Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 1 Accounting for Share Capital

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State which of the following statements are true
(a) A company is formed according to the provisions of Indian Companies Act, 1932.
Answer False
(b) A company is an artificial person.
Answer True
(c) Shareholders of a company are liable for the acts of the company.
Answer False
(d) Every member of a company is entitled to take part in its management.
Answer False
(e) Company's shares are generally transferable.
Answer True
(f) Share application account is a personal account.
Answer True
(g) The director of a company must be a shareholder.
Answer True
(h) Application money should not be less than 25% of the face value of shares.
Answer False
(i) Paid-up capital can exceed called-up capital. .
Answer True
(j) Capital reserves are created from capital profits.
Answer True
(k) Securities premium account is shown on the assets side of the balance sheet.
Answer False
(l) Premium on issue of shares is a capital loss.
Answer False
(m) At the time of issue of shares, the maximum rate of securities premium is 10%.

Answer False

(n) The part of capital which is called-up only on winding up is called reserve capital.

Answer True

(o) Forfeited shares can not be issued at a discount.

Answer False

(p) The shares originally issued at discount may be re-issued at a premium.

Answer True

Do it Yourself I

Question 1. On January 01, 2006, a limited company was incorporated with an authorised capital of Rs.40,000 divided into shares of Rs.10 each. It offered to the public for subscription of 3,000 shares payable as follows

	Rs.
On Application	3 per share
On Allotment	2 per share
On First Call (One month after allotment)	2.50 per share
On Second and Final Call	2.50 per share

The shares were fully subscribed for by the public and application money duly received on January 15, 2006. The directors made the allotment on February 1, 2006.

How will you record the share capital transactions in the books of a company if the amounts due has been duly received, and the company maintains the combined account for application and allotment.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Do it Yourself II

1. A company issued 20,000 equity shares of Rs.10 each payable at Rs.3 on application, Rs.3 on allotment, Rs.2 on first call and Rs.2 on second and the final call. The allotment money was payable on or before May 01, 2005; first call money on or before August Ist, 2005; and the second and final call on or before October Ist, 2005; 'X', whom 1,000 shares were allotted, did not pay the allotment and call money; 'Y', an allottee of Rs.600 shares, did not pay the two calls; and 'Z', whom 400 shares were allotted, did not pay the final call.
Pass journal entries and prepare the Balance Sheet of the company as on December 31, 2005.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. Alfa company Ltd. issued 10,000 shares of Rs.10 each for cash payable at Rs.3 on application, Rs.2 on allotment and the balance in two equal instalments. The allotment money was payable on or before March 3, 2006; the first call money on or before 30 June, 2006; and the final call money on or before 31st August, 2006. Mr. 'A', whom 600 shares were allotted, paid the entire remaining face value of shares allotted to him on allotment. Record journal entries in company's books and also prepare their balance sheet on the date.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Test your Understanding – II

Choose the Correct Answer.
(a) Equity share holders are :
(i) creditors
(ii) owners
(iii) customers of the company.
Answer (ii) Owners

(b) Nominal share capital is :
(i) that Part of the authorised capital which is issued by the company.
(ii) the amount of capital which is actually applied for by the prospective shareholders.
(iii) the maximum amount of share capital which a company is authorised to issue.

Answer (iv) the amount actually paid by the shareholders.

(**c) Interest on calls-in-arrears is charged according to "Table A" at :**
(i) 5%
(ii) 6%
(iii) 8%
(iv) 11%
Answer (i) 5%

(d) Money received in advance from shareholders before it is actually called-up by the directors is :
(i) debited to calls-in-advance account
(ii) credited to calls-in-advance account
(iii) debited to calls account.
Answer (ii) Credited to calls account

(e) Shares can be forfeited
(i) for non-paymnt of call money
(ii) for failure to attend meetings
(iii) for failure to repay the loan to the bank
(iv) for which shares are pledged as a security.
Answer (i) For non-paymntof call money

(f) The balance of share forfeited account after the reissue of forfeited shares is transferred to
(i) general reserve
(ii) capital redemption reserve
(iii) capital reserve
(iv) reveneue reserve
Answer (iii) Capital

(g) Balance of share forfeiture account is shown in the balance sheet under the item :
(i) current liabilities and provisions
(ii) reserves and surpluses
(iii) share capital account
(iv) unsecured loans
Answer (iii) Share capital account

Do it Yourself III
1. A company forfeited 100 equity shares of Rs.10 each issued at a premium of
20% for non-payment of final call of Rs.5 including the premium. Show the

journal entry to be passed for forefeiture of shares.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. A company forfeited 800 equity shares of Rs.10 each issued at a discount of 10% for non-payment of two calls of Rs.2 each. Calculate the amount forfeited by the company and pass the journal entry for forefeiture of the shares.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Do it Yourself IV

Excell Company Limited made an issue of 1,00,000 Equity Shares of Rs.10 each,
payable as follows :

	Rs.
On Application	**Rs.2.50 per share**
On Allotment	**Rs.2.50 per share**
On Ist and Final Call	**Rs.5.00 per share**

X, the holder of 400 shares did not pay the call money and his shares were forfeited. Two hundred of the forfeited shares were reissued as fully paid at Rs.8 per share. Draft necessary journal entries and prepare Share Capital and Share Forfeited' accounts in the books of the company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Test your Understanding – III

(a) If a Share of Rs. 10 on which Rs. 8 is called-up and Rs. 6 is paid is forfeited. State with what amount the Share Capital account will be debited.
(b) If a Share of Rs. 10 on which Rs. 6 has been paid is forfeited, at what minimum price it can be reissued.
(c) Allhuwalia Ltd. issued 1,000 equity shares of Rs. 100 each as fully paid-up in consideration of the purchase of plant and machinery worth Rs. 1,00,000. What entry will be recorded in company's journal.

Answer
(a) On forfeiture, share capital is debited with called up amount i.e.,X 8.
(b) The total price of money collected from 1st issue and reissue should be equal to face value atleast. It can exceed also. The share can be reissue for minimum ? 4 per share.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Do it Yourself V

Journalise the following :
(a) The directors of a company forfeited 200 equity shares of Rs. 10 each on which Rs. 800 had been paid. The Shares were re-issued upon payment of Rs. 1,500.
(b) A holds 100 shares of Rs. 10 each on which he has paid Re. 1 per share on application. B holds 200 Shares of Rs. 10 each on which he has paid Re. 1 on application Rs. 2 on allotment. C holds 300 shares of Rs. 10 each who has paidRe. 1 on applications, Rs. 2 on allotment and Rs. 3 on first call. They all failed to pay their arrears and second call of Rs. 4 per share as well. All the shares of A, B and C were forfeited and subsequently reissued at Rs. 11 per share as fully Paid-up.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

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Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Short Answer Type Questions

Question 1. What is public company?
Answer Minimum requirement of a public company is seven person. As per the Section 3 (1) (iv) of Companies Act 1956, public company is a company which (a) is not a private company, (b) has minimum capital of ?5 lakh or such higher paid-up capital as may be prescribed, and (c) is a private company which is a subsidiary public company.

Question 2. What is private limited company?
Answer As per Section 3 (1) (iii) of Companies Act 1956, A private company is one which has a minimum paid up capital of ^ 1 lakh or such higher paid-up capital as may be prescribed by its Articles
(i) Restricts the right to transfer its shares.
(ii) Limits the number of its members to fifty (excluding its employees).
(iii) Prohibits any invitation to the public to subscribe for any shares in or debentures of the company.

(iv) Prohibits any invitation or acceptance of deposits from person other than its members, directors and relatives.

Question 3. Define Government Company.
Answer Section 617 of Companies Act 1956 defines Government Company as a company in which not less than 51% of the paid up share capital is held by the Central Government or by any State Government or Governments or partly by the Central Government and partly by one or more State Governments and includes a company which is a subsidiary of a Government Company.

Question 4. What do you mean by a listed company?
Answer Listed companies are those companies whose shares are listed on a recognised stock exchange for public trading. When a company's security is listed in a recognised stock exchange the price fluctuation can easily be observed by the investor and he/she can easily determine the increase/decrease in value of their investment in a concerned listed company.
This is the only reason that the volume remain high in case of a listed company as all the moves can be observed and investment strategy can easily be planned in that company.

Question 5. What are the uses of securities premium?
Answer When securities like shares and debentures are issued to public more than their face value the excess is called security premium. As per the Section 78 of the Companies Act 1956, the amount of securities premium can be used by the company for the following purposes
(i) For paying up unissued shares of the company to be issued to members (shareholders) of the company as fully paid bonus share.
(ii) For writing off the preliminary expenses of the company.
(iii) For writing off the expenses of, or the commission paid or discount allowed on, any issue of shares or debentures of the company.
(iv) For paying up the premium that is to be payable on redemption of preference shares or debentures of the company.
(v) Further, as per the Section 77A, the securities premium amount can also be utilised by the company to buy-back its own shares.

Question 6. What is buy-back of shares?
Answer When a company repurchase its own share from the market to reduce the number of share it is called buy-back of shares. As per the Section 77A of the Companies Act, 1956 the procedure for buy back of share would be as follows
(i) First of all the Articles of the Association must authorise the company for the buy-back of shares.

(ii) A special resolution must be passed in the companies' Annual general body meeting.
(iii) The amount of buy-back of shares should not exceed 25% of the paid-up capital and free reserves.
(iv) The debt-equity ratio should not be more than a ratio of 2:1 after the buyback.
(v) All the shares of buy-back should be fully paid-up.
(vi) The buy-back of the shares should be completed within 12 months from the date of passing the special the resolution.
(vii) The company should file a solvency declaration with the Registrar and' SEBI which must be signed by at least two directors of the company. –

Sources for Buy-back of Share
(i) Free reserves.
(ii) Securities premium account.
(iii) Proceeds of any shares or other specified securities, provided that no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of the earlier issues of the similar kind of shares or specified securities.

Question 7. Write a brief note on 'Minimum Subscription'
Answer When shares are issued to the general public, it is necessary that the minimum subscription amount should be subscribed so that the company can allot shares to the applicants. This minimum amount of share subscription is termed as minimum subscription. As per the Company Act 1956, the minimum subscription of share cannot be less than 90% of the issued amount. If the minimum subscription is not received, the company cannot allot shares to its applicants and it shall immediately refund the entire application amount received to the public.
e.g., if a company issued 1,00,000 equity share than at least 90,000 share must be subscribed by the public.

Long Answer Type Questions

Question 1. What is meant by the word 'Company'? Describe i characteristics.
Answer According to Section 3 (1) (i) of the Company Act of 195 "Company means a company formed and registered under this Act or £ existing company."

In general, a company is an artificial person, created by law that has separate legal entity, perpetual succession, and common seal and t limited liability. It is a voluntary association of person who together contribu in the capital of the company to do business.

Generally, the capital of a company is divided into small parts known shares, the ownership of which is transferable subject to certain terms s conditions.
Characteristics of Company
(i) Incorporated Association A company comes into existence through the operation of law. Therefore, its incorporation under the Companies Act is must. Without such registration, no company can come into existence. Being created by law, it is regarded as an artificial legal person.
(ii) Separate Legal Entity A company has a separate legal entity, which is not affected by changes in the membership. Therefore being a separate entity, a company can contract, sue and be used in its corporate name and capacity.
(iii) Artificial Person A company is an artificial and juristic person that is created by law.
(iv) Limited Liability Every shareholder of accompany has limited liability. His liability is limited to the extent of the unpaid value of the shares held by him. If such shares are fully paid up, he is subject to no further liability.
(v) Perpetual Existence The existence of company is not affected by the death, retirement, and insolvency of its members. That is, the life of a company remains unaffected by the life and the tenure of its members in the company. The life of a company is infinite until it is properly wound up as per the Companies Act.
(vi) Common Seal The company is not a natural person and has no physical existence. Hence, it cannot put its signature. Thus, the common seal acts as an official signature of a company that validates the official documents.
(vii) Maintenance of Books A limited company is required by law to keep a prescribed set of account books and any failure in this regard attracts penalties.

Question 2. Explain in brief the main categories in which the share capital of a company is divided.
Answer Share capital of a company can be divided into the following categories
(i) Authorised Capital It refers to that amount which is laid down in clause of the memorandum of association of the company. This i maximum amount with which company is registered and to raise from the public by the issue of shares. The therefore, called the registered or nominal or authorised capital of company.
(ii) Issued Capital The authorised capital which is offered to the public for subscription including shares offered to the vendors for subscription other than cash is called the issued capital.
(iii) Subscribed Capital It is the portion of issued capital which has been subscribed to by the public i.e., applied for and allotted by the company. Thus, face value of allotted shares is known as subscribed capital.
(iv) Called-up Capital The portion of the subscribed capital which the shareholders are called upon to pay is termed as called up capital of the company.

The company usually does not require a shareholder to pay in one lot, the full value of the shares he has subscribed for. He is generally required to pay it by instalments. The balance of subscribed capital which has not been called-up represents uncalled capital.
(v) Paid-up Capital The amount of called-up capital which has been actually paid by the shareholders is called as paid-up capital and the amounts yet due from the shareholders are called as calls-in-arrears.
(vi) Reserve Capital Sometimes a company by means of special resolution decides that certain portion of its uncalled capital shall not be called-up during its existence and it would be available as an additional security to its creditors in the event of its liquidation. Such a portion of uncalled capital is termed as reserve capital.

Question 3. What do you mean by the term 'share? Discuss the type of shares, which can be issued under the Companies Act, 1956 as amended to date.
Answer The capital of a company is divided into a number of equal parts. Each part is called a share. A company may divide its capital into shares of ? 10, ? 50, ^100 or any suitable amount, but it is always preferable to have shares of small denomination in order to bring them within the reach of small investor.
According to Lord Lindley, "The portion of capital to which each member is entitled to his share". In this way, share is proportionate part of the share capital and forms ownership in a company.
According to Companies Act, 1956 there are two types of shares
(i) Preference Share Preference Share is one which carries the following two rights
(a) They have a right to receive dividend at a fixed rate before any dividend is paid on the equity shares
(b) On the winding up of the company, they have right to return of capital before the capital returned on equity shares.
However, not with standing the above two conditions, a holder of the preference share may have a right to share fully or to a limited extent in the surplus of the company as specified in the Memorandum or Articles* of the company.
(ii) Equity Share Under Indian Companies Act 1956, 'an equity share is share which is not preference share'. Thus, this share does not carry any preferential right or in other words, equity share is one which is entitled to dividend and repayment of capital after the claim of preference shares is satisfied. Usually the equity shareholders control the affairs of the company and hence right to all the profits after the preference dividend has been paid.

Question 4. Discuss the process for the allotment of shares of a company in case of over subscription.

Answer When shares are issued to the public for subscription through the prospectus by well managed and financially strong companies, it may happen that the total number of applications received for shares exceeds the number of shares offered by the company to the public, such situation is called the situation of over-subscription. A company can opt for any of the three alternatives to allot shares in case of over-subscription of shares.

(i) Excess Applications are Refused and Money received on Excess Applications is Returned to the Applicants

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(ii) If the Applicant are made Partially Allotment (or Pro-rata Basis) In case of over-subscription, when a company allots shares rateable to all the applicants, it is called as pro-rata allotment.

In such a case, the main problem is what to do with the excess amount received on application. Practically, it will be quite irrational to refund the excess money first and then ask the allottee applicants to pay the allotment money.

In practice, generally excess application money receive on these shares is adjusted towards the amount due on allotment or call. For this purpose the entry is made as follows

Pro-rata and Refund of Money In case of over-subscription, the director can adopt a combination of the above two alternatives i.e., they can accept full allotment to some applications, a pro-rata allotment to others and no allotment to the rest.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

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Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 5. What is a 'Preference Share'? Describe the different types of preference shares.

Answer Preference share is one which carries the following two rights
(i) They have a right to receive dividend at a fixed rate before any dividend is paid on the equity shares.
(iii) On the winding up of the company, they have right to return of capital before of the capital returned on equity shares.
However, not with standing the above two conditions, a holder of the preference share may have a right to share fully or to a limited extent in the surplus of the company as specified in the Memorandum or Articles of the Company.
Preference shares can be of various types which are as follows
(i) **Cumulative Preference** Shares If there are no profits in one year and the arrears of dividends are to be carried forward and paid out of the profits of subsequent years, the preference share is said to be cumulative. It is noted that the company should pay dividend out of profits only.
(ii) **Non-Cumulative Preference** Shares If unpaid dividend lapses, the share is said to be non-cumulative preference share. It means when a preference shareholder receives dividend only in case of profit and is not entitled any right to recover the arrears of dividend, then the type of preference shares held by the shareholder is known as non-cumulative preference shares.
(iii) **Redeemable Preference** Shares When shares are repaid after some specified time in accordance with the terms of issue they are called redeemable preference shares.
(iv) **Non-Redeemable Preference** Shares These are the preference shares, which do not carry with them the arrangement regarding redemption. According to Section 80 (54), no company limited by shares shall issue irredeemable

preference shares or preference shares redeemable after the expiry of 20 years from the date of issue.
(v) **Participating Preference** Shares When a preference shareholder enjoys the right to participate in the surplus profit (in addition to the fixed rate of dividend) that is left after the payment of dividend to the equity shareholders, the type of shares held by the shareholder is known as participating preference shares.
(vi) **Non-Participating Preference** Shares When a preference shareholder receives only a fixed rate of dividend every year and do not enjoy the additional participation in the surplus profit, then the type of shares held by the shareholder is known as non-participating preference shares.
(vii) **Convertible Preference** Shares These shares give the right to the holder to get them converted into equity shares at their option according to the terms and conditions of their issue.
(viii) **Non-Convertible Preference** Shares When the holder of a preference share has not been conferred the right to get his holding converted into equity share, it is called non-convertible preference shares. Preference shares are non-convertible unless otherwise stated.

Question 6. Describe the provisions of law relating to 'Calls-in-Arrears' and 'Calls in Advance'
Answer Calls-in-Arrears The portion of called up capital which is not paid by the shareholder within a specified time is known as calls-in-arrears. In other words, when a shareholder fails to pay the amount due on allotment or any subsequent calls, then it is termed as call-in-arrears.
The company is authorised by its Article of Association to charge interest at a specified rate on the amount of call-in-arrears from the due date till the date of payment. If the Article of Association is silent in this regard, then Table A shall be applicable that is interest at 5% pa is charged.
It is deducted from the called-up share capital on the liabilities side of the Company's Balance Sheet. The company can also forfeit the shares on account of non-payment of the calls money after giving proper notice to shareholders.
Calls in Advanqe It means calls not due but paid by the shareholder in advance. Thus, the amount of future calls is received in advance by the company.
In other words, when a shareholder pays the whole amount or a part of the amount in advance, i.e., before the company calls, then it is termed as calls in advance. The company is authorised by its Article of Association to pay interest at the specified rate on call in advance from the date of payment till the date of call made.
If the Article of Association is silent in this regard, then the Table A shall be

applicable that is, interest at 6% pa is provided. It is shown under the heading of current liabilities on the liabilities side of the Company's Balance Sheet.

Question 7. Explain the terms 'Over-subscription' and 'Under-subscription'. How are they dealt with in accounting records?
Answer When shares are issued to the public for subscription through the prospectus by well managed and financially strong companies, it may happen that the total number of applications received for shares exceeds the number of shares offered by the company to the public, such situation is called the situation of over-subscription. A company can opt for any of the three alternatives to allot shares in case of over-subscription of shares.
(i) Excess Applications are Refused and Money Received on Excess Applications is Returned to the Applicants

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(ii) If the Applicant are made Partially Allotment (or Pro-rata Basis) In case of over-subscription, when a company allots shares rateable to all the applicants, it is called as pro-rata allotment. In such a case the main problem is what to do with the excess amount received on application.
Practically, it will be quite irrational to refund the excess money first and then ask the allottee applicants to pay the allotment money.
In practice, generally excess application money receive on these shares is adjusted towards the amount due on allotment or call. For this purpose the entry is made as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(iii) Pro-rata and Refund of Money In case of over-subscription, the director can adopt a combination of the above two alternatives i.e., they ,can accept full allotment to some applications, a pro-rata allotment to others and no allotment to the rest.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Under-Subscription: In case when share are issued by the company and the number of shares applied by the public is lesser than the number of shares issued this is called the situation of under-subscription.
As per the Comprise Act, the minimum subscription is 90% of the shares issued by the company. This implies that the company can allot shares to the applicants provided if applications for 90% of the issued shares are received. Otherwise, the company should refund the entire application amount received.
In this regard, necessary journal entry is passed only after receiving and refunding of the application. In this case, normal entries are made as the adjustment is not needed for any excess.

Question 8. Describe the purposes for which a company can use 'Securities Premium Account.
Answer Securities premium account can be used only for the following four purposes as laid down by Section 78 of the Companies Act 1956
(i) To issue fully paid bonus shares to an extent not exceeding unissued share capital of the company.
(ii) To write-off preliminary expenses of the company.
(iii) To write-off the expenses of, or commission paid, or discount allowed on any of the shares or debentures of the company.
(iv) To pay premium on the redemption of preference shares or debentures of the company.

Question 9. State clearly the conditions under which a company can issue shares at a discount.
Answer In normal condition as a general rule, a company cannot ordinarily issue shares at a discount. It can do so only in cases such as 'reissue of forfeited shares' and in accordance with the provisions of Section 79 of the Companies Act. According to Section 79 of the Companies Act, 1932, a company is permitted to issue shares, at a discount provided the following conditions ara satisfied
(i) The issue of shares at a discount is authorised by an ordinary resolution

passed by the company at its general meeting and sanctioned by the Company Law Board now Central Government.
(ii) The resolution must specify the maximum rate of discount at which the shares are to be issued but the rate of discount must not exceed 10 per cent of the nominal value of shares. The rate of discount can be more than 10 per cent if the government is convinced that a higher rate is called-for under special circumstances of a case.
(iii) At least one year must have elapsed since the date on which the company became entitled to commence the business.
(iv) The shares are of a class which has already been issued. •
(v) The shares issued within two months from the date of receiving sanction for the same from the government or within such extended period as the government may allow.
(vi) If the offer prospectus at the date of issue must mention particulars of the discount allowed on the issue of shares.

Question 10. Explain the term 'Forfeiture of Shares' and give the accounting treatment on forfeiture.
Answer If a shareholder fails to pay the allotment money and or any call money on his shares as called upon by the directors, his shares may be forfeited by the directors, if they are so authorised by the Articles of Association. This is known as forfeiture of shares.
As per the Table A of the Company Act, the procedure of forfeiting shares is mentioned below.
(i) A notice is sent to default shareholder stating him/her to pay calls-in-arrears along with the interest accrued on the outstanding calls money within a period of 14 days of the receipt of notice, otherwise, the shares will be forfeited.
(ii) If the shareholder does not pay the amount, then the company has the right to forfeit his/her share by passing a resolution.
(iii) A notice of that resolution is send to the default shareholder and a public notice of the same is published in a daily newspaper.
(iv) The name of the shareholder is removed from the register of members (i.e., shareholders).

Accounting Treatment for Forfeiture of Shares
(i) Forfeiture of Shares that were Issued at Par

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(ii) Forfeiture of Shares that were Issued at Premium
(a) Sometimes forfeited shares would have been issued at premium in that case if amount of premium is received than premium received is not shown.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(b) Sometimes forfeited shares would have been issued at premium in that case if amount of premium is not received than premium not received is shown.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(iii) Forfeiture of shares that were issued at discount Sometimes forfeited shares would have been issued at discount in that case amount of discount will always be shown.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

NUMERICAL QUESTIONS

1. Anish Limited issued 30,000 equity shares of Rs.100 each payable at Rs.30 on application, Rs.50 on allotment and Rs.20 on Ist and final call. All money was duly received. Record these transactions in the journal of the company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. The Adersh Control Device Ltd was registered with the authorised capital of Rs.3,00,000 divided into 30,000 shares of Rs.10 each, which were offered to the public. Amount payable as Rs.3 per share on application, Rs.4 per share on allotment and Rs.3 per share on first and final call. These share were fully subscribed and all money was dully received. Prepare journal and Cash Book.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

3. Software solution India Ltd inviting application for 20,000 equity share of Rs.100 each, payable Rs.40 on application, Rs.30 on allotment and Rs.30 on call. The company received applications for 32,000 shares.
Application for 2,000 shares were rejected and money returned to Applicants. Applications for 10,000 shares were accepted in full and applicants for 20,000 share allotted half of
the number of share applied and excess application money adjusted into allotment. All money received due on allotment and call. Prepare journal and cash book.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

4. Rupak Ltd. issued 10,000 shares of Rs.100 each payable Rs.20 per share on application, Rs.30 per share on allotment and balance in two calls of Rs.25 per share. The application and allotment money were duly received. On first call
all member pays their dues except one member holding 200 shares, while another member holding 500 shares paid for the balance due in full. Final call was not made. Give journal entries and prepare cash book.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

5. Mohit Glass Ltd. issued 20,000 shares of Rs.100 each at Rs.110 per share, payable Rs.30 on application, Rs.40 on allotment (including Premium), Rs.20 on first call and Rs.20 on final call. The applications were received for 24,000 shares and allotted 20,000 shares and reject 4,000 shares and amount returned thereon. The money was duly received. Give journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

6. A limited company offered for subscription of 1,00,000 equity shares of Rs.10 each at a premium of Rs.2 per share. 2,00,000. 10% Preference shares of Rs.10 each at par.
The amount on share was payable as under :

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

7. Eastern Company Limited, having an authorised capital of Rs.10,00,000 in shares of Rs.10 each, issued 50,000 shares at a premium of Rs.3 per share payable as follows :

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Applications were received for 60,000 shares and the directors allotted the shares as follows :
(a) Applicants for 40,000 shares received shares, in full.
(b) Applicants for 15,000 shares received an allotment of 8,000

shares.
(c) Applicants for 500 shares received 200 shares on allotment, excess money being returned.
All amounts due on allotment were received. The first call was duly made and the money was received with the exception of the call due on 100 shares.
Give journal and cash book entries to record these transactions of the company. Also prepare the Balance Sheet of the company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

8. Sumit Machine Ltd issued 50,000 shares of Rs.100 each at discount of 5%. The shares were payable Rs.25 on application, Rs. 40 on allotment and Rs.30 on first and final call. The issue were fully subscribed and money were duly received except the final call on 400 shares. The discount was adjusted on allotment. Give journal entries and prepare balance sheet.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

9. Kumar Ltd purchases assets of Rs.6,30,000 from Bhanu Oil Ltd. Kumar Ltd. issued equity share of Rs.100 each fully paid in consideration. What journal entries will be made, if the share are issued, (a) at par, (b) at discount of 10 %
and (c) at premium of 20%

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

10. Bansal Heavy machine Ltd purchased machine worth Rs.3,20,000 from Handa Trader. Payment was made as Rs.50,000 cash and remaining amount by issue of equity share of the face value of Rs. 100 each fully paid at an issue price of Rs.90 each. Give journal entries to record the above transaction.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

11. Naman Ltd issued 20,000 shares of Rs.100 each, payable Rs.25 on application, Rs.30 on allotment , Rs.25 on first call and The balance on final call. All money duly received except Anubha, who holding 200 shares did not pay allotment
and calls money and Kumkum, who holding 100 shares did not pay both the calls. The directors forfeited shares of Anubha and kumkum. Give journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

12. Kishna Ltd issued 15,000 shares of Rs.100 each at a premium of Rs.10 per share, payable as follows:

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

All the shares subscribed and the company received all the money due, With the exception of the allotment and call money on 150 shares. These shares were forfeited and reissued to Neha as fully paid share of Rs.12 each.
Give journal entries in the books of the company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

13. Arushi Computers Ltd issued 10,000 equity shares of Rs.100 each at 10% discount. The net amount payable as follows:

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

A shareholder holding 200 shares did not pay final call. His shares Were forfeited. Out of these 150 shares were reissued to Ms.Sonia at Rs.75 per shares. Give journal entries in the books of the company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

14.Raunak Cotton Ltd. issued a prospectus inviting applications for 6,000 equity shares of Rs.100 each at a premium of Rs.20 per shares, payable as follows:

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Application were received for 10,000 shares and allotment was made Pro-rata to the applicants of 8,000 shares, the remaining applications Being refused. Money received in excess on the application was

adjusted toward the amount
due on allotment.Rohit, to whom 300 shares were allotted failed to pay allotment and calls money, his shares were forfeited. Itika, who applied for 600 shares, failed to pay the two calls and her share were also forfeited. All these shares were sold to Kartika
as fully paid for Rs.80 per shares. Give journal entries in the books of the company

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

15. Himalaya Company Limited issued for public subscription of 1,20,000 equity shares of Rs.10 each at a premium of Rs.2 per share payable as under :

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Applications were received for 1,60,000 shares. Allotment was made on pro-rata basis. Excess money on application was adjusted against the amount due on allotment.

Rohan, whom 4,800 shares were allotted, failed to pay for the two calls. These shares were subsequently forfeited after the second call was made. All the shares forfeited were reissued to Teena as fully paid at Rs 7 per share.

Record journal entries in the books of the company to record these transactions relating to share capital. Also show the company's balance sheet.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

16. Prince Limited issued a prospectus inviting applications for 2,00,000 equity shares of Rs.10 each at a premium of Rs.3 per share payable as follows :

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Applications were received for 30,000 shares and allotment was made on prorata basis. Money overpaid on applications was adjusted to the amount due on allotment.

Mr. 'Mohit' whom 400 shares were allotted, failed to pay the allotment money and the first call, and her shares were forfeited after the first call. Mr. 'Joly', whom 600 shares were allotted, failed to pay for the two calls and hence, his

shares were forfeited.Of the shares forfeited, 800 shares were reissued to Supriya as fully paid for Rs.9 per share, the whole of Mr. Mohit's shares being included. Record journal entries in the books of the Company and prepare the Balance

Sheet.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

17. Life machine tools Limited, issued 50,000 equity shares of Rs.10 each at Rs.12 per share, payable at to Rs.5 on application (including premium), Rs.4 on allotment and the balance on the first and final call.
Applications for 70,000 shares had been received. Of the cash received, Rs.40,000 was returned and Rs.60,000 was applied to the amount due on allotment, the balance of which was paid. All shareholders paid the call due,
with the exception of one share holder of 500 shares. These shares were forfeited and reissued as fully paid at Rs.8 per share. Journalise the transactions.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

18.The Orient Company Limited offered for public subscription 20,000 equity shares of Rs.10 each at a premium of 10% payable at Rs.2 on application; Rs.4 on allotment including premium; Rs.3 on First Call and Rs.2 on Second and Final call. Applications for 26,000 shares were received. Applications for 4,000 shares were rejected. Pro-rata allotment was made to the remaining applicants. Both the calls were made and all the money were received except the final call on 500 shares which were forfeited. 300 of the forfeited shares were later on issued as fully paid at Rs.9 per share. Give journal entries and prepare the balance sheet

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

19.Alfa Limited invited applications for 4,00,000 of its equity shares of Rs.10 each on the following terms :

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Applications for 5,00,000 shares were received. It was decided :
(a) to refuse allotment to the applicants for 20,000 shares;
(b) to allot in full to applicants for 80,000 shares;
(c) to allot the balance of the available shares' pro-rata among the other applicants; and
(d) to utilise excess application money in part as payment of allotment money.
One applicant, whom shares had been allotted on pro-rata basis, did not pay the amount due on allotment and on the call, and his 400 shares were forfeited.
The shares were reissued @ Rs.9 per share. Show the journal and prepare Cash book to record the above .

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

20. Ashoka Limited Company which had issued equity shares of Rs.20 each at a discount of Rs. 4 per share, forfeited 1,000 shares for non-payment of final call of Rs.4 per share. 400 of the forfeited shares are

reissued at Rs.14 per share
out of the remaining shares of 200 shares reissued at Rs.20 per share. Give journal entries for the forfeiture and reissue of shares and show the amount transferred to capital reserve and the balance in Share Forfeiture Account.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

21. Amit holds 100 shares of Rs.10 each on which he has paid Re.1 per share as application money. Bimal holds 200 shares of Rs.10 each on which he has paid Re.1 and Rs.2 per share as application and allotment money, respectively. Chetan holds 300 shares of Rs.10 each and has paid Re.1 on application, Rs.2 on

allotment and Rs.3 for the first call. They all fail to pay their arrears and the second call of Rs.2 per share and the directors, therefore, forfeited their shares. The shares are reissued subsequently for Rs.11 per share as fully paid. Journalise the transactions.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

22. Ajanta Company Limited having a normal capital of Rs.3,00,000, divided into shares of Rs.10 each offered for public subscription of

20,000 shares payable at Rs.2 on application; Rs.3 on allotment and the balance in two calls of Rs.2.50
each. Applications were received by the company for 24,000 shares. Applications for 20,000 shares were accepted in full and the shares allotted. Applications for the remaining shares were rejected and the application money was refunded.
All moneys due were received with the exception of the final call on 600 shares which were forfeited after legal formalities were fulfilled. 400 shares of the forfeited shares were reissued at Rs.9 per share.Record necessary journal entries and prepare the balance Sheet showing the
amount transferred to capital reserve and the balance in Share forfeiture account.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

23. Journalise the following transaction in the books Bhushan Oil Ltd:

(a) 200 shares of Rs.100 each issued at a discount of Rs.10 were forfeited for the non payment of allotment money of Rs.50 per share. The first and final call of Rs.20 per share on these share were not made. The forfeited share were reissued at Rs.70 per share as fully paid-up.

(b) 150 shares of Rs.10 each issued at a premium of Rs.4 per share payable with allotment were forfeited for non-payment of allotment money of Rs.8 per share including premium. The first and final call of Rs.4 per share were not made. The forfeited share were reissued at Rs.15 per share fully paid-up.

(c) 400 share of Rs.50 each issued at par were forfeited for non-payment of final call of Rs.10 per share. These share were reissued at Rs.45 per share fully paid-up.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

24. Amisha Ltd inviting application for 40,000 shares of Rs.100 each at a premium of Rs.20 per share payable; on application Rs.40 ; on allotment Rs.40 (Including premium): on first call Rs.25 and Second and final call Rs.15.
Application were received for 50,000 shares and allotment was made on prorata basis. Excess money on application was adjusted on sums due on allotment.
Rohit to whom 600 shares were allotted failed to pay the allotment money and his shares were forfeited after allotment. Ashmita, who applied for 1000 shares failed to pay the
Two calls and his shares were forfeited after the second call. Of the shares forfeited, 1200 shares were sold to Kapil for Rs.85 per share as fully paid, the whole of Rohit's shares being included. Record necessary journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

More Resources for CBSE Class 12

Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 2 Issue and Redemption of Debentures

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**Answers NCERT Solutions For Class 12 Accountancy
http://freehomedelivery.net/Ch 2 Issue and Redemption of Debentures**

1. Amrit Company Limited purchased assets of the book value of Rs.2,20,000 fromanother company and agreed to make the payment of purchase consideration by issuing 2,000, 10% debentures of Rs.100 each at a premium of 10%. Record necessary journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. A company purchased assets of the value of Rs.1,90,000 from another company and agreed to make the payment of purchase consideration by issuing 2,000,10% debentures of Rs.100 each at a discount of 5%. Record necessary journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

3. Rose Bond Limited purchased a business for Rs. 22,00,000. Purchase Price was paid by 6% debentures. Debentures of Rs. 20,00,000 were issued at a premium of 10% for

the purpose. Record necessary journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

4. Nikhil and Ashwin Limited bought business of Agarwal Limited consisting sundry assts of Rs. 3,60,000, sundry creditors Rs. 1,00,000 for a consideration ofRs. 3,07,200. It issued 14% debentures of Rs. 100 each fully paid at a discount of 4% in satisfaction of purchase consideration. Record necessary journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note If business is purchased and assets and liabilities are mentioned along with purchase price, pass a journal entry. To balance the entry use word 'Goodwill' if difference is on debit side and word 'Reserves' if difference is on credit side.

DO IT YOURSELF II

2. Record necessary journal entries in each of the following cases:
a. 27,000, 7% debentures of Rs. 100 each issued at par, redeemable at par.
b. 25,000, 7% debentures of Rs. 100 each issued at par redeemable at 4% premium.
c. 20,000, 7% debentures of Rs. 100 each issued at 5% discount and redeemable at par.

d. 30,000, 7% debentures of 100 each issued at 5% discount and redeemable at 2½ % premium.
e. 35,000, 7% debentures of Rs. 100 each issued at 4% premium and redeemable.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

DO IT YOURSELF III

1. Diwakar enterprises Ltd. Issued 10,00,000, 6% debentures on April 1, 2002. Interest is paid on September 30, 2002 and March 31, 2003.
Record necessary journal entries assuming that income tax is deducted @30% of the amount of interest.
(Amount of tax Rs.18,000 for the year ending March 31, 2003)

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. Laser India Ltd. Issued 7,00,000, 8% debentures of Rs. 100 each at par.Company deducts income tax from the interest of these debentures at source. Interest is to be paid on these debentures half-yearly on September 30 andMarch 31, every year. Amount of income tax deducted half-yearly iRs. 2,80,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

DO IT YOURSELF IV

1. X Ltd. Issued 2,000, 10% debentures of Rs.100 each at a discount of 8% on1 Jan, 1992 which are redeemable at par by annual drawings in 4 yearscommencing from 31st March 1993 as per the following redemption plan:Ist Draw 10%, 2nd Draw 20%, 3rd Draw 30%, and 4th Draw 40%. Calculate theamount of discount to be written-off each

year assuming that X Ltd. followscalendar year as its accounting year.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. Z Ltd. issued 15,00,000, 10% debenture of Rs.50 each at premium of 10% payable as Rs.20 on application and balance on allotment. Debentures are redeemable at par after 6 years. All the money due on allotment was calledand duly received. Record necessary entries when premium money is included:
(i) in application money
(ii) in allotment money

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

3. Z Ltd. issued 5,000, 10% debentures of Rs.100 each at a discount of 10% on 1.1.2005. The debentures are to be redeemed every year draw of lots – 1,000 debenture to be redeemed every year starting on 31.12.2005. Record the necessary journal entries including the payment of interest and writing off the discount on issue of debentures. The interest is payable on 30th June and 31st December. Z Ltd. Closes its books of accounts on 31st December.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

4. M Ltd. issued 10,000, 8% debentures of Rs.100 each at a premium of 10% on 1.1.2004. It purchased sundry assets of the value of Rs,2,50,000 and took over the liabilities of Rs,1,90,000 and issued 8% debentures at a discount of 5% to the vendor. On the same date it took loan from the Bank for Rs.1,00,000 and issued 8% debentures as Collateral Security. Record the relevant journal entries in the books of M Ltd. and prepare the extract of balance sheet on 31.12.2004. Ignore interest.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

5. On 1.1.2005 Fast Computers Ltd. issued 20,00,000, 6% debentures of Rs.100 each at a discount of 4%, redeemable at a premium of 5% after three years.
The amount was payable as follows:
On application Rs.50 per debenture,
Balance on allotment,
Record the necessary journal entries for issue of debentures.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

6. D Ltd. Purchased machinery worth Rs.2,00,000 from E Ltd. on 1.1.2001. Rs.50,000 were paid immediately and the balance was paid by issue of Rs.1,60,000, 12% Debentures in D Ltd. Record the necessary journal entries for recording the

transactions in the books of D Ltd.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

TEST YOUR UNDERSTANDING I

• State whether the following statements are True (T) or Fasle (F)
Question 1. Debenture is written instrument acknowledging a debt under the common seal of the company.
Answer True

Question 2. Debenture is a part of owned capital.
Answer False

Question 3. The payment of interest on debentures is a charge on the profits of the company.
Answer True

Question 4. The debentures cannot be issued at a discount of more than 10% of the face value.
Answer False
Question 5. Redeemable debentures are those debentures, which are payable on the expiry of the specific period.
Answer True

Question 6. Perpetual debentures are also known as irredeemable debentures.
Answer True

Question 7. Debentures cannot be converted into shares.
Answer False

Question 8. Debentures cannot be issued at a premium.
Answer False
Question 9. A Collateral Security is a Subsidiary Security.
Answer True

Question 10. Debentures cannot be issued at a premium and redeemable at par.
Answer False

Question 11. Loss on issue of debentures account is a revenue loss.
Answer False

Question 12. Premium on redemption of debentures account is shown under the 'Securities Premium' in the Balance Sheet.
Answer False

DO IT YOURSELF V

1. X Ltd. decides to redeem 8,000, 10% debentures of Rs.100 each on January 1, 2004 at a premium of 5%. The company has a balance of Rs.9, 00,000 at the credit of its profit and loss account. The company closes its books on December 31 every year. What journal entries the company will be recorded to redeem the above debentures.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. G Ltd. issued 5,00,000, 12 % debenture of Rs.100 each on April 1, 2002 redeemable at par on July 1, 2003. The company received applications for 6,00,000 debentures and the allotment was made to all the applicants on pro-rata basis. The debenture were redeemed on due date. How much amount of Debenture Redemption Reserve is to be created before the redemption is carried out? Also record necessary journal entries

regarding issue and redemption of debenture. Ignore tax deducted at source.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

TEST YOUR UNDERSTANDING II

Select the correct answer for the following multiple choice questions:
1. Debentures which are transferable by mere delivery are:
(a) Registered debentures, (b) First debentures,
(c) Bearer debentures.
2. The following journal entry appears in the books of X Co. Ltd.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 3. X Co Ltd purchased assets worth ? 28,80,000. It issued debentures of ? 100 each at a discount of 4% in full satisfaction of the purchase consideration. The number of debentures issued to vendor is
(a) 30,000 (b) 28,800 (c) 32,000
Answer (a) 30,000

Question 4. Convertible debentures cannot be issued at a discount if 1 (a) they are to be immediately converted
(b) they are not to be immediately converted
(c) None of the above
Answer (a) They are to be immediately converted

Question 5. Discount on issue of debentures is shown under the following head in the Balance Sheet
(a) Profit and loss account
(b) Miscellaneous expenditure
(c) Debentures account

Answer (b) Miscellaneous expenditure

Question 6. When debentures are issued at par and are redeemable at a premium, the loss on such an issue debited to
(a) Profit and loss account
(b) Debentures applications and allotment account
(c) Loss on issue of debentures account
Answer (c) Loss on issue of debentures account

Question 7. Excess value of net assets over purchase consideration at the time of purchase of business is credited to
(a) General reserve
(b) Capital reserve
(c) Vendor's account
Answer (b) Capital reserve

Question 8. When all the debentures are redeemed, balance in the debentures redemption fund account is transferred to
(a) Capital reserve
(b) General reserve
(c) Profits and loss appropriation account
Answer (b) General reserve

Question 9. The nominal and book values of debenture redemption fund investments account are respectively ? 1,00,000 and ? 96,000.
The company sold investments of nominal value of? 30,000 at a price which was just sufficient to redeem debentures of ? 30,000 at 10% premium, the profit on sale of investment is
(a) Rs. 4,200 (b)Rs. 3,000 (c) Nil
Answer (a) Rs. 4,200

Question 10. Own debentures are those debentures of the company which
(a) the company allots to its own promoters
(b) the company allots to its Director
(c) the company purchase from the market and keeps them as investments
Answer (c) The company purchase from the market and keeps them as investments

Question 11. Profit on cancellation of own debentures is transferred to
(a) Profit and loss appropriation account
(b) Debenture redemption reserve
(c) Capital reserve
Answer (c) Capital reserve

Question 12. When debentures are redeemed out of profits, an equal amount is transferred to
(a) General reserve
(b) Debenture redemption reserve
(c) Capital reserve
Answer (b) Debenture redemption reserve

Question 13. Profit on sale of debenture redemption fund investments in the first instance is credited to
(a) Debenture redemption fund account
(b) Profit and loss appropriation account
(c) General reserve account
Answer (a) Debenture redemption fund account

Question 14. The balance of sinking fund investment account after the realisation of investments is transferred to
(a) Profit and loss account
(b) Debentures account
(c) Sinking fund account
Answer (c) Sinking fund account

Question 15. When debentures are issued at a discount and are redeemable at a premium, which of the following accounts is debited at the time of issue
(a) Debentures account
(b) Premium on redemption of debentures account
(c) Loss on issue of debentures account
Answer (c) Loss on issue of debentures account .

TEST YOUR UNDERSTANDING III

• Indicate in the column below, the account to be debited in case of the following transactions.
Transaction Account to be Debited
Question 1. Issue of debentures to a vendor in consideration of the business purchase.
Question 2. Setting aside the amount for creating sinking fund for redemption of debentures.
Question 3. The balance of debenture redemption reserve account after redemption of the debentures.
Question 4. Purchase of own debentures by the company.
Question 5. Writing off discount on issue of debentures.
Answer Account to be Debited
1. Vendor A/c
2. Profit and Loss Appropriation A/c
3. Debenture Redemption Reserve A/c

4. Own debentures A/c
5. Profit and Loss A/c

• Indicate in the column below, the account to be credited in case of the following transactions
Transaction Account to be Credited
Question 6. Debentures issued at a discount and are redeemable at par.
Question 7. Transfer of interest on sinking fund investments to sinking fund account.
Question 8. Balance of DRR account after the redemption of Debentures.
Question 9. Profit on sate of sinking fund investment account.
Question 10. Writing off the loss on issue of debentures.
Answer Account to be Credited
6. On Issue-Debenture A/c
On Redemption-Bank A/c .
7. Sinking Fund A/c
8. General Reserve A/c
9. Profit transferred to Debenture Sinking Fund A/c
10. Loss on Issue of Debentures A/c

DO IT YOURSELF VI

1. G Ltd. has 800 lakhs, 10% debentures of Rs.100 each due for redemption on March 31, 2003. Assume that Debenture Redemption Reserve has a balance of Rs. 3,40,00,00,000 on that date. Record necessary entries at the time of redemption of debenture.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note:
Debentures for 80,000 (lakhs) were to be redeemed as per SEBI guidelines, 50% debenture redemption reserve is to be maintained. For Rs. 80,000 (lakhs) it comes to 40,000 (lakhs). Deberture redemption reserve already exist in books for Rs.34,000 (lakhs). Hence entry for balance 6,000 (lakhs) is passed in this solution.

2. R Ltd. issued 88,00,000, 8 % debenture of Rs. 50 each at a premium of 5 % on July 1, 2000 redeemable at par by conversion of debenture into shares of Rs.20 each at a premium of Rs.2 per share on June 30, 2003. Record necessary entries for redemption of debenture.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

3. C Ltd. has outstanding 11,00,000, 10% debentures of Rs.200 each, on April 1, 2003. The Board of Directors have decided to purchase 20% of own debenture for cancellation at Rs.200 each. Record necessary entries for the same.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

4. Record necessary journal entries in the books of the Company in following case for redemption of 1,000, 12% Debentures of Rs.10 each issued at par:
(a) Debentures redeemed at par by conversion into 12% Preference Shares of Rs.100 each,
(b) Debentures redeemed at a premium of 10% by conversion into Equity Share issued at par,
(c) Debentures redeemed at a premium of 10% by conversion into Equity Shares issued

at a premium of 25%.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

5. On 31.1.2005 Janta Ltd. converted its Rs.88,00,000, 6% debentures into equity shares of Rs.20 each at a premium of Rs.2 per share. Record necessary journal entries in the books of the company for redemption of debentures.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

6. Anirudh Ltd. has 4,000, 8% debentures of Rs.100 each due for redemption on March 31, 2005. The company has a debenture redemption reserve of Rs.1,50,000 on that date. Assuming that no interest is due record the necessary journal entries at the time of redemption of debentures.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Working Note

Debenture forRs.4,00,000 were to be redeemed. As per SEBI guidelines, 50% debenture redemption reserve is to be maintained. For Rs.14,00,000 it comes to Rs.2,00,000. Debenture redemption reserve already in books of account was Rs.1,50,000. Hence, entry for balance Rs. 50,000 was passed in this solution.

SHORT ANSWER TYPE QUESTIONS

Question 1. What is meant by a Debenture?
Answer Debenture The word 'Debenture' has been derived from a Latin word 'debere' which means to borrow.
Debenture is a written instrument acknowledging a debt under the common seal of the company. It contains a contract for repayment of principal after a specified period or at intervals or at the option of the company and for payment of interest at a fixed rate payable usually either half-yearly or yearly on fixed dates.
According, to Section 2(12) of The Companies Act, 1956 'Debenture' includes Debenture Stock, Bonds and any other securities of a company whether constituting a charge on the assets of the company or not.

Question 2. What does a Bearer Debenture mean?
Answer Bearer debentures are the debentures which can be transferred by way of delivery and the company does not keep any record of the debenture holders. Interest on debentures is paid to a person who produces the interest coupon attached to such debentures.

Question 3. State the meaning of 'Debentures issued as a Collateral Security'.
Answer Collateral security is given in addition to the primary security to the loan provider. In case when a company takes some loan it may issue debentures for additional security besides the primary security to that particular bank or financial institution.
Here it is to be remember that issue of debenture in ordinary course is different from issue of debenture as collateral security, in ordinary course debenture holders are entitled to get interest at an specified coupon rate where as in case of debenture issued as collateral security the holder of these debenture is not entitled to any such interest.
But in case of any default in payment of principle or interest of loan it may recover its amount from the issue of such debenture in the secondary market. Here it should be remembered that first of all the primary security will be sold after that debenture as collateral security will be used.

Question 4. What is meant by Issue of debentures for consideration other than Cash'?
Answer When a company purchase some assets it is supposed to pay the purchase consideration in cash but sometimes due to lack of sufficient fund, company may issue debenture for the payment of such purchase consideration. This is known as issue of debenture for consideration other than cash.
The issue of debenture for consideration other than cash serves the purpose of both the vendor as well as of the purchaser (company). From the purchaser's point of view, purchasing an asset against the issue of debentures requires no additional cost for raising loans or arranging funds immediately.
On the other hand, the vendor gets interest on the amount of debentures received. In this case, payment is deferred by issue of debentures and interest is paid for time lag. Here it should be remembered that such debentures may be issued at par, premium or discount to the vendor.

Question 5. What is meant by 'Issue of debentures at discount and redeemable at premium?
Answer As per the prevailing market circumstances sometimes company has to manage funds by issuing debenture below its par value and to attract the investor when these are redeemed at price higher than its par value, then it is termed as issue of debenture at discount and redeemable at premium.
The difference between the issue price and the redemption price is treated as loss on issue of debenture and posted in assets side of the company as miscellaneous expenditure. To have a better understanding about the issue we may take an example as follows

Example: A 10% debenture of ? 100 each is issued at 5% discount and is redeemed at 5% premium. The following Journal Entry will be passed for that

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 6 What is 'Capital Reserve'?
Answer Capital Reserve is a reserve that is created out of capital profits. Capital profits are those profits arising out of those activity which are not part of the business operations e.g., premium on issue of share and debentures, profits of sale of fixed asset, profit on redemption on debenture and profit on reissue of forfeited share and so on.

A capital reserve can be utilised for meeting the future capital losses. Here it is to be remembered that capital reserve cannot be used for distributing dividend to the share holders but bonus shares can be issued out of the capital reserve.

Question 7 What is meant by a 'Irredeemable Debenture?
Answer Irredeemable Debentures are those debentures which may not be redeemed during the life of a Company. They can only be paid off in the event of winding up of the Company. The holder of such debenture will enjoy interest on these debentures throughout the life of the company. Now-a-days no company issue irredeemable debentures.

Question 8. What is a 'Convertible Debenture?
Answer Convertible Debentures are those debentures which are convertible in equity shares after some specified time generally mentioned at the time of issue of such debentures. These convertible debentures are divided into two categories
(i) **Partly Convertible Debenture**: In this type of debenture only a part of such debenture is convertible in equity shares which is mentioned at the time of issue.
(ii) **Fully Convertible Debenture** :These are fully convertible into equity shares. It means in case of fully convertible debenture the whole amount of such debenture, is convertible in equity share after the period mentioned in the prospectus.

Question 9. What is meant by 'Mortgaged Debentures?
Answer Debentures which are secured against asset/s of a company known as Mortgaged Debenture. Mortgage Debentures are of two types first fixed charge mortgage debenture and second floating charge mortgage debentures.
When debentures are secured against a particular asset, then they are called fixed charge whereas, if the debentures are secured against all the assets of a company, then it is called floating charge. Mortgage debentures can only be sold by the holder when company fails to pay its loan or interest there on.

Question 10. What is discount on issue of debentures?
Answer Debenture is said to have been issued at discount where an applicant is required to pay a

total sum less than the face value of the debenture. The excess of the face value over the issue price is regarded as the discount. When debentures are issued at a discount, cash account is debited with net sum received, the discount on debentures account is debited with the amount of discount allowed and the debentures account is credited with the full nominal value of the debentures.
Here it is worth mentioning that there is no legal restriction on the companies for issuing debentures at discount. Maximum limit for discount on debentures is also not prescribed by the Companies Act. However, this Act requires that the amount of discount must be shown on the assets side of the Balance Sheet till written off under the head "Miscellaneous Expenditure."

Question 11. What is meant by 'Premium on Redemption of Debentures'?
Answer When the debentures are redeemed at a price more than its face value or the par value, then it is said that the debentures are redeemed at premium. The difference between the redeemed price and the par value is regarded as a capital loss and this loss is written off till the redemption of the debentures.
The Premium on Redemption of Debenture is shown on the Liabilities side of the Balance Sheet under the head of "Current Liabilities and Provisions" debentures are redeemed. –

Question 12. How debentures are different from shares? Give two points.
Answer Nature: A share is a part of the capital of the company and a debenture is a part of loan of the company.

Dividend or Interest :Dividend on shares is paid only when there are profits in
the company on the other hand debenture interest has to be paid, it the company does not have profit or even suffer a loss.

Ownership Equity share holders are the owners of the company on the other hand debenture holders are the creditors of the company.

Question 13. Name the head under which 'Discount on Issue of Debentures' appears in the Balance Sheet of a company.
Answer As we know that Discount on Issue of debentures is a capital loss and it will be written off out of the profit of coming years, Therefore, it is shown on the Assets side of the Balance Sheet under the heading of "Miscellaneous Expenditures" until it is written off.

Question 14. What is meant by redemption of debentures ?
Answer The term redemption implies the discharge of an obligation arising out of the contractual obligations created through the debenture Trust Deed. In other words, discharge of the liability on account of debentures is called redemption of debenture.
The redemption of debentures is made by the company in accordance with the terms and conditions of issue. Debentures may be redeemable at par, premium or discount, but in present scenario redemption of debentures at par and at premium is most popular. The redemption can be done out of profits or from the fresh issue of debentures or shares.
Redemption of debentures may be done by the following methods
(i) By paying after stipulated period
(ii) By annual drawing
(iii) By conversion into shares or new debentures
(iv) By purchasing own debentures in the open market
(v) At the option of the company

Question 15. Can the company purchase its own debentures?
Answer Yes, a company, if authorised by its Articles of Association, can purchase its own debentures in the open market. The main purposes of such purchase may be as follows
(i) A company may purchase its own debenture for immediate cancellation for reducing the debenture liability especially in case when the interest rate on its debenture is higher than the market rate of interest.
(ii) A company may also purchase its own debentures with the motive of investment and sell them at higher price in future and thereby earn profit.

Question 16. What is meant by redemption of debentures by conversion?
Answer Debentures are usually redeemed in cash but sometimes privilege is given to the debenture holders to exchange their debentures either for shares or for new debentures of the company. The redemption of debentures by means of shares or new debentures is known as redemption by conversion and the debentures which carry such a right is called convertible debentures.

Question 17. How would you deal with 'Premium on Redemption of Debentures?
Answer When the debentures are redeemed at a price more than its face value or the par value, then it is said that the debentures are redeemed at premium. The difference between the redeemed price and the par value is regarded as a capital loss and this loss is written off till the redemption of the debentures.
The Premium on Redemption of Debenture is shown on the Liabilities side of the Balance Sheet under the head of Current Liabilities and Provisions until debentures are redeemed.
Accounting Treatment for Premium on Redemption on Debentures

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 18. What is meant by 'Redemption out of Capital'?
Answer When debentures are redeemed out of current resources, the working capital of the company are reduced to that extent, and therefore, it is called redemption out of capital.

In other words when debentures are redeemed out of capital and no profits are utilised for redemption, then such redemption is termed as redemption out of capital.

A company cannot redeem its debentures purely out of capital. At least 50% of debentures issued must be redeemed out of profits by creating a 'Debenture Redemption Reserve' and the balance of debentures issued may be redeemed out of profits or out of capital. •

According to the Companies Act, 1956 when debentures are to be redeemed an adequate amount of profits is required to be transferred to 'Debenture Redemption Reserve' every year before the redemption begins. It is to be noted that the Companies Act, 1956 does not spell out at to what is the adequate amount.

For this one can refer to SEBI Guidelines which stipulates that an amount equal to 50% of the debentures issue should be transferred to 'Debenture Redemption Reserve' before the redemption begins.
There are exceptions in the following cases
(i) Infrastructure companies (i.e., those companies that are engaged in the business of developing, maintaining and operating infrastructure facilities)
(ii) A company that issues debentures with a maturity up to 18 months.
(iii) In case of Convertible debentures and convertible portion of partly convertible debentures

Question 19. What is meant by redemption of debentures by 'Purchase in the Open Market?
Answer A company, if authorised by its Articles of Association, can redeem its own debentures by purchasing them in the open market. This is advantageous for several reasons
(I) It would be saving the amount of interest on debentures purchased and cancelled.
(ii) Sometimes the own debentures are being sold at a discount. It would enable the company to save money equai to the amount of discount i.e., profit on redemption of debentures.
(iii) Debentures so purchased may be kept alive as investment. In need of fund, they can again be sold off in the market.
Objectives There may be the following objectives foP purchasing own debentures in the open market
(i) For immediate cancellation of debentures.
(ii) For investment in the own debentures.

Question 20. Under which head is the 'Debenture Redemption Reserve' shown in the Balance Sheet.
Answer The Debenture Redemption Reserve is shown on the Liabilities side of the Balance Sheet under the head Reserve and Surplus.

LONG ANSWER TYPE QUESTIONS

Question 1. What is meant by a debenture? Explain the different types of debentures?
Answer Debenture: The word 'Debenture' has been derived from a Latin w'ord 'Debere' which means to borrow. Debenture is a written instrument acknowledging a debt under the common seal of the company. It contains a contract for repayment of principal after a specified period or at intervals or at the option of the company and for payment of interest at a fixed rate payable usually either half-yearly or yearly on fixed dates.

According, to Section 2(12) of The Companies Act, 1956 'Debenture' includes Debenture Stock, Bonds and any other securities of a company whether constituting a charge on the assets of the company or not. There are various types of Debentures.
(i) **From Security Point of View** :From security point of view debentures can be classified into two broad categories naked or simple debentures and Mortgaged debentures.
(a) **Naked or Simple Debentures** :Naked or Simple Debentures are those debentures which do not carry any security in respect of repayment of interest or the principal. The general solvency of the company is the only security for the holders of simple debentures.
(b) **Mortgaged Debentures**: Mortgaged Debentures are the debentures which are secured by a charge on the asset or properties of the company. The debenture holders have the right to recover their principal amount as well as unpaid interest out of the assets mortgaged by the company.

In case of mortgage debentures, a company may prefer to appoint trustees who will hold the property given by way of security in trust for the benefits of debentures holders.

(ii) **From Permanence Point of View** From Permanence point of view the debentures may be Redeemable or Irredeemable debentures.
(a) **Redeemable Debentures** Redeemable debentures provide for the payment of principal amount on the expiry of certain period. Redeemable debentures can be reissued even after they have been redeemed until they have been cancelled.
(b) **Irredeemable Debentures** Irredeemable Debentures are retained as a part of the permanent capital structure during the life time of the company. Such debt becomes due for payment only when the company goes into liquidation or when the payment of interest is not made regularly.

The company has the option of cancelling its liability to the debenture holders at any time by giving due notice to them.

(iii) **From Priority Point of View** :From this point of view the debentures may be First and Second debentures.
(a) **First Debentures** :First Debentures are those debentures which are paid first before any payment is made to another type of debentures.
(b) **Second Debentures**: Second Debentures are those debentures which are paid after making the payment of first debentures.
(iv) **From Recording Point of View** :From recording point of view debentures can be classified into two categories bearer and registered debentures.
(a) **Bearer Debentures** :Bearer Debentures are transferable per bearer without endorsement and they are just like bearer cheques or government currency notes. They are treated as negotiable instrument and transferable by mere delivery. It is not necessary that transfer of such debentures should be registered with the company. The interest is paid to the holder irrespective of identity.
(b) **Registered Debentures**: Registered debentures are made out in the name of a particular person who is registered by the company as a holder and are transferable in the same way as shares.
The payment of interest and repayment of capital is made to those whose name are registered with the company and duly entered in the register of debenture holders.
(v) **From Conversion Point of View**: From conversion point of view debentures may be convertible or non-convertible.
(a) **Convertible Debentures** :Convertible debenture holders are given an option to convert them into equity or preference shares at a stated rate of exchange after a certain period. Convertible debentures are very popular these days with the companies as it provides them a major source of permanent working capital. It also provides safety, liquidity, capital appreciation and assured return to the investors.

(b) **Non-Convertible Debentures**: Non-convertible debentures are not convertible into equity or preference shares afterwards.

Question 2. Distinguish between a debenture and a share. Why debenture is known as loan capital? Explain.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 3. Describe the meaning of 'Debenture Issued as Collateral Securities'. What accounting treatment is given to the issue of debentures in the books of accounts?
Answer When a company takes a loan, it has to give some security, it may do so by giving debentures to the party from whom loan is takes. If on the due date principal is paid back by the Company and interest is also paid, the loan-giver will return the debentures to the Company and then they will be cancelled by the Company,

If the Company makes a default, the bank may either keep the debenture and become debenture-holder or sell them and realise money. This type of issue by the Company is called Issue of Debenture as Collateral Security.

When debentures are issued by the company, they are not really alive and no accounting entry is made in the books of the Company for it. Only a note is given in the balance sheet for it as under

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

If accounting record for these debentures is to be made Debentures Suspense A/c is debited and deoentures A/c credited, debentures are shown in the liability side and balance of debentures Suspense A/c is shown in the assets side of the Balance Sheet. When debt is paid off by the Company, Debentures A/c is debited and Debentures Suspense A/c is credited.

Question 4. How is 'Discount on Issue of Debentures' treated in the books of accounts? How will you deal with the 'Discount on issue of debentures' when the debentures are to be redeemed in instalments?
Answer When the debentures are issued at a price below its par value or face value, then it is said that the debentures are issued at discount. The difference between the issue price and the face value of the debenture is regarded as a capital loss. This loss is written off every year till the debentures are redeemed.

The loss on the issue of debenture is shown on the Assets side of the Balance Sheet under the heading of Miscellaneous Expenditures.

Accounting Treatment for Discount on Issue of Debentures:
At the time of issue of debentures at discoun

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

At the time of writing off the discount on issue of debentures at the end of each year

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(i) Fixed Instalment Method/Equal Instalment Method : This method is used when debentures are redeemable in lump sum after a specified period of time. In this case an equal amount of discount (loss) is written off in equal instalments over the life of the debenture. The formula for calculating amount of discount written off every year is given below

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(ii) Fluctuating Instalment Method/Variable Instalment Method/ Proportion Method:
When debentures are repaid by annuaLdrawings or in instalments, the discount should be written-off in the ratio of
debentures outstanding as at the end of each accounting year. The amount of discount, under this method, goes on reducing every year and so this method may also be known as Reducing Instalment Method. –

e.g., if a company has issued 10% debentures of Rs. 12,00,000 at 5% discount redeemable annually by Rs. 2,40,000 each year. The total amount of discount on Rs.12,00,000 debentures @ 5% is Rs. 60,000, i.e., (12,00,000 x 5/100 =Rs. 60,000). The amount of discount to be written off every year is calculated as

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Hence, the amount of the total discount of' 60,000 will be written off in the ratio of ,5 : 4 : 3 : 2 :1 i.e.,' 20,000,' 16,000,' 12,000,' 8,000 and 4,000 respectively.

Question 5. Explain the different terms for the issue of debentures with reference to their redemption.
Answer Debentures can be issued at par, at premium and at discount in the same way they can be redeem at par and at premium. Debentures can never be redeemed at discount. The following are the six situation under which debentures can be issued to their redemption.
(i) Issue at Par and Redeemable at Par: When the debentures are issued and are redeemed at their face value, then the following Journal entry is passed.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(ii) Issue at Premium and Redeemable at Par When the debentures are issued at premium and redeemable at par, then the following Journal entry is passed. As premium is a gain for a company so it is credited in the Journal entry.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(iv)Issue at Discount and Redeemable at Par When the debentures are issued at discount and redeemable at par, then the following Journal entry is passed. As discount is a loss for a company so it is debited in the Journal entry.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(v) Issue at Premium and Redeemable at Premium When debentures are issued at par and redeemable at premium, then the following Journal entry is passed. In such case, the company did not suffer any loss at the time of issue but there will be loss at the time of redemption.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(vi) Issue at Discount and Redemption at Premium When the debentures are issued at discount and redeemable at premium, then the following Journal entry is passed.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 6. Differentiate between redemption of debentures out of capital and out of profits.
Answer Debentures can be redeemed out of capital and out of profits. The following are the difference between these two methods.
Redemption of Debentures Out of Capital: This is the situation where debentures are redeemed out of capital and no profits are utilised for redemption of the debentures, such redemption is termed as redemption out of capital. In this situation, no profits are required to be transferred to the Debenture Redemption Reserve (DRR).
Here it is to be remembered that no company can redeem its debenture purely out of capital because as per the guideline laid down by Securities and Exchange Board of India (SEBI) and the Section 117C of Company Act of 1956, before starting any redemption process a company is required to create a DRR equal to 50% of the debentures issued).
Therefore, it is not possible to redeem debentures purely out of capital, as it reduces the value of assets. There are exceptions in the following case
(i) Infrastructure companies (i.e., those companies that are engaged in the business of developing, maintaining and operating infrastructure facilities)
(ii) A Company that issues debentures with a maturity up to 18 months.
(iii) In case of convertible debentures and convertible portion of partly convertible debentures.
Redemption of Debenture Out of Profits:When debentures are redeemed out of profit then no capital is utilised for redemption. Before redeeming the debentures profits are transferred to DRR from Profit and Loss Appropriation Account. The creation of DRR is mandatory as per the guidelines laid down by Securities and Exchange Board of India (SEBI).

SEBI mandates transferring amount equal to 50% of debentures issued to DRR before redeeming debentures. As transfer of amount (profits) to the DRR from Profit and Loss Appropriation Account reduces the amount of profit available for distribution of dividend, so this redemption process is known as redemption out of profit.

DRR is shown under the head of Reserves and Surpluses on the Liabilities side of the Balance Sheet. DRR account is closed by transferring it to General Reserve only when all the debentures are redeemed.

Question 7. Explain the guidelines of SEBI for creating Debenture Redemption Reserve.
Answer Securities and Exchange Board of India (SEBI) have provided some guidelines for

redemption of debentures. The focal points of these guidelines are *
(i) Every company shall create Debenture Redemption Reserve in case of issue of debenture redeemable after a period of more than 18 months from the date of issue.
(ii) The creation of Debenture Redemption Reserve is obligatory only for non-convertible debentures and non-convertible portion of partly convertible debentures.
(iii) A company shall create Debenture Redemption Reserve equivalent to at least 50% of the amount of debenture issue before starting the redemption of debenture.
(iv) Withdrawal from Debenture Redemption Reserve is permissible only after 10% of the debenture liability has already been reduced by the company.

SEBI guidelines would not apply under the following situations:
(i) Infrastructure company (a company wholly engaged in the business of developing, maintaining and operating infrastructure facilities), and
(ii) A company issuing debentures with a maturity period of not more than 18 months.

Question 8. Describe the steps for creating Sinking Fund for redemption of debentures.
Answer The steps involved in creation of Sinking Fund on redemption of Debenture are
(i) Calculate the amount of profit to be set-aside annually with the help of sinking fund table.
(ii) Set aside the amount of profit at the end of each year and credit to Debenture Redemption Fund (DRF) Account.
(iii) Purchase the investments of the equivalent amount at the end of first year and debit Debenture Redemption Fund Investment (DRFI) Account.
(iv) Receive interest on investment at the end of each subsequent year.
(v) Purchase the investments equivalent to the fixed amount of profit set aside and the interest earned every year except last year (year of redemption).
(vi) Receive interest on investment for the last year.
(vii) Set aside the fixed amount of profit for the last year.
(viii) Encash the investments at the end of the year of redemption.
(ix) Transfer the profit/loss on sale of investments reflected in the balance of Debenture Redemption Fund Investment Account to Debenture Redemption Fund Account.
(x) Make payment to debenture holders.
(xi) Transfer Debenture Redemption Fund A/c balance to General Reserve.

Question 9. Can a company purchase its own debentures in the open market? Explain.
Answer Yes, a company, if authorised by its Articles of Association, can purchase its own debentures in the open market. The main purposes of such purchase may be as follows
(i) A company may purchase its own debenture for immediate cancellation for reducing the debenture liability especially in case when the interest rate on its debenture is higher than the market rate of interest.
(ii) A company may also purchase its own debentures with the motive of investment and sell them at higher price in future and thereby earn profit.

When a company purchase its own debenture,in the open market it can happen in either of the two ways first debentures may be purchased at premium for cancellation and debenture may be purchase at discount for cancellation. The following will be the accounting treatment in both the situation

(i) If Debentures are Purchased at Discount for Cancellation :When the company purchase its own debentures at discount for cancellation, then the following Journal entries are recorded.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 10. What is meant by conversion of debentures? Describe the method of such a conversion.

Answer The debentures can also be redeemed by converting them into shares or new debentures. If debenture holders find that the offer is beneficial to them they may convert his/her debentures into shares or new debentures after the expiry of a specified period of time, then this whole process is known as redemption of debentures by conversion.

It is worth mentioning here that in such a case no Debenture Redemption Reserve is required because no funds are required for redemption.

If a debenture holder exercises the conversion option, then the issue price of shares must be equal to or less than the amount .actually received from debentures. The accounting treatment in that case will be as follows:

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

NUMERICAL PROBLEMS

1. G.Ltd. issued 75,00,000, 6% Debenture of Rs.50 each at par payable Rs.15 on application and Rs.35 on allotment, redeemable at par after 7 years from the date of issue of debenture. Record necessary entries in the books of Company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. Y.Ltd. issued 2,000, 6% Debentures of Rs.100 each payable as follows: Rs.25 on application; Rs.50 on allotment and Rs.25 on First and Final call.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

3. A.Ltd. issued 10,000, 10% Debentures of Rs.100 each at a premium of 5% payable as follows:
Rs.10 on Application;
Rs.20 along with premium on allotment and balance on First and Final call.
Record necessary Journal Entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

4. A. Ltd. issued 90,00,000, 9% Debenture of Rs.50 each at a discount of 8%, redeemable at par any time after 9 years. Record necessary entries in the books of A. Ltd.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

5. A.Ltd. issued 4,000, 9% Debentures of Rs.100 each on the following terms:
Rs.20 on Application;
Rs.20 on Allotment;
Rs.30 on First call; and
Rs.30 on Final call.
The public applied for 4,800 Debentures. Applications for 3,600 Debentures were accepted in full. Applications for 800 Debentures were allotted 400 Debentures and applications for 400 Debentures were rejected.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

6. T. Ltd. offered 2,00,000, 8% Debenture of Rs.500 each on June 30, 2002 at a premium of 10% payable as Rs.200 on application (including premium) and balance on allotment, redeemable at par after 8 years. But application are received

for 3,00,000 debenture and the allotment is made on pro-rata basis. All the money due on application and allotment is received. Record necessary entries regarding issue of debenture.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

7. X.Ltd. invites application for the issue of 10,000, 14% debentures of Rs.100 each payable as to Rs.20 on application, Rs.60 on allotment and the balance on call. The company receives applications for 13,500 debentures, out of which applications for 8,000 debentures are allotted in full, 5,000 only 40% and the remaining rejected. The surplus money on partially allotted applications is utilised

towards allotment. All the sums due are duly received.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

8. R.Ltd. offered 20,00,000, 10% Debenture of Rs.200 each at a discount of 7% redeemable at premium of 8% after 9 years. Record necessary entries in the books of R. Ltd.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

9. M.Ltd. took over assets of Rs.9,00,00,000 and liabilities of Rs.70,00,000 of S.Ltd. and issued 8%Debenture of Rs.100 each. Record necessary entries in the books of M. Ltd.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

10. B.Ltd. purchased assets of the book value of Rs.4,00,000 and took over the liability of Rs.50,000 from Mohan Bros. It was agreed that the purchase consideration, settled at Rs,3,80,000, be paid by issuing debentures of Rs.100 each. What Journal entries will be made in the following three cases, if debentures are issued: (a) at par; (b) at discount; (c) at premium of 10%? It was agreed that any fraction of debentures be paid in cash.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

11. X.Ltd. purchased a Machinery from Y for an agreed purchase consideration of Rs.4,40,000 to be satisfied by the issue of 12% debentures of Rs.100 each at a premium of Rs.10 per debenture. Journalise the transactions.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

12. X.Ltd. issued 15,000, 10% debentures of Rs.100 each. Give journal entries and the Balance Sheet in each of the following cases:
(i) The debentures are issued at a premium of 10%;
(ii) The debentures are issued at a discount of 5%;
(iii) The debentures are issued as a collateral security to bank against a loan of Rs.12,00,000; and
(iv) The debentures are issued to a supplier of machinery costing Rs.13,50,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

13. Journalise the following:
(i) A debenture issued at Rs.95, repayable at Rs.100;
(ii) A debenture issued at Rs.95, repayable at Rs.105; and
(iii) A debenture issued at Rs.100, repayable at Rs.105;

The face value of debenture in each of the above cases is Rs.100.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

14. A.Ltd. issued 50,00,000, 8% Debenture of Rs.100 at a discount of 6% on April 01, 2000 redeemable at premium of 4% by draw of lots as under:
20,00,000 Debentures on March, 2002
10,00,000 Debentures on March, 2004
20,00,000 Debentures on March, 2005
Compute the amount of discount to be written-off in each year till debentures are paid. Also prepare discount/loss on issue of debenture account.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

15. A company issues the following debentures:
(i) 10,000, 12% debentures of Rs.100 each at par but redeemable at premium of 5% after 5 years;
(ii) 10,000, 12% debentures of Rs.100 each at a discount of 10% but redeemable at par after 5 years;
(iii) 5,000, 12% debentures of Rs.1000 each at a premium of 5% but redeemable at par after 5 years;
(iv) 1,000, 12% debentures of Rs.100 each issued to a supplier of machinery costing Rs.95,000. The debentures are repayable after 5 years; and
(v) 300, 12% debentures of Rs.100 each as a collateral security to a bank which has advanced a loan of Rs.25,000 to the company for a period of 5 years. Pass the journal entries to record the: (a) issue of debentures; and (b) repayment of debentures after the given period.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

16. A company issued debentures of the face value of Rs,5,00,000 at a discount of 6% on January 01, 2001. These debentures are redeemable by annual drawings of Rs,1,00,000 made on December 31 each year. The directors decided to write off discount based on the debentures outstanding each year.
Calculate the amount of discount to be written-off each year. Give journal entries also.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

17. A company issued 10% Debentures of the face value of Rs,1,20,000 at a discount of 6% on January 01, 2001. The debentures are payable by annual drawings of Rs.40,000 commencing from the end of third year.
How will you deal with discount on debentures? Show the discount on debentures account in the company ledger for the period of duration of debentures. Assume accounts are closed on December 31.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

18. B.Ltd. issued debentures at 94% for Rs.4,00,000 on April 01, 2000 repayable by five equal drawings of Rs.80,000 each. The company prepares its final accounts on December 31 every year.
Indicate the amount of discount to be written-off every accounting year assuming that the company decides to write off the debentures discount during the life of debentures. (Amount to be written-off: 2000 Rs.6,000; 2001 Rs.6,800; 2002 Rs.5,200; 2003 Rs.3,600; 2004 Rs.2,000; 2005 Rs.400).

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

19. B. Ltd. issued 1,000, 12% debentures of Rs.100 each on January 01, 2005 at a discount of 5% redeemable at a premium of 10%. Give journal entries relating to the issue of debentures and debentures interest for the period ending December 31, 2005 assuming that interest is paid half yearly on June 30 and December 31 and tax deducted at source is 10%. B.Ltd. follows calendar year as its accounting year.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

20. What journal entries will be made in the following cases when company redeems debentures at the expiry of period by serving the notice: (a) when debentures were issued at par with a condition to redeem them at premium; (b) when debentures were issued at premium with a condition to redeem that at par; and (c) when debentures were issued at discount with a condition to redeem them at premium?

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

21. On January 01, 1998, X. Ltd. issues 5,000, 8% Debentures of Rs.100 each repayable at par at the end of three years. It has been decided to set up a cumulative sinking fund for the purpose of their redemption. The investments are expected to realise 4% net. The Sinking Fund Table shows that Rs.0.320348 amounts to one rupee @4% per annum in three years. On December 31, 2000 the balance at bank was Rs.2,42,360 and the investments realised Rs.3,25,000. The debentures were paid off. Give journal entries and show ledger account.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

22. On January 01, 2003 a company issued 15% debentures of Rs.10,00,000 at par. The debentures were redeemable at par after three years on December 31, 2003. A sinking fund was set up to raise funds for redemption of debentures. The amount for the purpose was invested in 6% Government securities of Rs.100 each available at par. The sinking fund table shows that if investments earn 6% per annum, to get Re.1 at the end of 3 years, one has to invest Rs.0.31411 every year together with interest that will be earned. On December 31, 2005, all the Government securities were sold at a total loss of Rs. 6,000 and the debentures were redeemed at par. Prepare Debentures Account Sinking Fund Account, Sinking Fund Investment Account and Interest on Sinking Fund Investment Company closes its books of accounts every year on December 31.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

23. On January 01, 2004 the following balances appeared in the books of Z. Ltd.:

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

The investments consisted of 4% Government securities of the face value of Rs.90,000. The annual instalment was Rs.16,400. On December 31, 2004, the balance at Bank was Rs.26,000 (after receipt of interest on D.R.Reserve Fund Investment). Investments were realised at 92% and the Debentures were redeemed. The interest for the year had already been paid. Show the ledger accounts affecting redemption.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

24. **The following balances appeared in the books of A.Ltd. on January 01, 2004**

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

On January 01, 2004, the company redeemed all the debentures at 105 per cent out of funds raised by selling all the investments at Rs.3,48,000. Prepare the necessary ledger accounts.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

25. The following balances appeared in the books of Z.Ltd. on January 01, 2004

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

The annual instalment added to the fund is Rs.20,575. On December 31, 2004, the bank balance after the receipt of interest on the investment was Rs.39,100. On that date, all the investments were sold at 83 per cent and the debentures were duly redeemed. Show the necessary ledger accounts for the year 2004.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

26.What entries for the redemption of debentures will be done when : (a) debentures are redeemed by annual drawings out of profits; (b) debentures are redeemed by drawing a lot out of capital; and (c) debentures are redeemed by purchasing them in the open market when sinking fund for the redemption of debentures is not maintained – (i) when out of profit, and (ii) when out of capital?

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

27. A. Ltd. Company issued Rs,5,00,000 Debentures at a discount of 5% repayable at par by annual drawings of Rs.1,00,000.
Make the necessary ledger accounts in the books of the company for the first year.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

28. X.Ltd. issued 5,000, 15% debentures of Rs.100 each on January 01, 2004 at a discount of 10%, redeemable at a premium of 10% in equal annual drawings in 4 years out of capital.
Give journal entries both at the time of issue and redemption of debentures.
(Ignore the treatment of loss on issue of debentures and interest.)

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

29. Z.Ltd. issued 2,000, 14% debentures of Rs.100 each on January 01, 2005 at a discount of 10%, redeemable at a premium of 10% in equal annual drawings in 4 years out of profits.
Give journal entries both at the time of issue and redemption of debentures.
(Ignore the treatment of loss on issue of debentures and interest.)

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

30. A.Ltd. purchased its own debentures of the face value of Rs.2,00,000 from the open market for immediate cancellation at Rs.92. Pass the journal entries.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

31.A.Ltd. purchased for cancellation Rs.50,000 of its 15% debentures at Rs.98. The expenses of purchase amounted to Rs.50. On January 01, 2002, X.Ltd. issued 40,000, 9% debentures of Rs.100 each at Rs.95. The terms of issue provided that,

beginning with 1999, Rs.2,00,000 debentures should be redeemed either by drawings at par or by purchase in the open market every year. The expenses of issue amounted to Rs.12,000 which were written-off in 2002. The company also wrote off Rs.40,000 every year from Discount on Debentures Account. At the end of 2004, debentures to be redeemed were repaid by drawings. During 2005, the company purchased for cancellation 2,000 debentures at the market price of Rs.98 on December 31, the expenses being Rs.400. Interest on debentures is payable at the end of every calendar year. Pass the journal entries in the books of the company to record these transactions.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

32. A.Ltd. redeemed 8,000, 12% debentures of Rs.100 each which were issued at a discount of 5%, by converting them into equity shares of Rs.10 each at par.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

33. Y.Ltd. redeemed 4,800, 12% debentures of Rs.100 each which were issued at par, at 110 per cent by converting them into equity shares of Rs.10 each issued at a discount of 4%. Journalise.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

34. Z.Ltd. redeemed 2,000, 12% debentures of Rs.100 each which were issued at a discount of 5%, by converting them into equity shares of Rs.10 each issued at a premium of 25%. Journalise.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

35. X.Ltd. redeemed 1,000, 12% debentures of Rs.50 each by converting them into 15% New Debentures of Rs.100 each. Journalise.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 3 Financial Statements of a Company

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TEST YOUR UNDERSTANDING I

• State whether the following statements are true or false.
(a) Financial statements are the end products of accounting process.
Answer True
(b) Financial statements are primarily directed towards the needs of owners.
Answer True

(c) Facts and figures presented in financial statements are not at all based on personal judgements.
Answer False
(d) Recorded facts are based on replacement cost.
Answer False
(e) Going Concern concept assumes that the enterprise continues for a long-period of time.
Answer True

• **Fill in the blanks with appropriate word(s)**
(a) Financial statements are the—————of information to interested parties.
Answer Basic sources
(b) The owners of a company are called ————————
Answer Shareholders
(c) For income measurement––––––basis of accounting is followed.
Answer Accrual . .
(d) The statement which shows the assets and liabilities of a company is known as——————-.
Answer Balance sheet
(e) Profit and loss account is also called—————-statement.
Answer Income

TEST YOUR UNDERSTANDING II

Question 1. What are the items shown under heading 'Reserve and Surplus'?
Answer Capital Reserve, Capital Redemption Reserve, Securities Premium other reserves, profit and loss account.

Question 2. What are the items shown under heading 'Miscellaneous Expenditure?
Answer Preliminary expenses, discount on Issue of share and debenture other deferred expenses and profit and loss account (debit balance).

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

SHORT ANSWER TYPE QUESTIONS

Question 1. State the nature of financial statements.
Answer Financial statements are the summarised reports of recorded-facts and are prepared following the accounting concepts, conventions and requirements of Law.
The American Institute of Certified Public Accountants states the nature of financial statements as,

“the statements prepared for the purpose of presenting a periodical review of report on progress by the management and deal with the status of investment in the business and the results achieved during the period under review.

The following points explain the nature of financial statements

(i) Recorded Facts :Financial statements are prepared on the basis of facts in the form of cost data recorded in accounting books. The

original cost or historical cost is the basis of recording transactions. The figures of various accounts such as cash in hand, cash at bank, bills receivable, sundry debtors, fixed assets, etc are taken as per the figures recorded in the accounting books.

The assets purchased at different times and at different prices are put together and shown at costs. As these are not based on market prices, the financial statements do not show current financial condition of the concern.

(ii) Accounting Conventions: Certain accounting conventions are followed

while preparing financial statements. The convention of valuing inventory at cost or market price, whichever is lower, is followed. The valuing of assets at cost less depreciation principle for balance sheet purposes is followed. •

The convention of materiality is followed in dealing with small items like penci’s, pens, postage stamps, etc. In this way the use of accounting conventions makes financial statements comparable, simple and realistic.

(iii) Based on Concepts: Financial statements are prepared on certain basic assumptions (prerequisites) known as Concepts such as going concern concept, money measurement concept, realisation concept, etc. Going concern concept assumes that the enterprise is treated as a going concern and exists for a longer period of time. So the assets are shown on historical cost basis. Money measurement concept assumes that the value of money will remain the same in different periods. While, preparing profit and loss account the revenue is included in the sales of the year in which the sale was undertaken even though the sale price may be received over a number of years. The assumption is known as realisation concept.

(iv) Personal Judgements: Under more than one circumstance, facts and figures presented through financial statements are based on personal opinion, estimates and judgements.

The depreciation is provided taking into consideration the useful economic life of fixed assets. Provisions for doubtful debts are made on estimates and personal judgments. In valuing inventory, cost or market value, whichever is less is being followed.

Question 2. Briefly explain the importance of preparing financial statements.

Answer Significance of Financial Statement :The users of financial statements include Shareholders, Investors, Creditors, Lenders, Customers, Management, Government, etc. Financial statements help all the users in their decision-making process. They provide data about general purpose needs of these members.

The various uses and importance of financial statements are as follows

(i) Reporting to the Share Holders: Financial statements report the performance of the management to the shareholders. The gaps between the management performance and ownership expectations can be understood with the help of financial statements.

(ii) Basis for Fiscal Policies :The fiscal policies, particularly taxation policies of the government, are related with the financial performance of corporate undertakings. The financial statements provide basic input for industrial, taxation and other economic policies of the government.

(iii) Basis for Granting of Credit: Corporate undertakings have to borrow funds from banks and other financial institutions. for different purposes. Credit granting institutions take decisions based on the financial performance of the undertakings. Thus, financial statements form tf\e basis for granting of credit.

(iv) Basis for Prospective Investors :The investors include both short-term and long-term investors. Their prime considerations in their investment decisions are security and liquidity of their investment with reasonable profitability. Financial statements help the investors to assess long term and short-term solvency as well as the profitability of the concern.

(v) Aids Trade Associations in Helping their Members: Trade associations may analyse the financial statements for the purpose of providing service and protection to their members. They may develop standard ratios and design uniform system of accounts.

(vi) Helps Stock Exchanges: Financial statements help the stock exchanges to understand the extent of transparency in reporting on financial performance and enables them to call for required information to protect the interest of investors.

Question 3. What are the limitations of financial statements?

Answer Financial statements are very useful to an organisation but still , they suffer from the following limitations

(i) Historical Data :Financial statements are prepared on the basis of historical cost. Since the purchasing power of money is changing, the values of assets and liabilities shown in financial statement do not reflect current market situation.

(ii) Assets May not Realise: Accounting is done on the basis of certain conventions. Some of the assets may not realise the stated values, if the liquidation is forced on the company. Assets shown in the balance sheet reflect merely unexpired or unamortised cost.

(iii) Bias: Financial statements are the outcome of recorded facts, accounting concepts and conventions used and personal judgments made in different situations by the accountants. Hence, bias may be observed in the results, and the financial position depicted in financial statements may not be realistic.

(iv) Aggregate Information: Financial statements show aggregate information but not detailed information. Hence, they may not help the users in decision-making much.

(v) Vital Information Missing: Balance sheet does not disclose information relating to loss of markets, and cessation of agreements, which have vital bearing on the enterprise.

(vi) No Qualitative Information: Financial statements contain only monetary information but not qualitative information like industrial relations, industrial climate, labour relations, quality of work, etc.

(vii) They are Only Interim Reports: Profit and loss account discloses the profit/loss for a specified period. It does not give an idea about the earning capacity over time similarly, the financial position reflected in balance sheet is true at that point of time, the likely change on a future date is not depicted.

Question 4. Prepare the format of income statement and discuss its elements.

Answer Income statement may also be presented in vertical form with detailed data. This is considered more suitable for further analysis and providing necessary data for decision-making. The form and contents of vertical income statement is shown below (Vertical Form)

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 5. Prepare the format of balance sheet and discuss its elements.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Elements of Balance Sheet: A brief description of various element of balance sheet is given below
Description of Elements at the Liabilities Side of Balance Sheet
(i) Share Capital :This is the first thing which is being shown in the liabilities side of balance sheet. It consists of the following items
(a) Authorised Capital
(b) Issued Capital Equity share and preference share.
(c) Subscribed Capital less Call in Arrears add Forfeited Shares

(ii) Reserve and Surplus: As per the Schedule VI, it consists of the following items
(a) Capital Reserve
(b) Capital Redemption Reserve
(c) Security Premium
(d) Other Reserve less Debit Balance of Profit and Loss account
(e) Surplus Credit Balance of Profit and Loss account
(f) Proposed Additions
(g) Sinking Fund

(iii) Secured Loans:
(a) Debentures
(b) Loan and advances from bank etc.

(iv) Unsecured Loans:
(a) Fixed Deposits
(b) Loan and Advances from subsidiaries

(v) Current Liabilities: Current Liabilities are those liabilities which are liable to pay with in an operating cycle generally one year; e.g., bank overdraft creditors, bills payable, outstanding wages, short term loans, etc are called current liabilities.

Description of Elements at the Liabilities Sfde of Balance Sheet
(i) **Fixed Assets**: These are those assets that are used for more than one year, like, Goodwill, Land and Building, Plant and Machinery, Motor Car, Patents, Trade Marks, Livestock etc.
(ii) **Investments** :Under this head, various investments made such as investment in government securities or trust securities; investment in shares, debentures, and bonds of other companies, immovable properties, etc., are to be shown separately in the balance sheet.
(iii) **Current Assets**: Assets which are converted into cash within an operating cycle is known as current assets. In other words current assets are required to run day to day business activities; e.g., cash, debtors, stock, etc.
(iv) **Miscellaneous Expenditure**: The expenditure which has not been written of fully its balance is shown under this heading. These expenses include preliminary expenses, advertisement expenditure, discount on issue of shares and debentures, share issue expenses, etc.
(v) **Profit and Loss Account**: When the Profit and Loss account shows a debit balance, i.e., loss which could not be adjusted against general reserves, the same is shown as a last item on the asset side.

LONG ANSWER TYPE QUESTIONS

Question 1. Explain how financial statements are useful to the various parties who are interested in the affairs of an undertaking?
Answer The various parties interested in financial statements directly or indirectly can be categorised in two broad categories
(i) **Internal Parties**: The following are the internal parties directly related to the company and interested in financial statements.
(a) **Owner** :The owner/s is/are interested in the profit earned or loss incurred during an accounting period. They are interested in assessing the profitability and viability of the capital invested by them in the business.
(b) **Management**: Management interested in financial statements for drafting various policies measures, facilitating planning and decision making process.
(c) **Employees and Workers**: The employee and workers are interested in financial statement for knowing about the timely payment of wages and salaries, bonus and appropriate increment in their wages and salaries. Financial statement enables them to know about the figure of profit earned during the year.
(ii) **External Parties** :There are various external parties who are interested in financial statements for a number of reasons.

The following are the various external parties.
(a) **Creditors**: Creditors are always interested in financial statement to gather information about

credit worthiness of the business.
(b) **Investors and Potential Investors**: Persons who are willing to invest in any organisation always wish to know about the profitability and solvency of the business concern. Hence, in order to assess the viability and prospectus of their investment, creditors need information about profitability and solvency of the business.
(c) **Consumers**: The survival and growth of any organisation largely depends upon the Goodwill earned in the heart of the customers. In this regards if the Business has transparent financial records it help in assisting the customers to know the correct cost of production and accordingly assess the degree of reasonability of the price charged by the business.
(d) **Banks/Financial Institutions**: Banks and financial institutions provide finance in the form of loans and advances to various businesses. Thus, they need information regarding liquidity, creditworthiness, solvency and profitability to advance loans.
(e) **Tax Authorities**: They need information about sales, revenues, profit and taxable income in order to determine and levy various types of tax on the business.
(f) **Government** :It needs information to determine national income, GDP, industrial growth, etc. The accounting information assist the government in the formulation of various policies measures and to address various economic problems like employment, poverty etc.
(g) **Researchers** :Various research institutes like NGOs and other independent research institutions undertake various research projects and the accounting information facilitates their research work.

Question 2. Financial statements reflect a combination of recorded facts, accounting conventions and personal judgements. Discuss.
Answer The financial statements not only help in presenting the true and real financial position of the company but they also help in taking managerial decisions. The nature of the financial statements depends upon the following aspects like recorded facts, conventions, concepts and personal judgement.
(i) **Recorded Facts**: The items recorded in the financial statements reflect their original cost i.e., the cost at which they were acquired. Consequently, financial statements do not reveal the current market price of the items. Further, financial statements fail to capture the inflation effects.
(ii) **Accounting Conventions**: The preparation of financial statements is based on some accounting conventions like, Prudence Convention, Materiality Convention, Matching Concept, etc. The adherence to such accounting conventions makes financial statements easy to understand, comparable and reflects the true and fair financial position of the company. Besides the above while preparing financial statements, certain concepts are adhered to. The nature of these concepts is reflected in the nature of the financial statements.
(iii) **Personal Judgements**: The nature of financial statement largely depends upon the personal value judgements. Personal judgements are attached to different practices of recording transactions in the financial statements, e.g., recording stock either at market value or at the cost requires value judgement depending upon the personal judgement. Thus, personal judgements help in determining the nature of the financial statements.

Question 3. Explain the process of preparing income statement and balance sheet.
Answer The process of preparing income statement is explained below
(i) First of all a Trial Balance is prepared on the basis of the balances of various accounts in the ledger.
(ii) After that trading account is prepared by recording Opening Stock, Purchases, Manufacturing Expenses and other direct expenses on the debit side.
(iii) On the other hand sales and closing stock is recorded on the credit side of the trading account.
(iv) After that the balancing figure of trading account is determined by totalling both the sides, if the credit side exceeds the debit side, then the balancing figure is termed as gross profit, but if the debit side exceeds the credit side, then the balancing figure is termed as gross loss.

(v) Carry forward the Gross Profit (Gross Loss) to the credit (debit) side of the Profit and Loss Account.
(vi) After that all the operating and non-operating revenue expenditures with their relevant adjustments are recorded on the debit side of the profit and loss account. Record all current year's operating and non operating revenue incomes with their relevant adjustments on the credit side of the profit and loss account.
(vii) Ascertain the balancing figure by totalling both the sides of the profit and loss* account. If the credit exceeds the debit side, then the balancing figure is termed as net profit, but if the debit side exceeds the credit side, then the balancing figure is termed as net loss.

The process of preparing Balance Sheet is given below
(i) First of all match the total of both the side of trail balance. If there is any difference in the debit side of trail balance it will be posted in assets side of balance sheet and if there is any difference in credit side of balance sheet it will be posted in the liabilities side of the balance sheet.
(ii) Record all the debit balances of real and personal accounts on the left hand side (i.e., Assets side) of the balance sheet after making all adjustments for provision and other related items.
(iii) Record all the credit balances of real and personal accounts on the right hand side (i.e., Liabilities side) of the balance sheet after making all adjustments for interest and outstanding items.
(iv) Add Net Profit to the opening capital and deduct Net Loss, if any from the opening capital.
(v) Acertain the total of two sides, which must be equal.

NUMERICAL QUESTIONS

Question 1. The following is the trial balance on June 30, 2011 of the Modern Manufacturing Company Ltd.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

stock, on June 3, 2011 Rs. 8,200, you are required to make out the trading account, and profit and loss account for the year ended June 30, 2011 and the balance sheet as on the date, you are also to make provision in respect of the following: (i)Depreciate , machinery @10% per annum; (ii) Reserve 5% for discount on debtors; (iii) One month rent Rs. 45 was due on 30th june; and (iv)six moth's insurance, included in general expenses, was unjexpired at Rs.75.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note: Reserve for discount on debtors is rounded off to next rupee. The actual amount calculated was Rs. 187.50.
It has been assured that the dividend paid, August 2005 of Rs. 500 has been declared and paid is the same accounting period.
as per Revised Schedule VI applicable from 2013 Board examinations, balance sheet will be prepared as given below

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. The following is the trial balance of Alfa Ltd, for the year ended June 30, 2011

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Prepare the profit and loss account and balance sheet of the company after taking the following particulars into consideration
(a) The original cost of land and building plant and machinery and furniture and fittings was Rs. 2,50,000, Rs. 6,00,000 and Rs. 60,000 respectively- Additions during the year were building Rs. 50,000 and plant Rs. 20,000.
(b) Depreciation is to be charged on plant and machinery and furniture and fitting at 10 per cent on original cost
(c) Of the sundry debtors, Rs. 10,000 is outstanding for a period exceeding 6 months, Rs. 5,000 are considered doubtful, while the others are considered good.
(d) The directors are entitled to a commission at 1 per cent of the net profits before charging such commission.
(e) Stock on 30th June, 2005 is Rs. 1,30,000.
(f) Provide Rs.34,800 for income tax.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

3. The following balances appeared in the books of Parasuram Flour Mills Ltd., as on December 31, 2005 :

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Prepare the company's trading and profit and loss account for the year and balance

sheet as on December 31, 2005 after taking the following adjustments into account: (a) Stock on December 31, 2005 were: Wheat at cost, Rs. 14,900: Flour at market price, Rs. 21,700; (b) Outstanding expenses: Manufacturing expenses, Rs. 23,500; and salaries and wages, Rs. 1,200; (c) Provide depreciation : Building at 2% ; Plant and machinery at 10%: Furniture at 10% ; and Vehicle 20%. (d) Interest accrued on Government Securities, Rs.100: (e) A tax provision of Rs. 8,000 is considered necessary. (f) The directors propose a dividend of 20%. (g) The authorised capital consists of 12,000 equity shares of Rs. 10 each of which 7,200 shares were issued and fully paid up.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note :Pension fund is assumed to be created out of profits. Dividend ? 9,000 is considered as declared and paid in same year.

As per Revised Schedule VI applicable from 2013 Board examinations, balance sheet will be prepared as given below.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

4. An unexperienced accountant prepared the following trial balance of Bang Vikas Ltd., for the year ending 31.12.2005. The cash in hand on 31.12.2005 was Rs. 750.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

After locating the mistakes and making the following adjustments prepare trading and profit and loss account and balance sheet in the prescribed form.

Adjustments: (i) Stock on 31.12.2005 Rs. 95,000 and (ii) Write-off preliminary expenses.

Note: Rectified trial balance need not be prepared

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

As per Revised Schedule VI applicable from 2013 Board examinations, balance sheet will be prepared as given below

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Working Note: Firstly the rectified trial balance will be made then the final accounts will be prepared.

Note: When the trial balance does not tally, it should be balanced by writing the difference amount on either side as required and then show it in balance sheet

5. The Silver Ore Co. Ltd. was formed on April 1, 2005 with an authorised capital of Rs.6,00,000 in shares of Rs. 10 each. Of these 52,000 shares had been issued and subscribed but there were calls in arrear on 100 shares @ Rs. 2.50. From the following trial balance as on March 31, 2006 prepare the trading and profit and loss account and the balance sheet:

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(i) Depreciate plant and railways by 10%; furniture and building by 5%;
(ii) Write off a third of the promotion expenses;
(iii) Value of silver ore on March 31, 1969 Rs.15,000. The directors forfeited on December 20, 1968, 100 shares on which only Rs. 7.50 had been paid

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

As Per Revised Schedule VI applicable from 2013 Board examinations, balance sheet will be prepared as given below

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 4 Analysis of Financial Statements

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TEST YOUR UNDERSTANDING I

• **Fill in the blanks with appropriate word(s).**
Question 1. Analysis simply means———data.
Answer Simplification .

Question 2. Interpretation means————-data.
Answer Explaining

Question 3. Comparative analysis is also known as——————Analysis.
Answer Horizontal

Question 4. Common size analysis is also known as——————Analysis
Answer Vertical

Question 5. The analysis of actual movement of money inflow and outflow in an organisation is called———-analysis.
Answer cash flow

DO IT YOURSELF I

From the following balance sheet and income statement of Day Dreaming Co.Ltd., for the year ending 2002 and 2003, prepare the comparative statements.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

DO IT YOURSELF II

The following are the Balance Sheets of Harsha Ltd. as on March 31, 2006 and March 31, 2007

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

TEST YOUR UNDERSTANDING – II

Choose the right answer :
1. The financial statements of a business enterprise include:
(a) Balance sheet

(b) Profit and loss account
(c) Cash flow statement
(d) All the above
Answer (d) All of above

2. The most commonly used tools for financial analysis are:
(a) Horizontal analysis
(b) Vertical analysis
(c) Ratio analysis
(d) All the above
Answer (d) All of above

3. An Annual Report is issued by a company to its:
(a) Directors
(b) Auditors
(c) Shareholders
(d) Management
Answer (c) Shareholders

4. Balance Sheet provides information about financial position of the enterprise:
(a) At a point in time
(b) Over a period of time
(c) For a period of time
(d) None of the above
Answer (a) At a Point of time

5. Comparative statement are also known as:
(a) Dynamic analysis
(b) Horizontal analysis
(c) Vertical analysis
(d) External analysis
Answer (b) Horizontal analysis

DO IT YOURSELF III

Question 1. The following data is available from the P&L Account of Deepak Limited

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

TEST YOUR UNDERSTANDING III

• **State whether each of the following is true or false**

(a) The financial statements of a business enterprise include funds flow statement.
Answer False

(b) Comparative statements are the form of horizontal analysis.
Answer True

(c) Common size statements and financial ratios are the two tools employed in vertical analysis.
Answer True

(d) Ratio analysis establishes relationship between two financial statements.
Answer False

(e) Ratio analysis is a total for analysing the financial statements of any enterprise.
Answer True

(f) Financial analysis is used only by the creditors.
Answer False

(g) Profit and loss account shows the operating performance of an enterprise for a period of time.
Answer True

(h) Financial analysis helps an analyst to arrive at a decision.
Answer True

(i) Cash flow statement is a tool of financial statement analysis.
Answer True

(j) In a common size statement each item is expressed as a percentage of some common base.
Answer True

SHORT ANSWER TYPE QUESTIONS

Question 1. List the techniques of Financial Statement Analysis.
Answer The following are the commonly used techniques of Financial Statement analysis
(i) Ratio Analysis (li) Cash Flow Statement
(iii) Fund Flow Statement
(iv) Comparative Financial Statements
(v) Common Size Financial Statements
(vi) Trend Analysis

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 3. Explain the meaning of Analysis and Interpretation.
Answer Analysis and Interpretation refers to a systematic and critical examination of the financial statements. It not only establishes cause and effect relationship among the various items of the financial statements but also presents the financial data in a proper manner.
The main purpose of Analysis and Interpretation is to present the financial data in such a manner that is easily understandable and self explanatory. This not only helps the accounting users to assess the financial performance of the business over a period of time but also enables them in decision making and policy and financial designing process.

Question 4. Bring out the importance of Financial Analysis.
Answer Financial Analysis has great importance to various accounting US' on various matters. Income Statements, Balance Sheets and other financ data that provides information about expenses and sources of income, profi loss and also helps in assessing the financial position of a business. The financial data are not useful until they are analysed. There are various tools a methods such as Ratio

Analysis, Cash Flow Statements that make the financ data to cater varying needs of various accounting users.
The following are the reasons that advocate in favour of Financial Analys
(i) It helps in evaluating the profit earning capacity and financ feasibility of a business.
(ii) It helps in assessing the long-term solvency of the business.
(iii) It helps in evaluating the relative financial status of a firm comparison to other competitive firms.
(iv) It assists management in decision making process, plans and also in establishing an effective controlling

Question 5. What are Comparative Financial Statements?
Answer Those financial statements that enable intra-firm and comparisons of financial statements over a period of time are called Comparative Financial Statements. In other words, these statements help the accounting users to evaluate and assess the financial progress in the relative terms.
These statements express the absolute figures, absolute change and the percentage change in the financial items over a period of time. Comparative Financial Statements present the financial data in such a manner that is easily understandable and can be analysed without any ambiguity. If the accounting policies and practices for the treatment of the items are same over the period of study, only then the Comparative Financial Statements enable meaningful comparisons.

The following are the two Comparative Financial Statements that are commonly prepared
(i) Comparative Balance Sheet
(ii) Comparative Income Statements

Question 6. What do you mean by Common Size Statements?
Answer These statements depict the relationship between various items of financial statements and some common items (like Net Sales and the Total of Balance Sheet) in percentage terms. In other words, various items of Trading and Profit and Loss Account such as Cost of Goods Sold, Non-Operating Incomes and Expenses are expressed in terms of percentage of Net Sales.
On the other hand, different items of Balance Sheet such as Fixed Assets, Current Assets, Share Capital etc are expressed in terms of percentage of Total of Balance Sheet. These percentage figures are easily comparable with that of the previous years' and with that of the figures of other firms in the same industry {i.e., inter-firm comparison) as well.
The analyses based on these statements are commonly known as Vertical Analysis.
The following are commonly prepared Common Size Statements.
(i) Common Size Balance Sheet
(ii) Common Size Income Statements

LONG ANSWER TYPE QUESTIONS

Question 1. Describe the different techniques of financial analysis and explain the limitations of financial analysis.
Answer The most commonly used techniques of financial analysis are as follows
(i) Comparative Statements: These are the statements showing the profitability and financial position of a firm for different periods of time in a comparative form to give an idea about the position of two or more periods. The financial data will be comparative only when same accounting principles are used in preparing these statements. Comparative figures indicate the trend and direction of financial position and operating results. This analysis is also known as 'horizontal analysis'.
(ii) Common Size Statements: These are the statements which indicate the relationship of different items of a financial statement with some common item by expressing each item as a percentage of the common item. The percentage thus calculated can be easily compared with the

results corresponding percentages of the previous year or of some other firms, as the numbers are brought to common base. Such statements also allow an analyst to compare the operating and financing characteristics of two companies of different sizes in the same industry. This analysis is also known as 'Vertical analysis'.

(iii) Trend Analysis : It is a technique of studying the operational results and financial position over a series of years. Using the previous years' data of a business enterprise, trend analysis can be done to observe the percentage changes over time in the selected data. Trend analysis is important because, with its long run view, it may point to basic changes in the nature of the business. By looking at a trend in a particular ratio, one may find whether the ratio is falling, rising or remaining relatively constant. From this observation, a problem is detected or the sign of good management is found. .

(iv) Ratio Analysis : It describes the significant relationship which exists between various items of a balance sheet and a profit and loss account of a firm. As a technique of financial analysis, accounting ratios measure the comparative significance of the individual items of the income and position statements.

(v) Cash Flow Analysis : It refers to the analysis of actual movement of cash into and out of an organisation. The flow of cash into the business is called as cash inflow or positive cash flow and the flow of cash out of the firm is called as cash outflow or a negative cash flow. The difference between the inflow and outflow of cash is the net cash flow.

Limitations of Financial Analysis

The following are the limitations of Financial Analysis

(i) Ignorance of Price Level Changes :Financial statement is based on historical cost method and fails to capture the change in price level. The figures of different years are taken on nominal values and not in real terms (i.e., not taking price change into considerations).

(ii) Misleading and Wrong information: The financial analysis fails to reveal the change in the accounting procedures and practices. Consequently, they may provide wrong and misleading information.

(iii) Fail to Provide Final Picture: The financial analysis presents only the interim report and thereby provides incomplete information. They fail to provide the final and holistic picture.

(iv) Consider Only Monetary Aspect: This is one of the limitations of financial analysis that it reveals only the monetary aspects. Only those items are considered here which can be measured in term of money and fail to disclose managerial efficiency, growth prospects, and other non-operational efficiency of a business.

(v) Non-Reliable Conclusions :Conclusion base on financial analysis may be non reliable because financial statement are based on certain concepts and conventions.

(vi) Involves Personal Biasness: The financial analysis reflects the personal biasness and personal value judgments of the accountants and clerks involved. There are different techniques used by different personnel for charging depreciation (original cost or written-down value method) and also for inventory valuation. The use of different techniques by different people reduces the effectiveness of the financial analysis.

(vii) Unsuitable for Comparisons :Due to the involvement of personal value judgment, personal biasness and use of different techniques by different accountant, various types of comparisons such as inter-firm and intra-firm comparisons may not be possible and reliable.

Question 2. Explain the usefulness of trend percentages in interpretation of financial performance of a company.

Answer The Trend Analysis presents each financial item in percentage terms for each year. These Trend Analysis not only help the accounting users to assess the financial performance of the business but also assist them to form an opinion about various tendencies and predict the future trend of the business.

Usefulness and Importance of Trend Analysis:
The following are the various importance of Trend Analysis
(i) **Assists in Forecasting**: The trends provided by Trend Analysis help the accounting users to forecast the future trend of the business.
(ii) **Percentage Terms**: The trends are expressed in percentage terms. Analysing the percentage figures is easy and also less time consuming.
(iii) **User Friendly**: As the trends are expressed in percentage figures, so it is the most popular financial analysis to analyse the financial performance and operational efficiency of the company. In other words, one needs not to have an in-depth and sophisticated knowledge of accounting in order to analyse these percentage trends.
(iv) **Presents a Broader Picture** :The trend analysis presents a broader picture about the financial performance, viability and operational efficiency of a business. Generally, companies prefer to present their financial data for a period of 5 or 10 years in forms of percentage trends.

Question 3. What is the importance of comparative statements? Illustrate your answer with particular reference to comparative income statement.
Answer The following are the importance of Comparative Statements.
(i) **Make Presentation Simpler** : Comparative statements presents the financial data in a simpler form. On the other hand, an year-wise data of the same items are presented side-by-side, which not only makes the presentation clear but also enables easy comparisons (both intra-firm and inter-firm) conclusive.
(ii) **Help in Drawing Conclusion**: The presentation of comparative statement is so effective that it helps the analyst to draw conclusion quickly and easily and that too without any ambiguity.
(iii) **Help in Forecasting** :The management may analyse the trend and forecast and draft various future plans and policy measures, with the help of comparative statement:
(iv) **Help in Detection of Problems** :The comparative analysis not only enables the management in locating the problems but also helps them to put various budgetary controls and corrective measures to check whether the current performance is aligned with that of the ” planned targets. With the help of the comparison of the financial data of two or more years, the financial management can easily detect the problems.

Question 4. What do you understand by analysis and interpretation of financial statements? Discuss their importance.
Answer Financial Analysis has great importance to various accounting users on various matters. Income Statements, Balance Sheets and other financial data‘provide information about expenses and sources of income, profit or loss and also helps in assessing the financial position of a business. These financial data are not useful until they are analysed. There are various tools and methods such as Ratio Analysis, Cash Flow Statements that make the financial data to cater varying needs of various accounting users.
The following are the reasons that advocate in favour of Financial Analysis
(i) It helps in evaluating the profit earning capacity and financial feasibility of a business.
(ii) It helps in assessing the long-term solvency of the business.
(iii) It helps in evaluating the relative financial status of a firm in comparison to other competitive firms.
(iv) It assists management in decision making process, drafting various plans and also in establishing an effective controlling system.

Question 5. Explain how common size statements are prepared giving an example.
Answer Common size statements can be classified into two broad categories
(i) Common Size Income Statements

(ii) Common Size Balance Sheet

Common Size Statement is prepared in a columnar form for analysis. In a Common Size Statement, each item of the financial statements is compared to a common item. The analyses based on these statements are commonly known as Vertical Analysis.

The following are the columns prepared in a Common Size Statement

(a) Particulars Column:This column shows the various financial items under their respective heads.

(b) Amount Columns :These columns depict the amount of each item, sub-totals and the gross total of a particular year.

(c) Percentage or Ratio Columns :These columns show the proportion of each item to the common item either in terms of percentage or ratio.

The Common Size Statements can be presented in the following two ways.

Method 1 Percentage column is shown beside the amount column of the year to which percentage column belongs.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Method 2 Amount columns are shown first and their percentage columns are shown after the amount columns.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Example :From the following information provided by Alfa Limited Prepare the Common Size Statements.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

NUMERICAL QUESTIONS

1. From the following information of Narsimham Company Ltd., prepare a Comparative Income Statement for the years 2004-2005

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Interpretation

(i) The Net Profit of the company increased.
(ii) Simultaneously the company has tried to reduce its costs to improve its profit margin.
(iii) Profitability of the company has improved over the year.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

2. The following are the Balance Sheets of Mohan Ltd., at the end of 2004 and 2005.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Prepare a Comparative Balance Sheet and study the financial position of the company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Comments

(i) Decrease in current Liabilities is more than decrease in current assets which indicates that the current ratio has improved.

(ii) Decrease in cash and bank may result in delay in payments.

(iii) Fixed Assets have increased along with share capital. It indicates that such asset has been purchased using Long term sources of finance.

(iv) Increase in reserve and surplus is a healthy indicator.

Question 3. The following are the balance sheets of Devi Company Limited at the end of 2011 and 2012. Prepare a comparative Balance Sheet and study the financial position of the concern.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Comments

(i) Change in current assets and current Liabilities is almost same. It indicates that ratio is same as of previous year.

(ii) Fixed Assets have increased along with share capital which shows that assets are purchased with long term sources of finance.

(iii) The overall financial position of company is satisfactory.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 4. Convert the following Income Statement into Common Size Statement and interpret the changes in 2011 in the light of the conditions in 2010.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Comment: Company has reduced its cost and expenses which has resulted in increase in income from operations and net profit.

Question 5. Following are the balance sheets of Reddy Limited as on 31 March, 2011 and 2012

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Analyse the financial position of the company with the help of the Common Size Balance Sheet.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Comments
(i) Inspite of decrease in current assets and current liabilities, the current ratio has improved.
(ii) Decrease in cash and bank balance indicates that there will be delay in payments.
(iii) Increase in fixed assets and share capital shows that assets are purchased with long term sources of finance.

Question 6. The accompanying balance sheet and profit and loss account related to SUMO Logistics Private Limited. Convert these into Common Size Statements. Previous Year = 2010, Current Year = 2011

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 7. From the following particulars extracted from P&L Account of 'Prashanth Limited, you are required to calculate trend percentages

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 8. Calculate trend percentages from the following figures of ABC Limited, taking 2000 as base and interpret them.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Interpretations
(i) Sales has exhibited continuous increasing trend over the period.
(ii) The value of stock also increases, with the increase in value of sales.
(iii) Profit increase more in earlier years as compare to later years. It implies cost of goods, sold and operating expenses are increased in later years.

Question 9. From the following data relating to the liabilities side of balance sheet of Madhuri Limited, as on 31st March, 2006, you are required to calculate trend percentages taking 2002 as the base year.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Effects of Revised Schedule VI on Tools of Analysis of Financial Statements As per revised Schedule VI part II the Format of Profit of Loss Statement is as follows.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 10. Prepare comparitive statements from the following.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 5 Accounting Ratios

Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 5 Accounting Ratios

Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 5 Accounting Ratios

TEST YOUR UNDERSTANDING I

• **State which of the following statements are True or False.**
(a) The only purpose of financial reporting is to keep the managers informed about the progress of operations.
Answer False

(b) Analyses of data provided in the financial statements a is termed as financial analysis.
Answer True

(c) Long term creditors are concerned about the ability of a firm to discharge its obligations to pay interest and repay the principal amount of term.
Answer True

(d) A ratio is always expressed as a quotient of one number divided by another.
Answer False

(e) Ratios help in comparisons of a firm's results over a number of accounting periods as well as with other business enterprises.
Answer True

(f) One ratios reflect both quantitative and qualitative aspects.
Answer False

DO IT YOURSELF I

Question 1. Current ratio =4.5:1,quick ratio =3:1, Inventory is Rs.36,000. Calculate the current assets and current liabilities.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. Current liabilities of a company are ? 5,60,000 current ratio is 5 : 2 and quick ratio is 2 : 1. Find the value of the stock.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 3. Current assets of a company are Rs. 5,00,000. Current ratio is 2.5 : 1 and quick ratio is 1 : 1. Calculate the value of current liabilities, liquid assets and stock.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

TEST YOUR UNDERSTANDING II

(i) The following groups of ratios primarily measure risk
(a) liquidity, activity and profitability
(b) liquidity, activity and common stock
(c) liquidity, activity and debt
(d) activity, debt and profitability
Answer (c) Liquidity, activity and debt

(ii) The————-ratios are primarily measures of return.
(a) liquidity (b) activity
(c) debt (d) profitability
Answer (b) Activity

(iii) The……………of a business firm is measured by its ability to satisfy its short term obligations as they come due.
(a) activity (b) liquidity
(c) debt (d) profitability
Answer (b) Liquidity

(iv) ………………ratios are a measure of the speed with which various accounts are converted into sales or cash.
(a) Activity (b) Liquidity
(c) Debt (d) Profitability
Answer (a) Activity

(v) The two basic measure of liquidity are
(a) inventory turnover and current ratio
(b) current ratio and liquid ratio
(c) gross profit margin and operating ratio
(d) current ratio and average collection period
Answer (b) Current ratio and liquid ratio

(vi) The..............is a measure of liquidity which excludes......................, generally the least liquid asset.
(a) current ratio, accounts debtors
(b) liquid ratio, accounts debtors
(c) current ratio, inventory
(d) liquid ratio, inventory
Answer (d) Liquid ratio, inventory

DO IT YOURSELF II

Question 1. Calculate the amount of gross profit
Average stock = Rs.80,000
Stock turnover ratio = 6 times
Selling price = 25% above cost
Answer Average stock = ? 80,000
Stock Turnover Ratio = 6 times
Selling Price = 25% above cost

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. Calculate stock Turnover Ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

TEST YOUR UNDERSTANDING III

(i) The...........is useful in evaluating credit and collection policies.
(a) average payment period (b) current ratio
(c) average collection period (d) current asset turnover
Answer (c) Average collection period

(ii) The.........measures the activity of a firm's inventory.
(a) average collection period (b) inventory turnover
(c) liquid ratio (d) current ratio
Answer (b) Inventory turnover

(iii) The...........ratio may indicate the firm is experiencing stock outs and lost sales.
(a) average payment period (b) inventory turnover
(c) average collection period (d) quick
Answer (d) Quick

(iv) ABC Co extends credit terms of 45 days to its customer, its credit collection would be considered poor if its average collection period was
(a) 30 days (b) 36 days

(c) 47 days (d) 57 days
Answer (c) 47 days

(v) .... are especially interested in the average payment period, since it provides them with a sense of the bill-paying patterns of the firm.
(a) Customers (b) Stockholders
(c) Lenders and suppliers (d) Borrowers and buyers
Answer (c) Lenders and suppliers

(vi) The.................... ratios provide the information critical to the long-run operation of the firm
(a) liquidity (b) activity
(c) solvency (d) profitability
Answer (c) Solvency

SHORT ANSWER TYPE QUESTIONS

Question 1. What do you mean by Ratio Analysis?
Answer The ratio analysis is the most powerful tool of financial statement analysis. Ratios simply mean one number expressed in terms of another. A ratio is a statistical yardstick by means of which relationship between two or various figures can be compared or measured. Ratios can be found out by dividing one number by another number. Ratios show how one number is related to another.

Question 2. What are various types of ratios?
Answer Accounting ratios are classified in two ways Categories as follows
(i) Traditional Classification: Traditional ratios are those accounting ratios which are based on the Financial Statement like Trading and Profit and Loss Account and Balance Sheet. On the basis of accounts of financial statements, the Traditional Classification is further divided into the following categories
(a) Income Statement Ratios: like Gross Profit Ratio, etc.
(b) Balance Sheet Ratios: like Current Ratio, Debt Equity Ratio, etc.
(c) Composite Ratios :like Debtors Turnover Ratio, etc.
(ii) Functional Classification This classification of ratios is based on the functional need and the purpose for calculating ratio. The functional ratios are further divided into the following categories
(a) Liquidity Ratio: These ratios are calculated to determine short term solvency.
(b) Solvency Ratio :These ratios are calculated to determine long term solvency.
(c) Activity Ratio :These ratios are calculated for measuring the operational efficiency and efficacy of the operations. These ratios relate to sales or cost of goods sold.
(d) Profitability Ratio: These ratios are calculated to assess the

Question 3. What relationships will be established to study?
(a) Inventory Turnover (b) Debtor Turnover
(c) Payables Turnover (d) Working Capital Turnover
Answer (a) Inventory Turnover Ratio: This ratio is a relationship between the cost of goods sold during a particular period of time and the cost of average inventory during a particular period. It is expressed in number of times. Stock turnover ratio/inventory turnover ratio indicates the number of time the stock has been turned over during the period and evaluates the efficiency with which a firm is able to manage its inventory.
This ratio indicates whether investment in stock is within proper limit or not. The ratio is calculated by dividing the cost of goods sold by the amount of average stock at cost. The formula for calculating

inventory turnover ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(b)Debtor Turnover Ratio :Debtor turnover ratio or accounts receivable turnover ratio indicates the velocity of debt collection of a firm. In simple words it indicates the number of times average debtors (receivable) are turned over during a year. The formula for calculating Debtors turnover ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(c)Creditors/Payables Turnover Ratio :It compares creditors with the total credit purchases. It signifies the credit period enjoyed by the firm in paying creditors. Accounts payable include both sundry creditors and bills payable. Same as debtor's turnover ratio, creditor's turnover ratio can be calculated in two forms, creditors' turnover ratio and average payment period. The following formula is used to calculate the creditors Turnover Ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(d)Working Capital Turnover Ratio Working capital turnover ratio indicates the velocity of the utilization of net working capital. This ratio represents the number of times the working capital is turned over in a year and is calculated as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 4. Why would the inventory turnover ratio be more important when analysing a grocery store than an insurance company?
Answer Nature of business make inventory turnover ratio more important in case of a grocery store as compare to an insurance company. A grocery store is a trading concern involved in trading i.e., buying and selling of goods and in this regards it is obvious to maintain some inventory in stores. On the other hand, insurance company involved in service business and involved in delivering service there is no question of inventory because service is perishable in nature and cannot be stored. That's why inventory turnover ratio is more important in case of grocery store than an insurance company.

Question 5. The liquidity of a business firm is measured by its ability to satisfy its long term obligations as they become due? Comment.
Answer Yes it is true that the liquidity of a business firm is measured by its ability to pay its long term obligations as they become due. Here the long term obligation means payments of principal amount on the due date and payments of interests on the regular basis. For measuring the long term solvency of any business we calculate the following ratios.

Debt Equity Ratio: Debt equity ratio indicates the relationship between the external equities or outsiders funds and the internal equities or shareholders funds. It is also known as external internal equity ratio. It is determined to ascertain soundness of the long term financial policies of the company. Following formula is used to calculate debt to equity ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Proprietory Ratio/Total Assets to Debt Ratio: Total assets to Debt Ratio or Proprietory Ratio are a variant of the debt equity ratio. It is also known as equity ratio or net worth to total assets ratio. This ratio relates the shareholder's funds to total assets. Proprietory / Equity ratio indicates the long-term or future solvency position of the business. Formula of Proprietory/Equity Ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Fixed Assets to Proprietor's Fund Ratio: Fixed assets to proprietor's fund ratio establish a relationship between fixed assets and shareholders' funds. The purpose of this ratio is to indicate the percentage of the owner's funds invested in fixed assets. The formula for calculating this ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Interest Coverage Ratio: This ratio deals only with servicing of return on loan as interest. This ratio depicts the relationship between amount of profit utilise for paying interest and amount of interest payable. A high Interest Coverage Ratio implies that the company can easily meet all its interest obligations out of its profit.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 6. The average age of inventory is viewed as the average length of time inventory is held by the firm or as the average number of day's sales in inventory. Explain.
Answer Inventory Turnover Ratio This ratio is a relationship between the cost of goods sold during a particular period of time and the cost of average inventory during a particular period. It is expressed in number of times. Stock turnover ratio/inventory turnover ratio indicates the number of time the stock has been turned over during the period and evaluates the efficiency with which a firm is able to manage its inventory. The formula for calculating inventory turnover ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

From the above formula, it is clear that this ratio reveals the average length of time for which the inventory is held by the firm.

LONG ANSWER TYPE QUESTIONS

Question 1. Who are the users of financial ratio analysis? Explain the significance of ratio analysis to them.

Answer Financial ratios help their users to take various managerial decisions. In this context there are four categories of users who are interested in financial ratios. These are the management, investors, long term creditors and short term creditors. The significance of ratios to the above mentioned users is as follows

(i) Management :Management calculate ratios for taking various managerial decisions. Management is always interested in future growth of the organisation. In this regard management design various policy measures and draft future plans. Management wish to know how effectively the resources are being utilised conseguently, they are interested in Activity Ratios and Profitability Ratios like Net Profit Ratio, Debtors Turnover Ratio, Fixed Assets Turnover Ratios, etc. ‘

(ii) Equity Investors :The prime concern of investors before investing in shares is to ensure the security of their principle and return on investment. It is a well known fact that the security of the funds is directly related to the profitability and operational efficiency of the business. In this way they are interested in knowing Earnings per Share, Return on Investment and Return on Equity.

(iii) Long Term Creditors: Long term creditors are those creditors who provide funds for more than one year, so they are interested in long term solvency of the firm and in assessing the ability of the firm to pay interest on time. In this way they are interested in calculating Long term Solvency Ratios like, Debt-Equity Ratio, Proprietory Ratio, Total Assets to Debt Ratio, Interest Coverage Ratio, etc.

(iv) Short Term Creditors :Short term creditors are those creditors who provide financial assistance through short term credit (Generally less than one year). That’s why short-term creditors are interested in timely payment of their debts in short run. In this way they are always interested in Liquidity Ratios like, Current Ratio, Quick Ratios etc. These ratios reveal the current financial position of the business. It is always observed that short term obligations are paid through current assest.

Question 2. What are liquidity ratios? Discuss the importance of current and liquid ratio.

Answer Liquidity ratios are calculated to determine the short-term solvency of the business. Analysis of current position of liquid funds determines* the ability of the business to pay the amount due as per commitment to stakeholders. Included in this category are current ratio, Quick ratio and Cash Fund Ratios.

Current Ratio/Working Capital Ratio: This ratio establish relationship between current assets and current liabilities. The standard for this ratio is 2 : 1. It means a ratio 2 : 1 is considered favourable. It is calculated by dividing the total of the current assets by total of the current liabilities. The formula for the current ratio is as follows

Current Ratio = Current Assets/Current Liabilities Or

Current Assets : Current Liabilities

Importance of Current Ratio Current Ratio Provides a measure of degree to which current assets cover current liabilities. The excess of current assets over current liabilities provides a measure of safety margin available against uncertainty in realisation of current assets and flow of funds. However, it must be interpreted carefully because window-dressing is possible by manipulating the components of current assets and current liabilities, e.g., it can be manipulated by making payment to creditors. A very high current ratio is not a good sign as it reflects under utilisation or improper utilisation of resources.

Liquid/Acid Test/Quick Ratio This ratio establishes relationship between Quick assets and Current liabilities. Quick assets are those assets which can get converted into cash easily in case of emergency. Out of current assets it is believed that stock, and prepaid expenses are not possible to convert in cash quickly. The standard for this ratio is 1:1. It means if quick assets are just equal to the current liabilities they will be considered favourable with the view point of company's credibility. The formula for the quick ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Importance of Current Ratio: Current Ratio Provides a measure of degree to which current assets cover current liabilities. The excess of current assets over current liabilities provides a measure of safety margin available against uncertainty in realisation of current assets and flow of funds. However, it must be interpreted carefully because window-dressing is possible by manipulating the components of current assets and current liabilities, e.g., it can be manipulated by making payment to creditors. A very high current ratio is not a good sign as it reflects under utilisation or improper utilisation of resources.

Liquid/Acid Test/Quick Ratio:This ratio establishes relationship between Quick assets and Current liabilities. Quick assets are those assets which can get converted into cash easily in case of emergency. Out of current assets it is believed that stock, and prepaid expenses are not possible to convert in cash quickly. The standard for this ratio is 1:1. It means if quick assets are just equal to the current liabilities they will be considered favourable with the view point of company's credibility. The formula for the quick ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Importance of Quick Ratio :It helps in determining whether a firm has sufficient funds if it has to pay all its current liabilities immediately. Because of exclusion of non-liquid current assets, it is considered better than current ratio as a measure of liquidity position of the business. Standard for liquid ratio is 1:1. Sometimes quick ratio is calculated on the basis of quick liability instead of current liabilities. Quick liabilities are calculated by ignoring bank overdraft, if any. It means to get the figure of quick liabilities from current liabilities; bank overdraft is deducted from current liabilities.

Question 3. How would you study the solvency position of the firm?

Answer The solvency position of any firm is determined and measured with the help of solvency ratios. In this way we can say that the ratios which throw light on the debt servicing ability of the businesses in the long run are known as solvency ratios. Solvency of a concern can be measured in two ways first to check the security of Debt and second is to check the security of return on Debt. For calculating the security of debt we calculate Debt-Equity Ratio, Proprietory Ratio, Fixed Assets – Proprietory Fund Ratio, etc. And for calculating Security of Return on Debt we calculate Interest Coverage Ratio. A brief description of the above mentioned ratios is as follows

Debt Equity Ratio :Debt Equity Ratio indicates the relationship between the external equities or outsiders funds and the internal equities or shareholders funds. It is also known as external internal equity ratio. It is determined to ascertain soundness of the long term financial policies of the company.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Proprietory Ratio/ Total Assets to Debt Ratio: Total assets to Debt Ratio or Proprietory Ratio are a variant of the debt equity ratio. It is also known as equity ratio or net worth to total assets ratio. This ratio relates the shareholder's funds to total assets. Proprietory/Equity Ratio indicates the long-term or future solvency position of the business. Formula of Proprietary/Equity Ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Shareholder's funds include equity share capital plus all reserves and surpluses items. Total assets include all assets, including Goodwill. Some authors exclude goodwill from total assets. In that case the total shareholder's funds are to be divided by total tangible assets. The total liabilities may also be used as the denominator in the above formula.

Fixed Assets to Proprietor's Fund Ratio: Fixed Assets to Proprietor's Fund Ratio establish a relationship between fixed assets and shareholders' funds. The purpose of this ratio is to indicate the percentage of the owner's funds invested in fixed assets. The formula for calculating this ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

The fixed assets are considered at their book value and the proprietor's funds consist of the same items as internal equities in the case of debt equity ratio.

Interest Coverage Ratio :This ratio deals only with servicing of return on loan as interest. This ratio depicts the relationship between amount of profit utilise for paying interest and amount of interest payable. A high Interest Coverage Ratio implies that the company can easily meet all its interest obligations out of its profit.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 4. What are important profitability ratios? How are they worked out? '
Answer Profitability Ratios Profitability ratios measure the results of business operations or overall performance and effectiveness of the firm. Some of the most Important and popular profitability ratios are as under
Gross Profit Ratio: Gross Profit Ratio (GP ratio) is the ratio of gross profit to net sales expressed as a percentage. It expresses the relationship between gross profit and sales. The basic components for the calculation of gross profit ratio are gross profit and net sales. Net sales mean sales minus sales returns.

Gross profit would be the difference between net sales and cost of goods sold. Cost of goods sold in the case of a trading concern would be equal to opening stock plus purchase, minus closing stock plus all direct expenses relating to purchases. In the case of manufacturing concern, it would be equal to the sum of the cost of raw materials, wages, direct expenses and all manufacturing expenses. In other words, generally the expenses charged to profit and loss account or operating expenses are excluded from the calculation of cost of goods sold.

Following formula is used to calculate gross profit ratios

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Net Profit Ratio :Net Profit Ratio is the ratio of net profit to net sales. It is expressed as percentage. The two basic components of the net profit ratio are the net profit and sales. The net profits are obtained after deducting income-tax and, generally, non-operating expenses and incomes are excluded from the net profits for calculating this ratio. Thus, incomes such as interest on investments outside the business, profit on sales of fixed assets and losses on sales of fixed assets, etc are excluded.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Operating Profit Ratio :Operating Profit Ratio is the ratio of operating profit to net sales. There are many non operating expenses and incomes included in the profit and loss account which has nothing to do with the operations of the business such as loss by fire, loss by theft etc. On the other had in credit side of the P&L account, there are so many incomes
which can be considered as operating incomes such as dividend, bank interest, rent etc. In this way net profit ratio will not tell the truth about the profit of the organisation. Hence operating profit ratio will be helpful in that case. The formula for calculating operating ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Operating Ratio :Operating ratio is the ratio of cost of goods sold plus operating expenses to net sales. It is generally expressed in percentage, Operating ratio measures the cost of operations per dollar of sales. This is closely related to the ratio of operating profit to net sales. The two basic components for the calculation of operating ratio are operating cost (cost of goods sold plus operating expenses) and net sales. Operating expenses normally include (a) administrative and office expenses and (b) selling and distribution expenses. The formula for calculating the operating ratio is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 5. Financial ratio analysis are conducted by four groups of analysts : managers, equity investors, long term creditors and short term creditors. What is the primary emphasis of each of these groups in evaluating ratios?
Answer This is very much true that the financial ratio analysis is conducted by four groups of

analysts : managers, equity investors, long term creditors and short term creditors. The primary emphasis of each of these groups in evaluating these ratios are as follows

(i) Management: Management calculate ratios for taking various managerial decisions. Management is always interested in future growth of the organisation. In this regard management design various policy measures and draft future plans. Management wish to know how effectively the resources are being utilised Consequently, they are interested in Activity Ratios and Profitability Ratios like Net Profit Ratio, Debtors Turnover Ratio, Fixed Assets Turnover Ratios, etc.

(ii) Equity Investors: The prime concern of investors before investing in shares is to ensure the security of their principle and return on investment. It is a well known fact that the security of the funds is directly related to the profitability and operational efficiency of the business. In this way they are interested in knowing Earnings per Share, Return on Investment and Return on Equity.

(iii) Long Term Creditors: Long term creditors are those creditors who provide funds for more than one year, so they are interested in long term solvency of the firm and in assessing the ability of the firm to pay interest on time. In this way they are interested in calculating Long term Solvency Ratios like, Debt-Equity Ratio, Proprietory Ratio, Total Assets to Debt Ratio, Interest Coverage Ratio, etc.

(iv) Short Term Creditors: Short term creditors are those creditors who provide financial assistance through short term credit (Generally less than one year). That's why short term creditors are interested in timely payment of their debts in short run. In this way, they are always interested in Liquidity Ratios like, Current Ratio, Quick Ratios etc. These ratios reveal the current financial position of the business. It is always observed that short term obligations are paid through current assest.

Question 6. The current ratio provides a better measure of overall liquidity only when a firm's inventory cannot easily be converted into cash. If inventory is liquid, the quick ratio is a preferred measure of overall liquidity. Explain.

Answer The above mentioned statement is true. There are two different ways to measure the liquidity of a firm first through current ratio of the firm and second through quick ratio of the firm. The second one is considered the more refine form of measuring the liquidity of the firm.

The current ratio 'explains the relationship between current assets and current liabilities. If current assets are quite capable to pay the current liability the liquidity of the concerned firm will be considered good. But here generally one question arises there are certain assets which cannot be converted into cash quickly such as stock and prepaid expenses.

As far as the matter of prepaid expenses is concerned it's ok but what about the stock if we measure the liquidity on the basis of conversion of current assets in cash there are many firms where conversion of stock is not possible into cash frequently say e.g., heavy machinery manufacturing companies, locomotive companies, etc. This is because, the heavy stocks like machinery, heavy tools etc. cannot be easily sold off. In this case it is always advisable to follow the current ratio for measuring the liquidity of a firm.

But on the other hand, in case of those firms where the stock can be easily realised or sold off consideration of stock should be avoided and to measure the liquidity of that firm Quick ratio should be calculated, e.g., the inventories of a service sector company are very liquid as there are no stocks kept for sale, so in that case liquid ratio must be followed for measuring the liquidity of the firm.

We can understand from the above mentioned statement in the light of another example where stock contribute the major portion in current assets in that case to find out the liquidity of that firm stock cannot be avoided to measure the liquidity of the firm. On the other hand where stock contributes a reasonably less amount it can be avoided and liquidity of that firm can be measured with the help of quick ratio. On the other hand where there is a lot of fluctuation in the price of stock it is always advisable to compute quick ratio and avoid the stock figure because it will reduce the authenticity of liquidity measure.

NUMERICAL QUESTIONS

Question 1. Following is the Balance Sheet of Rohit and Company as on March 31, 2006.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Calculate Current Ratio.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. Following is the Balance Sheet of Title Machine Limited as on March 31, 2006.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Calculate Current Ratio and Liquid Ratio.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 3. Current Ratio is 3:5 Working Capital is Rs. 9,00,000. Calculate the amount of Current Assets and Current Liabilities.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note :According to the ratio, current asset is less than current liability hence working capital should be negative. To match the figures and answer of the question current ratio is taken as 3.5 : 1 and working capital ? 90,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 4. Shine Limited has a current ratio 4.5:1 and quick ratio 3:1; if the stock is 36,000, calculate current liabilities and current assets.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 5. Current liabilities of a company are Rs. 75,000. If Current ratio is 4 : 1 and liquid ratio is 1:1, calculate value of current assets, liquid assets and stock.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 6. Handa Limited has stock of Rs. 20,000. Total liquid assets are Rs. 1,00,000 and quick ratio is 2:1 Calculate current ratio.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 7. Calculate debt equity ratio from the following information

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 8. Calculate Current Ratio if Stock is ? 6,00,000; Liquid Assets Rs. 24,00,000; Quick Ratio 2:1.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 9. Compute Stock Turnover Ratio from the following information

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 10. Calculate following ratios from the following information
(i) Current ratio (ii) Acid test ratio
(iii) Operating Ratio (iv) Gross Profit Ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note (i) Acid test ratio, quick ratio and liquid ratio are one and the same.
(ii) Students mostly get confused in operating ratio and operating profit ratio, so be careful while doing these ratios.

Question 11. From the following information calculate
(i) Gross Profit Ratio (ii) Inventory Turnover Ratio (iii) Current Ratio (iv) Liquid Ratio (v) Net Profit Ratio (vi) Working Capital Ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note :In this question stock is given separately from current assets, hence* it is added to make total current assets.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note :In this question current assetts should be considered as other current asset and stock is separate, in other words, other current assets means liquid assets. Working capital ratio and working capital turnover ratio means same.

Question 12. Compute Gross Profit Ratio, Working Capitat Turnover Ratio, Dept Equity Ratio and Proprietory Ratio from the fottowing information

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 13. Calculate Stock Turnover Ratio if Opening Stock is Rs. 76,250, Closing Stock is 98,500, Sales is Rs. 5,20,000, Sales Return is Rs.20,000, Purchase is Rs. 3,22,250.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 14. Calculate Stock Turnover Ratio from the data given below

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 15. A trading firm's average stock is ? 20,000 (cost). If the stock turnover ratio is 8 times and the firm setts goods at a profit of 20% on sales, ascertain the profit of the firm.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 16. You are able to collect the following information about a company for two years

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Calculate Stock Turnover Ratio and Debtor Turnover Ratio if in the year 2004 stock in

trade increased by Rs. 2,00,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 17. The following Balance Sheet and other information, calculate following ratios
(i) Debt Equity Ratio (ii) Working Capital Turnover Ratio
(iii) Debtors Turnover Ratio

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 18. The following is the summarised Profit and Loss account and the Balance Sheet of Nigam Limited for the year ended March 31, 2007

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Calculate
(i) Quick Ratio
(ii) Stock Trunover Ratio
(iii) Return on Investment

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 19. From the following,
Calculate
(a) Debt Equity Ratio (b) Total Assets to Debt Ratio (c) Propietory Ratio.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 20. Cost of Goods Sold is 1 1,50,000 Operating expenses are Rs. 60,000. Sales is Rs. 2,60,000 and Sales Return is Rs. 10,000. Calculate Operating Ratio.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 21. The following is the summerised transactions and Profit and Loss Account for the year ending March 31, 2007 and the Balance Sheet as on that date.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Calculate (i) Gross Profit Ratio (ii) Current Ratio (iii) Acid Test Ratio (iv) Stock Turnover Ratio (v) Fixed Assets Turnover Ratio.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 22. From the fotlowing information calcutate Gross Profit Ratio, Stock Turnover Ratio and Debtors Turnover Ratio.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Answers NCERT Solutions For Class 12 Accountancy http://freehomedelivery.net/Ch 6 Cash Flow Statement

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TEST YOUR UNDERSTANDING I

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

DO IT YOUR SELF I

Question 1. The profit and loss account of Roy Limited is given here under

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. From the following information calculate net cash from operations

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

TEST YOUR UNDERSTANDING II

Question 1. Choose one of the two alternatives given below and fill in the blanks in the following statements

(a) If the net profits earned during the year is Rs. 50,000 and the amount of debtors in the beginning and the end of the year is Rs. 10,000 and Rs.20,000 respectively, then the cash from operating activities will be equal to Rs................(Rs. 40,000/ Rs.60,000).

Answer Rs. 40,000

(b) If the net profits made during the year are Rs. 50,000 and the bills receivables have decreased by Rs. 10,000 during the year then the cash flow from operating activities will be equal to Rs......................(Rs. 40,000/Rs. 60,000).

Answer Rs. 60,000

(c) Expenses paid in advance at the end of the year are.......................the profit made during the year (added to/deducted from).

Answer Deducted from

(d) An increase in accrued income during the particular year is.........................for calculating the cash flow from operating activities (added to/deducted from).

Answer Added to

(f) For calculating cash flow from operating activities, provision for doubtful debts is....................................the profit made during the year (added to/deducted from).

Answer Added to

Question 2. While computing cash from operating activities, indicate whether the foltowing items witl be added or subtracted from the net profit, if not to be considered write NC.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

DO IT YOURSELF II

Question 1. From the following particulars, calculate cash flows form investing activities

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Interest received on debentures held as investment Rs.60,000 Dividend received on shares held as investment Rs.10,000
A plot of land had been purchased for investment purposes and was let out for

commercial use and rent received Rs. 30,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. From the following Information, calculate cash flow from investing and financing activities

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

In year 2011, machine costing Rs. 2,00,000 was sold at a profit of Rs. 1,50,000, depreciation charged on machine during the year 2011 amounted to Rs. 2,50,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

SHORT ANSWER TYPE QUESTIONS

Question 1. What is a cash flow statement?
Answer A cash flow statement shows inflow and outflow of cash and cash equivalents from various activities of a company during a specific period. The primary objective of cash flow statement is to provide useful information about cash flows (inflows and outflows) of an enterprise during a particular period under various heads, i.e., operating activities, investing activities and financing activities. It explains the reasons of receipts and payments in cash and change in cash balances during an accounting year in a company.

Question 2. How the various activities are classified (as per AS-3 revised) while preparing cash flow statement?
Answer As per Accounting Standard-3 various activities of cash flow statement are classified into three categories as follows
(i) Cash Flow from Operating Activities : These are the principal revenue producing activities of the enterprise and other activities. The cash flow statement begins with the operating activities section. Operating activities generally reflect cash generated and/or paid as a result of the firm's core business functions. Under US GAAP, this category incorporates the cash received from customers, paid to suppliers, paid for operating costs, paid for income taxes, received from interest or dividends, and paid for periodic interest costs.
(ii) Investing Activities: These are the acquisition and disposal of long-term assets, other investments not included in cash equivalents. Cash flows from investing activities are those involving non-current capital assets used in the firm's operations, such as Property, Plant, Equipment (PP&E) and intangible assets. When a company invests in new long-term capacity by acquiring either PP&E or another company, the investment is a cash outflow from investing activities. Disposals of these types of assets for cash generate inflows.
(iii) Financing Activities : These are the activities that result in changes in the size and composition of the owner's capital and borrowings of the enterprise. Cash flows from financing activities are those that take place between a firm and its investors. These include both the equity investments of stockholders (owners) and the loans from bondholders and other creditors. When the

company issues new shares, it records a cash inflow from financing, and when it repurchases shares, pays dividends or pays off debt, it records a cash outflow.

Question 3. State the uses of cash flow statement
Answer The various uses of cash flow statement are as follows
(i) First of all a cash flow statement along with other financial statements provides information that enables users to evaluate changes in net assets of an enterprise, its financial structure (including its liquidity and solvency) and its ability to affect the amounts and timings of cash flows in order to adapt to changing circumstances and opportunities.
(ii) Cash flow information is useful in assessing the ability of the enterprise to generate cash and cash equivalents and enables users to develop models to assess and compare the present value of the future cash flows of different enterprises.
(iii) It also enhances the comparability of the reporting of operating performance by different enterprises because it eliminates the effects of using different accounting treatments for the same transactions and events.
(iv) Historical cash flow information is often used as an indicator of the amount, timing and certainty of future cash flows. It is also helpful in checking the accuracy of past assessments of future cash flows and in examining the relationship between profitability and net cash flow and impact of changing prices.

Question 4. What are the objectives of preparing cash flow statement?
Answer The various objectives of preparing cash flow statement are as follows
(i) The first and most important objective of cash flow statement is that helps to ascertain the gross inflows and out flows of cash and cash equivalents from operating, investing and financial activities.
(ii) A cash flow statement helps in determining the various causes for change in the cash balances during an accounting period.
(iii) A cash flow statement is also prepared to determine the liquidity position of the organisation.
(iv) Moreover a cash flow statement is prepared to know about the requirenTent of cash in future.

Question 5. Explain the terms : Cash equivalents, Cash flows.
Answer A cash flow statement shows inflows and outflows of cash and cash equivalents from various activities of an enterprise during a particular period. As per AS-3, 'Cash equivalents' means short term highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.
Thus, cash equivalents refer to such investments that are held for the purpose of meeting short term cash commitments rather than for investments or other purposes. An investment normally qualifies as cash equivalent only when it has a short maturity, of say, three months or less from the date of acquisition.
Investments in shares are excluded from cash equivalents unless they are in substantial cash equivalents, e.g., preference shares of a company acquired shortly before their specific redemption date provided there is only insignificant risk of. failure of the company to repay the amount at maturity. Similarly, short term marketable securities which can be readily converted into cash are treated as cash equivalents.

Question 6. Prepare a format of cash flow from operating activities under direct method and indirect method.
Answer Format of cash flow from operating activities under direct method is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Format of cash flow from operating activities under indirect method is as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 7. Now that you know the meaning of operating activities, state clearly what would constitute the operating activities for the following types of enterprises
(i) Hotel (ii) Film production house
(iii) Financial enterprise (iv) Media enterprise
(v) Steel manufacturing unit (vi) Software business unit
Answer Operating Activities: As we know that these are the principal revenue producing activities of the enterprise and other activities. Operating activities generally reflect cash generated and/or paid as a result of the firm's core business functions. Hence, the following will be the operating activities in the above mentioned enterprises respectively
(i) In Case of a Hotel : Receipts from sale of goods and services to the customer will be operating activity related to revenue generation. And payment of wages and salaries, electricity, food items and other items used in accommodation and stay of customer will be an operating activity related to

expenditure.
(ii) Film Production House: In case of film production house revenue generating operating activity would be its receipts from selling film rights of a film to the distributors and its operating activity related to expenditure would be payment made to the staff member, unit, actors, dctresses, directors, location rent and air fare etc.
(iii) Financial Enterprise: In case of a financial enterprise like bank the receipts from repayment of loans, interest incomes from investments, etc will be considered as revenue generating operating activity and repayment of loans, recovery expenditure for recover of loans, etc. Salaries of employees will be considered as operating activity related to the expenditure.
(iv) Media Enterprise: A media enterprise is involved in service industry and its revenue generating operating activity would be receipts from advertisements. And expenditure related operating activity would be payments to staff, reporters, photographers, etc.
(v) Steel Manufacturing Unit : The main source for revenue for a steel manufacturing unit would be its receipts from sale of steel sheets, steel castings, steel rods, etc. And the expenditure related operating activity would be payment for raw material (iron, coal), salaries to staff, etc.
(vi) Software Business Unit: A software business unit is basically a service providing unit which get its revenue through receipts from sale of software and renewal of licenses as an operating activity and various payment made by it in the form of salaries to its employees, etc. It is the part of operating activity as expenditure.

Question 8. "The nature/type of enterprise can change altogether the category into which a particular activity may be classified." Do you agree? Illustrate your answer.
Answer Yes, the nature or type of an enterprise can change altogether the category into which a particular activity may be classified. This can be better understood with the help of an example of two firms. One engaged in real estate and the other engaged in general business.
For the firm that is engaged in real estate business purchase and sales of building will be part of the operating activity on the other hand firm that is engaged in general business purchase and sales of building will be part of the investing activity. Hence, it can be said that the classification of activities depends on the nature and type of enterprise.

LONG ANSWER TYPE QUESTIONS

Question 1. Describe the procedure to prepare cash flow statement.
Answer The procedure for preparing cash flow statement is as follows
Step 1 First of all cash flows from operating activities is ascertain.
Step 2 After that cash flows from investing activities is ascertain.
Step 3 The third step is to ascertain the cash flows from financing activities.
Step 4 Sum up the total of all the three steps and ascertain net increase or decrease.
Step 5 Write the opening balance of cash and cash equivalents and deduct it from the amount ascertained in Step 4. The resulting figure arrived is the closing balance of cash and cash equivalents.
There are two methods viz Direct Method and Indirect Method for the preparation of cash flow statement. The main difference in direct and indirect method is to calculate the cash flow from operating activities. Computation of rest of the two activities will remain same. Here are the Proforma of cash flow statement from both the methods.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. Describe “Direct” and “Indirect” method of ascertaining cash flow from operating activities.
Answer
Computation of Cash Flow From Operating Activities
The first section of cash flow statement, known as cash flow from operating activities, can be prepared by two methods known as direct method and indirect method.
(i) Direct Method : In the direct method format, each line of the operating activities section represents a sum of all cheques or deposits in a particular category, e.g., the operating activities section would include such items as cash received from customers; cash paid to suppliers; cash paid for interest; cash paid for wages; cash paid for research and development; cash paid for selling, general, and administrative costs; and any other relevant summary lines.
Direct Method Format: Cash flow from operating activities is calculated by direct method as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(ii) Indirect Method: In indirect method, the net income figure from the income statement is used to calculate the amount of net cash flow from operating activities. Since income statement is prepared on accrual basis in which revenue is recognised when earned and not when received therefore net income does not represent the net cash flow from operating activities and is necessary to adjust EBIT for those items which effect net income although no actual cash has been paid or received against them.
Indirect Method : Following is the indirect method formula which is used to calculate cash flow from operating activities
img src="https://farm1.staticflickr.com/654/22629407825_879ca2b55e_o.png" width="491″ height="335″ alt="ncert-solutions-for-class-12-accountancy-part-2-chapter-6-cash-flow-statement-laq -2-t2″>

Question 3. Explain the major cash inflows and outflows from investing activities.
Answer
Cash Flows from Investing Activities: The next step in building cash flow statement is to look at money a company spent on new capital investments. If a company capitalizes an investment, then that outflow of money does not show up on the income statement. That's because accounting rules allow the company to depreciate (expense) the cost of the investment over time.
From a practical standpoint, if a company purchase an asset such as new plant equipment or machinery, then they most likely paid for that asset in cash. When monpy leaves a company, we have an outflow of cash that we need to show in our statement.
Example In this example, let's say 'X' Company purchased a new computer system for Rs. 15,00,000 along with an assembly line machine for Rs. 20,00,000. These were the only two capital investments made by 'X' Company for the year. In this example, the company was also required to buy a new Machinery worth Rs. 5,00,000 into a special decommissioning fund.
Normally, a company might show one line item for the capital investments and label that line item as additions to plant. In this example, we are going to show these items separately

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

In the above example, we saw that the company made investment in fixed assets and used Rs.40,00,000.

Question 4. Explain the major Cash inflows and outflows from financing activities.
Answer
Cash Flows from Financing Activities : The final category of adjustments we need to address on a statement of cash flows is money raised by financing activities. As was the case with cash from operations, we can have both positive and negative adjustments to cash flow depending on the financing activities the company is engaged during the year.

Typical adjustments appearing here include changes in long and short term debt (issuing and redemption), issuing of preferred stock, issuing of common stock, retirement of stock, and stock dividends paid in cash.
Example In our example, 'X' Company decided to raise Rs. 2,50,000 by issuing common stock. They also issued around Rs.5,00,000 in preference share, and redeemed around Rs. 3,00,000 in long term debt. Finally, they paid a cash

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

In this example, 'X' Company used less money in their financing activities than they generated during the year.

NUMERICAL QUESTIONS

Question 1. Anand Ltd arrived at a net income of Rs. 5,00,000 for the year ended March 31, 2007. Depreciation for the year was Rs. 2,00,000. There was a gain of Rs. 50,000 on assets sold which was credited to profit and loss account. Bills receivable increased during the year by Rs. 40,000 and bills payable also increased by Rs. 60,000. Compute

the cash flow from operating activities by the indirect approach.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 2. From the information given below, you are required to prepare the cash paid for the inventory

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Cash paid for inventory amounts toRs. 1,59,500
Note : Purchase is considered to be credit purchase. Inventory in beginning and end has no effect.

Question 3. For each of the following transactions, calculate the resulting cash flow and state the nature of cash flow viz, operating, investing and financing.
(a) Acquired machinery for Rs. 2,50,000 paying 20% drawn and executing a bond for the balance payable.
(b) Paid Rs. 2,50,000 to acquire shares in Informa Tech and received a dividend of Rs.50,000 after acquisition.
(c) Sold machinery of original cost Rs. 2,00,000 with an accumulated depreciation of Rs. 1,60,000 for Rs. 60,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

(b) Related to investing activity. Acquiring shares in Informa Tech is an investment and dividend received on it is also part of same (Rs. 2,50,000-50,000= Rs. 2,00,000 outflow).
(c) Related to investing activity. It is treated as sale of investment. Rs. 60,000 inflow and Rs. 20,000 as profit on sale of investment as operating activity.

Question 4. The following is the profit and loss account of Yamuna Limited

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Additional Informations
(i) Trade debtors decrease by Rs. 30,000 during the year.
(ii) Prepaid expenses increase by Rs. 5,000 during the year.
(iii) Trade creditors decrease by Rs. 15,000 during the year.
(iv) Outstanding expenses increased by Rs. 3,000 during the year.
(v) Operating expenses intcuded depreciation of Rs. 25,000.
Compute net cash provided by operations for the year ended March 31, 2007 by the indirect method

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 5. Compute cash from operations from
(i) Profit for the year 2010-11 is a sum of Rs. 10,000 after providing for depreciation of Rs. 2,000.
(ii) The current assets of the business for the year ended March 31, 2010 and 2011 are as follows

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Prepare of cash flow statement from summary cash account.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 6. From the foltowing Particulars of Bharat Gas Limited, calculate cash flows from investing activities. Also show the workings clearly preparing the ledger accounts.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Additional Informations

(a) Patents were written-off to the extent of Rs. 40,000 and some patents were sold at a profit of Rs.20,000.

(b) A machine costing Rs. 1,40,000 (depreciation provided thereon Rs. 60,000) was sold for Rs. 50,000. Depreciation charged during the year was Rs. 1,40,000.

(c) On March 31, 2007, 10% investments were purchased for Rs. 1,80,000 and some investments were sold at a profit of Rs.20,000. Interest on investment was received on March 31, 2011.

(d) Amartax Ltd paid dividend @ 10% on its shares.

(e) A plot of land had been purchased for investment purposes and let out for commercial use and rent received Rs.30,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Working Note Machine costing Rs. 1,40,000 less depreciation Rs. 60,000, present value Rs. 80,000 sold for Rs. 50,000 i.e., loss on sale Rs. 30,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note: Any income received on investment is a part of investments like dividend,interest or rent received.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Additional Information

Machine costing Rs.80,000 on which accumulated depreciation was Rs.50,000 was sold for Rs. 20,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 8. From the foltowing Batance Sheet of Tiger Super Steel Ltd, prepare Cash flow statement.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Additional Information
Depreciation Charged on Land and building Rs. 20,000 and plant Rs. 10,000 during the year.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 9. Prepare cash flow statement from the following information

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Additional Information
Depreciation charged on plant amount to Rs. 80,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 10. From the following information, prepare cash flow statement for Yogeta Ltd.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Additional Information

Net profit for the year after charging Rs. 50,000 as depreciation was Rs. 1,50,000, dividend paid on share was Rs. 50,000, tax provision created during the year amounted to Rs. 60,000.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Question 11. Following is the Financial Statement of Garima Ltd. Prepare cash flow statement.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Note Debtors and creditors account can also be prepared to calculate cash receipt or cash paid.

Question 12. Foltowing is the Balance Sheet of Computer India Ltd

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000

Additional Information Interest paid on debenture ? 600.

Items	Soumya (₹)	Bimal (₹)
Capital Accounts	3,00,000	2,00,000
Current Accounts (Cr)	1,00,000	80,000