# XII – ACCOUNTANCY

**Name :**

**Class : Sec:**

**School :**

# BLUE STARS HIGHER SECONDARY SCHOOL

## XII – ACCOUNTANCY

## UNIT 1 ACCOUNTS FROM INCOMPLETE RECORDS

### I. Multiple Choice Questions

#### Choose the correct answer

1. Incomplete records are generally maintained by
   (a) A company
   (b) Government
   (c) Small sized sole trader business
   (d) Multinational enterprises
   [Ans. (c) Small sized sole trader business]

2. Statement of affairs is a
   (a) Statement of income and expenditure
   (b) Statement of assets and liabilities
   (c) Summary of cash transactions
   (d) Summary of credit transactions
   [Ans. (b) Statement of assets and liabilities]

3. Opening statement of affairs is usually prepared to find out the
   (a) Capital in the beginning of the year
   (b) Capital at the end of the year
   (c) Profit made during the year
   (d) Loss occurred during the year
   [Ans. (a) Capital in the beginning of the year]

4. The excess of assets over liabilities is
   (a) Loss (b) Cash
   (c) Capital (d) Profit
   [Ans. (c) Capital]

5. Which of the following items relating to bills payable is transferred to total creditors account?
   (a) Opening balance of bills payable
   (b) Closing balance of bills payable
   (c) Bills payable accepted during the year
   (d) Cash paid for bills payable
   [Ans. (c) Bills payable accepted during the year]

6. The amount of credit sales can be computed from
   (a) Total debtors account
   (b) Total creditors account
   (c) Bills receivables account
   (d) Bills payable account
   [Ans. (a) Total debtors account]

7. Which one of the following statements is not true in relation to incomplete records?
   (a) It is an unscientific method of recording transactions
   (b) Records are maintained only for cash and personal accounts
   (c) It is suitable for all types of organisations
   (d) Tax authorities do not accept
   [Ans. (c) It is suitable for all types of organisations]

**8. What is the amount of capital of the proprietor, if his assets are ₹ 85,000 and liabilities are ₹ 21,000?.**

(a) ₹ 85,000 (b) ₹ 1,06,000

(c) ₹ 21,000 (d) ₹ 64,000

[Ans. (d) ₹ 64,000]

*Hint:*

Capital = Assets – Liabilities

= ₹ 85,000 – ₹ 21,000 = ₹ 64,000

**9. When capital in the beginning is ₹ 10,000, drawings during the year is ₹ 6,000, profit made during the year is ₹ 2,000 and the additional capital introduced is ₹ 3,000, find the amount of capital at the end.**

(a) ₹ 9,000 (b) ₹ 11,000

(c) ₹ 21,000 (d) ₹ 3,000

[Ans. (a) ₹ 9,000]

*Hint:*

| Particulars | ₹ |
|---|---|
| Capital at the end | 9,000 |
| Add: Drawings | 6,000 |
| | 15,000 |
| Less: Additional Capital introduced | 3,000 |
| | 12,000 |
| Less: Opening Capital | 10,000 |
| Profit | 2,000 |

**10. Opening balance of debtors: ₹ 30,000, cash received: ₹1,00,000, credit sales: ₹ 90,000; closing balance of debtors is**

(a) ₹ 30,000 (b) ₹ 1,30,000

(c) ₹ 40,000 (d) ₹ 20,000

[Ans. (d) ₹ 20,000]

*Hint :*

Dr Total Debtors account Cr

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance c/d | 30,000 | By Cash A/c (Received) | 1,00,000 |
| To Credit Sales | 90,000 | By Balance b/d | 20,000 |
| | 1,20,000 | | 1,20,000 |

## II. Very short answer questions

**1. What is meant by incomplete records?**

**Ans.** (i) When accounting records are not strictly maintained according to double entry system, these records are called as incomplete accounting records.

(ii) Generally, cash account and the personal accounts of customers and creditors are maintained fully and other accounts are maintained based on necessity.

**2. State the accounts generally maintained by small sized sole trader when double entry accounting system is not followed.**

**Ans.** Incomplete accounting records.

**3. What is a statement of affairs?**

**Ans.** A statement of affairs is a statement showing the balances of assets and liabilities on a particular date. This method of ascertaining profit is also called as statement of affairs method or networth method or capital comparison method.

## III. Short answer questions

**1. What are the features of incomplete records?.**

**Ans.** (i) **Nature:**

It is an unscientific and unsystematic way of recording transactions. Accounting principles and accounting standards are not followed properly.

(ii) **Lack of uniformity:**

There is no uniformity in recording the transactions among different organisations. Different organisations record their transactions according to their needs and conveniences.

(iii) **Suitability:**

Only the business concerns which have no legal obligation to maintain books of accounts under double entry system may maintain incomplete records. Hence, it may be maintained by small sized sole traders and partnership firms.

**2. What are the limitations of incomplete records?**

**Ans.** (i) **Lack of proper maintenance of records:**

It is an unscientific and unsystematic way of maintaining records. Real and nominal accounts are not maintained properly.

(ii) **Difficulty in preparing trial balance:**

As accounts are not maintained for all items, the accounting records are incomplete. Hence, trial balance cannot be prepared to test the arithmetical accuracy of the accounts.

(iii) **Difficulty in ascertaining true profitability of the business:**

Profit is found out based on available information and estimates. Hence, it is difficult to ascertain true profit as the trading and profit and loss account cannot be prepared with accuracy.

(iv) **Errors and frauds cannot be detected easily:**

As only partial records are available, it may not be possible to have internal checks in maintaining accounts to detect errors and frauds.

**3. State the differences between double entry system and incomplete records.**

**Ans.**

| S. No. | Basis of distinction | Double entry system | Incomplete records |
|---|---|---|---|
| 1. | Recording of transaction | Both debit and credit aspects of all the transactions are recorded | Debit and credit aspects of all the transactions are not recorded completely. |
| 2. | Type of accounts maintained | Personal, real and nominal accounts are maintained fully | In general, Only personal and cash accounts are maintained fully. Real and nominal accounts are not maintained fully. |
| 3. | Preparation of trial balance | Trial balance can be prepared to check the arithmetical accuracy of the entries made in the books of accounts. | Trial balance cannot be prepared to check arithmetic accuracy of entries made in the books of accounts. |
| 4. | Suitability | It is suitable for all types of organisations | It may be suitable for small sized sole traders and partnership firms. |
| 5. | Reliability | It is reliable | It is not reliable. |

**4. State the procedure for calculating profit or loss through statement of affairs.**

**Ans.** Following are the steps to be followed under the statement of affairs method to find out the profit or loss.

(1) Ascertain the opening capital by preparing a statement of affairs at the beginning of the year by taking the opening balances of assets and liabilities.

(2) Ascertain the closing capital by preparing a statement of affairs at the end of the accounting period after making all adjustments such as depreciation, bad debts, outstanding and prepaid expenses, outstanding income, interest on capital, interest on drawings, etc.

(3) Add the amount of drawings (both in cash and/in kind) to the closing capital.

(4) Deduct the amount of additional capital introduced, to get adjusted closing capital.

(5) Ascertain profit or loss by subtracting opening capital from the adjusted closing capital.

a) If adjusted closing capital is more than the opening capital, it denotes profit

b) If adjusted closing capital is lesser than the opening capital, it denotes loss

Following format is used to find out the profit or loss:

**Statement of Profit or loss for the year ended ..........**

| Particulars | ₹ |
|---|---|
| Capital at the end of the year | xxxx |
| **Add:** Drawings during the year | xxxx |
| | xxxx |
| **Less:** Additional capital introduced during the year | xxxx |
| Adjusted closing capital | xxxx |
| **Less:** Opening Capital | xxxx |
| Profit or loss for the year | xxxx |

**5. Differentiate between statement of affairs and balance sheet.**

***Ans.***

| S. No. | Basis of distinction | Statement of affairs | Balance Sheet |
|---|---|---|---|
| 1. | Objective | Statement of affairs is prepared to find out the capital of the business. | Balance sheet is prepared to ascertain the financial position of the business. |
| 2. | Accounting system | Statement of affairs is prepared when double entry system is not strictly followed. | Balance sheet is prepared when accounts are maintained under double entry system. |
| 3. | Basis of preparation | It is not fully based on ledger balances. | It is prepared exclusively on the basis of ledger balances. |
| 4. | Reliability | It is not reliable as it is based on incomplete records. | It is reliable as it prepared under double entry system. |
| 5. | Missing items | It is difficult to trace the items omitted as complete records are not maintained. | Since both the aspects of all transactions are duly recorded, items omitted can be traced easily. |

**6. How is the amount of credit sale ascertained from incomplete records?**

***Ans.*** Total sales are calculated by adding cash and credit sales. Cash sales are given in cash book. For ascertaining the amount of credit sales, the total debtors account should be prepared. The specimen of total debtors account is given below.

**Dr** **Total debtors account** **Cr**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balace b/d (Op. Bal.) | xxxx | By Cash received | xxxx |
| To Credit sales (Bal. Fi.) | xxxx | By Discount allowed | xxxx |
| | | By Sales returns | xxxx |
| | | By balance c/d (Clos. Bal) | xxxx |
| | xxxx | | xxxx |

## IV EXERCISES

1. From the following particulars ascertain profit or loss:

| Particulars | ₹ |
|---|---|
| Capital at the beginning of the year (1st April, 2018) | 5,00,000 |
| Capital at the end of the year (31st March, 2019) | 8,50,000 |
| Additional capital introduced during the year | 1,20,000 |
| Drawings during the year | 70,000 |

*Solution :*

**Statement of profit or loss for the year ending 31st March 2019**

| Particulars | ₹ |
|---|---|
| Closing capital (as on 31.03.2019) | 8,50,000 |
| **Add :** Drawings during the year | 70, 000 |
| | 9,20,000 |
| **Less:** Additional capital introduced during the year | 1,20,000 |
| Adjusted closing capital | 8,00,000 |
| **Less:** Opening capital (as on 1st April, 2018) | 5,00,000 |
| Profit for the year | **3,00,000** |

2. From the following particulars ascertain profit or loss.

| Particulars | ₹ |
|---|---|
| Capital as on 1st January 2018 | 2,20,000 |
| Capital as on 31st December 2018 | 1,80,000 |
| Additional capital introduced during the year | 40,000 |
| Drawings made during the year | 50,000 |

*Solution :*

**Statement of profit or loss for the year ending 31st December 2018**

| Particulars | ₹ |
|---|---|
| Closing capital as on 31st December 2018 | 1,80,000 |
| **Add :** Drawings during the year | 50, 000 |
| | 2,30,000 |
| **Less:** Additional capital introduced during the year | 40,000 |
| Adjusted closing capital | 1,90,000 |
| **Less:** Opening capital as on 1st January, 2018 | 2,20,000 |
| Loss for the year | **30,000** |

16. From the following details you are required to calculate credit sales and credit purchases by preparing total debtors account, total creditors account, bills receivable account and bills payable account.

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| **Balances as on 1st April 2018** | | **Balances as on 31st March 2019** | |
| Sundry debtors | 2,40,000 | Sundry debtors | 2,20,000 |
| Bills receivable | 30,000 | Sundry creditors | 1,50,000 |
| Sundry creditors | 1,20,000 | Bills receivable | 8,000 |
| Bills payable | 10,000 | Bills payable | 20,000 |
| **Other information:** | ₹ | | ₹ |
| Cash received from debtors | 6,00,000 | Payments against bill payable | 30,000 |
| Discount allowed to customers | 25,000 | Cash received for bills receivable | 60,000 |
| Cash paid to creditors | 3,20,000 | Bills receivable dishonoured | 4,000 |
| Discount allowed by suppliers | 10,000 | Bad debts | 16,000 |

*Solution :*

**Dr Bills receivable account Cr**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance b/d | 30,000 | By Cash | 60,000 |
| To Debtors (Bills received - balancing figure) | 42,000 | By Debtors (Bills receivable dishonoured) | 4,000 |
| | | By Balance c/d | 8,000 |
| | 72,000 | | 72,000 |

**Dr Total Debtors account Cr**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance b/d | 2,40,000 | By Cash received | 6,00,000 |
| To Bills receivable (dishonored) | 4,000 | By Discount allowed | 25,000 |
| To Sales (credit) (balancing figure) | 6,59,000 | By Bad debts | 16,000 |
| | | By Bills receivable (bills received) | 42,000 |
| | | By Balance c/d | 2,20,000 |
| | 9,03,000 | | 9,03,000 |

**Dr Bills payable account Cr**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Cash (Bills paid) | 30,000 | By Balance b/d | 10,000 |
| To Balance c/d | 20,000 | By Sundry creditors (Bills accepted balancing figure) | 40,000 |
| | 50,000 | | 50,000 |

Dr **Total Creditors account** Cr

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Cash (paid) | 3,20,000 | By Balance b/d | 1,20,000 |
| To Discount received | 10,000 | By purchases (credit) (balancing figure) | **4,00,000** |
| To Bills payable (Bills accepted) | 40,000 | | |
| To Balance c/d | 1,50,000 | | |
| | 5,20,000 | | 5,20,000 |

**17. From the following details of Rakesh, prepare Trading and Profit and Loss account for the year ended 31st March, 2019 and a Balance Sheet as on that date.**

| Particulars | 31.3.2018 ₹ | 31.3.2019 ₹ |
|---|---|---|
| Stock of goods | 2,20,000 | 1,60,000 |
| Debtors | 5,30,000 | 6,40,000 |
| Cash at bank | 60,000 | 10,000 |
| Machinery | 80,000 | 80,000 |
| Sundry creditors | 3,70,000 | 4,20,000 |

**Other details :**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| Rent paid | 1,20,000 | Cash received from debtors | 12,50,000 |
| Discount received | 35,000 | Drawings | 1,00,000 |
| Discount allowed | 25,000 | Cash sales | 20,000 |
| Cash paid to creditors | 11,00,000 | Capital as on 1.4.2018 | 5,20,000 |

*Solution :*

Dr **Total Debtors account** Cr

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance b/d | 5,30,000 | By Cash received | 12,50,000 |
| To Credit sales (balancing figure) | **13,85,000** | By Discounts allowed | 25,000 |
| | | By Balance c/d | 6,40,000 |
| | 19,15,000 | | 19,15,000 |

Dr **Total Creditors account** Cr

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Cash (paid) | 11,00,000 | By Balance b/d | 3,70,000 |
| To Discount received | 35,000 | By Credit purchases (balancing figure) | **11,85,000** |
| To Balance c/d | 4,20,000 | | |
| | 15,55,000 | | 15,55,000 |

**In the Books of Rakash Trading and Profit and loss account for the year ended 31st March 2019**

Dr. Cr.

| Particulars | ₹ | Particulars | | ₹ |
|---|---|---|---|---|
| To Opening stock | 2,20,000 | By Sales | | |
| To Purchases | 11,85,000 | Cash sales | 20,000 | |
| To Gross profit c/d | 1,60,000 | Credit sales | 13,85,000 | 14,05,000 |
| | | By Closing stock | | 1,60,000 |
| | 15,65,000 | | | 15,65,000 |
| To Rent paid | 1,20,000 | By Gross Profit b/d | | 1,60,000 |
| To Discount allowed | 25,000 | By Discount received | | 35,000 |
| To Net profit (transferred to capital account) | 50,000 | | | |
| | 1,95,000 | | | 1,95,000 |

**Balance sheet as on 31st March 2019**

| Liabilities | ₹ | ₹ | Assets | ₹ |
|---|---|---|---|---|
| Sundry creditors | | 4,20,000 | Debtors | 6,40,000 |
| Capital | 5,20,000 | | Cash at bank | 10,000 |
| Add : Net profit | 50,000 | | Machinery | 80,000 |
| | 5,70,000 | | Closing stock | 1,60,000 |
| Less : Drawings | 1,00,000 | 4,70,000 | | |
| | | 8,90,000 | | 8,90,000 |

**18.** **Mary does not keep her books under double entry system. From the following details prepare trading and profit and loss account for the year ending 31st March, 2019 and a balance sheet as on that date.**

Dr **Cash Book** Cr

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance b/d | 1,20,000 | By Purchases | 1,50,000 |
| To Sales | 3,60,000 | By Creditors | 2,50,000 |
| To Debtors | 3,40,000 | By Wages | 70,000 |
| | | By Sundry expenses | 1,27,000 |
| | | By Balance c/d | 2,23,000 |
| | 8,20,000 | | 8,20,000 |

**Other information :**

| Particulars | 1.4.2018 ₹ | 31.3.2019 ₹ |
|---|---|---|
| Stock of goods | 1,10,000 | 1,80,000 |
| Sundry Debtors | 1,30,000 | ? |
| Sundry Creditors | 1,60,000 | 90,000 |
| Furniture and fittings | 80,000 | 80,000 |

**Additional information :**

| | ₹ |
|---|---|
| Credit purchases | 1,80,000 |
| Credit sales | 2,90,000 |
| Opening capital | 2,80,000 |

Depreciate furniture and fittings by 10% p.a

*Solution :*

**In the books of Mary**

**Total Debtors account**

Dr. Cr.

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance b/d | 1,30,000 | By Cash (received) | 3,40,000 |
| To Sales (Credit) | 2,90,000 | By Balance c/d (balancing figure) | 80,000 |
| | 4,20,000 | | 4,20,000 |
| To Balance b/d | 80,000 | | |

**Trading and Profit and loss account for the year ended 31st March 2019**

Dr. Cr.

| Particulars | ₹ | ₹ | Particulars | ₹ | ₹ |
|---|---|---|---|---|---|
| To Opening stock | | 1,10,000 | By Sales | | |
| To Purchases | | | Cash | 3,60,000 | |
| Cash | 1,50,000 | | Credit | 2,90,000 | 6,50,000 |
| Credit | 1,80,000 | 3,30,000 | By Closing stock | | 1,80,000 |
| To Wages | | 70,000 | | | |
| To Gross profit c/d | | 3,20,000 | | | |
| | | 8,30,000 | | | 8,30,000 |
| To Sundry expenses | | 1,27,000 | By Gross profits b/d | | 3,20,000 |
| To Depreciation on machinery 10% | | 8,000 | | | |
| To Net profit transfered to capital a/c | | 1,85,000 | | | |
| | | 3,20,000 | | | 3,20,000 |

**Balance sheet as on 31st March 2019**

| Liabilities | ₹ | ₹ | Assets | ₹ | ₹ |
|---|---|---|---|---|---|
| Capital | 2,80,000 | | Cash | | 2,23,000 |
| Add : Net profit | 1,85,000 | 4,65,000 | Stock of goods | | 1,80,000 |
| | | | Debtors | | 80,000 |
| Creditors | | 90,000 | Furniture and fittings | 80,000 | |
| | | | Less : Depreciation | 8,000 | 72,000 |
| | | 5,55,000 | | | 5,55,000 |

**19. Arun carries on hardware business and does not keep his books on double entry basis. The following particulars have been extracted from his books:**

| Particulars | 31.12.2017 ₹ | 31.12.2018 ₹ |
|---|---|---|
| Land and building | 2,40,000 | 2,40,000 |
| Stock-in-trade | 1,20,000 | 1,70,000 |
| Debtors | 40,000 | 51,500 |
| Creditors | 50,000 | 45,000 |
| Cash at bank | 30,000 | 53,000 |

**Other information for the year ending 31.12.2018 showed the following:**

| | ₹ |
|---|---|
| Wages | 65,000 |
| Carriage outwards | 7,500 |
| Sundry expense | 28,000 |
| Cash paid to creditors | 6,00,000 |
| Drawings | 10,000 |

**Total sales during the year were ₹7,70,000. Purchases returns during the year wer ₹30,000 and sales returns were ₹25,000. Depreciate land and buildings by 5%. Provid ₹1,500 for doubtful debts. Prepare trading and profit and loss account for the year ending 31 December, 2018 and a balance sheet as on that date.**

***Solution :*** **In the books of Arun**

**Statement of affairs as on 1st December 2018**

| Liabilities | ₹ | Assets | ₹ |
|---|---|---|---|
| Creditors | 50,000 | Land and Building | 2,40,000 |
| Opening capital | 3,80,000 | Stock in trade | 1,20,000 |
| (balancing figure) | | Debtors | 40,000 |
| | | Cash at bank | 30,000 |
| | 4,30,000 | | 4,30,000 |

**Dr** **Total Creditors account** **Cr**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Cash (paid) | 6,00,000 | By Balance b/d | 50,000 |
| To Purchase returns | 30,000 | By Credit purchases | 6,25,000 |
| To Balance c/d | 45,000 | (balancing figure) | |
| | 6,75,000 | | 6,75,000 |

**Trading and Profit and loss account for the year ended 31st December 2018**

**Dr.** **Cr.**

| Particulars | ₹ | ₹ | Particulars | ₹ | ₹ |
|---|---|---|---|---|---|
| To Opening stock | | 1,20,000 | By sales | 7,70,000 | |
| To Purchases credit | 6,25,000 | | Less : Sales returns | 25,000 | 7,45,000 |
| Less : Purchase returns | 30,000 | 5,95,000 | By Closing stock | | 1,70,000 |
| To Wages | | 65,000 | | | |
| To Gross profit c/d | | 1,35,000 | | | |
| | | 9,15,000 | | | 9,15,000 |
| To Carriage outwards | | 7,500 | By Gross profits c/d | | 1,35,000 |
| To Sundry expenses | | 28,000 | | | |
| To Depreciation on land and building @ 5% | | 12,000 | | | |
| To Provision for doubtful debts | | 1,500 | | | |
| To Net profit transfered to capital account | | 86,000 | | | |
| | | 1,35,000 | | | 1,35,000 |

**Balance sheet as on 31st December 2018**

| Liabilities | ₹ | ₹ | Assets | ₹ | ₹ |
|---|---|---|---|---|---|
| Capital | 3,80,000 | | Land and buildings | 2,40,000 | |
| Add : Net profit | 86,000 | | Less : Depreciation 5% | 12,000 | 2,28,000 |
| | 4,66,000 | | Closing stock | | 1,70,000 |
| Less : Drawings | 10,000 | 4,56,000 | Debtors | 51,500 | |
| | | | Less : Provision for debtors | 1,500 | 50,000 |
| Creditors | | 45,000 | Cash at bank | | 53,000 |
| | | 5,01,000 | | | 5,01,000 |

**20.** **Selvam does not keep his books under double entry system. From the following information prepare trading and P&L A/c and Balance Sheet as on 31-12-2018**

| Particulars | 1.1.2018 ₹ | 31.12.2018 ₹ |
|---|---|---|
| Machinery | 60,000 | 60,000 |
| Cash at bank | 25,000 | 33,000 |
| Sundry debtors | 70,000 | 1,00,000 |
| Stock | 45,000 | 22,000 |
| Bills receivable | 20,000 | 38,000 |
| Bank loan | 45,000 | 45,000 |
| Sundry creditors | 25,000 | 21,000 |

| | ₹ | | ₹ |
|---|---|---|---|
| Cash sales | 20,000 | Credit sales | 1,80,000 |
| Cash purchases | 8,000 | Credit purchases | 52,000 |
| Wages | 6,000 | Salaries | 23,500 |
| Advertisement | 7,000 | Interest on bank loan | 4,500 |
| Drawings | 60,000 | Additional capital | 21,000 |

**Adjustments:**

Write off depreciation of 10% on machinery. Create a reserve of 1% on debtors for doubtful debts.

*Solution :* **In the books of selvam**

**Statement of affairs as on 1st January 2018**

| Liabilities | ₹ | Assets | ₹ |
|---|---|---|---|
| Bank Loan | 45,000 | Machinery | 60,000 |
| Sundry creditors | 25,000 | Cash at bank | 25,000 |
| Opening capital | 1,50,000 | Sundry debtors | 70,000 |
| (Balancing figure) | | Stock | 45,000 |
| | | Bills receivable | 20,000 |
| | 2,20,000 | | 2,20,000 |

### Trading and Profit and loss account for the year ended 31st December 2018

Dr. Cr.

| Particulars | ₹ | ₹ | Particulars | ₹ | ₹ |
|---|---|---|---|---|---|
| To Opening stock | | 45,000 | By Sales | | |
| To Purchase | | | Cash | 20,000 | |
| Cash | 8,000 | | Credit | 1,80,000 | 2,00,000 |
| Credit | 52,000 | 60,000 | By Closing stock | | 22,000 |
| To Wages | | 6,000 | | | |
| To Gross profit c/d | | **1,11,000** | | | |
| | | 2,22,000 | | | 2,22,000 |
| To Advertisement | | 7,000 | By Gross profit b/d | | 1,11,000 |
| To Salaries | | 23,500 | | | |
| To Depreciation 10% | | 6,000 | | | |
| To Reserve on debtors 1 % | | 1,000 | | | |
| To Interest on bank loan | | 4,500 | | | |
| To Net profit transfered to capital a/c | | **69,000** | | | |
| | | 1,11,000 | | | 1,11,000 |

### Balance sheet as on 31st December 2018

| Liabilities | ₹ | ₹ | Assets | ₹ | ₹ |
|---|---|---|---|---|---|
| Bank loan | | 45,000 | Machinery | 60,000 | |
| Sundry creditors | | 21,000 | Less : Depreciation 10% | 6,000 | 54,000 |
| Capital | 1,50,000 | | Cash at bank | | 33,000 |
| Add : Net profit | 69,000 | | Sundry debtors | 1,00,000 | |
| | 2,19,000 | | Less : Reserve for doubtful debts | 1,000 | 99,000 |
| Add : Additional capital | 21,000 | | Closing stock | | 22,000 |
| | 2,40,000 | | Bills receivable | | 38,000 |
| Less : Drawings | 60,000 | 1,80,000 | | | |
| | | 2,46,000 | | | 2,46,000 |

## Fill in the missing information

**Text Book No. 38**

| Closing capital ₹ | Drawings ₹ | Additional capital ₹ | Opening capital ₹ | Profit / Loss ₹ |
|---|---|---|---|---|
| 1,00,000 | 40,000 | 20,000 | 90,000 | ? |
| ? | 30,000 | 40,000 | 80,000 | 20,000 |
| 70,000 | ? | 30,000 | 40,000 | 10,000 |
| 60,000 | 20,000 | ? | 50,000 | –10,000 |
| 2,00,000 | 30,000 | 10,000 | ? | 1,20,000 |

*Solution :*

| Closing capital ₹ | Drawings ₹ | Additional capital ₹ | Opening capital ₹ | Profit / Loss ₹ |
|---|---|---|---|---|
| 1,00,000 | 40,000 | 20,000 | 90,000 | **30,000** |
| **1,10,000** | 30,000 | 40,000 | 80,000 | 20,000 |
| 70,000 | **10,000** | 30,000 | 40,000 | 10,000 |
| 60,000 | 20,000 | **40,000** | 50,000 | –10,000 |
| 2,00,000 | 30,000 | 10,000 | **1,00,000** | 1,20,000 |

# UNIT 2 ACCOUNTS OF NOT-FOR-PROFIT ORGANISATION

## I MULTIPLE CHOICE QUESTIONS

### CHOOSE THE CORRECT ANSWER

1. Receipts and payments account is a
   (a) Nominal A/c
   (b) Real A/c
   (c) Personal A/c
   (d) Representative personal account
   [Ans. (b) Real A/c]

2. Receipts and payments account records receipts and payments of
   (a) Revenue nature only
   (b) Capital nature only
   (c) Both revenue and capital nature
   (d) None of the above
   [Ans. (c) Both revenue and capital nature]

3. Balance of receipts and payments account indicates the
   (a) Loss incurred during the period
   (b) Excess of income over expenditure of the period
   (c) Total cash payments during the period
   (d) Cash and bank balance as on the date
   [Ans. (d) Cash and bank balance as on the date]

4. Income and expenditure account is a
   (a) Nominal A/c
   (b) Real A/c
   (c) Personal A/c
   (d) Representative personal account
   [Ans. (a) Nominal A/c]

5. **Income and Expenditure Account is prepared to find out**
   (a) Profit or loss
   (b) Cash and bank balance
   (c) Surplus or deficit
   (d) Financial position
   [Ans. (c) Surplus or deficit]

6. **Which of the following should not be recorded in the income and expenditure account?**
   (a) Sale of old news papers
   (b) Loss on sale of asset
   (c) Honorarium paid to the secretary
   (d) Sale proceeds of furniture
   [Ans. (d) Sale proceeds of furniture]

7. **Subscription due but not received for the current year is**
   (a) An asset
   (b) A liability
   (c) An expense
   (d) An item to be ignored [Ans. (a) An asset]

8. **Legacy is a**
   (a) Revenue expenditure
   (b) Capital expenditure
   (c) Revenue receipt
   (d) Capital receipt [Ans. (d) Capital receipt]

9. **Donations received for a specific purpose is**
   (a) Revenue receipt
   (b) Capital receipt
   (c) Revenue expenditure
   (d) Capital expenditure
   [Ans. (b) Capital receipt]

10. **There are 500 members in a club each paying ₹ 100 as annual subscription. Subscription due but not received for the current year is ₹ 200; Subscription received in advance is ₹ 300. Find out the amount of subscription to be shown in the income and expenditure account.**
   (a) ₹ 50,000 (b) ₹ 50,200
   (c) ₹ 49,900 (d) ₹ 49,800
   [Ans. (a) ₹ 50,000]

## II VERY SHORT ANSWER QUESTIONS

1. **State the meaning of not-for-profit organisation.**

*Ans.* (i) Some organisations are established for the purpose of rendering services to the public without any profit motive.
(ii) They may be created for the promotion of art, culture, education, sports, etc. These organisations are called not-for-profit organisation.
(iii) Charitable institutions, educational institutions, cultural societies, sports and recreation clubs, hospitals, libraries and literary associations are some of the examples of not-for-profit organisations.

2. **What is receipts and payments account?**

*Ans.* (i) Receipts and Payments account is a summary of cash and bank transactions of not-for-profit organisations prepared at the end of each financial year.
(ii) It is a real account in nature. The receipts and payments account begins with the opening balances of cash and bank and ends with closing balances of cash and bank.

3. **What is legacy?**

*Ans.* A gift made to a not-for-profit organisation by a will, is called legacy. It is a capital receipt.

4. **Write a short note on life membership fees.**

*Ans.* Amount received towards life membership fee from members is a capital receipt as it is non-recurring in nature.

5. **Give four examples for capital receipts of not-for-profit organisation.**

*Ans.* (i) Life membership fee
(ii) Endowment fund
(iii) Sale of fixed assets
(iv) Specific donations.

6. **Give four examples for revenue receipts of not-for-profit organisation.**

*Ans.* (i) Interest on investment
(ii) Interest on fixed deposit
(iii) Sale of (old) sports materials
(iv) Sale of (old) news papers.

## III SHORT ANSWER QUESTIONS

**1. What is income and expenditure account?**

**Ans.** (i) Income and expenditure account is a summary of income and expenditure of a not-for-profit organisation prepared at the end of an accounting year.

(ii) It is prepared to find out the surplus or deficit pertaining to a particular year.

(iii) It is a nominal account in nature in which items of revenue receipts and revenue expenditure, relating to the current year alone are recorded.

(iv) It is just like preparing a profit and loss account. In this account, incomes are shown on the credit side and expenses are shown on the debit side.

(v) Apart from cash items, non-cash items such as income accrued but not received, loss or gain on sale of fixed assets, depreciation, etc. will also be recorded.

**2. State the differences between Receipts and Payments Account and Income and Expenditure Account.**

**Ans.**

| S.NO. | Basis | Receipts and Payments Account | Income and Expenditure Account |
|---|---|---|---|
| 1. | Nature of account | It is a real account. Cash receipts are recorded on the debit side and cash payments are recorded on the credit side. | It is a nominal account. Expenses are recorded on the debit side and incomes are recorded on the credit side. |
| 2. | Basis of accounting | It is based on cash system of accounting. Non-cash items are not recorded. | It is based on accrual system of accounting. Non-cash items like outstanding expenses, depreciation, etc. are also recorded. |
| 3. | Opening and closing balance | It commences with an opening balance of cash and bank and ends with closing balance of cash and bank. | There is no opening balance. It ends with surplus or deficit. |
| 4. | Nature of items | It contains actual receipts and payments irrespective of revenue or capital items in nature. | It contains only revenue items, that is, only revenue expenses and revenue incomes. |
| 5. | Period | All cash receipts and payments made during the year pertaining to the past period, current period and subsequent period are recorded. | It contains only the items relating to the current period. |

**3. How annual subscription is dealt with in the final accounts of not-for-profit organisation?**

**Ans.** (a) **Treatment in income and Expenditure account :**

When subscription received for the current year, previous years and subsequent period are given separately, subscription received for the current year will be shown on the credit side of Income and Expenditure Account after making the adjustments given below:

(i) Subscription outstanding for the current year is to be added.

(ii) Subscription received in advance in the previous year which is meant for the current year, is to be added.

When total subscription received during the current year is given, that total subscriptions received during the current year will be shown on the credit side of Income and Expenditure Account after making the following adjustments:

(i) Subscription outstanding in the previous year which is received in the current year will be subtracted. Subscription outstanding for the current year is added.

(ii) Subscriptions received in advance in the previous year which is meant for the current year, is added and subscriptions received in advance in the current year which is meant for the subsequent year must be subtracted.

(B) Treatment in Balance Sheet

(i) Subscriptions outstanding for the current year and still outstanding for the previous year will be shown on the assets side of the balance sheet.

(ii) Subscriptions received in advance in the current year will be shown on the liabilities side of the balance sheet.

**4. How the following items are dealt with in the final accounts of not-for-profit organisation?**

**a) Sale of sports materials**

**b) Life membership fees**

**c) Tournament fund**

*Ans.* (a) Sale of sports materials :

(i) Consumable items such as sports materials, stationery, medicines, etc., consumed during the year will appear on the debit side of income and expenditure account.

(ii) Consumption = Opening stock + Purchases during the current year – Closing stock

(iii) Closing stock will appear on the assets side of the balance sheet as at the end of the year.

(iv) If there is any sale of old sports materials, etc., that will be shown on the credit side of income and expenditure account or can be subtracted from the respective items consumed on the debit side of income and expenditure account.

(b) Life membership fees : Amount received towards life membership fee from members is a capital receipt as it is non-recurring in nature.

(c) Tournament fund : If there are any specific funds such as tournament fund, prize fund, etc., these funds should be shown on the liabilities side of the balance sheet separately.

## IV Exercises

**1. From the information given below, prepare Receipts and Payments account of Kurunji Sports Club for the year ended 31st December, 2018.**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| Cash in hand (1.1.2018) | 4,000 | Paid for printing charges | 2,500 |
| Salaries paid | 3,000 | Lockers rent received | 1,000 |
| Life membership fees received | 10,000 | Tournament receipts | 14,000 |
| Subscription received | 15,000 | Tournament expenses | 10,500 |
| Rent received | 2,000 | Investments purchased | 25,000 |

***Solution :*** **In the books of kurunji sports club**

**Receipts and Payments Account for the year ended 31st December 2018**

Dr. Cr.

| Receipts | ₹ | Payments | ₹ |
|---|---|---|---|
| To Balance b/d | | By Salaries paid | 3,000 |
| Cash in hand | 4,000 | By Printing charges paid | 2,500 |
| To Life membership fees received | 10,000 | By Tournament expenses | 10,500 |
| To Subscription received | 15,000 | By Investment purchased | 25,000 |
| To Rent received | 2,000 | By Balance c/d | |
| To Lockers rent received | 1,000 | Cash in hand | 5,000 |
| To Tournament receipts | 14,000 | | |
| | 46,000 | | 46,000 |

**2.** **From the information given below, prepare Receipts and Payments account of Coimbatore Cricket Club for the year ending 31st March, 2019.**

| Particulars | ₹ | ₹ | Particulars | ₹ |
|---|---|---|---|---|
| Bank overdraft (1.4.2018) | | 6,000 | Honorarium paid | 2,800 |
| Cash in hand (1.4.2018) | | 1,000 | Water and electricity charges | 700 |
| Wages paid for ground maintenance | | 2,000 | Match expenses | 2,600 |
| Subscription received: | | | Sports material purchased | 1,900 |
| | | | Match fund receipts | 5,200 |
| Previous year | 500 | | Legacies received | 2,000 |
| Current year | 9,600 | | Cash balance (31.03.2019) | 300 |
| Subsequent year | 400 | 10,500 | Donation received for pavilion | 2,000 |
| Wages yet to be paid | | 2,200 | | |
| Interest on loan paid | | 2,000 | | |

***Solution :*** **In the books of Coimbatore Cricket Club**

**Receipts and Payments Account for the year ended 31st March 2019**

Dr. Cr.

| Receipts | ₹ | ₹ | Payments | ₹ |
|---|---|---|---|---|
| To Balance b/d | | | By Balance b/d | |
| Cash in hand | | 1,000 | Bank overdraft | 6,000 |
| To Subscription received: | | | By Wages paid | 2,000 |
| Previous year | 500 | | By Interest on loan | 2,000 |
| Current year | 9,600 | | By Honorarium paid | 2,800 |
| Subsequent year | 400 | 10,500 | By Water and electricity charges | 700 |
| | | | By Match expenses | 2,600 |
| | | | By Sports material purchased | 1,900 |
| To Match fund receipts | | 5,200 | By Balance c/d | |
| To Legacies received | | 2,000 | Cash in hand | 300 |
| To Donation received | | 2,000 | Cash at bank | 2,400 |
| | | 20,700 | | 20,700 |

[Hint : Wages yet to be paid is a non cash item. Hence it is excluded in receipts and payments account]

# UNIT 3 ACCOUNTS OF PARTNERSHIP FIRMS – FUNDAMENTALS

## I MULTIPLE CHOICE QUESTIONS

### CHOOSE THE CORRECT ANSWER

**1. In the absence of a partnership deed, profits of the firm will be shared by the partners in**

(a) Equal ratio (b) Capital ratio
(c) Both (a) and (b) (d) None of these

[Ans. (a) Equal ratio]

**2. In the absence of an agreement among the partners, interest on capital is**

(a) Not allowed
(b) Allowed at bank rate
(c) Allowed @ 5% per annum
(d) Allowed @ 6% per annum

[Ans. (a) Not allowed]

**3. As per the Indian Partnership Act, 1932, the rate of interest allowed on loans advanced by partners is**

(a) 8% per annum (b) 12% per annum
(c) 5% per annum (d) 6% per annum

[Ans. (d) 6% per annum]

**4. Which of the following is shown in Profit and loss appropriation account?**

(a) Office expenses
(b) Salary of staff
(c) Partners' salary
(d) Interest on bank loan

[Ans. (c) Partners' salary]

**5. When fixed capital method is adopted by a partnership firm, which of the following items will appear in capital account?**

(a) Additional capital introduced
(b) Interest on capital
(c) Interest on drawings
(d) Share of profit

[Ans. (a) Additional capital introduced]

**6. When a partner withdraws regularly a fixed sum of money at the middle of every month, period for which interest is to be calculated on the drawings on an average is**

(a) 5.5 months (b) 6 months
(c) 12 months (d) 6.5 months

[Ans. (b) 6 months]

**7. Which of the following is the incorrect pair?**

| | | | |
|---|---|---|---|
| (a) | Interest on drawings | - | Debited to capital account |
| (b) | Interest on capital | - | Credited to capital account |
| (c) | Interest on loan | - | Debited to capital account |
| (d) | Share of profit | - | Credited to capital account |

[Ans. (c) **Interest on loan - Debited to capital account**]

**8. In the absence of an agreement, partners are entitled to**

(a) Salary

(b) Commission

(c) Interest on loan

(d) Interest on capital

[Ans. (c) **Interest on loan**]

**9. Pick the odd one out**

(a) Partners share profits and losses equally

(b) Interest on partners' capital is allowed at 7% per annum

(c) No salary or remuneration is allowed

(d) Interest on loan from partners is allowed at 6% per annum.

[Ans. (b) **Interest on partners' capital is allowed at 7% per annum**]

**10. Profit after interest on drawings, interest on capital and remuneration is ₹10,500. Geetha, a partner, is entitled to receive commission @ 5% on profits after charging such commission.**

**Find out commission.**

(a) ₹50 (b) ₹150

(c) ₹550 (d) ₹500

[Ans. (d) **₹500**]

*Hint :* Commission as a percentage of net profit after charging such commission

= Net profit before commission

$$\times \frac{\% \text{of commission}}{100 + \% \text{of commission}}$$

$$= ₹\ 10{,}500 \times \frac{5}{100+5} = \frac{10{,}500 \times 5}{105}$$

$$= ₹\ 500$$

## II Very Short Answer Questions

**1. Define partnership.**

*Ans.* According to section 4 of the Indian partnership Act, 1932, partnership is defined as "the relation between persons who gave agreed to share the profits of a business carried on by all or any of them acting for all".

**2. What is a partnership deed?**

*Ans.* Partnership deed is a document in writing that contains the terms of the agreement among the partners. It is not compulsory for a partnership to have a partnership deed as per the Indian Partnership Act, 1932

**3. What is meant by fixed capital method?**

*Ans.* (i) Under this method, two accounts are maintained for each partner viz. a) Capital account and b) current account

(ii) The transactions relating to initial capital introduced, additional capital introduced and capital permanently withdrawn are entered in the capital account and all other transactions are recorded in the current account.

**4. What is the journal entry to be passed for providing interest on capital to a partner?**

*Ans.* Following are the journal entries to be made in the books of the partnership firm.

**a. For providing interest on capital :**

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Interest on capital A/c Dr<br>To partner's capital / currentA/c | | XXXX | <br>XXXX |

***Note:***

☞ Interest on capital is due to the partners from the firm hence partner's capital/current account is credited and interest on capital account is debited.

**b. For closing interest on capital account :**

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Profit and loss appropriation A/c Dr<br>To Interest on Capital A/c | | XXXX | <br>XXXX |

**5. Why is Profit and loss appropriation account prepared?**

**Ans.** (i) The profit and loss appropriation account is an extension of profit and loss account prepared for the purpose of adjusting the transactions relating to amounts due to and amount due from partners. It is a nominal account in nature

(ii) The balance being the profit or loss is transferred to the partner's capital or current account in the profit sharing ratio.

## III SHORT ANSWER QUESTIONS

**1. State the features of partnership.**

**Ans.** Following are the essential features of partnership

(1) Partnership is an association of two or more persons. The maximum number of partners is limited to 50.

(2) There should be an agreement among the persons to share the profit or loss of the business.

(3) The agreement must be carry on a business and to share the profits of the business.

(4) The business may be carried on by all the partners or any of them acting for all.

**2. State any six contents of a partnership deed.**

**Ans.** (1) Name of the firm and nature and place of business.

(2) Date of commencement and duration of business

(3) Names and addresses of all partners

(4) Capital contributed by each partner

(5) Profit sharing ratio

(5) Rate of interest to be allowed on capital

**3. State the differences between fixed capital method and fluctuating capital method.**

**Ans.**

| Basis of destination | Fixed capital method | Fluctuating capitals method |
|---|---|---|
| 1.Number of accounts | Two accounts are maintained for each partner, that is, capital account and current account. | Only one account, that is, capital account is maintained for each partner. |
| 2.Change in capital | The amount of capital normally remains unchanged except when additional capital is introduced or capital is withdrawn permanently | The amount of capital changes from period to period. |
| 3.Closing balance | Capital account always shows a credit balance | Capital account generally shows credit balance. It may also show a debit balance. |
| 4.Adjustments | All adjustments relating to interest on capital, interest on drawings, salary or commission, share of profit or loss are done in current account | All adjustments relating to interest on capital, interest on drawings, salary or commission, share of profit or loss are done in the capital account |

**4. Write a brief note on the applications of the provisions of the Indian Partnership Act, 1932 in the absence of partnership deed.**

*Ans.* If there is no partnership deed or when there is no express statement in the partnership deed, then the following provisions of the act will apply

(i) **Remuneration to partners:**

No salary or remuneration is allowed to any partner (Section 13(a))

(ii) **Profit sharing ratio:**

Profits and losses are to be shared by the partners equally [section 13(b)]

(iii) **Interest on capital:**

No interest is allowed on the capital, where a partner is entitled to interest on capital contributed as per partnership deed, such interest on capital will be payable only out of profits. [section 13(c)]

(iv) **Interest on loans advanced by partners to the firm:**

Interest on loan is to be allowed at the rate of 6 per cent annum. [section 13(d)]

(v) **Interest on drawings:**

No interest is charged on the drawings of the partners.

**5. Jayaraman is a partner who withdrew ₹10,000 regularly in the middle of every month. Interest is charged on the drawings at 6% per annum. Calculate interest on drawings for the year ended 31st December, 2018.**

*Solution :*

If Drawings are made in the middle of every month :

Average period = 6

Interest on drawings = Total amount of drawings

$$\times \text{Rate of interest} \times \frac{\text{Average Period}}{12}$$

$$= ₹10{,}000 \times \frac{6}{100} \times \frac{6}{12}$$

$$= ₹\ 300$$

## IV Exercises

**1. Akash, Bala, Chandru and Daniel are partners in a firm. There is no partnership deed. How will you deal with the following?**

**(i) Akash has contributed maximum capital. He demands interest on capital at 10% per annum.**

**(ii) Bala has withdrawn ₹3,000 per month. Other partners ask Bala to pay interest on drawings @ 8% per annum to the firm. But, Bala did not agree to it.**

**(iii) Akash demands the profit to be shared in the capital ratio. But, others do not agree.**

**(iv) Daniel demands salary at the rate of ₹10,000 per month as he spends full time for the business.**

**(v) Loan advanced by Chandru to the firm is ₹50,000. He demands interest on loan @ 12% per annum.**

*Ans.* Since there is no partnership deed, provisions of the Indian partnership Act, 1932 will apply.

(i) No interest on capital is payable to any partner. Therefore Akash is entitled to the interest in capital.

(ii) No interest is chargeable on drawings made by the partner. Therefore, Bala need not pay interest on drawings.

(iii) Profits should be distributed equally.

(iv) No remuneration is payable to any partner. Hence Daniel is not entitled to salary.

(v) Interest on loan is payable at 6% per annum of ₹ 50,000.

# UNIT 4 GOODWILL IN PARTNERSHIP ACCOUNTS

## I MULTIPLE CHOICE QUESTIONS

### CHOOSE THE CORRECT ANSWER

**1. Which of the following statements is true?**

(a) Goodwill is an intangible asset
(b) Goodwill is a current asset
(c) Goodwill is a fictitious asset
(d) Goodwill cannot be acquired

[Ans. (a) Goodwill is an intangible asset]

**2. Super profit is the difference between**

(a) Capital employed and average profit
(b) Assets and liabilities
(c) Average profit and normal profit
(d) Current year's profit and average profit

[Ans. (c) Average profit and normal profit]

**3. The average rate of return of similar concerns is considered as**

(a) Average profit
(b) Normal rate of return
(c) Expected rate of return
(d) None of these

[Ans. (b) Normal rate of return]

**4. Which of the following is true?**

(a) Super profit = Total profit / number of years
(b) Super profit = Weighted profit / number of years
(c) Super profit = Average profit – Normal profit
(d) Super profit = Average profit × Years of purchase

[Ans. (c) Super profit = Average profit – Normal profit]

**5. Identify the incorrect pair**

| | | | |
|---|---|---|---|
| (a) | Goodwill under Average profit method | - | Average profit × Number of years of purchase |
| (b) | Goodwill under Super profit method | - | Super profit × Number of years of purchase |
| (c) | Goodwill under Annuity method | - | Average profit × Present value annuity factor |
| (c) | Goodwill under Weighted average profit method | - | Weighted average profit × Number of years of purchase |

[Ans. (c) Goodwill under Annuity method – Average profit × Present value annuity factor]

**6. When the average profit is ₹25,000 and the normal profit is ₹15,000, super profit is**

(a) ₹25,000 (b) ₹5,000

(c) ₹10,000 (d) ₹15,000

[Ans. (c) ₹10,000]

*Hint :* Super profit = Average profit – Normal profit

= ₹ 25,000 – ₹15,000

= ₹10,000

**7. Book profit of 2017 is ₹35,000; non-recurring income included in the profit is ₹1,000 and abnormal loss charged in the year 2017 was ₹2,000, then the adjusted profit is**

(a) ₹36,000 (b) ₹35,000

(c) ₹38,000 (d) ₹34,000

[Ans. (a) ₹36,000]

*Hint :* Calculation of adjusted profit :

| Particulars | 2017 ₹ |
|---|---|
| Book profit | 35,000 |
| Less : Non-recurring income | 1,000 |
| | 34,000 |
| Add : Abnormal loss | 2,000 |
| Ajusted profit | 36,000 |

**8. The total capitalised value of a business is ₹1,00,000; assets are ₹1,50,000 and liabilities are ₹80,000. The value of goodwill as per the capitalisation method will be**

(a) ₹40,000 (b) ₹70,000

(c) ₹1,00,000 (d) ₹30,000

[Ans. (d) ₹30,000]

*Hint :* Goodwill = Total capitalised value of the average profit – Capital employed

Capital employed = Current assets – Current liabilities

= ₹ 1,50,000 – ₹ 80,000

= ₹ 70,000

Goodwill = ₹ 1,00,000 – ₹ 70,000

= ₹ 30,000

## II VERY SHORT ANSWER QUESTIONS

**1. What is goodwill?**

*Ans.* Goodwill is the good name or reputation of the business which brings benefit to the business. It enables the business to earn more profit. It is the present value of a firm's future excess earnings. It is an intangible asset as it has no physical existence.

**2. What is acquired goodwill?**

*Ans.* Goodwill acquired by making payment in cash or kind is called acquired or purchased goodwill. The excess of purchase consideration over the value of net assets acquired is treated as acquired goodwill.

**3. What is super profit?**

*Ans.* The excess of average profit over normal profit is called super profit. The goodwill under the super profits method is calculated by multiplying the super profits by certain number of years purchase.

Super profit = Average profit – Normal profit

**4. What is normal rate of return?**

*Ans.* Normal rate of return refers to the rate at which profit is earned by similar business entities in the industry under normal circumstances.

**5. State any two circumstances under which goodwill of a partnership firm is valued.**

*Ans.* (i) When there is a change in the profit sharing ratio

(ii) When a new partner is admitted into a firm

## III SHORT ANSWER QUESTIONS

**1. State any six factors determining goodwill.**

*Ans.* Generally, the following factors determine the value of goodwill of a partnership firm:

(i) **Profitability of the firm:**

A firm earning higher profits and having potential to generate higher profits in future will have higher value of good will.

(ii) **Good quality of goods or services offered:**

If a firm enjoys good reputation among the customers and general public for the good quality of its products or services, the value of goodwill for the firm will be high.

(iii) **Tenure of the business enterprise:**

A firm which has carried on business for several years will have higher reputation among its customers as it is better known to the customers.

(iv) **Efficiency of management:**

A firm having efficient management will earn more profits and the value of its goodwill will be higher compared to a firm with less efficient managerial personnel .

(v) **Degree of competition :**

In the case of business enterprises having no competition or negligible competition, the value of goodwill will be high

(vi) **Other factors:**

There are other factors which add to the value of goodwill of a business such as popularity of the proprietor, impressive advertisements and publicity, good relations with customers, etc.

**2. How is goodwill calculated under the super profits method?**

**Ans.** (i) Under these methods, super profit is the base for calculation of the value of goodwill. Super profit is the excess of average profit over the normal profit of a business.

Super profit = Average profit – Normal profit

(ii) Average profit is calculated by dividing the total of adjusted actual profits of certain number of years by the total number of such years. Normal profit is the profit earned by the similar business firms under normal conditions.

(iii) Normal profit = Capital employed × Normal rate of return

(iv) Capital employed = Fixed assets +current assets – Current liabilities

(v) Normal rate of return = It is the rate at which profit is earned by similar business entities in the industry under normal circumstances.

**3. How is the value of goodwill calculated under the capitalisation method?**

**Ans.** (i) Under this method , goodwill is the excess of capitalised value of average profit of the business over the actual capital employed in the business.

Goodwill = Total capitalised value of the business – Actual capital employed

(ii) The total capitalised value of the business is calculated by capitalising the average profits on the basis of the normal rate of return.

Capitalised value of the business

$$= \frac{\text{Average profit}}{\text{Normal rate of return}} \times 100$$

(iii) Actual capital employed = Fixed assets (excluding goodwill ) + Current assets – Current liabilities

**4. Compute average profit from the following information.**

**2016: ₹8,000; 2017: ₹10,000; 2018: ₹9,000**

*Solution :*

$$\text{Average profit} = \frac{\text{Total profit}}{\text{Number of years}}$$

$$\text{Average profit} = \frac{8{,}000+10{,}000+9{,}000}{3}$$

Average profit = ₹ 9,000

**5. Calculate the value of goodwill at 2 years purchase of average profit when average profit is ₹15,000.**

*Solution :*

Goodwill = Average profit × Number of years of purchase

= 15,000 × 2

= 30,000

Goodwill = ₹30,000

## IV EXERCISES:

### 1. Simple average profit method

**The following are the profits of a firm in the last five years:**

**2014 : ₹10,000; 2015 : ₹11,000; 2016 : ₹12,000; 2017 : ₹13,000 and 2018 : ₹14,000**

**Calculate the value of goodwill at 2 years purchase of average profit of five years.**

*Solution :*

Goodwill = Average profit × Number of years of purchase

$$\text{Average profit} = \frac{\text{Total profit}}{\text{Number of years}}$$

$$= \frac{10{,}000+11{,}000+12{,}000+13{,}000+14{,}000}{5}$$

$$= \frac{60{,}000}{5} = ₹\ 12{,}000$$

Average profit = ₹12, 000

Goodwill = Average profit × Number of years of purchase

= 12,000 × 2 = 24,000

Goodwill = ₹ 24,000

# UNIT 5 ADMISSION OF A PARTNER

## I. Multiple Choice Questions.

**Choose the correct answer :**

1. **Revaluation A/c is a**
   - (a) Real A/c
   - (b) Nominal A/c
   - (c) Personal A/c
   - (d) Impersonal A/c

   [Ans. (b) Nominal A/c]

2. **On revaluation, the increase in the value of assets leads to**
   - (a) Gain
   - (b) Loss
   - (c) Expense
   - (d) None of these

   [Ans. (a) Gain]

3. **The profit or loss on revaluation of assets and liabilities is transferred to the capital account of**
   - (a) The old partners
   - (b) The new partner
   - (c) All the partners
   - (d) The Sacrificing partners

   [Ans. (a) The old partners]

4. **If the old profit sharing ratio is more than the new profit sharing ratio of a partner, the difference is called**
   - (a) Capital ratio
   - (b) Sacrificing ratio
   - (c) Gaining ratio
   - (d) None of these

   [Ans. (b) Sacrificing ratio]

5. **At the time of admission, the goodwill brought by the new partner may be credited to the capital accounts of**
   - (a) all the partners
   - (b) the old partners
   - (c) the new partner
   - (d) the sacrificing partners

   [Ans. (d) the sacrificing partners]

6. **Which of the following statements is not true in relation to admission of a partner**
   - (a) Generally mutual rights of the partners change
   - (b) The profits and losses of the previous years are distributed to the old partners

(c) The firm is reconstituted under a new agreement

(d) The existing agreement does not come to an end

[Ans. (d) The existing agreement does not come to an end]

**7. Match List I with List II and select the correct answer using the codes given below:**

| List I | | List II | |
|---|---|---|---|
| (i) | Sacrificing ratio | 1. | Investment fluctuation fund |
| (ii) | Old profit sharing ratio | 2. | Accumulated profit |
| (iii) | Revaluation Account | 3. | Goodwill |
| (iv) | Capital Account | 4. | Unrecorded liability |

Codes :

| | (i) | (ii) | (iii) | (iv) |
|---|---|---|---|---|
| (a) | 1 | 2 | 3 | 4 |
| (b) | 3 | 2 | 4 | 1 |
| (c) | 4 | 3 | 2 | 1 |
| (d) | 3 | 1 | 4 | 2 |

[Ans. (b) (i) - 3 (ii) - 2 (iii) - 4 (iv) - 1]

**8. Select the odd one out**

(a) Revaluation profit

(b) Accumulated loss

(c) Goodwill brought by new partner

(d) Investment fluctuation fund

[Ans. (c) Goodwill brought by new partner]

**9. James and Kamal are sharing profits and losses in the ratio of 5:3. They admit Sunil as a partner giving him 1/5 share of profits. Find out the sacrificing ratio.**

(a) 1:3 (b) 3:1 (c) 5:3 (d) 3:5

[Ans. (c) 5:3]

**10. Balaji and Kamalesh are partners sharing profits and losses in the ratio of 2:1. They admit Yogesh into partnership. The new profit sharing ratio between Balaji, Kamalesh and Yogesh is agreed to 3:1:1. Find the sacrificing ratio between Balaji and Kamalesh.**

(a) 1:3 (b) 3:1 (c) 2:1 (d) 1:2

[Ans. (d) 1:2]

## II. VERY SHORT ANSWER QUESTIONS.

**1. What is meant by revaluation of assets and liabilities?**

**Ans.** When a partner is admitted into the partnership, the assets and liabilities are revalued as the current value may differ from the book value. Determination of current values of assets and liabilities is called revaluation of assets and liabilities.

**2. How are accumulated profits and losses distributed among the partners at the time of admission of a new partner?**

**Ans.** Profits and losses of previous years which are not distributed to the partners are called accumulated profit and losses. Any reserve and accumulated profits and losses belong to the oldpartners and hence these should be distributed to the old partners in the old profit sharing ratio.

**3. What is sacrificing ratio?**

**Ans.** Sacrificing ratio is the proportion of the profit which is sacrificed or foregone by the old partners in favour of the new partner. The purpose of finding the sacrificing ratio is to share the goodwill brought in by the new partner.

Share sacrificed = Old share – New share

Sacrificing ratio = Ratio of share sacrificed by the old partners

**4. Give the journal entry for writing off existing goodwill at the time of admission of a new partner.**

**Ans.** Journal Entry

| Date | Particular | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Old partner's capital/current A/c (in old ratio) Dr | | XXX | |
| | To goodwill A/c | | | XXX |
| | (Existing goodwill written off) | | | |

**5. State whether the following will be debited or credited in the revaluation account.**

**(a) Depreciation on assets**

**(b) Unrecorded liability**

**(c) Provision for outstanding expenses**

**(d) Appreciation of assets**

**Ans.** (a) Debit account

(b) Debit account

(c) Debit account

(d) Credit account

## III. Short answer questions.

**1. What are the adjustments required at the time of admission of a partner?**

*Ans.* The following adjustment are necessary at the time of admission of a partner

(i) Distribution of accumulated profits, reserves and losses.

(ii) Revaluation of assets and liabilities

(iii) Determination of new profit sharing ratio and sacrificing ratio

(iv) Adjustment for goodwill

(v) Adjustment of capital on the basis of new profit sharing ratio (if so agreed).

**2. What are the journal entries to be passed on revaluation of assets and liabilities?**

*Solution :*

**Following are the journal entries to be passed to record the revaluation of assets and liabilities**

| Date | Particulars | | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|---|
| | 1. For increase in the value of asset | | | | |
| | Concerned asset A/c | Dr | | XXX | |
| | To Revaluation A/c | | | | XXX |
| | 2. For decrease in the value of asset | | | | |
| | Revaluation A/c | Dr | | XXX | |
| | To Concerned asset A/c | | | | XXX |
| | 3. For increase in the amount of liabilities | | | | |
| | Revaluation A/c | Dr | | XXX | |
| | To Concerned liabilities A/c | | | | XXX |
| | 4. For decrease in the amount of liability | | | | |
| | Concerned liability Dr | | | XXX | |
| | To Revaluation A/c | | | | XXX |
| | 5. For recording an unrecorded asset | | | | |
| | Concerned asset A/c | Dr | | XXX | |
| | To Revaluation A/c | | | | XXX |
| | 6. For recording an unrecorded liability | | | | |
| | Revaluation A/c | Dr | | XXX | |
| | To Concerned liability A/c | | | | XXX |
| | 7. For transferring the balance in revaluation A/c | | | | |
| | (a) If there is profit on revaluation | | | | |
| | Revaluation A/c | Dr | | XXX | |
| | To Old partner's capital A/c (individually in old ratio) | | | | XXX |
| | (b) If there is loss on revaluation | | | | |
| | Old partner's capital A/c (individually in old ratio) | | | XXX | |
| | To Revaluation A/c | | | | XXX |

3. **Write a short note on accounting treatment of goodwill.**

**Ans.** According treatment for goodwill on admission of a partner is discussed below:

(i) **When new partner brings cash onwards goodwill**

When the new partner brings cash towards goodwill in addition to the amount of capital it is distributed to the existing partners in the sacrificing ratio.

(ii) **When the new partner does not bring goodwill in cash or in kind**

If the new partner does not bring goodwill in cash or in kind, his share of goodwill must be adjusted through the capital accounts of the partners.

(iii) **When the new partner brings only a part of the goodwill in cash or in kind**

Sometimes the new partner may bring only a part of the goodwill in cash or assets. In such a case, for the cash or the assets brought the respective account is debited and for the amount not brought in cash or kind, the new partner's capital account is debited

(iv) **Existing goodwill**

If goodwill already appears in the books of accounts at the time of admission if the partners decide, it can be written off by transferring it to the existing partner's capital account/current account in the old profit sharing ratio.

## IV. Exercises.

### Distribution of accumulated profits, reserves and losses

1. **Arul and Anitha are partners sharing profits and losses in the ratio of 4:3. On 31.3.2018, Ajay was admitted as a partner. On the date of admission, the book of the firm showed a general reserve of ₹42,000. Pass the journal entry to distribute the general reserve.**

*Solution :*

**Journal Entry**

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| 2018 March 31 | General reserve A/c Dr | | 42,000 | |
| | To Arul's capital A/c $(42,000 \times \frac{4}{7})$ | | | 24,000 |
| | To Anita's capital A/c $(42,000 \times \frac{3}{7})$ | | | 18,000 |
| | (General reserve transferred to old partner's capital account in the old profit sharing ratio) | | | |

**25.** **Sundar and Suresh are partners sharing profits in the ratio of 3:2. Their balance sheet as on 1st January, 2017 was as follows:**

| Liabilities | ₹ | ₹ | Assets | ₹ |
|---|---|---|---|---|
| Capital accounts: | | | Buildings | 40,000 |
| Sundar | 30,000 | | Furniture | 13,000 |
| Suresh | 20,000 | 50,000 | Stock | 25,000 |
| Creditors | | 50,000 | Debtors | 15,000 |
| General reserve | | 10,000 | Bills receivable | 14,000 |
| Workmen compensation fund | | 15,000 | Bank | 18,000 |
| | | 1,25,000 | | 1,25,000 |

**They decided to admit Sugumar into partnership for 1/4 share in the profits on the following terms:**

**(a) Sugumar has to bring in ₹30,000 as capital. His share of goodwill is valued at ₹5,000. He could not bring cash towards goodwill.**

**(b) That the stock be valued at ₹20, 000.**

**(c) That the furniture be depreciated by ₹2,000.**

**(d) That the value of building be depreciated by 20%.**

**Prepare necessary ledger accounts and the balance sheet after admission.**

*Solution :*

## Revaluation Account

Dr | Cr

| Particulars | ₹ | Particulars | ₹ | ₹ |
|---|---|---|---|---|
| To Stock A/c | 5,000 | By Loss on revaluation transferred to | | |
| To Furniture A/c | 2,000 | | | |
| To Building A/c | 8,000 | Sundar's capital A/c (3/5) | 9,000 | |
| | | Suresh's capital A/c (2/5) | 6,000 | 15,000 |
| | 15,000 | | | 15,000 |

## Capital Account

Dr | Cr

| Particulars | Sundar ₹ | Suresh ₹ | Sugumar ₹ | Particulars | Sundar ₹ | Suresh ₹ | Sugumar ₹ |
|---|---|---|---|---|---|---|---|
| To Revaluation A/c | 9,000 | 6,000 | – | By Balance b/d | 30,000 | 20,000 | – |
| To Sundar's capital A/c (Share of goodwill) | – | – | 5,000 | By Bank A/c | – | – | 30,000 |
| To Balance c/d | 41,000 | 24,000 | 25,000 | By General reserve A/c | 6,000 | 4,000 | – |
| | | | | By Workmen Compensation fund A/c | 9,000 | 6,000 | – |
| | | | | By Sugumar's capital A/c (Share of goodwill) | 5,000 | – | |
| | 50,000 | 30,000 | 25,000 | | 50,000 | 30,000 | 30,000 |
| | | | | By Balance b/d | 41,000 | 24,000 | 25,000 |

### Balance sheet as on 1st January 2017

| Liabilities | ₹ | ₹ | Assets | ₹ | ₹ |
|---|---|---|---|---|---|
| Capital Account : | | | Building | 40,000 | |
| Sundar | 41,000 | | Add: Depreciation 20% | 8,000 | 32,000 |
| Suresh | 24,000 | | Furniture | 13,000 | |
| Sugumar | 25,000 | 90,000 | Less: Depreciation | 2,000 | 11,000 |
| Creditors | | 50,000 | Stock | 25,000 | |
| | | | Less: Depreciation | 5,000 | 20,000 |
| | | | Debtors | | 15,000 |
| | | | Bills receivable | | 14,000 |
| | | | Bank (18,000 + 30,000) | | 48,000 |
| | | 1,40,000 | | | 1,40,000 |

**26.** **The following is the balance sheet of James and Justina as on 1.1.2017. They share the profits and losses equally.**

| Liabilities | ₹ | ₹ | Assets | ₹ |
|---|---|---|---|---|
| Capital accounts: | | | Building | 70,000 |
| James | 40,000 | | Stock | 30,000 |
| Justina | 50,000 | 90,000 | Debtors | 20,000 |
| Creditors | | 35,000 | Bank | 15,000 |
| Reserve fund | | 15,000 | Prepaid insurance | 5,000 |
| | | 1,40,000 | | 1,40,000 |

**On the above date, Balan is admitted as a partner with 1/5 share in future profits. Following are the terms for his admission:**

(i) **Balan brings ₹25,000 as capital.**

(ii) **His share of goodwill is ₹10, 000 and he brings cash for it.**

(iii) **The assets are to be valued as under:**

**Building ₹80, 000; Debtors ₹18,000; Stock ₹33,000**

**Prepare necessary ledger accounts and the balance sheet after admission.**

*Solution :*

### Revaluation Account

Dr Cr

| Particulars | ₹ | ₹ | Particulars | ₹ |
|---|---|---|---|---|
| To Debtors A/c | | 2,000 | By Building A/c | 10,000 |
| To Profit on revaluation transferred to | | | By Stock A/c | 3,000 |
| James's capital A/c | 5,500 | | | |
| Justina's capital A/c | 5,500 | 11,000 | | |
| | | 13,000 | | 13,000 |

## Capital Account

Dr Cr

| Particulars | James ₹ | Justina ₹ | Balan ₹ | Particulars | James ₹ | Justina ₹ | Balan ₹ |
|---|---|---|---|---|---|---|---|
| To Balance c/d | 58,000 | 68,000 | 25,000 | By Balance b/d | 40,000 | 50,000 | – |
| | | | | By Reserve fund A/c | 7,500 | 7,500 | – |
| | | | | By Bank A/c | – | – | 25,000 |
| | | | | By Revaluation A/c | 5,500 | 5,500 | – |
| | | | | By Bank A/c (Share of goodwill) | 5,000 | 5,000 | – |
| | 58,000 | 68,000 | 25,000 | | 58,000 | 68,000 | 25,000 |
| | | | | By Balance b/d | 58,000 | 68,000 | 25,000 |

## Cash at Bank Account

Dr Cr

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance b/d | 15,000 | By Balance c/d | 50,000 |
| To Balan's capital A/c | 25,000 | | |
| To Jame's capital A/c | 5,000 | | |
| To Justina's capital A/c | 5,000 | | |
| | 50,000 | | 50,000 |

## Balance sheet as on 1st January 2017

| Liabilities | ₹ | ₹ | Assets | ₹ | ₹ |
|---|---|---|---|---|---|
| Capital Account : | | | Building | 70,000 | |
| James's A/c | 58,000 | | Add: Appreciation | 10,000 | 80,000 |
| Justina A/c | 68,000 | | Stock | 30,000 | |
| Balan A/c | 25,000 | 1,51,000 | Less: Appreciation | 3,000 | 33,000 |
| Creditors | | 35,000 | Debtors | 20,000 | |
| | | | Less: Undervalued | 2,000 | 18,000 |
| | | | Bank | | 50,000 |
| | | | Prepaid insurance | | 5,000 |
| | | 1,86,000 | | | 1,86,000 |

**27.** **Anbu and Shankar are partners in a business sharing profits and losses in the ratio of 3:2. The balance sheet of the partners on 31.03.2018 is as follows:**

| Liabilities | ₹ | ₹ | Assets | ₹ |
|---|---|---|---|---|
| Capital accounts: | | | Computer | 40,000 |
| Anbu | 4,00,000 | | Motor car | 1,60,000 |
| Shankar | 3,00,000 | 7,00,000 | Stock | 4,00,000 |
| Profit and loss | | 1,20,000 | Debtors | 3,60,000 |
| Creditors | | 1,20,000 | Bank | 40,000 |
| Workmen compensation fund | | 60,000 | | |
| | | 10,00,000 | | 10,00,000 |

Rajesh is admitted for 1/5 share on the following terms:

(i) Goodwill of the firm is valued at ₹75,000 and Rajesh brought cash for his share of goodwill.

(ii) Rajesh is to bring ₹1,50,000 as his capital.

(iii) Motor car is valued at ₹2,00,000; Stock at ₹3,80,000 and debtors at ₹3,50,000.

(iv) Anticipated claim on workmen compensation fund is ₹10,000

(v) Unrecorded investment of ₹5,000 has to be brought into account.

Prepare revaluation account, capital accounts and balance sheet after Rajesh's admission.

*Solution :*

**Revaluation Account**

Dr | Cr

| Particulars | ₹ | | Particulars | ₹ |
|---|---|---|---|---|
| To Stock A/c | | 20,000 | By Motor car | 40,000 |
| To Debtors A/c | | 10,000 | By Investment A/c | 5,000 |
| To Profit on revaluation transferred to | | | | |
| Anbu's capital A/c | 9,000 | | | |
| Shankar's capital A/c | 6,000 | 15,000 | | |
| | | 45,000 | | 45,000 |

**Capital Account**

Dr | Cr

| Particulars | Anbu ₹ | Shankar ₹ | Rajesh ₹ | Particulars | Anbu ₹ | Shankar ₹ | Rajesh ₹ |
|---|---|---|---|---|---|---|---|
| To Balance c/d | 5,20,000 | 3,80,000 | 1,50,000 | By Balance b/d | 4,00,000 | 3,00,000 | – |
| | | | | By Bank A/c | – | – | 1,50,000 |
| | | | | By Profit and loss A/c | 72,000 | 48,000 | – |
| | | | | By Workmen compensation fund (60,000 – 10,000) | 30,000 | 20,000 | – |
| | | | | By Revaluation A/c | 9,000 | 6,000 | – |
| | | | | By Goodwill A/c | 9,000 | 6,000 | – |
| | 5,20,000 | 3,80,000 | 1,50,000 | | 5,20,000 | 3,80,000 | 1,50,000 |
| | | | | By Balance b/d | 5,20,000 | 3,80,000 | 1,50,000 |

Good will of the firm is $=$ ₹75,000

Rajesh share of goodwill $= 75{,}000 \times \frac{1}{5}$

$=$ ₹ 15,000

It is to be distributed to Anbu and Shankar in their old ratio of 3:2

**Cash at Bank account**

Dr | Cr

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| To Balance b/d | 40,000 | | |
| To Rajesh capital A/c | 1,50,000 | | |
| To Anbu's capital A/c | 9,000 | | |
| To Shankar's capital A/c | 6,000 | By Balance c/d | 2,05,000 |
| | 2,05,000 | | 2,05,000 |

**Balance Sheet**

| Liabilities | ₹ | ₹ | Assets | ₹ | ₹ |
|---|---|---|---|---|---|
| Capital accounts: | | | Computer | | 40,000 |
| Anbu | 5,20,000 | | Motor Car | 1,60,000 | |
| Shankar | 3,80,000 | | <u>Add:</u> Appreciation | 40,000 | 2,00,000 |
| Rajesh | 1,50,000 | 10,50,000 | Stock | 4,00,000 | |
| Creditors | | 1,20,000 | <u>Less:</u> Depreciation | 20,000 | 3,80,000 |
| Workmen compensation fund (60,000 – 50,000) | | 10,000 | Debtors | 3,60,000 | |
| | | | <u>Less:</u> Under valued | 10,000 | 3,50,000 |
| | | | Bank | | 2,05,000 |
| | | | Unrecorded investment | | 5,000 |
| | | 11,80,000 | | | 11,80,000 |

# UNIT 6 RETIREMENT AND DEATH OF A PARTNER

## I Multiple choice questions

### Choose the correct answer

1. A partner retires from the partnership firm on 30th June. He is liable for all the acts of the firm up to the
   (a) End of the current accounting period
   (b) End of the previous accounting period
   (c) Date of his retirement
   (d) Date of his final settlement
   [Ans. (c) Date of his retirement]

2. On retirement of a partner from a partnership firm, accumulated profits and losses are distributed to the partners in the
   (a) New profit sharing ratio
   (b) Old profit sharing ratio
   (c) Gaining ratio
   (d) Sacrificing ratio
   [Ans. (b) Old profit sharing ratio]

3. On retirement of a partner, general reserve is transferred to the
   (a) Capital account of all the partners
   (b) Revaluation account
   (c) Capital account of the continuing partners
   (d) Memorandum revaluation account
   [Ans. (a) Capital account of all the partners]

4. On revaluation, the increase in liabilities leads to
   (a) Gain (b) Loss
   (c) Profit (d) None of these
   [Ans. (b) Loss]

5. At the time of retirement of a partner, determination of gaining ratio is required
   (a) To transfer revaluation profit or loss
   (b) To distribute accumulated profits and losses
   (c) To adjust goodwill
   (d) None of these
   [Ans. (c) To adjust goodwill]

**6. If the final amount due to a retiring partner is not paid immediately, it is transferred to**

(a) Bank A/c

(b) Retiring partner's capital A/c

(c) Retiring partner's loan A/c

(d) Other partners' capital A/c

[Ans. (c) Retiring partner's loan A/c]

**7. 'A' was a partner in a partnership firm. He died on 31st March 2019. The final amount due to him is ₹ 25,000 which is not paid immediately. It will be transferred to**

(a) A's capital account

(b) A's current account

(c) A's Executor account

(d) A's Executor loan account

[Ans. (d) A's Executor loan account]

**8. A, B and C are partners sharing profits in the ratio of 2:2:1. On retirement of B, goodwill of the firm was valued as ₹ 30,000. Find the contribution of A and C to compensate B:**

(a) ₹ 20,000 and ₹ 10,000

(b) ₹ 8,000 and ₹ 4,000

(c) ₹ 10,000 and ₹ 20,000

(d) ₹ 15,000 and ₹ 15,000

*Hint :*

$$\text{B's share of goodwill} = 30{,}000 \times \frac{2}{5}$$

$$= ₹12{,}000$$

$$\text{A's capital A/c } (12{,}000 \times \frac{2}{3}) = ₹8{,}000$$

$$\text{C's capital A/c } (12{,}000 \times \frac{1}{3}) = ₹4{,}000$$

[Ans. (b) ₹ 8,000 and ₹ 4,000]

**9. A, B and C are partners sharing profits in the ratio of 4:2:3. C retires. The new profit sharing ratio between A and B will be**

(a) 4:3 (b) 3:4

(c) 2:1 (d) 1:2 [Ans. (c) 2:1]

*Hint :*

A, B, C's sharing ratio = 4 : 2 : 3

C's retired, so A and B's share ratio = 4 : 2 = 2 : 1

**10. X, Y and Z were partners sharing profits and losses equally. X died on 1st April 2019. Find out the share of X in the profit of 2019 based on the profit of 2018 which showed ₹ 36,000.**

(a) ₹ 1,000 (b) ₹ 3,000

(c) ₹ 12,000 (d) ₹ 36,000

[Ans. (b) ₹ 3,000]

## II. Very Short Answer Questions:

**1. What is meant by retirement of partners?**

*Ans.* When a partner leaves from a partnership firm, it is known as retirement. The reasons for the retirement of a partner may be illness, old age, better opportunity elsewhere, disagreement with other partners, etc.

**2. What is gaining ratio?**

*Ans.* The continuing partners may again a portion of the share of profit of the retiring partner. The gain may be shared by all the partners or some of the partners. Gaining ratio is the proportion of the profit which is gained by the continuing partners.

**3. What is the purpose of calculating gaining ratio?**

*Ans.* The purpose of finding the gaining ratio is to bear the goodwill to be paid to the retiring partner. The share gained is calculated as follows:

Share gained = New share – Old share

Gaining ratio = Ratio of share gained by the continuing partners.

**4. What is the journal entry to be passed to transfer the amount due to the deceased partner to the executor of the deceased partner?**

*Ans.* To transfer the amount due to the deceased partner to the executor or legal representative of the deceased partner.

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Deceased partner's capital A/c Dr. | | XXX | |
| | To Deceased partner's executor's A/c | | | XXX |

## III. Short answer questions:

**1. List out the adjustments made at the time of retirement of a partner in a partnership firm.**

**Ans.** The following adjustments are necessary at the time of retirement of a partner.

(i) Distribution of accumulated profits, reserves and losses.

(ii) Revaluation of assets and liabilities.

(iii) Determination of new profit sharing ratio and gaining ratio.

(iv) Adjustment for goodwill.

(v) Adjustment for current year's profit or loss upto the date of retirement.

(vi) Settlement of the amount due to the retiring partner.

**2. Distinguish between sacrificing ratio and gaining ratio.**

| | Basic | Sacrificing ratio | Gaining ratio |
|---|---|---|---|
| 1. | Meaning | It is the proportion of the profit which is sacrificed by the old partners in favour of a new partner. | It is the proportion of the profit which is gained by the continuing partners from the retiring partner. |
| 2. | Purpose | It is calculated to determine the amount to be adjusted towards goodwill for the sacrificing partners. | It is calculated to determine the amount to be adjusted towards goodwill for the gaining partners. |
| 3. | Time of calculation | It is calculated at the time of admission of a new partner. | It is calculated at the time of retirement of a partner. |
| 4. | Method of Calculation | It is the difference between the old ratio and the new ratio.<br>Sacrificing ratio = Old profit sharing ratio – New profit sharing ratio. | It is the difference between the new ratio and the old ratio.<br>Gaining ratio = New profit sharing ratio – Old profit sharing ratio. |

**3. What are the ways in which the final amount due to an outgoing partner can be settled?**

**Ans.** The amount due to the retiring partner may be settled in one of the following ways.

(i) Paying the entire amount due immediately in cash.

(ii) Transfer the entire amount due to the loan account of the partner.

(iii) Paying part of the amount immediately in cash and transferring the balance to the loan account of the partner.

The journal entries to be made are as follows:

(a) When the amount due is paid in cash immediately.

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Retiring partner's capital A/c Dr.<br>To Cash / Bank A/c | | XXX | <br>XXX |

(b) When the amount due is not paid immediately in cash.

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Retiring partner's capital A/c Dr.<br>To Retiring partner's loan A/c | | XXX | <br>XXX |

(c) When the amount due is partly paid in cash immediately.

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Retiring partner's capital A/c Dr.<br>To Cash / Bank A/c (amount paid)<br>To Retiring partner's loan A/c | | XXX | <br>XXX<br>XXX |

Retiring partner's loan account will appear on the liabilities side o the balance sheet prepared after retirement till it is completely settled.

## IV. Exercise:

### Retirement of a partner

**Distribution of accumulated profits, reserves and losses:**

**1. Dheena, Surya and Janaki are partners sharing profits and losses in the ratio of 5:3:2. On 31.3.2018, Dheena retired. On the date of retirement, the books of the firm showed a reserve fund of ₹ 50,000. Pass journal entry to transfer the reserve fund.**

*Solution :*

Journal entry

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| 2018<br>March 31 | General reserve A/c Dr.<br>To Dheena A/c (50,000 × 5/10)<br>To Surya A/c (50,000 × 3/10)<br>To Janaki A/c (50,000 × 2/10)<br><br>(General reserve transferred to all partner's capital account in the profit sharing ratio) | | 50,000 | <br>25,000<br>15,000<br>10,000 |

**2. Rosi, Rathi and Rani are partners of a firm sharing profits and losses equally. Rathi retired from the partnership on 1.1.2018. On that date, their balance sheet showed accumulated loss of ₹ 45,000 on the asset side of the balance sheet. Give the journal entry to distribute the accumulated loss.**

*Solution :*

Journal entry

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| 2018<br>January 1 | Rosi A/c (45,000) Dr.<br>Rathi A/c Dr.<br>Rani A/c Dr.<br>To Profit and loss A/c<br>(Accumulated loss transferred to all partner's capital account in the old profit sharing ratio) | | 15,000<br>15,000<br>15,000 | <br><br><br>45,000 |

# UNIT 7 COMPANY ACCOUNTS

## I. Multiple Choice Questions.

### (i) Choose the correct answer :

1. A preference share is one
   (i) which carries preferential right with respect to payment of dividend at fixed rate
   (ii) which carries preferential right with respect to repayment of capital on winding up
   (a) Only (i) is correct
   (b) Only (ii) is correct
   (c) Both (i) and (ii) are correct
   (d) Both (i) and (ii) are incorrect

   [Ans. (c) Both (i) and (ii) are correct]

2. That part of share capital which can be called up only on the winding up of a company is called:
   (a) Authorised capital (b) Called up capital
   (c) Capital reserve (d) Reserve capital

   [Ans. (d) Reserve capital]

3. At the time of forfeiture, share capital account is debited with
   (a) Face value
   (b) Nominal value
   (c) Paid up amount
   (d) Called up amount

   [Ans. (d) Called up amount]

4. After the forfeited shares are reissued, the balance in the forfeited shares account should be transferred to
   (a) General reserve account
   (b) Capital reserve account
   (c) Securities premium account
   (d) Surplus account

   [Ans. (b) Capital reserve account]

5. The amount received over and above the par value is credited to
   (a) Securities premium account
   (b) Calls in advance account
   (c) Share capital account
   (d) Forfeited shares account

   [Ans. (a) Securities premium account]

6. **Which of the following statement is false?**

(a) Issued capital can never be more than the authorised capital

(b) In case of under subscription, issued capital will be less than the subscribed capital

(c) Reserve capital can be called at the time of winding up

(d) Paid up capital is part of called up capital

[Ans. (b) In case of under subscription, issued capital will be less than the subscribed capital]

7. **When shares are issued for purchase of assets, the amount should be credited to**

(a) Vendor's A/c

(b) Sundry assets A/c

(c) Share capital A/c

(d) Bank A/c

[Ans. (c) Share capital A/c]

8. **Match the pair and identiry the correct option**

| | | | |
|---|---|---|---|
| (1) | Under subscription | (i) | Amount prepaid for calls |
| (2) | Over subscription | (ii) | Subscription above the offered shares |
| (3) | Calls in arrear | (iii) | Subscription below the offered shares |
| (4) | Calls in advance | (iv) | Amount unpaid on calls |

| | (1) | (2) | (3) | (4) |
|---|---|---|---|---|
| (a) | (i) | (ii) | (iii) | (iv) |
| (b) | (iv) | (iii) | (ii) | (i) |
| (c) | (iii) | (ii) | (iv) | (i) |
| (d) | (iii) | (iv) | (i) | (ii) |

[Ans. (c) 1 - (iii), 2 - (ii), 3 - (iv), 4 - (i)]

9. **If a share of ₹10 on which ₹8 has been paid up is forfeited. Minimum reissue price is**

(a) ₹10 per share (b) ₹8 per share

(c) ₹5 per share (d) ₹2 per share

[Ans. (d) ₹2 per share]

*Hint :*

Minimum reissue price = ₹10 – ₹8
= ₹2

10. **Supreme Ltd. forfeited 100 shares of ₹10 each for non-payment of final call of ₹2 per share. All these shares were re-issued at ₹9 per share. What amount will be transferred to capital reserve account?**

(a) ₹700 (b) ₹800

(c) ₹900 (d) ₹1,000

[Ans. (a) ₹700]

*Hint :*

| | | |
|---|---|---|
| Forfeited amount for 100 shares | = | 900 |
| Final call amount (100 × 2) | = | 200 |
| Capital reserve | = | 700 |

## II. VERY SHORT ANSWER QUESTIONS.

1. **What is a share?**

**Ans.** The capital of a company is divided into small units of fixed amount. These units are called shares.

2. **What is over-subscription?**

**Ans.** When the number of shares applied for is more than the number of shares offered for subscription, it is said to be over subscription.

3. **What is meant by calls in arrear?**

**Ans.** When a shareholder fails to pay the amount due on allotment or on calls, the amount remaining unpaid is known a calls in arrears. In other words, the amount called up but not paid is calls in arrear.

4. **Write a short note on securities premium account.**

**Ans.** When a company issues shares at a price more than the face value (nominal value), the shares are said to be issued at premium. The excess is called as premium amount and is transferred to securities premium account. Securities premium account is shown under reserves and surplus as a separate head in the Note to Accounts to the balance sheet.

5. **Why are the shares forfeited?**

**Ans.** When a shareholder defaults in making payment of allotment and/or call money, the shares may be forfeited. On forfeiture, the share allotment is cancelled and to that extent paid up share capital a reduced. The person ceases to be a shareholder of the company after the shares are forfeited.

## III. Short answer questions.

**1. State the differences between preference shares and equity shares.**

*Ans.*

| | Basis | Equity shares | Preference shares |
|---|---|---|---|
| 1. | Meaning | Equity shares are the ordinary shares of the company representing the part ownership of the shareholder in the company | Preference shares are the shares that carry preferential rights on the matters of payment of dividend and repayment of capital. |
| 2. | Payment of dividend | The dividend is paid after the payment of all liabilities | Priority in payment of dividend over equity shareholders |
| 3. | Rate of dividend | Fluctuating | Fixed |
| 4. | Voting rights | Equity shares carry voting rights | Normally, preference shares do not carry voting rights |
| 5. | Convertibility | Equity shares can never be converted | Preference shares can be converted into equity shares. |

**2. Write a brief note on calls in advance.**

*Ans.* (i) The excess amount paid over the called up value of a share is known as calls in advance.

(ii) It is the excess money paid on application or allotment or calls. Such excess amount can be returned or adjusted towards future payment.

(iii) If the company decides to adjust such amount towards future payment, the excess amount may also be transferred to a separate account called call in advance.

(iv) Calls in advance does not form part of the company's share capital and no dividend is payable on such amount.

(v) In the balance sheet, it should be shown under current liabilities.

**3. What is reissue of forfeited shares?**

*Ans.* (i) Shares forfeited can be reissued by the company.

(ii) The shares can be reissued at any price. But, the reissue price cannot be less than the amount unpaid on forfeited shares.

(iii) Example: If a share of ₹10 on which ₹4 already been paid as application money is forfeited and reissued as fully paid up, then a maximum of ₹6 must be fixed as the new price (10 – 4 = 6)

(iv) When forfeited shares are reissued at a premium, the amount of such premium will be credited to securities premium account.

**4. Write a short note on**

**(a) Authorised capital**

**(b) Reserve capital**

*Ans.* (a) **Authorised capital :**

It means such capital as is authorised by the memorandum of association. It is the maximum amount which can be raised as capital. It is also known as registered capital or nominal capital.

(b) **Reserve capital :**

The company can reserve a part of its subscribed capital to be called up only at the time of winding up. It is called reserve capital.

**5. What is meant by issue of shares for consideration other than cash?**

*Ans.* A company may issue shares for consideration other than cash when the company acquires fixed assets such as land and buildings, machinery, etc under such situation, the following journal entries are to be passed.

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | (i) **For Purchase of asset :** | | | |
| | Respective asset A/c Dr | | xxx | |
| | To Vendor A/c | | | xxx |
| | (ii) **For issue of shares :** | | | |
| | Vendor A/c Dr | | xxx | |
| | To Equity share capital A/c | | | xxx |
| | To Securities premium A/c | | | xxx |
| | (if issued at premium) | | | |

A company may also issue shares a consideration for the purchase of business, to promoters for their services and to brokers and underwriters for commission.

## IV. Exercises.

1. **Progress Ltd. issued 50,000 ordinary shares of ₹10 each, payable ₹2 on application, ₹4 on allotment, ₹2 on first call and ₹2 on final call. All the shares are subscribed and amount was duly received. Pass journal entries.**

***Solution :***

**In the books of progress Ltd Journal entries**

| Date | Particulars | L.F | Debit ₹ | Credit ₹ |
|---|---|---|---|---|
| | Bank A/c (50,000 × 2) Dr<br>To Share application A/c<br>(Application money received) | | 1,00,000 | 1,00,000 |
| | Share application A/c Dr<br>To Share capital A/c<br>(Transfer of share application money to share capital) | | 1,00,000 | 1,00,000 |
| | Share allotment A/c Dr<br>To Share capital A/c<br>(Share allotment money due) | | 2,00,000 | 2,00,000 |
| | Bank A/c Dr<br>To Share allotment A/c<br>(Allotment money received) | | 2,00,000 | 2,00,000 |
| | Equity share first call A/c Dr<br>To Share capital A/c<br>(Share first call money due) | | 1,00,000 | 1,00,000 |
| | Bank A/c Dr<br>To Share first call A/c<br>(Share first call money received) | | 1,00,000 | 1,00,000 |
| | Share second and final call A/c Dr<br>To Share capital A/c<br>(Share second and final call money due) | | 1,00,000 | 1,00,000 |
| | Bank A/c Dr<br>To Share second and final call A/c<br>(Share second and final call money received) | | 1,00,000 | 1,00,000 |

# UNIT 8 FINANCIAL STATEMENT ANALYSIS

## I Multiple Choice Questions

### Choose the correct answer

1. Which of the following statements is not true?
   (a) Notes and schedules also form part of financial statements.
   (b) The tools of financial statement analysis include common-size statement
   (c) Trend analysis refers to the study of movement of figures for one year
   (d) The common–size statements show the relationship of various items with some common base, expressed as percentage of the common base

   [Ans. (c) Trend analysis refers to the study of movement of figures for one year]

2. Balance sheet provides information about the financial position of a business concern
   (a) Over a period of time
   (b) As on a particular date
   (c) For a period of time
   (d) For the accounting period

   [Ans. (b) As on a particular date]

3. Which of the following tools of financial statement analysis is suitable when data relating to several years are to be analysed?
   (a) Cash flow statement
   (b) Common size statement
   (c) Comparative statement
   (d) Trend analysis [Ans. (d) Trend analysis]

4. The financial statements do not exhibit
   (a) Non-monetary data
   (b) Past data
   (c) Short term data
   (d) Long term data

   [Ans. (a) Non-monetary data]

5. Which of the following is not a tool of financial statement analysis?
   (a) Trend analysis
   (b) Common size statement
   (c) Comparative statement
   (d) Standard costing

   [Ans. (d) Standard costing]

6. The term 'fund' refers to
(a) Current liabilities (b) Working capital
(c) Fixed assets
(d) Non-current assets
[Ans. (b) Working capital]

7. **Which of the following statements is not true?**
(a) All the limitations of financial statements are applicable to financial statement analysis also.
(b) Financial statement analysis is only the means and not an end.
(c) Expert knowledge is not required in analysing the financial statements.
(d) Interpretation of the analysed data involves personal judgement.
**[Ans. (c) Expert knowledge is not required in analysing the financial statements.]**

8. **A limited company's sales has increased from ₹ 1,25,000 to ₹ 1,50,000. How does this appear in comparative income statement?**
(a) + 20 % (b) + 120 %
(c) – 120 % (d) – 20 %
[Ans. (a) + 20 %]

**Hint :**

Comparative income statement

$= 1{,}25{,}000 - 1{,}50{,}000 = +25{,}000$

$= \dfrac{+25{,}000}{1{,}25{,}000} \times 100 = +20\ \%$

9. **In a common-size balance sheet, if the percentage of non-current assets is 75, what would be the percentage of current assets?**
(a) 175 (b) 125
(c) 25 (d) 100 [Ans. (c) 25]

**Hint :**

Total assets = Current assets – Non-current assets

$100 = x - 75$

$\therefore x = 100 - 75 = 25$

$\therefore$ Current assets = 25.

10. **Expenses for a business for the first year were ₹ 80,000. In the second year, it was increased to ₹ 88,000. What is the trend percentage in the second year?**
(a) 10 % (b) 110 %
(c) 90 % (d) 11%
[Ans. (b) 110%]

**Hint :**

Trend percentage $= \dfrac{88{,}000}{80{,}000} \times 100 = 110\%$.

## II Very short answer questions

1. **What are financial statements?**

**Ans.** Financial statements are the statements prepared by the business concern at the end of the accounting period to ascertain the operating results and the financial position. The basic financial statements prepared by business concerns are income statement and balance sheet.

2. **List the tools of financial statement analysis.**

**Ans.** Following are the commonly used tools of financial statement analysis
(i) Comparative statement
(ii) Common-size statement
(iii) Trend analysis
(iv) Funds flow analysis
(v) Cash flow analysis

3. **What is working capital?**

**Ans.** The term 'fund' refers to working capital. Working capital refers to the excess of current assets over current liabilities.

4. **When is trend analysis preferred to other tools?**

**Ans.** Trend analysis refers to the study of movement of figures over a period. The trend may be increasing trend or decreasing trend or irregular. When data for more than two years are to be analysed, it may be difficult to use comparative statement.

## III Short answer questions:

1. **'Financial statements are prepared based on the past data'. Explain how this is a limitation.**

**Ans.** Following are the limitations of financial statements.

(i) **Lack of qualitative information :**
Qualitative information that is non-monetary information is also important for business decisions.

(ii) **Record of historical data :**
Financial statements are prepared based on historical data. They may not reflect the current position.

2. **Write a short note on cash flow analysis.**

**Ans.** (i) Cash flow analysis is concerned with preparation of cash flow statement which shows the inflow and outflow of cash and cash equivalents in a given period of time.

(ii) Cash includes cash in hand and demand deposits with banks.

(iii) Cash equivalents denote short term investments which can be realised easily within a short period of time, without much loss in value.

(iv) Cash flow analysis helps in assessing the liquidity and solvency of a business concern.

**3. Briefly explain any three limitations of financial statements.**

**Ans.** (i) **Give only interim reports:**

Financial statements are prepared at the end of every accounting period. But the actual position of the business can be known only when the business is closed.

(ii) **Limited access to external users:**

The external users do not have detailed and frequent information of financial results as they have limited access.

(iii) **Influenced by personal judgement:**

Preparation of financial statements may be influenced by personal judgements and therefore these are not free from bias.

**4. Explain the steps involved in preparing comparative statement.**

**Ans.** A comparative statement has five columns. Following are the steps to be followed in preparation of the comparative statement.

(i) **Column 1:** In this column, particulars of items of income statement or balance sheet are written.

(ii) **Column 2:** Enter absolute amount of year 1

(iii) **Column 3:** Enter absolute amount of year 2

(iv) **Column 4:** Show the difference in amounts between year 1 and year 2. If there is an increase in year 2, put plus sign and if there is decrease put minus sign.

(v) **Column 5:** Show percentage increase or decrease of the difference amount shown in column 4 by dividing the amount shown in column 4 (absolute amount of increase or decrease) by column 2 (year 1 amount). That is,

Percentage increase or decrease

$$= \frac{\text{Absolute amount of increase or decrease}}{\text{Year 1 amount}} \times 100$$

**Format of comparative statement:**

| Particular | Year 1 | Year 2 | Absolute amount of increase (+) or Decrease (–) | Percentage increase (+) or decrease (–) |
|---|---|---|---|---|
| | ₹ | ₹ | ₹ | |
| (1) | (2) | (3) | (4) | (5) |

**5. Explain the procedure for preparing common-size statement.**

**Ans.** Common-size statement can be prepared with three columns. Following are the steps to be followed in preparation of common-size statement:

(i) **Column 1:** In this column, particulars of items of income statement or balance sheet are written.

(ii) **Column 2:** Enter absolute amount.

(iii) **Column 3:** Choose a common base as 100. For example, revenue from operations can be taken as the base for income statement and total of balance sheet can be taken as the base for balance sheet. Work out the percentage for all the items of column 2 in terms of the common base and enter them in column 3.

**Format of common-size statement:**

| Particulars | Absolute amount | Percentage |
|---|---|---|
| | | |

## IV. Exercises:

### Comparative statement analysis

1. From the following particulars, prepare comparative income statement of Arul Ltd.

| Particulars | 2015-16 ₹ | 2016-17 ₹ |
|---|---|---|
| Revenue from operations | 50,000 | 60,000 |
| Other income | 10,000 | 30,000 |
| Expenses | 40,000 | 50,000 |

*Solution* : Comparative income statement of Arul Ltd for the years ended 31st March 2016 and 31st March 2017

| Particulars | 2015-16 | 2016-17 | Absolute amount of increase (+) or decrease (–) | Percentage increase (+) or decrease (–) |
|---|---|---|---|---|
| Revenue from Operations | 50,000 | 60,000 | + 10,000 | + 20 |
| Add : Other income | 10,000 | 30,000 | + 20,000 | + 200 |
| Total revenue | 60,000 | 90,000 | + 30,000 | + 50 |
| Less : Expenses | 40,000 | 50,000 | + 10,000 | + 25 |
| Profit before tax | 20,000 | 40,000 | + 20,000 | 100 |

**Note:**

Computation of percentage increase for revenue form operations = $\frac{10,000}{50,000} \times 100 = 20\%$

Percentage increase for other incomes = $\frac{20,000}{10,000} \times 100 = 200\%$

Percentage increase for expenses = $\frac{10,000}{40,000} \times 100 = 25\%$

2. From the following particulars, prepare comparative income statement of Barani Ltd.

| Particulars | 2016-17 ₹ | 2017-18 ₹ |
|---|---|---|
| Revenue from operations | 30,000 | 45,000 |
| Other income | 4,000 | 6,000 |
| Expenses | 10,000 | 15,000 |
| Income tax | 30% | 30% |

*Solution* : Comparative income statement of Barani Ltd. for the years ended 2017 and 2018

| Particulars | 2016-17 ₹ | 2017-18 ₹ | Absolute amount of increase (+) or decrease (–) | Percentage increase (+) or decrease (–) |
|---|---|---|---|---|
| Revenue from Operations | 30,000 | 45,000 | + 15,000 | + 50 |
| Add : Other income | 4,000 | 6,000 | + 2,000 | + 50 |
| Total revenue | 34,000 | 51,000 | + 17,000 | + 50 |
| Less : Expenses | 10,000 | 15,000 | + 5,000 | + 50 |
| Profit before tax | 24,000 | 36,000 | + 12,000 | + 50 |
| Less : Tax (30%) | 7,200 | 10,800 | + 3,600 | + 50 |
| Profit after tax | 16,800 | 25,200 | + 8,400 | + 50 |

**Note:**

Percentage increase for revenue from operations $= \frac{15,000}{30,000} \times 100 = 50\%$

Percentage increase for other incomes $= \frac{2000}{4000} \times 100 = 50\%$

Percentage increase for expenses $= \frac{5,000}{10,000} \times 100 = 50\%$

Percentage increase for Tax $= \frac{3,600}{7,200} \times 100 = 50\%$

**3. From the following particulars, prepare comparative income statement of Daniel Ltd.**

| Particulars | 2015-16 ₹ | 2016-17 ₹ |
|---|---|---|
| Revenue from operations | 40,000 | 50,000 |
| Operating expenses | 25,000 | 27,500 |
| Income tax (% of the profit before tax) | 30 | 30 |

***Solution :***

**Comparative income statement of Daniel Ltd for the year ended 2016 and 2017**

| Particulars | 2015-16 ₹ | 2016-17 ₹ | Absolute amount of increase (+) or decrease (–) ₹ | Percentage increase (+) or decrease (–) |
|---|---|---|---|---|
| Revenue from Operations | 40,000 | 50,000 | + 10,000 | + 25 |
| <u>Less :</u> Operating expenses | 25,000 | 27,500 | + 2,500 | + 10 |
| Profit before tax | 15,000 | 22,500 | + 7,500 | + 50 |
| <u>Less :</u> Income tax | 4,500 | 6750 | + 2,250 | + 50 |
| Profit after tax | 10,500 | 15,750 | + 5,250 | + 50 |

**Note:**

Percentage increase for revenue from operations $= \frac{10,000}{40,000} \times 100 = 25\%$

Percentage increase for operating expenses $= \frac{2,500}{25,000} \times 100 = 10\%$

Percentage increase for profit before tax $= \frac{7,500}{15,000} \times 100 = 50\%$

Percentage increase for income for Income tax $= \frac{2250}{4500} \times 100 = 50\%$

Percentage increase for profit after tax $= \frac{5250}{10,500} \times 100 = 50\%$

**10.** Prepare common-size statement of financial position for the following particulars of Rani Ltd.

| Particulars | 31st March, 2016 ₹ | 31st March, 2016 ₹ |
|---|---|---|
| **I EQUITY AND LIABILITIES** | | |
| Shareholders' Fund | 5,40,000 | 6,40,000 |
| Non-current liabilities | 2,70,000 | 2,50,000 |
| Current liabilities | 90,000 | 1,50,000 |
| Total | 4,00,000 | 10,00,000 |
| **II ASSETS** | | |
| Non-current assets | 7,20,000 | 8,00,000 |
| Current assets | 1,80,000 | 2,00,000 |
| Total | 9,00,000 | 10,00,000 |

*Solution :*

**Common-size balance sheet of Rani Ltd for the year ended 31st March, 2016 and 31st March, 2017**

| Particulars | Absolute amount 2015-16 | Percentage of total assets | Absolute amount 2016-17 | Percentage of total assets |
|---|---|---|---|---|
| | ₹ | ₹ | ₹ | |
| **I Equity and Liabilities** | | | | |
| Share holder's funds | 5,40,000 | 60 | 6,00,000 | 60 |
| Non-current liabilities | 2,70,000 | 30 | 2,50,000 | 25 |
| Current liabilities | 90,000 | 10 | 1,50,000 | 15 |
| Total | 9,00,000 | 100 | 10,00,000 | 100 |
| **II Assets** | | | | |
| Non-current assets | 7,20,000 | 80 | 8,00,000 | 80 |
| Current assets | 1,80,000 | 20 | 2,00,000 | 20 |
| Total | 9,00,000 | 100 | 10,00,000 | 100 |

**Note: In 2015-16**

Percentage of shareholders fund $= \frac{5,40,000}{9,00,000} \times 100 = 60\%$

Percentage of Non-current liabilities$= \frac{2,70,000}{9,00,000} \times 100 = 30\%$

Percentage of current liabilities $= \frac{90,000}{9,00,000} \times 100 = 10\%$

Percentage of non-current assets $= \frac{7,20,000}{9,00,000} \times 100 = 80\%$

Percentage of current assets $= \frac{1,80,000}{9,00,000} \times 100 = 20\%$

**In 2016-17**

Percentage of share holders fund $= \frac{6,00,000}{10,00,000} \times 100 = 60\%$

Percentage of Non-current liabilities = $\frac{2,50,000}{10,00,000} \times 100$ = 25%

Percentage of current liabilities = $\frac{1,50,000}{10,00,000} \times 100$ = 15%

Percentage of Non-current assets = $\frac{8,00,000}{10,00,000} \times 100$ = 80%

Percentage of current assets = $\frac{2,00,000}{10,00,000} \times 100$ = 20%

**11. Prepare common-size statement of financial position for the following particulars of Yasmin Ltd. and Sakthi Ltd.**

| Particulars | Yasmin Ltd. ₹ | Sakthi Ltd. ₹ |
|---|---|---|
| **I EQUITY AND LIABILITIES** | | |
| 1. Shareholders' Fund | | |
| a) Share capital | 2.00,000 | 3,00,000 |
| b) Reserves and surplus | 50,000 | 60,000 |
| 2. Non-current liabilities | | |
| Long-term borrowings | 1,50,000 | 1,80,000 |
| 3. Current liabilities | | |
| Trade payables | 1,00,000 | 60,000 |
| Total | 5,00,000 | 6,00,000 |
| **II ASSETS** | | |
| 1. Non-current assets | | |
| a) Fixed assets | 2,00,000 | 3,00,000 |
| b) Non - current investments | 50,000 | 1,20,000 |
| 2. Current assets | | |
| Inventories | 2,00,0000 | 90,000 |
| Cash and cash equivalents | 50,000 | 90,000 |
| Total | 5,00,000 | 6,00,000 |

*Solution :*

**Common-size balance sheet of Yasmin Ltd and Sakthi Ltd**

| Particulars | Yasmin Ltd | | Sakthi Ltd | |
|---|---|---|---|---|
| | Absolute amount ₹ | Percentage of total assets | Absolute Amount ₹ | Percentage of total assets |
| **I Equity and liabilities** | | | | |
| 1. Shares holder's fund | | | | |
| a. Share capital | 2,00,000 | 40 | 3,00,000 | 50 |
| b. Reserve and surplus | 50,000 | 10 | 60,000 | 10 |
| 2. Non-current liabilities | | | | |
| Long-term borrowings | 1,50,000 | 30 | 1,80,000 | 30 |
| 3. Current liabilities | | | | |
| Trade payables | 1,00,000 | 20 | 60,000 | 10 |
| Total | 5,00,000 | 100 | 6,00,000 | 100 |
| **II. Assets** | | | | |
| 1. Non-current assets | | | | |
| a. Fixed assets | 2,00,000 | 40 | 3,00,000 | 50 |
| b. Non - current investments | 50,000 | 10 | 1,20,000 | 20 |
| 2. Current assets | | | | |
| Inventories | 2,00,000 | 40 | 90,000 | 15 |
| Cash and cash equivalents | 50,000 | 10 | 90,000 | 15 |
| Total | 5,00,000 | 100 | 6,00,000 | 100 |

**Note: Yasmin Ltd.**

Percentage of Share capital $= \frac{2,00,000}{5,00,000} \times 100 = 40\%$

Percentage of Reserves and surplus $= \frac{50,000}{5,00,000} \times 100 = 10\%$

Percentage of Long-term borrowing $= \frac{1,50,000}{5,00,000} \times 100 = 30\%$

Percentage of Trade payables $= \frac{1,00,000}{5,00,000} \times 100 = 20\%$

Percentage of fixed assets $= \frac{2,00,000}{5,00,000} \times 100 = 40\%$

Percentage of Non-current investment $= \frac{50,000}{5,00,000} \times 100 = 10\%$

Percentage of inventories $= \frac{2,00,000}{50,000} \times 100 = 40\%$

Percentage of cash and cash equivalents $= \frac{50,000}{5,00,000} \times 100 = 10\%$

**Note: Sakthi Ltd.**

Percentage of Share capital $= \frac{3,00,000}{6,00,000} \times 100 = 50\%$

Percentage of Reserves and surplus $= \frac{60,000}{6,00,000} \times 100 = 10\%$

Percentage of Long-term borrowing $= \frac{1,80,000}{6,00,000} \times 100 = 30\%$

Percentage of Trade payables $= \frac{60,000}{6,00,000} \times 100 = 10\%$

Percentage of fixed assets $= \frac{3,00,000}{6,00,000} \times 100 = 50\%$

Percentage of Non-current investment $= \frac{1,20,000}{6,00,000} \times 100 = 20\%$

Percentage of Inventories $= \frac{90,000}{6,00,000} \times 100 = 15\%$

Percentage of cash and cash equivalents $= \frac{90,000}{6,00,000} \times 100 = 15\%$

## Trend analysis :

**12. From the following particulars, calculate the trend percentages of Kala Ltd.**

| Particulars | ₹ in thousands | | |
|---|---|---|---|
| | 2015-16 | 2016-17 | 2017-18 |
| Revenue from operations | 400 | 500 | 600 |
| Other income | 100 | 150 | 200 |
| Expenses | 200 | 290 | 350 |

*Solution :*

**Trend analysis for kala ltd**

| Particulars | ₹ in thousands | | | Trends percentage | | |
|---|---|---|---|---|---|---|
| | 2015-16 | 2016-17 | 2017-18 | 2015-16 | 2016-17 | 2017-18 |
| Revenue from operations | 400 | 500 | 600 | 100 | 125 | 150 |
| <u>Add :</u> Other income | 100 | 150 | 200 | 100 | 150 | 200 |
| Total revenue | 500 | 650 | 800 | 100 | 130 | 160 |
| <u>Less :</u> Expenses | 200 | 290 | 350 | 100 | 145 | 175 |
| Profit after tax | 300 | 360 | 450 | 100 | 120 | 150 |

**Note: 2016 - 17.**

Percentage for Revenue from operations $= \frac{500}{400} \times 100 = 125\%$

Percentage of other income $= \frac{150}{100} \times 100 = 150\%$

Percentage of total revenue $= \frac{650}{500} \times 100 = 130\%$

Percentage for expenses $= \frac{290}{500} \times 100 = 145\%$

Percentage for profit before tax $= \frac{360}{300} \times 100 = 120\%$

In 2017 - 18.

Percentage for revenue from operations $= \frac{600}{400} \times 100 = 150\%$

Percentage for other income $= \frac{200}{100} \times 100 = 200\%$

Percentage of total revenue $= \frac{800}{500} \times 100 = 160\%$

Percentage for expenses $= \frac{350}{200} \times 100 = 175\%$

Percentage for profit before tax $= \frac{450}{300} \times 100 = 150\%$

**13. From the following particulars, calculate the Trend percentages of Kavitha Ltd.**

| Particulars | ₹ in thousands | | |
|---|---|---|---|
| | 2015-16 | 2016-17 | 2017-18 |
| Revenue from operations | 100 | 125 | 150 |
| Other income | 20 | 25 | 30 |
| Expenses | 100 | 120 | 80 |
| Income Tax | 30% | 30% | 30% |

*Solution :*

Trend analysis for Kavitha Ltd.

| Particular | ₹ in thousands | | | Trends percentage | | |
|---|---|---|---|---|---|---|
| | 2015-16 | 2016-17 | 2017-18 | 2015-16 | 2016-17 | 2017-18 |
| Revenue from operations | 100 | 125 | 150 | 100 | 125 | 150 |
| Add : Other income | 20 | 25 | 30 | 100 | 125 | 150 |
| Total revenue | 120 | 150 | 180 | 100 | 125 | 150 |
| Less : Expenses | 100 | 120 | 80 | 100 | 120 | 80 |
| Project before tax | 20 | 30 | 100 | 100 | 150 | 500 |
| Less Income tax (30%) | 6 | 9 | 30 | 100 | 150 | 500 |
| Profit after tax | 14 | 21 | 70 | 100 | 150 | 500 |

Note: 2016 - 17.

Percentage for Revenue from operations $= \frac{125}{100} \times 100 = 125\%$

Percentage of other income $= \frac{25}{20} \times 100 = 125\%$

Percentage of total revenue $= \frac{150}{120} \times 100 = 125\%$

Percentage for expenses $= \frac{120}{100} \times 100 = 120\%$

Percentage for before tax $= \frac{30}{20} \times 100 = 150\%$

Percentage for profit before tax $= \frac{21}{14} \times 100 = 150\%$

**In 2017 - 18.**

Percentage for revenue from operations $= \frac{150}{100} \times 100 = 150\%$

Percentage for other income $= \frac{25}{20} \times 100 = 125\%$

Percentage of total revenue $= \frac{180}{120} \times 100 = 150\%$

Percentage for expenses $= \frac{80}{100} \times 100 = 80\%$

Percentage for profit before tax $= \frac{100}{20} \times 100 = 500\%$

Percentage for profit after tax $= \frac{70}{14} \times 100 = 500\%$

**14. From the following particulars, calculate the trend percentages of Kumar Ltd.**

| Particulars | ₹ in thousands | | |
|---|---|---|---|
| | 2015-16 | 2016-17 | 2017-18 |
| Revenue from operations | 300 | 270 | 150 |
| Other income | 50 | 80 | 60 |
| Expenses | 250 | 200 | 125 |
| Income Tax | 40 | 40 | 40 |

*Solution :*

**Trend analysis for Kumar ltd**

| Particulars | ₹ in thousands | | | Trends percentage | | |
|---|---|---|---|---|---|---|
| | 2015-16 | 2016-17 | 2017-18 | 2015-16 | 2016-17 | 2017-18 |
| Revenue from operations | 300 | 270 | 150 | 100 | 90 | 50 |
| Add: Other income | 50 | 80 | 60 | 100 | 160 | 120 |
| | 350 | 350 | 210 | 100 | 100 | 60 |
| Less: Expenses | 250 | 200 | 125 | 100 | 80 | 50 |
| Profit before tax | 100 | 150 | 85 | 100 | 150 | 85 |
| Less Income tax (40%) | 40 | 60 | 34 | 100 | 150 | 85 |
| Profit after tax | 60 | 90 | 51 | 100 | 150 | 85 |

**Note: 2016 - 17.**

Percentage for Revenue from operation = $\frac{270}{300} \times 100 = 90\%$

Percentage of other income = $\frac{80}{50} \times 100 = 160\%$

Percentage for expenses = $\frac{200}{250} \times 100 = 80\%$

Percentage for before tax = $\frac{150}{100} \times 100 = 150\%$

Percentage for profit after tax = $\frac{90}{60} \times 100 = 150\%$

**In 2017 - 18.**

Percentage for revenue from operations = $\frac{150}{300} \times 100 = 50\%$

Percentage for other income = $\frac{60}{50} \times 100 = 120\%$

Percentage for expenses = $\frac{125}{250} \times 100 = 85\%$

Percentage for profit before tax = $\frac{85}{100} \times 100 = 85\%$

Percentage for income tax 40% = $\frac{34}{40} \times 100 = 85\%$

**15.** **From the following particulars, calculate the trend percentages of Anu Ltd.**

| Particulars | ₹ in thousands | | |
|---|---|---|---|
| | Year 1 | Year 2 | Year 3 |
| **I EQUITY AND LIABILITIES** | | | |
| Shareholders' Fund | 500 | 550 | 600 |
| Non-current liabilities | 200 | 250 | 240 |
| Current liabilities | 100 | 80 | 120 |
| Total | 800 | 880 | 960 |
| **II ASSETS** | | | |
| Non-current assets | 600 | 720 | 780 |
| Current assets | 200 | 160 | 180 |
| Total | 800 | 880 | 960 |

*Solution :*

**Trend analysis for Anu Ltd**

| Particulars | ₹ in thousands | | | Trends percentage | | |
|---|---|---|---|---|---|---|
| | Year 1 | Year 2 | Year 3 | Year 1 | Year 2 | Year 3 |
| **I Equity and liabilities** | | | | | | |
| Shares holder's fund | 500 | 550 | 600 | 100 | 110 | 120 |
| Non-current liabilities | 200 | 250 | 240 | 100 | 125 | 120 |
| Current liabilities | 100 | 80 | 120 | 100 | 80 | 120 |
| Total | 800 | 880 | 960 | 100 | 110 | 120 |
| **II. Assets** | | | | | | |
| Non-current assets | 600 | 720 | 780 | 100 | 120 | 130 |
| Current assets | 200 | 100 | 180 | 100 | 80 | 90 |
| Total | 800 | 880 | 960 | 100 | 110 | 120 |

**16.** **From the following particulars, calculate the trend percentages of Babu Ltd.**

| Particulars | ₹ in thousands | | |
|---|---|---|---|
| | Year 1 | Year 2 | Year 3 |
| **I EQUITY AND LIABILITIES** | | | |
| 1. Shareholders' Fund | | | |
| a) Share capital | 100 | 127 | 106 |
| b) Reserves and surplus | 30 | 30 | 45 |
| 2. Non-current liabilities | | | |
| Long-term borrowings | 70 | 77 | 84 |
| 3. Current liabilities | | | |
| Trade payables | 20 | 30 | 40 |
| Total | 220 | 264 | 275 |
| **II ASSETS** | | | |
| 1. Non-current assets | | | |
| a) Fixed assets | 100 | 118 | 103 |
| b) Non - current investments | 40 | 50 | 60 |
| 2. Current assets | | | |
| Inventories | 60 | 66 | 72 |
| Cash and cash equivalents | 20 | 30 | 40 |
| Total | 220 | 264 | 274 |

*Solution :*

**Trends analysis for Babu ltd**

| Particular | ₹ in thousands | | | Trends percentage | | |
|---|---|---|---|---|---|---|
| | Year 1 | Year 2 | Year 3 | Year 1 | Year 2 | Year 3 |
| **I Equity and liabilities** | | | | | | |
| 1. Shareholder's fund | | | | | | |
| a. Share capital | 100 | 127 | 106 | 100 | 127 | 106 |
| b. Reserve and surplus | 30 | 30 | 45 | 100 | 100 | 150 |
| 2. Non-current liabilities | | | | | | |
| Long-term borrowings | 70 | 77 | 84 | 100 | 110 | 120 |
| 3. Current liabilities | | | | | | |
| Trade payables | 20 | 30 | 40 | 100 | 150 | 200 |
| Total | 220 | 264 | 275 | 100 | 120 | 125 |
| **II. Assets** | | | | | | |
| 1. Non-current assets | | | | | | |
| a. Fixed assets | 100 | 118 | 103 | 100 | 118 | 103 |
| b. Non -investment | 40 | 50 | 60 | 100 | 125 | 150 |
| 2. Current assets | | | | | | |
| Inventories | 60 | 66 | 72 | 100 | 110 | 120 |
| Cash and cash equivalents | 20 | 30 | 40 | 100 | 150 | 200 |
| Total | 220 | 264 | 275 | 100 | 120 | 125 |

# UNIT 9 RATIO ANALYSIS

## I MULTIPLE CHOICE QUESTIONS

### CHOOSE THE CORRECT ANSWER

1. The mathematical expression that provides a measure of the relationship between two figures is called
   (a) Conclusion (b) Ratio
   (c) Model (d) Decision
   [Ans. (b) Ratio]

2. Current ratio indicates
   (a) Ability to meet short term obligations
   (b) Efficiency of management
   (c) Profitability
   (d) Long term solvency
   [Ans. (a) Ability to meet short term obligations]

3. Current assets excluding inventory and prepaid expenses is called
   (a) Reserves (b) Tangible assets
   (c) Funds (d) Quick assets
   [Ans. (d) Quick assets]

4. Debt equity ratio is a measure of
   (a) Short term solvency
   (b) Long term solvency
   (c) Profitability
   (d) Efficiency [Ans. (b) Long term solvency]

5. Match List I with List II and select the correct answer using the codes given below:

| List I | | List II | |
|---|---|---|---|
| (i) | Current ratio | 1. | Liquidity |
| (ii) | Net profit ratio | 2. | Efficiency |
| (iii) | Debt-equity ratio | 3. | Long term solvency |
| (iv) | Inventory turnover ratio | 4. | Profitability |

Codes :

| | (i) | (ii) | (iii) | (iv) |
|---|---|---|---|---|
| (a) | 1 | 4 | 3 | 2 |
| (b) | 3 | 2 | 4 | 1 |
| (c) | 4 | 3 | 2 | 1 |
| (d) | 1 | 2 | 3 | 4 |

[Ans. (a) (i)-1, (ii)-4, (iii)-3, (iv)-2]

6. **To test the liquidity of a concern, which of the following ratios are useful?**
(i) **Quick ratio**
(ii) **Net profit ratio**
(iii) **Debt-equity ratio**
(iv) **Current ratio**
**Select the correct answer using the codes given below:**
(a) (i) and (ii) (b) (i) and (iv)
(c) (ii) and (iii) (d) (ii) and (iv)
**[Ans. (b) (i) and (iv)]**

7. **Proportion of share holder's funds to total assets is called**
(a) Proprietary ratio
(b) Capital gearing ratio
(c) Debt equity ratio
(d) Current ratio **[Ans. (a) Proprietary ratio]**

8. **Which one of the following is not correctly matched?**

| | | | |
|---|---|---|---|
| (a) | Liquid ratio | – | Proportion |
| (b) | Gross profit ratio | – | Percentage |
| (c) | Fixed assets turnover ratio | – | Percentage |
| (d) | Debt-equity ratio | – | Proportion |

**[Ans. (c) Fixed assets turnover ratio – Percentage]**

9. **Current liabilities ₹40,000; Current assets ₹1,00,000; Inventory ₹20,000. Quick ratio is**
(a) 1:1 (b) 2.5:1 (c) 2:1 (d) 1:2
**[Ans. (c) 2:1]**

*Hint :*

$$\text{Quick ratio} = \frac{\text{Quick assets}}{\text{Current liabilities}}$$

Quick assets = Total current assets – Inventories – prepaid expenses.

$$= 1{,}00{,}000 - 20{,}000 - 0$$

$$= 80{,}000$$

Current liabilities = 40,000

$$\therefore \text{Quick ratio} = \frac{80{,}000}{40{,}000} = 2:1$$

10. **Cost of revenue from operations ₹ 3,00,000; Inventory in the beginning of the year ₹ 60,000; Inventory at the close of the year ₹ 40,000. Inventory turnover ratio is**
(a) 2 times (b) 3 times
(c) 6 times (d) 8 times
**[Ans. (c) 6 times]**

*Hint :*

Inventory turnover ratio

$$= \frac{\text{Cost of revenue from operations}}{\text{Average inventory}}$$

Cost of revenue from operations = ₹ 3,00,000

Average inventory

$$= \frac{\text{Opening inventory + Closing inventory}}{2}$$

$$= \frac{60{,}000 + 40{,}000}{2} = ₹\ 50{,}000$$

$$\therefore \text{Inventory turnover ratio} = \frac{3{,}00{,}000}{50{,}000} = 6 \text{ times}$$

## II VERY SHORT ANSWER QUESTIONS :

1. **What is meant by accounting ratios?**

**Ans.** (i) Ratio is a mathematical expression of relationship between two related or interdependent items.
(ii) It is the numerical or quantitative relationship between two items
(iii) It is calculated by dividing one item by the other related item.
(iv) When ratios are calculated on the basis of accounting information, these are called **'accounting ratios'**.

2. **What is quick ratio?**

**Ans.** (i) Quick ratio gives the proportion of quick assets to current liabilities.
(ii) It indicates whether the business concern is in a position to pay its current liabilities as and when they become due, out of its quick assets.
(iii) It is otherwise called liquid ratio or acid test ratio.
(iv) It is calculated as follows:

$$\text{Quick ratio} = \frac{\text{Quick assets}}{\text{Current liabilities}}$$

3. **What is meant by debt equity ratio?**

**Ans.** (i) Debt equity ratio is calculated to assess the long term solvency position of a business concern.
(ii) Debt equity ratio expresses the relationship between long term debt and shareholders' funds.
(iii) It is computed as follows:

$$\text{Debt equity ratio} = \frac{\text{Long term debt}}{\text{Shareholders funds}}$$

**4. What does return on investment ratio indicate?**

**Ans.** (i) Return on investment shows the proportion of net profit before interest and tax to capital employed (shareholders' funds and long term debts).

(ii) This ratio measures how efficiently the capital employed is used in the business.

(iii) It is an overall measure of profitability of a business concern.

(iv) It is computed as below:

Return on Investment (ROI)

$$= \frac{\text{Net profit before interest and tax}}{\text{Capital employed}} \times 100$$

**5. State any two limitations of ratio analysis.**

**Ans.** (i) **Ratios are only means :** Ratios are not end in themselves but they are only means to achieve a particular purpose.

(ii) **Accuracy of financial information :** The accuracy of a ratio depends on the accuracy of information taken from financial statements.

## III Short answer questions

**1. Explain the objectives of ratio analysis.**

**Ans. Following are the objectives of ratio analysis :**

(i) To simplify accounting figures

(ii) To facilitate analysis of financial statements

(iii) To analyse the operational efficiency of a business

(iv) To help in budgeting and forecasting

(v) To facilitate intra firm and inter firm comparison of performance

**2. What is inventory conversion period? How to calculated it?**

**Ans.** (i) Inventory conversion period is the time taken to sell the inventory.

(ii) A shorter inventory conversion period indicates more efficiency in the management of inventory.

(iii) It is computed as follows :

Inventory conversion period (in days)

$$= \frac{\text{Number of days in a year}}{\text{Inventory turnover ratio}}$$

Inventory conversion period (in months)

$$= \frac{\text{Number of month in a year}}{\text{Inventory turnover ratio}}$$

**3. How is operating profit ascertained?**

**Ans.** (i) Operating profit ratio gives the proportion of operating profit to revenue from operations.

(ii) Operating profit ratio is an indicator of operational efficiency of an organisation.

(iii) It may be computed as follows:

Operating profit ratio

$$= \frac{\text{Operating profit}}{\text{Revenue from operations}} \times 100$$

Alternatively, it is calculated as under.

Operating profit ratio = 100 – Operating cost ratio

Operating profit = Revenue from operations – Operating cost

(iv) A higher ratio indicates better profitability. Greater the operting ratio, higher is the margin available for paying non-operating expenses.

**4. State any three advantages of ratio analysis.**

**Ans. Following are the advantages of ratio analysis:**

(i) **Measuring operational efficiency :** Ratio analysis helps to know operational efficiency of a business by finding the relationship between operating cost and revenues and also by comparison of present ratios with those of the past ratios.

(ii) **Facilitating investment decisions :** Ratio analysis helps the management in making effective decisions regarding profitable avenues of investment.

(iii) **Analysing the profitability :** Ratio analysis helps to analyse the profitability of a business in terms of sales and investments.

**5. Bring out the limitations of ratio analysis.**

**Ans. Following are the limitations of ratio analysis:**

(i) **Accuracy of financial information :** The accuracy of a ratio depends on the accuracy of information taken from financial statements.

(ii) **Consistency in preparation of financial statements :** Inter-firm comparisons with the help of ratio analysis will be meaningful only if the firms follow uniform accounting procedures consistently.

(iii) **Non-availability of standards or norms :** Ratios will be meaningful only if they are compared with accepted standards or norms. Only few financial ratios have universally recognised standards.

(iv) **Change in price level :** Ratio analysis may not reflect price level changes and current values as they are calculated based on historical data given in financial statements.

## IV Exercises

### Liquidity ratios

**1. Calculate the current ratio from the following information.**

| Particulars | ₹ | Particulars | ₹ |
|---|---|---|---|
| Current investments | 40,000 | Fixed assets | 5,00,000 |
| Inventories | 2,00,000 | Trade creditors | 80,000 |
| Trade debtors | 1,20,000 | Bills payable | 50,000 |
| Bills receivable | 80,000 | Expenses payable | 20,000 |
| Cash and cash equivalents | 10,000 | Non-current liability | 3,00,000 |

***Solution :***

Current ratio $= \dfrac{\text{Current assets}}{\text{Current liabilities}}$

Current assets = Current investments + Inventories + Bills receivables + Trade debtors + Cash and cash equivalents

= ₹40,000 + ₹2,00,000 + ₹1,20,000 + ₹80,000 + ₹10,000

= ₹4,50,000

Current liabilities = Trade creditors + Bills payable + Expenses payable

= ₹80,000 + ₹50,000 + ₹20,000 = ₹1,50,000

Current ratio $= \dfrac{4,50,000}{1,50,000} = 3:1$

**2. Calculate quick ratio: Total current liabilities ₹ 2,40,000; Total current assets ₹ 4,50,000; Inventories ₹ 70,000; Prepaid expenses ₹ 20,000**

***Solution :***

Quick ratio $= \dfrac{\text{Quick assets}}{\text{Current liabilities}}$

Quick assets = Current assets – Inventories – Prepaid expenses

= ₹4,50,000 + ₹70,000 – ₹20,000

= ₹3,60,000

Quick ratio $= \dfrac{3,60,000}{2,40,000} = 1.5:1$

**3. Following is the balance sheet of Lakshmi Ltd. as on 31st March, 2019:**

| Particulars | ₹ |
|---|---|
| **I. EQUITY AND LIABILITIES** | |
| **1. Shareholders' funds** | |
| Equity share capital | 4,00,000 |
| **2. Non-current liabilities** | |
| Long term borrowings | 2,00,000 |
| **3. Current liabilities** | |
| (a) Short-term borrowings | 50,000 |
| (b) Trade payables | 3,10,000 |
| (c) Other current liabilities | |
| Expenses payable | 15,000 |
| (d) Short-term provisions | 25,000 |
| **Total** | **10,00,000** |

| Particulars | ₹ |
|---|---|
| **II. ASSETS** | |
| **1. Non-current assets** | |
| (a) Fixed assets | 4,00,000 |
| Tangible assets | |
| **2. Current assets** | |
| (a) Inventories | 1,60,000 |
| (b) Trade debtors | 3,20,000 |
| (c) Cash and cash equivalents | 80,000 |
| (d) Other current assets | |
| Prepaid expenses | 40,000 |
| **Total** | **10,00,000** |

**Calculate:**

**(i) Current ratio (ii) Quick ratio**

***Solution :***

(i) Current ratio $= \dfrac{\text{Current assets}}{\text{Current liabilities}}$

Current assets = Inventories + Trade debtors + Cash and cash equivalents + Prepaid expenses

= ₹1,60,0,000 + ₹3,20,000 + ₹80,000 + ₹40,000 = ₹6,00,000

Current liabilities = Short term borrowings + Trade payables + Expenses payable + Short term provisions

= ₹50,000 + ₹3,10,000 + ₹15,000 + ₹25,000 = ₹4,00,000

Current ratio $= \dfrac{6,00,000}{4,00,000} = 1.5:1$

(ii) Quick ratio $= \dfrac{\text{Quick assets}}{\text{Current liabilities}}$

Quick assets = Current assets – Inventories – Prepaid expenses

= ₹6,00,000 – ₹1,60,000 – ₹40,000 = ₹4,00,000

Quick ratio $= \dfrac{4,00,000}{4,00,000} = 1:1$

### Long term solvency ratios

**4. From the following information calculate debt equity ratio.**

**Balance Sheet (Extract) as on 31st March, 2019**

| Particulars | Amount ₹ |
|---|---|
| **I. EQUITY AND LIABILITIES** | |
| **1. Shareholders' funds** | |
| (a) Share capital | |
| Equity share capital | 6,00,000 |
| (b) Reserves and surplus | 2,00,000 |
| **2. Non-current liabilities** | |
| Long-term borrowings (Debentures) | 6,00,000 |
| **3. Current liabilities** | |
| (a) Trade payables | 1,60,000 |
| (b) Other current liabilities | |
| Outstanding expenses | 40,000 |
| **Total** | **16,00,000** |

**Solution :**

$$\text{Debt equity ratio} = \frac{\text{Long term debt}}{\text{Shareholders funds}}$$

Long term debt = Debentures

= ₹6,00,000

Shareholder's funds = Equity share capital + Reserves and surplus

= ₹6,00,000 + ₹2,00,000 = ₹8,00,000

$$\therefore \text{Debt equity ratio} = \frac{6,00,000}{8,00,000} = 0.75:1$$

5. From the following Balance Sheet of Sundaram Ltd. calculate proprietary ratio:

**Balance sheet of Sundaram Ltd. as on 31.3.2019**

| Particulars | Amount ₹ |
|---|---|
| **I. EQUITY AND LIABILITIES** | |
| **1. Shareholders' funds** | |
| (a) Share capital | |
| (i) Equity share capital | 2,50,000 |
| (ii) Preference share capital | 1,50,000 |
| (b) Reserves and surplus | 50,000 |
| **2. Non-current liabilities** | |
| Long term borrowings | - |
| **3. Current liabilities** | |
| Trade payables | 1,50,000 |
| **Total** | **6,00,000** |
| **II. ASSETS** | |
| **1. Non-current assets** | |
| (a) Fixed assets | 4,60,000 |
| (b) Non-current investments | 1,00,000 |
| **2. Current assets** | |
| Cash and cash equivalents | 40,000 |
| **Total** | **6,00,000** |

**Solution :**

$$\text{Proprietary ratio} = \frac{\text{Shareholder's funds}}{\text{Total assets}}$$

Shareholder's funds = Equity share capital + Preference share capital + Reserves and surplus

= ₹2,50,000 + ₹1,50,000 + ₹50,000 = ₹4,50,000

Total assets = ₹6,00,000

$$\therefore \text{Proprietary ratio} = \frac{4,50,000}{6,00,000} = 0.75:1$$

# UNIT 10 COMPUTERISED ACCOUNTING SYSTEM – TALLY

## I MULTIPLE CHOICE QUESTIONS

### CHOOSE THE CORRECT ANSWER

**1. Accounting report prepared according to the requirements of the user is**

(a) Routine accounting report
(b) Special purpose report
(c) Trial balance
(d) Balance sheet

[Ans. (b) Special purpose report]

**2. Function key F11 is used for**

(a) Company Features
(b) Accounting vouchers
(c) Company Configuration
(d) None of these

[Ans. (a) Company Features]

**3. Which submenu displays groups, ledgers and voucher types in Tally?**

(a) Inventory vouchers
(b) Accounting vouchers
(c) Company Info
(d) Account Info

[Ans. (d) Account Info]

**4. What are the predefined Ledger(s) in Tally?**

(i) Cash
(ii) Profit & Loss A/c
(iii) Capital A/c

(a) Only (i) (b) Only (ii)
(c) Both (i) and (ii) (d) Both (ii) and (iii)

[Ans. (c) Both (i) and (ii)]

**5. Contra voucher is used for**

(a) Master entry
(b) Withdrawal of cash from bank for office use
(c) Reports
(d) Credit purchase of assets

[Ans. (b) Withdrawal of cash from bank for office use]

**6. Which is not the default group in Tally?**

(a) Suspense account
(b) Outstanding expense
(c) Sales account
(d) Investments

[Ans. (b) Outstanding expense]

**7. Salary account comes under which of the following head?**

(a) Direct Incomes
(b) Direct Expenses
(c) Indirect Incomes
(d) Indirect Expenses

[Ans. (d) Indirect Expenses]

8. ₹25,000 withdrawn from bank for office use. In which voucher type, this transaction will be recorded

(a) Contra Voucher (b) Receipt Voucher
(c) Payment Voucher (d) Sales Voucher

[Ans. (a) Contra Voucher]

9. In which voucher type credit purchase of furniture is recorded in Tally

(a) Receipt voucher (b) Journal voucher
(c) Purchase voucher (d) Payment voucher

[Ans. (b) Journal voucher]

10. Which of the following options is used to view Trial Balance from Gateway of Tally?

(a) Gateway of Tally -> Reports -> Trial Balance
(b) Gateway of Tally -> Trial Balance
(c) Gateway of Tally -> Reports -> Display -> Trial Balance
(d) None of these

[Ans. (c) Gateway of Tally -> Reports -> Display -> Trial Balance]

## II VERY SHORT ANSWER QUESTIONS

1. What is automated accounting system?

Ans. (i) Automated accounting is an approach to maintain up-to-date accounting records with the aid of accounting software.

(ii) Under manual accounting system entries are made in different books of accounts while accounting software packages sallow manual entry in one field or one place.

2. What are accounting reports?

Ans. Accounting report is a compilation of accounting information that are derived from the accounting records of a business concern. Accounting reports may be classified as routine reports and special purpose reports.

3. State any five accounting reports.

Ans. Routine accounting reports include

(a) Day books / Journal
(b) Ledger
(c) Trial balance
(d) Income statement
(e) Balance sheet
(f) Cash flow statement

4. What is Accounting Information System (AIS)?

Ans. Accounting Information System (AIS) collects financial data, processes them and provides information to the various users. To provide information AIS requires data from other information system that is manufacturing, marketing and human resources.

5. What is a group in Tally.ERP 9?

Ans. In 2009, Tally Solutions introduced the software Tally.ERP 9. The software offers comprehensive business management solution. It maintains all books of accounts. Different types of vouchers such as vouchers for receipt, payment, sales, purchases, etc., can be used for recording transactions.

## III SHORT ANSWER QUESTIONS

1. Write a brief note on accounting vouchers.

Ans. This type of a voucher basically analyses a business transaction from the accounting stand point and is used for recording purposes

These are commonly prepared by accountants on the basis of supporting vouchers and approved by a different individual. They are further subdivided into two, Cash and Non-cash vouchers.

Examples of cash type :

1. Credit Vouchers
2. Debit Vouchers

Examples of the Non-cash type :

1. Debit note
2. Credit note
3. Invoice

2. What are the pre-defined ledgers available in Tally.ERP 9?

Ans. In Tally, to record transactions, the transactions are to be identified with the related ledger accounts. In Tally ERP 9, there are two types of pre. defined ledgers.

(i) Cash : Under the group cash-in-hand this ledger is created, you can enter the opening balance as on the books beginning from.

(ii) **Profit and loss account :** This ledger is created under the group primary. In this ledger previous year's profit or loss is entered as the opening balance of this ledger.

**To create ledger :**

Gateway of Tally →Masters >

Accounts Info > Ledgers >

Single Ledger > create

**3. Mention the commonly used voucher types in Tally. ERP 9.**

**Ans.** Following are some of the major accounting vouchers used in an organisation:

(i) Receipt Voucher

(ii) Payment Voucher

(iii) Contra Voucher

(iv) Purchase Voucher

(v) Sales Voucher

(vi) Journal Voucher

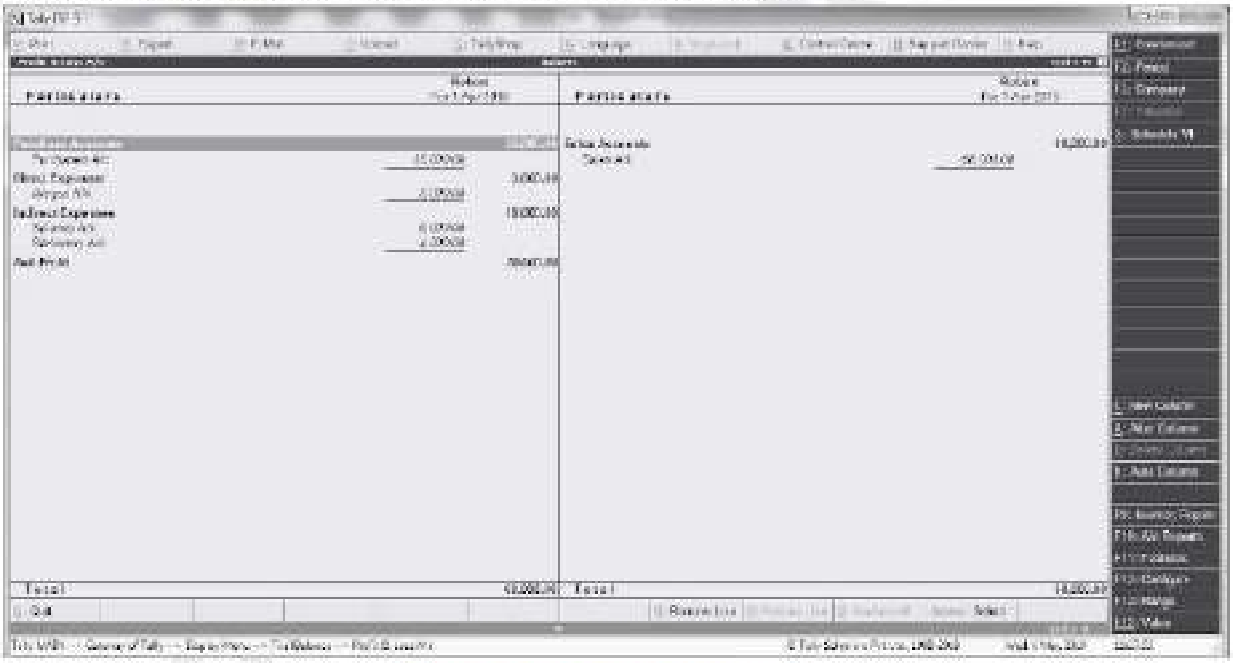
**4. Explain how to view profit and loss statement in Tally. ERP 9 ?**

**Ans.** To view Profit and Loss Account

F10: A/c Reports > Profit & Loss A/c > Alt F1 (detailed)

(or)

Gateway of Tally > Reports > Profit & Loss A/c > Alt F1 (detailed)



*Profit and Loss Account*

**5. Explain any five applications of computerised accounting system.**

**Ans.** **The applications of CAS are as follows :**

(i) **Maintaining accounting records :**

In CAS, accounting records can be maintained easily and efficiently for long time period. It facilitates fast and accurate retrieval of data and information.

(ii) **Inventory management :**

CAS facilitates efficient management of inventory. Updated information about availability of inventory, level of inventory, etc., can be obtained instantly.

(iii) **Report generation :**

CAS helps to generate various routine and special purpose reports.

(iv) **Data import/export :**

Accounting data and information can be imported from or exported to other users within the organisation as well as outside the organisation.

(v) **Taxation:**

CAS helps to compute various taxes and to deduct these and deposit the same to the Government account.

## IV Exercises

**1.** Record the following transactions in Tally.

(a) Devi commenced a business with a capital of ₹4,00,000
(b) An account was opened with Indian Bank and deposited ₹60,000
(c) Purchased furniture by paying cash ₹ 15,000
(d) Goods purchased on credit from Sumathy for ₹ 50,000
(e) Cash sales made for ₹10,000
(f) Goods purchased from Raja for ₹5,000 and paid by cheque
(g) Goods sold to Arun on credit for ₹70,000
(h) Money withdrawn from bank for office use ₹25,000
(i) Part payment of ₹ 30,000 made to Sumathy by cheque
(j) Arun made part payment of ₹ 10,000 by cash
(k) Salaries paid to staff through ECS ₹ 36,000
(l) Carriage on purchases of ₹ 6,000 paid by cash
(m) Purchased computer from Muthu Ltd. on credit ₹ 44,000.

***Solution :***

**Analysis of transactions, passing journal entries, identification of voucher**

| S.NO. | Particulars | | Debit ₹ | Credit ₹ | Voucher type | Group |
|---|---|---|---|---|---|---|
| (a) | Cash A/c | Dr. | 4,00,000 | | Receipt | Cash-in-Hand |
| | To Devi's Capital A/c | | | 4,00,000 | Voucher | Capital Account |
| (b) | Indian Bank A/c | Dr. | 60,000 | | Contra | Bank Accounts |
| | To Cash A/c | | | 60,000 | Voucher | Cash-in-Hand |
| (c) | Furniture A/c | Dr. | 15,000 | | Payment | Fixed Assets |
| | To Cash A/c | | | 15,000 | Voucher | Cash-in-Hand |
| (d) | Purchases A/c | Dr. | 50,000 | | Purchase | Purchase Accounts |
| | To Sumathy A/c | | | 50,000 | Voucher | Sundry Creditors |
| (e) | Cash A/c | Dr. | 10,000 | | Sales | Cash-in-Hand |
| | To Sales A/c | | | 10,000 | Voucher | Sales Accounts |
| (f) | Purchases A/c | Dr. | 5,000 | | Purchase | Purchase Accounts |
| | To Cash A/c | | | 5,000 | Voucher | Cash-in-Hand |
| (g) | Arun A/c | Dr. | 70,000 | | Sales | Sundry Debtors |
| | To Sales A/c | | | 70,000 | Voucher | Sales Accounts |
| (h) | Cash A/c | Dr. | 25,000 | | Contra | Cash-in-Hand |
| | To Bank A/c | | | 25,000 | Voucher | Bank Accounts |

| | | | | | |
|---|---|---|---|---|---|
| (i) | Sumathy A/c Dr.<br>To Bank A/c | 30,000 | <br>30,000 | Payment<br>Voucher | Sundry Creditors<br>Bank Accounts |
| (j) | Cash A/c Dr.<br>To Arun A/c | 10,000 | <br>10,000 | Receipt<br>Voucher | Cash-in-Hand<br>Sundry Debtors |
| (k) | Salaries A/c Dr.<br>To Bank A/c | 36,000 | <br>36,000 | Payment<br>Voucher | Indirect Expenses<br>Bank Accounts |
| (l) | Carriage A/c Dr.<br>To Cash A/c | 6,000 | <br>6,000 | Payment<br>Voucher | Direct Expenses<br>Cash-in-Hand |
| (m) | Computer A/c Dr.<br>To Muthu Ltd A/c | 44,000 | <br>44,000 | Journal<br>Voucher | Indirect Expenses<br>Sundry Creditors |

2. The following balance sheet has been prepared from the books of Pearl on 1-4-2018.

| Liabilities | ₹ | Assets | ₹ |
|---|---|---|---|
| Capital | 1,60,000 | Buildings | 40,000 |
| Sundry creditors: | | Furniture | 20,000 |
| Maya A/c | 20,000 | Stock | 10,000 |
| | | Sundry debtors | |
| | | Peter | 20,000 |
| | | Cash in hand | 30,000 |
| | | Cash at bank | 60,000 |
| | 1,80,000 | | 1,80,000 |

During the year the following transactions took place.

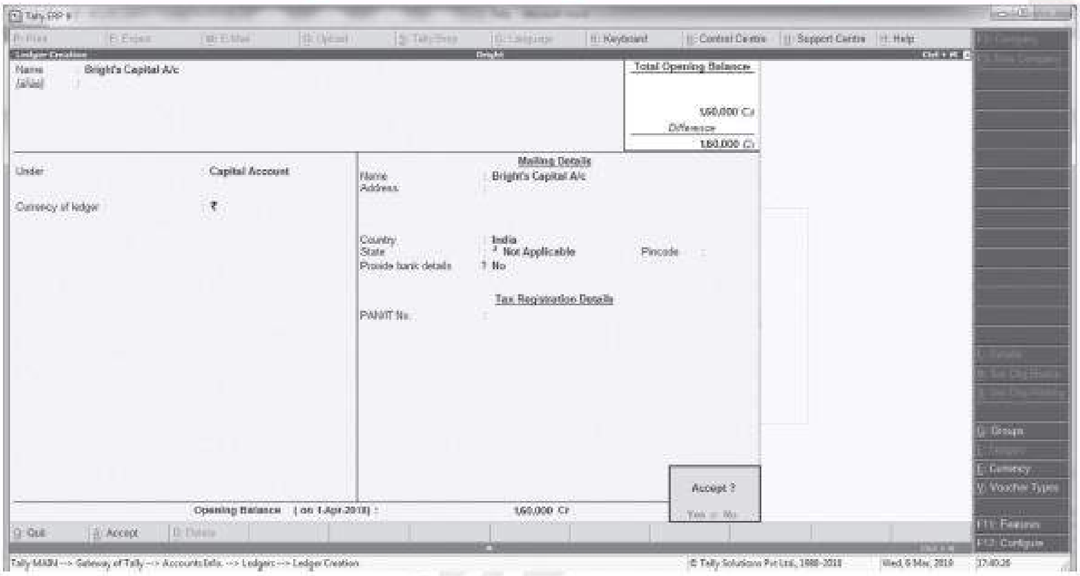
(a) Wages paid by cash ₹ 4,000
(b) Salaries paid by cheque ₹ 10,000
(c) Cash purchases made for ₹ 4,000
(d) Good purchased on credit from Yazhini ₹ 30,000
(e) Goods sold on credit to Jothi ₹ 40,000
(f) Payment made to Yazhini through NEFT ₹ 6,000
(g) Cash received from Peter ₹ 10,000
(h) Cash sales made for ₹ 4,000
(i) Depreciate buildings at 20%
(j) Closing stock on 31.03.2019 ₹ 9,000

You are required to prepare trading and profit and loss account for the year ended 31-03-2019 and a balance sheet as on that date using Tally.

**Solution :** Following steps are to be followed to enter the transactions in Tally ERP 9

1. To create company : Company Info > Create Company
   Type the Name as Peral and keep all other fields as they are and choose 'Yes' to accept.
2. To maintain accounts only :
   Gateway of Tally > F11 Accounting Features > General > Maintain accounts only: Yes > Accept Yes
3. To create ledger accounts with opening balances :
   Gateway of Tally > Masters > Accounts Info > Ledgers > Single Ledger > Create

| Creation of | Name | Under | Opening balance | Accept |
|---|---|---|---|---|
| Pearl's Capital A/c | Pearl's Capital A/c | Capital Account | 1,60,000 | Yes |
| Maya A/c (Sundry creditors) | Maya A/c | Sundry Creditors | 20,000 | Yes |
| Buildings A/c | Buildings A/c | Fixed Assets | 40,000 | Yes |
| Furnitures A/c | Furnitures A/c | Fixed Assets | 20,000 | Yes |
| Opening stock | Opening stock | Stock-in-Hand | 10,000 | Yes |
| Peter A/c (Sundry debtors) | Peter A/c | Sundry Debtors | 20,000 | Yes |
| Cash in hand | Cash | Cash-in-Hand | 30,000 | Yes |
| Cast at bank | Bank | Bank Accounts | 60,000 | Yes |




**CREATION OF PEARL CAPITAL A/C**

*NOTE :* Cash account need not be created as it is a default ledger. Only the opening balance has to be recorded by altering the cash account.

**To record the opening balance of cash :** Gateway of Tally > Masters > Accounts Info > Ledgers > Single Ledger > Alter