —
Balance carried over to Balance Sheet 572.80 362.40
TOTAL 716.00 453.00

1. Rs. 1245 – 529 = Rs. 716.00
2. Rs. 879 – 426 = Rs. 453;
3. 716 × 20/100 = Rs.143.20;
4. 453 × 20/100 = Rs. 90.60

SCHEDULE 13 - INTEREST EARNED

<table>
<thead>
<tr>
<th></th>
<th>Year ended 31.3.99</th>
<th>Year ended 31.3.99</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs. '000</td>
<td>Rs. '000</td>
</tr>
<tr>
<td>I. Interest/Discount on advertisement</td>
<td>410(^1)</td>
<td>241(^2)</td>
</tr>
<tr>
<td>II. Income on investments</td>
<td>700</td>
<td>600</td>
</tr>
<tr>
<td>III. Interest on balance with Reserve Bank of India and other inter- bank funds</td>
<td>100</td>
<td>8</td>
</tr>
<tr>
<td>IV. Others</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>TOTAL</td>
<td>1210</td>
<td>849</td>
</tr>
</tbody>
</table>

1 (Rs. 1,00,000 + 2,00,000 + 50,000 + 1,00,000) - 40,000 = Rs. 4,50,000 - 40,000 = Rs. 4,10,000
2 (Rs. 80,000 + 70,000 + 30,000 + 90,000) - 29,000 = Rs. 2,70,000 - 29,000 = Rs. 2,41,000.
### SCHEDULE 14 - OTHER INCOME

<table>
<thead>
<tr>
<th></th>
<th>Year ended 31.3.99</th>
<th>Year ended 31.3.99</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs. '000</td>
<td>Rs. '000</td>
</tr>
<tr>
<td>I. Commission, exchange and brokerage</td>
<td>35</td>
<td>30</td>
</tr>
<tr>
<td>(a) Profit on sale of investment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Loss on sale of investment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(b) Profit on revaluation of investment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Loss of revaluation of investment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(c) Profit on sale of land, buildings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Loss on sale of land, buildings and other assets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(d) Profit on exchange transactions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Loss on exchange transaction</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(e) Income earned by way of dividends etc., from subsidiaries/companies and/or joint ventures abroad/ in India.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>VII. Miscellaneous Income</td>
<td></td>
<td></td>
</tr>
<tr>
<td>TOTAL</td>
<td>35</td>
<td>30</td>
</tr>
</tbody>
</table>

1. Commission Rs. 5,000 + Brokerage Rs. 30,000 = Rs. 35,000 or 35 thousand;
2. Commission Rs. 2,000 + Brokerage Rs. 28,000 = Rs. 30,000 or 30 thousand.

### SCHEDULE 15 - INTEREST EXPENDED

<table>
<thead>
<tr>
<th></th>
<th>Year ended 31.3.99</th>
<th>Year ended 31.3.99</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs. '000</td>
<td>Rs. '000</td>
</tr>
<tr>
<td>I. Interest on deposits</td>
<td>380</td>
<td>320</td>
</tr>
<tr>
<td>II. Interest on RBI/Inter-bank borrowings</td>
<td></td>
<td></td>
</tr>
<tr>
<td>III. Others</td>
<td></td>
<td></td>
</tr>
<tr>
<td>TOTAL</td>
<td>380</td>
<td>320</td>
</tr>
</tbody>
</table>

1. Rs. 3,00,000 + 80,000 = Rs. 3,80,000 or 380 thousand;
2. Rs. 2,50,000 + 70,000 = Rs. 3,20,000 or 320 thousand.
Advanced Financial Accounting

**SCHEDULE 16 - OPERATION EXPENSES**

<table>
<thead>
<tr>
<th>Description</th>
<th>Year ended 31.3.99 Rs. '000</th>
<th>Year ended 31.3.99 Rs. '000</th>
</tr>
</thead>
<tbody>
<tr>
<td>I. Payment to and provision for employees</td>
<td>50</td>
<td>49</td>
</tr>
<tr>
<td>II. Rent, taxes and lighting</td>
<td>40</td>
<td>30</td>
</tr>
<tr>
<td>III. Printing and stationary</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td>IV. Advertisement and publicity</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>V. Depreciation on bank's property</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>(a) Directors fees, allowance and expenses</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td>(b) Auditors’ fees and expenses (including branch Auditors’ fees and expenses)</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>VIII. Law charges</td>
<td>30</td>
<td>2</td>
</tr>
<tr>
<td>IX. Postage, telegrams, telephones, etc.</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>X. Repair and maintenance</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>XI. Insurance</td>
<td>18</td>
<td>16</td>
</tr>
<tr>
<td>XII. Other expenditure</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>149</td>
<td>106</td>
</tr>
</tbody>
</table>

**Illustration 3:**

From the following particulars prepare the balance sheet of Progressive Bank Ltd., as on 31st March, 1991:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr. (Rs.)</th>
<th>Cr. (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>—</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Reserve Fund</td>
<td>—</td>
<td>16,00,000</td>
</tr>
<tr>
<td>Fixed Deposit</td>
<td>—</td>
<td>40,00,000</td>
</tr>
<tr>
<td>Savings bank deposits</td>
<td>—</td>
<td>60,00,000</td>
</tr>
<tr>
<td>Current Accounts</td>
<td>—</td>
<td>2,20,00,000</td>
</tr>
<tr>
<td>Money at call and short notice in India</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>Bills discounted and purchased in India</td>
<td>9,00,000</td>
<td></td>
</tr>
<tr>
<td>Investments at cost :</td>
<td></td>
<td></td>
</tr>
<tr>
<td>— securities</td>
<td>1,00,00,000</td>
<td></td>
</tr>
<tr>
<td>— debentures</td>
<td>4,00,000</td>
<td></td>
</tr>
<tr>
<td>— bullion</td>
<td>24,00,000</td>
<td></td>
</tr>
<tr>
<td>Reserve for buildings</td>
<td>—</td>
<td>10,00,000</td>
</tr>
<tr>
<td>Premises at cost</td>
<td>1,00,00,000</td>
<td></td>
</tr>
</tbody>
</table>
**Banking, Electricity, Insurance and Consequential Loss**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Addition to premises</td>
<td>20,00,000</td>
</tr>
<tr>
<td>Depreciation fund on premises</td>
<td>80,00,000</td>
</tr>
<tr>
<td>Cash with Reserve Bank of India</td>
<td>34,00,000</td>
</tr>
<tr>
<td>Cash with State Bank of India</td>
<td>12,00,000</td>
</tr>
<tr>
<td>Unclaimed dividend</td>
<td>24,000</td>
</tr>
<tr>
<td>Unexpired discount</td>
<td>50,000</td>
</tr>
<tr>
<td>Loans, advances, overdraft and cash credits in India</td>
<td>1,00,00,000</td>
</tr>
<tr>
<td>Branch adjustment</td>
<td>57,94,000</td>
</tr>
<tr>
<td>Silver</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Advance payment of tax</td>
<td>1,10,000</td>
</tr>
<tr>
<td>Interest accrued on investments</td>
<td>2,60,000</td>
</tr>
<tr>
<td>Non-banking assets acquired</td>
<td>70,000</td>
</tr>
<tr>
<td>Borrowings from banks in India</td>
<td>2,50,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>20,00,000</td>
</tr>
<tr>
<td>Profit &amp; Loss account including Rs.2, 10,000 for the year</td>
<td>4,10,000</td>
</tr>
<tr>
<td>Dividend fluctuation fund</td>
<td>6,00,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>4,69,34,000</strong></td>
</tr>
</tbody>
</table>

The bank had bills for collection for its constituents Rs.3,00,000 and acceptances Rs.4,00,000. There was a claim of Rs.2,00,000 against the bank but not acknowledged as debt. The liabilities for bills rediscounted was Rs.32,000. Liability for forward exchange contract was Rs.20,00,000. The directors decided to reserve Rs.2,000 for unexpired discounts and transfer reserve for building to depreciation fund.

**PROGRESSIVE BANK LIMITED**

**Balance Sheet as on 31st March, 1991**

<table>
<thead>
<tr>
<th>Schedule</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>1,000</td>
</tr>
<tr>
<td>2</td>
<td>2,608</td>
</tr>
<tr>
<td>3</td>
<td>32,000</td>
</tr>
<tr>
<td>4</td>
<td>250</td>
</tr>
<tr>
<td>5</td>
<td>11,076</td>
</tr>
<tr>
<td>6</td>
<td>3,400</td>
</tr>
<tr>
<td>7</td>
<td>1,400</td>
</tr>
<tr>
<td>8</td>
<td>12,800</td>
</tr>
<tr>
<td>9</td>
<td>10,900</td>
</tr>
<tr>
<td>10</td>
<td>12,000</td>
</tr>
<tr>
<td>11</td>
<td>6,434</td>
</tr>
<tr>
<td>12</td>
<td>2,632</td>
</tr>
<tr>
<td>13</td>
<td>300</td>
</tr>
</tbody>
</table>

**Schedule Rs. omitted**
### SCHEDULE 1 – CAPITAL
- Issued, Subscribed and Paid up: Rs. 1,000

### SCHEDULE 2 – RESERVE AND SURPLUS
- (i) Statutory Reserve: Rs. 1,600
- Addition during the year: 42
- (ii) Revenue and other Reserves: Dividend Equalisation Fund: 600
- (iii) Profit and Loss A/c (368 - 2): 366
- Total: 2,608

### SCHEDULE 3 – DEPOSITS
- (i) Demand Deposits: Rs. 22,000
- (ii) Saving Bank Deposits: 6,000
- (iii) Term Deposits: 4,000
- Total: 32,000

### SCHEDULE 4 – BORROWINGS
- Borrowings in India: Rs. 250

### SCHEDULE 5 – OTHER LIABILITIES AND PROVISIONS
- Bills payable: Rs. 2,000
- Unexpired Discount: 52
- Unclaimed Dividends: 24
- Depreciation Fund: 9,000
- Total: 11,076

### SCHEDULE 6 – CASH AND BALANCES WITH RBI
- Balance with RBI: Rs. 3,400

### SCHEDULE 7 – BALANCE WITH BANKS AND MONEY AT CALL AND SHORT NOTICE
- (i) Balance with SBI: Rs. 1,200
- (ii) Money at Call and Short Notice: 200
- Total: 1,400

### SCHEDULE 8 – INVESTMENTS
- (i) Central and State Government Securities: Rs. 10,000
- (ii) Debentures: 400
- (iii) Bullion: 2,400
- Total: 12,800
Banking, Electricity, Insurance and Consequential Loss

**SCHEDULE 9—ADVANCES**

(i) Bills purchased and discounted Rs. 900
(ii) Loans’, cash credit, advances and overdrafts 10,000
Total 10,900

**SCHEDULE 10—FIXED ASSETS**

(i) Premises at cost Rs. 10,000
Addition during the year 2,000
Total 12,000

**SCHEDULE 11—OTHER ASSETS**

(i) Branch Adjustment Rs. 5,794
(ii) Silver 200
(iii) Advance Payment of Tax 110
(iv) Interest accrued on Investments 260
(v) Non-Banking assets 70
Total 6,434

**SCHEDULE 12—CONTINGENT LIABILITIES**

(i) Claims against the bank acknowledge as debt Rs. 200
(ii) Liability on Bills Discounted 32
(iii) Liability for forward exchange contract 2,000
(iv) Acceptances, Endorsements and other Obligations 400
Total 2,632

6.2 ELECTRICITY COMPANY ACCOUNTS

The Indian Electricity Act, 1910 and the Electricity (Supply) Act of 1948 consist of the special legislations governing electricity companies. Electricity is a basic infrastructure industry which is of great importance to the public.

**Accounting Provisions**:

(a) *Depreciation*: The straight line method of depreciation is to be followed and the Central Government has been given the power to prescribe, by notification, the life of various types of assets. No depreciation is to be written off when the asset is useless due to obsolescence, superfluousness or has been written down, value of the discarded asset is to be carried to Discarded Asset Account. On sale of such asset the sale proceeds are credited to the account and any profit or loss is charged to contingencies reserve.
(b) **Reasonable Return**: The law defines the reasonable return in following terms in order to avoid electricity undertakings from earning too high a profit.

(c) A yield at the standard rate, which is the Reserve Bank rate plus two per cent on the capital base.

(d) Income derived from investments except investments made against Contingencies Reserve.

(e) An amount equal to 1/2 per cent on loans advanced by the Electricity Board;

(f) An amount equal to 1/2 per cent on the balance of Development Reserve; and

(g) An amount equal to 1/2 percent received on Debentures.

(h) An amount equal to 1/2 percent on amounts approved from approved institutions.

*Capital Base* means: (a) the original cost of fixed assets available for use and necessary for the purpose of the undertakings less contribution, if any, made by the consumers for construction of service lines and also amounts written off; (b) the cost of intangible assets; (c) the original cost of works in progress; (d) the amount of investments made compulsorily against Contingencies Reserve; and (e) the monthly average of the stores, materials, supplies and cash and bank balances held at the end of each month,

*Less*:

(i) the amounts written off or set aside on account depreciation of fixed assets and amounts written off in respect of intangible assets in the books of the undertaking;

(ii) loans advanced by the Board

(iii) debentures;

(iv) security deposits of consumers held in cash;

(v) the amount standing to the credit of the Tariff and Dividends Control Reserve;

(vi) the amount set apart for the Development Reserve; and

(vii) the amount carried forward in the accounts of the licensee for distribution to consumers.

**Clear Profit**: Clear Profit means the difference between the total income and the total expenditure plus specific appropriations. The Act defines the three terms - income, expenditure and appropriations. The provisions are set out below for ready undertakings in the form of an amount :-
### Banking, Electricity, Insurance and Consequential Loss

<table>
<thead>
<tr>
<th>Expenditure</th>
<th>Rs</th>
<th>Income</th>
<th>Rs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of generation and purchase of energy</td>
<td></td>
<td>Gross receipts from sale of energy</td>
<td></td>
</tr>
<tr>
<td>Cost of distribution and sale of energy</td>
<td></td>
<td>Less discount applicable to sale</td>
<td></td>
</tr>
<tr>
<td>Rent Rates and taxes (excluding taxes on income or profits)</td>
<td></td>
<td>Rental of meters and other apparatus hired to consumers</td>
<td></td>
</tr>
<tr>
<td>Interest on loans advanced by the Board</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest on debentures</td>
<td></td>
<td>Sale and repair of lamps and Apparatus</td>
<td></td>
</tr>
<tr>
<td>Interest on security deposits Bad debts</td>
<td></td>
<td>Rent, less outgoings not otherwise provided for transfer fee.</td>
<td></td>
</tr>
<tr>
<td>Auditor's fees</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management expenses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other expenses admissible under the</td>
<td></td>
<td>Interest from investments, fixed</td>
<td></td>
</tr>
<tr>
<td>Indian Income-tax Act and arising from</td>
<td></td>
<td>and call deposits and bank balances.</td>
<td></td>
</tr>
<tr>
<td>ancillary or incidental to the business of</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>electricity supply</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contribution to Provident Fund, staff</td>
<td></td>
<td>Other receipts liable for tax Indian</td>
<td></td>
</tr>
<tr>
<td>pension, gratuity and apprentice and</td>
<td></td>
<td>Income tax and arising from and</td>
<td></td>
</tr>
<tr>
<td>other training schemes</td>
<td></td>
<td>ancillary or incidental to the business</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>of electricity</td>
<td></td>
</tr>
<tr>
<td>Business of electricity supply</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bonus paid to the employees of the undertaking in accordance with the decision of labour tribunal or the State Government</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance of Profit c/d</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Appropriations</td>
<td>Balance of profit b/f</td>
<td>Balance of profit b/f</td>
<td></td>
</tr>
<tr>
<td>Previous losses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>All taxes on income and profits</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Instalments in respect of intangible assets and expenses regarding issue of capital</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contribution to Contingencies reserve</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Arrears of depreciation</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Development reserve</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other appropriations permitted by the</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Govt.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Balance, being clear Profit</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Advanced Financial Accounting

Disposal of Surplus:

Should the clear profit exceed the reasonable return, the surplus has to be disposed of as under—

(a) One-third of the surplus not exceeding 5% of the reasonable return will be at the disposal of the undertaking;
(b) of the balance, one-half will be transferred to "Tariffs and Dividends Control Reserve", and
(c) the balance will be distributed among consumers by way of reduction of rates or by way of special rebate.

Any electricity undertaking must so adjust rates that the amount of clear profit in any year does not exceed the reasonable return by more than 20% of the reasonable return.

Tariffs and Dividends Control Reserve:

This can be utilized whenever the clear profit is less than the reasonable return. The balance in the Reserve must be handed over to the purchaser of the undertakings, if it changes hands.

Contingencies Reserve:

A sum equal to not less than 1/4% and not more than 1/2% of the original cost of fixed assets must be transferred from the revenue account to Contingencies Reserves until it equals 5% of the original cost of fixed assets. The amount of the reserve must be kept invested in trust securities. The reserve can be utilised with the approval of the State Government for the following purposes:

(a) to meet expenses or loss of profits arising out of accidents, strikes or circumstances beyond the control of the management;
(b) to meet expenses of replacement or removal of plant or works other than the expenses necessary for normal maintenance or renewal, and
(c) to pay compensation payable under law for which no other provision has been made.

Any loss or profit on sale of fixed asset has to be transferred to Contingencies Reserve.

Development Reserve:

An amount equal to income-tax and super tax (calculated at current rates) which would have been paid but for the development rebate allowed by income-tax authorities on installation of new plant and machinery has to be transferred to the Development Reserve Account.
Banking, Electricity, Insurance and Consequential Loss

If, in any accounting year, the clear profit excluding the special appropriation together with the accumulations, if any, in the Tariff and Dividends Control Reserve less the amount to the credited to Development Reserve falls short of the reasonable return, the sum to be appropriated to the Development Reserve in respect of such accounting year may be reduced by the amount of the shortfall. Appropriations to the Development Reserve may be made over a period of 5 years. Development Reserve can be invested only in the business of electricity supply of the undertaking. On a transfer of the undertaking, the reserve should be transferred to the purchaser.

General Reserve:

Section 67 lays down that after interest and depreciation have been provided, a contribution to general reserve shall be made at the rate of not exceeding 1/2% of the original cost of the fixed assets until the total of such reserve comes to 8% of the original cost of the assets. This applies only to the Electricity Boards though there is nothing to stop electricity companies from building up reserves.

2. Final Accounts

The final accounts of an electricity company are made every year up to 31st March and submitted to the State Government in the forms prescribed in Annexures IV and V of the Indian Electricity Rules, 1956. These forms are given below:

These forms are slightly different from the usual manner in which final accounts are prepared under Double Account System. A comparative chart is given below:

<table>
<thead>
<tr>
<th>Double Account System</th>
<th>Electricity Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) Capital A/c</td>
<td>(i) Statement of share and loan Capital.</td>
</tr>
<tr>
<td>(ii) Revenue A/c</td>
<td>(ii) Statement of Capital expenditure</td>
</tr>
<tr>
<td>(iii) Net Revenue A/c</td>
<td>(iii) Statement of Operating revenue</td>
</tr>
<tr>
<td>(iv) General B/Sheet</td>
<td>(iv) Statement of Operating expenses</td>
</tr>
<tr>
<td></td>
<td>(v) Statement of Net Revenue &amp; Appropriation A/c</td>
</tr>
<tr>
<td></td>
<td>(vi) General B/Sheet.</td>
</tr>
</tbody>
</table>

The student should particularly note Statements No. III, IV, X and XI. Statement No. III and IV together constitute Revenue Account.

**Note:** It should be noted that though the Companies Act permits preparation of the final accounts in the forms prescribed by the Electricity (Supply) Act, electricity companies usually present their final accounts to their shareholders in the form laid down by Schedule VI to the Companies Act. This is because the forms under the Companies Act are much more compact than those under the Electricity Supply Act. Returns to State Governments, however, must be in the forms laid down by the Electricity (Supply) Act. They are specified in the form of annexures stated below:
3. **Double Accounting System:**

The final accounts of public utility concerns, such as electricity companies, railways, water supplies, gas companies etc. are prepared following the double account system. Double Account System is a method of presenting the final accounts where a firm prepares two Balance Sheets instead of one. The chief features of the Double Account System are as follows:-

1. The ordinary balance sheet is split in two parts: Capital account : This records all receipt and expenditure on capital accounts. It shows the sources from which the fixed capital has been raised and the purposes for which it has been utilised. The purpose of this account is to give the general public full and complete information about raising and utilization of fixed capital. One part contains fixed assets and fixed liabilities. It is called “Receipt and Expenditure on Capital Account”. On each side there are three columns for amount - one column to show figures up to the beginning of the year, the second column to show expenditure (assets) or receipts (liabilities) during the year and the third column to show total. The other part (called General
**Banking, Electricity, Insurance and Consequential Loss**

Balance Sheet) contains other assets and liabilities and the balance of the Receipts and Expenditure on Capital Account. In case of electricity companies, however, the total of the expenditure as per Capital Account is shown on the assets side and the total of receipts is shown on the liabilities side.

2. A Revenue Account is prepared which is like the ordinary Profit and Loss Account. Also, a Net Revenue Account is prepared which is like the ordinary Profit and Loss Appropriation Account. The exceptions are as follow:

   (a) Interest in all cases is debited or credited to Net Revenue Account and not to Revenue Account. In case of Railways, rent on leased land, etc., is also debited to Net Revenue Account.

   (b) Depreciation is debited to Revenue Account and credited to Depreciation Reserve. Depreciation Fixed A/c appears on the liability side of the General Balance Sheet. The amount standing to the credit of depreciation fund is invested in securities outside the business. The depreciation fund and the corresponding depreciation fund investments are shown in the general balance sheet. The fixed assets are shown at cost in the capital account. For the sake of convenience of the readers, we are giving below the prescribed form of important accounts/statements in a concise and summarized manner:

**ANNEXURE V**

[See Section II and Rule 26(3)]

<table>
<thead>
<tr>
<th>Electric Licence, 19………</th>
<th>Date of Commencement of Licence....</th>
</tr>
</thead>
<tbody>
<tr>
<td>Name of undertaking……...</td>
<td>Year of operation……...</td>
</tr>
</tbody>
</table>

No. 1

**STATEMENT OF SHARE AND LOAN CAPITAL**

for the year ended 31st March, 19...

(Applicable to Licensees other than Local Authority Licensees)

<table>
<thead>
<tr>
<th>Description of Capital</th>
<th>1 Balance at the beginning of the year</th>
<th>2 Receipts during the year</th>
<th>3 Redeemed during the year</th>
<th>4 Balance at the end of the year</th>
<th>5 Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Share Capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Authorized</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Issued</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Subscribed</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td></td>
<td>...</td>
</tr>
<tr>
<td>Called up capital</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td></td>
<td>...</td>
</tr>
<tr>
<td><strong>Less: Calls-in-arrears</strong></td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Total paid up capital</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
</tbody>
</table>
B. Capital Reserve

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Forfeited a/c</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Share Premium</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Other Items</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
</tbody>
</table>

(a) Loan Capital:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan from State Electricity Board</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Debentures</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Unsecured Loans</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Total Loan Capital</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
</tbody>
</table>

(b) Other Capital:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contributions from consumers</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>local authorities</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Total Capital raised and</td>
<td>...</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
<tr>
<td>Appropriated</td>
<td>(A + B + C + D)</td>
<td>...</td>
<td>...</td>
<td>...</td>
</tr>
</tbody>
</table>

No. II Statement of Capital Expenditure for the year ended 31 March 19...

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Balance at the Beginning of the year</th>
<th>Additions during the year</th>
<th>Retirements during the year</th>
<th>Balance at the end of the year</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Intangible Assets</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>(a) Hydraulic Power Plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(b) Steam Power Plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(c) Internal Combustion Power Plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>E. Transmission Plant</td>
<td>(High or Extra High voltage)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>F. Distribution Plant-High Voltage</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>G. Distribution Plant-Medium</td>
<td>and low voltage</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>and low voltage</td>
<td>(a) Public Lighting</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>and low voltage</td>
<td>(b) General Equipment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Capital Assets in use</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The details of assets under each head of Capital Expenditure are as given below:

A. **Intangible Assets:**
   1. Preliminary and Promotional Expenses.
   2. Cost of Licence.
   3. Other expenses, e.g. expenses incidental to conversion from D.C. to A.C. change of frequency, etc.

B. **Hydraulic Power Plant:**
   1. Land and Rights.
   2. Buildings and Civil engineering works containing generating and equipment.
   3. Hydraulic works forming part of a hydroelectric system including:
      (i) dams, spillways, weirs, canals, reinforced concrete flumes and siphons.
      (ii) reinforced concrete pipelines and surge tanks, steel pipe lines, sluice gates, steel surge tanks, hydraulic control valves and other hydraulic works.
   4. Water wheels, generators and ancillary equipment including plant foundations.
   5. Switchgear including cable connections.
   6. Miscellaneous power plant equipment.
   7. Other civil works (to be specified)

C. **Steam Power Plant:**
   1. Land and Rights.
   2. Building and civil engineering works containing generating plant and equipment.
   3. Boiler plant and equipment including plant foundations.
   4. Engines, Turbines, Generators and ancillary equipment including plant foundations.
   5. Water-cooling system comprising cooling towers and circulating water system.
   6. Switchgear including cable connections.
   7. Miscellaneous power plant and equipment.
   8. Other civil works (to be specified)

D. **International Power Plant**
   1. Land & Rights.
      (a) Buildings and civil engineering works containing generating plant and equipment.
      (b) Engines, Turbines, Generators and ancillary equipment including plant foundations.
Advanced Financial Accounting

(c) Water-cooling system comprising cooling towers and circulating water system.
(d) Switchgear including cable connections.

6. Miscellaneous power plant and equipment.
7. Other civil works (to be specified)

E. Transmission Plant (High or Extra High Voltage)
1. Land and Rights
2. Building and Structures including civil engineering works containing transmission plant and equipment.
3. Substation transformers, transformer kiosks, substation equipment and other fixed apparatus including plant foundations:
   (i) transformers including foundations having rating of 100 kilo volt amperes and over.
   (ii) other.
4. Switchgear including cable connection.
5. Tower, Poles, Fixtures, overhead conductors and devices
   (i) Lines on steel or reinforced concrete supporters operating at normal voltage higher than 13.2 kilovolts.
   (ii) Other lines on steel or reinforced concrete supports.
   (iii) Lines on wood supports.
6. (a) Underground cables and devices including joint boxes and disconnecting boxes.
   (b) Cable duct system.

F. Distribution Plant (High Voltage):
1. Land and Rights
2. Building and Structures including civil engineering works containing transmission plant and equipment.
3. Substation transformers, transformer kiosks, substation equipment and other fixed apparatus including plant foundations:
   (i) transformers including foundations having rating of 100 kilo volt amperes and over.
   (ii) other.
4. Switchgear including cable connection.
5. Tower, Poles, Fixtures, Overhead conductors and devices
   a. Lines on steel or reinforced concrete supporters operating at normal voltage higher than 13.2 kilovolts.
   b. Other lines on steel or reinforced concrete supports.
   c. Lines on wood supports.
Banking, Electricity, Insurance and Consequential Loss

6. (a) Underground cables and devices including joint boxes and disconnecting boxes.
   (b) Cable duct system.
7. Service lines.
8. Metering equipment.

G. Distribution Plant (medium and Lower Voltage)

1. Land and Rights
2. Building and Structures including civil engineering works containing transmission plant and equipment.
3. Substation transformers, transformer kiosks, substation equipment and other fixed apparatus including plant foundations:
   (i) transformers including foundations having rating of 100 kilo volt amperes and over.
   (ii) other.
4. Switchgear including cable connection.
5. Tower, Poles, Fixtures, Overhead conductors and devices
   (i) Lines on steel or reinforced concrete supporters operating, at normal voltage higher than 13.2 kilovolts.
   (ii) Other lines on steel or reinforced concrete supports.
   (iii) Lines on wood supports.
6. (a) Underground cables and devices including joint boxes and disconnecting boxes.
   (b) Cable duct system.
7. Service lines.
8. Metering equipment.

H. Public Lighting Street and signal lighting systems:

I. General Equipment (Not allocated to other sub-head)
   1. Land and Rights
   2. Building and Structures.
   3. Office Furniture and equipment.
   4. Transportation equipment.
   5. Laboratory and meter testing equipment.
   6. Workshop plant and equipment.
   7. Tools and work equipment.
   8. Communication equipment.
   9. Miscellaneous equipment.
### No. IIA Statement showing the Written-down Cost of Fixed Assets retired on account of Obsolescence, Inadequacy, Superfluity, etc.

<table>
<thead>
<tr>
<th>Particulars of Assets</th>
<th>Written down cost at the beginning of the year</th>
<th>Written down cost retired during the year</th>
<th>Amount realised during the year</th>
<th>Excess of sale proceeds over written down cost transferred in Contingencies Reserve A/c vide Col. 4 of statement VI</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
</tbody>
</table>
Banking, Electricity, Insurance and Consequential Loss

6. Irrigation.
7. Traction.
8. Supplies in bulk to distributing licensees
   Total Revenue by sale of electricity

B. Miscellaneous Revenue from consumers
1. Rent from
   (a) Meters.
   (b) Electric motors, fittings, appliances and
       other apparatus hired to consumers.
2. Service connection fees.
3. Public Lighting Maintenance.
   Total Miscellaneous Revenue from consumers

C. Other Revenues:
1. Sale of Stores.
2. Repair of lamps and apparatus.
4. Other miscellaneous items (to be specified).
   Total other revenue
   Total Operating Revenues

Deduct
Total Operating Expenses as per Statement IV
Net Surplus or deficit carried to the Net Revenue
and Appropriation A/c Statement X.

<table>
<thead>
<tr>
<th>NO. IV</th>
<th>Statement of Operating Expenses for the year ended 31st March, 19...</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Particulars of Expenses</td>
</tr>
<tr>
<td></td>
<td>1</td>
</tr>
</tbody>
</table>

A. Hydraulic Power Generation
   (a) Operation
   (b) Maintenance
   (c) Depreciation
   Total Hydraulic Power Generation Exps.

B. Steam Power Generation:
   (a) Operation
   (b) Maintenance
   (c) Depreciation
   Total Steam Power Generation Exps.
C. International Combustion Power Generation  
   (a) Operation  
   (b) Maintenance  
   (c) Depreciation  
   Total Internal Combustion Power Generation Expenses  

D. Power Purchased Total Production Expn. (A+B+C+D)  

E. Transmission(High or Extra Voltage)  
   (a) Operation and maintenance  
   (b) Deprecation on Transmission Plant and equipment (from statement V)  
   Total Transmission Expenses  

F. Distribution (High Voltage):  
   (a) Operation and maintenance  
   (b) Deprecation on Transmission Plant and equipment (from statement V)  
   Total Distribution (H.V) Expenses  

G. Distribution (Medium & Low Voltage):  
   (a) Operation and maintenance  
   (b) Deprecation on Transmission Plant and equipment (from statement V)  
   Total Distribution (M. and LV Exps)  

H. Public Lighting:  
   (a) Operation and maintenance  
   (b) Deprecation on Transmission Plant and equipment (from statement V)  
   Total Public Lighting Expenses  
   (a) Servicing, Meter Reading, Billing  
   Connecting, Accounting, Sales Promotion, etc.  
   Proportionate salaries, allowances, etc.  
   Meter reading and inspection  

J. Rates and Taxes  

K. General Establishment Charges  
   Total General Establishment charges  

L. Other Charges Total Other Charges  

M. Management Expenses  
   Total Operating Expenses Transferred to Statement III
### Statement X
Statement of Net Revenue and Appropriation Account for the year ended 31 March 19...

<table>
<thead>
<tr>
<th>Figures for last year</th>
<th>Particulars</th>
<th>Amount</th>
<th>Figures for last year</th>
<th>Particulars</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td></td>
</tr>
</tbody>
</table>

1. To Balance of loss brought forward from last account
2. To net operating deficit as per Statement III.
3. To appropriations (applicable to local authority licensee only)
   (a) Interest on loan capital
   (b) Instalment of redemption of loan capital, as per col.8 of Statement I-A(l)
4. To Taxes on income and profit pd.
5. To Instalment written down in respect of tangible assets.
6. To instalment of contribution towards arrears of depreciation, as per Statement V Column 6.
7. To Contribution towards contingencies Reserve as per Statement VI Columns 3.
   (a) To Appropriation towards development reserve as per statement VII columns 4 or 8 or 4 plus 8.
8. To Appropriation to Tariffs and dividends Control Reserve, as per Statement VII column 3.
   (b) To Appropriation to Consumers Rebate Reserve, as per Statement VIII column 4.
   (c) To Other special appropriation permitted by the State Govt., as per Column 3 of Statement IX.
Advanced Financial Accounting

(d) To Appropriation towards interest paid and accrued and dividends paid/payable.
   (a) Interest on debentures.
   (b) Interest on other secured loans.
   (c) Interest on unsecured loans, advances, deposits, bank overdrafts etc.
   (d) Dividends on preference share capital.
   (e) Dividends on ordinary share capital.
   To Balance of profit carried over.

General Balance Sheet as on 31 March, 19......

<table>
<thead>
<tr>
<th>Figures for last year</th>
<th>Particulars</th>
<th>Amount</th>
<th>Figures for last year</th>
<th>Particular</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td></td>
<td>Rs.</td>
</tr>
<tr>
<td></td>
<td>appropriated vide statement</td>
<td></td>
<td>on Works in use</td>
<td>Reserve and Surplus</td>
<td>1.</td>
</tr>
<tr>
<td></td>
<td>I or I-A</td>
<td>Reserve and Surplus</td>
<td>1.</td>
<td>Less : Accumulated provision for depreciation</td>
<td>1.</td>
</tr>
<tr>
<td>2.</td>
<td>Non Statutory Reserve.</td>
<td>2.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Contingencies Reserve Fund</td>
<td>3.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>as per Statement VI.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Tariffs and Dividends Control</td>
<td>4.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Reserve as per Statement VII.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Consumers' Rebate Reserve as per statement VIII.</td>
<td>5.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Special appropriations (as permitted by the State Govt.)</td>
<td>6.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>reserve as per Statement IX.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Current Liabilities and Provisions</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8.</td>
<td>Balance due on construction of Plant Machinery etc.</td>
<td>8.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>9.</td>
<td>Creditors on open accounts (as per schedule attached)</td>
<td>9.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(a) Fuel-Coal and/or oil etc. at cost.
(b) General Stores at or below cost,
Debtors for amount paid in advance on account of contracts,
Sundry debtors for electricity supplied.
Banking, Electricity, Insurance and Consequential Loss

11. Accounts payable (to be specified)  
12. Temporary accommodations, bank overdraft

7. Other debtors (as per schedule attached)
8. Accounts receivable (to be specified)
9. Investments in statutory securities at cost:
   (a) Contingencies Reserve Fund Investment
   (Market value on cl. date)
   (b) Depreciation Reserve Fund Investment
   (Market value on cl. date)
   (c) Other Investments
   (Market value on cl. date)

Illustration 4:
The following balances are extracted from the Books of Account of Vidut Electric Supply Company Ltd., for the year ended 31st March, 1999:

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Licence</td>
<td>9,000</td>
</tr>
<tr>
<td>Land (addition during the year Rs. 10,000)</td>
<td>2,10,000</td>
</tr>
<tr>
<td>Building</td>
<td>12,18,000</td>
</tr>
<tr>
<td>Plant and Machinery</td>
<td>2,04,000</td>
</tr>
<tr>
<td>Transformer substation</td>
<td>83,70,000</td>
</tr>
<tr>
<td>Mains-overhead and underground (additions during the year Rs. 17,70,000)</td>
<td>2,84,25,000</td>
</tr>
<tr>
<td>Meter House Service Connection</td>
<td>32,10,000</td>
</tr>
<tr>
<td>(additions during the year Rs. 2,25,000)</td>
<td></td>
</tr>
<tr>
<td>Furniture and Fixture</td>
<td>3,30,000</td>
</tr>
<tr>
<td>(additions during the year Rs. 21,000)</td>
<td></td>
</tr>
<tr>
<td>Motor Lorries (additions during the year Rs. 50,000)</td>
<td>3,15,000</td>
</tr>
<tr>
<td>Investments of Contingency Reserves (in Government Securities)</td>
<td>4,80,000</td>
</tr>
<tr>
<td>Purchase of Energy</td>
<td>62,25,000</td>
</tr>
<tr>
<td>Salaries and Wages</td>
<td>12,00,000</td>
</tr>
</tbody>
</table>
Advanced Financial Accounting

Repairs and Maintenance:
- Building: 22,500
- Plant & Machinery: 7,500
- Transformers: 90,000
- Mains and Services: 5,10,000
- Lorries: 18,000
- Establishment Expenses: 19,95,000
- Rent, Rates and Taxes: 76,500
- Conveyance and Traveling: 60,000
- Audit Fees: 22,500
- General Expenses: 1,50,000
- Electricity Duty: 10,50,000
- Directors: Fees and Allowances: 25,500
- Interest on Fixed Loans: 3,52,500
- Interest on Consumers 'Security' Deposits: 1,20,000
- Current Assets: 33,00,000
- Work-in-progress: 19,20,000
- Sundry Debtors: 40,50,000
- Cash and Bank Balances: 21,00,000
- Loans and Advances: 10,50,000
- Total: 6,71,16,000

Credit Balances

- Share Capital: Rs. 8,00,000
  - Equity Shares of Rs. 10 each: 75,00,000
  - 3,00,000 7 percent Preference share of Rs. 10 each: 30,00,000
- Reserve for Rebate to Consumers: 2,11,500
- Contingency Reserve: 4,80,000
- Tariff and Dividend Control Reserve: 2,10,000
- Development Reserve: 9,18,000
- Accumulated Depreciation: 2,40,000
- Balance of Net Revenue Account brought forward from previous year: 22,500
- Loan from State Government (secured by charge on Fixed Assets): 49,50,000
- Loan from State Electricity Board: 5,70,000
- Sundry Creditors: 25,74,000
- Consumers' Security Deposits: 48,00,000
- Unclaimed Dividends: 2,25,000
Banking, Electricity, Insurance and Consequential Loss

Sale of Energy 1,74,75,000
Rental of metres 1,05,000
Maintenance of Public Lamps 22,500
Hire on Machinery and Goods 37,500
Interest on bank accounts 15,000
Total 6,71,16,000

The following adjustments have to be made

(1) Depreciation for the year 17,25,000
(2) Provision for taxation 22,80,000
(3) Transfer to Contingency Reserve 2,25,000
(4) Transfer to Development Reserve 1,20,000

The amount of reasonable return may be presumed to be Rs. 11,94,000.

You are required to prepare Capital Account, Net Revenue Account and General Balance Sheet of the Vidvut Electric Supply, Company Ltd., in the prescribed form.

**STATEMENT No. I**

**Statement of Share and Loan Capital for the year ended 31st March, 1999**

<table>
<thead>
<tr>
<th>Description of Capitol</th>
<th>Balance at the beginning of the year</th>
<th>Receipts during the year</th>
<th>Redeemed during the year</th>
<th>Balance at the end of the year</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Share Capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Authorised</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Issued</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Subscribed Capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7,50,000 Equity Shares</td>
<td>75,00,000</td>
<td>...</td>
<td>...</td>
<td>75,00,000</td>
<td></td>
</tr>
<tr>
<td>of Rs. 10 each 7%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3,00,000 Equity Shares</td>
<td>30,00,000</td>
<td>...</td>
<td>...</td>
<td>30,00,000</td>
<td></td>
</tr>
<tr>
<td>Preference Shares</td>
<td>1,05,00,000</td>
<td>...</td>
<td>...</td>
<td>1,05,00,000</td>
<td></td>
</tr>
<tr>
<td>of Rs. 10 each 7%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Capital Reserve</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>C. Loan Capital Loan from State Govt.</td>
<td>49,50,000</td>
<td>...</td>
<td>...</td>
<td>49,50,000</td>
<td></td>
</tr>
<tr>
<td>State Electricity, Board</td>
<td>5,70,000</td>
<td>...</td>
<td>...</td>
<td>5,70,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>55,20,000</td>
<td>...</td>
<td>...</td>
<td>55,20,000</td>
<td></td>
</tr>
</tbody>
</table>
Other Capital Total  
Capital raised and Appropriated  
(A+B+C+D)  
1, 60,20,000  
...  
...  
1,60,20,000  

**STATEMENT No. II**  
Statement of Capital Expenditure for the year ended 31 March 1999  

<table>
<thead>
<tr>
<th>Particulars</th>
<th>2 Balance at the Beginning of the year</th>
<th>3 Addition during the year</th>
<th>4 Retirements during the year vide col. 3 statement IIA</th>
<th>5 Balance at the end of the year</th>
<th>6 Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Intangible Assets</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Licence</td>
<td>9,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Hydraulic power plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>C. Steam Power Plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>D. Internal Combustion Power Plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>E. Transmission Plant:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Land</td>
<td>2,00,000</td>
<td>10,000</td>
<td></td>
<td>2,10,000</td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>12,18,000</td>
<td></td>
<td></td>
<td>12,18,000</td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>2,04,000</td>
<td></td>
<td></td>
<td>2,04,000</td>
<td></td>
</tr>
<tr>
<td>F. Distribution Plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>High Voltage</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>G. Distribution Plant Medium and low voltage Mains</td>
<td>2,66,55,000</td>
<td>17,70,000</td>
<td></td>
<td>2,84,25,000</td>
<td></td>
</tr>
<tr>
<td>Transformers</td>
<td>83,70,000</td>
<td></td>
<td></td>
<td>83,70,000</td>
<td></td>
</tr>
<tr>
<td>Meter–House–Services Connection</td>
<td>29,85,000</td>
<td>2,25,000</td>
<td></td>
<td>32,10,000</td>
<td></td>
</tr>
<tr>
<td>H. Public Lighting</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>I. General Equipment</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Furniture &amp;Fixtures</td>
<td>3,09,000</td>
<td>21,000</td>
<td></td>
<td>3,30,000</td>
<td></td>
</tr>
<tr>
<td>Motor</td>
<td>2,65,000</td>
<td>50,000</td>
<td></td>
<td>3,15,000</td>
<td></td>
</tr>
<tr>
<td>Total Capital Assets in use</td>
<td>4,02,15,000</td>
<td>20,76,000</td>
<td></td>
<td>4,22,91,000</td>
<td></td>
</tr>
</tbody>
</table>

**Note:** In the absence of separate details regarding assets under different heads, they have been shown under headings clubbed together.
## STATEMENT No. III
### Statement of Operating Revenue for the year ended 31st March, 1999

<table>
<thead>
<tr>
<th>Particulars of revenue</th>
<th>Corresponding amount for the previous year of account</th>
<th>Amount for the year of account</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Net Revenue by Sale of Electricity for Cash and Credit</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Domestic and residential:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Commercial:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Industrial:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Public Lighting:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Public Water-works &amp; Sewage pumping:</td>
<td>1,74,75,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Irrigation:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. Traction:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8. Supplies in bulk:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Miscellaneous Revenue from Consumers:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rental of Meters</td>
<td>1,05,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Maintenance of public lamps</td>
<td>22,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>C. Other Revenues:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hire on machinery and goods</td>
<td>37,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Operating Revenues</td>
<td>1,76,40,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deduct:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Operating Expenses as per Statement IV</td>
<td>1,31,77,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net Surplus carried to Net. Revenue and Appropriation A/c</td>
<td>44,62,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### Statement of Operating Expenses for the year ended 31st March, 1999

<table>
<thead>
<tr>
<th>Particulars of Expenses</th>
<th>Corresponding amount for the previous year of account (Rs.)</th>
<th>Amount for the year of account (Rs.)</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Hydraulic Power Generation</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>B. Steam Power Generation</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>C. Internal Combustion Power Generation</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>D. Power Purchased Total Production</td>
<td>62,25,000</td>
<td>62,25,000</td>
<td>–</td>
</tr>
<tr>
<td>(A+B+C+D)</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>E. Transmission (High or Extra High Voltage)</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>F. Distribution (High Voltage)</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>G. Distribution (Medium and Low Voltage)</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Salaries and Wages</td>
<td>–</td>
<td>12,00,000</td>
<td>–</td>
</tr>
<tr>
<td>Repairs and Maintenance</td>
<td>–</td>
<td>6,48,000</td>
<td>–</td>
</tr>
<tr>
<td>Total Distribution costs</td>
<td>–</td>
<td>18,48,000</td>
<td>–</td>
</tr>
<tr>
<td>H. Public Lighting</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>I. Consumers Servicing, Meter Reading, tilling Connecting, Accounting</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>J. Rates and Taxes</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>K. General Establishment Charges</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Establishment charges</td>
<td>–</td>
<td>19,95,000</td>
<td>–</td>
</tr>
<tr>
<td>Rent, Rates and Taxes</td>
<td>–</td>
<td>76,500</td>
<td>–</td>
</tr>
<tr>
<td>Conveyance and Traveling</td>
<td>–</td>
<td>60,000</td>
<td>–</td>
</tr>
<tr>
<td>Audit Fees</td>
<td>–</td>
<td>22,500</td>
<td>–</td>
</tr>
<tr>
<td>General Expenses</td>
<td>–</td>
<td>1,50,000</td>
<td>–</td>
</tr>
<tr>
<td>Electricity Duty</td>
<td>–</td>
<td>10,50,000</td>
<td>–</td>
</tr>
<tr>
<td>Total General Establishment Charges</td>
<td>–</td>
<td>33,54,000</td>
<td>–</td>
</tr>
<tr>
<td>L. Other Charges Depreciation</td>
<td>–</td>
<td>17,25,000</td>
<td>–</td>
</tr>
<tr>
<td>M. Management Expenses</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Directors fees</td>
<td>–</td>
<td>25,500</td>
<td>–</td>
</tr>
<tr>
<td>Total Operating Expenses</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>Transferred to Statement III</td>
<td>–</td>
<td>1,31,77,500</td>
<td>–</td>
</tr>
</tbody>
</table>
### Banking, Electricity, Insurance and Consequential Loss

**STATEMENT - X**

Statement of Net Revenue and Appropriation Account

*for the year ended 31 March 1999*

<table>
<thead>
<tr>
<th>Figures for last year Rs.</th>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Figures for last year Rs.</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Appropriation to Tariff and Dividend control reserve</td>
<td>63,150</td>
<td>By Balance of profit brought forward from last account.</td>
<td>22,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Provision for Taxation</td>
<td>22,80,000</td>
<td>By Balance brought from Revenue A/c</td>
<td>44,62,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Appropriation to Development Reserve</td>
<td>1,20,000</td>
<td>By Interest on Bank A/c</td>
<td>15,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Appropriation to consumers Rebate Reserve</td>
<td>63,150</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest on Security Deposits</td>
<td>1,20,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest on Fixed Loans</td>
<td>3,52,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Appropriation to Contingency Reserve</td>
<td>2,25,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Balance of profit carried over</td>
<td>12,76,200</td>
<td>45,00,000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**General Balance Sheet**

*as on 31st March, 19......*

<table>
<thead>
<tr>
<th>Figures for last year Rs.</th>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Figures for last year Rs.</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital Reserve and appropriated vide Statement No 1 Reserve and Surplus: Contingency Reserve 'Tariffs and Dividends Control Reserve Consumers' Rebate Reserve Development</td>
<td>1,60,20,000 4,80,000 2,10,000 2,11,500</td>
<td>1,60,20,000 7,05,000 2,73,150 2,74,650</td>
<td>4,02,15,000 2,40,000,000 1,62,15,000 2,73,150 2,74,650</td>
<td>Capital amount expended on Works in use-Statement It. Less: Accumulated provision for depreciation Net Block Balance of written down cost of obsolete.. inadequate etc. Current Assets:</td>
<td>4,22,91,000 2,57,25,000 1,65,66,000</td>
</tr>
</tbody>
</table>
Working Note:

\[\text{Rs.} \]

Profit after interest or clear profit  \(13,80,000\)
Reasonable Return  \(11,94,000\)
Surplus  \(1,86,000\)

1/3 of surplus, i.e. Rs.62,000 subject to
5% of Reasonable Return is to remain
at the disposal of the undertaking  \(59,700\)
Balance  \(1,26,300\)
1/2 of the balance to Tariff and Dividend Control  \(63,150\)
Balance available for benefit of consumers  \(63,150\)

Replacement of Asset:

Ordinarily, the amount standing in books against an asset is written off when the asset is replaced by another. The amount spent on the new asset is capitalised. Under the Double Account System, however, the practice is different, Firstly, the account of the asset which is replaced is not affected at all. An appropriate amount out of the new expenditure is charged to revenue or written off and the balance is capitalised. Secondly, the amount to be written off is the amount which would have been spent had the asset been acquired now.

Suppose, a railway station built in 1990 at a cost of Rs.3,00,000 is replaced, in 1996, by a new station costing Rs. 16,00,000, Suppose further that between 1990 and 1996, prices of materials have risen to 2.50%, that labour rates have trebled and that the proportion of materials and labour in the old station is 4.6.

The amount to be written off will be arrived at as under

- Total cost of the old station  \(3,00,000\)
- Proportion of Materials  \(3,00,000 \times 4/10 \text{ or } 1,20,000\)
- Proportion of Labour  \(3,00,000 \times 6/10 \text{ or } 1,80,000\)
Banking, Electricity, Insurance and Consequential Loss

Had the station been built in 1996,

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr Rs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Materials would have cost, and</td>
<td>1,20,000 x 250/100 = 3,00,000</td>
</tr>
<tr>
<td>Labour would have cost</td>
<td>1,80,000 x 3 = 5,40,000</td>
</tr>
<tr>
<td>Total</td>
<td>8,40,000</td>
</tr>
</tbody>
</table>

Out of Rs. 16,00,000 spent in 1996, Rs. 8,40,000 would be written off and Rs. 7,60,000 i.e. (16,00,000 – 8,40,000) would be capitalised. The total amount capitalised is Rs. 10,60,000 i.e. Rs. 3,00,000 + Rs. 7,60,000.

The entries to be made are as follows —

1. Debit Replacement Account with the amount to be written off, Debit Works Account (new) with the amount to be capitalised and Credit Bank with the amount actually spent.

2. If any old materials have been used in the new construction : Debit Works Account Credit Replacement Account.

3. If any old materials have been sold.
   Debit Bank
   Credit Replacement Account.

The logic behind the treatment outlined above is firstly, that additional amount should be capitalised only if there is additional capacity and, secondly, that, when an old asset is replaced, the amount lost is the asset present value rather than its historical cost.

Illustration 5:

The Hindustan Gas Company rebuilt and reequipped part of their works at a cost of Rs. 5,00,000. The part of the old works thus superseded cost Rs. 3,00,000. The capacity of the new works is double the capacity of the old works. Rs. 20,000 is realised by the sale of old materials, and old materials worth Rs. 10,000 are used in the construction of the new works and included in the total cost of Rs. 5,00,000 mentioned above. The costs of labour and materials are 25% higher now than when the old works were built. Journalise the entries.

Solution:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr Rs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Replacement Account</td>
<td>Dr. 3,75,000</td>
</tr>
<tr>
<td>New Works Account</td>
<td>Dr. 1,15,000</td>
</tr>
<tr>
<td>To Bank</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,90,000</td>
</tr>
</tbody>
</table>

Being the amount written off (Rs. 3,00,000 + 25%) and the amount capitalised out of the Rs. 4,90,000 spent on reconstruction in cash i.e., 5,00,000 - 10,000)
Advanced Financial Accounting

New Works Account Dr. 10,000
To Replacement Account 10,000
(Being the materials used in the new works)

Bank Dr. 20,000
To Replacement Account 20,000
Being the amount realised by the sale of old materials.

6.3 ACCOUNTS OF INSURANCE COMPANIES

In order to provide some coverage for the risk exposure of the business especially from fire, a businessman takes an insurance policy. Usually two types of losses are covered under the policy.

(i) loss of stock, plant, buildings etc. and
(ii) loss of profits due to dislocation of the business.

Loss of Stock

A fire insurance policy compensates the insured for any loss that he may suffer on account of loss of stock due to fire in consideration of a certain amount being paid as premium. The value of stock lost on account of fire can be determined by finding out the value of stock on the date of fire less the value of the salvaged stock.

The value of stock can also be ascertained by compiling a Memorandum Trading Account wherein balancing figure will be value of stock.

Factors determining amount of claim.

(i) *Rate of Gross profit:* The rate of gross profit is determined on the basis of the performance of the business during the preceding 3-4 years. Abnormal factors during the same period are eliminated. If gross profit percent reflects a definite trend weighted average method is employed for finding the average gross profit.

(ii) *Average clause:* The insurance company in order to discourage under-insurance limits its liability to the proportion of the actual amount of loss which the insured amount bears to the actual value of the property e.g., stock work Rs. 1,00,000 is insured only for Rs.80,000 and if the loss amount to Rs.10,000, the claim will be

\[ \text{Claim} = \text{Amount of Loss} \times \left( \frac{\text{Amount of Policy}}{\text{Actual value of stock}} \right) \]

\[ = 20,000 \times \left( \frac{80,000}{1,00,000} \right) = \text{Rs.16,000} \]
The average clause is applicable only if it is proved that the loss sustained by the insured is less than the sum insured. However, when the loss is more than the sum insured, the insured can recover the whole amount in spite of the average clause.

**Illustration 6:**
Kamal Fair Price Shop suffered loss of stock due to fire on August 20, 1997. From the following particulars calculate claim to be made by the shop:

1. Stock on December 31, 1995
   (including stock purchased during the year at Rs. 8,000 valued at Rs. 4,000 because of poor selling price)

2. Wages paid - 1996
   (including wages paid for the construction of a showroom for which worker of the factory worked, Rs. 2,000. Manufacturing wages Rs. 1,500 were outstanding)

3. Freight inwards - 1996

4. Purchases - 1996
   (including purchases of furniture of Rs. 1500 wrongly passed through invoice book)

5. Sales - 1996
   (including sale of 1/4 of the stock at Rs. 1000. which had a poor selling line and which was valued at Rs. 4000 on Dec. 31, 1995)

6. Stock on December 31, 1996
   (including remaining stock which had a poor selling line at the same value)

7. Purchases - up to August 20, 1997

8. Sales - up to August 20, 1997
   (including sale of the 1/3 remaining stock which had a poor selling line at Rs. 800).

The remaining stock which had a poor selling line, was considered, at 80% of the original cost for the purpose of claim. The salvage was Rs. 47,400. The shop had taken the policy of Rs. 40,000. There was an average clause in the policy.
**Advanced Financial Accounting**

**Solution:**

**Statement of Normal Gross Profit for 1996**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales (exceeding poor line sale of Rs. 1000)</td>
<td>Rs. 2,45,000</td>
</tr>
<tr>
<td>Less: Cost of goods sold (other than of poor line)</td>
<td></td>
</tr>
<tr>
<td>Opening Stock (excluding poor line)</td>
<td>96,000</td>
</tr>
<tr>
<td>Purchases (excluding furniture of Rs. 1500)</td>
<td>1,18,500</td>
</tr>
<tr>
<td>Wages (paid Rs.30000 plus outstanding Rs. 1500)</td>
<td>29,500</td>
</tr>
<tr>
<td>Less: for showroom construction Rs.2000)</td>
<td></td>
</tr>
<tr>
<td>Freight</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>2,49,000</td>
</tr>
<tr>
<td>Less: Closing Stock (excluding Rs. 3000 of poor line)</td>
<td>39,000</td>
</tr>
<tr>
<td>Gross Profit (G.R)</td>
<td>35,000</td>
</tr>
<tr>
<td>G.P. Ratio to sales (35,000/2,45,000) = 1/7</td>
<td></td>
</tr>
</tbody>
</table>

**Statement of Unsold Stock on August 20, 1997 (date of Fire)**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock as at 1 January, 1997 (excluding of poor line)</td>
<td>39,000</td>
</tr>
<tr>
<td>Add: Purchase to date of fire</td>
<td>1,42,800</td>
</tr>
<tr>
<td>Cost of goods available for sale (excluding of poor line)</td>
<td>1,81,800</td>
</tr>
<tr>
<td>Less: Cost of sales (or normal selling line) up to fire date;</td>
<td></td>
</tr>
<tr>
<td>Sales (excluding Rs.800 of poor line)</td>
<td>1,42,100</td>
</tr>
<tr>
<td>Less: 1/7 being gross profit:</td>
<td>20,300</td>
</tr>
<tr>
<td>Stock of normal selling line at fire date</td>
<td>1,21,800</td>
</tr>
<tr>
<td>Add: Admissible value of poor line stock i.e.80% of the original</td>
<td></td>
</tr>
<tr>
<td>cost of Rs.4000 remaining unsold up to date of fire</td>
<td>3,200</td>
</tr>
<tr>
<td></td>
<td>63,200</td>
</tr>
<tr>
<td>Less: Salvage</td>
<td>47,400</td>
</tr>
<tr>
<td>Stock Lost by fire</td>
<td>15,800</td>
</tr>
<tr>
<td>Amount of claim having regard to average clause :</td>
<td></td>
</tr>
<tr>
<td>Lost Stock × (Policy Amount ÷ Stock at fire date)</td>
<td></td>
</tr>
<tr>
<td>= 15,800 × (40,000 ÷ 63,200) = Rs. 10,000</td>
<td></td>
</tr>
</tbody>
</table>
Banking, Electricity, Insurance and Consequential Loss

6.4 LOSS OF PROFITS OR CONSEQUENTIAL LOSS

Fire results not only in loss of property but also loss of profits to the business on account of its dislocation. Such a loss can be got covered by taking a loss of profits policy.

Amount of Policy

Considerable care should be exercised in determining the amount for which a loss policy should be taken. The policy should adequate to cover the likely amount of loss, which the insured may suffer on account of dislocation of the business. The policy specifies both the period as well as the amount it covers. While determining the amount of policy the insured should take into account not only the amount of net profit, he earns but also the amount of standing or fixed charges which have been charged against the revenue for determining the amount of net profit. Of course, he may not get such incomes covered by the insurance policy which will not be affected by dislocation of his business on account of fire. e.g. income from investments, rent from the property let out etc.

Computation of Claim:

Loss of profit occurs because of loss of sales on account of dislocation of the business. Moreover, the insured may have to incur certain additional expenses to mitigate the amount of loss. There may also be certain savings in expenses of the business because of its being closed down for some period. All these have to be taken into account while calculating the amount of insurance claim. This has been explained below:

1. **Short sales**: The term short sales refers to the loss of sales on account of fire resulting in dislocation of business. This is the difference between the "standard turnover" and the "actual turnover" during the period of fire.

Computation of short sales requires the understanding of the following terms

(a) **Standard turnover**: The term standard turnover refers to the turnover for the period corresponding with the indemnity period during the preceding accounting year adjusted in view of the trends noticed during the accounting year in which the fire occurred.

(b) **Indemnity Period**: The term indemnity period refers to the period beginning with the occurrence of the damage and ending not later than 12 months there after during which the results of the business shall be affected in consequence of the damage. This period is selected by the insured himself. It is not necessary for the policy to cover the entire indemnity period. Of course, it is essential that on the date of fire leading to partial or complete closure of the business activity the policy must be in force.
Illustration 7:

Fire occurs on 1st March, 1999 resulting in dislocation of the business activities for a period of 3 months. During the same period the sales in the last year amounted to Rs.10000. However, during the current year beginning with 1st January 1999, the sales were showing an increasing trend of 10%. The actual sales during the period of dislocation amounted to Rs. 4000. Calculate the short sales.

Solution:

Computation of short sales

\[
\text{Rs.}
\]

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard turnover (Rs.10,000 + Rs.1,000)</td>
<td>11,000</td>
</tr>
<tr>
<td>Less: Actual sales during the period of dislocation</td>
<td>4,000</td>
</tr>
<tr>
<td>Short sales</td>
<td>7,000</td>
</tr>
</tbody>
</table>

2. Rate of gross profit: The term gross profit has got a different meaning than that in which it is commonly understood. It is ascertained as follows:

\[
\text{Net Profit + Insured Standing Charges} \times \frac{100}{\text{Turnover}}
\]

All the figures relating to net profit, insured standing charges and turnover relate to the last period.

In case of net loss the rate of gross profit will be determined as follows:

\[
\text{Insured standing charged - Net loss} \times \frac{100}{\text{Turnover}}
\]

If all the standing charges are not insured, the amount of net loss will have to be reduced as follows:

\[
\text{Net loss} \times \frac{\text{Insured standing charges}}{\text{All standing charges}}
\]

3. Loss due to short sales: The loss due to sales is calculated by applying the rate of gross profit to short sales. For example, if the short sales are Rs.7000 and the rate of gross profit 20% the loss of profit on account of short sales amounts to Rs.1400 i.e. Rs.7000 \times 20/100

4. Increased cost of working: The insured may have to incur certain, additional expenses to keep the business running during the indemnity period. Such increased working expenses will be allowed subject to the limit which is lower of the two figures calculated as follows.

\[
(a) \quad (\text{Net Profit + Insured Standing Charges}) \times \frac{\text{Increased cost of working}}{\text{Net Profit + All Standing Charges}}
\]

\[
(b) \quad \text{Short sales avoided through increased cost of working} \times \text{Rate of gross profit}
\]

5. Saving in expenses: Any saving in expenses will have to be deducted from the amount calculated as explained above.

6. Average clause: Finally the amount calculated will be proportionally reduced if the sum insured under the policy is less than the amount for which the policy should have been taken.
Banking, Electricity, Insurance and Consequential Loss

The amount for which the policy should have been taken is determined by applying the rate of gross profit to the turnover for 12 months immediately preceding the date of fire. Such turnover may have to be adjusted keeping in view, the trend of sales in the accounting year in which the fire occurs.

Illustration 8:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Short sales</td>
<td>20,000</td>
</tr>
<tr>
<td>Increased working expenses</td>
<td>1,000</td>
</tr>
<tr>
<td>Rate of gross profit</td>
<td>20%</td>
</tr>
<tr>
<td>Saving in expenses</td>
<td>200</td>
</tr>
<tr>
<td>Sales during 12 months immediately</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Amount of policy</td>
<td>15,000</td>
</tr>
</tbody>
</table>

The sales are showing an increasing trend of 10% since the commencement the accounting year.

Calculate the amount of claim to be admitted by the insurance company.

Solution:

Loss of profit due to short sales : \( (20,000 \times 20/100) \) = 4,000

Increased working expenses = 1,000

Less: Saving in expenses = 200

Claims for loss of profit and increased working expenses = 4,800

However, the above claim will be subject to the average clause Amount for which the policy should have been taken : \( (1,10,000 \times 20 / 100) \) = 22,000

Amount for which the policy has been taken = 15,000

Amount of claim to be admitted by the insurance company

\[ \text{Amount of claim} = \frac{(\text{Amount of claim} \times \text{Amount of policy})}{\text{Amount for which the policy should have been taken}} \]

\[ = \frac{4,800 \times 15,000}{22,000} = \text{Rs. 3,273} \]

Illustration 9:

A fire occurred in the premises of a businessman on 31st January, 1997, which destroyed most of the building. However, stock worth Rs. 5,940 was salvaged. The company insurance policy covers the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock</td>
<td>Rs. 9,00,000</td>
</tr>
<tr>
<td>Building</td>
<td>Rs. 12,00,000</td>
</tr>
<tr>
<td>Loss of Profit (including standing charges)</td>
<td>Rs. 3,75,000</td>
</tr>
</tbody>
</table>

Period of indemnity - six months
Advanced Financial Accounting

The summarised Profit & Loss Account for the year
ended 31st December, 1996

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover</td>
<td>30,00,000</td>
</tr>
<tr>
<td>Closing Stock</td>
<td>7,87,500</td>
</tr>
<tr>
<td>Opening Stock</td>
<td>6,18,750</td>
</tr>
<tr>
<td>Purchases</td>
<td>27,18,750</td>
</tr>
<tr>
<td>Standing Charges</td>
<td>2,51,250</td>
</tr>
<tr>
<td>Variable Expenses</td>
<td>1,20,000</td>
</tr>
<tr>
<td></td>
<td>37,08,750</td>
</tr>
<tr>
<td></td>
<td>78,750</td>
</tr>
</tbody>
</table>

The transactions for the month of January, 1997 were as under:

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Payments to Creditors</td>
<td>1,60,020</td>
</tr>
<tr>
<td>Trade Creditors: Balance as on 1/1/1997</td>
<td>2,26,000</td>
</tr>
<tr>
<td>Trade Creditors Balance as on 31/1/1997</td>
<td>2,30,980</td>
</tr>
</tbody>
</table>

The company's business was disrupted until 30/4/1997, during which period the reduction in turnover amounted to Rs. 2,70,000 as compared with the turnover of same period corresponding in the previous year.

Building was worth Rs.15,00,000 on the date of fire and three quarters of its value was lost by fire. You are required to submit the claim for insurance for loss of stock, loss of building and loss of profit.

Solution:

(1) **Claim for loss of stock**

Memorandum Trading Account for the month ending 31st January, 1997

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td>7,87,500</td>
</tr>
<tr>
<td>To Purchases I Note 4 (ii)</td>
<td>1,65,000</td>
</tr>
<tr>
<td>To Gross Profit @15%</td>
<td>22,500</td>
</tr>
<tr>
<td></td>
<td>9,75,000</td>
</tr>
</tbody>
</table>

Closing stock as on 31st January, 1987 8,25,000

Less : Stock Salvaged 5,940

Claim for stock 8,19,060

(2) **Claim for loss of profit**

Short sales 2,70,000

Gross Profit Ratio [Note (iii)] 11%

Gross Profit on Short Sales 29,700

(3) **Claim for loss of Building**
Banking, Electricity, Insurance and Consequential Loss

Loss of Building, 3/4 of Rs 15,00,000 = 11,25,000
This building is insured for Rs.12,00,000 only
Hence, the claim will be subject to the average clause presuming that the policy contains such a clause.

3. Amount of claim = (Amount of Loss × Sum Assured)/Value of the Property
   = 11,25,000 × (12,00,000 ÷ 15,00,000) = Rs.9,00,000

4. Total Claim (8,19,060 + 29,700 + 9,00,000) = Rs.17,48,760

Working Notes:
Rate of Gross Profit for the year ending 31st December 1996

(i) Trading Account for the Year ending 31st December 1996

<table>
<thead>
<tr>
<th></th>
<th>Opening Stock</th>
<th>Sales</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>To</td>
<td>6,18,750</td>
<td>By Sales 30,00,000</td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Purchases 27,18,750</td>
<td>By Closing stock 7,87,500</td>
<td></td>
</tr>
<tr>
<td>To</td>
<td>Gross Profit 4,50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>37,87,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Rate of Gross Profit comes to 15% (i.e. Rs. 4,50,000 / 30,00,000)

(ii) Total Creditors Account

<table>
<thead>
<tr>
<th></th>
<th>1987 To Bank 1,60,020</th>
<th>1987 By Balance 2,26,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jan. 31 To Balance c/d 2,30,980</td>
<td>Jan. 1 By Purchases (balancing figure) 1,65,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,91,000</td>
<td>3,91,000</td>
</tr>
</tbody>
</table>

(iii) Calculation of Gross Profit Ratio for Loss of Profit:
Sales for 1986 30,00,000
Net Profit + Insured standing charges
Net Profit 78,750
Standing Charges (assumed all insured) 2,51,250 3,30,000
Rate of gross profit (3,30,000 / 30,00,000) 11%
6.5 QUESTIONS WITH SKELETON ANSWERS

1. Write short notes on the following:
   (b) Non-Performing assets.
   (c) Classification of Advances in the case of a banking company.
   (d) Sub system of Posting.

2. The following are the ledger balances of X Bank Limited owning its premises. You are required to prepare Profit and Loss Account and Balance Sheet as on 31st March, 1992 as per the banking regulation Act. Also append the usual Auditors certificate to Profit and Loss Account and the Balance Sheet.

\[
\begin{array}{|l|c|}
\hline
\text{Item} & \text{Amount (Rs. in '000)} \\
\hline
\text{Share Capital} & 20,00,000 \\
\text{Bad debts written off} & 1,28,710 \\
\text{Reserve Fund Investments} & 10,00,000 \\
\text{General Expenses} & 1,82,420 \\
\text{Current Account} & 2,02,44,220 \\
\text{Interest paid} & 1,60,520 \\
\text{Profit and Loss Account balance b/f} & 2,29,340 \\
\text{Acceptances for customers} & 15,42,820 \\
\text{Discount} & 2,43,760 \\
\text{Endorsements and Guarantees} & 74,020 \\
\text{Commission} & 44,240 \\
\text{Cash} & 2,26,540 \\
\text{Interest received} & 5,32,260 \\
\text{Cash with Reserve Bank} & 20,12,100 \\
\text{Endorsements and Guarantees per contra} & 74,020 \\
\text{Owing by foreign correspondents} & 2,00,440 \\
\text{Customers' Liabilities for acceptances} & 15,42,820 \\
\text{Short Loans} & 64,82,060 \\
\text{Loans and advances to customers} & 1,54,56,700 \\
\text{Investments} & 98,82,540 \\
\text{Bills discounted} & 62,28,240 \\
\text{Non-banking assets (estimated liabilities value Rs. 1,95,000)} & 2,10,000 \\
\hline
\end{array}
\]

Note: Reserve Rs.643,80,000 for rebate on bills discounted. The Profit and Loss Account balance in the balance left on that account after the payments of interim dividend of Rs. 20,00,00,000.

[Value of premises Rs. 200,79,00,000, Net Profit 26,92,30,000 ; Total of Balance Sheet Rs. 38,82,63,00,000]
3. Fire occurred in the premises of AB&C Company on 1st September, 1990 and stock of the value of Rs. 1,01,000 was salvaged and the business books and records were saved. The following information was obtained: -

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchases for the year ended 31st March, 1990</td>
<td>6,80,000</td>
</tr>
<tr>
<td>Sales for the year ended 31st March, 1990</td>
<td>11,00,000</td>
</tr>
<tr>
<td>Purchases from 31st March to 1st September, 1990</td>
<td>2,50,000</td>
</tr>
<tr>
<td>Sales from 31st March to 1st September, 1990</td>
<td>3,60,000</td>
</tr>
<tr>
<td>Stock on 31st March, 1989</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Stock on 31st March, 1990</td>
<td>3,40,000</td>
</tr>
</tbody>
</table>

Further information is that stock on 31st March, 1990 was overvalued by, Rs. 20,000. Calculate the amount of the claim to be presented to the Insurance Company, in respect of the loss. In April, 1990 selling price was lowered by 10% (Gross Profit to Sales Ratio 4,40,000 x 100 / 1,00,000 = 40% 1989-90

Expected Gross Profit ratio 30 x 100 / 90 = 33 1/3% 1990-91
As New Selling Price = 100 - 10 = 90
Gross Profit = 40 - 10 = 30

Stock on 1st September 1990 3,30,000
Less:
Stock Salvaged 1,01,010
Claim for insurance 2,29,000

4. The Bharat Fisheries Limited insure their fleet of boats with Marine Insurance for Rs. 20,00,000 through an official Broker. Premium is charged at the rate 8% and brokerage at 5%, discount is allowed at the rate of 10%.

During the period of the cover, as a result of collision of one of the company's vessels Hero is damaged and the damage is assessed at an agreed amount of Rs. 20,000. Another vessel Pawan strikes against a submerged rock and is totally wrecked. The amount of loss is assessed at Rs. 70,000 without considering salvage value. Salvage Rs. 5,000 is retained by the Shipping Company. Book value of Pawan is Rs. 80,000.

The Broker collects the amounts due from the Insurance and make over the collections, less their collection commission @ 1% to the shipping company. All payments are duly made and received. Write up the Journal entries and show the transactions in the company's books.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Insurance Premium Gross 8% of Rs. 20,00,000</td>
<td>Rs. 1,60,000</td>
</tr>
<tr>
<td>Less: 10% of discount calculated on</td>
<td>1,60,000</td>
</tr>
<tr>
<td>Gross</td>
<td>8,000</td>
</tr>
<tr>
<td>Less: 5% brokerage</td>
<td>1,52,000 @ 10% 15,200</td>
</tr>
<tr>
<td></td>
<td>1,44,800</td>
</tr>
</tbody>
</table>
Advanced Financial Accounting

Journal Entries

<table>
<thead>
<tr>
<th>Dr</th>
<th>1,44,800</th>
</tr>
</thead>
<tbody>
<tr>
<td>Insurance Premium</td>
<td></td>
</tr>
<tr>
<td>To Broker</td>
<td>1,44,800</td>
</tr>
<tr>
<td>Broker</td>
<td>1,44,800</td>
</tr>
<tr>
<td>To Bank</td>
<td>1,44,800</td>
</tr>
<tr>
<td>Broker</td>
<td></td>
</tr>
<tr>
<td>To Repairs to Hero</td>
<td>20,000</td>
</tr>
<tr>
<td>Broker</td>
<td>65,000</td>
</tr>
<tr>
<td>Salvage</td>
<td>5,000</td>
</tr>
<tr>
<td>Marine Loss</td>
<td>10,000</td>
</tr>
<tr>
<td>To Pawan</td>
<td>80,000</td>
</tr>
<tr>
<td>Commission</td>
<td>850</td>
</tr>
<tr>
<td>To Broker</td>
<td></td>
</tr>
<tr>
<td>Bank</td>
<td>84,150</td>
</tr>
<tr>
<td>To Broker</td>
<td></td>
</tr>
<tr>
<td>(20,000 + 65,000 – 850)</td>
<td></td>
</tr>
</tbody>
</table>

5. The Electricity Company earned a profit of Rs.16,90,000 during the year ended March 31, 1990, after debenture interest at 7-1/2% on Rs.5,00,000 with the help of the figures given below. Show the disposal of the profits. Assume the bank rate to be 5%.

- Original cost of fixed assets: 2,00,00,000
- Formation and other expenses: 10,00,000
- Monthly average of fixed assets: 50,00,000
- Reserve Fund (represented by 4% Govt. securities): 20,00,000
- Contingencies Reserve Investments: 5,00,000
- Loan from Electricity Board: 30,00,000
- Total depreciation written off to date: 40,00,000
- Tariffs & Dividends Control Reserve: 1,00,000
- Security Deposits received from customers: 4,00,000

[Rs. 1,23,437 due to customers]

6. The premises of a company were partly destroyed by fire which took place on 1st March, 1992 and as a result of which the business was disorganized from 1st March to 31st July, 1992. Accounts are closed on 31st December every year. The company is insured under a loss of Profits Policy for Rs.7,50,000. The period of indemnity specified in the policy is 6 months. From the following information you are required to compute the amount of claim under the loss of Profits Policy.
Banking, Electricity, Insurance and Consequential Loss

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover for 1991</td>
<td>40,00,000</td>
</tr>
<tr>
<td>Net profits for the year 1991</td>
<td>2,40,000</td>
</tr>
<tr>
<td>Insured standing charged</td>
<td>4,80,000</td>
</tr>
<tr>
<td>Uninsured standing charges</td>
<td>80,000</td>
</tr>
<tr>
<td>Turnover during the period dislocation i.e. from 1/3/1992 to 31/7/1992</td>
<td>80,000</td>
</tr>
<tr>
<td>Standard turnover for the same period in the preceding year i.e. 1/3/91 to 31/7/91</td>
<td>20,00,000</td>
</tr>
<tr>
<td>Annual Turnover for the year immediately preceding the fire i.e. 1/3/91 to 29/2/92</td>
<td>44,00,000</td>
</tr>
<tr>
<td>Increased cost working</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Savings in insured standing charges</td>
<td>30,000</td>
</tr>
<tr>
<td>Reduction in turnover avoided through increased working cost</td>
<td>4,00,000</td>
</tr>
</tbody>
</table>

Owing to reasons acceptable to the insurer the, "special circumstances clause" stipulates for –
(a) Increase of turnover (standard and annual) by, 10% and
(b) Increase of rate of gross profit by 2%.

\[ \text{Gross Profit Ratio} = 20\% \quad \text{Amount of claim} = \text{Rs. 2,55,680} \]

7. The premises of Sulav Enterprise, a proprietary concern, were damaged by fire on 12th February, 1998. As a result, some trading stock was totally destroyed, and, in addition, stock costing Rs. 96,000 was partly damaged. The insurance company agreed to reduce the value of the damaged stock by Rs. 52,800. On 31st December, 1997, the stock-in-trade of the concern was valued at Rs. 4,12,000. Subsequently the following purchases were made:

<table>
<thead>
<tr>
<th>Date</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>8th January, 1998</td>
<td>1,09,920</td>
</tr>
<tr>
<td>21st January, 1998</td>
<td>72,000</td>
</tr>
<tr>
<td>27th January, 1998</td>
<td>5,360</td>
</tr>
<tr>
<td>14th February, 1998</td>
<td>42,400</td>
</tr>
<tr>
<td>20th February, 1998</td>
<td>2,24,000</td>
</tr>
<tr>
<td>8th March, 1998</td>
<td>1,37,600</td>
</tr>
</tbody>
</table>

Additional information for the three months ended on 31st March, 1998 are given below.
(a) 50 per cent of the damaged goods were sold before 31st March, 1998 at a profit of 15%.
(b) With the exception of the damaged goods, the firm has earned a gross profit of 30% of the cost of goods sold.
(c) The sales during the three months ended 31st March, 1998, were Rs. 6,54,360.
(d) The undamaged stock at 31st March, 1998, was valued at Rs. 2,03,280.
(e) The firm has an insurance cover for loss and damage to stock by fire.

Prepare a statement of insurance claim.