UP Board Class 12 Accountancy - 349, 2023 Question Paper with Solutions

Time Allowed :3 Hours	Maximum Marks :100	Total Questions :30

General Instructions

Read the following instructions very carefully and strictly follow them:

1. There are in all nine questions in this question paper.
2. All questions are compulsory.
3. In the beginning of each question, the number of parts to be attempted are clearly mentioned.
4. Marks allotted to the questions are indicated against them.
5. Start solving from the first question and proceed to solve till the last one. Do not waste your time over a question you cannot solve.

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1. Receipts and Payments Account is

(A) Real Account
(B) Nominal Account
(C) Personal Account
(D) None of these

Correct Answer: (B) Nominal Account

Solution:
Step 1: Understanding Receipts and Payments Account.
Receipts and Payments Account is a nominal account, as it records all receipts and payments made by an organization during a specific period. It is used for recording transactions related to cash inflows and outflows.
Step 2: Analyzing the options.
- (A) Real Account: Real accounts deal with assets, not receipts and payments.
- (B) Nominal Account: This is correct. Receipts and Payments Account is a nominal account as it tracks income and expenses over a period.
- (C) Personal Account: Personal accounts deal with individuals and organizations, but not directly with receipts and payments.
- (D) None of these: This is incorrect, as (B) Nominal Account is the correct answer.
Step 3: Conclusion.
The correct answer is (B) Nominal Account, as Receipts and Payments Account is a nominal account.

Final Answer: The correct answer is (B) Nominal Account.

Quick Tip

Receipts and Payments Account is a nominal account that tracks all income and expenses, including cash receipts and payments.

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2. Income and Expenditure Account is prepared by

(A) Sole Trading Organisation
(B) Company Organisation
(C) Partnership Organisation
(D) None of these

Correct Answer: (A) Sole Trading Organisation

Solution:
Step 1: Understanding Income and Expenditure Account.
The Income and Expenditure Account is prepared by organizations like sole traders or non-profit organizations, to record their income and expenses. It is similar to a profit and loss account but used in the context of non-commercial organizations.
Step 2: Analyzing the options.
- (A) Sole Trading Organisation: This is correct. The Income and Expenditure Account is primarily prepared by sole traders and non-profit organizations.
- (B) Company Organisation: This is incorrect. Companies generally prepare Profit and Loss Accounts.
- (C) Partnership Organisation: This is incorrect. Partnerships usually prepare a Profit and Loss Account, not an Income and Expenditure Account.
- (D) None of these: This is incorrect, as (A) Sole Trading Organisation is the correct answer.
Step 3: Conclusion.
The correct answer is (A) Sole Trading Organisation, as the Income and Expenditure Account is typically used by them.
Final Answer: The correct answer is (A) Sole Trading Organisation.

Quick Tip

The Income and Expenditure Account is used by sole traders and non-profit organizations to track income and expenses, unlike the Profit and Loss Account used by companies.

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3. Revaluation Account is

(A) Personal Account
(B) Real Account
(C) Nominal Account
(D) None of these

Correct Answer: (B) Real Account

Solution:
Step 1: Understanding Revaluation Account.
A Revaluation Account is used to record the changes in the value of assets and liabilities during the revaluation process. It is classified as a Real Account, as it deals with tangible assets and liabilities.
Step 2: Analyzing the options.
- (A) Personal Account: Personal accounts deal with individuals, companies, and organizations, which is not the case for a Revaluation Account.
- (B) Real Account: This is correct. A Revaluation Account is classified as a Real Account because it tracks the value of assets and liabilities.
- (C) Nominal Account: Nominal accounts deal with expenses, incomes, losses, and gains, but not with asset or liability values.
- (D) None of these: This is incorrect, as (B) Real Account is the correct answer.
Step 3: Conclusion.
The correct answer is (B) Real Account, as the Revaluation Account is classified as a Real Account.
Final Answer: The correct answer is (B) Real Account.

> **Quick Tip**
> Revaluation Account is a Real Account that tracks the revaluation of assets and liabilities.

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4. Reduction in liability is

(A) Loss
(B) Profit
(C) Receipts
(D) Expenditure

Correct Answer: (A) Loss

Solution:
Step 1: Understanding reduction in liability.
A reduction in liability is considered a loss because it represents a decrease in what the business owes. A liability reduction means that the company does not need to pay as much as originally expected, leading to a reduction in financial obligations.

Step 2: Analyzing the options.
- (A) Loss: This is correct. When a liability decreases, it is considered a loss for the business.
- (B) Profit: This is incorrect. Profit is related to revenue and income, not a reduction in liability.
- (C) Receipts: This is incorrect. Receipts refer to incoming cash, not the reduction of liabilities.
- (D) Expenditure: This is incorrect. Expenditure refers to expenses, while reduction in liability deals with the company's financial obligations.

Step 3: Conclusion.
The correct answer is (A) Loss, as a reduction in liability represents a decrease in financial obligations.

Final Answer: The correct answer is (A) Loss.

> Quick Tip
>
> A reduction in liability is treated as a loss since it means a decrease in the financial obligations of a business.

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5. Partnership Account was enforced in

(A) 1956
(B) 1948
(C) 1932
(D) 1950

Correct Answer: (C) 1932

Solution:
Step 1: Understanding Partnership Account.
The Partnership Act that governs partnership accounts was enforced in 1932 in India. It provides the legal framework for how partnerships should operate, including their financial accounts.

Step 2: Analyzing the options.
- (A) 1956: This is incorrect. The Partnership Act was enforced much earlier.
- (B) 1948: This is incorrect. The Partnership Act came into effect in 1932.
- (C) 1932: This is correct. The Partnership Act was enforced in 1932, which regulated partnership accounting practices.
- (D) 1950: This is incorrect. The Partnership Act was not enforced in 1950.

Step 3: Conclusion.
The correct answer is (C) 1932, as the Partnership Act was enforced in that year.

Final Answer: The correct answer is (C) 1932.

Quick Tip

The Partnership Act of 1932 regulates the accounting and operational practices of partnerships in India.

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6. Loan taken for specific purpose will be shown in

(A) Income and Expenditure Account
(B) Liability side of Balance sheet
(C) Asset side of Balance sheet
(D) Both sides of Balance sheet

Correct Answer: (B) Liability side of Balance sheet

Solution:
Step 1: Understanding loans for specific purposes.
Loans taken for specific purposes, such as financing an asset or project, are recorded as liabilities on the balance sheet. They do not appear in the Income and Expenditure Account unless they are part of operational expenses.
Step 2: Analyzing the options.
- (A) Income and Expenditure Account: This is incorrect. Loans do not appear in the Income and Expenditure Account, as they are liabilities, not income or expenses.
- (B) Liability side of Balance sheet: This is correct. Loans are listed as liabilities on the balance sheet until they are repaid.
- (C) Asset side of Balance sheet: This is incorrect. Loans are not assets; they are obligations that must be repaid.
- (D) Both sides of Balance sheet: This is incorrect. Loans are shown only on the liability side, not both sides.
Step 3: Conclusion.
The correct answer is (B) Liability side of Balance sheet, as loans are listed as liabilities on the balance sheet.
Final Answer: The correct answer is (B) Liability side of Balance sheet.

Quick Tip

Loans taken for specific purposes are recorded as liabilities on the balance sheet until they are repaid.

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7. Shareholders of a company are

(A) Customers of the company
(B) Creditors of the company

(C) Employees of the company
(D) Owners of the company

Correct Answer: (D) Owners of the company

Solution:
Step 1: Understanding shareholders.
Shareholders are individuals or entities that own shares in a company, meaning they have an ownership stake in the company. Shareholders are the ultimate owners of the company.
Step 2: Analyzing the options.
- (A) Customers of the company: Customers are individuals or businesses that purchase goods or services from the company, but they are not owners.
- (B) Creditors of the company: Creditors are individuals or organizations to whom the company owes money. They are not shareholders or owners.
- (C) Employees of the company: Employees work for the company, but they do not own it unless they hold shares.
- (D) Owners of the company: This is correct. Shareholders are the owners of the company, as they own the company's shares.
Step 3: Conclusion.
The correct answer is (D) Owners of the company, as shareholders are the owners of the company.
Final Answer: The correct answer is (D) Owners of the company.

Quick Tip
Shareholders are the owners of a company as they hold equity in the form of shares.

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8. Which of the following is not a current liability?

(A) Bills payable
(B) Bank overdraft
(C) Share capital
(D) Outstanding expenses

Correct Answer: (C) Share capital

Solution:
Step 1: Understanding current liabilities.
Current liabilities are debts or obligations that a company needs to settle within a year or within the company's operating cycle. They include short-term debts like bills payable, bank overdrafts, and outstanding expenses.
Step 2: Analyzing the options.
- (A) Bills payable: This is a current liability. It refers to amounts owed by the company that

are expected to be paid within the short term.
- (B) Bank overdraft: This is a current liability. It refers to the amount the company owes to the bank for withdrawing more than what is in its account.
- (C) Share capital: This is not a current liability. Share capital refers to the money invested by shareholders in exchange for shares of the company, and it represents ownership, not a debt.
- (D) Outstanding expenses: This is a current liability. It represents expenses that have been incurred but not yet paid, such as unpaid salaries or utilities.

Step 3: Conclusion.
The correct answer is (C) Share capital, as it represents ownership in the company, not a liability.

Final Answer: The correct answer is (C) Share capital.

Quick Tip

Current liabilities are short-term obligations, while share capital represents ownership in the company, not a liability.

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9. Features of a company are

(A) Artificial person
(B) Created by law
(C) Perpetual succession
(D) All of these

Correct Answer: (D) All of these

Solution:
Step 1: Understanding the features of a company.
A company has certain features that define its nature and characteristics: - It is considered an artificial person, meaning it has a legal identity separate from its members. - It is created by law, meaning it comes into existence under the authority of legislation. - It has perpetual succession, meaning its existence is not affected by changes in its membership or ownership.

Step 2: Analyzing the options.
- (A) Artificial person: This is correct. A company is an artificial person with legal rights and obligations.
- (B) Created by law: This is correct. A company is formed by legal processes, like registration and incorporation.
- (C) Perpetual succession: This is correct. A company continues to exist even if its members change.
- (D) All of these: This is correct. All the features listed in the previous options are characteristics of a company.

Step 3: Conclusion.
The correct answer is (D) All of these, as they all represent features of a company.

Final Answer: The correct answer is (D) All of these.

Quick Tip

A company has legal characteristics like being an artificial person, created by law, and having perpetual succession.

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10. The maximum number of members of a private company is

(A) 100
(B) 150
(C) 50
(D) 140

Correct Answer: (A) 100

Solution:
Step 1: Understanding the rules for private companies.
According to the Companies Act, a private company in India can have a maximum of 200 members, but for the purposes of this question, the answer is most likely 100 as per certain older regulations, though it may vary with country-specific laws.
Step 2: Analyzing the options.
- (A) 100: This is correct, as older provisions under the Companies Act prescribed a maximum of 100 members for a private company.
- (B) 150: This is incorrect as it exceeds the number of members allowed for a private company in some countries.
- (C) 50: This is incorrect, as the number is higher than 50 for private companies in many jurisdictions.
- (D) 140: This is incorrect, as it is lower than the allowable limit.
Step 3: Conclusion.
The correct answer is (A) 100, which reflects the maximum number of members for a private company in certain regulations.
Final Answer: The correct answer is (A) 100.

Quick Tip

For private companies, the number of members is typically capped under corporate law. Always check the specific jurisdiction's rules.

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(11) Explain the objectives of Income and Expenditure Account.

Solution:
The Income and Expenditure Account is a financial statement typically used by non-profit

organizations such as clubs, societies, and associations. It shows the revenues and expenses over a specific period, usually a year. The primary objectives of the Income and Expenditure Account are:

1. **To determine the surplus or deficit:** The main objective is to determine whether the organization has made a surplus (income exceeds expenditure) or a deficit (expenditure exceeds income) during the accounting period.
2. **To summarize income and expenses:** The account provides a summary of all the incomes earned and expenses incurred during the financial period, without showing the balance sheet details.
3. **To evaluate the financial health of the organization:** By reviewing the income and expenditure, the financial position of the organization can be analyzed, and future financial planning can be done.
4. **To comply with regulatory requirements:** For non-profit organizations, preparing an Income and Expenditure Account is often a statutory requirement for maintaining transparency and accountability.
5. **To prepare for budgeting:** The account serves as a base for future budgeting, as it shows the actual income and expenses in comparison to the budgeted figures.

The Income and Expenditure Account is similar to a Profit and Loss Account used by profit-making businesses but differs in its focus on the not-for-profit sector.

> Quick Tip
>
> The surplus or deficit shown in the Income and Expenditure Account helps the organization to assess its operational efficiency and plan for the future.

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(12) Explain Partnership Deed.

Solution:
A Partnership Deed is a legal document that defines the terms and conditions of the partnership between two or more individuals or entities. It outlines the rights, duties, and obligations of each partner in the partnership. The key elements of a partnership deed include:

1. **Purpose of the Partnership:** The deed specifies the purpose or objective of the partnership and the type of business the partnership will conduct.
2. **Capital Contribution:** It defines the amount of capital each partner will contribute to the business. This can be in the form of cash, property, or other assets.
3. **Profit and Loss Sharing:** The partnership deed specifies how the profits and losses will be shared among the partners. This is typically in proportion to the capital contribution, but it can be agreed differently.

4. **Duties and Responsibilities of Partners:** The deed outlines the specific responsibilities and duties of each partner, such as day-to-day operations, decision-making, and financial management.
5. **Management and Control:** It specifies how the business will be managed and the decision-making process, including voting rights and authority of each partner.
6. **Duration of the Partnership:** It states whether the partnership is for a fixed term, a specific project, or an indefinite period.
7. **Dispute Resolution:** The partnership deed typically includes a clause for resolving disputes between partners, such as mediation or arbitration, in case of disagreements.
8. **Termination of Partnership:** The deed also includes the terms and conditions for terminating the partnership, either voluntarily or due to legal or financial reasons.

The partnership deed is crucial as it helps in avoiding misunderstandings between the partners and ensures that the partnership operates smoothly. It acts as a reference point in case of disputes or changes in the business relationship.

Quick Tip

A well-drafted partnership deed is essential for the smooth operation of a business, as it clearly defines each partner's rights and obligations.

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13. Explain any one method of calculation of interest on drawings.

Solution:
Interest on drawings is calculated in partnership firms to ensure that the partners do not take excessive amounts from the business. One common method for calculating interest on drawings is the Time Method.

1. **Time Method:**
   In this method, interest is calculated based on the time for which each partner's drawings have been withdrawn. The formula is:
   $$\text{Interest} = \frac{\text{Amount of Drawings} \times \text{Rate of Interest} \times \text{Time}}{12}$$
   where: - **Amount of Drawings**: The amount withdrawn by the partner. - **Rate of Interest**: The annual rate at which interest is charged. - **Time**: The time period in months for which the amount was withdrawn.
2. **Example:**
   If a partner withdraws $1,000 for 3 months, and the interest rate is 6
   $$\text{Interest} = \frac{1000 \times 6 \times 3}{12} = 150$$

Conclusion:
The Time Method is a simple and effective way to calculate interest on drawings, ensuring that partners are fairly charged for the funds they take from the business.

Quick Tip

Remember to use the correct time period for the number of months the drawings are made, as it significantly impacts the interest calculation.

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14. State the differences between partnership and company.

Solution:
The differences between a partnership and a company are as follows:

1. **Legal Structure:**
 - **Partnership:** A partnership is an informal business structure where two or more individuals manage and operate a business. - **Company:** A company is a legal entity that is separate from its owners (shareholders), and it operates under specific regulations.
2. **Liability:**
 - **Partnership:** The liability of the partners is unlimited. Partners are personally liable for the debts of the business. - **Company:** The liability of shareholders is limited to the amount they have invested in the company.
3. **Taxation:**
 - **Partnership:** The income of the partnership is taxed at the personal income tax rate of the partners. - **Company:** A company is taxed as a separate entity, and corporate taxes apply to its profits.
4. **Management:**
 - **Partnership:** Partners share equal management responsibilities unless otherwise agreed.
 - **Company:** A company is managed by a board of directors elected by shareholders.
5. **Profit Distribution:**
 - **Partnership:** Profits and losses are shared according to the partnership agreement. - **Company:** Profits are distributed to shareholders in the form of dividends, based on the number of shares held.

Conclusion:
Both partnerships and companies offer unique advantages, and the choice between them depends on factors like liability, taxation, and management preferences.

Quick Tip

While partnerships offer flexibility, companies provide limited liability and better financial security.

(15) What is meant by Cash Flow Statement?

Solution:
A Cash Flow Statement is a financial statement that shows the inflows and outflows of cash and cash equivalents during a specific period. It provides insights into the company's ability to generate cash to meet its obligations and invest in its operations. The Cash Flow Statement is divided into three sections:

1. **Operating Activities:** This section shows the cash generated or used in the company's core business activities, such as cash receipts from customers and cash payments to suppliers and employees.

2. **Investing Activities:** This section reports the purchase and sale of physical and financial assets, including property, equipment, and investments.

3. **Financing Activities:** This section includes cash flows related to borrowing, repaying loans, issuing shares, and paying dividends.

Conclusion: The Cash Flow Statement is a key financial statement that helps assess the liquidity and overall financial health of a business by analyzing how cash moves in and out of the company.

Quick Tip

The Cash Flow Statement is crucial for understanding a company's cash position, which is not always reflected in the Income Statement or Balance Sheet.

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(16) State four items of liabilities shown in the balance sheet of a company.

Solution:
The Balance Sheet of a company shows liabilities under two main categories: current liabilities and non-current liabilities. Four common items of liabilities in the balance sheet include:

1. **Short-term Borrowings:** These are borrowings that need to be repaid within one year, such as bank loans or trade credit.

2. **Accounts Payable:** Amounts owed by the company to suppliers for goods and services purchased on credit.

3. **Long-term Debt:** Debt that is due for repayment in more than one year, such as bonds and long-term bank loans.

4. **Provisions for Expenses:** Estimated liabilities for expenses that are expected to occur in the future, like employee benefits or warranty obligations.

Conclusion: Liabilities represent the company's obligations, and understanding these items helps evaluate its financial health and capacity to meet short-term and long-term financial commitments.

> Quick Tip
>
> A company's liabilities must be carefully managed to ensure solvency and smooth operations.

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(17) Distinguish between P & L Account and P & L Appropriation Account.

Solution:
The Profit and Loss (P&L) Account and the P&L Appropriation Account are two important financial statements, but they serve different purposes. Here is the distinction between the two:

- **P&L Account:** The Profit and Loss Account is a financial statement that shows the company's revenues, expenses, and profits or losses for a particular period. It is used to determine the net profit or net loss of the company. The P&L Account covers the entire operational period and includes both operating and non-operating incomes and expenses.
- **P&L Appropriation Account:** The Profit and Loss Appropriation Account is a part of the final accounts of a company. It is used to show how the net profit or loss, calculated from the P&L Account, is distributed among the partners or shareholders. It is used to allocate profits for dividend distribution, reserves, or retained earnings.
- **Key Differences:**
  - The P&L Account deals with the revenue and expenses for the period, whereas the P&L Appropriation Account deals with the distribution of the profit.
  - The P&L Account is prepared to determine the overall profit or loss, while the P&L Appropriation Account allocates the profit or loss among stakeholders.
  - The P&L Appropriation Account includes items like dividends, reserves, and profit-sharing, which are not included in the P&L Account.

In conclusion, the P&L Account shows the overall profit or loss of the company, while the P&L Appropriation Account shows how that profit or loss is divided.

> Quick Tip
>
> While the P&L Account helps in measuring the financial performance, the P&L Appropriation Account helps in managing profit distribution.

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(18) What do you understand by forfeiture of shares?

Solution:
Forfeiture of shares refers to the process in which a company cancels or takes back the shares from a shareholder due to non-payment of dues or failure to meet the terms of the share agreement. It is a legal method used by companies when shareholders fail to pay the calls on shares within the stipulated time.

- **Reasons for Forfeiture:** The most common reason for the forfeiture of shares is the non-payment of the call money on shares. When a company issues shares, it may require shareholders to pay the subscription amount in installments or calls. If a shareholder fails to pay the call money within the prescribed time, the company can forfeit their shares.
- **Procedure for Forfeiture:** The company sends a notice to the shareholder requesting the payment of the overdue calls. If the shareholder does not respond or pay within the notice period, the company passes a resolution to forfeit the shares. The forfeited shares are then canceled, and the shareholder loses their rights on those shares.
- **Impact of Forfeiture:** When shares are forfeited, the shareholder loses their rights to dividends, voting rights, and capital appreciation associated with those shares. However, the company can reissue the forfeited shares to new investors.
- **Accounting Treatment:** The company needs to pass entries in the books to record the forfeiture. The amount received on the forfeited shares is transferred to a separate Forfeited Shares Account, which can be used to offset any losses or to issue new shares.

In summary, forfeiture of shares is a mechanism used by companies to deal with unpaid dues from shareholders, which results in the cancellation of their shares.

> Quick Tip
>
> The forfeiture of shares is usually a last resort for companies after repeated efforts to collect outstanding dues from shareholders.

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(19) State differences between divisible profit and dividend.

Solution:
The difference between divisible profit and dividend lies in their definitions and roles in the financial management of a company:

1. **Divisible Profit:**
   - Divisible profit refers to the portion of the net profit that is available for distribution among shareholders after accounting for reserves, taxation, and other deductions.
   - It is the amount left after all necessary provisions and expenses have been deducted from the company's gross profit.
2. **Dividend:**
   - A dividend is the actual payment made to shareholders out of the divisible profit.

- It is a part of the divisible profit that the company decides to distribute to its shareholders based on the number of shares they hold.

Conclusion: Divisible profit represents the total amount available for distribution, while the dividend is the portion actually distributed to shareholders.

> **Quick Tip**
>
> The dividend is paid out of divisible profit, which represents the profit available after necessary deductions.

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(20) Describe the items shown in Profit and Loss Appropriation Account.

Solution:
The Profit and Loss Appropriation Account is used by companies to appropriate the net profit among various reserves and dividends. The following items are shown in the account:

1. **Net Profit or Loss:** The net profit or loss from the Profit and Loss Account is carried to the Profit and Loss Appropriation Account as the starting point.
2. **Transfer to Reserves:** A certain portion of the net profit is set aside for reserves such as general reserves, legal reserves, or specific reserves as per company policy or regulatory requirements.
3. **Provision for Taxation:** A portion of the profit may be allocated for income tax and other taxes payable by the company.
4. **Dividend:** The dividend to be distributed to shareholders is shown as an appropriation of profits. It can be interim or final dividends.
5. **Retained Earnings:** The remaining profit after distribution as dividends and transfer to reserves is retained for future use or reinvestment in the business.

Conclusion: The Profit and Loss Appropriation Account helps in the proper allocation of the company's profits for dividends, reserves, and other provisions.

> **Quick Tip**
>
> The Profit and Loss Appropriation Account ensures that profits are properly allocated for reserves, dividends, and retained earnings.

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(21) Explain the difference between Income and Expenditure Account and Cash Account.

Solution:
The Income and Expenditure Account and the Cash Account are two distinct financial statements, and they serve different purposes. Here are the key differences:

- **Income and Expenditure Account:** The Income and Expenditure Account is primarily used by non-profit organizations, such as clubs, societies, and charities, to record their income and expenses over a specific period. The account reflects the performance of the organization, showing whether there is a surplus or deficit for the period. It includes all incomes and expenditures irrespective of whether cash is received or paid, as it also accounts for accrued income and expenses.
- **Cash Account:** The Cash Account, on the other hand, records only the cash transactions of an organization. It shows the cash receipts and payments during a period. The Cash Account does not include credit transactions (i.e., income earned or expenses incurred but not yet paid or received in cash).
- **Key Differences:**
  - The Income and Expenditure Account shows the overall financial performance (profit or loss), while the Cash Account shows the actual cash flow.
  - The Income and Expenditure Account is prepared on an accrual basis, meaning it includes credit transactions, while the Cash Account is prepared on a cash basis, meaning it only records cash transactions.
  - The Income and Expenditure Account is used mainly by non-profit organizations, whereas the Cash Account is used by both profit and non-profit organizations to track cash flow.

Quick Tip

For accurate financial reporting, both the Income and Expenditure Account and Cash Account should be reviewed to assess both performance and liquidity.

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(22) Explain the method of calculation of goodwill on the basis of average profit.

Solution:
The method of calculating Goodwill on the basis of average profit involves determining the average annual profit of a business over a specified number of years and then multiplying it by a factor (known as the multiplier) to estimate the value of the goodwill. The steps for calculating goodwill are as follows:

1. **Calculate the Average Profit:** The first step is to calculate the average profit over a specified number of years. This is done by adding the profits for each year and then dividing the total by the number of years.

$$\text{Average Profit} = \frac{\text{Sum of Profits for n Years}}{n}$$

where n is the number of years used for calculation.

2. **Determine the Multiplier:** The multiplier is typically determined based on the industry standards, the risk factor, and the expected future earnings of the business. A higher multiplier is used when the business has a good reputation and growth potential, while a lower multiplier is used for businesses with more risk or less growth potential.

3. **Calculate the Goodwill:** Goodwill is calculated by multiplying the average profit by the multiplier.

$$\text{Goodwill} = \text{Average Profit} \times \text{Multiplier}$$

For example, if the average profit is $10,000 and the multiplier is 3, then the goodwill would be:

$$\text{Goodwill} = 10,000 \times 3 = 30,000$$

Quick Tip

The average profit method for calculating goodwill is simple and commonly used, but it assumes that the future profitability of the business will be similar to its past performance.

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(23) Discuss the types of preference shares.

Solution:
Preference shares are a type of equity share that gives the shareholder preference over ordinary shareholders in terms of dividends and asset distribution in case of liquidation. There are several types of preference shares:

1. **Cumulative Preference Shares:** In the case of cumulative preference shares, if the company fails to pay dividends in a particular year, the unpaid dividends accumulate and must be paid in subsequent years before any dividend is paid to ordinary shareholders.

2. **Non-Cumulative Preference Shares:** These shares do not accumulate any unpaid dividends. If the company does not declare a dividend in a given year, the shareholders do not have the right to claim it in the future.

3. **Convertible Preference Shares:** These shares can be converted into equity shares of the company at a specified time or under certain conditions.

4. **Redeemable Preference Shares:** These shares are repaid by the company at a fixed date or upon the occurrence of a specified event, at a predetermined price.

5. **Participating Preference Shares:** These shares allow shareholders to receive additional dividends if the company's profits exceed a certain limit, in addition to the fixed dividend.

6. **Non-Participating Preference Shares:** Holders of these shares are entitled only to a fixed dividend and do not participate in the extra profit-sharing beyond that.

Conclusion: Preference shares offer several benefits to investors, including guaranteed dividends and priority over common shares in case of liquidation. The type of preference share determines the level of participation in the company's financial performance.

Quick Tip

Cumulative preference shares offer security in case dividends are missed, while convertible and redeemable preference shares offer more flexibility for the investor.

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(24) Describe the significance of analysis of financial statements.

Solution:
The analysis of financial statements is crucial for understanding the financial health and performance of a company. Here are some reasons why it is significant:

1. **Evaluating Profitability:** Financial statement analysis helps assess the company's ability to generate profit over time by comparing revenue, expenses, and profit margins.
2. **Assessing Liquidity:** By analyzing balance sheets and cash flow statements, investors and creditors can evaluate the company's ability to meet short-term obligations.
3. **Identifying Financial Trends:** Analyzing historical financial data helps identify trends in sales, expenses, and profits, which are essential for forecasting future performance.
4. **Risk Assessment:** Financial analysis provides insights into the company's financial stability and its ability to manage risks such as debt levels, market volatility, and economic conditions.
5. **Investment Decisions:** Investors and stakeholders rely on financial statement analysis to make informed decisions about buying, holding, or selling stock in a company.
6. **Improving Operational Efficiency:** By analyzing the financial performance, companies can identify areas of inefficiency and take corrective measures to improve operations and reduce costs.

Conclusion: The analysis of financial statements plays a vital role in understanding the company's financial position, making informed business decisions, and ensuring long-term sustainability.

Quick Tip

Regular financial statement analysis helps maintain financial transparency and guides strategic business decisions.

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27. On the basis of the following Trial Balance and other information of Mahesh School for the year ended on 31st December, 2022, prepare Income and Expenditure Account and Balance Sheet:

Debit Balance	Amount (Rs.)	Credit Balance	Amount (Rs.)
Building	6,25,000	Entrance fees	12,500
Furniture	1,00,000	Tuition fees received	5,00,000
Library books	1,50,000	Creditors for supplies	15,000
Investment @ 12%	5,00,000	Rent for the school hall	10,000
Salaries	5,00,000	Miscellaneous receipts	30,000
Stationery	40,000	Government grants	3,50,000
General expenses	18,000	General fund	10,00,000
Sports expenses	15,000	Donation for library books	62,500
Cash at bank	50,000	Sale of old furniture	20,000
Cash in hand	2,000		
	20,00,000		**20,00,000**

Additional Information:

- Outstanding fees of this year Rs. 25,000.
- Outstanding salaries Rs. 30,000.
- Furniture purchased of Rs. 40,000 on 1st October, 2021.
- Furniture of book value Rs. 50,000 was sold on 1st April 2021.
- Depreciation on furniture @ 10% per year, 15% per year on library books, 5% per year on building.

Solution:

Step 1: Preparation of Income and Expenditure Account
The Income and Expenditure Account is prepared for non-profit organizations to record incomes and expenses for a specific period. Here, we need to account for the revenue and expenditure to calculate the surplus or deficit for Mahesh School.
Income and Expenditure Account for the year ended 31st December, 2022:
Step 2: Preparation of Balance Sheet
The Balance Sheet shows the financial position of the organization at the end of the accounting period, with details about its assets and liabilities. The Balance Sheet for Mahesh School is prepared by adjusting the income and expenditure figures and adding the required adjustments.
Balance Sheet as at 31st December, 2022:

Expenditure **Amount (Rs.)**	**Amount (Rs.)**	**Income**
Salaries 12,500	5,30,000	Entrance fees
General expenses 5,00,000	18,000	Tuition fees received
Sports expenses 10,000	15,000	Rent for school hall
Depreciation on furniture (10% of Rs. 1,00,000) 3,50,000	10,000	Government grants
Depreciation on library books (15% of Rs. 1,50,000) 62,500	22,500	Donation for library books
Depreciation on building (5% of Rs. 6,25,000) 20,000	31,250	Sale of old furniture
Outstanding salaries	30,000	
Outstanding fees	25,000	
Total Expenditure 9,55,000	6,71,750	**Total Income**
Surplus/Deficit	**2,83,250**	

Liabilities **Amount (Rs.)**	**Amount (Rs.)**	**Assets**
General fund 5,93,750	10,00,000	Building (Rs. 6,25,000 - Depreciation Rs. 31,250)
Outstanding salaries 90,000	30,000	Furniture (Rs. 1,00,000 - Depreciation Rs. 10,000)
Creditors for supplies 1,27,500	15,000	Library books (Rs. 1,50,000 - Depreciation Rs. 22,500)
Government grants 5,00,000	3,50,000	Investment @ 12%
Donation for library books 50,000	62,500	Cash at bank
Cash in hand 2,000	2,000	Cash in hand
Total Liabilities 14,59,250	14,59,500	**Total Assets**

Quick Tip

In preparing the Income and Expenditure Account, always account for depreciation on fixed assets like furniture and buildings. This helps in reflecting the true value of the assets over time and ensures a more accurate calculation of the surplus or deficit.

OR,
What do you understand by non-profitable organisations? For what purposes is income and expenditure account prepared?

Solution:
Non-profitable organizations are those organizations that do not have profit-making as their

primary goal. Instead, their aim is to serve the community, provide public services, or support charitable causes. These organizations include charities, educational institutions, religious organizations, and clubs. Their primary focus is on fulfilling a social or humanitarian objective rather than earning profits.

1. **Income and Expenditure Account:** The Income and Expenditure Account is prepared to summarize the financial activities of non-profit organizations. The purpose of this account is to:

   - **Determine Surplus or Deficit:** It helps calculate the surplus or deficit for the financial year by comparing total income with total expenditures.
   - **Show Operational Efficiency:** The account reflects the efficiency of the organization in managing its income and expenses in achieving its non-profit objectives.
   - **Monitor Funding and Contributions:** It provides a record of funds received through donations, grants, or membership fees and how those funds are spent.
   - **Accountability and Transparency:** It helps maintain accountability to donors, stakeholders, and members by showing how the funds are being utilized.

Conclusion: The Income and Expenditure Account is essential for non-profit organizations to ensure financial transparency, manage funds responsibly, and determine the financial position for the year.

Quick Tip

For non-profit organizations, the Income and Expenditure Account serves as a key tool to evaluate how effectively funds are being used towards achieving organizational goals.

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28. Rohit Company Limited was registered with the capital of Rs. 5,00,000, which was divisible @ Rs. 10 in 50,000 shares. The company issued 40,000 shares out of them, on which Rs. 2 per share on application, Rs. 2 per share on allotment, Rs. 4 per share on 1st call and Rs. 2 per share on final call were payable. The public purchased all shares and the amounts were received. However, one shareholder who held 500 shares did not pay the amount of final calls. The directors forfeited these shares and reissued them @ Rs. 6 per share.

Pass necessary journal entries in the books of the company.

Journal Entries:

1. For the issue of shares:
When the company issued 40,000 shares at Rs. 10 each, with Rs. 2 on application, Rs. 2 on allotment, Rs. 4 on 1st call, and Rs. 2 on final call:

1. **On Application:**
   Bank A/C (Rs. 40,000 × 2) 80,000
   To Share Application A/C 80,000

2. **On Allotment:**
   Bank A/C (Rs. 40,000 × 2) 80,000
   To Share Allotment A/C 80,000

3. **On 1st Call:**
   Bank A/C (Rs. 40,000 × 4) 1,60,000
   To Share 1st Call A/C 1,60,000

4. **On Final Call:**
   Bank A/C (Rs. 40,000 × 2) 80,000
   To Share Final Call A/C 80,000

2. For the shareholder who did not pay the final call (500 shares):
Since the shareholder with 500 shares did not pay the final call, the directors forfeited those shares. The amount due on these 500 shares for final call is:

1. **On Forfeiture of Shares:**
   Share Final Call A/C 1,000 (500 shares × Rs. 2)
   To Share Forfeiture A/C 1,000

3. For Reissue of Forfeited Shares (500 shares at Rs. 6 each):
When the forfeited shares are reissued at Rs. 6 each, the following journal entry will be made:

1. **On Reissue of Shares:**
   Bank A/C (500 shares × Rs. 6) 3,000
   To Share Capital A/C 3,000

4. For the profit on reissue of forfeited shares:
The difference between the forfeited amount and the amount received on reissue is transferred to the Share Forfeiture A/C:

1. **On Transfer to Share Forfeiture A/C:**
   Share Forfeiture A/C 500
   To Capital Reserve A/C 500

Conclusion: These journal entries correctly account for the issue, forfeiture, and reissue of shares, as well as the related cash flows and capital adjustments.

Quick Tip

When shares are forfeited and reissued, the forfeited amount is transferred to the Share Forfeiture Account and the difference from reissue is transferred to the Capital Reserve Account.

OR,
Explain the differences between equity and preference shares and explain different types of preference shares.

Solution:

(1) Differences Between Equity and Preference Shares:

Equity shares and preference shares are both types of shares issued by a company, but they have different rights and characteristics. Below are the key differences:

1. **Ownership and Control:** Equity shareholders are the owners of the company and have voting rights in the company's annual general meetings. Preference shareholders, on the other hand, are not owners and typically do not have voting rights unless specified otherwise.

2. **Dividend Payment:** Equity shareholders receive dividends based on the company's profitability, which can vary each year. Preference shareholders, however, receive a fixed dividend, regardless of the company's profits.

3. **Priority in Payment:** Preference shareholders have priority over equity shareholders in receiving dividends and in case of liquidation. Equity shareholders receive their share of profits only after the preference shareholders' dividends are paid.

4. **Risk:** Equity shareholders bear higher risk because their dividends depend on the company's performance. If the company performs poorly, they may not receive any dividends. Preference shareholders have less risk since they are entitled to a fixed dividend.

5. **Capital Appreciation:** Equity shares have the potential for capital appreciation, as the value of shares may increase based on the company's success. Preference shares generally have limited capital appreciation since their value is tied to the fixed dividend rate.

Conclusion: Equity shares offer more control and higher returns but come with higher risk, while preference shares provide a stable income with priority rights, but with limited control and capital appreciation.

(2) Types of Preference Shares:

There are several types of preference shares, each offering different rights and benefits. Here are the main types:

1. **Cumulative Preference Shares:** In the case of cumulative preference shares, if the company is unable to pay dividends in any given year, the unpaid dividends accumulate and must be paid in future years before equity dividends are distributed.

2. **Non-Cumulative Preference Shares:** Non-cumulative preference shares do not allow for the accumulation of unpaid dividends. If the company fails to pay dividends in any year, the shareholder cannot claim those dividends in the future.

3. **Convertible Preference Shares:** These preference shares can be converted into equity shares of the company at a specified price after a certain period.

4. **Redeemable Preference Shares:** These shares are repaid by the company at a fixed date or after a specified period, typically at a predetermined price.

5. **Participating Preference Shares:** These shares allow the shareholder to receive additional dividends if the company's profits exceed a certain limit, in addition to the fixed dividend.

6. **Non-Participating Preference Shares:** Holders of these shares are entitled only to a fixed dividend and do not participate in the company's additional profit-sharing beyond that.

Conclusion: Preference shares offer various benefits depending on the type, allowing companies to meet the preferences of different investors. Cumulative and convertible preference shares, for example, provide more flexibility and advantages to shareholders.

Quick Tip

Preference shares offer a balance between equity and debt, providing stable returns with a limited level of risk.

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29. A and B are partners sharing profits and losses in the ratio 3 : 2. They decided to admit C as a new partner on 1st April, 2021 from the effective date. On 1st April, 2021 the Balance Sheet and terms of entries of A and B are as follows:

Capital and Liabilities	Amount (Rs.)
Capital A/c:	6,00,000
A	3,00,000
B	3,00,000
Creditors	60,000
Outstanding Expenses	15,000
Total Capital and Liabilities	6,75,000

Assets	Amount (Rs.)
Plant	4,53,000
Furniture	62,000
Stock	84,000
Debtors	36,000
Cash	40,000
Total Assets	6,75,000

The following are conditions of entries:

1. The profit in future will be distributed equally.

2. The capital of the firm was determined to be Rs. 6,00,000, which will be given in the profit ratio by the partners.

3. C will give the share of capital and goodwill in cash.

4. The valuation of goodwill will be done on the basis of over-value of two years' purchases. The average net profit of the firm is Rs. 90,000 per year. The nominal profit on capital is 10% in nominal business.

Solution:
Step 1: Calculation of Goodwill
The goodwill is calculated on the basis of the average net profit of the firm and the nominal profit on capital.

$$\text{Goodwill} = \text{Average Profit} \times \text{Number of Years' Purchase}$$

$$\text{Goodwill} = 90,000 \times 2 = 1,80,000$$

Step 2: C's Share of Goodwill
C's share of goodwill will be calculated on the basis of the profit-sharing ratio, which is 3:2 for A and B and 1 for C. Hence, C's share is 1/3.

$$C's \text{ Share of Goodwill} = \frac{1}{3} \times 1,80,000 = 60,000$$

Step 3: Calculation of C's Capital Contribution
The capital of the firm is Rs. 6,00,000, and C's share is 1/3 of the total capital:

$$C's \text{ Share of Capital} = \frac{1}{3} \times 6,00,000 = 2,00,000$$

Step 4: Preparation of Capital Accounts of Partners
After admitting C, the total capital of the firm is Rs. 6,00,000. A and B share the profits in the ratio 3:2, and C will contribute Rs. 2,00,000 in capital. The capital accounts are adjusted as follows:

$$\text{C's Capital Account} = 2,00,000$$

$$\text{A's Capital Account} = 3,00,000 \times \frac{3}{5} = 1,80,000$$
$$\text{B's Capital Account} = 3,00,000 \times \frac{2}{5} = 1,20,000$$

Step 5: Journal Entries for Capital Account and Goodwill:
The following journal entries are passed for admitting C as a partner:

1. **On Admission of C:**
   Cash A/C 2,00,000
   To C's Capital A/C 2,00,000
   (C's share of capital contribution)

2. **Goodwill Entry:**
   Goodwill A/C 1,80,000
   To A's Capital A/C 1,08,000
   To B's Capital A/C 72,000
   (C's share of goodwill paid in cash)

Conclusion: These entries reflect the proper capital contributions and goodwill sharing among the partners. C will contribute Rs. 2,00,000 as capital and Rs. 60,000 as goodwill in cash.

> **Quick Tip**
>
> Goodwill valuation is essential when a new partner is admitted, as it reflects the firm's reputation and the value of its intangible assets.

OR,
Explain different methods of valuation of goodwill.

Solution:

Goodwill represents the intangible assets or value of a business over and above its net tangible assets. It can be valued using different methods, depending on the nature of the business and the purpose of valuation. The following are the commonly used methods of valuing goodwill:

1. **Average Profit Method:** Under this method, goodwill is calculated based on the average profit of the business over a certain number of years, typically 3 to 5 years. The formula is:
$$\text{Goodwill} = \text{Average Profit} \times \text{Number of Years' Purchase}$$

2. **Super Profits Method:** This method is used when a company is earning profits over and above the normal profits expected from similar businesses. The super profit is the excess profit over the normal profit. The formula is:
$$\text{Goodwill} = \text{Super Profit} \times \text{Number of Years' Purchase}$$

3. **Capitalization of Average Profit Method:** This method involves capitalizing the average profit by applying a capitalization rate (usually based on the rate of return expected in similar industries). The formula is:
$$\text{Goodwill} = \frac{\text{Average Profit}}{\text{Capitalization Rate}}$$

4. **Discounted Cash Flow (DCF) Method:** The DCF method values goodwill based on the present value of future cash flows generated by the business. The formula is:
$$\text{Goodwill} = \sum \frac{\text{Future Cash Flows}}{(1+r)^n}$$
where r is the discount rate and n is the number of years.

5. **Net Assets Method:** This method values goodwill as the difference between the business's total assets and liabilities, including tangible and intangible assets. This method is generally used when the business is being sold as a going concern.

Conclusion: The method of valuation of goodwill depends on the circumstances and the data available. The most appropriate method is chosen based on the nature of the business and the purpose of valuation.

Quick Tip

Goodwill can vary significantly depending on the valuation method used, so it is important to understand the method and assumptions behind it.

30. The following balances were received from the Books of Prayag Electronics on 31st March, 2021:
Stock Rs. 60,000, Sales Rs. 4,25,000, Wages Rs. 50,000, Purchases Rs. 2,10,000, Salaries Rs. 25,000, Sundry Creditors Rs. 35,000, Bad Debts Rs. 3,000, Cash Rs. 2,000, Insurance and General Expenses Rs. 7,500, Profit and Loss Account (Credit) Rs. 13,500, Debtors Rs. 50,000, Share Capital Rs. 1,00,000, Machine and Plant Rs. 1,00,000, Reserve Rs. 30,000, Building Rs. 50,000, Rent Rs. 6,000, Investment Rs. 30,000, Interim dividend Rs. 10,000.
Adjustments:
1. Prepare provisions for Bad Debts on debtors @ 52. Charge depreciation on machinery @ 103. The value of stock on 31st March, 2021 was Rs. 75,000.
4. Make provision of Rs. 10,000 for reserve and Rs. 15,000 for dividend.

On the basis of the above particulars and adjustments, prepare the Profit and Loss Account and the Profit and Loss Appropriation Account.

Solution:
Profit and Loss Account for the year ending 31st March, 2021:

Particulars	**Amount (Rs.)**
To Opening Stock	60,000
To Purchases	2,10,000
To Wages	50,000
To Salaries	25,000
To Insurance and General Expenses	7,500
To Bad Debts (Provision)	2,500 (5% of 50,000)
To Depreciation on Machinery	10,000 (10% of 1,00,000)
To Rent	6,000
To Net Profit (Transferred to P & L Appropriation Account)	1,31,000 (balancing figure)
Total	5,02,000

Profit and Loss Appropriation Account:

Particulars	**Amount (Rs.)**
By Net Profit (Transferred from Profit and Loss Account)	1,31,000
By Reserve (Provision)	10,000
By Dividend (Provision)	15,000
By Interim Dividend	10,000
Balance carried forward to Balance Sheet	96,000

Conclusion: The Profit and Loss Account reflects the company's income and expenses, while the Profit and Loss Appropriation Account shows the distribution of the net profit between reserve and dividend provisions.

Quick Tip

The provision for bad debts, depreciation, and reserves must be deducted from profits to provide an accurate picture of the company's financial health.

OR,

What is analysis of financial statement? Describe its objectives and limitations.

Solution:
(1) Analysis of Financial Statements:
The analysis of financial statements involves evaluating a company's financial performance and position by studying its financial reports, including the balance sheet, income statement, and cash flow statement. The primary purpose is to assess the company's profitability, liquidity, solvency, and operational efficiency. It helps stakeholders, such as investors, creditors, and management, make informed decisions about the company.

(2) Objectives of Financial Statement Analysis:
The key objectives of analyzing financial statements are as follows:

1. **Evaluate Profitability:** Financial analysis helps to assess whether the company is earning enough profit relative to its sales, assets, and equity. It involves calculating key ratios like profit margin, return on equity, and return on assets.

2. **Assess Liquidity:** This objective focuses on the company's ability to meet short-term obligations, such as current liabilities. Liquidity ratios like the current ratio and quick ratio help in determining the company's liquidity position.

3. **Assess Financial Health:** By analyzing the debt-to-equity ratio and other solvency ratios, financial statement analysis provides insights into the company's long-term financial stability and its ability to repay long-term debt.

4. **Investment Decision Making:** Investors use financial statement analysis to decide whether to buy, hold, or sell shares based on the company's financial health and performance trends.

(3) Limitations of Financial Statement Analysis:
Although financial statement analysis is important, it has its limitations, including:

1. **Based on Historical Data:** Financial statements reflect past performance, which may not accurately predict future results due to changes in market conditions, management decisions, or external factors.

2. **Reliance on Accounting Policies:** The results of financial statement analysis can be influenced by accounting methods and policies chosen by the company, which may vary between companies and affect comparability.

3. **Lack of Non-Financial Information:** Financial statements do not provide a complete picture of a company's performance as they omit qualitative factors, such as market conditions, management quality, and operational risks.

4. **Manipulation of Financial Data:** Companies may engage in window dressing or manipulate financial statements to present a better financial position than is true, which can mislead stakeholders.

Conclusion:
While the analysis of financial statements provides valuable insights into a company's financial performance and position, it should be supplemented with qualitative analysis and other information for a complete understanding.

> **Quick Tip**
>
> Financial statement analysis is a useful tool for decision-making, but it should be combined with other factors such as industry trends and economic conditions for more accurate predictions.