

CHAPTER - 1

FINANCIAL STATEMENT - I

Q1 :

From the following balances taken from the books of Simmi and Vimmi Ltd. for the year ending March 31, 2003, calculate the gross profit.

	Rs
Closing stock	2,50,000
Net sales during the year	40,00,000
Net purchases during the year	15,00,000
Opening stock	15,00,000
Direct expenses	80,000

Answer :

Trading Account as on March 31, 2003

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	15,00,000	Net Sales	40,00,000
Net Purchases	15,00,000	Closing Stock	2,50,000
Direct Expenses	80,000		
Gross Profit	11,70,000		
	42,50,000		42,50,000

Q2 :

From the following balances extracted from the books of M/s Ahuja and Nanda. Calculate the amount of:

- (a) Cost of goods available for sale
- (b) Cost of goods sold during the year
- (c) Gross Profit

	Rs
Opening stock	25,000
Credit purchases	7,50,000
Cash purchases	3,00,000
Credit sales	12,00,000
Cash sales	4,00,000
Wages	1,00,000
Salaries	1,40,000
Closing stock	30,000
Sales return	50,000
Purchases return	10,000

Answer :

(a) Cost of Goods Sold Available for Sales

Or

$$\begin{aligned}
 \text{Cost of Goods Manufactured} &= \text{Opening Stock} + \text{Net Purchases} + \text{Wages} \\
 &= 25,000 + 10,40,000 + 1,00,000 \\
 &= \text{Rs } 11,65,000
 \end{aligned}$$

$$\begin{aligned}
 \text{(b) Cost of Goods Sold} &= \text{Opening Stock} + \text{Net Purchases} + \text{Wages} - \text{Closing Stock} \\
 &= 25,000 + 10,40,000 + 1,00,000 - 30,000 \\
 &= \text{Rs } 11,35,000
 \end{aligned}$$

Or

$$\begin{aligned}
 \text{Cost of Goods Sold} &= \text{Net Sales} - \text{Gross Profit} \\
 &= 15,50,000 - 4,15,000 \\
 &= \text{Rs } 11,35,000
 \end{aligned}$$

(c)

Trading Account

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	25,000	Sales	
Purchases		<i>Add:</i> Credit Sales 12,00,000	
<i>Add:</i> Credit Purchases 7,50,000		<i>Add:</i> Cash Sales 4,00,000	
<i>Add:</i> Cash Purchases 3,00,000			16,00,000
	10,50,000	<i>Less:</i> Sales Return (50,000)	15,50,000
<i>Less:</i> Purchases Return (10,000)	10,40,000		
Wages	1,00,000	Closing Stock	30,000
Gross Profit	4,15,000		
	15,80,000		15,80,000

Gross Profit Rs 4,15,000

Q3 :

Calculate the amount of gross profit and operating profit on the basis of the following balances extracted from the books of M/s Rajiv and Sons for the year ended March 31, 2005.

	Rs
Opening stock	50,000
Net sales	11,00,000
Net purchases	6,00,000
Direct expenses	60,000
Administration expenses	45,000
Selling and distribution expenses	65,000
Loss due to fire	20,000
Closing stock	70,000

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	50,000	Net Sales	11,00,000
Net Purchases	6,00,000	Closing Stock	70,000
Direct Expenses	60,000		
Gross Profit	4,60,000		
	11,70,000		11,70,000

Operating Profit = Sales - (Opening Stock + Net Purchases + Direct Expenses + Administration Expenses + Selling and Distribution Expenses) + Closing Stock
= 11,00,000 - (50,000 + 6,00,000 + 60,000 + 45,000 + 65,000) + 70,000
= Rs 3,50,000

Q4 :

Operating profit earned by M/s Arora and Sachdeva in 2005-06 was Rs 17,00,000. Its non-operating incomes were Rs 1,50,000 and non-operating expenses were Rs 3,75,000. Calculate the amount of net profit earned by the firm.

Answer :

Net Profit = Operating Profit + Non-operating Income - Non-operating Expenses
= 17,00,000 + 1,50,000 - 3,75,000
= Rs 14,75,000

Net profit earned by M/S Arora and Sachdeva in 2005-06 is Rs 14,75,000.

Q5 :

The following are the extracts from the trial balance of M/s Bhola and Sons as on March 31, 2005

Account title	Debit Rs	Credit Rs
Opening Stock	2,00,000	
Purchases	8,10,000	
Sales		10,10,000
	10,10,000	10,10,000

(Only relevant items)

Closing Stock as on date was valued at Rs 3,00,000.

You are required to record the necessary journal entries and show how the above items will appear in the trading and profit and loss account and balance sheet of M/s Bhola and Sons.

Answer :

Books of M/s Bhola and Sons

Journal

Date	Particulars	L.F.	Debit Amount Rs	Credit Amount Rs
2006 Mar.31	Trading A/c Dr. To Opening Stock A/c To Purchases A/c (Balances from Purchases Account and Stock Account transferred to Trading Account)		10,10,000	2,00,000 8,10,000

Mar.31	Sales A/c	Dr.	10,10,000	
	Closing Stock A/c		3,00,000	
	To Trading A/c			13,10,000
	(Balance from sales and closing stock transferred to Trading Account)			
Mar.31	Trading A/c	Dr.	3,00,000	
	To Profit and Loss (Gross Profit) A/c			3,00,000
	(Balance of Trading Account (gross profit) transferred to Profit and Loss Account)			

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	2,00,000	Sales	10,10,000
Purchases	8,10,000	Closing Stock	3,00,000
Profit and Loss A/c - Gross Profit	3,00,000		
	13,10,000		13,10,000

Balance Sheet as on March 31, 2005

Liabilities	Amount Rs	Assets	Amount Rs
		Closing Stock	3,00,000

Q6 :

Prepare trading and profit and loss account and balance sheet, as on March 31, 2005 :

Account Title	Amount Rs	Account Title	Amount Rs
Machinery	27,000	Capital	60,000
Sundry debtors	21,600	Bills payable	2,800
Drawings	2,700	Sundry creditors	1,400
Purchases	58,500	Sales	73,500
Wages	15,000		
Sundry expenses	600		
Rent and taxes	1,350		
Carriage inwards	450		
Bank	4,500		
Openings stock	6,000		

Closing stock, as on March 31, 2005 Rs 22,400

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	6,000	Sales	73,500
Purchases	58,500	Closing Stock	22,400
Wages	15,000		
Carriage Inwards	450		
Profit and Loss (Gross Profit)	15,950		
	95,900		95,900

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount	Particulars	Amount
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	Rs		Rs
Sundry Expenses	600	Trading (Gross Profit)	15,950
Rent and Taxes	1,350		
Net Profit	14,000		
	15,950		15,950

Balance Sheet as on March 31, 2005

Liabilities	Amount Rs	Assets	Amount Rs
Capital	60,000	<u>Fixed Assets</u>	
Add: Net Profit	14,000	Machinery	27,000
	74,000		
Less: Drawings	2,700	<u>Current Assets</u>	
		Bank	4,500
Sundry Creditors	1,400	Closing Stock	22,400
Bills Payable	2,800	Sundry Debtors	21,600
	75,500		75,500

Q7 :

The following trial balance is extracted from the books of M/s Ram on March 31, 2005. You are required to prepare trading and profit and loss account and the balance sheet as on date:

Account title	Amount Rs	Account title	Amount Rs
Debtors	12,000	Apprenticeship premium	5,000
Purchases	50,000	Loan	10,000
Coal, gas and water	6,000	Bank overdraft	1,000

Factory wages	11,000	Sales	80,000
Salaries	9,000	Creditors	13,000
Rent	4,000	Capital	20,000
Discount	3,000		
Advertisement	500		
Drawings	1,000		
Loan	6,000		
Petty cash	500		
Sales return	1,000		
Machinery	5,000		
Land and building	10,000		
Income tax	100		
Furniture	9,900		

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Purchases	50,000	Sales	80,000
Coal, Gas and Water	6,000	Less: Sales Return	1,000
Factory Wages	11,000		
Profit and Loss (Gross Profit)	12,000		
	79,000		79,000

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Salaries	9,000	Trading (Gross Profit)	12,000

Rent	4,000	Apprenticeship Premium	5,000
Discount	3,000		
Advertisement	500		
Net Profit	500		
	17,000		17,000

Balance Sheet as on March 31, 2005

Liabilities		Amount Rs	Assets		Amount Rs
Capital	20,000		Machinery		5,000
Add: Profit and Loss (Net Profit)	500		Land and Building		10,000
	20,500		Furniture		9,900
Less: Drawings	(1,000)		Loan (Given)		6,000
Less: Income Tax	(100)	19,400	Debtors		12,000
			Petty Cash		500
Loan (Taken)		10,000			
Creditors		13,000			
Bank Overdraft		1,000			

Q8 :

The following is the trial balance of Manju Chawla on March 31, 2005. You are required to prepare trading and profit and loss account and a balance sheet as on date:

Account title	Debit Amount Rs	Credit Amount Rs
Opening stock	10,000	
Purchases and sales	40,000	80,000
Returns	200	600
Productive wages	6,000	
Dock and Clearing charges	4,000	
Donation and charity	600	

Delivery van expenses	6,000	
Lighting	500	
Sales tax collected		1,000
Bad debts 600		
Misc. incomes		6,000
Rent from tenants		2,000
Royalty	4,000	
Capital		40,000
Drawings	2,000	
Debtors and Creditors	6,000	7,000
Cash	3,000	
Investment	6,000	
Patents	4,000	
Land and Machinery	43,000	

Closing stock Rs 2,000.

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	10,000	Sales	80,000
Purchases	40,000	Less: Sales Returns	(200)
Less: Purchases Returns	(600)		
Productive Wages	6,000	Closing Stock	2,000
Dock and Clearing Charges	4,000		
Royalty	4,000		
Profit and Loss (Gross Profit)	18,400		
	81,800		81,800

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Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Donation and Charity	600	Trading (Gross Profit)	18,400
Delivery Van Expenses	6,000	Misc. Incomes	6,000
Lighting	500	Rent from Tenants	2,000
Bad Debts	600		
Net Profit	18,700		
	26,400		26,400

Note: As per the solution, net profit is Rs 18,700; however, according to the answer given in the book, it is Rs 18,400.

Balance Sheet as on March 31, 2005

Liabilities	Amount Rs	Assets
Capital	40,000	Patents
<i>Add:</i> Profit and Loss (Net Profit)	18,700	Land and Machinery
	58,700	Investment
<i>Less:</i> Drawings	(2,000)	Debtors
		Cash
Sales Tax Collected		

Q9 :

The following is the trial balance of Mr. Deepak as on March 31, 2005. You are required to prepare trading account, profit and loss account and a balance sheet as on date:

Account title	Debit Amount	Account title	Credit Amount
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	Rs		Rs
Drawings	36,000	Capital	2,50,000
Insurance	3,000	Bills payable	3,600
General expenses	29,000	Creditors	50,000
Rent and taxes	14,400	Discount received	10,400
Lighting (factory)	2,800	Purchases return	8,000
Travelling expenses	7,400	Sales	4,40,000
Cash in hand	12,600		
Bills receivable	5,000		
Sundry debtors	1,04,000		
Furniture	16,000		
Plant and Machinery	1,80,000		
Opening stock	40,000		
Purchases	1,60,000		
Sales return	6,000		
Carriage inwards	7,200		
Carriage outwards	1,600		
Wages	84,000		
Salaries	53,000		

Closing stock Rs 35,000.

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	40,000	Sales	4,40,000
Purchases	1,60,000	Less: Sales Return	6,000
Less: Purchases Return	(8,000)	Closing Stock	35,000
	1,52,000		

Lighting (Factory)	2,800		
Carriage Inwards	7,200		
Wages	84,000		
Profit and Loss (Gross Profit)	1,83,000		
	4,69,000		4,69,000

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Insurance	3,000	Trading (Gross Profit)	1,83,000
General Expenses	29,000	Discount Received	10,400
Rent and Taxes	14,400		
Travelling Expenses	7,400		
Carriage Outwards	1,600		
Salaries	53,000		
Net Profit	85,000		
	1,93,400		1,93,400

Balance Sheet as on March 31, 2005

Liabilities	Amount Rs	Assets	Amount Rs
Capital	2,50,000	Plant and Machinery	1,80,000
Add: Net Profit	85,000		

Q10 :

Prepare trading and profit and loss account and balance sheet from the following particulars as on March 31, 2005.

Account Title	Debit Amount Rs	Credit Amount Rs
Purchases and Sales	3,52,000	5,60,000
Return inwards and Return outwards	9,600	12,000
Carriage inwards	7,000	
Carriage outwards	3,360	
Fuel and power	24,800	
Opening stock	57,600	
Bad debts	9,950	
Debtors and Creditors	1,31,200	48,000
Capital		3,48,000
Investment	32,000	
Interest on investment		3,200
Loan		16,000
Repairs	2,400	
General expenses	17,000	
Wages and salaries	28,800	
Land and buildings	2,88,000	
Cash in hand	32,000	
Miscellaneous receipts		160
Sales tax collected		8,350

Closing stock Rs 30,000.

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	57,600	Sales	5,60,000
Purchases	3,52,000	Less: Return Inwards	(9,600)
			<u>5,50,400</u>

Less: Return Outwards	(12,000)	3,40,000	Closing Stock	30,000
Carriage Inwards		7,000		
Fuel and Power		24,800		
Wages and Salaries		28,800		
Profit and Loss (Gross Profit)		1,22,200		
		5,80,400		5,80,400

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Carriage Outwards	3,360	Trading (Gross Profit)	1,22,200
Bad Debts	9,950	Interest on Investment	3,200
Repairs	2,400	Miscellaneous Receipts	160
General Expenses	17,000		
Net Profit	92,850		
	1,25,560		1,25,560

Balance Sheet as on March 31,2005

Liabilities	Amount Rs	Assets	Amount Rs
Capital	3,48,000	Land and Building	2,88,000
Add: Net Profit	92,850	Investment	32,000
	4,40,850	Debtors	1,31,200
Loan	16,000	Closing Stock	30,000
Creditors			

Q11 :

From the following trial balance of Mr. A. Lal, prepare trading, profit and loss account and balance sheet as on March 31, 2005.

Account Title	Debit Amount Rs	Credit Amount Rs
Stock as on April 01, 2005	16,000	
Purchases and Sales	67,600	1,12,000
Returns inwards and outwards	4,600	3,200
Carriage inwards	1,400	
General expenses	2,400	
Bad debts	600	
Discount received		1,400
Bank over draft		10,000
Interest on bank overdraft	600	
Commission received		1,800
Insurance and taxes	4,000	
Scooter expenses	200	
Salaries	8,800	
Cash in hand	4,000	
Scooter	8,000	
Furniture	5,200	
Building	65,000	
Debtors and Creditors	6,000	16,000
Capital		50,000

Closing stock Rs 15,000.

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
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Opening Stock		16,000	Sales	1,12,000	
Purchases	67,600		Less: Sales Return Inwards	(4,600)	1,07,400
Less: Return Outwards	(3,200)	64,400	Closing Stock		15,000
Carriage Inwards		1,400			
Profit and Loss (Gross Profit)		40,600			
		1,22,400			1,22,400

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
General Expenses	2,400	Trading (Gross Profit)	40,600
Bad Debts	600	Discount Received	1,400
Interest on Bank Overdraft	600	Commission Received	1,800
Insurance and Taxes	4,000		
Scooter Expenses	200		
Salaries	8,800		
Net Profit	27,200		
	43,800		43,800

Balance Sheet as on March 31, 2005

Liabilities	Amount Rs	Assets	Amount Rs
Capital	50,000	Building	65,000
Add: Net Profit	27,200	Furniture	5,200
		Scooter	8,000
Creditors	16,000	Debtors	6,000
Bank Overdraft	10,000	Closing Stock	15,000

		Cash in Hand

Q12 :

Prepare trading and profit and loss account and balance sheet of M/s Royal Traders from the following balances as on March 31, 2005.

Debit balances	Amount Rs	Credit balances	Amount Rs
Stock	20,000	Sales	2,45,000
Cash	5,000	Creditors	10,000
Bank	10,000	Bills payable	4,000
Carriage on purchases	1,500	Capital	2,00,000
Purchases	1,90,000		
Drawings	9,000		
Wages	55,000		
Machinery	1,00,000		
Debtors	27,000		
Postage	300		
Sundry expenses	1,700		
Rent	4,500		
Furniture	35,000		

Closing stock Rs 8,000

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	20,000	Sales	2,45,000
Purchases	1,90,000	Closing Stock	8,000
Carriage on Purchases	1,500	Profit and Loss (Gross Loss)	13,500

Wages	55,000		
	2,66,500		2,66,500

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Trading (Gross Loss)	13,500		
Postage	300		
Sundry Expenses	1,700		
Rent	4,500	Net Loss	20,000
	20,000		20,000

Balance Sheet of M/s Royal Traders as on March 31, 2005

Liabilities	Amount Rs	Assets	Amount Rs
Capital 2,00,000		Machinery	1,00,000
Less: Net Loss (20,000)		Furniture	35,000
Less: Drawings (9,000)	1,71,000	Debtors	27,000
		Closing Stock	8,000
Creditors	10,000	Bank	10,000
Bills Payable	4,000	Cash	5,000
	1,85,000		1,85,000

Q13 :

Prepare trading and profit and loss account from the following particulars of M/s Neema Traders as on March 31, 2005.

Account Title	Debit Account Rs	Account Title	Credit Amount Rs
Buildings	23,000	Sales	1,80,000
Plant	16,930	Loan	8,000
Carriage inwards	1,000	Bills payable	2,520
Wages	3,300	Bank overdraft	4,720
Purchases	1,64,000	Creditors	8,000
Sales return	1,820	Capital	2,36,000
Opening stock	9,000	Purchases return	1,910
Machinery	2,10,940		
Insurance	1,610		
Interest	1,100		
Bad debts	250		
Postage	300		
Discount	1,000		
Salaries	3,000		
Debtors	3,900		

Stock on March 31, 2005 Rs 16,000.

Answer :

Trading Account as on March 31, 2005

Dr.

Cr.

Liabilities	Amount Rs	Assets	Amount Rs
Opening Stock	9,000	Sales	1,80,000
Purchases	1,64,000	<i>Less: Sales Return</i>	(1,820)
<i>Less: Purchases Return</i>	(1,910)	Closing Stock	16,000
	1,62,090		

Carriage Inwards	1,000		
Wages	3,300		
Profit and Loss (Gross Profit)	18,790		
	1,94,180		1,94,180

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Insurance	1,610	Trading (Gross Profit)	18,790
Interest	1,100		
Bad Debts	250		
Postage	300		
Discount	1,000		
Salaries	3,000		
Net Profit	11,530		
	18,790		18,790

Balance Sheet as on March 31, 2005

Liabilities	Amount Rs	Assets	Amount Rs
Capital	2,36,000	Building	23,000
Add: Net Profit	11,530	Plant	16,930
		Machinery	2,10,940
Loan	8,000	Debtors	

Q14 :

From the following balances of M/s Nilu Sarees as on March 31, 2005. Prepare trading and profit and loss account and balance sheet as on date.

Account Title	Debit Account Rs	Account Title	Credit Amount Rs
Opening stock	10,000	Sales	2,28,000
Purchases	78,000	Capital	70,000
Carriage inwards	2,500	Interest	7,000
Salaries	30,000	Commission	8,000
Commission	10,000	Creditors	28,000
Wages	11,000	Bills payable	2,370
Rent and taxes	2,800		
Repairs	5,000		
Telephone expenses	1,400		
Legal charges	1,500		
Sundry expenses	2,500		
cash in hand	12,000		
Debtors	30,000		
Machinery	60,000		
Investments	90,000		
Drawings	18,000		

Closing stock, as on March 31, 2005 Rs 22,000.

Answer :

Trading Account of M/s Nilu Sarees as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	10,000	Sales	2,28,000
Purchases	78,000	Closing Stock	22,000
Carriage Inwards	2,500		
Wages	11,000		
Profit and Loss (Gross Profit)	1,48,500		

	2,50,000		2,50,000

Note: As per solution, the Gross profit is Rs 1,48,500; however, the answer given in the book is Rs 1,56,500.

Profit and Loss Account as on March 31, 2005

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Salaries	30,000	Trading (Gross Profit)	1,48,500
Commission	10,000	Interest	7,000
Rent and Taxes	2,800	Commission	8,000
Repairs	5,000		
Telephone Expenses	1,400		
Legal Charges	1,500		
Sundry Expenses	2,500		
Net Profit	1,10,300		
	1,63,500		1,63,500

Balance Sheet as on March 31, 2005

Liabilities	Amount Rs	Assets	Amount Rs
Capital	70,000	Machinery	60,000
<i>Add: Net Profit</i>	1,10,300	Investments	90,000
	1,80,300	Debtors	30,000
<i>Less: Drawings</i>	(18,000)	Closing Stock	22,000
	1,62,300	Cash in Hand	12,000
Creditors	28,000		
Bills Payable	2,370		
Suspense	21,330		

Q15 :

Prepare trading and profit and loss account of M/s Sports Equipments for the year ended March 31, 2006 and balance sheet as on that date:

Account Title	Debit Amount Rs	Credit Amount Rs
Opening stock	50,000	
Purchases and sales	3,50,000	4,21,000
Sales returns	5,000	
Capital		3,00,000
Commission		4,000
Creditors		1,00,000
Bank overdraft		28,000
Cash in hand	32,000	
Furniture	1,28,000	
Debtors	1,40,000	
Plants	60,000	
Carriage on purchases	12,000	
Wages	8,000	
Rent	15,000	
Bad debts	7,000	
Drawings	24,000	
Stationery	6,000	
Travelling expenses	2,000	
Insurance	7,000	
Discount	5,000	
Office expenses	2,000	

Closing stock as on March 31, 2006 Rs 2,500

Answer :

Trading Account as on March 31, 2006

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Opening Stock	50,000	Sales	4,21,000
Purchases	3,50,000	Less: Sales Return	5,000
Carriage on Purchases	12,000	Closing Stock	2,500
Wages	8,000	Profit and Loss (Gross Loss)	1,500
	4,20,000		4,20,000

Profit and Loss Account as on March 31, 2006

Dr.

Cr.

Particulars	Amount Rs	Particulars	Amount Rs
Trading (Gross Loss)	1,500	Commission	4,000
Rent	15,000	Net Loss	41,500
Bad Debts	7,000		
Stationery	6,000		
Travelling Expenses	2,000		
Insurance	7,000		
Discount	5,000		
Office Expenses	2,000		
	45,500		45,500

Balance Sheet as on March 31, 2006

Liabilities	Amount Rs	Assets	Amount Rs
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Capital	3,00,000		Plants	60,000
Less: Net Loss	(41,500)		Furniture	1,28,000
Less: Drawings	(24,000)	2,34,500	Debtors	1,40,000
			Closing Stock	2,500
Creditors		1,00,000	Cash in Hand	32,000
Bank Overdraft		28,000		
		3,62,500		

Short answers : Solutions of Questions on Page Number : 364

Q1 :

What are the objectives of preparing financial statements?

Answer :

The following are the objectives of preparing financial statements.

1. To ascertain profit earned or loss incurred by a business during an accounting period. This is estimated by preparing Trading and Profit and Loss Account.
2. To ascertain the true financial position of a business. This is reflected by the Balance Sheet.
3. To enable comparison of current year's performance with that of the previous year's, i.e., intra-firm comparisons. Also, to compare own performance with that of the other firms in the same industry, i.e., inter-firm comparisons.
4. To assess the solvency and credit worthiness of the business
5. To provide various provisions and reserves to meet unforeseen future conditions and to toughen the financial position of the business
6. To provide vital information to facilitate various users of accounting information in decision making process.

Q2 :

What is the purpose of preparing trading and profit and loss account?

Answer :

The purposes of preparing Trading Account are:

1. To calculate gross profit earned or gross loss incurred during an accounting period
2. To estimate the cost of goods sold
3. To record direct expenses (i.e., expenses incurred on the purchases and manufacturing of goods)
4. To measure the adequacy and reasonability of direct expenses incurred by comparing purchases with direct expenses incurred
5. To compare the realised efficiency and performance with the desired or proposed targets

The purposes of preparing Profit and Loss Account are:

1. To calculate net profit or net loss
2. To ascertain net profit ratio and to compare this year's net profit ratio with that of the desired and proposed target in order to assess the efficiency and effectiveness

3. To measure the adequacy and reasonability of indirect expenses incurred by ascertaining ratio between indirect expenses and net profit
4. To compare current year's actual performance with desired and planned performance
5. To provide various provisions and reserves to meet unforeseen future conditions and to toughen the financial position of the business

Q3 :

Explain the concept of cost of goods sold?

Answer :

Cost of goods sold (COGS) is the cost of merchandise that is sold to the customers. It includes cost of raw materials purchased, direct expenses incurred, value of opening stock, i.e., the value of the last year's unsold stock and excludes closing stock if any, i.e., the value of current year's unsold stock. The formula to calculate COGS is:

Cost of Goods Sold = Opening Stock + Purchases + Direct Expenses - Closing Stock

Q4 :

What is a balance sheet? What are its characteristics?

Answer :

Balance Sheet is a statement prepared to ascertain values of assets and liabilities of a business on a particular date. It is called Balance Sheet as it contain balances of real and personal accounts, which are **not** closed on a particular date.

Characteristics of Balance Sheet

1. It is a statement of assets and liabilities.
2. The total of Assets side must be equal to Liabilities sides.
3. It is prepared at a particular date.
4. It helps in ascertaining the financial position of the business.

Q5 :

Distinguish between capital and revenue expenditure and state whether the following statements are items of capital or revenue expenditure:

- (a) Expenditure incurred on repairs and whitewashing at the time of purchase of an old building in order to make it usable.
- (b) Expenditure incurred to provide one more exit in a cinema hall in compliance with a government order.
- (c) Registration fees paid at the time of purchase of a building
- (d) Expenditure incurred in the maintenance of a tea garden which will produce tea after four years.
- (e) Depreciation charged on a plant.
- (f) The expenditure incurred in erecting a platform on which a machine will be fixed.
- (g) Advertising expenditure, the benefits of which will last for four years.

Answer :

Basis of Difference	Capital Expenditure	Revenue Expenditure
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Meaning	It is incurred to increase the earning capacity of a business.	It is incurred to maintain the earning capacity of a business.
Purpose	It is incurred to acquire fixed assets to carry out operations.	It is incurred to conduct day to day activities.
Benefits	The benefits of such expenditures can be availed for more than one year.	The benefits of such expenditures can only be availed for one year.
Nature	It is non-recurring by nature.	It is generally recurring in nature.
Shown	Capital expenditure is shown in the assets side of the Balance Sheet.	Revenue expenditure is shown in the debit side of the trading and Profit and Loss Account.

- (a) Capital expenditure
- (b) Revenue expenditure
- (c) Capital expenditure
- (d) Capital expenditure
- (e) Revenue expenditure
- (f) Capital expenditure
- (g) Deferred revenue expenditure

Q6 :

What is an operating profit?

Answer :

Operating profit is a profit earned through normal activities of a business. It is the excess of gross profit over operating expenses. In other words, it is the excess of operating revenue over operating cost. It is also termed as earning before interest and tax (EBIT). It does **not** include incomes and expenses that are **not** related to main course of the business.

It is calculated by following formulae:

Operating Profit = Gross Profit - Operating Expenses

Or,

Operating Profit = Sales - Operating Cost

Operating Profit = Sales - COGS - Operating Expenses

Operating expenses include office and administrative expenses, selling and distribution expenses, discount, bad debts, etc.

Long answers : Solutions of Questions on Page Number : 364

Q1 :

What are financial statements? What information do they provide?

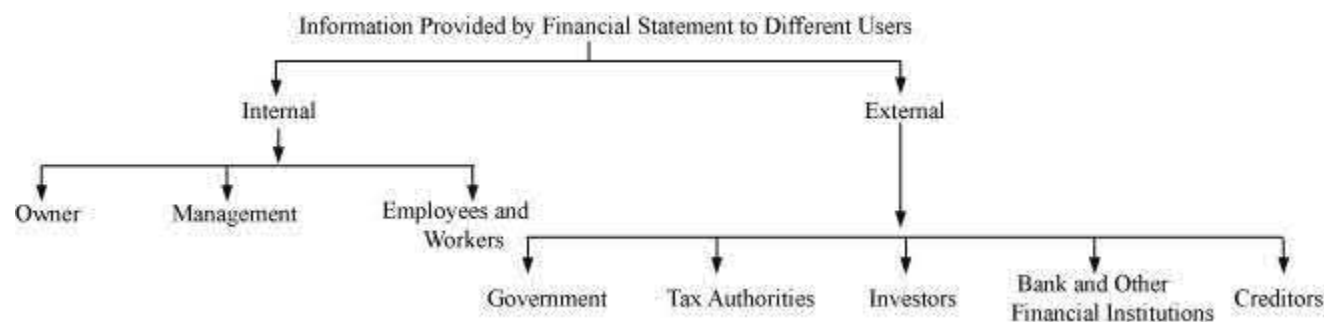
Answer :

Every business firm wants to know its financial position at the end of an accounting period. In order to assess its financial position, profit earned or loss incurred during an accounting period, the book value of its assets and liabilities is to be ascertained. In order to serve this purpose, financial statements are prepared. Financial statements are the statements showing profitability and financial position of a business at the end of the year. It includes:

1. Income statements, viz., Trading and Profit and Loss Account, which represents direct and indirect expenses incurred to generate revenues. On one hand, trading account discloses either gross profit or gross loss, on the other hand, profit and loss account discloses either net profit or net loss.

2. Statement of financial position, viz., Balance Sheet, which enlists the book value of all the assets and liabilities of the firm. Balance Sheet discloses the true financial position, solvency and credit worthiness of the business.

The information provided by the financial statements is in the form of gross profit or gross loss, net profit or net loss and book value of the assets and their liabilities. The value and relevance of the information provided by the financial statements varies from one user of accounting information to another. Various users of accounting information can be explained graphically as below.



1. Internal: Internal users are those persons who are directly related to the business. For example, owners, management, employees, workers, etc.

a. Owners: The information required by owners about profit earned or loss incurred during an accounting period. This information is provided by the financial statements in form of gross (net) profit or gross (net) loss.

b. Management: Financial statements provide vital information to the management for decision making, designing policies and future plans. There are various parameters such as ratio of direct (indirect) expenses to gross (net) profit, by the help of which management can check the adequacy, control and relevance of various expenses incurred and plans and policies implemented.

c. Employees and workers: They expect bonus at the year end, which is directly related to the profit of that particular period. The net profit as disclosed by the profit and loss account forms the basis of this expectation.

2. External: External users are those persons and institutions that are indirectly related to the business. For example, government, tax authorities, investors, etc.

a. Government: Government needs information in order to ascertain various macroeconomic variables, such as national income, GDP, employment opportunities generated, etc.

b. Tax authorities: Tax department is interested in knowing the actual sales, production, turnovers and exports and imports by the business. Tax department levies various taxes, such as income tax, VAT, excise tax, etc. The information disclosed by the financial statements form the basis of estimation of the tax dues of the business.

c. Investors: Financial statements help to know about the earning capacity, scope and potential to grow and to assess financial position of the business. It also helps in knowing various investments made by the business and also investments made by the organisations and individuals in the business. This information helps the investors to assess and determine whether investments by them will be fruitful or not.

d. Bank and other financial institutions: Financial statements provide information to banks and other financial institutions, such as LIC, GIC, etc., about the credit worthiness, solvency and repaying capacity of the business.

e. Creditors: Financial statements provide information to the creditors about the goodwill of the business and its credit worthiness and repaying capacity.

Q2 :

What are closing entries? Give four examples of closing entries.

Answer :

The balances of all nominal accounts are transferred to the Trading and Profit and Loss Account. The entries required for such transfers are termed as closing entries.

The examples of closing entries are given below.

1. Closing entries to transfer the following items to the debit side of trading account from Trial Balance:

Trading A/c Dr.

 To Opening Stock A/c

 To Purchase A/c

 To Wages A/c

 To Carriage A/c

 To All Other Direct Expenses A/c

(Transferred debit balances to Trading Account)

2. Closing entries to transfer the following items to the credit side of trading account from Trial Balance:

Sales A/c Dr.

Closing Stock A/c Dr.

 To Trading A/c

(Transferred credit balances to Trading Account)

3. Closing entries to transfer the following items to the debit side of Profit and Loss Account from Trial Balance:

Profit and Loss A/c Dr.

 To Salaries

 To Rent

 To Bad Debts

 To All in Direct Expenses

(Transferred debit balances to Profit and Loss Account)

4. Closing entries to transfer the following items to the credit side of Profit and Loss Account from Trial Balance:

Commission Received A/c Dr.

Interest Received A/c Dr.

All Other Indirect Income A/c Dr.

 To Profit and Loss A/c

(Transferred credit balances

to Profit and Loss Account)

Q3 :

Discuss the need of preparing a balance sheet.

Answer :

The needs to prepare a Balance Sheet are given below.

1. It helps in determining the nature and book value of various assets, such as fixed assets, investments, current assets, etc. at the end of an accounting period.
2. It helps in ascertaining the nature and amount of various liabilities like long term liabilities, current liabilities, provisions, etc., which a business owes.
3. It discloses important information about capital invested in a business. The additional capital invested during the accounting period, drawings of the owners and profit (or loss) added to (or deducted from) the capital of the business.
4. It helps in assessing the solvency of a business.
5. It discloses the true financial position of a business at a particular point of time.
6. It lays down the basis for maintaining new books for next accounting period.

Q4 :

What is meant by Grouping and Marshalling of assets and liabilities? Explain the ways in which a balance sheet may be marshalled.

Answer :

The rationale behind preparing financial statements is to present a summarised version of all financial activities in such a manner that all users can interpret and understand the information easily, appropriately and also take decisions accordingly.

Grouping of assets and liabilities: Grouping means showing similar assets and liabilities under a single head. For example, all assets that can be used for more than a year are clubbed together under the heading 'fixed assets', for example, building, furniture, machinery, etc.

Marshalling of asset and liabilities: When assets and liabilities are shown in a particular order of liquidity or permanence, they are said to be marshalled.

1. In order of liquidity: Liquidity means convertibility into cash. Assets that can be converted into cash in least possible time, i.e., more liquid assets are recorded first, followed by the lesser liquid assets. In a balance sheet, cash in hand is recorded at first and goodwill at last. In the same way, liabilities that are to be paid first, i.e., high priority liabilities are recorded first, followed by the lower priority ones. In a balance sheet, current liabilities are recorded first and then the long term liabilities and capital at the last.

Balance Sheet of....., as on.....

Liabilities	Amount Rs	Assets	Amount Rs
Current Liabilities:		Current Assets:	
Bills Payable	-	Cash in Hand	-
Sunday Creditors	-	Cash at Bank	-
Bank Overdraft	-	Bills Receivable	-
Long Term Loans	-	Debtors	-
Capital:		Closing Stock	-
Opening balance	-	Long Term Investments	
Add: Net Profit	-	Fixed Assets:	
Less: Drawings	-	Furniture	-
	-	Plant and Machinery	-
		Land and Building	-
		Goodwill	-
	-		-

2. In order of permanence: It is just the reverse of the above method. In this, assets and liabilities are arranged in their reducing level of permanence. The assets with higher degree of permanence are recorded first, followed by the assets with lower degree of permanence. For example, goodwill, land and building have the highest degree of permanence and hence are recorded at the top, whereas, cash at bank and cash in hand are recorded at the bottom. In the same way, liabilities are shown according to their life in the business. Liabilities with higher level of permanence like, capital is recorded at the top and other liabilities with lower permanence are recorded at the bottom.

Balance Sheet of....., as on.....

Liabilities	Amount Rs	Assets	Amount Rs
Capital:		Fixed assets:	
Opening Balance	-	Goodwill	-
Add: Net profit	-	Land and Building	-
Less: Drawings			