MAR GREGORIOS COLLEGE
OF ARTS & SCIENCE

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DEPARTMENT OF COMMERCE

(ACCOUNTING & FINANCE)

SUBJECT NAME: ADVANCED FINANCIAL ACCOUNTING

SEMESTER: II

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ADVANCED FINANCIAL ACCOUNTING
SYLLABUS

Unit I: Branch Accounts Dependent Branches - Stock and Debtors system – Distinction between Wholesale Profit and Retail Profit – Independent Branches (Foreign Branches excluded)

Unit II: Departmental Accounts Basis of Allocation of Expenses – Calculation of Profit - Inter-departmental Transfer at cost or Selling Price.

Unit III: Partnership Accounts Admission of a Partner – Retirement of a Partner – Death of a Partner.

Unit IV: Partnership Accounts Dissolution of a Partnership Firm – Insolvency of a Partner – Insolvency of all PartnersPiecemeal Distribution of cash in case of Liquidation of Partnership Firm.

Unit V: Accounting Standards for financial reporting Objectives and uses of financial statements for users-Role of accounting standardsDevelopment of accounting standards in India- Requirements of international accounting standards - Role of developing IFRS- IFRS adoption or convergence in India- Implementation plan in India- Ind AS-Difference between Ind AS and IFRS. Note: Questions in Sec. A, B & C shall be in the proportion of 20:80 between Theory and Problems.

TEXT BOOK:

1. Lt Bhupinder – principles of Financial Accounting – CENGAGE, New Delhi
2. Raj Kumar Sah –Concepts Building Approach to Financial Accounting - CENGAGE, New Delhi
3. Gupta, R. L & Gupta, V. K, Advanced Accounting, Sulthan Chand & Sons, New Delhi.
4. Jain &Narang, Financial Accounting, Kalyani Publishers, New Delhi. UNIVERS

UNIT- 1 BRANCHACCOUNTS

INTRODUCTION

Local demand for the products or services of a concern is easily met from its singleoffice. But as the area of its operation extends, it becomes increasingly difficult and costly topursue from the same office. Sooner or later, a section of the business is segregated from theexistingcentreofoperationandestablishedelsewhere.Everysuchsegregatedestablishmentiscalled'branch',asdistinguishedfrom theparentestablishment,termed 'headoffice'.

Branch merchandising or servicing activities: Section 2(9) of the Companies Act,1956, inter alia defines a branch office as "any establishment carrying on either the same orsubstantially the same activity as that carried on by the head office....or any establishmentengagedinanyproduction,processingormanufacture."Largeconcernsengagedinmerchandising,manufacturing,banking,insuranceandvariousotheroperationshavenumerous branches scattered at different places inside and outside the country of their origin.Accordingly, this chapter elaborates the fundamental accounting procedures applied to theoperationsof various branches.

DEPARTMENTSVs.BRANCHES

Althoughdepartments(seeLesson6.2)andbranchesaretheintrinsicdivisionsof theirrespective concern,yet theywidelydiffer asto thefollowing:

(1) Departmentsoperatealongwiththeirheadofficeinthesamepremisesbutbranchesare distantly segregated from each other as also their head office. This is why L.C. Croppercalls branches as 'departments conducted at a distance.' Thus, place or physical segregation isadistinguishingfeatureof branches.

(2) Because of (1), the head office is in constant touch with its departments. It closelysupervises and effectively controls their affairs. But in case of far off branches, it is well nighimpossiblefortheheadofficetoremaininconstanttouch.Itmayexerciseconsiderablecontrolovercloselylocated branches but onlyanominal control on overseas branches.

(3) Functionaldivisionisamustforthe existenceofdepartments.Notwodepartmentscan pursue the same line of trade. This is not so with branches. Usually they function on theline of multiple shops. Numerous offices of a commercial bank and retail shops of Bata ShoeCompany are the common examples of branch establishments. In some cases, they alsofunction diversely. For instance, branches of the Delhi Cloth and General

Mills Ltd. arevariously engaged in the manufactures of cotton textiles, sugar, chemicals, vegetable oils,engineeringproducts, business machines, etc.

TYPESOFBRANCHES

Branchesvaryaccordingtothenatureandmagnitudeofoperationspursuedasalsothedegree of autonomy enjoyed. Obviously, no single system of branch accounting would suiteach of the varied types of branches. Accordingly, numerous systems of branch accountinghavebeendevelopedandtheuseofanyonethereoflargelyrestswiththegiventypeofbranch.Studyof thebranch accountingis thus interlinked with thetypes of branches.

Branches may be variously classified. According to location, they are grouped intohome and foreign branches. Based on practical consideration (such as autonomy, variedcurrencies,etc.),theyare dividedintodependent, independentandforeignbranches.

As regards the work that is done by branches, there is no hard and fast rule. There arebranches, like the Bata Shops, that only do retailing. Others carry on wholesale business. Abranch may also be a full-fledged manufacturing unit. For example, the Delhi Cloth andGeneral Mills Ltd. has 'branches' at various places which manufacture sugar, cotton textiles,hydrogenated oils, fertilizers and chemicals, etc. These "branches", however, are so big thatthey are better termed as divisions; they enjoy a very large degree of autonomy and trade intheir own name. The same company also maintains a large number of retail shops. The parentorganisation-the Head Office-may itself be engaged in manufacturing and/or selling or it maybe only a controlling and co-ordinating agency. The accounting work that may be done at thebranches will depend on the decision made by the head office in this behalf; but generally,more the work entrusted to a branch, the more will be the accounting work that will be donebythe branch.Branchesareusuallydivided into five classes:

(a) A branch that receives goods only from the head office, sells only for cash andremits
all the cash collected to head office, the expenses of the branch being met byremittancesfrom the head office.

(b) A branch that receives goods only from the head office, sells both for cash andcredit
and remits all the cash collected to head office, the expenses of the

branch beingmetbyremittances from the head office.

(c) Same as above, but with the difference that goods are invoiced by the head officeto thebranchat sellingprice.

Intheabovethreecases,thebrancheswillnotdoanyaccountingworkexceptpreparingstatementsofstocksasregardsreceipt,saleandbalanceandcashstatements.Branchesthatareallowedto makecredit sales willalso maintain accounts of customers.

(d) "Independent" branches, i.e., those branches that are allowed to make purchasesthemselves, make sales both for cash and credit and carry on their work in an autonomousmanner.Suchbranchesusuallymaintaintheirownbooksofaccount.Theresultsofthebranchandthe head officeareintegrated at theend ofthefinancial period.

(e) Foreign branches: Such branches are also "independent" and have their own booksofaccount.

ACCOUNTSOFVARIOUSTYPESOFBRANCHES

(A) Branchsellingonlyforcash: Ashasbeenstated above,thebranchthatisallowedtosellonlyforcashisgenerallynotrequiredtomaintainaccountbooks.Thebranchwillmaintainapettycashbookacopyofwhichwillbeforwardedtotheheadoffice.Itwillalsoforwardto the head office, each week or each month, a stock statement. This statement will show,for each item, the opening stock, the stocks received during the period, sales during theperiod, breakage or losses during the month (for which head office sanction will berequired) and the closing stock. The stock statement will serve the purpose of controllingthestockatthebranchandthepurposeofguidingtheheadofficeastowhichstocksshouldbereplenished.Needless tosay, the statementmust besubmittedbyafixedday.

The column for total sale proceeds will enable the head office to check whether the totalcash realised has been remitted to the head office or not. In the remarks column, details ofbreakages,lossesorleakages(enteredinthecolumnforOtherIssues)togetherwithheadofficesanctiontowriteoffthe breakages, etc.,shouldbeentered.Thestatement shouldbesignedbythebranchmanagerandalsobythepersonin-chargeofthestocks.Itwouldbebettertopreparethis statement everyweek.

The head office finds out the profit or loss made at the branch by the simple method ofputtingononesidewhatissenttothebranch(goodsandcashforexpenses)andputtingon theother side the total cash received. Supposing there are no opening or closing stocks, if goodsworth Rs. 10,000 are sent to the branch and a sum of Rs.3,000 is incurred as expenses at thebranch and if the branch remits a sum of Rs.15,000, there is a net profit of Rs.2,000 at theBranch.The entries to bemadeat thehead officewillbeas follows:-

1. When goods are sent:Debitthe BranchAccount
   CreditGoodsSenttoBranchAccount
2. When Cash is sent to branch (for expenses):Debitthe Branch Account
   CreditCash
3. When Cash is received from the branch:DebitCash (or Bank)
   CreditBranchAccount.

If the branch has no stock left and no balance of cash, the Branch Account will revealprofitorlossmadeattheBranch. Butusually,thereisaclosingstockandaclosingbalanceofcash.Theentryto recordtheseat theend of theyear is:

Debit Stock at Branch Account;Debit Cash at Branch Account; andCreditBranch Account.

Profitorlossshouldbeascertainedaftermakingthisentry.Theprofitorlossshouldbetransferred to the General Profit and Loss Account. "Goods Sent to Branch Account" shouldbetransferredeithertothecreditoftheTradingAccountincaseofmanufacturingconcernsortothecreditofthePurchasesAccountincaseoftradingconcerns."StockatBranch"and"Cashat Branch" are assets and will appear in the balance sheet. Next year, in the beginning, boththeseaccounts will betransferred to thedebit of theBranch Account.

Tosummarize,theBranchAccountshouldbedebitedwith(1)theopeningbalancesofstock or cash; (2) the value of goods sent to the branch, and (3) the cash sent for expenses. Itshould be credited with cash received from the branch and the value of closing stock and cashinhand. Thedifferencein the two sides will beprofit or loss.

Illustration1: Branchsellingforcashonlyand invoicedat cost:

Pondicherry Papers Ltd. invoices goods to its Mahe Branch at cost. All the expensesare paid direct from the head office, except petty cash expenses which are paid by branchmanager. Branch is advised to sell for cash only, and deposit the day's sale proceeds in theHead Office Account with a local bank. From the following details, ascertain the profit of theMaheBranch through Debtors System.

	Rs.		Rs.
Stock(Jan. 1)	2,100	SalariesandWages	1,860
PettyCash (Jan. 1)	50	Advertisement	240
Furniture(Jan.1)	250	RentandRates	360
Goodssupplied from H.O.	7,800	Stock(Dec.31)	1,950
GoodsreturnedbacktoH.O	300	PettyCash (Dec. 31)	30
CashSales	15,250	Furniture(Dec.31)	230

SOLUTION: Books of Pondicherry Papers Ltd. (H.0.)MaheBranch Account

		Rs.	Rs.			Rs.	Rs.
Jan 1	ToBranchAssets:			Dec.31	ByReturn ofGoods to H.O.		300
	Stock	2,100			Bank(Saleproceeds)		15,250
	PettyCash	50			ByBranch Assets:		
	Furniture	250	2,400		Stock	1,950	
Dec.31	Goodssupplied to Branch		7,800		Furniture(1)	230	
	Cash:				PettyCash (2)	30	2,210
	Salaries&Wages	1,860					
	RentandRates	360					
	Advertisement	240	2,460				
	Profittransferredto Profit&LossA/c		5,100				
			17,760				17,760

(A) Branchsellingbothforcashandcredit:Inthiscasealso,themainaccountingworkisdoneat the head office. The branch will keep a petty cash book and prepare, periodically, the stockstatement to be sent to the head office. It will also have to keep accounts of credit customerssothatthecustomerscanberemindedaboutthebalancesduefromthem.Thehead officewillkeepaccountsofthebranchmuchinthesamewayinwhichintheaccountsofthefir sttypeofbrancharekept. Theonlyexception is thatthefollowingadditional entrieswill bemade:

1. To transfer the branch debtors in the beginning of the year:BranchAccount . .. Dr.
   ToBranchDebtors
2. To record the branch debtors at the end of the yearBranchDebtors .. . Dr.
   ToBranchAccount

TheBranchprofitorlosswillbeascertainedonlyaftertheaboveentriesaremade.The"BranchDebtors,"like "Branch Stock,"areassetsandwillbeshownintheBalanceSheet.

*Note:*Noentryismadeforcreditsalesatbranchintheheadofficebooks.Cashreceivedfromthedebtorswillberemittedtotheheadofficealongwithcashreceivedforcashsales.Theheadoffice will make entry only for cash received by it. It will debit cash and credit the branch. Bythe same token, the head office makes no entry for discounts allowed, bad debts written off orreturns by the branch debtors. If the branch has received a bill of exchange, it will be sent tothe head office. The entry then will be to debit Bills Receivable Account and credit BranchAccount.

Illustration 2: Messrs VST & Sons are having their Head Office at Pondicherry and Branchat Madras. The following are the transactions of the Head Office with Branch for the yearended31st August. ,1995.

StockatBranch ason1.9.94	30,800	
Debtorsatthe Branchason1.9.94	16,500	
PettyCash as on 1.9.94	500	
GoodssuppliedtotheBranch	1,51,200	
RemittancesfromBranch:		
CashSales	10,500	
RealizationofDebtors	1,57,740	1,68,240
AmountsenttoBranch:S		
alary	7,440	

Rent	2,400	
PettyCash	3,000	12,840
StockatBranch ason31.8.95		23,150

SundryDebtors attheBranchas on31.8.95 50,460

PettyCash as on 31.8.9 750

ShowtheBranch Accountin thebooks ofthe HeadOffice.

Solution

VST&SONSMadrasBranchAccount

		Rs.	Rs.			Rs.	Rs.
1994	ToBalanceb/d:			1994	ByBank/Cash :		
Sep.1	Stock at	30,800		Sep.1	Cash	10,500	
	BranchBranch	16,500		1995	SalesDebt	1,57,740	1,68,240
	DebtorsCash	500	1,51,200	Aug.3	ors		
	To Goods sent			1	By Balance c/d	23,150	
	toBranchA/c				:StockatBranch	50,460	
	ToBank				Branch	750	74,360
	(Remittances)				DebtorsCashat		
	Salary	7,440			Branch		
	Rent	2,440					
	Petty	3,000	12,840				
	CashToP &		30,760				
	LA/c						
			2,42,600				2,42,600

Illustration3:

FromthefollowingparticularsrelatingtoMaduraibranchfortheyearendingDecember31,1991 prepareBranch Account in the booksofHead Office:

Stockat branch onJanuary1, 1991		10,000
Branchdebtors onJanuary1,1991		4,000
BranchDebtorsonDec.31,1991		4,900
PettyCash at branch onJanuary1, 1991		500
Furnitureat branch on January1, 1991		2,000
Pre-paid fireinsuranceon January1, 1991		150
Salariesoutstanding atbranch on January1, 1991		100
GoodssenttoBranchduringtheyear		80,000
Cashsalesduringtheyear		1,30,000
CreditSalesduringtheyear		40,000
Cashreceivedfromdebtors		35,000
CashpaidbythebranchdebtorsdirecttoHead Office		2,000
Discountallowed to debtors		100
Cashsent tobranch forexpenses:		
Rent	2,000	
Salaries	2,400	
PettyCash	1,000	
Insuranceupto March 31, 1992	600	6,000
Goods returned bythebranch		1,000
Goods returnedbythe debtors		2,000
StockonDecember31		5,000
Pettyexpensesbythebranch		850
Providedepreciationon furniture10%p.a		

GoodscostingRs.1,200weredestroyedonaccountoffireandasumofRs.1,000wasreceivedfrom theInsuranceCompany.

Solution

MaduraiBranchAccount

	Rs.	Rs.		Rs.	Rs.
ToOpeningBalances:			ByOpeningBalances:		
Stock		10,000	SalariesOutstanding100		
Debtors		4,000	ByRemittances:		
PettyCash		500	Cashsales	1,30,000	
Furniture		2,000	Cashreceivedfrom debtors	35,000	
PrepaidInsurance		150	ByCashpaidbydebtors directtoH.O.	2,000	
ToGoodssenttobranch		80,000	ByReceived from InsuranceCompany	1,000	1,68,000
ToBank (expenses):			ByGoods sent to branch		
Rent	2,000		(return of goods bythe		
Salaries	2,400		branchtoH.O.)		1,000
PettyCash	1,000		ByClosingBalances:		
Insurance	600	6,000	Stock		5,000
ToNetProfit		78,950	PettyCash		650
			Debtors		4,900
			Furniture		1,800
			PrepaidInsurance (1/4 •Rs. 600)		150
		1,81,600			**1,81,600**

- Alternativelytheamountofliabilitiescould havebeendeducted from assets.

WorkingNote:

Calculationofpettycashbalance attheend:

Openingbalance	Rs.	500
Add:Cashrecd.fromthe Head	Office	1,000
TotalCashwithbranch		1,500
Less:Spent bythe branch		850
ClosingBalance	Rs.	650

(B) Goodsinvoicedatsellingpriceorinflatedprice: Somefirmschooseto"invoice"goodsto its branches at selling price. This presupposes that there will be a fixed selling price. Thepurpose of making out the invoice at selling price is to control stocks at the branch easily. Weshall see how this is done later. But at the moment we must remember that to ascertain profitwe must compare the sale proceeds only with the cost. If the Branch Account is debited withmorethanthecost, thedifferencemustbecreditedtothe Branch.Stockattheendwillalsobevalued according to the "invoiced" value. This will be more than the cost. The differencebetween the cost of the stock and its "invoiced" or loaded price must be put right. The BranchAccount is debited and Stock Reserve

Account is credited with the difference. Both BranchStock Account and Stock Reserve Account are carried forward to the next year and thentransferredto theBranchAccount.

Torecapitulate,the entriestobemadeare:

(a) When goodsaresenttothebranch
DebitBranchAccount(attheinvoicedfigure)
CreditGoodssenttoBranchAccount

(b) Whencashissenttothebranchforexpenses
DebitBranch Account and
CreditCashAccount.

(c) When cash is received from the branch-DebitCash Account and CreditBranchAccount.

(d) for amount of debtors at the end at the branch-DebitBranch Debtors Accountand CreditBranchAccount.

(e) forvalue ofstock at thebranch-
DebitBranchStockAccount(accordingtotheinvoicedprice)
CreditBranchAccount

(f) toremove theloading(orinflation) from gonds sentto thebranch-
DebitGoodsSenttoBranch Account(withtheamount addedtothecost)
CreditBranchAccount

(g) to "correct" the amount of the stock-DebitBranch Account and
CreditStockReserveAccount.

TheBranchAccountwillnowrevealprofitandlosswhichistransferredtotheProfitandLossAccount. The balance in the Goods sent to Branch Account is transferred to the TradingAccountor Purchases Account.

Illustration4: Dinesh&Co.Ltd.openedin1993abranchatGoa.ItinvoicedgoodstotheBranchat cost plus25%.Information about 1993and 1994 isgiven below:

	1993 Rs.	1994 Rs.
GoodssenttotheBranch (invoiceprice)	50,000	80,000
CashsenttotheBranchforexpenses	8,000	10,000
Sales-		
Cash	22,000	33,000
Credit	23,000	48,000
Cashreceivedfromdebtors	20,000	47,000
BadDebtswrittenoff	600	400
Stockon31stDecember(invoiceprice)	4,800	4,000

Journalise the entries to be made in the Head Office for 1993 and give ledgeraccountsforboth theyears.

Solution

Journal

1993	GoaBranchAccount Dr.	50,000	
	ToGoods sentto Branch A/c [Goodssent tothe GoaBranch(invoicevalue)]		50,000
	GoaBranchAccount Dr. ToCashAccount (CashremittedtotheBranchforexpenses)	50,000	50,000
	CashAccount. Dr. To Goa Branch Account(Cashreceivedfromthe Branch CashSales22,000fromDebtors20,000)	42,000	42,000
Dec.31	BranchDebtorsAccount Dr. ToGoaBranch Account [Thebalancesdue from BranchDebtors Rs.23,000 -(Rs. 20,000 plus Rs. 600)]	2,400	2,400
	BranchStockAccount Dr. ToGoaBranch Account (Invoicevalueof thestocklyingatthe Branch)	4,800	4,800
	GoodssenttoBranchAccount Dr. ToGoaBranch Account (Loading in the goods sent to Branch creditedtoGoaBranchA/c50,000*25/125=10,000)	10,000	10,000

BranchandDepartmentalAccounts

1993 Dec.31	GoaBranchAccount Dr. ToStock ReserveAccount (Reserveagainststockcreatedequaltotheloadingin theClosingStock)	960	960
	GoodssenttoBranchAccount Dr. ToTradingAccount (ThebalanceintheformeraccounttransferredtotheTradingAccount)	40,000	40,000
	GoaBranchAccount Dr. ToProfitand LossAccount (ProfitatGoa BranchtransferredtotheProfitandLossAccount)	240	240

GoaBranchAccount

1993		Rs.	1993		Rs.
Dec.31	To Goods Sent toBranchA/c To Cash – ExpensesToStockReserveA/cloading ToProfit&Loss	50,000 8,000 960 240	Dec.31	ByCash A/c ByBranchDebtorsA/cByBranch Stock A/c ByGoodssenttoBranchA/c-loading	42,000 2,400 4,800 10,000
		59,200			**59,200**

GoodsSenttoBranchAccount

1993		Rs.	1993		Rs.
Dec. 31	ToGoaBranch A/c loading	10,000	Dec.31	ByGoaBranch A/c	50,000
	ToTradingA/c-transfer	40,000			
		50,000			**50,000**

GoaBranchDebtors Account

1993		Rs.	1993		Rs.
Dec. 31	ToGoaBranchA/c	2,400	Dec.31	ByBalancec/d	2,400
1994			1994		
Jan. 1	ToBalanceb/d	2,400	Jan. 1	ByGoa Branch A/cTransfer	2,400

GoaStockAccount

1993		Rs.	1993		Rs.
Dec. 31	ToGoaBranchA/c	4,800	Dec.31	ByBalancec/d	4,800
1994			1994		
Jan. 1	ToBalanceb/d	4,800	Jan. 1	ByGoa Branch A/c-Transfer	4,800

StockReserveAccount

1993 Dec.31		Rs.	1993 Dec.31		Rs.
	ToBalance c/d	960		ByGoa Branch A/c	960
				Transfer	
1994			1994		
Jan. 1	ToGoaBranchA/c	960	Jan. 1		
	Transfer			ByBalanceb/d	960

GoaBranchAccount

1993		Rs.	1993		Rs.
Dec.31	ToOpeningBalances:		Dec.31	ByCash A/c	80,000
	Stock	4,800		ByBranch Debtors A/c	3,000
	Debtors	2,400		ByBranch Stock A/c	4,000
	ToGoodssenttoBranchA/c	80,000		ByStockReserve A/c (onopeningstock)	960

Dec.31	ToCash-expenses	10,000		ByGoods sent to BranchA/c(loading)	16,000
	ToStock–ReservesA/c (on closingstock)	800			
	ToProfit&LossA/c Profittransferred*	5,960			
		1,03,960			1,03,960

*The student should note that if there is opening stock at inflated price, there will be a stockreserveA/cshowingacredit balanceequal totheloading.

GoodsSenttoBranchAccount

Dr. Cr.

1993		Rs	1993		Rs.
Dec.31	ToGoaBranch A/cloading	16,000	Dec.31	ByGoa Branch A/c	80.000
	ToTradingA/ctransfer	64,000			
		80,000			80,000

BranchDebtorsAccount

		Rs.			Rs.
1993 Dec.31	ToGoaBranchA/c	3,000	1993 Dec.31	ByBalancec/d	3,000
1995 Jan. 1	ToBalanceb/d	3,000			

BranchStockAccount

		Rs.			Rs.
1993 Dec.31	ToGoaBranchA/c	4,000	1993 Dec.31	ByBalancec/d	4,000
1995 Jan. 1	ToBalanceb/d	4,000			

StockReserveAccount

		Rs.			Rs.
1994 Dec.31	ToBalance c/d	800	1993 Dec.31	ByGoa Branch A/c	800
				ByBalancec/d	800

Illustration 5: X & Co. of Delhi has a branch at Madras. ‘Goods are sent by the Head Officeatinvoicepricewhichisattheprofitof25%oncostprice.Allexpensesofthebrancharepaid bytheHeadOffice.Fromthefollowingparticulars,preparebranchaccountintheHeadOfficebooks:(a)whengoodsareshownatcostprice,and(b)whengoodsareshownatinvoiceprice.

	Rs.
OpeningBalance:	
Stockat invoiceprice	11,000
Debtors	1,700
PettyCash	100
Goodssent tobranch atinvoiceprice	20,000
Expensesmadebyheadoffice:	
Rent	600
Wages	200
Salary,etc.	900

RemittancesmadetoHeadOffice:	
Cashsales	2,650
CashcollectedfromDebtors	21,000
GoodsReturned byBranch at invoiceprice	400
Balanceattheend:	
Stockatinvoiceprice	13,000
Debtorsattheend	2,000
PettyCash	25

Solution

(a) WhengoodsareshownatcostpriceMadrasBranchAccount

ToOpeningBalance		ByCash:	
Stock		CashSales 2,650	
(Rs.11,000-2.200)	8,800	Cashcollectedfrom	
Debtors	1,700	Debtors 21,000	23,650
PettyCash	100	ByGoods sent toBranchA/c(at cost)	320
ToGoodssenttoBranchA/c(at cost)	16,000		
ToBankExpenses		ByClosingBalances:	
Rent 600		Stock(atcost)	10,400
Wages 200		Debtors	2,000
Salaries 900	1,700	PettyCash	25
ToNetProfittransferredto GeneralProfit&LossA/c	8,905		
	36,395		36,395

(b) Whengoodsareshownatinvoicepri ceMadrasBranch Account.

ToOpening BalanceStock DebtorsPe ttyCash To Goods sent to Branch A/cToBank Rent 600 Wages 200 Salaries 900 To Stock Reserve (Loading onclosingstock) To Net Profit transferred toGeneralProfit&LossA/c	 11,000 1,700 100 20,000 1,700 2,600 8,905	ByCash: CashSales CashcollectedfromDebtors By Goods sent to Branch A/c (returned)ByGoodssenttoBranch A/c(loadingonnetgoods sent) ByStockReserve(loadinginOp.stock)By ClosingBalances: Stock (at cost)13,000Debtors 2,000 PettyCash 25	2,650 21,000 400 3,920 2,200 15,025
	45,195		45,195

AscertainmentofBranchStockandBranchDebtors

In case in an examination question, the balance (opening or closing) of the BranchStock or Branch Debtors Account is not given, the students should prepare a MemorandumBranch Stock Account or a Memorandum Branch Debtors Account. The accounts will bepreparedas follows:

MemorandumBranchStockAccount

ToBalanceb/d	BySales:
ToGoodsreceivedfrom H.O.	Cash Sales
	Credit Sales
ToGoodsreturnedbyBranchDebtors	
	ByGoodsreturnedtoHeadOff
iceToSurplus ofStock	ByShortageof Stock
	ByBalancec/d

It should be noted that the Branch Stock Account should be prepared either at cost orat invoice price. In case some of the items have been given at invoice price and the others atcostprice,theyshould be suitablydecreased orincreasedto bringallitemsatauniform price.In case goods have been sent to the branch at invoice price, it will be better to prepare theBranchStock Account atinvoiceprice.

MemorandumBranchDebtorsAccount

ToBalanceb/d	ByCash received
ToCreditSales	ByBills receivablereceived
ToBillsreceivable	
	ByBad
debtsdishonoured	
	ByDisc
ount	
	BySalesre
	turnsByB
	alancec/d

The Memorandum Branch Debtors Account as shown above is prepared on the same patternonwhich aTotal Debtors Account isprepared under Single EntrySystem.

Illustration 6: Vasan of Madras has a branch at Calcutta. Goods are invoiced from the HeadOffice at cost plus 33.5%. Branch is allowed to make sales at invoice price only. Expenses ofthe Branch except pettyexpenses arepaid directlybythe Head Office.

Fromthefollowingparticulars,youarerequired topreparethenecessaryaccounts toascertainthenet profitatthebranchaccordingtotheDebtors System.

Debtorson1.1.1981		10,000
PettyCash on 1.1.1981with theBranch		1,000
Stockon1.1.1981 (atinvoiceprice)		8,000
Goodsinvoiced bythe Head Office		88,000
Furnitureon1.1,1981		2,000
Cash sent byHead Officeforpettyexpenses at the Branch		2,000
Sales:Cash	50,000	
Credit	36,000	
		86,000
SalesReturnsbyBranchDebtors		800
Goodsdamagedatinvoiceprice		1,000(amountrecovered from
theinsurancecompanyRs.500)		
GoodsreturnedbyBranchtoHead Office		2,000
CashremittedbyBranchtoHeadOffice		

70,500BranchExpenses:

Freightandcartage	500
Rent	1,000
Salary	3,900
Baddebts	50
Depreciationonfurniture	80
Advertisementforthe branch	200
Pettyexpenses	1,500

Solution

BranchAccount

ToOpeningBalances	Rs.			
PettyCash	1,000	ByRemittances:		
Debtors	10,000	CashSales	50,000	
Stock	8,000	RecoveryfromInsuranceCo.	500	
Furniture	2,000	CollectionsfromDebtors	20,000	70,500
ToGoodssenttoBranch	88,000	ByGoods sentto Branch(returns)		2,000
ToBank (expenses)	5,600	ByStock Reserve(loading)		2,000
ToBank(for pettyexpenses)	2,000	ByGoods sent toBranch(loading)		21,500
ToStockReserve(Loading)	1,950	ByClosingBalances:		
ToNetProfit	13,820	Stock		7,800
		Debtors		25,150
		PettyCash		1,500
		Furniture		1,920
	1,32,370			1,32,370

GoodssenttoBranchAccount

To.Branch Account(Returns)	2,000	ByBranch A/c	88,000
ToBranchAccount (LoadingonRs.86,000)	21,500		
ToTradingAccount(Cost ofgoods sentto branch)	64,500		
	88,000		88,000

WorkingNotes:

(i) MemorandumBranchPettyCashAccount

ToBalanceb/d	1,000	ByPettyExpenses	1,500
ToCashfromHeadOffice	2,000	ByBalance	1,500
	3,000		3,000

(ii) MemorandumBranchStockAccount

ToBalanceb/d	8,000	BySales	
ToGoodssenttoBranch	88,000	Cash50,000	
ToSalesReturns	800	Credit36,000	86,000
		ByGoods returned byBranch	2,000
		ByGoods damaged	1,000
		ByBalancec/d	7,800
	96,800		96,800

(i) MemorandumBranchDebtorsAccount

ToBalanceb/d	10,000	BySales Returns	800
ToCreditSales	36,000	ByCash	20,000
		ByBad Debts	50
		ByBalancec/d	25,150
	46,000		46,000

StockandDebtorssystem

Incaseofthissystem,theHeadOfficemaintainsanumberofaccountsforkeepingarecordofBranch transactions in place of one branch account. A brief description of each of theseaccountsisgiven below:

(i) Branch Stock Account : This account is on the pattern of a goods account. The accounthelps the Head Office in maintaining an effective control over the Branch Stock. It tells aboutshortageor surplus of stock and the closingstock at theBranch.

(ii) Branch Debtors Account : The account is maintained to keep a record of all transactionsrelatingto Branchandascertainmentofthebalanceofthedebtorsattheendoftheaccountingperiod.

(iii) Branch Fixed Assets Account : A separate account for each of the Branch Fixed assetsismaintained to record all transactions relatingtoeach of thesefixed assets.

(iv) Branch Cash Account : The account is maintained to record all cash transactions of theBranch. This is particularly helpful in those cases where the Branch is not required to sendimmediately all collections of cash made by it but to remit money at regular intervals. Theaccounthelps theHeadOfficein having acontrol overBranch Cash.

(v) BranchExpensesAccount: TheaccountispreparedtogivetotheHeadOfficeasummarypicture ofdifferentexpenses, baddebts anddiscounts etc. incurredat the Branch.

(vi) BranchAdjustmentAccount: Theaccountismaintainedforascertainingthegrossprofitmade at the Branch. All loadings in the goods sent to the branch, opening and closing stocksatthebranchandshortageand surplus ofstocketc., arerecordedin this account.

Branch Profit and Loss Account : The account is prepared to ascertain profit or loss madeattheBranch.ThegrossprofitorlossfromtheBranchAdjustmentAccountis transferred to this account. It is debited with all other expenses and losses and credited with all gains andprofits.Thebalanceof theaccount representsthenet profit or loss.

(vii) Goods sent to the Branch Account : The account is prepared to ascertain the net valueof goods sent to the Branch. Goods sent to the Branch and goods returned by the Branch andloadingincluded in themarerecorded in this account.

JournalEntries

ThefollowingJournalentriesarepassedinthebooksoftheHeadOfficeincasethetransactionsarerecorded accordingtothe Stock and Debtors System:

(i) For goods sent to the Branch (at invoice price)BranchStock Account Dr.
ToGoodssentto theBranchAccount

(ii) ForgoodsreturnedbytheBranchtotheHead Office (atinvoiceprice)Goodssent to the Branch Account Dr.
ToBranch StockAccount

(iii) For Credit Sales at the Branch (at invoice price)BranchDebtorsAccount Dr.
ToBranch StockAccount

(iv) For Cash Sales at the Branch (at invoice price)CashAccount Dr.
ToBranch StockAccount

(v) For goods returned by Branch Debtors to the Branch(atinvoiceprice)
BranchStockAccountDr.
ToBranch DebtorsAccount

(vi) For goods'returned byBranch'DebtorsdirectlytotheHeadOffice (at invoiceprice)
Goodssent tothe BranchAccount Dr.
ToBranchDebtorsAccount

(vii) ForGoods sent byoneBranch to Another.

It will be recorded as if the Branch .has first returned the .goods to the Head Office, and thenthe Head Office has sent goods to another Branch. For example, if. Branch X sends goods toBranch.-thefollowing entries will bepassed:

(a) GoodssenttoX BranchAccount Dr.
ToXBranchStockAccount

(b) Y BranchStockAccount Dr.
ToGoodssentto Y.BranchAccount

(viii) ForBadDebts,Discountetc.
BranchExpenses Account Dr.
ToBranchDebtorsAccount

(ix) ForExpensesatBranch
BranchExpensesAccount Dr.
ToBankAccount

(x) ForAbnormalShortage (orpilferageorloss)ofStock
BranchAdjustmentAccount Dr.
(withthe amount ofloading)
BranchProfit&LossAccount Dr.
(withshortageat cost)
ToBranch StockAccount
(withtheshortageatinvoiceprice)

For surplus at Branch, a reverse entry will be passed.

No entry is required for normal loss of stock. The Branch Stock balance will be shown at the net amount as found by physical verification.

Any amount received from the Insurance Company for abnormal loss of stock (if insured), will be debited to Branch Cash Account and Credited to Profit & Loss Account.

(i) For transfer of Branch Expenses
Branch Profit & Loss Account Dr.
To Branch Expensed Account

(ii) For adjustment of loading in the Opening Stock
Stock Reserve Account Dr.
To Branch Adjustment Account

(iii) For adjustment of loading in Closing Stock
Branch Adjustment Account Dr.
To Stock Reserve Account

(iv) For adjustment of loading in Net Goods sent to the Branch Account (i.e., goods sent less goods returned by branch)
Goods sent to the Branch Account Dr.
To Branch Adjustment Account

(v) For transfer of the balance in goods sent to the Branch Account
Goods sent to Branch Account Dr.
To Purchases/Trading Account

(vi) For transfer of Gross Profit shown by the Branch Adjustment Account
Branch Adjustment Account Dr.
To Branch Profit & Loss Account

In case of gross loss, the entry will be reversed.

(vii) For transfer of Net Profit at the Branch
Branch Profit & Loss Account Dr.
To General Profit & Loss Account

In case of net loss, the entry will be reversed.

Illustration 7: Kalyani Bros. have two retail sales branches selling goods supplied to them by the firm's central warehouse. All such supplies of goods are charged at the fixed selling price of cost plus 50 per cent.

Sales are mainly for cash but in approved cases limited credit sales are authorised. The whole book-keeping work is centralised at the Head Office.

From the following particulars in respect of the transactions of the branch at Lowhill, Delhi, for the period of 3 months ending on 31st March, 1982, you are required to record them in the Journal and Ledger accounts in the Head Office Books showing clearly how any balances thereon are dealt with (i.e., prepare Branch Stock Account, Branch Debtors Account, Branch Adjustment Account, Branch Profit and Loss Account and Goods sent to Branch Account).

	Rs.
Stock (at selling price) January 1, 1982	26,700

Debtors, January1, 1982	1,400
Cashsales	72,940
CashremittedtoHead Officebycustomers	2,800
GoodsReturned: byBranch to Head Office	1,170
bycredit customersto Branch	570
bycreditcustomerstoHeadOffice	120
GoodstransferredbytheBranchtoLowHillBranch	4,500
Goodsissuedto BranchbyHeadOffice (atsellingprice)	78,300
Baddebtswrittenoff	150
CashremittedtoHead Officebythe Branch	72,000

The amount due by credit customers on March 31, 1982 was Rs.960. Head Office toGoods(atasalesvalueofRs.660)lostintransitfromtheBranch,theactualstockonthatdatewas in agreement with the figures. A claim was made on the insurance company in respect ofthelost stock and asum of Rs.500 was accepted in fullsettlement.

Solution **JournalEntries**

Particulars	**Dr. Rs.**	**Cr. Rs.**
BranchCashA/c Dr. To Branch Stock A/c(CashSales atBranch)	72,940	72,940
CashA/c Dr. To Branch Debtors A/c(CashremittedbyBranchDebtors)	2,800	2,800
GoodssenttoBranch Account Dr. ToBranchStockAccount(Goodsreturned byBranch)	1,170	1,170
BranchStockAccount Dr. ToBranchDebtorsAccount (GoodsreturnedbyBranchDebtors toBranch)	570	570
GoodssenttoBranchAccount Dr. ToBranchDebtorsAccount (GoodsreturnedbyBranchDebtors toHead Office)	120	120
GoodssenttoBranchAccount Dr. ToBranchStockAccount(GoodstransferredtoLowHill)	4,500	4,500
BranchStockAccount Dr. ToGoodssenttoBranchAccount(Goodssent to Branch)	78,300	78,300
BranchProfit&LossAccount Dr.	150	
To Branch Debtors Account (Bad debts at Branch)		150

Branch Adjustment Account Dr. Branch Profit & Loss Account Dr. To Branch Stock Account (Loss at stock)	220 440	660
Branch Cash Account Dr. To Branch Profit & Loss Account (for recovery of money from Insurance (Company)	500	500
Branch Debtors Account Dr. To Branch Stock Account (For Credit Sales)	3,200	3,200
Goods sent to Branch Account Dr. To Branch adjustment account (Loading in goods sent to Branch net)	24,170	24,170
Goods sent to Branch Account Dr. To Purchases Account (For transfer of cost of goods sent to Branch)	48,340	48,340
Branch Adjustment Account Dr. To Stock Reserve (For loading in closing stock)	7,700	7,700
Stock Reserve Account Dr. To Branch Adjustment Account (For loading in opening stock)	8,900	8,900
Branch Adjustment Account Dr. To Branch Profit & Loss Account (For transfer of Gross Profit)	25,150	25,150
Branch Profit & Loss Account Dr. To General Profit & Loss Account (Transfer of Branch Profit)	25,060	25,060
Cash Account Dr. To Branch Cash Account (Remittance received from the Branch)	72,000	72,000

Notes:

1. Alternatively, the amount may be debited to Branch. Expenses Account which may later on be transferred to Profit & Loss Account
2. Alternatively, the amount may be transferred to Head Office Trading Account.

LEDGER ACCOUNTS

Branch Stock Account

	Rs.		Rs.
To Balance b/d	26,700	By Cash (Sales)	72,940
To Goods sent to Branch A/c	78,300	By Branch Debtors (credit sales)	3.200
To Branch Debtors	570	By Goods sent to Branch A/c (returns)	1,170
		By Goods sent to Branch A/c (transferred to Low Hill branch)	4,500
		By Branch Adj. A/c	220

		ByBranch P & LA/c(Loss in transit)	440
		ByBalance(Balancingfigure)	23,100
	1,05,570		1,05,570

BranchDebtorsAccount

	Rs.		Rs.
ToBalanceb/d	1,400	ByCash received	2,800
ToBranchStockA/c(creditsales) (Bal.fig.)	3,200	ByBranch StockA/c (returns) 570	570
		ByGoods sent to BranchA/c (directreturnstoH.0.)	120
		ByBranch P & L(bad debts) 150	150
		ByBalancec/d 960	960
	4,600		4,600

GoodsSenttoBranchAccount

	Rs.		Rs.
ToBranchStockA/c(returns)	1,170	ByBranch Stock A/c	78,300
ToBranchStockA/c	4,500		
ToBranchDebtorsA/c	120		
ToBranch Adj.A/c(loading1/3of Rs.72,510)	24,170		
ToPurchaseA/c(transfer)	48,340		
	78,300		78,300

BranchAdjustmentAccount

	Rs.		Rs.
ToStock Reserve(ClosingStock)	7,700	ByStock Reserve(openingstock)	8,900
ToBranchStockA/c(loadingin lossintransit)	220	Goodssent to BranchA/c(1/3 of 72,510)	24,170
ToGrossProfittakentoBranch P& LA/c	25,150		
	33,070		33,070

BranchP&LAccount

	Rs.		Rs.
ToBranchDebtors A/c(baddebts)	150	ByGross Profit	25,150
ToBranchStockA/c(lossin transit)	440	ByCash (Insuranceclaim)	500
ToNetProfittakento GeneralP &L A/c	25,060		
	25,650		25,650

BranchCashAccount

	Rs.		Rs.
ToBranch StockAccount	72,940	ByCash Account	72,000
ToBranchProfit& LossA/c	550	ByBalancec/d	1,490

	73,490		73,490

CashAccount(HeadOffice)

	Rs.		**Rs.**
ToBranch DebtorsAccount	2,800	ByBalancec/d	74,800
ToBranchCashAccount	72,000		
	74,800		74,800

Illustration8:ShriXhasaretailbranchatAllahabad.GoodsaresentbytheH.O.totheBranchmarkedat sellingpricewhich iscost plus25%. All theexpenses oftheBranch arepaid bythe H.O.AllcashcollectedbytheBranch(fromcustomersandfromcashsales)isdepositedtothecreditof H.O.

From the following particulars of the Branch, prepare Branch Stock Account, BranchDebtors Account, Branch Expenses Account and Branch Adjustment Account in the books oftheHead Office.

Debtorson1.1.1980	12,000
Debtorson31.12.1980	14,000
Inventorywith theBranch at invoice	
Priceon 1.1.1980	16,000
On31.12.1980	17,000
CashSalesduringtheyear	60,000
Totalamount deposited intheH.O	
Accountduringtheyear	1,27,000
Returnof goodstoH.O.atinvoiceprice	5,000
Salariespaid	6,000
Rent paid	4,000
Discount allowed to customers	2,000
Bad Debts written off	1,000
Spoilage	2,000

Solution

BOOKSOFSHRI X

BranchStockAccount

	Rs.		**Rs.**
ToBalanceb/d ToGoodssenttoBranchA/c(balancingfig.)	16,000 1,40,000	ByCash A/c(cash sales) ByGoods sent to BranchA/c(returns) ByBranchAdjustmentA/c(loadingon spoilage) ByBranchP &LA/c(actualspoilage)ByBranch Debtors (credit sales)* ByBalancec/d	60,000 5,000 400 1,600 72,000 17,000
	1,56,000		1,56,000

BranchDebtorsAccount

	Rs.		Rs.
ToBalanceb/d	12,000	ByCash(receivedfromDebtors)	67,000**
ToBranchStockA/c(Credit sales)	72,000	ByBranch Exp. A/c(discount)	2,000
(balancingfigure)		ByBranch Expenses(bad debts)	1,000
		ByBalancec/d	14,000
	84,000		84,000

BranchExpensesAccount

	Rs.		Rs.
ToCash A/c Salariespaid6,000 Rentpaid 4,000 To Branch Debtors A/c (discount)ToBranchDebtorsA/c(bad debts)	 10,000 2,000 1,000	ByBranchAdjustmentA/cb alancingfigure)	13,000
	13,000		13,000

GoodsSenttoBranchA/c

	Rs.		Rs.
ToBranchStock(returnstoH.O)	5,000	ByBranch Stock A/c	1,40,000
ToBranchAdjustmentA/c (1/5 x1,35,000)	27,000		
ToBalancetr. to Trading A/c	1,08,000		
	1,40,000		1,40,000

BranchAdjustmentAccount

	Rs.		Rs.
ToBranchStockA/c(1/5 x 2.000)(loadingspoilage)	400	ByGoods sent to BranchA/c (loading)	27,000
ToStock Reserve(adjustment of	3,400	ByStock Reserve (adjustment of	3,200
closing stock (1/5 x 17,000)		stock 1/5 x 16.000)	
To Gross Profit c/d	26,400		
	30,200		30,200

BranchP&L Account

	Rs.		Rs.
ToBranchStockA/c		ByGross Profit b/d	26,400
(spoilageat cost)	1,600		
ToBranchExpensesA/c	13,000		
ToNetProfit	11,800		
	26,400		26,400

****WorkingNote:**
Amount(collected)recovered fromDrs.=Totalamountdeposited inH.O A/cduringthe year-CashSales1,27,000 - 60,000 =67,000

Independentbranchorbranchkeepingownaccounts: Wehavesofarconsideredbranchesthat do not maintain accounts themselves. The accounting is done at the head office. Now weshallconsider thebranchthat keeps itsown books of account.

The method of accounting is really simple; in essence it means treating the branch as a sort ofspecial customer. The branch keeps its accounts like anyone else. The head office will have a"Branch Account" in its books. All goods sent to the branch or cash sent to it will be debitedtothisaccountandcashreceivedfromthebranchwillbecreditedtoit.Entriesaremadeintheus ualmanner.Thebalanceinthisaccountwillshowtheamountinvested bytheheadofficeatthebranch. Similarly,thebranchwillopen"HeadOfficeAccount"initsbooks.Thebalanceshownbythisaccount will usually be credit. The balance shown by the Branch Account (in head officebooks)willbedebit.Theamountsinbothcasesshouldbethesame.Butduetocertainreasonsther e may be a difference. If there is a difference, the cause of it must be located and suitableentriespassedat theendof thefinancialyear.

Cash or goods in transit: One of the reasons for difference in the balance of the twoaccountsmaybecashsentbybranchbutreceivedbytheheadofficeafterthecloseoftheyear.Simil arly,thegoodssentbytheheadofficemayreachthebranchafterthecloseofthefinancialyear. Entries are passed immediately by the branch when cash is sent by the branch but theheadofficewillnotpassentryforreceiptuntilcashisactuallyreceived.Soalsoforgoodsin

transit. A record must be made for cash or goods in transit. The entry is usually made by theparty which sent the cash or goods. If cash sent by the branch has not yet reached head office,thebranch will pass theentry:

CashinTransit A/c Dr.

ToHead Office Account.

If goods sent by the head office are in transit, the head office will record it as under :Goodsin TransitA/c Dr.

ToBranchAccount

Butthereisno hardandfast ruleaboutit.In factitis enoughiteitherpartymakesarecord oftheitems in transit.

BoththecashinTransitandGoodsinTransit are assetsandshowninthe BalanceSheet.

Note: In examination' problems. cash or goods in transit may have to be inferred. Thisis done by comparing the balance of the Branch Account (in head office books) and of theHead Office Account (in branch books). Suppose the Branch Account shows a debit balanceofRs.16,000intheHeadOfficeAccount,itcanbetakentobeeitherCashinTransitorGoodsint ransit.

Accounts of branch's fixed assets kept in 11.0. books: Often the accounts of branch'sfixed assets are kept in head office books and not in branch's books. Even if the branch paysfor them the amount is debited to Head Office Account. The Head Office will debit the assetaccount and credit Branch Account. At the end of the year, the question of depreciation willarise.The entries tobepassed are:

InHeadOfficeBooks

BranchAccount Dr.

To Branch Asset

A/cInBranchBooks-

DepreciationAccount Dr.

ToHeadOfficeA/c

Head Office expenses: The head office will always do some work for the branch. At the endof the year, the head office may charge the branch with an amount representing the value ofthetimedevoted to the branch. Theentries required are:

In Head OfficeBooks-

BranchAccount

Dr.

ToSalaries Account.

InBranchBooks

Head Office Expenses

A/cDr.ToHead Office A/c

Illustration 9: Preliminary accounts made by the Kanpur Branch on 31st December, 1968showed a profit of Rs.9,500. It was found that the following items were not yet taken intoaccount:

CashremittedtoH.O.notyetreceivedthere	5,000
GoodssentbytheH.O.notyet receivedat Kanpur	4,000
DepreciationonBranchassets(accountskeptinH.O.books)	1,200
H.O.expenseschargedtothebranch	2,500

JournalisetheaboveinthebooksofboththeHeadOfficeandtheBranch.Alsoshowhowmuch is thereal profit at Kanpur.

Solution

H.O.Journal

1978		Dr.	Cr.
Dec.3	Goodsin TransitA/c Dr. ToKanpur BranchA/c (GoodssenttoKanpur,notyetreceivedthere)	4,000	4,000
Dec.31	KanpurBranchA/c Dr. to Kanpur Branch Assets A/c(Depreciation on Kanpur Branch assetschargedtotheBranchaccountofassets beingkept in own books)	1,200	1,200
Dec.31	KanpurBranchA/c Dr. To Salaries Account(Amountofexpenseschargedtothe Branchforworkdoneonitsbehalf)	2,500	2,500

BranchJournal

1978		Rs.	Rs.
Dec.31	CashinTransit A/c Dr. ToHeadOfficeAccount	5,000	5,000
	(Theamountofthecash senttotheH.O.notyet received there)		
Dec.31	DepreciationAccount Dr. To Head Office Account(Depreciation of Branch assets whoseaccountsarein Head OfficeBooks)	1,200	1,200
Dec.31	HeadOfficeExpenses A/c Dr. ToHeadOfficeA/c (Amountchargedtothebranchinrespectof work doneat theH.O.)	2,500	2,500

The profit at the Branch is reduced by Rs.1,200 and Rs.2,500, It now stands atRs.5,800.

Incorporation of Branch accounts in H.O. books: The branch sends its trial balanceto the Head Office which will then incorporate branch figures to prepare consolidatedProfitandLossAccountandBalanceSheet.TheentriestobepassedintheHead OfficeBooksare:

(a) Debit Branch Trading Account (with the items debited to TradingA/c
CreditBranchAccount
suchasopeningstock,purchases,wages,etc., atthebranch.)

(b) DebitBranchAccount

(withthesaleandclosingstockattheCreditBranchTradingAccount branch.)

(c) DebitBranchTradingAccount (transferof grossprofits.)
CreditBranchprofitand LossA/c

(d) DebitBranchProfitand LossA/c (with the total of expenses at theCreditBranch Profit andLoss Account branch.)

(e) DebitBranchAccount (withitemsofgainatthebranch.)
CreditBranchProfitand LossAccount

(f) DebitBranchProfitand Loss theAccount theCredit(General)ProfitandLoss c with the net profit at branch, as disclosed by BranchProfitandLossA/cA/

(Thisentrywill bereversed in caseof loss.)

Withthesesixentriesgivenabove,theBranchAccountwillshowabalanceequaltonetassetsatthebranch,i.e.,assetslessliabilities.IfitisdesiredtoclosetheBranchAccounttwofurtherentrieswill berequired:

(f) DebitBranchAssets(individually)
CreditBranchAccount;and

(g) DebitBranchAccount
CreditBranchLiabilities(individually).

Illustration10: AheadofficereceivesthefollowingTrialBalance fromitsbranch:

Debit	Rs.	Credits	Rs.
OpeningStock	21,800	HeadOfficeA/c	21,000
Purchases	42,000	SundryCreditors	5,600
Wages	10,200	Discountreceived	300
Salaries	6,300	Sales	81,000
GeneralExpenses	8,300		
SundryDebtors	18,200		
CashatBank	800		
	1,07,900		1,07,900

The closing stock at the branch was Rs.19,700. The Branch Account (in Head Officebooks) stood at a debit of Rs.26,500. Goods sent by the Head Office, Rs.1,000, had not yetreachedtheBranch.HeadOfficeexpenseschargeabletotheBranchwereRs.3,100.Depreciation of Branch assets whose accounts are kept in Head Office books was Rs.3,600.Record the above noted items and the incorporation of Branch figures in Head Office booksbymeans of journal entries and showBranch Account.

Solution

HeadOfficeJournal

1978			
Dec.3	Goodsin TransitA/c Dr. To Branch Account(Adjustmentforgoodsstillintr ansit)	1,000	1,000
Dec.31	BranchAccount Dr. ToSalariesAccount(Amount charged to the Branch inrespectofworkdoneonitsbehalf)	3,100	3,100
Dec.31	BranchAccount Dr. ToBranchAssets Account .(Depreciation on Branch assets whoseaccountsarekeptin H.O.Books)	3,600	3,600
	BranchTradingAccount Dr. ToBranchAccount (TotalofitemsdebitedtotheBranch TradingAccount,viz.,openingstock,pu rchasesand wages)	74,300	74,300

* Thestudentisadvisedtofirstprepare BranchTradingandProfitand LossAccountandthento note thejournal entries.

BranchandDepartmentalAccounts

		Dr. Rs.	Cr. Rs.
	BranchAccount Dr. ToBranchTradingA/c (Total of credit items credited to Branch TradingAccount)	1,00,700	1,00,700
	BranchTradingAccount Dr. ToBranchProfitandLossAccount(T ransferof gross profit)	26,400	26,400
	BranchProfitandLossA/c Dr. ToBranchAccount (Total expenses debited to Branch P & L a/cSalaries 6,300 GeneralExpenses8,300 H.O. Expenses3,100Deprec iation 3,600	21,300	21,300
	BranchAccount Dr. ToBranchProfitand LossA/c (DiscountreceivedcreditedtoBranchP&LA/c)	300	300
	BranchProfitandLossA/c Dr. To General Profit and Loss Account (NetProfittransferredtoGeneralProfitand	5,400	5,400

	LossA/c)		
	BranchSundryDebtorsA/c Dr. BranchBankA/c Dr. BranchStockA/c Dr. CashinTransitA/c* Dr. ToBranchAccount(Branchassetstransferredto H.O.Books)	18,200 800 19,700 4,500	43,200
	BranchA/c Dr. ToBranch SundryCreditors (Branch LiabilitiestransferredtoH.O.Books)	5,600	5,600

Note: If the last two entries are not passed, the Branch Account will show a balance,showingtheH.O.investmentattheBranchattheendoftheyear.Ifthetwoentriesare passed,the BranchAccountwillbalanceandaccountforvariousassetsandliabilitieswill be opened in theH.O. Books.

* ThedifferencebetweentheBranchA/cbalanceandH.O.A/cbalanceisRs.5,500(Rs.26,500 -21,000).OfthisRs.1,000isexplainedbygoodsintransit.Thebalanceofdifferenceisduetocashin transit.

BranchAccount

Debits	Rs.	Credits	Rs.
ToBalanceb/d	26,500	ByGoods in Transit A/c	1,000
ToBranchA/c H.O.Expenses	3,100	ByBranch TradingAccount	74,300
ToBranchA/c (Depreciation)	3,600	ByBranch ProfitandLossA/c	21,300
ToBranchTradingAccount	1,00,700	BySundryAssets	
ToBranch P& LA/c	300	Debtors 18,200	
To Branch sundryCreditors	5,600	Bank 800	
		Cashin Transit4,500	
		Stock 19,700	43,200
	1,39,800		1,39,800

Problem 2. Head office of a company invoices goods to its Madras branch at cost plus 20%.TheMadrasbranchalsopurchasesindependentlyfromlocalpartiesgoodsforwhichpaymentsa remadebytheheadoffice.Allthe cashcollectedbythebranchisbankedonthesamedaytothe credit of the head office and all expenses are directly paid by the head office except for apetty cash account maintained by the branch for which periodical transfers are made from theheadoffice. From the following particulars, show branch account as maintained in the head office books,reflectingthe branch profit for the yearended December31, 1995.

Imprestcash:	
3-1-1995	2,000
31-12-1995	1,850
Sundrydebtorson1-1-1995	25,000
Stockon1-1-1995:	
Transferred fromheadofficeatinvoiceprice	24,000
Directlypurchased bybranch	16,000
Cashsales	45,000
Creditsales	1,30,000
Directpurchases	45,000
Returnsfromcustomer	3,000
Goodssenttobranchfromheadofficeatinvoice price	60,000
Transferfrom head officeforpettycash expenses	2,500
Baddebts	1,000
Discounttocustomers	2,000
Cashreceivedfromcustomers	1,25,000
Branchexpenses	30,000
Stockon31-12-1995:	
Directlypurchased bybranch	12,000
Transferred fromheadoffice(atinvoiceprice)	18,000

Problem 3. Mohan Brothers had a small branch at Pondicherry. You are required to preparePondicherry Branch account in the books of Mohan Brothers for calculating profit made atPondicherrybranch.Transactionsduringthe year endingonMarch31,1995wereas follows:

Stockat coston 1-4-1994	4,000
Furnitureon 1-4-1994	2,000
Goodssentto branchatcost	60,000
Cashsales madebythe branch	90,000
Furniturepurchasedbythebranchonpermission fromheadoffice	1,200
Stockattheendwithbranch	3,500
Expensespaid byhead office	5,300

It was required to write off furniture at 10% p.a. No depreciation is provided on additionsmadeduringtheyear.Hint:Remittances willbereducedbythe amountspentonpurchases offurniture.

Problem4.NirmalBrothersoperatearetailbranchatMahe.Allpurchasesasmadebytheheadoffice at Madargate, goods being charged out to the branch at cost price. All cash received bythebranchisremittedtoMadargate.Branchpettyexpensesarepaidoutofanimprestwhichisreimb ursedbytheheadofficefromtimetotime.Fromthefollowingparticularsrelatingto

Mahe branch, you are required to prepare branch account (for calculating profit) in the booksofhead office:

January1, 1993:	Rs.
Stockatcost	7,000
Pettycash	700
Plant	8,000
December31,1993:	
Stockatcost	6,300
Goodssent tobranch	40,800
Expensespaidbytheheadoffice	4,200
Pettyexpenses paidbythe branch out ofimprest	630
Cashsalesduringthe year	60,700
Sale ofplant onJuly1, 1993 (bookvalue ofplant onthe date ofsaleRs. 950)	900
Itisrequiredto writeoffplant at10%p.a.	

Hints:Pettyexpenses will appear on thedebit side ofbranch account andpettycash balancewillremain at Rs.700 becauseof imprest system.

Problem 5. The KotahDoria Ltd. with its head office at Kotah opened a branch at Ajmer on1st January, 1992. Goods are invoiced to the branch at cost plus 25%. From the followingparticulars calculate gross profit and net profit or loss at Ajmer Branch (by Stock and DebtorsSystem)and open all necessaryaccounts.

	Rs.
Goodssent toAjmerbranch atinvoiceprice	45,000
Expensespaid byhead office	7,200
Discountallowed to debtors	50
Baddebtswrittenoff	80
Sale:Cash21,000 Credit12,000	33,000
StockonDecember31(Invoiceprice)	11,800
Goodsreturned bythebranch (Invoiceprice)	600
Goods returnedbydebtors	500
Cashremittedtoheadoffice	30,800
Cashinhand onDecember31	300

(GrossprofitRs.6,500;NetlossRs.910; DebtorsattheendRs.1,570)

Problem6.SwamyBros.ofGunturhaveabranchatVijayawada.Goodsaresenttothebranchat cost price plus 1/2 of cost price. From the following particulars prepare necessary accountsonStock andDebtors systemand calculate gross profitand netprofit forthebranch.

	Rs.
Stockinthebeginning(atinvoiceprice)	3,900
Goodssenttobranch	30,000
Goods returned bythebranch	3,000
Credit sales bythebranch	15,000
Cashremitted bythe branch	31,000
Debtorsbalancein thebeginning	4,000
Cashreceived bythe branch fromthedebtors	16,000
Cashreceived bythe head officedirect fromthebranch debtors	2,000
Baddebts	100
Cashdiscountoncashpayment	20
Shortageatthebranch	120
Recurringexpensespaidbythe headoffice	1,600
Non-recurringexpensespaidbytheheadoffice	200

Gross profit Rs.9,800; Net profit Rs.8,000)Note:

1. Differencebetweencashremittedandcashreceivedwillbetreated ascashsales.
2. Non-recurring expense is a term used for direct expense. Hence, non-recurringexpenseshavebeen taken toadjustment accountfor calculatinggrossprofit.
3. Recurringexpenses,beingindirect expenses,havebeentaken tobranchprofitandlossaccount.
4. Shortagehasbeen dividedinto twoparts. Theadjustment portionofshortageisconsideredfor calculatinggrossprofit andrestoftheportionfor thenetprofits.

(b) **Problem7.**PreethamandJeethuaretwopartnerswhorespectivelymanagePondyandMadrasbranches of MessrsPreejee& Co., and have calendar year as accounting year and share profits2/3rdsand 1/3rd respectively.

(c)

(d) On31-12-1994thebalancesstoodasunder:

	Pondy Rs.	Madras Rs.
OpeningStock	54,000	39,000
Madrasbranch(Dr.)	22,500	
PondyBranch(Cr.)	…..	18,000
Preethamcapital	1,02,000	
Jeethucapital	…..	24,000
Purchases	96,000	51,000
Sales	1,56,000	72,000
Booksdebts	22,500	15,000

Creditors	21,000	6,000
Wages	18,000	12,000
Freight(Inward)	2,700	1,200
Machinery(Pondy)	36,000	
Machinery(Madras)	24,000	
Cashinhand	3,300	1,800
ClosingStock	50,400	42,600

(e)

(f) Madras officedebited Pondyofficewith remittance madeon 31-12-1994 for Rs.

(g) 4,500 which wasreceived byPondyon2-1-1995.

(h) Partners are to be allowed interest at 5% by the respective offices. Each of theseofficeshas tochargedepreciation at 5%.

(i) Preparejournalentrieswith narrationinthebooks ofeachoftheofficesandalso thecolumnartradingand profit and lossaccount and balancesheet of the firm.

(j) [Pondy branch-Gross profit Rs.35,700; Net profit Rs,28,800; Madras branch-GrossprofitRs.11,400;NetprofitRs.9,000;Balancesheettotal-MadrasRs.63,900;PondyRs.1,53,300; Balance-PondyOfficeRs.20,100 (Cr.); Madras OfficeRs.20,100 (Dr.)].

UNIT- 2 DEPARTMENTALACCOUNTS

Introduction

A business may have a number of Departments each dealing in a different type of goods.Forexample,onedepartmentmaybedealinginmedicines,theothermaybedealingintextiles,still another may be dealing in provisions etc. In order to ascertain the profit or loss made byeachDepartment,itwillbeadvisabletoprepareseparatelyTradingandProfit&LossAccountof each Department at the end of the accounting year. Preparation of such DepartmentalAccountsis helpful to thebusiness in thefollowingrespects:

(i) Itenablesthebusinesstocomparetheperformanceofone Departmentwiththat ofanother.

(ii) Ithelps thebusiness informulatingproperpolicies relatingto theexpansion ofthebusiness. New profitable lines of production of trading can be taken up while theexisting lines of production or trading which are running at a loss can be closeddown.

(iii) IthelpsinappropriaterewardingorpenalisingtheDepartmentalemployees onthebasisof theresults shown bythem.

MAINTENANCEOFCOLUMNARSUBSIDIARYBOOKS

The principle of Departmental Trading and Profit & Loss Account requires maintenanceofpropersubsidiarybookshavingappropriatecolumnsfordifferentdepartments.Fore xample,if a business has three departments A, B & C, the subsidiary books such as Purchases Book,PurchasesReturnsBook,SalesBook,SalesReturnsBooksetc.,shouldhaveseparatecolumnsf or each of the departments. Cash Book may also have columns for recording cash sales ofeachofthedepartmentsseparatelyincasethevolumeofcashsalesisquitelarge.ThespecimenofaPu rchases Bookhavingcolumns fordifferentDepartments isgiven below:

PurchasesBook

Date	Particulars	L.F.	Dept.A	Dept.B	Dept.C	Dept.D

Thesame pattern ofrulingsmaybefollowed incaseof other subsidiarybooks also.

DEPARTMENTALISATIONOFEXPENSES

In order to ascertain the profit or loss made by each department, it is necessary thateachdepartmentischargedwithapropershareofthevariousbusinessexpenses.Thefollowingba sismaybeadopted fordepartmentalisation ofsuch expenses:

(i) Expensesincurredspecificallyforaparticulardepartmentshouldbedirectlychargedtoth atdepartment.Forexample,salariespayabletoeachofthedepartmentalmanagerswillbechar gedtotherespectivedepartments.Similarlyifthereareseparateelectricitymetres for each of the departments, the electricity should be charged to each of thedepartmentson the basisof theelectricitybillsreceived foreach oneof them.

(ii) Expenseswhichhavebeenincurredforthebusinessasawholebutcapableofbeingapporti oned over different departments on a suitable basis should be charged to thedifferent departments, on such basis. Of course, there are no hard and fast rules asregards the basis to be applied for apportionment of such expenses. However, thefollowingbasis for apportionment maybeadopted:

(a) **Departmental wages:** Expenses which directly vary with the departmentalwagescanbeapportionedonthisbasis.Forexample,premiumforwork-men'scompensation,insurance,E.S.I. maybeapportionedon this basis.

(b) **Capital value of the assets:** Expenses such as depreciation of buildings,plant and machinery, fire insurance premiums in respect of these assets etc. may beapportionedon this basis.

(c) **Floorarea:**Expensessuchaslighting(unlessmeteredseparately),rentandrates, wages of night watchman etc. maybeapportioned on this basis.

(d) **Number of workers employed:** Expenses of workers' canteen, welfare,personnel and timekeepingdepartments etc. maybeapportionedon this basis.

(e) **Productionhoursofdirectlabour:**Worksmanager'sremuneration,general over-time expenses, cost of inter-departmental transport should be charged tothevariousdepartmentsintheratiowhichtheDepartmentalDirectLabourHoursbearstotheTotal FactoryDirectLabourHours.

(f) **Technical estimate:** Advice of the technical personnel may also be usefulfor the apportionment of certain expenses e.g., the cost of steam consumed by aparticulardepartment, maybeestimatedon the basis oftheengineer'sestimate.

(iii) Expenseswhichcannotbeallocatedorapportionedoverdifferentdepartments in a reasonable manner, should be charged to the total profit of all thedepartmentstakentogether.Forthispurpose,theprofitsshownbythedifferentdepartmentsshouldbebroughtdowninoneaccountwhichwillbetermedasthe

GeneralProfit&LossAccountandallsuchexpensesshouldbechargedthere.GeneralManager's salary, Director's fees, Auditor's remuneration, Interest on Debentures etc.aresomeof theexpenseswhichfall in this category.

DepartmentalisationofExpenses

Illustration1.M/sRajuAutoGaragehavethreedepartments,viz.(i)CarsandTrucks,(ii)Two-wheelers, and (iii) Servicing. The former two sell spare parts and occupy a godown-cum-show-room.Theservicingdepartmentuses agarageandadjoiningsite.
Thefollowingparticulars areextracted fromthebooksofthebusinessforthe yearended31stMarch, 1979, from whichyouare requiredto prepare:

(a) ADepartmental TradingandProfit andLoss A/c,
(b) AGeneralProfitandLossA/c, and
(c) ABalanceSheet.

		Rs.
Stock1-4-78		
CarsandTrucks		1,00,000
Two-wheelers		27,500
Purchases:		
CarsandTrucks		3,50,000
Two-wheelers		1,10,000
Sales:		
CarsandTrucks	6,00,000	
Two-wheelers	3,00,000	
Servicing	1,00,000	

Wages of Counter-salesmen:Carsand Trucks	30,000
Two-wheelers	12,000
Wagesof garagelabour	10,800
Officesalaries andwages	12,000
Godownandshowroomrent	24,000
Land andGarageBuilding	2,72,000
OfficeExpenses	36,000
GarageEquipment	1,00,000
ShowroomFurnitureand Fittings	70,000
Officevan	24,000
SundryDebtors	12,000
SundryCreditors	60,000
BankOverdraft	17,200
Powerandlighting	36,000
BankInterest	1,000
Cashinhand	900
DrawingsA/c	12,000
Proprietor'sCapitalAccount	1,63,000

FollowingfurtherInformationisavailable:
(i) Included in " Land and Garage Buidling" is cost of suite used by the servicingdepartment
Rs.2,00,000.

(ii) Closing stock on 31.03.1979 at the departments
:CarsandTrucks Rs.90,000
Two–wheelers Rs. 32,500

(iii) 50%ofpowerand lightingisto bechargedtoServicing Department,thebalanceequallytothe other departments.

(iv) Ratesfordepreciationare:
Building5%,GarageEquipment15%,Showroomfurnitureetc.10%andOfficeVan20%.

(v) Outstandingexpenses were
Interest Rs.150
Officeexpenses Rs.2,000

(vi) Interestandallexpensesrelatingtotheoffice aretobe considered commonandchargedtotheGeneral Profit andLoss A/c.

(vi) The departments using the showroom share the space and furniture and fittingsequally.

Solution:

MESSRSRAJUAUTOGARAGE

DepartmentalTrading&ProfitandLoss AccountfortheyearendingMarch31,1979

Particulars	Cars& Trucks Rs.	TwoWheelersRs.	Servi-cingRs.	Particulars	Cars& Trucks Rs.	TwoWheelersRs.	Servi-cingRs.
ToOpeningStock	100,000	27,500	---	BySales	600,000	300,000	100,000
ToPurchases	350,000	110,000	---	ByClosingStock	90,000	32,000	--
ToWages	30,000	12,000	10,800				
ToGrossProfitc/d	210,000	183,000	89,200				
	690,000	**332,500**	**100,000**		**690,000**	**332,500**	**100,000**
ToGodown& Showroom	12,000	12,000	--	ByGross Profit b/d	210,000	183,000	89,200
ToPower& Lighting	9,000	9,000	18,000				
ToDepreciation:							
Building			3,600				
GarageEquipment			15,000				
Furniture	3,500	3,500	--				
ToNetProfitc/d	185,500	158,500	52,600				
	210,000	**183,000**	**89,200**		**210,000**	**183,000**	**89,200**

GeneralProfit&LossAccount forthe year ending 31stMarch,1979

Particulars	Rs.	Particulars	Rs.
ToOfficesalaries&wages	12,000	ByProfit b/d:	
ToOfficeExpenses36,000		Cars&TrucksDept.	1,85,500
Outstanding 2,000	38,000	TwoWheelersDept.	1,58,500
ToDepreciationonVan	4,800	ServicingDept.	52,600
ToBankInterest 1,000			
Outstanding 150	1,150		
ToNetProfit	3,40,650		
	3,96,600		3,96,600

BalanceSheetasat31st March,1979

Liabilities	Rs.	Assets	Rs.
Bankoverdraft	17,200	CurrentAssets:	
Outstandingexpenses		Cash-in-Hand	900
Interest150		SundryDebtors 12,000	
OfficeExpenses2,000	2,150	Stockintrade	
SundryCreditors	60,000	Cars&Trucks90,000	
		TwoWheelers32,500	1,22,500
Capital 1,63,000		FixedAssets:	
NetProfit 3,40,650		Land	2,00,000
5,03,650		GarageBuilding 72,000	
Less:Drawings12,000	4,91,650	Less:Depreciation 3,600	68,400
		GarageEquip. 1,00,000	
		Less:Depreciation15,000	85,000
		ShowRoomFurniture&Fittings 70,000 Less:Depr. 7,000	63,000
		OfficeVan 24,000	
		Less:Depr. 4,800	19,200

	5,71,000		**5,71,000**

ComputationofDepartmentalCosts

Illustration2. Thefollowingpurchasesweremadebyabusiness househavingthreedepartments:

DepartmentA 1,000 units
Department B 2,000 units at a total cost of Rs 1,00,000DepartmentC 2,400 units
Stock on 1stJanuarywere:
DepartmentA 120units, DepartmentB80unitsand DepartmentC152units.

Thesaleswere.Thesales were:

DepartmentA 1,020 units @ Rs.20 each.Department B 1,929units@Rs.22.50each.DepartmentC 2,496 units @Rs. 25 each.

Therateof grossprofit isthesameineachcase. PrepareDepartmentalTradingAccount.

Solution

InordertodeterminetherateofGrossProfit,itisassumedthatallunits purchasedhavebeensoldaway.

Sales:Dept.A 1,000units@ Rs.20 each 20,000
Dept.B2,000 units @Rs. 22.50 each 45,000
Dept.C 2,400 units@ Rs.25 each 60,000

TotalSales 1,25,000
Less:CostofPurchases 1,00,000
GrossProfit 25,000
GrossProfit asapercentage=25,000/ 1,25,000x100=20%

CostPriceofunitspurchasedforeachDepartmentcannowbe ascertained asfollows:

	SellingPrice	GrossProfit	Cost
Dept.A	Rs.20	Rs.4	16
Dept.B	Rs.22.50	Rs.4.50	18
Dept.C	Rs.25	Rs.5	20

Unitsof ClosingStock	Opening Stock	+	Purchase-		Sales
Dept.A	120	+	1,000	-	1,020 =100
Dept.B	80	+	2,000	-	1,920 =160
Dept.C	152	+	2,400	-	2,496 =56

DepartmentalTradingAccount cannowbepreparedasfollows:

DepartmentalTradingAccount

	Dept. A	Dept. B	Dept. C		Dept. A	Dept. B	Dept. C
ToOpening Stock	1,920	1,440	3,040	To Sales	20,400	43,200	62,400

ToPurchases	16,000	36,000	48,000	ToClosing Stock	1,600	2,880	1,120
ToGrossProfit	4,080	8,640	12,480				
	22,000	**46,080**	**63,520**		**22,000**	**46,080**	**63,520**

INTER-DEPARTMENTALTRANSFERS

Transfers of goods or services may take place from one department to another whilepreparingtheDepartmentalTradingandProfit&LossAccount.Thedepartmentreceivingthegoods orservicesshouldbedebitedwiththevalueofthegoodsorservicessosuppliedand the department providing such goods or services should be credited with the sameamount.

The transfer of goods from one department to another is usually at cost. However, ifsuch transfer is at a profit, the pi Da or low of each department should be ascertained onthe basis of the transfer price itself. However, if the goods transferred by one departmentto another at a profit, still remain unsold with the transferee department, an appropriatereserveforunrealisedprofitwillhavetobecreatedbymeansofthefollowingjournalentry.

GeneralProfit&LossAccount Dr. -
ToStockReserve

IncasethetransferreeDepartmenthasalsosomestockinthebeginningoftheaccountingyear, includingsomeunrealisedprofit,againstwhichstockreservewascreatedlastyear, such reserve will also be transferred to the General Profit & Loss Account by means ofthefollowingjournal entry.

StockReserveAccount Dr. -
ToGeneralProfit&LossAccount -

Alternatively,asingle journalentrymaybepassed forthe unrealisedprofit on thebasis ofthe difference between unrealised profit included in the opening and closing stocks. This willbeclear with the help of thefollowingillustration.

Illustration3. FromthefollowingTrialBalance,prepareDepartmentalTradingandProfitandLoss Accountfortheyearending31stMarch, 1974andtheBalanceSheetasatthat date:

(Rs.in'000)

Stock,1st April, 1973 ADepartment 1,700
BDepartment 1,450
Purchases ADepartment 3,540
BDepartment 3,020

Sales	ADepartment	6,080
	BDepartment	5,125
Wages	ADepartment	820
	BDepartment	270
Rent,Rates, Taxes andInsurance		939
SundryExpenses		360
Salaries		300
Lightingand Heating		210
Discountallowed		222
Discountreceived		65
Advertising		368
CarriageInward		234
Furnitureand Fittings		300
Machinery		2,100
SundryDebtors		606
SundryCreditors		1,860
CapitalAccount		4,766
Drawings		450
CashatBank		1,007

Thefollowingfurtherinformationisavailable:

1. Internaltransferof goodsfromAtoBDepartmentRs.42,000.
2. TheitemsRent,RatesandTaxesandInsurance, SundryExpenses, LightingandheadingSalaries andCarriage areto beapportioned2/3rdtoA Departmentand

   1/3rdto BDepartment.
3. Advertisingisto beapportionedequally.
4. DiscountsallowedandreceivedaretobeapportionedonthebasisofDepartmentalSalesand Purchases (excludingTransfers).

5.Depreciation at 10 per cent per annum on Furniture and Fittings and on Machineryisto becharged 3/4thstoA Department and1/4th to BDepartment.

6. ServicesrenderedbyBDepartmentto ADepartmentareincludedinwagesRs.50,000

7. Stock on 31st March 1974 in A Department was worth Rs.16,74,000 and in BDepartmentit was worth Rs.12,05,000.

Solution

DepartmentalTrading&Profit

Particulars	Dept. A	Dept. B	Particulars	Dept. A	Dept. B
ToOpeningStock	1,700	1,450	BySales	6080	5,125
ToPurchases	3,540	3,020	ByTransfer	42	50
ToWages	820	270	ByClosingStock	1,674	1,205
ToTransfer	50	42			
ToCarriage Inward	156	78			
ToGrossProfit	1,530	1,520			
	7,796	6,380		7,796	6,380
ToSalaries	200	100	ByGross Profit	1,530	1,520
ToRent, Rates,Taxes & Insurances	625	313	ByDiscount	35	30
ToSundryExpenses	240	120	ByNetLoss	126	----
ToLightingHeating	140	70			
ToAdvertising	184	184			
ToDepreciationon Machinery	158	52			
ToFurniture	22	8			
ToDiscount	121	101			
ToNetProfit	---	602			
	1,691	**1,550**		**1,691**	**1,550**

&LossAccountforthe yearending31st March, 1974

BalanceSheetas on31st March,1974(in thousand Rupees)

Liabilities			Assets		
Capital	4,766		Machinery	2,100	
Add:Profit	476		Less:Depreciation	210	1,890
	5,242		Furniture&Fittings	300	
Less:Drawings	450	4,792	Less:Depreciation	30	270
SundryCreditors		1,800	Stockintrade		2,879
			SundryDebtors		606
			CashatBank		1,007
		6,652			**6,652**

QUESTIONS

Problem1. FromthefollowingThal Balance,prepareDepartmentalTradingand ProfitandLossA/cfortheyear ended 31stMarch,1985andBalanceSheet asatthatdate.

TRIALBALANCE

	Dr. Rs.	Cr. Rs.
Stock1.4.84 DepartmentA	17,000	
DepartmentB	14,500	
Purchases DepartmentA	35,400	
Department B	30,200	
Sales DepartmentA	---	60,800
Department B	---	51,250
Wages DepartmentA	8,200	
Department B	2,700	
Rent,rates,taxesandInsurance	9,390	
Sundryexpenses	3,600	
Salaries	3,000	
Lightandheating	2,100	
Discountallowed	2,220	
Discountreceived	---	
Advertising	3,680	
Carriageinwards	2,340	
FurnitureandFittings	3,000	
Plantand Machinery	21,000	
Sundrydebtors	6,060	
Sundrycreditors	---	18,600
A'sCapitalAccount		47,660
A'sDrawing	4,500	
Cashinhand	170	
CashatBank	9,900	
	1,78,960	1,78,960

Thefollowinginformation is also provided:

(a) Internaltransferof goodsfromDeptt.AtoDeptt.BRs.420.

(b) Theitemsrent,taxesandinsurance,sundryexpenses,lightingandheating,salariesandcarriageinwards to beapportioned at 2/3rd toDept.A and1/3rd to Dept. B.

(c) Advertisingtobeapportionedequally.

(d) Discount allowed and received are apportioned on the basis of departmental sales andpurchases(excludingtransfers)corrected to nearest Rs.10.

(e) Depreciations at 10% per annum on furniture and fittings and on plant and machinery.Thisis to becharged3/4 to Dept.A and1/4 to Dept.B.

(f) ServicesrenderedbyBDept. includedin wagesRs.500.

(g) Stockasat 31.3.85ADept.Rs.16,740 andBDept.Rs.12,050.

(h) Fixedassetsremainunchangedduringtheyear.

Problem 2. The following balances were extracted from the books of Vijay Shanker. You arerequired to prepare departmentalTrading Account and Profit and Loss Account for the yearended31stDecember1984,afteradjustingthe unrealiseddepartmental profit,if any.

	Departments ARs.	**Departments** B Rs.
OpeningStock	50,000	40,000
Purchases	6,50,000	9,10,000
Sales	10,00,000	15,00,000

Generalexpensesincurredforboththedepartmentswere Rs.1,25,000andyouarealsosupplie dwith the followinginformations:

(a) ClosingStockof DepartmentARs.1,00,000 includinggoodsfrom DepartmentBforRs.20,000,at cost to Department A.

(b) Closing Stock of Department B Rs.2,00.000 including goods from Department A forRs.30,000,at cost to DepartmentB.

(c) Opening Stock of Department A and Department B includes goods of the value ofRs.10,000 and Rs.15,000 taken from Department B and Department A respectively atcostto transferred Departments.

(d) Thegrossprofitisuniformfromyeartoyear.

Problem3. Thefollowingis thetrial balanceofAutomaticMotorsand Garageon31stMarch,1985:

	Rs.	Rs.
CapitalAccount		76,250
Drawings	8,500	
OpeningStock:		
PetrolandOil	1,675	
Sparepartsandtyres	5,500	
Tools	2,200	
HireCars	72,000	
Tools	4,000	
Sparepartsandtyres	32,000	
PetrolandOil	41,250	
AdvertisingExpenses	4,500	

Rent,RatesandTaxes	12,000	
InsurancePermium:		
Onhirecars	4,000	
Fire,theftandburglarycases	425	
Wages:		
Drivers	12,000	
RepairsDepartment	16,500	
Office	7,500	
Garage	1,000	
Sales:		
PetrolandOil		23,000
Sparepartsandtyres		37,000
Garagereceipts		4,000
RepairsDepartment		14,000
HireReceipts		70,000
Licence feesandpermitfeesforhire cars	3,000	
OfficeExpenses	4,000	
SundryDebtors	400	
SundryCreditors		1,200
Commissionreceivedoncarssold		5,000
Loan		4,000
Cashin handand atBank	2,000	
	2,34,450	2,34,450

Thefollowingadditionalinformationisalsogiven toyou:

(a) Theloan wastaken on1st January, 1985on whichinterest at12% is tobepaid:

(b) Stocksin hand on 31stMarch, 1985 wereasunder:

(i)Tools	5,000
(ii)Petrol andOil	4,300
(iii)Spareparts andtyres	10,000

(c) Petrolandoil whose values wereRs.15,600 andRs.1,800 wereused byhiredcarsandrepairs department respectively. Besides, the owner of the garage drew petrol and oilworthRs.3,000 forhis personal car;

(d) RepairsDepartmentperformedworkduringthe year asunder:

(i) onowner'scarRs.600

(ii) onhirecars Rs.7,500

(e) Spareparts used bytheRepairs Department intheyearcostRs.4,000 and bythehiredcarsRs.750;

(f) Depreciationonhiredcarsto beprovided at30%perannum;

(g) LicencesandtaxesamountingtoRs.200on owner'scarhavebeenpaidand includedinRent, Rates and Taxes;

(h) Rent,Ratesand Taxestobedistributedasunder:

(i) RepairsDepartment1/2

(ii) SpareParts1/4

(iii) Garage1/8

(iv) Office1/8

YouarerequiredtoprepareaDepartmentalTradingAccount,aProfitandLossAccountforth eyearended 31st March,1985andaBalanceSheetas onthat date.

UNIT- 3 PARTNERSHIPACCOUNTS

Partnership is a form of organization for doing business. Under an agreement, two ormorepersonsjointogethertodoabusinessandshareitsprofit.Thebusinessmayberunbyallor byoneamongthem actingfor all.

Partnershipaccountsincludenotonlyfinalizationofaccountsbutalsosolvingproblems that are special in nature to partnership organization viz., appropriation of profits,admissionofpartner,deathandretirementofpartner,dissolutionofpartnership,insolvencyo fpartnersetc.Partnershipaccountsaregovernedbygeneralprinciplesofaccountancy,partnershipag reement (deed) and Partnership Act, 1932.

The terms of the agreement among partners may be either verbal or in writing. If it isin writing, it is known as Partnership Deed. It is desirable to have it in writing. Following aretheusual contents of thePartnership Deed.

ContentsofPartnershipDeed

1. Namesandaddresses ofthefirmandpartners.
2. Natureof thebusiness.
3. Dateofcommencementofpartnership.
4. Durationofpartnership.
5. Amountof capitalcontributed or tobecontributed byeach partner
6. Amountof drawingsallowed bythefirmto eachpartner.
7. Rulesregardingoperationofbank accounts.
8. Interestonpartnerscapitalanddrawings.
9. Ratioin which profits andlosses areto beshared.
10. Intereston loanbythepartners tothe firm.
11. Salaries,commission,etc.ifpayabletopartners.
12. Methodsofkeepingaccountsandaudit.

13. Rights,dutiesandliabilitiesofthepartners.
14. Accountingtreatmentin caseof admission,retirement,death etcofapartner. Modeofsettlement ofaccounts ondissolutionof thefirm.
15. Methodof settlingdisputes amongstthepartners.

In case the Partnership Deed is silent on certain matters, the relevant provisions of thePartnershipActshallbeapplicable.FollowingaretheprovisionsofthePartnershipAct,whichhav eadirectbearingontheaccountingtreatmentofcertainitems,incasetheDeedissilentontheseutters.

1. Partnersshareprofits orlossesequally.
2. Nointerestischargedonpartners'capital.
3. Nointerestis chargedbythe firmon partners'drawings.
4. Nopartnerisentitledto salaryorcommission.
5. 6%interestischargedonpartners'loan.

Appropriationof Profit

In a proprietary organization, the entire profit belongs to the proprietor alone, but in apartnership it has to be shared among all partners. So the profit shown by the profit and lossaccount is to be apportioned among partners according to the terms of partnership deed, or incaseit is silent, accordingto theprovisions of theAct.

SometimestheDeedmayprovidesalarytoapartner,whoismanagingthefirm,intereston partners' capital and interest on partners' drawings. These items are to adjusted and theremaining profits are to be appropriated among the partners. In this context, a Profit and Loss(Appropriation)Accountisprepared toappropriateprofits amongpartners.

FormatofProfitandLoss(Appropriation)Account

		Rs.			**Rs.**
To Salaryto partner			ByProfit&Lossa/c (Netprofit)		-------
	X— Y—	------	ByInterestondrawingsX — Y—		-------
ToInterestoncapital	X— Y—	-------			
ToReservefund					
ToCapitalaccount	X— Y—	-------			
(Profitstransferred)		------- ------			

FixedandFluctuatingCapital

Capital accounts of partners are maintained either under fixed capital system or underfluctuatingcapitalsystem.Underfixedcapitalsystem,acapitalaccountandacurrentaccountis opened for each partner. A partner's original contribution is shown in his fixed capitalaccount and all other entries like his share of profit, salary, drawings, interest on capital andinterest on drawings are shown in his current account whereas in fluctuating capital system apartner's original contribution as well as other items are shown in his capital account. Herethereis onlyonecapital account for each partner.

Example1.

On January 1, 1993, X, Y, Z entered into a partnership contributing Rs.3,00,000,Rs.2,00,000 and Rs.1,00,000 respectively and sharing the profits in the ratio 2:2:1. X and Yareentitledtoanannualsalaryof Rs.30,000andRs.15,000respectively.5%interestoncapitalis to be allowed. Interest on drawings is to be charged at 6%. The drawings of X, Y and Z areRs.1500,Rs.1000,Rs.500permonthrespectivelydrawnattheendofeverymonth.Profitsforthe year ended 1993, before the above adjustment were Rs.1,50,000. Show how the profit isdistributedandalsopreparethecapitalaccounts(a)ifitheyarefluctuating(b)iftheyarefixed.

Solution

ProfitandLoss(Appropriation)Account(Fig.inrupees)

		Rs.			**Rs.**
ToPartner'sSalary			ByNet Profit		1,50,000
	X30,000 Y15,000	45,000	ByInterestondrawings	X495 Y330 Z165	990
ToInterestoncapital	X15,000 Y10,000 Z5,000	30,000			
ToCapitalaccount	X30,396 Y30,396 Z15,198	75,990			
		1,50,990			1,50,990

Date	**Particulars**	**X**	**Y**	**Z**	**Date**	**Particulars**	**X**	**Y**	**Z**
1993	ToDrawings	18000	12000	6000	1993				
1993 Dec. 31	To Interestondrawings	495	330	165	Jan. 1 Dec. 31	ByBank BySalary ByInterest OnCapital	3,00,000 2,00,000 15,000	2,00,000 15,000 10,000	1,00,000 5,000

						ByP &L (App)A/c	30,396	30,396	15,198
		3,56,901	2,43,066	1,14,033					
		3,75,396	2,55,396	1,20,198			3,75,396	2,55,396	1,20,198

FixedCapitalAccounts *(Fig.inrupees)*

Date	Particulars	X	Y	Z	Date	Particulars	X	Y	Z
1993 Dec.31	ToBalance c/d	3,00,000	2,00,000	1,00,000	1993 Jan.1	ByBank	3,00,000	2,00,000	1,00,000
		3,00,000	2,00,000	1,00,000			3,00,000	2,00,000	1,00,000

CurrentAccounts*(AlsoknownasDrawingsAccount* *(Fig.in Rupees)*

Date	Particulars	X	Y	Z	Date	Particulars	X	Y	Z
1993 Dec.31	ToDrawings	18,000	12,000	6,000	1993	BySalary	30,000	15,000	---
	ToInterestond rawings	495	330	165	Dec. 31	ByInterest onCapital	15,000	10,000	5,000
	ToBalance c/d	56,901	43,066	14,033		ByP &L (App)A/c	30,396	30,396	15,198
							75,396	55,396	20,198
		75,396	55,396	20,198	1994 Jan. 1	ByBalance b/d	75,396	55,396	20,198

Note:

Calculationofintereston drawings:

Ifdrawingsaremadeatregularintervalsandthattooinfixedamounts,theninterestondrawings can be calculated on the basis of average period. The calculation of average perioddepends whether they are made at the beginning of the month or at the end of the month.Suppose, fixed amounts are drawn at the beginning of the month, then the average period iscalculated as follows:

=(Totalperiods in months +1)/2

Ontheotherhand, iffixedamounts aredrawn at theend ofthemonth theaverageperiodis calculated as follows:

=(Total periods in month– 1)/2

In the above problem, fixed amounts are drawn at the end of every month. So interestondrawings is calculatedas below:

AveragePeriod	=12-1 /2
	=5.5 months
InterestonX'sdrawings	=1500 x5.5x6/100
	=Rs.495
InterestonY'sdrawings	=1000 x5.5x6/100
	=RS.330
Intereston Z'sdrawings	=600 x5.5x6/100
	=Rs.165

Admissionof aPartner

Apersoncanbeadmittedintoapartnershipfirmifalltheexistingpartnersagreetohisadmission.

Anewpartnerisadmittedtoimprovethebusiness,ashemaybringinadditionalcapitalor may possess business acumen. When admitted, the new partner has a right to his share ofprofit,as agreed, aswellas to his shareof assets in the firm.

In case of admission of a new partner, the following accounting problems are encounteredwith:

1. Calculationofnewprofitsharingratiosandthe sacrificingratios.
2. Calculationofgoodwillanditstreatment.
3. Revaluationofassetsandliabilities.
4. Distributionofundistributedreserves,profitsorlosses.
5. Adjustmentofcapital accounts.

I. Calculationofnew profitsharingratiosandthesacrificingratios

Calculationofnewprofitsharingratioswilldependonthetermsofagreementamongpartners admittingthenewpartner. Therearetwovariations in this regard.

1. The new partner is given his share of profit and the remaining share of profit ispresumedto bedividedbetween the oldpartners in theold profit sharingratio.
2. Hemayacquireit in someagreed ratio fromold partners.

SacrificingRatio

Sacrificingratioisthedifferencebetweenoldprofitsharingratioandnewprofitsharingratio. It will tell how much of share of profit is sacrificed by old partner due to admission of anew partner and giving him a share of profit. The following cases explain the calculation ofnewprofit sharingratios and sacrificing ratios.

Case1

Thenewpartnerisgivenhisshareofprofitandtheremainingshareofprofitispresumedto bedivided between the old partners in the old profitsharingratios.

XandYarepartnerssharingprofitsandlossesintheratioof3:2.Theyadmit'Z'tothepartnershipfor 1/3 ofprofits. Calculate thenew profit sharingratio and sacrificingratio.

Solution

‘Z’isgiven1/3profits.

Thereforeremainingshareofprofits = 1 – 1/3

=2/3

2/3 of profits are to be shared between X and Y in the old profit sharing ratio.Therefore,

X’s share =2/3 x3/5 =2/5

Y’s share =2/3 x2/5 =4/15

Z’s share =1/ 3

X’s share =2/3 x3/5 =2/5

Y’s share =2/3 x2/5 =4/15

Z’s share =1/ 3

Therefore,

NewprofitsharingratioX:Y:Z: 2/5:4/15:1/3

=6:4:5

Profit ratio between X and Y remains the same. So sacrificing ratio of X and Y isnothingbut theold profitsharingratio.

Case2(a)

A and B are partners sharing profits and losses in the ratio of 5:3. C is admitted to thepartnership and he acquires 3/16 share of profit from A and 1/16 share of profit from B.Calculate new profit sharing ratios among all partners and the sacrificing ratios between oldpartners.

A’snew shareof profit = 5/8 – 3/16

=10-3/16

=7/16

B'snew shareofprofit = 3/8 – 1/16

=6 – 1/16

=5/16

C'snew shareof profit=3/16+1/16

=3 +1/16

=4/16

Newprofitsharingratios=A:B:C

=7:5:4

SacrificingratiosbetweenAandBA gives up (sacrifices) 3/16 shareBgivesup (sacrifices)1/16 share

Therefore

Sacrificingratio=3:1

Case2(b)

M and N are partners sharing profits and losses in the ratio of 3:1. They admit '0' for1/5shareinprofitswhichheacquiresequallyfromMandN.Calculatenewprofitsharingratioandsacrificing ratio.

Ogets1/5share.

(i.e.)1/2of1/5=1/10 he getsit fromMandNeach.

Therefore,

M'snew share=3/4– 1/10

=15-2/20

=13/20

N'snew share=1/4-1/10

=5-2/20

=3/20

O'sshare = 1/5 or

4/20Therefore

Newprofit shareratio =M:N:O=13:3:4

Astheoldpartnersgive

uptheirsharestonewpartnersequally,thesacrificingratiobetweenM and N is 1:1.

Case2(c)

PandQarepartnerssharingprofitsandlossesintheratioof3:2.TheyadmitRfor1/5share of profit which he acquires wholly from 'P'. Calculate the new profit sharing ratio andsacrificingratio.

P'snewshare=3/5–1/5

=2/5

Q's new share = 2/5 (No

change)R'sshare=1/5

Newprofitsharingratio=2:2:1

Here,P,alonegiveshis1/5 sharetoR. SosacrificingratioforP is1/5.

CalculationandTreatmentofgoodwill

Goodwillisanintangibleasset.Theabilityofabusinesstoearnexcessprofitisduetoits reputation. This reputation expressed in monetary terms is goodwill. A number of factorsareresponsible for goodreputation likelocation,product, management,etc.

Goodwill is valued usually at the time of sale of business. But in the following casesalsogoodwill is valued.

1. Whenprofitsharingratiosamongexistingpartnersischanged
2. Admissionofapartner

3. Deathorretirementof apartner
4. Amalgamationoftwofirms.

Followingarethemethodsofvaluinggoodwill:

1. Averageprofitsmethod
2. Superprofitsmethod
3. Capitalizationmethod

I.Average ProfitsMethod

Inthismethod,goodwillisvaluedbymultiplyingtheaverageprofitsoflastfewyearsbyanagr eed number.

Goodwill=AverageprofitsxNo.of years'purchase.

Example1 Computethe valueofgoodwillonthe basisofthreeyears'purchaseof theaverageprofits oflast 4years.Theprofits ofthelast 4years are:

1990-Rs. 80,000

1991-Rs. 90,000

1992-Rs. 82,000

1993-.Rs. 86,000

Solution

Averageprofitsoflastfour years

80,000 +90,000 +82,000+86,000/4

3,38,000/4 =Rs. 84,500

Valueofgoodwill =Rs.84,500 x3 =Rs.2,53,500

Another variation of average profit method is weighted average method. Here weightsareassignedtoeachyear'sprofitandtheweightedaverageprofitsiscalculated.Heregoodwill is

Goodwill=weightedaverageprofitxNo.ofyears purchase

Example2

Computethegoodwillofafirmonthebasisof3years'purchaseofweightedprofitsoflastfoury ears (assign weights 1,2, 3 and 4 seriallyto theprofits).

Profitsoflast4 yearsare:

1990-Rs. 40,000

1991-Rs. 45,000

1992-Rs. 50,000

1993-Rs. 55,000

Solution

Year	AnnualProfits	Weights	Product
1990	40,000	1	40,000
1991	45,000	2	90,000
1992	50,000	3	1,50,000
1993	55,000	4	2,20,000
		10	5,00,000

Weightedaverageprofit=Totalproduct /Totalweight

=5,00,000/10=Rs. 50,000

Valueofgoodwill=Wt.averageprofitxNo.ofyearspurchase

=50,000 x3 =Rs. 1,50,000.

2. SuperProfitsMethod

Super profits are profits earned in excess of normal profits.Goodwillunderthis method=Super profitxNo. ofyears'purchaseNormalprofit=Capitalemployed xnormal rateof return

Example3

Fromthefollowinginformation, calculate goodwillusingsuperprofitsmethod.

a) Capitalemployed in thebusiness Rs.6,00,000

b) Normalrateofreturn 10%

c) Profitsforthelast 3years wereRs.75,000;Rs.80,000;Rs.85, 000

d) Goodwill is 4 years purchase of super profitAverageprofits=75,000 +80,000+85,000/3

=2,40,000/3 =Rs. 80,000

Normalprofit=Capitalemployedx normalrateofreturn

=6,00,000x10/100 =Rs. 60,000

Super profit = Rs. 80,000 - Rs. 60,000 = Rs. 20,000Goodwill= Rs. 20,000 x 4 =Rs. 80,000

CapitalizationMethod

Underthismethodgoodwillisthedifferencebetweencapitalizedvalueofaverageprofitsat normal rate ofreturn and actual capitalemployed.

ExampleFromthefollowing,calculategoodwill:

a) Normalrateofreturn 10%

b) Average profits for last 3 yearsRs.75,000;Rs.80,000;Rs.85 ,000

c) TotalassetsRs.7,00,000andtotalliabilitiesRs.2,00,000

Solution

Averageprofits=75,000 +80,000 +85,000 3 /3

=Rs. 80,000

Capitalizedvalueofaverageprofits

=averageprofitx100/Normalrate ofreturn

=80,000 x100/10

=Rs. 8,00,000

Capitalemployed=Totaltangibleasset-Totalliabilities

=Rs. 7,00,000 -Rs. 2,00,000

=Rs. 5,00,000

Goodwill =Capitalizedvalueofaverageprofitatnormal rateofreturn– Capital employed

=Rs. 8,00,000 - Rs. 5,00,000

=Rs. 3,00,000

TREATMENT OF GOODWILL

Whenanewpartnerisadmittedintoafirm,theoldpartnersgiveupapartoftheirshareof profits in favour of the new partner. Also the new partner is going to enjoy the goodwill ofthe firm which was built up by the old partners. So the old partners have to be compensatedeither by payment of money by the new partner or by way of extra credits in their capitalaccounts.

There are three ways by which goodwill is dealt with when a new partner is admitted. Theyare

1. PremiumMethod
2. RevaluationMethod
3. MemorandumRevaluationMethod

1. PremiumMethod

Underthismethod,thenewpartnerbringshisshareofgoodwillandthesameissharedbyoldpartnersintheirprofitsacrificingratios.Ifthepaymentismadeprivatelytooldpartnersno entry is required in the books of accounts. But if the payment is made through the booksthe—followingentries arepassed.

1. Bank/casha/c Dr–

Togoodwilla/c

[Theamountof goodwillbroughtin bythenew partneraspremium]

2. Goodwilla/c Dr–

Tooldpartner'scapitala/c(individually) –

[Goodwill brought in by new partner credited to old partners in their sacrificingratios]

Sometimestheoldpartnersmaybeallowedtowithdrawtheiramountofgoodwill(fullor apart ofit). Thefollowingentryis passed.

Oldpartnerscapitala/c Dr –
(individually)
Tocash
[Amountof goodwill withdrawn byold partners]

Example

X and Y are partners in a business, sharing profits and losses @ 3:1. They admit Z for 1/5share.Zbrings1s.10,000ashiscapitalandRs.8,000asgoodwill.PassJournalentrytorecordthetransactions

(a) whengoodwillamountisreturnedinthebusiness
(b) whenthe entireamount ofgoodwilliswithdrawn
(c) when50%of thegoodwill iswithdrawn

SOLUTION:

(a) WhengoodwillisreturnedinthebusinessBank/Casha/c
Dr18000
ToZ'scapitala/c10000Togoodwill a/c8000
[Amount brought in by 'Z' for capital and goodwill]Goodwilla/c
Dr8000
ToX'scapital a/c 6000
ToY'scapital a/c 2000
Amount goodwill brought in by new partner credited to old partners' capital accounttheirsacrificing ratios]

(a) Incasetheamountof goodwilliswithdrawn,thenapartfrompassingthetwo entries,thefollowingadditional entryis to bepassed forwithdrawal.

X's capitala/c Dr. 6000
Y's capitala/c Dr. 2000
Tocash/banka/c 8000
[Thegoodwillcreditediswithdrawn]

(b) Incase50%of thegoodwill is withdrawn,thewithdrawalentryis asbelowX's capitala/c Dr

Y's capitala/c Dr

Tocash/banka/c 4000

[50%ofgoodwillcreditediswithdrawn]

RevaluationMethod

When the incoming partner is not in a position to pay in cash for goodwill, thengoodwillisraised inthebooks,bycreditingtheold partners'capital accountin theirold profitsharingratio. Therearetwo possibilities here

1. Nogoodwillaccountappearsinthebooksatthetimeofadmission
2. Whenthereis goodwillaccount atthetimeofadmission

Nogoodwillaccountappearsin thebooksatthetimeof admission

In such a case goodwill is to be brought into books at its agreed value by debiting thegoodwill account and crediting the capital accounts of old partners in their old profit sharingratio. Here the goodwill account will appear in the balance sheet. The following journal entryis passed.

Goodwilla/c Dr -

Tooldpartnerscapitalaccount (individually)-

[Goodwillisraisedbydebitinggoodwilla/candcreditingoldpartnerscapitalaccountintheiroldprofit sharingratio]

Example

X and Y are partners sharing profits and losses in the ratio of 3:1. They admit 'Z' for1/5 share. 'Z' brings in Rs.20,000 for his capital, but is not in a position to bring cash forgoodwill. The value of goodwill is agreed at Rs.12,000. No goodwill account appears in thebooks.Pass necessaryentries.

Cash/banka/c Dr20000

ToZ'scapital account 20000

[Being the amount brought in by Z for his capital]Goodwilla/c Dr 12000

ToXs capital a/c 8000

ToY'scapital a/c 4000

[Goodwillaccountbeing raisedinthebooksat itsvaluebycreditingthe oldpartners'capitalaccountin theirold profitsharingratio]

1. **Whenthereisgoodwillaccountatthetimeof admission**

Incaseatthetimeofadmissionofapartnerthereappears goodwillaccountinthebooks,thenadjustment for goodwill in the old partners capital account is made only for the differencebetweentheagreedvalueofgoodwill andthe amountof goodwillappearinginthebooks.

Iftheagreedvalueofgoodwillismorethanthegoodwillaccountappearinginthebooks,thengoodwill accountistobefurtherincreasedbycreditingtheoldpartnerscapitalaccountintheiroldprofit sharingratio.

If the agreed value is less than the goodwill appearing in the books then the excess value ofgoodwill is written back by debiting the old partners capital account in the old profit sharingratio.

Example

X and Y are partners of a firm sharing profits and losses in the ratio of 3:2. They admit Z for1/5 share in profits. Z brings in Rs.20,000 as his capital. The value of goodwill is estimated atRs.20,000. Givejournal entries under the followingcircumstances.

1. Whenthereis no goodwill appearingin thebooks of thefirm
2. Whenthegoodwillaccount appearsatRs.10,000 inthebooks ofthefirm
3. Whenthegoodwillaccount appearsatRs.30,000 inthebooks ofthefirm

Solution

(a) when there is no goodwill appearing in the

booksCash/Banka/c Dr 20,000

To Z's capital account

20,000[Beingthecapital introduced byZ]

Goodwilla/c Dr 20,000

ToX's capitalaccount 12,000

ToY's capitalaccount 8,000

[Goodwillaccount israised bycreditingcapitalaccounts ofXandY intheir oldprofitsharingratio]

(b) whenthe goodwillaccountappearsatRs.10000inthebooksofthefirm(Agreedvalue ismorethan thebook value)

Cash/Banka/c Dr 20000

ToZ'scapitalaccount 20000

[BeingtheamountbroughtinbyZascapital]Goo dwilla/c Dr 10000

ToX'scapitala/c 6000

ToY'scapitala/c 4000

[Goodwillaccountisraisedtoitsagreedvalueofcreditingthecapitalaccounts ofXandYin their old profit sharingratio]

(c) When goodwill account appears at Rs.30,000 (Agreed value is less than the book value)Cash/Banka/c Dr 20000

To Z's capital a/c 20000[Beingtheamountbrought inbyZas his capital]

X's capitala/c Dr 6000

Y's capitala/c Dr 4000

Togoodwilla/c10000

[GoodwillaccountappearinginthebooksiswrittenofftotheextentofRs.10,000tomakeitappearatRs .20,000bydebitingtheoldpartnerscapitalaccountintheiroldprofitsharingratio].

MemorandumRevaluationMethod

If allpartnersdecidenottoshowthegoodwillaccountinthe books,thentheycanwriteback the same bypassingthefollowingentry.

Allpartnerscapitala/c(individually) Dr

Togoodwill a/c –

[Goodwilla/ciswritten backbydebitingthepartners capitalaccount,includingthenewpartner in thenew profit sharingratio].

Example

A and B are partners sharing profits and losses in the ratio of 5:4. They admit 'C' andthe new profit sharing ratio is 4:3:2. 'C' brings Rs.20,000 as his capital. The value of goodwillis estimated at Rs.36,000. Give necessary entries in the books of the firm on C's admissionassumingthat the partners do notwant goodwill toappear inthebooks.

1) Cash/banka/c Dr20000

ToC'scapital a/c20000

[Beingthecashbrought inby'C'ashis capital]

2) Goodwilla/c Dr36000

ToA'scapitala/c 20000

ToB'scapital a/c 16000

[Goodwillaccount raised in thebooks onC's admissionbycreditingtheoldpartners'capital account intheirold profit sharingratio (i.e.) 5:4]

3) A's capitala/c Dr

16000B'scapital a/c Dr 12000

C'scapital a/c Dr 4000

Togoodwilla/c36000

[Goodwill account is written back by delivering the partners capital account intheirnew profit sharingratio]

Revaluationof Assetsand Liabilities

At the time of admission of a partner into a partnership firm the assets and liabilitiesof the firm is revalued. The logic behind this exercise is to see that the new partner is notgaining due to understated assets and overstated liabilities or losing due to overstated assetsandunderstated liabilities.

A revaluation (also known as Profit and Loss Adjustment Account) is opened and necessaryentries are passed to bring the assets and liabilities to its real value at the time of admission.Then the profit or loss arising out of revaluation of assets and liabilities is transferred to thecapitalaccounts of theold partners in theirprofit sharing ratios.

Thefollowing entriesare passed torecord therevaluation of assetsand liabilities.

1) Forincreasein thevalue ofassets

Assetsa/c Dr –

Torevaluation a/c

2) FordecreaseinthevalueofassetsRe

valuationa/c Dr–

Toassetsa/c

3) For increase in the value of liabilitiesRevaluationa/c

Dr–

Toliabilitiesa/c

4) For anydecreasein thevalue

ofliabilitiesLiabilitiesa/c Dr–

Torevaluationa/c

5) Fortransferofprofitonrevaluation

Revaluationa/cDr–

Tooldpartnerscapitala/c(individually)

6) Fortransferoflossonrevaluation

Old partners' capital a/c (individually) Dr –

Torevaluation a/c

Sometimesthepartnersmaydecidenottoalterthevalueofassetsandliabilitiesbutatthesametime revalue the assets and liabilities and account for its profit/loss on revaluation. In such acircumstance,aMemorandumRevaluationAccountisprepared.First,entriesarepostedinthisacco unt for any increase/decrease in the value of assets/liabilities as explained before and theprofit/loss is transferred to capital accounts of old partners. Then the entries posted for anyincrease or decrease in assets/liabilities are reversed and so the assets and liabilities are againbroughttoitsoriginalvalue.Anyprofit/lossarisingoutofreversalofentriesforincrease/decreas e in the value of assets and liabilities are transferred to capital account of allpartnersin theirnew profit sharingratio.

Journalentriesinthisregardare:

Incaseofprofitonrevaluation

1. MemorandumRevaluationAccount Dr–

ToOldpartnerscapitalaccount(i ndividually)

[Profitonrevaluationtransferredtooldpartnersintheiroldprofitsharingratio]

2. Allpartners'capital account(individually)Dr –

ToMemorandumrevaluationa/c

[Profit previously credited is now returned back by debiting all partners capitalaccountsin their new profit sharing ratios]

In caseoflossonrevaluation,theaboveentriesarereversed.

3. Adjustmentofundistributedprofits,reserves orlosses

When a new partner is admitted, profits, reserves or losses appearing in the books at the timeof admission is to be distributed to old partners in the old profit sharing ratio. The followingjournalentries arerelevant in thisregard.Fordistributingprofits andreserves

Profitandloss a/cDr -

Reservea/c Dr -

Tooldpartnerscapitala/c(individually)

[Distributionofprofitsandreservesat thetimeofadmissionofanewpartnertooldpartnersin theirold profit sharing ratio]

Fordistributinglosses

Oldpartnerscapitala/c–(individually)

Toprofit&lossa/c (debit balance)–

[Losses at the time of admission of a partner distributed to old partner in the old profitsharingratio]

4. Adjustmentsof capitalaccounts

At the time of admission of a partner, the partners may decide to have a balance intheir capital accounts in proportion to their profit sharing ratio. So if they have excess orshortage of capital in relation to their profit sharing ratio, adjustment in their capital accountsare to be made. In case any partner has excess capital, the following entry is passed to correcthiscapital account in proportion to his profit sharingratio:

Partners capital a/c Dr-

Tocash/bank a/c –

[Excess capital withdrawn by the partner who is having excess capital] In case hiscapitalfallsshortofthe amountofcapital,calculatedinproportiontohisprofitsharingratio,the followingentryis passed:

Cash/Banka/c Dr -

ToPartnerscapitala/c–

[Cash is brought in by the partner to make his capital account in proportion to hisprofitsharingratio]

Illustration1

Thefollowingwas thebalancesheetofA,BandC whowere equalpartners.

Balancesheet ofA, B andC as onJune1, 1982

CapitalAccounts	Rupees		Rupees
A	16,800	Building	19,500
B	12,600	Furniture	2,400
C	6,000	Stock	11,400
Creditors	6,000	Debtors	10,800
Billspayable	3,300	Cash	600

	44,700		44,700

They agreed to take D into partnership and give him 1/4 share in the profits on thefollowingterms:

1. That'D'shouldbringin Rs.9,000forgoodwill andRs.15,000 as capital.
2. That1/2of thegoodwillshall bewithdrawnbytheoldpartners.
3. Thestock and furniturebe depreciated by10%
4. Thataprovision of5% on debtorsbecreatedfordoubtfuldebts.
5. Thata liabilityforRs.1,080becreated against bills discounted.
6. That the value of the building, having appreciated, should be valued at Rs.27,000.GivejournalentriesandprepareRevaluationAccountandtheopeningB alance

Sheetofthereconstitutedfirm;

(i) in case the partners decide to show the assets and liabilities at the newvalue.

(ii) in case the partners decide not to alter the value of asset& and liabilitiesexceptcash.

SOLUTION:

CASE1 :

If thepartnersdecidetoshowtheassetsandliabilitiesatthenewvalue.

JournalEntries

Casha/c Dr24,000

ToD'scapitala/c 15000

Togoodwilla/c 9000

(Cash brought in by the new partners D as his capital and goowill]Goodwilla/c Dr9000

To A's capital a/c 3000To B's capital a/c 3000ToC'scapitala/c3000

[Being the goodwill brought in by 'D' in cash distributed to old partners in their sacrificingratio].

A's capital a/c Dr 1500B's capital a/c Dr 1500C'scapital a/cDr1500

Tocash4500

[Halfofthegoodwillcreditedwithdrawn byoldpartners]Revaluationa/c Dr3000

Tostock a/c 1140

To furniturea/c 240

Toreserveforbad debtsa/c 540
To liabilityforbills discounted1080
[Entrypassed to decreasethe value ofassets or increasethevalue ofliabilities]
Buildingsa/c Dr 7500
Torevaluationa/c 7500
[Entrypassedtoincreasethevalueofbuilding]Rev
aluationa/c Dr 4500
ToA'scapitala/c1500

ToB'scapitala/c1500T
oC'scapitala/c1500
[Profit onrevaluationtransferredtooldpartners intheoldprofitsharingratio]

Balancesheet of A, B, Cand D as on 1stJune,1982

Creditors	Rs.	Cash	20,100
Billspayable	6,000	Stock(11400 -1140)	10,260
Liabilityforbills	3,300	Debtors 10800	
discounted	1,080	(-)Reserve 540	10,260
CapitalaccountsA	19,800	Furniture(2400-240)	2,160
CapitalaccountsB	15,600	Building	27,000
CapitalaccountsC	9,000		
CapitalaccountsD	15,000		
	69,780		69,780

RevaluationAccount ***(Fig.inRupees)***

ToStock	1,140	ByBuildinga/c	7,500
ToFurniture	240		
ToReserveforbad debts	540		
ToLiabilitiesforbillsdiscounted	1,080		
A'sCapitala/c1500			
B'sCapitala/c1500			
C'sCapitala/c1500	4,500		
(Profitonrevaluationcreditedtocapitala/c)			
	7,500		7,500

CashAccount ***(Fig.inRupees)***

ToBalanceb/d	600	ByA's Capitala/c	1,500
ToD’sCapitala/c	15,000	B'sCapitala/c	1,500
ToGoodwilla/c	9,000	C'sCapitala/c	1,500
		(halfof goodwillwithdrawn)	20,100
	24,600		24,600

	A	B	C	D		A	B	C	D

To Cash	1,500	1,500	1,500	-	ByBalanceb/d	16,800	12,600	12,600	---
ToBalance c/d	19,800	15,600	9000	15,000	ByCash a/c	---	---	---	15,000
					ByGoodwill a/c	3,000	3,000	3,000	---
					ByRevaluationa/c	1,500	1,500	1,500	---
	21,300	17,100	10,500	15,000		21,300	17,100	10,500	15,000

apitalAccounts

Case2

Ifthe partnersdecidenot to altertheassetsandliabilitiesexceptcash.

JournalEntries:

Cash a/c Dr 24,000

Togoodwilla/c 9,000

ToD'scapitala/c 15,000

[CashbroughtinbyD forhiscapitalandgoodwill]

2.Goodwill a/c Dr 9,000

ToA's capitala/c 3,000
ToB'scapitala/c 3,000
ToC'scapitala/c 3,000

[Goodwillbrought inbyD isdistributedtooldpartners]Dr

3.A'scapitala/c 1500
B'scapital a/c Dr 1500
C'scapital a/c Dr 1500
Tocash 4500

[Halfof thegoodwill withdrawn byold partners]

4.MemorandumRevaluationDr 4500
ToA's capitala/c 1500
ToB'scapitala/c 1500
ToC'scapitala/c 1500

[Profitonrevaluationdistributedtooldpartners]

5.A'scapitala/c Dr 1125
B'scapital a/c Dr 1125
C'scapital a/c Dr 1125
D's capitala/c Dr 1125
ToMemorandumRevaluationa/c

Profit revaluation account is written back by debiting all the partners capital accountintheir new profit sharingratio]

	A (Rs.)	B (Rs.)	C (Rs.)	D (Rs.)		A (Rs.)	B (Rs.)	C (Rs.)	D (Rs.)
ToCasha/c	1,500	1,500	1,500	-	ByBalancec/d	16,800	12,600	6,000	---
ToRevaluation a/c	1,125	1,125	1,125	1,125	ByCash a/c	---	---	---	15,000
ToBalance c/d	18,675	14,475	7,875	13,875	ByGoodwill a/c	3,000	3,000	3,000	---
					ByRevaluationa/c	1,500	1,500	1,500	---
	21,300	17,100	10,500	15,000		21,300	17,100	10,500	15,000

MemorandumRevaluationAccount

	Rs.		Rs.
ToStock	1,140	ByBuildings	7,500
ToFurniture	240		
ToProvision forbad debts	540		
ToProvisionforbillsdiscounted	1,080		
ToA'scapital a/c 1500			
ToB's capital a/c 1500			
ToC's capital a/c 1500	4,500		
Profitonrevaluation	7,500		7,500
ToReversalofentrieson credit side	7,500	ByReversal of entries onthe debtside	3,000
		ByA's capital a/c1125	
		By B's capital a/c 1125	
		By C's capital a/c 1125	
		By D's capital a/c 1125	4,500
	7,500	(Profit on revaluation is written back)	7,500

Balancesheet ason 1stJune, 1982

Liabilities	Rs.	Assets	Rs.

Creditors	6,000	Cash (600 +24000 -4500)	20,100
Billspayable	3,300	Debtors	10,800
CapitalAccounts		Stock	11,400
A-18675		Furniture	2,400
B-14475		Buildings	19,500
C -7875			
D-13875	54,900		
	64,200		64,200

Illustration2

Thefollowingisthebalancesheetof A,BandCshowingprofitsandlossesinthepr oportionof 6/14, 5/14 and 3/14 respectively.

	Rupees		Rupees
Creditors	18,900	Cash	1,890
Billspayable	6,300	Debtors	26,460
Generalreserve	10,500	Stock	29,400
A's capitala/c	35,400	Furniture	7,350
B'scapital a/c	29,850	LandandBuildings	45,150
C'scapital a/c	14,500	Goodwill	5,250
	1,15,000		1,15,000

Theyagreedtotake Dinto partnershipand givehim1/8 thshareonthefollowingterms:

1. That furniturebedepreciated byRs.920
2. Thatstock bedepreciated by10%
3. Thata provision ofRs.1320 bemadefor outstandingrepair bills
4. Thatthevalueoflandandbuildings beingappreciateu bebroughtupto Rs.59850.
5. Thatthevalue ofgoodwillbebroughttoRs.14070.
6. ThatDshould bringinRs.14700 ashiscapital.
7. That after making the above adjustments the capital accounts of the old partners areadjusted on the basis of the proportion of D's capital to his share in the business (i.e.)actualcash to bepaid offor broughtin bythe oldpartners as thecasemaybe.

Passthenecessaryjournal entriesand preparethebalancesheetof thenewfirm.

[B.Com(Hons)PartI,Delhi]

JournalEntries:

1. Revaluationa/c Dr 5180
   To furniturea/c 920
   Tostock a/c 2940
   Toprovision foroutstandingrepairs 1320
   [Beingthe assets(viz.furnitureandstock) revaluedand aprovisionismadeforoutstanding repairs]
2. Land andbuildinga/c Dr 14700
   ToRevaluation a/c 14700
   [Beingthe appreciationin thevalueofland andbuilding]
3. Revaluationa/c Dr 9520
   ToA'scapital a/c 4080
   ToB's capital a/c 3400
   ToC's capital a/c 2040
   [Profitonrevaluationcreditedtopartnerscapitala/c]

4. Goodwilla/c Dr 8820
ToA'scapital a/c 3780
ToB's capital a/c 3150
ToC's capital a/c 1890
[Valueof goodwillis raised toRs.14070 bycreditingthe old partnerscapitalaccountsin their profit sharing ratio]
5. Generalreservea/c Dr 10500
ToA'scapital a/c 4500
ToB's capital a/c 3750
ToC's capital a/c 2250
[Generalreserveisdistributed toold partnerson admissionofDI
6. A's capitala/c Dr 3660
B'scapital a/c Dr 3400
Tocash a/c 7060
[Excess amountinthecapitalaccounts ofA&Bwithdrawn]
7. Casha/c Dr 1320
ToC's capital a/c 1320
[CashbroughtinbyCtomeettheshortfall inhiscapitalaccount]

RevaluationAccount

	Rupees		Rupees
ToFurniture	920	ByLandandBuildings	14,700
ToStock	2,940		
ToProvisionforrepairs	1,320		
ToA'sCapital a/c4080			
ToB'sCapitala/c3400			
ToC's Capitala/c2040	9,520		
Profitonrevaluation	14,700		14,700

CapitalAccounts

	A (Rs.)	B (Rs.)	C (Rs.)	D (Rs.)		A (Rs.)	B (Rs.)	C (Rs.)	D (Rs.)
ToCasha/c	3,660	3,400	---	---	Bybalancec/d	35,400	29,850	14,550	---
ToBalance c/d	44,100	36,750	22,050	14,700	Bycasha/c	---	---	---	14,700
					ByRevaluationa/c	4,080	3,400	2,040	---
					Bygoodwilla/c	3,780	3,150	1,890	---
					Bygeneralreserve	4,500	3,750	2,250	---
					Bycash	---	---	1,320	---
	47,760	40,150	22,050	14,700		47,760	40,150	22,050	14,700

CashAccount

	Rupees		Rupees
ToBalanceb/d	1,890	ByA's capital a/c	3,660
ToD's capitala/c	14,700	ByB'scapitala/c	3,400
ToC'scapitala/c	1,320	ByBalancec/d	10,850
	17,910		17,910

Balancesheet ason………………..

Liabilities	**Rs.**	**Assets**	Rs.
Creditors	18,900	Cash	10,850
Billspayable	6,300	Debtors	26,460

Provisionforoutstanding		Goodwill	14,070
repairs	1,320	Stock(29400 -2940)	26,460
CapitalAccounts		Furniture (7350-920)	6,430
A-44100		Landandbuildings	59,850
B-36750			
C -22050			
D-14700	1,17,600		
	1,44,120		1,44,120

Calculationofcapitalbalances.

For1/8shareD's capitalis Rs. 14,700
A's capital(3/8) Rs.44,100
B'scapital(5/16) Rs. 36,750
C'scapital(3/16) Rs. 22,050

RETIREMENTOFAPARTNER

A partner of a firm may decide to retire due to various reasons like ill-health, old ageetc. He retires on the basis of retirement terms of a partner set out in the Partnership Deed.When a partner retires, the other partners enter into a fresh agreementand continue thebusiness.

Whenapartner retires, thefollowing accountingproblems areto be lookedinto.

1. Calculationofnewprofitsharingratioandprofitgainingratio.
2. Treatmentof goodwill.
3. Revaluationofassetsandliabilities.
4. Distributionofreserves/profitorlosses.
5. Adjustmentofcapitalaccountsof continuingpartners. Ascertaining amount payable to the retiring partner and the mode of payment of theamount.

1. **Calculation of new profit sharing ratio and profit gaining ratio of continuingpartners**

When a partner retires from a firm, the continuing partner may agree upon the new profitsharing ratio among themselves, otherwise they acquire the share of profit of the retiringpartner in their profit sharing ratio. Profit gaining ratios is the difference between new profitsharingratios and old profit sharing ratio ofold partners.

Case1

A,Band Carepartnerssharingprofitsandlossesintheratioof 4:3:3.Bretires.Calculatethenewprofit sharingratio, also calculateprofitgainingratio.

Solution

New profit sharing of A and C is 4:3 as there in no agreement on future profit sharing ratio, itis presumed the continuing partners purchase the retiring partner's share in their old profitsharingratio (i.e.) 4:3. Therefore,the profit gainingratiois also 4:3 betweenA:C.

Case2

A, B and C are partners and share profits and losses in the ratio of 3:2:2. B retires from thepartnership. A and C decide to share the future profits equally. Ascertain new profit sharingratioand profitgainingratio.

New profit sharing ratio between A and C is 1:1.Profitgainingratio for A=1/2– 3/7

=(7-6)/14=1/14

Profitgainingratio forB = 1/2 –2/7

=(7-4)/14=3/14

ProfitgainingratiobetweenA&Cis1:3.

2. GoodwillTreatment

Whenapartnerretiresfromafirm,theotherpartnersstandtogainashareofhisfutureprofits.So the retiring partner has to be compensated by way of extra credit for his share of goodwill.Thereare fourwaysfortreatinggoodwill at thetime ofretirement.Theyare

1. Goodwillisraised inthebooksforits fullvaluebycrediting allpartnerscapitalaccountin the old profitsharingratio.
2. Goodwill raised in the books as above is written off by debiting the capital accountsofthecontinuingpartners in thenew profit sharingratio.
3. Goodwillmayberaised in the booksonlyto theextent ofretiringpartner'sshareandis written off by debiting the continuing parterns' capital accounts in the profitsgivingratio.
4. Withoutraisinggoodwill,capitalaccountsofpartnersareadjusted for goodwill.

Example

A, B and C are partners in a firm sharing profits and losses in the ratio of 3:2:1. 'B'retires from the firm. The future profit sharing ratio of A and C is 2:1. The value of goodwillisestimatedatRs.42,000.Passentriesforthetreatmentofgoodwillineachofthe abovecases.**Case1**

Goodwill is raised in the books for its full value by crediting all partners' capitalaccountsintheirprofitsharingratio.Herethegoodwillaccountwillappearintheba lancesheetanasset.

Goodwilla/c Dr42000

ToA's capitala/c 21000

ToB's capitala/c 14000

ToC'scapitala/c 7000

[Goodwillisraised forits fullvalue bycreditingallthepartners’capitala/cintheoldratio]

Case2

Goodwillraisedandwrittenoff

a) Goodwilla/c Dr 42000

ToA'scapital a/c 21000

ToB's capital a/c 14000

ToC's capital a/c 7000

[Goodwillraisedtoitsfullvaluecreditingthecapitalaccountsintheoldratio]

b)A'scapitala/c Dr 28000

B'scapital a/c Dr 14000

Togoodwill a/c 42000

[Goodwillraised iswritten offbydebitingthe capitalaccounts of continuingpartners inthenewratio]

Case3

Goodwillraisedto theextentoftheretiringpartnersshareand writtenoff.

Goodwilla/c Dr 14000

To B's capital a/c

14000[Goodwillraisedtotheextentofretiringp

artner'sshare]

a) A'scapitala/c

Dr 7000C'scapital a/cDr 7000

Togoodwill a/c 14000

[Goodwillraisediswrittenoffintheprofitgivingratio]

Case4

Withoutraisinggoodwillaccountinthebook,whenadjustmentfor goodwillismade.

A's capital a/c Dr 7000

C'scapitala/cDr7000

ToB's capital a/c 14000

[Retiring partner's capital account is credited with his share of goodwill bydebitingthe capital accounts of continuingpartners in theirprofit sharingratio]

3. Revaluationof Assetsand Liabilities

When a partner retires the assets and liabilities are revalued so that he does not suffer orgainbecauseofover/understatedassetsandliabilities.Profitorlossarisingonthereval uationof assets and liabilities is distributed to all partners in their profit sharing ratio. In case thecontinuing partners decide to show the value of assets and liabilities in the old value and notintherevalued value, theyprepareMemorandum Revaluation Account.

4. DistributionofReserves/ProfitsorLosses

Anybalanceofreserves/profitsorlossesonthedateofretirementofapartnerisdistrib utedto all partners (including the retiring partner) in the old profit sharing ratio. The followingentriesareused in this regard.

For distribution of reserves/profitsReserves/Pro fit&Loss a/c Dr

To all partners capital a/c (individually)Fordistribution of losses

All partners capital account (individually)DrToprofit & Loss (Dr) a/c

5. Adjustmentsofcapitalaccountsofcontinuingpartners

Thecontinuingpartnersmaydecidetohavetheirbalanceofcapitalaccountsinpropo rtiontotheirprofitsharingratio.Insuchacasetheybringincashorwithdrawcashinorderto maketheircapitals in proportion to theprofit sharingratio.

6. Ascertainingtheaccountpayabletotheretiringpartnerandthe modeofpaymentof the amount

The capital account of the retiring partner is prepared on the date of retirement to arrive attheamount dueto him. Theusualcredit entries inhis account are:

1. Creditbalanceofhiscapitala/c
2. Creditbalanceofhiscurrenta/c
3. Hisshareof goodwill
4. Hisshareof accumulatedprofitsandreserves
5. Hisshareofprofit onrevaluation
6. Hisshareof profitupto thedate ofretirement

7. Interestoncapitaluptotherateofretirement

8. His share of joint

life

policyTheusualdebitentriesin

theaccountare

1. Debitbalanceofhiscapitalaccount
2. Debitbalanceofhiscurrentaccount
3. Hisshareof accumulatedlosses
4. Hisshareof loss onrevaluation
5. Hisshareoflossuptothedateofretirement
6. Hisdrawingsuptothe dateofretirement
7. Interestonhisdrawingsuptothedateofretirement

The account, after passing all relevant entries, is closed on the date of his retirement,and the balance (usually credit) is transferred to his loan account. Later the loan account ispaidoffas per thetermsof retirement.

ILLUSTRATION: 3 C,PandSwerepartners sharingprofits2/5,3/10and3/10respectively.Their balancesheeton 31st December 1983 was as follows.

Liabilities	Rs.	Assets	Rs.
CapitalAccounts		Building	18,000
P16000		Plant	14,000
B12000		MotorCar	4,000
C 10000	38,000	Stock	10,000
Reserve	5,000	Debtors 7000	
Billspayable	2,000	(-)Provision1000	6,000
Creditors	8,000	CashatBank	1,000
	53,000		53,000

Pretireson thatdateon theterms:

(a) The goodwill ofthefirm isto bevaluedat Rs.7000

(b) Stock and buildingareto be appreciated by10%

(c) Plant and motor car aretobe depreciated by10%

(d) Liabilityfor thepaymentof gratuitytoworkers Rs.2000 isnot recordedinthebooks,

butthesameis tobeprovidedfor

(e) Provision for bad debts is no morenecessary

(f) Itisdecidednotto maintaingoodwillaccountinthe books

(g) The amount payable to P is to be paid in 3 equal annual instalments beginningfrom

Youarerequiredtoprepare

(i) Revaluationaccount

(ii) Partners'capitalaccounts

(iii) Newbalancesheetof M/s.Land S

(iv) P'sloan accountfor 1984

Solution

RevaluationAccount

	Rs.		Rs.
Dec.31,1983		Dec.31,1983	
ToPlant	1,400	ByStock	1,000
ToMotor Car	400	ByBuildings	1,800
To Liabilityforpayment ofgratuity	2,000	ByProvision forbad	2,000
	3,800		3,800

[Note:Thereisno profitor losson revaluation]

CapitalAccounts

	C (Rs.)	P (Rs.)	S (Rs.)		C (Rs.)	P (Rs.)	S (Rs.)
Dec.31,1983				Dec.31,1983			
ToGoodwill(goodwill writtenback)	4,000		3,000	ByBalanceb/d	16,000	12,000	10,000
ToBalance c/d	16,800	----	10,600	ByGoodwill	2,800	2,100	2,100
ToP'sloana/c	----	15,600	----	ByReserve	2,000	1,500	1,500
	20,800	15,600	13,600		20,800	15,600	13,600

Balancesheetof M/s.LandS ason 31-12-1983

Liabilities	Rs.	Assets	Rs.
CapitalAccount		Buildings	19,800
C16,800		Plant	12,600
S10,600	27,400	MotorCars	3,600
P'sloanaccount	15,600	Stock	11,000
Billspayable	2,000	Debtors	7,000
Creditors	8,000	CashatBank	1,000
Liabilityforpayment of gratuity	2,000		
	55,000		55,000

P'sloanaccountfor1984

	Rs.		Rs.
Jan. 1, 1983		Jan. 1, 1983	
To Cash	5,200	ByBalanceb/d	15,600
Dec.31,1984		Dec.31,1984	
ToBalance c/d	11,440	ByInterest	1,040

Illustration4

The Balance sheet of X, Y and Z, sharing profits in proportion to their capitals was asfollowson December 31,1975.

Liabilities	Rs.	Assets		Rs.
Sundrycreditors	27,600	CashatBank		22,400
CapitalAccounts		Sundrydebtors	20000	
X-90000		(-)Reservefor bad Debts	400	19,600

Y-60000 Z-30000	1,80,000	Stockintrade Machinery Land andbuilding	32,000 34,000 1,00,000
	2,07,600		2,07,600

Yretiresandthefollowingadjustmentofthe assets andliabilitieshavebeenagreeduponbeforetheascertainment ofthe amount payable bythe firm to Y.

1. Insurancechargedtoprofitandlossaccountincludesunexpiredinsura nceofRs.300.

2. Provisionforbad debts toberaised to 5%.

3. Landandbuildingstobeappreciatedby20%.

4. Abill forrepairsforRs.5300is dueonDecember 31,1975.

5. Goodwill of the firm is fixed at Rs.43200 and Y's share of the same is to beadjustedinto theaccountofXandZwhoaregoingto sharefutureprofitsin theproportionof3/4and 1/4respectively,without raisingthegoodwillaccount.

6. That the entire capital of the firm as newly constituted is fixed at Rs.112000betweenX andZinproportionof 3/4and1/4eitherwithdrawingorcontributingincash bythecontinuingpartners as thecasemaybe.

7. Theamount duetoY isto treated ashis loan account.

Passjournalentries togiveeffectto theaboveand preparethe balancesheet ofXandY.

Journalentries:

1.Revaluationa/c	Dr	5900	
Toreserveforbad debts			600
Tooutstandingbillforrepair			5300

[Reserve for bad debts is increased by Rs.600 and the outstanding bill for repair isbroughtto book on Y's retirement]

2. Landandbuildings a/c	Dr	20300	
ToRevaluation a/c			20000
Tounexpired insurance			300

[Landandbuildingsrevaluedupwardsby20000 andunexpiredinsurance broughttobooks]

3. Revaluationa/c	Dr	14100	
ToX'scapital a/c			7200
ToY'scapital a/c			4800
ToZ'scapital a/c			2400

[Profit onrevaluationtransferredtooldpartnersintheirprofitsharingratioviz.3:2:1]

4. X's capitala/c	Dr	10800	
Z'scapitala/c	Dr	3600	
Y'scapital a/c			14400

[Y's share of goodwill in the firm is adjusted by debiting the continuing partners'accountsin their futureprofit sharingratio]

5. X's capitala/c Dr 2400
Z'scapitala/c Dr 800
Tobank 3200
[Cashwithdrawnbythe continuingpartners inexcessof their capital]
6. Y's capitala/c Dr 79100
ToY's loan a/c 79100
[Y'scapitalaccountistransferredtoY'sloanaccountonhisretirement]

RevaluationAccount

Dec.31,1975		Dec.31,1975	
ToReserveforbad debts	600	ByLandandbuildings	20,000
ToOutstandingbillsforRepair	5,300	ByUnexpired insurance	300
ToX'sCapital a/c7200			
ToY'sCapital a/c 4800			
ToZ'sCapitala/c2400	14,400		
(Profitonrevaluation)	20,300		20,300

CapitalAccounts

	X (Rs.)	Y (Rs.)	Z (Rs.)		C (Rs.)	P (Rs.)	S (Rs.)
Dec.31,1983				Dec.31,1983			
ToGoodwill	10,800	---	3,600	ByBalanceb/d	90,000	60,000	**30,000**
ToY'sloana/c	2,400	79,200	800	ByRevaluation a/c	7,200	4,800	2,400
ToBalance c/d	84,000	---	28,000	ByX'sCapital a/c	---	10,800	---
				ByY's Capital a/c	---	3,600	---
	97,200	79,200	32,400		97,200	79,200	32,400

Cashat Bank

	Rs.		**Rs.**
Dec.31,1975		Dec31,1975	
ToBalanceb/d	22,000	ByX's Capital a/c	2,400
		ByY's Capital a/c	800
		ByBalancec/d	18,800
	22,000		22,000

Balancesheet ofM/s. Xand Zason 31-12-1975

	Rs.		**Rs.**
Capitalaccounts		Cashatbank	18,800
X 84000		Unexpectedinsurance	300
Y 28000	1,12,000	Sundrydebtors 20000	
Y's Loanaccount	79,200	Less:Reserve forbad debts 1000	19,000
Outstandingbills forrepair	5,300	Stockintrade	32,000
Sundrydebtors	27,600	Machinery	34,000
		LandandBuildings	1,20,000
	2,24,100		2,24,100

Illustration5

A, B and C are partners in a firm. On 31-12-1990 B relieves from the firm. Aftermaking all adjustments the balance due to him is Rs.9705. On 31-12-1990 Rs.705 is paid tohim. The continuing partners agree to pay the balance in 3 annual instalments charging 5%interest,startingfrom 31-12-1991. Writeup his loanaccount,

1. Iftheloanamountispaidin3equalinstalmentstogetherwithinterest
2. Iftheloanamount ispaidin 3equatedinstalments.

Solution

(1) Iftheloan ispaidin3equalinstalmentstogetherwithinterest

B'sLoan Account (Fig.inrupees)

1990,Dec.31		1990,Dec.31	
ToCash	705	ByB's Capitala/c	9,705
ToBalancec/d	9,000		
	9,705		9,705
1991		1991	
Dec.31ToCash	3,450	Jan.1 ByBalanceb/d	9,000
Dec.31ToBalancec/d	6,000	Dec.31ByInterest a/c	450
	9,450		9,450
1992		1992	
Dec.31ToCash	3,300	Jan.1 ByBalanceb/d	6,000
Dec.31ToBalancec/d	3,000	Dec.31ByInterest	300
	6,300		6,300
1993		1993	
Dec.31ToCash	3,150	ByBalance	3,000
		ByInterest	150
	3,150		3,150

(2) Iftheloan is paid in3 equatedinstallments.

B'sLoan Account (Fig.inrupees)

1990,Dec.31		1990,Dec.31	
ToCash	705	ByB's Capitala/c	9,705
ToBalance c/d	9,000		
	9,705		9,705
1991		1991	
Dec.31Tocash	3,304.87	Jan.1 ByBalanceb/d	9,000
Dec.31ToBalance c/d	6,145.13	Dec.31ByInteresta/c	450
	9,450.00		9,450
1992		1992	
Dec.31ToCash	3,304.87	Jan.1 ByBalanceb/d	6,145.13
Dec.31ToBalance c/d	3,147.52	Dec.31ByInterest	307.26
	6,452.39		6,452.39
1993		1993	
Dec.31ToCash	3,304.87	ByBalanceb/d	3,147.57
		ByInterest	157.30
	3,304.87		3,304.87

[Annuity table shows that Re.1can buy an annuity of 0.367208 at 5% for 3 years. Thereforetheequatedinstallmentis Rs.3304.82 (9000 x0.367208)]

Deathof aPartner

When a partner dies, the partnership comes to an end, but other partners may carry onthe business by entering into a new agreement. The amount due to the deceased partner isascertained as per the terms of Partnership Deed and as similar lines when a partner retires.Theamountduetothedeceasedpartneronthedateofdeathispaidtotheexecutorso fthe deceasedpartner,immediatelyorininstalments.Retirementofapartnerisaplannedeven tandusuallyapartnerwillretireonthedateofclosingoftheaccountsofthefirm.Ontheothe rhanda partner may die on any date during the accounting period. So he is entitled to his share ofprofit upto the date of death. The profit for the accounting period during which a partner dies,is ascertained on the date of death, (without closing the books) on the basis of average profitsof past years, which is set in the Partnership Deed. Then his shares of profit upto the date ofdeath is arrived at and credited in his account. In case of death, treatment of goodwill,revaluationofassetsandliabilities,distributionofreserves/profitsetcaredone onsimilarlineswhen a partner retires. But goodwill is valued on the basis of the terms provided in thePartnership Deed in this regard. Moreover Sec.37 of the Partnership Act, is a relevant sectionin case of death, which says, the executors of the deceased partners would be entitled, at theirchoice, to interest at 6% p.a. on the amount due from the date of death to the date of paymentor to that portion of profit which is earned by the firm with the help of the amount due to thedeceasedpartner. Aretiringpartneris also eligible forsuchabenefit under this section.

Another important accounting aspect in case of death of a partner is the treatment ofJointLifePolicy.Thefirmtakesalifeinsurancepolicyonthejointlivesofitspartnersino rderto pay off the executors of the deceased partner without affecting the financial position of thefirm.

AccountingforJointLife Policyis donein threedifferent ways.Theyare

1. Premiumpaidistreatedasanexpense
2. Joint life policy is shown in the balance sheet at its surrender value by treating it is an asset
3. Joint life policy is treated as an asset and a reserve viz. joint life policy reserve is maintained

1. Premiumpaid istreatedasanexpense

When premium paid is treated as an expense it is written off at the end of the year, bytransferring it to Profit and Loss Account. In case a partner dies, the policy amount is creditedto all partners including the deceased partner in their profit sharing ratio. The relevant entriesare:

When premium is paid Premium on JLP a/c Dr -

To Bank/cash -

[Payment of JLP premium]

At the end of the year the premium account is closed by transferring it to Profit & loss a/c.

a) Profit and loss account Dr -

To Premium on JLP a/c -[Profit and loss account is cleared)

On the death of a partner, the policy amount receivable is credited to all partners in their profit sharing ratio.

Insurance Co. a/c Dr -

To Partners' capital a/c (individually) -

[Policy amount receivable is distributed to all partners in their profit sharing ratio] When policy amount is received, the following entry is made:

Bank a/c Dr -

To Insurance Co. -

[Receipt of policy amount from Insurance Co.]

2. JLP is treated as an asset at its surrender value

When JLP is treated as an asset, then the following entry is passed at the time of payment of JLP premium

JLP a/c Dr -

To Bank a/c -

[Payment of premium is debited to JLP a/c and it is treated as an asset]

At the end of the year, the amount in excess of surrender value is transferred to profit and loss account. The relevant entry is

Profit and loss a/c Dr

To JLP a/c -

[Premium paid in excess of surrender value is treated as loss and transferred to profit and loss a/c]

So every year joint life policy account appears in the balance sheet at its surrender value. On the death of a partner the policy amount in excess of the surrender value is again and is distributed to all partners in their profit sharing ratio. The relevant entries are

a) Insurance Co. a/c Dr -

To JLP a/c

[Amount due by the insurance company on the death of a partner]

b) JLP a/c Dr -

ToAllpartners'capital a/c(individually) -

[BalanceofamountintheJLP a/cisdistributedtoallpartners intheirprofitsharingratio]

c) Banka/cDr-

To InsuranceCo.a/c

[Receiptofmoneyfromthe InsuranceCompany]

3. **Joint Life Policy is treated as an investment and a reserve viz. JLP reserve, ismaintained**

Therelevantentriesare

a) Joint lifepolicya/c Dr -

ToBank -

[Paymentofpremium]

b) Profitandlossa/c Dr-

ToJLPreservea/c

[Anamountequaltothepremiumpaidisdebitedtoprofitandlossaccountandajoint lifepolicyreserveaccount is created]

Then JLP account and JLP reserve account are mutually adjusted so as to leave abalanceineachaccountequaltothesurrendervalueofthepolicy.Thefollowingentryispassedforthis:

Joint lifepolicyreserve a/c Dr -

To Jointlifepolicyaccount

[Mutual adjustment entry so that both the accounts show a balance which is equal to thesurrendervalue]

Theaboveentriesarepassedeveryyear.Onthedeathof apartner,thebalanceof jointlife policy reserve account is closed by transferring it to Joint Life Policy Account, and theamountreceivedasthepolicyamountiscreditedtoallpartnersintheiroldprofitsharingratioandjoint lifepolicyaccount is also closed. Thefollowingentriesarepassed.

a) Jointlifepolicyreserve account Dr-

To joint lifepolicyaccount

[OnthedeathofapartnerJLPreserveisclosedbytransferringittoJointlifepolicyaccount]

b) InsuranceCo.a/c Dr -

To Jointlifepolicya/c

[Policyamount dueon thedeath ofapartner]

c) Joint lifepolicya/c Dr-

Toallpartnerscapitala/c(individually) -

[Joint lifepolicyaccountisclosed bytransferringit toall partners'capitala/c intheirprofitsharingratio]

d) Bank a/c Dr-

ToInsuranceCo.a/c –

[Receipt ofpolicyamountfromthe InsuranceCo.]

Illustration6

X, Y and Z carried on business in partnership, profits being divisible to X 1/2; Y 1/3;Z1/6. Thebalancesheeton 31-12-1986 showedtheir capitals to be

X-Rs. 20,000; Y -Rs.15,000; Z-Rs.10,000

On 31-03-1987 X died and you are asked to prepare the executor's account of Xhavingregard to the followingfacts:

1. The firm insured the partners' life severally X for Rs.10000, Y for Rs.7500 and Zfor
   Rs.5000. The premiums have been charged to profit and loss account and thesurrender value on 31-03-1987 amounted in each case to one-half of the sumassured.
2. Capitalscarriedinterestat6%p.a.
3. X'sdrawings from 01-01-1987 to thedate ofdeath wereRs.3500.
4. X's share of profits for the portion of the current financial year for which he livedwas
   to be taken at the sum. Calculate on the average of the last three completed yearsand goodwill was to be raised on the basis of two years purchase of the averageprofits of those three years. The annual profits of last three years were Rs.7500,Rs.8000and Rs.9000 respectively.

Workings:X'sclaim

(1) Jointlifepolicies

X's policy-Rs.10000; 1/2of 10000 =Rs.5000

YandZpolicies Surrender value =1/2 (7500+5000)

=1/2x12500

=6250

X'sshare =6250 x1/2

=Rs.3125

(2) Interestoncapital

Rs.20000x6/100x3/12=300

(3) Shareof profit

X'sshareofprofit for3monthson theaverageprofits

oflast3yearsAverageprofit =(7500 +8000 +9000)/3

=Rs.8167

X'sshare =8167 x1/2x1/4

=Rs.1021

(4) Shareof goodwill

Averageprofits x2 =8167 x2

=16334

X's share of

goodwill =

Rs.8167(16334x1/

2)

Solution

Executor'sAccountofX

	Rupees		Rupees
March31,1987		March31,1987	
Todrawings	3,500	Bybalanceb/d	20,000
Tobalance c/d	24,113	Byjointlifepolicy	5,000
		Byinterest oncapital	300
		Bygoodwill	8,167
		Byprofit and loss suspensea/c	1,021
		ByYandZ'scapitala/c	3,125
		(Shareof surrendervalueof X andYpolicies)	
	37,613		37,613

A, B and C sharing profits and losses in the ratio of 5:3:2 took out a Joint life policyfor Rs. 1,00,000 paying an annual premium of Rs.5000 starting from 1st January, 1990. Thesurrendervalue of the policywas as follows:

1990 -NIL

1991 -Rs.1000

1992 -Rs.2500

1993 -Rs.4000

1994 -Rs.6000

Bdiedon25thMay,1994andthepolicymoneywasreceivedon30thJune,1994. Showtheaccount relatingto joint lifepolicyunder various treatments.

Solution

Case1 When premiumiswrittenoff:

Profitand LossAccount

Dr. Cr.

1990Dec.,31	Topremium on joint lifepolicy	5000
1991Dec.,31	Topremium on joint lifepolicy	5000
1992Dec.,31	Topremium on joint lifepolicy	5000
1993Dec..31	Topremium on joint lifepolicy	5000
1994Dec.,31	Topremium on joint lifepolicy	5000

JointLifePolicy Account

1994 June, 30		1994 June, 30	
TotransfertocapitalA/cA B C	50,000 30,000 20,000	ByBank (AmountreceivedfromInsuranceCo.)	1,00,000
	1,00,000		1,00,000

Case2 Surrendervalueistreatedasanasset

	Rs.		Rs.
1990 Jan. 1		1990 Jan. 1	
ToBank	5,000	ByProfitandLossa/c	5,000
	5,000		5,000
1991 Jan. 1		1991Dec.31	
ToBank	5,000	ByProfit andLossa/c	4,000
		ByBalancec/d	1,000
	5,000		5,000
1992 Jan. 1		1992Dec.31	
ToBalanceb/d	1,000	ByProfit andLossa/c	3,500
ToBank	5,000	ByBalancec/d	2,500
	6,000		6,000
1993 Jan. 1		1993Dec.31	
ToBalanceb/d	2,500	ByProfit andLossa/c	3,500
ToBank	5,000	ByBalancec/d	4,000
	7,500		7,500
1994 Jan. 1		1994 June 30	
ToBalanceb/d	4,000	ByBank	1,00,000
ToBank	5,000	Amountreceived from	
	7,500	InsuranceCo.)	
1994 June 30			
ToTransfertocapitalaccounts			
A	45,500		
B	27,300		
C	18,200		
	1,00,000		1,00,000

Case3
PremiumtobewrittenoffthroughJointLifePolicyreserveaccountJointLifePolicyAccount

JointLifePolicy Account

	Rs.		Rs.
1990 Jan. 1		1990 Jan. 1	
ToBank	5,000	ByProfitandLossa/c	5,000
	5,000		5,000
1991 Jan. 1		1991Dec.31	
ToBank	5,000	ByJoint LifePolicyReserve	4,000
	5,000	ByBalancec/d	1,000

1992 Jan. 1		1992Dec.31	
ToBalanceb/d	1,000	ByJointLifePolicyReserve	3,500
ToBank	5,000	ByBalancec/d	2,500
	6,000		6,000
1993 Jan. 1		1993Dec.31	
ToBalanceb/d	2,500	ByJointlifepolicyreserve	3,500
ToBank	5,000	ByBalancec/d	4,000
	7,500		7,500
1994 Jan. 1		1994 June 30	
ToBalanceb/d	4,000	ByBank	1,00,000
ToBank	5,000	ByJointlifepolicyreserve	9,000
	7,500		
1994 June 30			
ToTransfertocapitalaccounts			
A	50,000		
B	30,000		
C	20,000		
	1,09,000		1,09,000

JointLifePolicyReserveAccount

	Rs.		Rs.
1990Dec.31		1990 Jan. 1	
To Joint Life Policy a/c	5,000	By Profit and Loss a/c	5,000
	5,000		5,000
1991 Dec. 1		1991 Dec. 31	
To Joint Life Policy a/c	4,000	By Profit and Loss a/c	5,000
To Balance c/d	1,000		
	5,000		5,000
1992 Dec. 31		1992 Dec. 31	
To Joint Life Policy a/c	3,500	By balance c/d	1,000
To Balance c/d	2,500	By Profit and Loss a/c	5,000
	6,000		6,000
1993 Dec. 31		1993 Dec. 31	
To Joint Life Policy a/c	3,500	By Balance b/d	2,500
To Balance c/d	4,000	By Profit and Loss a/c	5,000
	7,500		7,500
1994 Dec. 31		1994 June 30	
To Joint Life Policy a/c	9,000	By Balance b/d	4,000
		By Profit and Loss a/c	5,000
	9,000		9,000

UNIT- 4 DISSOLUTIONOFA FIRM

Dissolution of a firm means the dissolution of partnership between all the partners inthefirm.Incaseofadmission,retirementordeathofapartner,thepartnershipisdissolved,buttheremainingpartnerscontinuethebusinessafterenteringintoanewagreement.Whenafirmis dissolved there will not be any business afterwards. The assets are disposed off, liabilitiesarepaidand all accountsareclosed, bysettlingthepartners'capital accounts.

Dissolutionofafirmtakesplaceinthe followingcases:

1. DissolutionbyAgreement.

Afirmisdissolvedincase

a) when allpartners give consentforitsdissolution,or

b) asper thetermsofagreement.

2. CompulsoryDissolution:

Afirm is compulsorydissolved on thefollowinggrounds:

a) Whenallthepartnersorallexceptingonepartner becomesinsolvent

b) Whenall partners exceptingonedecide to retirefrom thefirm

c) Whenallthepartnersor allexceptingarepartner dies

d) Whenthebusinessbecomesillegal.

3. Dissolutiononthe happeningofacertainevent:

a) Expiryof theperiod for whichthefirm was formed

4. Whentheventureorprojectis completed Dissolution bycourt:A court mayorder a partnershipfirm to bedissolved on asuitfiledbyapartner in thefollowing cases.

a) Where apartnerbecomes insane.

b) Whereapartner becomes permanentlyincapable ofdoingbusiness.

c) Whereapartner willfullyand consistentlycommits breach of agreementrelatingto the management of the firm.

d) Whereapartner'sconduct is likelyto adverselyaffectthebusinessto the firm.

e) Where apartnertransfersallhisshareto athird party.

f) Wherethebusiness of the firmcan't be carriedout exceptat aloss.

g) Onanyothergroundswhichthe courtthinks justand equitable.

Settlement of AccountsRules

In case of dissolution, business ceases to exist, and as such, assets are to be disposedoffandaftersettlementofallitsclaims,accountsaretobeclosed.AsperSec.48of the IndianPartnershipAct, thefollowingrulesare to be observed:

1. Losses are to be paid first out of profits, next out of capital, and lastly by thepartners,individually, inproportion totheirprofitsharingratios.
2. The assets of the firm, including the contribution made by the partners tomakeup the deficiencyofcapital are to beappliedin thefollowingorder:

   a) to paydebts of thefirm to third parties.

   b) topaypartners'loansandadvances.

   c) to paycapital accounts of thepartners.

In case after paying all the above claims, if any surplus is there, it should be distributedamongthe partners in theirprofit sharingratios.

Paymentoffirm'sdebtsand personaldebts

The assets of the firm are applied to pay the debts of the firm first and if any surplus isleft it is used to pay the personal debts. Likewise, personal asset of a partner is applied to paypersonaldebts and ifanysurplusis left it will beapplied to paythe debtsofthe firm.

AccountingTreatment

When a firm is dissolved all accounts are to be closed. For this purpose a new accountcalled 'Realization Account' is opened. All assets except cash is transferred to this account.Similarlyalloutsideliabilitiesaretransferredandclosed.When assetsarerealizeditispassedthroughthisaccount,likewisewhenliabilitiesarepaiditispassedthroughthebooks.Profitorlossonrealizationofassetsandsettlementofliabilitiesshownintheaccountaredistributedtoall partners in their profit sharing ratio. Partners' loan account is settled separately and closed.Reserves and profit and loss accounts are transferred to capital account of all partners in theirprofit sharing ratio and closed. Then capital accounts of partners are balanced and paid off.CashAccountisautomaticallyclosedwhenalltheentriesaffectingthecashaccountareposted.**JournalEntries**

1. To transfer all assets (except cash and bank) at their

   book valuesRealizationa/c Dr-

   ToAssetsaccount (individually)–

   [Note:Ifthereisaprovision forbaddebts,DebtorsAccount shouldbetransferredat grossamount.Provision forbad debtsisto betreated likean outsiderliability]

2. To transfer outsiders liability at their book

valueOutsidersliabilitya/c Dr -

ToRealizationa/c

3. Whenassetsaresold

Cash/Banka/c Dr -

ToRealizationa/c

4. Whenapartnertakes overanasset

Partnerscapital a/c Dr -

ToRealization a/c

5. Whenliabilitiesarepaid

Realizationa/c Dr -

ToBank/cash a/c

6. When aliabilityistakenover byapartner

Realizationa/c Dr

Topartners'capitala/c

7. Foranyunrecordedassetsold

Bank/casha/c Dr

ToRealization a/c

8. For anyunrecordedliabilitypaidbyfirm

Realizationa/c Dr

ToBank/cash a/c

9. Forexpensesof realization

Realizationa/c Dr

ToBank/cash a/c

10. If apartnerpaystherealizationexpensesonbehalfofthefirm

Realizationa/c Dr

Topartners'capitala/c

At this stage realization account is to be closed and profits or losses on realization is to betransferredto partners capital accountin theirprofit sharingratio.

11. For transfer of profits on realizationRealizationac

count Dr

ToPartners'capitala/c(individually)

12. Fortransfer oflosses onrealizationPartners'capitala/c Dr

ToRealizationa/c

13. Forpaymentofpartners'loanaccount

Partners'loanaccount DrToBank/cash a/c

14. Fortransferringaccumulatedprofits/reservestopartners'capitalaccountsintheirprofitsharingratio.

Profit&loanaccount(or)reserves Dr

Topartners'capitalaccount(individually)

15. For transferring accumulated losses (debit balance of profit and loss account) topartnerscapital account.

Partners'capitalaccount Dr -

(individually)ToProfitandLossa/c

16. Fortransferringcurrentaccountofpartnerstotheircapitalaccounts

a) Ifithas creditbalance

Partnerscurrenta/c Dr

ToPartners'capitalaccount

b) Ifithasdebitbalance

Partners capital A/c Dr.

To Partner's current a/c

17. Lastlycapitalaccountsofpartners areclosed

a) Ifithasacreditbalance

Partners'capitalaccount DrToCash/Bank a/c

a.If ithasadebitbalance

Cash/Banka/c Dr

Topartners'capitala/c

[Cash/Bankaccountwill getautomaticallyclosed ifallentrieseffectingcash/bankareposted]

ILLUSTRATION

PandQ arepartnerssharingprofitsand lossesintheratioof3:1. Theirbalancesheetason31-12-1992is given below.

BalanceSheet of M/sP and Qas on 31-12-92

Liabilities		Assets	
Sundrycreditors	35,000	Cashatbank	10,000
Mrs.P'sloan	12,000	Stockintrade	8,000

Q'sloan	18,000	Sundrydebtors 25000	
Reservefund	6,000	LessProvision 1000	24,000
P'scapital	10,000	Fixturesandfittings	2,000
Q'scapital	5,000	Machineryand plant	25,000
		Investments	9,000
		Profitandlossaccount	8,000
	86,000		86,000

Thefirm wasdissolved on31-12-1992 andthefollowingwasthe results.

(a) P took over investments at an agreed value of Rs.10000 and agreed to pay off the loanto Mrs. P.

(b) Theassetsrealized thefollowing:-

Stock Rs.7000

Debtors Rs. 22000Fixturesandfittings Rs. 1000

MachineryandPlantR s.23000

(c) ExpensesofrealizationamountedtoRs.875

(d) Thesundrycreditorswerepaid offless 21/2%discount.

Journalize the entries to be made on the dissolution and show Realisation account, Bankaccountand Partner's capital accounts.

Solution:

Journalentries

1992Dec.31

1.Realization a/c Dr 69000

Tostock-in-tradea/c 8000

To sundrydebtors 25000

Tofurnitureandfittings 2000

To machineryand plant 25000

Toinvestments 9000

[Variousassetstransferredtorealisationaccountandclosedondissolution]

2. SundryCreditors Dr 35000

Mrs.P's Loan Dr 12000

Provisionfordoubtful debts Dr 1000

ToRealisation a/c 48000

[Variouscirculationsand provisionfordoubtfuldebtstransferredtorealizationaccount closed]

3. Reservefund a/c Dr 6000

ToP's capitala/c 4500

ToQ'scapital a/c 1500

[Thereservefundtransferred topartners'capital accountsintheir profitsharingratioandclosed]

3.P'scapitala/c Dr. 6000

Q's capitala/c Dr. 2000

Toprofit and loss account 8000

[Profitandloss accountisclosed bytransferringtothecapital accountofPandQ]

4. Banka/c Dr 53000

Torealisation a/c 53000

(Amountrealizedfromsaleofassets)

5. P'scapitala/c Dr 10000

Torealization a/c 10000

[Investments takenoverbyPat an agreed valueofRs.10000]

6.Realization a/c Dr 875

ToBank 875

[Expensesonrealisation]

7.Realizationa/c Dr 34125

Tobank 34125

[Sundrycreditors paid less21/2 discount]

8.Realization a/cDr 12000

ToP's capital a/c 12000

[Mrs.P'sloan agreed tobe paid byP]

9. P'scapitala/c Dr 3750

Q's capitala/c Dr 1250

Torealization a/c 5000

[Loanonrealizationtransferredtopartners'capitalaccountintheircapitalratio]1992Dec.31

Q'sloan a/c Dr 18000

Tobank a/c 18000

[PaymentofQ'sloan]

P'scapitala/c Dr 6750

Q's capitala/c Dr 3250

Tobanka/c 10000

[Finalpaymentofpartnersondissolution]

RealizationAccount

1992Dec.31	Rs.	1992Dec.31	Rupees
ToStock-in-trade	8,000	BySundrycreditors	35,000
ToSundrydebtors	25,000	ByMrs. P's loan	12,000
ToFurniture &fittings	2,000	ByProvisionforbad debts	1,000
ToMachinery&plant	25,000	ByBank (assetsrealization)	53,000
ToInvestments	9,000	ByP's Capital (Investments)	10,000
ToBank	34,125	By P's Capital a/c 3750By Q's capital a/c	
ToBank (expenses)	875		

ToP'scapital (Mrs.P'sloan)	12,000	1250(Lossonrealization)	5,000
	1,16,000		1,16,000

CapitalAccounts

	P. (Rs.)	Q. (Rs.)		P. (Rs.)	Q. (Rs.)
Dec.31,1992			Dec.31,1992		
ToProfit andlossa/c	6,000	2,000	ByBalanceb/d	10,000	5,000
ToRealization a/c	10,000	---	ByReservefund	4,500	1,500
(investmenttaken)			ByRealization a/c	12,000	---
ToRealization(loss)	3,750	1,250	(Mrs.P'sloan)		
ToBank	6,750	3,250			
	26,500	6,500		26,500	6,500

Q'sloan account

1992Dec.31	Rs.	1992Dec.31	Rupees
ToBank	18,000	ByBalanceb/d	18,000
	18,000		18,000

BankAccount

1992Dec.31	Rs.	1992Dec.31	Rupees
ToBalance	10,000	ByRealization	34,125
ToRealization	53,000	ByRealization(expenses)	875
(assetsrealization)		ByQ's loan	18,000
		ByP'scapitala/c	6,750
		ByQ's capital a/c	3,250
	63,000		63,000

CapitalAccounts

Dissolution -Insolvencyofa partner

If at the time of dissolution, a partner of a firm having debit balance in his capitalaccount becomes insolvent and could not pay the deficiency in his capital account, then thefirm suffers a loss. This loss (due Ito insolvency of a partner) is a special loss and has to beshared by the solvent partners in the ratio of their capitals. The above principle was laid downinthefamous caseGarner Vs Murray.

Sec.48 (b) (ii) of the Indian Partnership Act, expresses the same view as far as sharingthe loss due to insolvency of a partner is concerned. The above rule laid down in Garner VsMurray is applicable only if the Partnership Deed is silent as to the mode of sharing the lossdueto insolvencyof apartner.

Themethodofdistributingtheloss(usingGarnerVsMurrayrule)duetotheinsolvencyof a partner to the solvent partners depends on the method of keeping the capital accounts ofthepartners.

In case capital accounts of the partners are kept under fixed capital method, the loss istobe distributed to thesolvent partners in theratio of their fixedcapitals.

In case the capital accounts of partners are kept under fluctuating capital method, thenthelossduetoinsolvencyofapartneristobedistributedtosolventpartnersintheratioo ftheircapital accounts after distributing profits/reserves appearing in the balance sheet but beforeadjusting the profit or loss on realization. So, in case realization loss is distributed to partnersthenthesolvent partnershaveto bringin cashequivalentto theirshareof realization loss.

Illustration10

X, Y and Z are partners sharing profits and losses in the ratio of 4/9, 2/9 and 1/3. On1st January1981, theyagreed to dissolvethe partnership, theirbalancesheet was as follows:

Liabilities	Rs.	Assets	Rs.
Profitand Loss	4,500	Buildings	45,000
Reservefund	12,600	Machinery	15,000
Billspayable	4,100	Furniture	3,700
Sundrydebtors	9,000	Stock	19,400
Loan fromX	4,000	Debtors	31,000
Capitalaccounts		Investments	24,000
X3000		Billsreceivable	5,600
Y46000		Cashatbank	6,500
Z68000	1,17,000	Cashathand	1,000
	1,51,200		1,51,200

TheassetsrealisedinvestmentsRs.20400;BillsreceivableanddebtorsRs.28200 ;stockRs.14500;FurnitureRs.2050.MachineryRs.8600;BuildingsRs.26450;Alltheli abilitieswerepaid off. The cost of realization was Rs.600. Z has become bankrupt and Rs.1024 only wasrecovered from estate once and for all. Partners were finally paid off. Show the realizationaccount, the bank account and the capital accounts of the partners (i) when the capitals arefixed(ii) when the capitals arefluctuating.

Solution

RealizationAccount

1981 Jan. 1	Rupees	1981 Jan. 1	Rupees
ToBuildings	45,000	ByBillspayable	4,100
ToMachinery	15,000	BySundrycreditors	9,000
ToFurniture	3,700	ByBank (assets realized)	1,00,200
ToStock	19,400	ByX's Capitala/c19600	
ToDebtors	31,000	ByY'sCapital a/c9800	

ToInvestments	24,000	ByZ's Capital a/c14700	44,100
ToBills receivable	5,600	(realizationloss)	
Tobank(creditors andB/P paidoff)	13,100		
ToBank(expenseon realization)	600		
	1,57,400		1,57,400

(a) Whencapitalaccountsarefixed

CapitalAccounts

	X (Rs.)	Y (Rs.)	Z (Rs.)		X (Rs.)	Y (Rs.)	Z (Rs
ToRealization	19,600	9,800	14,700	ByBalanceb/d	68,000	46,000	3,000
ToZ's capitala/c	2,968	2,008	----	ByProfit&loss	2,000	1,000	1,500
(Z's deficiencyDistributedtoXand Y)				ByReservefund	5,600	2,800	4,200
				By Bank a/c (realizationlossbroughtin bysolvent partners)	19,600	9,800	----
ToBanka/c	72,632	47,792	----	ByBank a/c	----	----	1,024
				By Xs capital a/c (Z'sdeficiencyintheratio 34/53)	----	----	2,968
				ByY'scapital a/c(Z's deficiencyintheratio23/53)	----	----	2,008

BankAccount

1981 Jan. 1	Rupees	1981 Jan. 1	Rupees
ToBalanceb/d	6,500	By Realization a/c(paymenttocreditorsand billspayable)	13,100
ToCash in hand	1,000	ByRealization a/c(costof realization)	600
ToRealization a/c(assets realized)	1,00,200	ByX's loan a/c	4,000
ToX'sCapital a/c (realizationlossbroughtin)	19,600	ByX's capital a/c	72,632
ToY'sCapital a/c (realizationlossbroughtin)	9,800	ByY's capital a/c	47,792
ToZ'sCapital a/c	1,024		
	1,38,124		1,38,124

X'sLoanAccount

1981 Jan. 1	Rupees	1981 Jan. 1	Rupees
ToBank	4,000	ByBalanceb/d	4,000
	4,000		4,000

(b) Whencapitalaccountsarefluctuating:

CapitalAccounts

	X (Rs.)	Y (Rs.)	Z (Rs.)		X (Rs.)	Y (Rs.)	Z (Rs.)
ToRealization	19,600	9,800	14,700	ByBalanceb/d	68,000	46,000	3,000
ToZ'sCapitala/c	3,000	1,976	----	ByProfit &loss	2,000	1,000	1,500
(Rs.4976intheratio of75600:49300)				ByReservefund	5,600	2,800	4,200
ToBanka/c	72,600	47,824	----	ByBank a/c (realization lossbroughtin)	19,600	9,800	----
				ByBank a/c	----	----	1,024
				ByXs Capitala/c	----	----	3,000
				ByY's Capital a/c	----	----	1,976
	95,200	59,600	14,700		95,200	59,600	14,700

(Rs.4976intheratio of75600:49300)				ByReservefund	5,600	2,800	4,200
ToBanka/c	72,600	47,824	----	ByBank a/c (realization lossbroughtin)	19,600	9,800	----
				ByBank a/c	----	----	1,024
				ByXs Capitala/c	----	----	3,000
				ByY's Capital a/c	----	----	1,976
	95,200	59,600	14,700		95,200	59,600	14,700

BankAccount

1981 Jan. 1	Rupees	1981 Jan. 1	Rupees
ToBalanceb/d	6,500	ByRealizationa/c	13,100
ToCash in hand	1,000	ByRealizationa/c	600
ToRealization a/c	1,00,200	ByX'sLoana/c	4,000
ToX'sCapital a/c	19,600	ByX's Capital a/c	72,632
ToY'sCapital a/c	9,800	ByY's Capital a/c	47,792
ToZ'sCapital a/c	1,024		
	1,38,124		1,38,124

X'sLoanAccount

1981 Jan. 1	Rs.	1981 Jan. 1	Rs.
ToBank	4,000	ByBalance b/d	4,000
	4,000		4,000

Insolvencyof allpartners

In case all partners became insolvent it is not possible to pay the liabilities of the firminfull.Soliabilities,usuallycreditors,arenottransferredtorealizationaccountondis solution.Cash realized from sale of assets and surpluses from private assets of partners are used to payoff the liabilities to the extent possible. Liabilities unpaid are a gain for the firm and aretransferred to a newly opened account viz'*Deficiency Account'*. Then capital accounts ofpartners are closed after adjusting for realization profit/loss, receipts from private estates etc,by transferring the balances in the capital accounts to deficiency account. The deficiencyaccountis then automaticallyclosed.

Illustration11

ArunandAnandanwereequalpartnerswhosefirmwasdissolvedonDecember31,1982.

BalanceSheetasonDecember31,1982

Liabilities	Rs.	Assets	Rs.
Creditors	3,200	Machinery	1,200
Arun'scapitala/c	400	Furniture	300
		Debtors	500
		Stock	400
		Cash	100
		Anandan'scapitala/c	1,020
	3,600		3,600

Assets realized the following: Machinery Rs.600; Furniture Rs.100; Debtors Rs.400; StockRs.300; realization expenses were Rs.140. Arun was declared insolvent. Anandan's privateestate yielded a surplus of Rs.140 only. Give necessary accounts to close the books of thefigure.

Solution

RealizationAccount

Dec.31,1982	Rs.	Dec.31,1982	Rs.
To Machinery	1,200	Bycash	1,400
ToFurniture	300	(Assetsrealized)	
ToDebtors	500	ByAruns'Capitala/c 570	
ToStock	400	ByAnandan'sCapital a/c 570	1,140
To Cash		(realizationloss)	
(realizationexpense)	140		
	2,540		2,540

CapitalAccounts

(Fig.inRupees)

	Arun	Anand		Arun	Anand
Dec.31,1982			Dec.31,1982		
ToBalanceb/d	----	1,020	ByBalancec/d	400	----
ToRealization a/c	570	570	ByCash	----	140
			ByDeficiency	170	1,450
			(Balancingfigure)		
	570	1,590		570	1,590

CreditorsAccount

Dec.31,1982	Rs.	Dec.31,1982	Rs.

ToCash	1,580	ByBalance b/d	3,200
ToDeficiencya/c	1,620		
(Balancingfigure)			
	3,200		3,200

CashAccount

Dec.31,1982	Rs.	Dec.31,1982	Rs.
ToBalanceb/d	180	ByRealizationa/c	140
ToRealizationa/c	1,400	(realizationexp.)	
(Assetsrealized)		ByCreditors	1,580
ToAnandan's Capitala/c	140	(Balancingfig)	
	1,720		1,720

DeficiencyAccount

Dec.31,1982	Rs.	Dec.31,1982	Rs.
ToArun'sCapitala/c	170	ByCreditors	1,620
ToAnand'sCapitala/c	1,450		
	1,620		1,620

Gradualrealizationofassets -Piecemeal Distribution

Whenafirmisdissolved assetsarerealized andliabilitiesarepaidoff.Incaseanysurplusis left after payment of liabilities, it is used to pay partners' capital accounts. Assets are soldgraduallyandsopaymentstovariouspartiesisalsomadegradually.Whilemakingpayments,firstoutsideliabilitiesarepaidandafterpayingoutsideliabilitiesinfull,partners'loanaccountsarepaid.Ifanysurplusisleftafterpaymenttopartners'loanaccounts,partnerscapitalbalancesarepaid.

When paying outsiders' liabilities, if two or more creditors are there and the accountavailable is not sufficient to pay them in full, then they are paid in proportion to their dues.Likewise while paying partners' loan accounts the same procedure is followed. Then lastlypartners'capital accountsarereturned.

Partners capital accounts are paid gradually as and when assets are realized. There aretwomethods available forthepayment cashto partners forthereturn oftheircapitals.

1. ProportionateCapitalMethod
2. MaximumLossMethod

Whatever method is used for payment of cash to partners' capital accounts, the unpaidbalance of capital accounts, after making final payments to partners, must be in the ratio ofprofitsharing.

1. ProportionateCapitalMethod

Under this method the partner who is having excess capital in relation to his profitsharing ratio is paid first by the excess amount only. This process will continue till thecapital accounts of all the partners are in proportion to their profit sharing ratios.Thereafter realizedamountsarePaidtopartnersintheratioof theirprofitsharing.

2. **MaximumLossmethod**

Under this method, every realization is assumed as the final realization andaccordingly the loss to partners is arrived at. The loss is transferred to all partners intheir profit sharing ratio. Then from the respective capital accounts of partners, thedistributed share of loss is deducted, if the balance amount shows a positive amountthen it represents the amount paid to each partners. Sometimes a partner's capitalaccount is less than the amount of loss distributed. In such a case his balance amountwill show a negative amount. This amount represents loss due to insolvency of thepartner and the other solvent partners have to share this amount in the ratio of theircapital accounts. The balance left in the capital accounts of solvent partners representstheamountpaid tothem.This processiscontinuedtoallsubsequent realizations.

Piecemeal Distribution

Illustration

A,BandCshareprofitsandlossesintheproportionof1/2,1/3and1/6.TheirBalanceSheet on31-12-1994, is as follows.

	Rs.		Rs.
Creditors	50,000	LandandBuildings	70,000
A'sloan	10,000	Plantand machinery	40,000
A'scapital	50,000	Stock	25,000
B'scapital	10,000	Debtors	20,000
C'scapital	40,000	Cash	5,000
	1,60,000		1,60,000

Thepartnershipisdissolvedandthe assetsare realizedasfollows:

Rs.

1strealization	40,000
2ndrealization	30,000
3rdrealization	54,000
4threalization	7,000

Prepareastatement how the distributionisto bemade.

Solution

ProportionateCapitalMethod

		Creditors	A'sloan a/c	A's capital	B's capital	C's capital
Amountdue		50,000	10,000	50,000	10,000	40,000
Cashinhand paidto creditors		5,000	---	---	---	---
Balancedue		45,000	10,000	50,000	10,000	40,000
Amountof1strealization paidtocreditors		40,000	---	---	---	---
Balancedue		5,000	10,000	50,000	10,000	40,000
Amountof2ndrealization	30,000					
Paidtocreditors	5,000	5,000	---	---	---	---
	25,000	NIL				
PaidA'sloan a/c	10,000		10,000			
	15,000	---	----	50,000	10,000	40,000
Paidto C	15,000	---	---	---	---	15,000
Amountdue				50,000	10,000	25,000
Amountofthirdrealization	54,000					
Paidto C	8,333					8,333
	45,667			50,000	10,000	16,667
PaidtoA andC	45,667			34,250	----	11,417
Amountdue				15,750	10,000	5,250
Amountof fourthrealization	7,000					
(-)Paidto AandC	1,000			750	----	250
	6,000			15,000	10,000	5,000
(-)Paid toA, Band C	6,000			3,000	2,000	1,000
Balanceunpaid orloss on realization	----			12,000	8,000	4,000

WorkingNotes

CapitalAccount

CapitalBalances(Rs.)	(a)	50,000	10,000	40,000
Profitsharingratios		3	2	1
Proportionatecapitals(Rs)	(b)	15,000	10,000	5,000
(takingB'scapitalasthe basis)				

Excesscapital(Rs.)(a- b)		35,000	----	35,000
Proportionatecapitalasbetween	(c)	50,000	----	16,667
Aand C,takingA's capitalas the basis				
Excesscapital(a- c)		----	----	24,333

Therefore C is to be paid first by Rs.24,333. Next A and C are to be paid their profitsharing ratio till the capital balances of all the partners are in proportionate to their profitsharingratio.Thenallpartners areto bepaid inproportionto theirprofit sharingratios.

Illustration13

A, B and C were partners sharing profits and losses as in the ratios of 5:3:2. OnDecember31,1985, theirBalanceSheet was as follows:

	Rs.		Rs.
Sundrycreditors	20,000	Cashatbank	2,000
A'sloan	10,000	Stock	28,000
B'sloan	4,000	Sundrydebtors	30,000
Capitals		Furnitureandfittings	4,000
A15000			
B12000			
C 3000	30,000		
	64,000		64,000

Thefirmwas dissolvedonthe 1stJanuary, 1986.Theassets realizedwere as follows:

	Stock	Debtors	Furniture’s	Expenses
January,31	5,000	6,000	1,500	500
February,28	7,000	4,000	----	800
March.31	10,000	15,000	----	1,500
April.30	4,000	3,000	2,000	500

Cashreceivedwaspaidtotherightful claimants.Giveaccountstoclearthebooksofthefirms.

WorkingNotes

Thecashavailableeachmonthisfollows:

	Stock		Debtors		Furniture’s		Expenses		Cash available

January, 31	5000	+	6000	+	1500	-	500	=	12000
February, 28	7000	+	4000	+	---	-	800	=	10800
March,31	10000	+	15000	+	---	-	1500	=	23500
April,30	4000	+	3000	+	2000	-	500	=	8500

Distributionof Cash

(Fig.inRupees)

		Creditors	A'sloan a/c	B'sloan a/c	A's capital	B's capital	C's capital
Balancedue		20,000	10,000	4,000	15,000	12,000	3,000
Cashinhand paidto creditors		2,000	---		---	---	---
Balancedue		18,000	10,000	4,000	15,000	12,000	3,000
January,31-Net realization Rs.15000 paidtocreditors		12,000	---	---	---	---	---
Balancedue		6,000	10,000	4,000	15,000	12,000	3,000
February28 – Net realization	10200						
Paidtocreditors	6,000 4,200	6,000	---		---	---	---
Rs. 4200 paid to A's andB'sloanintheratiooftheir loans		---	3,000	1,200			
March31,Netrealization Rs.23,500		---	7,000	2,800	15,000	12,000	3,000
		----	7,000	2,800	---	---	---
A's loan and B's loan paid 9800							
Balance due (a)		----	----	----	15,000	12,000	3,000
Cash available for partners 13700							
Maximum less distributed Rs.16300 (30000 - 13700) to A, B and C in the profit sharing ratio		----	----	----	8,150	4,890	3,260
Amount at credit		----	----	----	6,850	7,110	-260

Deficiency of C shared by A and B in their capital ratios of 15:12		----	----	----	-144	116	+260
Amount at credit and available cash paid 13700 (b)		----	----	----	6,706	6,994	----
Balance of capitals (a - b)		----	----	----	8,294	5,006	3,000
April 30 - Net realization Rs.8500							
Maximum loss distributed to A,B and C (16300 - 8500) = 7800		----	----	----	3,900	2,340	1,560
Amount at credit and available cash paid Rs.8500		----	----	----	4,394	2,666	1,440

RealizationAccount

(Fig.inRupees)

1986, Jan. 1		1986, Jan. 1	
ToStock	28,000	ByCreditors	20,000
ToSundrydebtors	30,000	ByCash - Assets realized	
ToFurniture &fittings	4,000	Stock -5000 Debtors-6000 Furniture–1500	12,500
ToCash-creditorspaid	2,000	1986,Feb.28	
ToCash -creditors &expenses	12,500	Bycash-Assets realized Stock– 7000 Debtors-4000	11,000
1986,Feb.28	6,800	1986,March31	
To Cash - creditors &expenses	1,500	ByCash - Assets realized Stock– 10000 Debtors-15000	25,000
1986,March31		1986,April30	
ToCash -expenses	500	By Cash - Assets realizedStock– 4000 Debtors-3000 Furniture -2000	9,000
		By Loss transferredA'scapital3900 B'scapital2340	7,800

		C'scapital1560	
	85,300		85,300

CashAccount

(Fig.in Rupees)

1985, Jan. 1		1986, Jan. 1	
ToBalanceb/d	2,000	ByCreditors	2,000
1985, Jan. 31		1985, Jan. 31	
To Realization a/cassetsrealized	12,500	ByRealization a/c creditors&expenses	12,500
		1985,Feb28	
1985,Feb28 To Realization a/cassetsrealized	11,000	ByRealization a/c creditors&expenses	6,800
		1985,March31	
		ByA's loan 3,000	3,000
1985,Feb31		ByB's loan	1,200
ToRealization a/c	25,000	ByRealization a/cexpenses	1,500
assetsrealized		ByA's loan	7,000
		ByB's loan	2,800
		ByA's Capital	6,706
		ByB's Capital	6,994
1985,April30		1985,April30	
ToRealization a/c	9,000	ByRealizationexpense	500
assetsrealized		ByA's Capital a/c	4,394
		ByB's Capitala/c	2,666
		ByC's Capitala/c	1,440
	59,500		59,500

March31 To Cash	2,800		
	4,000		4,000

CapitalAccount *(Fig.in Rupees)*

1986March31				1986Jan. 1			
To Cash	6,706	6,994		Bybalanceb/d	15,000	12,000	3,000
1986Apr,30							
To Cash	4,394	2,666	1,440				
	15,000	12,000	3,000		15,000	12,000	3,000

Illustration14.A, Band Cshareprofitsin theproportionof 1/2,1/3 and1/6. TheirBalanceSheetis as follows:

Liabilities	Rs.	Assets	Rs.
CapitalAccounts		Assetslessliabilities	80,000
A30000			
B30000			
C 20000	80,000		
	80,000		80,000

Thepartnershipisdissolved andtheassetsrealized areasfollows'

Rs.

Firstrealization 10,000

Secondrealization15,000

Thirdrealization 25,000

PrepareastatementshowinghowthedistributionshouldbemadeapplyingGarnerVs. Murrayprinciple.

Note:MaximumLossMethodisusedtodistributecashtocapitalaccountswhenGarner VsMurrayprincipleis to befollowed.

Solution

		A	**B**	**C**
Balanceofcapital	(a)	30,000	30,000	20,000
FirstRealizationRs.1,00,000				
Maximum loss (80000 - 10000) 70000 distributed to partners in their profit sharing ratios	(b)	35,000	23,333	11,667
Amount at credit	(c)	-5,000	6,667	8,333
A's loss shared by B and C in their capital ratios 3:2	(d)	+5000	-3,000	-2,000
Amount at credit and available cash paid	(e)	-	3,667	6,333
Balance of capital (a - e)	(f)	30,000	26,333	13,667
Second Realization Rs.15000				

Maximum balance distributed (70000 - 15000) = 55000	(g)	27,500	18,333	9,167
Amount at credit and available cash paid	(h)	2,500	8,000	4,500
Balance of capital (f - h)	(i)	27,500	18,333	9,167
Third Realization Rs.25000				
Maximum possible loss distributed (55000 - 25000) = 30000	(j)	15,000	10,000	5,000
Amount at credit and available cash paid (i - j)	(k)	12,500	8,333	4,167
Balance in capital account left unpaid and hence loss (i-k)		15,000	10,000	5,000

A'sLoanAccount

1986		1986	
Feb.28 To Cash	3,000	Jan.1 ByBalanceb/d	10,000
March31 To Cash	7,000		
	10,000		10,000

B'sLoan Account *(Fig.in Rupees)*

1986		1986	
Feb.28 To Cash	1,200	Jan. 1Bybalanceb/d	4,000

UNIT- 5 ACCOUNTINGSTANDARDFORFINANCIAL REPORTING

RobertAnthonyoncestatedthataccountingisalanguageofbusiness.Theprimary function of a language is to serve as a means of communication. It is throughaccounting that a business communicates with the outside world. Thus, accounting is alivinglanguage.

At the end of each accounting year, every business enterprise is curious to knowwhether it has earned a profit suffered a loss during an accounting period. Similarly, italso wants to know its financial position. It is for these purposes, financial statements areprepared.

Meaningoffinancialstatement

Financial statements are the final product of the accounting process. They arestatements containing financial information of a business enterprise. The basic purpose ofpreparing financial statements is to convey information about financial position of theenterpriseto owners,creditors and theinvestors.

Natureoffinancialstatement

Thefollowingcharacteristicsoffinancialstatementsindicatetheirnature.

1. Recorded fact: the term recorded facts refers to the data drawn from accountingrecords. Only those facts which have been recorded in the books are shown in thefinancialstatements.
2. Periodical report: financial statements are prepare usually at the end of each yeartoshowtheresult ofbusinessoperation andfinancialposition ofafirm.
3. Accountingprinciples:inthepreparationoffinancialstatements,certainaccounting principles, concepts and conventions are followed. For example, theprincipleofcost priceormarket pricewhicheveris less is followed.
4. Assumptions: business transactions are recorded on certain assumptions.Forexample,inpreparingfinancialstatements,theaccountantsmakeman yassumptionslikethatthevalueofmoneyremainsconstant,goingconcernconceptsetc..
5. Personaljudgement:thefinancialstatementsareaffectedbythepersonaljudgementofac countant.

Objectiveoffinancialstatement

Thesignificantobjectivesoffinancialstatementsare:

1. They provide necessary information about the financial activities to the interestedparties.

2. They provides necessary information about the efficiency or otherwise of themanagement,regardingtheproperutilization ofthescarceresources.
3. Theyprovidenecessaryinformationforpredictions(financialforecasting).
4. They help to evaluate the earning capacity of the firm by supplying a statement offinancial position, a statement of periodical earnings together with a statement offinancialactivities to thevarious interested persons.
5. Theyfacilitatedecisionsregardingthechangesinthemannerofacquisition,utilization,preservation and distributionofthescarceresources.
6. They facilitate decisions regarding replacement of fixed assets and expansion ofthefirm.
7. Theyprovidenecessarydatatothegovernmentfortakingproperdecisionsrelating to duties, taxes and price control, etc. and for some legal and controlpurposes.
8. Theydeviceremedialmeasuresforthedeviationsbetweentheactualandbudgetedperformances.
9. They also provide necessary data and information to the managers for internalreportingand formulation ofoverall policies.
10. They also help to safeguard the interest of shareholders who are not allowed to gothroughtheday-to-dayaffairs ofthefirm.
11. They help to settle disputes arising from High Court, Supreme Court, Arbitratorsetc.
12. Theyhelp thecredit ratingagencies to determinetheratingoftheCompany.

Uses(Utility)offinancialstatementsforusers

1. Ownersandinvestors

Stockholdersofcorporationsneedfinancialinformationtohelpthemmakedecisions on what to do with their investments (shares of stock), i.e. hold, sell, or buymore.

Prospective investors need information to assess the company's potential for success andprofitability.Inthesameway,smallbusinessownersneedfinancialinformationtodetermine ifthebusinessis profitableand whethertocontinue, improveordrop it.

2. Management

In small businesses, management may include the owners. In huge organizations,however, management is usually made up of hired professionals who are entrusted withthe responsibility of operating the business or a part of the business. They act as agents oftheowners.

3. Lenders

Lendersoffundssuchasbanksandotherfinancialinstitutionsareinterestedin thecompany'sability topayliabilitiesuponmaturity (*solvency*).

4. Tradecreditorsorsuppliers

Like lenders, trade creditors or suppliers are interested in the company's ability topay obligations when they become due. They are nonetheless especially interested in thecompany's*liquidity* – itsabilityto pay*short-term*obligations.

5. Government

Governing bodies of the state, especially the tax authorities, are interested in anentity's financial information for taxation and regulatory purposes. Taxes are computedbased on the results of operations and other tax bases. In general, the state would like toknowhowmuch thetaxpayermakesto determinethetaxduethereon.

6. Employees

Employees are interested in the company's profitability and stability. They areafter the ability of the company to pay salaries and provide employee benefits. They mayalso be interested in its financial position and performance to assess company expansionpossibilitiesand careerdevelopment opportunities.

7. Customers

When there is a long-term involvement or contract between the company and itscustomers,thecustomersbecomeinterestedinthecompany'sability tocontinueitsexistenceandmaintainstabilityofoperations.Thisneedisalsoheightenedincases wherethecustomers depend upon theentity.

8. GeneralPublic

Anyone outside the company such as researchers, students, analysts and others areinterestedin thefinancialstatementsofacompanyforsomevalid reason.

ACCOUNTINGSTANDARDS

Whendifferentfirmsusedifferentmethodsofrecordingthetransactions,comparison becomes difficult. In the absence of a uniform set of rules, there will be a lotof problems. Thus, there is a need for uniform rules and principles. This will make thepreparationandpresentationoffinancialstatementeasy,relevant,reliable,understandable and comparable. This is sought to be achieved by developing accountingstandards.

MeaningofAccountingStandards:

Accountingstandardsarethewrittenstatementsconsistingofrulesandguidelines,issuedby theaccounting institutions,forthepreparationofuniformandconsistent financial statements and also for other disclosures affecting the different usersofaccountinginformation.

Accounting standards lay down the terms and conditions of accounting policiesand practices by way ofcodes, guidelines and adjustments for making the interpretationof the items appearing in the financial statements easy and even their treatment in thebooksofaccount.

Definition

Kohlerdefinesaccountingstandardsas,“amodeofconductimposedonaccountantsbylaw,customsorprofessional body”

Objectiveofaccounting standard

Themainobjectiveofaccountingstandardistostandardizethediverseaccountingpoliciesand practices.

1. **To provide information**: one of the major objectives of accounting standard is toprovideinformation to theusers.
2. **To harmonize different accounting processes**: accounting standards are evolvedto bridge the gap between various accounting procedures to harmonize differentaccountingprocesses.
3. **To enhance the content:** another objective of accounting standard is to enhancethecredibilityand comparabilityofthefinancial statements.
4. **To communicate uniform results:** another objective of accounting standard is tocommunicateuniformresultstoexternalusersaswellasinternalusersfordecisionmaking.
5. **Tofacilitatecomparison:**accountingstandardsaimatfacilitatinginter-firmcomparisonand intrafirm comparison.
6. **To improve the quality of financial statement:** another important objective ofaccountingstandardistomakethefinancialstatementsmorereliable,comparable,relevant andunderstandable.

Roleandimportanceofaccountingstandards

Accounting standard plays an important role in facilitating uniform preparationand reporting of general purpose financial statement. These are very useful for investorsandotherexternalgroupsinassessingtheprogressandprospectsofalternativeinvestmentsin different companies in differentcountries.

In an era of globalization it is essential to adopt transparent accounting norms invaluation of fixed assets, revenue recognition, valuation of inventories, classification andvaluation of investment, foreign currency translation etc… accounting standard play animportant role in strengthening financial regulation and supervision. In short, accountingstandards improve transparency, consistency, adequacy, accuracy and comparability offinancialstatement.

Advantagesofaccountingstandards

1. **Credibility and reliability of financial statements:** the accounting standardscreate a sense of confidence amongst the users of the accounting information byprovidingadefinitestructureofuniformguidelines.
2. **Uniformity**: the accounting information disclosed in financial statementcannotbeinterpreted in anymannerotherthan thepurposeit is intended for.
3. **Elimination of ambiguity:** as the general principle of disclosure and valuationhavebeendevelopedonuniformbasis,therewouldbenoambiguityininterpretation.
4. **Comparison:** as the same methodology is being followed in all cases comparisonbetweentheresultsofdifferent organizationshas becomeeasier.
5. **Determination of managerial accountability:** accounting standards are useful inmeasuring the efficiency of the management regarding the profitability, liquidity,solvencyandgeneral progress oftheenterprise.

6. **Useful to the shareholders, investors, researchers etc**.: accounting standardshelptheinvestorstotakedecisionregardinginvestments.Thegovernmentofficialscan makeeffectiveuseofaccountingdataforplanningetc.
7. **Raises the standards of auditing:** accounting standards raise the standards ofauditingitselfin its task ofreportingonthefinancial statement.

AccountingstandardboardofIndia (ASB)

ASB was setup in india on 21st april 1977 with a view to harmonise the diverseaccounting policies and practices in india. It was set up by the council of ICAI. ICAIis one of the members of IASC. Hence, while formulating the accounting standards,ASB gives much weight to standardize issued by the IASC. ICAI tries to incorporatethose international standards inIndia, in the light of the condition and practicesprevailinginIndia.

Objectivesofaccountingstandardboardofindia

1. To conceive of and suggest areas in which Accounting Standards need to bedeveloped.
2. To formulate Accounting Standards with a view to assisting the Council of theICAIin evolvingand establishingAccountingStandards inIndia.
3. To examine how far the relevant International Financial Reporting Standards canbeadaptedwhileformulatingtheAccountingStandard and toadapt thesame.
4. To review, at regular intervals, the Accounting Standards from the pointof viewofacceptanceor changedconditions,and, ifnecessary, revisethesame.
5. Toprovide,fromtimetotime,interpretationsandguidanceonAccountingStandards.
6. To proactively participate with the national andinternational bodies engaged inthe Standard-setting process, such as, sending comments on various consultativepapers such as Exposure Drafts, Discussion Papers etc., issued by InternationalAccounting Standards Board and various other international bodies such as Asian-OceanianStandard-Setters Group(AOSSG).
7. TocarryoutsuchotherfunctionsrelatingtoAccountingandAccountingStandards.

AccountingstandardsinIndia

AS 1 Disclosure of Accounting PoliciesAS 2 Valuation of Inventories (amended)AS3 Cash FlowStatements

AS4ContingenciesandEventsOccurringaftertheBalanceSheetDate

AS5NetProfitorLoss fortheperiod,PriorPeriodItems andChangesinAccountingPoliciesAS6 Depreciation Accounting(withdrawn)

AS7ConstructionContracts(revised2002)

AS 8 Accounting for Research and Development (withdrawn for AS 26)AS9 RevenueRecognition

AS10AccountingforFixedAssets (amended)

AS11TheEffectsofChangesinForeignExchangeRates(revised2003)

AS12AccountingforGovernmentGrantsAS13
AccountingforInvestments(amended)
AS 14 Accounting for Amalgamations (amended)AS15EmployeeBenefits(revised 2005)
AS 16 Borrowing CostsAS17SegmentReporting
AS18RelatedPartyDisclosuresAS 19Leases
AS20EarningsPerShare
AS 21 Consolidated Financial Statements (amended)AS22 AccountingforTaxes onIncome
AS23AccountingforInvestmentsinAssociatesinConsolidatedFinancial StatementsAS24 DiscontinuingOperations
AS 25 Interim Financial ReportingAS26IntangibleAssets
AS 27 Financial Reporting of Interests in Joint VenturesAS28Impairment ofAssets
AS 29 Provisions, Contingent Liabilities and Contingent Assets (amended)AS30 Financialinstrument–recognition and measurement
AS 31 Financial instrument – presentationAS 32 Financial instrument-disclosures**Internationalaccountingstandards**

The main purpose of accounting is to provide information to internal and externalusers.Forthispurpose,financialstatementsareprepared.Ifdifferentaccountingprocedures and practices are followed by accountants, there would be a lot of difficulties.Sothe accountantsallover theworldhavedevelopedcertainrules,proceduresandconventions.Theseaccountingproceduresandpracticesareknownas GenerallyAccepted Accounting principles. But the generally accepted accounting principles permita number of alternative treatments for the same item. Therefore, there was a need toharmonize and standardize the diverse accounting policies and practices. However, therewas hesitation in doing so and making it mandatory. The great depression of 1929 forcedthe accounting professionals to rethink about accounting rules. USA took the lead in thisdirectionfollowedbyUK,Australia,Canada,andotherdevelopedcountries.InUSA,the American Institute of Certified public accountants was given the responsibilities tocodify accounting standards.Later onInternational Accounting Standards CommitteewasalsoestablishedforformulatingInternationalAccountingStandards.Thesearef ormulated ot convey the accounting language to all people in the world. In fact, theconceptofdevelopmentandestablishmentofInternationalAccountingStandardsemergedinitiallyinthefirstInternationalCongressAccountantheldatSt.Louisin1904.

InstitutionsengagedinAccountingHarmonizationatGloballevel

These are some institutions engaged in accounting harmonization at global level.Important among them are United Nations, European Union, international AccountingStandardsFoundation,InternationalAccountingStandardsBoard(IASB),FinancialAccounting Standards Board(FASB) etc. of these, the most important are IASB andFASB.

InternationalAccountingStandardsCommittee(IASC)

Due tothe increase inmalpracticesinaccounting,andincrease infailure ofbusiness units, there was a great demand for standardized accounting practices. Thisresulted in the formation of "Accountants International Study group" in 1967. For thepurpose of maintaining uniformity in accounting principles throughout the world, IASCcame into force on 29th June 1973. IASC is the outcome of the 1972 world AccountingCongress after the informal meeting between representatives of the Institute of CharteredAccountantsofEnglandandwalesandtheAmericanInstituteofCertifiedpublicaccountants.

The IASC Foundation is an independent body, not controlled by any particularGovernment or professional organization. Its main purpose is to oversee the IASB insetting the accounting principles which are used by business and otherorganizationsaroundtheworldconcerned with financialreporting.

The IASC was formed in 1973 through an agreement made by professional accountancybodiesfromAustralia,Canada,France,Germany,Ireland,Japan,Mexico,theNetherlands,theUKandtheUSA

International Accounting Standard Committee has issued certain standards. A listofsuch standards isgiven below.

IAS.1 Presentation of financial statementIAS.2 Inventories
IAS.3 ItisreplacedbyIAS.27&28
IAS.4 Withdrawn and replaced by IAS 16, 22 & 38IAS.5 ReplacedyIAS 15
IAS.6 Replaced y IAS 15IAS.7 Cashflowstatement
IAS.8 Profitandlossaccountfortheperiod,fundamentalerrorsandchangesin accountingpolicies
IAS.9 ResearchfordevelopmentcostswillbesupersededbyIAS38witheffectivefrom1/7/1999
IAS.10 Events after the balance sheet dateIAS.11 Constructioncontracts
IAS.12 Income taxesIAS.13 Replaced by IAS 1IAS.14 Segmentreporting

IAS.15 Information reflecting the effect of changing pricesIAS.16 Property,plant equipment
IAS.17
LeasesIA
S.18 Revenue
IAS.19 Employmentbenefits
IAS.20
Accountingforgovernmentgrantsanddisclosureofgovernmentassistance IAS.2
1 Theeffect ofchangesin foreign exchangerates
IAS.22 Business combinationsIAS.23
Borrowingcosts
IAS.24 Related party disclosuresIAS.25
Accountingforinvestment
IAS.26 Accountingand reportingbyretirement benefit plans
IAS.27
Consolidatedfinancialstatementsandaccountingforinvestmentinsubsidiaries IAS.2
8 Accountingforinvestment in associates
IAS.29 Financialreportingin hyperinflationaryeconomies
IAS.30
Disclosuresinfinancialstatementsofbankandsimilarfinancialinstitutions IAS.3
1 Financialreportingon interest in jointventures
IAS.32
Financialinstruments:disclosureandpresentationIA
S.33 Earningspershare
IAS.34 Interim financial reportingIAS.35 Discounting operationsIAS.36
Impairmentofassets
IAS.37
Provisions,contingentliabilities,andcontingentassetsIAS
.38 Intangible assets
IAS.39
Financialinstruments:recognitionandmeasurementIA
S.40 Investmentproperty
IAS.41 Agriculture

InternationalAccountingStandardBoard

TheIASB(InternationalAccountingStandardsBoard)istheindependentstandard-setting body of the IFRS Foundation. All meetings of the IASB are held in public andwebcast. In fulfilling its standard setting duties the IASB follows a thorough, open andtransparent due process.This process leads to publication of consultative documents,such as Discussion Papers and Exposure Drafts, for public comment. The IASB engagesclosely withstakeholdersaroundthe world,including investors,analysts,regulators,businessleaders,accountingstandard-settersand theaccountancyprofession.

RoleofIASBinDevelopingIFRS

1. **Setting the agenda:** The IASB, by developing high quality financial reportingstandards, seeks to address a demand for better quality information that is of valueto those users of financial reports. When deciding whether a proposed agenda itemwilladdressusers'needstheIASBconsiders:Therelevancetousersoftheinformation and the reliability of information that could be provided,Existingguidanceavailable,Thepossibilityofincreasingconvergence,Thequalityofthe

   IFRS to be developed, Resource constraints. To help the IASB in considering itsfuture agenda, its' staff is asked to identify, review and raise issues that mightwarrant the IASB's attention. New issues may also arise from a change in theIASB'sConceptual FrameworkforFinancialReporting.
2. **Planningtheproject**:Whenaddinganitemtoitsactiveagenda,theIASBdecides whether to conduct the project alone or jointly with another standard-setter. Similar due process is followed under both approaches. When consideringwhether to add an item to its active agenda, the IASB may determine that it meetsthe criteria to be included in the annual improvements process. The IASB assessestheissueagainstcriteriasuchasClarifying,Correcting,Welldefinedandsufficiently narrow in scope that the consequences of the proposed change havebeen considered, Completed on a timely basis, All criteria must be met to qualifyforinclusioninannualimprovements.Oncethisassessmentismade,theamendments included in the annual improvements process will follow the samedueprocessasotherIASBprojects.Theprimaryobjectiveoftheannualimprovements process is to enhance the quality of IFRSs by amending existingIFRSstoclarifyguidanceandwording,orcorrectingforrelativelyminorunintended consequences, conflicts or oversights. After considering the nature ofthe issues and the level of interest among constituents, the IASB may establish aworking group at this stage and a project team for the project will be selected. Theproject manager draws up a project plan under the supervision of the directors ofthe technical staff and the project team may also include members of staff fromotheraccountingstandard-setters, as deemed appropriatebytheIASB.

3. **Developing and publishing the discussion paper:** A discussion paper is not amandatorystepintheIASB'sdueprocess.NormallytheIASBpublishesadiscussion paper as its first publication on any major new topic as a vehicle toexplain the issue and solicit early comment from constituents. If the IASB decidesto omit this step, it will state its reasons. Typically, a discussion paper includes acomprehensive overview of the issue, possible approaches in addressing the issue,the preliminary views of its authors or the IASB, and an invitation to comment.Thisapproachmaydifferifanotheraccountingstandard-setterdevelopstheresearch paper. Discussion papers may result either from a research project beingconducted by another accounting standard-setter or as the first

stage of an activeagenda project carried out by the IASB. If research has been performed by anotheraccounting standard-setter, issues related to the discussion paper are discussed inIASB meetings, and publication of such a paper requires a simple majority vote bythe IASB. If the discussion paper includes the preliminary views of other authors,theIASBreviewsthedraftdiscussionpapertoensurethatitsanalysisisanappropriate basis on which to invite public comments. For discussion papers onagendaitemsthatareundertheIASB'sdirection,orincludetheIASB'spreliminary views,theIASBdevelopsthepaperoritsviewsonthebasisofanalysisdrawnfromstaffresearchandrecommendations,aswellassuggestions

made by the IFRS Advisory Council, working groups and accounting standard-setters and presentations from invited parties. All discussions of technical issuesrelated to the draft paper take place in public sessions. When the draft is completedand the IASB has approved it for publication the discussion paper is published toinvitepubliccomment.

4. **Developingandpublishingtheexposuredraft:**Publicationofanexposuredraftisamandatorystepindueprocess.AnexposuredraftistheIASB'smainvehicleforconsultingthepublic.Unlikeadiscussionpaper,anexposuredraftsetsoutaspecificproposalintheformofaproposedIFRS(oramendmenttoanIFRS).Thedevelopment of an exposure draft begins with the IASB considering issues on thebasisofstaffresearchandrecommendations,aswellascommentsreceivedonanydiscussionpaper,andsuggestionsmadebytheIFRSAdvisoryCouncil,workinggroupsandaccountingstandard-settersandarisingfrompubliceducationsessions.Afterresolvingissuesatitsmeetings,theIASBinstructsthestafftodrafttheexposuredraft.Whenthedrafthasbeencompleted,andtheIASBhasballotedonit,withaminimumofninevotesnecessarytopublishanexposuredraft, theIASBpublishesitforpubliccomment.AnexposuredraftcontainsaninvitationtocommentonadraftIFRS,ordraftamendmenttoanIFRS,thatproposesrequirementsonrecognition,measurementanddisclosures.Thedraftmayalsoincludemandatoryapplicationguidanceandimplementationguidance,andwillbeaccompaniedbyabasisforconclusionsontheproposalsandthealternativeviewsofdissentingIASBmembers (ifany).

5. **Developing and publishing the standard**: The development of an IFRS is carriedout during IASB meetings, when the IASB considers the comments received on theexposure draft. Changes from the exposure draft are posted on the website. Afterresolving issues arising from the exposure draft, the IASB considers whether itshould expose its revised proposals for public comment, for example by publishinga second exposure draft. If the IASB decides that re-exposure is necessary, the dueprocess to be followed is the same as for the first exposure draft As it movestowardscompletinganewIFRSormajoramendmenttoanIFRS,theIASBprepares a project summary and feedback statement. These give direct feedback tothose who submitted comments on the exposure draft, identify the most significantmatters raised in the comment process and explain how the IASB responded tothose

matters. At the same time, the IASB prepares an analysis of the likely effectsof the forthcoming IFRS or major amendment. The analysis will therefore attemptto assess the likely effects of the new IFRS on: The financial statements of thoseapplying IFRSs, The possible compliance costs for preparers, The costs of analysisfor users (including the costs of extracting data, Identifying how the data have beenmeasured and adjusting data for the purposes of including them in, for example, avaluation model, The comparability of financial information between reportingperiodsforanindividualentityandbetweendifferententitiesinaparticularreporting period, and The quality of the financial information and its usefulness inassessingthefuturecashflowsofanentity.WhentheIASBissatisfiedthatithas

reachedaconclusionontheissuesarisingfromtheexposuredraft,itinstructsthestaffto draft theIFRS.

FinancialAccountingStandardBoard

Establishedin1973,theFinancialAccountingStandardsBoard(FASB)istheindependent, private-sector, not-for-profit organization based in Norwalk, Connecticut, thatestablishes financial accounting and reporting standards for public and private companies andnot-for-profit organizations that followGAAP.The FASB is recognized by the Securities andExchange Commission as the designated accounting standard setter for public companies.FASB standards are recognized as authoritative by many other organizations, including stateBoards of Accountancy and the American Institute of CPAs (AICPA). The FASB developsandissuesfinancialaccountingstandardsthroughatransparentandinclusiveprocessintended to promote financial reporting that provides useful information to investors andotherswho usefinancialreports.

FunctionsoftheFASB

- EstablishReportingStandards
- ImproveExistingStandards
- EnsureInvestorsReceive Information
- EstablishAccountingPrinciples
- EnsureanUnderstandingofPrinciples

RoleofFASBinDevelopingAccountingStandardsandGAAPs

FASB hasa tremendous role in developing accounting standardsandGAAPs, itdevelopshighqualityaccountingstandards.Besides,itmonitorstheireffectiveimplementation. It is engaged in educating stakeholders, helping prepares and practitioners ininterpretingthestandards and makingnecessaryclarifications to thestandards.

FASBhas a unique position in the financial reporting process. Its main goal is toprovideleadershipforpubliccompaniesinestablishingandimprovingtheaccountingmethodsused to preparefinancial statements.

IFRS(InternationalFinancialReportingStandards)

InternationalFinancialReportingStandards(IFRS)aredesignedasacommongloballangua geforbusinessaffairssothatcompany accountsareunderstandableandcomparableacrossinternationalboundaries.Theyareaconsequenceofgrowinginternational shareholding and trade and are particularly important for companies that havedealings in several countries. They are progressively replacing the many different nationalaccounting standards. They are the rules to be followed by accountants to maintain books ofaccountswhicharecomparable,understandable,reliableandrelevantaspertheusersinternalorexternal.

International Financial Reporting Standards (IFRS) is a set of accounting standardsdevelopedbyanindependent,not-for-profitorganizationcalledtheInternationalAccountingStandardsBoard (IASB).

IFRSAdoption/IFRSConvergence

1. **Voluntaryadoption**

   CompaniescanvoluntarilyadoptIndASforaccountingperiodsbeginningonorafter 1April2015withcomparativesforperiodending31March2015orthereafter.However,oncetheyhavechosen this path, theycannot switch back.

2. MandatoryApplicability

   PhaseI

Ind AS will be mandatorily applicable to the following companies for periods beginning onorafter**1April2016**,withcomparativesfortheperiodending**31March2016**orthereafter:

1. Companies whose equity and/or debt securities are listed or are in the process oflisting on any stock exchange in India or outside India and having net worth of 500croreINR ormore.
2. Companies having net worth of 500 crore INR or more other than those coveredabove.
3. Holding, subsidiary, joint venture or associate companies of companies coveredabove.

PhaseII

Ind AS will be mandatorily applicable to the following companies for periods beginningon or after **1 April 2017**, with comparatives for the period ending **31 March 2017** orthereafter:

1. Companies whose equity and/or debt securities are listed or are in the process ofbeing listed on any stock exchange in India or outside India andhaving net worthofless than rupees 500 crore.
2. Unlisted companies other than those covered in Phase I and Phase II whose networtharemorethan 250croreINRbut lessthan 500 croreINR.
3. Holding,subsidiary,jointventureor associatecompaniesofabovecompanies.

NeedforIFRSConvergence

TheneedforIFRSConvergencehas arisenduetothefollowingdevelopments:

1. Financialglobalization
2. Multinationalcorporations
3. Accountingprofession
4. Govt.andrevenueauthorities

BenefitsofadoptingIFRS

1. Improved financial reporting and tax planning: Under IFRS, companies will produce astandardized and consistent set of accounting and financial reports for complying withlocal statutory and consolidated requirements. This will help improve the analysis offinancialreportingand taxplanningprocesses.
2. Improved day-to-day operations: Businesses will get faster access to more in-depthfinancial performance information to use in analysing and making better decisionsabout day-to-dayoperations.
3. Better managedresources: By standardizing processes andaccounting,companieswillbeabletostandardizeandstreamlineaccountingsystemsacrosstheenterpriseandreducethecost ofauditingand statutoryreporting.
4. Improved financial controls: By standardizing the approach and control over statutoryreporting,businesseswillreducetheriskofpenaltiesandcomplianceproblemsenterprise-wideand in individual countries.
5. Lowered cost of capital: Increased insight into financial results and adherence to high-quality financial standards, as specified by IFRS, can benefit both companies and theirinvestorswith reducedcost ofcapital.

ChallengesofIFRS

1. Itincreasescost
2. Unlike several other countries the accounting framework in india is deeply affected bylawsand regulations.
3. IfIFRShastobeuniformlyunderstoodandconsistentlyapplied,allstakeholdersemployees,auditors, regulators,taxauthoritiesetc. wouldneed tobetrained.
4. Theindustrywould beableto raisecapital.
5. Itwouldprovideprofessionalopportunitiestoserveinternationalclients.
6. Entitywouldneedtoincuradditionalcostformodifyingtheir IT systems.
7. DifferencebetweenGAAPandIFRSmayaffectbusinessdecision.
8. Limitedpooloftrainedresource and personhavingexpert knowledgeonIFRS.
9. Everybodyisreluctanttochange
10. Therearepracticaldifficultiesforimplementingcertain IFRS.

RoadmapforimplementationofIndAS(orConvergencewithIFRS)forscheduledCommercialbanks(ExcludingRRBs),insuranceCompaniesandNBFCs

1. ScheduledcommercialBanksand InsuranceCompanies
   a. Scheduledcommercialbank(excludingRRBs),AllIndiaTermLendingRefinancing Institutions(Like Exim Bank, NABARD, NHB and SIDBI)andinsuranceCompanies.
   b. Holding,subsidiary,jointventureorassociatecompaniesofScheduledCommercialbanks(ExcludingIFRS)
      i. Comparatives for these financial statements will be periods ending

31st march2018, orthereafter.

ii. IndASwillbeapplicabletobothconsolidatedandindividualfinancialstatement.

2. NonBankingFinanceCompanies(NBFCs)

PhaseI:IstApril2018onwards

a. NBFChavingnetworthofrs.500crores ormore
b. Holding, subsidiary, joint venture or associate companies of companies coveredunder (a) above, other than those companies already covered undercorporateroadmap announced bytheMCA.
   - Comparative for thesefinancialstatementswillbe periodsending 31st march2018 orthereafter.
   - Ind AS will be applicable to both consolidated and individual financialstatement.

PhaseII:1st April2019onwards

a) NBFCs whose entity and / or debt securities are listed or are in theprocess of listing on any stock exchange in india or outside indiahavingnetworth less than rs.500 crore.
b) NBFCs other than those covered under phase I (a) and Phase II (a)above, that are ulisted companies having networth of Rs. 250 croresormorebut less than Rs. 500 crores.
c) Holding,subsidiary,jointventureorassociatecompaniesofcompaniescoveredunder(a)above,otherthanthosecompaniesalreadycovered undercorporateroadmap announced bytheMCA.

ListofIAS/IFRSwithcorrespondingIndain As(beforeconvergence)andInd–AS

IASNO	TITLE	Corresponding IndianGAAP	Correspondingcoveraged Ind AS
IAS.1	Presentationoffinancialstatement	AS1	IND– AS1
IAS.2	Inventories	AS2	IND-AS2
IAS.7	Cashflowstatement	AS3	INDAS7
IAS.8	Accountingpolicies,changesinaccountingestimateanderrors	AS5	INDAS8
IAS.10	Eventsafterthebalancesheetdate	AS4	INDAS10
IAS.11	Constructioncontracts	AS7	INDAS11
IAS12	Incometaxes	AS22	INDAS12
IAS.16	Propertyplantandequipment	AS10 &AS6	INDAS16
IAS.17	Leases	AS19	INDAS17
IAS.18	Revenue	AS9	INDAS18
IAS.19	Employeebenefits	AS15	INDAS19
IAS.20	Accountingforgovt.grantsanddisclosureofgovtassistance	AS12	INDAS20
IAS.21	Theeffectofchangesinforeignexchangerate	AS11	INDAS21
IAS.23	Borrowingcost	AS16	INDAS23
IAS.24	Relatedpartydisclosures	AS18	INDAS24

IAS.26	Accountingandreportingbyretirementbenefitsplan	-	-
IAS.27	Separatefinancialstatements	-	-
IAS.28	Investmentsinassociateandjointventures	AS23	INDAS28
IAS.29	FinancialreportinginHyperInflationaryEconomics	-	INDAS29
IAS.32	Financialinstruments:presentation	AS31	INDAS32
IAS.33	Earningspershare	AS20	INDAS33
IAS.34	Interimfinancialreporting	AS25	INDAS34
IAS.36	Impairmentofassets	AS28	INDAS36
IAS.37	Provisions,contingentliabilitiesandcontingentassets	AS29	INDAS37
IAS.38	Intangibleasset	AS26	INDAS38
IAS.39	Financialinstrument:recognitionandmeasurement	AS30	INDAS39
IAS40	Investmentproperty	-	INDAS40
IAS41	agriculture		INDAS41

IAS3,4,5,6,9,13,14,15,22,25,30,31, and35havebeensuperseded. AS–8&issuedbyICAIiswithdrawn after theissueofAS 26

IFRS NO	TITLE	CorrespondingIndianAS	Corresponding Coveraged IndianAS
IFRS1	Firsttimeadoptionof IFRS	Notrelevant	INDAS101
IFRS2	Sharebasedpayment	Guidancenote	INDAS102
IFRS3	Businesscombinations	AS14	INDAS103
IFRS4	Insurancecontract	-	INDAS104
IFRS5	Noncurrentassetheldforsaleanddiscontinuedoperation	Partly covered byAS-24	INDAS105
IFRS6	exploration for and evaluation of mineralresources	-	INDAS106
IFRS7	Financialinstrument:disclosure	AS32	INDAS107
IFRS8	Operatingsegment	AS32	INDAS108
IFRS9	Financialinstrument	AS17	INDAS109
IFRS10	Consolidatedfinancialstatements(exposuredraftissuedforIFRS 10)	--	INDAS110
IFRS11	Jointagreement	AS27	INDAS111
IFRS12	Disclosureofinterestin otherentities	---	INDAS112
IFRS13	Fairvaluemeasurement	---	INDAS113
IFRS14	Regulatorydeferralaccount	---	INDAS114
IFRS15+	Revenuefromcontractwithcustomers	--	INDAS115

titleofthisstandardisfirsttimeadoptionofindian accountingstandards.

GeneraldifferencebetweenIFRSandIAS

1. IFRSisbasedonfairvalueconcept.But,Indianaccountingstandardsarebasedonhistoricalcost.
2. Financial statements under IFRSand Indian accounting standards differe in formandsubstance.
3. Under IFRS past errors are incorporated in the accounts of the years it pertains to,even if audited and adopted by shareholders. but, these are treated as adjustments inthecurrentyearunderIndian accountingstandards.
4. Depreciation on revalued assets needs to be routed through income statements underIFRS.ButIndianAccountingstandards disallowsuch atreatment.
5. Certain Indian standards offer accounting policy choices. These are not availableunder IRFS, eg.,useofpoolingofinterest methodin accountingforamalgamation.
6. Indian accounting standard define assets by classes which can be depreciated atgivenrates,whereasIFRSpromotestheconceptofcomponentsoffixedassetsbasedon theirusefulness.
7. Under IFRS, prior period items will be given retrospective effect in opening equity.Under Indain AS, it is not so.
8. Proposed dividend is not required to be reflected in financial statements under IFRS.Butthis is requiredtobereflectedinfinancial statementunderIndianAS.
9. Under IFRS, EPS has to be disclosed separately for continuing and discontinuingoperations.This is not required underIndianAS.
10. Under IFRS, provision made for dismantling of assets or for site closure can becapitalized.But underIAS, thiscannot becapitalized.

Standard wise differences between IFRS/IAS and Ind

ASSignificantdifferences betweenIFRS/IAS-1andIndAS-1

1. With regard to preparation of statement of profit and loss, IFRS/AS I provides anoption either to follow the single statement approach or to follow the two statementapproach.But ind As-1allows onlythesinglestatement approach.
2. Another differences lies in the terminology used. For example, in Ind AS-1 the termBalancesheetisused,whileinIFRS/IAS–1therterm‘statementoffinancialposition ‘ used . similarly, in IAS 1, the term statement of profit or loss” is used, butin IFRS/IAS -1, the term “statement of profit and loss and other comprehensiveincome“isused.
3. IFRS/IAS-1givestheoptiontoindividualentitiestofollowdifferentterminologyfor the titles of financial statement. On the other hand, Ind AS-1 gives only oneterminologyto beused byall entities.
4. IFRS/IAS-1permitstheperiodicityof52weeksforpreparationoffinancialstatements.IndAS-1 does not permit it.

Significant differences between IFRS/AS-2 and Ind AS-

2Thereis no significant difference

Significantdifferencesbetween IFRS/AS-7andIndAs-7

1. In case of other financial entities, IFRS/AS -7 gives an option to classify the interestpaid and interest and dividend received as items of operating cash flows. Ind AS-7does not provide such an option. It requires these items to be classified as itm offinancingactivityand investingactivityrespectively.
2. IFRS/IAS 7 gives an option to classify the dividend paid as an item of operatingactivity. However, Ind AS7 requires it to be classified as a part of financing activityonly.
3. IFRS/AS 7 does not require disclosure of extraordinary items, as there is no conceptofextraordinaryitem, whereasInd AS 3 requiresso.
4. Ind AS 7 does not make explicit distinction between bank borrowings and bankoverdraft,whereasIFRS/IAS 7 makeso.

ConceptualframeworkforIFRS

Accountingneedsaconceptualframework.Thereisalsoaframeworkforthepreparationand presentation offinancial statements.

Meaningofconceptualframework

A framework is the foundation of accounting standards. A conceptual frameworkacts asa constitution for the standard setting process. Concepts are the groundwork, thebasis,thefoundation upon which thesuperstructureofstandardcan becreated.

Elementsofconceptualframework

1. Objective: - the objective of financial statement is to provide information about thefinancial position, performanceandchangesin financial position ofanenterprisethatis useful to awiderangeof users in makingeconomicdecision.
2. Users:- investors,employees,lenders,suppliers,andothertraders,customers,governmentand theiragencies,public, management andothers.
3. Underlyingassumptions:-accrualbasisandgoingconcern.
4. Qualitativecharacteristics:-understandability,relevance,materiality,reliability,faithful representation, substance over form, neutrality, prudence, completeness andcomparability.
5. Elementsoffinancialstatement:-Assets,liabilities,equity,income andexpenses.
6. Conceptsof capital maintenance:- both financial and physical concepts of capitalhavebeen listed.

RequirementsofIFRS/IASs

1. Statementoffinancialposition
2. Statementofcomprehensiveincome.
3. Statementofchangesin equity.
4. Cashflowstatement
5. Comparativeinformationrequiredfortheprior reportingperiod.

6. Present all non owners changes in equity (ie comprehensive income) either in onestatementofcomprehensiveincomeorintwostatement(aseparateincomestatementand astatement ofcomprehensiveincome).
7. Present a statement of financial position(balance sheet) as at the beginning of theearliest comparative period in a complete set of financial statements when the entityappliesthenewstandard.
8. Presentastatementof cashflow.
9. Makenecessarydisclosure bywayof a note.

Financialelements

Financial elements are the important parts of conceptual framework. Some elementsare directly related ot the measurement of the financial position. Other elements are directlyrelatedto themeasurement offinancial performance.

Meaningoffinancialstatement

Financial elements are simply means the elements of financial statements. In otherwords,financialelementsaretheelementsfromwhichfinancialstatementandotherformoffinancial reports aretobeconstructed.

Definitionsoffinancialstatement

Assets:- Assets are the resources controlled by an entity as a result of past events and fromwhichfutureeconomicbenefits areexpected to flowto theentity.

Liabilities :-liabilities are the present obligations of an entity arising from past events, thesettlementofwhichisexpectedtoresultinanoutflowfromtheentityofresourcesembodyingeconomicbenefits.

Equity:- equity is the residual interest in the assets of an entity after deducting all of itsliabilities.Equityis otherwiseknown as shareholders fund.

Income:- income is the increase in economic benefits during the accounting period in theform of inflow or enhancements of assets,or decrease of liabilities that result in an increaseinequity.

Expenses:- expenses are decreases in economic benefits during the accounting period in theform of outflows or depletion of assets, or incurrence of liabilities that result in decreases inequity.

Recognition

Recognition is the process of incorporating in the statement of financial position orstatement of comprehensive income an item that meets the definition of an element andsatisfiesthecriteriaforrecognition.

Recognitioncriteriaofassets

In order for an asset to be recognized in the financial statements, it must meet thedefinition laid down in the IASB framework. The definition is “ resources controlled by theentity as a result of past events and from which future economic benefits are expected toflowto theentity.

Apart from meeting the above definition, the framework has advised the followingrecognition criteria that ought to be met before an asset is recognized in the financialstatements:

1. Theinflowofeconomicbenefitsto entityis probable.
2. Thecost/valuecanbemeasuredreliably.

Recognitioncriteriaofliabilities

In order for a liability to be recognized in the financial statement, it must meet thefollowingdefinition provided bytheframework.

“liabilities is a present obligation of the enterprise arising frompast events, thesettlement of which is expected to result in an ouflow from the enterprise of resourcesembodyingeconomicbenefits”

Revenuerecognitioncriteria

1. Economicbenefit increasesand therebyequityincreases(intheform ofinflow)
2. Assetsincreasesorliabilitydecreases,resultinginincreaseinequity(ie,economicbenefitsin creases)

Expenserecognitioncriteria

1. Economicbenefitsdecreasesasaresultofdecreaseinan asset.
2. Economic benefits decrease as a result of increase of a

liability.Measurement

Measurement simply refers to valuation. The term measurement is used to describetheprocessfordeterminingwhichnumberstopresentordiscloseinthefinancialstatements.

Basesofmeasurement

1. Historicalcost
2. Currentcost
3. Realizablecost
4. Presentvalue

Measurementcriteria

Typesofasset	Measurementatinitialrecognition
1.Financialinstruments	Fairvalue

2.Property,plantandequipment	Purchase cost + construction cost+cost tobring to the location nd condition necessarytobecapableofoperatinginthemann er intendedbythe management.
3.Intangibleasset	Purchase cost+development cost + cost tobringtothelocationandconditionnecessaryt obecapableofoperatingas intended bythemanagement.
4.Investmentproperties	Costsincludingtransactioncostaccounting policychoice:fairvalue
5.Biologicalassetsandagriculturalproduceat thepoint ofharvest.	Measuredatfairvaluelesscoststosell. Changesinfairvaluelesscoststosellarepresent edin profit orloss.
6.Assetsheldfordisposal	Fairvalue
7.Inventory	cost

Principlesofpresentation

1. Fairpresentationand compliancewith IFRS
2. Consistencyofpresentation
3. Materialityandaggregation
4. Offsetting
5. Comparativeinformation
6. Structureofstatementoffinancialposition(balancesheet)
7. Lineitems
8. Formatofstatementoffinancialposition
9. Statementofprofitorlossandothercomprehensiveincome.
10. Choiceinpresentationandbasic requirements
11. Profitorlosssectionorstatement
12. Othercomprehensiveincomesection
13. Statementofchangesinequity
14. Notes to the financial

statementsPrinciplesofdisclosuresinfinancial

statement

1. Materiality
2. Summaryof accountingpolicies
3. Sharecapitalandreserves
4. Dividends
5. Capitaldisclosures
6. Otherinformation

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