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Financial Accounting

Notes as per IKGPTU Syllabus

Faculty of Commerce, SBS College. Ludhiana

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UNIT-1

Accounting:

1. Identification

Accounting is concerned with financial transactions and events which bring 'about a change in the resources (or wealth) position of the business firm. Such transactions have to be identified first, as and when they occur. It is not difficult because. There will be proof in the form of a bill or receipt (called vouchers). With the help of these bills and receipts identification of a transaction is easy. For example, when you purchase something you get a bill, when you make payment you gets a receipt.

2. Measurement.

These transactions are to be measured or expressed in terms of money, if not done already. Generally, this problem will not arise, because the statement of proof expresses the transaction in terms of money. For example, if ten books are purchased at the rate of Rs. 20 each, then the bill is prepared for Rs. 200. But, if an event cannot be expressed in monetary terms, it will not come under the scope of accounting.

3.Recording

The transactions which are identified and measured are to be recorded in a book called journal or in one of its sub-divisions.

4 Classification

The recorded transactions are to be classified with a view to group transactions of similar nature at one place. The work of classification is done in a separate book called ledger. In the ledger, a separate account is opened for each item so that all transactions relating to it can be brought to one place. For example, all payments of salaries are brought to salaries account.

5. Summarizing

The recording and classification of many transactions will result in a mass of financial data. It is, therefore, necessary to summaries such data periodically (at least once a year), in a significant and meaningful form. The summarization is done in the form of profit and loss account which reveals the profit made or loss incurred, and the balance sheet which reveals the financial position.

6 Analyzing, interpretation and communication:

The summary results will have to be analyzed, interpreted (critically explained) and communicated to interested parties. Accounting information is generally communicated in the form of a 'report'. Big organizations generally present printed reports, called published accounts

Concept of book keeping:

A double-entry bookkeeping system is a set of rules for recording financial information in a financial accounting system in which every transaction or event changes at least two different nominal ledger The name derives from the fact that financial information used to be recorded using pen and ink in paper books – hence "bookkeeping" (whereas now it is recorded mainly in computer systems) and that these books were called journals and ledgers (hence nominal ledger, etc.)
– and that each transaction was entered twice (hence "double-entry"), with one side of the transaction being called a accounts. debit and the other a credit. **It was first codified in the 15th century by the Franciscan Friar, Luca Pacioli.** In deciding which account has to be debited and which account has to be credited, the golden rules of accounting are used. This is also accomplished using the accounting equation**: Equity = Assets − Liabilities**. The accounting equation serves as an error detection tool. If at any point the sum of debits for all accounts does not equal the corresponding sum of credits for all accounts, an error has occurred. It follows that the sum of debits and the sum of the credits must be equal in value. Double-entry bookkeeping is not a guarantee that no errors have been made – for example, the wrong ledger Accounting entries account may have been debited or credited, or the entries completely reversed.

DISTINCTION BETWEEN BOOK-KEEPING AND ACCOUNTING

Book-keeping is a part of accounting and is concerned with the recording of transactions which is often routine and clerical in nature, whereas accounting performs other functions as well, viz., measurement and communication, besides recording. An accountant is required to have a much higher level of knowledge, conceptual understanding and analytical skill than is required of the book-keeper. An accountant designs the accounting system, supervises and checks the work of the book-keeper, prepares the reports based on the recorded data and interprets the reports. Nowadays, he is required to take part in matters of management, control and planning of economic resources.

DISTINCTION BETWEEN ACCOUNTING AND ACCOUNTANCY

Although in practice Accountancy and Accounting are used interchangeably yet there is a thin line of demarcation between them. The word Accountancy is used for the profession of accountants - who do the work of accounting and are knowledgeable persons. Accounting is concerned with 6 recording all business transactions systematically and then arranging in the form of various accounts and financial statements. And it is a distinct discipline like economics, physics, astronomy etc. The word accounting tries to explain the nature of the work of the accountants (professionals) and the word Accountancy refers to the profession these people adopt.

ACCOUNTING EQUATION: BASIC ACCOUNTING TERMS

1. Business

Any legal action that is done in order to earn income or profit is called business. It includes the production of goods and services, purchase and sale of goods and services, banking, insurance, education transportation, and any other trading activity etc.

2. Trade

Purchase and sale of goods and services in order to earn profit is called trade.

3. Profession

Any work done in order to earn profit which necessarily requires prior training and education is called a profession. For example doctors, lawyers, engineers etc..

4. Proprietor

The person who invests capital in the business and entitled to have all profits and losses of the business is called proprietor or owner of the business. The nature of proprietor depends upon the type or nature of the business organization. In a sole trade business, sole trader is a proprietor, in a partnership firm, partners or proprietor and in company shareholders are proprietors.

5. Capital

The amount of cash, goods or assets which is initially invested by proprietor while commencing business is called capital. It is invested to earn profits. In other words, the excess of assets over liability is capital.

6. Assets

All the resources of business having economic value are called assets. These resources help the business to earn a profit and have future value. These are important for running a business and are in the possession of businessman. These are of two types: –

a. Fixed assets

The assets which are used by business for a long time are called fixed assets or non-current assets. These are continued to be used by the business for a period of more than one year. For example:- land ,building ,plant, machinery ,furniture ,vehicle etc.

b. Current assets

The assets which are used up in one year or easily get converted into cash in one year are called current assets. For example:- raw material, finished goods, debtors, cash balance and bank balance etc.

7. Liabilities

The amount which business owes to others is called its liabilities. There is a certain amount which business is under obligation to pay. There are two types of liabilities: –

a. Long-term liabilities

Those liabilities which are usually payable after a period of 1 year. Long-term loans from Financial Institutions, debentures issued by companies etc.

b. Short-term liabilities

These are those which are payable within one year. For example creditors, bank overdrafts etc.

8. Drawings

The amount of cash or goods which is withdrawn by proprietor from business for its private uses is called drawings. It reduces the capital of the business.

9. Goods

The things which are bought and sold by business are called goods. Goods maybe raw material work in progress of finished goods. In accounting, when goods are purchased it is written as

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purchases. When goods are sold it is written as sales. It is written as a stock if remain unsold at the end of the year.

10. Purchases

Goods bought for resale are called purchases. This may be in form of raw material or finished goods. Purchase of assets is not called purchases because assets are not purchased for resale.

11. Sales

When purchase goods are sold in order to earn a profit are called sales. When goods are sold for cash it is called cash sales and goods sold on credit are called credit sales.

12. Purchase return

Goods once purchased by the business, are returned back due to any reason is called purchase return or return outwards.

13. Sales return

Goods once sold to the customer when are returned back by them due to any reason then such goods are called as sales returns or return inwards.

14. Stock

These are those goods which are left unsold in the business at the end of the year. The goods unsold at the end of the accounting year are called closing stock. The same stock is called opening stock at the beginning of a new accounting year.

15. Revenue

These are the amount received by a business for selling goods or services. This amount is received from day to day business activity in the form of rent, interest, commission, discount, dividend etc.

16. Expenses

The cost which business incurs for producing goods and services or for using services is called expenses. These include payments made for wages, salaries, freight, advertisement, rent, insurance etc. In other words, we can say that the cost of earning revenue is an expense.

17. Expenditure

The amount which is paid for increasing profit earning capacity of business is called expenditure. It is of long period nature.

18. Income

That amount which increases the capital of the business is called income. The excess of revenue over expenses is also called income.

19. Loss

When expenses incurred are more than revenue then this excess of expenses is called loss. This reduces the capital of the business.

20. Gain

It is a monetary receipt as a result of business transaction. The excess of revenue over the expenses is called gain.

21. Cost

Total of direct or indirect expenses which are incurred for the production of goods and services is called cost. Like the cost of raw material cost of labor and cost of other services used to make the article is called its total cost.

22. Discount

Concession a rebate allowed by a businessman 2 its customer is called a discount. it may be of two types: –

a. Trade discount

When a trader allows a concession to its customers on the list price, it is known as trade discount. It is not recorded in the books. It is stated in the invoice.

b. Cash discount

When a trader allows a concession to the customer to make payment in cash or by cheque, it is known as cash discount. It is recorded in the books. When cash discount is allowed customer is required to pay the less due amount, so it encourages the customer to pay as early as possible.

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23. Debtor

The person, firm or an organization who takes goods or services on credit from the business are called debtors of the business. In other words, the person, firm or an organization who owes money or Money's worth to the business is called debtor.

24. Creditors

The person, firm or an organization from whom goods or services are purchased on credit by the business are called creditors of the business. The business owes money to them. The amount payable to creditors is a liability of the business.

25. Receivables

The total amount which is to be received in business is called receivables.

26. Payables

The total amount which is to be paid by the business is called payables.

27. Entry

Recording of the transaction in account books is called making an entry or the record of a transaction in books is called an entry.

28. Turnover

The total amount of cash and credit sales during a particular period is called turnover.

29. Insolvent

A person is said to be insolvent when he or she is incapable to meet all his or her liabilities. Such a person has more liability than assets.

30. Bad debts

The amount which could not be recovered from debtors due to his insolvency or disability to pay is called bad debts.

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31. Vouchers

The written document through which financial transactions are recorded in the books is called voucher.

32 Account

A list of all transactions relating to a person, property, income expenses is called into account. It is a tabular statement containing all the transaction of same nature at one place under a common heading in a systematic manner.

33 Debit and credit

Every account has two sides. Left side is called the debit side and the right side is called the credit side. In short, it is Dr. and Cr.

34 Commission

In a business activity, a remuneration is paid to the agent for his services, is called commission.

ACCOUNTING CYCLE:

MEANING OF DOUBLE ENTRY SYSTEM:

Double entry system owes its origin to an Italian merchant named LUCO PACIOLI who wrote the first book entitled 'De Computis et Scripturis' on double entry accounting in the year 1494. Every business transactions has two aspects, i.e. when we receive something, we give something else in return. For example, when we purchase goods for cash, we receive goods and give cash in return. Similarly in a credit sale of goods, goods are given to the customer and the customer becomes debtor for the amount of goods sold by him. This method of writing every transaction in two accounts is known as double entry system of accounting. Of the two accounts one account is given debit while the other account is given credit with an equal amount. Thus, on any date, the total of all debits must be equal to the total of all credits because every debit has a corresponding credit.

Rules for Double Entry System

An account is statement and it is a record of transactions relating to a person, or a firm, or a property, or a liability, or an income or expenditure. There are three kinds of rules for double entry system. They are as follows:-

1. **Personal Accounts**

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Under this statement, a separate account will be prepared for each person. It includes Natural person's account, artificial person's account and representative personal accounts. Some of the examples of personal account are Ram's account, Bank account, any firms account, any companies account, prepaid expense account, outstanding wages account etc.

Rule for personal Account:-

"***Debit the receiver***
Credit the giver"

2. **<u>Real Accounts</u>**

Under the real account, a separate account will create for each class of property or asset. There will have an account relating to a property, an asset or a possession of property. Some of the examples for real account are Cash account, Furniture account, Goodwill account etc.

Rule for Real Account:-

"***Debit what comes in***
Credit what goes out"

3. <u>Nominal Account</u>
4. These includes the expenses and losses or incomes and gains of business. Some of the examples of Nominal account are wages account, discount received account, interest account etc.

Rule for Real Account:-

"***Debit all expenses and losses***
Credit all incomes and gains"

Advantages:

Double entry system is acknowledged as the best method of accounting in the modern world. Following are the main **advantages of double entry system**:

1. Under this method both the aspects of each and every transaction are recorded. So it is possible to keep complete account.
2. Since both the aspects of a transaction are recorded, for each debit there must be a corresponding credit of an equal amount. Therefore, total debits must be equal to total credits. In fact, it is possible to verify the arithmetical accuracy of the books of accounts by ascertaining whether the two sides become equal or not through a process known as trial balance.
3. Under this system profit and loss account can be prepared easily by taking together all the accounts relating to income or revenue and expenses or losses and thereby the result of the business can be ascertained.
4. A balance sheet can be prepared by taking together all the accounts relating to assets and liabilities and thereby the financial position of the business can be assessed.

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5. Under this system mistakes and deflections can be detected - this exerts a moral pressure on the accountant and his staff.
6. Under this system necessary statistics are easily available so that the management can take appropriate decision and run the business efficiently.
7. All the necessary details about a transaction can be obtained quickly and easily.
8. The total amount owed by debtors and the total amount owed to creditors can be ascertained easily.
9. Sale, purchase of goods, stock, revenue, expenses and profit or loss of different years can be compared and the success or failure of the business measured. Thereafter the causes of failure can be found out and necessary remedial measures taken to ensure success of the business.

Disadvantages:

Despite so may advantages of the system, double entry system has some disadvantages which are as follows:

1. Under this method each transaction is recorded in books in two stages (journal and ledger) and two sides (debit and credit). This results in increase of number and size of books of account and creation of complications.
2. It involves time, labor and money. So it is not possible for small concerns to keep accounts under this system.
3. It requires expert knowledge to keep accounts under this system.
4. As the system is complex, there is greater possibility of committing errors and mistakes.

It is clear from the above discussion that the advantages of double entry system far outweigh its disadvantages. So, it is regarded as the best system in the modern world.

The following are the main advantages of double-entry book-keeping:

1. Scientific

The double-entry book-keeping system is a scientific system of book-keeping. Double-entry system has its own set of principles and rules. Under those principles and rules, two aspects of every financial transaction are recorded.

2. Systematic

A systematic technique is followed in recording financial transaction in double-entry book-keeping system. It records financial transactions in a systematic and chronological order with suitable narration of the financial transaction.

3. Complete

Double-entry system is a complete system of book-keeping. It records not only each and every financial transaction, but also each aspect of the transaction.

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4. Accuracy

Double-entry book-keeping system is based on the double-entry principle which means ' for every debit amount there is a corresponding credit amount'. Such a method of debit and credit can help ensure arithmetical accuracy of the recordings of financial transactions.

5. Profit Or Loss

Double-entry book-keeping system helps to ascertain the true profit or loss of a business by preparing the profit and loss account for a given period.

6. Financial Position

Double-entry book-keeping system also helps to reveal information about the financial position of the business by preparing a statement called balance sheet.

7. Control

Double-entry book-keeping system keeps a detailed record of financial transactions. Therefore, the recording of financial transactions in books provides necessary information for the purpose of costs control.

8. Decision Making

Double-entry book-keeping system communicates financial information that is necessary for taking decisions by a business. Double-entry book-keeping system also provides necessary information to different users such as owners, managers and creditors for their decision making purposes.

Advantages of Double Entry System

Double entry system is the most scientific method of keeping accounts. In the modem age, this system is accepted as the best one.

In every organization whether big or small accounts are kept under double entry system.

The advantages of the double entry system are stated in brief;

1. **Complete accounts of transactions:** Double entry system can keep complete accounts of transactions as it is based on dual aspects of each transaction; i.e. debit and credit are recorded simultaneously. For this reason, this system maintains accounts of all parties relating transactions.
2. **Verification of arithmetical accuracy:** Arithmetical accuracy of accounting can be verified through the preparation of trial balance if the accounts are maintained under the double entry system. Under this system, every debit for a certain amount of money will have corresponding credit for an equal amount. For this reason, the total amount of debt will be equal to the total amount of credit. It can be detected through trial balance whether two sides of accounts are equal or not and thereby the arithmetical accuracy of the account is verified.
3. **Determining profit or loss:** Under double entry system, profit or loss of the company for a particular accounting period can be known by preparing an income statement. Since all accounts relating to income and expenditure are maintained properly in the ledger under the double entry system, it becomes convenient to draw income statement at the end of a particular accounting period.

4. **Determining financial position:** Under double entry system, the total assets and liabilities of a business concern are recorded properly. As a result at the closing day of the accounting period balance sheet is prepared with the help of all assets and liabilities. Through this balance sheet financial position of the business concerned can be ascertained.
5. **Knowing asset and liabilities:** Total amount of assets and liabilities can be ascertained if the account is kept under double entry system and it becomes easier to settle liability and assets.
6. **Fixation of the price of commodities:** It becomes easier to fix-up the price of commodities as the accounts are maintained systematically under double entry system.
7. **Submission of income and VAT statements:** Double entry system being the reliable system of keeping accounts the submission of reliable income and VAT statement under it are possible on the basis of which income tax and VAT are fixed and paid.
8. **Comparative analysis:** Under this system of accounting future course of action can be formulated by comparing income -expenditure, asset and liability of the current year with that of the previous year.
9. **Increase in profit:** Under this system of accounting the picture of all incomes or profits is reflected. It can be identified which item is more profitable for a business comparing the items relating to a profit of the current year with that of the previous year. In this way, attempts can be made in order to make more profit.
10. **Expenditure control:** Through comparative analysis expenditure may be controlled curtailing expensive expenditure.
11. **Detection and prevention of forgery:** Under this system of accounts errors or forgery of accounts can easily be detected. As a result moral qualities of an accountant and other employees are upheld.
12. **Supply of information:** This system helps run the business properly supplying necessary information and statistics to the management.
13. **Future reference:** Under this system as every transaction is permanently recorded properly and completely, any necessary information can be detected easily in future.
14. **Easy application:** It is easier to record the transactions properly in the books of accounts following the scientific method of double entry system.
15. **Generally accepted method:** Double entry system being a scientific method is a generally accepted system. The accounts under double entry system become reliable and acceptable to all concerned like income tax authority, creditors etc.
16. **Efficiency evaluation of business concern:** Capacity for earning a profit and repaying liabilities can be evaluated with the help of various ratios relating to accounts from financial statements. For example, creditors or loan givers evaluate the loan repaying capacity of a business concern with the help of current ratio. If the ratio is 2:1 then it is assumed that the loan repaying capacity of the business concern is sound enough.
17. **Timely step for correcting accounting errors:** Accounting errors can properly be detected and taking necessary measures for correction is possible under double entry system of accounting; i.e. before going to next stage the errors of accounting can be corrected.
18. **Utility:** The utility and application of this system in the accounts of all business concerns whether big, medium or small are accepted by all.

Disadvantages or Limitations of Double Entry System

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The double entry system is a generally accepted scientific method. In spite of its many important advantages some limitations of it exist which are stated below:

1. **Increased size of books of accounts:** Under double entry system every transaction is recorded in two sides of two accounts and in two steps (Journal & ledger) of books of accounts.
2. **Complexity in accounting process:** Complexity arises in following rules, principles, techniques, and methods etc. for keeping accounts under the double entry system.
3. **Expensive, time and labor consuming:** Since accounting process under the double entry system is extensive, a good number of books are to be kept and a large number of employees are employed for accounting work. As a result, it requires enough labor, time and money. Therefore, it becomes impossible to follow this system by the small business concerns.
4. **Persons of specialized knowledge required:** The accountant should possess both theoretical and practical knowledge of accounting for proper keeping of accounts under double entry system. An inexperienced person in accounting fails and faces problems in maintaining accounts under this double entry system
5. **Possibility of mistake:** As the accounting process under the double entry system is complex and complicated, the possibility of errors and mistakes cannot be avoided completely.
6. **Limited scope of application:** In a small business organization, daily shopping, a cultural ceremony the application of single entry system of accounting is more popular and advantageous than double entry system.
7. **Problem in maintaining secrecy:** A lot of people are engaged in maintaining accounts under double entry system since the accounting process is very wide and extensive. As a result, a problem arises in maintaining the secrecy of the accounts or business.

Though there arise some problems in maintaining accounts under double entry systems, its advantages and acceptability are so wide and comprehensive that at present age in almost all field accounts is kept under this system.

- **MEANING OF TRIAL BALANCE:**

Trial balance is a statement of debit and credit totals or balances extracted from various accounts in the ledger with a view to test the arithmetical accuracy of the books. This statement is usually prepared at the end of the year and is a connecting link between the ledger accounts and the final accounts.

- **Objective of Trial Balance:**

The following are the main objective of trial balance.

1) To check the arithmetical accuracy of ledger

Trial balance is prepared on the basic of double entry systems of book keeping which states that every debit should have equal and corresponding credit and vice versa, as a result, the sum of the debit totals and credit totals of trial balances must be equal. If the debit total does not agree with the credit total, it is assumed that the transactions are not arithmetically accurate. Thus, one of the important objectives of trial balance is to provide check on the arithmetical accuracy of the financial transactions.

2) To help in locating accounting errors

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since the trial balance indicates whether there is an error committed in journal or ledger, it helps to locate errors as trial balance is the starting point of locating error. Thus locating error is one of the importance objectives of trial balance.

3) To provide the summary of transactions

A business organization performs number of financial transaction during a certain period of time. These transaction themselves cannot depict any picture of financial of the business organizations. To fulfill the purpose, the trial balance is prepared which summarized the financial transactions of business in a certain date.

4) To serve as basic for preparing final accounts

Financial statements are prepared from trial balance. Trial balance contains all ledger accounts, and provides a basis for further processing of accounting data i.e. preparation of financial statements.

5) To facilitate auditors:

Total of all debit balances must be equal to total of all credit balances. Agreement of trial balance assures auditors that all transactions have been recorded in books of accounts.

- **Limitations of Trial Balance:**

Following are the main limitations of trial balance:

1) Trial balance can be prepared only in those concerns where double entry system of accounting is adopted. This system is very costly and cannot be adopted by the small concerns.
2) Though trial balance gives arithmetic accuracy of the books of accounts but there are certain errors which are not disclosed by the trial balance. That is why it is said that trial balance is not a conclusive proof of the accuracy of the books of accounts.
3) If trial balance is not prepared correctly then the final accounts prepared will not reflect the true and fair view of the state of affairs of the business. Whatever conclusions and decisions are made by the various groups of person will not be correct and will mislead such persons.

- **METHODS OF PREPARATION OF TRIAL BALANCE**

  The following are the two methods of preparing trial balance:

1. **Total Method:**
   Under this method, every ledger account is totaled and that total amount (both credit and debit side) is transferred to trial balance. The difference of totals of each ledger account is the balance of that particular account. This method is not commonly used as it cannot help in the preparation of financial statements
2. **Balance Method:**
   Under this method, every ledger account is balanced and those balances only are carried forward to the trial balance. Financial statements are commonly prepared on the basis of this method
3. **Total and Balance Method:**

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As name shows it is combination of above two methods. Under this method, statement of trial balance shows to balance contains the balance in both ways as explained in the above two methods.

- **Rules:**
  Following are the rules to prepare trial balance from Ledger balances:

1. The following balances must be placed in the debit side of the trial balance:
• Asset Accounts
• Expenses Accounts
• Losses
• Drawing
• Cash and Bank Balances

2. The following balances must be placed in the credit side of the trial balance:
• Liabilities Accounts
• Income Accounts
• Profits
• Capital Account

Introduction to Subsidiary Books

Accounting can be a tiresome process. A company has thousands of financial transactions in a year and journalizing them all can get quite bothersome. So some companies choose to prepare subsidiary books, in which we record transactions of a similar nature in chronological order.

Subsidiary Books

Subsidiary books are books of original entry. In the normal course of business, a majority of transactions are either relate to sales, purchases or cash. So we record transactions of the same or similar nature in one place, i.e. the subsidiary book. And we record these transactions in chronological order.

This actually saves a lot of man-hours and tiresome clerical work. Instead of journalizing each entry, they are recorded into various subsidiary books. Think of your subsidiary book as sub-journals that record only one type of transaction.

There is no separate entry for these transactions in the general ledger. The posting to the Ledger Accounts is done from the subsidiary book itself. This method of recording is known as the Practical System of Accounting or sometimes the English System.

One thing to remember is that such a system does not violate the rules of Double Entry System. We have still recorded the transactions according to this system. All transactions are still affecting two accounts. Only instead of a journal, we are using subsidiary books as the books of original entry.

INTRODUCTION TO FINANCIAL ACCOUNTING:

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ACCOUNTING TO FINANCIAL ACCOUNTING:

1. Financial Accounting: Financial accounting involves recording and categorizing transactions for business. This data is generally historical, meaning it's from the past.It also involves generating financial statements based on these transactions. All financial statements, such a balance sheet and income statement, must be prepared according to the generally accepting accounting principles (GAAP), according to Accounting verse. Public companies have to follow a set of rules set out by the government (this is the Securities and Exchange Commission in the U.S.).Financial accounting is performed to conform to external regulations and is not for internal employees to analyze and make financial decisions—managerial accounting is used for this purpose.

2. Cost Accounting Cost accounting is considered a type of managerial accounting. Cost accounting is most commonly used in the manufacturing industry, an industry that has a lot of resources and costs to manage. It is a type of accounting used internally to assess a company's operations.Cost accounting concerns itself with recording and analyzing manufacturing costs. It looks at a company's fixed (unchanging and constant costs, like rent) and variable costs (changing costs, like shipping charges) and how they affect a business and how these costs can be better managed, according to Accounting Tools.

3. Auditing: There are two types of auditing: external and internal auditing. In external auditing, an independent third party reviews a company's financial statements to make sure they are presented correctly and comply with GAAP.Internal auditing involves evaluating how a business divides up accounting duties, who is authorized to do what accounting task and what procedures and policies are in place. Internal auditing helps a business zero in on fraud, mismanagement and waste or identify and control any potential weaknesses in its policies or procedures, according to Accounting Tools.

4. Managerial Accounting: Also known as management accounting, this type of accounting provides data about a company's operations to managers. The focus of managerial accounting is to provide data that managers need to make decisions about a business's operations, not comply strictly with GAAP.Managerial accounting includes budgeting and forecasting, cost analysis, financial analysis, reviewing past business decisions and more. Cost accounting is a type of managerial accounting.Fresh Books has simple online accounting software for small business that makes it easy to produce these reports.

5. Accounting Information Systems: Known as AIS for short, accounting information systems concerns itself with everything to do with accounting systems and processes and their construction, installment, application and observation. This can include accounting software management and the management of bookkeeping and accounting employees.

6. Tax Accounting: Tax accounting involves planning for tax time and the preparation of tax returns. This branch of accounting aides businesses be compliant with regulations set up by the IRS.Tax accounting also helps businesses figure out their income tax and other taxes and how to legally reduce their amount of tax owing. Tax accounting also analyzes tax-related business decisions and any other issues related to taxes.

7. Forensic Accounting: This specialized accounting service is trending in accounting and is becoming increasingly popular. Forensic accounting focuses on legal affairs such as inquiry into fraud, legal cases and dispute and claims resolution.Forensic accountants need to reconstruct financial data when the records aren't complete. This could be to decode fraudulent data or convert a cash accounting system to accrual accounting. Forensic accountants are usually consultants who work on a project basis, according to Accounting Tools.

8. Fiduciary Accounting: This branch of accounting centers around the management of property for another person or business. The fiduciary accountant manages any account and activities related to the administration and guardianship of property.Fiduciary accounting covers estate accounting, trust accounting and receivership (the appointing of a custodian of a business's assets during events such as bankruptcy).

Basis of Accountings: There are two types of accounting methods: cash and accrual. Most small businesses can use either method. Businesses that are corporations or have gross revenue over $5 million per year are required to use the accrual method, according to the IRS.

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CASH METHOD: The cash accounting method is the simplest method. When money comes in, revenue is recorded. When money goes out, an expense is recorded, according to the Houston Chronicle**.**

ACCRUAL METHOD: In accrual accounting, revenue is recorded when it's *earned*, not when money actually comes in. A company can perform a service and bill the client. Even if the client hasn't paid yet, revenue is still recorded in the books.Expenses are matched to revenue in accrual accounting, meaning they're recorded at the same time as revenue. So if a house painter has to buy paint for a job, the total income for the job and the cost of the paint are recorded in the books at same time. It doesn't matter exactly when the paint was purchased.

Advantages of Accounting:

1. Permanent recording of transactions

In a business organization, a huge number of transactions occur. It is not possible for anybody to keep it in mind for long. The permanent keeping of accounts is possible since transactions are recorded systematically.A businessman at any time can easily collect information from these accounts.

2. Ascertainment of profit and loss of business

At the end of a particular accounting period, profit and loss of a business concern can be ascertained by preparing an income statement.

3. Exhibition of total financial position

The total financial position of a business concern i.e. total capital, total payable, total receivable, total assets, and cash in hand and a bank can be known by preparing a balance sheet at a particular date.

3. Cost control

Head wise amount of income and expenditure can be known if accounts are maintained systematically and properly. As a result, excess expenditure or misuse can be controlled and expenditures are controlled keeping consistency with the income.

4. Helping management of business

Planning regarding income and expenditure becomes easier through proper and accurate accounts keeping.

Appropriate steps can be adopted identifying profitable and non-profitable items of income and expenditure. Besides, sales price and income tax are determined through accounts.

5. Prevention of errors; fraud and forgery

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Prevention and detection of fraud and forgery are possible by keeping accounts systematically. Arithmetical accuracy of accounts is also tested by preparing trial balance. And timely steps are possible, if necessary, like rectifying the errors in accounts.

6. Comparative analysis

Current year's profit-loss and property-liabilities can' be compared with previous year's matters of similar nature if accounts are kept systematically and accurately. This helps the businessman in formulating rules and taking decisions.

7. Helping settlement of the dispute

The misunderstanding may arise among the interested parties in a business concern i.e. debtors, creditors, investors, owners, employees etc. Systematic and accurate accounts' keeping minimizes the possibility of such unwanted developments.

8. Helping determination of tax

The systematic keeping of accounts in accepted principles helps to present reliable income tax statements based on which income tax is determined.

9. Keeping accounts regarding VAT

Accounting records all transactions of VAT systematically and helps to determine VAT.

10. Knowing cash position

In cash book, all cash receipts and cash payment are recorded. Day-to-day cash receipts, payments and cash in hand and cash at bank can be known from cash book. Information regarding cash in hand is very essential in running business.

11. Control over assets and liabilities

A businessman is to acquire various types of property and assets to run the business profitably and thereby he is to face a lot of liabilities.

The exact position of the assets and liabilities can be ascertained by maintaining accounts properly. As a result, a businessman can take necessary steps to control decrease of assets and an increase of liabilities.

12. Authentic and presentable documents before the court

In settlement of disputes among interested parties of business, cases are filed in the court. Accounts kept properly can be presented before the court as documentary evidence.

13 Helping in the valuation of assets and liabilities at the time of winding up the business and in case of insolvency of the owner

In both cases of winding up and insolvency, authorities concerned can determine the value of various assets and liabilities properly from the books of accounts maintained systematically and accurately. Under this situation, accurate valuation of assets and liabilities is very essential.

14. Helping in fixation of the sale price of a business

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For any reason, the question of selling the whole business or a. part may arise in course of time. In this situation, an accurate selling price can be determined on the basis of properly kept accounts.

15. Testing arithmetical accuracy of accounts

Under double entry system of accounting errors and frauds in accounts, if any, can be detected easily by preparing a trial balance and appropriate measures can be taken in time for rectification.

16. Matching of income and expenditure

Overall development of a business is possible through matching income and expenditure if accounts are kept properly.

17. Advantages in taking a loan

Taking loan becomes easier if accounts are kept properly. The loan giver sanctions loan on the basis of accounting information.

18. Settlement of outstanding debts receivable

Properly kept accounts help in preparing the statement of outstanding debts and receivable and thereby measures can be adopted for timely payment of debts and collection of receivables.

ACCOUNTING CONCEPTS AND CONVENTIONS

The term 'Concept' is used to connote the accounting postulates, i.e., necessary assumptions and ideas which are fundamental to accounting practice. In other words, fundamental accounting concepts are broad general assumptions which underline the periodic financial statements of business enterprises. The reason why some of the these terms should be called concepts is that they are basic assumptions and have a direct bearing on the quality of financial accounting information. The term 'convention' is used to signify customs or tradition as a guide to the preparation of accounting statements. The following are the important accounting concepts and conventions:

ACCOUNTING CONCEPTS

The more important accounting concepts are briefly described as follows:

1. **Separate Business Entity Concept.**

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In accounting we make a distinction between business and the owner. All the books of accounts records day to day financial transactions from the view point of the business rather than from that of the owner. The proprietor is considered as a creditor to the extent of the capital brought in business by him. For instance, when a person invests Rs. 10 lakh into a business, it will be treated that the business has borrowed that much money from the owner and it will be shown as a 'liability' in the books of accounts of business. Similarly, if the owner of a shop were to take cash from the cash box for meeting certain personal expenditure, the accounts would show that cash had been reduced even though it does not make any difference to the owner himself. Thus, in recording a transaction the important question is how does it affects the business? For example, if the owner puts cash into the business, he has a claim against the business for capital brought in

2. **Money Measurement Concept.**

In accounting, only those business transactions are recorded which can be expressed in terms of money. In other words, a fact or transaction or happening which cannot be expressed in terms of money is not recorded in the accounting books. As money is accepted not only as a medium of exchange but also as a store of value, it has a very important advantage since a number of assets and equities, which are otherwise different, can be measured and expressed in terms of a common denominator

3. **Dual Aspect Concept.**

Financial accounting records all the transactions and events involving financial element. Each of such transactions requires two aspects to be recorded. The recognition of these two aspects of every transaction is known as a dual aspect analysis. According to this concept every business transactions has dual effect. For example, if a firm sells goods of Rs. 10,000 this transaction involves two aspects. One aspect is the delivery of goods and the other aspect is immediate receipt of cash (in the case of cash sales). Infect, the term 'double entry' book keeping has come into vogue because for every transaction two entries are made. According to this system the total amount debited always equals the total amount credited. It follows from 'dual aspect concept' that at any point in time owners' equity and liabilities for any accounting entity will be equal to assets owned by that entity. This idea is fundamental to accounting and could be expressed as the following equalities:

(1) Assets = Liabilities + Owners Equity ....

(2) Owners Equity = Assets - Liabilities .... The above relationship is known as the 'Accounting Equation'. The term 'Owners Equity' denotes the resources supplied by the owners of the entity while the term 'liabilities' denotes the claim of outside parties such as creditors, debenture-holders, bank against the assets of the business. Assets are the resources

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owned by a business. The total of assets will be equal to total of liabilities plus owners capital because all assets of the business are claimed by either owners or outsiders.

4. **Going Concern Concept.**

Accounting assumes that the business (9) entity will continue to operate for a long time in the future unless there is good evidence to the contrary. The enterprise is viewed as a going concern, that is, as continuing in operations, at least in the foreseeable future. In other words, there is neither the intention nor the necessity to liquidate the particular business venture in the predictable future.

5. **Accounting Period Concept.**

This concept requires that the life of the business should be divided into appropriate segments for studying the financial results shown by the enterprise after each segment.

6. **Cost Concept.**

The term 'assets' denotes the resources land building, machinery etc. owned by a business. The money values that are assigned to assets are derived from the cost concept. According to this concept an asset is ordinarily entered on the accounting records at the price paid to acquire it. For example, if a business buys a plant for Rs. 5 lakh the asset would be recorded in the books at Rs. 5 lakh, even if its market value at that time happens to be Rs. 6 lakh. Thus, assets are recorded at their original purchase price and this cost is the basis for all subsequent accounting for the business. The assets shown in the financial statements do not necessarily indicate their present market values. The term 'book value' is used for amount shown in the accounting records.

7. **The Matching concept.**

This concept is based on the accounting period concept. In reality we match revenues and expenses during the accounting periods. Matching is the entire process of periodic earnings measurement, often described as a process of matching expenses with revenues. In other words, income made by the enterprise during a period can be measured only when the revenue earned during a period is compared with the expenditure

8. **Accrual Concept.**

It is generally accepted in accounting that the basis of reporting income is accrual. Accrual concept makes a distinction between the receipt of cash and the right to receive it,

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and the payment of cash and the legal obligation to pay it. This concept provides a guideline to the accountant as to how he should treat the cash receipts and the right related thereto. Accrual principle tries to evaluate every transaction in terms of its impact on the owner's equity. The essence of the accrual concept is that net income arises from events that change the owner's equity in a specified period and that these are not necessarily the same as change in the cash position of the business. Thus it helps in proper measurement of income.

9. **<u>According to realization concept</u>**

Revenue is recognised when sale is made. Sale is considered to be made at the point when the property in goods passes to the buyer and he becomes legally liable to pay. This implies that revenue is generally realized when goods are delivered or services are rendered. The rationale is that delivery validates a claim against the customer.

ACCOUNTING CONVENTIONS

1. **<u>Convention of Materiality.</u>**

   Materiality concept states that items of small significance need not be given strict theoretically correct treatment. Infact, there are many events in business which are insignificant in nature. The cost of recording and showing in financial statement such events may not be well justified by the utility derived from that information. For example, an ordinary calculator costing Rs. 100 may last for ten years. However, the effort involved in allocating its cost over the ten year period is not worth the benefit that can be derived from this operation. The cost incurred on calculator may be treated as the expense of the period in which it is purchased. Similarly, when a statement of outstanding debtors is prepared for sending to top management, figures may be rounded to the nearest ten or hundred.

2. **<u>Convention of Conservatism.</u>**

   This concept requires that the accountants must follow the policy of ''playing safe" while recording business transactions and events. That is why, the accountant follow the rule anticipate no profit but provide for all possible losses, while recording the business events. This rule means that an accountant should record lowest possible value for assets and revenues, and the highest possible value for liabilities and expenses. According to this concept, revenues or gains should be recognised only when they are realised in the form of cash or assets (i.e. debts) the ultimate cash realisation of which can be assessed with reasonable certainty. Further, provision must be made for all known liabilities, expenses and losses, Probable losses regarding all contingencies should also be provided for. 'Valuing the stock in trade at market price

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or cost price whichever is less', 'making the provision for doubtful debts on debtors in anticipation of actual bad debts', 'adopting written down value method of depreciation as against straight line method', not providing for discount on creditors but providing for discount on debtors', are some of the examples of the application of the convention of conservatism

3. **Convention of Consistency.**

The convention of consistency requires that once a firm decided on certain accounting policies and methods and has used these for some time, it should continue to follow the same methods or procedures for all subsequent similar events and transactions unless it has a sound reason to do otherwise. In other worlds, accounting practices should remain unchanged from one period to another. For example, if depreciation is charged on fixed assets according to straight line method, this method should be followed year after year. Analogously, if stock is valued at 'cost or market price whichever is less', this principle should be applied in each subsequent year.

ACCOUNTING STANDARDS

The accounting concepts and conventions discussed in the foregoing pages are the core elements in the theory of accounting. These principles, however, permit a variety of alternative practices to co-exist. On account of this the financial results of different companies cannot be compared and evaluated unless full information is available about the accounting methods which have been used. The lack of uniformity among accounting practices have made it difficult to compare the financial results of different companies. It means that there should not be too much discretion to companies and their accountants to present financial information the way they like. In other words, the information contained in financial statements should conform to carefully considered standards. Obviously, accounting standards are needed.

OBJECTIVES OF ACCOUNTING SATANADRD

a) Provide a basic framework for preparing financial statements to be uniformly followed by all business enterprises,

b) Make the financial statements of one firm comparable with the other firm and the financial statements of one period with the financial statements of another period of the same firm,

c) Make the financial statements credible and reliable, and

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d) Create general sense of confidence among the outside users of financial statements.

In order to harmonize varying accounting policies and practices, the Institute of Chartered Accountants of India (ICAI) formed the Accounting Standards Board (ASB) in April, 1977. ASB includes representatives from industry and government. The main function of the ASB is to formulate accounting standards. This Board of the Institute of Chartered Accountants of India has so far formulated around 27 Accounting Standards, the list of these (17) accounting standards is furnished. Regarding the position of accounting standards in India, it has been stated that the standards have been developed without first establishing the essential theoretical framework. As a result, accounting standards lack direction and coherence. This type of limitation also existed in UK and USA but it was remedied long back. Hence, there is an emergent need to make an attempt to develop a conceptual framework and also revise suitably the Indian Accounting Standards to reduce the number of alternative treatments.

Ind AS have many benefits, some of which are discussed below:

• Wider acceptability:

Since Ind AS are converged form of IFRS which are widely acceptable and will give confidence to the user of financial statements.

• Comparability of Financials:

Financial statements prepared using Ind AS are easily comparable with the financial statements prepared by companies of other countries.

• Changes in standards as per economic situations:

Principles of Ind AS are revised/modified in case there is any major change in economy. Ind AS 29 is 'Financial Reporting in hyperinflationary Economies' which deals with situations related to inflation.

• Attracts Foreign Investment:

Adopting Ind AS may attract foreign investors to invest in Indian Companies as that will ensure better comparability with similar companies across the globe.

• Saves financial statement preparation cost:

For multinational companies, it will be beneficial as it will be able to use the same accounting standards in all the markets in which they operate. This will save preparation costs of aligning financial statements of Indian company with other operations.

Indian Accounting Standards

Accounting Standard 1 : Disclosure of Accounting Policies

Accounting Standard 2 : Valuation of Inventories

Accounting Standard 3 : Cash Flow Statements

Accounting Standard 4 : Contingencies and Events Occurring after the Balance Sheet Date

Accounting Standard 5 : Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies

Accounting Standard 6 : Depreciation Accounting

Accounting Standard 7 : Construction Contracts

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Accounting Standard 8 : (Deleted)
Accounting Standard 9 : Revenue Recognition
Accounting Standard 10 : Property, Plant and Equipment
Accounting Standard 11 : The effects of changes in Foreign Exchange Rates
Accounting Standard 12 : Accounting for Government Grants
Accounting Standard 13 : Accounting for Investments
Accounting Standard 14 : Accounting for Amalgamations
Accounting Standard 15 : Employee benefits
Accounting Standard 16 : Borrowing Costs
Accounting Standard 17 : Segment Reporting
Accounting Standard 18 : Related Party Disclosures
Accounting Standard 19 : Leases
Accounting Standard 20 : Earnings Per Share
Accounting Standard 21 : Consolidated Financial Statements
Accounting Standard 22 : Accounting for Taxes on Income
Accounting Standard 23 : Accounting for Investments in Associates in Consolidated Financial Statements
Accounting Standard 24 : Discontinuing Operations
Accounting Standard 25 : Interim Financial Reporting
Accounting Standard 26 : Intangible Assets
Accounting Standard 27 : Financial Reporting of Interest in Joint Ventures
Accounting Standard 28 : Impairment of Assets
Accounting Standard 29 : Provisions Contingent Liabilities and Contingent Assets
Accounting Standard 30 : Financial Instruments : Recognition and Measurements*
Accounting Standard 31 : Financial Instruments : Presentation*
Accounting Standard 32 : Financial Instruments : Disclosures*

CAPTIAL AND REVEUNE EXPENDITURE

Capital Expenditure:

It consists of expenditure, the benefit of which is not fully consumed in the accounting period but spread over several periods. Any expenditure, which is undertaken for the purpose of increasing profit either by way of increasing earring capacity or by decreasing costs, is capital expenditure.

Capital expenditure is one which

(a) increase in quantity of fixed assets

(b) increase in quality of fixed assets and

(c) Replacement of fixed assets.

An expenditure cannot be said to be a capital expenditure only because 1] the amount is large

2] the amount paid in lump-sum

3] the receiver of amount is going to treat it for purchase of fixed asset

Examples: plant and machinery, motor car, lease, trademark, patent, copy right, Goodwill, expansion or erection of machinery, expansion expenditure(increasing seating capacity in theatre), experiment expenses, development expenses in case of mines, etc.

Revenue Expenditure:

It constitutes the expenditure incurred for the payment of money for services of whatever type such rent, salaries, commission, repair, carriage etc. It is incurred for carrying on business and maintains assets in their existing conditions. It doesn't increase the profit earning capacity but merely maintains it at existing level. It is used in the sense of immediate or short term importance.

Examples: cost of goods purchased, administrative expenses (rent, salary.etc.), manufacturing (oil, fuel, etc,) selling and distribution expenses (Commission,

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discount, advertising, etc.), Depreciation, interest on loan, loss on sale of assets, etc.

Deferred Revenue Expenditure:

It involves a heavy expenditure of revenue nature and it is not prudent and desirable to write it off from the profit of one financial year and hence a pert is taken to profit and loss account and the balance is shown on the assets side of the balance sheet. The benefit from such expenditure may spreads over for 3 to 5 years.

Example: preliminary expenses, brokerage on issue of shares or debentures, exceptional repairs, heavy advertisement cost, research and development expenses, special type of losses, etc.

Capital Expenditure	Revenue expenditure
It is non –recurring in nature	It is recurring in nature
It is heavy in volume	It is modest in volume
It involves of acquisition of asset	It incurred in the conduct of the business
Decision regarding capital expenditure is taken by top management	Decision regarding revenue expenditure is taken by middle and lower level management
It represent assets of the business and appears in the balance sheet	It is day today expenditure and appear in the profit and loss account
This expenditure is not deductible from income for Incometax purpose	This expenditure is deductible from income for Incometax purpose
This expenditure is met out of loans, funds borrowed from outside, capital	This expenditure is met out of short term funds, sale proceeds
It increases the earning capacity of the Business	It maintains the present capacity of the business

CAPITAL RECEIPTS Vs REVENUE RECEIPTS

CAPITAL RECEIPTS	REVENUE RECEIPTS

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It includes capital contributed by the proprietors, partners, shareholders, loans from bank, financial institutions, sale proceeds of fixed assets	It includes receipts such cash from sales, discount received, commission received, interest on investment, etc
These are the money received by the enterprise for the purpose of establishing, expanding or modernizing its business.	Receipts which are obtained during the course of trading and operations are revenue receipts
These receipts are not directly credited to profit and loss account	This receipts are directly credited to profit and loss account.

Objective Type questions

1. Capital expenditure is any expenditure benefiting.................................... period

A] current	B]future	C] past	D] more than one accounting period

2. The cost of housing plot purchased for sale is a .... expenditure

A] Capital	B] revenue	C] deferred revenue	D] miscellaneous

3. Amount spent on asset to make it useable conditions is debited to

A] profit and loss Account	B] Income and expenditure account	C] Assets account	D] Receipts and payment account

4. A heavy expenditure incurred in introducing a new product into the market is

A] Capital expenditure	B] revenue expenditure	C] deferred revenue	D] miscellaneous

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		expenditure	

5. Rs.200000 spent as traveling expenses by the directors to go to abroad for purchase of capital asset is

A] Capital expenditure	B] revenue expenditure	C] deferred revenue expenditure	D] miscellaneous

6. Rs.20000 spent on the repairs of machine is

A] Capital expenditure	B] revenue expenditure	C] deferred revenue expenditure	D] miscellaneous

7. Rs.25000 spent on overhauling the second hand machinery

A] Capital expenditure	B] revenue expenditure	C] deferred revenue expenditure	D] miscellaneous

8. White washing expenses is a

A] Capital expenditure	B] revenue expenditure	C] deferred revenue expenditure	D] miscellaneous

9. TVS limited received a subsidy of Rs 1 crore from the central government is a

A] Revenue receipt	B] Revenue expenditure	C] Capital expenditure	D] Capital receipt

10. A debt recorded as bad in the earlier year recovered during the year is a

A] Revenue receipt	B] Revenue expenditure	C] Capital expenditure	D] Capital receipt

11. Failure to make distinction between capital and revenue items will result in

A] under trading	B] overtrading	C] Receipts and payment A/c being false and misleading	D] Final accounts being false and misleading

12. Wages paid for installation of machinery included in the wages will affect

A] wages account	B] wages and Machinery	C] Profit and loss account	D] Machinery account

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	Account		

13. If an old machinery whose book value is Rs.4000 and is sold at Rs.4200

A] Rs.4200 treated as capital receipt	B] Rs. 4200 treated as revenue receipt	C] Rs.4000 treated as capital balance ignore	D] Rs.4000 treated as capital & 200 treated as revenue receipt

14. Consider the following - cost of extension of building Rs.250000/- cost of improvement of electrical wiring system Rs.19000, cost of repair to building Rs.25000 and whitewashing charges Rs.5000/- what is the amount of revenue expenditure?

A] Rs.30000/-	B] Rs.299000/-	C] Rs. 44000/-	D] Rs.49000/-

15. Donation received by a non-trading concern is normally

A] Revenue receipt	B] Revenue expenditure	C] Capital expenditure	D] Capital receipt

Problems on accounting equations

Assets = Capital + liabilities
Owner's equity or capital = Assets – liabilities
Gross profit = Sales – cost of goods sold
Cost of goods sold = Opening stock + Net purchases+ Direct expenses – Closing Stock
Net profit = Gross profit – indirect expenses

16. Goods purchased Rs.100000/- Sales Rs.90000/- Margin 20% on sales. Closing stock is

A] Rs.10000/-	B] Rs.25000/-	C] Rs. 28000/-	D] Rs.30000/-

17. Soman starts business with a capital of Rs.45000. He purchases goods on credit worth Rs.5000. How these transactions can be expressed in an Accounting Equation

A] 5000=50000-45000	B] 50000 = 50000	C] 50000 = 45000+5000	D] 45000 = 50000-5000

18. The capital at the beginning is Rs.50000. Goods withdrawn during the year is Rs.16000 and additional capital introduced during the year is Rs.20000. The capital at the end of the year Rs.52000. The net effect of the transactions is

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A] loss Rs.2000/-	B] profit Rs.2000/-	C] profit Rs. 30000/-	D] loss Rs.4000/-

19. In a balance sheet, if total assets amount to Rs.80000/- while the liabilities to outsiders amount to Rs.29000/- and profit during the year Rs.11000/-. What the amount of capital?

A] Rs.40000/-	B] Rs.51000/-	C] Rs. 80000/-	D] Rs.72000/-

20. 25. Ascertain the cost of goods sold from the following: Opening stock 8500, purchase 30700, direct expenses 4800 indirect expenses5200 closing stock 9000

A] 3500	B] 35000	C] 29800	D] 30000

ANSWSERS

1] d	2] b	3] c	4] c	5] a	6] b	7] a	8] b	9] d	10] a
11] d	12] b	13] d	14] a	15] d	16] b	17] c	18] a	19] a	20] B

What is a Financial Statement?

A financial statement is the combination of the three major reports on a business. It will contain the cash flow statement, the income statement and the balance sheet of the business. All three together produce an overall picture of the health of the business.

Why is a Financial Statement Important?

The answer to this question is in the definition; it is the complete report on the health of the business taking in cash flow, income and the balance sheet. The financial statement determines if a business has to ability to repay loans, if it has the cash flow to meet bills and purchase stock. It will also tell from where the business is generating cash and where the cash goes.

The financial statement tells if the business is profitable, if it will stay profitable and if there are any large problems looming, such as a continuous drop in sales over time. Reading the financial statement will give an overall view of the condition of the business and if there are any warnings signs of possible future problems. A bank or other such institution will look to the financial statement as the first indicator of how the business is performing and if there is a need for further investigation.

When Will a Company Prepare a Financial Statement?

Every business will ready a financial statement to go with their end of year results, to give interested parties the overview of how the business is functioning. If a business is looking to

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increase credit facilities with a bank or trying to raise capital for an expansion, it will produce a financial statement for the end of a fiscal quarter or the most recent month. When preparing a financial statement for such purposes the best practice is to use general accountancy language, understood by all parties. A financial statement that may accompany an end of year report and read just by employees, is often in terms familiar to just those involved.

Often a government body may request a financial statement for tax purposes and the company will need to produce one of high quality using generally accepted guidelines. A bank or investors may also request a financial statement without warning, if they are concerned about the profitability or otherwise of the company. For these reason alone it is vital for any business to keep good and current records so that a financial statement is easy and quick to produce

What is a Trading Account?

A trading account helps in determining the gross profit or gross loss of a business concern, made strictly out of trading activities. Trading involves buying and selling activities. In the trading account, the cost of goods sold is subtracted from net sales for the period to calculate gross profit. Only direct revenue and direct expenses are considered in it. Trading account is prepared mainly to know the profitability of the goods bought by the businessman.

The difference between selling price and cost of goods sold is the earning for the businessman, which is also known as gross profit. Whereas, net profit means all revenues minus all expenses including the cost of goods sold, the selling, general and administrative expenses, and the non-operating expenses. Thus in order to calculate the gross earning, it is necessary to know the cost of goods sold and sales figures. Also,

Gross Profit = Sales – COGS (Sales + Closing Stock) – (Stock in the beginning + Purchases + Direct Expenses)

Items included on the debit side are opening stock, purchases, and direct expenses and on the credit side are sales and closing stock. The resultant figure is either gross profit or gross loss.

What Is a Profit and Loss Statement (P&L)?

The profit and loss (P&L) statement is a financial statement that summarizes the revenues, costs, and expenses incurred during a specified period, usually a fiscal quarter or year. The P&L statement is synonymous with the income statement. These records provide information about a company's ability or inability to generate profit by increasing revenue, reducing costs, or both. Some refer to the P&L statement as a statement of profit and loss, income statement, statement of operations, statement of financial results or income, earnings statement or expense statement.

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- The P&L statement is a financial statement that summarizes the revenues, costs, and expenses incurred during a specified period.
- The P&L statement is one of three financial statements every public company issues quarterly and annually, along with the balance sheet and the cash flow statement.
- It is important to compare P&L statements from different accounting periods, as the changes in revenues, operating costs, R&D spending, and net earnings over time are more meaningful than the numbers themselves.
- Together with the balance sheet and cash flow statement, the P&L statement provides an in-depth look at a company's financial performance.
- It is important to compare income statements from different accounting periods, as the changes in revenues, operating costs, research and development spending, and net earnings over time are more meaningful than the numbers themselves. For example, a company's revenues may grow, but its expenses might grow at a faster rate.

What Is a Balance Sheet?

A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity at a specific point in time, and provides a basis for computing rates of return and evaluating its capital structure. It is a financial statement that provides a snapshot of what a company owns and owes, as well as the amount invested by shareholders.

The balance sheet is used alongside other important financial statements such as the income statement and statement of cash flows in conducting fundamental analysis or calculating financial ratios.

- A balance sheet is a financial statement that reports a company's assets, liabilities and shareholders' equity.
- The balance sheet is one of the three (income statement and statement of cash flows being the other two) core financial statements used to evaluate a business.
- The balance sheet is a snapshot, representing the state of a company's finances (what it owns and owes) as of the date of publication.
- Fundamental analysts use balance sheets, in conjunction with other financial statements, to calculate financial ratios.

Formula Used for a Balance Sheet

The balance sheet adheres to the following accounting equation, where assets on one side, and liabilities plus shareholders' equity on the other, balance out:

\text{Assets} = \text{Liabilities} + \text{Shareholders' Equity}Assets=Liabilities+Shareholders’ Equity

This formula is intuitive: a company has to pay for all the things it owns (assets) by either borrowing money (taking on liabilities) or taking it from investors (issuing shareholders' equity).

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For example, if a company takes out a five-year, $4,000 loan from a bank, its assets (specifically, the cash account) will increase by $4,000. Its liabilities (specifically, the long-term debt account) will also increase by $4,000, balancing the two sides of the equation. If the company takes $8,000 from investors, its assets will increase by that amount, as will its shareholders' equity. All revenues the company generates in excess of its expenses will go into the shareholders' equity account. These revenues will be balanced on the assets side, appearing as cash, investments, inventory, or some other asset.

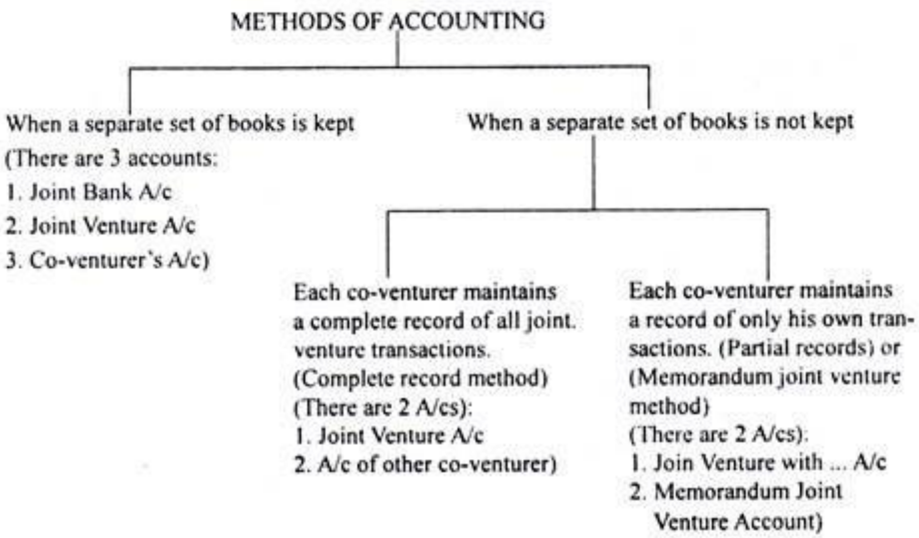
Assets, liabilities and shareholders' equity each consist of several smaller accounts that break down the specifics of a company's finances. These accounts vary widely by industry, and the same terms can have different implications depending on the nature of the business. Broadly, however, there are a few common components investors are likely to come across.

UNIT-2

JOINT VENTURE: It is a temporary form of business, where two or more persons join together to meet the short term objectives. It is quiet similar to Partnership firm, but established without name or registration separately under any law. Generally, JVs are formed for some particular purpose of business objective and once the objective is completed the JV is put to an end.

(A) Where Separate Set of Books is Kept:

This method is particularly followed where there are large transactions, that is, the venture is a large one and is continued for a comparatively long period. Accounts are prepared under double entry principle.



The following three accounts are prepared under this method:

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(I) Joint Venture Account

(II) Joint Bank Account

(III) Co-venturer’s Account

(Venturer’s Capital Account)

(I) Joint Venture Account:

This account represents the results of the business, that is, profit or loss. It is like a Trading/Profit & Loss Account of a trading concern. This account is debited by the cost of goods, expenses; goods supplied by the venturers etc. and are credited by sale proceeds, unsold stock, stock taken by venturers etc.

If credit side of this account is greater than the debit side, the difference represents profit on joint venture and vice versa in the opposite case. The profit or loss so made is transferred to co-venturer’s account.

(II) Joint Bank Account:

It is like an ordinary Cash Book or Bank Account. All incomes including the capital contribution by the ventures appear on the debit side of this account whereas all expenses of the venture appear on the credit side of this account. It is finally closed by payment to the co-venturers, leaving no balance either side.

(III) Co-Venturer’s Account:

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This is the capital account of the venturer relating to venture. This account is credited by the capital contributed by the venturers, goods supplied by them from their own stock, expenses made personally by them etc. whereas this account is debited for any withdrawals or any asset taken from the venture.

The profit or loss so made on venture is transferred to this account in profit sharing ratio and this account is closed by cash payment from joint bank and vice versa in the opposite case.

JOURNAL ENTRIES UNDER THIS METHOD

1. When cash contributed or invested or paid in by co-venturers	Joint Bank Account To Respective Co-venturer Account	Dr.
2. When goods purchased for joint venture	Joint Venture Account To Joint Bank Account	Dr.
3. When goods contributed by co-venturer	Joint Venture Account To Respective Co-venturer Account	Dr.
4. When goods purchased on credit	Joint Venture Account To Supplier's Account	Dr.
5. When suppliers are paid off	Suppliers' Account To Joint Bank Account	Dr.
6. When expenses incurred	Joint Venture Account To Joint Bank Account	Dr.
7. When expenses paid by a co-venturer	Joint Venture Account To Respective Co-venturer Account	Dr.
8. When goods sold for cash	Joint Bank Account To Joint Venture Account	Dr.
9. When goods sold on credit	Debtors' Account To Joint Venture Account	Dr.
10. When cash received from debtors/Bills Receivable	Joint Bank Account To Debtors/Bills Receivable A/c	Dr.
11. When goods taken by co-venturer	Respective Co-venturer Account To Joint Venture Account	Dr.
12. When commission or salary payable to co-venturers	Joint Venture Account To Respective Co-venturer A/c	Dr.
13. When discount received from creditors	Creditors Account To Joint Venture Account	Dr.
14. When discount allowed or bad debts incurred	Joint Venture Account To Debtors Account	Dr.
15. When cash is paid to creditors/Bills Payable	Creditors/Bills Payable A/c To Joint Bank Account	Dr.
16. Result of the joint venture: (*a*) Profit (*b*) Loss	Joint Venture Account To Each Co-venturer's Account Each Co-venturer's Account To Joint Venture Account	Dr. Dr.

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The Joint Bank Account should be now just sufficient to balance off the Co-venturers Account. That is, the Joint Bank Account is then closed by making payment to each partner of what is due to him in respect of his personal account. With the settlement of these accounts the separate books will automatically be closed off.

Illustration 1:

Rajeev and Ashok enter into a joint venture as dealers in land and opened a Joint Bank Account with Rs 60,000 towards which Rajeev contributed Rs 40,000. They agree to share profits and losses in proportion to their cash contribution. They purchased a plot of land measuring 5,000 square yards for Rs 50,000. It was decided to sell the land in smaller plots and a plan was got prepared at a cost of Rs 1,200.

In the said plan 1/5th of the total area of the land was left over for public roads and the remaining land was divided into 8 plots of equal size. Out of 8 plots, 3 plots were sold @ Rs 15 per square yard and the remaining 5 plots were sold @ Rs 14 per square yard. Expenses incurred in connection with the plots were: Registration Expenses Rs 4,000, Stamp Duty Rs 400 and Other Expenses Rs 1,000. Allow 2% on the sale proceeds as a commission to Rajeev.

Journalise the above transactions and prepare the necessary ledger accounts.

Solution:

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Journal

Date	Particulars		L.F.	Dr. Rs	Cr. Rs
	Joint Bank Account	Dr.		60,000	
	To Rajeev Account				40,000
	To Ashok Account				20,000
	(Being cash contributed by Rajeev and Ashok)				
	Joint Venture Account	Dr.		50,000	
	To Joint Bank Account				50,000
	(Being a plot of land purchased)				
	Joint Venture Account	Dr.		1,200	
	To Joint Bank Account				1,200
	(Being expenses incurred in preparation of a plan)				
	Joint Bank Account	Dr.		57,500	
	To Joint Venture Account				57,500
	(Being Sale Proceeds of: 3 plots of 500 sq. yards @ Rs 15 = 22,500 5 plots of 500 sq. yards @ Rs 14 = 35,000)				
	Joint Venture Account	Dr.		5,400	
	To Joint Bank Account				5,400
	(Being Expenses incurred: Registration Expenses 4,000 Stamp Duty 400 Other Expenses 1,000				
	Joint Venture Account	Dr.		1,150	
	To Rajeev Account				1,150
	(Being 2% commission on Rs 57,500)				
	Rajeev Account	Dr.		167	
	Ashok Account	Dr.		83	
	To Joint Venture Account				250
	(Being loss on Joint Venture transferred in the ratio of 2 : 1)				
	Rajeev Account	Dr.		40,983	
	Ashok Account	Dr.		19,917	
	To Joint Bank Account				60,900
	(Being amount paid in final settlement of Rajeev and Ashok Accounts)				

Dr. **Joint Venture Account** Cr.

	Rs			Rs
To Joint Bank Account	50,000	By Joint Bank Account		57,500
To Joint Bank Account–Expenses	1,200	By Loss on Joint Venture Account		
To Joint Bank Account–Expenses	5,400	Rajeev	Rs 167	
To Rajeev Account–Commission	1,150	Ashok	Rs 83	250
	57,750			57,750

Dr.	Joint Bank Account		Cr.
	Rs		Rs
To Rajeev Account	40,000	By Joint Venture Account	50,000
To Ashok Account	20,000	By Joint Venture Account	1,200
To Joint Venture Account	57,500	By Joint Venture Account	5,400
		By Rajeev Account	40,983
		By Ashok Account	19,917
	1,17,500		1,17,500

Co-Venturers Account

Dr.	Rajeev	Ashok	Cr	Rajeev	Ashok
	Rs	Rs		Rs	Rs
To Joint Venture Account–Loss	167	83	By Joint Bank Account	40,000	20,000
To Joint Bank Account	40,983	19,917	By Joint Venture Account	1,150	–
	41,150	20,000		41,150	20,000

Illustration 2:

Das Bose and Gupta undertake to erect a five-storied mansion for National Housing Trust Ltd. The contract price is agreed at Rs 25, 00,000 to be paid in cash, Rs 22, 00,000 by four equal installments and the balance amount in 8% Debentures of the company. They agree to share equally the profit or loss.

They opened a Joint Bank Account with cash contributed as stated below:

Das Rs 3, 00, 000; Bose Rs 3, 75,000 and Gupta Rs 2, 00,000

Das arranges the preparation of building plans etc. and pays Rs 32,000 as architect's fees. Bose brings a concrete mixer and other implements valued at Rs 80,000 and Gupta brings a motor lorry valued at Rs 75,000.

They paid in cash for the following:

	Rs		Rs
Materials	12,26,800	Sundry Expenses	20,000
Wages	7,33,200	Plant	60,000

`

On completion of the venture concrete mixer is sold for Rs 50,000 and Plant and other implements are sold for Rs 10,000. Gupta takes back the motor lorry at Rs 40,000. Das took over the Debentures issued by the company at a valuation of Rs 2, 80,000.

Show the necessary ledger accounts for the Joint Venture.

Solution:

In the books of Das, Bose and Gupta

Joint Venture Account

Dr.		Rs			Rs Cr.
To Das Account–			By Joint Bank A/c–		
Architect's Fees		32,000	Part of Contract Price		22,00,000
To Bose A/c–			By Debenture Account		3,00,000
Mixer and other Implements		80,000	By Joint Bank A/c–		
To Gupta A/c–Motor Lorry		75,000	Sale Proceeds of		
To Joint Bank A/c–			Mixer	50,000	
Materials	12,26,800		Plant	10,000	60,000
Wages	7,33,200		By Gupta A/c–		
Sundry Expenses	20,000		Motor Lorry taken back		40,000
Plant	60,000	20,40,000			
To Debenture Account		20,000			

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To Profit and Loss A/c–					
Das 1/3	1,17,667				
Bose 1/3	1,17,667				
Gupta 1/3	1,17,666	3,53,000			
		26,00,000			26,00,000

Dr. **Joint Bank Account** Cr.

		Rs			Rs
To Das A/c		3,00,000	By Joint Venture A/c–		
To Bose A/c		3,75,000	Material	12,26,800	
To Gupta A/c		2,00,000	Wages	7,33,200	
To Joint Venture A/c–			Sundry Expenses	20,000	
Part of Contract Price		22,00,000	Plant	60,000	20,40,000
To Joint Venture A/c–			By Das A/c		1,69,667
Sale Proceeds of			By Bose A/c		5,72,667
Mixer	50,000		By Gupta A/c		3,52,666
Plant	10,000	60,000			
		31,35,000			31,35,000

Dr. **Co-Venturers Account** Cr.

	Das	Bose	Gupta		Das	Bose	Gupta
	Rs	Rs	Rs		Rs	Rs	Rs
To Joint Venture A/c–				By Joint Bank A/c–	3,00,000	3,75,000	2,00,000
Debenture taken over	2,80,000			By Joint Venture A/c–			
To Joint Venture A/c-				Architect's Fees	32,000		
Motor Lorry taken over			40,000	By Joint Venture A/c–			
To Joint Bank A/c	1,69,667	5,72,667	3,52,666	Mixer		80,000	
				By Joint Venture A/c–			
				Motor Lorry			75,000
				By Joint Venture A/c–			
				Share of Profit	1,17,667	1,17,667	1,17,666
	4,49,667	5,72,667	3,92,666		4,49,667	5,72,667	3,92,666

(B) Where No Separate Set of Books is Kept:

This method is applicable where the joint venture transactions are limited and the venturers reside at two different places. Under this method each venturer will record his own transactions plus the transactions relating to other co-venturer's capital whereas the other venturer will prepare a Joint Venture Account and the capital of the others, that is, two accounts are prepared in each party s ledger.

For instance, there are two venturers, namely, A and B. So, A will prepare a Joint Venture Account and B's Capital Account in his books while B will also prepare a Joint Venture Account and A's Capital Account in his book.

(1) Joint Venture Account:

It should be prepared like the previous one which reveals the result of the business, that is, profit or loss which ultimately be transferred to Venturers Capital. But in this case one's own share of profit or loss should be transferred to his Profit and Loss Account but co-venturer's share of profit or loss should be transferred to his personal account.

(2) Other Co-Venturer's Account:

Since this is a personal account of the co-venturer, his account will be debited with the amount of goods purchased, expenses incurred, profit so earned etc. and is credited with the amount of sale proceeds, unsold stock taken etc.

The balance of this account will go to either:

(i) The Balance Sheet, if it is so prepared, or

(ii) The same will represent the final payment of Receipts and Payments between the venturers.

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Journal Entries

	A's Books		B's Books	
When goods are supplied by *A*	Joint Venture A/c To Purchase A/c	Dr.	Joint Venture To *A*'s Account	Dr.
When expenses paid by *A*	Joint Venture A/c To Cash A/c	Dr.	Joint Venture A/c To *A*'s A/c	Dr.
When goods are supplied by *B*	Joint Venture A/c To *B*'s A/c	Dr.	Joint Venture A/c To Purchase A/c	Dr.
When expenses paid by *B*	Joint Venture A/c To *B*'s A/c	Dr.	Joint Venture A/c To Cash A/c	Dr.
When cash is contributed by *A*	Joint Venture A/c To Cash A/c	Dr.	Joint Venture A/c To *A*'s Account	Dr.
When cash is contributed by *B*	Joint Venture A/c To *B*'s A/c	Dr.	Joint Venture A/c To Cash A/c	Dr.
When a Bill is drawn by *A* and accepted by *B*	Bills Receivable A/c To *B*'s A/c	Dr.	*A*'s A/c To Bills Payable A/c	Dr.
When Bill is discounted by *A*	Cash A/c Joint Venture A/c (Discount amount) To Bills Receivable A/c	Dr. Dr.	Joint Venture A/c (Discount Amount) To *A*'s A/c	Dr.
When Commission allowed to *B*	Joint Venture A/c To *B*'s A/c	Dr.	Joint Venture A/c To Commission A/c	Dr.
When salary allowed to *A*	Joint Venture A/c To Salary A/c	Dr.	Joint Venture A/c To *A*'s A/c	Dr.
When goods sold by *A*	Cash A/c To Joint Venture A/c	Dr.	*A*'s A/c To Joint Venture A/c	Dr.

	A's Books		B's Books	
When credit sales are made by *A*	Sundry Debtors A/c To Joint Venture A/c	Dr.	*A*'s A/c Joint Venture A/c	Dr.
When bad debts arise (sales made by *A*)	Joint Venture A/c To Sundry Debtors A/c	Dr.	Joint Venture A/c To *A*'s Account	Dr.
When unsold stocks taken by *A*	Purchase A/c To Joint Venture A/c	Dr.	*A*'s A/c To Joint Venture A/c	Dr.
When Joint Venture shows profit	Joint Venture A/c To *B*'s A/c To Profit & Loss A/c	Dr.	Joint Venture A/c To *A*'s A/c To Profit & Loss A/c	Dr.
When Joint Venture shows loss	Profit & Loss A/c *B*'s A/c To Joint Venture A/c	Dr. Dr.	Profit & Loss A/c *A*'s A/c To Joint Venture A/c	Dr. Dr.

Now, the balance in the personal account shows the amount due to or from him.

Illustration 1:

A and B were partners in a joint venture sharing profits and losses in the proportion of 60% and 40% respectively. A supplies goods to the value of Rs 10,000 and incurs on freight Rs 500. B also supplies goods to the value of Rs 8,000 and incurs Rs 400 towards freight and other incidental charges. B sells the entire stock of goods on behalf of the joint venture for Rs 25,000. B is also entitled to a commission of 5% on sales. B settles his account by remitting a bank draft.

Pass journal entries and ledger accounts in the books of A and B.

Solution:

A's Journal

				Dr.	Cr.
				Rs	Rs
	Joint Venture Account	Dr.		10,500	
	To Purchase Account				10,000
	To Bank Account				500
	(Being the value of goods sent to *B* and expenses incurred)				
	Joint Venture Account	Dr.		8,400	
	To *B*'s Account				8,400
	(Being the value of goods supplied and expenses incurred by *B*)				
	B's Account	Dr.		25,000	
	To Joint Venture Account				25,000
	(Being sale proceeds of goods received by *B* on behalf of joint venture)				
	Joint Venture Account	Dr.		1,250	
	To *B*'s Account				1,250
	(Being commission due to *B* at 5% on sales)				
	Joint Venture Account	Dr.		4,850	
	To *B* Account				1,940
	To Profit and Loss Account				2,910
	(Being division of profit in the agreed proportion)				
	Bank Account	Dr.		13,410	
	To *B*'s Account				13,410
	(Being receipt of balance due from *B*)				

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A's Ledger

Joint Venture Account

Dr.	Rs		Cr. Rs
To Purchase Account	10,000	By B's Account (Sales Proceeds)	25,000
To Bank Account	500		
To *B*'s Account	8,400		
To *B*'s Account (Commission)	1,250		
To Profit:			
B's Account	1,940		
Profit & Loss A/c	2,910		
	25,000		25,000

B's Account

Dr.	Rs		Cr. Rs
To Joint Venture (Sale Proceeds)	25,000	By Joint Venture A/c	8,400
		By Joint Venture A/c (Commission)	1,250
		By Joint Venture A/c (Profit)	1,940
		By Bank Account	13,410
	25,000		25,000

B's Journal

			Dr. Rs	Cr. Rs
	Joint Venture Account Dr.		10,500	
	To *A* Account			10,500
	(Being goods supplied and expenses met by *A*)			
	Joint Venture Account Dr.		8,400	
	To Purchase Account			8,000
	To Bank Account			400
	(Being the value of goods supplied and expenses incurred)			
	Bank Account Dr.		25,000	
	To Joint Venture A/c			25,000
	(Being sale proceeds of goods in cash)			
	Joint Venture Account Dr.		1,250	
	To Commission Account			1,250
	(Being commission due at 5% on Rs 25,000)			
	Joint Venture Account Dr.		4,850	
	To *A* Account			2,910
	To Profit and Loss Account			1,940
	(Being division of profit in the agreed proportion)			
	A Account Dr.		13,410	
	To Bank Account			13,410
	(Being remittance of balance due to *A*)			

B's Ledger

Joint Venture Account

Dr.	Rs		Cr. Rs
To *A* Account	10,500	By Bank Account	
To Purchase Account	8,000	(Sales proceeds)	25,000
To Bank Account	400		
To Commission	1,250		
To Profit:			
A Account	2,910		
Profit & Loss Account	1,940		
	25,000		25,000

A's Account

Dr.	Rs		Cr. Rs
To Bank Account	13,410	By Joint Venture Account	10,500
		By Joint Venture Account (Profit)	2,910
	13,410		13,410

Illustration 2:

A and B enter into a joint venture to sell a consignment of timber sharing profits and losses equally. A provides timber from stock at mutually agreed value of Rs 5.000. He pays expenses amounting to Rs 250. B incurs further expenses on cartage, storage, and coolie charges of Rs 650 and receives cash or sales Rs 3,000.

He also takes over goods to the value of Rs 1,000 for his use in his own business. At the close, A takes over the balance stock in hand which is valued at Rs 1,100. Prepare joint venture account and Co-sharer's account in the books of A.

Solution:

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In the books of A

B Account

Dr.	Rs		Cr. Rs
To Joint Venture (Sales)	3,000	By Joint Venture (Exp.)	650
To Joint Venture (Goods)	1,000	By Bank (Settlement)	3,750
To Joint Venture (Loss)	400		
	4,400		4,400

Joint Venture Account

Dr.	Rs		Cr. Rs
To Purchases	5,000	By B's (Sales)	3,000
To Bank (Exp.)	250	By B's A/c (Goods)	1,000
To B's A/c (Exp.)	650	By Purchase (Goods)	1,100
		By B's A/c (Loss)	400
		By Profit & Loss (Loss)	400
	5,900		5,900

Illustration 3:

A and B agree to enter into a joint venture to buy and sell second-hand ice-cream vehicles and to share profits and losses in the ratio of 5:3 respectively. It was agreed that/I would record all details of the venture in his books of account.

On 21st December, 2003, B purchased two vehicles and paid cash Rs 20,000 on 2nd January', 2004. He spent sums of Rs 2,480 on repairs, Rs 240 on driver's wages and Rs 360 on temporary insurance cover. He sold the vehicles a week later for Rs 28,000 subject to a 2% cash discount if paid within seven days. He paid the proceeds of sale into his bank account on 10th January, 2004.

On 31st January, 2004, A purchased five vehicles for Rs 50,000 of which he managed to sell three for Rs 36,000 for cash on the same day, without incurring any expenses. The fourth vehicle was sold for Rs 13,500 and on 7th February, 2004, he received a Bill Receivable to be presented for payment in three months' time.

On 31st March, 2004, the fifth vehicle was still unsold and it was agreed that B should take over the vehicle at a valuation of Rs 7,500. On 31st March, 2004, the parties made a settlement between each other, A agreeing to take the bill receivable at a value of Rs. 13,180.

`

You are required to prepare Joint Venture Account and B's account as they would appear in the books of A.

Solution:

In the books of A

Joint Venture Account

Dr.							Cr.
Date	Particulars		Rs	Date	Particulars		Rs
2003				2004			
Dec. 21	To *B* A/c–Purchases		20,000	Jan. 9	By *B* A/c–Sales		28,000
2004				Jan. 31	By Bank– Sales		36,000
Jan. 2	To *B* A/c:			Feb. 7	By Bills Receivable A/c- Sales		13,500
	Repairs	2,480		Mar. 31	By *B* A/c–Vehicle taken over		7,500
	Driver's Wages	240					
	Insurance	360	3,080				
Jan. 10	To *B* A/c–Discount		560				
Jan. 31	To Creditors A/c–Purchases		50,000				
Mar. 31	To Bills Receivable A/c– Reduction in book value		320				
Mar. 31	To Profit transferred to Profit and Loss A/c						
	A A/c: 5/3	6,900					
	B A/c: 3/5	4,140	11,040				
			85,000				85,000

B Account

Dr.							Cr.
Date	Particulars		Rs	Date	Particulars		Rs
2004				2003			
Jan. 9	To Joint Venture A/c– Sales		28,000	Dec. 21	By Joint Venture A/c– Purchases		20,000
Mar. 31	To Joint Venture A/c– Vehicle taken over		7,500	2004			
				Jan. 2	By Joint Venture A/c:		
					Repairs	2,480	
					Driver's Wages	240	
					Insurance	360	3,080
					By Joint Venture A/c- Discount		560
					By Joint Venture A/c– Share of Profit		4,140
					By Bank–Remittance		7,720
			35,500				35,500

(C) Where Each Co-Venturer Maintains A Record of His Own Transactions (or Partial Record Method) (or Momorandum Joint Venture Method):

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Under this method each co-venturer keeps a record of Joint Venture transactions in which he is involved i.e. each venturer records in his own book only the transactions of joint venture which relate to him. Each party keeps his account in his own books. He will not record the transactions of other co- venturer. Hence it is a partial record.

It will be clear from the following points:

1. Each Co-venturer will open one account in his book and it will be headed: Joint Venture with—(Name of other Co-Venturer) Account. This is a personal account. It is not a Nominal Account as Joint Venture, explained above. It does not disclose the profit or loss on Joint Venture. Each Co-Venturer debits the Account with the amount paid by him and credits the Account when he receives amounts.

2. In this Account, the concerned party records only his transactions. No account whatsoever is taken of the supplies made, expenses incurred etc. by the other co-venturer.

Journal entries in the books of one party, say, Mr A and the other Co-Venturer Mr. B.

1. When Goods are Purchased by A:

Joint Venture with B Account Dr

To cash Account

2. When Goods are Sold by A:

Cash Account Dr.

To Joint Venture with B Account

3. When Commission is Received by A:

Joint Venture with B Account Dr

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To Commission Account

4. When A Meets the Expenses:

Joint Venture with B Account Dr

To Cash Account

5. When Unsold Stock is Taken by A:

Purchase Account Dr

To Joint Venture with B Account

The above Account i.e. Joint Venture with B Account is a personal account. It does not reveal profit or loss of Joint Venture. In order to ascertain profit or loss of Joint Venture we have to prepare Memorandum Joint Venture Account. In order to prepare Memorandum Joint Venture Account, one co-venturer sends another co-venturer a copy of the account kept by him.

On the basis of the copy of account and his own account, Memorandum Joint Venture is prepared. In other words, Memorandum Joint Venture Account is just a combination of Joint Venture Accounts prepared by all the co-venturers.

The debit side of the Joint Venture with B Account is put on the debit side of the Memorandum Joint Venture Account and credit side of that account is put on the credit side of the Memorandum Joint Venture Account. That is, the transactions of personal accounts of all co-venturers are entered in the Memorandum Joint Venture Account.

Memorandum Joint Venture Account is just like a trading and profit and loss Account. All the co-venturers prepare the same Memorandum Joint Venture Account. The balance amount of

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Memorandum Joint Account shows either profit or loss on Joint Venture. The Co-venturers share the profit or loss in the agreed ratio.

For this co-venturers make the following entries:

In the books of A

If profit is there:	Joint Venture with B Account	Dr.
	To Profit and Loss Account	
If there is loss:	Profit and Loss Account	Dr.
	To Joint Venture with B Account	

Similarly, in the books of B

If profit is there:	Joint Venture with A Account	Dr.
	To Profit and Loss Account	
If there is loss:	Profit and Loss Account	Dr.
	To Joint Venture with A Account	

Remember that the balance of Joint Venture with account shows the amount due to the other Co-venturer or due from the other Co-venturer.

Illustration 1:

In the books of A

Dr. Joint Venture with B Account Cr.

	Rs		Rs
To Purchases Account	10,000	By Bank Account	13,410
To Bank Account	500		
To Profit and Loss Account	2,910		
	13,410		13,410

In the books of B

Dr. Joint Venture with A Account Cr.

	Rs		Rs
To Purchases Account	8,000	By Bank Account	25,000
To Bank Account	400	(Sale proceeds)	
To Commission A/c	1,250		
To Profit and Loss A/c	1,940		
To Bank Account	13,410		
	25,000		25,000

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Memorandum Joint Venture Account
(Common to both)

Dr.		Rs		Cr. Rs
To A (Purchase and Expenses)		10,500	By B (Sale proceeds)	25,000
To B (Purchase and Expenses)		8,400		
To B (Commission)		1,250		
To Profit:				
A–60%	2,910			
B–40%	1,940	4,850		
		25,000		25,000

Illustration 2:

A and B enter into joint venture for guaranteeing the subscription at par of 1, 00,000 shares of Rs 10 each of a joint stock company. They agree to share profits and losses in the ratio of 2:3. The terms with the company are 4.5% of commission in cash and 6.000 shares of the company as fully paid up?

The public took up 88,000 of the shares and the balance shares of the guaranteed issue are taken up by A and B who provide cash equally. The commission in cash is taken by partners in the ratio of 4: 5.

The entire shareholding of the joint venture is then sold through brokers:

25% at a price of Rs 9 per share;

50% at a price of Rs 8.75 per share;

15% at a price of Rs 8.50 per share; and the remaining 10% are taken over by A and B equally at Rs 8 per share.

The sale proceeds of the shares are taken by the partners equally.

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Prepare Joint Venture Memorandum Account and the separate accounts of A and B in the books of B and A respectively showing the adjustment of the final balance between A and B. Ignore interest.

SOLUTION

Dr. **Memorandum Joint Venture Account** Cr.

		Rs		Rs
To *A* Account–Cost of Share (1)		60,000	By *A* Account–Commission (3)	20,000
To *B* Account–Cost of Share (1)		60,000	By *B* Account–Commission (3)	25,000
To Profit transferred to:			By *A* Account–Sales Proceeds (2)	71,100
A Account	32,640		By *B* Account–Sales Proceeds (2)	71,100
B Account	48,960	81,600	By *A* Account–Shares taken (4)	7,200
			By *B* Account–Shares taken (4)	7,200
		2,01,600		2,01,600

In the books of A

Dr. **Joint Venture with B Account** Cr.

	Rs		Rs
To Bank Account–Cost of Share (1)	60,000	By Bank Account–Commission (3)	20,000
To Profit and Loss Account	32,640	By Bank Account–Sale Proceeds (2)	71,100
To Bank Account–Final Settlement	5,660	By Shares Account–Shares taken (4)	7,200
	98,300		98,300

In the books of B

Dr. **Joint Venture with A Account** Cr.

	Rs		Rs
To Bank Account–Cost of Shares (1)	60,000	By Bank Account–Commission (3)	25,000
To Profit and Loss Account	48,960	By Bank Account–Sale proceeds (2)	71,100
		By Shares Account–Shares taken (4)	7,200
		By Bank Account–Final settlement	5,660
	1,08,960		1,08,960

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Working Notes:

1. Purchase of Shares:

   1,00,000 – 88,000 = 12,000 shares @ Rs 10

   = Rs 1,20,000 provided by A and B equally *i.e.* Rs 60,000 each

2. Calculation of Sales:

   12,000 Shares purchased

   6,000 Shares are taken as commission

   Entire Shareholding 18,000

	Rs
25% of 18,000 = 4,500 Shares @ Rs 9.00	= 40,500
50% of 18,000 = 9,000 Shares @ Rs 8.75	= 78,750
15% of 18,000 = 2,700 Shares @ Rs 8.50	= 22,950
90%	1,42,200

   50% of Rs 1,42,200 taken by *A* = Rs 71,100

   50% of Rs 1,42,200 taken by *B* = Rs 71,100

3. Commission in Cash:

   1,00,000 Shares @ Rs 10 = Rs 10,00,000

   4½% of Rs 10,00,000 is taken by *A* and *B* in the ratio 4 : 5 *i.e.* Rs 45,000

   $$\text{For } A = 45{,}000 \times \frac{4}{9} = \text{Rs } 20{,}000$$

   $$\text{For } B = 45{,}000 \times \frac{5}{9} = \text{Rs } 25{,}000$$

4. Unsold Shares are taken equally by *A* and *B*.

   10% of 18,000 = 1,800 Shares @ Rs 8 = Rs 14,400

   A = Rs 7,200

   B = Rs 7,200

Illustration 3:

Mr. A and B decided to work a joint venture for the sale of electric motors. On 21st Jan Mr. A purchased 200 electric motors at Rs 175 each and despatched 150 motors to Mr B incurring Rs 1,000 as freight and insurance charges.

10 electric motors were damaged in transit. On 1st February Rs 500 were received by Mr. A from the Insurance Company, in full settlement of his claim. On 15th March, Mr. A sold 50 electric motors at Rs 225 each. He received Rs 15,000 from Mr B on 1st April.

On 25th Jan., Mr B took delivery of electric motors and incurred the following expenses:

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	Rs
Clearing charges	170
Repairs to electric motors damaged in transit	300
Godown rent for 3 months	600

He sold the electric motors as follows:

1st Feb.:	10 damaged motors at Rs 170 each
	40 motors at Rs 200 each
15th March:	20 motors at Rs 315 each
1st April:	80 motors at Rs 250 each.

It is agreed that they are entitled to commission at 10% on the respective sales effected by them and that the profits and losses shall be shared between Mr. A and Mr. B in the ratio of 2: 1.

Mr. B remits to Mr. A the balance amount due on 30th April. You are required to show in the books of A (i) Joint Venture Account and (ii) the Memorandum of Joint Venture Account.

Solution:

In the books of A

Dr. **Joint Venture with B Account** Cr.

		Rs			Rs
Jan. 21	To Bank A/c–Purchase of Motors: 175 × 200	35,000	Feb. 1	By Bank A/c– Insurance Claim	500
Jan. 21	To Bank A/c– Freight and Insurance	1,000	Mar. 15	By Bank A/c– Sales: 225 × 50	11,250
Apr. 30	To Commission A/c	1,125		By Bank A/c– Remittance from B	15,000
Apr. 30	To Profit and Loss A/c– Share of Profit	3,970		By Bank A/c– Remittance from B	14,345
		41,095			41,095

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Dr.	Memorandum Joint Venture Account					Cr.
			Rs			Rs
					By *A* A/c:	
Jan. 21	To *A* A/c:			Feb. 1	Insurance Claim	500
	Purchases		35,000	Mar. 15	Sales	11,250
Jan. 21	Freight and Insurance		1,000		By *B* A/c:	
Apr. 30	Commission		1,125		Sales:	
	To *B* A/c:				9,700 + 6,300 + 20,000	36,000
Jan. 25	Clearing Charges		170			
Jan. 25	Repairs to Motor		300			
Jan. 25	Godown Rent		600			
Apr. 30	Commission		3,600			
Apr. 30	To Profit on Venture:					
	A 2/3	3,970				
	B 1/3	1,985	5,955			
			47,750			47,750

Workings:

In the books of B

Dr.	Joint Venture with A Account				Cr.
		Rs			Rs
Jan. 25	To Bank A/c:		Feb. 1	By Bank A/c–	
	Clearing Charges	170		Sales:	
	Repairs to Motor	300		170 × 10 = Rs 1,700	
	Godown Rent	600		200 × 40 = Rs 8,000	9,700
Apr. 1	To Bank A/c–		Mar. 15	By Bank A/c	
	Remittance to *A*	15,000		Sales: 315 × 20	6,300
Apr. 30	To Commission A/c	3,600	Apr. 1	By Bank A/c–	
Apr. 30	To Profit and Loss A/c–			Sales: 250 × 80	20,000
	Share of Profit	1,985			
Apr. 30	To Bank A/c–				
	Remittance to *A*	14,345			
		36,000			36,000

N.B. The amount due from *B i.e.* Rs 14,345 is equal to the amount due to *A i.e.* Rs 14,345.

Illustration 4:

A and B enter into a joint venture as dealers in land with effect from 1st July 2005. On the same day A advanced Rs 90.000 and a plot of land, measuring 9,000 sq. yards, was purchased with this money. It was decided to sell the land in smaller plots and a plan was got prepared at a cost of Rs 1,000 paid by B.

In the said plan 1/3rd of the total area of the land was left over for public roads and the remaining land was divided into 6 plots of equal size. On 1st October 2005, two of the plots were sold at Rs

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30 per sq. yard, the buyer deducting Rs 1.000 per plot for stamp duty and registration expenses to be borne by the seller.

The remaining plots were sold at net price of Rs 25 per sq. yard on 1st December 2005. The sale proceeds of all the plots were received by A. After charging interest at 6% p.a. on the investments of A (allowing for money received by him) and allowed 1 % on the net sale proceeds of plots as commission to B, the net profit of the joint venture is to be shared in the proportion of 3/4th to A and 1/4th to B.

Draw up the memorandum joint venture revenue account and personal accounts in the books of A and B showing the balance payable by one to the other. Assume joint venture was completed on December 31.

Solution:

In the books of A

Joint Venture with B Account

Dr. Cr.

		Rs				Rs
2005			2005			
July 1	To Cash A/c–Advance	90,000.00	Oct. 1	By Cash A/c		
Dec. 31	To Interest A/c (1)	2,250.00		(2,000 × 30)	60,000	
Dec. 31	To Profit and Loss A/c (A)	47,812.50		Less: Expenses	2,000	58,000
Dec. 31	To Bank A/c		Dec. 1	By Cash A/c		
	-Final Settlement	18,517.50		(4,000 × 25)		1,00,000
			Dec. 1	By Interest A/c (2)		580
		1,58,580.00				1,58,580

(1) Interest receivable by *A*: 1st July to 1st Dec.: Rs $\frac{90,000 \times 6 \times 5}{100 \times 12}$ = Rs 2,250

(2) Interest payable by *A*: 1st Oct. to 1st Dec.: Rs $\frac{58,000 \times 6 \times 2}{100 \times 12}$ = Rs 580

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In the books of B

Joint Venture with A Account

Dr. Cr.

2005		Rs	2005		Rs
July 1	To Cash A/c–Expenses	1,000.00	Dec. 31	By Cash A/c– Final Settlement	18,517.50
Dec. 31	To Commission A/c (1% of 1,58,000)	1,580.00			
Dec. 31	To Profit and Loss A/c–(*B*)	15,937.50			
		18,517.50			18,517.50

Memorandum Joint Venture Account

Dr. Cr.

2005			Rs	2005			Rs
July 1	To Purchases A/c-*A*		90,000	Oct. 1	By Sales A/c		
Dec. 1	To Interest A/c–*A*		2,250		2,000 × 30 =	60,000	
	To Expenses A/c–*B*		1,000		4,000 × 25 =	1,00,000	
	To Commission A/c–*B*		1,580			1,60,000	
	Profits:				Less: Expenses	2,000	1,58,000
	A–	47,812.50			By Interest A/c–*A*		580
	B–	15,937.50	63,750				
			1,58,580				1,58,580

Illustration 5:

Das and Roy entered into a joint venture involving buying and selling old railway material. The profit or loss was to be shared equally. Cost of the material purchased was Rs. 42,500 which was paid by Das who drew a bill on Roy at 2 months' demand for Rs. 30,000. The bill was discounted by Das at a cost of Rs. 240.

The transactions relating to the venture were:

(a) Das paid Rs. 300 for carriage, Rs. 500 for Commission on sales and Rs. 200 travelling expenses;

(b) Roy paid Rs. 100 travelling expenses and Rs. 150 sundry expenses;

(c) Sales made by Das amounted to Rs 20,000 and

(d) Sales made by Roy were Rs. 30,000.

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Goods costing Rs. 1,000 and Rs. 1,500 (being unsold stock) were retained by Das and Roy respectively and these were charged to them at prices to show the same rate of gross profit as that made on the total sales (excluding these sales).

Das was credited with a sum of Rs. 400 to cover the cost of warehousing and insurance. The expenses in connection with the bill were to be treated as a charge against the venture.

You are required (a) to show the account in the books of each party to record his own transactions and (b) to prepare a joint venture account.

Solution:

Dr. **Memorandum Joint Venture Account** Cr.

Particulars	Rs	Particulars	Rs
To Das A/c:		By Das A/c :	
Cost of Materials	42,500	Sales proceeds	20,000
Discount on B/R	240	Goods taken over (1)	1,250
Carriage	300	By Roy A/c:	
Commission	500	Sales proceeds	30,000
Travelling Expenses	200	Goods taken over (1)	1,875
Warehousing & Insurance	400		
To Roy A/c:			
Travelling expenses	100		
Sundry expenses	150		
To Profit transferred to :			
Das A/c: $8,735 \times \frac{1}{2} = 4,368$			
Roy A/c: $8,735 \times \frac{1}{2} = 4,367$	8,735		
	53,125		53,125

In the books of Roy
Joint Venture with Das A/c

Particulars	Rs	Particulars	Rs
To Bills Payable A/c	30,000	By Bank A/c (Sales proceeds)	30,000
To Bank A/c (Travelling exp.)	100	By Purchases A/c (1)	
To Bank A/c (Sundry exp.)	150	(Goods taken over)	1,875
To P & L A/c (Share of profit)	4,367	By Balance (due from Das) c/d	2,742
	34,617		34,617

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In the books of Das
Joint Venture with Roy A/c

Particulars	Rs	Particulars	Rs
To Bank (Materials purchased)	42,500	By Bills Receivable A/c	30,000
To Discount on B/R A/c	240	By Bank A/c (Sales proceeds)	20,000
To Bank A/c (Carriage)	300	By Purchases A/c (1)	
To Bank A/c (Commission on sales)	500	(goods taken over)	1,250
To Bank A/c (Travelling exp.)	200		
To Bank A/c (Warehousing etc.)	400		
To P & L A/c (Share of profit)	4,368		
To Balance (due to Roy) c/d	2,742		
	51,250		51,250

Working Notes:

Computation of Gross Profit Percentage:

	Rs.
Purchases	42,500
Less : Unsold Stock (1,000 + 1,500)	2,500
Cost of goods sold	40,000
Sales (20,000 + 30,000)	50,000
Gross Profit	10,000

Percentage of Gross profit $= \frac{10,000}{40,000} \times 100 = 25\%$ on Cost.

(1) Computation of price at which unsold materials are taken over:

	Das Rs.	Roy Rs
Cost of materials	1,000	1,500
Add : Gross Profit:		
25% on Cost	250	375
	1,250	1,875

Illustration 6:

Ghosh and Bose enter into a joint venture for guaranteeing the subscription at par of 1, 00,000 shares of Rs. 10 each of a joint stock company. They agree to share profits and losses in the ratio of 1: 3. The terms with the company are 4 ½ % Commission in cash and 6.000 shares of the company to be allotted as fully paid up.

The public take up 94,000 of the shares and the balance shares of guaranteed issue are taken up by Ghose and Bose who provide cash equally. The commission in cash is taken by the partners in the ratio of 4: 5.

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The entire shareholding of the venture is then sold through brokers, 25% at a price of Rs. 9, 50% at a price of Rs. 8.75, 15% at a price of Rs. 8.50 and remaining 10% are taken over by Ghosh and Bose equally at Rs. 8 per share. The sale proceeds of the shares are taken by the partners equally.

Prepare a Joint Venture Memorandum A/c and the separate accounts in the books of Ghosh and Bose.

SOLUTION

Dr. **Memorandum Joint Venture Account** Cr.

Particulars	*Rs*	*Particulars*	*Rs*
To Ghosh A/c :		By Ghosh A/c :	
Cost of Shares $6,000 \times 10 \times \frac{1}{2}$	30,000	Commission	20,000
To Bose A/c:		Sale of shares (3)	47,400
Cost of Shares $6,000 \times 10 \times \frac{1}{2}$	30,000	Unsold shares taken over (4)	4,800
To Profit transferred to :		By Bose A/c:	
Ghosh : $89,400 \times \frac{1}{4} = 22,350$		Commission	25,000
Bose: $89,400 \times \frac{3}{4} = 67,050$	89,400	Sale of shares (3)	47,400
		Unsold shares taken over (4)	4,800
	1,49,400		1,49,400

In the books of Ghosh

Joint Venture with Bose A/c

Particulars	*Rs*	*Particulars*	*Rs*
To Bank A/c (Contribution for unsubscribed shares : 3000 × 10)	30,000	By Bank A/c (Commission in Cash : $45,000 \times \frac{4}{9}$)	20,000
To P & L (Share of profit)	22,350	By Bank A/c (Sale of shares : $94,800 \times \frac{1}{2}$)	47,400
To Balance (due to Bose) c/d	19,850	By Shares A/c (unsold shares taken over: (600 shares × 8)]	4,800
	72,200		72,200

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In the Books of Bose
Joint Venture with Ghosh A/c

Particulars	*Rs*	*Particulars*	*Rs*
To Bank A/c (Contribution for unsubscribed Shares)	30,000	By Bank A/c (Commission in Cash : $45,000 \times \frac{5}{9}$)	25,000
To P & L A/c (Share of Profit)	67,050	By Bank A/c (Sale of Shares : $94,800 \times \frac{1}{2}$)	47,400
		By Shares A/c (Unsold shares taken over 600 × 8)	4,800
		By Balance (due from Ghose) c/d	19,850
	97,050		97,050

Working Notes:

(i) No. of Shares to be subscribed by Co-venturers

= (1,00,000 – 94,000) = 6,000 shares

(ii) Calculation of Commission received in Cash:

$$= 1,00,000 \times 10 \times 4\frac{1}{2}\% = \text{Rs. } 45,000$$

3. ***Calculation of Value of shares sold:***

No. of shares at the disposal of the Co-venturers:

Shares subscribed	6,000
Shares received as Commission	6,000
	12,000
	Rs.
25% of 12,000 or 3,000 shares @ Rs. 9	= 27,000
50% of 12,000 or 6,000 shares @ Rs. 8.75	= 52,500
15% of 12,000 or 1,800 shares @ Rs. 8.50	= 15,300
Total Sale Proceeds	94,800

Ghose : $94,800 \times \frac{1}{2} = 47,400$; Bose : $94,800 \times \frac{1}{2} = 47,400$

4. Calculation value of unsold shares taken over by Ghosh and Bose:

10% of 12,000 or 1,200 shares equally @ Rs. 8 per share = Rs. 9,600

Ghosh : $9,600 \times \frac{1}{2} = 4,800$; Bose : $9,600 \times \frac{1}{2} = 4,800$

Recording in One of the Party's Books:

Illustration 1:

Anup, Rakesh and Jaipal entered into an agreement for a joint venture. Anup bought goods for Rs. 14.400 and took from his stock goods valued at 4,800. He received from Rakesh and Jaipal their

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shares of investment in the adventure. Rs. 6,400 each. Anup paid charges and expenses of Rs. 1,460. The goods were sold for Rs. 24,400. Anup charged 5% commission on sales and rendered statement to Rakesh and Jaipal.

Journalise the above transactions in the books of Anup.

SOLUTION

In the books of Anup

		Dr.	Cr.
		Rs	Rs
Cash Account	Dr.	12,800	
To Rakesh			6,400
To Jaipal			6,400
(Being cash received from other co-venturers)			
Joint Venture A/c	Dr.	14,400	
To Cash A/c			14,400
(Being goods purchased)			
Joint Venture A/c	Dr.	4,800	
To Purchase A/c			4,800
(Goods taken from stock)			
Joint Venture A/c	Dr.	1,460	
To Cash A/c			1,460
(Being charges & expenses)			
Cash Account	Dr.	24,400	
To Joint Venture A/c			24,400
(Goods sold)			
Joint Venture A/c	Dr.	1,220	
To Commission A/c			1,220
(Commission charged)			
Joint Venture A/c	Dr.	2,520	
To Rakesh			840
To Jaipal			840
To P & L A/c			840
(Being the division of profits)			
Rakesh Account	Dr.	7,240	
Jaipal Account	Dr.	7,240	
To Bank Account			14,480
(Amount paid to them)			

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Dr.	Joint Venture Account		Cr.
	Rs		Rs
To Cash–Purchase	14,400	By Cash–Sales	24,400
To Purchase–Transfer	4,800		
To Cash–Expenses	1,460		
To Commission	1,220		
To Profit:			
Profit & Loss A/c	840		
Rakesh A/c	840		
Jaipal A/c	840		
	24,400		24,400

Dr.	Rakesh Account		Cr.
	Rs		Rs
To Bank A/c	7,240	By Cash	6,400
		By Joint Venture (Profit)	840
	7,240		7,240

Dr.	Jaipal Account		Cr.
	Rs		Rs
To Bank A/c	7,240	By Cash	6,400
		By Joint Venture (Profit)	840
	7,240		7,240

Illustration 2:

A and B entered into a Joint Venture for purchase and sale of jute. They agreed to share profits in the proportion of 2: 1 and also to be entitled to an interest of 6% p.a. (on monthly basis) on capital invested by each of them.

The following transactions took place in between themselves:

1. On June 1, A purchased 1,400 bales of jute @ Rs 55 per bale, the brokerage being Rs 2 per bale.

3. On August 1, B sold 700 bales of jute @ Rs 69 per bale, the brokerage being Re l per bale and took the proceeds to himself.

4. On August 15, A sold 1,600 bales of jute @ Rs 66 per bale, brokerage @ Re 1 per bale and took the sale proceeds to himself.

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It was also agreed that each of the partners will at first sell from his own purchase and then, if required, from the stock purchased by the other one. The balance of stock was to be divided between the partners in proportion of their profit sharing ratio-the goods being valued at cost to the partner concerned.

On August 31, the partners settled their accounts. Prepare necessary accounts assuming a separate set of books is opened.

Solution:

Dr. **Joint Venture Account** Cr.

			Rs				Rs
June 1	To *A* A/c:			Aug. 1	By *B* A/c		
	Purchase 1400 @ 55	77,000			Sales	48,300	
	Add: Brokerage	2,800	79,800		Less: Brokerage	700	47,600
July	To *B* A/c:				By *A* A/c:		
	Purchase 1200 @ 62	74,400			Sales	1,05,600	
	Add: Brokerage	2,400	76,800		Less: Brokerage	1,600	1,04,000
Aug. 31	To *A* A/c				By *A* A/c		
	Interest on Capital Invested		998		Stock taken over		12,800
Aug. 31	To *B* A/c				By *B* A/c		
	Interest on Capital		530		Stock taken over		6,400
Aug. 31	To Profit transferred to:						
	A A/c (2/3)	8,448					
	B A/c (1/3)	4,224	12,672				
			1,70,800				1,70,800

Dr. **Co-Venturers Account** Cr.

		A	*B*			*A*	*B*
		Rs	*Rs*			*Rs*	*Rs*
Aug. 1	To Joint Venture A/c			June 1	By Joint Venture A/c		
	Sales less brokerage		47,600		Purchases and brokerage	79,800	
Aug. 15	To Joint Venture A/c				By Joint Venture A/c		
	Sales less brokerage	1,04,000			Purchases and brokerage		76,800
Aug. 31	To Joint Venture A/c				By Joint Venture A/c		
	Stock taken over	12,800	6,400		Interest on Capital	998	530
Aug. 31	To Bank A/c				By Joint Venture A/c		
	(A)		27,554		Profit	8,448	4,224
					By Bank A/c		
					(*B*)	27,554	
		1,16,800	81,554			1,16,800	81,554

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Interest Calculation:

For *A*:

Interest for Rs 76,800 for 2½ months *i.e.* from 1st June to 15th Aug. @ 6% p.a.

$$\frac{\text{Rs } 79{,}800 \times 2\tfrac{1}{2} \times 6}{12 \times 100} = \text{Rs } 998$$

For B:

Interest for Rs 76,800 for one month *i.e.* from 1st July to 1st Aug. @ 6% p.a.

$$\frac{\text{Rs } 76{,}800 \times 1 \times 6}{12 \times 100} = \text{Rs } 384$$

Interest for Rs 29,200 (76,800 – 47,600) for one month *i.e.* 1st Aug. to 31st Aug. @ 6% p.a.

$$\frac{\text{Rs } 29{,}200 \times 1 \times 6}{12 \times 100} = \text{Rs } 146$$

Total = Rs 530

Stock taken over by *A* and *B*:

Unsold stock = 300 bales, out of B's purchase

Value of one bale = Rs 62 + Rs 2 = Rs 64

$$A \text{ takes } 2/3 \text{ of } 300 \text{ bales} = \frac{300 \times 2 \times 64}{3} = \text{Rs } 12{,}800$$

$$B \text{ takes } 1/3 \text{ of } 300 \text{ bales} = \frac{300 \times 1 \times 64}{3} = \text{Rs } 6{,}400$$

Royalty Accounts:

Q.1. What journal entries are passed relating to rovalties in the books of lessee and landlord?

Ans. Journal Entries in the Books of Lessee:

A) Case 1: When Royalty is Less than Minimum Rent

1. When royalty is payable:

Royalty A/C Dr.

S.W.A/C Dr.

To Landlord A/C

(Being royalty earned and shortworkings to be payable to the landlord)

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2. When payment of royalty is made:

Landlord A/c Dr.

To Bank A/C

(Being amount paid to landlord)

3. For closing royalty account at the end of the year:

P&L A/C Dr.

To Royalty

(Being the amount of royalties transferred to P&L A/C)

(B) Case II: When Royalty is equal to minimum rent

1. When royalty is payable:

Royalty A/C Dr.

To Landlord A/C

(Being royalties earned and payable to landlord)

2. When amount of royalty is paid:

Landlord A/C Dr.

To Bank A/C

(Being payment made to landlord)

3. When royalty account is closed at the end of year:

P&LA/C Dr.

To Royalty A/C

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(Being the transfer of royalties to P & L A/C)

(C) Case III: When Royalty is More than Minimum Rent

1. When royalty is payable:

Royalty A/C Dr.

To Landlord A/C

(Being royalties earned and payable to landlord)

2. For writing off shortworking, if any

Landlord A/C Dr.

To Shortworkings A/C

(Being recoupment of S.W. of earlier year)

3. For payment of royalty is made:

Landlord A/C Dr.

To Bank A/c

(Being payment made to landlord) In place of above 2. and 3. entries following one entry may be passed; .

Landlord A/C Dr.

To Bank A/C

To Shortworkings A/C

4. For closing royalty account at the end of the year:

P&L A/c Dr.

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To Royalty A/C

(Being amount of royalties transferred to P&L A/c)

Note: When royalty is payable monthly, quarterly or half-yearly, royalty will be transferred to profit & loss not when the royalty is paid but at the end of each year.

Journal Entries in the Books of Landlord

(A) Case I: When Royalty is Less than Minimum Rent

1. At the time when royalty is receivable:

Lessee A/C Dr.

To Royalty receivable A/c

To Royalty reserve A/C

(Being the amount of royalty receivable earned and diff. between minimum rent and royalty receivable transferred to royalty reserve A/c)

2. When above amount is received:

Bank A/c Dr.

To Lessee A/C

(Being the amount received from lessee)

3. For closing royalty receivable account:

Royalty receivable A/c Dr.

To P&L A/C

(Being amount of royalty receivable transferred to P&L)

(B) Case II: When Royalty Receivable is Equal to Minimum Rent

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1. At the time when royalty is receivable:

Lessee A/C Dr.

To Royalty receivable A/c

(Being the royalty receivable earned)

2. On receipt of the amount:

Bank A/C

To Lessee A/C

(Being the amount received from lessee)

3. For closing royalty receivable account:

Royalty receivable A/C Dr.

To P&L A/C

(Being transfer of royalty receivable A/c to P&L A/C)

(c) Case III:When Royalty is More than Minimum Rent:

1. At the time when royalty is receivable:

Lessee A/C

To Royalty receivable A/C

(Being the amount of royalty receivable earned)

2. For writing of royalty reserve A/c

Royalty reserve A/C Dr.

To Lessee A/C

`

(Being royalty reserve recouped)

3. On receipt of royalty amount:

Bank A/C Dr.

To Lessee A/C

(Being amount received from lessee)

Combined entry may be passed for 2. and 3. above. Bank A/C Dr.

Royalty reserve A/C Dr.

To Lessee A/C

(Being amount received and royalty reserve recouped)

4. For closing royalty receivable account:

Royalty receivable A/C

To P&L A/C

(Being transfer of royalty receivable A/c to P & L A/c)

CONSIGNMENT ACCOUNTS:

WHAT IS CONSIGNMENT?

Consignment is a business arrangement between a consignor (owner) and a third party (consignee). This word has come from the French word "consigner" which means 'to hand over or to transmit'. The consignee agrees to sell the goods handed over to him by the consignor for a fee. For the consignor, it is outward consignment and for the consignee, it is inward consignment. Also, there is another similar term called consignment shop. The consignment shop is a retail store which displays goods for the buyers for sale.

FEATURES OF CONSIGNMENT

- The **possession** of the goods **transfers** from one party to another.

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- The **consignor** is **responsible** for all the risks, expenses and damages associated with the consigned goods.
- The **relation** of the persons in the consignment is that of consignor (principal) and the consignee (agent) and not of the buyer and seller.
- Only the **possession** of the goods is with the consignee and **not** the **ownership**.
- **Profit or loss** on the sale of the goods belongs to the consignor.
- The consignor sends **Pro-forma Invoice**. While the consignee sends **Account Sales**. Account Sales include the details regarding the goods, sales, expenses, commission, advances, and balances due.

OBJECTIVES OF CONSIGNMENT

- To make large consignments and increase sales volume by attracting customers.
- To launch a new product and create and capture the market for the same.
- Earning higher revenue from a different geographical area for the same product.
- To grow and expand the business.
- Sustainment in the domestic and international market.
- To increase sales by utilizing the talent and expertise of the consignee.

WORKING OF CONSIGNMENT

The consignor sends the goods on consignment to the consignee. The consignee will separate the goods suitable for sales and the ones not suitable (usually torn, dirty goods which may be unsaleable in some jurisdiction). However, until there is an actual sale of the goods to a buyer, one cannot treat those goods as a sale. The terms are predecided for the revenue distribution of the sales and the time period for the goods held for sale. If the goods are not sold within that time period, the consignor reclaims those goods. However, there can be an extension in the time period if it is allowed as per the agreement. In the end, there is a final payment by the consignee to the consignor for the sales proceeds less his part of commission and expenses.

Suppose there is a consignor 'Ohlin' who consigns his 20 musical instruments to a consignee 'Richard'. Richard pays some money in the form of advance to Ohlin. Here there is a transfer of the possession of the goods but not the ownership. However, Richard could only sell 18 instruments and agrees to buy the rest two at a 5% lesser price than the market price. Ohlin agrees for the same. If the instruments would have not yet been purchased by any, then the Ohlin would repossess them. At the last, Richard will do a final payment of the balances due by and to him. He will deduct his part of commission, expenses and obviously the advance.

ADVANTAGES OF CONSIGNMENT AND

ADVANTAGES FOR CONSIGNOR

- Increased sales and margin if the consignor is assigning the responsibility of the goods to a skilled and experienced consignee.
- Since the ownership is with the consignor, he may at any time reclaim those goods in the case of any default from the consignee's end.
- Inventory holding costs are lessened as the goods are sent to the consignee and are in his possession.
- If the sellers want to increase their sales and do not have time to promote their product or look after the customers, they prefer hiring an agent to look after the same.

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- If the consignee is well versed with the buyers, market, product, etc. he may sell the product very fast. Hence this would lead to product expansion, better market share, increased sales, etc.

ADVANTAGES FOR CONSIGNEE

- The consignee has to pay for only those goods that are sold.
- The consignee sometimes doesn't have to pay for some expenses if it agreed as per the agreement.
- If the consignee is well versed with the product, he may sell the goods faster thereby increasing his share of revenue.
- In the case of huge demand, he may earn higher revenue. As he need not incur any expense of the shipping also not to worry about the lead time.

DISADVANTAGES FOR CONSIGNOR

- Since the consignee is not the owner and doesn't face any monetary risk, he may not take this agreement seriously. Hence, he may not promote sales.
- Sometimes the consignor pays huge shipping charges by shipping a large amount of inventory instead of paying for smaller inventories to the consignee. However, the goods may or may not sell. So, if the goods don't sell, he suffers a huge loss as he remains to be the owner and they still have to count it as a part of his cost assessment.
- The consignor has to keep waiting for the payment creating uncertainty in regards to when and how much will be receipt of the sales proceeds from the consignee. So, until there is a sale of all or some of the goods, the consignor has to wait for the payment leading to an imbalance in cash flows.
- If the consignor sells the product directly into the market, he may earn comparatively higher revenue by removing the excess profit margin of the consignee.

DISADVANTAGES FOR CONSIGNEE

- If the consignee carries a bad reputation in a particular market, he may not be able to sell the goods so easily.
- The biggest con for the consignee is that he incurs a holding cost for that inventory either in his godown or in his store. That inventory may or may not sell. So, in the case of unsold goods, he suffers a loss.
- If the consignee repeatedly fails to sell the goods in time, he may either be discarded as an agent or would receive a lesser commission.
- If in the case of no sale of the goods and there is a possibility of it getting deteriorated, the consignee may have to buy them.

The main differences between consignment and joint venture are as follows:

- **Nature of Relationship**
  Joint Venture: It is a temporary partnership between two or more parties.
  Consignment: It refers to a principal (seller) sending goods to his agent (buyer) for sale to third parties.

- **Parties**

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Joint Venture: The participants in a joint venture are called co-ventures.
Consignment: The parties to a consignment agreement are known as consignor and consignee.

- **Relationship**
  Joint Venture: The relationship between co-ventures is like that of partners in a partnership.
  Consignment: The relationship between consignor and consignee is a principal-agent relation.

- **Profit Sharing**
  Joint Venture: Co-ventures share the profits and losses of the joint venture in their agreed proportion.
  Consignment: The consignor and consignee do not share profits; the consignee receives a commission.

- **All Rights**
  Joint Venture: The co-ventures enjoy equal rights in a joint venture.
  Consignment: The consignor and consignee do not enjoy equal rights. The consignor has the rights of a principal and the consignee those of an agent.

- **Governing Act**
  Joint Venture: The joint venture is governed either by the contract law in each U.S. state or the business organizations acts of each U.S. state.
  Consignment: The relation between the consignor (seller) and the consignee (buyer) is governed by Law of Agency because it involves a principal – agent relation.

- **Powers**
  Joint Venture: Co-ventures have unlimited powers with respect to the joint venture.
  Consignment: The consignee’s powers are limited. The consignee is the agent who follows instructions from the consignor.

- **Ownership**
  Joint Venture: The co-ventures are the co-owners of the joint venture.
  Consignment: The consignor is the owner of the business activity – the goods.

- **Information Sharing**
  Joint Venture: The co-ventures share the required information on a regular basis.
  Consignment: The consignee prepares and shares an account of sales with the consignor detailing the business activities carried on.

- **Maintenance of Accounts**
  Joint Venture: The co-ventures maintain the accounts as specified in the joint venture agreement.
  Consignment: There is only one method of maintaining the accounts of the consignment.

- **Basis of Accounting**
  Joint Venture: In joint venture cash basis of accounting is applied.
  Consignment: Actual basis of accounting is applicable.

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- **Continuity**
  Joint Venture: The joint venture terminates when the venture is completed.
  Consignment: The consignment is continuous for as long as both the consignor and consignee agree.

Accounting treatment in the Books of Consignor

The relationship between consignor and consignee is that of the principal and the agent. So entire profit or loss belongs to the consignor and consignee receives the commission as his remuneration.

Journal entries in the books of Consignor

Date	**Particulars**		**Amount (Dr.)**	**Amount (Cr.)**
1.Entry for sending goods	Consignment a/c	Dr.	xxxx	
	To Goods send on consignment a/c			xxxx
	(Being goods sent on the consignment basis)			
2.Entry for consignor's expenses	Consignment a/c	Dr.	xxxx	

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	To Cash/Bank a/c			xxxx
	(Being expenses for consignment)			
3.Entry for consignee’s expenses	Consignment a/c	Dr.	xxxx	
	To Consignee a/c			xxxx
	(Being expenses for consignment by consignee)			
4.Entry for advance given by consignee	Cash/Bank/B.R. a/c	Dr.	xxxx	
	To Consignee a/c			xxxx
	(Being receipt of advance)			
5.Entry for sales	Consignee a/c	Dr.	xxxx	
	To Consignment a/c			xxxx
	(Being sale of goods)			
6.Entry for commission	Consignment a/c	Dr.	xxxx	
	To Consignee			xxxx

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	(Being commission recorded)			
7.Entry for collection from debtors	No Entry			
8.Entry for Bad Debts				
(a)In the presence of Del-credre commission	No entry			
(b) In the absence of Del-credre commission	Consignment a/c	Dr.	xxxx	
	To Consignee a/c			xxxx
	(Being bad debts recorded)			
9.Entry for the final profit	Consignment a/c	Dr.	xxxx	
	To Profit and loss a/c			xxxx
	(Being transfer of profit to P&L a/c)			
10.Entry for final remittance	Bank a/c	Dr.	xxxx	

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	To Consignee			xxxx
	(Being payment to consignee)			
11. Entry for Balance in Goods sent a/c	Goods sent consignment a/c	Dr.	xxxx	
	To Trading a/c			xxxx
	(Being balance transferred to trading account)			
12.Entry for the closing stock	Consignment stock a/c	Dr.	xxxx	
	To Consignment a/c			
	(Being closing stock transferred)			

Q. Ram sent on 1st April 2016 to Sham goods costing Rs. 100000 and spent Rs. 2000 on packing etc. On 3rd April 2016 Sham received the goods and sent his acceptance to Ram and given Rs.60000 as advance. Sham spent Rs.2000 on freight and cartage, Rs.1000 on godown rent and 600 on insurance. On 31st Dec 2016, he sends his account sales(along with the amount due to Sham) showing that the sale is of 4/5 of the goods for Rs.110000. The terms of the consignment entitle Sham to a commission of 10 %. One of the customers turned insolvent and could not pay Rs.1200 due to him. Show the necessary general entries in the books of the consignor. Also, prepare ledger accounts.

Journal entries in the books of consignor

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Date	Particulars		Amount (Dr.)	Amount (Cr.
2016				
April 1	Consignment to Sham a/c	Dr.	100000	
	To Goods send on consignment a/c			100000
	(Being goods sent on the consignment basis)			
April 1	Consignment to Sham a/c	Dr.	2000	
	To Cash/Bank a/c			2000
	(Being expenses on consignment)			
April 3	Bank a/c	Dr.	60000	
	To Sham			60000

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	(Being receipt of advance)			
Dec 31	Sham a/c	Dr.	110000	
	To Consignment a/c			110000
	(Being sale of goods)			
Dec 31	Consignment to Sham a/c (4000+1000+600+1200)	Dr.	6800	
	To Sham a/c			6800
	(Being expenses incurred by Sham)			
Dec 31	Consignment to Sham (10%on 110000)	Dr.	11000	
	Sham a/c			11000

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	(Being commission recorded)			
Dec 31	Bank a/c	Dr.	32200	
	To Sham			32200
	(Being receipt of amount)			
Dec 31	Consignment Stock a/c (working note 1)	Dr.	21200	
	To Consignment to Sham a/c			21200
	(Being unsold stock recorded)			
Dec 31	Consignment to Sham a/c	Dr.	11400	
	To Profit and loss a/c			11400
	(Being profit)			

`

Dec 31	Goods sent on consignment a/c	Dr.	100000	
	To Trading a/c			100000
	(Being balance transferred to trading account)			

Ledgers Accounts

Consignment to Sham A/c

Date	**Particulars**	**Amount**		**Date**	**Particulars**	**Amount**
April 1	To goods sent on consignment a/c	100000		Dec 31	By Sham(sale proceeds)	110000
April 1	To Bank(expenses)	2000		Dec 31	By stock on consignment a/c	21200
Dec 31	To Sham(expenses &bad debts)	6800				
Dec	To Sham(commission)	11000				

`

31						
Dec 31	To P&L	11400				
		131200				**131200**

Goods sent on consignment A/c

Date	**Particulars**	**Amount**		**Date**	**Particulars**	**Amount**
Dec 31	To Trading a/c	100000		Dec 31	By consignment to Sham a/c	10000
		100000				**100000**

Stock on consignment A/c

Date	**Particulars**	**Amount**		**Date**	**Particulars**	**Amount**
Dec	To consignment	21200		Dec	By Balance c/d	21200

`

31	to Sham a/c			31		

Sham A/c

Date	**Particulars**	**Amount**		**Date**	**Particulars**	**Amount**
Dec 31	To consignment to Sham a/c	110000		May 3	By Bank	60000
				Dec 31	By consignment to sham a/c	6800
				Dec 31	By consignment to sham a/c	11000
				Dec 31	By Bank (Bal. Received)	32200
		110000				**110000**

Practice Questions:

1.Define the meaning of accounting, Accountancy and book keeping?
2.Difference between Financial accounting and book keeping and accountancy?
3.What is Accounting Equation?
4.Explain the term accounting cycle?

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5.Explain the following terms:
Journal Ledger Trial Balance
6.Give the full detail of financial accounting? Define meaning, nature, scope, objectives and limitations?
7.What is financial statement of sole proprietor?
8. What is financial statement of Partnership?
9. What is joint venture? Explain the all types of joint venture?
10.Write the full entries of joint venture (1-4) methods?

UNIT-III

Voyage Accounts– Meaning, accounting treatment in case of complete voyage & incomplete voyage, Departmental Accounts – Meaning – Objects – Advantages – Accounting procedure – Apportionment of Expenses and incomes – Interdepartmental transfers – Provision for unrealized profit.

Meaning of Voyage Account:
The method of accounting followed by shipping companies is known as voyage accounting. Shipping companies prepare their accounts periodically and also prepare the results of each voyage separately. Shipping companies carry goods from one place to another. Some companies carry passengers also in addition to goods from one place to another place.

In order to ascertain the result of operating a ship's voyage, Voyage Account is prepared. The Voyage Account is a revenue account. It is important to note that there is no difference in the manner of preparing accounts period-wise and voyage-wise.

All expenses connected with the voyage, such as port charges, wages and salaries of the crew, captain and other staff, transshipment, agency fees, provisions, loading and unloading charges, bunker and harbour wages, freight and insurance, insurance of the ship on a time policy according to duration of voyage, depreciation arising as a result of the journey, address commission paid to brokers for freight for the ship, commission to captain on net profit etc. are debited to concerned Voyage Account.

All incomes such as freight on cargo carried, passage money, primate etc. are credited.

Income

Following are the main sources of income of a Voyage −

- **Freight** − Freight charges are the main income collected against the transportation of the goods.
- **Passage Money** − Passage money is collected from the passengers, in case it is passengers' vessel.

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- **Primage** − Primage is an additional freight in the form of surcharge on the freight.

Expenses

Following are the various ways of expenses of a vessel −

- **Brokerage & Commission** − Brokerage and commission is calculated on the freight charges including primage and it is paid to the charters agent. Address commission is payable to the brokers on procurements of freight from the different parties.
- **Insurance** − The insurance charges on proportionate basis might be debited from the voyage account. For example, if insurance is for one year and journey of voyage is for three month, insurance charges will be debited from the voyage account on 14th14th ratio.
- **Stores** − Stores, which are purchased for voyage are debited from the voyage account on consumption basis i.e. opening stock + purchases – closing stock.
- **Depreciation** − Depreciation on ship is charged from the voyage account in the proportion of the period of a journey.
- **Bunker Cost** − Cost of water, coal, diesel, fuel, etc. used for the purpose of voyage is called bunker cost and may debited from the voyage account.
- **Port Charges** − Port authorities charge fees for allowing ships to use port for the loading/unloading the cargo. This fee amount is debited from the voyage account.
- **Stevedoring Charges** − Loading and unloading of cargo called stevedoring charges and should be debited from the voyage account.

Voyage in Progress

At the end of the accounting year where voyage is not completed and is still in progress, following accounting treatments are required −

Freight Received

Total freight received credited to the voyage account and the provision for incomplete voyage is debited from the voyage account. Provision is created for the voyage-in-progress in proportion of the incomplete journey.

Expenses

To complete matching concept, an income as well as expenses related to the incomplete voyage might be carried forward to the next accounting year on the respective account. Provision for the income earned should be debited from the voyage account and provision for the expenses should also be credited to the voyage account.

Basis of the expenses to be carried forward is as hereunder −

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- Expenses which are related to the freight, need to be carried forward in a proportion to return freight. For example, if total freight is Rs. 2,500,000 out of which return freight is Rs. 1,200,000 and total expenses are Rs. 500,000, then expenses to be carried forward to the next accounting year — will be Rs. 240,000.

=1,200,0002,500,000×500,000=1,200,0002,500,000×500,000

- In case of the standing expenses, if return journey is incomplete, ½ of the standing charges to be carried forward.

- In case where return journey is halfway back and the total expenses of voyage given 1212 of the total expenses to be carried forward.
- When the return journey is halfway back and the expenses till date are given 13rd13rd of the expense are to be carried forward.
- When one round of the trip is completed and on his half way back for single way and total expenses of voyage are given, then 13rd13rd expenses are to be carried forward.
- When one round trip is completed and on his half way back for single way and expenses till date are given, then 15th15th expenses are to be carried forward.

Pro-forma

In the books of M/s Titanic Shipping Company

Voyage Account

For the period ending 31-12-2014

Particulars	Amount	Particulars	Amount
To Coal Opening Stockxx Add: Purchasesxx --------- xxxx Less: Closing Stockxx --------- To Port Charges To Captain Expenses To Harbor Wages	xx	By Freight By Primage	Xx Xx

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To Address Commission	xx		
To Brokerage	xx		
To Insurance Premium	xx		
To Salary & Wages	xx		
To Stores	xx		
To Deprecation	xx		
To Provision for Incomplete	xx		
Voyage	xx		
To Net Profit	xx		
(trf. To Profit & Loss A/c)	xx		
	xx		

	XXXX		

			XXXX

`

Following are some of the items of income and expenditure peculiar to Voyage Accounts.
Accounting Entries- Debit and Credit:
Voyage Account is debited usually with the following items:
1. Bunker Cost:
This is the expenditure incurred on fuel oil, diesel, coal and fresh water used during the voyage. Now-a-days oil and diesel are used in place of coal. The bin or storing place of coal is referred to as bunker. Hence the name bunker costs.

2. Port Charges:
Port is used by the shipping companies for loading and unloading of goods and parking of ships, hence the charges paid for these purposes are known as port charges.

3. Depreciation:
Depreciation of the ship for the period of voyage is calculated and charged to the Voyage Account.

4. Insurance:
Insurance premium of cargo must be entirely debited to the concerned Voyage Account whereas the insurance charges of the ship are charged proportionately to each voyage on the basis of time of voyage.

5. Address Commission and Brokerage:
This is payable to the brokers and agents who help the shipping company in procurement of cargo, i.e., freight or business. This is calculated at a certain per cent of the freight earned including the primage or surcharge and debited to Voyage Account. Address commission is payable to the Charterer whereas brokerage is payable to the agent of the charterer.

6. Stevedoring Charges:
The expenses which are incurred in loading of goods on the ships and unloading of goods from the ships are known as stevedoring charges.

7. Port Charges:
These are the charges paid to port authorities for allowing the ship to use the port either for loading or unloading the cargo.

8. Salaries and wages of the crew, captain and other staff.

9. Harbour charges

10. Manager’s commission, if any.

Voyage Account is credited usually with the following items:

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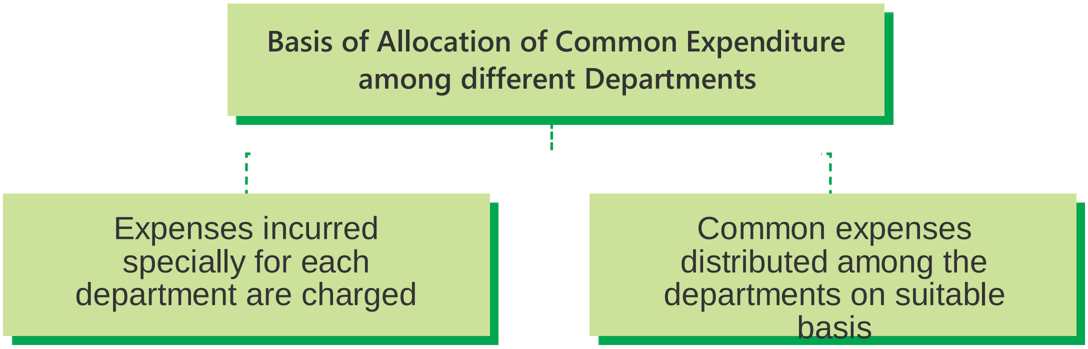
1. Freight:
The amount which is charged by the shipping companies for taking goods or cargo from one place to another is called freight. It is an income.

2. Primage:
It is additional freight just like surcharge on freight originally collected for the captain of the ship, now-a-days it is treated as income of the shipping company.

3. Passage Money:
Fare collected from the passengers travelled in addition to the fare collected for merchandise.

4. Closing Stocks of Stores, Provisions, Coal, Fuel etc.
Generally, voyage profit represents the excess of voyage incomes earned over the expenses incurred for this purpose. But if, however, the voyage is in progress, the incomes and expenses relating to the unfinished voyage are carried forward to the next year.

Excess of credit side of Voyage Account over its debit side is profit on the voyage. Excess of debit side of Voyage Account over its credit side is loss on the voyage. This profit or loss is transferred to General Profit and Loss Account of the shipping company.



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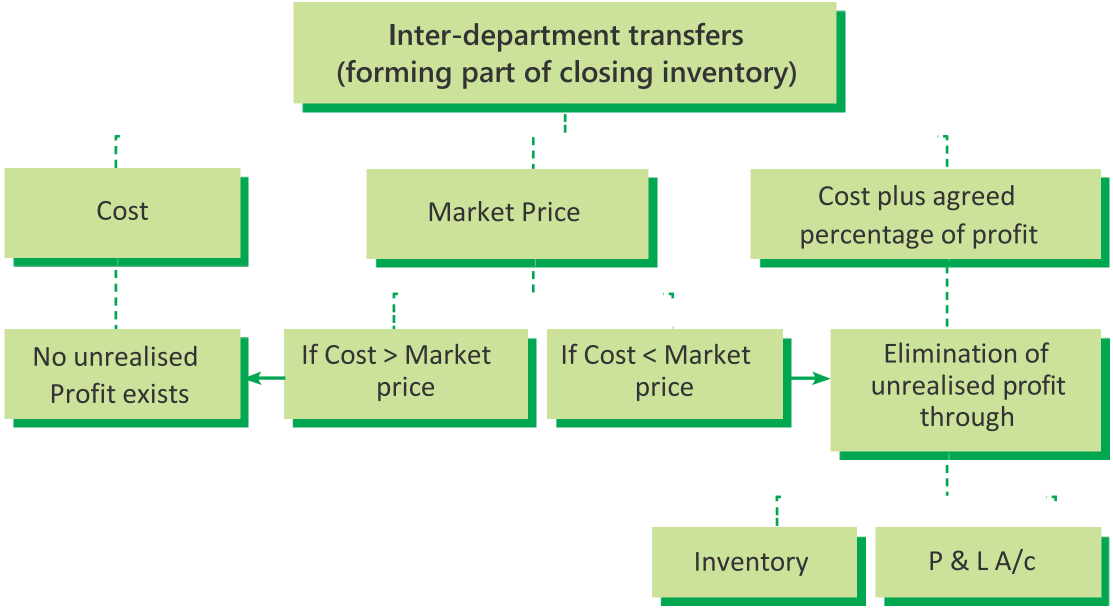


Inter-department transfers
(forming part of closing inventory)
Cost
Market Price
Cost plus agreed percentage of profit
No unrealised Profit exists
If Cost > Market price
If Cost < Market price
Elimination of unrealised profit through
Inventory
P & L A/c

DEPARTMENTAL ACCOUNTING

If a business consists of several independent activities, or is divided into several departments, for carrying on separate functions, its management is usually interested in finding out the working results of each department to ascertain their relative efficiencies. This can be made possible only if departmental accounts are prepared. Departmental accounts are of great help and assistance to the managements as they provide necessary information for controlling the business more intelligently and effectively. It is also helpful in readily identifying all types of wastages, e.g., wastage of material or of money; Also, attention is drawn to inadequacies or inefficiencies in the working of departments or units into which the business may be divided.

2. ADVANTAGES OFDEPARTMENTAL ACCOUNTING

The main advantages of departmental accounting are as follows:

1. ***Evaluation of performance*** : The performance of each department can be evaluated separately on the basis of trading results. An endeavour may be made to push up the sales of that department which is earning maximum profit.
2. ***Growth potential of each department*** : The growth potential of a department as compared to others can be evaluated.
3. ***Justification of capital outlay*** : It helps the management to determine the justification of capital outlay in each department.
4. ***Judgement of efficiency*** : It helps to calculate stock turnover ratio of each department separately, and thus the efficiency of each department can be revealed.
5. ***Planning and control :*** Availability of separate cost and profit figures for each department facilitates better control. Thus effective planning and control can be achieved on the basis of departmental accounting information.

Basically, an organisation usually divides the work in various departments, which is done on the principle of division of labour. Each department prepares its separate accounts to judge its individual performance. This can improve efficiency of each and every department of the organisation.

3. METHODS OFDEPARTMENTAL ACCOUNTING

There are two methods of keeping departmental accounts:

3.1 Accounts of all departments are kept in one book only

To prepare such accounts, it will be necessary first, for the income and expenditure of department to be separately recorded in subsidiary books and then for them to be accumulated under separate heads in a ledger or ledgers. This may be done by having columnar subsidiary books and a columnar ledger.

3.2 Separate set of books are kept for each department

A separate set of books may be kept for each department, including complete stock accounts of goods received from or transferred to other departments or as also sales.

Nevertheless, even when separate sets of books are maintained for different departments, it will also be necessary to devise a basis for allocation of common expenses among the different departments, if an organisation is interested in determining the separate departmental net profit in addition to the gross profit.

4. BASIS OF ALLOCATION OF COMMON EXPENDITURE AMONG DIFFERENT DEPARTMENTS

Expenses should be allocated among different departments on a rational basis while preparing departmental accounts.

Individual Identifiable Expenses: Expenses incurred specially for a particular department are charged directly thereto, e.g., insurance charges of stock held by the department.

Common Expenses : Common expenses, the benefit of which is shared by all the departments and which are capable of precise allocation are distributed among the departments concerned on some equitable basis considered suitable in the circumstances of the case.

Allocation of Expenses

S. No.	*Expenses*	*Basis*
1.	*Rent, rates and taxes, repairs and maintenance, insurance of building*	*Floor area occupied by each department (if given) other wise on time basis*
2.	*Lighting and Heating expenses (e.g., energy expenses)*	*Consumption of energy by each department*
3.	*Selling expenses, e.g., discount, bad debts, selling commission, freight outward, travelling sales manager's salary and other costs*	*Sales of each department*
4.	*Carriage inward/ Discount received*	*Purchases of each department*
5.	*Wages/Salaries*	*Time devoted to each department*
6.	*Depreciation, insurance, repairs and maintenance of capital assets*	*Value of assets of each department otherwise on time basis*
7.	*Administrative and other expenses, e.g., salaries of managers, directors, common advertisement expenses, etc.*	*Time basis or equally among all departments*
8.	*Labour welfare expenses*	*Number of employees in each department*
9.	*PF/ESI contributions*	*Wages and salaries of each department*

Note : There are certain expenses and income, most being of financial nature, which cannot be apportioned on a suitable basis; therefore they are recognised in the combined Profit and Loss Account, for example, interest on loan, profit/loss on sale of investment, etc.

5. TYPES OF DEPARTMENTS

There are two types of departments: Dependent and Independent Departments.

5.1 Independent Departments

Departments which work independently of each other and have negligible inter-department transfers are called Independent Departments.

5.2 Dependent Departments

Departments which transfer goods from one department to another department for further processing are called dependent departments. Here, the output of one department becomes the input for the other department. These transfers may be done at cost or some pre-decided selling price. The price at which this is done is known as transfer price. In these departments, unloading is required if the transfer price is having a profit element. The method of eliminating unrealised profit is being discussed in the succeeding para.

6. INTER-DEPARTMENTAL TRANSFERS

Whenever goods or services are provided by one department to another, their cost should be separately recorded and charged to the department benefiting thereby and credited to that providing the goods or services. The totals of such benefits (inter-departmental transfers) should be disclosed in the departmental Profit and Loss Account, to distinguish them from other items of expenditure.

6.1 Basis of Inter-Departmental Transfers

Goods and services may be charged by one department to another usually on either of the following three bases:

(i) Cost,

(ii) Current market price,

(iii) Cost plus agreed percentage of profit.

6.2 Stock Reserve

Unrealised profit included in unsold stock at the end of accounting period is eliminated by creating an appropriate stock reserve by debiting the combined Profit and Loss Account. The amount of stock reserve will be calculated as:

$$\frac{\text{Transfer price of unsold stock} \times \text{Profit included in transfer}}{\text{price Transfer price}}$$

6.3 Journal Entry

At the end of the accounting year, the following journal entry will be passed for elimination of unrealised profit (creation of stock reserve):

Profit and Loss Account Dr.

  To Stock Reserve

(Being a provision made for unrealised profit included in closing stock)

In the beginning of the next accounting year, the aforesaid journal entry will be reversed as under:

Stock Reserve Dr.

  To Profit and Loss Account

(Being provision for unrealised profit reversed.)

6.4 Disclosure in Balance Sheet

The unsold closing stock acquired from another department will appear on the assets side of the balance sheet as under:

(An extract of the assets side of the balance sheet)

Current assets	xxx	
Stock	xxx	
Less: Stock reserve	xxx	
		xxx

7. MEMORANDUM STOCK AND MEMORANDUM MARK UP ACCOUNTMETHOD

Under this method, goods supplied to each department are debited to a Memorandum Departmental Stock account at cost plus a ‘mark up’ (loading) to give the normal selling price of the goods. The sale proceeds of the department are credited in Memorandum Departmental Stock account and amount of ‘Mark up’ is credited to the Departmental Mark up Account. When it is necessary to reduce the selling price below the normal selling price, i.e., cost plus mark up, the reduction (mark down) is entered in the Memorandum Stock account as well as in the Mark up account. This method helps to achieve effective control of stock movements of various departments.

Illustration 1

Goods are transferred from Department P to Department Q at a price 50% above cost. If closing stock of Department Q is ` 27,000, compute the amount of stock reserve.

Answer

	`
Closing Stock of Department Q	27,000
Goods send by Department P to Department Q at a price 50% above cost	
Hence profit of Department P included in the stock will be - $\frac{27,000 \text{ X } 50}{150}$	9,000
Amount of the Stock Reserve will be ` 9,000.	

Working Note :

Dept P transfers goods to Dept Q at a profit of 50% of cost. Hence, if cost is ` 100/- the profit = ` 50 and Transfer Price = ` 150. Therefore, the profit of Dept P included in the stock value of Dept Q is one – third of the sale value

Illustration 2

Z Ltd. has three departments and submits the following information for the year ending on 31st March, 20X1:

	A	B	C	Total (`)
Purchases (units)	*6,000*	*12,000*	*14,400*	
Purchases				*6,00,000*
(Amount) Sales	*6,120*	*11,520*	*14,976*	
(Units)	*40*	*45*	*50*	
Selling Price (per unit) `	*600*	*960*	*36*	
Closing Stock (Units)				

You are required to prepare departmental trading account of Z Ltd., assuming that the rate of profit on sales is uniform in each case.

Answer

Departmental Trading Account for the year ended on 31st March, 20X1

Particulars	A	B	C	Particulars	A	B	C
To Opening Stock (W.N.4.)	11,520	8,640	12,240	By Sales A-6120×40 B-11,520×45 C-14,976×50	2,44,80 0	5,18,40 0	7,48,80 0

`

		A	B	C			A	B	C
To	Purchases (W.N.2)	96,000	2,16,000	2,88,000	By	Closing Stock (W.N.4)	9,600	17,280	720
To	Gross Profit (b.f.)	1,46,880	3,11,040	4,49,280					
		2,54,400	5,35,680	7,49,520			2,54,400	5,35,680	7,49,520

(1) Working Notes:

	Profit Margin Ratio	`
	Selling price of unit purchased:	
	Department A 6,000 x 40	2,40,000
	Department B 12,000 x 45	5,40,000
	Department C 14,400 x	7,20,000
	50 Total Selling Price	15,00,000
	Less: Purchase (Cost) Value	(6,00,000)
	Gross Profit	9,00,000
	Profit Margin Ratio = $\frac{9,00,000}{15,00,000}$ = 60%	

(2) Statement showing department-wise per unit Cost and Purchase Cost

	A	B	C
	`	`	`
Selling Price (Per unit) (`)	40	45	50
Less : Profit Margin @ 60% (`)			
Profit Margin is uniform for all depts at 60%	(24)	(27)	(30)
Purchase price per unit (`)	16	18	20
Number of units purchased	6,000	12,000	14,400
(Purchase cost per unit x Units purchased)	96,000	2,16,000	2,88,000

(3) Statement showing calculation of department-wise Opening Stock (in Units)

	A	B	C
Sales (Units)	6,120	11,520	14,976
Add: Closing Stock (Units)	600	960	36
	6,720	12,480	15,012
Less: Purchases (units)	(6,000)	(12,000)	(14,400)
Opening Stock (Units)	720	480	612

`

(4) Statement showing department-wise cost of Opening Stock and Closing Stock

	A	B	C
Cost of Opening Stock (`)	720 x 16 11,520	480 x 18 8,640	612 x 20 12,240
Cost of Closing Stock (`)	600 x 16 9,600	960 x 18 17,280	36 x 20 720

Illustration 3

Brahma Limited has three departments and submits the following information for the year ending on 31st March, 20X1:

Particulars	A	B	C	Total (`)
Purchases (units)	*5,000*	*10,000*	*15,000*	
Purchases (Amount)				*8,40,000*
Sales (units)	*5,200*	*9,800*	*15,300*	
Selling price (` per unit)	*40*	*45*	*50*	
Closing Stock (Units)	*400*	*600*	*700*	

You are required to prepare departmental trading account of Brahma Limited assuming that the rate of profit on sales is uniform in each case.

Answer

Departmental Trading Account for the year ended 31st March, 20X1

Particulars	A	B	C	Particulars	A	B	C
	`	`	`		`	`	`
To Opening Stock (W.N.4)	14,400	10,800	30,000	By Sales A-5,200×40 B-9,800×45 C-15,300×50	2,08,000	4,41,000	7,65,000
				By Closing Stock (W.N.4)	9,600	16,200	21,000
To Purchases (W.N.2)	1,20,000	2,70,000	4,50,000				
To Gross Profit (b.f.)	83,200	1,76,400	3,06,000				
	2,17,600	4,57,200	7,86,000		2,17,600	4,57,200	7,86,000

Working Notes :

(1) Profit Margin Ratio

Selling price of units purchased :	`
Department A (5,000 units x ` 40)	2,00,000
Department B (10,000 units x ` 45)	4,50,000
Department C (15,000 units x ` 50)	7,50,000
Total selling price of purchased units	14,00,000
Less: Purchases	(8,40,000)
Gross profit	5,60,000

$$\text{Profit margin ratio} = \frac{\text{Gross profit}}{\text{Selling price}} \text{ X } 100 = \frac{5,60,000}{14,00,000} \text{ X } 100 = 40\%$$

(2) Statement showing department-wise per unit cost and purchase cost

Particulars	A	B	C
Selling price per unit (`)	40	45	50
Less: Profit margin @ 40% (`) Profit margin is uniform for all depts.	(16)	(18)	(20)
Purchase price per unit (`)	24	27	30
No. of units purchased	5,000	10,000	15,000
Purchases (purchase cost per unit × units purchased)	1,20,000	2,70,000	4,50,000

(3) Statement showing calculation of department-wise Opening Stock (in units)

Particulars	A	B	C
Sales (Units)	5,200	9,800	15,300
Add: Closing Stock (Units)	400	600	700
	5,600	10,400	16,000
Less: Purchases (Units)	(5,000)	(10,000)	(15,000)
Opening Stock (Units)	600	400	1,000

(4) Statement showing department-wise cost of Opening and Closing Stock

	A	B	C
Cost of Opening Stock (`)	600 x 24 14,400	400 x 27 10,800	1,000 x 30 30,000
Cost of Closing Stock (`)	400 x 24 9,600	600 x 27 16,200	700 x 30 21,000

`

Illustration 4

M/s Omega is a departmental store having three departments X, Y and Z. The information regarding three departments for the year ended 31st March, 20X1 are given below:

	X	Y	Z
	`	`	`
Opening Stock	*36,000*	*24,000*	*20,000*
Purchases	*1,32,000*	*88,000*	*44,000*
Debtors at end	*15,000*	*10,000*	*10,000*
Sales	*1,80,000*	*1,35,000*	*90,000*
Closing stock	*45,000*	*17,500*	*21,000*
Value of furniture in each department	*20,000*	*20,000*	*10,000*
Floor space occupied by each department (in sq. ft.)	*3,000*	*2,500*	*2,000*
Number of employees in each Department	*25*	*20*	*15*
Electricity consumed by each department (in units)	*300*	*200*	*100*

The balances of other revenue items in the books for the year are given below:

	Amount (`)
Carriage inwards	*3,000*
Carriage outwards	*2,700*
Salaries	*48,000*
Advertisement	*2,700*
Discount allowed	*2,250*
Discount received	*1,800*
Rent, Rates and Taxes	*7,500*
Depreciation on furniture	*1,000*
Electricity expenses	*3,000*
Labour welfare expenses	*2,400*

You are required to prepare Departmental Trading and Profit and Loss Account for the year ended 31st March, 20X1 after providing provision for Bad Debts at 5%.

`

Solution

In the Books of M/s Omega
Departmental Trading and Profit and Loss Account
for the year ended 31st March, 20X1

Particulars	Deptt.X	Deptt.Y	Deptt.Z	Total	Particulars	Deptt.X	Deptt.Y	Deptt.Z	Total
	`	`	`	`		`	`	`	`
To Stock (opening)	36,000	24,000	20,000	80,000	By Sales	1,80,000	1,35,000	90,000	4,05,000
To Purchases	1,32,000	88,000	44,000	2,64,000	By Stock (closing)	45,000	17,500	21,000	83,500
To Carriage Inwards	1,500	1,000	500	3,000					
To Gross Profit c/d (b.f.)	55,500	39,500	46,500	1,41,500					
	2,25,000	1,52,500	1,11,000	4,88,500		2,25,000	1,52,500	1,11,000	4,88,500
To Carriage Outwards	1,200	900	600	2,700	By Gross Profit b/d	55,500	39,500	46,500	1,41,500
To Electricity	1,500	1,000	500	3,000	By Discount received	900	600	300	1,800
To Salaries	20,000	16,000	12,000	48,000					
To Advertisement	1,200	900	600	2,700					
To Discount allowed	1,000	750	500	2,250					
To Rent, Rates and Taxes	3,000	2,500	2,000	7,500					
To Depreciation	400	400	200	1,000					
To Provision for Bad Debts @ 5% of debtors	750	500	500	1,750					
To Labour welfare expenses	1,000	800	600	2,400					

To Net Profit (b.f.)	26,350	16,350	29,300	72,000					
	56,400	40,100	46,800	1,43,300		56,400	40,100	46,800	1,43,300

Working Note:

Basis of allocation of expenses	
Carriage inwards	Purchases (3:2:1)
Carriage outwards	Turnover (4:3:2)
Salaries	No. of Employees (5:4:3)
Advertisement	Turnover (4:3:2)
Discount allowed	Turnover (4:3:2)
Discount received	Purchases (3:2:1)
Rent, Rates and Taxes	Floor Space occupied (6:5:4)
Depreciation on furniture	Value of furniture (2:2:1)
Labour welfare expenses	No. of Employees (5:4:3)
Electricity expense	Units consumed (3:2:1)
Provision for bad debts	Debtors balances (3:2:2)

Illustration 5

M/s X has two departments, A and B. From the following particulars prepare the consolidated Trading Account and Departmental Trading Account for the year ending 31st December, 20X1 :

	A	B
	`	`
Opening Stock [consisting of purchased goods -at cost)]	20,000	12,000
Purchases	92,000	68,000
Sales	1,40,000	1,12,000
Wages	12,000	8,000
Carriage	2,000	2,000
Closing Stock:		
(i) Purchased goods	4,500	6,000
(ii) Finished goods	24,000	14,000
Purchased goods transferred:		
by B to A	10,000	
by A to B		8,000
Finished goods transferred:		
by A to B	35,000	
by B to A		40,000
Return of finished goods:		
by A to B	10,000	
by B to A		7,000

You are informed that purchased goods have been transferred mutually at their respective departmental purchase cost and finished goods at departmental market price and that 20% of the finished stock (closing) at each department represented finished goods received from the other department.

Solution

M/s X
Departmental Trading A/c for the year ending 31st December, 20X1

	Deptt.A. `	Deptt.B. `		Deptt.A. `	Deptt.B. `
To Stock	20,000	12,000	By Sales	1,40,000	1,12,000
To Purchases	92,000	68,000	By Purchased Goods transferred	8,000	10,000
To Wages	12,000	8,000	By Finished Goods transferred	35,000	40,000
To Carriage	2,000	2,000	By Return of finished Goods	10,000	7,000
To Purchased Goods transferred	10,000	8,000	By Closing Stock: Purchased Goods	4,500	6,000
To F.G. transferred	40,000	35,000	Finished Goods	24,000	14,000
To Return of finished Goods	7,000	10,000			
To Gross profit c/d (b.f.)	38,500	46,000			
	2,21,500	1,89,000		2,21,500	1,89,000

Consolidated Trading Account for the year ending 31st December, 20X1

Particular	`	Particulars	`
To Opening Stock	32,000	By Sales	2,52,000
To Purchases	1,60,000	By Closing Stock:	
To Wages	20,000	Purchased Goods	10,500
To Carriage	4,000	Finished Goods	38,000
To Stock Reserve	2,196		
To Gross Profit c/d	82,304		
	3,00,500		3,00,500

Working note:

	Deptt. A	Deptt. B
Sale	1,40,000	1,12,000
Add : Transfer	35,000	40,000
	1,75,000	1,52,000
Less: Returns	(7,000)	(10,000)
Net Sales plus Transfer	1,68,000	1,42,000
Rate of Gross profit	$\frac{38,500}{1,68,000} \times 100 = 22.916\%$	$\frac{46,000}{1,42,000} \times 100 = 32.394\%$
Closing Stock out of transfer (20% of closing stock)	4,800	2,800
Unrealised Profit	` 4,800 × 32.394% = 1,555	2,800 × 22.916% = ` 641

Illustration 6

Department P sells goods to Department S at a profit of 25% on cost and to Department Q at a profit of 15% on cost. Department S sells goods to P and Q at a profit of 20% and 30% on sales respectively. Department Q sells goods to P and S at 20% and 10% profit on cost respectively.

Departmental Managers are entitled to 10% commission on net profit subject to unrealised profit on departmental sales being eliminated. Departmental profits after charging Manager's commission, but before adjustment of unrealised profits are as below:

	`
Department P	*90,000*
Department S	*60,000*
Department Q	*45,000*

Stock lying at different Departments at the end of the year are as below:

	Figure in `		
	DEPARTMENTS		
	P	S	Q
Transfer from P	-	18,000	14,000
Transfer from S	48,000	-	38,000
Transfer from Q	12,000	8,000	-

Find out correct Departmental Profits after charging Managers' Commission.

Solution

Calculation of correct Departmental Profits

	Department P (`)	Department S (`)	Department Q (`)
Profit after charging Manager's Commission	90,000	60,000	45,000
Add: Manager's Commission (1/9)	10,000	6,667	5,000
	1,00,000	66,667	50,000
Less: Unrealised profit on Stock (WN)	(5,426)	(21,000)	(2,727)
Profit Before Manager's Commission	94,574	45,667	47,273
Less: Manager's Commission 10%	(9,457)	(4,567)	(4,727)
Correct Profit after Manager's Commission	85,117	41,100	42,546

Working Notes:

	Department P (`)	Department S (`)	Department Q (`)	Total (`)
Unrealised Profit of:				
Department P	-	25/125X18,000 =3,600	15/115X14,000 =1,826	5,426
Department S	20/100X48,000 =9,600	-	30/100X38,000 =11,400	21,000
Department Q	20/120X12,000 =2,000	10/110X8,000 =727		2,727

Illustration 7

M/s. Suman Enterprises has two Departments, Finished Leather and Shoes. Shoes are made by the Firm itself out of leather supplied by Leather Department at its usual selling price. From the following figures, prepare Departmental Trading and Profit & Loss Account for the year ended 31st March, 20X3:

	Finished Leather Department (`)	*Shoes Department (`)*
Opening Stock (As on 01.04.20X2)	*30,20,000*	*4,30,000*
Purchases	*1,50,00,000*	*2,60,000*
Sales	*1,80,00,000*	*45,20,000*
Transfer to Shoes Department	*30,00,000*	-

Manufacturing Expenses	*-*	*5,00,000*
Selling Expenses	*1,50,000*	*60,000*
Rent and Warehousing	*5,00,000*	*3,00,000*
Stock on 31.03.20X3	*12,20,000*	*5,00,000*

The following further information is available for necessary consideration:

(i) *The stock in Shoes Department may be considered as consisting of 75% of Leather and 25% of other expenses.*

(ii) *The Finished Leather Department earned a Gross Profit @ 15% in 20X1-X2.*

(iii) *General expenses of the business as a whole amount to ` 8,50,000.*

Answer

Departmental Trading and Profit and Loss Account for the year ended 31st March, 20X3

Particulars	Finished leather (`)	Shoes (`)	Total (`)	Particulars	Finished leather (`)	Shoes (`)	Total (`)
To Opening Stock	30,20,000	4,30,000	34,50,000	By Sales	1,80,00,000	45,20,000	2,25,20,000
To Purchases	1,50,00,000	2,60,000	1,52,60,000	By Transfer to shoes Deptt.	30,00,000	-	30,00,000
To Transfer from Leather Department		30,00,000	30,00,000	By Closing stock	12,20,000	5,00,000	17,20,000
To Manufacturing expenses		5,00,000	5,00,000				
To Gross profit c/d (b.f.)	42,00,000	8,30,000	50,30,000				
	2,22,20,000	50,20,000	2,72,40,000		2,22,20,000	50,20,000	2,72,40,000
To Selling expenses	1,50,000	60,000	2,10,000	By Gross Profit b/f	42,00,000	8,30,000	50,30,000
To Rent & warehousing	5,00,000	3,00,000	8,00,000				
To Net profit (b.f.)	35,50,000	4,70,000	40,20,000				
	42,00,000	8,30,000	50,30,000		42,00,000	8,30,000	50,30,000

General Profit and Loss Account

Particulars	Amount `	Particulars	Amount `
To General expenses	8,50,000	By Net Profit	40,20,000
To Unrealised profit (Refer W.N.)	26,625		
To General net profit (Bal. fig.)	31,43,375		
	40,20,000		40,20,000

Working Note:

Calculation of Stock Reserve

Rate of Gross Profit of Finished leather Department, for the year 20X2-X3

$= \frac{\text{Gross Profit}}{\text{Total Sales}} \times 100 = [(42,00,000)/ (1,80,00,000 + 30,00,000)] \times 100 = 20\%$

Closing Stock of Finished leather in Shoes Department = 75%

i.e. ` 5,00,000 x 75% = ` 3,75,000

Stock Reserve required for unrealised profit @ 20% on closing stock

` 3,75,000 x 20% = ` 75,000

Stock reserve for unrealised profit included in opening stock of Shoes dept. @ 15% i.e.

(` 4,30,000 x 75% x 15%) = ` 48,375

Additional Stock Reserve required during the year = ` 75,000 – ` 48,375 = ` 26,625

Illustration 8

Gram Udyog, a retail store, has two departments, 'Khadi and Silks' for each of which stock account and memorandum 'mark up' accounts are kept. All the goods supplied to each department are debited to the stock account at cost plus a 'mark up', which together make-up the selling-price of the goods and in the account of the sale proceeds of the goods are credited. The amount of 'mark-up' is credited to the Departmental Mark up Account. If the selling price of any goods is reduced below its normal selling price, the reduction 'marked down' is adjusted both in the Stock Account and the Departmental 'Mark up' Account. The rate of 'Mark up' for Khadi Department is 33-1/3% of the cost and for Silks Department it is 50% of the cost.

The following figures have been taken from the books for the year ended December 31,20X1 :

	Khadi Deptt.	Silks Deptt.
	₹	₹
Stock as on January 1st at cost	*10,500*	*18,600*
Purchases	*75,900*	*93,400*
Sales	*95,600*	*1,25,000*

(1) The stock of Khadi on January 1, 20X1 included goods the selling price of which had been marked down by ₹ 1,260. These goods were sold during the year at the reduced prices.

(2) Certain stock of the value of ₹ 6,900 purchased for the Khadi Department were later in the year transferred to the Silks department and sold for ₹ 10,350. As a result though cost of the goods is included in the Khadi Department the sale proceeds have been credited to the Silks Department.

(3) During the year 20X1 to promote sales the goods were marked down as follows:

	Cost	Marked down
	₹	₹
Khadi	*5,600*	*360*
Silk	*10,000*	*2,000*

All the goods marked down, were sold except Silks of the value of ₹ 5,000 marked down by ₹ 1,000.

(4) At the time of stock-taking on December 31, 20X1 it was discovered that Khadi cloth of the cost of ₹ 390 was missing and it was decided that the amount be written off.

You are required to prepare for both the departments for the year 20X1.

(a) The Memorandum Stock Account; and

(b) The Memorandum Mark up Account.

Solution

Silk Stock Account

20X1		₹	20X1	₹
To Balance b/d			By Sales A/c	1,25,000
To Cost	18,600		By Mark-up A/c	2,000
Mark-up @50%	9,300	27,900	By Balance c/d (bal. fig.)	51,350
To Purchases	93,400			
Mark-up @50%	46,700	1,40,100		

To Khadi A/c 6,900 Mark-up @50% 3,450	10,350		
	1,78,350		1,78,350

Silk Mark-up Account

20X1	`	20X1	`
To Stock A/c	2,000	By Balance b/d	9,300
To Profit & Loss A/c (bal. fig.)	41,000	By Stock A/c	46,700
To Balance c/d [(1/3* of {51,350 + 1,000}) – 1,000]	16,450	By Stock A/c	3,450
	59,450		59,450

* 1/2 on cost is equal to 1/3 on sales

Working Notes:

Verification of Profit

	`
Sales	1,25,000
Add : Mark down in goods sold	1,000
	1,26,000
Gross Profit 1/3	42,000
Less : Mark down	(1,000)
Gross profit as per books	41,000

Khadi Stock Account

20X1		`	20X1		`
	To Balance b/d (10,500+2,240#)	12,740		By Sales	95,600
	To Purchases 75,900 Markup 25,300 @33-1/3%	1,01,20 0		By Silk Deptt. 6,900 Mark-up A/c 2,300 @33-1/3%	9,200
				By Loss of stock A/c 390 Mark-up A/c 13 0 @33-1/3%	520
				By Mark-up A/c	360
				By Balance c/d (bal. fig.)	8,260
		1,13,94 0			1,13,940

[(10,500 x 33-1/3%) – 1,260] = ` 2,240

Khadi Mark-up Account

20X1		`	20X1		`
	To Stock A/c (transfer)	2,300		By Balance b/d	
	To Stock A/c (re-sale)	130		(3,500 – 1,260)	2,240
	To Stock A/c (mark down)	360		By Stock A/c	25,300
	To Profit & Loss A/c	22,685			
	To Balance (1/4 of ` 8,260)	2,065			
		27,540			27,540

Working Note:

Verification of Profit	`
Sales as per books	95,600
Add : Mark-down (1,260+360)	1,620
	97,220
Gross Profit on fixed selling price @ 25% on ` 97,220	24,305
Less : Mark down	(1,620)
	22,685

SUMMARY

- **Aspects of Departmental Accounting**
  - (i) Computation of unrealised profit if inter-department transfers form part of closing stock.
  - (ii) Preparation of departmental trading and profit and loss account.
  - (iii) Monitoring stock movements with help of memorandum mark-up account.
- **Methods of maintaining departmental accounts**

  There are two methods of keeping departmental accounts:
  - (i) When accounts of all departments are kept at in one book only
  - (ii) When separate set of books are kept for each department.
- **Classification of Departments :** (i) Dependent departments and (ii) Independent departments.

- **Basis of allocation of departmental expenses:**

S.No.	Expenses	Basis
1.	Rent, rates and taxes, repairs and maintenance, insurance of building	Floor area occupied by each department (if given) otherwise on time basis
2.	Lighting and Heating expenses	Consumption of energy by each department
3.	Selling expenses,	Sales of each department
4.	Carriage inward/ Discount received	Purchases of each department
5.	Wages/Salaries	Time devoted to each department
6.	Maintenance of capital assets	Value of assets of each department otherwise on time basis
7.	Administrative expenses	Time basis or equally among all departments
8.	Labour welfare expenses	Number of employees in each department
9.	PF/ESI contributions	Wages and salaries of each department

- There are certain expenses and income, most being of financial nature, which cannot be apportioned on a suitable basis; therefore they are recognised in the combined Profit and Loss Account, for example, interest on loan, profit/loss on sale of investment, etc.
- Goods and services may be charged by one department to another usually on any of the three basis: (i)Cost, (ii) Current market price,(iii) Cost plus percentage of profit.
- When profit is added in the inter-departmental transfers, the loading included in the unsold stock at the end of the year is to be excluded before final accounts are prepared so as to eliminate any anticipatory profit included therein. This is done by creating an appropriate stock reserve by debiting the combined Profit and Loss Account.

BRANCH ACCOUNTS:

What Is Branch Accounting?

Branch accounting is a bookkeeping system in which separate accounts are maintained for each branch or operating location of an organization. Typically found in geographically dispersed corporations, multinationals, and chain operators, it allows for greater transparency in the transactions, cash flows, and overall financial position and performance of each branch.

Branch accounts can also refer to records individually produced to show the performance of different locations, with the accounting records actually maintained at the corporate headquarters. However, branch accounting usually refers to branches keeping their own books and later sending them into the head office to be combined with those of other units.

Branch accounting is an accounting system in which separate accounts are maintained for each branch of a corporate entity or organization. The primary objectives of branch accounting are better accountability and control, since profitability and efficiency can be closely tracked at the branch level.

Branch accounting may involve added expenses for an organization in terms of accounting and infrastructure. This is because it may be necessary to appoint branch accountants to ensure accurate financial reporting and compliance with head office procedures and processes.

Objectives

To know the profit or loss of each branch.

To know the financial position of each branch.

To control the activities of the branch.

To find out the requirement of goods or cash for each branch.

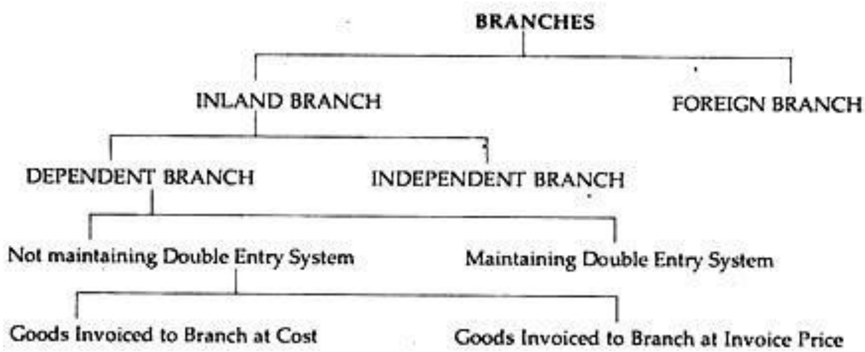
To provide concrete suggestions for the improvement in the working of different branches.

To compare the performance of one branch with that of another branch.

To meet the statutory requirements.

Types of Branches

There are different types of branches according to their nature and magnitude of operation, although all the branches are operated under the instruction of Head Office. As a result, the system of branch accounting is not the same in all the cases.



However, branches may be classified as:

Inland Branch (also known as Domestic Branch or Home Branch):

These branches are situated within the territory of the country. These branches do not maintain accounts under Double Entry System. They simply read out periodical statements to Head Office relating to goods received, goods sold, amounts returned, expenses, stock position (both at the beginning and at the end.)

These branches are not allowed to purchase goods from outside market. As all collections are directly remitted to Head Office, naturally, expenses of branches are met by Head Office. In other words, these branches are operated and controlled by Head Office.

Dependent Branch:

Dependent branches are those which do not maintain separate books of account and wholly depend on Head Office. The result of the operation, i.e., profit or loss, is ascertained by Head Office. In other words Head Office maintains and opens a Branch Account in its book in order to find out the result of the operation. Branches supply some related information to the Head Office, i.e., position of cash, debtors stocks, etc.

Independent Branch:

Independent branches are those which maintain complete system of accounting. This particularly happens when their sizes are very large due to various functional complexities. In short, they prepare their accounts independently, i.e., they also purchase and sell goods for cash and credit independently in addition to the goods that are supplied by the Head Office.

They may supply goods to Head Office, pay expenses and deposit cash in their own account like an independent unit. Thus, they maintain their own accounts under Double Account System. That is why they are called Independent Branch.

Foreign Branch:

These branches are located outside the country. They are operated in the foreign country which has a different currency and, as such, question of rate of exchange will arise. These branches may be of: (i) Dependent Branch or (ii) Independent Branch depending on the method of accounting.

KEY TAKE AWAYS:

Branch accounting is a bookkeeping system in which separate accounts are kept for each branch or operating location of an organization.

Technically, the branch account is a temporary or nominal ledger account, lasting for a designated accounting period.

Branch accounting provides better accountability and control since profitability and efficiency can be closely tracked for each location.

Branch accounting has a long history, going back to the Venetian banks of the 14th century.

Some typical features of a branch

- A branch is not a separate legal entity, it is a part of the foreign-based company.
- A foreign company may only have one branch in Sweden.
- The foreign-based company shall appoint a managing director to run the business activities in Sweden.
- The managing director represents the branch and is responsible for registering the branch with Bolagsverket.
- A branch is subject to Swedish law and the decisions of Swedish authorities regarding legal matters in connection with its business activities in Sweden.
- A branch has no independent capital and its assets and liabilities are a part of the total assets of the foreign-based company.
- A branch is to keep its own accounting records, and these are to be kept separate from the foreign-based company. Read more on the page Annual reports for branches.
- The accounts of a branch and the administration of the managing director are, when required, subject to examination by an authorized or approved public accountant.
- When a branch has been registered with Bolagsverket, it receives a Swedish registration number.

Branch Accounts: Problem and Solution # 1.

The Kanpur Shoe Company opened a branch at Delhi on 1st April 2010. From the following figures, prepare all the necessary accounts for the year ended 31st March, 2011 and Delhi Branch Account for the year ended 31st March 2012:

	2010-11	2010-2012
	₹	₹
Goods sent to Delhi Branch	2,15,000	6,45,000
Cash sent to Branch for :		
Rent	31,800	31,800
Salaries	33,000	45,000
Other expenses	11,200	21,600
Cash received from the Branch	3,24,000	8,60,000
Closing stock	32,300	65,800
Closing petty cash in hand	1,040	2,030

BOOKS OF KANPUR SHOE COMPANY

Solution:

Dr. **Delhi Branch Account** *Cr.*

Date	Particulars		₹	Date	Particulars	₹
Apr. 1 2010 to Mar. 31 2011	To Goods Sent to Branch A/c		2,15,000	Apr. 1, 2010 to Mar. 31 2011	By Cash	3,24,000
	To Cash—	₹		2011 Mar. 31	By Stock at Delhi Branch A/c	32,300
	Rent	31,800				
	Salaries	. 33,000				
	Other Expenses	11,200	76,000	Mar. 31	By Petty Cash at Delhi Branch A/c	1,040
2011 Mar. 31	To Net Profit transferred to Profit and Loss Account		66,340			
			3,57,340			3,57,340

Dr. **Goods Sent to Delhi Branch Account** *Cr.*

Date	Particulars	₹	Date	Particulars	₹
2011 Mar. 31	To Trading Account—transfer	2,15,000	Apr. 1, 2010 to Mar. 31 2010	By Delhi Branch A/c	2,15,000

Stock at Delhi Branch Account

Dr.			Cr.		
2011		₹	**2011**		₹
Mar. 31	To Delhi Branch Account	32,300	Mar. 31	By Balance *c/d*	32,300
2011			**2011**		
Apr. 1	To Balance *b/d*	32,300	Apr. 1	By Delhi Branch A/c—transfer	32,300

Petty Cash at Delhi Branch Account

Dr.			Cr.		
2011		₹	**2011**		₹
Mar. 31	To Delhi Branch A/c	1,040	Mar. 31	By Balance *c/d*	1,040
2011			**2011**		
Apr. 1	To Balance *b/d*	1,040	Apr. 1	By Delhi Branch A/c—transfer	1,040

Profit and Loss Account

Dr.			Cr.		
			2011		₹
			Mar. 31	By Delhi Branch A/c	66,340

Delhi Branch Account

Dr.				Cr.		
2011			₹	Apr. 1		₹
Apr. 1	To Stock at Delhi Branch A/c		32,300	2011 to		
" "	To Petty Cash at Delhi Branch A/c.		1,040	Mar. 31 2012	By Cash	8,60,000
Apr. 1, 2011 to Mar. 31, 2012	To Goods Sent to Branch A/c		6,45,000	2012 Mar. 31	By Stock at Delhi Branch A/c	65,800
" "	To Cash (expenses) :	₹		" "	By Petty Cash at Delhi Branch A/c	2,030
	Rent	31,800				
	Salaries	45,000				
	Other Expenses	21,600	98,400			
2012						
Mar. 31	To Net Profit transferred to Profit & Loss A/c		1,51,090			
			9,27,830			9,27,830

Branch Accounts: Problem and Solution # 2.

From following particulars relating to Patna Branch for the year ending 31st March, 2012, prepare accounts in the head office books:

	₹
Stock at Branch on 1st April, 2011	58,900
Branch Debtors on 1st April, 2011	14,700
Petty Cash at Branch on 1st April, 2011	720
Goods sent to Branch during the year	3,29,400
Cash sales during the year	3,15,800
Credits sales during the year	1,40,400
Cash received from debtors	1,37,900
Cash sent to Branch for expenses :	
Rent	12,000
Salaries	36,000
Petty cash	7,000
Stock at Branch on 31st March, 2012	55,400
Petty Cash at Branch on 31st March, 2012	730
Goods returned by Branch	1,800

Solution :

HEAD OFFICE LEDGER

Branch Stock Account

Dr. *Cr.*

Date		Particulars	₹	Date		Particulars	₹
2011				2011			
Apr.	1	To Balance *b/d*	58,900	Apr.	1	By Patna Branch Account—tranfer	58,900
2012				2012			
Mar.	31	To Patna Branch A/c	55,400	Mar.	31	By Balance *c/d*	55,400
2012							
Apr.	1	To Balance *b/d*	55,400				

Branch Debtors Accounts

Date		Particulars	₹	Date		Particulars	₹
2011				2011			
Apr.	1	To Balance *b/fd*	14,700	Apr.	1	By Patna Branch A/c—transfer	14,700
2012				2012			
Mar.	31	To Patna Branch A/c*	17,200	Mar.	31	By Balance *c/d*	17,200
2012							
Apr.	1	To Balance *b/d*	17,200				

Branch Petty Cash Account

		₹			₹
2011 Apr. 1	To Balance b/fd	720	2011 Apr. 1	By Patna Branch A/c—transfer	720
2012 Mar. 31	To Patna Branch A/c	730	2012 Mar. 31	By Balance c/d	730
2012 Apr. 1	To Balance b/d	730			

Memorandum Branch Debtors Account

Dr. Cr.

		₹			₹
	To Balance b/fd	14,700		By Cash	1,37,900
	To Credit Sales	1,40,400		By Balance c/fd	17,200
		1,55,100			1,55,100

Patna Branch Account

			₹				₹
2011 Apr. 1	To Branch Stock A/c		58,900	Apr. 1 2011 to Mar 31, 2012	By Cash :	₹	
" "	To Branch Debtors A/c		14,700		Cash Sales	3,15,800	
" "	To Branch Petty Cash A/c		720		Receipts from Debtors	1,37,900	4,53,700
Apr. 1, 11 to Mar. 31 2012	To Goods Sent to Branch A/c		3,29,400	" "	By Goods Sent to Branch A/c (returns)		1,800
" "	To Cash :	₹					
	Rent	12,000					
	Salaries	36,000					
	Petty Cash	7,000	55,000	2012 Mar. 31	By Branch Stock A/c		55,400
2012 Mar. 31	To Profit and Loss A/c—transfer of profit		70,110	" "	By Branch Debtors A/c		17,200
				" "	By Branch Petty Cash A/c		730
			5,28,830				5,28,830

Goods Sent to Branch Account

		₹			₹
Apr. 1, 2011 to Mar. 31, 2012	To Patna Branch A/c (returns)	1,800	April 1 2011 to Mar. 31, 2012	By Patna Branch A/c	3,29,400
2012 Mar. 31	To Trading A/c—transfer	3,27,600			
		3,29,400			3,29,400

The profit disclosed by the Patna Branch Account can be verified by preparing trading and profit and loss account as follows:

Tranding and Profit and Loss Account

		₹			₹
To Opening Stock		58,900	By Sales—	₹	
To Goods Received from Head Office	₹ 3,29,400		Cash	3,15,800	
Less: Returns	1,800	3,27,600	Credit	1,40,400	4,56,200

	₹			₹
To Gross Profit c/d	1,25,100	By Closing Stock		55,400
	5,11,600			5,11,600
To Rent	12,000	By Gross Profit b/d	1,25,100	
To Salaries	36,000			
To Petty Cash Expenses*	6,990			
To Net Profit	70,110			
	1,25,100			1,25,100

Branch Accounts: Problem and Solution # 3.

Amrit Oils Ltd. open a branch at Delhi on 1st April, 2010. Goods are invoiced to the branch at cost plus 33⅓% which is the selling price. From the following particulars relating to 2010-11 and 2011-2012 ascertain the profit made at Delhi Branch in the two years. For 2010-11 give journal entries and show how the relevant items will appear in the company's Balance Sheet as on 31st March, 2011.

	2010-11	2011-2012
	₹	₹
Goods sent to Delhi Branch during the year, at selling price	6,45,000	8,70,000
Sales at Branch — Cash	3,15,000	6,00,400
— Credit	2,19,600	2,41,000
Cash received from debtors	1,75,400	2,32,300
Discounts allowed to customers	3,200	4,500
Cash sent to branch for expenses (including perty cash)	96,000	1,10,000
Goods returned by the Branch (invoice price)	1,500	10,100
Stock at 31st March at invoice price	1,08,400	1,26,900
Petty cash at Branch on 31st March	690	970

Solution :

AMRIT OILS LTD.

Journal

Date	Particulars			Dr.	Cr.
2010-11				₹	₹
?	Delhi Branch Account	...	Dr.	6,45,000	
	To Goods Sent to Delhi Branch Account				6,45,000
	The value of goods sent to Branch at invoice value.				
?	Bank	...	Dr.	4,90,400	
	To Delhi Branch Account				4,90,400
	Cash received from branch against cash and credit sales made there.				
?	Delhi Branch Account	...	Dr.	96,000	
	To Bank				96,000
	The amount remitted to Delhi Branch for expenses.				
?	Goods Sent to Delhi Branch Account	...	Dr.	1,500	
	To Delhi Branch Account				1,500
	Goods returned by the branch at invoice value.				
2011 Mar. 31	Delhi Branch Stock Account	...	Dr.	1,08,400	
	Delhi Branch Debtors Account*	...	Dr.	41,000*	
	Delhi Branch Perty Cash Account	...	Dr.	690	
	To Delhi Branch Account				1,50,090
	The various assets at the branch (stock at invoice value) on 31st March, 2011.				
" "	Goods Sent to Delhi Branch Account	...	Dr.	1,60,875	
	To Delhi Branch Account				1,60,875
	The excess of invoice value over cost of the goods sent to Delhi Branch *less* returns—1/4 of ₹ 6,43,500.				
" "	Delhi Branch Account	...	Dr.	27,100	
	To Delhi Branch Stock Reserve Account				27,100
	The excess of invoice value of stock over cost—1/4 of ₹ 1,08,400				

*The amount is ascertained by making a memorandum branch debtors account.

Date	Particulars			Dr. ₹	Cr. ₹
2011 Mar. 31	Goods Sent to Delhi Branch Account	...	Dr.	4,82,625	
	To Trading Account				4,82,625
	The balance in the Goods Sent to Delhi Branch Account transferred to Trading Account.				
" "	Delhi Branch Account	...	Dr.	34,765	
	To Profit and Loss Account				34,765
	The transfer of profit at Delhi Branch to the Profit & Loss Account.				

Dr. **Delhi Branch Account** **Cr.**

Date	Particulars	₹	Date	Particulars	₹
Apr. 1, 2010 to Mar. 31, 2011	To Goods Sent to Delhi Branch A/c	6,45,000	Apr. 1, 2010 to Mar. 31 2011	By Cash— Cash Sales ₹ 3,15,000 From Debtors 1,75,400	4,90,400
	To Cash (for expenses)	96,000		By Goods Sent to Delhi Branch A/c—returns	1,500
2011 Mar. 31	To Delhi Branch Stock Reserve A/c	27,100*	2011 Mar. 31	By Goods Sent to Delhi Branch Stock A/c—loading*	1,60,875
" "	To Profit and Loss A/c—transfer of profit	34,765	" "	By Delhi Branch Stock A/c—	1,08,400
			" "	By Delhi Branch Debtors A/c	41,000
			" "	By Delhi Branch Petty Cash A/c	690
		8,02,865			8,02,865

*The goods are invoiced at cost plus $33^1/_3$%. If cost is 100, profit, is $33^1/_3$%; the selling price therefore, is $133^1/_3$. Hence, the ratio of profit to selling price is $33^1/_3/ 133^1/_3$ or ¼. The adjustment is made on the basis of $^1/_4$ of invoice price.

The other relevent ledger accounts will be as under :

Dr. **Goods Sent to Delhi Branch Account** **Cr.**

Date	Particulars	₹	Date	Particulars	₹
Apr. 1, 2010 to Mar. 31, 2011	To Delhi Branch Account (returns)	1,500	Apr. 1, 2010 to Mar. 31, 2011	By Delhi Branch A/c	6,45,000
2011 Mar. 31	To Delhi Branch A/c (loading)	1,60,875			
" "	To Trading A/c (transfer of cost)	4,82,625			
		6,45,000			6,45,000

Delhi Branch Stock Account

Dr.			₹	Cr.			₹
2011 Mar.	31	To Delhi Branch A/c	1,08,400	2011 Mar. 31		By Balance *c/d*	1,08,400
2011 Apr.	1	To Balance *b/d*	1,08,400	2011 Apr.	1	By Delhi Branch A/c —transfer	1,08,400

Delhi Branch Debtors Account

Dr.			₹	Cr.			₹
2011 Mar.	31	To Delhi Branch A/c	41,000	2011 Mar. 31		By Balance *c/d*	41,000
2011 Apr.	1	To Balance *b/d*	41,000	2011 Apr.	1	By Delhi Branch A/c —transfer	41,000

Delhi Branch Debtors Account

Dr.			₹	Cr.			₹
2011 Mar.	31	To Delhi Branch A/c	690	2011 Mar. 31		By Alance *c/d*	690
2011 Apr.	1	To Balance *b/d*	690	2011 Apr.	1	By Delhi Branch A/c — transfer	690

Delhi Branch Stock Reserve Account

Dr.			₹	Cr.			₹
2011 Mar.	31	To Balance *c/d*	27,000	2011 Mar. 31		By Delhi Branch A/c	27,100
2011 Apr.	1	To Delhi Branch A/c— transfer	27,100	2011 Apr.	1	By Balance *b/d*	27,100

Balance Sheet of Amrit Oils Ltd. as at 31st March, 2011
(Assets Side)

	₹	₹
Delhi Branch Stock	1,08,400	
Less : Delhi Branch Stock Reserve	27,100	81,300
Delhi Branch Debtors		41,000
Delhi Branch Petty Cash		690

Delhi Branch Account

Dr.			₹	Cr.			₹
2011 Apr.	1	To Delhi Branch Stock A/c	1,08,400	2011 Apr.	1	By Delhi Branch Stock Reserve A/c	27,100
Apr.	1	To Delhi Branch Debtors A/c	41,000	Apr.	1		
Apr.	1	To Delhi Branch Petty Cash A/c	690	2011 to Mar. 31 2012		By Cash— Cash Sales ₹ 6,00,400 From Debtors 2,32,300	8,32,700
April 2011 to Mar. 2012	1 / 31	To Goods Sent to Delhi Branch A/c	8,70,000				
		To Cash— for expenses	1,10,000	2012 Mar.	31	By Goods Sent to Delhi Branch A/c (returns)	10,100
Mar. 2012	31	To Delhi Branch Stock Reserve A/c (required on closing stock)	31,725	"	"	By Goods Sent to Delhi Branch A/c (adjustment)	2,14,975
"	"	To Profit and Loss A/c —transfer of profit	96,130	"	"	By Delhi Branch Stock A/c	1,26,900
						By Delhi Branch Debtors A/c	45,200
				"	"	By Delhi Branch Petty Cash A/c	970
			12,57,945				12,57,945

If the Memorandum Stock Account were to be prepared, it would appear as under :

Dr. **Memorandum Delhi Branch Stock Account** **Cr.**

Date	Particulars	₹	Date	Particulars	₹	₹
Apr. 1 2010 to Mar. 31, 2011	To Goods Sent to Delhi Branch	6,45,000	Apr. 1, 2010 to Mar. 31 2011	By Sales—		
				Cash	3,15,000	
				Credit	2,19,600	5,34,600
			" "	By Goods Returned		1,500
			2011 Mar. 31	By Wastage (balancing figure)		500
			" "	By Balance c/d		1,08,400
		6,45,000				6,45,000
2011 Apr. 1	To Balance b/d	1,08,400	Apr. 1 2011 to Mar. 31 2012	By Sales—		
				Cash	6,00,400	
Apr. 1, 2011 to Mar. 31, 2012	To Goods Sent to Delhi Branch	8,70,000		Credit	2,41,000	8,41,400
			" "	By Goods Returned		10,100
			2012 Mar. 31	By Balance b/d		1,26,900
		9,78,400				9,78,400
2012 Apr. 1	To Balance b/d	1,26,900				

The student can see for himself that if the closing stock is not given, it can be found out by preparing a memorandum stock account. Suppose, the following information is given :

	₹
Stock on 1st April, 2011	68,900
Goods sent to Branch during the year	4,34,500
Goods returned by the Branch during the year	2,400
Sales during the year :	2,20,500
Cash	2,01,600
Credit	2,01,600
Goods returned by the customers during the year	11,400
Leakage and spoilage during the year	700

The memorandum stock accout will appear as follows :—

Dr. **Memorandum Branch Stock Account** **Cr.**

Date	Particulars	₹	Date	Particulars	₹	₹
2011 Apr. 1	To Balance b/fd	68,900	Apr. 1, 2011 to Mar. 31 2012	By Sales—		
				Cash	2,20,500	
Apr. 1, 2011 to Mar. 31 2012	To Goods Sent to Branch	4,34,500		Credit	2,01,600	4,22,100
			" "	By Goods Sent to Branch— Returns		2,400
" "	To Returns from customers	11,400	2012 Mar. 31	By Leakage & Spoilage		700
			" "	By Balance c/d (balancing figure)		89,600
		5,14,800				5,14,800
2012 Apr. 1	To Balance b/d	89,600				

Branch Accounts: Problem and Solution # 4.

Vijay Merchant of Mumbai has a branch at Poona. Goods are invoiced to the branch at cost plus 25%. Branch is instructed to deposit cash every day in the head office account with the bank. All expenses are paid through cheques by the head office except petty cash expenses which are paid by the branch manager.

Prepare Branch Account in the books of head office after taking into account the following information also:

	₹
Stock at invoice price on 1st April, 2011	82,000
Stock at invoice price on 31st March, 2012	96,000
Debtors on 1st April, 2011	31,700
Debtors on 31st March, 2012	42,150
Furniture on 1st April, 2011	23,400
Cash sales	4,01,300
Credit sales	3,72,100
Goods invoiced to branch by head office	6,28,000
Furniture purchased on 1st October, 2011 by branch manager, payment having been made out of cash sales and collections from debtors	2.500
Expenses paid by head office	1,32,000
Petty expenses paid by branch	10,450

Depreciation is provided on branch furniture @ 10% per annum on diminishing balance method.

Solution :

In the books of Head Office

Branch Account

Dr. *Cr.*

	₹		₹
To Branch Stock (opening)	82,000	By Branch Stock Reserve (opening)	16,400
To Branch Debtors (opening)	31,700	By Bank (cash deposited by branch)	7,50,000
To Branch Furniture (opening)	23,400	By Goods sent to Branch Account (loading)	1,25,600
To Goods Sent to Branch Account	6,28,000	By Branch Stock (closing)	96,000
To Bank (Branch expenses paid by this office)	1,32,000	By Branch Debtors (closing)	42,150
To Branch Stock Reserve (closing)	19,200	By Branch Furniture (written down value of furniture at branch)	23,435
To Profit and Loss Account (profit at branch)	1,37,285		
	10,53,585		10,53,585

Working Notes :

(*i*) *Depreciation on furniture for the year :*

	₹
On ₹ 23,400 @ 10% p.a. for full year	2,340
On ₹ 2,500 @ 10% p.a. for 6 months	125
Total	2,465

(*ii*) *Written down value of furniture on 31st March, 2012 :*

	₹
Written down value on 1st April, 2009	23,400
Add : Addition made during the year	2,500
	25,900
Less : Depreciation for the year	2,465
	23,435

(*iii*) *Collection from branch debtors:*

Memorandum Branch Debtors Account

Dr.	₹		*Cr.* ₹
To Balance b/fd	31,700	By Bank —collections (balancing figure)	3,61,650
To Credit Sales	3,72.100	By Balance c/fd	42,150
	4,03,800		4,03,800

(*iv*) *Cash deposited by branch with bank*

	₹	₹
Cash sales		4,01,300
Add : Cash collected from debtors		3,61,650
		7,62,950
Less : Furniture purchased	2,500	
Petty expenses	10,450	12,950
		7,50,000

Branch Accounts: Problem and Solution # 5.

Kanpur Cloth Mills opened a branch at Delhi on 1st April, 2011. The invoiced to the branch at selling price which was 125% of the cost to the head office.

The following are the particulars of the transactions relating to branch during the year March, 2012:

		₹
Goods sent to branch, at cost to head office		28,08,400
Sales :	₹	
Cash	12,50,700	
Credit	17,74,300	30,25,000
Cash collected from debtors		15,70,000
Discount allowed to debtors		15,700
Returns from debtors		10,000
Spoiled cloth in bales written off, at invoice price		5,000
Cheques sent to branch for	₹	
Rent	72,000	
Salaries	1,80,000	
Other Expenses	35,000	2,87,000

Prepare Branch Account ascertaining profit for the year ended 31st March, 2012 after preparing Memorandum Branch Stock Account and Memorandum Branch Debtors Account.

Solution :

Memorandum Branch Stock Account

Dr.		₹		Cr. ₹
To Goods sent to Branch :	₹		By Cash Sales	12,50,000
			By Credit Sales	17,74,300
Cost	28,08,400		By Abnormal Loss	
Add : Loading @ 25%	7,02,100	35,10,500	— Spoiled cloth	5,000
To Returns from Debtors		10,000	By Stock on 31st March, 2,012	
			— Balancing figure	4,90,500
		35,20,500		35,20,500

Memorandum Branch Debtors Account

Dr.	₹		Cr. ₹
To Credit Sales	17,74,300	By Cash collected	15,70,000
		By Discount allowed	15,700
		By Returns	10,000
		By Debtors on 31st March, 2012	
		— Balancing figure	1,78,600
	17,74,300		17,74,300

Branch Account

Dr.	₹	₹		₹	Cr. ₹
To Goods Sent to			By Bank		
Branch Account		35,10,500	— Cash sales	12,50,700	
To Bank			— From debtors	15,70,000	28,20,700
— Rent	72,000		By Goods Sent to		
— Salaries	1,80,000		Branch Account		
— Other expenses	35,000	2,87,000	— Loading		7,02,100
To Branch Stock Reserve		98,100	By Abnormal Loss		
To Profit and Loss Account			— Cost of spoiled cloth		4,000
— Transfer of profit		3,00,300	By Branch Stock		4,90,500
			By Branch Debtors		1,78,600
		41,95,900			41,95,900

Branch Accounts: Problem and Solution # 6.

Calico Printers Ltd. opened a shop at Delhi on 1st April, 2010. Goods were invoiced at selling price which was fixed by adding 25% to the cost. From the following particulars relating to 2010-11 and 2011-2012, ascertain the profit or loss made in two years by the stock and debtors system:

	2010-11	2011-2012
	₹	₹
Goods sent to Branch (invoice value)	11,40,400	15,65,200
Sales— Cash	7,50,000	10,80,000
— Credit	2,70,000	4,60,000
Cash received from debtors	2,22,400	4,21,400
Distcounts allowed to customers	6,600	7,800
Goods returned by customers	7,000	9,500
Cash remitted to Branch for :		
Rent	12,000	12,000
Salaries	60,000	66,000
Sundry expenses	7,800	9,300
Defective cloth found in bales written off	5,200	5,000
Stock at Branch on 31st March	1,22,200	1,51,900

Solution :

Dr. **Branch Stock Account** *Cr.*

		₹			₹
Apr. 1, 2010 to Mar. 31 2011	To Goods Sent to Branch A/c (1)	11,40,400	Apr. 1, 2010 to Mar., 31 2011	By Cash—cash sales (2)	7,50,000
	To Branch Debtors A/c —returns (5)	7,000		By Branch Debtors A/c —credit sales (3)	2,70,000
				By Branch Adjustment A/c—spoilage (9)	5,200
			2011 Mar. 31	31 By Balance *c/d*	1,22,200
		11,47,400			11,47,400
2011 Apr. 1	To Balance *b/d*	1,22,200			

Dr. **Goods Sent to Branch Account** *Cr.*

		₹			₹
2011 Mar. 31	To Branch Adjustment A/c (8)	2,28,080	Apr. 1, 2010 to Mar. 31 2011	By Branch Stock A/c (1)	11,40,400
" "	To Trading A/c —transfer (12)	9,12,320			
		11,40,400			11,40,400

Dr. **Branch Debtors Account** *Cr.*

		₹			₹
Apr. 1, 2010 to Mar. 31 2011	To Branch Stock A/c —credit sales (3)	2,70,000	Apr. 1, 2010 to Mar. 31 2011	By Cash (4)	2,22,400
				By Branch Stock A/c —returns (5)	7,000
				By Branch Expenses A/c —discount (7)	6,600

		₹			₹
			2011 Mar. 31	By Balance c/d	34,000
		2,70,000			2,70,000
2011 Apr. 1	To Balance b/d	34,000			

Dr. Branch Expenses Account Cr.

			₹			₹
Apr. 1, 2010 to Mar. 31, 2011	To Cash : (6)	₹		2011 Mar. 31	By Branch Adjustment A/c	86,400
	Rent	12,000				
	Salaries	60,000				
	Sundry Expenses	7,800	79,800			
	To Branch Debtors A/c—discount	(7)	6,600			
			86,400			86,400

Dr. Branch Stock Reserve Account Cr.

		₹			₹
2011 Mar. 31	To Balance c/d	24,440	2011 Mar. 31	By Branch Adjustment A/c: (20% of ₹ 1,22,200) (10)	24,440
			2011 Apr. 1	By Balance b/d	24,400

Dr. Branch Adjustment Account Cr.

		₹			₹
2011 Mar. 31	To Branch Stock A/c (9)	5,200	2011 Mar. 31	By Goods Sent to Branch	2,28,080
	To Branch Stock Rserve A/c (10)	24,440			
	To Branch Expenses A/c (11)	86,400			
	To (General) Profit and Loss A/c—transfer of profit (13)	1,12,040			
		2,28,080			2,28,080

Note : Figures is brackets show the steps and the entries to be completed. Cash Book, Trading Account and (General) Profit and Loss Account have not been shown.

Dr. Branch Stock Account Cr.

		₹			₹
2011 Apr. 1	To Balance b/fd	1,22,200	Apr. 1, 2011 to Mar. 31, 2012	By Cash—Cash sales	10,80,000
Apr. 1, 2011 to Mar. 31, 2012	To Goods Sent to Branch A/c	15,65,200		By Branch Debtors A/c—credit sales	4,60,000
	To Branch Debtors A/c—returns	9,500		By Branch Adjustment A/c—spoilage	5,000
			2012 Mar. 31	By Balance c/d	1,51,900
		16,96,900			16,96,900
2012 Apr. 1	To Balance b/d	1,51,900			

Dr. **Goods Sent to Branch Account** Cr.

		₹			₹
2012 Mar. 31	To Branch Adjustment A/c	3,13,040	Apr. 1, 2011 to Mar. 31 2012	By Branch Stock A/c	15,65,200
	To Trading A/c —transfer	12,52,160			
		15,65,200			15,65,200

Dr. **Branch Debtors Account** Cr.

		₹			₹
2011 Apr. 1	To Balance b/fd	34,000	Apr. 1, 2011 to Mar. 31, 2012	By Cash	4,21,400
Apr. 1 2011 to Mar. 31 2012	To Branch Stock A/c —credit sales	4,60,000		By Branch Stock A/c —returns	9,500
				By Branch Expenses A/c —discount	7,800
			2012 Mar. 31	By Balance c/d	55,300
		4,94,000			4,94,000
2012 Apr. 1	To Balance b/d	55,300			

Dr. **Branch Expenses Account** Cr.

		₹	₹			₹
Apr. 1, 2011 to Mar. 31, 2012	To Cash—			2012 Mar. 31	By Branch Adjustment A/c—transfer	95,100
	Rent	12,000				
	Salaries	66,000				
	Sundry Expenses	9,300	87,300			
	To Branch Debtors A/c —discount		7,800			
			95,100			95,100

Dr. **Branch Stock Reserve Account** Cr.

		₹			₹
2011 Apr. 1	To Branch Adjustment A/c —transfer	24,440	2011 Apr. 1	By Balance b/fd	24,440
2012 Mar. 31	To Balance c/d	30,380	2012 Mar. 31	By Branch Adjustment A/c (20% of ₹ 1,51,900)	30,380
			2012 Apr. 1	By Balance b/d	30,380

Dr. **Branch Adjustment Account** Cr.

		₹			₹
2012 Mar. 31	To Branch Stock A/c —Spoilage	5,000	2011 Apr. 1	By Branch Stock Reserve A/c (opening)	24,440
Mar. 31	To Branch Expenses A/c	95,100	2012 Mar. 31	By Goods Sent to	

		₹		₹
2012				
Mar. 31	To Branch Stock Reserve A/c (closing)	30,380	Branch A/c	3,13,040
Mar. 31	To (General) Profit and Loss A/c —transfer of profit	2,07,000		
		3,37,480		3,37,480

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