CHAPTER 1

Partnership Accounts—Fundamentals

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Partnership

Partnership is a relationship between persons who have agreed to share profits and losses of business carried on by all or any of them acting for all.

2. Partners

Partners are the persons who have agreed to do business and share its profits and losses.

3. Firm

Partners carrying on the business are collectively known as **firm**. The name under which the business is carried on is called **firm name**.

4. Partnership Deed

Partnership Deed is a written agreement among the partners detailing the terms and conditions of the partnership.

5. The Indian Partnership Act, 1932

It is an Act that governs the partnership firms. In case, Partnership Deed is silent on any issue, provisions of the Act apply.

6. Capital

Capital is the amount in credit of Partner's Capital Account. It may be contributed by the partners in the firm and/or credited by way of his or her share of profit, salary, commission and interest on capital. Capitals of the partners may be fixed or fluctuating.

7. Fixed Capitals

Fixed Capitals mean that capitals of the partners remain fixed and change only with the introduction or withdrawal of capital. When capitals are fixed two accounts for each partner are maintained, *i.e.*, Capital Account and Current Account.

8. Fluctuating Capitals

Fluctuating Capitals mean that capitals of the partners do not remain fixed but change with each entry. When capitals are fluctuating only one account is maintained for each partner, *i.e.*, Capital Account.

9. Drawings

Drawings means withdrawal by the partner from the firm in cash or kind for his or her personal use.

10. Profit-sharing Ratio

Profit-sharing Ratio is the ratio in which the partners have agreed to share profits and losses of the firm. In the absence of agreement, it is as provided in the Indian Partnership Act, 1932, *i.e.*, equal.

11. Capital Ratio

Capital Ratio means the ratio in which the partners shall maintain their capitals in the firm.

12. Guarantee of Profit

Guarantee of Profit means minimum profit guaranteed to a partner or partners of the firm. Guarantee may be given by a partner or partners or the firm.

13. Past Adjustments

Past Adjustments means adjustment made either for the errors or omissions in the books of the firm or for the wrong or incorrect distribution of profits made in the past year or years.

SUMMARY OF THE CHAPTER

Meaning of Partnership as per Section 4 of Indian Partnership Act, 1932

"Partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all."

Nature: A partnership firm has no separate legal entity apart from the partners constituting it.

Partners, Firm and Firm Name: The persons who have entered into partnership with one another are individually called **partners** and collectively a **firm**. The name under which the business of the firm is carried on is called the **firm name**.

Essential Elements, Main Features or Characteristics of Partnership

1. There must be two or more persons.
2. There must be an agreement.
3. There must be a lawful business.
4. There must be sharing of profits of business.
5. There must be a mutual agency, *i.e.*, the business must be either carried on by all or any of them acting for all.

Partnership Deed: The document containing the terms and conditions of the agreement between/among partners, is known as the **Partnership Deed**. The Partnership Deed usually includes the following:

(*i*) Name and address of the firm.
(*ii*) Names and addresses of all partners.
(*iii*) Date of commencement of partnership.
(*iv*) Capital to be contributed by each partner.
(*v*) Whether interest is to be allowed on capitals.
(*vi*) Whether any partner is to be allowed salary.
(*vii*) The profit-sharing ratio.
(*viii*) The duties of each partner.
(*ix*) Mode of settlement of accounts in case of retirement/death of a partner.

Benefits or Advantages of having a Partnership Deed

(*i*) It facilitates functioning of the business.
(*ii*) It is helpful in the settlement of all disputes arising among the partners.
(*iii*) It helps to avoid misunderstandings among the partners.

Provisions Applicable in the Absence of Partnership Agreement/Partnership Deed

1. Interest is not allowed on Partners' Capitals or charged on Drawings.
2. Partner is not entitled to salary or remuneration for the work done for the firm.
3. Interest @ 6% p.a. is allowed on the loans advanced by any partner.
4. Profit or loss is distributed equally among the partners.

Profit and Loss Appropriation Account is an *extension* of the Profit and Loss Account. The purpose of this account is to show how Net Profit is appropriated and distributed among the partners.

It is credited with Net Profit and interest on drawings.

It is debited with interest on capitals, salary or commission to partners as per the terms of Partnership Deed.

Its balance is transferred to the Partners' Capital (or Current) Accounts in their agreed profit-sharing ratio (or equally if there is no agreed profit-sharing ratio).

- **Salary or Commission to a Partner:** Salary or Commission to a partner is allowed if the Partnership Deed provides for it.

A: *Commission as a percentage of the Net Profit before charging such commission*

$$= \text{Net Profit before Commission} \times \frac{\text{Rate of Commission}}{100}$$

B: *Commission as a percentage of Net Profit after charging such commission*

$$= \text{Net Profit before Commission} \times \frac{\text{Rate of Commission}}{100 + \text{Rate of Commission}}$$

Salary or commission to a partner *being an appropriation of profits* is transferred to the *debit of the Profit and Loss Appropriation Account* and not to the *debit of the Profit and Loss Account*.

- **Interest on Capital:** Interest on capital is calculated on time basis, taking into consideration any additional capital introduced or any existing capital withdrawn.
- **Interet on Current Account:** Interest on Current Account is allowed (in case of Credit Balance) and charged (in case of debit balance) on Opening Balance.
  It is allowed or charged if instructed in the question.
- **Interest on Drawings:** If the Partnership Deed so provides, interest on drawings is charged from the partners. The interest so charged is credited to the Profit and Loss Appropriation Account and debited to the Partners' Capital or Current Accounts.
  If the date of Drawings is not given, the Interest on total Drawings is calculated for 6 months.
  Interest @ 10% without the word 'per annum' means interest is calculated without any reference to time period.
- **Interest on Partner's Loan to the Firm:** If a partner gives a loan to the firm, he is entitled to interest on such loan at an agreed rate of interest. If there is no agreement as to the rate of interest on loan, the partner is entitled to interest on loan @ 6% p.a. Interest on partner's loan is a 'charge' against the profit and is credited to his/her Loan Account.
- **Interest on Loan by the Firm to a Partner:** Firm is entitled to receive interest on loan given to a partner. However, the firm will charge interest on loan advanced to a partner only, if it is provided in the Partnership Deed or is agreed to charge interest along with the rate of interest among the partners. It is a gain to the firm and is credited to Profit and Loss A/c.

Methods of Maintaining Capital Accounts of Partners

The Partners' Capital Accounts may be maintained according to *Fixed Capital Method* or *Fluctuating Capital Method*.

Fixed Capital Method: Under this method, the capital of partners *remains unchanged* except under special circumstances. In case of the fixed capital, *two* accounts are maintained for each partner, *viz.*, (*i*) Fixed Capital Account and (*ii*) Current Account. All adjustments regarding drawings, interest on drawings, salary, interest on capital, commission and share of profit or loss are recorded in *Current Account*. The Fixed Capital Account cannot have a negative balance.

Fluctuating Capital Method: Capital Accounts are called **fluctuating** when the balances of Capital Accounts change with each transaction. All adjustments relating to interest on capital, drawings, salary and profit are recorded in the Capital Accounts. Under this method, only one account is opened for each partner, *i.e.*, Capital Account.

In the absence of any instruction, Partners' Capital Accounts are prepared following Fluctuating Capital Method.

- **Guarantee of Minimum Profit to a Partner:** A partner may be guaranteed a minimum amount of his share in profits. Guarantee may be provided by one or some or all of the partners in an existing profit-sharing ratio or in some other agreed ratio. If in any year, the actual share of profit is less than the guaranteed amount, the deficiency is borne by the guaranteeing partners in their agreed ratio.
- **Past Adjustments:** Sometimes after closing the accounts of a partnership firm for a certain period, certain omissions or errors may be discovered. For example, interest on capital or interest on drawings may have been omitted or interest has been calculated at a different rate than agreed, or profits may have been distributed in a different manner than agreed among the partners. Corrections of these errors are generally done through the Partners' Capital Accounts by means of a single adjusting Journal entry. No attempt is made to reopen the accounts of the previous accounting period(s). Such adjustments are called **past adjustments** as these are related to past periods.

Solved Questions

Illustration 1 (*Provisions of the Indian Partnership Act, 1932*).

X and *Y* are partners in a firm. They do not have Partnership Deed. What shall be the position in the following cases?

(*i*) *X* devotes more time than *Y* in the business. *X* claims that he should get a salary of ₹ 6,000 per month for it.

(*ii*) *Y* has provided a capital of ₹ 50,000 whereas *X* has provided ₹ 5,000 only as capital. *X*, however, has advanced ₹ 10,000 as loan to the firm. What interest, if any, will be given to *X* and *Y*?

(*iii*) *X* wants to introduce his son *Z* into their business. *Y* objects to his proposal.

Solution:

In the absence of Partnership Deed, provisions of the Indian Partnership Act, 1932 shall apply to settle the disputes:

(*i*) Salary is not payable to any partner. Therefore, *X* is not entitled to any salary.

(*ii*) Interest on capital is not payable to any partner. Therefore, *X* and *Y* will not get interest on their capitals. Interest on Loan is allowed @ 6% p.a. Thus, *X* will get interest ₹ 600 (*i.e.*, 6% of ₹ 10,000).

(*iii*) A person cannot be introduced as partner without the consent of all the partners. Therefore, *Z* cannot be admitted into partnership because *Y* objects to it.

Illustration 2.

Ann and Rose are partners and they do not have Partnership Deed. They have different opinion on issues relating to sharing of profits, interest on capital, etc. They approach you for advice to know the correct position. You are to give your opinion, with reasons. The issues are:

(*i*) Ann devotes time to the partnership business and, therefore, claims salary. Rose opposes it.

(*ii*) Rose invested ₹ 2,50,000 less than Ann in the capital of the firm. Ann claims interest on ₹ 2,50,000 which also Rose opposes.

(*iii*) Rose proposes that interest be charged by the firm on the drawings. Ann opposes it.

(*iv*) Ann has advanced a loan of ₹ 2,00,000 to the firm and claims interest @ 8% p.a.

(*v*) Ann claims to share profits in their capital ratio, to which Rose does not agree and proposes that the profits be shared equally.

Solution:

It is important to note that Ann and Rose do not have Partnership Deed. Therefore, provisions of the Indian Partnership Act, 1932 will apply as follows:

(*i*) The Indian Partnership Act, 1932 provides that salary is not to be allowed to a partner, if the Partnership Deed does not exist or allow it. Therefore, the claim of Ann is not acceptable.

(*ii*) Ann cannot claim interest on ₹ 2,50,000 being excess capital contributed. The Indian Partnership Act, 1932 provides that interest is not to be allowed on capital, if the Partnership Deed does not exist or allow it.

(*iii*) The Indian Partnership Act, 1932 provides that interest on drawings is not to be charged if not so provided for in the Partnership Deed. Therefore, the proposal of Rose is not justified.

(*iv*) Ann is justified in claiming interest on the loan advanced by her. Since, Partnership Deed does not exist, interest on loan by a partner is a charge against profit and is allowed @ 6% p.a. as is provided for in the Indian Partnership Act, 1932.

(*v*) Ann is not right in claiming profits to be shared in their capital ratio. It is so because the Indian Partnership Act, 1932 provides that profits shall be shared equally in the absence of agreement on profit-sharing ratio.

Illustration 3 (*Partnership Deed does not Exist*).

A and *B* are partners from 1st April, 2017 without a Partnership Deed and they introduced capital of ₹ 7,00,000 and ₹ 4,00,000 respectively. On 1st October, 2017, *A* advanced loan of ₹ 3,75,000 to the firm without an agreement as to interest. *B* allows the firm to carry on business from premises owned by him for a yearly rent of ₹ 1,20,000. Profit as per the Profit and Loss Account for the year ended 31st March, 2018 was ₹ 7,97,390 before charging rent. The partners do not agree on allowing of interest and the basis of division of profits. You are required to divide the profits giving reasons for your method.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2018

Dr. *Cr.*

Particulars		₹	Particulars	₹
To Profit transferred to Capital A/cs:			By Profit and Loss A/c	6,66,140
A	3,33,070		(After rent and interest on loan)	
B	3,33,070	6,66,140	(₹ 7,97,390 – ₹ 1,20,000 – ₹ 11,250)	
		6,66,140		6,66,140

Reasons:

1. **Rent is a charge on profit** hence, is to be debited to Profit and Loss Account.
2. Since there is no Partnership Deed, *A* will be allowed interest @ 6% for six months, (₹ 3,75,000 × 6/100 × 6/12 = ₹ 11,250), because the loan has been advanced on 1st October, 2017. **Interest on Partner's Loan is a charge against profit** hence, is to be debited to Profit and Loss Account.
3. In the absence of Partnership Deed, **profit-sharing ratio will be equal**.

Illustration 4 (*Interest on Capital when Profit is Inadequate*).

A and *B* contribute ₹ 4,00,000 and ₹ 2,00,000 respectively as capital on which they agree to pay interest @ 6% p.a. They are to share profit in the ratio of 2 : 3. Business profit (before interest) for the year is ₹ 30,000. Show the relevant account to allocate interest on capitals:

(*i*) if Partnership Deed is silent about the treatment of interest on capital, and

(*ii*) if interest is a charge as per Partnership Deed.

Solution:

(*i*) *When Partnership Deed is silent in treating interest as a charge or appropriation:*

Dr. PROFIT AND LOSS APPROPRIATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Interest on Capital A/cs:			By Profit and Loss A/c	30,000
A	20,000		(Profit for the year)	
B	10,000	30,000		
		30,000		30,000

Working Note:

Interest on *A*'s Capital and *B*'s Capital is ₹ 24,000 and ₹ 12,000 respectively. Thus, total interest is ₹ 36,000. Since, the profit before interest is only ₹ 30,000, interest on capital will be shared in the ratio of interest allowable, *i.e.*, ₹ 24,000 : ₹ 12,000 or 2 : 1. Interest on Capital allowed to respective partner will be:

$$A = \frac{₹\,30,000 \times ₹\,24,000}{₹\,36,000} = ₹\ 20,000;\ B = \frac{₹\,30,000 \times ₹\,12,000}{₹\,36,000} = ₹\ 10,000.$$

(*ii*) *When Interest is a charge as per Partnership Deed:*

Dr. PROFIT AND LOSS ACCOUNT *Cr.*

Particulars		₹	Particulars		₹
To Interest on Capital A/cs:			By Profit before Interest		30,000
A	24,000		By Loss transferred to Capital A/cs:		
B	12,000	36,000	*A*	2,400	
			B	3,600	6,000
		36,000			36,000

Note: Profit and Loss Appropriation Account shall not be prepared because interest on capital is a charge against profit. Since, the profit is less than interest on capital, deficit (after interest) shall be treated as loss.

Illustration 5.

A, *B* and *C* are in partnership and during the year ended 31st March, 2018 earned profit of ₹ 83,000. *A* and *B* are entitled to 5% p.a. interest on their capitals of ₹ 60,000 and ₹ 1,00,000 respectively while *C*, who has no capital in the firm, is entitled to a salary of ₹ 12,000 p.a. *C* is also entitled to a commission of 5% on the balance profits, *i.e.*, after charging interest, salary and commission. It is further agreed that out of the remaining profit 20% shall be donated to Prime Minister's National Relief Fund and balance profit will be shared equally by the partners. Prepare Profit and Loss Appropriation Account for the year ended 31st March, 2018.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2018

Dr. *Cr.*

Particulars		₹	Particulars	₹
To *C*'s Salary A/c		12,000	By Profit and Loss A/c (Profit)	83,000
To Interest on Capital A/cs:				
A	3,000			
B	5,000	8,000		
To *C*'s Commission A/c		3,000		
[5/105 (₹ 83,000 – ₹ 12,000 – ₹ 8,000)]				
To Donation A/c [20% of ₹ (83,000 – 23,000)]		12,000		
To Profit transferred to Capital A/cs:				
A	16,000			
B	16,000			
C	16,000	48,000		
		83,000		83,000

Illustration 6 (*Calculation of Opening Capital*).

A and *B* are partners in a business and their capitals at the end of the year were ₹ 7,00,000 and ₹ 6,00,000 respectively. Calculate their opening capitals considering the following information:

(*a*) Drawings of *A* and *B* for the year were ₹ 75,000 and ₹ 50,000 respectively.

(*b*) *B* introduced capital of ₹ 1,00,000 during the year.

(*c*) Interest on drawings debited to the Capital Accounts of *A* and *B* were ₹ 7,500 and ₹ 5,000 respectively.

(*d*) Share of loss debited to each Partner's Capital Account was ₹ 20,000.

Solution:

CALCULATION OF OPENING CAPITAL

Particulars	*A* ₹	*B* ₹
Capitals at the end	7,00,000	6,00,000
Add: Drawings during the year	75,000	50,000
Interest on Drawings	7,500	5,000
Share of Loss for the year	20,000	20,000
	8,02,500	6,75,000
Less: Capital Introduced during the year	...	1,00,000
Opening Capitals or Capitals in the beginning	8,02,500	5,75,000

Alternatively, Capital Account of each partner may be prepared to determine Opening Capital as follows:

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*A* ₹	*B* ₹	Particulars	*A* ₹	*B* ₹
To Drawings A/c	75,000	50,000	By Balance *b/d* **(Balancing Figure)**	**8,02,500**	**5,75,000**
To Interest on Drawings A/c	7,500	5,000	By Cash/Bank A/c (Add. Capital Introduced)	...	1,00,000
To Profit and Loss A/c (Share of Loss)	20,000	20,000			
To Balance *c/d* (Given)	7,00,000	6,00,000			
	8,02,500	6,75,000		8,02,500	6,75,000

Illustration 7.

Akhil and Bhuvi are partners sharing profits and losses in the ratio of 3 : 1. On 1st April, 2018, their capitals were: *A* ₹ 5,00,000 and *B* ₹ 3,00,000. During the year ended 31st March, 2019, they earned net profit of ₹ 5,00,000. The terms of partnership are:

(*i*) Interest on capitals is to be allowed @ 6% p.a.

(*ii*) Akhil will get commission @ 2% on net sales.

(*iii*) Bhuvi will get a salary of ₹ 5,000 per month.

(*iv*) Bhuvi will get commission of 5% on profit after deduction of interest, salary and commission (including his own commission).

Partners' drawings during the year were: Akhil ₹ 80,000 and Bhuvi ₹ 60,000. Net sales for the year were ₹ 30,00,000. After considering the above factors, you are required to prepare Profit and Loss Appropriation Account and Capital Accounts of the Partners.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2019* *Cr.*

Particulars		₹	Particulars	₹
To Interest on Capital A/cs:			By Profit and Loss A/c	5,00,000
Akhil (₹ 5,00,000 × 6/100)	30,000		(Net Profit)	
Bhuvi (₹ 3,00,000 × 6/100)	18,000	48,000		
To Bhuvi's Salary A/c (₹ 5,000 × 12)		60,000		
To Commission A/c:				
Akhil (WN 1)	60,000			
Bhuvi (WN 2)	15,810	75,810		
To Profit transferred to Partners' Capital A/cs:				
Akhil (3/4)	2,37,142			
Bhuvi (1/4)	79,048	3,16,190		
		5,00,000		5,00,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Date	Particulars	Akhil ₹	Bhuvi ₹	Date	Particulars	Akhil ₹	Bhuvi ₹
2019				2018			
March 31	To Drawings A/c	80,000	60,000	April 1	By Balance *b/d*	5,00,000	3,00,000
March 31	To Balance *c/d*	7,47,142	4,12,858	2019			
				March 31	By Interest on Capital A/c	30,000	18,000
				March 31	By Profit and Loss Appropriation A/c (Salary)	...	60,000
				March 31	By Commission A/c	60,000	15,810
				March 31	By Profit and Loss Appropriation A/c (Profit)	2,37,142	79,048
		8,27,142	4,72,858			8,27,142	4,72,858

Working Notes:

1. Akhil's Commission = 2/100 × ₹ 30,00,000 = ₹ 60,000.
2. *Bhuvi's Commission:*

   Net profit after charging interest, salary and Akhil's Commission but before charging Bhuvi's commission = ₹ (5,00,000 − 48,000 − 60,000 − 60,000) = ₹ 3,32,000

   Bhuvi's Commission after charging his own Commission = 5/105 × ₹ 3,32,000 = ₹ 15,810.

Illustration 8.

Rahul, Shyam and Tarun are partners sharing profits and losses in proportion to their capitals in the beginning of the year. They are entitled to draw annually ₹ 3,000; ₹ 2,500 and ₹ 2,000 respectively against their anticipated share of profit. Any drawings in excess of these amounts are to be regarded as advances taken from the firm and are to be subject to interest @ 18% p.a. The capitals in the beginning of the year is to be allowed interest @ 15% p.a.

The capitals of the partners in the beginning of the year were Rahul ₹ 40,000; Shyam ₹ 30,000 and Tarun ₹ 20,000. The credit balances of their Current Accounts were Rahul ₹ 1,152; Shyam ₹ 1,864 and Tarun ₹ 576. Their drawings during the year were Rahul ₹ 7,000; Shyam ₹ 9,500 and Tarun ₹ 3,000. Net profit for the year ended 31st March, 2019 was ₹ 30,420.

Prepare Profit and Loss Appropriation Account, Capital and Current Accounts of the partners for the year ended 31st March, 2019.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2019* *Cr.*

Particulars		₹	Particulars		₹
To Interest on Capital A/cs:			By Profit and Loss A/c (Net Profit)		30,420
Rahul	6,000		By Interest on Drawings A/cs (Note):		
Shyam	4,500		Rahul on ₹ 4,000	360	
Tarun	3,000	13,500	(₹ 7,000 – ₹ 3,000)		
To Profit trfd. to Current A/cs:			Shyam on ₹ 7,000	630	
Rahul (4/9)	8,000		(₹ 9,500 – ₹ 2,500)		
Shyam (3/9)	6,000		Tarun on ₹ 1,000	90	1,080
Tarun (2/9)	4,000	18,000	(₹ 3,000 – ₹ 2,000)		
		31,500			31,500

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Date	Particulars	Rahul ₹	Shyam ₹	Tarun ₹	Date	Particulars	Rahul ₹	Shyam ₹	Tarun ₹
2019					2018				
Mar. 31	To Balance *c/d*	40,000	30,000	20,000	Apr. 1	By Balance *b/d*	40,000	30,000	20,000
		40,000	30,000	20,000			40,000	30,000	20,000

Dr. PARTNERS' CURRENT ACCOUNTS *Cr.*

Date	Particulars	Rahul ₹	Shyam ₹	Tarun ₹	Date	Particulars	Rahul ₹	Shyam ₹	Tarun ₹
2019					2018				
Mar. 31	To Drawings A/c	7,000	9,500	3,000	Apr. 1	By Balance *b/d*	1,152	1,864	576
Mar. 31	To Interest on Drawings A/c	360	630	90	2019 Mar. 31	By Interest on Capital A/c	6,000	4,500	3,000
Mar. 31	To Balance *c/d*	7,792	2,234	4,486	Mar. 31	By Profit and Loss Appropriation A/c	8,000	6,000	4,000
		15,152	12,364	7,576			15,152	12,364	7,576

Note: In the absence of actual dates of drawings, interest thereon has been calculated for the average period, *i.e.*, 6 months.

Illustration 9.

Asif and Ravi are partners in a firm, sharing profits and losses in the ratio of 3 : 2. Their fixed capitals as on 1st April, 2016, were ₹ 6,00,000 and ₹ 4,00,000 respectively.

Their Partnership Deed provides for the following:

(*a*) Partners are to be allowed interest on their capital @ 10% per annum.

(*b*) They are to be charged interest on drawings @ 4% per annum.

(*c*) Asif is entitled to a salary of ₹ 2,000 per month.

(*d*) Ravi is entitled to a commission of 5% of the correct net profit of the firm before charging such commission.

(*e*) Asif is entitled to a rent of ₹ 3,000 per month for the use of his premises by the firm.

The net profit of the firm for the year ended 31st March, 2017, before providing for any of the above clauses was ₹ 4,00,000.

Both partners withdrew ₹ 5,000 in the beginning of every month for the entire year.

You are required to prepare Profit and Loss Appropriation Account for the year ended 31st March, 2017. (*ISC 2018*)

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2017* *Cr.*

Particulars		₹	Particulars		₹
To Interest on Capital A/cs:			By Profit and Loss A/c (Net Profit) (WN 1)		3,64,000
Asif	60,000		By Interest on Drawing A/cs:		
Ravi	40,000	1,00,000	Asif	1,300	
To Asif's Salary A/c		24,000	Ravi	1,300	2,600
To Ravi's Commission A/c (5% of ₹ 3,64,000)		18,200			
To Profit transferred to:					
Asif's Current A/c	1,34,640				
Ravi's Current A/c	89,760	2,24,400			
		3,66,600			3,66,600

Working Notes:

1. Rent of ₹ 36,000 payable to Asif for the use of his premises is a charge against profit. Therefore, it is deducted before transferring the profit to Profit and Loss Appropriation Account. Thus, Amount transferred to Profit and Loss Appropriation Account ₹ 3,64,000 (*i.e.*, ₹ 4,00,000 – ₹ 36,000).

2. *Interest on Drawings:*

$$\text{Asif} = ₹\ 5{,}000 \times 12 \times \frac{6.5}{12} \times \frac{4}{100} = ₹\ 1{,}300;$$

$$\text{Ravi} = ₹\ 5{,}000 \times 12 \times \frac{6.5}{12} \times \frac{4}{100} = ₹\ 1{,}300.$$

Illustration 10.

A, *B* and *C* are partners sharing profits and losses in the ratio of 4 : 3 : 2. Their Capital Account balances as on 31st March, 2016 are as follows:

A—₹ 4,25,000 (Cr.); *B*—₹ 2,75,000 (Cr.); *C*—₹ 3,05,000 (Cr.).

Following further information is provided:

(*i*) ₹ 55,600 is to be transferred to General Reserve.

(*ii*) *A*, *B* and *C* are paid monthly salary in cash amounting to ₹ 6,000; ₹ 4,000 and ₹ 4,500 respectively.

(*iii*) Partners are allowed interest on their closing capital balances at 6% p.a. and are charged interest on drawings @ 8% p.a.

(*iv*) *A* and *B* are entitled to commission at 8% and 10% respectively on the Net profit before making any appropriation.

(*v*) *C* is entitled to commission at 15% of the Net profit before charging Interest on Drawings but after making all other appropriations.

(*vi*) During the year, *A* withdrew ₹ 5,000 in the beginning of every month, *B*—₹ 4,375 at the end of every month and *C*—₹ 3,125 in the middle of every month.

(*vii*) Firm's Accountant is entitled to a salary of ₹ 5,000 per month and a commission of 12% of Net profit after charging such commission.

Net profit of the firm for the year ended 31st March, 2016, before providing for any of the above adjustments was ₹ 6,90,000. You are required to prepare Profit and Loss Appropriation Account for the year ended on 31st March, 2016.

Solution:

PROFIT AND LOSS ACCOUNT
Dr. *for the year ended 31st March, 2016* *Cr.*

Particulars	₹	Particulars	₹
To Accountant's Salary (Note 1) (₹ 5,000 × 12)	60,000	By Net Profit *b/d*	6,90,000
To Accountant's Commission (Note1) 12/112 (₹ 6,90,000 – ₹ 60,000)	67,500		
To Net Profit trfd. to P and L Appropriation A/c	5,62,500		
	6,90,000		6,90,000

PROFIT AND LOSS APPROPRIATION ACCOUNT
Dr. *for the year ended 31st March, 2016* *Cr.*

Particulars		₹	Particulars		₹
To General Reserve A/c		55,600	By Net Profit (trfd. from Profit and Loss A/c)		5,62,500
To Partners' Salary:			By Interest on Drawings:		
A (₹ 6,000 × 12)	72,000		*A* (₹ 60,000 × 8/100 × 6.5/12)	2,600	
B (₹ 4,000 × 12)	48,000		*B* (₹ 52,500 × 8/100 × 5.5/12)	1,925	
C (₹ 4,500 × 12)	54,000	1,74,000	*C* (₹ 37,500 × 8/100 × 6/12)	1,500	6,025
To Interest on Capital A/cs:					
A (₹ 4,25,000 × 6/100)	25,500				
B (₹ 2,75,000 × 6/100)	16,500				
C (₹ 3,05,000 × 6/100)	18,300	60,300			
To Partners' Commission:					
A (₹ 5,62,500 × 8/100)	45,000				
B (₹ 5,62,500 × 10/100)	56,250				
C (Note 2)	25,703	1,26,953			
To Net Profit transferred to Capital A/cs:					
A (₹ 1,51,672 × 4/9)	67,410				
B (₹ 1,51,672 × 3/9)	50,557				
C (₹ 1,51,672 × 2/9)	33,705	1,51,672			
		5,68,525			5,68,525

Notes:

1. Salary and Commission to firm's Accountant are charge against firm's profits, and not an appropriation of profit. Hence, these items have been debited to Profit and Loss Account.
2. *C*'s Commission = 15/100 (₹ 5,62,500 – ₹ 55,600 – ₹ 1,74,000 – ₹ 60,300 – ₹ 1,01,250) = ₹ 25,703.

Illustration 11.

A, *B* and *C* are partners sharing profits and losses in proportion to their capitals in the beginning of the year. They are entitled to draw annually ₹ 30,000; ₹ 25,000 and ₹ 20,000 respectively out of their anticipated share of profit. Any drawings in excess of these amounts are to be regarded as advances taken from the firm and are to be subject to interest @ 18% p.a. The capitals in the beginning of the year is to be allowed interest @ 15% p.a.

Capitals of the partners in the beginning of the year were: *A* ₹ 4,00,000; *B* ₹ 3,00,000 and *C* ₹ 2,00,000. The credit balances of their Current Accounts were: *A* ₹ 11,520; *B* ₹ 18,640 and *C* ₹ 5,760. Their drawings during the year were: *A* ₹ 70,000; *B* ₹ 95,000 and *C* ₹ 30,000. The profit for the year was ₹ 3,04,200 before making any adjustments for interest as above.

Draw up Profit and Loss Appropriation Account, Capital and Current Accounts of the partners for the year ended 31st March, 2016.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2016

Dr. | *Cr.*

Particulars		₹	Particulars		₹
To Interest on Capital:			By Profit and Loss A/c (Net Profit)		3,04,200
A's Current A/c	60,000		By Interest on Drawings (Note):		
B's Current A/c	45,000		*A* on ₹ 40,000	3,600	
C's Current A/c	30,000	1,35,000	*B* on ₹ 70,000	6,300	
To Profit transferred to Current A/cs:			*C* on ₹ 10,000	900	10,800
A (4/9)	80,000				
B (3/9)	60,000				
C (2/9)	40,000	1,80,000			
		3,15,000			3,15,000

PARTNERS' CAPITAL ACCOUNTS

Dr. | *Cr.*

Date	Particulars	*A* ₹	*B* ₹	*C* ₹	Date	Particulars	*A* ₹	*B* ₹	*C* ₹
2016					2015				
Mar. 31	To Balance *c/d*	4,00,000	3,00,000	2,00,000	Apr. 1	By Balance *b/d*	4,00,000	3,00,000	2,00,000
		4,00,000	3,00,000	2,00,000			4,00,000	3,00,000	2,00,000

PARTNERS' CURRENT ACCOUNTS

Dr. | *Cr.*

Date	Particulars	*A* ₹	*B* ₹	*C* ₹	Date	Particulars	*A* ₹	*B* ₹	*C* ₹
2016					2015				
Mar. 31	To Drawings A/c	70,000	95,000	30,000	April 1	By Balance *b/d*	11,520	18,640	5,760
	To Interest on Drawings A/c	3,600	6,300	900	2016 Mar. 31	By Interest on Capital A/c	60,000	45,000	30,000
	To Balance *c/d*	77,920	22,340	44,860		By Profit and Loss App. A/c	80,000	60,000	40,000
		1,51,520	1,23,640	75,760			1,51,520	1,23,640	75,760

Note: In the absence of actual dates of drawings, interest thereon has been calculated for the average period, *i.e.*, 6 months.

Illustration 12.

A, *B* and *C* are partners in a firm. According to the Partnership Deed, the partners are entitled to draw ₹ 700 per month. On the 1st day of every month, *A*, *B* and *C* draw ₹ 700, ₹ 600 and ₹ 500 respectively. Interest on capitals and interest on drawings are fixed @ 8% and 10% respectively. Profit during the year 2017–18 was ₹ 75,500, out of which a sum of ₹ 20,000 is to be transferred to General Reserve. *B* and *C* are entitled to receive salary of ₹ 3,000 and ₹ 4,500 p.a. respectively and *A* is entitled to receive commission @ 10% on the net distributable profit after charging such commission. On 1st April, 2017, the balances of their Capital Accounts were ₹ 50,000; ₹ 40,000 and ₹ 35,000 respectively.

You are required to show Profit and Loss Appropriation Account for the year ended 31st March, 2018 and Capital Accounts of Partners in the books of the firm.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2018

Dr. *Cr.*

Particulars		₹	Particulars		₹
To General Reserve A/c		20,000	By Profit as per Profit and Loss A/c		75,500
To Interest on Capital A/c:			By Interest on Drawings A/c:		
A	4,000		*A* (₹ 8,400 × 10/100)	840	
B	3,200		*B* (₹ 7,200 × 10/100)	720	
C	2,800	10,000	*C* (₹ 6,000 × 10/100)	600	2,160
To Partners' Salaries A/c:					
B	3,000				
C	4,500	7,500			
To *A*'s Capital A/c (Commission)		3,651			
To Profit transferred to Capital A/cs:					
A	12,170				
B	12,170				
C	12,169	36,509			
		77,660			77,660

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*A* ₹	*B* ₹	*C* ₹	Particulars	*A* ₹	*B* ₹	*C* ₹
To Drawings A/c	8,400	7,200	6,000	By Balance *b/d*	50,000	40,000	35,000
To Interest on Drawings A/c	840	720	600	By Interest on Capital A/c	4,000	3,200	2,800
To Balance *c/d*	60,581	50,450	47,869	By Partners' Salaries A/c	...	3,000	4,500
				By Profit and Loss Appropriation A/c (Commission)	3,651	...	...
				By Profit and Loss Appropriation A/c	12,170	12,170	12,169
	69,821	58,370	54,469		69,821	58,370	54,469

Working Notes:

1. Interest on Capitals and Interest on Drawings are fixed @ 8% and 10% (and not 8% p.a. and 10% p.a.). Therefore, the time factor is ignored.
2. Unless otherwise stated in the Partnership Deed, all partners are deemed to be equal partners. Thus, profit of the year has been divided among partners equally.
3. *Commission payable to A is calculated as:*

A's Commission after charging his own Commission

$$= \frac{10}{110} \times (₹\ 75{,}500 + ₹\ 2{,}160 - ₹\ 10{,}000 - ₹\ 7{,}500 - ₹\ 20{,}000) = ₹\ 3{,}651.$$

Master Questions

Illustration 13.

Vivek, Naman and Akash started their partnership firm on 1st April, 2015 sharing profits and losses in the ratio of 4 : 3 : 2. Their capital accounts are as follows since the firm was started:

Vivek—₹ 8,00,000, Naman—₹ 6,00,000, and Akash—₹ 4,00,000.

Balances in their Current Accounts in the beginning of the year were as follows:

Vivek—₹ 1,00,000, Naman—₹ 80,000, and Akash—₹ 60,000 (Debit).

The Partnership Deed provides as under:

(*i*) Vivek will get annual salary of ₹ 60,000; Naman will get monthly salary of ₹ 4,000, while Akash will get commission @ 5% on net profit.

(*ii*) Interest on balances in current accounts will be charged/paid @ 10% p.a.

(*iii*) Interest on Capital will be allowed @ 6% p.a. whereas interest will be charged on drawings @ 10% p.a.

(*iv*) An amount equal to 10% of the net profit will be transferred to General Reserve.

(*v*) Interest on Loan to a partner will be charged at the rate of interest allowed on loan by the partner.

(*vii*) Akash was guaranteed minimum yearly profit of ₹ 2,00,000 by Vivek and Naman. Shortfall in share of profit was to borne by Vivek and Naman equally.

Additional Information:

(*i*) Naman had advanced a loan of ₹ 1,00,000 to the firm on 1st September, 2018.

(*ii*) Advance was given to Akash of ₹ 1,00,000 on 1st October, 2018.

(*iii*) Vivek has allowed the firm to use his property for business for a monthly rent of ₹ 10,000 payable at the end of the year.

(*iv*) Vivek withdrew ₹ 1,00,000 against capital on 1st December, 2018.

(*v*) Akash introduced further capital of ₹ 1,00,000 on 1st October, 2018.

(*vi*) Vivek withdrew regularly ₹ 5,000 per month in the beginning of each month; Naman withdrew regularly ₹ 5,000 per month in the middle of each month and Akash withdrew regularly ₹ 5,000 per month at the end of each month.

(*vii*) Divisible profit of the last year amounting to ₹ 7,20,000 was distributed equally among the partners before allowing interest on capital.

(*viii*) Profit for the year before the above adjustments was ₹ 12,60,000.

Prepare Profit and Loss Appropriation Account for the year ended 31st March, 2019.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2019* *Cr.*

Particulars		₹	Particulars		₹
To Partners' Salaries:			By Profit and Loss A/c (Net Profit) (WN 1)		11,39,500
Vivek	60,000		By Interest on Current A/c:		
Naman	48,000	1,08,000	Akash		7,600
To General Reserve (10% of ₹ 11,39,500)		1,13,950	By Interest on Drawings:		
To Akash's Commission (5% of ₹ 11,39,500)		56,975	Vivek	3,250	
To Interest on Current A/cs:			Naman	3,000	
Vivek	14,800		Akash	2,750	9,000
Naman	4,800	19,600			
To Interest on Capital A/cs:					
Vivek	46,000				
Naman	36,000				
Akash	27,000	1,09,000			
To Profit transferred to Current A/cs:					
Vivek	3,32,700				
Less: Transferred to Akash	16,825	3,15,875			
Naman	2,49,525				
Less: Transferred to Akash	16,825	2,32,700			
Akash	1,66,350				
Add: Received from Vivek	16,825				
Received from Naman	16,825	2,00,000			
		11,56,100			11,56,100

Working Notes:

1. *Calculation of Net Profit transferred to Profit and Loss Appropriation Account:*

PROFIT AND LOSS ACCOUNT

Dr. *for the year ended 31st March, 2019* *Cr.*

Particulars	₹	Particulars	₹
To Rent (12 × ₹ 10,000)	1,20,000	By Profit (Given)	12,60,000
To Interest on Naman's Loan (₹ 1,00,000 × 6/100 × 7/12)	3,500	By Interest on Loan to Akash (₹ 1,00,000 × 6/100 × 6/12)	3,000
To Net Profit transferred to Profit and Loss Appropriation A/c	11,39,500		
	12,63,000		12,63,000

2. *Adjustment Table:*

	Vivek (₹)	Naman (₹)	Akash (₹)
Divisible Profit (₹ 7,20,000) wrongly appropriated equally now taken back	(2,40,000)	(2,40,000)	(2,40,000)
Interest on Capital @ 6% p.a.	48,000	36,000	24,000
Profit to be credited in 4 : 3 : 2	2,72,000	2,04,000	1,36,000
Deficiency in Akash's Share	(32,000)	(32,000)	64,000
	48,000	(32,000)	(16,000)

ADJUSTMENT ENTRY

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Naman's Current A/c	...Dr.		32,000	
	Akash's Current A/c	...Dr.		16,000	
	To Vivek's Current A/c				48,000
	(Being the adjustment entry passed)				

3. *Current A/c Balances and Interest thereon:*

	Vivek (₹)	Naman (₹)	Akash (₹)
Given	1,00,000	80,000	(60,000)
Add/Less: Adjustment	48,000	(32,000)	(16,000)
	1,48,000	48,000	(76,000)
Interest on Current A/cs @ 10% p.a.	14,800	4,800	(7,600)

4. Divisible Profit = ₹ 7,48,575

   Akash's Share of Profit (Actual) = ₹ 1,66,350

   Whereas, his Guaranteed Share of Profit = ₹ 2,00,000

   Deficiency in Akash's Share of Profit = ₹ 33,650, which will be met by Vivek and Naman equally.

Illustration 14.

Karan, Hari and Ashish commenced business on 1st April, 2015 as partners with capitals of ₹ 2,00,000; ₹ 6,00,000 and ₹ 3,00,000. They mutually agreed for:

(*i*) 10% p.a. interest on capitals;

(*ii*) 15% p.a. interest on drawings;

(*iii*) Karan will get 5% commission on sales;

(*iv*) Hari will get ₹ 25,000 per month as salary; and

(*v*) Balance of profit to be distributed in the ratio of 2 : 2 : 1.

Ashish also provided a loan of ₹ 1,00,000 @ 16% p.a. to the firm.

Total sales during the first year (*i.e.*, year ended 31st March, 2016) was ₹ 40,00,000 and the net profit at the end of the year was ₹ 10,86,250 (after providing interest on loan).

During the year, Karan introduced ₹ 6,00,000 to the firm as additional capital on 30th September, 2015 but Hari withdrew ₹ 1,00,000 out of his capital on the same date.

Their drawings were:

Partners	On 30th Jun., 2015 ₹	On 30th Sept., 2015 ₹	On 31st Dec., 2015 ₹
Karan	50,000	90,000	1,00,000
Hari	80,000	80,000	80,000
Ashish	90,000	30,000	60,000

You are required to prepare Profit and Loss Appropriation Account for the year ended 31st March, 2016 and Partners' Capital and Current Accounts.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT
for the year ended 31st March, 2016

Dr. Particulars		₹	Particulars		*Cr.* ₹
To Interest on Capital A/c (WN 1):			By Profit and Loss A/c (Net Profit)		10,86,250
Karan's Current A/c	50,000		By Interest on Drawings A/cs (WN 2):		
Hari's Current A/c	55,000		Karan's Current A/c	16,125	
Ashish's Current A/c	30,000	1,35,000	Hari's Current A/c	18,000	
To Karan's Current A/c (Commission) (5% of ₹ 40,00,000)		2,00,000	Ashish's Current A/c	14,625	48,750
To Hari's Current A/c (Salary) (₹ 25,000 × 12)		3,00,000			
To Profit transferred to Current A/cs:					
Karan (₹ 5,00,000 × 2/5)	2,00,000				
Hari (₹ 5,00,000 × 2/5)	2,00,000				
Ashish (₹ 5,00,000 × 1/5)	1,00,000	5,00,000			
		11,35,000			11,35,000

PARTNERS' CAPITAL ACCOUNTS

Dr. Date	Particulars	Karan ₹	Hari ₹	Ashish ₹	Date	Particulars	Karan ₹	Hari ₹	*Cr.* Ashish ₹
2015					2015				
Sept. 30	To Bank A/c	...	1,00,000	...	Apr. 1	By Bank A/c	2,00,000	6,00,000	3,00,000
2016					Sept. 30	By Bank A/c	6,00,000	...	...
Mar. 31	To Balance *c/d*	8,00,000	5,00,000	3,00,000					
		8,00,000	6,00,000	3,00,000			8,00,000	6,00,000	3,00,000

PARTNERS' CURRENT ACCOUNTS

Dr. Date	Particulars	Karan ₹	Hari ₹	Ashish ₹	Date	Particulars	Karan ₹	Hari ₹	*Cr.* Ashish ₹
2015					2016				
June 30	To Drawings A/c	50,000	80,000	90,000	Mar. 31	By Interest on Capital A/c	50,000	55,000	30,000
Sept. 30	To Drawings A/c	90,000	80,000	30,000					
Dec. 31	To Drawings A/c	1,00,000	80,000	60,000	Mar. 31	By P and L Appropriation A/c (Commision)	2,00,000	...	...
2016									
Mar. 31	To Interest on Drawings A/c	16,125	18,000	14,625	Mar. 31	By Profit and Loss Appropriation A/c (Salaries)	...	3,00,000	...
Mar. 31	To Balance *c/d*	1,93,875	2,97,000	...	Mar. 31	By Profit and Loss Appropriation A/c (Profit)	2,00,000	2,00,000	1,00,000
					Mar. 31	By Balance *c/d*	...	...	64,625
		4,50,000	5,55,000	1,94,625			4,50,000	5,55,000	1,94,625

Working Notes:

1. *Calculation of Interest on Capitals:*

Partner	Interest on Capitals	Total (₹)
Karan	On ₹ 2,00,000 @ 10% for 1 year + On ₹ 6,00,000 @ 10% for 6 months	50,000
Hari	On ₹ 6,00,000 @ 10% for 6 months + On ₹ 5,00,000 @ 10% for 6 months	55,000
Ashish	On ₹ 3,00,000 @ 10% for 1 year	30,000
	Total	**1,35,000**

2. *Calculation of Interest on Drawings:*

Partner	Interest on Drawings	Total (₹)
Karan	On ₹ 50,000 @ 15% for 9 months + On ₹ 90,000 @ 15% for 6 months + On ₹ 1,00,000 @ 15% for 3 months	16,125
Hari	On ₹ 80,000 @ 15% for 9 months + On ₹ 80,000 @ 15% for 6 months + On ₹ 80,000 @ 15% for 3 months	18,000
Ashish	On ₹ 90,000 @ 15% for 9 months + On ₹ 30,000 @ 15% for 6 months + On ₹ 60,000 @ 15% for 3 months	14,625
	Total	**48,750**

Illustration 15.

Sachin and Saurabh are partners in a firm. Their profit-sharing ratio is 3 : 2. On 1st April, 2015, their Capital and Current Account balances were:

Partners	Capital Account ₹	Current Account ₹
Sachin	2,00,000	50,000
Saurabh	1,00,000	20,000

The partners are entitled to interest on capital @ 10% p.a. on monthly basis. They are also allowed to make withdrawals at any time during the year but they have agreed to charge interest on drawings @ 10% p.a. also on monthly basis.

The withdrawals of the partners were as under:

Partners	1st July, 2015 (₹)	1st January, 2016 (₹)
Sachin	10,000	18,000
Saurabh	8,000	4,000

On 1st October, 2015 Sachin took over some old furniture from the firm at a valuation of ₹ 40,000 and Saurabh introduced into the business some furniture valued at ₹ 25,000.

On 1st January, 2016 Sachin introduced some stock into the business at a valuation of ₹ 20,000.

On 1st February, 2016 Saurabh took some stock from the business for his personal use at a valuation of ₹ 5,000.

The net profit for the year ended 31st March, 2016 was ₹ 70,000.

Prepare Profit and Loss Appropriation Account for the year ended 31st March, 2016 and Partners' Capital and Current Accounts.

Solution:

PROFIT AND LOSS APPROPRIATION ACCOUNT

for the year ended 31st March, 2016

Dr. Particulars		₹	Particulars		₹ *Cr.*
To Interest on Capital A/cs (WN 1):			By Profit and Loss A/c (Net Profit)		70,000
Sachin	18,500		By Interest on Drawings A/cs (WN 2):		
Saurabh	11,250	29,750	Sachin	1,200	
To Share of Profit trfd. to Current A/cs:			Saurabh	783	1,983
Sachin	25,340				
Saurabh	16,893	42,233			
		71,983			71,983

PARTNERS' CAPITAL ACCOUNTS

Dr. Date	Particulars	Sachin ₹	Saurabh ₹	Date	Particulars	Sachin ₹	Saurabh ₹ *Cr.*
2015				2015			
Oct. 1	To Furniture A/c	40,000	...	April 1	By Balance *b/d*	2,00,000	1,00,000
2016				Oct. 1	By Furniture A/c	...	25,000
Mar. 31	To Balance *c/d*	1,80,000	1,25,000	2016			
				Jan. 1	By Purchases A/c (Stock)	20,000	...
		2,20,000	1,25,000			2,20,000	1,25,000

PARTNERS' CURRENT ACCOUNTS

Dr. Date	Particulars	Sachin ₹	Saurabh ₹	Date	Particulars	Sachin ₹	Saurabh ₹ *Cr.*
2015				2015			
July 1	To Bank A/c (Drawings)	10,000	8,000	April 1	By Balance *b/d*	50,000	20,000
2016				2016			
Jan. 1	To Bank A/c (Drawings)	18,000	4,000	March 31	By Interest on Capital A/c	18,500	11,250
Feb. 1	To Purchases A/c (Goods Withdrawn)		5,000	March 31	By Profit and Loss Appropriation A/c (Share of Profit)	25,340	16,893
March 31	To Interest on Drawings A/c	1,200	783				
March 31	To Balance *c/d*	64,640	30,360				
		93,840	48,143			93,840	48,143

Working Notes:

1. *Interest on Capital:* ₹

Sachin:

		₹
(*i*)	On ₹ 2,00,000 for 6 months (1st April, 2015 to 30th September, 2015) @ 10% p.a.	10,000
(*ii*)	On ₹ 1,60,000 for 3 months (1st October, 2015 to 31st December, 2015) @ 10% p.a. (₹ 2,00,000 – ₹ 40,000 for furniture taken over)	4,000
(*iii*)	On ₹ 1,80,000 for 3 months (1st January, 2016 to 31st March, 2016) @ 10% p.a. (₹ 1,60,000 + ₹ 20,000 for stock introduced)	4,500
Total		**18,500**

Saurabh

		₹
(*i*)	On ₹ 1,00,000 for 6 months (1st April, 2015 to 30th September, 2015) @ 10% p.a.	5,000
(*ii*)	On ₹ 1,25,000 for 6 months (1st October, 2015 to 31st December, 2015) @ 10% p.a. (₹ 1,00,000 + ₹ 25,000 for furniture introduced)	6,250
Total		**11,250**

2. *Interest on Drawings:*

Sachin:	
(*i*) On ₹ 10,000 @ 10% p.a. for 9 months	750
(*ii*) On ₹ 18,000 @ 10% p.a. for 3 months	450
Total	**1,200**
Saurabh:	
(*i*) On ₹ 8,000 @ 10% p.a. for 9 months	600
(*ii*) On ₹ 4,000 @ 10% p.a. for 3 months	100
(*iii*) On ₹ 5,000 @ 10% p.a. for 2 months	83
Total	**783**

Unsolved Questions

1. *X*, *Y* and *Z* commenced business on 1st April, 2017 as partners with capitals of ₹ 4,00,000; ₹ 12,00,000 and ₹ 6,00,000. They mutually agreed for:

(*i*) 10% p.a. interest on capitals;

(*ii*) 15% p.a. interest on drawings;

(*iii*) *X* will get 5% commission on sales;

(*iv*) *Y* will get ₹ 50,000 per month as salary and

(*v*) Balance of profit to be distributed in the ratio of 2 : 2 : 1.

Z also provided a loan of ₹ 2,00,000 @ 8% p.a. to the firm.

Total sales during the first year (*i.e.*, 2017–18) were ₹ 80,00,000 and the net profit at the end of the year was ₹ 21,72,500 (after providing interest on loan).

During the year, *X* introduced ₹ 12,00,000 to the firm as additional capital on 30th September, 2017 but *Y* withdrew ₹ 2,00,000 out of his capital on the same date.

Their drawings were:

Partners	On 30th June, 2017 (₹)	On 30th Sept., 2017 (₹)	On 31st Dec., 2017 (₹)
X	1,00,000	1,80,000	2,00,000
Y	1,60,000	1,60,000	1,60,000
Z	1,80,000	60,000	1,20,000

You are required to prepare Profit and Loss Appropriation Account for the year ended 31st March, 2018 and Partners' Capital and Current Accounts.

2. *X*, *Y* and *Z* started business on 1st April, 2017 with capitals of ₹ 1,00,000; ₹ 60,000 and ₹ 40,000 respectively. Their Partnership Deed provides that:

(*i*) interest on partners' capitals should be provided @ 5% p.a.

(*ii*) interest on partners' drawings should be charged @ 10% p.a.
(Drawings: *X*—₹ 10,000; *Y*—₹ 6,000 and *Z*—₹ 4,000)

(*iii*) the partners are entitled to a partnership salary of ₹ 5,000 each per annum.

(*iv*) *X* is entitled to a commission @ 10% on the profit before charging the above provisions.

(*v*) *Z* is entitled to a commission @ 10% on the net profit (after charging the above provisions) and after charging his commission.

(*vi*) 25% of the net profit (after charging all the above provisions) should be transferred to the Reserve Fund.

(*vii*) Partners will share profits and losses in the ratio of their capitals.

The profit for the year ended 31st March, 2018 amounted to ₹ 60,000.

You are required to prepare Profit and Loss Appropriation Account and Partners' Capital Accounts.

3. Dhoni, Modi and Soni are in partnership, sharing profits and losses in the ratio of 2 : 2 : 1 respectively. Interest is charged on Partners' Drawings @ 6% p.a. and credited to Partners' Capital Account Balances @ 6% p.a.

Modi is the firm's Marketing Manager and for his specialised services, he is credited with a salary of ₹ 5,000 per quarter.

During the year ended 31st March, 2018, net profit of the firm was ₹ 1,55,000 and the partners' drawings were:

		₹
Dhoni	:	30,000
Modi	:	20,000
Soni	:	20,000

In each case, the above drawings were made in two equal instalments on 30th September, 2017 and 31st March, 2018.

On 30th September, 2017, the firm agreed that Dhoni should withdraw ₹ 25,000 from his capital account and that Soni should subscribe a similar amount to his Capital Account.

The balances of the partners' accounts on 1st April, 2017 were:

		All Credit Balances	
		Capital Accounts	*Current Accounts*
		₹	₹
Dhoni	:	2,00,000	16,000
Modi	:	1,75,000	14,000
Soni	:	1,50,000	12,000

Transfer 5% of the net profit to the Reserve Fund of the firm.

Required:

(*i*) Prepare firm's Profit and Loss Appropriation Account for the year ended 31st March, 2018.

(*ii*) Prepare Partners' Capital and Current Accounts for the year ended 31st March, 2018.

(*ISC 1993, Modified*)

4. *A*, *B* and *C* are partners in a firm. *A* and *B* sharing profits in the ratio of 5 : 3 and *C* receiving a salary of ₹ 150 per month, plus a commission of 5% on the profits after charging such salary and commission or 1/5th of the profits of the firm, whichever is larger. Any excess of the latter over the former is, under the partnership agreement, to be borne personally by *A*.

The profits for the year ended 31st March, 2018 amounted to ₹ 10,710 after charging *C*'s salary.

Prepare Profit and Loss Appropriation Account showing the division of the profits of the year.

GUIDE TO ANSWERS

1. Share of Profit: *X*—₹ 4,00,000; *Y*—₹ 4,00,000; *Z*—₹ 2,00,000; Interest on Drawings: *X*—₹ 32,250; *Y*—₹ 36,000 and *Z*—₹ 29,250; Balance of Partners' Capital Accounts: *X*—₹ 16,00,000; *Y*—₹ 10,00,000 and *Z*—₹ 6,00,000; Balance of Partners' Current Accounts: *X*—₹ 3,87,750; *Y*—₹ 5,94,000; *Z*—₹ 1,29,250 (Dr. Balance).
2. Net Distributable Profit—₹ 20,455; Transferred to Reserve Fund—₹ 6,818; Share of Profit: *X*—₹ 10,228; *Y*—₹ 6,136; *Z*—₹ 4,091; *Z*'s Commission—₹ 2,727; Closing Balances of Capital Accounts: *X*—₹ 1,15,728; *Y*—₹ 67,836; *Z*—₹ 49,618.
3.

Particulars	Dhoni (₹)	Modi (₹)	Soni (₹)
Share of Profit	38,720	38,720	19,360
Interest on Drawings	450	300	300
Interest on Capital	11,250	10,500	9,750
Capital Accounts (Balance)	1,75,000	1,75,000	1,75,000
Current Accounts (Balance)	35,520	62,920	20,810

4. Share of Profit: *A*—₹ 6,183; *B*—₹ 3,825; *C*—₹ 2,502; Deficiency borne by *A*—₹ 192.

CHAPTER 2

Goodwill: Concept and Mode of Valuation

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Goodwill

Goodwill is the value of benefit or advantage that a business has because of the factors that help in increasing its profitability. It may be because of its location, favourable contracts, access to supplies and customer loyalty, etc.
Goodwill is an intangible asset.

2. Purchased Goodwill

Purchased Goodwill means the goodwill for which a consideration has been paid.

3. Self-generated Goodwill

Self-generated Goodwill is the goodwill that has been generated by the business because of which it is able to earn higher profit.

4. Methods of Valuation of Goodwill

(*i*) Simple Average Profit Method

It is calculated by taking the average profit for a specified number of years and multiplying it with the number of years of purchase.

Goodwill = Average Profit × No. of Years' Purchase

(*ii*) Weighted Average Profit Method

It is calculated by multiplying the profit for each year with the weight assigned to it. The amounts so arrived at are totalled and divided by the total of weights. The weighted average profit is multiplied by the number of years of purchase.

Goodwill = Weighted Average Profit × No. of Years' Purchase

(*iii*) Super Profit Method

Super profit is the profit earned by the business that is in excess of the normal profit. Goodwill is determined by multiplying the super profit by the number of years' purchase.

Goodwill = Super Profit × No. of Years' Purchase

Capitalisation Method

(*iv*) Capitalisation of Average Profit

Under the Capitalisation Method, the capitalised value of the business is determined by capitalising the average profit by the normal rate of return. Out of the value so determined, value of net assets is deducted to determine the value of goodwill.

Goodwill = Capitalised Value of Business – Net Assets of Business.

(*v*) Capitalisation of Super Profit

Under this method, super profit is capitalised at the normal rate of return.

$$\textbf{Goodwill} = \textbf{Super Profit} \times \frac{\textbf{100}}{\textbf{Normal Rate of Return}}.$$

SUMMARY OF THE CHAPTER

- **Goodwill:** Goodwill is the benefit and advantage of the good name, reputation and connection of a business. It is the attractive force which brings in customers. It is one factor which distinguishes an old established business from a new business at its first start.

- **Nature and Characteristics of Goodwill:**
  It is a valuable intangible asset (an asset which cannot be seen and touched) like patents, trademarks, copyrights, etc. It is not depreciated like tangible assets but is amortised over its useful life. Accounting Standard–26 (AS–26), Intangible Assets prescribes that goodwill should not be recorded in the books of account unless consideration is paid for it. Therefore, self-generated goodwill is not recorded in the books of account but purchased goodwill is recorded. It can be sold, though a sale will be possible only along with the sale of the business itself.
  The characteristics of goodwill are:
  (*i*) It is an intangible asset, *i.e.*, an asset which cannot be seen or touched.
  (*ii*) It does not have an existence separate from that of an enterprise. Thus, it has realisable value when business is sold.
  (*iii*) It helps in earning higher profits.
  (*iv*) It is an attractive force which brings in customers to old place of business.
  (*v*) It comes into existence due to various factors such as locational advantages, favourable contracts, brands, trademarks, patents, market reputation, etc.
  (*vi*) In the context of partnership, it is the value of share of profit sacrificed by the sacrificing partner.
  (*vii*) Value of goodwill is subjective as it depends on the assessment of the valuer.

- **Factors Affecting the Value of Goodwill:** Value of goodwill depends upon the capacity of the business to earn excess profits. Therefore, all such factors which help to increase the profitability of business, will also affect the value of goodwill. These factors are: 1. Efficient Management, 2. Quality of products, 3. Favourable location, 4. Contracts, 5. Control over raw materials, and 6. Other factors like, after sale service, good customer relations, good labour relations, etc.

  In determining normal business profits, interest earned on non-trade investments, is excluded.

- **Need for Valuation of Goodwill for Partnership Firms:** For partnership firms, the need for valuation of goodwill arises in the following circumstances:
  (*i*) When there is a change in the profit-sharing ratio of existing partners.
  (*ii*) When a new partner is admitted.
  (*iii*) When a partner retires or dies.
  (*iv*) When the firm is sold as a going concern.
  (*v*) When two or more firms are amalgamated.

- **Methods of Valuation of Goodwill:** 1. Average Profit Method: Simple Average Profit Method; and Weighted Average Profit Method, 2. Super Profit Method, and 3. Capitalisation Method: Capitalisation of Average Profit Method; and Capitalisation of Super Profit Method.

Solved Question

Illustration 1.

X and *Y* are partners sharing profits in the ratio of 3 : 2. They agree to admit Z into partnership for 1/5th share. Goodwill of the firm for this purpose is to be valued at three years' purchase of the weighted average profit of the past 4 years.

1. The appropriate weights to be used and profits are:

Year	Weight	Profit (₹)
2014–15	1	15,30,000
2015–16	2	20,30,000
2016–17	3	25,30,000
2017–18	4	30,30,000

2. In 2015–16, a machine having a book value of ₹ 10,000 was sold for ₹ 11,000 but the proceeds were wrongly credited to Profit and Loss Account (No effect has been given to rectify the same). Depreciation is charged on machine @ 10% on Diminishing Balance Method.
3. Interest on non-trade investments is ₹ 10,000 in each year.
4. Closing Inventories were undervalued by ₹ 10,000 in 2015–16, by ₹ 9,100 in 2016–17, by ₹ 8,290 in 2017–18.
5. On 1st October, 2016, a major repair was carried out on plant incurring ₹ 80,000 which amount was charged to revenue. The said sum is agreed to be capitalised for computation of goodwill subject to depreciation @ 10% p.a. on Diminishing Balance Method.
6. It is also agreed that ₹ 20,000 be charged on annual basis as management expenses which have not been charged earlier.

Calculate the value of goodwill.

Solution: CALCULATION OF ADJUSTED PROFITS

Particulars	2014–15	2015–16	2016–17	2017–18
Given Profit	15,30,000	20,30,000	25,30,000	30,30,000
Less: Interest on Non-Trade Investments	10,000	10,000	10,000	10,000
	15,20,000	20,20,000	25,20,000	30,20,000
Less: Sale proceeds of machinery wrongly credited	...	11,000	...	...
	15,20,000	20,09,000	25,20,000	30,20,000
Add: Depreciation on above machinery (Note 1)	...	1,000	900	810
	15,20,000	20,10,000	25,20,900	30,20,810
Add: Under valuation of closing inventories (Note 3)	...	10,000	9,100	8,290
	15,20,000	20,20,000	25,30,000	30,29,100
Less: Under valuation of Opening Inventories (Note 3)	...	...	10,000	9,100
	15,20,000	20,20,000	25,20,000	30,20,000
Add: Repair Expenses debited to Profit and Loss A/c	...	...	80,000	...
	15,20,000	20,20,000	26,00,000	30,20,000
Less: Depreciation (Note 2)	...	...	4,000	7,600
	15,20,000	20,20,000	25,96,000	30,12,400
Less: Management Expenses	20,000	20,000	20,000	20,000
Adjusted Profit	15,00,000	20,00,000	25,76,000	29,92,400

CALCULATION OF WEIGHTED AVERAGE PROFIT

Year	Profits (₹)	Weights	Product (₹)
2014–15	15,00,000	1	15,00,000
2015–16	20,00,000	2	40,00,000
2016–17	25,76,000	3	77,28,000
2017–18	29,92,400	4	1,19,69,600
Total		10	2,51,97,600

$$\text{Weighted Average Profit} = \frac{₹\ 2,51,97,60}{10} = ₹\ 25,19,760$$

$$\text{Goodwill} = \text{Weighted Average Profit} \times \text{No. of Years' Purchase}$$
$$= ₹\ 25,19,760 \times 3 = ₹\ 75,59,280.$$

Notes:

1. Due to wrong entry passed initially, the Machinery Account was overvalued by ₹ 10,000. Depreciation for the said amount of ₹ 10,000 was wrongly charged during the period 2015–2018, which is now added back to Profit and Loss Account.
2. Depreciation for 2016–17 = ₹ 80,000 × 10/100 × 6/12 = ₹ 4,000

   Depreciation for 2017–18 = (₹ 80,000 – ₹ 4,000) × 10/100 = ₹ 7,600.

Illustration 2.

From the following information, calculate the value of goodwill of M/s. Puneet and Gaurav:

(*i*) At three years' purchase of Average Profit.
(*ii*) At three years' purchase of Super Profit.
(*iii*) On the basis of Capitalisation of Super Profit.
(*iv*) On the basis of Capitalisation of Average Profit.

Information:

(*a*) Average capital employed in the business—₹ 25,00,000.

(*b*) Trading profits:

Year	Profit/Loss	₹
2012–13	Profit	7,50,000.
2013–14	Loss	6,25,000.
2014–15	Profit	21,25,000.

(*c*) Rate of interest expected from capital having regard to the risk involved—15%.

(*d*) Remuneration to each partner for his service (to be charged against profit)—₹ 12,500 per month.

(*e*) Assets (excluding goodwill)—₹ 30,00,000; Liabilities—₹ 2,50,000.

Solution:

(*i*) *Goodwill at 3 years' Purchase of Average Profit:*

$$\text{Average Profit} = \frac{₹\ 7,50,000 - ₹\ 6,25,000 + ₹\ 21,25,000}{3} = ₹\ 7,50,000$$

$$\text{Average Profit for Goodwill} = ₹\ 7,50,000 - \text{Remuneration of Partners}$$
$$= ₹\ 7,50,000 - (₹\ 12,500 \times 2 \times 12)$$
$$= ₹\ 7,50,000 - ₹\ 3,00,000 = ₹\ 4,50,000$$

$$\text{Goodwill} = \text{Average Profit} \times \text{No. of Years' Purchase}$$
$$= ₹\ 4,50,000 \times 3 = ₹\ 13,50,000.$$

(*ii*) *Value of Goodwill at 3 years' Purchase of Super Profit:*

Normal Profit = Average Capital Employed × Normal Rate of Return

$$= ₹\ 25,00,000 \times \frac{15}{100} = ₹\ 3,75,000$$

Super Profit = Average Profit – Normal Profit

= ₹ 4,50,000 – ₹ 3,75,000 = ₹ 75,000

Goodwill = Super Profit × No. of years' Purchase

= ₹ 75,000 × 3 = ₹ 2,25,000.

(*iii*) *Goodwill under Capitalisation of Super Profit:*

$$\text{Goodwill} = \text{Super Profit} \times \frac{100}{\text{Normal Rate of Return}}$$

$$= ₹\ 75,000 \times \frac{100}{15} = ₹\ 5,00,000.$$

(*iv*) *Goodwill under Capitalisation of Average Profit:*

Step 1: Total Capitalised Value of the Firm $= \dfrac{\text{Average Profit}}{\text{Normal Rate of Return}} \times 100$

$$= \frac{₹\ 4,50,000}{15} \times 100 = ₹\ 30,00,000$$

Step 2: Net Assets = Total Assets (excluding Goodwill) – Outsiders' Liabilities

= ₹ 30,00,000 – ₹ 2,50,000 = ₹ 27,50,000

Step 3: Goodwill = Total Capitalised Value of the Firm – Net Assets

= ₹ 30,00,000 – ₹ 27,50,000 = ₹ 2,50,000.

Master Question

Illustration 3.

Calculate Goodwill of the firm on the basis of:

(*a*) Three year's purchase of the Weighted Average Profit of the last four years.

(*b*) Three year's purchase of Average Profit.

(*c*) Three years' purchase of Super Profit.

(*d*) Capitalisation of Super Profit.

(*e*) Capitalisation of Average Profit.

The weights assigned and profit of each year are:

Year	31st March, 2016	31st March, 2017	31st Mach, 2018	31st March, 2019
Profit (₹)	2,02,000	2,48,000	2,00,000	2,80,000
Weight	1	2	3	4

On scrutiny of the accounts, following matters are revealed:

(*i*) On 1st December, 2017 major repair was carried out in respect of the Plant incurring ₹ 60,000 which enhanced the capacity of the machine and it was charged to revenue. Depreciation on Machinery is charged @ 10% p.a. on reducing balance method.

(*ii*) Closing stock as at 31st March, 2017 was overvalued by ₹ 24,000.

(*iii*) To cover management cost, an annual charge of ₹ 48,000 should be made for the purpose of goodwill valuation.

(*iv*) On 1st October, 2016, a machine having book value of ₹ 20,000 was sold for 22,000 but the proceeds were wrongly credited to Profit and Loss Account. No effect has been given to rectify the same. Depreciation is charged on machine @ 10% p.a. on reducing balance method.

(*v*) Following is the Balance Sheet as on 31st March, 2019:

Liabilities	₹	Assets	₹
Creditors	50,000	Cash	20,000
Capital	3,00,000	Debtors	80,000
		Plant and Machinery	1,60,000
		Stock	40,000
		Bills Receivable	50,000
	3,50,000		3,50,000

(*vi*) Normal Rate of Return in similar business is 10%.

Solution: CALCULATION OF ADJUSTED PROFIT

Particulars	31st March, 2016 (₹)	31st March, 2017 (₹)	31st March, 2018 (₹)	31st March, 2019 (₹)
Given Profits	2,02,000	2,48,000	2,00,000	2,80,000
Less: Annual Management Cost	(48,000)	(48,000)	(48,000)	(48,000)
Add: Capital Expenditure on Plant	...	...	60,000	...
	1,54,000	2,00,000	2,12,000	2,32,000
Less: Unprovided Depreciation on Plant	...	...	(2,000)	(5,800)
	1,54,000	2,00,000	2,10,000	2,26,200
Less: Overvaluation of Closing Stock	...	(24,000)	...	...
Less: Overvaluation of Opening Stock	...	...	24,000	...
	1,54,000	1,76,000	2,34,000	2,26,200
Less: Proceeds from Sale of Plant wrongly credited	...	(22,000)	...	...
	1,54,000	1,54,000	2,34,000	2,26,200
Add: Depreciation Wrongly Credited to Profit and Loss	...	1,000	1,900	1,710
Adjusted Profits	1,54,000	1,55,000	2,35,900	2,27,910

CALCULATION OF WEIGHTED AVERAGE PROFIT

Year Ended	Profits (₹)	Weights	Product (₹)
31st March, 2016	1,54,000	1	1,54,000
31st March, 2017	1,55,000	2	3,10,000
31st March, 2018	2,35,900	3	7,07,700
31st March, 2019	2,27,910	4	9,11,640
Total	7,72,810	10	20,83,340

Weighted Average profit = $\dfrac{₹\,20,83,340}{10}$ = ₹ 2,08,334.

(*a*) Goodwill = Weighted Average Profit × Number of Years' Purchase

= ₹ 2,08,334 × 3 = ₹ 6,25,002.

Working Notes:

1. ₹ 48,000 deducted as annual charge to cover management cost Or we can deduct one year's cost from Average Profit.
2. ₹ 22,000 was wrongly credited to Profit and Loss Account on proceed from sale of machinery. ₹ 2,000 added back on account of depreciation in the year 2015–16, ₹ 1,800 is added back in the year 2016–17 and ₹ 1,620 is added back in the year 2017–18.
3. Closing stock is overvalued by ₹ 24,000 in Financial year 2015–16 which is deducted and added in financial year 2016–17 because opening stock is overvalued because of which profit is reduced.
4. A major repair of plant costing ₹ 60,000 was wrongly charged to revenue. Depreciation is charged @ 10% p.a. on reducing balance method.

(*b*) Average Profit = $\dfrac{₹\,7,72,810}{4}$ = ₹ 1,93,203.

Goodwill = Average Profit × Number of Years' Purchase

= ₹ 1,93,203 × 3 = ₹ 5,79,609.

(*c*) Super Profit = Average Profit – Normal Profit

= ₹ 1,93,203 – $\left(3,00,000 \times \dfrac{10}{100}\right)$ = ₹ 1,63,203.

Goodwill = Super Profit × Number of Years' Purchase

= ₹ 1,63,203 × 3 = ₹ 4,89,609.

(*d*) Goodwill = $\dfrac{\text{Super Profit}}{\text{Normal Rate of Return}} \times 100$

= $₹\,1,63,203 \times \dfrac{100}{10}$ = ₹ 16,32,030.

(*e*) Capitlised Value of the Firm = $\dfrac{\text{Average Profit}}{\text{Normal Rate of Return}} \times 100$

= $\dfrac{₹\,1,93,203 \times 100}{10}$ = ₹ 19,32,030

Net Assets = ₹ 3,00,000 (Assets – Liabilities)

Goodwill = Capitalised Value of Firm – Net Assets

= ₹ 19,32,030 – 3,00,000 = ₹ 16,32,030.

CHAPTER 3

Admission of a Partner

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Admission of Partner or Partners

Admission of a Partner or partners means new partner or partners being admitted into partnership.

2. New Profit-sharing Ratio

New Profit-sharing Ratio is the ratio in which all the partners or partners including the new or incoming partner or partners share future profits and losses of the firm.

3. Sacrificing Ratio

Sacrificing Ratio is the ratio in which the old or existing partners forego, *i.e.*, sacrifice their share in favour of the new partner or partners.

4. Goodwill

Goodwill is an intangible asset resulting from the efforts made in the past by the existing partners of the firm which results in profits in the future years.

5. Revaluation of Assets

Revaluation of Assets means change in the value of assets, *i.e.*, present value being different from the book value of the assets.

6. Reassessment of Liabilities

Reassessment of Liabilities means reassessing the liabilities and determining the change, *i.e.*, whether the liability is more or less than that shown in the books of account.

7. Revaluation Account

It is a nominal account, prepared to ascertain gain (profit)/loss on account of revaluation of assets and reassessment of liabilities. It is credited with the increase in value of assets and decrease in the value of liabilities. It is debited with the increase the value of liabilities and decrease in the value of assets. It is closed by transferring the gain (profit) or loss to the Capital Accounts or Current Accounts of the old or existing partners in their old profit-sharing ratio.

8. Reserve

Reserve means accumulated or undistributed profits. It is created out of profits.

The reserve created is sometimes invested outside the business in instruments such as securities, which then becomes a *Reserve Fund*.

9. Workmen Compensation Reserve

It is a reserve created out of profits for payment of compensation to workers.

10. Investments Fluctuation Reserve

It is a reserve created out of profits to meet fall in the market value of investment.

SUMMARY OF THE CHAPTER

- When the existing partners of a firm allow a person to become a partner in the firm, it is called **admission of a partner**.
- The matters that require *adjustment* at the time of admission of a new partner are:
  (*i*) Adjustment for change in Profit-Sharing Ratio. Calculation of New Profit-sharing Ratio and Sacrificing Ratio.
  (*ii*) Adjustment for goodwill.
  (*iii*) Adjustment of Profit/Loss arising from the Revaluation of Assets and Reassessment of Liabilities.
  (*iv*) Adjustment of Accumulated Profits, Reserves and Losses.
  (*v*) Adjustment of Capital.
- Change in Profit-sharing Ratio takes place at the time of admission of a partner in the firm.
- The ratio in which all partners including the incoming partner share future profits and losses is known as **New Profit-Sharing Ratio**.

  Unless agreed otherwise, **New Profit-sharing Ratio** *of existing, i.e., old partners among them will be same as their old profit-sharing ratio.*
- Ratio in which the old (existing) partners have agreed to sacrifice their share in profit in favour of an incoming partner is called **Sacrificing Ratio**.

  Sacrificing Share = Old Share – New Share.

  Unless agreed otherwise, **Sacrificing Ratio** *of old partners will be the same as their old profit-sharing ratio.*
- The partners whose share in profit increase due to change in profit-sharing ratio are called *Gaining Partners* and the partners whose share in profit decrease are called *Sacrificing Partners*.
- **Goodwill** is the reputation of the organisation which attracts customers and increases the profit earning capacity of the business.

ACCOUNTING TREATMENT OF GOODWILL ON ADMISSION OF A PARTNER

1. *Goodwill (Premium) paid Privately*	No Entry	
2. *Goodwill brought in Cash*	Cash/Bank A/c To Premium for Goodwill A/c	...Dr.
Distribution of Goodwill	Premium for Goodwill A/c To Sacrificing Partners' Capital A/cs or To Sacrificing Partners' Current A/cs (When capitals are fixed)	...Dr. [In sacrificing ratio]
3. *Goodwill withdrawn by Sacrificing (Old) Partners*	Sacrificing Partners' Capital A/cs To Cash/Bank A/c	...Dr.
4. *Goodwill not brought in Cash*	New Partner's Current A/c To Sacrificing Partners' Capital A/cs	...Dr. [In sacrificing ratio]
5. *Goodwill brought in Kind*	Assets A/c To Premium for Goodwill A/c	...Dr.

Note: *Write off the goodwill appearing in the Old Balance Sheet by debiting the Old Partners' Capital Accounts (in case of fluctuating capitals) or Current Accounts (in case of fixed capitals) in their old profit-sharing ratio and crediting the Goodwill Account.*

- **Unless otherwise stated, the Partners' Capitals are assumed to be fluctuating. Current Accounts are to be used in case of Fixed Capitals**.
- **When the incoming partner cannot bring premium for goodwill in cash**, adjustments are made through the **Current Account** of Incoming Partner.

- **Revaluation Account or Profit and Loss Adjustment Account** is prepared to revalue the assets and reassess the liabilities of the firm at the time of reconstitution of the firm.

Dr. REVALUATION ACCOUNT *Cr.*

(i) Decrease in the value of assets.	Increase in the value of assets.
(ii) Increase in amount of liabilities.	Decrease in amount of liabilities.
(iii) Unrecorded liabilities.	Unrecorded assets.
(iv) Gain (Profit)—difference.	Loss—difference.

- **Need to Revalue Assets and Reassess Liabilities:** Assets are revalued and liabilities are reassessed at the time of admission of a partner because new partner should neither benefit nor suffer because of changes in the value of assets and liabilities as on the date of admission.
- **Any Past Profits** or **General Reserve** are also credited to Old Partners' Capital Accounts in their profit-sharing ratio. If there are any past losses, they will be debited to Old Partners' Capital Accounts.
- **Workmen Compensation Reserve** is a reserve created out of profit to meet the workmen compensaton claim, if any arise in future. *Excess of Workmen Compensation Reserve over the Workmen Compensation Claim should be credited to old partners' Capital Accounts in their old ratio.*
- **Investments Fluctuation Reserve** is created out of profit to guard against the fall in the price of the investment. *Excess of Investment Fluctuation Reserve over difference between book value and market value should be credited to old partners in their old profit sharing ratio.*
- Accounting Treatment of Accumulated Profits, Reserves and Losses through Single Journal Entry: *The net effect of accumulated profits, reserves and losses is adjusted through the following entry:*

  (*i*) **In Case of Net Profit:** Gaining Partners' Capital/Current A/cs ...Dr.
  To Sacrificing Partners' Capital/Current A/cs

  (*ii*) **In Case of Net Loss:** Sacrificing Partners' Capital/Current A/cs ...Dr.
  To Gaining Partners' Capital/Current A/cs
- **Employees' Provident Fund** is a statutory liability. Hence, is **not distributed** among the partners.
- **Adjustment of Capital:**

  (*i*) *Adjustment of Old Partners' Capitals on the basis of New Partner's Capital:*
  Step 1: Calculate the total capital of the new firm.
  Step 2: Determine the new capital of each partner.
  Step 3: Ascertain the present capitals of old partners (Adjusted).
  Step 4: Find out the surplus/deficit capitals by comparing Step 2 and Step 3.

  (*ii*) *Calculation of the New Partner's Capital on the basis of Old Partners' Capitals:*
  Step 1: Determine the total adjusted capital of the old partners.
  Step 2: Determine the total capital of the new firm.
  Step 3: Determine the total capital of the incoming partner as follows:
  Total capital of the new firm (Step 2) × Share of incoming partner.

  In the absence of any contract, **Shortage** or **Surplus of Capital** *should be adjusted in* **Cash** *and not by transfer to Current Account.*

Solved Questions

Illustration 1.

A and *B* are partners in a firm sharing Profits and Losses in the ratio of 17 : 16. They admit *C* as a partner on 1st April, 2016 on the basis of his buying 5/17th of *A*'s share and 4/16th of *B*'s share. On 1st April, 2018 they permit *C* to purchase a further 1/12th of their remaining shares. Goodwill is agreed to be valued at 2 years' purchase of the average profits of 3 years immediately before any change. Profits for the 5 years ended 31st March, 2018 are:

Years Ended	31st March, 2014	31st March, 2015	31st March, 2016	31st March, 2017	31st March, 2018
Profits (₹)	15,390	16,130	20,415	23,535	28,780

You are required to determine the amount to be paid by *C* to each partner on both the occasions and their ultimate Profit-sharing Ratio.

Solution:

On 1st Occasion (1st April, 2016):

C buys 5/17th share of *A*, *i.e.*, 17/33 × 5/17 = 5/33 and 4/16th share of *B*, *i.e.*, 16/33 × 4/16 = 4/33.

$$\text{Goodwill} = \frac{₹\,15{,}390 + ₹\,16{,}130 + ₹\,20{,}415}{3} \times 2 = ₹\,34{,}623$$

C will pay ₹ 5,246 to *A* (*i.e.*, ₹ 34,623 × 5/33 for acquiring 5/33rd share) and ₹ 4,197 to *B* (*i.e.*, ₹ 34,623 × 4/33 for acquiring 4/33rd share).

New Profit-sharing Ratio: A(17/33 – 5/33 = 12/33); *B*(16/33 – 4/33 = 12/33); *C*(5/33 + 4/33 = 9/33) or 12/33: 12/33: 9/33 or 4 : 4 : 3.

On 2nd Occasion (1st April, 2018):

C purchases 1/12th of remaining shares of *A* and *B* which is 12/33 (each). Therefore, *C* purchases 12/33 × 1/12 = 1/33rd share (each). New Profit-sharing Ratio will be *A*(12/33 – 1/33 = 11/33); *B*(12/33 – 1/33 = 11/33); C(9/33 + 1/33 + 1/33 = 11/33) or 11/33 : 11/33 : 11/33 or 1 : 1 : 1.

Ultimate Profit-Sharing Ratio will be equal.

$$\text{Goodwill} = \frac{₹\,20{,}415 + ₹\,23{,}535 + ₹\,28{,}780}{3} \times 2 = ₹\,48{,}487.$$

On 2nd occasion, *C* will pay ₹ 1,469 each (*i.e.*, ₹ 48,487 × 1/33) to *A* and *B* (for acquiring 1/33rd share from each of them).

Illustration 2 (*Calculation of Investment to be made to become a Partner*).

A commenced his business with a capital of ₹ 5,00,000 on 1st April, 2013. During 5 years ended 31st March, 2018, the results of his business were:

Year Ended		₹
31st March, 2014	Loss	10,000
31st March, 2015	Profit	26,000
31st March, 2016	Profit	34,000
31st March, 2017	Profit	40,000
31st March, 2018	Profit	50,000

During this period, he withdrew ₹ 80,000 for his personal use. On 1st April, 2018, he admitted *B* into partnership on the following terms:

(*i*) Goodwill is to be valued at 3 times the average profits of the last 5 years.

(*ii*) *B* will have 1/2 share in future profits.

(*iii*) He will bring his share of goodwill in cash.

(*iv*) He will bring capital in cash equal to that of *A* after his admission.

Calculate amount to be brought in by *B* and pass entries to record the transactions pertaining to admission.

Solution:

(*i*) *Calculation of Share of Goodwill to be brought in by B:*

		₹
(*a*)	Total profits for 5 years (– ₹ 10,000 + ₹ 26,000 + ₹ 34,000 + ₹ 40,000 + ₹ 50,000)	1,40,000
(*b*)	Average profits (₹ 1,40,000/5)	28,000
(*c*)	Amount of Goodwill (₹ 28,000 × 3)	84,000
(*d*)	Share of Goodwill to be brought in by *B* (₹ 84,000/2)	**42,000**

(*ii*) *Calculation of A's Capital as on 31st March, 2018:*

(*a*)	Capital as on 1st April, 2013	5,00,000
(*b*)	*Add:* Net profit for 5 years	1,40,000
		6,40,000
(*c*)	*Less*: Drawings	80,000
		5,60,000

(*iii*) *Calculation of amount to be invested by B:*

A's Capital after *B*'s admission = ₹ 5,60,000 + Amount of goodwill to be brought in

= ₹ 5,60,000 + ₹ 42,000 = ₹ 6,02,000

Therefore, *B* will have to bring ₹ 6,02,000 as Capital and ₹ 42,000 as share of Goodwill.

Total amount to be brought in by *B* = ₹ 6,02,000 + ₹ 42,000 = ₹ **6,44,000**.

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2018				
April 1	Cash A/c ...Dr.		6,44,000	
	To *B*'s Capital A/c			6,02,000
	To Premium for Goodwill A/c			42,000
	(Being the amount brought in by *B*)			
April 1	Premium for Goodwill A/c ...Dr.		42,000	
	To *A*'s Capital A/c			42,000
	(Being the amount of goodwill credited to *A*'s Capital Account)			

Illustration 3.

A, *B* and *C* are partners sharing profits and losses in the ratio of 3 : 2 : 1 respectively. *D* is admitted as a new partner on 31st March, 2018 for an equal share and is to pay ₹ 50,000 as Capital. Following is the Balance Sheet on the date of admission:

BALANCE SHEET

Liabilities	₹	Assets	₹
Capital A/cs:		Land and Building	50,000
A	60,000	Plant and Machinery	40,000
B	60,000	Furniture	30,000
C	40,000	Stock	20,000
Creditors	30,000	Debtors	30,000
Bills Payable	10,000	Bills Receivable	20,000
		Bank	10,000
	2,00,000		2,00,000

Following are the required adjustments on *D*'s admission:

(*i*) Out of the Creditors, a sum of ₹ 10,000 is due to *D* which will be transferred to his capital.

(*ii*) Advertisement Expenses of ₹ 1,200 is to be carried forward to next accounting period.

(*iii*) Expenses debited in the Profit and Loss Account includes a sum of ₹ 2,000 paid for *B*'s personal expenses.

(*iv*) A Bill of Exchange of ₹ 4,000, which was previously discounted with the banker, was dishonoured on 31st March, 2018 but no entry has been passed for that.

(*v*) Provision for Doubtful Debts @ 5% is to be created against Debtors.

(*vi*) Expenses on revaluation amounting to ₹ 2,100 is paid by *A*.

Prepare necessary Ledger Accounts and Balance Sheet after *D*'s admission.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Provision for Doubtful Debts A/c (5/100 × ₹ 34,000)	1,700	By Prepaid Advertisement Expenses A/c		1,200
To *A*'s Capital A/c (Revaluation Expenses)	2,100	By *B*'s Capital A/c (*B*'s Drawings)		2,000
		By Loss on Revaluation transferred to Capital A/cs:		
		A (₹ 600 × 3/6)	300	
		B (₹ 600 × 2/6)	200	
		C (₹ 600 × 1/6)	100	600
	3,800			3,800

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*A* ₹	*B* ₹	*C* ₹	Particulars	*A* ₹	*B* ₹	*C* ₹
To Revaluation A/c (Loss)	300	200	100	By Balance *b/d*	60,000	60,000	40,000
To Revaluation A/c (Drawings)	...	2,000	...	By Revaluation A/c (Revaluation Expenses)	2,100	...	...
To Balance *c/d*	61,800	57,800	39,900				
	62,100	60,000	40,000		62,100	60,000	40,000

Dr. *D*'S CAPITAL ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance *c/d*	50,000	By Bank A/c	40,000
		By Creditors A/c	10,000
	50,000		50,000

Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance *b/d*	10,000	By Debtors A/c (B/R Dishonoured)	4,000
To *D*'s Capital A/c	40,000	By Balance *c/d*	46,000
	50,000		50,000

BALANCE SHEET AFTER *D*'S ADMISSION
as at 31st March, 2018

Liabilities		₹	Assets		₹
Capital A/cs:			Land and Building		50,000
A	61,800		Plant and Machinery		40,000
B	57,800		Furniture		30,000
C	39,900		Stock		20,000
D	50,000	2,09,500	Debtors	30,000	
Creditors (₹ 30,000 – ₹ 10,000)		20,000	*Add:* B/R Dishonoured	4,000	
Bills Payable		10,000		34,000	
			Less: Provision for Doubtful Debts	1,700	32,300
			Bills Receivable		20,000
			Bank		46,000
			Prepaid Advertisement Expenses		1,200
		2,39,500			2,39,500

Illustration 4.

A and *B* are partners in a firm. The net profit of the firm is divided as follows: 1/2 to *A*, 1/3 to *B* and 1/6 carried to Reserve. They admit *C* as a partner for 1/5th share in the firm on 1st April, 2018 on which date, the Balance Sheet of the firm was as follows:

Liabilities		₹	Assets	₹
Capital A/cs:			Building	5,00,000
A	5,00,000		Plant and Machinery	3,00,000
B	4,00,000	9,00,000	Stock	1,80,000
Reserve		1,00,000	Debtors	2,20,000
Creditors		2,00,000	Bank	50,000
Outstanding Expenses		50,000		
		12,50,000		12,50,000

Following are the required adjustments on *C*'s admission:

(*i*) *C* brings in ₹ 2,00,000 as his Capital and ₹ 50,000 as his share of Goodwill.

(*ii*) Stock is undervalued by 10%.

(*iii*) Creditors include a liability of ₹ 40,000, which has been decided by the court at ₹ 32,000.

(*iv*) In regard to the Debtors, the following debts proved bad or doubtful:

₹ 20,000 due from *X*—bad to the full extent.

₹ 40,000 due from *Y*—insolvent, estate was expected to pay only 50%.

You are required to prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the new firm.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Bad Debts A/c (*X*)	20,000	By Stock A/c		20,000
To Provision for Doubtful Debts A/c (*Y*)	20,000	(₹ 2,00,000 (WN 1) – ₹ 1,80,000)		
(₹ 40,000 × 50/100)		By Creditors A/c		8,000
		(₹ 40,000 – ₹ 32,000)		
		By Loss on Revaluation transferred to:		
		A's Capital A/c	7,200	
		B's Capital A/c	4,800	12,000
	40,000			40,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*A* ₹	*B* ₹	*C* ₹	Particulars	*A* ₹	*B* ₹	*C* ₹
To Revaluation A/c (Loss)	7,200	4,800	...	By Balance *b/d*	5,00,000	4,00,000	...
To Balance *c/d*	5,82,800	4,55,200	2,00,000	By Reserve A/c	60,000	40,000	...
				By Bank A/c	...	...	2,00,000
				By Premium for Goodwill A/c	30,000	20,000	...
	5,90,000	4,60,000	2,00,000		5,90,000	4,60,000	2,00,000

BALANCE SHEET *as at 1st April, 2018*

Liabilities		₹	Assets		₹
Capital A/cs:			Building		5,00,000
A	5,82,800		Plant and Machinery		3,00,000
B	4,55,200		Stock		2,00,000
C	2,00,000	12,38,000	Debtors	2,20,000	
Creditors (₹ 2,00,000 – ₹ 8,000)		1,92,000	*Less:* Bad Debts (*X*)	20,000	
Outstanding Expenses		50,000		2,00,000	
			Less: Provision for Doubtful Debts (*Y*)	20,000	1,80,000
			Bank (₹ 50,000 + ₹ 50,000 + ₹ 2,00,000)		3,00,000
		14,80,000			14,80,000

Working Notes:

1. Original value of stock = ₹ 1,80,000 × 100/90 = ₹ 2,00,000.
2. Profit-sharing ratio between *A* and *B* = 1/2 : 1/3 = 3 : 2.

Illustration 5.

X and *Y* were trading in partnership sharing profits and losses in the ratio of 7 : 5. On 1st April, 2017, they admitted *Z* into partnership on the following terms:

Z was to have 1/6th share, 1/8th from *X* and 1/24th from *Y* paying ₹ 2,00,000 for that share towards premium for goodwill. *Z* also brought ₹ 2,50,000 as his Capital into the firm. It was further agreed that Machinery should be reduced by 10% and that Investments should be reduced to their market value of ₹ 80,000.

The Balance Sheet of the old firm as at 31st March, 2017 was as follows:

Liabilities		₹	Assets	₹
Creditors		1,60,000	Machinery	2,00,000
Capital A/cs:			Furniture	40,000
X	2,50,000		Investments (At Cost)	1,20,000
Y	2,50,000	5,00,000	Stock	1,00,000
			Debtors	60,000
			Cash at Bank	1,40,000
		6,60,000		6,60,000

Interest on Drawings is to be ignored but Interest on Capital is to be allowed at 5% p.a. The profits of the new firm for the year ended 31st March, 2018 amounted to ₹ 5,24,500 before allowing interest on capitals. Drawings of the partners during the year were: *X*—₹ 1,63,250; *Y*—₹ 1,38,750 and *Z*—₹ 32,500.

You are required to show Partners' Capital Accounts and prepare Balance Sheet as at 31st March, 2016.

Solution:

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Date	Particulars	*X* ₹	*Y* ₹	*Z* ₹	Date	Particulars	*X* ₹	*Y* ₹	*Z* ₹
2017					2017				
Apr. 1	To Revaluation A/c —Loss (WN 2)	35,000	25,000	...	Apr. 1	By Balance *b/d*	2,50,000	2,50,000	...
Apr. 1	To Balance *c/d* (WN 3)	3,65,000	2,75,000	2,50,000	Apr. 1	By Premium for Goodwill A/c (WN 1)	1,50,000	50,000	...
					Apr. 1	By Bank A/c	...	...	2,50,000
		4,00,000	3,00,000	2,50,000			4,00,000	3,00,000	2,50,000
2018					2017				
Mar. 31	To Drawings A/c	1,63,250	1,38,750	32,500	Apr. 1	By Balance *b/d*	3,65,000	2,75,000	2,50,000
Mar. 31	To Balance *c/d*	4,40,000	3,30,000	3,10,000	2018 Mar. 31	By Interest on Capital A/cs	18,250	13,750	12,500
					Mar. 31	By P and L App. A/c (Profit)	2,20,000	1,80,000	80,000
		6,03,250	4,68,750	3,42,500			6,03,250	4,68,750	3,42,500

BALANCE SHEET
as at 31st March, 2018

Liabilities		₹	Assets	₹
Capital A/cs: *X*	4,40,000		Machinery (₹ 2,00,000 – ₹ 20,000)	1,80,000
Y	3,30,000		Furniture	40,000
Z	3,10,000	10,80,000	Investments (₹ 1,20,000 – ₹ 40,000)	80,000
Creditors		1,60,000	Stock	1,00,000
			Debtors	60,000
			Cash at Bank (WN 5)	7,80,000
		12,40,000		12,40,000

Working Notes:

1. Goodwill should be distributed as per sacrificing ratio, *i.e.*, 1/8 : 1/24 or 3 : 1.

   X's share = ₹ 2,00,000 × 3/4 = ₹ **1,50,000**; *Y*'s share = ₹ 2,00,000 × 1/4 = ₹ **50,000**.

2. *Dr.* REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Machinery A/c	20,000	By Loss transferred to:		
To Investments A/c	40,000	*X*'s Capital A/c (7/12)	35,000	
		Y's Capital A/c (5/12)	25,000	**60,000**
	60,000			60,000

3. Since there is interest on capital, it is better to carry forward this balance of Capital Account and thereafter interest on capital should be allowed.

4. **New Profit-sharing Ratio**

   X's New Share = 7/12 – 1/8 = 11/24, *Y*'s New Share = 5/12 – 1/24 = 9/24.

   Hence New Profit Sharing Ratio of *X*, *Y* and *Z* = 11/24 : 9/24 : 1/6 = **11 : 9 : 4**.

PROFIT AND LOSS APPROPRIATION ACCOUNT
5. *Dr.* *for the year ended 31st March, 2018* *Cr.*

Particulars		₹	Particulars	₹
To Interest on Capital A/cs:			By Profit and Loss A/c	5,24,500
X	18,250		—Net Profit	
Y	13,750			
Z	12,500	44,500		
To Share of Profit trfd. to Capital A/cs:				
X (₹ 4,80,000 × 11/24)	2,20,000			
Y (₹ 4,80,000 × 9/24)	1,80,000			
Z (₹ 4,80,000 × 4/24)	80,000	**4,80,000**		
		5,24,500		5,24,500

6. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Balance *b/d*	1,40,000	By Drawings A/cs:		
To Premium for Goodwill A/c	2,00,000	*X*	1,63,250	
To *Z*'s Capital A/c	2,50,000	*Y*	1,38,750	
To Profit and Loss A/c (*i.e.*, Increase in Cash)	5,24,500	*Z*	32,500	3,34,500
		By Balance *c/d*		**7,80,000**
	11,14,500			11,14,500

Illustration 6.

X and *Y* are partners in a firm sharing profits and losses in the ratio of 3 : 2. They admit *Z* as a partner for 1/5th share. *Z* acquires his share from *X* and *Y* in the ratio of 2 : 3. Goodwill of the firm has been valued at ₹ 50,000. *Z* issued cheques from his account of ₹ 10,000 in favor of '*X*' and '*Y*' as his share of goodwill. What Journal entry in the books of the firm is to be passed?

Solution: No Journal entry will be passed in the books of the firm since *Z* has paid his share of goodwill to *X* and *Y* privately, outside the firm.

Illustration 7.

Pass Journal entry to distribute Workmen Compensation Reserve of ₹ 50,000 at the time of admission of *Z*, when there is no claim against it. The firm has two partners *X* and *Y*.

Solution: JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Workmen Compensation Reserve A/c ...Dr.		50,000	
	To *X*'s Capital A/c			25,000
	To *Y*'s Capital A/c			25,000
	(Being Workmen Compensation Reserve transferred to partners in their old profit-sharing ratio)			

Illustration 8.

Give Journal entry to distribute 'Workmen Compensation Reserve' of ₹ 80,000 at the time of admission of *Z*, when there is claim of ₹ 60,000 against it. The firm has two partners *X* and *Y*.

Solution: JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Workmen Compensation Reserve A/c ...Dr.		80,000	
	To Workmen Compensation Claim A/c			60,000
	To *X*'s Capital A/c			10,000
	To *Y*'s Capital A/c			10,000
	(Being the workmen compensation claim accepted and surplus WCR transferred to partners in their old profit-sharing ratio)			

Notes: After adjusting Workmen Compensation Claim against the Workmen Compensation Reserve, the balance amount of ₹ 20,000 (*i.e.*, ₹ 80,000 – ₹ 60,000) is distributed between *X* and *Y* in their old profit-sharing ratio.

Illustration 9.

Give Journal entry to distribute 'Investment Fluctuation Reserve' of ₹ 40,000 at the time of admission of *Z*, when investment (market value ₹ 1,90,000) appears in the Balance Sheet at ₹ 2,00,000. The firm has two partners *X* and *Y*.

Solution:

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Investment Fluctuation Reserve A/c ...Dr.		40,000	
	To Investment A/c			10,000
	To *X*'s Capital A/c			15,000
	To *Y*'s Capital A/c			15,000
	(Being the value of investment brought down to market value and surplus IFR transferred to old partners in their old profit-sharing ratio)			

Note: In the given case, the market value of investment is ₹ 1,90,000 and the book value is ₹ 2,00,000. So, the fall in the value of ₹ 10,000 will be met through Investment Fluctuation Reserve and balance of ₹ 30,000 will be distributed between the old partners in their old profit-sharing ratio, *i.e.*, equally.

Illustration 10.

Usha and Asha are partners in a firm sharing profits in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2019 was as follows:

Liabilities		₹	Assets		₹
Creditors		27,000	Cash		24,000
General Reserve		18,000	Debtors	48,000	
Bills Payable		5,000	*Less:* Provision for Doubtful Debts	4,800	43,200
Capital A/cs:			Stock		30,000
Usha	40,000		Patents		7,400
Asha	35,000	75,000	Building		20,400
		1,25,000			1,25,000

Neelam is admitted into the partnership giving her 1/5th share in the profits. Neelam is to bring in ₹ 30,000 as her Capital and her share of Goodwill in cash subject to the following terms:

(*i*) Goodwill of the firm to be valued at ₹ 50,000.

(*ii*) Stock to be reduced by 10% and Provision for Doubtful Debts be reduced by ₹ 2,400.

(*iii*) Patents are valueless.

(*iv*) There was a claim against the firm for damages amounted to ₹ 2,000. The claim has now been accepted.

(*v*) The partners have decided that General Reserve is to appear in the books of new firm at its original value.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the new firm.

Solution:

REVALUATION ACCOUNT

Dr. Particulars	₹	Particulars		Cr. ₹
To Stock A/c	3,000	By Provision for Doubtful Debts A/c		2,400
To Patents A/c	7,400	By Loss on Revaluation transferred to:		
To Claim for Damages A/c	2,000	Usha's Capital A/c	6,000	
		Asha's Capital A/c	4,000	10,000
	12,400			12,400

PARTNERS' CAPITAL ACCOUNTS

Dr. Particulars	Usha ₹	Asha ₹	Neelam ₹	Particulars	Usha ₹	Asha ₹	Cr. Neelam ₹
To Revaluation A/c (Loss)	6,000	4,000	...	By Balance *b/d*	40,000	35,000	...
To Usha's Capital A/c	...	...	2,160	By Neelam's Capital A/c	2,160	1,440	...
To Asha's Capital A/c	...	...	1,440	By Cash A/c	...	...	30,000
To Balance *c/d*	42,160	36,440	26,400	By Premium for Goodwill A/c	6,000	4,000	...
	48,160	40,440	30,000		48,160	40,440	30,000

BALANCE SHEET OF NEW FIRM *as at 31st March, 2019*

Liabilities		₹	Assets		₹
Creditors		27,000	Cash (₹ 24,000 + ₹ 40,000)		64,000
Claim for Damages		2,000	Debtors	48,000	
Bills Payable		5,000	*Less:* Provision for Doubtful Debts	2,400	45,600
General Reserve		18,000	Stock (₹ 30,000 – ₹ 3,000)		27,000
Capital A/cs:			Building		20,400
Usha	42,160				
Asha	36,440				
Neelam	26,400	1,05,000			
		1,57,000			1,57,000

Notes:

1. Neelam's Share of Goodwill = ₹ 50,000 × 1/5 = ₹ 10,000, credited to Usha and Asha in their sacrificing ratio, *i.e.*, 3 : 2.
2. *For Adjustment of General Reserve:*

   Dr. Neelam's Capital A/c: ₹ 3,600 (*i.e.*, ₹ 18,000 × 1/5);

   Cr. Usha's Capital A/c: ₹ 2,160 (*i.e.*, ₹ 3,600 × 3/5); and Asha's Capital A/c: ₹ 1,440 (*i.e.*, ₹ 3,600 × 2/5).

Illustration 11.

Rose and Daisy carried on a business in partnership sharing profits and losses in the ratio of 3 : 1. Their Balance Sheet as at 31st March, 2019 was as under:

Liabilities		₹	Assets		₹
Capital A/cs:			Land and Building		62,500
Rose	75,000		Furniture		2,500
Daisy	40,000	1,15,000	Debtors	41,250	
General Reserve		10,000	*Less:* Provision for Doubtful Debts	1,250	40,000
Creditors		93,750	Bills Receivable		7,500
			Stock		50,000
			Cash at Bank		56,250
		2,18,750			2,18,750

Lily was admitted as a partner on 1st April, 2019 on the following terms:

(*i*) She was to bring in ₹ 35,000 as her Capital for 1/5th share in the profits.

(*ii*) Goodwill of the firm was valued at ₹ 1,00,000. Lily was to bring half of her share of Goodwill in cash.

(*iii*) Stock and Furniture were to be reduced in value by 10% and the Provision for Doubtful Debts was to be brought up to 10% of the Debtors.

(*iv*) The value of Land and Building was appreciated by 25%.

(*v*) Creditors include an amount of ₹ 5,000 received as commission from Pinky. The necessary adjustment is required to be made.

You are required to prepare necessary accounts and Balance Sheet of the newly constituted firm. (*ISC 1995, Modified*)

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Stock A/c		5,000	By Land and Building A/c (25% of ₹ 62,500)	15,625
To Furniture A/c		250	By Creditors A/c	5,000
To Provision for Doubtful Debts A/c (₹ 4,125 – ₹ 1,250)		2,875		
To Gain (Profit) on Revaluation:				
Rose (3/4)	9,375			
Daisy (1/4)	3,125	12,500		
		20,625		20,625

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Rose ₹	Daisy ₹	Lily ₹	Particulars	Rose ₹	Daisy ₹	Lily ₹
To Balance *c/d*	1,06,875	50,625	35,000	By Balance *b/d*	75,000	40,000	...
				By General Reserve A/c	7,500	2,500	...
				By Bank A/c	...	...	35,000
				By Premium for Goodwill A/c (WN 1)	7,500	2,500	...
				By Lily's Current A/c (WN 2)	7,500	2,500	...
				By Revaluation A/c (Gain)	9,375	3,125	...
	1,06,875	50,625	35,000		1,06,875	50,625	35,000

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance b/d	56,250	By Balance *c/d*	1,01,250
To Lily's Capital A/c	35,000		
To Premium for Goodwill A/c	10,000		
	1,01,250		1,01,250

BALANCE SHEET *as at 1st April, 2019*

Liabilities		₹	Assets		₹
Capital A/cs:			Land and Building		78,125
Rose	1,06,875		Furniture		2,250
Daisy	50,625		Debtors	41,250	
Lily	35,000	1,92,500	*Less:* Provision for Doubtful Debts	4,125	37,125
Creditors		88,750	Stock		45,000
			Bills Receivable		7,500
			Cash at Bank		1,01,250
			Lily's Current A/c		10,000
		2,81,250			2,81,250

Working Notes:

1. Goodwill brought in part by Lily in cash (₹ 10,000) has been distributed between Rose and Daisy in their sacrificing ratio of 3 : 1.
2. Goodwill not brought in cash out of her share ₹10,000 (*i.e.*, ₹ 1,00,000 × 1/5 × 1/2). It has been adjusted through Lily's Current Account.

Illustration 12.

A and *B* are partners in a firm sharing profits in 2 : 1 ratio. They admitted *C* for 1/4th share in profits. *C* was to bring ₹ 30,000 as capital and capitals of *A* and *B* were to be adjusted in the profit-sharing ratio on the basis of *C*'s Capital. The Balance Sheet of *A* and *B* as at 31st March, 2018 (before *C*'s admission) was:

Liabilities		₹	Assets	₹
Sundry Creditors		20,000	Cash	2,000
Bills Payable		19,000	Sundry Debtors	50,000
General Reserve		6,000	Stock	10,000
Workmen Compensation Reserve		24,000	Machinery	25,000
Capital A/cs:			Building	40,000
A	50,000		Goodwill	15,000
B	32,000	82,000	Advertisement Expenditure	9,000
		1,51,000		1,51,000

Other terms of agreement were:

(*i*) *C* will bring ₹ 12,000 for his share of goodwill.
(*ii*) Building was valued at ₹ 45,000 and Machinery at ₹ 23,000.
(*iii*) A Provision of Doubtful Debts was created @ 6% on Sundry Debtors.
(*iv*) Capital Accounts of *A* and *B* were adjusted by opening Current Accounts.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of *A*, *B* and *C*.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Machinery A/c	2,000	By Building A/c	5,000
To Provision for Doubtful Debts A/c	3,000		
	5,000		5,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	A ₹	B ₹	C ₹	Particulars	A ₹	B ₹	C ₹
To Goodwill A/c	10,000	5,000	...	By Balance *b/d*	50,000	32,000	...
To Advertisement				By General Reserve A/c	4,000	2,000	...
Expenditure A/c	6,000	3,000	...	By Workmen Compensation			
To *A's* Current A/c (Bal. Fig.)	2,000	8,000	...	Reserve A/c	16,000	8,000	...
To Balance *c/d*	60,000	30,000	30,000	By Bank A/c	...	...	30,000
				By Premium for Goodwill A/c	8,000	4,000	...
	78,000	46,000	30,000		78,000	46,000	30,000

BALANCE SHEET OF *A*, *B* AND *C* *as at 31st March, 2018*

Liabilities		₹	Assets		₹
Sundry Creditors		20,000	Cash (₹ 2,000 + ₹ 30,000 + ₹ 12,000)		44,000
Bills Payable		19,000	Sundry Debtors	50,000	
Current A/cs:			*Less:* Provision for Doubtful Debts	3,000	47,000
A	2,000		Stock		10,000
B	8,000	10,000	Machinery		23,000
Capital A/cs:			Building		45,000
A	60,000				
B	30,000				
C	30,000	1,20,000			
		1,69,000			1,69,000

Working Notes:

1. *Calculation of New Profit-Sharing Ratio:*

   C joins the firm for 1/4th share of profits. Therefore, 3/4 (*i.e.*,1 – 1/4) will be shared by *A* and *B* in the ratio of 2 : 1. Thus,

   A's share = 3/4 × 2/3 = 6/12; *B*'s share = 3/4 × 1/3 = 3/12;

   C's share of profit = 1/4,

   Therefore, New Profit-sharing Ratio of *A*, *B* and *C* = 6/12 : 3/12 : 1/4 or 6 : 3 : 3 or 2 : 1 : 1.

2. *Adjustment of Capital:*

   Total capital of the firm on the basis of *C*'s capital = ₹ 30,000 × 4/1 = ₹ 1,20,000

   A's Capital = ₹ 1,20,000 × 6/12 = ₹ 60,000

   B's Capital = ₹ 1,20,000 × 3/12 = ₹ 30,000

   C's Capital = ₹ 1,20,000 × 3/12 = ₹ 30,000.

Illustration 13.

Angad and Vivek are partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 1st January, 2005 stood as follows:

BALANCE SHEET *as at 1st January, 2005*

Liabilities		₹	Assets	₹
Creditors		15,000	Cash	2,000
General Reserve		10,000	Debtors	18,000
Capital A/cs:			Stock	20,000
Angad	30,000		Furniture	10,000
Vivek	25,000	55,000	Plant	30,000
		80,000		80,000

Gopal is admitted as a partner on the above date on the following terms:

(*i*) He will pay ₹ 10,000 towards Goodwill for 1/4th share in profits.

(*ii*) The assets are to be revalued as under:
Plant ₹ 32,000; Stock ₹ 18,000.

(*iii*) A Provision for Bad Debts at 5% on Debtors has to be created.

(*iv*) A sum of ₹ 1,400 included in Creditors is not to be paid. There is an unrecorded liability for ₹ 5,000 which is to be recorded in the books.

(*v*) Gopal is to bring in ₹ 20,000 as capital. The capitals of other partners are to be adjusted in new profit-sharing ratio. For this purpose Current Accounts are to be opened.

Prepare:

(*a*) the Capital Accounts of Angad, Vivek and Gopal.

(*b*) the Balance Sheet of the new firm. (*ISC 2007*)

Solution:

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Angad ₹	Vivek ₹	Gopal ₹	Particulars	Angad ₹	Vivek ₹	Gopal ₹
To Revaluation A/c (Loss) (WN 1)	2,700	1,800	...	By Balance *b/d*	30,000	25,000	...
To Angad's Current A/c (Bal. Fig.—Transfer)	3,300	...	...	By General Reserve A/c	6,000	4,000	...
To Vivek's Current A/c (Bal. Fig.— Transfer)	...	7,200	...	By Cash A/c	...	...	20,000
To Balance *c/d* (WN 3)	36,000	24,000	20,000	By Premium for Goodwill A/c	6,000	4,000	...
	42,000	33,000	20,000		42,000	33,000	20,000

BALANCE SHEET OF THE NEW FIRM *as at 1st January, 2005*

Liabilities		₹	Assets		₹
Creditors (₹ 15,000 – ₹ 1,400)		13,600	Debtors	18,000	
Unrecorded Liability		5,000	*Less:* Provision for Bad Debts	900	17,100
Current A/cs:			Stock (₹ 20,000 – ₹ 2,000)		18,000
Angad	3,300		Furniture		10,000
Vivek	7,200	10,500	Plant (₹ 30,000 + ₹ 2,000)		32,000
Capital A/cs:			Cash		32,000
Angad	36,000				
Vivek	24,000				
Gopal	20,000	80,000			
		1,09,100			1,09,100

Working Notes:

1. *Dr.* REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Stock A/c	2,000	By Plant A/c	2,000
To Provision for Bad Debts A/c	900	By Creditors A/c	1,400
To Unrecorded Liability A/c	5,000	By Loss on Revaluation transferred to:	
		Angad's Capital A/c (₹ 4,500 × 3/5)	2,700
		Vivek's Capital A/c (₹ 4,500 × 2/5)	1,800
	7,900		7,900

2. *Calculation of New Profit-sharing Ratio:*

Gopal is coming for 1/4th share. The remaining $1-\frac{1}{4}$th $=\frac{3}{4}$th share will be divided between Angad and Vivek in the ratio of 3 : 2. Therefore, the new profit-sharing ratio will be:

Angad's Share of Profit = 3/5 of 3/4 = 9/20.

Vivek's Share of Profit = 2/5 of 3/4 = 6/20.

Gopal's Share of Profit = 1/4 = 5/20.

New Profit-sharing Ratio = 9/20 : 6/20 : 5/20 or 9 : 6 : 5.

3. *Calculation of Proportionate Capital of Angad and Vivek on the basis of New Profit-sharing Ratio:*

(*i*) Total Capital of the New Firm $= \dfrac{\text{Capital of the New Partner (Gopal)}}{\text{Share of Profit of the New Partner (Gopal)}}$

$$= \frac{₹\ 20{,}000}{1/4} = ₹\ 20{,}000 \times 4/1 = ₹\ 80{,}000.$$

(*ii*) Angad's Capital = ₹ 80,000 × 9/20 = ₹ 36,000

Vivek's Capital = ₹ 80,000 × 6/20 = ₹ 24,000.

Illustration 14.

Following is the Balance Sheet as at 31st March, 2018 of *A* and *B*, who share profits and losses in the ratio of 3 : 2:

Liabilities		₹	Assets		₹
Capital A/cs:			Plant and Machinery		10,000
A	10,000		Land and Building		8,000
B	10,000	20,000	Debtors	12,000	
General Reserve		15,000	*Less:* Provision for Doubtful Debts	1,000	11,000
Workmen's Compensation Reserve		10,000	Stock		12,000
Creditors		10,000	Cash		9,000
			Profit and Loss A/c		5,000
		55,000			55,000

On 1st April, 2018, they agreed to admit *C* for 1/5th share of profits into partnership on the following terms:

(*i*) Provision for Doubtful Debts would be increased by ₹ 2,000.

(*ii*) Value of Land and Building would be increased to ₹ 18,000.

(*iii*) Value of Stock would be increased by ₹ 4,000.

(*iv*) The liability against the Workmen's Compensation Reserve is determined at ₹ 2,000.

(*v*) *C* brought in as his share of goodwill ₹ 10,000 in cash.

(*vi*) *C* would bring in further cash as would make his capital equal to 20% of the total capital of the new firm after the above revaluation and adjustments are carried out.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet of the firm after *C*'s admission.

Solution:

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Provision for Doubtful Debts A/c		2,000	By Land and Building A/c	10,000
To Gain (Profit) transferred to:			By Stock A/c	4,000
A's Capital A/c	7,200			
B's Capital A/c	4,800	12,000		
		14,000		14,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*A* ₹	*B* ₹	*C* ₹	Particulars	*A* ₹	*B* ₹	*C* ₹
To Profit and Loss A/c	3,000	2,000	...	By Balance *b/d*	10,000	10,000	...
To Balance *c/d* (Balancing Figure)	34,000	26,000	15,000	By Premium for Goodwill A/c	6,000	4,000	...
				By Revaluation A/c	7,200	4,800	...
				By General Reserve A/c	9,000	6,000	...
				By Workmen's Compensation Reserve A/c	4,800	3,200	...
				By Cash A/c (WN)	...	...	15,000
	37,000	28,000	15,000		37,000	28,000	15,000

BALANCE SHEET OF M/s *A*, *B* AND *C*
as at 1st April, 2018

Liabilities		₹	Assets		₹
Capital A/cs:			Land and Building		18,000
A	34,000		Plant and Machinery		10,000
B	26,000		Debtors	12,000	
C	15,000	75,000	*Less:* Provision for Doubtful Debts	3,000	9,000
Liability for Workmen's Compensation		2,000	Stock		16,000
Creditors		10,000	Cash [₹ 9,000 + ₹ 25,000 (WN)]		34,000
		87,000			87,000

Working Note:

Computation of C's Capital:	₹
Capital of *A* after all adjustments	34,000
Capital of *B* after all adjustments	26,000
Combined capital of *A* and *B* for 4/5th share	60,000

∴ Total capital of new firm = ₹ 60,000 × 5/4

C's share in capital = ₹ 60,000 × 5/4 × 1/5 = ₹ 15,000.

Total cash paid by C = Capital (₹ 15,000) + Share of goodwill (₹ 10,000)
= ₹ 25,000.

Illustration 15.

Amit and Sumit are partners sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as at 31st March, 2018 is given below:

Liabilities		₹	Assets		₹
Capital A/cs:			Land and Building		3,20,000
Amit	1,76,000		Investments (Market Value ₹ 55,000)		50,000
Sumit	2,54,000	4,30,000	Debtors	3,00,000	
Loan from Puneet		3,00,000	*Less:* Provision for Doubtful Debts	10,000	2,90,000
General Reserve		30,000	Stock		1,10,000
Employees' Provident Fund		10,000	Cash at Bank		50,000
Creditors		50,000			
		8,20,000			8,20,000

They decided to admit Puneet as a new partner from 1st April, 2018 on the following terms:

(*i*) Amit will give 1/3rd of his share and Sumit will give 1/4th of his share to Puneet.

(*ii*) Puneet's Loan Account will be converted into his Capital.

(*iii*) The Goodwill of the firm is valued at ₹ 3,00,000. Puneet will bring his share of Goodwill in cash and the same was immediately withdrawn by the partners.

(*iv*) Based on the valuation of an Architect, Land and Building was found undervalued by ₹ 1,00,000. Architect was paid ₹ 10,000 as his fee for Valuation Report.

(*v*) Stock was found overvalued by ₹ 50,000.

(*vi*) Provision for Doubtful Debts will be made equal to 5% of Debtors.

(*vii*) Investments are to be valued at their market price.

It was decided that the total capital of the firm after admission of new partner would be ₹ 10,00,000. Capital Accounts of Partners will be readjusted on the basis of their profit-sharing ratio and excess or deficiency will be adjusted in cash.

Prepare (*i*) Revaluation Account; (*ii*) Partners' Capital Accounts; and (*iii*) Balance Sheet of the firm after admission of new partner.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Stock A/c		50,000	By Land and Building A/c	1,00,000
To Provision for Doubtful Debts A/c		5,000	By Investments A/c	5,000
To Bank A/c (Architect's Fee)		10,000		
To Gain (Profit) on Revaluation t/f to:				
Amit's Capital A/c	24,000			
Sumit's Capital A/c	16,000	40,000		
		1,05,000		1,05,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Amit ₹	Sumit ₹	Puneet ₹	Particulars	Amit ₹	Sumit ₹	Puneet ₹
To Bank A/c	60,000	30,000	...	By Balance *b/d*	1,76,000	2,54,000	...
To Balance *c/d* (WN 3)	4,00,000	3,00,000	3,00,000	By General Reserve A/c	18,000	12,000	...
				By Revaluation A/c (Gain)	24,000	16,000	...
				By Puneet's Loan A/c	...	...	3,00,000
				By Premium for Goodwill (WN 2)	60,000	30,000	...
				By Bank A/c (Balancing Figure)	1,82,000	18,000	...
	4,60,000	3,30,000	3,00,000		4,60,000	3,30,000	3,00,000

BALANCE SHEET OF THE NEW FIRM *as at 1st April, 2018*

Liabilities		₹	Assets		₹
Creditors		50,000	Land and Building		4,20,000
Employees' Provident Fund		10,000	Investments		55,000
Capital A/cs:			Debtors	3,00,000	
Amit	4,00,000		*Less:* Provision for Doubtful Debts	15,000	2,85,000
Sumit	3,00,000		Stock		60,000
Puneet	3,00,000	10,00,000	Cash at Bank (WN 4)		2,40,000
		10,60,000			10,60,000

Working Notes:

1. *Calculation of Sacrificing Ratio and New Ratio:*

	Amit	Sumit
(*a*) Their Old Share	3/5	2/5
(*b*) Their Sacrifice	1/5(*i.e.*, 1/3 × 3/5)	1/10(*i.e.*, 1/4 × 2/5)
(*c*) Their New Share (*a* – *b*)	2/5 or 4/10	3/10

∴ Sacrificing Ratio of Amit and Sumit = 1/5 : 1/10 = 2 : 1

Puneet's Share = Sacrifice Share of Amit + Sacrifice Share of Sumit

= 1/5 + 1/10 = 3/10

Thus, New Profit-sharing Ratio of Amit, Sumit and Puneet = 4/10 : 3/10 : 3/10 = 4 : 3 : 3.

2. Puneet's Share of Goodwill = ₹ 3,00,000 × 3/10 = ₹ 90,000, which is contributed by Amit and Sumit in his sacrificing ratio, *i.e.*, 2 : 1.

3. *Capital of the Partners in New Firm:*

Total Capital of the New Firm = ₹ 10,00,000

Thus, Amit's Capital = 4/10 × ₹ 10,00,000 = ₹ 4,00,000;

Sumit's Capital = 3/10 × ₹ 10,00,000 = ₹ 3,00,000;

Puneet's Capital = 3/10 × ₹ 10,00,000 = ₹ 3,00,000.

4. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	50,000	By Revaluation A/c (Architect's Fee)	10,000
To Premium for Goodwill A/c	90,000	By Amit's Capital A/c	60,000
To Amit's Capital A/c	1,82,000	By Sumit's Capital A/c	30,000
To Sumit's Capital A/c	18,000	By Balance *c/d*	2,40,000
	3,40,000		3,40,000

Illustration 16.

X and *Y* are partners sharing profits and losses in the ratio of 3 : 2. They admit *Z* as a new partner from 1st April, 2018. They have decided to share future profits in the ratio of 4 : 3 : 3. The Balance Sheet as at 31st March, 2018 is given below:

Liabilities	₹	Assets		₹
X's Capital	4,40,000	Goodwill		85,000
Y's Capital	6,35,000	Land and Building		1,50,000
Workmen Compensation Reserve	50,000	Investment (Market value ₹ 1,12,500)		1,25,000
Investment Fluctuation Reserve	25,000	Debtors	2,50,000	
Employees' Provident Fund	85,000	*Less:* Provision for Doubtful Debts	25,000	2,25,000
Z's Loan	7,50,000	Stock		7,50,000
		Bank Balance		6,25,000
		Advertisement Suspense A/c		25,000
	19,85,000			19,85,000

Terms of *Z*'s admission are as follows:

(*i*) *Z* contributes proportionate capital and 60% of his share of goodwill by cheque.

(*ii*) Goodwill is to be valued at 2 years' purchase of super profit of last three completed years. Profits for the years ended 31st March were:

2016—₹ 12,00,000; 2017—₹ 23,25,000; 2018—₹ 34,50,000.

The normal profit is ₹ 13,25,000 with same amount of capital invested in similar industry.

(*iii*) Land and Building was found undervalued by ₹ 2,50,000.

(*iv*) Stock was found overvalued by ₹ 77,500.

(*v*) Provision for Doubtful Debts is to be made equal to 5% of the debtors.

(*vi*) Claim on account of Workmen Compensation is ₹ 25,000.

(*vii*) Workmen Compensation Reserve and Investment Fluctuation Reserve are to appear in the books of the new firm after adjusting Workmen Compensation Claim and difference between the book value and market value of investment. This adjustment is to be made through Partners' Current Accounts.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the new firm.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars		₹
To Stock A/c		77,500	By Land and Building A/c		2,50,000
To Gain (Profit) on Revaluation transferred to:			By Provision for Doubtful Debts A/c:		
			Existing	25,000	
X's Capital A/c	1,11,000		*Less:* Required (₹ 2,50,000 × 5/100)	12,500	12,500
Y's Capital A/c	74,000	1,85,000			
		2,62,500			2,62,500

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*X* ₹	*Y* ₹	*Z* ₹	Particulars	*X* ₹	*Y* ₹	*Z* ₹
To Goodwill A/c	51,000	34,000	...	By Balance *b/d*	4,40,000	6,35,000	...
To Advertisement Suspense A/c	15,000	10,000	...	By Bank A/c (WN 5)	...	...	7,50,000
To Balance *c/d*	8,85,000	8,65,000	7,50,000	By Premium for Goodwill A/c	2,40,000	1,20,000	...
				By *Z*'s Current A/c (WN 3)	1,60,000	80,000	...
				By Revaluation A/c (Profit)	1,11,000	74,000	...
	9,51,000	9,09,000	7,50,000		9,51,000	9,09,000	7,50,000

Dr. PARTNERS' CURRENT ACCOUNTS *Cr.*

Particulars	*X* ₹	*Y* ₹	*Z* ₹	Particulars	*X* ₹	*Y* ₹	*Z* ₹
To *X*'s Capital A/c (WN 3)	...	...	1,60,000	By *Z*'s Current A/c (WN 4)	7,500	3,750	...
To *Y*'s Capital A/c (WN 3)	...	...	80,000	By Balance *c/d*	...	...	2,51,250
To *X*'s Current A/c (WN 4)	...	...	7,500				
To *Y*'s Current A/c (WN 4)	...	...	3,750				
To Balance *c/d*	7,500	3,750	...				
	7,500	3,750	2,51,250		7,500	3,750	2,51,250

BALANCE SHEET OF THE NEW FIRM
as at 1st April, 2018

Liabilities		₹	Assets		₹
Employees' Provident Fund		85,000	Land and Building		4,00,000
Workmen Compensation Claim		25,000	Investment		1,12,500
Workmen Compensation Reserve		25,000	Debtors	2,50,000	
(₹ 50,000 – ₹ 25,000)			*Less:* Provision for Doubtful Debts	12,500	2,37,500
Investment Fluctuation Reserve		12,500	Stock		6,72,500
Z's Loan		7,50,000	Bank Balance		17,35,000
Current Accounts:			*Z*'s Current Account		2,51,250
X	7,500				
Y	3,750	11,250			
Capital Accounts:					
X	8,85,000				
Y	8,65,000				
Z	7,50,000	25,00,000			
		34,08,750			34,08,750

Working Notes:

1. *Calculation of Sacrificing Ratio:*

		X	*Y*
(*a*)	Their Old Share	3/5	2/5
(*b*)	Their New Share	4/10	3/10
(*c*)	Share surrendered by old partner (*a* – *b*)	3/5 – 4/10 = 2/10	2/5 – 3/10 = 1/10

(*d*) Sacrificing Ratio of *X* and *Y* = 2/10 : 1/10 = 2 : 1.

2. *Calculation of Z's Share of Goodwill:*

(*a*) Average Profit = $\dfrac{₹\ 4{,}80{,}000 + ₹\ 9{,}30{,}000 + ₹\ 13{,}80{,}000}{3}$ = ₹ 23,25,000

(*b*) Normal Profit = ₹ 13,25,000

(*c*) Super Profit = ₹ 23,25,000 – ₹ 13,25,000 = ₹ 10,00,000

(*d*) Firm's Goodwill = Super Profit × No. of years' purchase = ₹ 10,00,000 × 2 = ₹ 20,00,000

(*e*) *Z*'s Share of Goodwill = ₹ 20,00,000 × 3/10 = ₹ 6,00,000.

3. *Journal Entries with respect to Goodwill:*

			₹	₹
(*i*)	Bank A/c	...Dr.	3,60,000	
	To Premium for Goodwill A/c			3,60,000
(*ii*)	Premium for Goodwill A/c	...Dr.	3,60,000	
	To *X*'s Capital A/c			2,40,000
	To *Y*'s Capital A/c			1,20,000
(*iii*)	*Z*'s Current A/c (₹ 6,00,000 – ₹ 3,60,000)	...Dr.	2,40,000	
	To *X*'s Capital A/c			1,60,000
	To *Y*'s Capital A/c			80,000

4. *For Adjustment of Workmen Compensation Reserve and Investment Fluctuation Reserve:*

	₹
Workmen Compensation Reserve = ₹ 50,000 – ₹ 25,000 (Claim)	25,000
Investment Fluctuation Reserve = ₹ 25,000 – (₹ 1,25,000 – ₹ 1,12,500)	12,500
	37,500

Adjustment Journal Entry with respect to Workmen Compensation Reserve and Investment Fluctuation Reserve:

	₹	₹
Z's Current A/c (₹ 37,500 × 3/10)	11,250	
To *X*'s Current A/c (₹ 37,500 × 2/10)		7,500
To *Y*'s Current A/c (₹ 37,500 × 1/10)		3,750

5. *Calculation of Z's Capital:*

	₹
X's Adjusted Capital	8,85,000
Y's Adjusted Capital	8,65,000
X's and *Y*'s Capital for 7/10th share	17,50,000

Thus, *Z*'s Capital for 3/10th share = ₹ 17,50,000 × 10/7 × 3/10 = ₹ 7,50,000.

6. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	6,25,000	By Balance *c/d*	17,35,000
To Premium for Goodwill A/c	3,60,000		
To *Z*'s Capital A/c	7,50,000		
	17,35,000		17,35,000

Master Question

Illustration 17.

Rohan, Sohan and Mohan are partners sharing Profits and Losses in the ratio of 5 : 4 : 1. Their Balance Sheet as at 31st March, 2019 was as follows:

Liabilities		₹	Assets		₹
Sundry Creditors		2,50,000	Cash at Bank		4,20,000
Salaries Payable		60,000	Sundry Debtors	2,00,000	
Outstanding Expenses		20,000	*Less:* Provision for Doubtful Debts	20,000	1,80,000
General Reserve		1,80,000	Stock		1,00,000
Workmen Compensation Reserve		2,00,000	Furniture		1,80,000
Investment Fluctuation Reserve		2,20,000	Computers		4,00,000
Capital A/cs:			Car		4,00,000
Rohan	6,00,000		Advertisement Expenses		50,000
Sohan	3,00,000		Building		4,00,000
Mohan	3,00,000	12,00,000			
		21,30,000			21,30,000

Profit-sharing ratio w.e.f. 1st April, 2019 was decided to be equal. It was agreed among the partners to carry out following adjustments:

(*i*) Stock to be reduced to ₹ 80,000.

(*ii*) All debtors are good.

(*iii*) Computers to be reduced by ₹ 40,000.

(*iv*) Out of the salaries payable ₹ 20,000 was not payable as the employee left without notice.

(*v*) Outstanding Expenses were not payable.

(*vi*) An unrecorded asset (Motor Cycle) valued at ₹ 20,000 to be accounted.

(*vii*) The average profit earned by the firm is ₹ 2,50,000 which includes overvaluation of stock of ₹ 15,000 on an average basis. The capital invested in the business is ₹ 14,00,000 and the normal rate of return is 15%. Goodwill of the firm is valued on the basis of 2 times the super profit.

(*viii*) Workmen Compensation claim is estimated at ₹ 1,00,000.

(*ix*) Total capital of the firm ₹ 12,00,000 was to be in profit-sharing ratio, excess capital to be withdrawn and shortfall to be made good.

Prepare Revaluation Account, Partner's Capital Accounts and Balance Sheet of the new firm.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Stock A/c		20,000	By Provision for Doubtful Debts A/c	20,000
To Computers A/c		40,000	By Salaries Payable A/c	20,000
To Gain (Profit) transferred to:			By Outstanding Expenses A/c	20,000
Rohan	10,000		By Motor Cycle	20,000
Sohan	8,000			
Mohan	2,000	20,000		
		80,000		80,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Rohan ₹	Sohan ₹	Mohan ₹	Particulars	Rohan ₹	Sohan ₹	Mohan ₹
To Advertisement Exp. A/c	25,000	20,000	5,000	By Balance *b/d*	6,00,000	3,00,000	3,00,000
To Rohan's Capital A/c	...	...	8,334	By Revaluation	10,000	8,000	2,000
To Sohan's Capital A/c	...	...	3,333	By General Reserve	90,000	72,000	18,000
To Bank A/c (Bal. Fig.)	4,43,334	91,333	...	By Workman Compensation Reserve	50,000	40,000	10,000
To Balance *c/d*	4,00,000	4,00,000	4,00,000	By Investment Fluctuation Reserve	1,10,000	88,000	22,000
				By Mohan's Capital A/c	8,334	3,333	...
				By Bank	...	...	64,667
	8,68,334	5,11,333	4,16,667		8,68,334	5,11,333	4,16,667

BALANCE SHEET
as on ...

Liabilities		₹	Assets	₹
Bank Overdraft		50,000	Sundry Debtors	2,00,000
Salaries Payable		40,000	Stock	80,000
Creditors		2,50,000	Furniture	1,80,000
Workmen Compensation Claim		1,00,000	Computers	3,60,000
Capital A/cs:			Car	4,00,000
Rohan	4,00,000		Motor Cycle	20,000
Sohan	4,00,000		Building	4,00,00
Mohan	4,00,000	12,00,000		
		16,40,000		16,40,000

Working Notes:

1. *Calculation of Goodwill of Firm:*

Average Profit = ₹ 2,50,000

Overvaluation of Stock = ₹ 1,5000

Adjusted Average Profit = ₹ 2,50,000 – ₹ 15,000 (Note) = ₹ 2,35,000

Normal Profit = Capital Employed (Investment) × NRR

$$= ₹\ 14,00,000 \times \frac{15}{100} = ₹\ 2,10,000$$

Super Profit = Adjusted Average Profit – Normal Profit

= ₹ 2,35,000 – ₹ 2,10,000 = ₹ 25,000

Goodwill = Super Profit × 2

= ₹ 25,000 × 2 = ₹ 50,000.

2. *Calculation of Sacrifice/Gain of each Partner:*

Particulars	Rohan	Sohan	Mohan
A. Old Share	5/10	4/10	1/10
B. New Share	1/3	1/3	1/3
C. Sacrifice/Gain (A – B)	5/10 – 1/3	4/10 – 1/3	1/10 – 1/3
	= 5/30 (Sacrifice)	2/30 (Sacrifice)	7/30 (Gain)

Note: Overvaluation of stock increases the net profit. Hence it has been deducted to calculate adjusted average profit.

3. *Adjustment of Goodwill:*

Mohan's Capital A/c	...Dr.	₹ 11,667	
To Rohan's Capital A/c			₹ 8333
To Sohan's Capital A/c			₹ 3,334

4. Total Capital of the Firm = ₹ 12,00,000
   Capital of each partner in the new firm as per new PGR will be ₹ 4,00,000.

5.

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	4,20,000	By Rohan's Capital A/c	4,43,334
To Mohan's Capital A/c	64,667	By Sohan's Capital A/c	91,333
To Balance *c/d*	50,000		
	5,34,667		5,34,667

Unsolved Questions

1. *A* and *B* are partners in a firm sharing Profits and Losses in the ratio of 17 : 16. They admit *C* as a partner on 1st April, 2016 on the basis of his buying 5/17th of *A*'s share and 4/16th of *B*'s share. On 1st April, 2018 they permit *C* to purchase further 1/12th of their remaining shares. Goodwill is agreed to be valued at 2 years' purchase of the average profits of 3 years immediately before any change. Profits for the 5 years ended 31st March, 2018 are:

Years Ended	31st March, 2014	31st March, 2015	31st March, 2016	31st March, 2017	31st March, 2018
Profits (₹)	61,560	64,520	81,660	94,140	1,15,120

You are required to determine the amount to be paid by *C* to each partner on both the occasions and their ultimate Profit-sharing Ratio.

2. *A* and *B* are partners sharing profits in the ratio of 3 : 2. They admit *C* into the firm for 3/7th share in profits which he takes 2/7th from *A* and 1/7th from *B* and brings ₹ 10,000 as premium out of his share of ₹ 16,000. Pass Journal entries for the above.

3. On the admission of Rao, it was agreed that the goodwill of Murty and Shah should be valued at ₹ 30,000. Rao is to get 1/4th share of profits. Previously Murty and Shah shared profits in the ratio of 3 : 2. Rao cannot bring his share of Goodwill. Give Journal entries in the books of Murty and Shah when: (i) there is no Goodwill Account; (ii) Goodwill appears at ₹ 10,000.

4. Following is the Balance Sheet of the firm, Ashirvad, owned by *A*, *B* and *C* who share profits and losses of the business in the ratio of 3 : 2 : 1:

BALANCE SHEET

as at 31st March, 2018

Liabilities		₹	Assets	₹
Capital A/cs:			Furniture	95,000
A	1,20,000		Business Premises	2,05,000
B	1,20,000		Stock-in-Trade	40,000
C	1,20,000	3,60,000	Debtors	28,000
Sundry Creditors		20,000	Cash at Bank	15,000
Outstanding Salaries and Wages		7,200	Cash in Hand	4,200
		3,87,200		3,87,200

On 1st April, 2018, they admit *D* as a partner on the following conditions:

(i) *D* will bring ₹ 1,20,000 as his Capital and also ₹ 30,000 as Goodwill premium for a quarter of the share in the future profit/loss of the firm.

(ii) The values of the fixed assets of the firm will be increased by 10% before the admission of *D*.

(iii) The future profits and losses of the firm will be shared equally by all the partners.

Show Journal entries, Revaluation Account, Partners' Capital Accounts and the opening Balance Sheet of the new firm to include the above-mentioned transactions assuming that the conditions were duly satisfied.

5. Jain and Gupta were partners in a firm sharing profits and losses in the ratio of 4 : 3. Following is the Balance Sheet of the firm as at 31st March, 2018:

BALANCE SHEET OF JAIN AND GUPTA *as at 31st March, 2018*

Liabilities		₹	Assets		₹
Sundry Creditors		20,000	Cash		14,800
Bills Payable		3,000	Debtors	20,500	
Bank Overdraft		17,000	*Less:* Provision for Doubtful Debts	300	20,200
Capital A/cs:			Stock		20,000
Jain	70,000		Plant		40,000
Gupta	60,000	1,30,000	Building		75,000
		1,70,000			1,70,000

They agreed to admit Mishra as partner with effect from 1st April, 2018 with 1/4th share in profits on the following terms:

(i) Mishra will bring in Capital to the extent of 1/4th of the total capital of the new firm after all adjustments have been made.

(ii) Building is to be appreciated by ₹ 14,000 and Plant to be depreciated by ₹ 7,000.

(iii) The Provision for Doubtful Debts on Debtors is to be raised to ₹ 1,000.

(iv) Mishra will bring ₹ 21,000 as his share of Goodwill.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the firm immediately after Mishra's admission.

6. *A* and *B* are partners in a firm sharing profits in the ratio of 5 : 3. Their Balance Sheet as at 31st March, 2018 is given below:

Liabilities		₹	Assets	₹
Capital A/cs:			Goodwill	10,000
A	55,000		Land and Building	25,000
B	30,000	85,000	Pant and Machinery	35,000
Creditors		19,000	Stock	20,000
Bills Payable		8,000	Debtors	25,000
General Reserve		16,000	Investments	14,000
Provision for Doubtful Debts		1,500	Cash	2,400
Outstanding Salary		2,400	Prepaid Insurance	500
		1,31,900		1,31,900

They agreed to admit *C* on 1st April, 2018 for 1/5th share of profit in future on the following terms:

(i) *C* brings in ₹ 5,200 as his share of Goodwill in cash and will bring in such an amount that his Capital will be 1/5th of the total capital of the new firm.

(ii) Land and Building and Plant and Machinery were to be valued at ₹ 38,000 and ₹ 30,000 respectively.

(iii) The Provision for Doubtful Debts was to be maintained up to ₹ 1,000.

(iv) A Liability for ₹ 1,200 included in Sundry Creditors was not likely to arise.

(v) Investments of ₹ 10,000 were taken over by old partners in their profit-sharing ratio.

(vi) *B* is to withdraw ₹ 2,400 in cash.

(vii) An amount of ₹ 100 is outstanding for repairs.

Prepare Revaluation Account, Partners' Capital Accounts, and Balance Sheet of the new firm.

GUIDE TO ANSWERS

1. *On Ist Occassion (1st April, 2016):*

Amount to be paid by *C*—₹ 20,984 to *A* and ₹ 16,787 to *B*. New Profit-sharing Ratio—4 : 4 : 3.

On 2nd Occassion (1st April, 2018):

Amount to be paid by *C*—₹ 5,877 to *A* and *B* each; New Profit-sharing Ratio—1 : 1 : 1.

Valuation of Goodwill:

$$\text{Average Profit} = \frac{₹\,61{,}560 + ₹\,64{,}520 + ₹\,81{,}660}{3} = ₹\,69{,}247$$

Goodwill at 2 Years' Purchase of Average Profit = ₹ 69,247 × 2 = ₹ 1,38,494.

$$C\text{'s Share in Goodwill} = ₹\,1{,}38{,}494 \times \frac{3}{11} = ₹\,37{,}771.$$

2. (i) Dr. Bank A/c and Cr. Premium for Goodwill A/c by ₹ 10,000.

(ii) Dr. Premium for Goodwill A/c—₹ 10,000; Cr. *A*'s Capital A/c—₹ 6,667 and *B*'s Capital A/c—₹ 3,333.

(iii) Dr. *C*'s Current A/c—₹ 6,000; Cr. *A*'s Capital A/c—₹ 4,000 and *B*'s Capital A/c—₹ 2,000.

3. (i) Dr. Rao's Current A/c—₹ 7,500; Cr. Murty's Capital A/c—₹ 4,500 and Shah's Capital A/c—₹ 3,000.

(ii) (a) Dr. Murty's Capital A/c—₹ 6,000 and Shah's Capital A/c—₹ 4,000; Cr. Goodwill A/c—₹ 10,000.

(b) Dr. Rao's Current A/c—₹ 7,500; Cr. Murty's Capital A/c—₹ 4,500 and Shah's Capital A/c—₹ 3,000.

4. Gain (Profit) on Revaluation—₹ 30,000; Capital Balances: *A*—₹ 1,65,000; *B*—₹ 1,40,000; *C*—₹ 1,15,000; *D*—₹ 1,20,000; Total of Balance Sheet—₹ 5,67,200.

[**Hint:** Change in profit-sharing ratio will result in loss of 6/24th to *A* and 2/24th to *B*; gain of 2/24th to *C* and 1/4th to *D*. Hence, the entry for adjustment of goodwill premium will be:

		₹	₹
C's Capital A/c	...Dr.	10,000	
Premium for Goodwill A/c	...Dr.	30,000	
To *A*'s Capital A/c			30,000
To *B*'s Capital A/c			10,000.]

5. Gain (Profit) on Revaluation—₹ 6,300; Capital Accounts of Jain—₹ 85,600; Gupta—₹ 71,700 and Mishra—₹ 52,433; Total of Balance Sheet—₹ 2,49,733.

[**Hint:** *Calculation of Mishra's Capital:* Combined Capital of Jain and Gupta (after adjustments) for 3/4th share = ₹ 85,600 + ₹ 71,700 = ₹ 1,57,300

New Firm's Total Capital = ₹ 1,57,300 × 4/3

Mishra's Capital for 1/4th share = ₹ 1,57,300 × 4/3 × 1/4 = ₹ 52,433.]

6. Gain (Profit) on Revaluation—₹ 9,600; Capital A/cs: *A*—₹ 61,750; *B*—₹ 31,650; *C*—₹ 23,350; Total of Balance Sheet—₹ 1,46,050.

[**Hint:** Capitals of *A* and *B* after all adjustments are ₹ 61,750 and ₹ 31,650 respectively. Hence, the combined capital of *A* and *B* is equal to ₹ 93,400 which is 4/5(1 – 1/5) of the capital of the firm.
Hence, *C*'s 1/5th share in the capital will be: ₹ 93,400 × 5/4 × 1/5 = ₹ 23,350.]

CHAPTER 4

Retirement and Death of a Partner

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Retirement of a Partner

When a partner ceases to be a partner of the firm (other than because of death), it is known as **retirement of a partner**.

A partner may retire from the firm:

(*i*) if there is an agreement to that effect, or

(*ii*) if all the partners agree to his/her retirement, or

(*iii*) if the partnership is at will, by giving notice in writing to other partners of his or her intention to retire.

It leads to reconstitution of the firm.

2. Death of a Partner

Death of a partner also leads to reconstitution of the firm. The firm may continue its business with the remaining partners.

3. Revaluation of Assets

Revaluation of Assets means change in the value of assets, *i.e.*, present value being different from the book value of the assets.

4. Reassessment of Liabilities

Reassessment of Liabilities means reassessing the liabilities and determining the change, *i.e.*, whether the liability is more or less than that shown in the books of account.

5. Gaining Ratio

Ratio in which the continuing partners acquire outgoing (retired or deceased) partner's share is called **gaining ratio**.

6. New Profit-sharing Ratio

Ratio in which the continuing partners (*i.e.*, partners other than outgoing partner) decide to share future profits and losses, is known as **new profit-sharing ratio**.

7. Profit and Loss Suspense Account

It is the account which is debited to adjust the share of profit of outgoing partner between the date of last Balance Sheet and the date of death/retirement, when profit-sharing ratio of continuing partners does not change.

SUMMARY OF THE CHAPTER

- **Retirement of a Partner:** When a partner ceases to be a partner it is called **'Retirement of a Partner'**.
- **Adjustment on Retirement of a Partner:** At the time of retirement of a partner, few accounting issues arise and are settled, *e.g.*, calculation of the new profit-sharing ratio and the gaining ratio, revaluation of assets and liabilities, treatment of goodwill, accumulated profits, reserves and surplus, share in profits or losses of the outgoing partner up to the date of retirement.

- **New Profit-sharing Ratio:** The ratio in which the continuing partners (*i.e.*, partners other than the outgoing one) decide to share the future profits and losses, is known as the **'New Profit-sharing Ratio'**.

  New Share = Old Share + Acquired Share

  Unless agreed otherwise, it is presumed that the continuing partners acquire the outgoing partner's share in their old profit-sharing ratio.

- **Gaining Ratio:** The ratio in which the continuing partners acquire the outgoing (retired or the deceased) partner's share is known as the **'Gaining Ratio'**.

  Gaining Ratio = New Ratio – Old Ratio

  Gain of a Partner = New Share – Old Share

- **Adjustment with regard to Goodwill:** When a partner retires (or dies) his share of profit is taken by the remaining partners. *The remaining partners then compensate the retiring or deceased partner in the form of goodwill in their gaining ratio.* The following entry is recorded for this purpose:

  Gaining Partners' Capital/Current A/cs ...Dr. [In gaining ratio]
  To Retiring/Deceased Partner's Capital/Current A/c [With his share of goodwill]

  If Goodwill Account appears in the old Balance Sheet, it is written off by passing the following entry:

  All Partners' Capital/Current A/cs ...Dr. [In old ratio]
  To Goodwill A/c

- **Hidden Goodwill:** If a firm pays an amount in excess of total amount due to the retiring partner (after making all adjustments), then the excess amount is treated as hidden goodwill or his share of goodwill.

- **Revaluation of Assets and Reassessment of Liabilities:** At the time of retirement of a partner, assets are revalued and liabilities are reassessed; the increase or decrease in value of each asset/liability is recorded in the Revaluation Account. The net balance in the Revaluation Account is transferred to the Capital Accounts of all the partners (including the outgoing partner) in their old profit-sharing ratio.

- **Adjustment for Reserves and Accumulated Profits/Losses:** For the past undistributed profits or reserves, the amount is credited to all the partners in the old profit-sharing ratio.

- *Excess of Workmen Compensation Reserve over the Workmen Compensation Liability is* **credited to all Partners** *in their* **Old Profit-sharing Ratio**.

- *Excess of Investment Fluctuation Reserve over difference between Book Value and Market Value is* **credited to all Partners** *in their* **Old Profit-sharing Ratio**.

- **Adjustments for Reserves and Accumulated Profits/Losses through Single Adjustment Entry:** The net effect may also be adjusted through the following entry:

  (*i*) In Case of Net Profit: Gaining Partners' Capital/Current A/cs ...Dr..
  To Sacrificing Partners' Capital/Current A/c

  (*ii*) In Case of Net Loss: Sacrificing Partners' Capital/Current A/cs ...Dr.
  To Gaining Partners' Capital/Current A/cs

- **Amount Due to a Retiring Partner:** Amount due to a retiring partner includes:

  (*i*) Capital on the date of last Balance Sheet.

  (*ii*) Interest or salary, if any, payable to him.

(*iii*) Share of profit or loss till the date of retirement.

(*iv*) Share in the gain (profit) or loss on revaluation of assets and reassessment of liabilities.

(*v*) Share in the goodwill of the firm.

(*vi*) Share in the General Reserve or Profit and Loss Account appearing in the Balance Sheet.

Out of the total of (*i*) to (*vi*), the amount of drawings and interest on drawings till the date of retirement is deducted.

The net amount payable will be settled by paying him cash or by transferring it to a separate Loan Account.

DEATH OF A PARTNER

- The issues arising on the death of a partner are similar to those arising on retirement of a partner. Assets are revalued and liabilities are reassessed; the resultant profit or loss is transferred to the Capital Accounts of all partners including the deceased partner. *Goodwill, Accumulated Profit or Loss and the General Reserve are also dealt in the same manner as is in the case of retirement.*

- **Share of Profit up to the Date of Death:** If a partner dies on any date after the date of Balance Sheet; his share of profit is calculated from the beginning of the accounting year to the date of death on the basis of average profits or last year's profit. It is calculated on the basis of time; or on the basis of sales.

  Journal Entry for both the basis:

  Profit and Loss Suspense A/c ...Dr.
  To Deceased Partner's Capital A/c

  Note: The balance of Profit and Loss Suspense Account is shown in the interim Balance Sheet, *i.e.*, Balance Sheet after retirement.

Retiring or Deceased Partner's share of profit will be credited to his Capital Account and debited to the continuing Partners' Capital Accounts in the **Gaining Ratio** when the profit-sharing ratio of the continuing partners, in between them, changes.

Gaining Partners' Capital/Current A/cs ...Dr. [in Gaining Ratio]
To Retiring/Deceased Partner's Capital A/c

- **Amount Due to Deceased Partner:** The deceased partner's share is also calculated in the same way as in the case of retiring partner's share. Amount due to a deceased partner shown by his Capital Account is transferred to his Executor's Account. The entry will be:

  Deceased Partner's Capital A/c ...Dr.
  To Deceased Partner's Executor's A/c

- **Settlement of Deceased Partner's Executor's Account:** If the amount is paid in cash or in instalment, the entry will be:

  Deceased Partner's Executor's A/c ...Dr.
  To Cash/Bank A/c

- In the absence of an agreement, the outgoing partner at his option is entitled to receive *either interest @ 6% p.a.* till the amount is paid off or *a share of the profit* which has been earned by using the amount due to him. [Section 37 of Indian Partnership Act, 1932]

Solved Questions

Illustration 1.

A, *B* and *C* are in partnership sharing profits and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March, 2017 stood as follows:

Liabilities		₹	Assets		₹
Capital A/cs:			Machinery at cost	50,000	
A	40,000		*Less:* Provision for Depreciation	8,000	42,000
B	60,000		Furniture		1,000
C	20,000	1,20,000	Sundry Debtors	80,000	
Reserve		30,000	*Less:* Provision for Doubtful Debts	3,000	77,000
Sundry Creditors		60,000	Stock		50,000
			Cash at Bank		40,000
		2,10,000			2,10,000

On 30th June, 2017, *B* retired and *A* and *C* continued in partnership, sharing profits and losses in the ratio of 3 : 2. They agreed to the following adjustments in the books of account to decide *B*'s Share:

(*i*) Machinery to be revalued at ₹ 45,000.

(*ii*) Stock to be reduced by ₹ 1,000.

(*iii*) Furniture to be reduced to 60%.

(*iv*) Provision for Doubtful Debts to be maintained at 5%.

(*v*) Provision of ₹ 300 to be made for Outstanding Expenses.

(*vi*) Goodwill of the firm to be valued at ₹ 24,000 and *B*'s share of the same was to be adjusted into the accounts of *A* and *C*.

(*vii*) The profits up to the date of retirement from the date of last Balance Sheet was estimated at ₹ 18,000. All the partners are to be credited with their respective share of profit earned till the date of retirement of *B*.

(*viii*) *B* was to be paid off in full. *A* and *C* were to bring sufficient amount so as to make their capitals in proportion to the new profit-sharing ratio, subject to the condition that a cash balance of ₹ 20,000 was to be maintained as working capital. Before making this adjustment the cash balance was ₹ 58,000 on 30th June, 2017.

Pass necessary Journal entries to give effect to the above arrangements and prepare Partners' Capital Accounts as on 30th June, 2017.

Solution:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2017	*A*'s Capital A/c	...Dr.		2,400	
June 30	*C*'s Capital A/c	...Dr.		5,600	
	To *B*'s Capital A/c				8,000
	(Being *B*'s share of goodwill adjusted in the Capital Accounts of *A* and *C* in the gaining ratio of 3 : 7) (WN 1 and 2)				

Revaluation A/c ...Dr.		2,700	
To Stock A/c			1,000
To Provision for Doubtful Debts A/c			1,000
To Furniture A/c			400
To Provision for Outstanding Expenses A/c			300
(Being the decrease in assets and increase in liabilities)			
Machinery A/c ...Dr.		3,000	
To Revaluation A/c			3,000
(Being the increase in the value of machinery)			
Revaluation A/c ...Dr.		300	
To *A*'s Capital A/c			150
To *B*'s Capital A/c			100
To *C*'s Capital A/c			50
(Being the gain (profit) on revaluation divided in the old ratio)			
Reserve A/c ...Dr.		30,000	
To *A*'s Capital A/c			15,000
To *B*'s Capital A/c			10,000
To *C*'s Capital A/c			5,000
(Being the transfer of Reserve to the Partners' Capital Accounts in the old ratio)			
Profit and Loss Suspense A/c ...Dr.		18,000	
To *A*'s Capital A/c			9,000
To *B*'s Capital A/c			6,000
To *C*'s Capital A/c			3,000
(Being the estimated profit till the date of retirement transferred to the Capital Accounts in the old ratio)			
Bank A/c ...Dr.		46,100	
To *A*'s Capital A/c			16,430
To *C*'s Capital A/c			29,670
(Being the cash brought in by *A* and *C* as per agreement) (WN 3)			
B's Capital A/c ...Dr.		84,100	
To Bank A/c			84,100
(Being the payment made to *B* on his retirement)			

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*A* (₹)	*B* (₹)	*C* (₹)	Particulars	*A* (₹)	*B* (₹)	*C* (₹)
To *B*'s Capital A/c (WN1) (Goodwill)	2,400	...	5,600	By Balance *b/d*	40,000	60,000	20,000
				By *A*'s Capital A/c (WN 1)	...	2,400	...
To Bank A/c (Balancing Figure)	...	84,100	...	By *C*'s Capital A/c (WN 1)	...	5,600	...
				By Revaluation A/c	150	100	50
To Balance *c/d*	78,180	...	52,120	By Reserve A/c	15,000	10,000	5,000
				By Profit and Loss Suspense A/c	9,000	6,000	3,000
				By Bank A/c (WN 3)	16,430	...	29,670
	80,580	84,100	57,720		80,580	84,100	57,720

Working Notes:

1. *Adjustment of Goodwill:*

   B's Share of Goodwill = ₹ 24,000 × 2/6 = ₹ 8,000, which is contributed by *A* and *C* in their Gaining Ratio of 3 : 7.

   A's contribution = ₹ 8,000 × 3/10 = ₹ **2,400**.

   C's contribution = ₹ 8,000 × 7/10 = ₹ **5,600**.

2. *Computation of Gaining Ratio:*

   Gain = New Share – Old Share

   A's Gain = 3/5 – 3/6 = 3/30; *C*'s Gain = 2/5 – 1/6 = 7/30

   Gaining Ratio = 3/30 : 7/30 or **3 : 7**

3. *Cash to be brought in by A and C*:

	₹
Amount payable to *B*	84,100
Add: Amount to be retained as Working Capital	20,000
	1,04,100
Less: Cash already available	58,000
Cash to be brought in by *A* and *C*	46,100

   Adjusted Old Capital of *A* ₹ (40,000 + 150 + 15,000 + 9,000 – 2,400) = ₹ 61,750.

   Adjusted Old Capital of *C* ₹ (20,000 + 50 + 5,000 + 3,000 – 5,600) = ₹ 22,450.

   Total Capital of the New Firm (₹ 46,100 + ₹ 61,750 + ₹ 22,450) = ₹ 1,30,300.

   A will bring (₹ 1,30,300 × 3/5 – ₹ 61,750) = ₹ 78,180 – ₹ 61,750 = ₹ **16,430**.

   C will bring (₹ 1,30,300 × 2/5 – ₹ 22,450) = ₹ 52,120 – ₹ 22,450 = ₹ **29,670**.

Illustration 2.

A, *B* and *C* were equal partners. Their Balance Sheet as at 31st March, 2018 is given below:

BALANCE SHEET *as at 31st March, 2018*

Liabilities		₹	Assets		₹
Bills Payable		20,000	Bank		20,000
Creditors		40,000	Stock		20,000
General Reserve		30,000	Furniture		28,000
Profit and Loss A/c		6,000	Debtors	45,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	5,000	40,000
A	60,000		Land and Building		1,20,000
B	40,000				
C	32,000	1,32,000			
		2,28,000			2,28,000

B retired on 1st April, 2018. *A* and *C* decided to continue the business as equal partners on the following terms:

(*i*) Goodwill of the firm was valued at ₹ 57,600.

(*ii*) Provision for Doubtful Debts to be maintained @ 10% on Debtors.

(*iii*) Land and Building to be increased to ₹ 1,32,000.

(*iv*) Furniture to be reduced by ₹ 8,000.

(*v*) Rent Outstanding (not provided for as yet) was ₹ 1,500.

The remaining partners decided to bring sufficient cash in the business to pay off *B* and to maintain a bank balance of ₹ 24,800. They also decided to readjust their capitals as per their new profit-sharing ratio.

Prepare necessary Ledger Accounts and Balance Sheet. (*ISC 2001, Modified*)

Solution:

In the Books of the Firm

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Furniture A/c		8,000	By Provision for Doubtful Debts A/c	500
To Outstanding Rent A/c		1,500	By Land and Building A/c	12,000
To Gain (Profit) on Revaluation transferred to:				
A's Capital A/c	1,000			
B's Capital A/c	1,000			
C's Capital A/c	1,000	3,000		
		12,500		12,500

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*A* ₹	*B* ₹	*C* ₹	Particulars	*A* ₹	*B* ₹	*C* ₹
To *B*'s Capital A/c	9,600	...	9,600	By Balance *b/d*	60,000	40,000	32,000
To Bank A/c	...	72,200	...	By General Reserve A/c	10,000	10,000	10,000
To Balance *c/d* (WN)	87,900	...	87,900	By Profit and Loss A/c	2,000	2,000	2,000
				By *A*'s Capital A/c	...	9,600	...
				By *C*'s Capital A/c	...	9,600	...
				By Revaluation A/c —Gain	1,000	1,000	1,000
				By Bank A/c (Bal. Fig.)	24,500	...	52,500
	97,500	72,200	97,500		97,500	72,200	97,500

Dr. BANK ACCOUNT Cr.

Date	Particulars	₹	Date	Particulars	₹
2017			2017		
April 1	To Balance *b/d*	20,000	April 1	By *B*'s Capital A/c	72,200
April 1	To *A*'s Capital A/c	24,500	April 1	By Balance *c/d*	24,800
April 1	To *C*'s Capital A/c	52,500			
		97,000			97,000

BALANCE SHEET OF *A* AND *C*
as at 1st April, 2018

Liabilities		₹	Assets		₹
Capital A/cs:			Land and Building		1,32,000
A	87,900		Furniture		20,000
C	87,900	1,75,800	Stock		20,000
Creditors		40,000	Debtors	45,000	
Bills Payable		20,000	*Less:* Provision for Doubtful Debts	4,500	40,500
Outstanding Rent		1,500	Bank		24,800
		2,37,300			2,37,300

Working Note:

Calculation of Capitals of A and C in the new firm:

(*i*) Amount payable to *B* = ₹ 72,200. Required Cash in Hand = ₹ 24,800. Cash already in Hand = ₹ 20,000. Thus, the amount to be brought in by *A* and *C* (shortage of cash) = ₹ 77,000 (*i.e.*, ₹ 72,200 + ₹ 24,800 – ₹ 20,000).

(*ii*) *Capitals of A and C before capital brought in:*

A—₹ (60,000 + 10,000 + 2,000 + 1,000 – 9,600) = ₹ 63,400

C—₹ (32,000 + 10,000 + 2,000 + 1,000 – 9,600) = ₹ 35,400

Total Capital of *A* and *C* is ₹ [63,400 + 35,400 + 77,000 (Shortage of cash)] = ₹ 1,75,800

Therefore, Capital of each partner is ½ of ₹ 1,75,800 = ₹ 87,900.

Illustration 3.

A, *B* and *C* are partners in a trading firm sharing profits in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March, 2018 stood as follows:

Liabilities		₹	Assets		₹
Sundry Creditors		12,500	Cash at Bank		1,500
General Reserve		18,000	Sundry Debtors	15,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	1,500	13,500
A	40,000		Stock		12,500
B	21,000		Investment		8,000
C	20,000	81,000	Office Equipments		14,000
			Furniture		12,000
			Building		50,000
		1,11,500			1,11,500

B retired on 1st April, 2018 subject to the following conditions:

(*i*) A typewriter purchased on 1st October, 2017 for ₹ 2,000 debited to Office Expenses Account is to be brought into account charging depreciation @ 10% p.a.

(*ii*) Building revalued at ₹ 75,000. Furniture is to written-down by ₹ 2,000 and stock is reduced to ₹ 10,000.

(*iii*) Provision for Doubtful Debts is to be calculated @ 5% on Sundry Debtors.

(*iv*) Goodwill of the firm is to be valued at ₹ 18,000.

(*v*) Market value of Investment is ₹ 7,500.

(*vi*) Amount due to *B* to be transferred to his Loan Account.

(*vii*) *A* and *C* will share profits and losses in the ratio of 2 : 1 and their capitals are to be adjusted in the profit-sharing ratio.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet immediately after *B*'s retirement.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Stock A/c		2,500	By Office Equipments A/c (WN 1)	1,900
To Furniture A/c		2,000	By Building A/c	25,000
To Investment A/c		500	By Provision for Doubtful Debts A/c	750
To Gain (Profit) transferred to:			(₹ 1,500 – 5% of ₹ 15,000)	
A's Capital A/c	11,325			
B's Capital A/c	7,550			
C's Capital A/c	3,775	22,650		
		27,650		27,650

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	A ₹	B ₹	C ₹	Particulars	A ₹	B ₹	C ₹
To *B*'s Capital A/c (WN 3)	3,000	...	3,000	By Balance *b/d*	40,000	21,000	20,000
To *B*'s Loan A/c	...	40,550	...	By General Reserve A/c	9,000	6,000	3,000
To Bank A/c (WN 2)	3,258	...	...	By *A*'s Capital A/c (WN 3)	...	3,000	...
To Balance *c/d* (WN 2)	54,067	...	27,033	By *C*'s Capital A/c (WN 3)	...	3,000	...
				By Revaluation A/c (Profit)	11,325	7,550	3,775
				By Bank A/c (WN 2)	...	...	3,258
	60,325	40,550	30,033		60,325	40,550	30,033

BALANCE SHEET *as at 1st April, 2018 (After B's Retirement)*

Liabilities		₹	Assets		₹
Sundry Creditors		12,500	Cash at Bank		1,500
Loan—*B*		40,550	Sundry Debtors	15,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	750	14,250
A	54,067		Stock		10,000
C	27,033	81,100	Investments		7,500
			Office Equipments (₹ 14,000 + ₹ 1,900)		15,900
			Furniture		10,000
			Building		75,000
		1,34,150			1,34,150

Working Notes:

1. The typewriter purchased was wrongly debited to Office Expense Account, but should have been debited to Office Equipments Account. In effect, depreciation for 6 months (from 1st October, 2017 and 31st March, 2018) has not been provided. Therefore, ₹ 2,000 – ₹ 100 (depreciation for 6 months) = ₹ 1,900 should be debited (added) to Office Equipments Account and also credited to Revaluation Account.
2. *Ascertainment of required Closing Capital:*

Adjusted capitals of *A* and *C* after *B*'s retirement are:	₹
A (₹ 40,000 + ₹ 9,000 + ₹ 11,325 – ₹ 3,000)	57,325
C (₹ 20,000 + ₹ 3,000 + ₹ 3,775 – ₹ 3,000)	23,775
Total capital of the new firm	81,100

Thus, ₹ 81,100 will be shared by *A* and *C* in their new ratio, *i.e.*, 2 : 1

A's New Capital = ₹ 54,067; and *C*'s New Capital = ₹ 27,033.

In effect, A will withdraw ₹ 3,258 (*i.e.*, ₹ 57,325 – ₹ 54,067) and *C* will bring ₹ 3,258 (*i.e.*, ₹ 27,033 – ₹ 23,775).

3. *Adjustment of Goodwill:*

(*i*) *Calculation of Gaining Ratio:*

Gain of a Partner = New Share – Old Share

$$A\text{'s Gain} = \frac{2}{3}-\frac{3}{6}=\frac{4-3}{6}=\frac{1}{6};\ C\text{'s Gain} = \frac{1}{3}-\frac{1}{6}=\frac{2-1}{6}=\frac{1}{6};$$

$$\text{Gaining Ratio of } A \text{ and } C = \frac{1}{6}:\frac{1}{6}=1:1.$$

(*ii*) Firm's Goodwill = ₹ 18,000

B's Share of Goodwill = ₹ 18,000 × 2/6 = ₹ 6,000, which is to be contributed by *A* and *C* in their gaining ratio, *i.e.*, 1 : 1.

Thus, *A*'s Contribution= ₹ 6,000 × 1/2 = ₹ 3,000; and *C*'s Contribution = ₹ 6,000 × 1/2 = ₹ 3,000.

Illustration 4.

Kushal, Kumar and Kavita were partners in a firm sharing profits in the ratio of 3 : 1 : 1. On 1st April, 2018, their Balance Sheet was as follows:

BALANCE SHEET OF KUSHAL, KUMAR AND KAVITA
as at 1st April, 2018

Liabilities		₹	Assets		₹
Creditors		1,20,000	Cash		70,000
Bills Payable		1,80,000	Debtors	2,00,000	
General Reserve		1,20,000	*Less:* Provision for doubtful debts	10,000	1,90,000
Capital A/cs:			Stock		2,20,000
Kushal	3,00,000		Furniture		1,20,000
Kumar	2,80,000		Building		3,00,000
Kavita	3,00,000	8,80,000	Land		4,00,000
		13,00,000			13,00,000

On the above date Kavita retired and the following was agreed:

(*i*) Goodwill of the firm was valued at ₹ 40,000.

(*ii*) Land was to be appreciated by 30% and building was to be depreciated by ₹ 1,00,000.

(*iii*) Value of furniture was to be reduced by ₹ 20,000.

(*iv*) Provision for Doubtful Debts is to be increased to ₹ 15,000.

(*v*) 10% of the amount payable to Kavita was paid in cash and the balance was transferred to her Loan Account.

(*vi*) It is decided by Kushal and Kumar that General Reserve is to appear in the books of the new firm at ₹ 80,000.

(*vii*) Capitals of Kushal and Kumar will be in proportion to their new profit-sharing ratio. The surplus/deficit, if any in their Capital Accounts will be adjusted through Current Accounts.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of Kushal and Kumar after Kavita's retirement.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Building A/c	1,00,000	By Land A/c		1,20,000
To Furniture A/c	20,000	By Loss transferred to:		
To Provision for Doubtful Debts A/c	5,000	Kushal's Capital A/c	3,000	
		Kumar's Capital A/c	1,000	
		Kavita's Capital A/c	1,000	5,000
	1,25,000			1,25,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	Kushal ₹	Kumar ₹	Kavita ₹	Particulars	Kushal ₹	Kumar ₹	Kavita ₹
To Revaluation A/c (Loss)	3,000	1,000	1,000	By Balance *b/d*	3,00,000	2,80,000	3,00,000
To Kavita's Capital A/c (Goodwill)	6,000	2,000	...	By General Reserve A/c*	12,000	4,000	24,000
To Cash A/c (10%)	...	...	33,100	By Kushal's Capital A/c (Goodwill)	...	...	6,000
To Kavita's Loan A/c (90%)	...	...	2,97,900	By Kumar's Capital A/c (Goodwill)	...	...	2,000
To Kumar's Current A/c (Bal. Fig.)	...	1,35,000	...	By Kushal's Current A/c (Bal. Fig.)	1,35,000	...	...
To Balance *c/d* (WN 1) (Adjusted Capital)	4,38,000	1,46,000	...				
	4,47,000	2,84,000	3,32,000		4,47,000	2,84,000	3,32,000

*Excess General Reserve = Existing General Reserve – Required in new firm = ₹ 1,20,000 – ₹ 80,000 = ₹ 40,000. Out of ₹ 40,000, Kavita's share in General Reserve ₹ 24,000 (*i.e.*, ₹ 1,20,000 × ₹ 1/5) is credited to her Capital Account, remaining ₹ 16,000 is distributed between Kushal and Kumar in the ratio of 3 : 1.

BALANCE SHEET OF THE RECONSTITUTED FIRM
as at 1st April, 2018

Liabilities		₹	Assets		₹
Creditors		1,20,000	Cash (WN 2)		36,900
Bills Payable		1,80,000	Debtors	2,00,000	
Kavita's Loan A/c		2,97,900	*Less:* Provision for Doubtful Debts	15,000	1,85,000
General Reserve		80,000	Stock		2,20,000
Capital A/cs:			Furniture		1,00,000
Kushal	4,38,000		Building		2,00,000
Kumar	1,46,000	5,84,000	Land		5,20,000
Kumar's Current A/c		1,35,000	Kushal's Current A/c		1,35,000
		13,96,900			13,96,900

Working Notes:

1. *Calculation of Adjusted Capital of Remaining Partners in the New Firm:*

	₹
Kushal's Capital before adjustment [₹ 3,00,000 + ₹ 12,000 – ₹ 3,000 – ₹ 6,000]	3,03,000
Kumar's Capital before adjustment [₹ 2,80,000 + ₹ 4,000 – ₹ 1,000 – ₹ 2,000]	2,81,000
Total Capital	5,84,000

Adjusted Capital of Kushal $= ₹ 5,84,000 \times \frac{3}{4} = ₹ 4,38,000;$

Adjusted Capital of Kumar $= ₹ 5,84,000 \times \frac{1}{4} = ₹ 1,46,000.$

2. Dr. CASH ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance *b/d*	70,000	By Kavita's Capital A/c	33,100
		By Balance *c/d*	36,900
	70,000		70,000

Illustration 5.

X, *Y* and *Z* were partners in a firm sharing profits in the ratio of 2 : 2 : 1. On 31st March, 2018, their Balance Sheet was as follows:

Liabilities		₹	Assets	₹
Creditors		60,000	Cash at Bank	90,000
Bills Payable		40,000	Stock	70,000
General Reserve		30,000	Debtors	40,000
Capital A/cs:			Land and Building	5,00,000
X	3,00,000		Profit and Loss A/c	1,60,000
Y	3,00,000		(Loss for the year ended 31st March, 2018)	
Z	1,30,000	7,30,000		
		8,60,000		8,60,000

Y died on 30th June, 2018. The Partnership Deed provided for the following on the death of a partner:

(*i*) Goodwill of the business was to be calculated on the basis of 2 times the average profits of the past 5 years. The profits for the years ended 31st March, 2017, 31st March, 2016, 31st March, 2015 and 31st March, 2014 were ₹ 50,000; ₹ 80,000; ₹ 1,10,000 and ₹ 2,20,000 respectively.

(*ii*) *Y*'s share of profit or loss from 1st April, 2018 till his death was to be calculated on the basis of the profit or loss for the year ended 31st March, 2018.

You are required to calculate the following:

(*a*) Goodwill of the firm and *Y*'s share of goodwill at the time of his death.

(*b*) *Y*'s share in the profit or loss of the firm till the date of his death.

(*c*) Prepare *Y*'s Capital Account at the time of his death to be presented to his executors.

Soltuion:

(*a*) Firm's Goodwill $= \dfrac{(₹\,50{,}000 + ₹\,80{,}000 + ₹\,1{,}10{,}000 + ₹\,2{,}20{,}000 - ₹\,1{,}60{,}000)}{5} \times 2$

= ₹ 1,20,000.

Y's Share of Goodwill = ₹ 1,20,000 × 2/5 = ₹ 48,000, which is contributed by *X* and *Z* in their Gaining Ratio of 2 : 1.

(*b*) *Y*'s Share in Loss = ₹ 1,60,000 × $\dfrac{3}{12} \times \dfrac{2}{5}$ = ₹ 16,000.

(*c*)

Dr. *Y*'S CAPITAL ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Profit and Loss A/c (₹ 1,60,000 × 2/5)	64,000	By Balance *b/d*	3,00,000
To Profit and Loss Suspense A/c	16,000	By General Reserve A/c (₹ 30,000 × 2/5)	12,000
To *Y*'s Executors' A/c	2,80,000	By *X*'s Capital A/c (Goodwill)	32,000
(Balancing Figure)		By *Z*'s Capital A/c (Goodwill)	16,000
	3,60,000		3,60,000

Illustration 6.

Albert, Boris and Cyril are partners sharing profits and losses in the ratio of 3 : 2 : 1 and their Balance Sheet as at 31st March, 2018 stood as under:

Liabilities	₹	Assets	₹
Albert's Capital	50,000	Building	70,000
Boris's Capital	50,000	Machinery	25,000
Cyril's Capital	50,000	Stock	32,000
Creditors	17,000	Debtors	15,000
		Bank	25,000
	1,67,000		1,67,000

Albert died on 1st July, 2018 and the following decisions were taken by the surviving partners. According to the Partnership Deed, his executors were entitled to:

(*i*) The deceased partner's capital as appearing in the last Balance Sheet and interest thereon @ 6% p.a. up to the date of death.

(*ii*) His share of profit for the period he was alive based on the figure of 31st March, 2018.

(*iii*) Goodwill according to his share of profit to be calculated by taking twice the amount of the average profit of the last three years. The profits of the previous years were:

31st March, 2018—₹ 11,000

31st March, 2017—₹ 15,000

31st March, 2016—₹ 10,000

(*iv*) Assets were to be revalued:

Building—₹ 80,000,

Stock—₹ 30,000,

Provision for Doubtful Debts @ 10%.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet as at 1st July, 2018.

(All calculations are to be made to the nearest rupee.) (*ISC 2000, Modified*)

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Stock A/c		2,000	By Building A/c	10,000
To Provision for Doubtful Debts A/c		1,500		
To Gain (Profit) transferred to Capital A/cs:				
Albert (3/6)	3,250			
Boris (2/6)	2,167			
Cyril (1/6)	1,083	6,500		
		10,000		10,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Albert ₹	Boris ₹	Cyril ₹	Particulars	Albert ₹	Boris ₹	Cyril ₹
To Albert's Capital A/c (Goodwill) (WN 3)	...	8,000	4,000	By Balance *b/d*	50,000	50,000	50,000
To Albert's Executors' A/c (Transfer)	67,375	...	...	By Profit and Loss Suspense A/c —Share of Profit (WN 2)	1,375	...	...
To Balance *c/d*	...	44,167	47,083	By Interest on Capital A/c (WN 1)	750	...	...
				By Boris's Capital A/c (WN 3)	8,000	...	...
				By Cyril's Capital A/c (WN 3)	4,000	...	...
				By Revaluation A/c —Gain	3,250	2,167	1,083
	67,375	52,167	51,083		67,375	52,167	51,083

BALANCE SHEET
as at 1st July, 2018

Liabilities		₹	Assets		₹
Capital A/cs:			Building		80,000
Boris	44,167		Machinery		25,000
Cyril	47,083	91,250	Stock		30,000
Albert's Executors' A/c		67,375	Debtors	15,000	
Creditors		17,000	*Less:* Provision for Doubtful Debts	1,500	13,500
			Bank		25,000
			Profit and Loss Suspense A/c*		2,125
		1,75,625			1,75,625

*Share of Profit + Interest on Capital = ₹ 1,375 + ₹ 750 = ₹ 2,125.

Working Notes:

1. Interest on Albert's Capital for 3 months up to date of his death: ₹ 50,000 × 6/100 × 3/12 = ₹ 750.
2. Albert's share of Profit up to the date of his death = ₹ 11,000 × 3/12 × 3/6 = ₹ 1,375.
3. Albert's Share of Goodwill:

   Average Profit of last 3 years = 1/3 × ₹ (11,000 + 15,000 + 10,000) = ₹ 12,000.

   Albert's Share of Average Profit = 3/6 × ₹ 12,000 = ₹ 6,000.

   Value of his Share of Goodwill = 2 × ₹ 6,000 = ₹ 12,000.

   Albert's Share of Goodwill credited to his Capital Account which is to be contributed by Boris and Cyril in their Gaining Ratio. (As the profit-sharing ratio of Boris and Cyril remains the same in the new firm, gaining ratio is the new ratio.)

Illustration 7.

Bina and Anita are partners.

Their partnership agreement provides for the following:

(*i*) Accounts are to be balanced on 31st December each year.

(*ii*) Profits are to be divided as follows:

Bina: one-half; Anita: one-third and carried to Reserve: one-sixth.

(*iii*) That in the event of death of a partner, her executors will be entitled to the following:

(*a*) Capital to her credit at the date of death.

(*b*) Proportionate profit to date of death based on the average profits of the last three completed years.

(*c*) Share of Goodwill based on three years' purchases of the average profits for the three preceding completed years.

Profits for the three years were: 2005—₹ 42,000; 2006—₹ 39,000 and 2007—₹ 45,000.

On 31st December, 2007, Anita's Capital stood at ₹ 60,000 and firm's General Reserve stood at ₹ 30,000. Anita expired on 1st May, 2008.

From the above, prepare Anita's Executors' Account as would appear in the firm's ledger transferring the amount to her Loan Account with proper working notes. (*ISC 2009*)

Solution:

Dr. ANITA'S EXECUTORS' ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Anita's Executors' Loan A/c	1,28,000	By Anita's Capital A/c	60,000
		By General Reserve A/c (₹ 30,000 × 2/5)	12,000
		By Bina's Capital A/c (Goodwill) (WN 2)	50,400
		By Profit and Loss Suspense A/c (WN 3)	5,600
	1,28,000		1,28,000

Working Notes:

1. Reserves, Goodwill and Share in Profit up to 1st May, 2008 will be shared in the ratio of 3 : 2.
2. Goodwill is valued as follows:

$$= \frac{(₹\,42,000 + ₹\,39,000 + ₹\,45,000)}{3} \times 3 = ₹\ 1,26,000$$

Anita's Share = ₹ 1,26,000 × 2/5 = ₹ 50,400.

3. Anita's Share in Profit up to 1st May, 2008:

		₹
(*i*)	Average Profit of last 3 years	42,000
(*ii*)	Profit for 4 months	14,000
(*iii*)	Anita's Share (2/5 of ₹ 14,000)	5,600

Illustration 8.

The Balance Sheet of *X*, *Y* and *Z* who are sharing profits in the ratio of 2 : 3 : 1, as at 31st March, 2018 is given below:

Liabilities	₹	Assets	₹
X's Capital A/c	2,00,000	Goodwill	24,000
Y's Capital A/c	4,00,000	Land and Building	5,00,000
Z's Capital A/c	6,00,000	Investments	1,00,000
Workmen Compensation Reserve	40,000	(Market Value ₹ 92,000)	
Investments Fluctuation Reserve	20,000	Stock	1,60,000
Provision for Doubtful Debts	20,000	Debtors	6,00,000
Creditors	7,20,000	Bank	5,92,000
		Advertisement Suspense A/c	24,000
	20,00,000		20,00,000

Z died on 30th September, 2018 and *X* and *Y* decided to share future profits and losses in the ratio of 3 : 2 and 50% of the amount payable to *Z* is to be paid immediately and the balance in two equal instalments together with interest @ 10% p.a.

Other Information:

(*i*) Goodwill is to be valued at 2 years' purchase of average profits of last three completed years. The profits were—2015–16 ₹ 90,000; 2016–17 ₹ 1,80,000; 2017–18 ₹ 2,70,000.

(*ii*) Land and Building was found undervalued by ₹ 1,70,000 and Stock was found overvalued by ₹ 16,000.

(*iii*) Provision for Doubtful Debts is to be made equal to 5% of the Debtors.

(*iv*) Claim on account of Workmen Compensation is ₹ 16,000.

(*v*) Profit for the current year is to be valued on the basis of last year's profit.

Prepare necessary Ledger Accounts and Balance Sheet of the new firm.

Solution:

Dr. REVALUATION ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Stock A/c	16,000	By Land and Building A/c	1,70,000
To Provision for Doubtful Debts A/c	10,000		
To Gain (Profit) on Revaluation transferred to:			
X's Capital A/c	48,000		
Y's Capital A/c	72,000		
Z's Capital A/c	24,000		
	1,70,000		1,70,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)	Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)
To Goodwill A/c	8,000	12,000	4,000	By Balance *b/d*	2,00,000	4,00,000	6,00,000
To *Y*'s Capital A/c	36,000	...	...	By *X*'s Capital A/c	...	36,000	60,000
To *Z*'s Capital A/c	60,000	...	...	By Revaluation A/c	48,000	72,000	24,000
To Adv. Susp. A/c	8,000	12,000	4,000	By Work. Com. Res. A/c	8,000	12,000	4,000
To *Z*'s Capital A/c	22,500	...	...	By Inv. Fluc. Res. A/c	4,000	6,000	2,000
To *Z*'s Executors' A/c	...	...	7,04,500	By *X*'s Capital A/c	...	...	22,500
To Balance *c/d*	1,25,500	5,02,000	...	(Share of Profit)			
	2,60,000	5,26,000	7,12,500		2,60,000	5,26,000	7,12,500

Dr. *Z*'S EXECUTOR'S ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Bank A/c	3,52,250	By *Z*'s Capital A/c	7,04,500
To Balance *c/d*	3,52,250		
	7,04,500		7,04,500

BALANCE SHEET *as at 30th September, 2018*

Liabilities	₹	Assets		₹
X's Capital A/c	1,25,500	Land and Building		6,70,000
Y's Capital A/c	5,02,000	Investments		92,000
Z's Executors' A/c	3,52,250	Stock		1,44,000
Creditors	7,20,000	Debtors	6,00,000	
Workmen Compensation Claim	16,000	*Less:* Provision for Doubtful Debts	30,000	5,70,000
		Bank ₹ (5,92,000 – 3,52,250)		2,39,750
	17,15,750			17,15,750

Working Notes:

1. *Calculation of Gain/(Sacrifice) of Share:*

	New Share	Old Share	Difference
X	3/5	2/6	3/5 – 2/6 = 8/30 (Gain)
Y	2/5	3/6	2/5 – 3/6 = – 3/30 (Sacrifice)

2. *Calculation of Goodwill:*

   (*i*) Average Profit $= \dfrac{₹\,90{,}000 + ₹\,1{,}80{,}000 + ₹\,2{,}70{,}000}{3} = ₹\,1{,}80{,}000$

   (*ii*) Firm's Goodwill = ₹ 1,80,000 × 2 = ₹ 3,60,000.

   Z's share in goodwill = ₹ 3,60,000 × 1/6 = ₹ 60,000. In this question *Y* is also sacrificing his 3/30 share of profit. He should also be compensated by ₹ 36,000 (*i.e.*, ₹ 3,60,000 × 3/30).

3. Excess Investments Fluctuation Reserve and Workmen Compensation Reserve have been transferred directly to Partners' Capital Accounts.

4. As per the terms, 50% of the amount payable to *Z* is to be paid immediately. Since, *Z* has died, 50% of the amount due to Z will be paid to his executors.

5. *Z*'s Share of Profit till the date of death = ₹ 2,70,000 × 6/12 × 1/6 = ₹ 22,500, it should be adjusted through *X*'s Capital Account (being a gaining partner).

Illustration 9.

A, *B* and *C* were partners sharing profits and losses in the ratio of 5 : 3 : 2. On 31st March, 2018, their Balance Sheet stood as under:

Liabilities		₹	Assets	₹
Sundry Creditors		1,55,000	Goodwill	25,000
Workmen Compensation Reserve		10,000	Leasehold	1,00,000
Reserve Fund		20,000	Patents	30,000
Capital A/cs:			Machinery	1,50,000
A	1,50,000		Stock	50,000
B	1,25,000		Debtors	1,40,000
C	75,000	3,50,000	Cash at Bank	40,000
		5,35,000		5,35,000

C died on 1st August, 2018. It was agreed that:

(*i*) Goodwill of the firm is to be valued at 2½ years' purchase of the average of annual profits of the last 4 years. The profits for the four preceding years were ₹ 65,000, ₹ 60,000, ₹ 80,000 and ₹ 75,000.

(*ii*) Machinery be valued at ₹ 1,40,000. Patents be valued at ₹ 40,000. Leasehold be valued at ₹ 1,25,000 on 1st August, 2018.

(*iii*) For the purpose of calculating *C*'s share in the profits of 2018–19, the profits in 2018–19 should be taken to have accrued on the same scale as in 2017–18.

(*iv*) A sum of ₹ 21,000 to be paid immediately to the executors of *C* and the balance to be paid in four equal half-yearly instalments together with interest @ 10% p.a.

Prepare *C*'s Capital Account and *C*'s Executors' Account for 2018–19.

Note: Firm closes its accounts on 31st March every year.

Solution:

Dr. *C'S* CAPITAL ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2018			2018		
Aug. 1	To Goodwill A/c	5,000	April 1	By Balance *b/d*	75,000
Aug. 1	To *C*'s Executors' A/c (Balancing Figure)	1,21,000	Aug. 1	By Revaluation A/c (Profit)	5,000
				By *A*'s Capital A/c (Goodwill) (WN 1)	21,875
				By *B*'s Capital A/c (Goodwill) (WN 1)	13,125
				By Profit and Loss Suspense A/c (WN 2)	5,000
				By Workmen Compensation Reserve A/c	2,000
				By Reserve Fund A/c	4,000
		1,26,000			1,26,000

Dr. *C'S* EXECUTORS' ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2018			2018		
Aug. 1	To Bank A/c	21,000	Aug. 1	By *C*'s Capital A/c	1,21,000
2019			2019		
Jan. 31	To Bank A/c (₹ 25,000 + ₹ 5,000)	30,000	Jan. 31	By Interest A/c (₹ 1,00,000 × 10/100 × 6/12)	5,000
Jan. 31	To Balance *c/d*	75,000			
		1,26,000			1,26,000
2019			2019		
March 31	To Balance *c/d*	76,250	Feb. 1	By Balance *b/d*	75,000
			March 31	By Interest A/c (₹ 75,000 × 10/100 × 2/12)	1,250
		76,250			76,250

Working Notes:

1. *Calculation of Goodwill:*

		₹
(*i*)	Total Profits for last 4 years (₹ 65,000 + ₹ 60,000 + ₹ 80,000 + ₹ 75,000)	2,80,000
(*ii*)	Average Profit (₹ 2,80,000/4)	70,000
(*iii*)	Goodwill (₹ 70,000 × 2½)	1,75,000
(*iv*)	*C*'s Share of Goodwill (₹ 1,75,000 × 2/10)	35,000

C's Share of Goodwill ₹ 35,000 will be adjusted between *A* and *B* in their Gaining Ratio, *i.e.*, 5 : 3.

2. *C*'s Share of Profit up to the date of death = ₹ 75,000 × 4/12 × 2/10 = ₹ 5,000.

Illustration 10.

On 1st April, 2016, *P* retired from active partnership and his share of the following was ascertained:

	₹
Goodwill	20,000
Interest on Capital	500
Salary	1,500
Drawings	20,000
Interest on Drawings	2,000
Share of Profit	25,000
Capital	75,000

The amount due to *P* was to be retained in the firm as a loan bearing interest @ 10% p.a. and was to be paid to *P* by annual instalments of ₹ 50,000 each, interest being calculated @ 10% p.a. on the unpaid balances. The first instalment was paid on 31st March, 2017.

You are required to prepare *P*'s Capital Account and also *P*'s Loan Account until the payment of the whole amount due to him was made.

Solution:

Dr. *P*'S CAPITAL ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Drawings A/c	20,000	By Balance *b/d*	75,000
To Interest on Drawings A/c	2,000	By Partners' Capital (Continuing) A/cs (Goodwill)	20,000
To *P*'s Loan A/c —Transfer	1,00,000	By Interest on Capital A/c	500
		By Partner's Salary A/c	1,500
		By Profit and Loss Appropriation A/c (Share of Profit)	25,000
	1,22,000		1,22,000

Dr. *P*'S LOAN ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2016 March 31	To Balance *c/d*	1,00,000	2016 March 31	By *P*'s Capital A/c	1,00,000
2017 March 31	To Bank A/c	50,000	2016 April 1	By Balance *b/d*	1,00,000
March 31	To Balance *c/d*	60,000	2017 March 31	By Interest A/c @ 10% p.a.	10,000
		1,10,000			1,10,000
2018 March 31	To Bank A/c	50,000	2017 April 1	By Balance *b/d*	60,000
March 31	To Balance *c/d*	16,000	2018 March 31	By Interest A/c @ 10% p.a.	6,000
		66,000			66,000
2019 March 31	To Bank A/c	17,600	2018 April 1	By Balance *b/d*	16,000
			2019 March 31	By Interest A/c @ 10% p.a.	1,600
		17,600			17,600

Illustration 11.

D, *R* and *L* were in partnership sharing profits and losses in the ratio of 3 : 2 : 1. The draft Balance Sheet as at 31st March, 2018 was as follows:

Liabilities		₹	Assets		₹
Capital A/cs:			Building		12,000
D	24,000		Plant and Equipment		18,800
R	12,000		Stock		9,200
L	6,000	42,000	Debtors	12,400	
Current A/cs:			*Less:* Provision for Doubtful Debts	1,200	11,200
D	1,920		Balance at Bank		16,120
R	1,680				
L	1,120	4,720			
Loan—*D*		5,000			
Creditors		15,600			
		67,320			67,320

D retired on 1st April, 2018 and *R* and *L* continued in partnership, sharing profits and losses in the ratio of 2 : 1. *D*'s loan was repaid on 1st April, 2018 and it was agreed that the remaining balance due to him, other than of the Current Account, shall remain as loan to the partnership.

For the purpose of *D*'s retirement, it was agreed that:

(*i*) Building be revalued at ₹ 24,000 and the Plant and Equipment at ₹ 15,800.

(*ii*) Provision for Doubtful Debts was to be increased by ₹ 400.

(*iii*) A creditor of ₹ 500 was not to be paid.

(*iv*) ₹ 1,200 was to be written off from stock for damaged items included therein.

(*v*) ₹ 4,240 payable as legal charges is to be accounted.

(*vi*) Goodwill of the firm to be valued at ₹ 14,400 and *D*'s share of the same be adjusted into the accounts of *R* and *L*.

You are required to prepare Revaluation Account, Capital and Current Accounts of the partners (assuming all adjustments are to be made through the Current Accounts) and the Balance Sheet of *R* and *L* as at 1st April, 2018.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Plant and Equipment A/c		3,000	By Building A/c	12,000
To Provision for Doubtful Debts A/c		400	By Creditors A/c	500
To Stock A/c		1,200		
To Outstanding Legal Charges A/c		4,240		
To Gain (Profit) on Revaluation trfd. to:				
D (3/6)	1,830			
R (2/6)	1,220			
L (1/6)	610	3,660		
		12,500		12,500

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*D* ₹	*R* ₹	*L* ₹	Particulars	*D* ₹	*R* ₹	*L* ₹
To *D*'s Loan A/c	24,000	...	...	By Balance *b/d*	24,000	12,000	6,000
To Balance *c/d*	...	12,000	6,000				
	24,000	12,000	6,000		24,000	12,000	6,000
				By Balance *b/d*	...	12,000	6,000

Dr. PARTNERS' CURRENT ACCOUNTS Cr.

Particulars	*D* ₹	*R* ₹	*L* ₹	Particulars	*D* ₹	*R* ₹	*L* ₹
To *D*'s Current A/c (Goodwill: WN 1 & 2)	...	4,800	2,400	By Balance *b/d*	1,920	1,680	1,120
				By Revaluation A/c	1,830	1,220	610
To Bank A/c	10,950	...	...	By *R*'s Current A/c	4,800	...	...
				By *L*'s Current A/c	2,400	...	...
				By Balance *c/d*	...	1,900	670
	10,950	4,800	2,400		10,950	4,800	2,400

BALANCE SHEET OF *R* AND *L as at 1st April, 2018*

Liabilities		₹	Assets		₹
Capital A/cs:			Building		24,000
R	12,000		Plant and Equipment		15,800
L	6,000	18,000	Stock		8,000
D's Loan		24,000	Debtors	12,400	
Creditors		15,100	*Less:* Provision for Doubtful Debts	1,600	10,800
Outstanding Legal Charges		4,240	Balance at Bank (WN 3)		170
			Current A/cs:		
			R	1,900	
			L	670	2,570
		61,340			61,340

Working Notes:

1. *Adjustment of Goodwill:*

   D's Share of Goodwill = ₹ 14,400 × 3/6 = ₹ 7,200.

   D's Share of Goodwill is to be adjusted against the Current Accounts of *R* and *L* in their Gaining Ratio of 2 : 1.
   R = ₹ 7,200 × 2/3 = ₹ 4,800; *L* = ₹ 7,200 × 1/3 = ₹ 2,400.

2. *Computation of Gaining Ratio:*

   Gain = New Share – Old Share

   $R = \frac{2}{3} - \frac{2}{6} = \frac{4-2}{6} = \frac{2}{6}$ (Gain); $L = \frac{1}{3} - \frac{1}{6} = \frac{2-1}{6} = \frac{1}{6}$ (Gain); Gaining Ratio = $\frac{2}{6} : \frac{1}{6}$ or 2 : 1.

3. Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance *b/d*	16,120	By *D*'s Loan A/c	5,000
		By *D*'s Current A/c	10,950
		By Balance *c/d*	170
	16,120		16,120

Illustration 12.

A, *B* and *C* are partners sharing profits in the ratio of 4 : 3 : 1. Their Balance Sheet as at 31st March, 2018 is given below:

Liabilities		₹	Assets		₹
Creditors		1,40,000	Cash in Hand		20,000
Bills Payable		30,000	Cash at Bank		1,50,000
Workmen Compensation Reserve		20,000	Stock		75,000
General Reserve		80,000	Debtors	1,30,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	5,000	1,25,000
A	2,00,000		Car		2,50,000
B	3,00,000		Plant and Machinery		1,20,000
C	2,00,000	7,00,000	Building		2,30,000
		9,70,000			9,70,000

On 1st April, 2018, *B* retired from the firm selling his share of profit to *A* for ₹ 36,000 and to *C* for ₹ 45,000. For the purpose of *B*'s retirement, it was agreed that:

(*i*) Stock is to be appreciated by 20% and Building by 10%.

(*ii*) Provision for Doubtful Debts is increased to 10%.

(*iii*) Claim on account of Workmen Compensation is ₹ 12,000.

(*iv*) Revaluation Expenses were ₹ 5,000 plus CGST and SGST @ 9% each and were paid.

(*v*) Car was valued at ₹ 3,05,000 and was given to *B* in part settlement of his dues. CGST and SGST were charged @ 9% each.

(*vi*) Amount due to *B* is to be settled on the following basis:
50% on retirement and the balance 50% within one year.

(*vii*) Capital of the newly constituted firm is fixed at ₹ 6,00,000 to be divided between *A* and *C* in new profit-sharing ratio. Adjustment is to be made in cash.

Calculate New Profit-sharing Ratio and prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the new firm.

Solution:

Calculation of New Profit-sharing Ratio:

B's share is 3/8 which he is surrendering in favour of *A* and *C* in the ratio of ₹ 36,000: ₹ 45,000 or 4 : 5.

Therefore *A* will get 4/9 of 3/8 = 1/6 and *C* will get 5/9 of 3/8 = 5/24.

Total share of *A* in the new firm will be: 4/8 + 1/6 = 16/24 or 2/3.

Total share of *C* in the new firm will be: 1/8 + 5/24 = 8/24 or 1/3.

New Profit-sharing Ratio of *A* and *C* = 2 : 1.

Dr. REVALUATION ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Provision for Doubtful Debts A/c		8,000	By Stock A/c	15,000
To Cash A/c		5,000	By Building A/c	23,000
(Revaluation Expenses)			By *B*'s Capital A/c	55,000
To Gain (Profit) transferred to:			(Gain on Car)	
A's Capital A/c	40,000			
B's Capital A/c	30,000			
C's Capital A/c	10,000	80,000		
		93,000		93,000

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	*A* (₹)	*B* (₹)	*C* (₹)	Particulars	*A* (₹)	*B* (₹)	*C* (₹)
To *B*'s Capital A/c (WN 1)	36,000	...	45,000	By Balance *b/d*	2,00,000	3,00,000	2,00,000
				By General Reserve A/c	40,000	30,000	10,000
To Car A/c	...	2,50,000	...	By *A*'s Capital A/c (WN 1)	...	36,000	...
To Revaluation A/c		55,000					
To Output CGST A/c		27,450		By *C*'s Capital A/c (WN 1)	...	45,000	...
To Output SGST A/c		27,450					
To Bank A/c	...	42,050*	...	By Revaluation A/c	40,000	30,000	10,000
To *B*'s Loan A/c	...	42,050*	...	By Workmen Compensation Reserve A/c	4,000	3,000	1,000
To Balance *c/d* (WN 2)	4,00,000	...	2,00,000	By Bank A/c (Bal. Fig.)	1,52,000	...	24,000
	4,36,000	4,44,000	2,45,000		4,36,000	4,44,000	2,45,000

*50% of ₹ 84,100, *i.e.*, Amount due to *B*.

BALANCE SHEET *as at 1st April, 2018* (After *B*'s Retirement)

Liabilities		₹	Assets		₹
Creditors		1,40,000	Cash in Hand		14,100
Bills Payable		30,000	Cash at Bank		2,83,950
Output CGST		27,450	Input CGST		450
Output SGST		27,450	Input SGST		450
Workmen Compensation Claim		12,000	Stock		90,000
B's Loan		42,050	Debtor	1,30,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	13,000	1,17,000
A	4,00,000		Plant and Machinery		1,20,000
C	2,00,000	6,00,000	Building		2,53,000
		8,78,950			8,78,950

Working Notes:

1. *B* sold his share to *A* and *C* in the ratio of 4 : 5. The consideration of ₹ 36,000 and ₹ 45,000 will be credited to *B*'s Capital Account and the respective amount will be debited to *A*'s and *C*'s Capital Accounts respectively.
2. Total Capital of the New Firm is ₹ 6,00,000. New Profit-sharing Ratio is 2 : 1.
   A's Share of Capital = ₹ 6,00,000 × 2/3 = ₹ 4,00,000
   C's Share of Capital = ₹ 6,00,000 × 1/3 = ₹ 2,00,000
   After all adjustments, *A*'s Capital will be ₹ (2,00,000 + 40,000 + 40,000 + 4,000 – 36,000) = ₹ 2,48,000. Therefore, *A* will bring in (₹ 4,00,000 – ₹ 2,48,000) = ₹ 1,52,000.
   After all adjustments, *C*'s Capital will be ₹ (2,00,000 + 10,000 + 10,000 + 1,000 – 45,000) = ₹ 1,76,000. Therefore, *C* will bring in (₹ 2,00,000 – ₹ 1,76,000) = ₹ 24,000.

3. *Journal entry for Car given to B will be:*

		₹	₹
B's Capital A/c	...Dr.	3,59,900	
To Car A/c			2,50,000
To Revaluation A/c			55,000
To Output CGST A/c			27,450
To Output SGST A/c			27,450
(Being Car given to *B* at ₹ 3,05,000 plus CGST and SGST)			

4. *Journal entry for Revaluation Expenses:*

		₹	₹
Revaluation A/c	...Dr.	5,000	
Input CGST A/c	...Dr.	450	
Input SGST A/c	...Dr.	450	
To Cash A/c			5,900
(Being Revaluation Expenses plus CGST an SGST paid)			

5. *Cash in Hand:*

	₹	₹
Opening Balance		20,000
Less: Revaluation Expenses	5,000	
Input CGST	450	
Input SGST	450	5,900
		14,100

6. *Cash at Bank:*

	₹
Opening Balance	1,50,000
Add: Amount Brought by:	
A	1,52,000
C	24,000
	3,26,000
Less: Paid to *B*	42,050
	2,83,950

Illustration 13.

X, *Y* and *Z* were partners in a partnership firm sharing profits in the ratio of 4 : 3 : 1. *Y* died on 30th June, 2015. The firm's profits for the past 5 years were:

Year	2010–11	2011–12	2012–13	2013–14	2014–15
Profit (₹)	8,22,225	7,00,000	2,50,000	*Loss:* (50,000)	5,00,000

X and *Z* decided to share future profits in the ratio of 3 : 1. Goodwill is to be valued on the basis of *Y*'s share of 2 year's profits calculated on the average of 5 completed years' profits immediately proceeding the year of death *less* 10%.

Solution:

$$X\text{'s Gain} = \frac{3}{4} - \frac{4}{8} = \frac{2}{8};$$

$$Z\text{'s Gain} = \frac{1}{4} - \frac{1}{8} = \frac{1}{8};$$

$$\text{Gaining Ratio of } X \text{ and } Z = \frac{2}{8} : \frac{1}{8} = 2:1.$$

Valuation of Goodwill:

$$\text{Average Profit} = \frac{₹\,8,22,225 + ₹\,7,00,000 + ₹\,2,50,000 - ₹\,50,000 + ₹\,5,00,000}{5} = ₹\,4,44,445$$

2 years' Average Profit = ₹ 4,44,445 × 2 = ₹ 8,88,890

Y's Share of 2 years' Average Profit = ₹ 8,88,890 × 3/8 = ₹ 3,33,334

Firm's Goodwill = ₹ 3,33,334 – 10% of ₹ 3,33,334 = ₹ 3,00,000

Y's Share of Goodwill = ₹ 3,00,000 × 3/8 = ₹ 1,12,500.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	X's Capital A/c	...Dr.		75,000	
	Z's Capital A/c	...Dr.		37,500	
	To *Y*'s Capital A/c				1,12,500
	(Being *Y*'s share of goodwill credited to *Y* and debited to *X* and *Z* in their gaining ratio)				

Illustration 14.

X, *Y* and *Z* were partners in a firm sharing profits in the ratio of 2 : 2 : 1. On 31st March, 2018, their Balance Sheet was as follows:

Liabilities	₹	Assets	₹
Creditors	60,000	Bank	90,000
Expenses Owing	2,500	Stock	70,000
Workmen Compensation Reserve	40,000	Debtors	40,000
General Reserve	27,500	Land and Building	5,00,000
Capital A/cs:		Profit and Loss A/c	1,60,000
X	3,00,000	(Loss for the year ended 31st March, 2018)	
Y	3,00,000		
Z	1,30,000		
	8,60,000		8,60,000

Y died on 30th June, 2018. Partnership Deed provided for the following on death of a partner:

(*i*) Goodwill of the firm was to be valued at 2 years' purchase of the average profit of last 5 years. The profits for the past four years were ₹ 50,000; ₹ 80,000; ₹ 1,10,000 and ₹ 2,20,000 respectively.

(*ii*) Share of profit or loss till the date of his death was to be calculated on the basis of the profit or loss for the year ended 31st March, 2018.

(*iii*) *X* and *Z* decide to record the effect of Workmen Compensation Reserve and General Reserve without affecting their book figures.

Prepare *Y*'s Capital Account at the time of his death to be presented to his executors.

Solution:

Dr. *Y*'S CAPITAL ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Profit and Loss A/c (₹ 1,60,000 × 2/5)	64,000	By Balance *b/d*	3,00,000
To Profit and Loss Suspense A/c (WN 2)	16,000	By *X*'s Capital A/c (Goodwill)	32,000
To *Y*'s Executors' A/c	2,95,000	By *Z*'s Capital A/c (Goodwill)	16,000
(Balancing Figure)		By *X*'s Capital A/c (WN 3)	18,000
		By *Z*'s Capital A/c (WN 3)	9,000
	3,75,000		3,75,000

Working Notes:

1. *Calculation of Y's Share of Goodwill:*

$$\text{Firm's Goodwill} = \frac{(₹\,50{,}000 + ₹\,80{,}000 + ₹\,1{,}10{,}000 + ₹\,2{,}20{,}000 - ₹\,1{,}60{,}000)}{5} \times 2 = ₹\ 1{,}20{,}000$$

   Y's Share of Goodwill = 1,20,000 × 2/5 = ₹ 48,000, which is contributed by *X* and *Z* in their gaining ratio of 2 : 1.

   Thus, *X*'s contribution = ₹ 48,000 × 2/3 = ₹ 32,000, and *Z*'s contribution = ₹ 4,80,000 × 1/3 = ₹ 16,000.

2. *Y*'s share in loss from the date of last Balance Sheet up to date of death = ₹ 1,60,000 × 2/5 × 3/12 = ₹ 16,000.
3. *Y*'s share in Workmen Compensation Reserve and General Reserve = 2/5 (₹ 40,000 + ₹ 27,500) = ₹ 27,000, which is contributed by *X* and *Z* in their gaining ratio of 2 : 1.
   X's contribution = ₹ 27,000 × 2/3 = ₹ 18,000; *Z*'s contribution = ₹ 27,000 × 1/3 = ₹ 9,000.

Illustration 15.

A, *B* and *C* are partners in a firm. Their Balance Sheet as at 31st March, 2017 is given below:

Liabilities	₹	Assets	₹
Creditors	10,000	Plant and Machinery	20,000
General Reserve	10,000	Furniture and Fixtures	2,500
A's Capital	20,000	Stock	10,500
B's Capital	15,000	Debtors	15,000
C's Capital	5,000	Investments	12,000
	60,000		60,000

B died on 30th September, 2017. The Partnership Deed provides that the representatives of the deceased partner shall be entitled to:

(*i*) Deceased Partner's Capital as appearing in last Balance Sheet.
(*ii*) Interest on Capital @ 6% p.a. up to the date of death.
(*iii*) His share of profit up to the date of death on the average of last three years' profit.
(*iv*) His share of any undistributed profits and losses as per last Balance Sheet.
(*v*) Interest on his Drawings up to the date of death will be charged @ 10% p.a.

Profits for the last three financial years were ₹ 65,000; ₹ 64,000 and ₹ 69,000. *B*'s drawings up to the date of death amounting to ₹ 10,000. Ascertain the amount payable to the legal representative of *B* (Goodwill excluded). (*ISC 1996, Modified*)

Solution: CALCULATION OF THE AMOUNT PAYABLE TO THE LEGAL REPRESENTATIVE OF *B*

Particulars		₹
Capital as per last Balance Sheet		15,000
Interest on Capital for 6 months @ 6% p.a.		450
Share of Profit for 6 months:		
Average Profit: 1/3 × ₹ (65,000 + 64,000 + 69,000) = ₹ 66,000		
Profit for 6 months: 1/2 × ₹ 66,000 = ₹ 33,000		
B's Share: 1/3 × ₹ 33,000		11,000
Share of General Reserve: 1/3 × ₹ 10,000		3,333
		29,783
Less: Drawings	10,000	
Interest on Drawings (₹ 10,000 × 10/100 × 3/12)	250	10,250
Total Amount Payable		19,533

Note: In the absence of actual dates of drawings, interest thereon has been calculated for the average period of 3 months on the assumption that the drawings were made evenly during the period of 6 months.

Master Questions and Advanced Level Questions

Illustration 16.

The Balance Sheet of Hari, Sonu and Zubin who were sharing profits in the ratio of 5 : 3 : 2 as at 31st March, 2019 is as below:

Liabilities		₹	Assets	₹
Creditors		50,000	Cash at Bank	40,000
Employees' Provident Fund		10,000	Sundry Debtors	1,00,000
Profit and Loss A/c		85,000	Stock	80,000
Workmen Compensation Reserve		10,000	Fixed Assets (Tangible)	60,000
Capital A/cs:			Goodwill	5,000
Hari	40,000		Advertisement Suspense A/c	5,000
Sonu	62,000			
Zubin	33,000	1,35,000		
		2,90,000		2,90,000

Hari retired on 31st March, 2019 and Sonu and Zubin decided to share profits in future in the ratio of 2 : 3 respectively.

The other terms on retirement were as follows:

(*i*) Goodwill of the firm is to be valued at ₹ 80,000.

(*ii*) Fixed Assets (Tangible) are to be depreciated to ₹ 57,500.

(*iii*) Make a Provision for Doubtful Debts at 5% on Debtors.

(*iv*) A liability for claim, included in Creditors for ₹ 10,000, is settled at ₹ 8,000.

The amount to be paid to Hari by Sonu and Zubin in such a way that their capitals are proportionate to their profit-sharing ratio and leave a balance of ₹ 15,000 in the Bank Account. Prepare Revaluation Account and Partners' Capital Accounts.

Solution:

Dr. REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Fixed Assets A/c	2,500	By Creditors A/c		2,000
To Provision for Doubtful Debts A/c	5,000	By Loss on Revaluation transferred to:		
		Hari's Capital A/c	2,750	
		Sonu's Capital A/c	1,650	
		Zubin's Capital A/c	1,100	5,500
	7,500			7,500

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Hari (₹)	Sonu (₹)	Zubin (₹)	Particulars	Hari (₹)	Sonu (₹)	Zubin (₹)
To Revaluation A/c (Loss)	2,750	1,650	1,100	By Balance *b/d*	40,000	62,000	33,000
To Hari's Capital A/c	...	8,000	32,000	By Workmen Compensation Reserve A/c	5,000	3,000	2,000
To Goodwill A/c	2,500	1,500	1,000	By Sonu's Capital A/c	8,000	...	...
To Advertisement Suspense A/c	2,500	1,500	1,000	By Zubin's Capital A/c	32,000	...	...
To Bank A/c	1,19,750	...	...	By Profit and Loss A/c	42,500	25,500	17,000
To Balance *c/d* (WN 3)	...	79,000	1,18,500	By Bank A/c (Balancing Figure)	...	1,150	1,01,600
	1,27,500	91,650	1,53,600		1,27,500	91,650	1,53,600

Working Notes:

1. **Gain/Sacrifice** = New Share – Old Share

   Sonu's Gain $= \frac{2}{5} - \frac{3}{10} = \frac{1}{10}$; Zubin's Gain $= \frac{3}{5} - \frac{2}{10} = \frac{4}{10}$

   Gaining Ratio = 1 : 4.

2. Hari's Share of Goodwill = ₹ 80,000 $\times \frac{5}{10}$ = ₹ 40,000 to be contributed by Sonu and Zubin in their gaining ratio.

3. **Total Capital of the New Firm** = Adjusted Capital of All Partners – Cash Available for Payment

   Hari's Adjusted Capital = ₹ 40,000 + ₹ 5,000 + ₹ 8,000 + ₹ 32,000 + ₹ 42,500 – ₹ 2,750 – ₹ 2,500 – ₹ 2,500 = ₹ 1,19,750.

   Sonu's Adjusted Capital = ₹ 62,000 + ₹ 3,000 + ₹ 25,500 – ₹ 1,650 – ₹ 1,500 – ₹ 1,500 – ₹ 8,000 = ₹ 77,850.

   Zubin's Adjusted Capital = ₹ 33,000 + ₹ 2,000 + ₹ 17,000 – ₹ 1,100 – ₹ 32,000 – ₹ 1,000 – ₹ 1,000 = ₹ 16,900.

   Cash Available for Payment = ₹ 40,000 – ₹ 8,000 – ₹ 15,000 = ₹ 17,000

   Total Capital of New Firm = ₹ 1,19,750 + ₹ 77,850 + ₹ 16,900 – ₹ 17,000 = ₹ 1,97,500

   Sonu's New Capital = ₹ 1,97,500 $\times \frac{2}{5}$ = ₹ 79,000

   Zubin's New Capital = ₹ 1,97,500 $\times \frac{3}{5}$ = ₹ 1,18,500.

4. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	40,000	By Creditors' A/c	8,000
To Sonu's Capital A/c	1,150	By Hari's Capital A/c	1,19,750
To Zubin's Capital A/c	1,01,600	By Balance *c/d*	15,000
	1,42,750		1,42,750

Illustration 17.

Micky, Ricky and Vicky were partners sharing profits and losses in the ratio of 5 : 3 : 2. On 31st March, 2019 their Balance Sheet was as follows:

Liabilities		₹	Assets		₹
Sundry Creditors		55,000	Goodwill		25,000
Investment Fluctuation Reserve		17,500	Patents		1,30,000
Workmen Compensation Reserve		17,500	Machinery		1,56,000
Capital A/cs:			Investments		15,000
Micky	3,37,500		Stock		50,000
Ricky	2,37,500		Sundry Debtors	62,000	
Vicky	1,85,000	7,60,000	*Less:* Provision for Doubtful Debts	2,000	60,000
			Loan to Vicky		5,000
			Cash at Bank		29,000
			Advertisement Expenditure		5,000
			Profit and Loss A/c (2018–19)		3,75,000
		8,50,000			8,50,000

Vicky died on 1st August, 2019. Vicky had withdrawn ₹ 25,000 during 2019–20. It was agreed between his executors and the remaining partners that—

(*i*) Goodwill be valued at 2½ years' purchase of average of four completed years' profits which were: 2015–16 ₹ 5,05,000; 2016–17 ₹ 70,000; 2017–18 ₹ 80,000.

(*ii*) Vicky's Share of profit from the closure of last accounting year till the date of death be calculated on the basis of the average of three completed years' profits before death.

(*iii*) Patents undervalued by ₹ 85,000; Machinery overvalued by ₹ 16,000.

(*iv*) Claim on account of Workmen Compensation is ₹ 10,000.

(*v*) Investments be sold for ₹ 21,000 and a sum of ₹ 24,000 be paid to Vicky's Executors immediately. The remainder to be paid in four equal half-yearly instalments together with interest @ 10% p.a.

You are required:

(*a*) to give necessary Journal entries to be passed on Vicky's death.

(*b*) to prepare the Capital Accounts of all the partners.

(*c*) to prepare the Balance Sheet of Micky and Ricky immediately after Vicky's death.

(*d*) to prepare Vicky's Executor's Account till it is finally settled.

Solution:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019					
Aug 1	Micky's Capital A/c	...Dr.		12,500	
	Ricky's Capital A/c	...Dr.		7,500	
	Vicky's Capital A/c	...Dr.		5,000	
	To Goodwill A/c				25,000
	(Being the existing goodwill written off)				
	Micky's Capital A/c (₹ 35,000 × 5/8)	...Dr.		21,875	
	Ricky's Capital A/c (₹ 35,000 × 3/8)	...Dr.		13,125	
	To Vicky's Capital A/c (₹ 1,75,000 × 2/10)				35,000
	(Being Vicky's share of goodwill adjusted)				
	Vicky's Capital A/c	...Dr.		5,000	
	To Profit and Loss Suspense A/c				5,000
	(Being Vicky's share of loss to date of death recorded)				
	Investment Fluctuation Reserve A/c	...Dr.		17,500	
	To Micky's Capital A/c				8,750
	To Ricky's Capital A/c				5,250
	To Vicky's Capital A/c				3,500
	(Being the transfer of Investment Fluctuation Reserve)				
	Workmen Compensation Reserve A/c	...Dr.		17,500	
	To Workmen Compensation Claim A/c				10,000
	To Micky's Capital A/c				3,750
	To Ricky's Capital A/c				2,250
	To Vicky's Capital A/c				1,500
	(Being the transfer of Workmen Compensation Reserve)				
	Micky's Capital A/c	...Dr.		2,500	
	Ricky's Capital A/c	...Dr.		1,500	
	Vicky's Capital A/c	...Dr.		1,000	
	To Advertisement Expenditure A/c				5,000
	(Being the transfer of Advertisement Expenditure)				

Micky's Capital A/c ...Dr. Ricky's Capital A/c ...Dr. Vicky's Capital A/c ...Dr. To Profit and Loss A/c (Being the transfer of Accumulated Loss)		1,87,500 1,12,500 75,000	 3,75,000
Revaluation A/c ...Dr. To Machinery A/c (Being the decrease in value of asset recorded)		16,000	 16,000
Patents A/c ...Dr. To Revaluation A/c (Being the increase in value of asset recorded)		85,000	 85,000
Bank A/c ...Dr. To Investment A/c To Revaluation A/c (Being the investment sold)		21,000	 15,000 6,000
Revaluation A/c ...Dr. To Micky's Capital A/c To Ricky's Capital A/c To Vicky's Capital A/c (Being the transfer of gain (profit) on revaluation)		75,000	 37,500 22,500 15,000
Vicky's Capital A/c ...Dr. To Loan to Vicky (Being the transfer of Loan to Vicky to his Capital Account)		5,000	 5,000
Vicky's Capital A/c ...Dr. To Vicky's Executor's A/c (Being the transfer of Vicky's Capital Account to his Executor's Account)		1,24,000	 1,24,000
Vicky's Executor's A/c ...Dr. To Bank A/c (Being the partial payment made to Vicky's Executor)		24,000	 24,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Micky ₹	Ricky ₹	Vicky ₹	Particulars	Micky ₹	Ricky ₹	Vicky ₹
To Bank A/c (Drawings)	...	...	25,000	By Balance *b/d*	3,37,500	2,37,500	1,85,000
To Goodwill A/c	12,500	7,500	5,000	By Revaluation A/c	37,500	22,500	15,000
To Profit and Loss A/c	1,87,500	1,12,500	75,000	By Micky's Capital A/c	...	...	21,875
To Vicky's Capital A/c	21,875	13,125	...	By Ricky's Capital A/c	...	...	13,125
To Profit and Loss Suspense A/c	...	...	5,000	By Investment Fluctuation Reserve A/c	8,750	5,250	3,500
To Loan to Vicky A/c	...	...	5,000	By Workmen Compensation Reserve A/c	3,750	2,250	1,500
To Advertisment Expenditure A/c	2,500	1,500	1,000				
To Vicky's Executor's A/c	...	...	1,24,000				
To Balance *c/d*	1,63,125	1,32,875	...				
	3,87,500	2,67,500	2,40,000		3,87,500	2,67,500	2,40,000

BALANCE SHEET OF MICKY AND RICKY
as at 1st August, 2019

Liabilities		₹	Assets		₹
Sundry Creditors		55,000	Patents		2,15,000
Vicky's Executor's A/c		1,00,000	Machinery		1,40,000
Profit and Loss Suspense A/c		5,000	Stock		50,000
Workmen Compensation Claim		10,000	Sundry Debtors	62,000	
Micky's Capital	1,63,125		*Less:* Provision for Doubtful Debts	2,000	60,000
Ricky's Capital	1,32,875	2,96,000	Cash at Bank		1,000
		4,66,000			4,66,000

Dr. VICKY'S EXECUTOR'S ACCOUNT *Cr.*

Date		Particulars	₹	Date		Particulars	₹
2019				2019			
Aug.	1	To Bank A/c	24,000	Aug.	1	By Vicky's Capital A/c	1,24,000
2020				2020			
Jan.	31	To Bank A/c (₹ 25,000 + ₹ 5,000)	30,000	Jan.	31	By Interest A/c (₹ 1,00,000 × 6/12 × 10/100)	5,000
Mar.	31	To Balance *c/d* (₹ 75,000 + ₹ 1,250)	76,250	Mar.	31	By Interest A/c (Accrued) (₹ 75,000 × 2/12 × 10/100)	1,250
			1,30,250				1,30,250
2020				2020			
July	31	To Bank A/c (₹ 25,000 + ₹ 1,250 + ₹ 2,500)	28,750	April	1	By Balance *b/d*	76,250
				July	31	By Interest A/c (₹ 75,000 × 4/12 × 10/100)	2,500
2021				2021			
Jan.	31	To Bank A/c (₹ 25,000 + ₹ 2,500)	27,500	Jan.	31	By Interest A/c (₹ 50,000 × 10/100 × 6/12)	2,500
Mar.	31	To Balance *c/d* (₹ 25,000 + ₹ 417)	25,417	Mar.	31	By Interest A/c (₹ 25,000 × 10/100 × 2/12)	417
			81,667				81,667
2021				2021			
July	31	To Bank A/c (₹ 25,000 + ₹ 417 + ₹ 833)	26,250	April	1	By Balance *b/d*	25,417
				July	31	By Interest A/c (₹ 25,000 × 10/100 × 4/12)	833
			26,250				26,250

Working Notes:

1. **Vicky's Share of Goodwill:**

$$\text{Firm's Goodwill} = \frac{₹\,5{,}05{,}000 + ₹\,70{,}000 + ₹\,90{,}000 - ₹\,3{,}75{,}000}{4} \times 2.5 = ₹\,1{,}75{,}000$$

$$\text{Vicky's Share of Goodwill} = ₹\,1{,}75{,}000 \times \frac{2}{10} = ₹\,35{,}000.$$

2. **Vicky's Share of Profit (Loss) till date of death:**

$$\text{Average Profit (Loss) of last three years} = \frac{₹\,70{,}000 + ₹\,80{,}000 - ₹\,3{,}75{,}000}{3} = ₹\,75{,}000 \text{ (Loss)}$$

$$\text{Vicky's Share of Loss} = ₹\,75{,}000 \times \frac{2}{10} \times \frac{4}{12} = ₹\,5{,}000.$$

3. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	29,000	By Vicky's Drawings A/c	25,000
To Investment A/c	21,000	By Vicky's Executor's A/c	24,000
		By Balance *c/d*	1,000
	50,000		50,000

Illustration 18.

Ansh, Vansh and Dev are in partnership sharing profits and losses in the ratio of 3 : 2 : 1.

BALANCE SHEET OF Ansh, Vansh AND Dev

as at 31st March, 2019

Liabilities		₹	Assets		₹
Capital A/cs:			Machinery at cost	50,000	
Ansh	80,000		*Less:* Provision for Depreciation	8,000	42,000
Vansh	60,000		Furniture		1,000
Dev	40,000	1,80,000	Sundry Debtors	80,000	
Reserve		24,000	*Less:* Provision for Doubtful Debts	3,000	77,000
Workmen Compensation Reserve		6,000	Stock		50,000
Sundry Creditors		60,000	Cash at Bank		1,00,000
		2,70,000			2,70,000

On 30th June, 2019, Vansh retired and Ansh and Dev continued in partnership, sharing profits and losses in the ratio of 3 : 2. It was agreed that the following adjustments were to be made in the Balance Sheet as at 30th June, 2019:

(*i*) Machinery was to be revalued at ₹ 45,000.

(*ii*) Stock was to be reduced by 2%.

(*iii*) Furniture was to be reduced to ₹ 600.

(*iv*) Provision for Doubtful Debts to be increased by ₹ 1,000.

(*v*) A Provision of ₹ 300 was to be created for Outstanding Expenses.

The partnership agreement provided that on the retirement of a partner, goodwill was to be valued at ₹ 24,000 and Vansh's share of the same was to be adjusted into the accounts of Ansh and Dev. The profits up to the date of retirement from the date of last Balance Sheet was estimated at ₹ 45,000. All the partners are to be credited with their respective share of profit earned till the date of retirement of Vansh.

Vansh was to be paid in full. Ansh and Dev were to bring sufficient amount so as to make their capitals in proportion to the new profit-sharing ratio, subject to the condition that a cash balance of ₹ 30,000 was to be maintained as working capital. Before making this adjustment the cash balance was ₹ 68,000 on 30th June, 2019.

Pass necessary Journal entries to give effect to the above arrangements and prepare Partners' Capital Accounts as on 30th June, 2019.

Solution:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019	Ansh's Capital A/c	...Dr.		2,400	
June 30	Dev's Capital A/c	...Dr.		5,600	
	To Vansh's Capital A/c				8,000
	(Being Vansh's share of goodwill adjusted in the Capital Accounts of Ansh and Dev in the gaining ratio of 3 : 7) (WN 1 and 2)				
	Revaluation A/c	...Dr.		2,700	
	To Stock A/c				1,000
	To Provision for Doubtful Debts A/c				1,000
	To Furniture A/c				400
	To Provision for Outstanding Expenses A/c				300
	(Being the decrease in assets and increase in liabilities)				
	Machinery A/c	...Dr.		3,000	
	To Revaluation A/c				3,000
	(Being the increase in the value of machinery)				
	Revaluation A/c	...Dr.		300	
	To Ansh's Capital A/c				150
	To Vansh's Capital A/c				100
	To Dev's Capital A/c				50
	(Being the gain (profit) on revaluation divided in the old ratio)				
	Reserve A/c	...Dr.		24,000	
	Workmen Compensation Reserve A/c	...Dr.		6,000	
	To Ansh's Capital A/c				15,000
	To Vansh's Capital A/c				10,000
	To Dev's Capital A/c				5,000
	(Being the transfer of free Reserves to the Partners' Capital Accounts in the old ratio)				
	Profit and Loss Suspense A/c	...Dr.		45,000	
	To Ansh's Capital A/c				22,500
	To Vansh's Capital A/c				15,000
	To Dev's Capital A/c				7,500
	(Being the estimated profit till the date of retirement transferred to the Capital Accounts in the old ratio)				
	Bank A/c	...Dr.		55,100	
	To Ansh's Capital A/c				15,130
	To Dev's Capital A/c				39,970
	(Being the cash brought in by Ansh and Dev as per agreement) (WN 3)				
	Vansh's Capital A/c	...Dr.		93,100	
	To Bank A/c				93,100
	(Being the payment made to Vansh on his retirement)				

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Ansh (₹)	Vansh (₹)	Dev (₹)	Particulars	Ansh (₹)	Vansh (₹)	Dev (₹)
To Vansh's Capital A/c (WN1) (Goodwill)	2,400	...	5,600	By Balance *b/d*	80,000	60,000	40,000
To Bank A/c (Balancing Figure)	...	93,100	...	By Ansh's Capital A/c (WN 1)	...	2,400	...
To Balance *c/d* (WN 3)	1,30,380	...	86,920	By Dev's Capital A/c (WN 1)	...	5,600	...
				By Revaluation A/c (Gain)	150	100	50
				By Reserve A/c	12,000	8,000	4,000
				By Workmen Compensation Reserve	3,000	2,000	1,000
				By Profit and Loss Suspense A/c	22,500	15,000	7,500
				By Bank A/c (Bal. Fig.)	15,130	...	39,970
	1,32,780	93,100	92,520		1,32,780	93,100	92,520

Working Notes:

1. *Adjustment of Goodwill:*

   Vansh's Share of Goodwill = ₹ 24,000 × 2/6 = ₹ 8,000, which is contributed by Ansh and Dev in their Gaining Ratio of 3 : 7.

   Ansh's contribution = ₹ 8,000 × 3/10 = ₹ **2,400**; Dev's contribution = ₹ 8,000 × 7/10 = ₹ **5,600**.

2. *Computation of Gaining Ratio (Gain = New Share – Old Share):*

   Ansh's Gain = 3/5 – 3/6 = 3/30; Dev's Gain = 2/5 – 1/6 = 7/30

   Gaining Ratio = 3/30 : 7/30 or **3 : 7**.

3. *Cash to be brought in by* Ansh *and* Dev:

	₹
Amount payable to Vansh	93,100
Add: Amount to be retained as Working Capital	30,000
	1,23,100
Less: Cash already available	68,000
Cash to be brought in by Ansh and Dev	55,100

Adjusted Old Capital of Ansh = ₹ (80,000 + 150 + 12,000 + 3,000 + 22,500 – 2,400) = ₹ 1,15,250.

Adjusted Old Capital of Dev = ₹ (40,000 + 50 + 4,000 + 1,000 + 7,500 – 5,600) = ₹ 46,950.

Total Capital of the New Firm = ₹ 55,100 + ₹ 1,15,250 + ₹ 46,950 = ₹ 2,17,300.

Ansh's Capital in New Firm = ₹ 2,17,300 × 3/5 = ₹ 1,30,380;

Dev's Capital in New Firm = ₹ 2,17,300 × 2/5 = ₹ 86,920.

Illustration 19.

Khanna, Seth and Mehta were partners sharing profits and losses in the ratio of 5 : 3 : 2. On 31st March, 2018 their Balance Sheet was as follows:

Liabilities		₹	Assets		₹
Trade Creditors		1,35,000	Goodwill		25,000
Employees' Provident Fund		20,000	Patents		1,30,000
Investment Fluctuation Reserve		17,500	Machinery		1,56,000
Workmen Compensation Reserve		17,500	Investments		15,000
Capital A/cs:			Stock		50,000
Khanna	3,37,500		Sundry Debtors	62,000	
Seth	2,37,500		*Less:* Provision for Doubtful Debts	2,000	60,000
Mehta	1,85,000	7,60,000	Loan to Mehta		5,000
			Cash at Bank		1,29,000
			Advertisement Expenditure		5,000
			Profit and Loss A/c (2017–18)		3,75,000
		9,50,000			9,50,000

Mehta died on 1st August, 2018. Mehta had withdrawn ₹ 25,000 during 2018–19. It was agreed between his executors and the remaining partners that:

(*i*) Goodwill be valued at 2½ years' purchase of average of four completed years' profits which were: 2014–15 ₹ 5,05,000; 2015–16 ₹ 60,000; 2016–17 ₹ 90,000.

(*ii*) Mehta's Share of profit from the closure of last accounting year till the date of death be calculated on the basis of the average of three completed years' profits before death.

(*iii*) Patents undervalued by ₹ 70,000; Stock overvalued by ₹ 20,000.

(*iv*) Machinery were to be valued at ₹ 1,75,000.

(*v*) Provision of ₹ 5,000 be made in respect of Outstanding Legal charges.

(*vi*) Out of the amount of Insurance Premium which was debited entirely to Profit and Loss Account, ₹ 5,000 be carried forward as an unexpired Insurance.

(*vii*) Included in Trade Creditors was an item of ₹ 1,100 which was not to be paid, therefore, had to be written back.

(*viii*) Provision for Doubtful Debts is to be maintained at 5% of Sundry Debtors.

(*ix*) Claim on account of Workmen Compensation is ₹ 10,000.

(*x*) Investments be sold for ₹ 21,000 and a sum of ₹ 24,000 be paid to Mehta's Executor immediately. The remainder to be paid in four equal half-yearly instalments together with interest @ 10% p.a.

You are required:

(*a*) to give necessary Journal entries to be passed on Mehta's death;

(*b*) to prepare the Capital Accounts of all the partners;

(*c*) to prepare the Balance Sheet of Khanna and Seth immediately after Mehta's death;

(*d*) to prepare Mehta's Executor's Account till it is finally settled.

Solution:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018					
Aug. 1	Khanna's Capital A/c	...Dr.		12,500	
	Seth's Capital A/c	...Dr.		7,500	
	Mehta's Capital A/c	...Dr.		5,000	
	To Goodwill A/c				25,000
	(Being the existing goodwill written off)				
	Khanna's Capital A/c (₹ 35,000 × 5/8)	...Dr.		21,875	
	Seth's Capital A/c (₹ 35,000 × 3/8)	...Dr.		13,125	
	To Mehta's Capital A/c (₹ 1,75,000 × 2/10)				35,000
	(Being the Mehta's share of goodwill adjusted)				
	Mehta's Capital A/c	...Dr.		5,000	
	To Profit and Loss Suspense A/c				5,000
	(Being the Mehta's share of loss to date of death recorded)				
	Investment Fluctuation Reserve A/c	...Dr.		17,500	
	To Khanna's Capital A/c				8,750
	To Seth's Capital A/c				5,250
	To Mehta's Capital A/c				3,500
	(Being the transfer of Investment Fluctuation Reserve)				
	Workmen Compensation Reserve A/c	...Dr.		17,500	
	To Workmen Compensation Claim A/c				10,000
	To Khanna's Capital A/c				3,750
	To Seth's Capital A/c				2,250
	To Mehta's Capital A/c				1,500
	(Being the transfer of Workmen Compensation Reserve)				
	Khanna's Capital A/c	...Dr.		2,500	
	Seth's Capital A/c	...Dr.		1,500	
	Mehta's Capital A/c	...Dr.		1,000	
	To Advertisement Expenditure A/c				5,000
	(Being the transfer of Advertisement Expenditure)				
	Khanna's Capital A/c	...Dr.		1,87,500	
	Seth's Capital A/c	...Dr.		1,12,500	
	Mehta's Capital A/c	...Dr.		75,000	
	To Profit and Loss A/c				3,75,000
	(Being the transfer of Accumulated Loss)				

Bank A/c ...Dr.		21,000	
To Investment A/c			15,000
To Revaluation A/c			6,000
(Being the investment sold)			
Patents A/c ...Dr.		70,000	
Machinery A/c ...Dr.		19,000	
Unexpired Insurance A/c ...Dr.		5,000	
Trade Creditors A/c ...Dr.		1,100	
To Revaluation A/c			95,100
(Being the increase in assets and decrease in liabilities recorded)			
Revaluation A/c ...Dr.		26,100	
To Stock A/c			20,000
To Provision for Outstanding Legal Charges A/c			5,000
To Provision for Doubtful Debts A/c			1,100
(Being the decrease in assets and increase in liabilities recorded)			
Revaluation A/c ...Dr.		75,000	
To Khanna's Capital A/c			37,500
To Seth's Capital A/c			22,500
To Mehta's Capital A/c			15,000
(Being the transfer of gain (profit) on revaluation)			
Mehta's Capital A/c ...Dr.		5,000	
To Loan to Mehta A/c			5,000
(Being the transfer of Loan to Mehta to his Capital Account)			
Mehta's Capital A/c ...Dr.		1,24,000	
To Mehta's Executor's A/c			1,24,000
(Being the transfer of Mehta's Capital Account to his Executor's Account)			
Mehta's Executor's A/c ...Dr.		24,000	
To Bank A/c			24,000
(Being the partial payment made to Mehta's Executor)			

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Khanna ₹	Seth ₹	Mehta ₹	Particulars	Khanna ₹	Seth ₹	Mehta ₹
To Bank A/c (Drawings)	...	...	25,000	By Balance *b/d*	3,37,500	2,37,500	1,85,000
To Goodwill A/c	12,500	7,500	5,000	By Revaluation A/c	37,500	22,500	15,000
To Profit and Loss A/c	1,87,500	1,12,500	75,000	By Khanna's Capital A/c	...	...	21,875
To Mehta's Capital A/c	21,875	13,125	...	By Seth's Capital A/c	...	...	13,125
To Profit and Loss Suspense A/c	...	...	5,000	By Investment Fluctuation Reserve A/c	8,750	5,250	3,500
To Loan to Mehta A/c	...	...	5,000	By Workmen Compensation Reserve A/c	3,750	2,250	1,500
To Advertisment Expenditure A/c	2,500	1,500	1,000				
To Mehta's Executor's A/c	...	...	1,24,000				
To Balance *c/d*	1,63,125	1,32,875	...				
	3,87,500	2,67,500	2,40,000		3,87,500	2,67,500	2,40,000

BALANCE SHEET OF KHANNA AND SETH *as at 1st August, 2018*

Liabilities		₹	Assets		₹
Trade Creditors		1,33,900	Unexpired Insurance		5,000
Mehta's Executor's A/c		1,00,000	Patents		2,00,000
Profit and Loss Suspense A/c		5,000	Machinery		1,75,000
Employees' Provident Fund		20,000	Stock		30,000
Provision for Outstanding Legal Charges		5,000	Sundry Debtors	62,000	
Workmen Compensation Claim		10,000	*Less:* Provision for Doubtful Debts	3,100	58,900
Khanna's Capital	1,63,125		Cash at Bank		1,01,000
Seth's Capital	1,32,875	2,96,000			
		5,69,900			5,69,900

Dr. MEHTA'S EXECUTOR'S ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2018			2018		
Aug. 1	To Bank A/c	24,000	Aug. 1	By Mehta's Capital A/c	1,24,000
2019			2019		
Jan. 31	To Bank A/c (₹ 25,000 + ₹ 5,000)	30,000	Jan. 31	By Interest A/c (₹ 1,00,000 × 6/12 × 10/100)	5,000
Mar. 31	To Balance *c/d* (₹ 75,000 + ₹ 1,250)	76,250	Mar. 31	By Interest A/c (Accrued) (₹ 75,000 × 2/12 × 10/100)	1,250
		1,30,250			1,30,250
2019			2019		
July 31	To Bank A/c (₹ 25,000 + ₹ 1,250 + ₹ 2,500)	28,750	April 1	By Balance *b/d*	76,250
			July 31	By Interest A/c (₹ 75,000 × 4/12 × 10/100)	2,500
2020			2020		
Jan. 31	To Bank A/c (₹ 25,000 + ₹ 2,500)	27,500	Jan. 31	By Interest A/c (₹ 50,000 × 10/100 × 6/12)	2,500
Mar. 31	To Balance *c/d* (₹ 25,000 + ₹ 417)	25,417	Mar. 31	By Interest A/c (₹ 25,000 × 10/100 × 2/12)	417
		81,667			81,667
2020			2020		
July 31	To Bank A/c (₹ 25,000 + ₹ 417 + ₹ 833)	26,250	April 1	By Balance *b/d*	25,417
			July 31	By Interest A/c (₹ 25,000 × 10/100 × 4/12)	833
		26,250			26,250

Working Notes:

1. *Mehta's Share of Goodwill:*

$$\text{Firm's Goodwill} = \frac{₹\,5{,}05{,}000 + ₹\,70{,}000 + ₹\,90{,}000 - ₹\,3{,}75{,}000}{4} \times 2.5 = ₹\,1{,}75{,}000$$

$$\text{Mehta's Share of Goodwill} = ₹\,1{,}75{,}000 \times \frac{2}{10} = ₹\,35{,}000.$$

2. *Mehta's Share of Profit (Loss) till date of death:*

$$\text{Average Profit (Loss) of last three years} = \frac{₹\,70,000 + ₹\,80,000 - ₹\,3,75,000}{3} = ₹\,75,000 \text{ (Loss)}$$

$$\text{Mehta's Share of Loss} = ₹\,75,000 \times \frac{2}{10} \times \frac{4}{12} = ₹\,5,000.$$

3. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,29,000	By Mehta's Drawings A/c	25,000
To Investment A/c	21,000	By Mehta's Executor's A/c	24,000
		By Balance *c/d*	1,01,000
	1,50,000		1,50,000

Unsolved Questions

1. *A, B* and *C* are partners in a firm sharing profits and losses in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March, 2018 is as under:

Liabilities		₹	Assets		₹
Creditors		30,000	Cash in Hand		18,000
Bills Payable		16,000	Debtors	25,000	
General Reserve		12,000	*Less:* Provision for Doubtful Debts	3,000	22,000
Capital A/cs:			Stock		18,000
A	40,000		Furniture		30,000
B	40,000		Machinery		70,000
C	30,000	1,10,000	Goodwill		10,000
		1,68,000			1,68,000

B retires on 1st April, 2018 on the following terms:

(*i*) Provision for Doubtful Debts be raised by ₹ 1,000.

(*ii*) Stock to be depreciated by 10% and Furniture by 5%.

(*iii*) There is an outstanding claim of damages of ₹ 1,100 and it is to be provided for.

(*iv*) Creditors will be written back by ₹ 6,000.

(*v*) Goodwill of the firm is valued at ₹ 22,000.

(*vi*) *B* is paid in full with the cash brought in by *A* and *C* in such a manner that their capitals are in proportion to their profit-sharing ratio and Cash in Hand remains at ₹ 10,000.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of *A* and *C*.

2. Balance Sheet of *X*, *Y* and *Z* who were sharing profits in the ratio of 4 : 3 : 2 stood as follows as at 31st March, 2018:

Liabilities		₹	Assets		₹
Sundry Creditors		82,800	Cash at Bank		66,000
Capital A/cs:			Sundry Debtors	60,900	
X	2,40,000		*Less:* Provision for Doubtful Debts	2,100	58,800
Y	1,80,000		Stock		96,000
Z	1,20,000	5,40,000	Plant and Machinery		1,02,000
			Land and Building		3,00,000
		6,22,800			6,22,800

Y having given notice to retire from the firm, the following adjustments in the books of the firm were agreed upon:

(*i*) That Land and Building be appreciated by 10%.

(*ii*) Provision for Doubtful Debts is no longer necessary.

(*iii*) Stock be appreciated by 20%.

(*iv*) Adjustment be made in the accounts to rectify a mistake previously made whereby *Y* was credited in excess by ₹ 16,200 while *X* and *Z* were debited in excess by ₹ 8,400 and by ₹ 7,800 respectively.

(*v*) Goodwill of the firm be fixed at ₹ 1,08,000 and *Y's* share of the same be adjusted to the Capital Accounts of *X* and *Z* who are going to share future profits in the ratio of 2 : 1.

(*vi*) The entire capital of the firm, as newly constituted, will be readjusted by bringing in or paying cash so that the future capitals of *X* and *Z* be in the ratio of 2 : 1.

Prepare Revaluation Account, Capital Accounts of Partners, and Balance Sheet of the new firm showing *Y's* balance as loan.

[**Hint:** For Rectification: Dr. *Y's* Capital A/c—₹ 16,200 and Cr. *X's* Capital A/c—₹ 8,400 and *Z's* Capital A/c—₹ 7,800.]

3. *P*, *Q* and *R* were partners sharing profits and losses in the ratio of 4 : 3 : 3. The Balance Sheet of the firm as at 31st March, 2015 stood as follows:

Liabilities		₹	Assets	₹
Creditors		10,000	Cash and Bank	20,000
Capital A/cs: *P*	30,000		Debtors	15,000
Q	15,000		Stock	17,000
R	15,000	60,000	Fixed Assets	52,000
Employees' Provident Fund		20,000	Drawings: *R*	6,000
Reserves		10,000		
Workmen Compensation Reserve		10,000		
		1,10,000		1,10,000

R retired on the above date and following terms and conditions were agreed upon:

(*i*) Fixed Assets are to be depreciated by ₹ 2,000 and Provision for Doubtful Debts is to be created ₹ 1,000.

(*ii*) A Liability of ₹ 4,000 for Workmen Compensation is to be created.

(*iii*) Goodwill of the firm is valued at ₹ 50,000.

(*iv*) New profit-sharing ratio of *P* and *Q* is 2 : 1.

(*v*) Final balance payable to *R* is to be treated as loan carrying interest @10% p.a.

(*vi*) Final balance of *R* is to be settled in three equal annual instalments *plus* interest and the first instalment is payable on 31st March, 2016.

Pass Journal entries relating to *R's* retirement. Also, show Balance Sheet of *P* and *Q* as at 1st April, 2015 and *R's* Loan Account for 2015–16, 2016–17 and 2017–18.

4. Manoj, Naveen and Deepak were partners sharing profits in the ratio of 3 : 2 : 1. On 1st April, 2017, Naveen retired. On that date Balance Sheet was as follows:

Liabilities			₹	Assets	₹
General Reserve			6,000	Plant	30,000
Expenses Owing			2,000	Patents	3,000
Bills Payable			5,000	Debtors	9,500
Creditors			10,000	Stock	11,000
Capital A/cs:	Manoj	12,000		Cash	500
	Naveen	10,000			
	Deepak	9,000	31,000		
			54,000		54,000

The terms were:

(*i*) Goodwill of the firm be valued at ₹ 12,000 and Naveen's share of goodwill be adjusted in the accounts of Manoj and Deepak who will share the future profits and losses in the ratio of 3 : 2.

(*ii*) Expenses owing are to be brought down to ₹ 1,500; Plant is to be valued at 10% less and Patents at ₹ 4,000.

(*iii*) The total capital of the new firm will be fixed at ₹ 25,000 to be contributed by partners in the profit-sharing ratio.

Prepare necessary Ledger Accounts to record the above and prepare Balance Sheet after Naveen's retirement.

5. Following is the Balance Sheet of *A*, *B* and *C* as at 31st March, 2018, who have agreed to share profits and losses in proportion of their capitals:

Liabilities		₹	Assets		₹
Sundry Creditors		2,00,000	Cash at Bank		4,10,000
Employees' Provident Fund		1,40,000	Closing Stock		4,00,000
Profit and Loss A/c		1,00,000	Sundry Debtors	4,40,000	
General Reserve		80,000	*Less:* Provision for Doubtful Debts	40,000	4,00,000
Investment Fluctuation Reserve		60,000	Land and Building		8,00,000
Workmen Compensation Reserve		60,000	Machinery		12,00,000
Capital A/cs:			Investment (Market Value ₹ 2,70,000)		2,00,000
A	8,00,000		Advertisement Expenditure		30,000
B	12,00,000				
C	8,00,000	28,00,000			
		34,40,000			34,40,000

On 1st April, 2018, *A* retired from the firm and remaining partners decided to carry on the business. It was agreed to revalue the assets and reassess the liabilities on that date, on the following basis:

(*i*) Land and Building to be appreciated by 30%.

(*ii*) Machinery be brought down by 30%.

(*iii*) There were Bad Debts of ₹ 60,000.

(*iv*) The claim on account of Workmen Compensation Reserve was determined at ₹ 32,000.

(*v*) Goodwill of the firm was valued at ₹ 5,60,000 and *A*'s share of Goodwill was adjusted against the Capital Accounts of the continuing partners *B* and *C* who have decided to share future profits in the ratio of 3 : 4 respectively.

(*vi*) Continuing partners decided to record the effect of reserves (after adjusting claim on account of Workmen Compensation Reserve) and accumulated profits/losses without effecting their book values.

(*vii*) Capital of the new firm in total will be the same as before the retirement of *A* and will be in the new profit-sharing ratio of the continuing partners.

(*viii*) Amount due to *A* be settled by paying ₹ 2,00,000 immediately and balance by transferring to her Loan Account which will be paid later.

Prepare Revaluation Account, Capital Accounts of Partners and Balance Sheet of the firm after Kusum's retirement.

6. The Balance Sheet *A*, *B* and *C* who were sharing profits in the ratio of 3 : 1 : 2 respectively stood as follows on 31st March, 2017:

Liabilities		₹	Assets		₹
Bills Payable		1,20,000	Cash		70,000
Sundry Creditors		1,80,000	Stock		2,20,000
General Reserve		1,80,000	Sundry Debtors	2,00,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	10,000	1,90,000
A	3,00,000		Building		4,00,000
B	3,00,000		Machinery		3,00,000
C	2,80,000	8,80,000	Furniture		1,20,000
			Advertisement Suspense A/c		60,000
		13,60,000			13,60,000

On 1st April, 2017, *C* retires from the firm and the partners agree to the following terms:

(*i*) Building and Stock are to be appreciated by 20% and 15% respectively.

(*ii*) Machinery and Furniture are to be reduced by 10% and 7% respectively.

(*iii*) Provision for Doubtful Debts to be increased to ₹ 15,000.

(*iv*) A computer previously written off is sold for ₹ 5,000 *plus* CGST and SGST @ 9% each.

(*v*) A provision of ₹ 5,000 be made in respect of outstanding legal charges.

(*vi*) Goodwill of the firm is valued at ₹ 2,10,000.

(*vii*) The continuing partners have decided to adjust their capitals in their New Profit-sharing Ratio after retirement of *C*. Surplus/deficit, if any, in their Capital Accounts will be adjusted through Current Accounts.

Prepare necessary Ledger Accounts and the Balance Sheet of the reconstituted firm.

7. *X*, *Y* and *Z* are in partnership sharing profits equally. *X* dies on 30th June, 2017 and the Partnership Deed provided *inter alia* that:

(*i*) The share of deceased partner's Capital Account shall be taken at the balance of the Capital Accounts as on the date of the last financial year, *less* the withdrawals, if any, made to the date of death.

(*ii*) His share of profit to the date of death be calculated on the basis of the average profits of the three preceding years.

(*iii*) Goodwill of the firm shall be taken at one year's purchase of the average profits of the preceding five years.

(*iv*) The firm's Freehold property shall be taken at an independent valuation.

The firm's Balance Sheet as at 31st March, 2017 was as under:

Liabilities		₹	Assets	₹
Capital A/cs:			Goodwill	56,700
X	90,000		Freehold Property	1,20,000
Y	60,000		Stock	45,000
Z	60,000	2,10,000	Debtors	30,000
Creditors		56,700	Bank	13,500
			Cash	1,500
		2,66,700		2,66,700

Freehold property was valued at ₹ 1,74,000.

The profits for five years ended 31st March were:

2012–13—₹ 34,500; 2013–14—₹ 42,000; 2014–15—₹ 27,000; 2015–16—₹ 24,000 and 2016–17—₹ 30,000.

Prepare *X*'s Capital Account.

GUIDE TO ANSWERS

1. Gain (Profit) on Revaluation—₹ 600; Existing Goodwill written off: Dr. *A*—₹ 5,000; *B*—₹ 3,333 and *C*—₹ 1,667 in Old Ratio of 3 : 2 : 1; Cr. Goodwill—₹ 10,000; Gaining Ratio 3 : 1. For Goodwill: Dr. *A*—₹ 5,500 and *C*—₹ 1,833; Cr. *B*—₹ 7,333; Balance of Capital A/cs after adjustments: *A*—₹ 35,800; *B*—₹ 48,200 and *C*—₹ 28,600; Capitals Rearranged: *A*—₹ 78,450 and *C*—₹ 26,150; Cash brought in by *A*—₹ 42,650 and cash withdrawn by *C*—₹ 2,450; Cash Balance—₹ 10,000 (₹ 18,000 + ₹ 42,650 – ₹ 2,450 – ₹ 48,200); Balance Sheet Total—₹ 1,45,700.
2. Gain Profit) on Revaluation—₹ 51,300; *Y*'s Loan A/c—₹ 2,16,900; Cash brought in by *X*—₹ 2,400 and Cash withdrawn by *Z*—₹ 2,400. New Capitals: *X*—₹ 2,49,600; *Z*—₹ 1,24,800. Balance Sheet Total—₹ 6,74,100.
3. Loss on Revaluation—₹ 3,000; *R*'s loan—₹ 27,900; *P*'s Capital—₹ 21,867; *Q*'s Capital—₹ 17,233; Balance Sheet Total as at 1st April, 2015—₹ 1,01,000.
4. Loss on Revaluation—₹ 1,500; Naveen's Loan—₹ 15,500; Capitals: Manoj—₹ 15,000; Deepak—₹ 10,000; Cash—₹ 1,950 paid by Manoj and ₹ 3,050 by Deepak; Cash Balance—₹ 5,500; Balance Sheet Total—₹ 57,000.
5. Loss on Revaluation—₹ 70,000; Capital Account Balances: *B*—₹ 12,00,000; *C*—₹ 16,00,000; *A*'s Loan A/c—₹ 8,08,000; Balance Sheet Total—₹ 42,48,000.
6. Gain on Revaluation—₹ 69,600; *C*'s Loan—₹ 4,13,200; Capital Account Balances: *A*—₹ 4,92,300; *B*—₹ 1,64,100; Balance Sheet Total—₹ 15,25,500.
7. Transfer to *X*'s Executor's Account—₹ 1,01,850.

CHAPTER 5

Dissolution of a Partnership Firm

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Dissolution of Partnership

It implies change in relationship of partners of the firm but the firm continues its business. In other words, there is dissolution of partnership whenever a partnership is reconstituted, *viz.*, admission, retirement, death or insolvency of a partner.

2. Dissolution of Firm

Dissolution of partnership among all the partners of a firm is called **dissolution of the firm**. In such a case the business of the firm also comes to an end.

3. Firm's Debts

Firm's Debts means the debts owed by the firm to outsiders.

4. Private Debts

Private Debts means debts owed by a partner to any other person.

5. Realisation Account

It records the realisation of assets and payments of liabilities. It is prepared to determine gain (profit)/loss on realisation of assets and settlement of liabilities.

6. Unrecorded Asset

Any asset which is not recorded in the books of the firm, is called **unrecorded asset**.

7. Unrecorded Liability

Any liability which is not recorded in the books of the firm is known as **unrecorded liability**.

SUMMARY OF THE CHAPTER

- **Dissolution of partnership between/among all the partners of a firm is called Dissolution of the Firm:** In case of dissolution of a firm, the business of the firm is closed, the assets are realised and the liabilities are paid.
- **Dissolution of partnership refers to the change in the existing relations of the partners:** The firm continues its business. It may take place on admission/retirement/death/insolvency of a partner or change in the profit-sharing ratio.

Settlement of Accounts (Section 48)

- **Treatment of Losses:** Losses including deficiencies of capital are to be paid in the following order:
  (*i*) First out of profits of the firm;
  (*ii*) Then out of capitals of the partners; and
  (*iii*) Lastly by partners individually in their profit-sharing ratio. [Section 48 (a)]

- **Application of Assets:** The assets of the firm, including any sum contributed by the partners to make up the deficiencies of capital will be applied in the following manner and order:
  (*i*) in paying firm's debts to the third parties.
  (*ii*) in paying to each partner rateably what is due to him on account of loans and advances;
  (*iii*) in paying to each partner rateably what is due to him on account of capital;
  (*iv*) the surplus, if any, shall be distributed between/among the partners in their profit-sharing ratio. [Section 48(b)]

Treatment of Firm's Debts and Private Debts (Section 49)

1. *Application of Firm's Property:* Firm's property is applied first towards the payment of firm's debts; then the surplus, if any, is applied towards the payment of partner's loan to the firm and balance towards his capital.
2. *Application of Partner's Private Property:* Partner's private property is applied first in payment of his private debts and the surplus, if any, in payment of firm's debts if the firm's liabilities exceed the firm's assets.

- **Closing of Firm's Books:** Firm's books are closed by preparing the following accounts:
  (*i*) Realisation Account; (*ii*) Partners' Loan Accounts;
  (*iii*) Partners' Capital Accounts; and (*iv*) Bank or Cash Account.
- **Realisation Account:** It is a nominal account and is prepared on the dissolution of a firm. The object of this account is to show the gain (profit) or loss on the realisation of assets and payment of liabilities.
- If Fixed Capital Account Method is followed, balance in Current Accounts is transferred to Capital Accounts of the Partners and adjustments are passed through the Capital Accounts. No adjustments are required to be passed through Current Account.
- Bank Overdraft is not to be transferred to Realisation Account.
- Bank Loan is to be transferred to Realisation Account.
- Partner's Loan Account (taken from a partner) is to be passed through Cash or Bank Account.
- Loan given to a partner is transferred (debited) to his Capital Account.

Accounting Entries Relating to Dissolution

The following entries are passed at the time of the dissolution of the firm:

Transfer of assets (except cash and bank balance)	Realisation A/c ...Dr. To Sundry Assets A/c	At book value
Transfer of liabilities (except partners' loans, capitals and undistributed profits)	Sundry Liabilities A/c ...Dr. To Realisation A/c	At book value
Sale of assets	Cash/Bank A/c ...Dr. To Realisation A/c	At realised value
Assets taken over by partner	Partner's Capital A/c ...Dr. To Realisation A/c	At agreed value
Payment of liabilities	Realisation A/c ...Dr. To Cash/Bank A/c	Amount of payment
Any liability taken over by the partner	Realisation A/c ...Dr. To Partner's Capital A/c	At agreed value
Payment of realisation expenses	Realisation A/c ...Dr. To Cash/Bank A/c	Amount of payment
Sale of unrecorded assets	Cash/Bank A/c ...Dr. To Realisation A/c	Amount received on sale

Payment of an unrecorded liability (which does not exist in the Balance Sheet)	Realisation A/c ...Dr. To Cash/Bank A/c	Paid amount
Payment of realisation expenses by any partner	Realisation A/c ...Dr. To Partner's Capital A/c	Amount of payment
Credit balance of Realisation Account (Gain or Profit)	Realisation A/c ...Dr. To Partners' Capital A/cs	In profit-sharing ratio
Debit balance of Realisation Account (Loss)	Partners' Capital A/cs ...Dr. To Realisation A/c	In profit-sharing ratio

Notes:

1. When an asset or liability is taken to the Realisation Account any related fund or reserve is also transferred to Realisation Account and not to Partners' Capital Accounts.
2. If the question is silent about the realisation of an asset, its value is assumed to be nil.
3. If the question is silent about the payment of a liability, then it has to be paid out in full.
4. Bank overdraft is taken to the Bank/Cash A/c and not transferred to Realisation Account but bank loan is transferred to Realisation Account.
5. Loan taken from a partner is passed through Cash or Bank Account.
6. Loan given to a partner is transferred (debited) to his Capital Account.

Solved Questions

Illustration 1.

Following was the Balance Sheet of Fox and Wolf as at 31st March, 2018, when they decided to dissolve the firm:

Liabilities		₹	Assets	₹
Creditors		88,500	Cash at Bank	4,500
Ms. Wolf's Loan		40,000	Stock	18,000
Bills Payable		23,000	Debtors	42,000
Capital A/cs:			Furniture	12,000
Fox	30,000		Machinery	1,06,500
Wolf	24,000	54,000	Profit and Loss A/c	22,500
		2,05,500		2,05,500

The assets realised: Stock—₹ 10,500; Debtors—₹ 27,750; Machinery—₹ 88,500. Furniture was taken by Fox at ₹ 7,500. Bills Payable were paid in full, while Creditors were settled at 2% discount. Ms. Wolf accepted ₹ 38,500 in full settlement of her Loan Account. There was a claim for damages against the firm for ₹ 4,000 which was settled at ₹ 2,000.

One customer, whose account was written off as bad, now paid ₹ 1,800, which is not included in ₹ 27,750 given above. Actual Realisation Expenses amounted to ₹ 2,100.

Prepare Realisation Account, Partners' Capital Accounts and Bank Account to close the books of the firm. (*ISC 1995, Modified*)

Solution:

In the Books of Fox and Wolf

Dr. REALISATION ACCOUNT *Cr.*

Particulars		₹	Particulars		₹
To Sundry Assets (Transfer):			By Sundry Liabilities (Transfer):		
Stock A/c	18,000		Creditors A/c	88,500	
Debtors A/c	42,000		Bills Payable A/c	23,000	
Furniture A/c	12,000		Ms. Wolf's Loan A/c	40,000	1,51,500
Machinery A/c	1,06,500	1,78,500	By Bank A/c (Assets Realised):		
To Bank A/c (Liabilities Paid):			Stock	10,500	
Bills Payable	23,000		Debtors	27,750	
Creditors	86,730		Machinery	88,500	1,26,750
Ms. Wolf's Loan	38,500		By Fox's Capital A/c (Furniture Taken Over)		7,500
Claim for Damages	2,000	1,50,230	By Bank A/c (Recovery of Bad Debts)		1,800
To Bank A/c (Expenses)		2,100	By Loss on Realisation:		
			Fox's Capital A/c	21,640	
			Wolf's Capital A/c	21,640	43,280
		3,30,830			3,30,830

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Fox (₹)	Wolf (₹)	Particulars	Fox (₹)	Wolf (₹)
To Profit and Loss A/c	11,250	11,250	By Balance *b/d*	30,000	24,000
To Realisation A/c (Furniture Taken Over)	7,500	...	By Bank A/c (Balancing Figure)	10,390	8,890
To Realisation A/c (Loss)	21,640	21,640			
	40,390	32,890		40,390	32,890

Dr. BANK ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Balance *b/d*		4,500	By Realisation A/c (Liabilities Paid)	1,50,230
To Realisation A/c:			By Realisation A/c (Expenses)	2,100
Assets Realised	1,26,750			
Recovery of Bad Debts	1,800	1,28,550		
To Fox's Capital A/c (Cash Brought in)		10,390		
To Wolf's Capital A/c (Cash Brought in)		8,890		
		1,52,330		1,52,330

Notes: 1. Profit-sharing ratio is not given. Therefore, profits/losses shall be shared equally.

2. Claim for damages was ₹ 4,000 but it was settled for ₹ 2,000. Therefore, payment of ₹ 2,000 shall be debited to Realisation Account.

Illustration 2.

X, Y and *Z* are sharing profits as 2 : 3 : 5 and their Balance Sheet as at 31st March, 2018 is as follows:

BALANCE SHEET *as at 31st March, 2018*

Liabilities		₹	Assets	₹
Capital A/cs:			Building	10,00,000
X	3,50,000		Equipments	2,00,000
Y	4,50,000		Stock	8,00,000
Z	5,50,000	13,50,000	Sundry Debtors	6,00,000
Sundry Creditors		3,00,000	Cash at Bank	3,00,000
Bank Loan		6,00,000		
X's Loan		6,50,000		
		29,00,000		29,00,000

The firm was dissolved on the above date. Close the books of the firm on the basis of the following information:

(*i*) An unrecorded asset was realised at ₹ 75,000.

(*ii*) A debt of ₹ 2,50,000 previously written off as bad was received.

(*iii*) Sundry Creditors took a computer included in Equipments, in part payments of ₹ 2,00,000. They were paid the balance at 10% discount. The remaining Equipments were sold for ₹ 30,000.

(*iv*) Building realised ₹ 9,75,000 and Sundry Debtors realised ₹ 5,50,000.

(*v*) Bank Loan was settled by handing over the entire Stock to them along with a payment of ₹ 50,000 by cheque.

(*vi*) *Y* was to get a remuneration of ₹ 60,000 for completing the dissolution process and he had to bear Realisation Expenses which amounted to ₹ 56,000 paid by the firm.

Solution:

Dr. REALISATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Building A/c	10,00,000	By Sundry Creditors A/c		3,00,000
To Equipments A/c	2,00,000	By Bank Loan A/c (Note)		6,00,000
To Stock A/c	8,00,000	By Bank A/c (Assets Realised):		
To Sundry Debtors A/c	6,00,000	Unrecorded Asset	75,000	
To Bank A/c (Bank Loan)	50,000	Bad Debts Recovered	2,50,000	
To Bank A/c (Sundry Creditors Paid) (₹ 1,00,000 – ₹ 10,000)	90,000	Building	9,75,000	
		Sundry Debtors	5,50,000	
To *Y*'s Capital A/c (Remuneration)	60,000	Equipments	30,000	18,80,000
		By Loss transferred to:		
		X's Capital A/c	4,000	
		Y's Capital A/c	6,000	
		Z's Capital A/c	10,000	20,000
	28,00,000			28,00,000

Dr. *X*'s LOAN ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Bank A/c (Repayment of Loan)	6,50,000	By Balance *b/d*	6,50,000
	6,50,000		6,50,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)	Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)
To Realisation A/c (Loss)	4,000	6,000	10,000	By Balance *b/d*	3,50,000	4,50,000	5,50,000
To Bank A/c (Expenses)	...	56,000	...	By Realisation A/c	...	60,000	...
To Bank A/c (Final Payment)	3,46,000	4,48,000	5,40,000				
	3,50,000	5,10,000	5,50,000		3,50,000	5,10,000	5,50,000

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	3,00,000	By Realisation A/c (Bank Loan)	50,000
To Realisation A/c (Assets Realised)	18,80,000	By Realisation A/c (Sundry Creditors Paid)	90,000
		By *Y*'s Capital A/c (Expenses)	56,000
		By *X*'s Loan A/c (Repayment)	6,50,000
		By *X*'s Capital A/c (Final Payment)	3,46,000
		By *Y*'s Capital A/c (Final Payment)	4,48,000
		By *Z*'s Capital A/c (Final Payment)	5,40,000
	21,80,000		21,80,000

Note: Bank overdraft is not transferred to Realisation Account whereas bank loan is transferred to Realisation Account.

Illustration 3.

X, *Y* and *Z* were the partners in a firm sharing profits in the ratio of 2 : 2 : 1. The firm was dissolved on 31st March, 2018. After transfer of assets and external liabilities to Realisation Account the following transactions took place:

(*i*) *R*, a Creditor, to whom ₹ 60,000 were due to be paid, accepted Office Furniture at ₹ 40,000 and the balance was paid to him in cash.

(*ii*) *S*, a Creditor, to whom ₹ 1,60,000 were due to be paid, took over Machinery at ₹ 2,00,000. Balance was paid by him in cash.

(*iii*) *T*, an Unrecorded Creditor of ₹ 90,000 was paid by *X* at a discount of 10%.

(*iv*) An Unrecorded Computer of ₹ 20,000 was taken over by *Y* at a discount of 10%.

(*v*) Workmen Compensation Reserve ₹ 30,000; Workmen Compensation paid ₹ 15,000.

(*vi*) Prepaid Insurance of ₹ 10,000 and Goodwill of ₹ 50,000 were also appearing in the Balance Sheet but no other additional information was given related to these two items.

Pass necessary Journal entries for the above transactions in the books of the firm.

Solution: JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
(*i*)	Realisation A/c ...Dr.		20,000	
	To Bank A/c			20,000
	(Being the balance cash paid to the creditor)			
(*ii*)	Bank A/c ...Dr.		40,000	
	To Realisation A/c			40,000
	(Being the net proceeds received from the creditor who took over machinery at ₹ 2,00,000)			
(*iii*)	Realisation A/c ...Dr.		81,000	
	To *X*'s Capital A/c			81,000
	(Being an unrecorded liability taken over by *X* at a discount of 10%)			
(*iv*)	*Y*'s Capital A/c ...Dr.		18,000	
	To Realisation A/c			18,000
	(Being an unrecorded computer taken over by *Y* at a discount of 10%)			

(*v*)	(*a*) Realisation A/c ...Dr.		15,000	
	To Bank A/c			15,000
	(Being the liability discharged)			
	(*b*) Workmen Compensation Reserve A/c ...Dr.		15,000	
	To *X*'s Capital A/c			6,000
	To *Y*'s Capital A/c			6,000
	To *Z*'s Capital A/c			3,000
	(Being the transfer of excess workmen compensation reserve)			
(*vi*)	No Journal entry is required since there is no realisation.			

Illustration 4.

X, *Y* and *Z* commenced business on 1st April, 2015 with capitals of ₹ 5,00,000; ₹ 4,00,000 and ₹ 3,00,000 respectively. Profits and losses were shared in the ratio of 4 : 3 : 3. Capitals carried interest at 5% p.a. During 2015–16 and 2016–17 they made profits of ₹ 2,00,000 and ₹ 2,50,000 (before allowing interest on capital). Drawings of each partner were ₹ 50,000 per year. After completion of the venture for which the firm was constituted, it was dissolved on 31st March, 2017. Creditors on that date were ₹ 1,20,000. The assets realised ₹ 13,00,000 net.

Give necessary accounts to close the books of the firm.

Solution:

In this problem, Balance Sheet on the date of dissolution is not given. Further, partners' capitals and book value of assets on the date of dissolution are also not given. Hence, first of all balances of partners' capitals will be ascertained. After that, Balance Sheet on the date of dissolution, *i.e.*, 31st March, 2017, shall be prepared to ascertain the value of assets.

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Date	Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)	Date	Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)
2016 March 31	To Bank A/c (Drawings)	50,000	50,000	50,000	2015 April 1	By Bank A/c	5,00,000	4,00,000	3,00,000
	To Balance *c/d*	5,31,000	4,12,000	3,07,000	2016 March 31	By Interest on Capital A/c	25,000	20,000	15,000
						By Profit and Loss App. A/c (Net Profit) (₹ 2,00,000 – ₹ 60,000)	56,000	42,000	42,000
		5,81,000	4,62,000	3,57,000			5,81,000	4,62,000	3,57,000
2017 March 31	To Bank A/c (Drawings)	50,000	50,000	50,000	2016 April 1	By Balance *b/d*	5,31,000	4,12,000	3,07,000
	To Balance *c/d*	5,82,550	4,38,850	3,28,600	2017 March 31	By Interest on Capital A/c	26,550	20,600	15,350
						By Profit and Loss App. A/c (Net Profit) (₹ 2,50,000 – ₹ 62,500)	75,000	56,250	56,250
		6,32,550	4,88,850	3,78,600			6,32,550	4,88,850	3,78,600

MEMORANDUM BALANCE SHEET
as at 31st March, 2017

Liabilities		₹	Assets	₹
Creditors		1,20,000	Sundry Assets	14,70,000
Capital A/cs: *X*	5,82,550		(Balancing Figure)	
Y	4,38,850			
Z	3,28,600	13,50,000		
		14,70,000		14,70,000

Dr. REALISATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Sundry Assets A/c	14,70,000	By Creditors A/c		1,20,000
To Bank A/c	1,20,000	By Bank A/c		13,00,000
		By Loss transferred to:		
		X's Capital A/c	68,000	
		Y's Capital A/c	51,000	
		Z's Capital A/c	51,000	1,70,000
	15,90,000			15,90,000

Dr. PARTNERS' CAPITAL ACCOUNTS (AFTER REALISATION) *Cr.*

Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)	Particulars	*X* (₹)	*Y* (₹)	*Z* (₹)
To Realisation A/c (Loss)	68,000	51,000	51,000	By Balance *b/d*	5,82,550	4,38,850	3,28,600
To Bank A/c (Balancing Figure)	5,14,550	3,87,850	2,77,600				
	5,82,550	4,38,850	3,28,600		5,82,550	4,38,850	3,28,600

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Realisation A/c	13,00,000	By Realisation A/c	1,20,000
		By *X*'s Capital A/c (Final Payment)	5,14,550
		By *Y*'s Capital A/c (Final Payment)	3,87,850
		By *Z*'s Capital A/c (Final Payment)	2,77,600
	13,00,000		13,00,000

Illustration 5 (*Considering GST*).

Kumar, Sham and Ram were partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. Due to a difference of opinion, they decided to dissolve the firm with effect from 1st April, 2018 on which date its Balance Sheet was as under:

BALANCE SHEET *as at 1st April, 2018*

Liabilities		₹	Assets	₹
Capital A/cs:			Plant and Machinery	80,000
Kumar	60,000		Furniture	45,000
Sham	40,000		Car	25,000
Ram	30,000	1,30,000	Stock-in-Trade	30,000
Current A/cs:			Sundry Debtors	71,000
Kumar	8,000		Cash at Bank	14,000
Sham	10,000	18,000	Current A/c:	
Sundry Creditors		1,20,000	Ram	3,000
		2,68,000		2,68,000

The following information is given:

(*i*) Plant and Machinery of book value ₹ 40,000 were taken by Kumar at an agreed value of ₹ 45,000 and the remaining Machinery realised ₹ 50,000.

(*ii*) Furniture realised ₹ 40,000.

(*iii*) Car was taken by Sham for ₹ 30,000.

(*iv*) Sundry Debtors included a Bad Debt for ₹ 1,200 and the rest were realised at a cash discount of 10%.

(*v*) Stock worth ₹ 5,000 was taken by Ram for ₹ 5,200 and the rest realised at 20% above their book value.

(*vi*) A Creditor for ₹ 2,000 was untraceable and other creditors accepted payment allowing 15% discount.

(*vii*) Realisation Expenses paid to an agency carrying out dissolution amounted to ₹ 5,000.

(*viii*) Sale of Plant and Machinery, Furniture, Car, Stock and Realisation Expenses are subject to levy of CGST and SGST @ 9% each.

You are required to pass the Journal entries, prepare Realisation Account, CGST and SGST Accounts, Bank Account, and Partners' Capital Accounts showing final payments to them.

Solution:

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
(*i*)	Realisation A/c ...Dr.		2,51,000	
	To Plant and Machinery A/c			80,000
	To Furniture A/c			45,000
	To Car A/c			25,000
	To Stock-in-Trade A/c			30,000
	To Sundry Debtors A/c			71,000
	(Being the assets transferred)			
(*ii*)	Sundry Creditors A/c ...Dr.		1,20,000	
	To Realisation A/c			1,20,000
	(Being the liability transferred)			
(*iii*)	Kumar's Capital A/c ...Dr.		53,100	
	To Realisation A/c			45,000
	To Outut CGST A/c			4,050
	To Output SGST A/c			4,050
	(Being the machinery taken by Kumar, CGST and SGST charged @ 9% each)			

(*iv*)	Bank A/c ...Dr.		59,000	
	To Realisation A/c			50,000
	To Output CGST A/c			4,500
	To Output SGST A/c			4,500
	(Being the balance machinery sold, charged CGST and SGST @ 9% each)			
(*v*)	Bank A/c ...Dr.		47,200	
	To Realisation A/c			40,000
	To Output CGST A/c			3,600
	To Output SGST A/c			3,600
	(Being the furniture sold, charged CGST and SGST @ 9% each)			
(*vi*)	Sham's Capital A/c ...Dr.		35,400	
	To Realisation A/c			30,000
	To Output CGST A/c			2,700
	To Output SGST A/c			2,700
	(Being the car sold to Sham, charged CGST and SGST @ 9% each)			
(*vii*)	Bank A/c ...Dr.		62,820	
	To Realisation A/c			62,820
	(Being the Debtors realised)			
(*viii*)	Ram's Capital A/c ...Dr.		6,136	
	To Realisation A/c			5,200
	To Output CGST A/c			468
	To Output SGST A/c			468
	(Being the stock taken by Ram, charged CGST and SGST @ 9% each)			
(*ix*)	Bank A/c ...Dr.		35,400	
	To Realisation A/c			30,000
	To Output CGST A/c			2,700
	To Output SGST A/c			2,700
	(Being the balance stock sold, charged CGST and SGST @ 9% each)			
(*x*)	Realisation A/c ...Dr.		1,00,300	
	To Bank A/c			1,00,300
	(Being the creditors paid)			
(*xi*)	Realisation A/c ...Dr.		5,000	
	Input CGST A/c ...Dr.		450	
	Input SGST A/c ...Dr.		450	
	To Bank A/c			5,900
	(Being the realisation expenses paid along with CGST and SGST @ 9% each)			
(*xii*)	Output CGST A/c ...Dr.		18,018	
	To Input CGST A/c			450
	To Bank A/c			17,568
	(Being the Output CGST deposited after setting off Input CGST)			
(*xiii*)	Output SGST A/c ...Dr.		18,018	
	To Input SGST A/c			450
	To Bank A/c			17,568
	(Being the Output SGST deposited after setting off Input SGST)			

Dr. OUTPUT CGST ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Input CGST A/c	450	By Kumar's Capital A/c	4,050
To Bank A/c (Balancing Figure)	17,568	By Bank A/c	4,500
		By Bank A/c	3,600
		By Sham's Capital A/c	2,700
		By Ram's Capital A/c	468
		By Bank A/c	2,700
	18,018		18,018

Dr. OUTPUT SGST ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Input SGST A/c	450	By Kumar's Capital A/c	4,050
To Bank A/c (Balancing Figure)	17,568	By Bank A/c	4,500
		By Bank A/c	3,600
		By Sham's Capital A/c	2,700
		By Ram's Capital A/c	468
		By Bank A/c	2,700
	18,018		18,018

Dr. INPUT CGST ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Bank A/c	450	By Output CGST A/c	450

Dr. INPUT SGST ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Bank A/c	450	By Output SGST A/c	450

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	Particulars		₹
To Sundry Assets (Transfer):			By Sundry Creditors A/c		1,20,000
Plant and Machinery A/c	80,000		By Kumar's Capital A/c		45,000
Furniture A/c	45,000		(Plant and Machinery Taken Over)		
Car A/c	25,000		By Sham's Capital A/c		30,000
Stock-in-Trade A/c	30,000		(Car Taken Over)		
Sundry Debtors A/c	71,000	2,51,000	By Ram's Capital A/c		5,200
To Bank A/c (Payments):			(Stock Taken Over)		
Sundry Creditors—	1,00,300		By Bank A/c (Assets Realised):		
85% of ₹ (1,20,000 – 2,000)			Machinery	50,000	
Realisation Expenses	5,000	1,05,300	Furniture	40,000	
To Gain (Profit) on Realisation:			Debtors—	62,820	
Kumar's Capital A/c	13,360		90% of ₹ (71,000 – 1,200)		
Sham's Capital A/c	8,016		Stock—	30,000	1,82,820
Ram's Capital A/c	5,344	26,720	120% of ₹ (30,000 – 5,000)		
		3,83,020			3,83,020

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Kumar (₹)	Sham (₹)	Ram (₹)	Particulars	Kumar (₹)	Sham (₹)	Ram (₹)
To Partner's Current A/c	...	...	3,000	By Balance *b/d*	60,000	40,000	30,000
To Realisation A/c (Plant and Machinery)	45,000	...	...	By Partners' Current A/cs	8,000	10,000	...
To Output CGST A/c	4,050			By Realisation A/c (Gain)	13,360	8,016	5,344
To Output SGST A/c	4,050						
To Realisation A/c (Car Taken Over)	...	30,000	...				
To Output CGST A/c		2,700					
To Output SGST A/c		2,700					
To Realisation A/c (Stock Taken Over)	...	...	5,200				
To Output CGST A/c			468				
To Output SGST A/c			468				
To Bank A/c (Final Payment)	28,260	22,616	26,208				
	81,360	58,016	35,344		81,360	58,016	35,344

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	14,000	By Realisation A/c	1,00,300
To Realisation A/c	50,000	By Realisation A/c	5,000
To Output CGST A/c	4,500	By Input CGST A/c	450
To Output SGST A/c	4,500	By Input SGST A/c	450
To Realisation A/c	40,000	By Output CGST A/c (CGST Deposited)	17,568
To Output CGST A/c	3,600	By Output SGST A/c (SGST Deposited)	17,568
To Output SGST A/c	3,600	By Kumar's Capital A/c (Final Payment)	28,260
To Realisation A/c	62,820	By Sham's Capital A/c (Final Payment)	22,616
To Realisation A/c	30,000	By Ram's Capital A/c (Final Payment)	26,208
To Output CGST A/c	2,700		
To Output SGST A/c	2,700		
	2,18,420		2,18,420

Note: Balances of Partners' Current Accounts are transferred to Capital Accounts.

Illustration 6.

A and *B* were partners sharing profits and losses in the ratio of 3 : 2. On 31st March, 2018, their Balance Sheet was as follows:

Liabilities		₹	Assets		₹
Capital A/cs:			Computers		60,000
A	2,00,000		Furniture		50,000
B	1,00,000	3,00,000	Machinery		1,50,000
General Reserve		30,000	Cash at Bank		70,000
Mrs. *A*'s Loan		50,000	Debtors	1,00,000	
Sundry Creditors		70,000	*Less:* Provision for Doubtful Debts	10,000	90,000
			Profit and Loss A/c		20,000
			Advertisement Suspense A/c		10,000
		4,50,000			4,50,000

The firm was dissolved and the assets and liabilities were settled as follows:

(*i*) Debtors realised ₹ 95,000 and machinery was sold for ₹ 1,30,000.

(*ii*) Half of the creditors accepted furniture at 25% less than the book value subject to levy of GST, which was paid by them and cash of ₹ 10,000. Remaining creditors were paid out at a discount of 10%.

(*iii*) An unrecorded asset (Bill of Exchange) of ₹ 6,900 was handed over to an unrecorded liability of ₹ 6,000 in full settlement.

(*iv*) *A* took over computers for ₹ 57,800.

(*v*) He also agreed to pay his wife's loan.

(*vi*) A liability in respect of workmen compensation of ₹ 10,000 is paid.

(*vii*) Realisation Expenses of ₹ 5,000 were paid by *B* on behalf of firm to an agency handling dissolution of the firm.

(*viii*) Sale of assets and payment of realisation expenses are subject to levy of CGST and SGST @ 9% each.

Pass the Journal entries, prepare Realisation Account, CGST and SGST (Output and Input) Accounts, Partners' Capital Accounts and Bank Account to close the books of the firm.

Solution:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Realisation A/c	...Dr.		3,60,000	
	To Computers A/c				60,000
	To Furniture A/c				50,000
	To Machinery A/c				1,50,000
	To Debtors A/c				1,00,000
	(Being the assets transferred)				
	Provision for Doubtful Debts A/c	...Dr.		10,000	
	Mrs. *A*'s Loan A/c	...Dr.		50,000	
	Sundry Creditors A/c	...Dr.		70,000	
	To Realisation A/c				1,30,000
	(Being the outside liabilities transferred)				
	A's Capital A/c	...Dr.		18,000	
	B's Capital A/c	...Dr.		12,000	
	To Profit and Loss A/c				20,000
	To Advertisement Suspense A/c				10,000
	(Being the debit balance of fictitious assets debited to Partners' Capital Accounts)				
	General Reserve A/c	...Dr.		30,000	
	To *A*'s Capital A/c				18,000
	To *B*'s Capital A/c				12,000
	(Being the Genaral Reserve credited to Partners' Capital Accounts)				

	Bank A/c ...Dr.		95,000	
	To Realisation A/c			95,000
	(Being the Debtors realised)			
	Bank A/c ...Dr.		1,53,400	
	To Realisation A/c			1,30,000
	To Output CGST A/c			11,700
	To Output SGST A/c			11,700
	(Being the machinery sold, CGST and SGST charged)			
	Realisation A/c ...Dr.		41,500	
	Bank A/c ...Dr.		6,750	
	To Output CGST A/c			3,375
	To Output SGST A/c			3,375
	To Bank A/c			41,500
	(Being the furniture given to 50% of creditors at 25% less CGST and SGST charged plus ₹ 10,000, Balance creditors paid at 10% Discount) (Note)			
	No entry for (*iii*) as both assets and liability are unrecorded			
	A's Capital A/c ...Dr.		68,204	
	To Realisation A/c			57,800
	To Output CGST A/c			5,202
	To Output SGST A/c			5,202
	(Being the computers taken by *A*, CGST and SGST charged)			
	Realisation A/c ...Dr.		50,000	
	To *A*'s Capital A/c			50,000
	(Being the liability to pay Mrs. *A*'s loan assumed)			
	Realisation A/c ...Dr.		10,000	
	To Bank A/c			10,000
	(Being the Workmen Compensation claim paid)			
	Realisation A/c ...Dr.		5,000	
	Input CGST A/c ...Dr.		450	
	Input SGST A/c ...Dr.		450	
	To *B*'s Capital A/c			5,900
	(Being the realisation expenses along with CGST and SGST paid by *B*)			
	Output CGST A/c ...Dr.		20,277	
	To Input CGST A/c			450
	To Bank A/c			19,827
	(Being the output CGST deposited after setting off input CGST)			
	Output SGST A/c ...Dr.		20,277	
	To Input SGST A/c			450
	To Bank A/c			19,827
	(Being the output SGST deposited after setting off input SGST)			
	A's Capital A/c ...Dr.		1,49,576	
	B's Capital A/c ...Dr.		84,420	
	To Bank A/c			2,33,996
	(Being the final payment to the partners)			

Note: Half of creditors accepted furniture at 25% less means that creditors of ₹ 35,000 are settled by giving furniture valued at ₹ 37,500 (*i.e.*, ₹ 50,000 *less* 25%). Giving furniture to creditors means sale of furniture on which CGST and SGST @ 9% each is charged.

Therefore, ₹ 3,375 each on account of CGST and SGST is recovered.

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	Particulars		₹
To Sundry Assets (Transfer):			By Sundry Liabilities (Transfer):		
Computer	60,000		Provision for Doubtful Debts	10,000	
Furniture	50,000		Sundry Creditors	70,000	
Machinery	1,50,000		Mrs. *A*'s Loan A/c	50,000	1,30,000
Debtors	1,00,000	3,60,000	By Bank A/c (Realisation):		
To Bank A/c (Payments):			Debtors	95,000	
Sundry Creditors		41,500	Machinery	1,30,000	2,25,000
To *A*'s Capital A/c (Mrs. *A*'s Loan)		50,000	By *A*'s Capital A/c (Computer taken)		57,800
To Bank A/c (Workmen Compensation Claim)		10,000	By Loss transferred to:		
To *B*'s Capital A/c		5,000	*A*'s Capital A/c	32,220	
			B's Capital A/c	21,480	53,700
		4,66,500			4,66,500

Dr. BANK ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Balance *b/d*		70,000	By Realisation A/c (Creditors)	41,500
To Realisation A/c:			By Realisation A/c (Workemen Comp. Claim)	10,000
Debtors	95,000		By Output CGST A/c	19,827
Machinery	1,30,000	2,25,000	By Output SGST A/c	19,827
To Output CGST A/c		11,700	By *A*'s Capital A/c	1,49,576
To Output SGST A/c		11,700	By *B*'s Capital A/c	84,420
To Output CGST A/c		3,375		
To Output SGST A/c		3,375		
		3,25,150		3,25,150

Dr. OUTPUT CGST ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Input CGST A/c	450	By Bank A/c (Machine)	11,700
To Bank A/c	19,827	By Bank A/c (Furniture)	3,375
		By *A*'s Capital A/c (Computer)	5,202
	20,277		20,277

Dr. OUTPUT SGST ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Input SGST A/c	450	By Bank A/c (Machine)	11,700
To Bank A/c	19,827	By Bank A/c (Furniture)	3,375
		By *A*'s Capital A/c (Computer)	5,202
	20,277		20,277

Dr. INPUT CGST ACCOUNT Cr.

Particulars	₹	Particulars	₹
To *B*'s Capital A/c	450	By Output CGST A/c	450

Dr. INPUT SGST ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To *B*'s Capital A/c	450	By Output SGST A/c	450

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*A* (₹)	*B* (₹)	Particulars	*A* (₹)	*B* (₹)
To Profit and Loss A/c	12,000	8,000	By Balance *b/d*	2,00,000	1,00,000
To Advertisement Suspense A/c	6,000	4,000	By General Reserve A/c	18,000	12,000
To Realisation A/c	57,800	...	By Realisation A/c	50,000	...
To Output CGST A/c	5,202	...	(Mrs. *A*'s Loan A/c)		
To Output SGST A/c	5,202	...	By Realisation A/c (Expenses)	...	5,000
To Realisation A/c (Loss)	32,220	21,480	By Input CGST A/c	...	450
To Bank A/c	1,49,576	84,420	By Input SGST A/c	...	450
	2,68,000	1,17,900		2,68,000	1,17,900

Illustration 7.

A, *B* and *C* sharing profits in the ratio of 2 : 2 : 1 agreed upon dissolution of their partnership on 31st March, 2018 on which date their Balance Sheet was as under:

Liabilities	₹	Assets		₹
Capital A/c—*A*	80,000	Fixed Assets		1,00,000
Capital A/c—*B*	60,000	Insurance Claim Receivable		50,000
Reserve	70,000	Debtors	20,000	
Creditors	37,000	*Less:* Provision for Doubtful Debts	1,000	19,000
Outstanding Rent	4,000	Stock		16,000
Investments Fluctuation Reserve	1,000	Investments		16,000
		Bank		47,000
		Capital A/c—*C*		4,000
	2,52,000			2,52,000

(*i*) Investments were taken over by *A* at ₹ 12,000; Creditors of ₹ 20,000 were taken over by *B* who has agreed to settle account with them at ₹ 19,800. Remaining Creditors were paid at ₹ 15,000.

(*ii*) Insurance Claim received ₹ 40,000 and Fixed Assets realised ₹ 1,40,000.

(*iii*) Stock and Debtors realised ₹ 14,000 and ₹ 18,000 respectively.

(*iv*) One customer, whose account was written off as bad, now paid ₹ 1,600 which is not included in ₹ 18,000 above.

(*v*) There was one unrecorded asset estimated at ₹ 6,000, half of which was handed over to an unrecorded liability of ₹ 10,000 in settlement of claim of ₹ 5,000 and remaining half was sold in the market which realised ₹ 2,600.

B took over the responsibility of completing dissolution and he is granted salary of ₹ 800 per month. Actual Realisation Expenses amounting to ₹ 2,200 were paid by the firm but were to be borne by *B*. Dissolution was completed and final payments were made on 30th July, 2018.

You are required to prepare Realisation Account, Partners' Capital Accounts and Bank Account.

Solution:

Dr. REALISATION ACCOUNT *Cr.*

Particulars		₹	Particulars		₹
To Sundry Assets (Transfer):			By Provision for Doubtful Debts A/c		1,000
Fixed Assets A/c	1,00,000		By Investments Fluctuation Reserve A/c		1,000
Insurance Claim Receivable A/c	50,000		By Creditors A/c		37,000
Debtors A/c	20,000		By Outstanding Rent A/c		4,000
Stock A/c	16,000		By *A*'s Capital A/c		12,000
Investments A/c	16,000	2,02,000	(Investments Taken Over)		
To *B*'s Capital A/c (Creditors Assumed)		19,800	By Bank A/c (Assets Realised):		
To *B*'s Capital A/c		3,200	Stock	14,000	
(Salary ₹ 800 × 4)			Debtors	18,000	
To Bank A/c (Liabilities Paid):			Bad Debts Recovered	1,600	
Creditors	15,000		Unrecorded Asset	2,600	
Unrecorded Liabilities	5,000		Fixed Assets	1,40,000	
Outstanding Rent	4,000	24,000	Insurance Claim	40,000	2,16,200
To Capital A/cs (Gain):					
A	8,880				
B	8,880				
C	4,440	22,200			
		2,71,200			2,71,200

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*A* ₹	*B* ₹	*C* ₹	Particulars	*A* ₹	*B* ₹	*C* ₹
To Balance *b/d*	...	...	4,000	By Balance *b/d*	80,000	60,000	...
To Realisation A/c	12,000	...	...	By Reserve Fund A/c	28,000	28,000	14,000
To Bank A/c (Actual Realisastion Exp.)	...	2,200	...	By Realisation A/c (Creditors + Salary) (₹ 19,800 + ₹ 3,200)	...	23,000	...
To Bank A/c (Final Settlement)	1,04,880	1,17,680	14,440	By Realisation A/c (Gain)	8,880	8,880	4,440
	1,16,880	1,19,880	18,440		1,16,880	1,19,880	18,440

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	47,000	By Realisation A/c (Liabilities Paid)	24,000
To Realisation A/c (Assets Realised)	2,16,200	By *B's* Capital A/c (Expenses)	2,200
		By *A's* Capital A/c (Final Payment)	1,04,880
		By *B's* Capital A/c (Final Payment)	1,17,680
		By *C's* Capital A/c (Final Payment)	14,440
	2,63,200		2,63,200

Illustration 8.

X and *Y* are partners sharing profits and losses in the ratio of 3 : 2 as at 31st March, 2018, their Balance Sheet stood as follows:

Liabilities		₹	Assets		₹
Creditors		1,60,000	Cash		22,000
Bills Payable		40,000	Cash at Bank		50,000
Loan from *X*		10,000	Stock		1,60,000
Loan from Mrs. *X*		30,000	Debtors	1,32,000	
Employees' Provident Fund		8,000	*Less:* Provision for Doubtful Debts	12,000	1,20,000
Commission Received in Advance		2,000	Plant and Machinery		60,000
Provision for Depreciation (Machinery)		20,000	Land and Building		66,000
General Reserve		50,000	Investments (Face Value ₹ 4,000)		20,000
Profit and Loss A/c		20,000	Other Investments		10,000
X's Capital	1,68,000		Goodwill		25,000
Y's Capital	52,000	2,20,000	Prepaid Insurance		7,000
			Deferred Revenue Advertisement Expenditure		20,000
		5,60,000			5,60,000

Note: There is a bill for ₹ 2,000 under discount. The bill was received from *Z*.

The firm was dissolved on the given date and the following transactions took place:

(*i*) *Y* undertook to pay Mrs. *X's* Loan.

(*ii*) *X* took over 50% of the Stock at a discount of 20%.

(*iii*) Remaining Stock was sold at a profit of 30% on cost.

(*iv*) ₹ 24,000 of the Book Debts proved bad.

(*v*) Land and Building sold for ₹ 3,00,000 through a broker who charged 2% commission.

(*vi*) Half the Creditors accepted Plant and Machinery at an agreed value of ₹ 54,000 and accepted cash in full settlement of their claims after allowing a discount of ₹ 16,000.

(*vii*) Remaining Creditors were paid ₹ 74,000 in final settlement including an Investment worth ₹ 4,000 unrecorded in the books.

(*viii*) Bills Payable falling due on 30th April, 2018 were discharged at a discount of 18% p.a.

(*ix*) *X* was to receive ₹ 11,100 as remuneration for completing the dissolution work and was to bear Realisation Expenses. Realisation Expenses were ₹ 9,100 paid by the firm.

(*x*) *W*, an old customer, whose account was written off as bad in the previous year, paid ₹ 1,000 which is not included in the above stated Debtors.

(*xi*) *Z* proved insolvent and a first and final dividend of 25% was received from his estate.

(*xii*) Investments realised 150% of their face value and Other Investments realised ₹ 10,000.

(*xiii*) Workmen Compensation Liability amounted to ₹ 2,400.

(*xiv*) Commission received in advance was returned to customers after deducting ₹ 400.

Prepare Realisation Account, Partners' Capital Accounts and Bank Account.

Solution:

Dr. REALISATION ACCOUNT *Cr.*

Particulars		₹	Particulars		₹
To Sundry Assets (Transfer):			By Provision for Doubtful Debts A/c		12,000
Stock A/c	1,60,000		By Creditors A/c		1,60,000
Debtors A/c	1,32,000		By Bills Payable A/c		40,000
Plant and Machinery A/c	60,000		By Mrs. *X*'s Loan A/c		30,000
Land and Building A/c	66,000		By Employees' Provident Fund A/c		8,000
Investments A/c	20,000		By Commission Received in Advance A/c		2,000
Other Investments A/c	10,000		By Machinery Depreciation Reserve A/c		20,000
Goodwill A/c	25,000		By *X*'s Capital A/c (Stock)		64,000
Prepaid Insurance A/c	7,000	4,80,000	By Bank A/c (Assets Realised):		
To *Y*'s Capital A/c (Mrs. *X*'s Loan)		30,000	Stock	1,04,000	
To Bank A/c (Liabilities Paid):			Debtors	1,08,000	
Creditors (₹ 10,000 + ₹ 70,000)	80,000		Land and Building	2,94,000	
Bills Payable	39,400		Investments	6,000	
EPF	8,000		Other Investments	10,000	5,22,000
Commission	1,600		By Bank A/c (Bad Debts Recovered)		1,000
Liability for Workmen			By Bank A/c (From *Z*)		500
Compensation	2,400	1,31,400			
To *X*'s Capital A/c (Realisation Expenses)		11,100			
To Bank A/c (Discounted B/R)		2,000			
To Gain (Profit) on Realisation transferred to:					
X's Capital A/c	1,23,000				
Y's Capital A/c	82,000	2,05,000			
		8,59,500			8,59,500

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	*X* ₹	*Y* ₹	Particulars	*X* ₹	*Y* ₹
To Realisation A/c (Stock)	64,000	...	By Balance *b/d*	1,68,000	52,000
To Bank A/c	9,100	...	By Realisation A/c (Mrs. *X*'s Loan)	...	30,000
To Deferred Revenue			By Realisation A/c (Expenses)	11,100	...
Advertisement Expenditure A/c	12,000	8,000	By Realisation A/c (Gain)	1,23,000	82,000
To Bank A/c	2,59,000	1,84,000	By General Reserve A/c	30,000	20,000
			By Profit and Loss A/c	12,000	8,000
	3,44,100	1,92,000		3,44,100	1,92,000

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	50,000	By Realisation A/c (Liabilities Paid)	1,31,400
To Cash A/c	22,000	By *X*'s Capital A/c	9,100
To Realisation A/c (Assets Realised)	5,22,000	By Realisation A/c	2,000
To Realisation A/c (Bad Debts Recovered)	1,000	By Loan from *X* A/c	10,000
To Realisation A/c	500	By *X*'s Capital A/c (Final Payment)	2,59,000
		By *Y*'s Capital A/c (Final Payment)	1,84,000
	5,95,500		5,95,500

Illustration 9.

Asha, Rekha and Saroj sharing profit in the proportion of 1/6 : 1/3 : 1/2 agreed upon dissolution of their partnership on 31st March, 2018 on which date their Balance Sheet was as follows:

Liabilities		₹	Assets		₹
Capital A/cs:			Sundry Assets		37,500
Asha	30,000		Debtors	7,500	
Rekha	22,500	52,500	*Less:* Provision for Discount on Debtors	375	7,125
Mrs. Asha's Husband's Loan		5,000	Stock (At Invoice Price)		7,500
Creditors		13,875	Investments		13,500
Salary Outstanding		1,500	Cash in Hand		7,625
Investments Fluctuation Reserve		10,500	Cash at Bank		17,625
Reserve		7,500	Saroj's Capital		1,500
Stock Reserve		1,500			
		92,375			92,375

Additional Information:

(*i*) Investments were taken by Asha at ₹ 12,000.

(*ii*) Creditors of ₹ 7,500 were taken over by Rekha, who has agreed to settle the account with them at ₹ 7,425. Remaining Creditors were paid ₹ 5,625.

(*iii*) Sundry Assets realised ₹ 52,500.

(*iv*) Stock and Debtors realised ₹ 5,250 and ₹ 6,750 respectively.

(*v*) A customer, whose account was written off as bad, now paid ₹ 600, which is not included in ₹ 7,500 above.

(*vi*) It was found that an Investment not recorded in the books was worth ₹ 2,250, half of which was handed over to an unrecorded liability of ₹ 3,750 in settlement of his claim of ₹ 1,875 and remaining half was sold in the market, which realised ₹ 975.

(*vii*) The Expenses of Realisation amounted to ₹ 825.

Prepare Realisation Account, Partners' Capital Accounts and Cash Account to close the books of firm. [*CA*(*P.E.I.*) *Nov., 2004, Modified*]

Solution:

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	Particulars		₹
To Sundry Assets A/c		37,500	By Provision for Discount on Debtors A/c		375
To Debtors A/c		7,500	By Mrs. Asha's Husband's Loan A/c		5,000
To Stock A/c		7,500	By Creditors A/c		13,875
To Investments		13,500	By Salary Outstanding A/c		1,500
To Rekha's Capital A/c (Creditors)		7,425	By Investments Fluctuation Reserve A/c		10,500
To Bank A/c (Asha's Husband's Loan)		5,000	By Stock Reserve A/c		1,500
To Bank A/c (Sundry Liabilities):			By Asha's Capital A/c (Investments)		12,000
Remaining Creditors	5,625		By Bank A/c (Assets Realised):		
Unrecorded Liability (Note)	1,875		Sundry Assets	52,500	
Salary Outstanding	1,500	9,000	Stock	5,250	
To Bank A/c (Realisation Expenses)		825	Debtors	6,750	
To Gain (Profit) transferred to:			Unrecorded Investments	975	65,475
Asha's Capital A/c	3,763		By Bank A/c (Bad Debts Recovered)		600
Rekha's Capital A/c	7,525				
Saroj's Capital A/c	11,287	22,575			
		1,10,825			1,10,825

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	Asha ₹	Rekha ₹	Saroj ₹	Particulars	Asha ₹	Rekha ₹	Saroj ₹
To Balance *c/d*	...	...	1,500	By Balance *b/d*	30,000	22,500	...
To Realisation A/c (Investment taken)	12,000	...	...	By Reserve A/c	1,250	2,500	3,750
				By Realisation A/c (Creditors taken over)	...	7,425	...
To Bank A/c (Bal. Fig.) (Final Payment)	23,013	39,950	13,537	By Realisation A/c (Gain)	3,763	7,525	11,287
	35,013	39,950	15,037		35,013	39,950	15,037

Dr. BANK ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance *b/d*	17,625	By Realisation A/c (Mrs. Asha's Husband Loan)	5,000
To Cash A/c	7,625	By Realisation A/c (Sundry Liabilities)	9,000
To Realisation A/c (Bad Debts Recovered)	600	By Realisation A/c (Realisation Expenses)	825
To Realisation A/c (Assets Realised)	65,475	By Asha's Capital A/c	23,013
		By Rekha's Capital A/c	39,950
		By Saroj's Capital A/c	13,537
	91,325		91,325

Note: Unrecorded investment worth ₹ 1,125 was given as settlement of unrecorded liability of ₹ 3,750 for a claim of ₹ 1,875. Balance amount of 1,875 has been paid in cash.

Advanced Level Questions

Illustration 10.

Lion and Tiger were in partnership sharing profits and losses in the ratio of 3 : 1. On 31st March, 2018, the Balance Sheet of the firm was as follows:

Liabilities		₹	Assets	₹
Capital A/cs:			Fixed Assets	2,10,000
Lion	2,40,000		Stock	1,12,000
Tiger	80,000	3,20,000	Sundry Debtors	1,96,000
Current A/cs:			Cash at Bank	37,200
Lion	42,000			
Tiger	20,000	62,000		
Loan (Tiger)		30,000		
Creditors		1,43,200		
		5,55,200		5,55,200

They decided to dissolve the partnership firm on the date of the Balance Sheet.

XYZ Ltd. agreed to take Stock and Fixed Assets excluding motor car having a book value of ₹ 41,000, for a consideration of ₹ 4,80,000 which is to be satisfied by payment of cash ₹ 1,60,000, allotment of 1,600 Debentures of ₹ 100 each valued at ₹ 75 per share and the balance by allotment of 1,600 Equity Shares of the face value of ₹ 100 each.

The Debtors realised ₹ 1,92,000 and the Creditors were settled for ₹ 1,40,000.

The following was the agreement between the partners:

(*i*) The Equity Shares should be allotted in the ratio of the Partners' Capital Accounts as per Balance Sheet.

(*ii*) Lion to take over the motor car at an agreed value of ₹ 42,000.

(*iii*) Debentures to be allotted to Tiger to the value of his loan and the remaining to be allotted equally between the partners.

(*iv*) Balance remaining to be settled in cash.

You are required to show Realisation Account, Partners' Capital Accounts, *XYZ* Ltd.'s Account, Bank Account and Statement showing distribution of shares and debentures.

Solution:

Dr. REALISATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Fixed Assets A/c		2,10,000	By Creditors A/c	1,43,200
To Stock A/c		1,12,000	By *XYZ* Ltd.	4,80,000
To Debtors A/c		1,96,000	By Lion's Capital A/c	42,000
To Bank A/c (Creditors)		1,40,000	(Motor Car Taken Over)	
To Gain (Profit) transferred to:			By Bank A/c (Debtors)	1,92,000
Lion's Capital A/c (3/4)	1,49,400			
Tiger's Capital A/c (1/4)	49,800	1,99,200		
		8,57,200		8,57,200

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Lion ₹	Tiger ₹	Particulars	Lion ₹	Tiger ₹
To Realisation A/c (Motor Car)	42,000	...	By Balance *b/d*	2,40,000	80,000
To Debentures of *XYZ* Ltd. A/c (₹ 1,20,000 – ₹ 30,000 = ₹ 90,000) (divided equally) (See Statement of Distribution of Shares and Debentures)	45,000	45,000	By Current A/cs (Transfer)	42,000	20,000
To Equity Shares A/c (3 : 1)	1,50,000	50,000	By Realisation A/c (Gain)	1,49,400	49,800
To Bank A/c (Final Payment)	1,94,400	54,800			
	4,31,400	1,49,800		4,31,400	1,49,800

Dr. *XYZ* LTD. *Cr.*

Particulars	₹	Particulars	₹
To Realisation A/c (Stock and Fixed Assets excluding Motor Car)	4,80,000	By Bank A/c	1,60,000
		By Debentures of *XYZ* Ltd. A/c (1,600 × ₹ 75)	1,20,000
		By Equity Shares of *XYZ* Ltd. A/c (1,600 × ₹ 125*)	2,00,000
	4,80,000		4,80,000

	₹	₹
* Total purchase consideration		4,80,000
Less: Cash received	1,60,000	
Value of Debentures Received	1,20,000	2,80,000
Balance being value of 1,600 Equity Shares		2,00,000

∴ Issue price of a share = ₹ 2,00,000/1,600 = ₹ 125.

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	37,200	By Realisation A/c (Creditors Paid)	1,40,000
To *XYZ* Ltd.	1,60,000	By Lion's Capital A/c (Final Payment)	1,94,400
To Realisation A/c (Debtors Realised)	1,92,000	By Tiger's Capital A/c (Final Payment)	54,800
	3,89,200		3,89,200

STATEMENT SHOWING DISTRIBUTION OF SHARES AND DEBENTURES

Particulars	Total ₹	Lion ₹	Tiger ₹
(*i*) Debentures of *XYZ* Ltd. 1,600 debentures of ₹ 100 each, valued @ ₹ 75 per debenture	1,20,000		
Less: Debentures allotted to Tiger against his Loan	30,000		
Balance Distributed between Partners equally against Capital	90,000	45,000	45,000
(*ii*) Equity Shares of *XYZ* Ltd. 1,600 shares of ₹ 100 each, valued @ ₹ 125 per share distributed in the ratio of capitals, *i.e.*, 2,40,000 : 80,000 or 3 : 1.		1,50,000	50,000

Illustration 11.

Cat and Rat were in partnership sharing profits and losses in the ratio of 3 : 1. On 31st March, 2018, the Balance Sheet of the firm was as follows:

Liabilities		₹	Assets	₹
Capital A/cs:			Fixed Assets	21,000
Cat	24,000		Stock	11,200
Rat	8,000	32,000	Sundry Debtors	19,600
Current A/cs:			Cash at Bank	3,720
Cat	4,200			
Rat	2,000	6,200		
Loan (Rat)		3,000		
Creditors		14,320		
		55,520		55,520

They decided to dissolve the partnership firm as at the date of the Balance Sheet.

Elephant Ltd. agreed to take Stock and Fixed Assets excluding furniture having a book value of ₹ 4,100, for a consideration of ₹ 48,000 which is to be satisfied by payment of cash ₹ 16,000, allotment of 160 Preference Shares of ₹ 100 each valued at ₹ 75 per share and the balance by allotment of 1,600 Equity Shares of the face value of ₹ 10 each.

The Debtors realised ₹ 19,200 and the Creditors were settled for ₹ 14,000.

The following was the agreement between the partners:

(*i*) The Equity Shares should be allotted in the ratio of the Partners' Capital Accounts as per Balance Sheet.

(*ii*) Cat to take over the furniture at an agreed value of ₹ 4,200.

(*iii*) The Preference Shares to be allotted to Rat to the value of his loan and the remaining to be allotted equally between the partners.

(*iv*) Balance remaining to be settled in cash.

You are required to show: (*i*) Realisation Account, (*ii*) Partners' Capital Accounts, (*iii*) Bank Account and Statement showing distribution of shares.

Solution:

Dr. REALISATION ACCOUNT Cr.

Particulars		₹	Particulars	₹
To Fixed Assets A/c		21,000	By Creditors A/c	14,320
To Stock A/c		11,200	By Elephant Ltd.	48,000
To Sundry Debtors A/c		19,600	By Cat's Capital A/c	4,200
To Bank A/c (Creditors)		14,000	(Furniture Taken Over)	
To Gain (Profit) transferred to:			By Bank A/c (Debtors)	19,200
Cat's Capital A/c (3/4)	14,940			
Rat's Capital A/c (1/4)	4,980	19,920		
		85,720		85,720

Dr. PARTNERS' CAPITAL ACCOUNTS Cr.

Particulars	Cat ₹	Rat ₹	Particulars	Cat ₹	Rat ₹
To Realisation A/c (Furniture)	4,200	...	By Balance *b/d*	24,000	8,000
To Preference Shares of			By Current A/cs	4,200	2,000
Elephant Ltd. A/c	4,500	4,500	(Transfer)		
(₹ 12,000 – ₹ 3,000 = ₹ 9,000)			By Realisation A/c	14,940	4,980
(divided equally) (See Statement			(Gain)		
of Distribution of Equity and					
Preference Shares)					
To Equity Shares of Elephant Ltd					
A/c (3 : 1)	15,000	5,000			
To Bank A/c (Final Payment)	19,440	5,480			
	43,140	14,980		43,140	14,980

Dr. ELEPHANT LTD. Cr.

Particulars	₹	Particulars	₹
To Realisation A/c	48,000	By Bank A/c	16,000
(Stock and Fixed Assets		By Preference Shares of Elephant Ltd. A/c	12,000
excluding Furniture)		(160 × ₹ 75)	
		By Equity Shares of Elephant Ltd. A/c	20,000
		(1,600 × ₹ 12.5*)	
	48,000		48,000

	₹	₹
* Total Purchase Consideration		48,000
Less: Cash Received	16,000	
Value of Preference Shares Received	12,000	28,000
Balance being value of 1,600 Equity Shares		20,000

∴ Issue price of an Equity Share = ₹ 20,000/1,600 = ₹ 12.5.

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	3,720	By Realisation A/c (Creditors Paid)	14,000
To Elephant Ltd.	16,000	By Cat's Capital A/c (Final Payment)	19,440
To Realisation A/c (Debtors Realised)	19,200	By Rat's Capital A/c (Final Payment)	5,480
	38,920		38,920

STATEMENT SHOWING DISTRIBUTION OF EQUITY AND PREFERENCE SHARES

Particulars	Total ₹	Cat ₹	Rat ₹
(*i*) Preference Shares of Elephant Ltd. 160 Preference Shares of ₹ 100 each, valued @ ₹ 75 each	12,000		
Less: Preference Shares allotted to Rat against his Loan	3,000		
Balance Distributed between Partners equally against Capital	9,000	4,500	4,500
(*ii*) Equity Shares of Elephant Ltd. 1,600 shares of ₹ 10 each, valued @ ₹ 12.5 per share distributed in the ratio of capitals, *i.e.*, 24,000 : 8,000 or 3 : 1.		15,000	5,000

Unsolved Questions

1. Following is the Balance Sheet as at 31st March, 2018 of *A*, *B* and *C* carrying on business in partnership sharing profits and losses in the ratio of 2 : 2 : 1:

Liabilities		₹	Assets	₹
Capital A/cs:			Fixed Assets	10,50,000
A	6,00,000		Sundry Debtors	4,50,000
B	3,75,000	9,75,000	Stock	1,50,000
Mortgage Loan		6,00,000	Cash at Bank	75,000
Reserve		90,000	*C*'s Capital A/c	90,000
Sundry Creditors		1,50,000		
		18,15,000		18,15,000

They decided to dissolve the partnership and the following arrangements were agreed upon:

(*i*) Fixed assets included:

(*a*) Machinery ₹ 82,500 taken by *B* at an agreed value of ₹ 1,35,000 after the repairing costs amounted to ₹ 30,000 to be borne by the firm.

(*b*) Land and Building ₹ 7,50,000 taken by *A* at an agreed value of ₹ 9,00,000 subject to the mortgage loan to be taken over at ₹ 6,00,000.

(*ii*) Other assets (excluding Cash at Bank) and Creditors are taken over by Welfare Limited in consideration of issue of 5,000 debentures of ₹ 150 each fully paid. These debentures are taken over at a total agreed value of ₹ 7,20,000 equally by *A* and *B*.

(*iii*) Creditors for ₹ 37,500 not provided for in the books had to be paid.

Prepare Realisation Account, Partners' Capital Accounts, Bank Account assuming that the final settlement was made by the partners bringing in the amounts due from them.

2. Give necessary Journal entries to record the discharge of following unrecorded liabilities:

(*i*) There was a contingent liability in respect of bill discounted but not matured of ₹ 10,000. An acceptor of one bill of ₹ 2,000 became insolvent and fifty paise in a rupee was recovered. The liability of the firm on account of this bill discounted has not so far been recorded.

(*ii*) There was a contingent liability in respect of a claim for damages for ₹ 15,000. Such liability was settled for ₹ 12,500 and was undertaken by a partner Mr. Ashok to pay.

(*iii*) The firm was required to pay ₹ 10,000 as compensation to an employee for an injury suffered by him, which was a contingent liability not accepted by the firm.

(*iv*) ₹ 8,000 for damages claimed by a customer against the firm. It was agreed at 50% by a compromise between the customer and the firm.

(*v*) Trade creditors were ₹ 3,20,000. Half the trade creditors accepted Plant and Machinery at the value of ₹ 1,08,000 and cash in full settlement of their claim after allowing a discount of ₹ 32,000. Remaining creditors were paid 95% in final settlement.

[**Hints:** (*i*) Dr. Realisation A/c and Cr. Bank A/c by ₹ 20,000*.

(*ii*) Dr. Realisation A/c and Cr. Bank A/c by ₹ 1,52,000.

*₹ 1,60,000 – ₹ 1,08,000 – ₹ 32,000 = ₹ 20,000.]

3. There was one unrecorded asset estimated at ₹ 20,000, half of which was handed over to an unrecorded liability of ₹ 20,000 in settlement of a claim of ₹ 13,000 and remaining half was sold in the market at a discount of ₹ 500. Give necessary Journal entries.

4. Following is the Balance Sheet of Rahul and Rohit as at 31st March, 2018:

Liabilities		₹	Assets		₹
Sundry Creditors		20,000	Goodwill		10,000
Bills Payable		20,000	Building		25,000
Bank Overdraft		10,000	Plant and Machinery		25,000
Mrs. Rahul's Loan		20,000	Investments		15,300
Rohit's Loan		10,000	Stock		8,700
Investments Fluctuation Fund		2,800	Debtors	17,000	
Employees' Provident Fund		1,200	*Less*: Provision for Doubtful Debts	2,000	15,000
General Reserve		2,000	Bills Receivable		10,000
Rahul's Capital	20,000		Cash at Bank		13,000
Rohit's Capital	20,000	40,000	Profit and Loss A/c		4,000
		1,26,000			1,26,000

The firm was dissolved on 31st March, 2018 and the following was agreed upon:

(*i*) Rahul agreed to pay off his wife's Loan.

(*ii*) Debtors realised ₹ 12,000.

(*iii*) Rohit took all Investments at ₹ 12,000.

(*iv*) Other assets realised as follows:

	₹
Plant and Machinery	20,000
Building	50,000
Goodwill	6,000

(*v*) Sundry Creditors and Bills Payable were settled at 5% discount.

(*vi*) Rahul accepted Stock at ₹ 8,000 and Rohit took over Bills Receivable at 20% discount.

(*vii*) Realisation Expenses amounted to ₹ 2,000.

Prepare Realisation Account, Partners' Capital Accounts and Bank Account.

5. Following is the Balance Sheet of *A* and *B* for the year ended 31st March, 2018:

Liabilities		₹	Assets		₹
Capital A/cs:			Goodwill		30,000
A	34,000		Building		24,000
B	28,000	62,000	Furniture		4,000
A's Loan		20,000	Stock		14,000
Reserve		12,000	Sundry Debtors	30,000	
Sundry Creditors		4,000	*Less:* Provision for Doubtful Debts	4,000	26,000
Bills Payable		10,000	Bills Receivable		6,000
			Cash		4,000
		1,08,000			1,08,000

A and *B* shared the profits and losses equally. They decided to dissolve the partnership on the above date.

The assets of the firm realised as follows:

Building ₹ 32,000; Furniture ₹ 4,000; Sundry Debtors ₹ 24,000; Goodwill Nil; Stock ₹ 10,000; Bills Receivable ₹ 5,000. Realisation Expenses amounted to ₹ 3,400.

The Creditors agreed to accept ₹ 400 less. Compensation to Employees paid by the firm amounted to ₹ 3,000. This liability was not provided for in the above Balance Sheet.

There was a printer in the firm, which was bought out of the firm's money, was not shown in the above Balance Sheet. This printer is now sold for ₹ 4,000.

Prepare Realisation Account, Partners' Capital Accounts and Cash Account.

6. *A* and *B* were partners sharing profits and losses as to 7/11th to *A* and 4/11th to *B*. They dissolved the partnership on 30th May, 2018. On that date their Capitals were: *A* ₹ 7,000 and *B* ₹ 4,000. There were also dues on Loan Account to *A* ₹ 4,500 and to *B* ₹ 750. The other liabilities amounted to ₹ 5,000. The assets proved to have been undervalued in the last Balance Sheet and actually realised ₹ 24,000.

Prepare necessary accounts showing the final settlement between partners.

7. On 1st April, 2018 *A, B* and *C* commenced business in partnership sharing profits and losses in proportion of 1/2, 1/3 and 1/6 respectively. They deposited in their Bank Account as their Capital ₹ 22,000: ₹ 10,000 by *A*; ₹ 7,000 by *B;* and ₹ 5,000 by *C*. During the year, they drew ₹ 5,000: being ₹ 1,900 by *A*; ₹ 1,700 by *B;* and ₹ 1,400 by *C*.

On 31st March, 2019 they dissolved their partnership, *A* taking up Stock at an agreed value of ₹ 5,000; *B* taking up Furniture at ₹ 2,000; and *C* taking up Debtors at ₹ 3,000. After paying up their Creditors, there remained a balance of ₹ 1,000 at Bank.

Prepare necessary accounts showing the distribution of the cash at the Bank and of the further cash brought in by any partner or partners as the case required.

8. *X* and *Y* were partners sharing profits and losses in the ratio of 3 : 2. They decided to dissolve the firm on 31st July, 2018. On that date, their Capitals were: *X* ₹ 40,000 and *Y* ₹ 30,000. Creditors amounted to ₹ 24,000.

Assets were realised for ₹ 88,500. Creditors of ₹ 16,000 were taken over by *X* at ₹ 14,000. Remaining Creditors were paid at ₹ 7,500. The cost of Realisation came to ₹ 500.

Prepare necessary accounts.

GUIDE TO ANSWERS

1. Gain (Profit) on Realisation—₹ 1,87,500; Final Payment to *A*—₹ 51,000; Amount brought in by *B*—₹ 9,000 and *C*—₹ 34,500. Total of Bank A/c—₹ 1,18,500.

3. (*i*) Dr. Bank A/c and Cr. Realisation A/c—₹ 9,500*.

(*ii*) Dr. Realisation A/c and Cr. Bank A/c—₹ 7,000**.

*₹ 20,000 (Unrecorded Assets) – $\frac{1}{2}$ of ₹ 20,000 (Settlement of Liability)—₹ 500 = ₹ 9,500.

**₹ 20,000 – ₹ 13,000 = ₹ 7,000.

4. Gain (Profit) on Realisation—₹ 9,800; Final Payment: Rahul—₹ 35,900; Rohit—₹ 13,900. Total of Bank Account—₹ 1,01,000.

5. Loss on Realisation—₹ 31,000; Final Payment: *A*—₹ 24,500; *B*—₹ 18,500. Total of Cash Account—₹ 83,000.

6. Sundry Assets on the date of dissolution were: ₹ 21,250; Gain (Profit) on Realisation: ₹ 2,750; Final Payment: *A*—₹ 8,750; *B*—₹ 5,000. Total of Bank Account—₹ 24,000.

7. Loss on Realisation—₹ 6,000; Final Payment: *A*—₹ 100; *B*—₹ 1,300; Cash brought in by *C*—₹ 400. Total of Bank Account—₹ 1,400.

8. Total Sundry Assets—₹ 94,000; Loss on Realisation—₹ 3,500; *X* receives—₹ 51,900; and *Y* receives—₹ 28,600. Total of Bank Account—₹ 88,500.

CHAPTER 6

Joint Stock Company—Issue of Shares

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Company

It is an entity incorporated through the process of law for undertaking (usually) a business. It is an artificial person distinct and separate from its members who are known as **shareholders**.

A company may be one person company or private company or a public company.

2. One Person Company

It is a company which has only one person as a member.

3. Private Company

It is a company which has minimum paid-up capital as may be prescribed* and which by its Articles of Association:

(*i*) restricts the right to transfer its shares, if any.

(*ii*) except in One Person Company, limits the number of its members excluding its present and past employee members to 200; if the past or present employee acquired the shares while in employment and continue to hold them.

If any share is held jointly by two or more persons, they shall be treated as a single member.

(*iii*) prohibits any invitation to the public to subscribe for any securities of the company.

The minimum number of members required to form a private company is **two**.

The name of a Private Company ends with the words, *'Private Limited'*.

4. Public Company

It is a company which has minimum paid-up capital as may be prescribed* and which

(*i*) is not a one person company or a private company;

(*ii*) is a private company, which is a subsidiary of a public company.

The minimum number of members required to form a public limited company is **seven**. There is no restriction on maximum number of members.

The name of a Public Company ends with the word *'Limited'*.

5. Share

'Share' means a share in the Share Capital of a company and includes stock.

[Section 2(84) of the Companies Act, 2013]

It is a unit into which Share Capital of a company is divided.

6. Preference Share Capital

It is a kind of share capital which carries preferential rights in respect of dividend payment and repayment of capital over Equity Shareholders, if the company is wound up.

*Companies are not required to have minimum paid-up capital *w.e.f.* 29th May, 2015.

7. Equity Share Capital

It is that share capital which is not Preference Share capital.

8. Allotment of Shares

Allotment is the allocation of shares to the successful applicants by the company.

9. Allotment Money

The amount payable on allotment is called **Allotment Money**.

10. Authorised or Nominal Capital

'Authorised Capital' or 'Nominal Capital' means such capital as is authorised by the Memorandum of a company to be the maximum amount of Share Capital of the company.

[Section 2(8) of the Companies Act, 2013]

It is the maximum amount of capital which the company is, for the time being, authorised to raise. It includes both Preference Share Capital and Equity Share Capital.

11. Issued Capital

'Issued Capital' means such capital as the company issues from time to time for Subscription.

[Section 2(50) of the Companies Act, 2013]

12. Subscribed Capital

'Subscribed Capital' means such part of the capital which is for the time being subscribed by the members of a company. [Section 2(86) of the Companies Act, 2013]

13. Paid-up Share Capital or Share Capital Paid-up

'Paid-up Share Capital' or 'Share Capital Paid-up' means such aggregate of money credited and paid-up as is equivalent to the amount received as paid-up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of a company, but does not include any other amount received in respect of such shares, by whatever name called.

[Section 2(64) of the Companies Act, 2013]

14. Subscribed and Fully Paid-up

It is the amount of share capital issued by a company that is subscribed on which the company has called and also received entire nominal (face) value of the share.

15. Subscribed but not Fully Paid-up

It is the amount of share capital issued by a company that is subscribed but the company has not received entire nominal (face) value of the share.

16. Reserve Capital

It is that part of the authorised capital that a company resolves to call in the event of its winding up.

17. Capital Reserve

It is a reserve created out of capital profits.

18. Issue of Shares for Cash

It means the consideration for shares is received through cash/cheque or any other banking instrument against the shares.

19. Issue of Shares for Consideration Other than Cash

It means the consideration for shares is received otherwise than through cash/cheque or any other banking instrument but they have been issued for assets purchased or services taken.

20. Par Value

Par value means the Nominal or Face value of a share.

21. Issue of Shares at Par

It means the issue price and nominal (face) value of the share is same.

22. Issue of Shares at Premium

It means the issue price of the share is higher than its nominal (face) value.

23. Shares Payable in Lump Sum

It means that shares are issued for a consideration payable in Lump sum, *i.e.*, entire issue price of a share is payable, along with the application.

24. Shares Payable in Instalments

It means that shares are issued for a consideration not payable in Lump sum but in parts, *i.e.*, issue price of a share is payable, partly on application and partly on allotment and calls.

25. Undersubscription of Shares

The shares are said to be undersubscribed if the number of shares applied for is less than the number of shares issued for subscription.

26. Oversubscription of Shares

When the company receives applications for more shares than issued, it is known as **Oversubscription**.

27. Pro rata Allotment

Pro rata allotment means allotment in proportion of shares applied for.

28. Calls-in-Arrears

It is that part of the calls money that has been called-up by the company but has not been received by it.

29. Calls-in-Advance

It is that amount which has not been called-up by the company but has been received by it.

30. Forfeiture of Shares

Forfeiture of shares means cancellation of allotted shares.

31. Reissue of Shares

Reissue of shares means sale of forfeited shares.

SUMMARY OF THE CHAPTER

- A *company* is an entity formed by an association of persons through the process of law for undertaking (usually) a business.

  The *essential characteristics* of a company are:

  (*i*) It is a *voluntary association* of individuals coming into existence through the process of law for undertaking (usually) a business venture.

  (*ii*) It is an *artificial person* created by the process of law.

  (*iii*) It has a *separate legal entity*.

  (*iv*) It has a *perpetual succession*, *i.e.*, it can be created and wound up by law only.

  (*v*) It has a *common seal*, *i.e.,* official seal of the company.

  (*vi*) The *shares of a company can be transferred* from one person to another.

- **Share and Share Capital**

  Share means a share in the capital of a company and includes stock.

  [Section 2(84) of the Companies Act, 2013]

  Share capital of a company is divided into small units with a definite face value. Each of these small units is called a **share**. Share capital is that part of the capital of a company which is represented by the total nominal value of shares, it has issued.

- **Sub-Division of Share Capital**
  - (*i*) *Authorised Share Capital:* 'Authorised Capital' or 'Nominal Capital' means such capital as is authorised by the Memorandum of a company to be the maximum amount of Share Capital of the company. [Section 2(8) of the Companies Act, 2013]
  - (*ii*) *Issued Share Capital:* 'Issued Capital' means such capital as the company issues from time to time for Subscription. [Section 2(50) of the Companies Act, 2013]
  - (*iii*) *Subscribed Share Capital:* 'Subscribed Capital' means such part of the capital which is for the time being subscribed by the members of a company. [Section 2(86) of the Companies Act, 2013]
  - (*iv*) *Called-up Share Capital* is the amount of nominal value of share capital that has been called by the company to be paid by the shareholders. [Section 2(15) of the Companies Act, 2013]
  - (*v*) *Paid-up Share Capital:* 'Paid-up Share Capital' or 'Share Capital Paid-up' means such aggregate of money credited and paid-up as is equivalent to the amount received as paid-up in respect of shares issued and also includes any amount credited as paid-up in respect of shares of a company, but does not include any other amount received in respect of such shares, by whatever name called. [Section 2(64) of the Companies Act, 2013]

  Reserve Capital is a part of subscribed share capital that a company resolves, by a Special Resolution, not to call except at the time of winding up of the company.

  Capital Reserve is the amount of profit arising out of capital transactions.

- **Types of Shares:** Shares that can be issued are Preference Shares or Equity Shares.

  Preference Shares are the shares that carry preferential right as to dividend at fixed rate or amount and preferential right as to repayment of capital.

  Equity Shares are the shares that are not Preference Shares.

  Shares can be issued for cash and for consideration other than cash.

  Shares can be issued at par or at premium.

  Shares are said to be issued at par when they are issued at a price equal to the nominal (face) value, *i.e.*, when the issue price and nominal (face) value are same.

  Shares are said to be issued at premium when they are issued at a price higher than nominal (face) value.

- **A Company can issue its shares:**
  - (*i*) for cash, and
  - (*ii*) for consideration other than cash.

- **Oversubscription of Shares** means shares applied for are more than the shares offered for subscription.

- **Undersubscription of Shares** means shares applied for are less than the shares offered for subscription.

- ***Pro rata* Allotment** means allotment of shares in a fixed proportion. *Pro rata* allotment takes place only when the shares are oversubscribed.

- **Securities Premium Reserve** can be utilised for the following purposes:
  - (*i*) issuing fully paid bonus shares;
  - (*ii*) writing off preliminary expenses;
  - (*iii*) writing off expenses such as share issue expenses, commission, discount allowed on issue of securities or debentures;
  - (*iv*) providing for the premium payable on redemption of debentures or Preference Shares; or
  - (*v*) in buying-back its own shares.

- **Call** is a demand by a company to the holders of partly paid shares to pay a further instalment towards full nominal value.

- **Calls-in-Arrears** is the amount not yet received by the company against the call or calls demanded. Calls not received by the company is transferred to Calls-in-Arrears Account.
- **Calls-in-Advance** is the amount received by the company from shareholders against the calls not yet made. Calls-in-Advance is shown as Other Current Liability.
- **Interest on Calls:** *Interest on Calls-in-Arrears* may be collected by the Company from the shareholders, if its Articles of Association so provides. If the company has adopted '*Table F*' of the Companies Act, 2013, then it can charge interest @ 10% p.a. from the due date to the date of actual payment.

  Interest may be paid on Calls-in-Advance if its Articles of Association so provides. If the company has adopted '*Table F*' of the Companies Act, 2013 then it is required to pay interest @ 12% p.a. from the date of receipt to the due date.
- **Forfeiture of shares** means cancellation of shares and forfeiting the amount received against these shares. Forfeiture of shares takes place when a shareholder fails to pay the calls made.
- **Journal Entry for forfeiture of shares:**

Share Capital A/c	...Dr.	[With the amount called-up on shares forfeited]
To Forfeited Shares A/c		[With the amount already received *less* premium]
To Calls-in-Arrears A/c		[With the amount due but not paid on allotment and Calls]

  Securities Premium Reserve Account—How dealt when shares are forfeited. In case Securities Premium Reserve Account has been credited and also it has been received: Securities Premium Reserve Account is not debited because of the restrictions imposed by Section 52(2) of the Companies Act, 2013 as to utilisation.

  In case Securities Premium Reserve Account has been credited but the amount has not been received: Securities Premium Reserve Account is debited because the amount has not been received and therefore, Section 52(2) of the Companies Act, 2013 does not apply.
- **Reissue of Shares:** Forfeited shares may be reissued by the company *at par, at premium or at discount*. When such shares are reissued at a discount, the amount of discount allowed per share must not exceed the amount forfeited on such a share in respect of capital (amount received per share *minus* any premium received thereon).

Regarding Reissue of Forfeited Shares, Always Remember:

1. Discount on Reissue cannot exceed the forfeited amount.
2. If the Discount on reissue is less than the amount forfeited, the surplus (*i.e.*, gain on reissue of shares) is transferred to Capital Reserve.
3. When only a part of the forfeited shares is reissued then the gain on reissue of such shares is transferred to Capital Reserve.
4. The forfeited amount on shares not yet reissued is shown in the Balance Sheet as an addition to the share capital.
5. When the shares are reissued at Discount, such discount is debited to Forfeited Shares Account.
6. If the shares are reissued at a price which is more than the nominal (face) value of the shares, the excess amount is credited to Securities Premium Reserve Account.
7. In case the forfeited shares are reissued at a price higher than the paid-up value, the excess of issue price over paid-up value is credited to 'Securities Premium Reserve Account'.

- **In Pro rata Allotment:** When shares are reissued at a premium, excess money received on application is first be adjusted towards Share Capital and the balance, if any, is utilised towards Securities Premium Reserve.

Solved Questions

Illustration 1.

Sweetwell Co. Ltd. purchased a running business from Lotus Ltd. for ₹ 18,00,000 payable 10% by cheque and the balance by the issue of fully paid Equity Shares of ₹ 100 each at a premium of 20%. The assets and liabilities consisted of the following:

Building ₹ 9,00,000; Plant and Machinery ₹ 3,00,000; Stock ₹ 6,00,000; Trade Receivables ₹ 3,00,000; Trade Payables ₹ 2,40,000.

Pass necessary Journal entries in the books of Sweetwell Co. Ltd.

Solution: JOURNAL OF SWEETWELL CO. LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Building A/c	...Dr.		9,00,000	
	Plant and Machinery A/c	...Dr.		3,00,000	
	Stock A/c	...Dr.		6,00,000	
	Trade Receivables A/c	...Dr.		3,00,000	
	To Trade Payables A/c				2,40,000
	To Lotus Ltd.				18,00,000
	To Capital Reserve A/c (Balancing Figure)				60,000
	(Being the purchase of Business from Lotus Ltd.)				
	Lotus Ltd.	...Dr.		1,80,000	
	To Bank A/c (₹ 18,00,000 × 10/100)				1,80,000
	(Being the part payment made to vendor by cheque)				
	Lotus Ltd.	...Dr.		16,20,000	
	To Equity Share Capital A/c				13,50,000
	To Securities Premium Reserve A/c				2,70,000
	(Being the issue of 13,500 Equity Shares of ₹ 100 each at a premium of 20%)				

Note: No. of Equity Shares to be issued = ₹ 16,20,000/₹ 120 = 13,500 shares.

Illustration 2.

East Coast Ltd. purchased a running business from Ronak Ltd. for ₹ 24,00,000 payable 10% by a cheque and the balance by the issue of fully paid Equity Shares of ₹ 100 each at a premium of 20%. The assets and liabilities consisted of the following:

Building ₹ 10,40,000; Plant and Machinery ₹ 4,00,000; Stock ₹ 8,00,000; Trade Receivables ₹ 4,00,000; Trade Payables ₹ 3,20,000.

Pass necessary Journal entries in the books of East Coast Ltd.

Solution: JOURNAL OF EAST COAST LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Building A/c	...Dr.		10,40,000	
	Plant and Machinery A/c	...Dr.		4,00,000	
	Stock A/c	...Dr.		8,00,000	
	Trade Receivables A/c	...Dr.		4,00,000	
	Goodwill A/c (Balancing Figure)	...Dr.		80,000	
	To Trade Payables A/c				3,20,000
	To Ronak Ltd.				24,00,000
	(Being the purchase of Business from Ronak Ltd.)				

	Ronak Ltd. ...Dr. To Bank A/c (10% of ₹ 24,00,000) (Being the part payment made to vendor by cheque)		2,40,000	2,40,000
	Ronak Ltd. ...Dr. To Equity Share Capital A/c To Securities Premium Reserve A/c (Being the issue of 18,000 Equity Shares at 20% premium to Ronak Ltd.)		21,60,000	18,00,000 3,60,000

Note: No. of Equity Shares to be issued = ₹ 21,60,000/₹ 120 = 18,000 shares.

Illustration 3.

M/s Blue Chips Ltd. issued 2,000 shares of ₹ 100 each credited as fully paid to the promoters for their services and issued 1,000 shares of ₹ 100 each credited as fully paid to the underwriters for their underwriting services. Journalise these transactions.

Solution: JOURNAL OF M/S BLUE CHIPS LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Incorporation Costs (or Goodwill) A/c ...Dr. To Promoters' A/c (Being the amount due to promoters)		2,00,000	2,00,000
	Promoters' A/c ...Dr. To Share Capital A/c (Being the issue of 2,000 shares of ₹ 100 each to promoters)		2,00,000	2,00,000
	Underwriting Commission A/c ...Dr. To Underwriter's A/c (Being the underwriting commission due on shares)		1,00,000	1,00,000
	Underwriters' A/c ...Dr. To Share Capital A/c (Being the issue of 1,000 shares of ₹ 100 each at par to underwriters)		1,00,000	1,00,000

Illustration 4.

X Ltd. forfeited 400 shares of ₹ 10 each (₹ 8 called-up) issued at 20% premium (payable on final call) to Mr. Ashok on which he had paid ₹ 2 per share. Journalise.

Solution: JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Share Capital A/c (400 × ₹ 8) ...Dr. To Calls-in-Arrears A/c (400 × ₹ 6) To Forfeited Shares A/c (400 × ₹ 2) (Being 400 shares forfeited for non-payment of called-up amount)		3,200	2,400 800

Illustration 5.

XYZ Ltd. was incorporated with an authorised capital of 1,00,000 Equity Shares of ₹ 10 each. The directors decided to allot 10,000 shares credited as fully paid to the promoters for their services. The company also purchased Land and Building from *Y* Co. Ltd. for ₹ 4,00,000 payable in fully paid-up shares of the company. The balance of the shares were issued to the public, which were fully subscribed and paid for.

You are required to pass Journal entries and show the 'Share Capital' in the Balance Sheet of the Company as at 31st March, 2018 and also show 'Note to Accounts' as per Schedule III of the Companies Act, 2013.

Solution:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Incorporation Costs (or Goodwill) A/c	...Dr.		1,00,000	
	To Promoters' A/c				1,00,000
	(Being the amount due to promoters)				
	Promoters' A/c	...Dr.		1,00,000	
	To Equity Share Capital A/c				1,00,000
	(Being the issue of 10,000 shares of ₹ 10 each fully paid to the promoters for their services)				
	Land and Building A/c	...Dr.		4,00,000	
	To *Y* Co. Ltd.				4,00,000
	(Being the land and building purchased from *Y* Co. Ltd.)				
	Y Co. Ltd.	...Dr.		4,00,000	
	To Equity Share Capital A/c				4,00,000
	(Being the issue of 40,000 shares of ₹ 10 each to *Y* Co. Ltd. against the purchase of land and building)				
	Bank A/c	...Dr.		5,00,000	
	To Equity Shares Application and Allotment A/c				5,00,000
	(Being the Application Money received for 50,000 shares)				
	Equity Shares Application and Allotment A/c	...Dr.		5,00,000	
	To Equity Share Capital A/c				5,00,000
	(Being the allotment of 50,000 shares of ₹ 10 each)				

AN EXTRACT OF BALANCE SHEET OF *XYZ* LTD.
as at 31st March, 2018

Particulars	Note No.	Current Year (₹)	Previous Year (₹)
EQUITY AND LIABILITIES			
Shareholders' Funds			
Share Capital	1	10,00,000	

Note to Accounts

	₹
1. Share Capital	
Authorised Capital	
1,00,000 Equity Shares of ₹ 10 each	10,00,000
Issued Capital	
1,00,000 Equity Shares of ₹ 10 each	10,00,000
(Of the above, 50,000 Equity Shares have been allotted for consideration other than cash)	
Subscribed Capital	
Subscribed and fully paid-up	
1,00,000 Equity Shares of ₹ 10 each fully paid-up	10,00,000
(Of the above, 50,000 Equity Shares have been allotted for consideration other than cash)	

Illustration 6.

Advance Solutions Ltd. purchased assets from *3A* Consultants for ₹ 4,00,000. Consideration was paid by issue of 35,000 Equity Shares of ₹ 10 each at par and balance was paid by cheque. Journalise the above transactions in the books of the company.

Solution: **In the Books of Advance Solutions Ltd.**

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Sundry Assets A/c ...Dr.		4,00,000	
	To *3A* Consultants			4,00,000
	(Being the assets purchased from *3A* Consultants vide agreement dated ...)			
	3A Consultants ...Dr.		4,00,000	
	To Equity Share Capital A/c			3,50,000
	To Bank A/c			50,000
	(Being issue of 35,000 fully paid Equity Shares of ₹ 10 each issued at par and balance paid by cheque)			

Illustration 7.

Aar Kay Ltd. has authorised capital of ₹ 5,00,000 divided into 50,000 Equity Shares of ₹ 10 each. It issued 20,000 shares to the public on the following terms: ₹ 5 on application and ₹ 5 on allotment.

Applications were received for 25,000 shares on 17th July, 2017 and allotment was made on 3rd August, 2017 on which date the excess application money was refunded to the applicants who were not allotted any share. The allotment money was duly received by 31st August, 2017. Show Bank Account, Share Application Account, Share Allotment Account and Share Capital Account for the year. Also, show as to how the share capital would appear in Balance Sheet as at 31st March, 2018.

Solution: **In the Books of Aar Kay Ltd.**

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Shares Application A/c (25,000 × ₹ 5)	1,25,000	By Shares Application A/c (5,000 × ₹ 5)	25,000
To Shares Allotment A/c (20,000 × ₹ 5)	1,00,000	By Balance *c/d*	2,00,000
	2,25,000		2,25,000

Dr. SHARES APPLICATION ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Share Capital A/c	1,00,000	By Bank A/c	1,25,000
To Bank A/c	25,000		
	1,25,000		1,25,000

Dr. SHARES ALLOTMENT ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Share Capital A/c	1,00,000	By Bank A/c	1,00,000
	1,00,000		1,00,000

Dr. SHARE CAPITAL ACCOUNT Cr.

Particulars	₹	Particulars	₹
To Balance *c/d*	2,00,000	By Shares Application A/c	1,00,000
		By Shares Allotment A/c	1,00,000
	2,00,000		2,00,000
		By Balance *b/d*	2,00,000

BALANCE SHEET (EXTRACT) *as at 31st March, 2018*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Share Capital	1	2,00,000
Total		2,00,000
II. ASSETS		
Current Assets		
Cash and Bank Balances	2	2,00,000
Total		2,00,000

Notes to Accounts

	₹
1. Share Capital	
Authorised Capital	
50,000 Equity Shares of ₹ 10 each	5,00,000
Issued Capital	
20,000 Equity Shares of ₹ 10 each	2,00,000
Subscribed Capital	
Subscribed and fully paid-up	
20,000 Equity Shares of ₹ 10 each	2,00,000
2. Cash and Bank Balances	
Cash at Bank	2,00,000

Illustration 8 (*Issue of Shares at Premium, Oversubscription of Shares*).

Hightech Ltd. issued 50,000 Equity Shares of ₹ 10 each at a premium of ₹ 4 per share payable ₹ 4 on application; ₹ 8 on allotment and balance on final call.

Applications were received for 80,000 shares. Applications for 18,000 shares were rejected and the amount was refunded. Excess application money was applied towards amount due on allotment. The amounts due were received.

Pass necessary Journal entries for the above transactions.

Solution: **In the Books of Hightech Ltd.**

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr.		3,20,000	
	To Equity Shares Application A/c			3,20,000
	(Being the application money received on 80,000 shares @ ₹ 4)			
	Equity Shares Application A/c ...Dr.		3,20,000	
	To Equity Share Capital A/c			2,00,000
	To Equity Shares Allotment A/c			48,000
	To Bank A/c (18,000 × ₹ 4)			72,000
	(Being 50,000 shares allotted, excess application money adjusted towards allotment and application money on rejected applications refunded)			

	Equity Shares Allotment A/c ...Dr. To Equity Share Capital A/c To Securities Premium Reserve A/c (Being the allotment money due)		4,00,000	 2,00,000 2,00,000
	Bank A/c ...Dr. To Equity Shares Allotment A/c (Being the amount received)		3,52,000	 3,52,000
	Equity Shares First and Final Call A/c ...Dr. To Equity Share Capital A/c (Being the first and final call due)		1,00,000	 1,00,000
	Bank A/c ...Dr. To Equity Shares First and Final Call A/c (Being the amount received)		1,00,000	 1,00,000

Illustration 9 (*Forfeiture of Shares issued at Par*).

A company offered for subscription 1,00,000 shares of ₹ 10 each on the following terms: ₹ 3 payable on application, ₹ 4 on allotment, the balance as and when required.

Applications were received for 1,40,000 shares. Allotment was made as under:

80,000 applications were allotted 80,000 shares;
50,000 applications were allotted 20,000 shares;
10,000 applications were not allotted any share.

Excess application money after applying towards allotment is to be refunded.

A shareholder who applied for 1,000 shares and was given 1,000 shares failed to pay the allotment money. His shares were forfeited.

Pass Journal entries to record the above transactions.

Solution: **In the Books of ...**

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr. To Shares Application A/c (Being the application money received on 1,40,000 shares @ ₹ 3 per share)		4,20,000	 4,20,000
	Shares Application A/c ...Dr. To Share Capital A/c (1,00,000 × ₹ 3) To Shares Allotment A/c (20,000 × ₹ 4) To Bank A/c (10,000 × ₹ 3 + ₹ 10,000) (Note 1) (Being the application money adjusted and surplus refunded upon allotment)		4,20,000	 3,00,000 80,000 40,000
	Shares Allotment A/c ...Dr. To Share Capital A/c (Being the allotment money due on 1,00,000 shares @ ₹ 4 per share)		4,00,000	 4,00,000
	Bank A/c ...Dr. Calls-in-Arrears A/c ...Dr. To Shares Allotment A/c (Being the allotment money received on all shares @ ₹ 4 per share except on 1,000 shares)		3,16,000 4,000	 3,20,000
	Share Capital A/c ...Dr. To Calls-in-Arrears A/c To Forfeited Shares A/c (Being 1,000 shares forfeited for non-payment of allotment money)		7,000	 4,000 3,000

Notes:

1. Application money was received on 50,000 shares (*i.e.*, 50,000 × ₹ 3 = ₹ 1,50,000) but against these applications, 20,000 shares are allotted. Therefore, the allotment money for 20,000 shares (*i.e.*, 20,000 × ₹ 4) will be adjusted on allotment and the balance of ₹ 10,000 will be refunded, *i.e.*, ₹ 1,50,000 (Amount received) – ₹ 60,000 (Adjusted on application) – ₹ 80,000 (Adjusted on allotment).
2. Shares that have been forfeited are from first category, *i.e.*, all the applicants were allotted shares as were applied.

Illustration 10 (*Comprehensive*).

A limited company was registered with an authorised capital of ₹ 2,00,000 in ₹ 10 per share, of these 6,000 shares were issued as fully paid to the vendors for the purchase of building, 8,000 shares were subscribed for by the public and during the first year ₹ 5 per share were called-up, payable ₹ 2 on application, ₹ 1 on allotment, ₹ 1 on the first call and ₹ 1 on the second call. The amounts received in respect of these shares were as follows:

On 6,000 shares the full amount called;

On 1,250 shares ₹ 4 per share;

On 500 shares ₹ 3 per share;

On 250 shares ₹ 2 per share.

The Directors forfeited 750 shares on which less than ₹ 4 per share had been paid.

Pass Journal entries in the books of the company and also show the share capital as it would appear in Balance Sheet.

Solution:

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Building A/c	...Dr.		60,000	
	To Vendor				60,000
	(Being the building purchased)				
	Vendor	...Dr.		60,000	
	To Share Capital A/c				60,000
	(Being the issue of 6,000 shares of ₹ 10 each as fully paid in payment of building purchased)				
	Bank A/c	...Dr.		16,000	
	To Shares Application A/c				16,000
	(Being the amount received in respect of application money on 8,000 shares @ ₹ 2 per share)				
	Shares Application A/c	...Dr.		16,000	
	To Share Capital A/c				16,000
	(Being the transfer of application money to Share Capital Account upon allotment)				
	Shares Allotment A/c	...Dr.		8,000	
	To Share Capital A/c				8,000
	(Being the allotment money due on 8,000 shares @ ₹ 1 per share)				
	Bank A/c	...Dr.		7,750	
	Calls-in-Arrears A/c	...Dr.		250	
	To Shares Allotment A/c				8,000
	(Being the amount received on the allotment except on 250 shares @ ₹ 1 per share) (WN 1)				

	Shares First Call A/c ...Dr.		8,000	
	To Share Capital A/c			8,000
	(Being the amount due on first call of 8,000 shares @ ₹ 1 per share)			
	Bank A/c ...Dr.		7,250	
	Calls-in-Arrears A/c ...Dr.		750	
	To Shares First Call A/c			8,000
	(Being the amount received on the first call except on 750 shares @ ₹ 1 per share) (WN 2)			
	Shares Second Call A/c ...Dr.		8,000	
	To Share Capital A/c			8,000
	(Being the amount due on second call on 8,000 shares @ ₹ 1 per share)			
	Bank A/c ...Dr.		6,000	
	Calls-in-Arrears A/c ...Dr.		2,000	
	To Shares Second Call A/c			8,000
	(Being the amount received on the second call except on 2,000 shares @ ₹ 1 per share) (WN 3)			
	Share Capital A/c ...Dr.		3,750	
	To Forfeited Shares A/c			2,000
	To Calls-in-Arrears A/c			1,750
	(Being 750 shares forfeited) (WN 4)			

Working Notes:

1. A holder of 250 shares paid only the application money. He has not paid the allotment and call money. Therefore, the allotment money has been received on 7,750 shares (8,000 – 250) @ ₹ 1 each, *i.e.*, ₹ 7,750.
2. First call money has not been paid by the holder of 250 shares and the holder of 500 shares. In total, the first call money has not been received on 750 shares.
3. The second and final call money has not been paid by the holder of 250 shares, holder of 500 shares and holder of 1,250 shares. In total, the second call money has not been received on 2,000 shares.
4. *Amount Forfeited:*

		₹
(*i*)	For 250 shares, application money @ ₹ 2 per share	500
(*ii*)	For 500 shares, application money @ ₹ 2 per share and allotment money @ ₹ 1 per share	1,500
		2,000

BALANCE SHEET *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Share Capital	1	97,000
Total		97,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets (Tangible)	2	60,000
2. Current Assets		
Cash and Bank Balances	3	37,000
Total		97,000

Notes to Accounts

			₹
1.	**Share Capital**		
	Authorised Capital		
	20,000 Equity Shares of ₹ 10 each		2,00,000
	Issued Capital		
	14,000 Equity Shares of ₹ 10 each		1,40,000
	(Out of the above 6,000 shares have been issued as fully paid-up pursuant to a contract for consideration other than cash, *i.e.*, for purchase of building)		
	Subscribed Capital		
	Subscribed and fully paid-up		
	6,000 Equity Shares of ₹ 10 each		60,000
	(Above shares have been issued as fully paid-up pursuant to a contract for consideration other than cash, *i.e.*, for purchase of building)		
	Subscribed but not fully paid-up		
	7,250 Equity Shares of ₹ 10 each; ₹ 5 called-up	36,250	
	Less: Calls-in-Arrears	1,250	
		35,000	
	Add: Forfeited Shares A/c	2,000	37,000
			97,000
2.	**Fixed Assets (Tangible)**		
	Building		60,000
3.	**Cash and Bank Balances**		
	Cash at Bank		37,000

Illustration 11 (*Forfeiture of Shares Originally Issued at Premium and Reissued at Discount*).

A Ltd. forfeited 60 shares of ₹ 10 each issued at a premium of 20% to Ram who had applied for 72 shares, for non-payment of the allotment money of ₹ 5 per share (including premium) and the first and final call of ₹ 5 per share. Out of these 20 shares were reissued to Shyam credited as fully paid for ₹ 9 per share.

Give Journal entries to record forfeiture and reissue of shares assuming that *A* Ltd. follows the policy of adjusting excess application money towards other sums due on shares.

Solution:

In the Books of *A* Ltd.

Journal

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Share Capital A/c	...Dr.		600	
	Securities Premium Reserve A/c	...Dr.		120	
	To Forfeited Shares A/c				144
	To Calls-in-Arrears (WN 1)				576
	(Being 60 shares forfeited for non-payment of allotment money and call)				
	Bank A/c	...Dr.		180	
	Forfeited Shares A/c	...Dr.		20	
	To Share Capital A/c				200
	(Being 20 forfeited shares reissued as fully paid-up for ₹ 9 per share)				
	Forfeited Shares A/c	...Dr.		28	
	To Capital Reserve A/c (WN 2)				28
	(Being the gain on reissue transferred to Capital Reserve)				

Working Notes:

1. *Amount of Calls-in-Arrears:*

(*a*)	No. of shares applied by Ram	72
(*b*)	Money paid on application (72 × ₹ 2)	₹ 144
(*c*)	Excess application money [₹ 144 – (60 × ₹ 2)]	₹ 24
(*d*)	Amount due on allotment (60 × ₹ 5)	₹ 300
(*e*)	Amount not paid by Ram (₹ 300 – ₹ 24)	₹ 276

2. *Amount transferred to Capital Reserve:*

Amount forfeited on 60 shares = ₹ 144	
∴ Amount forfeited on 20 shares = ₹ 144 × 20/60	₹ 48
Less: Discount allowed on 20 shares reissued	₹ 20
Gain (Profit) transferred to the Capital Reserve	₹ 28

Illustration 12.

Fortunate Limited issued 10,000 Equity Shares of ₹ 100 each. The amount was payable as under:

On application	₹ 20;	On first call	₹ 25;
On allotment	₹ 30;	On second call	₹ 25.

The company received applications for 10,000 Equity Shares. The company allotted the shares. The Directors made both the calls.

Mr. Unlucky holding 100 shares did not pay both the calls whereas Mr. Unsuccessful holding 40 shares did not pay the second call.

The Directors forfeited the shares on which both the calls were not paid. They were reissued as fully paid @ ₹ 75 per share.

Record the transactions in the Journal of the company. Also, show relevant items as they would appear in the Balance Sheet of the company.

Solution:

In the Books of Fortunate Limited

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c (10,000 × ₹ 20) ...Dr.		2,00,000	
	To Equity Shares Application A/c			2,00,000
	(Being the application money received on 10,000 shares)			
	Equity Shares Application A/c ...Dr.		2,00,000	
	To Equity Share Capital A/c			2,00,000
	(Being the application money transferred to Equity Share Capital Account on allotment of shares)			
	Equity Shares Allotment A/c ...Dr.		3,00,000	
	To Equity Share Capital A/c			3,00,000
	(Being the allotment money due)			
	Bank A/c (10,000 × ₹ 30) ...Dr.		3,00,000	
	To Equity Shares Allotment A/c			3,00,000
	(Being the allotment money received)			

	Equity Shares First Call A/c ...Dr.		2,50,000	
	To Equity Share Capital A/c			2,50,000
	(Being the first call money due on 10,000 shares)			
	Bank A/c [₹ 2,50,000 – (₹ 25 × 100)] ...Dr.		2,47,500	
	Calls-in-Arrears A/c ...Dr.		2,500	
	To Equity Share Capital A/c			2,50,000
	(Being the first call money received on 9,900 shares)			
	Equity Shares Second and Final Call A/c ...Dr.		2,50,000	
	To Equity Share Capital A/c			2,50,000
	(Being the second call money due on 10,000 shares)			
	Bank A/c [(₹ 2,50,000 – (₹ 25 × 140)] ...Dr.		2,46,500	
	Calls-in-Arrears A/c ...Dr.		3,500	
	To Equity Shares Second and Final Call A/c			2,50,000
	(Being the second call money received except on 140 shares)			
	Equity Share Capital A/c (100 × ₹ 100) ...Dr.		10,000	
	To Calls-in-Arrears A/c (100 × ₹ 50)			5,000
	To Forfeited Shares A/c (100 × ₹ 50)			5,000
	(Being 100 shares of Mr. Unlucky forfeited for non-payment of first and second and final calls)			
	Bank A/c (100 × ₹ 75) ...Dr.		7,500	
	Forfeited Shares A/c (100 × ₹ 25) ...Dr.		2,500	
	To Equity Share Capital A/c			10,000
	(Being the reissue of 100 forfeited shares as fully paid-up @ ₹ 75 per share)			
	Forfeited Shares A/c (₹ 5,000 – ₹ 2,500) ...Dr.		2,500	
	To Capital Reserve A/c			2,500
	(Being the gain on reissue of shares transferred to Capital Reserve)			

BALANCE SHEET *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
(*a*) Share Capital	1	9,99,000
(*b*) Reserves and Surplus	2	2,500
Total		10,01,500
II. ASSETS		
Current Assets		
Cash and Bank Balances	3	10,01,500
Total		10,01,500

Notes to Accounts

		₹
1. Share Capital		
Authorised Capital		
... Equity Shares of ₹ 100 each		...
Issued Capital		
10,000 Equity Shares of ₹ 100 each		10,00,000
Subscribed Capital		
Subscribed and fully paid-up		
9,960 Equity Shares of ₹ 100 each		9,96,000
Subscribed but not fully paid-up		
40 Equity Shares of ₹ 100 each	4,000	
Less: Calls-in-Arrears (40 × ₹ 25)	1,000	3,000
		9,99,000
2. Reserves and Surplus		
Capital Reserve		2,500
3. Cash and Bank Balances		
Cash at Bank		10,01,500

Illustration 13.

PQR & Co. Ltd., with authorised capital of 1,00,000 Equity Shares of ₹ 10 each, made a public issue of 80,000 Equity Shares at a premium of ₹ 3 per share payable ₹ 2 on application, ₹ 5 on allotment (including premium), ₹ 3 on the first call and the balance after some time.

Applications were received for 1,00,000 shares. The Board of Directors decided to refund the excess application money and thereafter allot the remaining shares.

During allotment, Mr. *M* holding 1,000 shares failed to pay the allotment money while Mr. *N* holding 2,000 shares paid the entire amount due up to the second and the final call.

Thereafter, the first call was made and after giving a sufficient notice to Mr. *M*, the company decided to forfeit his shares and subsequently reissued 800 of the forfeited shares to Mr. *O* @ ₹ 11 each fully paid-up @ ₹ 13 each.

You are required to Journalise the above issue of shares through Calls-in-Arrears Account and the Calls-in-Advance Account along with other entries in the books of *PQR* & Co. Ltd.

Solution: JOURNAL OF *PQR* & CO. LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c (1,00,000 × ₹ 2) ...Dr.		2,00,000	
	To Equity Shares Application A/c			2,00,000
	(Being the application money received for 1,00,000 shares @ ₹ 2 per share)			
	Equity Shares Application A/c ...Dr.		2,00,000	
	To Equity Share Capital A/c (80,000 × ₹ 2)			1,60,000
	To Bank A/c (20,000 × ₹ 2)			40,000
	(Being the application money received on 80,000 shares transferred to Equity Share Capital A/c on allotment of shares and that on 20,000 shares returned)			

	Equity Shares Allotment A/c (80,000 × ₹ 5) ...Dr.		4,00,000	
	To Equity Share Capital A/c (80,000 × ₹ 2)			1,60,000
	To Securities Premium Reserve A/c (80,000 × ₹ 3)			2,40,000
	(Being the allotment money due on 80,000 shares @ ₹ 5 per share including ₹ 3 being premium)			
	Bank A/c ...Dr.		4,07,000	
	Calls-in-Arrears A/c (1,000 × ₹ 5) ...Dr.		5,000	
	To Equity Shares Allotment A/c			4,00,000
	To Calls-in-Advance A/c (2,000 × ₹ 6)			12,000
	(Being the allotment money received on 79,000 shares and Calls-in-Advance received on 2,000 shares, arrear on 1,000 shares being transferred to Calls-in-Arrears Account)			
	Equity Shares First Call A/c (80,000 × ₹ 3) ...Dr.		2,40,000	
	To Equity Share Capital A/c			2,40,000
	(Being the first call money of ₹ 3 per share due on 80,000 shares)			
	Bank A/c (77,000 × ₹ 3) ...Dr.		2,31,000	
	Calls-in-Advance A/c (2,000 × ₹ 3) ...Dr.		6,000	
	Calls-in-Arrears A/c (1,000 × ₹ 3) ...Dr.		3,000	
	To Equity Shares First Call A/c			2,40,000
	(Being the first call money received on 77,000 shares and Calls-in-Advance adjusted on 2,000 shares, arrear on 1,000 shares being transferred to Calls-in-Arrears Account)			
	Equity Share Capital A/c (1,000 × ₹ 7) ...Dr.		7,000	
	Securities Premium Reserve A/c (1,000 × ₹ 3) ...Dr.		3,000	
	To Calls-in-Arrears A/c (₹ 5,000 + ₹ 3,000)			8,000
	To Forfeited Shares A/c (1,000 × ₹ 2)			2,000
	(Being the forfeiture of 1,000 shares for non-payment of allotment and call money)			
	Bank A/c (800 × ₹ 11) ...Dr.		8,800	
	Forfeited Shares A/c (800 × ₹ 2) ...Dr.		1,600	
	To Equity Share Capital A/c (800 × ₹ 10)			8,000
	To Securities Premium Reserve A/c (800 × ₹ 3)			2,400
	(Being the reissue of 800 forfeited shares @ ₹ 11 each considered as fully paid-up @ ₹ 13 each)			

Note: There is no gain on reissue of the forfeited shares as shown below:

	₹
Amount forfeited on 800 shares (800 × ₹ 2)	1,600
Less: Applied towards reissue (800 × ₹ 2)	1,600
	Nil

Therefore, nothing has been transferred to Capital Reserve.

Illustration 14.

Daksh Ltd. invited applications for 50,000 equity shares of ₹ 20 each at a premium of ₹ 4 per share payable as follows:

On application	—	₹ 5 per share;
On allotment	—	₹ 9 per share, (including premium);
On first call	—	₹ 5 per share;
On final call	—	₹ 5 per share.

Applications were received for 75,000 shares and shares were allotted on *pro rata* basis to the applicants for 60,000 shares and remaining applications were rejected. Excess money paid on application was adjusted against sum due on allotment.

A, who was allotted 100 shares, could not pay the sum due on allotment. Shares held by him were forfeited on his failure to pay the first call, *B*, holding 150 shares, could not pay two calls. The company forfeited his shares after the final call was made. Of the shares forfeited, 200 shares were sold to Ajay credited as fully paid at ₹ 16 per share, all of *A*'s forfeited shares being included.

Pass the necessary Journal entries to record the above transactions and prepare the Balance Sheet.

Solution: **In the Books of Daksh Ltd.**

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c (75,000 × ₹ 5)	...Dr.		3,75,000	
	To Equity Shares Application A/c				3,75,000
	(Being the application money received)				
	Equity Shares Application A/c	...Dr.		3,75,000	
	To Equity Share Capital A/c (50,000 × ₹ 5)				2,50,000
	To Equity Shares Allotment A/c (10,000 × ₹ 5)				50,000
	To Bank A/c (15,000 × ₹ 5)				75,000
	(Being the application money adjusted and surplus refunded)				
	Equity Shares Allotment A/c (50,000 × ₹ 9)	...Dr.		4,50,000	
	To Equity Share Capital A/c (50,000 × ₹ 5)				2,50,000
	To Securities Premium Reserve A/c (50,000 × ₹ 4)				2,00,000
	(Being the allotment money due)				
	Bank A/c (WN 3)	...Dr.		3,99,200	
	Calls-in-Arrears A/c (WN 1)	...Dr.		800	
	To Equity Shares Allotment A/c				4,00,000
	(Being the allotment money received except on 100 shares)				
	Equity Shares First Call A/c (50,000 × ₹ 5)	...Dr.		2,50,000	
	To Equity Share Capital A/c				2,50,000
	(Being the first call money due)				

Bank A/c (49,750 × ₹ 5) ...Dr.		2,48,750	
Calls-in-Arrears A/c (250 × ₹ 5) ...Dr.		1,250	
To Equity Shares First Call A/c			2,50,000
(Being the first and final call money received except on 250 shares)			
Equity Share Capital A/c (100 × ₹ 15) ...Dr.		1,500	
Securities Premium Reserve A/c (100 × ₹ 4) ...Dr.		400	
To Forfeited Shares A/c			600
To Calls-in-Arrears A/c (₹ 800 + ₹ 500)			1,300
(Being 100 shares forfeited for non-payment of allotment and first call money)			
Equity Shares Second and Final Call A/c (49,900 × ₹ 5) ...Dr.		2,49,500	
To Equity Share Capital A/c			2,49,500
(Being the second and final call money due)			
Bank A/c (49,750 × ₹ 5) ...Dr.		2,48,750	
Calls-in-Arrears A/c (150 × ₹ 5) ...Dr.		750	
To Equity Shares Second and Final Call A/c			2,49,500
(Being the second and final call money received on 49,750 shares @ ₹ 5 per share)			
Equity Share Capital A/c (150 × ₹ 20) ...Dr.		3,000	
To Calls-in-Arrears A/c (₹ 750 + ₹ 750)			1,500
To Forfeited Shares A/c (₹ 750 + ₹ 750)			1,500
(Being 150 shares forfeited for non-payment of both the calls)			
Bank A/c (200 × ₹ 16) ...Dr.		3,200	
Forfeited Shares A/c (200 × ₹ 4) ...Dr.		800	
To Equity Share Capital A/c			4,000
(Being the reissue of 200 equity shares credited as fully paid at ₹ 16 per share)			
Forfeited Shares A/c ...Dr.		800	
To Capital Reserve A/c			800
(Being the gain on reissue of 200 shares transferred to Capital Reserve)			

BALANCE SHEET OF DAKSH LTD.
as at ...

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
(*a*) Share Capital	1	9,99,500
(*b*) Reserves and Surplus	2	2,00,400
Total		11,99,900
II. ASSETS		
Current Assets		
Cash and Bank Balances	3	11,99,900

Notes to Accounts

			₹
1.	**Share Capital**		
	Authorised Capital		
	... Equity Shares of ₹ 20 each		...
	Issued Capital		
	50,000 Equity Share of ₹ 20 each		10,00,000
	Subscribed Capital		
	Subscribed and Fully paid-up		
	49,950 Equity Shares of ₹ 20 each	9,99,000	
	Add: Forfeited Shares Account (₹ 600 + ₹ 1,500 – ₹ 800 – ₹ 800)	500	9,99,500
2.	**Reserves and Surplus**		
	Capital Reserve (WN 4)	800	
	Securities Premium Reserve (₹ 2,00,000 – ₹ 400)	1,99,600	2,00,400
3.	**Cash and Bank Balances**		
	Cash at Bank (₹ 3,75,000 – ₹ 75,000 + ₹ 3,99,200 + ₹ 2,48,750 + ₹ 2,48,750 + ₹ 3,200)		11,99,900

Working Notes:

1. *Calculation of Excess Application Money Received from A:*

   Number of Shares Allotted = 100 shares

   Number of Shares Applied by *A* $\left[\frac{1,20,000}{1,00,000} \times 200\right]$ = 120 shares

   Excess Application Money to be adjusted on Allotment = [(120 – 100) × ₹ 5] = ₹ 100.

2. *Calculation of Amount due from A on Allotment:*

	₹
Total Amount due on Allotment from *A* (100 × ₹ 9)	900
Less: Excess Application Money to be adjusted (WN 1)	100
Net Amount due from *A* on Allotment which was not Received	800

3. *Calculation of Amount Received on Allotment:*

	₹
Total Amount due on Allotment (50,000 × ₹ 9)	4,50,000
Less: Excess Application Money Adjusted	50,000
	4,00,000
Less: Amount not Received from *A* (WN 2)	800
Amount Received on Allotment	3,99,200

4. *Calculation of Amount Transferred to Capital Reserve:*

	₹
Amount Forfeited on 100 Shares of A	600
Add: Amount Forfeited on 100 Shares of B (₹ 1,500/150 × 100)	1,000
	1,600
Less: Discount Allowed on Reissue	800
Gain on Reissue to be transferred to Capital Reserve	800

Master Questions and Advanced Level Questions

Illustration 15.

Pee Kay Ltd. issued 2,00,000 shares of ₹ 10 each at a premium of 20% to public for subscription payable as follows:

On application	₹ 3;
On allotment	₹ 3;
On first call	₹ 3 (including ₹ 1 as premium); and
On second and final call	₹ 3 (including ₹ 1 as premium).

Applications were received for 5,00,000 shares. The company allotted shares to all the applicants on *pro rata* basis and retained the excess application money towards allotment and calls. The company received the amounts due on due dates except from Dinesh holding 200 shares who failed to pay the two calls. His shares were subsequently forfeited. Out of the forfeited shares, 150 shares were reissued for ₹ 13 credited as fully paid-up.

Pass the Journal entries and draw the Balance Sheet having share capital.

Solution: JOURNAL OF PEE KAY LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	...Dr.		15,00,000	
	To Shares Application A/c				15,00,000
	(Being the application money received for 5,00,000 shares @ ₹ 3)				
	Shares Application A/c	...Dr.		15,00,000	
	To Share Capital A/c				6,00,000
	To Shares Allotment A/c				6,00,000
	To Calls-in-Advance A/c				3,00,000
	(Being the shares allotted on *pro rata* to all the applicants and excess money adjusted)				
	Shares Allotment A/c	...Dr.		6,00,000	
	To Share Capital A/c				6,00,000
	(Being the allotment money due on 2,00,000 shares @ ₹ 3)				
	Shares First Call A/c	...Dr.		6,00,000	
	To Share Capital A/c				4,00,000
	To Securities Premium Reserve A/c				2,00,000
	(Being the first call due on 2,00,000 shares @ ₹ 3 per share including securities premium of ₹ 1 per share)				
	Bank A/c (WN 1)	...Dr.		2,99,700	
	Calls-in-Advance A/c	...Dr		3,00,000	
	Calls-in Arrears A/c (WN 2)	...Dr.		300	
	To Shares First Call A/c				6,00,000
	(Being the amount adjusted from Calls-in-Advance and balance received except on 200 shares)				
	Shares Second and Final Call A/c	...Dr.		6,00,000	
	To Share Capital A/c				4,00,000
	To Securities Premium Reserve A/c				2,00,000
	(Being the second and final call due, including ₹ 1 per share towards securities premium)				

	Bank A/c ...Dr.		5,99,400	
	Calls-in-Arrears A/c ...Dr.		600	
	To Shares Second and Final Call A/c			6,00,000
	(Being the second and final call money received except on 200 shares)			
	Share Capital A/c ...Dr.		2,000	
	Securities Premium Reserve A/c ...Dr.		400	
	To Forfeited Shares A/c			1,500
	To Calls-in-Arrears A/c			900
	(Being 200 shares forfeited for non-payment of first call and second and final call, including premium (WN 3))			
	Bank A/c ...Dr.		1,950	
	To Share Capital A/c			1,500
	To Securities Premium Reserve A/c			450
	(Being 150 shares out of 200 forfeited shares issued @ ₹ 13 per share)			
	Forfeited Shares A/c ...Dr.		1,125	
	To Capital Reserve A/c			1,125
	(Being the amount forfeited on 150 reissued shares transferred to Capital Reserve)			

BALANCE SHEET *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Share Capital	1	19,99,875

Note to Accounts

1. Share Capital	₹
Authorised Capital	
... Shares of ₹ 10 each	...
Issued Capital	
2,00,000 Shares of ₹ 10 each	20,00,000
Subscribed Capital	
Subscribed and fully paid-up	
1,99,950 Shares of ₹ 10 each	19,99,500
Add: Forfeited Shares A/c	375
	19,99,875

Working Notes:

1. *Total Amount received towards First Call:*	Share Capital (₹)	Securities Premium (₹)
Total amount due	4,00,000	2,00,000
Less: Amount adjusted from Calls-in-Advance	3,00,000	...
	1,00,000	2,00,000
Less: Amount not received from Dinesh	100	200
	99,900	1,99,800

Total Amount Received = ₹ 2,99,700.

2. *Calls-in-Arrears:*

Amount received from Dinesh on application:

	₹
$\frac{200}{2,00,000} \times 5,00,000 = 500 \times ₹\ 3$	1,500
Less: Amount adjusted on application (200 × ₹ 3)	600
	900
Less: Amount adjusted on allotment (200 × ₹ 3)	600
Balance of Calls-in-Advance	300

Amount due from Dinesh on First call:

	Share Capital (₹)	Securities Premium (₹)
(200 × ₹ 2) + (200 × ₹ 1)	400	200
Less: Adjusted from Calls-in-Advance	300	...
Amount not received	100	200

3. *Amount forfeited on Shares allotted to Dinesh:*

$$\frac{200}{2,00,000} \times 5,00,000 \times ₹\ 3 = ₹\ 1,500.$$

Illustration 16.

Gee Kay Ltd. issued 1,00,000 shares of ₹ 10 each at a premium of ₹ 2 per share to public for subscription payable as follows:

On application	₹ 4;
On allotment	₹ 5 (including premium); and
On first and final call	Balance.

It received applications for 1,70,000 shares. It allotted shares on *pro rata* basis to applicants of 1,50,000 shares and sent letter of regret to applicants for 20,000 shares along with refund. Anil, to whom 1,000 shares were allotted, failed to pay allotment money and call money on due dates but paid the amount along with interest of ₹ 300 on receiving notice of forfeiture. Amit, to whom 2,000 shares were allotted, failed to pay allotment money and call money in spite of receiving the notice of forfeiture. His shares were forfeited.

Alok, to whom 3,000 shares were allotted, paid call money along with the allotment money. He was paid interest of ₹ 300 on Calls-in-Advance.

Out of the forfeited shares, 1,000 shares were reissued at ₹ 9 as fully paid-up.

Pass necessary Journal entries and draw the Balance Sheet of the company showing Shareholders' Funds.

Solution: JOURNAL OF GEE KAY LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	...Dr.		6,80,000	
	To Shares Application A/c				6,80,000
	(Being the applications received for 1,70,000 shares)				
	Shares Application A/c	...Dr.		6,80,000	
	To Share Capital A/c				4,00,000
	To Shares Allotment A/c				2,00,000
	To Bank A/c				80,000
	(Being the shares allotted and application money adjusted)				

Shares Allotment A/c	...Dr.	5,00,000	
To Share Capital A/c			3,00,000
To Securities Premium Reserve A/c			2,00,000
(Being the allotment money due including premium of ₹ 2 per share)			
Bank A/c (WN 2)	...Dr.	3,00,000	
Calls-in-Arrears A/c (WN 1 (i), (ii))	...Dr.	9,000	
To Shares Allotment A/c			3,00,000
To Calls-in-Advance A/c			9,000
(Being the Calls-in-Advance adjusted and balance received except on 1,000 shares)			
Shares First and Final Call A/c	...Dr.	3,00,000	
To Share Capital A/c			3,00,000
(Being the first and final call money due)			
Bank A/c (WN)	...Dr.	2,82,000	
Calls-in-Arrears A/c (WN 4)	...Dr.	9,000	
Calls-in-Advance A/c	...Dr.	9,000	
To Shares First and Final Call A/c			3,00,000
(Being the amount due on first and final call adjusted and balance amount received except on 3,000 shares)			
Bank A/c (WN 5)	...Dr.	6,300	
To Calls-in-Arrears A/c			6,000
To Interest on Calls-in-Arrears A/c			300
(Being the due amount received from Anil on 1,000 shares along with interest)			
Share Capital A/c (2,000 × ₹ 10)	...Dr.	20,000	
Securities Premium Reserve A/c	...Dr.	4,000	
To Forfeited Shares A/c			12,000
To Calls-in-Arrears A/c			12,000
(Being 2,000 shares of Amit forfeited)			
Bank A/c	...Dr.	9,000	
Forfeited Shares A/c	...Dr.	1,000	
To Share Capital A/c			10,000
(Being 1,000 shares out of 2,000 forfeited shares reissued)			
Forfeited Shares A/c	...Dr.	5,000	
To Capital Reserve A/c			5,000
(Being the gain on 1,000 reissued shares transferred to Capital Reserve)			
Interest on Calls-in-Advance A/c	...Dr.	300	
To Bank A/c			300
(Being the interest paid on Calls-in-Advance)			

BALANCE SHEET OF GEE KAY LTD. *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Share Capital	1	9,96,000
Reserves and Surplus	2	2,01,000
		11,97,000

Notes to Accounts

	₹
1. Share Capital	
Authorised Capital	
... Shares of ₹ 10 each	...
Issued Capital	
1,00,000 Shares of ₹ 10 each	10,00,000
Subscribed Capital	
Subscribed and fully paid-up	
99,000 Shares of ₹ 10 each	9,90,000
Add: Forfeited Shares A/c	6,000
	9,96,000
2. Reserves and Surplus	
Capital Reserve	5,000
Securities Premium Reserve (WN 8)	1,96,000
	2,01,000

Working Notes:

1. (*i*) *Shares applied by Anil and Shares Application money paid and adjusted:*

Shares allotted = 1,000

$$\therefore \quad \text{Shares applied} = \frac{1,000}{1,00,000} \times 1,50,000 = 1,500$$

	₹
Application money paid (1,500 × ₹ 4)	6,000
Less: Adjusted against share application (1,000 × ₹ 4)	4,000
Balance to be adjusted against allotment money	2,000
Amount due from Anil on allotment (1,000 × ₹ 5)	5,000
Less: Balance to be adjusted against allotment money	2,000
Balance not received on allotment	3,000
Comprising: Share Capital	1,000
Securities Premium Reserve	2,000

(*ii*) *Shares applied by Amit and application money paid and adjusted:*

Shares allotted = 2,000

$$\therefore \quad \text{Shares applied} = \frac{2,000}{1,00,000} \times 1,50,000 = 3,000$$

	₹
Application money paid (3,000 × ₹ 4)	12,000
Less: Adjusted against share application (2,000 × ₹ 4)	8,000
Balance to be adjusted against allotment	4,000
Amount due from Amit on allotment (2,000 × ₹ 5)	10,000
Less: Balance to adjusted against allotment	4,000
Amount not received on allotment	6,000
Comprising: Share Capital	2,000
Securities Premium Reserve	4,000
	6,000

(*iii*) *Amount paid by Alok on allotment:*

Shares allotted = 3,000

$\therefore$ Shares applied = $\frac{3,000}{1,00,000} \times 1,50,000 = 4,500$

	₹
Amount paid on application (4,500 × ₹ 4)	18,000
Less: Adjusted against shares application (3,000 × ₹ 4)	12,000
Balance to be adjusted against allotment	6,000
Amount due from Alok on allotment (3,000 × ₹ 5)	15,000
Less: Balance to be adjusted against allotment	6,000
	9,000
Add: Amount due on first and final call (3,000 × ₹ 3)	9,000
Amount received	18,000

2. *Amount received on allotment:*

	₹
Amount due (1,00,000 × ₹ 5)	5,00,000
Less: Adjusted against shares application	2,00,000
	3,00,000
Less: Calls-in-Arrears	9,000
	2,91,000
Add: Received in Advance from Alok	9,000
	3,00,000

3. *Amount received at the time of first and final call:*

	₹	₹
Amount due		3,00,000
Less: Calls-in-Arrears	9,000	
Calls-in-Advance	9,000	18,000
		2,82,000

4. *Calls-in-Arrears on first and final call:*

	₹
Due from Anil on 1,000 shares	3,000
Due from Amit on 2,000 shares	6,000
	9,000

5. *Amount received from Anil:*

	₹
Amount due on allotment	3,000
Amount due on first and final call	3,000
Interest	300
	6,300

6. *Dr.* CALLS-IN-ARREARS ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
	To Shares Allotment A/c (Anil and Amit)	9,000		By Bank A/c (Anil)	6,000
	To Shares First and Final Call A/c (Anil and Amit)	9,000		By Share Capital A/c (Amit)	12,000
		18,000			18,000

7. *Dr.* CALLS-IN-ADVANCE ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
	To Shares First and Final Call A/c (Alok)	9,000		By Bank A/c (Alok)	9,000
		9,000			9,000

8. *Dr.* SECURITIES PREMIUM RESERVE ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
	To Calls-in-Arrears A/c	4,000		By Shares Allotment A/c	2,00,000
	To Balance *c/d*	1,96,000			
		2,00,000			2,00,000

Illustration 17.

Zenon Ltd. issued 3,00,000 shares of ₹ 10 each at a premium of ₹ 4 per share, payable as under:

On application	₹ 3 (including ₹ 1 premium);
On allotment	₹ 4 (including ₹ 1 premium);
On first call	₹ 4 (including ₹ 1 premium);
On second and final call	₹ 3 (including balance premium).

Applications were received for 3,80,000 shares, allotment was made on *pro rata* basis to the applicants for 3,50,000 shares, the remaining applications being refused. The money overpaid on applications was utilised towards sum due on allotment.

Honey, to whom 6,000 shares were allotted, failed to pay the allotment money and his shares were forfeited after allotment. Khushal, who applied for 10,500 shares, failed to pay the two calls and on his such failure, his shares were also forfeited. Sukmani to whom 3,000 shares were allotted failed to pay the final call.

Of the shares forfeited, 11,000 shares were reissued as fully paid-up for ₹ 9 per share, the whole of Khushal's shares being included.

Prepare Cash Book, Journal and Balance Sheet.

Solution:

In the Books of Zenon Ltd.

Dr. CASH BOOK (BANK COLUMN ONLY) *Cr.*

Particulars	₹	Particulars	₹
To Shares Application A/c (3,80,000 shares × ₹ 3)	11,40,000	By Shares Application A/c (30,000 shares × ₹ 3)	90,000
To Shares Allotment A/c (WN 1)	10,29,000	By Balance *c/d*	41,64,000
To Shares First Call A/c (WN 2) (2,85,000 shares × ₹ 4)	11,40,000		
To Shares Second and Final Call A/c (2,82,000 shares × ₹ 3) (WN 2)	8,46,000		
To Share Capital A/c	99,000		
	42,54,000		42,54,000

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Shares Application A/c	...Dr.		10,50,000	
	To Share Capital A/c (3,00,000 shares × ₹ 2)				6,00,000
	To Securities Premium Reserve A/c (3,00,000 shares × ₹ 1)				3,00,000
	To Shares Allotment A/c (50,000 shares × ₹ 3)				1,50,000
	(Being the application money adjusted on allotment)				
	Shares Allotment A/c	...Dr.		12,00,000	
	To Share Capital A/c				9,00,000
	To Securities Premium Reserve A/c				3,00,000
	(Being the allotment money made due on 3,00,000 shares)				
	Calls-in-Arrears A/c	...Dr.		21,000	
	To Shares Allotment A/c				21,000
	(Being the allotment money not received transferred to Calls-in-Arrears Account)				
	Share Capital A/c (6,000 shares × ₹ 5)	...Dr.		30,000	
	Securities Premium Reserve A/c (6,000 shares × ₹ 1 due on allotment)	...Dr.		6,000	
	To Calls-in-Arrears A/c				21,000
	To Forfeited Shares A/c				15,000
	(Being the forfeiture of 6,000 shares of Honey for non-payment of allotment money)				
	Shares First Call A/c	...Dr.		11,76,000	
	To Share Capital A/c				8,82,000
	To Securities Premium Reserve A/c				2,94,000
	(Being the first call due on 2,94,000 shares)				
	Calls-in-Arrears A/c	...Dr.		36,000	
	To Shares First Call A/c				36,000
	(Being the first call money not received trfd. to Calls-in-Arrears Account)				
	Shares Second and Final Call A/c	...Dr.		8,82,000	
	To Share Capital A/c				5,88,000
	To Securities Premium Reserve A/c				2,94,000
	(Being the second and final call due on 2,94,000 shares)				
	Calls-in-Arrears A/c	...Dr.		36,000	
	To Shares Second and Final Call A/c				36,000
	(Being the second and final call not received transferred to Calls-in-Arrears Account)				
	Share Capital A/c	...Dr.		90,000	
	Securities Premium Reserve A/c	...Dr.		18,000	
	To Calls-in-Arrears A/c				63,000
	To Forfeited Shares A/c				45,000
	(Being the forfeiture of 9,000 shares of Khushal for non-payment of calls)				
	Forfeited Shares A/c	...Dr.		11,000	
	To Share Capital A/c				11,000
	(Being the loss of ₹ 1 per share on the reissue of 11,000 shares)				
	Forfeited Shares A/c	...Dr.		39,000	
	To Capital Reserve A/c				39,000
	(Being the gain on 11,000 reissued shares transferred to Capital Reserve) (WN 3)				

BALANCE SHEET OF ZENON LTD. *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
(*a*) Share Capital	1	29,61,000
(*b*) Reserves and Surplus	2	12,03,000
Total		41,64,000
II. ASSETS		
Current Assets		
Cash and Bank Balances	3	41,64,000
Total		41,64,000

Notes to Accounts

	₹	₹
1. Share Capital		
Authorised Capital		
... Equity Shares of ₹ 10 each		...
Issued Capital		
3,00,000 Equity Shares of ₹ 10 each		30,00,000
Subscribed Capital		
Subscribed and fully paid-up		
2,93,000 Equity Shares of ₹ 10 each		29,30,000
Subscribed but not fully paid-up		
3,000 Equity Shares of ₹ 10 each	30,000	
Less: Calls-in-Arrears	9,000	21,000
Add: Forfeited Shares A/c (WN 4)		10,000
		29,61,000
2. Reserves and Surplus		
Capital Reserve		39,000
Securities Premium Reserve		11,64,000
		12,03,000
3. Cash and Bank Balances		
Cash at Bank		41,64,000

Working Notes:

1. (*i*) *The excess amount received from Honey on application:*

Honey has been allotted 6,000 shares.

Therefore, he must have applied for $\frac{3,50,000}{3,00,000} \times 6,000 = 7,000$ shares.

The excess application money received from Honey:
7,000 shares − 6,000 shares = 1,000 shares × ₹ 3 = ₹ **3,000**.

(*ii*) *Amount not received from Honey on Allotment:*

	₹
Allotment money due on 6,000 shares @ ₹ 4	24,000
Less: Excess money received from Honey on application	3,000
The allotment money not received from Honey	**21,000**

(*iii*) *Net amount received on Allotment:*

Allotment money due on 3,00,000 shares @ ₹ 4	12,00,000
Less: The excess amount received on application	1,50,000
Balance due	10,50,000
Less: Amount not received from Honey on allotment	21,000
Net amount received on allotment in cash	**10,29,000**

2. Khushal applied for 10,500 shares.

   Therefore, he must have been allotted $\frac{3,50,000}{3,00,000} \times 10,500 = 9,000$ shares. He has not paid the first and the second call money. As such,

   (*a*) the first call money will be received on

   2,85,000 shares [3,00,000 – 6,000 (Honey) – 9,000 (Khushal)], and

   (*b*) the second call money will be received on 2,82,000 shares.

   [*i.e.,* 3,00,000 – 6,000 (Honey) – 9,000 (Khushal) – 3,000 (Sukmani)]

3. 11,000 shares have been reissued which include 9,000 shares of Khushal and the balance 2,000 shares of Honey.

	₹
Amount forfeited on 2,000 shares of Honey = $\frac{₹\,15,000}{6,000} \times 2,000$	5,000
Amount forfeited on 9,000 shares of Khushal	45,000
Total amount forfeited on 11,000 reissued shares	50,000
Less: Reissue discount	11,000
Gain on reissue to be transferred to Capital Reserve	**39,000**

4. Amount forfeited on 6,000 shares of Honey = ₹ 15,000
   Therefore, the balance of Forfeited Shares Account on 4,000 unissued shares

$$= \frac{₹\,15,000}{6,000} \times 4,000 = ₹\ \mathbf{10,000}.$$

Illustration 18.

Reliable Investments issued a prospectus inviting applications for 4,000 Equity Shares of ₹ 20 each at a Premium of ₹ 4 per share payable as under:

On application	₹ 4 per share;
On allotment	₹ 10 per share (including Premium);
On first call	₹ 6 per share;
On second call	₹ 4 per share.

Applications were received for 6,000 shares and allotment was made on *pro rata* basis to the applicants of 4,800 shares, the applications for the remaining shares were refused. The money overpaid on application was used on account of sums due on allotment.

Harish to whom 80 shares were allotted, could not pay the allotment money and on his subsequent failure to pay the first call, his shares were forfeited after the first call.

Mukesh to whom 120 shares were allotted, failed to pay the two calls and his shares were forfeited after the second call.

Of the shares forfeited, 160 shares were sold to Suresh credited as fully paid @ ₹ 18 per share, all of Harish's forfeited shares being included.

Pass Journal entries in the books of the company to record the above transactions.

Solution:

JOURNAL OF RELIABLE INVESTMENTS

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr.		24,000	
	To Shares Application A/c			24,000
	(Being the application money received for 6,000 shares @ ₹ 4 per share)			
	Shares Application A/c ...Dr.		24,000	
	To Share Capital A/c (4,000 × ₹ 4)			16,000
	To Shares Allotment A/c (800 × ₹ 4)			3,200
	To Bank A/c (1,200 × ₹ 4)			4,800
	(Being the shares allotted on *pro rata* to all the applicants and excess money adjusted)			

	Shares Allotment A/c (4,000 × ₹ 10) ...Dr. To Share Capital A/c (4,000 × ₹ 6) To Securities Premium Reserve A/c (4,000 × ₹ 4) (Being the allotment due on 4,000 shares @ ₹ 10 per share including securities premium of ₹ 4 per share)		40,000	 24,000 16,000
	Bank A/c (WN 1) ...Dr. Calls-in Arrears A/c ...Dr. To Shares Allotment A/c (Being the amount received except on 80 shares)		36,064 736	 36,800
	Shares First Call A/c (4,000 × 6) ...Dr. To Share Capital A/c (Being the first call due)		24,000	 24,000
	Bank A/c ...Dr. Calls-in-Arrears A/c ...Dr. To Shares First Call A/c (Being the first call money received except on 200 shares)		22,800 1,200	 24,000
	Share Capital A/c ...Dr. Securities Premium Reserve A/c ...Dr. To Forfeited Shares A/c (96 × ₹ 4) To Calls-in-Arrears A/c [₹ 736 + (80 × ₹ 6)] (Being 80 shares forfeited for non-payment of allotment and first call)		1,280 320	 384 1,216
	Shares Second and Final Call A/c ...Dr. To Share Capital A/c (Being the second and final call due on 3,920 shares @ ₹ 4 each)		15,680	 15,680
	Bank A/c ...Dr. Call-in-Arrears A/c ...Dr. To Shares Second and Final Call A/c (Being the second and final call received except on 120 shares)		15,200 480	 15,680
	Share Capital A/c ...Dr. To Forfeited Shares A/c To Calls-in-Arrears A/c (Being 120 shares forfeited for non-payment of first and second and final call)		2,400	 1,200 1,200
	Bank A/c ...Dr. Forfeited Shares A/c ...Dr. To Share Capital A/c (Being 160 shares out of 200 forfeited shares reissued @ ₹ 18 per share)		2,880 320	 3,200
	Forfeited Shares A/c ...Dr. To Capital Reserve A/c (Being the gain on 160 reissued shares transferred to Capital Reserve) (WN 2)		864	 864

Working Notes:

1. *Calculation of Allotment Money Received Later:*

   (*i*) *The excess amount received from Harish on application:*

   Harish has been allotted 80 shares

   ∴ He must have applied for $\left(\frac{4,800}{4,000} \times 80\right)$ = 96 shares.

   The excess application money received from Harish:

   96 shares – 80 shares = 16 shares × ₹ 4 = ₹ 64.

(*ii*) *Amount not received from Harish on Allotment:*

	₹
Allotment money due on 80 shares @ 10	800
Less: Excess money received from Harish on application	64
Allotment money not received from Harish	736

(*iii*) *Net amount received on Allotment:*

		₹
Allotment money due on 4,000 shares @ ₹ 10		40,000
Less: Excess amount received on application	3,200	
Amount not received from Harish	736	3,936
		36,064

2. *Calculation of Gain (Profit) on Re-issue to be transferred to Capital Reserve:*

160 shares have been reissued which include shares of Harish and Balance 80 shares of Mukesh.

	₹
Amount forfeited on 80 shares of Harish	384
Amount forfeited on 80 shares of Mukesh $\left(\frac{₹\,1{,}200}{120} \times 80\right)$	800
	1,184
Less: Reissue Discount (160 × ₹ 2)	320
Gain (Profit) on Re-issue to be transferred to Capital Reserve	864

Illustration 19.

Mahagun Ltd. invited applications for issuing 2,00,000 Equity Shares of ₹ 10 each. The amounts were payable as follows:

On application ₹ 2, on allotment ₹ 5, on first and final call ₹ 3.

Applications for 4,00,000 shares were received and the allotments were made as follows:

Category	*Shares Applied*	*Shares Allotted*
I	50,000	40,000
II	1,00,000	30,000
III	2,50,000	1,30,000

All the shares were allotted on *pro rata* basis and the excess application money was adjusted towards the sum due on allotment.

Madhu who belonged to Category I and to whom 600 shares were allotted failed to pay the allotment money. Her shares were forfeited immediately after the allotment money was not received. Pooja who belonged to Category III and who had applied for 250 shares failed to pay the final call. Her shares were forfeited after the final call. The forfeited shares were reissued @ ₹ 9 per share fully paid-up.

Pass necessary Journal entries in the books of Mahagun Ltd.

Solution: JOURNAL OF MAHAGUN LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr.		8,00,000	
	To Shares Application A/c			8,00,000
	(Being the applications received for 4,00,000 shares)			
	Shares Application A/c ...Dr.		8,00,000	
	To Share Capital A/c			4,00,000
	To Shares Allotment A/c			4,00,000
	(Being the shares allotted and application money adjusted)			

	Shares Allotment A/c ...Dr. To Share Capital A/c (Being the allotment money due on 2,00,000 shares @ ₹ 5 per share)		10,00,000	 10,00,000
	Bank A/c ...Dr. Calls-in-Arrears A/c ...Dr. To Shares Allotment A/c (Being the Calls-in-Advance adjusted and balance received except on 1,000 shares)		5,97,300 2,700	 6,00,000
	Share Capital A/c ...Dr. To Forfeited Shares A/c To Calls-in-Arrears A/c (Being 600 shares forfeited for non-payment of allotment money)		4,200	 1,500 2,700
	Shares First and Final Call A/c ...Dr. To Share Capital A/c (Being the first and final call money due on 1,99,400 shares @ ₹ 3 each)		5,98,200	 5,98,200
	Bank A/c ...Dr. Calls-in-Arrears A/c ...Dr. To Shares First and Final Call A/c (Being the amount due on first and final call received except on 130 shares)		5,97,810 390	 5,98,200
	Share Capital A/c ...Dr. To Forfeited Shares A/c To Calls-in-Arrears A/c (Being 130 shares of Pooja forfeited)		1,300	 910 390
	Bank A/c ...Dr. Forfeited Shares A/c ...Dr. To Share Capital A/c (Being 730 forfeited shares reissued @ ₹ 9 per share fully paid-up)		6,570 730	 7,300
	Forfeited Shares A/c ...Dr. To Capital Reserve A/c (Being the gain on 730 reissued shares transferred to Capital Reserve)		1,680	 1,680

Working Notes:

1. *Calculation of the Amount due but not Received on Allotment from Madhu:*
   Shares applied by Madhu and Share Application paid and adjusted:

   Shares allotted = 600

   $\therefore$ Shares applied = $\frac{600}{40,000}$ = 750

	₹
Application money paid (750 × ₹ 2)	1,500
Less: Adjusted against share application (600 × ₹ 2)	1,200
Balance to be adjusted against allotment money	300
Amount due from Madhu on allotment (600 × ₹ 5)	3,000
Less: Balance to be adjusted against allotment money	300
Balance not received on allotment	2,700

2. *Amount Received on Allotment:*

	₹
Amount due (2,00,000 × ₹ 5)	10,00,000
Less: Adjusted at the time of share application	4,00,000
	6,00,000
Less: Calls-in-Arrears (not paid by Madhu)	2,700
	5,97,300

Illustration 20.

Eros Ltd. issued a prospectus inviting applications for 2,000 shares of ₹ 10 each at a premium of ₹ 4 per share, payable as follows:

On application	₹ 6 (including ₹ 1 premium);
On allotment	₹ 2 (including ₹ 1 premium);
On first call	₹ 3 (including ₹ 1 premium);
On second and final call	₹ 3 (including ₹ 1 premium).

Applications were received for 3,000 shares and *pro rata* allotment was made on the applications for 2,400 shares. It was decided to utilise the excess application money towards the amount due on allotment.

Ajay, to whom 40 shares were allotted, failed to pay the allotment money and on his subsequent failure to pay the first call, his shares were forfeited.

Raghav, who applied for 72 shares, failed to pay the two calls and on his such failure, his shares were forfeited.

Of the shares forfeited, 80 shares were sold to Pooja credited as fully paid for ₹ 9 per share, the whole of Raghav's shares being included. Prepare Journal, Cash Book and Balance Sheet.

Solution:

In the Books of Eros Ltd.

Dr. CASH BOOK (BANK COLUMN ONLY) *Cr.*

Particulars	₹	Particulars	₹
To Shares Application A/c (3,000 × ₹ 6)	18,000	By Shares Application A/c (600 × ₹ 6)	3,600
To Shares Allotment A/c	1,568	By Balance *c/d*	28,088
To Shares First Call A/c (1,900 × ₹ 3)	5,700		
To Shares Second and Final Call A/c (1,900 × ₹ 3)	5,700		
To Share Capital A/c	720		
	31,688		31,688

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Shares Application A/c ...Dr.		14,400	
	To Share Capital A/c (2,000 × ₹ 5)			10,000
	To Securities Premium Reserve A/c (2,000 × ₹ 1)			2,000
	To Shares Allotment A/c (400 × ₹ 6)			2,400
	(Being the application money adjusted on allotment)			

	Shares Allotment A/c ...Dr. To Share Capital A/c To Securities Premium Reserve A/c (Being the allotment money made due on 2,000 shares)		4,000	 2,000 2,000
	Calls-in-Arrears A/c ...Dr. To Shares Allotment A/c (Being the allotment money not received transferred to Calls-in-Arrears Account)		32	 32
	Shares First Call A/c (2,000 × ₹ 3) ...Dr. To Share Capital A/c To Securities Premium Reserve A/c (Being the first call due)		6,000	 4,000 2,000
	Calls-in-Arrears A/c ...Dr. To Shares First Call A/c (Being the first call money not received trfd. to Calls-in-Arrears Account)		300	 300
	Share Capital A/c (40 × ₹ 8) ...Dr. Securities Premium Reserve A/c [(40 × ₹ 2) – ₹ 8] ...Dr. To Calls-in-Arrears A/c To Forfeited Shares A/c (Being the forfeiture of 40 shares of Ajay for non-payment of allotment and first call money)		320 72	 152 240
	Shares Second and Final Call A/c ...Dr. To Share Capital A/c To Securities Premium Reserve A/c (Being the second and final call due on 1,960 shares)		5,880	 3,920 1,960
	Calls-in-Arrears A/c ...Dr. To Shares Second and Final Call A/c (Being the second and final call not received transferred to Calls-in-Arrears Account)		180	 180
	Share Capital A/c ...Dr. Securities Premium Reserve A/c ...Dr. To Calls-in-Arrears A/c To Forfeited Shares A/c (Being the forfeiture of 60 shares of Raghav for non-payment of calls)		600 120	 360 360
	Forfeited Shares A/c ...Dr. To Share Capital A/c (Being the loss of ₹ 1 per share on the reissue of 80 shares)		80	 80
	Forfeited Shares A/c ...Dr. To Capital Reserve A/c (Being the gain on 80 reissued shares transferred to Capital Reserve) (WN 3)		400	 400

BALANCE SHEET *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
(*a*) Share Capital	1	19,920
(*b*) Reserves and Surplus	2	8,168
Total		28,088
II. ASSETS		
Current Assets		
Cash and Bank Balances	3	28,088
Total		28,088

Notes to Accounts

	₹
1. Share Capital	
Authorised Capital	
... Equity Shares of ₹ 10 each	...
Issued Capital	
2,000 Equity Shares of ₹ 10 each	20,000
Subscribed Capital	
Subscribed and fully paid-up	
1,980 Equity Shares of ₹ 10 each	19,800
Add: Forfeited Shares A/c (WN 4)	120
	19,920
2. Reserves and Surplus	
Capital Reserve	400
Securities Premium Reserve	7,768
	8,168
3. Cash and Bank Balances	
Cash at Bank	28,088

Working Notes:

1. (*i*) *The excess amount received from Ajay on application:*

Ajay has been allotted 40 shares.

Therefore, he must have applied for $\frac{2,400}{2,000} \times 40 = 48$ shares.

The excess application money received from Ajay:

48 shares − 40 shares = 8 shares × ₹ 6 = ₹ 48.

(*ii*) *Amount not received from* Ajay *on Allotment:*

	₹
Allotment money due on 40 shares @ ₹ 2	80
Less: Excess money received from Ajay on application	48
The allotment money not received from Ajay	**32**

(*iii*) *Net amount received on Allotment:*

Allotment money due on 2,000 shares @ ₹ 2	4,000
Less: The excess amount received on application	2,400
Balance due	1,600
Less: Amount not received from Ajay on allotment	32
Net amount received on allotment in cash	**1,568**

2. Raghav applied for 72 shares.

Therefore, he must have been allotted $\frac{2,000}{2,400} \times 72 = 60$ shares. He has not paid the first and the second call money. As such,

(*a*) the first call money will be received on 1,900 shares [2,000 − 40 (Ajay) − 60 (Raghav)], and

(*b*) the second call money will be received on 1,900 shares [*i.e.,* 2,000 − 40 (Ajay) − 60 (Raghav)].

3. 80 shares have been reissued which include 60 shares of Raghav and the balance 20 shares of Ajay.

	₹
Amount forfeited on 20 shares of Ajay = $\frac{₹\,240}{40} \times 20$	120
Amount forfeited on 60 shares of Raghav	360
Total amount forfeited on 80 reissued shares	480
Less: Reissue discount	80
Gain on reissue to be transferred to Capital Reserve	**400**

4. Amount forfeited on 40 shares of Ajay = ₹ 240

Therefore, the balance of Forfeited Shares Account on 20 unissued shares

$$= \frac{₹\,240}{40} \times 20 = ₹\ \mathbf{120}.$$

Unsolved Questions

1. Exe Ltd. issued 1,00,000 shares of ₹ 10 each at a premium of 20% payable as follows:

₹ 5 per share on application;
₹ 5 per share (including premium) on allotment; and
Balance on first and final call.

Excess payment on applications was to be applied towards amounts due on allotment and call.

The issue was subscribed in excess by 1,50,000 shares. Applicants for 2,30,000 shares were allotted 1,00,000 shares whereas applicants for 20,000 were sent letter of regret and application money was refunded to them. The due amounts on allotment and call were received.

Pass the necessary Journal entries.

2. Parijan Ltd. issued 75,000 Equity Shares of ₹ 10 each at a premium of ₹ 2 per share. Total amount was payable along with application. Raman had underwritten the issue for a commission of 3% to be paid by issue of shares at par.

The issue was oversubscribed by 75,000 shares and allotment was made to all the applicants on *pro rata*.

Pass the Journal entries for the above.

3. Ghosh Ltd. made the second and final call on its 50,000 Equity Shares @ ₹ 2 per share on 1st January, 2018. The whole amount was received on 15th January, 2018 except on 100 shares allotted to Venkat. Pass necessary Journal entries for the call money due and received by opening Calls-in- Arrears Account.

4. Grand Prospect Ltd. acquired land costing ₹ 1,00,000 and in payment allotted 1,000 Equity Shares of ₹ 100 each as fully paid. Further, the company issued 4,000 Equity Shares to the public. The shares were payable as follows:

₹ 30 on application;

₹ 30 on allotment; and

₹ 40 on the first and final call.

The public applied for all shares which were allotted. All the moneys were received except the call on 200 shares.

Pass Journal entries and prepare the Balance Sheet of the company.

5. Super Star Ltd. makes an issue of 10,000 Equity Shares of ₹ 100 each, payable as follows:

On application and allotment	₹ 50;
On first call	₹ 25;
On second call	₹ 25.

Members holding 400 shares did not pay the second call and the shares are duly forfeited, 200 of which are reissued as fully paid @ ₹ 50 per share.

Pass Journal entries in the books of the company.

6. Jindal Steel Ltd. issued 50,000 Equity Shares of ₹ 10 each at ₹ 12 (*i.e.*, at a premium of ₹ 2 per share) payable as follows:

₹ 3 on application; ₹ 4 on allotment (including premium); ₹ 2 on first call; and ₹ 3 on second and final call.

The company received applications for 65,000 Equity Shares. Applications for 40,000 Equity Shares were accepted in full; 10,000 Equity Shares were allotted to applicants of 20,000 Equity Shares and applications for 5,000 Equity Shares were rejected. All the moneys were duly received except the first call on 1,000 Equity Shares and final call on 1,500 Equity Shares.

Pass entries in the Cash Book and Journal of the company. Also, draw Balance Sheet.

GUIDE TO ANSWERS

1. Amount credited to Calls-in-Advance on allotment of shares—₹ 6,50,000;
Out of the above, amount applied or adjusted towards allotment money—₹ 5,00,000; and
Amount adjusted towards shares first and final call—₹ 1,50,000.

2. Shares Issued for Cash—75,000;
Shares issued for consideration other than cash—2,700; and
Securities Premium Reserve—₹ 1,50,000.

3. (i) Dr. Equity Shares Second and Final Call A/c and Cr. Equity Share Capital A/c by ₹ 1,00,000.
(ii) Dr. Bank A/c—₹ 99,800 and Calls-in-Arrears A/c—₹ 200;
Cr. Equity Shares Second and Final Call A/c—₹ 1,00,000.

4. Total of Balance Sheet—₹ 4,92,000.

5. Capital Reserve—₹ 5,000.

6. Share Capital—₹ 4,93,500; Reserves and Surplus—₹ 1,00,000; Total of Balance Sheet—₹ 5,93,500.

CHAPTER 7

Joint Stock Company—Issue of Debentures

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Debenture

It is a written acknowledgement of Debt issued by the company. 'Debenture' includes debenture stock, bonds or any other instrument of a company, evidencing a debt, whether constituting a charge on the assets of the company or not.

2. Debentureholder

The person who owns the debentures.

3. Issue of Debentures for Cash

It means issue of debentures against consideration being received through bank.

4. Issue of Debentures for Consideration other than Cash

It means issue of debentures against which amount is not received as consideration but is received in kind, *i.e.*, assets or services.

5. Issue of Debentures as Collateral Security

It means issue of debentures to secure a loan.

6. Issue of Debentures at Par

It means that debentures are issued at its nominal (face) value of debentures.

7. Issue of Debentures at Premium

It means that the issue price of the debentures is higher than their nominal (face) value.

8. Issue of Debentures at Discount

It means that the issue price of the debentures is lower than their nominal (face) value.

9. Redemption of Debentures at Par

It means that the redemption value and the nominal (face) value of debenture is same.

10. Redemption of Debentures at Premium

It means that the redemption value of the debenture is higher than its nominal (face) value.

SUMMARY OF THE CHAPTER

- **Debenture:** A debenture is a written instrument acknowledging a debt and issued under the common seal of the company. It is an agreement for the repayment of the principal sum at a specified date and for the payment of interest at the specified rate.
- **Types of Debentures**
  (*i*) *From the Security Point of View:* Secured Debentures or Unsecured Debentures.
  (*ii*) *From the Redemption Point of View:* Redeemable Debentures or Irredeemable Debentures.
  (*iii*) *From the Registration Point of View:* Registered Debentures or Bearer Debentures.
  (*iv*) *From the Convertibility Point of View:* Convertible Debentures or Non-Convertible Debentures.
- **Issue of Debentures:** Debentures can be issued for: (*i*) cash, (*ii*) consideration other than cash, and (*iii*) as Collateral Security. These debentures can be issued: (*a*) at par, or (*b*) at premium, or (*c*) at discount.

  Accounting for issue of debentures for cash is the same as the accounting for issue of shares with one difference, *i.e.*, the word 'Shares' shall be replaced by 'Debentures' and 'Share Capital' by 'Debentures'. The terms used for the issue of shares will be changed at the time of issue of debentures.

Terms for Issue of Shares	*Terms for Issue of Debentures*
1. Shares Application/Allotment/First Call ..., etc.	Debentures Application/Allotment/First Call ..., etc.
2. Share Capital	Debentures

Note: Premium on the issue of shares or debentures is called *Securities Premium*.
Only Debentures can be issued at discount.

- **Issue of Debentures for Consideration other than Cash:** A company can issue debentures to promoters, underwriters and the vendors as a payment for the purchase of the assets, such an issue of debentures is known as *issue of debentures for consideration other than cash*.
- Excess of purchase consideration over Net Assets acquired is debited to *'Goodwill Account'*.
- Excess of Net Assets acquired over purchase consideration is credited to *'Capital Reserve Account'*.
- **Issue of Debentures as Collateral Security:** Collateral security means an additional security pledged against loan. A company can issue its own debentures as a collateral security.

  No interest is payable on such debentures.
- **Writing off Discount/Loss on Issue of Debentures:** Discount or Loss on Issue of Debentures is a capital loss for a company which is written off in the year when debentures are allotted. It is written off from (*i*) Securities Premium Reserve (if it has a balance); or from (*ii*) Statement of Profit and Loss.
- **Underwriting Commission** is written off in the year in which it is incurred. It is written off from Securities Premium Reserve (if it has a balance) or from Statement of Profit and Loss.
- ***Premium on Redemption of Debentures*** *is to be shown under the main head* ***'Non-Current Liabilities'*** *and sub-head* ***'Long-term Borrowings'***.
- **Interest on Debentures** is an expense for the company. It is a charge against the profits of the company and is payable whether the company earns profit or not. It is shown as 'Finance Costs' in the Statement of Profit and Loss.

Solved Questions

Illustration 1 (*Interest on Debentures*).

X Ltd. issued 5,000, 10% Debentures of ₹ 100 each on 1st April, 2018 at par redeemable at a premium of 10%. TDS is deducted @ 10%. Pass Journal entries relating to issue of debentures and debentures' interest for the year ended 31st March, 2019 assuming that the interest was payable half-yearly on 30th September and 31st March.

Solution:

In the Books of *X* Ltd.

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2018 April 1	Bank A/c ...Dr. To Debentures Application and Allotment A/c (Being the amount received on application)		5,00,000	 5,00,000
April 1	Debentures Application and Allotment A/c ...Dr. Loss on Issue of Debentures A/c ...Dr. To 10% Debentures A/c To Premium on Redemption of Debentures A/c (Being the issue of debentures at par and redeemable at 10% premium)		5,00,000 50,000	 5,00,000 50,000
Sept. 30	Debentures' Interest A/c ...Dr. To Debentureholders' A/c To TDS Payable A/c (Being the interest due for 6 months; TDS deducted @ 10%)		25,000	 22,500 2,500
Sept. 30	Debentureholders' A/c ...Dr. To Bank A/c (Being the payment of interest)		22,500	 22,500
Sept. 30	TDS Payable A/c ...Dr. To Bank A/c (Being the TDS deducted deposited)		2,500	 2,500
2019 March 31	Debentures' Interest A/c ...Dr. To Debentureholders' A/c To TDS Payable A/c (Being the interest due for 6 months; TDS deducted @ 10%)		25,000	 22,500 2,500
March 31	Debentureholders' A/c ...Dr. To Bank A/c (Being the payment of interest)		22,500	 22,500
March 31	TDS Payable A/c ...Dr. To Bank A/c (Being the TDS deducted deposited)		2,500	 2,500
March 31	Statement of Profit and Loss ...Dr. To Debentures' Interest A/c To Loss on Issue of Debentures A/c (Being the transfer of Debentures' Interest and Loss on Issue to Statement of Profit and Loss)		1,00,000	 50,000 50,000

Illustration 2.

On 1st June, 2018, Goodluck Ltd. issued 5,000, 10% Debentures of ₹ 100 each at par redeemable after five years at a premium of 10%. All the debentures were subscribed and allotment made. The balance in Securities Premium Reserve is ₹ 20,000. Profit for the year was ₹ 50,000.

Pass the Journal entries for issue of debentures and writing off the loss and prepare the extract of the Balance Sheet as at 31st March, 2019 showing Loss on Issue of Debentures.

Solution:

In the Books of Goodluck Ltd.

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2018				
June 1	Bank A/c ...Dr.		5,00,000	
	To Debentures Application and Allotment A/c			5,00,000
	(Being the subscription received for 5,000, 10% Debentures of ₹ 100 each)			
	Debentures Application and Allotment A/c ...Dr.		5,00,000	
	Loss on Issue of Debentures A/c ...Dr.		50,000	
	To 10% Debentures A/c			5,00,000
	To Premium on Redemption of Debentures A/c			50,000
	(Being 5,000, 10% Debentures of ₹ 100 each issued at par, redeemable at 10% premium)			
2019				
March 31	Securities Premium Reserve A/c ...Dr.		20,000	
	Statement of Profit and Loss ...Dr.		30,000	
	To Loss on Issue of Debentures A/c			50,000
	(Being the of loss on issue of debentures written off)			

BALANCE SHEET (Extract)

as at 31st March, 2019

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Reserves and Surplus	1	20,000

Note to Accounts

1. Reserves and Surplus		₹
Securities Premium Reserve	20,000	
Less: Loss on Issue of Debentures written off	20,000	...
Surplus, *i.e.*, Balance in Statement of Profit and Loss (₹ 50,000 – ₹ 30,000)		20,000
		20,000

Illustration 3.

DSC Ventures Ltd. issued on 1st April, 2017, 10,000, 9% Debentures of ₹ 100 each at 10% discount redeemable after five years at a premium of ₹ 10. All the debentures were subscribed. During the year ended 31st March, 2018, the company incurred a loss of ₹ 20,000. It has balance in Securities Premium Reserve of ₹ 1,50,000.

Pass the Journal entries and prepare the extract of the Balance Sheet showing Loss on Issue of Debentures.

Solution: JOURNAL OF *DSC* VENTURES LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2017				
April 1	Bank A/c ...Dr.		9,00,000	
	To Debentures Application and Allotment A/c			9,00,000
	(Being the application money received for 10,000, 9% Debentures)			
	Debentures Application and Allotment A/c ...Dr.		9,00,000	
	Loss on Issue of Debentures A/c ...Dr.		2,00,000	
	To 9% Debentures A/c			10,00,000
	To Premium on Redemption of Debentures A/c			1,00,000
	(Being the debentures issued)			
	Securities Premium Reserve A/c ...Dr.		1,50,000	
	Statement of Profit and Loss ...Dr.		50,000	
	To Loss on Issue of Debentures A/c			2,00,000
	(Being the loss on issue of Debentures written off)			

BALANCE SHEET (EXTRACT) *as at 31st March, 2018*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Reserves and Surplus	1	(70,000)

Note to Accounts

Particulars	₹	₹
1. Reserves and Surplus		
Securities Premium Reserve	1,50,000	
Less: Loss on Issue of Debentures Written off	1,50,000	...
Surplus, *i.e.*, Balance in Statement of Profit and Loss (– ₹ 20,000 – ₹ 50,000)		(70,000)
		(70,000)

Master Questions and Advanced Level Question

Illustration 4.

Eey Kay Ltd. issued 10,000, 12% Debentures of ₹ 100 each at a discount of 10% and redeemable at 5% premium after 5 years. Interest was payable half-yearly on 30th September and 31st March each year. The amount was payable as follows:

₹ 50 on application; and

Balance on allotment.

Applications were received for 12,500 Debentures and allotment was made on *pro rata* basis to all the applicants. Excess application money was adjusted against allotment money due.

The company had purchased Plant and Machinery of ₹ 11,00,000. It paid the consideration by issue of 10% Debentures of ₹ 100 each at a premium of 10%.

You are required to:

(*i*) Pass Journal entries for issue of debentures; and

(*ii*) Prepare Balance Sheet showing the above transactions.

Solution:

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr.		6,25,000	
	To Debentures Application A/c			6,25,000
	(Being the applications received for 12,500, 12% Debentures along with application money @ ₹ 50 per debenture)			
	Debentures Application A/c ...Dr.		6,25,000	
	To 12% Debentures A/c			5,00,000
	To Debentures Allotment A/c			1,25,000
	(Being 12% Debentures allotted on *pro rata* basis to all the applicants)			
	Debentures Allotment A/c ...Dr.		4,00,000	
	Loss on Issue of Debentures A/c ...Dr.		1,50,000	
	To 12% Debentures A/c			5,00,000
	To Premium on Redemption of Debentures A/c			50,000
	(Being the allotment money due)			
	Bank A/c ...Dr.		2,75,000	
	To Debentures Allotment A/c			2,75,000
	(Being the balance debentures allotment money received)			
	Plant and Machinery A/c ...Dr.		11,00,000	
	To Vendor's A/c			11,00,000
	(Being the machinery purchased)			
	Vendor's A/c ...Dr.		11,00,000	
	To 10% Debentures A/c			10,00,000
	To Securities Premium Reserve A/c			1,00,000
	(Being 10,000; 10% Debentures issued to Vendor at 10% premium)			

BALANCE SHEET OF EEY KAY LTD.
as at ...

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
Reserves and Surplus	1	(50,000)
2. Non-Current Liabilities		
Long-term Borrowings	2	20,50,000
Total		20,00,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible	3	11,00,000
2. Current Assets		
Cash and Bank Balances	4	9,00,000
Total		20,00,000

Notes to Accounts

		₹
1. Reserves and Surplus		
Securities Premium Reserve	1,00,000	
Less: Loss on Issue of Debentures	1,00,000	...
Surplus, i.e., Balance in Statement of Profit and Loss:		
Opening Balance	...	
Less: Loss on Issue of Debentures	50,000	(50,000)
		(50,000)
2. Long-term Borrowings		
10,000; 12% Debentures of ₹ 100 each		10,00,000
10,000; 10% Debentures of ₹ 100 each		10,00,000
(Above 10% Debentures issued to Vendors of machinery pursuant to contract for consideration other than Cash)		
Premium Payable on Redemption of Debentures		50,000
		20,50,000
3. Fixed Assets—Tangible		
Plant and Machinery		11,00,000
4. Cash and Bank Balances		
Cash at Bank		9,00,000

Illustration 5.

Gee Ess Ltd. is registered with authorised capital of 2,00,000 shares of ₹ 10 each and issued, subscribed and fully paid-up capital of ₹ 15,00,000. It purchased computers of ₹ 7,50,000 and office furniture of ₹ 2,50,000 and issued 10% Debentures of ₹ 100 each at 10% discount to the Vendors, redeemable at par.

The company also issued 10,000, 8% Debentures of ₹ 100 each at a premium of 10% redeemable at 10% premium. The amount was payable along with application.

The applications were received for 12,500 debentures and allotment was made on *pro rata* basis to all the applicants. Both the allotments were made on 1st April, 2014.

You are required to:

(*i*) Pass Journal entries for issue of debentures;

(*ii*) Pass Journal entries for interest for the year ended 31st March, 2015; and

(*iii*) Prepare Balance Sheet showing the above transactions.

Note: According to the terms of issue, interest is payable on half-yearly basis.

Solution: JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2014					
April 1	Computers A/c	...Dr.		7,50,000	
	Furniture and Fixtures A/c	...Dr.		2,50,000	
	To Vendor's A/c				10,00,000
	(Being the computers and office furniture purchased)				
	Vendor's A/c	...Dr.		10,00,000	
	Discount on Issue of Debentures A/c	...Dr.		1,11,110	
	To 10% Debentures A/c				11,11,100
	To Bank A/c				10
	(Being the liability towards Vendor discharged by issue of 11,111; 10% Debentures of ₹ 100 each at a discount of 10%, balance paid by cheque)				
	Bank A/c	...Dr.		13,75,000	
	To Debentures Application and Allotment A/c				13,75,000
	(Being the application money received for 12,500; 8% Debentures @ ₹ 110 per debenture)				
	Debentures Application and Allotment A/c	...Dr.		13,75,000	
	Loss on Issue of Debentures A/c	...Dr.		1,00,000	
	To 8% Debentures A/c				10,00,000
	To Securities Premium Reserve A/c				1,00,000
	To Bank A/c				2,75,000
	To Premium on Redemption of Debentures A/c				1,00,000
	(Being 10,000; 8% Debentures allotted being redeemable at 10% premium, application money adjusted against debentures and securities premium reserve while balance refunded)				
Sept. 30	Debentures Interest A/c	...Dr.		95,555	
	To Debentureholders' A/c				95,555
	(Being the interest for half-year ending 30th September, 2014 on ₹ 11,11,100 @ 10% p.a., and on ₹ 10,00,000 @ 8% p.a. due)				
	Debentureholders' A/c	...Dr.		95,555	
	To Bank A/c				95,555
	(Being the interest paid)				
2015					
March 31	Debentures Interest A/c	...Dr.		95,555	
	To Debentureholders' A/c				95,555
	(Being the interest for half-year ending 31st March, 2015 on ₹ 11,11,100 @ 10% p.a. and on ₹ 10,00,000 @ 8% p.a. due)				
	Debentureholders' A/c	...Dr.		95,555	
	To Bank A/c				95,555
	(Being the interest paid)				
	Statement of Profit and Loss	...Dr.		3,02,220	
	To Debenture Interest A/c				1,91,110
	To Discount on Issue of Debentures A/c				1,11,110
	(Being the interest and discount on issue of debentures written off)				

BALANCE SHEET OF GEE ESS LTD.
as at ...

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital	1	15,00,000
(b) Reserves and Surplus	2	(3,02,220)
2. Non-Current Liabilities		
Long-term Borrowings	3	22,11,100
Total		34,08,880
II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible		10,00,000
2. Current Assets		
Cash and Bank Balances	4	24,08,880
Total		34,08,880

Notes to Accounts

Particulars			₹
1. Share Capital			
Authorised Capital			
2,00,000 shares of ₹ 10 each			20,00,000
Issued Capital			
1,50,000 shares of ₹ 10 each			15,00,000
Subscribed Capital			
Subscribed and fully paid-up			
1,50,000 shares of ₹ 10 each			15,00,000
2. Reserves and Surplus			
Securities Premium Reserve		1,00,000	
Less: Discount on Issue of Debentures Written off		1,00,000	...
Surplus, i.e., Balance in Statement of Profit and Loss:			
Opening Balance		...	
Less: Discount on Issue of Debentures	11,110		
Loss on Issue of Debentures	1,00,000		
Interest on Debentures (₹ 95,555 + ₹ 95,555)	1,91,110	3,02,220	(3,02,220)
			(3,02,220)
3. Long-term Borrowings			
11,111; 10% Debentures of ₹ 100 each			11,11,100
(Issued to Vendors of Computers and Office Furniture for consideration other than cash)			
10,000; 8% Debentures of ₹ 100 each			10,00,000
Premium payable on Redemption of Debentures			1,00,000
			22,11,100
4. Cash and Bank Balances			
Cash at Bank			24,08,880
(Opening Balance ₹ 15,00,000 + ₹ 13,75,000 – ₹ 2,75,000 – ₹ 1,91,110 – ₹ 10)			

Illustration 6.

On 1st April, 2016, the Earth Ltd. issued 10,000, 12% Debentures of ₹ 100 each at a premium of 5%, redeemable at a premium of 5%, after 5 years. The full amount was payable on application. Applications were received for 14,000 debentures out of which applicants for 9,000 debentures were allotted fully, applicants for 2,500 debentures were allotted 1,000 debentures and remaining applications were rejected.

On 1st October, 2016, company purchased building worth ₹ 10,00,000, Plant and Machinery worth ₹ 8,00,000 from M/s Raman & Company and took over their liabilities of ₹ 3,00,000 for a purchase price of ₹ 16,50,000. The company paid the purchase price by issuing 12% Debentures of ₹ 100 each at a premium of 10%, redeemable at the end of 5 years at par.

During the accounting year 2016–17 on 1st October, 2016 company took a loan of ₹ 10,00,000 from ICICI Bank payable on 31st March, 2018 and issued ₹ 15,00,000, 12% Debentures as collateral security.

Additional Information:

(*a*) Debenture interest is payable half-yearly on 30th September and 31st March.
(*b*) Tax to be deducted at source @ 10%.
(*c*) Ignore interest on bank loan.
(*d*) It was decided by the company to write-off Loss on Issue of Debentures as early as possible.

Pass necessary Journal entries in the books of Earth Ltd. for the year 2016–17.

Solution: **In the Books of Earth Ltd.**

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2016				
April 1	Bank A/c ...Dr.		14,70,000	
	To Debentures Application and Allotment A/c			14,70,000
	(Being the application money received for 14,000; 12% Debentures @ ₹ 105 each)			
April 1	Debentures Application and Allotment A/c ...Dr.		14,70,000	
	Loss on Issue of Debentures A/c ...Dr.		50,000	
	To 12% Debentures A/c			10,00,000
	To Securities Premium Reserve A/c			50,000
	To Premium on Redemption of Debentures A/c			50,000
	To Bank A/c			4,20,000
	(Being 10,000; 12% Debentures of ₹ 100 each issued at 5% premium and redeemable at 5% premium and excess money returned)			
Sept. 30	Debentures' Interest A/c ...Dr.		60,000	
	To Debentureholders' A/c			54,000
	To TDS Payable A/c			6,000
	(Being the interest due on 12% Debentures for half year ended 30th September, 2016, TDS being deducted @ 10%)			
Sept. 30	Debentureholders' A/c ...Dr.		54,000	
	To Bank A/c			54,000
	(Being the interest paid to debentureholders)			

Sept. 30	TDS Payable A/c	...Dr.	6,000	
	To Bank A/c			6,000
	(Being the TDS deposited in Government Account)			
Oct. 1	Building A/c	...Dr.	10,00,000	
	Plant and Machinery A/c	...Dr.	8,00,000	
	Goodwill A/c (Balancing Figure)	...Dr.	1,50,000	
	To Sundry Liabilities A/c			3,00,000
	To M/s Raman & Company			16,50,000
	(Being the assets and liabilities of M/s Raman & Company taken over for a purchase consideration of ₹ 16,50,000)			
Oct. 1	M/s Raman & Company	...Dr.	16,50,000	
	To 12% Debentures A/c			15,00,000
	To Securities Premium Reserve A/c			1,50,000
	(Being 15,000; 12% Debentures of ₹ 100 each issued at 10% premium to M/s Raman & Company against purchase consideration)			
Oct. 1	Bank A/c	...Dr.	10,00,000	
	To Loan from ICICI Bank A/c			10,00,000
	(Being the loan taken from ICICI Bank)			
Oct. 1	Debentures Suspense A/c	...Dr.	15,00,000	
	To 12% Debentures A/c			15,00,000
	(Being 15,000; 12% Debentures of ₹ 100 each issued as collateral security to bank against loan of ₹ 10,00,000)			
2017				
March 31	Debentures' Interest A/c	...Dr.	1,50,000	
	To Debentureholders' A/c			1,35,000
	To TDS Payable A/c			15,000
	(Being the interest due on 25,000; 12% Debentures of ₹ 100 each for half year ended 31st March, 2017, TDS being deducted @ 10%)			
March 31	Debentureholders' A/c	...Dr.	1,35,000	
	To Bank A/c			1,35,000
	(Being the interest paid to debentureholders)			
March 31	TDS Payable A/c	...Dr.	15,000	
	To Bank A/c			15,000
	(Being the TDS deposited in Government Account)			
March 31	Statement of Profit and Loss	...Dr.	2,10,000	
	To Debentures' Interest A/c			2,10,000
	(Being the transfer of Debentures' Interest to Statement of Profit and Loss)			
March 31	Securities Premium Reserve A/c	...Dr.	50,000	
	To Loss on Issue of Debentures A/c			50,000
	(Being the Loss on Issue of Debentures written off from Securities Premium Reserve)			

Notes:

1. Interest on Debentures issued as collateral security is not paid. Therefore, interest on 15,000; 12% Debentures of ₹ 100 each is not accounted.

2. *Calculation of Interest:*

	₹
(*i*) Half year ended 30th September, 2016	
10,000; 12% Debentures of ₹ 100 each $\left(₹\ 10,00,000 \times \frac{12}{100} \times \frac{1}{2}\right)$	60,000
TDS Payable (₹ 60,000 × 10%) = ₹ 6,000.	
(*ii*) Half year ended 31th March, 2017	
10,000; 12% Debentures of ₹ 100 each $\left(₹\ 10,00,000 \times \frac{12}{100} \times \frac{1}{2}\right)$	60,000
15,000; 12% Debentures of ₹ 100 each $\left(₹\ 15,00,000 \times \frac{12}{100} \times \frac{1}{2}\right)$	90,000
	1,50,000
TDS Payable (₹ 1,50,000 × 10%) = ₹ 15,000.	

CHAPTER 8

Joint Stock Company— Redemption of Debentures

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Redemption of Debentures

Redemption of Debentures means repayment of the amount of debentures.

2. Debentures Redemption Reserve (DRR)

It is a reserve created out of profits available for payment as dividend for the purpose of redemption of debentures.

It is created for Non-convertible Debentures (NCD) and Non-convertible part of Partly Convertible Debentures (PCD).

3. Debentures Redemption Investment (DRI)

It is an investment made by a company on or before 30th April of the current year of an amount that is at least equal to 15% of the nominal value of debentures to be redeemed by 31st March of next year.

4. Redemption of Debentures out of Capital

When profits are not transferred from Surplus, *i.e.,* Balance in Statement of Profit and Loss to Debentures Redemption Reserve (DRR) before the redemption of debentures, such redemption is Redemption of Debentures out of capital.

5. Redemption of Debentures out of Profits

When adequate profits are transferred from Surplus, *i.e.*, Balance in Statement of Profit and Loss to Debentures Redemption Reserve (DRR) before redemption of debentures, such redemption is Redemption of Debentures out of profits.

6. Redemption of Debentures in Lump Sum

It means all the debentures are redeemed at the date specified for redemption of debentures.

7. Redemption in Instalment by Draw of Lots

It means redemption of debentures (selected by lottery) at the specified date.

8. Redemption by Purchase from Open Market

When a company purchases its own debentures from open market for the purpose of cancellation, such an act of purchasing and cancelling the debentures is redemption by purchase from open market. The company may purchase its own debentures from the open market with the objective of (*i*) immediate cancellation, or (*ii*) as investments.

SUMMARY OF THE CHAPTER

- **Redemption of Debentures** is a process of repayment of loan taken by issue of debentures.
- **Methods of Redemption of Debentures:**
  1. On maturity in lump sum;
  2. In instalments by draw of lots;
  3. By purchase of Own Debentures from Open Market, and
  4. By Conversion into Shares or New Class of Debentures (It is not in Syllabus).
- **Sources of Redemption of Debentures:** Debentures can be redeemed by utilising any of the following sources:
  (*i*) *Redemption Out of Capital:* When debentures are redeemed without adequate profits being transferred from Surplus, *i.e.*, Statement of Profit and Loss to Debentures Redemption Reserve (DRR), at the time of redemption of debentures, such redemption is said to be out of capital.
  (*ii*) *Redemption Out of Profits:* When debentures are redeemed only out of profits and amount equal to nominal (face) value of Debentures is transferred from Surplus, *i.e.*, Statement of Profit and Loss to Debentures Redemption Reserve (DRR) before the redemption of debentures, such redemption is said to be out of profits.
  (*iii*) *Redemption Partly out of Profits and Partly out of Capital:* It means that the company does not transfer 100 per cent nominal (face) value of total redeemable debentures of a particular series to DRR out of surplus.
- **Debentures Redemption Reserve** (DRR) is created out of profits of the company available for payment as dividend for the purpose of redemption of debentures.

  DRR is created before the redemption starts.

  As per the provisions of Section 71(4) of the Companies Act, 2013 read with Rule 18(7) (*b*) of the Companies (Share Capital and Debentures) Rules, 2014, a company shall transfer at least 25 per cent of nominal (face) value of the outstanding debentures of that class out of surplus available for payment of dividend to DRR.

  DRR is required to be created only in case of **Non-convertible Debentures (NCD) and Non-convertible portion of Partly Convertible Debentures (PCD)**

  Debentures Redemption Investment: A company required to create/maintain DRR shall **on or before 30th April** of the current year, deposit or invest (as the case may be) **at least 15% of the amount of its debentures maturing during the year** ending on 31st March of the next year.

  Companies not required to create DRR are not required to invest in specified securities.

Solved Questions

Illustration 1.

N Ltd. issued 10,000; 9% Debentures of ₹ 100 each at par on April, 2014 with the condition that they will be redeemed at a premium of 5% after the expiry of five years.

Pass Journal entries for issue and redemption of these debentures along with the entries for DRR. Investment is to earn interest @ 6% p.a.

Solution:

In the Books of *N* Ltd.
JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2014				
April 1	**On Issue of Debentures**			
	Bank A/c ...Dr.		10,00,000	
	To Debentures Application and Allotment A/c			10,00,000
	(Being the amount received on 10,000 debentures @ ₹ 100 each)			

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Debentures Application and Allotment A/c	...Dr.		10,00,000	
	Loss on Issue of Debentures A/c	...Dr.		50,000	
	To 9% Debentures A/c				10,00,000
	To Premium on Redemption of Debentures A/c				50,000
	(Being the allotment of 10,000; 9% Debentures of ₹ 100 each at par redeemable at a premium of 5%)				
2015 March 31	Statement of Profit and Loss	...Dr.		50,000	
	To Loss on Issue of Debentures A/c				50,000
	(Being the loss written off)				
2018 March 31	**On Creation of DRR**				
	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c	...Dr.		2,50,000	
	To Debentures Redemption Reserve A/c				2,50,000
	(Being the transfer of profit to DRR equivalent to 25% of the nominal value of outstanding debentures)				
April 1	**On Investment being made**				
	Debentures Redemption Investment A/c	...Dr.		1,50,000	
	To Bank A/c				1,50,000
	(Being the amount equal to 15% of the value of debentures invested, earning interest @ 6% p.a.)				
2019 March 31	**On Redemption of Debentures**				
	Bank A/c	...Dr.		1,59,000	
	To Debentures Redemption Investment A/c				1,50,000
	To Interest Earned A/c				9,000
	(Being the investment bearing interest @ 6% p.a. encashed on redemption of debentures)				
	9% Debentures A/c	...Dr.		10,00,000	
	Premium on Redemption of Debentures A/c	...Dr.		50,000	
	To Debentureholders' A/c				10,50,000
	(Being the amount payable on redemption, transferred to Debentureholders' Account)				
	Debentureholders' A/c	...Dr.		10,50,000	
	To Bank A/c				10,50,000
	(Being the amount paid to debentureholders on redemption)				
	Debentures Redemption Reserve A/c	...Dr.		2,50,000	
	To General Reserve A/c				2,50,000
	(Being the transfer of Debentures Redemption Reserve to General Reserve after redemption of debentures)				
	Interest Earned A/c	...Dr.		9,000	
	To Statement of Profit and Loss (Other Income)				9,000
	(Being the interest on DRI transferred)				

Illustration 2.

Pragati Ltd. has 50,000; 8% Debentures of ₹ 100 each due for redemption in four equal instalments starting from 31st March, 2015. Debentures Redemption Reserve has a balance of ₹ 9,00,000 on that date. The company pays interest annually and deducted tax @ 10% on interest payment and deposits in Government Account on due date.

Pass Journal entries for investment, redemption of debentures and payment of interest on debentures. The company made investment in fixed deposit with bank earning interest @ 10% p.a. Bank deducted TDS @ 10%.

Solution:

In the Books of Pragati Ltd.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2015					
March 31	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c	...Dr.		3,50,000	
	To Debentures Redemption Reserve A/c				3,50,000
	(Being the transfer of profits to Debentures Redemption Reserve) (WN 2)				
April 1	Debentures Redemption Investment A/c	...Dr.		1,87,500	
	To Bank A/c				1,87,500
	(Being the fixed deposit placed with Bank for 15% nominal value of debentures to be redeemed)				
2016					
March 31	Interest on Debentures A/c (WN 1)	...Dr.		4,00,000	
	To Debentureholders' A/c				3,60,000
	To TDS Payable A/c				40,000
	(Being the interest on debentures due and tax deducted @ 10%)				
March 31	Debentureholders' A/c	...Dr.		3,60,000	
	TDS Payable A/c	...Dr.		40,000	
	To Bank A/c				4,00,000
	(Being the payment of debentures' interest and TDS payable)				
March 31	8% Debentures A/c	...Dr.		12,50,000	
	To Debentureholders' A/c				12,50,000
	(Being the payment due to debentureholders on redemption)				
March 31	Debentureholders' A/c	...Dr.		12,50,000	
	To Bank A/c				12,50,000
	(Being the payment due to debentureholders discharged)				
March 31	Debentures Redemption Reserve A/c	...Dr.		3,12,500	
	To General Reserve A/c				3,12,500
	(Being one-fourth of DRR transferred to General Reserve on redemption of one-fourth debentures)				
March 31	Statement of Profit and Loss	...Dr.		4,00,000	
	To Interest on Debentures A/c				4,00,000
	(Being the interest on debentures transferred)				
2017					
March 31	Interest on Debentures A/c	...Dr.		3,00,000	
	To Debentureholders' A/c (WN 3)				2,70,000
	To TDS Payable A/c				30,000
	(Being the interest due on debentures)				
March 31	Debentureholders' A/c	...Dr.		2,70,000	
	TDS Payable A/c	...Dr.		30,000	
	To Bank A/c				3,00,000
	(Being the debentures' interest and TDS paid)				
March 31	8% Debentures A/c	...Dr.		12,50,000	
	To Debentureholders' A/c				12,50,000
	(Being the payment due to debentureholders on redemption)				
March 31	Debentureholders' A/c	...Dr.		12,50,000	
	To Bank A/c				12,50,000
	(Being the payment due to debentureholders discharged)				

March 31	Debentures Redemption Reserve A/c	...Dr.	3,12,500	
	To General Reserve A/c			3,12,500
	(Being the one-fourth of DRR transferred to General Reserve on redemption of one-fourth debentures)			
March 31	Statement of Profit and Loss	...Dr.	3,00,000	
	To Interest on Debentures A/c			3,00,000
	(Being the interest on debentures transferred)			
2018				
March 31	Interest on Debentures A/c	...Dr.	2,00,000	
	To Debentureholders' A/c (WN 4)			1,80,000
	To TDS Payable A/c			20,000
	(Being the debentures' interest due)			
March 31	Debentureholders' A/c	...Dr.	1,80,000	
	TDS Payable A/c	...Dr.	20,000	
	To Bank A/c			2,00,000
	(Being the debentures' interest paid along with TDS payable)			
March 31	8% Debentures A/c	...Dr.	12,50,000	
	To Debentureholders' A/c			12,50,000
	(Being the payment due to debentureholders on redemption)			
March 31	Debentureholders' A/c	...Dr.	12,50,000	
	To Bank A/c			12,50,000
	(Being the payment due to debentureholders discharged)			
March 31	Debentures Redemption Reserve A/c	...Dr.	3,12,500	
	To General Reserve A/c			3,12,500
	(Being the one-fourth of DRR transferred to General Reserve on redemption of one-fourth debentures)			
March 31	Statement of Profit and Loss	...Dr.	2,00,000	
	To Interest on Debentures A/c			2,00,000
	(Being the interest on debentures transferred)			
2019				
March 31	Interest on Debentures A/c	...Dr.	1,00,000	
	To Debentureholders' A/c			90,000
	To TDS Payable A/c			10,000
	(Being the interest due on debentures)			
March 31	Debentureholders' A/c	...Dr.	90,000	
	TDS Payable A/c	...Dr.	10,000	
	To Bank A/c			1,00,000
	(Being the debentures' interest and TDS paid)			
March 31	8% Debentures A/c	...Dr.	12,50,000	
	To Debentureholders' A/c			12,50,000
	(Being the payment due to debentureholders on redemption)			
March 31	Debentureholders' A/c	...Dr.	12,50,000	
	To Bank A/c			12,50,000
	(Being the payment due to debentureholders discharged)			

March 31	Bank A/c ...Dr.		2,55,000	
	TDS Collected A/c ...Dr.		7,500	
	To Debentures Redemption Investment A/c			1,87,500
	To Interest Earned A/c			75,000
	(Being the fixed deposit placed on 1st April, 2014 encashed and interest earned on the same @ 10% p.a. but received after deducting tax @ 10% on all debentures having been redeemed)			
March 31	Debentures Redemption Reserve A/c ...Dr.		3,12,500	
	To General Reserve A/c			3,12,500
	(Being the DRR closed by transferring it to General Reserve)			
March 31	Statement of Profit and Loss ...Dr.		1,00,000	
	To Interest on Debentures A/c			1,00,000
	(Being the interest on debentures transferred)			
March 31	Interest Earned A/c ...Dr.		75,000	
	To Statement of Profit and Loss (Other Income)			75,000
	(Being the interest earned transferred)			

Working Notes:

	₹
1. Interest = ₹ 50,00,000 × 8/100	4,00,000
2. 25% of ₹ 50,00,000 (Face value of Debentures)	12,50,000
Less: Existing Debentures Redemption Reserve (DRR)	9,00,000
DRR to be created before redemption	3,50,000

3. ₹ 50,00,000 – ₹ 12,50,000 = ₹ 37,50,000 (After Redemption)
   Interest = ₹ 37,50,000 × 8/100 = ₹ 3,00,000
4. Interest = (₹ 37,50,000 – ₹ 12,50,000 = ₹ 25,00,000) × 8/100 = ₹ 2,00,000.
5. Investment in fixed deposit in terms of Section 71 (4) of the Companies Act, 2013 is assumed to have been made on 1st April, 2015 and encashed on the redemption of final lot of debentures.
6. Interest on Debentures Account is shown in Statement of Profit and Loss as 'Finance Costs'.

Illustration 3.

Ashoka Ltd. issued 10,000; 8% Debentures of ₹ 100 each on 1st September, 2012 redeemable at a premium of 7% as under:

On 31st March, 2017	5,000 Debentures;
On 31st March, 2018	2,500 Debentures;
On 31st March, 2019	2,500 Debentures.

The company decided to transfer the required amount to Debentures Redemption Reserve (DRR) in four equal annual instalments starting from 31st March, 2013. The company decided to make fresh investment in fixed deposit as required by the Companies Act, 2013 for each redemption.

Pass Journal entries for issue and redemption of debentures and transfer to Debentures Redemption Reserve.

Solution:

In the Books of Ashoka Ltd.

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2012	**Issue of Debentures**			
Sept. 1	Bank A/c (10,000 × ₹ 100) ...Dr.		10,00,000	
	To Debentures Application and Allotment A/c			10,00,000
	(Being the debentures application money received on issue of debentures)			
Sept. 1	Debentures Application and Allotment A/c (10,000 × ₹ 100) ...Dr.		10,00,000	
	Loss on Issue of Debentures A/c (₹ 10,00,000 × 7/100) ...Dr.		70,000	
	To 8% Debentures A/c			10,00,000
	To Premium on Redemption of Debentures A/c			70,000
	(Being the issue of debentures at par but redeemable at premium)			
2013	**Creation of DRR**			
March 31	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c (Note) ...Dr.		62,500	
	To Debentures Redemption Reserve A/c			62,500
	(Being the profit appropriated towards Debentures Redemption Reserve)			
March 31	Statement of Profit and Loss ...Dr.		70,000	
	To Loss on Issue of Debentures A/c			70,000
	(Being the loss on issue of debentures transferred)			
2014				
March 31	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c (Note) ...Dr.		62,500	
	To Debentures Redemption Reserve A/c			62,500
	(Being the profit appropriated towards Debentures Redemption Reserve)			
2015				
March 31	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c (Note) ...Dr.		62,500	
	To Debentures Redemption Reserve A/c			62,500
	(Being the profit appropriated towards Debentures Redemption Reserve)			
2016				
March 31	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c (Note) ...Dr.		62,500	
	To Debentures Redemption Reserve A/c			62,500
	(Being the profit appropriated towards Debentures Redemption Reserve)			
April 30	Debentures Redemption Investment A/c ...Dr.		75,000	
	To Bank A/c			75,000
	(Being the investment made of amount equal to 15% of nominal value of debentures to be redeemed on 31st March, 2017)			
2017	**Redemption of Debentures**			
March 31	Bank A/c ...Dr.		75,000	
	To Debentures Redemption Investment A/c			75,000
	(Being the fixed deposit encashed on redemption of 5,000 debentures)			
March 31	8% Debentures A/c ...Dr.		5,00,000	
	Premium on Redemption of Debentures A/c ...Dr.		35,000	
	To Debentureholders' A/c			5,35,000
	(Being the amount due to debentureholders on redemption of debentures)			

March 31	Debentureholders' A/c ...Dr.		5,35,000	
	To Bank A/c			5,35,000
	(Being the payment made to debentureholders)			
March 31	Debentures Redemption Reserve A/c ...Dr.		1,25,000	
	To General Reserve A/c			1,25,000
	(Being the amount proportionate to 5,000 debentures redeemed transferred to General Reserve)			
2017				
April 30	Debentures Redemption Investment A/c ...Dr.		37,500	
	To Bank A/c			37,500
	(Being the investment made of amount equal to 15% of nominal value of debentures to be redeemed on 31st March, 2018)			
2018				
March 31	Bank A/c ...Dr.		37,500	
	To Debentures Redemption Investment A/c			37,500
	(Being the fixed deposit encashed on redemption of 2,500 debentures)			
March 31	8% Debentures A/c ...Dr.		2,50,000	
	Premium on Redemption of Debentures A/c ...Dr.		17,500	
	To Debentureholders' A/c			2,67,500
	(Being the amount due to debentureholders on redemption of debentures)			
March 31	Debentureholders' A/c ...Dr.		2,67,500	
	To Bank A/c			2,67,500
	(Being the payment made to debentureholders)			
March 31	Debentures Redemption Reserve A/c ...Dr.		62,500	
	To General Reserve A/c			62,500
	(Being the amount proportionate to 2,500 debentures redeemed transferred to General Reserve)			
April 30	Debentures Redemption Investment A/c ...Dr.		37,500	
	To Bank A/c			37,500
	(Being the investment made for the amount equal to 15% of nominal value of debentures to be redeemed on 31st March, 2019)			
2019				
March 31	Bank A/c ...Dr.		37,500	
	To Debentures Redemption Investment A/c			37,500
	(Being the fixed deposit encashed on 2,500 debentures being reedemed)			
March 31	8% Debentures A/c ...Dr.		2,50,000	
	Premium on Redemption of Debentures A/c ...Dr.		17,500	
	To Debentureholders' A/c			2,67,500
	(Being the amount due to debentureholders on redemption of debentures)			
March 31	Debentureholders' A/c ...Dr.		2,67,500	
	To Bank A/c			2,67,500
	(Being the payment made to debentureholders)			
March 31	Debentures Redemption Reserve A/c ...Dr.		62,500	
	To General Reserve A/c			62,500
	(Being the Debentures Redemption Reserve closed by transferring it to General Reserve)			

Note: Outstanding amount on debentures = ₹ 10,00,000

DRR, *i.e.*, 25% of ₹ 10,00,000 = ₹ 2,50,000

Four equal annual instalments = 1/4 × ₹ 2,50,000 = ₹ 62,500.

Illustration 4 (*Purchase of Debentures from the Open Market for Cancellation*).

Zenith Ltd. purchased its own 200, 9% Debentures of ₹ 100 each from the open market for cancellation at ₹ 92. Pass Journal entries for purchase and cancellation of own debentures.

Solution: JOURNAL OF ZENITH LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Own Debentures A/c ...Dr.		18,400	
	To Bank A/c			18,400
	(Being the purchase of 200 own debentures @ ₹ 92 each)			
	9% Debentures A/c ...Dr.		20,000	
	To Own Debentures A/c			18,400
	To Gain (Profit) on Cancellation of Own Debentures A/c			1,600
	(Being own debentures of the face value of ₹ 20,000 purchased for ₹ 92 each from open market and cancelled)			
	Gain (Profit) on Cancellation of Own Debentures A/c ...Dr.		1,600	
	To Capital Reserve A/c			1,600
	(Being the transfer of Gain (Profit) on redemption of debentures to Capital Reserve)			

Illustration 5.

X Ltd. has 4,000; 9% Debentures of ₹ 100 each outstanding as on 31st March, 2019. These debentures are due for redemption on 31st March, 2019. Debentures Redemption Reserve has a balance of ₹ 50,000 on 31st March, 2018.

Pass Journal entries at the time of redemption of debentures.

Solution: JOURNAL OF *X* LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2018				
March 31	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c ...Dr.		50,000	
	To Debentures Redemption Reserve A/c			50,000
	(Being the transfer of Profit to DRR as per Rule 18(7)) (Note)			
April 30	Debentures Redemption Investment A/c ...Dr.		60,000	
	To Bank A/c			60,000
	(Being the investment made of a sum equal to 15% of the nominal value of debentures to be redeemed)			
2019				
March 31	Bank A/c ...Dr.		60,000	
	To Debentures Redemption Investment A/c			60,000
	(Being the Debentures Redemption investment realised)			
March 31	9% Debentures A/c ...Dr.		4,00,000	
	To Debentureholders' A/c			4,00,000
	(Being the amount due to debentureholders on redemption)			
March 31	Debentureholders' A/c ...Dr.		4,00,000	
	To Bank A/c			4,00,000
	(Being the amount due to debentureholders paid)			
March 31	Debentures Redemption Reserve A/c ...Dr.		1,00,000	
	To General Reserve A/c			1,00,000
	(Being the DRR transferred to General Reserve)			

Note: Balance in DRR is ₹ 50,000 as on 31st March, 2019. A further amount of ₹ 50,000 is transferred from Surplus, *i.e.*, Balance in Statement of Profit and Loss to make DRR equal to ₹ 1,00,000 (*i.e.*, 25% of ₹ 4,00,000).

Master Question and Advanced Level Question

Illustration 6.

Ananya Ltd. issued on 1st July, 2011, 20,000, 8% Debentures of ₹ 50 each at a premium of 10% redeemable at a premium of 20% in four equal annual instalments beginning 31st March, 2014 either by draw of lot or by purchase from open market. Interest on Debentures was payable yearly on 31st March on which TDS was deducted @ 10%. It was decided to create DRR in two years equally on 31st March, 2012 and 31st March, 2013. Investment, as required by law, shall be made in fixed deposit with a bank on 1st April, 2013, which shall be realised at the time of last investment. Fixed Deposit earned an interest @ 6% p.a. Bank deducted TDS @ 10% every year.

Pass the Journal entries for issue and redemption of debentures, DRR, Investment, interest on debentures and interest on investments.

Solution:

JOURNAL OF ANANYA LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2011				
July 1	Bank A/c ...Dr.		11,00,000	
	To Debentures Application and Allotment A/c			11,00,000
	(Being the applications received for 20,000, 8% Debentures @ ₹ 55 each)			
	Debentures Application and Allotment A/c ...Dr.		11,00,000	
	Loss on Issue of Debentures A/c ...Dr.		2,00,000	
	To 8% Debentures A/c			10,00,000
	To Securities Premium Reserve A/c			1,00,000
	To Premium on Redemption of Debentures A/c			2,00,000
	(Being 20,000; 8% Debentures of ₹ 50 each issued at a premium of 10% redeemable at 20% premium)			
2012				
March 31	Interest on Debentures A/c ...Dr.		60,000	
	To Debentureholders' A/c			54,000
	To TDS Payable A/c			6,000
	(Being the interest due on 8% Debentures for nine months and TDS deducted @ 10%)			
	Debentureholders' A/c ...Dr.		54,000	
	To Bank A/c			54,000
	(Being the interest on debentures paid)			
	TDS Payable A/c ...Dr.		6,000	
	To Bank A/c			6,000
	(Being the TDS deposited in Government Account)			
	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c ...Dr.		1,25,000	
	To Debentures Redemption Reserve A/c			1,25,000
	(Being one-half of total DRR required transferred)			

	Securities Premium Reserve A/c ...Dr.		1,00,000	
	Statement of Profit and Loss ...Dr.		1,00,000	
	To Loss on Issue of Debentures A/c			2,00,000
	(Being the loss written off)			
	Statement of Profit and Loss ...Dr.		60,000	
	To Interest on Debentures A/c			60,000
	(Being the interest transferred)			
2013 March 31	Interest on Debentures A/c ...Dr.		80,000	
	To Debentureholders' A/c			72,000
	To TDS Payable A/c			8,000
	(Being the interest due on 8% Debentures for one year and TDS deducted @ 10%)			
	Debentureholders' A/c ...Dr.		72,000	
	To Bank A/c			72,000
	(Being the interest on debentures paid)			
	TDS Payable A/c ...Dr.		8,000	
	To Bank A/c			8,000
	(Being the TDS deposited in Government Account)			
	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c ...Dr.		1,25,000	
	To Debentures Redemption Reserve A/c			1,25,000
	(Being one-half of total DRR required transferred)			
	Statement of Profit and Loss ...Dr.		80,000	
	To Interest on Debentures A/c			80,000
	(Being the interest transferred)			
April 1	Debentures Redemption Investment A/c ...Dr.		37,500	
	To Bank A/c			37,500
	(Being the investment made in fixed deposit with bank earning interest @ 6%)			
2014 March 31	Interest on Debentures A/c ...Dr.		80,000	
	To Debentureholders' A/c			72,000
	To TDS Payable A/c			8,000
	(Being the interest due on 20,000, 8% Debentures for one year and TDS deducted @ 10%)			
	Debentureholders' A/c ...Dr.		72,000	
	To Bank A/c			72,000
	(Being the interest on debentures paid)			
	TDS Payable A/c ...Dr.		8,000	
	To Bank A/c			8,000
	(Being the TDS deposited in Government Account)			

	Interest Accrued But Not Due A/c ...Dr. TDS Collected (Receivable) A/c ...Dr. To Interest Earned A/c (Being the interest on fixed deposit @ 6% provided, TDS was deducted by Bank @ 10%)		2,025 225	 2,250
	8% Debentures A/c ...Dr. Premium on Redemption of Debentures A/c ...Dr. To Debentureholders' A/c (Being the amount due on 5,000; 8% Debentures on redemption)		2,50,000 50,000	 3,00,000
	Debentureholders' A/c ...Dr. To Bank A/c (Being the payment made to debentureholders)		3,00,000	 3,00,000
	Debentures Redemption Reserve A/c ...Dr. To General Reserve A/c (Being the amount proportionate to debentures redeemed transferred to General Reserve)		62,500	 62,500
	Statement of Profit and Loss ...Dr. To Interest on Debentures A/c (Being the interest transferred)		80,000	 80,000
	Interest Earned A/c ...Dr. To Statement of Profit and Loss (Being the interest earned transferred)		2,250	 2,250
2015 March 31	Interest on Debentures A/c ...Dr. To Debentureholders' A/c To TDS Payable A/c (Being the interest due on 15,000; 8% Debentures for one year and TDS deducted @ 10%)		60,000	 54,000 6,000
	Debentureholders' A/c ...Dr. To Bank A/c (Being the interest on debentures paid)		54,000	 54,000
	TDS Payable A/c ...Dr. To Bank A/c (Being the TDS deposited in Government Account)		6,000	 6,000
	Interest Accrued But Not Due A/c ...Dr. TDS Collected (Receivable) A/c ...Dr. To Interest Earned A/c (Being the interest on fixed deposit @ 6% provided, TDS was deducted by Bank @ 10%)		2,025 225	 2,250
	8% Debentures A/c ...Dr. Premium on Redemption of Debentures A/c ...Dr. To Debentureholders' A/c (Being the amount due on 5,000; 8% Debentures on redemption)		2,50,000 50,000	 3,00,000
	Debentureholders' A/c ...Dr. To Bank A/c (Being the payment made to debentureholders)		3,00,000	 3,00,000
	Debentures Redemption Reserve A/c ...Dr. To General Reserve A/c (Being the amount proportionate to debentures redeemed transferred to General Reserve)		62,500	 62,500

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Statement of Profit and Loss	...Dr.		60,000	
	To Interest on Debentures A/c				60,000
	(Being the interest on debentures transferred)				
	Interest Earned A/c	...Dr.		2,250	
	To Statement of Profit and Loss				2,250
	(Being the interest earned transferred)				
2016 March 31	Interest on Debentures A/c	...Dr.		40,000	
	To Debentureholders' A/c				36,000
	To TDS Payable A/c				4,000
	(Being the interest due on 10,000, 8% Debentures for one year and TDS deducted @ 10%)				
	Debentureholders' A/c	...Dr.		36,000	
	To Bank A/c				36,000
	(Being the interest on debentures paid)				
	TDS Payable A/c	...Dr.		4,000	
	To Bank A/c				4,000
	(Being the TDS deposited in Government Account)				
	Interest Accrued But Not Due A/c	...Dr.		2,025	
	TDS Collected (Receivable) A/c	...Dr.		225	
	To Interest Earned A/c				2,250
	(Being the interest on fixed deposit @ 6% provided, TDS was deducted by Bank @ 10%)				
	Debentures Redemption Reserve A/c	...Dr.		62,500	
	To General Reserve A/c				62,500
	(Being the amount proportionate to debentures redeemed transferred to General Reserve)				
	Statement of Profit and Loss	...Dr.		40,000	
	To Interest on Debentures A/c				40,000
	(Being the interest transferred)				
	Interest Earned A/c	...Dr.		2,250	
	To Statement of Profit and Loss				2,250
	(Being the interest earned transferred)				
2017 March 31	Interest on Debentures A/c	...Dr.		20,000	
	To Debentureholders' A/c				18,000
	To TDS Payable A/c				2,000
	(Being the interest due on 5,000; 8% Debentures for one year and TDS deducted @ 10%)				
	Debentureholders' A/c	...Dr.		18,000	
	To Bank A/c				18,000
	(Being the interest on debentures paid)				
	TDS Payable A/c	...Dr.		2,000	
	To Bank A/c				2,000
	(Being the TDS deposited in Government Account)				
	Interest Accrued But Not Due A/c	...Dr.		2,025	
	TDS Collected (Receivable) A/c	...Dr.		225	
	To Interest Earned A/c				2,250
	(Being the interest on fixed deposit @ 6% provided, TDS was deducted by Bank @ 10%)				

	Interest Receivable A/c ...Dr.		8,100	
	To Interest Accrued But Not Due A/c*			8,100
	(Being the Interest Accrued became due)			
	Bank A/c ...Dr.		45,600	
	To Debentures Redemption Investment A/c			37,500
	To Interest Receivable A/c			8,100
	(Being the Investment made in fixed deposit realised)			
	Debentures Redemption Reserve A/c ...Dr.		62,500	
	To General Reserve A/c			62,500
	(Being the amount of DRR transferred to General Reserve)			
	Statement of Profit and Loss ...Dr.		20,000	
	To Interest on Debentures A/c			20,000
	(Being the interest transferred)			
	Interest Earned A/c ...Dr.		2,250	
	To Statement of Profit and Loss			2,250
	(Being the interest earned transferred)			

*Interest Accrued but not due on 31st March, 2017 = ₹ 2,025 (31st March, 2014) + ₹ 2,025 (31st March, 2015) + ₹ 2,025 (31st March, 2016) + ₹ 2,025 (31st March, 2017) = ₹ 8,100.

Illustration 7.

Master Business Ltd., on 1st July, 2012 issued 27,500, 8% Debentures of ₹ 50 each at a premium of 10% redeemable at a premium of 20% in five equal annual instalments either by draw of lots or by purchase from the open market beginning 31st March, 2015. Interest on debentures is payable yearly on 31st March on which TDS is 10%. Applications were received for 25,000 debentures.

The terms and conditions of issue of debentures provided that the company shall, as far as possible, purchase debentures from open market and if the debentures could not be purchased from open market then it will resort to redemption by draw of lots. In case, debentures were to be redeemed by draw of lots, the debentureholders will be paid nominal (face) value and premium on redemption of debentures.

The company decided to set aside to DRR an amount as prescribed in law in two equal instalments in the years ended 31st March, 2013 and 2014. The company also decided to invest amount as required in fixed deposit on 1st April, 2014 with Canara Bank earning 10% interest to be realised at the time of last redemption. Bank deducts TDS every year on interest @ 10%.

The company purchased 5,000, 8% Debentures on 31st March, 2015 at an average price of ₹ 52 and cancelled them.

The company, on 31st March, 2016, purchased 2,500, 8% Debentures @ ₹ 62 per debenture and 1,500, 8% Debentures @ ₹ 61 per debenture. Balance debentures were redeemed by draw of lots.

The company could not purchase any debenture from open market in the year ended 31st March, 2017 and thus, had to resort to redemption by draw of lots.

Pass Journal entries according to the above transactions for the years ended 31st March, 2015, 2016 and 2017. Also prepare Debentures Redemption Reserve Account, Interest Accrued But Not Due Account, TDS Payable and TDS Receivable Account.

Solution: JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2013					
July 1	Bank A/c	...Dr.		13,75,000	
	To Debentures Application and Allotment A/c				13,75,000
	(Being the applications received for 25,000, 8% Debentures @ ₹ 55 each)				
	Debentures Application and Allotment A/c	...Dr.		13,75,000	
	Loss on Issue of Debentures A/c	...Dr.		2,50,000	
	To 8% Debentures A/c				12,50,000
	To Securities Premium Reserve A/c				1,25,000
	To Premium on Redemption of Debentures A/c				2,50,000
	(Being the debentures issued at a premium of 10% redeemable at 20% premium)				
2013					
March 31	Interest on Debentures A/c	...Dr.		75,000	
	To Debentureholders' A/c				67,500
	To TDS Payable A/c				7,500
	(Being the interest due on debentures @ 8% p.a. for nine months and TDS deducted @ 10%)				
	Debentureholders' A/c	...Dr.		67,500	
	To Bank A/c				67,500
	(Being the interest on debentures paid)				
	TDS Payable A/c	...Dr.		7,500	
	To Bank A/c				7,500
	(Being the TDS deposited in Government Account)				
	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c	...Dr.		1,56,250	
	To Debentures Redemption Reserve A/c				1,56,250
	(Being one-half of total DRR required transferred)				
	Securities Premium Reserve A/c	...Dr.		1,25,000	
	Statement of Profit and Loss	...Dr.		1,25,000	
	To Loss on Issue of Debentures A/c				2,50,000
	(Being the loss written off)				
	Statement of Profit and Loss	...Dr.		75,000	
	To Interest on Debentures A/c				75,000
	(Being the interest on debentures transferred)				
2014					
March 31	Interest on Debentures A/c	...Dr.		1,00,000	
	To Debentureholders' A/c				90,000
	To TDS Payable A/c				10,000
	(Being the interest due on debentures @ 8% p.a. for one year and TDS deducted @ 10%)				
	Debentureholders' A/c	...Dr.		90,000	
	To Bank A/c				90,000
	(Being the interest on debentures paid)				
	TDS Payable A/c	...Dr.		10,000	
	To Bank A/c				10,000
	(Being the TDS deposited in Government Account)				
	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c	...Dr.		1,56,250	
	To Debentures Redemption Reserve A/c				1,56,250
	(Being one-half of total DRR required transferred)				

	Statement of Profit and Loss ...Dr. To Interest on Debentures A/c (Being the interest transferred)		1,00,000	1,00,000
April 1	Debentures Redemption Investment A/c ...Dr. To Bank A/c (Being the investment made in fixed deposit with bank earning interest @ 10%)		37,500	37,500
2015 March 31	Interest on Debentures A/c ...Dr. To Debentureholders' A/c To TDS Payable A/c (Being the interest due on 20,000, 8% Debentures @ 8% p.a. for one year and TDS deducted @ 10%)		80,000	72,000 8,000
	Debentureholders' A/c ...Dr. To Bank A/c (Being the interest on debentures paid)		72,000	72,000
	TDS Payable A/c ...Dr. To Bank A/c (Being the TDS deposited in Government Account)		8,000	8,000
	Interest Accrued But Not Due A/c ...Dr. TDS Collected (Receivable) A/c ...Dr. To Interest Earned A/c (Being the interest on fixed deposit @ 10% provided, TDS was deducted by Bank @ 10%)		3,375 375	3,750
	Own Debentures A/c ...Dr. To Bank A/c (Being own 5,000, 8% Debentures purchased at all average price of ₹ 52)		2,60,000	2,60,000
	8% Debentures A/c ...Dr. Premium on Redemption of Debentures A/c ...Dr. To Own Debentures A/c To Gain (Profit) on Cancellation of Own Debentures A/c (Being 5,000 Own Debentures cancelled resulting in a gain)		2,50,000 50,000	2,60,000 40,000
	Gain (Profit) on Cancellation of Own Debentures A/c ...Dr. To Capital Reserve A/c (Being the gain (profit) on Cancellation transferred)		40,000	40,000
	Debentures Redemption Reserve A/c ...Dr. To General Reserve A/c (Being the amount proportionate to debentures redeemed transferred to General Reserve)		62,500	62,500
	Statement of Profit and Loss ...Dr. To Interest on Debentures A/c (Being the interest transferred)		80,000	80,000
	Interest Earned A/c ...Dr. To Statement of Profit and Loss (Being the interest earned transferred)		3,750	3,750
2016 March 31	Interest on Debentures A/c ...Dr. To Debentureholders' A/c To TDS Payable A/c (Being the interest due on 15,000 Debentures @ 8% p.a. for one year and TDS deducted @ 10%)		60,000	54,000 6,000

	Debentureholders' A/c ...Dr.	54,000	
	To Bank A/c		54,000
	(Being the interest on debentures paid)		
	TDS Payable A/c ...Dr.	6,000	
	To Bank A/c		6,000
	(Being the TDS deposited in Government Account)		
	Interest Accrued But Not Due A/c ...Dr.	3,375	
	TDS Collected (Receivable) A/c ...Dr.	375	
	To Interest Earned A/c		3,750
	(Being the interest on fixed deposit @ 10% provided, TDS was deducted by Bank @ 10%)		
	Own Debentures A/c ...Dr.	2,46,500	
	To Bank A/c		2,46,500
	(Being own 2,500, 8% Debentures purchased @ ₹ 62 each, 1,500, 8% Debentures @ ₹ 61 each)		
	8% Debentures A/c ...Dr.	2,00,000	
	Premium on Redemption of Debentures A/c ...Dr.	40,000	
	Loss on Cancellation of Own Debentures A/c ...Dr.	6,500	
	To Own Debentures A/c		2,46,500
	(Being 4,000 Own Debentures cancelled resulting in a loss)		
	Capital Reserve A/c ...Dr.	6,500	
	To Loss on Cancellation of Own Debentures A/c		6,500
	(Being the loss on Cancellation of Own debentures set off from Capital Reserve)		
	8% Debentures A/c ...Dr.	50,000	
	Premium on Redemption of Debentures A/c ...Dr.	10,000	
	To Debentureholders' A/c		60,000
	(Being amount due to debentureholders)		
	Debentureholders' A/c ...Dr.	60,000	
	To Bank A/c		60,000
	(Being payment made to debentureholders)		
	Debentures Redemption Reserve A/c ...Dr.	62,500	
	To General Reserve A/c		62,500
	(Being the amount proportionate to debentures redeemed transferred to General Reserve)		
	Statement of Profit and Loss ...Dr.	60,000	
	To Interest on Debentures A/c		60,000
	(Being the interest transferred)		
	Interest Earned A/c ...Dr.	3,750	
	To Statement of Profit and Loss		3,750
	(Being the interest earned transferred)		
2017 March 31	Interest on Debentures A/c ...Dr.	40,000	
	To Debentureholders' A/c		36,000
	To TDS Payable A/c		4,000
	(Being the interest due on 10,000, 8% Debentures @ 8% p.a. for one year and TDS deducted @ 10%)		

	Debentureholders' A/c ...Dr. To Bank A/c (Being the interest on debentures paid)		36,000	36,000
	TDS Payable A/c ...Dr. To Bank A/c (Being the TDS deposited in Government Account)		4,000	4,000
	Interest Accrued But Not Due A/c ...Dr. TDS Collected (Receivable) A/c ...Dr. To Interest Earned A/c (Being the interest on fixed deposit @ 10% provided, TDS was deducted by Bank @ 10%)		3,375 375	3,750
	8% Debentures A/c ...Dr. Premium on Redemption of Debentures A/c ...Dr. To Debentureholders' A/c (Being 5,000; 8% Debentures due for redemption)		2,50,000 50,000	3,00,000
	Debentureholders' A/c ...Dr. To Bank A/c (Being the payment made to debentureholders)		3,00,000	3,00,000
	Debentures Redemption Reserve A/c ...Dr. To General Reserve A/c (Being the amount proportionate to debentures redeemed transferred to General Reserve)		62,500	62,500
	Statement of Profit and Loss ...Dr. To Interest on Debentures A/c (Being the interest on debentures transferred)		40,000	40,000
	Interest Earned A/c ...Dr. To Statement of Profit and Loss (Being the interest earned transferred)		3,750	3,750

Ledger Accounts

Dr. DEBENTURES REDEMPTION RESERVE ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2013 March 31	To Balance *c/d*	1,56,250	2013 March 31	By Surplus, *i.e.*, Balance in Statement of Profit and Loss	1,56,250
		1,56,250			1,56,250
2014 March 31	To Balance *c/d*	3,12,500	2013 April 1	By Balance *b/d*	1,56,250
			2014 March 31	By Surplus, *i.e.*, Balance in Statement of Profit and Loss	1,56,250
		3,12,500			3,12,500
2015 March 31	To General Reserve A/c	62,500	2014 April 1	By Balance *b/d*	3,12,500
	To Balance *c/d*	2,50,000			
		3,12,500			3,12,500
2016 March 31	To General Reserve A/c	62,500	2015 April 1	By Balance *b/d*	2,50,000
	To Balance *c/d*	1,87,500			
		2,50,000			2,50,000
2017 March 31	To General Reserve A/c	62,500	2016 April 1	By Balance *b/d*	1,87,500
	To Balance *c/d*	1,25,000			
		1,87,500			1,87,500

Dr. INTEREST ACCRUED BUT NOT DUE ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2015			2015		
March 31	To Interest Earned A/c	3,375	March 31	By Balance *c/d*	3,375
		3,375			3,375
2015			2016		
April 1	To Balance *b/d*	3,375	March 31	By Balance *c/d*	6,750
2016					
March 31	To Interest Earned A/c	3,375			
		6,750			6,750
2016			2017		
April 1	To Balance *b/d*	6,750	March 31	By Balance *c/d*	10,125
2017					
March 31	To Interest Earned A/c	3,375			
		10,125			10,125

Dr. TDS PAYABLE ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2013			2013		
March 31	To Bank A/c	7,500	March 31	By Interest on Debentures A/c	7,500
2014			2014		
March 31	To Bank A/c	10,000	March 31	By Interest on Debentures A/c	10,000
2015			2015		
March 31	To Bank A/c	8,000	March 31	By Interest on Debentures A/c	8,000
2016			2016		
March 31	To Bank A/c	6,000	March 31	By Interest on Debentures A/c	6,000
2017			2017		
March 31	To Bank A/c	4,000	March 31	By Interest on Debentures A/c	4,000

Dr. TDS COLLECTED (RECEIVABLE) ACCOUNT *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2015			2015		
March 31	To Interest Earned A/c	375	March 31	By Balance *c/d*	375
		375			375
2015			2016		
April 1	To Balance *b/d*	375	March 31	By Balance *c/d*	750
2016					
March 31	To Interest Earned A/c	375			
		750			750
2016			2017		
April 1	To Balance *b/d*	750	March 31	By Balance *c/d*	1,125
2017					
March 31	To Interest Earned A/c	375			
		1,125			1,125

CHAPTER 9

Final Accounts of Companies—Application of Schedule III, Part I of the Companies Act, 2013

MEANING OF KEY TERMS USED IN THE CHAPTER

BALANCE SHEET

Equity and Liabilities

1. Shareholders' Funds

Shareholders' Funds are the funds of the shareholders of the company. It comprises of: Share Capital, Reserves and Surplus and Money Received against Share Warrants.

(*a*) Share Capital

It is the amount received by the company as capital. It includes both Equity Share Capital and Preference Share Capital.

(*b*) Reserves and Surplus

It is the amount set aside out of Surplus (profit) or received as Securities Premium Reserve. It may be free reserve or committed reserve.

(*c*) Money Received against Share Warrants

It is the amount received against Share Warrants. Share Warrant is a financial instrument which gives the holder the right to acquire Equity Shares specified therein at a specified date at a specified price.

2. Share Application Money Pending Allotment

It is the amount received as share application and against which the company will make allotment.

3. Non-Current Liabilities

Non-Current Liabilities are defined in Schedule III of the Companies Act, 2013 as those liabilities which are not Current Liabilities. These are sub-classified into: Long-term Borrowings; Deferred Tax Liabilities (Net); Other Long-term Liabilities and Long-term Provisions.

(*a*) Long-term Borrowings

Long-term Borrowings are the borrowings which as on the date of borrowings, are repayable after more than 12 months from the date of Balance Sheet or after the period of Operating Cycle.

(*b*) Deferred Tax Liabilities (Net)

It is the amount of tax on the temporary difference between the accounting income and taxable income. It is only a book entry and not an actual liability. It arises when accounting income is more than the taxable income.

(*c*) Other Long-term Liabilities

These are the liabilities, other than Long-term Borrowings of the company.

(*d*) Long-term Provisions

These are the provisions for liabilities that will be payable after 12 months from the date of Balance Sheet or after the period of Operating Cycle.

4. Current Liabilities

Current Liabilities are those liabilities which are:

(*a*) expected to be settled in company's normal Operating Cycle; or

(*b*) due to be settled within 12 months after the reporting date; (Reporting date is the date on which financial statements are prepared); or

(*c*) held primarily for the purpose of being traded; or

(*d*) there is no unconditional right to defer settlement for at least 12 months after the reporting date.

Current liabilities are classified into: Short-term Borrowings; Trade Payables; Other Current Liabilities; and Short-term Provisions.

(*a*) Short-term Borrowings

These are the borrowings which as on the date of borrowing, are repayable within 12 months from the date of Balance Sheet or within the period of a Operating Cycle.

(*b*) Trade Payables

These are the amounts payable for goods purchased or services taken in the normal course of business and are payable within 12 months from the date of Balance Sheet or within the period of a Operating Cycle.

(*c*) Other Current Liabilities

These are short-term liabilities, other than short-term borrowings, trade payables and short-term provisions.

(*d*) Short-term Provisions

These are provisions for liabilities that will be payable within 12 months from the date of Balance Sheet or within the period of a Operating Cycle.

5. Operating Cycle

It is the time between the acquisition of assets for processing and their realisation into Cash and Cash Equivalents.

Where the Operating Cycle cannot be identified, it is assumed to be of 12 months.

Operating Cycle is determined for each business separately. It means a company can have more than one Operating Cycle.

ASSETS

6. Non-Current Assets

Non-Current Assets are those assets which are not Current Assets. These are sub-classified into: Fixed Assets; Non-Current Investments; Deferred Tax Assets (Net); Long-term Loans and Advances; and Other Non-Current Assets.

(*a*) Fixed Assets

(*i*) Tangible Assets

These are the assets which have physical existence. Examples are: land, building, machinery, computers, etc.

(*ii*) Intangible Assets

These are the assets which do not have physical existence. Examples are: patents, trademarks, computer software, etc.

(*iii*) Capital Work-in-Progress

Capital Work-in-Progress means expenditure incurred on construction or development of tangible assets.

(*iv*) Intangible Assets Under Development

Intangible Assets Under Development means expenditure incurred on development of intangible assets.

(*b*) Non-Current Investments

Non-Current Investments are those investments that are invested to be held for a period of more than 12 months from the date of Balance Sheet or after the period that is more than the period of a Operating Cycle.

A trade investment is Non-Current Investment when it is invested to be held for more than 12 months from the date of Balance Sheet or for a period that is more than the period of a Operating Cycle.

(*c*) Deferred Tax Assets (Net)

It is the amount of tax on the temporary difference between the accounting income and taxable income. It is only a book entry and not an actual asset. It arises when accounting income is less than the taxable income.

(*d*) Long-term Loans and Advances

Long-term Loans and Advances are loans and advances given by the company that are repayable or adjustable after 12 months from the date of Balance Sheet or after the period of Operating Cycle.

(*e*) Other Non-Current Assets

All Non-Current Assets that are not shown or classified under the above heads are Other Non-Current Assets.

7. Current Assets

Current Assets are those assets which are:

(*a*) expected to be realised in or intended for sale or consumption in normal Operating Cycle of the company; or

(*b*) held primarily for the purposes of trading; or

(*c*) expected to be realised within 12 months from the reporting date or closing date. (Reporting date is the date for which financial statements are prepared.); or

(*d*) Cash and Cash Equivalent unless it is restricted from being exchanged or used to settle a liability for at least 12 months after the reporting date.

Current Assets are classified into: Current Investments; Inventories; Trade Receivables; Cash and Cash Equivalents; Short-term Loans and Advances; and Other Current Assets.

(*a*) Current Investments

Current Investments are those investments that are invested to be held for a period of less than 12 months from the date of Balance Sheet or within the period of Operating Cycle.

(*b*) Inventories

Inventories mean stock. It is the tangible asset held

(*i*) for the purpose of sale in the normal course of business;

or

(*ii*) for the purpose of using it in the production of goods meant for sale or service to be rendered.

Inventory may be opening or closing inventory or both.

In case of trading company, it comprises of stock of goods traded in.

In case of a manufacturing company, it comprises of raw materials, work-in-progress and finished goods.

Inventories are valued at lower of cost or net realisable value, *i.e.*, market price.

(*c*) Trade Receivables

Trade Receivables are the amounts receivable for sale of goods or services rendered in the normal course of business receivable within 12 months of the reporting date or within the period of Operating Cycle.

(*d*) Cash and Cash Equivalents

It includes cash in hand and balance with bank.

(*e*) Short-term Loans and Advances

Short-term Loans and Advances are loans and advances given by the company that are repayable or adjustable within 12 months from the date of Balance Sheet or within the period of Operating Cycle.

(*f*) Other Current Assets

All other current assets that are not shown or classified under the above heads are Other Current Assets.

SUMMARY OF THE CHAPTER

- According to Section 2(40) of the Companies Act, 2013, Financial Statement includes:
  - (*i*) a Balance Sheet as at the end of the financial year;
  - (*ii*) a Profit and Loss Account (Statement of Profit and Loss);
  - (*iii*) Cash Flow Statement for the year;
  - (*iv*) a Statement of Changes in Equity, *if applicable;* and
  - (*v*) any explanatory note annexed to, or forming part of, any document referred to above.
- The form and contents of the Balance Sheet are prescribed in Schedule III, Part I of the Companies Act, 2013.
- **Balance Sheet:** Balance Sheet is a statement which shows the financial position of an enterprise as at a particular date. It lists the balances of various assets and liabilities as at a particular date.
- **Appropriation of Profit:** Profit is appropriated out of the balance in Surplus, *i.e.*, Balance in Statement of Profit and Loss under Reserves and Surplus. Profit for the year is transferred and added to the existing balance and appropriations (say transfer to Debenture Redemption Reserve, General Reserve, Workmen Compensation Reserve, Proposed Dividend, etc.) are deducted. Appropriations are shown under appropriate reserves (Debenture Redemption Reserve, General Reserve, Workmen Compensation Reserve, etc.). Proposed Dividend is shown under Short-term Provisions.

- **Provision:** Provision is the amount set aside to meet future liability, the amount of which cannot be determined with reasonable accuracy. Provisions are accounted in the books of account making the best estimate.
- **Reserve** means amount set aside out of profit and other surpluses to meet future uncertainties.

Loss on Issue of Debentures, Discount on Issue of Debentures, *Underwriting Commission and Preliminary Expenses* are written off in the year they are incurred from Securities Premium Reserve (if exists), or from Surplus, *i.e.*, Balance in Statement of Profit and Loss.

Solved Questions

Illustration 1.

Sharp Ltd. was formed on 1st December, 2013, with a capital of ₹ 5,00,000 divided into shares of ₹ 10 each. It offered 80% of the shares to the public.

The issue price was payable as follows:

30% of the face value per share was payable with application.

20% of the face value per share was payable with allotment.

The balance as and when required. The company did not call for the balance during the year.

All the shares offered by the company were subscribed for. The company did not receive the allotment money on 3,000 shares.

You are required to:

(*i*) Show the Share Capital in the Balance Sheet of the Company prepared as per Schedule III of the Companies Act, 2013 at the end of the financial year.

(*ii*) Prepare Notes to Accounts. (*ISC 2014, Modified as per Companies Act, 2013*)

Solution:

Sharp Ltd.

BALANCE SHEET *as at 31st March, 2014*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Share Capital	1	1,94,000
Total		1,94,000
II. ASSETS		
Current Assets		
Cash and Bank Balances	2	1,94,000
Total		1,94,000

Notes to Accounts

	₹
1. Share Capital	
Authorised Capital	
50,000 Shares of ₹ 10 each	5,00,000
Issued Capital	
40,000 Shares of ₹ 10 each	4,00,000
Subscribed Capital	
Subscribed but not fully paid-up:	
40,000 shares of ₹ 10 each, ₹ 5 called-up	2,00,000
Less: Calls-in-Arrears (3,000 × ₹ 2)	6,000
	1,94,000
2. Cash and Bank Balances	
Cash at Bank	1,94,000

Illustration 2.

Following balances have been extracted from the books of Robin Ltd. on 31st March, 2018:

Share Capital ₹ 10,00,000; (1,00,000 Equity Shares of ₹ 10 each) Securities Premium ₹ 1,00,000; 12% Debentures ₹ 5,00,000; Creditors ₹ 2,50,000; Balance—Profit and Loss (Dr.) ₹ 50,000; Livestock ₹ 9,00,000; Investments in Government Bonds ₹ 4,00,000; Work-in-Progress ₹ 4,00,000; Discount on Issue of 12% Debentures ₹ 1,00,000; Patents ₹ 40,000; Unclaimed Dividend ₹ 10,000; Accounts Receivable ₹ 20,000; and Fixed Deposits ₹ 50,000.

Prepare Balance Sheet of the company as per Schedule III, Part I of the Companies Act, 2013.

Proposed Dividend for the year is ₹ 50,000. *(ISC 2009, Modified)*

Solution:

Robin Ltd.

BALANCE SHEET *as at 31st March, 2018*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	10,00,000
(*b*) Reserves and Surplus	2	(50,000)
2. Non-Current Liabilities		
Long-term Borrowings	3	5,50,000
3. Current Liabilities		
(*a*) Trade Payables	4	2,50,000
(*b*) Other Current Liabilities	5	10,000
Total		17,60,000

II. ASSETS		
1. Non-Current Assets		
(*a*) Fixed Assets—Tangible	6	9,00,000
Intangible	7	40,000
Capital Work-in-Progress	8	4,00,000
(*b*) Non-Current Investments	9	4,00,000
2. Current Assets		
Trade Receivables	10	20,000
Total		17,60,000

Notes to Accounts

1. Share Capital		₹
Authorised Capital		
...Equity Shares of ₹ 10 each		...
Issued Capital		
1,00,000 Equity Shares of ₹ 10 each		10,00,000
Subscribed Capital		
Subscribed and Fully Paid-up:		
1,00,000 Equity Shares of ₹ 10 each		10,00,000
2. Reserves and Surplus		
Securities Premium Reserve	1,00,000	
Less: Discount on Issue of Debentures (W/o)	1,00,000	...
Surplus, *i.e.*, Balance in Statement of Profit and Loss		(50,000)
		(50,000)
3. Long-term Borrowings		
12% Debentures		5,00,000
Fixed Deposits		50,000
		5,50,000
4. Trade Payables		
Creditors		2,50,000
5. Other Current Liabilities		
Unclaimed Dividend		10,000
6. Fixed Assets—Tangible		
Livestock		9,00,000
7. Fixed Assets—Intangible		
Patents		40,000
8. Capital Work-in-Progress		
Work-in-Progress*		4,00,000
9. Non-Current Investments		
Government Bonds		4,00,000
10. Trade Receivables		
Accounts Receivable (Debtors)		20,000

*Work-in-Progress has been treated as Capital Work-in-Progress.

Illustration 3.

Following balances have been extracted from the books of King Furnishings Ltd. as at 31st March, 2018:

	₹		₹
Equity Share Capital (fully paid shares of ₹ 100 each)	4,00,000	Accumulated Depreciation	30,000
		Provision for Taxation	25,000
Fixed Assets (At cost)	6,60,000	Reserves and Surplus	1,00,000
Inventories	40,000	5% Debentures (secured against land)	2,00,000
Cash and Bank Balance	50,000	Unsecured Loan from Subsidiaries	50,000
Creditors	30,000	Underwriting Commission	5,000
Bills Receivable	20,000	Investments	70,000
		Interest accrued and due on 5% Debentures	10,000

You are required to prepare Balance Sheet of King Furnishings Ltd. as at 31st March, 2018, as prescribed under Schedule III of the Companies Act, 2013. *(ISC 2012, Modified)*

Solution:

BALANCE SHEET OF KING FURNISHINGS LTD.
as at 31st March, 2018

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	4,00,000
(*b*) Reserves and Surplus	2	95,000
2. Non-Current Liabilities		
Long-term Borrowings	3	2,50,000
3. Current Liabilities		
(*a*) Trade Payables	4	30,000
(*b*) Other Current Liabilities	5	10,000
(*c*) Short-term Provisions	6	25,000
Total		8,10,000
II. ASSETS		
1. Non-Current Assets		
(*a*) *Fixed Assets:*		
Tangible	7	6,30,000
(*b*) Non-Current Investments	8	70,000
2. Current Assets		
(*a*) Inventories		40,000
(*b*) Trade Receivables	9	20,000
(*c*) Cash and Bank Balances		50,000
Total		8,10,000

Notes to Accounts

		₹
1. Share Capital		
Authorised Capital		
... Equity Shares of ₹ 100 each		...
Issued Capital		
4,000 Equity Shares of ₹ 100 each		4,00,000
Subscribed Capital		
Subscribed and Fully Paid-up		
4,000 Equity Shares of ₹ 100 each		4,00,000
2. Reserves and Surplus		
Surplus, *i.e.*, Balance in Statement of Profit and Loss (Opening Balance)		1,00,000
Less: Underwriting Commission		5,000
		95,000
3. Long-term Borrowings		
5% Debentures		2,00,000
Loan from Subsidiary*		50,000
		2,50,000
*Loan from Subsidiary Company is Unsecured.		
4. Trade Payables		
Creditors		30,000
5. Other Current Liabilities		
Interest Accrued and Due on 5% Debentures		10,000
6. Short-term Provisions		
Provision for Taxation		25,000
7. Fixed Assets—Tangible		
Cost	6,60,000	
Less: Accumulated Depreciation	30,000	6,30,000
8. Non-Current Investments		
Investments		70,000
9. Trade Receivables		
Bills Receivable		20,000

Illustration 4.

From the list of following assets and liabilities, prepare Balance Sheet of the Company as per Schedule III, Part I of the Companies Act, 2013:

NISHANT COMPANY LTD.

Liabilities		₹	Assets		₹
Sundry Creditors		1,00,000	Cash at Bank		79,800
General Reserve		50,000	Cash in Hand		1,500
Accrued Interest on Debentures		28,000	Investments (Government Bonds)		95,000
Authorised Capital			Preliminary Expenses		9,000
1,20,000 Equity Shares of			Loans and Advances to Staff		95,000
₹ 10 per Share		12,00,000	Goodwill		50,000
Subscribed Capital			Building		6,00,000
80,000 Equity Shares of			Plant and Machinery	6,60,000	
₹ 10 each	8,00,000		*Less:* Depreciation	66,000	5,94,000
Less: Calls-in-Arrears	15,000	7,85,000	Stock-in-Trade		10,000
Surplus, *i.e.*, Balance in Statement of			Debtors	1,74,000	
Profit and Loss		75,000	*Less:* Provision for Doubtful Debts	8,700	1,65,300
6% Debentures		6,00,000	Furniture		14,400
Bills Payable		76,000			

Calls-in-Arrears are in respect of 5,000 Equity Shares being final call of ₹ 3 each.
There is a contingent liability in respect of a claim of ₹ 10,000 against the company not acknowledged as debt.

Solution:

Nishant Company Ltd.
BALANCE SHEET *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	7,85,000
(*b*) Reserves and Surplus	2	1,16,000
2. Non-Current Liabilities		
Long-term Borrowings	3	6,00,000
3. Current Liabilities		
(*a*) Trade Payables	4	1,76,000
(*b*) Other Current Liabilities	5	28,000
Total		17,05,000
II. ASSETS		
1. Non-Current Assets		
(*a*) Fixed Assets:		
Tangible Fixed Assets	6	12,08,400
Intangible Fixed Assets	7	50,000
(*b*) Non-Current Investments	8	95,000
2. Current Assets		
(*a*) Inventories	9	10,000
(*b*) Trade Receivables	10	1,65,300
(*c*) Cash and Bank Balances	11	81,300
(*d*) Short-term Loans and Advances	12	95,000
Total		17,05,000

Notes to Accounts

		₹
1. Share Capital		
Authorised Capital		
1,20,000 Equity Shares of ₹ 10 each		12,00,000
Issued Capital		
80,000 Equity Shares of ₹ 10 each		8,00,000
Subscribed Capital		
Subscribed and Fully Paid-up:		
75,000 Equity Shares of ₹ 10 each		7,50,000
Subscribed but not Fully Paid-up:		
5,000 Equity Shares of ₹ 10 each	50,000	
Less: Calls-in-Arrears	15,000	35,000
		7,85,000
2. Reserves and Surplus		
General Reserve		50,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	75,000	
Less: Preliminary Expenses written off	9,000	66,000
		1,16,000
3. Long-term Borrowings		
6% Debentures		6,00,000
4. Trade Payables		
Sundry Creditors		1,00,000
Bills Payable		76,000
		1,76,000

5. Other Current Liabilities		
Accrued Interest on Debentures		28,000
6. Tangible Fixed Assets		
(*i*) Building		6,00,000
(*ii*) Plant and Machinery	6,60,000	
Less: Depreciation	66,000	5,94,000
(*iii*) Furniture		14,400
		12,08,400
7. Intangible Fixed Assets		
Goodwill		50,000
8. Non-Current Investments		
Government Bonds		95,000
9. Inventories		
Stock-in-Trade		10,000
10. Trade Receivables*		
Debtors	1,74,000	
Less: Provision for Doubtful Debts	8,700	1,65,300
11. Cash and Bank Balances		
Cash in Hand		1,500
Cash at Bank		79,800
		81,300
12. Short-term Loans and Advances		
Advances to Staff		95,000
Contingent Liabilities		
A contingent liability in respect of claim of ₹ 10,000 is not acknowledged as debt.		

Illustration 5.

Following Ledger balances were extracted from the books of Varun Ltd. on 31st March, 2019:

Land and Building ₹ 2,00,000; 12% Debentures ₹ 2,00,000; Share Capital ₹ 10,00,000 (Equity Shares of ₹ 10 each Fully Paid up); Plant and Machinery ₹ 8,00,000; Goodwill ₹ 2,00,000; Investments in Shares of Raja Ltd. ₹ 2,00,000; General Reserve ₹ 2,00,000; Stock-in-Trade ₹ 1,00,000; Bills Receivable ₹ 1,00,000; Debtors ₹ 1,50,000; Creditors ₹ 1,00,000; Bank Loan (Unsecured) ₹ 1,00,000; Provision for Tax ₹ 55,000; and Discount on Issue of 12% Debentures ₹ 5,000.

Proposed Dividend for the year is ₹ 1,00,000.

You are required to prepare Balance Sheet of the company as per Schedule III, Part I of the Companies Act, 2013.

Solution:

Varun Ltd.

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	10,00,000
(*b*) Reserves and Surplus	2	1,95,000
2. Non-Current Liabilities		
Long-term Borrowings	3	3,00,000
3. Current Liabilities		
(*a*) Trade Payables	4	2,00,000
(*b*) Short-term Provisions	5	55,000
Total		17,50,000

II. ASSETS		
1. Non-Current Assets		
(*a*) *Fixed Assets:*		
(*i*) Tangible Assets	6	10,00,000
(*ii*) Intangible Assets	7	2,00,000
(*b*) Non-Current Investments	8	2,00,000
2. Current Assets		
(*a*) Inventories	9	1,00,000
(*b*) Trade Receivables	10	2,50,000
Total		17,50,000

Notes to Accounts

		₹
1. Share Capital		
Authorised Capital		
...Equity Shares of ₹ 10 each		...
Issued Capital		
1,00,000 Equity Shares of ₹ 10 each		10,00,000
Subscribed Capital		
Subscribed and Fully Paid-up:		
1,00,000 Equity Shares of ₹ 10 each		10,00,000
2. Reserves and Surplus		
General Reserve		2,00,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	...	
Less: Discount on Issue of 12% Debentures written off	5,000	(5,000)
		1,95,000
3. Long-term Borrowings		
12% Debentures		2,00,000
Bank Loan (Unsecured)		1,00,000
		3,00,000
4. Trade Payables		
Creditors		2,00,000
5. Short-term Provisions		
Provision for Tax		55,000
6. Fixed Assets—Tangible		
(*i*) Land and Building		2,00,000
(*ii*) Plant and Machinery		8,00,000
		10,00,000
7. Fixed Assets—Intangible		
Goodwill		2,00,000
8. Non-Current Investments		
Investments in Shares of Raja Ltd.		2,00,000
9. Inventories		
Stock-in-Trade		1,00,000
10. Trade Receivables		
Debtors		1,50,000
Bills Receivable		1,00,000
		2,50,000

Master Question and Advanced Level Questions

Illustration 6.

Ell Kay Ltd. is a company registered with authorised capital of 5,00,000 Equity Shares of ₹ 10 each and 50,000 Preference Shares of ₹ 100 each. It has existing paid-up capital as follows:

(*i*) 50,000 Equity Shares of ₹ 10 each,

(*ii*) 5,000, 10% Preference Shares of ₹ 100 each.

The amount received by the company as above is lying deposited in a Bank Account.

It purchased machinery from Excel Ltd. of ₹ 11,50,000 and paid the consideration by issuing cheque of ₹ 50,000 and balance by issuing 15% Preference Shares of ₹ 100 each at a premium of 10%.

It issued to public for subscription 2,00,000 Equity Shares of ₹ 10 each at a premium of ₹ 5 and also 25,000, 10% Preference Shares of ₹ 100 each at par. Amounts were payable as follows:

	Equity Shares (₹)	10% Preference Shares (₹)
On Application	5	50
On Allotment	8	30
On First and Final Call	Balance Amount	Balance Amount

Applications were received for 5,00,000 Equity Shares and 40,000 Preference Shares.

Equity Shares were allotted on *pro rata* basis to all the applicants and excess application money was retained to be adjusted towards allotment money and call money. Amount due on allotment and calls were received except allotment money on 1,000 Equity Shares from Anil and call money on 1,000 Equity Shares of Anil and 2,000 Equity Shares of Gopal. Shares of Anil were forfeited. Out of these forfeited shares, 500 Equity Shares were reissued at ₹ 15 each as fully paid-up.

Applications for 15,000, 10% Preference Shares were not allotted any share and amount was refunded. All amounts due on Preference Shares were received on due dates except first and final call on 1,000 Preference Shares. Amit holder of 500, 10% Preference Shares paid the call money together with allotment money.

Pass Journal entries, prepare Calls-in-Arrears and Calls-in-Advance Accounts and also the Balance Sheet.

Solution:

Ell Kay Ltd.

JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Machinery A/c	...Dr.		11,50,000	
	To Excel Ltd.				11,50,000
	(Being the machinery purchased from Excel Ltd.)				
	Excel Ltd.	...Dr.		11,50,000	
	To 15% Preference Share Capital A/c				10,00,000
	To Securities Premium Reserve A/c				1,00,000
	To Bank A/c				50,000
	(Being the amount due to Excel Ltd. settled)				
	Bank A/c	...Dr.		45,00,000	
	To Equity Shares Application A/c				25,00,000
	To Preference Shares Application A/c				20,00,000
	(Being the application money received for 5,00,000 Equity Shares @ ₹ 5 per Equity Share and 40,000, 10% Preference Shares @ ₹ 50 per Preference Share)				
	Equity Shares Application A/c	...Dr.		25,00,000	
	To Equity Share Capital A/c				10,00,000
	To Equity Shares Allotment A/c				15,00,000
	(Being the Equity Shares allotted on *pro rata* to all applicants and excess amount transferred to Equity Shares Allotment A/c)				
	Preference Shares Application A/c	...Dr.		20,00,000	
	To 10% Preference Share Capital A/c				12,50,000
	To Bank A/c				7,50,000
	(Being 25,000, 10% Preference Shares allotted to applicants of 25,000 Preference Shares and balance refunded)				
	Equity Shares Allotment A/c	...Dr.		16,00,000	
	To Equity Share Capital A/c				6,00,000
	To Securities Premium Reserve A/c				10,00,000
	(Being the allotment money due on 2,00,000 Equity Shares)				
	Preference Shares Allotment A/c	...Dr.		7,50,000	
	To 10% Preference Share Capital A/c				7,50,000
	(Being the allotment money due on 25,000, 10% Preference Shares)				
	Bank A/c (WN 1)	...Dr.		99,500	
	Calls-in-Arrears A/c (WN 1)	...Dr.		500	
	To Equity Shares Allotment A/c				1,00,000
	(Being the allotment money received after adjustment of advance and balance in arrears)				
	Bank A/c	...Dr.		7,60,000	
	To Preference Shares Allotment A/c				7,50,000
	To Calls-in-Advance A/c (500 × ₹ 20)				10,000
	(Being the due amount received against preference shares allotment)				
	Equity Shares First and Final Call A/c	...Dr.		4,00,000	
	To Equity Share Capital A/c				4,00,000
	(Being the first and final call due on 2,00,000 Equity Shares @ ₹ 2 each)				

	Preference Shares First and Final Call A/c ...Dr.		5,00,000	
	To 10% Preference Share Capital A/c			5,00,000
	(Being the first and final call due on 10% Preference Shares @ ₹ 20 each)			
	Bank A/c (WN 2) ...Dr.		3,94,000	
	Calls-in-Arrears A/c (WN 2) ...Dr.		6,000	
	To Equity Shares First and Final Call A/c			4,00,000
	(Being the first and final call amount received except on 3,000 Equity Shares)			
	Bank A/c ...Dr.		4,70,000	
	Calls-in-Advance A/c ...Dr.		10,000	
	Calls-in-Arrears A/c (1,000 × ₹ 20) ...Dr.		20,000	
	To Preference Shares First and Final Call A/c			5,00,000
	(Being the amount received and Calls-in-Advance adjusted, amount was not received on 1,000, 10% Preference Shares)			
	Equity Share Capital A/c ...Dr.		10,000	
	Securities Premium Reserve A/c ...Dr.		500	
	To Calls-in-Arrears A/c			2,500
	To Forfeited Shares A/c			8,000
	(Being 1,000 Equity Shares of Anil forfeited for non-payment of allotment money and first and final call)			
	Bank A/c ...Dr.		7,500	
	To Equity Share Capital A/c			5,000
	To Securities Premium Reserve A/c			2,500
	(Being 500 Equity Shares reissued at premium of ₹ 5 per share)			
	Forfeited Shares A/c ...Dr.		4,000	
	To Capital Reserve A/c			4,000
	(Being the gain on reissue transferred to Capital Reserve after reissue)			

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	10,00,000	By Preference Shares Application A/c	7,50,000
To Equity Shares Application A/c	25,00,000	By Excel Ltd.	50,000
To Preference Shares Application A/c	20,00,000	By Balance *c/d*	64,31,000
To Equity Shares Allotment A/c	99,500		
To Preference Shares Allotment A/c	7,50,000		
To Calls-in-Advance A/c	10,000		
To Equity Shares First and Final Call A/c	3,94,000		
To Preference Shares F and F Call A/c	4,70,000		
To Equity Share Capital A/c	5,000		
To Securities Premium Reserve A/c	2,500		
	72,31,000		72,31,000

Working Notes:

1. (*a*) *Amount received on Allotment of Equity Shares:*

	₹
Amount Due on Allotment	16,00,000
Less: Adjusted from Excess Shares Application Money	(15,00,000)
	1,00,000
Less: Amount not received on 1,000 Equity Shares of Anil (Note)	(500)
Amount Received	99,500

(*b*) *Amount not received from Anil:*

Shares allotted to Anil = 1,000

Shares applied by Anil = $\frac{1,000}{2,00,000} \times 5,00,000 = 2,500$

	₹
Application money received (2,500 × ₹5)	12,500
Less: Adjusted towards Shares Application (1,000 × ₹ 5)	(5,000)
Amount to be adjusted towards Shares Allotment	7,500
Less: Due on Allotment (1,000 × ₹ 8)	8,000
Amount not received on Allotment*	500

*Amount is not received towards Securities Premium Reserve since Calls-in-Advance is first appropriated towards Share Capital and thereafter towards Securities Premium.

2. *Amount received towards Equity Shares First and Final Call:*

	₹	₹
Amount Due		4,00,000
Less: Amount not received on:		
Anil's 1,000 Shares @ ₹ 2	(2,000)	
Gopal's 2,000 Shares @ ₹ 2	(4,000)	(6,000)
		3,94,000

Dr. CALLS-IN-ARREARS ACCOUNT (EQUITY SHARES) *Cr.*

Particulars	₹	Particulars	₹
To Equity Shares Allotment A/c	500	By Securities Premium Reserve A/c	500
To Equity Shares First and Final Call A/c	6,000	By Equity Share Capital A/c	2,000
		By Balance *c/d*	4,000
	6,500		6,500

Dr. CALLS-IN-ADVANCE ACCOUNT (PREFERENCE SHARES) *Cr.*

Particulars	₹	Particulars	₹
To Pref. Shares First and Final Call A/c	10,000	By Bank A/c (Received along with Pref. Shares Allotment)	10,000

Dr. CALLS-IN-ARREARS ACCOUNT (PREFERENCE SHARES) *Cr.*

Particulars	₹	Particulars	₹
To Pref. Shares First and Final Call A/c	20,000	By Balance *c/d*	20,000

Ell Kay Ltd.

BALANCE SHEET *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	64,75,000
(*b*) Reserves and Surplus	2	11,06,000
Total		75,81,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible	3	11,50,000
2. Current Assets		
Cash and Bank Balances	4	64,31,000
Total		75,81,000

Notes to Accounts

		₹
1. Share Capital		
Authorised Capital		
5,00,000 Equity Shares of ₹ 10 each		50,00,000
50,000 Preference Shares of ₹ 100 each		50,00,000
		1,00,00,000
Issued Capital		
2,50,000 Equity Shares of ₹ 10 each		25,00,000
30,000, 10% Preference Shares of ₹ 100 each		30,00,000
10,000, 15% Preference Shares of ₹ 100 each		10,00,000
(The above 15% Preference Shares have been issued to a Vendor for consideration other than cash pursuant to a contract)		
		65,00,000
Subscribed Capital		
Subscribed and Fully Paid-up		
2,47,500 Equity Shares of ₹ 10 each		24,75,000
10,000, 15% Preference Shares of ₹ 100 each		10,00,000
(The above 15% Preference Shares have been issued to a Vendor for consideration other than cash pursuant to a contract)		
29,000, 10% Preference Shares of ₹ 100 each		29,00,000
Subscribed but not Fully Paid-up		
2,000 Equity Shares of ₹ 10 each	20,000	
Less: Calls-in-Arrears	4,000	16,000
1,000, 10% Preference Shares of ₹ 100 each	1,00,000	
Less: Calls-in-Arrears	20,000	80,000
Add: Forfeited Shares		4,000
		64,75,000
2. Reserves and Surplus		
Capital Reserve		4,000
Securities Premium Reserve		11,02,000
		11,06,000
3. Fixed Assets—Tangible		
Machinery		11,50,000
4. Cash and Bank Balances		
Cash at Bank		64,31,000

Illustration 7.

Seaways Ltd. has an authorised capital of ₹ 1,20,000 divided into 2,000; 6% Preference Shares of ₹ 10 each and 10,000 Equity Shares of ₹ 10 each. The company commenced trading on 1st April, 2018.

Following balances were extracted from the books on 31st March, 2019:

Particulars	₹
Preference Share Capital (Fully paid)	20,000
Equity Share Capital (Fully called)	80,000
Calls-in-Arrears	2,000
Profit for the year ended 31st March, 2019	13,570
Premises (At cost)	68,000
Machinery (At cost)	30,000
Fixtures and Fittings (At cost)	6,000
Provision for Depreciation:	
Machinery	6,000
Fixtures and Fittings	600
Provision for Doubtful Debts	300
Stock	7,000
Debtors	6,300
Bank	2,000
Cash	70
Trade Creditors	900

The Directors decided to transfer ₹ 3,000 to reserve and to recommend a dividend of 10% on the Equity Shares.

Prepare Balance Sheet as at that date.

Solution:

Seaways Ltd.

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	98,000
(*b*) Reserves and Surplus	2	13,570
2. Current Liabilities		
(*a*) Trade Payables	3	900
(*b*) Short-term Provisions	4	300
Total		1,12,770
II. ASSETS		
1. Non-Current Assets		
Fixed Assets:		
Tangible Assets	5	97,400
2. Current Assets		
(*a*) Inventories	6	7,000
(*b*) Trade Receivables	7	6,300
(*c*) Cash and Bank Balances	8	2,070
Total		1,12,770

Notes to Accounts

			₹
1.	**Share Capital**		
	Authorised Capital		
	10,000 Equity Shares of ₹ 10 each		1,00,000
	2,000; 6% Preference Shares of ₹ 10 each		20,000
			1,20,000
	Issued Capital		
	8,000 Equity Shares of ₹ 10 each		80,000
	2,000; 6% Preference Shares of ₹ 10 each		20,000
			1,00,000
	Subscribed Capital		
	Subscribed and Fully Paid-up		
	2,000; 6% Preference Shares of ₹ 10 each		20,000
	Subscribed but not Fully Paid-up		
	8,000 Equity Shares of ₹ 10 each	80,000	
	Less: Calls-in-Arrears	2,000	78,000
			98,000
2.	**Reserves and Surplus**		
	General Reserve (transferred from Surplus, *i.e.*, Balance in Statement of Profit and Loss)		3,000
	Surplus, i.e., Balance in Statement of Profit and Loss:		
	Opening Balance	...	
	Add: Balance of Statement of Profit and Loss (Profit for the year)	13,570	
		13,570	
	Less: Appropriations:		
	General Reserve	3,000	10,570
			13,570
3.	**Trade Payables**		
	Trade Creditors		900
4.	**Short-term Provisions**		
	Provision for Doubtful Debts		300
5.	**Tangible Assets**		
	(*i*) Premises		68,000
	(*ii*) Machinery	30,000	
	Less: Provision for Depreciation	6,000	24,000
	(*iii*) Fixtures and Fittings	6,000	
	Less: Provision for Depreciation	600	5,400
			97,400
6.	**Inventories**		
	Stock		7,000
7.	**Trade Receivables**		
	Debtors		6,300
8.	**Cash and Bank Balances**		
	Cash in Hand		70
	Cash at Bank		2,000
			2,070

Note: Dividend has been proposed for the year ended 31st March, 2019:

On 6% Preference Shares	₹ 1,200
On Equity Shares	₹ 7,800

Illustration 8.

Following balances have been extracted from the books of Foresquare Ltd. as at 31st March, 2019:

	₹		₹
Equity Share Capital	10,00,000	Accumulated Depreciation	75,000
(fully paid shares of ₹ 100 each)		Provision for Tax	62,500
Fixed Assets (At cost)	16,50,000	Surplus, *i.e.*, Balance in Statement of Profit & Loss	2,37,500
Inventories	1,00,000	8% Debentures (secured against land)	5,00,000
Cash and Bank Balances	1,40,000	Unsecured Loan from Subsidiaries	1,25,000
Creditors	75,000	Investments (Non-current)	1,75,000
Bills Receivable	50,000	Interest accrued and due on 8% Debentures	40,000

You are required to prepare Balance Sheet of Foresquare Ltd. as at 31st March, 2019, as per Schedule III, Part I of the Companies Act, 2013.

Solution:

Foresquare Ltd.
BALANCE SHEET
as at 31st March, 2019

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	10,00,000
(*b*) Reserves and Surplus	2	2,37,500
2. Non-Current Liabilities		
Long-term Borrowings	3	6,25,000
3. Current Liabilities		
(*a*) Trade Payables	4	75,000
(*b*) Other Current Liabilities	5	40,000
(*c*) Short-term Provisions	6	62,500
Total		20,40,000
II. ASSETS		
1. Non-Current Assets		
(*a*) *Fixed Assets:*		
Tangible	7	15,75,000
(*b*) Non-Current Investments	8	1,75,000
2. Current Assets		
(*a*) Inventories		1,00,000
(*b*) Trade Receivables	9	50,000
(*c*) Cash and Bank Balances	10	1,40,000
Total		20,40,000

Notes to Accounts

		₹
1. Share Capital		
Authorised Capital		
... Equity Shares of ₹ 100 each		...
Issued Capital		
10,000 Equity Shares of ₹ 100 each		10,00,000
Subscribed Capital		
Subscribed and Fully Paid-up		
10,000 Equity Shares of ₹ 100 each		10,00,000
2. Reserves and Surplus		
Surplus, *i.e.*, Balance in Statement of Profit and Loss		2,37,500
3. Long-term Borrowings		
8% Debentures (Secured against Land)		5,00,000
Loan from Subsidiary		1,25,000
		6,25,000
4. Trade Payables		
Creditors		75,000
5. Other Current Liabilities		
Interest Accrued and Due on 8% Debentures		40,000
6. Short-term Provisions		
Provision for Tax		62,500
7. Fixed Assets—Tangible		
Cost	16,50,000	
Less: Accumulated Depreciation	75,000	15,75,000
8. Non-Current Investments		
Investments		1,75,000
9. Trade Receivables		
Bills Receivable		50,000
10. Cash and Bank Balances		
Cash and Bank Balance		1,40,000

Illustration 9.
From the details given below, prepare Balance Sheet of Silver Ore Co. Ltd. as at 31st March, 2019 as per Schedule III of the Companies Act, 2013:

	(₹ in '000)		(₹ in '000)
Balance in Statement of Profit and Loss (Dr.)	1,800	Trade Payables	750
10% Debentures	2,000	Calls-in-Advance	50
Proposed Dividend	200	Employees' Earned Leave Payable on Retirement	450
Equity Share Capital (₹ 100 each)	5,000	Inventories (Stores and Spares)	500
Cheques and Draft on Hand	480	Security Deposits for Telephone	50
12% Preference Share Capital (₹ 100 each)	4,000	Brands	1,100
Prepaid Expenses	500	Computer Software under development	200
Short-term Bank Loan	450	Trade Receivables	1,200
Interest accrued on Debentures of Tata Steels	120	Plant and Machinery	1,200
Building under construction	1,150	Investment in Land and Building	2,000
20,000, 12% Debentures of Tata Steel (₹ 100 each)	2,000	10% Debentures of Reliance Ltd.	1,000
Premium on Redemption of Debentures	200	(1/5th Redeemable within 1 year)	
Application Money Pending Allotment	400		

Solution:

Silver Ore Co. Ltd.
BALANCE SHEET *as at 31st March, 2019* (₹ in '000)

Particulars	Note No.	31st March, 2019 (₹)
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	9,000
(*b*) Reserves and Surplus	2	(1,800)
2. Share Application Money Pending Allotment		400
3. Non-Current Liabilities		
(*a*) Long-term Borrowings	3	2,200
(*b*) Long-term Provisions	4	450
4. Current Liabilities		
(*a*) Short-term Borrowings	5	450
(*b*) Trade Payables		750
(*c*) Other Current Liabilities	6	50
Total		11,500
II. ASSETS		
1. Non-Current Assets		
(*a*) *Fixed Assets:*		
(*i*) Tangible Assets (Plant and Machinery)		1,200
(*ii*) Intangible Assets (Brands)		1,100
(*iii*) Capital Work-in-Progress (Building under construction)		1,150
(*iv*) Intangible Assets Under Development (Computer Software under Development)		200
(*b*) Non-Current Investments	7	4,800
(*c*) Long-term Loans and Advances (Security Deposits)		50
2. Current Assets		
(*a*) Current Investments (1/5th Debentures of Reliance Ltd.)		200
(*b*) Inventories (Stores and Spares)		500
(*c*) Trade Receivables		1,200
(*d*) Cash and Bank Balances (Cheques and Draft)		480
(*e*) Other Current Assets	8	620
Total		11,500

Notes to Accounts (₹ in '000)

Particulars		₹
1. Share Capital		
Authorised Capital		
... Equity Shares of ₹ 100 each	...	
... 12% Preference Shares of ₹ 100 each	...	...
Issued Capital		
50,000 Equity Shares of ₹ 100 each	5,000	
40,000, 12% Preference Shares of ₹ 100 each	4,000	9,000
Subscribed Capital		
Subscribed and fully paid-up		
50,000 Equity Shares of ₹ 100 each	5,000	
20,000 Preference Shares of ₹ 100 each	4,000	9,000
2. Reserves and Surplus		
Surplus, *i.e.*, Balance in Statement of Profit and Loss (opening balance)	...	
Add: Loss as per Statement of Profit and Loss	(1,800)	(1,800)
3. Long-term Borrowings		
10% Debentures		2,000
Premium on Redemption of Debentures		200
		2,200
4. Long-term Provisions		
Employees' Earned Leave payable on Retirement		450
5. Short-term Borrowings		
Short-term Bank Loan		450
6. Other Current Liabilities		
Calls-in-Advance		50
7. Non-Current Investments		
20,000; 12% Debentures of Tata Steel (₹ 100 each)		2,000
10% Debentures of Reliance Ltd. (500 × 4/5th Redeemable after 12 months)		800
Investment in Land and Building		2,000
		4,800
8. Other Current Assets		
Prepaid Expenses		500
Interest Accrued on Debentures of Tata Steels		120
		620

Note: Proposed Dividend ₹ 2,00,000.

Unsolved Questions

1. *Z* Ltd. was registered on 1st April, 2017 with a nominal capital of ₹ 6,00,000 divided into 40,000 Equity Shares of ₹ 10 each and 20,000; 6% Preference Shares of ₹ 10 each.

TRIAL BALANCE
as at 31st March, 2018

Particulars	Dr. (₹)	Cr. (₹)
Net Profit for the year		58,000
Equity Share Capital; 20,000 shares of ₹ 10 each (Fully paid)		2,00,000
Preference Share Capital; 10,000 shares of ₹ 10 each (Fully paid)		1,00,000
Machinery (At cost)	35,000	
Premises (At cost)	60,000	
Debtors	80,000	
Creditors		20,000
Stock	1,60,000	
Office Furniture	6,000	
Cash at Bank	44,000	
Provision for Depreciation on Machinery		7,000
Total	3,85,000	3,85,000

It was decided:

(i) to transfer ₹ 10,000 to General Reserve.

(ii) to pay the dividend on the Preference Share Capital in full and to propose a dividend of 15% on the Equity Share Capital.

You are required to prepare Balance Sheet of the company as per Schedule III, Part I of the Companies Act, 2013.

2. Following Ledger balances were extracted from the books of Varun Ltd. on 31st March, 2019:

Land and Building ₹ 2,00,000; 12% Debentures ₹ 2,00,000; Share Capital ₹ 10,00,000 (Equity Shares of ₹ 10 each Fully Paid up); Plant and Machinery ₹ 8,00,000; Goodwill ₹ 2,00,000; Investments in Shares of Raja Ltd. ₹ 2,00,000; General Reserve ₹ 2,00,000; Stock-in-Trade ₹ 1,00,000; Bills Receivable ₹ 1,00,000; Debtors ₹ 1,50,000; Creditors ₹ 1,00,000; Bank Loan (Unsecured) ₹ 1,00,000; Provision for Tax ₹ 1,55,000; Discount on Issue of 12% Debentures ₹ 5,000.

You are required to prepare Balance Sheet of the company as per Schedule III, Part I of the Companies Act, 2013.

GUIDE TO ANSWERS

1. Dividend on Preference Shares—₹ 6,000 and on Equity Shares—₹ 30,000;

   Total of Balance Sheet—₹ 3,78,000.

2. Total of Balance Sheet—₹ 17,50,000.

CHAPTER 1

Financial Statement Analysis

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Analysis of Financial Statements

It is a systematic process of establishing, interpreting and analysing the quantitative relationship between the items, *i.e.*, components of financial statements to assess liquidity, solvency and profitability of the enterprise.

2. Comparative Financial Statements

Comparative Financial Statements are statements prepared to compare items, *i.e.*, components of:

- Financial Statements of an enterprise for two or more successive accounting periods, or
- Financial Statements of different enterprises for the same accounting period.

It is prepared separately for Balance Sheet and Statement of Profit and Loss.

3. Common-size Statements

Common-size Financial Statements are those statements in which reported amounts (figures) are converted to a common base. In the case of Common-size Statement of Profit and Loss, common base is Revenue from Operations, *i.e.*, Net Sales while in Common-size Balance Sheet, it is the total Assets or total of Equity and Liabilities.

4. Cash Flow Statement

Cash Flow Statement shows inflow or outflow of Cash and Cash Equivalents during a specific period.

5. Ratio Analysis

Analysis of financial statements on the basis of accounting ratios is known as **Ratio Analysis**.

6. Internal Analysis

It is conducted by those persons (management) who have access to the books of account to analyse the financial performance and position of the enterprise.

7. External Analysis

It is conducted by those persons who do not have access to the books of account to analyse the financial performance and position of the enterprise.

8. Horizontal (or Dynamic) Analysis

It is an analysis conducted to review and analyse financial statements of a number of years and, therefore, are based on financial data taken from those years.

9. Vertical (or Static) Analysis

It is an analysis conducted to review and analyse the financial statements of one accounting year only.

SUMMARY OF THE CHAPTER

- **Analysis of Financial Statements** is a systematic process of identifying the financial strengths and weaknesses of the firm by properly establishing relationships between the items of the Balance Sheet and Statement of Profit and Loss.

- **Tools or Techniques of Financial Statement Analysis**
  1. Comparative Financial Statements
  2. Common-size Financial Statements
  3. Cash Flow Statement
  4. Ratio Analysis.

- **Types of Financial Statement Analysis**
  1. External Analysis
  2. Internal Analysis
  3. Horizontal Analysis
  4. Vertical Analysis.

- **Objectives of Financial Analysis**
  1. To assess the enterprise's operating efficiency and profitability.
  2. To assess the financial stability of an enterprise.
  3. To assess the enterprise's short-term and long-term solvency.
  4. To compare intra-firm position, inter-firm position and pattern position within industry.
  5. To assess the future prospects of the enterprise.

- **Parties Interested in Financial Statement Analysis**
  1. Management,
  2. Employees and Trade Unions,
  3. Shareholders or Owners or Investors,
  4. Potential Investors,
  5. Suppliers or Creditors,
  6. Bankers and Lenders,
  7. Researchers,
  8. Government,
  9. Tax Authorities,
  10. Customers.

- **Limitations of Financial Statement Analysis**
  1. Analysis of Historical Data.
  2. Ignores price level changes.
  3. Qualitative aspect is ignored.
  4. Limitations of Financial Statements are also the limitations of Financial Statements Analysis.
  5. Not free from bias.
  6. Variation in Accounting Practices.
  7. Financial Analysis identifies the symptoms but does not suggest the diagnosis.
  8. Window Dressing.

CHAPTER 2

Comparative Statements and Common-Size Statements

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Comparative Financial Statements

Comparative Financial Statements are the statements prepared to compare items or components of:

- Financial Statements of an enterprise for two or more successive accounting periods (intra-firm), or
- Financial Statements of different enterprises for the same accounting periods (inter-firm).

It is prepared separately for Balance Sheet and Statement of Profit and Loss.

2. Comparative Balance Sheet

Comparative Balance Sheet is the horizontal analysis of Balance Sheet in which each item of Assets, Equity and Liabilities is analysed horizontally for two or more accounting periods.

3. Comparative Income Statement (Statement of Profit and Loss)

Comparative Income Statement is the horizontal analysis of Statement of Profit and Loss in which each item of Revenue and Expenses is analysed horizontally for two or more accounting periods.

4. Common-size Financial Statements

Common-size Financial Statements are the statements in which amounts of individual items of Balance Sheet and Statement of Profit and Loss for two or more years are written. These amounts are further converted into percentage to some common base.

5. Common-size Balance Sheet

Common-size Balance Sheet is a statement prepared to show each item or component of Balance Sheet as a percentage of total of Equity and Liabilities or total Assets taken as 100.

6. Common-size Income Statement

Common-size Income Statement is prepared to show each item or component of Statement of Profit and Loss as a percentage of Revenue from Operations, *i.e.*, Net Sales taken as 100.

SUMMARY OF THE CHAPTER

- **Comparative Financial Statement** is a tool of financial analysis that shows change in each item of the financial statements (Balance Sheet and Statement of Profit and Loss) in both absolute amount and percentage terms, taking the item in previous accounting period as base.
- **Significance or Purposes of Comparative Financial Statements**
  1. To know the nature of changes influencing financial position.
  2. To know the weaknesses and strengths about liquidity, profitability and solvency of the enterprise.
  3. To forecast and plan.
  4. To know the movements of key financial statistics.
- **Tools for Comparison**
  1. Comparative Balance Sheet.
  2. Comparative Income Statement, *i.e.*, Statement of Profit and Loss.
  3. Common-size Balance Sheet.
  4. Common-size Income Statement , *i.e.*, Statement of Profit and Loss.

- **Comparative Balance Sheet**

  "Comparative Balance Sheet analysis is the study of the trend of same items, group of items and computed items in two or more Balance Sheets of the same business enterprise on different dates." **—Foulka**

- **Comparative Income Statement, *i.e.*, Statement of Profit and Loss**

  A Comparative Income Statement or Comparative Statement of Profit and Loss shows the operating results for a number of accounting periods so that changes in data in terms of money and percentage from one period to another may be known.

- **Common-size Balance Sheet**

  Common-size Balance Sheet is the statement in which amounts of individual items of Balance Sheet for two or more years are written. These amounts are further converted into percentage to a common base which is total of Equity and Liabilities or total Assets.

- **Common-size Income Statement, *i.e.*, Statement of Profit and Loss.**

  Common-size Income Statement or Common-size Statement of Profit and Loss is the statement in which amounts of individual items of Statement of Profit and Loss for two or more years are written. These amounts are further converted into percentage to a common base which is Revenue from Operations.

Solved Questions

Illustration 1.

Prepare Comparative Income Statement (Statement of Profit and Loss) from the following information:

Year Ended 31st March, 2019:

Revenue from Operations—₹ 9,60,000, Cost of Revenue from Operations—₹ 5,80,000, Office and Administration Expenses—₹ 1,90,000, Selling and Distribution Expenses—₹ 70,000 and Other Expenses—₹ 5,000.

Year Ended 31st March, 2018:

Revenue from Operations—₹ 8,00,000, Cost of Revenue from Operations—₹ 5,00,000, Office and Administration Expenses—₹ 1,40,000, Selling and Distribution Expenses—₹ 90,000 and Other Expenses—₹ 10,000.

Solution: COMPARATIVE INCOME STATEMENT OR COMPARATIVE STATEMENT OF PROFIT AND LOSS

for the years ended 31st March, 2019 and 2018

Particulars	Note No.	31st March, 2019 ₹	31st March, 2018 ₹	Absolute Change (Increase/Decrease) ₹	Percentage Change (Increase/Decrease) %
I. Revenue from Operations		9,60,000	8,00,000	1,60,000	20.00
II. Expenses					
Cost of Revenue from Operations		5,80,000	5,00,000	80,000	16.00
Office and Administration Exp.		1,90,000	1,40,000	50,000	35.71
Selling and Distribution Exp.		70,000	90,000	(20,000)	(22.22)
Other Expenses		5,000	10,000	(5,000)	(50.00)
Total Expenses		8,45,000	7,40,000	1,05,000	14.19
III. Net Profit (I – II)		1,15,000	60,000	55,000	91.67

Illustration 2.

From the Statement of Profit and Loss, prepare Comparative Income Statement of Exe Ltd.:

Particulars	Note No.	31st March, 2019 ₹	31st March, 2018 ₹
I. Income			
Revenue from Operations		33,00,000	30,00,000
Other Income		60,000	60,000
Total		33,60,000	30,60,000
II. Expenses			
Purchases of Stock-in-Trade		24,00,000	23,00,000
Change in Inventory of Stock-in-Trade		1,20,000	1,00,000
Employees Benefit Expenses		90,000	70,000
Finance Costs		60,000	60,000
Other Expenses		90,000	80,000
Total		27,60,000	26,10,000
III. Profit (I – II)		6,00,000	4,50,000
IV. *Less:* Tax		3,00,000	2,25,000
V. Profit after Tax (III – IV)		3,00,000	2,25,000

Solution:

Exe Ltd.

COMPARATIVE INCOME STATEMENT OR COMPARATIVE STATEMENT OF PROFIT AND LOSS

for the years ended 31st March, 2019 and 2018

Particulars	Note No.	31st March, 2019 ₹	31st March, 2018 ₹	Absolute Change (Increase/ Decrease) ₹	Percentage Change (Increase/ Decrease) %
I. Revenue from Operations		33,00,000	30,00,000	3,00,000	10.00
II. Other Income		60,000	60,000	...	...
III. Total Revenue		33,60,000	30,60,000	3,00,000	9.80
IV. Expenses					
Purchases of Stock-in-Trade		24,00,000	23,00,000	1,00,000	4.35
Change in Inventory of Stock-in-Trade		1,20,000	1,00,000	20,000	20.00
Employees Benefit Expenses		90,000	70,000	20,000	28.57
Finance Costs		60,000	60,000	...	...
Other Expenses		90,000	80,000	10,000	12.50
Total Expenses		27,60,000	26,10,000	1,50,000	5.75
V. Profit before Tax (III – IV)		6,00,000	4,50,000	1,50,000	33.33
VI. *Less:* Tax		3,00,000	2,25,000	75,000	33.33
VII. Profit after Tax (V – VI)		3,00,000	2,25,000	75,000	33.33

Illustration 3.

From the following Balance Sheet of Sun Ltd. as at 31st March, 2019, prepare Common-size Balance Sheet:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		80,00,000	60,00,000
(*b*) Reserves and Surplus		12,00,000	8,00,000
2. Non-Current Liabilities			
Long-term Borrowings		24,00,000	20,00,000
3. Current Liabilities			
Short-term Borrowings		4,00,000	12,00,000
Total		1,20,00,000	1,00,00,000
II. ASSETS			
1. Non-Current Assets			
Fixed Assets:			
(*i*) Tangible Assets		80,00,000	60,00,000
(*ii*) Intangible Assets		4,00,000	12,00,000
2. Current Assets			
(*a*) Inventories		24,00,000	20,00,000
(*b*) Cash and Bank Balances		12,00,000	8,00,000
Total		1,20,00,000	1,00,00,000

Solution:

Sun Ltd.
COMMON-SIZE BALANCE SHEET
as at 31st March, 2019 and 2018

Particulars	Note No.	Absolute Amounts		Percentage of Balance Sheet Total	
		31st March, 2019 (₹)	31st March, 2018 (₹)	31st March, 2019 (%)	31st March, 2018 (%)
I. EQUITY AND LIABILITIES					
1. Shareholders' Funds					
(*a*) Share Capital		80,00,000	60,00,000	66.67	60.00
(*b*) Reserves and Surplus		12,00,000	8,00,000	10.00	8.00
2. Non-Current Liabilities					
Long-term Borrowings		24,00,000	20,00,000	20.00	20.00
3. Current Liabilities					
Short-term Borrowings		4,00,000	12,00,000	3.33	12.00
Total		1,20,00,000	1,00,00,000	100.00	100.00
II. ASSETS					
1. Non-Current Assets					
Fixed Assets:					
(*i*) Tangible Assets		80,00,000	60,00,000	66.67	60.00
(*ii*) Intangible Assets		4,00,000	12,00,000	3.33	12.00
2. Current Assets					
(*a*) Inventories		24,00,000	20,00,000	20.00	20.00
(*b*) Cash and Bank Balances		12,00,000	8,00,000	10.00	8.00
Total		1,20,00,000	1,00,00,000	100.00	100.00

Illustration 4.

From the following Balance Sheet of *XYZ* Ltd. as at 31st March, 2019, prepare Common-Size Balance Sheet:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		10,00,000	5,00,000
(*b*) Reserves and Surplus		2,00,000	3,00,000
2. Non-Current Liabilities			
Long-term Borrowings: 12% Loans		8,00,000	5,00,000
3. Current Liabilities			
Trade Payables		4,00,000	2,00,000
Total		24,00,000	15,00,000
II. ASSETS			
1. Non-Current Assets			
Fixed Assets—Tangible		15,00,000	10,00,000
2. Current Assets			
Cash and Bank Balances		9,00,000	5,00,000
Total		24,00,000	15,00,000

Solution: COMMON-SIZE BALANCE SHEET of *XYZ* LTD. *as at 31st March, 2019 and 2018*

Particulars	Note No.	Absolute Amounts		Percentage of Balance Sheet Total	
		31st March, 2019 (₹)	31st March, 2018 (₹)	31st March, 2019 (%)	31st March, 2018 (%)
I. EQUITY AND LIABILITIES					
1. Shareholders' Funds					
(*a*) Share Capital		10,00,000	5,00,000	41.67	33.33
(*b*) Reserves and Surplus		2,00,000	3,00,000	8.33	20.00
2. Non-Current Liabilities					
Long-term Borrowings: 12% Loans		8,00,000	5,00,000	33.33	33.33
3. Current Liabilities					
Trade Payables		4,00,000	2,00,000	16.67	13.33
Total		24,00,000	15,00,000	100.00	100.00
II. ASSETS					
1. Non-Current Assets					
Fixed Assets—Tangible		15,00,000	10,00,000	62.50	66.67
2. Current Assets					
Cash and Bank Balances		9,00,000	5,00,000	37.50	33.33
Total		24,00,000	15,00,000	100.00	100.00

Note: Percentage is calculated on the basis of Total of Equity and Liabilities/Total Assets.

$$\text{Percentage of Share Capital (31st March, 2019)} = \frac{₹\,10,00,000}{₹\,24,00,000} \times 100 = 41.67\%$$

In the same manner other percentages are calculated.

Unsolved Question

1. The Balance Sheet of Blue Bell Ltd. as at 31st March, 2019 is given below:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
Share Capital		4,26,000	3,44,000
2. Non-Current Liabilities			
Long-term Borrowings		6,96,000	4,38,000
3. Current Liabilities			
Short-term Borrowings, Trade Payables, etc.		2,98,000	78,000
Total		14,20,000	8,60,000
II. ASSETS			
1. Non-Current Assets			
(a) Fixed Assets (Tangible Assets)		5,68,000	4,30,000
(b) Non-Current Investments		6,000	4,000
2. Current Assets			
Inventories, Trade Receivables, Cash and Bank Balances, etc.		8,46,000	4,26,000
Total		14,20,000	8,60,000

Prepare Comparative Balance Sheet showing percentage changes from 2018 to 2019.

GUIDE TO ANSWER

1.

Particulars	Share Capital	Long-term Borrowings	Current Liabilities	Fixed Assets	Non-current Investments	Current Assets
Absolute Change (₹)	82,000	2,58,000	2,20,000	1,38,000	2,000	4,20,000
Percentage Change (%)	23.84	58.90	282.05	32.09	50.00	98.59

CHAPTER 3

Cash Flow Statement—Based on Accounting Standard-3 (Revised)

(Only for Non-Financing Companies)

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Cash Flow Statement

It is the statement that shows flow of Cash and Cash Equivalents during the period under report.

2. Cash Flows

These are the inflows (receipts) and outflows (payments) of Cash and Cash Equivalents.

3. Cash

It comprises of Cash on Hand and demand deposits with banks.

4. Cash Equivalents

These are short-term, highly liquid investments that are readily convertible into known amount of cash and which are subject to an insignificant risk of change in value. An investment normally qualifies as cash equivalent only when it has short maturity period of, say, three months or less from the date of acquisition, *i.e.*, purchase.

Short-term Investments and Marketable Securities are taken as Cash and Cash Equivalents.

Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes.

5. Operating Activities

These are the principal revenue producing activities of the enterprise and other activities that are not Investing and Financing Activities.

6. Investing Activities

These are activities of acquisition and disposal of long-term assets and other investments not included in cash equivalents.

7. Financing Activities

These are the activities that result in change in the size and composition of the owner's capital (including preference share capital in the case of a company) and borrowings of the enterprise.

Bank Overdraft and Cash Credit are taken as Short-term Borrowings. Thus, they are shown under Financing Activities.

SUMMARY OF THE CHAPTER

- **Cash Flows** are the inflows and outflows of Cash and Cash Equivalents.
- **Cash Flow Statement** is a statement that shows the flow of Cash and Cash Equivalents during a period. This statement shows the net increase or net decrease of Cash and Cash Equivalents under each activity (operating/investing/financing) and collectively.
- **When does the Flow of Cash Arise?**

  Cash Flow arises when the net effect of transactions is *either to increase* or *to decrease* the amount of Cash or Cash Equivalents.
- Cash means Cash in Hand and Demand Deposits with Bank.
- **Cash Equivalents:** Cash Equivalents are short-term, highly liquid investments that are readily convertible into known amount of cash and which are subject to an insignificant risk of change in value. An investment normally qualifies as cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition.

  Examples of Cash Equivalents are: (*a*) Treasury bills, (*b*) Commercial papers, (*c*) money market funds and (*d*) Investment in Preference Shares redeemable within three months can also be taken as cash equivalents if there is insignificant risk of change in its value.

  Cash Equivalents also include Bank, Short-term Investments and Marketable Securities.
- **Operating Activities:** Operating Activities are the principal revenue producing activities of the enterprise and other activities that are not investing or financing activities.
- **Investing Activities:** Investing Activities are the acquisition and disposal of long-term assets and other investments not included in cash equivalents.
- **Financing Activities:** Financing Activities are the activities that result in change in the size and composition of the owners' capital (including Preference Share Capital in the case of a company) and borrowings of the enterprise.

Notes:
- Bank Overdraft and Cash Credit are treated as **Short-term Borrowings**. They are shown under **Financing Activities** in Cash Flow Statement.
- Current Investment is a part of Working Capital.
- Short-term Investment and Marketable Securities are part of Cash Equivalents.

- Proposed Dividend (also called **final dividend**) is the dividend proposed by the Board of Directors of the company but it is paid only after it is approved, *i.e.*, declared by the shareholders. Shareholders have the power to approve it, not approve it or approve it at a lower rate. In effect, declaration of final dividend is contingent on approval by the shareholders. Proposed Dividend is not accounted and shown as short-term provision in the Balance Sheet because it is prescribed by revised **Accounting Standard–4, Contingencies and Events Occurring After the Balance Sheet Date** that Proposed Dividend should not be provided in the books of account but should be shown in the Notes to Accounts.

Since, declaration and payment of dividend is contingent upon approval of the shareholders, it becomes a liability only after being approved by the shareholders. As a result, it will be accounted in the books of account in the next year after it is approved by the shareholders. *It means Proposed Dividend for the current year will be approved by the shareholders in the next year and thereafter it will be paid. Whereas Proposed Dividend for the previous year will be approved by the shareholders in the current year and will be paid in the current year.*

Dividend is an appropriation of profit and not a charge. Therefore, it is debited to Surplus, *i.e.*, Statement of Profit and Loss by passing the following entry:

Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c ...Dr.
    To Dividend Payable A/c
(Being the dividend declared)

The effect of this is as follows:

(*i*) Proposed Dividend for previous year is shown as outflow of cash assuming that the shareholders have approved the proposed dividend as was recommended;

(*ii*) No effect is given to Proposed Dividend for the current year as it is not provided for.

Dividend paid is debited to Dividend Payable Account and balance, if any is retained in '*Dividend Payable Account*' or may be transferred to *'Unpaid Dividend Account'* which is shown in the Balance Sheet as Other Current Liabilities under Current Liabilities.

Dividend paid during the year, whether out of Dividend Payable Account or Unpaid Dividend Account, is shown as Outflow of Cash (Cash Used) under Cash Flow from Financing Activities.

- **Preparation of Cash Flow Statement:** Cash Flow Statement is prepared following the steps as under:

Step 1: Compute Cash Flow from Operating Activities.

Step 2: Compute Cash Flow from Investing Activities.

Step 3: Compute Cash Flow from Financing Activities.

Step 4: The cash flows under each activity, *i.e.*, Operating Activity, Investing Activity and Financing Activity as computed in Steps 1, 2 and 3 are shown in Cash Flow Statement and net flow is determined. This will be Net Increase or Decrease in Cash and Cash Equivalents.

Step 5: Add Opening Cash and Cash Equivalents balance to cash flows as arrived at in Step 4.

Step 6: The amount so determined should be equal to Cash and Cash Equivalents balance at the end of the year.

TREATMENT OF MISCELLANEOUS EXPENDITURE

Miscellaneous Expenditure such as Loss on Issue of Debentures, Discount on Issue of Debentures, Underwriting Commission, Preliminary Expenses are written off in the year in which they are incurred from Securities Premium (if it exists) or from Statement of Profit and Loss.

Solved Questions

Illustration 1 (*Treatment of final Dividend Payable*).

Following figures have been taken from the Balance Sheet of *ABC* Ltd.

Particulars	31st March, 2018 ₹	31st March, 2019 ₹
Surplus, *i.e.*, Balance in Statement of Profit and Loss	3,00,000	5,40,000
Dividend Payable A/c	Nil	24,000

Additional Information: Dividend proposed for the year 2017-18 was ₹ 1,80,000 and for the current year 2018–19 is ₹ 2,16,000. Show how the related items will appear in Cash Flow Statement.

Solution: AN EXTRACT OF CASH FLOW STATEMENT *for the year ended 31st March, 2019*

Particulars	₹
A. Cash Flow from Operating Activities	
Closing Balance of Surplus, *i.e.*, Balance in Statement of Profit and Loss	5,40,000
Less: Opening Balance of Surplus, *i.e.*, Balance in Statement of Profit and Loss	3,00,000
	2,40,000
Add: Dividend declared in the AGM in the year 2018–19	1,80,000
Cash Flow from Operating Activities	4,20,000
B. Cash Flow from Financing Activities	
Payment of dividend during the year 2018–19 (WN)	1,56,000
Cash used in Financing Activities	1,56,000

Working Note:

Dr. DIVIDEND PAYABLE ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Bank A/c (Balancing Figure)	1,56,000	By Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c	1,80,000
To Balance *c/d*	24,000		
	1,80,000		1,80,000

Illustration 2.

Statement of Profit and Loss of *XYZ* Ltd. for the year ended 31st March, 2019 and additional information are given below. Calculate Cash Flow from Operating Activities.

STATEMENT OF PROFIT AND LOSS *for the year ended 31st March, 2019*

Particulars	Note No.	₹
I. Revenue from Operations (Net Sales)		18,00,000
II. Other Income	1	22,000
III. Total Revenue (I + II)		18,22,000
IV. *Expenses:*		
(*a*) Purchases of Stock-in-Trade		14,56,000
(*b*) Change in Inventories of Stock-in-Trade (Opening Inventories ₹ 80,000 and Closing Inventories ₹ 96,000)		(16,000)
(*c*) Employees Benefit Expenses		1,80,000
(*d*) Depreciation and Amortisation Expense		50,000
(*e*) Other Expenses	2	1,74,000
		18,44,000
V. Net Loss for the Year (III – IV)		(22,000)

Notes to Accounts

Particulars	₹
1. Other Income	
Rent	15,000
Miscellaneous	7,000
	22,000
2. Other Expenses	
Manufacturing Expenses	30,000
Insurance	9,000
Administration Expenses	47,000
Selling and Distribution Expenses	58,000
Loss on Sale of Assets	30,000
	1,74,000

Additional Information:	*31st March, 2019* (₹)	*31st March, 2018* (₹)
1. Wages Payable	10,000	...
2. Salaries Payable	25,000	...
3. Prepaid Insurance	3,000	...
4. Accrued Commission	7,000	...

Solution: CASH FLOW FROM OPERATING ACTIVITIES

Particulars		₹
Net Loss as per Statement of Profit and Loss before Tax		(22,000)
Adjustments for Non-Cash and Non-Operating Items:		
Add: Depreciation and Amortisation Expense	50,000	
Loss of Sale of Assets	30,000	80,000
		58,000
Less: *Non-Operating Income:* Other Incomes (Rent and Miscellaneous)		22,000
Operating Profit before Working Capital Changes		36,000
Add: *Increase in Current Liabilities:*		
Wages Payable	10,000	
Salaries Payable	25,000	35,000
		71,000
Less: *Increase in Current Assets:*		
Inventories (₹ 96,000 – ₹ 80,000)	16,000	
Accrued Commission	7,000	
Prepaid Insurance	3,000	26,000
Cash Flow from Operating Activities		45,000

Illustration 3.

Sainath Enterprises Ltd. issued 1,00,000 Equity Shares of ₹ 10 each to its existing shareholders on the condition that they shall also subscribe 10,000; 10% Debentures of ₹ 100 each at a premium of 10%.

All the shares and debentures were subscribed and amount was received.

The company incurred expenses on issue of shares and debentures amounting to ₹ 1,00,000. You are required to calculate Cash Flow from Financing Activities for the period.

Solution: CASH FLOW FROM FINANCING ACTIVITIES

Particulars	₹
Proceeds from Issue of Equity Shares	10,00,000
Proceeds from Issue of 10% Debentures	10,00,000
Receipt of Securities Premium on Issue of 10% Debentures	1,00,000
Expenses on Issue of Equity Shares and 10% Debentures	(1,00,000)
Cash Flow from Financing Activities	20,00,000

Note: Expenses on Issue of Equity Shares and 10% Debentures are written off from Securities Premium Reserve.

Illustration 4.

From the following extract taken from the Balance Sheet of Khanduja Ltd. as at 31st March and the information provided, you are required to calculate:

(*i*) Cash Flow from Operating Activities; (*ii*) Cash Flow from Financing Activities.

Particulars	31st March, 2018 (₹)	31st March, 2019 (₹)
Equity Share Capital	20,00,000	30,00,000
10% Preference Share Capital	2,00,000	1,00,000
Securities Premium Reserve	...	1,00,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	4,00,000	8,00,000
10% Debentures	10,00,000	10,00,000
Public Deposits	...	1,00,000
Premium on Redemption of Preference Shares	10,000	5,000

Information:

1. Preference Shares are redeemed at a premium of 5% on 1st April, 2018.
2. Final dividend on Preference Shares and an interim dividend on Equity Shares @ 8% was paid on 31st October, 2018.
3. Fresh Equity Shares were issued on 1st April, 2018.
4. Public Deposits were accepted on 31st March, 2019.

Solution:

(*i*) CASH FLOW FROM OPERATING ACTIVITIES

Particulars	₹
Net Profit before Tax (Note)	7,60,000
Cash Flow from Operating Activities	7,60,000

(*ii*) CASH FLOW FROM FINANCING ACTIVITIES

Particulars	₹
Proceeds from Issue of Equity Shares	10,00,000
Receipt of Securities Premium	1,00,000
Receipt of Public Deposits	1,00,000
Payment for Redemption of Preference Shares (including premium)	(1,05,000)
Dividend paid on Preference Shares	(20,000)
Interim Dividend paid on Equity Shares	(2,40,000)
Interest paid on Debentures	(1,00,000)
Cash Flow from Financing Activities	7,35,000

Note: ***Calculation of Net Profit before Tax:***

			₹
Closing Surplus, *i.e.*, Balance in Statement of Profit and Loss			8,00,000
Less:	Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss		4,00,000
			4,00,000
Add:	Dividend paid on Preference Shares	20,000	
	Interim Dividend on Equity Shares	2,40,000	
	Interest paid on Debentures	1,00,000	3,60,000
Net Profit before Tax			7,60,000

Illustration 5.

Prepare Cash Flow Statement from the Balance Sheet of P.S. Ltd. as at 31st March, 2019:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		2,50,000	2,00,000
(*b*) Reserves and Surplus	1	70,000	50,000
2. Non-Current Liabilities			
Long-term Borrowings	2	80,000	1,00,000
3. Current Liabilities			
(*a*) Trade Payables	3	1,60,000	60,000
(*b*) Other Current Liabilities	4	20,000	25,000
Total		5,80,000	4,35,000
II. ASSETS			
1. Non-Current Assets			
(*a*) *Fixed Assets:*			
(*i*) Tangible Assets	5	2,80,000	2,00,000
(*ii*) Intangible Assets	6	2,000	10,000
(*b*) Long-term Loans and Advances		1,30,000	1,00,000
2. Current Assets			
(*a*) Inventories		90,000	70,000
(*b*) Trade Receivables		60,000	40,000
(*c*) Cash and Bank Balances		18,000	15,000
Total		5,80,000	4,35,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Surplus, *i.e.*, Balance in Statement of Profit and Loss	70,000	50,000
2. Long-term Borrowings		
12% Debentures	80,000	1,00,000
3. Trade Payables		
Creditors	60,000	40,000
Bills Payable	1,00,000	20,000
	1,60,000	60,000
4. Other Current Liabilities		
Outstanding Expenses	20,000	25,000
5. Tangible Assets		
Land and Building	2,80,000	2,00,000
6. Intangible Assets		
Goodwill	2,000	10,000

Solution: CASH FLOW STATEMENT *for the year ended 31st March, 2019*

Particulars		₹
I. Cash Flow from Operating Activities		
Net Profit before Tax (Note 1)		20,000
Add: *Non-cash and Non-operating Expenses:*		
Goodwill Amortised	8,000	
Interest on 12% Debentures (Note 2)	12,000	20,000
Operating Profit before Working Capital Changes		40,000
Add: *Increase in Current Liabilities:*		
Creditors	20,000	
Bills Payable	80,000	1,00,000
		1,40,000
Less: *Increase in Current Assets and Decrease in Current Liabilities:*		
Outstanding Expenses	5,000	
Inventories	20,000	
Trade Receivables	20,000	45,000
Cash Flow from Operating Activities		95,000
II. Cash Flow from Investing Activities		
Purchase of Land and Building	(80,000)	
Loans and Advances	(30,000)	
Cash Used in Investing Activities		(1,10,000)
III. Cash Flow from Financing Activities		
Proceeds from Issue of Equity Shares	50,000	
Redemption of 12% Debentures	(20,000)	
Interest on 12% Debentures	(12,000)	
Cash Flow from Financing Activities		18,000
IV. Net Increase in Cash and Bank Balances (I + II + III)		3,000
V. Cash and Bank Balances in the beginning of the year		15,000
VI. Cash and Bank Balances at the end of the year (IV + V)		18,000

Notes:

1. ***Calculation of Net Profit before Tax:***

	₹
Closing Surplus, *i.e.*, Balance in Statement of Profit and Loss	70,000
Less: Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss	50,000
Net Profit before Tax	20,000

2. Debenture interest @ 12% on ₹ 1,00,000.

Preparation of Cash Flow Statement with Adjustments

Illustration 6.

The Balance Sheet of Rajneesh Ltd. as at 31st March, 2019 is as follows:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		1,25,000	1,00,000
(*b*) Reserves and Surplus	1	33,800	30,250
2. Non-Current Liabilities			
Long-term Borrowings (Debentures)		7,500	10,000
3. Current Liabilities			
(*a*) Short-term Borrowings	2	...	35,000
(*b*) Trade Payables		72,600	75,000
(*c*) Short-term Provisions	3	16,500	15,000
Total		2,55,400	2,65,250

II. ASSETS			
1. Non-Current Assets			
Fixed Assets: Tangible Assets	4	1,82,000	1,75,000
2. Current Assets			
(*a*) Inventories		37,000	50,000
(*b*) Trade Receivables		32,100	40,000
(*c*) Cash and Bank Balances		4,300	250
Total		2,55,400	2,65,250

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Surplus, *i.e.*, Balance in Statement of Profit and Loss	33,800	30,250
2. Short-term Borrowings		
Bank Overdraft	...	35,000
3. Short-term Provisions		
Provision for Tax	16,500	15,000
4. Fixed Assets (Tangible)		
Land and Building	95,000	1,00,000
Plant and Machinery	87,000	75,000
	1,82,000	1,75,000

Additional Information:

1. Depreciation written off on Building during the year ended 31st March, 2019 was ₹ 6,000.
2. Land was purchased for ₹ 19,000 during the year ended 31st March, 2019.

Prepare Cash Flow Statement of Rajneesh Ltd. (*ISC 2006, Modified*)

Solution:

Rajneesh Ltd.

CASH FLOW STATEMENT *for the year ended 31st March, 2019*

Particulars		₹	₹
I. Cash Flow from Operating Activities			
Net Profit before Tax (Note 1)		20,050	
Add: Non-cash Expenses:			
Depreciation on Land and Building		6,000	
Operating Profit before Working Capital Changes		26,050	
Add: Decrease in Current Assets:			
Inventories	13,000		
Trade Receivables	7,900	20,900	
		46,950	
Less: Decrease in Current Liabilities:			
Trade Payables	2,400	2,400	
Cash Flow from Operating Activities before Tax		44,550	
Less: Income Tax Paid		15,000	
Cash Flow from Operating Activities			29,550

II.	**Cash Flow from Investing Activities**		
	Sale of Land and Building (Note 2)	18,000	
	Purchase of Land and Building	(19,000)	
	Purchase of Plant and Machinery	(12,000)	
	Cash Used in Investing Activities		(13,000)
III.	**Cash Flow from Financing Activities**		
	Proceeds from Issue of Shares	25,000	
	Redemption of Debentures	(2,500)	
	Repayment of Bank Overdraft	(35,000)	
	Cash Used in Financing Activities		(12,500)
IV.	**Net Increase in Cash and Bank Balances (I + II + III)**		4,050
V.	Cash and Bank Balances in the beginning of the Period		250
VI.	**Cash and Bank Balances at the end of the Period (IV + V)**		4,300

Notes:

1. ***Calculation of Net Profit before Tax:***

	₹
Surplus, *i.e.*, Balance in Statement of Profit and Loss (Closing)	33,800
Less: Surplus, *i.e.*, Balance in Statement of Profit and Loss (Opening)	30,250
	3,550
Add: Provision for Tax (Current Year)	16,500
Net Profit before Tax	20,050

2. *Dr.* LAND AND BUILDING ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,00,000	By Depreciation A/c	6,000
To Bank A/c (Purchase)	19,000	By Bank A/c (Sale) (Balancing Figure)	**18,000**
		By Balance *c/d*	95,000
	1,19,000		1,19,000

3. Interest on debentures is not considered while computing Operating Profit before Working Capital Changes because rate of interest is not given.

Illustration 7.

The Balance Sheet of Copper & Company Ltd. as at 31st March, 2019 is given below:

BALANCE SHEET *as at...*

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		1,80,000	1,50,000
(*b*) Reserves and Surplus	1	1,00,000	80,000
2. Non-Current Liabilities			
Long-term Borrowings	2	1,89,000	1,31,000
3. Current Liabilities			
(*a*) Short-term Borrowings	3	1,000	3,000
(*b*) Trade Payable	4	14,000	14,000
Total		4,84,000	3,78,000

II. ASSETS			
1. Non-Current Assets			
Fixed Assets:			
(*a*) Tangible Assets	5	3,20,000	2,30,000
(*b*) Intangible Assets (Goodwill)		5,000	10,000
2. Current Assets			
(*a*) Inventories		75,000	60,000
(*b*) Trade Receivables	6	26,000	28,000
(*c*) *Cash and Bank Balances:* Cash		50,000	40,000
(*d*) Other Current Assets	7	8,000	10,000
Total		4,84,000	3,78,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
General Reserve	30,000	30,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	70,000	50,000
	1,00,000	80,000
2. Long-term Borrowings		
12% Debentures	69,000	51,000
12% Public Deposits	1,20,000	80,000
	1,89,000	1,31,000
3. Short-term Borrowings		
Cash Credit	1,000	3,000
4. Trade Payables		
Creditors	10,000	8,000
Bills Payable	4,000	6,000
	14,000	14,000
5. Fixed Assets (Tangible)		
Building	2,20,000	1,50,000
Plant	1,00,000	80,000
	3,20,000	2,30,000
6. Trade Receivables		
Debtors	17,000	20,000
Bills Receivable	9,000	8,000
	26,000	28,000
7. Other Current Assets		
Accrued Income	6,000	10,000
Prepaid Expenses	2,000	...
	8,000	10,000

Additional Information:

(*i*) Depreciation charged on Building ₹ 10,000.

(*ii*) Depreciation charged on Plant ₹ 5,000.

(*iii*) Interest paid on Debentures ₹ 7,200 for the year.

(*iv*) Interest paid on Public Deposits ₹ 9,600 for the year.

From the above information, prepare Cash Flow Statement as per Accounting Standard-3 for the year ended 31st March, 2019. (*ISC 2012, Modified*)

Solution: CASH FLOW STATEMENT *for the year ended 31st March, 2019*

Particulars		₹	₹
I. Cash Flow from Operating Activities			
Net Profit before Tax (WN 1)		20,000	
Add: Non-cash and Non-operating Items:			
Depreciation on Building		10,000	
Depreciation on Plant		5,000	
Interest on Debentures		7,200	
Goodwill Amortised		5,000	
Interest on Public Deposits		9,600	
Operating Profit before Working Capital Changes		56,800	
Add: Decrease in Current Assets and Increase in Current Liabilities:			
Debtors		3,000	
Accrued Income		4,000	
Creditors		2,000	
		65,800	
Less: Increase in Current Assets and Decrease in Current Liabilities:			
Inventories	15,000		
Bills Receivable	1,000		
Prepaid Expenses	2,000		
Bills Payable	2,000	20,000	
Cash Flow from Operating Activities			45,800
II. Cash Flow from Investing Activities			
Purchase of Building (WN 2)		(80,000)	
Purchase of Plant (WN 3)		(25,000)	
Cash Used in Investing Activities			(1,05,000)
III. Cash Flow from Financing Activities			
Proceeds from Issue of Share Capital		30,000	
Proceeds from Issue of 12% Debentures		18,000	
Proceeds from 12% Public Deposit		40,000	
Decrease in Cash Credit		(2,000)	
Interest paid on Debentures		(7,200)	
Interest paid on Public Deposits		(9,600)	
Cash Flow from Financing Activities			69,200
IV. Net Increase in Cash and Bank Balances (I + II + III)			10,000
V. Cash and Bank Balances in the beginning of year			40,000
VI. Cash and Bank Balances at the end of the year (IV + V)			50,000

Working Notes:

1. ***Calculation of Net Profit before Tax:***

	₹
Closing Surplus, *i.e.*, Balance in Statement of Profit and Loss	70,000
Less: Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss	50,000
Net Profit before Tax	20,000

2. *Dr.* BUILDING ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,50,000	By Depreciation A/c	10,000
To Bank A/c (Balancing Figure: Purchase)	**80,000**	By Balance *c/d*	2,20,000
	2,30,000		2,30,000

3. *Dr.* PLANT ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	80,000	By Depreciation A/c	5,000
To Bank A/c (Balancing Figure: Purchase)	**25,000**	By Balance *c/d*	1,00,000
	1,05,000		1,05,000

Illustration 8.

Calculate Operating Profit before Working Capital Changes from the following Balance Sheet and information of Grand Marketing Ltd. as at 31st March, 2019:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital	1	20,00,000	11,50,000
(*b*) Reserves and Surplus	2	4,90,000	2,05,000
2. Current Liabilities			
(*a*) Trade Payables		1,20,000	1,10,000
(*b*) Other Current Liabilities	3	15,000	20,000
(*c*) Short-term Provisions	4	2,50,000	2,00,000
Total		28,75,000	16,85,000
II. ASSETS			
1. Non-Current Assets			
(*a*) Fixed Assets—Tangible		17,50,000	8,85,000
(*b*) Non-Current Investments		5,00,000	5,00,000
2. Current Assets		6,25,000	3,00,000
Total		28,75,000	16,85,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Share Capital		
Equity Share Capital	10,00,000	7,50,000
Preference Share Capital	10,00,000	4,00,000
	20,00,000	11,50,000
2. Reserves and Surplus		
General Reserve	1,50,000	75,000
Investments Fluctuation Reserve	1,00,000	40,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	2,40,000	90,000
	4,90,000	2,05,000
3. Other Current Liabilities		
Outstanding Expenses	15,000	20,000
4. Short-term Provisions		
Provision for Tax	2,50,000	2,00,000

Note: Proposed Dividend for the years ended 31st March, 2019 and 2018 were ₹ 1,50,000 and ₹ 1,00,000 respectively.

Additional Information:

1. Depreciation for the year was ₹ 1,10,000.
2. Bad Debts written off amounted to ₹ 15,000.
3. Income included excess provision written back ₹ 5,000.
4. Dividend received on investments was ₹ 5,000.

Solution: Calculation of Operating Profit before Working Capital Changes

Particulars		₹
Net Profit before Tax (Note)		6,35,000
Add: *Non-cash Expenses:*		
(*a*) Depreciation	1,10,000	
(*b*) Bad Debts	15,000	1,25,000
		7,60,000
Less: *Non-cash Income:*		
Excess Provision written back		5,000
		7,55,000
Less: Non-operating Income (Dividend)		5,000
Operating Profit before Working Capital Changes		7,50,000

Note:

Net Profit before Tax

	₹
Net Profit for the year (Difference between Closing and Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss) (₹ 2,40,000 – ₹ 90,000)	1,50,000
Add: Transfer to General Reserve (₹ 1,50,000 – ₹ 75,000)	75,000
Investments Fluctuation Reserve (₹ 1,00,000 – ₹ 40,000)	60,000
Proposed Dividend (Previous Year)	1,00,000
Provision for Tax (Current Year)	2,50,000
Net Profit before Tax	6,35,000

Master Questions and Advanced Level Questions

Illustration 9.

From the following Balance Sheet of Clay Ltd., prepare Cash Flow Statement:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		8,00,000	5,00,000
(*b*) Reserves and Surplus	1	3,50,000	2,05,000
2. Non-Current Liabilities			
Long-term Borrowings (10% Debentures)		4,00,000	5,00,000
3. Current Liabilities			
(*a*) Short-term Borrowings (10% Bank Loan)		50,000	...
(*b*) Trade Payables	2	75,000	1,00,000
(*c*) Other Current Liabilities	3	30,000	...
(*d*) Short-term Provisions	4	65,000	50,000
Total		17,70,000	13,55,000

II. ASSETS			
1. Non-Current Assets			
(*a*) *Fixed Assets:*			
(*i*) Tangible Assets	5	5,20,000	7,00,000
(*ii*) Intangible Assets		50,000	1,00,000
(*b*) Non-current Investments (10% Non-current Investments)		1,60,000	60,000
2. Current Assets			
(*a*) Inventories		50,000	60,000
(*b*) Trade Receivables		80,000	40,000
(*c*) Cash and Bank Balances		9,10,000	3,95,000
Total		17,70,000	13,55,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Securities Premium Reserve		
Opening Balance	75,000	75,000
Less: Share Issue Expenses Written off	40,000	...
	35,000	75,000
Capital Reserve	...	5,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	3,15,000	1,25,000
	3,50,000	2,05,000
2. Trade Payables		
Trade Creditors	55,000	50,000
Bills Payable	20,000	50,000
	75,000	1,00,000
3. Other Current Liabilities		
Unpaid Dividend	20,000	...
Unpaid Interest on Debentures	10,000	...
	30,000	...
4. Short-term Provisions		
Provision for Tax	65,000	50,000
5. Fixed Assets (Tangible)		
Building	2,50,000	4,00,000
Plant and Machinery	2,70,000	3,00,000
	5,20,000	7,00,000

Note: Proposed Dividend for the years 2017–18 and 2018–19 are ₹ 1,15,000 and ₹ 1,25,000 respectively.

Additional Information:

1. Interim Dividend of ₹ 50,000 was paid during the year.
2. Share Issue Expenses of ₹ 40,000 were incurred and written off during the year 2018–19 from Securities Premium Reserve.
3. Tax of ₹ 60,000 was paid during the year.
4. Debentures were redeemed at par on 1st April, 2018 and Bank Loan was raised on the same date.
5. At the end of the year some Non-current Investments costing ₹ 40,000 were sold at a loss of 25% and some Non-current Investments costing ₹ 20,000 were sold at a profit of 25%. Profit/Loss on investments was adjusted against Capital Reserve. Additional Non-current investments were made on 31st March, 2019.

Solution:

Clay Ltd.

CASH FLOW STATEMENT *for the year ended 31st March, 2019*

Particulars	₹	₹
I. Cash Flow from Operating Activities		
Net Profit before Tax (Note 1)	4,30,000	
Add: Non-cash and Non-Operating Expenses:		
Intangible Fixed Assets Amortised (₹ 1,00,000 – ₹ 50,000)	50,000	
Depreciation on Plant and Machinery (₹ 3,00,000 – ₹ 2,70,000)	30,000	
Debentures Interest (₹ 4,00,000 × 10/100)	40,000	
Interest on Bank Loan (10% of ₹ 50,000)	5,000	
	5,55,000	
Less: Non-Operating Income:		
Interest on Non-current Investments	6,000	
Operating Profit before Working Capital Changes	5,49,000	
Add: Increase in Current Liabilities and Decrease in Current Assets:		
Trade Payables (Creditors)	5,000	
Inventories	10,000	
Less: Increase in Current Assets and Decrease in Current Liabilities:		
Trade Receivables	(40,000)	
Trade Payables	(30,000)	
Cash Generated from Operations	4,94,000	
Less: Tax paid	(60,000)	
Cash Flow from Operating Activities		4,34,000
II. Cash Flow from Investing Activities		
Proceeds from Sale of Building (₹ 4,00,000 – ₹ 2,50,000)	1,50,000	
Purchase of Non-current Investments	(1,60,000)	
Sale of Non-current Investment	55,000	
Interest on Non-current Investments	6,000	
Cash Flow from Investing Activities		51,000
III. Cash Flow from Financing Activities		
Proceeds from Issue of Shares	3,00,000	
Payment of Interim Dividend	(50,000)	
Final Dividend Paid (₹ 1,15,000 – ₹ 20,000)	(95,000)	
Redemption of 10% Debentures	(1,00,000)	
Interest on Debentures (₹ 40,000 – ₹ 10,000)	(30,000)	
Share Issue Expenses paid	(40,000)	
Proceeds of Bank Loan	50,000	
Interest on Bank Loan	(5,000)	
Cash Flow from Financing Activities		30,000
IV. Net Increase in Cash and Bank Balances (I + II + III)		5,15,000
V. *Add:* Opening Balance of Cash and Bank Balances		3,95,000
VI. Cash and Bank Balances at the end (IV + V)		9,10,000

Notes:

1. ***Calculation of Net Profit before Tax:***

	₹
Closing Surplus, *i.e.*, Balance in Statement of Profit and Loss	3,15,000
Less: Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss	1,25,000
	1,90,000
Add: Provision for Tax made during the Current Year	75,000
Dividend Paid for the Current Year (Proposed Dividend for 2017–18)	1,15,000
Interim Dividend	50,000
Net Profit before Tax	**4,30,000**

2. *Dr.* PROVISION FOR TAX ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Bank A/c (Tax Paid)	60,000	By Balance *b/d*	50,000
To Balance *c/d*	65,000	By Statement of Profit and Loss (Provision)	75,000
	1,25,000		1,25,000

3. Share Issue Expenses written off ₹ 40,000 will not be taken in Cash Flow from Operating Activities because it is written off from Securities Premium Reserve. It does not affect current year's profit.

4. *Dr.* 10% NON-CURRENT INVESTMENTS ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	60,000	By Bank A/c (Sale) [₹ 40,000 – ₹ 10,000 (Loss)]	30,000
To Capital Reserve A/c (Profit)	5,000	By Capital Reserve A/c (Loss)	10,000
To Bank A/c (Purchases)—Bal. Fig.	1,60,000	By Bank A/c (Sale)	25,000
		By Balance *c/d*	1,60,000
	2,25,000		2,25,000

5. Capital Reserve = ₹ 5,000 + ₹ 5,000 – ₹ 10,000 = Nil.

Or

Dr. CAPITAL RESERVE ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To 10% Non-current Investments A/c	10,000	By Balance *b/d*	5,000
		By 10% Non-current Investments A/c	5,000
	10,000		10,000

6. As the Profit/Loss on sale of Non-current Investments have been transferred to Capital Reserve and not to Statement of Profit and Loss, such Profit/Loss will not be adjusted to calculate Operating Profit.

Illustration 10.

From the following Balance Sheet of Grow More Ltd., prepare Cash Flow Statement:

BALANCE SHEET

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		10,00,000	8,00,000
(b) Reserves and Surplus	1	3,00,000	2,10,000
2. Non-Current Liabilities			
Long-term Borrowings (10% Debentures)		2,00,000	...
3. Current Liabilities			
(a) Trade Payables		7,00,000	8,20,000
(b) Short-term Provisions	2	1,00,000	70,000
Total		23,00,000	19,00,000
II. ASSETS			
1. Non-Current Assets			
(a) *Fixed Assets:* Tangible	3	13,00,000	9,00,000
(b) Non-current Investments		1,00,000	...
2. Current Assets			
(a) Inventories		4,00,000	2,00,000
(b) Trade Receivables		5,00,000	7,00,000
(c) Cash and Bank Balances		...	1,00,000
Total		23,00,000	19,00,000

Note: Dividend proposed for the years 2017–18 and 2018–19 are ₹ 2,00,000 and ₹ 2,50,000 respectively.

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
General Reserve	2,00,000	1,50,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	1,00,000	60,000
	3,00,000	2,10,000
2. Short-term Provisions		
Provision for Tax	1,00,000	70,000
3. Fixed Assets (Tangible)		
Plant and Machinery	7,00,000	5,00,000
Land and Building	6,00,000	4,00,000
	13,00,000	9,00,000

Additional Information:

1. Depreciation @ 25% was charged on the opening value of Plant and Machinery.
2. During the year one old machine costing ₹ 50,000 (WDV ₹ 20,000) was sold at a profit of ₹ 15,000.
3. ₹ 50,000 was paid towards Income Tax during the year.
4. Building under construction was not subject to any depreciation.
5. Debentures were issued on 1st October, 2018 and Equity Shares were issued on 1st April, 2018.

Prepare Cash Flow Statement.

Solution:

CASH FLOW STATEMENT
for the year ended 31st March, 2019

Particulars	₹	₹
A. Cash Flow from Operating Activities		
Net Profit before Tax (WN 1)		3,70,000
Adjustments for Non-cash and Non-Operating Items:		
Add: Depreciation	1,25,000	
Interest on Debentures (₹ 2,00,000 × 10/100 × 6/12)	10,000	
	1,35,000	
Less: Profit on Sale of Machine	15,000	1,20,000
Operating Profit before Working Capital Changes		4,90,000
Add: Decrease in Current Assets and Increase in Current Liabilities:		
Trade Receivables	2,00,000	
Less: Increase in Current Assets and Decrease in Current Liabilities:		
Inventories	(2,00,000)	
Trade Payables	(1,20,000)	(1,20,000)
Cash Generated from Operations		3,70,000
Less: Tax Paid		50,000
Cash Flow from Operating Activities		3,20,000

B. Cash Flow from Investing Activities		
Purchase of Non-current Investments		(1,00,000)
Sale Proceeds of Machine		35,000
Purchase of Plant and Machinery (WN 2)		(3,45,000)
Purchase of Land and Building		(2,00,000)
Cash Used in Investing Activities		(6,10,000)
C. Cash Flow from Financing Activities		
Proceeds from Issue of Share Capital		2,00,000
Proceeds from 10% Debentures		2,00,000
Interest on Debentures		(10,000)
Payment of Dividend		(2,00,000)
Cash Flow from Financing Activities		1,90,000
D. Net Decrease in Cash and Bank Balances (A + B + C)		(1,00,000)
E. *Add:* Opening Balance of Cash and Bank Balances		1,00,000
F. Closing Balance of Cash and Bank Balances (D + E)		Nil

Working Notes:

1. ***Calculation of Net Profit before Tax:***

		₹
Closing Surplus, *i.e.*, Balance in Statement of Profit and Loss		1,00,000
Less: Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss		60,000
Net Profit		40,000
Add: Transfer to Reserve	50,000	
Dividend Paid (Proposed Dividend for 2017–18)	2,00,000	
Provision for Tax (WN 3)	80,000	3,30,000
Net Profit before Tax		3,70,000

2. *Dr.* PLANT AND MACHINERY ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	5,00,000	By Depreciation A/c	1,25,000
To Gain (Profit) on Sale of Plant A/c (Statement of Profit and Loss)	15,000	By Bank A/c	35,000
To Bank A/c (Balancing Figure) (Purchase)	3,45,000	By Balance *c/d*	7,00,000
	8,60,000		8,60,000

3. *Dr.* PROVISION FOR TAX ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Bank A/c	50,000	By Balance *b/d*	70,000
To Balance *c/d*	1,00,000	By Statement of Profit and Loss (Bal. Fig.)	80,000
	1,50,000		1,50,000

Illustration 11.

From the following Balance Sheet of New Light Ltd. as at 31st March, 2019 and information, prepare Cash Flow Statement for the year ended 31st March, 2019:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		5,00,000	4,00,000
(b) Reserves and Surplus	1	3,20,000	2,50,000
2. Non-Current Liabilities			
Long-term Borrowings	2	2,00,000	1,00,000
3. Current Liabilities			
(a) Short-term Borrowings (12% Bank Loan)		1,00,000	2,00,000
(b) Trade Payables		1,50,000	90,000
(c) Short-term Provisions	3	40,000	20,000
Total		13,10,000	10,60,000
II. ASSETS			
1. Non-Current Assets			
(a) Fixed Assets (Tangible)	4	7,00,000	5,00,000
(b) Non-Current Investments (10% Investments)		70,000	50,000
2. Current Assets			
(a) Inventories		60,000	90,000
(b) Trade Receivables		1,20,000	70,000
(c) *Cash and Bank Balances:* Cash at Bank		3,60,000	3,50,000
Total		13,10,000	10,60,000

Note: Dividend proposed for the years 2017–18 and 2018–19 are ₹ 1,50,000 and ₹ 2,00,000 respectively.

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Securities Premium Reserve	5,000	...
General Reserve	1,00,000	80,000
Surplus, *i.e.*, Balance in the Statement of Profit and Loss	2,15,000	1,70,000
	3,20,000	2,50,000
2. Long-term Borrowings		
10% Debentures	2,00,000	1,00,000
3. Short-term Provisions		
Provision for Tax	40,000	20,000
4. Fixed Assets (Tangible)		
Machinery (Cost)	8,50,000	6,10,000
Less: Accumulated Depreciation	1,50,000	1,10,000
	7,00,000	5,00,000

Additional Information:

(*i*) Machinery costing ₹ 50,000 (Accumulated Depreciation ₹ 35,000) was sold at a loss of 20%.

(*ii*) Equity Shares were issued at a premium of 15% on 1st April, 2018.

(*iii*) New Non-current Investments were made on 1st April, 2018 and Bank Loan was repaid on the same date.

(*iv*) Additional debentures were issued on 1st October, 2018 at a discount of 10%. The company wrote off the discount on issue of debentures from Securities Premium Reserve.

(*v*) An Interim Dividend paid during the year amount to ₹ 25,000.

(*vi*) Income-tax paid ₹ 50,000.

Solution:

CASH FLOW STATEMENT
for the year ended 31st March, 2019

Particulars	₹	₹
A. Cash Flow from Operating Activities		
Net Profit before Tax (WN 1)		3,10,000
Adjustments for Non-cash and Non-Operating Items:		
(*i*) Loss on Sale of Machine	3,000	
(*ii*) Depreciation (WN 3)	75,000	
(*iii*) Interest on Debentures (₹ 1,00,000 × 10/100) + (₹ 1,00,000 × 10/100 × 6/12)	15,000	
(*iv*) Interest on Bank Loan	12,000	
(*v*) Interest on Investment	(7,000)	98,000
Operating Profit before Working Capital Changes		4,08,000
Add: Decrease in Current Assets and Increase in Current Liabilities		
Trade Payables	60,000	
Inventories	30,000	90,000
		4,98,000
Less: Increase in Current Assets:		
Trade Receivables		50,000
Cash Generated from Operations		4,48,000
Less: Tax Paid		50,000
Cash Flow from Operating Activities		3,98,000
B. Cash Flow from Investing Activities		
Purchase of 10% Investments		(20,000)
Interest on Investment		7,000
Sale Proceeds from Machinery		12,000
Purchase of Machinery (WN 2)		(2,90,000)
Cash Used in Investing Activities		(2,91,000)
C. Cash Flow from Financing Activities		
Proceeds from Issue of Share Capital		1,00,000
Securities Premium Receipt		15,000
Proceeds from 10% Debentures		90,000
Interim Dividend Paid		(25,000)
Interest on Debentures		(15,000)
Payment of 12% Bank Loan		(1,00,000)
Interest on Bank Loan		(12,000)
Dividend Paid		(1,50,000)
Cash Used in Financing Activities		(97,000)
D. Net Increase in Cash and Bank Balances (A + B + C)		10,000
Add: Opening Balance of Cash and Bank Balances		3,50,000
E. Closing Balance of Cash and Bank Balances		3,60,000

Working Notes:

1. ***Calculation of Net Profit before Tax:***

		₹
Closing Surplus, *i.e.*, Balance in Statement of Profit and Loss		2,15,000
Less: Opening Surplus, *i.e.*, Balance in Statement of Profit and Loss		1,70,000
Net Profit		45,000
Add: Transfer to General Reserve	20,000	
Dividend Paid (Proposed Dividend for 2017–18)	1,50,000	
Provision for Tax (WN 4)	70,000	
Interim Dividend	25,000	2,65,000
Net Profit before Tax		3,10,000

2. *Dr.* MACHINERY ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	6,10,000	By Bank A/c (Sale)	12,000
To Bank A/c (Balancing Figure) (Purchase)	2,90,000	By Loss on Sale of Machinery A/c (Statement of Profit and Loss)	3,000
		By Accumulated Depreciation A/c	35,000
		By Balance *c/d*	8,50,000
	9,00,000		9,00,000

3. *Dr.* PROVISION FOR DEPRECIATION ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Machinery A/c	35,000	By Balance *b/d*	1,10,000
To Balance *c/d*	1,50,000	By Statement of Profit and Loss (Bal. Fig.)	75,000
	1,85,000		1,85,000

4. *Dr.* PROVISION FOR TAX ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Bank A/c	50,000	By Balance *b/d*	20,000
To Balance *c/d*	40,000	By Statement of Profit and Loss (Bal. Fig.)	70,000
	90,000		90,000

5. Discount on issue of debentures has been adjusted from Securities Premium Reserve as per Section 52(2) of the Companies Act, 2013. The balance of ₹ 5,000 in Securities Premium Reserve is after writing off discount of ₹ 10,000. As such discount has not been written off through Statement of Profit and Loss, it is not considered while computing Operating Profit.

Unsolved Questions

1. From the following particulars, prepare Cash Flow Statement:

BALANCE SHEET

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		5,50,000	5,00,000
(*b*) Reserves and Surplus	1	1,95,000	1,55,000
2. Non-Current Liabilities			
Long-term Borrowings: 8% Debentures		1,50,000	2,50,000
3. Current Liabilities			
(*a*) Trade Payables	2	35,000	35,000
(*b*) *Short-term Provisions:* Provision for Tax		55,000	20,000
Total		9,85,000	9,60,000
II. ASSETS			
1. Non-Current Assets			
Fixed Assets:			
(*i*) Tangible	3	7,40,000	5,25,000
(*ii*) Intangible (Goodwill)		20,000	25,000
2. Current Assets			
(*a*) Inventories		1,05,000	1,25,000
(*b*) Trade Receivables	4	1,08,000	1,35,000
(*c*) Cash and Bank Balances		12,000	1,50,000
Total		9,85,000	9,60,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
General Reserve	1,00,000	1,00,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	95,000	55,000
	1,95,000	1,55,000
2. Trade Payables		
Sundry Creditors	20,000	25,000
Bills Payable	15,000	10,000
	35,000	35,000
3. Fixed Assets (Tangible)		
Building	3,40,000	2,25,000
Plant and Machinery	4,00,000	3,00,000
	7,40,000	5,25,000
4. Trade Receivables		
Debtors	1,20,000	1,50,000
Less: Provision for Doubtful Debts	12,000	15,000
	1,08,000	1,35,000

Additional Information:

1. During the year, a part of Plant and Machinery having a book value of ₹ 2,500 was sold for ₹ 1,500.
2. Dividend of ₹ 50,000 was paid during the year.
3. Income Tax of ₹ 25,000 was paid during the year.
4. Depreciation charged during the year—
   Building: ₹ 5,000; Plant and Machinery: ₹ 25,000.
5. 8% Debentures of ₹ 1,00,000 were redeemed on 31st March, 2019.
6. Equity Shares of the face value of ₹ 50,000 were issued during the year at a discount of 10% and the discount was written off from Statement of Profit and Loss.

[Hints:

1. Interest on debentures ₹ 20,000 (*i.e.*, ₹ 2,50,000 × 8/100) has been paid.

2. *Dr.* BUILDING ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	2,25,000	By Depreciation A/c	5,000
To Bank A/c (Bal. Fig.) (Purchase)	**1,20,000**	By Balance *c/d*	3,40,000
	3,45,000		3,45,000

3. *Dr.* PLANT ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	3,00,000	By Bank A/c (Sale)	1,500
To Bank A/c (Bal. Fig.) (Purchase)	**1,27,500**	By Loss on Sale of Plant A/c (Statement of P & L)	1,000
		By Depreciation A/c	25,000
		By Balance *c/d*	4,00,000
	4,27,500		4,27,500

4. Cash Used in Investing Activities = ₹ 1,20,000 + ₹ 1,27,500 – ₹ 1,500 = ₹ 2,46,000.]

2. Following is the Balance Sheet of Gupta & Co. Ltd., prepare Cash Flow Statement:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		2,50,000	2,00,000
(b) Reserves and Surplus		23,000	10,000
2. Current Liabilities			
Trade Payables		45,000	70,000
Total		3,18,000	2,80,000
II. ASSETS			
1. Current Assets			
(a) Current Investments	1	66,000	50,000
(b) Inventories		90,000	80,000
(c) Trade Receivables		1,15,000	1,20,000
(d) Cash and Bank Balances		47,000	30,000
Total		3,18,000	2,80,000

Note to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Current Investments		
Short-term Investments	16,000	10,000
Others	50,000	40,000
	66,000	50,000

3. Harrington Gardens Ltd. commenced its business on 1st April, 2018. Its Balance Sheet as at 31st March, 2019 was as follows:

Particulars	Note No.	31st March, 2019 (₹)
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Equity Share Capital		15,00,000
(b) Reserves and Surplus	1	2,50,000
2. Current Liabilities		
(a) Short-term Borrowings (Bank Overdraft)		1,00,000
(b) Trade Payables		2,00,000
Total		20,50,000
II. ASSETS		
1. Non-Current Assets		
(a) Fixed Assets		14,50,000
(b) Non-Current Investments		4,75,000
2. Current Assets		
Cash and Bank Balances		1,25,000
Total		20,50,000

Note to Accounts

Particulars		31st March, 2019 (₹)
1. Reserves and Surplus		
Securities Premium Reserve	75,000	
Less: Share Issue Expenses Written off	75,000	...
Surplus, *i.e.*, Balance in Statement of Profit and Loss	3,50,000	
Less: Share Issue Expenses Written off	1,00,000	2,50,000
		2,50,000

Calculate Cash Flow from Financing Activities of the company for the year ended 31st March, 2019.

4. Calculate Operating Profit before Working Capital Changes from the following information and Balance Sheet as at 31st March, 2019:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		8,50,000	5,00,000
(b) Reserves and Surplus	1	4,50,000	3,20,000
2. Current Liabilities			
(a) Trade Payables	2	95,000	70,000
(b) Other Current Liabilities	3	30,000	15,000
(c) Short-term Provisions	4	1,50,000	1,00,000
Total		15,75,000	10,05,000
II. ASSETS			
1. Non-Current Assets			
Fixed Assets—Tangible Assets		12,00,000	7,30,000
2. Current Assets		3,75,000	2,75,000
Total		15,75,000	10,05,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Investments Fluctuation Reserve	50,000	40,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	4,00,000	2,80,000
	4,50,000	3,20,000
2. Trade Payables		
Trade Creditors	70,000	50,000
Bills Payable	25,000	20,000
	95,000	70,000
3. Other Current Liabilities		
Outstanding Expenses	30,000	15,000
4. Short-term Provisions		
Provision for Tax	1,50,000	1,00,000

Additional Information:

1. Depreciation on tangible fixed assets for the year 2018–19 was ₹ 50,000.
2. Bad Debts written off were ₹ 5,000.
3. Income included liability written back of ₹ 5,000.

5. Calculate Operating Profit before Working Capital Changes from the following information and Balance Sheet of Gati Ltd. as at 31st March, 2019:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital	1	12,00,000	12,00,000
(b) Reserves and Surplus	2	5,15,000	2,75,000
2. Current Liabilities			
(a) Trade Payables	3	1,40,000	1,10,000
(b) Other Current Liabilities	4	10,000	20,000
(c) Short-term Provisions	5	2,50,000	2,00,000
Total		21,15,000	18,05,000
II. ASSETS			
1. Non-Current Assets			
(a) Fixed Assets		13,80,000	10,40,000
(b) Non-Current Investments		5,00,000	5,00,000
2. Current Assets		2,35,000	2,65,000
Total		21,15,000	18,05,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Share Capital		
Equity Share Capital	10,00,000	10,00,000
8% Preference Share Capital	2,00,000	2,00,000
	12,00,000	12,00,000
2. Reserves and Surplus		
General Reserve	1,50,000	1,00,000
Investments Fluctuation Reserve	90,000	50,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	2,75,000	1,25,000
	5,15,000	2,75,000
3. Trade Payables		
Creditors	80,000	70,000
Bills Payable	60,000	40,000
	1,40,000	1,10,000
4. Other Current Liabilities		
Outstanding Expenses	10,000	20,000
5. Short-term Provisions		
Provision for Tax	2,50,000	2,00,000

Note: Proposed equity dividends for the years ended 31st March, 2018 and 2019 are ₹ 1,04,000 and ₹ 1,24,000 respectively.

Additional Information:

1. Depreciation for the year was ₹ 1,10,000.
2. Bad Debts written off amounted to ₹ 15,000.
3. Income included excess provision written back ₹ 5,000.
4. Dividend received on investments ₹ 10,000.

6. Following is the Balance Sheet of Monica Ltd. as at 31st March, 2019:

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		20,00,000	16,00,000
(b) Reserves and Surplus	1	9,00,000	8,00,000
2. Non-Current Liabilities			
Long-term Borrowings	2	5,00,000	1,40,000
3. Current Liabilities			
(a) Trade Payables		1,00,000	60,000
(b) Short-term Provisions	3	80,000	60,000
Total		35,80,000	26,60,000
II. ASSETS			
1. Non-Current Assets			
(a) *Fixed Assets:*			
(i) Tangible Assets	4	16,00,000	9,00,000
(ii) Intangible Assets	5	6,40,000	7,00,000
2. Current Assets			
(a) Inventories		2,50,000	2,00,000
(b) Trade Receivables		5,00,000	3,00,000
(c) *Cash and Bank Balances:* Cash at Bank		5,90,000	5,60,000
Total		35,80,000	26,60,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Surplus, *i.e.*, Balance in Statement of Profit and Loss	9,00,000	8,00,000
2. Long-term Borrowings		
10% Debentures	5,00,000	1,40,000
3. Short-term Provisions		
Provision for Tax	80,000	60,000
4. Tangible Assets		
Machinery	17,60,000	10,00,000
Less: Accumulated Depreciation	1,60,000	1,00,000
	16,00,000	9,00,000
5. Intangible Assets		
Goodwill	6,40,000	7,00,000

Prepare a Cash Flow Statement after taking into account the following adjustments:

1. Tax paid during the year amounted to ₹ 1,40,000.
2. During the year machinery costing ₹ 3,00,000 on which depreciation charged was ₹ 1,00,000, was sold for ₹ 1,00,000.
3. An Interim Dividend on equity shares @ 10% was paid on Opening Balance.
4. New Debentures have been issued on 1st July, 2018.

GUIDE TO ANSWER

1. Cash Flow from Operating Activities—₹ 2,33,000; Cash Used in Investing Activities—₹ 2,46,000; Cash Used in Financing Activities—₹ 1,25,000.

2. Cash Used in Operating Activities—₹ 27,000; Cash Flow from Financing Activities—₹ 50,000.

3. Cash Flow from Financing Activities—₹ 15,00,000.

4. Operating Profit before Working Capital Changes—₹ 3,30,000.

5. Operating Profit before Working Capital Changes—₹ 7,20,000.

6. Cash Flow from Operating Activities—₹ 4,31,000; Cash Used in Investing Activities—₹ 9,60,000; Cash Flow from Financing Activities—₹ 5,59,000. Net Increase in Cash and Bank Balances—₹ 30,000.

CHAPTER 4

Ratio Analysis

MEANING OF KEY TERMS USED IN THE CHAPTER

1. Ratio

It is an arithmetical expression of relationship between two interdependent or related items.

2. Accounting Ratio

Accounting Ratio means ratio calculated on the basis of accounting information (data).

3. Ratio Analysis

Analysis of financial statements on the basis of accounting ratios is known as **Ratio Analysis**.

4. Pure Ratio

It is a ratio expressed as a quotient. For example, Current Ratio is ratio of Current Assets to Current Liabilities. If Current Assets are ₹ 20 lakhs and Current Liabilities are ₹ 10 lakhs, then the Current Ratio is 2 : 1.

5. Percentage

It is a ratio expressed in percentage. For example, Net Profit Ratio is calculated as percentage of Revenue from Operations. if Net Profit is ₹ 10 lakhs and Revenue from Operations is ₹ 50 lakhs, then Net Profit Ratio comes to 20%.

6. Times

It is a ratio expressed in number of times. For example, Trade Receivables Turnover Ratio is 3 times [Calculated by dividing Credit Revenue from Operations (₹ 3,00,000) by Average Trade Receivables (₹ 1,00,000)].

7. Fraction

It is a ratio expressed as a fraction. For example, ¾ or .75.

8. Liquidity Ratios

These ratios show the ability of the enterprise to meet its short-term financial commitments. These include: Current Ratio and Quick Ratio/Liquid Ratio.

9. Solvency Ratios

These ratios measure long-term financial position of the enterprise. These include: Debt to Equity Ratio; Proprietary Ratio; Debt to Total Assets Ratio and Interest Coverage Ratio.

10. Activity or Turnover Ratios

These ratios measure efficiency in use of assets of the enterprise in generating sales. These include: Trade Receivables Turnover Ratio; Trade Payables Turnover Ratio; Working Capital Turnover Ratio and Inventory Turnover Ratio.

11. Profitability Ratios

These ratios show the profitability of the enterprise. These include: Gross Profit Ratio; Net Profit Ratio; Operating Ratio; Operating Profit Ratio, Earning Per Share (EPS), Price Earning (P/E) Ratio and Return on Investment (ROI).

SUMMARY OF THE CHAPTER

- **Accounting Ratio** is a mathematical expression of the relationship between two items or group of items shown in the financial statements. In simple words, when ratios are calculated on the basis of accounting information these are called **accounting ratios**.
- **Ratio Analysis** is the process of computing, determining and presenting the relationship of items and group of items in the financial statements. It is an important tool or technique of financial analysis.
- **Ratio** may be expressed as (i) Pure ratio; (ii) Percentage; (iii) Number of Times; or (iv) Fraction.
- **Objectives of Ratio Analysis**
  (*i*) To simplify the accounting information.
  (*ii*) To analyse the Financial Statements.
  (*iii*) To judge the operating efficiency of business.
  (*iv*) To help in forecasting, planning and control.
  (*v*) To help in comparative analysis.
  (*vi*) To find out strengths and weaknesses of the business.
- **Limitations of Ratio Analysis**
  (*i*) Ratios may be misleading if they are based on incorrect accounting information.
  (*ii*) Variance in accounting practices.
  (*iii*) Ignores price level changes.
  (*iv*) Only quantitative analysis and not qualitative analysis.
  (*v*) Based on historical data. Hence, it is historical analysis.
  (*vi*) Only symptom and not cure.
  (*vii*) No single standard ratio.
  (*viii*) In the absence of absolute data, ratios may be misleading.
  (*ix*) Not free from bias.
  (*x*) Window dressing.
- **Classification of Accounting Ratios**

Liquidity Ratios	*Solvency Ratios*	*Activity Ratios*	*Profitability Ratios*
1. Current Ratio 2. Quick/Liquid Ratio	1. Debt to Equity Ratio 2. Proprietary Ratio 3. Debt to Total Assets Ratio 4. Interest Coverage Ratio	1. Trade Receivables Turnover Ratio 2. Trade Payables Turnover Ratio 3. Working Capital Turnover Ratio 4. Inventory Turnover Ratio	1. Gross Profit Ratio 2. Net Profit Ratio 3. Operating Ratio 4. Operating Profit Ratio 5. Earning Per Share (EPS) 6. Price Earning (P/E) Ratio 7. Return on Investment (ROI)

Summary of Important Accounting Ratios

Description of the Ratio	*Formula*	*Significance*	*How Expressed*	*Remarks*
I. Liquidity Ratios 1. Current Ratio	$\frac{\text{Current Assets}}{\text{Current Liabilities}}$	This ratio shows short-term financial soundness of the business. A higher ratio means better capacity to meet its current obligation. The ideal Current Ratio is 2 : 1. In case it is very high it shows the idleness of funds.	Pure *e.g.,* 2 : 1	*Current Assets* mean those assets which are either in the form of cash or can be converted into cash within a year or within the period of Operating cycle. *For example*—Cash and Bank Balances, Inventory (Stock), Trade Receivables (Debtors + Bills Receivable) Prepaid Expenses, etc. Loose Tools and Spare Parts are excluded from Current Assets for the ratio. *Current Liabilities* are those liabilities which are payable within a year or within the period of Operating cycle. *For example*—Trade Payables (Creditors + Bills Payable), Bank Overdraft, Outstanding Expenses, etc.
2. Quick/Liquid/Acid Test Ratio	$\frac{\text{Quick Assets or Liquid Assets}}{\text{Current Liabilities}}$	Quick Ratio is a fairly stringent measure of liquidity. It is based on those current assets which are highly liquid. Quick Ratio of 1 : 1 is considered as ideal. The higher the Quick Ratio, the better the short-term financial position.	Pure	Quick Assets = Current Assets – Inventory (Stock) – Prepaid Expenses
II. Solvency Ratios 1. Debt to Equity Ratio	$\frac{\text{Debt/Long-term Debt}}{\text{Equity (Shareholders' Funds)}}$	This ratio assesses long-term financial position and soundness of the long-term financial policies of the firm. In general, lower the Debt to Equity Ratio higher the protection enjoyed by the lenders.	Pure	*Long-term Debts* are Long-term Borrowings + Long-term Provisions. Shareholders' Funds = Share Capital + Reserves and Surplus *Or* Non-Current Assets + (Current Assets – Current Liabilities) – Non-Current Liabilities, *i.e.,* Non-Current Assets + Working Capital – Non-Current Liabilities *Or* Tangible Assets + Intangible Assets + Non-Current Investments + Long-term Loans and Advances + Working Capital – (Long-term Borrowings + Long-term Provisions).

2. Proprietary Ratio	$\frac{\text{Shareholders' Funds}}{\text{Total Assets}}$	This ratio shows the extent to which the total assets have been financed by the proprietor. The higher the ratio, greater the satisfaction for lenders and creditors.	Fraction	*Shareholders' Funds* mean same as in the Debt to Equity Ratio. Total Assets include Non-Current Assets and Current Assets.
3. Debt to Total Assets Ratio	$\frac{\text{Debt}}{\text{Total Assets}}$	This ratio measures the safety margin available to the lenders of Long-term debts. It measures the extent to which debt is being covered by assets.	Pure Ratio, *e.g.*, 2 : 1	Debt = Long-term Borrowings + Long-term Provisions. *Total Assets* include Non-Current Assets and Current Assets.
4. Interest Coverage Ratio	$\frac{\text{Net Profit before Interest and Tax}}{\text{Interest}}$	It measures the safety margin available to lenders.	Times	Interest means interest on long-term debts.
III. Activity Ratios				
1. Trade Receivables Turnover Ratio	$\frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$	This ratio indicates efficiency in the collection of amount due from Trade Receivables. The higher the ratio, the better it is since it indicates that debts are being collected more quickly.	Times	Trade Receivables includes Debtors and Bills Receivable. Average Trade Receivables $= \frac{\text{Opening Trade Receivables + Closing Trade Receivables}}{2}$
2. Trade Payables Turnover Ratio	$\frac{\text{Net Credit Purchases}}{\text{Average Trade Payables}}$	This ratio indicates the efficiency with which creditors are managed and paid.	Times	Trade Payables includes Creditors and Bills Payable. Average Trade Payables $= \frac{\text{Opening Trade Payables + Closing Trade Payables}}{2}$
3. Working Capital Turnover Ratio	$\frac{\text{Revenue from Operations}}{\text{Working Capital}}$	This ratio shows the number of times the working capital has been employed in the process of carrying on business. The higher the ratio, the better the efficiency in the utilisation of working capital.	Times	Working Capital = Current Assets – Current Liabilities
4. Inventory Turnover Ratio	$\frac{\text{Cost of Revenue from Operations (Cost of Goods Sold)}}{\text{Average Inventory}}$	This ratio measures how fast the stock is moving and generating sales. A higher ratio, means more efficient management of inventories and vice versa.	Times	Average Inventory = $\frac{\text{Opening Inventory + Closing Inventory}}{2}$

IV. Profitability Ratios				
1. Gross Profit Ratio	$\frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$	The ratio indicates the relationship between gross profit and revenue from operations. A higher ratio indicates low Cost of Revenue from Operations (Cost of Goods Sold).	%	Gross Profit = Revenue from Operations – Cost of Revenue from Operations Cost of Revenue from Operations = Cost of Materials Consumed (Stock-in-Trade + Purchases of Stock-in-Trade + Direct Expenses) + Changes in Inventories of WIP and Finished Goods + Purchases of Stock-in-Trade Revenue from Operations = Credit Revenue from Operations + Cash Revenue from Operations Net Sales = Total Sales – Sales Return
2. Net Profit Ratio	$\frac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$	The ratio indicates the overall efficiency of the business. A higher Net Profit Ratio is better for the business.	%	Net Profit = Revenue from Operations – Cost of Revenue from Operations (Cost of Goods Sold) – Indirect Expenses – Tax *Or* Gross Profit + Other Incomes – Indirect Expenses – Tax
3. Operating Ratio	$\frac{\text{Cost of Revenue from Operations (Cost of Goods Sold)} + \text{Operating Expenses}}{\text{Revenue from Operations}} \times 100$	The ratio is calculated to judge the operational efficiency of the business. A decline in the Operating Ratio is better because it would leave a high margin, which means more profit.	%	Cost of Revenue from Operations (Cost of Goods Sold) = Revenue from Operations – Gross Profit
4. Operating Profit Ratio	$\frac{\text{Net Operating Profit}}{\text{Revenue from Operations}} \times 100$	The main objective of computing this ratio is to determine the operational efficiency of the management.	%	Net Operating Profit = Gross Profit – Operating Expenses (*i.e.*, Administrative Expenses and Selling Expenses) + Operating Incomes
5. Earning Per Share	$\frac{\text{Net Profit after Tax} - \text{Preference Dividend}}{\text{Number of Equity Shares}}$	The ratio helps in evaluating the prevailing market price of share in the light of profit earning capacity.	₹ Per Share	This ratio helps in evaluating the prevailing market price of share. The more the earning per share better is the performance and prospects of the company.
6. Price Earning Ratio	$\frac{\text{Martket Value of an Equity Share}}{\text{Earning Per Share}}$	The objective of computing this ratio is to find out the expectations of the shareholders.	Times	It is very important ratio to know whether the shares of the company are undervalued or in estimating future market price.
7. Return on Investment	$\frac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$	The objective of computing this ratio is to know how efficiently the resources of the business are used.	%	Return on investment is a fair measure of the profitability of any concern with the result that the performance of different industries may be compared.

Solved Questions

Illustration 1.

Following is the Statement of Profit and Loss of Grand Canyon Ltd. for the year ended 31st March, 2019:

STATEMENT OF PROFIT AND LOSS *for the year ended 31st March, 2019*

Particulars	Note No.	₹
I. Income		
Revenue from Operations		5,00,000
Other Income	1	5,000
Total		5,05,000
II. Expenses		
Purchases of Stock-in-Trade		3,00,000
Changes in Inventories of Stock-in-Trade	2	(20,000)
Employees Benefit Expenses	3	14,000
Finance Cost		3,000
Other Expenses	4	1,28,000
Total		4,25,000
III. Net Profit (I – II)		80,000

Notes to Accounts

	₹
1. Other Income	
Dividend	5,000
2. Changes in Inventories of Stock-in-Trade	
Opening Stock-in-Trade	70,000
Less: Closing Stock-in-Trade	90,000
	(20,000)
3. Employees Benefit Expenses	
Wages	14,000
4. Other Expenses	
Carriage Inwards	6,000
Administrative Expenses	1,02,000
Selling and Distribution Expenses	20,000
	1,28,000

You are required to calculate: (*i*) Gross Profit Ratio; (*ii*) Operating Ratio and (*iii*) Operating Profit Ratio.

Solution:

(*i*) $$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{₹\ 2,00,000}{₹\ 5,00,000} \times 100 = 40\%.$$

$$\text{Gross Profit} = \text{Revenue from Operations} - \text{Cost of Revenue from Operations/ Cost of Goods Sold (WN 1)}$$

$$= ₹\ 5,00,000 - ₹\ 3,00,000 = ₹\ 2,00,000.$$

(*ii*) $$\text{Operating Ratio} = \frac{\text{Cost of Goods Sold (WN 1)} + \text{Operating Expenses (WN 2)}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{₹\,3,00,000 + ₹\,1,22,000}{₹\,5,00,000} \times 100 = 84.4\%.$$

(*iii*) $$\text{Operating Profit Ratio} = \frac{\text{Operating Profit (WN 3)}}{\text{Revenue from Operations}} \times 100 = \frac{₹\,78,000}{₹\,5,00,000} \times 100 = 15.6\%.$$

Working Notes:

1. *Calculation of Cost of Goods Sold:*

	₹
Purchases of Stock-in-Trade	3,00,000
Changes in Inventories of Stock-in-Trade	(20,000)
Direct Expenses [₹ 6,000 (Carriage Inwards) + ₹ 14,000 (Wages)]	20,000
Cost of Goods Sold	**3,00,000**

2. *Calculation of Operating Expenses:*

Administrative Expenses	1,02,000
Selling and Distribution Expenses	20,000
Operating Expenses	**1,22,000**

3. Operating Profit = Net Profit + Interest (Finance Cost) – Dividend Received
= ₹ 80,000 + ₹ 3,000 – ₹ 5,000 = ₹ **78,000**.

4. Finance Cost is considered to be an expense not related to Operating Expenses.

Illustration 2.

From the following Balance Sheet of Defence Brokers Ltd., calculate Debt to Equity Ratio:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital		15,00,000
(*b*) Reserves and Surplus		(2,30,000)
2. Non-Current Liabilities		
(*a*) Long-term Borrowings		15,00,000
(*b*) Long-term Provisions		2,85,000
3. Current Liabilities		
(*a*) Short-term Borrowings		55,000
(*b*) Trade Payables		1,15,000
(*c*) Other Current Liabilities		25,000
Total		32,50,000

Particulars	Note No.	₹
II. ASSETS		
1. Non-Current Assets		
(*a*) *Fixed Assets:*		
(*i*) Tangible Assets		11,00,000
(*ii*) Intangible Assets		1,30,000
(*b*) Non-Current Investments	1	2,60,000
2. Current Assets		
(*a*) Current Investments	2	1,90,000
(*b*) Inventories		7,50,000
(*c*) Trade Receivables		3,00,000
(*d*) Cash and Bank Balances		5,20,000
Total		32,50,000

Notes to Accounts

Particulars	₹
1. Non-Current Investments	
Trade Investments	2,60,000
2. Current Investments	
Government Securities	50,000
Other Investments (Trade)	1,40,000
	1,90,000

Solution: Debt to Equity Ratio $= \dfrac{\text{Debt/Long-term Debt}}{\text{Equity/Shareholders' Funds}}$

$$= \frac{₹\,17,85,000}{₹\,12,70,000} = 1.4:1.$$

Notes:

1. Long-term Debt = Long-term Borrowings + Long-term Provisions
= ₹ 15,00,000 + ₹ 2,85,000 = ₹ 17,85,000.

2. Equity or Shareholders' Funds = Share Capital + Reserves and Surplus
= ₹ 15,00,000 – ₹ 2,30,000* = ₹ 12,70,000.

*₹ 2,30,000, being negative amount against Reserves and Surplus, it is deducted.

Illustration 3.

Given below is the Balance Sheet of a business:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
Share Capital		2,00,000
2. Non-Current Liabilities		
(*a*) Long-term Borrowings (8% Debentures)		1,00,000
(*b*) Long-term Provisions		25,000
3. Current Liabilities		
Trade Payables (Creditors and Bills Payable)		25,000
Total		3,50,000

II. ASSETS		
1. Non-Current Assets		
Fixed Assets (Tangible)		2,20,000
2. Current Assets		
(*a*) Inventories		80,000
(*b*) Trade Receivables		30,000
(*c*) Cash and Bank Balances		20,000
Total		3,50,000

Calculate the following ratios:

(*i*) Debt to Total Assets Ratio; and (*ii*) Proprietary Ratio.

Solution:

(*i*) $$\text{Debt to Total Assets Ratio} = \frac{\text{Debt}}{\text{Total Assets}} = \frac{₹\,1,25,000}{₹\,3,50,000} = 0.36:1.$$

$$\text{Debt} = \text{Long-term Borrowings} + \text{Long-term Provisions}$$
$$= ₹\,1,00,000 + ₹\,25,000 = ₹\,1,25,000.$$

(*ii*) $$\text{Proprietary Ratio} = \frac{\text{Shareholders' Funds/Equity}}{\text{Total Assets}} = \frac{\text{Share Capital}}{\text{Total Assets}}$$
$$= \frac{₹\,2,00,000}{₹\,3,50,000} = 0.57 : 1.$$

Illustration 4.

From the following information, calculate Trade Receivables Turnover Ratio and Trade Payables Turnover Ratio:

Average Stock held ₹ 5,00,000; Revenue from Operations ₹ 54,00,000; Purchases ₹ 36,00,000; Cost of Revenue from Operations or Cost of Goods Sold ₹ 16,20,000; Average Trade Receivables Outstanding ₹ 6,00,000; Average Trade Payables Outstanding ₹ 3,60,000.

Note: All purchases and sales are made on credit.

Solution:

$$\text{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$
$$= \frac{₹\,54,00,000}{₹\,6,00,000} = 9 \text{ Times.}$$

$$\text{Trade Payables Turnover Ratio} = \frac{\text{Net Credit Purchases}}{\text{Average Trade Payables}} = \frac{₹\,36,00,000}{₹\,3,60,000} = 10 \text{ Times.}$$

Illustration 5.

Calculate Opening Trade Payables and Closing Trade Payables from the following information:

(*i*) Cash Purchases 25% of Total Purchases.

(*ii*) Revenue from Operations ₹ 6,00,000.

(*iii*) Gross Profit Ratio 25%.

(*iv*) Opening Inventory ₹ 1,50,000, Closing Inventory ₹ 3,00,000.

(*v*) Trade Payables at the end were 3 times of the beginning.

(*vi*) Trade Payables Turnover Ratio 3 times.

Solution:

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

= ₹ 6,00,000 – (25% of ₹ 6,00,000) = ₹ 4,50,000

Total Purchases = Cost of Revenue from Operations + Closing Inventory – Opening Inventory

= ₹ 4,50,000 + ₹ 3,00,000 – ₹ 1,50,000 = ₹ 6,00,000

Net Credit Purchases = Total Purchase – Cash Purchases

= ₹ 6,00,000 – (25% of ₹ 6,00,000) = ₹ 4,50,000

$$\text{Trade Payables Turnover Ratio} = \frac{\text{Net Credit Purchases}}{\text{Average Trade Payables}}$$

$$3 = \frac{₹\ 4{,}50{,}000}{\text{Average Trade Payables}}$$

$$\text{Average Trade Payables} = \frac{₹\ 4{,}50{,}000}{3} = ₹\ 1{,}50{,}000$$

Calculation of Opening and Closing Trade Payables:

Let the Opening Trade Paybles = x

Closing Trade Payables = $3x$

$$₹\ 1{,}50{,}000\ (\text{Average Trade Payables}) = \frac{x + 3x}{2}$$

$$₹\ 3{,}00{,}000 = 4x$$

$$x = \frac{₹\ 3{,}00{,}000}{4} = ₹\ 75{,}000\ (\text{Opening Trade Payables})$$

Closing Trade Payables = $3x$ = ₹ 75,000 × 3 = ₹ 2,25,000.

Illustration 6.

Following is the Statement of Profit and Loss of Exe Ltd., calculate Inventory Turnover Ratio:

STATEMENT OF PROFIT AND LOSS

Particulars	Note No.	₹
I. Income		
Revenue from Operations	1	2,00,000
II. Expenses		
Purchases of Stock-in-Trade		1,30,000
Change in Inventories of Stock-in-Trade	2	20,000
Total		1,50,000
III. Net Profit (I – II)		50,000

Notes to Accounts

	₹
1. Revenue from Operations	
Sales	2,10,000
Less: Return	10,000
	2,00,000
2. Change in Inventories of Stock-in-Trade	
Opening Stock (Inventory)	40,000
Less: Closing Stock (Inventory)	20,000
	20,000

Solution:

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}} = \frac{₹\,1,50,000}{₹\,30,000} = 5 \text{ Times.}$$

Cost of Revenue from Operations

= Purchases of Stock-in-Trade + Change in Inventories of Stock-in-Trade

= ₹ 1,30,000 + ₹ 20,000 = ₹ 1,50,000

$$\text{Average Inventory} = \frac{1}{2} \times (\text{Opening Inventory} + \text{Closing Inventory})$$

$$= \frac{1}{2} \times (₹\ 40,000 + ₹\ 20,000) = ₹\ 30,000.$$

Illustration 7.

Following is the Statement of Profit and Loss of New Delhi Sales Ltd. for the year ended 31st March, 2019:

STATEMENT OF PROFIT AND LOSS *for the year ended 31st March, 2019*

Particulars	Note No.	₹
I. Income		
Revenue from Operations (Net Sales)		12,50,000
II. Expenses		
Purchases of Stock-in-Trade		8,75,000
Change in Inventories of Stock-in-Trade		(27,000)
Employees Benefit Expenses		1,20,000
Finance Costs		5,000
Depreciation and Amortisation Expense		8,000
Other Expenses	1	39,000
Total		10,20,000
III. Net Profit (I – II)		2,30,000

Note to Accounts

	₹
1. Other Expenses	
Administrative and General Expenses	10,000
Provision for Tax	29,000
	39,000

Calculate Net Profit Ratio.

Solution:

$$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{₹\,2,30,000}{₹\,12,50,000} \times 100 = 18.40\%.$$

Illustration 8.

Following is the Statement of Profit and Loss of a firm for the year ended 31st March, 2019, calculate Operating Ratio:

STATEMENT OF PROFIT AND LOSS *for the year ended 31st March, 2019*

Particulars	Note No.	₹
I. Income		
Revenue from Operations (Net Sales)		4,00,000
II. Expenses		
Purchases of Stock-in-Trade		2,25,000
Change in Inventories of Stock-in-Trade		(15,000)
Employees Benefit Expenses	1	6,000
Other Expenses	2	34,000
Total		2,50,000
III. Net Profit (I – II)		1,50,000

Notes to Accounts

	₹
1. Employees Benefit Expenses	
Wages	6,000
2. Other Expenses	
Administration Expenses	10,000
Selling and Distribution Expenses	14,000
Loss on Sale of Plant	10,000
	34,000

Solution:

Operating Ratio

$$= \frac{\text{Cost of Revenue from Operations (Cost of Sales) (WN 1)} + \text{Operating Expenses (WN 2)}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{₹\,2,16,000 + ₹\,24,000}{₹\,4,00,000} \times 100 = \frac{₹\,2,40,000}{₹\,4,00,000} \times 100 = 60\%.$$

Working Notes:

1. Cost of Revenue from Operations (Cost of Sales)

= Purchases of Stock-in-Trade + Change in Inventories of Stock-in-Trade + Wages (Employees Benefit Expenses)

= ₹ 2,25,000 – ₹ 15,000* + ₹ 6,000 = ₹ 2,16,000.

*Changes in Inventories of Stock-in-Trade is a negative amount. Hence, it is deducted.

2. Operating Expenses = Administration Expenses + Selling and Distribution Expenses or Other Expenses (except Loss on Sale of Plant)
= ₹ 10,000 + ₹ 14,000 = ₹ 24,000.

3. Loss on Sale of Plant will be excluded because it is not an operating loss but loss because of sale of an asset.

Illustration 9.

Calculate following ratios from the given information:

(*i*) Quick Ratio, (*ii*) Gross Profit Ratio,
(*iii*) Inventory Turnover Ratio, (*iv*) Operating Ratio, and
(*v*) Debt to Equity Ratio.

STATEMENT OF PROFIT AND LOSS *for the year ended 31st March, 2019*

Particulars	Note No.	₹
I. Income		
Revenue from Operations		5,00,000
II. Expenses		
Purchases of Stock-in-Trade		2,00,000
Change in Inventories of Stock-in-Trade	1	(30,000)
Employees Benefit Expenses		50,000
Finance Cost		25,000
Other Expenses	2	90,000
Total		3,35,000
III. Net Profit (I – II)		1,65,000

Notes to Accounts

Particulars	₹
1. Change in Inventories	
Stock-in-Trade—Opening	50,000
Less: Closing	80,000
	(30,000)
2. Other Expenses	
Administrative Expenses	20,000
Selling Expenses	30,000
Provision for Tax	40,000
	90,000

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital		7,00,000
(*b*) Reserves and Surplus		1,11,000
2. Non-Current Liabilities		
(*a*) Long-term Borrowings		1,40,000
(*b*) Long-term Provisions		10,000
3. Current Liabilities		
(*a*) Short-term Borrowings (Bank Overdraft)		4,000
(*b*) Trade Payables		20,000
Total		9,85,000

II. ASSETS		
1. Non-Current Assets		
Fixed Assets (Tangible)		7,20,000
2. Current Assets		
(*a*) Inventories		80,000
(*b*) Trade Receivables		1,20,000
(*c*) Cash and Bank Balances		60,000
(*d*) Other Current Assets (Prepaid Expenses)		5,000
Total		9,85,000

(*ISC 2007, Modified*)

Solution:

(*i*) $$\text{Quick Ratio} = \frac{\text{Quick Assets (Note 1)}}{\text{Current Liabilities (Note 2)}}$$

$$= \frac{₹\,1,80,000}{₹\,24,000} = 7.5 : 1.$$

Note: Quick Assets = Trade Receivables + Cash and Bank Balances
= ₹ 1,20,000 + ₹ 60,000 = ₹ 1,80,000.

(*ii*) $$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{₹\,3,30,000}{₹\,5,00,000} \times 100 = 66\%.$$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations
= ₹ 5,00,000 – (₹ 2,00,000 – ₹ 30,000) = ₹ 3,30,000.

Note: Direct Expenses are taken as Nil since no information is available.

(*iii*) Inventory Turnover Ratio

$$= \frac{\text{Cost of Revenue from Operations (Cost of Goods Sold) (Note 1)}}{\text{Average Inventory (Note 2)}}$$

$$= \frac{₹\,1,70,000}{₹\,65,000} = 2.62 \text{ Times.}$$

Notes: 1. Cost of Revenue from Operations (Cost of Goods Sold)
= Purchases of Stock-in-Trade + Change in Inventories of Stock-in-Trade
= ₹ 2,00,000 – ₹ 30,000 = ₹ 1,70,000.

2. $$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{₹\,50,000 + ₹\,80,000}{2} = ₹\,65,000.$$

(*iv*) Operating Ratio

$$= \frac{\text{Cost of Revenue from Operations (Cost of Goods Sold)}^{*} + \text{Operating Expenses}^{**}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{₹\,1{,}70{,}000 + ₹\,1{,}00{,}000}{₹\,5{,}00{,}000} \times 100 = \frac{₹\,2{,}70{,}000}{₹\,5{,}00{,}000} \times 100 = 54\%.$$

*Cost of Revenue from Operations (Cost of Goods Sold)
= Purchases of Stock-in-Trade + Change in Inventories of Stock-in-Trade
= ₹ 2,00,000 – ₹ 30,000 = ₹ 1,70,000

**Operating Expenses = Employees Benefit Expenses + Other Expenses (Administrative Expenses + Selling Expenses)
= ₹ 50,000 + ₹ 20,000 + ₹ 30,000 = ₹ 1,00,000.

(*v*) Debt to Equity Ratio $= \dfrac{\text{Debt (Long-term Debt)}}{\text{Equity [Shareholders' Funds]}}$

$$= \frac{₹\,1{,}50{,}000}{₹\,8{,}11{,}000} = 0.18 : 1.$$

Notes: 1. Debt/Long-term Debt = Long-term Borrowings + Long-term Provisions
= ₹ 1,40,000 + ₹ 10,000 = ₹ 1,50,000.

2. Shareholders' Funds = Share Capital + Reserves and Surplus
= ₹ 7,00,000 + ₹ 1,11,000 = ₹ 8,11,000.

Illustration 10.

Calculate following ratios from the Financial Statements of Annie Foods Limited:

(*i*) Gross Profit Ratio; (*ii*) Net Profit Ratio;
(*iii*) Working Capital Turnover Ratio; (*iv*) Inventory Turnover Ratio;
(*v*) Quick Ratio; (*vi*) Proprietary Ratio;
(*vii*) Current Ratio.

STATEMENT OF PROFIT AND LOSS OF ANNIE FOODS LIMITED *for the year ended 31st March, 2019*

Particulars	Note No.	₹
I. Income		
Revenue from Operations (Net Sales)		68,000
Other Income		1,000
Total		69,000
II. Expenses		
Purchases of Stock-in-Trade		28,000
Change in Inventories of Stock-in-Trade	1	(10,000)
Finance Cost		5,000
Other Expenses	2	21,000
Total		44,000
III. Net Profit (I – II)		25,000

BALANCE SHEET OF ANNIE FOODS LIMITED *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	3	1,50,000
(*b*) Reserves and Surplus		25,000
2. Non-Current Liabilities		
Long-term Borrowings	4	30,000
3. Current Liabilities		
Trade Payables	5	30,000
Total		2,35,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets (Tangible)		1,40,000
2. Current Assets		
(*a*) Inventories		40,000
(*b*) Trade Receivables		20,000
(*c*) Cash and Bank Balances		35,000
Total		2,35,000

Notes to Accounts

	₹
1. Changes in Inventories	
Stock-in-Trade—Opening Inventory	30,000
Less: Closing Inventory	40,000
	(10,000)
2. Other Expenses	
(*a*) Office Expenses	10,000
(*b*) Selling Expenses	9,000
(*c*) Loss on Sale of Plant	2,000
	21,000
3. Share Capital	
(*a*) Equity Share Capital	1,20,000
(*b*) Preference Share Capital	30,000
	1,50,000
4. Long-term Borrowings	
10% Debentures	30,000
5. Trade Payables	
(*a*) Bills Payable	10,000
(*b*) Creditors	20,000
	30,000

Note: All calculations are to be made up to two places of decimal. (*ISC 2010, Modified*)

Solution:

$$(i)\ \text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100 = \frac{₹\,50{,}000}{₹\,68{,}000} \times 100 = 73.53\%.$$

Gross Profit = Revenue from Operations – Cost of Revenue from Operations (Cost of Goods Sold)

Cost of Revenue from Operations (Cost of Goods Sold)

= Purchases of Stock-in-Trade + Change in Inventories of Stock-in-Trade

Gross Profit = ₹ 68,000 – ₹ 18,000 = ₹ 50,000.

(*ii*) $$\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100$$

$$= \frac{₹\,25{,}000}{₹\,68{,}000} \times 100 = 36.76\%.$$

(*iii*) $$\text{Working Capital Turnover Ratio} = \frac{\text{Revenue from Operations}}{\text{Working Capital (Note)}}$$

$$= \frac{₹\,68{,}000}{₹\,65{,}000} = 1.05 \text{ Times.}$$

Working Capital = Total Current Assets – Total Current Liabilities.

Note: *Calculation of Working Capital:*

Current Assets	₹	*Current Liabilities*	₹
Inventory	40,000	Trade Payables	30,000
Trade Receivables	20,000		
Cash and Bank Balances	35,000		
	95,000		30,000

∴ Working Capital = ₹ 95,000 – ₹ 30,000 = ₹ 65,000.

(*iv*) $$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations (Cost of Goods Sold)}}{\text{Average Inventory}}$$

$$= \frac{₹\,18{,}000}{₹\,35{,}000} = 0.51 \text{ Times.}$$

Cost of Revenue from Operations (Cost of Goods Sold)

= Purchases of Stock-in-Trade + Change in Inventories of Stock-in-Trade

= ₹ 28,000 – ₹ 10,000 = ₹ 18,000

$$\text{Average Inventory} = \frac{\text{Opening Inventory + Closing Inventory}}{2}$$

$$= \frac{₹\,30{,}000 + ₹\,40{,}000}{2} = ₹\,35{,}000.$$

(*v*) $$\text{Quick Ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}} = \frac{₹\,55{,}000}{₹\,30{,}000} = 1.83 : 1.$$

Quick Assets = Total Current Assets – Closing Inventory

= ₹ 95,000 – ₹ 40,000 = ₹ 55,000

(*vi*) Proprietary Ratio $= \dfrac{\text{Shareholders' Funds}}{\text{Total Assets}} = \dfrac{₹\,1,75,000}{₹\,2,35,000} = 0.74 : 1.$

Shareholders' Funds = Equity Share Capital + Preference Share Capital + Reserves and Surplus
= ₹ 1,20,000 + ₹ 30,000 + ₹ 25,000 = ₹ 1,75,000.

(*vii*) Current Ratio $= \dfrac{\text{Current Assets}}{\text{Current Liabilities}} = \dfrac{₹\,95,000}{₹\,30,000} = 3.17 : 1.$

Illustration 11.

Radient Engineering Ltd. has the following capital structure:	₹
15% Preference Shares of ₹ 100 each	10,00,000
Equity Shares of ₹ 100 each	40,00,000
10% Debentures of ₹ 100 each	15,00,000
	65,00,000

Following information relating to the financial year just ended are:

Profit after interest and tax	₹ 22,00,000
Reserves and Surplus	₹ 5,00,000
Equity Dividend Paid	20%
Market Price of Equity Share	₹ 205
Tax Rate	50%

Calculate:

(*i*) Return On Investment (ROI); (*ii*) Earning Per Share (EPS);
(*iii*) Price-Earning Ratio; and (*iv*) Debt to Equity Ratio.

Solution:

(*i*) Return on Investment $= \dfrac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$

$= \dfrac{₹\,45,50,000}{₹\,70,00,000} \times 100 = 65\%.$

Working Notes:

1. *Calculation of Net Profit before Interest and Tax:*

	₹
Let Profit before Tax	100
Tax rate @ 50%	50
Profit after Tax	50

Profit before Tax $= \dfrac{\text{Net Profit after Tax} \times 100}{50}$

$= \dfrac{₹\,22,00,000 \times 100}{50} = ₹\,44,00,000$

Add: Interest on Debentures	₹ 1,50,000
Net Profit before Interest and Tax	₹ 45,50,000

2. Capital Employed = Equity Share Capital + Preference Share Capital + Reserves and Surplus + Long-term Borrowings (*i.e.*, 10% Debentures)
= ₹ 40,00,000 + ₹ 10,00,000 + ₹ 5,00,000 + ₹ 15,00,000 = ₹ 70,00,000.

(*ii*) Earning Per Share = $\dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{No. of Equity Shares}}$

$$= \frac{₹\ 22{,}00{,}000 - ₹\ 1{,}50{,}000}{40{,}000} = ₹\ 51.25.$$

(*iii*) Price-Earning Ratio = $\dfrac{\text{Market Value of an Equity Share}}{\text{Earning Per Share (EPS)}} = \dfrac{₹\ 205}{₹\ 51.25}$ = 4 Times.

(*iv*) Debt to Equity Ratio = $\dfrac{\text{Debt/Long-term Debt}}{\text{Equity/Shareholders' Funds}} = \dfrac{₹\ 15{,}00{,}000}{₹\ 55{,}00{,}000}$ = 0.27 : 1.

Note: Equity = Equity Share Capital + 15% Preference Share Capital + Reserves and Surplus
= ₹ 40,00,000 + ₹ 10,00,000 + ₹ 5,00,000 = ₹ 55,00,000.

Illustration 12.

Following is the Balance Sheet of Gyan Ltd. You are required to calculate Working Capital Turnover Ratio:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital		5,00,000
(*b*) Reserves and Surplus		2,00,000
2. Current Liabilities		
(*a*) Trade Payables		2,50,000
(*b*) Short-term Provisions		50,000
Total		10,00,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible (Net)		4,00,000
2. Current Assets		
(*a*) Current Investments		1,00,000
(*b*) Inventories		1,00,000
(*c*) Trade Receivables		2,50,000
(*d*) Cash and Bank Balances		1,50,000
Total		10,00,000

(*i*) Total Sales during the year ₹ 32,00,000. (*ii*) Sales Return during the year ₹ 2,00,000.

Solution:

Working Capital Turnover Ratio = $\dfrac{\text{Revenue from Operations (WN 1)}}{\text{Working Capital (WN 2)}}$

$$= \frac{₹\ 30{,}00{,}000}{₹\ 3{,}00{,}000} = 10 \text{ Times.}$$

Working Notes:

1. Revenue from Operations = Total Sales – Sales Return
= ₹ 32,00,000 – ₹ 2,00,000 = ₹ 30,00,000.

2. Working Capital = Current Assets – Current Liabilities

Current Assets = Current Investments + Inventories + Trade Receivables + Cash and Bank Balances

= ₹ 1,00,000 + ₹ 1,00,000 + ₹ 2,50,000 + ₹ 1,50,000 = ₹ 6,00,000

Current Liabilities = Trade Payables + Short-term Provisions

= ₹ 2,50,000 + ₹ 50,000 = ₹ 3,00,000.

Therefore,

Working Capital = ₹ 6,00,000 – ₹ 3,00,000 = ₹ 3,00,000.

Illustration 13.

Opening Inventory ₹ 1,20,000, Closing Inventory ₹ 72,000. Inventory Turnover Ratio is 8 Times. Selling Price 25% above cost. Calculate Gross Profit Ratio.

Solution:

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100 = \frac{₹\,1,92,000}{₹\,9,60,000} \times 100 = 20\%.$$

$$\text{Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}$$

$$= \frac{₹\,1,20,000 + ₹\,72,000}{2} = ₹\,96,000$$

Cost of Revenue from Operations = Average Inventory × Inventory Turnover Ratio

= ₹ 96,000 × 8 = ₹ 7,68,000

$$\text{Gross Profit} = ₹\,7,68,000 \times \frac{25}{100} = ₹\,1,92,000$$

Revenue from Operations = Cost of Revenue from Operations + Gross Profit

= ₹ 7,68,000 + ₹ 1,92,000 = ₹ 9,60,000.

Master Question and Advanced Level Questions

Illustration 14. Following sets of final accounts relate to Hindustan Products Ltd., calculate following ratios for the company:

(*i*) Inventory Turnover Ratio;
(*ii*) Gross Profit Ratio;
(*iii*) Working Capital Turnover Ratio;
(*iv*) Current Ratio;
(*v*) Quick Ratio;
(*vi*) Net Profit Ratio;
(*vii*) Debt to Equity Ratio;
(*viii*) Trade Receivables Turnover Ratio;
(*ix*) Proprietary Ratio;
(*x*) Debt to Total Assets Ratio;
(*xi*) Earning Per Share;
(*xii*) Return on Investment (ROI);
(*xiii*) Price-Earning Ratio (assume Market Value of an Equity Share is ₹ 39.20).

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	31st March, 2019 (₹)
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital	1	1,85,000
(b) Reserves and Surplus	2	1,05,250
2. Non-Current Liabilities		
Long-term Borrowings	3	40,000
3. Current Liabilities		
(a) Trade Payables		34,000
(b) Short-term Provisions	4	42,000
Total		4,06,250
II. ASSETS		
1. Non-Current Assets		
Fixed Assets (Tangible)	5	3,04,350
2. Current Assets		
(a) Inventories		35,000
(b) Trade Receivables		46,000
(c) Cash and Bank Balances	6	20,900
Total		4,06,250

STATEMENT OF PROFIT AND LOSS *for the year ended 31st March, 2019*

Particulars	Note No.	31st March, 2019 (₹)
I. Revenue from Operations (Net Sales)		5,40,000
II. *Expenses:*		
(*a*) Purchases of Stock-in-Trade		3,26,000
(*b*) Change in Inventories of Stock-in-Trade	7	(11,000)
(*c*) Employees Benefit Expenses		48,000
(*d*) Finance Costs (Interest on Debentures)		3,200
(*e*) Other Expenses		33,800
Total Expenses		4,00,000
III. Profit before Tax (I – II)		1,40,000
IV. Tax Expenses @ 30%		42,000
V. Profit for the Period (III – IV)		98,000

Notes to Accounts

Particulars	31st March, 2019 (₹)
1. Share Capital	
Authorised Capital	
... Equity Shares of ₹ 10 each	...
... Preference Shares of ₹ 100 each	...
	...
Issued Capital	
12,500 Equity Shares of ₹ 10 each	1,25,000
600, 8% Preference Shares of ₹ 100 each	60,000
	1,85,000

Subscribed Capital	
Subscribed and fully paid-up	
12,500 Equity Shares of ₹ 10 each	1,25,000
600, 8% Preference Shares of ₹ 100 each	60,000
	1,85,000
2. Reserves and Surplus	
(*a*) *General Reserve:*	
Transferred from Surplus, *i.e.*, Balance in Statement of Profit and Loss	25,000
(*b*) *Surplus, i.e., Balance in Statement of Profit and Loss:*	
Opening Balance	7,250
Add: Profit for the Year	98,000
	1,05,250
Less: *Appropriations:*	
Transfer to General Reserve	25,000
	80,250
Total (*a* + *b*)	1,05,250
3. Long-term Borrowings	
400, 8% Debentures of ₹ 100 each	40,000
4. Short-term Provisions	
Provision for Tax	42,000
5. Fixed Assets (Tangible)	
Plant and Machinery	3,04,350
6. Cash and Bank Balances	
Cash at Bank	17,250
Cash in Hand	3,650
	20,900
7. Change in Inventories of Stock-in-Trade	
Opening Inventories	24,000
Less: Closing Inventories	35,000
	(11,000)

Additional Information:

(*i*) Trade Receivables on 1st April, 2018: ₹ 54,000.

(*ii*) Credit Revenue from Operations: 60% of Total Revenue from Operations.

(*iii*) Provide for Income Tax @ 30%.

Solution:

(*i*) *Inventory Turnover Ratio* $= \dfrac{\text{Cost of Revenue from Operations (Cost of Goods Sold)}}{\text{Average Inventory}}$

$$= \frac{₹\ 3,15,000}{₹\ 29,500} = 10.68 \text{ Times.}$$

Cost of Revenue from Operations (Cost of Goods Sold)

= Purchases of Stock-in-Trade + Change in Inventories of Stock-in-Trade

= ₹ 3,26,000 – ₹ 11,000 = ₹ 3,15,000.

Average Inventory = (Opening Inventories + Closing Inventories)/2

= (₹ 24,000 + ₹ 35,000)/2 = ₹ 29,500.

(*ii*) $$\textit{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Revenue from Operations (Net Sales)}} \times 100$$

$$= \frac{₹\,2,25,000}{₹\,5,40,000} \times 100 = 41.67\%.$$

Gross Profit = Revenue from Operations (Net Sales) – Cost of Revenue from Operations (Cost of Goods Sold)

= ₹ 5,40,000 – ₹ 3,15,000 = ₹ 2,25,000.

(*iii*) $$\textit{Working Capital Turnover Ratio} = \frac{\text{Revenue from Operations (Net Sales)}}{\text{Working Capital}}$$

$$= \frac{₹\,5,40,000}{₹\,25,900} = 20.85 \text{ Times.}$$

Working Capital = Current Assets – Current Liabilities

= ₹ 1,01,900 – ₹ 76,000 = ₹ 25,900.

(*iv*) $$\textit{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{₹\,1,01,900}{₹\,76,000} = 1.34 : 1.$$

Current Assets (CA) = Inventories + Trade Receivables + Cash and Bank Balances

= ₹ 35,000 + ₹ 46,000 + ₹ 20,900 = ₹ 1,01,900.

Current Liabilities (CL) = Trade Payables + Short-term Provisions

= ₹ 34,000 + ₹ 42,000 = ₹ 76,000.

(*v*) $$\textit{Quick Ratio} = \frac{\text{Current Assets – Inventories}}{\text{Current Liabilities}}$$

$$= \frac{₹\,1,01,900 - ₹\,35,000}{₹\,76,000} = 0.88 : 1.$$

(*vi*) $$\textit{Net Profit Ratio} = \frac{\text{Net Profit after Tax}}{\text{Revenue from Operations (Net Sales)}} \times 100$$

$$= \frac{₹\,98,000}{₹\,5,40,000} \times 100 = 18.15\%.$$

(*vii*) $$\textit{Debt to Equity Ratio} = \frac{\text{Debt/Long-term Debt}}{\text{Equity}}$$

$$= \frac{₹\,40,000}{₹\,2,90,250 \text{ (WN 2)}} = 0.14 : 1.$$

(*viii*) $$\textit{Trade Receivables Turnover Ratio} = \frac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$$

$$= \frac{₹\,3,24,000 \text{ (}\textit{i.e.}\text{, 60\% of 5,40,000)}}{₹\,50,000\,[\textit{i.e.}\text{, } 1/2\,(54,000 + 46,000)]} = 6.48 \text{ Times.}$$

(*ix*) $$\textit{Proprietary Ratio} = \frac{\text{Shareholders' Funds/Equity}}{\text{Total Assets}} = \frac{₹\,2,90,250}{₹\,4,06,250} = 0.71 : 1.$$

(*x*) *Debt to Total Assets Ratio* $= \dfrac{\text{Debt}}{\text{Total Assets}}$

$$= \frac{₹\,40,000}{₹\,4,06,250} = 0.098 : 1.$$

(*xi*) *Earning Per Share (EPS)* $= \dfrac{\text{Profit after Tax} - \text{Preference Dividend}}{\text{Number of Equity Shares}}$

$$= \frac{₹\,98,000}{₹\,12,500} = ₹\,7.84.$$

Note: Preference Dividend is Nil.

(*xii*) *Return on Investment* $= \dfrac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$

$$= \frac{₹\,98,000 + ₹\,3,200 + ₹\,42,000}{₹\,3,30,250} \times 100$$

$$= \frac{₹\,1,43,200}{₹\,3,30,250} \times 100 = 43.36\%.$$

(*xiii*) *Price-Earning Ratio* $= \dfrac{\text{Market Value of Equity Share}}{\text{Earning Per Share (EPS)}} = \dfrac{₹\,39.20}{₹\,7.84} = 5 \text{ Times.}$

Working Notes:

1. Capital Employed = Share Capital + Reserves and Surplus + Long-term Borrowings

	₹
Equity Share Capital	1,25,000
10% Preference Share Capital	60,000
Reserves and Surplus	1,05,250
Long-term Borrowings (Debentures)	40,000
	3,30,250

2. Shareholders' Funds = Share Capital + Reserves and Surplus

Share Capital (Equity Share Capital + 10% Preference Share Capital)	1,85,000
Reserves and Surplus	1,05,250
	2,90,250

Illustration 15.

From the following information, calculate the following ratios:
(*i*) Operating Ratio, (*ii*) Inventory Turnover Ratio.

Cash Revenue from Operations —₹ 10,00,000	Credit Revenue from Operations —120% of Cash Revenue form Operations
Operating Expenses —10% of Total Revenue from Operations	Gross Profit Ratio —40%
Opening Stock—₹ 1,50,000	Closing Stock—₹ 20,000 more than Opening Stock

Solution:

(*i*) *Operating Ratio* $= \dfrac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Revenue from Operations}} \times 100$

$$= \frac{₹\,13,20,000 + ₹\,2,20,0000}{₹\,22,00,000} \times 100 = 70\%.$$

(*ii*) *Inventory Turnover Ratio* $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

$$= \frac{₹\,13,20,000}{\dfrac{₹\,1,50,000 + ₹\,1,70,000}{2}} = \frac{₹\,13,20,000}{₹\,1,60,000} = 8.25 \text{ Times.}$$

Notes:

- **Total Revenue from Operations = Cash Revenue from Operations + Credit Revenue from Operations**
  = ₹ 10,00,000 + (₹ 10,00,000 × 120/100) = ₹ 22,00,000.
- **Gross Profit = Total Revenue from Operations × Rate of Gross Profit/100**
  = ₹ 22,00,000 × 40/100 = ₹ 8,80,000.
- **Cost of Revenue from Operations = Total Revenue from Operations – Gross Profit**
  = ₹ 22,00,000 – ₹ 8,80,000 = ₹ 13,20,000.
- **Operating Expenses = 10% of Total Revenue from Operations**
  = ₹ 22,00,000 × 10/100 = ₹ 2,20,000.
- **Operating Cost = Cost of Revenue from Operations + Operating Expenses**
  = ₹ 13,20,000 + ₹ 2,20,000 = ₹ 15,40,000.

Illustration 16.

(*a*) From the following, calculate 'Trade Receivables Turnover Ratio':

Total Revenue from Operations for the year—₹ 8,40,000

Cash Revenue from Operations—40% of Credit Revenue from Operations

Closing Trade Receivables—₹ 2,00,000

Excess of Closing Trade Receivables over Opening Trade Receivables—₹ 80,000.

(*b*) From the following information, calculate 'Interest Coverage Ratio':

Profit after Interest and Tax—₹ 4,97,000

Rate of Income Tax—30%

12% Debentures—₹ 6,00,000.

Solution:

(*a*) Trade Receivables Turnover Ratio $= \dfrac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

$$= \frac{₹\,6,00,000}{₹\,1,60,000} = 3.75 \text{ Times.}$$

Working Notes:

1. *Calculation of Credit Revenue from Operations:*

Let Credit Revenue from Operations = x

Cash Revenue from Operations = 40% of $x = 4x/10$

$$x + 4x/10 = ₹\,8{,}40{,}000$$

$$10x + 4x = ₹\,84{,}00{,}000$$

$$14x = ₹\,8{,}40{,}000$$

$$x = ₹\,6{,}00{,}000 \text{ (Credit Revenue from Operations).}$$

2. Average Trade Receivables $= \dfrac{\text{Opening Trade Receivables + Closing Trade Receivables}}{2}$

$$= \frac{₹\,1{,}20{,}000 + ₹\,2{,}00{,}000}{2} = ₹\,1{,}60{,}000.$$

(*b*) Interest Coverage Ratio $= \dfrac{\text{Net Profit before Interest and Tax}}{\text{Interest on Long-term Debt}}$

$$= \frac{₹\,7{,}82{,}000}{₹\,72{,}000} = 10.86 \text{ Times.}$$

Working Notes:

1. Interest on Debentures = 12% of ₹ 6,00,000 = ₹ 72,000.
2. *Calculation of Net Profit before Interest and Tax:*

Profit after Interest and Tax	₹ 4,97,000
Rate of Tax	30%

Step 1: Let Profit after Interest and before Tax be x.

It means, Tax = 30% of x

x – 30% of x = ₹ 4,97,000

70% of x = ₹ 4,97,000

x = ₹ 4,97,000 × 100/70 = ₹ 7,10,000.

Step 2: *Calculate 'Profit before Interest and Tax':*

Profit before Interest and Tax = Profit after Interest and before Tax + Interest

= ₹ 7,10,000 + ₹ 72,000 = ₹ 7,82,000.

Illustration 17.

Current Ratio 2.5, Quick Ratio 1.5, Working Capital ₹ 1,20,000, Gross Profit @ 25% on Revenue from Operations was ₹ 1,00,000, Inventory Turnover Ratio 3 Times. Calculate Opening Inventory, Current Liabilities, Current Assets and Quick Assets.

Solution:

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = 2.5$$

Current Assets = 2.5 Current Liabilities

Working Capital = ₹ 1,20,000 (Given) [Working Capital = C.A. – C.L.]

Let Current Liabilities = x

∴ Current Assets = $2.5x$

$$2.5x - x = ₹\ 1{,}20{,}000$$

$$1.5x = ₹\ 1{,}20{,}000$$

$$x = \frac{₹\ 1{,}20{,}000}{1.5} = ₹\ 80{,}000 \text{ (Current Liabilities)}$$

$$\text{Current Assets} = ₹\ 80{,}000 \times 2.5 = ₹\ 2{,}00{,}000$$

$$\text{Quick Assets} = ₹\ 80{,}000 \times 1.5 = ₹\ 1{,}20{,}000$$

$$\text{Closing Inventories} = \text{Current Assets} - \text{Quick Assets}$$

$$= ₹\ 2{,}00{,}000 - ₹\ 1{,}20{,}000 = ₹\ 80{,}000$$

$$\text{Revenue from Operation} = ₹\ 1{,}00{,}000 \times \frac{100}{26} = ₹\ 4{,}00{,}000.$$

$$\text{Cost of Revenue from Operations} = ₹\ 4{,}00{,}000 - ₹\ 1{,}00{,}000 = ₹\ 3{,}00{,}000$$

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operations}}{\text{Average Inventory*}}$$

$$3 = \frac{₹\ 3{,}00{,}000}{\dfrac{\text{Opening Inventory} + ₹\ 80{,}000}{2}}$$

$$3\ (\text{Opening Inventory} + ₹\ 80{,}000) = ₹\ 6{,}00{,}000$$

$$\text{Opening Inventory} = \frac{(₹\ 6{,}00{,}000 - ₹\ 2{,}40{,}000)}{3}$$

$$= ₹\ 1{,}20{,}000 \text{ (Opening Inventory)}$$

$$\text{*Average Inventory} = \frac{\text{Opening Inventory} + \text{Closing Inventory}}{2}.$$

Illustration 18.

The ledger balances of Rashmi Ltd. as on 31st March, 2019 are as follows:

	₹		₹
Equity Share Capital	2,00,000	Fixed Assets (Net)	10,00,000
(20,000 Equity Shares of ₹ 10 each)		Non-current Investments	4,00,000
10% Preference Share Capital	2,00,000	Long-term Loans and Advances	2,00,000
Debentures Redemption Reserve	1,60,000	Inventories	7,90,000
Surplus, *i.e.*, Balance in Statement		Current Investments	20,000
of Profit and Loss (Current Years)	2,40,000	Trade Receivables	8,00,000
12% Debentures	10,00,000	Cash and Bank Balances	10,000
Long-term Provisions	6,00,000	Prepaid Expenses	10,000
Trade Payables	2,00,000	Short-term Loans and Advances	10,000
Short-term Bank Loan	80,000	Provision for Doubtful Debts	40,000
Provision for Tax	2,40,000	Other Current Liabilities	2,80,000

Additional Information:

(*i*) Revenue from Operations for the Year 2018–19 amounted to ₹ 20,00,000; Cash Revenue from Operations ₹ 4,00,000.

(*ii*) Net Purchases ₹ 17,80,000.

(*iii*) Opening Inventory ₹ 2,10,000.

(*iv*) Operating Expenses ₹ 2,00,000.

Calculate:

(*a*) Current Ratio;
(*b*) Quick Ratio;
(*c*) Debt to Equity Ratio;
(*d*) Debt to Total Assets Ratio;
(*e*) Proprietary Ratio;
(*f*) Interest Coverage Ratio;
(*g*) Inventory Turnover Ratio;
(*h*) Trade Receivables Turnover Ratio;
(*i*) Trade Payables Turnover Ratio;
(*j*) Working Capital Turnover Ratio;
(*k*) Gross Profit Ratio;
(*l*) Net Profit Ratio;
(*m*) Operating Ratio;
(*n*) Operating Profit Ratio.

Solution:

(*a*) *Current Ratio* = $\dfrac{\text{Current Assets}}{\text{Current Liabilities}} = \dfrac{₹\,16,00,000}{₹\,8,00,000} = 2:1.$

CALCULATION OF CURRENT ASSETS AND CURRENT LIABILITIES

Current Assets		₹	Current Liabilities	₹
Current Investments		20,000	Short-term Borrowings	80,000
Inventories		7,90,000	Trade Payables	2,00,000
Trade Receivables	8,00,000		Other Current Liabilities	2,80,000
Less: Provision	40,000	7,60,000	Short-term Provisions	2,40,000
Cash and Bank Balances		10,000	(Provision for Tax)	
Short-term Loans and Advances		10,000		
Other Current Assets		10,000		
(Prepaid Expenses)				
		16,00,000		8,00,000

(*b*) *Quick Ratio* = $\dfrac{\text{Quick Assets}}{\text{Current Liabilities}} = \dfrac{₹\,8,00,000}{₹\,8,00,000} = 1:1.$

Note: Quick Assets = Current Assets – Inventories – Prepaid Expenses
= ₹ 16,00,000 – ₹ 7,90,000 – ₹ 10,000 = ₹ 8,00,000.

(*c*) *Debt to Equity Ratio* = $\dfrac{\text{Debt}}{\text{Equity}} = \dfrac{₹\,16,00,000}{₹\,8,00,000} = 2:1.$

Notes:

1. Debt = Long-term Borrowings (12% Debentures) + Long-term Provisions
= ₹ 10,00,000 + ₹ 6,00,000 = ₹ 16,00,000.

2. Equity = Equity Share Capital + Preference Share Capital + Reserves and Surplus
= ₹ 2,00,000 + ₹ 2,00,000 + ₹ 4,00,000 (*i.e.*, ₹ 1,60,000 + ₹ 2,40,000) = ₹ 8,00,000.

(d) *Debt to Total Assets Ratio* = $\dfrac{\text{Debt}}{\text{Total Assets}} = \dfrac{₹\,16,00,000}{₹\,32,00,000} = 0.5:1.$

Note:

Total Assets = Fixed Assets + Non-current Investments + Long-term Loans and Advances + Current Investments + Inventories + Trade Receivables (Net) + Cash and Bank Balances + Short-term Loans and Advances + Other Current Assets (Prepaid Expenses)

= ₹ 10,00,000 + ₹ 4,00,000 + ₹ 2,00,000 + ₹ 20,000 + ₹ 7,90,000 + ₹ 7,60,000 + ₹ 10,000 + ₹ 10,000 + ₹ 10,000 = ₹ 32,00,000.

Or

Total Assets = Shareholders Funds + Non-current Liabilities + Current Liabilities

= [₹ 2,00,000 + ₹ 2,00,000 + ₹ 1,60,000 + ₹ 2,40,000] + ₹ 16,00,000 + ₹ 8,00,000

= ₹ 32,00,000.

(e) *Proprietary Ratio* = $\dfrac{\text{Shareholders' Funds/Equity}}{\text{Total Assets}} = \dfrac{₹\,8,00,000}{₹\,32,00,000} = 0.25:1.$

(f) *Interest Coverage Ratio* = $\dfrac{\text{Net Profit before Interest and Tax}}{\text{Interest on Long-term Borrowings}}$

$$= \frac{₹\,6,00,000}{₹\,1,20,000} = 5 \text{ Times.}$$

Notes:

1. Net Profit before Interest and Tax = Profit after Tax + Tax + Interest
= ₹ 2,40,000 + ₹ 2,40,000 + ₹ 1,20,000 = ₹ 6,00,000.

2. Interest on Debentures = 12% of ₹ 10,00,000 = ₹ 1,20,000.

(g) *Inventory Turnover Ratio* = $\dfrac{\text{Cost of Goods Sold/Cost of Revenue from Operations}}{\text{Average Inventory}}$

$$= \frac{₹\,12,00,000}{₹\,5,00,000} = 2.4 \text{ Times.}$$

Notes:

1. Cost of Revenue from Operations = Net Purchases + Opening Inventory – Closing Inventory
= ₹ 17,80,000 + ₹ 2,10,000 – ₹ 7,90,000 = ₹ 12,00,000.

2. Average Inventory = $\dfrac{\text{Opening Inventory + Closing Inventory}}{2}$

$$= \frac{₹\,2,10,000 + ₹\,7,90,000}{2} = ₹\ 5,00,000.$$

(h) *Trade Receivables Turnover Ratio* = $\dfrac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

$$= \frac{₹\,16,00,000}{₹\,8,00,000} = 2 \text{ Times.}$$

Notes:

1. Credit Revenue from Operations = Revenue from Operations – Cash Revenue from Operations
   = ₹ 20,00,000 – ₹ 4,00,000 = ₹ 16,00,000.
2. In the absence of Opening Trade Receivables, Closing Trade Receivables have been used in the above formula.
3. Provision for Doubtful Debts is not deducted from the amount of Trade Receivables while calculating Trade Receivables Turnover Ratio.

(*i*) *Trade Payables Turnover Ratio* = $\dfrac{\text{Net Credit Purchases}}{\text{Average Trade Payables}}$

$$= \frac{₹\,17,80,000}{₹\,2,00,000} = 8.9 \text{ Times.}$$

Notes:

1. In the absence of any information regarding Opening Trade Payables, Closing Trade Payables have been used.
2. It has been assumed that all purchases are on credit.

(*j*) *Working Capital Turnover Ratio* = $\dfrac{\text{Revenue from Operations}}{\text{Working Capital}}$

$$= \frac{₹\,20,00,000}{₹\,16,00,000\,(\text{CA}) - ₹\,8,00,000\,(\text{CL})}$$

$$= \frac{₹\,20,00,000}{₹\,8,00,000} = 2.5 \text{ Times.}$$

(*k*) *Gross Profit Ratio* = $\dfrac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$

$$= \frac{₹\,8,00,000}{₹\,20,00,000} \times 100 = 40\%.$$

Note: Gross Profit = Revenue from Operations – Cost of Revenue from Operations
= ₹ 20,00,000 – ₹ 12,00,000 = ₹ 8,00,000.

(*l*) *Net Profit Ratio* = $\dfrac{\text{Net Profit}}{\text{Revenue from Operations}} \times 100 = \dfrac{₹\,2,40,000}{₹\,20,00,000} \times 100 = 12\%.$

Note: Net Profit = Gross Profit + Other Income – Indirect Expenses – Tax
= ₹ 8,00,000 + NIL – [₹ 2,00,000 (Operating Expenses)
– ₹ 1,20,000 (Interest on Debentures: Non-Operating Expenses)] – ₹ 2,40,000
= ₹ 2,40,000.

(*m*) *Operating Ratio* = $\dfrac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Revenue from Operations}} \times 100$

$$= \frac{₹\,12,00,000 + ₹\,2,00,000}{₹\,20,00,000} \times 100 = 70\%.$$

(*n*) *Operating Profit Ratio* $= \dfrac{\text{Net Operating Profit}}{\text{Revenue from Operations}} \times 100$

$$= \frac{₹\,6,00,000}{₹\,20,00,000} \times 100 = 30\%.$$

Note: Net Operating Profit = Gross Profit – Operating Expenses + Operating Income

= ₹ 8,00,000 – ₹ 2,00,000 + NIL = ₹ 6,00,000.

Or

= Revenue from Operations – Cost of Revenue from Operations – Operations – Operating Expenses

= ₹ 20,00,000 – ₹ 12,00,000 – ₹ 2,00,000 = ₹ 6,00,000.

Unsolved Questions

1. From the following Balance Sheet of Paper Products Ltd., calculate Debt to Equity Ratio:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital		2,50,000
(b) Reserves and Surplus		50,000
2. Non-Current Liabilities		
Long-term Borrowings		4,50,000
3. Current Liabilities		
(a) Trade Payables		50,000
(b) Other Current Liabilities		25,000
Total		8,25,000
II. ASSETS		
1. Non-Current Assets		
(a) Fixed Assets		
(i) Tangible Assets		4,00,000
(ii) Intangible Assets		1,00,000
(b) Non-Current Investments		1,75,000
2. Current Assets		
(a) Inventories		50,000
(b) Trade Receivables		75,000
(c) Cash and Bank Balances		25,000
Total		8,25,000

2. From the following Balance Sheet as at 31st March, 2019 of Matrix Ltd., calculate Interest Coverage Ratio:

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital		10,00,000
(b) Reserves and Surplus		7,50,000
2. Non-Current Liabilities		
(a) Long-term Borrowings	1	12,00,000
(b) Other Long-term Liabilities		4,00,000
3. Current Liabilities		
(a) Trade Payables		2,00,000
(b) Other Current Liabilities		1,00,000
(c) Short-term Provisions (Provision for Tax)		4,00,000
Total		40,50,000
II. ASSETS		
1. Non-Current Assets		
(a) Fixed Assets—Tangible		20,00,000
(b) Non-Current Investments		5,00,000
2. Current Assets		
(a) Current Investments		5,00,000
(b) Inventories		4,00,000
(c) Trade Receivables		3,50,000
(d) Cash and Bank Balances		3,00,000
Total		40,50,000

Note to Accounts

	₹
1. Long-term Borrowings	
5,000; 10% Debentures of ₹ 100 each	5,00,000
Term Loan from Bank	5,00,000
Loan from Shareholders/Directors	2,00,000
	12,00,000

Additional Information:

The company's profit for the year after interest but before tax was ₹ 6,20,000. Provision for Tax was ₹ 4,00,000. Interest on Bank Loan was ₹ 40,000 and that on Loan from Shareholders/Directors was ₹ 10,000.

3. From the following Balance Sheet of *ABC* Ltd. as at 31st March, 2019, calculate Debt to Equity Ratio:

BALANCE SHEET

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital	1	10,00,000
(b) Reserves and Surplus	2	2,40,000
2. Non-Current Liabilities		
(a) Long-term Borrowings	3	2,00,000
(b) Long-term Provisions		50,000
3. Current Liabilities		
(a) Trade Payables		4,30,000
(b) Other Current Liabilities		20,000
(c) Short-term Provisions (Provision for Tax)		3,00,000
Total		22,40,000

II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible		7,30,000
—Intangible		10,000
2. Current Assets		
(a) Inventories		7,50,000
(b) Trade Receivables		6,40,000
(c) Cash and Bank Balances		1,00,000
(d) Other Current Assets		10,000
Total		22,40,000

Notes to Accounts

	₹
1. Share Capital	
Equity Share Capital	5,00,000
12% Preference Share Capital	5,00,000
	10,00,000
2. Reserves and Surplus	
General Reserve	2,00,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	40,000
	2,40,000
3. Long-term Borrowings	
12% Debentures	1,50,000
Loan from Bank	50,000
	2,00,000

4. From the following data, calculate:

(i) Current Ratio; and (ii) Operating Ratio.

Sundry Debtors—₹ 10,000; Bills Payable—₹ 6,000; Stock—₹ 15,000; Cash and Bank Balances ₹ 15,000; Creditors—₹ 14,000; Revenue from Operations (Net Sales)—₹ 60,000; Operating Expenses—₹ 12,000; Cost of Revenue from Operations (Cost of Goods Sold)—₹ 18,000.

5. Following is the Balance Sheet of *ABC* Limited as at 31st March, 2019:

Particulars		₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital		48,000
(b) Reserves and Surplus		12,000
2. Non-Current Liabilities		
Long-term Borrowings		30,000
3. Current Liabilities		
(a) Short-term Borrowings—Bank Overdraft		10,000
(b) Trade Payables		36,800
(c) Short-term Provisions (Provision for Tax)		1,200
Total		1,38,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible		90,000
2. Current Assets		
(a) Inventories		24,000
(b) Trade Receivables		18,000
(c) Cash and Bank Balances		4,560
(d) Other Current Assets (Prepaid Expenses)		1,440
Total		1,38,000

Calculate the following:

(i) Current Ratio and (ii) Liquid Ratio.

6. Following is the Balance Sheet of Bharati Ltd. You are required to calculate Working Capital Turnover Ratio:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital		2,50,000
(b) Reserves and Surplus		1,00,000
2. Current Liabilities		
(a) Trade Payables		1,25,000
(b) Short-term Provisions		25,000
Total		5,00,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible (Net)		2,00,000
2. Current Assets		
(a) Short-term Investments		50,000
(b) Inventories		50,000
(c) Trade Receivables		1,25,000
(d) Cash and Bank Balances		75,000
Total		5,00,000

(i) Total Sales during the year ₹ 10,00,000.

(ii) Sales Return during the year ₹ 1,00,000.

[**Hints:** 1. Working Capital = ₹ 3,00,000 (C.A.) – ₹ 1,50,000 (C.L.) = ₹ 1,50,000
2. Revenue from Operations = ₹ 10,00,000 – ₹ 1,00,000 = ₹ 9,00,000.]

7. From the following Balance Sheet of Woodland Ltd. as at 31st March, 2019, calculate (i) Debt to Equity Ratio; (ii) Proprietary Ratio; and (iii) Debt to Total Assets Ratio:

BALANCE SHEET *as at 31st March, 2019*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital		10,00,000
(b) Reserves and Surplus		2,00,000
2. Non-Current Liabilities		
(a) Long-term Borrowings		2,60,000
(b) Long-term Provisions		40,000
3. Current Liabilities		
Trade Payables		3,00,000
Total		18,00,000
II. ASSETS		
1. Non-Current Assets		
(a) Fixed Assets—Tangible		11,00,000
(b) Non-Current Investments		2,00,000
2. Current Assets		
(a) Inventories		2,00,000
(b) Trade Receivables		1,00,000
(c) Cash and Bank Balances		2,00,000
Total		18,00,000

8. Following is the Balance Sheet of Arvind Mills Ltd., as at 31st March, 2019:

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital		6,00,000
(b) Reserves and Surplus		4,00,000
2. Non-Current Liabilities		
Long-term Borrowings	1	7,00,000
3. Current Liabilities		
(a) Trade Payables	2	1,60,000
(b) Other Current Liabilities	3	10,000
(c) Short-term Provisions	4	1,30,000
Total		20,00,000
II. ASSETS		
1. Non-Current Assets		
(a) Fixed Assets—Tangible		13,00,000
(b) Non-Current Investments		1,50,000
2. Current Assets		
(a) Inventories		3,00,000
(b) Trade Receivables	5	2,00,000
(c) Cash and Bank Balances		50,000
Total		20,00,000

Notes to Accounts

	₹
1. Long-term Borrowings	
8% Debentures	7,00,000
2. Trade Payables	
Sundry Creditors	60,000
Bills Payable	1,00,000
	1,60,000
3. Other Current Liabilities	
Outstanding Expenses	10,000
4. Short-term Provisions	
Provision for Tax	1,30,000
5. Trade Receivables	
Debtors	2,00,000

Other information supplied is as follows:

	₹
Revenue from Operations	30,00,000
Cost of Revenue from Operations	25,80,000
Net Profit before Tax	2,00,000
Net Profit after Tax	1,00,000

You are required to calculate:

(i) Liquid Ratio, (ii) Proprietary Ratio, (iii) Current Ratio, and (iv) Gross Profit Ratio.

9. The Balance Sheet of *X* Ltd. as at 31st March, 2019 was as follows:

BALANCE SHEET

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(a) Share Capital		4,00,000
(b) Reserves and Surplus		1,16,000
2. Non-Current Liabilities		
Long-term Borrowings		2,00,000
3. Current Liabilities		
(a) Trade Payables		1,20,000
(b) Other Current Liabilities		4,000
Total		8,40,000
II. ASSETS		
1. Non-Current Assets		
Fixed Assets—Tangible		3,00,000
—Intangible		2,40,000
2. Current Assets		
(a) Inventories		1,60,000
(b) Trade Receivables		90,000
(c) Cash and Bank Balances		34,000
(d) Other Current Assets	1	16,000
Total		8,40,000

Note to Accounts

	₹
1. Other Current Assets	
Prepaid Expenses	16,000

Other Information: ₹

Revenue from Operations (Net Sales) 8,00,000

Cost of Revenue from Operations (Cost of Goods Sold) 4,80,000

You are required to calculate following ratios:

(i) Current Ratio, (ii) Quick Ratio and (iii) Inventory Turnover Ratio.

GUIDE TO ANSWERS

1. 1.5 : 1.

2. 7.2 Times.

3. 0.2 : 1.

4. (a) Current Ratio—2 : 1; (b) Operating Ratio—50%.

5. (i) Current Ratio—1 : 1; (ii) Liquid Ratio—0.47 : 1.

6. 6 Times.

7. (i) Debt to Equity Ratio—1 : 4; (ii) Proprietary Ratio—66.67%; (iii) Debt to Total Assets Ratio—0.17 : 1.

8. (i) 0.83 : 1; (ii) 0.5 : 1; (iii) 1.83 : 1; (iv) 14%.

9. (i) 2.42 : 1; (ii) 1 : 1; (iii) 3 Times.

Model Test Paper 1

Time Allowed: 3 Hrs. **Max. Marks: 80**

General Instructions:

(Candidates are allowed additional 15 minutes for only reading the paper. They must NOT start writing during this time.)

(*i*) ***Part I*** *of* ***Section A*** *is Compulsory.*

(*ii*) *Answer* ***any 4*** *Questions from* ***Part II*** *of* ***Section A*** *and* ***any two*** *questions from* ***either Section B*** or ***Section C***.

(*iii*) *The intended marks for questions or parts of questions are given in the brackets [].*

(*iv*) *Transactions should be recorded in the answer book.*

(*v*) *All calculations should be shown clearly.*

(*vi*) *All working, including rough work, should be done on the same page as, and adjacent to, the rest of the answer.*

Section A

Part I (12 Marks)

(*Answer* ***all*** *questions*)

1. Answer each of the following questions briefly:

(*i*) What is meant by 'Redemption of Debentures by purchase in the Open Market'?

(*ii*) Malti, Paro and Arti are partners in a firm having fixed capital of ₹ 80,000, ₹ 40,000 and ₹ 50,000 respectively sharing profit in the ratio of 7 : 6 : 4. The rate of interest on capital was agreed at 10% per annum, but it was wrongly credited to them at 12% per annum. Give the necessary adjustment entry to rectify the error.

(*iii*) How are profits estimated from the date of last accounting year till the date of death of a partner, and, how the profit of deceased partner will be adjusted in case profit-sharing ratio of continuing partners changes?

(*iv*) Innovations Ltd. has the following balances appearing in its Balance Sheet:

	₹
Securities Premium Reserve	22,00,000
9% Debentures	1,20,00,000
Underwriting Commission	10,00,000

The company decided to redeem its 9% Debentures at a premium of 10%. You are required to suggest the way in which the company can utilise the Securities Premium Reserve.

(*v*) List **any four** items which are included under the head 'Reserves and Surplus' of the company's Balance Sheet as per Schedule III of the Companies Act, 2013.

(*vi*) Lenovo Ltd. took over assets of ₹ 8,40,000 and liabilities of ₹ 80,000 of Motorola Ltd. at an agreed value of ₹ 7,20,000. Lenovo Ltd. paid to Motorola Ltd. by issue of 9% Debentures of ₹ 100 each at a premium of 20%. Pass necessary Journal entries to record the above transactions in the books of Lenovo Ltd.

[6 × 2 = 12]

Part II (48 Marks)

(*Answer **any four** questions*)

2. Antony and Bose are partners in a firm sharing profits in the ratio of 2 : 3. They admitted Boman, an old employee as a partner for 1/2 share in the profits. Boman will bring ₹ 5,00,000 for his capital and the capitals of Antony and Bose will be adjusted in the profit-sharing ratio. For this Current Accounts will be opened. Balance Sheet of the firm as at 31st March, 2019 before Boman's admission was as follows:

BALANCE SHEET OF ANTONY AND BOSE *as at 31st March, 2019*

Liabilities		₹	Assets		₹
Creditors		1,20,000	Cash in Hand		40,000
Bills Payable		1,60,000	Sundry Debtors	2,05,000	
General Reserve		80,000	*Less:* Provision for Doubtful Debts	5,000	2,00,000
Workmen Compensation Reserve		40,000	Furniture		2,00,000
Capital A/cs: Antony	3,75,000		Machinery		3,10,000
Bose	1,25,000	5,00,000	Building		1,10,000
			Profit and Loss A/c		40,000
		9,00,000			9,00,000

Other terms of the agreement were as follows:

(*i*) Boman will bring ₹ 1,75,000 for his share of goodwill.

(*ii*) Building will be revalued at ₹ 3,90,000 and machinery be reduced by ₹ 70,000.

(*iii*) A liability towards damages payable to a customer of ₹ 14,000 is to be accounted.

(*iv*) All Debtors are good.

(*v*) There is a claim against the firm for damages, liability to the extent of ₹ 5,000 is to be created.

(*vi*) ₹ 10,000 included in creditors was not payable.

Prepare Revaluation Account, Partners' Capital Accounts, Partners' Current Accounts and Balance Sheet of the new firm. [12]

3. (*a*) Tara Industries Ltd. had issued 5,000, 9% Debentures of ₹ 100 each at par redeemable at 105% after 4 years. The company purchased 600 of these debentures for cancellation, 500 Debentures @ ₹ 95 per debenture and @ ₹ 98 per debenture for the remaining 100 Debentures. The expenses on purchase of Debentures were ₹ 400. Pass Journal entries for cancellation of debentures in the books of the company.

(*b*) Pass the Journal entries for forfeiture and reissue of shares in the following cases:

(*i*) Export Ltd. forfeited 600 shares of ₹ 10 each, ₹ 7 called-up, on which the shareholder had paid application and allotment money of ₹ 5 per share. Out of these, 450 shares were reissued to Mahesh as ₹ 7 paid-up for ₹ 8 per share.

(*ii*) Swan Ltd. forfeited 300 shares of ₹ 10 each, ₹ 8 called-up, issued at a premium of ₹ 2 per share held by 'Raj' for non-payment of allotment money of ₹ 5 per share (including premium). Out of these, 210 shares were reissued to Sanjay as ₹ 8 called-up for ₹ 10 per share. [4 + 8 = 12]

4. (*a*) Priya, Riya and Siya are partners sharing profits in the ratio of 6 : 3 : 1. They admitted Miya into partnership with effect from 1st April, 2019. New profit-sharing ratio among Priya, Riya, Siya and Miya will be 3 : 3 : 3 : 1. Partners decide to record the effect of the following without affecting the book values (after the required adjustment from Workmen Compensation Reserve and Investment Fluctuation Reserve) by passing an adjustment entry:

	Book Values (₹)
General Reserve	1,40,000
Profit and Loss (Cr.)	60,000
Advertisement Suspense A/c	50,000
Workmen Compensation Reserve	30,000
Investment Fluctuation Reserve	20,000

Additional Information:

(*i*) Claim on account of Workmen Compensation is ₹ 20,000.

(*ii*) Book value of Investment is ₹ 1,00,000 (Market Value ₹ 85,000).

Pass the required adjustment entry.

(*b*) Rose, Daisy and Lily were partners in a firm sharing profits and losses in the ratio of 5 : 3 : 2. On 31st March, 2019, their Balance Sheet was as under:

BALANCE SHEET *as at 31st March, 2019*

Liabilities		₹	Assets		₹
Creditors		55,000	Cash		40,000
General Reserve		30,000	Debtors	45,000	
Capitals:			*Less:* Provision	5,000	40,000
Rose	1,50,000		Stock		50,000
Daisy	1,25,000		Machinery		1,50,000
Lily	75,000	3,50,000	Patents		30,000
			Building		1,00,000
			Profit and Loss A/c		25,000
		4,35,000			4,35,000

Rose retired on 1st April, 2019 and it was agreed that:

(*i*) Debtors of ₹ 2,000 will be written off as bad debts and a provision of 5% on debtors for bad and doubtful debts will be maintained.

(*ii*) Patents will be written off and stock, machinery and building will be reduced by 5%.

(*iii*) An unrecorded creditor of ₹ 10,000 will be accounted.

(*iv*) Goodwill is valued at ₹ 3,00,000.

(*v*) Daisy and Lily will share future profits in the ratio of 2 : 3.

Pass necessary Journal entries for the above transactions in the books of the firm on Rose's retirement. [4 + 8 = 12]

5. (*a*) Partners Strong, Weak and Feeble of a firm distributed profit for the year ended 31st March, 2019 ₹ 1,40,000 in the ratio of 2 : 2 : 1 without providing for the following:

(*i*) Strong and Weak each were to get salary of ₹ 1,500 per quarter.

(*ii*) Feeble was to get a commission of ₹ 8,000.

(*iii*) Strong and Feeble had guaranteed a minimum profit of ₹ 50,000 p.a. to Weak.

(*iv*) Profits were to be shared in the ratio of 3 : 3 : 2.

Pass necessary Journal entry for the above adjustments in the books of the firm.

(*b*) A partnership firm earned net profits during the last three years as follows:

Year	2016–17	2017–18	2018–19
Profits (₹)	1,90,000	2,20,000	2,50,000

Capital employed in the firm throughout the above period has been ₹ 4,00,000. Having regard to the risk involved, 15% is considered to be a fair return on the capital. Remuneration of all the partners during this period is estimated to be ₹ 1,00,000 per annum.

Calculate the value of goodwill on the basis of:

(*i*) three years' purchase of Average Profit;

(*ii*) two years' purchase of Super Profits earned on average basis during the above mentioned three years; and

(*iii*) Capitalisation of Super Profit. [6 + 6 = 12]

6. Following is the Balance Sheet as at 31st March, 2019 of Ram and Rahim, who share profits and losses in the ratio of 4 : 1:

BALANCE SHEET *as at 31st March, 2019*

Liabilities		₹	Assets		₹
Sundry Creditors		80,000	Bank		2,00,000
Bank Overdraft		60,000	Debtors	1,70,000	
Ram's Brother's Loan		80,000	*Less:* Provision for Doubtful Debts	20,000	1,50,000
Rahim's Loan		30,000	Stock		1,50,000
Investment Fluctuation Fund		50,000	Investments		2,50,000
Capital A/cs:			Building		2,50,000
Ram	5,00,000		Goodwill		1,00,000
Rahim	4,00,000	9,00,000	Profit and Loss A/c		1,00,000
		12,00,000			12,00,000

The firm was dissolved on 1st April, 2019 and following was agreed:

(*i*) Ram agreed to pay his brother's Loan.

(*ii*) Debtors of ₹ 50,000 proved bad.

(*iii*) Other assets realised: Investments 20% *less*; and goodwill at 60%.

(*iv*) One of the creditors for ₹ 50,000 was paid ₹ 30,000.

(*v*) Building was auctioned for ₹ 3,00,000 and the auctioneer's commission paid was ₹ 10,000.

(*vi*) Rahim took a part of stock at ₹ 40,000 (being 20% less than the book value). Balance stock realised 50%.

(*vii*) Realisation expenses were ₹ 20,000.

Prepare: (*i*) Realisation Account, (*ii*) Partners' Capital Accounts, (*iii*) Bank Account. [12]

7. (*a*) Nova Ltd. had issued on 1st October, 2014, 10,000, 9% Debentures of ₹ 100 each at par redeemable at par at the end of 4 years. The Board of Directors decided to transfer the amount to Debentures Redemption Reserve as per the Companies Act, 2013, at the time of redemption.

Investments, as required by Rules framed under Section 71(4), were made on 1st April of the financial year in which redemption is due and realised at book value at the time of redemption. Interest on the investment is also received @ 8% per annum.

Pass the necessary Journal entries for Redemption of Debentures, Debentures Redemption Reserve and Debentures Redemption Investment. Ignore interest on Debentures.

(*b*) Pass necessary Journal entries relating to the issue of debentures for the following:

(*i*) Issued 4,000; 9% Debentures of ₹ 100 each at a premium of 8% redeemable at 10% premium.

(*ii*) Issued 6,000; 9% Debentures of ₹ 100 each at par, repayable at a premium of 10%.

(*iii*) Issued 10,000; 9% Debentures of ₹ 100 each at a premium of 5%, redeemable at par. [6 + 6 = 12]

8. (*a*) Sajal Ltd. offered 32,000 equity shares of ₹ 100 each to public at a premium of ₹ 20 per share. The amount was payable as: ₹ 20 on application; ₹ 40 (including premium) on allotment; and the balance on first and final call. Subscription was received for 30,000 shares.

All the amounts were duly received except from a shareholder holding 4,000 shares who did not pay the first and final call. His shares were forfeited. Show 'Share Capital' in the Balance Sheet of Sajal Ltd.

(*b*) From the following information extracted from the books of Imara Ltd., prepare Balance Sheet of the company as at 31st March, 2019 as per Schedule III, Part I of the Companies Act, 2013:

	(₹ in "000)		(₹ in "000)
Long-term Borrowings	600	Short-term Borrowings	180
Share Capital	780	Trade Payables	40
Fixed Assets (Tangible)	1,200	Reserves and Surplus	200
Trade Receivables	160	Inventories	40
Share Application Money Pending Allotment	20	Cash and Cash Equivalents	120
		Non-current Investments	400
Long-term Provisions	200	Current Investments	100
Prepaid Expenses	20	Outstanding Expenses	20

Note: Proposed Dividend for the year 2018–19 is ₹ 20,000. [3 + 9 = 12]

Section B
(20 Marks)

(*Answer **any two** questions*)

9. (*a*) While computing Trade Receivables Turnover Ratio, is 'Provision for Doubtful Debts' deducted from the total amount of Trade Receivables? Give reason.

(*b*) (*i*) Gross Profit Ratio of Moon Ltd. is 25%. State giving reason whether the ratio will *increase* or *decrease* or *not change* on purchase of goods for ₹ 30,000 against cheque.

(*ii*) Gross Profit Ratio of Star Ltd. is 20%. State giving reason, whether the ratio will *increase* or *decrease* or *not change* on sale of goods for ₹ 30,000 on credit.

(*c*) On the basis of the following information, calculate:

(*i*) Operating Ratio;

(*ii*) Inventory Turnover Ratio;

(*iii*) Proprietary Ratio.

Information:

Cash Revenue from Operations	₹ 10,00,000
Credit Revenue from Operations	120% of Cash Revenue from Operations
Operating Expenses	10% of Total Revenue from Operations
Gross Profit Ratio	40%
Opening Inventory	₹ 1,50,000
Closing Inventory ₹ 20,000 more than Opening Inventory	
Current Assets	₹ 3,00,000
Current Liabilities	₹ 2,00,000
Share Capital	₹ 6,00,000
Fixed Assets	₹ 5,00,000

[2 + 2 + 6 = 10]

10. Bhushan Steel Ltd. gives you the following information, you are required to prepare Cash Flow Statement as per AS-3 (Revised) for the year ended 31st March, 2019:

BALANCE SHEET OF BHUSHAN STEEL LTD. *as at 31st March 2019*

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		20,00,000	20,00,000
(*b*) Reserves and Surplus	1	9,00,000	5,00,000
2. Non-Current Liabilities			
Long-term Borrowings	2	10,00,000	10,00,000
3. Current Liabilities			
(*a*) Trade Payables		15,50,000	6,00,000
(*b*) Other Current Liabilities	3	1,00,000	70,000
Total		55,50,000	41,70,000

II. ASSETS			
1. Non-Current Assets			
(*a*) Fixed Assets			
(*i*) Tangible Assets (Machinery)		30,00,000	20,00,000
(*ii*) Intangible Assets (Patents)		3,00,000	3,40,000
(*b*) Non-current Investments		2,00,000	1,50,000
2. Current Assets			
(*a*) Inventories		4,00,000	6,00,000
(*b*) Trade Receivables		7,00,000	9,00,000
(*c*) Cash and Bank Balances		9,50,000	1,80,000
Total		55,50,000	41,70,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Surplus, *i.e.*, Balance in Statement of Profit and Loss	9,00,000	5,00,000
2. Long-term Borrowings		
10% Debentures	10,00,000	10,00,000
3. Other Current Liabilities		
Unclaimed Dividend	60,000	...
Outstanding Expenses	40,000	70,000
	1,00,000	70,000

Additional Information:

1. During the year, a Machinery costing ₹ 4,00,000, on which depreciation charged was ₹ 2,20,000, was sold at a profit of ₹ 60,000.
2. Depreciation charged on machinery was ₹ 7,00,000.
3. During the year, the company declared Interim Dividend @ 10%.
4. At the end of the year, investment costing ₹ 50,000 were sold at a profit of 20%. New investment was also purchased at the end of the current accounting year. [10]

11. (*a*) State **any two** objectives of Common-size Income Statement.

(*b*) What is meant by the term 'Cash Equivalents' as per AS-3, Cash Flow Statement?

(*c*) List **any two** Financing Activities which result into inflow of cash.

(*d*) Prepare Common-size Statement of Profit and Loss from the following information:

	31st March, 2019	31st March, 2018
Revenue from Operations	₹ 15,00,000	₹ 10,00,000
Other Income	₹ 1,80,000	₹ 2,00,000
Cost of Materials Consumed	₹ 9,00,000	₹ 5,00,000
Other Expenses	₹ 1,50,000	₹ 1,00,000
Tax Rate	30%	30%

[2 + 2 + 2 + 4 = 10]

Answers

1. (*i*) When a company purchases its own debentures in the open market for the purpose of cancellation, such an act of purchasing and cancelling the debentures is known as redemption by purchase of debentures in the open market.

(*ii*) ADJUSTMENT JOURNAL ENTRY

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Malti's Current A/c ...Dr.		200	
	Arti's Current A/c ...Dr.		200	
	To Paro's Current A/c			400
	(Being the excess interest credited to partners now rectified)			

ADJUSTMENT TABLE

Particulars	Malti's Current A/c		Paro's Current A/c		Arti's Current A/c		Firm	
	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)
Interest on Capital already credited @ 12%, now taken back	9,600	...	4,800	...	6,000	...	...	20,400
Interest on Capital to be credited @ 10%	...	8,000	...	4,000	...	5,000	17,000	...
Share of Profit ₹ 3,400 (*i.e.*, ₹ 20,400 – ₹ 17,000) in ratio of 7 : 6 : 4	...	1,400	...	1,200	...	800	3,400	...
	9,600	9,400	4,800	5,200	6,000	5,800	20,400	20,400
Net Effect	200 Dr.		400 Cr.		200 Dr.		Nil	

(*iii*) (*a*) On the basis of time; (*b*) On the basis of sales or turnover.
Deceased partner's share of profit will be credited to his Capital Account and debited to the continuing Partners' Capital Accounts in their Gaining Ratio when the profit-sharing ratio of the continuing partners changes.

(*iv*) Company can utilise the Securities Premium Reserve of ₹ 22,00,000 as follows:
(*a*) ₹ 10,00,000 to write off underwriting commission.
(*b*) Remaining ₹ 12,00,000 to provide for premium on redemption of 9% Debentures.

(*v*) (*a*) Capital Reserve.
(*b*) Securities Premium Reserve.
(*c*) Debentures Redemption Reserve.
(*d*) Surplus, *i.e.*, Balance in Statement of Profit and Loss.

(*vi*) JOURNAL OF LENOVO LTD.

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Sundry Assets A/c ...Dr.		8,40,000	
	To Sundry Liabilities A/c			80,000
	To Motorola Ltd.			7,20,000
	To Capital Reserve A/c (Balancing Figure)			40,000
	(Being assets and liabilities taken over from Motorola Ltd.)			
	Motorola Ltd. ...Dr.		7,20,000	
	To 9% Debentures A/c			6,00,000
	To Securities Premium Reserve A/c			1,20,000
	(Being 6,000; 9% Debentures issued at a premium of 20%)			

Working Note:

No. of Debentures to be issued = Purchase Consideration ÷ Issue Price = ₹ 7,20,000 ÷ ₹ 120 = 6,000 Debentures.

2.

REVALUATION ACCOUNT

Dr. Particulars		₹	Cr. Particulars	₹
To Machinery A/c		70,000	By Building A/c	2,80,000
To Liabilities against Damages Claims A/c*		19,000	By Provision for Doubtful Debts A/c (WN 4)	5,000
To Gain (Profit) transferred to:			By Creditors A/c	10,000
Antony's Capital A/c (2/5)	82,400			
Bose's Capital A/c (3/5)	1,23,600	2,06,000		
		2,95,000		2,95,000

*Liabilities against damages claims = ₹ 14,000 + ₹ 5,000 = ₹ 19,000.

PARTNERS' CAPITAL ACCOUNTS

Dr. Particulars	Antony ₹	Bose ₹	Boman ₹	Cr. Particulars	Antony ₹	Bose ₹	Boman ₹
To Profit and Loss A/c	16,000	24,000	...	By Balance *b/d*	3,75,000	1,25,000	...
To Antony's Current A/c (Bal. Fig.)	3,59,400	...	...	By Workmen Compensation Reserve A/c	16,000	24,000	...
To Bose's Current A/c (Bal. Fig.)	...	1,01,600	...	By General Reserve A/c	32,000	48,000	...
				By Revaluation A/c (Gain)	82,400	1,23,600	...
To Balance *c/d* (WN 3)	2,00,000	3,00,000	5,00,000	By Bank A/c	...	...	5,00,000
				By Premium for Goodwill A/c	70,000	1,05,000	...
	5,75,400	4,25,600	5,00,000		5,75,400	4,25,600	5,00,000

PARTNERS' CURRENT ACCOUNTS

Dr. Particulars	Antony ₹	Bose ₹	Cr. Particulars	Antony ₹	Bose ₹
To Balance *c/d*	3,59,400	1,01,600	By Antony's Capital A/c	3,59,400	...
			By Bose's Capital A/c	...	1,01,600
	3,59,400	1,01,600		3,59,400	1,01,600

BALANCE SHEET OF NEW FIRM *as at 1st April, 2019*

Liabilities		₹	Assets	₹
Creditors		1,10,000	Cash in Hand	40,000
Bills Payable		1,60,000	Cash at Bank (₹ 5,00,000 + ₹ 1,75,000)	6,75,000
Liabilities against Damages Claims		19,000	Sundry Debtors	2,05,000
Capital A/cs:			Furniture	2,00,000
Antony	2,00,000		Machinery	2,40,000
Bose	3,00,000		Building	3,90,000
Boman	5,00,000	10,00,000		
Current A/cs:				
Antony	3,59,400			
Bose	1,01,600	4,61,000		
		17,50,000		17,50,000

Working Notes:

1. Unless agreed otherwise, sacrificing ratio of old partners will be same as their old profit-sharing ratio.
2. *Calculation of New Profit-sharing Ratio:*

   Let, Total Profit = 1; Boman's Share = $\frac{1}{2}$

   Remaining Profit = $1-\frac{1}{2}=\frac{1}{2}$, which will be shared by Antony and Bose in their old profit-sharing, *i.e.*, 2 : 3. Thus,

   Antony's New Share = $\frac{2}{5}\times\frac{1}{2}=\frac{2}{10}$; Bose's New Share = $\frac{3}{5}\times\frac{1}{2}=\frac{3}{10}$; Boman's Share = $\frac{1}{2}$ or $\frac{5}{10}$

   Hence, New Profit-sharing Ratio of Antony, Bose and Boman = $\frac{2}{10}:\frac{3}{10}:\frac{5}{10}=2:3:5$.
3. *Total Capital of the New firm and New Capitals of Partners:*

   Total Capital of New firm on the basis of Boman's Capital = ₹ 5,00,000 × $\frac{2}{1}$ = ₹ 10,00,000

   Antony's Capital = ₹ 10,00,000 × $\frac{2}{10}$ = ₹ 2,00,000; Bose's Capital = ₹ 10,00,000 × $\frac{3}{10}$ = ₹ 3,00,000;

   Boman's Capital = ₹ 5,00,000.
4. **'All Debtors are Good'** means *Provision for Doubtful Debts* is no longer required and hence should be credited to Revaluation Account.

3. (*a*)

JOURNAL OF TARA INDUSTRIES LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Own Debentures A/c ((500 × ₹ 95) + (100 × ₹ 98) + ₹ 400)	...Dr.		57,700	
	To Bank A/c				57,700
	(Being the purchase of own 600 debentures)				
	9% Debentures A/c (600 × ₹ 100)	...Dr.		60,000	
	Premium on Redemption of Debentures A/c (600 × ₹ 5)	...Dr.		3,000	
	To Own Debentures A/c				57,700
	To Gain (Profit) on Cancellation of Own Debentures A/c				5,300
	(Being the cancellation of 600; 9% Debentures of ₹ 100 each redeemable at 105%) (Note)				
	Gain (Profit) on Cancellation of Own Debentures A/c	...Dr.		5,300	
	To Capital Reserve A/c				5,300
	(Being the gain (profit) on cancellation of own debentures transferred to Capital Reserve)				

Note: When the debentures are redeemable at premium, gain or loss on cancellation of own debentures should be calculated after taking into consideration the premium payable on redemption of debentures. In such a case Premium on Redemption of Debentures Account will be debited along with 9% Debentures Account.

(*b*) (*i*) JOURNAL OF EXPORT LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Share Capital A/c (600 × ₹ 7)	...Dr.		4,200	
	To Calls-in-Arrears A/c (600 × ₹ 2)				1,200
	To Forfeited Shares A/c (600 × ₹ 5)				3,000
	(Being 600 shares forfeited for non-payment of first call money of ₹ 2 each)				
	Bank A/c A/c (450 × ₹ 8)	...Dr.		3,600	
	To Share Capital A/c (450 × ₹ 7)				3,150
	To Securities Premium Reserve A/c (450 × ₹ 1)				450
	(Being 450 shares reissued as ₹ 7 paid-up for ₹ 8 per share)				
	Forfeited Shares A/c	...Dr.		2,250	
	To Capital Reserve A/c (450 × ₹ 5)				2,250
	(Being the transfer of gain on reissue of 450 shares)				

(*ii*) JOURNAL OF SWAN LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Share Capital A/c (300 × ₹ 8)	...Dr.		2,400	
	Securities Premium Reserve (300 × ₹ 2)	...Dr.		600	
	To Calls-in-Arrears A/c (300 × ₹ 5)				1,500
	To Forfeited Shares A/c (300 × ₹ 5)				1,500
	(Being 300 shares forfeited for non-payment of allotment money)				
	Bank A/c (210 × ₹ 10)	...Dr.		2,100	
	To Share Capital A/c (210 × ₹ 8)				1,680
	To Securities Premium Reserve (210 × ₹ 2)				420
	(Being 210 shares reissued as ₹ 8 called-up for ₹ 10 per share)				
	Forfeited Shares A/c	...Dr.		1,050	
	To Capital Reserve A/c				1,050
	(Being the gain on reissue of 210 forfeited shares transferred to Capital Reserve)				

4. (*a*) *Calculation of Net Effect of Accumulated Profits, Losses and Reserve:*

	₹
General Reserve	1,40,000
Profit and Los A/c (Cr.)	60,000
Workmen Compensation Reserve (Adjusted)	10,000
Investment Fluctuation Reserve (Adjusted)	5,000
	2,15,000
Less: Advertisement Suspense A/c (Dr.)	50,000
	1,65,000

Calculation of Sacrifice/(Gain) of Each Partner:

	Priya	Riya	Siya	Miya
(*i*) Their Old Share	6/10	3/10	1/10	...
(*ii*) Their New Share	3/10	3/10	3/10	1/10
(*iii*) Difference (*i* – *ii*)	3/10	...	(2/10)	(1/10)
	Sacrifice		Gain	Gain

ADJUSTMENT JOURNAL ENTRY

Date	Particulars		L.F.	Dr. ₹	Cr. ₹
	Siya's Capital A/c (₹ 1,65,000 × ₹ 2/10)	...Dr.		33,000	
	Miya's Capital A/c (₹ 1,65,000 × ₹ 1/10)	...Dr.		16,500	
	To Priya's Capital A/c (₹ 1,65,000 × ₹ 3/10)				49,500
	(Being the adjustment made for net accumulated profits , losses and reserves)				

(*b*) JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019					
March 31	General Reserve A/c	...Dr.		30,000	
	To Rose's Capital A/c				15,000
	To Daisy's Capital A/c				9,000
	To Lily's Capital A/c				6,000
	(Being the General Reserve distributed among partners)				
	Rose's Capital A/c	...Dr.		12,500	
	Daisy's Capital A/c	...Dr.		7,500	
	Lily's Capital A/c	...Dr.		5,000	
	To Profit and Loss A/c				25,000
	(Being the accumulated losses divided among partners)				
	Bad Debts A/c	...Dr.		2,000	
	To Debtors A/c				2,000
	(Being the debtors of ₹ 2,000 written off)				
	Provision for Doubtful Debts A/c	...Dr.		2,000	
	To Bad Debts A/c				2,000
	(Being the bad debts met from provision for bad and doubtful debts)				
	Provision for Doubtful Debts A/c	...Dr.		850	
	To Revaluation A/c (WN 1)				850
	(Being the excess provision for bad and doubtful debts transferred to Revaluation Account)				
	Revaluation A/c	...Dr.		45,000	
	To Patents A/c				30,000
	To Stock A/c				2,500
	To Machinery A/c				7,500
	To Building A/c				5,000
	(Being the decrease in value of assets recorded)				
	Revaluation A/c	...Dr.		10,000	
	To Creditors A/c				10,000
	(Being the unrecorded creditors recorded)				

Rose's Capital A/c ...Dr.		27,075	
Daisy's Capital A/c ...Dr.		16,245	
Lily's Capital A/c ...Dr.		10,830	
To Revaluation A/c (WN 2)			54,150
(Being the loss on revaluation transferred to Partners' Capital Accounts in their old ratio)			
Daisy's Capital A/c (₹ 1,50,000 × 1/5) ...Dr.		30,000	
Lily's Capital A/c (₹ 1,50,000 × 4/5) ...Dr.		1,20,000	
To Rose's Capital A/c (WN 3)			1,50,000
(Being the Rose's share of goodwill adjusted)			
Rose's Capital A/c ...Dr.		2,75,425	
To Rose's Loan A/c (WN 4)			2,75,425
(Being the net amount due to Rose transferred to her Loan Account)			

Working Notes:

1. *Dr.* PROVISION FOR DOUBTFUL DEBTS ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Bad Debts A/c	2,000	By Balance *b/d*	5,000
To Revaluation A/c (Balancing Figure)	850		
To Balance *c/d* (Required) [5% (₹ 45,000 – ₹ 2,000)]	2,150		
	5,000		5,000

2. *Dr.* REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Patents A/c	30,000	By Provision for Doubtful Debts A/c (WN 1)		850
To Stock A/c	2,500	By Loss on Revaluation transferred to:		
To Machinery A/c	7,500	Rose's Capital A/c	27,075	
To Building A/c	5,000	Daisy's Capital A/c	16,245	
To Creditor's A/c	10,000	Lily's Capital A/c	10,830	54,150
	55,000			55,000

3. *Adjustment of Goodwill:*

Daisy's Gaining Share = 2/5 (New Share) –3/10 (Old Share) = 1/10; Lily's Gain = 3/5 – 2/10 = 4/10. Gaining Ratio = 1 : 4; Rose's Share of Goodwill = ₹ 3,00,000 × 5/10 = ₹ 1,50,000, which is contributed by Daisy and Lily in their gaining ratio, *i.e.*, 1 : 4.

4. *Dr.* ROSE'S CAPITAL ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Profit and Loss A/c	12,500	By Balance *b/d*	1,50,000
To Revaluation A/c (Loss)	27,075	By General Reserve A/c	15,000
To Rose's Loan A/c (Balancing Figure)	2,75,425	By Daisy's Capital A/c	30,000
		By Lily's Capital A/c	1,20,000
	3,15,000		3,15,000

5. (*a*) ADJUSTMENT JOURNAL ENTRY

Date	Particulars		L.F.	Dr. ₹	Cr. ₹
	Strong's Capital A/c	...Dr.		8,000	
	To Feeble's Capital A/c				8,000
	(Being the error rectified)				

Working Notes:

1. STATEMENT SHOWING REQUIRED ADJUSTMENT

Particulars	Strong's Capital A/c		Weak's Capital A/c		Feeble's Capital A/c		Firm	
	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)
Salary Payable to Strong & Weak	...	6,000	...	6,000	...	...	12,000	...
Commission Payable to Feeble	...	...	...	...	...	8,000	8,000	...
Share of Profit in ₹ 1,20,000 (*i.e.*, ₹ 1,40,000 – ₹ 12,000 – ₹ 8,000) (WN 2)	...	42,000	...	50,000	...	28,000	1,20,000	...
Profit of ₹ 1,40,000 already distributed in 2 : 2 : 1, now taken back	56,000	...	56,000	...	28,000	...	...	1,40,000
	56,000	48,000	56,000	56,000	28,000	36,000	1,40,000	1,40,000
Net Effect	8,000 Dr.		...		8,000 Cr.		...	

2. DISTRIBUTION OF PROFITS

Particulars	Strong	Weak	Feeble
Profit of ₹ 1,20,000 [*i.e.*, ₹ 1,40,000 – ₹ 12,000 (Salary of Strong and Weak) – ₹ 8,000 (Commission of Feeble)] will be divided between Strong, Weak and Feeble in the ratio of 3 : 3 : 2	₹ 1,20,000 × 3/8 = ₹ 45,000	₹ 1,20,000 × 3/8 = ₹ 45,000	₹ 1,20,000 × 2/8 = ₹ 30,000

However, Weak's minimum guaranteed profit is ₹ 50,000. So, there is a deficiency of ₹ 5,000.

Deficiency to be borne by Strong and Feeble in 3 : 2	₹ 5,000 × 3/5 = ₹ 3,000	...	₹ 5,000 × 2/5 = ₹ 2,000
Adjusted Share of Profit	₹ 45,000 – ₹ 3,000 = ₹ 42,000	₹ 45,000 + ₹ 3,000 + ₹ 2,000 = ₹ 50,000	₹ 30,000 – ₹ 2,000 = ₹ 28,000

(*b*) (*i*) *Goodwill at 3 years' Purchase of Average Profit:*

$$\text{Average Profit} = \frac{₹\ 1,90,000 + ₹\ 2,20,000 + ₹\ 2,50,000}{3} = ₹\ 2,20,000$$

Average Profit for Goodwill = ₹ 2,20,000 – Remuneration of Partners
= ₹ 2,20,000 – ₹ 1,00,000 = ₹ 1,20,000

Goodwill = Average Profit × Number of Years' Purchase
= ₹ 1,20,000 × 3 = ₹ 3,60,000.

(*ii*) *Goodwill at 2 Years' Purchase of Super Profit:*

$$\text{Normal Profit} = \text{Capital Employed} \times \text{Normal Rate of Return}/100$$

$$= ₹\ 4,00,000 \times \frac{15}{100} = ₹\ 60,000$$

$$\text{Super Profit} = \text{Average Profit} - \text{Normal Profit}$$

$$= ₹\ 1,20,000 - ₹\ 60,000 = ₹\ 60,000$$

$$\text{Goodwill} = \text{Super Profit} \times \text{Number of Years' Purchase}$$

$$= ₹\ 60,000 \times 2 = ₹\ 1,20,000.$$

(*iii*) *Goodwill under Capitalisation of Super Profit:*

$$\text{Goodwill} = \text{Super Profit} \times \frac{100}{\text{Normal Rate of Return}}$$

$$= ₹\ 60,000 \times \frac{100}{15} = ₹\ 4,00,000.$$

6.

Dr. REALISATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Debtors A/c	1,70,000	By Sundry Creditors A/c		80,000
To Stock A/c	1,50,000	By Ram's Brother's Loan A/c		80,000
To Investments A/c	2,50,000	By Provision for Doubtful Debts A/c		20,000
To Building A/c	2,50,000	By Investment Fluctuation Fund A/c		50,000
To Goodwill A/c	1,00,000	By Bank A/c (Assets Realised)		
To Ram's Capital A/c (Ram's Brother's Loan)	80,000	Debtors (₹ 1,70,000 – ₹ 50,000)	1,20,000	
To Bank A/c:		Investments (80% of 2,50,000)	2,00,000	
Creditors (₹ 80,000 – ₹ 20,000)	60,000	Goodwill (60% of 1,00,000)	60,000	
To Bank A/c (Realisation Expenses)	20,000	Building (₹ 3,00,000 – ₹ 10,000)	2,90,000	
		Stock (WN 2)	50,000	7,20,000
		By Rahim's Capital A/c (WN 1)		40,000
		By Loss transferred to:		
		Ram's Capital A/c	72,000	
		Rahim's Capital A/c	18,000	90,000
	10,80,000			10,80,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Ram (₹)	Rahim (₹)	Particulars	Ram (₹)	Rahim (₹)
To Profit and Loss A/c	80,000	20,000	By Balance *b/d*	5,00,000	4,00,000
To Realisation A/c (Stock)	...	40,000	By Realisation A/c (Brother's Loan)	80,000	...
To Realisation A/c (Loss)	72,000	18,000			
To Bank A/c (Final Payment)	4,28,000	3,22,000			
	5,80,000	4,00,000		5,80,000	4,00,000

Dr. RAHIM'S LOAN ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Bank A/c	30,000	By Balance *b/d*	30,000
	30,000		30,000

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	2,00,000	By Bank Overdraft	60,000
To Realisation A/c (Assets Realised)	7,20,000	By Realisation A/c (Creditors)	60,000
		By Realisation A/c (Expenses)	20,000
		By Rahim's Loan A/c	30,000
		By Ram's Capital A/c (Final Payment)	4,28,000
		By Rahim's Capital A/c (Final Payment)	3,22,000
	9,20,000		9,20,000

Working Notes:

1. *Calculation of book value of stock taken by Rahim:*
   Let book value of stock taken over by Rahim = ₹ 100; Rahim takes it at 20% *less* than the book value, *i.e.*, ₹ 100 – ₹ 20 = ₹ 80
   Book Value of Stock taken by Rahim = ₹ 40,000 × ₹ 100/₹ 80 = ₹ 50,000.
2. Out of Total Stock of ₹ 1,50,000; Stock of ₹ 50,000 is taken by Rahim. Firm sold the remaining stock of ₹ 1,00,000 at 50% of its book value, *i.e.*, at ₹ 50,000.

7. (*a*) JOURNAL OF NOVA LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2018				
Mar. 31	Surplus, *i.e.*, Balance in Statement of Profit and Loss A/c ...Dr.		2,50,000	
	To Debentures Redemption Reserve A/c			2,50,000
	(Being the profit transferred to DRR equivalent to 25% of the value of Debentures outstanding)			
April 1	Debentures Redemption Investment A/c ...Dr.		1,50,000	
	To Bank A/c			1,50,000
	(Being the amount invested in specified securities equal to 15% of the amount of redeemable debentures)			
Sept. 30	Bank A/c ...Dr.		1,56,000	
	To Debentures Redemption Investment A/c			1,50,000
	To Interest Earned A/c			6,000
	(Being the debentures redemption investment realised and interest received)			
Oct. 1	9% Debentures A/c ...Dr.		10,00,000	
	To Debentureholders' A/c			10,00,000
	(Being the amount due on redemption)			
	Debentureholders' A/c ...Dr.		10,00,000	
	To Bank A/c			10,00,000
	(Being payment made to debentureholders)			
	Debentures Redemption Reserve A/c ...Dr.		2,50,000	
	To General Reserve A/c			2,50,000
	(Being the amount in DRR A/c transferred to General Reserve)			

Note: As per Section 71(4) of the Companies Act, 2013 and Rule 18(7)(*b*) of the Companies (Share Capital and Debentures) Rules, 2014, an amount at least equal to 25% of the Nominal Value of Debentures Outstanding is credited to Debentures Redemption Reserve Account and as per Rule 18(7)(*c*) of the Companies (Share Capital and Debentures), Rules, 2014 investment is made in specified securities of an amount equal to at least 15% of the nominal value of debentures to be redeemed.

(*b*) JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
(*i*)	Bank A/c	...Dr.		4,32,000	
	To Debentures Application and Allotment A/c				4,32,000
	(Being the application money received)				
	Debentures Application and Allotment A/c	...Dr.		4,32,000	
	Loss on Issue of Debentures A/c	...Dr.		40,000	
	To 9% Debentures A/c				4,00,000
	To Securities Premium Reserve A/c				32,000
	To Premium on Redemption of Debentures A/c				40,000
	(Being the issue of 4,000 debentures at a premium of 8% redeemable at 10% premium)				
(*ii*)	Bank A/c	...Dr.		6,00,000	
	To Debentures Application and Allotment A/c				6,00,000
	(Being the application money received for 6,000 debentures)				
	Debentures Application and Allotment A/c	...Dr.		6,00,000	
	Loss on Issue of Debentures A/c	...Dr.		60,000	
	To 9% Debentures A/c				6,00,000
	To Premium on Redemption of Debentures A/c				60,000
	(Being the issue of 6,000 debentures at par repayable at a premium of 10%)				
(*iii*)	Bank A/c	...Dr.		10,50,000	
	To Debentures Application and Allotment A/c				10,50,000
	(Being the application money received for 10,000 debentures)				
	Debentures Application and Allotment A/c	...Dr.		10,50,000	
	To 9% Debentures A/c				10,00,000
	To Securities Premium Reserve A/c				50,000
	(Being the issue of 10,000; 9% Debentures at a premium of 5% redeemable at par)				

8. (*a*) BALANCE SHEET OF SAJAL LTD.

as at ...

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
Share Capital	1	27,60,000

Note to Accounts

Particulars		₹
1. Share Capital		
Authorised Capital		
... Equity Shares of ₹ 100 each		...
Issued Capital		
32,000 Equity Shares of ₹ 100 each		32,00,000
Subscribed Capital		
Subscribed and fully paid-up		
26,000 Equity Shares of ₹ 100 each	26,00,000	
Add: Forfeited Shares A/c (4,000 × ₹ 40)	1,60,000	27,60,000

(*b*) **Imara Ltd.**

BALANCE SHEET *as at 31st March, 2019* (*₹ in "000*)

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital		780
(*b*) Reserves and Surplus		200
2. Share Application Money Pending Allotment		20
3. Non-Current Liabilities		
(*a*) Long-term Borrowings		600
(*b*) Long-term Provisions		200
4. Current Liabilities		
(*a*) Short-term Borrowings		180
(*b*) Trade Payables		40
(*c*) Other Current Liabilities	1	20
Total		2,040
II. ASSETS		
1. Non-Current Assets		
(*a*) Fixed Assets:		
Tangible		1,200
(*b*) Non-current Investments		400
2. Current Assets		
(*a*) Current Investments		100
(*b*) Inventories		40
(*c*) Trade Receivables		160
(*d*) Cash and Cash Equivalents		120
(*e*) Other Current Assets	2	20
Total		2,040

Notes to Accounts (*₹ in "000*)

Particulars	₹
1. Others Current Liabilities	
Oustanding Expenses	20
2. Other Current Assets	
Prepaid Expenses	20

Note: Dividend Proposed for the Year 2018–19 is ₹ 20,000.

Section B

9. (*a*) 'Provision for Doubtful Debts' is not deducted from the Trade Receivables as the purpose is to calculate the number of days for which sales are tied up in debtors and not to ascertain the realisable value of trade receivables. If the 'Provision for Doubtful Debts' is deducted, it would give an impression that a portion of Trade Receivables (to the extent of provision) has already been collected.

(*b*)

Change	*Reason*
(*i*) No Change	Both purchases and closing inventory will increase by the same amount hence, Cost of Revenue from Operations will remain unchanged.
(*ii*) No Change	Revenue from Operations will increase but closing inventory will decrease by the same percentage (not by same amount). As a result, Cost of Revenue from Operations will increase by the same percentage as the Revenue from Operations increase.

(*c*)

(*i*) Operating Ratio $= \dfrac{\text{Cost of Revenue from Operations} + \text{Operating Expenses}}{\text{Revenue from Operations}} \times 100$

$$= \frac{₹\ 13{,}20{,}000 + ₹\ 2{,}20{,}000}{₹\ 22{,}00{,}000} \times 100 = 70\%.$$

Notes: Revenue from Operations = Cash Revenue from Operations + Credit Revenue from Operations

= ₹ 10,00,000 + ₹ 12,00,000 = ₹ 22,00,000

Gross Profit = 40% of ₹ 22,00,000 = ₹ 8,80,000

Cost of Revenue from Operations = Revenue from Operations – Gross Profit

= ₹ 22,00,000 – ₹ 8,80,000 = ₹ 13,20,000

Operating Expenses = 10% of ₹ 22,00,000 = ₹ 2,20,000.

(*ii*) Inventory Turnover Ratio $= \dfrac{\text{Cost of Revenue from Operations}}{\text{Average Inventory}}$

Inventory Turnover Ratio $= \dfrac{₹\ 13{,}20{,}000}{\dfrac{₹\,1{,}50{,}000\ (\text{Opening}) + ₹\,1{,}70{,}000\ (\text{Closing})}{2}}$

= 8.25 Times.

(*iii*) Proprietary Ratio $= \dfrac{\text{Shareholders' Funds}}{\text{Total Assets}} \times 100$

$$= \frac{₹\ 6{,}00{,}000\ (\text{Share Capital})}{₹\ 8{,}00{,}000} \times 100 = 75\%.$$

Note: Total Assets = Current Assets + Non-Current Assets (Fixed Assets)

= ₹ 3,00,000 + ₹ 5,00,000 = ₹ 8,00,000.

10. CASH FLOW STATEMENT as Per AS–3
for the year ended 31st March, 2019

Particulars		₹	₹
I. Cash Flow from Operating Activities			
Net Profit before Tax (WN 1)		6,00,000	
Adjustment for Non-Cash and Non-Operating Items:			
Add: Depreciation on Machinery		7,00,000	
Interest on Debentures (10% of ₹ 10,00,000)		1,00,000	
Amortisation of Intangible Assets (Patents)		40,000	
		14,40,000	
Less: Profit on Sale of Non-current Investment	10,000		
Profit on Sale of Machinery	60,000	70,000	
Operating Profit before Working Capital Changes		13,70,000	
Add: Decrease in Current Assets and Increase in Current Liabilities:			
Inventories	2,00,000		
Trade Receivables	2,00,000		
Trade Payables	9,50,000	13,50,000	27,20,000
Less: Decrease in Current Liabilities:			
Outstanding Expenses			30,000
Cash Flow from Operating Activities			26,90,000
II. Cash Flow from Investing Activities			
Purchase of Machinery (WN 2)		(18,80,000)	
Sale of Machinery (WN 2)		2,40,000	
Sale of Non-current Investments (WN 3)		60,000	
Purchase of Non-current Investment (WN 3)		(1,00,000)	
Cash Used in Investing Activities			(16,80,000)
III. Cash Flow from Financing Activities			
Interest on Debentures Paid		(1,00,000)	
Dividend Paid (₹ 2,00,000 – ₹ 60,000)		(1,40,000)	
Cash Used in Financing Activities			(2,40,000)
IV. Net Increase in Cash and Bank Balances (I + II + III)			7,70,000
V. *Add:* Opening Cash and Bank Balances			1,80,000
VI. Closing Cash and Bank Balances (IV + V)			9,50,000

Working Notes:

1. *Calculation of Net Profit before Tax:*

	₹
Surplus, *i.e.*, Balance in Statement of Profit and Loss (Closing)	9,00,000
Less: Surplus, *i.e.*, Balance in Statement of Profit and Loss (Opening)	5,00,000
	4,00,000
Add: Interim Dividend Paid	2,00,000
Net Profit before Tax	6,00,000

2. *Dr.* MACHINERY ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	20,00,000	By Bank A/c (Sale)*	2,40,000
To Statement of Profit and Loss (Gain on Sale)	60,000	(₹ 4,00,000 – ₹ 2,20,000 + ₹ 60,000)	
To Bank A/c (Purchase)	18,80,000	By Depreciation A/c	7,00,000
(Balancing Figure)		By Balance *c/d*	30,00,000
	39,40,000		39,40,000

**Calculation of Sale Value*

	₹
Book value on the date of sale	1,80,000
Add: Gain (Profit) on Sale	60,000
Sale Value	2,40,000

3. *Dr.* NON-CURRENT INVESTMENTS ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,50,000	By Bank A/c (Sale)	60,000
To Statement of Profit and Loss (Gain on Sale)	10,000	By Balance *c/d*	2,00,000
To Bank A/c (Purchase)	1,00,000		
(Balancing Figure)			
	2,60,000		2,60,000

11. (*a*) Objectives of Common-size Income Statement:

(*i*) To analyse change in individual items of Income Statement.

(*ii*) To determine the trend in different items of Revenue and Expenses.

(*b*) Cash Equivalents are short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of change in value.

(*c*) (*i*) Proceeds from sale of Fixed Assets.

(*ii*) Proceeds from sale of Non-current Investment.

(*d*)

COMMON-SIZE STATEMENT OF PROFIT AND LOSS

for the years ended 31st March, 2019 and 2018

Particulars	Absolute Amounts		% of Revenue from Operations	
	31st March, 2019 (₹)	31st March, 2018 (₹)	31st March, 2019 (%)	31st March, 2018 (%)
I. Revenue from Operations	15,00,000	10,00,000	100	100
II. Other Income	1,80,000	2,00,000	12	20
III. Total Revenue	16,80,000	12,00,000	112	120
IV. Expenses:				
Cost of Materials Consumed	9,00,000	5,00,000	60	50
Other Expenses	1,50,000	1,00,000	10	10
Total Expenses	10,50,000	6,00,000	70	60
V. Profit before Tax (III – IV)	6,30,000	6,00,000	42	60
VI. Tax Expense	1,89,000	1,80,000	12.6	18
VII. Profit after Tax (V – VI)	4,41,000	4,20,000	29.4	42

Model Test Paper 2

Time Allowed: 3 Hrs. **Max. Marks: 80**

General Instructions: As per Model Test Paper 1

Section A

Part I (12 Marks)

(*Answer **all** questions*)

1. Answer each of the following questions briefly:

(*i*) Why is Revaluation Account prepared? State **any two** reasons.

(*ii*) What is meant by a *pro rata* allotment? When does the need for a *pro rata* allotment arise?

(*iii*) State **two** differences between Realisation Account and Revaluation Account.

(*iv*) What is meant by Redemption of Debentures? Enumerate **any two** methods of Redemption of Debentures.

(*v*) Why the Capital Account of a partner, when Capital Accounts are maintained following Fixed Capital Accounts Method, does not show a 'Debit balance' in spite of regular and consistent losses year after year?

(*vi*) What is meant by Calls-in-Advance? How is 'Calls-in-Advance' shown in the Balance Sheet? [6 × 2 = 12]

Part II (48 Marks)

(*Answer **any four** questions*)

2. (*a*) The capitals of Raghubir, Balbir and Krantibir as on 31st March, 2019 were ₹ 60,000; ₹ 2,20,000 and ₹ 4,40,000 respectively. Profit of ₹ 1,20,000 for the year ended 31st March, 2019 was distributed in the ratio of 4 : 1 : 1 after allowing interest on capital @ 10% p.a. During the year each partner withdrew ₹ 2,40,000. The Partnership Deed was silent as to profit-sharing ratio but provided for interest on capital @ 12%.

Pass the necessary adjusting Journal entry.

(*b*) Vrindan and Kundan are partners sharing profits and losses in the ratio of 2 : 1. On 1st April, 2018, they admit Srijan for 1/4th share in profits and guaranteed profit of ₹ 50,000. The profit for the year 2018–19 was ₹ 1,52,000. Pass the Journal entry in the books of the firm for distribution of profit and prepare Profit and Loss Appropriation Account. [6 + 6 = 12]

3. The Balance Sheet of Madan and Mohan who share profits and losses in the ratio of 3 : 2, as at 31st March, 2019 was as follows:

BALANCE SHEET OF MADAN AND MOHAN
as at 31st March, 2019

Liabilities	₹	Assets		₹
Creditors	28,000	Cash at Bank		10,000
Workmen Compensation Reserve	12,000	Debtors	65,000	
General Reserve	50,000	*Less:* Provision for Doubtful Debts	5,000	60,000
Capital A/cs:		Stock		30,000
Madan	60,000	Investments		50,000
Mohan	40,000	Patents		10,000
		Goodwill		30,000
	1,90,000			1,90,000

They admit Gopal on 1st April, 2019 for 1/5th share on the following terms:

(*a*) Gopal shall bring ₹ 25,000 by cheque as his share of premium for goodwill.

(*b*) Unaccounted accrued commission of ₹ 500 will be accounted.

(*c*) Market value of investments was ₹ 45,000.

(*d*) A debtor whose dues of ₹ 6,000 were written off as bad debts paid ₹ 5,800 in full settlement.

(*e*) A claim of ₹ 2,000 for workmen's compensation to be provided.

(*f*) Patents are undervalued by ₹ 5,000.

(*g*) Out of the amount of insurance which was debited to Profit and Loss Account, ₹ 5,000 to be carried forward as unexpired insurance.

(*h*) Gopal to bring in capital equal to 1/5th of the total capital of the new firm.

Prepare Revaluation Account, Capital Accounts of the Partners and the Balance Sheet of the new firm. [12]

4. Bayson Ltd. invited applications for 54,000 shares of ₹ 100 each payable as follows:

₹ 50 per share on application;

₹ 10 per share on allotment; and

Balance on first and final call.

Applications were received for 80,000 shares.

Full allotment was made to the applicants of 14,000 shares. The remaining applicants were allotted 40,000 shares on *pro rata* basis. Excess money received with application was adjusted towards sums due on allotment and call.

Vibhor, holding 1,200 shares, who belonged to the category of applicants to whom full allotment was made, paid the call money at the time of allotment. Vidur, who belonged to the category of applicants to whom shares were allotted on *pro rata* basis did not pay any amount after application money on his 400 shares. Vidur's shares were forfeited after the first and final call. All the forfeited shares were later on reissued @ ₹ 110 per share as fully paid-up.

Pass the Journal entries in the books of Bayson Ltd. for the above transactions. Also show relevant items as they would appear in the Balance Sheet of the company. [12]

5. (*a*) Mars Ltd. issued 5,000, 9% Debentures of ₹ 100 each at par and also raised a loan of ₹ 8,00,000 from ICICI Ltd. collaterally secured by issuing ₹ 10,00,000, 9% Debentures of ₹ 100 each. How will debentures be shown in the Balance Sheet of the company if the company has recorded the Debentures issued as collateral in the books? Also Journalise the Issue of Debentures.

(*b*) Europa Ltd. issued 2,000, 10% Debentures of ₹ 100 each credited as fully paid to the promoters for their services and issued 1,000, 10% Debentures of ₹ 100 each credited as fully paid to the underwriters for their underwriting services. Journalise these transactions.

(*c*) Show by means of Journal entries how will be the following recorded:

(*i*) Milton Ltd. issued 1,000, 10% Debentures of ₹ 100 each at a discount of 10%, redeemable at the end of 5 years at a premium of 5%.

(*ii*) Dubblin Ltd. issued 2,000, 9% Debentures of ₹ 100 each at a premium ₹ 20 per debenture, redeemable at the end of 5 years at a premium of ₹ 10 per debenture. [5 + 3 + 4 = 12]

6. (*a*) On 1st April, 2018, Moon Ltd. had 1,000; 10% Debentures of ₹ 100 each. On 1st October, 2018, the company purchased 300 Own Debentures @ ₹ 93 for immediate cancellation. Interest on debentures is payable half yearly on 30th September and 31st March.

Pass Journal entries on 1st October and 31st March.

(*b*) Under which major heading and sub-heading will the following items be shown in the Balance Sheet of a company as per Schedule III of the Companies Act, 2013:

(*i*) Long-term Borrowings; (*ii*) Trade Payables;
(*iii*) Provision for Tax; (*iv*) Patents;
(*v*) Accrued Income; (*vi*) Calls-in-Advance? [6 + 6 = 12]

7. The Balance Sheet of Amal, Bimal and Kamal, who are sharing profits in proportion of their capitals stood as follows on 31st March, 2019:

BALANCE SHEET OF AMAL, BIMAL AND KAMAL
as at 31st March, 2019

Liabilities		₹	Assets		₹
Capital A/cs:			Goodwill		21,000
Amal	2,00,000		Land and Building		2,00,000
Bimal	3,00,000		Machinery		3,00,000
Kamal	2,00,000	7,00,000	Closing Stock		1,00,000
General Reserve		70,000	Sundry Debtors	1,10,000	
Workmen Compensation Reserve		15,000	*Less:* Provision for Doubtful Debts	10,000	1,00,000
Sundry Creditors		50,000	Cash at Bank		1,00,000
			Advertisement Expenditure		14,000
		8,35,000			8,35,000

On 1st April, 2019, Amal retired from the firm and the remaining partners decided to carry on the business. It was agreed to revalue the assets and reassess the liabilities as follows:

(*i*) Land and Building to be appreciated by 30%.

(*ii*) Machinery be reduced by 20%.

(*iii*) There were bad debts of ₹ 17,000.

(*iv*) The claim on account of workmen compensation was ₹ 8,000.

(*v*) Goodwill of the firm was valued at ₹ 1,40,000 and Amal's share of goodwill be adjusted against the Capital Accounts of the continuing partners Bimal and Kamal who have decided to share future profits in the ratio of 4 : 3.

(*vi*) Capital of the new firm will be the same as it was before the retirement of Amal and will be in the new profit-sharing ratio of the continuing partners.

(*vii*) Amount due to Amal be settled by paying ₹ 50,000 in cash and the balance by transferring to his Loan Account to be paid later.

Prepare Revaluation Account, Capital Accounts of partners and Balance Sheet of the firm after Amal's retirement. [12]

8. Following is the Balance Sheet of Ram, Mohan and Sohan as at 31st March, 2019, who share profits and losses in the ratio of 3 : 1 : 1:

Liabilities		₹	Assets		₹
Sundry Creditors		60,000	Cash at Bank		32,000
Loan from Mrs. Mohan		15,000	Debtors	2,42,000	
General Reserve		1,00,000	*Less:* Provision for Doubtful Debts	12,000	2,30,000
Capital A/cs:			Stock		78,000
Ram	2,45,000		Investments		1,70,000
Mohan	90,000		Fixed Assets		10,000
Sohan	60,000	3,95,000	Advertisement Suspense A/c		50,000
		5,70,000			5,70,000

The firm was dissolved on the above date on the following terms:

(*a*) Goodwill is to be ignored.

(*b*) 'Ram' is to take all the fixed assets at ₹ 2,000 less, Debtors amounting to ₹ 2,00,000 at ₹ 1,72,000. The creditors of ₹ 60,000 to be assumed by 'Ram' at that value.

(*c*) 'Mohan' is to take entire stock at ₹ 70,000 and certain investments at ₹ 72,000 (being book value *less* 10%).

(*d*) 'Sohan' is to take remaining investments at 90% of the book value *less* ₹ 1,000 allowances and to assume responsibility for the discharge of Mrs. Mohan's loan, together with accrued interest of ₹ 300 which has not been recorded in the books of the firm.

(*e*) The remaining debtors were sold to a debt collecting agency for 50% of book values.

(*f*) Ram was to get ₹ 2,700 as remuneration for completing the dissolution work and was to bear the realisation expenses. The expenses of realisation ₹ 1,700 were paid by Ram out of his private funds.

Prepare Realisation Account, Bank Account and Partners' Capital Accounts. [12]

Section B

(20 Marks)

(*Answer* ***any two*** *questions*)

9. (*a*) From the following information, calculate Cash Flow from Investing Activities:

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
Investment in shares of Star Ltd.	1,50,000	1,50,000
Machinery	4,00,000	3,00,000
Patents	50,000	80,000
Goodwilll	45,000	60,000
10% Investments	2,00,000	1,50,000
Building	25,00,000	25,00,000

Additional Information:

(*i*) A part of Building was let out for commercial purpose and the rent received was ₹ 30,000.

(*ii*) Dividend received from Star Ltd. @ 10%.

(*iii*) Patents of ₹ 10,000 were written off. A part of patents was sold at a loss of ₹ 5,000.

(*iv*) During the year, 10% investments were purchased for ₹ 1,00,000 and some investments were sold at a profit of ₹ 10,000. Interest on investments of ₹ 12,000 for the year was duly received.

(*b*) From the following extract of Balance Sheet of Orpat Ltd., calculate Cash Flow from Financing Activities:

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
Equity Share Capital	6,00,000	4,00,000
10% Preference Share Capital	2,00,000	3,00,000
Securities Premium Reserve	15,000	...
10% Debentures	5,00,000	4,00,000

Additional Information:

(*i*) Equity Shares were issued at a premium of 10% on 31st March, 2019.

(*ii*) Preference Shares were redeemed on 31st March, 2019, at a premium of 5%. The company met premium on redemption from Securities Premium Reserve.

(*iii*) Additional Debentures were issued on 1st April, 2018.

(*iv*) The company declared and paid equity dividend @ 9% and also paid preference dividend for the year 2017–18. [5 + 5 = 10]

10. (*a*) Calculate following ratios from the given information:

(*i*) Liquid Ratio;

(*ii*) Proprietary Ratio; and

(*iii*) Working Capital Turnover Ratio.

	₹
Revenue from Operations	5,00,000
Total Current Assets	3,00,000
Prepaid Insurance	5,000
Share Capital	4,00,000
Non-Current Assets	6,00,000
Gross Profit	1,50,000
Closing Inventory	25,000
Total Current Liabilities	1,50,000
Reserves and Surplus	50,000

(*b*) Calculate Trade Receivables Turnover Ratio from the following:

Closing Trade Receivables ₹ 40,000; Credit Revenue from Operations being 25% of Cash Revenue from Operations; Excess of Closing Trade Receivables over Opening Trade Receivables ₹ 20,000; and Total Revenue from Operations ₹ 1,50,000.

[6 + 4 = 10]

11. (*a*) From the following information, prepare a Comparative Balance Sheet of Fable Ltd:

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
Equity Share Capital	25,00,000	25,00,000
Fixed Assets (Tangible)	36,00,000	30,00,000
Reserves and Surplus	6,00,000	5,00,000
Investment (Non-current)	5,00,000	5,00,000
Long-term Loans	15,00,000	15,00,000
Current Assets	10,50,000	15,00,000
Current Liabilities	5,50,000	5,00,000

(*b*) Sun Ltd. has 8% Debentures of ₹ 5,00,000. Its profit before interest and tax is ₹ 2,00,000. Calculate Interest Coverage Ratio.

(*c*) Give **two** advantages of Comparative Balance Sheet. [6 + 2 + 2 = 10]

Answers

1. (*i*) *Revaluation Account is prepared:*

(*a*) To record the effect of Revaluation of Assets and Reassessment of Liabilities so as to show the Assets and Liabilities at their revised (revalued) values.

(*b*) To ascertain the Gain (Profit)/Loss arising on account of Revaluation of Assets and Reassessment of Liabilities.

(*ii*) *Pro rata* Allotment means allotment of shares to the applicants in the ratio of number of shares offered to the number of shares applied.

For example:

Total No. of Shares offered to Public = 4,000

Total No. of Shares applied by Public = 4,800

No. of Shares applied by James = 96

No. of Shares to be allotted to James = $4{,}000/4{,}800 \times 96$ = 80 shares.

The need for a *pro rata* allotment arises in case of *oversubscription of Shares* (*i.e.*, when the number of shares applied for is more than the number of shares offered for subscription by the company.

(*iii*) **Difference between Realisation Account and Revaluation Account**

Basis	*Realisation Account*	*Revaluation Account*
1. **Meaning**	It records the realisation of assets and settlement of liabilities.	It records the effect of revaluation of assets and reassessment of liabilities.
2. **When Prepared**	It is prepared at the time of dissolution of the firm.	It is prepared at the time of reconstitution of the firm.

(*iv*) Redemption of Debentures means discharging the liability towards debentures by making repayment to the Debentureholders.

Methods of Redemption of Debentures:

1. By payment in lump sum at the time of their maturity.
2. By payment in instalments by draw of lots.
3. By purchase in the Open Market.

(*v*) When Fixed Capital Accounts Method is followed, the amount of loss is debited to Partners' Current Accounts. Therefore, Partner's Capital Account is not affected by the amount of losses and always shows credit balance.

(*vi*) Calls-in-Advance means the amount received from the shareholders which has not yet been called by the company.

The amount of Calls-in-Advance is shown under the head *'Current Liabilities'* and sub-head *'Other Current Liabilities'* in the Balance Sheet.

2. (*a*) JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Raghubir's Capital A/c ...Dr.		44,000	
	To Balbir's Capital A/c			20,000
	To Krantibir's Capital A/c			24,000
	(Being the short interest on capital provided and profits distributed in the wrong ratio, now rectified)			

Working Notes:

1. CALCULATION OF OPENING CAPITAL

Particulars	Raghubir (₹)	Balbir (₹)	Krantibir (₹)
A. Closing Capital	60,000	2,20,000	4,40,000
B. *Add:* Drawings already debited	2,40,000	2,40,000	2,40,000
	3,00,000	4,60,000	6,80,000
C. *Less:* Profit already credited	80,000	20,000	20,000
D. Opening Capital *plus* Interest on Capital	2,20,000	4,40,000	6,60,000
E. *Less:* Interest on Capital (D × 10/110)	20,000	40,000	60,000
F. Opening Capital	2,00,000	4,00,000	6,00,000

2. STATEMENT SHOWING REQUIRED ADJUSTMENT

Particulars	Raghubir's Capital A/c		Balbir's Capital A/c		Krantibir's Capital A/c		Firm	
	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)
I. Amount already credited, now taken back:								
Interest on Capital @ 10%	20,000	...	40,000	...	60,000	...	...	1,20,000
Share of Profit (4 : 1 : 1)	80,000	...	20,000	...	20,000	...	...	1,20,000
II. Amount which should have been credited:								
Interest on Capital @ 12%	...	24,000	...	48,000	...	72,000	1,44,000	...
Share of Profit ₹ 96,000 (*i.e.*, ₹ 2,40,000 – ₹ 1,44,000) in ratio of 1 : 1 : 1	...	32,000	...	32,000	...	32,000	96,000	...
	1,00,000	56,000	60,000	80,000	80,000	1,04,000	2,40,000	2,40,000
III. Net Effect	44,000 (Dr.)		20,000 (Cr.)		24,000 (Cr.)		...	

(*b*) JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2019					
March 31	Profit and Loss Appropriation A/c	...Dr.		1,52,000	
	To Vrindan's Capital A/c				68,000
	To Kundan's Capital A/c				34,000
	To Srijan's Capital A/c				50,000
	(Being the distribution of profit among partners)				

Dr. PROFIT AND LOSS APPROPRIATION ACCOUNT *for the year ending 31st March, 2019* *Cr.*

Particulars		₹	Particulars	₹
To Vrindan's Capital A/c (2/4 × ₹ 1,52,000)	76,000		By Profit and Loss A/c (Net Profit)	1,52,000
Less: Deficiency borne (2/3 × ₹ 12,000)	8,000	68,000		
To Kundan's Capital A/c (1/4 × ₹ 1,52,000)	38,000			
Less: Deficiency borne (1/3 of ₹ 12,000)	4,000	34,000		
To Srijan's Capital A/c	38,000			
Add: Deficiency recovered from:				
Vrindan	8,000			
Kundan	4,000	50,000		
		1,52,000		1,52,000

Working Notes:

1. *Calculation of New Profit-sharing Ratio:*

   Let the total share be = 1, Srijan's Share = 1/4, Remaining Share = 1 – 1/4 = 3/4

   Vrindan's New Share = 3/4 × 2/3 = 2/4; Kundan's New Share = 3/4 × 1/3 = 1/4

   Thus, New Profit-Sharing Ratio of Vrindan, Kundan and Srijan = 2/4 : 1/4 : 1/4 or 2 : 1 : 1.

2. Srijan's actual share of profit = ₹ 1,52,000 × 1/4 = ₹ 38,000.

3. Deficiency = Guaranteed Amount of Profit – Actual Share of Profit

   = ₹ 50,000 – ₹ 38,000 = ₹ 12,000.

4. Deficiency is to be borne by Vrindan and Kundan in the ratio of 2 : 1 as follows:

   Vrindan's contribution = ₹ 12,000 × 2/3 = ₹ 8,000;

   Kundan's contribution = ₹ 12,000 × 1/3 = ₹ 4,000.

3.

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars	₹
To Investment A/c		5,000	By Accrued Income A/c	500
To Gain (Profit) transferred to:			By Bad Debts Recovered A/c (WN 1)	5,800
Madan's Capital A/c	6,780		By Unexpired Insurance A/c	5,000
Mohan's Capital A/c	4,520	11,300	By Patents A/c	5,000
		16,300		16,300

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Madan ₹	Mohan ₹	Gopal ₹	Particulars	Madan ₹	Mohan ₹	Gopal ₹
To Goodwill A/c	18,000	12,000	...	By Balance *b/d*	60,000	40,000	...
To Balance *c/d*	99,780	66,520	41,575	By General Reserve A/c	30,000	20,000	...
				By Revaluation A/c	6,780	4,520	...
				By Workmen Comp. Reserve A/c (WN 2)	6,000	4,000	...
				By Premium for Goodwill A/c	15,000	10,000	...
				By Bank A/c (WN 3)	...	...	41,575
	1,17,780	78,520	41,575		1,17,780	78,520	41,575

BALANCE SHEET OF THE RECONSTITUTED FIRM *as at 1st April, 2019*

Liabilities		₹	Assets		₹
Creditors		28,000	Cash at Bank (WN 4)		82,375
Workmen Compensation Claim		2,000	Debtors	65,000	
Capital Accounts:			*Less:* Provision for Doubtful Debts	5,000	60,000
Madan	99,780		Stock		30,000
Mohan	66,520		Investments		45,000
Gopal	41,575	2,07,875	Patents		15,000
			Accrued Income		500
			Unexpired Insurance		5,000
		2,37,875			2,37,875

Working Notes:

1. Amount recovered in the form of bad debts written off last year is a gain for the firm. Therefore, Revaluation Account is credited with the amount.
2. In the given case, there is a claim of ₹ 2,000 on account of Workmen Compensation. Therefore, Workmen Compensation Reserve of ₹ 2,000 is used for providing the liability and balance amount of ₹ 10,000 (*i.e.*, 12,000 – 2,000) is distributed among Madan and Mohan in their old profit-sharing ratio.
3. *Calculation of Gopal's Share of Capital:*

	₹
Adjusted Capital of Madan	99,780
Adjusted Capital of Mohan	66,520
Combined capital of Madan and Mohan for 4/5 share	1,66,300

Total Capital of the firm should be = ₹ 1,66,300 × 5/4 = ₹ 2,07,875

Gopal's Share of Capital = ₹ 2,07,875 × 1/5 = ₹ 41,575.

4. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	10,000	By Balance *c/d*	82,375
To Bad Debts Recovered A/c	5,800		
To Gopal's Capital A/c (WN 3)	41,575		
To Premium for Goodwill A/c	25,000		
	82,375		82,375

4. JOURNAL OF BAYSON LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr.		40,00,000	
	To Equity Shares Application A/c			40,00,000
	(Being the application money received for 80,000 shares @ ₹ 50 per share)			
	Equity Shares Application A/c ...Dr.		40,00,000	
	To Equity Share Capital A/c (54,000 × ₹ 50)			27,00,000
	To Equity Shares Allotment A/c (40,000 × ₹ 10)			4,00,000
	To Calls-in-Advance A/c ₹ (40,00,000 – 27,00,000 – 4,00,000)			9,00,000
	(Being the application money adjusted)			
	Equity Shares Allotment A/c ...Dr.		5,40,000	
	To Equity Share Capital A/c			5,40,000
	(Being the allotment money due on 54,000 shares @ ₹ 10 per share)			
	Bank A/c (WN 3) ...Dr.		1,88,000	
	To Equity Shares Allotment A/c			1,40,000
	To Calls-in-Advance A/c (1,200 × ₹ 40)			48,000
	(Being the allotment money received and advance of call money on 1,200 shares)			
	Equity Shares First and Final Call A/c (54,000 × ₹ 40) ...Dr.		21,60,000	
	To Equity Share Capital A/c			21,60,000
	(Being the call money due)			
	Bank A/c ...Dr.		12,05,000	
	Calls-in-Advance A/c (₹ 9,00,000 + ₹ 48,000) ...Dr.		9,48,000	
	Calls-in-Arrears A/c (WN 4) ...Dr.		7,000	
	To Equity Shares First and Final Call A/c			21,60,000
	(Being the first and final call money received) (WN 4)			

	Equity Share Capital A/c (400 × ₹ 100) ...Dr. To Forfeited Shares A/c (660 × ₹ 50) To Calls-in-Arrears A/c (Being 400 shares of Vidur forfeited)		40,000	 33,000 7,000
	Bank A/c (400 × ₹ 110) ...Dr. To Equity Share Capital A/c (400 × ₹ 100) To Securities Premium Reserve A/c (400 × ₹ 10) (Being 400 shares reissued for ₹ 110 per share as fully paid-up)		44,000	 40,000 4,000
	Forfeited Shares A/c ...Dr. To Capital Reserve A/c (Being the gain on reissue transferred to Capital Reserve)		33,000	 33,000

BALANCE SHEET OF BAYSON LTD.

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
(a) Share Capital	1	54,00,000
(b) Reserves and Surplus	2	37,000
Total		54,37,000
II. ASSETS		
Current Assets		
Cash and Cash Equivalents	3	54,37,000
Total		54,37,000

Notes to Accounts

Particulars	₹
1. Share Capital	
Authorised Capital	
... Equity Shares of ₹ 100 each	...
Issued Capital	
54,000 Equity Shares of ₹ 100 each	54,00,000
Subscribed Capital	
Subscribed and Fully paid-up	
54,000 Equity Shares of ₹ 100 each	54,00,000
2. Reserves and Surplus	
Capital Reserve	33,000
Securities Premium Reserve	4,000
	37,000
3. Cash and Cash Equivalents	
Cash at Bank	54,37,000

Working Notes:

1. *Adjustment of Excess of Application Money:*

	Number of Applied Shares	*Number of Allotted Shares*
Total Shares	80,000	54,000
Full Allotment	14,000	14,000
Pro rata Allotment	66,000	40,000

Pro rata Allotment: Excess Application Money = (66,000 – 40,000) × ₹ 50 = ₹ 13,00,000;
Adjusted on Allotment = 40,000 × ₹ 10 = ₹ 4,00,000;
Adjusted on Call = ₹ 13,00,000 – ₹ 4,00,000 = ₹ 9,00,000.

2. *Calculation of Allotment money not paid by Vidur:*

		₹
(*a*)	Total Number of Shares applied by Vidur = $\frac{66,000}{40,000} \times 400 = 660$ shares.	
(*b*)	Application money received on shares allotted to Vidur (660 × ₹ 50)	33,000
(*c*)	*Less:* Application money due on shares allotted to Vidur (400 × ₹ 50)	20,000
(*d*)	Excess application money to be adjusted on allotment and call	13,000
(*e*)	Allotment money due on shares allotted to Vidur (400 × ₹ 10)	4,000
	Less: Excess application money adjusted on allotment	4,000
	Amount not paid by Vidur on Allotment	NIL

Still excess application money ₹ 9,000 (*i.e.*, ₹ 13,000 – ₹ 4,000) remains to be adjusted on call.

3. *Calculation of allotment money received later:*

	₹
Total allotment money due (54,000 × ₹ 10)	5,40,000
Less: Excess application money adjusted on allotment	4,00,000
	1,40,000
Add: Calls-in-Advance (1,200 × ₹ 40)	48,000
	1,88,000

4. *Calculation of first and final call money not paid by Vidur:*

	₹
Total first and final call money due (400 × ₹ 40)	16,000
Less: Excess application money to be adjusted on call (WN 2)	9,000
Call money not paid by Vidur	7,000

5. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Equity Shares Application A/c	40,00,000	By Balance *c/d*	54,37,000
To Equity Shares Allotment A/c	1,40,000		
To Calls-in-Advance A/c	48,000		
To Equity Shares First and Final Call A/c	12,05,000		
To Equity Share Capital A/c	40,000		
To Securities Premium Reserve A/c	4,000		
	54,37,000		54,37,000

5. (*a*) **Mars Ltd.**

JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr.		5,00,000	
	To Debentures Application and Allotment A/c			5,00,000
	(Being the application money received for 5,000 debentures)			
	Debentures Application and Allotment A/c ...Dr.		5,00,000	
	To 9% Debentures A/c			5,00,000
	(Being the issue of 5,000, 9% Debentures of ₹ 100 each at par)			
	Debentures Suspense A/c ...Dr.		10,00,000	
	To 9% Debentures A/c			10,00,000
	(Being the issue of 10,000, 9% Debentures of ₹ 100 each as collateral security for a loan from ICICI)			

AN EXTRACT OF BALANCE SHEET OF MARS LTD. *as at...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Non-Current Liabilities		
Long-term Borrowings	1	13,00,000

Note to Accounts

Particulars	₹	₹
1. Long-term Borrowings		
5,000, 9% Debentures of ₹ 100 each		5,00,000
Loan from ICICI Ltd.		8,00,000
(Secured by the issue of 10,000; 9% Debentures of ₹ 100 each as collateral security)		
10,000; 9% Debentures of ₹ 100 each (issued as collateral security)	10,00,000	
Less: Debentures Suspense Account	10,00,000	Nil
		13,00,000

(*b*) JOURNAL OF EUROPA LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Incorporation Cost A/c ...Dr.		2,00,000	
	To Promoters' A/c			2,00,000
	(Being the incorporation cost)			
	Promoters' A/c ...Dr.		2,00,000	
	To 10% Debentures A/c			2,00,000
	(Being 2,000; 10% Debentures of ₹ 100 each issued at par)			
	Underwriting Commission A/c ...Dr.		1,00,000	
	To Underwriters' A/c			1,00,000
	(Being the underwriting commission due)			
	Underwriters' A/c ...Dr.		1,00,000	
	To 10% Debentures A/c			1,00,000
	(Being 1,000; 10% Debentures of ₹ 100 each issued at par)			

(*c*) (*i*) JOURNAL OF MILTON LTD.

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c ...Dr.		90,000	
	To Debentures Application and Allotment A/c			90,000
	(Being the debentures application money received)			
	Debentures Application and Allotment A/c ...Dr.		90,000	
	Loss on Issue of Debentures A/c* ...Dr.		15,000	
	To 10% Debentures A/c			1,00,000
	To Premium on Redemption of Debentures A/c			5,000
	(Being 1,000; 10% Debentures issued at a discount of 10% and redeemable at a premium of 5%)			
	Statement of Profit and Loss (Finance Cost) ...Dr.		15,000	
	To Loss on Issue of Debentures A/c			15,000
	(Being the Loss on issue of Debentures written off from Statement of Profit and Loss)			

* Loss on Issue of Debentures = ₹ 10,000 (Discount on Issue) + ₹ 5,000 (Premium on Redemption) = ₹ 15,000.

(*ii*) JOURNAL OF DUBBLIN LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	...Dr.		2,40,000	
	To Debentures Application and Allotment A/c				2,40,000
	(Being the debentures application money received)				
	Debentures Application and Allotment A/c	...Dr.		2,40,000	
	Loss on Issue of Debentures A/c	...Dr.		20,000	
	To 9% Debentures A/c				2,00,000
	To Securities Premium Reserve A/c				40,000
	To Premium on Redemption of Debentures A/c				20,000
	(Being 2,000; 9% Debentures issued at a premium of ₹ 20 and redeemable at a premium of ₹ 10 per debenture)				
	Securities Premium Reserve A/c	...Dr.		20,000	
	To Loss on Issue of Debentures A/c				20,000
	(Being the loss on issue of debentures written off)				

6. (*a*) JOURNAL OF MOON LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2018					
Oct. 1	Own Debentures A/c	...Dr.		27,900	
	To Bank A/c				27,900
	(Being the purchase of 300 own debentures @ ₹ 93)				
	10% Debentures A/c	...Dr.		30,000	
	To Own Debentures A/c				27,900
	To Gain on Cancellation of Own Debentures A/c				2,100
	(Being the cancellation of 300 own debentures)				
	Gain on Cancellation of Own Debentures A/c	...Dr.		2,100	
	To Capital Reserve A/c				2,100
	(Being the transfer of gain on cancellation of own debentures to Capital Reserve)				
2019					
March 31	Interest on Debentures A/c	...Dr.		3,500	
	To Debentureholders' A/c				3,500
	(Being the interest due on ₹ 70,000 @ 10% p.a. for 6 months)				
March 31	Debentureholders' A/c	...Dr.		3,500	
	To Bank A/c				3,500
	(Being the payment made to debentureholders)				
March 31	Statement of Profit and Loss	...Dr.		8,500	
	To Interest on Debentures A/c (Note)				8,500
	(Being the interest on debentures transferred to Statement of Profit and Loss)				

Note: Interest on Debentures (30th September, 2017) = 1,00,000 × 10/100 × 6/12 = ₹ 5,000

Interest on Debentures (31st March, 2018) = ₹ 70,000 × 10/100 × 6/12 = ₹ 3,500

Total Interest for the year ended 31st March, 2018 = ₹ 8,500

(*b*)

S. No.	Items	Major Head	Sub-head
(*i*)	Long-term Borrowings	Non-current Liabilities	Long-term Borrowings
(*ii*)	Trade Payables	Current Liabilities	Trade Payables
(*iii*)	Provision for Tax	Current Liabilities	Short-term Provisions
(*iv*)	Patents	Non-current Assets	Fixed Assets—Intangible Assets
(*v*)	Accrued Income	Current Assets	Other Current Assets
(*vi*)	Calls-in-Advance	Current Liabilities	Other Current Liabilities

7.

Dr. REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Machinery A/c	60,000	By Land and Building A/c		60,000
To Bad Debts A/c (WN 1)	7,000	By Loss transferred to:		
		Amal's Capital A/c	2,000	
		Bimal's Capital A/c	3,000	
		Kamal's Capital A/c	2,000	7,000
	67,000			67,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Amal ₹	Bimal ₹	Kamal ₹	Particulars	Amal ₹	Bimal ₹	Kamal ₹
To Goodwill A/c	6,000	9,000	6,000	By Balance *b/d*	2,00,000	3,00,000	2,00,000
To Advertisement Expenditure A/c	4,000	6,000	4,000	By General Reserve A/c	20,000	30,000	20,000
To Revaluation A/c (Loss)	2,000	3,000	2,000	By Workmen Compen-Reserve A/c	2,000	3,000	2,000
To Amal's Capital A/c (WN 2)	...	20,000	20,000	By Bimal's Capital A/c (WN 2)	20,000	...	...
To Bank A/c	50,000	...	...	By Kamal's Capital A/c (WN 2)	20,000	...	...
To Amal's Loan A/c	2,00,000	...	...	By Bank A/c (Bal. Fig.)	...	1,05,000	1,10,000
To Balance *c/d* (WN 3)	...	4,00,000	3,00,000				
	2,62,000	4,38,000	3,32,000		2,62,000	4,38,000	3,32,000

BALANCE SHEET
(After Amal's Retirement)
as at 31st March, 2019

Liabilities		₹	Assets	₹
Capital A/cs:			Land and Building	2,60,000
Bimal	4,00,000		Machinery	2,40,000
Kamal	3,00,000	7,00,000	Closing Stock	1,00,000
Amal's Loan A/c		2,00,000	Sundry Debtors	93,000
Workmen Compensation Claim		8,000	Cash at Bank (WN 4)	2,65,000
Sundry Creditors		50,000		
		9,58,000		9,58,000

Working Notes:

1. *Accounting Entries for Bad Debts:*

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bad Debts A/c	...Dr.		17,000	
	To Sundry Debtors A/c				17,000
	Provision for Doubtful Debts A/c	...Dr.		10,000	
	Revaluation A/c	...Dr.		7,000	
	To Bad Debts A/c				17,000

2. (*i*) Amal's Share of Goodwill = ₹ 1,40,000 × $\frac{2}{7}$ = ₹ 40,000, which is contributed by Bimal and Kamal in their gaining ratio. It is calculated as follows:

   Bimal's Gain = $\frac{4}{7}-\frac{3}{7}=\frac{1}{7}$; Kamal's Gain = $\frac{3}{7}-\frac{2}{7}=\frac{1}{7}$

   Gaining Ratio of Bimal and Kamal = $\frac{1}{7}:\frac{1}{7}$ or 1 : 1.

   (*ii*) Thus, Bimal and Kamal will contribute for Amal's share of goodwill = ₹ 40,000 × $\frac{1}{2}$ = ₹ 20,000 each.

3. *Calculation of Proportionate Capital of the remaining partners in the new firm:*
   Total Capital of the firm before the retirement of Amal = ₹ 7,00,000, which is contributed by Bimal and Kamal in their new profit-sharing ratio, *i.e*, 4 : 3. Thus,

   Bimal's Capital in the new firm = ₹ 7,00,000 × $\frac{4}{7}$ = ₹ 4,00,000;

   Kamal's Capital in the new firm = ₹ 7,00,000 × $\frac{3}{7}$ = ₹ 3,00,000.

4. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,00,000	By Amal's Capital A/c	50,000
To Bimal's Capital A/c	1,05,000	By Balance *c/d*	2,65,000
To Kamal's Capital A/c	1,10,000		
	3,15,000		3,15,000

8.

Dr. REALISATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Debtors	2,42,000	By Sundry Creditors		60,000
To Stock	78,000	By Loan from Mrs. Mohan		15,000
To Investment	1,70,000	By Provision for Doubtful Debts		12,000
To Fixed Assets	10,000	By Ram's Capital A/c:		
To Ram's Capital A/c (Creditors)	60,000	Fixed Assets	8,000	
To Sohan's Capital A/c (Loan + Interest)	15,300	Debtors	1,72,000	1,80,000
To Ram's Capital A/c (Remuneration)	2,700	By Mohan's Capital A/c:		
		Stock	70,000	
		Investments	72,000	1,42,000
		By Sohan's Capital A/c (Investments)		80,000
		By Bank A/c (Debtors)		21,000
		By Loss on Realisation transferred to:		
		Ram's Capital A/c	40,800	
		Mohan's Capital A/c	13,600	
		Sohan's Capital A/c	13,600	68,000
	5,78,000			5,78,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Ram ₹	Mohan ₹	Sohan ₹	Particulars	Ram ₹	Mohan ₹	Sohan ₹
To Realisation A/c	1,80,000	1,42,000	80,000	By Balance *b/d*	2,45,000	90,000	60,000
To Realisation A/c (Loss)	40,800	13,600	13,600	By Realisation A/c	60,000	...	15,300
To Advertisement Suspense A/c	30,000	10,000	10,000	By Realisation A/c	2,700	...	...
To Bank A/c (Balancing Figure)	1,16,900	...	...	By General Reserve A/c	60,000	20,000	20,000
				By Bank A/c (Balancing Figure)	...	55,600	8,300
	3,67,700	1,65,600	1,03,600		3,67,700	1,65,600	1,03,600

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	32,000	By Ram's Capital A/c (Final Payment)	1,16,900
To Realisation A/c (Debtors)	21,000		
To Mohan's Capital A/c (Cash brought in)	55,600		
To Sohan's Capital A/c (Cash brought in)	8,300		
	1,16,900		1,16,900

Working Notes:

1. Book Value of Investment taken over by Mohan = ₹ 72,000 × 10/9 = ₹ 80,000.
2. Remaining investment = ₹ 1,70,000 – ₹ 80,000 = ₹ 90,000.
3. Book Value of Investment taken over by Sohan = 90% of ₹ 90,000 = ₹ 81,000.
4. Agreed value of investment taken over by Sohan = ₹ 81,000 – ₹ 1,000 = ₹ 80,000.

Section B

9. (*a*) CASH FLOW FROM INVESTING ACTIVITIES

Particulars	₹
Purchase of Machinery (₹ 4,00,000 – ₹ 3,00,000)	(1,00,000)
Purchase of 10% Investments	(1,00,000)
Rent Received	30,000
Dividend Received from Investment in shares (10% of ₹ 1,50,000)	15,000
Sale of 10% Investments (WN 1)	60,000
Interest Income on 10% Investments	12,000
Sale of Patents (WN 2)	15,000
Cash Used in Investing Activities	(68,000)

Working Notes:

1. *Dr.* 10% INVESTMENTS ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,50,000	By Bank A/c (Sale) (Balancing Figure)	60,000
To Bank A/c (Purchase)	1,00,000	By Balance *c/d*	2,00,000
To Statement of Profit and Loss (Profit on Sale)	10,000		
	2,60,000		2,60,000

2. *Dr.* PATENTS ACCOUNTS *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	80,000	By Statement of Profit and Loss (Written off)	10,000
		By Bank A/c (Sale) (Balancing Figure)	15,000
		By Statement of Profit and Loss (Loss on Sale)	5,000
		By Balance *c/d*	50,000
	80,000		80,000

3. Decrease in the book value of Goodwill by ₹ 15,000 indicates amortisation of Goodwill. It is adjusted while calculating Cash Flow from Operating Activities and does not effect Cash Flow from Investing Activities.

(*b*) CASH FLOW FROM FINANCING ACTIVITIES

Particulars	₹
Proceeds from issue of Equity Share Capital [₹ 2,00,000 + ₹ 20,000 (Premium]	2,20,000
Proceeds from Issue of Debentures (₹ 5,00,000 – ₹ 4,00,000)	1,00,000
Redemption of 10% Preference Shares [₹ 1,00,000 + ₹ 5,000 (Premium)]	(1,05,000)
Payment of Preference Dividend (10% × ₹ 3,00,000)	(30,000)
Payment of Equity Dividend (9% × ₹ 4,00,000)	(36,000)
Interest paid on Debentures (10% × ₹ 5,00,000)	(50,000)
Cash Flow from Financing Activities	99,000

10. (*a*) (*i*) $\text{Liquid Ratio} = \dfrac{\text{Quick Assets}}{\text{Current Liabilities}} = \dfrac{₹\ 2,70,000}{₹\ 1,50,000} = 1.8 : 1.$

Note: Quick Assets = Total Current Assets – Prepaid Insurance – Closing Inventory
= ₹ 3,00,000 – ₹ 5,000 – 25,000 = ₹ 2,70,000.

(*ii*) $\text{Proprietary Ratio} = \dfrac{\text{Shareholders' Funds/Equity}}{\text{Total Assets}} = \dfrac{₹\ 4,50,000}{₹\ 9,00,000} = 0.5 : 1.$

Notes:

1. Shareholders' Funds = Share Capital + Reserves and Surplus
= ₹ 4,00,000 + ₹ 50,000 = ₹ 4,50,000.

2. Total Assets = Total Current Assets + Non-current Assets
= ₹ 3,00,000 + ₹ 6,00,000 = ₹ 9,00,000.

(*iii*) $\text{Working Capital Turnover Ratio} = \dfrac{\text{Revenue from Operations}}{\text{Working Capital}} = \dfrac{₹\ 5,00,000}{₹\ 1,50,000} = 3.33 \text{ Times.}$

Note: Working Capital = Current Assets – Current Liabilities
= ₹ 3,00,000 – ₹ 1,50,000 = ₹ 1,50,000.

(*b*) $\text{Trade Receivables Turnover Ratio} = \dfrac{\text{Credit Revenue from Operations}}{\text{Average Trade Receivables}}$

$$= \dfrac{₹\ 30,000}{₹\ 30,000} = 1 \text{ Time.}$$

Working Notes:

1. *Calculation of Credit Revenue from Operations:*

Let Cash Revenue from Operation = X, credit Revenue from Operation will be 25% of X or $X/4$.

Total Revenue from Operations = Cash Revenue from Operations + Credit Revenue from Operation

$$₹\,1,50,000 = X + X/4$$

$$5X = ₹\,6,00,000$$

$$X = ₹\,6,00,000/5 = ₹\,1,20,000 \text{ (Cash Revenue from Operations)}$$

Credit Revenue from Operations = ₹ 1,20,000 × 1/4 = ₹ 30,000.

2. *Calculation of Average Trade Receivables:*

Opening Trade Receivables = ₹ 40,000 – ₹ 20,000 = ₹ 20,000

$$\text{Average Trade Receivables} = \frac{\text{Opening Trade Receivables} + \text{Closing Trade Receivables}}{2}$$

$$= \frac{₹\,20,000 + ₹\,40,000}{2} = ₹\,30,000.$$

11.

(*a*) COMPARATIVE BALANCE SHEET OF FABLE LTD. *as at 31st March, 2019 and 2018*

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)	Absolute Change (₹)	Percentage Change (%)
I. EQUITY AND LIABILITIES					
1. Shareholders' Funds					
(*a*) Share Capital		25,00,000	25,00,000	...	...
(*b*) Reserves and Surplus		6,00,000	5,00,000	1,00,000	20.00
2. Non-Current Liabilities					
(*a*) Long-term Borrowings		15,00,000	15,00,000	...	...
3. Current Liabilities		5,50,000	5,00,000	50,000	10.00
Total		51,50,000	50,00,000	1,50,000	3.00
II. ASSETS					
1. Non-Current Assets					
(*a*) Fixed Assets		36,00,000	30,00,000	6,00,000	20.00
(*b*) Non-current Investments		5,00,000	5,00,000	...	...
2. Current Assets		10,50,000	15,00,000	(4,50,000)	(30.00)
Total		51,50,000	50,00,000	1,50,000	3.00

Note: When the amount of current year has decreased, then the absolute change and percentage change is shown in brackets.

(*b*)
$$\text{Interest Coverage Ratio} = \frac{\text{Profit before Interest and Tax}}{\text{Interest on Long-term Debt}}$$

Profit before Interest and Tax = ₹ 2,00,000

Interest on Debentures = ₹ 5,00,000 × 8/100 = ₹ 40,000

$$\text{Interest Coverage Ratio} = \frac{₹\,2,00,000}{₹\,40,000} = 5 \text{ Times.}$$

(*c*) Advantages of Comparative Balance Sheet:

(*i*) Comparative Balance Sheet Shows the increase or decrease in various items of Balance Sheet as compared to single year's Balance Sheet which shows the balances of assets, equity and liabilities accounts at a certain date.

(*ii*) Comparative Balance Sheet acts as a connecting link between Statement of Profit and Loss and the Balance Sheet as it shows the effect of business operation on its assets, liabilities and capital.

Model Test Paper 3

Time Allowed: 3 Hrs. **Max. Marks: 80**

General Instructions: As per Model Test Paper 1

Section A

Part I (12 Marks)

*(Answer **all** questions)*

1. Answer the following questions briefly:

(*i*) What is meant by 'Debentures Redemption Reserve'? State the amount of profit required to be transferred to Debentures Redemption Reserve.

(*ii*) What is Gaining Ratio in case of retirement of a partner? Give **two** circumstances in which Gaining Ratio may be applied.

(*iii*) Raja, Badshah and Samrat are partners sharing profits in the ratio of 3 : 2 : 1. Badshah died on 30th June, 2019. Profit from 1st April, 2019 to 30th June, 2019 was ₹ 2,25,000. Raja and Samrat decided to share the future profits in the ratio of 3 : 2. Give the necessary Journal entry to record Badshah's share of profit up to the date of death.

(*iv*) Give the Journal entry to distribute 'Investment Fluctuation Reserve' of ₹ 40,000 at the time of admission of Sachin for 20% share of profit, when Investments (Market Value ₹ 1,90,000) appear at ₹ 2,00,000. The firm has two old partners Sunil and Dalip.

(*v*) State **two** differences between Undersubscription and Oversubscription.

(*vi*) List **four** items which are included under the head 'Non-Current Assets' of the company's Balance Sheet as per Schedule III. [6 × 2 = 12]

Part II (48 Marks)

*(Answer **any four** questions)*

2. (*a*) Anjan, Sooraj and Niranjan are in partnership with capitals of ₹ 3,00,000 (Credit), ₹ 2,50,000 (Credit) and ₹ 20,000 (Debit) respectively on 1st April, 2018. The Partnership Deed provides the following:

(*i*) 10% of Net Profit to be transferred to General Reserve.

(*ii*) Partners are to be allowed interest on capital @ 5% p.a. and are to be charged interest on drawings @ 6% p.a.

(*iii*) Niranjan is to get salary of ₹ 60,000 p.a.

(*iv*) Anjan is to get commission of 10% of the profit.

(*v*) Sooraj is also entitled to a commission of 10% of the net profit before charging interest on drawings but after making appropriations.

During the year, Anjan withdrew ₹ 3,000 in the beginning of every month, Sooraj withdrew ₹ 3,000 during every month and Niranjan withdrew ₹ 3,000 at the end of every month.

On 1st October, 2018, Niranjan gave a loan of ₹ 5,00,000.

The manager is entitled to salary of ₹ 2,000 p.m. and a commission of 10% of net profit after charging his salary and commission.

Net Profit of the firm for the year ended on 31st March, 2019 before providing for any of the above adjustments was ₹ 2,37,000.

Prepare Profit and Loss Appropriation Account for the year ended on 31st March, 2019.

(*b*) Calculate goodwill of a firm on the basis of three years' purchase of the weighted average profit of the last four years. The appropriate weights to be used and profits are:

Year	2015–16	2016–17	2017–18	2018–19
Profits (₹)	1,01,000	1,24,000	1,00,000	1,40,000
Weights	1	2	3	4

On a scrutiny of the accounts, following was noticed:

(*i*) On 1st December, 2017, major repair was carried on the plant incurring ₹ 30,000 which was charged to revenue. The said amount is agreed to be capitalised for goodwill valuation subject to adjustment of depreciation of 10% p.a. on Reducing Balance Method.

(*ii*) Closing stock for the year 2016–17 was overvalued by ₹ 12,000.

(*iii*) To cover management cost, an annual charge of ₹ 24,000 should be made for the purpose of goodwill valuation.

(*iv*) On 1st April, 2016 a machine having a book value of ₹ 10,000 was sold for ₹ 11,000 but the proceeds were wrongly credited to Profit and Loss Account. No effect has been given to rectify the same. Depreciation is charged on machine @ 10% p.a. on Reducing Balance Method. [6 + 6 = 12]

3. (*a*) Priya, Karam and Anna were partners of a firm sharing profits in the ratio of 3 : 2 : 1. Their Balance Sheet as at 31st March, 2019 was as follows:

BALANCE SHEET *as at 31st March, 2019*

Liabilities		₹	Assets	₹
Bills Payable		1,20,000	Cash at Bank	20,000
Creditors		1,40,000	Debtors	1,40,000
Karam's Loan @ 5%		1,00,000	Bills Receivable	70,000
General Reserve		1,80,000	Stock	1,70,000
Capital A/cs:			Investments	1,30,000
Priya	2,00,000		Advertisement Suspense A/c	1,20,000
Karam	1,20,000		Building	2,90,000
Anna	80,000	4,00,000		
		9,40,000		9,40,000

Karam died on 12th June, 2019 and according to the Partnership Deed his executors were entitled to be paid as under.

(*i*) His share in the profit of the firm till the date of his death which will be calculated on the basis of average profit of last three completed years.

(*ii*) His share in the goodwill of the firm which will be calculated on the basis of two years' purchase of total profits of last three years.

(*iii*) Profits for the last three years ended 31st March, were: ₹ 30,000, ₹ 70,000 and ₹ 80,000.

(*iv*) It is decided by Priya and Anna that General Reserve and accumulated losses to continue appearing in the books of the new firm at their existing values.

Prepare Karam's Capital Account to be rendered to his executors.

(*b*) Lokesh, Mansoor and Nihal were partners in a firm sharing profits as 50%, 30% and 20% respectively. On 31st March, 2019 their Balance Sheet was as follows:

Liabilities		₹	Assets		₹
Creditors		34,000	Cash at Bank		68,000
Employees' Provident Fund		10,000	Stock		38,000
Investment Fluctuation Reserve		20,000	Debtors	94,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	6,000	88,000
Lokesh	1,40,000		Investments		80,000
Mansoor	80,000		Goodwill		40,000
Nihal	50,000	2,70,000	Profit and Loss		20,000
		3,34,000			3,34,000

On 1st April, 2019, Mansoor retired and Lokesh and Nihal agreed to continue business on the following terms:

(*i*) Firm's goodwill was valued at ₹ 1,02,000 and it was decided to adjust Mansoor's share of goodwill into the Capital Accounts of the continuing partners.

(*ii*) There was a claim for Workmen's Compensation to the extent of ₹ 12,000 and investments were brought down to ₹ 30,000.

(*iii*) Provision for Doubtful Debts was to be reduced by ₹ 2,000.

(*iv*) Mansoor was to be paid ₹ 20,600 by cheque and the balance will be transferred to his loan account which was paid in two equal annual instalments along with interest @ 10% p.a.

(*v*) Capitals of Lokesh and Nihal were to be adjusted in their new profit-sharing ratio by bringing in or paying off by cheque as the case may be.

Prepare Revaluation Account, Partners' Capital Accounts and Balance Sheet of the new firm. [4 + 8 = 12]

4. Mamta Fab Ltd. issued 50,000 equity shares of ₹ 100 each payable ₹ 20 on application; ₹ 40 on allotment and ₹ 20 each on first and final call. Applications were received for 75,000 shares. Applicants of 25,000 shares were sent letters of regret and application money was refunded.

Mohan, a holder of 1,500 shares failed to pay allotment money which he paid along with the first call.

Raman, a shareholder holding 500 shares paid both the calls along with allotment. Kamal, a shareholder holding 1,000 shares did not pay first call and second and final call. His shares were forfeited. 800 of these forfeited shares were reissued at ₹ 120 per share as fully paid-up.

Pass necessary Journal entries for the above transactions in the books of the company. Also show relevant items as they would appear in the Balance Sheet of the company. [12]

5. Deepika and Rajshree are partners sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as on 31st March, 2019 is as under:

Liabilities		₹	Assets		₹
Creditors		75,000	Goodwill		5,000
Bank Overdraft		50,000	Building		30,000
Workmen Compensation Reserve		10,000	Furniture		1,25,000
Investment Fluctuation Reserve		5,000	Investments (Market Value ₹ 22,500)		25,000
Employees' Provident Fund		5,000	Debtors	50,000	
Anshu's Loan		1,50,000	*Less:* Provision for Doubtful Debts	5,000	45,000
Capital A/cs:			Stock		1,50,000
Deepika	88,000		Bank Balance		1,25,000
Rajshree	1,27,000	2,15,000	Advertisement Suspense A/c		5,000
		5,10,000			5,10,000

On 1st April, 2019, they admit Anshu as a partner on the following terms:

(*i*) Deepika will sacrifice 1/3rd of her share while Rajshree sacrifices 1/10 from her share in favour of Anshu.

(*ii*) Anshu's loan will be converted into his capital.

(*iii*) Anshu brings 60% of his share of goodwill by cheque.

(*iv*) Goodwill is to be valued at 2 years' purchase of super profit of last three completed years. Profits for the last three years ended 31st March, are as follows:
2017—₹ 2,40,000; 2018—₹ 4,65,000; and 2019—₹ 6,90,000.
Normal profit is ₹ 3,15,000 with same amount of capital invested in similar industry.

(*v*) Value of building is to be increased by ₹ 25,000, value of Stock and Furniture to be reduced by 15% and 10% respectively. Provision for Doubtful Debts is to be made equal to 5% of the debtors.

(*vi*) Claim on account of Workmen Compensation is ₹ 5,000.

(*vii*) An unrecorded accrued interest income of ₹ 5,000 to be accounted. A debtor whose dues of ₹ 25,000 were written off as bad debts, paid ₹ 20,000 in full settlement.

(*viii*) Workmen Compensation Reserve and Investment Fluctuation Reserve are to appear in the books of new firm after adjusting Workmen Compensation Claim and difference between book value and market value of investment.

(*ix*) Capital Accounts of the partners to be readjusted on the basis of their profit-sharing ratio and any excess or deficiency be adjusted in cash.

Prepare Revaluation Account, Partners' Capital Accounts and the Balance Sheet. [12]

6. On 1st April, 2017, Strong Ltd. issued ₹ 40,00,000, 10% Debentures of ₹ 100 each at a premium of 5% and redeemable at a premium of 10% in equal annual drawings by draw of lots in 2 years. Pass the necessary Journal entries during the years of Issue and Redemption of Debentures without providing for the interest and Loss on Issue of Debentures. [12]

7. (*a*) Given below is the Balance Sheet of Saurabh, Gaurav and Pawan as on 31st March, 2019 on which date they dissolved their partnership. They shared profit and loss in the ratio of 4 : 3 : 3. It was decided that Pawan shall be in charge of realisation and distribution. For this service, he was to get as remuneration 1% of the value of assets realised other than Cash and Bank and 10% of the amount distributed to partners.

BALANCE SHEET *as at 31st March, 2019*

Liabilities	₹	Assets	₹
Saurabh's Capital A/c	55,000	Cash at Bank	1,375
Gaurav's Capital A/c	22,500	Sundry Assets	2,68,625
Pawan's Capital A/c	60,000	(Other than Cash and Bank)	
Sundry Creditors	75,000		
Employees' Provident Fund	7,500		
Workmen Compensation Reserve	50,000		
	2,70,000		2,70,000

Sundry Assets were realised for ₹ 2,32,500 and creditors were paid in full. Prepare Realisation Account, Partners' Capital Accounts and Bank Account.

(*b*) Pass the necessary Journal entries for the following transactions on the dissolution of the firm of Samar, Bhanwar and Pratap (who were sharing profits in the ratio of 2 : 2 : 1) after the transfer of all assets (other than cash) and external liabilities to Realisation Account:

(*i*) Debtors were of ₹ 1,24,200. Samar takes debtors amounted to ₹ 1,20,000 at ₹ 1,17,200 and the remaining debtors were sold to a debt collecting agency at 50% of the value.

(*ii*) Sundry Assets were of ₹ 1,17,000. Bhanwar is to take some Sundry Assets at ₹ 72,000 (being 10% less than the book value). Pratap is to take over remaining Sundry Assets at 80% of the book value. [8 + 4 = 12]

8. From the following details given below and additional information, prepare Balance Sheet of Lotus Ltd. as at 31st March, 2019:

	(₹ in "000)		(₹ in "000)
10% Debentures	200	Trade Receivables	40
Trade Payables	10	Cash and Bank Balances	30
Share Capital	150	Share Application Money	
Reserves and Surplus	90	Pending Allotment	5
Advance Payment of Tax	50	Non-current Investment	100
Fixed Assets at Cost (Tangible)	350	Provision for Tax (2018–19)	45
Inventories	10	Long-term Provisions	10
Outstanding Expenses	5	Current Investment	25
Short-term Borrowings	45	Prepaid Expenses	5
Provision for Depreciation	40		

Additional Information:

(*i*) Authorised capital is 20,000 equity shares of ₹ 10 each. The company issued 15,000 shares of ₹ 10 each.

(*ii*) Provide ₹ 10,000 for depreciation on fixed assets.

(*iii*) Directors proposed dividend for the year 2018–19 ₹ 50,000. [12]

Section B

(20 Marks)

*(Answer **any two** questions)*

9. You are required to prepare a Cash Flow Statement for the year 2018–19 from the following Balance Sheet and additional information:

BALANCE SHEET OF STAR LTD. *as at 31st March, 2019*

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)
I. EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(*a*) Share Capital		5,00,000	4,00,000
(*b*) Reserves and Surplus	1	3,20,000	2,50,000
2. Non-Current Liabilities			
Long-term Borrowings	2	2,00,000	1,00,000
3. Current Liabilities			
(*a*) Trade Payables		1,50,000	90,000
(*b*) Short-term Provisions	3	30,000	10,000
Total		12,00,000	8,50,000
II. ASSETS			
1. Non-Current Assets			
(*a*) Fixed Assets—Tangible	4	7,00,000	5,00,000
(*b*) Non-Current Investments		70,000	50,000
2. Current Assets			
(*a*) Inventories		60,000	90,000
(*b*) Trade Receivables		1,20,000	70,000
(*c*) Cash and Bank Balance		2,50,000	1,40,000
Total		12,00,000	8,50,000

Notes to Accounts

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
1. Reserves and Surplus		
Securities Premium Reserve	5,000	...
General Reserve	1,00,000	80,000
Surplus, *i.e.*, Balance in Statement of Profit and Loss	2,15,000	1,70,000
	3,20,000	2,50,000
2. Long-term Borrowings		
10% Debentures	2,00,000	1,00,000
3. Short-term Provisions		
Provision for Tax	30,000	10,000
4. Fixed Assets—Tangible		
Machinery (*Cost*)	8,50,000	6,10,000
Less: Accumulated Depreciation	1,50,000	1,10,000
	7,00,000	5,00,000

Additional Information:

(*i*) Machinery costing ₹ 1,00,000 (Accumulated Depreciation ₹ 70,000) was sold at a loss of 20%. (*ii*) Equity Shares were issued at a premium of 15% on 1st April, 2018. (*iii*) Additional debentures were issued on 1st October, 2018 at a discount of 10%. The company wrote off the discount on issue of debentures from Securities Premium Reserve. (*iv*) Interim Dividend paid during the year amounted to ₹ 25,000. (*v*) Dividend have been proposed @ 12% for both the years. [10]

10. (*a*) From the following information, calculate **any two** of the following ratios:

(*i*) Debt to Equity Ratio;

(*ii*) Working Capital Turnover Ratio;

(*iii*) Return on Investment (ROI).

Information:

Equity Share Capital ₹ 5,50,000; General Reserve ₹ 50,000; Statement of Profit and Loss (Profit after Interest and Tax) ₹ 1,00,000; 9% Debentures ₹ 2,00,000; Creditors ₹ 1,00,000; Land and Building ₹ 6,50,000; Equipments ₹ 1,50,000; Debtors ₹ 1,45,000; Cash ₹ 55,000.

Revenue from Operations (Net Sales) for the year ended 31st March, 2019 was ₹ 15,00,000 and Tax Paid 50%.

(*b*) Calculate Debt to Total Assets Ratio from the following information:

	₹		₹
Fixed Assets (Gross)	18,00,000	Accumulated Depreciation	3,00,000
Non-current Investments	30,000	Current Liabilities	6,00,000
Long-term Loans and advances	1,20,000	Long-term Borrowings	9,00,000
Current Assets	7,50,000	Long-term Provisions	3,00,000

(*c*) Calculate Earning Per Share (EPS) from the following:

Net Profit after Tax,	₹ 1,00,000
10% Preference Share Capital (₹ 10 each)	₹ 2,00,000
Equity Share Capital (₹ 10 per share)	₹ 2,00,000

[6 + 2 + 2 = 10]

11. (*a*) What is Common-size Balance Sheet? Give **one** objective of Common-size Balance Sheet.

(*b*) Calculate Trade Payables Turnover Ratio from the following information:

	₹
Total Purchases	4,20,000
Cash Purchases	40,000
Purchases Return	20,000
Opening Creditors	40,000
Closing Creditors	30,000
Opening Bills Payable (B/P)	50,000
Closing Bills Payable (B/P)	60,000

(*c*) From the following information taken from the Income Statement of Sandalwood Products Ltd. for the year ended 31st March, 2019 and 2018, prepare Comparative Statement of Profit and Loss:

Particulars	31st March, 2019 (₹)	31st March, 2018 (₹)
Revenue from Operations	14,00,000	11,00,000
Other Incomes	4,00,000	3,00,000
Expenses	11,00,000	12,00,000

Rate of Income Tax was 50%.

Also, calculate Net Profit Ratio for 2018–19. [2 + 2 + 6 = 10]

Answers

1. (*i*) Debentures Redemption Reserve (DRR) is a reserve created out of profits available for distribution as dividend for the purpose of redemption of debentures.

The amount to be transferred to DRR is specified in Rule 18(7)(b) of the Companies (Share Capital and Debentures) Rules, 2014. The rule prescribes that a company shall *transfer at least 25 per cent of the nominal (face) value of the outstanding debentures to DRR*.

(*ii*) The ratio in which the remaining or continuing partners acquire the outgoing (retired or deceased) partner's share is called gaining ratio. This ratio is calculated by taking out the difference between the New Profit Share and Old Profit Share of each partner.

Gain of a Partner = New Share – Old Share.

Gaining Ratio may be applied:

(*a*) When there is change in profit-sharing ratio.

(*b*) When a partner retires/dies.

(*iii*) JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2019	Raja's Capital A/c (₹ 75,000 × 3/10) ...Dr.		22,500	
June 30	Samrat's Capital A/c (₹ 75,000 × 7/10) ...Dr.		52,500	
	To Badshah's Capital A/c (₹ 2,25,000 × 2/6)			75,000
	(Being the Badshah's share of profit till the date of death adjusted in the Capital Accounts of Raja and Samrat in their gaining ratio, *i.e.*, 3 : 1)			

Note: When the new profit-sharing ratio of continuing partners differs from their old profit-sharing ratio, outgoing partners' share of profit or loss is adjusted through the Capital Accounts of gaining partners in their gaining ratio. It is calculated as under:

Raja's Gain $= \frac{3}{5} - \frac{3}{6} = \frac{3}{30}$; Samrat's Gain $= \frac{2}{5} - \frac{1}{6} = \frac{7}{30}$.

Thus, Gaining Ratio of Raja and Samrat = 3 : 7.

(*iv*) JOURNAL

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Investment Fluctuation Reserve A/c ...Dr.		40,000	
	To Sunil's Capital A/c			15,000
	To Dalip's Capital A/c			15,000
	To Investments A/c			10,000
	(Being the value of Investments brought down to maket value and surplus Investment Fluctuation Reserve transferred to old Partners' Capital Accounts in the ratio of 1 : 1)			

(*v*)

Basis	*Undersubscription*	*Oversubscription*
1. **Shares Applied**	Number of shares applied is less than the number of shares offered for subscription.	Number of shares applied is more than the number of shares offered for subscription.
2. **Acceptance**	All the applications for shares are accepted, *i.e.*, full allotment is made.	All applications are not accepted. Some are rejected. Alternatively, shares are allotted on *pro rata* basis.
3. **Refund**	As all applications are accepted, there is no excess money to be refunded.	Excess application money is refunded or adjusted towards allotment.

(*vi*) Non-current Assets comprises of following items:

(*a*) Fixed Assets;

(*b*) Non-current Investments;

(*c*) Deferred Tax Assets (Net);

(*d*) Long-term Loans and Advances;

(*e*) Other Non-current Assets.

2. (*a*) PROFIT AND LOSS APPROPRIATION ACCOUNT

Dr. *for the year ended 31st March, 2019* *Cr.*

Particulars		₹	Particulars		₹
To General Reserve A/c (10% of ₹ 1,80,000)		18,000	By Profit and Loss A/c (Net Profit)		1,80,000
To Interest on Capital A/c:			By Interest on Drawings A/c:		
Anjan		15,000	Anjan (₹ 36,000 × 6.5/12 × 6/100)	1,170	
Sooraj	12,500	27,500	Sooraj (₹ 36,000 × 6/12 × 6/100)	1,080	
To Niranjan's Salary A/c		60,000	Niranjan (₹ 36,000 × 5.5/12 × 6/100)	990	3,240
To Anjan's Remuneration A/c (10% of ₹ 1,80,000)		18,000			
To Sooraj's Commission A/c [10/110(₹ 1,80,000 – ₹ 18,000 – ₹ 27,500 – ₹ 60,000 – ₹ 18,000)]		5,136			
To Profit transferred to:					
Anjan's Capital A/c	18,201				
Sooraj's Capital A/c	18,201				
Niranjan's Capital A/c	18,202	54,604			
		1,83,240			1,83,240

Working Notes: PROFIT AND LOSS ACCOUNT

1. *Dr.* *for the year ended 31st March, 2019* *Cr.*

Particulars	₹	Particulars	₹
To Interest on Niranjan's Loan A/c (₹ 5,00,000 × 6/100 × 6/12)	15,000	By Net Profit before Adjustments	2,37,000
To Manager's Salary A/c (₹ 2,000 × 12)	24,000		
To Manager's Commission A/c [10/110 (₹ 2,37,000 – ₹ 15,000 – ₹ 24,000)]	18,000		
To Net Profit transferred to Profit and Loss Appropriation A/c	1,80,000		
	2,37,000		2,37,000

2. Interest on Partner's Loan, Manager's Salary and Commission are charge against the profit and not appropriations of profits. Hence, these items have been debited to Profit and Loss Account and not to Profit and Loss Appropriation Account.

(*b*) CALCULATION OF PAST ADJUSTED PROFITS

Particulars	2015–16 (₹)	2016–17 (₹)	2017–18 (₹)	2018–19 (₹)
Profits as per Books	1,01,000	1,24,000	1,00,000	1,40,000
Less: Management Cost	24,000	24,000	24,000	24,000
	77,000	1,00,000	76,000	1,16,000
Less: Overvaluation of Closing Stock	...	12,000	...	...
	77,000	88,000	76,000	1,16,000
Add: Overvaluation of Opening Stock	...	...	12,000	...
	77,000	88,000	88,000	1,16,000
Add: Major repair of plant to be treated as Capital Expenditure	...	...	30,000	...
	77,000	88,000	1,18,000	1,16,000
Less: Depreciation on Capital Expenditure @ 10% on time basis by w.d.v. method	...	...	1,000	2,900
	77,000	88,000	1,17,000	1,13,100
Less: Sale Proceeds of Machinery wrongly credited to Profit and Loss A/c	...	11,000	...	...
	77,000	77,000	1,17,000	1,13,100
Add: Depreciation on above Sold Machinery	...	1,000	900	810
Adjusted Profit(P)	77,000	78,000	1,17,900	1,13,910

CALCULATION OF WEIGHTED PROFIT

Year Ended	Profits (₹)	Weight	Weighted Profit (₹)
31st March, 2016	77,000	1	77,000
31st March, 2017	78,000	2	1,56,000
31st March, 2018	1,17,900	3	3,53,700
31st March, 2019	1,13,910	4	4,55,640
Total		10	10,42,340

$$\text{Weighted Average Profit} = \frac{₹\ 10,42,340}{10} = ₹\ 1,04,234$$

Goodwill = Weighted Average Profit × Number of Years' Purchase
= ₹ 1,04,234 × 3 = ₹ 3,12,702.

3. (*a*)

Dr. KARAM'S CAPITAL ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Karam's Executors' A/c (Balancing Figure)	3,65,000	By Balance *b/d*	1,20,000
		By Profit and Loss Suspense A/c (WN 1)	4,000
		By Interest on Karam's Loan A/c	1,000*
		By Karam's Loan A/c	1,00,000
		By Priya's Capital A/c (Goodwill) (WN 2)	90,000
		By Anna's Capital A/c (Goodwill) (WN 2)	30,000
		By Priya's Capital A/c (₹ 20,000 × 3/4)(WN 3)	15,000
		By Anna's Capital A/c (₹ 20,000 × 1/4)(WN 3)	5,000
	3,65,000		3,65,000

*₹ 1,00,000 × 5/100 × 73/365 = ₹ 1,000.

Working Notes:

Calculations will be made from 1st April, 2019 to 12th June, 2019, i.e., for 73 days.

1. *Karam's share of profit till the date of his death:*

   Average Profit of last three years = $\frac{₹\,30{,}000 + ₹\,70{,}000 + ₹\,80{,}000}{3} = ₹\,60{,}000$

   Karam's share of profit = $₹\,60{,}000 \times \frac{73}{365} \times \frac{2}{6} = ₹\,4{,}000$.

2. *Karam's share of Goodwill:*

   Total of Profit of last three years = ₹ 30,000 + ₹ 70,000 + ₹ 80,000 = ₹ 1,80,000

   Firm's Goodwill = Total Profit × No. of years' purchase = ₹ 1,80,000 × 2 = ₹ 3,60,000

   Karam's Share of Goodwill = ₹ 3,60,000 × $\frac{2}{6}$ = ₹ 1,20,000, which is contributed by Priya and Anna in their Gaining Ratio of 3 : 1. Thus,

   Priya's contribution = ₹ 1,20,000 × $\frac{3}{4}$ = ₹ 90,000; and

   Anna's contribution = ₹ 1,20,000 × $\frac{1}{4}$ = ₹ 30,000.

3. *Adjustment of General Reserve and Advertisement Expenditure:*

	₹
General Reserve	1,80,000
Less: Advertisement Suspense A/c	1,20,000
Net Effect	60,000

   Karam's share in net effect of General Reserve & Advertisement Expenditure = ₹ 60,000 × $\frac{2}{6}$ = ₹ 20,000, which is contributed by Priya and Anna in their Gaining Ratio, *i.e.*, 3 : 1.

(*b*)

Dr. REVALUATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Workmen Compensation Claim A/c	12,000	By Provision for Doubtful Debts A/c		2,000
To Investments A/c (WN 1)	30,000	By Loss transferred to:		
		Lokesh's Capital A/c	20,000	
		Mansoor's Capital A/c	12,000	
		Nihal's Capital A/c	8,000	40,000
	42,000			42,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Lokesh ₹	Mansoor ₹	Nihal ₹	Particulars	Lokesh ₹	Mansoor ₹	Nihal ₹
To Profit and Loss A/c	10,000	6,000	4,000	By Balance *b/d*	1,40,000	80,000	50,000
To Revaluation A/c (Loss)	20,000	12,000	8,000	By Lokesh's Capital A/c (WN 2)	...	21,857	...
To Goodwill A/c	20,000	12,000	8,000				
To Mansoor's Capital A/c	21,857	...	8,743	By Nihal's Capital A/c (WN 2)	...	8,743	...
To Bank A/c	...	20,600	...	By Bank A/c (Balancing Figure)	...	...	4,286
To Mansoor's Loan A/c	...	60,000	...				
To Bank A/c (Bal. Fig.)	4,286	...	...				
To Balance *c/d* (WN 3)	63,857	...	25,543				
	1,40,000	1,10,600	54,286		1,40,000	1,10,600	54,286

BALANCE SHEET OF THE NEW FIRM *at at 1st April, 2019*

Liabilities		₹	Assets		₹
Creditors		34,000	Cash at Bank		47,400
Provident Fund		10,000	(₹ 68,000 + ₹ 4,286 – ₹ 4,286 – ₹ 20,600)		
Workmen Compensation Claim		12,000	Stock		38,000
Mansoor's Loan		60,000	Debtors	94,000	
Capital A/cs:			*Less:* Provision for Doubtful Debts	4,000	90,000
Lokesh	63,857		Investments		30,000
Nihal	25,543	89,400			
		2,05,400			2,05,400

Working Notes:

1. *Decrease in the Value of investments adjusted through Investment Fluctuation Reserve and Revaluation Account by passing the following accounting entry:*

Investment Fluctuation Reserve A/c	...Dr.	₹ 20,000	
Revaluation A/c (₹ 50,000 – ₹ 20,000)	...Dr.	₹ 30,000	
To Investments A/c			₹ 50,000

2. *Adjustment of Goodwill:*

Mansoor's Share of Goodwill = ₹ 1,02,000 × $\frac{3}{10}$ = ₹ 30,600, which is to be contributed by Lokesh and Nihal in their gaining ratio, *i.e.*, 5 : 2. Thus,

Lokesh will contribute = ₹ 30,600 × $\frac{5}{7}$ = ₹ 21,857; and

Nihal will contribute = ₹ 30,600 × $\frac{2}{7}$ = ₹ 8,743.

3. *Calculation of Total Capital of the new firm after Mansoor's Retirement:*

A. *Capital of Lokesh after all adjustments:*

= ₹ 1,40,000 – ₹ 10,000 – ₹ 20,000 – ₹ 20,000 – ₹ 21,857 = ₹ 68,143.

B. *Capital of Nihal after all adjustments:*

= ₹ 50,000 – ₹ 4,000 – ₹ 8,000 – ₹ 8,000 – ₹ 8,743 = ₹ 21,257

C. Total capital of the New Firm **(A + B)** = ₹ 89,400

- Lokesh's capital in the New Firm = ₹ 89,400 × $\frac{5}{7}$ = ₹ 63,857
- Nihal's capital in the New Firm = ₹ 89,400 × $\frac{2}{7}$ = ₹ 25,543.

4. JOURNAL OF MAMTA FAB LTD.

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
	Bank A/c	...Dr.		15,00,000	
	To Equity Shares Application A/c				15,00,000
	(Being the application money received on 75,000 shares @ ₹ 20 each)				
	Equity Shares Application A/c	...Dr.		15,00,000	
	To Equity Share Capital A/c (50,000 × ₹ 20)				10,00,000
	To Bank A/c (25,000 × ₹ 20)				5,00,000
	(Being the application money transferred to share capital and surplus refunded)				
	Equity Shares Allotment A/c	...Dr.		20,00,000	
	To Equity Share Capital A/c				20,00,000
	(Being allotment money due on 50,000 shares @ ₹ 40 each)				

Bank A/c	...Dr.	19,60,000	
Calls-in-Arrears A/c (1,500 × ₹ 40)	...Dr.	60,000	
To Equity Shares Allotment A/c			20,00,000
To Calls-in-Advance A/c (500 × ₹ 40)			20,000
(Being the allotment money received on 48,500 shares and both the calls money received on 500 shares in advance)			
Equity Shares First Call A/c (50,000 × ₹ 20)	...Dr.	10,00,000	
To Equity Share Capital A/c			10,00,000
(Being the first call due on 50,000 shares @ ₹ 20)			
Bank A/c	...Dr.	10,30,000	
Calls-in-Arrears A/c (1,000 × ₹ 20)	...Dr.	20,000	
Calls-in-Advance A/c (500 × ₹ 20)	...Dr.	10,000	
To Equity Shares First Call A/c			10,00,000
To Calls-in-Arrears A/c			60,000
(Being the first call money received except on 1,000 shares also allotment money due received)			
Equity Shares Second and Final Call A/c	...Dr.	10,00,000	
To Equity Share Capital A/c			10,00,000
(Being the second and final call due @ ₹ 20 each on 50,000 shares)			
Bank A/c	...Dr.	9,70,000	
Calls-in-Arrears A/c (1,000 × ₹ 20)	...Dr.	20,000	
Calls-in-Advance A/c (500 × ₹ 20)	...Dr.	10,000	
To Equity Shares Second and Final Call A/c			10,00,000
(Being the second and final call money received except on 1,000 shares)			
Equity Share Capital A/c (1,000 × ₹ 100)	...Dr.	1,00,000	
To Forfeited Shares A/c (1,000 × ₹ 60)			60,000
To Calls-in-Arrears A/c (1,000 × ₹ 40)			40,000
(Being the 1,000 shares forfeited for non-payment of first call and second and final call)			
Bank A/c (800 × ₹ 120)	...Dr.	96,000	
To Equity Share Capital A/c (800 × ₹ 100)			80,000
To Securities Premium Reserve A/c (800 × ₹ 20)			16,000
(Being 800 forfeited shares reissued @ ₹ 120 per share as fully paid-up)			
Forfeited Shares A/c (800 × ₹ 60)	...Dr.	48,000	
To Capital Reserve A/c			48,000
(Being the gain on reissue of 800 forfeited shares transferred to Capital Reserve)			

Mamta Fab Ltd.

BALANCE SHEET *as at ...*

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
Shareholders' Funds		
(*a*) Share Capital	1	49,92,000
(*b*) Reserves and Surplus	2	64,000
Total		50,56,000
II. ASSETS		
Current Assets		
Cash and Cash Equivalents	3	50,56,000
Total		50,56,000

Note to Accounts

Particulars	₹	₹
1. Share Capital		
Authorised Capital		
... Equity Shares of ₹ 100 each		...
Issued Capital		
50,000 Equity Shares of ₹ 100 each		50,00,000
Subscribed Capital		
Subscribed and fully paid-up		
49,800 Equity Shares of ₹ 100 each	49,80,000	
Add: Forfeited Shares A/c [₹ 60,000 – ₹ 48,000 (Capital Reserve)]	12,000	49,92,000
2. Reserves and Surplus		
Capital Reserve		48,000
Securities Premium Reserve		16,000
		64,000
3. Cash and Cash Equivalents		
Cash at Bank*		50,56,000

*₹ 15,00,000 – ₹ 5,00,000 + ₹ 19,60,000 + ₹ 10,30,000 + 9,70,000 + ₹ 96,000 = ₹ 50,56,000.

5.

Dr. REVALUATION ACCOUNT *Cr.*

Particulars		₹	Particulars		₹
To Stock A/c		22,500	By Building A/c		25,000
To Furniture A/c		12,500	By Provision for Doubtful Debt A/c:		
To Gain (Profit) on Revaluation transferred to:			Existing	5,000	
Deepika's Capital A/c	10,500		*Less:* Required (5% of ₹ 50,000)	2,500	2,500
Rajshree's Capital A/c	7,000	17,500	By Bad Debts Recovered A/c		20,000
			By Accrued Income A/c		5,000
		52,500			52,500

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Deepika (₹)	Rajshree (₹)	Anshu (₹)	Particulars	Deepika (₹)	Rajshree (₹)	Anshu (₹)
To Goodwill A/c	3,000	2,000	...	By Balance *b/d*	88,000	1,27,000	...
To Advertisement				By Anshu's Loan A/c	...	...	1,50,000
Suspense A/c	3,000	2,000	...	By Premium for Goodwill A/c	36,000	18,000	...
To Bank A/c (Bal. Fig.)	...	10,000	...	By Anshu's Current A/c (WN 3)	24,000	12,000	...
To Balance *c/d* (WN 6)	2,00,000	1,50,000	1,50,000	By Revaluation A/c (Profit)	10,500	7,000	...
				By Bank A/c (Bal. Fig.)	47,500	...	...
	2,06,000	1,64,000	1,50,000		2,06,000	1,64,000	1,50,000

BALANCE SHEET *as at 1st April, 2019*

Liabilities		₹	Assets		₹
Creditors		75,000	Building		55,000
Bank Overdraft		50,000	Furniture		1,12,500
Workmen Compensation Reserve		5,000	Investments		22,500
Investment Fluctuation Reserve		2,500	Debtors	50,000	
Employees' Provident Fund		5,000	*Less:* Provision for Doubtful Debts	2,500	47,500
Workmen Compensation Claim		5,000	Stock (₹ 1,50,000 – ₹ 22,500)		1,27,500
Current A/cs:			Bank Balance (WN 7)		2,36,500
Deepika	1,500		Accrued Income		5,000
Rajshree	750	2,250	Anshu's Current A/c		38,250
Capital A/cs:					
Deepika	2,00,000				
Rajshree	1,50,000				
Anshu	1,50,000	5,00,000			
		6,44,750			6,44,750

Working Notes:

1. *Calculation Sacrificing Ratio and New Ratio:*

   New Share = Old Share – Share surrendered

   Deepika's New Share = 3/5 – (1/3 × 3/5) = 3/5 – 1/5 = 2/5 or 4/10

   Rajshree's New Share = 2/5 – 1/10 = (4 – 1)/10 = 3/10

   Anshu's Share = 1/5 + 1/10 = (2 + 1)/10 = 3/10

   Thus, New Profit-sharing Ratio of Deepika, Rajshree and Anshu = 4/10 : 3/10 : 3/10 = 4 : 3 : 3;

   Sacrificing Ratio of Deepika and Rajshree = 1/5 : 1/10 = 2 : 1.

2. *Calculation of Anshu's Share of Goodwill:*

   $$\text{Average Profit} = \frac{₹\ 2,40,000 + ₹\ 4,65,000 + ₹\ 6,90,000}{3} = ₹\ 4,65,000$$

   Normal Profit = ₹ 3,15,000

   Super Profit = Average Profit – Normal Profit = ₹ 4,65,000 – ₹ 3,15,000 = ₹ 1,50,000

   Firm's Goodwill = Super Profit × No. of years' purchase = ₹ 1,50,000 × 2 = ₹ 3,00,000

   Anshu's Share of Goodwill = ₹ 3,00,000 × 3/10 = ₹ 90,000.

3. *Journal Entries with respect to Goodwill:*

		₹	₹
Bank A/c (60% of ₹ 90,000)	...Dr.	54,000	
To Premium for Goodwill A/c			54,000
Premium for Goodwill A/c	...Dr.	54,000	
To Deepika's Capital A/c			36,000
To Rajshree's Capital A/c			18,000
Anshu's Current A/c (₹ 90,000 – ₹ 54,000)	...Dr.	36,000	
To Deepika's Capital A/c			24,000
To Rajshree's Capital A/c			12,000

4. *For Adjustment of Workmen Compensation Reserve and Investment Fluctuation Reserve:*

	₹
Workmen Compensation Reserve = ₹ 10,000 – ₹ 5,000 (Claim)	5,000
Investment Fluctuation Reserve = ₹ 5,000 – (₹ 25,000 – ₹ 22,500)	2,500
	7,500

Journal Entry with respect to Workmen Compensation Reserve and Investment Fluctuation Reserve:

		₹	₹
Anshu's Current A/c (₹ 7,500 × 3/10)	...Dr.	2,250	
To Deepika's Current A/c (₹ 7,500 × 1/5)			1,500
To Rajshree's Current A/c (₹ 7,500 × 1/10)			750

Note: For adjusting capital of Deepika, Rajshree and Anshu this adjustment is made through Partners' Current Accounts.

5. *Dr.* PARTNERS' CURRENT ACCOUNTS *Cr.*

Particulars	Deepika (₹)	Rajshree (₹)	Anshu (₹)	Particulars	Deepika (₹)	Rajshree (₹)	Anshu (₹)
To Deepika's Capital A/c	...	...	24,000	By Anshu's Current A/c	1,500	750	...
To Rajshree's Capital A/c	...	...	12,000	By Balance *c/d*	...	...	38,250
To Deepika's Current A/c	...	...	1,500				
To Rajshree's Current A/c	...	...	750				
To Balance *c/d*	1,500	750	...				
	1,500	750	38,250		1,500	750	38,250

6. *Adjustment of Capital:*

Total Capital of the Firm = ₹ 1,50,000 × 10/3 = ₹ 5,00,000

Thus, Deepika's New Capital = ₹ 5,00,000 × 4/10 = ₹ 2,00,000;

Rajshree's New Capital = ₹ 5,00,000 × 3/10 = ₹ 1,50,000; and

Anshu's Capital = ₹ 1,50,000.

7. *Dr.* BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,25,000	By Rajshree's Capital A/c	10,000
To Bad Debts Recovered A/c	20,000	By Balance *c/d*	2,36,500
To Premium for Goodwill A/c	54,000		
To Deepika's Capital A/c	47,500		
	2,46,500		2,46,500

6. JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
2017					
April 1	Bank A/c	...Dr.		42,00,000	
	To Debentures Application and Allotment A/c				42,00,000
	(Being the receipt of application money for 40,000 debentures @ ₹ 105 per debentures)				
April 1	Debentures Application and Allotment A/c	...Dr.		42,00,000	
	Loss on Issue of Debentures A/c	...Dr.		4,00,000	
	To 10% Debentures A/c				40,00,000
	To Premium on Redemption of Debentures A/c				4,00,000
	To Securities Premium Reserve A/c				2,00,000
	(Being the issue of 40,000; 10% Debentures at a premium of 5% and redeemable at a premium of 10%)				
April 1	Surplus, *i.e.*, Balance in Statement of Profit and Loss	...Dr.		10,00,000	
	To Debentures Redemption Reserve A/c				10,00,000
	(Being the creation of DRR as per Rule 18(7))				
April 1	Debentures Redemption Investment (DRI) A/c	...Dr.		3,00,000	
	To Bank A/c				3,00,000
	(Being the DRI made equal to 15% of face value of debentures to be redeemed)				
2018					
March 31	Bank A/c	...Dr.		3,00,000	
	To Debentures Redemption Investments A/c				3,00,000
	(Being the DRI realised)				
March 31	10% Debentures A/c	...Dr.		20,00,000	
	Premium on Redemption of Debentures A/c	...Dr.		2,00,000	
	To Debentureholders' A/c				22,00,000
	(Being the amount due on redemption)				
March 31	Debentureholders' A/c	...Dr.		22,00,000	
	To Bank A/c				22,00,000
	(Being the payment made to debentureholders)				
March 31	Debentures Redemption Reserve A/c	...Dr.		5,00,000	
	To General Reserve A/c				5,00,000
	(Being the one-half of DRR transferred to General Reserve on redemption of one-half debentures)				
April 1	Debentures Redemption Investment A/c	...Dr.		3,00,000	
	To Bank A/c				3,00,000
	(Being the DRI made equal to 15% of face value of debentures to be redeemed)				
2019					
March 31	Bank A/c	...Dr.		3,00,000	
	To Debentures Redemption Investments A/c				3,00,000
	(Being the DRI realised)				

March 31	10% Debentures A/c ...Dr. Premium on Redemption of Debentures A/c ...Dr. To Debentureholders' A/c (Being the amount due on redemption)		20,00,000 2,00,000	22,00,000
March 31	Debentureholders' A/c ...Dr. To Bank A/c (Being the payment made to debentureholders)		22,00,000	22,00,000
	Debentures Redemption Reserve A/c ...Dr. To General Reserve A/c (Being the transfer of DRR to General Reserve on redemption of debentures)		5,00,000	5,00,000

7. (*a*)

Dr. REALISATION ACCOUNT *Cr.*

Particulars	₹	Particulars		₹
To Sundry Assets A/c	2,68,625	By Sundry Creditors A/c		75,000
To Bank A/c (Creditors)	75,000	By Employees' Provident Fund A/c		7,500
To Bank A/c (Employees' Provident Fund)	7,500	By Bank A/c (Sundry Assets)		2,32,500
To Pawan's Capital A/c (₹ 2,325 + ₹ 13,550 (WN))	15,875	By Loss on Realisation transferred to:		
		Saurabh's Capital A/c	20,800	
		Gaurav's Capital A/c	15,600	
		Pawan's Capital A/c	15,600	52,000
	3,67,000			3,67,000

Dr. PARTNERS' CAPITAL ACCOUNTS *Cr.*

Particulars	Saurabh (₹)	Gaurav (₹)	Pawan (₹)	Particulars	Saurabh (₹)	Gaurav (₹)	Pawan (₹)
To Realisation A/c (Loss)	20,800	15,600	15,600	By Balance *b/d*	55,000	22,500	60,000
To Bank A/c (Bal. Fig.) (Final Payment)	54,200	21,900	75,275	By Workmen Compensation Reserve A/c	20,000	15,000	15,000
				By Realisation A/c	...	...	15,875
	75,000	37,500	90,875		75,000	37,500	90,875

Dr. BANK ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	1,375	By Realisation A/c (Creditors)	75,000
To Realisation A/c (Assets)	2,32,500	By Realisation A/c (Employees' Provident Fund)	7,500
		By Saurabh's Capital A/c (Final Payment)	54,200
		By Gaurav's Capital A/c (Final Payment)	21,900
		By Pawan's Capital A/c (Final Payment)	75,275
	2,33,875		2,33,875

Working Note: *Calculation of Pawan's Remuneration:*

	₹	₹
A. Total cash available:		
(*i*) Cash at Bank	1,375	
(*ii*) Sale proceeds of assets	2,32,500	2,33,875
B. Total payment (except Pawan's commission of amount distributed and payment to partners):		
(*i*) Payment to Sundry Creditors	75,000	
(*ii*) Payment for Employees' Provident Fund	7,500	
(*iii*) Commission on value of assets realised (1% of ₹ 2,32,500)	2,325	84,825
Payment made to Partners (A – B)		1,49,050

C. Commission on amount distributed to the partners = ₹ 1,49,050 × 10/110 = ₹ 13,550.
Total amount payable to Pawan = ₹ 2,325 + ₹ 13,550 = ₹ 15,875.

(*b*) JOURNAL

Date	Particulars		L.F.	Dr. (₹)	Cr. (₹)
(*i*)	Samar's Capital A/c	...Dr.		1,17,200	
	To Realisation A/c				1,17,200
	(Being the Debtors of ₹ 1,20,000 taken over by Samar)				
	Cash/Bank A/c [₹ 1,24,200 – ₹ 1,20,000) × 50/100]	...Dr.		2,100	
	To Realisation A/c				2,100
	(Being the remaining debtors sold to debt collecting agency)				
(*ii*)	Bhanwar's Capital A/c	...Dr.		72,000	
	To Realisation A/c				72,000
	(Being Sundry Assets book value of ₹ 80,000, *i.e.*, ₹ 72,000 × 100/90 taken by Bhanwar)				
	Pratap's Capital A/c [(₹ 1,17,000 – ₹ 80,000) × 80/100]	...Dr.		29,600	
	To Realisation A/c				29,600
	(Being the remaining Sundry Assets taken over by Pratap)				

8. **Lotus Ltd.**

BALANCE SHEET *as at 31st March, 2019* (*₹ in "000*)

Particulars	Note No.	₹
I. EQUITY AND LIABILITIES		
1. Shareholders' Funds		
(*a*) Share Capital	1	150
(*b*) Reserves and Surplus		90
2. Share Application Money Pending Allotment		5
3. Non-Current Liabilities		
(*a*) Long-term Borrowings	2	200
(*b*) Long-term Provisions		10
4. Current Liabilities		
(*a*) Short-term Borrowings		45
(*b*) Trade Payables		10
(*c*) Other Current Liabilities	3	5
(*d*) Short-term Provisions	4	45
Total		560
II. ASSETS		
1. Non-Current Assets		
(*a*) Fixed Assets—Tangible	5	300
(*b*) Non-Current Investments		100
2. Current Assets		
(*a*) Current Investments		25
(*b*) Inventories		10
(*c*) Trade Receivables		40
(*d*) Cash and Cash Equivalents	6	30
(*e*) Short-term Loans and Advances	7	50
(*f*) Other Current Assets	8	5
Total		560

Notes to Accounts (₹ *in "000*)

Particulars	₹	₹
1. Share Capital		
Authorised Capital		
20,000 Equity Shares of ₹ 10 each		200
Issued Capital		
15,000 Equity Shares of ₹ 10 each		150
Subscribed Capital		
Subscribed and fully paid-up		
15,000 Equity Shares of ₹ 10 each		150
2. Long-term Borrowings		
10% Debentures		200
3. Other Current Liabilities		
Outstanding Expenses		5
4. Short-term Provisions		
Provision for Tax		45
5. Fixed Assets—Tangible		
Cost	350	
Less: Provision for Depreciation (₹ 40 + ₹ 10)	50	300
6. Cash and Cash Equivalents		
Cash and Bank Balance		30
7. Short-term Loans and Advances		
Advance Payment of Tax		50
8. Other Current Assets		
Prepaid Expenses		5

Note: Proposed Dividend for the year ended 31st March, 2019 is ₹ 50,000.

Section B

9. CASH FLOW STATEMENT (*as per AS–3*) *for the year ended 31st March, 2019*

Particulars	₹	₹
A. Cash Flow from Operating Activities		
Net Profit before Tax (WN 1)	1,68,000	
Add: Depreciation on Machinery (WN 2 and 3)	1,10,000	
Loss on Sale of Machinery (WN 2 and 3)	6,000	
Interest on Debentures	15,000	
[(₹ 1,00,000 × 10/100 × 6/12) + (₹ 2,00,000 × 6/12 × 10/100)]		
Operating Profit before Working Capital Changes	2,99,000	
Add: Decrease in Current Assets and Increase in Current Liabilities:		
Inventories	30,000	
Trade Payables	60,000	
	3,89,000	
Less: Increase in Current Assets:		
Trade Receivables	50,000	
Cash Generated from Operations	3,39,000	
Less: Tax Paid	10,000	
Cash Flow from Operating Activities		3,29,0000

B. Cash Flow from Investing Activities		
Purchase of Machinery (WN 2)	(3,40,000)	
Purchase of Non-Current Investments	(20,000)	
Sale of Machinery (WN 2)	24,000	
Cash Used in Investing Activities		(3,36,000)
C. Cash Flow from Financing Activities		
Proceeds from Issue of Equity Shares [₹ 1,00,000 + ₹ 15,000 (Premium)]	1,15,000	
Proceeds from Issue of Debentures [₹ 1,00,000 – ₹ 10,000 (Discount)]	90,000	
Interim Dividend Paid	(25,000)	
Interest on Debentures Paid	(15,000)	
Dividend Paid	(48,000)	
Cash Flow from Financing Activities		1,17,000
D. Net Increase in Cash and Bank Balances (A + B + C)		1,10,000
Add: Opening Balance of Cash and Bank Balances		1,40,000
E. Closing Balance of Cash and Bank Balances		2,50,000

Working Notes:

1. *Calculation of Net Profit before Tax:*

Particulars	₹
Surplus, *i.e.,* Balance in Statement of Profit and Loss (Closing)	2,15,000
Less: Surplus, *i.e.,* Balance in Statement of Profit and Loss (Opening)	1,70,000
Profit for the Year	45,000
Add: Transfer to General Reserve (₹ 1,00,000 – ₹ 80,000)	20,000
Interim Dividend Paid	25,000
Dividend Paid (Proposed Dividend for 2017–18)	48,000
Provision for Tax for 2018–19	30,000
Net Profit before Tax	1,68,000

2. *Dr.* MACHINERY ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Balance *b/d*	6,10,000	By Accumulated Depreciation A/c	70,000
To Bank A/c (Purchase) (Balancing Figure)	3,40,000	By Bank A/c (Sale Proceeds)*	24,000
		By Loss on Sale of Machinery A/c (Statement of Profit and Loss)	6,000
		By Balance *c/d*	8,50,000
	9,50,000		9,50,000

	₹
*Book value on the date of sale (₹ 1,00,000 – ₹ 70,000)	30,000
Less: Loss on Sale (20% of ₹ 30,000)	6,000
Sale Proceeds	24,000

3. *Dr.* ACCUMULATED DEPRECIATION ACCOUNT *Cr.*

Particulars	₹	Particulars	₹
To Machinery A/c	70,000	By Balance *b/d*	1,10,000
To Balance *c/d*	1,50,000	By Statement of Profit and Loss (Depreciation Provided) (Balancing Figure)	1,10,000
	2,20,000		2,20,000

4. Discount on issue of debentures has been adjusted from Securities Premium Reserve as per Section 52(2) of the Companies Act, 2013. The balance of ₹ 5,000 in Securities Premium Reserve is after writing off Discount on Issue of Debentures of ₹ 10,000.
5. Provision for tax of previous year, *i.e.*, ₹ 10,000 has been paid during the Current Year. So, it is substracted from Cash Generated from Operations to arrive at Cash Flow from Operating Activities. Provision for tax of Current Year ₹ 30,000 is added back to the Current Year's profit to arrive at Net Profit before tax.

10. (*a*) (*i*) Debt to Equity Ratio $= \dfrac{\text{Debt/Long-term Debt}}{\text{Equity/Shareholders' Funds}}$

$$= \frac{₹\ 2{,}00{,}000}{₹\ 7{,}00{,}000} = 0.29 : 1.$$

Notes: 1. Debt = 9% Debentures = ₹ 2,00,000.

2. Equity = Equity Share Capital + General Reserve + Statement of Profit and Loss (Cr.)
= ₹ 5,50,000 + ₹ 50,000 + ₹ 1,00,000 = ₹ 7,00,000.

(*ii*) Working Capital Turnover Ratio $= \dfrac{\text{Revenue from Operations}}{\text{Working Capital}}$

$$= \frac{₹\ 15{,}00{,}000}{₹\ 1{,}00{,}000} = 15 \text{ Times.}$$

Note: Working Capital = Current Assets – Current Liabilities
= [Debtors + Cash] – Creditors
= (₹ 1,45,000 + ₹ 55,000) – ₹ 1,00,000 = ₹ 1,00,000.

(*iii*) Return On Investment (ROI) $= \dfrac{\text{Net Profit before Interest and Tax}}{\text{Capital Employed}} \times 100$

$$= \frac{₹\ 2{,}18{,}000}{₹\ 9{,}00{,}000} \times 100 = 24.22\%.$$

Working Notes:

1. *Calculation of Net Profit before Interest and Tax:*

Profit after Interest and Tax = ₹ 1,00,000

Tax paid = 50%

Profit after interest but before Tax $= \dfrac{₹\ 1{,}00{,}000 \times 100}{50} = ₹\ 2{,}00{,}000$

Add: Interest on Debentures (9% of ₹ 2,00,000)	= ₹ 18,000
Net Profit before Interest and Tax	= ₹ 2,18,000

2. Capital Employed = Equity Share Capital + General Reserve + Statement of Profit and Loss + 9% Debentures
= ₹ 5,50,000 + ₹ 50,000 + ₹ 1,00,000 + ₹ 2,00,000 = ₹ 9,00,000.

(*b*) Debt to Total Assets Ratio $= \dfrac{\text{Debt}}{\text{Total Assets}}$

$$= \frac{₹\ 12{,}00{,}000}{₹\ 24{,}00{,}000} = 0.5 : 1.$$

Working Notes:

1. Debt = Long-term Borrowings + Long-term Provisions
   = ₹ 9,00,000 + ₹ 3,00,000 = ₹ 12,00,000.

2. Total Assets = Fixed Assets (Gross) – Accumulated Depreciation + Non-current Investments + Current Assets + Long-term Loans and Advances
   = ₹ 18,00,000 – ₹ 3,00,000 + ₹ 30,000 + ₹ 7,50,000 + ₹ 1,20,000
   = ₹ 24,00,000.

(*c*) Earning Per Share $= \dfrac{\text{Net Profit after Tax and Preference Dividend}}{\text{Number of Equity Shares}}$

$$= \frac{₹\,1{,}00{,}000 - ₹\,20{,}000}{20{,}000} = \frac{₹\,80{,}000}{20{,}000} = ₹\,4 \text{ per share}.$$

Note: Dividend on 10% Preference Shares = 10% of ₹ 2,00,000 = ₹ 20,000.

11. (*a*) Common-size Balance Sheet is a vertical analysis of Balance Sheet in which total assets is taken as 100 and all other figures of Assets, Equity and Liabilities are expressed as percentage of total assets figure.

(*b*) Trade Payables Turnover Ratio $= \dfrac{\text{Net Credit Purchases}}{\text{Average Trade Payables}} = \dfrac{₹\,3{,}60{,}000}{₹\,90{,}000} = 4$ Times.

Net Credit Purchases = Total Purchases – Cash Purchases – Purchases Return
= ₹ 4,20,000 – ₹ 40,000 – ₹ 20,000 = ₹ 3,60,000

Average Trade Payables

$$= \frac{\text{Opening Creditors + Opening Bills Payable + Closing Creditors + Closing Bills Payable}}{2}$$

$$= \frac{₹\,40{,}000 + ₹\,50{,}000 + ₹\,30{,}000 + ₹\,60{,}000}{2} = \frac{₹\,1{,}80{,}000}{2} = ₹\,90{,}000.$$

(*c*) COMPARATIVE STATEMENT OF PROFIT AND LOSS OF SANDALWOOD PRODUCTS LTD.

for the years ended 31st March, 2019 and 2018

Particulars	Note No.	31st March, 2019 (₹)	31st March, 2018 (₹)	Absolute Change (₹)	Percentage Change (%)
I. Revenue from Operations		14,00,000	11,00,000	3,00,000	27.27
II. *Add:* Other Incomes		4,00,000	3,00,000	1,00,000	33.33
III. Total Revenue (I + II)		18,00,000	14,00,000	4,00,000	28.57
IV. *Less:* Expenses		11,00,000	12,00,000	(1,00,000)	(8.33)
V. Profit before Tax (III – IV)		7,00,000	2,00,000	5,00,000	250.00
VI. *Less:* Tax @ 50%		3,50,000	1,00,000	2,50,000	250.00
VII. Profit after Tax (V – VI)		3,50,000	1,00,000	2,50,000	250.00

Net Profit Ratio $= \dfrac{\text{Net Profit after Tax}}{\text{Revenue from Operations}} \times 100$

$$= \frac{₹\,3{,}50{,}000}{₹\,14{,}00{,}000} \times 100 = 25\%.$$