மனோன்மணியம் சுந்தரனார் பல்கலைக்கழகம்

Manonmaniam Sundaranar University

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Tirunelveli - 627 012, Tamilnadu, India.

DIRECTORATE OF DISTANCE

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CONTINUING EDUCATION

FINANCIAL ACCOUNTING - II

INDEX

FINANCIAL ACCOUNTING

Unit 1 : Consignment

Consignment – Account Sales – Treatment of Bad Debts – Del-Credere commission -Over Riding Commission – Difference between consignment and sales – valuation of unsold stock -Recurring Expense – abnormal ,Normal Loss – Invoice Price Model.

Unit II: Joint Venture

Joint venture – Meaning Difference between Joint Venture and Partnership ,Difference between Consignment and joint venture – methods of Maintaining Accounts – Own Book model (Joint Bank Account) -Separate Book Model -Memorandum Joint Venture Model.

Unit III: Accounts of Non – Trading Concern

Accounts of Non – Trading Concern – Meaning – Capital and Revenue Expenditure -Capital and Revenue Receipts and Payments Accounts – Balance Sheet

Unit IV : Hire Purchase

Hire Purchase and instalment System – Calculation of Cash Price and Interest – Default and Repossession – complete and partial- Difference Between Hire Purchase and Instalment system – Instalment System

Unit V: Royalty Account

Meaning – Minimum Rent – Short working – Type of Recoupment -Strike and Lock out – Insolvency accounts – Insolvency of an individual – Statement of Affairs- Deficiency Account.

Text &Reference Books

1. S.P Jain & K.L.Narang ,Advanced Accountancy ,Kalyani Publishers ,New Delhi

2.RL.Gupta and M.Radhaswamy ,Advanced Accountancy ,Sultan Chand & Sons,New Delhi

3.M.C.Shukla and T .S Grewal ,Advanced Accountancy , Sultan Chand & Sons,New

Consignment

Consignment accounting is a type of business arrangement in which one person send goods to another person for sale on his behalf and the person who sends goods is called consignor and another person who receives the goods is called consignee, where consignee sells the goods on behalf of consignor on consideration of certain percentage on sale.

Features of consignment:

In consignment goods are sent by one person to another for sale by the later on behalf of the owner. Following are the features of consignment :

1. Two Parties: Consignment accounting mainly involves two party's consignor and consignee.

2. Transfer of Procession: Procession of goods transferred from consignor to consignee.

3. Agreement: There is a pre-agreement between the consignor and consignee for terms and conditions of the consignment.

4. No Transfer of Ownership: The ownership of goods remains in the hands of the consignor until the consignee sells it. The only procession of goods is transferred to a consignee.

5. Re-Conciliation: At the end of the year or periodic intervals consignor sends Pro- forma invoice while consignee sends account sale details and both reconcile their accounts

6. Separate Accounting: There is independent accounting done of consignment account in the books of consignor and consignee. Both prepare consignment account and record the journal entries of goods through consignment account only.

Important Terms in Consignment

The term like proforma invoice ,account sales,non-recurring and recurring expenses ,commission,advance etc are commonly used terms in consignment these are explained as follows.

Consignor: It is the person who sends goods.
Consignee: The person who receives the goods is called the consignee.
Consignment: Consignment is a business arrangement through which the consignor sends goods to the consignee for sale.
Consignment Agreement: It is legally written communication between the consignorand consignee, which defines the terms and conditions of the consignment.
Pro-Forma Invoice: goods sent on consignment cannot be treated as pales ,the consignor will not prepare invoice ,He will Prepare the Statement which is similar to invoice which shows the details of goods such as quantity, price, etc. and that statement is called as Pro-forma invoice.

Non- Recurring Expenses: Expenses that are incurred by the consignor to dispatch the goods from his place to place of the consignee are called non-recurring expenses.These expenses are added to the cost of goods.
Recurring Expenses: The consignee incurs these expenses after the goods reachedhis place. These expenses are of maintenance of goods type's expenses.
Account sales : Account sales is a statement which is sent by the consignee to the consignor .The consignee informs the consignor periodically about the volume and value of sales effected and also the expenses incurred by him through a statement called "Account Sales". The account sales contains the gross sales proceeds ,the selling expenses incurred by the consignee and the commission payable to him and also the method of settlement of balance due to the consignor.

illustration 1 may clearly understand as account sales has to be prepared.

Problem 1

On April 1 2020 ramesh Radio ltd of Madurai consigned 200 radio sets to suresh ltd,a radio dealer at Chennai .the cost of each set was Rs. 250 .on receiving the consignment ,suresh ltd sent a bank draft for Rs 30000 as an advance to Ramesh radio ltd .suresh ltd paid Rs 500 as freight and Rs 1000 for godown rent.Suresh Ltd ,submitted an account sales on 1st June 2020 ,Showing that all sets had been sold at Rs 300 each .they were entitled to 5% commission on sales.Prepare Account sales.

Account sales of 200 Radio sets received from and sold on account of

Ramesh radio ltd Madurai

Particulars		Amount
Sales Proceeds 200 × 300		60,000
Less : Freight	500	
Godown Rent	1000	
Commission (5% on 60000)	3000	4,500
		55,500
Less : Advance (Bank Draft)		30,000
Balance Due (Bank Draft Enclosed)		25,500

Commission

Commission:- The commission is the remuneration paid by the consignor to the consignee for the services rendered to the former for selling the consigned goods. Three types of commission can be provided by the consignor to the consignee, as per the agreement, either simultaneously or in isolation.

Types of Commission

1) Ordinary Commission The term commission simply denotes ordinary commission. It is based on a fixed percentage of the gross sales proceeds made by the consignee. It is given by the consignor regardless of whether the consignee is making credit sales or not. This type of commission does not give any protection to the consignor from bad debts and is provided on total sales.

2) Del-credere Commission To increase the sale and to encourage the consignee to make credit sales, the consignor provides an additional commission generally known as del-credere commission. This additional commission when provided to the consignee gives protection to the consignor against bad debts. In other words, after providing the del-credere commission, bad debts are no more the loss of the consignor. It is calculated on total sales unless there is an agreement between the consignor and the consignee to provide it on credit sales only.

3) Over-riding Commission It is an extra commission allowed by the consignor to the consignee to promote sales at a higher price than specified or to encourage the consignee to put hard work into introducing a new product in the market. Depending on the agreement it is calculated on total sales or on the difference between actual sales and sales at invoice price or any specified price. In order to encourage the consignee to earn higher margins, it can also be in the form of a share of additional profits made by the consignee on the sale of goods.

Difference between Sale and Consignment

1. When goods are sold by one to another, the property in the goods immediately passes to the buyer, whereas when goods are sent on consignment, the property in the goods remains with the consignor. Only the possession is transferred to the consignee.

2. When goods are sold by one to another, it becomes a relationship of a buyer and seller or a debtor and a creditor between the two persons, whereas when goods are consigned by one to another, it becomes a relationship of a principal and an agent between the consignor and the consignee.

3. When goods are sold, the buyer cannot return the goods to the seller whereas when goods are sent on consignment the goods are returnable, if they remain unsold.

4. The risk in the goods is not transferred to the consignee despite the transfer of possession of goods. Any damage or loss to the goods is therefore borne by consignor. But in the case of sale, the risk is immediately transferred to the buyer even when the goods are still in the possession of the seller.

5. The expenses, in respect of freight, cartage, insurance, etc. Are met by the consignor in a consignment transaction, but in the case of sale the expense are borne by the purchaser unless otherwise provided in the agreement.

6. The transfer of possession (i.e. Delivery of goods) is essential in a consignment transaction. In a sale, however, the goods may be delivered at a later date. The consignee will be treated as a debtor only when goods or part of them have been sold by him.

But if goods remain unsold, the consignee will send them back to the Consignor and the Consignor will pay the Consignee all the expenses he has incurred in keeping the goods in safety and in attempting to push the goods in the market

Operating Cycle of Consignment Arrangement

i. Goods are sent by consignor to the consignee

ii. Consignee may pay some advance or accept a bill of exchange

iii. Consignee will incur expenses for selling the goods

iv. Consignee maintains records of all cash and credit sale.

v. Consignee prepares a summary of results called as Account sales

vi. Consignor pays commission to the consignee

Accounting Treatment for consignment Business

The consignor and consignee keep their own books of accounts. The consignor may send goods to many consignees. Also, a consignee may act as agent for many consignors. It is appropriate that both of them would want to know profit or loss made on each consignment.

Necessary Accounts required in the books of consignor	**Necessary Accounts required in the books of consignee**
1. Consignment A/c 2. Consignee's A/c 3. Goods sent on Consignment A/c 4. Other accounts : Abnormal Loss A/c	1. Consignor's A/c 2. Commission A/c

Journal Entries Relating to Consignment Transactions

Let us see the entries in the books of consignor as well as consignee.

Situations	Consignor's Books
On sending goods	Consignment A/c .... Dr Goods Sent on Consignment Cr
On expenses for sending goods (by the consignor)	Consignment A/c .... Dr Cash/ Bank A/c Cr
On an advance made by the consignee	Cash / Bank / Bills Receivable A/c ……Dr Consignee's Personal A/c…Cr
Bills received from the consignee discounted withthe bank	Bank A/c .... Dr Discount A/c .... Dr Bills Receivable A/c…Cr
On expenses incurred by consignee	Consignment A/c .... Dr Consignee's Personal A/c Cr
On sales made by the consignee	Consignee's Personal A/c …..Dr Consignment A/c…Cr
For consignee's commission	Consignment A/c .... Dr Consignee's Personal A/c…Cr
Goods returned by the consignee	Goods Sent on Consignment...Dr Consignment A/c…….Cr
Bad debts incurred (when a consignee is entitled to ***del credere commission***, no entry for bad debts isto be passed as such a loss is to be borne by the consignee himself. Otherwise, the loss on account of bad debts should be borne by the consignor.	Consignment A/c .... Dr Consignee's Personal A/c…Cr
Remittance by the consignee in full settlement	Cash / Bank / Bills Receivable A/c ……Dr Consignee's Personal A/c… Cr
Profit or loss on consignment (a) If there is a profit (b) If there is a loss	Consignment A/c Dr Profit and loss A /c… Cr Profit and loss A /c… Dr Consignment A/c Cr

Closing entry for goods sent on consignment	Goods Sent on Consignment…Dr Trading A / c Cr
On closing stock/ unsold Stock with the consignee	Consignment Stock A/c Dr Consignment A/c… Cr

The Consignment account in the books of consignor will ultimately show the ***net profit or loss*** on account of consignment business. It must be noted that a separate consignment account must be opened for different agents. This will enable him to know profit or loss on each consignment.

Books of the Consignee

Situations	**Consignee's Books**
Goods received from the consignor	No Entry
Expenses incurred by the consignor	No Entry
Advance made by the consignee	Consignor's Personal A/c...Dr Bank / Cash / Bills Payable A/c………Cr
Bill discounted by the consignor with the bank	No Entry
Sales of goods by the consignee	Cash A / c (cash sales)…….Dr Consignment debtors A / c (credit sales) .... Dr Consignor's Personal A/c.......................... Cr
Expenses incurred by the consignee	Consignor's Personal A/c...Dr Cash/ Bank A/c ....Cr
Commission due to the consignee	Consignor's Personal A/c...Dr Commission A/c…Cr
Return of goods to the consignor	No Entry
Payment received from debtors	Cash/ Bank A/C ....Dr Consignment debtors A/C..Cr
Bad debts incurred	
(a) In case consignee does not get del credere commission, all bad debts have to be borne by the consignor himself. (b) In case del credere commission is paid to the consignee, bad debts are to be borne by him. When the bills payable accepted in favor of the consignor is met on the due date	Consignor's Personal A/c...Dr Consignment debtors A/C..Cr Bad debts A /c…Dr Consignment debtors A/C…Cr Bills payable A /c…............. Dr Bank A/c…Cr

Unsold stock in possession of the consignee	No Entry
Profit or loss on consignment	No Entry

***Note:** The discount on bills may be accounted for in one of two ways;

- As a normal operating expenses item and charged against the profit and loss account;or
- As a special expense item related to the consignment and therefore charged to theconsignment account.

The method of accounting depends on whether the advance is interpreted as a method of financing the business generally or whether it is regarded as a transaction particularly related to the consignment activity.

Format of Consignment Account

	Rs		**Rs**
To Consignment stock (opening balance if any)	**xxx**	By Consignee's Personal Account (Amount of gross proceeds (sales) realized by the Consignee)	**Xxxx**
To Goods Sent on Consignment	**xxxx**	By Goods Sent on Consignment (Difference in cost of goods sent andthe proforma Invoice price)	**Xx**
To Cash/bank (Expenses incurred by the consignor)	**xx**	By Abnormal loss (Whether insured or not)	**Xxx**
To Consignee's Personal Account (Expenses paid by the Consignee– total amount) (Commission, including del-credere payable to the consignee)	**xx**	By Goods sent on Consignment (Returned by the Consignee)	**Xx**
To Stock Reserve (Difference in thevalue of closing stock marked at Pro-forma invoice or loaded price & cost price)	**xx**	By Stock Reserve (Difference between the cost and pro-forma invoice price on the opening balance of consignment)	**Xx**
To Goods Sent on Consignment (Difference between cost price andPro-forma invoice price on the goods returned by the consignee)	**xx**	By General Profit and Loss Account(For consignment loss)	**xx**
To General Profit and Loss Account (For Consignment profit)	**xxx**		

Illustration: 1

Aju stores of Jaffna consigned on 1st January, 2010, 50 cases of goods at Rs.200 each to Riyash Traders of Warakkapola for sale on commission at 10% on gross sales. Aju stores paid Lkr.500 for packing, freight and insurance. Riyash Traders took delivery of the goods on11th January, 2010, after accepting a 15 days bill for Rs 5,000 and paid Rs 150 for carriage. They sold 40 cases of goods @ Rs. 250 and balance for Rs. 260 each. Their sales expenses amounted to Rs. 200. On 31st January, 2005, Riyash Traders forwarded an account sale together with a draft for the balance.

Prepare **account sales** rendered by Riyash Traders and also give **journal entries** and ledger accounts in the books of **Aju stores** and **Riyash Traders**.

Solution:

Account sales of 50 cases of goods received and sold on behalf of Aju stores, Jaffna.

Particulars	**Amount**(Rs)	
Sale Proceeds:		
40 cases sold at Rs 250 each10 cases	10,000	
sold at Rs 260 eachLess: Expense:	2,600	12,600
Carriage		
Sales expenses	150	
Commission @ 10% Net	200	
proceeds	1,260	(1,610)
Less: Advance (Bill)		10,990
Balance sent by Draft		(5,000)
		5,990

Books of Aju Stores (Consignor)Journal Entries

	Description	**Dr (Rs)**	**Cr (Rs)**
1.	Consignment to Warakkapola A/c Goods sent on Consignment A/c (Sent goods on consignment to Riyash Traders, Warakkapola)	10,000	10,000
2.	Consignment to Warakkapola A/c Bank A/c (Expenses incurred on the Consignment)	500	500
3.	Bill receivable A/c Riyash Traders A/c (Advance received from the Agent in the form of Bill)	5,000	5,000

5.	Consignment to Warakkapola A/c Riyash Traders A/c (paid carriage and sales expenses by consignee)	350	350
6.	Bank A/c Bills receivable A/c (The bill met on due date)	5,000	5,000
4.	Riyash Traders A/c Consignment to Warakkapola A/c (Gross sale proceeds as per Account Sales)	12,600	12,600
7.	Consignment to Warakkapola A/c Riyash Traders A/c (Commission on gross sales payable @ 10%)	1,260	1,260
8.	Consignment to Warakkapola A/c Profit and Loss A/c (Transferred profit on consignment to profit and loss A/c)	490	490
9.	Bank A/c Riyash Traders A/c (Amount received in draft along with account sales)	5,990	5,990
10.	Goods sent on Consignment A/c Trading A/c (Goods sent on consignment A/c closed by transfer to trading A/c)	10,000	10,000

Ledgers

Consignment to Warakkapola Account

	Dr		Cr
Goods sent on Consignment A/c	10,000	Riyash Traders A/c	12,600
Bank A/c (expenses)	500	(Sale proceeds)	
Riyash Traders A/c			
Carriage 150			
Sales expenses 200	350		
Riyash Traders: CommissionP	1,260		
& L A/c (Transfer)	490		
	12,600		12,600

Riyash Traders A/c

	Dr		Cr
Consignment to Warakkapola A/c	12,600	Bill Receivable A/c	5,000
		Consignment to Warakkapola A/c	350
		Consignment to Warakkapola A/c	1260
		Bank A/c	5,990
	12,600		12,600

Bill Receivable A/c

	Dr		Cr
Riyash Traders A/c	5,000	Bank A/c	5,000

Goods sent on Consignment Account

	Dr		Cr
Trading A/c (Transfer)	10,000	Consignment to Warakkapola A/c	10,000

Profit & Loss A/c

	Dr		Cr
		Consignment to Warakkapola A/c	490

Books of Riyash Traders (Consignee)Journal Entries

	Description	Dr (Rs)	Cr (Rs)
1.	Aju stores A/c Bank / Cash A/c (Paid expenses on the Consignment received)	350	350
2.	Aju stores A/c Bills payable A/c (Acceptance of bill drawn against the consignment)	5,000	5,000
3.	Bills payable A/c Bank A/c (The bill met on due date)	5,000	5,000

4.	Bank A/c Aju stores A/c (Sales effected for the Consignment received)	12,600	12,600
5.	Aju stores A/c Commission A/c (Commission receivable on the goods sold)	1,260	1,260
6.	Aju stores A/c Bank A/c (Amount remitted as final settlement)	5,990	5,990

Ledgers

Aju Stores A/c

	Dr		Cr
Bank A/c (Expenses)	350	Bank A/c (Sale proceeds)	12,600
Bills payable A/c	5,000		
Commission A/c	1,260		
Bank A/c (amount remitted)	5,990		
	12,600		12,600

Bills payable A/c

	Dr		Cr
Bank A/c	5000	Aju stores A/c	5,000

Commission A/c

	Dr		Cr
		Aju stores A/c	1,260

Valuation of unsold stock

It is necessary to calculate the value of unsold stock so that such unsold stock is brought in the balance sheet ofthe consignor Valuation of unsold stock is done as under-

(i) Actual value of unsold stock at cost price or market price, whichever is less.

(ii) Add proportionate expenses incurred by the consignor (such as freight, carriage on purchase, export andimport duties, loading charges).

(iii) Add proportionate expenses of non-recurring nature incurred by consignee such as freight on loading andunloading, octroi, wages, insurance of goods in transit etc. .

Important Note:-

Expenses of recurring nature (such as warehouse expenses, establishment, carriage on sales, packing expenses,godown rent or charges, advertisement, and other sale expenses) are not considered for valuation of unsold stock. Simple rule is all such expenses, which are incurred to bring the goods into saleable condition and incurred by consignee for bringing the goods upto the warehouse or godown are of non-recurring nature, which are considered for valuation of unsold stock.

Illustration: **2**

Y consigns goods to X valued at 8000 cost price. Expenses incurred by Y are: freight 40; insurance 100; cartage 20.Commission is allowed at 5% on sales. An advance of 5000 is made by the consignee. X incurs the following expenses: duty 80; cartage inward 40; advertising 200; and cash sales amounted to 7600. At balance date one-quarter of the goods are unsold. Calculate the value of unsold goods.

	Rs
¼ th of cost price (Rs 8,000)	2,000
¼ th of consignor‘s expenses [Rs 160 (freight 40; insurance 100; cartage 20)]	40
¼ th of consignee‘s relevant expenses [Rs 120 (duty 80; cartage inward 40)]	30
Total value of unsold Stock	2,070

Illustration: **3**

Ramu of Cochin consigned goods of the cost of Lkr.10000 to his agent, Ajith of Agra and incurred Lkr.2000 for packing, forwarding and freight. Ajith took delivery of the goods after spending Lkr.3000 for duty and clearing charges. He sold 3 / 4th of the goods for Lkr.15000 for which he was entitled to a commission of 5%. His sales expenses amounted to Lkr.300. Prepare consignment account after showing the valuation of unsold stock.

Solution:

Valuation of stock:

		Rs
Cost of stock at pro forma invoice = 10,000 * ¼		2500
Add: proportionate non-recurring expenses:		
Incurred by Ramu	2,000	
Incurred by Ramu	3,000	
	5,000 * ¼	1,250
Value of stock		3,750

Consignment to Agra A/c

	Dr		Cr
Goods sent on Consignment A/c	10,000	Ajith A/c (Sale proceeds)	15,000
Bank A/c (Packing charges)	2,000		
Ajith A/c (Duty + selling charges)	3,300	Stock on consignment	3,750
Ajith A/c: Commission	750		
P & L A/c (Transfer)	2,700		
	18,750		18,750

Losses on Consignment

In case the goods sent on consignment are lost or damaged in transit or otherwise, the loss is that of the consignor and not of the consignee. Accordingly the consignor will have to make the entries for such loss. There are two types of losses which may arise in case of aconsignment transaction, viz., Normal Loss and Abnormal Loss.

Normal Loss

Normal loss is natural, unavoidable and inherent in the nature of goods or commodities sent on consignment (due to evaporation, leakage & breaking the bulk into pieces). This type of loss is a part of the cost of the consignment, so the consignor does not make separate entryfor such a loss. However, the normal loss has to be taken into consideration while valuating the unsold consignment stock in the hand of the consignee. Since normal loss is a charge against gross profit. No additional adjustment is required for this purpose. Moreover, the same is a part of cost of goods, when valuation of unsold stock is made in case of consignment account the quantity of such loss (not the amount) should be deducted from the total quantity of the goods received by the consignee in good condition

The accounting treatment of normal loss is to charge the total cost of the goods to the remaining goods after the normal loss. In other words, the value of the unsold stock is calculated in proportion to the total cost of the goods consigned.

$$\text{Value of unsold stock} = \frac{\text{Total cost of the goods sent}}{\text{Units of Goods sent} - \text{Normal losses (units)}} \times \text{Unsold quantity} \qquad \text{……………….. (1)}$$

Or

$$\text{Value of unsold stock} = \frac{\text{Unsold quantity}}{\text{Good quantity received by consignee}} \times \text{Total value of goods sent} \qquad \text{……………… (2)}$$

Illustration : 4

From the following particulars ascertain the value of unsold stock on consignment.

	RS
Goods sent (1,000 kgs)	20,000
Consignor's expenses	4,000
Consignee's non-recurring expenses	3,000
Sold (800 kgs)	40,000
Loss due to natural wastage (100 kgs)	

Solution:

Value of unsold stock `

	RS
Total cost of goods sent	20,000
Add: Consignor's expenses	4,000
Non-recurring expenses	3,000
Cost of 900 kgs (1,000 kgs – 100 kgs)	**27,000**

∴Value of unsold stock 100 kgs (1,000 – 800 – 100) will be;

$$\frac{27,000}{(1000\ \text{kgs}-100\ \text{kgs})} \times 100\ \text{kgs}$$

= Rs .3, 000.....................................(1)

Illustration: 5

Mr. Achchu Consigned to Mr. Kajan 10,000 kgs of flour, costing Rs .33, 000. He spent Rs.880 as forwarding charges. 12% of the Consignment was lost in weighing and handling. Mr. Kajan sold 8,200 kgs of flour at Rs.6 per kg, his selling expenses being Rs .3, 300 and Commission 5% on sales. Prepare the Consignment Account.

Ledger of Mr. Achchu (Consignment Account)

	Dr		Cr
Goods sent on Consignment A/c	33,000	Mr. Kajan A/c	49,200
Bank (forwarding Charges)	880	[(Sale proceeds, 8,200×6]	
Mr. Kajan A/c		Consignment Stock A/c	2,310*
Selling Expenses 3,300			
Commission 2,460	5,760		

(@5% on Rs.49,200) P & L A/c (Transfer)	11,870		
	51,510		51,510

Working Notes:

1. Calculation of Closing Stock:

		Kgs
Total quantity of flour consigned		10,000
Less: Normal Loss 12%	1,200	
Sales	8,200	(9,400)
Closing Stock		600

2.valuation of closing Stock

$$\frac{\text{Total Cost of the goods sent + non recurring expenses}}{\text{Units of Goods sent – Normal losses (units)}} \times \text{Closing Stock (units)}$$

$$\frac{\text{Rs.33, 000 + Rs.880}}{10{,}000 - 1{,}200} * 600$$

= Rs 33880/8800*600

= Rs **2,310***

1. **Abnormal Loss :** The loss of stock which is due to carelessness or abnormal reasons is called abnormal loss. This loss is calculated as under :

(a) **Loss in Transit :** (Loss of stock that occurred before goods reached consignee's Warehouse) - In this case, to getvalue of abnormal loss proportionate share of consignor's expenses are added in the cost of stock lost. Consignee's expenses are not included.

(b) **Loss of stock in Consignee's Godown :** In this case, value of abnormal loss is caluculated : the cost of goods destroyed by adding proportionate expenses of the consignor as-well-as proportionate non-recurring (Direct) expenses of the Consignee.

Accounting Treatment of Abnormal Loss of stock : This Loss is to be borne by the Consignor, as such, the required entries will be passed in the books of the Consignor only.

(1) **When Abnormal Loss Occurs**

Abnormal Loss A/c	Dr.	Amount of Abnormal Loss
To Consignment A/c		

(2) **If stock is insured and insurance Company admits the claim**

Insurance Company A/c	Dr.	With the amount of claim admitted
Profit & Loss A/c	Dr.	With the amount not admitted
To Abnormal Loss A/c		Total amount of claim
Bank A/c	Dr.	Admitted claim received from Insurance Company

To Insurance Company A/c   To Insurance Company

Illustration 6 :

On 1 January 2016, Himi Glass Works of Mumbai consigned to Parth of Bhilwara 100 cases at ` 16000 on cost. Hepaid ` 1000 Railway freight,` 2000 wages. During transit 10 cases were lost and remaining cases were received by Parth. He paid octroi ` 1000, sales expenses ` 500, godown rent ` 500. Parth sold 75 cases @ ` 200 per case. Parth received 5% commission on sales and remaining amount was sent to consignor by consignee.

Prepare Consignment and consignee's account in the books of Himi Glass Works.

Solution :

In the Books of Himi Glass Works, Mumbai Consignment Account

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
2016 Jan, 1	To Goods sent on Consignment A/c	16,000		By Parth's A/c (Sales)	15,000
				By Abnormal Loss	1,900
	To Cash A/c (Exp.)	3,000		By Unsold Stock	3,017
	To Parth's A/c (Exp.)	2,000		By P & L (Loss)	1,833
	To Parth's A/c (Commission)	750			
		21,750			**21,750**

(1) Computation of commission : 15,000 x 5% = ` 750

(2) Amount of Abnormal Loss : 10 cases x 160 = ` 1,600   1600

Add : Proportionate Consignor's Expenses = ` 300 x 10/100 ` =300 = ` 1,900

(3) Unsold stock = 100 cases – 10 – 75 = 15 x ` 160 = ` 2,400

Add: Proportionate Exps. of Consignor = 23,000 x 5/100 = ` 450

Add: Proportionate Exps. of Consignee = `1,000 x 15/100 = ` 167

= `3,017

Parth's Account (Consignee's A/c)

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
	To Consignment A/c	15,000		By Cosignment A/c	2,000
				By Cosignment A/c	750
				By Bank A/c (B/F)	12,250
		15,000			**15,000**

JOINT VENTURE ACCOUNTS

Joint Venture

A Joint venture is a contract between two or more persons who agree to do a small piece of commercial undertaking jointly. It is a **temporary partnership**, without the use of a firm name limited or restricted to a particular venture in which the two or more persons agree to contribute a specific amount of capital and to share profits or losses either in equal proportions or in any other agreed proportion.

Nature of Joint Venture

A Joint venture may be in connection with a joint consignment of goods, and ***under-writing****of shares or debentures of a new joint stock company, speculation in shares, the construction of a building jointly, the purchase and sale of a particular plot of land or any other similar temporary or seasonal business enterprise. Once the joint undertaking is complete and over; the joint venture or limited partnership ends and no liability will then attach to any party.

Note: *Underwriting means undertaking the responsibility that shares or debentures issued bycompany will be taken up by the public. If the public does not take them, the underwriters agree to take up the shares or debentures.

The basic features of a Joint Venture business are:

(i) It is done for a specific purpose and hence has a limited duration.

(ii) The partners are called co-ventures.

(iii) The profit or loss on joint venture is shared between the co-ventures in the agreed ratio.

(iv) The co-ventures may or may not contribute initial capital.

(v) The joint venture is dissolved once the purpose of the business is over.

(vi) The accounts of the co-ventures are settled immediately on dissolution.

(vii) A joint venture has no name.

Advantages of a Joint Venture

Sometimes a party may be in a position to buy goods at a much lower cost and on far better terms than others. a second party may be in a position to sell the same at an exceptionally good price. Or, it may so happen that merchandise is bought cheap at one place by one party and when sent to another place it can be sold at a higher price by the second party. A third

party may have financial resources but may not be in a position either to buy at lower price orto sell at higher price. A combination of all these parties in a common venture may result in a successful and remunerative business.

The business activities for which Joint Ventures (JV) are formed could be :

- Construction of dams, bridges, roads etc.
- Buying & selling of goods for a particular season.
- Producing a film.
- Purchasing land selling plots .

Differences between Joint Venture and Consignment

Points of Difference	Consignment	Joint Venture
Relationship	The Consignor is principal while the consignee is agent.	Relationship between Covertures is that of the Partners.
Nature of Business	Agent is not necessarily a partner; hence it is not a partnership.	It is a partnership(Though temporary) since Co-ventures are partners
Powers	Consignee being an agent is simply a servant and has to obey the instructions of the Principal.	Co-ventures enjoy full powers as to sale and purchase of goods and collections of dues etc.
Scope	Consignment is concerned only with the sale of movable goods.	Joint Venture may be undertaken for any type of legal business e.g. construction of roads, building etc. in addition to purchase and sale of goods.
Finance	Consignor (Principal) provides the funds.	Funds are provided by the Co-Ventures
Profits and commission	The Consignee is entitled to receive only commission and reimbursement of his expenses.	Profits (or losses) are shared by the Co-ventures in thepredetermined ratios or equally in

	No share in the profits orliability for losses.	the absence of an agreement. Commission may or may not be granted to Co-ventures.
Number of Persons	There are normally two parties namely the principal and the agent.	The number of Co-ventures will be at least two though it may be more than two with equal status i.e. that each is a principal and agent at the same time like partners.

Differences between Joint Venture and Partnership

Points of Difference	Joint Venture	Partnership
Firm name	There is no need for firm name.	A Partnership firm always has a firm name.
Continuance	It comes to an end as soon as theproject is completed.	It is of a continuous nature.
Books of accounts	There is no need for a separate set of books. The accounts can be maintained even in one of the co-venture‘s books only.	Separate set of books have to bemaintained.
Similar business	The co-ventures are free to carry on the business of a similar nature.	No partner can carry on a similarbusiness.
Registration	There is no need for registrationat all.	Although the registration of partnership is not compulsory, it is not considered desirable.
Minor	A minor can‘t be a co-venturer as he is incompetent to enter intoa contract.	A minor can also be admitted tothe benefits of the firm.

Methods of recording Joint Venture transactions

It is necessary to maintain proper accounts of all transactions of joint venture so that correct profit or loss on joint venture may be ascertained. The following are main methods of recording joint venture transactions:

When one of the co-ventures is appointed to manage the joint venture.

When a separate set of books is not maintained for recording joint venture transactions.

When a separate set of books is kept for the joint venture.

When joint venture transactions are recorded through the memorandum joint ventureaccount.

(A) When one of the Co-ventures is appointed to manage the Joint Venture

Under this method, only one co-venturer records the joint venture transactions who open a joint venture account and personal accounts of other co-venturers.

This method of recording transactions is followed when the business is not very large. Under this method, one of the venturers is entrusted with the task of recording the transactions in his book. In this case, all other co-venturers will send their contributions to such a venturer. He will open a joint venture account and the personal accounts of other co- venturers in his books. The joint venture account is prepared to ascertain the profit or loss of the joint venture. It is a nominal account. All the expenses are debited and the incomes are credited in the joint venture account.

The difference between debit and credit is the profit or loss of the venture. The venturer who manages the joint venture transfers his share to profit and loss account and the share of other venturers to their personal accounts. The personal accounts of other co- venturers are prepared to ascertain the amount due from them.

The following entries are passed in the books of the co-venturer appointed to manage the affairs before the necessary accounts of the joint venture:

1)	When the co-venturers send their contribution	Bank A/c… .... Dr Other co-venturers A/c… .... Cr
2)	When the goods are purchased for the joint venture	Joint venture A/c… ....Dr Bank A/c(cash purchase) .... Cr

		Suppliers A/c(credit purchase) .... Cr
3)	When goods are supplied out of his stock by theco-venturer who is recording the transaction	Joint venture A/c... ....Dr Purchase A/c... .... Cr
4)	When goods are supplied by other co-venturers	Joint venture A/c... ....Dr Other co-venturers A/c... .... Cr
5)	When some expenditure is incurred on account of the joint venture	Joint venture A/c... ....Dr Bank A/c... .... Cr
6)	When expenses are met by other co-venturers	Joint venture A/c... ....Dr Other co-venturers A/c... .... Cr
7)	When the co-venturer records the transaction ofsales	(a) For cash sales Bank A/c... .... Dr Joint venture A/c... ....Cr (b) For credit sales Debtors personal A/c..Dr Joint venture A/c... ....Cr
8)	When cash is received from debtors	Bank A/c... .... Dr Debtors personal A/c... .... Cr
9)	When some cash discounts are allowed to the debtor making payment or some bad debts are incurred	Joint venture A/c... ......Dr Debtors personal A/c... .... Cr
10)	When sales are made by other co-venturers	Co-venturers personal A/c...... Dr Joint venture A/c... ....Cr
11)	When some cash or bills receivable are received	Bank / bills receivable A/c...Dr

	from other co-venturers on account of sales madeby them	Co-venturers personal A/c............. Cr
12)	When the co-venturer's recording transactions areentitled to some commission or salary	Joint venture A/c... ....Dr commission or salary A/c... .... Cr
13)	When the unsold stock of joint venture is takenover by the co-venturer recording the transactions	Purchase A/c... .... Dr Joint venture A/c... ....Cr
	If the unsold stock is taken over by some other co-venturers	Co-venturers personal A/c...Dr Joint venture A/c... ....Cr
14)	For any profit / loss on closing the joint venture	(a) For any profit Joint venture A/c... ....Dr Profit & loss A /c... .... Cr (Working venture's share) Other co-venturers A/c........... Cr (Other venturers' share) (b) For any loss Profit & loss A /c... Dr (Working venture's share) Other co-venturers A/c.Dr (Other venturers' share) Joint venture A/c... ....Cr
15)	On payment of any amount to a co-venturer onclosing the account	Co-venturers A/c... ....Dr Bank A/c... .... Cr
16)	On receipt of any amount due from a co-venturer	Bank A/c... .... Dr

	on closing the accounts	Other co-venturers A/c… ....Cr

Illustration: 1

Madhu and Muthu entered into a joint venture in which Madhu would manage the business. They brought Rs. 10,000 each in case for the venture. Madhu purchased goods for Rs. 19,000 and sold it for Rs. 25,000. Expenses on the venture paid by him amounted to Rs.1,000. Madhu would get a commission of 4% on sales. They shared profits and losses equally.Pass journal entries and prepare ledger accounts in the books of Madhu.

Solution:

In the Books of MadhuJournal Entries

Description	Rs	Rs
Bank A/c… ....Dr Muthu's A/c.. Cr (The amount received from Muthu as his share of investment)	10,000	10,000
Joint venture A/c… .... Dr Bank A/c… ....Cr (Bought goods for the venture)	19,000	19,000
Joint venture A/c… .... Dr Bank A/c… ....Cr (paid expenses for the venture)	1,000	1,000
Bank A/c… ....Dr Joint venture A/c… .... Cr (the amount of cash sales)	25,000	25,000
Joint venture A/c… .... Dr Commission A/ c ....Cr (The amount of commission at 4% on sales)	1,000	1,000
Joint venture A/c… .... Dr Profit and loss A/c ....Cr Muthu's A/c... Cr (profit from the venture shared equally)	4,000	2,000 2,000

Muthu's A/c...Dr Bank A/c... ....Cr	12,000	 12,000
(Paid the amount on final settlement)		

Joint Venture A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Bank (purchased goods)	19,000	Bank (Sales)	25,000
Bank (expenses)	1,000		
Commission (4% on sales)	1,000		
Profit and loss A/c 2,000			
(Half of profit)			
Muthu			
(Half of profit) 2,000	4,000		
	25,000		25,000

Muthu A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Bank	**12,000**	Bank	10,000
		Joint venture (% of profit)	2,000
	12,000		12,000

Illustration: 2

Anil entered into a contract to construct a building for Rs. 200,000. Anil and Sunil contributed Rs. 100,000 and Rs. 75,000, respectively. They agreed to share profits and losses in the ratio of 4:3. It was decided that the work would be looked after by Anil who would be paid 5% commission on contract price in addition to his share of profit. Anil boughtthe necessary materials for Rs. 160,000 and paid Rs. 4500 for expenses. Anil also contributed building materials from his own stock worth Rs. 10,000. Rs. 2,500 remained to be paid for wages. Sunil took over the stock of materials for an agreed valuation of Rs. 8,000. The building was completed and the contract money was duly received.

Record the above transactions in the books of Anil and show the joint venture accountthat the outstanding wages were paid by Anil.

Solution:

In the Books of MadhuJournal Entries

Description	Rs	Rs
Bank A/c… ....Dr Sunil's A/c…...Cr (Received cash from Sunil)	75,000	75,000
Joint venture A/c…... Dr Bank A/c… ....Cr (Purchased materials)	160,000	160,000
Joint venture A/c…... Dr Bank A/c… ....Cr (Paid expenses for the venture)	4,500	4,500
Joint venture A/c…... Dr Purchase A/c… ....Cr (Supplied materials from personal stock)	10,000	10,000
Joint venture A/c…... Dr Outstanding wages A/c... Cr (Outstanding wages to be paid)	2,500	2,500
Joint venture A/c…... Dr Commission A/ c ....Cr (The amount of commission at 5% on contract price)	10,000	10,000
Bank A/c… ....Dr Joint venture A/c….. Cr (Received the contract price)	200,000	200,000
Sunil's A/c…...Dr Joint venture A/c….. Cr (Goods taken over by Sunil)	8,000	8,000
Joint venture A/c…... Dr Profit and loss A/c..Cr Sunil's A/c…...Cr (Profit from the venture shared)	21,000	12,000 9,000
Outstanding wages A/c................................... Dr Bank A/c… ....Cr	2,500	2,500

(Paid wages by Anil)		
Sunil's A/c…………………………………………………Dr Bank A/c… ………………………………………………………………………Cr (Paid the amount on final settlement)	76,000	76,000

Joint Venture A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Bank (purchased)	160,000	Bank	200,000
Bank (expenses)	4500	Sunil	8,000
Purchases (material supplied)	10,000		
Outstanding wages	2,500		
Commission (5% on contract price)	10,000		
Profit and loss A/c 12,000 (4/7th of profit)			
Sunil (3/7th of profit) 9,000	21,000		
	208,000		208,000

Sunil A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Joint	8,000	Bank	75,000
ventureBank	76,000	Joint venture (% of profit)	9,000
	84,000		84,000

Illustration: 3

Anu and Anil entered into a joint venture agreement to share the profits and losses in the ratioof 2:1. Anu supplied goods worth Rs.30, 000 to Anil, and incurred expenses amounting to Rs.1, 000 for freight and insurance. During transit the goods costing Rs.2, 500 were damaged and a sum of Rs.1, 500 was received from the insurance company.anil reported that 90% of the remaining goods were sold at a profit of 30% of their original cost. Towards the end of the venture, a fire damaged the balance stock lying unsold with Anil. The goods were not insured and Anil agreed to compensate Anu by paying in cash 80% of the aggregate of the original cost of such goods, plus proportionate expenses incurred by Anu. In addition to the joint venture share of profit, Anil was also entitled to a commission of 5% on net profits of the joint venture after charging such commission. Selling expenses incurred by Aniltotaled Rs. 500. Anil had earlier remitted an advance of Rs. 5,000. Anil paid the balance due to Anu by a bank draft.

Prepare the joint venture account and Anil's account in Anu's books.

Solution:

In the Books of AnuJoint Venture A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Purchased (goods supplied)	30,000	Bank (Insurance)	1,500
Bank (expenses)	1,000	Anil (Sales)	32,175
Anil (expenses)	500	Anil (agreed value of damaged goods)	2,273
Anil (Commission 4,448*5/105)	212		
Profit and loss A/c 2,824			
Anil 1,412	4,236		
	35,948		35,948

Anil's A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Joint venture (Sales)	32,175	Bank (Advance)	5,000
Joint venture (Claim for damaged goods)	2,273	Joint venture(Expenses)	500
		Joint venture (Commission)	212
		Joint venture(Profit)	1,412
		Bank balance (Balance received by draft	27,324
	34,448		34,448

Working Notes:

1. **Computation of sales:**

	(Rs)
Cost of goods sent	30,000
Less: damage in transit	(2,500)
Cost of remaining goods	27,500
Cost of goods sold (90% of 27500)	24,750
Add: profit 30% of Rs. 24750	7,425
Sales	32,175

2. Loss by fire borne by Anil:

	(Rs)
Cost of goods in stock (10% of 27500)	2750
Add: proportionate expenses:	
1000*2750/30000	92
Total loss	2842
80% of this loss	2273

3. Abnormal loss in respect of damage in transit relates to the joint venture. Hence, no computation is required.

When a separate set of books is kept for the Joint Venture

Normally the joint venture activities are undertaken by the person in addition to his normal business activity. For example a building contractor (say A) who is independently handling a big business is awarded a contract jointly with another builder (say B). These persons may not like to disturb their accounting records for this specific activity and may decide to open a separate set of books for the venture.

The co-venturers jointly open a bank account and contribute for the requirements of theventure in money / non-money terms. The main accounts maintained under the system are:

- Joint Bank Account
- Joint venture Account
- Co-venturers Account

  Joint Bank Account is a real account like the ordinary bank account. All the venturers deposit a certain amount into the account. While the joint venture account shows the profits or loss from the venture, the venturers‘ accounts give the amount due to or due by them.

The usual entries under this method are as follows:

1)	Contribution of co-venturers	Joint Bank A/c… .... Dr Co-venturer's personal A/c...........Cr
2)	Goods or any other item contributed by a co-venturer or expenses paid by him.	Joint venture A/c…..Dr Co-venturer's personal A/c...........Cr
3)	For purchase of goods for cash.	Joint venture A/c…..Dr Joint Bank A/c… .... Cr
4)	For purchase of goods on Credit	Joint venture A/c….Dr Creditor's (Suppliers) A/c… ....Cr
5)	For expenses on Joint Venture	Joint venture A/c…..Dr Joint Bank A/c… .... Cr
6)	For good sold (Cash).	Joint Bank A/c… .... Dr Joint venture A/c… ....Cr
7)	Sale on Credit	Debtor's A/c… ....Dr Joint venture A/c… ....Cr
8)	Payment to creditors in cash or issue Bills payable.	Creditors' A/c… .... Dr Joint Bank A/c… .... Cr Bills Payable A/c… .... Cr
9)	Cash or Bills Receivable received from debtors	Joint Bank A/c… .... Dr Bills Receivable A/c..Dr Debtor's A/c… ....Cr
10)	Any Commission, salary, interest etc. payable to any Co-Venturer	Joint venture A/c… ...Dr Co-venturer's personal A/c...........Cr
11)	Part of the stock taken by Co-Venturer	Co-venturer's personal A/c …..Dr Joint venture A/c… ....Cr
12)	For profit on joint venture.	Joint venture A/c… ...Dr Co-venturer's personal A/c...........Cr

13)	For loss on joint venture	Co-venturer's personal A/c...... Dr Joint venture A/c... ....Cr
14)	For payment of the amount due to venturers	Co-venturer's personal A/c..... Dr Joint Bank A/c... .... Cr
15)	For receipt of any amount due by venturers	Joint Bank A/c... .... Dr Co-venturer's personal A/c............Cr

Note: ***Discount received*** should be ***debited*** to Creditor's Account and ***credited*** to Joint Venture Account. Similarly ***discount allowed*** and ***bad debts*** should be ***debited*** to Joint Venture Account and ***credited*** to Debtor's Account.

Illustration: 1

A and B enter into joint venture. A agrees to bring capital in cash. Accordingly a joint bank account is opened by A for a sum of Rs. 80000. B buys goods worth Rs. 50000 as part of his share of capital. Further goods worth Rs. 118000 were purchased from c paying Rs. 60000 and balance by a promissory note signed by A and B.The goods were sent to Calcutta for sale. Expenses totaling Rs. 5000 were incurred in sending the goods. Part goods were damaged and a sum of Rs. 25000 was recovered from the insurance company. The balance goods were sold for Rs. 220000.

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

Solution:

Journal Entries

Description	Rs	Rs
Joint Bank A/c… ....Dr A A/c… .... Cr (Being amount contributed by A)	80,000	 80,000
Joint venture A/c… .... Dr B A/c… .... Cr (Being goods purchased by B on account of joint venture)	50,000	 50,000
C A/c… .... Dr Joint Bank A/c ....Cr Bills Payable A/c… ....Cr (Being payment made to C)	118,000	 60,000 58,000
Joint venture A/c… .... Dr Joint Bank A/c… ....Cr (Being expenses incurred on account of joint venture)	5,000	 5,000
Joint Bank A/c… ....Dr Joint venture A/c… .... Cr (Being amount received from the insurance company for part of goods damaged)		25,000 25,000
Joint Bank A/c… ....Dr Joint venture A/c… .... Cr (Being sales on account of joint venture)	2,20,000	 2,20,000
Bills Payable A/c… ....Dr Joint Bank A/c… ....Cr (Being payment of the promissory note on the due date)	58,000	 58,000
Joint venture A/c… .... Dr A A /c. .... Cr B A /c. .... Cr (Being profit on joint venture transferred to A &B)	72,000	 36,000 36,000

A A /c.. Dr B A /c... Dr Joint Bank A/c… ....Cr (Being payment made to co-venturers in final settlement of their accounts)	1,16,000 86,000	 2,02,000

Joint Venture Account

Particulars	Amount (Rs)	Particulars	Amount (Rs)
B A/c (Goods)	50,000	Joint Bank A/c (Insurance Claim)	25,000
C A/c (Goods)	118,000	Joint Bank A/c (Sales)	220,000
Joint Bank A/c (Expenses)	5,000		
Profit on joint venture transferred to: A A/c 36,000 B A/c 36,000	72,000		
	245,000		245,000

A A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Joint Bank A/c	116,000	Joint Bank A/c	80,000
		Joint venture A/c (Profit)	36,000
	116,000		116,000

B A/c

Particulars	Amount (RS)	Particulars	Amount (RS)
Joint Bank A/c	86,000	Joint venture A/c (Goods)	50,000
		Joint venture A/c (Profit)	36,000
	86,000		86,000

Joint Bank A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)

A A/c	80,000	C A/c	60,000
Joint venture A/c	25,000	Joint venture A/c	5,000
Joint venture A/c	2,20,000	Bills payable A/c	58000
		A A/c	116,000
		B A/c	86,000
	3,25,000		3,25,000

Illustration: 2

Arun and Arvind entered into a joint venture to buy and sell goods, and to share profits and losses in the ratio 2:1. They opened a joint bank account to which Arun contributed Rs. 15000 and Arvind contributed Rs. 10,000.

Arun andArvind purchased goods for Rs. 24000 for the joint venture. Arun supplied goods for Rs. 6000, and Arvind paid for rent and sales expenses of Rs. 3000. They sold goods for Rs. 35000. On closing the venture, the unsold goods were taken over by Arvind for Rs. 4000.

Show journal entries and prepare joint bank account, joint venture account and joint venturers account.

Solution:

Journal Entries

Description	Rs	Rs
Joint Bank A/c… ....Dr Arun's A/c….. Cr Arvind's A/c… ....Cr (opened bank account for the venture with the amount contributed by Arun and Arvind)	25,000	 15,000 10,000
Joint venture A/c…......................... Dr Joint Bank A/c… ....Cr (Goods purchased for the joint venture)	24,000	 24,000
Joint venture A/c…......................... Dr Arun's A/c….. Cr (Supplied goods by Arun)	6,000	 6,000
Joint venture A/c…......................... Dr Arvind's A/c… ....Cr (Supplied goods by Arvind)	3,000	 3,000

Joint Bank A/c… ....Dr Joint venture A/c…... Cr (Being sales on account of joint venture)	35,000	 35,000
Arvind's A/c… ....Dr Joint venture A/c…... Cr (Unsold goods taken over by Arvind)	4,000	 4,000
Joint venture A/c…......................... Dr Arun's A /c... Cr Arvind's A /c. ....Cr (Profit on joint venture shared in the proportion of 2:1)	6,000	 4,000 2,000
Arun's A /c.................................... Dr Arvind's A /c. ....Dr Joint Bank A/c… ....Cr (Payment made to joint venturers in final settlement of theiraccounts)	25,000 11,000	 36,000

Joint Venture Account

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Arun A/c (Goods supplied) Arvind A/c (Expenses) Joint Bank A/c (Goods purchased) Profit on joint venture transferred to: Arun A/c 4,000 Arvind A/c 20,00	6,000 3,000 24,000 6,000	Joint Bank A/c (Sales) Arvind (Unsold goods taken over)	35,000 4,000
	39,000		39,000

Joint Bank A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Arun A/c Arvind A/c Joint venture A/c (sales)	15,000 10,000 35,000	Joint venture A/c (Goods purchased) Arun A/c (final payment)	 24,000 25,000

		Arvind A/c (final payment)	11,000
	60,000		60,000

Arun A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Joint Bank A/c	25,000	Joint Bank A/c (capital contributed)	15,000
		Joint venture A/c (Goods supplied)	6,000
		Joint venture A/c (Profit)	4,000
	25,000		25,000

Arvind A/c

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Joint venture A/c (unsold stock taken over)	4,000	Joint Bank A/c (capital contributed)	10,000
Joint Bank A/c	11,000	Joint venture A/c (Expenses)	3,000
		Joint venture A/c (Profit)	2,000
	15,000		15,000

When joint venture transactions are recorded through the Memorandum Joint Venture Account

Under this method, a co-venturer records only those transactions in which he himself features, for example, goods given for the venture, expenses incurred for the venture, sales made for the venture, goods taken over from the venture etc. the recording mechanism involves making only one account called ― Joint ***Venture With Co-Venturer Investment Account***‖. Hence, A will prepare ‒Joint Venture with B Investment Account‖ and B will prepare ‒Joint Venture with A Investment Account‖. The account is personal account and is used to effect settlement with the co-venturer. (Hence it will not disclose the profit or loss of the venture) All transactions are recorded from the perspective as if the co-venturer is the debtor of the business. The profit or loss of the venture is computed in an account which is not part of the double entry mechanism and hence is appropriately termed as ―***Memorandum Joint Venture Account”*** (pattern of profit and loss account). The term ―***Memorandum***‖ is prefixed as this account does not form part of the double entry system. The memorandum joint venture account is prepared exactly like a joint venture account prepared under the method B and this method is an alternative method of (B) method.

In the above case, the following are the scheme of entries to be given in the books of A;

1)	For goods supplied by A	Joint venture with B A/c… ....Dr Purchase A/c. ....Cr
2)	For expenses incurred by A	Joint venture with B A/c… ....Dr Bank A/c… ....Cr
3)	When a bill of exchange is received from B	Bills Receivable A/c… ....Dr Joint venture with B A/c… ....Cr
4)	If a bill of exchange is given f B	Joint venture with B A/c… ....Dr Bills Payable A/c… ....Cr
5)	When a bill is discounted by A	Bank A/c… ....Dr Joint venture with B A/c… ....Dr Bills Receivable A/c… ....Cr
6)	When goods are sold by A	Bank A/c… ....Dr Joint venture with B A/c… ....Cr
7)	When certain commission is earned by A	Joint venture with B A/c… ....Dr Commission A/c.............................Cr
8)	When unsold stock is taken over by A	Purchase A/c. ....Dr Joint venture with B A/c… ....Cr
9)	If there is any profit from joint venture to A	Joint venture with B A/c… ....Dr Profit and loss A/c .... Cr
10)	If there is any loss from joint venture to A	Profit and loss A/c .... Dr

		Joint venture with B A/c… ....Cr
11)	In case any payment is received by A	Bank A/c… ....Dr Joint venture with B A/c… ....Cr
12)	In case any payment is made by A	Joint venture with B A/c...........Dr Bank A/c… ....Cr

The same set of entries is to be followed in the books of B for preparing joint venture with A

Illustration: 1

On January 1st, 2005, Anu and Sunu entered into a joint venture to deal in second-hand bicycles for a period of twelve months and to share profits and losses equally.

Anu purchased cycles FOR Rs. 30,000 and Sunu purchased for Rs. 35,000. Repairing and other charges paid by Anu was Rs. 6000 and that by Sunu was Rs. 4,000. A nu sold cycles for Rs. 40,000 and Sunu sold for Rs. 45,000. On closing the books on June 30, the unsold cycles of the purchase price of Rs. 7,500 were taken over by Anu at cost plus 10%.

Prepare memorandum joint venture account. Also give journal entries in the books of Anu and Sunu, and show _joint venture with Sunu account‘ in the books of Anu and _joint venture with Anu account‘ in the books off Sunu assuming that the final settlement of accounts was made between Anu and Sunu.

Solution:

Memorandum Joint Venture Account

Particulars	Amount (Rs)	Particulars	Amount (Rs)
Anu A/c :		Anu A/c:	
Cost of cycles 30,000		Sales price	40,000
Repairing 6,000	36,000	Sunu A/c:	
Sunu A/c :		Sales price	45,000
Cost of cycles 35,000		Anu A/c:	
Repairing 4,000	39,000	Cycles (taken over)	8250
Profits:			
Anu A/c 9,125			
Sunu A/c 9,125	18,250		
	93,250		93,250

Books of Anu Journal Entries

Descriptions	Debit	Credit
Joint venture with Sunu A/c…......Dr Bank A/c… ....Cr (The cost of goods bought)	30,000	30,000
Joint venture with Sunu A/c….….. Dr Bank A/c… ....Cr (Paid repairing and other charges)	6,000	6,000
Bank A/c… .... Dr Joint venture with Sunu A/c…...Cr (Sales price of cycles sold)	40,000	40,000
Purchase A/c. .... Dr Joint venture with Sunu A/c…...Cr (Unsold goods taken over at cost plus 10%)	8,250	8,250
Joint venture with Sunu A/c… ....Dr Profit and loss A/c..Cr (The portion of profit)	9,125	9,125
Joint venture with Sunu A/c. ....Dr Bank A/c… ....Cr (Made payment on settlement of the account)	3,125	3,125

Joint Venture with Sunu Account

Particulars	Amount	Particulars	Amount
Bank A/c (Cost of goods bought) Bank A/c (Repair and other charges)Profits and loss A/c	30,000 6,000 9,125	Bank A/c (sales) Purchases A/c (Cycles taken over)	40,000 8,250

Bank A/c	3,125		
	48,250		48,250

Books of Sunu Journal Entries

Descriptions	Debit	Credit
Joint venture with Anu A/c…...........Dr Bank A/c… ....Cr (The cost of goods bought)	35,000	35,000
Joint venture with Anu A/c…..........Dr Bank A/c… ....Cr (Paid repairing and other charges)	4,000	4,000
Bank A/c… ....Dr Joint venture with Anu A/c…... Cr (Sales price of cycles sold)	45,000	45,000
Joint venture with Sunu A/c… ...... Dr Profit and loss A/c .... Cr (The portion of profit)	9,125	9,125
Joint venture with Anu A/c. ....Dr Bank A/c… ....Cr (Made payment on settlement of the account)	3,125	3,125

Joint Venture with Anu Account

Particulars	Amount	Particulars	Amount

Bank A/c (Cost of goods bought) Bank A/c (Repair and other charges)Profits and loss A/c	 35,000 4,000 9,125	Bank A/c (sales) Bank A/c (Final settlement)	45,000 3,125
	48,250		48,250

Illustration: 2

Ravi and Suresh entered into a Joint Venture for purchase and sale of electronic goods, sharing profit& loss in this ratio of 3:2. They also agreed to receive 5% commission on their individual sales and the following information was extracted from the records.

July 1. 2012: Ravi purchased goods worth Rs.1, 90,000 financed to the extent of 90% out of his funds and balance by load from his uncle Shyam.

Aug. 1 2012: Ravi sent goods costing Rs.1, 70,000 to Suresh and paid Rs.1, 410 as freight. Suresh paid Rs.13, 410 to Ravi.

Oct. 1 2012: Suresh sold all the goods sent to him. Ravi paid the loan takes from his uncle including interest of Rs.350.

All sales by either party were made at as uniform profit of 40% after cost. On Nov.30, 2012, they decided to close the venture by transforming the balance of goods unsold lyingwith Ravi at a cost of Rs.9, 000 to a wholesale dealer. They further disclosed that goods worth Rs. 4,000 were taken personally by Ravi at an agreed price of Rs. 5,000.

You are required to prepare the Memorandum Joint Venture Account, Joint Venture with Ravi in the books of Suresh and Joint Venture with Suresh in the books of Ravi.

Solution:

Memorandum Joint Venture Account

Particulars	Amount (RS)	Particulars	Amount (RS)
Ravi A/c:		Suresh A/c:	
Purchase 1,71,000		Sales (17000*140%)	238,000
Purchase(Loan) 19,000	190,000	Ravi A/c:	
Ravi A/c:		Sales (190000 – 170000 – 9000 - 4000) 7000*140%	9,800
Freight 1410		Ravi A/c:	
Interest on loan 350	1,760	Stock	5,000
Suresh A/c:		takenRavi	
Commission		A/c:	
(5% on Rs. 2,38,000)	11,900	(Stock transferred to whole	9,000
Ravi A/c:	490	saleleader)	
Commission			
(5% on Rs. 9800)			
Profit on Venture:	57,650		
Ravi - (3 / 5) 34,590			
Suresh - (2 / 5) 23,060			
	261,8 00		261,800

In the books of Ravi

Joint Venture with Suresh Account

Particulars		Amount (RS)	Particulars	Amount (RS)
Bank A/c			Cash A/c	13,410
(Cost of goods bought)		190,000	Stock taken	5,000
Bank A/c			Stock transferred to whole sale leader	9,000
Freight	1,410			
Interest on loan	350	1,760	Bank A/c (Sale proceeds)	9,800
Commission		490	Bank A/c (Final settlement)	189,630
Share of Profit		34,590		
		226,840		226,840

In the books of Suresh Joint Venture with Ravi Account

Particulars	Amount (RS)	Particulars	Amount (RS)
Cash A/c	13.410	Bank A/c	238,000
Commission	11.900		
Share of Profit	23.060		
Bank A/c (Final settlement)	189.630		
	226,840		226,840

PREPARATION OF FINANCIAL STATEMENTS OF NON-PROFIT ORGANIZATIONS

Until now, we have seen accounting treatment for business transaction of business entities whose main objective is to earn profit. There are certain organizations that are not established for making profit but to provide some service. These services are generally given to members who make subscriptions to avail them. These are also called as non-trading entities.

The examples of such organizations are:

Gymkhana / sports clubs; Educational institutions; Public hospitals; Libraries; Cultural clubs like Rotary or Lions club; Religious institutions; Charitable trusts.

These organizations get their funds in the form of contributions by way of entrance fees, life membership fees, annualsubscriptions, donations, grants, legacies etc. The accounting of such organizations is based on similar principles followed by the other organizations. Given the nature of these institutions, there are certain items of revenue andexpenses that need special understanding so that accounting treatment could be correctly decided.

Special Items

There are certain items of revenue and expenses that are unique for the non-trading entities. They could be listed as:

Revenue items	Expenditure items
Donations	Upkeep of grounds
Entrance fees	Tournament expenses
Subscriptions	Prizes
Grants received	Events

Let us see what accounting treatment should be given to some of the special items:

(a) Entrance Fees – These are received at the time of admission of a new member and thus are one-time fees. They are non-recurring in nature. It could be either capitalized as they are non-recurring or taken as revenueas per the rules of the institution. There's a view that addition of member is an ongoing activity and thus everyyear the institute will get entrance fees. So it may be taken as a normal revenue receipt.

(b) Donations – They could be used for meeting capital or revenue expenses. If donations are received for aspecial purpose, the amount is credited to a fund from which the amounts are disbursed. The fund may be invested in specified securities. Income from such investments is credited to the fund A/c only. Small donation amounts which are not earmarked for any specific purpose may be treated as revenue receipts.

(c) Legacy – Many times trusts are formed in the memory of certain persons by their will. In such case after thedemise of the person, the funds pass on to the institution. Such legacies are of course one-time and thereforeshould be taken to the capital fund.

(d) Endowments – Sometimes, donations are also in the form of endowments to be used as per instructions of thedonor. These are to be treated as capital receipts.

(e) Life membership fees – These could be taken as capital receipts and every year a charge is debited based on some logic. In other words, when received, it could be treated as deferred receipt in the balance sheet and every year a specific amount is credited to I & E A/c.

(f) Subscriptions – These are annual receipts and therefore taken as revenue receipts. These must be recognisedas revenue on the accrual concept.

Financial Statements

These non-profit organisations prepare:-

Receipt and Payment Account – This is similar to cash book. Entries are made on cash basis and items pertainingto previous year or current year or subsequent years are also recorded. Receipts are shown on debit side and payments are shown on credit side. Capital as well as revenue items are entered in the R & P A/c. This account is real account in nature. No provisions are recorded in this account. The account has an opening and a closing balance which is reflected as an asset in the balance sheet.

Features of Receipts and Payments Account

1. It is an Account which contains all Cash and Bank transactions made by a nonprofit organization during aparticular financial period.
2. It starts with the opening balances of Cash and Bank. All Cash Receipts both capital & revenue during theperiod are debited to it.
3. All Cash Payments both capital & revenue during the period are credited to this Account. It ends with theclosing Cash and Bank Balances.
4. While recording the Cash and Bank transactions all entries are made on Cash Basis.
5. It is a summary of Cash Book.
6. It follows Real Account.

Income and Expenditure Account – This is similar to the Profit and loss A/c and is prepared exactly based on sameprinciples. As the name suggests only revenue items are recorded herein. Incomes are recorded on the credit sidewhile the expenses on the debit side. Both incomes and expenses must be taken on the basis of accrual concept. This account should reflect only items that are pertaining to current period. Previous and subsequent year items are to be excluded. This account shows either a surplus or deficit. Excess of income over expenditure is called surplusand excess of expenditure over income is called as deficit.

Features of Income and Expenditure Account

1. It follows Nominal Account.
2. All expenses of revenue nature for the particular period are debited to this Account on accrual basis.
3. Similarly all revenue incomes related to the particular period are credited to this account on accrual basis.
4. All Capital incomes and Expenditures are excluded.
5. Only current year's incomes and expenses are recorded. Amounts related to other periods are deducted.Amounts outstanding for the current year are added.
6. Profit on Sale of Asset is credited. Loss on Sale of Asset is debited. Annual Depreciation on Assets is also debited.

7. If income is more than expenditure, it is called a Surplus, and is added with Capital or General Fund etc. inthe Balance Sheet.

8. If expenditure is more than income, it is a deficit, and is deducted from Capital or General Fund etc. in theBalance Sheet.

Balance Sheet – It is prepared as on the last day of the accounting period. It also has assets and liabilities and prepared based on accounting equation. But, there's no capital account. Instead there is a capital fund. The surplus or deficit from Income & Expenditure A/c is adjusted against this capital fund at the end of the year.

Receipt and Payment Account

Receipts	**Amount (`)**	**Payments**	**Amount (`)**
Starts with opening balance			
All receipts - capital or revenue		All payments - Capital or revenue	
May be related to any period previous,current or subsequent.		May be related to any period previous,current or subsequent.	
		Ends with closing balance	

Income and Expenditure Account

Expenses	**Amount (`)**	**Income**	**Amount (`)**
Only revenue expenses		Only revenue receipts	
Only related to current period		Only related to current period	
Shows either surplus		Or shows deficit	

Difference between Receipts and Payments Account and Income and Expenditure Account

	Receipts & Payments Account	**Income & Expenditure Account**
1.	It is a summarised Cash Book	It closely resembles the Profit & Loss Account of a Tradingconcern.
2.	Receipts are debited and Payments are credited.	Incomes are credited and Expenditures are debited.
3.	Transactions are recorded on Cash basis.	Transactions are recorded on Accrual Basis
4.	Amounts related to previous period or future period may remain included. Outstanding amount for current year is excluded.	Transactions are recorded on accrual basis. All amountsnot related to the current period are excluded. Outstanding amounts of current period are added.
5.	It records both Capital and Revenue transactions.	It records Revenue transactions only.
6.	It serves the purpose of a Real Account.	It serves the purpose of a Nominal Account.
7.	It starts with opening Cash and Bank Balances and ends with closing Cash	It does not record such balances,rather its final balanceshows a surplus or a deficit for the

	and BankBalances.	period.
8.	It does not record notional loss or noncashexpenses like bad debts, depreciations etc.	It considers all such expenses for matching against revenues
9.	Its closing balance is carried forward to the sameaccount of the next accounting Period.	Its closing balance is transferred to Capital Fund or General Fund or Accumulated Fund in the same period'sBalance Sheet.
10.	It helps to prepare an Income & Expenditure A/c.	It helps to prepare a Balance Sheet.

Fund Asset Accounting and its peculiarities:

Following are the concepts of some funds which are generally maintained by organizations:

(i) **Capital Fund :** It is also called "General Fund" or "Accumulated Fund." It is actually the Capital of a non-profit concern. It may be found out as the excess of assets over liabilities. Usually "Surplus" or "Deficit" during a periodis added with or deducted from it. A portion of Capitalised incomes like donations may be added with it.

(ii) **Special Fund:** It may be created out of special donation or subscription or out of a portion of the "Surplus". For example a club may have a "Building Fund". It may be used for meeting some specific expenses or foracquiring an asset. If any income is derived out of investments made against this fund or if any profit or loss occurs due to sale of such investments, such income or profit or loss is transferred to this fund.

(iii) **Donations**

(a) Donation received for a particular purpose should be credited to Special Fund. For example, Donationreceived for Building should be credited to Building Fund A/c.

(b) For other donations received the by-laws or rules of the concern should be followed.

(c) If there is no such rule, donations received of non-recurring nature should be credited to Capital Fund.Recurring donations received should be credited to Income & Expenditure Account.

(d) Donation paid by the concern should be debited to Income & Expenditure Account.

(iv) **Legacy received** : It is to be directly added with Capital Fund after deduction of tax,(if any). It is a kind ofdonation received according to the will made by a deceased person.

(v) Entrance Fees or Admission Fees

(a) The rules or by-laws of the concern should be followed.

(b) If there is no such rule, Admission or Entrance Fees paid once by members for acquiring membershipshould be added with Capital Fund.

(c) If such fees are of small amounts covering the expenses of admission only, the fees may be credited toIncome & Expenditure Account.

(vi) Subscriptions

(a) Annual subscriptions are credited to Income & Expenditure Account on accrual basis.

(b) Life membership subscription is usually credited to a separate account shown as a liability.

Annual Subscription apportioned out of that is credited to Income & Expenditure Account and deducted from the liability. Thus the balance is carried forward till the contribution by a member is fully exhausted. If any memberdies before hand, the balance of his life Membership contribution is transferred to Capital Fund or General Fund.

Illustration 1.

On 31st December 2012, a club had subscription in arrears of `16,000 and in advance `4,000. During the year ended31-12-2013, the club received subscription of `2,08,000 of which `10,400 was related to 2014. On 31st December2012, there were 4 members who had not paid subscription for 2013 @ `1,600 per person. Write up subscription A/cfor the year 2013.

Solution:

A single subscription account should be prepared to reflect both advance and arrears figures. The balancing figure will reflect the subscription amount that will be recognised as Income and transferred to I & E A/c as shown below:

Subscription Account

Particulars	**Amount (`)**	**Particulars**	**Amount (`)**
To, Balance b/d (arrears)	16,000	By, Balance b/d (advance)	4,000
To, I & E A/c (income for 2013)	1,92,000	By, R & P A/c (received)	2,08,000
To, Balance c/d (advance)	10,400	By, Balance c/d (arrears)	6,400
	2,18,400		2,18,400

Illustration 2.

The sports club of Orissa had received in 2012-2013 ` 2,000 towards subscription. Subscription for 2011-12 unpaid on 1.4.2012 were ` 200.Subscriptions paid in advance on 31.3.2012 were ` 50 and the same on 31.3.2013 was ` 40. Subscriptions for 2012- 2013 unpaid on 31.3.2013 were ` 90.Show how the subscriptions item will appear in the Income and Expenditure Account.

Solution:

Particulars	**Amount (`)**
Subscriptions received during the year 2012-2013	2,000
Add : Subscription outstanding on 31.3.2013	90

	2,090
Less : Subscription outstanding on 1.4.2012	200
	1,890
Add : Subscription paid in advance on 31.3.2012	50
	1,940
Less : Subscription received in advance on 31.3.2013	40
Subscription Income for 2012-2013	1,900

Illustration 3.

The amount of Subscription appears in the Income and Expenditure Account of South Indian Club is ` 3,000.Adjustments were made in respect of the following: Subscription for 2012 unpaid at 1st Jan. 2013, ` 400; ` 200 of which was received in 2013. Subscription paid in advance at 1.1.2013 100.Subscription paid in advance at 31.12.2013 ` 80. Subscription for 2013 unpaid at 31.12.2013 ` 140.Prepare Subscription Account.
Solution:

Subscription Account

Particulars	Amount (`)	Particulars	Amount (`)
To, Balance b/d	400	By, Balance b/d	100
To, Income & Expenditure A/c	3,000	By, Cash Received (bal fig)	3,040
To, Balance (paid in advance to 2013)	80	By, Balance c/d	340
		[200 + 140]	
	3,480		3,480
To, Balance b/d:		By, Balance b/d (2013)	80
For 2012	200		
For 2013	140		

Note: Opeaning Outstanding Subscription = ` 400, ` 200 received in 2013.

Illustration 4.

From the following information, prepare the Subscription Account for the year ending on March, 31, 2013

(i) Subscription in arrears on 31.03.2012 ` 1,500

(ii) Subscription received in advance on 31.03.2012 ` 1,000

(iii) Amount of Subscription received during 2012-13 ` 40,000, which includes `500 for the year 2011-12, ` 1,500 for the year 2013-14.

(iv) Subscription outstanding ` 1,000.

Solution:

Subscription Account

Particulars	**Amount (`)**	**Particulars**	**Amount (`)**
To, Balance b/d	1,500	By, Balance b/d	1,000
To, Income & Expenditure A/c	39,500	By, Bank A/c	40,000
		By, Balance c/d	
		For 2011-12	500
To, Balance c/d		For 2012-13	1,000
For 2013-14	1,500		
	42,500		42,500

Illustration 5.

The accumulated balance of Life Membership fees at the beginning of the year 2012 was `6,40,000. This representsthe balance of life membership fees paid by 20 members since the club started about 6 years ago. In the currentyear, 10 new life memberships were received totaling ` 4,00,000.It's the policy of the club to spread these fees over 20 years to income. The amount payable per person is always` 40,000.What is the amount to be recognised as income for the current year and what amount will be deferred through the balance sheet?

Solution:

Income to be recognised for new members

Life membership fees per person	`40,000
Income to be spread over	20 years
Income to be recognised each year	`2,000
Members added during the year	10
Income to be recognised (10×2000)	`20,000
Amount to be carried forward	`3,80,000
Income to be recognised for old members	
No. of members	20
Income to be recognised each year	`2,000
Income to be recognised (20×2000)	`40,000
Total income to be recognised (20,000+40,000)	`60,000
Amount to be shown in the balance sheet	
Accumulated Balance	`6,40,000
Add: New fees received	`4,00,000
Less: Recognised as income	(`60,000)
Balance to be carried forward	`9,80,000

Restaurant Trading and Bar Trading

Some clubs have Restaurant and Bar facilities for members and outsiders. Under the circumstances, Restaurant Trading or Bar Trading Account is opened to ascertain the Restaurant or Bar profit, it is just like Trading Account whichis opened in case of a trading concern. The Restaurant or Bar profit so ascertained from Restaurant Trading or BarTrading is transferred to the Income and Expenditure Account as we generally transfer the Gross Profit from Trading Account to Profit and Loss Account in case of Trading concern. Hence, the method of preparing a Restaurant or Bar Trading Account is just like the method of preparing a Trading Account.

Illustration 6.

The following summary of the Cash Book has been prepared by the treasurer of a club:

	Receipts	**Amount (`)**		**Payments**	**Amount (`)**
To	Balance b/d	4,740	By	Wages – outdoor staff	13,380
”	Subscriptions	29,720	”	Restaurant Purchase	50,400
”	Entrance Fees	3,200	”	Rent – 18 months’ to July 30, 2013	7,500
”	Restaurant Receipts	56,800	”	Rates	2,700
”	Games & Competition Receipts	13,640	”	Secretary’s Salary	3,120
”	Due to Secretary for Petty Expenses	80	”	Lighting	7,200
			”	Competition Prizes	4,000
			”	Printing & Postage etc.	6,000
			”	Placed in Fixed Deposit	8,000
			”	Balance c/d	5,880
		1,08,180			**1,08,180**

On April 1, 2012 the club’s assets were:- Furniture ` 48,000, Restaurant stock ` 2,600; Stock of prizes ` 800; ` 5,200was owing for supplies to the restaurant.On March, 31, 2013, the Restaurant stocks were ` 3,000 and prizes in hand were ` 500, while the club owed ` 5,600for restaurant supplies.It was also found that subscriptions unpaid at March 31, 2013, amounted to ` 1,000 and that the figure of ` 29,720 shown in the Cash Book included ` 700 in respect of previous year and ` 400 paid in advance for the following year.

Prepare an account showing the Profit or Loss made on the Restaurant and a General Income and Expenditure Account for the year ended 31.3.2013, together with a Balance Sheet as at that date, after writing 10% off the Furniture.

Solution:

Restaurant Trading Account

For the year ended 31st March, 2013

Particulars	Amount (`)	Amount (`)	Particulars	Amount (`)	Amount (`)
To Opening Stock A/c		2,600	By Restaurant Receipts A/c		56,800
” Purchases A/c	50,400		” Closing Stock A/c		3,000
” Add: Outstanding for 31.3.13	5,600				
	56,000				
Less: Outstanding for 01.04.12	5,200				
		50,800			
” Income & Expenditure A/c(G.P. transferred)		6,400			
		59,800			**59,800**

Balance Sheet as at 1st April, 2012

Liabilities	Amount (`)	Assets	Amount (`)
Accumulated Fund: (bal. fig.)	50,390	Furniture and Equipment	48,000
Owing for supplies to Restaurant	5,200	Restaurant Stock	2,600
Outstanding Rent (Jan. to March 2012)	1,250	Stock of Prize	800
		Outstanding Subscriptions	700
		Cash and Bank	4,740
	56,840		**56,840**

Income and Expenditure Account

For the year ended 31st March, 2013

Expenditure	Amount (`)	Amount (`)	Income	Amount (`)	Amount (`)
To Wages		13,380	By Subscription : Subscription already received	29,720	

`` Rent	7,500		Less: Outstanding for 1.4.12	700	
`` Less: Outstanding on 1.4.2012	1,250			29,020	
	6,250		Add: Outstanding for 2013	1,000	
`` Less: Prepaid for 3 months(7,500 x 3/18)	1,250	5,000		30,020	
`` Rates		2,700	Less: Received in advance	400	29,620
``Secretary's Salary		3,120	`` Games Competition Receipts		13,640
`` Lighting, Cleaning, Services		7,200	`` Restaurant Trading – Gross Profit		6,400
`` Competition Prize	4,000				
`` Add: Opening Stock	800				
	4,800				
`` Less: Closing Stock	500	4,300			
`` Printing, Postage and Sundries		6,000			
`` Dep. on Furniture andEquipment @ 10%		4,800			
`` Surplus – Excess of income overexpenditure		3,160			
		49,660			**49,660**

Balance Sheet as at 31st March, 2013

Liabilities	**Amount (`)**	**Amount (`)**	**Assets**	**Amount (`)**	**Amount (`)**
Accumulated Fund:			Furniture and Equipment	48,000	
Balance on 1.4.2012	50,390		Less: Depreciation	4,800	43,200
Add: Surplus	3,160	53,550	Restaurant Stock		3,000
Entrance fees		3,200	Stock of Prize		500
Subscription received in advance		400	Outstanding Subscriptions		1,000
Owing for supplies to Restaurant		5,600	Prepaid Rent		1,250
Outstanding Petty Expenses		80	Fixed Deposit with Bank		8,000
			Cash and Bank		5,880
		62,830			62,830

Illustration 7.

Prepare Income & Expenditure A/c for the year ended 31-12-2013 and the balance sheet as on 31-12-2013 in the books of an Education society.

Particulars	Debit (`)	Credit (`)
Library Books	2,30,000	
Books Added during the year	52,200	
Furniture	1,59,500	
Addition to Furniture	35,500	
Buildings	37,89,000	
Investment	21,25,000	
Creditors		1,77,900
Debtors	59,700	
Investment Reserve Fund		1,85,000
Entrance Fees		2,02,600
Examination Fees		32,500
Certificate Fees		7,800
Subscriptions Received		2,75,800
Hire Charges		95,500
Interest		85,000
Other Receipts		4,400
Salary	1,55,900	
Printing & Stationery	8,500	
Postage & Telephone	2,500	
Insurance	10,400	
Examination Expenses	24,000	
Periodicals	15,600	
Prizes Fund		2,15,000
Prizes Investments	2,10,400	
Prizes Investment Income		10,200
Prizes Given	9,500	
Prizes Bank Balance	2,450	
Donations (capital)		1,99,000
General Expenses	5,250	
Capital Fund		54,71,720
Bank Balance	65,500	
Cash in Hand	1,520	
Total	69,62,420	69,62,420

Additional information :

Subscription receivable `22,500, subscription received for 2014 `7,850, Interest accrued on investments `6,250, salaryoutstanding for 2013 `12,500, Prepaid insurance `4,500.Depreciate Books @ 15%, Building @ 1% and Furniture @ 10%.

Solution:

Income & Expenditure Account for the year ended 31.12.2013

Expenditure	Amount (`)	Amount (`)	Income	Amount (`)	Amount (`)
To Salary	1,55,900		By Examination fees		32,500
Add: Outstanding	12,500	1,68,400	By Certificate fees		7,800
To Printing & Stationery		8,500	By Subscriptions	2,75,800	
To Postage & Telephone		2,500	Add: Receivable	22,500	
To Insurance	10,400		Less: Pre-received	(7,850)	2,90,450
Less: Prepaid	(4,500)	5,900	By Hire charges		95,500
To Examination Expenses		24,000	By Interest		85,000
To Periodicals		15,600	By Other Receipts		4,400
To General Expenses		5,250	By Accrued interest		6,250
To Depreciation on Books		38,415			
To Depreciation on Building		37,890			
To Depreciation onFurniture		17,725			
To Surplus		1,97,720			
		5,21,900			5,21,900

Balance Sheet as at 31.12.2013

Liabilities	Amount (`)	Amount (`)	Assets	Amount (`)	Amount (`)
			Buildings	37,89,000	
			Less: Depreciation @ 1%	(37,890)	37,51,110
Capital Fund	54,71,720		Library Books	2,30,000	
Add: Entrance fees	2,02,600		Add: Purchased in 2012	52,200	
Add: Donations	1,99,000		Less: depreciation @ 15%	(38,415)	2,43,785
Add: Surplus	1,97,720	60,71,040	Furniture & fixture	1,59,500	
			Add: Purchased in 2012	35,500	
			Less: Depreciation @ 10%	(17,725)	1,77,275
Investment Reserve Fund		1,85,000			

Prize Fund	2,15,000		Investment		21,25,000
Add: Fund Income	10,200		Prize Investments		2,10,400
Less: Fund Expenses	(9,500)	2,15,700	Debtors		59,700
Creditors		1,77,900	Prize Bank balance		2,450
Subscription received inadvance		7,850	Bank balance		65,500
Salary Outstanding		12,500	Cash in hand		1,520
			Subscription receivable		22,500
			Interest Accrued		6,250
			Prepaid Insurance		4,500
		66,69,990			66,69,990

Illustration 8

The following information was obtained from the books of Young Bengal Club as on 31-03-2013 at the end of firstyear of the club. Prepare the Receipts & Payments A/c, Income & Expenditure A/c and Balance sheet of the club

(1) Donations received for Building & Books - ` 2,00,000

(2) Other revenue incomes and receipts were:

	Rev. Income (`)	**Actual Receipts (`)**
Entrance fees	17,000	17,000
Subscription	20,000	19,000
Locker rent	600	600
Sundry Income	1,600	1,060
Refreshment account	Nil	16,000

(3) Other revenue expenditure and actual payments were

	Rev. Exp (`)	**Actual Payment (`)**
Land (cost `10,000)	Nil	10,000
Furniture (cost ` 146,000)	Nil	130,000
Salaries	5,000	4,800
Maintenance of play ground	2,000	1,000
Rent	8,000	8,000
Refreshment account	Nil	8,000

Donations were utilized to the extent of `25,000 for buying books, balance were unutilized. In order to keep it safe, 9% Govt. Securities were purchased on 31-3-2013 for `1, 60,000. Remaining amount was put in bank as term deposit on 31-3-2013. Depreciate Furniture and books @ 10% for the whole year.

Solution:

Receipt and Payments for the year ended 31.3.2013

Receipts	Amount (`)	Payments	Amount (`)
To Donations	2,00,000	By Library books	25,000
To Entrance fees	17,000	By Land	10,000
To Subscription	19,000	By Furniture	1,30,000
To Locker Rent	600	By Salaries	4,800
To Sundry income	1,060	By Maintenance	1,000
To Refreshment A/c	16,000	By Rent	8,000
		By Refreshment A/c	8,000
To Balance c/d (Overdraft) (Bal. fig.)	1,08,140	By 9% Govt. Securities	1,60,000
		By Term deposits	15,000
	3,61,800		3,61,800

Income and Expenditure Account for the year ended 31.3.2013

Expenditures	`	`	Incomes	`	`
To Salary	4,800		By Subscriptions	19,000	
Add: Outstanding	200	5,000	Add: Outstanding	1,000	20,000
`` Playground maintenanceAdd: Outstanding	1,000		`` Locker Rent		600
	1,000	2,000	`` Sundry Income	1,060	
`` Rent		8,000	-Add: Outstanding	540	1,600
`` Depreciation on:Furniture	14,600		`` Profit on Refreshment		8,000
Library Books	2,500	17,100	`` Deficit (Excess of Expenditure over Income)		1,900
		40,100			40,100

Balance Sheet as at 31st March 2013

Liabilities	`	`	Assets	`	`
Capital Fund		---	Land		10,000
Entrance Fees		17,000	Furniture	1,46,000	
Donation for Building.			Less: Depreciation	14,600	1,31,400

Library Room Fund		2,00,000	Library Books	25,000	
Creditors for Furniture		16,000	Less: Depreciation	2,500	22,500
Outstanding Salaries		200	9% Govt. Bond		1,60,000
Outstanding Expenses for Playground		1,000	Subscription Receivable		1,000
			Accrued Sundry Income		540
Bank overdraft		1,08,140	Bank Term Deposit		15,000
			Deficit		1,900
		3,42,340			3,42,340

Workings:

Refreshment Account

Particulars	**Amount (`)**	**Particulars**	**Amount (`)**
To, Payment for Refreshment	8,000	By, Refreshment Receipts	16,000
To, Income and Expenditure A/c (Profit on Refreshment)	8,000		
	16,000		16,000

(1) Calculation of Term Deposit:

Donation Recd – (library books purchase + 9% Govt. Securities)

= 2,00,000 – (25,000 + 1,60,000)

= 2,00,000 – 1,85,000

=15,000

(2) Since there was no capital fund

(3) Donation received for Building and Library Room is treated as capital item.

(4) Since the investment in Govt. Securities has been made at the closing date of the year, no interest hasaccrued.

HIRE-PURCHASE AND INSTALLMENT SYSTEM

It is not always possible by a purchaser to meet up the higher demand for goods due to immediate cash payment. To meet this demand the concept of Hire Purchase is very popular in the market.

Under this system the purchaser **(Hirer)** pays the entire amount in staggered way viz. monthly, quarterly or yearly with some interest. Under this system the goods are sold with the following conditions:

Possession of goods is delivered to a hirer but the title to the goods (Ownership) are transferred only when the agreed sum (Hire Purchase price) is paid by the hirer.

Such hirer has a right to terminate the agreement at any time before the property so passes. That means he hasthe option to return the goods in which case he need not pay installments falling due thereafter. However, the hirer cannot recover the sums already paid as such sums legally represent hire charges of the goods in question.

The hire-purchaser, during that period of possession of goods, cannot damage, destroy, pledge or sell such goods. He is supposed to take all such care of goods as a prudent person does in his own goods.

In case of Installment Sale, it is not only the possession of goods but also the *ownership* in goods is transferredto the buyer immediately at the time of agreement.

Further, in installment system if the buyer stops the payment of dues, then he does not have the right of seizing his goods. The differences between installment sale and hire-purchase are as below:

Particulars	Hire Purchase	Installment Sale
Ownership	Stipulates the time at which the ownership passes to the buyer. It is usually on the payment of last installment.	Ownership passes at the time of sale.
Default in making payment	Seller can repossess the goods. In that case the installment so far paid is treated to be Hiring charges.	Seller does not have any other right except the right of suing the buyer for the non-payment of price.
Right of sale or other wise	No right to sale or otherwise transfer the goods since the legal position of the hirer is bailee.	Right to sale or otherwise transfer the goods.
Loss or damagesto the goods.	Any loss occurring to goods has to be borne by the seller if the buyer takes reasonable care.	Any loss occurring to goods has to be borne by the buyer.

SITUATION – I : WHEN RATE OF INTEREST, TOTAL CASH PRICE AND IN STALLMENTS ARE GIVEN

Illustration 1.

X purchases a car on hire-purchase system on 1.1.11. The total cash price of the car is ` 4,50,000 payable ` 90,000down and three installments of ` 1,70,000, ` 1,50,000 and ` 1,08,460 payable at the end of first, second and third year respectively. Interest is charged at 10% p.a.

You are required to calculate interest paid by the buyer to the seller each year.

Solution: Following table is useful for calculating interest paid with each installment :

Analysis of Instalments

Year	Opening Balance ofCash Price `	Installments `	Payment towards Principal/Cash Price `	Payment towards Interest `	Closing Balanceof Cas Price `
01.01.11	4,50,000	90,000	90,000	- 36,0	3,60,0
31.12.11	3,60,000	1,70,000	1,34,000	22,6	2,26,0
31.12.12	2,26,000	1,50,000	1,27,400	9,8	98,6
31.12.13	98,600	1,08,460	98,600		

SITUATION – II : WHEN RATE OF INTEREST AND INSTALLMENTS ARE GIVEN BUT TOTAL CASH PRICE IS NOT GIVEN.

Illustration 2.

X purchased a T.V on hire-purchase system. As per terms he is required to pay ` 3000 down, ` 4000 at the end of first year, ` 3000 at the end of second year, and ` 5000 at end of third year. Interest is charged at 12% p.a. You are required to calculate total cash price of T.V and interest paid with each installment.

Solution :

Calculation of Cash Price	Installment `	Analysis of Instalments	
		Interest `	Cash Price `
3rd Instalment			
(-) Interest (12/112 × 5,000)	5,000		
	536		
Balance of Cash Price	4,464	536	4,464
(+) 2nd Instalment	3,000		
	7,464		
(-) Interest (12/112 × 7,464)	800	800	2,200
Balance of Cash Price	6,664		
(+) 1st Instalment	4,000		
	10,664		
(-) Interest (12/112 × 10,664)	1,143	1,143	2,857
Balance of Cash Price	9,521		
(+) Down Payment Total Cash Price	3,000	- 2,479	3,000
	12,521		12,521

SITUATION – III : WHEN ONLY INSTALLMENTS ARE GIVEN, BUT CASH PRICE AND RATE OF INTEREST ARE NOT GIVEN.

Illustration 3.

X & Co. purchased a Motor car on April 1, 2009 on hire-purchase paying ` 60,000 cash down and balancein four annual installments of ` 55,000, ` 50,000, ` 45000 and ` 40,000 each Installment comprising equal amount of cash price at the end of each accounting period. You are required to calculate total cash price and amount of interest in each Installment.

Solution : Hire-purchase Price

Down Payment	60,000
1st installment	55,000
2nd installment	50,000
3rd installment	45,000
4th installment	40,000
Total	2,50,000

As each installment comprises equal amount of cash price the differences in installment amounts are due to interest amount only. Assuming X is the amount of Cash Price in each installment and I is the amount of interest.

Thus for the installments, starting from last installment, we have the following equations:

(i)	X + I	=	40,000
(ii)	X + 2I	=	45,000
(iii)	X + 3I	=	50,000
(iv)	X + 4I	=	55,000

Subtracting any preceding equation from the following equation we get I = ` 5,000 and by substituting the value of I in any equation we get X = ` 35,000.

The hire-purchase price is divided into cash price and interest parts as under :

Particulars	Cash Price `	Interest `	Installment `
Down Payment	60,000	-	60,000
First installment	35,000	20,000	55,000
Second installment	35,000	15,000	50,000
Third installment	35,000	10,000	45,000
Fourth installment	35,000	5,000	40,000
Total	2,00,000	50,000	250,000
Total Cash Price	2,00,000		
Hire Purchase Price	2,50,000		
Total Interest	50,000		

SITUATION – I V : WHEN REFERENCE TO ANNUITY TABLE RATE OF INTEREST AND INSTALLMENTS ARE GIVEN BUTTOTAL CASH PRICE IS NOT GIVEN.

In such questions the reference to annuity table gives the present value of the annuity for a number of years ata certain rate of interest. This present worth is equal to total cash price.

Therefore, with the help of annuity tablesthe total cash price of the total installments given can be calculated and then question can be solved by the firstmethod.

ACCOUNTING TREATMENT

Accounting treatment in the books of buyer is presented in below :

In the Books of the Hire-Purchaser

Cash Price Method:

	Particulars	Debit (`)	Credit (`)
1.	Hire Purchase A/c Dr.	xxxx	
	To, Hire Vendor A/c [Cash price]		xxxx
2.	Hire Vendor A/c Dr.	xxxx	
	To, Bank A/c [Down payment]		xxxx
3.	Interest A/c Dr.	xxxx	
	To, Hire Vendor A/c		xxxx
4.	Hire Vendor A/c Dr.	xxxx	
	To, Bank A/c [Instalment amount]		xxxx
5.	P/L A/c Dr.	xxxx	
	To, Interest A/c		xxxxxxxx
	To, Depreciation A/c		

Interest Suspense Method:

	Particulars	Debit (`)	Credit (`)
1.	Hire Purchase Asset A/c [Cash Price] Dr.	xxxxxxxx	
	Interest Suspense A/c [Total Interest] Dr.		
	To, Hire Vendor A/c [H.P price]		xxxx
2.	Hire Vendor A/c Dr.	xxxx	
	To, Bank A/c [Down payment]		xxxx
3.	Interest A/c Dr.	xxxx	
	To, Interest Suspense A/c		xxxx
4.	Hire Vendor A/c Dr.	xxxx	
	To, Bank A/c [Instalment amount]		xxxx
5.	P/L A/c Dr.	xxxx	
	To, Interest A/c		xxxxxxxx
	To, Depreciation A/c		

Meaning of Complete or Full Repossession

In case of complete or full repossession the hire vendor takes back the possession of all the goods.

Journal Entries under Complete or Full Repossession

All Entries till the date of default are passed in the usual manner. The additional Entries are as follows:

Books of Hire Purchaser	Books of Hire Vendor
1. For Closing Hire Vendor's Account Hire Vendor's A/c Dr. To Asset A/c **Note:** This entry is passed with the amount due to thehire-vendor.	**1. On Repossession of goods** Goods Repossessed A/c Dr. To Hire Purchaser's A/c **Note:** This entry is passed with the revalued amountof goods repossessed.
2. For Closing Asset Account **(i) If the Book Value of the Asset exceeds the amountdue to Hire-Vendor** Profit & Loss A/c Dr. To Asset A/c **(ii) If the amount due to Hire-Vendor exceeds the BookValue of the Asset** Asset A/c Dr. To Profit & Loss A/c	**2. For amount spent on reconditioningof Goods Repossessed** Goods Repossessed A/c Dr. To Cash A/c/Bank A/c **3. For sale of Goods Repossessed** Cash A/c/Bank A/c /Debtors A/c Dr. To Goods Repossessed A/c **4. For loss on sale of Goods Repossessed** Profit & Loss A/c Dr. To Goods Repossessed A/c **Note:** In case of profit, a reverse entry will be passed.

Illustration 7.

On 1.1.2011, A purchased 5 Machines from B. Payment was to be made — 20% down and the balance in four annual instalments of `2,80,000, ` 2,60,000, ` 2,40,000 and ` 2,20,000 commencing from 31.12.2011. The vendor charged interest @ 10% p.a. A, writes off depreciation @ 20% p.a. on the original cost.

On A's failure to pay the instalment due on 31.12.2012, B repossessed all the machines on 01.01.2013 and valuedthem on the basis of 40% p.a. depreciation on W.D.V. basis. B after incurring `6,000 on repairs sold the machinesfor `2,66,000 on 30th June 2013. Prepare the relevant accounts in the books of A and B.

Solution:

Computation of Cash Price and Periodic Interest

A Instalment Number	B Closing Balance after the Paymentof Instalment	C Instalment Amount	D = B + C Closing Balance before the payment ofInstalment	E = D × R/(100 + R) Interest D × 10/110	F = D-E Opening Balance
IV	—	2,20,000	2,20,000	20,000	2,00,000
III	2,00,000	2,40,000	4,40,000	40,000	4,00,000
II	4,00,000	2,60,000	6,60,000	60,000	6,00,000
I	6,00,000	2,80,000	8,80,000	80,000	8,00,000

Let the cash price be 'X

X = ` 8,00,000 + 20% of X (i.e. down payment) 0.8X = ` 8,00,000X = ` 8,00,000/0.8 = `10,00,000

Ledger Accounts in the book of A

Machinery Account .

Date	Particulars	`	Date	Particulars	`
01.01.11	To B's A/c	10,00,000	31.12.11	By Depreciation A/c	2,00,000
				By Balance c/d	8,00,000
		10,00,000			**10,00,000**
01.01.12	To Balance b/d	8,00,000	31.12.12	By Depreciation A/c	2,00,000
				By Balance c/d	6,00,000
		8,00,000			**8,00,000**
01.01.13	To Balance b/d	6,00,000	01.01.13	By B's A/c	6,60,000
	To P&L A/c (Profit)	60,000			
		6,60,000			**6,60,000**

B's Account

Date	Particulars	`	Date	Particulars	`
01.01.11	To Bank A/c (Down payment)	2,00,000	01.01.11	By Machinery A/c	10,00,000
31.12.11	To Bank A/c [`2,00,000 + `80,000]	2,80,000	31.12.11	By Interest A/c [(`10,00,000 - `2,00,000) × 10/100]	80,000
	To Balance c/d	6,00,000			
		10,80,000			**10,80,000**
31.12.12	To Balance c/d	6,60,000	01.01.12	By Balance b/d	6,00,000
				By Interest A/c (`6,00,000 × 10/100)]	60,000
01.01.13	To Machinery A/c	6,60,000	01.01.13	By Balance b/d	6,60,000

Ledger Accounts in the books of B

A's Account

Date	Particulars	`	Date	Particulars	`
01.01.11	To H.P. Sales A/c	10,00,000	01.01.11	By Bank A/c (Down Payment)	2,00,000
31.12.11	To Interest A/c [(`10,00,000 - `2,00,000) × 10/100]	80,000	31.12.11	By Bank A/c (`2,00,000 + `80,000)	2,80,000
				By Balance c/d	6,00,000
		10,80,000			**10,80,000**
01.01.12	To Balance b/d	6,00,000	31.12.12	By Balance c/d	6,60,000
31.12.12	To Interest A/c [`6,00,000 × 10/100]	60,000			
		6,60,000			**6,60,000**

01.01.13	To Balance b/d	6,60,000	01.01.13	By H.P. Goods Repossessed A/c	3,60,000
				By Profit & Loss A/c	3,00,000
		6,60,000			**6,60,000**

H.P. Goods Repossessed Account

Date	Particulars	`	Date	Particulars	`
01.01.13	To A's A/c	3,60,000	30.06.13	By Bank A/c	2,66,000
	To Bank A/c	6,000		By P&L A/c	1,00,000
		3,66,000			**3,66,000**

ROYALTIES

Introduction

The owner of an asset (e.g. mines, quarries, patent, copyright, etc), as a business arrangement, may allow otherparty (lessee, licencee, publisher, etc) the right to use that asset against some consideration. Such considerationis calculated with reference to the quantity produced or sold. This payment to the owner by the user of the assetis termed as **Royalty.**

We can therefore say that the royalty is the amount of consideration paid by a party to the owner of the asset inreturn for the right to use that asset.

For example, when a publisher publishes a book, he makes a payment to the author which is based on the number of copies sold known as royalty.

The following are some of cases where one party paid to another in the form of Royalty:

1. where the owner of a mine allows another the right to extract minerals from land;
2. where right such as patents or copyrights are licensed in favour of another;
3. where an author, artist or designer gives exclusive rights to another to copy the work.

Common terms Used in Connection with Accounting for Royalty :

1. **Minimum Rent / Dead Rent**

A contract is entered into between the landlord and the lessee for payment of royalty, usually calculated uponthe quantum of production or sale at a certain stipulated rate.

So, if there is little or no production or sale, the landlord would receive little or no royalty at all, thus affects the monetary interest of the landlord as well as the lessee. It is normally not acceptable to the owner, since sale or production mostly depends on the capacity of the person to whom the rights have been given. To avoid such a situation, the landlord and the lessee agreed upon a minimum periodical amount that the landlord will receivefrom the lessee, even if the actual royalty as calculated on the basis of actual production or sale is less than such minimum amount.

This assured and mutually agreed periodical minimum amount is known as **"Minimum Rent".**

Example: Suppose royalty per ton of production is ` 10 and the minimum (annual) rent is ` 4,00,000. Now, the actual production is 35,000 tons, then actual royalty would become ` 3,50,000. In this case the minimum rent of ` 4,00,000 will have to be paid by the lessee. On the other hand, if the actual production is 46,000 tons, thenthe actual royalty would become ` 4,60,000. In this case ` 4,60,000 will have to be paid by the lessee.

Thus, as there is a stipulation for minimum rent, then either the minimum rent or the actual royalty whichever is moreshall have to be paid by the lessee.

The minimum rent is also called dead rent, certain rent, fixed rent, etc.

2. Short workings/Redeemable Dead Rent

Short workings is the amount by which the minimum rent exceeds the actual royalty. It is the difference between Actual Rent and Minimum Rent.
In the above example, the short workings is ` 50,000 (` 4,00,000 – ` 3,50,000). Where there is

short workings in any period the lessee is liable to pay the minimum rent and, in effect, short workings becomes the part of the minimum rent and not represented by the use of rights.

The question of short workings will arise only when there is a stipulation for minimum rent in the agreement.

3. Excess working

It refers to the amount by which the actual royalty exceeds the minimum rent. In the above example, the excess workings is ` 60,000 (` 4,60,000 – ` 4,00,000) if the production is 46,000 tons.

4. Ground Rent/Surface Rent

It refers to the fixed yearly or half-yearly rent payable by the lessee to the landlord in addition to the minimum rent.

5. Recoupment of Short workings

Generally the royalty agreement contains a provision for carrying forward of short workings with a view to adjustit in the future. In the subsequent years, such shortworking is adjusted against the surplus royalty. This process ofadjustment is called recoupment of short workings. The right of recoupment of short workings enables the lesseeto recover the excess payment, made in the earlier years to meet the condition of payment of minimum rent. A time is usually agreed upon the number of years for which such short workings can be recouped. This time limit for recoupment of short workings may be fixed or fluctuating. If the short workings cannot be recouped within thespecified time, they lapse and are charged to Profit and Loss Account in the year when that specified time limit for recoupment ends.

(i) Fixed right :

When the lessee can recoup shortworkings within a certain period from the date of the lease it is known asfixed right. For example, short workings can be recouped within three years from the date of the lease. So, after three years from the date of the lease the short workings cannot be recouped.

(ii) Fluctuating right :

In this type of agreement, lessee can recoup short workings of any year during the next following year(s). For example, shortworkings can be recouped in the year subsequent to the year of short workings.

6. Strike and Lockout, etc :

If agreement so provides, the minimum rent may be proportionately reduced in the event of strike and/ or lockout. So special entry is required for the same except the adjustment of minimum rent for that particular year.

Accounting Entries in the Books of the Lessee/Licencee/Publisher etc.

1. Where a minimum rent exists with right to recoup short workings

(a) Where the actual royalty is less than the minimum rent

(i) Royalties (payable) Account Dr. [Actual royalties for the period]

Short workings Account Dr. [Minimum rent - Actual royalties]

To Landlord Account [Minimum rent]

(ii) Landlord Account Dr. [Minimum rent]

To Bank Account [Net amount paid]

To Income Tax Payable Account [Tax deducted at source]

(iii) Manufacturing / Profit & Loss Account Dr. [Transfer]

To Royalties (payable) Account [Actual royalties for the period]

If the user is a manufacturer and royalties are calculated on the basis of production, the actual royalties are debited to Manufacturing Account. Where royalties are calculated on the basis of sales, they are debited to Profit and Loss Account.

In case of a limited company, which does not prepare Manufacturing Account separately, the actual royaltiesare debited to Profit and Loss Account and they are shown in production or manufacturing section of the Profit and Loss Account.

Treatment of Short workings

As per agreed terms, short workings can be recouped in the year when the actual royalty is more than the Minimum rent. Any short workings, which cannot be recouped within the specified period becomes irrecoverable and it should be charged to Profit and Loss Account in the year in which the period ends.

However, the recoupable short workings should be carried forward and they are shown in the Balance Sheet as a Current Asset.

The relationship between Minimum rent, Actual Royalty and Royalty payable are in below : Minimum rent = Actual Royalty + Short workings.

(b) Where the actual royalty is more than the minimum rent :

(i) Royalties (payable) Account Dr.

To Landlord Account

[Actual royalties for the period]

(ii) Landlord Account Dr.

To Short workings Account

(Short workings, if any, recouped)

Landlord Account Dr.

To Bank Account

To Income Tax Payable Account

(iii) Profit & Loss Account Dr.

To Short workings Account

(Short workings, which can not be recouped)

(iv) Manufacturing / Profit & Loss Account Dr.

To Royalties (payable) Account

Important Points to note :

1. When the royalty agreement does not contain a clause for minimum rent, the question of short workings andits recoupment does not arise.
2. The landlord is always entitled to get either the minimum rent or the actual royalty whichever is higher subjectto any adjustment for short workings recouped.

Illustration 1.

The Bihar Coal Co. Ltd. holds a lease of coal mines for a period of twelve years, commencing from 1st April 2006.According to the lease, the company is to pay ` 7.50 as royalty per ton with a minimum rent of ` 150,000 per year.Short workings can, however, be recovered out of the royalty in excess of the minimum rent of the next two yearsonly. For the year of a strike the minimum rent is to be reduced to 60%. The output in tons for the 6 years ending31st March, 2012 is as under :

2006-07 :10,000; 2007-08 :12,000; 2008-09:25,000; 2009-10: 20,000; 2010-11: 50,000; and 2011-12: 15,000 (strike).

Write up the necessary Ledger Accounts in the books of Bihar Coal Co. Ltd.

In the books of Bihar Coal Co. Ltd.

Statement showing Royalty Payable

									Fig in (`)
Year	Output (Tons)	Actual Royalties	Min. Rent	ExcessShort Workings	Shortworkings				Amount
					Occurred	Recouped	Written offor lapsed	C/F	Payable
2006-07	10,000	75,000	150,000	0	75,000	0	0	75,000	150,000
2007-08	12,000	90,000	150,000	0	60,000	0	0	135,000	150,000
2008-09	25,000	187,500	150,000	37,500	0	37,500	37,500	60,000	150,000

2009-10	20,000	150,000	150,000	0	0	0	60,000	0	150,000
2010-11	50,000	375,000	150,000	225,000	0	0	0	0	375,000
2011-12	15,000	112,500	90,000	22,500	0	0	0	0	112,500

Royalties Account

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
31.03.07	To Landlord A/c	75,000	31.03.07	By Profit & Loss A/c	75,000
31.03.08	To Landlord A/c	90,000	31.03.08	By Profit & Loss A/c	90,000
31.03.09	To Landlord A/c	187,500	31.03.09	By Profit & Loss A/c	187,500
31.03.10	To Landlord A/c	150,000	31.03.10	By Profit & Loss A/c	150,000
31.03.11	To Landlord A/c	375,000	31.03.11	By Profit & Loss A/c	375,000
31.03.12	To Landlord A/c	112,500	31.03.12	By Profit & Loss A/c	112,500

Landlord Account

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
31.03.07	To Bank A/c	150,000	31.03.07	By Royalties A/c By Short workings A/c	75,000 75,000
		150,000			150,000
31.03.08	To Bank A/c	150,000	31.03.08	By Royalties A/c By Short workings A/c	90,000 60,000
		150,000			150,000
31.03.09	To Bank A/c To Short workings A/c	150,000 37,500	31.03.09	By Royalties A/c	187,500
		187,500			187,500
31.03.10	To Bank A/c	150,000	31.03.10	By Royalties A/c	150,000
		150,000			150,000
31.03.11	To Bank A/c	375,000	31.03.11	By Royalties A/c	375,000
		375,000			375,000
31.03.12	To Bank A/c	112,500	31.03.12	By Royalties A/c	112,500
		112,500			112,500

Short workings Account

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
31.03.07	To Landlord A/c	75,000	31.03.07	By Balance c/d	75,000
		75,000			75,000
1.4.07	To Balance b/d	75,000	31.03.08	By Balance c/d	135,000
31.03.08	To Landlord A/c	60,000			
		135,000			135,000
1.4.08	To Balance b/d	135,000	31.03.09	By Landlord A/c By Profit & Loss A/cBy Balance c/d	37,500 37,500 60,000
		135,000			135,000
1.4.09	To Balance b/d	60,000	31.03.10	By Profit & Loss A/c	60,000
		60,000			60,000

A. Ltd. obtain from B.S. Ltd. a lease of some coal-bearing land, the terms being a royalty of ` 15 per ton of coal raised subject to a minimum rent of ` 75,000 p.a. with a right of recoupment of short-working over the first fouryears of the lease. From the following details, show (i) Short-working Account, (ii) Royalty Account and (iii) B.S. Ltd. Account in the books of A. Ltd.

Year	Sales (Tons) `	Closing Stock (Tons) `
2009	2,000	300
2010	3,500	400
2011	4,800	600
2012	5,600	500
2013	8,000	800

Solution:

Workings:

[Coal raised i.e., Production = Sales + Closing Stock – Opening Stock.]

Year	Sales	+ Closing Stock	-	Opening Stock	=	Net Production
2009	2,000	+ 300	-	Nil	=	2,300
2010	3,500	+ 400	-	300	=	3,600
2011	4,800	+ 600	-	400	=	5,000
2012	5,600	+ 500	-	600	=	5,500
2013	8,000	+ 800	-	500	=	8,300

In the books of A. Ltd.

Memorandum Royalty Statement

Year	Quantity	Rate `	Royalty `	Minimum Rent `	Short working `	Recoupment `	Short working carried forward `	Short working Transferred to P&L A/c or lapsed `	Paymentto Landlord `
2009	2,300	15	34,500	75,000	40,500	---	40,500	---	75,000
2010	3,600	15	54,000	75,000	21,000	---	61,500	---	75,000
2011	5,000	15	75,000	75,000	---	---	61,500	---	75,000
2012	5,500	15	82,500	75,000	---	7,500	---	54,000	75,000
2013	8,300	15	1,24,500	75,000	---	---	---	---	1,24,500

B. S. Ltd. (Landlord) Account

Date	Particulars	Amount `	Date	Particulars	Amount `
2009	To Bank A/c	75,000	2009	By Royalty A/c	34,500
				" Short-working A/c	40,500
		75,000			75,000
2010	To Bank A/c	75,000	2010	By Royalty A/c	54,000
				" Short-working A/c	21,000
		75,000			75,000
2011	To Bank A/c	75,000	2011	By Royalty A/c	75,000
		75,000			75,000
2012	To Bank A/c	75,000	2012	By Royalty A/c	82,500
	To Short-Working A/c	7,500			
		82,500			82,500
2013	To Bank A/c	1,24,500	2013	By Royalty A/c	1,24,500
		1,24,500			1,24,500

Short-Working Account

Date	Particulars	Amount `	Date	Particulars	Amount `
2009	To B. S. Ltd. A/c (Landlord)	40,500	2009	By Balance c/d	40,500
		40,500			40,500
2010	To Balance b/d	40,500	2010	By Balance c/d	61,500
		21,000			

	" B. S. Ltd. A/c (Landlord)	61,500			61,500
2011	To Balance b/d	61,500	2011	By Balance c/d	61,500
		61,500			61,500
2012	To Balance b/d	61,500	2012	By B. S Ltd. (Landlord) A/c"	7,500
				Profit and Loss A/c	54,000
		61,500			61,500

Royalty Account

Date	Particulars	Amount `	Date	Particulars	Amount `
2009	To B. S. Ltd. A/c	34,500	2009	By Profit & Loss A/c	34,500
2010	To B. S. Ltd. A/c	54,000	2010	By Profit & Loss A/c	54,000
2011	To B. S. Ltd. A/c	75,000	2011	By Profit & Loss A/c	75,000
2012	To B. S. Ltd. A/c	82,500	2012	By Profit & Loss A/c	82,500
2013	To B. S. Ltd. A/c	1,24,500	2013	By Profit & Loss A/c	1,24,500

Accounting Entries in the Books of the Landlord / Lessor

1. Where a minimum rent exists with right to recoup short workings

(a) Where the actual royalty is less than the minimum rent :

(i) Lessee Account Dr. [Minimum rent]
To Royalty Receivable Account [Actual Royalties for the period]
To Royalty Suspense Account/ [Short fall in Royalties]
Or Shortworkings Allowable A/c

(ii) Bank Account Dr. [Net amount paid]
Tax Deducted at source Dr. [Tax deducted at source][Minimum rent]
To Lessee Account

(iii) Royalties Receivable Account Dr.
To Profit & Loss Account [Transfer]

Where the actual royalty is more than the minimum rent :

(ii)Royalty Suspense Account/ Dr.
Or Short workings Allowable A/c
To Lessee Account
[Recoupment of Short workings, if any]

(iii) Bank Account Dr. [Net amount paid]

Tax Deducted at source Dr. [Tax deducted at source]

To Lessee Account

(iv) Royalties (Receivable) Account Dr.

To Profit & Loss Account[Transfer]

v) Royalty Suspense Account/ Dr.

Or Short workings Allowable A/c

To Profit and Loss Account

[Short workings, which can not be recouped]

Illustration 3.

For the same figures as given in illustration 1, prepare necessary accounts in the books of Landlord.

Solution :

In the books of Landlord

Dr. **Royalty Receivable Account**

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
31.03.07	To Profit & Loss A/c	75,000	31.03.07	By Bihar Coal Co.Ltd	75,000
31.03.08	To Profit & Loss A/c	90,000	31.03.08	By Bihar Coal Co. Ltd	90,000
31.03.09	To Profit & Loss A/c	1,87,500	31.03.09	By Bihar Coal Co. Ltd	1,87,500
31.03.10	To Profit & Loss A/c	1,50,000	31.03.10	By Bihar Coal Co. Ltd	1,50,000
31.03.11	To Profit & Loss A/c	3,75,000	31.03.11	By Bihar Coal Co. Ltd	3,75,000
31.03.12	To Profit & Loss A/c	1,12,500	31.03.12	By Bihar Coal Co. Ltd	1,12,500

Dr. **Bihar Coal Co. Ltd. (Lessee) Account**

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
31.03.07	To Royalties Receivable A/c	75,000	31.03.07	By Bank A/c	150,000
	To Shortworkings Susp.A/c	75,000			
		150,000			150,000
31.03.08	To Royalties Receivable A/c	90,000	31.03.08	By Bank A/c	150,000
	To Shortworkings Susp.A/c	60,000			

		150,000			150,000
31.03.09	To Royalties Receivable A/c	187,500	31.03.09	By Bank A/c By Shortworkings Susp.A/c	150,000 37,500
		1,87,500			1,87,500
31.03.10	To Royalties Receivable A/c	150,000	31.03.10	By Bank A/c	150,000
		150,000			150,000
31.03.11	To Royalties Receivable A/c	375,000	31.03.11	By Bank A/c	375,000
		375,000			375,000
31.03.12	To Royalties Receivable A/c	112,500	31.03.12	By Bank A/c	112,500
		112,500			112,500

Shortworkings Suspense Account

Date	Particulars	Amount (`)	Date	Particulars	Amount (`)
31.03.07	To Balance c/d	75,000	31.03.07	By Bihar Coal Co. Ltd	75,000
			1.4.07	By Balance b/d	75,000
31.03.08	To Balance c/d	1,35,000	31.03.08	By Bihar Coal Co. Ltd	60,000
		1,35,000			1,35,000
31.03.09	To Bihar Coal Co. LtdTo Profit & Loss A/c To Balance c/d	37,000 37,500 60,000	1.4.08	By Balance b/d	135,000
		1,35,500			1,35,500
31.03.10	To Profit & Loss A/c	60,000	1.04.09	By Balance b/d	60,000
		60,000			60,000

Illustration 5.

A fire occurred in the office premises of lessee in the evening of 31.3.2012 destroying most of the books and records. From the documents saved, the following information is gathered:

Short-working recovered :

2009-10 ` 4,000 (towards short-workings which arose in 2006-07)

2010-11 ` 8,000 (including ` 1,000 for short-working 2007-08)

2011-12 ` 2,000

Short-working lapsed :

2008-09 ` 3,000

2009-10 ` 3,600

2011-12 ` 2,000

A sum of ` 50,000 was paid to the landlord in 2008-09. The agreement of Royalty contains a clause of MinimumRent payable for fixed amount and recoupment of short-workings within 3 years following the year in which Short-workings arise.

Information as regards payments to landlord subsequent to the year 2008-09 is not readily available.

Show the Short – working Account and the Royalty Account in the books of lessee.

Solution:

Working Notes:

Analysis of payments

Year	Minimum Rent `	Royalty `	Actual Payment `	Shortworking `			
				Occurred	Recouped	Lapsed	Carried Forward
2007-08	-	-	-	-	-	-	11,600
2008-09	50,000	39,000	50,000	11,000	-	3,000	19,600**(C)**
2009-10	50,000	54,000	50,000	-	4,000	3,600	12,000**(B)**
2010-11	50,000	58,000	50,000	-	8,000	-	4,000**(A)**
2011-12	50,000	52,000	50,000	-	2,000	2,000	-

Analysis of Royalty Payable:

		`	`
Royalty in 2008-09	Minimum Rent – Shortworking	50,000 - 11,000	39,000
Royalty in 2009-10	Minimum Rent + Recoupment	50,000 + 4,000	54,000
Royalty in 2010-11	Minimum Rent + Recoupment	50,000 + 8,000	58,000
Royalty in 2011-12	Minimum Rent + Recoupment	50,000 + 2,000	52,000