theclimb.in

Practice Questions – 2018
Class : XII
Accountancy

Please Note:
This sheet is prepared on the basis of important theory and numericals from NCERT which needs to be paid attention.
*Though all the questions are important but the * marked questions should necessarily be done.*

Not – for – Profit Organisation

1. What are Not-for-Profit Organisations?
   Ans: These are those organizations that are for the welfare of the society and are set up as charitable institutions which function without profit motive.
2. How are Not-for-Profit Organisations organized?
   Ans: These organisations are organized as charitable trusts or societies.
3. What are the main sources of income for NPO?
   Ans: Main sources of income for NPO are:
   a) Subscription from members
   b) Donations
   c) Legacies
   d) Grant-in-aid
   e) Income from investments etc
4. How is surplus of NPO treated?
   Ans: Surplus of NPO is not distributed amongst the members but is simply added to capital fund or general fund.
5. What is the excess of assets over liabilities is referred as in NPO and how it is created?
   Ans: Excess of assets over liabilities is referred as capital fund instead of capital in case of NPO. It is also called as general fund.
   This fund is created from –
   (i) Surplus generated
   (ii) Life membership fee
   (iii) Donations capitalised,
   (iv) Legacies and
   (v) Capitalised Entrance Fees
6. Why a Not-for-Profit Organisation has to prepare final accounts?
   Ans: NPO are supposed to make final accounts for the following reasons-
   - To provide the necessary financial information to members, donors and contributors and
   - To submit to Registrar of Societies
7. Which two purposes are served by preparing Receipts and Payments Account?
   Ans: Receipts and Payments A/c serves following purposes:
   a) Helps in the preparation of Income and Expenditure A/c and Balance Sheet and
   b) a NPO is supposed to submit this account to Registrar of Societies along with Income & Expenditure A/c and Balance Sheet.
8. Does a NPO makes Trial Balance? Why?
   Ans: Trial Balance can be made by any organization which makes accounts under double entry system. Thus even a NPO can make Trial Balance to check the accuracy of ledger accounts. It helps to prepare Receipts & Payments A/c, Income & Expenditure A/c and Balance Sheet.
9. State any four features of Receipts and Payments Account.
   Ans: Features of Receipts and Payments Account:
   a) It is a real account and is a summary of cash book
   b) It shows total receipts and payments irrespective of accounting period

c) It also shows all receipts and payments which may be either of capital nature or revenue nature.
d) Non cash transactions like depreciation, unpaid expenses and items like accrued incomes, advance expenses and incomes are not shown in it.
e) Opening and closing balances of this account shows cash and bank balances at the beginning or at end of the year.

10. While preparing Income & Expenditure A/c from Receipts and Payments A/c, which items are excluded?
Ans: (i) Opening and closing balances in Receipts & Payments A/c
(ii) Capital Receipts and Capital Payments

11. Which items are considered while preparing Income & Expenditure A/c from Receipts & Payments A/c?
Ans: Following items are included in Income & Expenditure A/c from preparing it from Receipts & Payments A/c:
(i) Revenue receipts after adjusting for amounts relating to preceding or succeeding years and unpaid amounts of current year
(ii) Revenue expenses after adjusting for outstanding and prepaid amounts.
(iii) Items to be considered like – Depreciation, provision for bad debts and profit or loss on sale of fixed assets.

12. Differentiate between Income & Expenditure A/c and Receipts & Payments A/c on the basis of – (i) Period, (ii) Nature of account, (iii) Nature of items (iv) Opening Balance and (iv) closing balance. (NCERT Page 16)
Ans: Difference between Income & Expenditure A/c and Receipts & Payments A/c

S.No.	Basis	Income & Expenditure A/c	Receipts & Payments A/c
(i)	Period	Income and Expenditure A/c items relate only to the current period	Receipts and Payments A/c may also relate to preceding and succeeding periods
(ii)	Nature of account	It is a nominal account like Profit & Loss A/c	It is a real account and is a summary of cash book
(iii)	Nature of items	It records items of revenue nature only	It records items of revenue and capital nature
(iv)	Opening Balance	There is no opening balance	Balance at the beginning represents cash in hand/ cash at bank or overdraft at the beginning
(v)	Closing Balance	Balance at the end represents excess of income over expenditure or vice versa	Balance at the end represents cash in hand at the end and bank balance or bank overdraft.

13. What are subscriptions in a not-for-profit organization? How its treatment differs in Receipts & Payments A/c and Income & Expenditure A/c?
Ans: Subscription is a membership fee paid by the member on annual basis. This is the main source of income of NPO.
Receipts & Payments A/c shows the total amount of subscription actually received during the year, whereas Income & Expenditure A/s shows amount related to current year only whether received or not.

14. What is the treatment of following items in the final accounts of NPO?
a) Legacies
b) Life membership fees
c) Entrance Fees
d) Sale of periodicals
e) Sale of assets
f) Sale of old sports materials

Ans: Treatment is as under:
a) Legacies: It appears in the receipts side of Receipt & Payments A/c
It is of non-recurring nature and is therefore directly added to capital fund in the balance sheet. Though, the small amount may be treated as income in Income & Expenditure A/c.

b) Life Membership Fees : It is a lump sum payment by members and is therefore of non-recurring nature. It is of capital nature and is added to capital fund.

c) Entrance Fees: It is paid only once by the member at the time of becoming member of the organization. Entrance Fees can be treated capital or revenue.
Capital Receipt – In organisations like clubs and other charitable institutions amount of entrance fees is quite high and number of members is limited. In such cases entrance fees is treated as capital receipt and is added to capital fund in the balance sheet.
Revenue Receipt – For educational institutions entrance fees is regular income besides amount may not be very big. It is treated as income and shown in income and expenditure account.

d) Sale of periodicals: It is of recurring nature and is shown as income in Income & Expenditure A/c

e) Sale of assets: Gain or loss on sale of old assets is shown in Income & Expenditure A/c and the book value of the asset sold is deducted from the balance of asset in Balance Sheet.

f) Sale of old sports materials: Sale of old sports materials is a regular feature of any sports club and is shown as income in the Income & Expenditure A/c

15. How is the negative balance of a fund shown in final accounts of NPO?
Ans: Negative balance of fund is transferred to debit side of Income & Expenditure A/c

Partnership Accounting

16. In which cases profits made by a partner through his personal efforts will belong to the firm?
Ans: In following cases profits made by a partner becomes profits of the firm:
(i) If a partner derives any profit for him/her self from any transaction of the firm or from the use of the property or business connection of the firm or of the firm name, he/she shall account for the profit and pay it to the firm.
(ii) If a partner carries on any business of the same nature as and competing with that of the firm, he/she shall account for and pay to the firm, all profit made by him/her in that business.

17. Name the account which is prepared to distribute the net loss among the partners of a firm.
Ans: Profit & Loss Appropriation A/c

18. A, B and C are partners their partnership deed stated that C is to be allowed an annual salary of ₹12,000. B and C changed the deed and stated salary to C as ₹15,000 in the new deed. A does not agree to this. If profits of the firm are ₹50,000, how much salary if any will be allowed to C?
Ans: Deed can be changed with the consent of all the partners and not otherwise. Therefore C will be entitled to get salary of ₹12,000 only.

19. A, B and C are partners with capitals of ₹2,00,000, ₹1,50,000 and ₹4,00,000. At the end of the year B is claiming interest on capital @10% p.a. even though it was not expressly agreed. At what rate partners can be allowed interest on capital?
Ans: Interest on capital can be allowed only when it is expressly agreed in the partnership deed by all the partners.

20. A, B and C are partners in a firm sharing profits and losses in the ratio of 2:2:1. D was a regular customer of the firm and had been buying lot of goods of the business. B contacted D and sold some of his goods to him and made a profit of ₹18,000. After knowing about it A and C claim that this profit made by B belongs to the firm, whereas B claims that he has sold his goods of his personal investment and therefore the profits belong to him. Justify your stand with reason.

Ans: The profits made by B belong to the firm.
Reason: If a partner carries on any business of the same nature as and competing with that of the firm, he/she shall account for and pay to the firm, all profit made by him/her in that business.

21. A, B and C started a partnership business on 1st July, 2017. Profit and Loss A/c for the period ending on 31st March, 2018 showed a net loss of ₹12,000. Their partnership deed provided as under:
a) Interest on capital @5% p.a. (Capitals – A ₹1,20,000; B - ₹2,00,000; C - ₹2,50,000.
b) Partners Salary as a charge – A ₹24,000 p.a.; B ₹36,000 p.a.
c) Profits and losses are to be shared in the ratio of 3:2:1.
Prepare necessary account to distribute the loss and Partners' Current Account for the period ending on 31st March, 2018.

Hint: Profit and Loss Appropriation Account will be prepared even in case of loss, though IOC will not be provided by Partners' Salary will be provided. Salaries to the partners is p.a. therefore it will be provided only for nine months, i.e. A's salary will be ₹18,000 and B's Salary will be ₹27,000.
Partners Current Account will be prepared normally without any opening balance.

(#NCERT very clearly states that Profit & Loss Appropriation A/c will be prepared even in case of loss)

22. State conditions when the partners can expressly agree to provide interest on capital.
Ans: Interest on Capital is provided only when partners have expressly agreed to provide for the same in the partnership deed. Partners may do so under following conditions:
a) When the partners contribute unequal amounts of capitals but share profits equally, and
b) where the capital contribution is same but profit sharing is unequal.

23. If the partners have agreed to provide interest on capitals and the profits of the firm is less than the total amount interest on capital. How if any interest on capital will be provided?
Ans: When profits are less than the total amount of interest on capital, the interest on capital will be restricted to profits and it will be distributed in the ratio of interest on capital.

24. Rani and Suman are in partnership with capitals of ₹80,000 and ₹60,000, respectively. During the year 2016-17, Rani withdrew ₹10,000 from her capital and Suman ₹15,000. Profits before charging interest on capital was ₹5,000. Ravi and Suman shared profits in the ratio of 3:2. Calculate the amounts of interest on their capitals @ 12% p.a. for the year ended March 31, 2017.
Hint: First interest on capital will be calculated for both the partners and then the profits will be distributed in the ratio of interest on capital as profits are less than the total interest on capital.

25. What is the purpose of charging interest on drawings?
Ans: The purpose of charging interest on drawings is to discourage the partners from withdrawing excess amount from the business.

26. What is Profit and Loss Appropriation Account and state two purposes of preparing it?
Ans: Profit and Loss Appropriation Account is an extension of Profit and Loss Account.
It is prepared –
- to distribute the profit or loss of the business to partners as per the provisions of the partnership deed and
- to distinguish between the results of operations of business and the distribution of the profit among the owners.

27. What happens to the agreement of partnership on reconstitution?
Ans: On reconstitution old agreement comes to an end and new agreement is created with changed relationship.

28. What are the conditions of reconstitution of a partnership firm?
Ans: A partnership firm can be reconstituted in the following situations:
a) Change of profit sharing ratio of partners
b) Admission of a new partner
c) Retirement of a partners
d) Death of a partner
e) Insolvency of a partner.

29. Why a partnership firm may decide to admit a new partner?
Ans: A partnership firm may decide to admit a new partner for any or both of the following reasons:
a) For additional capital
b) For managerial talent

30. * What are the two rights acquired by a new partner and what does the partner does for acquiring these rights?
Ans: A new partner acquires following rights in the firm:
a) Right to share the assets of the partnership firm for which partner invests capital in the firm; and
b) Right to share the profits of the partnership firm for which partner pays share in the goodwill of the firm.

31. A partnership firm of B and D was able to generate profits higher than the normal rate on capital. They decided to admit C as a new partner. B and D asked C to contribute additional amount. What is this additional amount called, why was C asked to pay for it and how this amount is recorded?
Ans: The additional amount paid by C to the firm is known as goodwill share or premium.
This additional amount is paid by the new partner for following reasons –

- As any new firm will not be able to earn profits in first few years and by joining a continuing business new partner will earn profits in these few years and
- By admission of a new partner will have to sacrifice a part of their earnings therefore new partner pays goodwill to compensate the old partners for loss in their share of super profits

This amount of premium is distributed to partners in their sacrificing ratio.

32. What are the points that require attention / consideration at the time of admission of a partner?
Ans: On admission of a new partner following points require attention:
    a) New profit sharing ratio;
    b) Sacrificing ratio;
    c) Valuation and adjustment of goodwill;
    d) Revaluation of assets and Reassessment of liabilities;
    e) Distribution of accumulated profits (reserves); and
    f) Adjustment of partners' capitals.

33. On admission of new partner in a firm, if nothing is mentioned in which ratio new partners acquires his share from the old partners?
Ans: In such a situation it is assumed that the new partner acquires his share from the old partners in their old profit sharing ratio.

34. What is sacrificing ratio?
Ans: The ratio in which the old partners agree to sacrifice their share of profit in favour of the incoming partner is called sacrificing ratio.
The sacrifice by a partner is equal to : Old Share of Profit – New Share of Profit

35. What is meant by 'Goodwill'?
Ans: Goodwill is the present value of a firm's anticipated excess earnings. It can also be said as the capitalised value the excess differential profit capacity of a business.

36. When adjustment entries for goodwill are required in a partnership firm?
Ans: Adjustment for goodwill is required at the time of reconstitution of a firm viz., a change in the profit sharing ratio, the admission of a partner or the retirement or death of a partner.

37. What are the factors that affect the valuation of goodwill?
Ans: The main factors affecting the value of goodwill are as follows:
    a) *Nature of business*: A firm that produces high value added products or having a stable demand is able to earn more profits and therefore has more goodwill.
    b) *Location*: If the business is centrally located or is at a place having heavy customer traffic, the goodwill tends to be high.
    c) *Efficiency of management*: A well-managed concern usually enjoys the advantage of high productivity and cost efficiency. This leads to higher profits and so the value of goodwill will also be high.
    d) *Market situation*: The monopoly condition or limited competition enables the concern to earn high profits which leads to higher value of goodwill.
    e) *Special advantages*: The firm that enjoys special advantages like import licences, low rate and assured supply of electricity, long-term contracts for supply of materials, well-known collaborators, patents, trademarks, etc. enjoy higher value of goodwill.

38. When the goodwill of the firm is valued in case of partnership firm?
Ans: In the context of a partnership firm it may also arise in the following circumstances:
    a) Change in the profit sharing ratio amongst the existing partners;
    b) Admission of new partner;
    c) Retirement of a partner;
    d) Death of a partner; and
    e) Dissolution of a firm involving sale of business as a going concern.
    f) Amalgamation of partnership firms.

39. A, B and C are partners in a firm. Their capitals were ₹4,00,000, ₹3,50,000 and ₹4,50,000 respectively. The normal rate of return in their category business is 10%. The firm made a profit of ₹1,00,000. They decided to admit D as a new partner for managerial support and for need of additional capital. A, B and C ask D to invest

₹2,50,000 as capital and to pay ₹1,50,000 as premium for goodwill. D agrees to invest ₹2,50,000 and refuses to pay premium. Was D correct to refuse to pay goodwill. Give reason for your answer.

Ans: Yes D is correct to refuse to pay goodwill premium.
Because goodwill is the value of reputation or good name which results in earning higher profits than the normal profits for the firm. Goodwill does not arise when the actual profit of the firm is equal to or less than the normal profits and firm is in loss. In the case of firm of A, B and C normal profit is ₹1,20,000 whereas the firm is earning only ₹1,00,000. As actual profits are less than normal profits therefore goodwill of the firm does not arise.

40. What do you understand by 'Number of years purchase' in case of valuation of goodwill?
Ans: Number of years is the duration for which it is expected that the firm will continue to earn super profits.

41. Do all businesses firms have goodwill? When goodwill does not exists?
Ans: Goodwill does not exist in all cases. A firm will not have goodwill in following cases –
a) When firm is new. Only running businesses have goodwill.
b) When firm is able to earn profits more than normal profits. Firms in loss or earning just normal profits do not have goodwill.

42. When it is advised to calculate goodwill on the basis of simple average and when on the basis of weighted average?
Ans: When it is expected that there is not going to be any change in the overall situation of profits is expected in the future, then goodwill is valued on the basis of simple average profits.

But when there exists an increasing on decreasing trend, it is considered to be better to give a higher weightage to the profits to the recent years than those of the earlier years.

43. Jagan Poultry is a partnership firm of Jagan and Magan. Due '*swine flu*' scare and rising prices of maize and other grains the poultry industry was facing average loss of 12%. Jagan Poultry was also facing a loss of 8%. Jagan and Magan decided to admit Chagan an expert in poultry industry as their partner for additional capital and expertise. Besides capital of ₹5,00,000 they asked Chagan to pay for goodwill share of ₹1,50,000.
Can a firm like Jagan Poultry claim goodwill share from the new partner?
Ans: Jagan Poultry can claim goodwill share from the new partner.
In case of losses in the industry the firm which suffers less loss can claim to have goodwill.

44. List the items that you would include to find out the sum due to the retiring partner (in case of retirement) and to the legal representatives/ executors (in case of death)?
Ans:
Following items will be included to determine the amount due to retiring partner or the executor of a deceased partner:
Following items will be added –
i) credit balance of his capital account;
ii) credit balance of his current account(if any);
iii) his share of goodwill ;
iv) his share of accumulated profits (reserves);
v) his share in the gain of revaluation of assets and liabilities;
vi) his share of profits up to the date of retirement/death;
vii) interest on his capital, if involved, up to the date of retirement/death; and
viii) salary/commission, if any, due to him up to the date of retirement/death.

Following items will be deducted:
i) debit balance of his current account(if any);
ii) his share of goodwill to be written off; if necessary;
iii) his share of accumulated losses;
iv) his share of loss on revaluation of assets and liabilities;
v) his share of loss up to the date of retirement/death;
vi) his drawings up to the date of retirement/death;
vii) interest on drawings, if involved, up to the date of retirement/death.

45. List the various accounting aspects that are involved on admission, retirement or death of a partner.

Ans:

Following items are involved on admission, retirement or death of a partner:

i) Ascertainment of new profit sharing ratio and gaining ratio;
ii) Treatment of goodwill;
iii) Revaluation of assets and liabilities;
iv) Adjustment in respect of unrecorded assets and liabilities;
v) Distribution of accumulated profits and losses;
vi) Ascertainment of share of profit or loss up to the date of retirement/death;
vii) Adjustment of capital, if required;
viii) Settlement of the amounts due to retired/deceased partner;

46. * When is new profit sharing ratio is not required to be calculated on retirement or death of a partner?

Ans: When the continuing partners acquire the share of retiring partner in their old profit sharing ratio, then new ratio of continuing partners need not be calculated, it is same as their old ratio.

47. When it is necessary to compute new profit sharing ratio of the continuing partners in case of retirement or death of a partner?

Ans: When the continuing partners acquire the share of retiring partner in some other ratio and not in their old profit sharing ratio, then new ratio of continuing partners must be calculated.

48. * When is gaining ratio and new ratio is same in retirement or death of a partner?

Ans: When the continuing partners acquire the share of the retiring or deceased partner in their old ratio, then the gaining ratio is also their old ratio. In such a case gaining ratio is not calculated.

49. Z retires from the firm. His capital on the date of retirement was ₹1,20,000 after all adjustments of profit of revaluation, share in undistributed profits and losses. He was paid ₹1,50,000 by the continuing partners. What for this difference was paid?

Ans: It is the share of goodwill of the retiring partner.

50. What are the conditions of dissolution of partnership?

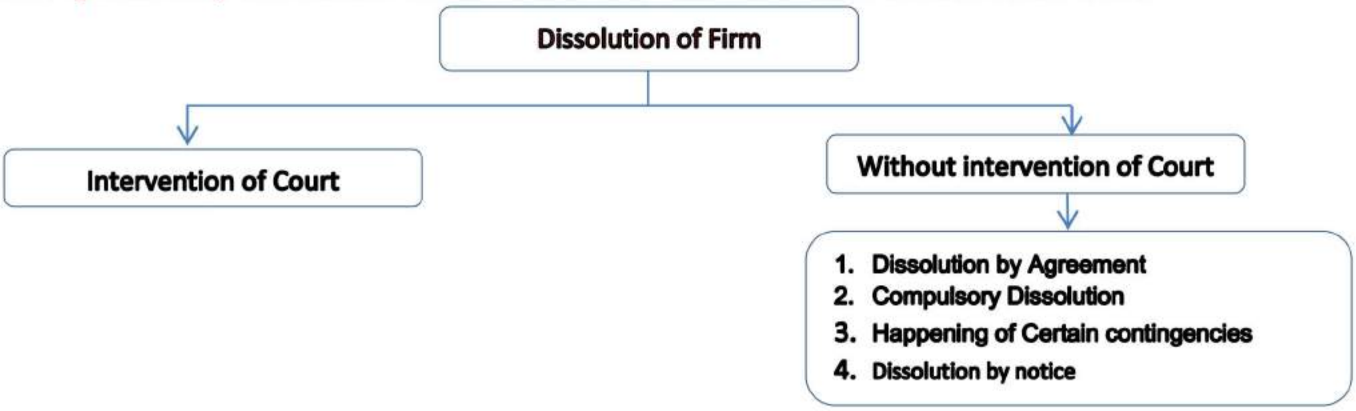
Ans:

The dissolution of partnership may take place in any of the following ways:

(1) Change in existing profit sharing ratio among partners;
(2) Admission of a new partner;
(3) Retirement of a partner;
(4) Death of a partner;
(5) Insolvency of a partner;
(6) Completion of the venture, if partnership is formed for that; and
(7) Expiry of the period of partnership, if partnership is for a specific period of time

51. When can the firm be dissolved? Explain the conditions.

Ans: A partnership firm can be dissolved with and without the intervention of the court.



1. **Dissolution by Agreement:** A firm is dissolved:
    a) With the consent of all the partners or
    b) In accordance with a contract between the partners.
2. **Compulsory Dissolution:** A firm is dissolved compulsorily in the following cases:
    a) When all partners or all but one partner, become insolvent, rendering them incompetent to sign a contract;
    b) When the business of the firm becomes illegal; or
    c) When some event has taken place which makes it unlawful for the partners to carry on the business of the firm in partnership, e.g. when a partner who is a citizen of a country becomes an alien enemy because of the declaration of war with his country and India
3. **On the happening of Certain Contingencies:** Subject to contract between the partners, a firm is dissolved:
    a) If constituted for a fixed term, by the expiry of that term;
    b) If constituted to carry out one or more ventures, by the completion thereof;
    c) By the death of a partner;
    d) By the adjudication of a partner as an insolvent.
4. **Dissolution by Notice:** In case of partnership at will, the firm may be dissolved if any one of the partners gives a notice in writing to the other partners, signifying his intention of seeking dissolution of the firm.
5. **Dissolution by Court:** At the suit of a partner, the court may order a partnership firm to be dissolved on any of the following grounds:
    a) When a partner becomes insane;
    b) When a partner becomes permanently incapable of performing his duties as a partner,
    c) When a partner is guilty of misconduct which is likely to adversely affect the business of the firm;
    d) When a partner persistently commits breach of partnership agreement
    e) When a partner has transferred the whole of his interest in the firm to a third party;
    f) When the business of the firm cannot be carried on except at a loss; or
    g) When, on any ground, the court regards dissolution to be just and equitable.

52. Distinguish between dissolution of partnership and dissolution of firm.

Basis	Dissolution of Partnership	Dissolution of firm
1. Termination of business	The business is not terminated	The business of the firm is closed
2. Settlement of assets and liabilities	Assets and liabilities are revalued and new balance sheet is drawn	Assets are sold and liabilities are paid off
3. Court's intervention	Court does not intervene because partnership is dissolved by mutual agreement	A firm can be dissolved by the court's order
4. Economic relationship	Economic relationship between the partners continues though in a changed form.	Economic relationship between the partners comes to an end.
5. Closure of books	Does not required because the business is not terminated	The books of account are closed
6. Other dissolution	It may or may not involve dissolution of the firm	It necessarily involves dissolution of partnership

Company Accounts

53. Explain the different categories of Share Capital.

Ans: Categories of Share Capital

Authorised Capital: It is that capital which the company is authorized to issue through its Memorandum of Association. It is also called Nominal or Registered Capital. It can be increased or decreased as per the provisions of the Act. Company can raise authorized capital according to its need.

Issued Capital: It is that part of Authorised Capital which is actually issued to the public including shares allotted to vendors and signatories to the memorandum of association. Issued capital cannot be more than authorized capital.

Subscribed Capital: It is that part of issued capital which has been subscribed by the public. Subscribed Capital is less than Issued Capital.

Called up Capital: It is that part of subscribed capital which has been called up by the company. Called up capital is same as subscribed capital if the entire amount of shares has been called up.

Paid up Capital: It is that portion of called up capital which has been actually received from the shareholders. When shareholders have paid all the called up amount. Called up capital is same as paid up capital.

Uncalled Capital: It is that amount of subscribed capital which has not been called up by the company and company can call this amount when it needs funds.

Reserve Capital: It is that portion of uncalled up capital. It can be called at the time of liquidation of the company. It is called reserve capital and is available only for creditors on winding up of the company.

54. What is a debenture?

Ans: Debenture is a written instrument acknowledging a debt under the common seal of the company.

55. What is the scope of Indian Companies Act,2013?

Or

Which companies are required to make financial statements according to Indian Companies Act,2013?

Ans : The Act is applicable to Indian companies preparing financial statement commencing on or after April 01, 2011

56. What is the nature of Discount on issue of debentures and how it is treated in financial statements?

Ans : Discount on issue of debentures is a capital loss. While preparing financial statements it is either debited to Securities Premium Reserve Account or is written off over a period of 3 to 5 years by debiting to Statement of Profit and Loss.

57. How will you treat the excess amount of debentures issued over the net assets taken over?

Ans : The excess amount of debentures issued over the net assets acquired when the business is taken over is debited to 'Goodwill A/c'.

58. How will you treat the difference when the amount of debentures issued is less than the net assets taken over?

Ans : The excess amount of net assets taken over the amount of debentures issued is credited to 'Capital Reserve A/c'.

59. * What is meant by 'Debentures issued as Collateral Security' and why is it given?

Ans : A collateral security is defined as a subsidiary or secondary or additional security besides the primary security when a company obtains a loan or overdraft from a bank or any other financial Institution.

The company may place own debentures to the lenders in addition to some other assets already pledged. Such an issue of debentures is known as 'Debentures issued as Collateral Security'. Collateral security is given so that the amount of loan can be realised in full with the help of collateral security in case the amount from the sale of principal security falls short of the loan money.

60. How does the lender uses the Debentures issued as Collateral Security if company is unable to pay off its debts?
Ans : If the lender is unable to recover its dues from the primary security then it can use collateral security to recover the amount. In such a case lender may either present the debentures for redemption or it may sell these debentures in the open market.

61. How is Debenture Suspense Account appears in the Balance Sheet of the company?
Ans : Debenture Suspense Account appears on the liability part as deduction from Debentures.

62. When the company pays off its loan to the lender which was secured by collateral issue of debentures, what entry will be made?
Ans : Following reverse entry is passed in such cases
Debenture A/c Dr
To Debenture Suspense A/c

63. * What is the nature 'Discount / Loss on Issue of Debentures' and how is it treated in the books of the company?
Ans : The discount/loss on issue of debentures is a capital loss or a fictitious asset. It can be written off as under:
   - If the company has balance in Securities Premium Reserve A/c, then this amount should be written off in the year of issue itself.
   - Since the benefit of debentures would accrue to the company till its redemption, it can also be written off through Statement of Profit and Loss over the life of debentures on the basis of amount of debentures outstanding.

64. How would you deal with 'Premium on Redemption of Debentures?
Ans : 'Premium on Redemption of Debentures' will be shown as under:
   - If the debentures are to be redeemed in the next account year/operating cycle - 'Other Current Liabilities' under Current Liabilities
   - If the debentures are to be redeemed after the coming next accounting year / operating cycle - Other Non-Current Liabilities under Non-Current Liabilities.

65. Can debentures be redeemed before the maturity date?
Ans: Debentures are normally redeemed on due date but a company may redeem its debentures before maturity date, if articles of the company provides for such redemption.

66. What are the three sources of redemption of debentures of a company?
Ans: A company may source its redemption of debentures either out of capital or out of profits as under:
   a. Out of Capital: Only those companies which are exempted from creating DRR may redeem debentures out of capital.
   b. Out of Profits: When any company planning to redeem its debentures purely out of profits, it should transfer 100 percent of the face value of the redeemable debentures to DRR out of the surplus available for payment of dividend.
   c. Out of Capital and Profits: Out of Capital and Profits: In case, company is planning to redeem its debentures by using both the sources partially, it does not transfer 100 percent of face value of outstanding debentures of a particular class to DRR out of the surplus available for payment of dividend.

67. Can any company redeem its debentures out of capital? Give reasons.

Ans : Company which is exempted from creating DRR can redeem its debentures out of capital.

68. XYZ Ltd redeemed its ₹10,00,000 12% Debentures of ₹100 each at premium of 10%. Company decided to create DRR for 40% of the amount of debentures redeemed. What is the source of redemption of debentures?

Ans : Company is redeeming its dentures out of profits and capital both as company is creating DRR for 40% of the face value of redeemed debentures and remaining 60% of the debentures are redeemed out of capital.

69. On what basis will you classify an asset or a liability as current or non-current?

Ans : An item is classified as current:

- if it is involved in entity's operating cycle or,
- is expected to be realized / settled within twelve months or,
- if it is held primarily for trading or,
- is cash and cash equivalent or,
- if entity does not have an unconditional rights to defer settlement of liability for at least 12 months after the reporting period.
- Other assets and liabilities are non-current.

70. What are preliminary expenses? How are these written off?

Ans: Preliminary expenses are to be written off completely in the year in which such expenses are incurred. They should first be written off from securities premium and the balance if any, from statement of profit & loss.

71. What is borrowing costs? Give two examples. How it is written off?

Ans: Ex. Discount on issue of debentures. Such expenses are written off over the loan period.

72. How are borrowings treated in the balance sheet?

Ans: Total borrowings are categorized into long term borrowings, short term borrowings and current maturities to long term debts.

i) Loans which are repayable in more than twelve months / operating cycle are classified as long term borrowings on the face of balance sheet.

ii) Loans repayable on demand or whose original tenure is not more than twelve months / operating cycle are classified as short term borrowings on the face of balance sheet.

iii) Current maturities to long term debts include amount repayable within twelve months / operating cycle under other current liabilities in notes to accounts.

73. How is trade payable shown in the Balance Sheet of a company?

Ans: Trade Payables are classified as current and non-current.

Non – Current Trade Payables: Trade payables to be settled beyond 12 months from the date of balance sheet or beyond the operating cycle are classified under 'other long term liabilities' in notes to accounts.

Current Trade Payables: Are classified under current liabilities on the face of balance sheet

74. How are trade receivables shown in the balance sheet of a company?

Ans: Trade Receivables are classified as current and non-current.

Non- Current Trade Receivables: Trade receivable realized beyond twelve months from reporting date are classified as 'Other non-current assets' under the heading of non-current assets in the notes to accounts.

Current Trade Receivables: Other trade receivables classified as current assets are shown in the face of the balance sheet.

75. Show the following items in the financial statements of a company:

S.No.	Items	Major Head	Sub Head (if any)
1.	Goodwill	Non-Current Assets	Fixed Assets – Intangible Assets
2.	Forfeited shares	Shareholders' Fund	Subscribed Capital
3.	Acceptances	Current Liabilities	Trade Payables

4.	Preliminary expenses	Non-Current Assets	Other non-current Assets
5.	Capital reserve	Shareholders' Funds	Reserves & Surplus
6.	Loans from banks	Non-Current Liabilities	Long Term Borrowings
7.	Investment in shares and debentures	Non-Current Assets	Non-Current Investments
8.	Interest accrued and due on debentures	Current Liabilities	Other current Assets
9.	Interest accrued but not due on Secured Loans	Current Liabilities	Other current Assets
10.	Interest accrued but not due on Unsecured	Current Liabilities	Other current Assets
11.	Loans	Non-Current Liabilities	Long Term Borrowings
12.	Interest accrued on Investments	Current Assets	Other Current Assets
13.	Surplus	Shareholders' Fund	Reserve & Surplus
14.	Securities Premium Reserve	Shareholders' Fund	Reserve & Surplus
15.	Loose Tools	Current Assets	Inventories
16.	Provision for Taxation	Current Liabilities	Short Term Provisions
17.	Under writing Commission	Non-Current Assets	Other non-current Assets
18.	Bills of Exchange	Current Assets	Trade Receivables
19.	Unclaimed dividend	Current Liabilities	Other Current Liabilities
20.	Short term loans & advances	Current Assets	
21.	Calls unpaid/calls in arrears	Shareholders' Funds	Subscribed Capital
22.	Uncalled liability on shares partly paid	Contingent Liabilities	
23.	Discount allowed on issue of shares and debentures (if amortised after 12 months)	Non-Current Assets	Other non-current Assets
24.	Discount allowed on issue of shares and debentures (if amortised within 12 months)	Current Assets	Other current Assets
25.	Pre-paid Insurance	Current Assets	Other Current Assets
26.	Stores and spare parts	Current Assets	Inventories
27.	Advances from customers	Current Liabilities	Other Current Liabilities
28.	Debentures redemption reserve	Shareholders' Fund	Reserve & Surplus
29.	Premium on redemption of debentures	Non-Current Liabilities	Long Term Borrowings
30.	Loss on issue of debentures	Non Current / Current Assets	
31.	Debentures redemption fund	Shareholders' Fund	Reserve & Surplus
32.	Debentures redemption fund investment	Non-Current Assets	Non-Current Investments
33.	Vehicles	Non-Current Assets	Fixed Assets – Tangible Assets
34.	Sinking fund	Shareholders' Fund	Reserve & Surplus
35.	Sinking fund investment	Non-Current Assets	Non-Current Investments
36.	Advances to suppliers	Current Assets	Other Current assets
37.	Patents, trademarks, design	Non-Current Assets	Fixed Assets – Intangible Assets
38.	Calls in advance	Current Liabilities	Other Current Liabilities
39.	Deposits with custom authorities	Non-Current Assets	Other Non-Current Assets
40.	Arrears of fixed cumulative dividend	Current Liabilities	Other Current Liabilities
41.	Furniture and fittings	Non-Current Assets	Fixed Assets – Tangible Assets
42.	Brokerage on issues of shares	Current Assets	Other Current Assets
43.	Statement of profit & loss (Dr.)	Shareholders' Fund	Reserve & Surplus
44.	Capital work-in-progress	Non-Current Assets	Fixed Assets

theclimb.in

45.	Provision for doubtful debts	Current Liabilities	Short Term Provisions
46.	Statement of profit & loss (Cr.)	Shareholders' Fund	Reserve & Surplus
47.	Uncalled liability on partly paid shares held as investments	Contingent Liabilities	
48.	Claims against the company not acknowledged as debt	Contingent Liabilities	
49.	Capital redemption reserve	Shareholders' Fund	Reserve & Surplus
50.	Public deposits	Non-Current Liabilities	Long Term Borrowings
51.	Authorised capital	Shareholders' Fund	Share Capital
52.	Bank Balance	Current Assets	Cash & Cash Equivalent

76. List any two items that are presented under the head 'other current liabilities' and any two items that are presented under the head 'other current assets' as per schedule III of the Companies Act, 2013.

Ans: Other Current Liabilities

(i) Current maturities of long term debts
(ii) Interest accrued but not due on borrowings
(iii) Interest accrued and due on borrowings
(iv) Income received in advance
(v) Unpaid Dividend
(vi) Application money received for allotment of securities and due for refund and interest due there on.
(vii) Unpaid matured deposits and interest accrued there on.
(viii) Unpaid matured debentures and interest accrued thereon.
(ix) Calls in advance
(x) Other payables(outstanding expenses, calls in advance, provident fund payable, ESI payable, CST payable, VAT payable etc.)

Other Current Assets (Any two)

(i) Unamortised expenses/losses (to be written off within 12 months from the date of balance sheet)
(ii) Prepaid expenses
(iii) Dividend receivable
(iv) Advance Taxes

77. List the items to be shown under 'Reserves and Surplus' in the Balance Sheet of a company.

Ans: Items shown under 'Reserves and Surplus'

i) Capital Reserve
ii) Capital Redemption Reserve
iii) Securities Premium Reserve
iv) Debenture Redemption Reserve
v) Revaluation Reserve
vi) Share Options Outstanding Account
vii) Other Reserves (Specifying nature and purpose)
viii) Surplus: Balance in statement of profit and loss; disclosing allocations and Appropriation such as dividend, bonus shares, transfer to/from reserve, etc

78. List the criteria according to which items are classified as current items in the Balance Sheet of a company?

Ans: An item is classified as current:

- if it is involved in entity's operating cycle or,

- is expected to be realised/settled within twelve months or,
- if it is held primarily for trading or,
- is cash and cash equivalent or,
- if entity does not have on unconditional rights to defer settlement of liability for atleast 12 months after the reporting period, other assets and liabilities are non-current.

79. State three items shown under Revenue from Operations in the Statement of Profit & Loss of a non-finance company.
Ans: (i) Sale of Products
(ii) Sale of Services
(iii) Other Operating Revenues

80. State three items shown under Revenue from Operations in the Statement of Profit & Loss of a finance company.
Ans: (i) Revenue from Interest
(ii) Revenue from Dividend
(iii) Income from other financial services

81. What you mean by Financial Statement Analysis?
Ans: Financial statement analysis is a process which involves regrouping and analysis of information provided by financial statements to establish relationships and throw light on the points of strengths and weaknesses of a business enterprise, which can be useful in decision-making involving comparison with other firms and with firms' own performance, over a time period.

82. * What is the significance of Financial Statement Analysis for Finance Manager, Lenders and Labour Unions?
Ans: Significance of Financial Statement Analysis:
a) Finance manager: Financial analysis focuses on the facts and relationships related to managerial performance, corporate efficiency, financial strengths and weaknesses and creditworthiness of the company. It helps the finance manager in understanding the continuity of the operating policies, investment value of the business, credit ratings, testing the efficiency of operations, effectiveness of systems of financial control etc and to take corrective action wherever required.
b) Lenders: Suppliers of long-term debt are concerned with the firm's long term solvency and survival. They analyse the firm's profitability over a period of time, its ability to generate cash, to be able to pay interest and repay the principal.
c) Labour unions: Labour unions analyse the financial statements to assess whether it can presently afford a wage increase and whether it can absorb a wage increase through increased productivity or by raising the prices.

83. What are the objectives of Financial Statement Analysis?
Ans: Analysis of financial statements reveals important facts concerning managerial performance and the efficiency of the firm. Normally following are the objectives of this analysis.
- to assess the current profitability and operational efficiency of the firm as a whole as well as its different departments so as to judge the financial health of the firm.
- to ascertain the relative importance of different components of the financial position of the firm.
- to identify the reasons for change in the profitability/financial position of the firm.
- to judge the ability of the firm to repay its debt and assessing the short-term as well as the long-term liquidity position of the firm.

84. What are the tools of Analysis of Financial Statements ?
Ans: Following tools are used for Analysis of Financial Statements.
a) Common Size Statements

b) Comparative Statements
c) Trend Analysis
d) Ratio Analysis
e) Cash Flow Statement

85. * Name the tool of financial statement analysis which is used for identifying the direction of changes and also the trends in different indicators of performance of an organization.
Ans: Comparative Statements

86. What is the other name for Common Size Statement?
Ans: Component Percentage Statement

87. * Name the tool of financial statement analysis which is used for studying the key changes and trends in the financial position and operational result of a company
Ans: Common Size Statement

88. What purpose is served by making Comparative Statements?
Ans: It is possible to find out not only the balances of accounts as on different dates and summaries of different operational activities of different periods, but also the extent of their increase or decrease between these dates.

89. What purposes are served by making Common Size Statements?
OR
What are the objectives of preparing Common Size Statements?
Ans: Following purposes are served by making Common Size Statements:
1. It is a financial tool for studying the key changes and trends in the financial position and operational result of a company.
2. Common size analysis is of immense use for comparing enterprises which differ substantially in size as it provides an insight into the structure of financial statements.
3. Inter-firm comparison or comparison of the company's position with the related industry as a whole is possible with the help of common size statement analysis.

90. What are the limitations of financial analysis?
Ans: Financial analysis is quite helpful in determining financial strengths and weaknesses of a firm, yet it has following limitations:
1. Financial analysis does not consider price level changes.
2. Financial analysis may be misleading without the knowledge of the changes in accounting procedure followed by a firm.
3. Financial analysis is just a study of reports of the company.
4. Monetary information alone is considered in financial analysis while non-monetary aspects are ignored.
5. The financial statements are prepared on the basis of accounting concept, as such, it does not reflect the current position.

91. What are Accounting Ratios?
Ans: A ratio is a mathematical number which refers to the relationship between two accounting figures derived from the financial statements. It can be expressed in terms of fraction, proportion, percentage or in number of times.

92. What are the objectives of Ratio Analysis?
Ans: Following are the main objectives of Ratio Analysis:
1. To know the areas of the business which need more attention;
2. To know about the potential areas which can be improved with the effort in the desired direction;
3. To provide a deeper analysis of the profitability, liquidity, solvency and efficiency levels in the business;

4. To provide information for making cross-sectional analysis by comparing the performance with the best industry standards; and
5. To provide information derived from financial statements useful for making projections and estimates for the future.

93. Which ratio is calculated to measures the degree of indebtedness of an enterprise and gives an idea to the long-term lender regarding extent of security of the debt?
Ans: Debt Equity Ratio

94. Name the ratios which measure the degree of liquidity.
Ans: Inventory Turnover Ratio and Trade Receivable Turnover Ratio

95. Which ratio tells us the margin available for meeting operating expenses, non-operating exp?
Ans: Gross Profit Ratio

96. Which ratio helps to analyse the performance of business and also throws light on the operational efficiency of the business in inter-firm as well as intra-firm comparisons?
Ans: Operating Profit Ratio

97. Why is quick ratio also called as 'Acid Test Ratio'?
Ans: It is calculated to serve as a supplementary check on liquidity position of the business and is therefore, also known as 'Acid-Test Ratio'.

98. State the benefits of making Cash flow statement.
Ans: Following are the benefits of making Cash Flow Statement:
- It provides information to evaluate changes in net assets of an enterprise, its financial structure (including its liquidity and solvency) and the estimation about the amounts and timings of cash flows.
- To assess the ability of the enterprise to generate cash and cash equivalents and to assess and compare the present value of the future cash flows of different enterprises.
- It enhances the comparability of the reporting of operating performance by different enterprises.
- It also helps in balancing its cash inflow and cash outflow.
- It is also helpful in checking the accuracy of past assessments of future cash flows and in examining the relationship between profitability and net cash flow and impact of changing prices.

99. What is meant by Cash and Cash Equivalents and when does an investment qualifies as cash equivalent?
Ans: 'Cash' comprises cash in hand and demand deposits with banks, and 'Cash equivalents' means short-term highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.
An investment qualifies as cash equivalents only when it has a short maturity, of say, three months or less from the date of acquisition.

100. Do we consider investment in shares as part of cash equivalents?
Ans: Investments in shares are excluded from cash equivalents unless they fulfill the criteria of cash equivalents substantially.
For example, preference shares of a company acquired shortly before their date of redemption and provided there is only insignificant risk of failure of the company to repay the amount on maturity.

101. Why are short-term marketable securities considered as cash equivalents?
Ans: Short-term marketable securities are presumed to be readily converted into cash without considerable change in their value.

102. Where will you show purchase of marketable securities in preparing cash flow statement?
Ans: Marketable Securities or Short-term Investment are considered as cash equivalent therefore their purchase is not considered or is not shown anywhere while preparing cash flow statement.

103. What are Operating Activities ? List few activities resulting in inflow and outflow.
Ans: Operating activities are the activities that constitute the primary or main activities of an enterprise. These are the principal revenue generating activities.

104. Give two examples of operating activities of a company manufacturing garments?
Ans: Operating activities are – (any two)
- Procurement of raw material,
- incurrence of manufacturing expenses,
- sale of garments, etc.

105. What does amount of cash from operating activities indicate?
Ans: The amount of cash from operations' indicates the internal solvency level of the company, and is an indicator to what extent operations of the enterprise are able to generate sufficient cash flows in within the organisation for paying dividends, making of new investments and repaying of loans without recourse to external source of financing.

106. List two examples of cash inflow from operating activities of a business enterprise.
Ans: Cash inflows from operating activities
- cash receipts from sale of goods and the rendering of services.
- cash receipts from royalties, fees, commissions and other revenues.

107. List two examples of cash outflows from operating activities.
Ans: Cash outflow from operating activities:
- Cash payments to suppliers for goods and services.
- Cash payments to and on behalf of the employees.
- Cash payments to an insurance enterprise for premiums and claims, annuities, and other policy benefits.
- Cash payments of income taxes unless they can be specifically identified with financing and investing activities

108. A financial enterprise is holding some securities and loans. Where will you show them in Cash Flow Statement?
Ans: If the financial enterprise holds them for trading purposes, then they represent Inventory specifically held for resale. Therefore, cash flows arising from the purchase and sale of dealing or trading securities are classified as operating activities.

109. Where will you show cash advances and loans made by financial enterprise?
Ans: For a financial enterprise they are considered as part of inventory and are therefore classified as operating activities since they relate to main activity of that enterprise.

110. Where will you show a loan raised by a financial institution?
Ans: A financial institution may raise loans for two purposes:
- For trading purposes i.e. to borrow at lower rate and lend it further at higher rate or
- For using the finds for setting up business like buying office space, computers etc

If loan is raised for trading purposes, any cash flows arising out of it is considered as operating activity.
But if the loan has been raised for use in the organization it is considered as financing activity.

111. Where will you show expenditures made for resources intended to generate future income and cash flows.
Ans: Investing Activities

112. Give examples of cash outflows from investing activities.
Ans: Followings are few examples-
- Cash payments to acquire fixed assets including intangibles
- Cash payments to acquire shares, warrants or debt instruments of other enterprises other than the instruments those held for trading purposes.
- Cash advances and loans made to third party (other than advances and loans made by a financial enterprise wherein it is operating activities).

113. Give examples of cash inflows from investing activities.
Ans: Examples of cash inflow from investing activities:
- Cash receipt from disposal of fixed assets including intangibles.
- Cash receipt from the repayment of advances or loans made to third parties (except in case of financial enterprise).
- Cash receipt from disposal of shares, warrants or debt instruments of other enterprises except those held for trading purposes.
- Interest received in cash from loans and advances. I Dividend received from investments in other enterprises.

114. 'An enterprise may hold securities and loans for dealing or trading purpose in which case they are similar to inventory acquired specifically for resale.' Is the statement correct? Cash Flows from such activities will be classified under which type of activity while preparing Cash Flow Statement?
Ans: Yes, the statement is correct.
Operating Activity

115. Which activities result in the changes in the size and composition of the owners' capital (including preference share capital in case of a company) and borrowings of the enterprise?
Ans: Financing Activities

116. Which activity it is useful in predicting claims on future cash flows by providers of funds (both capital and borrowings) to the enterprise?
Ans: Financing Activities

117. Give two examples of cash inflows from financing activities.
Ans: Examples of cash inflow from financing activities:
- Cash proceeds from issuing shares.
- Cash proceeds from issuing debentures, loans, bonds and other short/ long-term borrowings.

118. Give two examples of cash outflows from financing activities.
Ans: Examples of cash outflow from financing activities (any two)
- Cash repayments of amounts borrowed.
- Interest paid on debentures and long-term loans and advances.
- Dividends paid on equity and preference capital.

119. * A newly set up textile company has acquired large machinery on deferred payment basis. Its installment was paid with interest during the year. How will you treat this item in the cash flow statement?
Ans: In this case installment payment will include both interest and loan. The amount of interest in the installment will be treated as financing activity and the principal amount of the loan amount will be classified under investing activity.

120. * How will you treat shares purchased by a share broking firm, in cash flow statement?
Ans: Purchase of shares is an operating activity for a share brokerage firm while it is investing activity in case of other enterprises.

theclimb.in

121. * How are Interests and Dividends treated in cash flow statement?
Ans: Treatment will depend upon the nature of business:
- For a financial enterprise –
  - interest paid, interest received and dividend received are classified as operating activities and
  - dividend paid is a financing activity.
- But for a non-financial enterprise –
  - payment of interest and dividends are classified as financing activities and
  - receipt of interest and dividends are classified as investing activities.

122. How will you treat taxes on incomes and gains in preparing cash flow statement?
Ans: There can be three types of taxes –
  - Income Tax (tax on normal profit)
  - Capital Gains Tax (tax on capital profits) and
  - Dividend Tax (tax on the amount distributed as dividend to shareholders).

These taxes are disclosed as under –
- tax on operating profit should be classified as operating cash flows.
- dividend tax, i.e., tax paid on dividend should be classified as financing activity along with dividend paid.
- Capital gains tax paid on sale of fixed assets should be classified under investing activities.

123. What are non-cash transactions in cash flow statement?
Ans: Investing and financing transactions that do not require the use of cash and cash equivalents are called as non-cash transactions in cash flow statment.

124. * Which type of transactions are excluded from cash flow statement? Give two such examples.
Ans: Non cash transactions are excluded from cash flow statement.
Examples of such transactions are –
- acquisition of machinery by issue of equity shares
- redemption of debentures by issue of equity shares.

125. Classify the following activities into operating activities, investing activities, financing activities, cash equivalents:
1. Purchase of machinery.
2. Proceeds from issuance of equity share capital.
3. Cash revenue from operations.
4. Proceeds from long-term borrowings.
5. Proceeds from sale of old machinery.
6. Cash receipt from trade receivables.
7. Trading commission received.
8. Purchase of non-current investment.
9. Redemption of preference shares.
10. Cash purchases.
11. Proceeds from sale of non-current investment
12. Purchase of goodwill.
13. Cash paid to supplier.
14. Interim dividend paid on equity shares.
15. Employee benefits expenses paid.
16. Proceeds from sale of patents.
17. Interest received on debentures held as investments.
18. Interest paid on long-term borrowings.
19. Office and administrative expenses paid.
20. Manufacturing overheads paid
21. Dividend received on shares held as investments

22. Rent received on property held as investment.
23. Selling and distribution expenses paid.
24. Income tax paid.
25. Dividend paid on preferences shares.
26. Under-writing commission paid.
27. Rent paid.
28. Brokerage paid on purchase of non-current investment
29. Bank overdraft
30. Cash credit.
31. Short-term deposit.
32. Marketable securities.
33. Refund of income-tax received.

Hint:

(b) Operating Activities – 3, 6, 7, 10, 13, 15, 19, 20, 23, 24, 27, 33

(c) Investing Activities – 1, 5, 8, 11, 12, 16, 17, 21, 22, 28, 31,

(d) Financing activities – 2, 4, 9, 14, 18, 25, 26, 29, 30,

(e) Cash and Cash equivalent - 32