

MPBSE Class 12th Book Keeping & Accountancy - 2023 Question Paper with Solutions

Time Allowed :3 Hour	Maximum Marks :80	Total Questions :23
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General Instructions

Read the following instructions very carefully and strictly follow them:

1. Attempt all questions.
2. Read the instructions carefully.
3. Marks allotted to each question are indicated against it.

(1) (i) To which activity does the payment of dividend belong?

- (1) Operating activity
- (2) Investing activity
- (3) Financing activity
- (4) Bad debts

Correct Answer: (3) Financing activity

Solution:

The payment of dividends is treated as a financing activity because it involves decisions related to the company's capital structure and distribution of profits to shareholders. Operating activities relate to business operations and investing activities relate to long-term assets. Dividend payment reduces company reserves and affects equity, which falls under financing decisions. Hence, the correct classification is financing activity.

Quick Tip

Dividend payment is always reported under financing activities in cash flow statements.

(1) (ii) Which ratios are primarily measures of return?

- (1) Liquidity
- (2) Activity
- (3) Debt
- (4) Profitability

Correct Answer: (4) Profitability

Solution:

Profitability ratios measure a firm's ability to earn profits from its resources and operations. They include return on equity, net profit ratio and return on capital employed. Liquidity ratios measure short-term obligations, activity ratios measure efficiency and debt ratios measure long-term solvency. Because profitability ratios focus on returns, they are used to judge whether a company is generating adequate earnings relative to sales, assets or capital.

Quick Tip

Profitability ratios measure earnings capacity and overall financial performance.

(1) (iii) Which ratios provide information critical to the long-run operation of the firm?

- (1) Liquidity
- (2) Activity
- (3) Solvency
- (4) Profitability

Correct Answer: (3) Solvency

Solution:

Solvency ratios determine the firm's long-term financial stability and ability to meet future obligations. They include debt-equity ratio, proprietary ratio and interest coverage ratio. Liquidity ratios indicate short-term ability, activity ratios measure efficiency and profitability ratios show earnings. Long-run survival depends on the firm's capacity to repay long-term debts, which is why solvency ratios provide the most critical information for long-term operations.

Quick Tip

Solvency ratios reflect long-term financial strength and debt-paying ability.

(1) (iv) Preparation of financial statements of a company is:

- (1) Voluntary
- (2) Compulsory
- (3) Not essential
- (4) None of these

Correct Answer: (2) Compulsory

Solution:

Under the Companies Act, preparation of financial statements is mandatory for all registered

companies. These statements include the balance sheet, profit and loss account, cash flow statement and explanatory notes. They ensure transparency, accountability and proper reporting to shareholders, creditors and regulatory authorities. Because financial statements are essential for evaluating performance and ensuring compliance, their preparation is compulsory and not optional.

Quick Tip

Financial statements are legally required under the Companies Act.

(1) (v) On admission of a partner, the general reserve in the old balance sheet is transferred to:

- (1) All partners' capital accounts
- (2) New partner's capital account
- (3) Old partners' capital accounts
- (4) None of these

Correct Answer: (3) Old partners' capital accounts

Solution:

General reserve is accumulated profit earned before the new partner joins the firm. Since the new partner did not contribute to earning this profit, he is not entitled to a share in it. Therefore, at the time of admission, the general reserve is credited only to the old partners' capital accounts in their old profit-sharing ratio. This adjustment ensures fairness by giving past profits only to those who earned them.

Quick Tip

General reserve is shared only by old partners in their old ratio.

(1) (vi) Interest on partner's drawings in the absence of a partnership deed is:

- (1) 6%
- (2) 10%
- (3) 8%
- (4) No interest

Correct Answer: (4) No interest

Solution:

According to the Partnership Act, 1932, when there is no written partnership deed, default rules apply. One such rule states that no interest is charged on drawings made by partners.

Interest is only applicable when partners have explicitly agreed on such a clause in a duly prepared deed. Therefore, in the absence of a deed, partners do not pay any interest on drawings.

Quick Tip

Without a deed, no partner is charged interest on drawings.

(2) Fill in the blanks:

- (i) Partnership originates with
- (ii) In fixed capital method, the capital accounts always show balance.
- (iii) Premium brought by new partner is distributed to old partners in ratio.
- (iv) type of goodwill fetches highest value.
- (v) The annual reports of a company are issued to its
- (vi) Common size analysis is also known as analysis.
- (vii) Sale of property is type of activity.

Correct Answer:

- (i) Agreement
- (ii) Fixed
- (iii) Sacrificing
- (iv) Purchased goodwill
- (v) Shareholders
- (vi) Vertical
- (vii) Investing

Solution:

Partnership begins with an agreement because a partnership is created only when two or more persons decide to run a business together with a clear understanding. Under the fixed capital method, capital accounts always maintain a fixed balance, with adjustments made through current accounts. When a new partner brings premium, it compensates old partners for their sacrifice, so it is shared in the sacrificing ratio. Purchased goodwill carries the highest value because it is acquired for consideration. Annual reports are issued to shareholders as they are stakeholders. Common size statements use vertical analysis. Sale of property is an investing activity.

Quick Tip

Remember: sacrificing ratio is always used when new partners bring goodwill; fixed capital never changes.

(3) Match the columns:

A

- (i) Debentureholders
- (ii) Loss on Revaluation
- (iii) Equal profit loss sharing ratio
- (iv) Loan by partner
- (v) Admission of new partner
- (vi) Shareholders

B

- (1) Sacrifice by old partners
- (2) Internal liability
- (3) Creditors of company
- (4) Owners of company
- (5) Dr. side of capital account
- (6) Absence of partnership deed

Correct Answer:

(i)–(3), (ii)–(5), (iii)–(6), (iv)–(2), (v)–(1), (vi)–(4)

Solution:

Debentureholders are lenders of a company who are treated as creditors, so they match with (3). Loss on revaluation is transferred to the debit side of partners' capital accounts because it decreases capital, so it matches with (5). Equal profit and loss sharing ratio applies when there is no partnership deed, thus matching with (6). Loan given by a partner is an internal liability of the firm, hence linked to (2). Admission of a new partner requires old partners to sacrifice part of their share, matching with (1). Shareholders are owners of the company, so they match with (4).

Quick Tip

Always match items based on their fundamental meaning: lenders → creditors, goodwill sacrifice → old partners, and absence of deed → equal sharing.

(4) (i) The return on debentures is called –

Correct Answer:

The return on debentures is called interest.

Solution:

Debentures represent borrowed capital, therefore the company must pay a fixed return known as interest. This payment is compulsory and treated as an expense in the profit and loss account. It is different from dividends because dividends depend on profit availability, but interest must be paid regardless of profit. Debentureholders are creditors, not owners, so their return is a cost of borrowing. Interest ensures that the company compensates them for using their money for business operations. Hence, the return on debentures is always referred to as interest.

Quick Tip

Debentures = borrowed capital; therefore return = interest, not dividend.

(4) (ii) The profit sharing ratio of A, B and C is $\frac{5}{10} : \frac{6}{20} : \frac{4}{20}$. What will be the new profit sharing ratio if C retires?

Correct Answer:

The new profit-sharing ratio of A and B will be 5 : 3.

Solution:

To calculate the new ratio, we remove C's share from the ratio because he will no longer participate in profits. A's share is $\frac{5}{10} = \frac{10}{20}$, and B's share is $\frac{6}{20}$. C's $\frac{4}{20}$ share is removed completely. This leaves A and B with 10 and 6, giving a ratio of 10 : 6. To simplify, divide both by 2, resulting in 5 : 3. This method follows the principle that remaining partners continue with their old shares unless stated otherwise.

Quick Tip

When a partner retires, remove their share and simplify the remaining partners' original shares.

(4) (iii) The change in the value of assets and liabilities on reconstitution is recorded in which account?

Correct Answer:

It is recorded in the Revaluation Account.

Solution:

The Revaluation Account is prepared whenever the partnership is reconstituted due to admission, retirement or death. The purpose is to record the change in values of assets or liabilities so that partners are fairly compensated. If an asset increases in value, the account is credited; if it decreases, the account is debited. Similarly, a decrease in liabilities is credited and an increase is debited. After adjustments, the profit or loss from revaluation is transferred to old partners' capital accounts in their old ratio. This ensures that only those partners who contributed to past profits bear the gain or loss from value changes.

Quick Tip

Revaluation Account records only changes in values during reconstitution—not regular adjustments.

(4) (iv) Which account is also prepared along with capital account in fixed capital method?

Correct Answer:

Along with the capital account, the Current Account is prepared.

Solution:

In the fixed capital method, partners' capital remains constant unless additional capital is introduced or withdrawn. To handle daily or periodic adjustments, a separate account known as the Current Account is prepared. Items like interest on capital, interest on drawings, partners' salary, share of profits, and commission are recorded here. This system maintains clarity by separating long-term capital investments from temporary adjustments. Only permanent changes affect the capital account, while all operational changes affect the current account. This approach ensures systematic recording and proper representation of partners' equity.

Quick Tip

Fixed capital method = fixed capital account + separate current account.

(4) (v) How much interest is payable on the loan of a partner in the absence of partnership deed?

Correct Answer:

In the absence of a partnership deed, interest payable on a partner's loan is 6% per annum.

Solution:

The Indian Partnership Act, 1932 defines several default rules which automatically apply when there is no written deed. One such rule specifies that if a partner gives a loan to the firm separate from his capital, he is entitled to an interest at 6% per annum. This interest is a priority payment and must be given even if the partnership makes a loss. The Act ensures fairness by compensating partners who extend financial support to the firm. All other interest-related matters, like interest on capital or drawings, depend on the deed, but interest on loan always defaults to 6

Quick Tip

Without a deed, partner's loan always earns 6

(4) (vi) On the death of a partner, his claim is transferred to which account?

Correct Answer:

On the death of a partner, his claim is transferred to the Executor's Account.

Solution:

When a partner dies, his capital account must be settled by paying all amounts due to him. These include his capital balance, share of profits up to the date of death, interest on capital, share in reserves and goodwill entitlement. To record this liability properly, the amount due is transferred from the deceased partner's capital account to the Executor's Account. This ensures that the firm recognizes the legal representative who will receive the settlement. The

executor's account is then paid off either immediately or in installments depending on agreement. This process ensures fairness and legal compliance.

Quick Tip

Executor's Account represents the deceased partner's legal heir for settlement.

(4) (vii) The balance of share forfeiture account is transferred to which account?

Correct Answer:

The balance of the Share Forfeiture Account is transferred to Capital Reserve.

Solution:

When shares are forfeited, the amount already received from defaulting shareholders is transferred to the Share Forfeiture Account. After the forfeited shares are reissued, any remaining balance that the company retains becomes a capital profit. Since this profit arises from a capital transaction and not business operations, it cannot be distributed as dividends. Therefore, it is transferred to the Capital Reserve. This reserve strengthens the company's financial position and is used for specific purposes such as issuing bonus shares or writing off capital losses. Hence, Capital Reserve is the correct destination for the forfeiture balance.

Quick Tip

Share Forfeiture leftover → Capital Reserve (capital profit, not revenue profit).

(5) (i) Bank overdraft is transferred to Bank account on the dissolution of a firm.

Correct Answer: False

Solution:

A bank overdraft is a liability and therefore it is not transferred to the bank account at dissolution. Instead, all liabilities, including bank overdraft, are transferred to the Realisation Account. The liability is settled by paying the overdraft amount through the bank account. Only cash and bank balances are transferred to the Realisation Account on dissolution. Since the overdraft represents money owed to the bank, it cannot be transferred into the bank account itself; it must be paid off during settlement.

Quick Tip

Overdraft is a liability → goes to Realisation Account, not Bank Account.

(5) (ii) Paid-up capital can exceed called-up capital.

Correct Answer: False

Solution:

Called-up capital is the amount demanded by the company from shareholders, while paid-up capital is the amount actually received. Shareholders can never pay more than what the company has called for; they can either pay the full called amount or default partially. Therefore, paid-up capital can be equal to or less than called-up capital but never more. This makes the given statement false as it is legally and logically impossible for paid-up capital to exceed the called amount.

Quick Tip

Paid-up capital Called-up capital — never greater.

(5) (iii) Capital Reserves are created from Capital Profits.

Correct Answer: True

Solution:

Capital reserves arise from capital profits such as premium on issue of shares, profit on forfeiture of shares, profit prior to incorporation, and gains on revaluation. These profits come from non-operational activities and therefore cannot be distributed as dividends. Instead, they are transferred to the Capital Reserve for strengthening financial stability or issuing bonus shares. Revenue profits, on the other hand, go to the Profit and Loss Account. Hence, the statement is true because capital reserves are indeed created from capital profits.

Quick Tip

Capital Reserve comes only from capital profits, not trading income.

(5) (iv) Proposed dividend is shown as contingent liability.

Correct Answer: False

Solution:

Proposed dividend becomes a definite obligation once recommended by the board of directors, and therefore it is recorded under “Short-term Provisions.” Contingent liabilities depend on uncertain future events such as legal disputes or guarantees. Proposed dividend does not depend on uncertainty; it is payable to shareholders unless the company withdraws the proposal before approval. As per accounting standards, proposed dividend is a provision, not a contingent liability.

Quick Tip

Proposed dividend = provision, not a contingent liability.

(5) (v) The financial statements of a business include Cash Flow Statement.

Correct Answer: True

Solution:

A complete set of financial statements includes the balance sheet, profit and loss account, and cash flow statement. The cash flow statement is essential as it records cash inflows and outflows under operating, investing, and financing activities. Accounting standards require companies to prepare it to provide transparency about liquidity and financial health. It helps investors and stakeholders understand how cash is generated and used by the business. Therefore, it is rightly considered part of financial statements.

Quick Tip

Cash flow statement = mandatory part of modern financial reporting.

(5) (vi) Debenture is a part of owned capital.

Correct Answer: False

Solution:

Owned capital refers to funds provided by shareholders such as share capital and reserves. Debentures, however, are borrowed funds raised from creditors. Debentureholders receive fixed interest and repayment of principal, but they do not hold ownership rights. They are lenders and not owners. Therefore, debentures form part of borrowed capital, not owned capital. Companies must repay debentures regardless of profit, which distinguishes them further from owner-based funds.

Quick Tip

Debentures = borrowed capital; shareholders = owned capital.

(6) What is partnership deed?

Solution:

A partnership deed is a written legal document that contains the terms and conditions agreed

upon by all partners of a firm. It clearly defines the rights, duties, responsibilities and profit-sharing arrangements among partners. The deed helps in avoiding disputes by providing clarity on important matters such as capital contributions, interest on capital, loan terms, salary, admission or retirement of partners, and settlement procedures. It acts as evidence in case of disagreements and ensures smooth functioning of the partnership. A written deed is always preferable to avoid misunderstandings and to maintain transparency in the business.

Quick Tip

A partnership deed protects partners by clearly defining rights, duties and profit-sharing rules.

(6) Write any two characteristics of partnership.

Solution:

A partnership includes several important characteristics. First, it is formed by an agreement between two or more persons who agree to share profits and losses of a business. Second, partners contribute capital and participate in management according to the terms of the agreement. Third, the business is based on mutual trust and cooperation among partners. Fourth, liability of partners is generally unlimited, meaning partners are personally responsible for debts of the firm. Any two of these characteristics explain the essential nature of a partnership and show how partners work together to operate the business effectively.

Quick Tip

Remember: partnership is formed by agreement and involves sharing of profits and responsibilities.

(7) Write any two circumstances when a court can issue order for dissolution of a firm.

Solution:

A court may order dissolution of a firm under several circumstances. First, when a partner becomes permanently incapable of performing his duties due to illness, insanity or disability, dissolution may be granted. Second, if a partner is guilty of misconduct that negatively affects the business, the court may intervene. Third, if a partner continuously breaches the partnership agreement or acts in a manner that makes business operations impossible, dissolution can be ordered. Fourth, continued losses or the business becoming illegal may also lead the court to dissolve the firm. Any two of these situations are acceptable.

Quick Tip

Courts dissolve firms mainly due to incapacity, misconduct, breach or impracticability.

(7) Write any two circumstances for compulsory dissolution of a firm.

Solution:

Compulsory dissolution occurs automatically when certain events take place. First, if all or all except one partner become insolvent, the firm must be dissolved because the business cannot continue. Second, if the business becomes illegal due to changes in law, such as banning a particular trade, compulsory dissolution is required. Third, if an event occurs that makes the business impossible to carry on, such as destruction of essential assets, the firm must be dissolved. These circumstances do not require a court order, as dissolution happens by force of law. Any two such conditions are sufficient.

Quick Tip

Compulsory dissolution happens automatically due to insolvency or illegality.

(8) Anu, Vanu and Tanu are partners in the ratio of 4 : 3 : 2. Anu retires. Vanu and Tanu decide to share future profits in the ratio of 5 : 3. Calculate Gaining Ratio.

Solution:

Old ratio of Anu, Vanu and Tanu is 4 : 3 : 2. When Anu retires, her share is 4 parts out of 9 total parts. Vanu and Tanu's old shares are $\frac{3}{9}$ and $\frac{2}{9}$ respectively. Their new ratio is 5 : 3, which means Vanu receives $\frac{5}{8}$ and Tanu receives $\frac{3}{8}$. To calculate the gaining ratio, we find the difference between new share and old share. Vanu's gain is $\frac{5}{8}$ minus $\frac{3}{9}$ and Tanu's gain is $\frac{3}{8}$ minus $\frac{2}{9}$. After calculating the values, their gains simplify to $\frac{27}{72}$ for Vanu and $\frac{13}{72}$ for Tanu, giving a gaining ratio of 27 : 13. This ratio shows how much of Anu's share is gained individually by Vanu and Tanu.

Quick Tip

Gaining Ratio = New Share – Old Share for each continuing partner.

(8) X, Y and Z are partners in the ratio of 3 : 2 : 1. X retires and his share is taken up by Y and Z in the ratio of 3 : 2. Calculate new profit sharing ratio.

Solution:

The old ratio of X, Y and Z is 3 : 2 : 1. Total share is 6 parts. X's share is $\frac{3}{6}$. Y and Z take

this share in the ratio of 3 : 2. Therefore, Y gets $\frac{3}{5}$ of X's share which equals $\frac{3}{6} \times \frac{3}{5} = \frac{9}{30}$. Z gets $\frac{2}{5}$ of X's share which equals $\frac{3}{6} \times \frac{2}{5} = \frac{6}{30}$. Their old shares were $Y = \frac{2}{6}$ and $Z = \frac{1}{6}$. Adding the gained shares, Y becomes $\frac{2}{6} + \frac{9}{30}$ and Z becomes $\frac{1}{6} + \frac{6}{30}$. After converting to a common denominator and simplifying, the new ratio of Y and Z becomes 19 : 11. This ratio represents how they will share profits after X's retirement.

Quick Tip

New Ratio = Old Share + Acquired Share from retiring partner.

(9) Explain types of debentures from the point of view of convertibility.

Solution:

From the point of view of convertibility, debentures are classified into two main types. The first type is convertible debentures. These debentures can be converted into shares of the company after a specified period, either fully or partially. Their conversion terms are stated at the time of issue, and conversion gives the investor an opportunity to become a shareholder. The second type is non-convertible debentures. These cannot be converted into shares and remain a debt instrument until maturity. Non-convertible debentures usually offer a higher rate of interest because they lack the benefit of conversion. These two types provide companies and investors with flexible financing and investment options.

Quick Tip

Convertible = can turn into shares; Non-convertible = remain debt until maturity.

(9) Explain types of debentures from the point of view of security.

Solution:

From the security point of view, debentures are classified into two categories. The first type is secured debentures. These debentures are backed by a charge on the company's assets, which may be fixed or floating. If the company fails to pay interest or principal, debentureholders can claim the secured assets. The second type is unsecured debentures, also known as naked or simple debentures. These do not carry any charge on assets and rely entirely on the creditworthiness and reputation of the company. Because unsecured debentures carry higher risk, they generally offer a higher rate of interest to attract investors. Both types help companies raise long-term funds based on their financial strength and security structure.

Quick Tip

Secured = backed by assets; Unsecured = no asset security, higher risk.

(10) What is meant by Authorised Capital?

Solution:

Authorised capital refers to the maximum amount of share capital that a company is legally permitted to raise by issuing shares, as stated in its Memorandum of Association. It represents the upper limit of capital that the company can call from shareholders. A company cannot issue shares beyond this limit unless it amends its memorandum by following legal procedures. Authorised capital is divided into different classes of shares with specified nominal values. Although a company may not issue all of its authorised capital immediately, it provides flexibility for future expansion. It helps determine the company's overall financial capacity and borrowing power, as lenders often consider authorised capital as an indicator of financial strength.

Quick Tip

Authorised capital = maximum capital a company is allowed to issue legally.

(10) What is Un-called Capital?

Solution:

Un-called capital is the portion of subscribed share capital that the company has not yet demanded from shareholders. When shares are issued, shareholders agree to pay the full nominal value, but the company may choose to call for this amount in instalments. The part that remains unpaid because the company has not yet asked for it is known as un-called capital. It remains a liability for shareholders because they must pay it whenever the company demands. Un-called capital provides financial flexibility to the company, as it can call the remaining amount in the future to meet financial needs. It is different from calls in arrears, which refer to unpaid amounts that were already demanded.

Quick Tip

Un-called capital = amount not yet demanded from shareholders but still payable.

(11) Write two characteristics of Preference Shares.

Solution:

Preference shares have certain special characteristics that distinguish them from equity shares. First, preference shareholders receive a fixed rate of dividend before any dividend is paid to equity shareholders. This ensures priority in the distribution of profits. Second, in case the company is wound up, preference shareholders get repayment of capital before equity shareholders, giving them greater security. Preference shares may also carry cumulative or non-cumulative rights, meaning unpaid dividends may or may not accumulate. They may be redeemable or

convertible depending on the company's terms. These characteristics make preference shares a hybrid form of financing with both equity and debt features.

Quick Tip

Preference shareholders get priority in dividends and repayment during liquidation.

(11) What is meant by Share Capital?

Solution:

Share capital refers to the total amount of money raised by a company through the issue of shares to shareholders. It represents the ownership interest of members in the company and forms the main source of long-term finance. When individuals purchase shares, they contribute funds to the company, which can be used for expansion, operations or investment. Share capital may be classified into authorised, issued, subscribed, called-up and paid-up capital, depending on how much the company is permitted to raise and how much has been actually received. Share capital gives shareholders voting rights, dividend entitlement and a share in the company's assets at the time of winding up.

Quick Tip

Share capital = funds raised by issuing shares; represents ownership in the company.

(12) What is meant by Forfeiture of Shares?

Solution:

Forfeiture of shares refers to the cancellation of shares by a company when a shareholder fails to pay the allotment money or subsequent calls within the specified time. When the company issues a notice demanding payment and the shareholder still does not comply, the company has the right to forfeit those shares. Once forfeited, the shareholder loses ownership rights, voting rights and any amount already paid on those shares. The forfeited amount becomes a capital profit for the company and may later be transferred to the Capital Reserve after reissue. Forfeiture ensures discipline among shareholders and protects the company from non-payment issues.

Quick Tip

Forfeiture = cancellation of shares due to non-payment of calls.

(12) Which are two options available with the company in the condition of Over-subscription? Write.

Solution:

When a company receives more applications than the number of shares offered, it faces over-subscription. In such cases, the company has two main options. First, it may adopt the rejection method, where excess applications are completely rejected and application money is refunded. Second, it may use the pro-rata allotment method, where shares are allotted proportionately to applicants based on the number of applications received. Under this method, applicants receive fewer shares than they applied for, and excess application money is either refunded or adjusted towards allotment or call money. These options help the company manage excess demand fairly and maintain transparency in the allotment process.

Quick Tip

Over-subscription options: Rejection method or Pro-rata allotment.

(13) Shree Ltd. purchased a machine worth Rs. 3,80,000 from Heavy Machine Ltd. As per the purchase agreement, Rs. 20,000 were paid in cash and the balance was settled by issuing shares of Rs. 100 each. Give necessary journal entries in the books of Shree Ltd.

Solution:

When Shree Ltd. purchases a machine worth Rs. 3,80,000, it becomes a capital asset for the company. As per the agreement, Rs. 20,000 is paid in cash and the remaining Rs. 3,60,000 is discharged by issuing equity shares of Rs. 100 each. Therefore, 3,600 shares will be issued. The journal entries are as follows. First, the Machine Account is debited with Rs. 3,80,000 to record the asset. Heavy Machine Ltd. is credited with the same amount to recognise the liability. Then, Cash Account is credited with Rs. 20,000 for the cash payment, and Share Capital Account is credited with Rs. 3,60,000 to record the issue of shares. After these entries, the liability to Heavy Machine Ltd. becomes fully settled.

Quick Tip

When assets are purchased partly for cash and partly by shares, debit the asset and credit cash and share capital.

(13) ABC Ltd. purchased a building worth Rs. 5,40,000 from XYZ Ltd. and the payment was made by the issue of shares of Rs. 100 each issued at 20% premium. Give necessary journal entries in the books of ABC Ltd.

Solution:

ABC Ltd. acquired a building worth Rs. 5,40,000 from XYZ Ltd. and settled the payment by issuing shares of Rs. 100 each at a premium of 20 percent. This means each share is issued at Rs. 120, consisting of Rs. 100 face value and Rs. 20 premium. The number of shares issued will be 5,40,000 divided by 120, giving 4,500 shares. The Building Account is debited with

Rs. 5,40,000 to record the asset. XYZ Ltd. is credited with the same amount to recognise the liability. Then, Share Capital Account is credited with Rs. 4,50,000 ($4,500 \times 100$), and Securities Premium Account is credited with Rs. 90,000 ($4,500 \times 20$). These entries completely settle the amount payable to XYZ Ltd. and properly reflect capital raised with premium.

Quick Tip

When shares are issued at premium, credit share capital with face value and securities premium with excess amount.

(14) Write two objectives of Ratio Analysis.

Answer:

1. To evaluate the financial performance of a business.
2. To assess the financial position and stability of the firm.

Solution:

Ratio analysis helps in understanding the financial condition of a business by comparing different financial figures from the statements. One important objective is to evaluate the profitability, liquidity, solvency and efficiency of the firm through meaningful ratios. This helps management and stakeholders understand how effectively resources are being used. Another objective is to assist in decision making by highlighting strengths and weaknesses in financial performance. Ratios allow comparison over time and with other firms in the industry, helping identify trends and areas requiring improvement. By simplifying complex financial data into simple numerical indicators, ratio analysis becomes a useful tool for planning, forecasting and evaluating overall business health.

Quick Tip

Ratio analysis makes financial statements easier to interpret by converting raw numbers into meaningful relationships.

(14) Write two limitations of Ratio Analysis.

Answer:

1. Ratios are based on historical data.
2. Ratios may give misleading results if financial statements contain errors.

Solution:

While ratio analysis is useful, it also has several limitations. Since ratios are calculated from past financial statements, they reflect historical conditions and may not represent the current or future financial performance of the business. Moreover, ratios can become misleading if the underlying accounting data contains inaccuracies, manipulations or inconsistencies. Another

limitation is that ratios do not consider qualitative factors such as management efficiency, economic conditions or market competition. Industry norms also vary widely, making comparisons difficult. Inflation can distort financial values as well, reducing the reliability of ratios over time. Overall, ratios should be used carefully along with other financial and non-financial information for accurate interpretation.

Quick Tip

Ratios are helpful indicators but must always be interpreted along with qualitative and contextual information.

(15) What is meant by 'Cash Equivalents'?

Answer:

Cash equivalents are short-term, highly liquid investments that can be easily converted into cash.

Solution:

Cash equivalents refer to very short-term investments that a business holds for meeting its immediate cash obligations. These investments are highly liquid, meaning they can be converted into cash quickly without any significant loss of value. Typically, cash equivalents have a maturity period of three months or less from the date of acquisition. Examples include Treasury bills, commercial papers and money market instruments. The purpose of holding such assets is to ensure sufficient liquidity while earning small returns on idle cash. Cash equivalents form an essential part of cash and cash equivalents in the balance sheet and help a business manage its daily financial requirements efficiently. They are considered nearly as good as cash due to their stability and low risk.

Quick Tip

Cash equivalents must be highly liquid and carry insignificant risk of value change.

(15) Write two examples of cash inflows by financing activities.

Answer:

1. Issue of shares.
2. Issue of debentures or raising long-term loans.

Solution:

Financing activities are those business transactions that affect the long-term liabilities and owners' equity of a company. Cash inflows from financing activities arise when a company raises funds to support its operations or growth. One major example is the issue of shares, where the company receives cash from investors in exchange for ownership rights. Another

example is the issue of debentures or raising long-term loans from financial institutions, which brings additional funds into the business. These inflows increase the financial strength of the organisation and help finance expansion, asset purchases or other long-term projects. Cash flow from financing activities is an important part of the cash flow statement as it shows how the company obtains long-term funds to support its strategic objectives.

Quick Tip

Financing inflows mainly include issuing shares, raising loans and issuing debentures.

(16) (i) Anshi and Ayushi are partners in the ratio of 3 : 2. They admit Aman for 3/10 share which he acquired 2/10 from Anshi and 1/10 from Ayushi. Calculate new profit sharing ratio.

Answer:

New Ratio = Anshi $1/10$: Ayushi $9/30$: Aman $3/10$

Solution:

The old profit sharing ratio of Anshi and Ayushi is 3 : 2. Aman is admitted for $3/10$ share, which he receives by sacrificing $2/10$ from Anshi and $1/10$ from Ayushi.

To find the new ratio, we subtract the sacrificed portions from the original shares. Anshi's old share is $3/5$ and Ayushi's old share is $2/5$. When we deduct the sacrifice of $2/10$ from Anshi's share, her new share becomes $3/5 - 2/10 = 6/10 - 2/10 = 4/10$.

Similarly, Ayushi's new share becomes $2/5 - 1/10 = 4/10 - 1/10 = 3/10$. Aman's admitted share is already given as $3/10$. Therefore, the new ratio becomes Anshi $4/10$: Ayushi $3/10$: Aman $3/10$.

For simplification, we may convert to a common denominator or leave as fractions. Thus, the final new profit sharing ratio is $4/10$: $3/10$: $3/10$.

Quick Tip

Always subtract the sacrifice from old shares, then express all partners' shares together as the new ratio.

(16) (ii) A business has earned average profits of Rs. 1,00,000 during the last few years and the normal rate of return in similar business is 10%. If the total assets of the business are Rs. 10,00,000 and external liabilities are Rs. 1,80,000, calculate goodwill by the Capitalisation of Super Profits Method.

Answer:

Goodwill = Rs. 2,00,000

Solution:

In the capitalisation of super profits method, goodwill is calculated by capitalising the super profits at the normal rate of return. The first step is to compute the capital employed. Capital employed is equal to total assets minus external liabilities.

Here, total assets are Rs. 10,00,000 and external liabilities are Rs. 1,80,000. Therefore, capital employed becomes Rs. 10,00,000 – Rs. 1,80,000 = Rs. 8,20,000.

Next, we calculate the normal profit by applying the normal rate of return. Normal profit = 10% of capital employed = 10% of Rs. 8,20,000 = Rs. 82,000. Super profit is the excess of actual average profit over normal profit.

Since the actual average profit is Rs. 1,00,000, super profit equals Rs. 1,00,000 – Rs. 82,000 = Rs. 18,000.

Finally, goodwill is found by capitalising the super profit at the normal rate of return using the formula: Goodwill = Super Profit $\times$ 100 / Normal Rate.

Hence, Goodwill = 18,000 $\times$ 100 / 10 = Rs. 1,80,000.

Quick Tip

Under this method, goodwill depends entirely on extra profits earned above the normal expected return.

17.

Vimal and Nirmal are partners in the ratio of 3 : 2. They admit Sushil for $\frac{1}{3}$ share. Sushil brings Rs. 30,000 for his capital and also brings necessary amount of his share of goodwill in cash. On the date of admission, the goodwill of the firm is valued at Rs. 24,000. Goodwill already appears in the books at Rs. 12,000. Give necessary journal entries in the books of the firm.

Correct Answer: Journal entries for writing off old goodwill, goodwill brought in by Sushil, and capital introduced.

Solution:

Goodwill of the firm is Rs. 24,000 and goodwill already appearing in the books is Rs. 12,000. The old goodwill must be written off between Vimal and Nirmal in the old ratio of 3 : 2. Sushil's share of goodwill is $\frac{1}{3} \times 24,000 = 8,000$, which he brings in cash. This Rs. 8,000 is credited to Vimal and Nirmal in the old ratio of 3 : 2. Sushil also brings Rs. 30,000 for capital. All entries below represent correct accounting treatment.

Journal Entries:

Vimal's Capital A/c Dr.	7, 200
Nirmal's Capital A/c Dr.	4, 800
To Goodwill A/c	12, 000
(Old goodwill written off in old ratio 3:2)	
Bank A/c Dr.	30, 000
To Sushil's Capital A/c	30, 000
(Capital brought in by Sushil)	
Bank A/c Dr.	8, 000
To Vimal's Capital A/c	4, 800
To Nirmal's Capital A/c	3, 200
(Goodwill brought in by Sushil credited in 3:2 ratio)	

Quick Tip

Always write off existing goodwill before adjusting new goodwill brought in by an incoming partner.

17. (OR)

Sonu and Sandeep are partners in the ratio of 3 : 2. They admit Neeraj for $\frac{1}{3}$ share in profits. Neeraj brings Rs. 30,000 for his capital but fails to bring his share of goodwill in cash. The goodwill of the firm is valued at Rs. 9,000. Give necessary journal entries.

Correct Answer: Journal entries for capital introduction and adjustment of Neeraj's unpaid goodwill through capital account.

Solution:

Goodwill of the firm is Rs. 9,000. Neeraj's share of goodwill equals $\frac{1}{3} \times 9,000 = 3,000$. Since Neeraj does not bring his share of goodwill in cash, his capital account is debited for Rs. 3,000 and credited to Sonu and Sandeep in the old ratio of 3 : 2. Neeraj brings Rs. 30,000 as capital which is credited normally. The firm does not raise goodwill account; instead, goodwill is adjusted through partners' capital accounts. Journal entries are given below.

Journal Entries:

Bank A/c Dr.	30, 000
To Neeraj's Capital A/c	30, 000
(Capital brought in by Neeraj)	
Neeraj's Capital A/c Dr.	3, 000
To Sonu's Capital A/c	1, 800
To Sandeep's Capital A/c	1, 200
(Goodwill adjusted in old ratio 3:2 since Neeraj did not bring goodwill)	

Quick Tip

If goodwill is not brought in by the new partner, it must be adjusted through the new partner's capital account.

18.

What are Bearer Debentures?

Correct Answer: Bearer debentures are debentures that are transferable by delivery and payable to the holder without any name being recorded in the company register.

Solution:

Bearer debentures are negotiable instruments that do not include the name of the owner on the certificate. The person who physically holds the debenture certificate is considered the legal owner. These debentures can be transferred simply by handing over the certificate, without any formal transfer procedure. Interest on bearer debentures is paid to the holder who presents the attached interest coupon. They offer convenience and anonymity to investors but also involve higher risk of loss or misuse due to their bearer nature.

Quick Tip

Bearer debentures work like cash instruments—ownership passes through physical possession only.

18. (OR)

Shreyas Ltd. issued 10,000 debentures of Rs. 100 each. The public applied for 9,000 debentures which were fully allotted. All the money was received in lump-sum. Give necessary journal entries in the books of Shreyas Ltd.

Correct Answer: Journal entry for receipt of money and issue of 9,000 debentures at par in a single lump-sum.

Solution:

Shreyas Ltd. issued 10,000 debentures, but the public applied for only 9,000 debentures. Since applications matched the allotment, all 9,000 debentures were allotted. The debentures were issued at face value of Rs. 100 each and the entire amount was received in one lump-sum. The total money received equals $9,000 \times 100 = \text{Rs. } 9,00,000$. As there were no stages of application, allotment or calls, the company passes only one journal entry: receipt of cash and issue of debentures. The debentures account is credited to record liability.

Journal Entry:

Bank A/c Dr.	9,00,000
To Debentures A/c	9,00,000
(Money received for 9,000 debentures issued at Rs. 100 each)	

Quick Tip

When full debenture money is received in one lump-sum, only a single journal entry is required: Bank A/c Dr. to Debentures A/c.

20.

Akshay, Bhanu and Chakresh established a partnership firm on 01 April 2016 by investing Rs. 5,00,000, Rs. 4,00,000 and Rs. 3,00,000 as capital. Additional information: (i) Profit sharing ratio 3 : 2 : 1, (ii) 6% interest on capital, (iii) Akshay salary Rs. 1,20,000, (iv) Bhanu commission Rs. 50,000, (v) Drawings: Akshay Rs. 60,000, Bhanu Rs. 40,000, Chakresh Rs. 20,000, (vi) Interest on drawings: Akshay Rs. 2,700, Bhanu Rs. 1,800, Chakresh Rs. 900. Net Profit for the year was Rs. 3,56,600. Prepare Profit and Loss Appropriation Account.

Correct Answer: Profit and Loss Appropriation Account showing interest on capital, salary, commission, interest on drawings and distribution of profits.

Solution:

Interest on capital: Akshay 30,000, Bhanu 24,000, Chakresh 18,000. Salary to Akshay is 1,20,000 and commission to Bhanu is 50,000. Interest on drawings is added back: $2,700 + 1,800 + 900 = 5,400$. Adjusted profit becomes $3,56,600 + 5,400 = 3,62,000$. After deducting interest on capital, salary and commission ($30,000 + 24,000 + 18,000 + 1,20,000 + 50,000 = 2,42,000$), the remaining profit is 1,20,000. This is distributed in ratio 3 : 2 : 1 as: Akshay 60,000; Bhanu 40,000; Chakresh 20,000.

Profit & Loss Appropriation Account

Dr.	Amount (Rs.)	Cr.	Amount (Rs.)
To Interest on Capital:		By Net Profit	3,56,600
Akshay	30,000	By Interest on Drawings	5,400
Bhanu	24,000		
Chakresh	18,000		
To Salary (Akshay)	1,20,000		
To Commission (Bhanu)	50,000		
To Profit transferred to:			
Akshay	60,000		
Bhanu	40,000		
Chakresh	20,000		
Total	3,62,000	Total	3,62,000

20. (OR)

Amit and Babu are partners in the ratio of 3 : 2. They admit Charu for $\frac{1}{6}$ share. Interest on capital @ 6% p.a. Amit guarantees that Charu's profit after interest on capital will not be less than Rs. 30,000. Capitals: Amit Rs. 2,50,000, Babu Rs. 2,00,000, Charu Rs. 1,50,000. Profit before interest on capital Rs. 1,50,000. Prepare Profit and Loss Appropriation Account (New Ratio 3 : 2 : 1).

Correct Answer: Profit and Loss Appropriation Account with interest on capital, guaranteed profit to Charu and adjustment from Amit's share.

Solution:

Interest on capital @ 6%: Amit 15,000; Babu 12,000; Charu 9,000. Profit before interest is 1,50,000, so profit after interest becomes: 1,50,000 - 36,000 = 1,14,000. Charu must receive at least 30,000; her normal share in new ratio 3 : 2 : 1 is $1,14,000 \times \frac{1}{6} = 19,000$. Guarantee shortfall = 30,000 - 19,000 = 11,000, which Amit must bear. Hence Amit's share is reduced by 11,000 and added to Charu. Final distribution: Amit 57,000 - 11,000 = 46,000; Babu 38,000; Charu 30,000.

Profit & Loss Appropriation Account

Dr.	Amount (Rs.)	Cr.	Amount (Rs.)
To Interest on Capital:		By Profit before IOC	1, 50, 000
Amit	15, 000		
Babu	12, 000		
Charu	9, 000		
To Profit transferred to:			
Amit	46, 000		
Babu	38, 000		
Charu (Guaranteed)	30, 000		
Total	1, 50, 000	Total	1, 50, 000

21.

Ajeet, Mahesh and Sujeet are partners. Mahesh retires from the firm. On that date, Rs. 6,00,000 are payable to him. The amount due to Mahesh will be paid in four yearly instalments with interest @ 12% p.a. on the unpaid balance. Prepare Mahesh's Loan Account.

Correct Answer: Mahesh's Loan Account showing yearly instalments, interest on unpaid balance and closing balance every year.

Solution:

Mahesh is owed Rs. 6,00,000 on the date of retirement. This amount is to be paid in four equal annual instalments. Instalment per year = $6,00,000 \div 4 = 1,50,000$. Interest is charged at 12% p.a. on the balance outstanding at the beginning of each year. Interest is added to the balance, and then the instalment is deducted. The loan account below shows interest each

year, the amount paid, and the remaining balance.

Mahesh's Loan Account

Year	Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
1	To Bank A/c (Instalment)	1,50,000	By Balance b/d	6,00,000
	To Bank A/c (Interest)	72,000	(12% of 6,00,000)	
			By Interest	72,000
	Balance c/d		4,50,000	
2	To Bank A/c (Instalment)	1,50,000	By Balance b/d	4,50,000
	To Bank A/c (Interest)	54,000	(12% of 4,50,000)	
			By Interest	54,000
	Balance c/d		3,00,000	
3	To Bank A/c (Instalment)	1,50,000	By Balance b/d	3,00,000
	To Bank A/c (Interest)	36,000	(12% of 3,00,000)	
			By Interest	36,000
	Balance c/d		1,50,000	
4	To Bank A/c (Instalment)	1,50,000	By Balance b/d	1,50,000
	To Bank A/c (Interest)	18,000	(12% of 1,50,000)	
			By Interest	18,000
	Balance c/d	0	0	

Quick Tip

Interest on a retiring partner's loan is always calculated on the outstanding balance at the beginning of the year.

21. (OR)

Write journal entries for the revaluation of assets and liabilities and for adjustment of profit/loss on the Revaluation.

Correct Answer: Journal entries for increase/decrease in assets and liabilities and transfer of profit or loss on revaluation to partners' capital accounts.

Solution:

Revaluation is done when a partner retires, is admitted, or there is a change in profit-sharing ratio. Increase in asset value or decrease in liability value results in profit, while decrease in asset value or increase in liability value results in loss. Profit or loss from revaluation is transferred to partners' capital accounts in their old ratio. The common journal entries are provided below.

Journal Entries for Revaluation

1. Increase in Asset:	
Asset A/c Dr.	xxx
To Revaluation A/c	xxx
2. Decrease in Asset:	
Revaluation A/c Dr.	xxx
To Asset A/c	xxx
3. Increase in Liability:	
Revaluation A/c Dr.	xxx
To Liability A/c	xxx
4. Decrease in Liability:	
Liability A/c Dr.	xxx
To Revaluation A/c	xxx
5. Transfer of Profit on Revaluation:	
Revaluation A/c Dr.	xxx
To Partners' Capital A/c (Old Ratio)	xxx
6. Transfer of Loss on Revaluation:	
Partners' Capital A/c Dr. (Old Ratio)	xxx
To Revaluation A/c	xxx

Quick Tip

Revaluation profit or loss must always be shared in the old ratio, not the new ratio.

22.

Surabhi, a shareholder holding 5,000 shares of Rs. 10 each, did not pay the allotment money of Rs. 4 per share (including premium of Rs. 2) and the first and final call of Rs. 3 per share. Her shares were forfeited after first and final call. Give journal entry for forfeiture of shares.

Correct Answer: Share Forfeiture entry debiting Share Capital and crediting Securities Premium Forfeited and Calls in Arrears.

Solution:

Surabhi failed to pay allotment money (including premium) and first final call. The total unpaid amount per share is Rs. 4 (allotment) + Rs. 3 (call) = Rs. 7. When shares are forfeited, the called-up capital is cancelled. Since premium was not received, it must be reversed. Amount received on application remains in share forfeiture account. The journal entry is recorded as follows:

Journal Entry for Forfeiture of Shares

Called-up capital = Application Rs. 3 + Allotment Rs. 4 + Call Rs. 3 = Rs. 10 per share.
 Share capital to be cancelled = $5,000 \times 10 = \text{Rs. } 50,000$.
 Premium not received = $5,000 \times 2 = \text{Rs. } 10,000$.
 Calls unpaid = $5,000 \times 7 = \text{Rs. } 35,000$.
 Amount received (application) = $5,000 \times 3 = \text{Rs. } 15,000$ (credited to Forfeiture A/c).

Share Capital A/c Dr.	50,000
Securities Premium A/c Dr.	10,000
To Calls in Arrears A/c	35,000
To Share Forfeiture A/c	15,000

Quick Tip

When premium is unpaid at allotment, it must always be cancelled on forfeiture.

22. (OR)

Write the uses of securities premium received on shares.

Correct Answer: Securities premium can be used for purposes permitted under Section 52 of Companies Act.

Solution:

Securities premium arises when shares are issued at a price higher than their face value. This amount is kept in the Securities Premium Reserve and can be used only for specific statutory purposes. The important uses are as follows:

1. Issue of fully paid bonus shares to shareholders.
2. Writing off preliminary expenses of the company.
3. Writing off discount or commission on issue of shares or debentures.
4. Providing premium payable on the redemption of preference shares or debentures.

Quick Tip

Securities premium cannot be used for paying dividends because it is a capital profit, not a revenue profit.

23.

Write any four advantages of preparing Cash Flow Statement.

Correct Answer: Cash flow statement helps in assessing liquidity, financial planning, cash management and short-term decision-making.

Solution:

A cash flow statement provides important information about actual cash generated and used by a business. Its advantages include:

1. Helps assess short-term liquidity position by showing availability of cash to meet obligations.
2. Assists in financial planning by revealing future cash requirements and sources.
3. Helps evaluate operating efficiency by identifying cash flows from core business activities.
4. Facilitates decision-making on investments, financing and dividend policies by showing real cash movements.

Quick Tip

Cash Flow Statement shows actual cash movement and is more reliable than profit figures for analysing liquidity.

23. (OR)

Write examples of cash inflows and outflows from Investing activities.

Correct Answer: Inflow examples include sale of fixed assets; outflow examples include purchase of fixed assets.

Solution:

Investing activities relate to the purchase and sale of long-term assets. Cash inflows from investing activities include:

1. Cash received from sale of land, building or machinery.
2. Cash received from sale of investments (such as shares or debentures).

Cash outflows from investing activities include:

1. Cash paid for purchase of fixed assets such as plant, equipment or furniture.
2. Cash paid for purchasing long-term investments.

Quick Tip

Investing activities always relate to long-term assets, not day-to-day working capital items.