Elements of Financial Accounting (Paper - I)

[As per Revised Syllabus of 2016-17 for FY BAF
First Semester, University of Mumbai]

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PREFACE

It is a matter of great pleasure to present this new edition of the book on **Financial Accounting Paper - I** to the Students and Teachers of Bachelor of Commerce (Accounting and Finance) started by university of Mumbai. This book is written on lines of syllabus instituted by the university. The book presents the subject matter in a simple and convincing language.

We owe a great many thanks to a great many people who helped and supported me during the writing of this book which includes Principal, Co-coordinator and Students of BAF Section.

The syllabus contains a list of the topics covered in each chapter which will avoid the controversies regarding the exact scope of the syllabus. The text follows the term wise, chapter-topic pattern as prescribed in the syllabus. We have preferred to give the text of the section and rules as it is and thereafter added the comments with the intention of explaining the subject to the students in a simplified language. While making an attempt to explain in a simplified language, any mistake of interpretation might have crept in.

This book is an unique presentation of subject matter in an orderly manner. This is a student-friendly book and tutor at home. I hope the teaching faculty and the student community will find this book of great use.

We are extremely grateful to Mr. Pandey of Himalaya Publishing House Pvt. Ltd., for their devoted and untiring personal attention accorded by them to this publication.

We gratefully acknowledge and express my sincere thanks to the following people without whose inspiration, support, constructive suggestions, this book would not have been possible.

Mr. Jitendra Singh Thakur *(Trustee, Thakur College)*

Dr. Chaitaly Chakraborty *(Principal, Thakur College)*

Mrs. Janki Nishikhant Jha

We welcome suggestions from students and teachers for further improvement of quality of the book.

Authors

SYLLABUS

Revised Syllabus and Question Paper Pattern of Courses of B.Com. (Accounting and Finance) Programme at Semester I with Effect from the Academic Year 2016-2017

FY BAF FA -I text book

Financial Accounting - Elements of Financial Accounting - Paper I

Sr. No.	Modules/Units
1	**Accounting Standards Issued by ICAI and Inventory Valuation**
1.1	**Accounting Standards:** Concepts, Benefits, Procedures for Issue of Accounting Standards Various AS: **AS – 1: Disclosure of Accounting Policies** (a) Purpose (b) Areas of Policies (c) Disclosure of Policies (d) Disclosure of Change in Policies (e) Illustrations **AS – 2: Valuation of Inventories (Stock)** (a) Meaning, Definition (b) Applicability (c) Measurement of Inventory (d) Disclosure in Final Account (e) Explanation with Illustrations **AS – 9: Revenue Recognition** (a) Meaning and Scope (b) Transactions Excluded (c) Sale of Goods (d) Rendering of Services (e) Effects of Uncertainties (f) Disclosure (g) Illustrations
1.2	**Inventory Valuation:** Meaning of Inventories Cost for Inventory Valuation Inventory Systems: Periodic Inventory System and Perpetual Inventory SystemValuation: Meaning and Importance Methods of Stock Valuation as per AS-2: FIFO and Weighted Average Method Computation of Valuation of Inventory as on Balance Sheet Date:If Inventory is taken on a Date After the Balance Sheet or Before the Balance Sheet
2	**Final Accounts**
2.1	**Expenditure** (a) Capital (b) Revenue **Receipts** (a) Capital (b) Revenue
2.2	Adjustments and Closing Entries
2.3	Final Accounts of Manufacturing Concerns (Proprietary Firm)
3	**Departmental Accounts**
	Meaning Basis of Allocation of Expenses and Incomes / Receipts Inter Departmental Transfer: At Cost Price and Invoice Price Stock Reserve, Departmental Trading adn Profit and Loss Account and Balance Sheet
4	**Accounting for Hire Purchase**
	Meaning, Calculation of Interest, Accounting for Hire Purchase Transactions by Asset Purchase Method Based on Full Cash Price Journal Entries, Ledger Accounts and Disclosure in Balance Sheet for Hirer and Vendor (Excluding Default, Repossession and Calculation of Cash Price)

SCHEME OF EXAMINATION

Question Paper Pattern

Duration: 21/2 Hrs. Maximum Marks: 75

All Question are Compulsory Carrying 15 marks each. Questions to be Set: 05

	Particulars	Marks
Q.1	Objective Questions	15 Marks
	(A) Sub Questions to be asked 10 and to be answered any 08	
	(B) Sub Questions to be asked 10 and to be answered any 07	
	(*Multiple choice/True or False/Match the column/Fill in the blanks)	
Q.2	Full Length Question	15 Marks
	OR	
Q.2	Full Length Question	15 Marks
Q.3	Full Length Question	15 Marks
	OR	
Q.3	Full Length Question	15 Marks
Q.4	Full Length Question	15 Marks
	OR	
Q.4	Full Length Question	15 Marks
Q.5	(a)Theory Questions	08 Marks
	(b)Theory Questions	07 Marks
	OR	
Q.5	Short Notes	15 Marks
	To be asked 05	
	To be answered 03	

Note: Full length question of 15 marks may be divided into two sub questions of 7/8 and 10/5 Marks.

CONTENTS

Chapter 1

Accounting Standards Issued by ICAI and Inventory Valuation

ACCOUNTING STANDARDS

Accounting is the art of recording transactions in the best possible manner, so as to enable the reader to arrive at judgments/come to conclusions, and in this regard it is utmost necessary that there are set guidelines. These guidelines are generally called accounting policies. The intricacies of accounting policies permitted companies to alter their accounting principles for their benefit. This made it impossible to make comparisons. In order to avoid the above and to have a harmonised accounting principle, standards needed to be set by recognised accounting bodies. This paved the way for Accounting Standards to come into existence.

Accounting Standards in India are issued by the Institute of Chartered Accountants of India (ICAI). At present there are 30 Accounting Standards issued by ICAI.

OBJECTIVE OF ACCOUNTING STANDARDS

Objective of Accounting Standards is to standarize the diverse accounting policies and practices with a view to eliminate to the extent possible the non-comparability of financial statements and the reliability of the financial statements.

The Institute of Chatered Accountants of India, recognizing the need to harmonize the diverse accounting policies and practices, constituted an Accounting Standard Board (ASB) on 21st April, 1977.

COMPLIANCE WITH ACCOUNTING STANDARDS ISSUED BY ICAI

Subsection(3A) to section 211 of the Companies Act, 1956 requires that every Profit/Loss Account and Balance Sheet shall comply with the Accounting Standards. 'Accounting Standards' means the standard of accounting recomended by the ICAI and prescribed by the Central Government in consultation with the National Advisory Committee on Accounting Standards (NACAs) constituted under section 210(1) of the Companies Act, 1956.

Accounting Standards Apply only to material items.

The Accounting Standard Board (ASB) of the Institute of Chartered Accountants of India has issued the following Accounting Standards that are to be followed but its members.

Accounting Standards are collection of generally followed accounting principles, policies and practices. These help to ensure a common basis for financial statements different originations. This means that people can understand these more easily and make useful comparisons

Financial Statements are at the centre of business reporting. Financial statements usually provide users with essential information that heavily influence their decisions. The US is the leader in financial reporting, and US Securities and Exchange Commission is respected for it role in formulating and implementing US GAAP despite the general vote of confidence. In India, the Statements on Accounting Standards are issued by the Institute of Chartered Accountants of India (ICAI) to establish standards that have to be complied with to ensure that financial statements are prepared with generally accepted accounting standards in India (India GAAP)

The Council of ICAI constituted the Accounting Standards Board (ASB) in April 1977 to formulate Accounting Standards. While formulating the Accounting Standards, ASB takes into consideration the applicable laws, usages and business environment. However, users were strongly critical about certain aspects of financial statements and they offered or supported many substantive ideas for improvement. Standard setters, regulators, and many others devote considerate resources in maintaining and improving the standards.

The new accounting norms are aimed at protecting shareholders interest and recommending ways of improving corporate governance

Format of each Standard contains:

1. A statement of concepts and fundamental accounting principles relating to the standards.
2. Definition of the terms used in standard.
3. The manner in which the accounting principles have been applied for formulating the standard
4. Presentation and disclosure requirements.
5. Class of enterprise to which it applies
6. Effective date.

ACCOUNTING STANDARDS BENEFITS:

Running a business is not just about earning profits, depositing money in the bank, paying employees, and luring more clients and customers. It is about knowing if the business is thriving or if the owner is just investing in something that is not going to earn at all.

Businesses have to have accounting standards to ensure that everything goes smoothly and that cash flow is running perfectly. These accounting measures for businesses also have to adhere to the accounting standards set by regulating bodies like the ASB and the ICAI. This is because there are policies and other documents that are imperative to every accounting act. In many cases, businesses hire the services of auditors and bookkeepers in order to make sure that all record-keeping practices are done correctly. Doing so will provide access to investor capital, facilitate reasonable assessment of performance, and prevent costs brought about by legal action.

Here are other reasons why accounting standards are important to every business:

PROTECTING INVESTORS: By employing accounting standards, investors' interests are ensured as the documents they review are definitely accurate and genuine. As investors, they are interested to know that their money will eventually earn and go back to them. Accounting standards increase the investors' confidence in the business.

REGULATORY COMPLIANCE: Government regulators set accounting standards that have to be adhered to by all companies. This is both beneficial to the investor or business owner as well as to the customers or clients because it protects all of them from fraud in businesses. It also promotes transparency among the business' transactions, which will eventually lead to the improved efficiency of the markets. Following accounting standards set by the ASB and the ICAI will help prevent a company or business from spending on legal actions initiated by the government against it.

ASSESSING BUSINESS PERFORMANCE: The use of accounting standards will enable a business to see or assess its performance. By doing so, it can also compare and contrast its performance with other companies or competitors. These standards also help a business see its strengths and weaknesses. By also comparing past and current performances, a business can assess the success of its strategies.

Businesses will either prosper or fall. Depending on the trends and the economy of the country, an investment may grow or go down the drain. But in the end, accounting standards will make a difference. That is why all businesses have to follow and strictly adhere to these accounting standards.

PROCEDURE FOR ISSUING AN ACCOUNTING STANDARDS

Broadly, the following procedure is adopted for formulating Accounting Standard:

1. The ASB determines the broad areas in which Accounting Standards need to be formulated and the priority in regard to the selection thereof.
2. In the preparation of Accounting Standards, the ASB will be assisted by Study Groups constituted to consider specific subjects. In the formation of Study Groups, provision will be made for wide participation by the members of the Institute and others.
3. The draft of the proposed standard will normally include the following:
   (a) Objective of the Standards,
   (b) Scope of the Standard,
   (c) Definitions of the terms used in the Standard,
   (d) Recognition and measurement principles, whereever applicable,
   (e) Presentation and disclosure requirements.
4. The ASB will condier the preliminary draft prepared by the Study Group and if any revision of the draft is required on the basis of deliberations, the ASB will make the same or refer the same to the Study Group.
5. The ASB will circulate the draft of the Accounting Standard to the Council memebrs of the ICAI and the following specified bodies for their comments:

(i) Department of Company Affairs (DCA)
(ii) Comptroller and Auditor General of India (C&AG)
(iii) Central Board of Direct Taxes (CBDT)
(iv) The Institute of Cost and Works Accountants of India (ICWAI)
(v) The Institute of Company Secretaries of India (ICSI)
(vi) Associated Chambers of Commerce and Industry (ASSOCHAM), Confederation of Indian Industry (CII) and Federation of Indian Chambers of Commerce and Industry (FICCI)
(vii) Reserve Bank of India (RBI)
(viii) Securities and Exchange Board of India (SEBI)
(ix) Standing Conference of Public Enterprises (SCOPE)
(x) Indian Banks' Association (IBA)
(xi) Any other body considered relevant by the ASB keeping in view the nature of the Accounting Stnadard.

6. The ASB will hold a meeting with the representatitves of specified bodies to ascertain their views on the draft of the proposed Accounting Standards. On the basis of comments received and discussion with the representatives of specified bodies, the ASB will finalise the Exposure Draft of the proposed Accounting Standard.
7. The Exposure Draft of the proposed Standard will be issued for comments by the members of the Institute and the public. The Exposure Draft will specifically be sent to specified bodies (as listed above), stock exchanges, and other interest groups, as appropriate.
8. After taking into cosideration the comments received, the draft of the proposed Standard will be finalised by the ASB and submitted to the Council of the ICAI.
9. The Council of the ICAI will consider the final draft of the proposed Standard, and if found necessary, modify the same in consultation with the ASB. The Accounting Standard on the relevant subject will then be issued by the ICAI.
10. For a substantive revision of an Accounting Standard, the procedure followed for formulation of a new Accounting Standard, as detailed above, will be followed.
11. Subsequent to issuance of an Accounting Standard, some aspect(s) may require revision which are not substantive in nature. For this purpose, the ICAI may make limited revision to an Accounting Standard. The procedure followed for the limited revision will substantially be the same as that to be followed formulation of an Accounting Standard, ensuring that sufficient opportunity is given to various interest groups, and general public to react to the proposal for limited revision.

Accounting Standards Issued by the Institute of Chatered Accountants of India are as below:

Number of the Accounting Standard (AS)	*Title of the Accounting Standard*	*Date from which Mandatory (Accounting Periods Commencing on or After)*	*Enterprises to which Applicable*
AS-1	Disclosure of accounting policies	1-4-1993	All
AS-2 (Revised)	Valuation of inventories	1-4-1999	All
AS-3 (Revised	Cash Flow Statement	1-4-2001	Level-1
AS-4 (Revised)	Contingencies and events occurring after the balance sheet date	1-4-1998	All
AS-5 (Revised)	Net profit or loss for the period, prior period items and changes in accounting policies	1-4-1996	Level-I
AS-6 (Revised)	Depreciation Accounting	1-4-1995	All
AS-7 (Revised)	Construction Contracts	1-4-2002	All
AS-8	Withdrawn and included in AS-26	———————	————-
AS-9	Revenue Recognition	1-4-1993	All
AS-10	Accounting for fixed assets	1-4-1993	All
AS-11 (Revised 2003)	The effects of changes in foreign exchange rates	1-4-2004	All
AS-12	Accounting for government grants	1-4-1994	All
AS-13	Accounting for investments	1-4-1995	All
AS-14	Accounting for amalgamations	1-4-1995	All
AS-15	Employees benefits	1-4-2006	All
AS-16	Borrowing costs	1-4-2000	All
AS-17	Segment reporting	1-4-2001	Level-I
AS-18	Related party disclosures	1-4-2001	Level-I
AS-19	Leases	1-4-2001	All
AS-20	Earning per share	1-4-2001	Level-I Refer AS-12
AS-21	Consolidated financial statements	1-4-2001	See note 1
AS-22	Accounting for taxes on income	1-4-2001	For listed co.
		1-4-2002	Co. other than listed
		1-4-2006	See note 2
		1-4-2002	All
AS-23	Accounting for investment in associates in consolidated financial statements		
AS-24	Discounting operations	1-4-2004	All

AS-25	Interium financial reporting	1-4-2002	Level-I
AS-26	Intangible assets	1-4-2003	Level-I
AS-27	Financial reporting of interests in joint ventures	1-4-2002	See note 1
AS-28	Impairment of asset	1-4-2004	Level-I
	Amendments	1-4-2006	Level-II
	Amendments	1-4-2008	Level-III
AS-29	Provisions, contingent liabilities and contingent assets	1-4-2004	All
AS-30	Financial Instruments — Recognition and Measurement	1-4-2011	Non SMC
AS-31	Financial Instruments — Presentation	1-4-2011	Non SMC
AS-32	Financial Instruments — Disclosure	1-4-2011	Non SMC

- AS-8 was withdrawn in pursuant to AS-26 becoming mandatory.
- 29 accounting standards are issued as of date and only 28 are applicable
- AS-30, AS-31, AS-32 are published but they will come into effect from 1.4.2009. It is mandatory on or after 1.4.2011.

Disclosure of Accounting Policies: Accounting Policies refer to specific accounting principles and the method of applying those principles adopted by the enterprises in preparation and presentation of the financial statements.

Valuation of Inventories: The objective of this standard is to formulate the method of computation of cost of inventories/stock, determine the value of closing stock/inventory at which the inventory is to be shown in balance sheet till it is not sold and recognized as revenue.

Cash Flow Statements: Cash flow statement is additional information to user of financial statement. This statement exhibits the flow of incoming and outgoing cash. This statement assesses the ability of the enterprise to generate cash and to utilize the cash. This statement is one of the tools for assessing the liquidity and solvency of the enterprise.

Contigencies and Events Occuring after the Balance Sheet Date: In preparing financial statement of a particular enterprise, accounting is done by following accrual basis of accounting and prudent accounting policies to calculate the profit or loss for the year and to recognize assets and liabilities in balance sheet. While following the prudent accounting policies, the provision is made for all known liabilities and losses even for those liabilities/events, which are probable. Professional judgement is required to classify the likehood of the future events occuring and, therefore, the question of contingencies and their accounting arises. Objective of this standard is to prescribe the accounting of contigencies and the events, which take place after the balance sheet date but before approval of balance sheet by Board of Directors. The Accounting Standard deals with Contingencies and Events occuring after the balance sheet date.

Net Profit or Loss for the Period, Prior Period Items and Change in Accounting Policies: The objective of this accounting standard is to prescribe the criteria for certain items in the profit and loss account so that comparability of the financial statement can be enhanced. Profit and loss account being a period statement covers the items of the income and expenditure of the particular period. This accounting standard also deals with change in accounting policy, accounting estimates and extraordinary items.

Depreciation Accounting: It is a measure of wearing out, consumption or other loss of value of a depreciable asset arising from use, passage of time. Depreciation is nothing but distribution of total cost of asset over its useful life.

Construction Contracts: Accounting for long-term construction contracts involves question as to when revenue should be recognized and how to measure the revenue in the books of contractor. As the period of construction contract is long, work of construction starts in one year and is completed in another year or after 4-5 years or so. Therefore question arises how the profit or loss of construction contract by contractor should be determined. There may be following two ways to determine profit or loss: On year-to-year basis based on percentage of completion or on completion of the contract.

Revenue Recognition: The standard explains as to when the revenue should be recognized in profit and loss account and also states the circumstances in which revenue recognition can be postponed. Revenue means gross inflow of cash, receivable or other consideration arising in the course of ordinary activities of an enterprise such as:- The sale of goods, rendering of services, and use of enterprises resources by other yielding interest, dividend and royalties. In other words, revenue is a charge made to customers/clients for goods supplied and services rendered.

Accounting for Fixed Assets: It is an asset, which is held with intention of being used for the purpose of producing or providing goods and services. Not held for sale in the normal course of business. Expected to be used for more than one accounting period.

The Effects of Changes in Foreign Exchange Rates: Effect of Changes in Foreign Exchange Rate shall be applicable in Respect of Accounting Period commencing on or after 01-04-2004 and is mandatory in nature. This Accounting Standard applicable to accounting for transaction in Foreign currencies in translating the Financial Statement of foreign operation integral as well as non-integral and also accounting for forward exchange. Effect of Changes in Foreign Exchange Rate, an enterprises should disclose following aspects:

- ➜ Amount Exchange Difference included in Net Profit or Loss;
- ➜ Amount accumulated in foreign exchange translation reserve;
- ➜ Reconciliation of opening and closing balance of Foreign Exchange translation reserve;

Accounting for Government Grants: Governement Grants are assistance by the Govt. in the form of cash or kind to an enterprise in return for past or future compliance with certain conditions. Government assistance, which cannot be valued reasonably, is excluded from Govt. grants. Those transactions with Government, which cannot be distinguished from the normal trading transactions of the enterprise, are not considered as Government grants.

Accounting for Investments: It is the assets held for earning income by way of dividend, interest and rentals, for capital appreciation or for other benefits.

Accounting for Amalgamation: This accounting standard deals with accounting to be made in books of Transferee company in case of amalgamtion. This accounting standard is not applicable to cases of acquisition of shares when one company acquires/purcahses the share of another company and the acquired company is not dissolved and its seperate entity continues to exist. The standard is applicable when acquired company is dissolved and seperate entity ceases to exist and purchasing company continues with the business of acquired company

Employee Benefits: Accounting Standard has been revised by ICAI and is applicable in respect of accounting periods commencing on or after 1st April 2006. The scope of the accounting standard has been enlarged, to include accounting for short-term employee benefits and termination benefits.

Borrowing Costs: Enterprises are borrowing the funds to acquire, build and install the fixed assets and other assets, these assets take time to make them usable or saleable, therefore the enterprises incur the interest (cost on borrowing) to acquire and build these assets. The objective of the Accounting Standard is to prescribe the treatment of borrowing cost (interest + other cost) in accounting, whether the cost of borrowing should be included in the cost of assets or not.

Segment Reporting: An enterprise needs in multiple products/services and operates in different geographical areas. Multiple products/services and their operations in different geographical areas are exposed to different risks and returns. Information about multiple products/services and their operation in different geographical areas are called segment information. Such information is used to assess the risk and return of multiple products/services and their operation in different geographical areas. Disclosure of such information is called segment reporting.

Related Party Disclosure: Sometimes business transactions between related parties lose the feature and character of the arms length transactions. Related party relationship affects the volume and decision of business of one enterprise for the benefit of the other enterprise. Hence disclosure of related party transaction is essential for proper understanding of financial performance and financial position of the enterprise.

Accounting for Leases: Lease is an arrangement by which the lessor gives the right to use an asset for a given period of time to the lessee on rent. It involves two parties, a lessor and a lessee and an asset which is to be leased. The lessor who owns the asset agrees to allow the lessee to use it for a specified period of time in return of periodic rent payments.

Earning Per Share: Earning per share (EPS)is a financial ratio that gives the information regarding earning available to each equity share. It is very important financial ratio for assessing the state of market price of share. This accounting standard gives computational methodology for the determination and presentation of earning per share, which will improve the comparison of EPS. The statement is applicable to the enterprise whose equity shares or potential equity shares are listed in stock exchange.

Consolidated Financial Statements: The objective of this statement is to present financial statements of a parent and its subsidiary(ies) as a single economic entity. In other words the holding company and its subsidiary(ies) are treated as one entity for the preparation of these consolidated financial statements. Consolidated profit/loss account and consolidated balance sheet are prepared for disclosing the total profit/loss of the group and total assets and liabilities of the group. As per this accounting standard, the conslidated balance sheet if prepared should be prepared in the manner prescribed by this statement.

Accounting for Taxes on Income: This accounting standard prescribes the accounting treatment for taxes on income. Traditionally, amount of tax payable is determined on the profit/loss computed as per income tax laws. According to this accounting standard, tax on income is determined on the principle of accrual concept. According to this concept, tax should be accounted in the period in which corresponding revenue and expenses are accounted. In simple words tax shall be accounted on accrual basis; not on liability to pay basis.

Accounting for Investments in Associates in Consolidated Financial Statements: The accounting standard was formulated with the objective to set out the principles and procedures for recognizing the investment in associates in the cosolidated financial statements of the investor, so that the effect of investment in associates on the financial position of the group is indicated.

Discontinuing Operations: The objective of this standard is to establish principles for reporting information about discontinuing operations. This standard covers "discontinuing operations" rather than "discontinued operation". The focus of the disclosure of the Information is about the operations which the enterprise plans to discontinue rather than dsclosing on the operations which are already discontinued. However, the disclosure about discontinued operation is also covered by this standard.

Interim Financial Reporting (IFR): Interim financial reporting is the reporting for periods of less than a year generally for a period of 3 months. As per clause 41 of listing agreement the companies are required to publish the financial results on a quarterly basis.

Intangible Assets: An Intangible Asset is an identifiable non-monetary asset without physical substance held for use in the production or supplying of goods or services for rentals to others or for administrative purpose

Financial Reporting of Interest in Joint Ventures: Joint Venture is defined as a contractual arrangement whereby two or more parties carry on an economic activity under '**joint control**'. Control is the power to govern the financial and operating policies of an economic activity so as to obtain benefit from it. 'Joint control' is the contractually agreed sharing of control over economic activity.

Impairment of Assets: The dictionary meaning of 'impairment of asset' is weakening in value of asset. In other words when the value of asset decreases, it may be called impairment of an asset. As per AS-28, asset is said to be impaired when carrying amount of asset is more than its recoverable amount.

Provisions, Contingent Liabilities and Contingent Assets: Objective of this standard is to prescribe the accounting for Provisions, Contingent Liabilitites, Contingent Assets, Provision for Restructuring Cost. Provision: It is a liability, which can be measured only by using a substantial degree of estimation. Liability: A liability is present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

Financial Instrument: Recognition and Measurement, issued by The Council of the Institute of Chartered Accountants of India, comes into effect in respect of Accounting periods commencing on or after 1-4-2009 and will be recommendatory in nature for an initial period of two years. This Accounting Standard will become mandatory in respect of Accounting periods commencing on or after 1-4-2011 for all commercial, industrial and business entities except to a Small and Medium-sized Entity. The objective of this Standard is to establish principles for recognizing and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. Requirements for presenting information about financial instruments are in Accounting Standard.

Financial Instrument Presentation: The objective of this Standard is to establish principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and financial liabilities. It applies to the classification of financial instruments, from the perspective of the issuer, into financial assets, financial liabilities and equity instruments; the classification of related interest, dividends, losses and gains; and the circumstances in which financial assets and financial liabilities should be offset. The principles in this Standard complement the principles for recognising and measuring financial assets and financial liabilities in Accounting Standard Financial Instruments:

Financial Instruments, Disclosures and Limited Revision to Accounting Standards: The objective of this Standard is to require entities to provide disclosures in their financial statements that enable users to evaluate:

- ➔ the significance of financial instruments for the entity's financial position and performance; and
- ➔ the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the reporting date, and how the entity manages those risks.

AS-1: Disclosure of Accounting Policies. *Effective date April 1993*

This statements deal with the disclosures of significant accounting policies followed in preparing and presenting financial statements. The purpose of this statement is to promote preparing and presenting financial statements by instituting the disclosure of significant accounting policies in the financial statements and the manner of doing it.

The emphasis in AS-1 is on disclosure of accounting policies in the presentation of financial statements. These are normally to be disclosed at one place. All the companies now follow this practice. Accounting Polices refer to the specified accounting principles, adopted by the enterprise and methods of applying these principles in the preparation and presentation of financial statements. Some of the areas in which such disclosure is to be made are as under:

1. Methods of depreciation, depletion and amortization
2. Treatment of expenditure during construction
3. Valuation of inventories
4. Conversion or translation of foreign currency items
5. Treatment of goodwill
6. Valuation of investments

7. Valuation of fixed asset
8. Recognition of profits on long-term contracts
9. Treatment of retirement benefits
10. Treatment of contingent liabilities

It is for the management to select the accounting policy to be followed by the enterprise. However, while making this selection, it is necessary to ensure that the financial statements present a true and fair view of the state of affairs. The major considerations to be followed during the selection of accounting policies are stated in AS-1 as under.

- ➜ Prudence: This is a world of uncertainty. Profits are recognized only when realized. At the same time, provisions for all known liabilities and losses are made though the amount represents only the best estimate.
- ➜ Substance over form: The accounting treatment and presentation of transactions and events in the financial statements should be governed by their substance and not just by the legal form. For example, the accounting of finance leases is based on the substance rather than the form of transaction. The lessee capitalizes the lease equipment as fixed assets being the owner in the substance, whereas the lessor records the investment made as debtor
- ➜ Materiality: Financial statements disclose all material facts. The IASC audit materiality as under.

"Information is material if its omission or misstatement could influence the economic decision of users taken on the basis of financial statements. Materiality depends on the size of the item or error judged in the particular circumstances of its omission or misstatements. Thus materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic whose information should be there to be useful."

There are no hard and fast rules for determining materiality. Materiality is a matter of judgment. For instance, what is material to the financial statements of one firm may not be material to the financial statements of another firm of a different nature or size.

Why are Accounting Policies required to be disclosed:

1. Accounting Policies means principles and methods to apply the principles adopted by the enterprise in the preparation and presentation of financial statements. Example, providing for depreciation is accounting principle and the methods are SLM, WDV or any other appropriate method.
2. The state of affairs and of the profit or loss can be significantly affected by the accounting policies followed. The need for disclosure of accounting policies arises because accounting policies may differ from enterprise to enterprise and for different years within the same enterprise. Accounting policies can differ in many areas, example;
   (a) Depreciation on Fixed Assets.
   (b) Valuation of Inventories.
   (c) Valuation of Investments.

(d) Valuation of Fixed Assets.
(e) Treatment of Foreign Currency Translations.
(f) Treatment of Government Grants.
(g) Treatment of Goodwill.
(h) Treatment of Research and Development Costs.
(i) Treatment of Retirement benefits
(j) Recognition of Profit on Long-term Contracts.
(k) Treatment of Contingent Liabilities, etc.

What are Fundamental Accounting Assumptions? Are they required to be disclosed in the financial statements?

Certain fundamental accounting assumptions underlie the preparation and presentation of financial statements. These accounting assumptions are assumed to have been followed in preparation of Financial Statements and need not be disclosed. If any of these fundamental assumptions are not followed then this fact must be disclosed in the Financial Statements. The fundamental accounting assumptions are as follows;

1. **Going Concern/Concept of Continuity/Concept of Permanency:**

   According to this concept any business concern will continue to operate its activities for a fairly long time, i.e. it will have a perpetual succession. It is assumed that the business enterprise has got no intention to close down its business activities. Continuing activity is the normal business process. Business enterprise will never assume its closure till the circumstances are such that closure becomes inevitable.

2. **Consistency:**

   The comparison of one accounting period with the other is possible only when the consistency is followed. It means accounting from one accounting period to another should be on the same basis.

3. **Accrual:**

   Revenues and costs are accrued, i.e., recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate. The accrual concept forces the matching of revenues against relevant costs.

What are the Principles Governing selection of Accounting Policy:

The overriding obligation to provide “True and Fair View” of the state of affairs of the enterprise is the major consideration in selection of Accounting Policies. Major points which are considered for the purpose of selection and application of Accounting Policies are:

1. **Prudence (Conservatism):**

   Prudence is the caution in the exercise of judgements when making estimates. According to this principle, business enterprise should consider all future losses but ignore all the anticipated profits. Profits should be considered only when it is actually realised. In other words “Anticipate no profit but provide for all losses”. Example, inventory is valued at cost or net realisable value, whichever is less.

2. **Substance over Form:**

   Economic reality of the transaction is important than the legal form for its accounting treatment and presentation in financial statements. Example, assets purchased on hire purchase are shown in the books of buyer inspite of the fact that the hire purchase buyer is not the legal owner.

3. **Materiality:**

   Financial statements should disclose all "material" information. Information is material if it can influence the decision of the user of financial statement or information is material if its omission or wrong statement could influence the economic decisions taken by the user based on such financial statements.

AS-2: VALUATION OF INVENTORIES (STOCK)

Meaning and Definition

Inventories consist of the following:

1. Held for sale in the ordinary course of business (finished goods).
2. In the process of production of such sale (raw material and work-in-progress).
3. In the form of materials or supplies to be consumed in production process or in the rendering of services (stores, spares, raw material, consumables). Inventories do not include machinery.
4. Spares, which can be used only in connection with an item of fixed assets and whose use is irregular. Such machinery spares are accounted for in accordance with AS-10 'accounting for fixed assets'.

Accounting for Machinery Spares (ASI-2)

The Institute of Chartered Accountants of India has issued ASI-2 providing interpretative guidance on accounting for machinery spares in compliance with AS-2 and AS-10 which is as under:

1. Machinery spares, which are not specific to a particular item of fixed asset but can be used generally for various items of fixed assets, should be treated as inventories for the purpose of AS-2. Such machinery spares should be charged to the statement of profit and loss as and when issued for consumption in the ordinary course of operations.
2. Whether to capitalise machinery spare under AS-10 or not will depend on the facts and circumstances of each case. However, the machinery spares of the following types should be capitalized being of the nature of capital spares/insurance spares:
   (i) Machinery spares which are specific to a particular item of fixed asset, i.e., they can be used only in connection with a particular item of the fixed asset, and
   (ii) Their use is expected to be irregular.
3. Machinery spares of the nature of capital spares/insurance spares should be capitalised separately at the time of their purchase whether procured at the time of purchase of the fixed asset

concerned or subsequently. The total cost of such capital spares/insurance spares should be allocated on a systematic basis over a period not exceeding the useful life of the principal item, i.e., the fixed asset to which they relate.

4. When the related fixed asset is either discarded or sold, the written down value less disposal value, if any, of the capital spares/insurance spares should be written off.
5. The stand-by equipment is a separate fixed asset in its own right and should be depreciated like any other fixed assets.

Special Features of AS-2 (Revised)

AS-2 has been revised with a view to eliminate various alternatives given in the cost formulae and methods of costing. The following are special features of AS-2 :

1. Definition of inventory has been changed. Earlier inventories are defined as tangible property, now it has been defined as asset. By this, intangibles can be treated as inventory.
2. Direct costing approach for costing inventories has been eliminated. While determining cost of inventories it becomes necessary to consider both fixed and variable overheads.
3. Base stock and LIFO formulae are eliminated. Application of weighted average formula has been specified. Earlier the formula was mentioned as average, which could mean simple average as well as weighted average.
4. By-products, wastes and spares are to be valued at net realisable price if their value is not material.
5. Materials and supplies need not be written down applying net realisable value, if the finished goods in which they are to be used is expected to realise cost.

Objective

The objective of Accountings Standard 2 is to formulate the method of computation of cost of inventories/stock determine the value of closing stock/inventory at which the inventory is to be shown in Balance Sheet till it is not sold and recognized as revenue.

APPLICABILITY

Part I and Part II of the Schedule VI to the Companies Act, 1956 have suggested inventory valuation and disclosure techniques. Accounting Standard 2 (AS-2) "Valuation of Inventories" issued by the Institute of Chartered Accountants to supplement the legal reguirements.

Recently AS-2 has been revised. It is applicable with accounting period commencing on or after 1st April, 1999. It is applicable to all enterprises and is mandatory for all enterprises.

AS-2 is not applicable in following cases:

1. Work-in-progress arising under construction contract including directly related to service contract.
2. Work-in-progress arising in ordinary course of business for service providers (Incomplete consultancy services, Incomplete merchant bank activities, Medical services in progress)

3. Financial instrument held as stock-in-trade (Shares, Debentures, Bonds etc.)
4. Producer's inventories like livestock, agricultural and forest products, mineral oils, ores and gases. Such inventories are valued at net realizable value.

MEASUREMENT OF INVENTORY

Para 5 of AS-2 (Revised) requires that inventories should be valued at lower of the cost and net realizable value. This is an age-old principle of valuation of current assets.

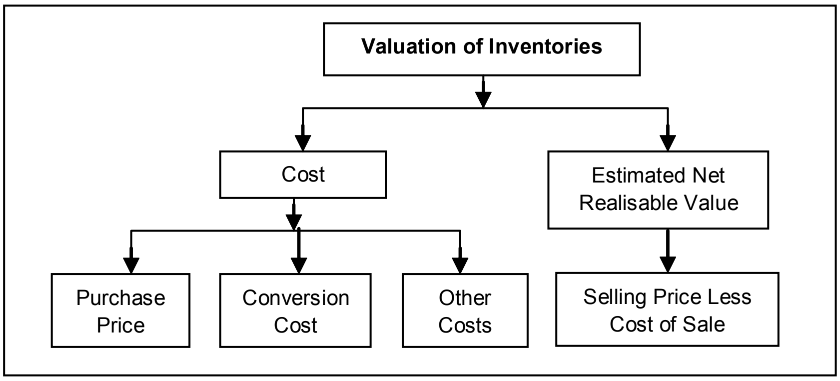

Fig. 1.1

Three important aspects of inventory valuation are:

- Measurement of cost.
- Measurement of net realisable value.
- Comparison between the cost and net realizable value.

Measurement of Cost

Cost of inventories comprise:

- Cost of purchases;
- Cost of conversion, and
- Other costs incurred in bringing the inventories to their present position and location.

Cost of Purchase

Cost of purchase includes:

1. Purchase price.
2. Duties and taxes.
3. Freight inward.
4. Other expenditures directly attributable to the acquisition.

Less:

(i) Duties and taxes recoverable by enterprise from taxing authorities.
(ii) Trade discount.
(iii) Duty drawback.
(iv) Other similar items.

Cost of Conversion

This includes cost directly related to units of production, i.e., Direct Labour, Direct Material, Direct Expenses + Systematic Allocation of Fixed and Variable Production Overheads that are incurred in converting material into finished goods.

Fixed Production Overheads

Fixed overheads remain fixed within a range of activities. They are step cost in nature. AS-2 (Revised) explains that fixed production overheads are indirect costs, which remain relatively constant regardless of the volume of production. Examples are: depreciation, maintenance of factory building and equipment and the cost of factory management and administration.

Variable Production Overheads

These are defined as indirect costs of production that vary directly or indirectly with the volume of production, such as indirect materials and indirect labour.

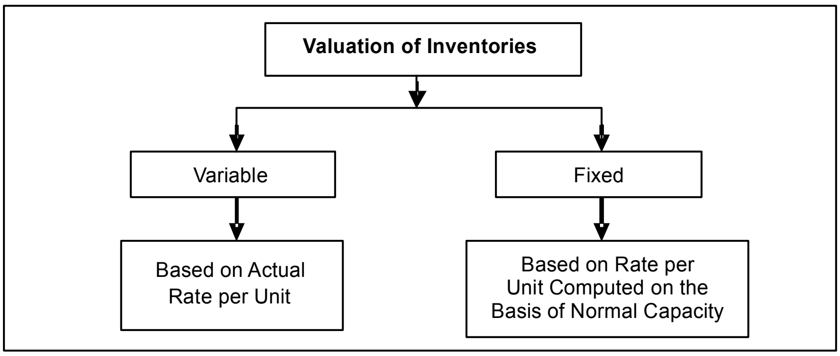

Fig. 1.2

Allocation of Fixed Production Overheads

Fixed production overheads are allocated to cost of conversion on the basis of normal capacity of production facilities. This principle takes care of fluctuation in actual capacity utilization, which results in fluctuation of fixed production overheads allocation. During the period of abnormally high production, the amount of fixed production overheads allocated to each unit of production is decreased so that inventories are not measured above cost.

Allocation of Variable Production Overheads

Variable production overheads are charged to each production unit on the basis of actual production.

Joint Products and By-products

Joint products emerge from the same production process. Generally, the cost of each product is not separately identifiable. Same is the case with a production situation when a main product and by-product emerges.

Definitions:

As per the standard literature, the terms joint products, main product any by-product are defined as follows:

1. **Joint Products:** Products that emerge from the same production process and are of significant value.
2. **Main Product:** The target product of significant value.
3. **By-product:** Products emerging from a process along with one more main products which are incidental and of insignificant value.

As the conversion cost of joint products or main products and by-products are not separately identifiable, it becomes necessary to allocate conversion cost on a national basis. If the by-products, scrap and waste materials are by nature not of material value, they are measured at net realisable value. Accordingly, net realisable value of by-products, scrap and waste is first deducted from the conversion cost, and balance of the conversion cost is distributed among the main products.

Treatment of Other Costs

Other costs are included in the inventories to the extent they are incurred for bringing the inventories to their present location and condition. AS-2 suggests that it may be required to charge non-production overheads to the cost of inventories when they are specifically incurred to bring the inventories at their present location and condition. In the same way, cost of designing may be included in the cost of inventories manufactured for special customers.

Inclusion of Excise Duty in Valuation of Finished Goods

Excise duty is required for bringing inventory to its present location and condition and being a direct cost, it should be included in the valuation of inventories. As per AS-2, excise duty is required to be included in the valuation of finished goods though excise duty is paid only when goods are removed from the factory. The Guidance Note on "Accounting Treatment for Excise Duty" issued by ICWA states that "**since the liability for excise duty arises when the manufacture of the goods is completed, it is in factory or bonded warehouse. The estimate of such liability can be made at the rates in force on the balance sheet date. The excise duty paid/provided on finished goods should therefore, be included, in inventory valuation.**" In estimating the provision, the factors to be considered are – whether the finished goods lying in stock in the current year would form part of the exempted goods next year and whether excise duty exemptions will continue in the next year. For instance, no excise duty would be included on stock meant for exports as excise is not leviable on goods meant for exports. It may be noted that in one case, a provision for excise duty will be made whereas in other case such provision will also be included as cost of inventory, therefore, the impact on profit and loss account will be nil.

Exclusion from Cost of Inventories

The following costs should be excluded from the Cost of Inventories:

1. Abnormal amounts of wasted materials, labour, other production costs.
2. Storage cost.
3. Administrative overheads.
4. Selling and distribution cost.
5. Interest and borrowing cost. However, if AS-16 allows such cost to be included, it can form part of the cost.

COST FORMULA

Specific Identification Method

Para 14 of AS-2 prescribes to use of specific identification method for determining cost of inventories. Specific identification means directly linking the costs with specific items of inventories. In case of some specified items, it is possible to identify and allocate the cost that seems to be the best method of cost ascertainment. Inventories earmarked for a specific project or purpose fall under this category. These items should not be ordinarily interchangeable.

Where specific identification method is not applicable

For the purpose of cost determination of other inventories not covered under specification identification method, AS-2 requires to follow either of the two cost formulae:

1. First in First Out (FIFO).
2. Weighted Average Method.

Either of the two formulae can be used for the determination of cost of:

(i) Raw material inventories.
(ii) Work-in-Progress.
(iii) Finished goods.
(iv) Stores and spares.

When it is not practical to calculate the cost, the following methods may be followed to ascertain cost of inventories.

Standard Cost

Retail Method

These two methods are used for convenience if the results approximate actual cost.

Standard Cost

Standard cost is ascertained by taking into account normal level of consumption of material and supplies, labour efficiency and capacity utilisation. Standard cost has to be regularly reviewed and revised by taking into account the current condition.

Retail Method

Retail Method is normally employed in retail business, when it is difficult to ascertain cost of individual item. It is applicable when items of inventories are rapidly changing items and have similar margins and for which it is not practicable to use other costing method.

Under the Retail Method, the cost of inventory is determined by reducing from the sale value of inventories the approximate percentage of gross margin. The percentage applied takes into account the inventory that has been marked down to below its original selling price. Retail method formula is also known as adjusted selling price formula.

Measurement of Net Realisable Value

As per AS-2 (Revised), Inventories are valued at a lower of the cost and net realizable value. The principle of net realizable value is based on the view that assets should not be carried in excess of amounts expected to be realized from their sale. Cost of inventories may not be recoverable for various reasons:

1. Inventories are damaged.
2. Inventories become obsolete.
3. Market price has declined.
4. Production cost has increased.

Net realisable value is defined as the estimated selling price in the ordinary course of business less the estimated cost of completion and the estimated cost necessary to make the sale.

Estimation of Net Realisable Value

The net realisable value of the materials and other supplies held for use in production of finished goods is estimated as under:

1. If finished product in which raw materials and supplies used is sold at cost or above cost, then the estimated realizable value of raw materials and supplies is considered more than its cost.
2. If finished product in which raw materials and supplies used is sold below cost. Then, the estimated realizable value of raw materials or supplies is equal to replacement price of raw materials or supplies.

Comparison between the Cost and Realisable Value

Para 18 of AS-2 requires that comparison between historical cost and net realizable value should be made item by item or by a group of items. Total historical cost of inventories should not be compared with total net realizable value. Comparison of aggregates may distort the value of inventories, because one or two items having low historical costs may offset low net realisable value of other items.

DISCLOSURE IN FINAL ACCOUNTS

Para 26 of AS-2 requires very simple disclosure. The financial statement should disclose

1. the accounting policies adopted in measuring inventories including the cost formulae used.
2. the total carrying amount of the inventories and its classification appropriate to the enterprise. For instance, finished goods, WIP, raw material, spare parts and its carrying amount.

Guidance Note on MODVAT/CENVAT

ICAI issued a "Guidance Note on Accounting Treatment for MODVAT/CENVAT" with the substitution of the MODVAT credit scheme with CENVAT *w.e.f.* 1st April, 2000. The revised Guidance Note has provided clarification on the above anomaly, with examples on both the inclusive method (Sec.145A) and exclusive method (AS-2) where it is clear that the above anomaly is only in respect of the disclosure with no effect on the total profit/loss of the enterprise.

Therefore, for purposes of tax filings and tax audit firms, the inclusive method should be used as per Section 145 A of the Income Tax Act, whereas for purposes of general purpose of financial statements, the exclusive method under AS-2 should be followed.

Inclusive Method (Gross Value Approach)

1. Raw material is accounted for at gross value inclusive of specified duty.
2. CENVAT credit available on final products can be accounted for through a separate account CENVAT Credit Availed Account.
3. Inputs may be consumed partly. CENVAT credit available should be segregated into two parts:
   - CENVAT credit on inputs consumed in respect of final products.
   - CENVAT credit on inputs lying in the stock.

CENVAT credit available on inputs consumed for final products is adjusted with the cost of raw materials consumed.

CENVAT credit available on inputs lying in the godown should be adjusted against the value of closing stock of raw materials.

Exclusive Method (Opening Separate CENVAT Credit Account)

1. Specified duty (i.e., duty paid against which CENVAT credit is available) paid on inputs is debited to a separate account, namely CENVAT Credit Receivable (Input) Account.
2. As and when CENVAT credit is actually utilised against payment of excise duty on final products, CENVAT Credit Receivable (Input) Account is credited.
3. Inputs consumed and inventory is valued excluding specified duty.
4. Balance standing in the CENVAT Credit Receivable (Input) Account is shown on the asset side of the Balance Sheet under Advances.

Courtesy Note on Source:

Guidance Note on MODVAT/CENVAT issued by the ICAI is reproduced from page 22 of *'Taxmann Students' Guide to Accounting Standards'* by D.S. Rawat.

Formula: Cost of Inventories

A. Cost of Purchase:			
(i) Purchase Price	xx		
(ii) Duties & Taxes	xx		
(iii) Freight Inward	xx		
(iv) Other Expenditure directly attributable to acquisition	xx	xx	
Less: (i) Duties and Taxes recoverable from tax authorities	xx		
(ii) Trade discount	xx		
(iii) Rebate	xx		
(iv) Duty Drawback	xx		
(v) Other similar items	xx	xx	xxx
B. Cost of Conversion:			
Direct Materials	xx		
Direct Labour	xx		
Direct Expenses	xx		
Systematic allocation of:			
Variable Production Overheads	xx		
Fixed Production Overheads	xx		xxx
C. Other Costs:			
Cost incurred for bringing the inventories to their present location and condition			xxx

SIMPLE ILLUSTRATION

1. Illustration: (Fixed production overheads including interest is given)

HCL Ltd., manufactures computers. During the year ended 31st March, 2015, the company manufactured 500 computers. The break up of cost is as under:

Raw Materials	₹ 450 lakhs
Direct Labour	₹ 300 lakhs
Variable Production Overheads	₹ 200 lakhs
Fixed Production Overheads (includes interest of ₹ 100 lakhs)	₹ 300 lakhs

Compute the cost per computer for the purpose of closing stock.

Solution:

As per AS-2 Inventory should be valued as per absorption costing.

The cost is calculated as under:

Calculation of Cost of Purchase

		₹ in lakhs
Raw Materials		450
Direct Labour		300
Variable Production Overheads		200
Fixed Production Overheads	300	
Less: Interest	100	200
		1,150

Cost per Computer = $\frac{1,150}{500}$ = 2.3 lakhs.

Note: Interest is excluded from cost of inventory.

2. Illustration: (Replacement cost given)

Raw material was purchased at ₹ 200 per kg. It is on decline. The finished goods in which raw material is incorporated are expected to be sold at below cost. 5,000 kgs of raw material is in stock at the end of the year. Replacement cost is ₹ 180 per kg.

- How would you decide the value of inventory?

Solution:

In this case, it is mentioned that the price of material is declining. As a result finished goods are expected to be sold below cost. In such a case, replacement cost of material is the measure of valuation.

Hence, the stock will be valued at = 5000kgs @ ₹ 180

= ₹ 9,00,000

3. Illustration: (Historical cost and replacement value given)

Tata company deals in three products A, B and C, which are neither similar nor interchangeable. At the time of closing of its accounts for the year 2015-16; the historical cost and net realizable values of the items of closing stock are given below:

Items	Historical Cost (₹ in lakhs)	Net Realisable Value (₹ in lakhs)
A	25	20
B	20	20
C	10	15
	55	55

What will be the value of stock?

Solution:

Historical Cost or Net Realisable Value whichever is less is the value of stock. This should be done item by item as given below:

		₹ in lakhs
A.	Net Realisable Value	20
B.	Historical Cost	20
C.	Historical Cost	10
	Value of Closing Stock	50

4. Illustration: (Fixed production overheads and normal capacity given)

From the following information, find the value of inventory per kg of finished goods by Satyam Ltd., as on 31/3/2015.

Material Cost	₹ 150 per kg
Direct Labour Cost	₹ 50 per kg
Direct Variable Production Overheads	₹ 20 per kg

Fixed production overheads for the year on normal capacity of 1,00,000 kgs is ₹ 15 lakhs.

Finished goods on stock at the end of the year 3,000 kgs.

Solution:

As per AS-2 cost of conversion includes a systematic allocation of fixed and variable production overheads, which are incurred for converting materials into finished goods. The allocation of fixed production overheads is based on normal capacity.

Statement of Cost (per Kg)

	₹
Material Cost	150
Direct Labour	50
Direct Variable Production Overheads	20
Fixed Production Overheads $\left(\frac{15,00,000}{1,00,000}\right)$	15
	235

Value of Stock = 3,000 kgs @ ₹ 235

= ₹ 7,05,000

5. Illustration: (Duties and taxes recoverable and not recoverable given)

Ascertain the cost of purchase of inventories by using the data given by Reliance Ltd on 31/03/2013:

(i)	Cost of Purchase of Inventory	₹ 20 lakhs
(ii)	Duties & Taxes paid and recoverable from Tax Authorities	₹ 5 lakhs
(iii)	Trade Discount	₹ 2 lakhs
(iv)	Duties & Taxes paid and not recoverable	₹ 2 lakhs
(v)	Freight Inward	₹ 1 lakhs
(vi)	Other Expenses directly attributable to Acquisition of Inventory	₹ 2 lakhs

Solution:

Calculation of Cost of Purchase

		₹ in lakhs
Cost of Purchase		20
Duties & Taxes paid and not recoverable		02
Freight Inward		01
Other Expenses		02
		25
Less: Duties & Taxes recoverable from Tax Authorities	05	
Trade discount	02	07
Total		18

6. Illustration: (Duties and taxes not recoverable)

Ascertain the cost of purchase of inventory by using the data of Tata Ltd. as on 31/03/2016 given below:

(i)	Purchase Price	₹ 10 lakhs
(ii)	Duties and Taxes paid on the acquisition and are not recoverable	₹ 2 lakhs
(iii)	Freight Inward	₹ 1 lakhs
(iv)	Others paid for acquisition of inventory	₹ 1 lakhs

Solution:

Cost of Purchase

	₹ in lakhs
Cost of Purchase	10
Duties & Taxes not recoverable	02
Freight Inward	01
Other Expenses	01
Total	14

1. Exercise:

X Ltd. produces Chemical Y. From the following data, calculate the value of Closing Stock.

Direct Materials	:	₹ 10 per unit
Direct Labour	:	₹ 4 per unit
Chargeable Expenses	:	₹ 6 per unit
Normal Capacity	:	10,000 units p.a.
Actual Production	:	8,000 units p.a.
Fixed Production Overheads	:	₹ 40,000 p.a.

The company has 4,000 units of closing stock at the end of the year.

[Ans. ₹ 96,000]

2. Exercise:

Cost of Production of Product* 100 is given below:

Direct Material per unit	₹ 150
Direct Wages per unit	₹ 100
Overheads per unit	₹ 50
	₹ 300

As on the balance sheet date replacement cost of material is ₹ 120 per unit. There were 2,000 units of material on 31st March 2016.

Calculate the value of stock of material under the following conditions:

(i) If finished product is sold at ₹ 320 per unit, what will be the value of stock of material.

(ii) If finished product is sold at the rate of ₹ 280 per unit, what will be the value of closing stock of materials.

[Ans. (i) ₹ 3,00,000. (ii) ₹ 2,40,000]

3. Exercise:

Historical Cost and Net Realisable Value of five inventory items are given below:

Items	Historical Cost	Net Realisable Value.
	₹	₹
A	20,000	30,000
B	12,000	10,000
C	12,000	18,000
D	32,000	26,000
E	28,000	26,000
	1,04,000	1,10,000

Determine the value of inventory.

[Ans. ₹ 94,000]

4. Exercise:

Instant Ltd. incurred ₹ 40,00,000 as fixed production overheads per year. Its normal production is 2,00,000 units in a year.

In 2015 16, the production has been 80,000 units. On 31st March, 2016, the closing stock was 20,000 units. The cost details are as under:

Direct Materials	₹ 1,000 per unit
Direct Labour	₹ 500 per unit
Fixed Administration Overheads	₹ 20,00,000 p.a.

Calculate the value of Closing Stock.

[Ans. ₹ 304,00,000 per unit ₹ 1,520]

5. Exercise:

Indulkar Ltd. produced 1,00,000 units during the year 2015-16.

The cost per unit is as follows:

Direct Materials	₹ 100
Direct Labour	₹ 50
Direct Expenses.	₹ 10
	₹ 160

Production overheads are ₹ 2,00,000 of which 60% is variable. The company sold 80,000 units and 20,000 units were in stock as on 31st March, 2016. Normal capacity is 50,000 units.

Calculate the value of Closing Stock.

[Ans. Variable Production Overheads ₹ 1,20,000
Fixed Production Overheads ₹ 80,000
Variable Production Overheads per unit ₹ 1,20,000
₹ 1,00,000 = 1.20
Fixed Production Overheads ₹ 80,000 = 1.60
Per unit ₹ 50,000
Cost per unit ₹ 162.80
Value of Stock = 20,000 × 162.80
= ₹ 32,56,000]

6. Exercise:

How do you ascertain the cost of purchase of inventory by using the following data:

(i)	Purchase Price	₹ 5,00,000
(ii)	Duties and Taxes paid on the Acquisition of Inventory and are not recoverable	₹ 2,00,000

(iii)	Freight Inward	₹ 1,00,000
(iv)	Other Expenses for Acquisition of Materials	₹ 2,00,000

[Ans. ₹ 10,00,000]

AS – 9: REVENUE RECOGNITION

Meaning and Scope

AS-9: Revenue Recognition is mandatory and applicable to all enterprises for accounting periods commencing on or after 1st April, 1993. Accounting standard explains when the revenue should be recognised in Profit & Loss Account and also states the circumstances in which revenue recognition can be postponed.

Revenue is gross inflow of cash, receivable or other consideration arising in the course of ordinary activities of the reporting entity from sale of goods, rendering of services, and from the use of entity's resources by others yielding interest, dividend and royalties.

TRANSACTIONS EXCLUDED

Revenue recognition criteria as specified in Para 3 of AS-9 is not applicable to –

(i) Realised capital gains arising out of disposal of non-current assets and unrealised capital gains, i.e., appreciation in the value of fixed assets;

(ii) Unrealised holding gains in the value of current assets, i.e., increase in the market value of stock-in-trade;

(iii) Natural increase in the herds of livestock and agricultural and forest products;

(iv) Realised/unrealised gains arising out of fluctuations in foreign ex-change rates and translation of foreign currency financial statements,

(v) Realised gains resulting from discharge of an obligation at a lesser amount than the carrying amount;

(vi) Unrealised gains resulting from restatement of the carrying amount of the obligation.

Timing of Revenue Recognition – Rendering of Services

Revenue from sale of rendering services should be recognised at the time of the sale or rendering of services. However, if at the time of rendering of services or sale there is significant uncertainty in ultimate collection of the revenue, then the revenue recognition is postponed. In such cases, revenue should be recognised only when it becomes reasonably certain that ultimate collection will be made. It also applies to the revenue arising out of escalation of price, export incentive, interest etc.

REVENUE FROM SALES OF GOODS

1. As per paras 10-11 of AS-9, revenue from sale of goods is recognized when the seller transfers the goods to the buyer for a consideration.

   Revenue is recognized when all the following conditions are fulfilled:

   (i) Seller has transferred the ownership of goods to buyer for a price. Or all significant risks and rewards of ownership have been transferred to buyer.

   (ii) Seller does not retain any effective control of ownership of the transferred goods.

   (iii) There is no significant uncertainty in collection of the amount of consideration (i.e., cash, receivables etc.)

2. **Delivery delayed at buyer's request**

   In some cases, the buyer may request for delayed delivery although he purchases the goods, takes the title and accepts billing. In such situations, sale is complete although physical delivery of the goods is delayed. Accordingly, revenue should be recognised and the inventory level should be reduced. It is prudent to disclose the value of goods held on behalf of the buyer as on the Balance Sheet date by way of note.

3. **Revenue Recognition when delivery of goods sold subject to conditions:**

   (i) Installation and inspection:

   Revenue should be recognised when

   (a) goods are installed at the buyer's place to his satisfaction.

   (b) goods are inspected and accepted by the buyer.

   (ii) Sale on approval:

   Revenue should be recognised when buyer confirms his desire to buy such goods by communication.

   (iii) Guaranteed sales:

   In this case, revenue should be recognised as per the substance of the agreement of sale or after the reasonable period has expired.

   (iv) Warranty sales:

   Sales should be recognised immediately but the provision should be made to cover unexpired warranty.

   (v) Consignment sales:

   In this regard, revenue should be recognised only when the goods are sold to third party.

   (vi) Special Order Shipments:

   Revenue from such sales should be recognised when the goods identified and ready for delivery.

   (vii) Subscriptions for publication:

   (a) Items delivered vary in value from period to period. Revenue should be recognised on the basis of sales value of items delivered.

(b) Items delivered do not vary in value from period to period. In this case, revenue should be recognised on straight-line basis over time.

(viii) Instalment sales:

Revenue of sale price excluding interest should be recogised on the date of sale. Interest should be recognised proportionately to the unpaid balance.

(ix) Revenue swaps:

IAS-18 contains the provision for revenue swaps. However, no such corresponding provisions are given in AS-9. As per IAS-18, when goods or services are exchanged or swapped for goods or services, which are of a similar nature and value, the exchange is not regarded as a transaction, which generates revenue. However, when goods are sold or services are rendered in exchange for dissimilar goods, the exchange is regarded as a transaction, which generates revenue. Such revenue is measured at the fair value of the goods or service received, adjusted by the amount of any cash or cash equivalents transferred.

(x) Repo Arrangements:

Under IAS-18, the recognition criteria are applied to two or more transactions together when they are linked in such a way that the commercial effect connot be understood without reference to the series of transactions as a whole. For instance, a company may sell goods and, at the same time, enter into a separate agreement to repurchase the goods at a later date. Thereby, the substantive effect of the transaction is negated. In such a case the two transactions are dealt with together. The Accounting Standard-9 too in case of repo arrangements requires that such transactions should be recorded as financing arrangements. Therefore, the resulting cash inflow is not revenue and should not be recognised as revenue.

REVENUE FROM RENDERING OF SERVICES

Normally, revenue from service is recognised as the service is performed. The performance of service is measured by employing two methods:

1. Completed Service Contract Method:

Revenue is recognised when service is about to be completed and significant uncertainties exist about the collection of amount of service charges.

2. Proportionate Competition Method:

In this method, revenue is recognised by reference to the performance of each Act. Under this method, the revenue recognised is determined on the basis of contract value, associated cost, number of acts or other suitable basis. Further, no significant uncertainty exists about the collection of amount of service charges of performed acts.

Revenue Recognition Norms:

The norms for revenue recognition for **rendering of service** under special condition are as follows:

1. Installation Fees:

It is recognised when the installation is completed and it is accepted by the clients.

2. Advertising and Insurance Agency Commission:

In this regards, the norms are as laid down under:

(i) Advertising commission is recognised when the advertisement appears before public.

(ii) Insurance commission is recognised on the effective commencement/renewal date of the policies.

3. Financial Service Commission:

Revenue recognition of financial service commission is dependent upon:

(i) Whether the service has been provided 'once and for all' or is on a continuing basis.

(ii) The incidence of costs relating to the service.

(iii) When the payment for the service will be received.

As regards to commission charged for arranging or granting loan and other facilities, it should be recognised when a loan is sanctioned and accepted by borrower. Commitment facility or loan management fees that relate to continuing obligations or services, should normally be recognised over the life of the loan.

4. Admission Fee:

Revenue from artistic performance, banquets and other special events should be recognised when events takes place.

5. Tuition Fee:

Revenue should be recognized over the period of instruction.

6. Entrance and Membership Fees:

Revenue recognition from entrance and membership fees depends upon the nature of service being provided. However, entrance fees are generally capitalised. Membership fees should be recognised on systematic and rational basis having regard to timing and nature of service provided.

7. Revenue from Interest:

Revenue from interest should be recognised on time proportion basis.

8. Revenue from Royalties:

Revenue from royalties is recognised on accrual basis as per terms of agreement.

9. Revenue from Dividend:

Revenues from dividend is recognised when the declaring company declared dividend.

EFFECT OF UNCERTAINTIES (SUBSEQUENT UNCERTAINTY IN COLLECTION)

When uncertainty of collection of revenue arises subsequently after the revenue recognition, it is desirable to make provision for the uncertainty in collection rather than adjustment in already recognised revenue.

DISCLOSURE

1. When revenue recognition is postponed, the disclosure of the circumstances necessitating such postponement should be made.

2. Disclosure of Revenue from Sales Transactions (ASI-14):

(i) Disclosure of Excise Duty in presentation of Profit & Loss Statement:

As per ASI-14, the manner of disclosure of excise duty in the presentation of revenue from sales transactions (turnover) in the statement of profit and loss should be as given below:

	Turnover (Gross)	xx
Less:	Excise Duty	xx
	Turnover (Net)	xx

(ii) Guidance Note on Revenue Recognition in Real Estate Sale:

The term 'Real Estate' is meant by land as well as building. The issue is when should the revenue be recognised in case of real estate sales by the enterprises engaged in such activities (commonly referred to as 'real estate developers', 'builders' or 'property developers'.

As regards to real estate, Revenue should be recognised when all the following conditions are fulfilled:

- The seller has transferred to the buyer all significant risk and reward of ownership and the seller retain no effective control of the real estate transferred to a degree usually associated with ownership.
- At the time of transfer of all significant risks and rewards of ownership it is not unreasonable to expect ultimate collection.
- No significant uncertainty exists regarding the amount of the consideration that will be derived.

Once the seller has transferred all risks and rewards of ownership to the buyer and other conditions for recognition of revenue is satisfied, any further act in real estate performed by the seller are in substance, performed on behalf of the buyer in the manner similar to a contractor. Therefore, if the seller is obliged to perform any substantial acts after the transfer of significant risks and rewards of ownership, revenue is recognised by applying the percentage of completion method in manner as specified in AS-7, 'Construction Contract'.

Export-related Benefits such as DEPB:

DEPB denotes Duty Entitlement Passbook. The objective of DEPB is to neutralise the incidence of basic custom duty on the import content of the export products. The neutralisation is provided by way of grant of credit against the export product.

In this regard, a recent ICAI opinion, the benefit of DEPB should be recognised in the year of export itself (provided no uncertainty exists). This is based on the matching concept. The activity of export results in an entitlement of DEPB credit and accordingly, this credit cannot be related to duty payable at the time of subsequent imports. At the time of subsequent imports, the full duty payable on such imports would form part of cost of purchase, which is paid partly, or fully by way of adjustment of DEPB credit. The export benefits should be booked separately as revenue by creating claim against it on the asset side. Accordingly, the cost of purchase of material subsequent to exports should be valued at full cost including the import duty saved i.e. full custom duty should be loaded irrespective of its payment in cash or payment by utilization of DEPB credit. If DEPB credit is held for sale, the treatment of DEPB credit would be similar to the treatment when it is intended to be utilised for imports. However, significant uncertainty as regards to the amount of consideration realisable and uncertainty regarding its ultimate collection has to be taken into account.

Treatment of Inter-divisional Transfers:

ICAI has announced that inter-divisional transfers/sales are not the revenue as per Accounting Standard-9 ‘Revenue Recognition’.

Since in case of inter-divisional transfers, risks and rewards remain within the enterprise and as there is no consideration from the point of view of the enterprise as a whole, the recognition criteria for revenue recognition are also not fulfilled in regard to inter-divisional transfers.

1. Illustration:

Goods worth ₹ 10 lakhs are sent to Amritlal & Co. Ltd. by Sudhir & Co. Ltd. as per their order. Goods are delivered to them and communicated by Amritlal that goods are in order.

Comment on whether it should be recognised as revenue.

Solution:

Yes, it should be recognised as revenue as it fulfilled all the conditions of sale of goods, which is complete in this respect. Against this sale, the amount of the sale is receivable. Hence, as per AS-9, it should be recognized as revenue.

Exercise:

Neelkanth Publishers Co. Ltd., supplied the books of ₹ 5 lakhs to Narendra Book Stores Ltd., as per their order. Narendra Book Stores intimated to Neelkanth Publishers Co. Ltd. that the books are in order.

Comment on whether it should be recognised as revenue.

2. Illustration:

Computers worth ₹ 5 lakhs are supplied to Maganlal & Co. Ltd. by Chhaganlal & Co. Ltd on sale on approval basis.

Mention what AS-9 suggests in this respect. Should it be recognised as revenue?

Solution:

As per AS-9, revenue should be recognised for sale on approval basis when the buyer confirms his desire to buy such goods by communication. In this, there is no communication from Maganalal & Co. Ltd. who are the buyers about their desire to buy the computers. Hence, no revenue should be recognised in this case. It will be recognised as revenue only after receipt of communication from Maganlal & Co. Ltd. indicating that they want to buy the computers, which were sent on sale on approval basis.

Exercise:

Goods of ₹ 2 lakhs are sent to Abhijit & Co. for sale on approval.

Comment on whether revenue should be recognised and state answer as per AS-9.

3. Illustration:

Goods of ₹ 300 are sent to Gambhir as advertising samples.

Comment on whether it should be recognised as Revenue as per AS-9.

Solution:

In this case refer solution to Illustration 1. No consideration is involved. Although goods are sent to Gambhir, they are sent as advertising samples free of charge for advertising purpose. Hence, there is no consideration in this case. Therefore, as per AS-9, no revenue can be recognised in this case.

Exercise:

Goods of ₹ 500 are sent to Abhay as advertising samples.

Comment as to whether it will be recognised as Revenue as per AS-9.

4. Illustration:

Abhay solds some goods to Abhijit without any consideration although goods are sent to Abhijit.

Offer your comment in this case on Revenue Recognition as per AS-9.

Solution:

In this case, revenue will not be recognised. As per AS-9, it is clear that for revenue recognition the following conditions should be fulfilled:

(i) The seller has transferred the ownership of goods to buyer for price or All significant risks and rewards of ownership have been transferred to buyer.

(ii) The seller does not retain any effective control of ownership of the transferred goods.

(iii) There is no significant uncertainty in collection of the amount of consideration. (i.e. cash, receivables etc.)

In the above case, there is no consideration, hence there is no sale, hence revenue should not be recognised.

Exercise:

Sanjay sells goods to Ajay without any consideration although goods are sent to Ajay.

Comment in this case on Revenue Recognition as per AS-9.

5. Illustration:

Jai & Co. Ltd. have an order for ₹ 1 crore from Jayashree & Co. Ltd. Jai & Co. Ltd. have yet to execute the order.

Will this be recognised as revenue? What do the AS-9 suggest in this regard? What are the condition to be fulfilled for revenue recognition

Solution:

It is mere receipt of an order and hence it is not a transaction of sale. The order is not even executed. Hence, no revenue can be recognised in this regard as per AS-9. The conditions to be fulfilled for sale of goods to be recognised as revenue are given under solution to Illustration 1.

Exercise:

We have an order for ₹ 1 lakh from XYZ Co. Ltd. We have yet to execute the order.

Will this be recognised as revenue? What do the AS-9 suggest in this regard? What are the conditions to be fulfilled for revenue recognition?

6. Illustration:

The Madanlal and Co. Ltd. have purchased the goods worth ₹ 5 crores. They have taken the title and accepted the billing from Tejas & Co. Ltd. But goods are not delivered to Madanlal and Co. Ltd. at their request.

In such a case, will the revenue be recognised? Comment with reference to AS-9.

Solution:

Yes, in this case, the revenue from the sale will be recognised since all the conditions of revenue recognition from the sale of goods are fulfilled. Hence, the sale is complete although goods are not delivered to Madanlal & Co. Ltd. at their request. Therefore, as per AS-9, revenue recognition is correct.

Exercise:

The Amritlal & Co. has purchased the goods worth ₹ 5 lakhs. The company has taken the title and accepted billing from us. But goods are not delivered to Amritlal by us.

In such a case, will the revenue be recognised? Comment with reference to AS-9.

7. Illustration:

Indu Ltd. used certain resources of Priyanka Ltd. In return, Priyanka Ltd. received ₹ 25,00,000 and ₹ 30,00,000 as interest and royalties respectively from Indu Ltd. during the year 2015-16.

State whether and on what basis, the revenue can be recognised by Priyanka Ltd.

Solution:

As per AS-9, revenue arising from use. By other company resources yielding interest and royalties should be recognised only when no significant uncertainty exists.

Interest is recognised on time proportion basis and royalty is recognised on accrual basis. Interest is recognised in the year to which it pertains. It is not clear as to which year it belongs. Same is the case with royalty. If both pertains to 2006-07, it should be recognised during this year only.

Exercise:

S & Co. used certain resources of P & Co. In return, P & Co. received ₹ 30,00,000 and ₹ 40,00,000 as interest and royalty respectively from S & Co. during the year 2015-16.

On what basis, the revenue can be recognised by P & Co.

8. Illustration:

XYZ Ltd. has recognised ₹ 6,00,000 on accrual basis income from dividend on securities and units of mutual funds of the face value of ₹ 60 lakhs held by it as at the end of the year ending 31st March, 2016. The dividends were declared at the rate of 10% on 15th June, 2016. The dividend was proposed on 10th April, 2016 by the declaring company.

Comment.

Solution:

The treatment is not as per AS-9. Dividend is recognised as income when the right to receive is established. In this case, right to receive is established on 15th June, 2015. Hence, dividend income should be recognised during the year 2015-16.

Exercise:

Rajita Ltd. has recognised ₹ 12,50,000 on accrual basis income from dividend on shares of the face value of ₹ 50,00,000 held by the company at the end of the year ending 31st March, 2016. The dividends were declared at the rate of 25% on 1st July, 2010. The dividend was proposed on 15th May, 2016 by the company.

Is this treatment right as per AS-9?

9. Illustration:

The directors of Rajashree Ltd. decided on 31st March, 2016 to increase the sale price of certain items retrospectively from 1st January, 2016. In view of the revision of price, the company has to receive ₹ 20 lakhs from its customers in respect of sales made from 1st January, 2016 to 31st March, 2016 and the accountant being inexperienced, cannot decide whether ₹20 lakhs due to price revision is revenue in the sale for 2015-16.

Give your suggestions.

Solution:

The company stands to receive ₹ 20 lakhs due to price revision. If there is a certainty about collection, the revenue arising from price revision should be recognised in 2015-16.

Exercise:

The directors of Monica Ltd. decided on 31st March, 2016 to increase the sale price of its products by 10% on sales taking place from 30th June, 2015 onwards. The intimation regarding the same was sent to all the customers by 15th June, 2015.

From which date, should the revenue pertaining to increase in sale price by 10% be recognised.

[**Hint:** Revenue will be recognised from 2015-16 provided there is a certainty that customers will accept the decision of the directors.]

10. Illustration:

Installation fees of ₹ 5,00,000 are recognised as revenue by a company when the installation is completed at the buyer's place and goods are inspected and accepted by the buyer.

Comment on whether it is correct as per AS-9.

Solution:

Revenue recognition in this respect is correct as the sale of services is complete as per AS-9.

Exercise:

Installation fees of ₹ 1 lakh are recognised as revenue when the installation is completed.

Comment as per AS-9.

11. Illustration:

Pfizer Ltd. 2002-03:

Revenue Recognition: Revenue from sale of goods is recognised when significant risks and rewards of ownership are transferred to the customers, which is at the point of dispatch of goods to the customers. Revenue from services is recognised on rendering of services. Interest income is recognised on time proportion basis.

12. Illustration:

Ceat Ltd. 2002-03:

Sales are recognised on despatch to customers. Sales include excise duty but exclude sales tax and freight recovery. Export incentives, Dividend and interest are accounted for on an accrual basis.

13. Illustration:

Nicholas Piramal India Ltd. 2002-03:

The Company recognizes sales at the point of dispatch of goods to the customer. Sales are net of discounts, sales tax, excise duty and returns.

14. Illustration:

P C I Papers Ltd. 2002-03:

Revenue Recognition: Sales include exports sales, domestic sales, inter-division transfer, conversion income and net of returns, claims and discount allowed.

Domestic sales includes excise duty realised but net of sales tax.

Export sales includes the foreign exchange rate difference arising upon subsequent realisation of invoices.

Benefits on account of entitlement of import duty free materials under the '**Duty Exemption Passbook Scheme**' is accounted for in the year of export.

15. Illustration:

Dr. Reddy's Laboratories Ltd. 2015-16:

Revenue Recognition: Revenue from sale of goods is recognised when significant risks and rewards in respect of ownership of the products are transferred to the customer. Revenue from domestic sales of formulation products is recognised on despatch of products to stockists by clearing and forwarding agents of the Company. Revenue from domestic sales of active pharmaceutical ingredients and intermediates is recognised on dispatch of products from the factories of the Company. Revenue from export sales is recognised on shipment of products.

Revenue from product sales is stated inclusive of excise duty and exclusive of returns, sales tax and applicable trade discounts and allowances.

Revenue from services is recognised as per the terms of the contracts with the customers when the services are performed.

Non-refundable upfront and milestone payments ("license fees") are recognised as revenue when earned, in accordance with the terms prescribed in the license agreements.

Dividend income is recognised when the unconditional right to receive the income is established. Income from interest on deposits and interest bearing securities is recognised on the time proportionate method.

Export entitlements under the Duty Entitlement Passbook ("DEPB") scheme are recognised in the profit and loss account when the right to receive credit as per the terms of the scheme is established in respect of the exports made and where there is no significant uncertainty regarding the ultimate collection of the relevant export proceeds.

STOCK VALUATION AND VALUATION OF INVENTORY

DEFINITION

An inventory valuation allows a company to provide a monetary value for items that make up their inventory. Inventories are usually the largest current asset of a business, and proper measurement of them is necessary to assure accurate financial statements. If inventory is not properly measured, expenses and revenues cannot be properly matched and a company could make poor business decisions.

OBJECTIVE

A primary issue in accounting for inventories is the determination of the value at which inventories are carried in the financial statements until the related revenues are recognised. This Statement deals with the determination of such value, including the ascertainment of cost of inventories and any write-down thereof to net realisable value.

Scope of Accounting Standard 2

1. This Statement should be applied in accounting for inventories other than:
   - (a) Work in progress arising under construction contracts, including directly related service contracts (see Accounting Standard (AS) 7, Accounting for Construction Contracts 3);
   - (b) Work in progress arising in the ordinary course of business of service providers;
   - (c) Shares, debentures and other financial instruments held as stock-in-trade; and
   - (d) Producers' inventories of livestock, agricultural and forest products, and mineral oils, ores and gases to the extent that they are measured at net realisable value in accordance with well established practices in those industries.

2. The inventories referred to in paragraph 1 (d) are measured at net realisable value at certain stages of production. This occurs, for example, when agricultural crops have been harvested or mineral oils, ores and gases have been extracted and sale is assured under a forward contract or a government guarantee, or when a homogeneous market exists and there is a negligible risk of failure to sell. These inventories are excluded from the scope of this statement.

   Variable costs are expenses that change in proportion to the activity of a business. Variable cost is the sum of marginal costs over all units produced. It can also be considered normal costs. Fixed costs and variable costs make up the two components of total cost. Direct Costs, however, are costs that can easily be associated with a particular cost object. However, not all variable costs are direct costs. For example, variable manufacturing overhead costs are variable costs that are indirect costs, not direct costs. Variable costs are sometimes called unit-level costs as they vary with the number of units produced.

Definitions

3. The following terms are used in this Statement with the meanings specified:

   Inventories are assets:

   (a) Held for sale in the ordinary course of business;

   (b) In the process of production for such sale; or

   (c) In the form of materials or supplies to be consumed in the production process or in the rendering of services.

   Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

4. Inventories encompass goods purchased and held for resale, for example, merchandise purchased by a retailer and held for resale, computer software held for resale, or land and other property held for resale. Inventories also encompass finished goods produced, or work in progress being produced, by the enterprise and include materials, maintenance supplies, consumables and loose tools awaiting use in the production process. Inventories do not include machinery spares which can be used only in connection with an item of fixed asset and whose use is expected to be irregular; such machinery spares are accounted for in accordance with Accounting Standard (AS) 10, Accounting for Fixed Assets.

Measurement of Inventories

5. Inventories should be valued at the lower of cost and net realisable value.

   Cost of Inventories

6. The cost of inventories should comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Costs of Purchase

7. The costs of purchase consist of the purchase price including duties and taxes (other than those subsequently recoverable by the enterprise from the taxing authorities), freight inwards

and other expenditure directly attributable to the acquisition. Trade discounts, rebates, duty drawbacks and other similar items are deducted in determining the costs of purchase.

Costs of Conversion

8. The costs of conversion of inventories include costs directly related to the units of production, such as direct labour. They also include a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods. Fixed production overheads are those indirect costs of production that remain relatively constant regardless of the volume of production, such as depreciation and maintenance of factory buildings and the cost of factory management and administration. Variable production overheads are those indirect costs of production that vary directly, or nearly directly, with the volume of production, such as indirect materials and indirect labour.
9. The allocation of fixed production overheads for the purpose of their inclusion in the costs of conversion is based on the normal capacity of the production facilities. Normal capacity is the production expected to be achieved on an average over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance. The actual level of production may be used if it approximates normal capacity. The amount of fixed production overheads allocated to each unit of production is not increased as a consequence of low production or idle plant. Unallocated overheads are recognised as an expense in the period in which they are incurred. In periods of abnormally high production, the amount of fixed production overheads allocated to each unit of production is decreased so that inventories are not measured above cost. Variable production overheads are assigned to each unit of production on the basis of the actual use of the production facilities.
10. A production process may result in more than one product being produced simultaneously. This is the case, for example, when joint products are produced or when there is a main product and a by-product. When the costs of conversion of each product are not separately identifiable, they are allocated between the products on a rational and consistent basis. The allocation may be based, for example, on the relative sales value of each product either at the stage in the production process when the products become separately identifiable, or at the completion of production. Most by-products as well as scrap or waste materials, by their nature, are immaterial. When this is the case, they are often measured at net realisable value and this value is deducted from the cost of the main product. As a result, the carrying amount of the main product is not materially different from its cost.

VALUATION OF INVENTORIES – AS-2

1. Introduction

1. Accounting Standard 2–(AS-2) issued by the Institute of Chartered Accountants of India (ICAI) deals with method of accounting for valuation of inventories. This standard was originally introduced by the ICAI in 1981; however it became mandatory only from 1.4.1999.
2. Basically, the main objective of having an accounting standard is to achieve 'Comparability,' i.e., enabling comparison of operating results of two years of the same entity or comparing the operating results of different entities of the same industry.

3. The wealth and future of the business is based on the inventory and its valuation. It is one of the most important items stated on Assets side of the Balance Sheet and plays an important role in determining the operational and financial results.
4. Generally it is the second largest item after fixed assets in the financial statements of a manufacturing organisation. The value attached to inventories can materially affect the operating result and financial position. However different bases of valuing inventories are used by different business and even by different undertakings within the same industry.
5. The statement applies to financial statements prepared on Historical Cost basis. Different considerations would be involved for statement prepared on other basis.
6. The inventory is the main item which can convert profit making unit into loss making and vice-versa. As per AS-1, i.e. Disclosure of Accounting Policies and disclosure of true and fair view, Inventory Valuation plays very important role.
7. As provided in the Companies Act 1956 Part I & II of Schedule VI and MAOCARO and now Companies (Auditor's Report) order 2003 issued by Central Government of India *w.e.f.* 1.4.2004, Inventory Valuation shown as per AS 2 gives better disclosure, reliability and comparability.

2. Objective of AS-2

1. The determination of the value at which inventories are carried in the financial statements until the related revenues are recognised, including the ascertainment of cost of inventories.
2. However, there will be on impact on 'Profit' or taxable income and Current Assets for disclosure of true and fair view of financial position and working results under companies act 1956.
3. The mandatory AS-2 is also applicable in respect of financial statements audited under section 44AB of the Income Tax Act, 1961.

3. Coverage

1. The standard lays down the coverage and valuation of inventories
2. Inventories encompass goods purchased and held for resale it can be raw material, finished goods or work in progress and stores and spares, Packing Material etc.

Definitions

The standard defines and stipulates the following factors to be considered for inventories are assets:

Held for sale in the ordinary course of business; In the process of production for such sale; or In the form of materials or supplies to be consumed in the production process or in the rendering of services.

Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

3. The cost of inventories should comprise all cost of purchase, cost of conversion & other cost incurred in bringing the inventories to that present location and condition.
4. It must be noted and clarified that AS-2 does not apply to.

Work-in Progress in Construction Contracts-AS-7

Work-in progress in case of service provides.

Inventory of live stock agricultural and forest products, mineral oils, ores and gases as specified in paras 1(d) of As-2.

Not includes machinery spare dedicated to a particular machinery or equipment and use of the spare is irregular.

Shares, debentures and financial instruments held as stock-in trade.

Question arises as to how the inventory of shares, debentures and financial assets held as stock-in trade should be valued as AS-2 which mandates lower of cost or net realisable value method of valuation is not applicable and the method of valuation prescribed by AS-13 dealing with investments to be lower of cost and fair value is also not applicable. Prudence requires the basis of valuation to be lower of cost of purchase. Cost of purchase in this case would be cost of the security plus brokerage and transfer charges.

AS 13 also deals with "current" or short term investments this would be applicable to inventory of shares and securities.

5. Paras 12 and 13 of AS-2 prescribe as to what is excluded whilst computing COST. These are: Abnormal wastage of labour and materials. Storage costs, unless those costs are necessary in the production process prior to further production. Administrative overheads that do not contribute to bringing inventories to their present location and condition. Selling and distribution costs. Interest and other borrowing Costs. Trade discounts and rebates, duty drawbacks.
6. Inclusion of Excise duty in inventory valuation.

The cost of purchase consists of the purchase price including duties & taxes (other than those subsequently recoverable by the enterprise from the taxing authorities)

As per the Guidance Note issued by the institute of Chartered Accountants of India, the excise duty is a cost incurred to bring the inventories to their present location and condition and accordingly it is required to be considered as an element of cost for inventory valuation.

7. In this connection MODVAT (now CENVAT) will not form part of cost of purchase.
8. Increase or decrease of exchange rate variation will be part of cost of inventories.
9. It must be noted that the Expert committee of the Institute of has consistently opined that interest cannot form of cost of inventories even if production or conversion of an item of inventory takes a long time.

However, interest can be part of cost of inventories which take long period of time to get completed before the inventory is ready for sale, e.g., wine, timber etc.

Inventory Accounting Systems: The two most widely used inventory accounting systems are the periodic and the perpetual.

- **Perpetual:** The perpetual inventory system requires accounting records to show the amount of inventory on hand at all times. It maintains a separate account in the subsidiary ledger for each good in stock, and the account is updated each time a quantity is added or taken out.
- **Periodic:** In the periodic inventory system, sales are recorded as they occur but the inventory is not updated. A physical inventory must be taken at the end of the year to determine the cost of goods sold. Regardless of what inventory accounting system is used, it is good practice to perform a physical inventory at least once a year.

Periodic Versus Perpetual Systems

There are fundamental differences for accounting and reporting merchandise inventory transactions under the periodic and perpetual inventory systems.

To record purchases, the periodic system debits the Purchases account while the perpetual system debits the Merchandise Inventory account.

To record sales, the perpetual system requires an extra entry to debit the Cost of goods sold and credit Merchandise Inventory.

By recording the cost of goods sold for each sale, the perpetual inventory system alleviated the need for adjusting entries and calculation of the goods sold at the end of a financial period, both of which the periodic inventory system requires.

In Perpetual Inventory System there must be actual figures and facts.

Using Non-cost Methods to Value Inventory: Under certain circumstances, valuation of inventory based on cost is impractical. If the market price of a good drops below the purchase price, the lower of cost or market method of valuation is recommended. This method allows declines in inventory value to be offset against income of the period. When goods are damaged or obsolete, and can only be sold for below purchase prices, they should be recorded at net realizable value. The net realizable value is the estimated selling price less any expense incurred to dispose of the good.

Methods Used to Estimate Inventory Cost: In certain business operations, taking a physical inventory is impossible or impractical. In such a situation, it is necessary to estimate the inventory cost.

Two very popular methods are (1) retail inventory method, and (2) gross profit (or gross margin) method. The retail inventory method uses a cost to retail price ratio. The physical inventory is valued at retail, and it is multiplied by the cost ratio (or percentage) to determine the estimated cost of the ending inventory.

The gross profit method uses the previous year's average gross profit margin (i.e., sales minus cost of goods sold divided by sales). Current year gross profit is estimated by multiplying current year sales by that gross profit margin, the current year cost of goods sold is estimated by subtracting the gross profit from sales, and the ending inventory is estimated by adding cost of goods sold to goods available for sale.

Inventory Costing Methods: Recall that a perpetual inventory system means the inventory accounts are adjusted after each sale or purchase transaction. Under FIFO, the cost of the goods that were acquired by the company first, is transferred from Inventory to Cost of Goods sold upon a sale. In other words, when a sale takes place, the cost of units from the earliest inventory layer is expensed first. If there are not enough units in the first layer, the unit cost from the next layer is expensed and so on like that.

First In First Out (FIFO) - Definition and Explanation

The **First In First Out (FIFO) Method** of costing is used to introduce the subject of **Materials Costing**. The FIFO method of costing issued materials follows the principle that materials used should carry the actual experienced cost of the specific units used. The method assumes that materials are issued from the **Oldest Supply** in stock and that the cost of those units when placed in stock is the cost of those same units when issued. However, FIFO costing may be used even though physical withdrawal is in a different order.

Advantages of First In First Out (FIFO) Costing Method:

Advantages Claimed for First In First Out (FIFO) Costing method are:

1. Materials used are drawn from the cost record in a logical and systematic manner.
2. Movement of materials in a continuous, orderly, single file manner represents a condition necessary to and consistent with efficient materials control, particularly for materials subject to deterioration, decay and quality are style changes.

FIFO Method is Recommended Whenever:

1. The size and cost of units are large.
2. Materials are easily identified as belonging to a particular purchased lot.
3. Not more than two or three different receipts of the materials are on a materials card at one time.

Illutration: 1

Brid's Drills Co. has Following Transaction in the Month of February 2016

	February 2016
(1)	Beginning balance: 800 units @ ₹ 6 per unit.
(4)	Received 200 units @ ₹ 7 per unit.
(10)	Received 200 units @ ₹ 8 per unit.
(11)	Issued 800 units.
(12)	Received 400 units @ ₹ 8 per unit.
(20)	Issued 500 units.
(25)	Returned 100 excess units from the factory to the storeroom to be recorded at the latest issued price.
(28)	Received 600 units @ ₹ 9 per unit.

Calculation for the Above Transactions would be as Follows
FIFO Method

February:			
01. Beginning balance	800 units @ ₹ 6	₹ 4,800	
04. Received	200 units @ ₹ 7	₹ 1,400	
10. Received	200 units @ ₹ 8	₹ 1,600	₹ 7,800
11. Issued	800 units @ ₹ 6		₹ 4,800
Balance	**200 units @ ₹ 7**	**₹ 1,400**	
	200 units @ ₹ 8	**₹ 1,600**	**₹ 3,000**
12. Received	400 units @ ₹ 8	₹ 3,200	₹ 6,200
20. Issued	200 units @ ₹ 7	₹ 1,400	
300 units @ ₹ 8	₹ 2,400	₹ 3,800	
Balance	**300 units @ ₹ 8**	**₹ 2,400**	
25. Returned to storeroom	100 units @ ₹ 8	₹ 800	
28. Received	600 units @ ₹ 9	₹ 5,400	8,600
Balance	**400 units @ ₹ 8**	**₹ 3,200**	
	600 units @ ₹ 9	**₹ 5,400**	**₹ 8,600**

Disadvantages or Limitations of FIFO Method

FIFO Method is definitely awkward if frequent purchases are made at different prices and if units from several purchases are on hand at the same time. Added costing difficulties arise when returns to vendors or to the storeroom occur.

Weighted Average Method: This method assumes that all inventories available are best represented by a weighted average cost. The average cost of goods held in inventory is recalculated every time a fresh purchase is made and goods issued or sold out of inventory are priced at such average price till such time as the next lot is purchased.

Weighted Average Cost is a method of calculating Ending Inventory cost. It is also known as AVCO. It takes Cost of Goods Available for Sale and divides it by the total amount of goods from Beginning Inventory and Purchases. This gives a Weighted Average Cost per Unit. A physical count is then performed on the ending inventory to determine the amount of goods left. Finally, this amount is multiplied by Weighted Average Cost per Unit to give an estimate of ending inventory cost.

Illustration: 2

The following is the record of receipts of certain material during the month of February 2015:

Feb1. Received 400 units for job no. 12 @ ₹ 10 per unit

Feb 4. Received 300 units for job no.13 @ ₹ 11 per unit

Feb 16. Received 200 units for job no. 14 @ ₹ 12 per unit

Feb 25 Received 400 units for job no. 15 2 ₹ 13 per unit.

During February 2015 following issue of material are made.

Feb 10. Issued 200 units to job no.12

Feb 15 Issued 100 units to job no.13

Feb 17. Issued 200 units to job no. 12

Feb 20. Issued 200 units to job no 14

Feb 26. Issued 100 units to job no. 13

Feb 28. Issued 200 units to job no. 15

Show how these transaction will appear in the stores ledger and state the amount of inventory of Feb. 28, 2015.

Solution

FIFO Method

Receipts						Issues					Balance	
Date	**Job no.**	**Qty**	**Rate**	**Amt**	**Date**	**Job no.**	**Qty**	**Due**	**Rate**	**Amt**	**Qty**	**Amt**
2015					2015							
Feb.1	12	400	10	4,000	Feb.						400	4,000
Feb 4	13	300	11	3,300	Feb.						700	7,300
					Feb.10	12	200	200	10	2,000	500	5,300
					Feb.15	13	100	200	11	1,100	400	4,200
Feb.16	16	200	12	2,400							600	6,600
					Feb.17	12	200		10	2,000	400	4,600
					Feb.20	14	200		12	2,400	200	2,200
Feb.25	15	400	13	5,200							600	7,400
					Feb.26	13	100	100	11	1,100	500	6,300
					Feb.28	15	200	200	13	2,600	300	3,700
Total		**1,300**		**14,900**			**1000**			**11,200**	**300**	**51,600**

Illustration: 3

From the following details calculate value of closing stock on 31-12-2015 according to (a) FIFO Method and (b) weighted average method.

Date	Transaction	No. of units	Rate per unit ₹
1-12-2015	Opening stock	4000	30.00
4-12-2015	Purchased	8000	32.10
8-12-2015	Issued	9000	
12-12-2015	Purchased	7000	32.50

16-12-2015	Issued	6000	
20-12-2015	Purchased	9000	32.30
23-12-2015	Issued	8000	
25-12-2015	Purchased	6000	33.25
27-12-2015	Issued	9000	
29-12-2015	Purchased	10000	32.50
31-12-2015	Issued	7000	32.50

Solution

FIFO Method

Purchases				Issued			Balance		
Date	**Units**	**₹**	**Total**	**Units**	**₹**	**Total**	**Units**	**₹**	**Total**
1.12.15	Opening						4000	30	1,20,000
4.12.15	8000	32.10	2,56,800				4000	30	1,20,000
							8000	32.1	2,56,800
8.12.15				4000	30	12,0,000			
				5000	32.1	1,60,500	3000	32.1	96,300
12.12.15	7000	32.5	2,27,500				3000	32.1	96,300
							7000	32.5	2,27,500
16.12.15				3000	32.1	96,300			
				3000	32.5	97,500	4000	32.5	1,30,000
20.12.15	9000	32..3	2,90,700				4000	32.5	1,30,000
							9000	32.3	2,90,700
23.12.15				4000	32.5	1,30,000			
				4000	32.3	1,29,200	5000	32.3	1,61,500
25.12.15	600O	33.25	1,99,500				5000	32.3	1,61,500
							6000	33.25	1,99,500
27.12.15				5000	32.3	1,61,500			
				4000	33.25	1,33,000	2000	33.25	66,500
29.12.15	10000	32.5	3,25,000				2000	33.25	66,500
						10,000	32.5	325000	
31.12.15				2000	33.25	66,500			
				5000	32.5	1,62,500	5000	32.5	1,62,500

The Closing Stock 5000 Units Amount into ₹ 1,62,500

Weighted Average Method

Receipts				Issued			Balance	
Date	Units	₹	Total	Units	₹ cost.avg	Total	Units	Value
1.12.15	Opening						4000	1,20,000
4.12.15	8000	32.1	2,56,800				12000	3,76,800
8.12.15				9000	31.4	2,82,600	3000	94,200
12.12.15	7000	32.5	2,27,500				10000	3,21,700
16.12.15				6000	32.17	1,93,020	4000	1,28,680
20.12.15	9000	3.3	2,90,700				13000	4,19,380
23.12.15				8000	32.26	2,58,080	5000	1,61,300
25.12.15	6000	33.25	1,99,500				11000	3,60,800
27.12.15				9000	32.8	2,95,200	2000	65,600
29.12.15	10000	32.5	3,25,000				12000	3,90,600
31.12.15				7000	32.55	2,27,850	5000	1,62,750

The Closing Stock 5000 Units Amounting To ₹ 1,62,750

Illustration: 4

The following transaction took place in respect of a material

Date	Receipt Quantity (Units)	Rate ₹	Issue Quantity (Units)
02/03/2015	200	2.00	-
10/03/2015	300	2.40	-
15/03/2015	-	-	250
18/03/2015	250	2.60	-
20/03/2015	-	-	300

Prepare a Stock register as per:

Weighted Average Method

(ICWA Adapted)

Solution

Stock Register (Weighted Average Method)

Date	Receipts			Issues			Balance		
	Aty	Rate	Amt	Qty	Rate	Amt	Qty	Rate	Amt
02/03/2015	200	2.00	400	-	-	-	200	2.00	400
10/03/2015	300	2.40	720	-	-	-	500	2.24	1,120
15/03/2015	-	-	-	250	2.24	560	250	2.24	560
18/03/2015	250	2.60	650	-	-	-	500	2.42	1,120
20/03/2015	-	-	-	300	2.42	726	200	2.42	484

Illustration: 5

From the follwing data yiu are required to compile a valued stock card in repect of material 'Mikytoya'for the month of Arpil 2015 and value the closing stock by:

(a) Weighted average method

April 1 Opening stock 100 units @ ₹ 15 per unit

April 4 Received 90 units under GRN No. 301 @ ₹ Per unit

April 7 Issued 80 units under Issue Note No. 501

April 11 Received 200 units under GRN No. 302 @ ₹ 17 per unit

April 14 Issued 150 units under Issue Note No. 502

April 21 Receuved 20 units under GRN No. 303 @ ₹ 25 per unit

April 25 Issued 100 units under Issue Note No. 503

April 27 Received 50 units under GRN No. 304 ₹ 16 per unit

Solution

Stock Card (Weighted Average Method)

Date April	Doc Ref.	Receipts			Issue			Balance		
2015		Qty	Rate	Amt	Qty	Rate	Amt	Qty	Rate	Amt
1								100	15	1,500
4	GRN 301	90	16	1,440				190	15,47	2,940
7	IN 501				80	15,47	1,238	110	15,47	1,702
11	GRN 302	200	17	3,400				310	16.46	5,102
14	IN 502				150	16.46	2,496	160	16.46	2,633

21	GRN 303	20	25	500				180	17.41	3,133
25	IN 503				100	17.41	1,741	80	17.40	1,392
27	GRN 304	50	16	800				130	16.86	2,192
		360		6,140	330		5,448			

Illustration: 6

(MU, DFM, 2001)

Followint date pertains to Raw Material 'Timmy' during the minthe September 2015

01/09/2015 Opening Balance 100kg. @ ₹ 15 per kg.

04/09/2015 GRN 903 90kg.@ ₹ per kg.

07/09/2015 M.R.95 80 kg.

11/09/2015 GRN 908 200kg.@ ₹ 17 per kg.

14/09/2015 M.R. 959 150 kg

20/09/2015 GRN 923 20kg. @ ₹ 25 per kg

24/09/2015 M.R. 963 100kg

29/09/2015 GRN 942 50kg @ ₹ per kg.

From the above details. You are reuired to find out:

(i) Value of total issues under "weighted average" Method

(ii) Quantity and value of closing stock under

  (i) Weighted average

  (ii) FIFO

(iii) Average purcjase price per unit, during the moth.

(iv) 2 kgs of "Timmy" are required to to manufacture 1 unit of "Tommy" and

(v) Other conversion cost per unit of Tommy are ₹ 6 per unit and Company want to earn 30% profit on sales.

What should be selling price per unit of "Tommy"?

Solution

Stock Register (Weighted Average Method)

Date April	Doc Ref.	Receipts			Issue			Balance		
2015		**Qty**	**Rate**	**Amt**	**Qty**	**Rate**	**Amt**	**Qty**	**Rate**	**Amt**
1								100	15.00	1,500
4	GRN 903	90	16	1,440				190	15,47	2,940

7	MR 951				80	15,47	1,238	110	15,47	1,702
11	GRN 908	200	17	3,400				310	16.46	5,102
14	MR959				150	16.46	2,496	160	16.46	2,633
20	GRN923	20	25	500				180	17.41	3,133
24	MR963				100	17.41	1,741	80	17.40	1,740
29	GRN942	50	16	800				130	16.86	2,196
		360		6,140	330		5,448			

(a) Simple Average $= \dfrac{16+17+25+16}{4} =$ ₹ 18.50 per unit

Weighted Average Method $= \dfrac{6140}{360} =$ ₹ 17.06 Per unit

Weighted Average:

Raw Material 2kg. × ₹ 17.06 = 34.11

Other Conversion Costs = 6,00

Total Cost = 40.11

(+) Profit (30 on Sales) = 17.19

Selling Price = 57.30

Stock Register (FIFO Methog)

Date April	Doc Ref.	Receipts			Issue			Balance		
2015		Qty	Rate	Amt	Qty	Rate	Amt	Qty	Rate	Amt
1								100	15	1,500
4	GRN 903	90	16	1,440				100	15	1,500
								90	16	1,440
								190		2,940
7	MR 951				80	15,47	1,238	20	15	300
								90	16	1,440
								110		1,740
11	GRN 908	200	17	3,400				20	15	300
								90	16	1,440
								200	17	3,400
								310		5,140
14	MR959				20	15.00	300			
					90	16.00	1,440	160	17	2,720

					40 150	17.00	680 2,420			
20	GRN923	20	25	500				160 20 180	17 25	2,720 500 3,220
24	MR963				100	17.41	1,741	60 20 80	17 25	1,020 500 1,520
29	GRN942	50	16	800				60 20 50 130	17 25 16	1,020 500 800 2,320
		360		6,140	330		5,448			

(b) Input 2 Kgs Output 1 Unit

Simple Average ₹ Per Unit Calculation

Raw Material 2kg. x ₹ 18.50	= 37.00	
Other Conversion Costs	= 6.00	
Total Cost	= 43.00	70
(+) Profit (30 on Sales	= 18.43)	30
Selling Price	= 61.43	100

Illustration: 7

Calculate the value of closing stock, cost sales according to FIFO and Weighted Average Method as on 31st March, 2016 using Periodic Inventory System.

March 1, 2016 Stock 5,000 units @ ₹ 8 per unit
March 7, 2016 Purchased 7,500 units @ ₹ 10 per unit
March 12, 2016 Purchased 8,500 units @ ₹ 12 per unit
March 21, 2016 Purchased 9,000 units @ ₹ 15 per unit
March 28, 2016 Purchased 12,000 units @ ₹ 11 per unit

The physical stock-taking competed on 31st March, 2016 revealed a closing stock of 3,500 units.

Assuming that sale price is @ ₹ 15 per unit, calculate the gross profit.

(B. Com., Delhi – Adapted)

Solution

Total cost of goods available for sale	
	= (5,000 x 8) + (7,500 x 10) + (8,500 x 12) + (9,000 x 15) + (12,000 x 11)
	= ₹ 4,84,000
Total No. of units	= 5,000 + 7,500 + 8,5000 + 9,000 + 12,000
	= 42,000 units
Stock (in units)	= 3,500 units
No. of units sold	= 42,000 – 3,500
	= 38,500 units
Sales	= 38,500 x 15
	= ₹ 5,77,500

Cost of Goods Sold, Stock and Gross Profit:

FIFO:

Closing Stock	= 3,500 x 11
	= ₹ 38,500
Cost of Goods sold	= Total Cost x Closing Stock
	= 4,84,000 – 38,500
	= ₹ 4,45,500
Gross Profit	= Sales – Cost of Goods Sold
	= 5,77,500 – 4,45,500
	= ₹ 1,32,000

Weighted Average:

$$\text{Weighted Average Cost Per unit} = \frac{\text{Total Cost}}{\text{Total Units}}$$

$$= \frac{4,84,000}{42,000}$$

= 11.52

Closing Stock	= 3,500 x 11.52
	= ₹ 40,320
Cost of goods sold	= 4,84,000 – 40,320
	= ₹ 4,43,680
Gross Profit	= 5,77,500 – 4,43,680
	= ₹ 1,33,820

Valuation of Stock on the Date of Final Accounts (Stock Reconciliation)

Under Perpetual System, value of stock can be determined easily on the basis of stock record. But under periodic system, it becomes necessary to take the stock on the date of Balance Sheet. In practices, it is not possible to take stock on the date of Balance Sheet. There are two option available to a firm:

1. To suspend business activities entirely and do stock taking. In this case the stock on date of balance sheet and physical stock taking will be the same.
2. To continue business activities and estimate the stock on the date of the balance Sheet by making adjustment regarding purchases, cost of goods sold, cost of return etc. during the inventory period. The effect of various transactions on flow of goods during the specific period is considered to decide the stock. While estimating the stock on the date of Balance Sheet it must be remembered that physical stock is the cost of goods in possession on that date. But the stock on the date of balance sheet is to be determined on the basis of Ownership of goods and not the possession of goods. Ownership is the sole criteria to decide whether a particular item is to be included or excluded. Hence, goods in transit, sale of goods on approval, branch stock, stock on consignment are included on the basis of ownership though the possession of goods not with the trader on the date of valuation.

Transfer of ownership may be decided on any one of the following bases:

1. Invoice Basis:

Purchase and sale is assumed to be completed on the date of invoice. Hence, date of invoice is important

2. Delivery Basis:

Transfer of ownership is assumed to take place on the date of delivery of goods

(i) If Stock is Taken Prior to the Date of Balance Sheet

		₹	₹
Value of stock on the date of stock taking			xx
Add:	Purchases during the period	xx	
Add:	Cost of Sales Returns during the period	xx	
Add:	Cost of Stock on Consignment with consignee, Stock with customers on sale or Return basis, Stock with branches.	xx	xx
Less:	Cost of sales during the period	xx	
Less:	Purchase returns during the period	xx	xx
Value of Stock on the Balance Sheet date			xx

Notes:

1. Sales should include normal sales only.
2. Exclude from sales goods on sale or return basis or hire purchase basis.

3. Deduct normal profit from sales to arrive at cost of goods sold.
4. Cost of goods sold should be ascertained separately when the goods are sold at a loss or at abnormal profit.

Illustration: 8

Determine the value of stock to be taken for Balance Sheet as at 31st March,2016 from the following information:

The stock was physically verified on 23rd March 2016 and was valued at 6,00,000. Between 23rd March, 2016 and 31st March, 2016; the following transaction had taken place:

1. Purchase ₹ 50,000 of this goods worth ₹ 20,000 were delivered on 5th April, 2016.
2. Out of goods sent on consignment, goods worth ₹ 30,000 (at cost) were unsold.

Solution

Statement Showing the Value of Stock on 31.03.2016

Particulars	₹	₹
Stock on 23rd March, 2016		
Add: Purchases during 23rd and 31st March		
(₹ 30,000 + 20,000 in transit)	50,000	
Add: Goods lying with consignee at cost	30,000	
(₹ 20,000 – ₹ 4,000)	16,000	96,000
		6,96.000
Less: Cost of goods sold during		
23rd March and 31st March (Note 1)	1,08,000	
Less: Cost of Abnormal Sales	30,000	1,38,000
Value of stock on 31st March, 2016		5,58,000

Working Notes:

1. Cost of goods sold during 23rd March, and 31st March, 2016:

	₹	₹
Sales		1,70,000
Less: Sales of abnormal items	15,000	
Less: Sent on approval	20,000	35,000
		1,35,000
Less: Gross Profit @ 25% of cost i.e, 20% on sale		27,000
		1,08,000

Illustration: 9

Mr. Mukesh's financial year ends on 30th June 2016 but the actual physical stock is not taken until the following 8th July 2016 when it is ascertained at ₹ 7,425. You find that.

1. Sales are entered in the sale day book on the 'day' of dispatch and returns inwards in return inward book are received back.
2. Purchases are entered in purchases book as the invoice are received.
3. Sale between 1-8 July as per sales book and cash book are ₹ 8,600.
4. Purchases between 1-8 July as per purchases book are ₹ 660 but out of these goods amounting to ₹ 60 are not received till 8th July.
5. Goods purchases and invoiced before 30th June amounted to ₹ 500 out of which ₹ 350 worth of goods are received between 1-8 July and remaining goods after 8th July. Find of the value of stock as at 30th June, 2016 assuming that rate of profit is 1/3 on cost.

(B.Com., Delhi and CA - Adapted)

Solution

Statement Showing the Value of Stock on 30.6.2016

	₹
Physical Stock on 8.7.2016	7,425
Add: Cost of goods sold during the period [8,600 – ¼ of ₹ 8,600]	6,450
	13.875
Less: Goods purchased and received during the period (660 – 60)	600
	13.275
Add: Goods invoiced before 30th June but not included in physical Stock* (500 – 350)	150
Value of Stock on 30.6.2016	**13.425**

*Because purchases are recorded on the basis of date of invoice.

(ii) If Stock is Taken After the Date of Balance Sheet

The above format should be followed. The items added should be deducted and the items deducted should be added.

Statement Showing the Value of Stock on

	₹	₹
Stock on the later date		
Add: Sales during the period (at cost)		xx
Add: Purchases Returns during the said period	xx	
Add: Undercasting in Stock Sheet	xx	

Add: Goods in transit	xx	
Less: Purchases during the period	xx	xx
Less: Sales Return at cost during the period	xx	
Less: Overcasting in Stock Sheet	xx	
Less: Goods held on consignment basis	xx	xx
Stock on the date of Balance Sheet		xx

Illustration: 10

TY Ltd. Conducts physical stock taking every every year at the end of the accounting year. Qwing to certain difficulties, it was not possible for it to conduct physical stock taking at the end of the accounting year ending 30th June, 2016. Physical stock was taken on 8th July, 2016 when it was valued at ₹ 34,000.

The following transaction took place during 1st July to 8th July, 2016.

1. Net sales during the period were ₹ 9,340. These goods were sold at the usual rate of gross profit of 25% on cost except goods, which realize ₹ 840 on the basis of 20% profit on cost.
2. Purchases during the period were ₹ 7,500 of which ₹ 800 worth of goods were delivered to the company only on 10th July, 2016.
3. Sales returns during the period were ₹ 1,500 of which 50% were out of the sales at 20% gross profi mentioned above.
4. On 5th July, 2016 goods worth ₹ 5,000 were received, which were to be sold on consignment basis.

You are required to prepare a statement showing clearly the value of the stock to be taken into account in TY Ltd.' Final accounts for the year ended 30th June, 2016.

(CA Ended – Adapted)

Solution

Statement showing the value of Stock on 30.06.2016

	₹	₹
Stock on 8th July, 2016		34,000
Add: Cost of goods sold during 1st July and 8th July, 2016		7,500
		41,500
Less: Cost of goods returned during 1st July and 8th July, 2016	1,225	
Less: Purchased during 1st July & 8th July, 2016 (₹ 7,500 – ₹ 800)	6,700	
Less: Goods held on consignment	5,000	12,925
Stock on 30th June, 2016		28,575

Working Notes

1. Cost of Goods Sold:

		₹	₹
(a)	Sales at cost plus 25% (9,340 – 840)	8,500	
	Less: 20% Profit on Sales	1,700	6,800
(b)	Sale at cost plus 20%	840	
	Less: 16.67% Profit on sale	140	700
			7,500

2. Cost of Goods Returned:

		₹	₹
(a)	Selling Price	750	
	Less: Profit 20% on Sales	150	600
(b)	Selling Price	750	
	Less: Profit 16.67% on Sale	125	625
			1,225

Illustration: 11

X who was closing his books on 31st March, 2016 failed to take the actual Stock, which he did only on 19th April, 2016, when it was ascertained by him to be worth ₹ 25,000.

It was found that sales are entered in the sales book on the same day of dispatch and return inwards in the returns book as and when the goods are received back. Purchases are entered In the purchases day book once the invoices are received.

It was found that sales between 31st March, 2016 and 9th April, 2016 as per the sales day book are ₹ 1,720. Purchase between 31st March 2016 and 9th April, 2016 as per purchases day book are 1,200 out of these, goods amounting to ₹ 50 were not received until after the stock was taken.

Goods invoiced during the month of March 2016 but goods received only on 4th April, 2001 amounted to ₹ 100 rate of gross profit is 33 1/3 %on cost.

Ascertain the value of physical stock as on 31st March, 2016.

(CA – Adapted)

Solution

Statement Showing the Value of Stock on 31.03.2016

		₹
Stock on 09.04.2016		25,000
Add: Cost of goods sold during the period Sale	1,720	
Less: Profit (25% of sales)	430	1,290
		26.290
Less: Goods Purchased and received during the period (1200 – 50)		1150
Value of stock on 31.3.2016		26.220

Less: Goods purchased before 31.3.2016 but delivered on 4.4.2016	100
Value of Physical Stock on 31.3.2016	**26,120**

SELF ASSESSMENT QUESTIONS

Multiple Choice Questions: Accounting Standards

1. Significant accounting policies are disclosed
   (a) Along with financial statement (b) In the books of accounts
   (c) Along with balance sheet (d) In the accounting software
2. Accounting Standard 1 is
   (a) Mandatory (b) Optional
   (c) Recommendatory (d) No longer valid
3. The purpose of AS 1 is to establish a Standard as to
   (a) The preparation of final statements (b) Fundamental accounting assumptions
   (c) Desirable accounting policies (d) Disclosure of accounting policies
4. Following is an example of an accounting policy
   (a) Consistency (b) Depreciation
   (c) Accrual (d) Going concern
5. Following is an example of an accounting policy
   (a) Going concern (b) Entity
   (c) Conservatism (d) Conversion of foreign currency items
6. Following is an example of accounting policy
   (a) Realisation (b) Accrual
   (c) Entity (d) Valuation of fixed assets
7. Factors to be considered while selecting accounting policies
   (a) Consistency (b) Prudence
   (c) Dual aspect (d) Cost
8. Disclosure should form part of
   (a) Directors report (b) Auditor's report
   (c) Final accounts (d) Books of accounts
9. As per AS 1 the effect of any change in accounting policy on the value of any item in the final accounts should
   (a) Be reported to directors (b) Be reported to CEO
   (c) Be disclosed (d) Be ignored

10. Accounting policies are
    (a) Prescribed by AS-1 (b) Same for all the organisations
    (c) Change from concern to concern (d) Laid down by law
11. Following is the example of accounting policy
    (a) Consistency (b) Goodwill treatment
    (c) Cost (d) Conservatism
12. Following is the example of accounting policy
    (a) Going Concern (b) Accrual
    (c) Treatment of retirement benefits (d) Disclosure
13. Following is the example of accounting policy
    (a) Realisation (b) Accrual
    (c) Accounting period (d) Recognition of profit on contract
14. Following factors should be considered in selection of accounting policies
    (a) Consistency (b) Prudence
    (c) Dual aspect (d) Cost
15. Following factors should be considered in selection of accounting policies
    (a) Going concern (b) Growth of business
    (c) Substance over form (d) Solvency
16. Following factors should be considered in selection of accounting policies
    (a) Liquidity (b) Cost
    (c) Materiality (d) Morale of employees
17. As per AS-1, disclosure should be made of
    (a) Significant accounting policies (b) Assumptions in accounting
    (c) Accounting principles (d) Accounting policies
18. As per AS-1, disclosure of accounting policies should form part of
    (a) Financial statements (b) Director's Report
    (c) Auditor's Report (d) Books of account
19. As per AS-1, disclosure of accounting policies should be made
    (a) At all relevant places (b) At one place
    (c) In Profit & Loss Account (d) In Balance Sheet
20. As per AS-1, any change in accounting policy
    (a) Should be disclosed (b) Should not be disclosed
    (c) Requires permission from ICAI (d) Requires permission from the Government

21. The Rule followed in disclosure of accounting policies
    (a) All significant policies should be disclosed
    (b) Only a few policies should be disclosed
    (c) Accounting policies should not be disclosed
    (d) None of the above

    [**Ans.** (1 – a), (2 – a), (3 – d), (4 – b), (5 – d), (6 – d), (7 – b), (8 – c), (9 – c), (10 – c), (11 – b), (12 – c), (13 – d), (14 – b), (15 – c), (16 – c), (17 – a), (18 – a), (19 – b), (20 – a), (21 – a)]

Accounting Standard – 2: Valuation of Inventories

1. Valuation of inventories is governed by
    (a) Companies Act (b) Income Tax Act
    (c) AS-2 (d) AS-6
2. AS-2 defines inventory as
    (a) Current assets (b) Current liabilities
    (c) Fixed assets
    (d) Assets held for sale in the ordinary course of business
3. As per AS-2, inventory covers
    (a) Livestock (b) Goods purchased for resale
    (c) Investment held as stock in trade (d) WIP in construction contracts
4. As per AS-2, inventory should be valued at
    (a) Cost (b) Lower of cost and net realisable value
    (c) Realisable value (d) Retail price
5. As per AS-2, cost of inventories should include
    (a) All cost of purchases
    (b) All cost of purchase, cost of conversion and cost incurred to bring the inventory to the present location
    (c) Cost of purchases and selling (d) Cost of purchases and transport
6. AS-2 states that, inventory should be valued at
    (a) FIFO or Weighted average basis (b) Retail price of standard cost
    (c) LIFO (d) Current replacement cost
7. Weighted Average method can be used under
    (a) Only periodic inventory system (b) Periodic and perpetual inventory systems
    (c) Only perpetual inventory system (d) None of the above

8. As per AS-2, cost of inventories should exclude
   (a) Direct labour (b) Interest on loans
   (c) Factory overheads (d) Cost of designing the product
9. Under periodic inventory system, closing stock is valued
   (a) By actually counting the stock on a particular date
   (b) From the stores ledger
   (c) By deducting value of sales from value of purchases
   (d) On estimate basis
10. As per AS-2, Inventory covers
   (a) Machinery spares (b) WIP in case of service providers
   (c) Materials or suppliers used in production
   (d) Stock of mineral oil
11. As per AS, goods and services produced and kept aside for specific projects should be valued at
   (a) Contract price (b) Net realisable value
   (c) Identified individual cost (d) Pre-placement cost

[**Ans.** (1 – c), (2 – d), (3 – b), (4 – b), (5 – b), (6 – a), (7 – b), (8 – b), (9 – a), (10 – c), (11 – c)]

Accounting Standard – 9: Revenue Recognition

1. The AS deals with revenue recognition is
   (a) AS-1 (b) AS-9
   (c) AS-3 (d) AS-10
2. AS-9 does not deal with revenue arising from
   (a) Sale of goods (b) Interest
   (c) Service contracts (d) Construction contracts
3. Revenue from interest is recognised when
   (a) Interest is received (b) Loan is repaid
   (c) Interest accrues on time basis (d) When loan is taken
4. Revenue from dividend is recognised when
   (a) Dividend is received (b) Right to receive dividend is established
   (c) Amount is credited to Bank Account (d) Dividend warrant is despatched by the company
5. In consignment revenue is recognised when
   (a) Goods are sent on consignment (b) Goods are received by the consignee
   (c) Goods are sold out by the consignee

[**Ans.** (1 – b), (2 – d), (3 – c), (4 – b), (5 – c)]

Inventory Valuation

1. Market Value is
   (a) Net realisable value (b) Net realisable value less profit
   (c) Discounted present value
2. The method reflects latest purchase cost in the closing stock is
   (a) FIFO (b) LIFO
   (c) Weighted Average
3. The system which keeps records continuously is
   (a) Perpetual (b) Periodic
   (c) Physical
4. Stock is valued at cost or at market value whichever is lower as per
   (a) Realisation concept (b) Cost concept
   (c) Matching concept
5. The system in which each and every item in the warehouse is physically verified is
   (a) Perpetual Inventory system (b) Physical Inventory system
   (c) Retail Inventory system
6. The standard which governs inventory valuation is
   (a) AS 3 (b) AS 2
   (c) AS 10
7. Carriage on purchases is
   (a) Added to the cost of inventory (b) Deducted from the cost of inventory
   (c) Multiplied by the cost of inventory
8. The system in which fluctuations in prices are averaged out
   (a) Weighted Average Method (b) FIFO Method
   (c) LIFO Method
9. The concept applicable for stock valuation is
   (a) Consistency (b) Realisation
   (c) Conservatism

   [**Ans.** (1 – a), (2 – a), (3 – a), (4 – a), (5 – b), (6 – b), (7 – a), (8 – a), (9 – b)]

MATCH THE FOLLOWING COLUMNS.

Accounting Standard – 1: Disclosure of Accounting Policies

	Column A		Column B
(a)	Accounting Standards issued by	(i)	Conservatism
(b)	Accounting policy	(ii)	AS-1
(c)	Accounting assumption	(iii)	Area of accounting policies
(d)	Disclosure of accounting policies	(iv)	Disclosure of policy
(e)	Treatment of goodwill	(v)	Method of Stock Valuation
		(vi)	ICAI

[**Ans.** (a – vi), (b – v), (c – i), (d – ii), (e – iii)]

Accounting Standard – 2: Valuation of Inventories

	Column A		Column B
(a)	Inventory valuation	(i)	Does not apply to machinery spares
(b)	Inventory covers	(ii)	Lower of cost and net realisable value
(c)	AS-2	(iii)	Net realisable value
(d)	Basic Rule of Valuation of Inventory	(iv)	AS-2
(e)	NRV	(v)	Raw material, consumables
		(vi)	Market price

[**Ans.** (a – iv), (b – v), (c – i), (d – ii), (e – iii)]

Accounting Standard – 9: Revenue Recognition

	Column A		Column B
(a)	Revenue recognition	(i)	With revenue from construction contract
(b)	AS-9 does not deal	(ii)	Amount earned by sale of goods
(c)	Revenue	(iii)	Booked on time basis
(d)	Revenue from interest	(iv)	When right to receive dividend is established
(e)	Dividend recognised	(v)	Royalties
		(vi)	AS-9

[**Ans.** (a – vi), (b – i), (c – ii), (d – iii), (e – iv)]

Inventory Valuation

	Column A		Column B
(a)	Stock is valued at current rate	(i)	Perpetual System
(b)	Issue is valued at latest rate	(ii)	Periodic Inventory System
(c)	Stock is valued continuously	(iii)	Weighed Average Method
(d)	Stock is physically valued	(iv)	LIFO
(e)	Fluctuations in prices are overcome	(v)	FIFO
		(vi)	FIFO

[**Ans.** (a – vi), (b – iv), (c – i), (d – ii), (e – iii)]

FILL IN THE BLANKS WITH SUITABLE WORDS.

Accounting Standard – 1: Disclosure of Accounting Policies

1. If standards are not followed, the ______ has to make a disclosure in the accounting report in case of failure.
2. The _______ statements are prepared from the books of accounts and other records maintained by the enterprise.
3. There is _______ to establish accounting standards.
4. There is need of ______ to accounts.
5. There is need of ______ change in accounting policies.
6. Depreciation can be calculated either by _____ line method or ______ value methods.
7. Inventories may be valued by the ______ methods.
8. It is difficult to follow a _______ accounting policy in all the circumstances.

[**Ans.** 1. auditor, 2. financial, 3. need, 4. notes, 5. disclose, 6. straight, written down, 7. different, 8. uniform]

Accounting Standard – 2: Valuation of Inventories

Valuation of inventories is governed by

1. Inventories are valued at _______ of cost and net realisable value.
2. Inventory consists of finished goods held for sale in the ______ course of business.
3. Inventories do _______ include machinery.
4. Inventories are defined as ______ (AS-2 (Revised)).
5. As per AS-2 (Revised) ______ approach for costing inventories has been eliminated.
6. By-products, wastes and spares are to be valued at net realizable price if their value is not ______ .

7. AS-2 (Revised) is applicable to _______ enterprise.
8. Main product is the target product of _______ value.

[**Ans.** 1. lower, 2. ordinary, 3. not, 4. asset, 5. Direct, costing, 6. material, 7. all, 8. significant]

Accounting Standard – 9: Revenue Recognition

1. AS-9 is applicable to _______ enterprises.
2. AS-9 explains when the _____ should be recognised in the Profit & Loss Account.
3. As per AS-9 revenue from sale of goods is recognised when the seller ______ the goods to the buyer for a _______ .
4. Installation fees are recognised as revenue when the installation is ______ and its is _____ by the client.
5. The buyer requests delayed delivery although he purchases the ____, takes the ______, and accepts billing, in this case the sale is complete.
6. Revenue should be recognised when goods are installed at the buyer's place to his _____ and goods are inspected and _______ by the buyer.

[**Ans.** 1. all, 2. revenue, 3. transfers, consideration, 4. completed, accepted, 5. goods, title, 6. satisfaction, accepted]

Inventor Valuation

1. _____ method assumes that stock received first is issued first.
2. _____ method assumes that stock received last is issued first.
3. In ______ method, stock is valued at oldest rate.
4. In ______ method, stock is valued at current rate.
5. In ______ method, stock is over valued when the prices are rising.
6. ______ method is suitable for perishable goods.
7. ______ method is applied when the lots of goods are not identifiable.
8. In ______ method, Balance Sheet shows current cost of stock.
9. Under ______ inventory system, stock is valued by physical stock taking.
10. Under ______ inventory system, stock is valued on the basis of stores ledger.
11. Under ______ method, fluctuations in prices are overcome.
12. AS-2 recognises _______ and _______ Methods.

[**Ans:** 1. FIFO; 2. LIFO; 3. LIFO; 4. FIFO; 5. FIFO; 6. FIFO; 7. Weighted Average; 8. FIFO; 9. Periodic; 10. Perpetual; 11. Weighted Average; 12. FIFO, Weighted Average]

1. Theory Question

1. What is the importance of proper valuation of stock?
2. Describe the various methods of valuation of stock.
3. Distinguish between Weighted Average and FIFO methods of valuation of stock. Explain with illustration.
4. What adjustments are required to be made to ascertaining the value of stock if stock if is not done on the date of balance sheet?

2. Practical Problems

1. Following is the record of transactions regarding purchases and sales:

2013			
January	Purchased	100 units	@ ₹ 4
February	Purchased	200 units	@ ₹ 4.5
March	Purchased	300 units	@ ₹ 5
April	Sold	70 units	@ ₹ 6
May	Sold	150	@ ₹ 7.50

Required:

(a) Prepare stock register as per the following methods:

(i) FIFO

(ii) Weighted Average.

(b) Find out cost of goods sold.

2. Keep stock record on FIFO. Weighted Average basis from the following transactions:

Purchases:

2013				
January	1	500	units	@ ₹ 18
	5	700	units	@ ₹ 20
	9	900	units	@ ₹ 18
	15	300	units	@ ₹ 25
	25	200	units	@ ₹ 20
	31	500	units	@ ₹ 25

2013				
January	2	200	units	@ ₹ 22
	7	500	units	@ ₹ 25
	11	400	units	@ ₹ 21
	18	800	units	@ ₹ 28
	27	500	units	@ ₹ 25

Also find out cost of goods sold and the profit.

3. The purchases and issues of materials of Alpha Industries Ltd. are as follows:

	Units	Unit Cost (₹)
Purchased	100	1
Purchased	400	1.50
Issued	200	
Purchased	300	1.25
Issued	300	

What is the value of the ending inventory under the following methods:

(a) Weighted Average Price Method.

(b) First in First out Method.

4. The following transactions took place in I of a material.

Date	Receipt Quantity	Rate	Issue Quantity
2.3.2013	200	2	
10.3.2013	300	2.40	
15.3.2013	–	–	250
18.3.2013	250	2.60	–
20.3.2013	–	–	300

Prepare a stock register as per Weighted Average Method.

5. Find the value of closing stock, under FIFO, and Weighted Average Price Method, from the following information: (under both the systems)

2013					
January	1	Opening Stock	700	units	@ ₹ 5
	4	Sales	300	units	
	8	Purchases	900	units	@ ₹ 6
	10	Sales	500	units	
	I 1	Sales	100	units	
	16	Purchases	800	units	@ ₹ 6.50
	1 8	Sales	400	units	
	23	Purchases	1,100	units	@ ₹ 7.00
	29	Sales	600	units	

The market value of closing stock on 31st January, 2001; was ₹ 6.50.

6. The following particulars have been extracted in respect of material X. Prepare a Stores Ledger Account showing the receipts and issues, pricing the materials issued in the basis of Weighted Average (under both the systems).

Receipts:

2016					
October	1	Opening Stock	200	units	at ₹ 3.50 per unit
	3	Purchased	300	units	at ₹ 4.00 per unit
	13	Purchased	900	units	at ₹ 4.30 per unit
	23	Purchased	600	units	at ₹ 3.80 per unit

Issues:

2016				
October	5	Issued	400	units
	15	Issued	600	units
	25	Issued	600	units

[**Ans.** Issue Price Rate 5th, 15th, 25th, Closing Stock Weighted Average 3.80, 4.25, 3.98, 400 units ₹ 1,592]

7. From the following transactions, prepare separately the Stores Ledger Accounts, using the following pricing methods: FIFO

January	1	Opening Balance	100	units	@ ₹ 5 each
January	5	Received	500	units	@ ₹ 6 each
January	20	Issued	300	units	
February	5	Issued	200	units	
February	6	Received	600	units	@ ₹ 5 each
March	10	Issued	300	units	
March	12	Issued	250	units	

[**Ans:** 150 units @ ₹ 5 = ₹ 750]

8. At the beginning of October 2016 the Bangalore Tin Co. had 10,000 lbs. of tin @ ₹ 2 per lb. Further purchases were made during the month as follows:

October	4	2,000	lbs.	@ ₹ 2.50 per lb.
	10	6,000	lbs.	@ 2.00 per lb.
	20	10,000	lbs	@ ₹ 3.50 per lb.

The issues to manufacture were as follows:

October	12	16,000 lbs.
	22	10,000 lbs.

Write the stores ledger cards with the above the transactions based in both the FIFO. What will be the value of the value of the closing stock in each case?

(**Ans.** FIFO: 2,000 units – ₹ 7,000)

9. Prepare a Stores Ledger Account from the following transactions assuming that issue of stores have been made on the principle of "First In First Out":

2016				
January	2	Purchased	2000	units at ₹ 4.00 per unit
January	20	Purchased	250	units at ₹ 5.00 per unit
February	5	Issued	1000	units
February	10	Purchased	3000	units at ₹ 6.00 per unit
February	12	Issued	2000	units
March	2	Issued	500	units
March	15	Purchased	2250	units at 5.50 per unit
March	20	Issued	1500	units

(**Ans.** FIFO Stock: 1,500 units at ₹ 5.50 = ₹ 8,250)

10. Prepare a Stores Ledger Account from the following information for the monthe of December 2016 on the basis of FIFO Method:

2016				
December	3	Opening Balance 200 kg at ₹ 20 per kg.		
December	4	Issue	100 kg.	
December	10	Issue	50 kg	
December	18	Purchases	300 kg	at ₹ 18 per kg.
December	20	Issue	300 kg	
December	28	Purchased	50 kg	at ₹ 15 per kg
December	30	Issue 1	0 kg.	
December	30	Received back from completed job 5 kg. (Previously issued at ₹ 20 per kg)		

(**Ans.** Stock 5 kg returned to stores valued at ₹ 20)

11. The following are the transactions in respect of material X for the month of October 2016.

2016				
October	5	Opening Balance	400	units at ₹ 2.90 per unit
"	5	Purchased	500	units at ₹ 3 per unit
"	10	Issued	700	units
"	15	Purchased	700	units at ₹ 3.10 per unit
"	20	Issued	800	units
"	25	Purchases	400	units at ₹ 3.20 per unit
"	30	Issued	500	units

Indicate at what price each issue must be made if based on Weighted Average Method.

(**Ans.** ₹ 2.955; ₹ 3.057; ₹ 3.153)

12. Prepare a Stores Ledger from the following transactions adopting the 'Weighted Average Method' of pricing out issues.

2016

June	1	Opening Balance	100 units at. ₹ 3 per unit
June	5	Issued to production	4 units
June	7	Purchased	96 units at ₹ 4 per unit
June	9	Issued	40 units to production
June	19	Purchased	152 units at ₹ 3 per
June	24	Received back into stores	38 units out of 40 units issued on 9th June, 1982.
June	27	Issued to production 20 units.	

(**Ans.** 322 units, ₹ 1.056, Rates ₹ 3, ₹ 3.5, ₹ 3.277)

13. With the help of the following information, prepare the Stores Ledger Card based on the Weighted Average Method of pricing issues: (under both the systems)

September	1	Opening Balance	24,000 kg.	@ 7,500 per tonne
	1	Purchased	44,000 kg.	@ ₹ 7,600 per tonne
	1	Issue	10,000 kg.	
	5	Issue	16,000 kg.	
	12	Issue	24,000 kg.	
	13	Purchase	10,000 kg.	@ ₹ 7,800 per tonne
	18	Issue	20,000 kg.	
	22	Purchase	50,000 kg.	@ ₹ 8,000 per tonne
	28	Issue	30,000 kg.	
	30	Issue	22,000 kg.	

(**Ans.** Closing Stock 2,000 kg. @ ₹ 7,974)

14. The following particulars relate to receipts and issues of material during March 2016.

2016

March	4	Received	500	units @ ₹ 2.000 each
	18	Received	350	units @ ₹ 2.10 each
	19	Issued	600	units
	24	Received	600	units @ ₹ 2.20 each
	25	Issued	450	units
	26	Received	500	units @ ₹ 2.30 each
	28	Issued	510	units
	20	Issued	100	units

Prepare a Store Ledger Account on the basis of Weighted Average Price Method

(**Ans** 290 units @ ₹ 2.2348)

15. You are presented with the following information by Sphinx Engineering Co. relating to the first week of September 2016.

Mateials: The transactions in connection with the materials are as follows:

Days	Units	Receipts Rate per unit (₹)	Issued Units
1st	40	15.00	
2nd	20	16.50	
3rd			30
4th	50	14.30	
5th			20
6th			40

Calculate the cost of materials issued under FIFO methos and Weighted Average method of issue of materials.

(**Ans.** FIFO ₹ 1,359, Weighted Average Method ₹ 1,350)

16. The following particulars relate to receipts and issues of a material during March 2016.

2016				
March	1	Received	500 units	@ ₹ 2.00 each
	18	Received	350 units	@ ₹ 2.10 each
	19	Issued	600 units	
	24	Received	600 units	@ ₹ 2.20 each
	25	Issued	450 units	
	26	Received	500 units	@ ₹ 2.30 each
	28	Issued	510 units	
	30	Issued	100 units	

Prepare a Stores Ledger Account on the basis of Weighted Average Price Method.

(**Ans.** 290 units ₹ 649; Issue Rate: ₹ 2,041: ₹ 2,153: ₹ 2,234)

17. Using the information given, draft Stores Ledger Records showing quantities and values of receipts, issues and balance in hand under the following method of pricing stores issues:

Weighted Average Price.

January	1	Balance in hand	1,000 units	₹ 1 each
January	15	Received	3,000 units costing	₹ 3,300
February	12	Received	2,000 units costing	₹ 2,400
January	20	Issued	2,000 units	
February	27	Issued	3,400 units	

(**Ans.** 600 units ₹ 683: Issue rates ₹ 1.075 and ₹ 1.1375)

18. Enter the following transactions in the stores Ledger of Y material using the FIFO Method.

2016

January	1	Balance 250 units @ ₹ 10 unit
	3	Issued 50 units on M.R. No 61
	6	Received 800 units vide G.R. No. 13 @ ₹ 11 per unit
	7	Issued 300 units on M.R. No. 63
	8	Returned to stores 20 units on M.R. No. 6
	12	Received 300 units per G.R.No. 15 @ ₹ 12 per unit
	15	Issued 320 units M.R. No. 83
	18	Received 100 unit, vide G.R.Note No. 77 @ ₹ 12 per unit
	20	Issued 120 units M.R.No. 102
	23	Returned to vendors 40 units from G.R.No.77 received on 18th instant
	26	Received 200 units on G.R.No 96 @ 10 per unit
	28	Fright paid on purchases (vide G.R. No.96) ₹ 50
	30	Issued 250 units on M.R. No. 113

Note: M.R. = Material Requisition

G.R. Note = Goods Received Note

(P.U.)

(**Ans.** FIFO 340 x 12.00 = ₹ 4,080; 200 x 12.50 = ₹ 2,500)

19. From the following details find out closing stock as per FIFO Method:

Purchases:

Date	**Purchases Units**	**Price Per Unit ₹**
4.11.2016	20	15
17.11.2016	30	14
2.12.2016	40	14.50
30.12.2016	50	13.00

Sales:

Date	**Sales (Units)**	**Selling Price Per Unit ₹**
20.11.2016	25	20
5.12.2016	40	21
10.12.2016	10	18
31.12.2016	45	15

On 20th December, 2016; two units sold on 10th December, 2016 were returned by the customers. On 29th December, 2016; one unit was damaged and it had to be discarded.

Also calculate profit.

20. Sumit Ltd. Has purchased and issued the materials in the following order:

2016				
August	1	Purchases	300 units	₹ 2 per unit
	4	Purchases	600 units	₹ 4 per unit
	6	Issued	500 units	
	10	Purchases	700 units	₹ 4 per unit
	15	Issues	800 units	
	20	Purchases	300 units	₹.5 per unit
	23	Issues	100 units	

Ascertain the quantity of closing stock as on 31st August, 2016 and state what will be the value under the following methods:

(a) First In First Out Method.

(b) Weighted Average Method under Physical Inventory Method and Perpetual Inventory Method.

21. Determine the value of stock to be taken for Balance Sheet as on 31st March, 2016 from the following information:

The stock was physically verified on 23rd March, 2016 and was valued at ₹ 6,00,000. Between 23rd March, 2016 and 31st March, 2016; the following transactions had taken place:

(a) Purchases ₹ 50,000, of this goods worth ₹ 20,000 were delived on 5th April, 2016.

(b) Out of goods sent on consignment, goods worth ₹ 30,000 (at cost) were unsold.

(c) Sales were ₹ 1,70,000. These includes goods worth ₹ 40,000 sent on approval. Half of these were returned before 31st March as regards remaining no institution is received.

(d) Normally firm sells goods on cost + 25%. However, one lot of goods costing ₹ 30,000 was sold for ₹ 15,000

(ICWA–Adapted)

(**Ans.** 5,58,000)

2

Chapter

Final Accounts

CAPITAL AND REVENUE EXPENDITURE

Accounting is the recording and reporting of business transactions. Business transactions involve activities of actual business (selling goods or services), investment (purchasing assets) and financing (raising money for investment). In accounting, business activities give rise to revenue income and revenue expenditure; investment activities give rise to capital expenditure; financing activities give rise to capital receipts, P & L a/c is a summary of revenue income and revenue expenses, Balance Sheet is summary of capital receipts and capital expenditure.

Expenditure is usually of two types:

1. Capital Expenditure
2. Revenue Expenditure

Capital Expenditure: Capital expenditure consists of expenditure, the benefit of which is not fully enjoyed in one accounting period but spread over several accounting periods. It includes assets acquired for the purpose of earning income or increasing the earning capacity of the business or effecting economy in the operation of an asset. These are not meant for sale. Expenditure incurred for improving assets and extending an existing asset is also capital expenditure.

Definition: Eric Kohler has defined capital expenditure as "an expenditure intended to benefit future periods; an addition to fixed assets. The term is generally restricted to expenditures that add fixed asset units or that has the effect of increasing the capacity, efficiency, life span or economy of operation of an existing asset."

Examples:

(a) Interest on capital paid during the period of construction of company.

(b) Expenditure in connection with or incidental to the purchase or installation of an asset.

(c) Acquisition of new assets.

(d) Expenditure incurred for putting the old asset purchased into working condition.

(e) Additions and extensions to existing assets.

(f) Betterment of fixed assets or improvement of an asset to produce more to improve its earning capacity or to reduce its operating expenses or to increase the life of asset.

Revenue Expenditure: Revenue expenditure consists of expenditure incurred in one period of the accounting, the full benefit of which is enjoyed in that period only. This does not increase the earning capacity of the business but it is incurred in order to maintain the existing earning capacity of the business. It includes all expenses which arise in normal course of business. The benefit of such expenditure is for a short period, say, one year only and it is not to be carried forward to the next year. The expenditure is of a recurring nature, i.e., arises again and again.

Definition: Eric Kohler has defined revenue expenditure as "an expenditure charged against operation: a term used to contrast with capital expenditure."

Examples:

(a) Purchase of raw materials for conversion into finished goods.

(b) Selling and distribution expenses incurred for sale of finished goods, e.g., sales office expenses, delivery expenses, advertisement charges, etc.

(c) Establishment expenses like salaries, wages, rent, rates, taxes, insurance and depreciation on office equipment.

(d) Depreciation of plant, machinery and equipment.

(e) Expenses incurred in order to maintain the existing fixed assets in an efficient and workable state such as repairs to building, repairs to plant, whitewashing and painting of building.

Difference between Capital and Revenue Expenditures

Capital Expenditures	*Revenue Expenditures*
1. Its effect is long term, i.e., it is not exhausted within the current account year. Its benefit is enjoyed in future year or years also. In a word, its effect reduces gradually.	1. Its effect is temporary, i.e., it is exhausted within the current accounting year.
2. An asset is acquired or the value of an asset is increased as a result of this expenditure.	2. Neither an asset is acquired nor is the value of an asset increased.
3. It does not occur again and again – it is non-recurring and irregular.	3. It occurs repeatedly. It is recurring and regular.
4. Generally, it has physical existence, i.e., it can be seen with eyes.	4. It has no physical existence, i.e., it cannot be seen with eyes.
5. This expenditure improves the position of the concern.	5. This expenditure helps to maintain the position of the concern.
6 A portion of this expenditure is shown in the trading and profit and loss account or income and expenditure account as depreciation.	6 The whole amount of this expenditure is shown in trading and profit and loss account or income and expense account. But deferred revenue

	expenditures and prepaid expenses are not shown.
7. It pertains to investing activity.	7 It pertains to business activity.
8. It does not reduce the revenue of the concern. Purchase of fixed assets does not affect revenue.	8 It reduces revenue. Payment of salaries to employees decreases revenue.

Deferred Revenue Expenditure: Deferred revenue expenditure is a revenue expenditure which has been incurred during one accounting year which is applicable either wholly or in part to further accounting years.

Definition: According to Prof. AW. Johnson, "Deferred revenue expenditure includes those non-recurring expenses, which are expected to be of financial nature, distributed to several accounting periods of indeterminate total length. These are of revenue nature but are deferred or postponed. It is of quasi-capital nature."

In simple words, we can say that Deferred Revenue Expenses are those expenses, the benefit of which may be extended to a number of years, say, 3 to 5 years. It is basically expenditure while forming company. The benefit of this will be derived in the future years also. Any expenditures relating to capital (shares, debentures, securities) is called deferred revenue expenditure.

Examples:

(a) Every expenditure for launching of new project (Advertisement Expenditure).

(b) Expenditure for the issue or raising loan or capital or debentures.

(c) Expenditure for the formation or registration of company.

(d) Preliminary expenditure.

RECEIPTS

Receipts refer to the actual amounts of cash received. They can be either of capital nature or revenue nature.

Capital Receipts: Capital receipts mean an amount received by a concern in the course of its financing activity (obtaining money as capital or loan or sale of assets). Concerns need money to carry on its business activities and investment activities (purchase of assets or investments). The money is obtained either from the proprietor (capital) or loans (liabilities) or sale of assets or sale of investments. Capital receipts are non-recurring in nature. Thus, loan is obtained from the bank only once in a while and not everyday.

Capital receipts include the following:

1. Capital brought in by the proprietor at the commencement and any additions made subsequently.
2. Money borrowed from partners, bankers, private individuals, etc.
3. Money received by the sale of fixed assets.
4. Money received on account of capital profit.

Revenue Receipts: Revenue receipts means the receipts from customers for sale of goods, for services given, or for use of funds (loans, capital) or use of assets (patents). Total revenue receipts are computed by adding up the sale price of goods sold, fees for services, interest on loans given, dividend on shares and royalty for use of patents etc. Just like trees planted earlier yield fruits, revenue receipts arise from past capital expenditure, i.e., from exploiting assets and investments acquired earlier. Revenue receipts are recurring in nature, e.g., income from sale of goods is received regularly so long as the business continues.

Revenue receipts include the following:

1. Money received by the sale of floating assets — by sale of goods.
2. Money received on account of some revenue profit.

Distinction between Capital Receipts and Revenue Receipts

Capital Receipts	*Revenue Receipts*
1. Capital receipt pertains to financing activity.	1. Revenue receipts pertains to business activity.
2. Examples are capital from owner, loans from bank, etc.	2. Examples are revenue receipts from sale of goods, fees, interest, dividend, royalty.
3. Capital receipts are shown as liability in balance sheet.	3. Revenue receipt pertaining to current year is shown as income in P & L a/c. Revenue receipt pertaining to future period is shown as liability (advance income) in balance sheet.
4. Capital receipts may be returned back.	4. Revenue receipt cannot be returned/refunded.
5. Capital receipts is non-recurring in nature.	5. Revenue receipt is recurring in nature
6. Capital receipts increases funds available for investment, but may reduce profits as interest is to be paid on loans obtained.	6. Revenue receipts increases profits and funds.

CAPITAL AND REVENUE PROFITS

Definition and Explanation

Capital profit means a profit made on the sale of a fixed asset or profit earned on raising monies for the business. For example, a building purchased for ₹ 20,000 is sold for ₹ 25,000. The profit ₹ 5,000, thus, made is a capital profit.

Revenue profit, on the other hand, is a profit made by the business, e.g., profit on the sale of goods, interest from investments, commission earned, etc.

Whenever capital profit is made, it should either be transferred to the capital account of the proprietor or credited to capital reserve account which would appear as a liability on the balance sheet. But capital profits, should in no case be transferred to profit and loss account because it is non-trading profit. Revenue profits, on the other hand, should be transferred to profit and loss account because they arise out of regular trading operation.

CAPITAL AND REVENUE LOSSES

Definition and Explanation

Capital loss means a loss made on the sale of a fixed asset or a loss incurred in connection with the raising of money for business. Capital loss may be shown as an asset in the balance sheet. But as this asset is of fictitious nature, it would advisable to write it off.

Revenue loss, on the other hand, is the loss incurred in trading operations such as loss on the sale of goods. Revenue losses are charged to profit and loss account of the year in which they occur.

CAPITALIZED OR DEFERRED REVENUE EXPENDITURES

Where a certain revenue expenditure incurred is of such a nature that its benefit is likely to be spread over a certain number of years, or where it is of non-recurring and special nature and large in amount, in such circumstances, instead of debiting the entire amount to the profit and loss account of the year in which it has been incurred, it may be spread over a number of years, a proportionate amount as Revenue Expenditure being charged to each year's Profit and Loss account. The remaining portion of the expenditure is carried forward and is known as Capital Expenditure or Deferred Revenue Expenditure and is shown as an asset in the Balance Sheet. Items such as preliminary expenses, cost of issue of debentures are examples that may be classified under this head.

Exceptions to General Rules

There are certain expenses which are usually of revenue in nature but under certain circumstances they become capital expenditures. The following are the examples of expenses which are usually revenue but under certain circumstances become capital.

Legal Charges: These are, as a rule, revenue charges, but legal charges incurred in connection with the purchase of a fixed asset are capital expenditures as they form an additional cost of the asset acquired.

Wages: Wages are ordinary revenue expenditure. But in a manufacturing business where the firm's own men are employed in making of fixed asset, the wages paid for such purpose would be capitalized. For example, if the firm's own men are employed in making extension to the factory building or in erection of plant or manufacturing tools for own requirements, the wages and salaries paid to the persons are not revenue but capital expenditures.

Brokerage and Stamp Duty: Normally, these are revenue expenditures, but brokerage paid on acquisition of a property and stamp duty involved thereon can be capitalized.

Freight and Carriage: This is revenue charge, but freight and carriage paid on newly acquired plant or fixed assets are capital expenditures.

Advertising: Ordinarily, amount expended on advertising is revenue charge but the cost of special advertising undertaken for the purpose of introducing a new line of goods may be capitalized.

Development Expenses: In concern like collieries, mines, tea, rubber, etc., all expenses incurred during the period of development are treated as capital.

Preliminary Expenses: These are the expenses incurred in connection with the formation of a public company. These expenses although are revenue in nature but are allowed to be capitalized and can be shown as an asset in the balance sheet.

Illustration 1: If a building is purchased for ₹ 20,000 from X and ₹ 10,000 is paid in cash and the remaining sum to be paid after six months; ₹ 20,000 is capital expenditure, but ₹ 10,000 is only capital payment. Similarly, if goods are purchased from X for 30,000 and ₹ 15,000 is paid in cash, ₹ 30,000 is revenue expenditure but only ₹ 15,000 is revenue payment.

Illustration 2: Examples of capital acquisitions include the purchase of an office building and the purchase of a vehicle for business use. However, in acquiring a capital asset, certain costs are incurred, such as carriage inwards, installation costs, import duties and valuator fees. Those costs are included as part of the acquisition cost and form part of capital expenditure as well.

Illustration 3: Depreciation of non-current assets: Revenue Expenditure

Insurance, salaries and regular maintenance: Revenue Expenditure

Major repairs of a fixed asset that increases its productivity: Capital Expenditure

Transport costs for tradeable assets: Revenue Expenditure

Transport and installation costs for non-current assets: Capital Expenditure

Illustration 4: The following table illustrates examples of capital and revenue expenditure:

Capital Expenditure	***Revenue Expenditure***
Installation of heating system	Annual costs of heating system
Upgrades to computer system	Power cost of computing system
New premises	Repairs to premises
Painting new premises	Repainting existing premises
Carriage inwards on new equipment	Carriage inwards on stocks for resale
Installation costs of machinery	Running costs of machinery
One-off license fee	Annual road tax

EXERCISE

Self Assessment Questions

1. ***State with reasons whether the following are capital, revenue or deferred revenue expenses:***

   (i) Payment for purchase of goods.

   (ii) Payment for purchase of stationery.

   (iii) Payment for purchase of a car.

   (iv) Payment for heavy inaugural expenses.

(v) Partial refund of capital to a partner.

(vi) Payment of a loan taken earlier.

(vii) Payment of salaries.

(viii) Wages for erection of machinery.

Answers: Capital — 3, 6, 8; Revenue — 1, 2, 5, 7; Deferred — 4.

Terminal Questions

1. State whether the following expenditure is a capital, revenue or deferred revenue expenditure. Give reasons:
   (i) Legal expenses incurred in connection with issue of capital.
   (ii) Cost of replacement of a defective part of the machinery.
   (iii) Expenditure incurred in preparing a project report.
   (iv) Expenditure for training employees for better running of machinery.
   (v) Expenditure incurred for repairing cinema screen.
2. State whether the following expenditure is a capital, revenue or deferred revenue expenditure. Give reasons:
   (i) Legal expenses incurred in connection with issue of equity shares of the company.
   (ii) Cost of replacement of a defective part of the machinery.
   (iii) Expenditure incurred in preparing a project report.
   (iv) Expenditure for training employees for better running of machinery.
   (v) Purchase of machinery for sale.
   (vi) Daily wages paid to office peon.
3. S. Jaggi sells and services typewriters. State which of the following are capital expenditure and which are revenue expenditure, giving reasons for your answer:
   (i) Purchase of a typewriter for office use.
   (ii) Purchase of typewriters for resale.
   (iii) Travelling expenses to service typewriters.
   (iv) Purchase of spare parts to service typewriters.
   (v) Wages of mechanic.
   (vi) Wages of office staff.
   (vii) Telephone charges.
   (viii) Purchase of tools for servicing work.
4. State which of the following are capital expenditure and which are revenue expenditure, giving reasons in each case:
   (i) Payment by cheque for carriage on purchase.
   (ii) Purchase of packing material for distribution of goods from the Calcutta Paper Mill Ltd.

(iii) Purchase of duplicator for use in own office from Gulab & Co.

(iv) The firm acquired a private car from B. Raha, one of the partners of the firm.

5. State with reasons whether the following are Capital or Revenue expenditure:

(i) Expenses incurred in connection with obtaining a license for starting the factory were ₹ 8,000.

(ii) ₹ 1,500 paid for removal of stock to a new site.

(iii) Rings and Pistons of an engine were changed at a cost of ₹ 4,000 to get fuel efficiency.

(iv) ₹ 2,500 spent as lawyer's fee to defend a suit claiming that the firm's factory site belonged to the plaintiff. The suit was not successful.

(v) ₹ 8,000 were spent on advertising the introduction of a new product in the market, the benefit of which will be effective during four years.

(vi) A factory shed was constructed at a cost of ₹ 1,20,000. A sum of ₹ 7,000 had been incurred in the construction of temporary huts for storing building material.

6. The Building Account of Calcutta High School stands in the books at ₹ 75,000. The undermentioned expenses were incurred on the Building during the year. You are asked to state how these items will be treated in the books?

(i) Addition of a new wing to the Library – ₹ 40,000.

(ii) Repairs to the Student's Common Room – ₹ 500.

(iii) Whitewashing the entire Building – ₹ 2,000.

(iv) Pulling out an old structure ₹ 750 and rebuilding it ₹ 10,500.

7. Classify the following between capital expenditure and revenue expenditure giving brief reasons in each case.

(i) Cost of ₹ 30,000 for dismantling, removing and reinstalling plant by a sugar mill incurred in connection with the removal of works to a more suitable locality.

(ii) A sum of ₹ 10,000 spent for alternation of existing plant incorporating thereby new devices, which could effect substantial reduction in power consumption.

(iii) Imported goods worth ₹ 25,000 confiscated by custom authority for non-disclosure of material facts.

(iv) A petrol driven engine of a passenger bus was replaced by a diesel engine.

(v) Cost of repainting the factory shed.

(vi) Cost of transportation ₹ 500 in connection with a newly acquired machine.

(vii) Cost of improving seating capacity of a Cinema Hall.

(viii) Heavy amount spent in a legal suit.

(ix) ₹ 1,000 spent on replacement of defective parts of an old plant.

8. Under what category can we place amounts paid for acquisition of brands?

9. If a capital equipment is purchased with an expected life of seven years, but after two years it is realized that the useful life overall will be only five years. How do we take this into account for purposes of depreciation?

FILL IN THE BLANKS WITH SUITABLE WORDS.

Capital and Revenue Expenditure

1. ______ expenditure is recurring.
2. ______ expenditure is non-recurring.
3. ______ expenditure is shown in the Balance Sheet on asset side.
4. ______ expenditure is shown in Profit & Loss Account.
5. ______ receipts are shown as income in Profit & Loss Account.
6. ______ receipts are shown in Balance Sheet.
7. ______ is expenditure on asset held for generation of interest/dividend.
8. ______ expenditure does not give any future benefits.
9. Wages paid for installation of machinery is a ______ expenditure.
10. Carriage on purchase of furniture is _______ expenditure.
11. Repairs of machinery is a _______ expenditure.
12. Payment of penalty is a ________ expenditure.
13. Documentation charges regarding purchase of building is a _______ expenditure.
14. Depreciation is _______ in nature.
15. Advertising is a _______ expenditure.
16. Demolition cost of old building is a ______ ______ _______.
17. Overhauling of machinery is a _______ expenditure.
18. Amount received on sale of goods is a ______ receipt.
19. Commission received is a ______ receipt.
20. Heavy legal expenses are ______ ______ ______.

FINAL ACCOUNTS OF MANUFACTURING CONCERNS (PROPRIETARY FIRM) ALONG WITH ADJUSTMENTS AND CLOSING ENTRIES

Introduction

The primary function of accounting is to accumulate accounting data in a manner that the amount of profit made or loss suffered during a period can be determined. The manner in which the amount of profit or has been arrived at disclosed in the statement of accounts, prepared at the end of the accounting year. The various items of income and expenditure which arose during the accounting period are detailed out bothering, grouped under significant heads. It is also accompanied by a balance sheet, exhibiting assets and liabilities of the business as at the close of the period. In addition, for showing the nature of economic activity to which the account pertains, the revenue account as well as different sections in which it is set up are invariably headed as manufacturing trading and profit and loss account or simply as profit and loss account. These two statements, i.e., trading and profit and loss account and balance sheet are prepared to give the final results of the business. That is why both are collectively called final accounts.

Thus, preparation of final accounts is the last step in the accounting cycle. In fact, final accounts include a number of accounts such as: (i) trading accounts, (ii) profit and loss account and (iii) balance sheet. Though balance sheet is a statement, for all practical purposes, it is treated as one of the final accounts.

Once the "trial balance" is extracted and 'errors' rectified, a trader prepares the "final accounts" so as to know the final results (i.e., net profits or loss) and the financial position (i.e., assets and liabilities) of his business. Trading account and profit and loss account concerning goods by passing entries are known as "closing entries". All remaining accounts, *viz.,* real and personal accounts pertaining to property, assets, debtors and creditors are just shown in a statement called balance sheet.

This procedure is discussed in detail in the following pages.

Manufacturing account

Those concerns which are converting raw materials into finished goods and then sell the finished goods are required to prepare manufacturing account besides preparing trading and profit and loss account. This account is prepared to calculate the cost of goods manufactured, which is transferred to the trading account. The expenses relating to the factory are transferred to manufacturing account. The main object of manufacturing account is to show:

(i) Cost of finished goods produced and

(ii) Constituent items thereof such as cost of material consumed, productive wages, direct and indirect expenses.

Features of Manufacturing Account

(a) Stock of Finished Goods: Since the main purpose of preparing this account, is to find out the cost of goods produced during the year, the opening and closing stock of finished goods are not to be shown in this account. They will be shown in the trading account.

(b) ***Raw Materials Consumed:*** The cost of raw materials consumed during the year is to be debited in the account. It can be found out as follows:

Cost of raw materials consumed

Opening stock of raw materials	xxx	
Add: Purchase of raw materials	xxx	
	xxx	
Less: Closing stock of raw materials	xxx	xxx

(c) ***Work-in-progress (partly finished stock):*** In a manufacturing business concern, there are always some unfinished goods, the cost of closing work-in-progress is credited in the account, shown in the balance sheet and debited to the manufacturing account of the next year as an opening balance.

(d) ***Factory Expenses:*** All factory expenses are debited to this account factory rent, rates, salaries of supervising staff, light, heat and fuel, repairs and renewals, depreciation relating to factory property (i.e., machinery) etc.

(e) ***Sale of Scrap:*** Scrap is the incidental residue from certain types of manufacture. The value realized from the sale of scrap is credited to the manufacturing account.

(f) ***Cost of Production:*** At this stage, the difference between the two sides of the manufacturing account shows the cost of goods produced during the year. The balancing figure in the account is the cost of goods manufactured which will be debited to trading account. The trading account therefore, will compromise only the opening stock of finished goods, cost of goods manufactured, sales (less sales returns), and the closing stock of finished goods.

A Pro forma of manufacturing account is given below:

Manufacturing a/c for the year ended……

Particulars		***(₹)***	***Particulars***	***(₹)***
To Work-in-progress (opening)		xxx	By Sale of scrap	xxx
To Material used			By Work-in-progress (closing)	xxx
Opening stock	xxx		By Cost of goods produced transferred	
Add: Purchases	xxx		to Trading a/c (bal. fig.)	xxx
Less: Closing stock	xxx			
		xxx		
To Wages		xxx		
To Factory expenses		xxx		
To Purchase expenses		xxx		

To Import duty	xxx		
To Carriage inward	xxx		
To Depreciation on machinery	xxx		
To Repairs to machinery	xxx		
	xxx		xxx

TRADING ACCOUNT

Trading account is prepared for specific period to know the trading results of the business. It contains in a summarized form all the transactions occurring during a trading period which have direct relation to the goods dealt in by the business. It is prepared usually by merchandising concerns which purchase goods and sell the same during a particular accounting period. It is mainly prepared to ascertain the gross profit or gross loss. Gross profit or gross loss is the difference between actual sale proceeds and the cost of goods sold (Gross profit = Excess of sale proceeds over cost of goods sold and Gross Loss = Excess of cost of goods sold over sale proceeds). The 'cost of goods sold' includes the "purchase value" of such goods plus the "buying and bringing" expenses and the "conversion expenses of raw materials into saleable finished goods. Thus, 'cost of goods' consists of:

(i) The opening stock of goods plus net purchases (i.e., purchases less returns) less closing stock of such goods and

(ii) All expenses of bringing the goods into saleable condition and also to the point of sale, i.e., all manufacturing expenses, carriage, cartage, freight, duty, etc.

Preparation of Trading Account

Trading account is a ledger account. Therefore, its form and construction conform to the rules of double entry principles of debit and credit.

As the trading account contains the results of operations over a period , the heading should be “Trading account for the year (or any period) ended….. “.

A Pro forma of a trading account is given below:

Trading account for the year ended…………..

Particulars		*(₹)*	*Particulars*		*(₹)*
To Opening stock of Fin. Goods		xxx	By Sales	xxx	
To Purchases	xxx		***Less:*** Sales returns	xxx	xxx
Less: Purchase returns	xxx	xxx	By Closing stock of Fin. Goods		xxx
To Cost of production (from Manufacturing Account)		xxx	By Gross Loss c/d (tranf. to Profit & Loss a/c)		xxx
To Gross profit c/d (tranf. to Profit & Loss a/c)		xxx			
		xxx			xxx

Note: Balancing figure will be either gross profit or loss.

Closing Entries in Respect of Trading Account

The following entries are passed in the journal to transfer the relevant ledger balances to the trading account.

(i) For transferring opening stock, net purchases and direct expenses to trading account:

Trading a/c	Dr.	xxx	
To Opening stock a/c			xxx
To Purchases (net) a/c			xxx
To Direct expenses a/c			xxx

(ii) For transferring net sales and closing stock to trading account:

Sales (net) a/c	Dr.	xxx	
Closing stock a/c	Dr.	xxx	
To Trading a/c			xxx

(iii) (a) For gross profit

Trading a/c	Dr.	xxx	
To Gross profit a/c			xxx

(b) For gross loss

Gross loss a/c	Dr.	xxx	
To Trading a/c			xxx

PROFIT AND LOSS ACCOUNT

According to Prof. Carter, "profit and loss account is an account into which all gains and losses are collected in order to ascertain the excess of gains and losses or *vice versa*". Profit and loss account is prepared in order to calculate the net profit or net loss of the business. This account starts with the credit from the trading account in respect of gross profit (or debit if there is gross loss). From gross profit, operating and non-operating expenses are deducted and operating and non-operating income is added in order to calculate the net profit. When total of all the expenses is more than gross profit and other income, there remains a deficit and this is called net loss. The net profit or net loss ultimately transfers to capital account of the proprietor’s capital accounts.

Preparation of Profit and Loss Account

As in the case of a trading account, the profit and loss account is an account and hence, its form and construction conform to the rules of ledger account and principles of double entry system.

Since the profit and loss account is prepared to show the net profit earned or net loss incurred during a particular period, it should be headed as under:

Profit and Loss A/c of............ for the year ended........

Particulars	*(₹)*	*Particulars*	*(₹)*
To Gross loss b/d	xx	By Gross profit b/d	xx
To Office & Admin expenses:		By Interest received	xx
Office salaries	xx	By Discount received	xx
Rent, rates and taxes	xx	By Commission received	xx
Printing & stationery	xx	By Rent from tenants	xx
Postage & telegrams	xx	By Income from investments	xx
Telephone charges	xx	By Apprenticeship premium	xx
Legal charges	xx	By Interest on debentures	xx
Audit fees	xx	By Miscellaneous revenue receipts	xx
Insurance	xx	By Net loss transferred to Capital a/c	xx
General expenses	xx		
Office lightning	xx		
To Financial expenses:			
Interest on capital	xx		
Interest on loans	xx		
Discount allowed	xx		
Discount on bills	xx		
To Selling and Distribution Expenses:			
Advertising	xx		
Traveller's salaries	xx		
Expenses and commission	xx		
Bad debts	xx		
Godown rent	xx		
Carriage outwards	xx		
Agent's commission	xx		
Upkeep of motor vans	xx		
Export expenses	xx		
To Depreciation and Maintenance:	xx		
Depreciation	xx		

Repairs & maintenance	xx		
To Extraordinary expenses:			
Loss by fire (no covers by insurance)	xx		
Cash defalcations	xx		
To Net Profit transferred to Capital a/c	xx		

Items Appearing on Debit Side of Profit & Loss a/c: The business expenses are divided into two types. Direct expenses which are recorded in the Trading a/c and indirect expenses which are recorded in the debit side of profit & loss a/c. Indirect expenses can be further divided into two types:

(i) ***Operating Expenses:*** It refers to those expenses which are incurred in order to operate the business efficiently and smoothly. These include administration, selling, distribution, finance and maintenance expenses.

(ii) ***Non-operating Expenses:*** These expenses are not related to the operation of the business and include capital losses as loss on the sale of furniture, etc., writing off fictitious assets as preliminary expenses, underwriting commission, etc., writing off intangible assets as goodwill, copyright, patents etc.

Items Appearing on Credit Side of Profit & Loss a/c: Gross profit is shown on the credit side of profit & loss account. Also other gains and incomes of the business are shown on the credit side. The other incomes are generally classified into two types:

(a) ***Operating Income:*** It refers to that portion of income which is earned for the operations of the business. Examples, interest, commission and discount earned etc.

(b) ***Non-operating Income:*** This income is not earned from the routine operations of the, business. Examples are profit on sale of any fixed assets, refund of tax, etc.

Closing Entries for Profit & Loss a/c

(i) For transferring the various expenses to profit & loss a/c:

Profit and loss a/c Dr.

To Various expenses a/c

(ii) (a) For net profit:

P & L a/c Dr.

To Capital a/c

(b) For net loss:

Capital a/c Dr.

To P & L a/c

BALANCE SHEET

It is a classified summary of balances remaining open in the general ledger after all the income and expenditure accounts have been closed off by transfer to trading and profit & loss account. It shows readily the financial position of the business at a given date by disclosing the amount of capital contributed and how the same has been invested and the values of assets and liabilities and their nature. The capital and liabilities of the business are shown on the left hand side and assets and other debit balances are shown on the right hand side. It is a statement containing all the unclosed balance "real" and "personal" accounts.

Balance sheet is prepared with a view to measure the correct financial position of a business enterprise on a certain fixed date. It is a device for describing the financial position of a business in systematic standard form. By putting the financial position into such a form, it is possible to tell a complicated story of the enterprise in less time and space than if the same story were to be written as an extended narration. "Balance Sheet is a snapshot of the financial condition of the business". At one glance, the situation of the enterprise at certain date can be understood. Therefore, it is rightly called as "Mirror" of the business wherein the business can see its face, i.e., its true position.

An important thing to note about the balance sheet is that it always balances, that is to say, the total value of the assets is always equal to the total value of the claims or liabilities. In other words,

Assets = Liabilities + Capital (or)

Assets – Liabilities = Capital

In the other words of Francis R. Stead, "Balance sheet is a screen picture of the financial position of a going business at a certain moment."

According to R.N. Antony, "Balance sheet is a statement which reports the property values owned by the enterprise and the claims of the creditors and owners against the properties. It shows the status of the business as at a given moment of time, insofar as a counting of figures can show its status."

A Pro forma of balance sheet in the order of permanency is given below:

Balance Sheet of ....as on.....

Liabilities	*(₹)*	*Assets*	*(₹)*
Capital		***Fixed assets:***	
Add: Net profit		Goodwill	
Add: Interest on capital		Land & building	
Less: Drawings		Loose tools	
Less: Interest on drawings		Furniture & fixtures	
Less: Loss if any		Vehicles	
		Patents	
		Trademarks	

Long-term liabilities:		***Long-term loans (advances):***	
Loan on mortgage		Investments	
Bank loan		***Current assets:***	
Current liabilities:		Closing stock	
Sundry creditors		Sundry debtors	
Bills payable		Bills receivable	
Bank overdraft		Prepaid expenses	
Creditors for outstanding expenses		Accrued income	
Income received in advance		Cash at bank	
		Cash in hand	
		Fictitious assets:	
		Preliminary expenses	
		Advertising expenses	
		Underwriting commission	
		Discount on issue of shares	
		Discount on issue of debentures	

ADJUSTMENTS AND CLOSING ENTRIES

Final accounts are prepared for a completed period. It must be kept in mind that expenses and incomes for the full accounting period are to be taken while preparing final accounts. If an expense has been incurred but not paid during the period, a liability for the unpaid amount should be created before finding out the operating results and financial position of a concern. In order to prepare the final accounts on mercantile system of accountancy, all expenses and incomes relating to the period whether incurred or not, received or not should be brought into account. For doing this, a concern is required to pass certain entries at the end of the year to adjust the various items of incomes and expenses. Such entries are called adjusting entries. The various adjustments required are given below:

Closing Stock: It refers to the value of unsold goods lying in stock at the end of the accounting period. It should be valued either at cost price or market whichever is lower. It consists of three items, i.e., raw materials, work-in-progress and finished goods. The adjustment entry is:

Closing stock a/c	Dr.	xxx	
To Trading a/c			xxx

The value of closing stock will appear on the assets side of balance sheet and on the credit side of trading account.

Outstanding Expenses: These are certain expenses which relate to a particular accounting period but they are not paid in that accounting period due to certain reasons, i.e., all expenses which are due for payment in one accounting year but actually paid in future accounting years or payment on which is postponed are all outstanding or unpaid expenses. At the end of the accounting year, all such expenses must be brought into books, otherwise the profit will be overstated. The adjustment entry is:

Expenses a/c	Dr.	xxx	
To Expenses outstanding a/c			xxx

Expenses outstanding are added to the respective expenses account in trading or profit & loss a/c and also shown on the liabilities side of the balance sheet. Next year, the expenses outstanding account will be transferred to the expenses account.

If the outstanding expenses a/c appears in the trial balance, it means that the adjustment has already been made and hence nothing has to be done in trading or P & L account. But the liability already appearing in the trial balance should be shown in the balance sheet.

Prepaid Expenses: Prepaid expenses are those expenses which have been paid in advance but relating to the future accounting period. These are also called the unexpired expenses. The adjustment entry is:

Prepaid expenses a/c	Dr.	xxx	
To Expenses a/c			xxx

Prepaid expenses account is shown on the assets side of balance sheet and expenses account is shown as a deduction from the respective expenses account in trading and P & L a/c. If prepaid expenses appear in the trial balance, it means that the adjustments has already been made nothing is to be done in trading and P & L accounts. But the prepaid expenses will appear as an asset in the balance sheet. Generally, insurance, taxes, telephone subscription, etc., are paid in advance thus, requiring adjustments.

Accrued Income: Outstanding or accrued income is the income which has been earned but not received during the accounting period. The adjustment entry is:

Accrued income a/c	Dr.	xxx	
To Income a/c			xxx

Accrued income is shown on the assets side of balance sheet and it is added to the respective income account in P & L a/c credit side. No adjustment is required in the P & L a/c if accrued income a/c appears in the trial balance, but such an account must be shown as an asset in balance sheet.

Income Received in Advance: Many a time, traders receive money during a particular trading period for the work to be done in future period. Thus, without rendering any service, they receive income. Such an income is known as income received in advance, i.e., the income received but not earned during the accounting period. The adjustment entry is:

Income a/c	Dr.	xxx	
To Income received in advance a/c			xxx

Income received in advance is shown as deduction from the respective income in P & L a/c and is shown on the liabilities side of balance sheet. No treatment is required in the P & L account if income received in advance account appears in the trial balance. But such account must be shown as a liability in the balance sheet.

Depreciation of Assets: Depreciation is a permanent decrease or reduction in the value of a fixed asset. The asset may reduce in value due to its constant use or even sometimes due to its non-use, i.e., merely by passage of time. Whatever may be the cause for decline, the fact is that such reduction is a loss to the business. Therefore, it must be written off from the asset so as to arrive at the true results of the business. The adjustment entry for depreciation of assets is:

Depreciation a/c	Dr.	xxx	
To Asset a/c			xxx

Depreciation is shown on the debit side of profit and loss account and is deducted from the asset in the balance sheet. Depreciation account (Dr.) appearing in the trial balance has to be debited to profit and loss account and no deduction from asset balance is required because this has already been done.

Interest on Capital: In order to see the real profitability of the business, it is desirable to charge interest on capital treating it as a business expense. In order to bring this interest books, the following adjustment entry is passed:

Interest on capital a/c	Dr.	xxx	
To Capital a/c			xxx

Interest on capital is shown on the debit side of profit and loss account and is added to the capital on the liabilities side of balance sheet. Interest on capital account appearing in the trial balance is only to be shown in P & L a/c on debit side and it is not required to be included in capital account because this has been already included.

Interest on Drawings: When the proprietor withdraws money from the business for personnel use almost to temporary loan by the business to the proprietor. This should be treated on par with loan to an outsider from whom interest is receivable by the business. Therefore, the business charges the proprietor with interest on amounts drawn by him. Thus, interest on drawings is a business income. The following adjustment entry is to be passed to bring this item into account:

Capital a/c	Dr.	xxx	
To Interest on drawings a/c			xxx

Interest on capital is shown on the credit side of profit and loss account and it is deducted from the capital account on the liabilities side of balance sheet. Interest on drawings account appearing in the trial balance has to be transferred to profit and loss account on credit side alone.

Bad Debts: When a claim against a debtor becomes irrecoverable, it is called bad debt. If a person files a petition in bankruptcy, his creditors generally write-off the irrecoverable amount due as a bad debt. The entry in the books of the creditor is:

Bad debts a/c	Dr.	xxx	
To Debtor's a/c			xxx

Bad debts is shown on the debit side of P & L a/c and also deducted from debtors in the balance sheet. Alternatively, bad debts amount is closed by transfer to the debit of provision for bad & doubtful debts.

Provision for doubtful debts a/c	Dr.	xxx	
To Bad debts a/c			xxx

If the bad debt amount is recovered in future years, the cash is debited and bad debts recovered a/c is credited in that year. The balance in the later account is closed by transferring it to the credit of P & L a/c as revenue in that year. If the bad debt appears in the trial balance, it means that an adjustment has already been made and this will appear only on the debit side of the profit and loss account. It need not be reduced from debtors in the balance sheet.

Provision for Bad and Doubtful Debts: Sometimes, a merchant feels that there are certain debtors from whom the money may or may not be realizable. As there is a possibility of anticipated losses and in order to provide for such loss in the accounts, a provision for doubtful debts is required to be made. It is generally a percentage on the debtors and the percentage are fixed on the basis of past experience. The following adjusting entry will be made in order to bring the provision for doubtful debts into the books:

Profit and loss a/c	Dr.	xxx	
To Provision for doubtful debts a/c			xxx

This provision is shown as a deduction from existing debtors on the assets side of balance sheet.

If the net existing provision is in excess of required provision and bad debts, the excess should be credited back to profit and loss account with the following entry:

Provision for doubtful debts a/c	Dr.	xxx	
To Profit & loss a/c			xxx

In this case also, the amount of 'provision required' should be shown as a deduction from the existing debtors on the assets side of the balance sheet. The object of making the provision is to show the debtors on the balance sheet at a realizable value.

Sometimes, bad debts may be written off during the year. Some additional bad debts are to be written off at the time of finalizing accounts. There may be existing provision for doubtful debtors (old provision). Provision is required on the debtors as on the closing date. The following is the usual way of dealing with all these items:

Profit & loss a/c (debit side)

Bad debts (as per trial balance)	xxx
Add: Bad debts (as per adjustments)	xxx

Add: New provision required	xxx	
	----	
	xxx	
Less: Existing provision (given in trial balance)	xxx	
Net debit to P & L a/c	----	xxx

The new provision required is to be reduced from the debtors in the balance sheet along with additional bad debts as per adjustments.

Provision for Discount on Debtors: The provision for discount on debtors is calculated at a certain percentage on good debtors. No discount is allowed on doubtful debtors. This is to provide a certain amount for allowing discount to customers for prompt payment. The adjustment entry is:

Profit & loss a/c	Dr.	xxx	
To Provision for discount on debtors a/c			xxx

The provision for discount on debtors is shown as a deduction from good debtors on the assets side of balance sheet and is debited to profit and loss account.

Provision for Discount on Creditors: The creditors may offer some discount for prompt payment by the firm. This is calculated at a certain percentage on sundry creditors. The adjustment entry is:

Provision for discount on creditors a/c	Dr.	xxx	
To Profit & loss a/c			xxx

The provision for discount on creditors is shown as a deduction from sundry creditors on the liabilities side of balance sheet and is credited to P & L A/c.

Loss of Stock by Accident, Fire etc.: Stock of goods destroyed due to abnormal causes must be treated as abnormal loss. If there is no insurance, the entire stock lost should be treated as abnormal loss. The entry is:

Abnormal loss a/c	Dr.	xxx	
To Trading a/c			xxx

Since there will be no recovery, the abnormal loss has to be closed.

Profit & loss a/c	Dr.	xxx	
To Abnormal loss a/c			xxx

If there is insurance, amount recoverable from insurance company has to be debited to insurance company and the balance of abnormal loss is written off to P & L a/c.

Profit & loss a/c	Dr.	xxx	
Insurance company a/c	Dr.	xxx	
To Abnormal loss a/c			xxx

Illustration 1: Prepare Trading Account of Archana for the year ending 30-12-15 from the following information:

Particulars	*(₹)*
Opening stock	80,000
Purchases	8,60,000
Freight inward	52,000
Wages	24,000
Sales	14,40,000
Purchase Returns	10,000
Sales Returns	3,16,000
Closing stock	1,00,000
Import duty	30,000

Solution:

Trading Account of Archana for the year ending 30-12-2015

Particulars		*(₹)*	*Particulars*		*(₹)*
To Opening stock		80,000	By Sales	14,40,000	
To Purchases	8,60,000		***Less:*** Sales returns	3,16,000	11,24,000
Less: Purchase returns	10,000	8,50,000	By Closing stock		1,00,000
To Freight inward		52,000			
To Wages		24,000			
To Import duty		30,000			
To Gross Profit c/d		1,88,000			
		12,24,000			**12,24,000**

Illustration 2: From the following particulars, prepare Manufacturing account for the year ended 31st March, 2016.

Raw materials (1-4-2015)	33,000
Work-in-progress (1-4-2015)	17,000
Finished goods (1-4-2015)	27,000
Purchases:	
Raw materials	1,00,000
Finished goods	10,000
Carriage inwards:	
on Raw materials	2,500
on Finished goods	100
Purchases returns:	
on Raw materials	5,000
on Finished goods	200

Freight & octroi:

on Purchases of Raw materials	500
on Purchases of Finished goods	100
Sales:	
Sales of scrap	150
Sales of Finished goods	3,00,000
Rent (3/4th for factory)	4,000
Insurance (20% for factory)	1,000
Productive wages	6,000
Repairs to building (40% on office building)	1,000
Depreciation on machinery	2,100
Factory supervisor's salary	2,400
Manager's salary (1/4th for factory)	5,000
Raw materials (31-3-2016)	22,000
Work-in-progress (31-3-2016)	13,500
Finished goods (31-3-2016)	40,000

Solution:

Manufacturing account for the year ended 31-3-2016

Particulars	(₹)	(₹)	*Particulars*	(₹)	(₹)
To Opening stock			By Sales of scrap		150
Raw materials (1-4-2008)	33,000		By Cost of production		1,27,900
Work-in-progress (1-4-2008)	17,000	50,000	(trfd to trading a/c (b/f))		
To Purchases of:			By Closing stock		
Raw materials	1,00,000		Raw materials	22,000	
Less: Purchases returns	5,000	95,000	Work-in-progress	13,500	35,500
To Carriage inwards		2,500			
To Freight & octroi		500			
To Rent (3/4th for factory)		3000			
To Insurance (20% for factory)		200			
To Productive wages		6,000			
To Repairs to building (60%)		600			
To Depreciation on machinery		2,100			
To Factory supervisor's salary		2,400			
To Manager's salary (1/4th)		1,250			
		1,63,550			**1,63,550**

Illustration 3: From the following balance extracted at the close of the year ended 31st Dec. 2015, prepare profit and loss account of Mr. Raj as at that date:

Particulars	*(₹)*	*Particulars*	*(₹)*
Gross profit	55,000	Repairs	500
Carriage on sale	500	Telephone expenses	520
Office rent	500	Interest (Dr.)	480
General expenses	900	Fire insurance premium	900
Discount to customers	360	Bad debts	2,100
Interest from Bank	200	Apprentice premium (Cr.)	1,500
Travelling expenses	700	Printing & Stationery	2,500
Salaries	900	Trade expenses	300
Commission	300		

Solution:

Profit & Loss Account of Mr. Raj for the year ending 30-12-2015

Particulars	*(₹)*	*Particulars*	*(₹)*
To Carriage on sales	500	By Gross profit b/d	55,000
To Office rent	500	By Bank Interest	200
To General expenses	900	By Apprentice Premium	1,500
To Discount to customers	36		
To Travelling expenses	700		
To Salaries	900		
To Commission	300		
To Repairs	500		
To Telephone expenses	520		
To Interest paid	480		
To Fire Insurance Premium	900		
To Bad debts	2,100		
To Printing & stationery	2,500		
To Trade expenses	300		
To Net Profit transferred to Capital a/c	45,240		
	56,700		**56,700**

Illustration 4: The following are the balances in the Ledger of Mr. Sherif for the year ended 31st March, 2016.

Opening stock [1/4/2015]	
Raw materials	20,000
Work-in-progress	3,000
Finished goods	10,800
Purchase of raw materials	50,000
Sales	2,40,000
Fuel and coal	1,000
Wages	32,000
Factory expenses	40,000
Office expenses	30,000
Depreciation on Plant & Machinery	3,000
Closing Stock [31/3/2016]	
Raw materials	2,000
Work-in-progress	4,000
Finished goods	8,000

Prepare Manufacturing and Trading Account for the year ended 31st March, 2016.

Solution:

Manufacturing and Trading Account of Mr. Sherif for the year ending 31.3.16

Particulars	(₹)	(₹)	*Particulars*	(₹)	(₹)
To Opening work-in-progress		3,000	By Closing work-in-progress		4,000
To Cost of Materials consumed Opening stock	20,000		By Cost of goods manufactured transferred to Trading a/c		143000
Add: Purchases	50,000				
	70,000				
Less: Closing stock	20,000	68,000			
To Wages		32,000			
To Fuel & Coal		1,000			
To Factory expenses		40,000			
To Depreciation on Plant & machinery		3,000			
		1,47,000			1,47,000
To Opening stock of finished goods		10,800	By Sales		2,40,000
To Cost of goods manufactured		1,43,000	By Closing stock		
To Gross Profit c/d		94,200	of finished goods		8.000
		2,48,000			**2,48,000**

Illustration 5: From the following adjusted Trial Balance, prepared after Trading and Profit & loss Accounts are drafted, prepare Balance Sheet of Ramagopalan as at 31st December, 2015 under:

Particulars	*Dr. (₹)*	*Cr. (₹)*
Capital		1,00,000
Closing stock	40,000	-
Fixed assets (less depreciation ₹ 16,000)	72,000	-
Sundry debtors	1,00,000	-
Provision for bad debts	-	5,000
Profit & loss account	-	42,000
Sundry creditors	-	80,000
Liabilities for expenses	-	11,000
Drawings	6,000	
Cash & Bank	20,000	
	2,38,000	2,38,000

Solution:

Balance Sheet of Ramagopalan as on 30-12-15

Liabilities	*(₹)*	*(₹)*	*Assets*	*(₹)*	*(₹)*
Capital (opening balance)	1,00,000		Fixed assets	88,000	
Add: Net profit	42,000		*Less:* Depreciation	16,000	72,000
	1,42,000		Stock		40,000
Less: Drawings	6,000	1,36,000	Debtors	1,00,000	
Sundry Creditors		80,000	*Less:* Provision for bad debts	5,000	95,000
Liabilities for expenses		11,000	Cash & bank		20,000
		2,27,000			**2,27,000**

Illustration 6: The following is the trial balance of Dhandapani of Madras as on 31st December, 2015:

Particulars	*(₹)*	*Particulars*	*(₹)*
Debit balances:		***Credit balances:***	
Opening stock	6,200	Sales	82,920
Buildings	34,000	Capital	24,000
Furniture	2,000	Bank loan	6,000
Purchases	42,400	Sundry creditors	9,840
Salaries	4,400	Return outwards	840
Rent	1,200	Interest	260
Miscellaneous expenses	1,000	Dividend	220

Postage	560		
Stationery	520		
Wages	10,400		
Freight on purchases	1,120		
Carriage on sales	1,600		
Repairs	1,800		
Sundry debtors	12,000		
Bad debts	240		
Cash in hand	2,600		
Return inwards	2,040		
	1,24,080		**1,24,080**

The value of stock on 31-12-2015 was estimated at ₹ 5960. You are required to make the necessary closing and prepare Trading and Profit & Loss account and a Balance Sheet as on 31st December, 2015.

Solution:

Date	*Particulars*		*Dr.*	*Cr.*
2015	Trading a/c	Dr.	62,160	
	To Opening stock a/c			6,200
	To Purchases a/c			42,400
	To Wages a/c			10,400
	To Return Inwards a/c			2,040
	To Freight on purchase a/c			1,120
	(Being transfer)			
	Sales a/c	Dr.	82,920	
	Return outwards a/c	Dr.	840	
	To Trading a/c			83,760
	(Being transfer)			
	Closing stock a/c	Dr.	5,960	
	To Trading a/c			5,960
	(Being incorporation of closing stock in trading a/c)			
	Trading a/c	Dr.	27,560	
	To Profit & loss a/c			27,560
	(Being gross profit transferred)			
	Profit & loss a/c	Dr.	11,320	
	To Salaries a/c			4,400
	To Rent a/c			1,200
	To Miscellaneous expenses a/c			1,000

	To Postage a/c			560
	To Stationery a/c			520
	To Carriage on sales a/c			1,600
	To Repairs a/c			1,800
	To Bad debts a/c			240
	(Being the various expenses transferred)			
	Interest a/c	Dr.	260	
	Dividend a/c	Dr.	220	
	To Profit & loss a/c			480
	(Being interest and dividend transferred)			
	Profit & loss a/c	Dr.	16,720	
	To Capital a/c			16,720
	(Being net profit transferred)			

Trading and P & L a/c of Dhandapani for the year ending 31-12-15

Particulars		(₹)	*Particulars*		(₹)
To Opening stock		6,200	By Sales	82,920	
To Purchases	42,400		***Less:*** Return inwards	2,040	80,880
Less: Return outwards	840	41,560	By Closing stock		5,960
To Wages		10,400			
To Freight on purchase		1,120			
To Gross profit c/d		27,560			
		86,840			**86,840**
To Salaries		4,400	By Gross profit b/d		27,560
To Rent		1,200	By Interest		260
To Miscellaneous expenses		1,000	By Dividend		220
To Postage		560			
To Stationery		520			
To Carriage on sales		1,600			
To Repairs		1,800			
To Bad debts		240			
To Net profit transferred to Capital a/c		16,720			
		28,040			**28,040**

Balance Sheet of Dhandapani as on 31-12-15

Liabilities		***(₹)***	***Assets***	***(₹)***
Sundry Creditors		9,840	Cash in hand	2,600
Bank loan		6,000	Sundry debtors	12,000
Capital A/c			Stock	5,960
Balance	24,000		Furniture	2,000
Add: Net profit	16,720	40,720	Buildings	34,000
		56,560		**56,560**

Illustration 7: Pass necessary adjustment entries for the following adjustment:

(a) Depreciation at 10% is to be charged on machinery standing in the books at ₹ 1,00,000.

(b) Insurance unexpired is ₹ 200.

(c) Salaries outstanding ₹ 10,000.

(d) To provide provision for doubtful debts at 2% on sundry debtors worth ₹ 20,000.

(e) Closing stock ₹ 55,000.

(f) Interest has accrued on investment ₹ 500.

(g) Commission received in advance ₹ 1,000.

(h) To provide 10% interest on capital of ₹ 2,50,000.

(i) Interest charged on drawings of ₹ 520.

(j) The proprietor has withdrawn goods worth ₹ 200 from stock.

(k) Goods in stock worth ₹ 8,000 are destroyed by fire. Insurance company accepts the claim of ₹ 6,000.

(l) ₹ 2,000 to be transferred to Reserve fund.

(m) Goods worth ₹ 2,000 distributed as free samples to customers.

Solution:

Adjustments Entries

Particulars		***Dr.***	***Cr.***
(a) Depreciation a/c	Dr.	10,000	
To Machinery a/c			10,000
(Being depreciation on machinery)			
(b) Prepaid insurance a/c	Dr.	200	
To Insurance a/c			200
(Being insurance prepaid)			
(c) Salaries a/c	Dr.	10,000	
To Outstanding salaries a/c			10,000
(Being salaries outstanding)			

(d)	Profit & loss a/c	Dr.	400	
	To Provision for doubtful debts a/c			400
	(Being creating provision for doubtful debts)			
(e)	Closing stock a/c	Dr.	55,000	
	To Trading a/c			55,000
	(Being bringing stock into account)			
(f)	Accrued interest a/c	Dr.	500	
	To Interest a/c			500
	(Being interest accrued on investment)			
(g)	Commission a/c	Dr.	1,000	
	To Commission received in advance a/c			1,000
	(Being commission received in advance)			
(h)	Interest on capital a/c	Dr.	25,000	
	To Capital a/c			25,000
	(Being interest on capital)			
(i)	Capital a/c	Dr.	520	
	To Interest on drawings a/c			520
	(Being interest charged on drawings)			
(j)	Drawings a/c	Dr.	200	
	To Purchases a/c			200
	(Being goods taken from business for personal use)			
(k)	Abnormal loss account a/c	Dr.	8,000	
	To Trading a/c			8,000
	(Being abnormal loss credited to trading a/c)			
(l)	Insurance company a/c	Dr.	6,000	
	Profit & loss a/c	Dr.	2,000	
	To abnormal loss a/c			8,000
	(Being stock destroyed admitted by insurance company to the extent of ₹ 6,000)			
(m)	Profit & loss a/c	Dr.	2,000	
	To Reserve fund a/c			2,000
	(Being transferring to reserve fund)			
(n)	Advertising a/c	Dr.	2,000	
	To Purchase a/c			2,000
	(Being goods distributed as free sample)			

Illustration 8: The sundry debtors on 31st Dec. 2015 are ₹ 40,000. On analysis, it is found that debtors for ₹ 36,000 are good. The debtors for ₹ 3,000 are doubtful and are estimated to realize 2/3rds of the amount and the doubts for ₹ 1,000 are bad. Make a provision for doubtful debts. Show the journal, profit & loss a/c and Balance Sheet.

Solution:

Journal

Dr. **Cr.**

Date	*Particulars*	(₹)	(₹)
2015 Dec. 31	Profit & loss a/c Dr.	2,000	
	To Provision for bad debts & doubtful debts a/c		2,000
	(Being amount of provision for bad debts & doubtful debts – 1/3rd of ₹ 3,000, i.e., ₹ 1,000 doubtful and ₹ 1,000 bad)		

Ledger

Provision for bad debts & doubtful debts a/c

Dr. **Cr.**

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
2015					
Dec. 31	To Balance b/d	2,000	2015 Dec. 31	By Profit & loss a/c	2,000
		2,000			**2,000**
			2016 June 1	By Balance b/d	2,000

Profit & loss a/c for the year ended 31-12-15

Dr. **Cr.**

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
	To Provision for doubtful debts	2,000			
		2,000			2,000

Balance Sheet as on 31-12-2015

Liabilities	(₹)	*Assets*		(₹)
		Sundry debtors	40,000	
		Less: Provision for bad	2,000	
	38,000	and doubtful debts		**38,000**

Illustration 9: The provision for bad and doubtful debts account shows a balance of ₹ 2,000 on 1st January 2015. The bad debts during the year 2015 amount to ₹ 1,600. The sundry debtors on 31st December 2016 are ₹ 32,000. Create a new provision for bad debts @ 5%. Show the journal, ledger, profit & loss account and balance sheet.

Solution:

Journal

Dr. Cr.

Date	*Particulars*	(₹)	(₹)
2015 Dec. 31	Provision for bad debts & doubtful debts a/c Dr. To Bad debts a/c (Being transfer of bad debts)	1,600	 1,600
	Profit & loss a/c Dr. To Provision for bad debts & doubtful debts a/c (Being amount of additional reserve required to raise it to ₹ 1,600)	1,200	 1,200

Ledger

Bad debts a/c

Dr. Cr.

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
2015 Dec. 31	To Balance b/d	1,600	2015 Dec. 31	By Provision for bad debts & doubtful debts a/c (transfer)	1,600
		1,600			**1,600**

Provision for bad debts and doubtful debts a/c

Dr. Cr.

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
31-12-15	To Bad debts a/c	1,600	1-1-15	By Balance b/d	2,000
31-12-15	To Balance c/d	1,600	31-12-15	By Profit & loss a/c	1,200
		3,200			**3,200**
			1-1-16	By Balance b/d	1,600

Profit & loss a/c for the year ended 31-12-15

Particulars	(₹)	(₹)	*Particulars*	(₹)	(₹)
To Bad debts	1,600				
Add: New provision for bad debts	1,600				
	3,200				
Less: Existing provision for bad debts	2,000	1,200			

Balance Sheet as on 31-12-15

Liabilities	(₹)	*Assets*		(₹)
		Sundry debtors	32,000	
		Less: Provision for bad debts	1,600	30,400

Illustration 10: The provision for bad and doubtful debts shows a balance of ₹ 1,600 on 1st January 2015. The bad debts during the year 2015 amount to ₹ 600. The sundry debtors on 31st December 2015 are ₹ 16,000. Create a provision of 5% for bad and doubtful debts.

Solution:

Journal

Dr. **Cr.**

Date	*Particulars*	(₹)	(₹)
2015 Dec. 31	Provision for bad debts & doubtful debts a/c Dr.	600	
	To Bad debts a/c		600
	(Being transfer of bad debts)		
Dec. 31	Provision for bad & doubtful debts a/c Dr.	200	
	To Profit & loss a/c		200
	(Being amount credited back to P & L a/c to reduce old reserve from (1,600 – 1,600), i.e., 1,000 to 800)		

Ledger

Bad debts a/c

Dr. **Cr.**

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
2015 Dec. 31	To Balance b/d	600	2015 Dec. 31	By Provision for bad & doubtful debts a/c (transfer)	600
		600			**600**

Provision for bad & doubtful debts a/c

Dr. **Cr.**

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
2015 Dec. 31	To Bad debts	600	2015 Jan. 1	By Balance b/d	1,600
Dec. 31	To P&L a/c	200			
	To Balance c/d	800			
		1,600			**1,600**

Profit & Loss a/c for the year ended 31-12-15

Dr. **Cr.**

Particulars	(₹)	(₹)	*Particulars*	(₹)	(₹)
			By Provision for bad & doubtful debts (old)	1,600	
			Less: Bad debts 600		
			New provision 800	1,400	200

Balance Sheet as on 31-12-15

Liabilities	(₹)	(₹)	*Assets*	(₹)	(₹)
			Sundry Debtors	16,000	
			Less: Provision for B.D.	800	15,200

Illustration 11: The following particulars are extracted from the books of Kalyani.

2015		₹	
Jan. 1	Provision for bad & doubtful debts	12,000	
	Provision for discount on debtors	5,600	
Dec. 31	Provision allowed during the year	9,300	
	Bad debts written off during the year		4,700
	Bad debts recovered during the year		250
	Debtors		1,00,600

Write-off further ₹ 2,400 (definitely bad). Provision for discount allowed at 2% and for doubtful debts 10% are to be maintained.

Show how the relevant items would appear in ledger, P & L a/c and balance sheets as on Dec. 31, 2015.

Solution:

Bad debts a/c

Dr. **Cr.**

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
2015			2015		
Dec. 31	To Balance b/d	4700	Dec. 31	By Provision for Bad Debts a/c	7100
Dec. 31	To Sundry debtors a/c	2400			

Provision for bad & doubtful debts a/c

Dr. **Cr.**

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
2015			2015		
Dec. 31	To Bad debts a/c	7,100	Jan. 1	By Balance b/d	12,000
	To Balance c/d	9,820	Dec. 31	By P & L (bal. fig. a/c)	4,920
		16,920			**16,920**
			2016		
			Jan. 1	By Balance b/d	9,820

Bad debts recovered a/c

Dr. **Cr.**

Date	*Particulars*	(₹)	*Date*	*Particulars*	(₹)
2015			2015		
Dec. 31	To Profit & loss a/c	250	Dec. 31	By Balance b/d	250
		250			**250**

Discount on Debtors a/c

Dr. Cr.

Date	Particulars	(₹)	Date	Particulars	(₹)
2015 Dec. 31	To Balance b/d	9,300	2015 Dec. 31	By Provision for discount on debtors a/c	9,300
		9,300			**9,300**

Provision for discount on debtors a/c

Dr. Cr.

Date	Particulars	(₹)	Date	Particulars	(₹)
2015 Dec. 31	To Discount on debtors a/c	9,300.00	2015 Jan. 1	By Balance b/d	5,600.00
	To Balance c/d	1,767.60	Dec. 31	By P & L a/c	5,467.60
		11,067.60			**11,067.60**
			2016 Jan. 1	By Balance b/d	1,767.60

Working Note:

Debtors	1,00,600
Less: FBD	2,400
	98,200
Less: New RDD 10%	9,820
	88,380
Less: Provision for Discount Debt	1,768
	86,612

Profit & loss a/c for the year ended 31-12-15

Dr. Cr.

Particulars	(₹)	(₹)	Particulars	(₹)	(₹)
To Provision for bad debts.			By Bad debts recovered		250
Provision required	9,820				
Add: Bad debts	7,100				
	16,920				
Less: Existing provision	12,000	4,920			
To Provision for discount on debtors					
Provision required	1,768				
Add: Discount allowed	9,300				
	11,068				
Less: Existing provision	5,600.00	5,468			

Balance Sheet as on 31-12-15

Liabilities	(₹)	(₹)	Assets	(₹)	(₹)
			Sundry debtors	1,00,600	
			Less: Bad debts	2,400	
				98,200	
			Less: Provision for bad debts	9,820	
				88,380	
			Less: Provision for discount	1,768	86,612

Illustration 12: The following is the schedule of balance on 31-3-2015 extracted from the books of Manikandan.

Cash in hand	22,800	Capital account	3,24,000
Cash at bank	5,200	Discount received from creditors	3,200
Sundry debtors	1,72,000	Purchase returns	5,200
Stock as on 1-4-14	1,24,000	Sales	4,60,000
Furniture & fixtures	42,800	Provision for bad debts	6,000
Office equipments	3,200	Loan from Gopu	60,000
Buildings	1,20,000	Sundry creditors	1,06,000
Motor car	40,000		
Purchases	2,80,000		
Sales returns	8,400		
Salaries	22,000		
Rent for godown	11,000		
Interest on loan from Gopu	5,400		
Rates and taxes	4,200		
Discount allowed to debtors	4,800		
Freight on purchases	2,400		
Carriage outwards	4,000		
Drawings	24,000		
Printing & stationery	3,600		
Electric charges	4,400		
Insurance premium	11,000		
General office expenses	6,000		
Bad debts	4,000		
Bank charges	3,200		
Motor car expenses	7,200		
	9,64,400		**9,64,400**

Prepare trading and profit and loss a/c for the year ended 31-3-2015 and the balance sheet as at that date after making provision for the following:.

(i) Value of stock on 31-3-2015 was ₹ 88,000.

(ii) One month's rent for godown is outstanding.

(iii) One month's salary is outstanding.

(iv) Interest on loan from Gopu is payable at 12%. This loan was taken on 1-5-2015.

(v) A provision for bad debt is to be maintained at 5% on Sundry Debtors.

(vi) Insurance premium includes ₹ 8,000 paid towards proprietor's life insurance policy and the balance of the insurance charges covers the period from 1-4-16 to 30-6-16.

(vii) Depreciate:

(a) Buildings used for business by 5%.

(b) Furniture & fixtures by 10%. One steel table purchased during the year for ₹ 2,800 was sold for same price but the sale proceeds were wrongly credited to Sales a/c.

(c) Office equipments by 15%. Purchase of a typewriter during the year for ₹ 8,000 has been wrongly debited to Purchase a/c.

(d) Motor car by 20%.

Solution:

Trading and Profit & Loss a/c of Manikandan for the year ended 31-3-15

Particulars	(₹)	(₹)	*Particulars*	(₹)	(₹)
To Opening stock		1,24,000	By Sales	4,60,000	
To Purchases	2,80,000		***Less:*** Sale of fittings	2,800	
Less: Purchase of office equipment	8,000			4,57,200	
	2,72,000		***Less:*** Returns	8,400	44,88,000
			By Closing stock		8,800
Less: Returns	5,200	2,66,800			
To Freight on purchases		2,400			
To Gross Profit c/d		1,43,600			
		536,800			**5,36,800**
To Salaries	22,000		By Gross profit b/d		1,43,600
Add: Outstanding	2,000	24,000	By Discount received		3,200
To Rent for godown	11,000				
Add: Outstanding	1,000	12,000			
To Interest on loan	5,400				
Add: Outstanding	1,200	6,600			
To Rates & taxes		4,200			
To Discount allowed		4,800			
To Carriage outward		4,000			
To Printing & stationery		3,600			
To Electric charges		4,400			
To Insurance premium	11,000				
Less: Premium on own life policy	8,000				
	3,000				
Less: Prepaid	3,000	Nil			
To General office expenses		6,000			
To Bad debts	4,000				
Add: New provision	8,600				
	12,600				
Less: Existing provision	6,000	6,600			
To Bank charges		3,200			
To Motor car expenses		7,200			
To Depreciation on:					
Building		3,000			
Furniture & fittings		4,000			
Office equipments		6,000			
Motor car		8,000			
To Net profit transferred to Capital a/c		39,200			
		1,46,800			**1,46,800**

Balance Sheet as on 31.3.15

Liabilities	**(₹)**	**(₹)**	***Assets***	**(₹)**	**(₹)**
Capital	3,24,000		Buildings	1,20,000	
Add: Net profit	39,200		***Less:*** Depreciation	3,000	1,17,000
	3,63,200				
Less: Drawings			Furniture & fittings	42,800	
(24,000 + 8,000)	32,000	3,31,200	***Less:*** Sale	2,800	
Loan from Gopu	60,000			40,000	
Add: Outstanding interest	1,200	61,200	***Less:*** Depreciation	4,000	36,000
Sundry creditors		1,06,000	Office equipments	32,000	
Outstanding expenses:			***Add:*** Purchase	8,000	
Salaries	2,000			40,000	
Rent for godown	1,000	3,000	***Less:*** Depreciation	6,000	34,000
			Motor car	40,000	
			Less: Depreciation	8,000	32,000
			Stock		88,000
			Sundry debtors	1,72,000	
			Less: Provision for B.D.	8,600	1,63,400
			Cash at Bank		5,200
			Cash at Hand		22,800
			Prepaid Insurance		3,000
		5,01,400			**5,01,400**

Illustration 13: From the following particulars presented by Mr. S. Tendulkar, prepare a Trading a/c, Profit & Loss a/c for the year ended 31st Dec. 2015 and Balance sheet as on that date.

Debit balances	**(₹)**	***Credit balances***	**(₹)**
Plant & machinery	1,00,000	Sales (net)	4,00,000
Drawings	36,000	Capital	1,00,000
Purchases	1,20,000	Creditors	40,000
Sundry debtors	80,000	Bank overdraft	20,000
Wages	20,000	Provision for debts	4,000
Carriages	6,000	Cash credit	20,000
Salaries	14,000	Bills payable	16,000
Rent	12,000		
Repairs	6,000		
Insurance	10,000		
Opening stock	24,000		
Land & buildings	80,000		

Furniture	20,000		
Discount	40,000		
Suspense A/c	32,000		
	6,00,000		**6,00,000**

Adjustment:

(i) Closing stock ₹ 60,000.

(ii) Purchases include purchase of materials used for the construction of buildings ₹ 10,000.

(iii) Sales include sale of furniture at a selling prices of ₹ 2,000 (book value ₹ 4,000).

(iv) Purchased a plant for ₹ 10,000, wrongly debited to purchases a/c.

(v) A sale of goods to a customer not debited to customers account ₹ 32,000

(vi) Stock destroyed by fire amounted ₹ 20,000. Insurance company admitted only ₹ 16,000 as its liability.

(vii) Wages include ₹ 6,000 incurred for the erection of machinery.

(viii) The proprietor Mr. S. Tendulkar took goods for his own from the business amounted to ₹ 2,000.

(ix) Rent included ₹ 2,000 paid for Mrs. S. Tendulkar's residential portion.

(x) Purchase of stationery for ₹ 200 was debited to Repairs a/c.

(xi) A customer's cheque returned dishonoured wrongly debited to Discount a/c ₹ 2,000.

Solution:

Trading and Profit & Loss a/c of S. Tendulkar for the year ended 31-12-15

Particulars	**(₹)**	**(₹)**	***Particulars***	**(₹)**	**(₹)**
To Opening stock		24,000	By Sales	4,00,000	
To Purchases	1,20,000		***Less:*** Furniture	2,000	3,98,000
Less: Buildings	10,000		By Closing stock		60,000
	1,10,000		By Stock destroyed by fire		20,000
Less: Drawings	2,000				
	1,08,000				
Less: Plant & Machinery	10,000	98,000			
To Wages	20,000				
Less: Plant & Machinery	6,000	14,000			
To Carriage		6,000			
To Gross profit c/d		3,36,000			
		4,78,000			**4,78,000**

To Salaries		14,000	By Gross profit b/d		3,36,000
To Rent	12,000		By Provision for bad debts		4,000
Less: Drawings	2,000	10,000			
To Repairs	6,000				
Less: Stationery	200	5,800			
To Insurance		10,000			
To Discount	40,000				
Less: Cheque dishonoured	2,000	38,000			
To Loss on sale of furniture		2,000			
To Stationery		200			
To Loss of stock by fire		4,000			
To Net profit transferred to Capital a/c		2,56,000			
		3,40,000			**3,40,000**

Balance Sheet of Mr. S. Tendulkar as on 31-12-15

Liabilities		***(₹)***	***(₹)***	***Assets***	***(₹)***	***(₹)***
Capital		1,00,000		Plant & Machinery	1,00,000	
Add: Net profit		2,56,000		***Add:*** Wages	6,000	
		3,56,000			1,06,000	
Less: Drawings		36,000		***Add:*** Additions	10,000	1,16,000
Purchases	2,000			Land & Buildings	80,000	
Rent	2,000	4,000	3,16,000	***Add:*** Additions	10,000	90,000
Creditors			40,000	Furniture	20,000	
Bank Overdraft			20,000	***Less:*** Sale of furniture	4,000	16,000
Cash credit			20,000	Stock		60,000
Bills Payable			16,000	Sundry debtors	80,000	
				Add: Cheque dishonoured	2,000	
					82,000	
				Add: Suspense a/c	32,000	1,14,000
				Suspense a/c	32,000	
				Less: Debtors	32,000	Nil
				Insurance claim		16,000
			4,12,000			**4,12,000**

Illustration 14: The following figures have been extracted from the records of Fancy Stores, a proprietor concern as at 31st December 2015.

Particulars	*(₹)*	*Particulars*	*(₹)*
Furniture	15,000	Insurance	60,000
Capital	5,40,000	Rent	2,20,000
Cash in hand	30,000	Sundry Debtors	6,00,000
Opening stock	5,00,000	Sales	60,00,000
Fixed Deposits	13,46,000	Advertisements	1,00,000
Drawings	50,000	Postage & telephone	34,000
Provision for bad debts	30,000	Bad debts	20,000
Cash at Bank	1,00,000	Printing & stationery	90,000
Purchases	30,00,000	General charges	1,30,000
Salaries	1,90,000	Sundry creditors	4,00,000
Carriage Inwards	4,10,000	Deposit from customers	60,000

Prepare Trading & Profit & Loss a/c and Balance Sheet after taking into consideration the following further information:

(i) The closing stock as on 31-12-2015 was ₹ 1,00,000.

(ii) A sale of ₹ 2,50,000 made for cash had been credited to the Purchases a/c.

(iii) Salary of ₹ 20,000 paid to an employee had been entered in the cash book bank column as ₹ 10,000.

(iv) Charge depreciation on furniture at 10%.

(v) Furniture had been sold during the year for ₹ 1,00,000 and the proceeds had been credited to furniture account. The written down value of furniture sold was ₹ 50,000.

(vi) A sum of ₹ 1,00,000 received from a party which had purchased some stock belonging to a separate business of the proprietor was credited to the Sundry debtors account.

(vii) The proceeds of a matured fixed deposits amounting to ₹ 2,54,000 had been credited to the fixed deposit account. The original amount of the deposit was ₹ 2,00,000.

(viii) There was an outstanding liability for rent of ₹ 20,000.

(ix) An advance of ₹ 10,000 paid to an employee against his salary of January 2016 had been debited to the Salary a/c.

(x) The office premises were sublet from December 2010 for a monthly rental of ₹ 10,000, but the rent for December has not yet been received.

Solution:

Trading and Profit & Loss a/c of Fancy Stores for the year ended 31-12-15

Particulars	*(₹)*	*(₹)*	*Particulars*	*(₹)*	*(₹)*
To Opening Stock		5,00,000	By Sales		62,50,000
To Purchases		32,50,000	By Closing Stock		1,00,000
To Carriage Inwards		4,10,000			
To Gross profit c/d		21,90,000			
		63,50,000			**63,50,000**
To Salaries	19,000		By Gross Profit b/d		21,90,000
Add: Under recording in Cash book	10,000		By Interest on deposit		54,000
	20,000		By Rent from subletting		10,000
Less: Advance Salary	10,000	19,000	By Profit on sale of furniture		50,000
To Insurance		60,000			
To Rent		2,40,000			
To Advertisement		1,00,000			
To Postage & telephone		34,000			
To Bad debts		20,000			
To Printing & stationery		90,000			
To General charges		1,30,000			
To Depreciation on furniture		20,000			
To Net profit transferred to Capital a/c		14,20,000			
		23,04,000			**23,04,000**

Balance Sheet of Fancy Stores as on 31-12-15

Liabilities	*(₹)*	*(₹)*	*Assets*	*(₹)*	*(₹)*
Deposits from customers		60,000	Cash in hand		30,000
Sundry creditors		4,00,000	Cash in Bank (1,00,000 – 10,000)		90,000
Outstanding Rent		20,000	Stock		1,00,000
Capital	5,40,000		Sundry debtors	7,00,000	
Add: Addition	1,00,000		***Less:*** Provision for B.D.	30,000	6,70,000
	6,40,000		Advance Salary		10,000
Less: Drawings	50,000		Rent outstanding		10,000
	5,90,000		Furniture	2,00,000	
Add: Net Profit	14,20,000	20,10,000	***Less:*** Depreciation	20,000	1,80,000
			Fixed Deposits		14,00,000
		24,90,000			**24,90,000**

Illustration 15: Sasikala is a manufacturer. From the following details, prepare:

(i) Sasikala's manufacturing account to show the cost of goods manufactured during the year ended 31st December 2015 and

(ii) Sasikala's Trading and Profit & Loss Account for the same period.

Stock as on 1st Jan 2015			
Raw materials	7,000	Travelling expenses	5,400
Work-in-progress	10,000	Manufacturing expenses	5,400
Finished goods	25,400	***Miscellaneous:***	
Purchase of raw materials	90,000	Return outwards	4,000
Carriage of raw materials	2,000	Discount allowed	1,000
Sale of finished goods	3,80,000	Discount received	600
Stock on 31st Dec. 2015:		Import duty on raw materials	24,000
Raw materials	13,000	Sale of waste materials	6,000
Work-in-progress	12,000	Carriage outwards	1,600
Finished goods	28,000	Factory insurance, rent & taxes	12,000
Factory wages	60,000	Bad debts	1,200
Factory expenses	4,800	Salaries (including Sasikala's salary ₹ 9600)	25,600
Return inwards	4,600	Salary of works manager	14,400
Depreciation on machinery	10,800	Office rent & insurance	3,000
Repairs to machinery	9,200	Motive power	7,000
Interest on Bank Overdraft	600		
Miscellaneous expenses	2,600		
Depreciation on office furniture	2,200		
Selling expenses	10,400		

Sasikala's salary is to be allocated 2/3 to factory and 1/3 to office.

Solution:

Manufacturing a/c of Sasikala for the year ended 31-12-15

Particulars	**(₹)**	***Particulars***	**(₹)**
To Work-in-progress on 1-1-15	10,000	By Sale of waste material	6,000
To Material consumed during the year (opening stock + net purchases – closing stock [7,000 + 86,000 (i.e., 9,000 – 4,000) – 13,000])	80,000	By Work-in-progress on 31-12-15	12,000
		By Cost of finished goods transferred to Trading a/c	2,28,000
To Carriage on raw materials	2,000		
To Import duty on raw materials	24,000		
To Factory wages	60,000		
To Salary of works manager	14,400		

To 2/3 of Sasikala's salary	6,400		
To Motive power	7,000		
To Factory expenses	4,800		
To Factory insurance, rent and taxes	12,000		
To Manufacturing expenses	5,400		
To Depreciation of machinery	10,800		
To Repairs of machinery	9,200		
	2,46,000		**2,46,000**

Trading and Profit & Loss a/c of Sasikala for the year ended 31-12-15

Particulars	(₹)	*Particulars*	(₹)
To Stock of finished goods (1-1-15)	25,400	By Sales 3,80,000	
To Manufacturing a/c (cost of finished goods)	2,28,000	*Less:* Returns inwards 4,600	3,75,400
To Gross profit c/d	1,50,000	By Stock of finished goods (on 31-12-15)	28,000
	4,03,400		**4,03,400**
To Depreciation on office furniture	2,200	By Gross profit b/d	1,50,000
To Interest on bank overdraft	600	By Discount received	600
To Miscellaneous expenses	2,600		
To Travelling expenses	5,400		
To Selling expenses	10,400		
To Discount allowed	1,000		
To Carriage outwards	16,000		
To Bad debts	1,200		
To Salaries 25,600			
Less: 2/3 of Sasikala's salary 6,400	19,200		
To Office rent & insurance	3,000		
To Net profit transferred to Capital a/c	1,03,400		
	1,50,600		**1,50,600**

Illustration 16: From the following particulars of Ajay Sharma, prepare the manufacturing, trading and profit and loss a/c for the year end 31st Dec. 2015 and a balance sheet as on that date.

Capital a/c (1-1-15)	7,32,000	Factory buildings	2,00,000
Drawings a/c	1,00,000	Furniture & fixtures	51,500
Purchases	21,05,000	Plant & machinery	95,000
Rates & taxes	25,000	Sundry debtors	1,87,000
Salaries	1,00,000	4% Govt. Promissory Notes (subscribed on 1-1-15)	20,000
Carriage	20,000	Sundry creditors	1,05,000

Fuel & coal	14,000	Sales	25,33,000
Factory insurance	6,000	Cash in hand	45,500
Advertisement	20,000	Cash in bank	1,94,500
Factory power	16,000		
Bad debts written off	10,000		
Cash discount allowed	2,000		
Sundry expenses	3,500		
Opening stock:			
Raw materials	60,000		
Finished goods	50,000		
Patents	12,000		
Postage & telegram	13,000		
Wages	35,000		
Cash discount received	15,000		

Additional information:

(i) Depreciation to be provided at the following rates:
Plant & machinery – 10%; patents – 10%; buildings – 2.5%; furniture 5%.

(ii) Provide 2.5% on debtors for doubtful debts.

(iii) Purchases invoices aggregating ₹ 25,000 were omitted to be entered in the purchase day book.

(iv) Debtors include ₹ 5,000 due from the proprietor.

(v) An amount of ₹ 5,000 received in respect of a private loan advanced by the proprietor which was wrongly credited to Sundry debtors a/c.

(vi) Purchase invoices of the value of ₹ 75,000 were entered in the purchase day book on 29th December 2006 but the goods in respect thereof were received on 3rd January 2007.

(vii) An amount of ₹ 3,500 received from a debtor was wrongly credited to Sales a/c.

(viii) The annual interest on government promissory notes accrued due on 31st Dec. 2015 but was collected only in 2016.

(ix) Carriages include ₹ 8,000 towards outwards charges.

(x) Stock in trade as on 31-12-15:
Raw material ₹ 50,000; finished goods ₹ 40,000.

Solution:

Manufacting, Trading and Profit & Loss a/c of Ajay Sharma for the year ended 31.12.2015.

Particulars		(₹)	*Particulars*	(₹)
To Cost of materials consumed (opening stock + purchase + carriage inwards – closing stock) (60,000 + 2,13,0000 + 12,000 - 1,25,000)		20,77,000	By cost of finished goods transferred to Trading a/c	21,63,700
To Wages		35,000		
To **Factory expenses:**				
Fuel & coal		14,000		
Factory insurance		6,000		
Factory power		16,000		
To **Depreciation on:**				
Plants & machinery	9,500			
Patents	1,200			
Factory buildings	5,000	15,700		
		21,63,700		**21,63,700**
To Opening stock		50,000	By Sales (25,33,000 – 3,500)	25,29,500
To Cost of finished goods		21,63,700	By Closing stock	40,000
To Gross profit c/d		3,55,800		
		25,69,500		**25,69,500**
To Rent, rates & taxes		25,000	By Gross profit b/d	3,55,800
To Salaries		1,00,000	By Discount	15,000
To Carriage outwards		8,000	By Interest on Govt. Promissory notes	800
To Advertisement		20,000		
To Bad debts	10,000			
Add: Provision for B.D.	4,588	14,588		
To Depreciation on furniture		2,576		
To Discount		2,000		
To Sundry expenses		3,500		
To Postage & telegrams		13,000		
To Net profit – transferred to Capital a/c		1,82,936		
		3,71,600		**3,71,600**

Balance Sheet of Ajay Sharma as on 31-12-15

Liabilities	(₹)	(₹)	*Assets15 (₹)*	(₹)	
Capital	7,32,000		Factory buildings	2,00,000	
Add: Additional capital	5,000		***Less:*** Depreciation	5,000	1,95,000
Add: Net profit	1,82,936		Plant & Machinery	95,000	
	9,19,936		***Less:*** Depreciation	9,500	85,500
Less: Drawings			Furniture & fittings	51,500	
(1,00,000 + 5,000)	1,05,000	8,14,936	***Less:*** Depreciation	2,576	48,924

Sundry Creditors (1,05,000 + 25,000)		1,30,000	Patents	12,000	
			Less: Depreciation	1,200	10,800
			4% govt. promissory notes		20,000
			Stock-in-trade:		
			Raw materials (50,000 + 75,000)		1,25,000
			Finished goods		40,000
			Sundry debtors (1,87,000 – 5,000 + 5,000 – 3,500)	1,83,500	
			Less: Provision for B.D.	4,588	1,78,912
			Accrued Interest on Govt promissory notes		800
			Cash in bank		1,94,500
			Cash in hand		45,500
		9,44,936			**9,44,936**

EXERCISE

Short Answer Questions

1. What do you understand by final accounts?
2. What are the distinct stages in final accounts and what are the results of each such stage?
3. What is the purpose of preparation of financial statements?
4. What is gross profit?
5. When do you prepare a 'manufacturing account'?
6. Are adjustments necessary for the preparation of final account? If yes, why?
7. What are the situations in which purchases account is credited?
8. What is balance sheet?
9. Explain the meaning of "liquidity order" in arranging the balance sheet items.
10. Explain the meaning of 'permanency order' in arranging the balance sheet items.
11. What are all the items added to and reduced from the capital of a sole trader in balance sheet?
12. How do you treat stock when it is given in (a) trial balance and (b) adjustments?
13. How do you treat outstanding and prepaid expenses when they are given in (a) trial balances and (b) adjustments?
14. How do you treat accrued incomes and incomes received in advance when they are given (a) in trial balance (b) in adjustments?

Long Answer Questions

1. "Preparation of final accounts is the culmination of the accounting process." Explain.
2. Describe the procedure for preparation of the final accounts of a sole trader, step by step.
3. Distinguish between 'trial balance' and 'balance sheet'.
4. What are the differences between trading account and profit and loss accounts?
5. "The accrual concept is the basis for final accounts." Explain.
6. What do you understand by 'liquidity order' and 'permanency order' in the context of preparing balance sheet? When should usage of each of them be appropriate?
7. What is 'grouping and marshalling' of assets and liabilities? How is it done?

Objective Type Questions

1. Fill in the Blanks

1. Expenses due but not yet paid are known as _______.
2. Income earned but not received is called _______.
3. Depreciation is for _______ of an asset.
4. Unrecovered debts are called _______.

Ans.: 1. Outstanding expenses, 2. Accrued or Outstanding income, 3. Wear and Tear, 4. Baddebts.

State whether the following statements are True or False:

1. Prepaid expenses appear on the assets side of balance sheet.
2. Any income received in advance is a liability.
3. Bad debts are not expenses but they incur loss to the firm.
4. Provision for Doubtful debts is a charge against the profits of the firm.
5. Bad debts incurred in the subsequent period are written off against reserve for baddebts.
6. Provision for Discount on Debtors is a charge against P & L A/c.
7. Provision for discount on debtors appears as a liability in the Balance Sheet.
8. Discount on creditors is an item of income.
9. Provision for discount on creditors is shown as an anticipated income.
10. Closing stock always appears as an asset in balance sheet.
11. Overvaluation of opening stock shows less gross profit.
12. Overvaluation of closing stock shows more gross profit.
13. Sale of old furniture is credited to Tracing Account.
14. Income received in advance is an asset.
15. Balance Sheet shows profitability of business.
16. Plants means tree plants around the factory.

Ans.: (1) True, (2.) True, (3.) True, (4.) True, (5.) True, (6.) True, (7.) True, (8.i) True, (9.) True,(10.) True, (11.) True, (12.) True, (13.), False, (14.), False, (15.) False, (16.) False.)

Match the Column:

(A)

	Column A		Column B
(a)	Goods lost by fire	(i)	Shown on debit side of Trading Account and Profit and Loss Account debit side
(b)	Goods distributed as sample	(ii)	Debit of Trading Account
(c)	Bad debts	(iii)	Deduct from debtors and shown on debit side of Profit and Loss Account
(d)	Prepaid expenses in Trial Balance	(iv)	Balance sheet asset side
		(v)	Shown on credit side of Trading Account and Profit and Loss Account debit side
(e)	Expenses payable in Trial Balance	(vi)	Balance Sheet liability side

(**Ans.:** (a) (v), (b) (i), (c) (iii), (d) (iv), (e) (vi).)

(B)

	Column A		Column B
(a)	Depreciation in Trial Balance	(i)	Profit and loss Account debit side
(b)	Income received in advance	(ii)	Deduct from income, show on liability side
(c)	Accrued income	(iii)	Add to income, show on asset side
(d)	Closing stock	(iv)	Profit and Loss Account debit, deduct from asset in Balance sheet
(e)	Depreciation	(vi)	Trading account credit balance sheet asset side
		(vi)	Add to expenses

(**Ans.:** (a) (i), (b) (ii), (c) (iii), (d) (v), (e) (iv).)

(C)

	Column A		Column B
(a)	Opening balance – Debtors Account	(i)	Debit
(b)	Opening balance – Creditors Account	(ii)	Debit
(c)	Opening balance – Bills Receivable Account	(iii)	Credit
(d)	Opening balance – Bills Payable Account	(iv)	Debit
(e)	Cash Account balance	(vi)	Credit
		(vi)	Credit

(**Ans.:** (a) (iv), (b) (iii), (c) (ii), (d) (v), (e) (i)]

Multiple Choice Questions

(i) Opening stock of finished goods is shown on debit side of __________.

(a) Trading Account (b) Profit and Loss Account

(c) Balance Sheet

(ii) Goodwill is shown on __________.
- (a) Asset side of Balance Sheet
- (b) Credit side of Trading Account
- (c) Credit side of Profit and Loss Account

(iii) Sale of scrap is shown on __________.
- (a) Credit side of Trading Account
- (b) Credit side of Manufacturing Account
- (c) Credit side of Profit and Loss Account

(iv) Livestock is __________.
- (a) Current asset
- (b) Fixed asset
- (c) Fictitious asset
- (d) Intangible asset

(v) Patents and copyright is a __________.
- (a) Current asset
- (b) Fixed asset
- (c) Fictitious asset
- (d) Intangible asset

(vi) Drawing reduces __________.
- (a) Capital
- (b) Profit
- (c) Income
- (d) Purchases

(vii) For a sugar mill, sugarcane is a __________.
- (a) Raw material
- (b) WIP
- (c) Finished goods
- (d) Asset

(viii) For a sugar mill, sugar is a __________.
- (a) Raw material
- (b) WIP
- (c) Finished goods
- (d) Assets

(ix) WIP in the books of a manufacturer is __________.
- (a) Partly finished goods
- (b) Finished goods
- (c) Raw material
- (d) None of the above

(x) Opening stock of WIP is shown on __________.
- (a) Debit side of Trading Account
- (b) Debit side of Manufacturing Account
- (c) Credit side of Profit and Loss Account
- (d) Balance Sheet asset side

(xi) Closing stock of finished goods is shown on __________.
- (a) Credit side of Manufacturing Account
- (b) Credit side of Trading Account
- (c) Credit side of Profit and Loss Account
- (d) None of the above

(xii) Discount represents __________.

(a) Discount allowed (b) Discount received

(c) Asset (d) Liability

(xiii) Productive wages are __________.

(a) Debited to Trading Account

(b) Debited to Profit and Loss Account

(c) Shown as asset

(d) None of the above

(xiv) Closing stock appearing in the Trial Balance is shown on __________.

(a) Asset side of Balance sheet

(b) Liability side of Balance Sheet

(c) Credit side of Trading Account

(d) None of the above

(xv) Prepaid insurance is __________.

(a) Deducted from insurance (b) Added to insurance

(c) Shown on asset side (d) (a) and (b)

(xvi) Income received in advance is shown on __________.

(a) Liability side (b) Asset side

(c) Debit side of Profit and Loss Account (d) None of the above

(xvii) Which of the following account is not closed?

(a) Expenses (b) Interest received

(c) Prepaid insurance (d) Drawings

(xviii) Classification of assets and liabilities as current or long term depends on __________.

(a) Order of listing in the ledger

(b) Whether they appear on Balance Sheet or the income statement

(c) Relative liquidity of the items.

(d) Format of balance sheet

(xix) Cost of goods sold can be computed by adding opening inventory and net purchases and subtracting __________.

(a) Net Sales (b) Sales discount

(c) Closing Stock (d) Net Purchase

(xx) Closing entry sales discount is __________.

(a) Sales Discount A/c Dr.
    To Profit and Loss A/c

(b) Sales Discount A/c Dr.
    To Sales A/c

(c) Profit and Loss A/c Dr.
To sales Discount

(xxi) Which income statement format reports income from operations?
(a) Account format (b) Single step format
(c) Multiple step format

(xxii) Balance sheet gives information regarding __________.
(a) Result of operations (b) Financial position on a particular date
(c) Operating efficiency of the firm

(xxiii) Closing stock is shown in the Balance Sheet under __________.(a)Fixed assets(b)Current assets(c)Current liabilities

(Ans.: (i) (a), (ii) (a), (iii) (b), (iv) (b), (v) (b), (vi) (a), (vi) (a), (viii) (c), (ix) (a), (x) (b), (xi) (b),(xii) (a), (xiii) (a), (xiv) (a), (xv) (d), (xvi) (a), (xvii) (c), (xviii) (c), (xix) (c), (xx) (c),(xxi) (c), (xxii) (b), (xxiii) (b).)

Answer in one word

(i) Advertisement expenses outstanding for the year ending March 2005 is ₹ 5,000. Givethe journal entry.

(ii) What entry is drawn if furniture costing ₹50,000 is depreciated at 5% under straight-line method?

(iii) Calculate the depreciation amount charged for the second year under written down orreducing balance method for Plant and Machinery costing ₹7,50,000. The depreciationrate is 10%.

(iv) If bad debts are recovered, what entry can be drawn?

(v) What is the difference between bad debts and doubtful debts?

(vi) Give the journal entry for writing off of bad debts against RBD.

(vii) What is the entry for adjusting the closing stock?

(Ans.: (i) Advertisement Expenses A/c Dr. To Outstanding Advertisement Expenses A/c, (ii) Depreciation A/c Dr. 2,500 To Furniture A/c 2,500 (Being furniture depreciated), (iii) (7,50,000 – 75,000) = 6,75,000 × 10% = 67,500, (iv) Cash A/c To Bad Debts RecoveredA/c, (v) Bad Debts are totally not recoverable, doubtful debts may be recovered, (vi) Reservefor Bad Debts A/c Dr. To Bad Debts A/c, (vii) Closing Stock A/c Dr. To Trading A/c.)

THEORY QUESTIONS

Short Answer Questions:

1. What do you understand by final accounts?
2. What are the distinct stages in final accounts and what are the results of each such stage?

3. What is the purpose of preparation of financial statements?
4. What is gross profit?
5. When do you prepare a 'manufacturing account'?
6. Are adjustments necessary for the preparation of final account? If yes, why?
7. What are the situations in which purchases account is credited?
8. What is balance sheet?
9. Explain the meaning of "liquidity order" in arranging balance sheet items.
10. Explain the meaning of 'permanency order' in arranging the balance sheet items.
11. What are all the items added to and reduced from the capital of a sole trader in balance sheet?
12. How do you treat stock when it is given in (a) trial balance and (b) adjustments?
13. How do you treat outstanding and prepaid expenses when they are given in (a) trial balances and (b) adjustments?
14. How do you treat accrued incomes and incomes received in advance when they are given (a) in trial balance (b) in adjustments?

Short Answer Problems

1. Pass necessary adjusting in Mr. X's journal on 31st December 1998:
   (i) ₹ 20,000 for wages was outstanding.
   (ii) Write off depreciation on machinery ₹ 50,000
   (iii) ₹ 15,000 was received in advance as interest.
2. Pass adjustment entries for the following:
   (i) Closing stock ₹ 49,280:
   (ii) Provide depreciation on vehicles @ 10% on cost of ₹ 1,40,000.
   (iii) Materials purchased and received from Mr. X for which no entry is passed register ₹ 10,000.
3. Pass necessary journal entries for the following while finalizing the annual accounts:
   (i) Debtors include ₹ 500 receivable from the proprietor for goods drawn by him.
   (ii) Trade debtors of ₹ 1,05,000 include ₹ 5,000 which are considered bad. Provide for doubtful debts at 2.5%.
   (iii) Provide for discount on creditors on closing day @ 2.5% on ₹ 85,000.
4. The trial balance of a trader shows ₹ 3000 to the debit of general expenses a/c included in that are:
   (a) Travelling expenses ₹ 1,000
   (b) School fees of his children ₹ 30
   (c) Subscription and other fees ₹ 500 paid to the Ladies Club on behalf of the trader's wife.

   Make the necessary adjusting journal entry.

(***Ans:*** Debit ₹ 1,000 to Travelling Expenses a/c and ₹ 800 to Drawings a/c, Crediting General Expenses a/c ₹ 1,800)

5. Dawson, a businessman, has invested on 1-4-2010 ₹ 10,000 in government securities on which he gets a net interest of 6% p.a. after 31st March every year. His accounts are closed on 31st December every year. Find out the interest earned by him but not yet received and show by means of journal entry the necessary adjustment.

(***Ans:*** Accrued interest ₹ 450)

6. Pass journal entries for the following transactions:
   (i) Samples worth ₹ 5,000 distributed during a sale campaign programme.
   (ii) Proprietor brought his personal car into the business and the value of the same is ₹ 1,00,000.
   (iii) Interest of ₹ 9,000 received on investment amounting to ₹ 50,000 (20% Govt. of India Bonds).

   The above interest was net of income tax.

7. Show the necessary adjustments in Trading a/c and Balance Sheet from the following information.

   31.12.15 Value of goods still with customers', sold on sale or return basis, treated as sales ₹ 40,000

   G.P. on cost – 25%

(***Ans:*** Cost of stock with customer: ₹ 32,000)

8. Which of the following items of expenditure and income belong to the current accounting year?
   (i) Cash sales;
   (ii) Outstanding expense;
   (iii) Credit purchases;
   (iv) Salaries paid to employees;
   (v) Rent received in advance;
   (vi) Commission received but not yet earned.

(***Ans:*** (i); (ii); (iii); (iv))

9. Mr. Gotham has ₹ 50,000 to the credit of his capital account on 1-1-2015. His drawings during the same year amounted to ₹ 7,000. You are to charge interest on capital at 5% p.a. and ₹ 430 on drawings. Ascertain his closing capital, assuming that his net profit for the year after all adjustments is ₹ 12,400.

(***Ans:*** ₹ 57,470)

10. Form the following, calculate the amount of provision for doubtful debts to be debited to P & L a/c:

Opening provision for doubtful debts	₹ 2,400
Closing sundry debtors	₹ 42,000
Bad debts yet to be written off	₹ 2,000

Provide for doubtful debts at 10% on debtors.

(***Ans:*** Amount to be debited to P & L a/c: ₹ 3,600)

11. On 1st Jan 2015, the provision for doubtful debts account in the books of a firm which maintain it at 5% had a credit balance of ₹ 3,300. During the year, the Bad debts amounted to ₹ 2,400 and the debtors at the end of the year were ₹ 60,000. Show provision for doubtful debts a/c and bad debts a/c for the year 2015.

(***Ans:*** Debit to P & L a/c – ₹ 2,100)

12. Make adjustments from the information given below while preparing P & L account:

	Dr.	Cr.
Loan @ 15% p.a.		20,000
Interest on loan	2,000	
Deposit @ 14% p.a.	15,000	
Interest on deposit		1,000

(***Ans:*** Add ₹ 1,000 interest outstanding to ₹ 2,000 on the debit side of P & L a/c; add ₹ 1,100 to interest on deposit of ₹ 1,000 and show the total on the credit side of P & L a/c)

13. During the year ended 31-12-2015, a firm suffered the following losses. Explain how you would treat them in the accounts on 31-12-2016:
    (a) Stock lost ₹ 15,000
    (b) A machinery of the value of ₹ 21,000 was discarded, being totally out of order.
    (c) A portion of the buildings worth ₹ 12,000 became completely useless.

(***Ans:*** (a) Credit Trading a/c ₹ 15,000 and debit P & L ₹ 15,000 assuming no insurance; (b) Debit P & L a/c and credit Machinery a/c ₹ 21,000; (c) Debit P & L a/c and credit Building a/c with ₹ 12,000)

14. A manager gets 5% commission on net profit after charging such commission. What shall be his commission if gross profit is ₹ 96,000 and expenses of indirect natures other than manager's commission are ₹ 12,000?

(***Ans***: Manager's Commission ₹ 4,000, i.e., 84,000 × 5/105)

15. Calculate gross profit and cost of goods sold from the following information:
    Net sales ₹ 2,00,000
    Gross Profit is 25% on cost.

(***Ans:*** G.P. = ₹ 40,000; C.O.G.S. = ₹ 1,60,000)

16. Ascertain the cost of goods sold from the following:

	₹		₹
Opening stock	17,000	Indirect expenses	10,400
Purchases	61,400	Closing stock	18,000
Direct expenses	9,600		

(***Ans:*** C.O.G.S. = ₹ 70,000)

17. Calculate Net Profit from the following:

	₹
Purchase (200 units)	10,000
Freight and carriage	1,200
Rent and advertising	600
Sales (150 units)	10,800

(***Ans:*** N.P. = ₹ 180; Closing stock = ₹ 2,800) ***Hint:*** Closing stock = ₹ 11,200 × 50 / 200

18. The drawings of a proprietor for the year 2002 are ₹ 30,000. Profit for the year ₹ 50,000 and capital at the end ₹ 1,40,000. Calculate the capital at the beginning.

(***Ans:*** Opening capital: ₹ 1,20,000)

19. Prepare trading account of a trader for the year ending 31^{st} December 2016 from the following data:

	₹
Opening stock (1.1.16)	50,000
Goods purchased during 2016	2,80,000
Freight and packing on the above	20,000
Closing stock (31.12.10)	60,000
Sales	3,80,000
Packing expenses on sales for distribution	12,000

(***Ans:*** Gross profit – ₹ 90,000) ***Hint:*** Ignore packing expenses.

20. From the information given below, prepare Trading Account.

	₹
Opening stock	1,00,000
Purchases	1,50,000
Purchases returns	25,000
Direct expenses	10,000
Carriages inwards	5,000
Sales	4,00,000
Closing stock	50,000

(***Ans:*** Gross profit: ₹ 2,10,000)

Adjustments for Final Accounts

1. Show the necessary entries to adjust the following:
   (a) Outstanding salaries ₹ 1,200; Rent ₹ 300
   (b) Prepaid insurance premium ₹ 450
   (c) Income outstanding: interest on investments ₹ 400; dividend ₹ 350

(d) Discount received in advance ₹ 150

(e) Bad debts written off ₹ 200

(f) Interest on securities received in advance ₹ 500

2. Show the necessary entries to adjust the following in the books of X on 30th June 2008:

   (a) Salaries for the month of June 2008 ₹ 1,500 unpaid.

   (b) Insurance includes annual premium of ₹ 170 on a policy, expiring on 31-12-08.

   (c) Wages include a sum of ₹ 2,000 spent on the erection of a cycle shed for employees.

   (d) Goods issued as samples ₹ 200.

   (e) Rent paid in advance ₹ 250.

3. Pass journal entries to incorporate the following at the time of preparing final accounts:

   (a) Provide 2.5% for discount on debtors and a bad debts provision at 10% of debtors (debtors ₹ 30,000).

   (b) Closing stock was valued at ₹ 43,000.

   (c) Wages owing ₹ 2,500.

   (d) Insurance paid in advances ₹ 1,500.

   (e) Included in debtors is ₹ 1,000 owing by the proprietor.

   (f) Plant which stood at ₹ 75,000 in the books on the first day of the year was disposed of for ₹ 30,000 in part exchange for a new machine costing ₹ 60,000. A net invoice of ₹ 30,000 was passed through the purchases book.

Provision on debtors and creditors

4. From the following figures, you are required to prepare:

   (a) Provision for doubtful debts a/c

   (b) Bad debts a/c

   (c) Profit & loss a/c

Jan. 1 2000	Provision for bad debts	₹ 2,500
Dec. 31 2000	Bad debts	₹ 2,870
Dec. 31 2000	Debtors	₹ 20,000

Information: Make provision for bad debts at 5% on debtors.

(***Ans:*** Debit to P & L a/c: ₹ 370)

5. The provision for bad and doubtful debts stood at ₹ 3,200 on 31st December 2015. On 31st December 2016, debtors stood at ₹ 1,42,250 out of which ₹ 2,250 had to be written of. On December 2016, the debtors were ₹ 76,900 out of which ₹ 1,900 had to be written off as bad debts. The firm creates a bad debts provision to the extent of 5% on the debtors.

   Make the necessary journal entries and show the provision for bad and doubtful debts a/c for 2015 and 2016.

(***Ans:*** In 2015, debit P & L a/c = ₹ 6,050 and in 2016 credit P & L a/c = ₹ 1,350)

6. On 1st Jan 2015, M/s Kamakshi had a bad debt provision of ₹ 2,600. On 31st December 2015, the total debtors amounted to ₹ 73,600 out of which ₹ 1,600 were bad and had to be

written off. The firm wants to maintain a provision for bad debts at 5% of the debtors.

On 31st December 2016, the total debtors amounted to ₹ 1,280 out of which ₹ 1,280 had to be written of as bad debts. The provision for bad debts is to be maintained at 5% of debtors.

Show the bad debts account and the provision for bad debts account for 1992 and 1993.

(***Ans:*** In 2015, debit P & L a/c = ₹ 2,600 and in 2016, credit P & L a/c = ₹ 320).

7. The books of a firm had the following balance on Jan. 1, 2016.

	₹
Sundry debtors	85,000
Sundry creditors	60,000
Provision for doubtful debts	1,700
Provision for discount debtors	1,666
Provision for discount on creditors	600

The sundry debtors and creditors at December 31, 2016 stand at ₹ 1,25,000 and ₹ 83,000 respectively. Bad debts during the year were ended ₹ 1,500 and discounts allowed and earned were ₹ 166 and ₹ 500 respectively. You are required to show relevant ledger accounts and create provision for doubtful debts at 3% and provision for discounts on debtors and creditors at 2%.

(***Ans:*** Transfer of provision for bad debts to P & L a/c = ₹ 3,550; Transfer of provision for discount on debtors to P & L a/c = ₹ 925; Transfer of provision for discount on creditors to P & L a/c = ₹ 1,560)

Preparation of final accounts:

8. Prepare manufacturing trading and profit and loss account from the information given below:

Particulars	₹	***Particulars***	₹
Opening Stock:		Rent (factory)	400
Raw Materials	1,000	Rent (offices)	500
Work In Progress	1,000	Sales return	700
Finished Goods	1,600	Purchase returns	900
Purchases	18,260	General expenses	900
Wages	3,620	Discount to customers	360
Closing Stock:		Interest from bank	200
Raw Materials	2,000		
Work In Progress	1,000		
Finished Goods	1,420		
Sales	32,000		
Carriage on purchases	500		
Carriage on sales	400		
(***Ans:*** Gross profit: ₹ 1,240; Net profit: ₹ 8,280)			

9. Following are the balances extracted from the books of M/s R.K. Enterprises as on 31st March, 2015. You are required to prepare the Manufacturing Account and the Trading Account for the year ended and a Balance Sheet as on that date.

Particulars		***(₹)***
Opening Stock:		
Raw Materials		50,000
Work-in-progress		37,500
Finished Goods		45,000
Raw Material Purchases		1,25,000
Finished goods Purchases		50,000
Productive Wages		75,000
Coal and Fuel		12,500
Sales		3,95,000
Carriage Inward on raw material purchases		2,500
Railway Freight on raw material purchases		1,250
Repairs to Machinery		3,750
Royalty on Production		2,500
Purchase returns		1,250
Sales returns		2,500
Factory Insurance		3,750
Factory Rent		46,250
Closing Stock:		
Raw Materials		37,500
Work-in-progress		45,000
Finished Goods		25,000

(***Ans:*** Cost of Production = 2,76,250 Gross Profit = ₹ 46,250)

10.. From the following details, prepare Manufacturing, Trading and Profit and Loss Account for the year ended on 31st March, 2016.

Particulars			***(₹)***
Opening Stock:			
Raw Materials			60,000
Work-in-progress			50,000
Finished Goods			75,000
Purchase of Raw Materials			3,20,000
Sales			6,25,000
Purchase Returns			5,000
Sales Returns			4,000

Carriage Inward			1,500
Carriage Outward			1,000
Power			2,500
Bad debts			2,000
Coal and Fuel Charges			3,000
Duty and Clearing Charges			2,000
Factory Rent			4,000
Office Rent			5,000
Electric and Water Charges			6,000
Wages			1,40,000
Salary of Works Manager			2,000
Office salaries			5,000
Advertisement			4,000
Depreciation:			
On Plant			3,000
On Factory Shed			1,000
On Office Furniture			600
Closing Stock:			
Raw Materials			40,500
Work-in-progress			60,000
Finished Goods			55,000

(***Ans:*** Cost of Production = 4,89,500 Gross Profit = ₹ 1,11,500)

11. From the following balances of Arvind, prepare manufacturing Trading a/c. Profit & Loss a/c and Balance Sheet as at 31st December 2016.

Particulars	₹	***Particulars***	₹
Credit balances:		Postage	546
Capital	72,000	Bad debts	574
Creditors	17,440	Interest	2,590
Bills payable	5,054	Insurance	834
Sales	1,56,364	Machinery	20,000
Loan	24,000	***Stock (1.1.15):***	
Debit balances:		Raw Materials	10,000
Debtors	7,770	Work In Progress	5,000
Salaries	8,000	Finished Goods	***4,890***
		Purchases	1,24,184
Discount	2,000	Wages	8,600
		Buildings	47,560
		Furniture	32,310

Value of goods on hand 31.12.16

Raw Materials	20,000
Work In Progress	4,000
Finished Goods	4,600

(*Ans:* Gross Profit – ₹ 32,290; Net Profit – ₹ 17,746; Balance Sheet total – ₹ 1,36,240)

12. The following balances were extracted from the books of Prasad on 31st March 2016.

Particulars	**(₹)**	***Particulars***	**(₹)**
Capital	50,000	Creditors	50,001
Drawings	4,000	Bad debts	100
General expenses	5,000	Loan	15,760
Buildings	22,000	Sales	13,020
Machinery	18,680	Purchases	94,000
Stock:		Motor car	4,000
Raw Materials	10,000	Reserve Fund (Cr.)	180
Work In Progress	10,000	Commission (Cr)	2,640
Finished Goods	12,400	Car expenses	3,600
Power	4,480	Bills payable	6,700
Taxes & insurance	2,630	Cash	160
Wages	14,400		
Debtors	12,560		
Bank overdraft	6,600		
Charity	210		

Prepare the final accounts for the year ended on 31st March 2016.

Stock on 31st March 2016 Valued at

Raw Materials	15,000
Work In Progress	15,000
Finished Goods	17,000

(*Ans:* Gross Profit – ₹ 32,440; Net Profit – ₹ 22,540; Balance Sheet total – ₹ 1,04,400)

13. From the following trial balance of Ravi, prepare trading and profit & loss account for the year ended 31st December 2016 and a balance sheet as on that date.

Trial Balance

Particulars	**(₹)**	**(₹)**
Capital		40,000
Sales		25,000

Purchases	15,000	
Salaries	2,000	
Rent	1,500	
Insurance	300	
Drawings	5,000	
Machinery	28,000	
Bank balance	4,500	
Cash	2,000	
Opening Stock:		
Raw Materials	2,000	
Work In Progress	2,000	
Finished Goods	1,200	
Debtors and Creditors	2,500	1,000
	66,000	**66,000**

Adjustment required:

(i) Stock on 31.12.16

Raw Materials	1,500
Work In Progress	1,500
Finished Goods	1,900

(ii) Salaries unpaid ₹ 300

(iii) Rent paid in advance ₹ 200

(iv) Insurance prepaid ₹ 90

(***Ans:*** G.P. = ₹ 9,700 , N.P. = ₹ 5,890; B/S Total = ₹ 42,190)

14. From the following trial balance, prepare trading, profit & loss a/c for the year ended 31.12.2016 and a balance sheet as on that date:

Trial Balance

Purchases	11,870	Capital	8,000
Debtors	7,580	Bad debts recovered	25
Return inwards	450	Creditors	1,250
Bank deposit	2,750	Return outwards	350
Rent	360	Bank overdraft	1,570
Salaries	850	Sales	14,690
Travelling expenses	300	Bills payable	1,350
Cash	210		
Stock:			
Raw Materials	1,000		
Work In Progress	1,000		
Finished Goods	450		
Discount allowed	40		
Drawings	600		
	27,460		**27,650**

Adjustments:

(i) The Closing Stock on 31.12.16 was

Raw Materials	1,500
Work In Progress	1,500
Finished Goods	1,200

(ii) Write off ₹ 80 as bad debts and create a reserve for bad debts at 5% on sundry debtors.

(iii) Three month's rent is outstanding.

(*Ans:* Gross Profit = ₹ 4,470, Net profit = ₹ 2,595; Balance Sheet total = ₹ 14,285)

15. From the following balances as at 31st December 2016 of a trader, prepare a trading and profit & loss a/c for the year 2016 and a balance sheet as on that date:

Particulars	***(₹)***	***Particulars***	***(₹)***
Salaries	5,500	Creditors	9,500
Rent	1,300	Sales	32,000
Cash	1,000	Capital	30,000
Debtors	40,000	Loans	10,000
Trade expenses	600		
Purchases	25,000		
Advances	2,500		

Stock:			
Raw Materials	2,000		
Work In Progress	2,000		
Finished Goods	1,600		
	81,500		**81,500**

Adjustments:

(i) Closing Stock amounted to

Raw Materials	3,000
Work In Progress	3,000
Finished Goods	3,000

(ii) One month's salary is outstanding.

(iii) One month's rent has been paid in advance.

(iv) Provide 5% for doubtful debts.

(***Ans:*** Gross Profit = ₹ 16,000; Net profit = ₹ 6,200; Balance Sheet total – ₹ 56,200)

16. Prepare manufacturing trading and profit & loss a/c for the year ended 31st December, 2016 and a balance sheet as on that date from the following trial balance of Mr. Akilan:

Particulars	***(₹)***	***Particulars***	***(₹)***
Drawings	45,000	Creditors	1,60,000
Goodwill	90,000	Capital	35,000
Buildings	60,000	Bills payable	70,000
Machinery	40,000	Purchase returns	2,650
Bills receivable	6,000	Sales	2,18,000
Opening Stock:			
Raw Materials	15,000		
Work In Progress	15,000		
Finished Goods	10,000		
Purchase	51,000		
Wages	26,000		
Carriage outwards	500		
Carriage inwards	1,000		
Salaries	35,000		
Rent	3,000		
Discount	1,100		
Repairs	2,300		
Bank	25,000		

Cash	1,600		
Debtors	45,000		
Bad debts	1,200		
Sales returns	2,000		
Furniture	6,000		
Advertisements	3,500		
General expenses	450		
	4,85,650		**4,85,650**

Adjustments:

(i) Closing Stock was

Raw Materials	15,000
Work In Progress	15,000
Finished Goods	5,000

(ii) Depreciate machinery and furniture by 10%.

(iii) Outstanding wages ₹ 1,500.

(iv) Prepaid advertisement ₹ 500.

(v) Create 5% on debtors for bad debts as provision.

(**Ans.:** Gross Profit = ₹ 1,00,930, Net profit = ₹ 84,450, Balance Sheet Total = ₹ 3,00,500]

17. From the following trial balance of Thiru Rehman as on 31st March 2016, prepare manufacturing trading and profit & loss a/c and balance sheet taking into account the adjustments:

Debit balance	***(₹)***	***Credit balance***	***(₹)***
Land and buildings	42,000	Capital	62,000
Machines	20,000	Sales	98,780
Patents	7,500	Return outwards	500
Stock 1-4-2015:		Sundry creditors	6,300
Raw Materials	1,500	Bills payable	9,000
Work In Progress	1,500		
Finished Goods	2,760		
Sundry debtors	14,500		
Purchases	40,675		
Cash in hand	540		
Cash at bank	2,630		
Return inwards	680		
Wages	8,480		
Fuel & power	4,730		

Carriage on sales	3,200		
Carriage on purchases	2,040		
Salaries	15,000		
General expense	3.000		
Insurance	600		
Drawings	5,245		
	1,76,580		**1,76,580**

Adjustments:

(i) Stock on 31.3.2016

Raw Materials	2,000
Work In Progress	2,000
Finished Goods	2,800

(ii) Salary outstanding ₹ 1,500.

(iii) Insurance prepaid ₹ 150.

(iv) Depreciate machinery at 10%and patents at 20%.

(v) Create a provision of 2% on debtors for bad debts.

(***Ans:*** Gross profit = ₹ 43,715; Net profit = ₹ 16,775; Balance Sheet total = ₹ 90,330)

18. The following are the balances extracted from the books of Ganesh as on 31-12-2016. Prepare manufacturing trading and profit and loss a/c for the year ending 31-12-2016 and a balance sheet as on that date.

Trial Balance as on 31-12-2016

Debit balance	***(₹)***	***Credit balance***	***(₹)***
Drawings	4,000	Capital	20,000
Cash at bank	1,700	Sales	16,000
Cash in hand	6,500	Sundry creditors	4,500
Wages	1,000		
Purchases	2,000		
Stock (1-1-2016):			
Raw Materials	2,000		
Work In Progress	2,000		
Finished Goods	2,000		
Buildings	10,000		
Sundry debtors	4,400		
Sills receivable	2,900		
Rent	450		
Commission	250		

General expense	800		
Furniture	500		
	40,500		**40,500**

Adjustments:

(i) Stock on 31.3.2016

Raw Materials	2,000
Work In Progress	1,000
Finished Goods	1,000

(ii) Interest on capital at 6% to be provided.

(iii) Interest on drawings at 5% to be provided.

(iv) Wages yet to be paid ₹ 100.

(v) Rent prepaid ₹ 50.

(***Ans:*** Gross profit = ₹ 10,900; Net profit = ₹ 8,450; Balance Sheet total = ₹ 30,050)

19. Below is given the trial Balance of Tripathi Brothers of Ahmedabad as on 31st December, 2016:

Debit balance	**(₹)**	***Credit balance***	**(₹)**
Opening Stock:		Capital	12,000
Raw Materials	1,000	Bank loan	3,000
Work In Progress	1,000	Sundry creditors	4,920
Finished Goods	1,100	Return outwards	420
Buildings	17,000	Interest	130
Furniture	1,000	Dividends	110
Purchases	21,200	Sales	41,460
Salaries	2,200		
Bad debts	120		
Cash in hand	1,300		
Returns inwards	1,020		
Rent	600		
Miscellaneous expenses	500		
Postage	280		
Stationery	260		
Wages	5,200		
Freight and carriage on purchase	560		
Carriage on Sales	800		
Repairs	900		
Sundry debtors	6,000		
	62,040		**62,040**

In addition, the following information is given:

(a) A provision at 5% for doubtful debts has to be made.

(b) Value of stock on 31st December 2016 was estimated at

Raw Materials	1,000
Work In Progress	1,000
Finished Goods	980

(c) In the miscellaneous expenses included is an yearly insurance premium of ₹ 120. The yearly premium falls due every year on 31st March.

(d) Depreciation on building is to be charged at 10%.

(e) Salaries for December 2002 amounting to ₹ 200 were not paid till the date of preparing Trial Balance.

Prepare Trading Account and Profit & Loss Account of Tripathi Brothers for the year 2002 and Balance Sheet as on that date.

(*Ans:* Gross Profit = ₹ 13,780; Net Profit = ₹ 6,190; Balance Sheet total = ₹ 26,310)

20. Prepare manufacturing, Trading & Profit and Loss Account and Balance Sheet as on 31st March, 2016.

Debit balance	***(₹)***	***Credit balance***	***(₹)***
S. Chandra's Capital a/c	1,19,400	Manufacturing wages	40,970
S. Chandra's Drawings a/c	10,550	Sales	3,56,430
Sundry Creditors	59,630	Return Inwards	2,780
6% Loan a/c (Credit)	20,000	Salaries	11,000
Cash in hand	3,030	Rent & taxes	5,620
Cash at Bank	18,970	Interest & Discount (Dr.)	5,870
Sundry debtors (including Kalpana for dishonoured bill of ₹ 1,000)	62,00	Travelling Expenses Repairs & Renewals	1,880 3,370
Bills Receivable	9,500	Insurance (including premium	400
Provision for doubtful debts	2,500	of ₹ 300 p.a. paid up to 30th Sep. 2004	3,620
Fixtures & fittings	8,970	Bad debts	5,620
Stock 1st April, 2015:		Commission received	5,640
Raw Materials	30,000	Plant & Machinery	28,800
Work In Progress	30,000		
Finished Goods	29,680		
Purchases	2,56,590		

Adjustments:

(i) Stock on hand 31st March 2016 was

Raw Materials	50,000
Work In Progress	50,000
Finished Goods	28,960

(ii) Write off half of Kalpana's dishonoured bill.

(iii) Create a provision of 5% on sundry debtors.

(iv) Charge 5% interest on capital.

(v) Manufacturing wages include ₹ 1,200 for erection of new machinery purchased last year.

(vi) Depreciate plant and machinery by 5% and fixtures and fittings by 10% p.a.

(vii) Commission earned but not received amount to ₹ 600.

(viii) Interest on loan for the last two months is not paid.

(***Ans:*** Gross Profit = ₹ 96,570; Net Profit = ₹ 61,583, Balance Sheet Total = ₹ 2,56,233)

21. The following are the balances extracted from the ledger of Karikalan as on December 31, 2016:

Particulars	***(₹)***	***Particulars***	***(₹)***
Karikalan's Capital a/c	20,000	Reserve for discount on debtors	200
Drawings	3,500	Loans @ 9%	5,000
Buildings	10,000	Salaries	4,400
Machinery	2,500	Wages	7,500
Furniture & fittings	600	Rent	2,750
Opening Stock:		Travelling expenses	1,250
Raw Materials	5,000	Postage & telegrams	135
Work In Progress	5,000	Rates & taxes	90
Finished Goods	2,500	Carriage Inwards	2,500
Cycle	400	Carriage Outwards	750
Purchases	75,000	Interest paid	375
Sales	1,25,000	General charges	900
Sales Returns	5,000	Bad debts	300
Duty paid on purchases	15,000	Cash in hand	250
Sundry Debtors	10,000	Cash at Bank	2,400
Sundry Creditors	7,500		
Reserve for bad & doubtful debts	400		

The following adjustments are necessary:

(a) Stock on 31.12.16 was

Raw Materials	5,000
Work In Progress	5,000
Finished Goods	4,000

(b) Provide the following outstanding:

Salary ₹ 400; Rent ₹ 250; Wages ₹ 600 and Interest ₹ 75.

(c) Maintain the reserve for doubtful debts at 5% and the reserve for discount on debtors at 2.5% on sundry debtors.

(d) Provide depreciation for Building 2.5%, Furniture 6% and Cycle 15%.

Prepare Trading and Profit and Loss a/c and the Balance Sheet for the year ended 31-12-16.

(***Ans:*** Gross Profit = ₹ 20,900; Net Profit = ₹ 8,491.50, Balance Sheet Total = ₹ 38,816.50)

22. Edward's books show the following balances. Prepare manufacturing, Trading and Profit & Loss a/c for the year ended 31st December, 2016 and a Balance Sheet as at that date:

Debit balance	**(₹)**	***Credit balance***	**(₹)**
Drawings	5,000	Capital	1,08,850
Bills Receivable	4,500	Loan at 6% p.a.	20,000
Land & Buildings	37,770	Sales	3,50,000
Sundry Debtors	62,000	Interest on investments	5,640
Wages and Salaries	40,970	Sundry Creditors	59,000
Return Inwards	2,780	Commission received	630
Purchases	2,56,590	Return outwards	6,430
Postage & telegrams	5,620		
Stock on 1-1-2016:			
Raw Materials	30,000		
Work In Progress	30,000		
Finished Goods	29,680		
Printing & Stationery	880		
Travelling expenses	12,000		
Interest on loan paid	300		
Petty Cash	70		
Bank Balance	8,800		
Repairs	3,620		
Commission	470		
Furniture	500		
Investments	19,000		
	5,50,550		**5,50,550**

Adjustments:

(i) Closing Stock on 31-12-2016

Raw Materials	50,000
Work In Progress	50,000
Finished Goods	28,960

(ii) Commission received but not earned ₹ 130.

(iii) Travelling expenses were overdrawn by the employees to the extent of ₹ 2,000.

(iv) Create a 5% reserve on sundry debtors and allow 2% discount on debtors and creditors.

(v) Interest on loan due for 9 months.

(vi) 1/4th of wages and salaries should be charged to Trading Account.

(***Ans:*** Gross Profit = ₹ 1,26,097.50; Net Profit = ₹ 76,622, Balance Sheet Total = ₹ 2,59,322)

23. From the following Trial Balance of Mr. Xavier as on 31-3-2016, prepare manufacturing, Trading a/c, Profit & Loss a/c for the year ended 31-3-2016 and a Balance Sheet as on that date after making necessary adjustments:

Trial Balance

Debit balance	**(₹)**	***Credit balance***	**(₹)**
Xavier's Drawings	12,000	Xaviers's Capital	60,000
Furniture & fixtures	4,000	Returns Outward	2,000
Plant & Machinery	30,000	Sales	1,30,000
Opening Stock:		Creditors	12,000
Raw Materials	5,000	Loan at 6% p.a. taken from P. Abdul on 1-1-93	10,000
Work In Progress	5,000	Discount	600
Finished Goods	10,000		
Purchases	80,000		
Salaries & Wages	22,400		
Debtors	20,400		
Returns Inward	5,000		
Postage & telegrams	1,500		
Rent, rates, and taxes	3,600		
Bad debts written off	400		
Trade Expenses	200		
Interest on loan from P. Abdul	150		
Insurance	800		
Travelling expenses	500		
Sundry Expenses	300		
Cash in hand	3,050		
Cash at Bank	10,300		
	214600		**214600**

Adjustments:

(i) Closing Stock Cost Price ₹ 21,000 and Market Price ₹ 25,000 consist Raw Materials, Work In Progress & Finished Goods in same proportion as it was in last year.

(ii) Of the debtors, ₹ 400 are bad and should be written off. Create a reserve for discount on debtors 2.5%.

(iii) Interest on Capital is to be calculated at 6% p.a. and on drawings ₹ 330.

(iv) Prepaid insurance amounted to ₹ 100.

(v) Depreciate furniture & fixtures by 5% and Plant and Machinery by 10%.

(vi) Make a reserve for discount on creditors at 2%.

(***Ans:*** Gross Profit = ₹ 48,000; Net Profit = ₹ 10,920; Balance Sheet Total = ₹ 84,750)

24. From the following Trial Balance of Appu as on 31st March 2016, prepare manufacturing, Trading and Profit and Loss a/c for the year and a Balance Sheet as on that date:

Debit balance	***(₹)***	***Credit balance***	***(₹)***
Stock on 1-4-2015:		Sundry Creditors	23,500
Raw materials	21,000	Bills Payable	7,500
Work-in-progress	9,500	Sale of scrap	2,500
Finished goods	15,500	Commission	450
Sundry Debtors	24,000	Provision for doubtful debts	1,650
Carriage	1,500	Capital	1,00,000
Bills Receivable	15,000	Sales	1,67,200
Wages	13,000		
Salaries	10,000		
Postage & telegrams	1,000		
Repairs & Renewals	1,100		
Purchases	85,000		
Cash at Bank	17,000		
Plant & Machinery	70,000		
Furniture	10,000		
Rent	6,000		
Lighting	1,350		
General expenses	1,850		
	3,02,800		3,02,800

Adjustments:

(i) Stock on 31st March 2016:

Raw materials – ₹ 16,200

Work-in-progress – ₹ 7,800

Finished goods – ₹ 18,100

(ii) Salaries and wages outstanding were ₹ 900 and ₹ 2,000.

(iii) Machinery is to be depreciated by 10% and furniture by 7.5%.

(iv) Office premises occupy 1/4 of total area. Lighting is to be charged as to 2/3 to factory and 1/3 to office.

(***Ans:*** Gross Profit = ₹ 56,400; Net Profit = ₹ 36,450; Balance Sheet total = ₹ 1,70,350)

25. Prepare manufacturing, Trading and Profit and Loss Account and Balance Sheet for the year ended 31-3-16.

Particulars	***(₹)***
Capital	2,80,000
Plant & Machinery	60,000
Drawings	6,000
Opening Stock (1-4-2015)	
Raw Materials	15,000
Work In Progress	15,000
Finished Goods	15,000
Purchases	3,10,000
Sales	2,50,000
Furniture	10,000
Debtors	40,000
Freight and Octroi	4,800
Trade Expenses	500
Salary	5,500
Rent	2,400
Advertisement	5,000
Insurance Premium	400
Commission earned	1,300
Discount allowed	200
Bad debts	1,800
Provision for Bad Debts	900
Cash	5,200
Bank	5,800
Goodwill (at cost)	20,000

Adjustments:

(i) Closing Stock

Raw Materials	20,000
Work In Progress	20,000
Finished Goods	13,000

(ii) Salaries have been paid for 11 months only.

(iii) Prepaid Insurance Premium ₹ 100.

(iv) Commission earned but not received ₹ 122.

(v) Create 3% provision for bad debts in debtors.

(vi) Depreciation on furniture at 10% is to be charged.

(vii) 1/4th of advertisements is to be written off.

(***Ans:*** G.P. = ₹ 63,200; N.P. = 50,872: B/S Total = ₹ 1,45,372)

Hint: Difference in trial balance = ₹ 9,600 (Dr).

26. The following in trial balance from the books of Mr. Rahul on 31st December, 2015.

Particulars	***(₹) Dr.***	***(₹) Cr.***
Furniture & Fitings	640	–
Motor Vehicles	6,250	–
Buildings	7,500	–
Capital a/c		12,500
Bad debts	125	–
Provision for bad debts		200
Sundry debtors and creditors	3,800	2,500
Stock on 1st January, 2015		
Raw Materials	1,000	
Work In Progress	1,000	
Finished Goods	1,460	
Purchases and sales	5,475	15,450
Bank Overdraft		2,850
Sales and Purchases returns	200	125
Advertising	450	–
Interest Account	118	–
Commission	–	375
Cash	650	–
Taxes and insurance	1,250	–
General Expenses	782	–
Salaries	3,300	–
	34,000	34,000

Adjustments:

(i) Stock on 31.12.15 was

Raw Materials	1,000
Work In Progress	1,000
Finished Goods	1,250

(ii) Depreciate building at 5%, Furniture & fittings at 10% and Motor vehicles at 20%.

(iii) ₹ 85 is due for interest on Bank overdraft.

(iv) Salaries ₹ 300 and taxes ₹ 120 are outstanding.

(v) Insurance amounting to ₹ 100 is prepaid.

(vi) One-third of the commission received is in respect of work to be done next year.

(vii) Write off further ₹ 100 as bad debts and provision for bad debts is to be made equal to 5% on sundry debtors.

(viii) Building occupied by Factory & Office in the proportion of 8:2

(ix) Purchase of furniture worth Rs. 100 included in purchases

Prepare Trading and Profit & Loss a/c for the year ending 31-12-2004 and a Balance Sheet as on that date.

(***Ans:*** Gross Profit = ₹ 9,390; Net Profit = ₹ 1,736; Balance Sheet total = ₹ 20,216)

27. Prepare Manufacturing, Trading Profit and Loss Account and Trial Balance of Anbumani as on 31-12-2015.

Debit balance	***(₹)***	***Credit balance***	***(₹)***
Cash in hand	540	Sales	98,780
Cash at bank	2,630	Return outwards	500
Purchases	40,675	Anbumani's capital	71,000
Return inwards	680	Creditors	6,300
Wages	10,480		
Fuel and power	4,730		
Carriage inwards	2,040		
Carriage outwards	3,200		
Opening stock:			
Raw Materials	2,000		
Work In Progress	2,000		
Finished Goods	1,760		
Premises	30,000		
Lands	10,000		
Machinery	20,000		
Patents	7,500		
Salaries	15,000		
Sundry Expenses	3,000		
Insurance	600		
Drawings	5,245		
Debtors	14,500		
	1,76,580		1,76,580

Taking into consideration the following adjustments, prepare Trading and Profit and Loss account and a Balance Sheet as on 31-12-2015.

Adjustment

(a) Closing Stock on 31-12-2015

Raw Materials	2,000
Work In Progress	2,000
Finished Goods	2,800

(b) ₹ 2,000 spent on erection of a shed were included in wages account.

(c) The insurance policy expires on 30-6-2016.

(d) Provide 5% for doubtful debts.

(e) ₹ 2,000 is to be transferred to Reserve Fund out of profits if any.

(***Ans:*** G.P. = ₹ 43,715; N.P. = ₹ 21,490; Balance profit transferred to B/S = ₹ 19,490; B/S Total = ₹ 93,545)

28. From the following particulars, prepare manufacturing, trading and profit & loss a/c for the year ended 31-12-2015 and the Balance Sheet as on that date:

Trail Balance

Particulars	***Debit (₹)***	***Credit (₹)***
Cash at Bank	20,500	
Capital a/c		80,000
Drawings a/c	6,000	
Machinery	25,000	
Stock on 1-1-2015:		
Raw Materials	5,000	
Work In Progress	5,000	
Finished Goods	5,000	
Purchases	82,000	
Sales returns	2,000	
Sundry Debtors	20,600	
Furniture	5,000	
Taxes	2,000	
Carriage Outwards	500	
Rent	4,600	
Printing & Stationery	800	
Trade expenses	400	
Sundry Creditors		10,000

Sales		1,20,000
Purchase returns		1,000
Postage & Telegram	800	
Reserve for bad & doubtful debts		400
Discount		800
Rent received		1,200
Insurance premium	700	
Salary & wages	21,300	
Cash in hand	6,200	
	2,13,400	**2,13,400**

Adjustments:

(i) Closing Stock on 31-12-2015

Raw Materials	5,000
Work In Progress	5,000
Finished Goods	4,600

(ii) Write off Bad debts ₹ 600.

(iii) Reserve for bad doubtful debts at 5% on sundry debtors is required.

(iv) Provide reserve for discount on debtors at 2% and reserve for discount on creditors also at 2%.

(v) Depreciate machinery and furniture at 5% and 20% respectively.

(vi) Prepaid Insurance ₹ 100.

(vii) A fire occurred on 25-12-2015 destroying stock to the extent of ₹ 5,000. The stock were insured and the insurance company reimbursed the loss.

(viii) Building occupied by Factory & Office in the proportion of 6:4

(ix) Purchase of furniture worth Rs. 1,000 included in purchases

(***Ans:*** Gross Profit = ₹ 38,050; Net Profit = ₹ 8,970; Balance Sheet total = ₹ 92,770)

29. From the following Trial Balance of Mr. Satish, prepare manufacturing, Trading and Profit & Loss a/c for the year ended 30th June, 2016 and a Balance Sheet as on that date.

Particulars	***Debit (₹)***	***Credit (₹)***
Satish's Capital		71,000
Cash in hand and at Bank	3,900	
Purchases and sales	41,000	98,800
Returns	600	500
Productive wages	10,500	
Power & fuel	4,000	

Carriage outward	15,000	
Carriage inward	3,200	
Opening Stock:		
Raw Materials	1,000	
Work In Progress	500	
Finished Goods	500	
Buildings	5,800	
Plant & Machinery	40,000	
Furniture	20,000	
Debtors and Creditors	7,500	6,300
General expenses	14,500	
Insurance	3,000	
Drawings	600	
Salary	5,000	
	1,76,600	**1,76,600**

Adjustment:

(i) Stock on 30th June 2016 was valued at ₹ 7,000.

Raw Materials	2,000
Work In Progress	2,000
Finished Goods	3,000

(ii) Goods purchased worth ₹ 5,000 were received and included in closing stock but were not entered in purchases book.

(iii) Prepaid insurance amounted to ₹ 170.

(iv) Salaries and advertisement bill are outstanding to the extent of ₹ 500 and ₹ 1,000 respectively.

(v) Building, machinery and furniture are to be depreciated by ₹ 2,000, ₹ 3,000 and ₹ 1,500 respectively.

(***Ans:*** Gross Profit = ₹ 37,000; Net Profit = ₹ 5,300; Balance Sheet total = ₹ 77,870)

3

Chapter

Accounting from Incomplete Records

INTRODUCTION

A Single-entry bookkeeping system or Single-entry accounting system is a method of book-keeping relying on a one-sided accounting entry to maintain financial information. Most businesses maintain a record of all transactions based on the Double-entry bookkeeping system. However, many small, simple businesses maintain only a Single-entry system that records the “Bare essentials.” In some cases only records of cash, accounts receivable, accounts payable and taxes paid may be maintained. Records of assets, inventory, expenses, revenues and other elements usually considered essential in an accounting system may not be kept, except in memorandum form. Single-entry systems are usually inadequate except where operations are especially simple and the volume of activity is low. This type of accounting system with additional information can typically be compiled into an income statement and balance sheet by a professional accountant.

The single-entry system is really no system at all for keeping accounts. Under this system only such accounts are kept as seem to be absolutely necessary. Usually the accounts that are kept are those relating to cash, credit customers and creditors. One may not find accounts relating to fixed assets, purchases, sales expenses are recorded at all some transaction are recorded only in one of their aspect while for some others both the aspect are recorded goods sold on credit will be recorded only in the account of the customer concerned. Cash received from him will be recorded both in the cash account and in the account of the customer. Purchase of machinery on credit will not be recorded at all till payment is made.

This system of recording transaction is very defective. No trial balance can be taken out and hence accuracy of books cannot be proved. Chances of mischief or fraud remaining undetected are high. Trading and profit and loss account cannot be prepared and hence the proprietor will have no firm idea of profit earned or loss suffered. Balance sheet called statement of affairs here, is prepared in an unsatisfactory manner, the assets and liabilities are not proved from records but are put down by physical inspection and on estimated basis. In spite of all the defects the system is quite popular with small firms which cannot afford to spend money on proper accounting.

DEFINITION

According to R.N. Carter, "Single-entry cannot be termed as as a system, as it is not based on any scientific system, like double-entry system. For this purpose, single-entry is nowadays known as preparation of account from incomplete records".

Advantages

1. **Single-entry Systems are used in the Interest of Simplicity:** They are usually less expensive to maintain than double-entry systems because they do not require the services of a trained person.
2. **According to the U.S. Internal Revenue Service:** A single-entry system is based on the income statement (profit or loss statement). It can be a simple and practical system if you are starting a small business. The system records the flow of income and expenses through the use of:
   (a) A daily summary of cash receipts, and
   (b) Monthly summaries of cash receipts and disbursements (IRS Publication 583: Starting a Business and Keeping Records, 2007)
3. Additionally, in the Internal Revenue Manual 4.10.3.13.2 (03-01-2003), it is stated. The single-entry system of record keeping does not include equal debits and credits to the balance sheet and income statement accounts. A single-entry accounting system is not self-balancing. Mathematical errors in the account totals are thus common. Reconciliation of the books and records to the return is an important audit step.
4. A single-entry system may consist only of transactions posted in a notebook, daybook, or journal. However, it may include a complete set of journals and a ledger providing accounts for all important items.
5. A single-entry system for a small business might include a business checkbook, check disbursements journal or register, daily/monthly summaries of cash receipts, a depreciation schedule, employee wages records, and ledgers showing debtor and creditor balances.
6. Single-entry system is simple to understand and easy to maintain as it has no fixed set of principles to follow while recording financial transactions.
7. Single-entry system is an economical system of recording financial transactions. It does not require hiring skilled accounting personnel to record financial transactions of the business. Further, it does not require large number of books to record the limited number of financial transactions.
8. Under single-entry system, the amount of profit can be determined easily. The amount of profit or loss of the period can be determined by making comparison between the amounts of closing capital and opening capital.

9. The Single-entry system is simple, easy, and economical system. It is suitable for small businesses because they cannot afford the cost of double-entry system. Besides, small businesses are not required to maintain their books of accounts under double-entry system.

Disadvantages

1. Data may not be available to management for effectively planning and controlling the business.
2. Lack of systematic and precise bookkeeping may lead to inefficient administration and reduced control over the affairs of the business.
3. Single-entry records do not provide a check against clerical error, as does a double-entry system. This is one of the most serious defects of single-entry systems.
4. Single-entry records seldom make provision for recording all transactions. In addition, many internal transactions, such as adjusting entries are often not recorded.
5. Because no accounts are provided for many of the items appearing in both the Income Statement and Balance Sheet, omission of important data is possible.
6. In the absence of detailed records of all assets, lax administration of those assets may occur.
7. Theft and other losses are less likely to be detected.
8. The single-entry system is unsystematic and unscientific system of recording financial transactions. It does not have any set of fixed rules and principles for recording and reporting the financial transactions.
9. Single-entry system is incomplete system because it does not record the two aspects or accounts of all the financial transactions of the business. It does not maintain any record of the transactions relating to the nominal account and real account except cash account.
10. Single-entry system is not based on the principles of debit and credit. It fails to provide the arithmetical accuracy of the books of accounts. Trial balance cannot be prepared under this system to check the arithmetical accuracy of books of accounts.
11. Under single-entry system, the true amount of profit or loss cannot be ascertained because it does not maintain the nominal accounts.
12. The single-entry system does not maintain real accounts except cash book. Therefore, it cannot reveal the true financial position of the business.
13. The single-entry system of bookkeeping is incomplete, inaccurate and unscientific. It does not help to check the arithmetical accuracy of the books of accounts. Therefore, there is always a possibility of committing frauds and errors in the books of accounts.
14. The single-entry of bookkeeping has incomplete records of the financial transactions of the business. Hence, the tax office cannot accept the account maintained under this system for the purpose of assessment of tax.

Difference between Double-entry and Single-entry Systems

Sr. No	Basis of Difference	Double-entry System	Single-entry System
1.	Recording of Transaction	Both aspects of all transactions are recorded in some cases	Both aspects, in some others a single aspect or no aspect is recorded
2.	Opening of Accounts	All personal, real and nominal accounts are opened.	Only personal accounts and cash accounts are opened
3.	Preparation of Trial Balance	Trial Balance can be prepared	Trial Balance cannot be prepared
4.	Ascertaining Profit or Loss	Account profit or loss can be found, through Trading and Profit and Loss A/c	Profit or loss cannot be found normally, in the absence or Trading and Profit and Loss A/c
5.	Revealing Financial Position	Reliable Financial position can be found through Balance Sheet	Balance sheet cannot be prepared. So financial position is difficult to ascertain.
6.	Acceptability	Acceptable for Income tax and other tax purposes, for raising of bank loans etc.	Not acceptable for taxation claims, raising of loans.
7.	Acceptable Evidence	In case of disputes, accounting records can be produced in courts of law.	The accounting records are not acceptable evidence.
8.	Utility	Suitable for any type of business of any size	It can be followed by small business men who can exercise personal control over the business.
9.	Internal Check	Internal check is possible	Internal check is not possible.

The Single-entry System is really no system at all for keeping accounts. Under this system, only such accounts are kept as seem to be absolutely necessary. Usually the accounts that are kept are those relating to cash, credit customers and creditors. One may not find accounts relating to fixed assets, purchases, sales, expenses, incomes, etc., thus one may find that some transactions are not recorded at all, some transactions are recorded only in one of their aspects while, for some others, both the aspects are recorded. Goods sold on credit will be recorded only in the account of the customer concerned. Cash received from him will be recorded both in the Cash Account and in the account of the customer. Purchase of machinery on credit will not be recorded at all till payment is made.

This system of recording transactions is very defective. No trial balance can be taken out an hence, accuracy of books cannot be proved. Chances of mischief of fraud remaining undetected are high. Trading and profit and loss Account cannot be prepared and, hence, the proprietor will have no firm idea of profit earned or loss suffered. Balance sheet, called statement of affairs here, is prepared in an unsatisfactory manner. The assets and liabilities are one proved from records but are put down by physical inspection and on estimated basis. In spite of all the defects, the system is quite popular with small firms which cannot afford to spend money on proper accounting.

Conversion Method

Step 1: Prepare a Cash Book if both the sides are not tallied. It appears as follows.

Cash Book

Receipts	Cash ₹	Bank ₹	Payments	Cash ₹	Bank ₹
To Balance b/d	xx	xx	By Balance B/d	xx	xx
To Cash Sales	xx	xx	(Bank overdraft)		
To Collection from Debtors	xx	xx	By Purchases	xx	x x
To B/R Collected	xx	xx	By Creditors	xx	xx
To Capital introduced	xx	xx	(Payment to		
To Sale of fixed asset	xx	xx	Creditors)	xx	xx
To Misc. Income	xx	xx	By Bills Payable paid	xx	xx
To Balance c/d	xx	xx	By Drawings		
			By Fixed Assets	xx	xx
			Purchases	xx	xx
			By Misc. Expenses	xx	xx
	x x	**x x**	By Balance c/d	**x x**	**x x**

If the difference appears on receipt side of the Cash Book, the missing information may be any of the items appearing on Receipt side of the cash book. If the difference appears on Payments side of the Cash Book the missing information maybe any of the items appearing on payments side of the Cash book.

Step 2: Prepare Total Debtors A/c on the basis of the information given.

Total Debtors A/c

	₹		₹
To Balance b/d	xx	By Cash /Bank	xx
To B/R (Dishonoured)	xx	By B/R A/c	xx
To Bank A/c	xx	By Discount A/c	xx
(Cheque Dishonoured)	xx	By Bad Debts A/c	xx
To Credit Sales	xx	By Sales Return A/c	xx
		By Balance c/d	xx
	x x		**x x**

The difference on debit side of Total Debtors A/c may be any of the items appearing on the debit side of Total Debtors A/c. The difference on credit side of Total Debtors A/c may be any of the items appearing on credit side Total Debtors A/c.

Step 3: Prepare Bills Receivable A/c

Bills Receivable A/c

	₹		₹
To Balance b/d	x x	By Cash/Bank A/c	x x
To Total Debtors A/c	x x	By Discount A/c	x x
(B/R drawn)		By Total Debtors A/c	x x
		(B/R Dishonoured)	
		By Total Creditors A/c	x x
		(B/R Endorsed)	
		By Balance c/d	x x
	x x		**x x**

If the difference appears on debit side of B/R A/c, it may be either opening balance or B/R Received . If the difference appears as credit side of B/R It may be any of the items appearing on credit side of B/R A/c.

Step 4: Prepare Total Creditors A/c

Total Creditors A/c

	₹		₹
To Cash/Bank A/c	x x	By Balance b/d	x x
To B/P A/c	x x	By Bills Payable A/c	x x
(Bills accepted)		(Dishonoured)	
To B/R A/c	x x	By Total Debtors A/c	x x
(Bills endorsed)		(Endorsed Bill Dishonoured)	
To Discount A/c	x x	By Bank A/c	x x
To Purchase Returns	x x	(Cheque Dishonoured)	
To Balance c/d	x x		
	x x		**x x**

If the difference appears on debit side of Total Creditors A/c. It may be any of the items on debit side of the A/c. If the difference appears on credit side of Total Creditors A/c. The difference may be any of the items on credit side of the A/c.

Step 5: Prepare Bills Payable A/c

Bill Payable A/c

	₹		₹
To Cash /Bank A/c	x x	By Balance b/d	x x
(Payment made)		By Total Creditors A/c	x x
To Total creditors A/c	x x	(B/P accepted)	

(B/P Dishonoured)			
To Balance c/d	xx		
	x x		**x x**

If the difference appears on date side of Bills Payable A/c, it may be any of the three items appearing on debit side of Bills Payable A/c. If the difference appears on credit side of Fixed Asset A/c, it mat be any one of the items appearing on credit side of Fixed Asset A/c.

Step 6: Prepare Revenue Expenses A/c.

Revenue Expenses A/c

	₹		₹
To Balance b/d	xx	By Balance b/d	xx
(Paid in advance in the beginning)		(Unpaid in the beginning)	
To Cash/Bank A/c	xx	By Trading and P&L A/c	xx
(Expenses paid)		(Expenses for the year)	
To Balance c/d	xx	To Balance c/d	xx
(Unpaid at the end)	—	(Paid in advance at the end)	—
	x x		**x x**

If the difference appears on debit side of the A/c, if may be considered any of the items on debit side of Expenses A/c. If the difference appears on credit side of the A/c. It may be any of the items appearing on credit side of the A/c.

Step 7: Prepare Revenue Income A/c.

	₹		₹
To Balance b/d	x x	By Balance b/d	x x
(Accrued in the beginning)		(Income not accrued at the beginning)	
To P & L A/c	x x	By Cash/Bank A/c	xx
(Income earned during the year)		(Received during the year)	
To Balance c/d	x x	By Balance c/d	xx
(Income not accrued at the end of the year)		(Accrued at the end of the year)	
	x x		**x x**

If the difference appears on debit side of the Income A/c, the missing information may be any one of the items appearing on debit side. If the difference appears on credit side of the A/c, the missing information may be any one of the items appearing on credit side of the A/c.

Step 8: Prepare Fixed Asset A/c.

Fixed Asset A/c

	₹		₹
To Balance b/d	xx	By Bank A/c	xx
To Bank A/c	xx	By Loss on Sale	xx
To Bank A/c	xx	By Depreciation A/c	xx
(Expenses)		By Balance c/d	xx
To Profit on sale	xx		—
	x x		**x x**

If the difference appears on debit side of the Fixed Asset A/c, it may be any one of the items appearing on debit side of the A/c. If the difference appears on credit side of Fixed Asset A/c, it may be any one of the items appearing on credit side of Fixed Asset A/c.

Step 9: Prepare Stock A/c/Goods A/c

Stock/Goods A/c

	₹		₹
To Opening Stock	xx	By Cost of Goods Sold	xx
To Purchases	xx	By Closing Stock	xx
	x x		**x x**

If the difference appears on debit side of the Stock A/c, it may either opening Stock or purchases. If the difference appears on credit side of Stock A/c, it may be either cost of goods sold or closing stock.

Step 10: Prepare a Trial Balance to verify arithmetical accuracy.

Step 11: Draw opening Statement of affairs to find out opening capital.

Step 12: Prepare Trading and P & L A/c and Balance Sheet as per usual principles.

Clues for Trading Missing Information

Missing information	Clues for trading
(i) Cash Sales	(a) Prepare Cash/Bank Summary
	(b) Cash Sales = Total Sales – Net Credit Sales
(ii) Net Credit Sales	(a) Prepare Total Debtors A/c
	(b) Net Credit Sales = Total Sales – Cash Sales – Sales Returns
	(c) Closing Debtors × $\frac{12}{\text{Credit Period}}$
(iii) Net Sales	(a) Cash Sales + Credit Sales – Sales Returns
	(b) Cost of Goods Sold + Gross Profit
(iv) Cost of Goods Sold	(a) Prepare Stock A/c
	(b) Opening Stock + Purchases + Direct Expenses – Closing Stock

	(c) Net Sales – Gross Profit
(v) Gross Profit	(a) Net Sales – Cost of Goods Sold
	(b) Net Sales $\times \dfrac{\text{Rate of G.P.}}{100}$
(vi) Cash purchases	(a) Prepare Cash/Bank Summary
	(b) Total Purchases – Net Credit Purchases
(vii) Net Credit purchases	(a) Prepare Total Creditors A/c
	(b) Total Purchases – Cash Purchases – Purchases Returns
	(c) Closing Creditors $\times \dfrac{12}{\text{Credit Period}}$
(viii) Net Purchases	(a) Prepare Stock A/c
	(b) Cost of Goods Sold + Closing Stock – Opening Stock
	(c) Cash Purchases + Credit Purchases – Purchases Returns
(ix) Drawing /Expenses/Repayment of Loans/Loan taken/Capital introduction	Prepare a Cash Book with Cash/Bank column.
(x) Amount collected from Debtors	(a) Prepare Total Debtors A/c
	(b) Prepare Cash/Bank A/c
(xi) Amount paid to Creditors	(a) Prepare Total Creditors A/c
	(b) Prepare Cash/Bank A/c
(xii) B/R accepted by Debtors	(a) Prepare Total Debtors A/c
	(b) Prepare Bills Receivable A/c
(xiii) B/P drawn by Creditors	(a) Prepare Total Creditors A/c
	(b) Prepare Bills Payable A/c
(xiv) Collection on account of Bills Receivable	(a) Prepare Cash/Bank A/c
	(b) Prepare Bills Receivable A/c
(xv) Payment on account of Bills Payable	(a) Prepare Cash/Bank A/c
	(b) Prepare Bills Payable A/c
(xvi) Cash Stolen	Prepare Cash/Bank A/c
(xvii) Cash/Bank Balance	Prepare Cash/Bank A/c
(xviii) Capital at the Beginning of the Year.	Prepare Opening Balance Sheet/ Statement of affairs

Illustration 1: Mr. Bhopatrao does not maintain proper books of accounts from the following information prepare trading and profit and loss account for the year ended 31-3-2016 and a balance sheet as on 1-4-2015:

Assets and Liabilities	1-4-2015 (₹)	31-3-2016 (₹)
Plant and Machinery	1,40,000	1,40,000
Furniture	10,000	10,000
Stock	44,000	60,000
Debtors	81,000	1,12,500
Creditors	27,000	22,500
6% Investment	50,000	50,000

Analysis of Other Transaction

Particulars	₹
Cash paid to creditors	1,98,000
Cash received from debtors	2,73,600
Salaries	54,000
Rent	7,500
Office expenses	19,000
Drawings	13,500
Additional capital introduced	10,000
Cash sales	35,000
Cash purchases	25,000
Discount received	3,150
Discount allowed	1,350
Return inward	4,500
Return outward	3,600
Cash on 1-4-2014	20,000
Bad debts	900

Depreciate plant and machinery @ 5% p.a. and furniture @ 10% p.a. and also provide interest receivable on investment.

Solution: In the Books of MR. BHOPATRAO Opening B/S as on 1-4-2015

Liabilities	Amount	Assets	Amount
Capital	3,18,000	Plant and Machinery	1,40,000
Creditors	27,000	Furniture	10,000
		Stock	44,000
		Debtors	81,000
		6% Investment	50,000
		Cash in hand	20,000
	3,45,000		**3,45,000**

Debtors A/c

Particulars	Amount	Particulars	Amount
To Balance b/d	81,000	By Cash	2,73,600
To Sales	3,11,850	By Discount	1,350
		By Return inward	4,500
		By Bad debts	900
		By Balance c/d	1,12,500
	3,92,850		**3,92,850**

Creditors A/c

Particulars	Amount	Particulars	Amount
To Cash	1,98,000	By Balance b/d	27,000
To Discount	3,150	By Purchases	2,00,250
To Return outward	3,600		
To Balance c/d	22,500		
	2,27,250		**2,27,250**

Cash A/c

Particulars	Amount	Particulars	Amount
To Balance b/d	20,000	By Creditors	1,98,000
To Debtors	2,73,600	By Salaries	54,000
To Cash sales	35,000	By Rent	7,500
To Capital introduced	10,000	By Office expenses	19,000
		By Drawings	13,500
		By Cash purchase	25,000
		By Balance c/d	21,600
	3,38,600		**3,38,600**

Trading and P & L A/c for the year ended 31st March 2016

Particulars		Amount	Particulars		Amount
To Opening Stock		44,000	By Sale:		
To Purchases:			Cash:	35,000	
Cash:	25,000		Credit:	3,11,850	
Credit:	2,00,250		(–) Return	(4500)	3,42,350
(–) Return	(3600)	2,21,650	By Closing Stock		60,000
To Gross Profit c/d		1,36,700			
		4,02,350			**4,02,350**
To Salaries		54,000	By Gross Profit b/d		1,36,700
To Rent		7,500	By Interest		3,000
To Office Expenses		19,000	By Discount Received		3,150
To Discount Allowed		1,350			

To Bad Debts		900		
To Depreciation:				
Plant:	7,000			
Furniture:	1,000	8,000		
To Net Profit c/d		52,100		
		1,42,850		**1,42,850**

Illustration 2: Mr. Ramji Supplies you the following information:

Particulars	1st April, 2015	31st March, 2016
Sundry Debtors	90,000	1,05,000
Stock	75,000	85,000
Sundry Creditors	55,000	60,000
Furniture	20,000	?
Machinery	1,75,000	?

Summary of Cash Transaction for the Year 2015-2016

Particulars	₹	Payments	₹
Opening balance	5,000	Creditors	1,75,000
Cash sales	55,000	Wages	80,000
Received from debtors	3,90,000	Salaries	75,000
Loan from Raj	50,000	Expenses	30,000
		Drawings	45,000
		Income tax	15,000
		Machinery purchased on 1st October 2015	50,000
		Closing Balance	30,000

Discount allowed were ₹ 6,000 and discount received ₹ 5,000. Bad debts written off were ₹ 4,000. Depreciation is to be provided on furniture @ 5% p.a. and machinery @ 10% p.a. expenses include payments of ₹ 1,000 which relates to 2016-17. Wages outstanding ₹ 7,500. Prepare trading profit and loss account of Mr. Ramji for the year ended 31st March, 2016 and balance sheet as on date.

Solution: **Opening Balance as on 1-4-2016**

Particulars	₹	Payments	₹
Sundry Creditors	55,000	Sundry Debtors	90,000
Capital (Balancing Figure)	3,10,000	Stock	75,000
		Furniture	20,000
		Machinery	1,75,000
		Cash and Bank	5,000
	3,65,000		**3,65,000**

Sundry Debtors A/c

Particulars	₹	Payments	₹
To Balance b/d	90,000	By Cash and Bank A/c	3,90,000
To Sales (Balancing Figure)	4,15,000	By Discount Allowed	6,000
		By Bad Debts	4,000
		By Closing Balance	1,05,000
	5,05,000		**5,05,000**

Sundry Creditors A/c

Particulars	₹	Payments	₹
To Cash and Bank A/c	1,75,000	By Balance b/d	55,000
To Discount Received	5,000	By Purchases (Balancing Figure)	1,85,000
To Balance c/d	60,000		
	2,40,000		**2,40,000**

Trading A/c for the Year Ended 31-03-2016

Particulars		₹	Payments		₹
To Opening Stock		75,000	By Sales		
To Purchases		1,85,000	Cash:	55,000	
To Wages	80,000		Credit:	4,15,000	4,70,000
(+) O/S	7,500	87,500	By Closing Stock		85,000
To Gross Profit c/d		2,07,500			
		5,55,000			**5,55,000**

Profit & Loss A/c for the Year Ended 31-3-2016

Particulars		₹	Payments	₹
To Salaries		75,000	By Gross Profit b/d	2,07,500
To Expenses	30,000		By Discount received	5,000
(–) Prepaid	1,000	29,000		
To Discount allowed		6,000		
To Bad debts		4,000		
To Depreciation:				
Furniture:	1,000			
Machinery:	20,000	21,000		
To Net Profit		77,500		
		2,12,500		**2,12,500**

Closing Balance Sheet as on 31-3-2016

Particulars		₹	Particulars		₹
Capital	3,10,000		Furniture	20,000	
(+) Net profit	77,500		(–) Depreciation	1,000	19,000
(–) Drawings	45,000		Machinery	1,75,000	

(–) Income tax	15,000	3,27,500	(+) Additions	50000	
			(–) Depreciation (17500 + 2500)		
				20,000	2,05,000
Loan from Raj		50,000	Cash and bank		30,000
Outstanding wages		7,500	Prepaid expenses		1,000
Sundry creditors		60,000	Sundry debtors		1,05,000
			Stock		85,000
		4,45,000			**4,45,000**

Illustration 3: From the following information, prepare Trading and Profit & Loss Account for the year ended 31st March, 2016 and Balance Sheet as on that date.

Particulars	31-3-2015	31-3-2016
Stock	41,600	31,200
Bills Receivable	20,200	?
Fixed Assets	57,200	57,200
Bills Payable	10,400	?
Debtors	20,800	?
Cash	5,200	?
Creditors	20,800	?

Cash Transaction During the Year 2015-16

Particulars	₹
Wages and salaries	52,000
Drawings	5,200
Received from debtors	1,45,600
Bills receivable encased	52,000
Payment to creditors	78,000
Bills payable paid	62,400
Sundry expenses	2,600
Cash sales	20,800

Non-cash Transaction During the Year 2015-16

Particulars	₹
Discount Allowed	5,200
Discount Received	7,800
Credit Purchases	1,56,000
Credit Sales	2,13,200
Bills Receivable Drawn	57,200
Bills Payable Accepted	72,800

Adjustment to be made for the preparation of Final Accounts:

(a) Wages Outstanding – ₹ 5,200

(b) 10% Depreciation on Fixed Assets

(c) 5% Provision for Doubtful Debts

(d) Prepaid Insurance ₹ 520

Solution: **Trading A/c for the year ended 31st March 2016**

Particulars	₹	₹	Particulars	₹	₹
To Opening stock		41,600	By Sales:		
To Purchases		1,56,000	Cash	20,800	
To Wages & salaries	52,000		Credit	2,13,200	2,34,000
Add: O/S wages	5,200	57,200			
To Gross Profit c/d		10,400	By Closing stock		31,200
		2,65,200			**2,65,200**

P & L A/c for the year ended 31st March 2016

Particulars	₹	₹	Particulars	₹	₹
To Discount Allowed		5,200	By Gross Profit b/d		10,400
To Sundry Expenses	2,600		By Discount Received		7,800
(–) Prepaid Insurance	520	2,080			
To Dep FA		5,720			
To Provision For Doubtful Debts		1,300			
To Net Profit c/d		3,900			
		18,200			**18,200**

Balance Sheet as on 31st March 2016

Liabilities	₹	₹	Assets	₹	₹
Capital Account	1,13,800		Fixed Assets	57,200	
(–) Drawings	5,200		(–) Dep 10%	5,720	51,480
	1,08,600		Prepaid Insurance		520
(+) Net Profit	3,900	1,12,500	Stock		31,200
Bills Payable		20,800	Bills Receivable		25,400
Creditors		18,200	Debtors	26,000	
O/S Wages		5,200	(–) Provision	1,300	24,700
			Cash/Bank		23,400
		1,56,700			**1,56,700**

W.N. Statement of Affairs as on 1-4-2015

Liabilities	₹	Assets	₹
Capital Account[Bal fig]	1,13,800	Stock	41,600
Bills Payable	10,400	Bills Receivable	20,200
Creditors	20,800	Fixed Assets	57,200
		Debtors	20,800
		Cash	5,200
	1,45,000		**1,45,000**

Bills Receivable A/c

Particulars	₹	Particulars	₹
To Balance b/d	20,200	By Cash/Bank	52,000
To Debtors	57,200	By Balance c/d	25,400
	77,400		**77,400**

Bills Payable A/c

Particulars	₹	Particulars	₹
To Cash/Bank	62,400	By Balance b/d	10,400
To Balance c/d	20,800	By Creditors	72,800
	83,200		**83,200**

Debtors A/c

Particulars	₹	Particulars	₹
To Balance b/d	20,800	By Bills Receivable	57,200
		By Cash/Bank	1,45,600
To Sales	2,13,200	By Discount Allowed	5,200
		By Balance c/d	26,000
	2,34,000		**2,34,000**

Creditors A/c

Particulars	₹	Particulars	₹
To Bills Payable	72,800	By Balance b/d	20,800
To Cash/Bank	78,000	By Purchases	1,56,000
To Discount Received	7,800		
To Balance c/d	18,200		
	1,76,800		**1,76,800**

Comprehensive Problem

Illustration 4: You are given (1) The Balance Sheet of Raj Kumar on 31st March, 2015 (2) A cash account for the year ended 31st March, 2016 and (3) Additional information. You are required to prepare a Trading and Profit and Loss A/c for the year ended 31st March, 2016 and a Balance Sheet as on that date.

Balance Sheet as on 31.3.2015

Liabilities	Amt. ₹	Assets	Amt. ₹
Creditors	20,000	Cash	5,000
Bills Payable	40,000	Banks	10,000
		Bills Receivable	20,000
Capital	1,00,000	Debtors	25,000
		Stock	20,000
		Furniture	10,000
		Plant	70,000
	1,60,000		**1,60,000**

Cash A/c for the year ended 31.3.2016

		Amt. ₹			Amt. ₹
Balance			Drawing		12,000
Cash	5,000		Wages		20,000
Bank	10,000	15,000	Payment to Creditors		35,000
Cash Sales		35,000	Bills paid		60,000
Collection from Debtors		80,000	Sundry Expenses		30,000
Bills Receivable		75,000	Rent, Rates and Taxes		20,000
			Balance:		
			Cash	3,000	
			Bank	25,000	28,000
		2,05,000			**2,05,000**

Additional Information

Particulars	₹
Debtors on 31st March, 2016	40,000
Creditors on 31st March, 2016	25,000
Bills Receivable on 31st March, 2016	30,000
Bills Payable on 31st March, 2016	50,000
Stock in Trade on 31st March, 2016	30,000
Bills Receivable in hand dishonoured during the year	5,000
Bills payable dishonoured	2,000
Bills Receivable endorsed	15,000

Bills receivable as endorsed dishonoured	2,000
Discount Allowed	1,000
Discount Received	2,000

(CS Modified)

Solution:

Dr. Bills Receivable A/c Cr.

	Amt. ₹		Amt. ₹
To Balance b/d	20,000	By Cash	75,000
To Debtors	1,05,000	By Debtors	5,000
		By Creditors	15,000
		By Balance c/d	30,000
	1,25,000		**1,25,000**

Dr. Bills Payable A/c Cr.

	Amt. ₹		Amt. ₹
To Cash	60,000	By Balance b/d	40,000
To Creditors	2,000	By Sundry Creditors	72,000
To Balance	50,000		
	1,12,000		**1,12,000**

Dr. Total Debtors A/c Cr.

	Amt. ₹		Amt. ₹
To Balance b/d	25,000	By Cash	80,000
To Bills Receivable	5,000	By Discount	1,000
To Creditors	2,000	By Bills Receivable	1,05,000
To Sales	1,94,000	By Balance c/d	40,000
	2,26,000		**2,26,000**

Dr. Total Creditors A/c Cr.

	Amt. ₹		Amt. ₹
To Cash	35,000	By Balance b/d	20,000
To Bills Receivable	15,000	By Bills Payable	2,000
To Discount	2,000	By Debtors	2,000
To Bills Payable	72,000	By Purchase	1,25,000
To Balance c/d	25,000		
	1,49,000		**1,49,000**

Dr. **Trading and Profit & Loss A/c** **Cr.**

	Amt. ₹			Amt ₹
To Opening Stock	20,000	By Sales		
To Purchases	1,25,000	Cash	35,000	
To Wages	20,000	Credit	1,94,000	2,29,000
To Gross Profit c/d	94,000	By Closing Stock		30,000
	2,59,000			**2,59,000**
To Sundry Experience	30,000	By Gross Profit b/d		94,000
To Rent, Rates and Taxes	20,000	By Discount		2,000
To Discount	1,000			
To Net Profit transferred to Capital A/c	45,000			
	96,000			**96,000**

Balance Sheet as on 31st March, 2016

Liabilities		Amt. ₹	Assets	Amt. ₹
Creditors		25,000	Cash	3,000
Bills Payable		50,000	Bank	25,000
			Bills Receivable	30,000
Capital:	1,00,000		Debtors	40,000
Add: Profit	45,000		Stock	30,000
	1,45,000		Furniture	10,000
Less: Drawings	12,000	1,33,000	Plant	70,000
		2,08,000		**2,08,000**

Two Years Information Given

Illustration 5: Balance Sheet of Mr. Jolly as on December 31, 2015 is as follows:

Liabilities	Amt. ₹	Assets	Amt. ₹
Creditors	20,855	Bank	15,615
Accruals	935	Debtors	31,150
Capital	65,360	Stock	20,835
		Fixtures	10,800
		Machinery at cost	8,750
	87,150		**87,150**

Following information is disclosed by the book:

	31.12.2015 ₹	31.12.2016 ₹
Cash received from debtors	37,160	43,110
Cash paid: Expenses	9,240	11,450
Creditors	16,345	37,835
Drawings	4,600	6,950
Sales	41,550	54,000
Purchases	21,150	40,900
Bad debts	1,350	Nil
Expenses outstanding	865	615
Stock in hand	—	16,000

No stock was taken on December 31, 2015 but it was agreed that it should be taken at a figure consistent with total rate of gross profit for two years. Depreciation is to be provided on machinery at 20% p.a. on original cost.

You are required to prepare Trading and Loss account for two years and the Balance sheet as on December 31, 2016

(IPCC Modified)

Solution: **Trading and Profit & Loss A/c**

Dr. **For the year Ended** **Cr.**

	31.12.15 ₹	31.12.16 ₹		31.12.15 ₹	31.12.16 ₹
To Opening Stock	20,835	12,900	By Sales	41,550	54,000
To Purchases	21,150	40,900	By Closing Stock	12,900	16,000
To Gross Profit c/d					
(at 30% on sales)	12,465	16,200			
	54,450	**70,000**		**54,450**	**70,000**
To Bad Debts	1,350	Nil	By Gross Profit b/d	12,465	16,200
To Expenses	9,170	11,200			
To Depreciation	1,750	1,750			
To Net Profit	195	3,250			
	12,465	**16,250**		**12,465**	**16,250**

Balance Sheet as on 31st December

Liabilities	2015 ₹	2016 ₹	Assets	2015 ₹	2016 ₹
Creditors	25,660	28,725	Bank	22,590	9,465
Outstanding Expenses	865	615	Debtors	34,190	45,080
Capital	60,955	57,255	Stock	12,900	16,000
			Fixtures	10,800	10,000
			Machinery		
			Less: Depreciation	7,000	5,250
	87,480	**86,595**		**87,480**	**86,595**

1. Closing stock for 31.12.2015 is the balancing figure.
2. Expenses for 2015. Expenses for 2016

Expenses	9,240	Expenses	11,450
Less: Opening Balance	935	*Less:* Opening Balance	865
	8,305		10,585
Add: Closing Balance	865	*Add:* Closing Balance	615
	9,170		**11,200**

3. Calculate of rate of Gross Profit

Combined Trading A/c
For the Period Ended 31st December, 2016

		Amt. ₹			Amt. ₹
To Stock		20,835	By Sales:		
To Purchases:			2014	41,550	
2014	21,150		2015	54,000	95,550
2015	40,900	62,050	By Stock		16,000
To Gross Profit		28,665			
		1,11,550			**1,11,550**

$$\text{Gross Profit Ratio} = \frac{28{,}665}{95{,}550} \times 100 = 30\%$$

4. Calculation of Bank Balance on 31st December, 2015 and 2016

	2015 ₹	2016 ₹		2015 ₹	2016 ₹
To Balance b/d	15,615	22,590	By Exp.	9,240	11,450
To Debtors	37,160	43,110	By Creditors	16,345	37,835
			By Drawings	4,600	6,950
			By Balance c/d		
			(Closing Balance)	22,590	9,465
	52,775	**65,700**		**52,775**	**65,700**

5. Calculation of debtors balance as on 31st Dec. 2015 and 2016

Total Debtors A/c

	2015 ₹	2016 ₹		2015 ₹	2016 ₹
To Balance b/d	31,150	34,190	By Cash	37,160	43,110
To Sales	41,550	54,000	By Bad debts	1,350	Nil
			By Balance c/d		
			(Balancing Figure)	34,190	45,080
	72,700	**88,190**		**72,700**	**88,190**

6. Calculation of creditors balance as on 31st Dec. 2014 and 2015

Total Creditors A/c

	2015 ₹	2016 ₹		2015 ₹	2016 ₹
To Cash	16,345	37,835	By Balance b/d	20,855	25,660
To Balance c/d (Bal. Fig.)	25,660	28,725	By Purchases	21,150	40,900
	42,005	**66,560**		**42,005**	**66,560**

7. Capital for 2015	₹	Capital for 2016	₹
Opening Balance	65,360	Opening Balance	60,955
Add: N.P.	195	*Add:* N.P.	3,250
	65,155		64,205
Less: Drawing	4,600	*Less:* Drawing	6,950
	60,955		**57,255**

Comprehensive Problem

Illustration 6: You are given:

1. The Balance sheet of Deepak as at 31st December 2015
2. The Cash Account for the year ended 31st December 2016
3. Additional information.

You are required to prepare a Trading and Profit and Loss Account for the year ended 31st December 2016 and Balance Sheet as on that date.

Balance Sheet as on 31st December 2015

Liabilities	Amt. ₹	Assets	Amt. ₹
Sundry Creditors	2,000	Cash	1,500
Bills Payable	4,000	Bills Receivable	2,000
Outstanding Wages	100	Sundry Debtors	2,500
Capital	9,900	Stock	2,000
		Furniture	1,000
		Plant and Machinery	7,000
	16,000		**16,000**

Cash A/c for the year ended 31.12.2016

Receipts	Amt. ₹	Payments	Amt. ₹
To Balance b/d	1,500	By Wages	2,000
To Cash Sales	3,500	By Drawings	1,200
To Debtors	8,000	By Payment to Creditors	3,500
To Bills Receivable	7,500	By Bills Payable	6,000
By Sundry Expenses	3,000		

		By Rent, Rates and Taxes	2,000
		By Balance c/d	2,800
	20,500		**20,500**

Additional Information:

		₹
Sundry Debtors	31.12.2016	4,000
Sundry Creditors	31.12.2016	2,500
Bills Receivable	31.12.2016	4,500
Bills Payable	31.12.2016	5,000
Stock	31.12.2016	3,000
Bills Receivable dishonoured during the year		500
Bills Payable dishonoured		200
Discount allowed		250
Bills Receivable endorsed		1,500
Bills Receivable endorsed dishonoured		200
Discount Received		650

Solution

Dr. **Bills Receivable A/c** **Cr.**

	Amt. ₹		Amt. ₹
To Balance b/d	2,000	By Cash	7,500
To Debtors (Balancing Figure)	12,000	By Debtors (B/R Dishonoured)	500
		By Creditors (B/R Endorsed)	1,500
		By Balance c/d	4,500
	14,000		**14,000**

Dr. **Total Debtors A/c** **Cr.**

	Amt. ₹		Amt. ₹
To Balance b/d	2,500	By Cash	8,000
To B/R (Dishonored)	500	By Discount	250
To Creditors		By Bills Receivable	12,000
(B/R Endorsed are Dishonoured)	200	By Balance c/d	4,000
To Sales (Balancing Figure)	21,050		
	24,250		**24,250**

Dr. **Bills Payable A/c** **Cr.**

	Amt. ₹		Amt. ₹
To Cash	6,000	By Balance b/d	4,000
To Creditors		By Creditors	
(B/P Dishonoured)	5,200	(Balancing Figure)	7,200
	11,200		**11,200**

Dr. Total Creditors A/c Cr.

	Amt. ₹		Amt. ₹
To Cash	3,500	By Balance b/d	2,000
To Discount	650	By Bills Payable (Dishonoured)	200
To Bills Payable	7,200	By Debtors	
To Bills Receivable	1,500	(B/R Endorsed dishonoured)	200
To Balance c/d	2,500	By Purchases (Balancing Figure)	12,950
	15,350		**15,350**

Trading and Profit & Loss A/c
for the year ended 31st December 2016

		Amt. ₹			Amt. ₹
To Opening Stock		2,000	By Sales:		
To Purchases		12,950	Cash Sales	3,500	
To Wages	2,000		Credit Sales	21,050	24,550
Less: for 1987	100	1,900			
To Gross Profit c/d		10,700	By Closing Stock		3,000
		27,550			**27,550**
To Rent, Rates and Taxes		2,000	By Gross Profit b/d		10,700
To Sundry Expenses		3,000	By Discount		650
To Discount		250			
To Net Profit transferred to Capital		6,100			
		11,350			**11,350**

Balance Sheet as on 31.12.2016

Liabilities		Amt. ₹	Assets	Amt. ₹
Sundry Creditors		2,500	Cash	2,800
Bills Payable		5,000	Sundry Debtors	4,000
Capital	9,900		Stock	3,000
Add: N.P	6,100		Bills Receivable	4,500
	16,000		Furniture	1,000
Less: Drawing	1,200	14,800	Plant & Machinery	7,000
		22,300		**22,300**

Where Cash Diary is Kept

Illustration 7: Bhuvanabhoopati who commenced business as a trader on 1.1.2015 has not kept proper records of his transaction for the year ended 31st December, 2015 He, however, has kept a cash dairy from which he has extracted the following:

Cash A/c

Receipts	Amt. ₹	Payments	Amt. ₹
Amounts withdrawals from		Postage Expenses	720
Bank on various dates	3,520	Conveyance Expenses	2,400
		License Fees	60
		Miscellaneous Expenses	220
		Balance c/d	120
	3,520		**3,520**

An analysis of his Bank statements reveals the following deposits and withdrawals:

Deposits:	₹
Capitals introduced	50,000
Cash Sales	2,40,000
Collection from Debtors	20,000
Withdrawals:	
Cash withdrawals for petty expenses	3,520
Rent paid	2,200
Electricity Bills paid	660
Payments to suppliers	1,80,000
Insurance	12,000
Salaries	3,600
Furniture & Fixtures purchased	24,000
Advance income-tax paid	12,000
Typewriter Purchased	2,000
Personal drawings	36,000

1. All fixed assets were purchased in early January. Furniture is to be depreciated at 10% and Typewriter at 15%.
2. Rent and Electricity Payable to the landlord are in arrear for December, 2015
3. At the end of the year, debtors were ₹ 5,000, creditors ₹ 2,700 and stock ₹ 39,000.

You are required to prepare:

(a) A summary of the Bank A/c and ascertain the closing balance.

(b) Trading and Profit & Loss A/c for the year ended 31st December, 2015

(c) Balance Sheet as at that date.

(CIMA, Modified)

Solution: **(a) Book of Bhuvanabhoopati**

Dr. **Bank A/c for the year ended 31.12.2015** **Cr.**

Receipts	Amt. ₹	Payments	Amt. ₹
To Capital A/c	50,000	By Furniture and Fixtures	24,000
To Cash Sales	2,40,000	By Sundry Creditors	1,80,000

To Sundry Debtors	20,000	By Typewriter	2,000
By Insurance	12,000		
		By Cash for Petty Expenses	3,520
		By Rent	2,200
		By Electricity	660
		By Salaries	3,600
		By Advance Income Tax	12,000
		By Drawings	36,000
		By Balance c/d	34,020
	3,10,000		**3,10,000**
To Balance b/d	34,020		

(b) **Trading and Profit & Loss A/c**

Dr. **for the year ended 31.12.2015** **Cr.**

	Amt. ₹			Amt. ₹
To Purchases	1,82,700	By Sales:		
To Gross Profit c/d	1,21,300	Cash	2,40,000	
		Credit	25,000	2,65,000
		By Stock - Closing		39,000
	3,04,000			**3,04,000**
To Rent	2,400	By Gross Profit b/d		1,21,300
To Electricity	720			
To Insurance	12,000			
To Salaries	3,600			
To Postage	720			
To Conveyance	2,400			
To License Fees	60			
To Miscellaneous Expenses	220			
To Depreciation:				
Furniture	2,400			
Typewriter	300			
To Net Profit transferred to Capital A/c	96,480			
	1,21,300			**1,21,300**

(c) **Bhuvanabhoopati**

Dr. **Balance Sheet as at 31.12.2015** **Cr.**

Liabilities		Amt. ₹	Assets	Amt. ₹
Sundry Creditors		2,700	Current Assets:	
Outstanding Expenses:			Cash in Hand	120
Rent	200		Cash at Bank	34,020
Electricity	60	260	Stock	39,000

Capital:			Sundry Debtors		5,000
Introduced	50,000		Fixed Asset:		
Add: Net Profit	96,480		Furniture	24,000	
	1,46,480		*Less:* Depreciation	2,400	21,600
			Typewriter	2,000	
Less: Advance Tax 12,000			*Less:* Depreciation	300	1,700
Drawing 36,000					
	48,000	98,480			
		1,01,440			**1,01,440**

Total Debtors A/c

	Amt. ₹		Amt. ₹
To Sales (Balancing Figure)	25,000	By Bank	20,000
		By Balance c/d	5,000
	25,000		**25,000**

Total Creditors A/c

	Amt. ₹		Amt ₹
To Bank b/d	1,80,000	By Purchases (Balancing Figure)	1,82,700
To Balance c/d	2,700		
	1,82,700		**1,82,700**

Note: Advance Income Tax paid should be treated as drawings.

Deposit for Rent Given

Illustration: 8: Rama Reddi is a retail merchant who keeps only a memorandum of his transaction. By going through his notes and records, you are able to ascertain the following:

1. Summary of Bank A/c (1.4.2015 to 31.3.2016)

	Amt. ₹		Amt. ₹
To Balance b/d	2,500	By Payments to Creditors	2,20,000
To Cash deposited	2,30,000	By Rent paid	12,000
To Balance c/d	13,100	By Electricity Charges	3,600
		By Drawing	10,000
	2,45,600		**2,45,600**

2. Other Cash Transactions

	₹
Cash Purchases	20,000
Office Expenses paid	20,500
Cash Balance on 1.4.2015	500
Cash Balance on 31.3 2016	1,000

3. Other information
   (a) Stock in trade:

As on 1.4.2015	50,000
As on 31.3.2016	75,000

   (b) A deposit of ₹ 3,000 for rent lies with the landlord.
   (c) Furniture with a written down value of ₹ 30,000 on 1.4.2015 is subject to depreciation at 10% p.a.
   (d) Electricity bills to be paid on 1.4.2015 and 31.3.2016 were for ₹ 400 and ₹ 600 respectively.
   (e) Amount due to creditors on 1.4.2015 and 31.3.2016 were ₹ 10,600 and ₹ 21,000 respectively.
   (f) An amount of ₹ 2,000 being irrecoverable from customer is to be written off as bad.
   (g) Debtors on 1.4.2015 and 31.3.2016 were ₹ 20,000 and ₹ 17,000 (excluding bad debts of ₹ 2,000) respectively.

From the above information, prepare Rama Reddi's:

(i) Trading and Profit & Loss Account for the year ended 31st March, 2016; and
(ii) Balance Sheet as at 31st March, 2016

(CIMA, London Modified)

Solution:

Mr. Rama Reddi
Trading and Profit & Loss A/c
Dr. for the year ended 31.3.2016 Cr.

		Amt. ₹		Amt. ₹
To Opening Stock		50,000	By Sales	2,70,000
To Purchases:			By Closing Stock	75,000
Cash	20,000			
Credit	2,30,400	2,50,400		
To Gross Profit c/d		44,600		
		3,45,000		**3,45,000**
To Office Expenses		20,500	By Gross Profit b/d	44,600
To Rent		12,000		
To Electricity		3,800		
To Depreciation on Furniture		3,000		
To Bad Debts		2,000		
To Net Profit transferred to Capital A/c		3,300		
		44,600		**44,600**

Mr. Rama Reddi
Balance Sheet as on 31st March, 2016

Liabilities		Amt. ₹	Assets		Amt. ₹
Bank Overdraft		13,100	Cash in hand		1,000
Electricity Expenses Payable		600	Sundry Debtors		17,000
Sundry Creditors		21,000	Stock in trade		75,000
Capital:			Rent Deposit		3,000
Balance	95,000		Furniture	30,000	
Add: Net Profit	3,300		*Less:* Depreciation	3,000	27,000
	98,300				
Less: Drawings	10,000	88,300			
		1,23,000			**1,23,000**

Working Notes:

Cash A/c

	Amt. ₹		Amt. ₹
To Balance b/d	500	By Bank	2,30,000
To Receipts from Debtors		By Purchases	20,000
(Balancing Figure)	2,71,000	By Office Expenses	20,500
		By Balance c/d	1,000
	2,71,500		**2,71,500**

Sundry Debtors A/c

	Amt. ₹		Amt. ₹
To Balance b/d	20,000	By Cash	2,71,000
To Sales (Balancing Figure)	2,70,000	By Bad Debts	2,000
		By Balance c/d	17,000
	2,90,000		**2,90,000**

Sundry Creditors A/c

	Amt. ₹		Amt. ₹
To Bank	2,20,000	By Balance b/d	10,600
To Balance c/d	21,000	By Purchases (Balancing Figure)	2,30,400
	2,41,000		**2,41,000**

Balance Sheet as on 31st March, 2015

Liabilities	Amt. ₹	Assets	Amt. ₹
Electricity Expenses Payable	400	Cash in hand	500
Sundry Creditors	10,600	Cash at Bank	2,500
Capital (Balancing Figure)	95,000	Sundry Debtors	20,000

		Stock in Trade	50,000
		Rent Deposit	3,000
		Furniture	30,000
	1,06,000		**1,06,000**

Note: Deposits for rent with the landlord should be shown as on asset.

Analysis of Bank Statement Given

Illustration 9: Mr. Ambani keeps his boos on Single-entry System. You are required to prepare his Trading and Profit & Loss Account for the year ended 31st March, 2016 from the following information and also to show the balance sheet as on that date:

1. A scrutiny of various Ledger Accounts reveals the following:

	As on 1.4.2015	As on 31.3.2016
Stock in hand	4,500	6,000
Sundry Debtors	24,000	27,000
Sundry Creditors	15,000	12,500
Furniture	6,000	8,000
Machinery	30,000	30,000
Bills Receivable	20,000	21,000
Bills Payable	16,500	14,500
Reserve for Bad and Doubtful Debts	1,200	1,350

2. An analysis of the Bank Statements for the year ended 31st March, 2016 is as follows:

Receipts	Amt. ₹	Payments	Amt. ₹
To Sundry Debtors	68,000	By Balance b/f (as on 1.4.2014)	6,000
To Cash Sales	24,400	By Sundry Creditors	40,000
To Bills Receivable		By Cash Purchases	16,000
(Proceeds of a B/R		By Interest on Bank Overdraft	500
for ₹ 8,000 on discounting)	7,800	By Salaries	7,500
		By Insurance	3,000
		By General Charges	2,500
		By Rent and Taxes	1,000
		By Drawings	4,000
		By Carriage Inwards	2,500
		By Freight and Duty	1,500
		By Furniture	2,000
		By Bills Payable	12,000
		By Balance b/d	1,700
	1,00,200		**1,00,200**

3. There was a bad debt of ₹ 400 which was written off.
4. He had allowed ₹ 450 as discount and earned ₹ 300 as discount.
5. He also paid ₹ 1,500 for expenses.
6. Depreciation has to be Provided at 5% on Machinery and 10% on Furniture per annum for full year.
7. Interest on capital is to be allowed at 10% per annum.

(CS Inter Modified)

Solution:

Mr. Ambani
Trading and Profit & Loss A/c
for the year ended 31st March, 2016

Dr. **Cr.**

		Amt. ₹			Amt. ₹
To Opening Stock		4,500	By Sales:		
To Purchases:			Cash	24,400	
Cash	16,000		Credit	80,850	1,05,250
Credit	47,800	63,800	By Closing Stock		6,000
To Freight and Duty		1,500			
To Carriage Inwards		2,500			
To Gross Profit c/d		38,950			
		1,11,250			**1,11,250**
To Interest on Bank Overdraft		500	By Gross Profit b/d		38,950
To Salaries		7,500	By Discount received		300
To Insurance Charges		3,000			
To General Charges		2,500			
To Expenses Outstanding		1,500			
To Rent and Taxes		1,000			
To Discount allowed		450			
To Discount (on bill discounting)		200			
To Bad Debts		400			
To Reserve for Bad Debts					
(5% on ₹ 27,000)	1,350				
Less: Old Reserve	1,200	150			
To Depreciation:					
Machinery 5%					
on ₹ 30,000	1,500				
Furniture 10%					
on ₹ 8,000	800	2,300			

To Interest on Capital:			
10% on ₹ 45,800	4,580		
To Net Profit			
transferred to Capital A/c	15,170		
	39,250		**39,250**

Working Notes:

Mr. Ambani Balance Sheet as on 31st March, 2015

Liabilities		Amt. ₹	Assets		Amt. ₹
Capital as on 1.4.2014	45,800		Machinery	30,000	
Add: Net Profit	15,170		*Less:* Depreciation	1,500	28,500
	60,970		Furniture	8,000	
Interest on Capital	4,580		*Less:* Depreciation	800	7,200
	65,550		Stock in Trade		6,000
Less: Drawings	4,000	61,550	Sundry Debtors	27,000	
Bills Payable		14,500	*Less:* Reserve for Bad Debts	1,350	25,650
Sundry Creditors		12,500	Bills Receivable		21,000
Outstanding Expenses		1,500	Cash at Bank		1,700
		90,050			**90,050**

Total Debtors A/c

	Amt. ₹		Amt. ₹
To Balance b/f	24,000	By Bank	68,000
To Sales (Balancing Figure)	80,850	By Bills Receivable	9,000
		By Discount allowed	450
		By Bad Debts	400
		By Balance c/d	27,000
	1,04,850		**1,04,850**

Total Creditors A/c

	Amt. ₹		Amt. ₹
To Bank	40,000	By Balance b/f	15,000
To Bills Payable	10,000	By Purchases (Balancing Figure)	47,800
To Discount Received	300		
To Balance c/d	12,500		
	62,800		**62,800**

Analysis of Bank Statement Given

Illustration 10: (Mr. Manish, a retailer in Mumbai adds 25% to cost of goods sold to arrive at sales price. His financial position as on 30th June, 2015 was as under:

	₹
Plant/Machinery	50,000
Stock (at cost)	38,250
Debtors	71,750
Cash at Bank	22,000
Creditors	30,000
Loan from Vivek	20,000

During the year ended 30th June, 2016, Mr. Manish

(a) Paid ₹ 1,16,750 to creditors for goods.

(b) Repaid ₹ 5,000 of Vivek's Loan

(c) Purchased a typewriter ₹ 7,000.

(d) Withdrew ₹ 800 p.m. From Bank for domestic use.

(e) Paid into Bank Personal Lottery Prize of ₹ 3,000.

(f) Paid Income Tax ₹ 6,000

(g) Sold goods on credit ₹ 1,46,100

(h) Spent business Expenses ₹ 9,000.

(i) Goods taken for personal use ₹ 3,120.

On 30.6.2016 stock at cost was ₹ 40,000, debtors totaled ₹ 70,000 and creditors were ₹ 35,000. On that date Bank balance was ₹ 19,500. Depreciate plant and typewriter by 20% p.a.

Prepare Manish's Final Account.

(All your workings be shown).

(University Modified)

Solution: **Mr. Manish Balance Sheet as on 30th June 2015**

Liabilities	Amt. ₹	Assets	Amt. ₹
Capital (Balancing Figure)	1,32,000	Plant and Machinery	50,000
Creditors	30,000	Stock	38,250
Loan from Vivek	20,000	Debtors	71,750
		Cash at bank	22,000
	1,82,000		**1,82,000**

Total Debtors A/c

	₹		₹
To Balance b/d	71,750	By Bank	1,47,850
To Sales	1,46,100	By Balance c/d	70,000
	2,17,850		**2,17,850**

Total Creditors A/c

	₹		₹
To Balance b/d	1,16,750	By Balance b/d	30,000
To Sales	35,000	By Purchases	1,21,750
	1,51,750		**1,51,750**

Trading and P & L A/c
for the year ended 30th June, 2016

	₹		₹
To Opening Stock	38,250	By Sales	1,46,100
To Purchases	1,21,750	By Goods taken For Personal use	3,120
To Gross Profit c/d	29,220	By Closing Stock	40,000
	1,89,220		**1,89,220**
To Business Expenses	9,000	By Gross Profit b/d	29,220
To Depreciation			
Plant and Machinery	10,000		
Typewriter	1,400		
To Net Profit	8,820		
	29,220		**29,220**

Balance Sheet as on 30th June, 2016

Liabilities		Amt. ₹	Assets		Amt. ₹
Capital	1,32,000		Plant and Machinery	50,000	
Add: Additional Capital	3,000		*Less:* Depreciation	10,000	40,000
Add: Net Profit	8,820		Typewriter	7,000	
	1,43,820		*Less:* Depreciation	1,400	5,600
Less: Drawings	9,600		Closing Stock		40,000
Less: Income tax	6,000		Debtors		70,000
Less: Goods withdrawn	3,120	1,25,100	Bank		19,500
Loan from Vivek	20,000				
Less: Repaid	5,000	15,000			
Creditors		35,000			
		1,75,100			**1,75,100**

Difference in Trading A/c is assumed to be goods taken for personal use not recorded.

Illustration 11: On April, 2015 Mr. Silgardo bought for ₹ 50,000 a business whose assets and liabilities are shown below. The business carried on its operation in a rented shop from and it sold cosmetics and confectionery. The business did not keep double-entry accounts. But you are provided with the following information.

(i) Balance Sheet of the Company Mr. Silgardo as on 31st March, 2015

Liabilities	Amt. ₹	Assets	Amt. ₹
Capital Amount	50,000	Furniture & Fitting at Cost	30,000
Profit & Loss A/c	10,500	Stock at cost:	
Creditors		Cosmetics	5,000
Cosmetics	2,500	Confectionery	3,000
Confectionery	2,000	Sundry Debtors:	
Outstanding Rent	500	Confectionery	500
		Prepaid Rates & Insurance	2,500
		Balance with Bank	23,500
		Cash in hand	1,000
	65,500		**65,500**

(ii) Analysis of the Bank Statements for the year ended March 31st, 2016

	₹
Paid in cash	2,45,000
Withdrawn for:	
Purchase of Cosmetics	1,00,000
Purchase of Confectionery	1,10,000
Repairs	4,000
Rent	6,000
Rates and Insurance	10,000
Electricity	4,000
Mr. Sligardo	15,000

(iii) The Following were Paid in Cash

Salaries	15,000
Confectionery Purchases	1,500
Trade Expenses	1,250
Cosmetics purchases	5,000

(iv) Mr. Silgardo had taken from the shop Cosmetics for his own consumption and paid into the business the cost price of ₹ 4,550.

(v) The following are the gross profit percentages with reference to sales:

Cosmetics 9%

Confectionery 30%

(vi) On 31st March, 2016 there were:

	Stock at cost ₹	Debtors/Prepayments and Cash ₹	Liabilities ₹
Cosmetics	4,850	Nil	2,000
Confectionery	3,500	1,000	3,000
Rent	-	-	500
Rates & Insurance	-	2,750	-
Cash on hand	-	250	-
Accountancy/Audit fees	-	-	2,000

(vii) Mr. Silgardo has instructed you to regard any shortage in cash as being due to amounts withdrawn by him.

You are required to prepare:

(a) The Trading and Profit and Loss Account for the year ended March 31, 2015 showing separately the Gross Profit from (i) Cosmetics and (ii) Confectionery.

(b) The Balance Sheet as at March 31, 2016

(c) Total Debtors and Total Creditors Account and

(d) An account in columnar form for cash

(IPCC Modified)

Solution:

Dr. Total Debtors A/c Cr.

	Cosmetics ₹	Confectionery ₹		Cosmetics ₹	Confectionery ₹
To Balance b/d	–	500	By Cash A/c (Balancing Figure)	1,10,000	1,59,500
To Sales	1,10,000	1,60,000	By Balance c/d	—	1,000
	1,10,000	**1,60,500**		**1,10,000**	**1,60,500**

Dr. Total Creditors A/c Cr.

	Cosmetics ₹	Confectionery ₹		Cosmetics ₹	Confectionery ₹
To Bank A/c	1,00,000	1,10,000	By Balance b/d	2,500	2,000
To Cash A/c	5,000	1,500	By Purchases A/c (Balancing Figure)	1,04,500	1,12,000
To Balance c/d	2,000	3,000			
	1,07,000	**1,14,500**		**1,07,000**	**1,14,500**

Dr. **Cash Book** **Cr.**

	Cash ₹	Bank ₹		Cash ₹	Bank ₹
To Balance b/d	1,00,000	23,500	By Creditors:		
To Drawing of goods	4,550	—	Cosmetics	5,000	1,00,000
and sales (at cost)			Confectionery	1,500	1,10,000
To Debtors:			By Bank A/c	2,45,000	
Cosmetics	1,10,000	—	By Repairs A/c	—	4,000
Confectionery	1,59,500	—	By Rent A/c	—	6,000
To Cash A/c	—	2,45,000	By Rates and		
			Insurance A/c	—	10,000
			By Electricity A/c	—	4,000
			By Drawing A/c	—	15,000
			By Salaries A/c		
			By Trade	15,000	—
			Expenses A/c	1,250	—
			By Drawings A/c	7,050	—
			(Balancing Figure)		
			By Balance c/d	250	19,500
	2,75,050	**2,68,500**		**2,75,050**	**2,68,500**

Trading & Profit & Loss A/c

Dr. **for the year ended 31st March 2016** **Cr.**

	Cosmetics ₹	Confectionery ₹		Cosmetics ₹	Confectionery ₹
To Opening Stock A/c	5,000	3,000	By sales A/c	1,10,000	1,60,000
To Purchases A/c	1,04,500	1,12,500	By Goods for	4,550	
To Gross Profit A/c	9,900	48,000	Personal Use		
			By closing Stock A/c	4,850	3,500
	1,19,400	**1,63,500**		**1,19,400**	**1,63,500**
To Salaries A/c		15,000	By Gross Profit b/d		
To Rates &			Cosmetics		9,900
Insurance A/c		9,750	Confectionery		48,000
(10,000 + 2,500 – 2,750)					
To Rent A/c					
(6,000 + 500 – 500)		6,000			
To Repair A/c	4,000				
To Electricity A/c	4,000				
To Trade					
Expenses A/c	1,250				
To Audit Fees A/c	2,000				
To Net Profit	15,900				
	57,900				**57,900**

Balance Sheet as at 31st March, 2016

Liabilities		Amt. ₹	Assets	Amt. ₹
Capital (including	60,500		Fixture & Fittings	30,000
Profit & Loss)			Stock (4,850 + 3,500)	8,350
Add: Profit	15,900		Debtors	1,000
Less: Drawings	22,050	54,350	Bank	19,500
(15,000 + 7,050)			Cash	250
Creditors		5,000	Prepaid Insurance	2,750
Audit Fees		2,000		
Rent outstanding		500		
		61,850		**61,850**

Closing Balance of Cash, Creditors and Debtors not Given

Illustration 12: Thomas does not maintain his books on the Double-entry System and Bank Account. From the following information, prepare Profit and Loss Account and Balance Sheet as at June 30, 2016.

(A)	Assets and Liabilities	30.6.2015 ₹	30.6.2016 ₹
	Stock	19,800	1,13,200
	Creditors	31,000	14,500
	Debtors	1,18,000	1,25,000
	Premises	90,000	90,000
	Furniture	11,000	11,500
	Air Conditioner	15,000	15,000

(b) Creditors as at 30.6.2015, include ₹ 15,000 for Purchases of Air Conditioner.

(c) Cash transaction:

		₹
	Cash as at 1st July, 2015	15,000
	Collection from Customers	1,60,800
	Payments to Creditors (Trade)	1,44,000
	Rent, Rates and Taxes	11,500
	Salaries	1,12,000
	Sundry Expenses	18,000
	Sundry Income	16,500
	Drawings by Thomas	30,000
	Loan from Mrs. Fernandes	23,000
	Capital introduced	12,000
	Cash Sales	11,500
	Cash Purchases	15,000
	Paid to Creditors for Air Conditioner	15,000
(d)	Bad debts written off	1,200

(I.C.W.A., Adapted)

Solution:

Dr. Trading and Profit and Loss Account for the year ended 30.6.2016 Cr.

	₹	₹		₹	₹
To Opening Stock		19,800	By Sales:		
To Purchases:			- Cash	11,500	
- Cash	15,000		- Credit	1,69,000	1,80,500
- Credit	1,42,500	1,57,500	By Closing Stock		1,13,200
To Gross Profit c/d		1,16,400			
		2,93,700			**2,93,700**
To Salaries		1,12,000	By Gross Profit b/d		1,16,400
To Sundry Expenses		18,000			
To Rent, Rates & Taxes		11,500	By Sundry Income		16,500
			By Net Loss		9,800
To Bad Debts		1,200	Carried to Capital A/c		
		1,42,700			**1,42,700**

Balance Sheet of Thomas as at 30.6.2016

Liabilities	₹	₹	**Assets**	₹
Capital Account:			Premises	90,000
Balance b/d (opening)	2,37,800		Furniture	11,500
Add: Additional Capital	12,000		Air Conditioner	15,000
			Stock	1,13,200
	2,49,800		Sundry Debtors	1,25,000
Less: Net Loss	9,800			
	2,40,000			
Less: Drawing	30,000	2,10,000		
Loan		23,000		
Creditors		14,500		
Bank Overdraft		1,07,200		
		3,54,700		**3,54,700**

Working Notes:

1. Furniture Purchased:

   Furniture on 30.6.2015 was ₹ 11,000 and on 30.6.2016 is ₹ 11,500. It is assumed that furniture worth ₹ 500 must have been purchased during the year and paid in cash.

2. Bad debts are written off, i.e., are already to Sundry Debtors Account, hence not deducted once again from Closing Debtors but only shown on the debit of the P& L A/c.

3. Calculation of Cash/Bank balance.

Dr. **Cash/Bank Account** **Cr.**

Receipts	₹	Payments	₹
To Balance b/d	15,000	By Creditors (Trade)	1,44,000
To Debtors	1,60,800	By Rent, Rates and Taxes	11,500
To Sundry Income	16,000	By Salaries	1,12,000
To Capital Introduced	12,000	By Sundry Expenses	18,000
To Loan	23,000	By Drawings	30,000
To Sales	11,500	By Purchases	15,000
To Balances c/d	1,07,200	By Furniture	500
(balancing figure O.D.)	–	By Creditors	15,000
	3,54,700		**3,54,700**

4. Caculation of Credit Purchases.

Dr. **Total Creditors Account** **Cr.**

	₹		₹
To Cash	1,44,000	By Balance b/d	31,000
To Cash (Air Conditioner)	15,000	Credit Purchases	1,42,500
To Balance c/d)	14,500	(balance figure)	–
	3,46,000		**3,46,000**

5. Calculation of Credit Sales

Dr. **Total Debtors Account** **Cr.**

	₹		₹
To Balance b/d	1,18,000	By Cash	1,60,800
To Credit Sales (Balancing Figure)	1,69,000	By Bad Debts	1,200
		By Balance c/d	1,25,000
	2,87,000		**2,87,000**

6. Calculation of Opening Capital

Dr. **Balance Sheet as on 1st July, 2015** **Cr.**

	₹		₹
Sundry Creditors	31,000	Furniture	11,000
Capital Account on 1-7-11	2,37,800	Premises	90,000
(Balancing Figure)		Air Conditioner	15,000
		Sundry Debtors	1,18,000
		Stock-in-trade	19,800
		Cash	15,000
	2,68,800		**2,68,800**

SELF ASSESSMENT QUESTIONS

Multiple Choice Questions

(i) Capital in the beginning of the year is ascertained by the preparing:
  (a) Cash account
  (b) Opening statement of affairs
  (c) Total debtors

(ii) Capital at the end of the year is ascertained by the preparing:
  (a) Cash account
  (b) Closing statements of affairs
  (c) Total Creditors A/c

(iii) Opening Stock can ascertained by the preparing:
  (a) Memorandum Trading A/c
  (b) Total Creditors A/c
  (c) Opening statements of affairs

(iv) Closing balance on Creditors A/c can be ascertained from:
  (a) Cash account
  (b) Total Creditors Account
  (c) Balance Sheet at the end of the year

(v) Credit Sale can be ascertained from:
  (a) Cash account
  (b) Total Debtors Account
  (c) Balance Sheet

(vi) If the rate of gross profit is 25% on sales and the cost of goods sold is ` 1,00,000 the gross profit will be:
  (a) ₹ 25,000
  (b) ₹ 33,333
  (c) ₹ 28,000

  [**Ans.:** (i) – (b), (ii) – (b), (iii) – (a), (iv) – (b), (v) – (b), (vi) – (b).]

MATCH THE FOLLOWING COLUMNS.

	Column A		Column B
(i)	Balance Sheet	(a)	Single-entry System
(ii)	Single-entry System	(b)	A Daily Summary of Cash
(iii)	Bad Debts	(c)	Double-entry System
(iv)	Disclosure of Policy	(d)	Statements of Affairs
(v)	Cash Book	(e)	Debtors
(vi)	Account from Incomplete Records		

[**Ans.:** (i) – (b), (ii) – (b), (iii) – (a), (iv) – (b), (v) – (b), (vi) – (b).]

FILL IN THE BLANKS WITH SUITABLE WORDS.

1. Single-entry accounting system is a method of book keeping relying on a _______ accounting entry to maintain financial information.
2. The _______ is really no system at all for keeping accounts.
3. Cash received from him will be recorded both in the cash account and _______.
4. No trial balance can be taken out from _______.
5. Chances of mischief or fraud remaining undetected are _______.
6. single-entry is nowadays known as _______ from incomplete records.
7. Single-entry system is an _______ of recording financial transactions.
8. Purchase of machinery on credit will _______ at all till payment is made.
9. _______ is called statement of affairs.
10. Prepare a _______ to verify arithmetical accuracy.

[**Ans.:** (1) One-sided, (2) Single-entry System, (3) Customer Account, (4) Single-entry System, (5) High, (6) Preparation of Account, (7) Economical System, (8) Not be Recorded, (9) Balance Sheet, (10) Trial Balance.]

STATE WHETHER TRUE OR FALSE:

1. Limited companies also can adopt single-entry system.
2. Single-entry system is suitable to small organisations.
3. Trial Balance can be prepared under single entry system.
4. Nominal accounts are maintained under single entry system.
5. Statement of affairs shows financial position on a certain date under single-entry system.
6. Single-entry system follows the basic principles of accounting.
7. Trial Balance is prepared under single-entry system to verify accuracy.
8. Gross profit cannot be ascertained under single-entry system.

9. Under single-entry system, only single entry is made in the books of accounts.
10. Credit sales can be ascertained from debtors account.
11. Credit purchases can be ascertained from creditors account.
12. Under single entry, cash account is maintained with receipts and payments.
13. Single-entry system is followed by large sized companies.
14. Closing stock is ascertained by preparing stock register.
15. Limited companies have to maintain their accounts as per single-entry system.
16. Under single-entry system, personal accounts of debtors and creditors are maintained.
17. Under conversion method, credit purchases are ascertained from Creditors Account.
18. Under single-entry system, opening capital is ascertained by preparing statement of affairs.
19. Collection from debtors is ascertained from debtors account.
20. Payment to suppliers is ascertained from creditors account.
21. Credit sales are ascertained by preparing sales register.

[**Ans.:** (1) False, (2) True, (3) False, (4) False, (5) True, (6) False, (7) True, (8) True, (9) True, (10) True, (11) True, (12) True, (13) False, (14) True, (15) False, (16) True, (17) True, (18) True, (19) True, (20) True, (21) True.]

THEORY QUESTIONS

1. What is Single-entry System of Bookkeeping?
2. Explain the main features of Single-entry System?
3. State the limitations of single-entry system.
4. State the procedure of calculating profit or loss under single-entry system.
5. How is the single-entry converted into double entry?
6. What are the advantages and disadvantages of single-entry?
7. What is a statements of affairs?
8. What is the difference between a statements of affairs and balance sheet?
5. Balance sheet.
6. Financial transactions.
7. Double-entry System.
8. Bad debts.
9. Bills Recivable.
10. Creditor account.

PRACTICAL QUESTIONS

1. Calculate credit sales from the following figures:

	₹		₹
Opening Balance of Debtors	20,000	Discount Allowed	4,000
Cash Received from Debtors	95,000	Closing Balance of Debtors	18,000
Bad Debts Written Off	2,000		

(**Ans.:** Credit Sale ₹ 99,000)

2. Calculate credit purchase from the following information:

	₹		₹
Opening Balance of Creditors	15,000	Discount Received	3,000
Cash Paid to Creditors	80,000	Closing Balance of Creditors	18,000
B/R Endorsed to Creditors	7,000		

(**Ans.:** Credit Purchase: ₹ 93,000)

3. Calculate closing stock from the following figures:

	₹		₹
Opening Stock	12,000	Sales	60,000
Purchases	70,000	Sales Returns	2,000
Purchases Returns	5,000	Gross Profit Rate on Cost	25%

(**Ans.:** Closing Stock ₹ 30,600)

4. Desai wants to ascertain the profit he earned during 2016 and his balance sheet at the end of the year. He does not keep systematic books of account and can give you only the following information:

Assets and Liabilities	**Dec 31.2015** ₹	**Dec 31.2016** ₹
Sundry Debtors	45,000	48,600
Sundry Creditors	2,400	?
Cash	6,300	?
Furniture and Fixtures	11,000	13,600
Stock at Cost	25,000	30,000

Transactions During 2016:	₹
Cash Received from Debtors	80,000
Discount Allowed to Them	1,400
Bad Debts Written Off	1,800
Cash Paid to Creditors	64,000

Goods Returned by Customers	3,000
Goods Returned to Suppliers	2,000
Expenses Paid	5,200
Drawings	9,000

He still owes ₹ 800 for expenses and the depreciation on furniture and fixtures is 15%. He affirms that he always sells goods at cost plus 40%. A provision of 2.5% on debtors is required against bad debts. Help Desai. ***(CA Inter)***

(**Ans.:** Gross profit ₹ 24,800; Net profit ₹ 13,770; Total of Balance Sheet ₹ 95870)

5. The books of Moneymaker showed the following figures:

	31.12.15 ₹	**31.12.16** ₹
Cash at Bank	3,500	8,500
Cash in Hand	410	850
Stock on Trade	22,500	25,500
Sundry Debtors	18,000	?
Sundry Creditors	8,000	7,300
Bills Payable	20,000	18,000
Furniture and Fittings	5,000	?
Outstanding Salary	200	?

The cash book analysis showed the following figures amongst others:

	₹		₹
Receipts from Customers	1,05,000	Drawings	6,000
Discount allowed to Customers	1,300	Payments to Creditors	19,00
Salary up to 31.12.16	2,600	Discount Received from Creditors	2,600
Rent	3,600	Payment for Bills Payable	80,000
Sundry Trade Expenses	8,500		
Furniture Purchased on 1.7.16	1,000		

Depreciation is provided on furniture and fittings @ 10% p.a. No figures are available for total sales. However, Moneymaker informs you that he maintains a steady gross profit rate of 25% on sales.

Prepare Moneymaker's Trading and Profit and Loss Account for the year ended 31st December, 2016 and the balance sheet as at date.

(CIMA London Modified)

(**Ans.:** Net profit: ₹ 18,217; Total of Balance Sheet ₹ 58,727; Closing Balance of debtors ₹ 18,427; Furniture and fittings after depreciation ₹ 5,450; Credit purchase of ₹ 98,900; Opening capital ₹ 21,210)

6. Calculate total sales from the following information:

	₹
Bills Receivable on 1st January 2015	7,800
Debtors on 1st January 2015	30,800
Cash Received on Maturity of Bills Receivable during the Month	20,900
Cash Received from Debtors	70,000
Bad Debts Written Off	4,800
Returns Inwards	8,700
Bills Receivable Dishonored	1,800
Bills Receivable on 31st January 2015	6,000
Debtors on 31st January 2016	25,500
Cash Sales during the months	15,900

(CS Inter Modified)

(**Ans.:** Credit sales ₹ 97,300 B/R drawn during the year ₹ 20,900; Total sales ₹ 1,13,200)

7. The Balance Sheet of Bose and Dass was as under on 31st December 2015.

Liabilities		₹	**Assets**	₹
Sundry Creditors		11,600	Stock	15,000
Bills Payable		4,300	Debtors	16,100
Capitals:			Furniture	4,000
Bose	20,000		Delivery Van	13,000
Dass	15,000	35,000	Cash at Bank	2,800

The transactions during 2016 were:

	₹		₹
Purchases	30,000	Bills Payable Issued	7,000
Sales	50,000	Discount Received	500
Bills Receivable Received	6,000	Discount Allowed	800

The Stock on 31st Dec, 2016 was ₹ 18,200. Cash transactions were as follows:

	₹
Received from Debtors	45,000
Received against B/R	4,500
Received from Sale of Old Gunny Bags	200
Payment to Creditors	21,500
Payment against B/P	8,000
Expenses (Including Salaries)	10,000

The balance at Bank on 31st Dec 2016 was ₹ 4,500 delivery van is to be depreciated @ 15%. During the year, both partners had withdrawn an equal sum of money. Allowing a commission of 10%

of net profits before such commission to the manager, prepare Trading and Profit and Loss Account and Balance Sheet relating to 2016.

(IPCC Modified)

(**Ans.:** Gross Profit, ₹ 23,200, Net profit ₹ 10,035; Total of Balance Sheet ₹ 53,550; Drawings ₹ 8,500)

8. Balance Sheet of Mr. Roy as on 31st December 2015 is as follows:

Liabilities	**₹**	**Assets**	**₹**
Creditors	41,710	Bank	31,230
Accruals	1,870	Debtors	62,300
Capitals	1,30,720	Stock	41,670
		Fixtures	21,600
		Machinery at Cost	17,500
	1,74,300		**1,74,300**

Following information is disclosed by the books:

Particulars	**For the year ended 31-12-2016**
Cash Received from Debtors	74,320
Cash Paid Expenses	18,480
Creditors	32,690
Drawings	9,200
Sales	83,100
Purchases	42,300
Bad Debts	2,700
Expenses Outstanding	1,730

Stock in Trade was taken on 31st December, 2016 ₹ 12,900. Depreciation is to be provided on Machinery at 20% p.a. on Original Cost.

You are required to prepare Trading and Profit and Loss Account for the year and the Balance Sheet as on 31st December 2016.

(CIMA London Modified)

(**Ans.:** Gross Profit = ₹ 56,930, Net profit = ₹ 34,450, Balance Sheet Total = ₹ 1,00,500)

9. Mr. Mark does not maintain proper books of accounts . From the following, prepare Trading and Profit and Loss Account for the year ended 31st March, 2016 at Balance Sheet.

Particulars	**31-3-2015 ₹**	**31-3-2016 ₹**
Debtors	31,500	43,750
Stock	17,150	23,100
Cash and Bank	8,750	?
Creditors	10,500	7,875
Furniture	3,000	3,500

Plant and Machinery	55,000	55,000
Land and Building	1,40,000	1,40,000

Analysis of the other transactions are:

Particulars	**₹**
Cash Collected from Debtors	1,07,000
Cash Paid to Creditors	77,000
Salaries	21,000
Rent	2,700
Office Expenses	3,150
Drawings	5,000
Fresh Capital Introduced	3,500
Cash Sales	3,000
Cash Purchases	8,800
Discount Received	1,225
Discount Allowed	525
Return Inward	1,750
Return Outward	1,400
Bad Debts	350

(a) Depreciate Plant and Machinery by 2%, Land and Building by 5% and Furniture by 10%.

(b) Office Expenses are prepaid ₹ 150 on 31st March 2016.

(ICWA Inter Modified)

(**Ans.:** Gross Profit – ₹ 44,675, Net profit – ₹ 9,875, Balance Sheet Total – ₹ 2,61,150)

10. The following information is available from the records of Vilasrao.

Particulars	**As on 31-12-2016**	**As on 31-12-2015**
Plant and Machinery	60,000	50,000
Bank Balance	40,000	60,000
Debtors	40,000	30,000
Creditors	30,000	25,000
Loan Taken	5,000	6,000
Closing Stock	15,000	17,000

The following transactions has been taken place in the calendar year 2010.

Additional Capital introduced – ₹ 5,000

Drawings during the year – ₹ 20,000

Plant Purchased during the year on 1st Jan, 2016 was ₹ 10,000. Provide depreciation on plant @ 25% on W.D.V.

Compute Profit/Loss of Mr. Vilasrao for the year ended 31-12-2016.

(CS Inter Modified)

(**Ans.:** Gross Profit – ₹ 16,900, Net profit – ₹ 14,450, Balance Sheet Total – ₹ 1,00,500)

11. Mr. Nagpal submits to you the following relating to his business for the year ended 31st December 2016. you are required to prepare Trading and Profit and Loss accounts for the year ended 31st December, 2016 and a balance sheet as on that date.

Any difference in cash book as to be taken as his personal drawing:

Deposits in to bank	**₹**
Personal dividend paid into business a/c	26,700
Personal payment out of bank	600
Payments to creditors	2,250
Withdrawn for bank	23,850
Withdrawn from debtors	23,250
Received from debtors	3,900
Paid from wages	1,800
Paid for delivery charges	600
Paid for rent	405
Paid for general expenses	750
Interest credited by bank	30

Assets and Liabilities:

	1.1.16 ₹	**31.12.16 ₹**
Stock	1,800	2,250
Balance	2,400	3,000
Cash	90	60
Debtors	2,250	3,150
Creditors	3,600	4,200

(**Ans.:** G.P. – ₹ 8,100; N.P. – ₹ 4,575; Balance Sheet total – ₹ 8,460; Difference in cash book – ₹ 1,605)

12. Mr. Bholenath does not maintain proper books of accounts. From the following information, prepare Trading and P & L A/c for the year ended 31st December, 2016 and balance sheet as on that date:

Assets and Liabilities	**1.1.16 ₹**	**31.12.16 ₹**
Debtors	9,000	12,500
Stock	4,900	6,600
Furniture	750	750
Creditors	3,000	2,250

Analysis of other transactions:

	₹
Cash collected from debtors	30,400
Cash paid to creditors	22,000
Salaries	6,000
Rent	750
Office experience	900

Drawing	1,500
Fresh capital introduced	1,000
Cash sales	750
Cash purchases	2,500
Discount received	350
Discount allowed	150
Returns inward	500
Returns outward	400
Bad debts	100
Cash at the beginning of the year	2,500

(**Ans.:** G.P. ₹ 12,500; N.P. ₹ 4,950; B/s total – ₹ 20,850. It is assumed that furniture is purchased on credit basis)

13. You are required to prepare Trading and P & L A/c for the year ended 31.12.16 and the balance sheet at that date from the following information:

(a) Assets and Liabilities

Assets and Liabilities	**31st December 2015 ₹**	**31st December 2016 ₹**
Bank balance	Not available	20,000
Debtors	15,000	16,000
Creditors	5,000	8,000
Stock	15,000	20,000
Fixed asset	30,000	30,000

(b) Sundry debtors on 31.12.16 include bad debtors ₹ 1,000.

(c) Fixed assets include property rented out for which rent of ₹ 500 was received for the year and utilised for personal use.

(d) Repairs to premises amount to ₹ 600 which remained unpaid on 31.12.16.

(e) All sales receipts were banked after meeting business expenses of ₹ 5,000 and personal experience of ₹ 3,000.

(f) All business payments are made by cheques.

(g) Cash purchases and cash sales amounted to ₹ 1,000 and ₹ 2,000 respectively.

(h) Account with bankers reveals that withdrawals amounted to ₹ 70,000 and deposits ₹ 90,000 for the year.

(**Ans.:** G.P. – ₹ 31,000; N.P. – ₹ 24,900; B/S total – ₹ 85,000)

14. Ranbow Co.carried on a business without maintaining a proper set of books of accounts. An analysis of its cash book revealed the following figures for the year ended 30.6.2016.

Analysis of cash book:

Particulars	Amt ₹	Particulars	Amt ₹
Paid for credit purchase	1,34,000	Other payments:	
Received for credit sales	1,55,000	Salaries	20,000
Received for cash sales	21,050	Rent paid up to May 2016	
Further capital introduced	10,000	for the months	6,000
Purchases of furniture	21,050	Sundry Experience	2,500
(on 1st April 2016)	2,000	Electric charges	3,000
Purchases of investment		Drawings	8,000
(on 1st April, 2016)	10,000	Motor Car Upkeep	2,375

The following further information is given to you:

	As on 30.6.2015 ₹	As on 30.6.2016 ₹
Cash in hand and at bank	2,905	-
Stock-in-trade	22,500	31,255
Sundry Debtors	15,800	17,900
Sundry creditors	10,550	13,755
Furniture (depreciation @ 5%)	10,000	-
Motor car (depreciation @ 15%)	15,000	-

Bad debts during the year amounted to ₹ 400. Discount allowed was ₹ 250 and discount received was ₹ 125. Provision should be created on sundry debtors at @ 5% on 30th June, 2015. Salaries were outstanding to the extent of ₹ 2,550, while advance of salary amounts to ₹ 1,500. The rate of interest on investment is 6%.

Prepare Trading and Profit and Loss Account of Rainbow Co. for the year ended 30th June, 2016 and the balance sheet as on that date.

(**Ans.:** Opening capital – ₹ 55,155; Gross profit – ₹ 50,725; Net profit – ₹ 13,230; B/S total 87,190)

15. Atmacharan keeps his books by single-entry and the position of his business as on 1st January, 2016 is as follows:

Particulars	₹
Capital	70,000
Sundry Creditors	10,000
Bills Payable	7,000
Freehold Premises	50,000
Stock	25,000
Debtors	15,000
Furniture	2,000
Bills Receivable	5,000

His transaction during the year were as follows:

Receipts	Amt. ₹	Payments	Amt. ₹
Sundry Debtors & Bills Receivable	15,000	Bank Overdraft (as on 1.1.2016)	10,000
Cash Sales	80,000	Drawings	23,000
		Expenses	5,000
		Payments to Creditors &	
		Bills Payable	20,000
		Balance:	
		Cash in hand	2,000
		At Bank	35,000
	95,000		**95,000**

You are asked to prepare a trading and P & L A/c for the year ended 31.12.2016 and a balance sheet as on that date. The following additional information is supplied:

Closing stock ₹ 30,000; Closing Debtors 20,000 ₹ Bills Receivable ₹ 5,000. No additional has been made during the year to freehold premises and furniture but they are to be depreciated as under:

Freehold Premises 10% and Furniture 15%.

A bad and doubtful debts provision at 2½% is to be raised against closing debtors.

There were balance of bills payable account ₹ 3,000 and creditors account ₹ 4,000. Expenses were outstanding to ₹ 200.

(IPCC Modified)

(**Ans.:** G.P. – ₹ 95,000; N.P. – ₹ 84,000; B/S total – ₹ 1,38,200)

(Hint: Prepare combined account for B/R And for B/P and creditors).

16. From the following particulars, prepare a trading and profit and loss account for the year ended 30th June 2016 and Balance Sheet as on that date:

(a) Assets and Liabilities:

Particulars	1.7.2015 ₹	30.6.2016 ₹
Furniture	8,000	9,000
Stock	10,000	9,000
Debtors	20,000	?
Creditors	14,000	18,000
Unpaid expenses	2,200	2,000
Cash at book	1,800	1,225

(b) Receipts and Payments during the year:

	₹
Receipts from debtors	1,17,000
Creditors paid	78,400
Freight paid (Inward)	6,000
Furniture purchases	1,800
Expenses paid	29,000
Miscellaneous Receipts	5,000

(c) Goods costing ₹ 2,000 were used as advertising materials.

(d) Goods are sold to show profit $33\ ^1/_3\%$ on sales.

(e) Difference in Bank, if any, is to be treated as drawing or introduction by the proprietor.

(CIMA London Modified)

(**Ans.:** G.P. – ₹ 43,700; N.P. – ₹ 17,100; B/S total – ₹ 53,325; Sales – ₹ 1,31,100; Debtors – ₹ 34,100)

4

Chapter

Hire Purchase

INTRODUCTION

A fire at a business place destroys assets such as building, Machinery, furniture, stock, etc. It destroys records also. Not only does it destroy the assets but also creates dislocation in the usual working of a business concern. Hence, a prudent businessman prefers to take out an insurance policy to cover the risk of loss due to fire. In case of happening of an event, the businessman gets compensation equal to the amount of loss sustained. For this purpose he has to lodge a claim for loss of stock with the Insurance company. It is easy to claim for loss of assets except stock. In case of stock, the insured has to decide the stock on date of fire [SOFD]. It becomes difficult to decide the claim when there is no proper record of inventory is left due to loss of documents due to fire.

Procedure of claim for loss of stock:

- If records are not destroyed by fire:- In such a case calculation of claim will be:-

Calculate the amount of stock lost by fire:

SOFD	xx
(-) Salvage	xx
Stock lost by fire	xx

Calculation for amount of claim:

- If there no average clause then stock lost by fire = Amount of claim
- If there is average clause then

  amount of claim = Policy Amount/SOFD × Stock lost by fire
- If records are also destroyed by fire

  Calculate Percentage of Gross Profit:

Determine the Gross Profit to sales. In absence of any information. It is necessary to take the figure of pervious year for deciding the percentage. In case of information about sale and gross profit is available. It is necessary to take average of these figures.

Prepare a Trading Account in the usual manner. Following are some of the items connected with preparation of Trading Account:

(a) Stock: Stock includes stock on Raw materials, Work in progress, Finished goods, etc. In absence of clear information, stock is considered as stock of finished goods only. Valuation of such stock should be at cost. If any other basis is given, convert it to cost.

(b) Purchases less returns.

(c) Wages.

(d) Manufacturing expenses.

(e) Sales less returns.

(g) Gross profit.

The rate of Gross profit is important for deciding the stock on the date of fire. Therefore, there should be consistency in the gross profit ratio.

1. MEMORANDUM TRADING ACCOUNT

Prepare Memorandum Trading Account up to the date of fire by collecting figures in respect of opening stock, purchases, direct expenses and sales from the record. In case the record is destroyed by fire, the information can be made available from the documentary evidence.

The balancing figure on the credit side of the Memorandum Trading Account is the estimated value of stock on the date of fire. While preparing Memorandum or Pro forma Trading Account, following points should be given proper consideration:

(i) Period: This Account is prepared for the period from last date of accounts to the date of fire which is given in the problem.

(ii) Stock (Opening): The basis of valuation of stock should be changed to cost.

If there is undervaluation of stock:

Cost of stock = (100\100 – Rate of Undervaluation) × Value of stock

If there is overvaluation of stock :

Cost of stock = (100\100 + Rate of Overvaluation) × Value of stock

(iii) Purchases: Purchases should be for the period from last date of accounts to the date of fire. Goods included in the purchases. Goods received but not accounted should be added to purchases. If the amount of purchases is not given, the same can be calculated by preparing Creditors Account.

	₹
Purchases	XX
Less: Goods included in purchases but not actually received	XX
Add: Unrecorded purchases	XX
Less: Purchase Returns	XX
Purchases to be debited to Trading A/c	XX

If purchases are not given. It should be decided by preparing creditors A/c as follows.

Creditors A/c

	₹		₹
To Bank A/c	XX	By Balance b/d	XX
To Discount A/c	XX	By Purchases (Bal.fig.)	XX
To Bills Payable A/c	XX		
To Balance c/d	XX		
	XX		XX

(iv) Sales: Sales should be for the period from last date of accounts to the date of fire. Goods included in the above sales but not delivered should be deducted from sales. Misappropriated cash sales and goods delivered but not recorded should be added to sales.

	₹
Sales	XX
Less: Goods sold but not delivered	XX
Less: Sale of assets	XX
Add: Unrecorded sales	XX
Less: Sales Returns	XX
Sales to be credited to Trading A/c	**XX**

If sales are not given it should be ascertained by preparing Debtors A/c as follows:

Debtors A/c

	₹		₹
To Balance b/d	XX	By Bank A/c	XX
To Sales A/c (Bal.fig.)	XX	By Discount A/c	XX
		By Sales Returns A/c	XX
		By Bills Receivable A/c	XX
	XX		XX

(v) Wages : Wages for the period from the last accounts to the date of fire should be debited to Pro forma Trading Account.

Amount of wages should be calculated as follows:

	₹
Wages paid	XX
Less: Wages incurred for installation of machinery	XX
Less: Outstanding wages of the last year paid during the year	XX
Add: Outstanding wages for the current year	XX
Wages to be debited to Trading A/c	**XX**

(vi) Manufacturing Expenses: Any manufacturing expenses or factory expenses for the period to the date of fire should also be considered.

(vii) Gross Profit and Gross Profit Ratio: Gross profit ratio may be at a certain percentage on cost or on sales. Consistent gross profit ratio over the past years is necessary to find out stock on the date of fire. Gross profit ratio should be adjusted under the following circumstances:

(a) Different gross profit ratios in past years should be averaged out.

(b) Change in material prices.

(c) Change in expenses ratio.

(d) Change in sales price.

(e) Different gross profit ratios for different goods.

The ratio of Gross Profit for the purpose of claim should be normal rate.

(i) If information about the Gross Profit ratio of the just preceding year is given, then the Gross Profit ratio of the previous year should be taken as a normal rate of Gross Profit.

(ii) If the rate of Gross Profit of previous years has been falling from year to year consistently then it is not proper to consider the average rate of gross profit of previous years as normal rate of gross profit. In such a situation, make an estimate of the rate of gross profit that is likely to prevail in the current year and consider that rate as the normal rate of gross profit for, e.g., gross profit rates for three years have been 30%, 25% and 20%. In this case, average will be 25%, Instead of taking average reasonable gross profit rate likely to prevail will be 15%.

The above procedure should be followed. In case there is a continuous rise in the rate of gross profit.

(viii) Abnormal Goods: Goods which are slow moving or which are damaged are called as abnormal goods. Valuation of such goods may be at cost or at a lower value as given. It becomes necessary to adjust purchases, sales and stock on account of abnormal goods.

Abnormal items are treated as follows:

1. If abnormal items are included in closing stock:
   (a) Deduct value of abnormal items from closing stock.
   (b) Deduct cost of abnormal items from purchases.
   (c) Deduct sale of abnormal items from sales.
2. If abnormal items are included in opening stock:
   (a) Deduct value of abnormal items from opening stock.
   (b) Deduct sale of abnormal items from sales.
   (c) Deduct value of abnormal items if any, from closing stock.
3. If abnormal items are written off to some extent from closing stock:
   (a) Deduct the value of remaining items from closing stock.
   (b) Deduct cost of abnormal items from purchases.
   (c) Deduct sale of abnormal items from sales.

(ix) Stock: Balancing figure in Pro forma Trading Account after adjustment of gross profit is the stock of normal goods. Then it should be adjusted for (i) Goods with consignee or third party and (ii) Salvage, i.e., realisable value of scrap or partly damaged goods. The adjusted stock is the amount of loss suffered.

3. Loss of Stock

Deduct the amount of salvage from the value of stock on the date of fire to get the value of loss of stock.

Loss of stock = stock on the date of fire – salvage.

4. Average Clause

The purpose of insurance is to compensate loss and not to allow profit. Hence, a fire insurance policy usually includes an average clause in order to discourage under insurance of stock. As per this clause, the insurance company pays compensation to the insured proportionately if the value of stock or asset on the date of fire is more than the amount of policy. Following formula may be applied in the case of an average clause:

Claim = (Value of policy/Value of stock on the date of fire) ×Value of stock destroyed

3. PROFORMA OR MEMORANDUM

Trading A/c for period __

		₹			₹
To Opening stock		XX	By Sales	XX	
To Purchases	XX		*Less:* Returns	XX	XX
Less: returns	XX	XX	By Stock distributed as free samples		XX
To Wages		XX	By Stock sent on		XX
To Carriage		XX	Consignment		
To Gross Profit		XX	By Stock sent on approval		XX
			By Stock kept with bailee		XX
			By Stock on the date of fire (bal.fig.)		XX
	XX				XX

Illustration 1: Find out sales when cost of goods sold is 80,000 and Gross Profit ratio 20%.

[B.Com., BU, April, 2005]

Solution:

Gross Profit = $80{,}000 \times \frac{1}{4} = 20{,}000$

$\therefore$ Sales = cost of goods sold + Gross Profit

= 80,000 + 20,000 = ₹ 1,00,000

Illustration 2: Ascertain purchases when cost of goods sold is ₹ 2,00,000

Opening stock : 20,000

Closing stock : 50,000 **[B.Com., BU, April, 2005]**

Solution:

Cost of goods sold = Opening Stock + Purchases – Closing Stock

2,00,000 = 20,000 + Purchases – 50,000

2,00,000 – 20,000 + 50,000 = Purcahses

∴ Purchases = ₹ 2,30,000

Illustration 3 (Calculation of claim in case of under Insurance):

Particulars	₹
Loss of stock by fire	4,00,000
Amount of policy	3,42,000
Total value of stock destroyed by fire	4,56,000

Calculate the amount of claim by applying average clause.

(Bangalore University, B.Com. April 1994)

Solution:

$$\text{Amount of Claim} = \text{Policy Amount} \times \frac{\text{Actual Loss of Stock}}{\text{Stock on the date of Fire}}$$

$$= ₹\ 3{,}42{,}000 \times \frac{₹\ 4{,}00{,}000}{₹\ 4{,}56{,}000}$$

= ₹ 3,00,000

Illustration 4 (Calculation of Claim in case of under insurance, using average clause): Find out the actual claim in the following case:

Particulars	₹
Value of stock on the date of fire	25,000
Value of stock saved from fire	5,000
Value of the Insurance Policy	20,000

There is an average clause in the policy. **(Bangalore University, B.Com. November 1993)**

Solution:

1. Calculation of Actual Amount of Loss

	₹
Stock on the date of fire	25,000
Less: Stock saved from fire	5,000
Actual Amount of Loss	20,000

2. Calculation of Amount of Claim

$$\text{Amount of Claim} = \text{Policy Amount} \times \frac{\text{Actual Loss of Stock}}{\text{Stock on the date of Fire}}$$

$$= ₹\,20{,}000 \times \frac{₹\,20{,}000}{₹\,25{,}000}$$

$$\mathbf{= ₹\,16{,}000}$$

Illustration 5 (when rate of Gross Profit and policy amount is not given): On 15th June 2016, the premises and stock of a firm was destroyed by fire but the accounting records were saved from which the following particulars are available:

	₹
Stock on 1.1.2015	73,500
Stock on 31.12.2015	81,900
Purchases for the year 2015	3,98,000
Sales for the year 2015	4,87,000
Purchases from 1.1.2016 to 15.6.2016	1,62,000
Sales from 1.1.2016 to 15.6.2016	2,31,200

The stock salvaged was ₹ 5,300. Show the amount of claim.

(Bangalore University, B.Com. October 1991)

Solution:

Step 1: Preparation of Last Year Trading Account

Dr. Trading Account for the year ending 31st December 2015 Cr.

Particulars	₹	Particulars	₹
To Opening Stock	73,500	By Sales	4,87,000
To Purchases	3,98,000	By Closing Stock	81,900
To Gross Profit (Balancing figure)	97,400		
	5,68,900		**5,68,900**

Step 2: Calculation of Rate of Gross Profit on Sales

$$\text{Rate of G/P} = \frac{\text{Gross Profit}}{\text{Net Sales}} \times 100 = \frac{₹\,97{,}400}{₹\,4{,}87{,}000} \times 100 = 20\%$$

Step 3: Preparation of Memorandum Trading Account

Memorandum Trading Account

Dr. **(From 1.1.2016 to 15.6.2016)** **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock	81,900	By Sales	2,31,200
To Purchases	1,62,000	By Closing Stock (Balancing figure)	58,940
To Gross Profit (20% of ₹ 2,31,200)	46,240		
	2,90,140		**2,90,140**

Step 4: Calculation of Actual Amount of Loss

Particulars	₹
Stock on the date of fire	58,940
Less: Salvaged Stock	5,300
Actual Amount of Loss	**53,640**

Step 5: Calculation of Amount of Claim

The problem does not provide any information about the policy amount. Hence, the amount of claim will be the same as actual amount of loss.

∴ The amount of claim = ₹ 53,640.

Illustration 6 (When information of Debtors are given): A fire broke out in the warehouse of Merchantile Traders Ltd. on 30th Sep., 15. The company desires to file a claim with the insurance company for loss of stock. From the following information prepare a statement showing the amount of claim. The last account of company were prepared on 31.12.14.

Stock on 31.12.14	1,20,000
Sundry debtors on 31.12.14	3,20,000
Sundry debtors on 30.9.15	2,40,000
Cash received from debtors	11,52,000
Purchases from 1.1.15 to 30.9.15	10,00,000

Rate of Gross Profit on sales 25%

Solution:

Dr. Total Debtors Account Cr.

Particulars	₹	Particulars	₹
To Opening bal b/d	3,20,000	By Cash received	11,52,000
To Credit Sales (Bal. fig.)	10,72,000	By Closing bal. c/d	2,40,000
	13,92,000		**13,92,000**

Dr. Memorandom Trading Account for the Year 30.9.15 Cr.

Particulars	₹	Particulars	₹
To Opening stock	1,20,000	By Sales	10,72,000
To Purchases	10,00,000	By Closing stock (bal. fig.)	3,16,000
To Gross Profit (10,72,000 × 25%)	2,68,000		
	13,88,000		**13,88,000**

Statement of Claim

Particulars	₹
Closing stock	3,16,000
Less: Salvage	—
Amount of claim	**3,16,000**

Illustration 7 (When commission on Purchases is given): Balu Traders have taken a fire policy of ₹ 4,80,000 covering its stock in Trade. A fire occurs on 31-3-2015 and stock was destroyed with the exception of the value of ₹ 1,24,080.

Following particulars are available from the books of accounts of the firm:

	₹
Stock on 31-12-2014	1,80,000
Purchases to the date of fire	7,80,000
Sales to the date of fire	5,40,000
Carriage Inwards	24,000
Commission paid on purchases	2%
Rate of Gross Profit on cost	50%

The policy was subject to average clause. You are required to calculate

(i) Total loss of stock.

(ii) Amount of claim to be lodged with the Insurance Company.

(iii) Loss suffered due to under insurance. **[B.Com. BU, April, 2004]**

Solution:

Step 1

Memorandum Trading Account from 1-1-2015 to 31-3-2015

Particulars	₹	Particulars	₹
To Opening Stock	1,80,000	By Sales	5,40,000
To Purchases	7,80,000	By Closing Stock (Bal. fig.)	6,39,600
To Carriage Inwards	24,000		
To Commission (2/100 × 7,80,000)	15,600		
To Gross Profit [5,40,000×1/3]	1,80,000		
	11,79,600		**11,79,600**

Note: 50% or 1/2 on cost = 1/3 on sales.

Step 2

Calculation of Actual Loss

Closing Stock	6,39,600
Less: Salvage	1,24,080
Actual Loss	**5,15,520**

Step 3

Calculation of Amount of Claim

$$\text{Claim} = \frac{\text{Policy Amount}}{\text{Closing Stock}} \times \text{Actual Loss}$$

$$= \frac{4,80,000}{6,39,600} \times 5,15,520$$

$$= ₹\ 3,86,882$$

Step 4

Calculation of loss due to under insurance

Actual Loss	5,15,520
Less: Amount of claim	3,86,882
Loss due to under insurance =	**1,28,638**

Illustration 8 (when rate of Gross Profit and policy amount is not given and distribution of sample is given): On 1st April, 2015, a fire destroyed the stock of a business firm. From the records which were saved, the following information was obtained:

		₹
Stock	- on 1.1.2014	45,000
	- on 1.1.2015	55,000
Purchases	- for calender year 2014	1,29,250
	- for 3 months upto 31.3.2015	60,000
Sales	- for year ended 31.12.2014	1,70,000
	- upto the date of fire	1,00,000
Manufacturing Expenses	- Calender year 2014	21,000
	- 3 months upto 31.3.2015	?

In February 2015, goods valued at a cost price of ₹ 500 were distributed as samples. Manufacturing expenses were normally found to be constant per month. The salvaged stock was estimated at ₹ 7,000. Prepare a statement showing the amount of claim. **(Bangalore University, B.Com. April 1991)**

Solution:

Step 1: Preparation of Last Year Trading Account

Dr. **Trading Account for the year ending 31st December 2014** **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock	45,000	By Sales	1,70,000
To Purchases	1,29,250	By Closing Stock	55,000
To Manufacturing Expenses	21,000		
To Gross Profit (Balancing figure)	29,750		
	2,25,000		**2,25,000**

Step 2: Calculation of Rate of Gross Profit on Sales

$$\text{Rate of G/P} = \frac{\text{Gross Profit}}{\text{Net Sales}} \times 100 = \frac{₹\,29{,}750}{₹\,1{,}70{,}000} \times 100 = 17.5\%$$

Step 3: Preparation of Memorandum Trading Account:

Dr. Memorandum Trading Account for Three months ending 1.4.2015 Cr.

Particulars	₹	Particulars	₹
To Opening Stock	55,000	By Sales	1,00,000
To Purchases (₹ 60,000 less samples ₹ 500)	59,500	By Closing Stock (Balancing figure)	37,250
To Manufacturing Expenses			
($\frac{3}{12}$ × ₹ 21,000)	5,250		
To Gross Profit (17.5% of ₹ 1,00,000)	17,500		
	1,37,250		**1,37,250**

Note: 1. Samples given are deducted from purchases, since so much of purchases are not available for sale. 2. Manufacturing expenses are calculated proportionately.

Step 4: Calculation of Actual Amount of Loss:

Particulars	₹
Stock on the date of fire	37,250
Less: Salvaged Stock	7,000
Actual Loss of Stock	**30,250**

Step 5: Calculation of Amount of Claim:

The problem does not provide any information about the policy amount. Hence, the amount of claim will be the same as actual amount of loss.

∴ The amount of claim = ₹ 30,250.

Illustration 9 (when average rate of Gross Profit is required): The Premises and Stock of Gulab Jam were totally destroyed by fire on 30.1.2016 from the books and other records that were saved the following information is available.

The stock on hand has always been valued at 10% less than cost.

Particulars	**2013**	**2014**	**2015**	**2016**
Opening stock as valued	27,090	32,400	36,000	36,900
Purchases less returns	74,900	80,000	81,000	6,000
Sales less returns	1,20,000	1,32,000	1,40,000	12,000
Wages	17,400	19,000	20,900	2,000
Closing stock as valued	32,400	36,000	36,900	–

Prepare a statement for submission to the Insurance Company in support of the company for loss of stock.

Solution: Step - 1

Dr. **Trading Account for the year ending 31.12.13** **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock $\left(27{,}090 \times \frac{100}{90}\right)$	30,100	By Sales A/c	1,20,000
		By Closing Stock A/c $\left(32{,}400 \times \frac{100}{90}\right)$	36,000
To Purchases A/c	74,900		
To Wages	17,400		
To Gross Profit	33,600		
	1,56,000		**1,56,000**

$$\text{Rate of Gross Profit} = \frac{33{,}600}{1{,}20{,}000} \times 100 = 28\%$$

Dr. **Trading Account for the year ending 31.12.14** **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock	36,000	By Sales	1,32,000
To Purchases	80,000	By Closing Stock $\left(36{,}000 \times \frac{100}{90}\right)$	40,000
To Wages	19,000		
To Gross Profit	37,000		
	1,72,000		**1,72,000**

$$\text{Rate of Gross Profit} = \frac{37{,}000}{1{,}32{,}000} \times 100 = 28\%$$

Dr. **Trading Account for the year ending 31.12.15** **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock	40,000	By Sales	1,40,000
To Purchases A/c	81,000	By Closing Stock $\left(36{,}900 \times \frac{100}{90}\right)$	41,000
To Wages A/c	20,900		
To Gross Profit	39,100		
	1,81,000		**1,81,000**

$$\text{Rate of Gross Profit} = \frac{39{,}100}{1{,}40{,}000} \times 100 = 28\%$$

$$\text{Average rate of Gross Profit} = \frac{28 + 28 + 28}{3} = 28\%$$

Step 2:

Dr. Memorandum Trading Account for 1.1.2016 to 30.1.2016 Cr.

Particulars	₹	Particulars	₹
To Opening Stock	41,000	By Sales A/c	12,000
To Purchases A/c	6,000	By Closing Stock A/c (Bal. fig)	40,360
To Wages	2,000	(Value of stock on the date of fire)	
To Gross Profit (12,000 × 28%)	3,360		
	52,360		**52,360**

Step 3: Statement of claims: Claims = 40,360 (claim amount is equal to value of stock on the date of fire).

Illustration 10 (when average clause is to be applied): A fire occurred in the premises of a firm on 1.7.2015. From the following information, calculate the claim to be made by the firm:

	₹
Stock on 1.1.2014	63,000
Purchases for the year ending 31.12.2014	4,17,500
Sales for the year ending 31.12.2014	5,00,000
Wages for the year ending 31.12.2014	20,000
Salary for the year ending 31.12.2014	10,000
Stock on 31.12.2014	81,000
Purchases from 1.1.2015 to date of fire	2,00,000
Sales from 1.1.2015 to date of fire	3,00,000
Stock salvaged	10,000
Value of Policy	30,000

There is an average clause in the policy. The firm had the practice of valuing stock at 20% above cost price. However, during 2014 the policy was changed and the stock on 31.12.2014 was valued at 10% less than the cost. Expenses incurred for extingwishing the fire was ₹ 2,000.

Solution:

Step 1: Preparation of Last Year Trading Account:

Dr. Trading Account for the year ended 31st December, 2014 Cr.

Particulars	₹	Particulars	₹
To Opening Stock $\left(₹\,63{,}000 \times \frac{100}{120}\right)$	52,500	By Sales	5,00,000
To Purchases	4,17,500	By Closing Stock $\left(₹\,81{,}000 \times \frac{100}{90}\right)$	90,000
To Wages	20,000		
To Gross Profit (Balancing figure)	1,00,000		
	5,90,000		**5,90,000**

Notes: 1. Stocks have been valued at cost price and recorded.

2. Salaries doesn't appear in the Trading Account. Hence, it is not considered.

Step 2: Calculation of Rate of Gross Profit on Sales:

$$\text{Rate of G/P} = \frac{\text{Gross Profit}}{\text{Net Sales}} \times 100 = \frac{₹\,1{,}00{,}000}{₹\,5{,}00{,}000} \times 100 = 20\%$$

Step 3: Preparation of Memorandum Trading Account:

Memorandum Trading Account

Dr. (from 1.1.2015 to 1.7.2015) Cr.

Particulars	₹	Particulars	₹
To Opening Stock	90,000	By Sales	3,00,000
To Purchases	2,00,000	By Closing Stock (Balancing figure)	50,000
To Gross Profit (20% of ₹ 3,00,000)	60,000		
	3,50,000		**3,50,000**

Step 4: Calculation of Actual Amount of Loss:

Particulars	₹
Stock on the date of fire	50,000
Less: Salvaged stock	10,000
	40,000
Add: Expenses on extinguishment of fire	2,000
Actual Loss	**42,000**

Step 5: Calculation of Amount of Claim:

Stock on the date of fire = ₹ 50,000

Policy Amount = ₹ 30,000

So, there is under-insurance and average clause is applicable.

$$\therefore \text{ Amount of Claim} = \text{Policy Amount} \times \frac{\text{Actual Loss of Stock}}{\text{Stock on the date of Fire}}$$

$$\text{Amount of Claim} = ₹\ 30{,}000 \times \frac{₹\ 42{,}000}{₹\ 50{,}000}$$

Amount of Claim = ₹ 25,200

Illustration 11 (When free samples are given): The premises of Mercantile Traders caught fire on 1.7.2015, and their stock was damaged. The stock was *fully insured*. The concern has made accounts upto 31st December of each year. The following information is available:

	₹
Stock on 31.12.2014	1,32,720
Stock on 31.12.2013	96,140
Purchases from 1.1.2015 upto date of fire	3,48,270
Purchases upto 31.12.2014	4,52,580
Sales upto 31.12.2014	5,20,000
Sales from 1.1.2015 upto date of fire	4,91,700

Further Information

1. In May 2015, goods costing ₹ 10,000 were given away for advertising purposes, no entry being made in the books.
2. During 2015, a Clerk had misappropriated unrecorded cash sales of ₹ 4,000.
3. The rate of Gross Profit is constant over the years.
4. Value of stock salvaged was ₹ 13,000 and the expenses incurred to extinguish fire ₹ 800.

From the above information, prepare a statement showing the claim for loss of stock.

(Bangalore University, B.Com. November 1993)

Solution:

Step 1: Preparation of Previous Year Trading Account

Dr. **Trading Account for the year ended 31st December, 2014** **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock	96,140	By Sales	5,20,000
To Purchases	4,52,580	By Closing Stock	1,32,720
To Gross Profit (Balancing figure)	1,04,000		
	6,52,720		**6,52,720**

Step 2: Calculation of Rate of Gross Profit on Sales

$$\text{Rate of Gross Profit} = \frac{\text{Gross Profit}}{\text{Net Sales}} \times 100 = \frac{₹\,1{,}04{,}000}{₹\,5{,}20{,}000} \times 100 = 20\%$$

Step 3: Preparation of Memorandum Trading Account:

Memorandum Trading Account
Dr. **(From 1.1.2015 to 1.11.2015)** **Cr.**

Particulars	₹	₹	Particulars	₹	₹
To Opening Stock		1,32,720	To Sales	4,91,700	
To Purchases	3,48,270		*Add:* Unrecorded sales	4,000	4,95,700
Less: Goods given for advertising, not available for sales	10,000	3,38,270	To Closing Stock (Balancing figure)		74,430
To Gross Profit (20% of ₹ 4,95,700)		99,140			
		5,70,130			**5,70,130**

Step 4: Calculation of Actual Amount of Loss:

Particulars	₹
Stock on the date of fire	74,430
Less: Salvaged stock	13,000
	61,430
Add: Expenses incurred for extinguishing fire	800
Actual Loss of Stock	**62,230**

Step 5: Calculation of Amount of Claim:

The problem clearly states that stock was fully insured. Hence, the amount of claim will be the same as actual amount of loss.

Amount of claim = ₹ 62,230

Note: 1. Goods given away for advertisement purposes is to be deducted from purchases in the Memorandum Trading A/c because it is given at cost price.

2. Unrecorded cash sales must be added to sales in Memorandum Trading A/c.

3. Expenses for extinguishing fine is to be added to calculation of Actual Loss.

Illustration 12 (When ratio of gross profit is given): On 12th June, 2015, fire occurred in the premises of N.R.Patel, a paper merchant. Most of the stocks were destroyed, cost of stock salvaged being ₹ 11,200. In addition, some stock was salvaged in a damaged condition and its value in that condition was agreed at ₹ 10,500. From the books of accounts, the following particulars were available:

1. His stock at the close of account on December 31, 2014 was valued at ₹ 83,500.
2. His purchases from 1.1.2015 to 12.6.2015 amounted to ₹ 1,12,000 and his sales during that period amounted to ₹ 1,54,000.

On the basis of his accounts for the past three years it appears that he earns on an average a gross profit of 30% on sales.

Patel has insured his stock for ₹ 60,000. Compute the amount of claim.

Solution:

Step 1: Preparation of Last Year Trading Account

- Not required in this problem -

Step 2: Calculation of Rate of Gross Profit on Sales

Rate of Gross Profit on Sales (given) = 30%

Step 3: Preparation of Memorandum Trading Account

Memorandum Trading Account

Dr. **(From 1.1.2015 to 12.6.2015)** **Cr.**

Particulars	₹	Particulars	₹
To Opening Stock	83,500	By Sales	1,54,000
To Purchases	1,12,000	By Closing Stock (Balancing figure)	87,700
To Gross Profit (30% of ₹ 1,54,000)	46,200		
	2,41,700		**2,41,700**

Step 4: Calculation of Actual Amount of Loss

Particulars		₹
Stock on the date of fire		87,700
Less: Salvaged Stock:		
In good condition	11,200	
In damaged condition	10,500	21,700
Actual Loss of Stock		**66,000**

Step 5: Calculation of Amount of Claim

Stock on the date of fire ₹ 87,700

Policy Amount ₹ 60,000

There is an under-insurance and average clause is applicable.

$$\text{Amount of Claim} = \text{Policy Amount} \times \frac{\text{Actual Loss of Stock}}{\text{Stock on the date of Fire}}$$

$$\text{Amount of Claim} = ₹\ 60{,}000 \times \frac{₹\ 66{,}000}{₹\ 87{,}700}$$

Amount of Claim = ₹ 45,154

Illustration 13 (Simple problem – Overvaluation of stock): A fire occurred in the godown of Make Money Ltd, on 15th April 2015, the books of accounts and stock amounting to ₹ 10,800 were saved. Company's average rate of Gross Profit is 33% on sales. The stock on hand on 31st Dec. 2014 valued at 10% above cost was ₹ 58,300. Purchases, Wages and Sales were at ₹ 45,000 ₹ 18,000 and ₹ 95,400 respectively.

Prepare a statement of claim.

Solution:

Memorandum Trading A/c for the period 1.1.2015 to 15.4.2015

	₹		₹
To stock	53,000	By Sales	95,400
To Purchases	45,000	By Closing Stock	52,082
To Wages	18,000	(bal.fig.)	
To Gross Profit	31,482		
	1,47,482		**1,47,482**

Statement of Claim	₹
Stock on the date of fire	52,082
Less: Salvage	10,800
Claim	**41,282**

Note: For deciding claim find out the stock at cost

Cost of Stock (58,300\110) × 100 = 53,000

Illustration 14 (When sales and gross profit are given for different years): A fire occurred on April 15, 2015, and destroyed the business premises of X and Co. The books of accounts and Stock amounting to ₹ 1,80,000 were saved and the following information was rendered available from the books:

	Sales ₹	Gross Profit ₹
Year ending Dec.31.2010	86,00,000	21,50,000
Year ending Dec.31.2011	71,00,000	21,30,000
Year ending Dec.31.2012	60,00,000	20,00,000
Year ending Dec.31.2013	55,00,000	18,70,000
Year ending Dec.31.2014	48,00,000	16,00,000

The stock on Dec. 31.2014, was valued at ₹ 9,70,000. The Purchases, sales and production wages from Jan. 1.2015, to April 14.2015 were at ₹ 7,50,000, ₹ 15,90,000 and ₹ 3,00,000 respectively.

You are to prepare a statement in support of your claim against the Insurance Company together with any comments you may feel necessary to make.

Solution:

Proforma Trading A/c for the Period 1 Jan. to April 14, 2015

	₹		₹
To Stock	9,70,000	By Sales	15,90,000
To Purchases	7,50,000	By Stock	9,60,000
To Wages	3,00,000	(bal.fig.)	
To Gross Profit			
(₹ 15,90,000 x 33 1/3%)	5,30,000		
	25,50,000		**25,50,000**

Amount of Claim = (Stock on 14.4.2013 – Stock Salvaged)

= ₹ 9,60,000 – ₹ 1,80,000

= ₹ 7,80,000

Hints and solution

Rate of Gross Profit in different years:

for 2010 = ₹ 21,50,000/86,00,000 × 100 = 25%

for 2011 = ₹ 21,30,000/71,00,000 × 100 = 30%

for 2012 = ₹ 20,00,000/60,00,000 × 100 = 33,1/3%

for 2013 = ₹ 18,70,000/55,00,000 × 100 = 34%

for 2014 = ₹ 16,00,000/48,00,000 × 100 = 33,1/3%

The rate of Gross Profit in 2015 may be considered as 33,1/3% (and not the average of 5 years) on the assumption that this is the conservative basis of rate of Gross Profit. Because it shows that there is a constant increase in the rate of gross profit from 2010 to 2013 and then the same is declined. That is why, the rate of Gross Profit, for 2015, should be considered as the rate of Gross Profit for 2014.

Illustration 15 (When stock is over-valued): A fire occurred in the godown of X Ltd. on 9th March, 2015, destroying the entire Stock. the books records were salvaged from which the following particulars were ascertained:

	₹
Sales for the year, 2014	10,01,000
Sales for the period 1.1.2015 - 8.3.2015	3,00,000
Purchases for the year, 2014	8,00,000
Purchases for the period 1.1.2015 - 8.3.2015	1,25,000
Stock on 1.1.2014	3,31,100
Stock on 31.12.2014	3,85,000

The Company has been following the practice of valuing the stock of goods at actual cost plus 10%. Included in the stock on 1.1.2014 were some shop-soiled goods which originally cost ₹ 2,000, but were valued at ₹ 1,100. These goods were sold during sold during the year 2014 for ₹ 1,000. Subject to these, the rate of Gross Profit on the basis of valuation of stock was uniform.

You are required to ascertain the value of the stock destroyed.

Solution:

Dr. **Trading A/c for the year ended 31.12.2014** **Cr.**

	₹		₹
To Opening Stock	3,00,000	By Sales	10,00,000
To Purchases	8,00,000	(₹ 10,01,000-1000)	
To Gross Profit	2,50,000	By Closing stock	3,50,000
	13,50,000		**13,50,000**

Workings: ₹

1. Opening Stock	3,31,1000
Less: Shop Soiled Goods	1,100
	3,30,000
Less: Profit @ 1/11 (10/110)	30,000
therefore, at cost	3,00,000
2. Closing Stock	3,85,000
Less: Profit 1/11	35,000
Therefore, at cost	3,50,000

Rate of Gross Profit on Sales = 2,50,000/10,00,000 × 100

Trading A/c for the year ended 31.12.2014.

Dr. **Cr.**

	₹		₹
To Stock	3,50,000	By Sales	3,00,000
To Purchases	1,25,000	By Stock	2,50,000
		(bal.fig.)	
To Gross Profit	75,000		
(25% on sales)			
	5,50,000		**5,50,000**

Value of the stock destroyed ₹ 2,50,000.

Illustration 16: A fire occurred on the premises of a business man on 30th June, 2015, destroying a part of his stock. No stock records have been maintained. The following information was ascertained from his books which were not involved in the fire:

	₹
Valued of stock on 1st January, 2015	12,500
Purchases from 1st January, 2015 to 30th June, 2015	45,500
Sales for the above period	56,500
Purchases in 2012	2,20,000
Purchases in 2013	1,75,000
Purchases in 2014	1,50,000
Sales in 2012	2,50,000
Sales in 2013	1,60,000
Sales in 2014	1,90,000
Gross Profit in 2012	75,000
Gross Profit in 2013	32,000
Gross Profit in 2014	19,000
Value of stock saved from fire	2,500

Prepare a statement showing the amount to be claimed from the Insurance Company, mentioning any further factors which you consider should be taken into consideration while preparing the claim.

Solution:

Calculate G/P

	2012	2013	2014
Sales	2,50,000	1,60,000	1,90,000
Gross Profit	75,000	32,000	19,000
G/P %	30%	20%	10%

Note: The above G/P percentages show a declining trend of 10% each year and accordingly current year's G/P percentage works out to 0%. It is assumed that minimum margin of profit of the current year was 5%.

Memorandum Trading Account (From 1.1.15 to 30.6.15)

	₹		₹
To Opening Stock	12,500	By Sales	56,500
To Purchases	45,500	By Closing Stock (Bal fig.)	4,325
To Gross Profit (5% of 56,500)	2,825		
	60,825		**60,825**

Statement of Claim

Estimated Value of Closing Stock	4,325
On the date of fire	
(–) Salvaged	2,500
∴ Loss of Stock	1,825

Illustration 17: The Trading Account of M/s. Good & Bad Co. for the year ending 31st March, 2014 is given below:

	₹		₹
To Opening Stock	68,480	By Sales Less Return	1,95,000
To Purchases Less Return	1,56,940	By Closing Stock	58,820
To Gross Profit c/d.	29,400		
	2,54,820		**2,54,820**

A fire occurred in their godwon, which was situated behind their offices premises, on 31st December 2015. A considerable part of the stock of ready-made garments was destroyed by fire. The salvaged stock realized ₹ 2,255. The stocks and the premises were fully insured against fire risks.

Considering the following further particulars, prepare a statement showing the amount of claim to be lodged by M/s Good & Bad Co. with the All India Insurance Co. Ltd. for the loss of stocks only.

Sales for the period ending 31st December, 2015 were ₹ 1,09,200. The amount paid for purchases was ₹ 88,016 including a cheque for ₹ 562 which was not presented to the bankers upto 31.12.2015. As shown by the books of account, Trade Creditors on 31.3.2015 amounted to ₹ 24,608 and on 31st December, 2015 were ₹ 22,112. Good worth ₹ 6,390 were returned to creditor during the period ending 31.12.2015.

Solution:

To find out the purchases upto the date of size, creditors a/c. is prepared.

Creditors A/c

	₹		₹
To Cash/Bank	88,016	By Opening Balance b/d	24,608
To P/Return	6,390	By Purchase (bal. fig.)	91,910
To Closing Balance c/f	22,112		
	1,16,518		**1,16,518**

Memorandum Trading A/c (From 1.4.15-31.12.15)

		₹		₹
To Opening Stock		58,820	By Sales	1,09,200
To Purchase	91,910		By Closing Stock (Bal.fig.)	51,520
(–) P/Return	6,390	85,520		
To Gross Profit (15% of 1,09,200)		16,380		
		1,60,720		**1,60,720**

Statement of Claim

Estimated Value of Closing Stock on the date of fire	51,520
(–) Salvaged	2,255
∴ Loss of Stock	49,265

Illustration 18: A trader, who had covered his stock by taking an insurance policy of ₹ 30,000 his stock partly destroyed by fire on March 18, 2015. Ledgers were saved and accounts disclosed.

	₹
Stock on 31st December, 2013	31,300
Purchases during 2014	78,050
Carriage paid and due during 2014	3,770
Wages paid during 2014	39,810
Sales during 2014	1,85,310
Stock on 31st December, 2014	30,110
Purchases from January 1, 2013 to March 18, 2015	15,500
Wages paid from January 1, 2015 to March 18, 2015	7,600
Wages owing on March 18, 2015	60
Sales from January 1, 2015 to March 18, 2015	24,200

Addition information:

(i) Included in the stock on 31st December, 2013 was the stock of stationery ₹ 500.

(ii) Included in the stock at 31st December, 2014 was the stock of stationery ₹ 620.

(iii) Wages owing during 2014, ₹ 2,500.

(iv) During 2014, purchase invoices amounting to ₹ 1,200 had been omitted from the books.

(v) During 2014 private purchases amounting to ₹ 1,200 had been included in purchase day book.

(vi) During 2014, stock of ₹ 400 (cost price) was sold to Mr. X at 33-1/3% profit on sale on 30th December, 2014 and was recorded as sales. However, the goods being not delivered were by mistake included in the stock at cost price. The goods were delivered on 8th January, 2015.

(vii) During 2014 a plant which stood at ₹ 5,000 in the books on 1st January was sold for ₹ 1,900 in part exchange for a new machinery costing ₹ 4,200. A net invoice of ₹ 2,300 was passed through purchases day book.

(viii) Purchases in 2015, included a wrong purchase of ₹ 500 half of which was sold in the same year at a loss of ₹ 50 and the remaining was treated at cost price for insurance claim.

(ix) Stock saved ₹ 12,000.

(x) There was an average clause in the policy.

Calculate loss of stock and claim on average basis.

Solution:

Trading A/c of 2014

		₹			₹
To Opening	31,300		By Sales		1,85,310
(–) Stationery	500	30,800	By Closing Stock	30,110	
To Purchase	78,050		(–) Stationery	620	
(+) Not recorded	1,200		(–) Customer's Stock	400	29,090
(–) Drawings	1,200				
(–) Plant Purchases	2,300	75,750			
To Carriage		3,770			
To Wages	39,810				
(+) Outstanding	2,500	42,310			
To Gross Profit (33-1/3%)		61,770			
		2,14,400			**2,14,400**

Memorandum Trading A/c (From 1.1.15 to 18.3.15)

		₹			₹
To Opening		29,090	By Sales	24,200	
To Purchases	15,500		(–) Ab. Sales	200	24,000
(–) Additional	500	15,000	By Closing Stock (Bal.fig.)		33,250
To Wages	7,600				
(+) Outstanding	60				

(–) O/S of L/y paid	2,500	5,160		
To Gross Profit (33-1/3% of 24,000)		8,000		
		57,250		**57,250**

Statement of Claim		**For Problem**	
Estimated Value of Stock		If Loss	100
1. Normal Goods (As per T.A/c)	33,250	(+) Profit	100
2. Abnormal Goods (As per T.A/c)	250	∴ at Price	200
Total Stock	33,500	**At Price**	**Cost Price**
(–) Salvaged	12,000	200	100
∴ Loss of Stock	21,500	3,00,000	(?)
		= 1,50,000 (at cost)	

Applying Average Clause

$$\text{Amount of Claim} = \frac{\text{Amount of Policy}}{\text{Actual Stock}} \times \text{Loss of Stock}$$

$$= \frac{30{,}000}{35{,}500} \times 21{,}500 \quad = \mathbf{19{,}225}$$

Illustration 19: A fire occurred in the shop of Nirbhaya on 13th Feb., 2015 and destroyed a part of the stock and furniture goods, costing ₹ 13,000 and furniture of the value of ₹ 400 were salvaged from the fire. Stock of goods and furniture were insured against fire as:

	₹
Stock	5,100
Furniture	2,000

Following information was obtained from the books and records saved:

(i) Balances as per the Balance sheet as on 31st Dec., 2014

	₹
Stock (at cost)	13,000
Furniture	2,500

Creditors for goods	1,200
Debtors for goods	2,000

(ii) Transactions from 1.1.15 to 13.2.15

	₹
Payment made to the creditors for goods	11,000
Receipts from debtors for goods	12,000
Purchase returns	300
Sales return	700
Balance of Creditors for goods on 31.02.15	2,000
Balance of Debtors goods on 13.2.15	3,500

All the sales were made so as to realize a profit of 20% on selling price. There were no other purchases or sales. Prepare a statement of claim to be lodged in respect of stock of goods and furniture.

Solution:

Memorandum Trading Account (From 1.1.15 to 13.2.15)

		₹			₹
To Opening Stock		13,000	By Sales	14,200	
To Purchase	12,100		(–) Sales Return	700	13,500
(–) Purchase return	300	11,800	By Closing Stock (Bal.fig.)		14,000
To Gross Profit (20%)		2,700			
		27,500			**27,500**

Total Debtors A/c.

	₹		₹
To Balance b/d	2,000	By Cash/Bank	12,000
To Sales	14,200	By Sales Returns	700
		By Balance c/f	3,500
	16,200		**16,200**

Total Creditors A/c

	₹		₹
To Cash/Bank	11,000	By Balance b/d	1,200
To Purchase Return	300	By Purchase	12,100
To Balance c/f	2,000		
	13,300		**13,300**

Statement of Claim

(1) For Stock

	₹
Estimated Value of Closing Stock	14,000
(–) Salvaged	1,300
∴ Loss of Stock	12,700

Applying Average Clause

$$\frac{5,100}{14,000} \times 12,700 \quad = \mathbf{4,626}$$

(2) For Furniture

	₹
Book Value	2,500
(–) Salvaged	400
∴ Loss	2,100

Applying Average Clause

$$\frac{2,000}{2,500} \times 2,100 \quad = \mathbf{1,680}$$

∴ Total Claim for Stock & Furniture **₹ 6,306**

Illustration 20: On Friday 13th May, 2015, a fire at the premises of P. (Wholeseller) Ltd. destroyed a substantial part of the stock. It also destroyed some of the office records. The company has a loss of stock insurance policy under which the amount insured is ₹ 84,000. The amount of the claim for stock lost in the fire will have to be calculated from what information is available. For the financial year ended 31 December, 2014 the following figures were included in the profit calculation:

	₹
Sales	4,06,000
Purchases	2,96,000
Stock 1.1.2014	70,000
Stock 31.12.2014	80,000

Note:

(a) The stock at 1st January included ₹ 6,000 representing goods which had been reduced in value at the stock taking and were all sold during 2014 for the same reduced amount.

(b) The stock at 31st December, 2014 included ₹ 10,000 representing goods which were reduced to half-cost at the stock taking. Of these, ₹ 6,000 were sold at the reduced amount in January, 2015. ₹ 2,000 were scrapped in February, 2015, without any revenue at and he balance had not been disposed off at the time of the fire.

The cost price of stock at 13th May, 2015 unaffected by the fire was ₹ 32,000 but the rest of the stock was completely destroyed and this included in the balance of the marked down stock referred to in (b) above.

The mix products sold up to 13th May, 2015 was substantially the same as for 2014. No writing-down of the stock values takes place except at annual stock taking and with the exception of the items mentioned, there have been no alternatives to normal selling prices.

Purchases from 1st January to 13th May, 2015 total ₹ 1,45,500. Sales for the same period total ₹ 1,90,000 and there were returns from customers of ₹ 4,000.

You are required to calculate the amount you expect the Company could claim for the loss of stock.

Solution:

Trading A/c (2014)

		₹			₹
To Opening Stock	70,000		By Sales	4,06,000	
(–) Abnormal	6,000	64,000	(–) Abnormal	6,000	4,00,000
To Purchases	2,96,000		By Closing Stock	80,000	
(–) Abnormal	20,000	2,76,000	(–) Abnormal	10,000	70,000
To Gross Profit (32.5%)		1,30,000			
		4,70,000			**4,70,000**

Memorandum Trading A/c (From 1.1.15 to 13.5.15)

	₹			₹
To Opening Stock	70,000	By Sales	1,90,000	
To Purchases	1,45,500	(–) Returns	4,000	
To Gross Profit (32.5%) (1,83,000)	59,475	(–) Sale of	3,000	1,83,000
		Abnormal Stock (50% of 6,000)		
		By Goods Scrapped (50% of 2,000)		1,000
		By Closing Stock		90,975
	2,74,975			**2,74,975**

Abnormal	
Cost	20,000
(–) Sold in '84	6,000
(–) Scrapped	2,000
∴ Left	12,000

Apply Average Clause

$$\text{Amount of Claim} = \frac{\text{Amount of Policy}}{\text{Actual Stock}} \times \text{Loss of Stock}$$

$$\frac{84,000}{1,03,975} \times 71,975 \quad = \ 58,148$$

Statement of Claim

Estimated Value of Stock		
1. Normal Goods (Trading A/c.)	91,975	
2. Abnormal Goods (at cost) (W.Note)	12,000	1,03,975
Less: Salvaged		32,000
∴ Loss of Stock		**71,975**

Illustration 21: A fire occurred in the business premises of M/s. Poonawala on 15th Oct., 2015. From the following particulars ascertain the loss of stock and prepare a claim for insurance.

	₹
Stock as on 1.1.14	30,600
Purchases from 1.1.14 to 31.12.14	1,22,000
Sales from 1.1.14 to 31.12.14	1,80,000
Stock as on 31.12.14	27,000
Purchases from 1.1.15 to 14.10.15	1,47,000
Sales from 1.1.15 to 14.10.15	1,50,000

The stocks were always valued at 90 per cent of cost. The stock saved from fire was worth ₹ 18,000. The amount of the policy was ₹ 63,000. There was an average clause in the policy.

Solution:

M/s. Poonawala Trading A/c (2014)

		₹			₹
To Opening	30,600		By Sales		1,80,000
(–) Under Value (10/90)	3,400	34,000	By Closing Stock	27,000	
To Purchases		1,22,000	(+) Undervalue (10/90)	3,000	30,000
To Gross Profit		54,000			
		2,10,000			**2,10,000**

$$\text{Gross Profit Margin} = \frac{GP}{Sales} \times 100 = \frac{54,000}{1,80,000} \times 100 = 30\% \text{ of Sales}$$

Memorandum Trading A/c (From 1.1.15 to 5.10.15)

	₹		₹
To Opening Stock	30,000	By Sales	1,50,000
To Purchases	1,47,000	By Estimated Stock	72,000
To Gross Profit (30%)	45,000		
	2,22,000		**2,22,000**

Statement of Claim

Estimated Stock on date of fire	72,000
Less: Salvage	18,000
Loss	54,000

Average Clause

Estimated Stock	72,000
Policy Amount	63,000

Since Stock > Policy

∴ Average Clause is applicable

$$\text{Claim} = \frac{\text{Amount of Policy}}{\text{Actual Stock}} \times \text{Loss of Stock}$$

$$= \frac{54,000}{72,000} \times 63,000 \quad = \mathbf{47,250}$$

Illustration 22: On 1st April, 2015 an accidental fire completely destroyed the stock of Chhote Nawab. However, from the various records available from his chartered accountant, the following information was obtained, from which you are requested to prepare a statement showing the amount of claim to be lodged with the Sharmila Insurance Company Limited.

Stock at Cost	1st January, 2014	45,000
	1st January, 2015	55,000
Purchases:	Calendar Year 2014	1,25,000
	Three months to 31.3.2015	60,000
Sales:	Year ended 31st Dec., 2014	1,70,000
	Period upto the date of fire	1,00,000
Manufacturing	Calendar Year 2014	21,000
Expenses:	Three months to 31st March, 2015	?

In February, 2015 goods valued at sale price of ₹ 5,000 were distributed as samples. Manufacturing expenses were normally found to be constant. The value of the salvaged stock was estimated at ₹ 7,000.

Solution:

Choote Nawab Trading A/c. (2014)

	₹		₹
To Opening Stock	45,000	By Sales	1,70,000
To Purchases	1,25,000	By Closing Stock	55,000
To Manu. Expenses	21,000		
To Gross Profit	34,000		
	2,25,000		**2,25,000**

$$\text{G.P. Marging} = \frac{\text{G.P.}}{\text{Sales}} \times 100 = \frac{34,000}{1,70,000} \times 100 = 20\% \text{ on Sales}$$

Memorandum Trading A/c. (1.1.15 to 31.3.15)

	₹			₹
To Opening Stock	55,000	By Sales	1,00,000	
To Purchases	60,000	(+) Samples	5,000	1,05,000
To Manu. Expenses (21,000 ×3/12)	5,250	By Estimated Stock		36,250
To Gross Profit (20%)	21,000			
	1,41,250			**1,41,250**

Statement of Claim

Estimated Stock on date of fire	36,250
Less: Salvage	7,000
Loss	29,250

Claim = 29,250

Illustration 23: A fire occurred in the godwon of M/s. Pratap & Co. on 31st Dec., 2015. Godown was situated behind their office premises. A considerable part of the stock of ready-made garments was destroyed by fire. The salvaged stock realized ₹ 1,520, the stock and premises were fully insured against fire risks. Considering the following particulars, prepare a statement showing the amount of claim to be lodged by M/s. Pratap & Co. with New India Insurance Co. for the loss of stock only.

	₹
Purchases	
Less: returns for the year ending 31.3.2015	1,56,940
Sales less returns for the year ending 31.3.2015	1,96,000

Stock on 1.4.2014	68,480
Stock on 31.3.2015	58,820
Sales for the period ending 31.12.2015	1,09,200
Trade Creditors on 31.3.2015	24,608
Trade Creditors on 31.12.2015	22,112
Amount paid to Creditors during period ending 31.12.2015	88,016
Goods returned to Creditors for the period ending 31.12.2015	6,390

Note: Working shall be treated as part of your answer.

Solution:

M/s. Pratap & Co. Trading A/cf (31.3.15)

	₹		₹
To Opening Stock	68,480	By Sales	1,96,000
To Purchases	1,56,940	By Closing Stock	58,820
To Gross Profit	29,400		
	2,54,820		**2,54,820**

$$\text{G.P. Margin} = \frac{\text{G.P.}}{\text{Sales}} \times 100 = \frac{29,400}{1,96,000} \times 100 = 15\% \text{ on Sales}$$

Memorandum Trading A/c. (1.4.15 to 31.12.15)

		₹		₹
To Opening Stock		58,820	By Sales	1,09,200
To Purchases	91,910		By Estimated Stock	51,520
(–) Returns	6,390	85,520		
To Gross Profit (15%)		16,380		
		1,60,720		**1,60,720**

Creditors A/c

	₹		₹
To Cash/Bank	88,016	By Balance b/d	24,608
To Purchase Return	6,390	By Purchase A/c	91,910
To Balance c/d	22,112		
	1,16,518		**1,16,518**

Statement of Claim

Estimated Stock on date of Fire	51,520
Less: Salvage	1,520
Loss	50,000

Claim = 50,000

Illustration 24: Nixon Prepares accounts on 31st March each year but on 30th June 2015 fire destroyed the greater part of his stock. Following information was collected from his books.

	₹
Stock on 31st March, 2015	29,250
Purchases from 1st April, 2015 to 30th June, 2015	60,000
Wages from 1st April, 2015 to 30th June	22,750
Sales from 1st April, 2015 to 30th June, 2015	1,00,000

Average percentage of gross profit to cost is 33-1/3% stock to the value of ₹ 7,000 was salvaged. Policy was for ₹ 25,000 Claim was subject to average clause.

Following additional information is available:

(a) Stock in the beginning was calculated at 10% less than cost.

(b) Purchases include purchase of plant of ₹ 5,000.

(c) Plan was installed in May and firm's own men has spent time amounts to ₹ 250 which was included in wages.

You are required to calculate the claim for the loss of stock.

Solution:

Nixon

Memorandum Trading A/c (1.4.15 to30.6.15)

		₹		₹
To Opening Stock	29,250		By Sales	1,00,000
(+) Under Value (10/90)	3,250	32,500	By Estimated Stock	35,000
To Purchases	60,000			
(–) Plant	5,000	55,000		
To Wages	22,750			
(–) Installation	250	22,500		
To Gross Profit (1/4)		25,400		
		1,35,000		**1,35,000**

Statement of Claim

Estimated Stock on date of fire	35,000
Less: Salvage	7,000
Loss	28,000

Average Clause

Estimated Stock	35,000
Policy Amount	25,000

Since Stock Policy Amount $\therefore$ Average Clause is applicable

$$\text{Claim} = \frac{\text{Loss}}{\text{Stock}} \times \text{Policy Amount} \quad = \frac{28{,}000}{35{,}000} \times 25{,}000 \quad = \mathbf{20{,}000}$$

Illustration 25: The premises of M/s. Nariman & Co. were gutted by fier on 31st August, 2015 and some stock was found badly damaged.

The accounts of the firm are closed on 31st March each year. On 31st March, 2015 stock was valued at cost ₹ 26,544 against ₹ 19,228 as at 31st March, 2014. Purchases and Sales were as follows:

	Full year ended 31st March, 2015 ₹	**Period upto 31st August., 2015** ₹
Purchases	90,516	69,654
Sales	1,04,000	98,340

In addition to the above, you collect the following information:

(1) Sometime in May, 2015 goods costing ₹ 10,000 were distributed as part of advertisement campaign in support whereof no entry appears to have been passed in the books.

(2) During the memorandum period cash sales of ₹ 1,190 were misappropriated and these were not recorded in the books.

Ascertain the estimated value of stock at the date of fire, assuming that the rate of gross profit has been constant.

Solution:

M/s. Nariman & Co. Trading A/c. (31.3.15)

	₹		₹
To Opening Stock	19,228	By Sales	1,04,000
To Purchases	90,516	By Closing Stock	26,544
To Gross Profit	20,800		
	1,30,544		**1,30,544**

$$\text{G.P. Margin} = \frac{\text{G.P.}}{\text{Sales}} \times 100 \quad = \frac{20,800}{1,04,000} \times 100 \quad = 20\% \text{ on Sales}$$

Memorandum Trading A/c. (1.4.15 to 31.8.15)

	₹			₹
To Opening Stock	26,544	By Sales	98,340	
To Purchases	69,654	(+) Unrec. Sales	1,190	99,530
To Gross Profit (20%)	19,906	By Good dist. On Samples		10,000
		By Estimated Stock		6,574
	1,16,104			**1,16,104**

Claim = **6,574**

Illustration 26: A fire occurred on 15th August, 2015 in the premises of X Co. Ltd. From the following figures, calculate the amount of claim to be lodged with the insurance company for loss of stock.

	₹
Stock at cost as on 1st April, 2014	20,000
Stock at cost as on 1st April, 2015	30,000
Purchases – 2012-15	40,000
Purchases from 1st April, 2015 to 15th August, 2015	88,000
Sales – 2012-15	60,000
Sales from 1st April, 2015 to 15th August, 2015	1,05,000

During the current year cost of purchases have risen by 10% above last year's levels. Selling price have gone up by 5%.

Salvage value of stocks after fire was ₹ 2,000.

Solution:

'X' Co. Ltd. Trading A/c (31.3.15)

	₹		₹
To Opening Stock	20,000	By Sales	60,000
To Purchases	40,000	By Closing Stock	30,000
To Gross Profit	30,000		
	90,000		**90,000**

$$\text{G.P. Margin} = \frac{\text{G.P.}}{\text{Sales}} \times 100 \quad = \frac{30,000}{60,000} \times 100 \quad = 50\% \text{ on Sales}$$

Memorandum Trading A/c (1.4.15 to 15.8.15)

		₹			₹
To Opening Stock		30,000	By Sales	1,05,000	
To Purchases	88,000		(-) Decre. In price	5,000	1,00,000
(-) Increase in price 10/110	8,000	80,000	By Estimated Stock		60,000
To Gross Profit (50%)		50,000			
		1,60,000			**1,60,000**

Statement of Claim

Estimated Stock on date of fire	60,000
(As per last year's prices)	
Add: Increase in purchase price 10%	6,000
Stock at current year price level	66,000
Less: Salvage	2,000
Loss	64,000

Claim = **64,000**

Illustration 27: The warehouse of National Traders caught fire on 13th June, 2015. The salvaged Stock was ₹ 1,00,000. From following information, prepare a statement showing the amount of the claim to be made upon the Insurance company.

1. Opening Stock at Catalogue price on 1.1.2015 ₹ 3,00,000.
2. Purchases at cost from 1.1.2015 to the date of fire ₹ 10,00,000.
3. Wages from 1.1.1996 to the date of fire ₹ 4,00,000.

4. Goods sold to wholesaler at 20% below catalogue price from 1.1.2015 to the date of fire ₹ 3.50,000.
5. Goods sold to retailers at 10% below catalogue price from 1.1.2015 to the date of fire ₹ 2,70,000.
6. Goods sent to consignee at 25% above cost (Out of the consigned goods 60% goods were unsold on the date of fire) ₹ 2,25,000.
7. Goods sent on sale or return basis at 40% above cost (Out of the sale or return 50% goods were accepted by customers upto the date of fire) ₹ 1,40,000.
8. Goods sold to customers at catalogue price, which is 50% above cost ₹ 4,50,000.
9. The stock was fully insured.

Solution:

National Traders

Cost Structure	Wholesalers	Retailers	Sent to Con.	Sale or Return	Customer
Cost	100	100	100	100	100
(+) Loading	50	50			50
Catalogue Price	150	150	100	100	150
(-) 20%	30 (-) 10%	15 (+) 25%	125 (+) 40%	40	
Selling Price	120	135	125	140	150
Profit	20	35	25	40	50
Margin	20/120	35/135	25/125	40/140	50/150

Memorandum Trading A/c (1.1.15 to 13.6.15)

	₹		₹
To Opening Stock (at cost)	2,00,000	By Sales	
To Purchases	10,00,000	Wholesalers	3,50,000
To Wages	4,00,000	Retailers	2,70,000
To Gross Profit		Sent to Consign	2,25,000
1. Wholesalers 20/120	58,333	On Sale of Return	1,40,000
2. Retailers 35/135	70,000	Customers	4,50,000
3. Sent to consign 25/125	45,000	By Estimated Stock	5,28,333
4. Sale or Return 40/140	40,000		
5. Customers 50/150	1,50,000		
	19,63,333		**19,63,333**

Opening Stock at Cost		**Statement of Claim**	
Cost	At price	Estimated Stock on date of fire	5,28,333
100	150	*Less:* Salvage	1,00,000
(?)	3,00,000	Loss	4,28,333
= 2,00,000		Claim	

Illustration 28: Depression Ltd. suffered loss of stock due to fire on May 31, 2015. From the following information prepare a Statement showing the claim to be lodged:

	₹
Stock on 1st January, 2014	38,400
Purchases during 2014	1,60,000
Sales During 2014	2,02,600
Closing stock on 31st December, 2014	31,800
Purchases from 1st January, 2015 to 31st May 2015	54,000
Sales from 1st January, 2015 to 31st May, 2015	61,400

An item of Stock purchased in 2013 at a cost of ₹ 10,000 was valued at ₹ 6,000 on 31st December, 2013. Half of this stock was sold in 2014 for ₹ 2,600. Remaining Stock was valued at ₹ 2,400 on 31.12.2014. One-fourth of the original stock was sold in March, 2015 for ₹ 1.400. The remaining stock was considered to be worth 60% of the original cost. Salvage was ₹ 12,000. The amount of the policy was ₹ 30,000. There was an average clause in the policy.

Solution:

Depression Ltd. Trading A/c (2014)

		₹			₹
To Opening Stock	38,400		By Sales	2,02,600	
(-) Abnormal Goods	6,000	32,4000	(-) Abnormal Goods	2,600	2,00,000
To Purchases		1,60,000	By Closing Stock	31,800	
To Gross Profit		37,000	(-) Abnormal Goods	2,400	29,400
		2,29,400			**2,29,400**

$$\text{G.P. Margin} = \frac{\text{G.P.}}{\text{Sales}} \times 100 = \frac{37,000}{2,00,000} \times 100 = 18.5\% \text{ on Sales}$$

Memorandum Trading A/c (1.1.15 to 31.5.15)

	₹			₹
To Opening Stock	29,400	By Sales	61,400	
To Purchases	54,000	(-) Abnormal Goods	1,400	60,000
To Gross Profit (18.5%)	11,100	By Estimated Stock		34,500
	94,500			**94,500**

Statement of Claim

Estimated stock on date of fire	
Add (a) Normal goods	34,500
(b) Abnormal goods	1,500
Total Stock	36,000
Less: Salvage	12,000
Loss	24,000

Abnormal Stock

1	(1.1.14) (cost ₹ 10,000)	10,000
(-)1/2	sold in '14	5,000
1/2	Left on 1.1.15	5,000
(-)1/4	sold in '15	2,500
1/4	Left/destroyed/put the claim	2,500
	Valued at	60%
	AMT:	1,500

Application Average Clause

$$\text{Claim} = \frac{\text{Loss}}{\text{Stock}} \times \text{Policy Amount} \quad = \frac{24,000}{36,000} \times 30,000 = \mathbf{20,000}$$

Valuation of Abnormal Stock

60% of 1/4 × 10,000 = **1,500**

Illustration 29: A fire occurred on April, 15, 2015, and destroyed the business premises of X & Co. The books of accounts and stock amounting to ₹ 1,80,000 were saved and the following information were rendered available from the books.

	Sales ₹	Gross Profits ₹
Year ending Dec. 31, 2010	86,00,000	21,50,000
Year ending Dec. 31, 2011	71,00,000	21,30,000
Year ending Dec. 31, 2012	60,00,000	20,00,000
Year ending Dec. 31, 2013	55,00,000	18,70,000
Year ending Dec. 31, 2014	48,00,000	16,00,000

The stock on Dec. 31, 2014 was valued of ₹ 9,70,000. The Purchases, sales and production wages from Jan. 1, 2013 to April 14, 2015 were ascertained of ₹ 7,50,000, ₹ 15,90,000 and ₹ 3,00,000 respectively.

You are to prepare a statement in support of your claim against the Insurance Company together with any comments you may feel necessary to make.

Solution:

'X' & Co. Memorandum Trading A/c (1.1.15 to 15.4.15)

	₹		₹
To Opening Stock	9,70,000	By Sales	15,90,000
To Purchases	7,50,000	By Estimated Stock	9,60,000
To Production Wages	3,00,000		
To Gross Profit (1/3)	5,30,000		
	25,50,000		**25,50,000**

G.P. Margin 2010 $\frac{21,50,000}{86,00,000}\times 100$ 25%

2011 $\frac{21,30,000}{71,00,000}\times 100$ 30%

2012 $\frac{20,00,000}{60,00,000}\times 100$ 33.33%

2013 $\frac{18,70,000}{55,00,000}\times 100$ 34%

2014 $\frac{16,00,000}{48,00,000}\times 100$ 33.33%

G.P. Margin for 2015 is assumed to be the average of last three years.

G.P. i.e. 1/3 = 33.33%

Statement of Claim

Estimated Stock on date of Claim	9,60,000
Less: Salvage	1,80,000
Loss	7,80,000
Claim =	**7,80,000**

Illustration 30: Fire occurred in the premises of Shri Ramesh on 1st April, 2015. All the stock with the exception of ₹ 1,12,000 were destroyed by fire. Shri Ramesh had taken a policy for ₹ 6,84,000 you are required to ascertain the claim. The following particular are available.

	₹
Purchase for the year 2014	37,52,000
Sales for the year 2014	46,40,000
Purchases from 1.1.15 to 1.4.15	7,28,000
Sales from 1.1.15 to 1.4.15	9,60,000
Stock on 1.1.2014	5,76,000
Stock on 31.12.2014	9,68,000
Wages paid during 2014	4,00,000
Wages paid during 1.1.15 to 1.4.15	72,000

Shri Ramesh had in June, 2014 consigned goods worth ₹ 2,00,000 which were lost in an accident. The goods were not insured and the loss was borne by him.

Stock at end of each year for and till the end of calendar year 2013 had been valued of cost less10% from 2014, however, there a change in the valuation and closing stock was ascertained by during 10% to cost.

Solution:

Shri Ramesh Trading A/c. (2014)

		₹			₹
To Opening Stock	5,76,000		By Sales		46,40,000
(+) Under Value (10/90)	64,000	6,40,000	By Goods sent on Consignment		2,00,000
To Purchases		37,52,000	By Closing Stock	9,68,000	
To Wages		4,00,000	(-) Over Value (10/110)	88,000	8,80,000
To Gross Profit		9,28,000			
		57,20,000			**57,20,000**

$$\text{G.P. Margin} = \frac{\text{G.P.}}{\text{Sales}} \times 100 \quad = \frac{9,28,000}{46,40,000} \times 100 \quad = 20\%$$

Memorandum Trading A/c (1.1.15 to 1.4.15)

	₹		₹
To Opening Stock	8,80,000	By Sales	9,60,000
To Purchases	7,28,000	By Estimated Stock	9,12,000
To Wages	72,000		
To Gross Profit (20%)	1,92,000		
	18,72,000		**18,72,000**

Statement of Claim

Estimated Stock on date of fire	9,12,000	
Less: Salvage	1,12,000	
Loss	8,00,000	Claim $= \dfrac{\text{Loss}}{\text{Stock}} \times \text{Policy Amount}$

$$= \frac{8,00,000}{9,12,000} \times 6,84,000 \quad = \mathbf{6,00,000}$$

Illustration 31: On 1st May, 2015 the building of X Ltd., was destroyed by fire but the following particulars were available from the records saved.

1.	Stock at cost on 1st January, 2014	1,10,250
2.	Stock as valued on 31st December, 2014	1,19,400
3.	Purchase for the year ended 31st December, 2014	5,97,000
4.	Sales for the year ended 31st December, 2014	7,30,500
5.	Purchases from 1st January, 2015 to 1st May, 2015	2,43,000
6.	Sales from 1st January, 2015 to 1st May, 2015	3,46,800

In valuing stock for the Balance Sheet at 31st December, 2014 a portion of goods purchased for ₹ 10,350 has been valued below cost by ₹ 3,450 as it was a poor selling line. A portion of these goods was sold in March, 2015 at a loss of ₹ 2,375 on its original cost ₹ 5,175. The remaining stock of these goods was estimated of ₹ 2,800. Subject to this gross profit had remained at a uniform rate. The value of stock salvaged was ₹ 700.

Solution:

Trading A/c. for the year ended 31st Dec., 2014

Particulars		Amount	Particulars		Amount
To Opening Stock		1,10,250	By Sales		7,30,500
To purchases	5,97,000		By Closing Stock	1,19,400	
(-) Abnormal Goods Cost	10,350	5,86,650	(-) Abnormal Goods (value)	6,900	1,12,500
To Gross Profit		1,46,100			
		8,43,000			**8,43,000**

$$\text{G.P. Ratio} = \frac{\text{G.P.}}{\text{Sales}} \times 100 \quad = \frac{1,46,100}{7,30,500} \times 100 \quad = 20\%$$

Memorandum Trading A/c. (From 1.1.15 to 1.5.15)

Particulars	Amount	Particulars		Amount
To Opening Stock	1,12,500	By Sales	3,46,800	
To Purchases	2,43,000	(-) Ab. Goods Sold	2,800	3,44,000
To G.P. (20%)	68,800	By Closing Stock (Bal. fig.)		80,300
	4,24,300			**4,24,300**

Statement of Claim

Value of Goods on date of fire (Normal)	80,300
(Abnormal)	2,800
Total	83,100
(-) Salvage	700
Loss of Stock/Amount of Claim	**82,400**

Illustration 32: Mr. Ashok sells goods at a profit of 20% on sales. On 9.9.2015, a fire destroyed the entire stock. Sales and purchases to the date of fire were ₹ 58,100 and ₹ 48,000 respectively, unsold stock as on 31.12.2014 being ₹ 16,000.

During 2015, Purchase price had declined by 25% ; 15% of the amount of benefit being passed on to the customers by revising downwards the sale price.

Accordingly, with effect from 1.1.2015, all sales during 2015 were effected at the revised prices only. Including sales in respect of stock of goods as on 31.12.2014, such sales being ₹ 9,700. Ascertain the Loss of Stock.

Solution:

Memorandum Trading A/c (From 1.1.15 to 9.9.15)

		₹			₹
To Opening Stock		16,000	By Sales	58,100	
To Purchase	48,000		(+) Reduction in Price (3/97)	1,797	59,897
(+) Reduction in Price (1/13)	16,000	64,000	By Closing Stock (bal.fig.)		32,082
To Gross Profit (20% of 59,897)		11,979			
		91,979			**91,979**

W. Note:

1. G.P. Margin

	Old	New	
SP	100	97	(100 – 3) (15% of 20 = 3)
(-) G.P.	20	37	
∴ Cost	80	60	(80 – 25% of 80) (80 – 20)

2. Break up of closing stock into old stock & New stock

   (i) 32,082 closing stock at old prices

   8,000 Old — 24,082 new

   (ii) Old Stock sold at 9,700/-

   ∴ Sales at Original Price = 10,000/- (100/97 × 9,700)

   ∴ Cost of that goods = 8,000

   (iii) Total Opening Stock = 16,000

   (-) Sold = 8,000

   ∴ Left = 8,000

Statement of Claim

Closing Stock on the date of firm	₹
(a) Old stock (at cost)	8,000
(b) New Stock (24,082 – 25% less)	18,062
Total Stock (at cost)	26,062
(-) Salvaged	Nil
∴ Loss of Stock	26,062

Illustration 33: The premises of KIM Enterprises Ltd. were engulfed by fire on 31st August, 2015. In this fire major portion of stock was destroyed. The company has an insurance policy for ₹ 60,000 with average clause. From the following details, ascertain amount of claim.

(i) During year ended 31.3.2015, Sales were ₹ 5,00,000 and Purchases were ₹ 4,24,000.

(ii) For period 1.4.2015 to 31.8.2015, same were ₹ 4,00,000 and ₹ 3,00,000.

(iii) Stock on 1.4.2014 was ₹ 90,000 and 1.4.2014 it was valued ₹ 1,32,000.

(iv) The stock was valued @ 90% of cost upto 31.3.2015 it was valued @ 110% of cost.

(v) The accounts for 2014-15 had an error Purchase of Equipment costing ₹ 4,000 was included in Purchases.

(vi) The sales since April, 2015 does not include goods costing ₹ 40,000 despatched to customers at normal profit margins. Till date of fire 50% of these are approved.

Solution:

KIM Enterprise Ltd. (Trading A/c of 2014/15)

		₹			₹
To Opening Stock	90,000		By Sales		5,00,000
(+) Undervalue (1/9)	10,000	1,00,000	By Closing Stock	1,32,000	
To Purchase	4,24,000		(-) Over Value	12,000	1,20,000
(-) Equity Purch.	4,000	4,20,000			
To Gross Profit (20%)		1,00,000			
		6,20,000			**6,20,000**

Memorandum Trading A/c (From 1.4.15 to 31.8.15)

	₹		₹
To Opening Stock	1,20,000	By Sales	4,00,000
To Purchases	3,00,000	By Goods Sent on	
		approval (at cost)	40,000
To Gross Profit (20%)	80,000	By Closing Stock (bal.fig.)	60,000
	5,00,000		**5,00,000**

Statement of Claim	₹
Estimated Value Closing Stock	60,000
On the date of fire (-) Salvaged	Nil
Loss of Stock	60,000

Applying Avg. Clause

$$\text{Amount of Claim} = \frac{\text{Amount of Policy}}{\text{Actual Stock}} \times \text{Lock of Stock} \qquad = \frac{60,000}{60,000} \times 60,000$$

= 60,000

Illustration 34: M/s. Bharat Glass Works Limited suffered loss of stock due to fire on 31st March, 2015.

From the following particulars, calculate the amount of claim to be lodged by the company with the Insurance company:

1. Stock on 1.1.2014 ₹ 20,000 including abnormal Goods Costing ₹ 10,000 valued at ₹ 3,000.
2. Purchases during the year 2014 amounted to ₹ 1,00,000 including purchases of abnormal item of ₹ 15,000/-.
3. Wages paid during the year 2014 ₹ 20,000, including installation charges of machinery ₹ 5,000/-.
4. Wages outstanding for the year 2014 ₹ 2,500.
5. Factory expenses for the year 2014 ₹ 3,000.
6. Sales during the year 2014 was ₹ 1,10,000, including sale of 1/5th of the total cost of abnormal items at 50% loss.
7. Stock as on 31st December, 2014 was ₹ 45,000, including abnormal items valued at cost.
8. Purchases upto the date of fire ₹ 50,000, including the purchases of furniture ₹ 5,000.
9. Actual wages paid upto date of fire ₹ 7,000.
10. Sales upto the date of fire ₹ 60,200 including sale of 50% of the remaining abnormal items at a profit of ₹ 500.
11. There was salvage ₹ 17,000.

It is the practice of the firm to insure the Goods at 20% less cost. Abnormal Goods are valued at 60% less cost. The policy is taken at the commencement of every year.

Apply average clause to ascertain the insurance claim.

Solution:

(A) Amount Rcvd. From Customers For Sales:

	Total amount deposited into bank		1,06,300
Less:	I. Interest on 10,000, 6% Deb. For 6 months	300	
	II. Sale proceeds of deb.	10,000	10,300
		96,000	
Add:	Amount used by the -		
	Proprietor before depositing it into the bank		
		99,000	

(B)	**Sales:**		
	Debtors at the end		11,000
	Add: Cash recd. From Drs.		99,000
		1,10,000	
	Less: Debtors at the beginning		20,500
		89,500	
Add:	Goods given to Darpan		500
	Sales up to the date of fire		90,000
(C)	**Cash Paid to CRS.:**		
	Total Amount withdrawn from Bank		1,30,000
	Less: Paid for plant	35,000	
	Paid for installation	1,000	
	Paid for business expenses	4,000	40,000
	Amount paid to Creditors		90,000
(D)	**Purchases:**		
	Creditors at the end		30,000
	Add: Amount paid to Creditor		90,000
		1,20,000	
	Less: Creditors at the beginning		35,000
	Purchases up to the date of fire		85,000

(E) Calculation of Stock at the End:

Proforma Trading Account for the Period Ending 15th August, 2013.

Particulars	₹	Particulars	₹
To Opening Stock	40,000	By Sales	90,000
To Purchases	85,000	By Goods withdrawn by proprietor	5,000
To Gross Profit (90,000 × 33.33%)	30,000	By Stock (bal. fig.)	60,000
	1,55,000		**1,55,000**

(F) Claim on an Average Basis:

$$\frac{\text{Policy Amount}}{\text{Stock on the Date of Fire}} \times \text{Actual Loss}$$

$$= \frac{50,000}{60,000} \times 45,000 \ (60,000 - \text{Salvage ₹ } 15,000) = \mathbf{37,500}$$

M/s. Bharat Glass Work Trading (2014)

Particulars		₹	Particulars		₹
To Op. Stock	20,000		By Sales	1,10,000	
(-) Ab. goods	3,000	17,000	(-) Ab. goods	2,500	1,07,500
To Purchase	1,00,000		By Closing Stock	45,000	
(-) Ab. goods	15,000	85,000	(-) Ab. goods	20,000	25,000
To Wages	20,000		(25 – 2)		
(-) Invest charges	5,000				
	15,000				
(+) O/S	2,500	17,500			
To Factory Expenses		3,000			
To Gross Profit		10,000			
		1,32,500			**1,32,500**

$$\text{G.P. Margin} = \frac{\text{G.P.}}{\text{Sales}} \times 100$$

$$= \frac{10,000}{1,07,500} \times 100 \quad = 9.30\%$$

Memorandum Trading A/c (1.1.15 to 31.3.15)

Particulars		₹	Particulars		₹
To Op. Stock		25,000	By Sales	60,200	
To Purchase	50,000		(-) Ab. goods	10,500	49,700
(-) Furniture	5,000	45,000	By Closing Stock		29,422
To Wages	7,000				
(-) O/S L.Y.	2,500	4,500			
To Gross Profit		4,622			
		79,122			**79,122**

Statement of Claim

Est. stock on date of fire	29,422
Add: Ab. Goods (40% of 10,000)	4,000
Total Stock	33,422
Less: Salvage	17,000
Loss	16,422

Average Clause	
Policy Amount	
Total Opening Stock (1.1.15)	45,000
(-) 20%	9,000
	36,000

Since Stock < Policy Amount

Average Clause is not Applicable

Amount of Claim = Amount of Loss = 16,422/-

Abnormal Stock (At cost)

Opening 10,000
(+) New 15,000
25,000

1/5	4/5
(Sold in 1995)	(Left incl. stock)
5,000	20,000
@ 50% cost	AT cost
= 2,500	Less from ct. st. on
Less from 2012 sales	31.12.14

In 2013 (Ab. Stock)

20,000

50%	50%
= 10,000	= 10,000
Sold	Left in godown
@ 10,500	volume
(Less from Sales)	60% Less
	∴ 40% of 10,000
	= **4,000**

Illustration 35: The premised of EMARBEE LIMITED were engulfed by fire on 16th November, 2015 whereby substantial stock was severely destroyed. The records available with the company yields the following information:

(a) For year ended 31st March, 2015:

	₹		₹
To Opening Stock	1,50,000	By Sales	30,00,000
To Purchases	12,30,000	By Stocks	1,80,000
To Freight & Direct Expenses	3,00,000	To Wages	6,00,000
To Gross Profit	9,00,000		
	31,80,000		**31,80,000**

(b) For half year ended 30th September, 2015

Sales ₹ 18,00,000

Purchases ₹ 8,40,000

(c) For period from 1st October to date of fire sales and purchases were at same, monthly rate as for period 1st April, 2015 to 30th September, 2015.

(d) The freight, Wages and direct Expenses during period 1st April, 2015 to date of fire were at the same rate per months as in last year.

(e) Salvage value is 10% of Cost of Stocks.

(f) The sum insured is ₹ 2,00,000 and policy contains Average Clause.

Solution:

Working Note No. 1.

EMARBEE Limited

G.P. Margin for year ended 31.3.15

$$\frac{\text{G.P.}}{\text{Sales}} \times 100 = \frac{9,00,000}{30,00,000} \times 100$$

= 30% on Sales

Working Note No. 2

Calculation of purchases from 1.10.97 to 16.11.15

Months	**Purchases**
1.4.97 to 30.9.15 (6 months)	8,40,000
1.10.97 to 16.11.15 (1.5 months)	?
$\frac{8,40,000}{6} \times 1.5$	= 2,10,000

Working Note No. 3

Calculation of sales from 1.10.15 to 16.11.15

Months	**Sales**
1.4.97 to 30.9.15 (6 months)	18,00,000
1.10.97 to 16.11.15 (1.5 months)	?
$\frac{18,00,000}{6} \times 1.5$	= 4,50,00

Working Note No. 4

Calculation of freight & Direct expenses & wages

Months	**Expenses**		
Freight 1.4.14 to 31.3.15 (12 months)	3,00,000		
(7.5 months)	?	=	1,87,500
Wages 1.4.97 to 31.3.15 (12 months)	6,00,000		
(7.5 months)	?	=	3,75,000

Memorandum Trading A/c (1.4.15 to 16.11.15)

		Amount			**Amount**
To Opening Stock		1,80,000	By Sales	18,00,000	
To Purchase	8,40,000		(+) from 1.10.97 to 16.11.97	4,50,000	22,50,000
(+) from 1.10.97 to 16.11.97	2,10,000	10,50,000	By Estimated Stock		2,17,500
To freight & direct exp.		1,87,500			
To Wages		3,75,000			
To Gross Profit (30% of 22,50,000)		6,75,000			
		24,67,500			**24,67,500**

Statement of Claim

Estimated of Stock on date of fire	2,17,500
Less: Salvage (10%)	21,750
Loss of Stock	1,95,750

Average Clause

Stock	2,17,500

Poling Amount/Average Clause is Applicable

$$\text{Claim} = \frac{\text{Amount of Policy}}{\text{Actual Stock}} \times \text{Loss of Stock}$$

$$= \frac{2,00,000}{2,17,500} \times 1,95,750 = \mathbf{1,80,000}$$

EXERCISE

Self Assessment Questions

Objective Questions

1. Fire insurance
   - (a) Covers risk of loss
   - (b) Prevents loss
   - (c) Increases loss
2. In fire insurance compensation is
   - (a) Equal to policy amount
   - (b) Stock on the date of fire
   - (c) Actual loss incurred
3. Salvage refers to
   - (a) Stock destroyed by fire
   - (b) Stock saved from fire
   - (c) Stock moving fast
4. Purchase of furniture should be
   - (a) Added to purchases
   - (b) Deducted from purchases
   - (c) Ignored
5. % of gross profit should be
   - (a) Fluctuating
   - (b) Consistent
   - (c) Increasing
6. Stock for the purpose of claim should be
   - (a) At marginal price
   - (b) At market value
   - (c) At cost
7. Purchase of furniture included in purchases should be
   - (a) Added to purchases
   - (b) Deducted from purchases
   - (c) Ignored

8. Unrecorded sales should be
   (a) Added to purchases
   (b) Added to sales
   (c) Ignored
9. Credit purchases should be ascertained from
   (a) Total Creditors Account
   (b) Total Debtors Account
   (c) Cash Account
10. Debtors Account is prepared to find out
   (a) Credit sales
   (b) Cash purchases
   (c) Cash sales
11. Abnormal items included in closing stock should be
   (a) Deducted from closing stock
   (b) Deducted from purchases
   (c) Added to sales
12. Salvage is
   (a) Added to stock on the data of fire
   (b) Deducted from stock on the date of fire
   (c) Ignored for deciding claim
13. As per average clause insurance company pays compensation
   (a) Proportionately
   (b) More than the loss
   (c) Less than the loss
14. Goods sent on consignment are
   (a) Debited to Memorandum Trading Account
   (b) Credited to Memorandum Trading Account
   (c) Ignored
15. Goods sent on approval is
   (a) Debited to Memorandum Trading Account
   (b) Credited to Memorandum Trading Account
   (c) Deducted from sales
16. Carriage on purchases should be
   (a) Debited to Memorandum Trading Account
   (b) Credited to Memorandum Trading Account
   (c) Deducted from sales

17. Unrecorded purchases should be
    (a) Added to sales (b) Added to purchases
    (c) Ignored

18. Misappropriated cash sales should be
    (a) Added to Sales Account (b) Added to Purchases
    (c) Added

19. The main objective of the average clause is to
    (a) Encourage full insurance (b) Encourage under insurance
    (b) Discourage full insurance (d) None of these

20. In case of average clause the loss is suffered by both the insurer and the insured
    (a) In the ratio of risk covered, (b) In equal ratio
    (b) Only by insurer (d) None of these

21. A plant worth ₹ 40,000 has been insured for ₹ 30,000, the loss on account of fire is ₹ 25,000. The insurance company will bear loss of extent of
    (a) ₹ 30,000 (b) ₹ 25,000
    (c) ₹ 18,750 (d) ₹ 28,000

22. In case the net profit is ₹ 10,000 insured standing charges ₹ 5,000 and the sales ₹ 1,00,000 the rate of gross profit will be
    (a) 10% (b) 15%
    (c) 5% (d) 20%

23. A property worth ₹ 20,000 is insured for ₹ 15,000. It is completely destroyed by the fire. The policy contains an average clause. The loss to be born by the insurance company will be
    (a) ₹ 15,000 (b) ₹ 10,000
    (c) ₹ 20,000 (d) ₹ 25,000

24. Find gross profit when GP ratio is 25% on sales and cost of goods sold is ₹ 1,00,000
    (a) ₹ 25,000 (b) ₹ 33,333
    (c) ₹ 20,000 (d) None of these

25. If the rate of gross profit for department A is 25% of cost, the amount is gross profit on a turn over of ₹ 1,00,000 will be
    (a) ₹ 25,000 (b) ₹ 20,000
    (c) ₹ 33,333 (d) ₹ 49,000

26. A building worth ₹ 10,00,000 is insured for ₹ 6,00,000. It is completely destroyed by fire. The loss to be admitted will be

(a) ₹ 10 Lakhs (b) ₹ 6 Lakhs

(c) ₹ 5 Lakhs (d) None of these

27. The loss of profit policy covers loss of profit due to

(a) Loss of Sales

(b) Non-recovery of standing charges

(c) Loss of sales as well as loss of insured standing charges

(d) None of these

28. The object of inserting average clause in loss of stock policy is to

(a) Encourage under insurance (b) Discourage under insurance

(b) Discourage full insurance (d) None of these

29. Loss of profit insurance is otherwise known as

(a) Consequential loss policy (b) Average policy

(b) Both (d) None of these

30. Any savings in expenses is to be deducted for determining the

(a) First claim (b) Final claim

(c) Both (a) and (b) (d) None of these

31. The value of closing stock on the date of fire stock can be ascertained by preparing a

(a) Trading A/c (b) Memorandum trading a/c

(c) Memorandum P & L A/c (d) None of these

32. _________ claim is lodged with the insurance company for the loss of stock and other assets by fire

(a) Life insurance (b) Fire insurance

(c) Medical insurance (d) None of the above

33. To lodge claim for the loss of stock by fire, the value of _______ on the date of fire has to be estimated.

(a) Opening stock in trade (b) Closing stock in trade

(c) Sales (d) Claim

34. ________ can be calculated or a reasonably increasing rate of gross profit as compared to the previous year can be applied to the current year.

(a) Value of stock (b) Average

(c) Weighted average (d) None of these

35. A fire insurance policy usually includes an _________ to discourage the under insurance of stock or any asset

(a) Average clause (b) Weighted clause

(c) Closing stock (d) None of these

36. If the rate of gross profit is 25% on cost it will be equal to

(a) 20% on sales (b) 20% on cost

(c) 1/3 on sales (d) 1/5 on cost

37. Fire insurance provides cover for

(a) Tangible assets (b) Intangible assets

(c) Fictitious assets (d) None of these

38. Opening stock ₹ 13,500 Purchases ₹ 82,500 Sales ₹ 1,20,000 Stock salvaged ₹ 1,260 Rate of Gross Profit ₹ 50% on cost. Find the claim amount.

(a) ₹ 14,740 (b) ₹ 24,740

(c) ₹ 36,000 (d) None of these

39. The average clause in a loss of profit protects the

(a) Insurer (b) Insured

(c) Workers (d) None of these

40. Fire insurance policy is taken up to indemnify

(a) Capital losses to tangible property

(b) Revenue losses to tangible property

(b) Capital losses to intangible property

(d) None of these

41. Claim to be lodged with insurance company is the excess of

(a) Closing stock + salvaged good

(b) Closing stock on the date of fire-salvaged goods

(c) Policy amount – Salvaged goods

(d) None of these

42. Goods recovered in good condition at the time of fire accident is called
    (a) Salvaged goods (b) Saved goods
    (c) Damaged goods (d) None of these

[***Ans.:*** (1 – a), (2 – c), (3 – b), (4 – b), (5 – b), (6 – c), (7 – b), (8 – b), (9 – a), (10 – a), (11 – a), (12 – b), (13 – a), (14 – b), (15 – b), (16 – a), (17 – b), (18 – a), (19 – a), (20 – a), (21 – c), (22 – b), (23 – a), (24 – b), (25 – b), (26 – b), (27 – c), (28 – b), (29 – a), (30 – b), (31 – b), (32 – b), (33 – b), (34 – c), (35 – a), (36 – a), (37 – a), (38 – a), (39 – a), (40 – a), (41 – b), (42 – a).]

State with Reasons Whether the Following Statements Are True or False

1. Insurance avoids loss due to fire.
2. It is not compulsory to insure the stock.
3. Rate of gross profit need not be consistent for deciding the stock on the date of fire.
4. Valuation of stock is done at market value only.
5. Purchase of machinery should be debited to Trading Account.
6. Goods distributed as free sample should be credited to Trading Account.
7. Sale of asset should be debited to Trading Account.
8. Insured gets compensation equal to the amount of policy.
9. Average clause has no effect on calculation of claim.
10. Memorandum Trading Account is prepared to find out credit sales.
11. Salvage value is added to stock on the date of fire to get claim.
12. Carriage on purchase of machinery should be added to purchases to get the stock on the date of fire.
13. Abnormal goods are fast moving goods.
14. Goods sent on consignment should be credited to Trading Account for deciding stock on the date of fire.
15. In case of overvaluation of stock, it should be brought down to cost.
16. Purchases are ascertained from Debtors Account.
17. Sales are ascertained from Creditors Account.
18. Cash sales are ascertained from Cash Journal.
19. The loss of profit policy covers loss of profit policy covers loss of profits due to loss of sales as well as loss of standing charges due to their non-recovery.
20. The insertion of the Average Clause in an insurance policy results in bearing a part of the loss by the insured himself.
21. It is not necessary to make any adjustment in the standard sales of the preceding period in the light of any change in future prospects.

22. The term 'gross profit' in case of a loss of profit policy is different from the term 'gross profit' as used in case of a loss of stock policy.
23. Any saving in expenses is to be deducted for determining the final claim.

[*Ans.:* **True:** 6, 14, 15, 18, 19, 20, 22, 23;

False: 1, 2, 3, 4, 5, 7, 8, 9, 10, 11, 12, 13, 16, 17, 21.]

Match the Following Columns

Group 'A'		Group 'B'	
(a)	Credit Sales	(i)	Slow moving goods
(b)	Credit purchases	(ii)	Ascertained from Creditors A/c
(c)	Abnormal goods	(iii)	Ascertained from Debtors A/c
(d)	Loss of stock	(iv)	Stock on the date of fire salvage
(e)	Average change	(v)	Discourage under insurance
(f)	Mark up	(vi)	Based on cost
		(vii)	Based on selling price

[*Ans.:* (a) – (ii), (b) – (ii), (c) – (i), (d) – (iv), (e) – (v), (f) – (vi)]

Theory Questions

1. State the different parties for an Insurance Policy.
2. Who is an Insurer?
3. Who is an Insured?
4. Show the format of Memorandum Trading account.
5. How do you calculate Gross Profit Ratio?
6. State the format for ascertaining Actual Amount of Loss of Stock.
7. What is Average Clause? When is it applicable?
8. How can claim for loss of stock be calculated when average clause is applicable?
9. What is salvage?
10. List the steps in calculating the claim for loss of stock.
11. What are 'abnormal goods' in the context of fire insurance claim?
12. Amount of Insurance Policy is ₹ 50,000. Stock in hand on the date of fire is ₹ 70,000. Of this, the stock destroyed is estimated to be ₹ 35,000. Calculate the claim admitted by the Insurance Company in case of Average Clause. **(Bangalore University, B.Com. April 1995)**

(**Ans:** ₹ 25,000)

Practical Questions

1. A fire occurred on April 15, 2015, and destroyed the business premises of X & Co. The books of accounts and Stock amounting to ₹ 1,80,000 were saved and the following information was rendered available from the books:

Particulars	**Sales (₹)**	**Gross Profit (₹)**
Year ending December 31, 2010	86,00,000	21,50,000
Year ending December 31, 2011	71,00.000	21,30,000
Year ending December 31, 2012	60,00,000	20,00,000
Year ending December 31, 2013	55,00,000	18,70,000
Year ending December 31, 2014	48,00,000	16,00,000

The stock on December 31, 2014, was valued at ₹ 9,70,000. The Purchases, sales and production wages from January 1, 2015 to April 14, 2015 were ascertained at ₹ 7,50,000, ₹ 15,90,000 and ₹ 3,00,000 respectively.

You are to prepare a statement in support of your claim against the Insurance Company together with any comments you may feel necessary to make.

[Ans.: G.P. Ratio $3\frac{1}{3}$ %, SOFD = 9,60,000, Loss Claim = 7,80,000]

2. M Traders have taken out a fire policy of ₹ 80,000 covering its stock in trade. A fare occurs on 31st March, 2015 and stock was destroyed with the exception of ₹ 20,680 worth. Following particulars are available from the books of accounts of the firm:

Particulars	**₹**
Stock on 1st January, 2015	30,000
Purchase to the date of fire	1,30,000
Sale to the date of fire	90,000
Commission paid to the purchase manager on purchase	2%
Carriage paid on purchases	800
Average gross profit on cost	50%

The policy was subject to average clause.

You are required to calculate the:

(i) Total loss of stock, and (ii) Amount of claim made against the Insurance Co.

3. The Godown of Seo was destroyed by fire on 15.4.15. From the following figures, ascertain the value of goods destroyed by fire.

Particulars		**₹**
Stock as on 1.1.2014		720
Purchases less Returns:	From 1.1.10 to 31.12.14	2,800
	From 1.1.15 to 15.4.15	2,920
Sales Less Returns:	From 1.1.14 to 31.12.14	4,000
	From 1.1.15 to 15.4.15	3,200
Stock as on 31.12.14		480
Cost price of goods salvaged		240
Cost price of goods taken by the proprietor for personal use and not recorded in the books	(From 1.1.15 to 15.4.15)	320

The stocks are valued at cost less 20%.

[Ans.: G.P. Ratio = 19.5%, SOFD = 504, Claim = 264/-]

4. The premises of Orange Plastic Co. caught fire on 20th November, 2015 and the stock was damaged. The firm made up accounts on 31st March each year. On 31st March, 2015 the stock was valued at ₹ 36,000, being 10% less than the cost as against stock was valued at cost as on 31st March, 2014 amounted to ₹ 10,000.

Purchases during the period 1st April, 2015 to the date of fire amounted to ₹ 1,26,200 as against purchases of ₹ 2,40,000 for full year ended 31st March, 2015 and corresponding sales figures were ₹ 1,80,000 and ₹ 3,00,000 respectively.

Following further information is available:

In October, 2015 goods of the sale value of ₹ 6,000 were given as samples and no entry was made in books. Also during the period, goods costing ₹ 500 were being misappropriated every month by the Store-keeper from 1st May, 2015 until he was caught on 31st August, 2015 and the value of misappropriated goods was recovered from him and he was dismissed.

The rate of gross profit was constant. From the above information make an estimate of stock on hand on the date of fire.

Value of goods salvaged amount to ₹ 10,000. Calculate the amount of claim.

5. On 21st June, 2015 the premises of X Ltd., were destroyed by fire but sufficient records were saved from which the following particulars were ascertained:

Particulars	₹
Stock at cost on 1.1.2014	73,500
Stock on 31.12.2014	79,600
Purchases during the year 2014	3,98,000
Sales during the year 2014	4,87,000
Purchases from 1.1.2015 to 21.6.2015	1,62,000
Sales from 1.1.2015 to 21.6.2015	2,31,200

In valuing the stock for the Balance Sheet at 31-12-2014 ₹ 2,300 had been written off certain stock, which was a poor selling line, having cost ₹ 6,900. A portion of these goods was sold in April, 2015 at a loss of ₹ 250 on original cost of ₹ 3,450. The remainder of this stock was now estimated to be worth the original cost. Subject to above exception, gross profit had remained at a uniform rate throughout.

The stock salvaged was ₹ 5,800.

Show the amount of claim.

6. On 1st April, 2015 there was a devastating fire in the godown of Fire proof Equipment Manufacturing Ltd., which completely destroyed the stock and also other books and records. However, they are able to obtain the following information from their Income-Tax and Sales Tax Consultants:

Particulars	₹
Sales: For the year to 31-12-2014.	8,00,000
For January and February 2015.	80,000
Purchases: For the year to 31-12-20142.	3,65,000
For January and February 2015.	24,000
Stocks (At cost):	
As at 1-1-2014	1,00,000
As at 31-12-2014	45,000
Wages for the year to 31-12-2014.	1,08,000
Other direct expenses for the year to 31-12-2014.	72,000

Further Information:

(1) The Sales and Purchases for March, 2015 may be assumed as having been made at the same rate as in past two months.

(2) In January, 2015 a theft had taken place as a result of which goods of the value of ₹ 6,000 were lost.

(3) Wages and other direct expenses may be taken after 31-12-2014 at the same rate as in the year 2014.

(4) Insurance policy was taken for ₹ 22,500. There was an average clause in the policy.

You are required to prepare a statement showing the claim to be lodged with the Insurance Co., taking the value of Salvage at ₹ 5,000. All workings should form part of your answer.

7.The premises of Simal were destroyed by fire on 30-4-2015. Following details were available.

Details	**2012** ₹	**2013** ₹	**2014** ₹	**2015** ₹
Opening Stock	20,000	22,000	11,800	34,020
Sales	2,22,000	2,02,500	1,93,500	28,000
Purchases	1,60,000	1 ,45,000	1,70,000	35,000
Freight Outward	6,000	7,000	3,000	2,500
Freight Inward	5,000	3,000	5,000	1,000
Return Inward	22,000	4,000	6,000	2,000
Closing Stock	22,000	11,800	34,020	?

Further Information:

(1) In 2012, while valuing closing stock, goods costing ₹ 5,000 were valued at ₹ 4,000 and they were sold in 2013, for ₹ 4,500.

(2) In 2013, while valuing closing stock, goods costing ₹ 6,000 were wrongly valued at ₹ 7,000 and were sold in 2015 for ₹ 5,500.

(3) In December 2014 while valuing closing stock, goods costing ₹ 12,000 were valued at ₹ 10,000. 50% of these goods were sold before 30-4-2015 for ₹ 6,000.

(4) The goods salvaged were ₹ 10,000.

(5) Accounts were closed every year on 31st December.

Prepare statement of claim, showing the amount of claim.

8. A fire occurred in the premises of Ajit on 1st Sept., 2015 and stock of the value of ₹ 1,01,000 was salvaged. However, books and records were saved. The following information was available:

Particulars	₹
Purchases for the year ended 31-3-2015	6,80,000
Sales for the year ended 31-3-2015	11,00,000
Purchases from 1-3-2015 to 1-9-2015	2,50,000
Sales from 1-3-2015 to 1-9-2015	3,60,000
Stock on 31-3-2014	3,00,000
Stock on 31-3-2015	3,40,000

Further information is given:

(1) The stock on 31-3-2015 was overvalued by ₹ 20,000.

(2) The sales and purchases for the year ended 31-3-2015 were spread evenly during the year.

(3) From April, 2015 selling price was lowered by 10%.

(4) The stock was insured for ₹ 3,00,000 and there was average clause in the policy.

Calculate the amount of the claim.

[Ans.: G.P. Ratio = 42%, SOFD = 4,39,499, Claim = 2,31,057]

9. Hari was a paper merchant and his shop was destroyed by fire on 30th April, 2014. He insured the stock for ₹ 20,000. The balance sheet as on 31st December, 2014 disclosed inter alia following items:

Stock ₹ 22,500 and Creditors ₹ 13,500

On examination of books of accounts up to the date of fire, the following particulars were found:

(1) Payments to Creditors ₹ 79,000

(2) Sales ₹ 98,400

(3) Creditors as on 30th April, 2014 ₹ 11,800

The stock on 31st Dec., 2014 included shop-soiled items amounting to ₹ 6,800. These goods were sold at a loss of ₹ 400 in Feb., 2015. Undamaged goods after the fire were ₹ 12,000.

The normal rate of gross profit was 33-1/3% on cost and there was average clause in the policy.

Calculate the amount of claim to be made to the insurance company.

[Ans.: G.P. Ratio = $\frac{1}{3}$ – 33%, SOFD = 19,600, Claim = 7,755]

10. On 30-9-2015, the stock of Fred Perry was lost in a fire accident. From the available records the following information is made available to you to enable you to prepare a statement of claim on the insurer:

Particulars	₹
Stock at cost on 1-4-2014	37,500
Stock at cost on 31-3-2015	52,000
Purchases less returns for the year ended 31-3-2015	2,53,750
Sales less returns for the year ended 31-3-2015	3,15,000
Purchases less returns upto 30-9-2015	1,45,000
Sales less returns upto 30-9-2015	1,84,050

In valuing the stock on 31-3-2015, due to obsolescence 50% of the value of the Stock, which originally cost ₹ 6,000, had been written off. In May 2015, three-fourth of this Stock had been sold at 90% of original cost and it is now expected that the balance of the obsolete stock would also realise the same price. Subject to the above, Gross Profit had remained uniform throughout.

Stock to the value of ₹ 7,200 was salvaged.

11. A fire occurred in the godown of a firm on 31st January, 2015. The stock on 1st January, 2015 was valued at ₹ 67,460. The transactions and other information of the period between 1st January to 31st January were as follows from which you are required to ascertain the value of goods destroyed.

(1) Purchases from 1-1-2015 to 31-1-2015 amounted to ₹ 48,200 of which goods worth ₹ 1,900 were received on 2-2-2015.

(2) Sales from 1-1-2015 to 31-1-2015 amounted to ₹ 56,800 of which sales on the basis of sale or return amounted to ₹ 3,600. No intimation has been received from the customers about half the goods sold on sale or return.

(3) Some of the goods costing ₹ 2,800 were defective and were sold for ₹ 1,200. The same was included in the stock at cost on 1st January.

(4) On 31st January, 2015, goods worth ₹ 3,200 were lying unsold with the consignee, sent to the them on 25-1-2015.

(5) Information regarding cost of goods sold & gross profit of the last three years was as follows:

YEARS	Cost of Goods Sold (₹)	Gross Profit (₹)
2012	80,000	20,000
2013	1,23,000	27,000
2014	1,40,000	39,600

12. On 1st April, 2015 the godown of Stone Ltd. was destroyed by fire. The records of the company revealed the following particulars.

Particulars	₹
Stock on 1st January, 2014	75,000
Stock on 31st December, 2014	80,000
Purchases during 2014	3,10,000
Sales during 2014	4,00,000
Purchases from 1st January, 2015 to the date of the fire	75,000
Sales from 1st January, 2015 to the date of the fire	1,00,000

In valuing closing stock of 2014 ₹ 5,000 were written off whose cost was ₹ 4,800. Part of this stock was sold in 2015 at a loss of ₹ 400 for ₹ 2,400. Stock salvaged was ₹ 5,000. The godown was fully insured.

Indicate the amount of claim to be lodged with the Insurance company.

13. On 31st May, 2015, the Premises and Stock of a firm were totally destroyed by fire, the books of account, however, being saved. In order to make a Claim on their Fire Policy they ask your advice and you are able to obtain the following information. The Stock on hand has always been valued at 5% below cost:

Details	2012 ₹	2013 ₹	2014 ₹	2015 ₹
Opening Stock as valued	22,800	30,400	36,100	39,900
Purchases less Returns	91,000	1,10,000	1,20,000	41,000
Sales less Returns	1,40,000	1,70,000	1,86,000	75,000
Wages	28,400	31,200	34,200	12,000
Closing Stock	30,400	36,100	39,900	?

Prepare a Statement for Submission to the Insurance Company in support of your Claim for loss of Stock.

14. The premises of KIM Enterprise Ltd. were engulfed by fire on 31st August, 2015. In this fire major portion of stock was destroyed. The Company has an insurance policy for ₹ 60,000 with average clause. From the following details, ascertain amount of claim.

(1) During the year ended 31-3-2015, Sales were ₹ 5,00,000 and Purchases were ₹ 4,24,000.

(2) For period 1-4-2015 to 31-8-2015, same were ₹ 4,00,000 and ₹ 3,00,000.

(3) Stock on 1-4-2014 was ₹ 90,000 and 1-4-2015 it was valued ₹ 1,32,000.

(4) The stock was valued @ 90% of cost up to 31-3-2014, but on 31-3-2015 it was valued @110% of cost.

(5) The account for 2014-2015 had an error Purchase of Equipment costing ₹ 4,000 was included in Purchases.

(6) The sales since April, 2015 does not include goods costing ₹ 40,000 dispatched to customers at normal profit margins. Till date of fire 50% of these are approved.

15. A fire on October 1, 2015 destroyed the stocks of a firm. The business records were saved and from them the following particulars were ascertained.

Particulars	₹
Stock at cost on April 30, 2014	44,300
Stock at cost on April 30, 2015	37,550
Purchases for the year to April 30, 2015	1,03,850
Sales for the year to April 30, 2015	1,52,500
Purchase form May 1, 2015 to September 30, 2015	37,350
Sales from May 1, 2015 to September 30, 2015	59,000

In valuing the stock on April 30, 2015 ₹ 800 had been written off a particular line of goods which had originally cost ₹ 1,800 and which were sold in June 2015 for ₹ 1,750. Except as regards this transaction the ratio of gross profit had remained unchanged throughout.

The value of stock salvaged from the fire was ₹ 5,105. You are required to calculate the amount of the claim to be presented to the insurance company in respect of the loss of stock.

16. Mr. Rao Bahadur suffered loss of stock due to fire on August 20, 2015. From the following particulars, calculate claim to be made by the trader.

Particulars	₹
Stock on 31st December 2013	1,00,000
(Including stock purchased during the year at ₹ 8,000 valued at ₹ 4,000 because of poor selling price)	
Wages paid 2014	30,000
(Including wages paid for the construction of a showroom for which workers of the factory worked ₹ 2,000. Manufacturing wages ₹ 1,500 were outstanding)	
Freight inward: 2014	5,000
Purchases: 2014	1,20,000
(Including purchases of furniture of ₹ 1,500 wrongly passed through Invoice book)	
Sales: 2014	2,46,000
(Including sale of 1/4th of the stock at ₹ 1,000 which has a poor selling line and which was valued at ₹ 4,000 on 31.12.2013)	
Stock on December 31, 2014:	42,000
(Including remaining stock which had a poor selling line at the same value)	

Purchases upto August 20, 2015	1,42,800
Sales upto August 20, 2015 (Including sale of the 1/3 of the remaining stock which had a poor selling line at ₹ 800)	1,42,900

The remaining stock, which had a poor selling line, was considered at 80% of the original cost for the purpose of insurance claim. The salvage was ₹ 47,400. The firm had taken a policy of ₹ 40,000. There was an average clause in the policy.