DIRECTORATE OF EDUCATION
Govt. of NCT, Delhi

SUPPORT MATERIAL

(2022-2023)

Class : XII

ACCOUNTANCY

Under the Guidance of

Shri Ashok Kumar
Secretary (Education)

Shri Himanshu Gupta
Director (Education)

Dr. Rita Sharma
Addl. DE (School & Exam.)

Coordinators

Mr. Sanjay Subhas Kumar	**Mrs. Sunita Dua**	**Mr. Raj Kumar**	**Mr. Krishan Kumar**
DDE (Exam)	OSD (Exam)	OSD (Exam)	OSD (Exam)

Production Team
Anil Kumar Sharma

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ASHOK KUMAR
IAS

सत्यमेव जयते

सचिव (शिक्षा)
राष्ट्रीय राजधानी क्षेत्र
दिल्ली सरकार
पुराना सचिवालय, दिल्ली-110054
दूरभाष : 23890187 टेलीफैक्स : 23890119

Secretary (Education)
Government of National Capital Territory of Delhi
Old Secretariat, Delhi-110054
Phone : 23890187 Telefax : 23890119
e-mail : secyedu@nic.in

MESSAGE

Remembering the words of John Dewey, "Education is not preparation for life, education is life itself, I highly commend the sincere efforts of the officials and subject experts from Directorate of Education involved in the development of Support Material for classes IX to XII for the session 2022-23.

The Support Material is a comprehensive, yet concise learning support tool to strengthen the subject competencies of the students. I am sure that this will help our students in performing to the best of their abilities.

I am sure that the Heads of School and teachers will motivate the students to utilise this material and the students will make optimum use of this Support Material to enrich themselves.

I would like to congratulate the team of the Examination Branch along with all the Subject Experts for their incessant and diligent efforts in making this material so useful for students.

I extend my Best Wishes to all the students for success in their future endeavours.

(Ashok Kumar)

HIMANSHU GUPTA, IAS
Director, Education & Sports

सत्यमेव जयते

Directorate of Education
Govt. of NCT of Delhi
Room No. 12, Civil Lines
Near Vidhan Sabha,
Delhi-110054
Ph.: 011-23890172
E-mail: diredu@nic.in

MESSAGE

"A good education is a foundation for a better future."
- Elizabeth Warren

Believing in this quote, Directorate of Education, GNCT of Delhi tries to fulfill its objective of providing quality education to all its students.

Keeping this aim in mind, every year support material is developed for the students of classes IX to XII. Our expert faculty members undertake the responsibility to review and update the Support Material incorporating thelatest changes made by CBSE. This helps the students become familiar with the new approaches and methods, enabling them to become good at problem solving and critical thinking. This year too, I am positive that it will help our students to excel in academics.

The support material is the outcome of persistent and sincere efforts of our dedicated team of subject experts from the Directorate of Education. This Support Material has been especially prepared for the students. I believe its thoughtful and intelligent use will definitely lead to learning enhancement.

Lastly, I would like to applaud the entire team for their valuable contribution in making this Support Material so beneficial and practical for our students.

Best wishes to all the students for a bright future.

(HIMANSHU GUPTA)

Dr. RITA SHARMA
Additional Director of Education
(School/Exam)

सत्यमेव जयते

Govt. of NCT of Delhi
Directorate of Education
Old Secretariat, Delhi-110054
Ph. : 23890185

D.O. No. PS/Addl.DE/Sch/2022/131
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संदेश

शिक्षा निदेशालय, दिल्ली सरकार का महत्वपूर्ण लक्ष्य अपने विद्यार्थियों का सर्वांगीण विकास करना है। इस उद्देश्य को ध्यान में रखते हुए शिक्षा निदेशालय ने अपने विद्यार्थियों को उच्च कोटि के शैक्षणिक मानकों के अनुरूप विद्यार्थियों के स्तरानुकूल सहायक सामग्री कराने का प्रयास किया है। कोरोना काल के कठिनतम समय में भी शिक्षण अधिगम की प्रक्रिया को निर्बाध रूप से संचालित करने के लिए संबंधित समस्त अकादमि समूहों और क्रियान्वित करने वाले शिक्षकों को हार्दिक बधाई देती हूँ।

प्रत्येक वर्ष की भाँति इस वर्ष भी कक्षा 9वीं से कक्षा 12वीं तक की सहायक सामग्रियों में सी.बी.एस.ई के नवीनतम दिशा-निर्देशों के अनुसार पाठयक्रम में आवश्यक संशोधन किए गए हैं। साथ ही साथ मूल्यांकन से संबंधित आवश्यक निर्देश भी दिए गए हैं। इन सहायक सामग्रियों में कठिन से कठिन सामग्री को भी सरलतम रूप में प्रस्तुत किया गया है ताकि शिक्षा निदेशालय के विद्यार्थियों को इसका भरपूर लाभ मिल सके।

मुझे आशा है कि इन सहायक सामग्रियों के गहन और निंरतर अध्ययन के फलस्वरूप विद्यार्थियों में गुणात्मक शैक्षणिक संवर्धन का विस्तार उनके प्रदर्शनो में भी परिलक्षित होगा। इस उत्कृष्ट सहायक सामग्री को तैयार करने में शामिल सभी अधिकारियों तथा शिक्षकों को हार्दिक बधाई देती हूँ तथा सभी विद्यार्थियों को उनके उज्जवल भविष्य की शुभकामनाएं देती हूँ।

रीता शर्मा
(रीता शर्मा)

DIRECTORATE OF EDUCATION
Govt. of NCT, Delhi

SUPPORT MATERIAL
(2022-2023)

ACCOUNTANCY

Class : XII

(English Medium)

NOT FOR SALE

PUBLISHED BY : DELHI BUREAU OF TEXTBOOKS

भारत का संविधान

भाग 4क

नागरिकों के मूल कर्तव्य

अनुच्छेद 51 क

मूल कर्तव्य – भारत के प्रत्येक नागरिक का यह कर्तव्य होगा कि वह –

(क) संविधान का पालन करे और उसके आदर्शों, संस्थाओं, राष्ट्रध्वज और राष्ट्रगान का आदर करे;

(ख) स्वतंत्रता के लिए हमारे राष्ट्रीय आंदोलन को प्रेरित करने वाले उच्च आदर्शों को हृदय में संजोए रखे और उनका पालन करे;

(ग) भारत की संप्रभुता, एकता और अखंडता की रक्षा करे और उसे अक्षुण्ण बनाए रखे;

(घ) देश की रक्षा करे और आह्वान किए जाने पर राष्ट्र की सेवा करे;

(ङ) भारत के सभी लोगों में समरसता और समान भ्रातृत्व की भावना का निर्माण करे जो धर्म, भाषा और प्रदेश या वर्ग पर आधारित सभी भेदभावों से परे हो, ऐसी प्रथाओं का त्याग करे जो महिलाओं के सम्मान के विरुद्ध हों;

(च) हमारी सामासिक संस्कृति की गौरवशाली परंपरा का महत्त्व समझे और उसका परिरक्षण करे;

(छ) प्राकृतिक पर्यावरण की, जिसके अंतर्गत वन, झील, नदी और वन्य जीव हैं, रक्षा करे और उसका संवर्धन करे तथा प्राणिमात्र के प्रति दयाभाव रखे;

(ज) वैज्ञानिक दृष्टिकोण, मानववाद और ज्ञानार्जन तथा सुधार की भावना का विकास करे;

(झ) सार्वजनिक संपत्ति को सुरक्षित रखे और हिंसा से दूर रहे;

(ञ) व्यक्तिगत और सामूहिक गतिविधियों के सभी क्षेत्रों में उत्कर्ष की ओर बढ़ने का सतत् प्रयास करे, जिससे राष्ट्र निरंतर बढ़ते हुए प्रयत्न और उपलब्धि की नई ऊँचाइयों को छू सके; और

(ट) यदि माता-पिता या संरक्षक है, छह वर्ष से चौदह वर्ष तक की आयु वाले अपने, यथास्थिति, बालक या प्रतिपाल्य को शिक्षा के अवसर प्रदान करे।

Constitution of India

Part IV A (Article 51 A)

Fundamental Duties

It shall be the duty of every citizen of India —

(a) to abide by the Constitution and respect its ideals and institutions, the National Flag and the National Anthem;

(b) to cherish and follow the noble ideals which inspired our national struggle for freedom;

(c) to uphold and protect the sovereignty, unity and integrity of India;

(d) to defend the country and render national service when called upon to do so;

(e) to promote harmony and the spirit of common brotherhood amongst all the people of India transcending religious, linguistic and regional or sectional diversities; to renounce practices derogatory to the dignity of women;

(f) to value and preserve the rich heritage of our composite culture;

(g) to protect and improve the natural environment including forests, lakes, rivers, wildlife and to have compassion for living creatures;

(h) to develop the scientific temper, humanism and the spirit of inquiry and reform;

(i) to safeguard public property and to abjure violence;

(j) to strive towards excellence in all spheres of individual and collective activity so that the nation constantly rises to higher levels of endeavour and achievement;

*(k) who is a parent or guardian, to provide opportunities for education to his child or, as the case may be, ward between the age of six and fourteen years.

Note: The Article 51A containing Fundamental Duties was inserted by the Constitution (42nd Amendment) Act, 1976 (with effect from 3 January 1977).

*(k) was inserted by the Constitution (86th Amendment) Act, 2002 (with effect from 1 April 2010).

भारत का संविधान

उद्देशिका

हम, भारत के लोग, भारत को एक [1][**संपूर्ण प्रभुत्व-संपन्न समाजवादी पंथनिरपेक्ष लोकतंत्रात्मक गणराज्य**] बनाने के लिए, तथा उसके समस्त नागरिकों को :

सामाजिक, आर्थिक और राजनैतिक **न्याय,**

विचार, अभिव्यक्ति, विश्वास, धर्म

और उपासना की **स्वतंत्रता,**

प्रतिष्ठा और अवसर की **समता**

प्राप्त कराने के लिए,

तथा उन **सब में**

व्यक्ति की गरिमा और [2][**राष्ट्र की एकता और अखंडता**] सुनिश्चित करने वाली **बंधुता**

बढ़ाने के लिए

दृढ़संकल्प होकर **अपनी इस संविधान सभा में** आज तारीख 26 नवंबर, 1949 ई. को **एतद्द्वारा इस संविधान को अंगीकृत, अधिनियमित और आत्मार्पित करते हैं।**

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1. संविधान (बयालीसवां संशोधन) अधिनियम, 1976 की धारा 2 द्वारा (3.1.1977 से) ''प्रभुत्व-संपन्न लोकतंत्रात्मक गणराज्य'' के स्थान पर प्रतिस्थापित।
2. संविधान (बयालीसवां संशोधन) अधिनियम, 1976 की धारा 2 द्वारा (3.1.1977 से) ''राष्ट्र की एकता'' के स्थान पर प्रतिस्थापित।

THE CONSTITUTION OF INDIA

PREAMBLE

WE, THE PEOPLE OF INDIA, having solemnly resolved to constitute India into a [1]**[SOVEREIGN SOCIALIST SECULAR DEMOCRATIC REPUBLIC]** and to secure to all its citizens :

JUSTICE, social, economic and political;

LIBERTY of thought, expression, belief, faith and worship;

EQUALITY of status and of opportunity; and to promote among them all

FRATERNITY assuring the dignity of the individual and the [2][unity and integrity of the Nation];

IN OUR CONSTITUENT ASSEMBLY this twenty-sixth day of November, 1949 do **HEREBY ADOPT, ENACT AND GIVE TO OURSELVES THIS CONSTITUTION.**

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1. Subs. by the Constitution (Forty-second Amendment) Act, 1976, Sec.2, for "Sovereign Democratic Republic" (w.e.f. 3.1.1977)
2. Subs. by the Constitution (Forty-second Amendment) Act, 1976, Sec.2, for "Unity of the Nation" (w.e.f. 3.1.1977)

Team Members for Review of Support Material

S.No.	Name & Designation	School Name/Branch
1.	Mr. Ram Deo (Vice-Principal) (OSD Exam)	Examination Branch Directorate of Education Old Secretariat, Delhi-54
2.	Mr. Arun Kumar Sethi (Lecturer Commerce)	Core Academic Unit DOE, Old Secretariat Delhi-54 Yogi Arvind SBV No.1, Sec IV, Dr. Ambedkar Nagar New Delhi-110062
3.	Mr. Pramod Chander (Lecturer Commerce)	SBV Gokhle Marg, Delhi-6
4.	Ms. Sonia Gupta (Lecturer Commerce)	SKV, Sec. 20, Rohini Extn.
5.	Mr. Shivam Kumar (Lecturer Commerce)	RPVV Civil lines, Delhi

Accountancy (Code No. 055)

Class-XII (20220-23)

Theory: 80 Marks **3 Hours**

Project: 20 Marks

Units			Periods	Marks
Part A	**Accountancy for Partnership Firms and Companies**			
	Unit 1. Accounting for Partnership Firms		105	36
	Unit 2. Accounting for Companies		45	24
			150	60
Part B	**Financial Statement Analysis**			
	Unit 3. Analysis of Financial Statement		30	12
	Unit 4. Cash Flow Statement		20	8
			50	20
Part C	**Project Work**		50	20
	Project work will include:			
	Project File	4 Mark		
	Written Test	12 Marks (One Hour)		
	Viva Voice	4 Marks		

Part A: Accounting for Partnership Firms and Companies

Unit 1: Accounting for Partnership Firms

Units/Topics	Learning Outcomes
• Partnership, features, Partnership Deed	**After going through this Unit, the students will be able to:**
• Provisions of the Indian Partnership Act 1932 in the absence of partnership deed	• state the meaning of partnership, partnership firm and partnership deed.
• Fixed v/s fluctuating capital accounts Preparation of Profit and Loss Appropriation account-division of profit among partners, guarantee of profits	• describe the characteristic features of partnership and the contents of partnership deed.
• Past adjustments (relating to interest on capital, interest on drawing, salary and profit sharing ratio).	• discuss the significance of provision of Partnership Act in the absence of partnership deed.
• Goodwill meaning, nature, factors affecting and methods of valuation-average profit, super profit and capitalization.	• differentiate between fixed and fluctuating capital, outline the process and develop the understanding and skill of preparation of Profit and Loss Appropriation Account.
Note: Interest on partner's loan is to be treated as a charge against profits Goodwill meaning, factors affecting, need for valuation, methods for calculation (average profits, super profits and capitalization), adjusted through partners capital/ current account or by raising and writing off goodwill (AS 26)	• develop the understanding and skill of preparation profit and loss appropriation account involving guarantee of profits. • develop the understanding and skill of making past adjustments. • state the meaning, nature and factors affecting goodwill
Accounting for Partnership firms - Reconstitution and Dissolution.	• develop the understanding and skill of valuation of goodwill using different methods.

• **Change in the Profit Sharing Ratio** among the existing partners - sacrificing ratio, gaining ratio, accounting for revaluation of assets and reassessment of liabilities and treatment of reserves, accumulated profits and losses. Preparation of revaluation account and balance sheet.	• state the meaning of sacrificing ratio, gaining ratio and the change in profit sharing ratio among existing partners. • develop the understanding of accounting treatment of revaluation assets and reassessment of liabilities and treatment of reserves and accumulated profits by preparing revaluation account and balance sheet.
• **Admission of a partner -** effect of admission of a partner on change in the profit sharing ratio, treatment of goodwill (as per AS 26). treatment for revaluation of assets and re assessment of liabilities, treatment of reserves, accumulated profits and losses, adjustment of capital accounts and preparation of capital, current account and balance sheet.	• explain the effect of change in profit sharing ratio on admission of a new partner. • develop the understanding and skill of treatment of goodwill as per AS-26, treatment of revaluation of assets and re-assessment of liabilities, treatment of reserves and accumulated profits, adjustment of capital accounts and preparation of capital, current account and balance sheet of the new firm.
• **Retirement and death of a partner**: effect of retirement/ death of a partner on change in profit sharing ratio, treatment of goodwill (as per AS 26), treatment for revaluation of assets and reassessment of liabilities, adjustment of accumulated profits, losses and reserves, adjustment of capital accounts and preparation of capital, current account and balance sheet. Preparation of loan account of the retiring partner.	• explain the effect of retirement/ death of a partner on change in profit sharing ratio. • develop the understanding of accounting treatment of goodwill, revaluation of assets and re-assessment of liabilities and adjustment of accumulated profits, losses and reserves on retirement/ death of a partner and capital adjustment.
• Calculation of deceased partner's share of profit till the date of death. Preparation of deceased partner's capital account and his executor's account.	• develop the skill of calculation of deceased partner's share till the time of his death and prepare deceased partner's and executor's account.

• **Dissolution of a partnership firm:** meaning of dissolution of partnership and partnership firm, types of dissolution of a firm. Settlement of accounts - preparation of realization account, and other related accounts: capital accounts of partners and cash/ bank a/c (excluding piecemeal distribution, sale to a company and insolvency of partner(s)).	• discuss the preparation of the capital accounts of the remaining partners and the balance sheet of the firm after retirement/ death of a partner. • understand the situations under which a partnership firm can be dissolved. • develop the understanding of preparation of realisation account and other related accounts.
Note: (i) If the realized value of tangible assets is not given it should be considered as realized at book value itself. (ii) If the realized value of intangible assets is not given it should be considered as nil (zero value). (iii) In case, the realization expenses are borne by a partner, clear indication should be given regarding the payment thereof.	

Unit-3 Accounting for Companies

Units/Topics	Learning Outcomes
Accounting for Share Capital • Features and types of companies • Share and share capital: nature and types.	• state the meaning of share and share capital and differentiate between equity shares and preference shares and different types of share capital.
• Accounting for share capital: issue and allotment of equity and preferences shares. Public subscription of shares - over subscription and under subscription of shares; issue at par and at premium, calls in advance and arrears (excluding interest), issue of shares for consideration other than cash.	• state the meaning of share and share capital and differentiate between equity shares and preference shares and different types of share capital. • understand the meaning of private placement of shares and Employee Stock Option Plan. explain the accounting treatment of share capital transactions regarding issue of shares.

• Concept of Private Placement and Employee Stock Option Plan (ESOP), Sweat Equity.	• develop the understanding of accounting treatment of forfeiture and re-issue of forfeited shares.
• Accounting treatment of forfeiture and reissue of shares. • Disclosure of share capital in the Balance Sheet of a company.	• describe the presentation of share capital in the balance sheet of the company as per schedule III part I of the Companies Act 2013.
Accounting for Debentures • Debentures: Meaning, types, Issue of debentures at par, at a premium and at a discount. Issue of debentures for consideration other than cash; Issue of debentures with terms of redemption; debentures as collateral security-concept, interest on debentures. Writing off discount / loss on issue of debentures.	• explain the accounting treatment of different categories of transactions related to issue of debentures. • develop the understanding and skill of writing of discount / loss on issue of debentures. • understand the concept of collateral security and its presentation in balance sheet.
Note: Discount or loss on issue of debentures to be written off in the year debentures are allotted from Security Premium Reserve (if it exits) and then from Statement of Profit and Loss as Financial Cost (AS 16)	• develop the skill of calculating interest on debentures and its accounting treatment. • state the meaning of redemption of debentures.

Part B: Financial Statement Analysis

Unit 4: Analysis of Financial Statements

Units/Topics	Learning Outcomes
Financial statements of a Company: Meaning, Nature, Uses and importance of financial Statement. Statement of Profit and Loss and Balance Sheet in prescribed form with major headings and sub headings (as per Schedule III to the Companies Act, 2013)	**After going through this Unit, the students will be able to:** develop the understanding of major headings and sub-headings (as per Schedule III to the Companies Act, 2013) of balance sheet as per the prescribed norms / formats.
Note: Exceptional items, extraordinary items and profit (loss) from discontinued operations are excluded,	• state the meaning, objectives and limitations of financial statement analysis.

• **Financial Statement Analysis:** Meaning, Significance Objectives, importance and limitations.	• discuss the meaning of different tools of 'financial statements analysis'.
• **Tools for Financial Statement Analysis:** Cash flow analysis, ratio analysis.	• state the meaning, objectives and significance of different types of ratios.
• **Accounting Ratios:** Meaning, Objectives, Advantages, classification and computation.	• develop the understanding of computation of current ratio and quick ratio.
• **Liquidity Ratios:** Current ratio and Quick ratio.	• develop the skill of computation of debt equity ratio, total asset to debt ratio, proprietary ratio and interest coverage ratio.
• **Solvency Ratios:** Debt to Equity Ratio, Total Asset to Debt Ratio, Proprietary Ratio and Interest Coverage Ratio. Debt to Capital Employed Ratio.	• develop the skill of computation of inventory turnover ratio, trade receivables and trade payables ratio and working capital turnover ratio and others.
• **Activity Ratios:** Inventory Turnover Ratio, Trade Receivables Turnover Ratio, Trade Payables Turnover Ratio, Fixed Asset Turnover Ratio, Net Asset Turnover Ratio and Working Capital Turnover Ratio.	• develop the skill of computation of gross profit ratio, operating ratio, operating profit ratio, net profit ratio and return on investment.
• **Profitability Ratios:** Gross Profit Ratio, Operating Ratio, Operating Profit Ratio, Net Profit Ratio and Return on Investment.	

Note: Net Profit Ratio is to be calculated on the basis of profit before and after tax.

Unit 5: Cash Flow Statement

Units/Topics	**Learning Outcomes**
• Meaning, objectives Benefits, Cash and Cash Equivalents, Classification of Activities and preparation (as per AS 3 (Revised) (Indirect Method only)	**After going through this Unit, the students will be able to:** • state the meaning and objectives of cash flow statement.

Note: (i) Adjustments relating to depreciation and amortization, profit or loss on sale of assets including investments, dividend (both final and interim) and tax. (ii) Bank overdraft and cash credit to be treated as short term borrowings. (iii) Current Investments to be taken as Marketable securities unless otherwise specified.	• develop the understanding of preparation of Cash Flow Statement using indirect method as per AS 3 with given adjustments.

Note: Previous years' Proposed Dividend to be given effect, as prescribed in AS-4, Events occurring after the Balance Sheet date. Current years' Proposed Dividend will be accounted for in the next year after it is declared short term borrowings. by the shareholders.

PROJECT WORK

Note: Kindly refer to the Guidelines published by the CBSE The comprehensive project may contain simple GST calculations

Suggested Question Paper Design
Accountancy (Code No. 055)
Class XII (2022-23)

Theory: 80 Marks

Project: 20 Marks **3 Hrs.**

S.no.	Typology of Questions	Marks	Percentage
1.	**Remembering and Understanding:** Exhibit memory of previously learned material by recalling facts, terms, basic concepts, and answers Demonstrate understanding of facts and ideas by organizing, comparing, translating interpreting, giving descriptions, and stating main ideas	44	55%
2.	**Applying:** Solve problems to new situations by applying acquired knowledge, facts, techniques and rules in a different way.	19	23.25%
3.	**Analysing, Evaluating and Creating:** Examine and break information into parts by identifying motives or causes. Make inferences and find evidence to support generalizations. Present and defend opinions by making judgments about information, validity of ideas, or quality of work based on a set of criteria. Compile information together in a different way by combining elements in a new pattern or proposing alternative solutions	17	21.25%
	Total	**80**	**100%**

CONTENTS

Chapter -1

Accounting for Partnersip Firms Fundamentals

TOPIC	MEANING/EXPLANATION
Meaning of Partnership	Section 4 of the Indian Partnership Act 1932 defines partnerships as the 'relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.
Essential Features of Partnership	1. Two or More Persons 2. Agreement 3. Lawful Business 4. Mutual Agency 5. Sharing of Profit 6. Relationship of Mutual agency among the partners **Note:** • By virtue of Section 464 of the Companies Act 2013, the Central Government is empowered to prescribe maximum number of partners in a firm but the number of partners cannot be more than 100 • The Central government has prescribed the maximum number of partners in a firm to be 50 under Rule 10 of the Companies (Micellanous) Rules, 2014, So, a partnership firm cannot have more than 50 partners.
Partnership Deed	The Partnership Act does not require that the agreement must be in writing. But wherever it is in writing, the document, which contains terms of the agreement is called 'Partnership Deed'
In the absence of partnership deed/if partnership deed is silent (the relevant provisions of the	1. Profits/losses are shared equally by all the partners 2. Interest on capital is not allowed to partners 3. Interest on drawing is not charged from partners 4. Interest on advances/loan by a partner is paid @ 6% p. a.

Indian Partenrships act 1932, become applicable Meaning of Partners and firm Firm's name	5. Remuneration (Salary and Commission etc.) to Parters not allowed. Persons who have entered into partnership with one another are individually called partners and collectively called 'firm' The Name under which the business is carried is calle the 'firm's name'
Is Partnership firm has legal entity?	A partnership firm has no separate legal entity, apart from the partner's constituting it.
Rights of partners	1. Right to participate in the management of the business. 2. Right to be constituted about affairs of the company 3. Right to inspect the books of account and have a copy of it. 4. Right to spare profits or losses with others in the agreed ratio etc.
Contents of partnership deed	• Description of the Partners and Firm. • Principal place and nature of the business. • Commencement of Partnership, Capital Contribution • Interest on Capital/Drawing/Partnes Loan • Methods of valuation of Good will/Assets etc.
Liabilities of Partners (subject to contract between the partners	1. If a partner derives any profit for him/her self from any transaction of the firm or from the use of the property or business connection of the firm or the firm name, he/she shall account for the profit and pay it to the firm. 2. If a partner carries on any business of the same nature as and competing with that of the firm, he/she shall account for and pay to the firm, all profit made by him/her in that business.
Profit and Loss Appropriation Account	It is merely an extension of the Profit and Loss Accoutn of the firm. It shows how the profits are appropriated or distributed among the partners.

	All adjustments in respect of partner's salary, partner's commission, interest on capital, interest on drawings, etc are made through this account.

	Charge against profit	**_Appropriation of profit_**
Difference between Charge against profit and Appropriation of Profit	1. It is always debited to profit and loss account (whether profit or loss) before appropriation.	1. It is debited to profit and loss appropriation account (If profit avai lable) after charging.
	2. Examples are rent paid to a partner, interest on partners loan.	2. Examples are salary/ commission to partners, interest on capital, transfer of profits to general reserve

	B asis of Distinction	***Fixed Capital Account***	***Fluctuating Capital Account***
Difference between fixed and fluctating capital account	*1. Number Of Accounts*	• *Two accounts maintained for each partner i.e. fixed capital account and current ccount*	• *Only one ac-count capital account is main-tained*
	2. Fixed balance	• *Balance of fixed account remains fixed except when fresh capital is intro duced or withdrwan*	• *Balance fluctuate with every transaction of partner with firm.*
	3. Ajustments	• *All adjustments for drawing, interest on drawing , Interest on capital, salary, commi-ssion, share of profit/ loss are adjusted in current account*	• *All adjustments for drawing, interest on drawing,interest on capital, salary, commission, fresh capital introduced / withdrawn, share of profit/loss are adjusted in capital account*

	4. Balance	• *It always shows credit balance in capital account*	• *It may show credit or debit balance*
Commission to Partners	*It may be computed as follows:* *1. If it is given as a precentage of net profit or of net profit before charging such commission.* ***COMMISSION** = Net Profit (before commission) xrate of commission/100* *2. If it is given as a percentage of net profit after charging such commission.* ***COMMISSION**=Net Profit (before commission)x rate of commission/100 +rate of commission*		
Calculation of interest of drawing	**[*INTREST ON DRAWING = TOTAL DRAWINGS X RATE OF INTREST /100 X AVERAGE PERIOD/12*]** • **[AVERAGE PERIOD =MONTHS LEFT AFTER FIRST DRAWING + MONTHS LEFT AFTER LAST DRAWING/2]**		

CASES	***AVERAGE PERIOD***
When the same amount is withdrawn at the beginning of each month	*6.5 Months*
When the same amount is withdrawn at the end of each month	*5.5 Months*
When the same amount is withdrawn in the middle of the month/quarter or date of drawing is not given	*6 Months*
If the same amount is withdrawn at the beginning of each quarter	*7.5 Months*
If the same amount is withdrawn at the end of each quarter	*4.5 Months*

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<td>Note: if the unequal amount is withdrawn at different dates or when there is irregular drawings, Interest on drawing will be calculated by simple method or product method Intrest on drawing in case of product mehtod =
Total product X rate of interest/100x1/12 (in case of months or 1/365 (in case of days)</td>
</tr>
<tr>
<td>Calculation of interest of capital</td>
<td>1. Interest on capital is generally provided for in two situations:
(i) when the partners contribute unequal amounts of capitals but share profits equally
(ii) where the capital contribution is same but porfit sharing is unequal
2. where there are both additon and withdrawl of capital by of partners during a financial year, the interest on capital is caluculated as follows:
(i) On the opening balance of the capital accounts of partners, interest is calcualted fot the whole year.
(ii) On the additional capital brought in by any partner during the year, interest is calculated from the date of introduction of additional capital to the last day of the financial year.
(iii) On the amount of capital withdrawn (other than usual drawings) during the year interest for the period from the date of withdrawal to the last day of the financial year is calcualted and deducted from the total of the interest calculated under points: (i) and (ii) above.
Alternatively, it can be calculated with respect to the amounts remained invested for the relevant periods.</td>
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<tr>
<td>Provisions related to interest on capital</td>
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<table>
<tr><th>CASES</th><th>PROVISION</th></tr>
<tr><td>1. When partership deed does not exist or nothing is mention in question about interest on capital</td><td>Interest on capital is not allowed</td></tr>
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2. *When partership deed provides for interest on capital but silent as to treatment of interest as a charge of appropriation*	• Interest on capital always treated as appropriaton • In case of loss: interest on capital is not allowed • In case of sufficient profit: interest on capital is allowed • In case of insufficient profit: interest is allowed only to the extent of rofits in the ratio of interest on capital.
When parterships deed provides for interest on capital as a charge	Interest on capital is allowed whether there is a profit or loss.

Gurantee of Profit to a Partner	Sometimes a partner is admitted into the firm with a gurantee of certain minimum amount by way of his share of profits of the firm. Such assurance may be given by all the old partners in a certain ratio or by any of the old partners, individually to the new partner. The minimum guranteed amount shall be paid to such new partner when his share of profit as per the profit sharing ratio is less than the guranteed amount.
Past Adjustments	Sometimes a few omissions or errors in the recording of transactions or the preparation of summary statements are found after the final accounts have been prepared and the profits distributed among the partners. The omission may be in respect of interest on capitals, interest on drawings, interest on partner's loan, partner's salary, partner's commi-ssions or outstanding expenses. There may may also be some changes in the provisions of partenrship deed or system of accounting having impact with retrospective effect. All these acts of omission and commissions need djustments for correction of their impact. Instead of altering old accounts, necessary adjustment can be made either; (a) through 'Profit and Loss Adjustments', or (b) directly in the capital accounts of the concerned partners.

Journal Entries Related to Profit and Loss Appropriation Account:

Data	Particulars	L.F.	Debit ₹	Credit ₹
1.	**For transfer of balance of Profit and Loss Account:** Profit and Loss A/c Dr. To Profit and Loss Appropriation A/c (Being net profit transferred to P&L Appropriation A/c) **For transfer of balance of Profit and Loss Account: if there is loss**			
	Profit and Loss appropriation A/c Dr. To Profit and Loss A/c (Being net loss transferred to P&L Appropriation A/c)			
2.	For Interest on Capital: (a) For allowing Interest on Capital Interest on Capital A/c Dr. To Partners Capital/Current A/cs (Being interest on Capital allowed @ % p.a.)			
	(b) For transferring Interest on Capital to Profit and Loss Appropriation A/C Profit and Loss Appropriation A/c Dr. To Interest on Capital A/c (Being Interest on Capital transferred to P&L Appropriation A/c)			
3.	For Salary or Commission payable to a Partner: (a) For allowing Salary or Commission to a partner- Partner's Salary or Commission A/c Dr. To Partner's Capital/Current A/c's (Being Salary/ Commission payable to partner) (b) For transferring Partner's salary/Commission A/C to Profit and Loss Appropriation A/c Profit and Loss Appropriation A/c Dr. To Partner's Salary/Commission A/c			

4.	For transfer of Reserves: Profit and Loss Appropriation A/c Dr To Reserve A/c (Being ressrve created)			
5. 6.	For Interest on Drawings: (a) For charging interest on partner's drawings Partner's Capital/Current A/c Dr. To interest on Drawings A/c (Being interest on drawings changed @% p.a.) (b) For transferring interest on drawings to Profit and Loss Appropriation A/c: Interest on Drawings A/c Dr. To Profit and Loss Appropriation A/c (Being interest on drawings transferred to P&L Appropriation A/c)			
	For transfer of profit (Credit balance of profit and loss Appropriation account) to partners Profit and Loss Appropriation A/c Dr. To Partner's Capital/Current A/cs (Being profits distributed among partners in profit sharing ratio)			

PARTNERSHIP FUNDAMENTALS PRACTISE QUESTIONS

1. Kumar Raja and Sanjay set up a partnership firm on April 1 2018. They contributed ₹. 5,00,000, ₹ 4, 00,000 and ₹ 3, 000,00, respectively as their capitals and agreed to share profits and losses in the ration of 3: 2: 1. Kumar is to be paid a salary of Rs. 10,000 per month and Raja, a Commission of ₹ 50,000. It is also provided that interest to be allowed on capital at 6% p.a.The drawings for the year were Kumar rs. 60,000, Raja ₹ 40,000 and Sanjay ₹ 20,000. Interest on drawings of ₹ 2700 was charged on Kumar's drawings, Rs 1800 on Raja's drawings and ₹ 900 on Sanjay's drawings. The net profit as per Profit and Loss Account for the year ending March 31, 2019 was ₹ 3, 56600. Pass the necessary journal entries and Prepare the Profit and Loss Appropriation Account to show the distribution of profit among the partners.

DATE	PARTICULAR	Dr. (₹)	Cr. (₹)
1.	Profit and Loss A/c Dr. To Profit and Loss Appropriation A/c (Transfer of the balance of Profit and Loss Account to Profit and Loss Appropriation (Account)	3,56,600	 3,56,600
2.	Salary to Kumar A/c Dr. To Kumar's Capital A/c (For crediting partner's salary to partner's capital account)	1,20,000	 1,20,000
3.	Profit and Loss Appropriation A/c Or. To Salary to Kumar A/c (For transferring partner's salary to Profit and Loss Appropriation Account)	1,20,000	 1,20,000
4.	Commission to Raja A/c Dr. To Raja's Capital A/c (For crediting commission to a partner, to partner's capital account)	50,000	 50,000
5.	Profit and Los Appropriation A/c Or To Commission to Raja A/c (For transferring commission paid to partners to Profit and Loss Appropriation	50,000	 50,000
6.	Interest on capital A/c Dr. To Kumar's capital A/c To Raja's capital A/c To Sanjay's Capital (For crediting interest on capital to partner's capital account)	72,000	 30,000 24,000 18,000

7.	Profit and Loss Appropriation A/c Dr. To Interest on capital A/c (For transferring interest on capital to profit and Loss Appropriation Account)	72,000	72, 000
8.	Kumar's capital A/c tDr. Raja's capital A/c Dr. Sanjay's capital A/c Dr To interest on drawings (For charging interest on drawings to partner's capital accounts	2,700 1,800 900	5,400
9.	Interest on drawings A/c Dr. To Profit and Loss Appropriation Ac/ (For transferring interest on drawings to Profit and Loss Appropriation Account)	5,400	5,400
10.	Profit and Loss Appropriation A/c Dr To Kumar's capital A/c To Raja's capital A/c To Sanjay 's capital A/c (For transferring Share of profit or Loss after appropriations	1,20,000	60,000 40,000 20,000

Dr. **Profit and Loss Appropriation** Cr.

Particulars	*Amount (Rs.)*	*Particulars*	*Amount (Rs.)*
Kumar's Salary Raja's Commission Interest On Capital Kumar 30,000 Raja 24,000 Sanjay 18,000	1,20,000 50,000 72,000	Net Profit Interest on Drawing : Kumar 2,700 Raja 1800 Sanjay 900	3,56,600 5,400
Profit transferred to capital A/c: Kumar 60,000 Raja 40,000 Sanjay 20,000	1,20,000		
	3,62,000		3,62,000

2. Sonia and Rajiv are partners sharing profits in the ratio of 3: 2 with capitals of ₹ 5,00,000 and ₹ 3,00,000 respectively. Interest on capital is agreed @ 6% p.a . Rajiv is to be allowed an annual salary of Rs. 25,000. During a year 2018-19 the profits prior to the calculation of interest on capital but after charging Rajiv's salary amounted to ₹ 1,25,000. A provision of 5% of the profit is to be made in respect of commission to the Manager. Prepare Profit and Loss Appropriation account showing the distribution of profit and the partner's capital accounts for the year endign March 31, 2019.

Profit and Loss Appropriation Account

Particulars	Amount (₹).	Particulars	Amount (₹).
Rajiv's Salary	25,000	Net Profit (before Rajiv's salary) and after manager commission [1,50,000-7,500]	1,42,500
Interest on capital Sonia 30,000 Rajiv 18000	48,000		
Profit transferred to capital A/c: Sonia 41,700 Rajiv 27,800	69,500		
	1,42,500		1,42,500

Partners Capital Account

Dr. Cr.

Date	Particulars	Sonia (Rs.)	Rajiv (Rs.)	Date	Particulars	Sonia (Rs.)	Rajiv (Rs.)
2019 Mar. 31	Bal. c/d	5,71,700	3,70,8 00	2018 Apr. 3	Bal. b/d	5,00,000	3,00,000
				2019 Mar. 31	Interest on capital	30,000	18,000
				Mar. 31	Salary		25,000
				Mar. 31	P&L app. (profit)	41,700	27,800
		5,71,700	3,70,800			5,71,700	3,70,800

2. Jagdeep and Kavita are partners sharing profits and losses in the ratio of 3 : 1. their capitals at the end of the financial yar 2018-2019 were ₹ 15,00,000 and ₹ 7,50,000. During the year 2018-2019, Jagdeep's drawings were ₹ 2,00,000 and the drawings of Kavita were ₹ 50,000, which had been duly debited to partner's capital accounts. Profit before charging interest on capital for the year was ₹ 1,60,000. The same has also been debited in their profit sharing ratio. Kavita had brought additional capital of ₹ 1,60,000 on October 1, 2018. Calcualte interest in capital @ 12% p.a. for the year 2018-2019

Particulars	Jagdeep (₹)	Kavita (₹)
Capital at the end	15,00,000	7,50,000
Add. Drawings during the year	2,00,000	50,000
Less: Share of profit (Credited)		(40,000)
Less: Additonal capital	(1,20,000)	(1,60,000)
	15,80,000	6,00,000

Interest on capital will be as ₹ 1, 89, 600 (12% of ₹ 15, 80,000) for Jagdeep and Rs, 81,600 for Kavita calculated as follows:

$$\left(6{,}00{,}000 \times \frac{12}{100}\right) + \left(1{,}600{,}000 \times \frac{12}{100} \times \frac{6}{12}\right) = 72{,}000+9{,}600 = ₹\ 81{,}600$$

4. Arun and Ajay are partners sharing profits and losses in the ration of 3:2 . Their capital accounts showed balance of ₹ 15,00,000 and

₹ 20,00,000 respectively on march 31, 2018. Show the treatment of interest on capital for the year ending march 31, 2019 in each of the following alternatives:

(a) if the partneresihp deed is silent as to the payment of interest on capital and the profit for the year is ₹ 5,00,000.

(b) if partnership deed provides for interest on capital @ 8% p.a. and the firm incurred a loss of ₹ 1,00,000 during the year.

(c) If partnership deed provides for interest on capital @ 8% p.a. and the firm earned a profit of ₹ 5,00,000; during the year.

(d) if the partnership deed provides for interest on capital @ 8% p.a. and the firm earned a profit of ₹ 1,40,000; during the year.

Ans. (a) In the absence of a specific provision in the Deed, no interest will be paid on the capital to the partner. The whole amount of profit will however, be distributed among the partners in their profit sharing ratio.

(b) As the firm has incurred lossed during the accounting year, no interest on capital will be allowed to any partner. The firm's loss will however be shared by the partners in their profit sharing ratio.

(c) Interest to Arun @ 8% on ₹ 15,00,000 = 1,20,000

Interest to Ajay @ 8% on ₹ 20,00,000 = 1,60,000

2,80,000

As the profit is sufficient to pay interest at agreed rate, the whole amount of interest on capital shall be allowed and the remaining profit amounting to ₹ 2,20,000 (₹ 5,00,000 - ₹ 2, 80,000) shall be shared by the partners in their profit sharing ratio.

(d) As the profit for the year is ₹ 1, 40,000, which is less than the amount of interest on capital due to partners i.e. ₹ 2, 80,000 (Rs 1, 20,000 for Arun and ₹ 1,60,000 for Ajay) , interest will be paid to the extent of available profit i.e. ₹ 1,40,000. Arun and Ajay will be credited with Rs . 60,000 and ₹ 80,000, respectively. Effectively this amounts to sharing the fir's profit in the ratio of interest on capital.

5. Kapil, a partner in a firm withdrew money during the year ending March, 31, 2019, from his capital account, for his personal use. Calculate interest in drawings in each of the following alternative situations, if rate of interest is 9 percent per annum.

(a) if he withdrew ₹ 30,000 per month at the beginning of the month.

(b) if an amount of ₹ 30,000 per month was withdrawn by him at the end of each month.

(c) if the amounts withdrawn were: ₹ 1, 20,000 on June 01, 2018, Rs 80,000; of August 31, ₹ 30,000; on September 30, 2018, ₹ 70,000, on November

30, 2018, and ₹ 60,000 on January 31, 2019.

(d) if he withdrew ₹ 3,00,000 per quarter at the beginning of the quarter.

(e) if he withdrew ₹ 3,00,000 per quarter at the end of the quarter.

(f) if he withdrew ₹ 3,00,000 during the year.

(g) if he withdrew ₹ 1,50,000 at the middle of the each quarter.

Ans. (a) 3,60,000 × 9/100 × 6.5/12 = ₹ 17,550

(b) 3,60,000 × 9/100 × 5.5/12= ₹ 14, 850

(c) Statements showing Calculation of Interest on Drawings (product method)

Date	Amount Withdrawn	Period (in months)	Product
June 01, 2018	1, 20,000	10	12, 00,000
August 31, 2018	80,000	7	5, 60,000
September 30, 2018	30,000	6	1,80,000
November 30, 2018	70,000	4	2,80,000
January 31, 2019	60,000	2	1,20,000
			23,40,000

Interest on drawings = $23,40,000 \times \frac{9}{10} \times \frac{1}{12}$ = ₹ 17, 550

(d) $12,00,000 \times \frac{9}{100} \times \frac{7.5}{12}$ = ₹ 67,500

(e) $12,00,000 \times \frac{9}{100} \times \frac{4.5}{12}$ = ₹ 40,500

(f) $3,00,000 \times \frac{9}{100} \times \frac{6}{12}$ = ₹ 13,500

(g) $6,00,000 \times \frac{9}{100} \times \frac{6}{12}$ = ₹ 27,000

6. Dinesh an Manish share profits and losses in the ratio of 3:2. They admit Nipun into their firm to 1/6 share in profits. Dinesh personally guaranteed that Nipun's share of profit, after charging interest on capital @ 10 percent per annum would not be less than ₹ 3,00,000 in any year. The capital provided was as follows: Dinesh ₹ 25,00,000, Manish ₹ 20,00,000 and Nipun ₹ 15,00,000. The Profit for the year ending March 31, 2019 amounted to ₹ 15,00,000 before providing interest on capital. Show, the Profit and Loss Appropriation Account if new profit sharing ratio is 3:2:1.

Profit and Loss Appropriation Account

Dr. Cr

Particulars	Amount (Rs,)	Particulars	Amount (Rs,)
Interest on capital: Dinesh 2,50,000 Manish 2,00,000 Nipun 1,50,000	6,00,000	Net Profit	15,00,000
Profit transferred to capital A/c: Dinesh 4,50,000 Less : share of deficiency 1,50,000 Manish Nipun 1,50,000 Add: deficiency recieved from Dinesh 1,50,000	 3,00,000 3,00,000 3,00,000		
	15,00,000		15,00,000

7. Priya, Deepa and Kashish are partner's sharing profits in the ratio of 5:4:1 Kashish is given a guarantee that her share of profits in any given year would not be less than ₹ 50,000. Deficiency , if any would be borne by Priya and Deepa equally. Profits for the year amounted to ₹ 4,00,000. Record necessary journal entries in the bools of the firm showing the distribution of profit.

Profit and Loss Appropriate Account

Particulars	**Amount (Rs)**	**Particulars**	**Amount (Rs)**
Profit transferred to capital A/c: Priya 2,00,000 Less: share of deficiency 5000 Deepa 1,60,000 Less: share of deficiency 5000	 1,95,000 1,55,000	Net Profit	4,00,000
Kashish 40,000 Add: deficiency received from Priya 5,000 Deepa 5000	50,000		
	4,00,000		4,00,000

8. On March, 31, 2019 the balance in the capital accounts of Sonu, Monu an Tony, after making adjustments for profits. drawing, etc. were ₹ 8,00,000. Rs, 6,00,000 and ₹ 4,00,000 respectively. Subsequently, it was discovered that interest on capital and interest on drawings had been omitted. The partners were entitled to interest on capital @ 5 p.a. The drawings during the year were Sonu ₹ 2,00,000; Monu ₹ 1,50,000 and Tony, ₹ 90,000. Interest on drawings, chargeable to partners were Sonu Rs, 5000, Monu ₹ 3600 and Tony ₹ 2000. The net profit during the year amount to ₹ 1,20,000, The Profit sharing ratio was 3:2:1. Record necessary adjustment entries.

Statement Showing Calculation of Capital at the Beginning

Particulars	Sonu (₹)	Monu (₹)	Tony (₹)
Capital at the end Add: drawings during the year Less: profit credited	8,00,000 2,00,000 (60,000)	6,00,000 1,50,000 (40,000)	4,00,000 90,000 (20,000)
Opening capital	9,40,000	7,10,000	4,70,000
Interest on capital @ 5 % p.a	47,000	35,500	23,500

Statement Showing Adjustment

Particulars	Sonu (₹)	Monu (₹)	Tony (₹)	Firm (₹)
Profit already credited now reversed	60,000(dr.)	40,000(dr.)	20,000(dr.)	1, 20,000(cr.)
Interest on capital	47,000 (cr.)	35,500 (cr.)	23,500 (cr.)	1,06,000 (dr.)
Interest on drawings	5,000 (dr.)	3,600 (dr.)	2,000 (dr.)	10,600 (cr.)
Net Profit (bal. Fig.)	12,300 (cr.)	8,200 (cr.)	4,100 (cr.)	24,600 (dr.)
Net effect	5,700 (dr.)	100 (cr.)	5,600 (cr.)	

Journal

Date	Particulars	Dr.(₹)	Cr. (₹)
	Sonu's capital Ac/ Dr. To Monu's Capital a/c To Tony's capital a/c (being adjustment entry made)	5,700	 100 5,600

9. Aanchal, Aarav and Avika form a partnership firm , sharing profits in the ratio of 3:2:1, subject to the following:

   (i) Avika's share in the profits, guranteed to be not less than ₹ 1,50,000 in any year.

   (ii) Aarav gives gurantee to the effect that gross fee earned by her for the firm shall be equal to her average gross fee of the proceeding five years, when she was carrying on profession alone (which is ₹ 2,50,000). The net profit for the year ended March 31, 2019 is ₹ 7,50,000. The gross fee earned by Aarav for the firm was ₹ 1, 60,000. Your are required to show Profit and Loss Appropriation Account (after giving effect to the alone).

Dr. Profit and Loss Appropriation Account Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
Profit trnasfered to capital A/c: Aanchal 4, 20,000 Less: share of deficiency 6,000	4, 14,000	Net Profit	7,50,000
		Aarav's capital A/c (shortage of gross fees)	90,000
Aarav 2, 80,000 Less: share of deficiency 4,000	2,76,000		
Avika 1,40,000 Add : deficiency received from Aanchal 6,000 Aarav 4,000	1,50,000		
	8,40,000		8,40,000

10. Mudit, Sudhir and Uday are partners in a firm sharing profits in the ratio of 3 : 1 : 1. Their fixed capital balances are ₹ 4,00,000, ₹ 1,60,000 and ₹ 1,20,000 respectively. Net profit for the year ended 31st March, 2018 distributed amongst the partners was ₹ 1,00,000, without taking into account the following adjustments:

(a) Interest on capital @ 2.5% p.a.;

(b) Salary to Mudit ₹ 18,000 p.a. and commission to Uday ₹ 12,000

(c) Mudit was allowed a commission of 6% of divisible profit after charging such commission.

Pass a rectifying journal entry in the books of the firm. Show workings clearly.

Sol.

Adjustment Table

Particulars	Mudit's		Sudhir's		Uday's		Firm's	
	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)
Profit given	60,000	–	20,000	–	20,000	–	–	1,00,000
Interest on Capital	–	10,000	–	4,000	–	3,000	17,.000	–
Salary	–	18,000	–	–	–	–	18,000	–
Commission	–	3,000	–	–	–	12,000	15,000	–
Profit to be credited	–	30,000	–	10,000	–	10,000	50,000	–
Total	60,000	61,000	20,000	14,000	20,000	25,000		

Mudit's Commission = (53,000 × 6/106) = ₹ 3,000

Rectifying Journal Entry

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Sudhir's Current A/c Dr.		6,000	
	To Mudit's Current A/c			1,000
	To Uday's Current A/c			5,000
	(Being interest on capital, salary and commission to partners omitted in distributing profits, now adjusted)			

11. The partners of a firm, Alia, Bhanu and Chand distributed the profits for the year ended 31st March, 2017, ₹ 80,000 in the ratio of 3 : 3 : 2 without providing for the following adjustments.

(a) Alia and Chand were entitled to a salary of ₹ 1,500 each p.a.

(b) Bhanu was entitled for a commission of ₹ 4,000.

(c) Bhanu and Chand had guaranteed a minimum profit of ₹ 35,000 p.a. to Alia any deficiency to borne equally by Bhanu and Chand.

Pass the necessary Journal entry for the above adjustments in the books of the firm. Show workings clearly.

Sol.

Adjustment Table

Particulars	Alia's		Bhanu's		Chand's		Firm's	
	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)	Dr. (₹)	Cr. (₹)
Profit Given	30,000	–	30,000	–	20,000	–	–	80,000
Salary	–	18,000	–	–	–	18,000	36,000	–
Commission	–	–	–	4,000	–	–	4,000	–
Profit to be credited	–	35,000	–	5,000	–	–	40,000	–
Total	30,000	53,000	30,000	9,000	20,000	18,000		

Divisible profits = ₹ 80,000 – ₹ 36,000 – ₹ 4,000 = ₹ 40,000

Alia's Share = ₹ 15,000 + ₹ 20,000 = ₹ 35,000

Bhanu's Share = ₹ 15,000 – 10,000 = ₹ 5,000

Chand's share = ₹ 10,000 – 10,000 = nil

Rectifying Journal Entry

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
	Bhanu's Capital A/c Dr.		21,000	
	Chand's Capital A/c Dr.		2,000	
	To Alia's Capital A/c			23,000
	(Being salary, commission to partners omitted i n distribution of profit, guarantee to Alia, now adjusted)			

12. Following is the extract of the Balance Sheet of, Neelkant and Mahadev as on March 31, 2017:

Balance Sheet as at March 31, 2017

Liabilities	Amount (₹)	Assets	Amount (₹)
Neelkant's Capital	10,00,000	Sundry Assets	30,00,000
Mahadev's Capital	10,00,000		
Neelkant's Current Amount	1,00,000		
Mahadev's Current Account	1,00,000		
Profit and Loss Appropriation (March 2017)	8,00,000		
	30,00,000		30,00,000

During the year Mahadev's drawings were ₹ 30,000. Profits during 2017 is ₹ 10,00,000. Calculate interest on capital @ 5% p.a. for the year ending March 31, 2017.

Sol. Interest on Capital:

Neelkant's $10,00,000 \times \frac{5}{100}$ = ₹ 50,000

Mahadev's $10,00,000 \times \frac{5}{100}$ = ₹ 50,000

Note: In this question, as the balances of both Partner's Capital Account and of Partner's Current Account are mentioned, so it has been assumed that the capital of the partners is fixed

As we know, when the capital of the partners is fixed, drawings and interest on capital does not affect the capital balances of the partne₹ Rather, it would affect their current account balances. Therefore in this case, capital at the beginning (ie opening capital) and capital at the end (i.e. closing capital) of the year would remain same. Thus, the interest on capital is calculated on fixed capital balances (given in the Balance Sheet of the question).

13. A & B are partners in the ratio of 3 : 2 The firm maintains fluctuating capital accounts and the balance of the same as on 31-03 2020 amounted to ₹ 1,60,000 and ₹ 1,40,000 for A and B respectively Their drawings during the year were Rs 30,000 each As per partnership deed interest on capital @10% pa on opening capitals had been provided to them. Calculate opening capital of partners given that their profits were ₹ 90,000. Show your workings clearly.

Sol. **Calculation of Opening Capital**

Particulars	A	B
Closing Capital	1,60,000	1,40,000
Add: Drawings	30,000	30,000
Less Profits	37,800	25,200
	1,52,200	1,44,800
Less: Interest on Capital	13,836	13,164
Opening Capital	1,38,364	1,31,636

Total closing capital (of A and B) = 1,60,000 + 1,40,000 = ₹ 3,00,000

Add: Total Drawing (of A and B) = ₹ 60,000

Less: Profits (including interest on Capital) = ₹ 90,000

Total capital in the begining of the year = ₹ 2,70,000

Interest on Capital ₹ $2,70,000 \times \frac{10}{100}$ = ₹ 27,000

Divisible profits = 90,000 – 27,000 = ₹ 63,000

Accounting for Partnership Firms - Fundamentals

MCQ/OBJECTIVES

Fill In the Blanks

1. In the absence of the date of withdrawal, interest should be charged for ________ month on the whole amount.
2. If partner's capital is fixed; interest on drawing will be recorded on________
3. A and B are Partne. A drew ₹ 16,000 .If the rate of Interest on Drawing is 12% per annum then ________ will amount of interest on drawing .
4. A drew ₹ 30,000 during the year. If the rate of Interest on Drawing is 10% then ________ will be the amount of Interest on Drawing.
5. According to Section 464 of the Companies Act, 2013, the Central Government has the authority to prescribe maximum number of partners in a firm however the prescribed number of partners cannot be more than________
6. As per Rule 10 of the Companies Rules (Miscellaneous) 2014, the Central Government has prescribed the maximum number of partners in a firm to be________
7. Each partner is the________ of the firm as well as of the other partne₹
8. _______ is an extension of Profit & Loss A/c.
9. Salary or Commission to a partner is a/an ________ out of profit.
10. Arjun, Ajay and Vijay are partners in the ratio of 5: 4: 3. Arjun given to Vijay a guarantee of minimum ₹ 10,000 profit. For the year ending 31st March, 2021, firm's profit is ₹ 28,800. Arjun's share in profit will be ________

True /False

1. Section 4 of the Indian Partnership Act, 1932, defines partnership.
2. It is not necessary that every partner should actively participate in the conduct of the business.
3. It is not legally compulsory for every firm to have a partnership deed.
4. A charge is debited to Profit and Loss A/c only when firm incurs profit.
5. At the end of the year, if the current account shows debit balance, it will be shown in the 'liability' side of the balance sheet.
6. Fixed Capital Account can never show a debit balance.

7. One of the partners in a partnership firm has withdrawn ₹9 000 at the end of each quarter, throughout the year. Amount of Interest on drawings for the respective partner is ₹ 810 at the rate of 6% per annum.

8. In case of fixed capitals, drawings made by a partner will be recorded on the debit side of the Current Accounts.

9. A partner can be exempted from sharing the losses in a firm if all the partner agrees to it.

10. Private assets of the partners cannot be used to meet the liability of the firm in case firm's assets are insufficient to meet its liabilities.

MULTIPLE CHOICE QUESTIONS

1. Find the odd one out:

   a) Interest on Loan
   b) Partner Salary
   c) Rent paid to Partner's
   d) Managers Commission

2. A, B, and C are partner's sharing profits in the ratio of 5:3:2. According to the partnership agreement C is to get a minimum amount of ₹ 20,000 as his share of profits every year. The net profit for the year ended 31st March, 2019 amounted to ₹ 80,000. How much amount contributed by A in favour of C?

   a) ₹ 1,500
   b) ₹ 1,250
   c) ₹ 2,500
   d) ₹ 4,000

3. The relation of partner with the firm is that of:

   a) An Owner
   b) An Agent
   c) An Owner and an Agent
   d) Manager

4. Arun and Anugya are Partne₹ They do not have any Partnership agreement (Partnership deed) Arun has provided a Capital of ₹ 70,000 whereas Anugya has provided ₹ 15,000 only as Capital. Anugya however, has provided ₹ 20,000 as loan to the Firm. What interest (if any) will be given to Arun and Anugya?

   a) Arun — ₹ 7,000 and Anugya - ₹ 1,500

   b) Anugya is entitled to claim interest on his loan of ₹20,000 @ 6% p.a. and Arun - Nil

   c) Arun - Nil and Anugya - ₹ 3,500

   d) Anugya - Nil and Arun - Nil

5. X, Y and Z are Partners in a Firm. At the time of division of profit for the year, there was dispute between the Partne₹ Profits before interest on Partner's Capital were ₹ 45,000. Y demands interest @ 24% p.a. on his loan of ₹ 2,40,000. There was no agreement on this point. Share of profit of X, Y and Z will be:

   a) ₹ 15,000 to each Partner

   b) ₹ 12,600 for X and Z & Y ₹ 19,800

   c) X - ₹10,200, Y - ₹ 39,000 and Z - ₹ 10,200

   d) ₹ 10,200 to each Partner

6. Mohit and Rajesh are partners in the ratio of 3 ; 2. Their capitals are ₹ 4,00,000 and ₹ 2,00,000 respectively. Interest on capitals is allowed @ 8% p.a. Firm incurred a loss of ₹ 1,20,000 for the year ended 31st March 2021. Interest on Capital will be:

   (a) Mohit ₹ 32,000; Rajesh ₹ 16,000

   (b) Mohit ₹ 16,000; Rajesh ₹ 8.000

   (c) Mohit ₹ 28,400; Rajesh ₹ 19,000

   (d) No Interest will be allowed

7. X. Y. and Z are equal partners with fixed capitals of ₹ 1.00,000, ₹ 1,50.000 and ₹ 2.00.000 respectively. After closing the accounts for the year ending 31 st March, 2020 it was discovered that interest on capitals @ 8% p.a. was omitted to be provided. In the adjusting entry :

   a) Dr. X and Cr. Y by ₹ 4,000

   b) Cr. X and Dr. Z by ₹ 4,000

   c) Dr. X and Cr. Z by ₹ 4,000

   d) Cr. X and Dr. Y by ₹ 4,000

8. A, B, and C sharing profits in the ratio of 2 : 1: 1 have fixed capitals of ₹ 8,00,000, ₹' 6,00,000 and ₹ 4,00,000 respectively. After closing the accounts for the year ending 31st March, 2020 it was discovered that interest on capitals was provided @ 6% instead of 8% p.a. In the adjusting entry:

   a) Cr. A ₹ 2,000; Dr. B ₹ 3,000 and Cr. C ₹ 1,000

   b) Dr. A ₹ 1,000; Cr. B ₹ 3,000 and Dr. C ₹ 2,000

   c) Cr. A ₹ 1,000; Dr. B ₹ 3,000 and Cr. C ₹ 2,000

   d) Dr. A ₹ 2,000; Cr. B ₹ 3,000 and Dr. C ₹ 1,000

9. If fixed amount is withdrawn by a partner on the first day of each quarter, interest on the total amount is charged for______months.

   a) 4.5 months b) 6 months

   c) 7.5 months d) 3 months

10. On 1st January 2021, a partner advanced a loan of ₹ 1,00,000 to the firm. In the absence of agreement, interest on loan on 31st March, 2021 will be

   a) ₹ 9,000 b) ₹ 3,000

   c) ₹ 6,000 d) ₹ 1,500

Matching Questions

1. Match the following if partnership deed is absent/silent.

Description	**Options**
1 Interest on partners' capitals.	a.@ 6% per annum.
2 Interest on partners' drawings.	b. Not allowed
3 Partners share profits and losses	c. Not Charged
4 Interest on partner's loan	d. Equally

2. Match the following items:

Description	**Options**
1. Interest on drawings of equal amounts drawn on the first day of every month	a. 7.5 months
2. Interest on drawings of equal amounts drawn on the last day of every month	b. 6 months
3. Interest on drawings of equal amounts drawn on the first day of every quarter	c. 5.5 months
4. Interest on drawings of equal amounts drawn on the last day of every quarter	d. 6.5 months
5. Interest on drawings of equal amounts drawn on the middle of every quarter	e. 4.5 months

3. Match the following

Description	**Options**
1 Drawing against profits	(a) Debited to partner's capital account
2 Drawing against capital	(b) Credited to partner's capital account

	(c) Debited to drawing account
	(d) Credited to drawing account

4. Match the following

Description	**Options**
1 A entitled to a salary of Rs 10,000 per annum and commission of 10 % of the Net profit after charging his salary but before charging his commission . The Net profit Rs 2,30,000. What will be the amount of A's Commission.	(a) Rs 23,000
2 B entitled to commission of 10 % on net profit after charging his commission . The Net profit Rs 2,20,000 what will be the amount of B's Commission .	(b) Rs 22,000
	(c) Rs 20,000
	(d) Rs 25,000
	(e) Rs 27,000

5. Match the following

Description	**Options**
1. Charge against profit	a) Rent paid to a partner
2. Appropriation of profit	b) Interest on partners loan
	c) Managers Commission
	d) Partners Salary
	e) Interest on partners' Capital

ANSWERS

Fill In the Blanks

Q.NO.	ANSWER
1.	6 (Six)
2.	Partner's Current A/c
3.	₹ 960
4.	₹ 3,000
5.	100
6.	50

7. Agent

8. Profit & Loss Appropriation A/c

9. Appropriation

10. ₹ 9,200

True /False

Q.NO.	ANSWER
1.	T
2.	T
3.	T
4.	F
5.	F
6.	T
7.	T
8.	T
9.	T
10.	F

MULTIPLE CHOICE Questions

Q.NO.	ANSWER
1.	b
2.	c
3.	c
4.	b
5.	d
6.	d
7.	c
8.	d
9.	c
10.	d

Matching Questions

Q.NO.	ANSWER
1.	[l-b;2-c;3-d;4-a]
2.	[l-d;2-c;3-a;4-e;5-b]
3.	[l-c;2-a]
4.	[l-b;2-c]
5.	[1 - a,b and c; 2 -d and e]

Work Sheet on Accounting for Partnership Firms Fundamentals

Q.1 Does partnership firm has a separate legal entity? Give reason in support of your answer.

Q.2 A group of 55 persons want to form a partnership business in India. Can they do so? Give reason in support of your answer.

Q.3 Why is it necessary to have a partnership deed?

Q.4 Arun and Anugya are childhood friends. Arun is a consultant whereas Anugya is an architect. They contributed equal amounts and purchased a building for ₹5 crores. After a year, they sold it for ₹8 crores and shared the profits equally. Are they doing the business in partnership? Give reason in support of your answer.?

Q.5 Do all forms of business organisation prepare a Profit and Loss Appropriation Account?

Q.6 List any two circumstances under which the fixed capital of partners may change.

Q.7 If the Partners' Capital Accounts are fixed, where will you record the following items: (a) Salary payable to a partner (b) Drawings made by a partner (c) Fresh capital introduced (d) Shares of profit earned by a partner.

Q.8 Can a partner be exempted from sharing the losses in a firm? If yes, under what circumstances?

Q.9 A partnership deed provides for the payment of interest on capital but there was a loss instead of profit during the year 2020-21. At what rate will interest on capital be allowed?

Q.10 Distinguish between 'Fixed Capital Account' and 'Fluctuating Capital Account'

Q.11 A and B are partners without any partnership agreement. They have difference of opinion on the following points. State who is correct in each case,

(a) A wants a salary of ₹ 12,000 p.m. as he works for the business and B does not.

(b) A has invested three times the capital invested by B. So he wants interest @ 6% p.a. B objects to it.

(c) B has given a loan of ₹ 8,00,000 to firm, without any agreement on interest. B wants interest @ 9% p.a. (Bank rate) whereas A wants to pay interest @ 6%.

(d) A wants to distribute profits in the ratio of capitals i.e., 3 : 1. B says that the profits should be divided equally,

(e) A wants to introduce his son C into his business, B has objection to it.

Q.12. The partners P and Q decided to appropriate the profits of the firm on the following terms :

(a) Interest on capital is payable @ 10% p.a.

(b) Both P and Q will get remuneration as : P — ₹3,000 per month. Q —₹ 40,000 per annum,

(c) Interest on P's Loan @ 6% p.a. which was advanced on 1-9-2019 and the amount being ₹ 2,00,000.

(d) Interest on drawings @ 2% irrespective of period. The amount of drawings being P — ₹ 1,20,000 and Q — ₹1, 60,000.

(e) Profits will be shared in the ratio 3 : 2.

(f) One-tenth of divisible profit is to be transferred to General Reserve. For the year ended 31-3-2020 the profit of the firm was ₹ 3,09,400. On 1-4-2019 the capital balances of P and Q were ₹ 3,20,000 and ₹ 4,00,000 respectively. Pass necessary journal entries and prepare Profit and Loss Appropriation A/c on that date in the books of the firm.

Q.13 X and Y are partners with capital of ₹60,000 and ₹20,000 respectively on 1st April, 2019. The net profit (before taking into account the provisions of the Deed) for the year ended 31st March, 2020 was ₹24,500. Interest on capitals is to be allowed at 6% per annum. Y is entitled to a salary of ₹6,000 per annum. The drawings of the partners were ₹6,000 and ₹8,000; the Interest for X being ₹200 and Y ₹100. Show how the profit will be divided between X and Y and also show the Capital Accounts

(i) If the capitals are fluctuating and

(ii) if the capitals are fixed.

Q.14 Nipun withdrew ₹30,000 per month from the firm for his personal use during the year ending March 31, 2021. Calculate interest on drawings at the rate of 10% p.a.

(a) When the amount is withdrawn at the beginning of each month,

(b) When the amount is withdrawn at the end of each month,

(c) When the amount is withdrawn in the middle of each month,

(d) When the amount is withdrawn at the beginning of each quarter,

(e) When the amount is withdrawn at the end of each quarter,

(f) When the amount is withdrawn in the middle of each quarter.

Q.15 Anu withdrew the following amounts from her firm, for personal use during the year ending March 31, 2020. Calculate interest on drawing, if the rate of interest to be charged is 7% p.a.

DATE	AMOUNT (₹)
April 1, 2019,,	48,000
June 30, 2019	45,000
October 31, 2019	30,000
December 31, 2019	42,000
March 1, 2020	33,000

Q.16 Sonu, Monu and Tony are partners with capital on Dec. 31, 2019 as ₹80,000. ₹70,000 and ₹50,000 respectively. Profit already divided for the year was ₹1,50,000. Drawings during the year had been ₹5,000; ₹8,000; ₹17,000 respectively. Profit sharing ratio of Sonu, Monu and Tony is 4 : 5 : 6. At the end of year, it was found that interest on capital @ 10% p.a. had not been provided. Calculate the interest on capital.

Q.17 Kapil and Ruby are partners showing profits in the ratio 3 : 2. On April, 2019 they had capitals of ₹4,00,000 and ₹4,40,000. Accoording to partnership deed.

(a) Kapil will get a half yearly salary of ₹ 9,000 and Ruby will get a quarterly salary of ₹6,000.

(b) Interest on capital will be allowed @ 6% p.a.

(c) Kapil will be allowed a commission of 5% of profits after charging salary and interest on capital but before commission,

(d) Ruby will be allowed a commission of 10% after charging all salary, interest on capital and commissions. Pofits for the year ended 31st March, 2020 amounted to ₹3,12,000. Prepare Profit and Loss Appropriation A/c.

Q.18 X, Y and Z were partne₹ Their Fixed capitals were ₹30,000; ₹20,000 and ₹10,000 respectively. According to the Partnership Deed, they were entitled to an interest on capital @ 5% p.a. In addition Y was also entitled to draw a salary of ₹ 500 per month. Z was entitled to a commission of 5% on the profits after charging the interest on capital, but before charging the salary payable to Y. The net profits for the year were ₹ 30,000, distributed in the ratio of their capitals without providing for any of the above adjustments. The profits were to be shared in the ratio of 2 : 2 :1. Pass the necessary adjustment entry showing the workings clearly.

Q.19 Maanika, Bhavi and Komal are partners sharing profits in the ratio of 6:4:1. Komal is guaranteed a minimum profit of ₹ 2,00,000. The firm incurred a loss of ₹ 22,00,000 for the year ended 31st March, 2018. Pass necessary journal entry regarding deficiency borne by Maanika and Bhavi.

Q.20 Show the division of profit among the partners in the following cases:

(a) A and B are partners sharing profits in the ratio of 3 : 2. From 1st January, 2019 they admit C into partnership giving him l/5th share of the profits with a guaranteed profit of ₹ 6,000 minimum. A and B as between themselves continued to share profits as before. Profits of the firm for 2019 were ₹ 24,000.

(b) X and Y share profits and losses in the ratio of 3 : 2. As from 1st January, 2019. They admit Z who is to have a tenth share of the profits with a guaranteed minimum of ₹7,500. X and Y continued to share profits as before but agree to suffer any excess over l/10th going to Z. The profits of the firm in respect of the year are ₹50,000.

(c) Z, the manager, was admitted by X and Y with a l/3rd share in the profits and a salary of ₹3,000 p.a. X and Y were sharing profits in the ratio of 3 : 2. Z, as manager, was getting a salary of ₹9,000 p.a. and commission of 5% on net profit after charging such commission and salary.

The excess of Z's share in the profits over his remuneration (drawn in the capacity of manager) is to be borne by X and Y in the ratio of 2 : 3. Profits for the year before charging commission, but after charging salary, were ₹42,000.

Q.21 Ravi and Mohan were partners in a firm sharing profits in the ratio of 7 : 5. Their respective fixed capitals were : Ravi— ₹10,00,000 and Mohan— ₹7,00,000. The Partnership Deed provided for the following :

(i) Interest on capital @ 12% p.a.

(ii) Ravi's salary ₹6,000 per month and Mohan's salary ₹60,000 per year.

The profit for the year ended 31.3.2020 was ₹5,04,000 which was distributed equally, without providing for the above. Pass an adjustment entry.

Q.22 The partners of a firm distributed the profits for the year ended 31st March, 2021, ₹ 90,000 in the ratio of 3 : 2 : 1 without providing for the following adjustments:

(i) X and Z were entitled to a salary of ₹1,500 p.a.

(ii) Y was entitled to a commission of ₹4,500.

(iii) Y and Z had guaranteed a minimum profit of ₹35,000 p.a to X.

(iv) Profits were to be shared in the ratio of 3 : 3 : 2. Pass the necessary Journal entry for the above adjustments in the books of the firm.

Q.23 A, B and C were partners in a firm. On 1st April 2018 their fixed capitals stood at ₹50,000, ₹25,000 and ₹25,000 respectively. As per the provisions of the partnership deed :

(a) B was entitled for a salary of ₹5,000 p.a.

(b) All the partners were entitled to interest on capital at 5% p.a.

(c) Profits were to be shared in the ratio of capitals. The net profit for the year ending 31.3.2019 of ₹33,000 and 31.3.2020 of ₹45,000, was divided equally without providing for the above terms. Pass an adjustment Journal entry to rectify the above error.

Q.24 Rajiv and Sanjeev were partners in a firm. Their Partnership Deed provided that the profits shall be divided as follows : First ₹20,000 to Rajiv and the balance in the ratio of 4 : 1. The profits for the year ended 31st March, 2021 were ₹60,000 which had been distributed among the partne₹ On 1st April, 2020 their capitals were Rajiv ₹90,000 and Sanjeev ₹80,000. Interest on capital was to be provided @ 6% p.a. While preparing the Profit & Loss Appropriation Account interest on capital was omitted. Pass necessary rectifying entry for the same. Show your workings clearly.

Q.25 Mudit, Sudhir and Uday are partners in a firm sharing profits in the ratio of 3 : 1 : 1. Their fixed capital balances are ₹4,00,000, ₹1,60,000 and ₹1,20,000 respectively. Net profit for the year ended 31st March, 2018 distributed amongst the partners was ₹1,00,000, without taking into account the following adjustments :

(a) Interest on capitals @ 2.5% p.a.;

(b) Salary to Mudit ₹18,000 p.a. and commission to Uday ₹12,000

(c) Mudit was allowed a commission of 6% of divisible profit after charging such commission. Pass a rectifying journal entry in the books of the firm. Show workings clearly.

Q.26 On March 31, 2021 after the close of books of accounts the Capital Accounts of A, B and C stood at ₹50,000, ₹40,000 and ₹25,000 respectively. The profits of ₹42,000 were divided equally between them. Later on it was discovered that interest on capital @ 5% p.a. had been omitted. The partners shared profits in the ratio 2:2:1. Pass necessary journal entry.

Q.27 P, Q and R were partners in a firm having fixed capitals of ₹80,000; ₹90,000 and ₹1,00,000 respectively. They share profits in the ratio 5:3:2. During the year 2020-2021 interest on capital was allowed @ 12% p.a. instead of 10% p.a. Q and R noticed the error and brought it to the attention of P. You are required to pass an adjustment entry to rectify the above

Q.28 A, B and C were partners in a firm sharing profits and losses in the ratio 5 : 3 : 2. On April, 2020 their capitals were ₹1,50,000; ₹1,20,000 and ₹1,00,000 respectively. For the year ended 31st March, 2021, interest on capital was credited to them @ 9% p.a. instead of 12% p.a. Give rectifying journal entry.

WORK SHEET ANSWERS

Q.NO.	ANSWER
11	(a) B; (b) B; (c) A; (d) B; (e) B.
12	Share of Profit P ₹86,400 Q ₹57,600
13	Profit transferred to : X's Capital ₹7,000 Y's Capital ₹7,000 (i) Fluctuating Capital Method: X's Capital A/c balance ₹64,400; Y's Capital A/c balance ₹30,100 (ii) Fixed Capital Method X's Capital A/c balance ₹60,000; Y's Capital A/c balance ₹20,000 Fixed Capital Method X's Current A/c balance ₹4,400; Y's Current A/c balance ₹10,100
14	a- ₹19,500; b- ₹16,500, c- ₹18,000, d-₹22,500, e-₹13,500, f-₹18,000
15	₹7525
16	Sonu ₹4500, Monu ₹2800, Tony ₹700
17	(Share of profit Kapil- ₹1,13,792; Ruby- ₹75,862)
18	X's current A/c Dr. 5640
	To Y's current A/c 4860 To Z's Current A/c 780
19	Maanika's Capital A/c Dr. 2,40,000 Bhavi's Capital A/c Dr 1,60,000 To Komal's Capital A/c 4,00,000

20	(a) DIVISION OF PROFIT A's share ₹11,520 – 720 = ₹10,800 B's share ₹7,680 – 480 = ₹7,200 C's share = ₹ 6,000 Total = ₹24,000
	(b) X's share ₹25,500 Y's share ₹17,000 Z's share ₹7,500
	(c) X = ₹20,800 (24,000 – 3,200) Y = ₹ 11,200 (16,000 – 4,800) Z = ₹19,000 (including salary)
21	Mohan's current A/c Dr. 38,000 To Ravi's current A/c 38,000
22	X's capital A/c Dr. 8,500
	To Y's capital A/c 5,500 To Z's capital A/c 3,000
23	C's current A/c Dr. 9,000
	To A's cur rent A/c 8,000 To B's Current A/c 1,000
24	Rajiv's capital A/c Dr. 2,760 To Sanjeev's capital A/c 2,760
25	Sudhir's current A/c Dr. 6,000
	To Mudit's current A/c 1,000 To Uday's Current A/c 5,000
26	Cr. A₹3,140; B ₹2,640 and Dr. C ₹5,780
27	Current A/c's : Cr. P₹I,100; Dr. Q ₹180; Dr. R ₹920
28	Dr. A₹1,050; Cr. B₹270 and Cr. C₹780

Assertion and Reason Type Questions

1. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): Transfer to reserves is shown in P&L Appropriation A/c

Reason (R): Reserves are charge against the profits

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong.

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct

(d) Both (A) and (R) are wrong

2. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R)

Assertion (A): A partnership firm has no separate legal entity, apart from the partners constituting it.

Reason (R): Partner's private assets can also be used for paying off the firm's debts.

In the context of the above two statements, which of the following is correct?

Codes:

(a) Both (A) and (R) are correct and (R) is the correct reason of (A)

(b) Both (A) and (R) are correct but (R) is not the correct reason of (A).

(c) Only (R) is correct.

(d) Both (A) and (R) are wrong

3. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): The Partnership Act does not require that the agreement must be in writing.

Reason (R): The clauses of partnership deed can be altered with the consent of all the partners.

Codes:

(a) Both (A) and (R) are true, but (R) is not the explanation of (A).

(b) Both(A) and (R) are true and (R) is a correct explanation of (A).

(c) Both (A) and (R) are false.

(d) (A) is false, but (R) is true.

4. Given below are two statements is labelled as Assertion (A) and the other labelled as Reason (R)

Assertion (A): No partner is entitled to claim any interest on the amount of capital contributed by him in the firm as a matter of right

Reason (R): Interest can be allowed when it is expressly agreed to by the partners.

in the contest of the above statements, which one of the following correct?

Codes:

(a) (A) a correct, but (R) wrong

(b) Both (A) and (R) are correct

(c) (A) wrong but (R) is sect

(d) Both (A) and (R) are wrong

5. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): in the absence of any instruction, the capital account should be prepared by fluctuating capital method

Reason (R): Under the fluctuating capital method only one account, i.e. capital account is maintained for each partner.

In the context of the above two statements, which of the following is correct?

Codes:

(a) Both (A) and (8) are correct and (R) is the correct reason of (A).

(b) Both (A) and (R) are correct but (R) is not the correct reason of (A)

(c) Only (R) is correct

(d) Both (A) and (B) are wrong

6. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): If the partnership deed is silent, the firm's profits and losses are to be shared equally by all the partners.

Reason (R): Profit and Loss Appropriation Account is merely an extension of the Profit and Loss Account of the firm.

Codes:

(a) Both (A) and (R) are true, but (R) is not the explanation of (A).

(b) Both(A) and (R) are true and (R) is a correct explanation of (A).

(c) Bath (A) and (R) are false.

(d) (A) false, but (R) is true.

7. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (A):

Assertion (A): If partnership deed is silent in respect of certain aspects, the relevant provisions of the Indian Companies Act become applicable.

Reason (R): in the absence of partnership deed, if any partner has given some loan to the firm, he is entitled to interest on amount 6% per annum.

In the contest of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong.

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct.

(d) Both (A) and (R) are wrong.

8. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): The fixed capital accounts always show a credit balance.

Reason (R): The fluctuating capital accounts may sometimes show a debit balance.

In the context of the above two statements, which of the following is correct?

Codes:

(a) Both (A) and (R) are correct and (R) is the correct reason of (A)

(b) Both (A) and (R) are correct but (R) is not the correct reason of (A).

(c) Only (R) is correct.

(d) Both (A) and (R) are wrong.

9. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): The Central government has prescribed the maximum number of partners in a firm to be 50,

Reason (R): By virtue of Section 454 of the Companies Act 2013, the Central Government is empowered to prescribe maximum number of partners in a firm but the number of partners cannot be more than 100

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct

(d) Both (A) and (R) are wrong

10. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): Rohit, and Sachin jointly purchase a plot of land they become the joint owners of the property and not the partners.

Reason (R): Mere co-ownership of a property does not amount to partnership.

in the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (K) is wrong

(b) Both (A) and (R) are correct.

(c) (A) is wrong but (R) is correct.

(d) Both (A) and (R) are wrong

Answer

1. (a)	2. (b)	3. (a)	4. (b)	5. (b)
6. (a)	7. (c)	8. (b)	9. (b)	10. (b)

Case Study Based Questions

FUNDAMENTAL OF PARTNERSHIP

Read the following information carefully and answer the questions 1 to 5 that follow:

X and Y are partners in the ratio of 3 : 2. Their capital balances as on 1st April 2020 amounting to ₹2,00,000 each. On 1st February, 2021, X contributed an additional capital of 1,00,000. Following are the terms of deed:

(a) Interest on capital @6% per annum

(b) Interest on drawings @ 8% per annum.

(c) Salary to X ₹ 1500 per month

(d) Commission to Y @10% on net profit after charging interest on capital, salary and his commission.

Drawings of the partners were ₹ 20,000 and ₹ 30,000 respectively during the year

Net profit earned by the firm was ₹ 2,08,000

Choose the correct option based on the above information:

1. What is the amount of Interest on capitals of X and Y?

(a) ₹ 12,000 each

(b) ₹ 12,000 to X and ₹ 13,000 to Y

(c) ₹ 13,000 to X and ₹ 12,000 to Y

(d) None of the above

2. What is the amount of interest on drawings of X and Y?

(a) ₹ 1200 and ₹ 1800 respectively

(b) ₹ 800 and ₹ 1200 respectively

(c) ₹ 1200 and ₹ 800 respectively

(d) ₹ 1600 ₹ 2400 respectively

3. What is the amount of commission payable to Y?

(a) ₹ 15000 (b) ₹ 16500

(c) ₹ 20800 (d) None of these

4. What is X's share in the net divisible profit?

(a) ₹ 124400 (b) ₹ 83600

(c) ₹ 91200 (d) ₹ 60800

5. What will be the closing capital of X after all adjustments?

(a) ₹ 422200 (b) ₹ 401400

(c) ₹ 300000 (d) ₹ 423000

ANSWER:

Q. NO.	ANSWER WITH EXPLANATION
1.	(c) : IOC to X = (2,00,000*6/100) + (1,00,000*6/100*2/12) = 13,000 IOC to Y = 2,00,000*6/100 = 12,000
2.	(b) : IOD will be calculated for an average period of six months since time of drawings is not given.
3.	(a) : 2,08,000 – 13,000 – 12.000 (OC) – 18,000 (salary) = 1,65,000*10/110 = 15,000
4.	(c) : Divisible profit = 2,08,000 (NP) + 800 + 1,200 (IOD) – 13,000 – 12,000 (IOC) – 18,000 (salary) – 15,000(commission) = 1,52,000. Share of X in divisible profit = 1,52,000 × 3/5 = 91,200
5.	(b) : Closing capital of x = 2,00,000 (opening capital) + 1,00,000 (addl capital) + 13,000 (IOC) + 18,000 (salary) + 91,200 (profit share) – 20,000 (drawings) – 800 (IOD) = 4,01,400

CHAPTER 2

GOODWILL METHODS OF VALUATION OF GOODWILL

TOPIC	MEANING/EXPLANATION
Meaning of Goodwill	Goodwill is the value of the reputation of a firm in respect of the profits expected in future over and above the normal profits. In simple words, goodwill can be defined as "the present value of a firm's anticipated excess earnings" or as "the capitalised value attached to the differential profit capacity of a business". Thus, goodwill exists only when the firm earns super profits Any firm that earns normal profits or is incurring losses has no goodwill.
Characteristic/ Features of Goodwill	1. It is an intangible asset. 2. It is not a fictitious asset. 3. It is difficult to ascertain the exact value of goodwill. 4. It enhances the present as well as the future earning capacity a business. 5. It helps in earning the supernormal profits against the normal profits. 6. It is a basis for winning customers trust and faith 7 A positive goodwill not only facilitates a firm to win customers trust but also helps the company to excel over its competitors.

Factors Affecting the Value of Goodwill:	The main factors affecting the value of goodwill are as follows: 1. Nature of business: A firm that produces high value added products or having a stable demand is able to earn more profits and therefore has more goodwill. 2. Location If the business is centrally located or is at a place having heavy customer traffic, the goodwill tends to be high. 3. Efficiency of management A well-managed concern usually enjoys the advantage of high productivity and cost efficiency. This leads to higher profits and so the value of goodwill will also be high. 4. Market situation: The monopoly condition or limited competition enables the concern to earn high profits which leads to higher value of goodwill. 5. Special advantages The firm that enjoys special advantages like import licences, low rate and assured supply of electricity, long term contracts for supply of materials, well-known collaborators, patents, trademarks, etc. enjoy higher value of goodwill.
Need for Valuation of Goodwill:	Normally, the need for valuation of goodwill arises at the time of sale of a business. But, in the context of a partnership firm it may also arise in the following circumstances: 1. Change in the profit sharing ratio amongst the existing partners; 2. Admission of new partner; 3. Retirement of a partner; 4. Death of a partner; and 5. Dissolution of a firm involving sale of business as a going concern. 6. Amalgamation of partnership firms
Types of Goodwill	**1. Purchased/Acquired Goodwill** Purchased goodwill comes around when a business concern is purchased for an amount above the fair value of the separable acquired net assets. As a result, it is shown on the balance sheet as an asset they are the only types of goodwill which can be recognized on a company's accounts. Value of Purchased Goodwill = Purchase Consideration – Net Assets

	2. Self Generated/Inherent Goodwill Self Generated/Inherent goodwill is the opposite of purchased goodwill and represents the value of a business more than the fair value of its separable net assets. This type of goodwill is internally generated and arises over time due to reputation, and it can be either positive or negative
Methods of Valuation of Goodwill	Goodwill calculated by one method may differ from the goodwill calculated by another method Hence, the method by which goodwill is to be calculated may be specifically decided between the existing partners and the incoming partner. The important methods of valuation of goodwill are as follows: 1. Average Profits Method 2. Super Profits Method 3. Capitalisation Method
Accounting treatment of goodwill as per AS 26	Accounting Standard 26 implies that (a) Purchased goodwill may be accounted for in the books and shown as an asset, where it is accounted for in the books and shown as assets, it should be written off as early as possible, but where it is to be written-off in more than one accounting year, it should be written off in a period not exceeding 10 years. In line with what is prescribed by the Accounting Standard, goodwill appearing in the balance sheet in written off at the time of firm's reconstitution (b) Self-generated goodwill is not accounted for in the books and shown as an asset. Thus if self generated goodwill be debited to goodwill account it should be written-off in the same financial year and should not be shown as an asset in the balance sheet. Alternatively value of goodwill may be adjusted by deducting new partners' current account and crediting in sacrificing partners in their sacrificing ratio. The effect under both the methods is same.

SIMPLE AVERAGE PROFIT METHOD	Under this method, the goodwill is valued at the agreed numbers of years of purchase of the average profits of the past years. STEPS OF CALCULATE GOODWILL 1. Calculate Adjusted Profits/Normal Business Profit: Profit or Loss of the past year ADD : Abnormal losses Loss on Sale of Fixed Assets Overvaluation of opening stock Undervaluation of closing stock Non-recurring Expenses Capital Expenditure charged as Revenue Expenditure LESS : Abnormal gains Profit on sale of Fixed Assets Overvaluation of closing stock Undervaluation of opening stock Non-recurring incomes Partner's remuneration, if it is not deducted Income from Non-trade Investments Any future Expense

	ADJUSTED/FUTURE MAINTAINABLE PROFIT
	2. AVERAGE PROFIT = $\dfrac{\text{TOTAL OF ADJUSTED PROFIT}}{\text{No. of YEARS}}$ 3. GOODWILL = AVERAGE PROFIT X NO. OF YEAR'S OF PURCHASE
SUPER PROFIT METHOD	Under this method, the goodwill is valued at the agreed number of year's of purchase of the super profits of the firm STEPS TO CALCULATE GOODWILL 1) Average Capital = $\dfrac{\text{Opening capital employed} + \text{closing capital employed}}{2}$ 2) Calculate average maintainable profit (as above) 3) Normal of profit = Average Capital Employed $\times \dfrac{\text{Normal rate of return}}{100}$ 4) Super Profit = Average maintainable profits - Normal Profits 5) GOODWILL = SUPER PROFIT × NO. OF YEAR'S OF PURCHASE <u>Calculation of capital employed</u> • Assets side Approach • Capital Employed = All Assets (except goodwill, non-trade investments and ficitious assets) - Outside liabilities • Liabilities side Approach

	Capital Employed = Capital + Reserves - Goodwill (if exists in books)- Ficitious Asset - Non- trade investments
CAPITALISATION OF AVERAGE PROFITS	Under this method, the value of goodwill is calculated by deducting the actual capital employed from the capitalization value of the average profits on the basis of the normal rate of return **STEPS TO CALCULATE GOODWILL** 1. Calculate Average Normal Profit 2. Capitalised value of the Business = $\frac{\text{Average profit} \times 100}{\text{Normal rate of return}}$ 3. Capital Emloyed = All Assets (except goodwill, non-trade investment and ficitious assets) - Outside liabilities 4. GOODWILL = Capitalised value of the Business - Net Assets
CAPITALISATION OF SUPER PROFITS	Under this method, Goodwill is calculated by capitalizing the super profits **STEPS TO CALCULATE GOODWILL** 1. Capital Employed = All Assets (except goodwill, non-trade investments and ficitious assets) - Outside Liabilities 2. Normal Profit = Capital Employed × $\frac{\text{Normal rate of return}}{100}$ 3. Capital average maintainable profit (as above) 4. Super Profit = Average maintainable profits - Normal Profits 5. GOODWILL = $\frac{\text{Super Profit}}{\text{Normal rate of return}} \times 100$

1. Calculate value of goodwill on the basis of three years' purchase of average profit of the preceding five years which were as follows:

Year	2017–18	2016–17	2015–16	2014–15	2013–14
Profits (₹)	8,00,000	15,00,000	18,00,000	4,00,000 (Loss)	13,00,000

Answer: Goodwill = Average Profit × Number of year's purchase

$$\text{Average Profit} = \frac{8,00,000 + 15,00,000 + 18,00,000 - 4,00,000 + 13,00,000}{5}$$

$$= \frac{50,00,000}{5} = ₹\ 10,00,000$$

Number of year's Purchase = 3

$\therefore$ Goodwill = 10,00,000 × 3 = ₹ 30,00,000

2. A and B area partners sharing profits in the ratio of 3 : 2. They decided to admit c as a partner from 1st April, 2018 on the following terms:

(a) C will be given 2/5th share of the profit.

(b) Goodwill of the firm be valued at two years' purchase of three year's normal average profit of the firm.

Profits of the previous three years ended 31st March, were:

2018 – Profit ₹ 30,000 (after debiting loss of stock by fire ₹ 40,000)

2017 – Loss ₹ 80,000 (includes voluntary retirement compensation paid ₹ 1,10,000).

2016 – Profit ₹ 1,10,000 (including a gain (profit) of ₹ 30,000 on the sale of fixed assets).

You are required to calculate the value the goodwill

Answer

Goodwill = Normal Average Profit × Number of years' purchase

Year	**Actual Profit**	**+**	**Abnormal Loss Non-recurring**	**–**	**Abnormal Gain Non-recurring**	**=**	**Normal Profit**
2018	30,000	+	40,000	–	Nil	=	70,000
2017	80,000	+	1,10,000	–	Nil	=	30,000
2016	1,10,000	+	Nil	–	30,000	=	80,000
Normal Profit for 3 Years							1,80,000

$$\text{Normal Average Profit} = \frac{\text{Normal Profits for last 3 years}}{3}$$

$$= \frac{1,80,000}{3} = ₹\ 60,000$$

Numbers of year's purchase 2

$\therefore$ Goodwill = 60,000 × 2 = ₹ 1,20,000

3. X and Y are partners sharing profits and losses in the ratio of 3 : 2. They admit Z into partnership for 1/4th share in goodwill. z brings in his share of goodwill in cash.

Goodwill for this purpose is to be calculated at two years' purchase of the average normal profit of past three years Profits of the last three years ended 31st March, were:

2016 – Profit ₹ 50,000 (including profit on sale of assets ₹ 5,000)

2017 – Loss ₹ 20,000 (includes loss by fire ₹ 30,000)

2018 – Profit ₹70,000 (including insurance claim received ₹ 18,000 and interest on investments and dividend received ₹ 8,000).

Calculate value of goodwill. Also, calculate goodwill brought in by Z.

Answer

Goodwill = Normal Average Profit × Number of years' purchase

Year	**Actual Profit**	**+**	**Abnormal Loss Non-recurring**	**–**	**Abnormal Gain Non-recurring**	**=**	**Normal Profit**
2016	50,000	+	Nil	–	5,000	=	45,000
2017	(20,000)	+	30,000	–	Nil	=	10,000
2018	70,000	+	Nil	–	18,000 + 8,000	=	44,000
Normal Profit for 3 Years							99,000

$$\text{Normal Average Profit} = \frac{\text{Normal Profits for last 3 years}}{3}$$

$$= \frac{99,000}{3} = ₹\ 33,000$$

Number of years' purchase = 2

$\therefore$ Goodwill = 33,000 × 2 = ₹ 66,000

Z's Share of Goodwill = Goodwill of the Firm × Z's Share of Profit

$$= 66,000 \times \frac{1}{4} = ₹\ 16,500$$

4. A and B are partners in a firm sharing profits and losses in the ratio of 2 : 1. They decide to take C into partnership for 1/4th share on 1st April, 2018. For this purpose, goodwill is to be valued at four times the average annual profit of the previous four or five years whichever is higher. The agreed profits for goodwill purpose of then past five years are:

Year	2013–14	2014–15	2015–16	2016–17	2017–18
Profit (₹)	14,000	15,500	10,000	16,000	15,000

Answer

Calculation of Average Profit for Five Years

Year	Profit
2013–14	14,000
2014–15	15,500
2015–16	10,000
2016–17	16,000
2017–18	15,000
Total Profit	**70,500**

Average Profit 70,500/5 = ₹ 14,100

Year	Profit
2014–15	15,500
2015–16	10,000
2016–17	16,000
2017–18	15,000
Total Profit	**56,500**

Average Profit 56,500/4 = ₹ 14,125

Average Profit of four years is taken to compute the value of goodwill of the firm. This is because Average Profit of four years is more than the Average Profit of five yea₹

∴ Goodwill = Average Profit × Number of years' purchase

= 14,125 × 4 = ₹ 56,500

5. X and Y are partners in a firm. They admit Z into partnership for equal share. It was agreed that goodwill will be valued at three yeas; purchase of average profit of last five year. Profits for the last five years were:

Year Ended	31st March 2014	31st March 2015	31st March 2016	31st March 2017	31st March 2018
Profit (₹)	90,000 (Loss)	1, 60,000	1,50,000	65,000	1,77,000

Books of Account of the firm revealed that:

(i) The firm had gain (profit) of ₹ 50,000 from sale of machinery sold in the year ended 31st March, 2015. The gain (profit) was credited in Profit and Loss Account.

(ii) There was an abnormal loss of ₹ 20,000 incurred in the year ended 31st March, 2016 because of a machine becoming obsolete in accident.

(iii) Overhauling cost of second hand machinery purchase on 1st July, 2016 amounting to ₹ 1,00,000 was debited to Repairs Accounts. Depreciation is charged @ 20% p.a. on Written Down Value Method.

Calculate the value of goodwill.

Answer

Goodwill = Average Profit × No. of years' purchase

= 1,00,000 × 3 = ₹ 3,00,000

Working Notes

W.N: 1 Calculation of Normal Profits

Year	Profit/Loss (₹)	Adjustment	Normal Profit (₹)
31 March, 2014	(90,000)		(90,000)
31 March, 2015	1,60,000	(50,000)	1,10,000
31 March, 2016	1,50,000	20,000	1,70,000
31 March, 2017	65,000	85,000	1,50,000
31 March, 2018	1.77,000	(17,000)	1,60,000
			5,00,000

***Adjustment Amount**

Overhauling cost of second hand machinery wrongly accounted as expense instead of capital expenditure. Profit to be increase by ₹ 1,00,000	1,00,000
Depreciation to be debited form P&L A/c (1,00,000 × 20/100 × 9/12)	15,000
Amount to be added back	85,000

W.N: 2 Calculation of Average Profit

Average Profit = Total Profit for past given year Number of Years

= 5,00,000/5 = ₹ 1,00,000

6. Gupta and Bose had a firm in which they had invested ₹ 50,000. On an average, the profit were ₹ 16,000. The normal rate of return in the industry is 15%. Goodwill is to be valued at four years' purchase of profits in excess of profits @ 15% on the money invested. Calculate the value Goodwill.

Answer

Goodwill = Super Profit × Number of Years' Purchase

$$\text{Normal Profit} = \text{Capital Employed} \times \frac{\text{Normal Rate of Return}}{100}$$

$$= 50{,}000 \times \frac{15}{100} = ₹\ 7{,}500$$

Actual Profit = ₹ 16,000

Super Profit = Actual Profit – Normal Profit

= 16,000 – 7,500 = ₹ 8,500

Number of years' purchase = 4

∴ Goodwill = 8,500 × 4

= ₹ 34,000

7. The total capital of the firm of Sakshi Mehak and Megha is ₹ 1,00,000 and the market rate of interest is 15% The net profits for the last 3 years were ₹ 30,000, ₹ 36,000 and ₹ 42,000 Goodwill is to be valued at 2 years' purchase of the last 3 years super profits Calculate the goodwill of the firm.

Answer

Goodwill = Super Profit × Number of Years' Purchase

Super Profits = Average Profit – Normal Profit

Average Profits = Total Profits/Number of Years

30.000 + 36,000 + 42,000/3 = ₹ 36,000

Normal Profits = Capital Employed × Normal Rate of Return

1,00,000 × 15/100 = 15.000

Super Profits = 36,000 – 15,000 = 21,000

Goodwill = 21.000 × 2 = ₹ 42,000

8. A partnership firm earned net profits during the past three years as follows:

Year ended	31st March, 2018	31st March, 2017	31st March, 2016
Net Profit (₹)	2,30,000	2,00,000	1,70,000

Capital investment in the firm throughout the above-mentioned period has been ₹ 4,00,000 Having regard to the risk involved, 15% in considered to be a fair return on the capital The remuneration of the partners during this period is estimated to be ₹ 1,00,000 pa Calculate value of goodwill on the basis of two years' purchase of average super profit earned during the above-mentioned three years.

Answer

Goodwill = Super Profit × Number of Years Purchase

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

= $4{,}00{,}000 \times \frac{15}{100}$ = ₹ 60,000

Year	Profit before Partners' Remuneration	–	Partners' Remuneration	=	Actual Profit after Remuneration
2016	1,70,000	–	1,00,000	=	70,000
2017	2,00,000	–	1,00,000	=	1,00,000
2018	2,30,000	–	1,00,000	=	1,30,000

Average Actual Profit after Remuneration = $\frac{70{,}000 + 1{,}00{,}000 + 130{,}000}{3} = \frac{3{,}00{,}000}{3}$

= ₹ 1,00,000

Super Profit = Average Actual Profit after Remuneration – Normal Profit

= 1,00,000 – 60,000 = ₹ 40,000

Number of years' purchase = 2

∴ Goodwill = ₹ 40,000 × 2 = ₹ 80,000

9. On 1st April, 2018, an existing firm had assets of 75,000 including cash of ₹ 5,000. Its creditors amounted to ₹ 5,000 on that date. The firm had a Reserve of ₹ 10,000 while Partners' Capital Accounts showed a balance of ₹ 60,000. If Normal Rate of Return is 20% and goodwill of the firm is valued at 24,000 at four years' purchase of super profit, find average profit per year of the existing firm.

Answer

Average Profit = Normal Profit + Super Profit

Capital Employed = total Assets – Creditors

= 75,000 – 5,000 = ₹ 70,000

Normal Profit = Capital Employed × $\frac{\text{Normal Rate of Return}}{100}$

= $70{,}000 \times \frac{20}{100}$

Goodwill of the firm = ₹ 24,000

Number of years' purchase = 4

Goodwill = Super Profit × Number of Years' Purchase or, 24,000 = Super Profit × 4

or. Super Profit = $\frac{24,000}{4}$

= ₹ 6,000

∴ Average Profit = Normal Profit + Super Profit

= 14,000 + 6,000 = ₹ 20,000

9. Ayub and Amit are partners in a firm and they admit Jaspal into partnership w.e. f. 1st April, 2028. they agreed to value goodwill at 3 years' purchase of Super Profit Method for which they decided to average profit of last 5 yea₹ The profit for the last 5 years were.

Year Ended	Net Profit (₹)	
31st March, 2014	1,50,000	
31st March, 2015	1,80,000	
31st March, 2016	1,00,000	(Including abnormal loss of ₹1,00,000)
31st March, 2017	2,60,000	(Including abnormal gain (profit) of 40,000)
31st March, 2018	2,40,000	

The firm has total assets of ₹ 20,00,000 and Outside Liabilities of ₹ 5,00,000 as on that date. Normal Rate of Return in similar business is 10%. Calculate value of goodwill.

Answer

Goodwill = Super profit × No. of Years' Purchase

= 48,000 × 3 = ₹ 1,44,000

Goodwill = Super Profit × No. of Years; Purchase

= 48,000 × 3 = ₹ 1,44,000

Working Notes:

WN: 1 Calculation of Normal Profits:

Year	Profit (Loss) (₹)	Adjustment	Normal Profit (₹)
31 March, 2014	1,50,000	–	1,50,000
31 March, 2015	1,80,000	–	1,80,000
31 March, 2016	1,00,000	1,00,000	2,00,000
31 March, 2017	2,60,000	(40,000)	2,20,000
31 March, 2018	2,40,000		2,40,000
		Total Profit	9,90,000

WN: 2 Calculation of Super Profits

Average Profit = Total profit of past given yeas/Number of Years

= 9,90,000/5 = ₹ 1,98,000

Normal Profit = Capital Employed × Normal Rate of Return/100

= 15,00,000 × 10100 = ₹ 1,50,000

Super Profit = Average Profit – Normal Profit

= 1,98,000 – 1,50,000 = ₹ 48,000

WN: 3 Calculation of Capital Employed

Capital Employed = Total Assets – Outside Liabilities

= 20,00,000 – 5,00,000 = ₹ 15,00,000

11. A business has earned average profit of ₹ 1,00.000 during the last few years Find out the value of goodwill by capitalisation method, given that the assets of the business are ₹ 10,00,000 and its external liabilities are ₹ 1,80,000 The normal rate of return is 10%.

Answer

Goodwill = Capitalised Value of Average Profits – Actual Capital Employed

Capitalised Value of Average = Profit Average Profit × 100/Nominal Rate of Return = 1,00,000 100/10 = 10,00,000

Actual Capital Employed = 10,00,000 – 1,80,000 = 8,20,000

Goodwill = 10,00,000 – 8,20,000 = ₹ 1,80,000

12. Calculate the value of goodwill of X and Y using following Information:

(i) At two years' purchase of Average Profit

(ii) At two years' purchase of Super Profit

(iii) On the basis of capitalisation of super profit

(iv) On the basis of capitalisation of average profit. It is given that

(a) Average Capital Employed is Rs 12,00,000

(b) Profit for the firm for past three years

2017 – ₹ 1,80,000; 2018 – ₹ 1,60,000; 2019 – ₹ 2,60,000

(c) Normal rate of return is 10%

(d) Remuneration to each partner is ₹ 3,000 per month

(e) Assets – ₹ 13 50,000 and liabilities ₹ 1,50,000,

Answer. (i) At two years' purchase of average profit:

$$\text{Average Profit} = \frac{1{,}80{,}000 + 1{,}60{,}000 + 2{,}60{,}000}{3}$$

$$= \frac{6,00,000}{3} = ₹\ 2,00,000$$

Average Normal Profit = Average Profit – Partners' Remuneration

= ₹ 2,00,000 – (₹ 3,000 × 12 × 2)

= ₹ 1,28,000

Goodwill = Average Normal Profit × 2

= ₹ 1,28,000 × 2

= ₹ 2,56,000

(ii) At two years' purchase of super profit:

$$\text{Normal Profit} = \text{Capital Employed} \times \frac{\text{Normal Rate of Return}}{100}$$

$$= ₹\ 12,00,000 \times \frac{10}{100} = ₹\ 1,20,000$$

Super Profit = Average Profit – Normal Profit

= ₹ 1,28,000 – ₹ 1,20,000

= ₹ 8,000

Goodwill at two years' Purchase = 8,000 × 2

= ₹ 16,000

(iii) By Capitalisation of Super Profit

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

= ₹ 8,000 × 100/10

= ₹ 80,000

(iv) By Capitalisation of Average Profit

Goodwill = Capitalised Value of Business – Net Assets

$$\text{Capitalised Value of business} = \frac{\text{Average Normal Profit} \times 100}{\text{Normal Rate of Returns}}$$

$$= \frac{1,28,000 \times 100}{10}$$

= ₹ 12,80,000

Net Assets = total Assets – Outsider's Liabilities

= ₹ 13,50,000 – ₹ 1,50,000

= ₹ 12,00,000

So, Goodwill = ₹ 12,80,000 – ₹ 12,00,000

= ₹ 80,000

Assertion Reason Based Questions

Goodwill

1. Given below are two statements, one labeled as Assertion (A) and the other labeled as Reason (R):

Assertion (A): Goodwill is as an intangible asset.

Reason (R): Goodwill helps the business to earn more profits as compared to a newly set up business.

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct.

(d) Both (A) and (R) are wrong.

2. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): Goodwill is the value of the reputation of a firm in respect of the profits expected in future over and above the Super profits.

Reason (R): "Goodwill is the present value of a firm's anticipated excess earnings"

In the context of the above two statements, which of the following is correct?

Codes:

(a) Both (A) and (R) are correct and (R) is the correct reason of (A).

(b) Both (A) and (R) are correct but (R) is not the correct reason of (A).

(c) Only (R) is correct.

(d) Both (A) and (R) are wrong.

3. Given below are two statements, one labeled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): "Goodwill is the capitalised value attached to the differential profit capacity of a business.

Reason (R): Goodwill exists only when the firm earns super profits.

Codes:

(a) Both (A) and (R) are true, but (R) is not the explanation of (A).

(b) Bath(A) and (R) are true and (R) is a correct explanation of (A).

(c) Both (A) and (R) are false.

(d) (A) is false, but (R) is true.

4. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): A firm that produces high value added products or having a stable demand is able to earn more profits.

Reason (R): Nature of business does not affect the value of Goodwill.

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong.

(b) Both (A) and (R) are correct.

(c) (A) it wrong, but (R) is correct.

(d) Both (A) and (R) are wrong.

5. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): A well-managed concern usually enjoys the advantage of low productivity and cost inefficiency.

Reason (R): Efficiency of management leads to Lower profits and so the value of goodwill will also be Low:

In the context of the above two statements, which of the following is correct?

Codes:

(a) Both (A) and (R) are correct and (R) is the correct reason of (A).

(b) Both (A) and (R) are correct but (R) is not the correct reason of (A).

(c) Only (R) is correct.

(d) Both (A) and (R) are wrong.

6. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): Normally, the need for valuation of goodwill arises at the time of sale of a business.

Reason (R): in the context of a partnership firm, the need for valuation of goodwill arises at the time of change in the profit sharing ratio amongst the existing partner.

Codes:

(a) Both (A) and (R) are true, but (R) is not the explanation of (A).

(b) Both(A) and (R) are true and (R) is a correct explanation of (A).

(c) Both (A) and (R) are false.

(d) (A) is false, but (R) is true:

7. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): Since goodwill is an intangible asset it is very difficult to accurately calculate its value

Reason (R): Goodwill calculated by one method may differ from the goodwill calculated by another method.

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong.

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct.

(d) Both (A) and (R) are wrong.

8. Given below are two statements, one labeled as Assertion (A) and the other labeled as Reason (R):

Assertion (A): The excess of actual profits over the normal profits is termed as super profits.

Reason (R): The goodwill under the super profit method is ascertained by multiplying the super profits by certain number of years' purchase.

In the context of the above two statements, which of the following is correct?

Codes:

(a) Both (A) and (R) are correct and (R) is the correct reason of (A).

(b) Both (A) and (R) are correct but (R) is not the correct reason of (A).

(c) Only (R) is correct.

(d) Both (A) and (R) are wrong.

9. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): Under Capitalisation of Average Profits method, the value of goodwill is ascertained by deducting the actual firm's capital in the business from the capitalized value of the average profits on the basis of normal rate of return.

Reason (R): Actual firm's capital (net assets) can be asertaines by deducting outside liabilities from the total assets (excluding goodwill and ficticious assets).

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct

(d) Both (A) and (R) are wrong.

10. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): Accounting Standard 26 implies that Self-generated goodwill is not accounted for in the books and shown as an asset.

Reason (R): Accounting Standard 26 implies that Purchased goodwill may be accounted for in the books and shown as an asset, where it is accounted for in the books and shown as assets.

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong.

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct.

(d) Both (A) and (R) are wrong.

Q. No.	Answer
1.	B
2.	C
3.	A
4.	A
5.	D
6.	A
7.	B
8.	B
9.	B
10.	B

Case Study Based Questions

GOODWILL

Read the following information carefully and answer the questions 1 to 4 that follow:

Average profit earned by a firm is ₹ 80,000 which includes undervaluation of stock of ₹ 8,000 on an average basis. The capital invested in the business is ₹ 8,00,000 and the normal rate of return is 8%.

1. Average Profits after adjustment of stock of the firm is:

(a) ₹ 80.000 (b) ₹ 88.000

(c) ₹ 72.000 (d) ₹ 64,000

2. Normal Profits of the firm is:

(a) ₹ 80,000 (b) ₹ 88,000

(c) ₹ 72,000 (d) ₹ 64,000

3. Super Profits of the firm is:

(a) ₹ 80,000 (b) ₹ 88,000

(c) ₹ 68.000 (d) ₹ 24,000

4. Goodwill of the firm as per super profit method on the basis of 7 year of purchase is:

(a) ₹ 1,80,000 (b) ₹ 1.88,000

(c) ₹ 1.68.000 (d) ₹ 1.24.000

Q. No.	Answer with Explanation
1.	(b) Average Profits of the firm after adjustment = (Average Profits + Undervaluation of stock) = ₹ (80,000 + 8,000) = ₹ 88,000
2.	(d) Normal Profits = ₹ (Capital Employed × Normal Rate of Return/100) = ₹ (8,00,000 × 8/100) = ₹ 64,000
3.	(d) Super Profits = Average Profits – Normal Profits = ₹ (88,000 – 64,000) = ₹ 24,000
4.	(c) Goodwill = Super Profits × No. of Years of Purchase = ₹ (24,000 × 7) = ₹ 1,68,000

MCQ

1. Capital employed by a partnership firm is ₹ 15,00,000. Its average profit is ₹ 60,000. The normal rate of return for is a similar type of business is 10%. The amount of super profit is ....

(a) ₹ 50.000 (b) ₹ 10,000

(c) ₹ 6,000 (d) ₹ 56.000

2. Which of the following statement is correct?

(a) Goodwill is a fictitious asset.

(b) Goodwill is a current asset.

(c) Goodwill is a wasting asset.

(d) Goodwill is an intangible asset

3. Average profit of a business over the last five years ware ₹ 60,000. The normal yield on capital invested in such a business is estimated at 10% pa. Capital invested in the business is ₹ 5,00,000. Amount of goodwill, it is based on 3 year's purchase of last 5 years super profit will be

(a) ₹ 1,00.000 (b) ₹ 1.80.000

(a) ₹ 30,000 (d) ₹ 1,50,000

4. Net assets of a firm including fictitious assets of ₹ 5,000 are ₹ 85,000. Net liabilities of the firm are ₹ 30,000. The normal Rate of Return is 10% and the average profit of the firm is ₹ 8.000. Value of goodwill as per capitalization of super profit method will be

(a) ₹ 20,000 (b) ₹ 30,000

(c) ₹ 25.000 (d) ₹ 15,000

5. As per AS – 26, ________ Goodwill is recorded in the books of accounts.

(a) Purchase (b) Self-generated

(c) Both a and b (d) None of these

6. The average Capital Employed of a firm is ₹ 4,00,000 and the Normal Rate of Return is 15%. The average Profit of the firm is ₹ 80,000 per annum. If management cost is estimated at ₹ 10,000 per annum, then on the basis of two years purchase of super profit, the value of goodwill will be

(a) ₹ 10,000 (b) ₹ 20,000

(c) ₹ 60,000 (d) ₹ 80,000

7. A firm earns a profit of ₹ 1,10,00. The Normal Rate of Return is 10%. Assets of the firm are ₹ 11,00,000 and liabilities ₹ 1,00,000. Value of goodwill by the capitalisation of Average profit will be

(a) ₹ 2,00,000 (b) ₹ 10,000

(c) ₹ 5,000 (d) ₹ 1,00,000

8. Net profits during the last three years of a firm are

(a) 1st Year – 18,000 (b) 2nd Year – 20,000

(c) 3rd Year – 22,000

The capital investment of the firm is ₹ 60,000. The normal Rat of Return is 10%. Value of goodwill on the basis of three years purchase of the super profit for the last three years will be

(a) ₹ 21,000 (b) ₹ 42,000

(c) ₹ 84,000 (d) ₹ 20,000

9. For valuation of goodwill, normal profit is calculated by ________ abnormal gains and ________ abnormal losses.

(a) Adding, deducting (b) Deducting, adding

(c) deducting, not treating (d) Not treating, adding

10. Net Asset = All Assets (Except goodwill, fictitious assets and ______ investments) – Outside liabilities.

(a) Trade (b) Non-trade

(c) Long term (d) Short term

11. M/s Supertech India has assets of ₹ 5,00,000, whereas Liabilities are: Partners capitals – ₹ 3,50,000, General Reserve – ₹ 60,000 and Sundry

creditors – ₹ 90,000. If the Normal rate of return is 10% and the Goodwill of the firm is valued at 90,000 at 2 years' purchase of super profit, the average profit of the firm will be

(a) ₹ 46,000 (b) ₹ 86,000

(c) ₹ 1,63,000 (d) ₹ 23,000

12. __________ refers to a specific number of years for which a business will earn the same amount of profits because of its past efforts.

(a) Amount of profits (b) Span of years

(c) Number of year purchase (d) Time of profits

13. If super profits are negative, then goodwill will be

(a) positive (b) negative

(c) either a and b (d) Ni

14. Tangible assets of the firm are ₹ 14,00,000 and outside liabilities are ₹ 4,00,000. The profit of the firm is ₹ 1,50,000 and the normal rate of return is 10%. The amount of capital employed will be

(a) ₹ 10,00,000 (b) ₹ 1,00,000

(c) ₹ 50,000 (d) ₹ 20,000

15. The profits earned by a business over the last 5 years are as follows: ₹ 12,000; ₹ 13,000; ₹ 14,0000; ₹ 18,000 and ₹ 2,000 (loss). Based on 2 years purchase of the last 5 years profits, value of Goodwill will be

(a) ₹ 23,600 (b) ₹ 22,000

(c) ₹ 1,10,000 (d) ₹ 1,18,000

Q. No.	Answer
1.	B
2.	D
3.	C
4.	B
5.	A
6.	B
7.	D
8.	B
9.	B
10.	B
11.	B
12.	C
13.	D
14.	A
15.	B

Goodwill

MCQ/OBJECTIVES

Fill In the Blanks

1. Goodwill is an ________ assets.
2. If average capital employed in a firm is ₹ 7,00,000, actual profit is ₹ 90,000 and normal rate of return is 10%, then super profit is ______ .
3. The Goodwill of firm ₹ 3,60,000 valued at three year's purchase of super profit. If capital employed is ₹ 4,00,000 and Normal rate of return is 10% per annum The amount of average profit will be ______ .
4. _______ is the value of reputation of a firm in respect of the profits expected in future over and above the normal profits.
5. As per Accounting Standard goodwill should not be recorded in the books of accounts _______ unless consideration is paid for it.

True /False

1. As per AS-26, self-generated goodwill cannot be raised and recorded in the books of accounts though it is considered an Asset.
2. While calculating the average profits any abnormal loss is excluded by deducting it out of the net profit of that year.
3. Any surplus profit in excess of super profit earned by a firm is known as average profit.
4. If the firm is earning only normal rate of return (or normal profits) there will be no goodwill of the firm.
5. Number of years' purchase means the years for which the firm is likely to earn that much profit because of the reputation earned by its past efforts.

MULTIPLE CHOICE QUESTIONS

1. If Goodwill is ₹ 2,40,000, Average Profit is ₹ 1,20,000 Normal. Rate of Return is 10% on Capital Employed ₹ 9,60,000. Calculate capitalized value of the firm:

   a) ₹ 12,00,000 b) ₹ 10,00,000

   c) ₹ 8,00,000 d) ₹ 14,00,000

2. Tangible Assets of the firm are ₹ 7,00,000 and Outside liabilities are ₹ 2,00,000, Profit of the firm is ₹ 75,000 and normal rate of return is 10% Calculate capital employed?

a) ₹ 9,00,000 b) ₹ 7,50,000

c) ₹ 5,00,000 d) ₹ 9,75,000

3. A firm had Assets of ₹ 3,00,000 partner's capital account showed a balance of ₹ 2,40,000 and reserves constituted the rest. If normal rate of return is 10% per annum and Goodwill is valued at ₹ 96,000 at four years purchase of super profits, find the super profit of firm :

   a) ₹ 12,000 b) ₹ 36,000

   c) ₹ 16,000 d) ₹ 24,000

4. Which of the following is not correct?

   a) Super Profit = Actual (average) Profit - Normal Profit

   b) Super Profit = Actual (average) Profit + Normal Profit

   c) Value of goodwill = Total Capitalised Value of the business - Net Assets.

   d) Goodwill = Average Profit x Number of Years Purchased

5. A business has earned Super profit of ₹ 2,00,000 during the last few years and Normal rate of returns in 10% Value of goodwill as per capitalisation of super profit is:

   a) ₹ 20,000 b) ₹ 20,00,000

   c) ₹ 10,000 d) ₹ 20,000

Matching Questions

1. Match the following:

Description	Options
1 Closing stock under valued	a. Deducted to the current year profits and added to the previous year profits for calculating the average profits
2 Closing stock over valued	b. Added to the current year profits and deducted from previous year profits for calculating the average profits
3 Opening stock over valued	c. No effect on the average profits
4 Opening stock under valued	d. Added to the current year profits for calculating the average profits
	e. Deducted to the current year profits for calculating the average profits

2. Identify the factors affecting the value of goodwill:

Description	Options
1. If the firm is situated at a prominent centrally located convenient place	a. Favourable Contracts
2. If the firm is managed and controlled by the experienced and efficient management	b. Time Factor
3. If the business is running for the last twenty thirty years on profitable line	c. Type of Business
4 If the business is monopoly business	d. Location of Business
	e. Efficiency of Management

3. Match the following

Description	Options
1 Average Profit Method	a. Normal Profit
2 In every type of industry there is an average rate of profits which every firm is expected to earn	b. Super Profit
3 Goodwill as per Capitalised Value of Average Profits	c. Average profit
4 Any surplus profit in excess of normal profit earned by a firm is	d. This is a very simple and widely followed method of valuation of goodwill
	e. Capitalised Value of business - Net Asset

4. Match the following

Description	Options
1 A firm having the assets of ₹25,00,000 and liabilities of ₹11,00,000 earns annual profits of ₹2,40,000. The rate of normal profits being 15%. Amount of goodwill by capitalisation of super profit method	(a) ₹ 62,500
2 A firm earns ₹ 25,000 as its annual profits, the rate of normal profit being 10%. The assets of the firm amounted to ₹ 2,00,000. The value of goodwill is ₹ 1,12,500. Value of outsiders' liabilities	(b) ₹ 37,500
	(c) ₹ 1,35,000

	(d) ₹ 4,00,000
	(e) ₹ 2,00,000

5. Match the following

Description	Options
1. Classification of Goodwill	a) Number of years of purchase
2. Need for Valuation of Goodwill	b) Personal Popularity and Relationship
	c) When there is a change in profit sharing ratio
	d) When there are Better Quality of Products
	e) Self-Generated Goodwill

ANSWERS

Fill In the Blanks

1. Intangible
2. ₹ 20,000
3. ₹ 1,60,000
4. Goodwill
5. 26

True /False

1. T
2. F
3. F
4. T
5. T

MULTIPLE CHOICE QUESTIONS

1. a
2. c
3. d
4. b
5. b

Matching Questions

1. [l-b;2-a;3-d;4-e]
2. [l-d;2-e;3-b;4-c]

3. [l-d;2-a;3-e;4-b]
4. [l-e;2-a]
5. [l-e;2-c]

Work Sheet on Goodwill

Q.1 State the meaning and characteristics of goodwill.

Q.2 State any three circumstances other than (i) admission of a new partner; (ii) retirement of a partner, and (iii) death of a partner, when need for valuation of goodwill of a firm may arise.

Q.3 Apart from Location and Profitability, list any two other factors affecting goodwill of a firm.

Q.4 Why is 'Goodwill considered an Intangible Asset' but not a 'Fictitious Asset'?

Q.5 Distinguish between average profits and super profits.

Q.6 Differentiate between self-generated goodwill and purchased goodwill.

Q.7 The profits and losses for last five years were : 1st Year —₹44,000 (including an abnormal gain of ₹8,000) 2nd Year— ₹60,000 (excluding ₹16,000 as insurance premium) 3rd Year—₹24,000 (after charging an abnormal loss of f 8,000) 4th Year —₹24,000 5th Year - ₹8,000 (Loss) Calculate the amount of goodwill on the basis of 2½ years' purchases of last five years' average profits.

Q.8 The profits of the firm of Arun, Ajay and Dinesh are given below:

Year ended 31st March	Profit (₹)
2016	40,000
2017	56,000
2018	40,000
2019	52,000

(i) On 1st July, 2018 the firm purchased machinery costing ₹20,000 but it was charged to revenue by mistake. Depreciation @ 10% p.a. was also not provided on it.

(ii) During the year 2018-19 the personal expenses of Arun ₹6,000 and Ajay ₹4,000 were debited to miscellaneous expenses of the firm,

(iii) Value of closing stock for the year ended 31st March 2017 was undervalued by ₹3,000.

(iv) An annual insurance premium of (2,000 was not charged to Profit and Loss in any of the yea₹

You are required to calculate adjusted profits for all the years and the value of goodwill on the basis of two years purchase of average profits of last four yea₹

Q.9 A firm earned net profits during the last five years as follows :

Year ended 31st March	Profit (₹)
2016	14,000
2017	13,000
2018	16,000
2019	15,000
2020	12,000

The capital investment of the firm is (80,000. A fair return on capital in the market is 12%. Find out the value of goodwill of the business if it is based on three years' purchase of average super profits of the past five yea₹

Q.10 On April 1, 2021, an existing firm had assets of ₹1,50,000 including cash of ₹10,000. The partners' capital accounts showed a balance of ₹1,20,000 and reserves constituted the rest. If the normal rate of return is 10% and the goodwill of the firm is valued at ₹48,000 at 4 years' purchase of super profits, find out the average profits of the firm.

Q.11 A business has earned average profits of ₹24,000 during the last few years and the normal rate of return in a similar type of business is 12%. Ascertain the value of goodwill by capitalisation of average profits method, given that the value of net assets of the business is ₹1,40,000.

Q.12. A firm having the assets of (50,00,000 and liabilities of ₹22,00,000 earns annual profits of (4,80,000. The rate of normal profits being 15%. Calculate the amount of goodwill by capitalisation of super profit method.

Q.13 Calculate the value of goodwill of Nipun and Prisha using following information :

(i) At two years' purchase of Average Profit.

(ii) At two years' purchase of Super Profit.

(iii) On the basis of capitalisation of super profit.

(iv) On the basis of capitalisation of average profit.

It is given that : (a) Average Capital Employed is ₹12,00,000 (b) Profit for the firm for past three years : 2017— ₹1,80,000; 2018— ₹1,60,000; 2019— ₹2,60,000 (c) Normal rate of return is 10%. (d) Remuneration to each partner is ₹3,000 per month, (e) Assets—₹13,50,000 and liabilities ₹1,50,000.

Q.14 A business has earned average profits of ₹ 1,00,000 during the last few years and the normal rate of return in similar business is 10%. Find out the value of goodwill by

(i) Capitalisation of super profit method.

(ii) Super profit method, if the goodwill is valued at 3 years' purchase of super profit. The assets of the business were ₹ 10,00,000 and its external liabilities ₹ 1.80.000.

Q.15 On April 1, 2020 an existing firm had assets of ₹ 1,50,000 including cash ₹ 20,000. The Partners' Capital Accounts totaled ₹ 1,10,000 and the balance being the reserves. If the normal rate of return is 10% and the value of goodwill is valued at ₹ 36,000 at 4 years purchase of super profits, find out the average profits of the firm.

16. Calculate the value of Goodwill on the basis of three years' purchase of the average profit of the last five yea₹ The Profit/Losses were

Year ended 31s" March	Profit (₹)
2016	82,000
2017	70,000
2018	80,000
2019	Loss (32,000)
2020	40,000

During the year 2019-2020 there was a loss of ₹25,000 due to fire which was not accounted for while calculating the profit.

Work Sheet Answers

Q. NO.	ANSWER
7	₹ 64,000
8	₹1,04,250
9	₹ 13,200
10	₹ 27,000
11	₹ 60,000
12	₹ 4,00,000
13	i. ₹2,56,000; ii. ₹16,000 ; iii. ₹80,000; iv. ₹80,000
14	i. ₹1,80,000 ; ii. ₹ 54,000
15	₹ 24,000
16	₹ 1,44,000

CHAPTER 3

CHANGE IN PROFIT SHARING RATIO AMONG THE EXISTING PARTNERS

Meaning of Reconstitution of Partenrship firm	Whenever old partnership deed comes to an end and a new partnership deed is formed] it is called reconstitution of partnership firm] In other words any change in Existing agreement of partnerships is Reconstitution of Partneship"
When reconstitution of partnership takes place	Reconstitution of partnership takes place in the following circumstances: 1. Change in proft sharing ratio among existing partners- 2. Admission of a new partner 3. Retirement of an Existing partner 4. Death of a parnter 5. Amalgamation of two Partnership firms
What is the effect of change in profit sharing ratio?	It leads to dissolution of partnership and not the dissolution of the firm because the Existing partnership agreement ends and the new agreement comes into effect.
Issues which are to be dealt with at the time of change in profit sharing ratio	1. Determination of sacrificing ratio and gaining ratio- 2. Accounting treatment of Goodwill- 3. Accounting treatment of Reserves accumulated profits or losses. 4. Revaluation of Assests and reassessment liabilities. 5. Adjustment of Capital
Why do partner's change their profit sharing ratio	This may happen on account of a change in the existing partner's role in the firm
Sacrificing Ratio	The ratio in which one or more partners of the firm agree to sacrifice their share of profit in favour of one or more partners of the firm. Gaining Ratio = New Rato – Old Ratio
When is Sacrificing ratio computed?	1. In case of change in Profit sharing ratio 2. If there is admission of a new partner

Gaining Ratio	It is ratio in which one or more partners gain share of profit as a result of sacrificed share in profit by one or more partners of the firm Gaining Ratio = New Rato – Old Ratio
NEW PROFIT SHARING RATIO	The ratio in which the partners agree to share the profits in furture on reconstitution is known as new sharing ratio.
TREATMENT OF GOOD-WILL IN CASE OF CHANGE IN PROFIT SHARING RATIO	A) WHEN GOODWILLIS ADJUSTED THROUGH PARTNER'S CAPITAL ACCOUNTS
	i) In case of Fluctuating Capitals Gaining Partner's Capital Accounts Dr. To Sacrificing Partner's Capital Accounts (Being adustment made for goodwill on change in profit sharing ratio)
	ii) In case of Fixed Capitals Gaining Partner's Current Accounts Dr- To Sacrificing Partner's Current Accounts (Being adustment made for goodwill on change in profit sharing ratio)
	B) WHEN GOODWILL IS RAISED & WRITTEN OFF
	i) In case of Fluctuating Capitals Goodwill Account Dr. To Partner's Capital Accounts (Being the goodwill raised among partners in old ratio) Partner's Capital Accounts Dr. To Goodwill A/c (Being the goodwill written off among partners in new ratio)
	ii) In case of Fixed Capitals Goodwill Account Dr. To Partner's Current Accounts (Being the goodwill raised among partner's in old ratio) Partner's Current Accounts Dr. To Goodwill Account (Being the goodwill written off among partners in new ratio)

	C) WHEN EXISTING GOODWILL IS WRITTEN OFF
	All Partner's Capital Accounts/Current A/c Dr. To Goodwill Account (Being the goodwill written off among partners in old ratio)
TREATMENT OF RESERVES, ACCUMULATED PROFITS & LOSSES	Accumulated Profits include credit balance of P&L A/c, General Reserves, Resseve Fund, Workmen Compensation Reserve, Investment Fluctuation Reserve etc. Accumulated Losses include debit balance of P&LA/c, Deferred Revenue Expenditure i.e. Advertisement Suspense A/c.
	A) WHEN QUESTIONS SILENT OR WHEN ACCUMULATED PROFITS OR LOSSES ARE TO BE DISTRIBUTED OR WHEN ACCUMULATED PROFITS LOSSES ARE NOT TO BE SHOWN IN NEW BALANCE SHEET
	Contengency Reserve A/c Dr. Reserve Ac/ Dr. P&L A/c (Cr. Balance) Dr. Workmen Compensation Reserve A/c Dr. Investment Fluctuation Reserve A/c Dr. To all Partner's Capital A/cs (Being reserves & accumulate profits transferred to all partners in old ratio) All Partners Capital A/c Dr. To P&L A/c (Dr Balance) ToDefered Revenue exp. A/c
	B) WHEN ACCUMULATED PROFITS OR LOSSES ARE NOT TO BE DISTRIBUTED OR WHEN ACCUMULATAED PROFIT OR LOSSES ARE TO BE SHOWN IN NEWBALANCE SHEET AT SAME BOOK VALUE
	Calculate the net effect of Reserve Accumulated Profits & Losses- ₹ Reserves xx ACCUMULATED PROFITS xx Less ACCUMULATED LOSSES (xx) Net Effect +/–

	i) In case the Net Effect is Positive Gainng Partner's Capital/Current Accounts Dr. To Sacrificing Patner's Capital/Current Accounts **ii) In case the Net Effect is Negative** Sacrificing Partner's Capital/Current/Accounts Dr. To Gaining Patner's Capital/Current Accounts
TREATMENT OF WORKMEN COMPENSATION RESERVE	
CASE 1 When there is no Claim (if there is no information)	Workmen Compensation Reserve A/c Dr. To Partner's Capital/Current A/cs
CASE 2 WCC = WCR (equal	Workmen Compensation Reserve A/c Dr. To Provision's for workmen Compensation Claim A.c
CASE 3 WCC < WCR (less)	Workmen Compensation Reserve A/c Dr. To Provision for workmen Compensation Claim A/c To Partner's Capital/Current A/cs
CASE 4 WCC >WCR (more)	(i) Workmen Compensation Reserve A/c Dr. Revaluation A/c Dr. To Provision forWorkmen Compensation Claim A/c (ii) Partner's Capital/Current A/cs Dr. To Revaluation A/c

WCC stands for WORKMEN COMPENSATION CLAIM

WCR stands for WORKMEN COMPENSATION RESERVE

TREATMENT OF INVESTMENT FLUCTUATION RESERVE

CASE 1 BV = MV	Investment Fluctuation Reserve A/c Dr. To partner's Capital/Current A/cs
CASE 2 BV < MV	Investment Fluctuation Reserve A/c Dr- To Partner's Capital/Current A/cs (Entire reserve distributed in partner's old ratio) Investments A/c Dr. To Revaluation A/c (For increase in value of Investments) Revaluation A/c To Partner's Capital/Current A/cs

CASE 3 BV > MV	**i) When Fall in value is less than investment Fluctuation Reserve** Investment Fluctuation Reserve A/c Dr. To Investment A/c (BV-MV) To Partner's Capital/Current A/cs (In old ratio) **ii) When Fall in vaue is equal to Investment Fluctuation Reserve** Investment Fluctuation Reserve A/c Dr. To investment A/c **iii) When Fall in value is more than Investment Fluctuation Reserve** Investment Fluctuation Reserve A/c Dr. Revaluation A/c Dr. To Investment A/c
	Partner's Capital/Current A/cs Dr. To Revaluation A/c

BV stands for Book value of Investments
Mv Stands for Market vale of Investments

REVALUATION OFASSETS & REASSESSMENT OF LIABILITIES

It is a nominal account & prepared to revalue assets & reassess liabilities.

WHEN QUESTION IS SILENT OR A) WHEN REVISED VALUES OFASSETS & LIABILITIES ARE TO BE RECORDED

Revaluation A/c is prepared & Profit/Loss of revaluation is distributed among old partner's in old ratio

Dr. Revaluation A/c Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
to Asset (decrease in value)	xxx	By Asset (increase in value)	xxx
To Liability (increase in value)	xxx	By Liability (decrease in value)	xxx
To Unrecorded liability	xxx	By Unrecorded asset	xxx
To Profit (transferred to partner's capital account in old ratio	xxx	By Loss (transferred to partner's capital account in old ratio)	xxx
Total	xxx	Total	xxx

WHEN REVISED VALUES OFASSETS & LIABILITIES ARE NOT TO BE RECORDED (Assets & Liabilities will appear in Balnace Sheet at old Value)

Calculate the net effect of revaluation -------	₹
Increase in the value of Assests	xx
Add Decrease in the value of liabilities	xx
Less Decrease in the value of Assets	(xx)
Less Increase in the vaule of liablities	(xx)
Net Effect on Revaluation	**Gain/Loss**

For Gaining Partner = Share Gained × Net Effect on Revaluation

For Sacrificing Partner = Share Sacrificed × net Effect on Revaluation

i) In case the Net Effect is Gain on revaluation

Gaining Partner's Capital/Current Accounts Dr.

To Sacrificing Partner's Capital/Current Accounts

ii) In case the Net Effect is loss on revaluation

Sacrificing Partner's Capital/Current Accounts Dr.

To Gaining Partner's captial/current A/Cs

CHAPTER-4 RECONSTITUTION OF PARTNERSHIP
SACRIFICING & GAINING RATIO

Illustration 1) A, B & C ar Partners sharing profits in the ratio of 5 : 3 : 2. They decided to share profits in the future in the ration of 2:2:1 w.e.f 1st April 2019. Calculate Sacrificing & Gaining Ratio?

Solution:

Sacrificing ratio = Old ratio – New ratio

$$A = \frac{5}{10} - \frac{2}{5} = \frac{5-4}{10} = \frac{1}{10} \text{ Sacrifice}$$

$$B = \frac{3}{10} - \frac{2}{5} = \frac{3-4}{10} = \frac{-1}{10} \text{ Gain}$$

$$C = \frac{2}{10} - \frac{1}{5} = \frac{2-2}{10} = 0$$

TREATMENT OF GOOD WILL

Illustration 2. A, B & C are partners sharing profit & losses in the ratio of 5:4:1. It was decided that w.e.f. 15th April 2019. The profit sharing ratio will be 9:6:5.

Goodwill is to be valued at 2 years purchase of average profits of last 3 years profits. The profit for 2016-17, 2017-18 & 2018-19 were -₹ 42,000 & –₹ 48,000 & –₹ 60,000 respectively- Goodwill appears in the books at ₹ 10,000. Pass necessasry journal entries for the treatment of goodwill- Also give journal entries if goodwill is raised & writeen off.

Solution WHEN GOODWILL IS ADJUSTED THROUGH PARTNER'S CAPITAL

$$\textbf{Average Profit} = \frac{₹\ 42,000 + ₹\ 48,000 + ₹\ 60,000}{3} = ₹\ \mathbf{50,000}$$

Goodwill = ₹ **50,000** × 2 = ₹ **1,00,000**

Sacrificing/Gaining Ratio

$$A = \frac{5}{10} - \frac{9}{20} = \frac{10-9}{20} = \frac{1}{20} \quad \text{(Sacrifice)}$$

$$B = \frac{4}{10} - \frac{6}{20} = \frac{8-6}{20} = \frac{2}{20} \quad \text{(Sacrifice)}$$

$$C = \frac{1}{10} - \frac{5}{20} = \frac{2-5}{20} = \frac{-3}{20} \quad \text{(Gain)}$$

Journal

Date	Particulars	l.f	Dr.	
1st April 2019	A' Capital A/c Dr. B's Capital A/c Dr. C's Capital A/c Dr. To Goodwill A/c		5000 4000 1000	10,000
	(Being existing goodwill written off)			

Journal

Date	Particulars	l.f	Dr.	
1st April 2019	C's Capital A/c Dr. To A's Capital A/c To B's Capital A/c		15000	5,000 10,000
	(Being goodwill adjusted due to change in profit sharing			

WHEN GOODWILL IS RAISED & WRITTEN OFF

Journal

Date	Particulars	l.f	Dr.	
1st April 2019	Goodwill A/c Dr. To A's Capital A/c To B's Capital A/c To C's Capital A/c		1,00,000	 50,000 40,000 10,000
	(Being goodwill raised in old profit sharing ratio)			
1st April 2019	A's Capital A/c Dr. B's Capital A/c Dr. C's Capital A/c Dr. To goodwill A/c		45,000 30,000 25,000	 1,00,000
	(Being goodwill written off in new profit sharing ratio)			

TREATMENT OF RESERVES & LOSSES

Illustration 3) X, Y, Z are partners sharing profits & losses in the ratio of 5:3:2. They decide to share future profits & losses in the ratio of 2:3:5 w.e.f 1st April 2019

Following items appear in the balance sheet as on 31/3/18

General Reserve 75,000

Workmen Compensation Reserve ₹ 12,500

Profit & Loss Account ₹ 37,500

Advertisement Suspense A/c (Dr), ₹ 50,000

ii) Pass necessary journal entries

iii) Show the effect without affecting their book values by passing an adjustment entry.

Solution (i)

Journal

Date	Particulars	l.f	Dr.	Cr.
1st April	General Reserve A/c Dr.		75,000	
2019	Workmen Compensation		12,500	
	Reserve A/c Dr.		37,500	
	Profit & Loss Account Dr.			
	To X's Capital A/c			62,500
	To Y's Capital A/c			37,500
	To Z's Capital A/c			25,000
	(Being the reserves & profits transferred to odd partners int their old ratio)			
1st April	X's Capital A/c Dr.		25,000	
2019	Y's Capital A/c Dr.		15,000	
	Z's Capital A/c Dr.		10,000	
	To advertisement Suspense A/c			50,000
	(Being advertisement suspense transferred to lod partners in old ratio)			

ii) ADJUSTMENT ENTRY

1st April 2019	Z's Capital A/c Dr.	25,500	
	To x's Capital A/c		25,500
	(Being adjustment madr		
	for net reserves & losses)		

Here, Reserves & Losses will appear in Balance Sheet of New Firm as their old values

Working Notes

1) Calculation of Net Effect of Reserves & Profit

General Reserve	75,000
Workmen Compensation Resrve	12500
Profit & Loss A/c	37500
	1,25,000
	(50,000)
Less: Advertisement Suspense A/c (Dr.)	75,000

2) Calculation of Sacrificing/Gaining Ratio

$$X = \frac{5}{10} - \frac{2}{10} = \frac{3}{10} \quad \text{Sacrifice}$$

$$Y = \frac{3}{10} - \frac{3}{10} = 0 \quad \text{Sacrifice}$$

$$Z = \frac{2}{10} - \frac{5}{10} = \frac{-3}{10} \quad \text{Gain}$$

REVALUATION OF ASSETS & LIABILITIES

Illustration 4) Piyushm Pooja & Praveen are partners sharing Profits &losses in Ratio 3:3:2. Their balance sheet a on 31st March 2019 was as follows-

Liatilities	(₹)	Assets	(₹)
Sunday creditors Bank	48,000	Cash at bank	74,000
Bank Loan	72,000	Sundry debtors	88,000
Capital:		Stock	2,40,000
Piyush - 4,00,000	10,00,0000	Machinery	3,18,000
Pooja - 3,00,000		Building	4,00,000
Praveen- 3,00,000			
	11,20,000		11,20,000

Partners decided that with effect from April 1 2019 they would share profits and losses in the ratio of 4:3:2. It was agreed that:

(i) Stock be valued at (₹) 2,20,000.

(ii) Machinery is to be depreciated by 10%

(iii) A provision for doubtful debts is to be made on debrots at 5%

(iv) Building is to be appreciated by 20%

(v) A liability for (₹) 5,000 included in Sundry creditors is not likely to arise-Partners agreed that the revised values are to be recorded in the books- You are required to prepare journal revaluation account partner's capital Accounts and revised Balance Sheet.

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
1st	Revaluation A/c Dr.		56,200	
April	To Stock			20,000
2019	To Machinery			31,800
	To Provision for doubtful debts A/c			4,400
	(Revaluation of assets)			

1st April 2019	Building A/c Dr. Sundry creditor A/c Dr. To Revaluation A/c (Revaluation of assets and liabilities)		80,000 5,000	 8500
1st April 2019	Revaluation A/c Dr. To Piyush's capital A/c To Pooja's capital A/c To Praveen's capital A/c (Profit on revaluation)		28,800	 10,800 10,800 7,200

Dr. **Revaluation A/c**

Particulars	(₹)	Particulars	(₹)
To stock To Machinery To Provision for doubtful debts To profits transferred to capital accounts of: Piyush 10,800 Pooja 10,800 Praveen 7,200	20,000 31,800 4,400 28,800	By Building By Sundry creditors	80,000 5,000
	85,000		85,000

Dr. **Partner's Capital A/cs** **Cr.**

Particulars	Piyush	Pooja	Praveen	Particulars	Piyush	Pooja	Praveen
To balance	4,10,800	3,10,800	3,07,200	By bal. b/d by	40,00,000	3,00,000	3,00,000
				Revaluation	10,800	10,800	7,200
	4,10,800	3,10,800	3,07,200		4,10,800	3,10,800	3,07,200

Balance Sheet

As on April 1, 2019

Liabilites	(₹)	Assests	(₹)
Sundry creditiors Bank Loan Capital acconts Piyush 4,10,800 Pooja 3,10,800 Praveen 307200	43,000 72,000 1028800	Cash at bank Sundry debtors 88,000 Less: provision 5% (4,400) Stock Machninery Building	74,00 83,600 2,20,000 2,86,200 4,80,000
	11,43,800		11,43,800

Illustration 5- If in the above Illustration No&4 Partners agread that The revised values of assets & Liabilities are not to be shown the books- You are required to record the effect by passing a single journal entry- Also prepare the revised balance sheet.

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
2019 Apr. 1	Piyush's capital A/c Dr. To Pooja's capital A/c To Praveen's Capital A/c (Adjustment for profit on revaluation)		2,000	 1,200 800

Capital Accounts

Particulars	Piyush	Pooja	Praveen	Particulars	Piyush	Pooja	Praveen
To Pooja's Capital A/c To Praveen Capital A/c To Balance c/d	1,200 800 398,000	 3,01,200	 3,00,800	By bal. b/d by By Piyush's Capitial A/c	40,00,000	3,00,000 1,200	3,00,000 800
	4,00,000	3,01,200	3,00,800		4,00,000	3,01,200	3,00,800

Balance Sheet
As on April 1 2019
Balance Sheet of Piyush Pooja and Praveen

Liabilites	(₹)	Assets	(₹)
Sundry creditiors Bank Loan Capital account Piyush 3,98,000 Pooja 3,01,200 Praveen 3,00,800	48,000 72,000 10,00,000	Cash at bank Sundry debrors Stock Machinery Building	74,000 88,000 2,40,000 3,18,200 4,6000
	11,20,000		**11,20,000**

W.Note-1 Calculation of Gain due to revaluation

Building	80,000
Sundry Creditors	5,000
Total	85,000
Less Loss due to revaluation	
Of Stock	(20,000)
Machinery	(31,800)
Provision for Doubtfurl Debts	(4,400)
Net Gain	**28,800**

2. Calculation of Sacrificing / Gaining Ratio-

Piyush = $\frac{3}{8} - \frac{4}{9} = \frac{27-32}{72} = \frac{5}{72}$ (Gain)

Pooja = $\frac{3}{8} - \frac{3}{9} = \frac{27-24}{72} = \frac{3}{72}$ (Sacrifice)

Praveen = $\frac{2}{8} - \frac{2}{9} = \frac{18-16}{72} = \frac{2}{72}$ (Sacrifice)

Amount Sacrificed/Gained

Piyush =	28,800 × 5/72 =	(₹)	2000 Dr.
Pooja =	28,800 × 3/72 =	(₹)	1200 Cr.
Praveen =	28,800 × 2/72 =	(₹)	800 Cr.

Illustration 6) Bhavya and Sakshi are partners in a firm- Sharing prifits and losses in the ratio in the of 3 : 2 On 31st March-2018 their balance Sheet was as under.

Balance Sheet of Bhavya and Sakshi

Liabilites	(₹)	Assets	(₹)
Sundry Creditors	13,800	Furniture	16,000
General Reserve	23,400	Land and Building	56,000
Investment Fluetuation Fund	20,000	Investments	30,000
Bhavya's Capital	50,000	Trade Receivables	18,500
Sakshi's Capital	40,000	Cash in Hand	26,700
	1,47,200		**1,47,200**

The partners have decided to change their profit sharing ratio to 1:1 with immediate effect- For the purpose- they decided that:

a. Investment to be valued at (₹) 20,000

b. Goodwill of the firm valued at (₹) 24,000

c. General Reserve not to be distributed between the partners-

You are required to pass necessary journal entries in the goods of the firm-Show working-

Data	Particuars	L.F.	Amounts (₹)	Amounts (₹)
31.3.18	Investment Fluctuation Fund A/c		20,000	
	To Investment			10,000
	To Bhavya's Capital A/c			6,000
	To Sakshi's Capital A/c			4,000

	(Being Investment Fluctuation Fund adjusted against the Fluctuations in market Value and balance was distributed amongst partners)			
31.3.18	Sakshi's Capital A/c Dr. To Bhavya's Capital A/c (Being adjustment of goodwill made between partners due to change in profit sharing ratio between partners)		2,400	2,400
31.3.18	Sakshi's Capital A/c Dr. To Bhavya's Capital A./c (Being Genrral Reserve adjusted among the partners without writing it off)		2340	2340

Sacrificing ratio = old ratio & new ratio

Bhavya's = 3/5 – 1/2 = 1/10 Sacrifice

Sakshi's = 2/5 – 1/2 = (1/10) Gain

Change in Profit sharing ratio

7. A, B and C sharing profits and losses in the ratio of 4 : 3 : 2, decide to share future profits and losses in the ratio of 2 : 3 : 4 with effect from 1st April, 2018. An extract of their Balance Sheet as at 31st March, 2020 is as follows:

Liabilities	**Assets**
Workmen Compensation Reserve 63,000	

Show the accounting treatment under the following alternative cases:

Case 1: If there is no claim made against Workmen Compensation Reserve.

Case 2: If a claim on account of workmen compensation is estimated at 18,000.

Case 3: If claim on account of workmen compensation reserve is exactly 63,000.

Case 4: If claim on account of workmen compensation reserve is 72,000,

Solution:

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2020	**Case 1**			
1 April	Workmen Compensation Reserve A/c Dr.		63,000	
	To A's Capital A/c			28,000
	To B's Capital A/c			21,000
	To C's Capital A/c			14,000
	(Being the transfer of workmen compensation reserve to partners' capital accounts in their old profit-sharing ratio)			
2020	**Case 2**			
1 April	Workmen Compensation Reserve A/c Dr.		63,000	
	To Provision for Workmen Compensation Claim A/c			18,000
	To A's Capital A/c			20,000
	To B's Capital A/c			15,000
	To C's Capital A/c			10,000
	(Being the transfer of surplus workmen compensation reserve to partners' capital accounts in their old profit-sharing ratio)			
2020	**Case 3**			
1 April	Workmen Compensation Reserve A/c Dr.		63,000	
	To Provision for Workmen Compensation Claim A/c			63,000
	(Being amount for workmen compensation claim provided for)			
2020	**Case 4**			
1 April	Workmen Compensation Reserve A/c Dr.		63,000	
	Revaluation A/c Dr.		9,000	
	To Provision for Workmen Compensation Claim A/c			72,000
	(Being amount provided for workmen compensation claim)			
1 April	A's Capital A/c Dr.		4,000	
	B's Capital A/c Dr.		3,000	
	C's Capital A/c Dr.		2,000	
	To Revaluation A/c			9,000
	(Being loss on revaluation transferred partners capital accounts in old ratio)			

8. A, B and C are sharing profits and losses in the ratio of 4 : 3 : 2, decided to share future profits and losses inn the ratio of 2 : 3 : 4 with effect from 1st April, 2018.

An extract of their Balance Sheet as at 31st March, 2020 is:

Liabilities	Assets
Investments Fluctuation Reserve 18,0000.	Investments (At cost) 2,00,000

Case 1: If there is nor additional information.

Case 2: If the market value of investments is ₹ 2,00,000.

Case 3: If the market value of investment is ₹ 1,91,000.

Case 4: If the market value of investment is ₹ 2,18,000.

Case 5: If the market value of investments is ₹ 1,73,000.

Solution.

Journal

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2020	**Case 1**			
1 April	Investment Fluctuation Reserve A/c Dr.		18,000	
	To A's Capital A/c			8,000
	To B's Capital A/c			6,000
	To C's Capital A/c			4,000
	(Being the transfer of excess Investment Fluctuation Reserve to Partners' Capital Accounts in their old profit-sharing ratio)			
2020	**Case 2**			
1 April	Investment Fluctuation Reserve A/c Dr.		18,000	
	To A's Capital A/c			8,000
	To B's Capital A/c			6,000
	To C's Capital A/c			4,000
	(Being the transfer of excess Investment Fluctuation Reserve to Partners' Capital Accounts in their old profit-sharing ratio)			
2020	**Case 3**			
1 April	Investment Fluctuation Reserve A/c Dr.		18,000	
	To Investments A/c			9,000
	To A's Capital A/c			4,000
	To B's Capital A/c			3,000
	To C's Capital A/c			2,000
	(Being the transfer of excess Investments Fluctuation Reserve to Partners' Capital Accounts in their old profit-sharing ratio)			

2020	**Case 4**			
1 April	Investments Fluctuation Reserve A/c Dr.		18,000	
	To A's Capital A/c			8,000
	To B's Capital A/c			6,000
	To C's Capital A/c			4,000
	(Being the transfer of excess Investments Fluctuation Reserve to Partners' Capital Accounts in their old profit-sharing ratio)			
1 April	Investment A/c Dr.		18,000	
	To Revaluation A//c			18,000
	(Being the value of Investment brought up to market value)			
1 April	Revaluation A/c Dr.		18,000	
	To A's Capital A/c			8,000
	To B's Capital A/c			6,000
	To C's Capital A/c			4,000
	(Being the transfer of gain (profit) on revaluation)			
2020	**Case 5**			
1 April	Investments Fluctuation Reserve A/c Dr.		18,000	
	Revaluation A/c Dr.		9,000	
	To Investment A/c			27,000
	(Being the fall in value of investment adjusted through Investments Fluctuation Reserve and shortfall charged to Revaluation Account)			
1 April	A's Capital A/c Dr.		4,000	
	B's Capital A/c Dr.		3,000	
	C's Capital A/c Dr.		2,000	
	To Revaluation A/c			9,000

9. A, B and C are partners sharing profits and losses in the ratio of 5 : 3 : 2. Their Balance Sheet as at 31st March, 2019 stood as follows:

Liabilities		Amount (₹)	Assets	Amount (₹)
Capital A/c			Land and Building	3,50,000
A	2,50,000		Machinery	2,40,000
B	2,50,000		Computers	70,000

C 2,00,000	7,00,00	Investments (Market value ₹ 90,000)	1,00,000
General Reserve	60,000	Sundry Debtors	50,000
Investments Fluctuation Reserve	30,000	Cash in Hand	10,000
Sundry Creditors	90,000	Cash at Bank	55,000
		Advertisement Suspense	5,000
	8,80,000		8,80,000

They decided to share profits equally w.e.f 1st April, 2019. They also agreed that:

(i) Value of Land and Building be decreased by 5%.

(ii) value of Machinery be increased by 5%.

(iii) A Provision for Doubtful Debts be created @ 5% on Sunday debtors.

(iv) A Motor Cycle valued at ₹ 20,000 was unrecorded and is not to be recorded in the books.

(v) Out of Sundry Creditors ₹ 10,000 is not payable.

(vi) Goodwill is to be valued at 2 years' purchase of last 3 years profits. Profits being for 2018-19 ₹ 50,000 (Loss); 2017-18 ₹ 2,50,000 and 2016-17 ₹ 2,50,000.

(vii) C was to carry out the work for reconstituting the firm at a remuneration (including expenses) of ₹ 5,000 which was paid by cheque. Expenses came to ₹ 3,000.

Pass Journal entries and prepare Revaluation Account.

Journal

Date	Particulars		L.F.	Dr. Amount (₹)	Cr. Amount (₹)
2019 April1	General Reserve A/c	Dr.		60,000	
	To A's Capital A/c				30,000
	To B's Capital A/c				18,000
	To C's Capital A/c				12,000
	(Reserve distributed)				
	A's Capital A/c	Dr.		2,500	
	B's Capital A/c	Dr.		1,500	
	C's Capital A/c	Dr.		1,000	
	To Advertisement Suspense A/c				5,000
	(Advertisement Suspense distributed)				

	Investment Fluctuation Reserve A/c Dr.		30,000	
	To Investment A/c			10,000
	To A's Capital A/c			10,000
	To B's Capital A/c			6,000
	To C's Capital A/c			4,000
	(Investment Fluctuation Reserve distributed)			
	Machinery A/c Dr.		12,000	
	Motor Cycle A/c Dr.		20,000	
	Creditors A/c Dr.		10,000	
	To Revaluation A/c			42,000
	(Assets revalued)			
	Revaluation A/c Dr.		25,000	
	To Land and Building A/c			17,500
	To Provision for doubtful debts A/c			2,500
	To Bank A/c (Recreation)			5,000
	Revaluation A/c Dr.		17,000	
	To A's Capital A/c			8,500
	To B's Capital A/c			5,100
	To C's Capital A/c`			3,400
	(Profit on revaluation transferred to Partners' Capital A/c)			
	B's Capital A/c Dr.		10,000	
	C's Capital A/c Dr.		40,000	
	To A's Capital A/c			50,000
	(Goodwill Adjusted)			

Dr. Revaluation A/c Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
Land & Building A/c	17,500	Machinery A/c	12,000
Provision for Doubtful Debts A/c	2,500	Motor Cycle A/c	20,000
Bank A/c (Remuneration)	5,000	Creditors A/c	10,000
Profit transferred to:			
A 8,500			
B 5,100			
C 3,400	17,000		
	42,000		42,000

Working Notes:

WN 1: Calculation of sacrifice or gain

A : B : C = 5 : 3 : 2 (Old Ratio)

A : B : C = 1 : 1 : 1 (New Ratio)

Sacrificing (or Gaining Ratio) = Old ratio – New Ratio

A's Share = 5/10 – 1/3 = 5/20 (Sacrifice)

B's Share = 3/10 – 13 = 1/30 (Gain)

C's Share = 2/10 – 1/3 = 4/30 (Gain)

WN 2: Valuation of Goodwill

Goodwill = Average Profit × No. of years' Purchase

= 1,50,000 × 2 = ₹ 3,00,000

Goodwill = Average Profit × No. of years' Purchase

= 1,50,000 × 2 = ₹ 3,00,000

WN 3: Adjustment of Goodwill

Amount credited to A's Capital A/c = 3,00,000 × 5/30 = ₹ 50,000

Amount debited to B's Capital A/c = 3,00,000 × 1/30 = ₹ 10,000

Amount debited to C's Capital A/c = 3,00,000 × 4/30 = ₹ 40,000

10. Parth, Raman and Zaisha are partners in a firm manufacturing furniture. They have been sharing profits and losses in the ratio of 5 : 3 : 2. From 1st April, 2017 they decided to share future profits and losses in the ratio of 2 : 5 : 3. Their Balance Sheet showed a debit balance of ₹ 4,000 in Profit & Loss Account; balance of ₹ 36,000 in General Reserve and a balance of ₹ 12,000 in Workmen's Compensation Reserve. It was agreed that:

(i) The goodwill of the firm be valued at ₹ 76,000.

(ii) The Stock (book value of ₹ 40,000) was to be depreciated by 8%.

(iii) Creditors amounting to ₹ 900 were not likely to be claimed.

(iv) Claim on account of Workmen's Compensation amounted to ₹ 20,000.

(v) Investments (book value ₹ 38,000) were revalued at ₹ 40,000.

Pass necessary Journal Entries for the above

Solution.

Books of the Parth, Raman And Zaisha

Journal Entires

Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2017 April 1	Parth's Capital A/c Dr.		2,000	
	Raman's Capital A/c Dr.		1,200	

	Zaisha's Capital A/c Dr.		800	
	To P & L A/c			4,000
	(Being Debit balance of P & L A/c Distributed in old ratio)			
April 1	General Reserve A/c Dr.		36,000	
	To Parth's Capital A/c			18,000
	To Raman's Capital A/c			10,800
	To Zaisha's Capital A/c			7,200
	(Being General Reserve distributed in old ratio)			
April 1	Revaluation A/c Dr.		8,000	
	Workmen's Compensation Reserve A/c Dr.		12,000	
	To Provision for Workmen's Compensation Claim A/c			20,000
	(Being Liability created for workmen's compensation claim)			
April 1	Revaluation A/c Dr.		3,200	
	To Stock A/c			3,200
	(Being decrease in value of stock)			
April 1	Investments A/c Dr.		2,000	
	Creditors A/c Dr.		900	
	To Revaluation A/c			2,900
	(Being increase in value of investments and amount not likely to be claimed by creditors)			
April 1	Parth's Capital A/c Dr.		4,150	
	Rman's Capital A/c Dr.		2,490	
	Zaisha's Capital Ac Dr.		1,660	
	To Revaluation A/c			8,300
	(Being Loss on Revaluation transferred in old ratio)			
April 1	Raman's Capital A/c (2/10 of 76,000) Dr.		15,200	
	Zaisha's Capital A/c (1/10 of 76,000) Dr.		7,600	
	To Parth's Capital A/c (3/10 of 76,000)			22,800

Working Notes:

(i) Revaluation A/c Debited with 8,000 + 3,200 11,200

Revaluation A/c Credited with 2,900

Therefore, Loss on Revaluation 8,300

(ii) Calculation of Sacrifice or Gain

Old Ratio 5 : 3 : 2 New Ratio 2 : 5 : 3

Parth:	$\frac{5}{10}$	$\frac{3}{10}$	$\frac{2}{10}$	Sacrifice
Raman:	$\frac{2}{10}$	$\frac{3}{10}$	$\frac{1}{10}$	Gain
Zaisha:	$\frac{2}{10}$	$\frac{3}{10}$	$\frac{1}{10}$	Gain

Practice Exercise

Que.1) A, B, C are partners in a firm sharing profit in the ratio 5:3:2. They agreed to share profite losses equally w-e-f- 1st April 2019- Goodwill if the firm is valued at (₹) 90,000 Pass necessory Jorunal entry.

Que. 2) Keshav, Meenakshi & Mohit are parteners sharing Profits & losses in the ratio of 1:2:2 have decided to share future profit equally w.e.f. 1St April 2019. On that date] General Reserve Showed a balance of (₹) 2,40,000 Partners do not want to distribute the reserves pass necessary adjusting entry.

Que. 3) P, Q & R are partners sharing Profits equally- they decided that in future R will get 1/5th share in profit & remaining profit will be shared by P & Q equally. On the day of change] firm's goodwill is valued at (₹) 60,000- Deferred revenue expenditure was (₹) 4000 & balance in profit & loos A/c (Dr) Was (₹) 8000.

Give journal entrires arising on account of change in profit sharing ratio without disturbing the balance sheet.

Que. 4) P, Q, R & S were partners in af firm sharing profits in the ratio of 1:4:2:3. on 1stth April 2019, their balance sheet was as following.

Balance Sheet as on 1/4/19

Liabilities	Amt. (₹)	Assets	Amt. (₹)
Capitals-		Fixed Assets	12,70,000
P 200000		Current Assets	5,30,000
Q 300000			
R 400000			
S 500000	14,00,000		
Sundry Creditors	2,,30,000		
Workman Compensation Reserve	1,70,000		
	18,00,000		18,00,000

From the above date the partners decided to share the future profits equally.

For this purpose the goodwill of the firm was valued at ₹ 2,70,000

The partners also agreed for the following -

(1) The claim against workmen compensation reserve was estimated at ₹ 2,00,000

(2) Capitals of the partners was to be adjusted according to the new profit sharing ratio by opening Partners Current A/c

Prepare Revaluation A/c Partners Capital Account & the Balance Sheet of the reconstituted firm

Ques 5 Om, Jai, Jagdish are partner's sharing profits & losses in the ratio of 5:4:1. Their Balance sheet as at 31/03/2019 was as follows.

Liabilities		Amt. (₹)	Assets	Amt. (₹)
Sundry Criditors		1,10,000	Cash at Bank	2,10,000
Salaries Payable			Sundry Debtors 1,00,000	90,000
Outstanding Expenses		30,000	Less for D/d	(10,000)
General Reserve Capital A/cs		10,000	Stock	50,000
			Furniture	40,000
OM	3,00,000	40,000	Computers	2,00,000
Jai	1,50,000		Cars	2,00,000
Jagdish	1,50,000	7,90,000		
				7,90,000

Profit sharing ratio w.e.f Ist April 2019 was decided to be equal following was also agreed among the partners;

(1) Stock to be reduced to ₹ 40,000

(2) Provision for D/d to be written back, Since al debtors are good-

(3) Computers to be reduced by ₹ 20,000

(4) Out of the salaries Payable, ₹ 10,000 was not payable

(5) Outstanding expenises were not payable

(6) An unrecorded asset (motor cycle) valued at ₹ 10,000 to be accounted

(7) Goodwill of the firm was valued at ₹ 50,000

(8) Total Capita of the firm ₹ 6,00,000 was to be in profit sharing ratio excess capital to be withdrawn & short to be made good-

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

Ques 6. P, Q and R partners in a firm sharing profits and losses in the ratio 3:3:2. Their Balance Sheet as at 31st March 2016 was:

Liablities	(₹)	Asset	(₹)
Sundry Creditors	24,000	Cash at Bank	27,000
General Reserve	36,000	Sundry Debtors	50,000
Capital A/cs	5,00,000	stock	1,20,000
P 2,00,000		Machinery	1,59,000
Q 2,00,000		Building	2,00,000
R 1,00,000		Advertisement Expenditure	4,000
	5,60,000		5,60,000

Partners decided that with effect from 1st April, 2016, they would share profits and losses in the ratio of 4:3:2. It was agreed that:

(i) Stock is to be valued at (₹) 1,10,000

(ii) Machinery is to be depriciated by 10%

(iii) A provision for doubtful debts is to be made on debtors @ 5%.

(iv) Building to be appreciated by 20%

(v) A liability for (₹) 3000 included in Sundry Creditors are not likely to arise.

Partners agreed that revised values of assets and liablities are to be recorded in the books They decided to retain the General Reserve in the books. Find missing figures in Journal.

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
2016	Revaluation A/c		(a)	
April	To Stock			(b)
1	To Machinery A/c			(c)
	To Provision for Doubtful Debt A/c			(d)
	(For Decrease in the value of assets and provisions made for D/D)			
April	Building A/c Dr.		(e)	
1	Creditors A/c Dr.		(f)	
	To Revaluation A/c			(g)
	(For increase in the value of assets and decrease in the value of liablities)			

April 1	Ps Capital A/c Dr. To Qs Capital A.c To Rs Capital A/c (for transferring profit on revaluation to the capital A/c of partners in old profit sharing ratio		(j)	
April 1	P's Capital A/c Dr. Q's Capital A/c Dr. R's Capital A/c Dr. To (n) (For tranfer of advertisement expenditure to all partners		(k) (l) (m)	

CHAPTER-4 CHANGE IN PROFIT SHARING RATIO
(MCQs) AMONG THE EXISTING PARTNERS

Que-1) A,B & C are partners sharing profits in the ratio of 4:3:2, decided to share profit equally Goodwill of the firm is valued at (₹) 10,800. Good adjusting entry will then be:

a) A's Capital A/c Cr. by (₹) 4800; B's Capital A/c Cr. by (₹) 3600; C's Capital A/c Cr. by (₹) 2400
b) A's Capital A/c Cr. by (₹) 3600; B's Capital A/c Cr. by (₹) 3600; C's Capital A/c Cr. by (₹) 2400
c) A's Capital A/c Cr-.by (₹) 1200; C's Capital A/c Cr. by (₹) 1200;
d) A's Capital A/c Cr. by (₹) 1200; C's Capital A/c Dr. by (₹) 1200;

Que. 2 X, Y & Z are partners sharing profit in the ratio of 1:2:3 On April 1st, 2019, they deicided to share the profite equally on that date there was a credit balance of (₹) 1,20,000 in Their profit & Loss Account & a balance of (₹) 1,80,000 in General Reserve Account. Instead of closing the Gereral Reserve

Account & Profit and Loss Account, it is decided to record on adjustment entry which will be

a) Dr. A by (₹) 50,000; Cr. B by (₹) 50,000
b) Dr. A by (₹) 50,000; Cr C by (₹) 50m,000
c) Cr. A by (₹) 50,000; Dr. B by (₹) 50,000
d) Cr. A by (₹) 50,000; Dr. C by (₹) 50,000

Que. 3 A B & C are partners sharing profits are losses in the ratio of 4:3:2, decided to share future profit & losses in the ratio of 2:3:4, w.e.f. 1st April.2019. Workmen Compensation Reserve appearing in the balance sheet is (₹) 45,000 & a claim on account5 of Workmen Conpensation is estimated at (₹) 54,000. Then-

a) (₹) 9000 is distributed amongst partner in old profit sharing ratio

b) (₹) 9000 is distributed amongst partner in new profit sharing ratio

c) (₹) 9000 is shown as provision in revalvation A/c

d) (₹) 9000 is distributed amongst partner in their Capital ratio.

Que. 4) Any change in the relationship of Existing partners Which results in an end of the eñisting agreement and enforces making of a new agreement is called

a) Revaluation of Partnership

b) Reconstitution of Partnership

c) Realization of Partnership

d) None of the Above.

Que. 5) A, B, & C are partners sharing ratio profits in the ratio of 5:3:2. They decided to share furture profits is the ratio of 2:3:5 w.e.f 1st April/2019. They also decide to record the effect of following revaluation without affecting the book values of assets & liabilities by passing single adjusting entry:

	Book Value (₹)	Revised Value (₹)
Land & Building	7,00,000	8,50,000
Stock	2,50,000	2,20,000
Sundry Crditor's	3,50,000	3,35,000
Outstanding Rent	2,35,000	2,80,000

The Single Adjustment entry will be

a) Dr. C by (₹) 27000; Cr. A by (₹) 27000;

b) Dr. A by (₹) 27000; Cr. C by (₹) 27000;

c) Cr. B by (₹) 27000; Cr. A by (₹) 27000;

d) Dr A by (₹) 27000; Cr. B by (₹) 27000;

Answers to MCQ

1. (d)
2. (b)
3. (c)
4. (b)
5. (a)

Answers to Practice Exercise

Q.1	B's Capital A/c	Dr 3000
	C's Capital A/c	Dr 12000
	To A's Capital Ac	15,000

Q.2.	Keshav's Capital A/c	Dr. 32000		
	To Meenakshi's Capital A/c 16000			
	To Mohit's Capital A/c	16000		
Q.3.	R's Capital	6,400		
	To P's Capital A/c	3200		
	To Q's Capital A/c	3200		
Q.4.	Loss of Revaluation	= ₹ 30,000		
	P's Currentl A/c (Dr)	₹ 18600		
	Q's Current A/c (Dr)	₹ 14000		
	R's Current A/c	₹ 38000		
	R's Current A/c	₹ 1,62,000		
Q.5	Gain of Revaluation A/c = ₹ 10,000			
	Om, Jai, Jagdish Cap A/c = ₹ 2,00,000 each			
	Shortage of Capital for Jai = ₹ 26,666			
	Shortage of Capital for Jagdish = ₹ 56,667			
	Surplus of Capital for Om = ₹ 1,33,333			
Q.6	a) 28, 400	b) 10,000	c) 15,900	d) 2,500
	e) 40,000	f) 3,000	g) 43,000	h) 43,000
	i) 5,475	j) 5,475	k) 3,650	l) 1,500
	m) 1,500	n) 1,000	o) 4,000	

Change in Profit sharing ratio

1. Given below are two statements, one labeled as Assertion (A) and the other labelled as Reason (R):

Assertion (A): One of the forms of reconstitution of the firm is Change in Profit Sharing Ratio among Existing Partners.

Reason (R): Here there is no change in the partners carrying on the business of the firm.

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong

(b) Both (A) and (R) are correct.

(c) (A) is wrong, but (R) is correct.

(D) Both (A) and (R) are wrong

2. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R).

Assertion (A): Change in Profit Sharing Ratio among Existing Partners may result in the gain to a few partners and loss to others.

Reason (R): Without any admission or retirement of the partner, sometimes the partners may decide to change their existing profit sharing ratio.

In the context of the above two statements, which of the following is correct?

Codes

(a) Both (A) and (R) are correct and (R) is the correct reason of (A)

(b) Both (A) and (R) are correct but (R) is not the correct reason of (A).

(c) Only (R) is correct

(d) Both (A) and (R) are wrong

3. Given below are two statements, one labeled as Assertion (A) and the other labeled at Reason (R)

Assertion (A): Reconstitution of partnership means a change in existing agreement Ie mutual terms and conditions among partners.

Reason (R): As a result, an old agreement among the partners comes to an end and a new agreement comes into existence.

Codes

(a) Both (A) and (R) are true, but (R) is not the explanation of (A)

(b) Both(A) and (R) are true and (R) is a correct explanation of (A).

(c) Both (A) and (R) are false

(d) (A) is false, but (H) is true.

4. Given below are two statements, one labelled as Assertion (A) and the other labelled as Reason (R)

Assertion (A): Gaining Ratio = New Ratio - Old Ratio

Reason (R): As a result of change in profit sharing ratio, one or more of the existing partners gain some portion of other partner's share of profit.

In the context of the above statements, which one of the following is correct?

Codes:

(a) (A) is correct, but (R) is wrong.

(b) Both (A) and (R) are correct

(c) (A) is wrong, but (R) is correct

(d) Both (A) and (R) are wrong

ANSWER

Q. No.	Answer
1.	(b)
2.	(b)
3.	(b)
4.	(b)

Change in Profit sharing ratio

MCQ

1. A, B and C are partners sharing profits in the ratio of 4 : 3 : 2 decided to share profits equally. Goodwill of the firm is valued at ₹ 10,800. In adjusting entry for goodwill.

(a) A's Capital A/c Cr. by ₹4,800 B's Capital A/c Cr. by ₹3,600; C's Capital A/c Cr. by ₹2,400.

(b) A's Capital A/c Cr. by ₹3,600 B's Capital A/c Cr. by ₹3,600; C's Capital A/c Cr. by ₹3,600.

(c) A's Capital A/c Dr. by ₹1,200 B's Capital A/c Cr. by ₹1,200;

(d) A's Capital A/c Cr. by ₹1,200 B's Capital A/c Dr. by ₹1,200;

2. A, B and C are partners in a firm sharing profits in the ratio of 3 : 4 : 1. They decided to share profits equally w.e.f 1st April, 2019. On that date the Profit and Loss Account showed the credit balance of ₹ 96,000. Instead of closing the Profit and Loss Account, it was decided to record an adjustment entry reflecting the change in profit sharing ratio In the journal entry.

(a) Dr. A by ₹4,000 Dr. B by ₹16.000 Cr. C by ₹20,000

(b) Cr. A by ₹4,000 Dr. B by ₹16.000 Cr. C by ₹20,000

(c) Cr. A by ₹16,000 Cr. B by ₹4,000 Dr. C by ₹20,000

(d) Dr. A by ₹16,000 Dr. B by ₹4,000 Cr. C by ₹20,000

3. X, Y and Z are partners in a firm sharing profits in the ratio 4 : 3 : 2 Their Balance Sheet as at 31-3-2019 showed a debit balance of Profit & Loss A/c ₹180,000 From 1-4-2019 they will share profits equally In the necessary joumal entry to give effect to the above arrangement when A Y and Z decided not to close the Profit & Loss Account

(a) Dr. X by ₹20,000 Cr. Z by ₹20,000

(b) Cr. X by ₹20,000 Dr. Z by ₹20,000

(c) Dr. X by ₹40,000, Cr. Z by ₹40,000

(d) Cr. X by ₹40,000 Dr. Z by ₹40,000

4. X, Y and Z are partners sharing profits and losses in the ratio 5 : 3 : 2. They decide to share the future profits in the ratio 3 : 2 : 1 Workmen compensation reserve appearing in the balance sheet on the date if no information is available for the same will be:

(a) Distributed to the partners in old profit sharing ratio

(b) Distributed to the partners in new profit sharing ratio

(c) Distributed to the partners in capital ratio

(d) Camed forward to new balance sheet without any adjustment

5. Any change in the relationship of existing partners which results in an end of the existing agreement and enforces making of a new agreement is called

(a) Revaluation of partnership

(b) Reconstitution of partnership.

(c) Realization of partnership.

(d) Rearrangement of partnership.

ANSWER

Q. No.	**Answer**
1.	(d)
2.	(b)
3.	(a)
4.	(a)
5.	(b)

Case Study Based Questions

Change In Profit Sharing Ratio

Read the following paragraph and answer the following Question from 1 to 4.

Bhavya and Naman were partner in a firm carrying on a tiffin service in Hyderabad Bhavya noticed that a lot of food is left at the end of the day. To avoid wastage, the suggested that it can be distributed to the needy Naman wanted that it should be mixed with the food being served the next day. Naman then give a advice that if his share in the profit increased, he will not mind free distribution of leftover food. Bhavya happily agreed. So they decided to change their profit sharing ratio 1:2 with immediate effect On that date revaluation of assets and reassessment of liability was carried out that resulted into a gain of ₹18,000. On that day at the Goodwill of the firm was valued at its ₹1,20,000

Based on the above information you are required to answer the following questions.

1. sacrificing ratio equal to:

(A) Old ratio minus new ratio

(B) New share minus old share

(C) Old share plus new share

(d) Old share

2. sacrificing/gain of Bhavya and Naman will be

(a) Bhavya sacrifice 1/6, Naman gains 1/6

(b) Bhavya gains 1/6, Naman sacrifice 1/6

(c) Only Bhavya gains 1/6

(d) Only Naman sacrifice 1/6

3. at the time of change in profit sharing ratio gaining partner capital account is .... sacrificing partner is ...... For the adjustment of goodwill

(a) Credited debited

(b) Debited credited

(d) Increased or decreased

(d) Decreased or increased

4. Pass the journal entry for adjustment of Goowill.

(a) Naman's Capital a/c Dr. 1,20,000 To Bhavya's Capital a/c 1,20,000

(b) Bhavya's Capital a/c Dr. 60,000 To Bhavya's Capital a/c 60,000

(d) Naman's Capital a/c Dr. 20,000 To Bhavya's Capital a/c 20,000

(d) Naman's Capital a/c Dr. 1,00,000 To Bhavya's Capital a/c 1,00,000

ANSWER

Q. No.	**Answer**
1.	(a) Old ratio minus new ratio
2.	(a) Bhavya sacrifice 1/6, Naman gains 1/6
3.	(b) Debited credited
4.	(a) Naman's Capital a/c Dr. 20,000 To Bhavya's Capital a/c 20,000

CHAPTER 4

ADMISSION OF A NEW PARTNER

Why a new partner is admitted?	A new partner may be admitted when the firm needs a. Additional Capital b. Managerial Help c. Both
How can a new partner be admitted?	Unless it is otherwise provided in the partnership deed a new partner can be admitted only when the existing partners unanimously agree for it.
Two main Rights acquired by a newly admitted partner	1. Right to share the assets of the partnership firm. 2. Right to share the profits of the partnership firm and Right to participate in the business activity
What does a new partner bring to acquire the rights?	To acquire share in the assets and profits of the firm, the partner brings 1. An agreed amount of Capital either in Cash or kind and / or some technical skill 2. Additional amount known as premium of Goodwill
Why is new partner required to bring premium?	This is due to compensate the existing partners for loss of their Share in the Super Profits of the firm. When a person pays for Goodwill, he pays for sacrifice of the profits by old partner
New profit sharing ratio and sacrificing ratio	The ratio in which all partners, including new partner will share future profits losses of the firm is known as new profit sharing ratio. Sacrificing ratio is the ratio in which old or existing partners forego their share of profit in favour of the new partner.

	New Profit Sharing Ratio and Sacrificing Ratio
When share of new partner is given but sacrifice made by old partners is not given	(i) Deduct the new partner's share from 1 (ii) Divide the remaining share among old partner in old profit sharing ratio. **Sacrificing Ratio** is same as that of **Old Profit Sharing Ratio.**
When share of new partner is given and new share of old partner is given	(i) Deduct the new partners' share from 1 (ii) Divide the remaining share among old partner in new profit sharing ratio. Sacrificing share = Old share – New share
When new partner acquires his share from old partners' equally or in particular ratio.	(i) Deduct the sacrifice made in favour of new partner from the old share of old partne₹ (ii) Share surrendered by old partners is added to calculate new partner share.
When existing partner retains his original share on admission of a partner	(i) Deduct the new partners' share and share of existing partner (who retains his old share) from 1 (ii) Divide the remaining share among old partner in profit sharing ratio.

Treatment of Goodwill in case of Admission of a Partner	**When Goodwill is Paid Privately**	**No Entry**
	When goodwill is brought in cash or cheque by new partner and retained in the firm	Cash / Bank A/c Dr. To new partner' capital A/c To premium for goodwill A/c (Being capital and premium for goodwill brought in) **Premium for Goodwill A/c Dr.** **To Sacrificing Partners' Capital/Current A/cs** (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio) "Current A/c incase of Fixed capitals"
	When Goodwill is brought in cash or cheque by new	**Cash/Bank A/c Dr.** **To New partners' CapitalA/c** **To premium for Goodwill A/c**
	Partner and Withdrawn by sacrificing partners	(Being capital and premium for goodwill brought in) **Premium for Goodwill A/c Dr.** To sacrificing Partners Capital / Current A/cs (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio) **Sacrificing Partners' Capital / Current A/Cs Dr.** **To Cash / Bank A/c** (Being withdrawal of premium by the partners)
		Current A/C in case of Fixed capitals

	When Goodwill is Brought in Kind	Asset A/c To New Partners' Capital A/c To Premium for Goodwill A/c To Liabilities A/c (Being asset contributed as capital and premium for goodwill) **Premium for Goodwill A/c Dr.** To sacrificing Partners' Capital / Current A/cs (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio) "Current A/c in case of Fixed capitals"
	When Goodwill is not Brought in Full or Part by the New Partner (In case Goodwill is not Raised)	**Cash / Bank A/c Dr.** **To new Partners' Capital A/c** **To Premium for Goodwill A/c** (with share of goodwill brought in) (Being capital and premium for goodwill brought in) Premium for Goodwill A/c (with paid share of goodwill) Dr. Incoming partners' Current A/c (with unpaid share of goodwill) Dr. **To sacrificing partners' Capital / Current A/cs** (Being premium for goodwill is distributed among sacrificing partners's in sacrificing ratio) "Sacrificing partners current A/c in case of Fixed capital"
	When Goodwill is Raised and Written Off (In case Goodwill is Brought in Part By the New Partner	Cash / Bank A/c To New Partners' Capital A/c To Premium for Goodwill A/c (Being capitals premium for goodwill brought in)

		Premium for Goodwill A/c (with share of goodwill brought in) **Dr.** To Sacrificing Partners' Capital / Current A/cs (Being premium for goodwill is distributed among sacrificing partners' in sacrificing ratio)
		Goodwill A/c Dr. To Sacrificing Partners' Capital / Current A/cs (Being goodwill is raised in old ratio) **Sacrificing Partners' Capital / Current A/cs** **Dr.** **Incoming Partners' Current A/c Dr.** **To Goodwill A/c** (Being goodwill written off in new ratio) "Sacrificing partners Current A/c in case of Fixed capital."
	When Goodwill is Raised Written Off (In Case Goodwill is not Brought in Full)	**Cash / Bank A/c Dr.** **To New Partner's Capital A/c** (Being capital brought in by new partner Goodwill A/c) **Goodwill A/C Dr.** To Sacrificing Partner's capital Current A/cs (Being goodwill is raised in old ratio)
		Sacrificing Partner's Capital / Current A/cs **Dr.** Incoming Partner's current A/c **Dr.** To Goodwill A/c (Being goodwill written off in new ratio)

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<tr><td></td><td><table><tr><td>When Existing Good will is Written Off</td><td>Old Partner's Capital / Current A/cs
To Goodwill A/c
(Being goodwill written off among old partner's in old ratio)
Current A/c incase of Fixed capitals</td></tr></table></td></tr>
<tr><td>Treatment of Reserves, Accumulated Profits and Losses</td><td>Accumulated profits include credit balance of P and L A/c, General Reserves, Reserve Fund, Workmen Compensation Reserves, Investment Fluctuation Reserve etc.
Accumulated Losses include debit balance of P and L A/c, Deferred Revenue Expenditure i.e., Advertisement Suspense A/c.
(A) When question is silent of when accumulated profits of losses are to be distributed or when accumulated profits or losses are not to be shown in new balance sheet
Contingency Reserve A/c Dr.
Reserve A/c Dr.
P and L A/c (Cr. Balance) Dr.
Workmen Compensation Reserve A/c Dr.
Investment Fluctuation Reserve A/c Dr.
To Old Partners' Capital / Current A/cs
(Being reserves and accumulated profits transferred to old partners in old ratio)
Old Partners' Capital / Current A/Cs Dr.
To P and L A/c (Dr. balance)
To Deferred Revenue Expenditure A/c
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Current A/c in case of Fixed capitals</td></tr>
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When there is no Claim</td><td>Workmen Compensation Reserve A/c Dr.
To Old Partners' Capital / Current A/cs</td></tr><tr><td>Case 2. WCC = WCR (equal)</td><td>Workmen Compensation Reserve A/c Dr.
To Provision for Workmen Compensation Claim A/c</td></tr></table></td></tr>
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Case 3. WCC < WCR (less)	Workmen Compensation Reserve A/c Dr. To Provision for Workmen Compensation Claim A/c To Old Partners' Capital / Current A/cs
Case 4. WCC > WCR (more)	Workmen Compensation Reserve A/c Dr. Revaluation A/c Dr. To Provision for Workmen Compensation Claim A/c
	Old Partners' Capital / Current A/cs Dr. To Revaluation A/c

WCC stands for Workmen Compensation Claim
WCR stands for Workmen Compensation Reserve

Treatment of Investment Fluctuation Reserve

Case 1. BV = MV	Investment Fluctuation Reserve A/c Dr. To Old Partners' Capital / Current A/cs
Case 2. BV < MV	Investment Fluctuation Reserve A/c Dr. To Old Partners' Capital / Current A/cs (Entire reserve distributed in partners' old ratio)
	Investment A/c Dr. To Revaluation A/c (For increase in value of Investments)
	Revaluation A/c Dr. To Old Partners' Capital / Current A/cs
Case 3. BV > MV	(i) When fall in value is less than investment Fluctuation Reserve Investment Fluctuation Reserve A/c Dr. To Investment A/c (BV-MV) To Old Partners' Capital / Current A/cs (In Old ratio)
	(ii) When fall in value is equal to investment Fluctuation Reserve Investment Fluctuation Reserve A/c Dr. To Investment A/c

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<tr><td></td><td>(iii) When fall in value is more than investment Fluctuation Reserve
Investment Fluctuation Reserve A/c Dr.
Revaluation A/c Dr.
To Investment A/c</td></tr>
<tr><td></td><td>Old Partners' Capital / Current A/cs Dr.
To Revaluation A/c</td></tr>
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BV stands for Book value of Investment
MV stands for Market value of investment
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<td>Revaluation of Assets and Reas- sess- ment of Liabilities</td>
<td>
It is a nominal account and prepared to revalue assets and reassess liabilities.
(A) When Revised Values of Assets and Liabilities are to be Recorded
Revaluation A/c is prepared and Profit/Loss of revaluation is distributed among old partners' in old ratio.
Dr. RevaluationA/c Cr
<table>
<tr><th>Particulars</th><th>Amount (Rs)</th><th>Particulars</th><th>Amount (₹)</th></tr>
<tr><td>To asset (decrease in value)</td><td>xxx</td><td>By asset (increase in value)</td><td>xxx</td></tr>
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<tr>
<td>Adjustment of capital</td>
<td>
(i) Adjustment of Old Partners' Capital on the basis of new Partners' Capital
Step 1. Calculate total Capital of the firm on the basis of New Partners' Capital :
Total capital of the firm on the basis of New Partners' Capital = $\frac{\text{Capital of the New Partner}}{\text{Share of profitof New Partner}}$
Step 2. Determine New Capital of each Partner by dividing the Total Capital in new profit sharing ratio.
Step 3. Ascertain Present Capital of the Old Partners' after all adjustments
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	Step 4. Find Surplus / Deficit— Surplus = Present Capital > New Capital Deficit = Present Capital < New Capital **Step 5.** In case of **Surplus** (Present Capital > New Capital) Concerned partners' Capital A/c Dr. To Bank / Cash A/c Or Concerned Partners' Current A/c In case of **Deficit** (Present Capital < New Capital) Bank / Cash A/c Dr. Concerned Partners' Current A/c Dr. Or To Concerned Partners' Capital A/c (ii) **Adjustment of New Partners' Capital on the basis of Old Partners' Capital** **Step 1.** Determine Total Adjusted Capital of the Old Partners' after all adjustments **Step 2.** Calculate Total Capital of the new firm on the basis of Old Partner's after all adjustment: Total Capital of the new firm $= \frac{\text{Total adjusted Capital of Old Partners}}{\text{Reciprocal of remaining share}}$ **Step 3.** Determine Capital of New Partner by multiplying the total Capital by Share of New Partner.

NEW PROFIT SHARING RATIO

Illustration 1.

A and B are partners in a firm sharing profit and losses in the ratio of 3 : 2. C is admitted for $1/5^{th}$ share in profits of the firm.

Calculate new profit sharing ratio; if—

(a) C gets his share equally from A and B.
(b) C gets it from A and B in 2 : 1.
(c) C gets it 3/20 from A and 1/20 from B.
(d) C gets it wholly from A

Solution.

(a) C gets 1/5 equally from A and B

Share acquired by C from A = $\frac{1}{2} \times \frac{1}{5} = \frac{1}{10}$

Share acquired by C from B = $\frac{1}{2} \times \frac{1}{5} = \frac{1}{10}$

A's New Share = $\frac{3}{5} - \frac{1}{10} = \frac{6-1}{10} = \frac{5}{10}$

B's New Share = $\frac{2}{5} - \frac{1}{10} = \frac{4-1}{10} = \frac{3}{10}$

C's New Share = $\frac{1}{5}$ or $\frac{2}{10}$

New Profit sharing Ratio = A : B : C = 5 : 3 : 2

(b) C gets 1/5 from A and B in 2 : 1

Share acquired by C from A = $\frac{2}{3} \times \frac{1}{5} = \frac{2}{15}$

Share acquired by C from B = $\frac{1}{3} \times \frac{1}{5} = \frac{1}{15}$

A's new share = $\frac{3}{5} - \frac{2}{15} = \frac{9-2}{15} = \frac{7}{15}$

B's new share = $\frac{2}{5} - \frac{1}{15} = \frac{6-1}{15} = \frac{5}{15}$

C's new share = $\frac{1}{5}$ or $\frac{3}{15}$

New profit sharing ratio = A : B : C = 7 : 5 : 3

(c) C gets 1/5 from A and B as 3/20 and 1/20 respectively

A's new share = $\frac{3}{5} - \frac{3}{20} = \frac{12-3}{20} = \frac{9}{20}$

B's new share = $\frac{2}{5} - \frac{1}{20} = \frac{8-1}{20} = \frac{7}{20}$

C's new share = $\frac{3}{20} + \frac{1}{20} = \frac{4}{20}$

New profit sharing Ratio = A : B : C = 9 : 7 : 4

(d) C gets 1/5 wholly from A

A's new share = $\frac{3}{5} - \frac{1}{5} = \frac{2}{5}$

B's new share = $\frac{2}{5}$

C's new share = $\frac{1}{5}$

New profit sharing Ratio = 2 : 2 : 1 in A : B : C

In case (d), B retains his old share (2/5)

SACRIFICING RATIO

Illustration 2.

X and Y are partners sharing profit in the ratio 3 : 2. They admit P and Q as new partne₹ X surrendered 1/3rd of his share in favour of P and Y surrendered 1/4th of his share in favour of Q.

Calculate (a) Sacrificing ratio

(b) New profit sharing ratio X, Y, P and Q.

Solution:

(a) Calculation of Sacrificing Ratio

X surrenders 1/3 of his share in factor of P = $\frac{1}{3} \times \frac{3}{5} = \frac{3}{15}$

Y surrenders 1/4 of his share in favour of Q = $\frac{1}{4} \times \frac{2}{5} = \frac{2}{20}$

$$X : Y = \frac{3}{15} : \frac{2}{20}$$

$$\frac{3}{15} \times \frac{4}{4} : \frac{2}{20} \times \frac{3}{3}$$

$$\frac{12}{60} : \frac{6}{60}$$

$\Rightarrow$ 12 : 6 or 2 : 1

(b) Calculation of New Profit sharing ratio

X's New share = $\frac{3}{5} - \frac{3}{15} = \frac{9-3}{15} = \frac{6}{15}$ or $\frac{24}{60}$

Y's New share = $\frac{2}{5} - \frac{2}{20} = \frac{8-3}{20} = \frac{6}{20}$ or $\frac{18}{60}$

P's = $\frac{3}{15}$ or $\frac{12}{60}$

$$Q's = \frac{2}{20} \text{ or } \frac{6}{60}$$

$$X : Y : P : Q = 24 : 18 : 12 : 6$$
$$= 4 : 3 : 2 : 1$$

Illustration 3.

X and Y are partners sharing profit and losses in the ratio 3 : 2. They admit Z into the partnership, who acquires 1/4th of his share from X and 3/16th share from Y.

Calculate New Profit Sharing Ratio and Sacrificing Ratio.

Solution:

Since Z acquires $\frac{1}{4}^{th}$ of his share from X

It means he acquires $\frac{3}{4}^{th}$ $\left(1-\frac{1}{4}\right)$ of his share from Y.

If 3/4th share of Z = $\frac{3}{16}$ (Received from Y)

$$Z's \text{ share} = \frac{3}{16} \times \frac{4}{3} = \frac{1}{4}$$

Share acquired by Z from X = $\frac{1}{4} \times \frac{1}{4} = \frac{1}{16}$

Share acquired by Z from Y = $\frac{3}{16}$

Hence, X's new share = $\frac{3}{5} - \frac{1}{16} = \frac{48-5}{80} = \frac{43}{80}$

Y's new share = $\frac{2}{5} - \frac{3}{16} = \frac{32-15}{80} = \frac{17}{80}$

Z's share = $\frac{1}{4}$ or $\frac{20}{80}$

New profit sharing ratio = X : Y : Z = 43 : 17 : 20

Sacrificing Ratio X : Y = $\frac{1}{16} : \frac{3}{16} = 1 : 3$

Admission of a partner.

New Profit sharing Ratio

Illustration 4.

Guddu and Bablu are partners sharing profits and losses in 2 : 1 have decided to share profits and losses in 3 : 2 in future. On that date munna was admitted for $\frac{1}{5}$th share. Calculate new ratio and secrificing ratio:

Sol. Existing P.S.R. = 2 :1

Future ratio of Guddu and Bablu = 3 : 2

Munna's share = $\frac{1}{5}$

Remaining share = $1-\frac{1}{5} = \frac{4}{5}$

This remaining share will be distributed among old partners in their future ratio.

So, N.P.S.R.

$$\text{Guddu} = \frac{3}{5}\times\frac{4}{5}=\frac{12}{25}$$

$$\text{Bablu} = \frac{2}{5}\times\frac{4}{5}=\frac{8}{25}$$

$$\text{Munna} = \frac{1}{5}\times\frac{5}{5}=\frac{5}{25}$$

Sacrificing ratio = old Ratio – New Ratio

$$\text{Guddu} = \frac{2}{3}-\frac{12}{25}=\frac{50-36}{75}=\frac{14}{75}$$

$$\text{Bablu} = \frac{1}{3}-\frac{8}{25}=\frac{25-24}{75}=\frac{1}{75}=14:1$$

Illustration 5. P, Q and R are partners are sharing Profits equally. They decided to admit S as a partner for $\frac{1}{4}$th share. Q decided to retain his orginal share calcuale new profit sharing ratio.

Sol. Old profit sharing ratioo = 1 : 1

Remaining share (Afters's share) = $1-\frac{1}{4}=\frac{3}{4}$

(Treat Partner who is retaning his/her share as new partner to calculate share of Profit)

Remaining share (after Q's share) = $\frac{3}{4}-\frac{1}{3}=\frac{5}{12}$

This $\frac{5}{12}$ share will be divided b/w P and R

P's new share = $\frac{1}{2}\times\frac{5}{12}=\frac{5}{24}$

New P.S.R.

$$P = \frac{5}{24}$$

$$Q = \frac{1}{3}\times\frac{8}{8}=\frac{8}{24}$$

$$R = \frac{5}{24}$$

$$S = \frac{1}{4}\times\frac{6}{6}=\frac{6}{24}$$

$$= 5 : 8 : 5 : 6$$

ADMISSION OF A PARTNER

REVALUATION OF ASSETS AND REASSESSMENT OF LIABILITIES

When revised values of assets and liabilities are to be recorded Revaluation Account is opened.

It's a nominal account.

It is prepared to find out gain/loss on account of revaluation of assets and reassessment of liabilities.

Such gain/loss is then distributed among partners in old profit sharing ratio. At the end new values are recorded in the new balance sheet of the firm.

Journal entries of revaluation account

	Adjustments	entry
(1)	For an increase in value of assets	Assets a/c ...Dr. *** To Revaluation a/c ***
(2)	For a decrease in value of assets	Revaluation a/c ...Dr. *** To assets a/c ***
(3)	For an increase in amount of liabilities	Revaluation a/c ...Dr. *** To Liabilities a/c ***

(4)	For a decrease in amount of liabilities	Liabilities A/c ...Dr. *** To Revaluation A/C ***
(5)	Ac Counting unrecorded Assets	Revaluation Assets A/C ... Dr. ***** To Revaluation A/C ****
(6)	Unrecorded Liabilities	Revaluation A/C ...Dr. *** To Unrecorded Lia. A/C ***
(7)	Expenses Paid By Firm	Revaluation A/C ...Dr. *** To Cash/Bank A/C ***
(8)	Remuneration Paid To A Partner for the process of revaluation	Revaluation A/C ...Dr. *** To Partner's Capital ***
(9)	In Case Of Profit Ie. Excess Of Credit Side Of Revaluation A/C Over Debit Side	Revaluation A/C ...Dr. *** To old Partner's Capital A/C *** (In Their Old Profit Sharing Ratio)
(10)	In Case Of Loss i.e. Excess Of Debit Side Of Revaluation A/C Over Credit Side	Old Partner's Capital A/C ...Dr. *** To Revaluation A/C *** (In Their Old Profit Sharing Ratio)

Note : in case of fixed capital method we will use current a/c instead of capital a/c

Some Typical Cases of Revaluation of Assets & Reassessment of Liabilities.

(i) Value of stock is to be increased by ₹ 5,000 {Book value of stock is ₹ 1,00,000).

(ii) Value of stock is to be increased to ₹ 1,05,000 (Book value of stock is ₹ 1,00,000).

(iii) Value of stock is to be brought up to 105% of its value (Book value of stock is ₹ 1,00,000).

Date	Particulars	L.F.	Dr.	Cr.
	Stock A/c To Revaluation A/c (Being the increase in the value of stock recorded)		5,000	 5,000

(iv) Plant is undervalued by 10% (book value of Plant ₹ 90,000) or Plant is recorded at 90% in the books of account.

Book value of Plant is ₹ 90,000 which is 90%.

So 100% value is

90,000 x 100/90 = 1,00,000.

Therefore, Increase in Plant is ₹ 10,000.

Date	Particulars	L.F.	Dr.	Cr.
(iv)	Plant A/C ...Dr. To Revaluation A/c (Being the plant is undervalued by ₹ 10,000)		10,000	 10,000

(v) Book value of Machinery is ₹1,10,000 which is 110%.
So 100% value is
1,10,000 x 100/110 = 1,00,000 .
Therefore, Decrease in machinery is ₹ 10,000.
Revalvation A/c Dr 10,000
To Machinery 10,000

Date	Particulars	L.F.	Dr.	Cr.
(vi)	Sundry Creditors A/C ...Dr. To Revaluation A/c (Creditors of ₹ 8,000 will be written back.)		8,000	 8,000

(vii) Write off ₹ 8,000 as bad debts and maintain a 5% provision for doubtful debts on debto₹fDebtors 68,000 and Provision for doubtful debts 10,000 are appearing in the balance sheet)

Debtors	68,000	Existing PDD	10,000
Less: bad debts	(8,000)	Less: bad debts	(8,000)
Net debtors	60,000	Net PDD available	2,000
Less: PDD @5%	(3,000)	Required PDD (5% of 60,000) 3,000	
		PDD to be raised by	
		(3000- 2,000)	1,000

Date	Particulars	L.F.	Debit	Credit
April 1	Bad debts A/c Dr.		8,000	
	To Debtors (Being 8,000 as bad debts)			8,000
April 1	Provision for doubtful debts A/c Dr. To Bad debts (Being bad debts transferred to PDD a/c)		8,000	 8,000
April 1	Revaluation A/c Dr. To Provision for doubtful debts A/c (Being PDD Created @5% on debtors)		1,000	 1,000

Question for practice

Q. K and S are partners sharing profits in the ratio of 3:2.They share. Pass Journal entries for the following on P's admisssion

(i) Value of furniture is to be increased by ₹10,000 (Book ₹50,000).

(ii) Value of furniture is to be increased to ₹50,000 (Book ₹40,000).

(iii) Value of furniture is to be brought up to 120% of its value furniture is ₹20,000).

(iv) Stock is found undervalued by ₹4,000 (Book value of stock ₹ 20,000

(v) Creditors are written back by ₹ 5,000.

(vi) Debtors ₹ 80,000. Existing provision for doubtful ₹ 4,000 debts are to be written off on P's admission ₹ 5,000 and 5% Provision is to be maintained for doubtful debts on debto₹

Illustration 6.

(a) A, B and C are partners sharing profits and losses in the ratio of 5 : 3 : 2. C retired and his capital balance after adjustments regarding reserves, accumulated profits/losses and gain/loss on revaluation was ₹ 2,50,000. C was paid ₹ 3,00,000 in full settlement. Afterwards D was admitted for 1/4th share. Calculate the amount of goodwill premium brought by D.

Solution:

Goodwill share of C = ₹ 3,00,000 – ₹ 2,50,000 = ₹ 50,000

Firm's Goodwill = 50,000 × $\frac{10}{2}$ = ₹ 2,50,000

D's share in Goodwill = ₹ 2,50,000 × $\frac{1}{4}$ = ₹ 62,500

(b) A and B were partners in a firm. They admitted C as a new partner for 20% share in the profits. After all adjustments regarding general reserve, goodwill, gain or loss on revaluation, the balances in capital accounts of A and B were ₹ 3,85,000 and ₹ 4,15,000 respectively. C bought proportionate capital so as to give him 20% share in the profits.

Calculate the amount of capital to be brought by C.

Solution:

Combined capital of A and B = ₹ 3,85,000 + ₹ 4,15,000 = ₹ 8,00,000

C's share = $\frac{1}{5}$ th of total capital

Remaining share = $1 - \frac{1}{5} = \frac{4}{5}$

$\frac{4}{5}$ = ₹ 8,00,000

C's capital = ₹ 8,00,000 × $\frac{5}{4} \times \frac{1}{5}$ = ₹ 2,00,000

(C) Rekha, Sunita and Teena are partners in a firm sharing profits in the ratio of 3 : 2 : 1. Samiksha joins the firm. Rekha surrenders 1/4th of her share; Sunita surrenders 1/3rd of her share and Teena surrenders 1/5th of her share in favour of Samiksha. Find the new Profit sharing ratio.

Solution:

Rekha surrenders for Samiksha = $\frac{1}{4} \times \frac{3}{6} = \frac{3}{24}$

Sunita surrenders for Samiksha = $\frac{1}{3} \times \frac{2}{6} = \frac{2}{18}$

Teena surrenders for Samiksha = $\frac{1}{5} \times \frac{1}{6} = \frac{1}{30}$

New share of Rekha = $\frac{3}{6} - \frac{3}{24} = \frac{9}{24}$

New share of Sunita = $\frac{2}{6} - \frac{2}{18} = \frac{4}{18}$

New share of Teena = $\frac{1}{6} - \frac{1}{30} = \frac{4}{30}$

Share of Samiksha = $\frac{3}{24} + \frac{2}{18} + \frac{1}{30} = \frac{97}{360}$

New ratio : $\frac{9}{24} : \frac{4}{18} : \frac{4}{30} : \frac{97}{360}$ = 135 : 80 : 48 : 97

Illustration 7. When Premium for Goodwill is Brought in Cash

(a) A and B are partners in a firm sharing profits and losses in the ratio of 3 : 2. C is admitted as a new partner. A surrenders 1/5th of his share and B 2/5th of his share in favour of C. Goodwill of the firm is valued at ₹ 75,000. C brings his share of goodwill in cash.

Journalise the above transaction when–

(i) Goodwill is retained in the firm

(ii) Goodwill is withdrawn by old partners

Solution:

(i) **Goodwill is Retained in the Firm**

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr.		21,000	
	To Premium for Goodwill A/c			21,000
	(Being the amount of Goodwill brought in)			
	Premium for Goodwill A/c Dr.		21,000	
	To A's Capital A/c			9,000
	To B's Capital A/c			12,000
	(Being goodwill distributed between A and B in sacrificing ratio, i.e., 3 : 4)			

(ii) **Goodwill is Withdrawn by Old Partners**

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr.		21,000	
	To Premium for Goodwill A/c			21,000
	(Being the amount of Goodwill brought in)			
	Premium for Goodwill A/c Dr.		21,000	
	To A's Capital A/c			9,000
	To B's Capital A/c			12,000
	(Being amount of goodwill distributed between A and B in sacrificing ratio, i.e., 3 : 4)			
	A's Capital A/c Dr.			
	B's Capital A/c Dr.			
	To Bank A/c		9,000	
	(Being amount of goodwill is withdrawn by old partners)		12,000	21,000

Working Notes:

1. Calculation of Sacrificing ratio–

A's Sacrifice $\frac{1}{5}$ of his share = $\frac{1}{5} \times \frac{3}{5} = \frac{3}{25}$

B's Sacrifice $\frac{2}{5}$ of his share = $\frac{2}{5} \times \frac{2}{5} = \frac{4}{25}$

Thus, Sacrificing ratio of A : B = 3 : 4

2. Calculation of C's share of Goodwill–

C's share of profit = $\frac{3}{25} + \frac{4}{25} = \frac{7}{25}$

Hence, C's share of Goodwill = $\frac{7}{25} \times 75{,}000$ = ₹ 21,000

(b) When Premium for Goodwill is Brought in Kind

A and B are partners in a firm sharing profits and losses in the ratio of 3 : 2. C is admitted as a new partner for 3/13th share in the profits. C contributed following assets towards his capital and for his share of goodwill. Land ₹ 90,000; Machinery ₹ 90,000; Stock ₹ 60,000; Debtors ₹ 60,000. On the date of admission, Goodwill of the firm is valued at ₹ 5,20,000. Journalize the above transaction.

Solution:

Goodwill is Brought in Kind

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Land A/c Dr. Machinery A/c Dr. Stock A/c Dr. Debtors A/c Dr. To premium for Goodwill A/c (5,20,000 × 3/13) To C's Capital A/c (b/f) (Being the amount of capital and Goodwill brought in kind)		90,000 90,000 60,000 60,000	 1,20,000 1,80,000
	Premium for Goodwill A/c Dr. To A's Capital A/c To B's Capital A/c (Being goodwill distributed between A and B in sacrificing ratio, i.e., 3 : 2)		1,20,000	 72,000 48,000

(c) When Premium for Goodwill is not Brought in Kind

Neeta and Sunita are partners in a firm sharing profits and losses in the ratio of 2 : 1. Geeta is admitted as anew partner for 1/4th share in the profits. Geeta pays ₹ 50,000 as capital but does not bring any amount for goodwill. Goodwill of the firm is valued at ₹ 36,000.

(i) Journalize the above transaction.

(ii) Also, give journal entries if Goodwill is raised and written off.

Solution:

(i) Goodwill is not Brought in Cash and Adjusted Through Partner's Current A/c

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Cash A/c Dr.		50,000	
	To Geeta's Capital A/c			50,000
	(Being the amount of capital brought in)			
	Geeta's Current A/c Dr.			
	To Neeta's Capital A/c			
	To Sunita's Capital A/c		9,000	
	(Being goodwill distributed between Neeta and Sunita in sacrificing ratio, i.e., 2 : 1)			6,000 3,000

(ii) When Goodwill is Raised and Written Off

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Cash A/c Dr.		50,000	
	To Geeta's Capital A/c			50,000
	(Being the amount of capital brought in)			
	Goodwill A/c Dr.		36,000	
	To Neeta's Capital A/c			24,000
	To Sunita's Capital A/c			12,000
	(Being goodwill raised in old ratio, i.e., 2 : 1)			
	Neeta's Capital A/c Dr.		18,000	
	Sunita's Capital A/c Dr.		9,000	
	Geeta's Capital A/c Dr.		9,000	
	To Goodwill A/c			36,000
	(Being Goodwill written off in new ratio i.e., 2 : 1 : 1)			

Working Note: Calculation of New Profit sharing ratio–

Let total share of the firm = 1

Geeta's share = $\frac{1}{4}$

Remaining share = $1-\frac{1}{4}=\frac{3}{4}$

Neeta's new share = $\frac{3}{4}\times\frac{2}{3}=\frac{2}{4}$

Sunita's new share = $\frac{3}{4}\times\frac{1}{3}=\frac{1}{4}$

Hence, New profit sharing ratio N : S : G = 2 : 1 : 1

(d) When Premium for Goodwill is Partly Brought in Cash

Neeta and Sunita are partners in a firm sharing profits and losses equally. Geeta is admitted as a new partner. Geeta pays ₹ 1,000 for premium out of her share of goodwill of ₹ 1,600 for $1/4^{th}$ share of profit. Goodwill A/c appears in the books at ₹ 6,000.

(i) Journalize the above transaction.

(ii) Also, give journal entries if Goodwill is raised and written off.

Solution: (i) When Premium for Goodwill is Partly Brought in Cash

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr. To Premium for Goodwill A/c (Being the amount of Goodwill brought in cash)		1,000	 1,000
	Premium for Goodwill A/c Dr. Geeta's Current A/c Dr. To Neeta's Capital A/c To Sunita's Capital A/c (Being goodwill distributed between Neeta and Sunita in sacrificing ratio, i.e., 1 : 1)		1,000 600	 800 800
	Neeta's Capital A/c Dr. Sunita's Capital A/c Dr. To Goodwill A/c (Being existing goodwill written of between old partners in old ratio i.e., equal)		3,000 3,000	 6,000

(ii) When Goodwill is Raised and Written Off

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Bank A/c Dr.		1,000	
	To Premium for Goodwill A/c			1,000
	(Being the amount of Goodwill brought in cash)			
	Premium for Goodwill A/c Dr.		1,000	
	To Neeta's Capital A/c			500
	To Sunita's Capital A/c			500
	(Being goodwill distributed between Neeta and Sunita in sacrificing ratio, i.e., 1 : 1)			
	Goodwill A/c (600 × 4/1) Dr.		2,400	
	To Neeta's Capital A/c			1,200
	To Sunita's Capital A/c			2,200
	(Being goodwill raised in old ratio, i.e., 1 : 1)			
	Neeta's Capital A/c Dr.		900	
	Sunita's Capital A/c Dr.		900	
	Geeta's Current A/c Dr.		600	
	To Goodwill A/c			
	(Being goodwill written off in new ratio i.e., 3 : 2 : 2)			2,400
	Neeta's Capital A/c Dr.		3,000	
	Sunita's Capital A/c Dr.		3,000	
	To Goodwill A/c			6,000
	(Being existing goodwill written off between old partners in old ratio i.e., equal)			

Working Note: 1. Calculation of New profit sharing ratio–

Geeta's share = $\frac{1}{4}$

Remaining share = $1-\frac{1}{4}=\frac{3}{4}$

Neeta's new share = $\frac{3}{4}\times\frac{1}{2}=\frac{3}{8}$

Sunita's new share = $\frac{3}{4}\times\frac{1}{2}=\frac{3}{8}$

Hence, New profit sharing ratio N : S : G = 3 : 3 : 2

2. Calculation of amount of Goodwill to be raised and written off

Amount of Goodwill not brought by Geeta = 600

His share of profit = $\frac{1}{4}$

Amount of Goodwill to be raised and written off = $600\times\frac{4}{1}=2400$

Illustration 8.

Naresh and Suresh are partners in a firm sharing profits and losses in the ratio of 3 : 1. On April 1st 2019, they admitted Rahul as a partner for 1/5th share in the profits of the firm. On the date of admission, the balance sheet showed a General Reserve of ₹ 1,20,000; a debit balance of ₹ 60,000 in Profit and Loss A/c; Workmen compensation Reserve of ₹ 1,50,000 and Investment fluctuation Reserve of ₹ 10,000.

The following terms were agreed upon–

(i) Rahul will bring ₹ 1,50,000 as his capital and his share of goodwill in cash.

(ii) Goodwill of the firm be valued at ₹ 2,40,000.

(iii) There was a claim of Workmen compensation for ₹ 1,70,000

(iv) The market value of investment was ₹ 18,000 less than the Book value.

(v) The partners decided to share future profits in the ratio of 3 : 1 : 1.

Pass the necessary Journal entries on Rahul's admission.

Solution:

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
1st April 2019	General Reserve A/c Dr.		1,20,000	
	To Naresh's Capital A/c			1,20,000
	To Suresh's Capital A/c			
	(Being General Reserve distributed between old partners in oldratio, 3 : 1)			
	Naresh's Capital A/c Dr.		45,000	
	Suresh's Capital A/c Dr.		15,000	
	To Profit and Loss A/c			60,000
	(Being P and L distributed between old partners in old ratio, 3 : 1)			
	Workmen compensation Reserve A/c Dr.		1,50,000	
	Revaluation A/c Dr.		20,000	
	To Provision for Workmen Compensation Claim A/c			1,70,000
	(Being Workmen Compensation Claim adjusted against Workmen compensation Reserve)			
	Investment fluctuation Reserve A/c Dr.		10,000	
	Revaluation A/c Dr.		8,000	
	To Investment A/c			18,000
	(Being fall in value of investment adjusted against Investment fluctuation Reserve and Revaluation A/c)			
	Naresh's Capital A/c Dr.		21,000	
	Suresh's Capital A/c Dr.		7,000	
	To Revaluation A/c			28,000
	(Being loss on revaluation transferred to old partners in old ratio)			

	Bank A/c Dr. To Rahul's Capital A/c To Premium for Goodwill A/c (2,40,000 × 1/5) (Being the amount of capital and Goodwill brought in)		1,98,000	 1,50,000 48,000
	Premium for Goodwill A/c Dr. To Naresh's Capital A/c To Suresh's Capital A/c (Being amount of Goodwill distributed between Naresh and Suresh sacrificing ratio, i.e., 3 : 1)		48,000	 36,000 12,000

Hidden Goodwill

Illustration 9.

A and B are partners with capital of ₹ 26000 and ₹ 22000 respectively. They admit C as partner with 1/4th share in the profits of the firm. C brings ₹ 26,000 as his share of capital.

Give journal entry to record goodwill on C's admission

Solution :

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
1st April 2019	Bank A/c Dr. To C's Capital A/c (Being the amount of Capital brought in by new partner)		26,000	 26,000
	C's Current A/c Dr. To A's Capital A/c To B's Capital A/c (Being the Goodwill credited to sacrificing partners Capital A/cs in their sacrificing ratio, i.e., equal)		7,500	 3,750 3,750

Working Note :

(1) Calculation of C's share of Goodwill–

Total capital of new firm on the basis of C's capital

$$= 26000 \times \frac{4}{1} = ₹\ 1{,}04{,}000$$

Total capital of A, B and C

= ₹ 26000 + ₹ 22000 + ₹ 26000

= ₹ 74000

Goodwill of the firm

= Total capital of new firm – Combined capital of A, B and C

= ₹ 104000 – ₹ 74000

= ₹ 30000

C's share of Goodwill

$= 30000 \times \frac{1}{4} =$ ₹ 7500

(2) In the absence of information, profits will be shared Equally.

Illustration 10.

X and Y were partners in a firm sharing profits and losses in the ratio of 3 : 2. Their Balance sheet as at 31st March, 2019 was as follows:

Liabilities	₹	Assets	₹
Creditors	42,000	Current Assets	2,00,000
Employee's Provident Fund	20,000	Investments	50,000
Contigency Reserve	30,000	Furniture	20,000
Profit and Loss Account	45,000	Machinery	90,000
Workment Compensation Reserve	18,000	Advertisement Expenditure (Deffered Revenue Expenditure)	20,000
Investment Fluctuation Reserve	25,000		
Capitals X 1,20,000			
Capitals Y 80,000	2,00,000		
	3,80,000		3,80,000

They admit Z into partnership on 1st April, 2019 and the new profit sharing ratio is agreed at 2 : 1 : 1. It is estimated that:

(i) Claim on account of Workmen's Compensation is estimated at ₹ 10,000.

(ii) Market value of Investments is ₹ 46,000.

Give necessary journal entries to adjust accumulated profits and losses.

Solution:

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
1st April 2019	Investment Fluctuation Reserve Dr. To Investment A/c (Value of Investment brought down to market value)		4,000	4,000

	Workmen Compensation Reserve A/c Dr. To Provision for Workmen Compensation Claim A/c (Provision made for workmen compensationclaim)		10,000	 10,000
1st April 2019	Contigency Reserve Dr. Profit and Loss A/c Dr. Workmen Compensation Reserve (₹ 18,000 – ₹ 10,000) Dr. Investment Fluctuation Reserve (₹ 25,000 – ₹ 4,000) Dr. To X's Capital A/c To Y's Capital A/c (Transfer of accumulated profits to old partners in their old profit sharing ratio i.e., 3 : 2)		30,000 45,000 8,000 21,000	 62,400 41,600
1st April 2019	X's Capital A/c Dr. Y's Capital A/c Dr. To Advertisement Expenditure A/c (Transfer of accumulated loss to old partners in their old profit sharing ratio i.e., 3 : 2)		12,000 8,000	 20,000

Working Note: Employee's Provident Fund is outside liability payable by the firm.

Illustration 11.

X and Y are in partnership, sharing profits in the ratio of 5 : 3 respectively. Their balance sheet is as follows:

Liabilities	₹	Assets	₹
Creditors	28,000	Cash at Bank	15,800
Workment Compensation Reserve	12,000	Debtors 40,000 Less : Provision 1,800	38,200
Z's Loan A/c	30,000	Stock	56,000
		Investment	10,000
Capitals X 1,20,000	50,000	Goodwill	10,000
Capitals Y 80,000	40,000	Plant	30,000
	1,60,000		1,60,000

Z is admitted into partnership on the following terms:

1. The new profit-sharing ratio will be 4 : 3 : 2 between X, Y and Z respectively.

2. Z's loan should be treated as his capital.
3. Goodwill of the firm is valued at ₹ 27,000.
4. ₹ 8,000 of investments were to be taken over by X and Y in their profit sharing ratio.
5. Stock be reduced by 10%.
6. Provision for doubtful debts should be @ 5% on debtors and a provision for discount on debtors @ 2% should also bemade.
7. The liability of Workmen's Compensation Reserve was determined to be ₹ 15,000.
8. X is to withdraw ₹ 6,000 in cash.

Give journal entries to record the above and prepare balance sheet of the new firm.

Solution:

Date	Particulars	L.F.	Dr. ₹	Cr. ₹
	Revaluation A/c Dr. To Stock A/c To Provision for Doubtful Debts To Provision for Discount on Debtors (Decrease in the value of stock and creation of provision on debtors)		6,560	 5,600 200 760
	Workmen Compensation Reserve A/c Dr. Revaluation A/c Dr. To Liability for Workmen's Compensation A/c (Recording of liability for Workmen's Compensation)		12,000 3,000	 15,000
	X's Capital A/c Dr. Y's Capital A/c Dr. To Revaluation A/c (Loss on revaluation transferred to old partner's Capital A/cs)		5.975 3,585	 9,560
	X's Capital A/c Dr. Y's Capital A/c Dr. To Investments A/c (Investments taken over by old partners)		5,000 3,000	 8,000

X's Capital A/c Dr. Y's Capital A/c Dr. To Goodwill A/c (Existing goodwill written off in old ratio i.e., 5 : 3)		6,250 3,750	10,000
Z's Current A/c Dr. To X's Capital A/c To Y's Capital A/c (Z's share of goodwill credited to old partners in the sacrificing ratio i.e., 13 : 3)		6,000	4,875 1,125
Z's Loan A/c Dr. To Z's Capital A/c (Z's Loan Account transferred to Z's Capital Account)		30,000	30,000
X's Capital A/c Dr. To Bank A/c (Cash withdrew by X)		6,000	6,000

Dr. **Partner's Capital Accounts**

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
To Revaluation	5,975	3,585	–	By Balance b/d	50,000	40,000	–
To Investment	5,000	3,000	–	By Z's Current A/c	4,875	1,125	–
To goodwill A/c	6,250	3,750	–	By Z's Loan A/c	–	–	30,000
To Bank A/c	6,000	–	–		–	–	30,000
To Balance c/d	31,650	30,790	30,000				
	54,875	41,125	30,000		54,875	41,125	30,000

Balance Sheet as at .....

Liabilities	₹	Assets	₹
Creditors	28,000	Cash at Bank (₹ 15800 – ₹ 6000)	9,800
Liabilities for Workmen's Compensation	15000	Debtors 40,000	

Capital A/cs :			Less : Provision for Doubtful Debts		
X	31,650				
Y	30,790			2,000	
Z	30,000	92,440		38,000	
			Less : Provision for Discount on Debtors		
				760	37,240
			Stock		50,400
			Investment		2,000
			Plant		30,000
			Z's Current A/c		6,000
		1,35,440			1,35,440

Working Note: (1) Calculation of sacrificing ratio–

Sacrificing ratio = Old ratio – New ratio

$$X = \frac{5}{8} - \frac{4}{9} = \frac{45-32}{72} = \frac{13}{72}$$

$$Y = \frac{3}{8} - \frac{3}{9} = \frac{27-24}{72} = \frac{3}{72}$$

Sacrificing ratio = 13 : 3

(2) From Z's share of goodwill, his current A/c has been debited instead of A/c so that his Capital is not reduced and remains intact at ₹ 30,000.

Illustration 10.

Deepika and Rajshree are partners in a firm sharing profits and losses in the ratio of 3 : 2. On 31st March, 2017, their Balance Sheet was as under:

Liabilities		₹	**Assets**		₹
Sundry Creditors		16,000	Cash in Hand		1,200
Public Deposits		61,000	Cash at Bank		2,800
Bank Overdraft		6,000	Stock		32,000
Outstanding Liabilities		2,000	Prepaid Insurance		1,000
Capital Accounts :			Sundry Debtors		
Deepika	48,000			28,000	
Rajshree	40,000	88,000	Less : Provision for Doubtful Debts		
				800	28,000
			Plant and Machinery		48,000
			Land and Building		50,000
			Furniture		10,000
		1,73,000			1,73,000

On the above date, the partners decide to admit Anshu as a partner on the following terms:

(i) The new profit-sharing ratio of Deepika, Rajshree and Anshu will be 5 : 3 : 2, respectively

(ii) Anshu shall bring ₹ 32,000 as his capital.

(iii) Anshu is unable to bring in any cash for his share of goodwill. Partners, therefore, decide to calculate goodwill on the basis of Anshu's share in the profits and the capital contribution made by him to the firm.

(iv) Plant and Machinery would be increased by ₹ 12,000.

(v) Stock would be increased to ₹ 40,000.

(vi) Provision for Doubtful Debts is to be maintained at ₹ 4,000. Value of Land and Building has appreciated by 20%. Furniture has depreciated by 10%.

(vii) There is an additional liability of ₹ 8,000 being outstanding salary payable to employees of the firm. This liability is not included in the outstanding liabilities, stated in the above Balance sheet. Partners decide to show this liability in the books of accounts of the reconstituted new firm.

Prepare revaluation account, Partner's Capital Accounts and the Balance Sheet Deepika, Rajshree and Anshu.

Solution:

Dr. Revaluation Account Cr.

Particulars	₹	Particulars	₹
To Provision for Doubtful debts	3,200	By Plant and Machinery	12,000
To Furniture	1,000	By Stock	8,000
To Outstanding Salary	8,000	By Land and Building	10,000
To Profit transferred to :			
Deepika Capital A/c (3/5) 10,680			
Rajshree Capital A/c (2/5) 7,120	17,800		
	30,000		30,000

Dr. Capital Accounts Cr.

Particulars	X	Y	Z	Particulars	X	Y	Z
	₹	₹	₹		₹	₹	₹
				By Balance b/d	48,000	40,000	—
				By Revaluation	10,680	7,120	—
				By Anshu's Current A/c	2,220	2,220	—
To Balance	60,900	49,340	32,000	By Bank A/c	—		32,000
c/d	60,900	49,340	32,000		60,900	48,340	32,000

Opening Balance Sheet

(as at 1st April, 2017)

Liabilities		₹	Assets		₹
Sundry Creditors		16,000	Cash in Hand		1,200
Public Deposits		61,000	Cash at Bank		28,800
Outstanding Liabilities		10,000	Stock		40,000
Capital Accounts :		2,000	Prepaid Insurance		1,000
Deepika	48,000		Sundry Debtors		
Rajshree	40,000			28,000	
Anshu	32,000	1,42,240	Less : Provision		
				4,000	24,800
			Plant and Machinery		60,000
			Land and Building		60,000
			Furniture		9,000
			Anshu's Current A/c		4,440
		2,29,240			2,29,240

Working Note: (1) Bank Balance : ₹ 2,800 + ₹ 32,000 – Bank Overdraft ₹ 6,000 = ₹ 28,800.

(2) Calculation of Hidden Goodwill –

Total capital of firm based on Anshu shave should be–

$$₹\ 32,000 \times \frac{10}{2} = ₹\ 1,60,000$$

Less Capital of Deepika (48,000 + 10,680) = ₹ (58,680)

Capital of Rajshree (40,000 + 7,120) = ₹ (47,120)

Capital of Anshu = ₹ (37,000)

Value of Goodwill = ₹ 22,200

Anshu's share of Goodwill = 22,200 × $\frac{2}{10}$ = ₹ 4440

(3) Calculation of sacrificing ratio

Deepika = $\frac{3}{5} - \frac{5}{10} = \frac{6-5}{10} = \frac{1}{10}$ (Sacrifice)

Rajshree = $\frac{2}{5} - \frac{3}{10} = \frac{4-3}{10} = \frac{1}{10}$ (Sacrifice)

(4) Journal Entry–

Anshu's current A/c Dr.	4,440	
To Deepika Capital A/c		2,220
To Rajshree CapitalA/c		2.220
(Being amount of goodwill credited to sacrificing partner in their SR)		

Illustration 13.

P and K were partners in a firm. On March 31, 2019 their Balance Sheet was as follows:

Bank Account

Liabilities	Amount ₹	Assets	Amount ₹
Capitals:		Bank	18,000
P 3,00,000		Stock	19,000
K 2,00,000	5,00,000	Debtors 22,000	
General Reserve	1,00,000	Less : Prov. For D/d	
Creditors	50,000	1,500	20,500
Outstanding Expenses	8,000	Unexpired Insurance	5,000
C's Loan	1,20,000	Shares in X Limited	65,000
Profit and Loss Account (Profit		Plant and Machinery	1,45,500
for 2018-19)	55,000	Land and Building	5,60,000
	8,33,000		8,33,000

On April 1, 2019, they decided to admit C as a new partner for 1/4th share in profits on the following terms:

(i) C's Loan will be converted into his capital.

(ii) C will bring his share of goodwill premium by cheque. Goodwill of the firm will be calculated on the basis of 2 times of Average Profits of previous three yea₹ Profits for the year ended March 31, 2017 and March 31, 2018 were ₹ 55,000 and ₹ 1,00,000 respectively.

(iii) 10% depreciation will be charged on Plant and Machinery and Land and Building will be appreciated by 5%.

(iv) Capitals of P and K will be adjusted on the basis C's capital. Adjustments be done through bank and in case required overdraft facility be availed.

Prepare Ladger Accounts and Balance Sheet.

Solution:

Dr. **Revaluation A/c** **Cr.**

Particulars	Amount (₹)	Particulars	Amount (₹)
To plant and machinery	14,550	by Land and Building	28,000
To Gain on Revaluation			
P 6,725			
K 6,725	13,450		
	28,000		28,000

Dr. **Revaluation Capital A/c** **Cr.**

Particulars	P	K	C	Particular	P	K	C
				by balance b/d	3,00,000	2,00,000	
				by C's Loan			1,20,000
				by General reserve	50,000	50,000	
To Bank A/c	2,21,725	1,21,725		by P&L A/c	27,500	27,500	
				by Premium for Good will A/c	17,500	17,500	
To balance c/d	1,80,000	1,80,000	1,20,000	by Revaluation A/c	6,725	6,725	
	4,01,725	3,01,725	1,20,000		4,01,725	3,01,725	1,20,000

Balance Sheet

Liabilities	Amount (₹)	Assets	Amount (₹)
Capitals			
P 1,80,000		Stock	19,000
K 1,80,000		Debtors 22,000	
C 1,20,000	4,80,000	Less: PDD 1,500	20,500
Creditors	50,000	Unexpired Insurance	5,000

Outstanding expenses	8,000	Share in x ltd.	65,000
Bank overdraft	2,90,450	Plant & Machinery	1,30,950
		Land and Building	5,88,000
	8,28,450		8,28,450

Working Notes:

(1) Average Profit (3 years) $= \dfrac{55,000 + 1,00,000 + 55,000}{3}$

$= 70,000$

Goodwill of the firm $= 2 \times 70,000$

$= 1,40,000$

C's share of Goodwill $= 1,40,000 \times \dfrac{1}{4}$

$= 35,000$

(2) Total Capital of new firm $= 1,40,000 \times \dfrac{4}{1}$

$= 4,80,000$

New profit sharing ratio:

$$P = \frac{1}{2} \times \frac{3}{4} = \frac{3}{8}$$

$$K = \frac{1}{2} \times \frac{3}{4} = \frac{3}{8}$$

$$C = \frac{1}{4} \times \frac{2}{2} = \frac{2}{8}$$

New Capitals:

$$P = 4,80,000 \times \frac{3}{8} = 1,80,000$$

$$K = 4,80,000 \times \frac{3}{8} = 1,80,000$$

(3) Bank Overdraft $= 2,21,725 + 1,21,725 - 18,000 - 35,000$

$= 2,90,450$

Illustration 14.

A and B are in partnership sharing profits and losses in the ratio of 3 : 2. Their Balance Sheet as on 31/3/2019 is as under–

Liabilities	Amount ₹	Assets	Amount ₹
A's Capitals 88,000		Goodwill	5,000
B's Capitals 1,27,000	2,15,000	Land and Building	30,000
Workmen Compensation Reserve	10000	Investments (Market value ₹ 22,500)	25,000
Investment Fluctuation Reserve	5000	Debtors 47,500	45,000
	5000	Less Prov. For D/d	
Employee's Provident Fund	1,50,000	2,500	1,50,000
C's Loan		Stock	1,25,000
		Bank	1,25,000
		Advertisement Suspense A/c	5,000
	3,85,000		3,85,000

On April 1st 2019, they agreed to take C as a partner on the following conditions–

(i) A will sacrifice 1/3rd of his share with B sacrifices 1/10th from his share in favour of C.

(ii) C's loan will be converted into his capital.

(iii) C brings in 60% of his share of goodwill in cash.

(iv) Land and Building was found undervalued by ₹ 25,000 and Stock was found overvalued by ₹ 35,000.

(v) All debtors are good.

(vi) AB/R of ₹ 7004 discounted with bank was dishonoured, which is to be recorded in the books of account.

(vii) Claim on account of Workmen Compensation is ₹ 5,000.

(viii) An unrecorded accrued income of ₹ 5,000 to be provided for.

(ix) A debtor whose dues of ₹ 25,000 were written off as bad debts, paid ₹ 20,000 in full settlement.

(x) Goodwill is to be valued at 2 years' purchase of super profit of last 3 completed yea₹ Profits for year ended 31st March are as follows–

2017 – ₹ 2,40,000;
2018 – ₹ 4,65,000;
2019 – ₹ 6,90,000

The normal profit is ₹ 3,15,000.

(xi) Capital Accounts of the partners to be readjusted on the basis of their profit-sharing ratio and any excess or deficiency be adjusted by payment or receipt of amount.

Prepare Revaluation Account, Partner's Capital Account and the Balance sheet.

Solution:

Dr. **Revaluation Account** **Cr.**

Particulars		Amount ₹	Particulars	Amount ₹
To Stock A/c		35,000	By Land and Building A/c	25,000
To Gain on Revaluation transferred to–			By Provision for doubtful debt A/c	2,500
A's Capital A/c	10,500		By bad debts recovered A/c	20,000
B's Capital A/c	7000	17,500	By Accrued Income A/c	5,000
		52,500		52,500

Dr. **Partner's Capital Account** **Cr.**

Particulars	A	B	C	Particulars	A	B	C
	₹	₹	₹		₹	₹	₹
To Goodwill A/c	3,000	3,000	—	By balance b/d	88,000	127000	—
Suspense A/c	2,000	2,000	—	By C's Loan A/c	—	—	150000
To Bank A/c	—	13,000	—	By Premium for Goodwill A/c	36,000	18,000	—
To balance c/d	2,00,000	1,50,000	1,50,000	By C's current A/c	24,000	12,000	—
				By Revaluation A/c (Gain	10,500	7,000	—
				By Workmen compensation Reserve A/c	3,000	2,000	—
				By Investment Fluctuation Reserve A/c	1,500	1,000	—
				By Bank A/c	43,000	—	—
	206000	167000	150000		206000	167000	150000

Balance Sheet as at 1st April 2019

Liabilities	Amount ₹	Assets	Amount ₹
Workmen Compensation Claim	5,000	Land and Building	55,000
Employee's Provident Fund	5,000	Investment	22,500
Capital A/cs		Debtors	
A 2,00,000		(47,500 + 7004)	54,504
B 1,50,000		Stock	1,15,000
C 1,50,000	5,00,000	Bank	2,21,996
		Accrued Income	5,000
		C's Current Account	36,000
	5,10,000		5,10,000

Working Note:

1. Sacrificing share = Old share – New share

A's new share = $\frac{3}{5} - \left(\frac{1}{3} \times \frac{3}{5}\right) = \frac{3}{5} - \frac{1}{5} = \frac{2}{5}$ or $\frac{4}{10}$

B's new share = $\frac{2}{5} - \frac{1}{10} = \frac{3}{10}$

C's new share = $\frac{1}{5} + \frac{1}{10} = \frac{3}{10}$

New Profit sharing ratio A : B : C = 4 : 3 : 3

Sacrificing ratio A : B = 2 : 1

2. Calculation of C's share of Goodwill–

Average profit = $\frac{2,40,000 + 4,65,000 + 6,90,000}{3}$

= ₹ 4,65,000

Normal Profit = 3,15,000

Super Profit = Average profit – Normal profit

= ₹ 4,65,000 – ₹ 3,15,000 = ₹ 1,50,000

Firm's Goodwill = Super Profit × No. of Year's purchase

= ₹ 1,50,000 × ₹ 3,00,000

Super Profit = Average profit – Normal profit

= ₹ 4,65,000 – ₹ 3,15,000 = ₹ 1,50,000

Firm's Goodwill = Super profit × No. of yrs' purchase

= ₹ 1,50,000 × 2 = ₹ 3,00,000

C's share of goodwill = ₹ 3,00,000 × 3/10 = ₹ 90,000

Journal

Bank A/c (60% 90,000)	Dr.	54,000	
To Premium for Goodwill A/c			54,000
Premium for Goodwill A/c	Dr.	54,000	
To A's Capital A/c			36,000
To B's Capital A/c			18,000
C's Current A/c	Dr.	36,000	
To A's Capital A/c			24,000
To B's Capital A/c			12,000

3. Adjustment of Capital

Total Capital of firm = ₹ 1,50,000 × $\frac{10}{3}$ = ₹ 5,00,000

A's new Capital = ₹ 5,00,000 × $\frac{4}{10}$ = ₹ 2,00,000

B's new Capital = ₹ 5,00,000 × $\frac{3}{10}$ = ₹ 1,50,000

C's Capital = ₹ 1,50,000

4. Dr. Bank A/C Cr.

Particulars	Amount ₹	Particulars	Amount ₹
To balance b/d	1,25,000	By B's Capital A/c	13,000
To Bad debt Recovered A/c	20,000	By dishonoured B/R paid	7,004
To Premium for Goodwill A/c	54,000	By bal. c/d	2,21,996
To A's Capital A/c	43,000		
	2,42,000		2,42,000

Adjusting Capital of New Partner on the Basis of Old Partners.

Illustration 15.

Sahaj and Nimish are partners in a firm. They share profit and losses in the ratio 2 : 1. They decided to admit Gauri for 1/3 share. At the time of her admission, Balance sheet of Sahaj and Nimish was as under–

Liabilities		Amount ₹	Assets	Amount ₹
Capital A/cs			Machinery	1,20,000
Sahaj	20,000		Furniture	80,000
Nimish	80,000	2,00,000	Stock	50,000
General Reserve		30,000	Sundry Debtors	30,000
Creditors		30,000	Cash	20,000
Employees Provident Fund		40,000		
		3,00,000		3,00,000

Gauri brought her share of Goodwill in cash and proportionate capital. It was also agreed–

(i) Reduce the value of stock by ₹ 5000.

(ii) Depreciate furniture by 10% and appreciate machinery by 5%

(iii) ₹ 3000 of the debtors proved bad. A provision of 5% was to be created on S.debtors for doubtful debts.

(iv) Goodwill of the firm was valued at ₹ 45000.

Prepare Revaluation A/c, Partner's Capital A/cs and Balance sheet of reconstituted firm.

Solution:

Revaluation Account

Particulars	Amount ₹	Particulars		Amount ₹
To Stock A/c	5,000	By Machinery A/c		6,000
To Furniture	8,000	By Loss transferred to		
To (Sundry Debtors) Bad debts	3,000	Sahay's Capital A/c	7,567	
To provision for bad debts $(30,000 - 3000) \times \frac{5}{100}$	1,350	Nimish's Capital A/c	3,783	11,350
	17,350			17,350

Partners Capital Account

Particulars	Sahaj	Nimish	Gauri	Particulars	Sahaj	Nimish	Gauri
	₹	₹	₹		₹	₹	₹
To Revaluation A/c	7,567	3,783	—	By balance b/d	120000	80000	—
To Balance c/d	142433	91217	116825	By General Reserve A/c	20000	10000	—
				By Premium for Goodwill A/c	10000	5000	—
				By Bank A/c			116825
	150000	95000	116825		150000	95000	116825

Bank A/c

Particulars	Amount ₹	Particulars	Amount ₹
To Gauri's Capital A/c	116825	By balance c/d	131825
To Premium for Goodwill	15000		
	131825		131825

Balance Sheet of New Firm

As on 1st January 2019

Liabilities		Amount ₹	Assets		Amount ₹
Capital A/cs			Machinery		1,26,000
Sahaj	142433		Furniture		72,000
Nimish	91217		Stock		45,000
Gauri	116825	350475	Sundry Debtors		
Employees Provident Fund				30,000	
Creditors		40000	Less Bed debts		
		30000		(3,000)	
			Less Provision for D/d		
				(1,350)	25,650
			Cash		20,000
			Bank		1,31,825
		4,20,475			4,20,475

Working Note:

(1) Gauri's share of Goodwill

$$= 45000 \times \frac{1}{3} = ₹\ 15{,}000$$

(2) Total adjusted Capital Old

$$= ₹\ 14{,}2{,}433 + ₹\ 91{,}217 = ₹\ 2{,}33{,}650$$

Proportionate Capital Gauri (1/3 share)

$$= ₹\ 2{,}33{,}652 \times \frac{\cancel{3}}{2} \times \frac{1}{\cancel{3}}$$

$$= ₹\ \frac{2{,}33{,}650}{2} = ₹\ 1{,}16{,}825$$

PRACTICE EXERCISE

1. On 1-4-2016, A and B entered into partnership for sharing profits in the ratio of 4 : 3. They admitted C as a new partner on 1-4-2018 for 1/5th share which he acquired equally from A and B.

A , B and C earned profit at a higher rate than the Normal Rate of Return for 31-3-2019. Therefore, they decided to expand their business. To meet the requirements of addition at Capital they admitted D as a new partner on 1-4-2019 for 1/7th share in profits which he acquired from A and B in 7 : 3 ratio.

Calculate :

(a) New Profit Sharing Ratio of A : B : C for 2018-19.

(b) New Profit Sharing Ratio of A : B : C : D on D's admission.

2. (a) Vikram and Abhishek are partners sharing profits and Losses in the ratio of 8 : 5. They admit 'Avishi' and decide that the profit sharing ratio between Abhishek and Avishi shall be the same as existing between 'Vikram' and 'Abhishek'.

Calculate New Profit Sharing Ratio and Sacrificing Ratio.

(b) A, B and C are partners in a firm for the profit sharing ratio 4 : 3 : 1. They admitted 'D' as a new partner. 'A', sacrifice 1/3rd of his share in favour of 'D' and 'B', Sacrifice 1/4th from his share in favour of new partner C in neutral.

Calculate New Profit Sharing Ratio.

3. A and B share profits and losses in the ratio of 5 : 3. They admit Cas a partner who pays ₹ 54,000 as premium for goodwill for 1/5th share in the future profits of the firm.

Pass journal entries for goodwill and calculate new profit sharing ratio in each of the following case–

(a) If he acquires his share of profits in the Original ratio of existing partne₹

(b) If he acquires his share of profits in equal proportions from the existing partne₹

(c) If he acquires his share in the ratio of 3 : 1 from the existing partne₹

(d) If he acquires his share of profits as 1/6th from A and 1/30th from B.

4. Rahul and Anurag are partners sharing profits in the ratio of 3 : 2. They decided to admit Bajaj as a new partner and to share future profits and losses equally.

Bajaj brings in ₹ 50,000 as his capital. Goodwill of the firm is valued at ₹ 60,000.

Pass necessary Journal entries–

(a) When no goodwill appears in books.

(b) When goodwill appears at ₹ 50,000.

(c) When goodwill appears at ₹ 1,00,000 and goodwill is raised and written off.

5. P and Q share profits in the ratio of 7 : 3. R is admitted for 2/7th share in profits. Goodwill already appears in the balance sheet at ₹ 1,00,000. Pass necessary journal entries if–

(a) R cannot bring cash for his share of goodwill ₹ 80,000.

(b) R brings in cash ₹ 40,000 out of his share of goodwill ₹ 80,000.

6. Hari, Ravi and Shri were partners in a firm sharing profits in the ratio of 3 : 2 : 1. They admitted Mihir as a new partner for 1/7th share in the profit. The new profit sharing ratio will be 2 : 2 : 2 : 1 respectively. Mihir brought ₹ 3,00,000 for his Capital and ₹ 45000 for his 1/7th share of goodwill.

Pass necessary Journal entries in the books of the firm.

7. Balance sheet of X and Y who share profit and losses in the ratio of 5 : 3 as at 31-3-2019 was as follows–

Liabilities	Amount ₹	Assets	Amount ₹
Capital A/cs		Land and Building	3,00,000
X 2,50,000		Machinery	2,00,000
Y 1,50,000	4,00,000	Stock	70,000
Profit and Loss A/c	1,30,000	Debtors	30,000
Workmen Compensation Reserve	60,000	Cash	10,000
Sundry Creditors	50,000	Advertisement Expenditure	30,000
	6,40,000		6,40,000

They admit Z as a new partner for 1/3rd share in profits of the firm which he acquires from X and Y in the ratio of 3 : 1. Z brings in ₹ 4,00,000 as Capital. Ascertain the amount of goodwill and pass journal entries on admission of Z.

8. A, B and C are partners in a firm sharing profit and losses in the ratio of 3 : 2 : 1. D is admitted as new partner for 1/4th share in the profits of the firm, which he gets 1.8th from A and 1/16th each from B and C. The total capital of the new firm after D's admission will be ₹ 2,40,000. D is required to bring in cash equal to 1/4 of the total capital of the new firm. The capitals of the old partners also have to be adjusted in proportion of their profit sharing ratio. The capital of A, B and C after all adjustment in respect of goodwill and revaluation of assets and liabilities have been made are A ₹ 80,000; B ₹ 28,000.

Calculate the capitals of all the partners and record the journal Entries.

9. Krishna and Suresh are partners in a firm sharing profits in the ratio of 3 : 2.

Liabilities	Amount ₹	Assets	Amount ₹
Creditors	15,000	Plant and Machinery	30,000
Reserves	5,000	Patents	5,000
Capital account		Furniture	3,000
Krishan 30,000		Stock	16,000
Suresh 20,000	50,000	Debtors	15,000
		Cash	1,000
	70,000		70,000

On that data Mohan is admitted as a partner for 1/5 share on the following terms.

(a) He is contribute ₹ 14,000 cash which includes his share of premium for goodwill and capital.

(b) Goodwill is valued at 2 years, purchase of the average profits of the last four years which were ₹ 10,000; ₹ 9,000; ₹ 8,000 and ₹ 13,000 respectively.

(c) Plant to be written down to ₹ 25,000 and patents written up by ₹ 8,000.

(d) Revaluation Account, Partners' capital accounts and the balance sheet of the new firm.

10. A and B are partners in a firm. C was taken in to partners from 1-4-2019. C brought in ₹ 40,000 as his capital but he is unable to bring any amount for goodwill. Now profit sharing ratio is 3 : 2 : 1.

Their Balance Sheet as on 31-3-2019 was as follows:

Liabilities	**Amount** ₹	**Assets**	**Amount** ₹
Provision for Doubtful Depts.	4,000	Cash	10,000
Workmen Compensation fund	5,600	Sundry Debtors	80,000
Outstanding Expenses			
Creditors	3,000		
Capitals :	30,000	Stock	20,000
A			
B	50,000	Fixed Assets	38,600
	60,000	Profit and Loss	4,000
	1,52,600		1,52,600

Following terms were agreed upon–

(a) Claim on account of workmen's Compensation in ₹ 3,000.

(b) To write off Bad Debts amounting to ₹ 6,000.

(c) Creditors are to be paid ₹ 2,000 more.

(d) ₹ 2,000 be provided for an unforeseen liability.

(e) Outstanding expenses be brought down to ₹ 1,200.

(f) Goodwill is valued at 1½ years purchase of the average profits of last three years, less ₹ 12,000. Profits of 3 years amounting to ₹ 12,000; ₹ 18,000 and ₹ 30,000. Prepare Revaluation A/C, capital accounts and balance sheet.

11. Following is the balance sheet of A, B and C sharing profits and losses in the ratio of 6 : 5 : 3 respectively.

Liabilities		Amount ₹	Assets	Amount ₹
Creditors		18,900	Cash	1,890
Bills Payable		6,300	Debtors	24,460
General Reserve		10,500	Stock	29,400
Capitals :			Furniture	7,350
A	35,400		Land and Building	45,150
B	29,850		Goodwill	5,250
C	14,550	79,800		
		1,15,500		1,15,500

They agreed to take D into partnership and give him 1/8th share on the following terms–

(a) That furniture be depreciated by ₹ 920.

(b) An old customer, whose account was written off as bad, has promised to pay ₹ 2,000 in full settlement of his debts.

(c) That a provision of ₹ 1,320 be made for outstanding repair bills.

(d) That the value of land and building have appreciated to brought up to ₹ 54,910.

(e) That D should bring in ₹ 17,700 as his capital.

(f) That D should bring in ₹ 14,070 as his share of goodwill.

(g) That after making above adjustment, the capital accounts of old partners be adjusted on the basis of the proportion of D's capital to his share in business i.e., actual cash to be paid off or brought in by the old partners, as the case may be.

Pass Journal Entries and prepare the balance sheet of new firm.

12. P and R were partners in a firm sharing profits in the ratio of 3 : 1. On 31-3-2019. Q admitted to the firm. On the date of admission, the Balance Sheet of the firm was as follows:

Liabilities	Amount ₹	Assets	Amount ₹
Creditors	27,000	Bank	27,600
Bills Payable	12,000	Debtors 6,000	
Outstanding Salary	2,200	Less : Provision 400	5,600
Provision for Legal Claims	6,000	Stock	9,000
Capitals :		Furniture	4,100
P 66,000		Building	96,900
R 30,000	96,000		
	1,43,200		1,43,200

On Q's admission, it was agreed that

New profit sharing ratio of P : R : Q will be 3 : 1 : 2.

Premisses will be appreciated by 2% and furniture will be appreciated by ₹ 1,700. Stock will be depreciated by 10%. 5% provision for doubtful debts was to be made on debtors and ₹ 7,200 for legal damages. Goodwill of the firm was valued at ₹ 24,000. Q will bring sufficient amount of cash for goodwill and capital in such a way that his capital is 1/3 of the capital of the firm after his admission.

Prepare Revaluation Account, Partners Capital Accounts and the Balance Sheet of P, R and Q's.

13. Following is the balance sheet of A and B as on 31 March 2019 who were partners sharing profits and loses in the ration of 2 : 1. When they admitted C for 1/5 share on the terms that after his admission capitals of all the partners will be proportionate to their profits in the firm on the basis of the capitals of A and B after making all the adjustment.

You are required to complete the following balance sheet, revaluation A/c and capital a/cs of the partners after admission of C and the balance sheet of the Balance Sheet of A and B as on 31st March 2019.

Liabilities	Amount ₹	Assets	Amount ₹
Creditors	30,000	Building	2,00000
A's capital A/c	a	Machinery	50,000
B's capital A/c	b	Debtors 20,000	
General reserves	30,000	By provision for	
		doubtful debts (1000)	19,000
		Stock	18,000
		Goodwill	12,000
		Cash A/c	4,000
		Profit and loss A/c	c

Revaluation A/c

Liabilities	Amount ₹	Assets	Amount ₹
To stock	2000	By buiding	3000
To creditors	600	By provision for doubtful debts	500
To A's capital A/c	d		
To B's capital A/c	e		

Partners Capital A/c

Particulars	A's Capital	B's Capital	C's Capital	Particulars	A's Capital	B's Capital	C's Capital
To Goodwill	8000	4000		By balance B/d	1,30,000	1,40,000	
To profit and loss A/c	18000	9000		By general reserves	f	g	
				By premium for goodwill	20,000	10,000	
				By h	i	j	
To balance C/d	l	m	n	By cash			k
	o	p	q		o	p	q

Balance Sheet of A, B and C as on 31st March 2019

Particulars	Amount ₹	Particulars	Amount ₹
Creditors	—	Building	—
General reserves	—	Machinery	—
A's Capital A/c	—	Debtors	—
B's Capital A/c	—	By provision for doubtful debts	—
C's Capital A/c	—	Stock	—
		Goodwill	—
		Profit and loss A/c	—
		Cash	—
	—		—

14. A, B and C are partners sharing profits in the ratio of 4 : 3 : 2. Their Balance Sheet slood as under–

Liabilities		Amount ₹	Assets	Amount ₹
Outstanding Expenses		16,000	Cash	121000
Sundry Creditors		1,24,000		
Capitals : Amount				
A	7,20,000		Debtors	172000
B	4,15,000		Stock	185000
C	3,45,000	14,80000	Furniture	77000
			Plant and Machinery	465000
Reserve Fund		1800000	Landand Building	780000
		180000		1800000

D is admitted on the following terms for 1/5th share:

(a) Stock was valued at ₹ 1,72,000.

(b) Furniture were under valued by ₹ 3,000

(c) An amount due to a customer ₹ 10,000 was doubtful and provision was required.

(d) Goodwill of firm was valued ₹ 2,00,000.

(e) D was required to bring ₹ 4,00,000 and on the basis of his share, other partners will also share capital proportionately.

(f) A, B and C will share profits in the ratio of 3 : 2 : 1 were to share future profits in ratio 3 : 2.

Prepare Revaluation A/c, Partner's Capital A/c and Balance Sheet of new firm.

Multiple Choice Questions

1. When a new partner brings his share of goodwill in cash, the amount is debited to–

(a) Goodwill A/c

(b) Capital A/cs of new partner

(c) Capital A/cs of old partners

(d) Cash A/c

2. When a new partner doesn't bring his share of goodwill in cash, the amount is debited to–

(a) Cash A/c

(b) Current A/c of new partner

(c) Capital A/cs of old partners
(d) Premium for Goodwill A/c

3. It, at the time of admission, some profit and loss account balance appears in the books, it will be transferred to–
(a) Profit and loss adjustment A/c
(b) Revaluation A/c
(c) Old partner's capital account
(d) All partner's capital accounts

4. If, at the time of admission, there is some unrecorded liability, it will be–
(a) Credited to revaluation account
(b) Debited to revaluation account
(c) Debited to partner's capital account
(d) Credited to partner's capital account

5. If at the time of admission, the revaluation A/c shows a loss, it should be–
(a) Credited to old partners capital A/c in old ratio.
(b) Credited to old partners capital A/c in sacrificing ratio.
(c) Debited to old partners capital A/c in old ratio.
(d) Debited to old partners capital A/c in sacrificing ratio.

6. Revaluation A/c is a–
(a) Real account
(b) Asset account
(c) Personal account
(d) Nominal account

7. When the balance sheet is prepared after the new partnership agreement, the assets and liabilities are recorded at–
(a) Current figures
(b) Revalued figures
(c) Historical cost
(d) Realisable value

8. L and M are partners sharing profits in ratio of 3 : 2 respectively. N was admitted for $1/5^{th}$ share of profit. Machinery would be appreciated by 10% (Book value ₹ 80,000) and Building would be depreciated by 20% (₹ 2,00,000). Unrecorded debtors of ₹ 1250 would be brought into books new and a creditor amounting to ₹ 2750 died and need not pay anything on this account. What will be profit/loss on revaluation?
(a) Loss ₹ 28,000
(b) Profit ₹ 28,000

(c) Loss ₹ 40,000

(d) Profit ₹ 40,000

9. A and B are partners sharing profits in the ratio of 5 : 4. They admitted C for 1/5th profit, for which he paid ₹ 90,000 against capital and ₹ 45,000 against goodwill. Find the capital balance for each partner taking C's capital as base capital.

(a) ₹ 2,00,000; ₹ 90,000; ₹ 90,000

(b) ₹ 3,00,000; ₹ 2,40,000; ₹ 1,35,000

(c) ₹ 2,00,000; ₹ 1,60,000; ₹ 90,000

(d) ₹ 3,00,000; ₹ 1,35,000; ₹ 1,35,000

10. X and Y are partners sharing profits and losses in the ratio of 5 : 3. On admission, C brings ₹ 70,000 as cash and ₹ 40,000 against Goodwill. New profit ratio between X,Y and Z is 7 : 5 : 4. The Sacrificing ratio of X and Y is–

(a) 3 : 1 (b) 1 : 3

(c) 4 : 5 (d) 5 : 9

11. A and B are partners in a firm with capital of ₹ 1,80,000 and ₹ 2,00,000. C was admitted for 1/3rd share in profit and brings ₹ 3,40,000 as capital, calculate the amount of goodwill–

(a) ₹ 2,40,000 (b) ₹ 1,00,000

(c) ₹ 1,50,000 (d) ₹ 3,00,000

12. A, B, C and D are partne₹ A and B share 2/3rd of profits equally and C and D share remaining profits in the ratio of 3 : 2. Find the profit sharing ratio of A, B, C and D.

(a) 5 : 5 : 3 : 2 (b) 7 : 7 : 6 : 4

(c) 2.5 : 2.5 : 8 : 6 (d) 3 : 9 : 8 : 3

13. Sacrificing ratio is used to distribute .... in case of admission of a partner.

(a) Reserves

(b) Goodwill

(c) Revaluation profit

(d) Balance in profit and loss account

14. X, Y and Z are partners sharing profit in the ratio of 3 : 2 : 1. They agree to admit M into the firm. X, Y and Z agreed to give 1/3rd, 1/6th, 1/9th share of their profit. The share of profit of M will be–

(a) 11/54 (b) 12/54

(c) 13/54 (d) 14/54

15. A and B are partners sharing profits in the ratio of 2 : 3. Their balance sheet shows machinery at ₹ 4,00,000; stock at ₹ 1,60,000 and Debtors at ₹ 3,20,000. C is admitted and new profit sharing ratio is agreed at 6 : 9 : 5. Machinery is revalued at ₹ 3,40,000 and a provision is made for doubtful debts @ 2.5%. A's share in loss on revaluation amount to ₹ 20,000. Revalued value of stock will be–

(a) ₹ 98,000 (b) ₹ 1,00,000

(c) ₹ 60,000 (d) ₹ 62,000

Answers

1. (d)	**2.** (b)	**3.** (c)	**4.** (b)
5. (c)	**6.** (d)	**7.** (b)	**8.** (a)
9. (c)	**10.** (a)	**11.** (d)	**12.** (a)
13. (b)	**14.** (c)	**15.** (a)	

True or False

1. Contigent liability becoming a certain liability is debited to Revaluation Account at the time of admission of a partner.

2. On revaluation of assets and liabilities, capital accounts of old partners donot change.

3. Unless agreed otherwise, the new profit sharing ratio of old partners will be the same as their old profit sharing ratio.

4. It is necessary that partners should have capitals in their profit sharing ratios.

5. In the absence of any information, any surplus or deficiency in capital should be adjusted through current account.

6. Revaluation account is credited for bills accepted issued by creditors, not recorded in books earlier.

7. An old customer, whose account was written off as bad debts, has promised to pay but it will not be shown in revaluation account.

8. Employee's provident fund will be distributed among old partners in old ratio, at the time of admission of a partner.

9. General reserve, in balance sheet at the time of admission of partner be distributed among partners in their sacrificing ratio.

10. Existing Goodwill A/c in balance sheet is to be written off in old partners in odd ratio at the time of admission of partner.

Answers

1. True	**2.** False	**3.** True	**4.** False
5. False	**6.** False	**7.** True	**8.** False
9. False	**10.** True		

Fill in the Blanks with Appropriate Words–

1. Partner's current A/c balances in the balance sheet means that the capital A/cs are ....
2. For any decrease in the value of Asset, the Revaluation Account is ....
3. Investment fluctuation reserve is a reserve set aside out of profit to adjust the difference between .... and .... of investments.
4. C, the incoming partner, is to bring ₹ 6000 as goodwill for $1/5^{th}$ share in the firms profits. Total goodwill of the firm will be ....
5. Revaluation A/c is prepared to record the assets and liabilities at their .... values.

Answers

1. Fixed	**2.** Debited
3. Book value, Market value	
4. ₹ 30,000	**5.** Revised

EXERCISE

1. (a) 33 : 23 : 14

(b) 13 : 10 : 7 : 5

2. (a) NPSR 64 : 40 : 25; SR 8 : 5

(b) NPSR 8 : 3 : 3 : 10

3. (a) Cr. A's Capital A/c by ₹ 33750 and B's Capital A/c by ₹ 20250; NPSR = 5 : 3 : 2

(b) Cr. A's Capital A/c by ₹ 27000 and B's Capital A/c by ₹ 27000; NPSR = 21 : 11 : 8

(c) Cr. A's Capital A/c by ₹ 40500 and B's Capital A/c by ₹ 13500; NPSR = 19 : 13 : 8

(d) Cr. A's Capital A/c by ₹ 45000 and B's Capital A/c by ₹ 9000; NPSR = 55 : 41 : 24

4. (a) Bajaj (Dr.) ₹ 20,000; Rahul (Cr.) ₹ 16,000; Anurag (Cr.) ₹ 4000

(b) (i) Bajaj (Dr.) ₹ 20,000; Rahul (Cr.) ₹ 16,000; Anurag (Cr.) ₹ 4000

(ii) Rahul (Dr.) ₹ 30,000; Anurag (Dr.) ₹ 20,000; Goodwill (Cr.) ₹ 50,000

(c) (i) Rahul (Dr.) ₹ 60,000; Anurag (Dr.) ₹ 40,000; Goodwill (Cr.) ₹ 1,00,000

(ii) Goodwill (Dr.) ₹ 60,000; Rahul (Dr.) ₹ 36,000; Anurag (Cr.) ₹ 24,000

(iii) Rahul (Dr.) ₹ 20,000; Anurag (Dr.) ₹ 20,000; Bajaj (Dr.) ₹ 20,000; Goodwill (Cr.) ₹ 60,000

5. (a) Rs current A/c Dr. by ₹ 80,000; P(Cr.) ₹ 56,000 and Q(Cr.) ₹ 24000

(b) (i) Bank A/c Dr. ₹ 40,000; Premium for Goodwill A/c (Cr.) ₹ 40,000

(ii) Premium for Goodwill Dr. ₹ 40,000; R's current A/c Dr. ₹ 40,000; P(Cr.) ₹ 56,000 and Q (Cr.) ₹ 24,000.

6. Premium for Goodwill Dr. 45000; Shri Dr. 37500; Hari Cr. 67500 and Ravi Cr. 15,000.

7. Hidden Goodwill = 2,40,000; Z's share of Goodwill = 80,000

(a) Z's current Dr. 80,000; X Cr. 60,000 and Y Cr. 20,000

(b) P and L Dr. 1,30,000; WCR Dr. 60,000; X Cr. 118750 and Y Cr. 71250

8. A,B and D will bring 10,000; 35,000; 60,000 respectively while C will withdraw 3000.

A's capital = ₹ 9000; B's capital = ₹ 65,000; C's capital = ₹ 25,000; D's capital = ₹ 60,000.

9. Profit on Revaluation = ₹ 3000

Krishna's Capital A/c = ₹ 37200

Suresh's Capital A/c = ₹ 24800

Mohan's Capital A/c = ₹ 10000

Balance Sheet Total = ₹ 87000

10. Loss on Revaluation = ₹ 4200

A's Capital A/c = ₹ 47200

B's Capital A/c = ₹ 60200

C's Capital A/c = ₹ 40000

Balance Sheet Total = ₹ 185600

11. Profit on Revaluation = ₹ 9520

A's Capital A/c = ₹ 44100

B's Capital A/c = ₹ 36750

C's Capital A/c = ₹ 22050

D's Capital A/c = ₹ 14700

Balance Sheet Total = ₹ 144120

13. (a) 130000 (b) 140000

(c) 27000	(d) 600
(e) 300	(f) 20000
(g) 10000	(h) Revaluation A/c
(i) 600	(j) 300
(k) 72975	(l) 144600
(m) 147300	(n) 72975
(o) 170600	(p) 16300
(q) 72975	

Balance Sheet Total = ₹ 395475

14. Loss on Revaluation = ₹ 20000

A's Capital A/c = ₹ 780000

C's Capital A/c = ₹ 337000

Balance Sheet Total = ₹ 1740000

CHAPTER 5

RETIREMENT/DEATH OF A PARTNER

Retirement of a Partner	Retirement of a partner means ceasing to be partner of the firm. A partner may retire 1. If there is Agreement to this effect 2. All Partners' give consent 3. At Will by giving written notice
Amount due to Retiring/ Deceased Partner	1. Credit Balance of his capital. 2. Credit Balance of his current account (if any). 3. Share of Goodwill. (To be given by gaining partners) 4. Share of Reserves or Undistributed Profits. 5. His share in the profit on revaluation of assets and reassessment of liabilities. 6. If retirement is during the year, the retiring partner will be given. Share in profits up to the date of retirement. 7. Interest on capital if involved. 8. Salary if any up to the date of Retirement/Death Deductions from the above Sum (To be Debited to the Capital Account) 1. Debit balance of his current account (if any) 2. Share of existing Goodwill to be written off. 3. Share of Accumulated loss. 4. Drawings and interest on drawings (if any). 5. Share of loss on account of Revaluation of assets and liabilities. 6. His share of business loss up to the date of Retirement/Death (To P & L suspense A/c)
Gaining Ratio	The ratio in which the continuing partners have acquired the share from the retiring/deceased Partner is called Gaining Ratio.

Sacrificing Ratio v/s Gaining Ratio	
Why the Retiring or Deceased Partner is entitled to his share of Goodwill at the time of Retirement/Death?	Because the Goodwill has been earned by the firm with the efforts of the existing partners, hence at the time of retirement/ death of a partner it is valued as per agreement.
Hidden Goodwill	If the firm has agreed to settle the retiring or deceased partner by paying a lump sum amount, then the amount paid to him in access of what is due shall be treated as his share of goodwill and known as hidden goodwill
Disposal Amount due to Retiring partner	The outgoing partners' account is settled as per the terms of partnership deed i.e. 1. In lump sum immediately 2. In various instalments with or without interest as agreed 3. Partly in cash immediately and partly in instalments at the agreed intervals
What are the provisions if the Retiring Partner is not paid fully at the time of Retirement	In the absence of any agreement, Section 37 of the Indian Partnership Act, 1932 is applicable, which states that the outgoing partner has an option to receive 1. Either Interest @ 6% till the date of payment 2. Such share of Profits which has been earned with his/her money
Deceased Partner share of profit may be calculated	1. On the basis of last years profit (On Average Basis) 2. On the basis of sales

Points to remember -

1. When the question is silent about the amount payable to retiring partner, then the whole amount payable is transferred to his/her loan account.
2. In case of death of a partner, Capital Account of the Deceased Partner is closed by transferring the whole amount to the executors of the deceased Partner.
3. Any payment to the executors of the deceased partner is made through executor's account, not through the deceased partners' capital account.
4. Goodwill already appeared in the books must be written off in old PSR.
5. All accumulated profits and all accumulated losses are to be distributed among old partners in their old PSR.

6. In case of specific fund, like investment fluctuation fund, market value of the investment must be considered. For workman compensation fund, actual liabilities must be considered (to be deducted from fund).
7. Revaluation profit/loss is to be distributed in old PSR.

Accounting Treatment

1. Calculation of new profit-sharing ratio and gaining ratio
2. Treatment of goodwill.
3. Revaluation account preparation with the adjustment in respect of unrecorded assets/liabilities.
4. Distribution of reserves and accumulated profits/loss.
5. Ascertainment of share of profit/loss till the date of retirement/death.
6. Adjustment of capital if required.
7. Settlement of the Accounts due to Retired/Deceased partner.

1. New Profit Sharing Ratio & Gaining Ratio

Calculation of the two ratios.

Following situations may arise

(i) When no information about new ratio or gaining ratio is given in the question

> In this case it is considered that the share of the retiring partner is acquired by the remaining partners in the old ratio. Then no need to calculate the new ratio/gaining ratio as it will be the same as before.

(ii) Gaining ratio is given which is different from the old ratio in this case,

> New share of continuing partner = old share + share gained from the outgoing partner.

(iii) If the new ratio is given

> Gaining ratio = New Ratio - Old ratio

2. Treatment Of Goodwill.

Steps to be followed

1. When old goodwill appears in the books then first of all this is written off in the old ratio. Remember **Old Goodwill in Old Ratio.**

All Partner's capital A/c Dr.
To Goodwill A/c

2. After written off old goodwill, adjustment of retiring partner's share of goodwill will be made through the following journal entry

Gaining Partner's Capital A/c	Dr. (in gaining ratio)
To Retiring / Deceased Partner's	Current A/c (if any)
To Retiring/Deceased Partners'	Capital A/c

OR

Alternative entry with raising of goodwill of its value and written off:-

1. Journal entries passed are : -

Goodwill A/c Dr. (Current value of goodwill)

To all partners capital A/c

(Being the goodwill raised is current value) (In old profit sharing ratio)

2. Counting partners capitals A/c Dr. (In new profit sharing ratio)

To goodwill A/c

(Being the goodwill written of)

3. Revaluation of Assets and Reassessment of Liabilities

Revaluation A/c is prepared in the same way as in the case of admission of a new partner. Profit and loss on revaluation is transferred among all the partners in old ratio.

4. Adjustment of Reserves and Surplus (Profits)

(Appearing in the Balance Sheet - Liability Side)

(a) General Reserve A/c Dr.

Reserve Fund A/c Dr.

Profit & Loss A/c (Credit Balance) Dr.

To all partners' Capital/Current A/c (in old ratio)

(b) Specific Funds - if the specific funds such as workmen's compensation fund or investment fluctuation fund are in excess of actual requirement, the excess will be transferred to the Capital A/c in old ratio.

Workmen Compensation Fund A/c Dr.

Investment Fluctuation Funds A/c Dr

To All Partner's Cap A/c's (in old Ratio)

(c) For distributing accumulated losses (P & A/c Dr. Balance)

All partner's Capital/Current A/c Dr. (in old ratio)
To P & L A/c

5. Adjustment of Capitals

At the time of retirement /death, the remaining partners may decide to adjust their capitals in their new profit sharing Ratio. Then following situation may arise

Case 1 . When the total capital of the new firm is not given in the question

- Then the sum of their adjusted capitals of remaining partners' will be treated as the total capital of the new firm which will be divided in their New Profit Sharing Ratio.
- Excess or Deficiency of capital in the individual capital A/c is calculated.
- Such excess or shortage is adjusted by withdrawal or contribution in cash or transferring to Partner's current A/cs.

Journal Entries

(a) For excess Capital withdrawn by the partners
Partner's Capital A/c Dr.
To Cash/Bank A/c / Partner's Current A/c

(b) For deficiency, cash will be brought in by the partner
Cash/Bank A/c /Partner's Current A/c Dr.
To Partner's Capital A/c

Case 2. When the capital of the new firm as decided by the partners is specified, divide the capital in new profit sharing ratio and make adjustments accordingly.

Case 3. When the amount payable to retiring partner will be contributed by continuing partners in such a way that their capitals are adjusted proportionate to their new profit sharing ratio then calculations will be as under

> Total capital of the new firm = balance in capital accounts of remaining partners + amount payable to retiring/deceased partner

(Retirement of a Partmer)

Illustration 1: A, B and C are partners sharing profit and loss in the ratio of 3:2:1 then on retirement of a partner; the gaining ratio/new ratio will be

On A's Retirement ratio between B and C will be 2: 1

On B's Retirement ratio between A and C will be 3: 1

On C's Retirement ratio between A and B will be 3: 2

Illustration 2: A, B & C share profit and losses in the ratio 3:2:1. On C's death his share is taken by A and B in the ratio of 2:1 Calculate new ratio.

Solution: In this case gaining ratio = 2:1 (given)

A's old share = 3/6, B's old share = 2/6 & C's share = 1/6

A's gain = 2/3 of C's share 2/3* 1/6 = 2/18

B's gain = 1/3 of C's share = 1/3* 1/6 = 1/18

A's new share = A's old + A's gain

= 3/6 + 2/18 = 11/18

B's new share = B's old share + B's gain

= 2/6 + 1/18 = 7/18

New ratio = 11:7

Illustration 3 : A, B and C are partners in the ratio of 3:2:1. C retires and A & B decide to share future profit in the ratio of 5:3. Calculate Gaining ratio of A and B.

Solution: A's Gain = 5/8- 3/6=3/24

B's Gain = 3/8-2/6 = 1/24

Gaining ratio = 3:1

Illustration 4: A, B and C are partners sharing profits and losses in the ratio of 3:2:1. B retires and gifted $\frac{1}{2}$ of his share in favour of A and sells remaining share to A and C in the ratio of 1:2. Find out gaining ratio and new ratio.

Solution:

B's share = $\frac{2}{6} = \frac{1}{3}$; gifted to A = $\frac{1}{3} \times \frac{1}{2} \times \frac{1}{6}$

Remaining shares of B = $\frac{1}{3} - \frac{1}{6} = \frac{2-1}{6} = \frac{1}{6}$

A's gain = Gifted share of B + Share sold by B

Share sold by B to A = $\frac{1}{6} \times \frac{1}{3} = \frac{1}{18}$

A's gain = $\frac{1}{6} + \frac{1}{18} = \frac{3+1}{18} = \frac{4}{18}$ or $\frac{2}{9}$

C's gain = $\frac{1}{6} \times \frac{2}{3} = \frac{2}{18}$ or $\frac{1}{9}$

Gaining ratio = $\frac{2}{9}:\frac{1}{9}$ or 2 : 1

A's new share = $\frac{3}{6}+\frac{2}{9}=\frac{9+4}{18}=\frac{13}{18}$

C's new share = $\frac{1}{6}+\frac{1}{9}=\frac{3+2}{18}=\frac{5}{8}$

New profit sharing ratio of A and C is $\frac{13}{18}:\frac{5}{18}$ or 13 : 5

Illustration 5: A, B and C were partners sharing profits in the ratio of 6:4:5. On 1st April, 2016, B retired from the firm and the new profit sharing ratio between A and C was decided as 11:4. On B's retirement, the goodwill of the firm valued at ₹ 1,80,000. Pass journal entry for treatment of goodwill on B's retirement.

(CBSE Delhi)

Solution:

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Date	Particulars	L.F.	Dr. (₹)	Cr. (₹)
2016 April,1	A's Capital A/c Dr.		60,000	
	To B's Capital A/c			48,000
	To C's Capital A/c			12,000
	(Being adjustment of goodwill made on B's retirement)			

Working Notes:

Gaining Ratio = A's gain = $\frac{11}{15}-\frac{6}{15}=\frac{11-6}{15}=\frac{5}{15}$

C's gain = $\frac{4}{15}-\frac{5}{15}=-\frac{1}{15}$ (sacrificed)

B's share is goodwill = 1,80,000 × $\frac{4}{15}$ = ₹ 48,000

A will compensate C to the extent of sacrifice made by C i.e. 1,80,000 × $\frac{1}{15}$

= ₹ 12,000

Illustration 6: M. N. & P are partners in a firm. P retires & the goodwill of the firm is valued at ₹ 30,000. M & N decide to share future profits in the ratio of 3:2. Pass necessary

1. If goodwill A/c already appears in the books at ₹ 18,000
2. When goodwill account raised and written books.

Solution:

Old ratio of M, N & P = 1:1:1 (since profit sharing ratio is not given it is treated as equal) New ratio = 3:2

M's gain = 3/5 - 1/3 = 4/15
N's gain = 2/5 - 1/3 = 1/15
Gaining ratio = 4 : 1

Ps share of goodwill = 30,000 ×1/3
= ₹ 10,000

Case 1. If goodwill A/c appears in the books at ₹ 18,000.

Journal

Date	Particulars	LF.	Debit (₹)	Credit (₹)
1.	M's Capital A/c Dr. N's Capital A/c Dr. P's Capital A/c Dr. To Goodwill A/c (Being the existing goodwill written off in old ratio i.e. 1:1:1)		6,000 6,000 6,000	 18,000
2.	Goodwill Dr. To M's Capital A/c To N's Capital A/c To P's Capital A/c (Being adjustment made for goodwill on retirement in gaining ratio i.e. 4:1)		30,000	 10,000 10,000 10,000
3.	M's Capital A/c Dr. N's Capital A/c Dr. To Goodwill (Goodwill writing off immediately with new profit ratio 3.2)		18,000 12,000	 30,000

Case 2. When no goodwill account appears in the book entry as 2 & 3 above.

Illustration 7 : R, S & T are partners in a firm sharing profit & loss in the ratio of 2:2:1. T Retires and his balance in capital a/c after adjustment for reserve & revaluation of assets & liabilities comes out to be ₹ 50,000. R &S agree to pay him ₹ 60,000. Give journal entry for the adjustment of goodwill.

Solution:

New ratio between R & S = gaining ratio = 2:2 or 1:1

T's share of goodwill (hidden) = 60,000 – 50,000 = 10,000

Hence adjustment entry is

Journal

Date	**Particulars**	**L.F.**	**Debit (₹)**	**Credit (₹)**
	R's capital A/c Dr.		5,000	
	S's capital A/C Dr.		5,000	
	To T's capital A/c			10,000
	(T's share of goodwill adjusted in gaining ratio i.e. 1:1			

Illustration 8: X, Y and Z are partners sharing profits in the ratio of 3:2:1. Y retires selling his share to X and Z for ₹ 36,000; ₹ 24,000 being paid by X and ₹ 12,000 by Z. The profit after Y's retirement is ₹ 63,000.

Pass necessary journal entries to

(i) Record the sale of Y's share to X and Z and

(ii) Distribute the profit between X and Z.

Solution:

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Date	Particulars	L.F.	Debit (₹)	Credit (₹)
(i)	X's Capital A/c Dr.		24,000	
	Z's Capital A/c Dr.		12,000	
	To Y's Capital A/c			36,000
	(Being Y's share is purchase by X and Z on his retirement)			
(ii)	Profit & Loss Appropriation A/c Dr.		63,000	
	To X's Capital A/c			45,500
	To Y's Capital A/c			17,500
	(Being profit distributed between X and Z in new profit sharing ratio			

Working Notes:

Gaining ratio= 24000:12000 = 2:1

Y's share = $\frac{2}{6}$

X's gaining share = $\frac{2}{6} \times \frac{2}{3} = \frac{4}{18}$

Z's gaining share = $\frac{2}{6} \times \frac{1}{3} = \frac{2}{18}$

X's new share is = $\frac{3}{6} + \frac{4}{18} = \frac{9+4}{18} = \frac{13}{18}$

Z's new share is = $\frac{1}{6} + \frac{2}{18} = \frac{5}{18}$

New Profit sharing Ratio between X and Z = 13: 5

Illustration 9: A,B and C are partner sharing profits in the ration of 3:2:1 . A dies on 31st July 2015. The profits of the firm for the year ending 31st March 2015, were 42,000. Calculate as share of profit :-

A). On time Basis from 1 April to 31st July 2015 on the basis of Last year's Profrit

(B). On sales basis Sales for the last year ₹ 2,10,000 and for current year upto 31st July are ₹ 90,000?

Solution

(A). A's Profit = Preceding year's profit × Proportionate Period × Share of A

= ₹ 42,000 × 4/12 × 3/6

= ₹ 7,000

Journal Entries

Date	**Particulars**	**L.F**	**Debit (Rs)**	**Credit (₹)**
2015 July 31	Profit and Loss Suspense A/c Dr. To A's Capital A/c (A's share of profit transferred to his capital A/c)		7,000	7,000

(B). $= \dfrac{90,000}{2,10,000} \times 42,000$

= ₹ 18,000

A's share = ₹ 18,000×3/6

= ₹ 9,000

Illustration 10. Anjali, Muskan and Jasmeet were partners in a firm sharing profits in capitial ratio. On 31st March, 2020. Their Balance sheet was as follows:

Liabilities	**(₹)**	**Assets**	**(₹)**
Creditors	30,000	Cash	12,000
Investment Fluctuation reserve	10,000	Bank balance	3,000
Workmen compensation Reserve	12,000	Bulding Furniture	6,00,000 1,00,000
		Investments stock	1,00,000 2,00,000
		Debtors	60,000
Profit and Loss A/c	20,000	Less : PDD (3,000)	57,000
Capitals			
Anjali 4,00,000			
Muskan 3,00,000			
Jasmeet 3,00,000	10,00,000		
	10,72,000		10,72,000

On the above date, Muskan retired and Anjali and Jasmeet agreed to continue the business with following terms:

(1) Goodwill of the firm was valued at ₹ 70,000.

(2) Workmen compensation claim is estimated 25% more than the balane in workmen compensation reserve.

(3) Investment were sold to muskan for cash ₹ 95,000.

(4) Provisian for doubtful debts is to be maintained at the existing rate after writing off. Some debtors as bad debts, and the new provision for doubtful debts amounts to ₹ 2,500.

(5) Furitture prchased for ₹ 40,000 wrongly included in the value of building.

(6) Building to be depreciated by 10%.

(7) Amount due to muskan was transterred to her loan account after paying 30% of the tatal dues, By taking necessary loan from bank if any.

Prepare Revaluation A/c Partners capital AICS and the Balance sheet after Muskan's Retirement.

Solution:

Dr. Revaluation A/c Cr.

Particulars	₹	Particulars	₹
To workmen			
Compensation claim	3,000		
To Bad debts	7,000		
To Provision for doubtful debts	2,500	by Loos on Revalvation A/c	68,500
	56,000		
	68,500		68,500

Dr. Partner's Capital A/cs Cr.

Particulars	Anjali	Muskan	Jasmeet	Particulars	Anjali	Muskan	Jasmeet
To Revalva-tions A/c	27,400	20,550	20,550	by bal. b/d	4,00,000	3,00,000	3,00,000
To muskan	12,000		9,000	by IFRA/C	2,000	1,500	1,500
To BankA/c Cash A/c		92,385		by P&LA/C	8,000	6,000	6,000
To Muskan's Loan	2, 15,565			By Anjali		12,000	
To balance c/d	3,70,600		2,77,950	by Jasmeet		9, 000	
	4,10,000	3,28,500	3,07,500		4,10,000	3,28,500	3,07,500

Balance Sheet

Liabilities		Amount (₹)	Assets	Amount (₹)
Creditors		30,000	Cash	14,615
Workmen			Bank Balance	3,000
Compensation claim		15,000	Bulding	5,04,000
Muskan's Loan		2,15,565	Furniture	1,40,000
Capital A/cs			Stock	2,00,000
Anjali	3,70,600		Debtors	47,500
Jasmeet	2,77,950	6,48,550		
		9,09,115		9,09,115

Working Note:

(1) Debtors 60,000

Less: bad debts (10,000)
50,000

Less: PDD (2,500)
47,500

Rate of Provision for doubtfuldebts = $\frac{3,000}{60,000} \times 100$ = 5 %

debtors after bad debts = $\frac{2,500}{5} \times 100$ = 50,000

$\therefore$ bad debts = 60,000 – 50,000 = 10,000

Illustration 11. P, Q and R are partners in a from whose B/s as an 31.3.2019 was as follows:

Liabilities		Amount (₹)	Assets	Amount (₹)
Creditors		18,240	Bank	16,240
Gen. Reserve		7,500	Debtors	22,500
Capitals			Plant	26,500
Capitals			Furniture	5,000
P	20,000			
Q	14,500			
R	10,000	44,500		
		70,240		70,240

Retired with the following terms:

(i) To reduce plant and furniture by 5% and 10% resp.

(ii) To provide for PDD @ 5% on debtors.

(iii) Creditors are to be for paid more ₹ 3050.

(iv) Goodwill was valued at ₹ 12,000

(v) New ratio 5 : 3.

(vi) Q should be paid and the amount required to pay Q shall be brought in by P and R in such a way that their capitals are in new profit sharing ratio. Prepare revalvation A/c. Partrner's capital A/c and B/S.

Ans. Dr. Revaluation A/c Cr.

Particulars	**Amount (₹)**	**Porticulars**	**Amount (₹)**
To plant	1,325		
To Furniture	500		
To PDD	1125	by loss on Revalation	6,000
To Creditors	3050		
	6,000		6,000

Dr. Cr.

Particulars	**P**	**Q**	**R**	**Particular**	**P**	**Q**	**R**
To (loss on Rev. Revalvatin)	2,000	2,000	2,000	by bal. b/d	20,000	14,500	10,000
To Q's Cap	3,500		500	by Gen. Reserve	2,500	2,500	2,500
To Bank A/c		19,000		by R's cap		3500	
				by bank		500	
To bal. C/d	28,750		17,250	by bank	11,750		7250
	34,250	21,000	19,750		34,250	21,000	19750

B/S

Liabilties	**Amount (₹)**	**Assets**	**Amount (₹)**
Creditors (1824 + 3050)	21,290	Bank	16,240
Capitals		Debtors 22,500	
		Less: PDD 1125	21,375
Capitals		Plant	25,175
P 28,750		Fruniture	4,500
R 17,250	46,000		
	67,290		67,290

W.N.

(1) Q's Share of G/w = $12,000 \times \frac{1}{3} = 4,000$

(2) Gaining Ratio

$$P = \frac{5}{8} - \frac{1}{3} = \frac{7}{24}$$

$$R = \frac{3}{8} - \frac{1}{3} = \frac{1}{24} = 7 : 1$$

(3) Tatal Capital of new form = adjusted capitals of P and R + amount payable to Q

= 17,000 + 10,000 + 19,000 = 46,000

(4) New Capitals

$$P = 46,000 \times \frac{3}{8} = 17,250$$

$$R = 46,000 \times \frac{3}{8} = 17,250$$

DEATH OF A PARTNER

Accounting treatment in the case of death is same as in the case of retirement except the following:

1. The deceased partners claim is transferred to his executer's account.
2. Normally the retirement takes place at the end of the Accounting Period but the death may occur at any time. Hence the claim of deceased partner shall also include his share of profit or loss, interest on capital and drawings if any from the date of the last balance sheet to the date of his death.

- Calculation of Profits/ Loss for the intervening Period

  It is calculated by any one of the two methods given below:

a. On Time Basis: In this method proportionally profit for the time period is calculated either on the basis of last year's profit or on the basis of average profits of last few years and then deceased partner's share is calculated based on his share of profits.

b. On Turnover or Sales Basis: in this method the profits up to the date of death for the current year are calculated on the basis of current year's sales up to the date of death by using the formula.

Profits for the current year up to the date of death =

Sales of the current year up to the date of death/total sales of last year x Profit for the last year.

Then from this profit the deceased partner's share of profit is calculated.

If the remaining partners decides to change their profit sharing ratio in new firm, then the adjustment entry for deceased partners' share in current year's profit will be passed.

Payment for retiring deceased partner :-

a. When payment is made in full

retiring deceased partners capitals A/c to bank Dr.

b. When Payment is made in instalments. When payment is made in instalments interest is paid on instalments at agreed price or @ 6% per annum. Journal entries are

(i) When interest is allowed

Interest A/c Dr.

To Deceased Partner's Executor or retiring partner loan A/c

(ii) When instalment is paid

retiring partners loan A/c or Desease partners executor a = A/c Dr.

To Bank A/c (interest & instalment amount)

Illustration 12.

Rinku, Pinku and Tinku were in partnership sharing profits in 3 : 2 : 1. On Ist April, Pinku retires from the firm. On that date, their balance sheet was as follows:

Liabilities	Amount (₹)	Assets		Amount (₹)
Trade creditors	5,700	Cash in Hand		9,000
Outstanding expenses	4,500	Debtors	16,000	
General Reserve	10,500	Less: Prevision	1,000	15,000
		Stock		12,000
		Building		22,500
Workmen compensation Reserve	4,8000	Investments		8,000
Capitals		Plant		4,000
Rinku 20,000				
Pinku 15,000				
Tinku 10,000	45,000			
	70,500			70,500

Adjustments:

(1) Goodwill of the firm valued at ₹ 15,000.

(2) Rinku took over investments at an agreed value of ₹ 7,200 for cash.

(3) Building and plant were revalued at ₹ 24,300 and ₹ 3,600 respectively.
(4) Provision for doubtful debts to be increased to ₹ 2,950
(5) Outstanding expenses to be reduced to ₹ 3,750.
(6) Claim on account of workmen compensation is ₹ 1,800.
(7) Pinku be paid ₹ 5,000 in cash and balance will be transferred to his Loan A/c.
(8) Rinku and Tinku decided to adjust their capital in profit sharing ratio after Pinku's retirement, by bringing or withdrawing necessary cash.
Prepare Revaluation A/c partner's Capital A/c and Balance sheet after Pinku's retirement.

Dr. **Revaluation A/c** **Cr.**

Particulars	Amount (₹)	Particulars	Amount (₹)
To Investments	800	by outstanding expenses	750
To Plant	400	by building	1,800
To Provision for doubtful debts	1,950	by Loss on Revaluation	600
	3,150		3,150

Dr. **Partners' Capital A/c** **Cr.**

Particular	Rinku	Pinku	Tinku	Particular	Rinku	Pinku	Tinku
To Pinku's Capital	3,750		1,250	by balance b/d	20,000	15,000	10,000
To Revaluation A/c (Loss)	300	200	100	by General Reserve	5,250	3,500	1,750
To Cash A/c To Pinku's Loan		5,000 19,300		by Workmen Compensation Reserve	1,500	1,000	500
Cash A/c			2,500	by Rinku's Capital		3,750	
				by Tinku's Capital		1,250	
To balance c/d	25,200		8,400	by Cash A/c	2,500		
	29,2500	24,500	12,250		29,250	24,500	12,250

Balance Sheet

Liabilities	Amount (₹)	Assets		Amount (₹)
Trade creditors	5,700	Cash in Hand (900 + 2500 – 2500 + 7200 – 500)		11,200
Outstanding Expenses	3,750	Debtors	16,000	
		Less: Provision	2,950	13,050
Workmen Compensation claim	1,800	Stock		12,000

Pinku's Loan	19,300	Building	24,300
Capital		Plant	3,600
Rinku 25,200			
Tinku 8,400	33,600		
	64,150		64,150

Working Notes:

(1) Pinku's share of Goodwill $= 15{,}000 \times \frac{2}{6} = 5.000$

(2) Total Capital of new firm = adjusted capital of Rinku + adjusted capital of Tinku
= 22,700 + 10,900 = 33,600

to be divided in 3 : 1

Retirement of a Partner

Illustration 13

Raman, Ayush and Aalok are partners in a firm, sharing profits and losses in 5 : 3 : 2. On Ist April, 2021 Raman decided to retire from the firm.

After making all the adjustments in his capital on the date of retirement his claim amounted to ₹ 2,50,000.

You are required to pass journal entries in the following cases:

(i) When no information is given regarding settlement of Raman's Claim.

(ii) When Raman's claim is to be settled immediately in full. Available cash and bank balance on Ist April, 2021 was ₹ 90,000.

(iii) When Raman's claim is to be paid in full and if required, bank load should be taken to the extent of shortage of funds.

(iv) Raman is to paid ₹ 80,000 by a cheque accepting a 3 month draft of ₹ 50,000 and balance is to be transferred into his Loan A/c.

Solution **Journal**

Date	Particular	L.F.	Dr.₹	Cr.₹
(i)	Raman Capital A/c Dr.		2,50,00	
	To Raman's Loan A/c			2,50,000
	(Amount due to Raman transferred to his Loan A/c)			
(ii)	Raman's Capital A/c Dr.		2,50,000	
	To Bank A/c			90,000
	To Bank overdraft			1,60,000
	(Raman paid in full by availing overdraft facility of ₹ 1,60,000)			
(iii)	Bank A/c Dr.		1,60,000	
	To Bank Loan A/c			1,60,000

	(Loan of ₹ 1,60,000 taken from bank)			
	Raman's Capital A/c Dr.		2,50,000	
	To Bank A/c			2,50,000
	(Full payment made to Raman)			
(iv)	Raman's Capital A/c Dr.		2,50,000	
	To Bank A/c			80,000
	To Bills Payable A/c			50,000
	To Raman's Loan A/c			1,20,000
	(Paid Raman ₹ 80,000 by cheque accepting a draft ₹ 50,000 fro 3 months and balance transferred to his Loan A/c)			

Illustration 14.

Seeta, Geeta and Anita are partners in a firm. Geeta retires on Ist April, 2018. On the date of retirement 60,000 is due to her after all adjustments. It is agreed to pay her 20,000 on the date of retirement and balance into four half yearly in instalments (equal) along with Interest @ 10% p.a. Books are closing on 31st march every years. First instalment is due on 31 st Dec, 2018. Prepare Geeta's Loan A/c till final settlement.

Solution:

Dr. Geeta's Loan A/c Cr.

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2018 July1	To Bank A/c	20,000	2018 July 1	by Geeta's Capital A/c	60,000
2018 Dec 31	To Bank A/c (10,0000 + 2,000)	12,000	Dec 31	by Interest A/c (40,000 × $\frac{10}{100} \times \frac{6}{12}$)	2,000
			2019 March 31	by Interest A/c (30,000 × $\frac{10}{100} \times \frac{3}{12}$)	750
2019 March 31	To balance c/d	30,750			
		62,750			62,750
2019 June 30	To Bank A/c (10,000 + 750 + 750)	11.500	2019	by balance b/d	30,750
Dec 31	To Bank A/c (10,000 + 1,000)	11,000	June 30	by Interest A/c (30,000 × $\frac{10}{100} \times \frac{3}{12}$)	750

			31 Dec	by Interest A/c (20,000 × $\frac{10}{100} \times \frac{6}{12}$)	1,000
			2020 March 31	by Interest A/c (1,000 × $\frac{10}{100} \times \frac{3}{12}$)	250
2020 March 30	To balance c/d	10,250			
		32,750			32,750
			2020 April 1	by balance c/d	10,250
2020 June 30	To Bank A/c (10,000 + 250 + 250)	10,500	June 30	by Interest A/c (10,000 × $\frac{10}{100} \times \frac{3}{12}$)	250
		10,500			10,500

Illustration 15.

Ram, Lakhan and Bharat are partners in a firm. On Ist April 2015. Bharat retires. On the date of retirement ₹ 1,20,000 was due to him after all the adjustments. Ram and Lakhan agreed tow pay him this amount into three instalments of ₹ 40,0000 including interest @ 10% p.a. on the outstanding amount and the balance including interest in the fourth years, at the end of each years. Prepare Bharat's Loan A/c till the date of final settlement.

Dr. **Bharat's Loan A/c** **Cr.**

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2016 March 31	To bank A/c	40,000	2015 April 12	by Bharat's Capital	1,20,000
			2016 March 31	by Interest A/c (1,20,000 × $\frac{10}{100}$)	12,000
March 31	To balance c/d	92,000			
		1,32,000			1,32,000
			2016 April 1	by balance b/d	92,000
2017 March 31	To Bank A/c	40,000	2017 March	by Interest A/c (92,000 × $\frac{10}{100}$)	9,200

March 31	To balance c/d	61,200			
		1,01,200			1,01,200
			2017 April 1	by balance b/d	61,200
2018 March 31	To Bank A/c	40,000	2018 March 31	by Interest A/c $(61,200 \times \frac{10}{100})$	61,20
March 31	To balance c/d	27,320			
		67,320			67,320
			2018 April 1	by balance c/d	27,320
2019 March 31	To Bank A/c	30,052	2019 March 31	by Interest A/c $(27,320 \times \frac{10}{100})$	2,732
		30,052			30,052

Illustration 16: Karma, Varma and Sharma are partners sharing profit and losses in the ratio 4 : 3 : 2. Verma died after 3 months of closing books of account. His share of profit calculated as 9,000. Pass Journal entries if:

(i) There is no change in profit sharing ratio

(ii) New profit sharing of karma and sharma is 1 : 1.

Sol. (i) P & C suspense A/c Dr. 9000

To Verma's Cap A/c9,000

(ii) Gaining Ratio = New Ratio – Old Ratio

$$\text{Karma} = \frac{1}{2} - \frac{4}{9} = \frac{1}{18}$$

$$\text{Sharma} = \frac{1}{2} - \frac{2}{9} = \frac{5}{18} = 1 : 5$$

Karma's Cap A/c Dr. 1,800

Sharma's cap A/c Dr. 7,200

To verma's Cap A/c 9,000

Illustration 17: What will be the entries if in above Question there was a share of loss of ₹6,000 of verma.

Sol. (i) Verma's cap A/c Dr.. 6,000

To P & L Suspense A/c 6,000

(ii) Verma's Cap A/c Dr... 6,000

To Karma's cap A/c 1,000

To Sharma's cap A/c 5,000

Illustration 18: The balance sheet of P, Q & R as at 31st Dec.2014 was as follows.

Liabilities	₹	Assets	₹
Bills Payable	20,000	Cash at Bank	1,58,000
Employees Provident Fund	50,000	Bills Receivable	8,000
Workmen compensation	90,000	Stock	90,000
reserve		Sundry Debtors	1,60,000
Loan	1,71,000	Furniture	20,000
Capital Accounts		Plant & Machinery	65,000
P 2,27,500		Building	3,00,000
Q 1,52,500		Advertisement	
R1,20,000	5,00,000	Suspense	30,000
	8,31,000		**8,31,000**

The profit ratio was 3:2:1 R died on 30th April 2015. The partnership deed provides that:

a. Goodwills is to be calculated on the basis of 3 years purchase of preceding 5 years' average profits. The profits were 2014. ₹ 2,40,000, 2013 ₹ 1,60,000, 2012 ₹ 2,00,000, 2011 ₹ 1,00,000 and 2010 - ₹ 50,000.

b. Deceased partner should be given share of profits upto the date of death on the basis of previous year profits.

c. The assets have been revalued as under
Stock ₹ 1,00,000, Debtors ₹ 1,50,000, Furniture ₹ 15,000. Plant and Machinery ₹ 50,000, Building ₹ 3,50,000. A bill for ₹ 6000 was found worthless.

d. A sum of ₹ 72,333 was paid immediately to R's executor & balance is paid in two equal instalments (annual) with interest of 10% p.a. On outstanding amount. Ist instalment was paid on 30th April 2016.

Prepare Revolution account & R's executor account till it is finally settled. Accounts are closed on 31st December each year.

Solution:

Revaluation Account

Dr. **Cr.**

Particulars		(₹)	Particulars	(₹)
To Debtors A/c		10,000	By Stock A/c	10,000
To Furniture A/c		5,000	By Building A/c	50,000
To Plant & Machinery A/c		15,000		
To Bill Receivable A/c		6,000		
To profits transferred to				
P's capital A/c	12,000			
Q's Capital A/c	8,000			
R's Capital A/c	4000	24,000		
		60,000		60,000

R's Capital Account

Dr. **Cr.**

Date	Particular	₹	Date	Particular	₹
2013 30th April	To Advertisement Suspense A/c (30,000 × 1/6)	5,000	2013	By balance b/d	1,20,000
			30th April	By Workmen Compensation reserve	15,000
			30th April	By Revaluation A/c	4,000
30th April	To R's Executor A/c	2,22,333	30th April	By P's Capital A/c (Goodwill)	45,000
			30th April	By Q's capital A/c (Goodwill)	30,000
			30th April	By P&L Suspense A/c	13,333
		2,27,333			**2,27,333**

R's Executor Account

Dr. **Cr.**

Date	Particulars	₹	Date	Particular	₹
30.4.15	To Bank A/c	72,333	30.4.15	By R's capital A/c	2,22.333
31.12.15	To Balance c/d	1,60,000	31.12.15	By interest A/c	
				(10% on 1,50,000× $\frac{8}{12}$)	10,000
		2,32,333			**2,32,333**
30.4.16	To Bank A/c 75000		1.1.16	By Balance b/d	1,60,000
	15000	90,000	30.4.16	By Interest A/c	
30.12.16	To Balance c/d	80,000		$(\frac{10}{100} \times 1{,}50{,}000 \times \frac{4}{12})$	5,000
			31.12.16	$(\frac{10}{100} \times 75{,}000 \times \frac{8}{12})$	5,000
		1,70,000			**1,70,000**
				By Balance b/d	80,000
30.4.17	To Bank A/c 80,000		1.1.17	By interest A/c	
	Add Interest 2,500	82,500	30.4.17	$(\frac{10}{100} \times 75{,}000 \times \frac{4}{12})$	2,500
		82,500			**82,500**

Working Note:

Average Profit = 2,40,000 + 1,60,000 + 2,00,000 + 1,00,000 + 50,000/5

= ₹ 1,50,000Goodwill = ₹ 1,50,000 × 3 = ₹ 4,50,000

R's share = $4,50,000 \times \frac{1}{6}$ = ₹ 75,000

contribution by P&Q in ratio 3:2

P's share = $\frac{3}{5} \times 75000$ = ₹ 45000 Q's share $\frac{2}{5} \times 75{,}000$ = ₹ 30,000

R's share of profits = $2,40,000 \times \frac{4}{12} \times \frac{1}{6}$ = ₹ 13,333

Illustration 19: (Death of a partner) M, N and O were partners in a firm sharing profits and losses equally.

Their Balance Sheet on 31-12.2014 was as follows:

Liabilities		(₹)	Assets	₹
Capitals:			Plant and machinery	60,000
M	70,000		Stock	30,000
N	70,000		Sundry Debtors	95,000
O	70,000	2,10,000	Cash at Bank	40,000
General Reserve		30,000	Cash in Hand	35,000
Creditors		20,000		
		2,60,000		2,60,000

N died on 14th March, 2015. According to the Partnership Deed, executers of the deceased partner are entitling to:

(i) Balance of partner's capital A/c

(ii) Interest on capital @ 5% p.a.

(ii) Share of goodwill calculated on the basis of twice the average of past three years' profits.

(iv) Share of profits from the closure of the last accounting year till the date of death on the basis of twice the average of three completed year's profits before death.

Profits for 2012, 2013 and 2014 were ₹ 80,000, ₹ 90,000, ₹ 1,00,000 respectively. Show the working for deceased partner's share of goodwill and profits till the date of his death. Pass the necessary journal entries and prepare N's Capital A/c to be rendered to his executors.

(CBSE 2011 Modified)

Solution

Journal

Date	Particulars	L.F.	Debit (₹)	Credit (₹)
2015 March, 14th	General Reserve A/c Dr. To N's Capital A/c (Being transfer of N's share of general reserve of his Capital A/c)		10,000	10,000
	Interest on Capital A/c Dr. To N's Capital A/c (Being interest 5% p.a. credited to N's Capital A/c upto 14.03.2010)		700	700
	M's Capital A/c Dr. O's Capital A/c Dr. To N's Capital A/c (Being goodwill adjusted in gaining ratio i.e. 1:1)		30,000 30,000	60,000
	Profit and Loss Suspense A/c Dr. To N's Capital A/c (Being the transfer of N's share of profit to his capital A/c)		12,000	12,000
	N's Capital A/c Dr. To N's Executor A/c (Being the transfer of amount due to N's executor A/c)		1,52,700	1,52,700

N's Capital A/c

Dr. Cr.

Particulars	(₹)	Particulars	(₹)
To N's Executors A/c	1,52,700	By Balance b/d	70,000
		By General Reserve A/c	10,000
		By Interest on Capital A/c	
		(70,000*5/100*73/365)	700
		By M's Capital A/c	30,000
		By O's Capital A/c	30,000
		By Profit & Loss	
		Suspense A/c	
		(90,000*2*73/365*1/3)	12,000
	1,52,700		**1,52,700**

Working Note:

1. Calculation of Goodwill

   Average profit for 3 years

   (₹ 80,000 + 90,000 + 1,00,000)/3 = ₹ 90,000

   Goodwill of the firm=Average Profit × No. of years of Purchase

   = 90,000 × 2 = ₹ 1,80,000

   N's Share in Goodwill = 1,80,000 × 1/3 = 60,000

2. Time from the date of last balance Sheet (31st December, 2014) to the date of death (14th March, 2015)

   = 31 days of January + 28 days of Feb (2015 is not a leap year) + 14 days of March = 73 days

Death of a Partner (Share of Profit/Loss)

If books have not been closed, then share of Profit/Loss for the period of work done in current year is calulated either on the basis of previous year's average profit or on the basis of percentage of profit/loss on sales/turnonver such profit/Loss share of deceased partner can be recorded in the books in two ways:

(1) If there is no change in profit sharing ratio of remaining partners.

In this case profit and loss suspense A/c is opened entry.

For share of profit	For share of loss
P & L suspense A/c for	Deceased partner's
To deceased partners	Capital/current A/c Dr
capial/current A/c	To P&L suspense A/c

(2) If new profit sharing ratio to remaining partners changes.

In this case profit/Loss of deceased partner is recorded through capital/current A/cs entry.

For share of profit	For share of Loss
Gaining partners's cap.current A/c	Deceased/sacrificing partner's cap/current A/c
To deceased/sacificing	To caining partner's
Partner's cap/current A/c	capital/current A/c

PRACTICE QUESTIONS

Q.1 Fiil in the missing information/figures in the following Ledger accounts and Balance of the firm

Revaluation Account

Dr. Cr.

Particulars	₹	Particulars	₹
To stock A/c	_____	By Fixed Assets	_____
To profit transferred to			
P's Capital A/c _____			
Q's Capital A/c _____			
R's Capital A/c _____	_____		
	_____		_____

Partner's Capital Account

Dr. Cr.

Particulars	P (₹)	Q (₹)	R(₹)	Particulars	P (₹)	Q (₹)	R (₹)
To ___	___	___	___	By balance b/d	___	___	___
To ___	___		___				
To Q's Loan A/c		___		By ___ (Profit)	___	___	___
To balance c/d	___		___	By ___		___	
				By ___		___	
	___	___	___		___	___	___

Balance sheet of P and R (After Retirement)

As at 31.03.2016

Liabilities	Amount (₹)	Assets	**Amount** (₹)
Sundry creditors	48,000	Cash	43,000
Bills Payables	20,000	Debtors ___	
Q's Loan A/c	___	Less: provision ___	___
Capitals:		Stock	54,000
P ___		Fixed assets (tangible)	___
R ___	___		
	___		___

Hints to answer:

Stock ₹ 6,000, Revaluation Profits ₹ 63,600 (distributed in old ratio 5:4:3)

Q's goodwill share = $72{,}000 \times \dfrac{4}{12} = 24{,}000$ (in gaining ratio of P and R)

Q's Loan A/c = ₹ 1,85,200,

Ps Capital – ₹ 1,86,000

Q's Capital – ₹ 1,11,900

Balance sheet total ₹ 5,51,600.

Q.2 L, M and N were partners in a firm sharing profits in the ratio of 3 : 2 : 1. The firm closes its books on 31st March every year and balance of general reserve as on 31.03.2016 was ₹ 12,000.

N died on 1st Oct. 2016. It was agreed between his executors and the remaining partners that:

a) Goodwill be valued at 3 years purchase of the average profits of the previous eight yea₹ The average profits of previous eight years were ₹ 12,000.

b) Revaluation profit was ₹ 18,000.

c) Profit for the year 2016-2017 be taken as having accrued at the same rate as the previous year which was ₹ 30,000.

d) Interest on Capital be provided @ 10% p.a.

Fill in the missing figures in the following accounts:

N's Capital Account

Dr. Cr.

Particulars	(₹)	Particulars	₹
To _____	_______	By balance b/d	____
		By ____	____
		By ____	____
		By ____	____
		By ____	____
		By L's Capital A/c	____
	____	By M's Capital A/c	____

N's Executor's Account

Dr. Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
To cash	4,250	By ______	______
To Executors Loan A/c	25,000		

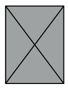
Balance is N's opening Capital & interest on Capital

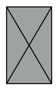
29,250-13,500 = ₹ 15,750

Let N's Capital = ₹ x

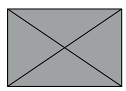
Interest on capital = $x \times \dfrac{10}{1000} \times \dfrac{6}{12} = \dfrac{x}{20}$

₹ 15,750 = $x + \dfrac{x}{20}$

₹ 15,750 = 

x = 15,750 ×  = ₹ 15,000

N's Capital (opening) = ₹ 15,000

Interest on Capital = 15000 × 

Interest N's Capital = ₹ 750

Q.3. **B/s**

Liabilities	**(₹)**	**Amount**	**Amount**
Profit & loss A/c	9,000	Cash	51,300
Capitals :		Bill receivable	10,800
R 80,000		Debtors	35,600
S 50,000		Stock	44,600
T 40,000	1,70,000	Furniture	7,000
Bank loan	12,800	Plant & Machinery	19,500
Creditors	25,000	Building	48,000
	2,16,800		2,16,800

S retired from the firm on 1-4-2009 and his share was ascertained on the revaluaton of assets as follows:

Stock ₹ 40,000; Furniture ₹ 6,000; Plant and Machinery ₹ 18,000; Building ₹ 60,000; ₹ 1,700 were to be provided for doubtful debts. The goodwill of the firm was valued at ₹ 12,000.

R & T agreed to share future profits in ratio 3 : 2. S was to be paid ₹ 17,680 in cash on retirement and the balance in three equal yearly installments. Prepare Revaluation Account, Partners' Capital Accounts, S's Loan Account and Balance Sheet on 1-4-2009.

[Ans. Profit on Revaluation ₹ 3,200; Capital A/cs : R ₹ 82,480 and T ₹ 40,040; S's Loan ₹ 42,000; Balance Sheet Total ₹ 2,02,320; Gain Ratio 1:1]

Q 4. Practical Question

P,Q and R are partners in a firm whose books are closed on 31st March every year.. R died on 24 August 2018 and R is share of profits upto date of death is to be calculated on the basis of the average profits of the last three yea₹ Net Profits of the last three years were ₹ 10,000 ₹ 14,000 and ₹ 13,800. Calculate R's share of Profits and pass journal entry.

Q.5. A, B, and C partners sharing profits in 4 : 3 : 2. Their Balance Sheet as under:

Liabilities			**Assets**		
Capitals :			Land & Building		1,20,000
(₹)			Stock		32,000
A	50,000		Debtors	25,000	
B	40,000		Less : Provision	500	24,500
C	26,000	1,16,000	Bank		3,500
Creditors		64,000			
		1,80,000			1,80,000

B retired on this date on the following terms.

1. Land & Building appreciated by 15%.

2. Create provision for doubtful debts @ 5% on debto₹ (Hi) Stock be reduce to ₹ 28,000.

3. Liability for damages ₹ 650.

4. Goodwill of the firm was ₹ 45,000 and new profit sharing ratio was agreed as 5:3.

5. B was paid ₹ 3,100 and balance in 3 equal instalments with interest @ 5% p.a. Prepare Revaluation A/c, Partners' Capital A/c and Balance Sheet of new firm and B's loan A/c till the date of his final payment.

[Ans. Profit on Revaluation ₹ 12,600; For Goodwill: Dr. A ₹ 8.125 and C ₹ 6,875; Capital A/cs: A ₹ 47,475 and C ₹ 21,925; Bank Balance ₹ 400; Balance Sheet ₹ 1,90,000)

Q.6. B, C and D are partners, sharing profits in the ratio 2:2:1:1. B and D died in an accident and A and C decided to share future profits equally. Goodwill of the firm is valued at ₹ 60,000. Pass necessary journal entry. -

[Ans. Gaining ratio of A and C is 1:2, Dr. A ₹ 10,000, C ₹ 20,000 and Cr. B ₹ 20,000, D ₹ 10,000]

Q.7. Mohan Sohan ad Hari were partners in a firm sharing profits in 2:2:1 ratio firm closes its books on 31st March every year. Mohan died on 24-8-2017. Mohan's death, the goodwill of the firm was valued ₹ 75,000. The partnership deed provided that on the death of a partner, his share in the profits of! firm in the year of his death will be calculated on the basis of last year's profits. The profit of the firm for the year ended 31-3-2017 was ₹ 2,00,000. Calculate Mohan's share of profit till the time of his death and pass the necessary journal entries for the treatment of goodwill and his share of profit.

[Ans. Profit share ₹ 32,000, (i) Dr. Hari ₹ 20,000, Sohan ₹ 10,000 and Cr. Mohan ₹ 30,000, (ii) Dr.P&L Suspense and Cr. Mohan ₹ 32,000]

Q.8. A,B and C were partners in a firm sharing profits in the ratio of 5:3:2. On 31st March, 2017, their Balance sheet was as under:

Liabilities		Amount	Assets	Amount
Creditors		17,000	Buildings	20,000
General Reserve		10,000	Machinery	30,000

A's capital A/c	30,000		Stock	10,000
B's capital A/c	25,000		Patents	6,000
C's capital A/c	15,000	70,000	Debtors	8,000
			Cash	13,000
		87,000		87,000

A died on 1st October, 2017. It was agreed between his executors and the remaining partners that: (a) Goodwill to be valued at 2 years' purchase of the average profits of the previous five years, which were, 2012: ₹ 15000; 2013, 113,000; 2014 : ₹ 12,000 and 2015: 15,000 and 2016: ₹ 20,000. Patents be valued at ₹ 8,000; Machinery at ₹ 28,000; Buildings at ₹ 30,000.

(c) Profits for the year 2017-18 be taken as having accrued at the same rate as that of the previous year.

(d) Interest on capital be provided at 10% p.a.

(e) A sum of ₹ 11,500 was to be paid to his executors immediately. Prepare A's Capital A/c and his

Executor's Account at the time of his death.

Ans: Balance of A's Executor's Account ₹ 50,000 and A's Capital ₹ 61,500: Goodwill share of ₹ 15,000(3:2), Profit share ₹ 5,000]

Q.9. A, B and C were partners in a firm sharing profits in the ratio of 3 : 2 :1. The Balance Sheet as on 31.3.2016

Liabilities		Amount	(?) Assets	Amount
Creditors		4,000	Building	20,000
Reserves		6,000	Plant & Machinery	16,000
Capitals :			Stock	5,100
A	24,000		Debtors	6,000
B	12,000		Cash at Bank	6,900
C	8,000	44,000		
		54,000		54,000

A died on 30-9-2016. Under the partnership agreement, the executors of a deceased partner were entitled to:

(a) Amount standing to the credit of partner's Capital A/c.

(b) Interest on capital® 12% p.a.

(c) Share of goodwill on the basis of four years' purchase of last three years average profit.

(d) Interest on drawings @8% p.a. A had been with drawing ₹ 500 in the beginning of every month.

(e) Share of profit from the closing of the last financial year to the date of death on the basis of the last year's profit. Profits for the year 2014, 2015 and 2016 were ₹ 8,000, ₹ 12,000 and ₹ 7,000 respectively. Prepare A's Capital A/c to be rendered to his executo₹

Ans. A's Executors A/c '45120, Goodwill share = Rs 18,000

Question 10: (Preparation of balance sheet of the reconstituted firm) Vijay, Vivek and Vinay are partners in a firm sharing profits in 2:2:1 ratio, On 31.3.2015 Vivek retires from the firm. On the date of Vivek's retirement the balance sheet of the firm was as follows:

Balance Sheet of Vijay, Vivek and Vinay

Liabilities		₹	**Assets**		₹
Creditors		54,000	Bank		55,200
Bills Payable		24,000	Debtor	12,000	
Outstanding Rent		4,400	Less: Provision for		
Provision for Legal Claim		12,000	Doubtful	800	11,200
Capitals:			Stock		18,000
Vijay	92,000		Furniture		8,000
Vivek	60,000		Premises		1,94,000
Vinay	40,000	1,92,000			
		2,86,400			2,86,400

On Vivek's retirement it was agreed that:

i. Premises will be appreciated by 5% and furniture will be appreciated by ₹ 2,000. Stock will be depreciated by 10%

ii. Provision for bad debts was to be made at 5% on debtors and provision for legal damages to be made for ₹14,400.

iii. Goodwill of the firm is valued at ₹ 48000

iv. Amount due to Vivek is to be settled on the following basis

Case1. ₹50,000 from Vivek Capital A/c will be transferred to his loan A/c and the balance will be paid by cheque.

or

Case 2: Transfer to Vivek loan A/c and Vijay and Vinay decided to adjust their capital in new Profit sharing Ratio by withdrawing or bringng cash.

or

Case 3. Transfer to Vivek loan A/c and New firm capital is fixed 1,20,000 in new profit sharing Ratio.

or

Case 4. Vivek is to be paid through cash brought in by Vinay and Vijay in a manner that their capital are proportionate to their new profit sharing ratio which was to be 3:2

or

Case 5. Remaining partners decided to bring adequate amount to pay Vivek and to manintain a bank balance of ₹ 15,200. They also adequate their capitals as per their New Profit sharing Ratio.

Prepare Revaluation A/c, Partner's Capital A/c and balance that in alone all cases after Vivek retirement.

Retirement & Death of a Partner

Q.1 A, B and C are partner's with profit sharing ratio 4:3:2. B retires and Goodwill was valued ₹1, 08,000. If A& C share profits in 5:3, find out the goodwill shared by A and C in favour B.

A) ₹ 22,500 and ₹ 13, 500 B) ₹ 16, 500 and ₹.19, 500

C) ₹ 67,500 and ₹ 40, 500 D) ₹19,500 and ₹ 16, 500

Q.2 A, B and C share profits and losses of the firm equally. B retires from business and his share is purchased by A and C in the ratio of 2:3 New Profti sharing ratio between A and C respectively would be:-

A) 1:1 B) 2:2

C) 7:8 D) 3:5

Q.3 The accounting procedure at the retirement of a partners involves:-

A) Revaluation of Assets and liabilities

B) Ascertain his share of Goodwill

C) Finding the amount due to him

D) All of them

Q.4 If the remaining partner want to continue the business, after the death of a partner, a new partnership agreement is:-

A) Necessary B) Not necessary

C) Optional D) All of them

Q.5 An account operated to ascertain the loss or gain at the death of a partner is called :-

A) Realisation A/c B) Revaluaton A/c

C) Executor Ac D) Deceased Patner's A/c

Q.6 Amout due to outgoing partner is shown on the balance sheet as his:-

A) Liability B) Assets

C) Capital D) Loan

Q. 7 Retiring partner is compensated for parting with the firm's future profits in favour of remaining partner's. The remaining partner's contribute to such compensation amount in:-

A) Gaining Ratio B) Capital Ratio

C) Sacrificing Ratio D) Profit sharing Ratio

Fill in the Blanks :-

Q.8 Intangible asset which are not shown in the Balance Sheet results in an .... in the outgoing proprietorship.

Q.9 Goodwill may be .... if all the partner's are agreed, that it should not remain in the books.

Q.10 The payment made to the retiring partner in installment is known as ....

CHAPTER 6

DISSOLUTION OF PARTNERSHIP FIRM

<table>
<tr><td>S.NO.</td><td>TOPIC</td><td colspan="3"></td></tr>
<tr><td>1.</td><td>Dissolution of partnership firm</td><td colspan="3">As per 39 of the partnership act 1932, "Dissolution of the firm means dissolution of partnership among all the partners in the firm." Its means business of the firm ends. All the assets of the firm are disposed off and all outside Liabilities and partner capital are paid.</td></tr>
<tr><td>2.</td><td>Mode of dissolution of firm</td><td colspan="3">1. Dissolution by agreement
2. Compulsory Dissolution
3. On happening of an event like insolvency of a partner
4. Dissolution by notice
5. Dissolution by court</td></tr>
<tr><td>3.</td><td>Dissolution of partnership V/S Dissolution of firm</td><td>BASIS</td><td>Dissolution of Partnership</td><td>Dissolution of firm</td></tr>
<tr><td></td><td></td><td>1. End of business</td><td>The business of the firm continue</td><td>The business of the firm closed</td></tr>
</table>

		2. Settlement of assets & liabilities	Liabilities are reassessed and new balance sheet is opened	Assets are realized and liabilities are paid off.
		3. Economic relationship	Economic relationship between the partners are changed	Economic relationship between the partners are to end.
		4. Court's intervention	No intervention of the court can be dissolved by mental agreement	A firm can be dissolved by the court's order.
		5. Closer of books and accounts	Books of accounts of the firm need not to be closed.	Books of accounts of the firm are closed.
		6. Effect	It may or may not dissolution of firm	It necessarily in dissolution of partnership.

4.	SETTLEMENT OF ACCOUNTS	As per sectin 48 of the partnership act 1932, the following rules shall apply. 1. Treatment of losses: losses including deficiencies of capital, shall be paid :- (i) first out of profit, (ii) next out of capital and (iii) if necessary, by the partners individually in the profit sharing ratio. 2. Application of assets: Assets of the firm shall be applied in the following manner. (i) In paying firm's debts to the third party. (ii) In paying each partner proportionately what is due to him on a/c of loan(i.e. partner's loan) (iii) In paying each partner proportionately what is due to him on a/c of capital (iv) The residue, if any shall be divided among the partners in their profit sharing ratio.
5.	PRIVATE DEBTS V/S FIRM'S DEBTS	SEC 49 Of the act applied as follows: (i) Firms property is applied first for settling the firms debts, surplus if any can be utilized for payment of their private debts up to received share. (ii) Private property is applied first for private debts then towards firms liability.

Dissolution of a Partnership Firm

Settlement of Accounts

Section 48 of the Indian Partnership Act, 1932 deals with the settlement of accounts when the firm is dissolved.

In brief, when firm is dissolved, assets are realised, liabilities are paid and the balance, if any, is distributed among the partne₹

On dissolution of the firm, the accounting treatment involves preparation of following accounts:

- Realisation A/c
- Loan by Partner A/c(If any)
- Loan by firm to Partner A/c(If any)
- Partners' Capital/Current A/c
- Cash/Bank A/c

REALISATION ACCOUNT

- It is prepared on the dissolution of a firm.
- It is prepared to find out Gain/loss on the realisation of assets and payment of liabilities.
- It's a nominal A/c.

STEPS INVOLVED IN PREPARATION OF REALISATION ACCOUNT

1. Transfer all assets from balance sheet to the debit side of realisation A/c except:

   Cash/Bank balance, Loan to partner(s). Partners" capital/current a/c,Partners' Drawings. Accumulated losses, Fictitious assets.

2. Transfer all liabilities from balance sheet to the credit side ot realisation A/c Except:

   Partners' capital/current A/c,Loan by partner(s),General reserve,Accumulated Profits,Workmen compensation reserve (surplus only).

3. Record the sale of assets at given realised value and assets(s) taken over by the partner(s) against credit side of realisation account.

   As per CBSE Tangible assets are realised either at given value or. Book values

4. Record the payment of liabilities or agreed to be paid by partner (whether recorded or unrecorded) to the debit side of realisation A/c except investment fluctuation reserve, provision for doubtful debts, provision for depreciation, Provision for discount on debtors.

   If amount payable is not given for a liability then it is paid at book value.

5. Record Dissolution expenses and remuneration payable to a partner (if any).
6. Find gain/loss on account of realisation of assets and repayment of liabilities by balancing the account and distribute it among partners in their profit sharing ratio.

STEP:1 TO TRANSFER THE ASSETS TO REALISATION A/c

Date	Particulars	L.F.	Dr.	Cr.
	Realisation A/c Dr. To Assets (Individually) A/c (Being assets are transferred to realisation A/c)			

STEP : 2 TRANSFER THE LIABILITIES TO REALISATION A/c

Date	Particulars	L.F.	Dr.	Cr.
	Liabilities (individually) Dr. To Realisation A/c (Being liabilities are transferred to realisation A/c)			

STEP:3a For sale of assets

Date	Particulars	L.F.	Dr.	Cr.
	Cash/Bank A/c Dr. To Realisation A/c (Being assets sold at given value)			

STEP:3b Asset(s) taken over by the partner

Date	Particulars	L.F.	Dr.	Cr.
	Partners capital/current A/c Dr. To Realisation A/c (Being asset(s) taken over by the partner at an agreed value)			

STEP:4a To pay liability

Date	Particulars	L.F.	Dr.	Cr.
	Realisation A/c Dr. To Bank A/c (Being liability paid)			

STEP:4b Liability assumed by the partner

Date	Particulars	L.F.	Dr.	Cr.
	Realisation A/c To Partners' capital/current A/c (Being liability assumed by the partner)			

STEP:5 Remuneration to a Partner

Data	Particulars	L.F.	Dr.	Cr.
	Realisation A/c To Partners' capital/current A/c (Being partner credited for remuneration)			

TEP:6 TO DISTRIBUTE GAIN ON REALISATION

Date	Particulars	L.F.	Dr.	Cr.
	Realisation A/c Dr. To Partners' capital/current A/c (Being partners credited for gain on realisation in old ratio)			

To distribute

Loss on Realisation

Partners Capital/current A/c Dr.

To Realisation A/c

* Accumulated Profits, Losses & Reserves

(1) General Reserve, P & L A/c credit Balance, Contingening Reserve

General Reserve A/c Dr.

P & L A/c Dr.

Contingeny Resere A/c Dr.

To Partners capital A/c

(2) P & L A/c Debit Balance, Advertisment suspense A/c

Partner's capital A/c Dr.

To profit and loss A/c

To deferred revenve expendture

(Advestisement suspense A/c)

(3) Workmen Compensation Reserve

(i) Workmen compensation Reserve

To Realisation A/c (To the extant of claim) (if any)

(ii) Workmen compensation A/c Dr.

To partner's capital Aics

(Surplus in workman compensation reserve A/c after claim)

JOURNAL ENTRIES FOR FEW IMPORTANT ITEMS

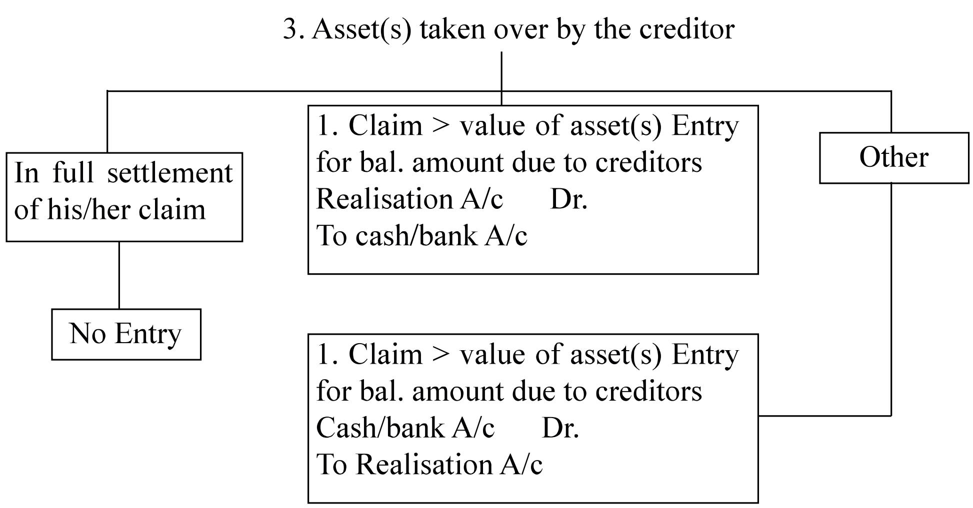
1. TO SETTLE LOAN GIVEN BY PARTNER TO THE FIRM

Date	Particulars	L.F.	Dr.	Cr.
	Partners' loan A/c Dr. To Cash/Bank / Realisation A/c (for asset given against loan) To Realisation A/c (if any, difference) (Being partners' loan discharged)			

2. TO SETTLE LOAN GIVEN TO PARTNER BY THE FIRM

Date	Particulars	L.F.	Dr.	Cr.
	Bank/ Capital A/c (if liability assumed against the loan) A/c Dr. Realisation A/c (if any, difference) Dr. To Partners' loan A/c (Being loan to partner recovered)			

Note : Until unless specified Loan to partner is not debited to his/her capital/current A/c but received in cash/bank.



4. **Realisation Expenses**

To be Borne by	Paid paid by
1. Firm	Firm
2. Firm	Partner
3. Partner	Same Partner
4. Partner	Firm
5. Partner	Another partner

For Realistion Expenses Journal

Date	Particulars	L.F.	Dr.	Cr.
	Bearing Party A/c Dr. (In case of firm-Realisation A/c) In case of partner-partners capital A/c partners current A/c To Paying Party A/c (In case of firm-cash A/c or realistion A/c for asset given for expenses) In case of partner-partners capital A/c Partners current A/c			

Note: If it is not mentioned that who is bearing expenses it is assumed to be borne by FIRM

Illust. 1. Record necessary journal entries in the following cases:

(a) Creditors were ₹16,000. They accepted Machinery valued at ₹18,000 in full settlement of their claim.

(b) Creditors worth ₹85,000 accepted ₹40,000 as cash and Investment worth ₹43,000, in full settlement of their claim.

(c) Creditors were ₹90,000. They accepted Buildings valued ₹1,20,000 and paid cash to the firm ₹30,000.

JOURNAL

Date	Particulars	LF.	Dr.	Cr.
a.	NO ENTRY			
b.	Realisation A/c Dr.		40,000	
	To Cash A/c (Being balance due paid in cash to creditors)			40,000
	Cash A/c		30,000	
	To Realisation A/c (Being balance received in cash from creditors)			30,000

Distinction between Revaluation Account and Realisation Account

Basis of Difference	Revaluation Account	Realisation Account
Purpose	It is prepared to show assets and liabilities in the books at their revised values.	It is prepared to ascertain profit or loss from sale of assets and repayment of Liabilities.

When to be prepared	It is prepared at the time of change in profit sharing ratio among the existing partner, admission, retirement and death of a partner.	It is prepared at the time of dissolution of a firm.
Preparation of Account	This account may be prepared at a number of times during the life of a firm.	This account is prepared once during the life of a firm.
Content	This account records only those assets and liabilities whose book values have been changed.	This account records all assets (except cash, fictitious assets etc.) and all outside liabilities.
Result	A Firm continues its business even after the preparation of revaluation account.	The business activities of a partnership firm comes to an end after preparation of realisation account

Illust. 2: Following is the Balance Sheet of X and Y, who share profits and losses in the ratio of 4.1, as at 31st March, 2015

BALANCE SHEETAs on 31st March, 2015

Liabilities	**(₹)**	**Assets**		**(₹)**
Sundry Creditors	8,000	Bank		20,000
Bank Overdraft	6,000	Debtors	17,000	
X's Wife Loan	8,000	Less : Provision	(2,000)	15,000
Y's Loan	3,000	Stock		15,000
Investment Fluctuation fund	5,000	Investments		25,000
Capital		Buildings		25,000
X	50,000	Goodwill		10,000
Y	40,000	Profit and Loss A/c		10,000
	1,20,000			1,20,000

The firm dissolved on the above date and the following arrangement was decided upon:

(i) X agreed to pay off his wife's loan.

(ii) Debtors of ₹ 5,000 proved bad.

(iii) Other assets realised-Investment 20% less; and Goodwill at 60%

(iv) One of the creditors for ₹ 5,000 was paid only ₹ 3,000

(v) Buildings were auctioned for ₹ 30,000 and auctioneer's commission amounted to ₹ 1,000.

(vi) Y took over part of Stock at ₹ 4,000 (being 20% less that the book value. Balance stock realised 50%.

(vii) Realisation expenses amounted to ₹ 2,000.

Prepare Realisation A/c, Partner's Capital A/cs and Bank A/c

Realisation Account

Dr. **Cr.**

Particulars	₹	**Particulars**		₹
To Goodwill	10,000	By Investment Fluctuation		
To Buildings	25,000	Fund		5,000
To Investments	25,000	By Provision for Doubtful		
To Stock	15,000	Debts		2,000
To Debtors	17,000	By Creditors		8,000
To X's Capital A/c	8,000	By Bank overdraft		6,000
(X's wife loan)		By X's Wife Loan		8,000
To Bank A/c	6,000	By Bank A/c		
(Bank overdraft)		(Asset realised)		
To Bank A/c	6,000	Debtors	12,000	
(Creditors) (3000+3000)		Investment	20,000	
To Bank A/c	2,000	Goodwill	6,000	
(Expenses on Realisation)		Buildings	30,000	
To Bank A/c (auctioneer Commission)	1000	Stock	5,000	73,000
		By Y's Capital A/c (Stock)		4,000
		By Loss transferred to:		
		X's Capital A/cs	7,200	
		Y's Capital A/cs	1,800	9,000
	1,15,000			1,15,000

Y's Loan A/c

Dr. **Cr.**

Particulars	₹	**Particulars**	₹
To Bank A/c	3,000	By balance b/d	3,000
	3,000		3,000

Partner's Capital A/cs

Dr. Cr.

Particulars	₹	₹	Particulars	₹	₹
To Profit and Loss A/c	8,000	2,000	By Balance b/d	50,000	40,000
To Realisation A/c			(Cr. Balance)		
(Assets taken)	——	4,000	(By Realisation A/c	8,000	—
To Realisation A/c			Liabilities		
(Loss on Realisation	7,200	1,800	taken)		
To Bank A/c					
(Excess cash paid)	42,800	32,200			
	58,000	40,000		58,000	40,000

Bank A/c

Dr. Cr.

Particulars	₹	Particulars	₹
To Balance b/d	20,000	By Balance b/d	6,000
(Cash at Bank)		(Bank Overdraft)	
To Realisation A/c	73,000	By Realisation A/c	1,000
(Assets Realised)		(Liabilities Paid)	
		By Realisation A/c	6,000
		By Realisation A/c	2,000
		(Exp. Paid)	
		By Y's Loan A/c	3,000
		(Partner's Loan Paid)	
		By X' Capital A/c	42,000
		By Y's Capital A/c	32,200
	93,000		93,000

Illust. 3 Pass the necessary journal entries on the dissolution of a firm in the following cases:

(a) Dharama, a partner, was appointed to look after the process of dissolution at a remuneration of ₹ 12,000 and he had to bear the dissolution expenses. Dissolution expenses ₹ 11,000 were part by the Bharma.

(b) Jay a partner was to look after the process of dissolution and for this work he was allowed a remuneration of ₹ 7,000 agreed to bear all dissolution expenses. Actual expenses ₹ 6000 were pound from firm's Bank A/c.

(c) Realisation expenses ₹ 12000 born by the partner Deepa. These expenses were paid by Deepa by drawing cash from the firm. She was allowed commission ₹ 10,000 for process of dissolution.

(d) Dev, a partner, agreed to do the work of dissolution for ₹ 7500. He took away stock for his commission.

(e) A debtor of ₹ 8,000 already transferred to realization account agreed to pay the realization expenses of ₹ 78,00 in full settlement.

(f) Realisation expenses amounted to ₹ 15,000 out of this ₹ 12000 were to be born by 'A' a partner and the balance by firm.

Solution:

Journal

Date	Particular	L.F.	Dr. Amount (₹)	Cr. Amount (₹)
(1)	Realisations A/c Dr.		12,000	
	To Dharam's capital A/c			12,000
	(Being remuneration allowed to partner to carry out dissolution)			
(2)	(i) Realisation A/c			
	To Jay's capital A/c Dr.		7,000	
	(Being the remunerable all out to partner for bear realsiation expenses)			7,000
	(ii) Jay' capital A/c Dr.			
	To Bank A/c		6,000	6,000
	(Being the expenses paid by firm on behalf partner)			
(3)	(i) Realisation A/c			
	To Deepa's capital A/c		10,000	
	(Being the commission paid for realisation expenses to Deepa)			10,000
	(ii) Deepa's capital A/c		12,000	
	To cash A/c			12,000
	(Being the cash is drawn for payment of realisation expenses by Deepa)			
(4)	No Entry			
(5)	No Entry			
(6)	A's capital A/c Dr.			
	Realisation A/c Dr.			
	To Bank A/c		12,000	
	(Being the payment of realization expenses by partner 'A' and Balance by firm)		3,000	15,000

Illust. 4 Pass Journal entries for the following transactions in the book of the firm on its dissolution:

A) Bills receivable of ₹ 20000 discounted with the bank is dishonoured as drawee was declared insolvent and 30% amount is received in cash from him.

b) 100 shares of Bajaj Auto Ltd. acquired at a cost ₹ 3,600 had been written of from the books. These were valued at ₹ 12 par share, and were divided among partner's A and B in 2 : 1.

c) Mr. Verma, a creditor to whom ₹ 6,000 are due, accepted office equipment at ₹ 4,000 and the balance paid to him by cash.

d) Debtors of ₹ 5,00,000 and provision for doubtul debts of ₹ 20,000 transferred to realisation account. On dissolution bad debts were ₹ 1,00,000 and remaining debtors realised at 30% discount.

e) Loan owed by B towards firm is ₹ 30,000. It was decided by the firm that B will pay to the creditor ₹ 25,000 in settlement of his loan.

f) The firm had borrowed ₹ 35,000 from Rashmi, a partner. The firm got dissolved; Rashmi decided to take furniture against the payment of her loan.

Date	Particulars	L.F.	Amount (₹)	Amount (₹)
	(a) Cash A/c Dr. To Realisation A/c (Being 30% realized from drawer)		6,000	6,000
	Realistion A/c Dr. To Bank A/c (Being full amount paid to Bank)		20,000	20,000
	(b) As capital A/c Dr B's Capital A/c Dr. To Realisation A/c (Being shares taken by A and B)		800 400	12,00
	(c) Realisation A/c Dr To cash A/c (Being Net ₹2000 paid to Mr. Verma)		2,000	2,000
	(d) Cash A/c Dr To Realisation A/c (Being 70% realised from Debtors)		2,80,000	2,80,000
	(e) Realisation A/c Dr To B's Loan A/c (Being B's loan transferred)		30,000	30,000
	(f) Rashmi's Loan A/c Dr To Realisation A/c (Being loan settled by providing furniture)		35,000	35,000

Practice Question

Q.1 Pass the journal entries entries to effect the followings

(i) bank loan of ₹ 12000 is paid off.

(ii) Deferred advertisement expenses A/c appeared in the books at ₹28000.

(iii) Creditors agreed to take over the machine in full settlement of their calim. (creditors ₹ 2,50,000 and machinery ₹ 2,25,000)

(iv) Z, an old customer, whose account was written off as bad in the previous year, paid ₹ 500.

(v) A contingent liability (not provided for) of ₹ 1000 was also discharge.

(vi) An unrecorded computer realized ₹ 7000.

Q.2 X and Y were partners sharing profits and losses in ratio of 4:1. Their firm was dissolved on 31.3.15. Complete the missing information:

Realisation Account

Particulars	₹	**Particulars**	₹
To Goodwill A/c	10,000	By Investment Fluctuation Fund A/c	5,000
To building A/c	25,000	By Provision for Doubtful Debts A/c	2,000
To Investments A/c	25,000	By Creditors A/c	8,000
To Stock A/c	15,000	By Bank Overdraft A/c	6,000
To Debtors A/c	20,000	By X's Brother Loan	8,000
To X's Capital A/c (Brother's loan)	**(a)**	By Bank A/c (Assets Realised) ₹	
To Bank A/c's: ₹		Debtors 12,000	
Creditors 6000		Investments 20,000	
Bank Overdraft 6000	12,000	Goodwill 7,000	
To Bank A/c (Realisation Expenses)	**(b)**	Buildings 30,000	
		Stock (50% of 10,000) 5,000	74,000
		By Y's Capital A/c(stock)	**(c)**
		X's Capital A/c **(d)**	
		Y's Capital A/c **(e)**	
	(f)		**(f)**

Partner's Capital Account

Particulars	X (₹)	Y (₹)	Particulars	X (₹)	Y (₹)
To profit & Loss A/c	8,000	2,000	By Balance b/d	50,000	40,000
			By Realisation A/c	**(k)**	
To Realisation A/c (Stock)		4,000			
To Realisation A/c (Loss)	**(g)**	**(h)**			
To Bank A/c (Bal. Fig.)	(i)	(j)			
	(l)	**(m)**		**(l)**	**(m)**

Bank Acconut

Particulars	₹	Particulars	₹
To Balance b/d	20,000	By Y's loan A/c	6,000
To Realisation A/c	**(n)**	By Realisation A/c (liabilities paid off)	12,000
		By Realisation Expenses A/c	2,000
		By X's Capital A/c	**(o)**
		By Y's Capital A/c	**(p)**
	(q)		**(q)**

Hints:

a) Brother's ₹ 8,000 (Given on Cr. Side of Realisation A/c)

b) Realisation Expenses ₹ 2,000 (From Bank A/c Cr. side)

c) Stock ₹ 4,000 (From Y's Capital A/c Dr. side)

d) ₹ 8,000 (e) ₹ 2,000 (f) 1,17,000 (g) ₹ 8,000 (h) ₹ 2,000

(i) ₹ 42,000 (j) ₹ 32,000 (k) ₹ 8,000 (l) ₹ 58,000 (m) ₹ 40,000

(n) ₹ 74,000 (o) ₹ 42,000 (p) ₹ 32,000 (q) ₹ 94,000

Q.3 A and B showing profits and losses in the ratio of 3:2 agreed upon the dissolution of the firm an 31st march 2018 at which date thair Balance sheet was as follows:

Liabilities	₹ Amount	Assets	₹ Amount
Trade creditor	60,000	Cash	6,000
Employee Provident Fund	15,000	Bank	30,000
Bills payable	25,000	Stock	80,000
Investment flutuation reserve	24,000	Sunday Debtors 66,000 Loss Provision for D/D 6,000	60,000
Profit and Loss A/c	11,000	Plant and Machinery	30,000
Capital A/c		Land and Building	33,000
A 90,000	1,20,000	Investment	10,000
B 30,000		Goodwill	15,000
Workman Compensation Reserve	20,000	Pre Paid Insurance	1,000
		Advertisement Expenditure	10,000
	2,75,000		2,75,000

The firm was dissolve on the given date and following transition took place :

(1) B undertook to pay employee provident fund.

(2) A took 60% stock at a profit of 10% and remaining stock was sold at a discount of 20% on cost.

(3) Land and building & investments realized ₹ 1,40,000 and ₹ 8,000 respectively.

(4) Trade creditor accepted plant & machinery loss 10% of value and cash ₹ 27000 in full settlement of their claim.

(5) ₹ 8,000 of Book debts proved bad bills payable were point in full.

(6) Realisation expenses paid by A ₹ 5000.

(7) There were a contingent liability of ₹ 1,000 for Bill discounted also discharge.

Prepare Realisation A/c, partner's capital A/c and Bank A/c.

(Ans. Profit of realisation ₹ 1,06,200, partner final payment ₹ 1,18,520 A, ₹ 5880 B Total & Bank A/c 2,67,400)

Q.4. Ram, Rahim and Rehman were partners in a firm sharing profits in ratio 4 :1 :5. On 28-2-2017, the firm was dissolved. On the date of dissolution, the Balance Sheet of the firm was as follows : Rehman was appointed to realize the assets and liabilities for which he was to be given a commission of ₹ 5000 and to bear the actual expenses of realization himself.

Liabilities	Amount(₹)	Assets	Amoumt (₹)
Bank loan	4,34,000	Bank	48,000
Creditors	3,80,000	Debtors 2,74,000	
General reserve	1,00,000	Less provision 8,000	2,66.000
Ram's wife's loan	40,000	Stock	1,08,000
Capitals:		Furniture	1,32,000
Ram	14,00,000	Machinery	4,00,000
Rahim	6,00,000	Building	30,00,000
Rehman	10,00,000		
	39,54,000		39,54,000

Assets realised as follows: bad debts proved ₹ 4,000. Stock at 15% less. Furniture was taken over by Ram for 9,000. Building was sold for ₹ 29,00,000. Rehman took over 50% of the machinery at 5% less than the book value. Bank Loan was paid with interest of ₹ 79,500. A computer already written off was taken over by Rahim for ₹ 3000. Creditors allowed a discount of 5%. Expenses of dissolution ₹ 7,000 were paid by Rehman. Remaining machinery was sold at 10% profit.

Pass journal entries at the time of dissolution.

Q.5. Complete the following journal at the time of a partner ship firm of A, B and C and D were sharing the profits & losses in the ratio of 1 : 2 : 2

Realisation A/c Dr. To stock A/c To building A/c To machinery A/c To Goodwill A/c To debtors A/c To investment A/c (______________________________ ______________________________ ______________)	6,50,000	 40,000 2,10,000 2,50,0000 ________ 12,000 1,00,000
Creditors A/c Dr. A's Loan A/c Dr. Bank Loan A/c Dr. Provision for doubtful debts A/c Dr. To realization A/c (______________________________ ______________________________ ________________)	45,000 1,20,000 2,00,000 2,000	 ________
________ Dr. To ______________ (being the machinery sold at 10% less than book value, debtors realized at 20% discount and half of the investment was realized at 25% above book value)	________	 ________

(being the machinery sold at 10% less than book value, debtors realized at 20% discount and half of the investment was realized at 25% above book value)		
________ Dr. To ________ (creditors worth ₹ 36,000 took over the stock at valuation of ₹ 30,000)	________	________
________ Dr. To ________ (A agreed to pay off his wife's loan) ________ Dr. To ________ (A took over the half of the investment at 10% discount)	________ ________	________ ________
________ Dr. To ________ (Building was sold by the bank for setting off its loan for ₹ 2,50,000 and the balance amount of cash was given to the firm)		
(________Dr.________ ________To ________ ________ ________)	________	________
(________Dr________ ________To________ ________)		

B's loan A/c ———————— Dr. To ————— (B's loan for ₹ 50,000 ————)		

Partners' Capital A/c

Particulars	A's capital	B's capital	C's capital	Particulars	A's capital	B's Capital	C's capital
To realization A/c				By balance B/d	5000	175,000	1,15,000
To cash				By gen reserves	2,000	2,000	4,000
				By Profit & loss A/c	30000	30000	60000
				By realization A/c			
				By realization A/c			
				By cash			

Cash A/c

Particulars	**Amount**	**Partners**	**Amount**
balance B/d	4000		

Q. 6 Following was the balance sheet of D, G, And T on 28-2-2017

Liabilities(₹)	Amount	Assets	Amount
R's Loan	12,000	Furniture	15,000
Creditors	50,000	Land & Building	2,45,000
General Insurance	20,000	G' s Capital	20,000
G's Loan	8,000	Bank	20,000
Bills payable	10,000	Debtors	30,000
D' s Capital 1,00,000		Stock	20,000
T's Capital 1,50,000	2,50,000		
	3, 50,000		3,50,000

The firm was dissolved on the above date on the following terms:-

(i) Debtors realised ₹ 28,000 and creditores and bills payable were paid at discount of 10%

(ii) Stock was taken over by T for ₹ 15,000 and furniture was sold to N for ₹ 12,000.

(iii) Land & Building was sold for ₹ 2,80,000.

(iv) R1 Loan was Paid by Cheque for same amount,

Multiple Choice Question **Dissolution of Partnership Firm**

Q. 1 In which condition a partnership firm is deemed to be dissolved?

(A) On a Partner's admission (B) on retirement of a partner

(C) On expiry of the period of partnership (D) On loss in partnership

Q.2 Contingent liability, when paid on dissolution of a firm is debited to :-

(A) Partner's Capital A/c (B) Realisation Account

(C) Liabilities A/c (D) Asset A/c

Q.3 A partnership firm is compulsory dissolved:-

(A) When the business of the firm is declared illegal

(B) When a partner of the firm dies

(C) When a partner of the firm become Insolvent

(D) When a partner transfer his share to some other person without the consent of the partner

Q.4. At the time of dissolution of Partnership firm, ficitious, assets are transferred to :-

(A) Capital Account of Partners (B) Realisation Account

(C) Cash Account (D) Partner's Loan Account

Q.5. On dissolution of a firm,debtor (₹) 17,000 were shown in the balance sheet out of this (₹) 2,000 become bad. One debtor become insolvent 70 % were recovered from him out of ₹) 5,000 . Full amount was recovered from the balance debto₹ On account of this item loss in realisiation account will be:-

(A) ₹) 5,100 (B) ₹) 1.500

(C) ₹) 3, 500 (D) ₹) 2,000

Q.6 Anu, Khusi and Anmol are partners, The firm had given a loan of (₹) 20,000 to khushi. On the event of dissolution, the loan will be selled by :-

(A) Transferring it to debt side of Realisation A/c

(B) Transferring it to credit side of Realisation A/c

(C) Transferring it to debti side of Partner's capital.

(D) Khusi paying Anu and Anmol Privately

Q.7 On dissolution, goodwill account is transferred to :-

(A) In the capital accounts of partners (B) On the Credit of Cash account

(C) On the debit of Realisation A/c (D) On Credit of Realisation A/c

Q.8 Where it is agreed that a partner will be paid a lumsum amount for dissiolution expenses payment is made by the firm, the payment is debited to

(A) Realisation Account (B) Concerned Partner's Capital Account

(C) All Partner's Capital A/c (D) None of these

Q.9 In case of dissolution of Partnership firm, a creditor of ₹ 3,60,000 accepted machine value at ₹ 5,00.000 and paid to the firm ₹ 140,000 and a second creditor for ₹ 50,000 accepted stock ₹ 45,000. in full settlement. What amount should be shown in Realisation for above transaction.

(A) Dr Realisation ₹ 1,40,000 Cr HIL

(B) Dr realisation and Cr. NIL ₹ 1,40,000

(C) Dr Realisation 1,40,000 &cr Realisation 500

(D) Dr Realisation ₹ 5,000 & cr ₹ 14,0,000

Q.10 Retirement and Death of a partner:-

(A) Is dissolution of partnership agreement

(B) Is dissolution of a firm

(C) a and b both

(D) None of the above

Q.11 At the time of dissolution non-cash assets ared credited with :-

(A) Market value

(B) Book Value

(C) As the agreed amount among partner's

(D) None of the above

Q.12 Admission of a partner is termination of .... and not dissolution of .... (agreement, firm)

Q.13 If all partners mutaually decide for the dissolution, it will be dissolution of the .... (firm)

Q.14 .... of partner will be paid off before the settlement of partner's capital. (Loan)

CHAPTER 7

ACCOUNTING FOR SHARE CAPITAL

Company	A Company is an artificial person created by law, having separate entity with a perpetual succession and a common seal.
Characteristics of a company	1. A company has a separate legal entity which is distinct and separate from its members. 2. It has perpetual existence 3. It has its own common seal. 4. Shares of a company are transferrable subject to certain conditions. 5. The liability of the members of the company is limited to the extent of unpaid amount of the shares held by them.

TYPES OF COMPANY

(i) Public Company	A company which is not a private company and which is not a subsidiary of a private company.
(ii) Private Company	A private company is one which by its articles-restricts the right to transfer its shares, must have at least 2 persons, except in case of one person company and limits the number of its members to 200 (excluding its employees)
(iii) One Person Company (OPC)	The companies Act, 2013, define OPC as a Company which has only one person as a member'. Rule 3 of the companies (Incorporation) Rules, 2014, provides that: (a) Only a natural person being an Indian Citizen and resident in India can form one person company. (b) It cannot carry out nonbanking financial investment activities (c) Its paid up share capital is not more than ₹ 50 Lakhs (d) Its average annual turnover of three years does net exceed ₹ 2 Crores.

IMPORTANT TERMS USED IN ACCOUNTING FOR SHARE CAPITAL

a) Share Capital	Capital raised by issue of shares is called share capital.
b) Authorized Capital	It is also called as Nominal or Registered capital. It is the maximum amount of Capital a company can issue. It is Stated in the memorandum of Association.
c) Issued Capital	This is part of authorized capital which is offered to public for subscription. It can not exceed authorized capital.
d) Subscribed and fully paid up capital	It is that part of the issued capital which is fully called up by the company and fully paid up by the shareholders.
e) Subscribed but not fully paid up capital	It is that part of the issued capital which is either not fully called up by the company or not fully paid up by the shareholders or both.
f) Called Up Capital	It is the amount of nominal values of shares that has been called up by the company for payment by the subscriber towards the share.
g) Paid Up Capital	It is part of called up capital that the members of company or shareholders have paid. Paid up capital = Called-up capital - Call in arrears
h) Reserve Capital	It is part or portion of uncalled share capital of a company which can be called only in case of winding up of the company.
i) Capital Reserve	It is capital profit not available for distribution as dividend. It is represented in balance sheet of company as Reserves and Surplus under the heading Shareholders Funds.
j) Private Placement of Shares (Section-42)	Private Placement of Shares means issue and allotment of shares to a select group of persons privately and institutional investors, not to the public.
k) Calls in arrear	Any Amount which has been called or demanded by company from shareholders but not paid by the shareholder till the last date mentioned in call letter is called as calls in arrears. Company can charge interest on this rate mentioned in Article of Association or 10% p.a. as per Table F. Such amounts are shown in "Note to Accounts".
1) Calls in advance	Any Amount paid in excess of what has asked to pay is called as call in advance. Interest is paid on this at rate mentioned in Article of Association or 12% p.a. as per Table F

m) Issue of shares at discount (Sec 53)	A Company cannot ordinarily issue shares at discount other than sweat equity shares.
n) Issue of shares at premium (Sec 52)	The money received on premium is transferred to securities Premium Reserve (SPR) account and the amount received on SPR can be utilized for the following purpose; (Section 52) 1. Issue of fully paid bonus shares to the shareholders 2. Write off preliminary expenses of the company 3. Writing off securities issue expenses, commission paid, discount on issue of securities. 4. For providing the premium payable on redemption of Redeemable preference shares or debentures of the company. 5. For Buy back of its own shares as per Section 68.
o) Employee stock option plan (ESOP)	ESOP or sweat equity share means option granted by the company to its employees and directors to subscribe the shares of the company at a price that is lower than the market price. But it is not an obligation on the employee to subscribe for it.
p) Over Subscription	When applications for more shares of a company are received than the number of shares offered to the public for subscription, it is called over subscription. First Alternative - To fully accept some applications and totally reject the others; the application money received on rejected applications is fully refunded. Second Alternative - To make a proportionate allotment to all applicants (called 'pro-rata' allotment), the excess application money received is normally adjusted towards the amount due on allotment. Third Alternative - To reject some shares out rightly & pro-rata allotment is made to the remaining applicants.
q) Under Subscription	When number of shares applied is less than the shares offered for subscription, it is called under subscription. In this case, allotment is made in full to all the applicants if minimum subscription is followed. Acc. to SEBI guidelines, minimum subscription means if a company does not receive subscription for at least 90% of the shares issued, it cannot allot the shares. Rather it will have to refund the application money to the subscribers.

Accounting treatment of Issue of Shares to Public for Cash

	Issue at par	*Issue at premium*
1. For Receipt of Application Money	Bank A/c Dr. To Share Application A/c Dr.	Bank A/c Dr. To Share Application A/c (including Premium)
2. For transfer of Application Money	Share Application A/c Dr. To Share Capital A/c	Share Application A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c
3. For Amount Due on Allotment	Share Allotment A/c Dr. To Share Capital A/c	Share Allotment A/c Dr. To Share Capital A/c To securites Premium Reserve A/c
4. For Receipt of AlWment Money	Bank A/c Dr. To Share Allotment A/c	Bank A/c Dr. To Share Allotment A/c (including Premium)
5. For First & Final Call Amount	Share First & Final Call A/c Dr. To Share Capital A/c	Share First & Final Call A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c
6. For Receipt of First & Final call amount	Bank A/c Dr. To Share First & Final Call A/c	Bank A/c Dr. To Share First & Final Call A/c (including Premium)

If Calls in Arrear A/c is Opened

On non-receipt of call amount	Calls-in-arrears A/c Dr. To Relevant Call A/c
On receipt of Calls-in-arrear at a subsequent date	Bank A/c Dr. To Calls-in arrears A/c

Disclosure in Balance Sheet -

It is shown in Note to Accounts in Share Capital as a deduction from the amount of Subscribed but not fully paid up' under Subscribed capital.

If Calls in Advance A/c is Opened

On non-receipt of call amount	Bank A/c Dr. To Calls-in Advance A/c
When relevant call is made due, calls in advance A/c is adjusted	Calls-in Advance A/c Dr. To Relevant Call A/c

Disclosure in Balance Sheet -
It is shown in Equity & Liabilities part of Balance Sheet under the head Current Liabilities & sub-head Other Current Liabilities.

Issue of Shares for Consideration other than Cash	
Issue at par	***Issue at premium***

On Purchase of Assets		
1. On Purchase of Assets	Sundry Assets A/c Dr. To Vendor's A/c	Sundry Assets A/c Dr. To Vendor's A/c
2. On Issue of Shares	Vendor's A/c Dr. To Share Capital A/c	Vendor's A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c
Purchase of Business		
l. On Purchase of Bu ness	Sundry Assets A/c Dr. Goodwill A/c (b/f) Dr. To Sundry Liabilities A/c To Vendor's A/c To Capital Reserve A/c (b/f)	Sundry Assets A/c Dr. Goodwill A/c (b/f) Dr. To Sundry Liabilities A/c To Vendor's A/c To Capital Reserve A/c (b/f)
2. On Issue of Shares	Vendor's A/c Dr. To Share Capital A/c	Vendor's A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c

Number of shares = Amount Payable or Purchase Consideration / Issue Price

Forfeiture of Shares

Forfeiture of shares issued at par	*Forfeiture of shares issued at premium*
(When Premium on issue of shares has been received wholly, it will be treated just like issued at par)	(When Premium has not been received wholly or partially)

If Calls-in-arrear account is not maintained

Share Capital A/c (Called up amount) Dr. To Share Forfeiture A/c (Amount already received) To Share Allotment A/c (unpaid allotment amount) To Share Calls A/c (unpaid calls amount individually)	Share Capital A/c (Called up amount) Dr. Securities Premium Reserve A/c Dr. To share Forfeiture A/c (Amount already received) To Share Allotment A/c (unpaid allotment amount) To Share Calls A/c (unpaid calls amount individually)

If Calls-in-arrear account is maintained

Share Capital A/c (Called up amount) Dr. To Share Forfeiture A/c (Amount already received) To Calls in Arrears A/c (unpaid allotment and calls amount)	Share Capital A/c (Called up amount) Dr. Securities Premium Reserve A/c Dr. To Share Forfeiture A/c (Amount already received) To Calls in Arrears A/c (unpaid allotment and calls amount)

Re-issue of Forfeited Shares

Reissue at par	Re-issue at premium	Reissue at Discount
Bank A/c Dr. To Share Capital A/c	Bank A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c	Bank A/c (re-issued price) Dr. Shares Forfeited A/c (discount) Dr. To Share Capital A/c (at paid-up value)

- **Maximum discount on re-issue of forfeited shares** = Amount forfeited (i.e. amount already received at the time of forfeiture)
- **Minimum re-issue price of a forfeited share**

  = Paid-up value of a share – Forfeited amount per share

  = Amount not received

Transfer of Share Forfeiture A/c to Capital Reserve A/c

(Gain on Reissued Shares)

On Transfer of Share Forfeiture A/c to Capital Reserve A/c	Share Forfeiture A/c Dr. To Capital Reserve A/c Dr.

Case 1) When All Forfeited Shares are Reissued

Profit / Gain on Reissued Shares	= Balance left in Forfeited Shares Account after providing for reissue discount

Case 2) When All Forfeited Shares are not Reissued

Profit / Gain on Reissued Shares =

$$\left\{\frac{\text{Total Amount Forfeited}}{\text{No. of Shares Forfeited}} \times \text{No. of Shares Reissued}\right\} - \text{Reissue Discount}$$

- Reissue Discount means the amount with which Forfeited Shares Account was debited at the time of reissue of such shares.

CHAPTER - 7 SHARE CAPITAL

Illustration l: Bliss Products Ltd. registered with capital of ₹ 90,00,000 divided into 90,000 equity-share, of ₹100 each.

The company issued prospectus inviting applications for 50,000 equity shares of ₹ 100 each payable as ₹ 20 on application, ₹ 30 on allotment, ₹ 20 on first call and balance on second call.

Applications were received for ₹ 40,000 shares. Raman to whom 1600 shares were allotted failed to pay final call money and these shares were forfeited. Of the forfeited shares, 600 shares were reissued to Sukhman, credited as fully paid for ₹ 90 per share.

Present the Share Capital as per Schedule III of Companies Act, 2013

Sol.

Extract of Balance Sheet of Bliss Products Ltd.

As at

Particulars	Note No.	Amount Current Year	Amount Previous Year
I. EQUITY AND LIABILITIES 1. Shareholder's Fund			
a. Share Capital	1	39,70,000	

Notes to Accounts:

Note No.	Particulars		Amount (₹)
1.	**Share Capital**		
	Authorized Capital		90.00.000
	90.000 Equity shares of ₹ 100 each		
	Issued Capital		50,00,000
	50.000 Equity shares of ₹ 100 each		
	Subscribed Capital		
	Subscribed and Fully Paid Capital		39,70,000
	39.000 Equity shares of ₹ 100 each	39,00.000	
	Add: Forfeited Shares (1.000 of ₹ 70 each)	70,000	

Illustration 2: Denpar Ltd. was registered with an authorized capital of ₹ 20,00,000 in shares of ₹ 10 each. Of these, 6,000 shares were issued as fully paid-up to the vendor for purchase of building. 8,000 shares were subscribed for by the people. ₹ 5 per share were called up, payable ₹ 2 on application; ₹ 1 on allotment; ₹1 on first cal and ₹ 1 on second call. The amounts received in respect of these shares were as follows:

On 6000 shares – the full amount called

On 1250 shares – ₹ 4 per shares

On 500 shares – ₹ 3 per shares

On 250 shares – ₹ 2 per shares

Present the capital in the Balance Sheet of the company as per Scheduele II of the Companies Act, 2013. Also prepare Notes to accounts.

Sol.

Balance Sheet of Denpar Ltd. (an Extract)

	Note No.	Current Year (₹)	Previous Year (₹)
I. EQUITY AND LIABILITIES			
1. Shareholder's Fund			
a. Share Capital	1	97,000	

Notes to Accounts:

Particulars	Details	Amount (₹)
Authorized Capital		
20,000 shares of ₹ 10 each		2,00,000
Issued Capital		
6,000 shares of ₹ 10 each issued to vendor of building	60,000	
8,000 shares of ₹ 10 each issued to public	80,000	1,40,000
Subscribed Capital		60,000
Subscribed and Fully Paid Share Capital		
6,000 shares of ₹ 10 each issued to vendor		
Subscribed but not not fully paid share capital		
8,000 shares of ₹ 10 each, ₹ 5 called up	40,000	
Less Calls-in-arrears A/c	(3,000)	37,000
		97,000

Illustration 3: Dev Ltd. has an authorized capital of ₹ 10,00,000 divided into equity shares of ₹ 10 each. The company invited application of 50,000 shares. Applications for 45,000 shares were received. Final call of ₹ 3 per share was not made. All money were duly received except on first call of ₹ 2 per share on 1000 shares. 600 of these shares were forfeited. Present the 'share capital' in the Balance Sheet of the company. Also, prepare Notes to accounts.

Sol.

Balance Sheet of Dev Ltd. (an Extract)

	Note No.	Current Years (₹)	Previous Year (₹)
I. EQUITY AND LIABILITIES 1. Shareholder's Fund			
a. Share Capital	1	3,13,000	

Notes to Accounts:

Particulars	Details	Amount (₹)
Authorized Capital		
1,00,000 shares of ₹ 10 each		10,00,000
Issued Capital		
50,000 equity shares of ₹ 10 each issued to public		5,00,000
8,000 shares of ₹ 10 each issued to public		
Subscribed Capital		
Subscribed but not fully paid share capital		
44,400 equity shares of ₹10 each, ₹ 7 called up	3,10,800	
Add shares forfeited A/c (600 × 5)	3,000	
Less Calls-in-arrears A/c (400 × 2)	(800)	
		3,13,000

Illustration 4: Ram Ltd. has an authorized capital of ₹15,00,000 divided into 1,00,000 equity shares of ₹10 each and 50,000, 9% preference share of ₹ 10 each. The company invited applications for all the preference shares but only 90,000, equity shares.

All the preference shares were subscribed, called and paid while subscriptions were received for only 85,000 equity shares. During the first year ₹ 8 per share were called.

Ram holding 1,000 shares and Shyam holding 2,000 shares did not pay first call of ₹ 2. Shyam's shares were forfeited after the first call and later on 1,500 of the forfeited shares were reissued at ₹ 6 per share 8 called up.

Prepare Balance Sheet as per Schedule III of Companies Act.

Sol.

Extract of Balance Sheet

Particulars	Note No	Amount
Equity and Liabilities		
(i) Shareholder Fund		
(a) Share Capital	1	11,77,000
(b) Reserve and Surplus	2	6,000
		11,83,000

Notes to Account

Particulars		Amount
Share Capital		
Authorized Capital		
1,00,000 equity shares of ₹ 10 each		10,00,000
50,000, 9% preference shares of ₹ 10 each		5,00,000
		15,00.000
Issued Capital		
90,000 equity shares of ₹10 each		9,00,000
50,000, 9% preference shares of ₹ 10 each		5,00,000
		14,00,000
Subscribed Capital		
Subscribed and fully paid		
50,000, 9% preference shares of ₹ 10 each		5,00,000
Subscribed but not fully paid		
84,500 equity shares of ₹ 10 each ₹ 8 called up	6,76,000	
Less: Call in arrears	(2,000)	
Add: shares forfeited	3,000	6,77,000
Reserves and Surplus		
Capital Reserve		6,000
		11,83,000

Illustration 5: Janta Papers Limited invited applications for 1,00,000 equity shares of 25 each payable as under:

On Application ₹5.00 per share
On Allotment ₹7.50 per share
On First Call ₹7.50 per share (due two months after allotment)
On Second and Final Call ₹ 5.00 per share (due two months after First Call)

Applications were received for 4,00,000 shares on January 01, 2022 and allotment was made on February 01, 2022. Record journal entries in the books of the company to record these share capital transactions under each of the following circumstances:

I. The directors decide to allot 1,00,000 shares in full to selected applicants and the applications for the remaining 3,00,000 shares were rejected outright.

II. The directors decide to make a pro-rata allotment of 25 per cent of the shares applied for to every applicant; to apply the balance of application money towards amount due on allotment; and to refund the amount remaining thereafter. The company does not open Calls-in-Advance A/c.

III. The directors totally reject applications for 2,00,000 shares, accept full applications for 80,000 shares and make a pro-rata allotment of the 20,000 shares to remaining applicants and the excess application money is to be adjusted towards allotment and calls to be made.

Sol. **Case I** **Journal**

	Particulars	LF	Dr. (₹)	Cr. (₹)
1 Jan 2022	Bank A/c Dr. To Equity Share Application A/c (Being the money received on application for 4,00,000 shares @ ₹ 5 per share)		20,00,000	 20,00,000
1 Feb 2022	Equity Share Application A/c Dr. To Equity Share Capital A/c To Bank A/c (Being shares allotted & money refunded on rejected applications)		20,00,000	 5,00,000 15,00,000
1 Feb 2022	Equity Share Allotement A/c Dr. To Equity Share Capital A/c (Being amount due on alloment of 1,00,000 shares @ ₹ 7.50 per share)		7,50,000	 7,50,000
1 Feb 2022	Bank A/c Dr. To Equity Share Allomtment A/c (Being the allotment money received)		7,50,000	 7,50,000
1 Apr 2022	Equity Share First Call A/c Dr. To Equity Share Capital A/c (Being final call money due on 1,00,000 shares @ ₹ 7.50 per share)		7,50,000	 7, 50,000
1 Apr 2022	Bank A/c Dr. To Equity Share First Call A/c (Being the first call money received)		7,50,000	7,50,000
1 June 2022	Equity Share Second & Final Call A/c Dr. To Equity Share Capital A/c (Being final call money due on 1,00,000) shares @ ₹ 5 per share)		5,00,000	5,00,000
1 June 2022	Banck A/c Dr. To Equity Share Second and Final Call A/c (Being the final call money received)		5,00,000	5,00,000

Sol. **Case II** **Journal**

Date	**Particulars**	**LF**	**Dr. (₹)**	**Cr. (₹)**
1 Jan 2022	Bank A/c Dr. To Equity Share Application A/c (Being the money received on application for 4,00,000 shares @ ₹ 5 per share)		20,00,000	 20,00,000
1 Feb 2022	Equity Share Application A/c Dr. To Equity Share Capital A/c To Equity Share Allotment A/c To Bank A/c (Being shares allotted, excess application money transferred to allotment account & money refunded on rejected applications)		20,00,000	 5,00,000 7,50,000 7,50,000
1 Feb 2022	Equity Share Allotment A/c Dr. To Equity Share Capital A/c (Being amount due on allotment of 1,00,000 share @ ₹ 7.50 per share)		7,50,000	 7,50,000
1 Apr 2022	Equity Share First Call A/c Dr. To Equity- Share Capital A/c (Being first call money due on 1,00,000 shares @ ₹ 7.50 per share)		7,50,000	 7,50,000
1 Apr 2022	Bank A/c Dr. To Equity Share First Call A/c (Being the first call money received)		7,50,000	 7,50,000
1 June 2022	Equity Share Second & Final Call A/c Dr. To Equity Share Capital A/c (Being final call money due on 1,00,000 shares @ ₹ 5 per share)		5,00,000	 5,00,000
1 June 2020	Bank A/c Dr. To Equity Share Second & Final Call A/c (Being the final call money received)		5,00,000	5,00,000

Sol. **Case III** **Journal**

Date	**Particulars**	**LF**	**Dr. (₹)**	**Cr. (₹)**
1 Jan 2022	Bank A/c Dr. To Equity Share Application A/c (Being the money received on application for 4,00,000 shares @ ₹ 5 per share)		20,00,000	 20,00,000

1 Feb 2022	Equity Share Application A/c Dr. To Equity Share Capital A/c To Call-in-advance A/c To Bank A/c (Being amount of application adjusted to share capital, Share allotment and calls in advance and balance money refunded on rejected applications)		20,00,000	 5,00,000 4,00,000 11,00,000
1 Feb 2022	Equity Share Allotement A/c Dr. To Equity Share Capital A/c (Being amount due on allotment of 1,00,000 @ ₹ 7.50 per share)		7,50,000	 7,50,000
1 Feb 2022	Bank A/c Dr. Calls-in-advance A/c Dr. To Equity Share Allotment A/c (Being the allotment money received)		6,00,000 1,50,000	 7,50,000
1 Apr 2022	Equity Share First Call A/c Dr. To Equity Share Capital A/c (Being final call money due on 1,00,000 shares @ ₹ 7.50 per share)		7,50,000	 7,50,000
1 Apr 2022	Bank A/c Dr. Calls-in-advance A/c To Equity Share First Call A/c (Being calls in advance adjusted against first call and the balance money on call received)		6,00,000 1,50,000	 7,50,000
1 June 2022	Equity share Second and Final Call A/c Dr. To Equity Share Capital A/c (Being final call money due on 1,00,000 shares @ ₹ 5 per share)		5,00,000	 5,00,000
1 June 2022	Bank A/c Dr. Calls-in-advance A/c Dr. To Equity Share Second & Final Call A/c (Being calls in advance adjusted against final call and the balance money on call received)		4,00,000 1,00,000	 5,00,000

Working Notes:

1. Application received for 4.00,000 .shares. 2,00,000 shares were rejected. Remaining 2,00,000 shares were allotcd 1,00,000 shares as follows:
   (a) 80,000 shares were alloted 80,000 shares (i.e. full allotment)
   (b) 1,20,000 shares were alloted 20,000 shares (i.e. pro-rata allotment in the ratio ot 1 : 6)

2. Excess Application Money ₹ 15,00,000

Less: Transfers:

Share allotment 20,000 shares ₹ 7.50	₹ 1.50.000	
Share first call 20,000 shares ₹ 7.50	₹ 1,50.000	
Share second and final call 20.000 shares @ ₹ 5	₹ 1,00.000	₹(4.00.000)
		₹ 11,00,000

Amount to be refunded (including ₹10,00,000 of the rejected applications)

Illustration 6: Saregama Ltd invited applications for issuing 80,000 equity shares of ₹ 100 each at a premium of ₹ 10. The amount was payable as follows

On Application - ₹ 30

On allotment - ₹ 30 (including a premium of ₹ 10)

On 1st call - ₹ 30

On Final Call Balance

Applications of 1,20,000 shares were received. Allotment was made on pro rata basis to all applicants. Excess money received on application was adjusted on sums due on allotment. Dhwani, who was allotted 1,600 shares, failed to pay allotment money and Sargam who applied of 6,000 shares did not pay 1st call money. These shares were forfeited immediately after 1st call. 2,000 of these shares (including all shares of Dhwani were issued to Tarang for ₹ 95 per share as 80 paid up. Pass necessary journal entries in books of Saregama Ltd. by opening call in arrear, call in advance account, if final call has not been made.

Sol. **Journal**

Date	Particulars	L.F	Amount (₹)	Amount (₹)
	Bank A/c Dr. To Share Application A/c (Being the money received on application)		36,00,000	36,00,000
	Share Application A/c Dr. To Equity Share Capital A/c To Calls-in-advance A/c (Being application money adjusted)		36,00,000	24,00,000 12,00,000
	Share Allotment A/c Dr. To Share Capital A/c To securities Premium Reserve A/c (Being amount due on allotment)		24,00,000	16,00,000 8,00,000
	Bank A/c Dr. Calls-in-advance A/c Dr. Calls-in-arrear A/c Dr. To Share Allotment A/c (Being the allotment money received)		11,76,000 12,00,000 24,000	24,00,000

	Share First Call A/c Dr. To Share Capital A/c (Being first call money due) .		24,00,000	24,00,000
	Bank A/c Dr. Calls-in-arrear A/c Dr. To Share First Call A/c (Being first call money received)		22,32,000 1,68,000	24,00,000
	Share Capital A/c Dr. Security Premium reserve A/c Dr. To Calls in Arrear A/c To Share forfeited A/c (Being Dhwani & Sargam's share forfeited for non¬payment of allotment & / or call money)		4,48,000 16,000	2,72,000 1,92,000
	Bank A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c (Being forfeited share's reissued for 95 per share ₹ 80 paid up)		1,90,000	1,60,000 30,000
	Share Forfeited A/c Dr. To Capital Reserve A/c (Being balance in shares forfeited account transferred to capital reserve)		92,000	92,000

Illustration 7: BG Limited issued 2,00,000 equity shares of ₹ 20 each at a premium of ₹ 5 per share. The shares were allotted in the proportion of 5 : 4 of shares applied and allotted to all the applicants.

Deepak, who had aplied for 900 shares, failed to pay Allotment money of ₹ 7 per share (including premium) and on his failure to pay 'First and Final Call' of ₹ 2 per share, his shares were forfeited. 400 of the forfeited shares were reissued at ₹ 15 per share as fully paid up.

Showing your working clearly, pass necessary Journal entries for the Forfeited and reissue of Deepak's shares in the books of BG Limited. The company maintains 'Call in Arrears' Account'.

Sol. **Journal**

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Share Capital A/c Dr. Security Premium reserve A/c Dr. To Calls in Arrear A/c To Share forfeited A/c (Being 720 shares forfeited)		14,400 2,160	3,600 12,960

	Bank A/c Dr. Share Forfeited A/c Dr. To Share Capital A/c (Being 400 forfeited share's reissued @ ₹ 15 each)		6,000 2,000	 8,000
	Share forfeited A/c Dr. To Capital Reserve A/c (Being balance in share forfeited account transferred to capital reserve)		5,200	 5,200

Working Note :

1. Deepak applied for 900 shares. He must have been allotted 900 × $\frac{4}{5}$ = 720 sh.

   Excess money received on application = 900 – 720 = 180 sh. × ₹ 16 = ₹ 2,880

2. Amount due from Deepak on allotment on 720 shares @ 7 each = ₹ 5,400

   Less Excess money on application = (2,880)

   Amount to be paid on allotment = 2,160

   (Out of this amount, 720 × ₹ 2 = ₹ 1,440 is a part of share capital & balance of ₹ 1,440 is a part of securities premium)

3. Securities Premium Reserve related to Deepak's shares is 720 × ₹ 5 = ₹ 3,600

   Out of which. Excess application money already received = (1,440)

   Balance amount not received will be debited in forfeiture entry = 2,160

4. Calls in arrear = Allotment ₹ 2,160 + First & Final call ₹ 1,440 = ₹ 3600

5. Amount transferred to Capital Reserve:

   Since, Forfeited amount on 720 shares = ₹ 12,960

   Hence, Forfeited amount on 400 reissued shares = $\frac{12960}{720}$ × 400 = ₹ 7200

   Less Loss on Reissue 400 shares @ 5 each = (2000)

   Amount transferred to Capital Reserve = ₹ 5200

Illustration 9: R.P. Ltd. forfeited 1,500 shares of Rahim of ₹ 10 each issued at a premium of ₹ 3 per share for non-paymcnl of allotment and first call money. Rahim had applied for 3,000 shares. On these shares, amount was payable as follows :

On application – ₹ 3 per share

On allotment (including premium) – ₹ 5 Per share

On first call – ₹ 3 per share

On final call – Balance

Final call has not been called up 1,000 of the forfeited shares were reissued for ₹ 8,500 as fully paid-up. Record the necessary journal entries for the above transactions in the books of R.P. Ltd. Also, Prepare Share Forfeited A/c.

Sol. **Journal**

Date	Particulars		L.F	Dr. (₹)	Cr. (₹)
	Share Capital A/c	Dr.		12,000	
	Security Premium reserve A/c	Dr.		3,000	
	To Share forfeited A/c				7,500
	To Calls in Arrcar A/c				7,500
	(Being, 1500 shares forfeited)				
	Bank A/c	Dr.		8,500	
	Share Forfeited A/c	Dr.		1,500	
	To Share Capital A/c				10,000
	(Being 1000 forfeited share's reissued)				
	Share Forfeited A/c	Dr.		3,500	
	To Capital Reserve A/c				3,500
	(Being balance in share forfeited account transferred to capital reserve)				

Dr. **SHARE FORFEITED A/c** **Cr.**

Particulars	Amount (₹)	Particulars	Amount (₹)
To Share Capital A/c	1,500	By Share Capital A/c	7,500
To Capital Reserve A/c	3,500		
To Balance c/d	2,500		
	7,500		7,500

Illustration 10:

(a) X Ltd. forfeited 10 shares of ₹10 each, ₹7 called up on which the shareholder had paid application and allotment money of ₹5 per share. Out of these, 8 shares were re-issued to Y for ₹8 per share at ₹8 per paid up per share. Record the journal entries for forfeiture and reissue of shares by opening call in arrear, call in advance account.

(b) L ltd forfeited Mr M's shares who has applied for 600 shares and was allotted 400 shares failed to pay allotment money of ₹ 4 per share including premium of ₹ 2 on which he had paid application money of ₹ 2 only. Pass necessary journal entries for forfeiture of shares by opening call in arrcar, call in advance account.

(c) Crown Ltd forfeited 50 shares of ₹10 each, for non- payment of final call money of ₹ 3 per share. Out of these 20 shares were reissued to Taj at ₹8 per share. Record the journal entries for forfeiture and reissue of shares assuming that the company maintains call in arrcar, call in advance account.

Sol. (a) **Journal**

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Equity Share Capital A/c Dr.		70	
	To Equity Share Forfeiture A/c			50
	To Calls-in Arrear A/c			20
	(Being 10 shares forfeited)			
	Bank A/c Dr.		64	
	To Equity Share Capitial A/c			64
	(Being 80 shares reissued as ₹ 8 per share paid up for ₹ 8 per share)			
	Equity Share Forfeited A/c Dr.		40	
	To Capital Reserve A/c			40
	(Being the balance in share forfeited account transferred to capital reserve)			

Sol. (b) **Journal**

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Equity Share Capital A/c Dr.		1,600	
	Securities Premium Reserve A/c Dr.		1,800	
	To Equity Share Forfeiture A/c			1,200
	To Calls-in Arrear A/c			1,200
	(Being Mr. M's shares forfeited)			

Sol. (c) **Journal**

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Equity Share Capital A/c Dr.		500	
	To Equity Share Forfeiture A/c			350
	To Calls-in Arrear A/c			150
	(Being 50 shares forfeited)			
	Bank A/c Dr.		160	
	Equity Share Forfeited A/c Dr.		40	
	To Equity Share Capital A/c			200
	(Being 20 shares forfeited as ₹ 8per share)			
	Equity Share Forfeited A/c Dr.		100	
	To Capital Reserve A/c			100
	(Being the balance in share forfeited account transferred to capital reserve)			

Illustration 11: Khyati Ltd. issued a prospectus inviting applications for 80,000 equity) shares of ₹ 10 each payable as follows:

₹ 2 on application

₹ 3 on allotment

₹ 2 on first call

₹ 3 on final call

Applications were received for 1,20,000 equity shares. It was decided to adjust the excess amount received on account of over subscription till allotment only. Hence allotment was made as under:

(i) To applicants for 20,000 shares - in full

(ii) To applicants for 40,000 shares - 10,000 shares

(iii) To applicants for 60,000 shares - 50,000 shares

Allotment was made and all shareholders except Tamanna, who had applied for 2,400 shares out of the group (iii), could not pay allotment money. Her shares were forfeited immediately, after allotment. Another shareholder Chhaya ,who was allotted 500 shares out of group (ii), failed to pay first call. 50% of Tamanna's shares were reissued to Satnaam as ₹ 7 paid up for payment of ₹ 9 per share.

Pass necessary journal entries in the books of Khyati Ltd. for the above transactions by opening calls in arrears and calls in advance account wherever necessary.

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Bank A/c Dr.		2,40,000	
	To Equity Share Application A/c			2,40,000
	(Being the application money received on 1,20,000 shares @ ₹ 2 per share)			
	Equity Share Application A/c Dr.		2,40,000	
	To Equity Share Capital A/c			1,60,000
	To Equity Share Allotment A/c			50,000
	To Bank A/c			30,000
	(Being shares allotted, excess application money transferred to allotment account & money refunded on rejected applications)			
	Equity Share Allotment A/c Dr.		2,40,000	
	To Equity Share Capital A/c			2,40,000
	(Being amount due on allotment of 80,000 shares @ ₹ 3 per share)			

	Bank A/c Dr. Calls-in Arrear A/c Dr. To Equity Share Allotment A/c (Being the allotment money received on 80,000 shares after adjusting excess application money)		1,84,800 5,200	 1,90,000
	Equity Share Capital A/c Dr. To Share Forfeiture A/c To Calls-in Arrear A/c (Being 2,000 shares forfeited)		10,000	 4,800 5,200
	Equity Share First Call A/c Dr. To Equity Share Capital A/c (Being first call money due on 78,200 shares @ ₹ 2 per share)		1,56,000	 1,56,000
	Bank A/c Dr. Calls-in Arrear A/c Dr. To Equity Share first Call A/c (Being the first call money received)		1,55,000 1,000	 1,56,000
	Bank A/c (1000 × 9) Dr. To Equity Share Capital A/c To Security Premium Reserve A/c (Being 1,000 forfeited shares reissued @ 7 paid up, for ₹ 9 per share)		9,000	 7,000 2,000
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Being the balance of share forfeiture account transferred to capital reserve)		2,400	 2,400

Working Note :

1. In Category (ii) applicants of 40,000 shares arc allotted 10,000 shares

   Excess money received on application

   = 40.000 – 10,000 = 30,000 sh. x ₹ 2 = ₹ 60,000

   Since amount due on allotment on 10,000 shares @3 each = ₹30,000.

   Only ₹30.000 can be adjusted & remaining ₹30,000 will be returned.

   In Category (iii) applicants of 60,000 shares arc allotted 50,000 shares

   Excess money received on application

   = 60,000 – 50,000 = 10,000 sh. x ₹2 = ₹ 20,000

   Entire excess of ₹20,000 will be adjusted on allotment.

Total Excess money received on application = ₹30,000 + ₹20,000 = ₹50,000

2. Shares allotted to Tamanna = $2400 \times \frac{50,000}{60,000}$ = 2000 shares

Excess money received from Tamanna = 2400 – 2000 = 400 sh. × ₹2 = ₹800

3. Amount not received from Tamanna on allotment

Amount due on allotment	= 2000 × 3 = ₹6000
Less Excess money on application	= (800)
	5,200

4. Amount received on allotment

Total Amount due on allotment	= 80,000 sh. X ₹3 = 2,40,000
Less Excess money on application	= (50,000)
Less Amount not received from Tamanna	= (5,200)
	1,84,800

Illustration 12: Concept Stationary Ltd. invited applications for issuing 3,00,000 shares of ₹10 each at a premium of ₹3 per share. The amounts were payable as follows :

On application and allotment – ₹7 per share.

On first & final call – balance (including premium of ₹3)

Applications were received for 4,00,000 shares & allotment was made as follows :

(i) To applicants for 80,000 shares – 80,000 shares.

(ii) To applicants for 40,000 shares – nil

(iii) Balance of the applicants were allotted shares on pro-rata basis.

Excess money received with applications was adjusted towards sums due on first and final call. Amit, who belonged to category (i) and was allotted 4,000 shares and Veni, who belonged to category (iii) and was allotted 4,400 shares failed to pay the first and final call money. Their shares were forfeited.

The forfeited shares were re-issued at ₹7 per share fully paid-up. Pass necessary journal entries for the above transactions in the books of the company.

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Bank A/c Dr.		28,00,000	
	To Share Application & Allotment A/c			28,00,000
	(Being the application & allotment money received on 4,00,000 shares @ ₹ 7 per share)			

	Share Application & Allotment A/c Dr. To Share Capital A/c To Calls in Advance A/c To Bank A/c (Being shares allotted, excess application money transferred to allotment account & money refunded on rejected applications)		28,00,000	 21,00,000 4,20,000 2,80,000
	Share First & Final Call A/c Dr. To Share Capital A/c To Securities Premium Reserve A/c (Being first & final call money due)		18,00,000	 9,00,000 9,00,000
	Bank A/c Dr. Calls-in Arrear A/c Dr. Calls-in Advance A/c Dr. To Share First Call A/c (Being the first call money received) **OR** Bank A/c Dr. Calls-in Advance A/c Dr. To Share Capital A/c (Being the first call money received)		13,38,000 42,000 4,20,000 13,38,000 4,20,000	 18,00,000 17,58,000
	Share Capital A/c Dr. Securities Premium Reserve A/c Dr. To Share Forfeiture A/c To Calls-in Arrear A/c (Being 8,400 shares forfeited)		84,000 25,200	 67,200 42,000
	Bank A/c Dr. Share Forfeiture A/c Dr. To Share Capital A/c (Being forfeited shares reisssued @ 7 per share, as fully paid up)		58,800 25,200	 84,000
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Being the balance of share forfeiture account transferred to capital reserve)		42,000	 42,000

Illustration 13: DLF Ltd. invited applications for issuing 50,000 shares of ₹10 each at a premium of ₹2 per share. The amount was payable as follows:

On application ₹3 per share (including premium ₹1)

On Allotment ₹3 per share (including premium ₹1)

On First Call ₹3 per share

On Second & Final Call Balance amount

Applications for 70,000 shares were received. Allotment was made on the following basis:

Applications for 10,000 shares - Full;

Applications for 50,000 shares - 80%

Balance of the applications were rejected.

₹ 1,13,250 were received on account of allotment. A few shareholders to whom shares were allotted on pro-rata basis, failed to pay the allotment money ₹1,41,000 were received on first call. The directors decided to forfeit all those shares on which amount was due but was not received. The forfeited shares were re-issued @8 per share fully paid up. Final call was not made.

Pass the necessary journal entries assuming that the company maintains Calls-in-Arrears Account.

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Bank A/c Dr.		2,10,000	
	To Equity share Application A/c			2,10,000
	(Being the application money received on 70,000 shares@ ₹3 per share)			
	Equity Share Application A/c Dr.		2,10,000	
	To Equity Share Capital A/c			1,00,000
	To Securities Premium Reserve A/c			50,000
	To Equity Share Allotment A/c			30,000
	To Bank A/c Dr.			30,000
	(Being shares allotted,excess application money transferred to allotment account and money refunded on rejected application)			
	Equity Share Allotment A/c Dr.		1,50,000	
	To Equity Share Capital A/c			
	To Securities Premium Reserve A/c			1,00,000
	(Being amount due on allotment of 50,000 shares @ ₹2 + 1 per share)			50,000
	Bank A/c Dr.		1,13,250	
	Calls-in Arrear A/c Dr.		6,750	
	To Equity Share Allotment A/c			1,20,000
	(Being the allotment money received on 50,000 shares @ ₹3 per share after adjusting excess application money)			

	Equity Share First Call A/c Dr. To Equity Share Capital A/c (Being first call money due on 50,000 shares @ ₹ 2 + 1 per share)		1,50,000	 1,50,000
	Bank A/c Dr. Calls-in Arrear A/c Dr. To Equity Share First Call A/c (Being the first call money received)		1,41,000 9,000	 1,50,000
	Equity Share Capital A/c (3000 × 7) Dr. Securities Premium Reserve A/c (3000 × 2) Dr. To Share Forfeiture A/c To Calls-in Arrear A/c (Being 3,000 shares forfeited)		21,000 6,000	 11,250 15,750
	Bank A/c (3000 × 8) Dr. Share Forfeiture A/c Dr. To Equity Share Capital A/c (Being forfeited shares reissued @ 8 per share, as fully paid up)		24,000 6,000	30,000
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Being the balance of share forfeiture account transferred to capital reserve)		5,250	 5,250

Working Note:

No. of shares forfeited = Unpaid first call money/ Amount of first call per share

= ₹9,000/ ₹3

= 3,000 shares

If 3,000 shares are allotted, then no. of shares applied = $\frac{50}{40} \times 3000 = 3750$ shares

Amount received on 3750 shares on application @ 3 per share = ₹11,250

Amount due on 3000 shares on application @ 3 per share = ₹ 9000

Excess application money adjusted towards allotment = ₹ 2250

Illustration 14: Sudarshan Ltd. invited applications for 1,00,000 Equity Shares of ₹10 each. The shares are issued at a premium of ₹5 per share. The amount was payable as follows:

On Application & Allotment	₹8 per share (including premium ₹3)
On First & Final Call	Balance including premium

Applications for 1,50,000 shares were received. Applications for 10,000 shares were rejected & Pro-rata was made to the remaining applicants on the following basis:

(i) Applications for 80,000 shares were allotted 60,000 shares

(ii) Applications for 60,000 shares were allotted 40,000 shares

X, who belonged to the first category & was allotted 300 shares, failed to pay the first call money. Y, who belonged to the second category & was allotted 200 shares also failed to pay the first call money. Their shares are forfeited. The forfeited shares were issued @ 12 per share fully paid up. Final call was not made.

Pass the necessary journal entries & prepare Cash Book.

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Equity Share Application & Allotment A/c Dr. To Equity Share Capital A/c To Securities Premium reserve A/c To Calls in Advance A/c (40,000 sh. @ ₹ 8) (Being shares allotted, excess application money transferred to allotment)		11,20,000	 5,00,000 3,00,000 3,20,000
	Equity Share First & Final Call A/c Dr. To Equity Share Capital A/c To Securities Premium Reserve A/c (Being first & final call money due on 1,00,000 shares)		7,00,000	 5,00,000 2,00,000
	Call-in Advance A/c Dr. To Equity Share First & Final Call A/c (Being the calls in advance adjusted to share first & final call A/c)		3,20,000	 3,20,000
	Equity Share Capital A/c Dr. Securities Premium Reserve A/c Dr. To Equity Share First & Final Call A/c To Share Forfeiture A/c (Being 300 shares of X & 200 shares of Y forfeited)		5,000 1,000	 1,900 4,190
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Being the balance of share forfeiture account transferred to capital reserve)		4,100	 4,100

Dr. **CASH BOOK** **Cr.**

Particulars	Amount (₹)	Particulars	Amount (₹)
To Equity Shave Application & Allotment A/c (1,50,000 shares × ₹8)	12,00,000	By Equity Share Application & Allotment A/c (Refund of applications for 10,000 shares @8 per share)	80,000
To Equity Share First & Final Call A/c	3,78,000	By Balance c/d	15,04,100
To Equity Share Capital A/c	5,000		
To Securities Premium Reserve A/c	1,000		
	15,84,100		**15,84,100**

Working Note :

1. No. of shares applied by X = $\frac{80,000}{60,000} \times 300 = 400$

   No. of shares applied by Y = $\frac{80,000}{60,000} \times 200 = 300$

2. Excess amount received from X = 400 – 300 = 100 shares @ ₹8 = ₹ 800

   Excess amount received from Y = 300 – 200 = 100 shares @ ₹8 = ₹ 800

3. Amount due from X & Y on First & Final call = ₹3,500

   (300 sh. @ ₹ 7 of X ; 200 sh. @ ₹ 7 of Y)

   Less Excess received on Application & Allotment = (1,600)

   Amount due but not paid on First & final call = 1,900

4. Total Amount due on First & Final call = ₹7,00,000

   Less Excess Received on Application & Allotment = (3,20,000)

   Less Amount not received from X and Y on First and Final Call = (1,900)

   Amount due but not paid on First & Final call = 3,78,100

Illustration 15: From the following information complete Journal entries.

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Share Capital A/c Dr.		?	
	Securities Premium Reserve A/c Dr.		1000	
	To Share Forfeiture A/c			
	To Calls in Arrears A/c			3,500
	(Being ......? ...... shares forfeited for non payment of ...? ... including premium of ₹ 2 per share)			

	Bank A/c Dr. Share Forfeiture A/c Dr. To Share Capital A/c (Being __?__shares reissued at `9 per share as fully paid)		? ?	?
	Share forfeiture A/c Dr. To Capital Reserve A/c (Being forfeiture money transferred to capital reserve)		600	600

Dr. **Share Forfeited A/c** **Cr.**

Particulars	Amount (₹)	Particulars	Amount (₹)
To Share Capital A/c	?	By Share Capital A/c	1500
To Capital Reserve A/c	600		
To Balance c/d	600		
	1500		1500

Sol.

Date	Particulars	L.F	Dr. (₹)	Cr. (₹)
	Share Capital A/c Dr. Securities Premium Reserve A/c Dr. To Share Forfeiture A/c To Calls in Arrears A/c (Being 500_shares forfeited for non-payment of ₹7 per share including premium of ₹2 per share).		4,000 1,000	1,500 3,500
	Bank A/c Dr. Share Forfeiture A/c Dr. To Share Capital A/c (Being 300_shares reissued at ₹ 9 per share as fully paid).		2,700 300	3,000
	Share forfeiture A/c Dr. To Capital Reserve A/c (Being forfeiture money transferred to capital reserve)		600	600

Dr. **Share Forfeited A/c** **Cr.**

Particulars	Amount (₹)	Particulars	Amount (₹)
To Share Capital A/c	300	By Share Capital A/c	1500
To Capital Reserve A/c	600		
To Balance c/d	600		
	1500		1500

Illustration 16: Vinod Ltd. forfeited 5,000 shares of Rs.10 each, fully called-up, on which they had received only Rs.35,000. Out of the forfeited shares 125 were reissued for Rs.9 per share fully paid up. Fill the following missing figures:

Date	Particulars	L.F	Debit (?)	Credit (?)
	Share Capital A/c Dr. To Share Forfeiture A/c To Calls in Arrears A/c (Being 5,000 shares forfeited for non-payment ofRs.15,000)		?	?
	Bank A/c Dr. Share Forfeiture A/c Dr. To Share Capital A/c (Being 125 forfeited shares reissued)		? ?	?
	Share Forfeiture A/c Dr. To Capital Reserve (Being gain on reissue of shares)		?	?

Sol. **Journal**

Date	Particulars	L.F	Debit (?)	Credit (?)
	Share Capital A/c Dr. To Share Forfeiture A/c To Calls-in-arrear A/c (Being 5000 shares forfeited for non-payment of ₹ 15000)		50,000	35,000 15,000
	Bank A/c Dr. Share Forfeiture A/c Dr. To Share Capital A/c (Being 125 forfeited shares reissued)		1,125 125	1,250
	Share Forfeiture A/c Dr. To Capital Reserve A/c (Being gain on reissue of shares)		750	750

PRACTICE QUESTIONS

Q.1. On 1st April, 2012, .Janta Ltd. was formed with an authorized capital of ₹50,00,000 divided into 1,00,000 equity shares of ₹50 each. The company issued prospectus inviting application for 90,000 Shares. The issue price was payable as under:

On application ₹15 on allotment 20, balance on final call

The issue was fully subscribed and the company allotted shares to all the applicants. The company did not make the call during the year.

Show the following:

(a) Share capital in the Balance sheet of the company as per revised schedule III, Part-I of the companies Act, 2013.

(b) Also prepare' Notes to Accounts for the same. {Hint: Subscribed but not fully paid up - ₹ 31,50,000}

Q.2. Sibar Media & Entertainment Ltd. invited applications for 1,00,000 shares of ₹10 each at a premium of 10% payable as follows:

On Application	₹3
On Allotment	₹4 (including premium)
On first & final call	₹4

The applications were received for 90,000 shares and all of these were accepted. All money due were received except the first and final call on 2,000 shares which were forfeited. 1,000 shares were re¬issued @ ₹ 9 per share as fully paid. Assuming that all requirements of law were complied with, show how these transactions will be reflected in the company's Balance Sheet.

{Hint: Subscribed and fully paid: ₹8,90,000}

Q.3. Pass necessary journal entries for the following transactions in the Books of Rajan Ltd.

(a) Rajan Ltd. purchased machinery of ₹7,20,000 from Kundan Ltd. The payment was made to Kundan Ltd. by issue of equity shares of ₹ 100 each at 20% premium.

(b) Rajan Ltd. purchased a running business from Vikas Ltd. for a sum of ₹2,50,000 payable as ₹2,20,000 in fully paid equity shares of ₹10 each and balance by a bank draft. The assets and liabilities consisted of the following: Plant & Machinery ₹90,000; Buildings ₹90,000; Sundry Debtors ₹30,000; Stock 50,000; Sundry Creditors ₹20,000; Cash ₹20,000

{Hint: (a) Equity shares issued = 6000 ; (b) Capital reserve - ₹10,000}

Q.4. Elpha ltd. Forfeited 400 shares of Rohit which were issued at ₹10 per share and ₹2 as premium for non payment of allotment money of ₹5 (including premium) and first call of ₹2, final call of ₹3 has not been done.

{Hint: Share forfeiture A/c - ₹800}

Q.5. Ram holding 10 shares of ₹10 each of which ₹2 on application ₹3 on allotment but could not pay ₹3 on first call. His shares were forfeited by the Director. The Final call is not made yet. Give Journal entries in the book of company.

{Hint: Share forfeited ₹50}

Q.6. Abhishek. Ltd. Forfeited 200 shares of ₹10 each fully called up held by X for non-payment of allotment money of ₹3 per share and First & Final call of ₹4 per share. He paid the application money of ₹3 per share. These shares were reissued to Y for ₹8 per shares. Pass necessary journal entries.

{Hint: capital reserve ₹200}

Q.7. Max Ltd. forfeited 500 shares of ₹100 each for non-payment of first call of ₹20 per share and final call of ₹25 per share 250 of these shares were re-issued at ₹50 per share fully paid-up. Pass the necessary journal entries in the books of Max Ltd. for forfeiture and re-issue of shares. Also prepare the Share Forfeiture Account

(Hint: capital reserve ₹1250; Total of Share Forfeited A/c ₹27,500)

Q.8. AB Lid invited applications for ₹1,00,000 Equity Shares ₹10 each payable as ₹2 application, ₹3 on Allotment and the balance on first and final call. Application were received for ₹3,00,000 shares and shares were allotted on prorata basis. The excess application money was to be adjusted against allotment only. Ram, a shareholder who has applied for 3,000 shares failed to pay the call money and his shares were forfeited and re-issued at ₹8 per share as fully paid. Pass necessary journal entries in the books of company.

(Hint: Share forfeited A/c ₹5000, capital reserve ₹3000)

Q.9. AB Ltd. invites application for 75,000 equities of ₹100 each at premium of ₹30 per share. The amount was payable as follows

On Application and allotment ₹85 per share (including premium) First and final call - The balance amount

Application for 1,27,500 shares were received. Applications for 27,500 shares were rejected and shares were allotted on pro-rata basis to remaining applicants. Excess money received on application and allotment was adjusted towards sum due on first and final call. The calls were made. A shareholder who applied for 1,000 shares, failed to pay the first and Final call money His shares were forfeited. All the forfeited shares were reissued at 150 per share fully paid up. Pass necessary journal entries for the above transaction in the books of AB Ltd.

(Hint: Capital reserve ₹62500)

Q.10. A holds 100 share of ₹10 each on which he has paid ₹1 per share on application.

B holds 200 shares of ₹10 each on which he has paid ₹ 1 and ₹2 share on application and allotment respectively.

C holds 300 shares of ₹10 each and he has paid ₹ 1, ₹2 and ₹3 per share on application, allotment and first call respectively.

They all failed to pay their arrears and the second call of ₹2 per share, subsequently, their shares were forfeited and then reissued at ₹11 per share as fully paid. Pass necessary journal entries.

{Hint: Amount transferred to Capital Reserve – ₹2500}

	Amount forfeited	Allotment (2)	First call (3)	2nd call (2)	
A(100)	✓ 100	× 200	× 300	× 200	800
B(200)	✓ 200	✓ 400	× 600	× 400	1600
C(300)	✓ 300	✓ 600	✓ 900	× 600	2400
	✓ 600	✓ 1000 × 200	✓ 900 × 900	× 1200	4800

Q.11. AB Ltd. invited applications for 1,00,000 Equity Shares ₹10 each payable as ₹2 application, ₹3 on Allotment and the balance on first and final call. Application were received for 3,00,000 shares and shares were allotted on prorate basis. The excess application money was to be adjusted against allotment only.

Ram, a shareholder who has applied for 3,000 shares failed to pay the call money and his shares were forfeited and re-issued at ₹8 per share as fully paid. Pass necessary journal entries in the books of company prepare Cash Book and journal for the above transaction.

{Hint: Cash book Total - 11,03,000; Amount transferred to Capital Reserve - ₹3000}

Q.12. Beta Ltd. issued 40,000 shares of ₹10 each at a premium of ₹2 payable ₹5 on application including premium, ₹4 on allotment and ₹3 on call.

Company received applications for 55,000 shares and allotment was made as under:

(i) Applicants for 20,000 shares were allotted in full.

(ii) Applicants for 25,000 shares were allotted 20,000 shares.

(iii) Applicants for rest shares were allotted Nil shares.

Mr. X who was allotted 200 shares under category (i) paid full amount due on allotment.

Mr. Y holding 500 shares failed to pay call money. His shares were forfeited and reissued @ ₹8 per share fully paid.

{Hint: Amount transferred to Capital Reserve – ₹500}

Q.13. HP Ltd. issued 50,000 shares of ₹10 each payable ₹3 on application, ₹4 on allotment and ₹2 on final call. Company received applications for 70,000 shares and allotment was made on prorata basis. Alok who had applied for 700 shares failed to pay allotment and his shares were forfeited after allotment. Mohit failed to pay call money on 300 shares and his shares were forfeited. Company-reissued 500 shares ₹8 each fully paid up, including all the shares of Mohit. Journalise the transactions and draw Balance Sheet.

{Hint: Amount transferred to capital Reserve – ₹2440}

Q.14. Dawar Ltd. issued 50,000 shares of 10 each at a premium of 10% payable at a ₹2 per share on application, ₹3 on allotment, ₹3 each on first and final call. Applications were received for 70,000 shares. It was decided that:

(a) Refuse allotment to the applicants for 10,000 shares;

(b) After 20,000 shares to Pawan who had applied for similar number and

(c) Allot the remaining shares on pro-data basis.

Pawan failed to pay the allotment money and Mohan who belonged to the category 'C and was allotted 3,000 shares, paid both the calls with allotment. Calculate the amount received on allotment.

{Hint: Allotment due 50,000 × 3 = 1,50,000,

Excess application money adjusted ₹20,000; Calls received in Advanced ₹18,000; Amount Received on Allotment ₹88,000 (1,50,000 – 20,000 – 60,000 + 18,000)}

Q.15. Rama Ltd. issued 40,000 shares of ₹10 each at a premium of ₹2.50 per share. The amount was payable as follows:

On Application – ₹2 per share

On Allotment – ₹4.50 per share

On First and Final Call ₹ 6 per share

Owing to the heavy subscription, the allotment was made on pro-rata basis as follows:

(i) Applicants for 20,000 shares were allotted 10,000 shares.

(ii) Applicants for 56,000 shares were allotted 14,000 shares.

(iii) Applicants for 48,000 shares were allotted 16,000 shares.

It was decided that excess amount received on applications would be utilized on allotment and the surplus, if any, would be refunded. The directors decided to forfeit the shares of one shareholder Shyam, to whom, 1000 shares were allotted, who belongs to category (i), failed to pay allotment Money. Shares were forfeited after final call.

You are required to Pass necessary journal entries in the books of Rama Ltd. for the issue and forfeiture of shares.

{Hint: (1) Transfer of share application money to Share Capital A/c ₹80,000; to Share Allotment A/c ₹1,47,000; to bank A/c ₹21,000.

(2) Share Allotment Money Received in Cash ₹30,500,

(3) Amount forfeited ₹4,000}

Q.16. High Light India Ltd. imited applications for 30,000 Shares of ₹100 each at a premium of ₹20 per share payable as follows:

On Application ₹40 (including 10 premium)

On Allotment ₹30 (including 10 premium)

On First Call ₹30

On Second and Final Call ₹20

Applications were received for 40,000 shares and pro-rata allotment was made on the application for 35,000 share. Excess application money was utilised towards allotment. Rohan to whom 600 shares were allotted failed to pay the allotment money and his shares were forfeited immediately after allotment. Aman who applied for 1,050 shares failed to pay first call and his share were forfeited immediately after first call. Second and final call was made. All the money due on second call have been received.

Of the shares forfeited, 1,000 share were reissued as fully paid-up for ₹8o per share, which included the whole of Aman's shares. Record necessary journal entries in the books of High Light India Ltd. Also present the share capital in Balance Sheet of the company showing above transactions. As a matter of policy, the company does not maintain Calls-in-arrear account.

{Hint: Amount transferred to Capital Reserve – ₹28,667 ; Subscribed & fully paid up – ₹29,50,000 ; Share Forfeited A/c – ₹18,333}

Q.17. Karur Ltd. invited applications for issuing 2,40,000 equity shares of ₹10 each at a premium of ₹4 per share. The amount was payable as under: On application ₹4 per share (including premium ₹2) On allotment ₹4 per share On first and final call ₹6 per share (including premium ₹2) Applications for 3,00,000 shares were received and pro-rata allotment was made to all the applicants. Excess application money received on application was adjusted towards sums due on allotment. All calls were made and were duly received except from Rohini, who failed to pay allotment and first and final call on 7,500 shares applied by her. These shares were forfeited Afterwards, 40% of the forfeited shares were re-issued at ₹11 per share as fully paid-up. Pass the necessary journal entries in the books of Karur Ltd. Open call-in-arrears and call-in advance accounts wherever necessary.

(Hint: Amount transferred to Capital Reserve – ₹7,200, Calls in arrear – ₹18,000 in allotment ₹ 36,000 in first call = ₹54,000)

Q.18. On 1st Jan 2022, Saraswati Ltd. issued 50,000 equity shares of ₹10 each at a premium of ₹4 per share, payable as follows:

On Application ₹6 (including ₹1 premium)

On Allotment ₹2 (including ₹1 premium)

On First Call ₹4

On Second and Final Call ₹2

Applications were received for 65,000 shares, of which applications for 5,000 shares were rejected & their money was refunded. Rest of the applications were issued shares on pro-rata basis & their excess money was towards allotment.

Ashok to whom 1,000 shares were allotted failed to pay the allotment money and his shares were forfeited immediately after allotment. Kohan, who applied for 1,800 shares failed to pay the two calls and his share were forfeited after the final call. 1,900 share were reissued as fully paid-up on receipt of ₹9 per share, which included the whole of Rohan's shares.

Record necessary journal entries.

(Hint: Amount transferred to Capital Reserve – ₹9,500)

ASSERTION - REASONING QUESTIONS

1. **Assertion (A):** In case of shares issued on Pro-rata basis, excess money received at the time of application can be utilized till allotment only.

   Reason (R): Company has to pay interest on calls in advance for amount adjusted towards call (if any).

   Codes:

   (A) Both (A) & (R) are true, but (R) is not the correct explanation of (A),

   (B) Both (A) & (R) are true, but (R) is the correct explanation of (A).

   (C) Both (A) & (R) are false.

   (D) (A) is false, but (R) is true.

2. **Assertion (A):** X Ltd. issued 50,000 Equity shares of ₹100 each. It received the full amount on shares except first & final of ₹25 on 200 shares. These 200 shares will be shown as 'Subscribed but not fully paid Capital'.

   Reason (R): The shares on which calls are in arrears are not fully paid. Hence, they will be shown as Subscribed but not fully paid Capital'

   Codes:

   (A) Both (A) & (R) are correct and (R) is the correct reason of (A).

   (B) Both (A) & (R) are correct but (R) is not the correct reason of (A).

   (C) Only (R) is correct.

   (D) Both (A) and (R) are wrong.

3. **Assertion (A):** Calls in arrears are deducted from Subscribed but not fully paid Capital.

   Reason (R): Calls in advance are added to Subscribed but not fully paid Capital.

   Codes:

   (A) Both (A) & (R) are correct and (R) is the correct reason of (A).

   (B) Both (A) & (R) are correct but (R) is not the correct reason of (A).

   (C) Only (A) is correct.

   (D) Both (A) and (R) are wrong.

4. **Assertion (A):** Forfeited shares may be reissued by the company at a discount also.

   Reason (R): Amount of discount on reissue of forfeited shares cannot exceed the amount forfeited on reissued shares.

   Codes:

   (A) Both (A) & (R) are correct and (R) is the correct reason of (A).

   (B) Both (A) & (R) are correct but (R) is not the correct reason of (A).

   (C) Only (R) is correct.

   (D) Both (A) and (R) are wrong

5. **Assertion (A):** Issued Share Capital & Subscribed Share Capital are always different.

   Reason (R): Subscribed Share Capital is a part of Issued Share Capital. Thus, it will always be different from Issued Share Capital.

   Codes:

   (A) Both (A) & (R) are correct and (R) is the correct reason of (A)

   (B) Both (A) & (R) are correct but (R) is not the correct reason of (A)

   (C) Both (A) & (R) are incorrect.

   (D) (A) is correct but (R) is incorrect.

MULTIPLE CHOICE QUESTIONS

1. The forfeited shares can be reissued at:

   (a) Par (b) Premium

   (c) Discount (d) All of them

2. Ordinary shares are also called:

   (a) Equity shares (b) Founder's shares

   (c) Deferred shares (d) Preference shares

3. Forfeited amount is credited to
   (a) Share premium (b) Share capital
   (c) Forfeited shares (d) None of these
4. The maximum amount with which the company is registered is called.
   (a) Authorized Share Capital (b) Issued Share Capital
   (c) Paid up capital (d) Called up capital
5. When shares are issued at premium amount of premium will be credited to
   (a) Securities premium account (b) Share first call account
   (c) Share allotment account (d) Share forfeited account
6. Minimum number of members in case of public company is
   (a) 4 (b) 5
   (c) 6 (d) 7
7. Maximum number of members in public limited company is
   (a) 10 (b) 20
   (c) 50 (d) unlimited
8. Premium on issue of shares can be used for
   (a) distribution of dividend (b) writing of capital losses
   (c) transferring to general reserve (d) paying fees to directors
9. Share allotment account is a
   a) personal account b) Real account
   c) Nominal account d) Impersonal account
10. A company forfeited 3,000 shares of ₹10 each (which were issued at par) held by Kishore for non-payment of allotment money of ₹5 per share. The called up value per share was ₹8 on forfeiture, the amount debited to share capital -
    (a) ₹30,000 (b) ₹24,000
    (c) ₹15,000 (d) ₹6,000
11. Z limited issued shares of ₹100 each at a premium of 10%. Premium is to be adjusted with allotment. Mr. Q holding 500 shares paid ₹ 20 on application but did not pay the allotment money of ₹30. If the company forfeited his 30% shares immediately after allotment, the share forfeiture account will be credited by–
    (a) ₹4,500 (b) ₹13,500
    (c) ₹1,650 (d) ₹3,000
12. Mithas Limited was formed with share capital of ₹50,00,000 divided into 50,000 shares of ₹100 each. 9,000 shares were issued to the vendor as fully paid for purchase consideration of a furniture acquired. 30,000 shares were allotted in payment of cash on which ₹70 per share was called and paid. State the amount of subscribed capital.

(a) ₹50,00,000 (b) ₹30,50,000

(c) ₹30,00,000 (d) ₹120,00,000

13. Metacaf Ltd. issued 50,000 shares of ₹100 each payable 20 on application (on 1st May 2018) ₹30 on allotment (on 1st January 2019); ₹20 on first call (on 1st July 2019) and the balance on final call (on 1st February 2020). Shankar, a shareholder holding 5,000 shares did not pay the first call on the due date. The second call was made and Shankar paid the first call amount along with the second call. All sums due were received. Total amount received on 1st February was

(a) ₹15,00,000 (b) ₹16,00,000

(c) ₹10,00,000 (d) ₹11,00,000

14. A company allotted 20,000 shares to the applicants of 50,000 shares after rejecting 10,000 applications. The ratio in which company allotted the shares will be

(a) 2 : 5 (b) 3 : 5

(c) 1: 2 (d) 1: 3

Fill in the blanks

(a) The portion of the authorised capital which can be called up only on the liquidation of the company is called_______.

(b) G Ltd acquired assets worth 7,50,000 from H Ltd. by issue of shares of 100 at a premium of 25%.The number of shares to be issued by G Ltd. to settle the purchase______. .

(c) Maximum amount that can be collected as premium as a percentage of face value________.

(d) Loss of re-issue should not exceed the ______ amount.

(e) The subscribed capital of a company is 80,00,000 and the nominal value of the share is 100 each. There were no calls in arrear till the final call was made. The final call made was paid on 77,500 shares only. The balance in the calls in arrear amounted to ₹55,000. The final call amount per share is_______.

(f) At the time of forfeiture of shares, Share Capital Account will be debited with ________Value.

(g) On forfeiture of shares,______account is credited with the allotment money and/or calls money unpaid.

(h) If the premium amount has not been received, either wholly or partially, in respect of the shares forfeited,______Account will also be debited with the amount of ______ along with share capital account at the time of forfeiture.

True / False

1. Securities premium received on issue of shares cannot be used for the purpose of buy back of shares.
2. Maximum amount of discount allowed at the time of reissue of forfeited shares should not exceed the forfeited amount.
3. Minimum amount at which shares can be reissued is the amount received at the time of forfeiture of shares.
4. The options granted by the company to its employees and employee directors at a price that is lower than the market price is Employee Stock Option Plan.
5. A Company can issue and allot shares to a select group of people privately.
6. Calls-in-advance on shares is added to the amount of paid up share capital in the company's Balance Sheet.

Assertion Reason Solution

Que. No.	1	2	3	4	5
Ans.	D	A	C	A	C

MCQs Solution

Que. No.	1	2	3	4	5	6	7
Ans.	A	B	B	A	A	D	D
Que. No.	8	9	10	11	12	13	14
Ans.	B	A	B	D	C	B	C

Fill in the blanks Solution

Que. No.	(a)	(b)	(c)	(d)	(e)
Ans.	Reserve Capital	6000 shares	Unlimited	Forfeited	₹ 22
Que. No.	(f)	(g)	(h)		
	Called up	Calls-in-arrear	Securities Premium Reserve ; Premium not received		

True / False Solution

Que. No.	1	2	3	4	5	6
Ans.	False	True	False	True	True	False

CHAPTER 8

ISSUE OF DEBENTURES

Debentures	It is a document issued by a company under its common seal acknowledging the debt and it also contains the terms of repayment of debt and payment of interest at a specified rate.
TYPES OF DEBENTURES	
Secured Debentures	It refer to those debentures which are secured either by a fixed or floating charge on the assets of the company.
Unsecured Debentures	They are not secured by a charge on the assets of the company.
Redeemable Debentures	It refers to those debentures which are payable on the expiry of the specific period either in lump sum or in installments during the life time of the company.
I Irredeemable Debentures	It refers to those debentures that are not repayable during the life time of the company & hence are repaid only when the company is liquidated.
Convertible Debentures	It refers to those debentures which are convertible into equity shares or in any other security. They are either fully convertible or partly convertible.
Non-Convertible Debentures	It refers to those debentures which cannot be converted into shares or in any other securities.
Specific Coupon Rate Debentures	These debentures are issued with a specified rate of interest, which is called the coupon rate.
Zero Coupon Rate Debentures	These debentures do not carry a specific rate of interest. In order to compensate the investors, such debentures are issued at substantial discount.
Registered Debentures	Registered debentures are those debentures that are registered in the company's record in the name of the holder.
Bearer Debentures	Bearer debentures are the debentures that are not registered in the records of the company & can be transferred by mere delivery.

<table>
<tr><th colspan="2">ISSUE OF DEBENTURES</th></tr>
<tr><td>Issue of Debentures for Cash</td><td>Just like shares, debentures may be issued either at par or at a premium or at discount. The accounting entries are same as in case of issue of shares.</td></tr>
<tr><td>Issue of Debentures for Consideration other than cash</td><td>Issue of debentures to vendors as purchase consideration of assets/business purchased.
On purchase of Asset
Sundry Assets A/c Dr.
To Vendor's A/c (purchase consideration)
On issue of debentures at par
Vendor's A/c Dr.
To x% debentures A/c
On issue of debentures at premium
Vendor's A/c Dr.
To x% debentures A/c
To Securities Premium Reserve A/c
On issue of debentures at discount
Vendor's A/c Dr.
Discount on issue of debenture A/c
To x% debentures A/c
On purchase of Business
Sundry Assets A/c Dr.
To Sundry Liabilities A/c
To Vendor's A/c
If purchase consideration > net assets;
difference is debited to Goodwill &
If purchase consideration < net assets;
difference is credited to Capital Reserve</td></tr>
<tr><td>Issue of Debentures as Collateral Security</td><td>When the company issues debentures to lenders as an additional security in addition to the principal security, it is called issue of debentures as collateral security. No interest is paid on such debentures.
First method
No entry is made in the books of accounts since no liability is created. However, a note of this fact is given in the liability-side of Balance sheet.</td></tr>
</table>

	Second method Debentures Suspense A/c will appear in Balance Sheet as a deduction from debentures in notes to accounts of Long term Borrowings. Debenture Suspense A/c Dr. To x% Debentures A/c
TERMS OF ISSUE OF DEBENTURES	
Issued at par and redeemable at par	***For receipt of application money*** Bank A/c Dr. To Debenture Application & Allotment A/c ***For allotment of debentures*** Debenture Application & Allotment A/c Dr. To x% Debentures A/c
Issued at a discount and redeemable at par	*For receipt of application money* Bank A/c Dr. To Debenture Application & Allotment A/c ***For allotment of debentures at a discount*** Debenture Application & Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To x% Debentures A/c
Issued at premium and redeemable at par	***For receipt of application money*** Bank A/c Dr. To Debenture Application & Allotment A/c ***For allotment of debentures at a premium*** Debenture Application & Allotment A/c Dr. To x% Debentures A/c (with nominal value of deb.) To Securities Premium Reserve A/c (premium)
Issued at par and redeemable at a premium	***For receipt of application money*** Bank A/c Dr. To Debenture Application & Allotment A/c ***For allotment of debentures at par and redeemable at premium*** Debenture Application & Allotment A/c Dr. Loss on Issue of Debentures A/c (prem. on redem.) Dr. To x% Debentures A/c (nominal value of deb.) To Premium on Redemption of Debenture A/c

Issued at a discount and redeemable at a premium	***For receipt of application money*** Bank A/c Dr. To Debenture Application & Allotment A/c ***For allotment of debentures at a discount and redeemable at premium*** Debenture Application & Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. (with dis. on issue and prem. on redemption) To x% Debentures A/c (nominal value of deb.) To Premium on Redemption of Debentures A/c
Issued at a premium and redeemable at a premium	***For receipt of application money*** Bank A/c Dr. To Debenture Application & Allotment A/c ***For allotment of debentures at premium and redeemable at premium*** Debenture Application & Allotment A/c Dr. Loss on Issue of Debentures A/c (prem. on redem.) Dr. To Debentures A/c (nominal value of deb.) To Securities Premium Reserve A/c (prem. on issue) To Premium on Redemption of Debentures A/c
Writing-off Discount or Loss on Issue of Debentures (AS 16)	• *Discount or loss on issue of debentures is to be written off in the year debentures are allotted from Secuities Premium Reserve (if it exists) and then from Statement of Profit and Loss as Financial Cost.* Securities Premium Reserve A/c Dr. Statement of Profit and Loss Dr. To Discount or Loss on Issue of Debentures A/c
Interest on debentures	• *It is calculated at a fixed rate on its face value and is to be paid even when company is suffering from loss because it is charge against profit. Income Tax deducted from interest before payment to debenture holders is called T.D.S. (Tax deducted at source).* ***When interest is due*** Debenture Interest A/c Dr. To TDS Payable/Income Tax Payable A/c To Debentureholders A/c

	For payment of interest to debentureholders Debentureholders A/c Dr. To Bank A/c ***On payment of tax deducted at source to the Government*** TDS Payable/Income Tax Payable A/c Dr. To Bank A/c ***On transfer of Debenture Interest to Statement of Profit and Loss*** Statement of Profit and Loss To Debenture Interest A/c Dr.

Illustration 1. Rose Ltd. issued 10,000,10% debenture of ₹100 each at a premium of 10% , payable as follows – ₹10 on application, ₹30 on allotment (including premium), ₹30 on first call and ₹40 on second & final call.

Public applied for 12,000 debentures. Applications for 1,000 debentures were rejected & the application money was refunded. Debentures were allotted to the remaining applicants on pro-rata basis. Pass necessary journal entries for the issue of debentures.

Sol. **Journal**

Date	Particulars	LF	Dr. ( )	Cr. ( )
	Bank A/c Dr. To Debenture application A/c (Being the debenture application money received for 12,000 debenture ₹ 10 each)		1,20,000	 1,20,000
	Debenture Application A/c Dr. To 10% Debentures A/c To Debenture Allotment A/c To Bank A/c (Being 10,000 debentures allotted)		1,20,000	 1,00,000 10,000 10,000
	Debenture Allotment A/c Dr. To 10% Debenture A/c To Securities Premium Reserve A/c (Being the allotment money due on 10,000 debentures @ 20 + 10 each)		3,00,000	 2,00,000 1,00,000
	Bank A/c Dr. To Debenture Allotment A/c (Being the allotment money received)		3,00,000	 3,00,000

	Debenture First Call A/c Dr. To 10% Debenture A/c (Being the first call money due on 1,000 deb. @30 each)		3,00,000	3,00,000
	Bank A/c Dr. To Debenture First Call A/c (Being the first call money received)		3,00,000	3,00,000
	Debenture Second & Final Call A/c Dr. To 10% Debenture A/c (Being the second & final call money due on 1,000 deb. @ 40 each)		4,00,000	4,00,000
	Bank A/c To Debenture Second & Final Call A/c (Being the second & final call money received)		4,00,000	4,00,000

Illustration 2. ABC Ltd. issued ₹5, 00,000 10% debenture-of ₹100 each at 10% discount payable ₹30 on application and Balance on allotment. These debentures were to be redeemed at a premium of 5% after 5 year. All the debentures are subscribed for public.

Pass necessary journal entries for the issue of debentures.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
	Bank A/c Dr. To Debenture application A/c (Being the debenture application money receivable for 5,000 debenture ₹30 each)		1,50,000	1,50,000
	Debenture Application A/c Dr. To 10% Debentures A/c (Being 5000 debentures allotted)		1,50,000	1,50,000
	Debenture Allotment A/c Dr. Loss on issue of Debenture A/c Dr. To 10% Debenture A/c To Premium of redemption of Debentures A/c (Being the allotment money due on 5,000,10% Debenture issued at 10% discount and redeemable at 5% premium)		3,00,000 75,000	3,50,000 25,000
	Bank A/c Dr. To Debenture Allotment A/c (Being the allotment money received)		3,00,000	3,00,000

Illustration 3. Surya Ltd. took over assets of ₹20,00,000 & Liabilities of ₹7,60,000 of Anant Ltd. Surya Ltd. paid the purchase consideration by issuing 10,000, 9% Debentures of ₹100 each at a discount of 5% & accepting a bank draft of ₹2,00,000 payable after 3 months.

Pass necessary journal entries in the books of Surya Ltd. Also, Surya Ltd. writes off all capital losses in the first year itself. Also, Prepare Discount on Issue of Debentures A/c.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
(i)	Sundry Assets A/c Dr. To Sundry Liabilities A/c To Anant Ltd. To Capital Reserve A/c (Purchase of assets & labilities).		20,00,000	 7,60,000 11,50,000 90,000
(ii)	Anant Ltd. Dr. Discount on Issue of Debentures A/c Dr. To 9% Debentures A/c To Bills Payable A/c (Issue of 6,000 debentures at 5% discount & ₹2,00,000 draft payable after 3 months.)		11,50,000 50,000	 10,00,000 2,00,000
(iii)	Capital Reserve A/c Dr. To Discount on Issue of Debentures A/c (Discount on Issue of Debentures written off).		50,000	 50,000

Dr. **Discount on Issue of Debentures A/c** **Cr.**

Date	Particulars	₹	Date	Particulars	₹
	To 9% Debentures A/c	50,000		By Capital Reserve A/c	50,000
		50,000			50,000

Illustration 4. Neeraj Ltd. took over business of Ajay Enterprises on 01/04/2021. The details of the agreement rearding assets & liabilities to be taken over are:

Particulars	Book Value (₹)	Agreed Value (₹)
Building	20,00,000	35,00,000
Plant & Machinery	12,00,000	8,00,000
Stock	4,00,000	4,00,000
Trade Receivables	5,00,000	4,00,000
Creditors	2,00,000	3,00,000
Outstanding Expenses	50,000	1,00,000

It was decided to pay for purchase consideration as 7,00,000 through Cheque & balance by issue of 2,00,000, 9% Debentures of ₹20 each at a premium of 25%. Pass necessary journal entries

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
(i)	Building A/c Dr.		35,00,000	
	Plant & Machinery A/c Dr.		8,00,000	
	Stock A/c Dr.		4,00,000	
	Trade Receivables A/c Dr.		4,00,000	
	Goodwill A/c Dr.		10,00,000	
	To Creditors A/c			3,00,000
	To Outstanding Expenses A/c			1,00,000
	To Ajay Enterprises			57,00,000
	(Purchase of Assets & liabilities)			
(ii)	Ajay Enterprises Dr.		57,00,000	
	To Bank A/c Dr.			7,00,000
	To 9% Debentures A/c			40,00,000
	To Securities Premium Reserve A/c			10,00,000
	(Issue of 2,00,000 9% debentures @ 20 + 5 each)			

Illustration 5. Vedesh Ltd. purchased a running business of Vibhu Enterprises for a sum of ₹12,00,000. Vedesh Ltd. paid ₹60,000 by drawing a promissory note in favour of Vibhu Enterprises., ₹1,90,000 through bank draft and balance by issue of 8% debentures of ₹100 each at a discount of 5%. The assets and liabilities of Vibhu Enterprises consisted of Fixed Assets valued at ₹17,30,000 and Trade Payables at ₹3,20,000. You are required to pass necessary journal entries in the books of Vedesh Ltd.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
(i)	Fixed Assets A/c Dr.		17,30,000	
	To Trade Payables A/c			3,20,000
	To Vibhu Enterprises			12,00,000
	To Capital Reserve A/c			2,10,000
	(Purchase of assets & liabilities).			
(ii)	Vibhu Enterprises Dr.		12,00,000	
	Discount on Issue of Debentures A/c Dr.		50,000	
	To Bills Payable A/c			
	To Bank A/c			60,000
	To 8% Debentures A/c			1,90,000
	(Issue of bank draft, acceptance of bill & issue of 8% debentures in settlement of purchase consideration).			10,00,000

No. of Debentures issued = ₹9,50,000 / ₹95 = 10,000

Illustration 6. Zee Ltd. purchased machinery from King Ltd. Zee Ltd. paid King Ltd. as following:

(i) By issuing 5000, 12% debentures of ₹100 each at a premium of 30%.

(ii) Balance by giving a promissory note of ₹50,000 payable after two month.

Pass the necessary journal entries for the above transaction in the books of Zee ltd.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
	Machinery A/c Dr. To King Ltd. (Being the machinery purchased from king Ltd.)		2,03,000	 2,03,000
	King Ltd Dr. To 12% Debentures A/c To Securities Premium Reserve A/c (Being 5,000 12% debentures issued@ 100 + 30 each).		6,50,000	 5,00,000 1,50,000
	King Ltd. Dr. To Bill Payable A/c (Debentures issued to Vendors at a discount of 10%)		50,000	 50,000

Calculation of Purchase Consideration

(i) 5,000 12% debentures @ 130 = ₹6,50,000

(ii) Promissory Note = ₹50,000

₹7,00,000

Illustration 7. Pass Journal entries to record the following transaction:

(i) 120 , 8% debentures of ₹1000 each are issued at 5% discount & repayable at par.

(ii) 150, 7% debentures of ₹1000 each are issued at 5% discount & repayable at premium of 10%.

(iii) 700 , 9% debentures of ₹1000 each are issued at 5% premium & repayable at premium of 10%.

Date	Particulars	LF	Dr. ( )	Cr. ( )
	Bank A/c Dr. To 8% Debenture Application & Allotment A/c (Being the debenture application money received)		1,14,000	 1,14,000

	8% Debenture Application & Allotment A/c Dr. Discount on Issue of Debentures A/c Dr. To 8% Debentures A/c (Being debentures application money transferred to debentures A/c)		1,14,000 6,000	 1,20,000

Sol: (ii)

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
	Bank A/c Dr. To Debenture Application & Allotment A/c (Being the debenture application money received)		1,42,500	 1,42,500
	Debenture Application and Allotement A/c Dr. Loss on Issue of Debentures of A/c Dr. To 7% Debenture A/c To Premium on redemption of Debentures A/c (Being debentures application money transfered to debentures A/c)		1,42,500 22,500	 1,50,000 15,000

Sol: (iii)

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
	Bank A/c Dr. To Debenture Application & Allotment A/c (Being the debenture application money received)		7,35,000	 7,35,000
	Debenture Application & Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 9% Debentures A/c To Securities Premium Reserve A/c To Premium on Redemption of Debentures A/c (Being debentures application money transferred to debentures A/c)		7,35,000 70,000	 7,00,000 35,000 70,000

Illustration 8. Give necessary journal entries assuming that company write off all its capital losses in the year in which it occurs-

Vinod Ltd. took over running business with assets of ₹6,00,000 and liabilities of ₹60,000 from Fukrey Ltd for the purchase consideration of ₹ 5,70,000. It paid the purchase consideration by issuing 8% debentures of ₹100 each at 5% discount. repayable after 5 years at a premium of 10%.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
	Assets A/c Dr. Goodwill A/c Dr. To Liabilities A/c To Fukrey Ltd. (Being Purchase of assets & Liabilities)		6,00,000 30,000	 60,000 5,70,000

	Fukrey Ltd. Dr. Loss on Issue of Debentures A/c Dr. To 8% Debentures A/c To Premium on Redemption of Debentures A/c (Being 8% debentures of ₹100 each at 5% discount, repayable at a premium of 10% issued as purchase consideration)		5,70,000 90,000	6,00,000 60,000
	Statement of P&L A/c Dr. To Loss on Issue of Debentures A/c (Being discount on issue of debentures written off).		90,000	90,000

No. of Debentures issued = ₹ 5,70,000/ ₹ 95 = 6,000

Illustration 9. Raghuveer Ltd. issued ₹ 10,000, 8% debentures of ₹ 100 each at a premium of 10 % on 1st April 2021. It purchased fixed assets of the value of ₹ 2,50,000 and took over current liabilities of ₹ 40,000 and issued 8% debentures at a premium of 5% to the vendor. On the same date it took loan from the Bank for ₹ 1,00,000 and issued 8% debentures as collateral security

Pass necessary Journal entries in the books of Raghuveer Ltd. & Prepare the extract of balance sheet on 31/03/2022. Ignore Interest.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
1st April 2021	Bank A/c Dr. To Debentures Application & Allotment A/c (Application money received for 10,000, 8% debentures @ 110 each).		11,00,000	11,00,000
1st April 2021	Debentures Application & Allotment Dr. To 8% Debentures A/c To Securities Premium Reserve A/c (Application money transferred to Debentures & Securities Premium Reserve A/c		11,00,000	10,00,000 1,00,000
1st April 2021	Fixed Assets A/c Dr. To Current Liabilities A/c To Vendor's A/c (Purchase of Assets & Liabilities).		2,50,000	40,000 2,10,000
1st April 2021	Vendor's A/c Dr. To 8% Debentures A/c To Securities Premium Reserve A/c (Issue of 2,000 debentures of ₹100 each at 5% premium i.e. 2,10,000/105 = 2,000 deb).		2,10,000	2,00,000 10,000

1st April 2021	Bank A/c Dr. To Bank Loan A/c (Loan taken, secured by issue of ₹1,00,000 deb).		1,00,000	 1,00,000
1st April 2021	8% Debentures Suspense A/c Dr. To 8% Debentures A/c (Issue of debentures as collateral security).		1,00,000	 1,00,000

Balance Sheet Extract as at 31/03/2022

Particulars	Note No.	Current y (₹)
I. Equity& Liabilities :		
Shareholder's Funds:		
Reserve & Surplus	1	1,10,000
Non – Current Liabilities:		
Long term borrowings	2	13,00,000
Current Liabilities:	3	40,000
II. Assets		
Non - Current Assets	4	2,50,000
Fixed Assets		

Illustration 10: S. Singh Limited obtained a loan of ₹ 5,00,000 from State Bank of India @ 10 % Interest. The company issued ₹ 7, 50,000,10 % debentures of ₹ 100/- each, in favor of State Bank of India as collateral security. Pass necessary journal entries for the above transactions:

i. When company decided to record the issue of 10 % Debentures as collateral security.

ii. When company decided not to record the issue of 10 % Debentures as collateral security.

Also show, how the Debentures & Bank Loan will appear in the Company's Balance Sheet as at 31st March 2022.

Sol. **Journal**

(i)

Date	Particulars	LF	Dr. ( )	Cr. ( )
	Bank Account Dr. To Bank Loan Account (Being loan obtained from State Bank of India @ 10 % p.a. interest, against collateral security of 7,500 10 % debentures of ₹ 100 each)		5,00,000	 5,00,000

	Debenture Suspense Account Dr. 10% Debentures Account (Being 10 % Debentures issued as collateral security in favour of State Bank of India)		7,50,000	7,50,000

Balance Sheet Extract as at 31/03/2022

Particulars	Note No.	Amount (₹)
I. Equity& Liabilities :		
Non – Current Liabilities:		
Long term borrowings	1	5,00,000

Notes to Accounts:

Particulars	Details	Amount (₹)
I. Long term borrowings		
Loan from SBI		5,00,000
7,500 ,10% Debentures of ₹100 each	7,50,000	
Less: Suspense A/c Debenture	(7,50,000)	—
		5,00,000

Sol. (ii)

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
	Bank Account Dr. To Bank Loan Account (Being loan obtained from State Bank of India @ 10 % p.a. interest, against collateral security of 7,500 10 % debentures of ₹ 100 each)		5,00,000	5,00,000

Balance Sheet Extract as at 31/03/2022

Particulars	Note No.	Amount (₹)
II. Equity& Liabilities :		
Non – Current Liabilities:		
Long term borrowings	1	5,00,000

Notes to Accounts:

Particulars	Details	Amount (₹)
II. Long term borrowings		
Loan from SBI		5,00,000
(Secured by issue of 7,500 debentures of ₹100 each as collacteral security)		

Illustration 11. On 1.04.2021, B.G. Ltd. issued 2,000, 9% debentures of ₹100 each at a discount of 6%, redeemable at a premium of 5% after 2 years. According to the terms of issue, interest on debentures is payable half yearly on 30th September and 31st March. Pass necessary journal entries for the year ended 31/03/2022.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
1st April 2021	Bank A/c Dr. To Debentures Application & Allotment A/c (Application money received for 2,000, 9% debentures @ 94 each).		1,88,000	 1,88,000
1st April 2021	Debentures Application & Allotment Dr. Loss on Issue of Debentures A/c Dr. To 9% Debentures A/c To Premium on Redemption of Debentures A/c (Issue of debentures at 6% discount redeemable at 5% premium).		1,88,000 22,000	 2,00,000 10,000
30th Sep. 2021	Interest on Debentures A/c Dr. To Debenture holder's A/c (Half yearly interest due on debentures)		9,000	 9,000
30th Sep. 2021	Debenture holder's A/c Dr. To Bank A/c (Payment of Interest)		9,000	 9,000
31st Mar. 2021	Interest on Debentures A/c Dr. To Debenture holder's A/c Half yearly interest due on debentures)		9,000	 9,000
31st Mar. 2021	Debenture holder's A/c Dr. To Bank A/c (Payment of Interest)		9,000	 9,000
30th Sep. 2021	Statement of Profit & Loss A/c Dr. To Loss of Issue of Debentures A/c To interest on Debentures A/c (Loss on Issue & Interest transferred to Statement of P/L)		40,000	 22,000 18,000

Illustration 12. X Ltd. issued ₹10,00,00, 8% debentures at as discount of 10 % on 1st April 2018, redeemable in 4 equal annual instalments starting form 31st March 2019.

Pass necessary Journal entries for issue of Debentures & to Write off Discount on issue of debentures if-

(a) There is no Securities Premium Reserve Balance

(b) The Securities Premium Reserve A/c shows a balance of 30,000.

(c) The Securities Premium Reserve A/c shows a balance of 1,50,000.

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
1st April 2018	Bank A/c Dr. To Debentures Application & Allotment A/c (Application for ₹10 lakh, 8% debentures @ 10% discounts received).		9,00,000	9,00,000
1st April 2018	Debentures Application & Allotment Dr. Discount on Issue of Debentures A/c To 8% Debentures A/c (Application money transferred to Debentures A/c)		9,00,000 1,00,000	10,00,000
	Case (a) There is no Securities Premium Reserve Balance			
31 March 2019	Statement of Profit & Loss A/c Dr. To discount on Issue of Debentures A/c (Being discount on Issue of debentures written off)		1,00,000	1,00,000
	Case (b) The Securities Premium Reserve A/c Shows a balance of 1 30,000			
31 March 2019	Securities Premium Reserve A/c Dr. Statement of Profit & Loss A/c Dr. To Discount on Issue of Debentures A/c (Being discount on issue of Debentures written off)		30,000 70,000	1,00,000
	Case (c) The Securities Premium Reserve Ac/ Shows a balance of ₹ l, 50,000			
31 March 2019	Securities Premium Reserve A/c Dr. To Discount on Issue of Debentures A/c (Being discount on issue of Debentures written off)		1,00,000	1,00,000

Illustration 13: On April 1, 2021 Z Ltd. issued, 10,000, 8% Debentures of ₹100 each at premium of 5%, to be redeemable at a premium of 10%, after 5 years. The entire amount was payable on application. The issue was oversubscribed to the extent of 10,000 debentures and the allotment was made proportionately to all the applicants. The securities premium amount has not been utilized for any other purpose during the year.

Give journal entries for the issue of debentures and writing off loss on issue of debentures. Also, Prepare Loss on Issue of Debenetures A/c

Sol. **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
2021 April 01	Bank A/c To Debenture Application and Allotment A/c (Being application money received on 20,000 8% debentures @ 105 each).		21,00,000	 21,00,000
01 April 2021	Debentures Application & Allotment Dr. Loss on Issue of Debentures A/c Dr. To 8% Debentures A/c To Securities Premium Reserve A/c To Premium on Redemption of Debentures A/c To Bank A/c (Application money transferred to Debentures & Securities Premium Reserve A/c & balance refunded).		21,00,000 1,00,000	 10,00,000 50,000 1,00,000 10,50,000
2022 Mar-31	Securities Premium Reserve A/c Dr. Statement of Profit and Loss A/c Dr. To Loss on Issue of Debentures A/c (Being loss on Issue of Debentures written off)		50,000 50,000	 1,00,000

Dr. **Loss on Issue of Debentures A/c** **Cr.**

Date	Particulars	₹	Date	Particulars	₹
1st Apr. 2021	To Premium on Redemption of Debentures A/c	1,00,000	31st Mar. 2022	By Sec. Prem. Rserve A/c By Statement of P& L A/c	50,000 50,000
		1,00,000			1,00,000

Illustration 14. Yogadatra Ltd. (pharmaceutical company) appointed marketing expert, Mr. Kartikay as the CEO of the company, with a target to penetrate their roots in the rural regions. Mr. kartikay discussed the ways and means to achieve target of the company with financial, production and marketing departmental heads and asked the finance manager to prepare the budget. After reviewing the suggestions given by all the departmental heads, the finance manager proposed requirement of an additional fund of ₹52,50,000.

Yogadatra Ltd. is a zero-debt company. To avail the benefits of financial leverage, the finance manager proposed to include debt in the capital structure. After deliberations, on 1st April, 2020, the board of directors had decided to issue 6% Debentures of ₹100 each to the public at a premium of 5%, redeemable after 5 years at ₹ 110 per share.

You are required to answer the following questions:

(i) Calculate the number of debentures to be issued to raise additional funds.

(ii) Pass Journal entry for the allotment of debentures.

(iii) Pass Journal entry to write off loss on issue of debentures.

(iv) Calculate the amount of annual fixed obligation associated with debentures.

(v) Prepare loss on Issues of Debentures Account.

Sol. (i) Number of debentures to be issued = ₹ 52,50,00/ ₹105 = 50,000

(ii) **Journal**

Date	Particulars	LF	Dr. ( )	Cr. ( )
1st Apr. 2020	Debentures Application & Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 6% Debentures A/c To Securities Premium Reserve A/c To Premium on Redemption of Debentures A/c (Being allotment of debentures made)		52,50,000 5,00,000	 50,00,000 2,50,000 5,00,000

Sol: (iii) **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
31st Mar. 2021	Securities Premium Reserve A/c Dr. Statement of Profit & Loss A/c Dr. To Loss on Issue of Debentures A/c (Being Loss on issue of debentures A/c written off)		2,50,000 2,50,000	 5,00,000

(iv) Interest on 6% Debentures = ₹ 50,00,000 × 6% ₹ 3,00,000

Sol: (v)

Date	**Particulars**	**Amount (₹)**	**Date**	**Particulars**	**Amount (₹)**
1st April 2020	To Premium on Redemption of Debentures A/c	5,00,000	31th Mar. 2021	By Sec. Prem. Reserve A/c By Statement of P& L A/c	2,50,000 2,50,000
		5,00,000			5,00,000

Illustration 15: Mohan & Co. is a leading pharmaceutical company dealing with variety of medications for patients. They believe in rigorous R&D before going ahead with processing of the cure for any disease. When the pandemic hit in 2020, they also started their research for vaccination development & mass production but for this purpose huge investment is need. So, the directors decided to issue, 10,000, 11% Debentures of ₹100 each at a premium of 10% on 1st April 2020. It Purchased Sundry

Assets of the value of ₹2,50,000 & took over the liabilities of ₹60,000& issued 11% Debentures of ₹100 each at a discount of 5% to the vendor.

Answer the following questions on the basis of above information:

a. How much amount is received from issue of debentures for cash?

b. State the amount credited to Securities Premium Reserve Account.

c. How many debentures are issued to the vendors against the purchase of Sundry Assets?

d. State the amount debited to "Discount on issue of 11% Debentures".

e. Pass the necessary journal entry to write off the Discount on Issue of Debentures Account?

Sol.

a. ₹11,00,000 is received from issue of debentures for cash

(10,000 11% debentures @ ₹110 each)

b. ₹1,00,000 is credited to Securities Premium Reserve Account

(10,000 11% debentures @ ₹10 each)

c. 2,000 debentures are issued to the vendors against the purchase of Sundry Assets, i.e. ₹1,90,000 / ₹95

d. ₹ 10,000 is debited to Discount on issue of 11% Debentures A/c

(2,000 debentures @ ₹ 5 each)

(e) Journal

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
	Securities Premium Reserve A/c Dr. To Discount on Issue of Debentures A/c (Being Discount on issue of debentures A/c written off out of securities premium reserve account)		10,000	 10,000

Illustration 16. Surat Textiles Ltd. was in need of additional funds of ₹38,00,000. On 1 October 2021, it decided to raise this amount by the issue of 6% debentures of ₹100 each the public at a discount of 5%, redeemable after 6 years at a premium of 8%. Company closes its books on 31st March every year.

You are required to-

(i) Pass journal entry for the allotment of debentures.

(ii) Pass journal entries for payment of interest on debentures.

(iii) Pass journal entry for closing the interest on debentures account.

(iv) Pass journal entry to write off "Loss on Issue of Debentures Account". You are informed that company has a balance of ₹ 2,50,000 in its Capital Reserve.

Solu (i) **Journal**

Date	Particulars	LF	Dr. ( )	Cr. ( )
1st Oct. 2021	Debentures Application & Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 6% Debentures A/c To Premium on Redemption of Debentures A/c ((Being allotment of 40,000 debentures made))		38,00,000 5,20,000	 40,00,000 3,20,000

Sol: (ii) **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
31st Mar. 2022	Debentures Interest A/c Dr. To Debenture holders A/c (Interest due on debentures for half year)		1,20,000	 1,20,000
31th Mar. 2022	Debenture holders A/c Dr. To Bank A/c (Payment of Interest)		1,20,000	 1,20,000

Sol: (iii) **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
31th Mar. 2022	Statement of Profit & Loss A/c Dr. To Debentures Interest A/c (Debentures Interest transferred to Statement of Profit & Loss A/c)		1,20,000	 1,20,000

Sol: (iv) **Journal**

Date	Particulars	LF	Dr. (₹)	Cr. (₹)
31th Mar. 2022	Capital Reserve A/c Dr. Statement of Profit & Loss A/c Dr. To Loss on Issue of Debentures A/c (Being Loss on issue of debentures A/c written off from Capital reserve & Statement of Profit & Loss)		2,50,000 2,70,000	 5,20,000

PRACTICE QUESTIONS

Que. 1) X Ltd. invited application for issuing 1000, 9% debentures of ₹100 each at a discount of 6%. Applications for 1,200 debentures were received. Pro-rata allotment was made to all the applicants. Pass necessary journal entries for the issue of debenture assuming that the whole amount was payable with application.

Que. 2) Zed Ltd. issued 2,00,000, 8% debentures of ₹ 100 each at a discount of 6% redeemable at a premium of 10% after 5 years. The amount was payable as follows:

On application – ₹ 50 per debenture and On allotment – balance Record the necessary entries for the issue of debentures in the books of Zed Ltd.

Que. 3) On 1st April, 2019, Bright Ltd. issued ₹ 4,00,000, 6% Debentures of ₹100 each at a discount of 5%, redeemable after three years.

The amount per debenture was payable as follows :

On Application - ₹ 80 per debenture

On Allotment - Balance

The debentures were fully subscribed and all money was duly received. Pass necessary journal entries for issue of debentures.

Que. 4) BGP Ltd. invited applications for issuing 15,000,11% debentures of ₹ 100 each at a premium of ₹ 50 per debenture. The full amount was payable on application. Applications were received for 25,000 debentures. Applications for 5,000 debentures were rejected and the application money was refunded. Debentures were allotted to the remaining applicants on pro-rata basis. Pass the necessary journal entries for the above transactions in the books of BGP Ltd.

Que. 5) On 1st April, 2018, Sakshi Ltd. issued 1,000, 11% Debentures of ₹100 each at a discount of 6%, redeemable at a premium of 5% after three years. Pass the necessary journal entries for the issue of debentures in the books of Sakshi Ltd.

Que. 6) B Ltd. purchased assets of the book value ₹4, 00,000 and took over the liability of ₹ 50,000 from Mohan Bros. It was agreed that the purchase consideration, settled at 3. 80,000, be paid by issuing 8% debentures Pass necessary journal entries if debentures are issued at 10% discount & balance is paid in cash.

(Hint: Goodwill- ₹ 30,000; No of Deb = 4,222; Bank ₹ 20)

Que. 7) Deepak Ltd purchased furniture of 2,20,000 from M/s Furniture Mart. 50% of the amount was paid to Furniture Mart by accepting a bill of exchange & for the balance the company issued 9% debentures of ₹100 each at a premium of 10% in favor of Furniture Mart. Pass necessary journal entries in the books of Deepak Ltd. for the above transactions

(Hint: Bills Payable- ₹ 1,10,000: Securities Premium Reserve– ₹10,000)

Que 8) Disha Ltd. took over assets of ₹ 8,00,000 and liabilities of ₹ 3,00,000 from Kriti Ltd. for a purchase consideration of ₹ 6,00,000. The payment was made by issue of 9% Debentures of ₹100 each at 20% premium Pass the necessary journal entries for the above transactions in the books of Disha Ltd.

(Hint: Goodwill- ₹1,00,000, No. of Deb 5,000: SPR-₹1,00,000)

Que 9) Vayce Ltd. purchased the following assets of EX. Ltd.: Land and Building of ₹60,00,000 at ₹84,00,000; Plant and Machinery of ₹ 40,00,000 at ₹ 36,00,000. The purchase consideration was ₹1,10,00,000. Payment was made by accepting a Bill of Exchange in favour of EX. Ltd. of ₹ 20,00,000 and remaining by issue of 8% debentures of ₹100 each at a premium of 20%. Record the necessary journal entries for the above transactions in the books of Vayee Ltd.

(Hint: Capital Reserve- ₹10,00,000; No. of Deb. ₹75.000, SPR– ₹15,00,000)

Que. 10) Pass the necessary journal entries for the issue of debentures for the following transactions:

(a) Anand Ltd. issued 800, 9% Debentures of ₹500 each at a premium of 20%, to the vendors for machinery purchased from them costing ₹4,80,000.

(b) Dawar Ltd. issued 5,000, 7% Debentures of ₹200 each at a premium of 5%, redeemable at a premium of 10%.

(c) Novelty Ltd. issued 1,000, 8% Debentures of ₹100 each at a discount of 5%, redeemable at a premium of 10%

Que. 11) Pass journal entries

(a) Mayur Ltd., issued 5,000, 12% Debentures of ₹100 each. The debentures are issued at a discount @ 10% and redeemable at premium @ 5%.

(b) A Ltd issued 6,000, 12% debentures of ₹100 each. The debentures are issued to a supplier of machine costing ₹5,50,000.

(c) J Ltd., took a loan of ₹5,30,000 the Bank of India for which the company placed with the bank, debenture ₹6,00,000 as collateral security.

(**Hint:** (a) Premium on red. Of deh. - ₹25000, Loss on issue of deb. - ₹50000

(b) Discount on issue of deb. - ₹50000

(c) Bank Loan - ₹5.30,000; Deb. Suspense A/c- ₹6,00,000)

Que. 12) Youth Ltd. took a loan of ₹15,00,000 from State Bank of India against the security of tangible assets. In addition to principal security, it issued 10,000 11% debentures of ₹100 each as collateral security. Pass necessary journal entries for the above transactions, if the company decided to record the issue of 11% debentures as collateral security and show the presentation in the Balance Sheet of Youth Ltd.

Que. 13) R Ltd. issued 1,000, 16% Debentures of ₹100 each on 1st January 2018 Interest on these debentures is paid half yearly, ie, on 30th June and 31st December. Pass the necessary journal entry for the period.

(**Hint:** Interest on debentures- ₹25000; Statement of P&L A/c debited by - ₹50000)

Que 14) On 1-4-2015 ABC Ltd. issued 750, 11% debentures of ₹ 100 each at a discount of 5% redeemable at a premium of 10% after three years, interest on debentures is payable on 30th September and 31st march. ABC Ltd closes its books on 31st march every year. Pass necessary entries for the issue of debenture and the payment of interest for the year ended 31st March 2016.

Que. 15) Agam Ltd issued 40,000 9% debentures of ₹ 100 each on April 1, 2018 at a discount of 10%, redeemable at a premium of 10%. Assuming that the interest was paid half yearly on September 30 and March 31, give journal entries relating to debenture interest for the half year ended March 31, 2019.

Que 16) A Ltd issued 10,000, 8% Debentures If ₹100 each at par on 1st April 2018 redeemable at a premium of 5 % after 3 year. Pass necessary journal entries for issue of debentures & to write off loss on Issue of Debentures if

(a) There is no balance in Securities Premium Reserve A/e

(b) The Securities Premium Reserve A/c Showed a balance of ₹10,000.

(c) The Securities Premium Reserve A/c Showed a balance of ₹80,000.

MCQs

1. At the time of issue of debentures, debentures account is:

   A) Credited by the amount Received

   B) Credited by the issue price of the debentures

   C) Credited by nominal value of the debenture

   D) none of the above

2. Return on debenture is called:

   A) Interest B) Dividend

   C) A & B both D) None of the above

3. Perpetual Debenture is the other name of:

   A) Convertible debentures B) Irredeemable debenture

   C) Naked debenture D) None of the above

4. In case of debenture of ₹ 10,000 are issued at par but redeemable at a premium of 10%, the premium payable is debited to :

   A) Debenture suspense account

   B) Premium on redemption of debentures

   C) Loss on issue of debentures

   D) A & B both

5. Debenture holder account are:

   (A) Personal B) Real

   C) Nominal D) None of the above

6. X Ltd has purchased the building and debentures are issued at discount which account will be debited for discount:

   A) Discount on issue of Debentures

   B) Loss on issue of debenture

   C) Both of A & B

   D) None of the above

7. Debentures are shown in the balance sheet of the company under the head of;

A) Non-current liabilities | B) Current liability
C) Share capital | D) None of the these

8. Discount or loss of issue of debenture to be written off after 12 months from the date of balance sheet or after the period of operating cycle in shown as:

A) Other current assets | B) Other noncurrent assets
C) Other long term liability | D) Other current liabilities

9. ABC Ltd Purchase a machinery worth ₹1,98,000.The payment made by issue of debenture of ₹ 100 each at 10% Discount in this case no. of debenture will be:

A) 1100 | B) 2200
C) 3300 | D) 4400

10. Which of the following do not have voting right in the company?

A) Debenture holders | B) Shareholders
C) Both A & B | D) None of these

11. When 100 debenture issued at 5% discount ₹100 each but redeemable at premium of 8%. How much amount will be credited as premium on redemption of debentures account:

A) 5000 | B) 4000
C) 8000 | D) 6000

12. A Ltd took over Assets of ₹ 5,00,000 and liability of ₹ 50,000 from B Ltd in the agreed consideration of ₹ 4,80,000 and Issued Debentures of ₹100 each at the premium of ₹ 20. Number of Debenture issued are:

A) 48,000 | B) 40,000
C) 4,000 | D) 4,800

13. A company issued 1000 7% Debentures of ₹ 100 at 5% Discount and repayable at 10% Premium. What will be the amount of Loss on issue of Debentures?

(a) ₹ 10,000 | B) ₹ 20,000
(c) ₹ 15,000 | D) ₹ 30,000.

14. A Company issued 1000 7% Debentures of ₹ 100 each at 5% Premium and repayable at 10% Premium. What will be the amount of Loss on issue of Debentures:

A) ₹ 5,000 | B) ₹ 10,000
C) ₹ 5,000 | D) ₹ 20,000.

15. A company redeem 1,000 6% Debentures of ₹ 100 each at 10% Discount and repayable at 10 % Premium. Interest on Debentures are payable half yearly on

which tax deducted at source of 10% p.a. What will the amount of tax deduction of a year :

A) ₹ 3,000 B) ₹ 4,000

C) ₹ 5-000 D) ₹ 6,000

True /False

1. Debentures can be redeemed at premium
2. Unsecure debentures can be issued in India
3. A debenture holders is the owner of the company
4. A debenture is written instrument acknowledging a debt

FILL IN THE BLANKS

1. Debenture holder are the _______ of the company.
2. A collateral security is a _______ security besides the primary security when a company obtains a loan from a Bank or any other financial institution.
3. Interest on debenture is charge against _______ and is to be paid even if there is no profit in the company.
4. A debenture is said to be issued at a discount when the issue value is_______ than its nominal value.
5. Debentures are issued as other than cash, number of debentures will be calculated as purchase price dividing by _______.
6. Discount on issue of debenture is _______ loss of the company.
7. Interest payable on Debenture is calculated at the _______value of debentures.
8. Security premium reserve A/c is shown _______ side of the balance sheet under the head _______.
9. When debentures issued at par and redeemable at premium, loss on issue of debentures A/c will be _______.
10. A company issued 100 debentures@ ₹ 100 each at par redeemable at 5% premium ₹ _______will be debited to loss on issue of debenture A/c.
11. A company issued 500 debenture @ ₹ 100 each at 5% discount and redeemable at 7% premium ₹ _______will be credited as premium on redemption of debenture A/c.
12. A company took a Bank loan of ₹ 10,00,000 byissue of 10,00,000 6% Debenture as collateral security_______amount will be shown in non-current liabilities in the balance sheet.

MCQs Solution

Que. No.	1	2	3	4	5
Ans	C	A	B	B	A

Que. No.	6	7	8	9	10
Ans	A	A	C	B	A
Que. No.	11	12	13	14	15
Ans	C	A	C	B	D

True /False Solution

Que. No.	1	2	3	4
Ans	T	F	F	T

Fill in the blanks Solution

Que. No.	1	2	3	4
Ans	Creditors	Secondary	Profit	Less
Que. No.	5	6	7	8
Ans	Issue price	Capital	Nominal/ face value	Liabilities; Reserve & surplus
Que. No.	9	10	11	12
Ans	Debited	₹ 5,000	₹ 7,000	₹ 1,00,0000

PART-B
CHAPTER-1

FINANCIAL STATEMENTS OF A COMPANY

Financial Statement

Financial Statements are the end products of accounting process and are prepared at the end of the accounting period **to reveal the financial position** of the enterprise at a particular date and **the result of its business operations during an accounting period.**

As per Section 2(40) of the Companies Act, 2013 Financial Statements include :

1. Balance Sheet or Position Statement
2. Statement of Profit and Loss or Income Statement
3. Note to Accounts.
4. Cash Flow Statement.

Balance Sheet : It is a statement of assets, liabilities and Equities of a business and it is prepared to show the financial position of the company at a particular date.

A balance sheet of a company is prepared as per the format prescribed in Part I of Schedule III of the Companies Act, 2013.

The Schedule III prescribes only the vertical format for presentation of financial statements. Thus, a company will now not have an option to use horizontal format for the presentation of financial statements.

Important contents of Balance Sheet

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

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

Equity is the residual interest in the assets of the enterprise after deducting all its liabilities.

Part-I - Form of Balance Sheet

(₹ in-----)

Particulars	Note No	Figures as at the end of current reporting period	Figures as at the end of the previous reporting period
1	2	3	4
I. EQUITY AND LIABILITIES			
(1) Shareholders' funds			
(a) Share capital			
(b) Reserves and surplus			
(c) Money received against share warrants			
(2) Share application money pending allotment			
(3) Non-current liabilities			
(a) Long-term borrowings			
(b) Deferred tax liabilities (Net)			
(c) Other Long term liabilities			
(d) Long-term provisions			
(4) Current liabilities			
(a) Short-term borrowings			
(b) Trade payables			
(c) Other current liabilities			
(d) Short-term provisions			
TOTAL			

I. ASSETS		
(i) Non-current assets		
(a) Property plant and equipment and Intangible Assets		
(i) Property plant and equipment		
(ii) Property plant and equipment		
(iii) Intangible assets		
(iv) Capital work-in- progress		
(v) Intangible assets under development		
(b) Non-current investment		
(c) Deferred tax assets (net)		
(d) Long-term loans and advances		
(e) other non-current assets		
(2) Current Assets		
(a) current investments		
(b) Inventories		
(c) Trade receivables		
(d) Cash and cash equivalents		
(e) Short term loans and advances		
(f) other current assets		
TOTAL		

Illustration 1: C Ltd. has an opening credit balance of ₹ 2, 50,000 in Securities Premium Reserve and also debit balance of ₹ 5,00,000 in Surplus i.e., Balance in statement of Profit and Loss in Reserve and Surplus. During the year ended 31st march, 2016, it incurred a loss of ₹ 3,00,000. Prepare Notes to Account on Reserve and Surplus showing the amount to be shown in Balance Sheet.

Solution:

Note to Accounts

Particulars		₹
Reserve and Surplus		
(a) Securities Premium Reserve		2,50,000
(b) Surplus i.e., Balance in statement of Profit & Loss		
Opening Balance	(5,00,000)	(8,00,000)
Add- Loss for the year	(3,00,000)	(5,50,000)

₹ (5,50,000) will be shown against Reserve and Surplus under shareholders' funds in the Balance Sheet.

Statement of Profit and Loss

Statement of Profit and Loss: It is a statement prepared to show the result of business operations during an accounting period.

It shows the operating performance of a company during the accounting period.

A Statement of Profit & Loss of a Company is prepared as per the format prescribed in Part II of Schedule III of the Companies Act, 2013.

PART II - FORM OF STATEMENT OF PROFIT AND LOSS

Statement of Profit & Loss

For the year ended ....

(₹ in ....)

Particulars	Note No.	Figures for the current reporting period	Figures for the Previous reporting period
I. Revenue from operations		....	....
II. Other Income		....	....
III. Total Revenue (I+II)		....	....
IV. Expenses:			
• Cost of Material consumed			
• Purchases of Stock-in-Trade			
• Changes in Inventories of Finished Goods, work-in-progress and stock-in-trade			
• Employees Benefit Expenses			
• Finance Cost			
• Depreciation & Amortisation Expenses		....	
• Other Expenses		....	....
Total Expenses			....
V. Profit before Tax (III—IV)		....	....
VI. Less: Tax		....	....
		(.....................)	(.....................)
VII. Profit after Tax (V—VI)		....	....

BALANCE SHEET (Companies Act 2013 Schedule III Part 1)				
B/s Heading	**Major Heading**	**Sub Heading**	**Sub Sub Heading**	**Treatment if any**
Equity and Liabilities	**1. Shareholders Fund**	**a. Share Capital**	• Authorised Capital • Issued Capital • Subscribed Capital	
			• Calls in Arrear	In Note to Accounts on share capital under subscribed capital as deduction
			• Share Forfeited Account	In note to Accounts on share capital under subscribed capital as addition
Equity and Liabilities	**1. Shareholders Fund**	**b. Reserves and Surplus**	• Capital Reserve • Securities Premium Reserve • Debenture Redemption Reserve • Capital Redemption **Reserve** • General Reserve • Sinking fund • Revaluation Reserve • Share Option Outsanding A/c • Surplus (or Retained earnings or Accumulated Profits) *Note: -* • *This Surplus has to be after transfer to Reserves and Proposed dividend.* • *Surplus can be a Negative figure.*	

Equity and Liabilities	**1. Shareholders Fund**	c. **Money Received Against Share Warrants**	*Share Warrants are issued to promoters for preferential issue. This instrument gives the holder the right to acquire equity shares. Money is already allocated at the time of issue of warrants.*	
Equity and Liabilities	**2. Share Application Money Pending Allotment**			
Equity and Liabilities	**3. Non-Current Liabilities**	**a. Long Term Borrowing**	• Debentures • Bonds • Loans from banks • Loan from other parties • Deposits (Public Deposits, Fixed Deposits) *Note: -* *1. They should be classified as secured and unsecured* 2. *Borrowing which is due for*	

			payment within 12 months is to be treated as Other Current Liabilities
Equity and Liabilities	**3. Non-Current Liabilities**	**b. Deferred Tax Liabilities**	
Equity and Liabilities	**3. Non-Current Liabilities**	**c. Other Long Term Liabilities**	• Trade Payables if settled after (12 months) • Premium Payable on Redemption of Debentures • Premium Payable on Redemption of Preference Share
Equity and Liabilities	**3. Non-Current Liabilities**	**d. Long Term Provisions**	• Provision for employees retirement benefits. i.e. amount of earned leave etc. • Provision for Warranty Claims
Equity and Liabilities	**4. Current Liabilities**	**a. Short Term Borrowings**	• Loans from bank • Loans from other parties • Deposits (Public Deposits, Fixed Deposits)
Equity and Liabilities	**4. Current Liabilities**	**b. Trade Payable**	• Creditors • Bills payables
Equity and Liabilities	**4. Current Liabilities**	**c. Other Current Liabilities**	• Current maturities of long term loans • Interest accrued but not due on borrowings • Interest accrued and due on borrowings • Income received in Advance • Unpaid dividend / Unclaimed dividend • Unpaid matured deposit and interest accrued there on • Unpaid matured debentures and interest accrued thereon • Outstanding expenses • Calls in advance • Application money due for refund and Interest thereon

Equity and Liabilities	**4. Current Liabilities**	**d. Short Term Provisions**	• Provision for tax • Provision for employees benefits • Provision for doubtful debts • Provision for discount on debtors
As-sets	**1. Non-current Assets**	**a. Property, plant & equipment and Intangible Assets (i) Property plant and Equipment**	• Land • Building • Machinery & Plant • Vehicles • Office equipment • Furniture and fixture • Live stock • Computers • Office Equipment
As-sets	**1. Non-Current Assets**	**a. Property plant and Equipment (ii) Intangible Assets**	• Goodwill • Brands/trademarks • Copyrights & patents • Computer software • Mastheads and Publishing titles (name of newspapers/ magazines printed at the top of first page) • Mining rights • Recipes, formulae, model, de-signs • Licenses and franchise • Intellectual Property Rights
As-sets	**1. Non-Current Assets**	**a. Property, plant & equip-ment and Intangible Assets (iii) Capital Work in Progress**	Construction of assets in progress E.g. construction of building
As-sets	**1. Non-Current Assets**	**a. Property, plant & equip-ment and Intangible Assets (iv) Intangible Assets Under Development**	

As-sets	**1. Non-Current Assets**	**b. Non-Current Investments**	• Investment in property • Investment in equity instruments • Investment in preference shares • Investment in govt. securities • Investment in debentures/ bonds • Investment in mutual funds • Investments in Partnership firms Note: -Fixed deposit in banks. • They should be classified as Trade Investment&Non-Trade Investment • Trade investment -Investment in shares and debentures for promoting its own business E.g. a company invests in other company which is supplying raw material to it, so as to ensure a continuous supply.
Assets	**1. Non-Current Assets**	**c. Deferred Tax Assets (Net)**	
Assets	**1. Non-Current Assets**	**d. Long Term Loans and Advances**	• Capital advance, (advances for acquiring fixed assets) • Security deposits • Long term loans to employees. • Long term loans to suppliers.
Assets	**1. Non-Current Assets**	**e. Other Non-Current Assets**	• Long term trade receivables • Preliminary expenses, Underwriting Commission, which are to be amortized after a period of 12 months

Assets	**2. Current Assets**	**a. Current Investments**	• Investment in equity instruments • Investment in preference shares • Investment in govt, securities • Investment in debentures / bonds • Investment in mutual funds • Investments in Partnership firms.
Assets	**2. Current Assets**	**b. Inventories**	• Inventory of raw material • Inventory of work in progress • Inventory of finished goods • Stock in trade (goods acquired for trading) • Stores and spares • Loose tools
Assets	**2. Current Assets**	**c. Trade Receivables**	• Debtors • Bills receivable.
Assets	**2. Current Assets**	**d. Cash and Cash Equivalents**	• Cash • Bank balance • Cheques and drafts in hand
Assets	**2. Current Assets**	**e. Short Term Loans and Advances**	• Loans and advances to related parties.
Assets	**2. Current Assets**	**f. Other Current Assets**	• Prepaid expenses • Advance taxes • Interest accrued on investments • Preliminary expenses, Underwriting Commission, which are to be amortized within a period of 12 months

Contingent Liabilities			Contingent Liabilities are those liabilities which are not actual liabilities but may become so on happening of certain events. Examples are following: • Claim against the company not acknowledged as debts • Guarantees • Bills discounted fron bank

Capital Commitments			Capital commitments are agreements to perform a particular activity at a certain time in the future under certain circumstances. Examples are followinqs: • Estimated amounts of contract remaining to be executed on capital account and not provided for • Uncalled liability on investment in partly paid shares. • Arrears of dividend on cumulative preference share Example of Estimated amount of contract remaining to be executed on capital account and not provided for: • A project of ₹ 100 crore to construct a bridge time is 60% complete & 40% remaining If 40% is completed on time the company will get entire ₹ 100 crore and thereby make a profit. (Because ₹ 100 crore which is the contract price includes profit). But if the project is not completed on time penalties rmay be imposed and the company may not be able <u>to make profit out of the project.</u>

DISCLOSURE OF IMPORT ANT ITEMS IN THE COMPANY'S BALANCE SHEET AS PER SCHEDULE III

S. No.	Items	Main Head	Sub-head
1.	Debentures	Non-current Liabilities	Long-term Borrowings
2.	Public Deposits	Non-current Liabilities	Long-term Borrowings
3.	Securities Premium Reserve	Shareholders' Funds	Reserves and Surplus
4.	Capital Reserve	Shareholders' Funds	Reserves and Surplus
5.	Forfeited Shares Account	Shareholders' Funds	Subscribed Capital (Shown by way of addition)
6.	Interest Accrued and due on Debentures	Current Liabilities	Other Current Liabilities
7.	Interest Accrued but not due on Debentures	Current Liabilities	Other Current Liabilities
8.	Bills Payable	Current Liabilities	Trade Payables
9.	Advances Received from Customers	Current Liabilities	Other Current Liabilities
10.	Sundry Creditors	Current Liabilities	Trade Payables
11.	Unclaimed Dividend	Current Liabilities	Other Current Liabilities
12.	Calls-in-Arrears	Shareholders' Funds	Subscribed Capital (shown by way of deduction)
13.	Calls-in-Advance and Interest	Current Liabilities	Other Current Liabilities
14.	Interest Accrued but not due on Unsecured Loans	Current Liabilities	Other Current Liabilities
15.	Debentures Redemption Resrve	Shareholders' Funds	Reserves and Surplus
16.	Capital Redemption Reserve	Shareholders' Funds	Reserves and Surplus
17.	Advance from Customers (Long-term)	Non-current Liabilities	Other Non-current Liabilities
18.	Trade Payables	Current Liabilities	Trade Payables
19.	provision for Tax	Current Liabilities	Short-term Provisions
20.	surplus, Balance in Statement of profit and Loss (Dr.)	Shareholders' Funds	Reserves and Surplus (As negative amount)
21.	surplus, Balance in statement of Profit and Loss	Shareholders' Funds	Reserves and Surplus
22.	Mortagage Loan	Non-current Liabilities	Long-term Borrowings

23.	Patents	Non-current Assets	Property, plants equipment and Intangible Assets—Intangible Assets
24.	Investment	Non-current Assets	Non-current Investments
25.	General Reserve	Shareholders' Funds	Reserves and Surplus
26.	Bills Receivable	Current Assets	Trade Receivables
27.	Borrowings Repayable after 3yrs.	Non-current Liabilities	Long-term Borrowings
28.	Loose Tools	Current Assets	Inventories
29.	current Maturities of Long-term	Current Liabilities	Other Current Liabilities
30.	Premium on Redemption of Debentures	Non-current Liabilities	Other Non-current Liabilities
31.	Balances with Banks	Current Assets	Cash and Cash Equivalents
32.	Tax Reserve	Shareholders' Funds	Reserves and surplus
33.	Stores and Spares	Current Assets	Inventories
34.	Mining Rights	Non-current Assets	Property, plants equipment and Intangible Assets-Intangible Assets
35.	Encashment of Employees Earned Leave Payable on Retirement	Non-current Liabilities	Long-term Provisions
36.	Subsidy Reserve	Shareholders' Funds	Reserves and Surplus
37.	Copyrights	Non-current Assets	Property, plants equipment and Intangible Assets-Intangible Assets
38.	Accrued Incomes	Current Assets	Other Current Assets
39.	Provision for Employees Benefits	Non-Current Liabilities	Long-term Provisions
40.	Unpaid/unclaimed Dividend	Current Liabilities	Other Current Liabilities
41.	Short-term Loans	Current Liabilities	Short-term Borrowings
42.	Long-term Loans	Non-Current Liabilities	Long-term Borrowings
43.	Share Options Outstanding Account	Shareholders' Funds	Reserves and Surplus
44.	Computers	Non-current Assets	Property, plants equipment and Intangible Assets—Tangible Assets
45.	Goodwill	Non-current Assets	Property, plants equipment and Intangible Assets—Intangible Assets

46.	Sundry Debtors	Current Assets	Trade Receivables
47	Long-term Investments	Non-Current Assets	Non-current Investment
48.	Prepaid Insurance	Current Assets	Other Current / Assets
49.	Building	Non-current Assets	Property, plants equipment and Intangible Assets—Tangible Assets
50.	General Reserve	Shareholders' Funds	Reserves and Surplus
51.	Bonds	Non-current Liabilities	Long-term Borrowings
52.	Loans repayable on demand	Current Liabilities	Short-term Borrowings
53.	Income received in advance	Current Liabilities	Other Current liabilities
54.	Office Equipments	Non-current Assets	Property, plants equipment and Intangible Assets—Tangible Assets
55.	Trademarks	Non-current Assets	Property plant & equipment and Intangible Assets
56.	Advance Tax	Current Assets	Other Current Assets
57.	Bank Overdraft	Current Liabilities	Short-term Borrowings
58.	Cheques/Drafts in Hand	Current Assets	Cash and Cash Equivalents
59.	Stock-in-Trade	Current Assets	Inventories
60.	Long-term Provisions	Non-current Liabilities	Long-term Provisions
61.	Stock of Finished Goods	Current Assets	Inventories
62.	Computer software	Non-current Assets	Property, plants equipment and Intangible Assets—Intangible Assets
63.	Work-in-Progress (Building)	Non-current Assets	Property, plants equipment and Intangible Assets—Capital Work-in-Progress
64.	Intellectual Property Rights under Development	Non-current Assets	Property, plants equipment and Intangible Assets—Intangible Assets under Development
65.	Provision for Expenses	Current Liabilities	Short-term Provisions
66.	Capital Advances	Non-current Assets	Long-term Loans and Advance
67.	Designs	Non-current Assets	Property, plants equipment and Intangible Assets—Intangible Assets
68.	Shares in Companies	Non-current Assets	Non-current Investments

CONTENTS OF STATEMENT OF PROFIT AND LOSS

S.No.	Item/Heads	Meaning	Examples/Sub heads
1.	Revenue from operation	Revenue earned by the company from its operating activities.	• Revenue from sale of products or service. • Revenue from sale of scrap.
2.	Other income	Income earned by the company from its non-operating activities.	• Interest income • Dividend income • Profit from sale of investment or fixed assets • Bad debts recovered • Excess provision written back • Rental income etc.
3.	Cost of material consumed	Cost of raw material and other material used in manufacturing of goods.	COMC = opening inventory of raw material + net purchases of raw materials-closing stock of raw materials **Note : inventory of work in progress, finished goods and stock in trade are not considered.**
4.	Purchase of stock-in-trade	Goods purchased for reselling without any further processing.	
5.	Changes in inventories of finished goods, work-in-progress and stock-in-trade	Difference between opening and closing inventories	Change in inventory = opening inventories-closing inventories
6.	Employees benefits expenses	All expenses incurred by the company on its employees.	Direct expenses: • Wages; • Bonus • Leave encashment; • Salaries • Staff welfare expenses • Contribution to employees provident fund and other funds
7.	Finance cost	Cost incurred by the company on borrowings.	• Interest paid on term loan from bank • Interest paid on overdraft and cash credit limit from bank • Interest paid on debentures, bonds public deposits • Discount or loss on issue of debentures written off • Premium payable on redemption of debentures written off • Load processing fees • Guarantee charges • Commitment charges etc. **Note : Service charges not included like bank charges.**
8.	Depreciation and amortization expenses	Depreciation is the cost of tangible assets while amortization is the cost of intangible assets written off their useful life.	• Depreciation of plant and machinery, building, furniture etc. • Amortization of patents, trademarks, copyrights, computer software etc.
9.	Other expenses	Expenses that are not shown any of above mentioned heads are shown here.	• Carriage inwards/outwards • Audit fees; • Insurance charges • Rates and taxes; • Bank charges • Advertisement expenses • Administrative expenses • Selling and distribution expenses • Power and electricity charges • Repair of fixed assets • Rent; • Telephone expenses • Sundry expenses etc.

Practice Questions

1. **Under what format, balance sheet of a company is required to be prepared?**

Sol. Schedule III, Part I

2. **How calls-in-Arrear & calls-in-Advance appear in a company balance sheet?**

Sol. Calls-in-Arrear: it is deducted from the subscribed capital under the head shareholder's fund.

Calls-in-Advance: Major head – current liabilities

Sub-head – other current liabilities

3. **How capital advances appears in a company balance sheet?**

Sol. Major head – Non-current assets

Sub-head – Long-term loans & Advances

4. **How share forfeited account appears in a company balance sheet?**

Sol. Major head – Shareholder's fund

Sub-head – By way of addition to subscribed but not fully paid-up

5. **How ₹ 80,000 7% Debentures redeemable within 12 months from the date of Balance Sheet appears in a company balance sheet?**

Sol. Major head – current liability

Sub-head – other current liability

6. **How ₹ 16,000 Bills Receivable discounted from bank not yet due from payment appears in a company Balance Sheet?**

Sol. Contingent liability.

7. **How 'Mining Rights' appears in a company Balance Sheet?**

Sol. Major head – Non-current assets

Sub-head – Property, plants equipment and Intangible Assets– intangible assets

8. **Match the following:**

(i)	Demand Draft	(a)	Inventories
(ii)	Work-in-progress	(b)	Trade Receivable
(iii)	Debtors	(c)	Cash and cash equivalent

Sol. (i) c

(ii) a

(iii) b

9. State whether the following statements are true/false.

(a) Interest accrued on investment is shown in a company's Balance Sheet under non-current investment.

(b) Proposed divided is a Contingent Liability.

(c) Interest accrued but not due on borrowing is a current Liability.

(d) A company Balance Sheet may be prepared in vertical or horizontal form.

(e) Share forfeited A/c is shown by way of addition to subscribed but not full paid-up capital.

(f) Reserve capital is shown under share capital.

(g) Andit fee is included in other income while preparing income statements.

(h) Investment in preference share for a period of less than 12 months is included in non-current investment.

(i) Format of Balance Sheet is given in schedule III, Part II of companies Act, 2013.

Sol. (a) False (b) True (c) True (d) False (e) True
(f) False (g) False (h) False (i) False

Q.10. Fill in the balance

1. Computer software will be shown under the head _____.
2. Debit balance of statement of profit & loss will be shown under the head.
3. Current assets are realisable within ____ months or _____ which ever is larger.
4. Capital reserve is shown under the major head ______

   Sub head _____ in balance sheet.
5. _____ and _____ are two basic financial statements.
6. While preparing statement of profit and loss of a company, sale of services is shown under the head _____.
7. Calls in advance will be covered under major head ____ sub-head ____
8. Live stock will be covered under major head ____ sub head ____.

9. Loan repayable on demand will be covered under major head ____ subhead _____.

10. Self-generated good will _____ be shown in balance sheet.

Sol. 1. Property, plant and equipment and Intangible Assets

2. Shareholders funds by way of deduction under reserve and surplus

3. 12, operation cycle.

4. Shareholders' funds; reserve and surplus

5. Balance sheet; statement of profit & loss

6. Revenue from operation

7. Current liabilities; other current liabilities

8. Non-current assets Property, Plant and Equipment

   Sol. 9 Major head-Current liabilities

   Sub-head-Short term borrowing

10. not

Assertion and Reason:

Direction: In the following questions, a statements of Assertion (A) is followed by a statement of Reason (R). Mark the correct choices

(A) Both Assertion (A) and Reason (R) are true, and Reason (R) is the correct explanation of assertion (A).

(B) Both Assertion (A) and Reason (R) are true, but Reason (R) is not the correct explanation of Assertion (A).

(C) Assertion (A) is true, but Reason (R) is false.

(D) Assertion (A) is false, but Reason (R) is true.

1. Assertion (A): The Balance Sheet is a list of Assets & Liabilities of the company presented the specified format for the year ended on that date.

Reason (R): The Balance Sheet is a statement of assets and liabilities of the company as of that day.

2. Assertion (A): Balance Sheet and statement of profit & loss show the line items and details there of are given in the notes to accounts.

Reason (R): The companies Act, 2013 has prescribed so far an easy understanding of the financial statements.

Case Based MCQ

Read the following information & answer the following questions x to has the following liabilities

Share Capital ₹ 20,00,000	9% Debenture ₹ 10,00,000
General Reserve ₹ 10,00,000	Loan ₹ 8,00,000
Capital Redemption Reserve ₹ 5,00,000	Trade payable ₹ 4,00,000
Securities premium Reserve ₹ 5,00,000 demand ₹	Loans repayable on 2,00,000

1. How 9% Debenture will be recorded in the Balance Sheet?

(a) Current Liabilities (b) Shareholder's fund

(c) Long-term borrowing (d) None of the above

2. What is the total amount of shareholder's fund?

(a) ₹ 30,00,000 (b) ₹ 35,00,000

(c) ₹ 20,00,000 (d) ₹ 40,00,000

3. What is the total amount of Reserve & Surplus?

(a) ₹ 20,00,000 (b) ₹ 25,00,000

(c) ₹ 15,00,000 (d) ₹ 10,00,000

4. How will loans repayable on demand be recorded in Balance Sheet?

(a) Long term Borrowing (b) Short term Borrowing

(c) Non-current Liabilities (d) Share capital

CHAPTER – 2

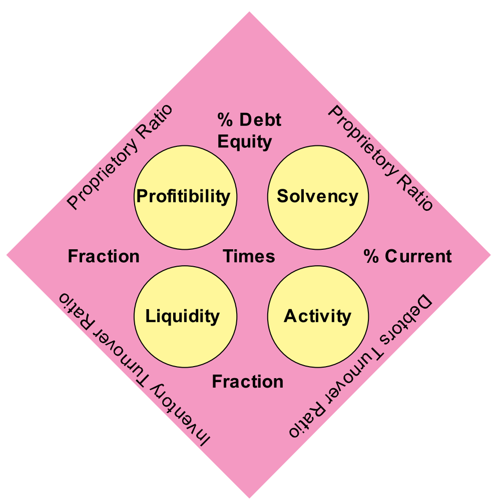
ACCOUNTING RATIOS

Points to Remember:
1. Loose tools and stores & spares will be excluded from inventories while calculating. Current ratio and inventories Turnover ratio.
2. Provision for doubtful debt will be deducted from Trade receivables for calculating current and liquid ratios. But it will not be deducted while calculating trade Receivables turnover ratio.
3. Non-trade Investment will be excluded from shareholder's funds and Capital employed and Total Assets for calculating solvency and Profitability ratios, and their corresponding income (i.e., interest on Non-trade Investment) will be excluded from Net Profit.
4. Operating cost and operating expenses are seperate concept hence shouldn't inter change.

Accounting Ratio: It is an arithmetical relationship between two accounting variables.

Ratio Analysis: It is a technique of analysis of financial statements to conduct a quantitative analysis of information in a company's financial statements.

"Ratio analysis is a study of relationship among various financial factors in a business." -Myers



RATIO ANALYSIS

Expression of ratios: Ratios are expressed in following four ways:

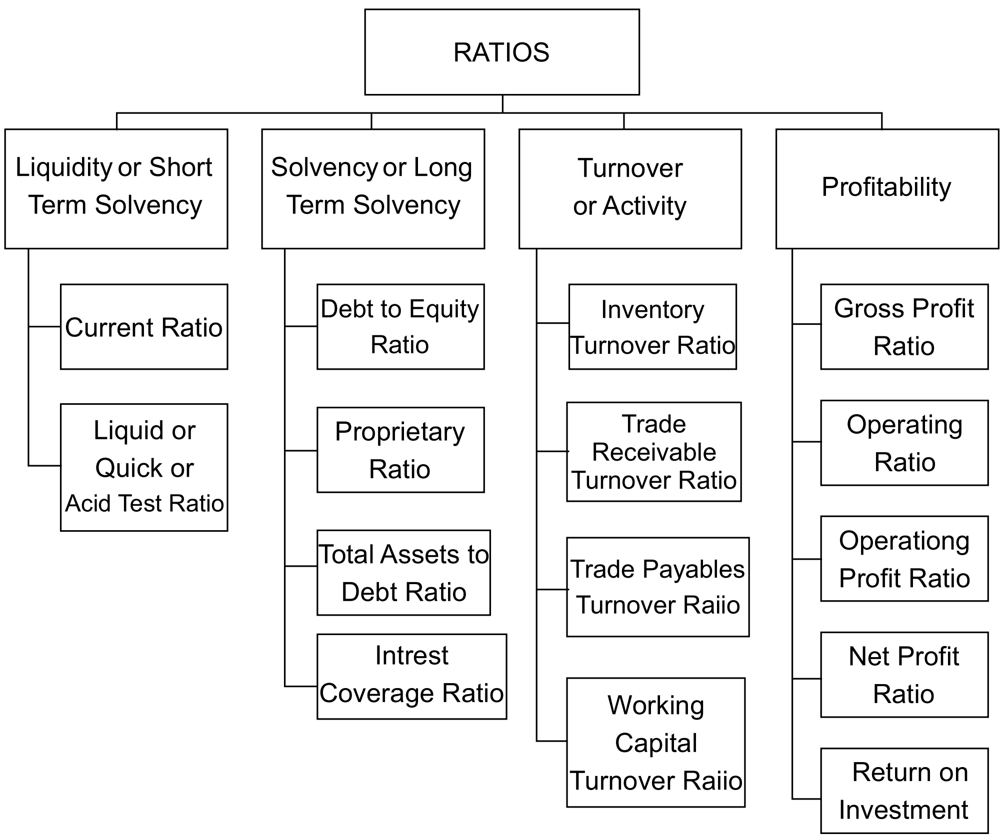
<u>**Pure Ratio**</u> Like 2:1. All liquidity and solvency ratios are expressed in pure form.

<u>**Percentage**</u> **e.g. 15%. All profitabilityratios are presented in percentage** form.

<u>**Times**</u> Like 4 times. All turnover ratios and Interest Coverage Ratio are presented in this form.

<u>**Fraction**</u> **like 3/4.**

Classification or Types of Ratios:



Liquidity Ratios

Current Ratio

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Liquid or Quick or Acid Test Ratio

$$\text{Liquid Ratio} = \frac{\text{Liquid Assets/Quick Assets}}{\text{Current Liabilities}}$$

Supporting Formulae

1. Current Assets = Current Investments (also known as Marketable Securities or ST. Investment)

   + Inventories (except Loose Tools & Stores and Spares)

   + Trade Receivables (Debtors and B.R.) Net after provision for bad dost.

   + Cash and Cash Equivalents (Cash and Bank Balances, Cheques/drafts in hand etc.)

   + Short Term Loans and Advances

   + Other Current Assets (Prepaid Expenses, Accrued Income & Advance Tax)

2. Current Liabilities = Short Term Borrowings (Bank Overdraft and Cash Credit)

   + Trade Payables (Creditors and B.P)

   + Other Current Liabilities (O/s Expenses, Income Received in Advance, Unpaid or unclaimed Dividend interest accrued on borrowing, calls in Advance, current maturities of long term debts).

   + Short Term Provisions (Provision for Tax)

3. Liquid Assets = Current Assets

   - Inventory (closing)

   - Other Current assets (Prepaid Expenses, Accrued Inicome & Advance Tax)

4. Working Capital = Current Assets - Current Liabilities
5. Total Assets = Non-Current Assets + Current Assets
6. Total Liabilities = Non-Current Liabilities + Current Liabilities

7. Non-Current Assets = Fixed Assets (tangible and intangible)

+ Non-Current Investments

+ Long Term Loans & Advances (Capital Advances, Security Deposits)

8. Non-Current Liabilities = Long Term Loans(Debentures, Bank Loans, Bonds)

+ Long Term Provisions (Provision for employee benefit & Warranties)

9. Capital Employed = Shareholders' Fund

+ Borrowed Fund (Non-Current Liabilities)

10. Capital Employed = Total Assets - Current Liabilities

= Non-Current Assets + Working Capital

11. Shareholders' Fund = Share Capital

+ Reserves and Surplus –

Non-Current Non Trade Investments – Interest on Non-Current Non-trade investment

Shareholders Fund = Total Assets - Non Current Liabilities - Current liabilities

Note : Non-Current trade Investments will be included for Capital employed purpase.

Non Current: Investment will remain Non-Current TRADE Investments in absence of any other information.

Solvency Ratios

• Debt - Equity Ratio

$$\text{Debt - Equity Ratio} = \frac{\text{Debt (Non Current Liabilities)}}{\text{Equility (Shareholders Fund)}}$$

• Proprietary Ratio

$$\text{Proprietary Ratio} = \frac{\text{Shareholders' Fund}}{\text{Total Assets}}$$

• Total Asset to Debt Ratio

$$\text{Total Asset to Debt Ratio} = \frac{\text{Total Assets}}{\text{Debt (Non Current Liabilities)}}$$

• Interest Coverage Ratio

$$\text{Interest Coverage Ratio} = \frac{\text{Profit BEFORE Interest, Tax and Dividend}}{\text{Interest on Long Term Loans}}$$

Activityor Turnover Ratios

- Working Capital Turnover Ratio

$$\text{Working Capital Turnover Ratio} = \frac{\text{Revenue from Operation / cost of Revenue from operation}}{\text{Working Capital}}$$

- Inventory Turnover Ratio

$$\text{Inventory Turnover Ratio} = \frac{\text{Cost of Revenue from Operation}}{\text{Average Inventory}}$$

- Receivable Turnover Ratio

$$\text{Receivable Turnover Ratio} = \frac{\text{Net Credit Revenue from Operation}}{\text{Average trade receivables (Average Debt ors+Average BR.)}}$$

$$\text{Receivable Turnover Ratio} = \frac{\text{12 months or 365 days or 52 weeks}}{\text{Debt or Average Collection Period}}$$

- Payable Turnover Ratio

$$\text{Payable Turnover Ratio} = \frac{\text{Net Credit Purchases}}{\text{Average trade payables (Average Creditors + Average B.P.)}}$$

$$\text{Payable Turnover Ratio} = \frac{\text{12 months or 365 days or 52 weeks}}{\text{Average Payment Period}}$$

Supporting Formulae

a) Revenue from Operation (Net Sales) = Total Revenue from Operation - Return of Revenue from Operation

b) Total Revenue from Operation = Cash Revenue from Operation + Credit Revenue from Operation

c) Net Credit Revenue from Operation = Credit Revenue from Operation - Return of Revenue from Operation

d) Cost Of Revenue From Operation (COGS) = Opening Inventory + Net Purchases + Direct Expenses - Closing Inventory

e) Cost Of Revenue From Operation (COGS) = Revenue From Operation - Gross Profit

f) Cost Of Revenue From Operation (COGS) = Cost of Raw Material Consumed
+ Purchases of Stock in Trade
+ Change in Inventory of Finished Goods, WIP, Stock in Trade
+ Direct Expenses

g) Average Inventory = $\frac{\text{Opening Inventory + Closing Inventory}}{2}$

h) Average Debtors = $\frac{\text{Opening Debtors + Closing Debtors}}{2}$

i) Average B.R. = $\frac{\text{Opening B.R. + Closing B.R.}}{2}$

j) Average Creditors = $\frac{\text{Opening Creditors + Closing Creditors}}{2}$

k) Average B.P. = $\frac{\text{Opening BP + Closing B. P.}}{2}$

l) Average Receivable = Average Debtors + Average B.R.

m) Average Payable = Average Creditors + Average B.P.

In absence of Information
• Debtors = Opening Debtors = Closing Debtors = Average Debtors
• B.R. = Opening B.R. = Closing B.R. = Average B.R.
• Creditors = Opening Creditors = Closing Creditors = Average Creditors
• B.P. = Opening B.P. = Closing B.P. = Average B.P.

<u>Profitabiliy Ratio</u>

Gross Profit Ratio

Gross Profit Ratio = $\frac{\text{Groos Profit}}{\text{Revenue from Operation}} \times 100$

Net Profit Ratio

Net Profit Ratio = $\frac{\text{Net Profit After Tax}}{\text{Revenue from Operation}} \times 100$

Operating Ratio or Operating Cost Ratio

$$\text{Operating Ratio} = \frac{\text{Operating Cost}}{\text{Revenue from Operation}} \times 100$$

Operating Profit Ratio

$$\text{Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Revenue from Operation}} \times 100$$

Return on Investmetn or Return on Capital employed

$$\text{ROI} = \frac{\text{Profit BEFORE Interest, Tax and Dividend}}{\text{Capital Employed}} \times 100$$

<u>Supporting Formulae</u>

- Net Profit = Gross Profit + Indirect Incomes - Indirect Expenses

  = Gross profit + Non-Operating Income – (Operating Expenses + Non-Operating Expenses)

  = Gross profit + Non-Operating Incomes – Operating Expenses - Non Operating Expenses

  = Gross profit – Operating Expeses + Non-Operating Incomes - Non Operating Expenses

  = (Gross profit – Operating Expenses) + Non-Operating Incomes, - Non Operating Expenses
- Net Profit = Operating Profit + Non-Operating Incomes - Non Operating Expenses
- Indirect Expenses = Operating Expenses + Non-Operating Expenses
- Non-Operating expenses
- Example Interest Paid on loans (a finance cost)

- Operating Expenses = Office and Administrative Expenses

  + Selling and Distribution Expenses

  + General Expenses

  + Depreciation
- Operating Expenses = Employee Benefit Expenses + Other Operating Expenses
- Indirect Incomes (also known Non-Operating Incomes)

  Example: Interest Received on Investment , dividend, rental in come
- Operating Cost = Cost of Revenue from Operation + Operating Expenses
- Operating Profit = Gross Profit - Operating Expenses

  = Revenue from Operation - Cost of Revenue from operation - Operating Expenses

  = Revenue from Operation - (Cost of Revenue from operation + Operating Expenses)
- Operating Profit = Revenue from Operation-Operating Cost
- Operating Profit = Net Profit - Non Operating Incomes + Non-Operating Expenses

RATIO ANALYSLS

Illustration-1

A firm had current Liabilities of 60,000. After the payment of current liabilities of ₹20,000 current ratio was 3.25:1. Determine current Assests & current ratio before the payment was made.

Sol. Let the current Assets after payment be x

$$\text{The current Ratio} = \frac{\text{Current Assets (CA)}}{\text{Current Liabilities (CL)}}$$

$$\frac{3.25}{1} = \frac{x}{60{,}00 - 20{,}000}$$

$$3.25 \times 40{,}000 = x$$

$$x = 1{,}30{,}000$$

Hence, Current Asset after payment = 1,30,000

Current Asset before payment = (1,30,000 + 20,000)

$$= \boxed{₹1{,}50{,}000}$$

$$\text{Current ratio} = \frac{\text{CA before payment}}{\text{CL before payment}}$$

(Before payment)

$$= \frac{1{,}50{,}000}{60{,}000}$$

$$CR = \frac{2.5}{1}$$

Illustration 2: From the following information, calculate working capital turnover ratio

	₹
Cost of Revenue from operation	6,00,000
Gross profit ratio	25%
Land & Building	2,50,000
(Accumulated Depreciation 50,000)	

Premises	1,50,000
Furniture	2,00,000
Patents	1,00,000
Equity share capital	4,00,000
Pref. Share capital	2,00,000
Securities premium Reserve	2,00,000
9% Debenture	2,00,000

Sol. Working capital turnover ratio = $\frac{\text{Revenue from operation}}{\text{Working capital}}$

When sales is ₹ 100, Gross profit = ₹ 25

Cost of Revenue from operation = 100 – 25 = 75

When cost is 6,00,000, Revenue from operation = 6,00,000 × $\frac{100}{75}$

= 8,00,000

Working capital = Capital employed – Fixed Assets

Capital employed = Eq. Share capital + Pref. Share capital + SPR + 9 % Deb.

(Lia. side approach) 4,00,000 + 2,00,000 + 2,00,000 + 2,00,000

= ₹ 10,00,000

Fixed Asset = L & B (Net) + Premises + Furniture + Patents

2,00,000 + 1,50,000 + 2,00,000 + 1,00,000

= ₹ 6,50,000

Working capital = 10,00,000 – 6,50,00

= ₹ 3,50,000

Working capital turnover ratio= $\frac{8,00,000}{3,50,000}$ = 2.28 times

Illustrations 3. Deb equity ratio is 0.8:1. State giving reason which of the following transaction would improve, reduce or not change the debt-equity ratio.

(a) Issue of bonus shares

(b) Conversation of debenture into equity shares

(c) Purchase of machinery by taking long-term loan

(d) Issue of preference shares for cash

(e) Sale of furniture (Book value ₹ 1,00,000) at ₹ 1,30,000

Sol. (a) **No Change** Only equity will increase and decrease by same amount.

(b) **Reduce** Debt will decrease and equity will increase

(c) **Improve** Debt will increase but equity will remain unchanged.

(d) **Reduce** Equity will increase but debt will remain unchanged.

(e) **Reduce** Equity will increase by profit margin and debt will remain unchanged.

Illustration - 4 Calculate current ratio & Quick ratio

	₹		₹
Total Assets	15,00,000	Long term Borrowings	4,00,000
Fixed Assets	5,00,000	Long term provision	2,00,000
Non- current investment	1,00,000	Inventories	1,70,000
Long term Loans Advances	1,00,000	Prepaid Expenses	30,000
		Total Debt	10,00,000

Sol. Current ratio = $\dfrac{\text{Current Assets}}{\text{Current Liabilities}}$

Current Assets = Total Assets - Non current Assets

= Total Assets - (Fixed Asset + Non Current Invt.+ Long term Loans& Adv.)

= 1500,000 – (500 000+10 0000+100000)

$\boxed{\text{CA} = \text{Rs } 800{,}000}$

Current Liabilities = Total debt - Non - current liiabilites

$$= \text{Total Debt} - (\text{Long term Borrowings} + \text{Long term provisions})$$

$$= 10,00,000 - (400,000 + 200,000)$$

$$\boxed{CL = ₹\ 4,00,000}$$

$$\boxed{\text{Current Ratio}} = \frac{₹8,00,000}{₹\ 4,00,000} = \boxed{2:1}$$

$$\boxed{\text{Quick ratio}} = \frac{\text{Quick Assest}}{\text{Current Liablities}} = \frac{₹6,00,000}{₹4,00,000} = \boxed{1.5 : 1}$$

$$\boxed{\text{Quick Assets}} = \text{Current Assets} - \text{inventories} - \text{prepaid expenses}$$

$$= ₹\ 8,00,000 - ₹170,000 - ₹30000$$

$$\boxed{QA = ₹600000}$$

Illustration 5: Trade Receivable turnover ratio is 4 times state giving reason, which of the following transactions will increase, decrease or no change the ratio:

(a) Bed debt ₹ 4000

(b) Discount allowed ₹ 6,000

(c) Revenue from operation return ₹ 5,000

(d) Collection from trade Receivable ₹ 6,000

(e) Bill Receivables ₹ 10,000 drawn

Sol.

Transactions	Effector Ratio	Reason
(a)	Reduce	Bad debts will reduce closing debtors which will result in decrease in T/R turnover ratio.
(b)	Reduce	Discount allowed will reduce closing debtors which will result in decrease in T/R turnover ratio.
(c)	Improve	Both Revenue from operation & closing trade receivable will decrease by same amount resulting in increase in T/R turnover ratio.

(d)	Reduce	Closing trade receivable will decrease resulting in decrease of T/R turnover ratio.
(e)	No change	Trade receivable will remain unchanged. Hence T/R turnover ratio.

Illustration 6. Calculate (i) Operating ratio; (ii) Inventory turn over ratio

Cash revenue from operation ₹ 10,00,000

Credit revenue from operation 120% of cash revenue from operation

Operating expenses- 10% of total revenue from operation

Rate of gross profit- 40%

Opening inventory- ₹ 1,50,000

Closing inventory- ₹ 20,00 more than opening inventory

Solution. Operating ratio

$$= \frac{\text{Cost of revenue from operation} + \text{operating expenses}}{\text{Revenue from operation}} \times 100$$

Credit revenue from operation $= \frac{120}{100} \times 10,00,000 = ₹12,00,000$

Total revenue from operation = 12,00,000 + 10,00,000 = ₹ 22,00,000

Operating expenses = 10% of ₹ 22,00,000 = ₹ 2,20,000

Gross profit = 40% of 22,00,000 = ₹ 8,80,000

Cost of revenue from operation = ₹ 22,00,000 - ₹ 8,80,000 = ₹ 13,20,000

Operating ratio $= \frac{13,20,000 + ₹\,2,20,000}{22,00,000} \times 100 = 70\%$

(ii) Inventory turnover ratio $= \frac{\text{Cost of revenue from operation}}{\text{Average inventory}}$

(iii) Average inventory $= \frac{\text{Opening inventory + Closing inventory}}{2}$

Closing inventory = Opening inventory + ₹ 20,000

= 1,50,000 + 20,000 = ₹ 1,70,000

$$= \frac{13,20,000}{1,70,000} = 7.76$$

Illustration 7:

The Following particulars are extracted from the Balance Sheet of XYZ ltd. as at 31st Mar 2019 :-

Particulars	Rs Amount
Equity share capital	2,00,000
10% preference share capital	1,80,000
capital reserve	40,000
profit & loss balance	1,00,000
12% Debenlures	50,000
10% Mortgage laon	1,50,000
Current Liabilities	4,20,000
Current Assets	300,000

calculate the following ratio:

(a) Debt - EquityRatio

(b) Proprietary ratio

(c) Interest coverage ratio when Net profit after tax ₹ 50,400 & rate of Income tax was 40%

Sol. (a) DEBT - EQUITY RATIO $= \dfrac{\text{Debt}}{\text{Equity}}$

Debt (long - term) = Debentures + Mortgage loan

= ₹ 50,000 + 1,50,000

= 200,000

Equity / Share holder`s Funds = Eq share cap + pref. share cap + cap. Reserve + p& L balance

= 200,000 + 180,000 + 40,000 + 100,000

= ₹ 520,000

Debt - Equity Ratio $= \dfrac{₹\ 200{,}000}{₹\ 520{,}000} = \dfrac{0.38}{1}$

(b) Proprietory Ratio $= \dfrac{\text{Shareholder`s funds}}{\text{Total Assets}}$

$= \dfrac{₹\ 5{,}20{,}000}{₹\ 11{,}40{,}000} = 0.456$

Eq. share capital + Pref. sh. + Cap. Res.
+ P & L Bal. + 12% Des. + 10% mortgage loan + C.L.

= 2,00,000+1,80,000+40,000+1,00,000+10,000 +1,50,000+4,20,000 = 11,40,000

(c) Interest Coverage Ratio $= \dfrac{\text{Net profit before interest \& tax}}{\text{Int. on Long term Loans}}$

Interest on Long term Loans = 12% int. on Deb. of Rs 50,000 + 10% Int. on mortgage loan of Rs 150,000

$$= \left(\frac{12}{100} \times 50{,}000\right) + \left(\frac{10}{100} \times 150{,}000\right)$$

$$= 6000+15000 = \text{Rs } 21000$$

Let net profit bfore tax = Rs 100

Tax = Rs 40

Net profit after tax = Rs 60

Net profit after Tax is Rs 60 when net profit before Tax = 100

Net profit after tax is Rs 50,400 Then net profit before Tax = $100 \times \frac{50{,}400}{60}$

Rs = 84000

Net profit before tax = Rs 84000

Net Profit before int. & tax = Rs 84000+21000

= Rs 10,5000

Interest Coverage Ratio = $\frac{\text{Rs } 105000}{\text{Rs } 21000}$ =5 times

Illustration - 8

Calculate Total Assets to Debt Ratio from foll. inf. -

			₹
Capital Employed	16,20,000	Equity share capital	8,00,000
Current Liabilities	180,000	8% Debentures	3,00,000
Fixed Asset (Gross)	9,50,000	Capital Reserve	2,40,000
Accumulated Depreciation	1,50,000	Surplus (i.e., balance in Statement of P&L - dr.)	20,000
Non - Current Investment	700,000		
Trade Receivables	2,50,00	Cash & Cash Equivalents	50,000

Sol. Total Asset to debt Ratio = $\frac{\text{Total Assets}}{\text{Debt}}$

Total Assets = Non - Current Assets + Current Assets

= [Fixed asset (Gross) (-) Accumulated Depreciation + Non - current - Investment] + [Trade Receivable + cash & cash eq.]

= [9,50,000 – 1,50,000 + 7,00,000] + [250,000 +50,000]

= 15,00,000 + 3,00,000

$\boxed{\text{Total assets = Rs } 18{,}00{,}000}$

Capital employed = shareholders fund + long term Debts

16,20,000 = 10,20,000 + long term Debts

$\boxed{\text{Long term Debts}}$ = 16,20,000 – 10,20,000

$\boxed{\text{Rs } 6,00,000}$

Shareholders funds = Eq share cap +cap reserve (–) Surplus Balance in Statement of P & L

= 8,00,000 + 2,40,000 - 20,000

= Rs 10,20,000

Total Asset to Debt ratio $= \dfrac{\text{Rs } 18,00,000}{\text{Rs } 6,00,000} = 3:1$

Illustration - 9

Following is the balance sheet of Davi Exports ltd. As at 31st march 2019

Particulars	Rs
I. EQUITY & LIBILITIESS	
1. Shareholder`s Funds	
(a) Share Capital	5,00,000
(b) Reserve & Surplus	13,92,000
2. Non- current Liabilities	
15% Long term Borrowings	16,00,000
3. Current Liabilities	8,00,000
Total	42,92,000
II ASSETS	Rs
1. Non - current Assets	
(a) Fixed Assets	18,00,000
(b) Non - Current investment	
(I) 10% Investment	2,00,000
(II) 10% Non- Trade investment	1,20,000
2. Current Assets	21,72,000
Total	42,92,000

I. Calculate Return on investment if net profit before tax for the year 2018-19 is ₹ 7,83,600

II. Calculate Return on investment for the year 2018-19 W.r.t. opening capital employed given–

(a) Reserve & surplus

Surplus	4,20,000
Opening balance	9,72,000
	13,92,000

Solution: (I) If Net profit before tax = ₹ 7,83,600

$$\text{ROI} = \frac{\text{Net profit before int. \& fax}}{\text{Capital Employed}} \times 100$$

$$= \frac{₹\ 10,11,600}{₹\ 33,72,000} \times 100 = 30\%$$

Net Profit before interest & fax:

	Net Profit before tax	₹ 7,83,600
Add	Int on long term borrowing (15% 1600000)	₹ 2,40,000
Less	Int on Non-trade Investments (10% of 120000)	₹ (12000)
	Net Profit before Int & tax	₹ 10,11,600

Calculation of capital Employed—

Asset side Approach

Capital Employed = Fixed Asset + Working capital

= Non-current Assets (excluding Non-Trade investment) + Current Assets – current liabilities

= 20,00,000 + 21,72,000 – 8,00,000

= ₹ 33,72,000

Liabilities side Approach :-

Capital Employed = Share capital +Reserve & Surplus+ Non Current liabilities - Non - Trade Investment

= 5,00,000 + 13,92,000 + 16,00,000 - 1,20,000

= Rs33,72,000

II ROI = $\frac{\textbf{Net profit before int \& Tax}}{\text{Opening capital Employed}} \times \mathbf{100}$

Given - Net profit RS 9,72,000

Add Int. on Long term Borrowing Rs 2,40,000
(15% 16,00,000)

Less Int. on Non- Trade investment Rs (12,000)
(10% 1,20,000)

Net profit before int. & tax Rs 12,00,000

Calculation of capital employed :-

Asset side Approach :-

Capital Employed = Non Current Assets (excluding Non-trade investment) + Current Assets - Current Liabilities -Current Years Profit

= Rs (20,00,000 + 21,72,000 - 8,00,000,-9,72,000)

= Rs 24,00,000

Liabilities side Approach :-

Capital Employed = Share capital + Reserve & Surplus (Current year's profit) + Non current Liabilities - Non - Trade Investments

= Rs (5,00,00 + 4,20,000+16,00,000 - 1,20,000)

= Rs 24,00,000

Hence, RoI = $\frac{\text{Rs}12,00,000}{\text{Rs } 24,00,000} \times 100 = 50\%$

Illustration -10

Calculate Gross profit ratio from the foll -

Cash sales 25 % of Net Sales

Average inventory Rs 1,60,000

Inventory Turnover ratio 8 times

Average Trade Receivables Rs 2,00,000

Trade recevables Turnover ratio 6 times

Sol. Gross profit ratio = $\frac{\text{Gross Profit}}{\text{Revenue from Operations}} \times 100$

= Rs $\frac{3,20,000}{16,00,000} \times 100 = 20\%$

Cost of Revenue from Opertions :-

Inventory Turnover Ratio = $\frac{\text{COGS}}{\text{Average Inventory}}$

$8 = \frac{\text{COGS}}{\text{Rs } 1,60,000}$

COGS = Rs 1,60,000 × 8

= $\boxed{\text{Rs } 12,80,000}$

Credit sales :-

Trade Receivable Turnover Ratio = $\frac{\text{Net credit sales}}{\text{average trade receivables}}$

$$6 = \frac{\text{Net cr. sales}}{\text{Rs } 2,00,000}$$

$$\text{Net cr. sales} = 6 \times \text{Rs } 2,00,000$$

$$= \boxed{\text{Rs } 12,00,000}$$

If Cash sales = 25% net sales

Then Credit sales = 75% of net sales

Rs 12,00,000 = 75% Net sales

$$\text{Net sales} = \text{Rs } \frac{12,00,000}{75\%} = \boxed{16,00,000}$$

Gross profit = [Revenue from operations] - [Cost of revenue from
(Net sales) Operations (COGS)]

= Rs 16,00,000 - Rs 12,80,000

= Rs 3,20,000

Illustration -11

calculate Operating rato from the following

Operating cost	Rs 6,80,000
Operating expenses	Rs 80,000
Purchase of stock in trade	Rs 6,06,000
change in invetories of stock in trade	Rs(15,000)
Employes benefits Expenses	Rs 9,000
Selling & Distribution Expenses	Rs 58,000
Loss on sale of fixed Asset	Rs 12,000
Gross profit Ratio	- 25%

Administrative Expenses ₹ 22,000

Sol. Operating Ratio = $\dfrac{\text{Cost of revenue from operations} + \text{Operating Expenses}}{\text{Revenue from opertaion}} \times 100 = 85\%$

$= \dfrac{Rs\,6,00,000 + Rs\,80,000}{Rs\,8,00,000} \times 100$

Cost of revenue from Operation = operating cost - operating expenses

= Rs6,80,000 - Rs 80,000

= Rs6,00,000

Cost of revenue from operation = Purchase of stock in Trade + Change in inventories + stock in stock + Employe Benefit Expenses

= Rs6,06,000 – Rs15,000 + Rs9000

= Rs 6,00,000

Operating Expenses = Given Rs80,000

Otherwise Operating Exp. = Administrative Expenses + selling & Distribution Expenses

= Rs 22000+ Rs58000

= Rs80,000

(a) Cost of Revenue from operations -

Let Revenue from Operations be rs 100

and If Gross profit = 25

Then, Cost of revenue fom operation = Rs75

If cost of revenue from operation is Rs75 Revenue fom operations Rs100

If cost of revenue from operation is Rs6,00,000

Then revenue from Operation = $Rs\,6,00,000 \times \dfrac{100}{Rs\,75}$

= 8,00,000

Illustration - 12

Revenue from operation 8,00,000

Gross profit ratio 25%

Operating ratio 90%

Non - Operating Expenses Rs4000

Non - Operating income Rs44000

calculate Net profit ratio:

Sol. Net profit ratio = $\dfrac{\text{Net Profit}}{\text{Revenue from operations}} \times 100$

$= \dfrac{Rs\,1,20,000}{Rs\,8,00,000} \times 100 = 15\%$

Calculation of Net profit

Operating profit ratio = 100% − Operating Ratio

$= 100\% - 90\%$

$= 10\%$

Operating profit Ratio = $\frac{\text{Operating profit} \quad *100}{\text{Revenue from Operations}}$

$$10 = \frac{\text{operating Profit}}{8{,}00{,}000} \times 100$$

Operating profit = $\frac{\text{Rs } 8{,}00{,}0000 \times 10}{100}$ = 80,000

Net profit = Operating profit +Non operating Income - Non Operating Expenses

= Rs80,000+ Rs44,000 - Rs4000

Rs1,20,000

Illustration 13. Cash sales ₹ 60,000; Credit sales $66\frac{2}{3}\%$ of total sales; Adjusted purchase ₹ 1,20,000;
closing inventory ₹ 10,000; wages ₹ 10,000; selling and distribution exp. ₹ 10,000; office expenses ₹ 25,000; interest received ₹ 20,000; dividend received ₹ 10,000; loss on sale of machinery ₹ 5000.

Calculate net profit ratio.

Sol. Net profit ratio $= \frac{\text{Net profit after tax}}{\text{Revenue from operation}} \times 100$

Total revenue from operation = 100 percent

Cash revenue from operation = 100 - $66\frac{2}{3} = 33\frac{1}{3}\%$ or $\frac{1}{3}$ of total.

Cash revenue from operation $= \frac{1}{3}$ of total revenue from operation

Total revenue from operation $= 60{,}000 \times 3$ = ₹ 1,80,000

Gross profit = Total revenue from operation - Adjusted purchase - Wages
= 1,80,000 - 1,20,000 - 10,000 = ₹ 50,000

Net profit = Gross profit - office Exp. - selling and dist. exp. - loss on sale of machinery + divident recieved + interest received
= 50,000 - 25,000 - 10,000 - 5,000 + 10,000 + 20,000 = ₹ 40,000

Net profit ratio $= \frac{40{,}000}{1{,}80{,}000} \times 100 = 22.22\%$

Illustration 14: Calculate operating profit ratio:

	₹
Credit Revenue from operation	3,00,000
Wages	10,000
Cash Revenue from operation	1/4 of total Revenue from operation
Adjusted purchase	2,40,000
Finance cost	8,000
Discount Received	5,000
Selling & distribution expenses	30,000
Loss on fixed assets	20,000
Carriage outward	6,000

Sol. Operating profit ratio = $\dfrac{\text{Operating profit}}{\text{Revenue from operation}} \times 100$

Let total revenue from operation be ₹ x

credit revenue from operation = $x - \dfrac{1}{4}x$

$= \dfrac{3}{4}x$

$\dfrac{3}{4}x = 3{,}00{,}000$

$x = 3{,}00{,}00 \times \dfrac{4}{3} =$ ₹ 4,00,000

Gross profit = Revenue from operation – cost of Revenue from operation

= 4,00,00 –(2,40,000 + 10,000)

= ₹ 1,50,000

Operating profit = Gross profit – operating exp. + operating income

= 1,50,000 – 30,000 – 6,000 + 5,000

= 1,19,000

Operating profit ratio = $\dfrac{1{,}19{,}000}{4{,}00{,}000} \times 100 = 29.75\%$

Illustration 15: Calculate debt to capital employed ratio from the following information:

	₹		₹
Equity Share Capital	50,00,000	Plant & Machinery	30,00,000
6% pref. Share Capital	20,00,000	Land & Building	25,00,000
General Revenue	10,00,000	Furniture & Fixture	10,00,000
Debenture Red. Reserve	10,00,000	Non-current investment fund	10,00,000
Statements of P&L A/c (Dr.)	10,00,000	Long term Loans and Advances	10,00,000
7% Debenture (Non-convertible)	20,00,000		
Bank Loan	9,00,000	Inventory	20,00,000
Trade payable	5,00,000	Debtors	13,00,000
Creditors	4,00,000	Trade Receivables	10,00,000
Outstanding exp.	1,00,000		

Sol.

Debt to capital employed = $\dfrac{\text{Long term Debt}}{\text{Capital employed (or Net Assets)}}$

Capital employed = Eq. Sh. Capital + Pref. Sh. Capital + Gen. Res. + Deb. Red. Res – Statement of P & L + Deb. + Bank Loan

or

Net Assets = Total Assets (Net) – current liabilities or fixed assets + working capital

= 50,00,000 + 20,00,000 + 10,00,000 + 10,00,000 – 10,00,000 + 20,00,000 + 9,00,000 = 1,18,00,000

= 128,00,000 – 10,00,000 = 1,18,00,000

= 30,00,000 + 25,00,000 + 10,00,000 + 10,00,000+10,000,000+20,00,000 +13,00,000+10,000,000 – 5,00,000 – 4,00,000 – 1,00,000

= 85,00,000 + 33,00,000 (43,00,000 – 10,00,000)

= 1,18,00,000

Long term Debt = 7% Debenture + Bank Loan

= 20,00,000 + 9,00,000 = 29,00,000

Debt to capital employed = $\dfrac{29,00,000}{1,18,00,000}$ = 0.24 : 1

Illustration 16: Calculate net assets turnover ratio from the following information credit revenue from operation ₹ 40,00,000

Cash revenue from operation – 50% of credit revenue from operation

Revenue from operation (return) ₹ 2,00,000

Share Capital	₹ 15,00,000	Property, plant, equipment and Intangible Assets	₹
General Reserve	₹ 5, 00,000	(a) Tangible	15,00,000
Statement of P& L	₹ 5,00,000	(b) Intangible	5,00,000
Loan from SBI	₹ 5,00,000	Non-current Invest.	10,00,000
8% Debenture	₹ 5,00,000	Inventory	4,00,000
Trade payable	₹ 4,00,000	Debtors	4,00,000
Outstanding exp.	₹ 1,00,000	Trade Receivables	2,00,000

Sol

Net Assets turnover ratio = $\frac{\text{Net Revenue from operation}}{\text{Capital employed (or Net Asset)}}$

Credit revenue from operation = ₹ 40,00,000

Cash revenue from operation = $\frac{50}{100} \times 40,00,000$

= ₹ 20,00,000

Revenue from operation = 40,00,000 + 20,00,000 – 2,00,000

= ₹ 58,00,000

Capital employed = Sh. Capital + G/R + St. of P& L A/c + Loan + Deb.

or

Property, plant, equipment and intangible assets + working capital

Net Assets = Total Assets (Net) – Current Liabilities

= 15,00,000 + 5,00,000 + 5,00,000 + 5,00,000 + 5,00,000

= 35,00,000 ₹

= 15,00,000 + 5,00,000 + 10,00,000 + 4,00,000 + 4,00,000 + 2,00,000 – 4,00,000 – 1,00,000

= ₹ 35,00,000

Net Assets turnover ratio = $\frac{58,00,000}{35,00,000}$ = 1.65 times

Practice Questions

Q.1 Tick (✓) the appropriate answer.

_____ may indicate that the resources of the business are being effectively managed.

(a)	profitability ratio	(b)	Turn over ratio
(c)	solvency ratio	(d)	liquidity ratio

2. What will be the operating profit ratio, if operating ratio is 85.38%

(a)	13.62%	(b)	14.62%
(c)	15.28%	(d)	16.62%

3. The area of interest for a long term lender while analysing financial position of a business will be

(a)	Liquidity ratio	(b)	profitability ratio
(c)	solvency ratio	(d)	turn over ratio

4. If opening inventory ₹ 38,500; closing inventory ₹ 41,500; revenue from operation ₹ 2,40,000; gross profit 20% on cost, inventory turn over ratio will be

(a)	3 times	(b)	4 times
(c)	5 times	(d)	6 times

5. If revenue from operation is ₹ 1,80,000 and gross profit ratio is 45%. If there is decrease in interest on investment. Then net profit ratio will

(a)	improve	(b)	decline
(c)	no change	(d)	None of these

6. Liquid ratio of a company 1 : 6 : 1. Which of the following will result in decrease of this ratio

(a) Bill Receivable drawn on Debtors

(b) Purchase of goods on credit

(c) Sale of goods for cash

(d) Bill payable accepted for one month

7. Net profit after tax and interest ₹ 1,00,000; current assets ₹ 4,00,000 current liability. ₹ 2,00,000; Tax rate @ 50%; Total assets ₹ 10,00,000 and 10% debenmture ₹ 4,00,000. Calculate return on investment.

(a)	25%	(b)	30%
(c)	35%	(d)	40%

8. The _____ may indicate that the firm is experiencing stock out and cost sales.

(a) Average payment period (b) inventory turn over ratio

(c) average collection period (d) quick ratio

9. Proprietary ratio of a company will be:

Equity Share Capital 3,00,000; Debenture 1,00,000; Trade payable 10,000; Creditors 20,000; Statement of Profit & Loss (Debit Balance) 30,000; Bank Loan 1,40,000

(a) 75% (b) 50%

(c) 70% (d) 82%

10. If share capital ₹ 5,00,000; Reserve and surplus ₹ 1,00,000 long term borrowing ₹ 8,00,000; long term provision ₹ 2,00,000 non-trade investment ₹ 1,50,000 compute capital employed

(a) 15,00,000 (b) 14,00,000

(c) 16,00,000 (d) 14,50,000

11. State whether the following statements are true/false

(a) Provision for bad debt is included in calculating current ratio.

(b) Gross profit helps in assessing efficiency of business and fixing selling prices.

(c) Purchase of building by issue of equity shares improves debt equity ratio.

(d) Loss of stock by fire is included in calculating operating ratio.

(e) High interest coverage ratio shows the inability of business to pay long-term debts and interest.

12. Fill in the blanks.

(a) Loose tools, stores & spare parts are not included in current Assets while calculating current ratio as _________.

(b) If gross profit is 25% on cost, then grass profit ratio _________.

(c) Ideal liquid ratio is _________.

(d) _________ and operating profit ratio are complimentary to each other.

(e) Earning capacity of the business is assessed through ________.

13. Net profit after interest and tax ₹ 1,00,000; current assets ₹ 4,00,000 current liabilities ₹ 2,00,000; Tax rate @ 20%; fixed assets ₹ 6,00,000; 10% long term debt ₹ 4,00,000.

Calculate return on investment.

[Hint- Capital employed = Fixed Assets + Current Assets – Current Liabilities]

NPBT = NPAT & Int/1 – tax rate

14. Equity share capital 12,00,000

Equity share capital	12,00,000
General Reserve	5,00,000
Debenture Redemption Reserve	1,00,000
Surplus i.e. Balance in statement of P&L A/c (Dr.)	2,00,000
Proprietary ratio	0.2 : 1

Calculate total Assets

15. Calculate current ratio -

Working capital - ₹ 150,000

Total Liabilities other than shareholder's funds - Rs 3,85,000

Long term debt - ₹ 2,85,00

16. Working capital ₹ 36000

Current ratio 2 · 8 : 1

Inventory Rs 16000

Calculate current Assets, current Liabilities & Quick ratio

(Hint = WC = CA-CL

Quick Assets = Current Asset - Inventory)

17. Calculate working capital turnover ratio from the following information

Revenue from operations	₹ 1200,000
Current Assets	₹ 500,000
Total Assets	₹ 10,00,000
Non - current Liabilities	₹ 4,00,000
Shareholder's funds	₹ 4,00,000

(Hint - Current Assets = Total Assets - Non-CL - Shareholder's fund)

18. Calculate Trade payables Turnover ratio -

op, sundry Creditors ₹ 80,000 Closing sundry creditors ₹ 90,000

op, Bill Payable	₹ 10,000	CL Bill payable	₹ 20,000
purchase	₹ 10,00,000	cash purchase	₹ 3,28,000
purchase returns	₹ 72,000		

Hint - Net cr. purchase = purchase - PR - cash purchase

19. Calculate inventory turnover ratio from the foll inf-

Net sales	₹ 40,000
Average inventory	₹ 5500

Gross loss on sales is 10%

(Hint: Cost of revenue from operation = Net sales + Gross loss)

20. Calculate gross profit ratio

	₹
Cash revenue from operation	3,00,000
Purchase : Cash	2,00,000
Credit	4,00,000
Carriage inwards	6,000
Salaries	80,000
Decrease in inventory	80,000
Return outwards	20,000
Wages	50,000

Ratio of cash revenue from operation to credit revenue from operation 1 : 5.

(Hint : COGs = Purchase + Decrease in inventory + direct expenses)

21. Operating ratio is 70% state giving reason, which of the following transaction will (a) increase (b) decrease (c) no change

(a) Revenue from operation return (sales return) ₹ 10,000

(b) Goods costing ₹ 5000 withdrawn for personal use

(c) Loss on sale of building ₹ 10,000

(d) Purchase return ₹ 5,000

(e) Selling and distribution exp. 10,000

22. Calculate trade receivable turnover ratio & average collection period from the following particulars as on 31st March 2022, assuming 365 working days in a year:

	₹
Total Revenue from operation	10,00,000
Revenue from operation (return)	10,000
Discount Allowed	825
Provision for Bed Debt	1630
Debtors on 31.3.21	65,000
Debtors on 31.3.22	75,000
Bills Receivables 31.3.21	45,000
Bills Receivables 31.3.22	65,000

23. Calculate proprielary ratio from the foil, inf-Long terms Debt ₹ 32,00,000

Working Capital ₹ 4,00,000 Current Assets ₹ 20,00,000 shareholder's fund 18,00,000 Reserves & surplus ₹ 2,00,000

(Hint - Total Assets = shareholder's funds + Long term Debt + Current Liab.)

24. Calculate Total Asset to Debt Ratio -

Fixed Aset (Gross)	10,00,000
Accumulated Depreciation	500,000
Non - current investment	1,50,000
Long term loans & Advance	1,00,000
Current Assets	4,50,000
Total Debt	7,50,000
Sundry Creditors	25,000
Expenses Payable	25,000
Bill payable	25,000
Short term bank loan	50,000

25. A company has loan of ₹ 20,00,000 as part of its capital Employed. The interest payable on loan is 15% &the RoI of the company is 25% The rate of income Tax is 40%. What is the gain to the shareholders due to the loan raised by the company?

(Net Gain = Net profit before int. & Tax - Interest - Tax)

26. Calculate (a) Gross profit ratio (b) Net profit ratio (c) Current ratio (d) Inventory turn over ratio (e) operating ratio

		₹	
Revenue from operation	28,25,000	Cost of revenue from operation	19,20,000
Operating expenses	2,50,000	Net worth	15,00,000
Current liabilities	7,00,000	Fixed assets	16,00,000
Average inventory	8,00,000	long term borrowing	9,00,000

Hint- Current assets = Networth + Long term debt + CL - Fixed assets

27. Net profit after interest and tax ₹ 1,00,000; Current assets ₹ 4,00,000

Current liabilities ₹ 2,00,000; Tax rate @ 20%; fixed assets ₹ 6,00,000; 10% long term debt ₹ 4,00,000

Calculate return on investment.

Hint- Capital employed = Fixed assets + Current assets - Current liabilities

$$\text{Net profit before tax} = \frac{\text{Net profit after tax and interest}}{1 - \text{Tax rate}}$$

Assertion and Reason

Directions: In the following questions, a statement of Assertion (A) is followed by a statement of Reason (R). Mark the correct choice as:

(A) Both Assertion (A) and Reason (R)n are true and Reason (R) is the correct explanation of Assertion (A)

(B) Both Assertion (A) and Reason (R) are true but Reason (R) is not the correct explanation of Assertion (A)

(C) Assertion (A) is true, but Reason (R) is false

(D) Assertion (A) is false, but Reason (R) is true

1. **Assertion (A):** The standard ratio of liquid ratios is 1 : 1.

Reason (R): A company should have sufficient liquid assets to meet its current liabilities.

2. **Assertion (A):** Debt equity ratio determines the long-term solvency of the business.

   Reason (R): A high debt-equity reveals that the business is being managed effectively.

Cash Based MCQ

Read the following information & answer the following questions. Inventory ₹ 2,00,000; Debtors ₹ 3,00,000; Prepaid exp ₹ 1,00,000; Cash ₹ 2,00,000; Bank ₹ 1,00,000; Revenue from operation (Net) ₹ 24,00,000; Trade payable ₹ 2,00,000; Bills payable ₹ 1,00,000.

1. **What is the current ratio?**

   (a) 2 : 1 (b) 2.5 : 1

   (c) 3 : 1 (d) 4 : 1

2. **What is liquid ratio?**

   (a) 2 : 1 (b) 3 : 1

   (c) 1 : 1 (d) 2.5 : 1

3. **What is working capital?**

   (a) ₹ 5,00,000 (b) ₹ 7,00,000

   (c) ₹ 8,00,000 (d) ₹ 6,00,000

4. **What is working capital turnover ratio?**

   (a) 2 times (b) 3 times

   (c) 4 times (d) 5 times

POINT TO REMEMBER

Calculation of Gross profit-

Gross profit on cost = Gross profit on sales

1. 20% on cost or 1/5 on cost = 16.66% on sales or 1/6 on sales
2. 25% on cost of 1/4 on cost = 20% on sales or 1/5 on sales
3. $33\frac{1}{3}$% on cost of 1/3 on cost = 25% on sales or 1/4 on sales
4. 50% on cost of 1/2 on cost = $33\frac{1}{3}$% on sales or 1/3 on sales

   Note: When we go from cost to sales, add numerator to denominator.

Ex. 1/5 on cost or 20% = $\frac{1}{1+5} = \frac{1}{6}$ on sales or 16.66%

Similarly when we go from sales to cost, substract numerator from denominator.

Ex. 1/4 on sales or 25% $= \frac{1}{4-1} = \frac{1}{3}$ or $33\frac{1}{3}$ on cost

Note: While calculating ROI, profit after interest and tax is given and tax rate is given then

Profit before tax $= \frac{\text{Profit after interest and tax}}{100 - \text{tax rate\%}}$

Ex. If tax rate is 40%, then $\frac{PAT}{100-40} = \frac{PAT}{60\%}$

Note-:

Ideal Ratios

- Current ratios 2:1
- Liquid Ratio 1:1
- Destequity ratios 2:1
- Interest Coverage ratio → Should be higher

CHAPTER-3

CASH FLOW STATEMENT

Points to Remember:

1. First decide the nature of enterprise it is financial or Non-Financial.
2. For Calculating depreciation, check the Balance Sheet to find out that values of assets are given at net value (i.e., written down value) or at Gross Block (Shown Accumulated dep. A/c also). There after attempt question according to the instructions.
3. Current Investment or marketable securities is a part of Cash and Cash equivalent as per As-3 (revised.) if both are given separately than marketable securities will be consider as cash equivalent and remaining current Investment will be considered in Investing activities.
4. Bank overdraft and cash credit will be considered as financial activity rather than working capital changes in operating activities.
5. If main item belongs to a particular activity, then its sub-component also belongs to same activity. Ex. Bank overdraft is finance activity, then interest on bank overdraft is also finance activity.
6. Type of adjustment to be considered
   (a) Tax paid/provided during the year
   (b) Fixed assets having book value of ₹ (accumulated dep. ₹ ___) was sold at a loss/profit of ₹ _____
   (c) Interim dividend/proposed dividend of ₹ _____ paid during the year.
   (d) Additional debenture were issued/redeemed on _____.

Meaning: It is a statement that shows flow (Inflow or outflow) of cash and cash equivalents during a given period of time.

As per Accounting Standard-3 (Revised) the changes resulting in the flow of cash & cash equivalent arises on account of three types of activities i.e.,

(1) Cash flow from Operating Activities.

(2) Cash flow from Investing Activities.

(3) Cash flow from Financing Activities.

Cash: Cash comprises cash in hand and demand deposits with bank.

Cash equivalents: Cash equivalents are short-term, highly liquid investment that are readily convertible into known amount of cash and which are subject to an insignificant risk of change in the value e.g. short-term investment. Generally, these investments have a maturity period of less than three months.

Some examples of cash equivalent: Short-term deposits, marketable securities, treasury bills, commercial papers, money market funds, investment in preference shares if redeemable within three months provided that there is no risk of the failure of the company.

Some types of transaction which are considered movement between cash and cash equivalents are given below:

1. Cash deposited into bank.
2. Cash withdrawn from bank.
3. Sale of cash equivalent securities (e.g. Sale of short-term investment, sale of commercial papers)
4 Purchases of cash equivalent securities (e.g. Purchase of short-term investment, Purchases of Treasury bills).

Note 1: The above types of transaction are part of cash and cash equivalents, so these are included in opening and closing cash and cash equivalent only. So these types of transaction should not be included in cash flow from different activities like operating, investing, financing activities.

Note 2: A,B,C can have negative balance as well indicating cash used in operating, investing & financing activities respectively.

Objectives of Cash Flow Statement

1. To ascertain how much cash or cash equivalents have been generated or used in different activities i.e., operating/investing/financing activity.
2. To ascertain the net changes in cash and cash equivalents.
3. To assess the causes of difference between actual cash & cash equivalent and related net earnings/income.
4. To help in formulation of financial policies such as dividend policy, fixed assets policy, capital structure related policy.
5. To help in short-term financial planning.
6. To ascertain the liquidity of enterprises.

Limitations of Cash Flow Statement

1. Non cash transactions are not taken into consideration like shares or debentures issued to vendors, depreciation charged during the year.
2. It is a statement related with past data.
3. It is not used for judging the profitability of enterprise.
4. Accrual accounting concept is ignored in this statement e.g. credit sales, credit purchases, outstanding expenses, accrued income are not included.

Computation of Cash flows from different activities.

(1) Cash flow from operating activities : Operating activities are the main revenue generating activities of the enterprises. It also includes all those transactions which are not included in investing and financing activities.

Indirect Method of calculating the cash flow from Operating Activities : Under this method Net Profit before Tax and Extra-ordinary Item is the starting point for further calculations.

(A) Calculation of Net Profit before Tax and Extra-ordinary Items:

Difference between closing balance and opening balance of Balance in Statement of Profit & Loss A/c (In absence of this balance, difference of Reserve and surplus is taken as initial point.)

Add: 1. Dividend (proposed dividend of previous year paid) paid during the year ....

2. Interim Dividend paid during the year ....

3. Profit Transferred to Reserve ....

(If reserve of current year increased from previous year)

4. Provision for Taxation made during the year ....

5. Extra Ordinary Item.

If any Debited to Statement of Profit & Loss ....

Less: 1. Refund of Tax credited to Statement of P&L (................)

2. Extraordinary-item if any credited to Statement of P&L (................)

3. Reserves transferred back to statement of Profit and Loss (................)

Net Profit before Tax and Extra-ordinary items ....
....

* Extraordinary items: These items are not related to normal business operation.

FORMAT: CASH FLOW FROM OPERATING ACTIVITIES

		₹
I. Cash Flow from Operating Activities		
(A) Net Profit before Tax and Extraordinary Items (as per Working Note) Adjustment for Non-cash and Non-operating Items		–
(B) *Add:* **Items to be Added**		
— Depreciation	....	
— Goodwill, Patents and Trademarks Amortised	....	
— Interest on Bank Overdraft/Cash Credit	.....	
— Interest on Borrowings (Short-term and Long-term) and Debentures	....	
— Writing off Underwriting Commission/Share Issue Expenses	....	
— Loss on Sale of Fixed Assets	....	
— Increase in Provision for Doubtful Debts*	....	–
(C) *Less:* **Items to be Deducted**		
— Interest Income	(.....)	
— Dividend Income	(.....)	
— Rental Income	(.....)	
— Gain (Profit) on Salt of Fixed Assets	(.....)	
— Decrease in Provision for Doubtful Debts*	(.....)	(–)
(D) **Operating Profit before Working Capital Changes (A + B - C)**		–
(E) *Add:* **Decrease in Current Assets and Increase in Current Liabilities**		
— Decrease in Inventories (Stock)	....	
— Decrease in Trade receivables (Debtors/Bills Receivable)	....	
— Decrease in Accrued Incomes	....	
— Decrease in Prepaid Expenses	....	
— Increase in Trade Payables (Creditors/Bills Payable)	....	
— Increase in Outstanding Expenses	....	
— Increase in Advance Incomes	....	–
(F) *Less:* **Increase in Current Assets and Decrease in Current Liabilities**		

— Increase in Inventories (Stock)	(.....)	
— Increase in Trade Rceivables (Debtors/Bills Receivable)	(.....)	
— Increase in Accrued Incomes	(.....)	
— Increase in Prepaid Expenses	(.....)	
— Decrease in Trade Payables (Creditors/Bills Payable)	(.....)	
— Decrease in Outstanding Expenses	(.....)	
— Decrease in Advance Incomes	(.....)	(–)
(G) Cash Generated from Operations (D + E-F)		–
(H) *Less:* Income Tax Paid (Net of Tax Refund)		(....)
(I) Cash Flow before Extraordinary Items Less Extraordinary Itmes (+/-)		(–)
(U) CashFlowfrom(orUsedin) operating Activities		–

Cash Flow Statement

Illustration 1: From the following, calculate cash flow from operating activities.

Particulars	31.3.2022 (₹)	31.3.21 (₹)
Surplus (i.e. Balance in the statements of Profit & Loss)	69,000	84,000
Outstanding Salary	15,000	18,000
Prepaid Insurance	9,000	6,000
Patent	40,000	50,000
Inventory	14,000	6,000
Cash at Bank	10,000	13,000
Machinery	82,000	56,000
Provision for tax	35,000	30,000
General Reserve	44,000	34,000

Adjustments:

(i) A piece of machinery costing ₹ 50,000 on which depreciation of ₹ 20,000 had been charged was sold for ₹ 10,000. Depreciation charged during the year was ₹10,000.

(ii) Income tax paid during the year ₹ 23,000.

(iii) Divided paid during the year was ₹ 36,000.

Solution:

Dr. Provision for tax A/c Cr.

Particulars	₹	Particulars	₹
To Bank (tax paid)	23,000	By Balance b/d	30,000
To Balance c/d	35,000	By statement of P&L A/c (Provision made during the year)	28,000
	58,000		58,000

(W.N.I.)

Calculation of net profit before tax and extraordinary item

	Difference of surplus (i.e.) Balance in P&L A/c	(15,000)
Add:	Provision for tax	28,000
	Transfer to Reserve	10,000
	Divided paid	36,000
		59,000

Cash flow from operating activities for the yea ended 31st March, 2022

Particulars	₹	₹
Net profit before tax and extra-ordinary items (W.N.I)		59,000
Add: Adjustment for non-cash and non-operating items		
Dep. on Machinery	10,000	
Loss on sale of machinery (50,000 – 20,000 – 40,000)	20,000	
Patent written of (50,000 – 40,000)	10,000	40,000
Operating profit before working capital changes		99,000
Less: Increase in current Assets & decrease in current Liabilities		
Outstanding Salary	3,000	
Prepaid Insurance	3,000	
Inventory	8,000	14,000
Cash flow from operating activities before tax		85,000
Less: Tax paid		23,000
Net cash flow from operating activities		62,000

2. Cash Flow from Investing Activities

Investing activities are those activities which are related to the acquisition (buying) and disposal (selling) of fixed assets and investment (other than cash equivalents). It also includes income from fixed assets and investment like rent received, interest received on investment, dividend received on investment in shares and mutual funds.

Inflows of Cash: (Plus items)	Outflows of Cash (minus items)
1. Cash Received from sale of Fixed Assets. 2. Cash Received from sale of Investment. Excluding Marketable Securities 3. Cash Received from sale of intangible Assets like Patents. 4. Interest Received, 5. Dividend Received, 6. Rent Received	1. Cash paid for purchase of fixed assets. 2. Cash paid for purchase of investment. Excluding Marketable Securities 3. Cash paid for purchase of intangible Fixed assets like goodwill, patents and copy rights.

For the calculation of sale or purchase of fixed assets and investment, the following accounts are prepared:

1. Fixed Assets Account 2. Investment Account

Fixed Assets Account: Fixed assets accounts may be prepared by two methods:

(a) At written down value method (when provision for depreciation account/ accumulated depreciation account is not maintained):

Fixed Assets Account (at written down value).

Dr. Cr.

Date	Particulars		Date	Particulars	
	To Balance b/d	....		By BankA/c (Sale of investment)	......
	To BankA/c (Additional Purchase)	....		By Loss on sale of fixed assets	......
	To Profit on sale of fixed assets A/c	....		By Depreciation charged during the year A/c	......
				By Balance c/d	
		......			.....

(b) Fixed Assets (at cost); When provision for depreciation account or accumulated depreciation account has been separately maintained. In this method two separate accounts named Fixed Assets Account and Provision for Depreciation account are maintained

Fixed Assets Account (at original cost)

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	....		By BankA/c (Sale of investment)	......
	To Bank A/c (Additional Purchase)	....		By Provision for Depreciation A/c (Dep. on fixed assets sold)	....
	To Profit on sale of fixed assets A/c	....		By Loss on sale of fixed assets A/c	......
				By Balance c/d	......
		......			.....

Provision for Depreciation Account

Dr. Cr.

Date	Particulars		Date	Particulars	
	To Fixed Assets A/c (Total Depreciation provide till the date of sale on Fixed assets sold)	....		By Balance b/d	....
	To balance c/d	....		By Statement of Profit & Loss A/c (Depreciation charged on fixed assets during the current year including the part sold)	....
		....			....

Preparation of Investment Account:

Dr. Investment Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	....		By Bank A/c	....
	To Bank A/c(Additional Purchase)	....		(Sale of investment)	....
	To Profit on sale of investment A/c	....		By Loss on sale of Investment A/c	
				By balance c/d	
		....			....

Illustration2. From the following information calculate cash flow from investing activities:

Particulars	31-03-2014 (₹)	31-03-2015 (₹)
Machinery (at Cost)	5,00,000	5,50,000
Accumulated Depreciation	1,00,000	1,20,000
Patents	2,00,000	1,20,000
Goodwill	1,50,000	1,00,000
Investment	2,50,000	5,00,000

Additional Information

(i) During the year, a machine costing ₹50,000 with its accumulated depreciation of ₹ 25,000 was sold for ₹ 20,000.

(ii) Patents were written off to the extent of ₹60,000 and some patents were sold at a profit of ₹10,000.

(iii) 40% of the investments held in the beginning of the year were sold at 10% Profit.

(iv) Interest received on investment ₹ 25,500.

(v) Dividend received on investment ₹ 8,500.

(vi) Rent received ₹ 5,000.

Solution:

Cash Flow from Investing Activities

Particulars	₹
Proceeds from sale of machinery	20,000
Proceeds from sale of investment	1,10,000
Proceeds from sale of Patents	30,000
Cash paid for purchase of machinery	(1,00,000)
Cash paid for purchase of Investment	(3,50,000)
Interest Received	25,500
Dividend Received	8,500
Rent Received	5,000
Net Cash Used in Investing Activities	(2,51,000)

Working Notes:

Investment Account

Dr. Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	2,50,000		By Bank A/c	1,10,000
	To Profit on sale of InvestmentA/c	10,000		(Sale of investment)	
				By balance c/d	5,00,000
	ToBankA/c B/F) (Additional Purchase)	3,50,000			
		6,10,000			6,10,000

Dr. Machinery Account (at original cost) Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Balance b/d	5,00,000		By Bank A/c	20,000
	To Bank A/c (additional			(Sale of investment)	
	Purchase) (B/F)	1,00,000		By Provision for Depreciation A/c	25,000
				(Dep. on Machinery sold)	
				By Loss on sale of	5,000
				Machinery Ac	
				By balance c/d	5,50,000
		6,00,000			6,00,000

Dr. Provision for Depreciation Account Cr.

Date	Particulars	₹	Date	Particulars	₹
	To Machinery A/c	25,000		By Balance b/d	1,00,000
	(Total Depreciation on Machinery sold)			By Statement of Profit & Loss	45,000
				(Depreciation charged on machinery during the current year) (B/F)	
	To Balance c/d	1,20,000			
		1,45,000			1,45,000

Patents Account

Dr. Cr.

Date	Particulars		Date	Particulars	
	To Balance b/d	2,00,000		By Bank A/c	30,000
	To Profit on sale of			(B/F - Sale of Patents)	
	patents A/c	10,000		By Statement of Profit	60,000

				& Loss (Written off)	
				By balance c/d	1,20,000
		2,10,000			2,10,000

3. Cash Flow from Financing Activities

Financing activities are those activities that result in the change in size and composition of the share capital (equity and preference) and borrowed fund of the business enterprises. Generally cost related to these funds are also included in financing activities like interest paid on loans and debentures and dividend paid on equity and preference share capital.

Inflows of Cash: (Plus items)	Outflows of Cash (minus items)
1. Proceeds from Issue of equity shares capital. 2. Proceeds from Issue of preference share capital. 3. Proceeds from taking long-term loan and issue of debentures. 4. Proceeds from Bank Overdraft and Cash credit.	1. Amount paid for repayment of long-term loan. 2. Redemption of Preference share capital in cash. 3. Redemption of Debenture in cash. 4. Buy back of Equity shares (Extra-Ordinary Item) 5. Payment of Bank Overdraft and Cash Credits. 6. Interest paid on long term loan and debentures 7. Final Dividend paid. 8. Interim dividend paid. 9. Dividend paid on Preference Shares.

Illustration 3. From the following information, calculate the net cash flow from Financing Activities.

Particulars	31-3-2017 (₹)	31-3-2018 (₹)
Equity Share Capital	10,00,000	16,00,000
9% Debentures	1,50,000	1,00,000
Dividend Payable	—	50,000
10% Preference Share Capital	2,00,000	3,00,000

Additional Information

1. Interest paid on Debentures ₹ 12,500.
2. During the year 2017-2018, company issued bonus shares to equity shareholders in the ratio of 2:1 by capitalizing reserve.
3. The interim dividend of ₹ 75,000 has been paid during the year.
4. 9% Debentures were redeemed at 5% premium.
5. Proposed equity dividend for the years ended 31/3/2017 and 31/3/2018 ended ₹ 3,00,000 and ₹ 150000 respectively.

Solution:

Cash Flow from Financing Activities

Particulars	₹
Proceeds from Issue of Equity Share Capital	1,00,000
Proceeds from Issue of 10% Preference Share Capital	1,00,000
Cash paid for Redemption of 9% Debentures (50,000 × 105%)	(52,500)
Interest paid on Debentures	(12,500)
Interim Dividend paid	(75,000)
Final Dividend paid (3,00,000-50,000)	(2,50,000)
Net Cash Used in Financing Activities	(1,90,000)

Note:

1. Bonus shares worth ₹ 5, 00,000 issued to equity shareholder are not to be shown in the cash flow statement because there is no flow of cash by this activity.
2. As per the provisions of As-4, dividend proposed by the Directors of the company for the current year Rs. 1,50,000 will be shown in the notes to accounts as contingent liability. Dividend of the previous year of Rs. 3,00,000 has been declared and approved in the annual general meeting of shareholders for current year will be shown as appropriation of profits of current year so will be added to determine the net profit before dividend, taxes and extraordinary item and as an outflow from the firm under the finacing activity.
3. Previous year proposed dividend- unpaid dividend = final dividend paid during the current year is cash used in financing activities.

Financing Business Enterprise Transaction Treatment in Cash Flow Statement

Financing business enterprises are the business enterprises which deal in finance like investment companies, mutual fund house, banks. These enterprises purchases and sale of securities as their stock, so it is treated as operating activities and interest received, dividend received and interest paid are considered as routine business activities and included in their operating activities.

Illustration 4: Prepare cash flow statement on the basis of information given in the Balance Sheet of Relga its, as at 31st March, 2019 & 31 March 2020

Particulars	Note no.	31.3.19	31.3.320
I. EQUITY AND LIABILITIES			
1. Shareholder's funds			
(a) Share capital	1	2,00,000	2,50,000
(b) Reserve and Surplus		50,000	70,000
2. Non-current Liabilities Long term Borrowing	2	1,00,000	80,000
3. Current Liabilities			
(a) Trade payable	3	60,000	1,60,000
(b) Other current liabilities	4	25,000	20,000
Total		4,35,000	5,80,000

II. ASSETS			
1. Non-Current Assets			
(a) Fixed Assets			
(i) Tangible	5	1,50,000	2,00,000
(ii) Intangible	6	10,000	2,000
(b) Long term Loans & Advances		1,00,000	1,30,000
2. Current Assets			
(a) Inventors		70.000	90,000
(b) Trade Receivables		40,000	60,000
(c) Cash & cash equivalent		65,000	98,000
Total		4,35,000	5,80,000

Note to Accounts

Note no.	Particulars	31.3.2019	31.3.2020
1.	Reserve & Surplus	50,000	70,000
2.	Long term Borrowing 12% Debentures	1,00,000	80,000
3.	Trade payable creditors	40,000	60,000
	Bills payable	20,000	1,00,000
		60,000	1,60,000
4.	Other current liabilities outstanding exp.	25,000	20,000
5.	Tangible Fixed Assets Machinery	2,00,000	2,60,000
	Less: Provision for Depreciation	50,000	60,000
		1,50,000	2,00,000
6.	Intangible Fixed Assets Goodwill	10,000	2,000

Adjustment: 1. During the year a piece of machinery with a book value of ₹ 40,000, provision for Depreciation on it ₹ 10,000 was sold at a loss of 50% on book value.

2. Debentures were redeemed on 31st March, 2020

Sol.

Dr. Machinery A/c Cr.

Particulars	₹	Particulars	₹
To Balance b/d	2,00,000	By Bank A/c	15,000
To Bank A/c	1,00,000	By P&L A/c	15,000
		By provision for Dep.	10,000
		By Balance c/d	2,60,000
	3,00,000		3,00,000

Dr. Provision for Dep. A/c Cr.

Particulars	₹	Particulars	₹
To Machinery A/c	10,000	By Balance b/d	50,000
To Balance c/d	60,000	By Statement of profit & Loss (Dep.)	20,000
	70,000		70,000

Cash flow statement for the year ended 31st March, 2020

Particulars	₹	₹
Profit Before tax & extraordinary items (70,000 – 50,000)	20,000	
Adjustment for non-cash & non-operating items		
Loss on sale of Machinery	15,000	
Dep. on Machinery	20,000	
Goodwill written off	8,000	
Interest on Deb.	12,000	

Operating profit before working capital changes	75,000	
Changes in working capital		
Increase in creditors	20,000	
Increase in Bills payable	80,000	
Decrease in o/s exp.	(5,000)	
Increase in inventories	(20,000)	
Increase in trade receivables	(20,000)	
I net cash flow from operating activities		1,30,000
Investing activities		
Sale of Machinery	15,000	
Purchase of Machinery	(1,00,000)	
Loans Advanced	(30,000)	
II cash used in investing activities		(1,15,000)
Financing activities		
Issue of share	50,000	
Debentures Redeemed	(20,000)	
Interest on Debentures	(12,000)	
III net cash flow from financing activities		18,000
Net cash in flow during the year (I + II + III)		33,000
IV cash & cash equivalent in the beginning		65,000
V cash & cash equivalent at the end		98,000

Prepare cash flow statement from the balance sheet as at 31st March, 2021

Illustration 5.

Particulars	Note no.	2021 ₹	2020 ₹
1. Equity and liabilities			
(i) Shareholders' fund			
Share capital		4,00,000	4,00,000
Reserve and surplus	1	2,20,000	1,20,000
2. Non-current liabilities			
Long-term borrowing	2	4,80,000	3,80,000
3. Current liabilities			
(a) Short-term borrowing	3	60,000	40,000
(b) Trade payable		1,40,000	80,000
(c) Short-term provisions	4	1,00,000	80,000
Total		14,00,000	11,00,000
II Assets			
1. Non-current assets			
Fixed Assets			
(i) Property, Plant, Equipment	5	8,60,000	7,40,000
(ii) Intangible assets	6	20,000	30,000
2. Current Assets			
(i) Inventories		2,00,000	1,10,000
(ii) Trade Receivables		1,80,000	1,00,000
(iii) Cash and cash equivalent		1,10,000	80,000
(iv) Other current assets		30,000	40,000
		14,00,000	11,00,000

Notes to Accounts

Particulars	2021	2020
1. Reserve and surplus		
General reserve	70,000	40,000
Balance in statement of profit & loss	1,50,000	80,000
	2,20,000	1,20,000
2. Long term borrowing		
10% debenture	3,00,000	2,00,000
Mortage loan	1,80,000	1,80,000
	4,80,000	3,80,000
3. Short-term borrowing		
Bank overdraft	44,000	20,000
Cash credit	16,000	20,000
4. Short-term provision	60,000	40,000
Provision for tax	1,00,00	80,000
5. Fixed assets- Tangible		
Land and building	2,80,000	5,20,000
Machinery	5,80,000	2,20,000
6. Fixed assets- Intangible	8,60,000	7,40,000
Branding	20,000	30,000
7. Other current assets Accrued income	30,000	40,000

Additional Information:

(i) Gain on sale of land and building ₹40,000

(ii) Depreciation on machinery @10% p.a. on last year balance

(iii) Interest paid ₹50,000.

Solution: Net profit before tax and extraordinary items:

₹

Net profit (1,50,000 – 80,000)	70,000
Add: General Reserve (70,000 – 40000)	30,000
Provision for tax	1,00,000
Net Profit before tax & extraording ary items	2,00,000

Land & Building A/C

Dr. **CR.**

Particulars	₹	Particular	₹
To Balance b/d	5,20,000	By bank A/c (Bal. figure)	2,80,000
To statement of profit	40,000	By balance dd	2,80,000
& loss (Gain)			
	5,60,000		5,60,000

Machinery A/C

Particulars	₹	Particular	₹
To Balance b/d	2,20,000	By Dep.	22,000
To bank (bal. figure)	3,82,000	By balance dd	5,80,000
	6,02,000		6,02,000

Cash flow statement for the year ended 31st match, 2021

Particular	**Details**	**Amount**
	₹	₹
(A) Cash flow from operating activities		2,00,000
Net profit before tax and extra ordinary items		
Adjustment for non-cash and non-operating items		
Add: Depreciation	22,000	
Branding written off	10,000	
Interest paid	50,000	

Less: Gain on sale of land and building	(40,000)	
Operating profit before working capital charges		2,42,000
Add: Increase in current liabilities		
Trade payable	60,000	
Accrued income	10,000	
Less: Increase in current assets		
Inventory	(90,000)	
Trade Receivables	(80,000)	(1,00,000)
		1,42,000
Less: tax paid		(80,000)
Net cash flow from operating activities		62,000
(B) Cash flow from investing activities		
sale of land and building	2,80,000	
Purchase of machinery	(3,82,000)	
Net cash used in investing activities	(1,02,000)	(1,02,000)
(C) Cash flow financing activities		
Proceeds from bank overdraft	24,000	
Proceeds from debenture	1,00,000	
Payment of cash credit	(4,000)	
Interest paid	(50,000)	
Net cash flow from financing activities	70,000	70,000
(D) Net increase in cash and cash equivalent (A+B+C)		30,000
(E) Cash and cash equivalent (opening balance)		80,000
(F) Cash and cash equivalent (closing balance)		1,10,000

Illustration 6: From the following information, complete the Cash flow Statement of RK Ltd.

Cash flow Statement
For the year ended on 31-3-2017

Particulars	₹	₹
A. Cash flow from operating Activities:		
Net profit before tax and Extraordinary items	....	
Adjustment for Non-cash and non operating items:		
Depreciation	....	
Loss on sale of Machinery	....	
Operating profit before working capital changes	....	
Adjustment for changes in working Capital:		
Decrease in Trade Payables	(8,000)	
Increase in Inventory	(........)	
Cash generated from operations before tax & extraordinary items	50,000	
Less: Income tax paid	(.......)	
Net cash flow from operating activities:		....
B Cash flow from Investing Activities:		
Purchase of Machinery	(.......)	
Sale of Machinery	....	
Net cash flow from Investing Activities		....
C .Cash flow from Financing Activities:		
Proceeds from Issue of Shares	....	
Net cash flow from Financing Activities		....
(A+B+C)net Increase in cash & Cash Equivalents during the year		....
Add: Cash & cash equivalents at the beginning of the period		....
Cash & cash equivalents at the end of the period		....

Notes to Account

Particulars	31-3-2017 (₹)	31-3-2016 (₹)
Note 1. Reserve & Surplus		
General Reserve	55,000	40,000
Balance in Statement of Profit & Loss	70,000	50,000
	1,25,000	90,000
Note 2. Cash and Cash equivalents Cash at Bank	52,000	37,000
	52,000	37,000
Note 3. Short term Provisions		
Provision for Taxation	25,000	20,000
	25,000	20,000

Additional Information:

1. Depreciation charges on Building for the year 2016- 17 was ₹ 10,000.
2. During the year 2016-17, machinery of ₹ 1,38,000 was purchased.
3. A part of machinery costing ₹ 20,000 with accumulated depreciation of ₹ 6,500 was sold for ₹ 8,500.
4. Income tax paid during the year 2016-17 was ₹ 18,000.

Solution:

Cash flow Statement
For the year ended on 31-3-2017

Particulars	₹	₹
B. Cash flow from operating Activities:		
Net profit before tax and Extraordinary items	58,000	
Adjustment for Non-cash and non-operating items:		
Depreciation	10,000	
Loss on sale of Machinery	5,000	
Operating profit before working capital changes	73,000	
Adjustment for charges in working Capital:		
Decrease in Trade Payables	(8,000)	
Increase in Inventory	(15,000)	
Cash generated from operations before tax & extraordinary items	50,000	
Less: Income tax paid	(18,000)	
Net cash flow from operating activities:		32,000
B Cash flow from Investing Activities:		
Purchase of Machinery	(1,38,000)	
Sale of Machinery	8,500	
Net cash flow from Investing Activities		(1,29,500)
C .Cash flow from Financing Activities:		
Proceeds from Issue of Shares	1,12,500	
Net cash flow from Financing Activities		1,12,500
(A+B+C)net Increase in cash & Cash Equivalents during the year		15,000
Add: Cash & cash equivalents at the beginning of the period		37,000
Cash & cash equivalents at the end of the period		52,000

Working Notes

. Calculation of Net Profit before tax and extraordinary items:

	₹
Difference in Balance in Statement of P&L (70,000-50,000)	20,000
Add: Transfer to General Reserve	15,000
Provision for Taxation	23,000
	58,000

2. Provision for taxation account

Dr. **CR.**

Particulars	₹	**Particular**	₹
To Bank a/c (tax paid)	18,000	By balance b/d	20,000
To Balance c/d	25,000	By statement of P&L (balancing figure) (Provision made during the year)	23,000
	43,000		43,000

Note: 1. There is no need to prepare machinery A/c as both purchase and Sale value are given in the question.

2. Proceeds from issue of shares have been calculated by moving backwards from the figure of net increase in cash and cash equivalent i.e.,

i.e. 15,000 = ₹32,000 + (1,29,500) + cash flow from financing activity.

Illustration 7: Prepare cash flow statement from the following information.

Balance sheet xits

Particulars	Note no.	31.3.22	31.3.21
I. EQUITY AND LIABILITIES			
1. Shareholder's funds			
(a) Share capital		3,20,000	2,40,000
(b) Reserve & Surplus	1	1,36,000	1,24,000
2. Non-current liabilities Long-term Borrowing	2	2,00,000	1,20,000
3. Current liabilities			
(a) Trade payable		88,000	68,000
(b) Other current liabilities short-term provision	3	12,000	8,000
		7,56,000	5,60,000
II. ASSETS			
1. Non-Current Assets			
(a) Fixed Assets			
(i) Tangible Assets	4	3,36,000	2,64,000
(ii) Intangible Assets	5	56,000	80,000

(b) Non-Current Investment	6	64,000	24,000
2. Current Assets			
(a) Inventories		40,000	32,000
(c) Trade Receivable		1,56,000	64,000
(c) Cash & cash equivalent		1,04,000	96,000
Total		7,56,000	5,60,000

Note to Accounts

Note no.	Particulars	31.3.22	31.3.21
1.	Reserve & Surplus		
	Balance in statement of P&L A/c (Surplus)	56,000	52,000
	General Reserve	80,000	72,000
		1,36,000	1,24,000
2.	Long term Borrowing 12% Debentures	2,00,000	1,20,000
3.	Short term provision Provision for tax	13,000	8,000
4.	Tangible Assets Machinery	3,36,000	2,64,000
5.	Intangible Assets patents	56,000	80,000
6.	Non-current Investment 10% Govt. Bonds	64,000	24,000

Additional Information

(a) Investment costing ₹ 24,000 were sold for ₹ 16,000.

(b) Dep. on Machinery ₹ 48,000.

(c) Tax paid ₹ 4,800.

(d) Debenture were issued and investments were purchased & sold on March 31st, 2022.

Dr. 10% Govt. Bonds A/c Cr.

Particulars	₹	Particulars	₹
To Balance b/d	24,000	By Bank A/c	16,000
To Bank A/c (Purchase)	64,000	By loss on sale	8,000
		By balance c/d	64,000
	88,000		88,000

Dr.		Machinery A/c	Cr.
Particulars	₹	Particulars	₹
To Balance b/d	2,64,000	By Dep. A/c	48,000
To Bank A/c (Purchase)	1,20,000	By Balance c/d	3,36,000
	3,84,000		3,84,000

Dr.		Provision taxation A/c	Cr.
Particulars	₹	Particulars	₹
To Bank A/c	4,800	By Balance b/d	8,000
To Balance c/d	12,000	By statement of P&L A/c	8,800
	16,800		16,800

Cash flow statement for year ended 31st March, 2022

Particulars	₹	₹
Cash flow from operating activities		
Net profit before tax & extraordinary items (W.N.)	20,800	
Adjustment for non-cash & non-operating items		
Add: Depreciation	48,000	
Patents	24,000	
Loss on sale of investment	8,000	
Int on 12% Debentures	14,400	
Less: Interest on 10% Govt. Bonds	(24,00)	
	1,12,800	
Operating profit before working capital changes		
Less: Increase in inventories	(8,000)	
Increase in trade receivable	(92,000)	
Add: Increase in trade payable	20,000	
	32,800	
Less: tax paid	4,800	
I. Net cash flow from operating Activities		28,000

Cash flow from financing activities		
Proceeds from sale of investment	16,000	
Interest on investment	2,400	
Purchase of investment	(64,000)	
Purchase of Machinery	(1,20,000)	
II. Net cash used in investing activities		(1,65,600)
Cash flow from financing activities		
Issue of share capital	80,000	
Issue of Debenture	80,000	
Interest on Debenture	(14,400)	
III. Net cash flow from financing activities		1,45,600
IV. Net increase in cash &cash equivalent (I + II + III)		8,000
V, Cash & cash equivalent in the beginning		96,000
VI. Cash & cash equivalent at the end		1,04,000

W.N. Net profit before tax & extraordinary item:	₹
Profit for the year (56,000 – 52,000)	4,000
Add: transfer to Reserve (80,000 – 72000)	8,000
Add: provision for tax	8,800
	20,800

Illustration 8: Following was the Balance of vasudha Ltd. an on 31st March 2017.

Particulars	Note No.	31-3-2017 (₹)	31-3-2016 (₹)
Equity & Liabilities			
(1) Shareholders Funds			
(a) Share Capital		20,00,000	15,00,000
(b) Reserves and Surplus	1	50,00,000	3,00,000
(2) Non-current Liabilities			
Long term borrowings		3,00,000	2,00,000
(3) Current Liabilities			
(a) Trade payables		1,50,000	2,00,000

(b) Short term provisions	2	70,000	60,000
Total		**30,20,000**	**22,60,000**

Assets			
(1) Non-Current Assets			
(a) Fixed Assets			
(i) Tangible assets	3	19,00,000	15,00,000
(ii) Intangible assets	4	4,70,000	2,70,000
(2) Current Assets			
(a) Inventories		2,50,000	1,60,000
(b) Trade Receivables		2,10,000	2,10,000
(c) Cash and Cash Equivalents		1,90,000	1,20,000
Total		**30,20,000**	**22,60,000**

Notes to Accounts :

S. No.	Particulars	As on 31-3-2017 (₹)	As on 31-3-2016 (₹)
1.	Reserve and Surplus		
	Surplus (Balance in Statement of Profit and Loss)	5,00,000	3,00,000
2.	Short term provisions		
	Provision for tax	70,000	60,000
3.	Tangible Assets		
	Machinery	27,00,000	21,00,000
	Accumulated Depreciation	(8,00,000)	(6,00,000)
4.	Intangible Assets		
	Goodwill	4,70,000	2,70,000

(Prepare a Cash Flow Statement after taking into account the following adjustment)

During the year a piece of machinery costing ₹ 30,000 on which accumulated depreciation was ₹ 6,000, was sold for ₹ 20,000.

Cash Flow Statement of Vasudha Ltd.
For the year ended 31st March, 2017 As per As-3 (Revised)

Particulars	Details (₹)	Amt (₹)
<u>Cash Flows from Operating Activities:</u>		
Net Profit before tax & extraordinary items	2,00,000	
Add: Provision for Tax	70,000	
<u>Add: Non cash and non-operating charges</u>		
Depreciation on machinery	2,06,000	
Loss on sale of machinery	4.000	
Operating profit before working capital changes	4,80,000	
<u>Less: Increase in Current Assets</u>		
Increase in inventories	(90,000)	
<u>Less: Decrease in Current Liabilities</u>		
Decrease in trade payables	(50,000)	
Operating profit after working capital changes	3,40,000	
Less: Tax Paid	(60,000)	
Cash generated from Operating Activities		2,80,000
<u>Cash flows from Investing Activities :</u>		
Purchase of Machinery	(6,30,000)	
Sale of machinery	20,000	
Purchase of Goodwill	(2,00,000)	
Cash used in investing activities		(8,10,000)
<u>Cash flows from Financing Activities :</u>		
Issue of share capital	5,00,000	
Money raised from long term borrowings	1,00,000	

Cash from financing activities		6,00,000 70,000
Net increase in cash & cash equivalents:		
Add: Opening balance of cash & cash equivalents:		1,20,000
Closing Balance of cash & cash equivalents:		1,90,000

Machinery A/c

Dr. Cr.

Particulars		Particulars	
Balance b/d	21,00,000	Bank A/c	20,000
Cash/Bank A/c	6,30,000	Accumlated Dep. A/c	6,000
		Statement of P/L	4,000
		Balance c/d	27,00,000
	27,30,000		27,30,000

Dr.I Accumlated Dep. A/c Cr.

Particulars		Particulars	
Machinery A/c	6,000	balance b/d	6,00,000
balance c/d	8,00,000	statement of P/L	2,06,000
	8,06,000		8,06,000

Illustration 9. From the following Balance Sheet of B.C.R. prepare Cash Flow Statement:

BALANCE SHEET OF B.C.R. LTD. as at 31 st March, 2018

Particulars	Note No.	31st March, 2018 (Rs.)	31 March 2017(Rs.)
EQUITY AND LIABILITIES			
1. Shareholders' Funds			
(a) Share Capital		7,00,000	5,00,000.

(b) Reserve end Surplus: Surplus, i.e., Balance in statement of Profit & Loss	1	3,50,000	2,00,000
2. Non-Current Liabilities			
Bank Loan		50,000	1,00,000
3. Currant Liabilities			
(a) Trade Payables (Creditors)		52,000	55,000
(b) Short-term Provisions		50,000	30,000
Total		12,02,000	8,85,000

II. ASSETS			
1. Non-Current Assets			
(a) Fixed Assets:			
(i) Tangible Assets: Equipment		5,00,000	5,00,000
(ii) Intangible Assets: Patents		95,000	1,00,000
(b) Non-current Investments		1,00,000	—
2. Current Assets			
(a) Inventories (Stock)		1,30,000	55,000
(b) Trade Receivables (Debtors)		1,47,000	80,000
(c) Cash and Cash Equivalents: Bank		2,30,000	1,50,000
Total		12,02,000	8,85,000

Note to Accounts

Particulars	31st March, 2018 (₹)	31st March 2017 (₹)
1. Short-term Provisions Provision for Tax	50,000	30,000

Additional Information:

1. Proposed dividend for the year ended 31st March, 2017: ₹ 70,000 was declared and paid in the year ended 31st March, 2018.
2. During the year Equipment costing ₹ 1,00,000 was purchased. Loss on sale of Equipment amounted to ₹ 12,000. ₹ 18,000 depreciation was charged on Equipment.

CASH FLOW STATEMENT for the year ended 21st March, 2018

Particulars	₹	₹
(a) Cash Flow from Operating Activities		
Net Profit before Tax and Extraordinary Items (WN 1)	2,70,000	
Add: Non-cash and Non-operating Expenses:		
Depreciation on Equipment	18,000	
Patents amortised	5,000	
Loss on sale of Equipment	12,000	
Operating Profit before Working Capital Changes	3,05,000	
Adjustment for Change in Current Assets and Current' Labilities:		
Trade Receivables (Debtors)	(67,000)	
Inventories (Stock)	(75,000)	
Trade Payables (Creditors)	(3,000)	
Cash Generated from Operations	1,60,000	
Less: Tax Paid	30,000	
Cash Flow from Operating Activities		1,30,000
(b) Cash Flow from Investing Activities		
Proceeds from Sale of Equipment (WN 2)	70,000	
Equipment Purchased	(1,00,000)	
Investment Purchased	(1,00,000)	
Cosh Used in Investing Activities		(1,30,000)
(c) Cash Flow from Financing Activities		
Cash-Proceeds from Issue of Equity Shares	2,00,000	
Repayment of Bank Loan	(50,000)	
Dividend Paid	(70,000)	
Cash Flow from Financing Activities		80,000
Net Increase in Cash and Cash Equivalents (A + B C)		80,000
Add: Opening Balance of Cash and Cash Equivalents		1,50,000
(d) Closing Balance of Cash and Cash Equivalents		2,30,000

Working Notes:

1. Calculation of Net Profit before Tax and Extraordinary Items: ₹

Balance as per Statement of Profit and Loss	1,50,000
Add: Provision for Tax (current year)	50,000
Dividend paid during 2017-18	70,000
Net Profit before Tax and Extraordinary Items	2,70,000

2. Calculation of amount of Sale of Equipment:

Equipment Account

Particulars	₹	Particulars	₹
To Balance b/d	5,00,000	By Depreciation A/c	18,000
To BankA/c	1,00,000	By BankA/c (Sale)—Balancing Figure	**70,000**
		By Loss on Sale of Equipment A/c (Statement of Profit and Loss)	12,000
		By Balance c/d	5,00,000
	6,00,000		6,00,000

Illustration 10: Following are the Balance Sheet of z its.

Particulars	**Note no.**	**31.3.22**	**31.3.21**
I. EQUITY AND LIABILITIES			
1. Shareholder's funds:			
(a) Share capital	1	4,50,000	4,50,000
(b) Reserve & Surplus	2	4,78,000	3,56,000
2. Non-Current Liabilities Long-term Borrowing	3	1,70,000	
3. Current Liabilities			
(a) Trade Payable		1,09,000	2,03,000
(b) Short-term Provision	4	35,000	40,000
Total		12,42,000	10,49,000
II. ASSETS			
1. Non-Current Assets Fixed Assets			
(a) Tangible Assets	5	3,20,000	4,00,000

(b) Intangible Assets	6	60,000	50,000
2. Current Assets			
(a) Current Investments		70,000	78,000
(b) Inventory		1,70,000	2,15,000
(c) Trade Receivables		4,55,000	2,10,000
(d) Cash at Bank		1,67,000	96,000
Total		12,42,000	10,49,000

Note s to Accounts

Note no.	Particulars	31.3.22	31.3.21
1.	Share capital		
	Equity share capital	2,50,000	2,50,000
	10% Preference share capital	2,00,000	2,00,000
		4,50,000	4,50,000
2.	Reserve & Surplus		`
	Retained Earning	4,78,000	3,56,000
3.	Long-term Borrowing		
	9% Debenture	1,70,000	
4.	Short-term Provision		
	Provision for taxation	35,000	40,000
5.	Tangible Assets		
	Land	1,40,000	2,50,000
	Plant & Machinery	1,80,000	1,50,000
		3,20,000	4,00,000
6.	Intangible Assets		
	Goodwill	60,000	50,000

Additional Information

1. Loss on sale of land ₹ 40,000
2. Interim dividend on equity shares paid @ 10%
3. Debenture were issued at the beginning of the year.
4. Tax paid ₹ 30,000 during the year.

Solution:

Dr. Provision for taxation A/c Cr.

Particulars	₹	Particulars	₹
To Bank A/c	30,000	By Balance b/d	40,000
To Balance c/d	35,000	By Statement of P&L A/c	25,000
	65,000		65,000

Dr. Land A/c Cr.

Particulars	₹	Particulars	₹
To Balance b/d	2,50,000	By Loss on sale	40,000
		By Bank (sale) (B/F)	70,000
		By Balance c/d	1,40,000
	2,50,000		2,50,000

W.N.I Net profit before tax & extraordinary items: ₹

Difference in the surplus i.e. Balance in	
statement of P&L A/c (47,8000 – 3,56,000)	1,22,000
Add: Provision for tax	25,000
10% Pref. Dividend	20,000
Equity Dividend	25,000
	1,92,000

Cash flow statement for the year ended 31st March, 2022

Particulars	₹	₹
A. Cash flow operating activities		
Net profit before tax & extraordinary item (W.N.I.)	1,92,000	
Adjustment for non-cash non operating items		
Add: Loss on sale of land	40,000	
Interest on debenture	15,300	
	2,47,300	
Operating profit before working capital changes		
Add: Decrease in Current Assets Inventory	45,000	
	2,92,300	

Less: Increase in Current Assets & decrease in Current Liabilities		
Trade Receivable 2,45,000		
Trade Payables 94,000	(3,39,000)	
	(46,700)	
Less: Tax paid	(30,000)	(76,700)
Net cash used in operating activities	(76,7000)	
B. Cash flow from Investing Activities		
Purchase of plant & Machinery (1,50,000 – 1,80,000)	(30,000)	
Purchase of Goodwill	(10,000)	
Sale of Land	70,000	
Net cash flow from Investing Activities	30,000	30,000
C. Cash flow from financing activities		
Issue of Debenture	1,70,000	
Interest on Debenture	(15,300)	
Preference share dividend	(20,000)	
Equity share dividend	(25,000)	
Net cash flow from financing activities	1,09,700	1,09,700
D. Net increase in cash & cash equivalent (A + B + C)		63,000
E. Cash & cash equivalent in the beginning		
Current Investment 78,000		
Cash at Bank 96,000		1,74,000
F. Cash & cash equivalent at the end (1,67,000 + 70,000)		2,37,000

Illustration 11: From the Balance Sheet of T Ltd. & additional information as at 31st March, 2022. Prepare a cash from statement.

Balance Sheet as at 31st March, 2022

Particular	Note no.	31.3.22	31.3.21
I. EQUITY AND LIABILITIES			
1. Shareholder’s funds			

(a) Share capital		28,00,000	21,00,000
(b) Reserve & Surplus	1	6,00,000	5,00,000
2. Non-current Liabilities Long-term Borrowing	2	8,00,000	5,00,000
3. Current Liabilities			
(a) Trade payable		1,50,000	1,00,000
(b) Short-term provision	3	76,000	56,000
Total		44,26,000	32,56,000
II. ASSETS			
1. Non-current Assets Fixed Assets			
(a) Tangible Assets (Machinery)		27,00,000	20,00,000
(b) Intangible Assets		8,00,000	7,00,000
2. Current Assets			
(a) Current Investment		89,000	78,000
(b) Inventories		8,00,000	4,00,000
(c) Cash & cash equivalent		37,000	78,000
Total		44,26,000	32,56,000

Notes to Accounts

Note no.	Particulars	31.3.22 (₹)	31.3.21(₹)
1.	Reserves and Surplus		
	Surplus i.e. Balance in the statement of P&L	6,00,000	4,85,000
	Security Premium Reserve		15,000
		6,00,000	5,00,000
2.	Long-term Borrowing 8% Debenture	8,00,000	5,00,000
3.	Short-term Provision		
	Provision for tax	76,000	56,000

Additional Information:

1. Machinery was purchased by issue of additional shares.
2. Debenture were issued @ 5% Discount on Jan 1, 2022.

Sol.

W.N.I Net profit before tax & extraordinary item	₹
Surplus i.e. Balance in the statement of P&L	
(6,00,000 – 48,5000)	1,15,000
Add: Provision for tax	76,000
	1,91,000

Cash flow statement for the year ended 31st March, 2022

Particulars	₹	₹
A. Cash flow from operating activities		
Net profit before tax & extraordinary item	1,91,000	
Adjustment for non-cash, non-operating item		
Add: Interest on Debenture	46,000	
	2,37,000	
Operating profit before working capital changes		
Add: Increase in current lia Trade payable 50,000		
Less: Increase in current Assets Inventories 4,00,000	(3,50,000)	
Operating Loss before tax	(1,13,000)	
Less: Tax paid	(56,000)	
Net cash used in operating activities	(1,69,000)	1,69,000
B. Cash flow from Investing Activities Purchase of Intangible Assets	(1,00,000)	
Net cash used in Investing Activities		(1,00,000)
C. Cash flow from financing Activities		
Proceeds from issue of Debenture	2,85,000	

Interest on Debenture	(46,000)	
Net cash flow financing activities	2,39,000	2,39,000
D. Net decrease in cash & cash equivalent (A + B + C)		(30,000)
E. Cash and cash equivalent in the beginning (78,000 + 78,000)		1,56,000
F. Cash & cash equivalent at the end (89,000 + 37,000)		1,26,000

PRACTICE QUESTIONS

Q.1 From the following Balance sheets of zeal Ltd. Prepare cash flow statement.

Particular	Note No.	31.3.2021 ₹	31.3.2020 ₹
I. Equity and Liabilities			
(1) Share holder's fund			
(a) Share capital		6,60,000	6,00,000
(b) Reserve and surplus		50,000	60,000
(2) Non-current liabilities			
Long-term borrowing		50,000	80,000
(3) Current liabilities			
(a) Short term borrowing	1	10,000	-
(b) Trade payable		1,94,000	2,48,000
(c) Short term provision	2	60,000	48,000
		10,24,000	10,36,000
II. Assets			
(1) Non-current assets			
(a) Fixed assets			
(i) Tangible assets		5,20,000	4,00,000
(ii) Intangible assets	3	15,000	1,20,000
(b) Non-current investment		1,28,000	1,00,000
(2) Current assets			
(a) Inventories		1,25,000	1,40,000
(b) Trade receivables		1,96,000	2,60,000
(c) Cash and cash equivalent		40,000	16,000
		10,24,000	10,36,000

Notes to Accounts

	Particular	31.3.2021 ₹	31.3.20 ₹
1.	Short-term borrowing		
	Bank overdraft	10,000	–
2.	Short term provision:		
	Provision for tax	60,000	48,000
3.	Intangible assets:		
	Good will	15,000	1,00,000
	Patents	15,000	20,000

Additional information:

(i) Machinery whose original cost was ₹1,00,000 (accummulated deprecation thereon ₹64,000) was sold for ₹20,000.

(ii) Depreciation on machinery charged during the year ₹50,000

(iii) Non-current investments costing ₹40,000 were sold for ₹64,000 during the year.

(iv) Interest paid on long-term borrowing ₹6,000.

Sol. Cash from operating activities ₹1,80,000

cash used in investing activities ₹1,90,000

Cash from financing activities ₹34,000

Q.2 For each of the following transaction, calculate the resulting cash flow and state the nature of cash flow i.e. operating, investing and financing

(a) Paid ₹4,50,000 to acquire shares in Infosys Ltd. and receive a dividend of ₹30,000 after acquisition.

(b) Acquired machinery for ₹3,00,000 paying 30% down payment and executing a bond for the balance payable.

(c) A machine with a book value of ₹50,000 provision for dep. on it ₹10,000 sold at a loss 20% on book value.

(d) The patents of Roxy Ltd. increased from ₹4,00,000 to ₹6,50,000 in 2020-21.

(e) 10% Debenture- ₹2,00,000 in 2019-20.

10% Debenture- ₹2,50,000 in 2020-21

(f) Y LTD. purchased a machinery of ₹50,00,000 in instalments under hire purchase system, paid ₹5,00,000 towards Principal payment and ₹50,000 towards interest.

Solution:

(a) Cash used in investing activity ₹4,20,000

(b) ₹90,000 cash used in investing

(c) Cash from investing activity ₹40,000

(d) Cash used in investing activity ₹2,50,000

(e) Cash flow from financing activity ₹27,500

(f) Cash used investing activity ₹5,00,000

Cash used in financing activity ₹50,000

Q. 3 P Ltd. Earned a profit of ₹ 2,50,000 after charging the following items.

S.No.	Particulars	(₹)
1.	Depreciation on Fixed Tangible Assets (Machinery)	20,000
2.	Loss on Sale of Fixed Tangible Assets (Furniture)	2,000
3.	Writing off Goodwill	9,000
4.	Provision for Doubtful Debts	2500
5.	Provision for Taxation	35,000
6.	Transfer to General Reserve	15,000
7.	Gain on sale of Fixed Tangible Assets (Machinery)	8,000

The following information about Assets and Liabilities is given

Particulars	31.3.2016 (₹)	31.3.2017 (₹)
Trade Receivable (All Good)	50,000	62,000
Trade Payables	45,000	55,000
Inventory	12,000	8,000
Income Received in Advance	8,000	–
Outstanding Expenses	6,000	3,000
Prepaid Expenses	–	5,000

Q4. Calculate cash flow from investing & financing activities

Particulars	31.3.22	31.3.21
Machinery	1,40,000	1,20,000
Patents	3,00,000	1,00,000
8% Long term investment	1,80,000	80,000
Investment in shares of Y Ltd.	1,00,000	1,00,000
Share capital	14,00,000	10,00,000
Share Issue Expenses	30,000	40,000
Land	50,00,000	50,00,000
8% Bank loan	4,00,000	4,00,000

Additional Information:

(a) A machinery costing ₹ 50,000 (depreciation provided thereon being ₹ 20,000) was sold for ₹ 5,000. Depreciation charged during the year ₹ 10,000.

(b) Y its. paid dividend @ 20% on its shares

(c) A plot of land purchased for investment purpose & let out for commercial use on which rent received ₹ 40,000.

(d) On March 31, 2022, 8% investment were purchased for ₹ 2,00,000 & some investment were sold at a profit of ₹ 10,000.

5. Interest received on debenture would result in inflow, outflow or no flow of cash?

Ans. Inflow of cash

6. Vinod ltd. is carrying on a paper manufacturing business. In the current year, it purchased machinery for ₹ 30,00,000, paid salaries of ₹ 30,000 to its employees, issued shares of ₹ 20,00,000 for expansion. It earned a profit of ₹ 4,00,000 for the current year. Find out cash flow from operating activities.

Ans. ₹ 4,00,000

7. Will the following result in cash inflow, cash outflow or no cash flow?

(a) Increase in Goodwill

(b) Sale of furniture book value ₹ 10,000 at a loss of 20%.

Ans. (a) Outflow of cash

(b) Inflow of cash

8. How will you treat the following transactions while preparing cash flow statement?

(a) Increase in outstanding employee benefits by ₹ 5,000.

(b) Decrease in marketable securities by ₹ 2,000.

Ans. (a) Working capital changes while determining cash flow from operating activities.

(b) Part of cash & cash equivalent.

9. Ram, a customers deposited ₹ 500 into bank. Which type of activity will it be considered while preparing cash flow statement?

Ans. operating activity

10. Which of the following is cash flow from operating activity.

(a) Purchase of Machinery

(b) Issue of bonus share

(c) Interest paid on term deposit by a bank.

(d) Sale of building at a loss.

11. Which of the following is not a cash outflow.

(a) increase in creditors

(b) increase in debtors

(c) increase in stock

(d) increase in prepaid expenses

Ans. increase in creditors

12. Purchase of fixed assets on long term deferred payment would result in inflow, outflow or no flow of cash?

Ans. No flow of cash

13. Which of the following is not included in cash & cash equivalent?

(a) Cash in hand

(b) Bank balance

(c) Bank deposit with 100 days of maturity

(d) Cheque & drafts in hand

Ans. (c) Bank deposit with 100 days of maturity.

14. Following are included in cash & cash equivalent

(a) Treasury bill

(b) Trade bill

(c) Bank deposit of short term maturity

(d) All of above

Ans. (d) All of above

15. Cash from operation is equal to

(a) Net profit + Increase in Current Assets

(b) Net profit + Decrease in Current Liabilities

(c) Operating profit + Adjustment of Current Assets & current Lia.

(d) All of the above

Ans. (b) Net profit + Decrease in Current Liabilities

16. Fill in the blank with appropriate answer:

(a) Redemption of debenture/preference share result into ________ of fund.

(b) Net profit during the year ₹ 40,000 and creditors in the beginning ₹ 30,000 & creditors at the end ₹ 34,000. Cash flow from operating activities ________.

(c) Receipt of insurance claim for loss of stock by earthquake is shown under ________ activities in a cash flow statement.

(d) Buy back of share is shown as ________ activity while preparing cash flow statement.

Assertion and Reason (A-R)

Directions: In the following questions, a statement of Assertion (A) is followed by a statement of Reason (R). Mark the correct as:

(A) Both Assertion (A) and Reason (R) are true and Reason (R) is the correct explanation of Assertion (A)

(b) Both Assertion (A) & Reason (R) are true but Reason (R) is not the correct explanation of Assertion (A).

(c) Assertion (A) is true, but Reason (R) is false.

(d) Assertion (A) is false, but Reason (R) is true.

1. Assertion (A): Cash flow statement is a n analytical tool to determine the inflow & outflow of cash & cash equivalents during a financial year under appropriate heads

   Reason (R): Cash flow statement is prepared to show inflow and outflow under operating activities, investing activities and financing activities.

2. Assertion (A): Loss on sale of fixed assets is added back to net profit before tax.

   Reason (R): Loss on sale of fixed assets is a non-cash expense.

Cash Based MCQ

Read the following information & Answer the following Questions

Particulars	31.3.21	31.3.22
9% Debenture	1,00,000	1,50,000
Fixed Assets (Net)	3,00,000	2,10,000
Equity share	5,00,000	4,20,000
Prefence share	1,30,000	1,00,000
Investment	2,00,000	1,00,000
Marketable securities	30,000	30,000
Bank overdraft	70,000	40,000

Additional Information:

(a) Fixed assets book value ₹ 70,000 was sold for ₹ 50,000.

(b) Interest received ₹ 7,000.

(c) Debenture issued at the end of financial year

1. While preparing cash flow statement, under what head will Bank overdraft will be recorded?

   (a) Investing (b) Operating

   (c) Financing (d) Cash & cash equivalent

2. While preparing cash flow statement, under what head will marketable securities be recorded?

   (a) Investing (b) Operating

   (c) Financing (d) Cash & cash equivalent

3. What is the amount of net cash flow/used from financing activities?

(a) ₹ 89,000 inflow (b) ₹ 99,000 outflow

(c) ₹ 78,000 inflow (d) ₹ 1,00,00 outflow

4. What is the amount of net cash flow/used from investing activities?

(a) ₹ 43,000 inflow (b) ₹ 43,000 outflow

(c) ₹ 45,000 inflow (d) ₹ 48,000 outflow

SAMPLE QUESTION PAPER 2022-23

SUBJECT ACCOUNTANCY 055

CLASS XII

TIME 3 HOURS **MAX. MARKS 80**

GENERAL INSTRUCTIONS:

1. This question paper contains 34 questions. All questions are compulsory.
2. This question paper is divided into two parts, Part A and B.
3. Part - **A is compulsory for all candidates**.
4. Part - B **Analysis of Financial Statements**
5. Question 1 to 16 and 27 to 30 carries 1 mark each.
6. Questions 17 to 20, 31and 32 carries **3** marks each.
7. Questions from 21 ,22 and 33 carries **4** marks each
8. Questions from 23 to 26 and 34 carries **6** marks each
9. There is no overall choice. However, an internal choice has been provided in 7 questions of **one mark**, 2 questions of **three marks**, 1 question of **four marks** and 2 questions of **six marks.**

PART A

(Accounting for Partnership Firms and Companies)

S.No.	Question	Marks
	Part A :- Accounting for Partnership Firms and Companies	
1.	Navya and Radhey were partners sharing profits and losses in the ratio of 3: 1. Shreya was admitted for 1/5th share in the profits. Shreya was unable to bring her share of goodwill premium in cash. The journal entry recorded for goodwill premium is given below:	1

Date	Particular	LF	Debit (₹)	Credit (₹)
	Shreya's Current A/c. Dr. To Navya's Capital A/c. To Radhey's Capital A/c (Being entry for goodwill treatment passed)		24,000	 8,000 16,000

The new profit-sharing ratio of Navya, Radhey and Shreya will be:

a) 41: 7: 12

b) 13:12: 10

c) 3:1: 1

d) 5:3: 2

2. Assertion (A):- Commission provided to partner is shown in Profit and Loss A/c. Reason (R):- Commission provided to partner is charge against profits and is to be provided at fixed rate. — 1

a) (A) is correct but (R) is wrong
b) Both (A) and (R) are correct, but (R) is not the correct explanation of (A)
c) Both (A) and (R) are incorrect.
d) Both (A) and (R) are correct, and (R) is the correct explanation of (A)

3. A share of ₹ 10 each, issued at ₹ 4 premium out of which ₹ 7 (including ₹ 1 premium) was called up and paid up. The uncalled Capital will be ____________. — 1

a) ₹ 7 per share	b) ₹ 4 per share
c) ₹ 8 per share	d) ₹ 3 per share

OR

While issuing ____________ type of Debentures, company doesn't give any undertaking for the repayment of money borrowed by issuing such debentures.

a) Zero Coupon Rate Debentures	b) Non-Convertible Debentures
c) Secured Debentures	d) Non-Redeemable Debentures

4. Samiksha, Arshiya and Divya were partners in a firm sharing profits and losses in the ratio of 5: 3: 2. With effect from 1st April 2022, they agreed to share future profits and losses in the ratio of 2: 5: 3. Their Balance Sheet showed a debit balance of ₹ 50,000 in the Profit and Loss Account and a balance of ₹ 40,000 in the Investment Fluctuation Fund. The market value of an investment is ₹30,000 against the book value of ₹50,000. Partners have decided, not to show revised valued in the balance sheet and to pass an adjusting entry for it. Which of the following is the correct treatment of the above? — 1

a)	Samiksha's Capital A/c. Dr. To Arshiya's Capital A/c. To Divya's Capital A/c	9,000	 6,000 3,000
b)	Arshiya's Capital A/c. Dr. To Samiksha's Capital A/c. To Divya's Capital A/c.	5,000	 2,000 3,000
c)	Arshiya's Capital A/c. Dr. Divya's Capital A/c. Dr. To Samiksha's Capital A/c	2,000 1,000	 3,000
d)	Arshiya's Capital A/c. Dr. Divya's Capital A/c. Dr. To Samiksha's Capital A/c	6,000 3,000	 9,000

Or

Sohan and Mohan are partners sharing profits and losses in the ratio of 2:3 with the capitals of ₹ 5,00,000 and ₹ 6,00,000 respectively. On 1st January 2022, Sohan and Mohan granted loans of ₹ 20,000 and ₹ 10,000 respectively to

	the firm. Determine the amount of loss to be borne by each partner for the year ended 31st March 2022 if the loss before interest for the year amounted to ₹ 2,500. a) Share of Loss Sohan –₹ 1,250 Mohan – ₹ 1,250 b) Share of Loss Sohan –₹ 1,000 Mohan – ₹ 1,500 c) Share of Loss Sohan –₹ 820 Mohan – ₹ 1,230 d) Share of Loss Sohan –₹ 1,180 Mohan – ₹ 1,770	
5.	Vihaan and Mann are partners sharing profits and losses in the ratio of 3:2. The firm maintains fluctuating capital accounts and the balance of the same as on 31st March 2022 is ₹ 4,00,000 and ₹ 4,65,000 for Vihaan and Mann respectively. Drawings during the year were ₹ 65,000 each. As per the partnership Deed, Interest on capital @ 10% p.a. on Opening Capital has been allowed to them. Calculate the opening capital of Vihaan given that the divisible profits during the year 2021-22 was ₹ 2,25,000. a) ₹ 3,30,000 b) ₹ 4,40,000 c) ₹ 4,00,000 d) ₹ 3,00,000	1
6.	Savitri Ltd. issued 50,000, 8% Debentures of ₹ 100 each at certain rate of premium and to be redeemed at 10% premium. At the time of writing off Loss on Issue of Debentures, Statement of Profit and Loss was debited with ₹ 2,00,000. At what rate of premium, these debentures were issued? a) 10% b) 16% c) 6% d) 4% **Or** Durga Ltd. issued 80,000, 10% Debentures of ₹ 100 each at certain rate of discount and were to be redeemed at 20% premium. Existing balance of Securities Premium before issuing of these debentures was ₹ 25,00,000 and after writing off Loss on Issue of Debentures, the balance in Securities Premium was ₹ 5,00,000. At what rate of discount, these debentures were issued? a) 10% b) 5% c) 25% d) 15%	1
7.	Attire Ltd, issued a prospectus inviting applications for 12,000 shares of ₹10 each payable ₹3 on application, ₹ 5 on allotment and balance on call. Public had applied for certain number of shares and application money was received. Which of the following application money, if received restricts the company to proceed with the allotment of shares, as per SEBI guidelines? a) ₹ 36,000 b) ₹ 45,000 c) ₹ 30,000 d) ₹ 32,400	1
8.	Amay, Bina and Chander are partners in a firm with capital balances of ₹ 50,000, ₹ 70,000 and ₹ 80,000 respectively on 31st March, 2022. Amay decides	1

	to retire from the firm on 31st March, 2022. With the help of the information provided, calculate the amount to be paid to Amay on his retirement. There existed a general reserve of ₹ 7,500 in the balance sheet on that date. The goodwill of the firm was valued at ₹ 30,000. Gain on revaluation was ₹24,000. **a)** ₹ 88,500 **b)** ₹ 90,500 **c)** ₹ 65,375 **d)** ₹ 70,500 **Or** A, B and C are partners. A's capital is ₹ 3,00,000 and B's capital is ₹1,00,000. C has not invested any amount as capital but he alone manages the whole business. C wants 30,000 p.a. as salary, though the deed is silent. Firm earned a profit of ₹1,50,000. How much will each partner receives as an appropriation of profits? **a)** A ₹ 60,000; B ₹ 60,000; C ₹ 30,000 **b)** A ₹ 90,000; B ₹ 30,000; C ₹ 30,000 **c)** A ₹ 40,000; B ₹ 40,000 and C ₹ 70,000 **d)** A ₹ 50,000; B ₹ 50,000 and C ₹ 50,000	

Read the following hypothetical situation, Answer Question No. 9 and 10

Puneet and Raju are partners in a clay toys making firm. Their capitals were ₹ 5,00,000 and ₹ 10,00,000 respectively. The firm allowed Puneet to get a commission of 10% on the net profit before charging any commission and Raju to get a commission of 10% on the net profit after charging all commission. Following is the Profit and Loss Appropriation Account for the year ended 31st March 2022.

Dr. Profit and Loss Appropriation Account for the year ended 31st March 2022 Cr.

Particulars	Amount (₹)	Particulars	Amount (₹)
To Puneet's Capital A/c (Commission) (------ x10/100)	44,000	By Profit and Loss a/c	....
To Raju's Capital A/c (Commission)	-----------		
To Profit share transferred to :-			
Puneet's Capital A/c	-----------		
Raju's Capital A/c	------------		
	=========		==========

9.	Raju's commission will be:- a) ₹ 40,000 b) ₹ 44,000	1

	c) ₹ 36,000 d) ₹ 36,440		
10.	Puneet's share of profit will be :- a) ₹ 1,80,000 b) ₹ 1,44,000 c) ₹ 2,16,000 d) ₹ 1,60,000	1
11.	Choose the correct sequence of the following transactions in context of Division of Profits. (i) Guarantee by Firm to Partners (ii) Guarantee by Partners to Firm (iii) Transfer of Profits to Profit and Loss Appropriation Account (iv) Guarantee by Partner to Partner a) (i); (iii) ; (iv) ; (ii) b) (iii); (i) ; (ii) ; (iv) c) (iii) ; (ii) ; (i); (iv) d) (ii); (iii); (iv); (i)	1
12.	If 10,000 shares of ₹10 each were forfeited for non-payment of final call money of ₹ 3 per share and only 7,000 shares were re-issued @ ₹ 11 per share as fully paid up, then what is the amount of maximum possible discount that company can allow at the time of re-issue of the remaining 3,000 shares? a) ₹ 28,000 b) ₹ 21,000 c) ₹ 9,000 d) ₹ 16,000	1
13.	As per Companies Act 2013, Securities Premium Balance can be utilised for which of the following purpose? a) Issuing bonus to existing shareholders to convert partly paid up into fully paid-up bonus shares. b) Providing for Premium payable on Redemption of Debentures. c) Writing off all Capitalised Expenditures d) Buy Back of Debentures	1
14.	Ganga and Jamuna are partners sharing profits in the ratio of 2:1. They admit Saraswati for 1/5th share in future profits. On the date of admission, Ganga's capital was ₹ 1,02,000 and Jamuna's capital was ₹ 73,000. Saraswati brings ₹ 25,000 as her share of goodwill and she agrees to contribute proportionate capital of the new firm. How much capital will be brought by Saraswati? a) ₹ 43,750 b) ₹ 37,500 c) ₹ 50,000 d) ₹ 40,000	1
15.	Green and Orange are partners. Green draws a fixed amount at the beginning of every month. Interest on drawings is charged @8% p.a. At the end of the year interest on Green's drawings amounts to ₹ 2,600. Monthly drawings of Green were: a) ₹ 8,000	1

	b) ₹ 60,000 c) ₹ 7,000 d) ₹ 5,000 **Or** Girdhar, a partner withdrew ₹ 5,000 in the beginning of each quarter and interest on drawings was calculated as ₹ 1,500 at the end of accounting year 31 March 2022. What is the rate of interest on drawings charged? a) 6% p.a. b) 8% p.a. c) 10% p.a. d) 12% p.a.	
16.	At the time of dissolution of a firm, Creditors are ₹ 70,000; Firm's Capital is ₹ 1,20,000; Cash Balance is ₹ 10,000. Other assets realised ₹ 1,50,000. Gain/Loss in the realisation account will be: a) ₹ 30,000 (Gain) b) ₹ 40,000 (Gain) c) ₹ 40,000 (Loss) d) ₹ 30,000 (Loss)	1
17.	Nirmala, Divisha and Sara were partners in a firm sharing profits and losses in the 3:4:3. Books were closed on 31st March every year. Sara died on 1st February, 2022. As per the partnership deed Sara's executors are entitled to her share of profit till the date of death on the basis of Sales turnover. Sales for the year ended 31st March 2021 was ₹ 10,00,000 and profit for the same year was ₹ 1,20,000. Sales show a positive trend of 20% and percentage of profit earning is reduced by 2%. Journalise the transaction along with the working notes.	3
18.	Amay, Anmol and Rohan entered into partnership on 1st July, 2021 to share profits and losses in the ratio of 3:2:1. Amay guaranteed that Rohan's share of profit after charging interest on capital @ 6% p.a would not be less than ₹ 36,000 p.a. Their fixed capital balances are: ₹ 2,00,000, ₹ 1,00,000 and ₹ 1,00,000 respectively. Profit for the year ended 31st March, 2022 was ₹1,38,000. Prepare Profit and Loss Appropriation A/c. **Or** Ajay, Manish and Sachin were partners sharing profits in the ratio 5:3:2. Their Capitals were ₹ 6,00,000; ₹ 8,00,000 and ₹ 11,00,000 as on April 01, 2021. As per Partnership deed, Interest on Capitals were to be provided @ 10% p.a. For the year ended March 31, 2022, Profits of ₹ 2,00,000 were distributed without providing for Interest on Capitals. Pass an adjustment entry and show the workings clearly.	3

19.	Anthony Ltd. issued 20,000, 9% Debentures of ₹ 100 each at 10% discount to Mithoo Ltd. from whom Assets of ₹ 23,50,000 and Liabilities of ₹ 6,00,000 were taken over. Pass entries in the books of Anthony Ltd. if these debentures were to be redeemed at 5% premium. **Or** Random Ltd. took over running business of Mature Ltd. comprising of Assets of ₹ 45,00,000 and Liabilities of ₹ 6,40,000 for a purchase consideration of ₹ 36,00,000. The amount was settled by bank draft of ₹ 1,50,000 and balance by issuing 12% preference shares of ₹ 100 each at 15% premium. Pass entries in the books of Random Ltd.	3
20.	Doremon, Shinchan and Nobita are partners sharing profits and losses in the ratio of 3:2:1. With effect from 1st April, 2022 they agree to share profits equally. For this purpose, goodwill is to be valued at two year's purchase of the average profit of last four years which were as follows: Year ending on 31st March,2019 ₹ 50,000 (Profit) Year ending on 31st March,2020 ₹ 1,20,000 (Profit) Year ending on 31st March,2021 ₹ 1,80,000 (Profit) Year ending on 31st March,2022 ₹ 70,000 (Loss) On 1st April, 2021 a Motor Bike costing ₹ 50,000 was purchased and debited to travelling expenses account, on which depreciation is to be charged @ 20% p.a by Straight Line Method. The firm also paid an annual insurance premium of ₹ 20,000 which had already been charged to Profit and Loss Account for all the years. Journalise the transaction along with the working notes.	3
21.	Altaur Ltd. was registered with an authorised Capital of ₹ 4,00,00,000 divided in 25,00,000 Equity Shares of ₹ 10 each and 1,50,000, 9% Preference Shares of ₹ 100 each. The company issued 8,00,000 Equity Shares for public subscription at 20% premium, payable ₹ 3 on application; ₹ 7 on allotment (including premium) and balance on call. Public had applied for 10,00,000 shares. Excess Applications were sent letters of regret. All the dues on allotment received except on 15,000 shares held by Sanju. Another shareholder Rocky paid his call dues along with allotment on his holding of 25,000 shares. You are required to prepare the Balance Sheet of the company as per Schedule III of Companies Act, 2013, showing Share Capital balance and also prepare Notes to Accounts.	4
22.	Charu, Dhwani, Iknoor and Paavni were partners in a firm. They had entered into partnership firm last year only, through a verbal agreement. They contributed Capitals in the firm and to meet other financial requirements, few partners also provided loan to the firm. Within a year, their conflicts arisen due	4

	to certain disagreements and they decided to dissolve the firm. The firm had appointed Ms. Kavya, who is a financial advisor and legal consultant, to carry on the dissolution process. In the first instance, Ms. Kavya had transferred various assets and external liabilities to Realisation A/c. Due to her busy schedule; Ms. Kavya has delegated this assignment to you, being an intern in her firm. On the date of dissolution, you have observed the following transactions: (i) Dhwani's Loan of ₹ 50,000 to the firm was settled by paying ₹ 42,000. (ii)Paavni's Loan of ₹ 40,000 was settled by giving an unrecorded asset of ₹ 45,000. (iii)Loan to Charu of ₹ 60,000 was settled by payment to Charu's brother loan of the same amount. (iv)Iknoor's Loan of ₹ 80,000 to the firm and she took over Machinery of ₹ 60,000 as part payment. You are required to pass necessary entries for all the above mentioned transactions.	
23.	OTUA Ltd. was registered with an authorised capital of 2,00,000 equity shares of ₹ 100 each. The company offered 60,000 shares for public subscription at 25% premium. The share was payable as ₹ 40 on application and balance on allotment, with premium. Public had applied for 85,000 shares. Pro-rata allotment was made in the ratio of 5:4 and remaining applications were sent letters of regret. Mr. Anand holding 4,000 shares failed to pay allotment money and his shares were forfeited. Out of these 3,000 shares were re-issued at a discount of ₹ 20 per share. Pass necessary entries in the books of the OTUA Ltd. **Or** Pass entries for forfeiture and re-issue in both the following cases. **(a)** Vikram Ltd. forfeited 5,000 shares of Rahul, who had applied for 6,000 shares for non-payment of allotment money of ₹ 5 per share and first and final call of ₹ 2 per share. Only application money of ₹ 3 was paid by him. Out of these 3,000 shares were re-issued @ ₹ 12 per share as fully paid. **(b)** Ratan Ltd. forfeited 3,000 shares of ₹ 10 each (issued at ₹ 2 premium) for non-payment of first call of ₹ 2 per share. Final call of ₹ 3 per share was not yet made. Out of these 2,000 shares were re-issued at ₹ 10 per share as fully paid.	6
24.	X and Y were partners in the profit-sharing ratio of 3: 2. Their balance sheet as at March 31, 2022 was as follows:	6

Balance Sheet as at March 31, 2022

Liabilities		**Amount (₹)**	**Assets**		**Amount (₹)**
Creditors		56,000	Plant and Machinery		70,000
General Reserve		14,000	Buildings		98,000
Capital Accounts:			Stock		21,000
X	1,19,000		Debtors	42,000	
Y	1,12,000	2,31,000	(-)Provision	7,000	35,000
			Cash in Hand		77,000
		3,01,000			3,01,000

Z was admitted for 1/6th share on the following terms:

(i) Z will bring ₹ 56,000 as his share of capital, but was not able to bring any amount to compensate the sacrificing partners.

(ii) Goodwill of the firm is valued at ₹. 84,000.

(iii) Plant and Machinery were found to be undervalued by ₹ 14,000 Building was to brought up to ₹ 1,09,000.

(iv) All debtors are good.

(v) Capitals of X and Y will be adjusted on the basis of Z's share and adjustments will be done by opening necessary current accounts.

You are required to prepare revaluation account and partners' capital account.

Or

P, Q and R were partners in a firm sharing profits in the ratio of 3:2:1 respectively. On March 31st, 2022, the balance sheet of the firm stood as follows:

Balance Sheet

Liabilities		Amount (₹)	Assets	Amount (₹)
Creditors		13,000	Cash	4,700
Bills Payable		590	Debtors	8,000
Capital Accounts:			Stock	11,690
P	15,000		Buildings	23,000
Q	10,000		Profit and Loss Account	1,200
R	10,000	35,000		
		48,590		48,590

Q retired on the above-mentioned date on the following terms:

(i) Buildings to be appreciated by ₹7,000

(ii) A provision for doubtful debts to be made at 5 % on debtors.

(iii) Goodwill of the firm is valued at ₹ 18,000 and adjustment to be made by raising and writing off the goodwill.

(iv) ₹ 2,800 was to be paid to Q immediately and the balance in his capital account to be transferred to his loan account carrying interest as per the agreement.

(v) Remaining partner decided to maintain equal capital balances, by opening current account.

Prepare the revaluation account and partner's capital accounts.

25. A, B and C were partners sharing P&L in the ratio 5:3:2. A died on 30th June, 2019. Entry for treatment of goodwill after his death was passed as follows:- (6)

Date	Particulars	L.F	Debit (₹)	Credit (₹)
	B's Capital A/c Dr. C's Capital A/c Dr. To A's Capital A/c (Entry for goodwill treatment passed at the time of death of partner)		1,80,000 1,20,000	 3,00,000

A's profit till date of death was estimated as ₹ 1,20,000, based on the average profits of past three years. Final dues payable to A's executors on the date of death was calculated as ₹ 8,40,000 out of which ₹ 2,40,000 was paid immediately by giving him Furniture valued for the same and balance was to be paid in three equal annual instalments starting from 30 June, 2020, together with interest rate as specified in Section 37 of Indian Partnership Act, 1932..
Pass necessary entry for profit share to be credited to A's Capital and also prepare A's executors account till final settlement.

26. Health2Wealth Ltd. had share capital of ₹ 80,00,000 divided in shares of ₹ 100 each and 20,000, 8% Debentures of ₹ 100 each as part of capital employed. (6)
The company need additional funds of ₹ 55,00,000 for which they decided to issue debentures in such a way that they got required funds after issuing debentures of the same class as earlier, at 10% premium. These debentures were to be redeemed at 20% premium after 4 years. These debentures were issued on 01 October, 2021.
You are required to

(a) Pass entries for issue of Debentures.
(b) Prepare Loss on Issue of Debentures Account assuming there was existing balance of Securities Premium Account of ₹ 2,80,000.
(c) Pass entries for Interest on debentures on March 31, 2022 assuming interest is payable on 30 September and 31 March every year.

Part B :- Analysis of Financial Statements
(Option – I)

27. Financial statements are prepared on certain basic assumptions (pre-requisites) known as____________. (1)

a) Provision of Companies Act,2013	b) Accounting Standards
c) Postulates	d) Basis of Accounting

Or

Which one of the following is correct?

	(i) Quick Ratio can be more than Current Ratio. (ii) High Inventory Turnover ratio is good for the organisation, except when goods are bought in small lots or sold quickly at low margins to realise cash. (iii) Sum of Operating Ratio and Operating Profit ratio is always 100%. a) All are correct. b) Only (i) and (iii) are correct. c) Only (ii) and (iii) are correct. d) Only (i) and (ii) are correct	
28.	From the following calculate Interest coverage ratio Net profit after tax Rs 12,00,000; 10% debentures Rs 1,00,00,000; Tax Rate 40% a) 1.2 times b) 3 times c) 2 times d) 5 times	1
29.	Insurance Claim received by Albert Co. Ltd. of ₹ 5,00,000 for Loss of Machinery due to theft will be recorded in Cash Flow Statement in which of the following manner? a) Added under Operating Activities as Extraordinary Item and Subtracted from Operating Activities also. b) Subtracted under Operating Activities as Extraordinary Item and Added to Operating Activities also. c) Added under Operating Activities as Extraordinary Item and Outflow under Investing Activity also. d) Subtracted under Operating Activities as Extraordinary Item and Inflow under Investing Activities also. **Or** A company issued 20,000; 9% Debentures of ₹ 100 each at 10% Discount. These debentures were to be redeemed at 15% Premium at the end of 5 years. The balance in Securities Premium Account as on the date of Issue was ₹ 3,70,000. How this transaction will be reflected in Cash Flow Statement? a) Added ₹ 1,30,000 under Operating Activities as Loss on Issue of Debentures written off and Inflow of ₹ 20,00,000 under Financing Activities. b) Added ₹ 5,00,000 under Operating Activities as Loss on Issue of Debentures written off and Inflow of ₹ 18,00,000 under Financing Activities. c) Added ₹ 1,30,000 under Operating Activities as Loss on Issue of Debentures written off and Inflow of ₹ 18,00,000 under Financing Activities. d) Added ₹ 5,00,000 under Operating Activities as Loss on Issue of Debentures written off and Inflow of ₹ 20,00,000 under Financing Activities.	1
30.	From the following information find out the inflow of Cash by sale of Office	1

	equipment's 31st March, 2022 31st March, 2021 Office Equipment ₹ 2,00,000 ₹ 3,00,000 Additional Information: Depreciation for the year 2021-22 was Rs. 40,000 Purchase of Office Equipment purchased during the year Rs. 30,000 Part of Office Equipment sold at a profit of Rs. 12,000 a) ₹ 1,00,000 b) ₹ 1,02,000 c) ₹ 90,000 d) ₹ 1,12,000	
31.	Classify the following items under Major heads and Sub-head (if any) in the Balance Sheet of a Company as per schedule III of the Companies Act 2013. (i) Current maturities of long term debts (ii) Furniture and Fixtures (iii) Provision for Warranties (iv) Income received in advance (v) Capital Advances (vi) Advances recoverable in cash within the operation cycle	3
32.	Lala Ltd. and Bala Ltd. use different accounting policies for inventory valuation. These variations leave a big question mark on the cross-sectional analysis and comparison of these two firms was not possible. Identify the limitation of Ratio Analysis highlighted in the above situation. Also explain any two other limitations of Ratio Analysis apart from the identified above.	3
33.	Determine Return on Investment and Net Assets Turnover ratio from the following information:- Profits after Tax were ₹ 6,00,000; Tax rate was 40%; 15% Debentures were of ₹20,00,000; 10% Bank Loan was ₹ 20,00,000; 12% Preference Share Capital ₹ 30,00,000; Equity Share Capital ₹ 40,00,000 ; Reserves and Surplus were ₹ 10,00,000; Sales ₹ 3,75,00,000 and Sales Return ₹ 15,00,000. **Or** Debt to Capital Employed ratio is 0.3:1. State whether the following transactions, will improve, decline or will have no change on the Debt to Capital Employed Ratio. Also give reasons for the same. (i) Sale of Equipments costing ₹ 10,00,000 for ₹ 9,00,000. (ii) Purchased Goods on Credit for ₹ 1,00,000 for a credit of 15 months, assuming operating cycle is of 18 months. (iii) Conversion of Debentures into Equity Shares of ₹ 2,00,000.	4

	(iv) Tax Refund of ₹ 50,000 during the year.	
34.	Read the following hypothetical text and answer the given questions on the basis of the same: Aashna, an alumnus of CBSE School, initiated her start up Smartpay, in 2015. Smartpay is a service platform that processes payments via UPI and POS, and provides credit or loans to their clients.. During the year 2021-22, Smartpay issued bonus shares in the ratio of 5:1 by capitalising reserves. The profits of Smartpay in the year 2021-22 after all appropriations was ₹ 7,50,000. This profit was arrived after taking into consideration the following items: -	6

Particulars	Amount (₹)
Interim Dividend paid during the year	90,000
Depreciation on Machinery	40,000
Loss of Machinery due to fire	20,000
Insurance claim received for Loss of Machinery due to Fire	10,000
Interest on Non-Current Investments received	30,000
Tax Refund	20,000

Additional Information:

Particulars	**31.3.22 (₹)**	**31.3. 21(₹)**
Equity Share Capital	12,00,000	10,00,000
Securities Premium Account	3,00,000	5,00,000
General Reserve	1,50,000	1,50,000
Investment in Marketable Securities	1,50,000	1,00,000
Cash in hand	2,00,000	3,00,000
Machinery	3,00,000	2,00,000
10% Non-Current Investments	4,00,000	3,00,000
Bank Overdraft	2,50,000	2,00,000
Goodwill	30,000	80,000
Provision for Tax	80,000	60,000

(i) Goodwill purchased during the year was ₹ 20,000.
(ii) Proposed Dividend for the year ended March 31, 2021 was ₹ 1,60,000 and for the year ended March 31,2022 was ₹ 2,00,000.

You are required to:
1. Calculate Net Profit before tax and extraordinary items.
2. Calculate Operating profit before working capital changes.
3. Calculate Cash flow from Investing activities.
4. Calculate Cash flow from Financing activities.
5. Calculate closing cash and cash equivalents.

ANSWER KEY - SAMPLE QUESTION PAPER 2022-23

SUBJECT ACCOUNTANCY 055

CLASS XII

S.NO	Question	Marks
	Part A **(Accounting for Partnership Firms and Companies)**	
1.	a) 41: 7: 12	1
2.	c) Both (A) and (R) are incorrect	1
3.	b) ₹ 4 per share OR d) Non – Redeemable Debentures	1
4.	a) Samiksha's Capital A/c. Dr. 9,000 To Arshiya's Capital A/c. 6,000 To Divya's Capital A/c 3,000 Or d) Share of Loss Sohan –₹ 1,180 Mohan – ₹ 1,770	1
5.	d) ₹ 3,00,000	1
6.	c) 6% OR b) 5%	1
7.	c) ₹ 30,000	1
8.	d) ₹70,500 Or d) A ₹ 50,000; B ₹ 50,000 and C ₹ 50,000	1
9.	c) ₹ 36,000	1
10.	a) ₹ 1,80,000	1
11.	c) (iii) ; (ii) ; (i); (iv)	1
12.	b) ₹ 21,000	1
13.	b) Providing for Premium payable on Redemption of Debentures.	1
14.	c) ₹ 50,000	1
15.	d) 5,000 Or d) 12% p.a	1
16.	d) ₹ 30,000 (loss)	1
17	Journal Entry	3 (1 + 2)

Date	Particulars	L.F.	Dr. Amount	Cr. Amount

	1.02.22	Profit and Loss Suspense A/c Dr. To Sara's Capital A/c (Being Sara's share of profit allowed till the date of her death)		30,000	30,000	

Workings: Profit % to sales turnover for the year ended 31st March,2021=1,20,000/10,00,000 X100= 12%

Estimated sales for the year ended 31st March,2022=₹ 10,00,000+20% of ₹ 10,00,000 = ₹ 12,00,000

Estimated sales till 01st February,2022 = ₹ 12,00,000 x 10/12 = ₹ 10,00,000

Profit percentage 12-2=10%

Profit amount till 01st February, 2022 = 10% of ₹ 10,00,000 = ₹ 1,00,000

Sara's share of profit till 1st February,2022= $\frac{1,00,000 \times 3}{10}$ = ₹ 30,000

18 Dr. Profit and Loss Appropriation A/c for the year ending on 31st March, 2022 Cr. — 3 (1/2 x6)

Particulars	Amount (₹)	Particulars	Amount (₹)
To Interest on Capital:		By Profit and Loss A/c	1,38,000
Amay's Current A/c	9,000		
Anmol's Current A/c	4,500		
Rohan's Current A/c	4,500		
To Partners' Current A/c:			
Amay 53,000			
Anmol 40,000			
Rohan 27,000**	1,20,000		
	1,38,000		**1,38,000**

** Guarantee met for 9 months.

Or

Journal Entry

Or — 3 (1+2)

Date	Particulars	L.F	Debit (₹)	Credit (₹)
(i)	Ajay's Capital A/c Dr. To Manish's Capital A/c To Sachin's Capital A/c (Adjustment entry passed)		52,000	 4,000 48,000

Working Notes

Particulars	Ajay		Manish		Sachin		Firm	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Profits taken back	1,00,000		60,000		40,000			2,00,000
Interest on Capital to be credited		48,000		64,000		88,000	2,00,000	
	1,00,000	48,000	60,000	64,000	40,000	88,000	2,00,000	2,00,000
	52,000 (Dr.)		4,000 (Cr.)		48,000 (Cr.)			

19. Books of Anthony Ltd. — 3

Journal Entries

Date	Particulars	L.F	Debit (₹)	Credit (₹)

(i)	Assets A/c Dr. Goodwill A/c Dr. To Liabilities A/c To Mithoo Ltd. A/c (Business purchased of Mithoo Ltd. comprising of Assets and Liabilities)		23,50,000 50,000	 6,00,000 18,00,000
(ii)	Mithoo Ltd. A/c Dr. Loss on Issue of Debentures A/c Dr. To 9% Debentures A/c To Premium on Redemption of Debentures A/c (Debentures issued to Mithoo Ltd. at Discount, redeemable at Premium)		18,00,000 3,00,000	 20,00,000 1,00,000

OR

Books of Random Ltd.

Journal Entries

Date	Particulars	L.F	Debit (₹)	Credit (₹)
(i)	Assets A/c Dr. To Liabilities A/c To Mature Ltd. A/c To Capital Reserve A/c (Business purchased of Mithoo Ltd. comprising of Assets and Liabilities)		45,00,000	 6,40,000 36,00,000 2,60,00
(ii)	Mature Ltd. A/c Dr. To Bank A/c To 12% Preference Share Capital A/c To Securities Premium A/c (Debentures issued to Mithoo Ltd. at Discount, redeemable at Premium)		36,00,000	 1,50,000 30,00,000 4,50,000
	No. of Shares = 34,50,000/115 = 30,000 shares @ 100 + 15 each			

20. Sol

Journal Entry

3 (1+2)

Date	**Particulars**	**L.F.**	**Dr. Amount**	**Cr. Amount**
1.4.20	Nobita's Capital A/c Dr. To Doremon's Capital A/c (Being goodwill adjusted at the time of change in profit sharing ratio)		26,667	 26,667

Workings:

(i) Calculation of gaining ratio and sacrificing ratio:

Doremon's gain or sacrifice = 3/6-2/6= 1/6 (sacrifice)

Shinchan's gain or sacrifice = 2/6-2/6 =0

Nobita's gain or sacrifice = 1/6 – 2/6 = -1/6 (gain)

(ii) Calculation of goodwill:

CALCULATIONOF NORMAL PROFIT

Year Ended	Profit/ Loss	Adjustments	Normal Profit
31st March,2019	50,000	----	50,000
31st March,2020	1,20,000	-----	1,20,000
31st March,2021	1,80,000	-----	1,80,000
31st March,2022	(70,000)	50,000-10,000	(30,000)
Total			3,20,000

Goodwill =Average Profits X No. of years Purchase
Average Profits = Total Normal Profits/Number of years
= 3,20,000/4 = 80,000
Goodwill= 80,000 X 2= ₹1,60,000
A's share of goodwill= 1,60,000 X 1/6= ₹26,667

21. Books of Altaur Ltd.
Balance Sheet (Extract) as at .....

4 (1+3)

Particulars	Note No.	Current Year (₹)	Previous Year (₹)
EQUITY AND LIABILITIES Shareholders' Funds Share Capital	1	63,25,000	Nil

Notes to Accounts

1. Share Capital		Amount (₹)
Authorised Share Capital		
25,00,000 Equity Shares @ ₹ 10 each		2,50,00,000
1,50,000 9% Preference Shares @ ₹ 100 each		1,50,00,000
		4,00,00,000
Issued Share Capital		
8,00,000 Equity Shares @ ₹ 10 each		**80,00,000**
Subscribed Share Capital		
(i) Subscribed and Fully Paid up	--------	
(ii) Subscribed but not Fully Paid up		
8,00,000 Equity Shares @ ₹ 8 each	64,00,000	
(-) Calls in Arrears**	(75,000)	63,25,000

22. Journal Entries in the Books of Charu, Dhwani, Iknoor and Paavni

4

Date	Particulars	L.F.	Dr. Amount	Cr. Amount
(i)	Dhwani's Loan A/c Dr.		50,000	
	To Bank A/c			42,000
	To Realisation A/c			8,000
	(Dhwani's Loan of ₹ 50,000 settled at ₹ 42,000)			
(ii)	Paavni's Loan A/c Dr.		40,000	
	To Realisation A/c			40,000

	(Paavni's Loan of ₹ 40,000 settled by giving an unrecorded asset)				
(iii)	Realisation A/c Dr. To Loan to Charu A/c (Loan to Charu was settled by payment to Charu's brother Loan)		60,000	60,000
(iv)	Iknoor's Loan A/c Dr. To Realisation A/c To Bank A/c (Iknoor's Loan of ₹ 80,000 and Machinery was given as part payment and rest through bank)		80,000	60,000 20,000

23. Books of OTUA Ltd. 6

Journal Entries

Date	Particulars	L.F	Debit (₹)	Credit (₹)
(i)	Bank A/c Dr. To Equity Share Application A/c (Application money received on 85,000 shares)		34,00,000	34,00,000
(ii)	Equity Share Application A/c Dr. To Equity Share Capital A/c To Equity Share Allotment A/c To Bank A/c (Application money transferred to share capital, share allotment and refunded)		34,00,000	24,00,000 6,00,000 4,00,000
(iii)	Equity Share Allotment A/c Dr. To Equity Share Capital A/c To Securities Premium A/c (Allotment due on 60,000 shares with Premium)		51,00,000	36,00,000 15,00,000
(iv)	Bank A/c Dr. Calls in Arrears A/c Dr. To Equity Share Allotment A/c (Allotment received on 56,000 shares)		42,00,000 3,00,000	45,00,000
(v)	Equity Share Capital A/c Dr. Securities Premium A/c Dr. To Share Forfeited A/c To Calls in Arrears A/c (4,000 shares forfeited for non-payment of allotment money)		4,00,000 1,00,000	2,00,000 3,00,000
	Bank A/c Dr. Share Forfeited A/c Dr. To Equity Share Capital A/c (3,000 shares re-issued @ ₹ 80 per share)		2,40,000 60,000	3,00,000
	Share Forfeited A/c Dr. To Capital Reserve A/c		90,000	90,000

	(Gain on re-issue of forfeited shares transferred to capital reserve)			

OR

Books of Vikram Ltd.

Journal Entries

(i)

Date	Particulars	L.F	Debit (₹)	Credit (₹)
(i)	Share Capital A/c Dr. To Share Forfeited A/c To Calls in Arrears A/c (5,000 shares forfeited for non-payment of allotment and call money)		50,000	 18,000 32,000
(ii)	Bank A/c Dr. To Share Capital A/c To Securities Premium A/c (3,000 shares re-issued @ ₹ 12 per share)		36,000	 30,000 6,000
(iii)	Share Forfeited A/c Dr. To Capital Reserve A/c (Gain on re-issue of forfeited shares transferred to capital reserve)		10,800	 10,800

(ii)

Books of Ratan Ltd.

Journal Entries

Date	Particular	L.F	Debit (₹)	Credit (₹)
	Share Capital A/c Dr. To Share Forfeited A/c To Calls in Arrears A/c (3,000 shares forfeited for non-payment of first call money)		21,000	 15,000 6,000
	Bank A/c Dr. To Share Capital A/c (2,000 shares re-issued @ ₹ 10 per share)		20,000	 20,000
	Share Forfeited A/c Dr. To Capital Reserve A/c (Gain on re-issue of forfeited shares transferred to capital reserve)		10,000	 10,000

24. Dr. Revaluation Account Cr. 6

Particulars	Amount (₹)	Particulars	Amount (₹)
To Partner's Capital A/c: X 19,200		Plant and Machinery Buildings A/c	14,000 11,000

Y 12,800	32,000	Provisions for Doubtful Debt A/c	7,000
	32,000		32,000

Dr. Partner's Capital Accounts Cr.

Particulars	X	Y	Z	Particulars	X	Y	Z
Y's Current A/c	----	24,000	----	Balance b/d	1,19,000	1,12,000	—
Balance c/d	1,68,000	1,12,000	56,000	Bank A/c	—	—	56,000
				Z's Current A/c	8,400	5,600	—
				General Reserve A/c	8,400	5,600	—
				Revaluation A/c	19,200	12,800	—
				X's Current A/c	13,000		
	1,68,000	1,36,000	56,000		1,68,000	1,36,000	56,000

OR

Dr. Revaluation A/c Cr.

Particulars	Amount(₹)	Particulars	Amount(₹)
To Provision for Doubtful Debts	400	By Building A/c	7,000
To Partner's Capital A/c:			
P 3,300			
Q 2,200			
R 1,100	6,600		
	7,000		7,000

Dr. Partner's Capital Accounts Cr.

Particulars	P	Q	R	Particulars	P	Q	R
Goodwill A/c	13,500	—	4,500	Balance b/d	15,000	10,000	10,000
Profit & Loss	600	400	200	Revaluation A/c	3,300	2,200	1,100
Cash	—	2,800	—	Goodwill A/c	9,000	6,000	3,000
Q's Loan	—	15,000	—	R's Current A/c	----	----	1,900
P's Current A/c	1,900	—	----				
Balance c/d	11,300	----	11,300				
	27,300	18,200	16,000		27,300	18,200	16,000

25. Journal Entries 6

Date	Particulars	L.F.	Dr. Amount	Cr. Amount
2019 June 30	Profit and Loss Suspense A/c Dr. To A's Capital A/c (Being share of profit provided till the date of his death)		1,20,000	1,20,000

Dr. A's Executors A/c Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
2019 June 30	Furniture A/c		2,40,000	2019 June 30	A's Capital A/c		8,40,000
2020 Mar.31	Balance c/d		6,27,000	2020 Mar.31	Interest A/c		27,000
			8,67,000				8,67,000

2020 June 30 2021 Mar. 31	Bank A/c Balance c/d		2,36,000 4,18,000	2020 Apr. 1 June 30 2021 Mar. 31	Balance b/d Interest A/c Interest A/c		6,27,000 9,000 18,000
			6,54,000				6,54,000
2021 June 30 2022 Mar. 31	Bank A/c Balance c/d		2,24,000 2,09,000	2021 Apr. 1 June 30 2022 Mar. 31	Balance b/d Interest A/c Interest A/c		4,18,000 6,000 9,000
			4,33,000				4,33,000
2022 June 30	Bank A/c		2,12,000	2021 Apr. 1 June 30	Balance b/d Interest A/c		2,09,000 3,000
			2,12,000				2,12,000

26. Books of Health2Wealth Ltd. — 6 (2+2+2)

a) Journal Entries

Date	Particulars	L.F	Debit (₹)	Credit (₹)
(i)	Bank A/c Dr. To Debenture Application and Allotment A/c (Application money received)		55,00,000	 55,00,00
(ii)	Debenture Application and Allotment A/c Dr. Loss on Issue of Debentures A/c Dr. To 8% Debentures A/c To Securities Premium A/c To Premium on Redemption of Debentures A/c (Debenture issued at premium, to be redeemed at premium)		55,00,000 10,00,000	 50,00,000 5,00,000 10,00,000

b)

Dr. Loss on Issue of Debentures A/c Cr.

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
2021 1 Oct.	To Premium on Redemption of Debentures	10,00,000	2022 31 Mar.	By Securities Premium A/c By Statement of Profit and Loss A/c	7,80,000 2,20,000
		10,00,000			10,00,000

c) Journal Entries

Date	Particulars	L.F	Debit (₹)	Credit (₹)
31 Mar. 2022	Debenture Interest A/c Dr. To Debentureholders A/c (Interest due on debentures)		2,00,000	 2,00,000
31	Debentureholders A/c Dr.		2,00,000	

	Mar. 2022	To Bank A/c (Interest paid to debentureholders)			2,00,000		
	31 Mar. 2022	Statement of Profit and Loss Dr. To Debenture Interest A/c (Interest on Debentures charged to Statement of Profit and Loss)		2,00,000	2,00,000		

Part B :- Analysis of Financial Statements
Option -I

27.	c) Postulates Or c) Only (ii) and (iii) are correct	1
28.	b) 3 times	1
29.	d) Subtracted under Operating Activities as Extraordinary Item and Inflow under Investing Activities also Or c) Added ₹ 1,30,000 under Operating Activities as Loss on Issue of Debentures written off and Inflow of ₹ 18,00,000 under Financing Activities.	1
30.	b) ₹ 1,02,000	1
31.	(see table below)	3

Item	Heading	Sub – Heading
(i) Current maturities of long term debts	Current Liabilities	Short term borrowings
(ii) Furniture and Fixtures	Non – Current Assets	Property, Plant and Equipments and Intangible Assets Property, Plant and Equipments
(iii) Provision for Warranties	Non – Current Liabilities	Long Term Provisions
(iv) Income received in advance	Current Liabilities	Other Current Liabilities
(v) Capital Advances	Non – Current Assets	Long Term Loans and Advances
(vi) Advances recoverable in cash within the operation cycle	Current Assets	Short Term Loans and Advances

32.	Variations of Accounting Practice as Limitation is highlighted in the given statement.	3

	Two Other Limitations (Any two of the following, with suitable explanation) (a) Limitations of Accounting Data (b) Ignores Price-level Changes (c) Ignore Qualitative or Non-monetary Aspects (d) Forecasting	
33.	Return on Investment = EBIT / Capital Employed x 100 = 15,00,000/1,20,00,000 x 100 = 12.5% Capital Employed = 12% Preference Share Capital + Equity Share Capital + Reserves and Surplus + 15% Debentures + 10% Bank Loan = 30,00,000 + 40,00,000 + 10,00,000 + 20,00,000 + 20,00,000 = ₹ 1,20,00,000 EBIT = Profits after Tax + Tax + Interest = 6,00,000 + 4,00,000 + 5,00,000 = ₹ 15,00,000 Net Assets Turnover ratio = Revenue from Operations/Capital Employed = 3,60,00,000/1,20,00,000 = 3 times Or (i) Ratio will improve. Reason – Capital Employed will decrease and Debt will remain same (ii) Ratio will remain same. Reason – Both Debt and Capital Employed will remain same. (iii) Ratio will decline. Reason – Debt will decrease but Capital Employed will remain same. (iv) Ratio will decline. Reason – Capital Employed will increase but Debt will remain same.	4
34.	1. Net Profit before tax and extraordinary items=Net Profit for the year+ Interim Dividend + Loss of assets due to fire + Provision for Tax + Proposed Dividend - Insurance claim received for Loss due to Fire – Tax refund = 7,50,000 + 90,000 + 20,000 + 80,000 + 1,60,000 – 10,000 – 20,000 = ₹ 10,70,000 2. Operating profit before working capital changes= Net Profit before tax and extraordinary items + Adjustments for non-cash and non-operating expenses and goodwill amortised – Adjustments for non-cash and non-operating incomes = 10,70,000 + 40,000 + 70,000** – 30,000 = 11,50,000 ** Goodwill amortised = Opening goodwill + Goodwill purchased - Closing goodwill 3. Cash flow from Investing Activities = Interest on Non-Current Investments + Insurance claim for loss of assets due to fire – Purchase of Investments – Purchase of Machinery – Goodwill purchased = 30,000 + 10,000 – 1,00,000 - 1,60,000 – 20,000 = ₹ (2,40,000) Outflow 4. Cash flow from Financing Activities: Raise of Bank overdraft – Interim Dividend Paid – Final Dividend paid = 50,000 – 90,000 – 1,60,000 = ₹ (2,00,000) Outflow 5. Closing Cash and Cash Equivalents : Cash in Hand + Investment in Marketable Securities = 2,00,000 + 1,50,000 =3,50,000	6 (1.5+ 1.5+ 1+ 1+ 1)

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