The book on Accountancy has been written strictly in accordance with the new syllabus framed by the Directorate of School Education, Government of Tamil Nadu.

As curriculum renewal is a continuous process, Accountancy Curriculum has been improved from time to time in accordance with the changing needs of the society. The present effort of reframing and updating the curriculum in Accountancy at the Higher Secondary level is an exercise based on the feed back.

The text book for Higher Secondary - First year deals with the basic framework of accounting in all its aspects. The next step is the logical application of the subject matter in maintaining records in different forms of business enterprises.

The text books for Higher Secondary - Second year has been divided into two volumes. Volume I, the present book deals with the preparation of financial statements and their analysis. The two chapters Financial Statement Analysis - Ratio Analysis and Cash Budget are included in the new syllabus, because of its significance in the sphere of decision making in business. Volume II deals with Partnership Accounts and Company Accounts.

Each chapter starts with a simple and lucid discussion of the topic followed by properly arranged worked out illustrations and ends with theoretical questions and practical exercises.

Students are strongly advised to go through the “Reference Books” as Questions for examinations need not be restricted to the exercises alone.
SYLLABUS

VOLUME I

1. Final Accounts - Adjustments [24 Periods]
   Adjustments - Closing Stock - Outstanding Expenses - Prepaid Expenses - Accrued Incomes - Incomes received in Advance - Interest on Capital - Interest on Drawings - Interest on Loan - Interest on Investments - Depreciation - Bad Debts - Provision for Bad & Doubtful Debts - Provision for Discount on Debtors - Provision for Discount on Creditors - Preparation of Final Accounts.

2. Accounts from Incomplete Records (Single Entry) [21 Periods]

3. Depreciation Accounting [14 Periods]


5. Cash Budget [7 Periods]
   Budget - Definition - Characteristics - Cash Budget - Advantages - Preparation of Cash Budget - Receipts and Payments Method.

VOLUME II

6. Partnership - Basic Concepts [14 Periods]

7. Partnership - Admission [28 Periods]
   Introduction - Adjustments - New Profit Sharing Ratio - Sacrificing Ratio - Calculation of New Profit Sharing Ratio and Sacrificing
8. Partnership - Retirement of a Partner  [19 Periods]


9. Company Accounts  [35 Periods]

Introduction - Characteristics - Types of Share Capital - Kinds of Shares - Issue of Shares - For consideration - For cash - Issue of Shares at Par - Issue of Shares at Premium - Issue of Shares at Discount - Calls in Advance - Calls in Arrears - Forfeiture of Shares - Reissue of Forfeited Shares - Capital Reserve.

CONTENTS

VOLUME - I

Chapter  | Page No.
--- | ---
1. Final Accounts - Adjustments | 1
2. Accounts from Incomplete Records (Single Entry) | 79
3. Depreciation Accounting | 126
4. Financial Statement Analysis - Ratio Analysis | 169
5. Cash Budget | 229
Books for further reference:

2. R.L. Gupta – *Principles and Practice of Accountancy*
3. T.S.Grewal – *Introduction to Accountancy*
5. Institute of Company Secretaries of India – *Principle of Accountancy.*
17. T.S.Grewal - *Analysis of Financial Statements*
18. Dr.R.K.Sharma, Dr.R.S.Popli - *Self Tutor, Accountancy.*
Learning Objectives

After studying this Chapter, you will be able to

- understand the need for making adjustments in final accounts.
- know the items in respect of which adjustments are usually made in the books of account.
- pass necessary journal entries for different adjustments.
- prepare final accounts with adjustments.

When a person starts a business he wishes to know the financial performance of his business. A convenient and universally accepted method of knowing this is to ascertain the profit or loss at yearly intervals (1st April to 31st March) and the financial position of the business on a given date. He can ascertain these by preparing the Final Accounts, which is prepared on the basis of the Trial Balance. The preparation of Final Accounts is the last step in the accounting cycle and that is why they are called Final Accounts.
Final Accounts include the preparation of
i) Trading and Profit and Loss Account; and
ii) Balance sheet.

Final accounts are the means of conveying the profitability and financial position to management, owners and interested outsiders of the business. Final accounts have to be prepared every year, to make a continuous assessment of the business for a completed period. It must be kept in mind that expenses and incomes for the full accounting period are to be taken into account.

Suppose, the firm closes its books on 31st March and rent for the month of March has not been paid, this expense (rent) has been incurred and yet to be paid. Therefore, it would be proper to include the rent for the month (March) along with the rent of the year to know the true profit. In a firm there will be a number of items, both expenses and incomes, which have to be adjusted. If such items are not adjusted, the final accounts will not reveal the true and fair picture of the business performance. All such items which need to be brought into books of account at the time of preparing final accounts are called “adjustments”.

Journal entries passed to effect the required adjustments are known as adjusting entries.

1.1 Adjustments

Some important and common items, which need to be adjusted at the time of preparing the final accounts are discussed below.

1. Closing stock
2. Outstanding expenses
3. Prepaid Expenses
4. Accrued incomes
5. Incomes received in advance
6. Interest on capital
7. Interest on drawings
8. Interest on loan
9. Interest on investment
10. Depreciation
11. Bad Debts
12. Provision for bad and doubtful debts
13. Provision for discount on debtors

Note: All adjustments are given outside the trial balance.

1.1.1 Closing Stock

The unsold goods in stock at the end of the accounting period is called as closing stock. This is to be valued at cost or market price whichever is lower.

Example:

The value of closing stock shown outside the trial balance on 31.3.2004 is Rs.1,00,000.

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Closing stock A/c</td>
<td>Dr</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Trading A/c</td>
<td></td>
<td></td>
<td>1,00,000</td>
</tr>
<tr>
<td></td>
<td>(closing stock recorded)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Value of closing stock will appear
i) on the credit side of trading account and
ii) on the assets side of balance sheet.
Trading account for the year ending 31st March, 2004

Dr. Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>By Closing Stock</td>
<td>1,00,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2004

Liabilities Rs. | Assets Rs.
---|---
Closing Stock | 1,00,000

1.1.2 Outstanding Expenses

Expenses which have been incurred but not yet paid during the accounting period for which the final accounts are being prepared are called as outstanding expenses.

**Example:** Trial balance shows salaries paid Rs.22,000. Adjustment: Salary for March 2004, Rs.2,000 not yet paid.

**Adjusting Entry**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Salaries A/c Dr</td>
<td></td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Salaries outstanding A/c</td>
<td></td>
<td></td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td>(March salary outstanding)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Outstanding expenses will be shown
i) on the debit side of Profit and Loss account by way of additions to the particular expenses and
ii) on the liabilities side of the Balance Sheet.

Profit and Loss account for the year ending 31st March, 2004

Dr. Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Salaries A/c</td>
<td>22,000</td>
<td></td>
<td>Add: Outstanding</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>24,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2004

Liabilities Rs. | Assets Rs.
---|---
Outstanding Salaries | 2,000

1.1.3 Prepaid Expenses

Expenses which have been paid in advance are called as prepaid (unexpired) expenses.

**Example:** Trial Balance for the period ending 31st March, 2004 shows Rs.15,000 as insurance premium. Adjustment: Prepaid Insurance premium Rs.7,500.

**Adjusting Entry**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Prepaid Insurance Premium A/c Dr</td>
<td></td>
<td>7,500</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Insurance Premium A/c</td>
<td></td>
<td></td>
<td>7,500</td>
</tr>
<tr>
<td></td>
<td>(Insurance premium paid in advance)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Prepaid expenses will be shown
i) on the debit side of the Profit and Loss account by way of deduction from the particular expenses and
ii) on the assets side of the Balance Sheet.
Profit & Loss Account
for the year ending 31\textsuperscript{st} March, 2004

\begin{tabular}{|c|c|c|c|c|c|}
\hline
Dr. & Cr. & \\
\hline
Particulars & Rs. & Rs. & Particulars & Rs. & Rs. \\
\hline
To Insurance premium A/c & 15,000 & & & & \\
Less: Prepaid & 7,500 & & & & \\
\hline
& & 7,500 & & & \\
\hline
\end{tabular}

Balance Sheet as on 31\textsuperscript{st} March, 2004

\begin{tabular}{|c|c|c|}
\hline
Liabilities & Rs. & Assets & Rs. \\
\hline
Prepaid Insurance premium & 7,500 & & \\
\hline
\end{tabular}

1.1.4 Accrued Incomes or Outstanding Incomes

Income which has been earned but not received during the accounting period is called as \textit{accrued income}.

\textbf{Example:} Credit side of Trial Balance (31.3.2004) shows commission received Rs.8,000. Adjustment: Commission accrued but not yet received Rs.2,000.

\textbf{Adjusting Entry}

\begin{tabular}{|c|c|c|c|}
\hline
Date & Particulars & Debit Rs. & Credit Rs. \\
\hline
2004 Mar 31 & Accrued commission A/c & Dr & 2,000 & 2,000 \\
& To Commission A/c (commission earned but not received) & & & \\
\hline
\end{tabular}

Accrued income will be shown
i) on the credit side of Profit and Loss account by way of addition to particular income and
ii) on the assets side of the Balance Sheet

Profit & Loss Account
for the year ending 31\textsuperscript{st} March, 2004

\begin{tabular}{|c|c|c|c|c|c|}
\hline
Dr. & Cr. & \\
\hline
Particulars & Rs. & Rs. & Particulars & Rs. & Rs. \\
\hline
By Commission received & & 8,000 & Add: Accrued Comm -ission & 2,000 & 10,000 \\
\hline
\end{tabular}

Balance Sheet as on March 31, 2004

\begin{tabular}{|c|c|c|}
\hline
Liabilities & Rs. & Assets & Rs. \\
\hline
Accrued Commission & 2,000 & & \\
\hline
\end{tabular}

1.1.5 Incomes Received in Advance

Income received during a particular accounting period for the work to be done in future period is called as \textit{income received in advance}.

\textbf{Example:} Trial Balance for the period ending 31st March, 2004 shows Rent received Rs.25,000. Adjustment: Rent received in advance Rs.5,000.

\textbf{Adjusting Entry}

\begin{tabular}{|c|c|c|c|}
\hline
Date & Particulars & Debit Rs. & Credit Rs. \\
\hline
2004 Mar 31 & Rent received A/c & Dr & 5,000 & 5,000 \\
& To Rent received in advance A/c (rent received in advance) & & & \\
\hline
\end{tabular}

Incomes received in advance will be shown
i) on the credit side of the Profit and Loss account by way of deducting from the particular income and
ii) on the liabilities side of the Balance Sheet.
Profit & Loss Account
for the year ending 31st March, 2004

Dr. Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>By Rent received</td>
<td>25,000</td>
<td></td>
<td>Less: Rent received in advance</td>
<td>5,000</td>
<td>20,000</td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent received in advance</td>
<td>5,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

1.1.6 Interest on Capital

In order to see whether the business is really earning profit or not, it is desirable to charge interest on capital at a certain rate.

Example: As per Trial Balance, capital as on 31.3.2004 is Rs.4,00,000. Adjustment: Provide 6% interest on capital.

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Interest on capital A/c</td>
<td>Dr</td>
<td>24,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Capital A/c (6% interest on capital)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Transfer Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Profit &amp; Loss A/c</td>
<td></td>
<td>24,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Interest on Capital A/c (Interest on capital transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td>24,000</td>
<td></td>
</tr>
</tbody>
</table>

Interest on capital will be shown
i) on the debit side of Profit and Loss account and
ii) on the liabilities side of the Balance Sheet by way of addition to the capital.

Profit & Loss Account
for the year ending 31st March, 2004

Dr. Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Interest on Capital A/c</td>
<td>24,000</td>
</tr>
</tbody>
</table>

Balance Sheet as on March 31, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>4,00,000</td>
<td></td>
</tr>
<tr>
<td>Add: Interest on capital</td>
<td>24,000</td>
<td>4,24,000</td>
</tr>
</tbody>
</table>

1.1.7 Interest on Drawings

Amount withdrawn by the owner for his personal use is called as drawings. When interest on capital is allowed, then interest on drawings is charged from the owner. Interest on drawings is an income for the business and will reduce the capital of the owner.
Example: The trial balance shows the following:

Rs.
Capital as on 31.3.2004 4,00,000
Drawings as on 31.3.2004 30,000

Adjustment: Charge interest on drawings @ 5%.

### Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Capital A/c Dr</td>
<td></td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Interest on Drawings A/c</td>
<td></td>
<td></td>
<td>1,500</td>
</tr>
<tr>
<td></td>
<td>(Interest on drawings)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

To bring interest on drawings to Profit and Loss account the following transfer entry is required.

### Transfer Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Interest on drawings A/c Dr</td>
<td></td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Profit &amp; Loss A/c</td>
<td></td>
<td></td>
<td>1,500</td>
</tr>
<tr>
<td></td>
<td>(Interest on drawings)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Interest on drawings will be shown
i) on the credit side of Profit and Loss account and
ii) on the liabilities side of the Balance Sheet by way of addition to the drawings which are ultimately deducted from the capital.

### Profit & Loss Account

for the year ending 31st March, 2004

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>By Interest on</td>
<td>1,500</td>
</tr>
<tr>
<td>drawings</td>
<td></td>
</tr>
</tbody>
</table>

### Balance Sheet as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>4,00,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>30,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest on drawings</td>
<td>1,500</td>
<td>31,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>3,68,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

1.1.8 Interest on Loan (Outstanding)

Borrowings from banks, financial institutions and outsiders for business are called loans. Amount payable towards interest on loan is an expense for the business.

Example: The trial balance (31.3.2004) shows the following:

Bank loan @ 10% on 1.4.03   Rs. 4,00,000
Interest paid              Rs. 14,000

Adjustment: Provide for interest on bank loan outstanding.

### Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Interest on Bank loan A/c Dr</td>
<td></td>
<td>26,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Interest outstanding A/c</td>
<td></td>
<td></td>
<td>26,000</td>
</tr>
<tr>
<td></td>
<td>(the interest on bank loan)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Interest on loan outstanding will be shown
i) on the debit side of the Profit and Loss account by way of addition to the appropriate interest account and
ii) on the liability side of the Balance sheet by way of addition to the particular loan account.
Profit & Loss Account
for the year ending 31st March, 2004

Dr. Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Interest on loan</td>
<td>14,000</td>
<td></td>
<td>Add: Interest outstanding</td>
<td>26,000</td>
<td>40,000</td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2004

Liabilities Rs. Rs. Assets Rs. Rs.

<p>| Bank loan @ 10%               | 4,00,000 |     | Investments @10%             | 5,00,000 |</p>
<table>
<thead>
<tr>
<th>Add: Interest outstanding</th>
<th>26,000</th>
<th></th>
<th>Interest received on investments</th>
<th>40,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: Interest on Bank loan @ 10% on Rs. 4,00,000 for the year

= Rs. 4,00,000 x 10/100 = Rs. 40,000

Less: Interest paid as per Trial balance = Rs. 14,000

Interest outstanding (Yet to be paid) = Rs. 26,000

1.1.9 Interest on Investment:

Interest receivable on investments is an income for the business.

Example: The Trial Balance (31.03.04) shows the following:
Investments @ 10% Rs. 5,00,000
Interest received on investments Rs. 40,000

Adjustment:

Provide for accrued interest on investments Rs. 10,000.

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Accrued interest on investments A/c</td>
<td></td>
<td>Dr 10,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Interest received A/c</td>
<td></td>
<td></td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td>(Accrued interest on investments provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Accrued interest on investments (outstanding interest receivable) will be shown

i) On the credit side of the Profit and Loss account by way of addition to the appropriate interest account and

ii) On the assets side of the balance sheet by way of addition to the investments account.

Profit and loss account for the period year 31st March, 2004

Dr. Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>By Interest received</td>
<td>40,000</td>
<td></td>
<td>Add: Accrued interest</td>
<td>10,000</td>
<td>50,000</td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2004

Liabilities Rs. Rs. Assets Rs. Rs.

| Investments                  | 5,00,000 |     | Add: Accrued Interest        | 10,000 | 5,10,000 |
1.1.10 Depreciation

Depreciation is the reduction in the value of fixed assets due to its use or obsolescence. Generally depreciation is charged at some percentage on the value of fixed asset.

Example: The Trial balance shows the value of furniture on 31.3.2004 as Rs.60,000. Adjustment: Furniture is to be depreciated at 10%.

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Depreciation A/c Dr</td>
<td></td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Furniture A/c</td>
<td></td>
<td></td>
<td>6,000</td>
</tr>
<tr>
<td></td>
<td>(10% depreciation on furniture)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

To bring depreciation into Profit and Loss account the following transfer entry is required.

Transfer Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Profit &amp; Loss A/c Dr</td>
<td></td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td></td>
<td>6,000</td>
</tr>
<tr>
<td></td>
<td>(10% depreciation on furniture transferred to Profit and Loss account)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Depreciation will be shown

i) on the debit side of Profit and Loss account and

ii) on the assets side of the Balance Sheet by way of deduction from the value of concerned asset.

1.1.11 Bad Debts

Debts which cannot be recovered are called bad debts. It is a loss for the business.

Example: The trial balance as on 31st March 2004 shows, Sundry debtors Rs.52,500. Adjustment: Write off Rs. 2,500 as bad debts.

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Bad debts A/c Dr</td>
<td></td>
<td>2,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Sundry debtors A/c</td>
<td></td>
<td></td>
<td>2,500</td>
</tr>
<tr>
<td></td>
<td>(Bad debts written off)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

To transfer bad debts to Profit and Loss account the following transfer entry is required.

Transfer Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>Profit &amp; Loss A/c Dr</td>
<td></td>
<td>2,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bad debts A/c</td>
<td></td>
<td></td>
<td>2,500</td>
</tr>
<tr>
<td></td>
<td>(Bad debts transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Bad debts will be shown
i) on the debit side of Profit and Loss account and
ii) on the assets side of the Balance Sheet by way of deduction from sundry debtors.

### Profit & Loss Account
for the year ending 31st March, 2004

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To Bad debts A/c</td>
<td>2,500</td>
</tr>
</tbody>
</table>

### Balance Sheet as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors</td>
<td>52,500</td>
<td></td>
<td>Less: Bad debts written off</td>
<td>2,500</td>
<td>50,000</td>
</tr>
</tbody>
</table>

**Note:**
**Bad Debts Account**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To Sundry debtors A/c</td>
<td>2,500</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### 1.1.12 Provision for Bad and Doubtful Debts

Every business suffers a percentage of bad debts over and above the debts definitely known as irrecoverable and written off as Bad (Bad debts written off). If Sundry debtors figure is to be shown correctly in the Balance sheet provision for bad and doubtful debts must be adjusted. This Provision for bad and doubtful debts is generally provided at a certain percentage on Debtors, based on past experience.

While preparing final accounts, the bad debts written off given in adjustment is first deducted from the Sundry debtors then on the balance amount (Sundry debtors – Bad debt written off) provision for bad and doubtful debts calculated.

### Example:
The trial balance shows on 31.3.2004, Sundry Debtors as Rs.60,000.

Adjustment: Provide 5% provision for bad & doubtful debts on Sundry debtors.

### Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mar 31</td>
<td>Profit &amp; Loss A/c</td>
<td>Dr</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Provision for bad &amp; doubtful debts A/c</td>
<td></td>
<td></td>
<td>3,000</td>
</tr>
<tr>
<td></td>
<td>(5% provision for bad and doubtful debts)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Provision for bad and doubtful debts will be shown
i) on the debit side of Profit and Loss Account and
ii) on the assets side of the Balance Sheet by way of deduction from Sundry debtors (after Bad debts written off if any).

### Profit & Loss Account
for the year ending 31st March, 2004

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To Provision for bad and doubtful debts A/c</td>
<td>3,000</td>
</tr>
</tbody>
</table>

### Balance Sheet as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors</td>
<td>60,000</td>
<td></td>
<td>Less: Provision for bad and doubtful debts</td>
<td>3,000</td>
<td>57,000</td>
</tr>
</tbody>
</table>
Example: The Trial Balance as on 31st March 2004 shows the following:

Sundry Debtors Rs. 81,200

Adjustment: Write off Rs. 1,200 as bad debts. Create a provision for Bad and doubtful debts @ 5% on Sundry Debtors.

### Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004 Mar 31</td>
<td>Bad debts A/c</td>
<td>Dr</td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Sundry debtors A/c</td>
<td></td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Bad debts written off)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>&quot;</td>
<td>Dr</td>
<td></td>
<td>4,000</td>
</tr>
<tr>
<td></td>
<td>Profit and Loss A/c</td>
<td></td>
<td></td>
<td>4,000</td>
</tr>
<tr>
<td></td>
<td>(5% provision for bad &amp; doubtful debts)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: 5% should be calculated on Rs. 80,000 (i.e. The amount of Sundry debtors after writing off Bad Debts).

### Profit and Loss Account for the year ending 31st March, 2004

<table>
<thead>
<tr>
<th>Dr. Particulars</th>
<th>Rs.</th>
<th>Cr. Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Bad Debts A/c</td>
<td>1,200</td>
<td>To Provision for Bad &amp; doubtful debts A/c</td>
<td>4,000</td>
</tr>
</tbody>
</table>

### Balance Sheet as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors</td>
<td>81,200</td>
<td></td>
</tr>
<tr>
<td>Less: Bad debts written off</td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td>Less: Provision for Bad &amp; Doubtful debts</td>
<td>80,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>76,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Note:

**Bad Debts Account**

<table>
<thead>
<tr>
<th>Dr. Particulars</th>
<th>Rs.</th>
<th>Cr. Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Sundry Debtors A/c</td>
<td>1,200</td>
<td>By Profit &amp; Loss A/c</td>
<td>1,200</td>
</tr>
</tbody>
</table>

**1.1.13 Provision for Discount on Debtors**

To motivate the debtors to make prompt payments, cash discount may be allowed to them. After providing provision for bad and doubtful debts, the remaining debtors are called as **good debtors**. They may pay their dues in time and avail themselves of the cash discount permissible. So a provision for discount on good debtors at a certain percentage may have to be created.

Example: The Trial Balance as on 31st March 2004 shows the following:

Sundry debtors Rs. 45,000

Adjustment: Create 2% provision for discount on Debtors.

### Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004 Mar 31</td>
<td>Profit and Loss Account</td>
<td>Dr</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Provision for discount on Debtors</td>
<td></td>
<td></td>
<td>900</td>
</tr>
<tr>
<td></td>
<td>(2% provision for discount on Debtors)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Profit and Loss Account for the period ended 31st March, 2004

<table>
<thead>
<tr>
<th>Dr. Particulars</th>
<th>Rs.</th>
<th>Cr. Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Provision for discount on debtors</td>
<td>900</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Balance Sheet on 31st March 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors</td>
<td>45,000</td>
<td></td>
</tr>
<tr>
<td>Less: Provision for discount on debtors</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td></td>
<td>44,100</td>
<td></td>
</tr>
</tbody>
</table>

Example: The trial balance shows on 31.03.2004,
Sundry debtors Rs. 85,000

Adjustments: Bad debts written off Rs. 5,000. Provide @ 5% provision for bad and doubtful debts and @ 2% provision for discount on debtors.

Note:

- Debtors as per Trial Balance: Rs. 85,000
- Less: Bad debts: Rs. 5,000
- Amount for which Bad & doubtful debts is to be calculated: Rs. 80,000
- Less: 5% Provision for bad and doubtful debts: Rs. 4,000
- Estimated value of good debtors: Rs. 76,000
- Less: 2% Provision for discount on debtors: Rs. 1,520
- Adjusting Entries:

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mar 31</td>
<td>Bad debts A/c</td>
<td>5,000</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>To Sundry debtors A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Bad debts written off)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>** Profit and Loss A/c</td>
<td>4,000</td>
<td>4,000</td>
</tr>
<tr>
<td></td>
<td>To Provision for bad and doubtful debts A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(5% Provision for bad and doubtful debts)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Provision for discount on debtors will be shown
i) on the debit side of Profit and Loss account and
ii) on the asset side of the Balance sheet by way of deduction from Sundry debtors (after deducting bad debts written off and provision for bad and doubtful debts).

Profit and Loss Account for the year ended 31st March, 2004

<table>
<thead>
<tr>
<th>Dr. Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Bad debts A/c</td>
<td>5,000</td>
</tr>
<tr>
<td>To Provision for Bad and doubtful debts A/c</td>
<td>4,000</td>
</tr>
<tr>
<td>To Provision for discount on debtors</td>
<td>1,520</td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors</td>
<td>85,000</td>
<td>80,000</td>
</tr>
<tr>
<td>Less: Bad debts</td>
<td>5,000</td>
<td>4,000</td>
</tr>
<tr>
<td>Less: Provision for bad and doubtful debts A/c</td>
<td>4,000</td>
<td>76,000</td>
</tr>
<tr>
<td>Less: Provision for discount on debtors</td>
<td>1,520</td>
<td>74,480</td>
</tr>
</tbody>
</table>
Note:

Transfer Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004 Mar 31</td>
<td>Profit &amp; Loss A/c</td>
<td></td>
<td>Dr</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>To Bad debts A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Bad debts A/c closed by transfer to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Bad Debts Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004 Mar 31</td>
<td>To Sundry Debtors A/c</td>
<td>5,000</td>
<td>Mar 31</td>
<td>By Profit &amp; Loss A/c</td>
<td>5,000</td>
</tr>
</tbody>
</table>

1.1.14 Provision for Discount on Creditors

Similar to cash discount allowed to debtors, the firm may have a chance to receive the cash discount from the creditors for prompt payment. Provision for discount on Creditors is calculated at a certain percentage on Sundry Creditors.

**Example:** The Trial balance for the year ended 31st March, 2004 shows Sundry Creditors Rs.50,000.

**Adjustment:**

Create a provision for discount on creditors @ 2%.

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>LF</th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004 Mar 31</td>
<td>Provision for discount on creditors A/c</td>
<td>Dr</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Profit and Loss A/c</td>
<td></td>
<td></td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>(2% Provision for discount on creditors)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Provision for discount on creditors will be shown

1. on the credit side of Profit and Loss account and
2. on the liabilities side of the Balance sheet by way of deduction from Sundry creditors.

**Profit and Loss Account for the year ended 31st March, 2004**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>By Provision for discount on Creditors</td>
<td></td>
<td></td>
<td>1,000</td>
</tr>
</tbody>
</table>

**Balance Sheet as on 31st March, 2004**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry creditors</td>
<td>50,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Provision for discount on creditors</td>
<td>1,000</td>
<td></td>
<td></td>
<td>49,000</td>
<td></td>
</tr>
<tr>
<td>Sl. No.</td>
<td>Type of Adjustment</td>
<td>Adjustment Entry</td>
<td>How dealt with in →</td>
<td></td>
<td></td>
</tr>
<tr>
<td>--------</td>
<td>------------------------------------</td>
<td>----------------------------------------------------------------------------------</td>
<td>------------------------------------------------------------------------------------</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Trading or Profit and Loss Account</td>
<td>Balance Sheet</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1.</td>
<td>Closing stock</td>
<td>Closing Stock A/c Dr To Trading A/c</td>
<td>Credit side of the Trading A/c</td>
<td>Asset side.</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Outstanding Expenses:</td>
<td>Respective Expenses A/c Dr To Respective outstanding expenses A/c</td>
<td>i. If the outstanding is an item chargeable to Trading A/c, add the outstanding expenses with relevant expenses in the debit side of the Trading A/c.</td>
<td>Liabilities side.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Wages, Rent, Salaries etc.)</td>
<td></td>
<td>ii. If it is an item chargeable to Profit and Loss A/c, add the outstanding expenses to the relevant expenses in the debit side of the Profit and Loss A/c.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Example: Wages A/c To Wages outstanding A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Salaries A/c Dr To Salaries outstanding A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Insurance Premium)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Accrued Income (Commission)</td>
<td>Accrued Income A/c Dr To Respective Income A/c</td>
<td>Credit side of Profit and Loss A/c by way of addition to respective Income A/c.</td>
<td>Assets side.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Example: Accrued Commission A/c To Commission A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Income received in advance (Rent)</td>
<td>Respective Income A/c Dr To Respective Income received in advance A/c</td>
<td>Credit side of Profit and Loss A/c by way of deduction from the respective income A/c.</td>
<td>Liabilities side.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Example: Rent received A/c Dr To Rent received in advance A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Interest on Capital</td>
<td>Interest on Capital A/c Dr To Capital A/c</td>
<td>Debit side of Profit and Loss A/c by way of addition to the Capital</td>
<td>Liabilities side.</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
<td></td>
</tr>
<tr>
<td>7.</td>
<td>Interest on Drawings</td>
<td>Capital A/c Dr To Interest on drawings A/c</td>
<td>Credit side of the Profit and Loss A/c</td>
<td>Liabilities side by way of addition to the drawings which are ultimately deducted from the Capital.</td>
<td></td>
</tr>
<tr>
<td>8.</td>
<td>Interest on Loan (Interest on Bank Loan)</td>
<td>Interest A/c Dr To Interest Outstanding A/c Example: Interest on Bank Loan A/c To Interest Outstanding A/c</td>
<td>Debit side of Profit and Loss A/c by way of addition to the appropriate interest A/c</td>
<td>Liabilities side by way of addition to the particular loan A/c</td>
<td></td>
</tr>
<tr>
<td>9.</td>
<td>Interest on Investments</td>
<td>Accrued Interest on investments A/c Dr To Interest received A/c</td>
<td>Credit side of Profit and Loss A/c by way of addition to the appropriate interest A/c.</td>
<td>Assets side by way of addition to the particular investment A/c</td>
<td></td>
</tr>
<tr>
<td>10.</td>
<td>Depreciation on Fixed Asset</td>
<td>Depreciation A/c Dr To Fixed Asset A/c Example: Depreciation A/c Dr To Machinery A/c</td>
<td>Debit side of Profit and Loss A/c.</td>
<td>Assets side by way of deduction from the concerned asset account.</td>
<td></td>
</tr>
<tr>
<td>11.</td>
<td>Bad debts</td>
<td>Bad debts A/c Dr To Sundry debtors A/c</td>
<td>Debit side of Profit and Loss A/c</td>
<td>Assets side by way of deduction from Sundry debtors</td>
<td></td>
</tr>
</tbody>
</table>
| 12. | Provision for Bad and doubtful debts. | Profit and Loss A/c Dr To Provision for Bad and doubtful debts A/c | i. If the provision for bad and doubtful debts is given outside the Trial balance, then it is shown on the debit side of Profit and Loss account.  

  ii. If provision for bad and doubtful debts is given in the Trial Balance (Old) and also in the adjustment (New):  

  - Add new provision for bad and doubtful debts with bad debts written off.  

  a) If the old provision for bad and doubtful debts is less than the above total, then the difference will be shown on the debit side of the Profit and Loss account. | Assets side by way of deducting New Provision alone from Sundry debtors |
## Format:

Trading and Profit and Loss Account of
Thiru............ for the year ending 31st March, ........

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td>xxx</td>
<td></td>
<td>By Sales</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>To Purchases</td>
<td>xxx</td>
<td></td>
<td>Less: Sales returns</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>Less: Purchases returns</td>
<td>xxx</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Wages</td>
<td>xxx</td>
<td></td>
<td>By Closing Stock</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>Add: Outstanding wages</td>
<td>xxx</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Factory rent</td>
<td>xxx</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Prepaid Factory rent</td>
<td>xxx</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>xxx</td>
<td></td>
<td>(Transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Salaries</td>
<td>xxx</td>
<td></td>
<td>By Gross Profit b/d</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>Add: Outstanding Salaries</td>
<td>xxx</td>
<td></td>
<td>(Transferred from Trading A/c)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Insurance premium</td>
<td>xxx</td>
<td></td>
<td>By Commission received</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Prepaid Insurance Premium</td>
<td>xxx</td>
<td></td>
<td>Add: Commission accrued but not yet received</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>To Interest on Capital</td>
<td>xxx</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest on loan</td>
<td>xxx</td>
<td></td>
<td>By Rent received</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>Add: Interest on loan</td>
<td>xxx</td>
<td></td>
<td>Less: Rent received in advance</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>outstanding</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>By Interest on drawings</td>
<td>xxx</td>
<td></td>
</tr>
</tbody>
</table>

b) If the old provision for bad and doubtful debts is more than the above total, then the differences should be shown on the credit side of the Profit and Loss account.

13. Provision for Discount on Debtors

14. Provision for Discount on Creditors
To Depreciation on:
- Fixed Assets,
- Buildings, Machinery,
- Furniture etc.

By Discount received
By New provision for
discount on creditors
(given in adjustment)
Less: Old provision

To Bad Debts

Add: New Bad Debts
(given in adjustment)
Add: New Provision for
bad & doubtful debts
(given in adjustment)

Less: Old Provision

To Discount allowed

To New Provision for
discount on debtors
(given in adjustment)
Less: Old Provision

To Net profit
(Transferred to
Capital A/c)

Less: Drawings

Interest on drawings

Less: Income tax

Sundry Creditors
Less: Provision for
Discount on Creditors

Loan
Add: Interest on loan
outstanding
Outstanding Expenses
Incomes received in
advance

Less: Provision for
Bad & doubtful debts

Less: Provision for
discount on debtors

Land and Buildings
Less: Depreciation

Plant & Machinery
Less: Depreciation

Furniture

Less: Depreciation

Goodwill
Less: Written off

Closing stock
Prepaid expenses
Accrued Commission

2.2 Preparation of Final Accounts

Illustration : 1

Pass necessary adjustment entries for the following adjustments:

1. Salaries outstanding Rs.20,000
2. Prepaid Insurance Rs.400
3. Interest accrued on investments Rs.1000
4. Commission received in advance Rs.2,000
5. To provide 10% interest on capital of Rs.5,00,000
6. Closing Stock Rs.4,00,000

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td></td>
<td></td>
<td>Cash in Hand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add: Net Profit</td>
<td></td>
<td></td>
<td>Cash at Bank</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(or)</td>
<td></td>
<td></td>
<td>Sundry debtors</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Net Loss</td>
<td></td>
<td></td>
<td>Less: Bad debts</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>written off</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Balance Sheet of Thiru .......... as on 31st March, ............

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td></td>
<td></td>
<td>Cash in Hand</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add: Net Profit</td>
<td></td>
<td></td>
<td>Cash at Bank</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(or)</td>
<td></td>
<td></td>
<td>Sundry debtors</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Net Loss</td>
<td></td>
<td></td>
<td>Less: Bad debts</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>written off</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Less: Drawings

Interest on drawings

Less: Income tax

Sundry Creditors
Less: Provision for
Discount on Creditors

Loan
Add: Interest on loan
outstanding
Outstanding Expenses
Incomes received in
advance

Less: Provision for
Bad & doubtful debts

Less: Provision for
discount on debtors

Land and Buildings
Less: Depreciation

Plant & Machinery
Less: Depreciation

Furniture

Less: Depreciation

Goodwill
Less: Written off

Closing stock
Prepaid expenses
Accrued Commission

xxxx

xxx
### Solution:

**Adjustment Entries**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Salaries A/c</td>
<td>Dr</td>
<td>20,000</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td>To Salaries outstanding A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Salaries outstanding)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Prepaid Insurance A/c</td>
<td>Dr</td>
<td>400</td>
<td>400</td>
</tr>
<tr>
<td></td>
<td>To Insurance A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Insurance prepaid)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Accrued Interest A/c</td>
<td>Dr</td>
<td>1,000</td>
<td>1,000</td>
</tr>
<tr>
<td></td>
<td>To Interest A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Interest accrued on investments)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Commission received A/c</td>
<td>Dr</td>
<td>2,000</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td>To Commission received in advance A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Commission received in advance)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Interest on Capital A/c</td>
<td>Dr</td>
<td>50,000</td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td>To Capital A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(10% interest on capital)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Closing Stock A/c</td>
<td>Dr</td>
<td>4,00,000</td>
<td>4,00,000</td>
</tr>
<tr>
<td></td>
<td>To Trading A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Closing stock recorded)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Illustration : 2

Pass necessary adjusting entries for the following adjustments:

1. Interest charged on drawings Rs.5,000
2. Interest on loan outstanding Rs.3,000
3. Depreciation at 10% is to be charged on Machinery Rs.3,00,000.

### Solution:

**Journal Entries**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Capital A/c</td>
<td>Dr</td>
<td>5,000</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>To Interest on drawings A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Interest charged on drawings)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Interest on loan A/c</td>
<td>Dr</td>
<td>3,000</td>
<td>3,000</td>
</tr>
<tr>
<td></td>
<td>To Interest outstanding A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Interest due on loan)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Depreciation A/c</td>
<td>Dr</td>
<td>30,000</td>
<td>30,000</td>
</tr>
<tr>
<td></td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation on Machinery)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Bad debts A/c</td>
<td>Dr</td>
<td>2,000</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td>To Sundry debtors A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Bad debts written off)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Profit and Loss A/c</td>
<td>Dr</td>
<td>1,200</td>
<td>1,200</td>
</tr>
<tr>
<td></td>
<td>To Provision for Bad &amp; doubtful debts A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(2% provision for Bad &amp; doubtful debts)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Provision for discount on creditors A/c</td>
<td>Dr</td>
<td>2,000</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td>To Profit &amp; Loss A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(2% provision for discount on Creditors)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
**Illustration : 3**

The Trial Balance as on 31st March 2004 shows Sundry debtors as Rs.12,000 and bad debts as Rs.300.

No adjustment given.

**Solution:**

**Profit and Loss Account for the year ended 31st March 2004**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Bad Debts</td>
<td>300</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Balance Sheet as on 31st March 2004**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors</td>
<td>12,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Illustration : 4**

The Trial Balance as on 31st March 2004 shows the following:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors</td>
<td>40,800</td>
</tr>
<tr>
<td>Bad debts written off</td>
<td>1,400</td>
</tr>
</tbody>
</table>

Adjustment: Write off Rs.800/- as bad debts.

**Solution:**

**Adjusting Entry**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bad debts A/c</td>
<td>Dr.</td>
<td>800</td>
<td>800</td>
</tr>
<tr>
<td></td>
<td>To Sundry debtors A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(bad debts written off)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Profit and Loss Account for the year ending 31st March 2004**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Bad Debts</td>
<td>1,400</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add: Bad debts</td>
<td></td>
<td>800</td>
<td>Written off</td>
<td>2,200</td>
<td></td>
</tr>
</tbody>
</table>

**Balance Sheet as on 31st March 2004**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors</td>
<td>40,800</td>
<td></td>
<td>Less: Bad debts written off</td>
<td>800</td>
<td>40,000</td>
</tr>
</tbody>
</table>

**Note:**

In the above example, Trial Balance shows Rs.1,400 as Bad debts. This means the double entry in respect of Rs.1,400 i.e. debiting Bad debts and crediting Sundry debtors is already completed. Hence Rs.1,400 found in the Trial Balance will not affect the sundry debtors of Rs.40,800.

But for the adjustment given outside the Trial Balance, the adjustment has to be done after the preparation of Trial Balance, and this would result in increasing bad debts by Rs.800 and decreasing debtors by Rs.800.

**Profit and Loss Account for the year ending 31st March 2004**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d</td>
<td>1,400</td>
<td>By Profit &amp; Loss</td>
<td>2,200</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Sundry Debtors</td>
<td>800</td>
<td>2,200</td>
<td></td>
<td>2,200</td>
<td></td>
</tr>
</tbody>
</table>
Illustration : 5

The following items are found in the Trial Balance of Mr. Vivekanandan as on 31st March 2004.

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors</td>
<td>Rs. 64,000</td>
</tr>
<tr>
<td>Bad debts</td>
<td>Rs. 1,200</td>
</tr>
<tr>
<td>Provision for Bad &amp; doubtful debts</td>
<td>Rs. 2,800</td>
</tr>
</tbody>
</table>

Adjustment:

Provide for bad & doubtful debts at 5% on Sundry debtors.

Give necessary entries and show how these items will appear in the final accounts.

Solution:

Step :1

Transfer Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>Provision for bad &amp; doubtful debts A/c</td>
<td>Dr.</td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bad debts A/c (Transfer of bad debts)</td>
<td></td>
<td></td>
<td>1,200</td>
</tr>
</tbody>
</table>

Note:

If Provision for bad and doubtful debts account is maintained, the loss on account of bad debts is taken to Profit and Loss Account not directly but via provision for bad and doubtful debts account.

Step 2:

Apply the rule:

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bad debts</td>
<td>Rs. 1,200</td>
</tr>
<tr>
<td>Add: New Provision required</td>
<td></td>
</tr>
<tr>
<td>5% on 64,000</td>
<td>Rs. 3,200</td>
</tr>
<tr>
<td>Total required</td>
<td>Rs. 4,400</td>
</tr>
<tr>
<td>Less: Existing provision</td>
<td>Rs. 2,800</td>
</tr>
<tr>
<td>Amount required</td>
<td>Rs. 1,600</td>
</tr>
</tbody>
</table>

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>Profit and Loass A/c Dr.</td>
<td></td>
<td>1,600</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Provision for bad and doubtful debts A/c</td>
<td></td>
<td></td>
<td>1,600</td>
</tr>
<tr>
<td></td>
<td>(Additional provision for bad and doubtful debts)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Profit and Loss Account for the Period ended 31st March 2004

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Provision for bad &amp; doubtful debts A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bad debts</td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td>Add: New provision</td>
<td>3,200</td>
<td></td>
</tr>
<tr>
<td>Less: Old provision</td>
<td>2,800</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,600</td>
</tr>
</tbody>
</table>

Total: 1,600
Balance Sheet as on 31st March 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debtors</td>
<td>64,000</td>
<td></td>
<td>Less: Provision for Bad &amp; doubtful debts (New)</td>
<td>3,200</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>60,800</td>
</tr>
</tbody>
</table>

Note:

When the existing provision is larger than what is required even after the transfer of bad debts, the second step will give a negative figure, which indicates that the profit and loss account is to be credited with the excess.

Illustration : 6

Following are the balances extracted from the Trial Balance of Mr. Mohan as on 31st March, 2002.

Trial Balance as on 31st March, 2002

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Bad debts</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Provision for bad &amp; doubtful debts</td>
<td>10,000</td>
<td></td>
</tr>
</tbody>
</table>

Adjustment

Create provision for bad & doubtful debts @ 5% on Sundry Debtors.

Pass adjusting entry and show how these items will appear in the final accounts.

Solution:

Adjusting Entry

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002 Mar 31</td>
<td>Provision for Bad and Doubtful debts A/c Dr</td>
<td></td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Profit &amp; Loss A/c Dr</td>
<td></td>
<td></td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td>(Excess: 5% Provision for bad and doubtful debts)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Profit and Loss Account for the year ending 31st March, 2002

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>By Provision for bad and doubtful debts:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Old Provision for bad &amp; doubtful debts</td>
<td>10,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Bad debts 5000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>New Provision</td>
<td>3,000</td>
<td>8,000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2002

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors</td>
<td>60,000</td>
<td></td>
<td>Less: New Provision</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>57,000</td>
</tr>
</tbody>
</table>
Illustration : 7

The following balances have been extracted from the trial balance of Mr. Ashok as on 31.3.2002.

Trial Balance of Mr. Ashok as on 31st March, 2002

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debtors</td>
<td>2,01,200</td>
<td></td>
</tr>
<tr>
<td>Bad debts</td>
<td>9,400</td>
<td></td>
</tr>
<tr>
<td>Provision for bad &amp; doubtful debts</td>
<td>24,000</td>
<td></td>
</tr>
<tr>
<td>Provision for Discount on debtors</td>
<td>1,200</td>
<td></td>
</tr>
<tr>
<td>Discount allowed</td>
<td>18,600</td>
<td></td>
</tr>
</tbody>
</table>

Adjustments:
1. Write off additional bad debts Rs. 4,800
2. Create Provision of 10% for bad & doubtful debts on debtors.
3. Create Provision of 2% for discount on debtors.

Show how these items will appear in the Profit and Loss Account and Balance Sheet.

Solution:

Profit and Loss Account of Mr. Ashok
for the year ending 31st March, 2002

Dr. Cr.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Provision for Bad &amp; Doubtful</td>
<td></td>
<td></td>
</tr>
<tr>
<td>debts A/c</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bad debts</td>
<td>9,400</td>
<td></td>
</tr>
<tr>
<td>Add: Bad debts written off</td>
<td>4,800</td>
<td></td>
</tr>
<tr>
<td></td>
<td>14,200</td>
<td></td>
</tr>
<tr>
<td>Add: New Provision</td>
<td>19,640</td>
<td></td>
</tr>
</tbody>
</table>

Less: Old provision

To Provision for discount on debtors
Discount allowed 18,600
Add: New provision 3,535

Less: Old provision 1,200

Balance Sheet as on 31st March, 2002

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors</td>
<td>2,01,200</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: Bad debts</td>
<td></td>
<td>4,800</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>written off</td>
<td></td>
<td>1,96,400</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Less: New provision for bad &amp; doubtful debts</td>
<td>19,640</td>
<td></td>
<td></td>
<td>1,76,760</td>
<td></td>
</tr>
<tr>
<td>Less: New Provision for discount on debtors</td>
<td>3,535</td>
<td></td>
<td></td>
<td>1,73,225</td>
<td></td>
</tr>
</tbody>
</table>

Illustration : 8

From the following trial balance of a trader, make out a Trading and Profit and Loss account and Balance Sheet as on 31st March, 2000.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td></td>
<td>4,20,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>1,05,000</td>
<td></td>
</tr>
</tbody>
</table>
Printing Charges | 2,500  
Wages | 77,500  
Salaries | 12,500  
Opening Stock | 2,25,000  
Carriage Inwards | 8,800  
General Expenses | 26,250  
Trade Marks | 5,000  
Rates and Taxes | 2,500  
Capital | 1,74,800  
Discount received | 1,250  
Loan | 1,75,000  
Buildings | 2,00,000  
Furniture | 25,000  
Machinery | 50,000  
Cash | 1,000  
Bank | 30,000  

<p>| | | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>7,71,050</td>
<td>7,71,050</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Adjustments:
1. The closing stock was valued at Rs.3,20,000.
2. Outstanding Salaries Rs.10,000.

Solution:

**Trading and Profit and Loss Account for the year ending 31st March, 2000**

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Rs.</td>
</tr>
<tr>
<td>To Opening Stock</td>
<td>2,25,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>1,05,000</td>
</tr>
<tr>
<td>To Wages</td>
<td>77,500</td>
</tr>
</tbody>
</table>

Balance Sheet as on 31st March, 2000

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outstanding Salary</td>
<td>10,000</td>
<td>Cash</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loans</td>
<td>1,75,000</td>
<td>Bank</td>
<td>30,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>1,74,800</td>
<td>Closing Stock</td>
<td>3,20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add: Net Profit</td>
<td>2,71,700</td>
<td>Prepaid rates &amp; taxes</td>
<td>500</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,46,500</td>
<td>Building</td>
<td>2,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Furniture</td>
<td>25,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Machinery</td>
<td>50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Trade Marks</td>
<td>5,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>6,31,500</td>
<td>6,31,500</td>
<td></td>
</tr>
</tbody>
</table>
Illustration : 9

The following Trial Balance has been extracted from the books of Mr. Bhaskar on 31.03.2003.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Machinery</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Cash in Hand</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Wages</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>80,000</td>
<td></td>
</tr>
<tr>
<td>Stock (01.04.2002)</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Bills Receivable</td>
<td>29,000</td>
<td></td>
</tr>
<tr>
<td>Rent</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Interest on Bank Loan</td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>Commission received</td>
<td></td>
<td>3,000</td>
</tr>
<tr>
<td>General Expenses</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>7,500</td>
<td></td>
</tr>
<tr>
<td>Discount received</td>
<td></td>
<td>4,000</td>
</tr>
<tr>
<td>Capital</td>
<td>90,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td>Bank Loan</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Purchase returns</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Sales returns</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>3,02,000</td>
<td>3,02,000</td>
</tr>
</tbody>
</table>

Adjustments:
1. Closing Stock Rs.80,000
2. Interest on Bank loan not yet paid Rs.400
3. Commission received in advance Rs.1,000

Prepare Trading and Profit and Loss Account for the year ended 31.03.2003 and Balance Sheet as on that date after giving effect to the above adjustments.

Solution:

Trading and Profit and Loss Account of Mr. Bhaskar for the year ending 31st March, 2003

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Rs.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>To Purchases</td>
<td>80,000</td>
<td></td>
</tr>
<tr>
<td>Less: Returns</td>
<td>5,000</td>
<td>75,000</td>
</tr>
<tr>
<td>To Wages</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>To Gross Profit c/d (Transferred to Profit and Loss A/c)</td>
<td>51,000</td>
<td></td>
</tr>
<tr>
<td>To Rent</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>To Interest on Bank Loan (Transferred from Trading A/c)</td>
<td>500</td>
<td></td>
</tr>
<tr>
<td>Add: Outstanding</td>
<td>400</td>
<td></td>
</tr>
<tr>
<td>To General Expenses</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td>To Salaries</td>
<td>7,500</td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>32,600</td>
<td></td>
</tr>
<tr>
<td>(Transferred to Capital A/c)</td>
<td></td>
<td>3,000</td>
</tr>
<tr>
<td>By Discount received</td>
<td></td>
<td>4,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>57,000</td>
<td></td>
</tr>
</tbody>
</table>

57,000
## Illustration : 10

The following are the balances extracted from the books of Mrs. Suguna as on 31st March, 2004.

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Drawings</td>
<td>40,000</td>
<td>Capital</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>17,000</td>
<td>Sales</td>
<td>1,60,000</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>60,000</td>
<td>Sundry Creditors</td>
<td>45,000</td>
</tr>
<tr>
<td>Wages</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stock (31.03.03)</td>
<td>60,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>1,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>44,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bills Receivable</td>
<td>29,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rent</td>
<td>4,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commission</td>
<td>2,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Expenses</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>5,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Suspense Account</td>
<td>5,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,05,000</td>
<td></td>
<td>4,05,000</td>
</tr>
</tbody>
</table>

### Adjustments:
1. Closing Stock Rs.40,000 valued as on 31.03.04.
2. Interest on Capital at 6% to be provided.
3. Interest on Drawings at 5% to be provided.
4. Depreciate buildings at the rate of 10% per annum.
5. Write off Bad debts Rs.1,000.
6. Wages yet to be paid Rs.500


### Solution:

**Trading and Profit and Loss Account of Mrs. Suguna for the year ending 31st Marh, 2004**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>60,000</td>
<td>By Sales</td>
<td>1,60,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>20,000</td>
<td>By Closing Stock</td>
<td>40,000</td>
</tr>
<tr>
<td>To Wages</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add: Outstanding</td>
<td>500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>1,09,500</td>
<td>(Transferred to Profit &amp; Loss A/c)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,00,000</td>
<td></td>
<td>2,00,000</td>
</tr>
<tr>
<td>To Rent</td>
<td>4,500</td>
<td>By Gross Profit b/d</td>
<td>1,09,500</td>
</tr>
<tr>
<td>To Commission</td>
<td>2,500</td>
<td>(Transferred from Trading A/c)</td>
<td></td>
</tr>
<tr>
<td>To General Expenses</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest on Capital</td>
<td>12,000</td>
<td>By interest on Drawings</td>
<td>2,000</td>
</tr>
<tr>
<td>To Depreciation on buildings</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Bad debts written off</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>73,500</td>
<td>(Transferred to Capital A/c)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,11,500</td>
<td></td>
<td>1,11,500</td>
</tr>
</tbody>
</table>
### Balance Sheet of Mrs. Suguna as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>45,000</td>
<td></td>
<td>Cash in hand</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Outstanding wages</td>
<td>500</td>
<td></td>
<td>Cash at bank</td>
<td>17,000</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>2,00,000</td>
<td></td>
<td>Bills Receivable</td>
<td>29,000</td>
<td></td>
</tr>
<tr>
<td>Add: Net Profit</td>
<td>73,500</td>
<td></td>
<td>Sundry Debtors</td>
<td>44,000</td>
<td></td>
</tr>
<tr>
<td>Add: Interest on</td>
<td>2,73,500</td>
<td></td>
<td>Less: Bad debts written off</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>12,000</td>
<td></td>
<td></td>
<td></td>
<td>43,000</td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>40,000</td>
<td></td>
<td>Buildings</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Less: Interest on</td>
<td>2,45,500</td>
<td></td>
<td>Less: Depreciation</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td>2,000</td>
<td></td>
<td>Furniture</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,43,500</td>
<td></td>
<td>Suspense Account</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,89,000</td>
<td></td>
<td></td>
<td>2,89,000</td>
<td></td>
</tr>
</tbody>
</table>

### Illustration : 11

Mr. Senthil’s book shows the following balances. Prepare his Trading and Profit and Loss account for the year ended 31st March 2005 and Balance Sheet as on that date.

#### Particulars

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Stock on 1.4.2004</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>1,30,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td>Carriage inwards</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Printing and Stationery</td>
<td>8,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,20,000</td>
<td>(Transferred to Profit &amp; Loss A/c)</td>
</tr>
</tbody>
</table>
To Salaries 50,000
To Printing & Stationery 8,000
Less: Prepaid 2,000
To Postage & Telephone 7,500
To Interest paid 4,000
To Provision for Bad & Doubtful debts 9,000
To Depreciation on:
  Machinery 2075
  Furniture 500
To interest on Capital 12,500
To Net Profit 46,425

Balance Sheet of Mr. Senthil as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>Loan Account</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>250,000</td>
<td></td>
</tr>
<tr>
<td>Add: Net Profit (Transferred to Capital A/c)</td>
<td>46,425</td>
<td>1,38,000</td>
</tr>
<tr>
<td>Add: Interest on Capital</td>
<td>12,500</td>
<td></td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>17,000</td>
<td>10,000</td>
</tr>
</tbody>
</table>

Illustration : 12

From the Trial Balance of Mr. Raghuraman as on 31st March, 2003 prepare Final accounts.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>3,60,000</td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td>6,400</td>
<td></td>
</tr>
<tr>
<td>Stock (1.4.2002)</td>
<td>18,000</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>1,29,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>2,38,000</td>
<td></td>
</tr>
<tr>
<td>Sales Returns</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Wages</td>
<td>32,000</td>
<td></td>
</tr>
<tr>
<td>Insurance Premium</td>
<td>3,000</td>
<td></td>
</tr>
<tr>
<td>Packing Expenses</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Postage</td>
<td>200</td>
<td></td>
</tr>
<tr>
<td>Advertisement</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Carriage outwards</td>
<td>16,000</td>
<td></td>
</tr>
<tr>
<td>Bad debts</td>
<td>600</td>
<td></td>
</tr>
<tr>
<td>Commission received</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>Bills Payable</td>
<td>18,000</td>
<td></td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>Land &amp; Buildings</td>
<td>2,61,000</td>
<td></td>
</tr>
<tr>
<td>Plant &amp; Machinery</td>
<td>1,80,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>50,800</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>84,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,07,000</td>
<td>7,07,000</td>
</tr>
</tbody>
</table>
Adjustments:
1. Closing Stock on 31.03.2003, Rs.15,000.
2. Write off bad debts Rs.800 and make provision for Bad & doubtful debts @ 5% on Sundry debtors.
3. Commission accrued but not received Rs.2,000.

Solution:

Trading and Profit and Loss Account of Mr.Raguraman
for the year ending 31st March, 2003

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>18,000</td>
<td>By Sales 2,38,000</td>
</tr>
<tr>
<td>To Purchase</td>
<td>1,29,000</td>
<td>Less:Sales</td>
</tr>
<tr>
<td>To Wages</td>
<td>32,000</td>
<td>Returns 4,000</td>
</tr>
<tr>
<td>To Packing Expenses</td>
<td>4,000</td>
<td>By Gross Profit c/d 66,000</td>
</tr>
<tr>
<td>To Gross Profit c/d (Transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Insurance</td>
<td>5,000</td>
<td>By Gross Profit b/d 66,000</td>
</tr>
<tr>
<td>To Postage</td>
<td>200</td>
<td>(Transferred from Trading A/c)</td>
</tr>
<tr>
<td>To Advertisement</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>To Carriage outwards</td>
<td>16,000</td>
<td>By Commission</td>
</tr>
<tr>
<td>To Bad debts</td>
<td>600</td>
<td>received 1,000</td>
</tr>
<tr>
<td>Add: Bad debts written off</td>
<td>800</td>
<td>Add: Accrued Commission 2,000</td>
</tr>
<tr>
<td>To Provision for bad &amp; doubtful debts</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net Profit (Transferred to Capital A/c)</td>
<td>43,900</td>
<td></td>
</tr>
<tr>
<td></td>
<td>69,000</td>
<td>69,000</td>
</tr>
</tbody>
</table>
Sales 7,50,000  
Carriage inwards 5,000  
Fuel, Gas 37,000  
Sundry Debtors 2,50,000  
Sundry Creditors 1,20,000  
Bills Receivable 53,000  
Dividend 28,000  
Loan 60,000  
Bad debts 2,000  
Advertisement 16,000  
Provision for Bad & Doubtful Debts 6,000  
  17,14,000 17,14,000

Adjustments:
1. Closing stock Rs.1,40,000.
2. Write off Rs.10,000 as bad debts; Provide 5% for Bad and Doubtful debts.
3. Make provision for discount on Debtors at 2%.
4. Provision for discount on Creditors at 2%.

Solution:
Trading and Profit and Loss Account of Mrs. Sulochana for the year ending 31st March, 2004

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>1,20,000</td>
<td>By Sales</td>
<td>7,50,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>5,00,000</td>
<td>By Closing Stock</td>
<td>1,40,000</td>
</tr>
<tr>
<td>To Carriage inwards</td>
<td>5,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Fuel, Gas</td>
<td>37,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>2,28,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>(Transferred to Profit &amp; Loss A/c)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>8,90,000</td>
<td></td>
<td>8,90,000</td>
</tr>
</tbody>
</table>

To Salary 1,10,000  
To Rent & Taxes 21,000 (Transferred from Trading A/c)  
To Advertisement 16,000  
To Provision for bad & doubtful debts A/c  
Bad debts 2,000  
Add: Bad debts written off 10,000  
Add: New Provision 12,000  
Less: Old Provision 6,000  
To Provision for discount on debtors 4,560  
To Net Profit (Transferred to Capital A/c) 88,840  
To Provision for bad & doubtful debts A/c  
Add: New Provision 12,000  
Less: Old Provision 6,000  
To Provision for discount on debtors 4,560  
To Net Profit (Transferred to Capital A/c) 88,840

Balance Sheet of Mrs. Sulochana as on 31st March, 2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>1,20,000</td>
<td></td>
<td>Cash</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Less: Provision for discount on creditors</td>
<td>2,400</td>
<td></td>
<td>Bills Receivable</td>
<td>53,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,17,600</td>
<td></td>
<td>Sundry Debtors</td>
<td>2,50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>60,000</td>
<td></td>
<td>Less: Bad debts written off</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Loan</td>
<td>75,000</td>
<td></td>
<td>Add: Net Profit</td>
<td>88,840</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,98,840</td>
<td></td>
<td>for Bad &amp; doubtful debts</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,98,840</td>
<td></td>
<td>Less: New Provision</td>
<td>2,28,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7,98,840</td>
<td></td>
<td>for discount on debtors</td>
<td>4,560</td>
<td></td>
</tr>
</tbody>
</table>
Illustration : 14

Prepare Trading, Profit and Loss A/c and Balance Sheet as on 31.3.2005 from the following Trial Balance of Mr.Imran.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>25,200</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>9,03,000</td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>30,600</td>
<td></td>
</tr>
<tr>
<td>Business Premises</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td>Creditors</td>
<td>79,800</td>
<td></td>
</tr>
<tr>
<td>Opening Stock</td>
<td>1,32,000</td>
<td></td>
</tr>
<tr>
<td>Debtors</td>
<td>1,08,000</td>
<td></td>
</tr>
<tr>
<td>Rent</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>6,60,000</td>
<td></td>
</tr>
<tr>
<td>Discount</td>
<td>2,400</td>
<td></td>
</tr>
<tr>
<td>Insurance</td>
<td>16,000</td>
<td></td>
</tr>
<tr>
<td>Wages</td>
<td>24,000</td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>54,000</td>
<td></td>
</tr>
<tr>
<td>Advertisement</td>
<td>13,200</td>
<td></td>
</tr>
<tr>
<td>Carriage on Purchases</td>
<td>10,800</td>
<td></td>
</tr>
<tr>
<td>Provision for bad and doubtful debts</td>
<td>7,000</td>
<td></td>
</tr>
<tr>
<td>Bad debts</td>
<td>800</td>
<td></td>
</tr>
<tr>
<td>Income tax</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>11,73,400</td>
<td>11,73,400</td>
</tr>
</tbody>
</table>

Adjustments:
1. Closing Stock on 31.03.2005 was Rs.1,20,000
2. Make a provision of 5% on Sundry debtors for bad and doubtful debts.
3. Rent received in advance Rs.2,000
4. Provide 10% depreciation on Furniture and Business Premises.

Solution:

Trading and Profit and Loss Account of Mr.Imran for the year ending 31st March, 2005

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Dr. Rs.</th>
<th>Cr. Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>1,32,000</td>
<td>By Sales 9,03,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>6,60,000</td>
<td>By Closing stock 1,20,000</td>
</tr>
<tr>
<td>To Wages</td>
<td>24,000</td>
<td></td>
</tr>
<tr>
<td>To Carriage on Purchases</td>
<td>10,800</td>
<td></td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>1,96,200</td>
<td>(Transferred to Profit &amp; Loss A/c) 10,23,000</td>
</tr>
<tr>
<td>To Insurance</td>
<td>16,000</td>
<td>By Gross Profit b/d 1,96,200</td>
</tr>
<tr>
<td>To Salaries</td>
<td>54,000</td>
<td>(Transferred from Trading A/c)</td>
</tr>
<tr>
<td>To Advertisement</td>
<td>13,200</td>
<td>By Rent 6,000</td>
</tr>
<tr>
<td>To Depreciation on:</td>
<td></td>
<td>Less: Received in advance 2,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>3060</td>
<td></td>
</tr>
<tr>
<td>Business Premises</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>15,060</td>
<td>4,000</td>
</tr>
<tr>
<td>To Net Profit</td>
<td>1,05,140</td>
<td>By Discount 2,400</td>
</tr>
<tr>
<td>(Transferred to Capital A/c)</td>
<td></td>
<td>By Provision for bad &amp; doubtful debts 7,000</td>
</tr>
<tr>
<td></td>
<td>1,08,000</td>
<td>Old Provision 7,000</td>
</tr>
<tr>
<td></td>
<td>1,08,000</td>
<td>Less: Bad debts 800</td>
</tr>
<tr>
<td></td>
<td>1,08,000</td>
<td>New Provision 5,400</td>
</tr>
<tr>
<td></td>
<td>800</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,03,400</td>
<td>2,03,400</td>
</tr>
</tbody>
</table>
Balance Sheet of Mr. Imran as on 31st March, 2005

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>79,800</td>
<td></td>
<td>Sundry Debtors</td>
<td>1,08,000</td>
<td></td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>25,200</td>
<td></td>
<td>Less: New Provision for bad and doubtful debts</td>
<td>5,400</td>
<td></td>
</tr>
<tr>
<td>Rent received in advance</td>
<td>2,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital</td>
<td>1,50,000</td>
<td>1,02,600</td>
<td>Closing Stock</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td>Add: Net profit</td>
<td>1,05,140</td>
<td></td>
<td>Furniture</td>
<td>30,600</td>
<td></td>
</tr>
<tr>
<td>Less: Income Tax</td>
<td>4,000</td>
<td>27,540</td>
<td>Less: Depreciation</td>
<td>3,060</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,51,140</td>
<td></td>
<td>Business Premises</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Less: Depreciation</td>
<td>12,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,58,140</td>
<td></td>
<td></td>
<td>1,08,000</td>
<td></td>
</tr>
</tbody>
</table>

Note:

Total of Bad debts written off and new provision for bad and doubtful debts is (Rs. 800 + Rs. 5,400) Rs. 6,200. Old provision for bad and doubtful debts given in the Trial Balance is Rs. 7,000 which is greater than Rs. 6,200. So the difference will appear on the credit side of the Profit and Loss account as follows:

Old provision Rs. 7,000

Less: Total of bad debts and new provision for bad and doubtful debts (Rs. 800 + Rs. 5,400) Rs. 6,200

QUESTIONS

I. Objective type:

a) Fill in the blanks:

1. Net Profit is transferred from Profit and Loss account to ________ account.
2. Closing stock is valued at Cost Price or ________ price whichever is lower.
3. Outstanding expenses are shown on the ________ side of the balance sheet.
4. Prepaid expenses are shown on the ________ side of the balance sheet.
5. Income accrued but not received will be shown on the ________ side of the Balance sheet.
6. Income received in advance will be shown on the ________ side of the Balance sheet.
7. Interest on capital is debited in ________ account.
8. Interest on drawings is credited in ________ account.
9. Interest on loan borrowed unpaid is shown on the ________ side of the Balance sheet.
10. Depreciation is deducted from the concerned ________ in the Balance sheet.
11. Provision for Bad and Doubtful debts is deducted from ________ in the Balance sheet.
12. Provision for discount on creditors is deducted from ________ in the Balance sheet.
13. Debts which are not recoverable from Sundry debtors are termed as ________.

b) Choose the correct answer:

1. Returns inwards are deducted from
   a) Purchases  b) Sales  c) Returns outward

2. The Profit and Loss account shows
   a) Financial position of the concern
   b) Net profit or Net loss  c) Gross profit or Gross Loss

3. Rent outstanding is
   a) a liability  b) an asset  c) an income

4. Closing stock is shown in
   a) Profit and loss account
   b) Trading account and Balance sheet
   c) None of the above.

5. Opening stock is shown in
   a) Balance sheet  b) Profit and Loss account
   c) Trading account

6. Gross Profit is transferred to
   a) Capital account  b) Profit and loss account
   c) None of the above.

7. Interest on capital is added to
   a) Expense A/c  b) Income A/c  c) Capital A/c

8. Interest on drawings is deducted from
   a) Income A/c  b) Capital A/c  c) Expense A/c

9. Outstanding interest on loan borrowed is to be added to
   a) Asset A/c  b) Income A/c  c) Loan A/c

10. All the items given in the adjustment will appear at _________ in
    the Final accounts.
    a) Three places  b) Two places  c) One Place

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

II. Other Questions:

1. What is outstanding expense?
2. What is prepaid expense?
3. What is accrued income?
4. What is income received in advance?
5. What is bad debt?
6. Write notes on Provision for bad and Doubtful debts.
7. Write notes on Provision for discount on Debtors.
8. Write notes on Provision for discount on Creditors.
9. What is adjusting entry?
10. Write notes on
    a) Trading Account  b) Profit and loss account and
    c) Balance sheet.

III. Problems:

1. Pass necessary adjusting entries for the following adjustments:
   a) Closing stock Rs. 6,00,000.
   b) Provide 6% interest on capital of Rs. 16,00,000
   c) Rent received in advance Rs. 5,000
   d) Interest accrued on investments Rs. 2,000
   e) Insurance premium prepaid Rs. 1,000
   f) Wages outstanding Rs. 15,000.

2. Pass necessary adjusting entries for the following adjustments:
   a) Interest on drawings Rs. 10,000.
   b) Interest on loan outstanding Rs.5,000.
   c) Depreciation at 5% on furniture Rs.50,000.
   d) Write off bad and doubtful debts Rs.3,000.
e) Provide provision for bad and doubtful debts at 5% on Sundry debtors Rs.4,00,000.
f) Provide provision for discount on creditors at 2% on Sundry creditors Rs. 3,50,000.

3. Give adjusting entry and transfer entry for the following adjustments:
   a) Interest on drawings Rs. 5,000.
   b) Depreciation on machinery Rs.4,000.
   c) Write off bad debts Rs.2,000.

4. The value of closing stock shown outside the Trial Balance (31.3.05) is Rs.2,50,000. Pass adjusting entry. Show how this item will appear in the Final accounts as on 31.3.05.

5. Trial Balance (31.3.05) shows salaries paid Rs.1,50,000. Salary for March 2005 Rs.4,000 not yet paid. Pass adjusting entry and show how this item will appear in the Final accounts.

6. Trial Balance as on 31.3.05 shows Rs.40,000 as Insurance premium paid. Unexpired insurance premium Rs.5,000. Pass adjusting entry and show how this item will appear in the Final accounts.

7. Credit side of Trial Balance as on 31.4.05 shows ‘Commission received Rs.10,000.’ Commission accrued but not yet received Rs.4,000. Pass adjusting entry and show how this item will appear in the Final accounts.

8. Trial balance as on 31.3.05 shows ‘Rent received Rs.30,000.’ Rent received in advance Rs.6,000. Pass adjusting entry and show how this item will appear in the Final accounts.

9. As per Trial Balance (31.3.05) capital is Rs. 6,00,000. Provide 6% interest on capital. Pass adjusting and transfer entries. Show how this item will appear in the Final accounts.

10. The Trial Balance shows the followings
    Capital as on 31.3.03 – Rs.6,00,000

11. The Trial Balance (31.3.04) shows the following:

    
    | Dr.  | Cr.  |
    |------|------|
    | Bank loan @ 10% (1.4.03) | ---- | Rs. 10,00,000 |
    | Interest paid | Rs. 60,000 |

    Provide interest outstanding. Pass adjusting entry and show how this item will appear in the Final accounts.

12. The trial balance shows the following as on 31.3.98.

    Capital | Rs. 5,00,000 |
    Drawings (1.7.97) | Rs. 50,000 |

    Charge interest on drawings @ 5%. Pass adjusting and transfer entry. Show how this item will appear in the Final accounts.

    (Oct. 2000)

13. Rent received shown in the Trial Balance as on 31st March 2001, Rs.10,000. Rent received in advance is Rs.1,000. You are required to show how it appears in the Profit and Loss account and Balance sheet.

    (June 2002)


    Sundry debtors | Rs 21,000 |
    Bad debts to be written off | Rs. 1,000 |

    **Adjustment:** Provide @ 5% provision for Bad and Doubtful debts and @2% Provision for discount on Debtors.

    (Answer: Rs.18,620 - March 2003)
15. Commission received given in Trial Balance is Rs.1,000 as on 31st March 1994. Commission accrued but not yet received Rs.150. Show the adjusting entry.

(June 2003)

16. The Trial Balance shows the value of machinery on 31.3.04 as Rs.50,000. Machinery is to be depreciated at 10%. Pass adjustment entry and show how this item will appear in the Final accounts.

17. The Trial Balance as on 31st March 2003 show Sundry debtors Rs.60,000. Write off bad debts Rs.4,000. Pass adjusting and transfer entry. Show how this item will appear in the Final accounts.

18. The Trial Balance shows on 31.3.2002, Sundry debtors Rs.1,50,000. Provide 5% provision for bad and doubtful debts on Sundry debtors. Pass adjusting entry and how this item will appear in the Final accounts.

19. The Trial Balance shows on 31.3.2002, Sundry debtors Rs.1,25,000.

Adjustment:
1. Bad debts to be written off Rs.5,000.
2. Provide @ 5% Provision for bad and doubtful debts and
3. Provide @ 2% Provision for discount on debtors.

Pass entries and show how these items will appear in the Final accounts.

20. The Trial Balance as on 31st March 2003 shows.

Sundry debtors 90,000 ---

Adjustment: Create 2% Provision for discount on Debtors.

Pass Journal entry and show how this item will appear in the Final accounts.

21. The Trial Balance shows sundry creditors at Rs.10,000 on 31.3.2000.

Adjustment: It is desired to make a provision for discount on Sundry creditors at 2½ %. You are required to show how it appears in Profit and Loss account and Balance sheet.

(March 2002)

22. The following is the Trial Balance extracted from the books of Mr. Kumar as on 31.3.96.

Prepare Trading and Profit and Loss account and Balance sheet on 31.3.96.

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buildings</td>
<td>30,000</td>
<td>Capital</td>
<td>40,000</td>
</tr>
<tr>
<td>Machinery</td>
<td>31,400</td>
<td>Purchase returns</td>
<td>2,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>2,000</td>
<td>Sales</td>
<td>2,80,000</td>
</tr>
<tr>
<td>Motor Car</td>
<td>16,000</td>
<td>Sundry Creditors</td>
<td>9,600</td>
</tr>
<tr>
<td>Purchases</td>
<td>1,88,000</td>
<td>Discount received</td>
<td>1,000</td>
</tr>
<tr>
<td>Sales returns</td>
<td>1,000</td>
<td>Provision for bad and doubtful debts</td>
<td>600</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>30,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Expenses</td>
<td>1,600</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>9,400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rates and Taxes</td>
<td>1,200</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bad Debts</td>
<td>400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Insurance premium</td>
<td>800</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Discount allowed</td>
<td>1,400</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening stock</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

3,33,200

3,33,200

Adjustments:

i) Outstanding rates and taxes Rs.1,600.

ii) Insurance Premium Prepaid Rs.200.
iii) Maintain Provision for bad and doubtful debts at 5% on debtors.

iv) Depreciate Motor car by 10%, Furniture by 4% and Buildings by 3%.

v) Stock on 31.3.96 Rs.20,000.

(Modified :March, 2000)

(Answer: G.P. Rs. 93,000; N.P. Rs. 83,720; B/s Rs. 1,34,920)

23. From the undermentioned Trial Balance of Mr. Saleem as on 31.3.2001, prepare Trading and Profit and Loss Account and Balance sheet as on that date.

**Trial Balance**

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in Hand</td>
<td>1,500</td>
<td>Capital</td>
<td>80,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>1,20,000</td>
<td>Bank loan @ 4%</td>
<td>20,000</td>
</tr>
<tr>
<td>Opening stock</td>
<td>40,000</td>
<td>Bills payable</td>
<td>25,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>60,000</td>
<td>Sundry Creditors</td>
<td>25,000</td>
</tr>
<tr>
<td>Plant and Machinery</td>
<td>50,000</td>
<td>Sales</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>20,000</td>
<td>Provision for bad &amp;</td>
<td></td>
</tr>
<tr>
<td>Bills Receivable</td>
<td>15,000</td>
<td>doubtful debts</td>
<td>1,500</td>
</tr>
<tr>
<td>Rent and Taxes</td>
<td>10,000</td>
<td>Interest</td>
<td>1,000</td>
</tr>
<tr>
<td>Wages</td>
<td>16,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,52,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Additional information supplied:

i) Closing stock Rs.50,000.

ii) Provide for outstanding liabilities.

   Rent and taxes Rs.2,000.

   Wages Rs.3,000.

   Salaries Rs.4,000.

 iii) Depreciation on Plant and Machinery @5% and on furniture @ 10%.

 iv) Provide 4% interest on Bank loan.

 v) Write off bad debts Rs.2,000.

(Answer: G.P. Rs. 71,000; N.P. Rs. 30,200; B/s Rs. 1,90,000)

24. Trial Balance of Anuradha Agencies as on 31.03.2001:

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Drawings</td>
<td>1,800</td>
<td>Capital</td>
<td>80,000</td>
</tr>
<tr>
<td>Buildings</td>
<td>15,000</td>
<td>General Reserve</td>
<td>20,000</td>
</tr>
<tr>
<td>Furniture &amp; Fittings</td>
<td>7,500</td>
<td>Loan from Hari @6%</td>
<td>15,000</td>
</tr>
<tr>
<td>Computer</td>
<td>25,000</td>
<td>Sales</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Interest on loan</td>
<td>900</td>
<td>Commission received</td>
<td>7,500</td>
</tr>
<tr>
<td>Loose tools</td>
<td>6,100</td>
<td>Sundry Creditors</td>
<td>10,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>75,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stock on 1.4.2000</td>
<td>25,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Expenses</td>
<td>15,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Freight inward</td>
<td>2,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Freight outward</td>
<td>1,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>28,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bank</td>
<td>20,200</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Goodwill</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,32,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Adjustments:

i) Closing stock is Rs.32,000.

ii) Depreciate Computer @10%; Buildings @ 5%; Furniture and Fittings @ 10%

iii) Provide for bad and doubtful debts @ 5% and for discount on debtors @2%.
iv) Provide interest on drawings @6% and on Capital @ 8%.

Prepare final accounts for the said period after giving effect to the adjustments.

(October - 2002)
(Answer: G.P. Rs.30,000; N.P. Rs.8,376; B/s Rs. 1,37,868)

25. Trial Balance of Mr.Velu as on 31st March 1994.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td>3,600</td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Furniture &amp; Fittings</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Computer</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Loan from Mr.Ravi at 6%</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Interest on Loan</td>
<td>1,800</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>Loose tools</td>
<td>32,200</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>Stock on 1.4.94</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>General Expenses</td>
<td>30,000</td>
<td></td>
</tr>
<tr>
<td>Freight inward</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Freight outward</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Commission received</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>56,000</td>
<td></td>
</tr>
<tr>
<td>Bank</td>
<td>40,400</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,65,000</td>
<td>4,65,000</td>
</tr>
</tbody>
</table>

Adjustments:

i) Closing stock Rs.64,000.

ii) Depreciate computer at 10%; Buildings at 5%,; Furniture and Fittings at 10%

iii) Provide for Bad and doubtful Debts at 5% and for Discount on Debtors at 2%.

iv) Provide interest on Drawings at 6% and on Capital at 6%.


(October - 1994)
(Answer: G.P. Rs. 60,000; N.P. Rs.17,552; B/s Rs.2,75,736)

26. The following balances have been extracted from the books of Mrs.Padma as on 31st March, 2002.

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Furniture</td>
<td>30,000</td>
<td>Capital</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Cash in Hand</td>
<td>8,000</td>
<td>Commission</td>
<td>14,000</td>
</tr>
<tr>
<td>Opening Stock</td>
<td>1,00,000</td>
<td>Sales</td>
<td>6,00,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>3,20,000</td>
<td>Creditors</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Investments @10%</td>
<td>20,000</td>
<td>Interest</td>
<td>1,500</td>
</tr>
<tr>
<td>Drawings</td>
<td>60,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bad debts</td>
<td>12,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>60,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Carriage inwards</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Insurance</td>
<td>12,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rent</td>
<td>26,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Debtors</td>
<td>1,80,000</td>
<td>Advertising</td>
<td>40,000</td>
</tr>
<tr>
<td>Advertising</td>
<td>40,000</td>
<td>Printing &amp; Stationery</td>
<td>12,000</td>
</tr>
<tr>
<td>Printing &amp; Stationery</td>
<td>12,000</td>
<td>General Expenses</td>
<td>15,500</td>
</tr>
<tr>
<td>General Expenses</td>
<td>15,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>9,15,500</td>
<td></td>
<td>9,15,500</td>
</tr>
</tbody>
</table>

68  69
The following adjustments are to be made:

1. Closing stock was valued at Rs. 80,000.
2. Provide for accrued interest on investments Rs. 500.
3. Commission received in advance Rs. 4,000.
4. A provision for Bad and Doubtful Debts is to be created to the extent of 5% on Sundry Debtors.
5. A provision for discount on Sundry creditors is to be created to the extent of 2% on Sundry creditors.

(Answer: G.P. Rs. 2,40,000; N.P. Rs. 67,500; B/s Rs. 3,09,500)

27. The Trial Balance of Mrs. Kalpana shows the following balances on March 31, 2001.

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchases</td>
<td>1,40,000</td>
<td>Capital</td>
<td>2,40,000</td>
</tr>
<tr>
<td>Sales Returns</td>
<td>10,000</td>
<td>Sales</td>
<td>30,000</td>
</tr>
<tr>
<td>Opening Stock</td>
<td>40,000</td>
<td>Discount received</td>
<td>2,000</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>4,000</td>
<td>Commission received</td>
<td>8,000</td>
</tr>
<tr>
<td>Bank charges</td>
<td>1,000</td>
<td>Sundry Creditors</td>
<td>58,000</td>
</tr>
<tr>
<td>Salaries</td>
<td>9,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wages</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Freight inwards</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Freight outwards</td>
<td>2,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rent, Rates &amp; Taxes</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Advertising</td>
<td>12,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash in hand</td>
<td>2,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Plant &amp; Machinery</td>
<td>1,00,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>1,20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>1,40,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<p>| | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>6,08,000</td>
<td>6,08,000</td>
<td></td>
</tr>
</tbody>
</table>

Adjustments required:

1. Stock on 31.3.2003 Rs. 14,700
2. Salaries unpaid Rs. 1,000

28. From the following Trial Balance of Mr. Joseph, prepare Trading and Profit and Loss Account for the year ended 31st March, 2003 and a Balance Sheet as on that date.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>75,000</td>
<td>75,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>45,000</td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>Rent</td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td>Insurance Premium</td>
<td>900</td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>84,000</td>
<td></td>
</tr>
<tr>
<td>Bank</td>
<td>13,500</td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>13,500</td>
<td></td>
</tr>
<tr>
<td>Stock (1.4.2002)</td>
<td>15,600</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>7,500</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>10,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,05,500</td>
<td>2,05,500</td>
</tr>
</tbody>
</table>

Adjustments required:

1. Stock on 31.3.2003 Rs. 14,700
2. Salaries unpaid Rs. 1,000

(Answer: G.P. Rs. 1,52,000; N.P. Rs. 1,24,000; B/s Rs. 4,22,000)
3. Rent paid in advance  Rs. 750
4. Create 5% Provision for bad and doubtful debts on Sundry debtors.

(Answer: G.P. Rs. 29,100; N.P. Rs. 17,075; B/s Rs. 1,33,575)

29. The following balances are extracted from the books of Mr. Venugopal as on 31st March 2004. Prepare Trading, Profit and Loss Account and the Balance Sheet.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>1,20,000</td>
<td></td>
</tr>
<tr>
<td>General expenses</td>
<td>16,500</td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td>16,000</td>
<td></td>
</tr>
<tr>
<td>Commission</td>
<td>11,000</td>
<td></td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Cash in Hand</td>
<td>2,500</td>
<td></td>
</tr>
<tr>
<td>Stock (1.4.2003)</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>80,000</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>3,00,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>5,00,000</td>
<td></td>
</tr>
<tr>
<td>Wages</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Insurance Premium</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>1,50,000</td>
<td></td>
</tr>
<tr>
<td>Bills Payable</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>731,000</td>
<td>731,000</td>
</tr>
</tbody>
</table>

Adjustments:
1. Closing Stock Rs. 1,00,000
2. Write off bad debts Rs. 20,000
3. Create provision for Bad and doubtful debts @ 5%
4. Create provision for discount on debtors @ 2%
5. Create provision for discount on creditors @ 2%

(Answer: G.P. Rs. 1,50,000; N.P. Rs. 1,00,530; B/s Rs. 3,03,530)

30. The following are the balances extracted from the books of Mrs. Nandhini as on 31.03.2002. Prepare Trading and Profit and Loss Account and Balance Sheet.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Balances Rs.</th>
<th>Credit Balances Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Drawings</td>
<td>40,000</td>
<td>Capital</td>
</tr>
<tr>
<td>Cash in Hand</td>
<td>17,000</td>
<td>Sales</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>65,000</td>
<td>Sundry Creditors</td>
</tr>
<tr>
<td>Wages</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td>Stock (1.4.2001)</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Buildings</td>
<td>1,00,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>44,000</td>
<td></td>
</tr>
<tr>
<td>Bills Receivable</td>
<td>29,000</td>
<td></td>
</tr>
<tr>
<td>Rent</td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td>Commission</td>
<td>2,500</td>
<td></td>
</tr>
<tr>
<td>General Expenses</td>
<td>8,000</td>
<td></td>
</tr>
<tr>
<td>Furniture</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,05,000</td>
<td></td>
</tr>
</tbody>
</table>

Adjustments:
1. Closing stock Rs. 40,000
2. Interest on Capital at 6% to be provided.
3. Interest on Drawings at 5% to be provided.
4. Wages yet to be paid Rs. 1,000
5. Rent Prepaid Rs. 900

Prepare Trading and Profit and Loss Account and Balance sheet as on 31.3.2002.

(Answer: G.P. Rs. 1,09,000; N.P. Rs. 84,900; B/s Rs. 3,00,900)
31. From the following Trial Balance of Mr. Ravi, prepare Trading and Profit and Loss Account for the year ended 31st March, 2002 and a Balance Sheet as on that date.

**Trial Balance**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Rent</td>
<td>1,500</td>
<td></td>
</tr>
<tr>
<td>Insurance</td>
<td>300</td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>28,000</td>
<td></td>
</tr>
<tr>
<td>Bank Balance</td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>2,000</td>
<td></td>
</tr>
<tr>
<td>Stock (1.4.2001)</td>
<td>5,200</td>
<td></td>
</tr>
<tr>
<td>Creditors</td>
<td>2,500</td>
<td></td>
</tr>
</tbody>
</table>

**Adjustments required:**

a) Stock on 31.3.02 Rs. 4,900
b) Salaries unpaid Rs. 300
c) Rent paid in advance Rs. 200
d) Insurance prepaid Rs. 90

**Trial Balance**

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchases</td>
<td>11,870</td>
</tr>
<tr>
<td>Debtors</td>
<td>7,580</td>
</tr>
<tr>
<td>Return inwards</td>
<td>450</td>
</tr>
<tr>
<td>Bank deposit</td>
<td>2,750</td>
</tr>
<tr>
<td>Rent</td>
<td>360</td>
</tr>
<tr>
<td>Salaries</td>
<td>850</td>
</tr>
<tr>
<td>Travelling expenses</td>
<td>300</td>
</tr>
<tr>
<td>Cash</td>
<td>210</td>
</tr>
<tr>
<td>Stock (1.4.1980)</td>
<td>2,450</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>40</td>
</tr>
<tr>
<td>Drawings</td>
<td>600</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>27,460</td>
</tr>
</tbody>
</table>

**Credit Balances**

<table>
<thead>
<tr>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>8,000</td>
</tr>
<tr>
<td>Bad debts recovered</td>
<td>250</td>
</tr>
<tr>
<td>Creditors</td>
<td>1,250</td>
</tr>
<tr>
<td>Return Outwards</td>
<td>350</td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>1,570</td>
</tr>
<tr>
<td>Sales</td>
<td>14,690</td>
</tr>
<tr>
<td>Bills payable</td>
<td>1,350</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>27,460</td>
</tr>
</tbody>
</table>

**Adjustments:**

a) The closing stock on 31.3.81 was Rs.4,200.
b) Write off Rs.80 as bad debts.
c) Create a provision for bad and doubtful debts at 5% on Sundry debtors.
d) Rent outstanding Rs.120.

**Answer:** G.P. Rs. 4,470; N.P Rs. 2,595; B/s Rs. 14,285

33. The following are the balances extracted from the books of Ganesh as on 31.3.1999. Prepare Trading and Profit and Loss account for the year ending 31.3.1999 and a Balance Sheet as on that date.

**Trial Balance as on 31.3.1999**

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Drawings</td>
<td>4,000</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>1,700</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>20,000</td>
</tr>
<tr>
<td>Sales</td>
<td>16,000</td>
</tr>
</tbody>
</table>
The following adjustments are to be made:

a) Stock on 31.3.99 was Rs.4,000.

b) Interest on capital at 6% to be provided.

c) Interest on Drawings at 5% to be provided.

d) Wages yet to be paid Rs.100.

e) Rent prepaid Rs. 50.

(Answer: G.P. Rs.10,900; N.P. Rs. 8,450; B/s Rs.30,050)

34. From the following Trial Balance of Thiru. Rehman as on 31st March 1995, prepare Trading and Profit and Loss account and Balance sheet taking into account the adjustments.

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land and Building</td>
<td>42,000</td>
<td>Capital</td>
<td>62,000</td>
</tr>
<tr>
<td>Machinery</td>
<td>20,000</td>
<td>Sales</td>
<td>98,780</td>
</tr>
<tr>
<td>Patents</td>
<td>7,500</td>
<td>Returns outwards</td>
<td>500</td>
</tr>
<tr>
<td>Stock (1.4.1994)</td>
<td>5,760</td>
<td>Sundry creditors</td>
<td>15,300</td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>14,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>40,675</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>40,500</td>
</tr>
</tbody>
</table>

The following adjustments are to be made:

a) Stock on 31.3.1995 was Rs. 6,800.

b) Salary outstanding Rs.1,500

c) Insurance prepaid Rs.150.

d) Depreciate machinery @ 10% and patents @ 20%.

e) Create a provision of 2% on debtors for bad debts.

(Answer: G.P. Rs. 43,715; N.P. Rs. 11,530; B/s Rs. 90,330).

35. From the following Trial Balance of Tmt. Selvapriya as on 31st March 2005, prepare Trading and Profit and Loss account and Balance sheet taking into account the adjustments.

<table>
<thead>
<tr>
<th>Debit Balances</th>
<th>Rs.</th>
<th>Credit Balances</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchases</td>
<td>2,000,000</td>
<td>Capital</td>
<td>3,000,000</td>
</tr>
<tr>
<td>Salaries</td>
<td>10,000</td>
<td>Sales</td>
<td>25,000</td>
</tr>
<tr>
<td>Rent</td>
<td>7,500</td>
<td>Sundry creditors</td>
<td>1,05,000</td>
</tr>
<tr>
<td>Insurance premium</td>
<td>1,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Drawings</td>
<td>50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Machinery</td>
<td>1,40,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash at bank</td>
<td>22,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(Answer: G.P. Rs. 43,715; N.P. Rs. 11,530; B/s Rs. 90,330).
<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Computers</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>50,000</td>
</tr>
<tr>
<td>Cash</td>
<td>10,000</td>
</tr>
<tr>
<td>Opening Stock</td>
<td>26,000</td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>12,500</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>6,55,000</strong></td>
</tr>
<tr>
<td><strong>Adjustments</strong></td>
<td></td>
</tr>
<tr>
<td>1. Closing stock as on 31.3.2005 Rs. 39,000</td>
<td></td>
</tr>
<tr>
<td>2. Rent outstanding</td>
<td>Rs. 1,000</td>
</tr>
<tr>
<td>3. Provide interest on capital @ 10% and on Drawings @ 8%</td>
<td></td>
</tr>
</tbody>
</table>

*(Answer: G.P. Rs. 63,000; N.P. Rs. 17,000; B/s Rs. 3,99,000)*
Learning Objectives

After studying this chapter, you will be able to:

- understand the meaning, definition, features and limitations of single entry system.
- see the relationship between double entry and single entry.
- estimate the capital by preparing statement of affairs.
- determine the profit or loss by preparing the statement of Profit or Loss.
- prepare the final accounts.

Single Entry System is an incomplete, inaccurate, unscientific and unsystematic system of book keeping. The name of the system itself shows that the double aspects of business transactions are not recorded. This system makes use of Double Entry System partially. It maintains only personal and cash accounts. Real and nominal accounts are not maintained. It is a system, adopted by certain business houses which, for their convenience and more practical approach, reject the strict rules of the double entry system and maintain only the bare essential
records. In other words, it is a defective double entry system manipulated to meet the needs of small trading concerns.

According to Kohler “Single Entry System is a system of bookkeeping in which as a rule, only records of cash and personal accounts are maintained. It is always incomplete double entry varying with circumstances”.

Thus, single entry actually refers to incomplete double entry system or the defective double entry system. It is not based on dual aspect concept. Hence it is incomplete, inaccurate and unscientific.

2.1 Features of Single Entry:

1. Suitable for sole traders and partnership firms: The single entry system is suitable only for sole traders and partnership firms. Companies cannot keep books on single entry system because of legal provisions.

2. Only personal accounts and cash accounts are kept: In this system it is very common to keep only personal accounts and to avoid real and nominal accounts. It also keeps one cash book which mixes up business as well as private transactions.

3. All transactions are not recorded: All business transactions are not recorded in the books of account. Some of them are recorded in the books of accounts, certain transactions are noted in the diary and some of them are in the memories.

4. Lack of uniformity: This system lacks uniformity as it is a mere adjustment of double entry system, according to the convenience of the individual.

5. Collection of information from original documents: It is quite often seen that for information one has to depend on original vouchers. For example to know total purchases and sales, one has to depend on copies of invoices.

6. Profit only an estimate: Profit under this system is only an estimate.

7. True financial position can not be ascertained: True financial position can not be ascertained as Balance Sheet is not prepared due to the absence of nominal and real accounts.

8. Not accepted by Tax Authorities: Due to incompleteness, inaccuracy, and unsystematic nature, it is not accepted by tax authorities.

2.2 Limitations of Single Entry:

1. Incomplete and unscientific method: This system is incomplete, because real and nominal accounts are not prepared and also due to the fact that the debit and credit aspect of all transactions are not recorded.

2. Trial Balance can not be prepared: Quite often this system does not record both the aspects of transactions, therefore, at the end of the year arithmetical accuracy of the books cannot be checked by preparing a trial balance.

3. Performance of the business cannot be ascertained: Trading, profit and loss account cannot be prepared and hence the gross profit, net profit and rate of net profit on sales cannot be known.

4. True financial position cannot be ascertained: It is very difficult to prepare balance sheet, so the true financial position cannot be ascertained.

5. Comparison with previous years performance is not possible: Due to incomplete information and non-availability of previous years’ information, comparison between the current and previous years’ performance cannot be made. Comparison is required to identify the areas of weakness and rectification.

6. Unacceptable to tax authorities: Tax authorities (income tax and sales tax) do not accept accounts prepared according to single entry system for computation of taxes.
7. **Difficulty in obtaining loan:** Accounts prepared according to this system are not accepted by banks and other money lending institutions, so it is very difficult to obtain loan.

8. **Difficult to locate frauds:** It is difficult to locate frauds under this system and so employees may become dishonest and negligent. It encourages misappropriation, fraud and carelessness.

9. **Difficult to determine the price of the business:** Due to the absence of true and reliable net profit or assets and liabilities, it is difficult to determine the price of the business at the time of its sale.

### 2.3 Differences between Double Entry System and Single Entry System:

<table>
<thead>
<tr>
<th>Basis of Distinction</th>
<th>Double Entry System</th>
<th>Single Entry System</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Principle</td>
<td>For every debit there is a corresponding credit and vice versa</td>
<td>Debit and credits do not agree.</td>
</tr>
<tr>
<td>2. Recording of transaction</td>
<td>Debit and credit aspects of all transactions are recorded.</td>
<td>Debit and credit aspects of all transactions are not recorded.</td>
</tr>
<tr>
<td>3. Nature of accounts maintained</td>
<td>Maintains complete record of personal, real and nominal accounts.</td>
<td>An incomplete record. Only personal and cash accounts are maintained.</td>
</tr>
<tr>
<td>4. Trial Balance</td>
<td>Arithmetical accuracy of the records can be checked by preparing a Trial Balance</td>
<td>Trial Balance cannot be prepared.</td>
</tr>
<tr>
<td>5. Determination of profit or loss and financial position</td>
<td>A Profit and Loss Account and Balance sheet can be conveniently prepared since the book of accounts present a complete picture.</td>
<td>A Profit &amp; Loss Account and Balance sheet cannot be conveniently prepared since the accounting records are incomplete.</td>
</tr>
<tr>
<td>6. Suitability</td>
<td>It is suitable for all types of traders.</td>
<td>It is suitable for only small traders.</td>
</tr>
</tbody>
</table>

### 2.4 Distinction between Statement of Affairs and Balance Sheet:

Statement of affairs which looks like a balance sheet differs from the balance sheet in the following respects.

<table>
<thead>
<tr>
<th>Basis of Distinction</th>
<th>Balance Sheet</th>
<th>Statement of Affairs</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Objectives</td>
<td>To Know the financial position of the business</td>
<td>To find out the capital of business</td>
</tr>
<tr>
<td>2. Accounting method</td>
<td>When accounting is maintained under double entry system, balance sheet is prepared</td>
<td>Statement of affairs is prepared when accounts are maintained under single entry system of accounting</td>
</tr>
<tr>
<td>3. Basis of preparation</td>
<td>It is prepared exclusively on the basis of ledger accounts</td>
<td>It is prepared on the basis of some ledger accounts and estimates.</td>
</tr>
<tr>
<td>4. Reliability</td>
<td>It is regarded as a reliable statement</td>
<td>It is not regarded as reliable.</td>
</tr>
<tr>
<td>5. Missing of Facts</td>
<td>Since both the aspects of all transactions are duly recorded, no chance for missing of facts.</td>
<td>There remains always a possibility for missing of facts, because the accounts are incomplete.</td>
</tr>
</tbody>
</table>
2.5 Methods of ascertaining profit or loss:

When accounts are kept under single entry system, the following methods are adopted to find out profit or loss of the business.

1. Statement of affairs method or Net worth method or Capital comparison method
2. Conversion method

2.5.1 Statement of Affairs Method:

The following procedures are adopted to calculate profit.

**Step 1** → Ascertain opening capital: A statement of affairs at the beginning of the year is prepared to find out the amount of capital in the beginning. A statement affairs is like a Balance sheet. The difference between assets and liabilities side represents “Opening Capital”.

**Format of statement of affairs**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>xxxx</td>
<td>Cash in Hand</td>
<td>xxxx</td>
</tr>
<tr>
<td>Bills Payable</td>
<td>xxxx</td>
<td>Cash at Bank</td>
<td>xxxx</td>
</tr>
<tr>
<td>Outstanding Expenses</td>
<td>xxxx</td>
<td>Sundry Debtors</td>
<td>xxxx</td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>xxxx</td>
<td>Bills Receivable</td>
<td>xxxx</td>
</tr>
<tr>
<td>Capital (Balancing figure)</td>
<td>xxxx</td>
<td>Stock in trade</td>
<td>xxxx</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Prepaid Expenses</td>
<td>xxxx</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Fixed Assets</td>
<td>xxxx</td>
</tr>
<tr>
<td></td>
<td>xxxx</td>
<td>xxxx</td>
<td></td>
</tr>
</tbody>
</table>

**Step 2** → Ascertainment Closing Capital: Prepare a statement of affairs (after all adjustments*) at the end of the accounting period, to ascertain closing capital.

**Step 3** → Add the amount of drawings (whether in cash or in kind) to the closing capital.

**Step 4** → Deduct the amount of Additional Capital introduced, from the above, to get Adjusted capital.

**Step 5** → Ascertainment profit or loss by deducting opening capital from the adjusted closing capital.

Adjusted closing capital = Closing capital + Drawings — Additional capital introduced during the year.

*Adjustments: Depreciation, interest on capitals, interest on drawings, Provision for Bad debts etc.

**Statement of Profit or Loss for the year ______**

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Closing Capital</td>
<td>xxx x x x</td>
</tr>
<tr>
<td>Add: Drawings</td>
<td>xxx</td>
</tr>
<tr>
<td></td>
<td>xxx</td>
</tr>
<tr>
<td>Less: Additional capital introduced</td>
<td>xxx</td>
</tr>
<tr>
<td>Adjusted closing capital</td>
<td>xxx</td>
</tr>
<tr>
<td>Less: Opening capital</td>
<td>xxx</td>
</tr>
<tr>
<td>Net Profit or loss for the year</td>
<td>xxx</td>
</tr>
</tbody>
</table>

**Note:** If adjusted closing capital is more than opening capital = Profit
If adjusted closing capital is less than opening capital = Loss

**Illustration : 1**

Find out profit or loss from the following information.

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Capital</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Drawings</td>
<td>90,000</td>
</tr>
<tr>
<td>Closing Capital</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Additional Capital during the year</td>
<td>30,000</td>
</tr>
</tbody>
</table>
Solution:

Statement of profit or loss

Rs.

Closing capital 5,00,000
Add: Drawings 90,000
5,90,000
Less: Additional Capital 30,000
Adjusted closing capital 5,60,000
Less: Opening capital 4,00,000
Profit for the year 1,60,000

Illustration : 2

Calculate the missing information from the following.

Rs.
Profit made during the year 4,800
Capital at the end ?
Additional Capital introduced during the year 4,000
Drawings 2,400
Capital in the beginning 9,600

Solution:

Rs.
Closing capital (Balancing figure) 16,000
Add: Drawings 2,400
18,400
Less: Additional Capital 4,000
Adjusted closing capital 14,400
Less: Opening capital 9,600
Profit made during the year 4,800

Ans: Capital at the end Rs.16,000.

Note:

Step 1 \( \rightarrow \) Add Profit of Rs.4,800 with opening capital Rs.9,600 = Adjusted closing capital Rs.14,400.

Step 2 \( \rightarrow \) Add Additional capital of Rs.4,000 with Adjusted closing capital Rs.14,400 = Rs.18,400

Step 3 \( \rightarrow \) Deduct drawings Rs.2,400 from the total amount arrived (Step 2) Rs. 18,400 = Closing capital Rs.16,000.

Illustration : 3

Mr. Suresh started business with Rs.2,00,000 on 1st April 2003. His books are kept under single entry. On 31st March, 2004 his position was as under:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>40,000</td>
<td>Cash in Hand</td>
<td>6,000</td>
</tr>
<tr>
<td>Bills Payable</td>
<td>5,000</td>
<td>Cash at Bank</td>
<td>10,000</td>
</tr>
<tr>
<td>Outstanding creditors</td>
<td>7,500</td>
<td>Furniture</td>
<td>30,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Plant &amp; Machinery</td>
<td>1,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Sundry Debtors</td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stock</td>
<td>90,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Bills Receivable</td>
<td>15,000</td>
</tr>
</tbody>
</table>

Ascertain the profit or loss made by Mr. Suresh for the year ended 31st March 2004.

Solution:

Calculation of closing capital:

Statement of affairs of Mr. Suresh as on 31.3.2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry creditors</td>
<td>40,000</td>
<td>Cash in hand</td>
<td>6,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>5,000</td>
<td>Cash at Bank</td>
<td>10,000</td>
</tr>
<tr>
<td>Outstanding creditors</td>
<td>7,500</td>
<td>Furniture</td>
<td>30,000</td>
</tr>
</tbody>
</table>
Statement of profit or loss for the year ended 31.3.2004

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Closing capital</td>
</tr>
<tr>
<td>Less: Opening capital</td>
</tr>
<tr>
<td>Profit for the year</td>
</tr>
</tbody>
</table>

Illustration : 4

Prakash keeps his books by ‘Single Entry System’. His position on 1.4.2003 and 31.3.2004 was as follows:

<table>
<thead>
<tr>
<th>1.4.2003</th>
<th>31.3.2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Cash</td>
<td>500</td>
</tr>
<tr>
<td>Bank Balance</td>
<td>10,000</td>
</tr>
<tr>
<td>Stock</td>
<td>7,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>30,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>6,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>6,000</td>
</tr>
</tbody>
</table>

He introduced an additional capital of Rs.8,000 during the financial year. He withdrew Rs.14,000 for domestic purpose. Find out the profit for the year ended 31.3.2004.
Illustration : 5

Mrs. Vanitha keeps her books on singly entry basis. Find out the profit or loss made for the period ending 31.3.2004.

<table>
<thead>
<tr>
<th>Assets &amp; Liabilities</th>
<th>1.4.2003</th>
<th>31.3.2004</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>Bank Balance</td>
<td>3,500 (Cr.)</td>
<td>4,500 (Dr.)</td>
</tr>
<tr>
<td>Cash on hand</td>
<td>200</td>
<td>300</td>
</tr>
<tr>
<td>Stock</td>
<td>3,000</td>
<td>4,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>8,500</td>
<td>7,600</td>
</tr>
<tr>
<td>Plant</td>
<td>20,000</td>
<td>20,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>10,000</td>
<td>10,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>15,000</td>
<td>18,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>15,000</td>
<td>18,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>15,000</td>
<td>18,000</td>
</tr>
</tbody>
</table>

Mrs. Vanitha had withdrawn Rs. 10,000 for her personal use and had introduced fresh capital of Rs. 4,000. A provision of 5% on debtors is necessary. Write off depreciation on plant at 10% and furniture at 15%.

Solution:

i) Calculation of Opening Capital:

Statement of affairs of Mrs. Vanitha as on 1.4.2003

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank Balance (O/d)</td>
<td>3,500</td>
<td>Cash on hand</td>
<td>200</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>15,000</td>
<td>Stock</td>
<td>3,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Sundry Debtors</td>
<td>8,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Plant</td>
<td>20,000</td>
</tr>
<tr>
<td>Opening capital</td>
<td>23,200</td>
<td>Furniture</td>
<td>10,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>41,700</td>
<td></td>
<td>41,700</td>
</tr>
</tbody>
</table>

ii) Calculation of closing capital

Statement of affairs of Mrs. Vanitha as on 31.3.2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>18,000</td>
<td>Bank balance</td>
<td>4,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash on hand</td>
<td>300</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stock</td>
<td>4,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Sundry Debtors</td>
<td>7,600</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Less: Provision</td>
<td>380</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Plant</td>
<td>20,000</td>
</tr>
<tr>
<td>Closing capital</td>
<td>24,520</td>
<td>Less: Depreciation</td>
<td>2,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td></td>
<td>Furniture</td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Less: Depreciation</td>
<td>1,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>42,520</td>
<td></td>
<td>42,520</td>
</tr>
</tbody>
</table>

Statement of Profit or loss for the period ended 31.3.2004

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Closing capital</td>
<td>24,520</td>
</tr>
<tr>
<td>Add: Drawings</td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td>34,520</td>
</tr>
<tr>
<td>Less: Additional capital</td>
<td>4,000</td>
</tr>
<tr>
<td>Adjusted closing capital</td>
<td>30,520</td>
</tr>
<tr>
<td>Less: Opening capital</td>
<td>23,200</td>
</tr>
<tr>
<td></td>
<td>7,320</td>
</tr>
</tbody>
</table>
Illustration 6:

Ram and Laxman are equal partners in a business in which the books are kept by single entry. On 1.4.2004 their position was as under:

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital accounts:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ram 2,50,000</td>
<td></td>
<td>Cash in hand</td>
<td>5,000</td>
</tr>
<tr>
<td>Laxman 2,50,000</td>
<td>5,00,000</td>
<td>Cash at bank</td>
<td>15,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>20,000</td>
<td>Bills receivable</td>
<td>30,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>30,000</td>
<td>Stock</td>
<td>1,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Furniture</td>
<td>1,25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Plant &amp; Machinery</td>
<td>2,50,000</td>
</tr>
<tr>
<td></td>
<td>5,50,000</td>
<td></td>
<td>5,50,000</td>
</tr>
</tbody>
</table>

On 31.3.2005 their position was as under:

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in hand</td>
<td>2,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>35,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>30,000</td>
</tr>
<tr>
<td>Bills receivable</td>
<td>26,000</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>10,000</td>
</tr>
<tr>
<td>Stock</td>
<td>1,10,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>10,000</td>
</tr>
</tbody>
</table>

Plant & Machinery and furniture are to be depreciated by 10%.

Drawings: Ram 30,000
Laxman 25,000

Ascertain the profit for the year ended 31.3.2005.

Solution:

Calculation of closing capital:

Statement of affairs of Ram & Laxman as on 31.3.2005

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry creditors</td>
<td>35,000</td>
<td>Cash in hand</td>
<td>2,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bills payable</td>
<td>10,000</td>
<td>Cash at bank</td>
<td>10,000</td>
<td>Sundry debtors</td>
<td>30,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Bills receivable</td>
<td>26,000</td>
<td>Stock</td>
<td>1,10,000</td>
</tr>
<tr>
<td>Closing capital</td>
<td>4,70,500</td>
<td>Plant &amp; Machinery</td>
<td>2,50,000</td>
<td>Less: Depreciation</td>
<td>25,000</td>
</tr>
<tr>
<td>(Combined capital</td>
<td></td>
<td>Furniture</td>
<td>1,25,000</td>
<td>Less: Depreciation</td>
<td>12,500</td>
</tr>
<tr>
<td>of Ram &amp; Laxman)</td>
<td>5,15,500</td>
<td></td>
<td></td>
<td></td>
<td>1,12,500</td>
</tr>
<tr>
<td></td>
<td>5,15,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Statement of profit or loss for the year ended 31.3.2005

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Combined closing capital</td>
<td>4,70,500</td>
</tr>
<tr>
<td>Add: Drawings:</td>
<td></td>
</tr>
<tr>
<td>Ram</td>
<td>30,000</td>
</tr>
<tr>
<td>Laxman</td>
<td>25,000</td>
</tr>
<tr>
<td>Adjusted closing capital</td>
<td>5,25,500</td>
</tr>
<tr>
<td>Less: Combined opening capital</td>
<td>5,00,000</td>
</tr>
<tr>
<td>Profit for the year</td>
<td>25,500</td>
</tr>
</tbody>
</table>
2.5.2 Conversion Method: (Conversion of single entry into double entry system)

If it is desired to calculate profit by preparing Trading and Profit and Loss account under single entry then it is called conversion method. Following steps are necessary to prepare Trading and Profit and Loss account and Balance Sheet from the incomplete information.

**Step 1** → **Opening Statement of Affairs:** Prepare statement of affairs in the beginning so as to calculate capital in the beginning.

**Step 2** → **Other Accounts:** Then prepare (i) Total debtors account, and (ii) Total Creditors account, to find out credit sales, credit purchases, creditors or debtors balance either in the beginning or at the end.

**Step 3** → **Total sales and total purchase:** After preparing these accounts, calculate

1. **Total sales,** by adding cash sales and credit sales, and
2. **Total purchases** by adding cash purchases and credit purchases.

**Step 4** → **Final Account:** Now prepare Trading, Profit and Loss account and Balance Sheet.

**Calculation of Missing Figures:**

The information which is needed for preparing the final accounts is not directly available from the incomplete records. Hence, we need to find out such missing figures by preparing relevant accounts. Let us learn how such missing figures can be extracted from incomplete records by preparing the relevant accounts. The important ones are discussed below:

1. Calculation of total purchases or creditors in the beginning or at the end of the year.
2. Calculation of total sales or debtors in the beginning or at the end of the year.

**(i) Ascertainment of Total Purchases:**

Total purchases are calculated by adding cash and credit purchases. Cash purchases, are given in Cash Book. Credit purchases are calculated by preparing total creditors account. The specimen of Total Creditors Account is given below:

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Total Creditors Account</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Amount Rs.</td>
<td>Particulars</td>
</tr>
<tr>
<td>To Cash paid</td>
<td>..</td>
<td>By Balance b/d (Opening Balance)</td>
</tr>
<tr>
<td>To Discount Received</td>
<td>..</td>
<td>By Credit Purchases (balancing figure)</td>
</tr>
<tr>
<td>To Purchases Returns</td>
<td>..</td>
<td></td>
</tr>
<tr>
<td>To Balance c/d (Closing Balance)</td>
<td>..</td>
<td></td>
</tr>
</tbody>
</table>

Look at the following illustration and see how total purchases have been found out.

**Illustration 7:** From the following information, you are required to calculate total purchases:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash purchases</td>
<td>17,000</td>
</tr>
<tr>
<td>Creditors as on April 1, 2002</td>
<td>8,000</td>
</tr>
<tr>
<td>Cash paid to creditors</td>
<td>31,000</td>
</tr>
<tr>
<td>Purchases returns</td>
<td>1,000</td>
</tr>
<tr>
<td>Creditors as on March 31, 2003</td>
<td>13,400</td>
</tr>
</tbody>
</table>
Solution:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash paid</td>
<td>31,000</td>
<td>By Balance b/d</td>
<td>8,000</td>
</tr>
<tr>
<td>To Purchases return</td>
<td>1,000</td>
<td>(Opening Balance)</td>
<td></td>
</tr>
<tr>
<td>To Balance c/d (Closing Balance)</td>
<td>13,400</td>
<td>By Credit Purchases</td>
<td>37,400</td>
</tr>
</tbody>
</table>

Total Creditors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d (Op. Bal.)</td>
<td>.........</td>
<td>By Cash received</td>
<td>.........</td>
</tr>
<tr>
<td>To Credit Sales (Bal. Fig.)</td>
<td>.........</td>
<td>By Discount Allowed</td>
<td>.........</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Sales Returns</td>
<td>.........</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d (Clo. Bal.)</td>
<td>.........</td>
</tr>
</tbody>
</table>

(ii) Ascertainment of Total Sales:

Total Purchases = Cash purchases + Credit purchases

= 17,000 + 37,400

= Rs. 54,400.

Illustration 8:

From the following facts you are required to calculate total sales made during the period:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors as on April 1, 2002</td>
<td>20,400</td>
<td>Sundry Debtors as on March 31, 2003</td>
<td>27,600</td>
</tr>
<tr>
<td>Cash received</td>
<td></td>
<td>Cash Sales</td>
<td>56,800</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>60,800</td>
<td>Sales Return</td>
<td>5,400</td>
</tr>
</tbody>
</table>

Dr. Total Debtors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Amount Rs.</th>
<th>Particulars</th>
<th>Amount Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d (Op. Bal.)</td>
<td>20,400</td>
<td>By Cash received</td>
<td>60,800</td>
</tr>
<tr>
<td>To Credit Sales (Bal. Fig.)</td>
<td>73,400</td>
<td>By Sales Return</td>
<td>5,400</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d (Clo. Bal.)</td>
<td>27,600</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>93,800</td>
</tr>
</tbody>
</table>

Total Sales = Cash Sales + Credit Sales

= Rs. 56,800 + Rs. 73,400

= Rs. 1,30,200

(iii) Ascertainment of balances of sundry debtors and sundry creditors:

If credit sales and credit purchases are given, the opening or closing balances of debtors and/or creditors can be ascertained by preparing total debtors account and total creditors accounts.

Illustration : 9

From the following particulars, calculate closing balances Debtors and Creditors:
Illustration : 10

From the following details, find out Credit Sales for the year.

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening balance of Sundry Debtors</td>
<td>30,000</td>
</tr>
<tr>
<td>Cash received during the year</td>
<td>2,05,000</td>
</tr>
<tr>
<td>Closing balance of Sundry debtors</td>
<td>48,000</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>13,000</td>
</tr>
<tr>
<td>Goods returned by Customers</td>
<td>14,000</td>
</tr>
</tbody>
</table>

Solution:

<table>
<thead>
<tr>
<th>Dr. Total Debtors Account</th>
<th>Cr. Total Debtors Account</th>
</tr>
</thead>
<tbody>
<tr>
<td>Particulars</td>
<td>Amount Rs.</td>
</tr>
<tr>
<td>To Balance b/d (1.4.2001)</td>
<td>30,000</td>
</tr>
<tr>
<td>To Credit Sales</td>
<td>2,50,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,80,000</td>
</tr>
</tbody>
</table>

Illustration : 11

From the following details find out Credit Purchases.

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening balance of Sundry Creditors</td>
<td>50,000</td>
</tr>
<tr>
<td>Closing balance of Sundry Creditors</td>
<td>60,000</td>
</tr>
<tr>
<td>Cash paid</td>
<td>2,65,000</td>
</tr>
<tr>
<td>Discount received</td>
<td>15,000</td>
</tr>
<tr>
<td>Purchase returns</td>
<td>15,000</td>
</tr>
</tbody>
</table>

Solution:

<table>
<thead>
<tr>
<th>Dr. Total Creditors Account</th>
<th>Cr. Total Creditors Account</th>
</tr>
</thead>
</table>
### Solution:

#### Total Creditors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash paid</td>
<td>2,65,000</td>
<td>By Balance c/d</td>
<td>50,000</td>
</tr>
<tr>
<td>To Discount received</td>
<td>15,000</td>
<td>By Credit Purchases</td>
<td>3,05,000</td>
</tr>
<tr>
<td>To Purchase return</td>
<td>15,000</td>
<td>(Balancing figure)</td>
<td></td>
</tr>
<tr>
<td>By Balance c/d</td>
<td>60,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>3,55,000</strong></td>
<td><strong>Total</strong></td>
<td><strong>3,55,000</strong></td>
</tr>
</tbody>
</table>

#### Illustration : 12

Find out total purchases and total sales from the following details by making necessary accounts:

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening balance of Sundry debtors</td>
</tr>
<tr>
<td>Opening balance of Sundry creditors</td>
</tr>
<tr>
<td>Cash collected from Sundry debtors</td>
</tr>
<tr>
<td>Discount received</td>
</tr>
<tr>
<td>Cash Paid to Sundry creditors</td>
</tr>
<tr>
<td>Discount allowed</td>
</tr>
<tr>
<td>Return inwards</td>
</tr>
<tr>
<td>Return outwards</td>
</tr>
<tr>
<td>Closing balance of Sundry debtors</td>
</tr>
<tr>
<td>Closing balance of Sundry creditors</td>
</tr>
<tr>
<td>Cash Purchases</td>
</tr>
<tr>
<td>Cash Sales</td>
</tr>
</tbody>
</table>

### Solution:

#### i) Calculation of Credit Sales

#### Total Debtors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d</td>
<td>50,000</td>
<td>By Cash received</td>
<td>3,00,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Discount allowed</td>
<td>5,000</td>
</tr>
<tr>
<td>To Credit Sales</td>
<td>2,96,000</td>
<td>By Returns Inwards</td>
<td>6,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td></td>
<td>By Balance c/d</td>
<td>35,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>3,46,000</strong></td>
<td><strong>Total</strong></td>
<td><strong>3,46,000</strong></td>
</tr>
</tbody>
</table>

#### ii) Calculation of Credit Purchases

#### Total Creditors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Discount received</td>
<td>1,500</td>
<td>By Balance b/d</td>
<td>30,000</td>
</tr>
<tr>
<td>To Cash paid</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Return outwards</td>
<td>8,000</td>
<td>By Credit Purchases</td>
<td>24,500</td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>25,000</td>
<td>(Balancing figure)</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>54,500</strong></td>
<td><strong>Total</strong></td>
<td><strong>54,500</strong></td>
</tr>
</tbody>
</table>

Total Purchases = Cash purchases + Credit Purchases

Total Sales = Cash sales + Credit sales

100 101
Illustration : 13

Mr. James commenced business on 1.4.2004 with a capital of Rs.75,000. He immediately bought furniture for Rs.12,000. During the year, he borrowed Rs.15,000 from his wife as loan. He has withdrawn Rs.21,600 for his family expenses. From the following particulars you are required to prepare Trading and Profit & Loss A/c and Balance Sheet as on 31.3.2005.

Solution:

i) Calculation of Credit Sales

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash received from Sundry debtors</td>
<td>1,21,000</td>
</tr>
<tr>
<td>Cash paid to Sundry creditors</td>
<td>1,75,000</td>
</tr>
<tr>
<td>Cash Sales</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Cash Purchases</td>
<td>40,000</td>
</tr>
<tr>
<td>Carriage inwards</td>
<td>4,500</td>
</tr>
<tr>
<td>Discount allowed to Sundry debtors</td>
<td>4,000</td>
</tr>
<tr>
<td>Salaries</td>
<td>5,000</td>
</tr>
<tr>
<td>Office Expenses</td>
<td>4,000</td>
</tr>
<tr>
<td>Advertisement</td>
<td>5,000</td>
</tr>
<tr>
<td>Closing balance of Sundry debtors</td>
<td>75,000</td>
</tr>
<tr>
<td>Closing balance of Sundry creditors</td>
<td>50,000</td>
</tr>
<tr>
<td>Closing Stock</td>
<td>35,000</td>
</tr>
<tr>
<td>Closing cash balance</td>
<td>43,900</td>
</tr>
</tbody>
</table>

Provide 10% depreciation on furniture.

ii) Calculation of Credit Purchases

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash paid</td>
<td>1,75,000</td>
</tr>
<tr>
<td>Balance c/d</td>
<td>50,000</td>
</tr>
</tbody>
</table>

Trading and Profit and Loss Account of Mr. James for the year ended 31.3.2005

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>---</td>
</tr>
<tr>
<td>To Purchases:</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Cash</td>
<td>40,000</td>
</tr>
<tr>
<td>Credit</td>
<td>2,25,000</td>
</tr>
<tr>
<td>To Carriage inwards</td>
<td>4,500</td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>65,500</td>
</tr>
<tr>
<td>To Discount allowed</td>
<td>4,000</td>
</tr>
<tr>
<td>To Salaries</td>
<td>5,000</td>
</tr>
<tr>
<td>To Office expenses</td>
<td>4,000</td>
</tr>
<tr>
<td>To Advertisement</td>
<td>5,000</td>
</tr>
<tr>
<td>To Depreciation on furniture</td>
<td>1,200</td>
</tr>
<tr>
<td>To Net Profit</td>
<td>46,300</td>
</tr>
<tr>
<td>(transferred to Capital A/c)</td>
<td>65,500</td>
</tr>
</tbody>
</table>

Balance Sheet

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d</td>
<td>---</td>
</tr>
<tr>
<td>By Cash received</td>
<td>1,21,000</td>
</tr>
<tr>
<td>By Discount allowed</td>
<td>4,000</td>
</tr>
<tr>
<td>To Credit sales</td>
<td>2,00,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash paid</td>
<td>1,75,000</td>
</tr>
<tr>
<td>Balance c/d</td>
<td>50,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d</td>
<td>---</td>
</tr>
<tr>
<td>By Cash received</td>
<td>1,21,000</td>
</tr>
<tr>
<td>By Discount allowed</td>
<td>4,000</td>
</tr>
<tr>
<td>To Credit sales</td>
<td>2,00,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash paid</td>
<td>1,75,000</td>
</tr>
<tr>
<td>Balance c/d</td>
<td>50,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d</td>
<td>---</td>
</tr>
<tr>
<td>By Cash received</td>
<td>1,21,000</td>
</tr>
<tr>
<td>By Discount allowed</td>
<td>4,000</td>
</tr>
<tr>
<td>To Credit sales</td>
<td>2,00,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td>2,00,000</td>
</tr>
</tbody>
</table>
Balance Sheet of Mr. James as on 31.3.2005

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>75,000</td>
<td>Furniture</td>
<td>12,000</td>
</tr>
<tr>
<td>Add: Net Profit</td>
<td>46,300</td>
<td>Less: Depreciation</td>
<td>1,200</td>
</tr>
<tr>
<td></td>
<td>121,300</td>
<td></td>
<td>10,800</td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>21,600</td>
<td>Sundry Debtors</td>
<td>75,000</td>
</tr>
<tr>
<td>Loan from wife</td>
<td>15,000</td>
<td>Closing Stock</td>
<td>35,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>50,000</td>
<td>Cash</td>
<td>43,900</td>
</tr>
<tr>
<td></td>
<td>1,64,700</td>
<td></td>
<td>1,64,700</td>
</tr>
</tbody>
</table>

Illustration : 14

Mrs. Malathy maintained her account books on single entry system. On 1.4.2003 her capital was Rs.2,50,000.

Additional information:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening stock</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Cash received from Sundry debtors</td>
<td>25,000</td>
</tr>
<tr>
<td>Cash sales</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Cash paid to Sundry creditors</td>
<td>30,000</td>
</tr>
<tr>
<td>Opening Sundry debtors</td>
<td>20,000</td>
</tr>
<tr>
<td>Opening Sundry creditors</td>
<td>91,500</td>
</tr>
<tr>
<td>Business expenses</td>
<td>60,400</td>
</tr>
<tr>
<td>Free hold premises (31.3.2004)</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Furniture (31.3.2004)</td>
<td>3,600</td>
</tr>
<tr>
<td>Closing stock</td>
<td>1,30,000</td>
</tr>
<tr>
<td>Closing Sundry debtors</td>
<td>40,000</td>
</tr>
<tr>
<td>Closing Sundry creditors</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Closing cash balance</td>
<td>27,500</td>
</tr>
</tbody>
</table>

Prepare trading and profit & loss account for the year ended 31.03.2004 and balance sheet as on that date.

Solution:

i) Calculation of credit sales:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Total Debtors Account</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d</td>
<td>20,000</td>
<td>25,000</td>
</tr>
<tr>
<td>To Credit Sales</td>
<td>45,000</td>
<td>40,000</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td>65,000</td>
<td>65,000</td>
</tr>
</tbody>
</table>

ii) Calculation of credit purchases:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Total Creditors Account</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Cash paid</td>
<td>30,000</td>
<td>91,500</td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>1,00,000</td>
<td>38,500</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td>1,30,000</td>
<td>1,30,000</td>
</tr>
</tbody>
</table>

Trading and Profit & Loss Account of Mrs. Malathy for the year ended 31.3.2004

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td>1,25,000</td>
<td>By Sales:</td>
<td></td>
</tr>
<tr>
<td>To Purchases - Credit</td>
<td>38,500</td>
<td>Cash</td>
<td>1,00,000</td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>1,11,500</td>
<td>Credit</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Closing stock</td>
<td>1,30,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>2,75,000</td>
</tr>
<tr>
<td>To Business expenses</td>
<td>60,400</td>
<td>By Gross Profit b/d</td>
<td>1,11,500</td>
</tr>
<tr>
<td>To Net profit</td>
<td>51,100</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Transferred to capital A/c)</td>
<td>1,11,500</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Balance Sheet of Mrs. Malathy as on 31.3.2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>2,50,000</td>
<td></td>
<td>Free hold premises</td>
<td>2,00,000</td>
<td></td>
</tr>
<tr>
<td>Add: Net profit</td>
<td>51,100</td>
<td></td>
<td>Furniture</td>
<td>3,600</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,01,100</td>
<td></td>
<td>Closing stock</td>
<td>1,30,000</td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>1,00,000</td>
<td></td>
<td>Sundry Debtors</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>27,500</td>
<td></td>
<td>Cash in hand</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,01,100</td>
<td></td>
<td></td>
<td>4,01,100</td>
<td></td>
</tr>
</tbody>
</table>

Illustration 15:

From the following details, prepare Trading and Profit & Loss account for the period ended 31.3.2004 and a Balance sheet on that date.

As on 1.4.2003 As on 31.3.2004

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock</td>
<td>50,000</td>
<td>25,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>1,25,000</td>
<td>1,75,000</td>
</tr>
<tr>
<td>Cash</td>
<td>12,500</td>
<td>20,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>5,000</td>
<td>5,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>75,000</td>
<td>87,500</td>
</tr>
</tbody>
</table>

Other Details:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Drawings</td>
<td>20,000</td>
</tr>
<tr>
<td>Discount received</td>
<td>7,500</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>5,000</td>
</tr>
<tr>
<td>Sundry expenses</td>
<td>17,500</td>
</tr>
<tr>
<td>Cash paid to creditors</td>
<td>2,25,000</td>
</tr>
</tbody>
</table>

Solution:

i) Calculation of opening capital:

Statement of affairs as on 1.4.2003

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>75,000</td>
<td>Stock</td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Sundry Debtors</td>
<td>1,25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash</td>
<td>12,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Furniture</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>1,17,500</td>
<td></td>
<td>1,92,500</td>
</tr>
</tbody>
</table>

ii) Calculation of Credit Sales:

Total Debtors Account

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Balance b/d</td>
<td>1,25,000</td>
<td>By Discount allowed</td>
<td>5,000</td>
</tr>
<tr>
<td>To Credit sales</td>
<td>3,30,000</td>
<td>By Cash received</td>
<td>2,67,500</td>
</tr>
<tr>
<td>(Balancing figure)</td>
<td></td>
<td></td>
<td>7,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Sales returns</td>
<td>1,75,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>4,55,000</td>
</tr>
<tr>
<td></td>
<td>4,55,000</td>
<td></td>
<td>4,55,000</td>
</tr>
</tbody>
</table>
### Calculation of Credit Purchases:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Discount received</td>
<td>7,500</td>
<td>By Balance b/d</td>
<td>75,000</td>
</tr>
<tr>
<td>To Cash paid</td>
<td>2,25,000</td>
<td>By Credit purchases</td>
<td>2,47,500</td>
</tr>
<tr>
<td>To Purchases return</td>
<td>2,500</td>
<td>(Balancing figure)</td>
<td></td>
</tr>
<tr>
<td>To Balance c/d</td>
<td>87,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,22,500</td>
<td></td>
<td>3,22,500</td>
</tr>
</tbody>
</table>

#### Trading and Profit and Loss Account

**for the year ended 31.3.2004**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td>50,000</td>
<td>By Sales:</td>
<td>Cash</td>
<td>2,500</td>
<td>3,32,500</td>
</tr>
<tr>
<td>To Purchases</td>
<td>2,47,500</td>
<td></td>
<td>Credit</td>
<td>3,30,000</td>
<td></td>
</tr>
<tr>
<td>Less: Purchase Returns</td>
<td>2,45,000</td>
<td></td>
<td></td>
<td>55,000</td>
<td>3,25,000</td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>3,50,000</td>
<td></td>
<td>By Closing Stock</td>
<td>25,000</td>
<td>3,50,000</td>
</tr>
<tr>
<td>To Discount allowed</td>
<td>5,000</td>
<td>By Gross</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Sundry Expenses</td>
<td>17,500</td>
<td>Profit b/d</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>40,000</td>
<td>By Discount received</td>
<td>7,500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Transferred to Capital A/c)</td>
<td>62,500</td>
<td></td>
<td></td>
<td></td>
<td>62,500</td>
</tr>
</tbody>
</table>

### Balance Sheet as on 31.3.2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>1,17,500</td>
<td></td>
<td>Furniture</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Add: Net Profit</td>
<td>40,000</td>
<td></td>
<td>Sundry Debtors</td>
<td>1,75,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,57,500</td>
<td></td>
<td>Closing Stock</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Less: Drawings</td>
<td>20,000</td>
<td></td>
<td>Cash</td>
<td>20,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,37,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>87,500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,25,000</td>
<td></td>
<td></td>
<td>2,25,000</td>
<td></td>
</tr>
</tbody>
</table>

### QUESTIONS

**I. Objective Type:**

**a) Fill in the blanks:**

1. Incomplete records are those records which are not kept under ________ system.
2. Statement of affairs method is also called as ________ method.
3. ________ capital can be found by preparing a statement of affairs at the beginning of the year.
4. A statement of affairs resembles a ________.
5. Closing capital can be found by preparing a statement affairs at the ________ of the year.
6. In ________ system, only personal and cash accounts are opened.
7. Credit purchase can be ascertained as the balancing figure in the ________.
8. The excess of assets over liabilities is ________.

9. The total assets of a proprietor are Rs.5,00,000. His liabilities Rs.3,50,000. Then his capital in the business is ________.

10. A firm has assets worth Rs.60,000 and capital Rs.45,000. Then it’s liabilities is ________.

(Answer: 1) Double Entry; 2) Net worth; 3) Opening; 4) Balance Sheet; 5) end; 6) Single entry; 7) Total creditors A/c.; 8) Capital; 9) Rs. 1,50,000; 10) Rs.15,000)

b) Choose the Correct Answer:

1. Under the networth method the basis for ascertaining the profit is
   a) the difference between the capital on two dates.
   b) the difference between the liabilities on two dates.
   c) the difference between the gross assets on two dates.

2. Incomplete records are generally used by
   a) Small traders  b) Company  c) Government

3. Credit sales is obtained from
   a) Bills Receivable account  b) Total debtors account
   c) Total creditors account

4. Single Entry System is
   a) a Scientific method  b) an Incomplete Double Entry System
   c) None of the above.

5. The capital of a business is ascertained by preparing
   a) Trading account b) Statement of profit or loss
   c) Statement of affairs

(Answers: 1.(a); 2.(a); 3.(b); 4. (b); 5.(c))

II. Other Questions:

1. What is the meaning for incomplete records?
2. Define Single Entry System.
3. What are the features of Single Entry?
4. What are the limitations of Single Entry System?
5. What is networth method?
6. What is conversion method?
7. What is statement of affairs?
8. What are the differences between single entry and Double Entry?
9. Mention the procedure to calculate profit by statement of affairs method.
10. Mention the procedure to calculate profit by conversion method.

III. Problems:

Statement of Affairs method:

1. What shall be the profits of the concern if:
   Opening capital Rs. 1,60,000
   Closing capital Rs. 1,80,000
   Drawings Rs. 36,000
   Additional Capital Rs. 10,000

(Answer: Rs.46,000)

2. Calculate the missing information:
   Closing capital Rs. 32,000
   Drawings Rs. 4,800
   Additional Capital Rs. 8,000
   Profit made during the year Rs. 9,600

(Answer: Opening capital Rs.19,200)
3. Calculate the missing information when there is no drawings:
   - Capital at the end: Rs. 91,000
   - Capital in the beginning: Rs. 35,000
   - Profits made during the year: Rs. 14,000
   
   (Answer: Capital introduced Rs. 42,000)

4. Calculate the missing information:
   - Closing capital: Rs. 1,63,800
   - Additional Capital: Rs. 42,300
   - Drawings: Rs. 25,200
   - Loss: Rs. 12,600

   (Answer: Opening Capital Rs. 1,59,300)

5. Mr. Rajesh maintains his books on single entry system. He gives you the following information.

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital as on 1.4.2003: 4,80,000</td>
</tr>
<tr>
<td>Capital as on 31.3.2004: 5,40,000</td>
</tr>
<tr>
<td>Drawings during the financial year: 1,50,000</td>
</tr>
<tr>
<td>Capital introduced during the financial year: 90,000</td>
</tr>
</tbody>
</table>

   You are required to calculate profit or loss made by Mr. Rajesh during 2003 - 04.

   (Answer: Profit Rs. 1,20,000)

6. Calculate the missing information:
   - Rs.        |
   | Capital in the beginning: 24,000 |
   | Profits made during the year: 9,000 |

   Capital introduced during the year: 12,000
   Capital at the end: 39,000

   (Answer: Drawings Rs. 6,000)

7. Calculate the missing information:
   - Drawings: Rs. 50,000
   - Additional Capital: Rs. 10,000
   - Opening Capital: Rs. 1,00,000
   - Profit made during the year: Rs. 25,000

   (Answer: Closing capital Rs. 85,000)

8. Find out the profit of the business for the year 1996 from the particulars given below:

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital on 1.4.1996: 30,000</td>
</tr>
<tr>
<td>Capital introduced during 1996: 6,000</td>
</tr>
<tr>
<td>Capital as on 31.3.1997: 42,000</td>
</tr>
<tr>
<td>Drawings: 3,000</td>
</tr>
</tbody>
</table>

   (Answer: Profit Rs. 9,000 - October 2000)

9. Calculate the missing figure:
   - Rs.        |
   | Profit made during the year: 2,500 |
   | Capital at the end: 6,000 |
   | Capital introduced during the year: 2,000 |
   | Drawings: 1,200 |
   | Capital at the beginning: ? |

   (Answer: Rs. 2,700 - Oct. 2001)
10. Calculate the missing figure:

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital at the beginning</td>
<td>15,000</td>
</tr>
<tr>
<td>Profits made during the year</td>
<td>8,000</td>
</tr>
<tr>
<td>Capital at the end</td>
<td>20,000</td>
</tr>
<tr>
<td>Drawings</td>
<td>?</td>
</tr>
</tbody>
</table>

(Answer: Rs.3,000 - March 2002)

11. Mrs. Sheela keeps her books by single entry. She started business on 1st April 2002 with Rs. 3,00,000. On 31st March 2003 her position was as under:

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in hand</td>
<td>8,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>50,000</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>20,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>10,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>40,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>8,000</td>
</tr>
<tr>
<td>Plant</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Stock</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Bills Receivable</td>
<td>15,000</td>
</tr>
</tbody>
</table>

Ascertain the profit or loss made by Mrs. Sheela during 2002 – 03.

(Answer: Profit Rs. 2,15,000)

12. Mrs. Revathi started business with Rs.1,20,000 as capital on 1.4.2003. During the year she has withdrawn at the rate of Rs.1,000 per month. She introduced Rs.20,000 as additional capital. Her position on 31.3.2004 was as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank balance</td>
<td>8,000</td>
</tr>
<tr>
<td>Stock</td>
<td>80,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>50,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>2,500</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>2,000</td>
</tr>
<tr>
<td>Sundry Creditors</td>
<td>25,000</td>
</tr>
<tr>
<td>Expenses outstanding</td>
<td>1,000</td>
</tr>
</tbody>
</table>

She keeps her books under single entry system. Determine her profit or loss for the year 2003-04.

(Answer: Loss Rs.11,500)

13. Mr. Murali keeps his books under single entry system. Assets and liabilities on 31.3.2002 and 31.3.2003 stood as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>31.3.2002</th>
<th>31.3.2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>15,000</td>
<td>30,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>15,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>75,000</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Stock</td>
<td>35,000</td>
<td>50,000</td>
</tr>
<tr>
<td>Cash Balance</td>
<td>5,000</td>
<td>60,000</td>
</tr>
</tbody>
</table>

He introduced an additional capital of Rs.15,000 during the year. He withdrew Rs.35,000 for domestic purpose. Find out the profit or loss for 2002-03.

(Answer: Profit Rs.1,00,000)

14. The balances appear in Bharanidharans’ books which are kept on single entry basis:
<table>
<thead>
<tr>
<th></th>
<th>1st April, 2000</th>
<th>31st March, 2001</th>
</tr>
</thead>
<tbody>
<tr>
<td><em>Furniture</em></td>
<td>Rs. 2,000</td>
<td>Rs. 2,000</td>
</tr>
<tr>
<td><em>Stock</em></td>
<td>Rs. 5,000</td>
<td>Rs. 6,000</td>
</tr>
<tr>
<td><em>Sundry Debtors</em></td>
<td>Rs. 6,000</td>
<td>Rs. 4,000</td>
</tr>
<tr>
<td><em>Cash</em></td>
<td>Rs. 10,000</td>
<td>Rs. 20,000</td>
</tr>
<tr>
<td><em>Sundry Creditors</em></td>
<td>Rs. 2,000</td>
<td>Rs. 3,500</td>
</tr>
<tr>
<td><em>Bills Receivable</em></td>
<td>Rs. 1,000</td>
<td>Rs. 500</td>
</tr>
<tr>
<td><em>Loan (Dr)</em></td>
<td>—</td>
<td>Rs. 1,000</td>
</tr>
<tr>
<td><em>Investment</em></td>
<td>—</td>
<td>Rs. 4,000</td>
</tr>
</tbody>
</table>

His drawings during the year were Rs.2,000. Depreciate furniture by 10% and provide a reserve for bad and doubtful debts at 5% on Sundry debtors.

Prepare a statement showing profit for the year.

*(Answer: Profit Rs.13,600 – Mar. 2002)*

15. **Vijayan** maintains books on single entry. He gives you the following information:

<table>
<thead>
<tr>
<th></th>
<th>1st April, 2001</th>
<th>31st March, 2002</th>
</tr>
</thead>
<tbody>
<tr>
<td><em>Cash in hand</em></td>
<td>Rs. 4,000</td>
<td>Rs. 6,000</td>
</tr>
<tr>
<td><em>Cash at Bank</em></td>
<td>Rs. 2,000</td>
<td>Rs. 4,000</td>
</tr>
<tr>
<td><em>Stock in trade</em></td>
<td>Rs. 24,000</td>
<td>Rs. 24,000</td>
</tr>
<tr>
<td><em>Furniture</em></td>
<td>Rs. 6,000</td>
<td>Rs. 10,000</td>
</tr>
<tr>
<td><em>Sundry debtors</em></td>
<td>Rs. 20,000</td>
<td>Rs. 25,000</td>
</tr>
<tr>
<td><em>Sundry creditors</em></td>
<td>Rs. 10,000</td>
<td>Rs. 14,000</td>
</tr>
</tbody>
</table>

He has taken Rs.4,000 from the business to meet his personal expenses. Depreciate furniture by 10% p.a.

Prepare a statement showing profit or loss for the year.

*(June - 2002)*

*(Answer: Profit Rs.12,000)*

**Hint:** Depreciation is calculated for one year on opening balance and for the difference Rs.4,000 for six months.

16. A trader has not kept proper books of accounts. His position as on 31.3.2003 and 31.3.2004 was as follows:

<table>
<thead>
<tr>
<th></th>
<th>31.3.2003</th>
<th>31.3.2004</th>
</tr>
</thead>
<tbody>
<tr>
<td><em>Cash at Bank</em></td>
<td>Rs. 75,000</td>
<td>Rs. 50,000</td>
</tr>
<tr>
<td><em>Cash in hand</em></td>
<td>Rs. 5,000</td>
<td>Rs. 10,000</td>
</tr>
<tr>
<td><em>Stock</em></td>
<td>Rs. 5,00,000</td>
<td>3,25,000</td>
</tr>
<tr>
<td><em>Sundry Debtors</em></td>
<td>Rs. 2,00,000</td>
<td>4,00,000</td>
</tr>
<tr>
<td><em>Furniture</em></td>
<td>Rs. 50,000</td>
<td>Rs. 50,000</td>
</tr>
<tr>
<td><em>Machinery</em></td>
<td>Rs. 4,00,000</td>
<td>4,00,000</td>
</tr>
<tr>
<td><em>Sundry Creditors</em></td>
<td>Rs. 6,00,000</td>
<td>7,00,000</td>
</tr>
</tbody>
</table>

During the year he introduced Rs.1,00,000 as additional capital and withdrew Rs.10,000 per month for domestic purpose. Depreciate furniture and machinery by 10% per year. Ascertain profit or loss for the year ended 31.3.2004.

*(Answer: Loss Rs.1,20,000)*

17. Vani and Veni were partners sharing profits and losses equally. The accounts are maintained on single entry system. On 31.3.2002 their position was as follows:
### Liabilities vs. Assets

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Creditors</td>
<td>1,00,000</td>
<td>Cash at Bank</td>
<td>40,000</td>
</tr>
<tr>
<td>Loan</td>
<td>40,000</td>
<td>Sundry Debtors</td>
<td>1,60,000</td>
</tr>
<tr>
<td>Capital:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Vani</td>
<td>80,000</td>
<td>Plant &amp; Machinery</td>
<td>60,000</td>
</tr>
<tr>
<td>Veni</td>
<td>80,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>3,00,000</td>
<td></td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

The position of the firm on 31.3.2003 was follows:

- Sundry Creditors: Rs. 1,20,000
- Stock: Rs. 80,000
- Plant & Machinery: Rs. 1,00,000
- Sundry Debtors: Rs. 1,50,000
- Cash at Bank: Rs. 60,000

Depreciate plant & Machinery by 10% p.a.

Drawings: Vani Rs. 10,000; Veni Rs. 6,000.

Find out the profit or loss made during the year 2002-03.

*(Answer: Profit Rs. 1,18,000)*

### Conversion method:

18. From the following, find out credit sales:

- Opening Sundry debtors: Rs. 50,000
- Cash received from Sundry debtors: Rs. 80,000
- Discount allowed to Sundry debtors: Rs. 2,000
- Sales return: Rs. 5,000
- Closing Sundry debtors: Rs. 75,000

*(Answer: Rs. 1,12,000)*

19. From the following details, calculate credit sales made during the year 2004.

<table>
<thead>
<tr>
<th>Sundry Debtors (1.4.2004)</th>
<th>Rs. 87,125</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors (31.3.2005)</td>
<td>Rs. 76,500</td>
</tr>
<tr>
<td>Cash received from Sundry debtors</td>
<td>Rs. 2,46,000</td>
</tr>
<tr>
<td>Sales return</td>
<td>Rs. 18,500</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>Rs. 9,000</td>
</tr>
</tbody>
</table>

*(Answer: Rs. 2,62,875)*

20. Calculate Closing Sundry debtors:

<table>
<thead>
<tr>
<th>Opening Sundry debtors</th>
<th>Rs. 2,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit Sales</td>
<td>Rs. 7,00,000</td>
</tr>
<tr>
<td>Cash received from Sundry debtors</td>
<td>Rs. 3,00,000</td>
</tr>
<tr>
<td>Returns inward</td>
<td>Rs. 5,000</td>
</tr>
</tbody>
</table>

*(Answer: Rs. 5,95,000)*

21. From the following details, find out credit purchases:

<table>
<thead>
<tr>
<th>Opening Sundry creditors</th>
<th>Rs. 75,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Closing Sundry creditors</td>
<td>Rs. 90,000</td>
</tr>
<tr>
<td>Cash paid to Sundry creditors</td>
<td>Rs. 22,500</td>
</tr>
<tr>
<td>Discount received</td>
<td>Rs. 15,000</td>
</tr>
<tr>
<td>Purchased returns</td>
<td>Rs. 7,500</td>
</tr>
</tbody>
</table>

*(Answer: Rs. 60,000)*
22. From the following details, calculate the Sundry debtors at the end.

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry Debtors (1.1.2000)</td>
<td>17,425</td>
</tr>
<tr>
<td>Credit sales</td>
<td>60,075</td>
</tr>
<tr>
<td>Cash received from Sundry Debtors</td>
<td>49,200</td>
</tr>
<tr>
<td>Sales Returns</td>
<td>3,700</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>4,300</td>
</tr>
<tr>
<td>Cash sales</td>
<td>12,000</td>
</tr>
</tbody>
</table>

(Answer: Clo. Drs. Rs. 20,300)

23. Calculate the Sundry debtors at the end.

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Sundry Debtors</td>
<td>40,000</td>
</tr>
<tr>
<td>Total sales</td>
<td>1,60,000</td>
</tr>
<tr>
<td>Cash sales</td>
<td>20,000</td>
</tr>
<tr>
<td>Cash received from Sundry Debtors</td>
<td>78,000</td>
</tr>
<tr>
<td>Returns Inward</td>
<td>5,000</td>
</tr>
</tbody>
</table>

(Answer: Total Sales Rs. 6,21,000; Total Purchases Rs. 63,000)

24. From the following, find out Sundry creditors at the end.

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Sundry creditors</td>
<td>19,000</td>
</tr>
<tr>
<td>Cash paid to Sundry creditors</td>
<td>40,000</td>
</tr>
<tr>
<td>Discount received</td>
<td>1,000</td>
</tr>
<tr>
<td>Return outwards</td>
<td>4,800</td>
</tr>
<tr>
<td>Credit purchases</td>
<td>51,200</td>
</tr>
</tbody>
</table>

(Answer: Clo. Crs. Rs. 24,400)

25. Find out total purchases and total sales from the following details by preparing necessary accounts:

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Sundry debtors</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Opening Sundry creditors</td>
<td>65,000</td>
</tr>
<tr>
<td>Cash received from Sundry debtors</td>
<td>5,90,000</td>
</tr>
<tr>
<td>Discount received</td>
<td>3,000</td>
</tr>
<tr>
<td>Cash paid to Sundry creditors</td>
<td>40,000</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>5,000</td>
</tr>
<tr>
<td>Returns outward</td>
<td>10,000</td>
</tr>
<tr>
<td>Returns inward</td>
<td>6,000</td>
</tr>
<tr>
<td>Closing Sundry debtors</td>
<td>70,000</td>
</tr>
<tr>
<td>Closing Sundry creditors</td>
<td>50,000</td>
</tr>
<tr>
<td>Cash sales</td>
<td>50,000</td>
</tr>
<tr>
<td>Cash purchases</td>
<td>25,000</td>
</tr>
</tbody>
</table>

(Answer: Total Sales Rs. 6,21,000; Total Purchases Rs. 63,000)

26. From the following particulars calculate closing balance of Sundry debtors and Sundry creditors.

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry debtors as on 1.4.2002</td>
<td>30,000</td>
</tr>
<tr>
<td>Sundry creditors as on 1.4.2002</td>
<td>41,000</td>
</tr>
<tr>
<td>Credit purchases</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Credit sales</td>
<td>1,70,000</td>
</tr>
<tr>
<td>Discount earned</td>
<td>5,000</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>6,000</td>
</tr>
<tr>
<td>Purchase returns</td>
<td>7,500</td>
</tr>
<tr>
<td>Sales returns</td>
<td>6,500</td>
</tr>
<tr>
<td>Cash received from Sundry debtors</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Cash paid to Sundry creditors</td>
<td>1,40,000</td>
</tr>
</tbody>
</table>

(Answer: Clo. Drs. Rs.37,500; Clo. Crs. Rs.38,500)
27. Mr. Kannan started business with Rs. 2,62,500 on 1.4.2003. He bought furniture for Rs. 42,000. He borrowed Rs. 52,500 from bank. He had withdrawn for personal expenses Rs. 75,600. From the details given below prepare Trading and Profit and Loss account and Balance Sheet on 31.4.2004.

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit sales</td>
<td>7,00,000</td>
</tr>
<tr>
<td>Cash sales</td>
<td>3,50,000</td>
</tr>
<tr>
<td>Credit purchases</td>
<td>7,87,500</td>
</tr>
<tr>
<td>Cash purchases</td>
<td>1,40,000</td>
</tr>
<tr>
<td>Wages</td>
<td>15,750</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>3,500</td>
</tr>
<tr>
<td>Salaries</td>
<td>17,500</td>
</tr>
<tr>
<td>Business expenses</td>
<td>14,000</td>
</tr>
<tr>
<td>Advertisement</td>
<td>17,500</td>
</tr>
<tr>
<td>Closing Sundry debtors</td>
<td>2,62,500</td>
</tr>
<tr>
<td>Closing Sundry creditors</td>
<td>1,75,000</td>
</tr>
<tr>
<td>Closing stock</td>
<td>1,22,500</td>
</tr>
<tr>
<td>Closing cash balance</td>
<td>1,64,150</td>
</tr>
</tbody>
</table>

Depreciation to be provided on furniture @ 10%.

(Answer: Cash receipts from Drs. Rs. 4,34,000; Cash payments to Crs. Rs. 6,12,500; G.P. Rs. 2,29,250; N.P. Rs. 1,72,550; B/s Rs. 5,86,950)

28. Mrs. Pramila maintained her account books on single entry system. From the following information available in her records, prepare Trading, Profit and Loss account for the year ending 31.3.2003 and a Balance Sheet as on that date, depreciating machinery at 10% per annum.

<table>
<thead>
<tr>
<th>Cash Book</th>
</tr>
</thead>
<tbody>
<tr>
<td>Receipts</td>
</tr>
<tr>
<td>To Balance b/d</td>
</tr>
<tr>
<td>To (Cash) Sales</td>
</tr>
<tr>
<td>To Sundry Debtors</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Other Information:</th>
</tr>
</thead>
<tbody>
<tr>
<td>31.3.2002</td>
</tr>
<tr>
<td>Rs.</td>
</tr>
<tr>
<td>Sundry Debtors</td>
</tr>
<tr>
<td>Sundry Creditors</td>
</tr>
<tr>
<td>Stock</td>
</tr>
<tr>
<td>Machinery</td>
</tr>
<tr>
<td>Furniture</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Additional information:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discount allowed</td>
</tr>
<tr>
<td>Discount received</td>
</tr>
<tr>
<td>Credit Sales</td>
</tr>
<tr>
<td>Credit purchases</td>
</tr>
</tbody>
</table>

(Answer: Clo. Drs. Rs. 24,000; Clo. Crs. Rs. 13,600; Op. capital Rs. 1,11,200; G.P. Rs. 1,00,600; N.P. Rs. 81,200; B/s Rs. 1,90,000)

29. From the following details, prepare Trading and Profit & Loss account and Balance Sheet for the year ended 31.3.04.
Furniture  5,000  5,000  
Cash  12,500  20,000  
Sundry Creditors  75,000  87,500  

Other Details:
  Discount received  7,500  
  Discount allowed  5,000  
  Sundry expenses  15,000  
  Cash paid to Sundry creditors  225,000  
  Cash received from Sundry debtors  267,500  
  Drawings  20,000  
  Sales Returns  7,500  
  Purchase Returns  2,500  

Charge depreciation on furniture @ 5%.

(Ans: Op. capital Rs.1,17,500; Cr. sales Rs.3,30,000; 
Cr. Purchases Rs.2,47,500; G.P. Rs. 52,500; 
N.P. Rs.39,750; B/s Rs.2,24,750)

30. From the following information, prepare Trading and Profit and 
Loss account and a Balance Sheet as on 31.3.98.

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>As on 1.4.1997</th>
<th>As on 31.3.1998</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sundry creditors</td>
<td>37,500</td>
<td>43,750</td>
</tr>
<tr>
<td>Furniture</td>
<td>2,500</td>
<td>2,500</td>
</tr>
<tr>
<td>Cash</td>
<td>6,250</td>
<td>10,000</td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>62,500</td>
<td>87,500</td>
</tr>
<tr>
<td>Stock</td>
<td>25,000</td>
<td>12,500</td>
</tr>
</tbody>
</table>

Other Details:
  Drawings  10,000  
  Discount received  3,750  
  Discount allowed  2,500  
  Cash received from Sundry debtors  1,35,000  
  Cash paid to creditors  1,12,500  

Sales returns  3,750  
Purchase returns  1,250  
Sundry expenses paid  8,750  
Charge depreciation on furniture @ 5%

(Ans: Op. Capital Rs.58,750; Cr. sales Rs.1,66,250; 
Cr. Purchase Rs.1,23,750; G.P. Rs.27,500; 
N. P. Rs. 19,875; B/s Rs.1,12,375)

31. The books of Mr. Ravishankar revealed the following information 
on 1.4.2000.

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>83,030</td>
<td>Goodwill</td>
<td>18,540</td>
</tr>
<tr>
<td>Sundry creditors</td>
<td>9,010</td>
<td>Furniture</td>
<td>14,010</td>
</tr>
<tr>
<td>Sundry debtors</td>
<td>46,830</td>
<td>Sundry debtors</td>
<td>46,830</td>
</tr>
<tr>
<td>Cash at bank</td>
<td>12,660</td>
<td>Cash at bank</td>
<td>12,660</td>
</tr>
</tbody>
</table>

| Total          | 92,040 | 92,040 |

Other information:

Cash received from Sundry debtors  2,12,460  
Drawings  81,600  
Salaries paid  18,300  
Rent paid  9,450  
Cash paid to Sundry creditors  90,360  
Sundry expenses paid  3,840  
Closing stock (31.3.2001)  32,000  
Sundry debtors (31.3.2001)  56,700  
Sundry creditors (31.3.2001)  16,000  
Cash at bank (31.3.2001)  21,570  

Prepare Trading account and Profit and Loss account and a 
Balance Sheet as on 31.3.2001.

(Ans: Cr. sales Rs. 2,22,330; Cr. purchases Rs. 97,350; G.P. 
Rs.1,56,980; N.P Rs. 1,25,390; B/s Rs.1,42,820)
CHAPTER - 3
DEPRECIATION ACCOUNTING

Learning Objectives

After studying this Chapter, you will be able to:

- understand the meaning and definition of depreciation.
- recognise the reasons and causes for providing depreciation.
- identify various methods of depreciation.
- determine the profit or loss at the time of sale of asset.
- prepare asset account and depreciation account under straight line and written down value methods.

All assets whose benefit is derived for a long period of time, usually more than one year period are called as Fixed Assets. These assets decrease in value year after year due to wear and tear or lapse of time. This reduction in value of Fixed Assets is called Depreciation.

Generally, the term ‘depreciation’ is used to denote decrease in value, but in accounting, this term is used to denote decrease in the book value of a fixed asset. Depreciation is the permanent and continuous decrease in the book value of a fixed asset due to use, effluxion of time, obsolescence, expiration of legal rights or any other cause.

For instance, a factory owner, owns a machinery worth Rs.1,00,000, may estimate the life of the machinery as five years. This means that the value of the asset is reducing every year. Hence, it is necessary to spread the cost over five years during which the benefit of the asset is derived. Thus depreciation Rs.20,000 (Rs.1,00,000 / 5 years) is to be treated as an expense, which is debited to Profit and Loss account.

3.1 Definition:

In the words of Spicer and Pegler, “Depreciation is the measure of the exhaustion of the effective life of an asset from any cause during a given period”.

Carter defines depreciation as “the gradual and permanent decrease in the value of an asset from any cause”.

According to ICMA (Institute of Cost and Management Accountants - London) Terminology “Depreciation is the diminution in intrinsic value of asset due to use and / lapse of time”.

The above definitions reveal that when fixed assets are used in business to generate income, they lose their production capacity or earning capacity and at a particular point of time they render themselves useless. This reduction in the production capacity or earning capacity is termed as depreciation.

3.2 Need for Providing Depreciation:

The need for providing depreciation in accounting records arises due to any one or more of the following reasons.

1. To ascertain correct profit / loss

For proper matching of cost with revenues, it is necessary to charge depreciation against revenue in each accounting year, to calculate the correct net profit or net loss.
2. To present a true and fair view of the financial position

If the amount of depreciation is not provided on fixed assets in the books of account, the value of fixed assets will be shown at a higher value than it’s real value in the balance sheet. As such it will not reflect the true and fair financial position of the business. Hence, to present a true and fair view of the financial position of the business, it is necessary that depreciation must be deducted from the book value of the assets in the balance sheet.

3. To ascertain the real cost of production

For ascertaining the real cost of production, it is necessary to provide depreciation.

4. To comply with legal requirements

As per Section 205(1) of the Companies Act 1956, it is compulsory for companies to provide depreciation on fixed assets before it declares dividend.

5. To replace assets

Depreciation is provided to replace the assets when it becomes useless.

3.3 Causes of Depreciation

The causes of depreciation may be internal or external. The internal causes arise from operation of any cause natural to or inherent in the asset itself. External causes arise from the operation of forces outside the business. These are being discussed below:

I. Internal Causes

1. Wear and tear: Wear and tear is an important cause of depreciation in case of tangible fixed asset. It is due to use of the asset.

2. Disuse: When a machine is kept continuously idle, it becomes potentially less useful.


4. Depletion: It refers to the physical deterioration by the exhaustion of natural resources eg., mines, quarries, oil wells etc.

II. External Causes

1. Obsolescence: The old asset will become obsolete (useless) due to new inventions, improved techniques and technological advancement.

2. Effluxion of time: When assets are exposed to forces of nature, like weather, wind, rain, etc., the value of such assets may decrease even if they are not put into any use.

3. Time Factor: Lease, copy-right, patents are acquired for a fixed period of time. On the expiry of the fixed period of time, the assets cease to exist.

3.4 Terms used for Depreciation:

1. Amortization: This refers to loss in the value of intangible assets such as goodwill, patents and preliminary expenses.
2. **Depletion**: Decrease in the value of mineral wealth such as coal, oil, iron ore, etc. is termed as **depletion**. The more we extract mineral wealth, the more they are depleted.

3. **Obsolescence**: When an asset becomes useless due to new inventions, improved techniques and technological advances, it is termed as **obsolescence**.

3.5 **Factors Determining the Amount of Depreciation**

1. **Original cost of the asset**: It implies the cost incurred on its acquisition, installation, commissioning and for additions or improvements thereof which are of capital nature.

2. **Estimated life**: It implies the period over which an asset is expected to be used.

3. **Residual value**: It implies the value expected to be realised on its sale on the expiry of its useful life. This is otherwise known as **scrap value** or **turn-in value**.

3.6 **Methods of Calculating Depreciation**

1. Straight line method or fixed instalment method.
2. Written down value method or diminishing balance method.
3. Annuity method.
4. Depreciation Fund method.
5. Insurance Policy method.
6. Revaluation method.

Let us discuss these methods in detail.

3.6.1 **Straight Line Method or Fixed Instalment Method or Original Cost Method**

Under this method, the same amount of depreciation is charged every year throughout the life of the asset. The amount and rate of depreciation is calculated as under.

1) Amount of depreciation

\[
\text{Total cost} - \text{Scrap value} = \frac{\text{Estimated Life}}{\text{Total cost} - \text{Scrap value}}
\]

2) Rate of depreciation

\[
\text{Amount of Depreciation} \times 100 = \frac{\text{Estimated Life}}{\text{Original Cost}}
\]

**Illustration : 1**

A company purchased Machinery for Rs.1,00,000. Its installation costs amounted to Rs.10,000. It’s estimated life is 5 years and the scrap value is Rs.5,000. Calculate the amount and rate of depreciation.

**Solution:**

Total cost = Purchase Price + Installation Charges

= Rs.1,00,000 + Rs.10,000

= Rs.1,10,000

Amount of depreciation = \( \frac{\text{Total cost} - \text{Scrap value}}{\text{Estimated life}} \)

= \( \frac{\text{Rs.1,10,000} - \text{Rs.5,000}}{5} \)

= \( \frac{\text{Rs.1,05,000}}{5} \)

= Rs.21,000

Rate of depreciation = \( \frac{\text{Amount of depreciation}}{\text{Original cost}} \times 100 \)

= \( \frac{\text{Rs.21,000}}{\text{Rs.1,10,000}} \times 100 \)

= 19.09%
Depreciation for the 1st year = 10% on Rs.1,00,000 = Rs.10,000
Depreciation for the 2nd year = 10% on Rs.90,000
(Rs.1,00,000 — Rs.10,000)
= Rs.9,000
Depreciation for the 3rd year = 10% on Rs.81,000
(Rs.90,000 - Rs.9,000)
= Rs.8,100 and so on.

Merits:
1. Uniform effect on the Profit and Loss account of different years:
The total charge (i.e., depreciation plus repairs and renewals) remains almost uniform year after year, since in earlier years the amount of depreciation is more and the amount of repairs and renewals is less, whereas in later years the amount of depreciation is less and the amount of repairs and renewals is more.

Depreciation amount Repairs & renewals amount
Ist Year Ist Year
IInd Year + IInd Year
IIlrd Year, etc. IIlrd Year, etc.

2. Recognised by the Income Tax authorities: This method is recognised by the Income Tax authorities

3. Logical Method: It is a logical method as the depreciation is calculated on the diminished balance every year.

Demerits:
It is very difficult to determine the rate by which the value of asset could be written down to zero.

3.6.3 Annuity Method:
The annuity method considers that the business besides loosing the original cost of the asset in terms of depreciation and also looses
interest on the amount used for buying the asset. This is based on the assumption that the amount invested in the asset would have earned in case the same amount would have been invested in some other form of investment. The annual amount of depreciation is determined with the help of annuity table. This method is used to calculate depreciation amount on lease.

### 3.6.4 Depreciation Fund Method or Sinking Fund Method:

Under this method, funds are made available for the replacement of asset at the end of its useful life. The depreciation remains the same year after year and is charged to Profit and Loss account every year through the creation of depreciation fund. The amount of annual depreciation is invested in good securities bearing interest at a specified rate. The aggregate amount of interest and annual provision is invested every year. When the asset is completely written off or is to be replaced, the securities are sold and the amount so realised by selling securities is used to replace the old asset.

### 3.6.5 Insurance Policy Method:

According to this method, an Insurance policy is taken for the amount of the asset to be replaced. The amount of the policy is such that it is sufficient to replace the asset when it is worn out. A sum equal to the amount of depreciation is paid as premium every year. The amount goes on accumulating at a certain rate of interest and is received on maturity. The amount so received is used for the purchase of new asset, replacing the old one.

### 3.6.6 Revaluation Method:

Under this method, the assets like loose tools are revalued at the end of the accounting period and the same is compared with the value of the asset at the beginning of the year. The difference is considered as depreciation.

### 3.7 Recording Depreciation

Depreciation is directly charged against the asset by debiting Depreciation account and crediting the Asset account. Depreciation account is closed by transferring to Profit and Loss account at the end of the year. The entries will be as under:

1. For the amount of depreciation to be provided at the end of the year:
   
   Depreciation A/c..... Dr. with the amount of depreciation
   To Asset A/c.

2. For transferring the amount of depreciation at the end of the year:

   Profit and Loss A/c..... Dr. with the amount of depreciation transferred
   To Depreciation A/c.

Asset Account will be shown at cost less depreciation i.e., written down value at the end of the year in the Balance sheet.

### Illustration : 2

Raheem & Co. purchased a fixed asset on 1.4.2000 for Rs.2,50,000. Depreciation is to be provided @ 10% annually according to the Straight line method. The books are closed on 31st March every year.

Pass the necessary journal entries, prepare Fixed asset Account and Depreciation Account for the first three years.

### Solution:

\[
\text{Amount of Depreciation} = \frac{2,50,000 \times 10}{100} = \text{Rs. 25,000}
\]
### In the Books of Raheem & Co.

#### Journal Entries

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>Fixed asset A/c</td>
<td>Dr</td>
<td>2,50,000</td>
<td></td>
</tr>
<tr>
<td>Apr 1</td>
<td>To Bank A/c</td>
<td></td>
<td>2,50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Fixed asset purchased)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2001</td>
<td>Depreciation A/c</td>
<td>Dr</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Fixed asset A/c</td>
<td></td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profit &amp; Loss A/c</td>
<td>Dr</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>Depreciation A/c</td>
<td>Dr</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Fixed asset A/c</td>
<td></td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profit &amp; Loss A/c</td>
<td>Dr</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Depreciation A/c</td>
<td>Dr</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Fixed asset A/c</td>
<td></td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profits &amp; Loss A/c</td>
<td>Dr</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Ledger Accounts

##### Fixed Asset Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>To Bank A/c</td>
<td>2,50,000</td>
<td>2001</td>
<td>By Balance c/d</td>
<td>2,25,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>By Depreciation A/c</td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2,50,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2,25,000</td>
</tr>
<tr>
<td>2001</td>
<td>To Balance b/d</td>
<td>2,25,000</td>
<td>2002</td>
<td>By Balance c/d</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>By Depreciation A/c</td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2,25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2,00,000</td>
</tr>
<tr>
<td>2002</td>
<td>To Balance b/d</td>
<td>2,00,000</td>
<td>2003</td>
<td>By Depreciation A/c</td>
<td>25,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>By Balance c/d</td>
<td>1,75,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

##### Depreciation Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>To Fixed Asset A/c</td>
<td>25,000</td>
<td>2001</td>
<td>By Profit &amp; Loss A/c</td>
<td>25,000</td>
</tr>
<tr>
<td>Mar 31</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td></td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>25,000</td>
</tr>
<tr>
<td>2002</td>
<td>To Fixed Asset A/c</td>
<td>25,000</td>
<td>2002</td>
<td>By Profit &amp; Loss A/c</td>
<td>25,000</td>
</tr>
<tr>
<td>Mar 31</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td></td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>25,000</td>
</tr>
<tr>
<td>2003</td>
<td>To Fixed Asset A/c</td>
<td>25,000</td>
<td>2003</td>
<td>By Profit &amp; Loss A/c</td>
<td>25,000</td>
</tr>
<tr>
<td>Mar 31</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td></td>
<td>25,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>25,000</td>
</tr>
</tbody>
</table>
Illustration : 3

A Company purchased Machinery for Rs.50,000 on 1st April 2002. It is depreciated at 10% per annum on Written Down Value method. The accounting year ends on 31st March of every year.

Pass necessary Journal entries, prepare Machinery account and Depreciation account for three years.

Solution:

### Journal Entries

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>Machinery A/c Dr</td>
<td></td>
<td>50,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bank A/c</td>
<td></td>
<td></td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td>(Machinery purchased)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Depreciation A/c Dr</td>
<td></td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profit &amp; Loss A/c Dr</td>
<td></td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td></td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>Depreciation A/c Dr</td>
<td></td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td>4,500</td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profit &amp; Loss A/c Dr</td>
<td></td>
<td>4,500</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td></td>
<td>4,500</td>
</tr>
<tr>
<td></td>
<td>(Depreciation transferred to Profit &amp; Loss account)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>Depreciation A/c Dr</td>
<td></td>
<td>4,050</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td>4,050</td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Machinery Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>To Bank A/c</td>
<td>50,000</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d</td>
<td>45,000</td>
</tr>
<tr>
<td>2003</td>
<td>To Balance b/d</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d</td>
<td>40,500</td>
</tr>
<tr>
<td>2004</td>
<td>To Balance b/d</td>
<td>40,500</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d</td>
<td>36,450</td>
</tr>
<tr>
<td>2005</td>
<td>To Balance b/d</td>
<td>36,450</td>
</tr>
</tbody>
</table>

### Depreciation Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>To Machinery A/c</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>By Profit &amp; Loss A/c</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d</td>
<td>45,000</td>
</tr>
<tr>
<td>2004</td>
<td>To Machinery A/c</td>
<td>4,500</td>
</tr>
<tr>
<td></td>
<td>By Profit &amp; Loss A/c</td>
<td>4,500</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d</td>
<td>4,500</td>
</tr>
<tr>
<td>2005</td>
<td>To Machinery A/c</td>
<td>4,050</td>
</tr>
<tr>
<td></td>
<td>By Profit &amp; Loss A/c</td>
<td>4,050</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d</td>
<td>4,050</td>
</tr>
</tbody>
</table>
3.8 Calculation of Profit or Loss on sale of asset:

Some times, a business may dispose an asset when it is worn out. In that case, it is advisable to find the profit or loss on sale of asset. This is done by comparing the selling price with the book value of the asset.

Book value = Cost Price less Total Depreciation provided till the date of sale

If the book value is less than the selling price, then it is Profit on Sale.

If the book value is more than the selling price, it is Loss on Sale.

Illustration : 4

Ram manufacturing company purchased on 1st April 2002, Machinery for Rs.1,00,000. After having used it for three years it was sold for Rs. 85,000. Depreciation is to be provided every year at the rate of 10% per annum on the fixed instalment method. Books are closed on 31st March every year. Find out the profit or loss on sale of machinery.

<table>
<thead>
<tr>
<th>Calculation of Profit or Loss on Sale of Machinery</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
</tr>
<tr>
<td>Cost Price</td>
</tr>
<tr>
<td>Less: Depreciation for 2002-03</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Less: Depreciation for 2003-04</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Less: Depreciation for 2004-05</td>
</tr>
<tr>
<td>Book value on the date of sale</td>
</tr>
</tbody>
</table>

Selling price is Rs. 85,000.

Book value on the date of sale is Rs. 70,000

As book value is less than selling price the difference is Profit.

\[\text{Profit on sale of machinery} = 85,000 - 70,000\]

\[\therefore \text{Profit on sale of machinery} = \text{Rs. 15,000.}\]

Illustration : 5

Robert & Co. purchased a Machinery on 1st April 2002 for Rs.75,000. After having used it for three years it was sold for Rs.35,000. Depreciation is to be provided every year at the rate of 10% per annum on Diminishing balance method. Accounts are closed on 31st March every year. Find out the profit or loss on sale of machinery.

<table>
<thead>
<tr>
<th>Calculation of Profit or Loss on sale of Machinery</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
</tr>
<tr>
<td>Cost Price</td>
</tr>
<tr>
<td>Less: Depreciation for 2002-03</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Less: Depreciation for 2003-04</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Less: Depreciation for 2004-05</td>
</tr>
<tr>
<td>Book value on the date of sale</td>
</tr>
</tbody>
</table>

Selling price = Rs. 35,000.

Book value on the date of sale = Rs.54,675.

As book value is greater than selling price the difference is Loss.

\[\text{Loss on sale of Machinery} = 54,675 - 35,000\]

\[\therefore \text{Loss on sale of Machinery} = \text{Rs. 19,675.}\]
3.9 Entries for sale of asset:

When the following entries are made:

1. Entry for sale
   Bank A/c…. Dr. With the amount of sale proceeds
   To Asset A/c.

2. Entry for depreciation provided during the year of sale.
   Depreciation A/c…. Dr. With the amount of depreciation provided during the year
   To Asset A/c.

Note: Depreciation is calculated on the date of sale which may be during the year or end of the year.

3. Entry for the transfer of profit on sale of asset.
   Asset A/c…. Dr. With the amount of profit on sale of asset.
   To Profit & Loss A/c.

4. Entry for the transfer of Loss on sale of asset
   Profit & Loss A/c…. Dr. With the amount of Loss on sale of asset.
   To Asset A/c.

a) Format of Fixed Asset Account when it is profit on sales

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
</tr>
<tr>
<td>Date on which Sale is made</td>
<td>To Balance b/d</td>
</tr>
<tr>
<td></td>
<td>To Profit &amp; Loss A/c</td>
</tr>
<tr>
<td></td>
<td>(Profit on Sales)</td>
</tr>
</tbody>
</table>

b) Format of Fixed Asset Account when it is loss on sales

<table>
<thead>
<tr>
<th>Dr.</th>
<th>Cr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Date</td>
<td>Particulars</td>
</tr>
<tr>
<td>Year Begin-ning</td>
<td>To Balance b/d</td>
</tr>
<tr>
<td></td>
<td>By Bank A/c</td>
</tr>
<tr>
<td></td>
<td>(Loss on sale)</td>
</tr>
</tbody>
</table>

Note: The above format relates only to the year in which sales are made.

Illustration: 6

Deepak Manufacturing Company purchased on 1st April 2002, Machinery for Rs.2,90,000 and spent Rs.10,000 on its installation. After having used it for three years it was sold for Rs.2,00,000. Depreciation is to be provided every year at the rate of 15% per annum on the Fixed Instalment method.

Pass the necessary journal entries, prepare machinery account and depreciation account for three years ends on 31st March every year.

Solution:

Calculation of profit or loss on sale of machinery

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost Price (2,90,000 + 10,000)</td>
</tr>
<tr>
<td>Less: Depreciation for 2002-03 @ 15%</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>
Less: Depreciation for 2003-04 @ 15% 45,000

Less: Depreciation for 2004-05 @ 15% 45,000

Book value as on the date of sale 1,65,000

As book value is less than selling price the difference is Profit.

= Rs.2,00,000 - 1,65,000

Profit is Rs.35,000.

---

**Journal Entries in the books of Deepak Manufacturing Company**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>Apr 1</td>
<td></td>
<td>3,00,000</td>
<td>3,00,000</td>
</tr>
<tr>
<td></td>
<td>Machinery A/c To Bank A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Machinery Purchased and installation charges paid)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Mar 31</td>
<td></td>
<td>45,000</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td>Depreciation A/c To Machinery A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation Provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>** Profit &amp; Loss A/c To Depreciation A/c (Depreciation transferred to Profit &amp; Loss account)</td>
<td></td>
<td>45,000</td>
<td>45,000</td>
</tr>
<tr>
<td>2004</td>
<td>Mar 31</td>
<td></td>
<td>45,000</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td>Depreciation A/c To Machinery A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>** Profit &amp; Loss A/c To Depreciation A/c (Depreciation transferred to Profit &amp; Loss account)</td>
<td></td>
<td>45,000</td>
<td>45,000</td>
</tr>
</tbody>
</table>

---

**Ledger Account**

**Dr.**

**Machinery Account**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>Apr 1</td>
<td>3,00,000</td>
<td>2003</td>
<td>By Depreciation A/c</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td>To Bank A/c</td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>2,55,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>3,00,000</td>
</tr>
<tr>
<td></td>
<td>Mar 31</td>
<td></td>
<td>2004</td>
<td>By Depreciation A/c</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td>By Balance c/d</td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>2,10,000</td>
</tr>
<tr>
<td>2003</td>
<td>Apr 1</td>
<td>2,55,000</td>
<td>2005</td>
<td>By Depreciation A/c</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td>To Balance b/d</td>
<td></td>
<td></td>
<td>By Bank A/c</td>
<td>2,00,000</td>
</tr>
<tr>
<td></td>
<td>Mar 31</td>
<td></td>
<td></td>
<td></td>
<td>2,45,000</td>
</tr>
<tr>
<td></td>
<td>To Profit &amp; Loss A/c (Profit on sale)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Depreciation Account

<table>
<thead>
<tr>
<th>Dr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Cr. Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>To Machinery A/c</td>
<td>45,000</td>
<td>2003</td>
<td>By Profit &amp; Loss A/c</td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>45,000</td>
<td></td>
<td></td>
<td>45,000</td>
</tr>
<tr>
<td>2004</td>
<td>To Machinery A/c</td>
<td>45,000</td>
<td>2004</td>
<td></td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>45,000</td>
<td></td>
<td></td>
<td>45,000</td>
</tr>
<tr>
<td>2005</td>
<td>To Machinery A/c</td>
<td>45,000</td>
<td>2005</td>
<td></td>
<td>45,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>45,000</td>
<td></td>
<td></td>
<td>45,000</td>
</tr>
</tbody>
</table>

Illustration : 7

Machinery account showed a balance of Rs.80,000 on 1st April 2001. On 1st October 2003, another machinery was purchased for Rs.48,000. On 30th September 2003, a machinery which has book value Rs.80,000 on 1.4.2001 was sold for the Rs.48,000. Depreciation is to be provided at 10% per annum on Written Down Value Method. The accounting year ends on 31st March.

Prepare Machinery account and Depreciation account for three years.

Solution:

**Calculation of Profit or Loss on Sale of Machinery**

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of Machinery (1.4.2001)</td>
<td>80,000</td>
</tr>
<tr>
<td>Less: Depreciation for 2001-02</td>
<td>8,000</td>
</tr>
<tr>
<td></td>
<td>72,000</td>
</tr>
</tbody>
</table>

Less: Depreciation for 2002-03 | 7,200

Less: Depreciation till the date of sale (30.9.2003) | 3,240

Book value on the date of sale | 61,560

As book value is greater than selling price the difference is loss.

\[ = 61,560 - 48,000 \]

\[ \text{Loss} = \text{Rs.} 13,560 \]

**Ledger Accounts**

**Machinery Account**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>Apr 1 To Balance b/d</td>
<td>80,000</td>
<td>2002</td>
<td>Mar 31 By Depreciation A/c</td>
<td>8,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>72,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>80,000</td>
<td>2003</td>
<td>Mar 31 By Depreciation A/c</td>
<td>7,200</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Balance c/d</td>
<td>64,800</td>
</tr>
<tr>
<td></td>
<td></td>
<td>72,000</td>
<td></td>
<td></td>
<td>72,000</td>
</tr>
<tr>
<td>2003</td>
<td>Apr 1 To Balance b/d</td>
<td>64,800</td>
<td>2003</td>
<td>Mar 31 By Depreciation A/c</td>
<td>3,240</td>
</tr>
<tr>
<td></td>
<td>(for 6 months)</td>
<td></td>
<td></td>
<td>By Bank A/c</td>
<td>48,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>By Profit &amp; Loss A/c</td>
<td>13,560</td>
</tr>
<tr>
<td></td>
<td>(Loss on sale)</td>
<td></td>
<td></td>
<td></td>
<td>2,400</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,12,800</td>
<td>2004</td>
<td>Mar 31 By Depreciation A/c</td>
<td>45,600</td>
</tr>
<tr>
<td></td>
<td>(on new machine</td>
<td></td>
<td></td>
<td>By Bank c/d</td>
<td></td>
</tr>
<tr>
<td></td>
<td>for 6 months)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,12,800</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Apr 1 To Balance b/d</td>
<td>45,600</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## Depreciation Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>Mar 31</td>
<td>To Machinery A/c 8,000</td>
<td>2002</td>
<td>Mar 31</td>
<td>By Profit &amp; Loss A/c 8,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>8,000</td>
<td></td>
<td></td>
<td>8,000</td>
</tr>
<tr>
<td>2003</td>
<td>Mar 31</td>
<td>To Machinery A/c 7,200</td>
<td>2003</td>
<td>Mar 31</td>
<td>By Profit &amp; Loss A/c 7,200</td>
</tr>
<tr>
<td></td>
<td></td>
<td>7,200</td>
<td></td>
<td></td>
<td>7,200</td>
</tr>
<tr>
<td>2003</td>
<td>Sep 30</td>
<td>To Machinery A/c 3,240</td>
<td>2004</td>
<td>Mar 31</td>
<td>By Profit &amp; Loss A/c 5,640</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3,240</td>
<td></td>
<td></td>
<td>5,640</td>
</tr>
<tr>
<td>2004</td>
<td>Mar 31</td>
<td>To Machinery A/c 2,400</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,400</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>5,640</td>
</tr>
</tbody>
</table>

### Illustration: 8

Vimal & Brothers purchased a Machinery for Rs.3,75,000 on 1st July 2002. It is depreciated at 20% per annum on Straight Line Method for three years. Having became obsolete it was sold for Rs.75,000 on 31.3.2005.

Pass the journal entries, prepare Machinery account and Depreciation account. Accounts are closed 31st March every year.

### Solution:

**Calculation of Profit or loss on sale of Machinery**

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of Machinery (1.7.2002)</td>
</tr>
<tr>
<td>Less: Depreciation for 2002-03</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

Less: Depreciation for 2003-04 75,000

Less: Depreciation for 2004-05 75,000

Book value on the date of sale 1,68,750

As book value is greater than selling price the difference is loss.

= Rs. 1,68,750 — 75,000

\[\star \text{ Loss} = \text{Rs. 93,750}\]

### In the Books of Vimal & Brothers

#### Journal Entries

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>July 31</td>
<td></td>
<td>3,75,000</td>
<td>3,75,000</td>
</tr>
<tr>
<td></td>
<td>Machinery A/c Dr</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Bank A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Machinery purchased)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>Mar 31</td>
<td></td>
<td>56,250</td>
<td>56,250</td>
</tr>
<tr>
<td></td>
<td>Depreciation A/c Dr</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>&quot;</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profit &amp; Loss A/c Dr</td>
<td></td>
<td>56,250</td>
<td>56,250</td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation transferred to Profit &amp; Loss account)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>Mar 31</td>
<td></td>
<td>75,000</td>
<td>75,000</td>
</tr>
<tr>
<td></td>
<td>Depreciation A/c Dr</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>&quot;</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Profit &amp; Loss A/c Dr</td>
<td></td>
<td>75,000</td>
<td>75,000</td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation transferred to Profit &amp; Loss account)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
**Ledger Accounts**

**Plant Account**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>To Bank A/c</td>
<td>3,75,000</td>
<td>2003</td>
<td>By Depreciation A/c</td>
<td>56,250</td>
</tr>
<tr>
<td>July 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>By Balance c/d</td>
<td>3,18,750</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3,75,000</td>
<td></td>
<td></td>
<td>3,18,750</td>
</tr>
<tr>
<td>2003</td>
<td>To Balance b/d</td>
<td>3,18,750</td>
<td>2004</td>
<td>By Depreciation A/c</td>
<td>75,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>By Balance c/d</td>
<td>2,43,750</td>
</tr>
<tr>
<td></td>
<td></td>
<td>3,18,750</td>
<td></td>
<td></td>
<td>3,18,750</td>
</tr>
<tr>
<td>2004</td>
<td>To Balance b/d</td>
<td>2,43,750</td>
<td>2005</td>
<td>By Depreciation A/c</td>
<td>75,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>By Bank A/c</td>
<td>75,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2,43,750</td>
<td></td>
<td>By Profit &amp; Loss A/c</td>
<td>93,750</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(Loss on sale)</td>
<td>93,750</td>
</tr>
</tbody>
</table>

**Depreciation Account**

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>To Machinery A/c</td>
<td>56,250</td>
<td>2003</td>
<td>By Profit &amp; Loss A/c</td>
<td>56,250</td>
</tr>
<tr>
<td>Mar 31</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>56,250</td>
</tr>
<tr>
<td>2004</td>
<td>To Machinery A/c</td>
<td>75,000</td>
<td>2004</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>To Machinery A/c</td>
<td>75,000</td>
<td>2005</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mar 31</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Illustration : 9**

On April 1, 2001 Machinery was purchased for Rs.4,00,000. On 1st October 2002, a new machine costing Rs.2,40,000 was purchased. On 30th September 2003, the machinery purchased on 1st April 2001 having became obsolete was sold for Rs.2,40,000. The accounting year ends on 31st March and depreciation is to be provided at 10% p.a. on straight line method.

Pass journal entries and prepare important ledger accounts for three years.

**Solution:**

**Calculation of Profit or Loss on Sale of Machinery**

<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of Machinery (April, 2001)</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Less: Depreciation for 2001-02</td>
<td>40,000</td>
</tr>
<tr>
<td></td>
<td>3,60,000</td>
</tr>
</tbody>
</table>
Less: Depreciation for 2002-03 40,000

3,20,000

Less: Depreciation till the date of sale (30.9.2003) 20,000

Book value on the date of sale 3,00,000

As book value is greater than selling price the difference is loss.

= Rs.3,00,000 - 2,40,000

\* Loss = Rs.60,000.

### Journal Entries

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>L.F.</th>
<th>Debit Rs.</th>
<th>Credit Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>Machinery A/c Dr</td>
<td></td>
<td>4,00,000</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td>To Bank A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Machinery purchased)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>Depreciation A/c Dr</td>
<td></td>
<td>40,000</td>
<td>40,000</td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>&quot; Profit &amp; Loss A/c Dr</td>
<td></td>
<td>40,000</td>
<td>40,000</td>
</tr>
<tr>
<td></td>
<td>To Depreciation A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation transferred to Profit &amp; Loss A/c)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>Machinery A/c Dr</td>
<td></td>
<td>2,40,000</td>
<td>2,40,000</td>
</tr>
<tr>
<td>Oct 1</td>
<td>To Bank A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(New machine purchased)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>Depreciation A/c Dr</td>
<td></td>
<td>52,000</td>
<td>52,000</td>
</tr>
<tr>
<td>Mar 31</td>
<td>To Machinery A/c</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Depreciation provided 40,000+12,000)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Ledger Accounts

#### Machinery Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>To Bank A/c</td>
<td>4,00,000</td>
<td>2002</td>
<td>By Depreciation A/c</td>
<td>40,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>By Balance c/d</td>
<td>3,60,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>4,00,000</td>
</tr>
<tr>
<td>2002</td>
<td>To Balance b/d</td>
<td>3,60,000</td>
<td>2003</td>
<td>By Depreciation A/c</td>
<td>52,000</td>
</tr>
<tr>
<td>Apr 1</td>
<td></td>
<td></td>
<td>Mar 31</td>
<td>(40,000 + 12,000)</td>
<td></td>
</tr>
<tr>
<td>Oct 1</td>
<td>To Bank A/c</td>
<td>2,40,000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Illustration : 10

Aravinth & Brothers purchased a Machinery for Rs.90,000 on 1st April 2001. They spent Rs.10,000 for installation charges. But the machinery was brought into use from 1st October 2001. It further purchased a machinery costing Rs.20,000 on 1st January 2004. Accounts are closed 31st March every year. Depreciation is to be provided at the rate of 10% per annum on Written Down Value Method.

Prepare Machinery account & Depreciation account for three years.

In the Books of Aravinth & Brothers

Ledger Accounts

Machinery Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>Apr 1</td>
<td>100,000</td>
<td>2002</td>
<td>Mar 31</td>
<td>By Depreciation A/c (10% on Rs.1,00,000 for 6 months) 5,000</td>
</tr>
<tr>
<td>2003</td>
<td>Apr 1</td>
<td>To Bank A/c</td>
<td>100,000</td>
<td>2003</td>
<td>By Depreciation A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Apr 1</td>
<td>To Balance b/d</td>
<td>95,000</td>
<td>2004</td>
<td>By Depreciation A/c</td>
</tr>
<tr>
<td>2003</td>
<td>Dec 31</td>
<td>By Profit &amp; Loss A/c</td>
<td>100,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>To Bank A/c</td>
<td>20,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>By Balance c/d</td>
<td>96,500</td>
<td>2004</td>
<td>By Balance c/d</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>By Bank A/c</td>
<td>20,000</td>
<td>2004</td>
<td>By Bank A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Mar 31</td>
<td>By Profit &amp; Loss A/c</td>
<td>44,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
</tbody>
</table>

Illustration : 10

Aravinth & Brothers purchased a Machinery for Rs.90,000 on 1st April 2001. They spent Rs.10,000 for installation charges. But the machinery was brought into use from 1st October 2001. It further purchased a machinery costing Rs.20,000 on 1st January 2004. Accounts are closed 31st March every year. Depreciation is to be provided at the rate of 10% per annum on Written Down Value Method.

Prepare Machinery account & Depreciation account for three years.

In the Books of Aravinth & Brothers

Ledger Accounts

Machinery Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>Apr 1</td>
<td>100,000</td>
<td>2002</td>
<td>Mar 31</td>
<td>By Depreciation A/c (10% on Rs.1,00,000 for 6 months) 5,000</td>
</tr>
<tr>
<td>2003</td>
<td>Apr 1</td>
<td>To Bank A/c</td>
<td>100,000</td>
<td>2003</td>
<td>By Depreciation A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Apr 1</td>
<td>To Balance b/d</td>
<td>95,000</td>
<td>2004</td>
<td>By Depreciation A/c</td>
</tr>
<tr>
<td>2003</td>
<td>Dec 31</td>
<td>By Profit &amp; Loss A/c</td>
<td>100,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>To Bank A/c</td>
<td>20,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>By Balance c/d</td>
<td>96,500</td>
<td>2004</td>
<td>By Balance c/d</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>By Bank A/c</td>
<td>20,000</td>
<td>2004</td>
<td>By Bank A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Mar 31</td>
<td>By Profit &amp; Loss A/c</td>
<td>44,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
</tbody>
</table>

Illustration : 10

Aravinth & Brothers purchased a Machinery for Rs.90,000 on 1st April 2001. They spent Rs.10,000 for installation charges. But the machinery was brought into use from 1st October 2001. It further purchased a machinery costing Rs.20,000 on 1st January 2004. Accounts are closed 31st March every year. Depreciation is to be provided at the rate of 10% per annum on Written Down Value Method.

Prepare Machinery account & Depreciation account for three years.

In the Books of Aravinth & Brothers

Ledger Accounts

Machinery Account

<table>
<thead>
<tr>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
<th>Date</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>Apr 1</td>
<td>100,000</td>
<td>2002</td>
<td>Mar 31</td>
<td>By Depreciation A/c (10% on Rs.1,00,000 for 6 months) 5,000</td>
</tr>
<tr>
<td>2003</td>
<td>Apr 1</td>
<td>To Bank A/c</td>
<td>100,000</td>
<td>2003</td>
<td>By Depreciation A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Apr 1</td>
<td>To Balance b/d</td>
<td>95,000</td>
<td>2004</td>
<td>By Depreciation A/c</td>
</tr>
<tr>
<td>2003</td>
<td>Dec 31</td>
<td>By Profit &amp; Loss A/c</td>
<td>100,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>To Bank A/c</td>
<td>20,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>By Balance C/d</td>
<td>96,500</td>
<td>2004</td>
<td>By Balance C/d</td>
</tr>
<tr>
<td>2004</td>
<td>Jan 1</td>
<td>By Bank A/c</td>
<td>20,000</td>
<td>2004</td>
<td>By Bank A/c</td>
</tr>
<tr>
<td>2004</td>
<td>Mar 31</td>
<td>By Profit &amp; Loss A/c</td>
<td>44,000</td>
<td>2004</td>
<td>By Profit &amp; Loss A/c</td>
</tr>
</tbody>
</table>
**Illustration : 11**

Machinery was purchased on 1.4.2000 for Rs.1,60,000. On 1.10.2000 another machinery was purchased for Rs.80,000. On 30.9.2001 the second machine was sold for Rs.80,000. Assuming that the books are closed on March 31 each year and the depreciation is 10% under diminishing balance method.

Prepare Machinery account for three years.

**Solution:**

**Calculation of Profit or Loss on Sale of Machinery**

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of Machinery (1.10.2000)</td>
</tr>
<tr>
<td>Less:</td>
</tr>
<tr>
<td>Depreciation for 2000-01</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Less:</td>
</tr>
<tr>
<td>Depreciation till the date of sale (30.9.2001)</td>
</tr>
<tr>
<td>Book Value on the date of sale</td>
</tr>
</tbody>
</table>

As book value is less than selling price the difference is profit.
QUESTIONS

I. Objective Type:

a) Fill in the blanks:

1. All assets whose benefit is derived for a __________ period of time are called as Fixed Assets.
2. The estimated sale value of the asset at the end of it’s economic life is called as ________ value.
3. ________ method of depreciation is calculated on the original cost of assets.
4. Under ________ method, depreciation is calculated on the book value of the asset each year.
5. _______ method of depreciation is used in the case of Lease.
6. Under insurance policy method, cash is paid by way of _______ every year.
7. ________ method of depreciation is suitable for special type of asset like Loose tools.


b) Choose the correct answer :

1. Depreciation arises due to
   a) wear and tear of the asset
   b) fall in the market value of asset
   c) fall in the value of money
2. Under straight line method, rate of depreciation is calculated on
   a) Original cost  b) Written down value
   c) Cost less scrap value
3. Under diminishing balance method, depreciation
   a) decreases every year  b) increases every year
   c) constant every year
4. The term depletion is used for
   a) Intangible assets  b) Fixed assets
   c) Natural resources
5. If selling price is more than the book value of the asset on the date of sale, it is
   a) a loss  b) an income  c) a profit
6. If selling price is less than the book value of the asset it denotes
   a) loss  b) capital profit  c) expenditure
7. Profit made on sale of fixed asset is debited to
   a) Profit and Loss account  b) Fixed Asset account
   c) Depreciation account
8. Loss on sale of fixed asset appear on the
   a) credit side of Depreciation account
   b) debit side of fixed asset account
   c) credit side of fixed asset account
9. The amount of depreciation charged on a machinery will be debited to
   a) Machinery account  b) Depreciation account
   c) Cash account
10. Total amount of depreciation provided on the written down value method at the rate of 10% p.a. on Rs.10,000 for first three years will be
    a) Rs. 2,107  b) Rs. 2,710  c) Rs. 2,701

(Answers : 1. (a); 2. (a); 3. (a); 4. (c); 5. (a); 6. (a); 7. (b); 8. (c); 9. (b); 10. (b))
II. Other Questions:

1. Define Depreciation.
2. What is Fixed Asset?
3. What is residual value?
4. What is obsolescence?
5. Write notes on ‘Effluxion of time’.
6. What is straight line method of depreciation?
7. Write notes on written down value method of depreciation.
8. What is Depreciation Fund Method of depreciation?
9. What is Annuity method of depreciation?
10. What is insurance policy method of depreciation?
11. Write notes on revaluation method of depreciation.
12. Write the formula to calculate rate of depreciation under straight line method.
13. What are different methods of providing depreciation?
14. What are the reasons for providing depreciation?
15. What are the causes of depreciation?
16. What are merits and demerits of straight line method of depreciation?
17. What are merits and demerits of written down value method?
18. What are the factors determining the amount of depreciation?

III. Problems:

1. A company purchased Furniture for Rs.28,000. Depreciation is to be provided annually according to the Straight Line Method. The useful life of the furniture is 5 years and the residual value is Rs.2,000.

   You are required to find out the amount of depreciation.
   
   \( \text{Answer: Rs. 5,200} \)

2. From the following particulars, find out the rate of depreciation, under Straight Line Method.

   \[
   \begin{array}{|l|l|}
   \hline
   \text{Cost of Fixed Asset} & \text{Rs. 50,000} \\
   \text{Residual Value} & \text{Rs. 5,000} \\
   \text{Estimated Life} & \text{10 years} \\
   \hline
   \end{array}
   \]

   \( \text{Answer: Rate of Dep. 9%} \)

3. A Plant has the original value of Rs.5,00,000. The scrap value in 10 years time is expected to be Rs.20,000. Determine the rate of depreciation when the management wants to depreciate it by Straight Line Method.

   \( \text{Answer: Rate of Dep. : 9.6%} \)

4. A machine costing Rs.3,00,000 is estimated to have a life of 10 years and estimated scrap value is Rs.20,000 at the end of its life. Calculate the rate of depreciation under the Straight Line Method.

   \( \text{Answer: Rate of dep : 9.3%} \)

5. A machine was purchased for Rs.2,40,000 on 1.1.2000. This is expected to last for five years. Estimated scrap at the end of five years is Rs.40,000. Find out the rate of depreciation under the Straight Line Method.

   \( \text{Answer: Rate of Dep : 16.7%} \)

6. Find out the rate of depreciation under straight line method:

   \[
   \begin{array}{|l|l|}
   \hline
   \text{Cost of the plant} & \text{Rs. 2,30,000} \\
   \text{Installation charges} & \text{Rs. 20,000} \\
   \text{Expected life in years} & \text{10 years} \\
   \text{Scrap value} & \text{Rs. 50,000} \\
   \hline
   \end{array}
   \]

   \( \text{Answer: Rate of Dep: 8%} \)

7. From the following particulars find out the rate of depreciation under the Straight Line Method.

   \[
   \begin{array}{|l|l|}
   \hline
   \text{Cost of assets} & \text{Rs.10,000} \\
   \hline
   \end{array}
   \]
8. A company purchased a Machinery for Rs.12,000. It’s useful life is 10 years and the scrap value is Rs.1,200. Determine the rate of depreciation under the Straight Line Method.

(Answer : 9%)

9. Sudha & Co., purchased a Machinery for Rs.64,000 on 1st April 1996. They spent Rs.28,000 on the repairs and installed the same. Depreciation is written off at 10% p.a. on the Straight Line Method. On 30th June, 1998 the machinery was found to be unsuitable and sold for Rs.52,000. Assume that the accounts are closed on 31st December every year.

Pass the journal entries and prepare Machinery account and Depreciation account for three years.

(Answer: Loss on sale of machinery Rs. 19,300)

10. Sunil & Co. purchased a fixed asset on 1.4.2002 for Rs.5,00,000. Depreciation is to be provided at the rate of 15% annually according to the Straight Line Method. The books are closed on 31st March every year.

Pass the necessary journal entries, prepare Fixed asset account and Depreciation account for the first three years.

(Answer: Balance at the end of third year Rs. 2,75,000)

11. M/s. Shankar & Co. purchased a Machinery on 1.1.2002 for Rs.10,00,000. The firm writes off depreciation at 10% on the original cost every year. The books are closed on 31st March every year.

Pass the necessary journal entries, prepare Machinery account and Depreciation account for the first three years.

(Answer: Balance at the end of third year : Rs. 7,75,000)

12. Ganesh & Co. purchased a Machinery worth Rs.3,00,000 on 1st October 2000. They spent Rs.20,000 on it’s erection. The firm writes off depreciation at the rate of 10% on the original cost every year. The books are closed on 31st March of every year.

Prepare Machinery account and Depreciation account for three years.

(Answer: Balance at the end of the third year: Rs. 2,40,000)

13. On 1st April, 2001, Excel Company Limited purchased a machine for Rs.56,000. On the date of purchase it was estimated that the effective life of the machine will be 10 years and after 10 years it’s scrap value will be Rs.6,000.

Prepare Machine Account and Depreciation Account for three years. Depreciation is charged on Straight Line Method. Accounts are closed on 31st March of every year.

(Answer: Depreciation amount: Rs.5,000. Balance at the end of third year: Rs.41,000).

14. Senthil purchased Machinery for Rs.4,00,000 on 1st April 2000. On 1st April 2001, an additional machinery was purchased for Rs.40,000. Prepare the Asset account for three years. Depreciation is to be provided at 10% p.a. using Straight Line Method. The firm closes its book on 31st March of every year.

(Answer: Balance at the end of third year Rs.3,12,000)

15. A garment company purchased a Plant on 1st April 2001 for Rs.1,00,000. After having used it for three years it was sold for Rs.80,000. Depreciation is to be provided at the rate of 10% per annum on Fixed Instalment Method. Accounts are closed on 31st March every year.
Find out the Profit or Loss on sale of Plant.

(Answer: Profit on sale of plant Rs.10,000)

16. Gayathri Garments purchased a Plant on 1.4.2000 for Rs.2,40,000. After three years the plant was sold for Rs.1,50,000. The firm charges depreciation at the rate of 10% per annum on straight line method. Accounts are closed on 31st March every year.
Pass Journal entries, prepare Plant account and Depreciation account.

(Answer: Loss on sale of Plant Rs.18,000)

17. Kumaran Brothers purchased a Machinery on 1.1.2000 for Rs.5,00,000. On 1.1.2002 the machinery was sold for Rs.4,00,000. The firm charges depreciation at the rate of 15% per annum on Straight Line Method. The books are closed on 31st March every year.
Prepare Machinery account and Depreciation account.

(Answer: Profit on sale of machinery Rs.50,000)

18. Michel & Co. purchased a second hand plant for Rs.4,70,000 on 1st July 2001. They spent Rs.30,000 on the repairs and installed the plant. Depreciation is written off at 10% p.a. on the Straight Line Method. On 30th September 2003, the plant was found to be unsuitable and sold for Rs.3,50,000.
Prepare Plant account and Depreciation account for three years assuming that the accounts are closed on 31st March every year.

(Answer: Loss on sale of plant Rs.37,500)

19. A company purchased a Machinery on 1.4.2001 for Rs.2,40,000. On 1st October 2002, it purchased another machinery for Rs.60,000. On 1st October 2003, it sold off the first machine purchased on 1.4.2001 for Rs.1,68,000. On the same date, it purchased another machinery for Rs.1,50,000.
Accounts are closed every year on 31st March. Depreciation is written off at 10% p.a. on original cost.
Prepare Machinery account and Depreciation account for three years.

(Answer: Loss on sale of machinery Rs.12,000. Balance at the end of third year: Rs.1,93,500)

20. Akbar & Co. purchased a plant for Rs.80,000 on 1.4.2001. It is depreciated at 10% p.a. on reducing balance method for three years. Accounts are closed on 31st March every year.
Pass the Journal entries, prepare Plant account and Depreciation account for three years.

(Answer: Balance at the end of third year Rs.58,320)

21. Bhaskar & Brothers purchased a Machinery on 1.12.2002 for Rs.5,70,000. The firm writes off depreciation at 10% on reducing balance method. The books are closed on 31st March every year.
Pass the necessary journal entries, prepare Machinery account and Depreciation account for the first three years.

(Answer: Balance at the end of third year Rs.4,46,310)

22. On 1st October 2000, a company purchased a plant for Rs.6,00,000. They spent Rs.40,000 on its erection. The firm writes off depreciation at the rate of 20% on Reducing Balance Method. The books are closed on 31st March every year.
Prepare Plant account and Depreciation account for three years.

(Answer: Balance at the end of third year Rs.3,68,640)

23. Archana started business on 1st April 2001 and she purchased a Machinery for Rs.1,40,000. She purchased another machinery on 1st November 2002 costing Rs.30,000. She adopted a policy of charging 15% p.a. depreciation under Diminishing Balance Method.
The accounts are closed every year on 31st March. Prepare Machinery account and Depreciation account for the first three years.

(Answer: Balance at the end of third year Rs.1,09,884)

24. Abdul purchased a Machinery on 1st April 2001 for Rs.2,00,000. After having used it for three years it was sold for Rs.1,60,000. Depreciation is to be provided at the rate of 10% p.a. on Diminishing Balance Method. Accounts are closed on 31st March of every year. Find out the Profit or Loss on sale of machinery.

(Answer: Profit on sale of machinery Rs.14,200)

25. Sivam Printing Press purchased a printing machinery costing Rs.3,00,000 on 1.4.2001. After three years the machinery was sold for Rs.2,80,000. The firm charges depreciation @ 10% per annum on Diminishing Balance Method. Accounts are closed on 31st March every year. Pass journals, prepare Machinery account and Depreciation account.

(Answer: Profit on sale of machinery Rs.61,300)

26. A firm bought a machinery on 1.1.2002 for Rs.5,00,000. On 31.12.2003 the machinery was sold for Rs.3,90,000. The firm charges depreciation at the rate of 10% per annum on Diminishing Balance Method. The books are closed on 31st March every year. Pass journal entries, prepare Machinery account and Depreciation account.

(Answer: Loss on sale of machinery Rs.15,844)

27. Chennai Printing House purchased a Machinery for Rs.4,60,000 on 1st July 2001. It spent Rs.40,000 on the repairs and installed the machinery. Depreciation is written off at 10% p.a. on Diminishing Balance Method. On 31st October 2003, the machinery was found to be unsuitable and sold for Rs.4,10,000. Prepare Machinery account and Depreciation account for three years assuming that the accounts are closed on 31st March every year.

(Answer: Profit on sale of machinery Rs.18,031)

28. A Limited company purchased a Machinery on 1.6.2001 for Rs.2,10,000. On 1st October 2003, it purchased another machinery for Rs.1,00,000. On 1st October 2003, it sold off the first machinery purchased on 1.6.2001 for Rs.1,80,000. Accounts are closed every year on 31st March. Depreciation is written off at 10% per annum on Diminishing Balance Method. Prepare Machinery account and Depreciation account for the first three years.

(Answer: Profit on sale of machinery Rs.15,413 Balance at the end of third year Rs.95,000)

29. A plant is purchased for Rs.90,000. It is depreciated as 10% p.a. on reducing balance for three years. When it becomes obsolete due to new method of production and is scrapped. The scrap produces Rs.66,000 at the end of the third year. Prepare plant and depreciation account for three years.

(Answer: Profit on sale of plant Rs.390)

30. On 1st January 2003, Ramesh & Co., purchased plant worth Rs.1,00,000 was sold away on 31st December 2004 for Rs.50,000. Depreciation was provided at 20% p.a. on the written down value every year. Accounts are prepared on 31st March every year. Show the plant account and depreciation account for three years.

(Answer: Loss on sale of plant Rs. 14,600)

31. Alexander Company Limited purchased a plant for Rs.1,80,000 on 1st January 2003. They spent Rs. 20,000 for installation
expenses. Depreciation is to be provided @ 10% p.a. on the
diminishing value method.

Prepare plant account and depreciation account for three years
ending 31st March every year.

\[(Answer: \text{Balance at the end of third year Rs.1,57,950})\]
Learning Objectives

After studying this Chapter, you will be able to:

- understand the meaning, significance and limitations of financial statement analysis.
- calculate liquidity, solvency, profitability and activity ratios.

Financial statements are final result of accounting work done during the accounting period. Financial statements normally include Trading, Profit and Loss Account and Balance Sheet. The users of accounting information may not be able to get direct reply to certain questions from the above statements. However, by expressing the items in the financial statements, in relation to each other we can get meaningful information.

Analysis of financial statement has been defined as “a process of evaluating the relationship between the component parts of the financial statements to obtain a better understanding of a firm’s position and performance”.

Financial statement analysis is an important part of the overall financial assessment. The different users look at the business concern
from their respective view point and are interested in knowing about its profitability and financial condition. A detailed cause and effect study of the profitability and financial condition is the overall objective of financial statement analysis.

4.1 Significance of Financial Statement Analysis:
1. Judging the earning capacity or profitability of a business concern.
2. Analysing the short term and long term solvency of the business concern.
3. Helps in making comparative studies between various firms.
4. Assists in preparing budgets.

4.1.1 Limitations of Financial Statement Analysis:
Analysis of financial statements helps to ascertain the strength and weakness of the business concern, but at the same time it suffers from the following limitations.
1. It analyses what has happened till date and does not reflect the future.
2. It ignores price level changes.
3. Financial analysis takes into consideration only monetary matters, qualitative aspects are ignored.
4. The conclusions of the analysis is based on the correctness of the financial statements.
5. Analysis is a means to an end and not the end itself.
6. As there is variation in accounting practices followed by different firms a valid comparison of their financial analysis is not possible.

There are different ways by which financial statement analysis can be undertaken and one among them is “Ratio Analysis”. In this chapter we are discussing the Ratio Analysis.

4.2 Ratio Analysis:

Ratio is an expression of one number in relation to another. Ratio analysis is the process of determining and interpreting the numerical relationship between figures of financial statements. A ratio is a mathematical relationship between two items expressed in a quantitative form. An absolute figure does not convey much meaning. Generally, with the help of other related information the significance of the absolute figure could be understood better.

For example Nila earns Rs.50,000 profit in her business while Nivedita earns Rs.40,000 profit. Whose business is more profitable? Instantly we may say that as Nila earns more profit, her business is more profitable. But in order to answer this question we must know what was the sales made by both of them. Suppose Nila has made a sale of Rs.4,00,000 and Nivedita Rs.3,00,000. Now we can calculate the percentage of profit earned on the sales (Profit / Sales x 100) to know whose business is more profitable.

\[
\text{Nila} = \frac{50,000}{4,00,000} \times 100 = 12.5 \%
\]
\[
\text{Nivedita} = \frac{40,000}{3,00,000} \times 100 = 13.33\%
\]

From the above calculations it is clear that the profitability of Nivedita is more than Nila, because, she is getting 13.33% return and Nila is getting only 12.5%.

Thus, the above example explains that absolute figures by themselves may not communicate meaningful information. Hence, business results are understood properly only when the relevant figures are considered together.
4.2.1 Definition:
In the words of Kennedy and Mc Millan “the relationship of an item to another expressed in simple mathematical form is known as a ratio”

Expression of Ratios:
Ratios are expressed in three ways:

1. **Time:** In this type of expression one number is divided by another number and the quotient is taken as number of times. For example, expressing the attendance of 40 students present in a class of 80 students would be:
\[
\frac{40}{80} = 0.5 \text{ times}
\]

2. **Percentage:** It is expressed in Percentage. When the above example is expressed as percentage, it would be as under
\[
\frac{40}{80} \times 100 = 50\%
\]

3. **Pure:** It is expressed as a proportion. In the above example, this would be as under
\[
\frac{40}{80} = \frac{1}{2} = 0.5
\]
This may also be expressed as 0.5:1.

The study of relationships between various items or groups of items in financial statements is known as ‘Financial Ratio Analysis’.

4.2.2 Objectives:
The objectives of using ratios are to test the profitability, financial position (liquidity and solvency) and the operating efficiency of a concern.

4.2.3 Advantages of Ratio Analysis:
Ratio analysis is an important technique in financial analysis. It is a means for judging the financial soundness of the concern. The advantages of accounting ratios are as follows:

1. It is an useful device for analysing the financial statements.
2. It simplifies, summarizes the accounting figures to make it understandable.
3. It helps in financial forecasting.
4. It facilitates interfirm and intrafirm comparisons.

Ratio analysis is useful in finding the strength and weakness of a business concern. After identifying the weakness, the ratios are also helpful in determining the causes of the weakness.

4.2.4 Classification of Ratios:
The classification of ratios on the basis of purpose is as follows:

<table>
<thead>
<tr>
<th>Ratios</th>
<th>Liquidity</th>
<th>Solvency</th>
<th>Profitability</th>
<th>Activity (Turnover)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>3. Absolute Liquid Ratio</td>
<td>3. Operating Profit Ratio</td>
<td>4. Operating Ratio</td>
<td>Turnover Ratio</td>
</tr>
<tr>
<td></td>
<td></td>
<td>4. Operating Ratio</td>
<td></td>
<td>Stock Turnover Ratio</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Debtors Turnover Ratio</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Creditors Turnover Ratio</td>
</tr>
</tbody>
</table>
I. Liquidity Ratios

Liquidity Ratios measure the firms’ ability to pay off current dues i.e., repayable within a year. Liquidity ratios are otherwise called as Short Term Solvency Ratios. The important liquidity ratios are

1. Current Ratio
2. Liquid Ratio
3. Absolute Liquid Ratio

1. Current Ratio :

This ratio is used to assess the firm’s ability to meet its current liabilities. The relationship of current assets to current liabilities is known as current ratio. The ratio is calculated as:

\[
\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}
\]

Current Assets are those assets, which are easily convertible into cash within one year. This includes cash in hand, cash at bank, sundry debtors, bills receivable, short term investment or marketable securities, stock and prepaid expenses.

Current Liabilities are those liabilities which are payable within one year. This includes bank overdraft, sundry creditors, bills payable and outstanding expenses.

Illustration: 1

From the following compute current ratio:

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock</td>
<td>36,500</td>
</tr>
<tr>
<td>Sundry Debtors</td>
<td>63,500</td>
</tr>
<tr>
<td>Cash in hand &amp; bank</td>
<td>10,000</td>
</tr>
<tr>
<td>Bills receivable</td>
<td>9,000</td>
</tr>
<tr>
<td>Short term investments</td>
<td>30,000</td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>1,000</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>20,000</td>
</tr>
<tr>
<td>Sundry creditors</td>
<td>25,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>16,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>14,000</td>
</tr>
</tbody>
</table>

Solution:

\[
\text{Current Assets} = \text{Stock + Sundry debtors + Cash in hand and bank + Bills receivable + Short term investments + Prepaid expenses} \\
= 36,500 + 63,500 + 10,000 + 9,000 + 30,000 + 1,000 \\
= Rs. 1,50,000
\]

\[
\text{Current Liabilities} = \text{Bank overdraft + Sundry creditors + Bills payable + Outstanding expenses} \\
= 20,000 + 25,000 + 16,000 + 14,000 \\
= Rs. 75,000.
\]

\[
\text{Current Ratio} = \frac{1,50,000}{75,000} = 2 : 1
\]

2. Liquid Ratio

This ratio is used to assess the firm’s short term liquidity. The relationship of liquid assets to current liabilities is known as liquid ratio. It is otherwise called as Quick ratio or Acid Test ratio. The ratio is calculated as:

\[
\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}
\]

Liquid assets means current assets less stock and prepaid expenses.
**Illustration : 2**

Taking the figures from the above illustration liquid ratio is calculated as follows:

**Solution:**

\[
\text{Liquid Ratio} = \frac{\text{Liquid Assets}}{\text{Current liabilities}}
\]

\[
\text{Liquid Assets} = \text{Current Assets} - (\text{Stock} + \text{Prepaid expenses})
\]

\[
= 1,50,000 - (36,500 + 1,000)
\]

\[
= 1,50,000 - 37,500
\]

\[
= \text{Rs. 1,12,500}
\]

\[
\text{Liquid Ratio} = \frac{1,12,500}{75,000}
\]

\[
= 1.5 : 1
\]

**3. Absolute Liquid Ratio**

It is a modified form of liquid ratio. The relationship of absolute liquid assets to liquid liabilities is known as **absolute liquid ratio**. This ratio is also called as ‘**Super Quick Ratio**’. The ratio is calculated as:

\[
\text{Absolute Liquid Ratio} = \frac{\text{Absolute Liquid Assets}}{\text{Liquid Liabilities}}
\]

**Absolute liquid assets** means cash, bank and short term investments. **Liquid liabilities** means current liabilities less bank overdraft.

**Illustration : 3**

Taking the figures from Illustration : 1

**Solution:**

\[
\text{Absolute Liquid Ratio} = \frac{\text{Absolute Liquid Assets}}{\text{Liquid Liabilities}}
\]

\[
\text{Absolute Liquid Assets} = \text{Cash} + \text{Bank} + \text{Short term investments}
\]

\[
= 10,000 + 30,000
\]

\[
= \text{Rs. 40,000}
\]

\[
\text{Liquid Liabilities} = \text{Current liabilities} - \text{Bank overdraft}
\]

\[
= 75,000 - 20,000
\]

\[
= \text{Rs. 55,000}
\]

\[
\text{Absolute Liquid Ratio} = \frac{40,000}{55,000}
\]

\[
= 0.73 : 1
\]

**(Note : All liquidity ratios are expressed as a proportion)**

**II. Solvency Ratios**

**Solvency** refers to the firm’s ability to meet its long term indebtedness. Solvency ratio studies the firm’s ability to meet its long term obligations. The following are the important solvency ratios:

1. **Debt-Equity Ratio**
2. **Proprietary Ratio**

**1. Debt Equity Ratio**

This ratio helps to ascertain the soundness of the long term financial position of the concern. It indicates the proportion between total long
term debt and shareholders funds. This also indicates the extent to which the firm depends upon outsiders for its existence. The ratio is calculated as:

\[
\text{Debt-Equity Ratio} = \frac{\text{Total long term Debt}}{\text{Shareholders funds}}
\]

**Total long term debt** includes Debentures, long term loans from banks and financial institutions. **Shareholders funds** includes Equity share capital, Preference share capital, Reserves and surplus.

**Illustration : 4**

Calculate Debt Equity Ratio from the following information.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debentures</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Loan from Banks</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Equity share capital</td>
<td>1,25,000</td>
</tr>
<tr>
<td>Reserves</td>
<td>25,000</td>
</tr>
</tbody>
</table>

**Solution:**

\[
\begin{align*}
\text{Total long term debt} &= \text{Debentures} + \text{Loans from Bank} \\
&= 2,00,000 + 1,00,000 \\
&= \text{Rs. 3,00,000} \\
\text{Shareholders funds} &= \text{Equity Share Capital} + \text{Reserves} \\
&= 1,25,000 + 25,000 \\
&= \text{Rs. 1,50,000} \\
\text{Debt-Equity Ratio} &= \frac{3,00,000}{1,50,000} = 2:1
\end{align*}
\]

2. **Proprietary Ratio**

This ratio shows the relationship between proprietors or shareholders funds and total tangible assets. The ratio is calculated as:

\[
\text{Proprietary Ratio} = \frac{\text{Share holders funds (Proprietors funds)}}{\text{Total tangible assets}}
\]

**Tangible assets** will include all assets except goodwill, preliminary expenses etc.

**Illustration : 5**

From the following calculate Proprietary Ratio

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity share capital</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Preference share capital</td>
<td>75,000</td>
</tr>
<tr>
<td>Reserves &amp; surplus</td>
<td>25,000</td>
</tr>
<tr>
<td>Machinery</td>
<td>30,000</td>
</tr>
<tr>
<td>Goodwill</td>
<td>5,000</td>
</tr>
<tr>
<td>Furniture</td>
<td>10,000</td>
</tr>
<tr>
<td>Bank</td>
<td>20,000</td>
</tr>
<tr>
<td>Cash</td>
<td>25,000</td>
</tr>
<tr>
<td>Stock</td>
<td>15,000</td>
</tr>
</tbody>
</table>

**Solution :**

\[
\begin{align*}
\text{Proprietary Ratio} &= \frac{\text{Shareholders funds}}{\text{Total tangible assets}} \\
&= \frac{1,00,000 + 75,000 + 25,000 + 30,000 + 5,000}{10,000 + 20,000 + 25,000 + 15,000 + 5,000 + 10,000 + 20,000 + 25,000 + 15,000 + 5,000} \\
&= \frac{2,15,000}{150,000} \\
&= \frac{215}{150} \\
&= 1.43
\end{align*}
\]
Shareholders fund = Equity capital + Preference Share Capital + Reserve & Surplus

= 1,00,000 + 75,000 + 25,000

= Rs. 2,00,000

Total tangible assets = Machinery + Furniture + Bank + Cash + Stock

= 30,000 + 10,000 + 20,000 + 25,000 + 15,000

= Rs. 1,00,000

\[
\frac{2,00,000}{1,00,000} = \frac{2}{1}
\]

(Note: All solvency ratios are expressed as a proportion.)

III. Profitability Ratios

Efficiency of a business is measured by profitability. Profitability ratio measures the profit earning capacity of the business concern. The important profitability ratios are discussed below:

1. Gross Profit Ratio
2. Net Profit Ratio
3. Operating Profit Ratio
4. Operating Ratio

1. Gross Profit Ratio

This ratio indicates the efficiency of trading activities. The relationship of Gross profit to Sales is known as gross profit ratio. The ratio is calculated as:

\[
\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100
\]

Gross profit is taken from the Trading Account of a business concern. Otherwise, Gross profit can be calculated by deducting cost of goods sold from sales. Sales means Net sales.

\[
\text{Gross Profit} = \text{Sales} - \text{Cost of goods sold}
\]

Cost of goods sold = Opening Stock + Purchases — Closing Stock

(or)

Sales — Gross Profit

Illustration: 6

From the following particulars ascertain gross profit ratio

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash sales  40,000</td>
<td>Sales return  5,000</td>
</tr>
<tr>
<td>Credit sales  65,000</td>
<td>Gross profit  40,000</td>
</tr>
</tbody>
</table>

Solution:

\[
\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100
\]

\[
\begin{align*}
\text{Sales} & = \text{Total Sales} - \text{Sales Returns} \\
& = 40,000 + 65,000 - 5,000 \\
& = \text{Rs. 1,00,000} \\
\text{Gross Profit} & = 40,000 \\
\text{Gross Profit Ratio} & = \frac{40,000}{1,00,000} \times 100 = 40\% 
\end{align*}
\]
2. Net Profit Ratio:

This ratio determines the overall efficiency of the business. The relationship of Net profit to Sales is known as net profit ratio. The ratio is calculated as:

\[
\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Sales}} \times 100
\]

Net profit is taken from the Profit and Loss account of the business concern or the gross profit of the concern less administration expenses, selling and distribution expenses and financial expenses.

**Illustration : 7**

Calculate net profit ratio from the following:

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Profit</td>
<td>60,000</td>
</tr>
<tr>
<td>Sales</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

**Solution:**

\[
\text{Net Profit Ratio} = \frac{60,000}{3,00,000} \times 100 = 20\%
\]

3. Operating Profit Ratio

This ratio is an indicator of the operational efficiency of the management. It establishes the relationship between Operating profit and Sales. The ratio is calculated as:

\[
\text{Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Sales}} \times 100
\]

Where operating profit is Net profit + Non-operating expenses – Non-operating income.

Where, Non-operating expenses are interest on loan and loss on sale of assets.

Non-operating income are dividend, interest received and profit on sale of asset. (or) Operating profit = Gross profit — Operating expenses.

**Operating expenses** include administration, selling and distribution expenses. Financial expenses like interest on loan are excluded for this purpose.

**Illustration : 8**

Calculate the operating profit ratio from the following:

<table>
<thead>
<tr>
<th>Rs.</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Profit</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Loss on Sale of Furniture</td>
<td>10,000</td>
</tr>
<tr>
<td>Profit on sale of investments</td>
<td>30,000</td>
</tr>
<tr>
<td>Interest paid on loan</td>
<td>30,000</td>
</tr>
<tr>
<td>Interest from investments</td>
<td>20,000</td>
</tr>
<tr>
<td>Sales</td>
<td>5,80,000</td>
</tr>
</tbody>
</table>
Solution:

Operating Profit Ratio = \( \frac{\text{Operating Profit}}{\text{Sales}} \times 100 \)

Operating profit = Net profit + Non-operating expenses — Non-operating income.

Non-operating expenses = Interest on loan + Loss on sale of furniture.

= 30,000 + 10,000
= Rs. 40,000

Non-operating income = Interest received from investments + Profit on sale of investment

= 20,000 + 30,000
= Rs.50,000

Operating profit = 3,00,000 + 40,000 — 50,000
= Rs. 2,90,000

Operating Profit Ratio = \( \frac{2,90,000}{5,80,000} \times 100 \)
= 50%

4. Operating Ratio

This ratio determines the operating efficiency of the business concern. Operating ratio measures the amount of expenditure incurred in production, sales and distribution of output. The relationship between Operating cost to Sales is known as Operating Ratio. The ratio is calculated as:

\[
\text{Operating Ratio} = \frac{\text{Cost of goods sold} + \text{Operating expenses}}{\text{Sales}} \times 100
\]

Illustration : 9

From the following details, calculate the operating ratio.

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Cost of goods sold</th>
<th>6,00,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating expenses</td>
<td>40,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>8,20,000</td>
<td></td>
</tr>
<tr>
<td>Sales returns</td>
<td>20,000</td>
<td></td>
</tr>
</tbody>
</table>

Solution:

\[
\text{Operating Ratio} = \frac{\text{Cost of goods sold} + \text{Operating expenses}}{\text{Sales}} \times 100
\]

\[
= \frac{\frac{6,00,000 + 40,000}{8,20,000 - 20,000}}{\frac{8,20,000 - 20,000}{100}}
\]

= 80%

(Note: All profitability ratios will be expressed in terms of percentage.)
IV. Activity Ratios

Activity ratios indicate the performance of the business. The performance of a business is judged with its sales (turnover) or cost of goods sold. These ratios are thus referred to as turnover ratios. A few important activity ratios are discussed below:

1. Capital turnover ratio
2. Fixed assets turnover ratio
3. Stock turnover ratio
4. Debtors turnover ratio
5. Creditors turnover ratio

1. Capital Turnover Ratio

This shows the number of times the capital has been rotated in the process of carrying on business. Efficient utilisation of capital would lead to higher profitability. The relationship between Sales and Capital employed is known as Capital Turnover Ratio. The ratio is calculated as:

\[
\text{Capital Turnover Ratio} = \frac{\text{Sales}}{\text{Capital Employed}}
\]

Where Sales means Sales less sales returns and Capital employed refers to total long term funds of the business concern i.e., Equity share capital, Preference share capital, Reserves and surplus and Long term borrowed funds.

Illustration : 10

Calculate capital turnover ratio from the following information

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash sales</td>
<td>Rs. 2,00,000</td>
</tr>
<tr>
<td>Credit sales</td>
<td>Rs. 1,75,000</td>
</tr>
</tbody>
</table>

Solution:

\[
\text{Capital Turnover Ratio} = \frac{\text{Sales}}{\text{Capital Employed}}
\]

Net Sales = Cash sales + Credit sales - Sales returns
= 2,00,000 + 1,75,000 - 25,000
= Rs. 3,50,000

Capital Employed = Share capital + Long term loan + Reserves
= 1,00,000 + 50,000 + 25,000
= Rs. 1,75,000

\[
\text{Capital Turnover Ratio} = \frac{3,50,000}{1,75,000} = 2 \text{ times}
\]

2. Fixed Assets Turnover Ratio:

This shows how best the fixed assets are being utilised in the business concern. The relationship between Sales and Fixed assets is known as Fixed assets turnover ratio. The ratio is calculated as:

\[
\text{Fixed assets turnover Ratio} = \frac{\text{Sales}}{\text{Fixed assets}}
\]

Fixed assets means Fixed assets less depreciation.
Illustration: 11

Calculate the fixed asset turnover ratio from the following figures.

\[
\begin{align*}
\text{Rs.} \\
\text{Sales} & \quad 6,15,000 \\
\text{Sales Return} & \quad 15,000 \\
\text{Fixed assets} & \quad 1,50,000
\end{align*}
\]

Solution:

\[
\text{Sales} = \text{Sales} - \text{Sales return} = 6,15,000 - 15,000 = \text{Rs. 6,00,000}
\]

\[
\text{Fixed assets turnover ratio} = \frac{\text{Sales}}{\text{Fixed assets}} = \frac{6,00,000}{1,50,000} = 4 \text{ Times}
\]

3. Stock Turnover Ratio

This ratio is otherwise called as inventory turnover ratio. It indicates whether stock has been efficiently used or not. It establishes a relationship between the cost of goods sold during a particular period and the average amount of stock in the concern. The ratio is calculated as:

\[
\text{Stock turnover ratio} = \frac{\text{Cost of goods sold}}{\text{Average stock}}
\]

Illustration: 12

Calculate stock turnover ratio from the following:

\[
\begin{align*}
\text{Rs.} \\
\text{Cost of goods sold} & \quad 6,75,000 \\
\text{Stock at the beginning of the year} & \quad 1,00,000 \\
\text{Stock at the end of the year} & \quad 1,25,000
\end{align*}
\]

Solution:

\[
\text{Stock turnover ratio} = \frac{\text{Cost of goods sold}}{\text{Average stock}} = \frac{6,75,000}{1,12,500} = \text{Rs. 6} \text{ Times}
\]

Average stock = \frac{\text{Opening stock + Closing stock}}{2}

\[
\begin{align*}
\text{Opening stock + Closing stock} & = 1,00,000 + 1,25,000 = 2,25,000 \\
\text{Average stock} & = \frac{2,25,000}{2} = \text{Rs. 1,12,500}
\end{align*}
\]
Stock turnover ratio $= \frac{6,75,000}{1,12,500} = 6$ Times

**Illustration : 13**

Calculate stock turnover ratio from the following information.

- Rs.
  - Sales 2,00,000
  - Gross profit 50,000
  - Stock 30,000

**Solution:**

Cost of goods sold $= \text{Sales} - \text{Gross profit}$

$= 2,00,000 - 50,000$

$= \text{Rs.} 1,50,000$

Stock turnover ratio $= \frac{1,50,000}{30,000} = 5$ Times

4. **Debtors Turnover Ratio**

This establishes the relationship between credit sales and average accounts receivable. Debtors turnover ratio indicates the efficiency of the business concern towards the collection of amount due from debtors. The ratio is calculated as:

\[
\text{Debtors Turnover Ratio} = \frac{\text{Credit Sales}}{\text{Average Accounts Receivable}}
\]

**Accounts receivable** includes sundry debtors and bills receivable.

- Opening (debtors + bills receivable)
- + Closing (debtors + bills receivable)

Average accounts receivable $= \frac{\text{Opening} + \text{Closing}}{2}$

In case credit sales is not given, total sales can be taken as credit sales.

**Illustration : 14**

Calculate Debtors turnover ratio from the following:

- Rs.
  - Total sales 2,00,000
  - Cash sales 40,000
  - Opening debtors 35,000
  - Closing debtors 45,000

**Solution:**

Credit Sales $= \text{Total sales} - \text{Cash sales}$

$= 2,00,000 - 40,000$

$= \text{Rs.} 1,60,000$

\[
\text{Average Debtors} = \frac{\text{Opening Debtors} + \text{Closing Debtors}}{2}
\]

$= \frac{35,000 + 45,000}{2}$

$= \text{Rs.} 40,000$

\[
\text{Debtors Turnover Ratio} = \frac{1,60,000}{40,000} = 4 \text{ Times}
\]
80,000  

\[ \frac{80,000}{2} = Rs. 40,000 \]

Debtors Turnover Ratio  
\[ \frac{1,60,000}{40,000} = 4 \text{ Times} \]

5. Creditors Turnover Ratio:

This establishes the relationship between credit purchases and average accounts payable. Creditors turnover ratio indicates the period in which the payments are made to creditors. The ratio is calculated as:

\[
\text{Creditors turnover ratio} = \frac{\text{Credit Purchases}}{\text{Average Accounts payable}}
\]

Accounts payable include sundry creditors and bills payable.

Opening (creditors + bills payable)  
+ Closing (creditors + bills payable)

Average accounts payable  
\[ \frac{\text{Opening (creditors + bills payable)} + \text{Closing (creditors + bills payable)}}{2} \]

In case credit purchases is not given total purchases can be taken as credit purchases.

Illustration : 15

Calculate creditors turnover ratio from the following:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit purchases</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Opening creditors</td>
<td>36,000</td>
</tr>
<tr>
<td>Closing creditors</td>
<td>24,000</td>
</tr>
</tbody>
</table>

Solution:

\[
\text{Creditors Turnover Ratio} = \frac{\text{Credit Purchases}}{\text{Average accounts payable}}
\]

\[
\frac{1,50,000}{36,000 + 24,000} = \frac{1,50,000}{60,000} = \frac{60,000}{2} = Rs. 30,000
\]

\[
\frac{60,000}{2} = Rs. 30,000
\]

\[
\frac{1,50,000}{30,000} = 5 \text{ Times}
\]

(Note: All turnover ratios will be expressed in terms of times.)

Other Illustrations:

Illustration : 16

From the following calculate current ratio

Babu Co. Ltd.

Balance Sheet as on 31.3.04

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share capital</td>
<td>21,000</td>
<td>Fixed Assets</td>
<td>17,000</td>
</tr>
<tr>
<td>Reserves</td>
<td>4,000</td>
<td>Stock</td>
<td>6,000</td>
</tr>
<tr>
<td>Bank Overdraft</td>
<td>2,000</td>
<td>Debtors</td>
<td>3,200</td>
</tr>
<tr>
<td>Creditors</td>
<td>6,000</td>
<td>Cash</td>
<td>6,800</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>33,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>33,000</td>
</tr>
</tbody>
</table>
Solution:

Current Ratio = \frac{\text{Current Assets}}{\text{Current Liabilities}}

Current Assets = \text{Stock + Debtors + Cash + Prepaid expenses}
= 6,000 + 3,200 + 6,800 + 2,000
= Rs. 16,000

Current Liabilities = \text{Bank overdraft + Creditors + Prepaid expenses}
= 2,000 + 6,000 + 2,000
= Rs. 8,000

\frac{16,000}{8,000} = 2:1

Illustration : 17

From the following Balance Sheet as on 31.3.2005, calculate current ratio and liquid ratio.

Pavithra Co. Ltd.

Balance Sheet as on 31.3.05

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity share capital</td>
<td>40,000</td>
<td>Machinery</td>
<td>45,000</td>
</tr>
<tr>
<td>Profit &amp; Loss A/c</td>
<td>4,000</td>
<td>Stock</td>
<td>22,000</td>
</tr>
<tr>
<td>Debentures</td>
<td>25,000</td>
<td>Debtors</td>
<td>19,000</td>
</tr>
<tr>
<td>Creditors</td>
<td>24,000</td>
<td>Cash</td>
<td>5,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Prepaid expenses</td>
<td>2,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>93,000</td>
<td><strong>Total</strong></td>
<td>93,000</td>
</tr>
</tbody>
</table>

Solution:

Current Ratio = \frac{\text{Current Assets}}{\text{Current Liabilities}}

Current Assets = \text{Stock + Debtors + Cash + Prepaid expenses}
= 22,000 + 19,000 + 15,000 + 20,000
= Rs. 48,000

Current liabilities = Creditors + Prepaid expenses
= Rs. 24,000 + 2,000
= Rs. 26,000

\frac{48,000}{26,000} = 1:1

Liquid Ratio = \frac{\text{Liquid Assets}}{\text{Current Liabilities}}

Liquid Assets = \text{Current Assets} – \text{(Stock + Prepaid expenses)}
= 48,000 – (22,000 + 2,000)
= 48,000 – 24,000
= Rs. 24,000

\frac{24,000}{24,000} = 1:1
Illustration : 18

From the following, calculate Debt-Equity Ratio.

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity shares</td>
<td>1,00,000</td>
<td>General reserves</td>
<td>75,000</td>
</tr>
<tr>
<td>Debentures</td>
<td>75,000</td>
<td>Sundry creditors</td>
<td>40,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Solution:

Debt-Equity ratio = \[
\frac{\text{Long term Debt}}{\text{Shareholders funds}}
\]

Long term Debt = Debentures = Rs. 75,000

Shareholders funds = Equity shares + General Reserves

= 1,00,000 + 75,000

= Rs. 1,75,000

Debt-Equity ratio = \[
\frac{75,000}{1,75,000}
\] = 0.42 : 1

Illustration : 19

Calculate Gross Profit Ratio from the following:

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchases</td>
<td>2,65,000</td>
</tr>
<tr>
<td>Opening stock</td>
<td>10,000</td>
</tr>
<tr>
<td>Closing stock</td>
<td>20,000</td>
</tr>
<tr>
<td>Sales</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

Solution:

Gross Profit Ratio = \[
\frac{\text{Gross Profit}}{\text{Sales}}\] x 100

Gross Profit = Sales — Cost of Goods Sold

Cost of goods sold = Opening stock + Purchases — Closing stock

= 10,000 + 2,65,000 — 20,000

= Rs. 2,55,000

Gross Profit = 3,00,000 — 2,55,000

= Rs. 45,000

Gross Profit Ratio = \[
\frac{45,000}{3,00,000}\] x 100

= 15%

Illustration : 20

From the following data, calculate the fixed asset turnover ratio.

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash sales</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Credit sales</td>
<td>1,20,000</td>
</tr>
<tr>
<td>Sales Returns</td>
<td>20,000</td>
</tr>
<tr>
<td>Fixed assets</td>
<td>45,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>5,000</td>
</tr>
</tbody>
</table>
Solution:

Fixed Asset Turnover Ratio = \[
\frac{\text{Sales}}{\text{Fixed Assets}}
\]

Sales = Cash sales + Credit sales — Sales Returns
= 1,00,000 + 1,20,000 — 20,000
= 2,20,000 — 20,000
= Rs. 2,00,000

Fixed Assets = Fixed Assets – Depreciation
= 45,000 — 5,000
= Rs. 40,000

Fixed Asset Turnover Ratio = \[
\frac{2,00,000}{40,000}
\] = 5 Times

Illustration : 21

From the following trading account, calculate stock turnover ratio and gross profit ratio.

Trading Account of Mohammed Ali & Co.
for the year ended 31.3.2004

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td>40,000</td>
<td>By Sales</td>
<td>2,00,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>1,20,000</td>
<td>By Closing stock</td>
<td>20,000</td>
</tr>
<tr>
<td>To Carriage</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Gross profit</td>
<td>50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>2,20,000</td>
<td></td>
<td>2,20,000</td>
</tr>
</tbody>
</table>

Solution:

Stock Turnover Ratio = \[
\frac{\text{Cost of Goods Sold}}{\text{Average Stock}}
\]

Cost of Goods Sold = Sales — Gross Profit
= 2,00,000 — 50,000
= Rs. 1,50,000

Average Stock = \[
\frac{\text{Opening Stock} + \text{Closing Stock}}{2}
\]

Opening Stock + Closing Stock
= 40,000 + 20,000
= 60,000
= Rs. 30,000

Stock Turnover Ratio = \[
\frac{1,50,000}{30,000}
\] = 5 Times

Gross Profit = \[
\frac{50,000}{2,00,000}
\] x 100
= 25%

Gross Profit Ratio = \[
\frac{50,000}{2,00,000}
\] x 100
= 25%
Illustration : 22

From the following figures calculate creditors turnover ratio

Rs.
Credit purchases 1,80,000
Bills payable 50,000
Creditors 40,000

Solution:

Credit Purchases
Creditors Turnover Ratio = ————————————
Average Accounts Payable

Average accounts payable = Bills payable + Creditors
= 50,000 + 40,000
= Rs. 90,000

Creditors Turnover Ratio = 1,80,000 = 2 Times
90,000

Illustration : 23

The following is the Trading & Profit and Loss Account of a firm for the year ended 31.3.04.

Trading and Profit and Loss Account of Lilly & Co.
for the year ended 31.3.2003

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening stock</td>
<td>35,000</td>
<td>By Sales</td>
<td>4,00,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>2,25,000</td>
<td>By Closing stock</td>
<td>50,000</td>
</tr>
<tr>
<td>To Wages</td>
<td>10,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Gross profit</td>
<td>1,80,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>4,50,000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Calculate profitability ratios.

Solution:

1. Gross Profit Ratio = Gross Profit x 100
   Sales
   = 1,80,000 x 100
   = 45%

2. Net Profit Ratio = Net Profit x 100
   Sales
   = 1,55,000 x 100
   = 38.75%

3. Operating Profit Ratio = Operating profit x 100
   Sales
   = 1,82,000 x 100
   = 38.75%
Operating Profit = Net Profit + Non-operating expenses – Non-operating income
= Net Profit + Interest + Loss on sale of machinery – Dividend
= 1,55,000 + 2,000 + 5,000 – 2,000
= Rs. 1,60,000

Operating Profit Ratio = \(\frac{1,60,000}{4,00,000}\) x 100
= 40%

4. Operating Ratio

Cost of goods sold = Sales – Gross Profit
= 4,00,000 – 1,80,000
= Rs. 2,20,000

Operating Expenses = Administration + Selling Expenses
= 10,000 + 10,000
= Rs. 20,000

Operating Ratio = \(\frac{2,20,000 + 20,000}{4,00,000}\) x 100
= 60%*

* Note: Operating ratio = 100% — Operating profit ratio
= 100% — 40%
= 60%

Illustration : 24

From the given data, calculate
1. Gross Profit Ratio
2. Net Profit Ratio and
3. Current Ratio

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Net Profit</td>
<td>30,000</td>
</tr>
<tr>
<td>Current liabilities</td>
<td>30,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of goods sold</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Current Assets</td>
<td>60,000</td>
</tr>
</tbody>
</table>

Solution:

i) Gross profit ratio = \(\frac{3,00,000}{2,00,000}\) x 100
= 60%

Gross Profit = Sales – Cost of Goods sold
= 3,00,000 – 2,00,000
= Rs. 1,00,000

Gross Profit Ratio = \(\frac{1,00,000}{3,00,000}\) x 100 = 33.33%

ii) Net Profit Ratio = \(\frac{30,000}{Sales}\) x 100

\[
\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100
\]
\[
\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Sales}} \times 100
\]
\[
\text{Stock Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Average Stock}}
\]

**Illustration : 25**

From the following details calculate
1. Gross Profit Ratio
2. Net Profit Ratio
3. Stock Turnover Ratio
4. Debtors Turnover Ratio

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Cost of Goods Sold</td>
<td>1,20,000</td>
</tr>
<tr>
<td>Opening Stock</td>
<td>29,000</td>
</tr>
<tr>
<td>Closing Stock</td>
<td>31,000</td>
</tr>
<tr>
<td>Debtors</td>
<td>15,000</td>
</tr>
<tr>
<td>Administration Expenses</td>
<td>15,000</td>
</tr>
</tbody>
</table>

\[
\text{Gross Profit} = \text{Sales} - \text{Cost of goods sold}
\]
\[
\text{Net Profit} = \text{Gross Profit} - \text{Administration Expenses}
\]
\[
\text{Stock Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Average Stock}}
\]

**Solution:**

1) Gross Profit Ratio
\[
\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100
\]
\[
\text{Gross Profit} = \text{Sales} - \text{Cost of goods sold}
\]
\[
\text{Net Profit} = \text{Gross Profit} - \text{Administration Expenses}
\]
\[
\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Sales}} \times 100
\]
\[
\text{Cost of Goods Sold} = \frac{\text{Net Profit} + \text{Administration Expenses}}{\text{Stock Turnover Ratio}}
\]

2) Net Profit Ratio
\[
\text{Net Profit Ratio} = \frac{\text{Net Profit}}{\text{Sales}} \times 100
\]
\[
\text{Net Profit} = \text{Gross Profit} - \text{Administration Expenses}
\]
\[
\text{Stock Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Average Stock}}
\]

3) Stock Turnover Ratio
\[
\text{Stock Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Average Stock}}
\]
Average Stock = \frac{\text{Opening Stock + Closing Stock}}{2} \[
\frac{29,000 + 31,000}{2} = 30,000 \]

Credit Sales = \frac{1,20,000}{30,000} = 4 \text{ Times}

Illustration : 26

From the Balance Sheet given below, calculate Current Ratio & Proprietary Ratio.

Balance Sheet of Ram & Co. Ltd. as on 31.3.2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>60,000</td>
<td>Fixed Assets</td>
<td>1,65,000</td>
</tr>
<tr>
<td>Reserves</td>
<td>45,000</td>
<td>Current Assets</td>
<td>75,000</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>70,000</td>
<td>Investments (long term)</td>
<td>35,000</td>
</tr>
<tr>
<td>Current liabilities</td>
<td>1,20,000</td>
<td>Preliminary expenses</td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Goodwill</td>
<td>10,000</td>
</tr>
<tr>
<td></td>
<td>2,95,000</td>
<td></td>
<td>2,95,000</td>
</tr>
</tbody>
</table>

Solution:

1. Current ratio = \frac{\text{Current Assets}}{\text{Current liabilities}}

   \[
   \frac{75,000}{1,20,000} = 0.625 : 1
   \]

2) Proprietary Ratio = \frac{\text{Shareholders funds}}{\text{Tangible Assets}}

   \[
   \frac{60,000 + 45,000}{1,65,000 + 75,000 + 35,000} = 0.382 : 1
   \]

Illustration : 27

Surya Ltd. provides the following information for the year ending 31.3.05. Calculate Gross Profit ratio, Net profit ratio, Operating profit ratio and Operating ratio.
<table>
<thead>
<tr>
<th>Description</th>
<th>Rs.</th>
<th>Description</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>2,00,000</td>
<td>Gross Profit</td>
<td>80,000</td>
</tr>
<tr>
<td>Office Expenses</td>
<td>6,000</td>
<td>Selling Expenses</td>
<td>4,000</td>
</tr>
<tr>
<td>Finance expenses</td>
<td>3,000</td>
<td>Loss on sale of plant</td>
<td>400</td>
</tr>
<tr>
<td>Interest received</td>
<td>500</td>
<td>Net Profit</td>
<td>67,100</td>
</tr>
</tbody>
</table>

**Solution:**

1) Gross Profit ratio
   \[ \text{Gross Profit ratio} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100 \]
   \[ = \frac{80,000}{2,00,000} \times 100 = 40\% \]

2) Net Profit ratio
   \[ \text{Net Profit ratio} = \frac{\text{Net Profit}}{\text{Sales}} \times 100 \]
   \[ = \frac{67,100}{2,00,000} \times 100 = 33.55\% \]

3) Operating Profit Ratio
   \[ \text{Operating Profit Ratio} = \frac{\text{Operating Profit}}{\text{Sales}} \]
   \[ \text{Operating profit} = \text{Net Profit} + \text{Non-operating expenses} - \text{Non-operating Income} \]
   \[ = \text{Net Profit} + \text{Loss on sale of plant} + \text{Financial expenses} - \text{Interest received} \]
   \[ = 67,100 + 400 + 3,000 - 500 = \text{Rs. 70,000} \]

4) Operating Ratio
   \[ \text{Operating Ratio} = \frac{\text{Cost of goods sold + Operating expenses}}{\text{Sales}} \]
   \[ \text{Cost of goods sold} = \text{Sales} - \text{Gross Profit} \]
   \[ = 2,00,000 - 80,000 = \text{Rs. 1,20,000} \]
   \[ \text{Operating expenses} = \text{Office expenses} + \text{Selling expenses} \]
   \[ = 6,000 + 4,000 = \text{Rs. 10,000} \]
   \[ = \frac{10,000 + 1,20,000}{2,00,000} \times 100 = 65\% \]
Illustration : 28

From the following Profit and Loss Account of a company, ascertain the following ratios.

1. Gross Profit Ratio
2. Net Profit Ratio
3. Operating Ratio
4. Operating Profit Ratio
5. Stock Turnover Ratio

Trading and Profit & Loss Account for the year ending 31.3.2005

<table>
<thead>
<tr>
<th>Dr Particulars</th>
<th>Rs.</th>
<th>Cr Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>10,000</td>
<td>By Sales</td>
<td>56,000</td>
</tr>
<tr>
<td>To Purchase</td>
<td>44,000</td>
<td>By Closing stock</td>
<td>10,000</td>
</tr>
<tr>
<td>To Gross Profit</td>
<td>20,100</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>66,000</td>
<td></td>
<td>66,000</td>
</tr>
<tr>
<td>To Administration expenses</td>
<td>2,000</td>
<td>By Gross Profit</td>
<td>20,100</td>
</tr>
<tr>
<td>To Selling expenses</td>
<td>8,900</td>
<td>By Dividend</td>
<td>1,000</td>
</tr>
<tr>
<td>To Interest</td>
<td>3,000</td>
<td>By Profit on sale</td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>8,000</td>
<td>of investments</td>
<td>800</td>
</tr>
<tr>
<td></td>
<td>21,900</td>
<td></td>
<td>21,900</td>
</tr>
</tbody>
</table>

Solution:

1) Gross Profit ratio
   \[
   \text{Gross Profit ratio} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100
   \]
   \[
   = \frac{20,100}{56,000} \times 100 = 35.89\%
   \]

2) Net Profit ratio
   \[
   \text{Net Profit ratio} = \frac{\text{Net Profit}}{\text{Sales}} \times 100
   \]
   \[
   = \frac{8,000}{56,000} \times 100 = 14.29\%
   \]

3) Operating Profit Ratio
   \[
   \text{Operating Profit ratio} = \frac{\text{Operating Profit}}{\text{Sales}} \times 100
   \]
   \[
   = \frac{9,200}{56,000} \times 100 = 16.43\%
   \]

4) Operating Ratio
   \[
   \text{Operating Ratio} = \frac{\text{Cost of goods sold} + \text{Operating Expenses}}{\text{Sales}} \times 100
   \]
Gross Profit = Sales – Cost of goods sold
= 56,000 – 20,100
= Rs. 35,900

Operating expenses = Administration Expenses + Selling Expenses
= 2,000 + 8,900
= Rs. 10,900

Operating Ratio = \( \frac{35,900 + 10,900}{56,000} \times 100 \) = 83.57%

Cost of Goods Sold

5. Stock Turnover Ratio = \( \frac{35,900}{Average \ Stock} \) = 3.59 times

Average Stock = \( \frac{10,000 + 10,000}{2} \) = Rs. 10,000

Illustration : 29
Calculate Debtors turnover ratio from the following.

Total Sales 10,000 Cash Sales 2,000
Opening Debtors 1,000 Closing Debtors 1,500
Opening Bills Receivable 750 Closing Bills Receivable 1,250

Solution:

Credit Sales = Total Sales – Cash Sales
= 10,000 – 2,000
= Rs. 8,000

Opening (Debtors + Bills receivables) + Closing (Debtors + Bills receivables)

Average Accounts Receivable = \( \frac{2}{(1,000 + 750) + (1,500 + 1,250)} \)
= \( \frac{2}{1,750 + 2,750} \)
= \( \frac{2}{4,500} \) = Rs. 2,250

Debtors Turnover Ratio = \( \frac{8,000}{2,250} \) = 3.56 times.
<table>
<thead>
<tr>
<th>S.No</th>
<th>Description of the Ratio</th>
<th>Formula</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Current ratio</td>
<td>Current assets (\frac{\text{Current assets}}{\text{Current liabilities}})</td>
<td>Current assets include cash in hand, cash at bank, sundry debtors, bills receivable, marketable securities, stock and prepaid expenses. Current liabilities include Bank overdraft, sundry creditors, bills payable and outstanding expenses.</td>
</tr>
<tr>
<td>2.</td>
<td>Liquid Ratio</td>
<td>Liquid assets (\frac{\text{Liquid assets}}{\text{Current liabilities}})</td>
<td>Liquid assets mean current assets less stock and prepaid expenses</td>
</tr>
<tr>
<td>3.</td>
<td>Absolute Liquid Ratio</td>
<td>Absolute Liquid assets (\frac{\text{Absolute Liquid assets}}{\text{Liquid liabilities}})</td>
<td>Absolute Liquid assets mean cash, bank and short term investment. Liquid liabilities mean current liabilities less bank overdraft.</td>
</tr>
<tr>
<td>4.</td>
<td>Debt Equity Ratio</td>
<td>Long Term Debts Shareholders funds (\frac{\text{Long Term Debts}}{\text{Shareholders funds}})</td>
<td>Long term debts include Debentures, long term loans from banks and financial institutions. Shareholders funds include Equity share capital, Preference share capital, Reserves and surplus.</td>
</tr>
<tr>
<td>5.</td>
<td>Proprietary Ratio</td>
<td>Shareholders funds Total tangible assets</td>
<td>Tangible assets include all assets except goodwill, preliminary expenses etc.</td>
</tr>
<tr>
<td>6.</td>
<td>Gross Profit Ratio</td>
<td>Gross profit (\frac{\text{Gross profit}}{\text{Sales}}) \times 100</td>
<td>Gross profit = Sales – Cost of goods sold. Cost of goods sold = Opening stock + Purchases – Closing stock</td>
</tr>
<tr>
<td>7.</td>
<td>Net Profit Ratio</td>
<td>Net profit (\frac{\text{Net profit}}{\text{Sales}}) \times 100</td>
<td>Net profit = Gross profit – (Administration, Selling and distribution and financial expenses expenses)</td>
</tr>
<tr>
<td>8.</td>
<td>Operating Profit Ratio</td>
<td>Operating profit (\frac{\text{Operating profit}}{\text{Sales}}) \times 100</td>
<td>Operating profit = Net profit + Non-operating expenses – Non-operating income [OR] Gross profit – Operating expenses</td>
</tr>
<tr>
<td>9.</td>
<td>Operating Ratio</td>
<td>Cost of goods sold + Operating expenses (\frac{\text{Cost of goods sold + Operating expenses}}{\text{Sales}}) \times 100</td>
<td></td>
</tr>
<tr>
<td>10.</td>
<td>Capital Turnover Ratio</td>
<td>Sales Capital Employed</td>
<td>Capital employed = Equity share capital + Preference share capital + reserves and surplus + long term borrowed funds</td>
</tr>
<tr>
<td>11.</td>
<td>Fixed Assets Turnover Ratio</td>
<td>Sales Fixed Assets</td>
<td>Fixed assets = Fixed assets – Depreciation</td>
</tr>
<tr>
<td>12.</td>
<td>Stock Turnover Ratio</td>
<td>Cost of goods sold Average stock</td>
<td>Average stock = opening stock + closing stock divided by two.</td>
</tr>
<tr>
<td>13.</td>
<td>Debtors Turnover Ratio</td>
<td>Credit Sales Average accounts receivable (\frac{\text{Credit Sales}}{\text{Average accounts receivable (Debtors + Bills receivable)}})</td>
<td>Average accounts receivable is calculated by dividing the opening balance of debtors and bills receivable and closing balance of debtors and bills receivable by two.</td>
</tr>
</tbody>
</table>
I. Objective Type:

a) Fill in the blanks:

1. _______ is a mathematical relationship between two items expressed in quantitative form.

2. Ratio helps in _______ forecasting.

3. _______ Ratio measures the firm’s ability to pay off its current dues.

4. _______ are those assets which are easily convertible into cash.

5. Bank overdraft is an example of _______ liability.

6. Liquid ratio is used to assess the firm’s _______ liquidity.

7. Liquid assets means current assets less _______ and _______.

8. _______ ratio is modified form of liquid ratio.

9. Liquid liabilities means current liabilities less _______.

10. Proprietary ratio shows the relationship between _______ and total tangible assets.

b) Choose the correct answer:

1. All solvency ratios are expressed in terms of a) Proportion b) Times c) Percentage

2. All activity ratios are expressed in terms of a) Proportion b) Times c) Percentage

3. All profitability ratios are expressed in terms of a) Proportion b) Times c) Percentage


5. Shareholders funds includes a) Equity share capital, Preference share capital, Reserves & Surplus b) Loans from banks and financial institutions c) Equity share capital, Preference share capital, Reserves & Surplus and Loans from banks and financial institutions

11. Gross profit can be ascertained by deducting cost of goods sold from _______.

12. Stock turnover ratio is otherwise called as _______.

13. 100% – Operating profit ratio is equal to _______ ratio.

14. When total sales is Rs.2,00,000, cash sales is Rs.65,000, then credit sales will be Rs._______.

15. Liquid ratio is otherwise known as _______.

6. Which of the following option is correct
   a) Tangible Assets = Land + Building + Furniture
   b) Tangible Assets = Land + Building + Goodwill
   c) Tangible Assets = Land + Furniture + Goodwill + Copy right

7. Gross profit ratio establishes the relationship between
   a) Gross profit & Total sales
   b) Gross profit & Credit sales
   c) Gross profit & Cash sales

8. Opening stock is equal to Rs.10,000, Purchase Rs.2,00,000 and closing stock is Rs.5,000. Cost of goods sold is equal to
   a) Rs. 2,15,000   b) Rs. 2,10,000   c) Rs. 2,05,000

9. Operating ratio is equal to
   a) 100 – Operating profit ratio
   b) 100 + Operating profit ratio
   c) Operating profit ratio

10. Total sales is Rs.3,40,000 and the gross profit made is Rs.1,40,000. The cost of goods sold will be ________
    a) Rs.2,00,000    b) Rs. 4,80,000    c) Rs. 3,40,000

11. Total sales of a business concern is Rs.8,75,000. If cash sales is Rs.3,75,000, then credit sales will be
    a) Rs.12,50,000   b) Rs.5,00,000   c) 12,00,000

12. Cost of goods sold is Rs.4,00,000 and average stock is Rs.80,000. Stock turnover ratio will be
    a) 5 times   b) 4 times   c) 7 times

13. Current assets of a business concern is Rs.60,000 and current liabilities are Rs.30,000. Current ratio will be
    a) 1 : 2   b) 1 : 1   c) 2 : 1

14. Equity share capital is Rs.2,00,000, Reserves & surplus is Rs.30,000. Debenture Rs.40,000 and the shareholders funds will be
    a) Rs.2,00,000   b) Rs. 2,30,000   c) Rs. 1,90,000

(Answers: 1. (a); 2. (b); 3. (c); 4. (b); 5. (a); 6. (a); 7. (a); 8. (c); 9. (a); 10. (a); 11. (b); 12. (a); 13. (c); 14. (b))

II. Other Questions:
1. What are the significance of financial statement analysis?
2. What are the limitations of financial statement analysis?
3. Explain current ratio.
4. What is the need for calculating Debt – Equity ratio?
5. What are profitability ratios?
6. What are operating expenses?
7. Write notes on operating ratio.
8. What are activity ratios?
9. What is debtors turnover ratio?
10. What is accounts receivable?
11. What is account payable?
12. Explain solvency ratios.
13. Write notes on capital turnover ratio.
14. What are current assets?
15. Write notes on net profit ratio.

III. Problems:
1. From the following, calculate the current ratio.
   
<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in hand</td>
</tr>
<tr>
<td>Sundry debtors</td>
</tr>
<tr>
<td>Stock</td>
</tr>
</tbody>
</table>
2. Calculate liquid ratio

<table>
<thead>
<tr>
<th>Current assets</th>
<th>Rs.</th>
<th>Stock</th>
<th>Rs.</th>
<th>Prepaid expenses</th>
<th>Rs.</th>
<th>Current liabilities</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>20,000</td>
<td></td>
<td>3,000</td>
<td></td>
<td>1,000</td>
<td></td>
<td>8,000</td>
<td></td>
</tr>
</tbody>
</table>

(Answer: 2:1)

3. From the following information, calculate current ratio and liquid ratio

<table>
<thead>
<tr>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>5,000</td>
</tr>
<tr>
<td>Bills receivable</td>
<td>5,000</td>
</tr>
<tr>
<td>Stock</td>
<td>52,000</td>
</tr>
<tr>
<td>Creditors</td>
<td>36,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>8,000</td>
</tr>
</tbody>
</table>

(Answer: Current ratio 2:1; Liquid ratio 1:1)

4. From the following, calculate Current ratio & Liquid ratio

**Balance Sheet of Gopi Co.Ltd., as on 31.3.05**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>6,300</td>
<td>Fixed Assets</td>
<td>5,100</td>
</tr>
<tr>
<td>Reserves</td>
<td>1,200</td>
<td>Stock</td>
<td>2,100</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>600</td>
<td>Debtors</td>
<td>960</td>
</tr>
<tr>
<td>Creditors</td>
<td>1,800</td>
<td>Cash</td>
<td>1,740</td>
</tr>
<tr>
<td></td>
<td>9,900</td>
<td></td>
<td>9,900</td>
</tr>
</tbody>
</table>

(Answer: Current ratio 2:1; Liquid ratio 1.13:1)

5. From the following, you are required to calculate liquidity ratios.

<table>
<thead>
<tr>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debtors</td>
<td>5,000</td>
</tr>
<tr>
<td>Creditors</td>
<td>4,000</td>
</tr>
<tr>
<td>Cash in hand</td>
<td>4,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>3,000</td>
</tr>
<tr>
<td>Cash at Bank</td>
<td>6,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>250</td>
</tr>
<tr>
<td>Short Term Investments</td>
<td>2,000</td>
</tr>
<tr>
<td>Bills receivable</td>
<td>3,000</td>
</tr>
<tr>
<td>Prepaid expenses</td>
<td>1,000</td>
</tr>
<tr>
<td>Closing stock</td>
<td>8,000</td>
</tr>
</tbody>
</table>

(Answer: Current Ratio 4:1; Liquid Ratio 2.76:1; Absolute Ratio 1.66:1)

6. From the following information, calculate current ratio, liquid ratio & Absolute liquid ratio.

| Cash | 1,800 | Creditors | 5,000 |
| Debtors | 14,200 | Outstanding expenses | 1,500 |
| Stock | 18,000 | Bank overdraft | 7,500 |
| Bills Payable | 2,700 |

(Answer: Current ratio 2.04:1; Liquid ratio 0.96:1; Absolute liquid ratio 0.196:1)

7. Calculate Debt - Equity ratio

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity share capital</td>
</tr>
<tr>
<td>General Reserve</td>
</tr>
<tr>
<td>Long term loan</td>
</tr>
<tr>
<td>Debentures</td>
</tr>
</tbody>
</table>

(Answer: 0.43:1)

8. From the following, Calculate Gross Profit Ratio

<table>
<thead>
<tr>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Profit</td>
</tr>
<tr>
<td>Sales</td>
</tr>
<tr>
<td>Sales Return</td>
</tr>
</tbody>
</table>

(Answer: 10%)
9. Calculate Gross Profit ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>6,50,000</td>
</tr>
<tr>
<td>Cost of Goods sold</td>
<td>4,80,000</td>
</tr>
<tr>
<td>Sales Return</td>
<td>50,000</td>
</tr>
</tbody>
</table>

(Answer: 20%)

10. Calculate Capital turnover ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>10,20,000</td>
</tr>
<tr>
<td>Sales Returns</td>
<td>20,000</td>
</tr>
<tr>
<td>Equity Share Capital</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Loans</td>
<td>25,000</td>
</tr>
<tr>
<td>Preference Share Capital</td>
<td>50,000</td>
</tr>
<tr>
<td>Reserves</td>
<td>25,000</td>
</tr>
</tbody>
</table>

(Answer: 5 Times)

11. From the following data, calculate the Fixed Asset Turnover ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed Assets</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Total Sales</td>
<td>8,50,000</td>
</tr>
<tr>
<td>Sales Returns</td>
<td>50,000</td>
</tr>
</tbody>
</table>

(Answer: 4 times)

12. Calculate Net Profit Ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Profit</td>
<td>4,000</td>
</tr>
<tr>
<td>Sales</td>
<td>44,000</td>
</tr>
<tr>
<td>Sales Return</td>
<td>4,000</td>
</tr>
</tbody>
</table>

(Answer: 10%)

13. Calculate Operating profit ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross profit</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Operating expenses</td>
<td>40,000</td>
</tr>
<tr>
<td>Sales</td>
<td>6,02,000</td>
</tr>
<tr>
<td>Sales return</td>
<td>2,000</td>
</tr>
</tbody>
</table>

(Answer: 10%)

14. Calculate Fixed Assets Turnover Ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed asset</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>25,000</td>
</tr>
<tr>
<td>Sales</td>
<td>3,00,000</td>
</tr>
</tbody>
</table>

(Answer: 4 times)

15. Calculate Fixed Assets Turnover Ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed Assets</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Sales</td>
<td>4,50,000</td>
</tr>
</tbody>
</table>

(Answer: 3 times)

16. From the following, determine the stock turnover ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Stock</td>
<td>40,000</td>
</tr>
<tr>
<td>Closing stock</td>
<td>30,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>95,000</td>
</tr>
</tbody>
</table>

(Answer: 3 times)

17. Calculate Stock turnover ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Stock</td>
<td>15,000</td>
</tr>
<tr>
<td>Closing Stock</td>
<td>25,000</td>
</tr>
<tr>
<td>Purchases</td>
<td>60,000</td>
</tr>
</tbody>
</table>

(Answer: 2.5 times)

18. Compute Debtors turnover ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Sales</td>
<td>7,50,000</td>
</tr>
<tr>
<td>Sales Return</td>
<td>50,000</td>
</tr>
<tr>
<td>Opening Debtors</td>
<td>1,17,000</td>
</tr>
<tr>
<td>Closing Debtors</td>
<td>83,000</td>
</tr>
</tbody>
</table>

(Answer: 7 times)
19. From the following, determine Debtors Turnover ratio

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Sales</td>
<td>1,75,000</td>
<td></td>
</tr>
<tr>
<td>Cash Sales</td>
<td></td>
<td>35,000</td>
</tr>
<tr>
<td>Sales Return</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Opening Debtors</td>
<td>8,000</td>
<td></td>
</tr>
<tr>
<td>Closing Debtors</td>
<td>12,000</td>
<td></td>
</tr>
</tbody>
</table>

(Answer: 13 times)

20. Calculate creditors turnover from the following information

<table>
<thead>
<tr>
<th></th>
<th>Rs.</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Purchases</td>
<td>85,000</td>
<td></td>
</tr>
<tr>
<td>Cash Purchases</td>
<td></td>
<td>20,000</td>
</tr>
<tr>
<td>Purchases Return</td>
<td>5,000</td>
<td></td>
</tr>
<tr>
<td>Opening Creditors</td>
<td>25,000</td>
<td></td>
</tr>
<tr>
<td>Closing Creditors</td>
<td>15,000</td>
<td></td>
</tr>
</tbody>
</table>

(Answer: 3 times)

21. From the Trading & Profit & Loss Account of Fashion World Ltd., ascertain the profitability ratios.

**Trading and Profit & Loss Account for the year ending 31.3.04**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Other Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>20,000</td>
<td></td>
<td>1,60,000</td>
</tr>
<tr>
<td>To Purchase</td>
<td>1,20,000</td>
<td></td>
<td>32,000</td>
</tr>
<tr>
<td>To Gross Profit (transferred to profit &amp; loss A/c)</td>
<td>52,000</td>
<td></td>
<td>1,92,000</td>
</tr>
<tr>
<td>To Administration expenses</td>
<td>12,000</td>
<td>By Gross Profit</td>
<td>52,000</td>
</tr>
<tr>
<td>To Selling expenses</td>
<td>8,000</td>
<td>By Dividend</td>
<td>400</td>
</tr>
<tr>
<td>To Finance expenses</td>
<td>4,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Loss on sale of furniture</td>
<td>500</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>27,900</td>
<td></td>
<td>52,400</td>
</tr>
</tbody>
</table>

(Answer: Gross Profit ratio 32.5%; Net Profit ratio 17.44%; Operating Profit ratio 20%; Operating cost ratio 80%)

22. From the following, calculate Profitability ratios.

**Trading & Profit and Loss of Ambika & Co. for the year ending 31.3.2004**

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Other Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Opening Stock</td>
<td>1,99,000</td>
<td></td>
<td>17,00,000</td>
</tr>
<tr>
<td>To Purchase</td>
<td>11,19,000</td>
<td></td>
<td>2,98,000</td>
</tr>
<tr>
<td>To Gross Profit</td>
<td>6,80,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>19,98,000</td>
<td></td>
<td>19,98,000</td>
</tr>
<tr>
<td>To Administration expenses</td>
<td>3,00,000</td>
<td>By Gross Profit</td>
<td>6,80,000</td>
</tr>
<tr>
<td>To Selling expenses</td>
<td>60,000</td>
<td>By Interest</td>
<td>18,000</td>
</tr>
<tr>
<td>To Financial expenses</td>
<td>30,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Loss on sale of Plant</td>
<td>8,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>3,00,000</td>
<td></td>
<td>6,98,000</td>
</tr>
</tbody>
</table>

(Answer: Gross Profit ratio 40%; Net Profit ratio 17.65%; Operating Profit ratio 18.82%; Operating ratio 81.18%)

23. From the following Balance sheet, calculate Debtors turnover, creditors turnover, Capital turnover & Fixed asset turnover ratio.

**Balance Sheet as on 31.3.04**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>4,00,000</td>
<td>Land &amp; Building</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Reserves</td>
<td>2,40,000</td>
<td>Plant &amp; Machinery</td>
<td>1,60,000</td>
</tr>
<tr>
<td>Creditors</td>
<td>2,60,000</td>
<td>Stock</td>
<td>2,96,000</td>
</tr>
<tr>
<td>6% Debentures</td>
<td>60,000</td>
<td>Debtor</td>
<td>1,42,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash</td>
<td>62,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>9,60,000</td>
</tr>
</tbody>
</table>

(Answer: Credit Purchases during the year Rs. 10,40,000
Credit Sales during the year Rs. 4,26,000)
24. From the following, calculate Operating profit ratio and Operating ratio, Gross profit ratio and Net profit ratio.

Sales 1,00,000  Dividend received 400
Gross profit 30,000  Net profit 26,600
Administration expenses 1,000
Selling expense 2,000
Loss on sale of investments 800

(Assert: Gross profit ratio - 30%; Net profit ratio - 26.6%; Operating profit ratio - 27%; Operating ratio - 73%)

25. From the following Balance sheet of Mumthaj Industries Ltd., you required to calculate Debt-Equity ratio, Proprietory ratio, Current ratio, Fixed assets turnover ratio.

Balance Sheet as on 31.03.05

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>1,00,000</td>
<td>Fixed Assets</td>
<td>1,20,000</td>
</tr>
<tr>
<td>General Reserve</td>
<td>20,000</td>
<td>Current Assets</td>
<td>80,000</td>
</tr>
<tr>
<td>Debentures</td>
<td>30,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current liabilities</td>
<td>50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>2,00,000</td>
<td></td>
<td>2,00,000</td>
</tr>
</tbody>
</table>

Additional information: Credit sales during the year was Rs.4,80,000.

(Assert: Debt-Equity ratio - 0.25:1; Proprietory ratio - 0.6:1; Current ratio - 1.6:1; Fixed asset turnover ratio - 4 times)


Balance Sheet of Jasmine Ltd. as on 31.03.2004

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Capital</td>
<td>20,000</td>
<td>Goodwill</td>
<td>12,000</td>
</tr>
<tr>
<td>Reserves</td>
<td>10,000</td>
<td>Fixed Assets</td>
<td>28,000</td>
</tr>
<tr>
<td>Loans</td>
<td>16,000</td>
<td>Stock</td>
<td>8,000</td>
</tr>
<tr>
<td>Creditors</td>
<td>10,000</td>
<td>Debtors</td>
<td>4,000</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>4,000</td>
<td>Bills receivable</td>
<td>2,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash</td>
<td>6,000</td>
</tr>
<tr>
<td></td>
<td>60,000</td>
<td></td>
<td>60,000</td>
</tr>
</tbody>
</table>

(Assert: Current ratio 1.43:1; Liquid ratio 0.86:1; Debt-Equity ratio 0.53:1; Proprietory ratio 0.625:1)

27. Calculate Current Ratio, Liquid ratio, Absolute liquid ratio, Debtors turnover and Creditors turnover ratio from the following Balance Sheet

Balance sheet

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity Share Capital</td>
<td>55,000</td>
<td>Land &amp; Buildings</td>
<td>20,000</td>
</tr>
<tr>
<td>Preference share</td>
<td>15,000</td>
<td>Plant &amp; Machinery</td>
<td>22,000</td>
</tr>
<tr>
<td>capital</td>
<td></td>
<td>Furniture &amp; fixtures</td>
<td>3,000</td>
</tr>
<tr>
<td>General Reserve</td>
<td>25,000</td>
<td>Stock</td>
<td>47,000</td>
</tr>
<tr>
<td>Debentures</td>
<td>35,000</td>
<td>Bills Receivable</td>
<td>10,000</td>
</tr>
<tr>
<td>Bills payable</td>
<td>3,000</td>
<td>Debtors</td>
<td>23,000</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>3,000</td>
<td>Short term investments</td>
<td>5,000</td>
</tr>
<tr>
<td>Creditors</td>
<td>8,000</td>
<td>Prepaid expenses</td>
<td>1,000</td>
</tr>
<tr>
<td>Outstanding expenses</td>
<td>6,000</td>
<td>Cash</td>
<td>19,000</td>
</tr>
<tr>
<td></td>
<td>1,50,000</td>
<td></td>
<td>1,50,000</td>
</tr>
</tbody>
</table>

Additional information:

Credit sales Rs. 1,65,000 Credit purchases Rs. 44,000

(Assert: Current ratio 5.25:1; Liquid ratio 2.85:1; Absolute liquid ratio 1.41:1; Debtors turnover ratio 5 times; Creditors turnover ratio 4 times)
28. The following is the summarised Trading and Profit and Loss A/c, for the year ending and the Balance Sheet as at that date:

**Trading and Profit and Loss Account**  
for the year ending 31.3.2005

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Stock</td>
<td>10,000</td>
<td>By Sales</td>
<td>1,00,000</td>
</tr>
<tr>
<td>To Purchases</td>
<td>50,000</td>
<td>By Closing stock</td>
<td>15,000</td>
</tr>
<tr>
<td>To Direct expenses</td>
<td>5,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Gross Profit c/d</td>
<td>50,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>1,15,000</td>
<td>By Gross Profit b/d</td>
<td>50,000</td>
</tr>
<tr>
<td>To Administrative expenses</td>
<td>15,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Interest</td>
<td>3,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Selling expenses</td>
<td>12,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>To Net Profit</td>
<td>20,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>50,000</td>
<td></td>
<td>50,000</td>
</tr>
</tbody>
</table>

**Balance Sheet as on 31.3.2005**

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Rs.</th>
<th>Assets</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital</td>
<td>1,00,000</td>
<td>Land and Building</td>
<td>50,000</td>
</tr>
<tr>
<td>Current liabilities</td>
<td>40,000</td>
<td>Plant and Machinery</td>
<td>30,000</td>
</tr>
<tr>
<td>Profit and Loss A/c</td>
<td>20,000</td>
<td>Furniture</td>
<td>20,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Stock</td>
<td>15,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Sundry debtors</td>
<td>15,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Bills receivable</td>
<td>12,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash in hand &amp; at bank</td>
<td>17,500</td>
</tr>
<tr>
<td></td>
<td>1,60,000</td>
<td></td>
<td>1,60,000</td>
</tr>
</tbody>
</table>

From the above, calculate –


*(Answer: Gross Profit Ratio 50%; Current Ratio 1.5:1; Acid Test Ratio 1.125:1; Stock Turnover Ratio 4 times; Fixed Assets Turnover Ratio 1 time)*
Chapter - 5
CASH BUDGET

Learning Objectives

After studying this Chapter, you will be able to

- understand the meaning, definition, characteristics and advantages of Cash budget.
- prepare cash budget using receipts and payments method.

Cash Budget is a component of two words - cash and budget. The term “cash” here stands for cash and bank balance. “Budget” means, in simple words, an estimate relating to future activities of an organisation.

5.1 Budget:

Budget is a blue print of future course of action and activities. Budget means expressing the future course of action of an organisation in quantitative terms.

*Longman’s Dictionary of Business English* defines a budget as “an account of the probable future income and expenditure”.

According to the *Institute of Cost and Management Accountants, London*, Budget is “a financial and/or quantitative statement, prepared and approved prior to a defined period of time, of
the policy to be pursued during that period for the purpose of attaining a given objective”.

5.1.1 Characteristics:

Budget has the following important characteristics
1. It is prepared in advance and relates to a future period.
2. It is expressed in terms of money and/or physical units.
3. It is a mean to achieve the planned objective.

In business, the different kinds of budgets are prepared to facilitate different aspects of the business concern. Such aspects relate to sales, purchases, production, overheads as well as financing of the business. One of the main budgets prepared by a business concern is **Cash Budget**.

5.2 Cash Budget:

Cash budget is one of the most important budgets prepared by a business concern as every transaction directly or indirectly deals with cash. **Cash budget** shows the estimate of cash receipts and cash payments from all sources over a specific period. This is also called as **Finance Budget**.

5.2.1 Advantages:

1. It helps in maintaining an adequate cash balance.
2. It provides the following useful information to the management
   a. to determine the future cash needs of a business concern
   b. to plan for financing those needs and
   c. to have control over cash balance of the business concern.

Thus, in short cash budget is an useful tool for financial planning.

5.2.2 Preparation of cash budget – Methods

There are three methods by which a cash budget is prepared. They are
1. Receipts and Payments Method
2. Adjusted Profit and Loss Account Method or Cash Flow Method
3. Balance Sheet Method

However, among the three methods only “Receipts and Payments Method” alone is discussed in this chapter.

**Receipts and Payments Method**

Under this method Cash budget projects the concern’s cash receipts and payments for a certain period (budget period). It has two basic components:
1. Estimate of cash receipts and
2. Estimate of cash payments

**Cash Receipts** include:
- Cash sales
- Cash receivable from customers
- Business receipts like interest, commission, dividend etc
- Sale of assets
- Proceeds from issue of shares/debentures
- Loans borrowed

**Cash Payments** include:
- Cash purchases
- Cash payable to suppliers
- Business expenses like wages, office expenses, selling expenses, etc.
• Payment of interest, income tax, dividend etc.
• Purchase of assets
• Redemption of shares/debentures
• Repayment of loans

**Steps in the preparation of cash budget**

*Step 1 →* Take opening cash balance

*Step 2 →* Add the estimated total cash receipts for the month

*Step 3 →* Calculate the total cash available for the month

*Step 4 →* Less the estimated total cash payments during the month

*Step 5 →* Calculate the closing cash balance

**Format:**

### Cash Budget for the period ————

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Month 1 Rs.</th>
<th>Month 2 Rs.</th>
<th>Month 3 Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening Cash Balance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Add: Estimated cash receipts :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash sales</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash receivable from customers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Business receipts like Interest, commission, dividend etc</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sale of assets</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loans borrowed</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proceeds from issue of shares/debentures</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total cash available during the month</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| Less: Estimated cash payments : |             |             |             |
| Cash purchases |             |             |             |
| Payable to suppliers |             |             |             |
| Business expenses – wages, office expenses, selling expenses, etc |             |             |             |
| Business Payments – Interest paid, income tax, dividend etc |             |             |             |
| Purchase of assets |             |             |             |
| Repayment of loans |             |             |             |
| Redemption of shares/debentures |             |             |             |
| **Total cash payments during the month** |             |             |             |
| **Closing cash balance** |             |             |             |

The closing cash balance of the current month will be the opening cash balance of the next month.

**Illustration : 1**

From the following information, prepare cash budget for June 2005.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash in hand 1.6.2005</td>
<td>10,000</td>
</tr>
<tr>
<td>Cash purchases for June, 2005</td>
<td>70,000</td>
</tr>
<tr>
<td>Cash sales for June, 2005</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Interest payable in June, 2005</td>
<td>1,000</td>
</tr>
<tr>
<td>Purchase of Office furniture in June, 2005</td>
<td>2,500</td>
</tr>
</tbody>
</table>
Solution:

### Cash Budget for the month June, 2005

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening cash balance</td>
<td>10,000</td>
</tr>
<tr>
<td>Add: Estimated receipts:</td>
<td></td>
</tr>
<tr>
<td>Cash Sales</td>
<td>1,00,000</td>
</tr>
<tr>
<td>Total cash available during the month</td>
<td>1,10,000</td>
</tr>
<tr>
<td>Less: Estimated cash payments:</td>
<td></td>
</tr>
<tr>
<td>Cash purchases</td>
<td>70,000</td>
</tr>
<tr>
<td>Interest paid</td>
<td>1,000</td>
</tr>
<tr>
<td>Purchase of furniture</td>
<td>2,500</td>
</tr>
<tr>
<td>Total cash payments</td>
<td>73,500</td>
</tr>
<tr>
<td>Closing cash balance</td>
<td>36,500</td>
</tr>
</tbody>
</table>

### Illustration : 2

Prepare a cash budget for the months of June, July, August 2004 from the following information:

1) Opening cash balance in June Rs.7,000.
2) Cash sales for June Rs.20,000; July Rs.30,000 and August Rs.40,000.
3) Wages payable Rs.6,000 every month.
4) Interest receivable Rs.500 in the month of August.
5) Purchase of furniture for Rs.16,000 in July.
6) Cash Purchases for June Rs.10,000; July Rs.9,000 and August Rs.14,000.

Solution:

### Cash Budget for the period June to August 2004

<table>
<thead>
<tr>
<th>Particulars</th>
<th>June Rs.</th>
<th>July Rs.</th>
<th>August Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening cash balance</td>
<td>7,000</td>
<td>11,000</td>
<td>10,000</td>
</tr>
<tr>
<td>Add: Estimated cash receipts:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash sales</td>
<td>20,000</td>
<td>30,000</td>
<td>40,000</td>
</tr>
<tr>
<td>Interest</td>
<td>—</td>
<td>—</td>
<td>500</td>
</tr>
<tr>
<td>Total cash available during the month</td>
<td>27,000</td>
<td>41,000</td>
<td>50,500</td>
</tr>
<tr>
<td>Less: Estimated cash payments:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash purchases</td>
<td>10,000</td>
<td>9,000</td>
<td>14,000</td>
</tr>
<tr>
<td>Payment of wages</td>
<td>6,000</td>
<td>6,000</td>
<td>6,000</td>
</tr>
<tr>
<td>Purchase of furniture</td>
<td>—</td>
<td>16,000</td>
<td>—</td>
</tr>
<tr>
<td>Total cash payments during the month</td>
<td>16,000</td>
<td>31,000</td>
<td>20,000</td>
</tr>
<tr>
<td>Closing cash balance</td>
<td>11,000</td>
<td>10,000</td>
<td>30,500</td>
</tr>
</tbody>
</table>

**Note:** The closing cash balance in June will be the opening cash balance in July.

### Illustration : 3

From the following information, prepare a budget for three months from October 2003.

1) Opening cash balance in October Rs.3000.
2) Cash Sales October: Rs.25,000; November : Rs.20,000; December : Rs.15,000.
3) Credit purchases – September Rs.10,000; October Rs.12,000; November Rs.14,000; December Rs.16,000. The period of credit allowed by suppliers is one month.

4) Dividend to be received in December Rs.4,000.

5) Advance tax Rs.3,000 payable in October.

6) Sale of an old asset for Rs.12,000 during November.

**Solution:**

### Cash Budget for the period October to December 2003

<table>
<thead>
<tr>
<th>Particulars</th>
<th>October Rs.</th>
<th>November Rs.</th>
<th>December Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening cash balance</td>
<td>3,000</td>
<td>15,000</td>
<td>35,000</td>
</tr>
<tr>
<td>Add: Estimated cash receipts :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash sales</td>
<td>25,000</td>
<td>20,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Dividend</td>
<td>—</td>
<td>—</td>
<td>4,000</td>
</tr>
<tr>
<td>Sale of asset</td>
<td>—</td>
<td>12,000</td>
<td>—</td>
</tr>
<tr>
<td>Total cash available during the month</td>
<td>28,000</td>
<td>47,000</td>
<td>54,000</td>
</tr>
</tbody>
</table>

| Less: Estimated cash payments :      |             |              |              |
| Payment to suppliers                 | 10,000      | 12,000       | 14,000       |
| Advance income tax payable           | 3,000       | —            | —            |
| Total cash payments during themonth  | 13,000      | 12,000       | 14,000       |

| Closing cash balance                 | 15,000      | 35,000       | 40,000       |

**Note:** The suppliers of goods have given one month credit, so the purchases made in September will be paid in October and those purchases in October will be paid in November, those purchases in November will be paid in December.

### Illustration : 4

From the following information, prepare a cash budget for April, May and June 2005.

<table>
<thead>
<tr>
<th>Month</th>
<th>Credit Sales Rs.</th>
<th>Credit Purchases Rs.</th>
<th>Office Expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>February</td>
<td>45,000</td>
<td>30,000</td>
<td>8,000</td>
</tr>
<tr>
<td>March</td>
<td>55,000</td>
<td>25,000</td>
<td>7,000</td>
</tr>
<tr>
<td>April</td>
<td>60,000</td>
<td>20,000</td>
<td>7,000</td>
</tr>
<tr>
<td>May</td>
<td>60,000</td>
<td>40,000</td>
<td>9,000</td>
</tr>
<tr>
<td>June</td>
<td>65,000</td>
<td>40,000</td>
<td>9,000</td>
</tr>
</tbody>
</table>

1) Opening cash balance Rs.5000.
2) Credit allowed by suppliers is two months.
3) Credit allowed to customers is one month.
4) Office expenses are payable in the same month.
5) Dividend Rs.1000 is receivable in April.
6) Interest payable in May Rs.1,800.

**Solution:**

### Cash Budget for the period April to June, 2005

<table>
<thead>
<tr>
<th>Particulars</th>
<th>April Rs.</th>
<th>May Rs.</th>
<th>June Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening cash balance</td>
<td>5,000</td>
<td>24,000</td>
<td>48,200</td>
</tr>
<tr>
<td>Add: Estimated cash receipts :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash receivable from customers</td>
<td>55,000</td>
<td>60,000</td>
<td>60,000</td>
</tr>
<tr>
<td>Dividend</td>
<td>1,000</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Total cash available during the month</td>
<td>61,000</td>
<td>84,000</td>
<td>1,08,200</td>
</tr>
</tbody>
</table>
Illustration : 5

Prepare a cash budget for the months – March, April and May 2005 from the following information

<table>
<thead>
<tr>
<th>Month</th>
<th>Credit Sales Rs.</th>
<th>Credit Purchase Rs.</th>
<th>Wages Rs.</th>
<th>Misc. Expenses Rs.</th>
<th>Office Expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>60,000</td>
<td>36,000</td>
<td>9,000</td>
<td>4,000</td>
<td>2,000</td>
</tr>
<tr>
<td>February</td>
<td>82,000</td>
<td>38,000</td>
<td>8,000</td>
<td>3,000</td>
<td>1,500</td>
</tr>
<tr>
<td>March</td>
<td>84,000</td>
<td>33,000</td>
<td>10,000</td>
<td>4,500</td>
<td>2,500</td>
</tr>
<tr>
<td>April</td>
<td>78,000</td>
<td>35,000</td>
<td>8,500</td>
<td>3,500</td>
<td>2,000</td>
</tr>
<tr>
<td>May</td>
<td>56,000</td>
<td>39,000</td>
<td>9,500</td>
<td>4,000</td>
<td>1,000</td>
</tr>
</tbody>
</table>

Additional information :
1) Opening cash balance Rs.8,000.
2) Period of credit allowed to customers one month
3) Period of credit allowed by suppliers two months.
4) Wages and miscellaneous expenses are payable in the same month.
5) Lag in payment of office expenses is one month

Solution:

Cash Budget for the period March, April & May 2005

<table>
<thead>
<tr>
<th>Particulars</th>
<th>March Rs.</th>
<th>April Rs.</th>
<th>May Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opening cash balance</td>
<td>8,000</td>
<td>38,000</td>
<td>69,500</td>
</tr>
<tr>
<td>Add: Estimated cash receipts :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash receivable from customers</td>
<td>82,000</td>
<td>84,000</td>
<td>78,000</td>
</tr>
<tr>
<td>Total cash available during the month</td>
<td>90,000</td>
<td>1,22,000</td>
<td>1,47,500</td>
</tr>
<tr>
<td>Less: Estimated cash payments :</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payments to suppliers</td>
<td>36,000</td>
<td>38,000</td>
<td>33,000</td>
</tr>
<tr>
<td>Wages</td>
<td>10,000</td>
<td>8,500</td>
<td>9,500</td>
</tr>
<tr>
<td>Office expenses</td>
<td>1,500</td>
<td>2,500</td>
<td>2,000</td>
</tr>
<tr>
<td>Miscellaneous expenses</td>
<td>4,500</td>
<td>3,500</td>
<td>4,000</td>
</tr>
<tr>
<td>Total cash payments during the month</td>
<td>52,000</td>
<td>52,500</td>
<td>48,500</td>
</tr>
<tr>
<td>Closing cash balance</td>
<td>38,000</td>
<td>69,500</td>
<td>99,000</td>
</tr>
</tbody>
</table>

Notes:
1. The closing cash balance in March will be the opening balance in April and so on.
2. Since credit allowed to customers is one month, the amount of credit sales in February is collected in March and so on.
3. Since credit allowed by suppliers is two month credit purchases of January is paid in March and so on.
4. Office expenses are paid in the next month, so office expenses for February will be paid in March and so on.
QUESTIONS

I. Objective Type:

a) Fill in the blanks:

1. The term ‘cash’ in cash budget stands for _________ and __________.
2. Cash budget is also called as __________.
3. There are __________ methods by which a cash budget is prepared.
4. The opening balance of cash in April is Rs.1250. Total receipts for the month are Rs.4300 and total payments amounted to Rs.3750. Opening balance of cash in May will be __________
5. Cash budget is a useful tool for __________.
6. The closing balance of one month will be the __________ balance of the next month.


b) Choose the correct answer:

1. Budget is an estimate relating to __________ period.
   a) future  b) current  c) past
2. Budget is expressed in terms of
   a) Money  b) Physical units  c) Money & Physical units
3. Cash budget deals with
   a) Estimated cash receipts  b) Estimated cash payments  c) Estimated cash receipts & Estimated cash payments
4. Purchase of Furniture is an example for
   a) Cash receipts  b) Cash payments  c) None of the above
5. The opening balance of cash in January is Rs.9,000. The estimated receipts are Rs.14,000 and the estimated payments are Rs.10,000. The opening balance of cash in February will be
   a) Rs. 21,000  b) Rs. 11,000  c) Rs. 13,000

(Answers: 1. (a); 2. (c); 3. (c); 4. (b); 5. (c))

II. Other Questions:

1. Define Budget
2. What are the characteristics of a budget?
3. Write notes on Cash budget
4. What are the advantages of cash budget?
5. List the methods that can be used for the preparation of the cash budget.
6. Give few examples for cash receipts?
7. Give few examples for cash payments?
8. Enumerate the steps in the preparation of cash budget.

III. Problems:

1. Prepare cash budget for the month of January 2005 from the following information
   a) Cash in hand (estimated) Rs.250
   b) Cash sales for January, 2005 Rs.6,500
   c) Wages for the month January Rs.2,375
   d) Cash purchases Rs.2,745
   e) Interest receivable on investments Rs.175.

   (Answer: Balance of cash Rs.1,805)
2. Prepare cash budget for the month of October from the following information
   a) Estimated cash balance on 1st October Rs.1,775
   b) Credit sales:
      - August Rs.14,000
      - September Rs.16,000
      - October Rs.17,000
   Period of credit allowed to customers is one month
   c) Credit purchases:
      - August Rs.8,000
      - September Rs.12,000
      - October Rs.10,000
   Period of credit allowed by suppliers is two months
   d) Purchase of plant Rs.7,000
   e) Wages to be paid in October Rs.2,000

   (Answer: Rs. 775)

3. Prepare cash budget for the month of March from the following information
   a) Estimated cash balance on 1st March Rs.8,775
   b) Credit sales:
      - January Rs.70,000
      - February Rs.80,000
      - March Rs.85,000
   Period of credit allowed to customers is one month
   c) Credit purchases:
      - January Rs.40,000
      - February Rs.60,000
      - March Rs.50,000
   Period of credit allowed by suppliers is two months
   d) Purchase of plant Rs.7,000
   e) Wages to be paid in March Rs.10,000

   (Answer: Rs. 3,775)

   a) Opening cash balance estimated in June Rs.4,025
   b) Cash purchases in June Rs.12,000 and July Rs.16,000
   c) Cash sales in June Rs.18,000 and July Rs.24,000
   d) Salaries payable in June Rs.5,000 and July Rs.5,000
   e) Repayment of a loan in July Rs.6,500

   (Answer: Closing balance – June Rs.5,025; July Rs.1525)

5. Prepare a cash budget for the month of August and September 2004 from the following information
<table>
<thead>
<tr>
<th></th>
<th>Credit Sales</th>
<th>Credit Purchases</th>
<th>Wages</th>
<th>Selling Expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>June</td>
<td>2004</td>
<td>1,87,000</td>
<td>1,24,800</td>
<td>12,000</td>
</tr>
<tr>
<td>July</td>
<td>2004</td>
<td>1,92,000</td>
<td>1,83,600</td>
<td>14,000</td>
</tr>
<tr>
<td>August</td>
<td>2004</td>
<td>1,94,000</td>
<td>1,46,000</td>
<td>11,000</td>
</tr>
<tr>
<td>September 2004</td>
<td>1,26,000</td>
<td>1,73,400</td>
<td>10,000</td>
<td>7,500</td>
</tr>
</tbody>
</table>

   1. Suppliers allowed two months credit.
   2. Customers were given one month credit.
   3. Wages are payable in the same month.
   4. Delay in payment of selling expenses was one month.
   5. Commission receivable Rs.11,025 in August.
   6. Estimated cash balance as on 1st August Rs.9,075

   (Answer: August Rs. 71,500; September Rs.65,300)

6. Prepare a cash budget for the month of January, February and March 2005 from the following information
Month & Year | Credit purchases | Credit sales | Wages |
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>November 2004</td>
<td>2,00,000</td>
<td>2,50,000</td>
<td>50,000</td>
</tr>
<tr>
<td>December 2004</td>
<td>3,00,000</td>
<td>3,50,000</td>
<td>60,000</td>
</tr>
<tr>
<td>January 2005</td>
<td>4,00,000</td>
<td>4,50,000</td>
<td>60,000</td>
</tr>
</tbody>
</table>

1. Expected Cash balance on 1.1.2005 is Rs.75,000
2. Suppliers allowed a credit period of two months
3. A credit period of two months is allowed to customers
4. Lag in payment of wages is one month

(Answer: January Rs.65,000; February Rs.55,000; March Rs. 1,25,000)

7. From the following, prepare a cash budget for August & September 2004

<table>
<thead>
<tr>
<th></th>
<th>July Rs.</th>
<th>August Rs.</th>
<th>September Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash purchases</td>
<td>1,00,000</td>
<td>2,00,000</td>
<td>3,00,000</td>
</tr>
<tr>
<td>Cash sales</td>
<td>2,75,000</td>
<td>3,25,000</td>
<td>4,75,000</td>
</tr>
<tr>
<td>Credit purchase</td>
<td>1,45,000</td>
<td>2,45,000</td>
<td>3,25,000</td>
</tr>
<tr>
<td>Credit sales</td>
<td>2,75,000</td>
<td>3,45,000</td>
<td>4,00,000</td>
</tr>
<tr>
<td>Expenses</td>
<td>50,000</td>
<td>60,000</td>
<td>70,000</td>
</tr>
</tbody>
</table>

1. Estimated Opening balance of cash on 1st August Rs.80,000
2. Credit allowed by suppliers and to customer is one month
3. Expenses are payable in the same month
4. Dividend receivable in August is Rs.16,000
5. Commission payable in September is Rs.2,70,000.

(Answer: August Rs. 2,91,000; September Rs.2,26,000)

8. Prepare a cash budget for January, February and March 2005 from the following information

<table>
<thead>
<tr>
<th>Month</th>
<th>Sales Rs.</th>
<th>Purchases Rs.</th>
<th>Expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 2004</td>
<td>5,00,000</td>
<td>4,00,000</td>
<td>55,000</td>
</tr>
<tr>
<td>January 2005</td>
<td>6,00,000</td>
<td>6,00,000</td>
<td>65,000</td>
</tr>
<tr>
<td>February 2005</td>
<td>7,00,000</td>
<td>4,00,000</td>
<td>75,000</td>
</tr>
<tr>
<td>March 2005</td>
<td>8,00,000</td>
<td>5,00,000</td>
<td>85,000</td>
</tr>
</tbody>
</table>

1. All sales are for cash.
2. The period of credit allowed by the suppliers is one month.
3. Lag in payment of expenses is one month.
4. Opening cash balance on 1.1.05 is Rs.45,000.
5. In March, an asset for Rs.2,00,000 is to be purchased.

(Answer: January Rs.1,90,000; February Rs.2,25,000; March Rs.3,50,000)

9. From the following, prepare a cash budget for June & July 2005

<table>
<thead>
<tr>
<th></th>
<th>May Rs.</th>
<th>June Rs.</th>
<th>July Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash purchases</td>
<td>50,000</td>
<td>1,00,000</td>
<td>1,50,000</td>
</tr>
<tr>
<td>Cash sales</td>
<td>1,37,500</td>
<td>1,62,500</td>
<td>2,37,500</td>
</tr>
<tr>
<td>Credit purchase</td>
<td>72,500</td>
<td>1,22,500</td>
<td>1,62,500</td>
</tr>
<tr>
<td>Credit sales</td>
<td>1,37,500</td>
<td>1,72,500</td>
<td>2,00,000</td>
</tr>
<tr>
<td>Expenses</td>
<td>25,000</td>
<td>30,000</td>
<td>35,000</td>
</tr>
</tbody>
</table>

1. Estimated Opening balance of cash on 1st June Rs.40,000
2. Credit allowed by suppliers and to customer is one month
3. Expenses are payable in the same month
4. Dividend receivable in June is Rs.8,000
5. Commission payable in July is Rs.1,35,000.

(Answer: June Rs. 1,45,500; July Rs.1,13,000)

10. Prepare a cash budget for October, November and December 2004 from the following information

<table>
<thead>
<tr>
<th>Month</th>
<th>Sales Rs.</th>
<th>Purchases Rs.</th>
<th>Expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>September</td>
<td>10,00,000</td>
<td>8,00,000</td>
<td>1,10,000</td>
</tr>
<tr>
<td>October</td>
<td>12,00,000</td>
<td>12,00,000</td>
<td>1,30,000</td>
</tr>
<tr>
<td>November</td>
<td>14,00,000</td>
<td>8,00,000</td>
<td>1,50,000</td>
</tr>
<tr>
<td>December</td>
<td>16,00,000</td>
<td>10,00,000</td>
<td>1,70,000</td>
</tr>
</tbody>
</table>

1. All sales are for cash.
2. The period of credit allowed by the suppliers is one month.
3. Lag in payment of expenses is one month.
4. Opening balance of cash on 1.10.04 is Rs.90,000.
5. In December, an asset for Rs.4,00,000 is to be purchased.

(Answer: October Rs.3,80,000; November Rs.4,50,000; December Rs.70,000)

11. Prepare a cash budget for the month of March, April and May 2005 from the following information

<table>
<thead>
<tr>
<th>Month</th>
<th>Credit Purchases Rs.</th>
<th>Credit Sales Rs.</th>
<th>Administration &amp; Selling expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>75,000</td>
<td>1,50,000</td>
<td>1,20,000</td>
</tr>
<tr>
<td>February</td>
<td>1,00,000</td>
<td>1,35,000</td>
<td>1,35,000</td>
</tr>
<tr>
<td>March</td>
<td>85,000</td>
<td>1,75,000</td>
<td>65,000</td>
</tr>
</tbody>
</table>

April
<table>
<thead>
<tr>
<th>Credit Purchases Rs.</th>
<th>Credit Sales Rs.</th>
<th>Expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,25,000</td>
<td>1,20,000</td>
<td>70,000</td>
</tr>
</tbody>
</table>
May
<table>
<thead>
<tr>
<th>Credit Purchases Rs.</th>
<th>Credit Sales Rs.</th>
<th>Expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>90,000</td>
<td>1,40,000</td>
<td>80,000</td>
</tr>
</tbody>
</table>

1. Expected Cash balance on 1.3.2005 is Rs.80,000
2. Suppliers allowed a credit period of two months
3. A credit period of one month is allowed to customers
4. Expenses are paid in the same month.
5. Sale of fixed asset Rs. 25,000 in April.
6. Purchase of fixed asset in May Rs.25,000.

(Answer: March Rs.75,000; April Rs.1,05,000; May Rs. 35,000)

12. Prepare a Cash Budget of Rama Ltd., for the months of January to March 2004 from the following information:

<table>
<thead>
<tr>
<th>Credit Purchases Rs.</th>
<th>Credit Sales Rs.</th>
<th>Expenses Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td></td>
<td></td>
</tr>
<tr>
<td>November</td>
<td>2,00,000</td>
<td>2,50,000</td>
</tr>
<tr>
<td>December</td>
<td>3,50,000</td>
<td>3,00,000</td>
</tr>
<tr>
<td>2004</td>
<td></td>
<td></td>
</tr>
<tr>
<td>January</td>
<td>3,00,000</td>
<td>4,50,000</td>
</tr>
<tr>
<td>February</td>
<td>4,00,000</td>
<td>2,00,000</td>
</tr>
<tr>
<td>March</td>
<td>5,00,000</td>
<td>3,50,000</td>
</tr>
</tbody>
</table>

Additional Information:

i) Expected cash balance as on 1.1.2004 Rs.75,000
ii) Suppliers allowed credit of two months and a credit of two months is allowed to the customers
iii) Lag in payment of expenses one month.
iv) Sale of fixed assets in the month of February Rs. 95,000

(Answer: January Rs.65,000; February Rs.40,000; March Rs.1,10,000)