

**I YEAR – I SEMESTER
COURSE CODE: 7BCS1C2**

CORE COURSE - II – FINANCIAL ACCOUNTING – I

Unit I

Accounting Principles – Conventions – concepts and process – Double entry book keeping – Rules– limitations – collection and recording of financial data – journal – Ledger – Trial balance. Preparation of Bank Reconciliation Statement.

Unit II

Errors – Rectification of Errors – suspense account – Final Accounts.

Unit III

Bills of Exchange – Trading and Accommodation Bills – Renewal – Dishonour of bills – Retiring of Bills

Unit IV

Accounting of non-trading concerns (All methods) – Consignment accounts – normal loss – abnormal loss – calculation of unsold stock – prices of goods returned – loading factors

Unit V

Joint ventures (All methods) – Insurance Claims (Loss of Stock) – Sale or return

Books for Reference:

1. M.C.Shukla and T.S.Grewal, Advanced Accounts, S.Chand & Company, New Delhi
2. S.N.Maheswari, An introduction to Accountancy, Sultan Chand & Sons, New Delhi
3. M.A.Arulanandam and K.S.Raman, Advanced Accountancy, Himalaya Publishing House, Mumbai
4. R.L.Gupta and M.Radhaswamy, Advanced Accountancy, Sultan Chand & Sons, New Delhi
5. S.P.Jain and Narang, Advanced Accountancy, Kalyani Publishers, Ludhiyana



GOVERNMENT ARTS COLLEGE FOR WOMEN RAMANATHAPURAM

FINANCIAL ACCOUNTING –I (7BCS1C2)

UNIT-I

Meaning :

Accounting is a systematic record of the daily events of a business. It leads to presentation of a complete of a financial picture. Accounting in its elementary stages is called book Keeping.

Definition :

The American institute of certified public accounts defines accounting as the “ art of recording , classifying and summarizing in a significant manner and in items of money. Transactions and events which are, in part at least, of a financial character and interpreting the results thereof”.

ACCOUNTING PRINCIPLES

Accounting principles may be defined as those rules of conduct or procedure which are adopted by the accountants universally, while recording the accounting transactions. Following these principal while recording the transaction will ensure uniformity, clarity and understanding. The accounting principal can be classified into two categories: (i) accounting concepts (ii) accounting conventions.

ACCOUNTING CONCEPTS:

Accounting is the language of business. The basic assumptions or conditions upon which the science of accounting are based on the concepts of accounting. The different concepts of accounting are given below.

I) Business Entity concept:

This concept denotes that a business unit is separate and distinct from the owner's . Therefore , it is necessary to record the business separately to distinguish from the owners personal transactions . This concept has now been extended to accounting for various divisions of a firm in order to ascertain the results of each division.

II) Going concern concept:

It is assumed that the business will exist for a long time and transaction are recorded from this point of view. That people may come and go, but business remains, is the principle of this concept. Hence, proper classification of expenses (capital and revenue) is to be made.

III) Money measurement concept:

Accounting records only those transactions which are expressed in items of money. The use of building and the use of clerical services can be added up only through money values and not otherwise.

IV) Cost concept :

The transactions are entered in the books of accounts at the amounts actually involved. For example : if a firm purchases a land for Rs. 2,00,000 but considers it as worthy Rs.

4,00,000 the purchase will be recorded at Rs. 2,00,000 and not at any more. This is one of the most important concepts.

V) Dual –Aspect concept:

Each transaction has two aspects. If a business has acquired an asset, the asset which comes in this is one aspect. To acquire the asset the business has to pay money (cash or bank) which goes out –this is another aspect. If it is acquired for credit, a liability arises to that extent. Thus if there is an increase in assets, there will be an increase in liability also.

$\text{Assets} = \text{Liabilities} + \text{Capital}$

(or)

$\text{Capital} = \text{Assets} - \text{Liabilities}$

VI) Realization concept

Accounting is a historical record of transaction. It records what has happened. Unless money has been realized-either cash has been received or legal obligation to receive from the customer –no sale can be said to have taken place and no profit or income can be said to have arisen.

VII) Accounting period concept :

A business is assumed to continue indefinitely. In order to ascertain the state of affairs of the business at different intervals, we have to choose the intervals for ascertaining the financial position and the operation results at each such interval which is known as the accounting periods . visually a period of 52 weeks or 365 days is considered as the accounting period.

Accounting conventions :

The term convention implies customs or traditions which guide the accountant while preparing the accounting statements. The following are the accounting conventions.

- i) Convention of consistency ii) Convention of full disclosure
- iii) Convention of conservatism

I) Convention Of Consistency :

The accounting practices should remain the same for all years to come. The rule and practices should not be changed from time to time. For example : the stock – in trade must be valued on the basis of the same method in all the years.

II) Convention Of Full Disclosure :

Apart from legal requirements, good accounting practice also demands that all significant information should be disclosed. For example : the values of assets have to be stated along with the mode of valuation.

III) Convention Of Conservatism :

Anticipation of future losses like reserve for bad and doubtful debts etc. but not the future profits or gains like raise in the value of stock or reserve for discount on creditors is the basic rule of conservatism.

DOUBLE – ENTRY SYSTEM OF ACCOUNTING :

There are two different systems of accounting for recording the business transactions:

- (a) **cash system of accounting** : under this system, only actual cash received and cash paid are recorded. No entry is made for a receipt which is merely due: however, any payment outstanding will be accounted for. Government accounting is based on the cash system only. Professional people like lawyers, chartered Accountants, etc., maintain accounts under this system.

- (b) Mercantile system or accrual system of accounting :

Under this system of accounting , entries are made not only for actual receipt or payment of cash but also for amounts having become due for payment or receipt. In other words, both cash transactions and credit transaction are recorded in the books of accounts. All commercial establishments and even non-trading concerns follow this system only. Further , accounting records can be prepared under any one of the following system :

- i) Single-entry system :

Under this system only the personal aspects of the transactions are recorded in the books and the Impersonal aspects are ignored. It is not based on the ‘dual’ aspect and is incomplete, inaccurate and unscientific.

- ii) Double-entry system:

It is the most common system of keeping records whereby the two Aspects of every transaction- the giving aspect and the receiving aspect-are Recorded in the book of accounts. Each aspect will be recorded in one account and This method of writing every transaction in two accounts is known as double entry System of book-keeping. This is the must scientific complete and accurate system of Accounting .

THE RULES OF THE DOUBLE ENTRY SYSTEM:

Types of accounts :

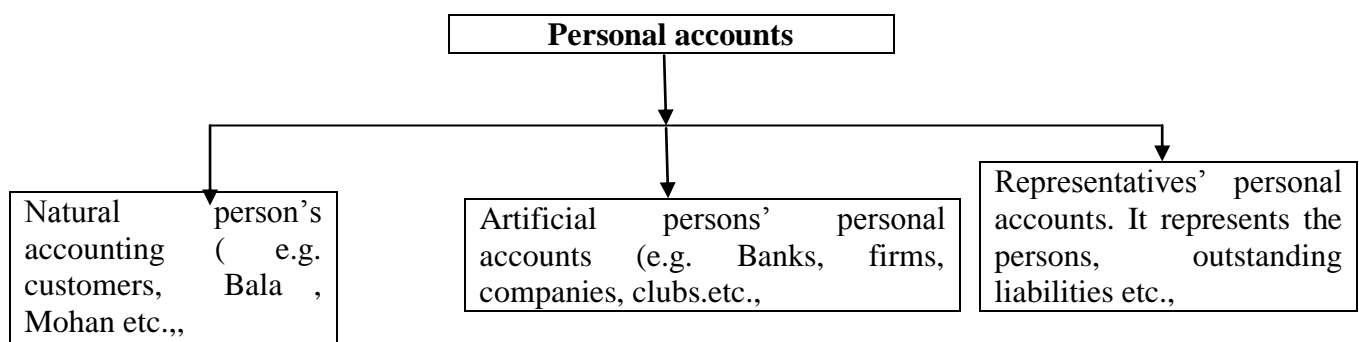
- i) A business May with persons, firms, institutions, companies etc.,
- ii) With assets and liabilities
- iii) Expenses and income

Based on these dealing the accounts are classified into three category , namely,

- a) Personal Accounts b) Real Accounts C) Nominal Accounts

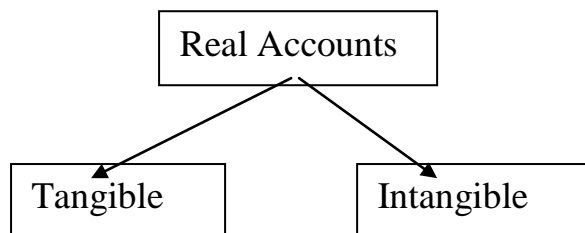
- a) Personal Accounts:

It deals with accounts relating to person, firm, companies and man-made institutions. It is further classified into three as shown below:



a) **Real accounts :**

It deals with accounts relating to the properties and assets of the business (e.g., cash a/c , furniture a/c, Land and Building a/c, Machinery a/c, shares a/c, goods (purchases and sales) a/c.



C) **Nominal accounts :**

It deals with those items which exist in names only . i.e., it deals with items of income and expenditures. (e.g., Rent, Salary, Commission , Discount , Dividend received , Depreciations etc.,,

Limitations:

The following are the various limitations of accounting .

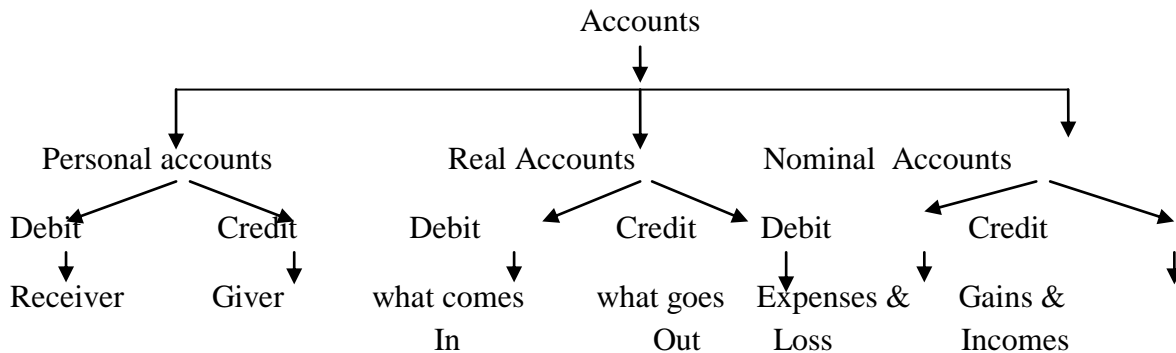
- i) Transactions of non-monetary nature do not find place in accounting . Accounting is limited to monetary transactions only. It excludes qualitative elements like reputation, employee morale and so on.
- ii) It is historical in nature. So it does not reflect current financial worth of the business.
- iii) Price changes are not considered. Money value is bound to change often from time to time. This is a strong limitation of accounting.
- iv) Elaborate recording of transactions increase the volume of accounting and the cost of operations.
- v) The system needs competent people, who should have sound knowledge for maintenance of accounting records.
- vi) Accounting policies are framed by the accountant. The figures of balance sheet are largely resulted by personal judgment of accountant hence it is the subjective factor that prevails in accounting and objective factor in Ignored
- vii)

Double Entry and single Entry system

	DOUBLE ENTRY SYSTEM	SINGLE ENTRY SYSTEM
i)	Both debit and credit aspects of a transaction are recorded.	Only one aspect of a transaction is recorded.
ii)	All the three accounts namely personal ,Real and Nominal – are maintained.	Only personal accounts and cash accounts are maintained.
iii)	For every debit there is a corresponding and equal credit.	There may be a debit a without a corresponding and equal credit.
iv)	Trial Balance can be prepared	Trial Balance can't be prepared

v)	Arithmetic accuracy can be checked.	No arithmetic accuracy can be checked.
vi)	Trading , profit & loss a/c and balance-sheet can be prepared.	Trading , profit & loss a/c and balance-sheet can't be prepared directly.
vii)	Accurate net profit can be calculated.	Only approximate profit can be calculated .
viii)	It is a perfect and scientific system.	It is an imperfect and unscientific system.
ix)	It involves more clerical work.	It involves less clerical work.
x)	Tax authorities accept this method.	Tax authorities do not accept as such.

Collection and recording of financial data



To make a correct record of the transactions, find out in the order shown below:

- What are the two aspects of the transaction?
- What are the two accounts in which these aspects are to be recorded?
- To which category these accounts belong – personal , Real or Nominal?
- What rules of debit and credit are applicable to the accounts involved?
- What account should be debited or credited?

Example : From the following transactions find out the nature of account and also state which account should be debited and which account should be credited:

- a) Wage paid; b) Dividends received ; c) Building purchased for cash ; d) furniture sold :
e) outstanding rent; f) Received cash from Balan; g) Proprietor introduced capital.

Solution:

Transaction	Account involved	Nature of Accounts	Debit /Credit
a) Wage paid	Wage A/c Cash A/c	Nominal Real	Debit Credit
b) Dividend received	Cash A/c Dividends A/c	Real Nominal	Debit Credit
c) Building purchased	Buildings A/c Cash A/c	Real Real	Debit Credit
d) Furniture sold	Cash A/c Furniture A/c	Real Real	Debit Credit
e) outstanding Rent	Rent A/c Outstanding Rent A/c	Nominal personal	Debit Credit
f) Received cash from Balan	Cash A/c Balan A/c	Real personal	Debit Credit
g) Capital introduced	Cash A/c Capital A/c	Real personal	Debit Credit

Illustration :1

Journalise the following transaction :

2008,jan.

11 purchased goods for	Rs.1,500.
12 purchased goods from GK stores	Rs.900
13 sold goods for	Rs.1,100
14 sold goods to Raju	Rs.250
15 Bought furniture for cash	Rs.2,000
16 Bought furniture from JFA furniture mart	Rs.800
17 Goods returned to GK stores	Rs.200
18 Raju returned goods worth	Rs.100
19 Drew for private use	Rs.500
20 Electric charges amounted to	Rs.120

Solution :

JOURNAL ENTRIES

Date	Particulars	L.F	Debit Rs	Credit Rs.
2008 Jan 11	Purchase a/c Dr. To Cash (Being cash purchase made)		1,500	1,500
“ Jan 12	Purchase a/c Dr. To GK stores (Being credit purchase made)		900	900
“ Jan 13	Cash a/c Dr. To sales (Being cash sales made)		1,100	1,100
“ Jan 14	Raju a/c Dr. To sales (Being credit sales made)		250	250
“ Jan 15	Furniture a/c Dr. To cash (Being the furniture purchase for cash)		2,000	2,000
“ Jan 16	Furniture a/c Dr. To JFA furniture mart (Being the furniture purchase on credit)		800	800
“ Jan 17	GK stores a/c Dr. To Purchase return (Being the goods returned to GK stores)		200	200
“ Jan 18	Sales return a/c Dr. To Raju (Being the goods returned from Raju)		100	100

“ Jan 19	Drawing a/c To cash (Being the cash drew for private use)	Dr.	500	500
“ Jan 20	Electric charges a/c To cash (Being electric charges paid)	Dr.	120	120
	Total		7,470	7,470

Illustration :2

Journalise the following transactions in the books of shanthi.

2009,june

3 purchase of furniture and payment by cheque	Rs. 5,000
8 Sold goods to Arvind	Rs.4,000
10 Goods purchased from Lal	Rs. 7,000
12 Goods returned to Lal	Rs. 1,000
15 Goods returned by Arvind	Rs. 200
18 Cash received from Arvind	Rs.3,760
Discount allowed to him	Rs. 40
21 withdrew from bank for private use	Rs.1,000
21 withdrew from bank for use in the business	Rs. 5,000
25 paid telephone rent for two months	Rs.500
28 Cash paid to Lal in full settlement of his account	Rs. 5,940
30 Paid for: stationery Rs. 200	
Rent Rs.1,000	
Salaries to staff Rs.2,500	

Solution :

JOURNAL OF SHANTHI

Date	Particulars	L.F	Debit Rs	Credit Rs.
2009 June 3	Furniture a/c To Bank (Being purchases of furniture and payment made by cheque)		5,000	5,000
“ June 8	Arvind a/c To Sales a/c (Being goods sold to Arvind on credit)		4,000	4,000
“ Jun 10	Purchases a/c To Lal (Being credit purchase from Lal)		7,000	7,000

“ Jun 12	Lal a/c To Returns outwards a/c (Being goods returned to Lal)	Dr.	1,000	1,000
“ Jun 15	Return Inwards a/c To Arvind a/c (Being goods sold returned by Arvind)	Dr.	200	200
“ Jun 18	Cash a/c Discount a/c To Arvind (Being the furniture purchases on credit)	Dr. Dr.	3,760 40	3,800
“ Jun 21	Drawings a/c Cash a/c To Bank (Being cash withdraw from bank for personal use and for use in the business)	Dr. Dr.	1,000 5,000	6,000
“ Jun 25	Telephone rent a/c To cash (Being payment of telephone rent made)	Dr.	500	500
“ Jun 28	Lal a/c To Cash a/c To discount a/c (Being cash paid to Lal for credit purchase on 10th and discount allowed by him)	Dr.	,000	5,940 60
“ Jun 30	Stationary a/c Rent a/c Salary a/c To cash a/c (Being electric charges paid)	Dr. Dr. Dr.	200 1,000 2,500	3,700
	Total		37,200	37,200

Illustration :3

Journalies the following transaction in the books of Gery :

1997 Jan

- | | |
|--|------------|
| 1 Started business with cash | Rs. 4,500. |
| 1 Paid Into Bank | Rs.2,500. |
| 2 Goods Purchased For Cash | Rs. 1,500 |
| 3 Purchase Of Furniture And Payment By Cheque | Rs. 500 |
| 5 Sold Goods For Cash | Rs. 600 |
| 8 Sold Goods To Arvind | Rs. 400 |
| 10 Goods Purchasesd From Amrit | Rs. 700 |
| 12 Goods Returned To Amrit | Rs.100 |
| 15 Sold Goods To Ram Swaroop For Cash | Rs. 250 |
| 18 Cash Received From Arvind Rs.396 And Discount Allowed To Him Rs.4 | |

21	Withdrew From Bank For Private Use	Rs.100
21	Withdrew From Bank For Use In The Business	Rs.500
25	Paid Telephone Rent For One Year	Rs.40
28	Cash Paid To Amrit In Full Settlement Of His Account	Rs.594
30	Paid For: Stationery	Rs. 20
	Rent	Rs.100
	Salaries To Staff	Rs.250

Solution :

JOURNAL ENTRIES

Date	Particulars	L.F	Debit Rs	Credit Rs.
1997 Jan 1	Cash a/c Dr. To capital account (Being cash brought in to start business)		4,500	4,500
“ Jan 1	Bank a/c Dr. To Cash a/c (Being cash paid into bank)		2,500	2,500
“ Jan 2	Purchase a/c Dr. To Cash a/c (Being goods purchased for cash)		1,500	1,500
“ Jan 3	Furniture a/c Dr. To Bank a/c (Being purchases of furniture and payment made by cheque)		500	500
“ Jan 5	Cash a/c Dr. To sales a/c (Being the goods sold for cash)		600	600
“ Jan 8	Arvind a/c Dr. To sales a/c (Being the goods sold for credit)		400	400
“ Jan 10	Purchase a/c Dr. To Amrit (Being credit purchase)		700	700
“ Jan 12	Amrit a/c Dr. To Return outwards a/c (Being the goods returned)		100	100
“ Jan 15	Cash a/c Dr. To sales a/c (Being goods sold for cash)		250	250
“ Jan 18	Cash a/c Dr. Discount a/c Dr. To Arvind a/c (Being Rs. 396 received from Arvind and Rs.4 discount allowed to him)		396 4	400
“ Jan 21	Drawing a/c Dr. Cash a/c Dr. To Bank a/c (Being cash withdrew from bank for personal use and for use in the business)		100 500	600

“ Jan 25	Telephone Rent a/c To Cash a/c (Being payment of Telephone Rent)	Dr.		40	40
“ Jan 28	Amrit a/c To Cash a/c To discount a/c (Being cash paid to Amrit and discount allowed to him)	Dr.		600	594 6
“ Jun 30	Stationary a/c Rent a/c Salaries a/c To cash a/c (Being cash paid for stationery, rent , salaries)	Dr. Dr. Dr.		20 100 250	370

LEDGER

As seen already, journal records all business transactions separately and as per the order of date of the transactions. The transactions pertaining to a particular person, asset or expense, are recorded at different places in the journal as they occur on different dates. Hence, journal fail to bring the similar transactions together and it's not useful for any reference . In order to have a consolidated view of the similar transactions the transactions entered in the journal will have to be posted to the Ledger Accounts. Ledger is the book of Main entry and its contains various accounts such as personal Accounts ,Real Accounts and nominal Accounts A Ledger accounts is nothing but a summary statement of all transactions relating to a person, asset, expense or income which have taken place during a given period of time showing their net effect

The rulings of each account in the ledger is as follows:

NAME OF ACCOUNT

Dr

Cr

Date	particular	J.F	Amount Rs.	Date	particular	J.F	Amount Rs
	To Name of Credit A/c				By Name of Debit A/c		

Each account in the ledger is divided into two equal parts. The left hand side is the debit side and the right hand side is the credit side. Each of the two is further divided in to four columns for recording the date of the transactions, the name of the account to be credited or debited, folio and the amount of the transaction .J.F. stands for folio (page number) in the journal or the subsidiary books from where the posting to the account is made.

Rules Regarding posting:

The following rules should be followed while posting transactions in the ledger:

- i) Separate account should be opened in the Ledger for posting transactions relating to the separate persons, assets, expenses or losses as shown in the Journal.
- ii) The concerned account which has been debited in the journal should also be debited in The Ledger. However , a reference should be made of the other account which has to Be credited in the journal. In other words, in the account to be debited the name if the Other account which is to be credited is entered in the debit side for giving a meaning To this posting. The debit posting is prefixed by the word 'To.

- iii) Similarly , the concerned account which has been credit in the journal should be credited in the Ledger. But a reference should be given of the account which has been debited in the journal. In other words , in the account to be credited name of the other account which has been debited is entered in the credit side. The credit posting is prefixed by the word 'By'.

For example, for salaries paid Rs. 1,000 in January 31, 1997, salaries account in the ledger should be debited and cash account should be credited.

Dr				salaries Account				Cr.			
Date	particular	J.F	Amount Rs.	Date	particular	J.F	Amount Rs				
1997 Jan 31	To cash a/c		1,000								

Dr				Cash Account				Cr.			
Date	particular	J.F	Amount Rs.	Date	particular	J.F	Amount Rs				
				1997 Jan 31	By salaries		1,000				

Balancing of an Account :

The various transaction entered in the journal in the chronological order are posted to the concerned ledger accounts as explained above. At the end of a period (say a month , a quarter or a Year), the account will have to be closed in order to find out the position shown by it. This is done by totaling the debited and credited of the account separately and finding the difference . The difference is entered on the side which is smaller and this difference is the ' closing balance ' shown by the account and this will be carried forward to the next year as the ' opening balance' in the account. This process is known as ' Balancing the Account.' If the debite side total is greater than the credit side the difference is entered on the credit side to close the account for the period and the balance is known as 'debit' balance. If the credit side total is greater , the difference will become a 'credit, balance.

Illustration :1

Journalise the following transactions, post them in the ledger and balance the accounts as on 31st December,1998.

1 Rajini started business with a capital of	Rs.50,000
2 He purchased furniture for	Rs.5,000
3 He bought goods on credit from vinod for	Rs.8,000
14 He sold goods to suresh for	Rs.5,000
15 He received cash from suresh	Rs. 3,000
18 He purchased goods for cash	Rs. 12,000
27 He sold goods for cash	Rs. 8,000
28 He paid Rent	Rs.1,200
31 He paid vinod Rs. 3,000 on account.	

Solution :

JOURNAL ENTRIES

Date	Particulars	L.F	Debit Rs	Credit Rs.
1998 Dec 1	Cash account a/c Dr. To capital account (Being capital Introduced)		50 ,000	50,000
“ Dec 2	Furniture a/c Dr. To Cash a/c (Being furniture purchased for cash)		5,000	5,000
“ Dec 3	Purchase a/c Dr. To vinod a/c (Being purchase of goods on credit)		8,000	8,000
“ Dec14	Suresh a/c Dr. To Sales a/c (Being credit sales)		5000	5000
“ Dec15	Cash a/c Dr. To suresh a/c (Being cash received)		3,000	3,000
“ Dec18	Purchases a/c Dr. To cash a/c (Being cash purchases)		12,000	12,000
“ Dec27	Cash a/c Dr. To sales a/c (Being cash sales)		8,000	8,000
“ Dec27	Rent a/c Dr. To Cash a/c (Being Rent paid)		1,200	1,200
“ Dec27	vinod a/c Dr. To Cash a/c (Being cash paid to vinod)		3,000	3,000

LEGER

Dr

Cash Account

Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 1	To capital a/c		50,000	1998 Dec 2	By furniture A/c		5,000
Dec 15	To suresh a/c		3,000	Dec 18	By purchasesA/c		12,000
Dec 27	To sales a/c		8,000	Dec 27	By Rent A/c		1,200
				Dec 31	By vinod A/c		3,000
				Dec 31	By balance c/d		39,800
			61,000				61,000
1999 Jan 1	To balance b/d						

Dr **Rajini's capital Account** Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 31	To Balance c/d		50,000	1998 Dec 1	By Cash A/c		50,000
			50,000				50,000
				1999 Jan 1	By balance b/d		50,000

Dr **Furniture Account** Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 2	To cash a/c		5,000	1998 Dec 31	By balance c/d		5,000
			5,000				5,000
1999 Jan 1	To Balance b/d		5,000				

Dr **Purchases Account** Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 3	To vinod a/c		8,000	1998 Dec 31	By balance c/d		20,000
Dec 18	To cash a/c		12,000				20,000
			20 ,000				
1999 Jan 1	To Balance b/d		20,000				

Dr **Sales Account** Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 31	To Balance c/d		13,000	1998 Dec 14	By Suresh a/c		5,000
			13,000	" 27	By Cash A/c		8,000
							13,000
				1999 Jan 1	By balance b/d		13,000

Dr

Vinod Account

Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 31	To cash		3,000	1998 Dec 1	By purchasesA/c		8,000
	To Balance c/d		5,000				8,000
			8,000				
				1999 Jan 1	By balance b/d		5,000

Dr

Suresh Account

Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 14	To sales a/c		5,000	1998 Dec 15	By Cash a/c		3,000
			5,000	“ 31	By balance c/d		2,000
							5,000
1999 Jan 1	To Balance b/d		2,000				

Dr

Rent Account

Cr.

Date	particular	J. F	Amount Rs.	Date	particular	J.F	Amount Rs
1998 Dec 28	To cash a/c		1,200	1998 Dec 31	By balance c/d		1,200
			1,200				1,200
1999 Jan 1	To Balance b/d		1,200				

TRIAL BALANCE**Meaning:**

A trial Balance is the list of balance extracted from the ledger account prepared to check the arithmetic accuracy of accounts.

Objects / Advantages of Trial Balance:

- i) The trial balance is prepared to check the arithmetic accuracy of accounts.
- ii) Errors in the accounts are disclosed. But there are some errors that are not disclosed by trial balance.
- iii) It is useful in the preparation of the final account.
- iv) It helps to prepare the trading, profit and loss account.
- v) It also helps to prepare the Balance sheet.
- vi) It is the lucid form of the accounts prepared.

Define “Trial Balance”

Trial Balance can be defined as “ a list of all balance standing on the ledger Accounts and cash books of a concern at any given time”

Prepared the Trial Balance:

As the balance are to be extracted from the ledger accounts, first go to the ledger accounts of each and every head of accounts, see the amount appearing in the ‘balance b/d , and the side it appears.

Post it to the Trial Balance by writing the name of account to the respective side. Now total the debit column and credit column in the Trial Balance. Both the totals should tally with each other if not verify the posting, Totaling , carry forward and transferring to the Trial Balance.

For this purpose, the following rules are worth remembering.

Debit Balances	Credit Balance
Assets	Liabilities
Expenses	Income
Losses	Gains
Drawings	Capital
Opening stock	Reserves
	Provisions

The Various Methods of preparing Trial Balance?

There are two methods in preparing Trial Balance .they are:

- (i) Balance Method (ii) Total Method

(i) Balance Method :

This method is used in preparing the Trial balance from the ledger account. Under this method the ledger account are balanced and the balance is carried forward to Trial balance. The excess of debit over credit is called debit balance and written in the debit column of the Trial balance and the excess of credit over debit is called credit balance and written on the credit side of the Trial Balance. Both the debit side and the credit side of the Trial Balance total should tally

(ii) Total Method:

Under this method, the total of the debit side and the credit side of every ledger account is separately written in the debit and credit of the Trial Balance.

SOLVED PROBLEMS:

Illustration : 1

From the under mentioned balances, prepare a Trial Balance as on 31.3.2007.

Particular	Rs	Particular	Rs
Cash in hand	4,800	Furniture	60,000
Purchases	4,80,000	Bills receivable	80,000
Opening stock	1,40,000	Salaries	80,000
Sundry creditors	96,000	Capital	4,00,000
Machinery	2,40,000	Bills payable	88,000
Wages	64,000	Sundry debtors	2,00,000
Sales	8,04,800	Rent	40,000

Solution :**Trial Balance as on 31.3.2007**

Name of Accounts	Debit Rs.	Name of Accounts	Credit Rs.
Cash in hand	4,800	Sundry creditors	96,000
Purchases	4,80,000	Sales	8,04,800
Opening stock	1,40,000	Capital	4,00,000
Machinery	2,40,000	Bills payable	88,000
Wages	64,000		
Furniture	60,000		
Bills receivable	80,000		
Salaries	80,000		
Sundry debtors	2,00,000		
Rent	40,000		
Total	13,88,800	Total	13,88,800

Illustration : 2

The following balances are extracted from the books of Kalidas you are required to prepare the trial balance as on 31.03.2009

Particular	Rs	Particular	Rs
Purchases	20,000	Miscellaneous Income	400
Purchases returns	800	Bills payables	7,000
Sales	30,000	Bills receivables	11,000
Sales returns	1,000	Cash in hand	1,800
Capital	30,000	Sundry creditors	4,000
Interest (Dr)	400	Discount earned	800
Wages	7,000	Sundry debtors	15,000
Rent	800	Commission (Dr)	1,000
Telephone charges	1,000	Plant and machinery	8,000
		Cash at bank	6,000

Solution :**Trial Balance of Mr.Kalidas as on 31.3.2009**

Name of Accounts	Debit Rs.	Name of Accounts	Credit Rs.
Purchases	20,000	Purchases returns	800
Sales returns	1,000	Sales	30,000
Wages	7,000	Miscellaneous Income	400
Rent	800	Capital	30,000
Telephone charges	1,000	Sundry creditors	4,000
Bills receivables	11,000	Discount earned	800
Cash at bank	6,000	Bills payables	7,000
Cash in hand	1,800		
Sundry debtors	15,000		
Commission	1,000		
Plant and machinery	8,000		
Interest	400		
Total	73,000	Total	73,000

Bank Reconciliation Statement

Meaning:

A bank reconciliation statement is a statement prepared to reconcile the bank balance as per cash book and pass book. This statement explains the reasons for the disagreement of balances between these two books, on any given date.

Before knowing the rules for the preparation of a bank reconciliation statement, the operation of cash book and pass book must be understood.

Cash book :

cash book is maintained by the customers. The bank transaction are entered in the column of the cash book. If cash /cheque is deposited in the bank , the bank column is debited. If expenses are paid through cheque or any cheque is issued, then bank a/c is credit in the cash book.

- i) If cash / cheque is deposited 'Bank' a/c is debited and bank balance increases.
- ii) If cheque issued , 'Bank' a/c is credited and bank balance decreases.
- iii) Favourable balance shows debit balance in cash book .
- iv) Unfavourable balance shows credit balance in cash book.

Pass book:

A pass book is the record of the transaction between a customer and bank , which is maintained by the banker.

If cash/cheque is deposited by the customers, the banker credits the pass book and the balance increases.

If cheque has been issued, the banker debits the pass book and the balance decreases.

Difference between cash book and pass book :

		Cash Book	Pass Book
i)	Maintained by	Customer	Banker
ii)	If cash cheque is deposited	Debited	Credited
iii)	If cheque has been issued or presented	Credited	Debited
iv)	If debited	Balance increases	Balance decreases
v)	If credited	Balance decreases	Balance increases
vi)	Favorable balance	Debit balance	Credited balance
vii)	unfavorable balance or overdraft	Credit balance	Debited balance

Procedure for the preparation of Bank Reconciliation statement :**I. Favourable balance from cash book to pass book and overdraft or unfavorable balance from pass book to cash book**

Balance as per cash Book / overdraft as per pass book		xxx
ADD:		
i) Cheque issued but not presented for payment	Xxx	
ii) Interest credited by the bank not entered in the cash book	xxx	
iii) Dividend , interest on investment collected by the bank not entered in the cash book	Xxx	
iv) Direct payment by customer into the bank	Xxx	
v) Any other items which decrease the balance in cash book	Xxx	
vi) Any wrong entry on credit side of the pass book	Xxx	Xxx
		Xxx

LESS :		
i) Cheque deposited into the bank but not yet collected	Xxx	
ii) Debits in pass book only (bank charges , insurance premium paid etc....)	Xxx	
iii) Insurance premium paid by the bank	Xxx	
iv) Bills received and discounted but informed as dishonored.	Xxx	
v) Any other item which increases the cash book balance	Xxx	
vi) Any wrong entry on the Dr. side of the cash book	Xxx	Xxx
Balance as per pass book / Overdraft as per cash book		xxx

If the total items to be deducted are more than the added balance, the negative balance is taken as overdraft as per pass book or Balance as per cash book.

II. Favorable balance from pass book to cash book and unfavorable or over draft balance from cash book to pass book

In order to find out the (favourable) balance of the cash book from the pass book and the unfavorable balance of the pass book from the cash book above ‘added’ items are ‘deducted ‘ and the ‘deducted’ items are ‘added’

Balance as per pass Book / overdraft as per cash book		Xxx
ADD:		
i) Cheque deposited into the bank but not yet collected	Xxx	
ii) Debits in pass book only (bank charges , insurance premium paid etc....)	Xxx	
iii) Insurance premium paid by the bank	Xxx	
iv) Bills received and discounted but informed as dishonoured.	Xxx	
v) Any other item which increases the book balance	Xxx	
vi) Any wrong entry on the Dr. side of the cash book	Xxx	Xxx
		Xxx
LESS:		
i) Cheque issued but not presented for payment	Xxx	
ii) Interest credited by the bank not entered in the cash book	xxx	
iii) Dividend , interest on investment collected by the bank not entered in the cash book	Xxx	
iv) Direct payment by customer into the bank	Xxx	
v) Any other items which decrease the balance in cash book	Xxx	
vi) Any wrong entry on credit side of the pass book	Xxx	Xxx
Balance as per pass Book / overdraft as per cash book		Xxx

SOLVED PROBLEMS:

Illustration : 1

From the following particulars of Mr. Kalidass, prepare a bank reconciliation statement as on 31-12-2010.

- Balance as per cash book on 31-12-2008 was Rs.15,000.
- Cheque for Rs.6,000 were deposited on 25th December. but collected in January 2009.
- Cheque for Rs.3,000 were issued in December out of which only cheques for Rs. 2,000 were presented for payment in December 2008.
- Banker has debited bank charges of Rs. 25 for which no entry has been made in cash book.

Solution:**Bank Reconciliation Statement of Mr.kalidass as on 31-12-2010.**

Particular	Rs	Rs
Bank balance as per Cash Book		15,000
ADD : i) cheque issued but not presented for Payment (3000 -2000)		1,000
		16,000
LESS : i) cheque deposited into the bank but not yet collected	6,000	
ii) Bank charges debited in pass book but not entered in cash book	25	6025
Bank balance as per pass book		9975

Illustration : 2

From the following particulars prepare a bank reconciliation statement as on 31-12-2011.

i)	Balance as per Cash Book	Rs.5,877.
ii)	Cheques issued but not presented for payment	Rs.2,013
iii)	Cheques deposited but not cleared upto 31 st December 31-12-2011	Rs.1,419
iv)	Banker had wrongly debited the firm's a/c of Which was rectified in January	Rs.225

Solution:**Bank Reconciliation Statement of Mr.kalidass as on 31-12-2011.**

Particular	Rs	Rs
Bank balance as per Cash Book		5,877
ADD : i) cheque issued but not presented for Payment.		2,013
		7,890
LESS : i) cheque deposited but not cleared	1,419	
ii) Amount wrongly debited	225	1644
Bank balance as per pass book		6246

Illustration : 3

on June 30, 1998, my Pass Book Account No.1 showed a balance of Rs.8,500. I had drawn cheques for Rs.2,800 on June 25 out of which Rs.1,000 only had been entered in the pass Book before June 30. Rs. 5,200 paid in by me on June 28 was wrongly credited to my No.2A/c , cash for a Bills Receivable for Rs.500 was collected by the bankers on June 27, but on corresponding entry was made in the Cash Book . A payment of Rs. 600 from my No.2 A/c has been wrongly debited by the bankers to this account. The bankers have also recovered a fire insurance claim of Rs. 1,200, their charges and commission on the same being Rs.50, the entries for which were made only in the Pass Book. A wrong credit of Rs. 250 relating to some other account appeared in the Pass Book . prepare a Reconciliation Statement as on June 30, 1998, of Bank Account No.1.

Solution:**Bank Reconciliation Statement of Account No.1 as on June30, 1998.**

Particular	Rs	Rs
Bank balance as per Pass Book		8,500
ADD : i) cash paid in but wrongly credited to No.2 Account	5,200	
Wrong debit by the banker to No.1 A/c	600	
Charges and commission debited in the Pass Book only	50	5,850
		14,350
LESS : Cheque issued but not presented for Payment(Rs.2,000-Rs.1,000)	1,800	
Cash collected by the bank bills Receivable Entered in Pass Book	500	
Fire insurance claim received by the banker credited in the Pass Book but not entered in the cash Book	1,200	
wrong credit appearing in No. 1 Account	250	3,750
Bank balance as per Cash book		10,600

UNIT –II

RECTIFICATION OF ERRORS

Meaning of Errors :

An error is a mistake committed in the books of account by the employee of an organization without any purpose.

The Following are the different types of errors:

- i) Error of principle ii) error of Omission
 - iii) Error of commission iv) Error of Duplication
 - v) Error of compensation (or) Offsetting error
-
- i) **Error Of Principle :** when the transaction are entered in the books of account without knowing the accountancy principles properly , it is error of principle . This error would not affect the Trial Balance.
For example : Purchase of Machinery is wrongly debited to 'purchase account' Instead of 'Machinery a/c'.
 - ii) **Error Of Omission :** This error arises when a transaction is omitted to be recorded in the books of account. This error also does not affect the Trial Balance.
For example : If the purchase of goods from Mohan is left unrecorded it is error of omission.
 - iii) **Error Of commission :** when the amount of a transaction is wrongly entered it is called an error of commission.
For example : If rent paid Rs.325 is entered as Rs.235 it is an error of commission . if this error is committed while posting to ledger ,the trial balance would not tally.
 - iv) **Error Of Duplication :** when a transaction is entered twice in the books of accounts, it is error of duplication . This error also would not affect the trial balance .
 - v) **Error Of Compensation or Offsetting error:** The error that compensates another error is an error of compensation.
For example: The excess debit of Rs.100 is compensated by the excess credit of Rs.100.

suspense Account :

suspense account is a temporary account opened to transfer the difference, if the trial balance does not agree with each side.

When the trial balance does not tally , there is some error and pending detection of error. In case the errors are detected after preparing trial balance but before preparing the final statements , they are rectified by journal entries and the suspense account is cancelled.

Solved Problems :

One –side errors :

Illustration: 1

Rectify the following errors:

- a) Purchases book is overcast by Rs.500.
- b) Sale book has been undercast by Rs.300
- c) Purchases returns book has been overcast by Rs.50
- d) Sales returns book has been undercast by Rs.75

Solution :

Rectifying Journal Entries

	Particular	Debit Rs.	Credit Rs.
a)	Suspense a/c Dr. To purchases a/c (Being the error of overcasting of purchases book rectified)	500	500
b)	Suspense a/c Dr. To sales a/c (Being under casting of sales rectified)	300	300
c)	Purchase return a/c Dr. To suspense a/c (Being overcasting of purchases return book rectified)	50	50
d)	Sale Return a/c Dr. To suspense a/c (Being under casting of sales return book rectified)	75	75

Illustration: 2

- i) an entry for the goods sold for Rs.102 to vasan was posted to his account as Rs.120
- ii) Rs.200 being the monthly total of discount allowed to customers was credited to discount account in the ledger.
- iii) Rs.2,700 paid by vasan were credited to sohan's account.
- iv) Rs.250 appearing the cash book as paid for the purchase of stationery for office use has not been posted to Ledger.
- v) The debit side of purchase account was under cast by Rs.600.

You are required to make the necessary journal entries.

Solution :

Rectifying Journal Entries

	Particular	Debit Rs.	Credit Rs.
i)	Suspense a/c Dr. To Vasan a/c (Entry for rectifying excess posting)	18	18
ii)	Discount a/c Dr. To Suspense a/c (Entry for rectifying wrong credit to discount a/c)	400	400
iii)	Sohan a/c Dr. To vasan a/c ((Entry for rectifying wrong posting)	2,700	2,700
iv)	Stationery a/c Dr. To suspense a/c ((Entry for rectifying omission of posting)	250	250
v)	Purchase a/c Dr. To suspense a/c (Entry for rectifying shot totaling)	600	600

TWO –SIDE ERRORS

Illustration: 3

Give the necessary entries to correct the following errors found in the books of paul & sons .

- i) Rs.5,000 paid in cash for a typewriter was charged to office expenses.

- ii) Rs.1,500 paid for furniture purchase has been charged to purchases account .
- iii) Repairs made were debited to building account for Rs.3,000

Solution :

Rectifying Journal Entries

	Particular	Debit Rs.	Credit Rs.
i)	Wrong entry : Office expenses a/c Dr. To cash a/c Correct Entry : Typewriter a/c Dr. To cash a/c Rectifying Entry: Typewriter a/c Dr. To Office expenses a/c (Entry for rectifying wrong debit of office expenses)	 5,000 5,000 5,000 5,000	 5,000 5,000
ii)	Wrong entry : Purchases a/c Dr. To cash a/c Correct Entry : Furniture a/c Dr. To cash a/c Rectifying Entry: Furniture a/c Dr. To Purchases a/c (Entry for rectifying wrong debit)	 1,500 1,500 1,500	 1,500 1,500
iii)	Wrong entry : Building a/c Dr. To cash a/c Correct Entry : Repairs a/c Dr. To cash a/c Rectifying Entry: Repairs a/c Dr. To Building a/c (Entry for rectifying wrong debit)	 3,500 3,000 3,000	 3,000 3,000

BOTH SIDE ERRORS :

Illustration: 4

Rectify the following errors:

- i) Purchase of Rs. 1,000 from Karthik wrongly entered in the sales book.
- ii) Goods taken by the proprietor Rs. 2,000 not recorded in the books at all.
- iii) Salaries paid to Ramesh Rs. 3,000 debited to his personal a/c.
- iv) Discount Rs.100 allowed to sunder has been credited to discount a/c.
- v) Credit sales to Ramu Rs.3,000 wrongly posted to the credit of his a/c.

Solution :**Rectifying Journal Entries**

	Particular	Debit Rs.	Credit Rs.
i)	Wrong entry : Karthik a/c Dr. 1,000 To sales a/c 1,000 Correct Entry : Purchase a/c Dr. 1,000 To Karthik a/c 1,000 Rectifying Entry: Sales a/c Dr. 1,000 Purchase a/c Dr. 1,000 To Karthik a/c 2,000 (Being the error of principle rectifying)		
ii)	Drawings a/c Dr. 2,000 To purchases a/c 2,000 (Entry for goods by the proprietor)		
iii)	Salaries a/c Dr. 3,000 To Ramesh A/c 3,000 (Entry for rectifying the wrong debit)		
iv)	Discount a/c Dr. 200 To Suspense A/c 200 (Being the wrong credit rectified)		
v)	Ramu a/c Dr. 3,000 Ramu a/c Dr. 3,000 To suspense a/c 6,000 (Being wrong posting rectifying)		

SUSPENSE ACCOUNT :**Illustration: 5**

The Trial Balance of a trader is out by excess debit of Rs.217. The following errors were discovered:

- The sales day book for the month of September had been under cast by Rs.300.
- Discount allowed of Rs.46 has been posted to the credit of discount received account as Rs.64
- Wages of Rs.69 for the erection of shelves in the warehouse had been debited to wages a/c as Rs.96.
- Defective furniture and fittings costing Rs. 124 returned to furniture supplier Ltd. Has been recorded in the books as goods purchased .
- The cost of a new van Rs. 5,000 had been debited to purchases account.
- A payment of Rs.120 for repairs to Motor van had been debited to Motor van's Account.

You are required to rectify the above errors and prepare the suspense account.

Solution :**Rectifying Journal Entries**

	Particular	Debit Rs.	Credit Rs.
a)	Suspense a/c Dr. To Sales a/c (Being under casting of sales book rectified)	300	300
b)	Discount received a/c Dr. Discount allowed a/c Dr. To suspense a/c (Being wrong posting rectified)	64 46	110
c)	Shelvas a/c Dr. Suspense a/c Dr. To Wages a/c (Being the error of principle rectified)	69 27	96
d)	Furniture supplier Ltd. a/c Dr. Furniture supplier Ltd. a/c Dr. To Furniture & fittings . a/c To purchase a/c (Being the error of principle rectified)	124 124	124 124
e)	Van a/c Dr. To Purchase a/c (Being the error of principles rectified)	5000	5000
f)	Repairs a/c Dr. To Motor Van's a/c (Being the error of principles rectified)	120	120

Dr

SUSPENSE ACCOUNT

Cr.

particular	Amount Rs.	particular	Amount Rs
To sales	300	By Balance b/d	217
To wages	27	By Discount received	64
		By Discount allowed	46
	327		327

FINAL ACCONT WITH ADJUSTMENTS**The term 'Final Account :**

The term 'final account ' means statement which result finally from the preparation of accounts. It shows the profit earned or loss suffered by the firm.

The objectives of preparing final accounts:

- To know the business results.
- To know the soundness of the business.
- To know the financial position of the business.
- To know the true and fair view of assets and liabilities.

Type of Adjustment	Adjusting Journal Entry	How deal with in	
		Trading a/c (or) Profit & Loss a/c	Balance sheet
1) closing stock	Stock a/c Dr. To Trading a/c	Credit side of Trading a/c	Assets side
2) interest on capital	Interest on capital a/c Dr. To capital a/c	Debit side of P&L a/c Interest a/c	Added to capital on liabilities side
3) interest on Drawings	Capital a/c Dr. To interest on drawing a/c	Credit side of P&L a/c	Deduct from capital along with drawings
4) Goods taken by the proprietor for personal use	Drawing a/c Dr. To purchases a/c	Deduct it from purchases as drawings of goods in Trading a/c	Deduct it from capital as goods taken for personal use.
5) Loss by Fire	Insurance co., a/c Dr. P&L a/c Dr. To Trading a/c	I) show the value of stock lost in the credit side of Trading a/c II) show the actual loss (total loss – insurance claim) in the debit side of P&L a/c	Show the insurance claim accepted in the asset side.
6) Goods distributed as free samples	Advertisement a/c Dr. To Purchases a/c	Deduct from purchase in the Trading a/c	Show in the debit side of the P&L a/c as free samples (or) advertisement expense.
7) Manager's commission	P&L a/c Dr. To commission payable	Debit side of the P&L a/c	Liabilities side as commission payable .
8) Depreciation on Assets	Depreciation a/c Dr. To Assets a/c	Debit side of the P&L a/c	Deduct from the value of the assets .
9) Bad Debts	Bad debit a/c Dr. To sundry debtors a/c	Debit side of the P&L a/c	Deduct from sundry debtors
10) Reserve for Bad and Doubtful Debts	P&L a/c Dr. To RBDD a/c	Debit side of the P&L a/c	The amount of new reserve alone is deducted from sundry debtors.

COMMISSION ON THE NET PROFIT :

i) Before charging such commission :

$$\text{Commission payable} = \frac{\text{profit} \times \% \text{ of commission}}{100}$$

ii) After charging such commission :

$$\text{Commission payable} = \frac{\text{profit} \times \% \text{ of commission}}{100 + \text{Rate of commission}}$$

PROFIT & LOSS ACCOUNT :**PROFIT & LOSS ACCOUNT****For the year ending**

Particulars		Debit Rs.	Particulars	Credit Rs.
To Bad Debts (as in Trial Balance) Add: Bad Debts (as in adjustment)	Xxx Xxx			
	Xxx			
To Reserve for Bad and Doubtful Debts (as in adjustment)	Xxx			
Less : Reserve for Bad and Doubtful Debts (as in Trang Balance)	Xxx	Xxx		
	xxxx	xxx		

BALANCE SHEET :**BALANCE SHEET as on**

Liabilities	Assets		
	Sundry Debtors	Xxx	
	Less: Bad Debts (as in adjustment)	Xxx	
	Less: Reserve for Bad & doubtful Debts (as in adjustment)	Xxx	Xxx
		Xxx	
		xxx	xxx

SOLVED PROBLEMS:**Illustration : 1**

Give suitable adjustment entries and show their effect on final accounts for the following transactions (assuming accounting year ends by December 31).

- Rs.500 p.m. is said as salaries to an Employee , but during the year 2002, Rs.5,000 are paid as salary . Three month's salary which is due but paid is Outstanding.
- A fire insurance policy is taken for a year paying Rs. 2,000 as insurance premium on 1st July 2002, which is to expire on 30th June 2003.
- A business has invested Rs.20,000 in 6% goverment securities on 1.1.2002 but during the year Rs. 700 has been received as interest on securities.

- iv) A building has been given to a tenant on Rs. 6,000 p.a. but during the year on amount of Rs. 7,500 has been received.

Solution :

JOURNALS ENTRYYS

Date	Particulars	L.F	Debit Rs	Credit Rs.
i)	Salary a/c (500x3) Dr. To outstanding salary a/c (Rs. 15,000 added with salary in the P&L a/c and O/s salary is shown as liability in the Balance sheet)		1,500	1,500
ii)	Premium paid in advance a/c Dr. To insurance premium a/c (Rs. 1,000 is deducted from the insurance premium in the P&L a/c and insurance premium a/c is show as asset in the Balance sheet)		1,000	1,000
iii)	Outstanding interest a/c Dr. To interest received a/c (Rs. 500 added with interest received in P&L a/c and O/s interest is shown as asset in the Balance sheet)		500	500
iv)	Rent received in advance a/c Dr. To Rent received a/c (Rs. 1,500 is deducted from rent received in P&L a/c (Cr.) and Received advance a/c is show as liabilities in the Balance sheet)		1,500	1,500

Illustration : 2

The following are the balance extracted from the books of Thiru. Muniyasamy as on 31.12.2006. prepare Trading and profit and loss a/c for the year ended 31st December,2006 and a Balance sheet as on that date.

Debit Balance	Rs	Credit Balance	Rs
Opening stock	20,000	Capital	1,00,000
Machinery	40,000	Purchases returns	1,000
Purchases	70,000	Sales	90,000
Sales returns	1,000	Creditors	29,000
Wages	2,000		
Salaries	5,000		
Office rent	2,000		
Insurance	1,000		
Debtors	50,000		
Cash	4,000		
Bank	25,000		
	2,20,000		2,20,000

Adjustment:

- | | |
|-------------------------------|------------|
| a) Closing stock is valued at | Rs.20,000. |
| b) Outstanding salaries | Rs. 1,000. |
| c) Bad debts | Rs. 1,000. |

d) Prepared insurance

Rs.500

e) Provide 10% depreciation on machinery .

Solution :

TRADING ACCOUNT OF THIRU.MUNIYASAMY

For the year ended 31.12.2006

Particulars	Debit Rs	Particulars	Credit Rs.
To opening stock	20,000	By sales 90,000 Add: Return 1,000	89,000
To purchase 70,000 Less : Return 1,000	69,000	By Closing stock	20,000
To wages	2,000		
To Gross profit c/d	18,000		
	1,09,000		1,09,000

PROFIT AND LOSS ACCOUNT OF THIRU.MUNIYASAMY

For the year ended 31.12.2006

Particulars	Debit Rs	Particulars	Credit Rs.
To salaries 5,000 Add: outstanding 1,000	6,000	By Gross profit b/d	18,000
To office Rent	2,000		
To Insurance 1,000 Less: prepaid 500	500		
To Bad debts	1,000		
To Depreciation on machinery	4,000		
To Net profit	4,500		
	18,000		18,000

BALANCE SHEET AS ON 31.12.2006

Liabilities	Rs.	Assets	Rs.
Capital 1,00,000 Add: Net Profit 4,500	1,04,500	Cash	4,000
Creditors	29,000	Bank	25,000
Outstanding salary	1,000	Prepaid insurance	500
		Debtors 50,000 Less: Bad debts 1,000	49,500
		Closing stock	20,000
		Machinery 40,000 Less : depreciation 40,000x10/100 4,000	36,000
	1,34,500		1,34,500

UNIT III

BILLS OF EXCHANGE

Meaning :

It is a document used in commercial transaction for monetary dealings. They are freely transferable and had a good title. These documents are made payable to order/bearer” and the provisions of the Negotiable instruments Act 1881 is applied.

Define :

As per section 5 of Negotiable Instruments Act 1881 “It is an instrument in writing containing an unconditional order. Signed by the maker, directing a certain person, to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument”.

Features of bill of exchange :

The following are the features of bill of exchange:

- a) It is an instrument in writing.
- b) It is an unconditional order.
- c) It is an order to pay a definite sum of money.
- d) It should be signed by the maker or drawer.
- e) The payee must be certain and his name must be mentioned in the instrument.
- f) There are three parties Drawer, Acceptor and payee.
- g) It certain money only , not goods and the amount should be specified .
- h) It direct a person or the bearer of the order .
- i) It is paid within a stipulated time.

Define promissory Note.

As per section 4 of Negotiable Instrument Act,1881 “It is an instrument in writing containing an unconditional undertaking , signed by the maker to pay a certain sum of money only to, or the order of a certain person or to the bearer of the instrument” .

Who is called “Drawer” “Acceptor” and “payee”?

Drawer: He is the seller/ creditor of the goods and prepare a bill on his debtor He put his signature on the bill and sent it to his debtor for acceptance after acceptance he received the bill Hence for him it is “Bills Receivable”.

Acceptor : He is the purchaser/debtor of the goods and he accept the bill drawn by the seller and return It to drawer He pay the bill to the drawer hence for him it is “Bills payable” He is also known as “ Drawee ”

payee: The person who is entitled to payment of the amount mentioned in the bill.

BILL OF EXCHANGES AND PROMISSORY NOTE

	Bill of Exchange	Promissory Note
1.	It is prepared by creditor	It is prepared by debtor
2.	It has three parties, “Drawer, Drawee and payee”	It has two parties Drawer and payee.
3.	It is an order to pay	It is a promise to pay
4.	It is used in trading activities	It is used to borrow money
5.	It must be accepted by the drawee for validity.	It need not accepted, since the debtor himself prepare it .
6.	Demand bill not requires stamp duty.	Promissory note requires stamp duty.
7.	One copy for inland bill and three copies for foreign bills are drawn.	Only one copy is prepared
8.	Widely used in business	Not so common.

Various kinds of bills

Bills may be classified into

- a) Inland bills
- b) foreign bills
- c) Time bills
- d) Demand bills
- e) Trade bills
- f) Accommodation bills

The terms “Discounting “ and “ Endorsing “ a bill

Discounting the Bills: The drawer of the bill instead of keeping the bill with him, discount the bill with banker and obtained cash. The process of transfer ownership to the banker is known as “Discounting of Bills”.

When a bill is discounted the banker does not make full payment, they calculate interest for the period and deduct the interest. The interest is charged to the discount account. The drawer is liable to pay the amount incase the acceptor is unable to pay on the date.

Endorsing the Bills: The process of transaction the bills received by the drawer to another person is known as endorsement. The drawer can make use of his bill to settle his debt with another person. Here the drawer is termed “Endorser” and the person who received the bill is known as “Endorsee”. The drawer (endorser) is liable to the endorsee and the acceptor is liable to drawer in case of bills dishonoured. A bill can be endorsed any number of times till due date.

The term Bills dishonoured “and Noting Charges”.

Dishonour of Bills : on the date of maturity, the acceptor is unable to pay the money of refused to accept the bill is known as dishonour of bill. Dishonour of bill makes the drawer liable to compensate the amount to the banker (discounted bill) and the endorsee (endorsed bill) When the bill is dishonoured, notice of dishonour must be given to the drawer and endorser.

Nothing Charges : on maturity, the acceptor fails to pay the dues the holder of the bill (drawer / banker / endorsee) handover the bill to the “Notary Public” officer, who represent the bill to the acceptor and note down the dishonour in his register. This is known as “Noting”. The Notary public issue a dishonour notice. Which is attached with the bill. The recording of dishonour is called “ **Protest**”. It is a documentary proof under Negotiable Instrument Act.

The Notary public is charging an amount for his service of nothing a bill is known as “Noting Charges”. The acceptor of the bill is liable to pay the noting charges to the drawer .

Books of Drawer	Books of Acceptor
i) Goods sold and purchased on credit: Debtor/customer a/c Dr. To Sales a/c	Purchased a/c To creditor /supplier a/c
ii) Bill of drawn and accepted: Bill Receivable a/c Dr. To Acceptor a/c	Drawer a/c To Bills Payable a/c
iii) Bill is discounted , endorsed and sent for collection: Bank a/c Dr. Discount a/c Dr. (Or) Endorsee a/c Dr. (or) Bills sent for collection a/c Dr. To Bills Receivable a/c	No Entry
iv) Bill is honoured / discharged : Cash a/c Dr. To Bills Receivable a/c (Note: No entry for the bills discounted and endorsed)	Bill Payable a/c Dr. To cash a/c
v) Bill is collected by bank: Bank a/c Dr. To Bill sent for collection a/c	No Entry
vi) Bill is dishonoured : Acceptor a/c Dr. To Bills Receivable a/c (or) To Bank a/c (or) To Endorsee a/c (or) To Bill sent for collection a/c	Bills Payable a/c Dr. To Drawer a/c
vii) Renewal of Bill :	

<p>a) Cancel old bill Acceptor a/c Dr. To Bills Receivable a/c</p> <p>b) Interest : Acceptor a/c Dr. To Interest a/c</p> <p>c) Interest / partial repayment received in cash : Cash a/c Dr. To Acceptor a/c</p> <p>d) Drawer new Bill: Bills Receivable a/c Dr. To Acceptor a/c</p>	<p>Bills Payable a/c Dr. To Drawer a/c</p> <p>Interest a/c Dr. To Drawer a/c</p> <p>Drawer a/c Dr. To Cash a/c</p> <p>Drawer a/c Dr. To Bills Payable a/c</p>
<p>viii) Retiring a Bill : Cash a/c Dr. Discount a/c Dr. To Bills Receivable a/c</p>	<p>Bills Payable a/c Dr. To Cash a/c To Discount a/c</p>
<p>ix) Acceptor become insolvent: a) Dishonour of Bill Acceptor a/c Dr. To Bill Receivable a/c</p> <p>b) Dividend received from acceptor's estate: Cash a/c Dr. Bad debts a/c Dr. To Acceptor a/c</p>	<p>Bills Payable a/c Dr. To Drawer a/c</p> <p>Drawer a/c Dr. To cash a/c</p>

Bill Honoured :-

Illustration :1

On March 10th, A sold goods to B and draw a bill at three months for Rs. 800, which B accepts immediately and return it to A. The Bill is honoured on the due date. Pass entries in the books of both A and B.

Solution :

A'S JOURNAL (Drawer or Maker)

Date	Particular	Amount Rs.	Amount Rs.
March 10	B Account Dr. To sales a/c (Being credit sales made to B)	800	800
March 10	Bills Receivable a/c Dr. To B Account (Being acceptance received)	800	800
March 10	Cash Account Dr. To Bills Receivable a/c (Being amount received)	800	800

B'S JOURNAL (Acceptor or Drawer)

Date	Particular	Amount Rs.	Amount Rs.
March 10	Purchases a/c Dr. To B Account a/c (Being credit purchases made)	800	800
March 10	A Account a/c Dr. To Bills Payable a/c (Being acceptance given)	800	800
June 13	Bills Payable a/c Dr. To Cash Account (Being acceptance met)	800	800

BILL DISHONoured :-**Illustration :2**

Mr.kali draws a Bill for Rs.2,000 on Madhan on 15th September for three months. On maturity , Madhan fallied to honour the Bill. Pass the necessary journal entries in the books of kali and madhan, if he had retained the bill with him til maturity .

KALI 'S JOURNAL

Date	Particular	Debit Rs.	Credit Rs.
Sep 15	Bills Receivable a/c Dr. To Madhan a/c (Being acceptance received)	2,000	2,000
Dec 18	Madhan a/c Dr. To Bills Receivable a/c (Being Bill dishonoured at maturity)	2,000	2,000

MADHAN 'S JOURNAL

Date	Particular	Debit Rs.	Credit Rs.
Sep 15	Kali a/c Dr. To Bills Payable a/c (Being acceptance given)	2,000	2,000
Dec 18	Bills Payable a/c Dr. To Kali a/c (Being acceptance dishonoured at maturity)	2,000	2,000

RENEWAL OF BILL:-**Illustration :3**

Vasan having accepted a bill from Muniyasamy for Rs. 6,000 finds that he will be unable to honour it on maturity. Before the due date , he requests Muniyasamy to receive Rs.3,300 in cash (Rs.300 Being interest) and to draw on him a new bill for Rs.3,000 for further period of 3 months and to cancel the old bill Muniyasamy agrees to his proposal Make journal entries in the books the parties to record the above transaction.

Solution:**VASAN 'S JOURNAL (Drawer)**

Particular	Debit Rs.	Credit Rs.
Bills Receivable a/c Dr. To Vasan a/c (Being acceptance received)	6,000	6,000
Vasan a/c Dr. To Bills Receivable a/c (Being old Bill cancelled)	6,000	6,000
Vasan a/c Dr. To interest a/c (Being interest for renewal)	300	300
Cash a/c Dr. To Vasan a/c (Being part amount of bill with interest received)	3,300	3, 300
Bills Receivable a/c Dr. To Vasan a/c (Being new bill for 3 months received)	3,000	3,000

MUNIYASAMY 'S JOURNAL (Acceptor)

Particular	Debit Rs.	Credit Rs.
Muniyasmy a/c Dr. To Bills Payable a/c (Being bill accepted)	6,000	6,000
Bills Payable a/c Dr. To Muniyasamy a/c (Being old Bill cancelled before the due date)	6,000	6,000
Muniyasamy a/c Dr. Interest a/c Dr. To cash a/c (Being part Payment of the old bill and Rs. 300 given as interest)	3,000 300	3, 300
Muniyasmy a/c Dr. To Bills Payable a/c (Being new bill accepted for 3 months)	3,000	3,000

RETIRINF A BILL :-**Illustration :4**

on 1st January, a sold goods to B for Rs.1,000 and drew upon him a bill at three months for the amount. B accepted the bill and returned it to A. On 4th March; B returned the bill under rebate of 12% p.a.

Record these transaction in the journal of A and B.

Solution :

A'S JOURNAL (Drawer)

Date	Particular	Amount Rs.	Amount Rs.
Jan 1	B Account Dr. To sales a/c (Being goods sold on credit)	1,000	1,000
Jan 1	Bills Receivable a/c Dr. To B Account (Being acceptance received)	1,000	1,000
Mar 4	Cash Account Dr. Rebate a/c Dr. To Bills Receivable a/c (Being Bill honoured under rebate)	990 10	1,000

Note: Rebate is given for the period between settlement date (4th March)and actual due date (4th April), that is 1 month.

$$\text{Rebate} = \text{Rs.}1,000 \times 12/100 \times 1/12 = 10$$

B'S JOURNAL (Acceptor)

Date	Particular	Amount Rs.	Amount Rs.
Jan 1	Purchases a/c Dr. To A Account a/c (Being purchase of goods on credit)	1,000	1,000
Jan 1	A Account a/c Dr. To Bills Payable a/c (Being acceptance given)	1,000	1,000
Mar 4	Bills Payable a/c Dr. To Cash Account To Rebate a/c (Being acceptance met under rebate)	1,000	990 10

UNIT IV

ACCOUNTS OF NON-TRADING CONCERNS

Non- Trading Concerns:

Non- Trading concerns of association are those concerns which are established for the purpose of rendering services to the public. They are also called as non-profit motive concerns or organization E.g. school, colleges , Library , Sports Clubs, social club , Hospitals etc.

The Accounts that are prepared by Non-Trading concerns :

As Non-trading association are non-profit originations. They do not prepare Trading and Profit and Loss a/c like a business or trading organization. But in order to know the closing cash and bank balance and the surplus or deficit, they prepare the following books of accounts.

- a) Receipts and payments a/c
- b) Income and Expenditure a/c and
- c) Balance sheet.

Receipts and Payment accounts with its general format:

It is a summary of cash transactions under various heads, prepared at the end of the year to know the nature of the transaction. Both the Capital Revenue receipts and payment are entered here. It take into account the receipts and payments relating to previous , current and subsequent year. It starts with opening balance and ends with closing balance. It is just like a cash book. For example, the total subscription received during the year is shown on the receipts side of the Receipts and Payments a/c and the salary, rent paid etc., appear on the payment side of the Receipts & Payments a/c . The format of a Receipts & Payment a/c is given below.

Format:-

RECEIPTS & PAYMENTS A/C For the year ended 31st March 2009

Dr.			Cr.		
Date	particular	Amount Rs.	Date	particular	Amount Rs
1.4.09	To Balance b/d:			By honorarium	Xxx
	Cash	Xxx		By Rent	Xxx
	Bank	Xxx		By Interest	Xxx
31.03.09	To subscription	Xxx		By Sports expenses	Xxx
	To Entrance fees	Xxx			
	To sale of old Newspaper	xxx	31.03.09	By Balance c/d:	
				Cash	Xxx
				Bank	Xxx
		xxx			xxx

Income Expenditure and General Format :

Income and Expenditure a/c is the summary of incomes and expenditure of the whole year. It is like a profit and loss account prepared on accrual basis, to find out the surplus or deficit. Unlike the receipt and payment account. The income and expenditure accounts takes into account only the revenue expenditures and receipts. Also it take into account of the expenditure , and income of the whole year, whether paid/ received or not. The format of a income &Expenditure account is given below:

INCOME AND EXPENDITURE a/c
For the year ended 31st March 2006

Expenditure	Rs.	Income	Rs
To Rent xxx Add: O/s for the current Year xxx Less : O/s of the previous year Lees: prepaid during the current Year Add: paid in advance in the previous year To salary To Depreciation on fixed assets To surplus of excess of income over expenditure (B/F)*	Xxx Xxx Xxx Xxx	By subscription xxx Add: O/s for the current Year xxx Less : O/s of the previous year Lees: prepaid during the current Year Add: paid in advance in the previous year By sports receipts By sale of news paper By deficit or Excess of expenditure over income (B/F)*	Xxx Xxx Xxx Xxx
	xxx		xxx

Receipts & payments Account And Income & Expenditure :

	Receipts & Payment a/c	Income & Expenditure a/c
1.	It is a summary of cash transaction	It is a summary of Income and Expenditures
2.	It is a Real A/c	It is a Nominal A/c
3.	It is like a cash book	It is like a profit& Loss a/c
4.	It starts with opening balance of cash and bank	It does not start with opening balance.
5.	All receipts are entered on the debit side.	All Incomes are entered on the credit side.
6.	All Payments are entered on the credit side.	All Expenditure are entered on the debit side.
7.	It takes into account both revenue and capital receipts.	It takes into account only the revenue income.
8.	It takes into account both revenue and capital expenditure.	It takes into account only the revenue expenditure .
9.	It take into account the receipts relating to previous , current and subsequent years.	It takes into account the incomes relating to current years only whether received or not.
10.	It takes into account the payments relating to previous , current and subsequent years.	It takes into account the expenditure relating to previous years only whether paid or not.
11.	The purpose is to find either the opening or closing balance of cash /bank	The purpose is to find either surplus or deficit.
12.	It ends with the closing balance of cash and	It does not end with closing balance.

	Bank	
--	------	--

Illustration :1

From the following information of APJ Sports Club of Calculate you are required to prepare the Receipt and payment a/c for the year ended 31st March 2006.

Balance on 1.4.2005

Cash	5,000
------	-------

Bank	3,000
------	-------

Transaction during the year:

Entrance fee	4500	Honororiuon paid	8000
Donation	27000	Billiard table purchased	40000
Legacy	16000	Sports meet collection	18000
Life membership	6080	Sports expenses	12000
Rent Paid	9000	Interest paid	5600
Stationary purchased	1800	Purchase of news paper	1000
Subscription		Sale of news paper	600
2004-05	5800	Balance on 31.03.06:	
2005-06	37000	Cash	2500
2006-07	3200		

Solution :

RECEPITS & PAYMENT a/c OF APJ SPORTS CLUB
for the year ended 31.03.2006

Receipts	Rs.	Payments	Rs.
1.4.05		31.3.06	
To Balance b/d: cash	5,000	By Rent	9,000
: Bank	3,000	By stationery	1,800
		By honorarium	8,000
31.3.06		By purchase of billiard table	40,000
To Entrance Fee	4,500	By sports expenses	12,000
To Donation	27,000	By interest	5,600
To Legacy	16,000	By news papers	1,000
To Life membership fee	6,080	By Balance c/d :	
To subscription		Cash	2,500
2004-05 5,800		Bank(B.F)	46,280
2005-06 37,000			
2006-07 3,200			
	46,000		
To sports meet collection	18,000		
To sale of news paper	600		
	1,26,180		1,26,180

Illustration :2

From the information given below prepare on income and expenditure a/c for 2006.

Receipts	Rs.	Payments	Rs.
Opening Balance in hand	200	Salaries	4,800
at Bank	1,600	Rent	500
subscription		Stationary & postage	200
2005 0,500		Bicycle purchased	300
2006 8,300		National saving certificates	3,000
2007 0,600		Help to poor student	2,000
		Closing Balance	
	9,400	in hand 300	
Sale of investments	2,000	at bank <u>2400</u>	2,700
Sale of old furniture (Book value Rs.400)	300		
	13,500		13,500

Subscription for 2006 still receivable was Rs. 700, interest due on saving certificates Rs.100 and rent unpaid but due was Rs.60.

Solution :

**INCOME AND EXPENDITURE a/c
for the year ended 2006**

Expenditure	Rs.	Income	Rs.
To salaries	4,800	By subscription 2006 8300	
To Rent 500		Add: O/s subscription for 700	
Add O/s 60			9,000
	560	By Accrued interest on N.S.C	100
To stationery and postage	200		
To Help to poor students	2,000		
To Loss on sale of old (furniture 400-300)	100		
To excess of income over Expenditure (surplus)(B.F)	1,440		
	9,100		9,100

CONSIGNMENT ACCOUNT

Consignment :

Consignment signifies an agency arrangement under which a manufacturer or a wholesaler sends his goods at his own risk to his agent, in a different place for the purpose of sale.

Distinguish between a consignment and a sale:

	Consignment	Sale
1.	Legal ownership is not transferred to the consignee .	Legal ownership is transferred to the Purchaser
2.	The relationship between the seller consignor and the purchaser consignee is owner and agent.	The relation the seller and the purchase is creditor and debtor .
3.	Expenditure on consignment is borne by the consignor.	Expenses after sale is borne by the purchaser
4.	Risk on consignment lies with the consignor.	Risk on sale lies with the purchaser

Overriding commission :-

Ordinary commission is calculate as per terms agreed between consignor and consignee. In addition to the ordinary commission, sometimes an extra commission is allowed to the consignee, in case the sales exceed a specific amount.

Meaning of ‘ proforma invoice :

Proforma invoices is a statement showing the quantity of the goods, its quality and the price of the goods send by consignor to the consignee on consignment .

Non-Recurring expenses:-

Expenses incurred to bring the consignment goods till it reaches of the god own of the consignee is known as non-recurring expenses.

Value the unsold (closing) stock under consignment account:-

In general closing stock is value at cost price. Under consignment account. The unsold stock in the hands of consignee are valued by the consignor with cost plus proportionate non recurring expenses.

Treat normal and abnormal loss in consignment account**Normal loss:**

Loss arises due to natural causes like evaporation drying, breaking in bulk, loading and unloading of goods, cutting bulk material into small parts etc., are known as normal loss.

Abnormal Loss:

Loss of goods in transit, thefts, goods destroyed by fire careless handing etc. are known as abnormal loss. It is also known as avoidable loss. The loss will be debited to abnormal loss account.

- i) When loss arised :
Abnormal loss a/c Dr.
 To consignment a/c
- ii) If the risk is not insured :
 Profit and loss a/c Dr.
 To abnormal a/c
- iii) If the risk is insured:
 Insurance claim a/c Dr.(for the amount claimed)
 Profit and loss a/c Dr. (for the balance loss)
 To Abnormal Loss a/c

The invoice price method:

Sometimes the goods consigned to the consignee was charged at higher than the cost price. Which is known as invoice price. In such a case, the consignment account for the goods sent should be debited with invoice price.

- i) Adjustment for excessive price in the consignment account:
 Goods set on consignment a/c Dr .
 To consignment a/c
- ii) Adjustment for excessive price in unsold stock account:
 Consignment a/c Dr.
 To consignment stock Reserve a/c

iii) Consignment stock will appear in the Balance Sheet at Invoice price less stock reserve.

Consignment outwards and consignment inwards :

- I) Goods which are sent by the consignor to consignee, the consignment is referred to as consignment outwards.
- II) In consignment when goods are received by the consignee, it is termed as consignment inwards. It may be defined as , “the receipt of goods by consignee, to be sold on commission basis and at the risk of the consignor.”

Journal entries for consignment account:

Though there are two parties involved in consignment account. The journal entry is passed in the books of both the consignor and consignee they are:

In the books of

	Consignor	Consignee
a)	Goods sent on consignment Consignment a/c Dr. To good sent on consignment a/c (Being the value of the consignment)	No entry
b)	Expenses paid by consignor Consignment a/c Dr. To Cash/ Bank a/c (Being Expenses paid)	No entry
c)	Advance from consignee Cash /Bank a/c Dr. To consignee a/c (Being the advance received)	Consignor a/c Dr. To cash /Bank a/c To B/P a/c (Being the advance made)
d)	Expenses paid by consignee Consignment a/c Dr. To consignee a/c (Being expenses paid by consignee)	Consignor a/c Dr. To cash /Bank a/c (Being expense paid)
e)	Cash /credit sales by consignee Consignee a/c Dr. To consignment a/c (Being sale proceeds effected)	Cash a/c Dr. Debtors a/c Dr. To consignor a/c (Being cash /credit sale made)
f)	Commission due for consignee Consignment a/c Dr. To Consignee a/c (Being commission due)	Consignor a/c Dr. To commission a/c To Del-credere commission a/c (Being commission due)
g)	Collection of debts No entry	Bank /cash a/c Dr. To consignment debtors a/c (Being amount collectied)
h)	Bad debts (ordinary commission) Consignment a/c Dr. To consignee a/c (Being bad debts borne by consignee)	Consignor a/c Dr. To consignment Debtors a/c (Being bad debts on debtors)
i)	Bad debts Del-credere commission No Entry	Bad debts a/c Dr. To consignment debtors a/c (Being Bad debts on consignment)

j)	Unsold stock Consignment stock a/c Dr. To consignment a/c (Being unsold stock valued)	No Entry
k)	Excess price on consignment Goods sent on consignment a/c Dr. To consignment a/c (Being excess price on consignment adjusted)	No Entry
l)	Excess price on Unsold stock Consignment a/c Dr. To Consignment stock Reserve a/c (Being excess price on unsold stock adjusted)	No Entry
m)	Profit on consignment transferred Consignment a/c Dr. To profit and loss a/c (Being profit transferred)	No Entry
n)	Final settlement of consignee Cash /Bank a/c Dr. B/R Dr. To consignee a/c (Being balance due settled)	Consignor a/c Dr. To cash /Bank a/c To B/P a/c (Being balance due settled)
o)	Transfer of goods sent account Goods sent on consignment a/c Dr. To Trading /purchase a/c (Being the account transferred)	No Entry

Account sales :-

Illustration :1

On April 1,2003, Alpha Radio Limited of madras consigned to K.Kalidass, radio dealer at Coimbatore, 200 radio sets, invoice at Rs.300 per set. The cost of each set was Rs. 250 and Railway freight of Rs. 600 was paid by the consignor, other expenses being paid by the consignee. On 1st July 2003 K.Kalidass remitted an account sales showing that 160 sets have been sold at the price of Rs.300 per set. They deducted unloading charges and cartage of Rs.30 establishment expenses Rs.120 and commission at 5% on sales, remitting the draft for the balance. Make out an account sales.

Solution :

Account sales of 160 radio sets vide consignment dated 1st April 2003, sold by order and for account of Alpha Radio Limited:

Sale proceeds : 160 radio sets at Rs.300 per set	Rs.	Rs. 48,000
Less Charges: Unloading charges and cartage	30	
Establishment expenses	120	
Commission at 5% on Rs.48,000	2,400	2,550
		45,450
E&O.E. Coimbatore, July 1 st 2003		By K.Kalidass, Radio Dealer, Coimbatore.

COMMISSION :**Illustration :2**

Vasan cycles (P) Ltd. Hyderabad, sent 2,000 dynamos costing Rs.50 each for sale on consignment basis to Ram of Madras, subject to the following terms :

- i) Normal selling price per dynamo Rs.60
- ii) Consignee's commission to be calculated as under:
 - a) 5per cent on normal selling price .
 - b) 1 per cent additional commission, if selling price is more than normal price ; and
 - c) ½ per cent del-credere commission on total sales for guaranteeing collection of credit sales.

Ramoo reported sales as follows :

Cash sales : 500 dynamos at Rs.60 each	30,000
200 dynamos at Rs.75 each	15,000
Credit sales : 400 dynamos at Rs.75 each	30,000
400 dynamos at Rs.80 each	32,000
	<u>1,07,000</u>

Ascertain the commission due to consignee.

Solution :**Statement of commission due to consignee**

	Rs.
Normal (or simple) commission: $1,500 \times 60 \times 5/100$	4,500
Additional (or Overriding) commission: $77,000 \times 1/100$	770
Del –credere commission: $1,07,000 \times 1/2 \times 100$	535
	<u>5,805</u>

Valuation of unsold stock**Illustration :3**

on 1st January,2000. Rohit sends 150 sewing machines costing Rs. 30,000 to Anurag to be sold on behalf of the former at 5% commission on sales. Rohit paid Rs.1,500 as freight and carriage for sending the machines. Anurag sent the account sales on 31st March , 2000 standing That

- i) 120 sewing machines were sold for Rs.27,000
- ii) Expenses incurred on inward consignment were : octroi Rs.250:
Carriage Rs. 50, God won Rent Rs.2,100 and Advertisement and other selling Expenses Rs. 1,500.

Calculate the value of consignment stock on 31st March,2000.

Solution :

	Rs.
Normal of sewing machines consigned	150
Lee: Number of sewing machines sold	120
Number of machines unsold (i.e. consignment stock)	<u>30</u>
Cost price of 150 sewing machines	Rs. 30,000

Cost price of 30 machines	i.e. $\frac{30,000}{150} \times 30$	Rs. 6,000
Add: proportionate share of non-recurring expenses :	Rs.	
Freight and carriage incurred by Rohit on 150 machines	1,500	
octroi on 150 machines paid by Anurag	250	
carriage on 150 machines paid by Anurag	50	
	1800	
Therefore , expenses on 30 machines	$\frac{1,800}{150} \times 30$	Rs.360
Value of consignment stock		Rs.6,360

UNIT V

JOINT VENTURES

Meaning of joint venture :

Joint venture is a temporary partnership without any firm name. two or more persons joined to undertake and agreed to excess a specific work/business is known as joint venture.

Define a joint venture :

“when two or more persons join to- gather to conduct a trading operations and contribute capital in an agreed proportion and sharing the profit or loss arised” is known as joint venture .

The features / characteristic of a joint venture :

The essential feature of a joint venture can be as follows:

- i) It is a temporary partnership.
- ii) The partnership is for a specific venture (business) .
- iii) The partnership is credited without a firm name.
- iv) Co-venture agreed to contribute capital and share the profit/loss in the agreed ratio.
- v) The venture will be closed automatically when the transaction is completed.

Distinguish between consignment and joint venture :

	Consignment	Joint venture
a)	The relationship between consignment and consignee is principal and agent .	The relationship between co-venture are partners.
b)	Consignee is entitled to get commission only.	Co-venture share the profit and losses.
C)	Consignee has power to obey the consignor.	All the co-venture has equal powers.
D)	Nature of business is selling of goods only.	Nature of business may be for any activities.
E)	Capital is contributed by the consignor.	Capital is contributed by all the co-venture.
F)	It is governed by the agreement between consignor and consignee.	Besides agreement , provisions of partnership act binding the co-venture.

Journal entries under separate set of books maintained for the joint venture .

When a venture is big in nature a separate set of books to be maintained for each venture. It is prepared as per the double entry system.

JOURNAL ENTRIES

1) For capital contribution : Joint Bank a/c To co-venture's a/c (Being capital contributed by)	Dr.
2) For amount spent on expenses and purchases : Joint venture a/c To joint Bank a/c (Being purchases made /expenses paid)	Dr.
3) For goods supplied by co-venture : Joint venture a/c	Dr.

To co-venture a/c (Being goods supplied by)	
4) For credit purchase: Joint venture a/c To creditors a/c (Being goods purchased from...)	Dr.
5) Expenses paid by co-venture : Joint venture a/c To co-venture a/c (Being expenses paid by....)	Dr.
6) For sale made: Joint Bank a/c Debtors a/c To joint venture a/c (Being sale made)	Dr.(cash sales) Dr.(credit sales)
7) For unsold stock: Joint venture stock a/c To joint venture a/c (Being goods unsold kept in stock a/c)	Dr.
8) For unsold stock taken by the venture : Co-venture a/c To joint venture a/c (Being unsold stock taken by.....)	Dr.
9) For transfer of joint venture profit : Joint venture a/c To co-venture a/c (Being profit transferred to each co-venture)	Dr.
10) For settlement of co-venture account : Co-venture a/c To joint Bank a/c (Being amount settled to each co-venture)	Dr.

Journal entry, when only one co-venture keep the account of joint venture on behalf of all:

When a venture is small in nature there is no need of preparing a separate set of account for the venture.

JOURNAL ENTRY

1) For contribution by the other co-venture : Cash a/c To co-venture's a/c (Being contribution received from)	Dr.
2) For goods supplied and expenses paid by other co-ventures: Joint venture a/c To co-venture's a/c (Being goods supplied / expenses paid by ...)	Dr.
3) For goods supplied by the same co-venture ; Joint venture a/c To purchased a/c (Being goods supplied by ...)	Dr.
4) For purchase of goods and expenses paid : Joint venture a/c To cash a/c To creditors a/c (for credit) (Being goods purchased /expenses paid)	Dr.

5) For commission to the venture, who maintain the account : Joint venture a/c Dr. To commission a/c (Being commission due on venture)
6) For sales : Cash a/c Dr. Debtors a/c Dr. To joint venture a/c (Being sales realized)
7) For unsold stock : No Entry
8) For unsold stock taken by other co-ventures: Co-venture a/c Dr. To joint venture a/c (Being good taken by...)
9) For unsold stock taken by same co-ventures: Purchase a/c Dr. To joint venture a/c (Being goods taken by..)
10) for transfer of joint venture profit : Joint venture a/c Dr. To profit and loss a/c (same) To co-venture a/c (others)
11) for settlement to other co-venture : Co-venture a/c Dr. To cash /Bank a/c (Being amount settled to ...)

SOLVED PROBLEMS SEPARATE SET OF BOOKS

Illustration: 1

A and B enter into joint venture. A agrees to bring capital in cash accordingly a joint Banking account is opened by A for a sum of Rs.80,000 . B buys goods worth Rs.50,000 as part of his share of capital. Further goods worth Rs.1,18,000 were purchased from C paying Rs.60,000 and balance by a promissory note signed by A and B.

The goods were sent to calculate for sale. Expenses totaling Rs.5,000 were incurred in sending the goods. Part of goods were damaged and a sum of Rs. 25,000. Were recovered from the insurance company. The balance goods were sold for Rs.2,20,000.

Give journal entries to record the above transactions. Also prepare joint venture account. Joint Banking account and accounts of A and B assuming that the promissory note was duly honored.

Solution :

JOURNAL ENTRIES

	Particular	Debit Rs.	Credit Rs.
1)	Joint Bank Account a/c Dr. To A a/c (Being amount contributed by A)	80,000	80,000
2)	Joint venture a/c Dr. To B a/c (Being goods purchased by B for joint venture)	50,000	50,000

3)	Joint venture a/c To C a/c (Being goods purchased from C for joint venture)	Dr. 1,18,000	1,18,000
4)	C a/c To joint Bank a/c To Bills Payable a/c (Being payment made to C)	Dr. 1,18,000	60,000 58,000
5)	Joint venture a/c To Joint Bank a/c (Being expenses incurred for joint venture)	Dr. 5,000	5,000
6)	Joint Bank a/c To joint venture a/c (Being amount received from the insurance company for part of the goods damaged)	Dr. 25,000	25,000
7)	Joint Bank a/c To joint venture a/c (Being sales realized)	Dr. 2,20,000	2,20,000
8)	Bills payable a/c To joint Bank a/c (Being payment for promissory note due)	Dr. 58,000	58,000
9)	Joint venture a/c To A a/c To B a/c (Being profit on joint venture transferred)	Dr. 72,000	36,000 36,000
10)	A a/c B a/c To joint Bank a/c (Being payment made to co-venture in final settlement of their account)	Dr. Dr. 86,000 1,16,000	2,02,000

Illustration: 2

A,B and C enter into a joint venture to divide profit equally. They bought goods from D for Rs.1,25,000 and from A for Rs.25,000. A contributed Rs.30,000, B Rs.40,000 and C Rs.90,000 which amount were banked in a joint account . they settled their account with D by cheque and paid for carriage and other expenses for Rs.7,500. They sold goods for cash Rs.65,000 and to E on credit for 1,40,000 who accepted a draft for the amount. The acceptance was cashed and realized Rs. 1,37,000. A was allowed 5% commission on sales for effecting the transaction. Pass settlement between parties was made by cheques.

Solution :

JOURNAL ENTRIES

	Particular	Debit Rs.	Credit Rs.
1)	Joint Venture Account To D's a/c To A's capital a/c (Being goods purchased)	Dr. 1,50,000	1,25,000 25,000
2)	Joint Bank a/c To A's capital a/c To B's capital a/c To C's capital a/c (Being capital contributed by partners)	Dr. 1,60,000	30,000 40,000 90,000

3)	D's a/c To joint Bank a/c (Being payment for goods purchases)	Dr. 1,25,000	1,25,000
4)	Joint venture a/c To Joint Bank a/c (Being payment of carriage and expenses)	Dr. 7,500	7,500
5)	Joint Bank a/c E's a/c To Joint Venture a/c (Being sales in cash and credit)	Dr. Dr. 65,000 1,40,000	2,05,000
6)	Bills receivable a/c To E's a/c (Being E's acceptance of bill)	Dr. 1,40,000	1,40,000
7)	Joint Bank a/c Discount a/c To Bills Receivable a/c (Being the above bill discounted)	Dr. Dr. 1,37,000 3,000	1,40,000
8)	Joint venture a/c To Discount a/c (Being discount charges transferred)	Dr. 3,000	3,000
9)	Joint venture a/c To A's capital a/c (Being commission of A@ 5% on sales)	Dr. 10,250	10,250
10)	Joint venture a/c To A's capital a/c To B's capital a/c To C's capital a/c (Being distribution of joint venture profit)	Dr. 34,250	11,416.67 11,416.67 11,416.66
11)	A's capital a/c B's capital a/c C's capital a/c To joint Bank a/c (Being the final settlement among partners)	Dr. Dr. Dr. 76,666.67 51,416.67 1,01,416.66	2,29,500.00

**NO SEPARATE SET OF BOOKS
ONLY ONE CO-VENTURE KEEPS ACCOUNT**

Illustration:3

A of Bangalore enters into a joint venture with B of Bombay to ship cotton bales to C in Japan. A sends cotton of the value of Rs.30,000. Pays Railways freight etc. Rs. 1,500 and sundry expenses Rs.1,575. B sends goods valued at Rs.20,750 and pays freight and insurance Rs.1,200. Dock dues Rs.200; customs charges Rs.500 and other sundry expenses Rs.500. A advance to B Rs.6,000 on account of the venture. B received account sale and remittance of the net proceeds from C in Japan for the value of goods amounting to Rs.80,000. Show how joint venture transactions will be recorded in the books of A.

Solution :

JOURNAL ENTRIES

	Particular	Debit Rs.	Credit Rs.
1)	Joint Venture a/c To Cash Account a/c (Being goods purchased)	Dr. 30,000	30,000

Dr.		B ACCOUNT		Cr.	
Particular		Rs.	Particular	Rs	
To joint venture		80,000	By joint venture (goods)	20,750	
To cash (advance)		6,000	By joint venture (freight)	1,200	
			By joint venture (dock dues)	200	
			By joint venture (customs)	500	
			By joint venture (expenses)	500	
			By joint venture (profit)	11,887.50	
			By cash (settlement)	50,962.50	
		86,000		86,000	

Each Venture's Keeps Accounts:

Illustration:4

Raman and Laxman were participants in a joint venture sharing profit and losses in the proportion of 2/3 and 1/3 respectively. Each party maintains a complete record in his own books. Raman supplies goods to the value of Rs. 15,000 and incurs an expenditure of Rs.600 on them. And laxman supplies goods to the extent of Rs. 12,000 and his expenses thereon amount to Rs.900. Raman sells all the goods for Rs.36,000 for which he is entitled to receive commission at 5 per cent. Accounts are settled by bank draft. Give the necessary journal entries in the books of Raman to record the above transactions.

Solution :

RAMAN'S JOURNAL ENTRIES

	Particular	Debit Rs.	Credit Rs.
1)	Joint Venture A/c Dr. To purchases A/c To Bank A/c (Being goods supplied and expenses incurred)	15,600	15,000 600
2)	Joint Venture A/c Dr. To Laxman A/c (Being goods supplies for Rs.12,000 expenses and Rs.900 paid)	12,900	12,900
3)	Bank Account Dr. To Joint Venture Account (Being sales proceeds received)	36,000	36,000
4)	Joint Venture A/c Dr. To commission A/c (Being 5% commission on goods sold)	1,800	1,800
5)	Joint Venture Account Dr. To profit and loss A/c To Laxman A/c (Being profit on joint venture transferred)	5,700	3,800 1,900
6)	Laxman A/c Dr. To Bank Account A/c (Being amount settled to Laxman)	14,800	14,800

MEMORANDUM METHOD

Illustration:5

C of Calcutta and D of Delhi entered into a joint venture for the purpose of buying and selling second-hand motor cars, C to make purchases and D to effect sales. The profit or loss was to be shared as to C two fifths and D three-fifths. A sum of Rs.10,000 was remitted by D to C towards the venture.

C purchased 10 cars for Rs.8,000 paid Rs.4,350 for their reconditioning and sent them to Delhi. his other expenses were : Buying commission 2 ½ per cent and sundry expenses Rs.350.

D took delivery of the cars by paying Rs.750 for railway freight and Rs.375 for octroi. He sold four cars at Rs.1,600 each, two at Rs.1,800 each and three at Rs.2,250 each he retained the remaining car for himself at an agreed value of Rs.2,100 his expenses were: insurance Rs.150 Garage Rent Rs.250. Brokerage Rs.685 sundries Rs.450.

Each party's ledger contains a record of his own transactions on joint account prepare a statement showing the result of the venture and the account of the venture in each party's ledger as it will finally appear, assuming that the matter was finally settled between the parties.

Solution :

MEMORANDUM JOINT VENTURE ACCOUNT

Dr.			Cr.		
Particular		Rs.	Particular		Rs.
To C:					
Purchases	8,000		By D (sales)		
Reconditioning			4 cars @Rs.1,600		6,400
Charges	4,350		2 cars @Rs.1,800		3,400
Buying comm..	200		3 cars @Rs.2,250		6,750
(2 ½ % of Rs.8,000)					
Sundry expenses	350				
		12,900			
To D (Expenses)			By D (one car taken		
Railway freight			over)		2,100
Octroi					
Insurance	750				
Garage Rent	375				
Brokerage	150				
Sundries	250				
	685				
	450	2,260			
To profit transferred to					
C (2/5 share)					
D (3/5 share)	1,316	3,290			
	1,974				
		18,850			18,850

BOOKS OF C
JOINT VENTURE ACCOUNT WITH “D”

Dr.		Cr.	
Particular	Rs.	Particular	Rs.
To Bank Account (purchases)	8,000	By Bank Account	10,000
To Bank Account (Reconditioning charges)	4,350	By Bank (Amount received from D for settlement)(Bal.fig)	4,216
To Bank Account (Commission)	200		
To Bank Account (Expenses)	350		
To profit and loss Account (share of profit)	1,316		
	80,000		80,000

BOOKS OF D
JOINT VENTURE ACCOUNT WITH “C”

Dr.		Cr.	
Particular	Rs.	Particular	Rs
To Bank Account	10,000	By Bank (sales)	16,750
To Bank Account (Expenses)		By Vehicle Account (one car taken over)	2,100
Railway freight 750			
Octroi 375			
Insurance 150			
Garage Rent 250			
Brokerage 685			
Sundries 450	2,660		
To profit and loss account (share of profit)	1,974		
To Bank Account (Bal.fig.) (Amount remitted to C)	4,216		
	18,850		18,850

INSURANCE CLAIMS

Insurance Claims :

Any loss suffered by a business due to fire, theft, and loss of profit can be compensated by taking an appropriate policy with the insurance company.

In majority of the business house separate stock account is not maintained and at the end of the accounting year the stock taking is done in order to prepare the final accounts for the year.

However if there is an increase or decrease in trend is noted in the previous year's profit the trend is considered for fixing the gross profit rate the purposes of calculating the gross profit rate to be applied. For (e.g. if the gross profit for 1994-10% ,1995-15%, and for 1996-20%, then for the year 1997, the reasonable rate would be 25%.Similary the rate would be decreased where there is a decrease in trend in the previous years, profit.

Memorandum Trading Account

To opening stock	xxx	By sales	xxx
To purchases	xxx	By stock (Closing)	xxx
To wages	xxx	(Balance figure)	xxx
To gross profit	xxx		
	-----		-----
	xxx		xxx
	-----		-----

Value of stock on hand on the date of fire

Less: salvaged stock

Claim to be lodged

Illustration:1

A fire occurred on September 30,1998, in the go down of Mr.Vasan a from the following figures ascertain the claim to be lodged.

Stock on January 1,1998	Rs. 17,000.
Purchases from January 1,1998 to date of fire	Rs.1,70,000.
Wages and other manufacturing expenses	Rs.17,000.
Sales from January 1,1998 to date of fire	Rs.2,00,000.
The rate of gross profit is 25% on cost. The stock salvaged was valued at	Rs.4,000.

Memorandum Trading Account up to September 30,1998

Dr.

Cr.

Particular	Rs.	Particular	Rs.
To opening stock	17,000	By sales	2,00,000
To purchases	1,70,000	By closing stock	44,000
To wages and other manufacturing Expenses	17,000	(Balance figure)	
To Gross profit 25% on cost	40,000		
2,00,000x 25/125			
	2,44,000		2,44,000

Value of stock on hand on the date of fire .	44,000
Less: stock salvaged	4,000
Claim to be lodged	<u>40,000</u>

Consequential loss or loss of profit : In the event of fire , it not only destroys the properties but also affects the earning capacity of the business for same time due to decrease in the production rate. Decrease in production rate leads to decrease in sale and due to the shortage of sales the profit that would have been earned is also affected and the reduction in the profit is called loss or profit.

Indemnity period : Any period not exceeding twelve months from the date of damage during which the results of the business shall be affected due to fire is known as indemnity period.

Standard turnover : standard turnover refers the turnover effected in the preceding period corresponding to the indemnity period. This turnover is adjusted in the light of the trend in the current year.

Short sales: This is the difference between the, 'standard turnover' and the 'actual turnover' short sales refer to the loss of sales due to fire which has resulted in dislocation of the business.

Loss due to short sales: This is calculated by applying the rate of gross profit to short sales. The rate of gross profit is calculated in different ways for this purpose.

Rate of gross profit: here the term 'rate of gross profit' is not used in the sense as it has been understood commonly. It has different meaning in various circumstances and the same being explained as follows:

$$1. \text{ G.P. rate} = \frac{\text{Net Profit} + \text{Insured Standing Charges}}{\text{Turnover}} \times 100$$

Where there is net loss

$$2. \text{ G.P. rate} = \frac{\text{Insured Standing Charges} - \text{Net Loss}}{\text{Turnover}} \times 100$$

Where the amount of loss is arrived at as follows when only a portion of the standing charges are insured.

$$\frac{\text{Net loss} \times \text{Insured standing charges}}{\text{All standing charges}}$$

The Gross profit rate is calculated by taking the previous year's figures.

Increased cost of working : This expenditure is an additional expenditure incurred by the insured in order to carry on the business during the indemnity period. The insured is entitled to get such additional expenses subject to the lowest of the following two calculations:

$$1. \frac{\text{Net Profit} + \text{Insured Standing Charges}}{\text{Net Profit} + \text{All Standing Charges}} \times \text{Increased cost of working and}$$

$$2. \text{ Short sales avoided through increased cost of the working} \times \text{Rate of gross profit}$$

Saving in Expenses: Any saving in expenses will have to be deducted before arriving the claim for loss of profit and increased working expenses.

Illustration:2

From the following particulars, prepare a claim for loss of profit covering consequential loss:

- Accounts are prepared on 31st December, the profit for 1997 amounted to Rs.65,000 after debiting constant expenses totaling Rs. 75,000. Sales for 1997 were Rs. 11,20,000.
- Fire occurred on June 1, 1998. And affected sales for four months.
- Sales for four months ending Sept,30, in 1997 and 1998 were respectively Rs. 3,00,000 and Rs. 40,000.
- The policy was Rs. 2,00,000 the sale for the year ending on May 31,1998 were Rs.12,50,000.

Solution :

$$1. \text{ G.P. rate} = \frac{\text{Net Profit} + \text{Insured Standing Charges}}{\text{Turnover}} \times 100$$

$$= \frac{65,000 + 75,000}{11,20,000} \times 100$$

$$= 12.5\%$$

2. Calculation of short sales:

Standard Turnover during 1.6.97 to 30.09.97	Rs. 3,00,000
Less: sales during 1.6.98 to 30.9.98	Rs. 40,000
Shot Sales	<u>Rs. 2,60,000</u>

3. Loss of profit :

Short sales x Gross Profit Rate 2,60,000 x 12.5% Rs. 32,500.

4. Claim to be admitted:

Sales during the preceding 12 months	Rs. 12,50,000
Policy required for 12,50,000 @ 12.5%	Rs. 1,56,250
Policy taken for	Rs. 2,00,000

As the policy taken is sufficient, the claim admitted in full Rs. 32,000

Average Clause: As it has been explained already, the insured is entitled to get only a proportion of his claim. Where the policy covers a portion of the loss, this is ascertained by first calculating the amount of profit for which insurance policy ought to have been taken and then allowing the claim only proportionately.

1. Amount to be insured : Adjusted Turnover for the 12 months before fire x G.P. rate

2. Claim allowed loss x $\frac{\text{amount actually insured}}{\text{Amount ought to have been insured}}$

Illustration:3

Items related to the previous year :

Rate of gross profit	25%
	Rs.
Insured standing charges	10,000
Total standing charges	15,000
Net profit	25,000
Items related to the current year :	
Shot sales	20,000
Increased working expenses	2,000
Saving in expenses	750
Short sale avoided though increased cost of working	5,000
Amount of policy	20,000

Sales during 12 months immediately preceding the fire being Rs. 1,00,000 the sales of the current year up to the date of fire has increased by 10% over the sales of the same period in the previous year. Calculate the amount of claim to be admitted by the insurance company.

Solution :

Calculation of the allowable limit of the increased working expenses

$$1. \frac{\text{Net Profit} + \text{Insured Standing Charges}}{\text{Net Profit} + \text{All Standing Charges}} \times \text{increased working expenses}$$

$$= \frac{25,000 + 10,000}{25,000 + 15,000} \times 2,000 = 1,750$$

$$2. \text{Short sales avoided through increased cost of working} \times \text{Rate of G.P}$$

$$5,000 \times \frac{25}{100} = 1,250$$

Rs.1,250 being the lowest of the above calculation is allowed by the insurance company.

	Rs.
Loss profit due to short sales $20,000 \times \frac{25}{100}$	5,000
Increased working expenses	1,250
	<hr/> 6,250
Less: saving in expenses	750
Claim for loss of profit and increased working expenses	<hr/> 5,500
Sales during 12 months immediately preceding the fire	1,00,000
Add: increased in trend	10,000
	<hr/> 1,10,000

$$\text{Amount for which the policy should have been taken } 1,10,000 \left[\times \frac{25}{100} \right] 27,500$$

Amount of claim to be admitted by the insurance company:

$$\text{Amount of Claim} \times \frac{\text{Amount of Policy taken}}{\text{Amount of policy ought to have been taken}}$$

$$5,500 \times \frac{20,000}{27,000} = 4,000$$