CHAPTER - 7

ACCOUNTING FOR SPECIAL TRANSACTIONS

Unit 1

Consignment

Learning Objectives :

After studying this unit, you will be able to :

- Understand the special features of consignment business, meaning of the terms *consignor* and *consignee*.
- Analyse the difference between the two transactions – sale and consignment and understand that why consignment is termed as special transaction.
- Practise the accounting treatments for consignment transactions and events in the books of consignor and consignee.
- Note the variations in accounting when goods are sent at cost and goods are sent above the cost.
- Learn the technique of computing value of closing Inventory lying with the consignor and also the amount of Inventory reserve in it.
- Learn the technique of computing cost of abnormal loss and treatment of insurance claim in relation to it.
- Understand the distinction between ordinary commission, del-credere commission and over-riding commission paid to the consignee.
- See the variation of accounting treatment for bad debts when consignee is paid ordinary commission and when consignee is paid del-credere commission in addition.
- Understand the reason of including/excluding various expenditures to cost while valuing the goods returned by the consignee.

1. MEANING OF CONSIGNMENT ACCOUNT

To consign means to send. In Accounting, the term "consignment account" relates to accounts dealing with a situation where one person (or firm) sends goods to another person (or firm) on the basis that the goods will be sold *on behalf of and at the risk of the former*. The following should be noted carefully:

(i) The party which sends the goods (consignor) is called principal.

(ii) The party to whom goods are sent (consignee) is called agent.

(iii) The ownership of the goods, i.e., the property in the goods, remains with the consignor or the principal – the agent does not become their owner even though they are in his possession. On sale, of course, the buyer will become the owner.

(iv) The principal does not send an invoice to the agent. He sends only a proforma invoice, a statement that looks like an invoice but is really not one. The object of the proforma invoice is only to convey information to the agent regarding particulars of the goods sent.

(v) Usually, the agent recovers from the principal all expenses incurred by him on the consignment. This however can be changed by agreement between the two parties.

(vi) It is also usual for the agent to give an advance to the principal in the form of cash or a bill of exchange. It is adjusted against the sale proceeds of the goods.

(vii) For his work the agent receives a commission, calculated on the basis of gross sale. For ordinary commission the agent is not responsible for any bad debt that may arise. If the agent is to be made responsible for bad debts, he is to be paid a commission called del-credere commission. It is calculated on total sales, not merely on credit sales until and unless agreed.

(viii) Periodically, the agent sends to the principal a statement called Account Sales. It sets out the sales made by the agent, the expenses incurred on behalf of the principal, the commission earned by the agent and the balance due to the principal.

(ix) Firms usually like to ascertain the profit or loss on each consignment or consignments to each agent.

Consignment Account relates to accounts dealing with such business where one person sends goods to another person on the basis that such goods will be sold on behalf of and at the risk of the former.

2. DISTINCTION BETWEEN CONSIGNMENT AND SALE

S.No.	*Consignment*	*Sale*
1.	Ownership of the goods rests with the consignor till the time they are sold by the consignee, no matter the goods are transferred to the consignee.	The ownership of the goods transfers with the transfer of goods from the seller to the buyer.
2.	The consignee can return the unsold goods to the consignor.	Goods sold are the property of the buyer and can be returned only if the seller agrees.
3.	Consignor bears the loss of goods held with the consignee.	It is the buyer who will bear the loss if any, after the delivery of goods.
4.	The relationship between the consignor and the consignee is that of a principal and agent.	The relationship between the seller and the buyer is that of a creditor and a debtor.
5.	Expenses done by the consignee to receive the goods and to keep it safely is borne by the consignor.	Expenses incurred by the buyer are to be borne by the buyer itself after the delivery of goods.

3. ACCOUNTING FOR CONSIGNMENT TRANSACTIONS AND EVENTS IN THE BOOKS OF THE CONSIGNOR

For ascertaining profit or loss on any transaction (or series of transactions) there is one golden rule; open an account for the transaction (or series of transactions) and (i) put down the cost of goods and other expenses incurred or to be incurred on the debit side; and (ii) enter the sale proceeds as also the cost of goods remaining unsold on the right hand or the credit side. The difference between the total of the two sides will reveal profit or loss. There is profit if the credit side is more.

We shall illustrate the scheme of entries on the basis of the following information:

Illustration 1

Exe sent on 1st July, 2011 to Wye goods costing ₹ 50,000 and spent ₹ 1,000 on packing etc. On 3rd July, 2011, Wye received the goods and sent his acceptance to Exe for ₹ 30,000 payable at 3 months. Wye spent ₹ 2,000 on freight and cartage, ₹ 500 on godown rent and ₹ 300 on insurance. On 31st December, 2011 he sent his Account Sales (along with the amount due to Exe) showing that 4/5 of the goods had been sold for ₹ 55,000. Wye is entitled to a commission of 10%. One of the customers turned insolvent and could not pay ₹ 600 due from him. Show the necessary journal entries.

Solution

Journal Entries

			Dr.	***Cr.***
1.	*Open Consignment Account and debit it with the cost of goods and credit it with "Goods sent on Consignment Account". In the above case:*		₹	₹
1/7/2011	Consignment to Wye A/c	Dr.	50,000	
	To Goods Sent on Consignment A/c			50,000
2.	*For the expenses incurred by the consignor, debit Consignment Account and credit cash (or Bank as the case may be)*			
1/7/2011	Consignment to Wye A/c	Dr.	1,000	
	To Bank A/c			1,000
3.	*If the consignee sends an advance, debit Cash (or Bank) or Bills Receivable and credit the consignee's personal account*			
3/7/2011	Bills Receivable A/c	Dr.	30,000	
	To Wye			30,000
	(*Note:* Wye's account has appeared only now, in the previous two entries his account did not figure since he is not personally involved)			
4.	*Wye's acceptance will mature on 6/10/2011 Assuming it was met the entry will be:*			
6/10/2011	Bank A/c	Dr.	30,000	
	To Bills Receivable A/c			30,000
	(*Note*: If such bill is discounted by consignor with the bank before maturity, pass usual entry for discounting a bill. The discount on bills may either be treated as consignment expenses and charged to Consignment A/c or it may be treated as general financial charges and charged to Profit & Loss Account)			
5.	*On receipt of Account sale*			
	(a) For sales made by the consignee, debit his personal account and credit Consignment Account			
	Wye	Dr.	55,000	
	To Consignment to Wye A/c			55,000

	(b) *For expenses incurred by the consignee as well as bad debts suffered by him on behalf of the consignor, debit Consignment Account and credit Consignee Account* Consignment to Wye A/c Dr. To Wye	3,400	 3,400
	(c) *For commission due to the consignee, debit Consignment Account and credit the consignee.* Consignment to Wye A/c To Wye (10% on ₹ 55,000)	5,500	 5,500
	(d) *For the remittance that may accompany the Account Sales, debit Bank and credit the consignee.* Bank A/c Dr. To Wye	16,100	 16,100
6.	For the goods that may remain unsold debit the Inventories on Consignment Account and credit Consignment Account. Inventories on Consignment A/c Dr. To Consignment to Wye A/c	10,600	 10,600
	Note: (i) Cost of Inventories 1/5 of Cost to consignor ₹ 10,000 1/5 of expense incurred ₹ 200 1/5 of freight ₹ 400 ₹ 10,600 (ii) Inventories on Consignment Account is an asset; it will be shown in the balance sheet of the consignor and next year it will be transferred to the debit of the Consignment Account.		
7.	*At this stage the Consignment Account will reveal profit or loss (see the account given below). The profit or loss will be transferred to the Profit and Loss Account by debit to the Consignment Account.* Consignment to Wye A/c Dr. To Profit and Loss A/c	5,700	 5,700
8.	*The Goods sent on Consignment Account should be closed by transfer to the Trading Account debit the former and credit the latter:* Goods sent on Consignment Account Dr. To Trading Account	50,000	 50,000

Important Ledger Accounts

Consignment to Wye Account

2011		₹	2011		₹
July 1	To Goods sent on Consignment A/c	50,000	Dec. 31	By Wye-sale proceeds	55,000
July 1	To Bank expenses	1,000		By Inventories on Consignment Account	10,600
Dec. 31	To Wye-expenses & bad debt	3,400			
Dec. 31	To Wye-commission	5,500			
Dec. 31	To P&L Account-transfer of profit	5,700			
		65,600			65,600

Goods sent on consignment account

2011		₹	2011		₹
Dec. 31	To Trading A/c	50,000	July 1	By Consignment to Wye A/c	50,000

Inventories on consignment account

2011		₹	2011		₹
Dec. 31	To Consignment to Wye A/c	10,600	Dec. 31	By Balance c/d	10,600
2012					
Jan. 1	To Balance b/d	10,600			

Wye's account

2011		₹	2011		₹
Dec. 31	To Consignment Wye A/c	55,000	July 3	By Bills Receivable Account	30,000
				By Consignment to Wye A/c –	
				Expenses & bad debt	3,400
				Commission	5,500
				By Bank (balance received)	16,100
		55,000			55,000

4. VALUATION OF INVENTORIES

The principle is that inventories should be valued at cost or net realisable value whichever is lower, the same principle as is practised for preparing final accounts. In the case of consignment, cost means not only the cost of the goods as such to the consignor but also all expenses incurred till the goods reach the premises of the consignee. Such expenses include packaging, freight, cartage, insurance in transit, octroi, etc. But expenses incurred after the goods have reached the consignee's godown (such as godown rent, insurance of godown, delivery charges) are not treated as part of the cost of purchase for valuing inventories on hand. That is why in the case given above, inventories has been valued ignoring godown rent and insurance.

(Sometimes an examination problem states only that the consignor's expenses amounted to such and such amount and that consignee spent so much. If details are not available for valuing inventories the expenses incurred by the consignor should be treated as part of cost while those incurred by the consignee should be ignored).

If the expected selling price of inventories on hand is lower than the cost, the value put on the inventories should be expected net selling price only, i.e. expected selling price less delivery expenses, etc.

5. GOODS INVOICED ABOVE COST

Sometimes the proforma invoice is made out at a value higher than the cost and entries in the books of the consignor are made out on that basis – even the inventories remaining unsold will initially be valued on the basis of the invoice price. It must be remembered, however, that the profit or loss can be ascertained *only* if sale proceeds (plus) inventories on hand, valued on cost basis, is compared with the cost of the goods concerned together with expenses. Hence, if entries are first made on invoice basis, the effect of the loading (i.e., amount added to arrive at the invoice price) must be removed by *additional entries*. Suppose in the example given above, if the invoice is cost plus 20%, i.e., ₹ 60,000 for the goods sent to Wye. The entries will be initially:

			Dr. ₹	***Cr.*** ₹
(i)	Consignment to Wye A/c	Dr.	60,000	
	To Goods sent on Consignment A/c			60,000
(ii)	Consignment to Wye A/c	Dr.	1,000	
	To Bank			1,000
(iii)	Bills Receivable A/c	Dr.	30,000	
	To Wye			30,000

			Dr. ₹	Cr. ₹
(iv)	Bank A/c	Dr.	30,000	
	To Bills Receivable A/c			30,000
(v)	Wye	Dr.	55,000	
	To Consignment to Wye A/c			55,000
(vi)	Consignment to Wye A/c	Dr.	3,400	
	To Wye			3,400
(vii)	Consignment to Wye A/c	Dr.	5,500	
	To Wye			5,500
(viii)	Bank A/c	Dr.	16,100	
	To Wye			16,100
(ix)	Inventories on Consignment A/c	Dr.	12,600	
	To Consignment to Wye A/c			12,600
	[1/5 of 60,000 + 1/5 of (1,000 + 2,000)]			

[Students will see that except for difference in the amounts in entries (i) and (ix), these and other entries are the same as those already given.]

Additional entries (before ascertaining profit) to remove the effect of loading:

(a)	Goods sent on Consignment A/c	Dr.	10,000	
	To Consignment to Wye A/c			10,000

[Entry (i) reversed to the extent of loading in order to debit the Consignment A/c on cost basis].

(b)	Consignment to Wye A/c	Dr.	2,000	
	To Inventory Reserve Account			2,000

(The amount of loading included in the value of the closing Inventories is unrealised profit – hence reserve is created by debit to the Consignment Account).

The Consignment Account will now reveal a profit of ₹ 5,700 the same as before. It will be transferred to the P&L A/c. Similarly entry given in 8 above will be made to transfer the balance in the Goods sent on Consignment Account (now against ₹ 50,000) after entry in (a) above to the credit of Trading Account. The accounts (except for Wye whose account will be the same as already shown) are given below:

Consignment to Wye Account

2011		₹	2011		₹
July 1	To Goods sent on Consignment A/c	60,000	Dec. 31	By Wye Sales proceeds	55,000
	To Bank A/c – expenses	1,000		By Inventories on Consignment A/c	12,600
Dec. 31	To Wye-expenses & bad debt	3,400	"	By Goods sent on Consignment A/c loading	10,000
"	To Wye-commission	5,500			
"	To Inventory Reserve A/c	2,000			
"	To Profit and Loss A/c transfer of profit	5,700			
		77,600			77,600

Goods sent on Consignment Account

2011		₹	2011		₹
Dec. 31	To Consignment to Wye A/c – loading	10,000	July 1	By Consignment to Wye A/c	60,000
	To Trading A/c – transfer	50,000			
		60,000			60,000

Inventories on Consignment Account

2011		₹	2011		₹
Dec. 31	To Consignment to Wye A/c	12,600	Dec. 31	By Balance c/d	12,600
2012					
Jan. 1	Balance b/d	12,600			

Inventory Reserve Account

2011		₹	2011		₹
Dec. 31	To Balance c/d	2,000	Dec. 31	By Consignment to Wye A/c	2,000
			2012		
			Jan. 1	By Balance b/d	2,000

The last two accounts will be carried forward to the next year and their balance will then be transferred to the Consignment Account – ₹ 12,600 on the debit side and ₹ 2,000 on the credit. This year in the balance sheet the net amount of ₹ 10,600 will be shown on the assets side as shown below:

	₹
Inventories on consignment	12,600
Less: Reserve	2,000
	10,600

What would be the situation if the commission to Wye includes del-credere commission also? In that case Wye would not be able to charge the bad debt of ₹ 600 to Exe; he will have to bear the loss himself. The student can see that then the profit on consignment will be ₹ 6,300.

In this regard it is to be noted that when del – credere commission is paid to the consignee, the consignee account is debited in the books of consignor for both cash and credit sales. But if no such del – credere commission is paid then consignee account cannot be debited for credit sales and in that case the following entry is passed in the books of consignor for credit sales.

Consignment Trade receivables A/c Dr.

To Consignment A/c

6. ABNORMAL LOSS

If any accidental or unnecessary loss occurs, the proper thing to do is to find out the cost of the goods thus lost and then to credit the Consignment Account and debit the Profit and Loss Account – this will enable the consignor to know what profit would have been earned had the loss not taken place. Suppose 1,000 sewing machines costing ₹ 250 each are sent on consignment basis and ₹ 10,000 are spent on freight etc. 20 machines are damaged beyond repair. The amount of loss will be:

Cost = 20×250	₹ 5,000
Expenses = $2 \times \frac{10,000}{1,000}$	₹ 200
	₹ 5,200

This amount should be credited to the Consignment Account and debited to the P&L A/c. If any amount, say, ₹ 4,000 is received from the insurers, then debit to the P&L A/c will be only ₹ 1,200. But the credit to the Consignment Account will still be ₹ 5,200. ₹ 4,000 will have been debited to the Bank Account.

Students will have noted that abnormal loss is valued just like inventories in hand.

Students should be careful while valuing goods lost in transit and goods lost in consignee's godown. Both are abnormal loss but in case of former consignee's non-recurring expenses are not to be included whereas it is to be included in case of latter.

7. NORMAL LOSS

If some loss is essential and unavoidable, it would be spread over the entire consignment while valuing inventories. The total cost plus expenses incurred should be divided by the quantity available after the normal loss to ascertain the cost per unit. Suppose 1,000 kg of apples are consigned to a wholesaler, the cost being ₹ 3 per kg, plus ₹ 400 of freight. It is concluded that a loss of 15% is unavoidable. The cost per kg will be ₹ 3,400 ÷ 850 or ₹ 4. If the inventories is 100 kg its value will be ₹ 400.

8. COMMISSION

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

8.1 ORDINARY COMMISSION

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

8.2 DEL-CREDERE COMMISSION

To increase the sale and to encourage the consignee to make credit sales, the consignor provides an additional commission generally known as del-credere commission which is generally calculated on credit sales. This additional commission when provided to the consignee gives a protection to the consignor against bad debts. In other words, after providing the del-credere commission, bad debts is no more the loss of the consignor.

8.3 OVER-RIDING COMMISSION

It is an extra commission allowed by the consignor to the consignee to promote sales at higher price then specified or to encourage the consignee to put hard work in introducing new product in the market. Depending on the agreement it is calculated on total sales or on the difference between actual sales and sales at invoice price or any specified price.

9. RETURN OF GOODS FROM THE CONSIGNEE

Consigned goods can be returned by the consignee because of many reasons like poor quality or not upto the specimen or destroyed in transit etc. In such a situation, the question arises is the valuation of returned goods. Consigned goods returned by the consignee to the consignor are valued at the price at which it was consigned to the consignee. Expenses incurred by the consignee to send those goods back to the consignor are not taken into consideration while valuing it because only those expenses are included in the cost of goods which help to bring the goods into present location and condition i.e. the saleable condition.

10. ACCOUNT SALES

An account sale is the periodical summary statement sent by the consignee to the consignor. It contains details regarding –

(a) sales made,

(b) expenses incurred on behalf of the consignor,

(c) commission earned,

(d) unsold inventories left with the consignee,

(e) advance payment or security deposited with the consignor and the extent to which it has been adjusted,

(f) balance payment due or remitted.

It is a summary statement and is different from Sales Account.

11. ACCOUNTING BOOKS OF THE CONSIGNEE

The consignee is not concerned when goods are consigned to him or when the consignor incurs expenses. He is concerned only when he sends an advance to the consignor, makes a sale, incurs expenses on the consignment and earns his commission. He debits or credits the consignor for all these as the case may be.

Illustration 2

Exe sent on 1st July, 2011 to Wye goods costing ₹ 50,000 and spent ₹ 1,000 on packing etc. On 3rd July, 2011, Wye received the goods and sent his acceptance to Exe for ₹ 30,000 payable at 3 months. Wye spent ₹ 2,000 on freight and cartage, ₹ 500 on godown rent and ₹ 300 on insurance. On 31st December, 2011 he sent his Account Sales (along with the amount due to Exe) showing that 4/5 of the goods had been sold for ₹ 55,000. Wye is entitled to a commission of 10%. One of the customers turned insolvent and could not pay ₹ 600 due from him. Show the necessary journal entries in the consignee's book.

Solution

			Dr.	**Cr.**
			₹	₹
1.	On sending the acceptance to Exe			
	2011 July 3, Exe	Dr.	30,000	
	To Bills Payable A/c			30,000
2.	On meeting expenses on the consignment:			
	2011 July 3, Exe	Dr.	2,800	
	To Bank			2,800
3.	On meeting his acceptance:			
	2011 Oct. 6, Bills payable	Dr.	30,000	
	To Bank			30,000

4. On sales being effected:

Trade receivables/Bank	Dr.	55,000	
To Exe			55,000

5. On there being a bad debt:

Exe	Dr.	600	
To Trade receivables			600

6. On earning the commission:

Exe	Dr.	5,500	
To Commission Earned A/c			5,500

7. On settling the account to Exe:

Exe	Dr.	16,100	
To Bank			16,100

If the commission includes del-credere commission also, he would not be able to debit Exe for the bad debt. In that case the debit should be to the Commission Earned Account whose net balance will then be ₹ 4,900 and he will have to pay ₹ 16,700 to Exe.

12. ADVANCE BY THE CONSIGNEE VS SECURITY AGAINST THE CONSIGNMENT

Generally the consignor insist the consignee for some advance payment for the goods consigned at the time of delivery of goods. This advance payment is adjusted in full against the amount due by the consignee on account of the goods sold.

But if the advance money deposited by the consignee is in the form of security against the goods consigned then the full amount is not adjusted against the amount due by the consignee to the consignor on account of goods sold in case, there is any unsold inventories left with the consignee. In that case proportionate security in respect of unsold goods is carried forward till the time the respective goods held with the consignee are sold.

An overview of the consignment transaction between consignee and consignor can be depicted with the help of the following chart :

Consignment Account

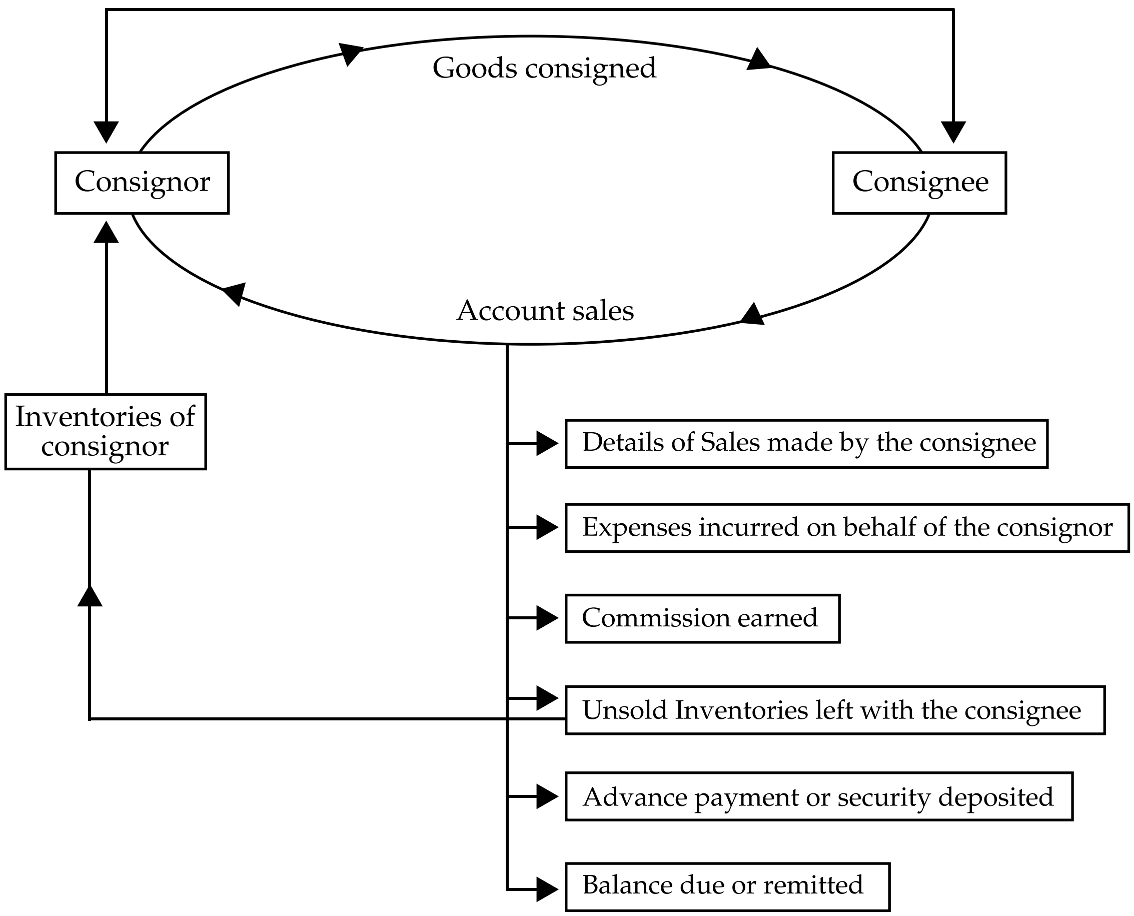


Illustration 3

Miss Rakhi consigned 1,000 radio sets costing ₹ 900 each to Miss Geeta, her agent on 1st July, 2011. Miss Rakhi incurred the following expenditure on sending the consignment.

Freight	₹ 7,650
Insurance	₹ 3,250

Miss Geeta received the delivery of 950 radio sets. An account sale dated 30th November, 2011 showed that 750 sets were sold for ₹ 9,00,000 and Miss Geeta incurred ₹ 10,500 for carriage.

Miss Geeta was entitled to commission 6% on the sales effected by her. She incurred expenses amounting to ₹ 2,500 for repairing the damaged radio sets remaining in the inventories.

Miss Rakhi lodged a claim with the insurance company which was admitted at ₹ 35,000. Show the Consignment Account and Miss Geeta's Account in the books of Miss Rakhi.

Solution

In the books of Miss Rakhi

Consignment Account

	₹	₹		₹.
To Goods sent on Consignment A/c		9,00,000	By Miss Geeta	9,00,000
			By Insurance Co.	35,000
To Cash			By Profit & Loss A/c abnormal loss	10,545
Freight	7,650		By Consignment Inventories	1,84,391
Insurance	3,250	10,900		
To Miss Geeta				
Carriage	10,500			
Repairs	2,500			
Commission	54,000	67,000		
To Profit & Loss A/c		1,52,036		
		11,29,936		11,29,936

Miss Geeta's Account

	₹		₹	₹
To Consignment A/c (Sales)	9,00,000	By Consignment A/c		
		Expenses:		
		Carriage	10,500	
		Repairs	2,500	
		Commission	54,000	67,000
		By Bank		8,33,000
	9,00,000			9,00,000

Note: It is assumed that the agent has remitted the amount due from her.

Working Notes:

1. Abnormal loss :

Cost to the consignor: 50 sets @ ₹ 900		45,000
Add: Proportionate expenses incurred by the consignor	$\frac{50 \times 10,900}{1,000}$	545
		45,545
Less: Insurance claim		(35,000)
		10,545

2. Valuation of Inventories

200 sets @ ₹ 900		1,80,000
Add: Proportionate expenses of the consignor	$\frac{200 \times 10,900}{1,000}$	2,180
Carriage and customs duty paid by the consignee	$\frac{200 \times 10,500}{950}$	2,211
		1,84,391

Illustration 4

Vikram Milk Foods Co. Ltd. of Vikrampur sent to Sunder Stores, Sonepuri 5,000 kgs of baby food packed in 2,000 tins of net weight 1 kg and 6,000 packets of net weight 1/2 kg for sale on consignment basis. The consignee's commission was fixed at 5% of sale proceeds. The cost price and selling price of the product were as under:

	1 kg. tin	*1/2 kg. packet*
	₹	₹
Cost Price	10	6
Selling Price	15	7

The consignment was booked on freight "To Pay" basis, and freight charges came to 2% of selling value. One case containing 50 1 kg. tins was lost in transit and the transport carrier admitted a claim of ₹ 450.

At the end of the first half-year, the following information is gathered from the "Account Sales" sent by the consignee:

(i) Sale proceeds: 1,500 1 kg. tins
4,000 1/2 kg. packets

(ii) Store rent and insurance charges ₹ 600.

Find out the value of closing Inventory on consignment.

Show the Consignment A/c and the Consignee's A/c in the books of Vikram Milk Food Co. Ltd. assuming that the consignees had paid the amount due from them.

Solution

Vikram Milk Foods Co. Ltd.
Consignment to Sonepuri Account

Dr. *Cr.*

		₹		₹	₹
To Goods sent on			By Sunder Stores		
Consignment A/c			1,500 1 kg. tins	22,500	
2,000 1 kg. tins	20,000		4,000 1/2 kg. pkts.	28,000	50,500
6,000 1/2 kg. pkts.	36,000	56,000			
To Sunder Stores:			By Insurance - Claim		450
Freight	1,440		By Profit & Loss A/c -		
Rent and insurance	600		abnormal loss		65
Commission	2,525	4,565	By Inventory A/c		16,915
To Profit & Loss A/c - Profit		7,365			
		67,930			67,930

Sunder Stores, Sonepuri

	₹		₹
To Consignment to Sonepuri Account - Sales Proceeds	50,500	By Consignment to Sonepuri Account -	
		Freight	1,440
		Rent & Insurance	600
		Commission	2,525
		By Bank	45,935
	50,500		50,500

Working Notes:

(i) Sale value of total consignment:

2,000 1 kg. tins	30,000
6,000 1/2 kg. pkts.	42,000
	72,000

(ii) Freight @ 2% of above — 1,440

(iii) Inventories at the end:

450 1 kg. tins @ ₹ 10 (Selling Price ₹ 6,750)	4,500
2,000 1/2 kg. pkts. @ ₹ 6 (Selling Price ₹ 14,000)	12,000
	16,500
Add: Freight 2% of (Selling Price ₹ 20,750)	415
	16,915

(iv) Loss in transit:

Cost of 50 1 kg. tins @ ₹ 10	500
Freight @ 2% of Selling Price ₹ 750	15
	515
Less : Claim	(450)
Loss	65

Illustration 5

Vandana Traders of Delhi purchased 10,000 pieces of Sarees @ ₹ 100 per Saree. Out of these Sarees, 6,000 Sarees were sent on consignment to Vastralaya of Jabalpur at the selling price of ₹ 120 per Saree. The consignors paid ₹ 3,000 for packaging and freight.

Vastralaya sold 5,000 Sarees at ₹ 125 per Saree and incurred ₹ 1,000 for selling expenses and remitted ₹ 5,00,000 to Delhi on account. They are entitled to a commission of 5% on total sales plus a further 20% commission on any surplus price realised over ₹ 120 per Saree.

3,000 Sarees were sold at ₹ 110 per Saree.

Owing to fall in market price, the value of the inventories of Sarees in hand is to be reduced by 10%.

Prepare the Consignment Account and Trading Account in the books of Vandana Traders and their account in the books of the agents Messrs Vastralaya of Jabalpur.

Solution

Vandana Traders, Delhi

Consignment Account

		₹		₹
To Goods sent on Consignment		7,20,000	By Vastrayala (Sales)	6,25,000
To Bank (expenses)		3,000	By Goods Sent on	
To Vastrayala	- Expenses	1,000	Consignment (Loading)	1,20,000
	- Commission	36,250	By Inventories out on	
To Inventories Reserve		18,000	Consignment	1,08,450
To Net Profit		75,200		
		8,53,450		8,53,450

Trading and Profit & Loss Account for the period ending....

		₹		₹
To Purchases	10,00,000		By Sales	3,30,000
Less: Goods on			By Closing Inventories	90,000
Consignment	(6,00,000)	4,00,000		
To By Gross Profit		20,000		
		4,20,000		4,20,000
To Net Profit		95,200	By Gross Profit	20,000
			By Profit on Consignment	75,200
		95,200		95,200

Vastralaya, Jabalpur
Vandana Traders (Delhi) Account

	₹		₹
To Bank (Expenses)	1,000	By Bank/Trade receivables	6,25,000
To Commission	36,250		
To Bank	5,00,000		
To Balance c/d	87,750		
	6,25,000		6,25,000

Working Notes:

		₹
(1)	Commission payable	
	5% on ₹ 6,25,000	31,250
	20% on ₹ 25,000	5,000
		36,250
(2)	The closing Inventories will be	
	1,000 Sarees @ ₹ 120 =	1,20,000
	Add : Proportionate expenses $\left[₹\ 3{,}000 \times \frac{1{,}000}{6{,}000}\right]$	500
		1,20,500
	Less : 10% reduction due to fall in market price	(12,050)
	Consignment Inventories (at loaded amount)	1,08,450
	Loading (₹ 20 × 1,000) - 10% of (₹ 20 × 1,000) = 20,000 - 2,000 =	₹ 18,000

(3) It is better to transfer profit on consignment to profit and loss account instead of trading account.

Illustration 6

Shri Mehta of Bombay consigns 1,000 cases of goods costing ₹ 100 each to Shri Sundaram of Madras. Shri Mehta pays the following expenses in connection with consignment:

	₹
Carriage	1,000
Freight	3,000
Loading charges	1,000
Shri Sundaram sells 700 cases at ₹ 140 per case and incurs the following expenses:	
Clearing charges	850
Warehousing and storage	1,700
Packing and selling expenses	600

It is found that 50 cases have been lost in transit and 100 cases are still in transit.

Shri Sundaram is entitled to a commission of 10% on gross sales. Draw up the Consignment Account and Sundaram's Account in the books of Shri Mehta.

Solution

In the books of Shri Mehta

Consignment of Madras Account

Dr.	₹			*Cr.* ₹
To Goods sent on Consignment	1,00,000	By Sundaram (Sales)		98,000
To Bank (Expenses)	5,000	By Loss in Transit 50 cases @ ₹ 105 each		5,250
To Sundaram (Expenses)	3,150			
To Sundaram (Commission)	9,800	By Consignment Inventories		
To Profit on Consignment to Profit & Loss A/c	11,700	In hand 150 @ ₹ 106 each	15,900	
		In transit 100 @ ₹ 105 each	10,500	26,400
	1,29,650			1,29,650

Sundaram's Account

	₹		₹
To Consignment to Madras A/c	98,000	By Consignment A/c (Expenses)	3,150
		By Consignment A/c (Commission)	9,800
		By Balance c/d	85,050
	98,000		98,000

Working Notes:

(i) Consignor's expenses on 1,000 cases amounts to ₹ 5,000; it comes to ₹ 5 per case. The cost of cases lost will be computed at ₹ 105 per case.

(ii) Sundaram has incurred ₹ 850 on clearing 850 cases, i.e., ₹ 1 per case; while valuing closing Inventories with the agent ₹ 1 per case has been added to cases in hand with the agent.

Illustration 7

Ajay of Mumbai consigned to Vijay of Delhi, goods to be sold at invoice price which represents 125% of cost. Vijay is entitled to a commission of 10% on sales at invoice price and 25% of any excess realised over invoice price. The expenses on freight and insurance incurred by Ajay were ₹ 10,000. The account sales received by Ajay shows that Vijay has effected sales amounting to ₹ 1,00,000 in respect of 75% of the consignment. His selling expenses to be reimbursed were ₹ 8,000. 10% of consignment goods of the value of ₹ 12,500 were destroyed in fire at the Delhi godown and the insurance company paid ₹ 12,000 net of salvage. Vijay remitted the balance in favour of

Ajay. Prepare consignment account and the account of Vijay in the books of Ajay alongwith the necessary calculations.

Solution

Books of Ajay

Consignment Account

Dr.	₹		*Cr.* ₹
To Goods sent on Consignment A/c	1,25,000	By Goods sent on Consignment A/c	25,000
To Cash A/c	10,000	By Abnormal Loss	11,000
To Vijay (Expenses)	8,000	By Vijay (Sales)	1,00,000
To Vijay (Commission)	10,937.50	By Inventories on Consignment A/c	20,250
To Inventories Reserve A/c	3,750	By General Profit & Loss A/c	1,437.50
	1,57,687.50		1,57,687.50

Vijay's Account

Dr.	₹		*Cr.* ₹
To Consignment A/c	1,00,000.00	By Consignment A/c	8,000.00
		By Consignment A/c	10,937.50
		By Bank A/c	81,062.50
	1,00,000.00		1,00,000.00

Working Notes:

1. Calculation of value of goods sent on consignment:

   Abnormal Loss at Invoice price = ₹ 12,500.

   Abnormal Loss as a percentage of total consignment = 10%.

   Hence the value of goods sent on consignment = ₹ 12,500 X 100/ 10 = ₹ 1,25,000.

   Loading of goods sent on consignment = ₹ 1,25,000 X 25/125 = ₹ 25,000.

2. Calculation of abnormal loss (10%):

   Abnormal Loss at Invoice price = ₹ 12,500.

Abnormal Loss at cost = ₹ 12,500 X 100/125	=	₹ 10,000
Proportionate expenses of Ajay (10 % of ₹ 10,000)	=	₹ 1,000
		₹ 11,000

3. Calculation of closing Inventories (15%):

Ajay's Basic Invoice price of consignment	=	₹ 1,25,000
Ajay's expenses on consignment	=	₹ 10,000
		₹ 1,35,000
Value of closing Inventories = 15% of ₹ 1,35,000	=	₹ 20,250
Loading in closing Inventories = ₹ 18,750 X 25/125	=	₹ 3,750

Where ₹ 18,750 (15% of ₹ 1,25,000) is the basic invoice price of the goods sent on consignment remaining unsold.

4. Calculation of commission:

Invoice price of the goods sold = 75% of ₹ 1,25,000 = ₹ 93,750

Excess of selling price over invoice price = ₹ 6,250 (₹ 1,00,000- ₹ 93,750)

Total commission	=	10% of ₹ 93,750 + 25% of ₹ 6,250
	=	₹ 9,375 + ₹ 1,562.50
	=	₹ 10,937.50

Illustration 8

X of Delhi purchased 10,000 metres of cloth for ₹ 2,00,000 of which 5,000 metres were sent on consignment to Y of Agra at the selling price of ₹ 30 per metre. X paid ₹ 5,000 for freight and ₹ 500 for packing etc.

Y sold 4,000 metre at ₹ 40 per metre and incurred ₹ 2,000 for selling expenses. Y is entitled to a commission of 5% on total sales proceeds plus a further 20% on any surplus price realised over ₹ 30 per metre. 3,000 metres were sold at Delhi at ₹ 30 per metre less ₹ 3,000 for expenses and commission. Owing to fall in market price, the Inventories of cloth in hand is to be reduced by 10%.

Prepare the Consignment Account and Trading and Profit & Loss Account in Books of X.

Solution

In the books of Mr. X
Consignment Account

Dr. *Particulars*	*Amount* ₹	*Particulars*	*Cr.* *Amount* ₹
To Goods sent on			
Consignment Account	1,50,000	By Y's account: Sales	1,60,000
		By Goods sent on consignment	50,000
To Bank account:		(cancellation of loading)	
Freight and packing etc.	5,500	By Inventories on consignment	
		(W.N.2)	27,990
To Y's account:			
Selling expenses	2,000		
Commission (W.N.1)	16,000		
To Inventories Reserve (W.N.3)	9,000		
To Profit and loss account (profit			
on consignment transferred)	55,490		
	2,37,990		2,37,990

Trading and Profit and Loss Account
for the year ended……..

Dr. *Particulars*	*Amount* ₹	*Particulars*		*Cr.* *Amount* ₹
To Purchases	2,00,000	By Sales		90,000
To Gross profit c/d	26,000	By Goods sent on consignment		1,00,000
		By Inventories in hand		
		Cost	₹ 40,000	
		Less: 10%	(4,000)	36,000
	2,26,000			2,26,000
To Expenses and commission	3,000	By Gross profit b/d		26,000
To Net profit	78,490	By Consignment A/c		
		(profit on consignment)		55,490
	81,490			81,490

Working Notes:

1. Calculation of commission payable to Y:

	₹
Total sale proceeds of Y	1,60,000
Surplus proceeds realised over ₹ 30 per metre	
[4,000 x ₹ (40-30)]	40,000
Commission:	
5% of total sale proceeds (5% of ₹ 1,60,000)	8,000
20% of surplus (20% of ₹ 40,000)	8,000
	16,000

2. Inventories on Consignment:

	₹
Cost of consignment Inventories (1000 mtrs@ ₹ 30)	30,000
Add: Expenses of consignor	1,100
	31,100
Less: Reduction of 10% due to fall in market price	3,110
	27,990

3. Loading (₹ 10 x 1,000 mtrs) – 10% of (₹ 10 x 1,000 mtrs) 9,000

SELF EXAMINATION QUESTIONS

Choose the most appropriate answer from the given options:

1. P of Delhi sends out 100 boxes of toothpaste costing ₹ 200 each. Each box consist of 12 packets. 60 boxes were sold by consignee at ₹ 20 per packet. Amount of sale value will be:

   (a) ₹ 14,400 (b) ₹ 12,000 (c) ₹ 13,200 (d) ₹ 14,200

2. X of Kolkata sends out 2,000 boxes to Y of Delhi costing ₹ 100 each. Consignor's expenses ₹ 5,000. 1/10th of the boxes were lost in consignee's godown and treated as normal loss. 1,200 boxes were sold by consignee. The value of consignment Inventories will be:

   (a) ₹ 68,333 (b) ₹ 61,500 (c) ₹ 60,000 (d) ₹ 60,250

3. Goods costing ₹ 2,00,000 sent out to consignee at Cost + 25%. Invoice value of the goods will be:

   (a) ₹ 2,50,000 (b) ₹ 2,40,000 (c) ₹ 3,00,000 (d) None

4. Goods costing ₹ 1,80,000 sent out to consignee to show a profit of 20% on Invoice Price. Invoice price of the goods will be:

   (a) ₹ 2,16,000 (b) ₹ 2,25,000 (c) ₹ 2,10,000 (d) None

5. Goods of the Invoice value ₹ 2,40,000 sent out to consignee at 20% profit on cost. The loading amount will be:

   (a) ₹ 40,000 (b) ₹ 48,000 (c) ₹ 50,000 (d) None

6. X sent out certain goods to Y of Delhi. 1/10 of the goods were lost in transit. Invoice value of goods lost ₹ 12,500. Invoice value of goods sent out on consignment will be:

   (a) ₹ 1,20,000 (b) ₹ 1,25,000 (c) ₹ 1,40,000 (d) ₹ 1,00,000

7. Rabin consigned goods for the value of ₹ 8,250 to Raj of Kanpur and paid freight etc. of ₹ 650 and insurance ₹ 400. He drew a bill on Raj for 3 months after date for ₹ 3,000 as an advance against consignment, and discounted the bill for ₹ 2,960. Further, he received Account Sales from Raj showing that, part of the goods had realized gross ₹ 8,350 and that his expenses and commission amounted to ₹ 870. The Inventories unsold was valued at ₹ 2750. Consignee wants to remit a draft for the amount due. The amount of draft will be:

   (a) ₹ 2,130 (b) ₹ 4,480 (c) ₹ 5,130 (d) ₹ 5,090

8. X of Kolkata sends out goods costing ₹ 1,00,000 to Y of Delhi. 3/5th of the goods were sold by consignee for ₹ 70,000. Commission 2% on sales plus 20% of gross sales less all commission exceeds cost price. The amount of Commission will be:

   (a) ₹ 2,833 (b) ₹ 2,900 (c) ₹ 3,000 (d) ₹ 2,800

9. X of Kolkata send out 1,000 bags to Y of Delhi costing ₹ 200 each. Consignor's expenses ₹ 2,000. Y's expenses non-selling ₹ 1000, selling ₹ 2000. 100 bags were lost in transit. Value of lost in transit will be:

   (a) ₹ 20,200 (b) ₹ 20,300 (c) ₹ 20,000 (d) ₹ 23,000

10. X of Kolkata sends out 1,000 bags to Y of Delhi costing ₹ 2,000 each. 600 bags were sold at 10% above cost price. Sales value will be:

    (a) ₹ 13,20,000 (b) ₹ 13,00,000 (c) ₹ 12,00,000 (d) 13,50,000

11. Which of the following statement is not true:

    (a) If del-credere commission is allowed, bad debt will not be recorded in the books of consignor

    (b) If del-credere commission is allowed, bad debt will be debited in consignment account

    (c) Del-credere commission is allowed by consignor to consignee

    (d) Del-credere commission is generally relevant for credit sales

12. X of Kolkata sends out 400 bags to Y of Delhi costing ₹ 200 each. Consignor expenses ₹ 2,000. Y's non selling expenses ₹ 2,000 and selling expenses ₹ 1,000. 300 bags were sold by Y. Value of consignment Inventories will be:

    (a) ₹ 20,400 (b) ₹ 20,200 (c) ₹ 20,000 (d) ₹ 21,000

13. X of Kolkata sent out 2,000 boxes costing 100 each with the instruction that sales are to be made at cost + 45%. X draws a bill on Y for an amount equivalent to 60% of sales value. The amount of bill will be:

    (a) ₹ 1,74,000 (b) ₹ 2,00,000 (c) ₹ 2,90,000 (d) ₹ 1,20,000

14. Which of the following statement is wrong:

    (a) Consignor is the owner of the consignment Inventories
    (b) Del-credere commission is allowed by consignor to protect himself from bad debt
    (c) Proportionate consignor's expenses is added up with consignment Inventories
    (d) All proportionate consignee's expenses will be added up for valuation of consignment Inventories.

15. X of Kolkata sends out 500 bags to Y costing ₹ 400 each at an invoice price of ₹ 500 each. Consignor's expenses ₹ 4,000 consignee's non-selling expenses ₹ 1,000 and selling expenses ₹ 2,000. 400 bags were sold.

    The amount of consignment Inventories at Invoice Price will be:

    (a) ₹ 50,900 (b) ₹ 50,800 (c) ₹ 50,000 (d) ₹ 51,000

16. X of Kolkata sends out 500 bags to Y costing ₹ 400 each at an invoice price of ₹ 500 each. Consignor's expenses ₹ 4,000 consignee's, non-selling expenses ₹ 1000, selling expenses ₹ 2,000. 400 bags were sold. The amount of Inventories Reserve will be

    (a) ₹ 10,000 (b) Nil (c) ₹ 20,000 (d) ₹ 20,400

17. Commission will be shared by:

    (a) Consignor & Consignee (b) Only Consignee
    (c) Only Consignor (d) Third Party

18. X of Kolkata sends out certain goods to Y of Mumbai at cost + 25%. 1/2 of the goods received by Y is sold at ₹ 1,76,000 at 10% above invoice price. Invoice value of goods send out is:

    (a) ₹ 300,000 (b) ₹ 3,20,000 (c) ₹ 180,000 (d) ₹ 340,000

19. X of Kolkata sends out goods costing ₹ 3,00,000 to Y of Mumbai at cost + 25%. Consignor's expenses ₹ 5,000. 1/10th of the goods were lost in transit. Insurance claim received ₹ 3,000. The net loss on account of abnormal loss is:

    (a) ₹ 27,500 (b) ₹ 25,500 (c) ₹ 30,500 (d) ₹ 27,000

20. Rahim of Kolkata sends out 1,000 boxes to Ram of Delhi costing ₹ 100 each at an invoice price of ₹ 120 each. Goods send out on consignment to be credited in general trading will be:

    (a) ₹ 1,00,000 (b) ₹ 1,20,000 (c) ₹ 20,000 (d) None

21. In the books of consignor, the profit of consignment will be transferred to:

    (a) General Trading A/c (b) General P/L A/c (c) Drawings A/c (d) None of these

22. Ram of Kolkata sends out 1,000 boxes to Y of Delhi, costing ₹ 200 each. 1/10th of the boxes

were lost in transit. 2/3rd of the boxes received by consignee is sold at cost + 25%. The amount of sales value will be:

(a) ₹ 1,00,000 (b) ₹ 1,50,000 (c) ₹ 1,20,000 (d) ₹ 1,40,000

23. X of Kolkata sends out goods costing ₹ 80,000 to Y of Mumbai so as to show 20% profit on invoice value. 3/5th of the goods received by consignee is sold at 5% above invoice price. The amount of sales value will be:

(a) ₹ 63,000 (b) ₹ 60,000 (c) ₹ 50,400 (d) ₹ 40,000

24. X of Kolkata sends out certain goods at cost + 25%. Invoice value of goods sends out ₹ 200,000. 4/5th of the goods were sold by consignee at ₹1,76,000. Commission 2% upto invoice value and 10% of any surplus above invoice value.

The amount of commission will be:

(a) ₹ 4,800 (b) ₹ 5,200 (c) ₹ 3,200 (d) ₹ 1,600

25. Ram of Kolkata sends out goods costing ₹ 1,00,000 to Y of Mumbai at 20% profit on invoice price. 1/10th of the goods were lost in transit. ½ of the balance goods were sold. The amount of Inventories reserve on consignment Inventories will be:

(a) ₹ 4,500 (b) ₹ 9,000 (c) ₹ 11,250 (d) None

26. C of Bangalore consigned goods costing ₹ 3,000 to his agent at Delhi. Freight and insurance paid by consignor ₹ 100. Consignee's expenses ₹ 200. 4/5th of the goods were sold for ₹ 3,000. Commission 2% on sales. Consignee want to settle the balance with the help of a bank draft. The amount of draft will be:

(a) ₹ 2,740 (b) ₹ 2,800 (c) ₹ 3,000 (d) ₹ 1,800

27. Out of the following at which point the treatment of "Sales" and "Consignment" is same:

(a) Ownership transfer. (b) Money receive. (c) Inventories outflow. (d) Risk.

28. If del-credere commission is allowed for bad debt, consignee will debit the bad debt amount to:

(a) Commission Earned A/c (b) Consignor's A/c

(c) Trade receivables (Customers) A/c (d) General Trading A/c

29. A proforma invoice is sent by:

(a) Consignee to Consignor (b) Consignor to Consignee

(c) Customer/Debtors to Consignee (d) Customer/Debtors to Consignor

30. Which of the following statement is correct:

(a) Consignee will pass a journal entry in his books at the time of receiving goods from consignor.

(b) Consignee will not pass any journal entry in his books at the time of receiving goods from consignor.

(c) The ownership of goods will be transferred to consignee at the time of receiving the goods.

(d) Consignee will treat consignor as creditor at the time of receiving goods.

31. 1,000 kg of apples are consigned to a wholesaler, the cost being ₹ 3 per kg plus ₹ 400 of freight, it is known that a loss of 15% is unavoidable. The cost per kg will be:

(a) ₹ 5 (b) ₹ 4 (c) ₹ 3.40 (d) ₹ 3

32. A of Mumbai sold goods to B of Delhi, the goods are to be sold at 125% of cost which is invoice price. Commission 10% on sales at invoice price and 25% of any surplus realized above invoice price. 10% of the goods sent out on consignment, invoice value of which is ₹ 12,500 were destroyed. 75% of the total consignment is sold by B at ₹ 1,00,000. What will be the amount of commission payable to B?

(a) ₹ 10,937.50 (b) ₹ 10,000 (c) ₹ 9,000 (d) ₹ 9,700

33. Consignment A/c is prepared in the books of :

(a) Consignor (b) Consignee (c) Third Party (d) None

34. Goods sent on consignment Invoice value ₹ 2,00,000, at cost + $33^{1/3}$ %. 1/5th of the goods were lost in transit. Insurance claim received ₹ 10,000. The amount of abnormal loss to be transferred to General P/L is:

(a) ₹ 30,000 (b) ₹ 20,000 (c) ₹ 35,000 (d) ₹ 25,000

35. X of Kolkata sends out 100 boxes to Y of Delhi costing ₹ 200 each. Consignor's expenses ₹ 4,000. Consignee's non-selling expenses (incurred till goods were reached to godown) ₹ 900 and selling expenses ₹ 500. 1/10th of the boxes were lost in transit. 2/3rd of the boxes received by consignee were sold. The amount of consignment Inventories will be:

(a) ₹ 7,200 (b) ₹ 7,500 (c) ₹ 7,000 (d) ₹ 6,000

36. X of Kolkata sends out goods costing ₹ 1,00,000 to Y of Mumbai at cost + 25%. Consignor's expenses ₹ 2,000. 3/5th of the goods were sold by consignee at ₹ 85,000. Commission 2% on sales + 20% of gross sales less all commission exceeds invoice value. Amount of commission will be:

(a) ₹ 3,083 (b) ₹ 3,000 (c) ₹ 2,500 (d) ₹ 2,000

37. Consignment Inventories will be recorded in the balance sheet of consignor on asset side at:

(a) Invoice Value (b) At Invoice value less Inventories reserve

(c) At lower than cost price (d) At 10% lower than invoice value

38. Which of the following expenses of consignee will be considered as non-selling expenses:

(a) Advertisement (b) Insurance

(c) Selling Expenses (d) None of the above

39. The consignment accounting is made on the following basis:

(a) Accrual (b) Realisation (c) Cash Basis (d) None

40. Goods sent on consignment ₹ 7,60,000. Opening consignment Inventories ₹ 48,000. Cash sales ₹ 7,00,000. Consignor's expenses ₹ 20,000. Consignee's expenses ₹ 12,000. Commission ₹ 20,000. Closing consignment Inventories ₹ 3,00,000. The profit on consignment is:

(a) ₹ 1,50,000 (b) ₹ 1,40,000 (c) ₹ 92,000 (d) None

41. X of Kolkata sends out 100 boxes to Y of Delhi costing ₹ 100 each. Consignor's expenses ₹ 1,000. Consignee's selling expenses ₹ 500. 3/5th of the goods sold by consignee, ½ of the balance goods were lost in consignee's godown due to fire. The value of abnormal loss will be:

(a) ₹ 3,000 (b) ₹ 2,200 (c) ₹ 4,000 (d) None

42. X of Kolkata sends out 1000 boxes costing ₹ 200 each to Y of Delhi. 1/10th of the boxes were lost in transit. 2/3rd of the remaining boxes sold by consignee at cost + 25%. The sale value will be:

(a) ₹ 1,50,000 (b) ₹ 1,40,000 (c) ₹ 1,20,000 (d) ₹ 1,00,000

43. Which of the following item is not credited to consignment account?

(a) Cash sales made by consignee

(b) Credit sales made by consignee

(c) Consignment Inventories

(d) Inventories Reserve on closing consignment Inventories.

44. Goods sent out on consignment ₹ 2,00,000. Consignor's expenses ₹ 5,000. Consignee's expenses ₹ 2,000. Cash sales ₹ 1,00,000, credit sales ₹ 1,10,000. Consignment Inventories ₹ 40,000. Ordinary commission payable to consignee ₹ 3,000. Del-credere commission ₹ 2,000. The amount irrecoverable from customer ₹ 2,000. What will be the profit on consignment?

(a) ₹ 38,000 (b) ₹ 40,000 (c) ₹ 36,000 (d) ₹ 43,000

45. The commission received from consignor will be transferred to which account?

(a) General Trading (b) General P/L (c) Balance Sheet (d) None of these

46. X of Kolkata sends out 1,000 boxes to Y of Delhi costing ₹ 20 each. Consignor's expenses ₹ 2,000. 4/5th of the boxes were sold at ₹ 25 each. The profit on consignment will be:

(a) ₹ 2,400 (b) ₹ 2,000 (c) ₹ 3,000 (d) ₹ 3,500

47. If del-credere commission is allowed by consignor to consignee the bad debt treatment in the books of Consignor will be:

(a) Will not be recorded in consignor's books

(b) Bad Debt will be debited in Consignor's A/c

(c) Bad Debt will be charged to General P/L A/c

(d) Bad Debt will be recoverable along with credit sales

48. The owner of the consignment Inventories is:

(a) Consignor (b) Consignee (c) Trade receivables (d) None

49. The nature of the consignment account is:

(a) Capital in nature (b) Nominal in nature

(c) Realisation A/c in nature (d) Bank A/c in nature

50. Rahim of Kolkata sends out goods of the invoice value ₹ 2,00,000 to Ram of Delhi at cost + 25%. The amount of loading will be:

(a) ₹ 50,000 (b) ₹ 40,000 (c) ₹ 30,000 (d) ₹ 60,000

51. Goods sent to consignment at cost + $33^{1/3}$ %. The percentage of loading on invoice price will be:

(a) 25% (b) $33^{1/3}$ % (c) 20% (d) None

52. The balance of goods sent out on consignment will be transferred to:

(a) General P/L (b) General Trading (c) Balance Sheet (d) Capital A/c

53. X of Kolkata purchased 1,000 boxes costing ₹ 100 each. 200 boxes were sent out to Y of Delhi at cost + 25%. 600 boxes were sold at 120 each. The amount of gross profit to be recorded in general trading account will be:

(a) ₹ 12,000 (b) ₹ 17,000 (c) ₹ (3,000) (d) None

54. In the books of consignee, the profit on consignment will be transferred to:

(a) General Trading A/c (b) General Profit and Loss A/c

(c) Drawings A/c (d) None of the above

55. P of Faridabad sent out goods costing ₹ 45,000 to Y of Delhi at cost + $33^{1/3}$ %. $1/10^{th}$ of goods were lost in transit. $2/3^{rd}$ of the goods received, are sold at 20% above invoice price. The amount of sale value will be:

(a) ₹ 54,000 (b) ₹ 43,200 (c) ₹ 60,000 (d) ₹ 36,000

56. M of Kolkata sent out goods costing ₹ 45,000 to N of Mumbai at cost + $33^{1/3}$ %. $1/10^{th}$ of goods were lost in transit. $2/3^{rd}$ of the goods are sold at 20% above invoice price. ½ of the sales are on credit. The amount of credit sales will be:

(a) ₹ 21,600 (b) ₹ 18,000 (c) ₹ 21,000 (d) ₹ 22,500

57. A of Ahmedabad sent out certain goods so as to show a profit of 20% on invoice price. $1/10^{th}$ of the goods were lost in transit. The cost price of goods lost is ₹20,000. The invoice value of goods sent out is:

(a) ₹ 2,50,000 (b) ₹ 2,00,000 (c) ₹ 2,25,000 (d) ₹ 2,40,000

58. Ram of Delhi sends out goods costing ₹2,00,000 to Krishna of Brindaban. Consignor's expenses ₹5,000. Consignee's expenses in relation to sales ₹ 2,000. $4/5^{th}$ of the goods were sold at 20% above cost. The profit on consignment will be:

(a) ₹ 26,000 (b) ₹ 32,000 (c) ₹ 26,200 (d) ₹ (6,000)

59. Over-riding commission is a commission payable to consignee by consignor for:
    (a) For protecting himself from bad debt
    (b) For making sales above specific price
    (c) As good friend
    (d) As loyalty payment
60. A of Kolkata sends out 500 boxes to B of Delhi costing ₹ 200 each. Consignor's expenses ₹ 5,000. $1/5^{th}$ of the boxes were still in transit. $3/4^{th}$ of the goods received by consignee, were sold. The amount of goods still in transit will be:
    (a) ₹ 20,000 (b) ₹ 21,000 (c) ₹ 21,200 (d) None
61. Consignment account is
    (a) Real account (b) Personal account
    (c) Nominal account (d) None of the above
62. In the books of consignor, the loss on consignment business will be charged to:
    (a) Consignee A/c (b) General Trading A/c
    (c) General P/L A/c (d) Bank A/c
63. Dravid of Delhi sends out goods to Sourav of Kolkata, goods costing ₹ 2,00,000 at cost + 25%, with the instruction to sell it at invoice + 20%. If $4/5^{th}$ of the goods are sold at stipulated selling price and commission allowable 2% on sales. What will be the profit on consignment in the books of consignor?
    (a) ₹ 86,200 (b) ₹ 70,000 (c) ₹ 75,200 (d) ₹ 76,800
64. X of Kolkata sends out goods costing Rs 3,00,000 to Y of Delhi. Goods are to be sold at cost + $33^{1/3}$ %. The consignor asked consignee to pay an advance for an amount equivalent to 60% of sales value. The amount of advance will be:
    (a) ₹ 2,40,000 (b) ₹ 2,00,000 (c) ₹ 3,00,000 (d) None
65. If consignor draws a bill on consignee and discounted it with the banker the discounting charges will be debited in:
    (a) General P/L (b) Trade Payable (c) Consignee (d) Trade receivables
66. X of Kolkata sends out goods costing ₹ 3,00,000 to Y of Delhi. Commission agreement – 2% on sales + 3% on sales as del-credere commission. The entire goods is sold by consignee for ₹ 4 lacs. However, consignee is able to recover ₹ 3,95,000 from the Trade receivables. The amount of profit to be transferred to P/L as net commission by consignee will be:
    (a) ₹ 15,000 (b) ₹ 22,000 (c) ₹ 21,000 (d) ₹ 20,000

ANSWERS

1. (a)	2. (a)	3. (a)	4. (b)	5. (a)
6. (b)	7. (b)	8. (a)	9. (a)	10. (a)
11. (b)	12. (d)	13. (a)	14. (d)	15. (d)
16. (a)	17. (b)	18. (b)	19. (a)	20. (a)
21. (b)	22. (b)	23. (a)	24. (a)	25. (c)
26. (a)	27. (c)	28. (a)	29. (b)	30. (b)
31. (b)	32. (a)	33. (a)	34. (b)	35. (b)
36. (a)	37. (b)	38. (b)	39. (a)	40. (b)
41. (b)	42. (a)	43. (d)	44. (a)	45. (b)
46. (a)	47. (a)	48. (a)	49. (b)	50. (b)
51. (a)	52. (b)	53. (a)	54. (d)	55. (b)
56. (a)	57. (a)	58. (a)	59. (b)	60. (b)
61. (c)	62. (c)	63. (c)	64. (a)	65. (a)
66. (a)				

CHAPTER - 7

ACCOUNTING FOR SPECIAL TRANSACTIONS

Unit 2

Joint Ventures

Learning Objectives:

After studying this unit, you will be able to :

- Understand special features of joint venture transactions,
- Learn the techniques of preparing Joint Venture Account and also the settlement of accounts with the co-venturer(s),
- Familiarise with the use of Memorandum Joint Venture Account,
- Learn the technique of deriving venture profit and its allocation among the venturers,
- Distinguish joint venture with partnership.

1. MEANING OF JOINT VENTURE

A Joint Venture is a very short duration "business" (generally, confined to a single transaction, like, buying some surplus stores and selling them) entered into by two or more persons jointly. Joint Venture may be described as a temporary partnership between two or more persons without the use of the firm name, for a limited purpose. In other words, under Joint Venture, two or more persons agree to undertake a particular venture (e.g. Joint consignment of goods, Joint construction of a building, Joint underwriting of a particular issue of shares or debentures) and to share the profits and losses thereof in an agreed ratio (if agreement is silent on this point, then in equal ratio).

Venture may be for the construction of a building or a bridge, for the supply of certain quantity of materials or labour and even for the supply of technical services. The persons who have so agreed to undertake a Joint Venture are known as 'Joint Venturers' or 'Co-Venturers'. If the co-venturers are in business, then they often supply goods from their regular business for the venture. This limited partnership automatically expires on the completion of the venture for which it was formed.

Let us take two examples to appreciate the nature of joint venture business.

Example 1: A and B decided to purchase Assam Teak in Guwahati and send to Delhi. A of Guwahati purchased Teak of ₹ 1,00,000, spent ₹ 20,000 for transportation and ₹ 8,000 for transit insurance. B of Delhi received the goods. B spent ₹ 2,000 for unloading, ₹ 6,000 for godown rent and ₹ 4,000 for selling expenses. He sold the entire lot for ₹ 1,75,000. They agreed to share profit of the venture in the ratio of A:B = 3:2.

In the above example, A and B are co-venturers. The venture was for sale of a certain quantity of Assam Teak. The venture would be over on sale of such Teak. Obviously some accounting is necessary to find out profit/loss of the venture and settlement of claims of the co-venturers.

Example 2: Mr. Arun and Barun entered into a joint venture for supply of 15,000 pcs. of Bengal handloom sarees to an exporter of Delhi @ ₹ 520 per piece. Arun and Barun contacted handloom weavers and paid advance to them. They collected production by lots and delivered to Delhi in a lot of 1,000 pcs.

In this example, Arun and Barun were co-venturers. The venture was for a special purpose of supplying of 15,000 pcs. of Bengal handloom sarees. The venture was over on supply of such quantity. Obviously, Arun and Barun had to maintain accounts to book all costs relating to the venture and revenue received from the exporter for determining profit/loss of the venture and for settling the claims of co-venturers *inter se*.

2. FEATURES OF JOINT VENTURE

Some important features of joint venture business are as follows:

(i) It is short duration special purpose partnership. Parties in venture are called co-venturers.

(ii) Co-venturers may contribute funds for running the venture or supply Inventories from their regular business.

(iii) Co-venturers share profit/loss of the venture at an agreed ratio likewise partnership.

(iv) Generally profit/loss of the venture is computed on completion of the venture.

(v) Going concern assumption of accounting is not appropriate for joint venture accounting. There does not arise problem of distinction between capital and revenue expenditure. Plant, machinery and other fixed assets when used in venture are first charged to venture account at cost. On completion of venture such assets are revalued and shown as revenue of the venture. Thus, accounting approach for measurement of venture profit is totally different.

3. DISTINCTION OF JOINT VENTURE WITH PARTNERSHIP

Joint Venture differs from Partnership in the following respects:

Basis of Distinction	Joint Venture	Partnership
1. Scope	It is limited to a specific venture.	It is not limited to a specific venture.
2. Persons involved	The persons carrying on business are called co-venturers.	The persons carrying on business are called partners.
3. Ascertainment of profit/loss	The profits/losses are ascertained at the end of specific venture (if venture continues for a short period) or on interim basis annually (if venture continues for a longer period).	The profits/losses are ascertained on an annual basis.
4. Act governing	No specific Act is there.	Partnership firms are governed by the Indian Partnership Act, 1932.
5. Name	There is no need for firm name.	A partnership firm always has a name.
6. Separate set of Books	There is no need for a separate set of books. The accounts can	Separate set of books have to be maintained.

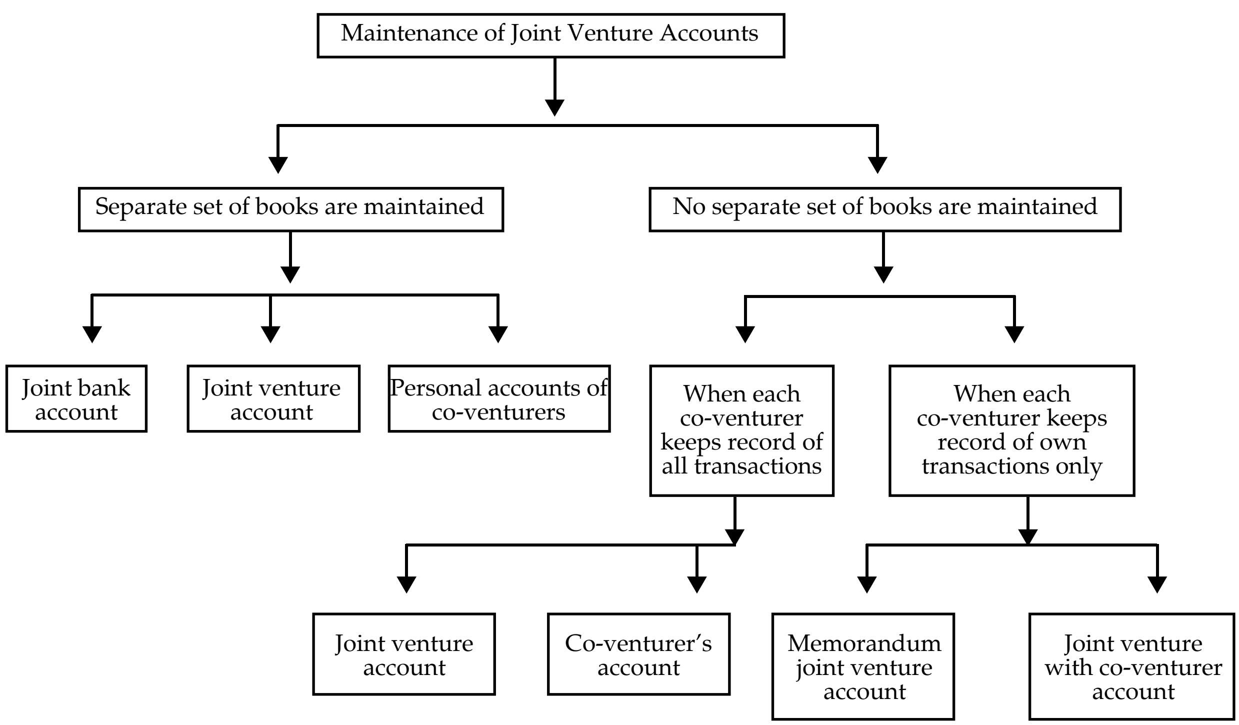
	be maintained even in one of the Co-venturer's books only.	
7. Admission of Minor	A minor cannot be a co-venturer as he is incompetent to contract.	A minor can be admitted to the benefits of the firm.
8. Accounting	Accounting for joint venture is done on liquidation basis.	Accounting for partnership is done on going concern basis.
9. Competition	It is a rule rather than exception that chances of co-venturers in the competing business are very high.	Partners generally do not involve in competing business.

4. METHODS OF MAINTAINING JOINT VENTURE ACCOUNTS

Co-venturers can maintain the accounts for joint venture in the manner that suits them in a particular situation.

Generally there are two ways to keep records of joint venture:

1. When separate set of books are maintained.
2. When no separate set of books are maintained.



4.1. WHEN SEPARATE SET OF BOOKS ARE MAINTAINED

When size of the venture is fairly big, the co-venturers keep separate set of books of account for the joint venture. Joint venture transactions are separate from their regular business activities. In the books of Joint Venture the following accounts are opened:

(i) Joint Bank Account.

(ii) Joint Venture Account.

(iii) Personal Accounts of the Co-venturers or Co-venturers' Accounts.

(i) Joint Bank Account: The co-venturers open a separate bank account for the venture transactions by making initial contributions. The bank account is generally operated jointly. Expenses are met from this Joint Bank Account. Also sales or collections from transactions are deposited to this account. However, sometimes the co-venturers may make direct payments and direct collections. On completion of the venture the Joint Bank Account is closed by paying the balance to co-venturers.

(ii) Joint Venture Account: This account is prepared for measurement of venture profit. This account is debited for all venture expenses and is credited for all sales or collections. Venture profit/loss is transferred to co-venturers' accounts.

(iii) Co-venturers' Accounts: Personal accounts of the venturers are maintained to keep record of their contributions of cash, goods or meeting venture expenditure directly and direct payment received by them on venture transactions. This account is also closed simultaneously with the closure of joint bank account.

The following journal entries are necessary in the books of joint venture:

Journal Entries

(a)	*For initial contribution by the co-venturers in Joint Bank Account*	
	Joint Bank A/c	Dr.
	To Co-venturers' A/c	
(b)	*For expenses paid out of Joint Bank Account*	
	Joint Venture A/c	Dr.
	To Joint Bank A/c	
(c)	*For material supplied by venturers or direct payment made by venturers*	
	Joint Venture A/c	Dr.
	To Co-venturers' A/cs	
(d)	*For sale or payment received*	
	Joint Bank A/c	Dr.
	To Joint Venture A/c	
(e)	*For sale or payment received directly by the venturers*	
	Co-venturers' A/cs	Dr.
	To Joint Venture A/c	
(f)	*For profit on Joint Venture*	
	Joint Venture A/c	Dr.
	To Co-venturers' A/cs	
or	*For loss on Joint Venture*	
	Co-venturers' A/cs	Dr.
	To Joint Venture A/c	
(g)	*For closing the Joint Bank A/c*	
	Co-venturers' A/cs	Dr.
	To Joint Bank A/c	

Illustration 1

B and C enter a joint venture to prepare a film for the Government. The Government agrees to pay ₹ 1,00,000. B contributes ₹ 10,000 and C contributes ₹ 15,000. These amounts are paid into a Joint Bank Account. Payments made out of the joint bank account were:

	₹
Purchase of equipment	6,000
Hire of equipment	5,000
Wages	45,000
Materials	10,000
Office expenses	5,000

B paid ₹ 2,000 as licensing fees. On completion, the film was found defective and Government made a deduction of ₹ 10,000. The equipment was taken over by C at a valuation of ₹ 2,000.

Separate books were maintained for the joint venture whose profits were divided in the ratio of B-2/5 and C-3/5. Give ledger accounts.

Solution

Dr. ***Cr.***

Joint Bank Account

Date	*Particulars*	*Amount (₹)*	*Date*	*Particulars*	*Amount (₹)*
??	To B	10,000	??	By Joint Venture A/c-	
??	To C	15,000		Equipment	6,000
				Hire of equipment	5,000
??	To Joint Venture A/c	90,000		Wages	45,000
				Materials	10,000
				Office expenses	5,000
			??	By B	19,600
				By C	24,400
		1,15,000			1,15,000

Dr. *Cr.*

Joint Venture Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
??	To Joint Bank A/c:		??	By Joint Bank A/c	
	Equipment	6,000		(₹ 1,00,000-10,000)	90,000
	Hire of equipment	5,000			
	Wages	45,000	??	By C	
	Materials	10,000		(Equipment taken)	2,000
	Off. Expenses	5,000			
??	To B - Licensing fee	2,000			
??	To Profit to:				
	B 2/5 7,600				
	C 3/5 11,400				
		19,000			
		92,000			92,000

B's Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
??	To Joint Bank A/c		??	By Joint Bank A/c	10,000
	- Repayment	19,600			
			??	By Joint Venture A/c	2,000
				- Fees	
			??	By Joint Venture A/c	7,600
				- Profit	
		19,600			19,600

C's Account

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
??	To Joint Venture A/c		??	By Joint Bank A/c	15,000
	- Equipment	2,000			
??	To Joint Bank A/c		??	By Joint Venture A/c	
	- Repayment	24,400		- Profit	11,400
		26,400			26,400

4.2 WHEN NO SEPARATE SET OF BOOKS ARE MAINTAINED

When no separate set of books of accounts are maintained for joint venture, each venturer maintains accounts independently for the venture transactions. The standard practice is to keep full records of own transactions as well as transactions of the co-venturer relating to the venture. But sometimes the parties to a venture keep record of their own transactions only. In that case a Memorandum Joint Venture Account is prepared by the parties.

4.2.1 WHEN EACH CO-VENTURER KEEPS RECORDS OF ALL TRANSACTIONS

When venturers maintain full records of joint venture, the following journal entries are necessary:

Journal Entries

(i)	*For supply of goods to venture out of business Inventories*		
	Joint Venture A/c	Dr.	
	To Purchase A/c		
(ii)	*For meeting expenses of venture*		
	Joint Venture A/c	Dr.	
	To Bank A/c		
(iii)	*When co-venturer supplies goods and incurs expenses for venture*		
	Joint Venture A/c	Dr.	
	To Co-venturer A/c		
(iv)	*For venture sale*		
	Bank A/c	Dr.	
	To Joint Venture A/c		
(v)	*For venture sale made by the co-venturer*		
	Co-venturer A/c	Dr.	
	To Joint Venture A/c		
(vi)	*For venture profit*		
	Joint Venture A/c	Dr.	
	To Profit and Loss A/c		(for own shares)
	To Co-venturer A/c		(for co-venturer's share)
(vii)	*For venture loss*		
	Profit and Loss A/c	Dr.	(for own share)
	Co-venturer A/c	Dr.	(for co-venturer's share)
	To Joint Venture A/c		
(viii)	*For settlement of claims*		
	When payment is due to co-venturer		
	Co-venturer A/c	Dr.	
	To Bank A/c		
	When payment is due from co-venturer		
	Bank A/c	Dr.	
	To Co-venturer A/c		

So two special ledger accounts are necessary for joint venture transactions in the books of a venturer: (i) Joint Venture Account and (ii) Co-venturer's A/c.

Illustration 2

A and B entered into a joint venture of underwriting the subscription of the entire share capital of the Copper Mines Ltd. consisting of 1,00,000 equity shares of ₹ 10 each and to pay all expenses upto allotment. The profits were to be shared by them in proportions of 3/5ths and 2/5ths. The consideration in return for this agreement was the allotment of 12,000 other shares of ₹ 10 each to be issued to them as fully paid. A provided funds for registration fees ₹ 12,000, advertising expenses of ₹ 11,000, for expenses on printing and distributing the prospectus amounting to ₹ 7,500 and other printing and stationery expenses of ₹ 2,000. B contributed towards payment of office rent ₹ 3,000, legal charges ₹ 13,750, salary to clerical staff ₹ 9,000 and other petty disbursements of ₹ 1,750. The prospectus was issued and applications fell short by 15,000 shares. A took over these on joint account and paid for the same in full. The venturers received the 12,000 fully paid shares as underwriting commission. They sold their entire holding at ₹ 12.50 less 50 paise brokerage per share. The net proceeds were received by A for 15,000 shares and B for 12,000 shares. Write out the necessary accounts in the books of A showing the final adjustments.

Solution

In the books of A

Joint Venture Account

Dr. Particulars	Amount (₹)	Particulars	*Cr.* Amount (₹)
To Bank A/c - Registration Fee	12,000	By Bank A/c - sale proceeds of	
- Advertising	11,000	15,000 shares ₹ 12.50 each	
- Printing & Distribution		less 50 paise brokerage	1,80,000
of Prospectus	7,500	By B - sale proceeds of 12,000	
- Printing & Stationery	2,000	shares ₹ 12.50 each less	1,44,000
To B - Office Rent	3,000	50 paise per share brokerage	
- Legal Charges	13,750		
- Clerical Staff	9,000		
- Petty Payments	1,750		
To Bank - Cost of Shares	1,50,000		
Net profit to:			
- P & L A/c [3/5]	68,400		
- B [2/5]	45,600		
	3,24,000		3,24,000

B's Account

Particulars	*Amount (₹)*	*Particulars*	*Amount (₹)*
To Joint Venture A/c - Sale		By Joint Venture A/c	
proceeds of shares	1,44,000	- Office Rent	3,000
		- Legal Charges	13,750
		- Clerical Staff	9,000
		- Petty Payments	1,750
		By Joint Venture A/c -	
		share of profit	45,600
		By Bank	70,900
	1,44,000		1,44,000

Illustration 3

With the information given in Illustration 2, let us prepare the necessary accounts in the books of B also.

In the books of B

Joint Venture Account

Particulars	*Amount (₹)*	*Particulars*	*Amount (₹)*
To Bank - Office Rent	3,000	By Bank (Sale of Investments)	1,44,000
- Legal Charge	13,750		
- Clerical Staff	9,000	By A (Sale of Investments)	1,80,000
- Petty Payments	1,750		
To A - Registration Fee	12,000		
- Advertisement	11,000		
- Printing of Prospectus	7,500		
- Printing Stationery	2,000		
- Cost of Shares	1,50,000		
To Net Profit to:			
P&L A/c (2/5)	45,600		
A (3/5)	68,400		
	3,24,000		3,24,000

A's Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Joint Venture A/c		By Joint Venture A/c	
sale proceeds	1,80,000	- Registration Fee	12,000
To Bank A/c	70,900	- Advertisement Charges	11,000
		- Printing & Distribution of	
		- Prospectus	7,500
		- Printing & Stationery	2,000
		- Cost of Shares	1,50,000
		By Joint Venture A/c -	
		share of profit	68,400
	2,50,900		2,50,900

Illustration 4

A and B entered into a joint venture agreement to share the profits and losses in the ratio of 2:1. A supplied goods worth ₹ 60,000 to B incurring expenses amounting to ₹ 2,000 for freight and insurance. During transit goods costing ₹ 5,000 became damaged and a sum of ₹ 3,000 was recovered from the insurance company. B reported that 90% of the remaining goods were sold at a profit of 30% of their original cost. Towards the end of the venture, a fire occurred and as a result the balance Inventories lying unsold with B was damaged. The goods were not insured and B agreed to compensate A by paying in cash 80% of the aggregate of the original cost of such goods plus proportionate expenses incurred by A. Apart from the share of profit of the joint venture, B was also entitled under the agreement to a commission of 5% of net profits of joint venture after charging such commission. Selling expenses incurred by B totalled ₹ 1,000. B had earlier remitted an advance of ₹ 10,000. B duly paid the balance due to A by Bank Draft.

You are required to prepare in A's books:

(i) Joint Venture Account.

(ii) B's Account.

Solution

In the books of A
Joint Venture Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Purchases (Cost of goods supplied)	60,000	By Bank (Insurance claim)	3,000
To Bank (Expenses)	2,000	By B (Sales)	64,350
To B (Expenses)	1,000	By B (agreed value	
To B (Commission - 1/21 of ₹ 8,896)	424	for damaged goods)	4,546
To Profit transferred to:			
Profit & Loss A/c	5,648		
B	2,824		
	71,896		71,896

B's Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Joint Venture A/c (Sales)	64,350	By Bank (Advance)	10,000
To Joint Venture A/c (Claim Portion)	4,546	By Joint Venture A/c (Expenses)	1,000
		By Joint Venture A/c (Commission)	424
		By Joint Venture A/c (Share of Profit)	2,824
		By Bank (Balance received)	54,648
	68,896		68,896

Working Notes:

1. It has been assumed that the goods damaged in transit have no residual value.
2. Computation of Sales:

	₹
Cost of goods sent	60,000
Less: Cost of damaged goods	(5,000)
	55,000
Less: Cost of goods remaining unsold	(5,500)
Cost of goods sold	49,500
Add: Profit @ 30%	14,850
Sales	64,350

3. Claim for loss of fire admitted by B

Cost of goods	5,500
Add: Proportionate expenses	
(2,000 x 5,500)/60,000	183
	5,683
Less: 20%	(1,137)
	4,546

Illustration 5

Ram and Rahim enter into a joint venture to take a building contract for ₹ 24,00,000. They provide the following information regarding the expenditure incurred by them:

	Ram	*Rahim*
	₹	₹
Materials	6,80,000	5,00,000
Cement	1,30,000	1,70,000
Wages	-	2,70,000
Architect's fees	1,00,000	-
License fees	-	50,000
Plant	-	2,00,000

Plant was valued at ₹ 1,00,000 at the end of the contract and Rahim agreed to take it at that value. Contract amount ₹ 24,00,000 was received by Ram. Profits or losses to be shared equally. You are asked to show:

Joint Venture Account and Rahim's Account in the books of Ram.

Solution

In the books of Ram
Joint Venture Account

Dr. Particulars		Amount (₹)	Particulars	*Cr.* Amount (₹)
To Bank A/c:			By Bank A/c	24,00,000
Material	6,80,000		By Rahim's A/c (plant)	1,00,000
Cement	1,30,000			
Architect's fee	1,00,000	9,10,000		
To Rahim's A/c:				
Material	5,00,000			
Cement	1,70,000			
Wages	2,70,000			
License fees	50,000			
Plant	2,00,000	11,90,000		
To Net profit transferred to				
Rahim's A/c	2,00,000			
Profit & Loss A/c	2,00,000	4,00,000		
		25,00,000		25,00,000

Rahim's Account

Dr. Particulars	Amount (₹)	Particulars	*Cr.* Amount (₹)
To Joint Venture A/c (plant)	1,00,000	By Joint Venture A/c (sundries)	11,90,000
To Bank A/c	12,90,000	By Joint Venture A/c (profit)	2,00,000
	13,90,000		13,90,000

Illustration 6

With the information given in illustration 5, prepare Joint Venture Account and Ram's Account in the books of Rahim.

In the books of Rahim

Joint Venture Account

Dr. *Particulars*	₹	*Amount* (₹)	*Particulars*	*Cr.* *Amount* (₹)
To Ram's A/c:			By Ram's A/c (contract amount)	24,00,000
Material	6,80,000		By Plant A/c	1,00,000
Cement	1,30,000			
Architect's fee	1,00,000	9,10,000		
To Bank A/c:				
Material	5,00,000			
Cement	1,70,000			
Wages	2,70,000			
License fees	50,000			
Plant	2,00,000	11,90,000		
To Net profit transferred to:				
Ram's A/c	2,00,000			
Profit & Loss A/c	2,00,000	4,00,000		
		25,00,000		25,00,000

Ram's Account

Dr. *Particulars*	*Amount* (₹)	*Particulars*	*Cr.* *Amount* (₹)
To Joint Venture A/c (contract amount)	24,00,000	By Joint Venture A/c (sundries)	9,10,000
		By Joint Venture A/c (profit)	2,00,000
		By Bank A/c	12,90,000
	24,00,000		24,00,000

4.2.2 WHEN EACH CO-VENTURER KEEPS RECORDS OF THEIR OWN TRANSACTIONS ONLY

Sometimes the venturers find it useless to keep full record of venture transactions. Rather it is considered convenient to keep record of own transactions only. For this purpose, it is necessary to open 'Joint Venture with Co-venturer A/c'. All expenses incurred, materials sent, etc. are debited to this account. Profit earned is also debited to this account while the loss sustained is credited. Any receipt from joint venture or from co-venturer is credited to this account, while any payment to the co-venturer is debited to this account, profit/loss on joint venture cannot be determined from this account. For determination of profit/loss a Memorandum Joint Venture Account is prepared.

Venturers usually pass the following journal entries:

Journal Entries

(a) *For supply of material from stores:*

Joint Venture with X A/c	Dr.
To Purchases A/c	

(b) *For payment of expenses*

Joint Venture with X A/c	Dr.
To Bank/Cash A/c	

(c) *For sale on venture*

Bank A/c	Dr.
To Joint Venture with X A/c	

(d) *For profit on venture*

Joint Venture with X A/c	Dr.
To Profit & Loss A/c	

(e) *For final payment to co-venturer*

Joint Venture with X A/c	Dr.
To Bank A/c	

or For final payment made by co-venturer

Bank A/c	Dr.
To Joint Venture with X A/c	

4.2.2.1 Memorandum Joint Venture Account

It is a rough statement prepared by the venturers for determination of venture profit when they do not maintain full records of venture transactions in the books of accounts. Unless this memorandum account is prepared, the venturer cannot compute venture profit.

Let us now take some illustrations to understand the book keeping system of joint venture, when venturers maintain records of their own transactions only.

Illustration 7

Ram and Gautham entered into a joint venture to buy and sell TV sets, on 1st July, 2011.

On 1.7.2011, Ram sent a draft for ₹ 2,50,000 in favour of Gautham, and on 4.7.2011, the latter purchased 200 sets each at a cost of ₹ 2,000 each. The sets were sent to Ram by lorry under freight "to pay" for ₹ 2,000 and were cleared by Ram on 15.7.2011.

Ram effected sales in the following manner:

Date	*No. of sets*	*Sale price per set*	*Discount on sales price*
16.7.2011	20	3,000	10%
31.7.2011	100	2,800	-
15.8.2011	80	2,700	5%

On 25.8.2011, Ram settled the account by sending a draft in favour of Gautham, profits being shared equally. Gautham does not maintain any books. Show in Ram's book:

(i) Joint Venture with Gautham A/c; and

(ii) Memorandum Joint Venture A/c.

Solution

Ram's Books

Joint Venture with Gautham A/c

Dr. 2011	*Particulars*	*Amount (₹)*	*2011*	*Particulars*	*Cr.* *Amount (₹)*
July 1	To Bank - draft sent on A/c	2,50,000	July 16	By Bank-sale proceeds	54,000
July 15	To Bank - freight	2,000	July 31	By Bank-sale proceeds	2,80,000
" 25	To Profit and Loss A/c share of profit	68,600	Aug 14	By Bank-sale proceeds	2,05,200
	To Bank - draft sent in settlement	2,18,600			
		5,39,200			5,39,200

Memorandum Joint Venture A/c

Particulars		*Amount (₹)*	*Particulars*	*Amount (₹)*
To Cost of 200 sets		4,00,000	By Sales proceeds (net)	
" Freight		2,000	20 sets @ ₹ 2,700 net	54,000
" Profit :			100 sets @ ₹ 2,800 net	2,80,000
Ram	68,600		80 sets @ ₹ 2,565 net	2,05,200
Gautham	68,600			
		1,37,200		
		5,39,200		5,39,200

Illustration 8

D of Delhi and B of Mumbai entered into a joint venture for the purpose of buying and selling second-hand typewriters, B to make purchases and D to effect sales. The profit and loss was to be shared equally by D and B. A sum of ₹ 15,000 was remitted by D to B towards the venture.

B purchased 22 old typewriters for ₹ 15,000 and paid ₹ 9,000 for their reconditioning and sent them to Delhi. His other expenses were: Buying commission ₹ 1,000; Cartage ₹ 200 and Miscellaneous ₹ 100.

D took delivery of the typewriters and paid ₹ 270 for Octroi and ₹ 100 for Cartage. He sold 12 typewriters at ₹ 2,200 each; 4 typewriters at ₹ 2,100 each and 3 typewriters at ₹ 2,000 each. He retained remaining typewriters for his personal use at an agreed value of ₹ 1,500. His other expenses – Insurance ₹ 250; Rent ₹ 400; Brokerage ₹ 1,200 and Miscellaneous ₹ 200.

Each party's ledger contains a record of his own transactions on account of joint venture. Prepare a statement showing the result of the venture and the account of the venturer in D's ledger as it will finally appear, assuming that the matter was finally settled between the parties.

Solution

Statement showing the results of the venture

		₹	₹
Sales			
12 typewriters @		₹ 2,200 each	26,400
4 " "		₹ 2,100 each	8,400
3 " "		₹ 2,000 each	6,000
Taken by D at agreed value			1,500
			42,300
Less: Paid for purchases		15,000	
Repairs		9,000	
Expenses –	Buying Commission	1,000	
	Cartage (200 + 100)	300	
	Misc. Expenses (200 + 100)	300	
	Octroi	270	
	Insurance	250	
	Rent	400	
	Brokerage	1,200	
			(27,720)
Profit on Joint Venture			14,580

In the books of D
Joint Venture with B Account

Particulars		*Amount* (₹)	*Particulars*	*Amount* (₹)
To Cash - remittance to B		15,000	By Cash - Sale proceeds received	40,800
To Cash - expenses				
- Octroi	270		By Drawings (Goods taken for	
- Cartage	100		personal use)	1,500
- Insurance	250			
- Rent	400			
- Brokerage	1,200			
- Misc.	200	2,420		
To Profit and Loss - own				
share of profit (1/2)		7,290		
To Cash - Balance remitted		17,590		
		42,300		42,300

Illustration 9

David of Mumbai and Khosla of Delhi entered into a joint venture for the purpose of buying and selling second-hand motor cars: David to make purchases and Khosla to effect sales. The profit and loss was to be shared equally. Khosla remitted a sum of ₹ 1,50,000 to David towards the venture.

David purchased 5 cars for ₹ 1,60,000 and paid ₹ 60,000 for their reconditioning and sent them to Delhi. He also incurred an expense of ₹ 5,000 in transporting the cars to Delhi.

Khosla sold 4 cars for ₹ 2,40,000 and retained the fifth car for himself at an agreed value of ₹ 50,000. His expenses were: Insurance ₹ 1,000; Garage Rent ₹ 2,000; Brokerage ₹ 2,000; and Sundry Expenses ₹ 400.

Each party's ledger contains a record of his own transactions on account of joint venture. Prepare a Memorandum Joint Venture Account showing the result of the venture and the joint venture account with David in the books of Khosla as it will appear, assuming that the matter was finally settled between the parties.

Solution

Books of Khosla

Joint Venture Account with David

Particulars	*Amount* (₹)	*Particulars*	*Amount* (₹)
To Bank - Remittance	1,50,000	By Bank - Sales	2,40,000
To Bank - Insurance	1,000	By Vehicles A/c - Car Purchase	50,000
To Bank - Garage Rent	2,000		
To Bank - Brokerage	2,000		
To Bank - Sundry	400		
To Profit & Loss A/c			
- Share of Profit	29,800		
To Bank - Final Settlement	1,04,800		
	2,90,000		2,90,000

Memorandum Joint Venture Account

Particulars	*Amount* (₹)	*Particulars*	*Amount* (₹)
To David - cost of cars	1,60,000	By Khosla - Sales	2,40,000
To David - Reconditioning	60,000	By Khosla - car taken	50,000
To David - Transport charges	5,000		
To Khosla - Expenses *	5,400*		
To Net Profit			
- David 29,800			
- Khosla 29,800	59,600		
	2,90,000		2,90,000
* Expenses incurred by Khosla			
- Insurance			1,000
- Garage Rent			2,000
- Brokerage			2,000
- Sundry Expenses			400
			5,400

Illustration 10

A of Delhi and B of Bangalore entered into a joint venture for purchase and sale of one lot of mopeds. The cost of each moped was ₹ 3,600 and the fixed retail selling price; ₹ 4,500. The following were the recorded transactions:

2011

Jan 1 A purchased 100 mopeds paying ₹ 72,000 in cash on account.
A raised a loan from X Bank for ₹ 50,000 at 18% p.a., interest repayable with loan amount on 1.3.2011.
A forwarded 80 mopeds to B incurring ₹ 2,880 as forwarding and insurance charges.

Jan. 7 B received the consignment and paid ₹ 720 as clearing charges.
A sold 5 mopeds for cash.
B sold 20 mopeds for cash.

Feb. 1 B raised a loan of ₹ 1,50,000 from Y Bank, repayable with interest at 18% p.a on 1.3.2011.
B telegraphically transferred ₹ 1,50,000 to A incurring charges of ₹ 50. A paid balance due for the mopeds.

Feb. 26 A sold the balance mopeds for cash.
B sold balance mopeds for cash.
A paid selling expenses ₹ 5,000.
B paid selling expenses ₹ 20,000.

Mar. 1 Accounts settled between the venturer and loans repaid, profit being appropriated equally.

You are required to show Memorandum Joint Venture A/c.

Solution

Memorandum Joint Venture Account
for the period Jan. 1 to March 1, 2011

Particulars		*Amount* (₹)	*Particulars*	*Amount* (₹)
To A :			By Sales :	
Cost of Mopeds		3,60,000	B (80 × 4,500)	3,60,000
Forwarding & Insurance		2,880	A (20 × 4,500)	90,000
Interest (2 months)		1,500		
Selling Expenses		5,000		
To B :				
Clearing Charges		720		
Interest (1 month)		2,250		
Sundry Expenses (Telegraphic transfer charges)		50		
Selling Expenses		20,000		
To Net Profit to				
A	28,800			
B	28,800	57,600		
		4,50,000		4,50,000

Illustration 11

With the data given in Illustration 10, prepare

(1) Joint Venture with B A/c in A's books; and

(2) Joint Venture with A A/c in B's books.

You have to assume that each venturer recorded only such transactions as concluded by him.

Solution

In the books of A

Joint Venture with B Account

Particulars	*Amount* (₹)	*Particulars*	*Amount* (₹)
To Bank A/c - (part payment of cost)	72,000	By Bank A/c (sales proceeds)	22,500
To Bank A/c - (forwarding charges)	2,880	By Bank A/c - (remittance from B)	1,50,000
To Bank A/c - (balance cost of purchases)	2,88,000	By Bank A/c (sales proceeds)	67,500
To Bank A/c - (selling exp.)	5,000	By Bank A/c - (cash received in settlement)	1,58,180
To Interest A/c	1,500		
To Profit & Loss A/c - (share of profit)	28,800		
	3,98,180		3,98,180

Books of B

Joint Venture with A Account

Dr. *Particulars*	*Amount* (₹)	*Particulars*	*Cr.* *Amount* (₹)
To Bank A/c - (clearing charges)	720	By Bank A/c - (Sales proceeds of 20 mopeds)	90,000
To Bank A/c - (remittance including charges)	1,50,000	By Bank A/c - (sales proceeds of 60 mopeds)	2,70,000
To Bank A/c - (selling exp.)	20,000		
To Bank A/c - (interest)	2,250		
To Sundry Expenses	50		
To P & L A/c (share of profit)	28,800		
To Bank A/c - (paid in settlement)	1,58,180		
	3,60,000		3,60,000

Illustration 12

K and A of Nagpur entered into a joint venture to trade in silk goods in the ratio 2:1. On June 1, 2011, K bought goods worth ₹ 7,200 and handed over half of the goods to A. On July 1, 2011, K bought another lot of goods costing ₹ 2,400 and paid ₹ 180 as expenses. On September 1, A purchased goods for ₹ 4,500 and on the same day he sent to K a part of these goods costing ₹ 1,800 and paid ₹ 240 towards expenses. On the same day K remitted ₹ 1,800 to A. The goods were invariably sold by the venturers at a uniform price of 33.33% above cost price excluding expenses. Each of the venturers collected cash proceeds on sales excepting an amount of ₹ 250 owing to K by a customer and this was written off as a loss relating to the venture. In addition, goods costing ₹ 600 in possession of A were destroyed by fire and an amount of ₹ 500 was realised by him as compensation from the Insurance Company. On December 20, unsold goods costing ₹ 1,500 (at cost) were lying with K. Of these, goods costing ₹ 600 were taken by K for personal use and the balance was purchased by him at an agreed value of ₹ 1,000. A disposed of all the goods with him on December 31, excepting some damaged goods costing ₹ 300 which were written off as unsaleable.

Prepare a Memorandum Joint Venture Account to find the amount of profit or loss.

Solution

Memorandum Joint Venture Account

Dr. *Date*	*Particulars*	₹	*Date*	*Particulars*	*Cr.* ₹
	To K:			By K:	
	Cost of goods			Sales (W.N.1)	8,400
	(₹ 7,200 + ₹ 2,400)	9,600		Inventories taken over	
1,600					
	Expenses	180		By A:	
	Bad Debts	250		Sales (W.N.2)	7,200
	To A:			Insurance claim	500
	Cost of goods	4,500			
	Expenses	240			
	To Net Profit:				
	K - 2/3rd	1,953			
	A - 1/3rd	977			
		17,700			17,700

Working Notes:

1. Calculation of sales affected by K

		₹
Goods purchased in first lot	₹ 7,200	
Less: Send to A	(₹ 3,600)	3,600
Goods purchased in another lot		2,400
Goods received from A		1,800
		7,800
Less: Unsold goods:		
Taken for personal use	₹ 600	
Purchase by K (1500-600)	₹ 900	(1,500)
Cost of goods sold		6,300
Add: Profit @ 33.33% on cost		2,100
Sales price of goods sold		8,400

2. Calculation of sales affected by A

		₹
Goods received by K		3,600
Goods purchased	₹ 4,500	
Less: Goods sent to K	(₹ 1,800)	2,700
		6,300
Less: Goods destroyed by fire		(600)
Damaged goods		(300)
Cost of goods sold		5,400
Add: Profit @ 33.33% on costs		1,800
Sales price of goods sold		7,200

SELF EXAMINATION QUESTIONS

Choose the most appropriate answer from the given options

1. M and N enter into a Joint venture where M supplies goods worth ₹ 6,000 and spends ₹ 100 on various expenses. N sells the entire lot for ₹ 7,500 meeting selling expenses amounting to ₹ 200. Profit sharing ratio is equal. N remits to M the amount due. The amount of remittance will be:

   (a) ₹ 6,700 (b) ₹ 7,300 (c) ₹ 6,400 (d) ₹ 6,100

2. A purchased goods costing ₹ 42,500. B sold goods costing ₹ 40,000 at ₹ 50,000. Balance goods were taken over by A at same gross profit percentage as in case of sale. The amount of goods taken over will be:

   (a) ₹ 3,125 (b) ₹ 2,500 (c) ₹ 3,000 (d) None

3. Which of the following statement is true?

   (a) Only one venturer bears the risk

   (b) Only one venturer can sell the goods

   (c) Only one venturer can purchase the goods

   (d) In joint venture, provisions of partnership act applies

4. Which of the following statement is true:

   (a) In case of separate sets of books method of Joint Venture, co-venturer's contribution of goods is debited in Joint Bank A/c

   (b) Co-venturer's contribution in cash is debited in Venturer's personal account

   (c) Discount on discounting of B/R is debited to Venturer's personal account

   (d) Contract money received is credited to Joint Venture Account.

5. For opening Joint Bank account, in case of separate sets of books:

   (a) Venture A/c will be debited and Venturers A/c will be credited

   (b) Joint Bank A/c is debited and Venturers Capital A/c is credited

   (c) Joint Venture A/c is debited and Joint Bank A/c will be credited

   (d) Joint Bank A/c will be debited and Joint Venture A/c will be credited

6. For purchase of plant from Joint Bank Account, in case separate sets of books are maintained, the correct journal entry will be:

   (a) Plant A/c will be debited and Joint Bank A/c will be credited

   (b) Joint Venture A/c will be debited and Joint Bank A/c will be credited

   (c) Plant A/c will be debited and Venturers Capital A/c will be credited

   (d) Joint Venture A/c will be debited and Plant A/c will be credited

7. For material supplied from own Inventories by any of the venturer, the correct journal entry will be: (In case of separate sets of books)

   (a) Joint Venture A/c will be debited and Venturers Capital A/c will be credited

   (b) Joint Venture A/c will be debited and Joint Bank A/c will be credited

   (c) Joint Venture A/c will be debited and Material A/c will be credited

   (d) Joint Bank A/c will be debited and Joint Venture A/c will be credited

8. A and B enter into a joint venture to underwrite the shares of K Ltd. K Ltd make an equity issue of 1,00,000 equity shares of ₹ 10 each. 80% of the issue was subscribed by the public. The profit sharing ratio between A and B is 3:2. The balance shares not subscribed by the public, purchased by A and B in profit sharing ratio. How many shares to be purchased by A.

   (a) 80,000 shares (b) 72,000 shares (c) 12,000 shares (d) 8,000 shares

9. A and B enter into a joint venture to underwrite shares of K Ltd. K Ltd make an equity issue of 2,00,000 equity shares. 80% of the shares underwritten by the venturer. 1,60,000 shares are subscribed by the public. How many shares are to be subscribed by the venturer?

   (a) Nil (b) 32,000 shares (c) 36,000 shares (d) 40,000 shares

10. A and B purchased a piece of land for ₹ 20,000 and sold it for ₹ 60,000 in 2011. Originally A had contributed ₹ 12,000 and B ₹ 8,000. What will be the profit on venture?

   (a) ₹ 40,000 (b) ₹ 20,000 (c) ₹ 60,000 (d) Nil

11.. A and B enter into a joint venture sharing profit and losses in the ratio 2:1. A purchased goods costing ₹ 2,00,000. B sold the goods for ₹ 2,50,000. A is entitled to get 1% commission on purchase and B is entitled to get 5% commission on sales. The profit on venture will be:

   (a) ₹ 35,500 (b) ₹ 36,000 (c) ₹ 34,000 (d) ₹38,000

12. P and Q enter into a Joint Venture sharing profits and losses in the ratio 3:2. P purchased goods costing ₹ 2,00,000. Other expenses of P ₹ 10,000. Q sold the goods for 180,000. Remaining goods were taken over by Q at ₹ 20,000. The amount of final remittance to be paid by Q to P will be:

   (a) ₹ 2,15,000 (b) ₹ 2,04,000 (c) ₹ 2,10,000 (d) None

13. C and D entered into a Joint Venture to construct a bridge. They did not open separate set of books. They shared profits and losses as 3:2. C contributed ₹ 1,50,000 for purchase of materials. D paid wages amounting to ₹ 80,000. Other expenses were paid as:

   C – ₹ 5,000 D – ₹ 15,000

   C purchased one machine for ₹ 20,000. The machine was taken over by C for ₹ 10,000. Total contract value of ₹ 3,00,000 was received by D. What will be the profit on venture?

   (a) ₹ 30,000 (b) ₹ 40,000 (c) ₹ 20,000 (d) ₹ 15,000

14. R and M entered into a joint venture to purchase and sell new year gifts. They agreed to share the profit and losses equally. R purchased goods worth ₹ 1,00,000 and spent

₹ 10,000 in sending the goods to M. He also paid ₹ 5,000 for insurance. M spent ₹ 10,000 as selling expenses and sold goods for ₹ 2,00,000. Remaining goods were taken over by him at ₹ 5000. What will be the amount to be remitted by M to R as final settlement?

(a) ₹1,55,000 (b) ₹1,50,000 (c) ₹11,5000 (d) ₹80,000

15. R and M entered into a joint venture to purchase and sell new year gifts. They agreed to share the profit and losses equally. R purchased goods worth ₹ 100,000 and spent ₹ 10,000 in sending the goods to M. He also paid ₹ 5,000 for insurance. M spent ₹ 10,000 as selling expenses and sold goods for ₹ 2,00,000. Remaining goods were taken over by him at ₹ 5,000. Find out profit on venture?

(a) ₹70,000 (b) ₹75,000 (c) ₹80,000 (d) ₹85,000

16. A and B enter into a joint venture sharing profit and losses in the ratio 3:2. A will purchase goods and B will affect the sale. A purchase goods costing ₹ 200,000. B sold it for ₹ 3,00,000. The venture is terminated after 3 months. A is entitled to get 10% interest on capital invested irrespective of utilization period. The amount of interest received by A will be

(a) ₹ 20,000 (b) ₹ 10,000 (c) ₹ 15,000 (d) ₹ 25,000

17. A bought goods of the value of ₹ 10,000 and consigned them to B to be sold by them on a joint venture, profits being divided equally. A draws a bill on B for an amount equivalent to 80% of cost on consignment. The amount of bill will be:

(a) ₹10,000 (b) ₹8,000 (c) ₹6,000 (d) ₹9,000

18. A bought goods of the value of ₹ 10,000 and consigned them to B to be sold by them on a joint venture, profits being divided equally, A paid ₹ 1,000 for freight and insurance. A draws a bill on B for ₹ 10,000. A got it discounted at ₹ 9,500. B sold the goods for ₹ 15,000. Commission payable to B, ₹ 500. Find out the profit on venture?

(a) ₹3,000 (b) ₹3,500 (c) ₹4,000 (d) ₹3,200

19. A bought goods of the value of ₹ 10,000 and consigned them to B to be sold by them on a joint venture, profits being divided equally, A paid ₹ 1,000 for freight and insurance. A draws a bill on B for ₹ 10,000. A got it discounted at ₹ 9,500. B sold the goods for ₹ 15,000. Commission payable to B, ₹ 500. The amount to be remitted by B to A will be:

(a) ₹12,500 (b) ₹3,000 (c) ₹14,500 (d) ₹13,500

20. If any Inventories is taken over by the venturer, it will be treated as an:

(a) Income of the joint venture, hence credited to Joint Venture Account

(b) Expenses of Joint Venture, hence debited to Joint Venture Account

(c) To be ignored as Joint Venture Transaction

(d) It will be treated in the personal book of the venturer and not in the books of Joint Venture.

21. Advise which of the statement is true:

(a) The Joint Venture can be formed by a single person only.

(b) A legal deed should be drafted before forming Joint Venture.

(c) The profit to be shared between the venturer in agreed ratio

(d) Joint Venture follows going concern concept.

22. A and B were partners in a joint venture sharing profits and losses in the proportion of 3/5th and 2/5th respectively. A supplies goods to the value of ₹ 80,000 and incurs expenses amounting ₹ 6,000. B supplies goods to the value of ₹ 14,000 and his expenses amount to ₹ 2,000. B sells goods on behalf of the joint venture and realizes ₹ 1,50,000. B entitled to a commission of 5% on sales. B settles his account by bank draft. Find out A's share of profit on venture?

(a) ₹ 24,300 (b) ₹ 25,000 (c) ₹ 26,000 (d) ₹ 20,300

23. A and B were partners in a joint venture sharing profits and losses in the proportion of 3/5th and 2/5th respectively. A supplies goods to the value of ₹ 60,000 and incurs expenses amounting ₹ 6,000. B supplies goods to the value of ₹ 16,000 and his expenses amount to ₹ 3,000. B sells goods on behalf of the joint venture and realizes ₹ 1,20,000. B entitled to a commission of 5% on sales. B settles his account by bank draft. How much amount, B will pay to A as final settlement?

(a) ₹83,400 (b) ₹93,200 (c) ₹80,000 (d) ₹66,000

24. A and V enter into a joint venture to sell a consignment of biscuits sharing profits and losses equally. A provides biscuits from Inventories ₹ 10,000. He pays expenses amounting to ₹ 1,000. V incurs further expenses on carriage ₹ 1,000. He receives cash for sales ₹ 15,000. He also takes over goods to the value of ₹ 2,000. What will be the amount to be remitted by V to A?

(a) ₹13,500 (b) ₹15,000 (c) ₹11,000 (d) ₹10,000

25. A and V enter into a joint venture to sell a consignment of biscuits sharing profits and losses equally. A provides biscuits from Inventories ₹ 10,000. He pays expenses amounting to ₹ 1,000. V incurs further expenses on carriage ₹ 1,000. He receives cash for sales ₹ 15,000. He also takes over goods to the value of ₹ 2,000. Find out profit on venture?

(a) ₹3,000 (b) ₹5,000 (c) ₹6,000 (d) ₹3,500

26. A purchased 1000 kg of rice costing ₹ 200 per kg. Paid carriage ₹ 2,000 and insurance ₹ 3,000. 4/5th of the same were sold by B at ₹ 250 per kg. Remaining Inventories were taken over by B at cost. The amount of Inventories taken over will be:

(a) ₹ 40,000 (b) ₹41,000 (c) ₹50,000 (d) ₹50,200

27. Goods costing ₹ 10,000 destroyed by an accident, insurance claim nil.

(a) ₹ 10000 will be credited to Joint Venture Account.

(b) No Entry will be made in the books of Joint Venture

(c) ₹ 10000 will be debited in Joint Venture Account as Loss

(d) ₹ 8000 will be credited in Joint Venture Account

28. A and B were partners in a joint venture sharing profits and losses in the proportion of 3/5th and 2/5th respectively. A supplies goods to the value of ₹ 60,000 and incurs expenses

amounting ₹ 6,000. B supplies goods to the value of ₹ 14,000 and his expenses amount to ₹ 1,000. B sells goods on behalf of the joint venture and realizes ₹ 1,00,000. B entitled to a commission of 5% on sales. B settles his account by bank draft. Find out the profit on venture?

(a) ₹ 14,400 (b) ₹14,000 (c) ₹13,000 (d) ₹13,200

29. A purchased goods costing ₹ 1,00,000. B sold the goods for ₹ 1,50,000. Profit sharing ratio between A and B equal. If same sets of books is maintained, what will be the final remittance?

(a) B will remit ₹ 1,25,000 to A (b) B will remit ₹ 1,50,000 to A

(c) A will remit ₹ 1,00,000 to B (d) B will remit ₹ 25,000 to A

30. A purchased goods costing ₹ 2,00,000, B sold 4/5th of the goods for ₹ 2,50,000. Balance goods were taken over by B at cost less 20%. If same sets of books is maintained, find out profit on venture?

(a) ₹ 82,000 (b) ₹ 90,000 (c) ₹ 50,000 (d) None of these

31. A purchased goods costing ₹ 2,00,000. B sold the goods for ₹ 2,80,000. Unused material costing ₹ 10,000 taken over by A at ₹ 8,000. A is entitled to get 1% commission on purchase. B is entitled to get 2% commission on sales. Profit sharing ratio equal. A's share of profit on venture will be:

(a) ₹ 40,000 (b) ₹ 40,400 (c) ₹ 40,600 (d) ₹ 40,200

32. A and B enter into joint venture sharing profit and loss equally. A purchased 100 kg of rice @ ₹ 20/kg. Brokerage paid ₹ 200, carriage paid ₹ 300. B sold 90 kg of rice @ ₹ 22/kg. Balance rice were taken over by B at cost. The value of rice taken over to be recorded in joint venture will be:

(a) ₹ 200 (b) ₹ 250 (c) ₹ 230 (d) ₹ 220

33. A and B enter into a joint venture sharing profit and losses equally. A purchased 5,000 kg of rice @ ₹ 50/kg. B purchased 1,000 kg of wheat @ ₹ 60/kg. A sold 1,000 kg of wheat @ ₹ 70/kg and B sold 5,000 kg of rice @ ₹ 60/kg. The profit on venture when same sets of books is maintained will be:

(a) ₹ 1,10,000 (b) ₹1,00,000 (c) ₹1,20,000 (d) ₹60,000

34. A and B enter into a joint venture sharing profits and losses equally. A purchased 5000 kg of rice @ ₹ 50/kg. B purchased 1,000 kg of wheat @ ₹ 60/kg. A sold 1,000 kg of wheat @ ₹ 70/kg and B sold 5,000 kg of rice @ ₹ 60/kg. What will be the final remittance?

(a) B will remit ₹ 2,10,000 to A

(b) A will remit ₹ 2,10,000 to B

(c) A will remit ₹ 2,00,000 to B

(d) B will remit ₹ 1,80,000 to A

35. A and B enter into a Joint Venture by opening a joint bank account contributing ₹ 10,00,000. The profit sharing ratio between A and B is 3:2. How much amount to be contributed by A?

(a) ₹6,00,000 (b) ₹4,00,000 (c) ₹3,00,000 (d) ₹5,00,000

36. A, B and C are co-venturer. The relative Profit sharing ratio between A and B is 3:2 and between B and C is also 3:2. Find out the profit sharing ratio between A, B and C.

(a) 3:2:2 (b) 9:6:4 (c) 4:3:2 (d) 3:2:1

37. A and B entered into a joint venture. They opened a joint bank account by contributing ₹ 2,00,000 each. The expenses incurred on venture is exactly equal to ₹ 2,00,000. Once the work is completed, contract money received by cheque ₹ 4,00,000 and in shares ₹ 50,000. The shares are sold for ₹ 40,000. What will be the profit on venture?

(a) ₹2,50,000 (b) ₹2,40,000 (c) ₹ 4,40,000 (d) ₹ 4,50,000

38. If a venturer draws a bill on his co-venturer and if the drawer discounts the bill with same sets of books maintained, the discounting charges will be borne by:

(a) The drawer of the bill (b) The drawee of the bill

(c) The discounting charges will be recorded in memorandum joint venture account

(d) The discounting charges will be borne by bank

39. Which of the following statement is not true?

(a) Joint venture is a going concern

(b) Joint venture is terminable in nature

(c) Joint venture does not follow accrual basis of accounting if lasts for less than a year...

(d) The co-venturer shares the profit in agreed ratio

40. A and B were partners in a joint venture sharing profits and losses in the proportion of $4/5^{th}$ and $1/5^{th}$ respectively. A supplies goods to the value of ₹ 50,000 and incurs expenses amounting to ₹ 5,400. B supplies goods to the value of ₹ 14,000 and his expense amount to ₹ 800. B sells goods on behalf of the joint venture and realizes ₹ 92,000. B is entitled to a commission of 5 percent on sales. B settles his account by bank draft. What will be the final remittance?

(a) B will remit ₹69,160 to A

(b) A will remit ₹69,160 to B

(c) A will remit ₹69,000 to B

(d) B will remit ₹69,000 to A

41. A and B were partners in a joint venture sharing profits and losses in the proportion of $4/5^{th}$ and $1/5^{th}$ respectively. A supplies goods to the value of ₹ 50,000 and incurs expenses amounting to ₹ 5,400. B supplies goods to the value of ₹ 14,000 and his expense amount to ₹ 800. B sells goods on behalf of the joint venture and realizes ₹ 92,000. B is entitled to a

commission of 5 percent on sales. B settles his account by bank draft. What will be the profit on venture?

(a) ₹17,200 (b) ₹17,000 (c) ₹18,000 (d) ₹18,200

42. In a Joint venture A contributes ₹ 5,000 and B contributes ₹ 10,000. Goods are purchased for ₹ 11,200. Expenses amount to ₹ 800. Sales amount to ₹ 14,000 the remaining goods were taken by B at an agree price of ₹ 400. A and B share profit and losses in the ratio of 1:2 respectively. As a final settlement, how much A will receive?

(a) ₹ 5,800 (b) ₹ 6,000 (c) ₹ 5,000 (d) ₹ 10,800

43. Which of the following statement is true?

(a) There is no difference between Joint Venture and Partnership

(b) Consignment and Joint Venture is same

(c) There is no separate act for Joint Venture

(d) In case of Joint Venture, the number of third party is one only.

44. A and B enter into a joint venture sharing profits and losses in the ratio 2:3. Goods purchased by A for ₹ 45,000. Expenses incurred by A ₹ 13,500 and by B ₹ 5,200. B sold the goods for ₹ 85,000. Remaining Inventories taken over by B at ₹ 7,200. What will be the final remittance to be made by B to A:

(a) ₹69,900 (b) ₹11,400 (c) ₹17,100 (d) ₹7,200

45. If separate sets of books is maintained and suppliers grant discount at the time of making the payment for purchase of goods, such discount received will be treated as:

(a) Income of Joint Venture, hence credited to Joint Venture A/c

(b) Will be credited to Joint Bank A/c

(c) Will be credited to Co-venturer's Capital A/c

(d) Will be ignored from the books

46. If unsold goods costing ₹ 20,000 is taken over by Venturer at ₹ 15,000, the Joint Venture A/c will be credited by:

(a) ₹20,000 (b) ₹15,000 (c) ₹5,000 (d) Nil

47. A and B enter into a venture sharing profits and losses in the ratio 2:3. Goods purchased by A for ₹ 45,000. Expenses incurred by A, ₹ 13,500 and by B ₹ 5,200. B sold the goods for ₹ 85,000. Remaining Inventories taken over by B at ₹ 7,200. The profit on venture will be:

(a) ₹ 28,500 (b) ₹ 21,300 (c) ₹ 35,700 (d) ₹ 9,800

48. State which of the statement is **true**?

(a) Memorandum Joint Venture Account is prepared to find out profit on venture

(b) Memorandum Joint Venture Account is prepared to find out amount due from co-venturer

(c) Memorandum Joint Venture Account is prepared when separate sets of books is maintained

(d) In Memorandum Joint Venture Account only one venturer's transaction is recorded

49. A and B enter into a joint venture for purchase and sale of Typewriter. A purchased old Typewriter costing ₹ 1,00,000. Repairing expenses ₹ 10,000, ink expenses ₹ 10,000. B sold it at 20% margin on selling price. The sales value will be:

(a) ₹ 1,25,000 (b) ₹ 1,50,000 (c) ₹ 1,00,000 (d) ₹ 1,40,000

50. Which of the following statement is true?

(a) When separate set of books is maintained, expenses paid by venturer will be credited to joint bank account.

(b) When separate set of books is maintained, expenses paid by venturer will be credited to venturer's capital account.

(c) When separate set of books is maintained, expenses paid by venturer will be credited to Joint venture account.

(d) When separate set of books is maintained, expenses paid by venturer will be credited to Outstanding Expenses Account.

ANSWERS

1.	(a)	2.	(a)	3.	(d)	4.	(d)	5.	(b)	6.	(b)	7.	(a)
8.	(c)	9.	(b)	10.	(a)	11.	(a)	12.	(b)	13.	(b)	14.	(a)
15.	(c)	16.	(a)	17.	(b)	18.	(a)	19.	(b)	20.	(a)	21.	(c)
22.	(a)	23.	(a)	24.	(a)	25.	(b)	26.	(b)	27.	(b)	28.	(b)
29.	(a)	30.	(a)	31.	(d)	32.	(b)	33.	(d)	34.	(a)	35.	(a)
36.	(b)	37.	(b)	38.	(c)	39.	(a)	40.	(a)	41.	(a)	42.	(a)
43.	(c)	44.	(a)	45.	(a)	46.	(b)	47.	(a)	48.	(a)	49.	(b)
50.	(b)												

CHAPTER - 7

ACCOUNTING FOR SPECIAL TRANSACTIONS

Unit 3

Bills of Exchange and Promissory Notes

Learning Objectives

After studying this unit, you will be able to :

- Understand the meaning of Bills of Exchange and Promissory Notes and also try to grasp their underlying features.
- Grasp the accounting treatments relating to issue, acceptance, discounting, maturity and endorsement of bills and notes in the books of drawer and drawee.
- Learn the technique of accounting relating to accommodation bills.
- Learn the special treatment needed in case of insolvency as well as early retirement of bill.

1. BILLS OF EXCHANGE

Often when goods are sold on credit, the seller would like that the purchaser should give a definite promise in writing to pay the amount of the goods on a certain date. Commercial practice has developed to treat these written promises into valuable instruments of credit so much so that when a written promise is made in proper form and is properly stamped, it is supposed that the buyer has discharged his debt and that the seller has received payment. This is because written promises are often accepted by banks and money is advanced against them. Otherwise also they can be passed on from person to person. The written promise is either in the form of a Bill of Exchange or in the form of a promissory note.

A Bill of Exchange has been defined as an "instrument in writing containing an unconditional order signed by the maker directing a certain person to pay a certain sum of money only to or to the order of a certain person or to the bearer of the instrument". When such an order is accepted in writing on the face of the order itself, it becomes a valid bill of exchange. Suppose A order B to pay ₹ 500 three months after date and B accepts this order by signing his name, then it will be a bill of exchange.

The following is a specimen of a properly drawn bill of exchange.

₹ 1,000 Delhi

June, 2011

Three months after date pay to M/s. Mohanlal & Sons or order the sum of ₹ One thousand for value received.

G. Nanda

To,

Gulab Singh & Co.
Sardar Bazaar.

This is known as draft. This will be sent to M/s. Mohanlal & Sons or order as accepted by them who will write across the order as under :

Accepted
Gulab Singh
Partner

After acceptance it becomes a proper bill of exchange.

The following points should be noted:

1. A Bill of Exchange must be in writing.
2. It must be dated.
3. It must contain an order to pay a certain sum of money.
4. The money must be payable to a definite person or to his order to the bearer.
5. The draft must be accepted for payment by the party to whom the order is made.

The party which makes the order is known as the drawer. the party which accepts the order is known as the acceptor and the party to whom the amount has to be paid is known as the payee. The drawer and the payee can be the same.

A Bill of Exchange can be passed on to another person by endorsement. Endorsement on a bill of exchange is made exactly as it is done in the case of a cheque. The primary liability on a bill of exchange is that of the acceptor. If he does not pay, a holder can recover the amount from any of the previous endorsers or the drawee.

The meaning of the term Payee, Drawee and Drawer can be explained with the help of following example :

Sohan sold goods worth ₹ 1,00,000 to Mohan for which the former drew a bill to be paid 3 months after date and sent it to later for acceptance. After acceptance, this bill becomes a bill of exchange. In the mean time, Sohan bought goods worth ₹ 1,00,000 from Ram Lal & Sons and directed Mohan to pay the amount to Ram Lal & Sons.

Specimen of a Bill of Exchange

Payee

₹ 1,00,000/- only

Delhi,
June 25, 2011

Three months after pay to M/s. Ram Lal & Sons or order the sum of ₹ One lakh only,
for value received.

Stamp

To,
Mohan
23, Rajasthali Apartments,
Pitampura, Delhi-110 034.

Accepted
(Mohan)

Sd/-
(Sohan)

Drawee

Drawer

A foreign bill of exchange is generally drawn up in triplicate. Each copy is sent by separate post so that at least one copy reaches the intented party. Of course payment will be made only on one of the copies and when such payment is made the other copies become useless. A foreign bill of exchange drawn like the following :

₹ 5,000 New Delhi

July, 2011

Ninety days after date of this First Bill of Exchange (Second and Thrid of the same tenure and date being unpaid) pay to the order of M/s. Ghosh Sons, London the sum of ₹ Five thousand only, value received.

To, Wallis Sons

M/s. Black White

Birmingham, UK.

Section 12 of the Negotiable Instruments Act provides that all instruments which are not inland instrument are foreign. The following are examples of foreign bills.

1. A bill drawn in India on a person resident outside India and made payable outside India.
2. A bill drawn outside India on a person resident outside India.
3. A bill drawn outside India and made payable in India.
4. A bill drawn outside India and made payable outside India.

2. PROMISSORY NOTES

A promissory note is an instrument in writing, not being a bank note or currency note containing an unconditional undertaking signed by the maker to pay a certain sum of money only to or to the order of a certain person. Under Section 31(2) of the Reserve Bank of India Act a promissory note cannot be made payable to bearer. A promissory note has the following characteristics.

1. It must be in writing.
2. It must contain a clear promise to pay. Mere acknowledgement of a debt is not a promissory note.
3. The promise to pay must be unconditional "I promise to pay ₹ 500 as soon as I can" is not an unconditional promise.
4. The promiser or maker must sign the promissory note.
5. The maker must be a certain person.
6. The payee (the person to whom the payment is promised) must also be certain.
7. The sum payable must be certain. "I promise to pay ₹ 500 plus all fine" is not certain.
8. Payment must be in legal currency of the country.
9. It should not be made payable to the bearer.
10. It should be properly stamped.

Specimen of promissory note :

Specimen of a Promissory Note

₹ 1,00,000/- only

Mohan
84, Sector-1, Noida.
June 20, 2011.

Three months after date I promise to pay Sohan or his order the sum of ₹ One lakh only, for value received

To,
Sohan
D-14, Pitampura, Delhi-110 034.

Stamp

(Mohan)

Payee

Maker

3. RECORD OF BILLS OF EXCHANGE AND PROMISSORY NOTES

A party which receives a Promissory Note or receives an accepted Bill of Exchange will treat it as a new asset under the name of Bills receivable. A party which issues a Promissory Note or accepts a Bill of Exchange will treat it as new liability under the heading of Bills Payable. We shall first deal with the entries in the books of the party which receives promissory notes or bills. (When we talk of bills, we include promissory notes also).

(1) On receipt of Bill :

Bills Receivable Account ...... Dr.

To Drawee/Maker of the note

Example 1 : A accepts a Bill of exchange drawn on him by B. In the books of B the entry will be :

Bills Receivable Account Dr.

To A

(2) A sends to B the acceptance of D. In this case also, the entry in the books of B will be :

Bills Receivable Account ..... Dr.

To A

Example 2 : The person who receives the bill has three options. These are :

(i) He can hold the bill till maturity. (Naturally in this case no further entry is passed until the date of maturity arrives).

(ii) The bill can be endorsed in favour of another party. In this case the entry will be to debit the party which now receives the bill and to credit the Bills Receivable Account.

A ...... Dr.

To Bills Receivable Account

(iii) The Bill of Exchange can be discounted with bank. The bank will deduct a small sum of money as discount and pay rest of the money.

Bank Account Dr. (with the amount actually received)

Discount Account Dr. (with the amount of loss or discount)

To Bills Receivable Account

Example 3 : On the date of maturity there will be two possibilities. The first is that the bill will be paid, that is to say, met or honoured. The entries for this will depend upon what was done to the bill during the period of maturity. If the bill was kept, the cash will be received by the party which originally received the bill. In his books, therefore, the entry will be :

Cash Account ... Dr.

To Bills Receivable Account

But if he has already endorsed the bill in favour of his creditor or if the bill has been discounted with the bank he will not get the amount; it will be the creditor or the bank wich will receive the money. Therefore, in these two cases, no entry will be made in the books of the party which originally received the bill.

The second possibility is that the bill will be dishonoured, that is to say, the bill will not be paid. If the bill is dishonoured, the bill becomes useless and the party from whom the bill was received will be liable to pay the amount (and also the expenses incurred by the party).

Therefore, the following entires will be made :

1. If the bill was kept till maturity then :

   Drawee / Maker of the note .... Dr.

   To Bills Receivable Account

2. If the bill was endorsed in favour of a creditor, the entry is :

   Drawee / Maker of the note .... Dr.

   To Bill payables

3. If the bill was discounted with the bank :

   Drawee / Maker of the note .... Dr.

   To Bank A/c

Thus it will be seen that in case of dishonour, the party which gave the bill has to be debited (because he has become liable to pay the amount). The credit entry is in Bills Receivable Account (if it was retained) or the Creditor or the bank (if it was endorsed/discounted in their favour).

4. TERM OF A BILL

The term of bill of exchange may be of any duration. Usually the term does not exceed 90 days from the date of the bill. When a bill is drawn after sight, the term of the bill begins to run from the date of 'sighting', i.e., when the bill is accepted. When a bill is drawn 'after date', the term of the bill begins to run from the date of drawing the bill.

5. EXPIRY / DUE DATE OF A BILL

The date on which the term of the bill terminates is called as 'Expiry/Due Date of the bill'.

6. DAYS OF GRACE

Every instrument payable otherwise than on demand is entitled to three days of grace.

7. DATE OF MATURITY OF BILL

The date which comes after adding three days to the expiry/due date of a bill, is called the date of maturity.

The maturity of a promissory note or bill of exchang is the date at which it falls due. Every promissory note or bill of exchange which is not expessed to be payable on demand, at sight or on presentment is at maturity on the third day after the day on which it is expressed to be payable.

8. BILL AT SIGHT

Bill at Sight means the instruments in which no time for payment is mentioned. A cheque is always payable on demand. A promissory note or bill of exchange is payable on demand-

(a) when no time for payment is specified, or

(b) when it is expressed to be payable on demand, or at sight or on presentment.

Notes:

(i) 'At sight' and 'presentment' means on demand.

(ii) An instrument payable on demand may be presented for payment at anytime.

(iii) Days of grace is not to added to calculate maturity for such types of bill.

9. BILL AFTER DATE

Bill after date means the instrument in which time for payment is mentioned. A promissory note or bill of exchange is a time instrument when it is expressed to be payable-

(a) after a specified period.

(b) on a specific day

(c) after sight

(d) on the happening of event which is certain to happen

Notes:

(i) The expression 'after sight' means-

(a) in a promissory note, after presentment for sight

(b) in a bill of exchange, after acceptance or noting for non-acceptance or protest for non-acceptance.

(ii) A cheque cannot be a time instrument because the cheque is always payable on demand.

10. HOW TO CALCULATE DUE DATE OF A BILL

The due date of each bill is calculated as follows:

Case	Due Date
(a) When the bill is made payable on a specific date.	(a) That specific date will be the due date.
(b) When the bill is made payable at a stated number of months(s) after date.	(b) That date on which the term of the bill shall expire will be the due date. **Note:** The term shall expire on that day of the month which corresponds with the day on which the bill is dated. If the month in which the period terminates has no corresponding day, the period shall be deemed to expire on the last day of such a month.
(c) When the bill is made payable at a stated number of days after date.	(c) That date which comes after adding stated number of days to the date of bill, shall be the due date. **Note:** The date of Bill is excluded.
(d) When the due date is a public holiday.	(d) The preceding business day will be the due date.
(e) When the due date is an emergency/ unforeseen holiday.	(e) The next following day will be the due date.

Note: The term of a **Bill after sight** commences from the date of acceptance of the bill whereas the term of a **Bill after date** of drawing a bill commences from the date of drawing of bill.

11. HOW TO CALCULATE DATE OF MATURITY IN CASE OF TIME BILLS

In case of time or tenor bills, three days (called days of grace) are added to the due date to arrive at the date of maturity.

12. NOTING CHARGES

It is necessary that the fact of dishonour and the causes of dishonour should be established. If the acceptor can prove that the bill was not properly presented to him for payment, he may escape liability. Therefore, if there is dishonour, or fear of dishonour, the bill will be given to a public official known as "Notary Public". These officials present the bill for payment and if the money is received, they will hand over the money to the original party. But if the bill is dishonoured they will note the fact of dishonuour, with the reasons and give the bill back to their client. For this service they charge a small fee. This fee is known as noting charges. The amount of noting charges is recoverable from the party which is responsible for dishounour.

Suppose X received from Y a bill for ₹ 1,000. On Maturity the bill is dishonoured and ₹ 10 is paid as noting charges. The entry in this case will be

		₹	₹
Y	Dr.	1,010	
To Bills Receivable Account			1,000
To Bank A/c			10

Suppose X had endorsed this bill in favour of Z. In that case entry for dishonoured bill would have been

Y	Dr.	1,010	
To Z			1,010

This is because Z will claim ₹ 1,010 from X and X has the right of recovering ₹ 1,010 from Y. Similarly, if the bill has been discounted with a bank, entry will be :

Y	Dr.	1,010	
To Bank A/c			1,010

13. RENEWAL OF BILL

Sometimes the acceptor is unable to pay the amount and he himself moves that he should be given extension of time. In such a case a new bill will be drawn and the old bill will be cancelled. If this happens entries should be passed for cancellation of the old bill. This is done exactly as already explained for dishonuour. When the new bill is received entries for the receipt of the bill will be repeated.

Illustration 1

Mohan sold goods to Gupta on 1st September, 2011 for ₹ 1,600. Gupta immediately accepted a three months bill. On due date Gupta requested that the bill be renewed for a fresh period of two months. Mohan agrees provided interest at 9% was paid immediately in cash. To this Gupta was agreeable. The second bill was met on due date. Give Journal entries in the books of Mohan.

Solution

Books of Mohan

Journal

2011			*Dr.* ₹	*Cr.* ₹
Sept. 1	Gupta	Dr.	1,600	
	To Sales Account			1,600
	(Sales of goods to Gupta as per Invoice No...)			
	Bills Receivable Account	Dr.	1,600	
	To Gupta			1,600
	(3 months acceptance received from Gupta for the amount due from him)			
Dec. 4	Gupta	Dr.	1,600	
	To Bills Receivable Account			1,600
	(Gupta's acceptance cancelled because of renewal)			
	Gupta	Dr.	24	
	To interest			24
	(Interest @ 9% on ₹ 1,600 due from Gupta for 2 months because of renewal)			
	Bills Receivable Account	Dr.	1,600	
	Cash Account	Dr.	24	
	To Gupta			1,624
	[New acceptance for 2 months for ₹ 1,600 and Cash (for interest) received from Gupta]			
2012				
Feb. 7	Cash Account	Dr.	1,600	
	To Bills Receivable Account			1,600
	(Cash received against Gupta's second acceptance)			

Illustration 2

On 1st January, 2011, A sells goods for ₹ 10,000 to B and draws a bill at three months for the amount. B accepts it and returns it to A. On 1st March, 2011, B retires his acceptance under rebate of 12% per annum. Record these transactions in the journals of A.

Solution

Journal Entries in the books of A

Date 2011	*Particulars*		*Dr.* ₹	*Cr.* ₹
Jan. 1	B's account	Dr.	10,000	
	To Sales account			10,000
	(Being the goods sold to B on credit)			
	Bills receivable account	Dr.	10,000	
	To B's account			10,000
	(Being the acceptance of bill received)			
March 1	Bank account	Dr.	9,900	
	Rebate on bills account	Dr.	100	
	To Bills receivable account			10,000
	(Being retirement of bill by B one month before maturity, the rebate being given to him at 12% p.a.)			

Illustration 3

On 1st January, 2011, A sells goods for ₹ 10,000 to B and draws a bill at three months for the amount. B accepts it and returns it to A. On 1st March, 2011, B retires his acceptance under rebate of 12% per annum. Record these transactions in the journals of B.

Solution

Journal Entries in the books of B

Date 2011	*Particulars*		*Debit* ₹	*Credit* ₹
Jan. 1	Purchases account	Dr.	10,000	
	To A's account			10,000
	(Being the goods purchased from A on credit)			
	A's account	Dr.	10,000	
	To Bills payable account			10,000
	(Being the acceptance of bill given to A)			
March 1	Bills payable account	Dr.	10,000	
	To Bank account			9,900
	To Rebate on bills account			100
	(Being the bill discharged under rebate @ 12% p.a.)			

Working Note :

Calculation of rebate:

10,000 x 12/100 x 1/12 = ₹ 100

Illustration 4

A draws upon B three Bills of Exchange of ₹ 3,000, ₹ 2,000 and ₹ 1,000 respectively. A week later his first bill was mutually cancelled, B agreeing to pay 50% of the amount in cash immediately and for the balance plus interest ₹ 100, he accepted a fresh Bill drawn by A. This new bill was endorsed to C who discounted the same with his bankers for ₹ 1,500. The second bill was discounted by A at 5%. This bill on maturity was returned dishonoured (nothing charge being ₹ 30). The third bill was retained till maturity when it was duly met.

Give the necessary journal entries recording the above transactions in the books of A.

Solution

Journal of A

		Dr. ₹	*Cr.* ₹
Bills Receivable A/c	Dr.	6,000	
To B			6,000
(Three bills for ₹ 3,000, ₹ 2,000 and ₹ 1,000 drawn on B and duly accepted by him received)			
B	Dr.	3,000	
To Bills Receivable A/c			3,000
(Bill received from B cancelled for renewal)			
Cash Account	Dr.	1,500	
Bill Receivable Account	Dr.	1,600	
To B			3,000
To Interest Account			100
(Amount received on cancellation of the first bill, 50% along with a new bill for 50% of the amount plus interest ₹ 100)			
C	Dr.	1,600	
To Bills Receivable A/c			1,600
(A's acceptance endorsed in favour of C)			
Bank A/c	Dr.	1,900	
Discount A/c	Dr.	100	
To Bills Receivable A/c			2,000
(Second Bill for ₹ 2,000 discounted with the bank @ 5%)			
B	Dr.	2,030	
To Bank A/c			2,030
(Second Bill for ₹ 2,000 discounted with the Bank dishonoured, noting charges ₹ 30 paid by the Bank)			
Bank A/c	Dr.	1,000	
To Bills Receivable A/c			1,000
(Amount received on maturity of the third bill)			

Note : It is assumed that the bill for ₹ 1,600 has not yet fallen due for payment.

Illustration 5

Journalise the following transactions in K. Katrak's books.

(i) Katrak's acceptance to Basu for ₹ 2,500 discharged by a cash payment of ₹ 1,000 and a new bill for the balance plus ₹ 50 for interest.

(ii) G. Gupta's acceptance for ₹ 4,000 which was endorsed by Katrak to M. Mehta was dishonoured. Mehta paid ₹ 20 noting charges. Bill withdrawn against cheque.

(iii) D. Dalal retires a bill for ₹ 2,000 drawn on him by Katrak for ₹ 10 discount.

(iv) Katrak's acceptance to P. Patel for ₹ 5,000 discharged by P. Mody's acceptance to Katrak for a similar amount.

Solution

Books of K. Katrak
Journal Entries

			Dr. ₹	*Cr.* ₹
(i)	Bills Payable Account	Dr.	2,500	
	Interest Account	Dr.	50	
	To Cash A/c			1,000
	To Bills Payable Account			1,550
	(Bills Payable to Basu discharged by cash payment of ₹ 1,000 and a new bill for ₹ 1,550 including ₹ 50 as interest)			
(ii)	(a) G. Gupta	Dr.	4,020	
	To M. Mehta			4,020
	(G. Gupta's acceptance for ₹ 4,000 endorsed to M. Mehta dishonoured, ₹ 20 paid by M. Mehta as noting charges)			
	(b) M. Mehta	Dr.	4,020	
	To Bank Account			4,020
	(Payment to M. Mehta on withdrawal of bill earlier received from Mr. G. Gupta)			
(iii)	Bank Account	Dr.	1,990	
	Discount Account	Dr.	10	
	To Bills Receivable Account			2,000
	(Payment received from D. Dalal against his acceptance for ₹ 2,000. Allowed him a discount of ₹ 10)			
(iv)	Bills Payable Account	Dr.	5,000	
	To Bills Receivable Account			5,000
	(Bills Receivable from M. Mody endorsed to P. Patel in settlement of bills payable issued to him earlier)			

Illustration 6

Journalise the folllowing in the books of Don :

(i) Bob informs Don that Ray's acceptance for ₹ 3,000 has been dishonoured and noting charges are ₹ 40. Bob accepts ₹ 1,000 cash and the balance as bill at three months at interest of 10%. Don accepts from Ray his acceptance at two months plus interest @ 12% p.a.

(ii) James owes Don ₹ 3,200; he sends Don's own acceptance in favour of Ralph for ₹ 3,160; in full settlement.

(iii) Don meets his acceptance in favour of Singh for ₹ 4,500 by endorsing John's acceptance for ₹ 4,450 in full settlement.

(iv) Ray's acceptance in favour of Don retired one month before due date, interest is taken at the rate of 6% p.a.

Solution

Books of Don

				Dr. ₹	Cr. ₹
(i)	(a)	Ray	Dr.	3,040	
		To Bob			3,040
		(Ray's acceptance endorsed to Bob dishonoured on due date nothing charges paid by Bob ₹ 40)			
	(b)	Bob	Dr.	3,040	
		Interest	Dr.	51	
		To Cash			1,000
		To Bills Payable A/c			2,091
		(Amount payable to Bob ₹ 3,040 settled by cash payment ₹ 1,000 and issue of new bill for ₹ 2,091 including interest ₹ 51 for three months on ₹ 2,040 @ 10% p.a.)			
	(c)	Bills Receivable A/c	Dr.	3,100.80	
		To Ray			3,040.00
		To Interest			60.80
		(Bill received from Ray for ₹ 3,040 due against earlier acceptance dishonoured plus ₹ 60.80 interest for two months @ 12% p.a.)			
(ii)		Bills Payable A/c	Dr.	3,160	
		Discount A/c	Dr.	40	
		To James			3,200
		(Cancellation of bills payable to Ralph for ₹ 3,160 in settlement of ₹ 3,200 due from James)			

(iii)	Bills payable A/c	Dr.	4,500	
	To Bills Receivable A/c			4,450
	To Discount A/c			50
	(Settlement of acceptance issued to Mr. Singh by endorsement of John's Acceptance for ₹ 4,450)			
(iv)	Bank A/c	Dr.	3,085.30	
	Discount A/c	Dr.	15.50	
	Total Bills Receivable A/c			3,100.80
	(Amount received fro Ray in settlement of Bills Payable, retired one month before due date)			

14. ACCOMMODATION BILLS

Bills of Exchange are usually drawn to facilitate trade transmission, that is, bills are meant to finance actual purchase and sale of goods. But the mechanism of bill can be utilised to raise finance also. Suppose Bhalla needs, finance for three months. In that case he may persuade his friend Kohli to accept his draft. The bill of exchange may then be taken by Bhalla to his bank and get it discounted there. Thus, Bhalla will be able to make use of funds. When the three months period expires, Bhalla will send the requisite amount to Kohli and Kohli will meet the bill. Thus, Bhalla is able to raise money for his use. If both Bhalla and Kohli need money, the same devise can be used. Either Bhalla accepts a bill of exchange or Kohli does. In either case, the bill will be discounted with the bank and the proceeds divided between the two parties according to mutual agreement. The discounting charges must also be borne by the two parties in the same ratio in which the proceeds are divided. On the due date the acceptor will receive from the other party his share. The bill will then be met. When bills are used for such a purpose, they are known as accommodation bills.

Entries are passed in the books of two parties exactly in the way already pointed out for ordinary bills. The only additional entry to be passed is for sending the remittance to the other party and also debiting the other party with the shared amount of discount.

15. INSOLVENCY

Insolvency of a person means that he is unable to pay his liabilities. This means that bills accepted by him will be dishonoured. Therefore when it is known that a person has become insolvent, entry for dishonour of his acceptance must be passed. Later on, something may be received from his estate. When and if an amount is received, cash account will be debited and the personal account of the debtor will be credited. The remaining amount will be irrecoverable and, threfore, should be written off as bad debt. The student should be careful to calculate the amount actually received from an insolvent's estate and amount to be written off only after preparing his account.

In the books of drawee of the bill, the amount not ultimately paid by him due to insolvency, should be credited to deficiency account.

Illustration 7

R owed ₹ 1,000 to S. On 1st October, 2011, R accepted a bill drawn by S for the amount at 3 months. S got the bill discounted with his bank for ₹ 900 on 3rd October, 2011. Before the due date, R approached S for renewal of the bill. S agreed on the conditions that ₹ 500 be paid immediately together with interest on the remaining amount at 12% per annum for 3 months and for the balance, R should accept a new bill at three months. These arrangements were carried out. But afterwards, R became insolvent and 40% of the amount could be recovered from his estate.

Pass journal entries (with narration) in the books of S.

Solution

In the books of S
Journal Entries

Particulars	*L.F.*		*Dr.* ₹	*Cr.* ₹
Bills Receivable A/c		Dr.	1,000	
To R				1,000
(Being a 3 month's bill drawn on R for the amount due)				
Bank A/c		Dr.	900	
Discount A/c		Dr.		100
To Bills Receivable A/c				1,000
(Being the bill discounted)				
R		Dr.	1,000	
To Bank A/c				1,000
(Being the bill cancelled up due to R's inability to pay it)				
R		Dr.	15	
To Interest A/c				15
(Being the interest due on ₹ 500 @ 12% for 3 months)				
Bank A/c		Dr.	515	
To R				515
(Being the receipt of a portion of the amount due on the bill together with interest)				
Bills Receivable A/c		Dr.	500	
To R				500
(Being the new bill drawn for the balance)				
R		Dr.	500	
To Bills Receivable A/c				500
(Being the dishonour of the bill due to R's insolvency)				
Bank A/c		Dr.	200	
Bad Debts A/c		Dr.	300	
To R				500
(Being the receipt of 40% of the amount due on the bill from R's estate)				

Illustration 8

On 1st July, 2011 G drew a bill for ₹ 80,000 for 3 months on H for mutual accommodation. H accepted the bill of exchange. G had purchased goods worth ₹ 81,000 from J on the same date. G endorsed H's acceptance to J in full settlement. On 1st September, 2011, J purchased goods worth ₹ 90,000 from H. J endorsed the bill of exchange received from G to H and paid ₹ 9,000 in full settlement of the amount due to H. On 1st October, 2011, H purchased goods worth ₹ 1,00,000 from G. H paid the amount due to G by cheque. Give the necessary Journal Entries in the books of H.

Solution

In the books of H

Journal Entries

Date	*Particulars*		*Dr.* ₹	*Cr.* ₹
1.7.2011	G's account	Dr.	80,000	
	To Bills payable account			80,000
	(Acceptance of bill drawn by G)			
1.9.2011	J's account	Dr.	90,000	
	To Sales account			90,000
	(Sales made to J)			
1.9.2011	Bills receivable account	Dr.	80,000	
	Bank account	Dr.	9,000	
	Discount account	Dr.	1,000	
	To J's account			90,000
	(Acceptance received from J's endorsement of bill received from G for ₹ 80,000 and ₹ 9,000 received in full settlement of the amount due)			
1.9.2011	Bills payable account	Dr.	80,000	
	To Bills receivable account			80,000
	(Own acceptance received from J's endorsement, cancelled)			
1.10.2011	Purchase account	Dr.	1,00,000	
	To G's account			1,00,000
	(Purchases made from G)			
	G's account	Dr.	20,000	
	To Bank account			20,000
	(Amount paid to G after adjusting ₹ 80,000 for accommodation extended to him)			

Illustration 9

For the mutual accommodation of 'X' and 'Y' on 1st April, 2011, 'X' drew a four months' bill on 'Y' for ₹ 4,000. 'Y' returned the bill after acceptance of the same date. 'X' discounts the bill from his bankers @ 6% per annum and remit 50% of the proceed to 'Y'. On due date 'X' is unable to send the amount due and therefore 'Y' draws a bill for ₹ 7,000, which is duly accepted by 'X'. 'Y' discounts the bill for ₹ 6,600 and sends ₹ 1,300 to 'X'. Before the bill is due for payment 'X' becomes insolvent. Later 25 paise in a rupee received from his estate.

Record Journal entries in the books of 'X'.

Solution

In the books of X

Journal Entries

Date 2011	*Particulars*		*Debit* ₹	*Credit* ₹
April 1	Bills receivable account	Dr.	4,000	
	To Y's account			4,000
	(Acceptance received from Y for mutual accommodation)			
April 1	Bank account	Dr.	3,920	
	Discount account	Dr.	80	
	To Bills receivable account			4,000
	(Bill discounted for ₹ 3,920)			
	Y's account	Dr.	2,000	
	To Cash account			1,960
	To Discount account			40
	(Half of proceeds remitted to Y)			
Aug. 4	Y's account	Dr.	7,000	
	To Bills payable account			7,000
	(Acceptance given to Y, being unable to remit the due amount)			
	Bank account	Dr.	1300	
	Discount account $40 \times \frac{(2,000 + 1,300)}{660}$	Dr.	200	
	To Y's account			1500
	(Amount received from Y and discount amount credited to him)			
	Bills payable account	Dr.	7,000	
	To Y's account			7,000
	(Acceptance to Y dishonoured because of insolvency)			
	Y account	Dr.	3,500	
	To Bank account			875
	To Deficiency account			2,625
	(Amount paid @ 25 paise in a rupee and balance credited to deficiency account as being unable to pay)			

Illustration 10

Anil draws a bill for ₹ 9,000 on Sanjay on 5th April, 2011 for 3 months, which Sanjay returns it to Anil after accepting the same. Anil gets it discounted with the bank for ₹ 8,820 on 8th April, 2011 and remits one-third amount to Sanjay. On the due date Anil fails to remit the amount due to Sanjay, but he accepts a bill for ₹ 12,600 for three months, which Sanjay discounts it for ₹ 12,330 and remits ₹ 2,220 to Anil. Before the maturity of the renewed bill Anil becomes insolvent and only 50% was realized from his estate on 15th October, 2011.

Pass necessary Journal entries for the above transactions in the books of Anil.

Solution

In the books of Anil

Journal Entries

Date 2011	*Particulars*		*Debit Amount* ₹	*Credit Amount* ₹
April 5	Bills receivable account	Dr.	9,000	
	To Sanjay's account			9,000
	(Being acceptance received from Sanjay for mutual accommodation)			
April 5	Bank account	Dr.	8,820	
	Discount account	Dr.	180	
	To Bills receivable account			9,000
	(Being bill discounted with bank)			
April 5	Sanjay's account	Dr.	3,000	
	To Bank account			2,940
	To Discount account			60
	(Being one-third proceeds of the bill sent to Sanjay)			
July 8	Sanjay's account	Dr.	12,600	
	To Bills payable account			12,600
	(Being Acceptance given)			
July 8	Bank account	Dr.	2,220	
	Discount account	Dr.	180	
	To Sanjay's account			2,400
	(Being proceeds of second bill received from Sanjay)			
Oct.11	Bills payable account	Dr.	12,600	
	To Sanjay's account			12,600
	(Being bill dishonoured due to insolvency)			
Oct.15	Sanjay's account (6,000+2,400)	Dr.	8,400	
	To Bank account			4,200
	To Deficiency account			4,200
	(Being insolvent, only 50% amount paid to Sanjay)			

Illustration 11

Bose and Mitra were in need of funds. On 1st May, 2011 Bose accepted Mitra's draft for ₹ 6,000 at 3 months. After 3 days, Mitra got it discounted at 6% p.a. and remitted 1/3 of the proceeds to Bose. On the due date Mitra was not able to sent the amount instead he accepted to Bose's bill for ₹ 4,500 at two months. Bose got it discounted for ₹ 4,420 on 7th August, 2011. Out of this ₹ 280 were sent to Mitra. Early in October Mitra became insolvent. His estate paid 40%.

Give Journal entries in the books of Bose.

Solution

In the books of Bose

Journal Entries

2011			Dr. ₹	Cr. ₹
May 1	Mitra	Dr.	6,000	
	To Bills Payable Account			6,000
	(Mitra's draft for ₹ 6,000 accepted for mutal accommodation)			
May 4	Bank Account	Dr.	1,970	
	Discount Account	Dr.	30	
	To Mitra			2,000
	(One third of the proceeds of bill after discount received from Mitra)			
Aug. 4	Bills Receivable Account	Dr.	4,500	
	To Mitra			4,500
	(Acceptance received from Mitra to cover the amount due from him)			
	Bank Account	Dr.	4,420	
	Discount Account	Dr.	80	
	To Bills Receivable Account			4,500
	(Mitra's acceptance discounted for ₹ 4,420)			
	Bills Payable Account	Dr.	6,000	
	To Bank Account			6,000
	(Own acceptance due on this date met)			
	Mitra	Dr.	357.47	
	To Bank Account			280.00
	To Discount Account*			77.47
	(Amount remitted to Mitra after discounting the bill)			
Oct. 7	Mitra	Dr.	4,500	
	To Bank Account			4,500
	(Mitra's acceptance dishonoured because of his insolvency)			
	Bank Account	Dr.	1742.99	
	Bad Debts Account	Dr.	2614.48	
	To Mitra			4357.47
	(Amount received and debts written off in respect of amount due for Mitra)			

Illustration 12

Mr. David draws two bills of exchange on 1.1.2011 for ₹ 6,000 and ₹ 10,000. The bills of exchange for ₹ 6,000 is for two months while the bill of exchange for ₹ 10,000 is for three months. These bills are accepted by Mr. Thomas. On 4.3.2011, Mr. Thomas requests Mr. David to renew the first bill with interest at 18% p.a. for a period of two months. Mr. David agrees to this proposal. On 20.3.2011, Mr. Thomas retires the acceptance for ₹ 10,000, the interest rebate i.e. discount being ₹ 100. Before the due date of the renewed bill, Mr. Thomas becomes insolvent and only 50 paise in a rupee could be recovered from his estate.

You are to give the journal entries in the books of Mr. David.

Solution

Journal Entries in the books of Mr. David

2011			*Dr.* (₹)	*Cr.*(₹)
Jan. 1	Bills receivable (No. 1) A/c	Dr.	6,000	
	Bills receivable (No. 2) A/c	Dr.	10,000	
	To Mr. Thomas's A/c			16,000
	(Being drawing of bills receivable No. 1 due for maturity on 4.3.2011 and bills receivable No. 2 due for maturity on 4.4.2011)			
March 4	Mr. Thomas's A/c	Dr.	6,000	
	To Bills receivable (No.1) A/c			6,000
	(Being the reversal entry for bill No.1 on agreed renewal)			
March 4	Bills receivable (No. 3) A/c	Dr.	6,180	
	To Interest A/c			180
	To Mr. Thomas's A/c			6,000
	(Being the drawing of bill of exchange no. 3 due for maturity on 7.5.2011 together with interest at 18% p.a. in lieu of the original acceptance of Mr. Thomas)			
March 20	Bank A/c	Dr.	9,900	
	Discount A/c	Dr.	100	
	To Bills receivable (No. 2) A/c			10,000
	(Being the amount received on retirement of bills No.2 before the due date)			

May 7	Mr. Thomas's A/c	Dr.	6,180	
	To Bills receivable (No. 3) A/c			6,180
	(Being the amount due from Mr. Thomas on dishonour of his acceptance on presentation on the due date)			
May 7	Bank A/c	Dr.	3,090	
	To Mr. Thomas's A/c			3,090
	(Being the amount received from official assignee of Mr. Thomas at 50 paise per rupee against dishonoured bill)			
May 7	Bad debts A/c	Dr.	3,090	
	To Mr. Thomas's A/c			3,090
	(Being the balance 50% debt in Mr. Thomas's Account arising out of dishonoured bill written as bad)			

16. BILLS OF COLLECTION

When a person received a bill of exchange he may decide to retain the bill till the date of maturity. But in order to ensure safety, he may send it to bank with instructions that the bill should be retained till maturity and should be realised on that date. This does not mean discounting because the bank will not credit the client until the amount is actually realised. If the bill is sent to the bank with such instructions it is known as "Bill sent for collection".

It is better to make a record of this also in books by passing following entry:

Bills for Collection Account	Dr.
To Bills Receivable Account	
When the amount is realised the entry will be	
Bank Account	Dr.
To Bills for Collection Account	
When the amount is not honoured, the entry will be	
Party (from whom the bill was received)	Dr.
To Bills for collections A/c	

17. RETIREMENT OF BILLS OF EXCHANGE

We have seen that renewal of a bill of exchange is made when a person does not have sufficient fund to pay for the bill of exchange on the due date and he requires a further period of credit. Many a time instances do arise when the acceptor has spare funds much before the maturity date of the bill of exchange accepted by him. In such circumstances he approaches the payee of the bill of exchange and asks him whether the payee is prepared to accept cash before the maturity date. In such cases the acceptor gets a certain rebate or interest or discount for premature payment. The interest becomes the income of the acceptor and expense of the payee. It is a consideration of premature payment.

Illustration 13

On 1st January, 2011, Vilas draws a bill of exchange for ₹ 10,000 due for payment after 3 months on Eknath. Eknath accepts to this bill of exchange. On 4th March, 2011. Eknath retires the bill of exchange at a discount of 12% p.a. You are asked to show the journal entries in the books of Eknath.

Solution

Journal entries in the books of Eknath

Date	*Particulars*	*L.F.*	*Debit* ₹	*Credit* ₹
Jan. 1	Vilas A/c	Dr.	10,000	
	To Bills Payable A/c			10,000
	(Being the bill draws by him accepted)			
Mar. 4	Bills Payable A/c	Dr.	10,000	
	To Bank A/c			9,900
	To Interest A/c (Discount A/c)			100
	(Being retirement of acceptance 1 month before maturity, interest allowed at 12% p.a.)			

Illustration 14

On 1st January, 2011, Vilas draws a Bill of Exchange for ₹ 10,000 due for payment after 3 months on Eknath. Eknath accepts to this bill of exchange. On 4th March, 2011. Eknath retires the bill of exchange at a discount of 12% p.a. You are asked to show the journal entries in the books of Vilas.

Solution

Journal entries in the books of Vilas

Date 2011	*Particulars*		*Debit* ₹	*Credit* ₹
Jan. 1	Bills Receivable A/c	Dr.	10,000	
	To Eknath A/c			10,000
	(Being bill of exchange no . . . drawn on Eknath due for payment on 4th April 2011)			
Mar. 4	Bank A/c	Dr.	9,900	
	Interest A/c (Discount) A/c	Dr.	100	
	To Bills Receivable A/c			10,000
	(Being retirement of bill of exchange due for maturity on 4th April, 2011 by Eknath 1 month before maturity, the rebate being given to him at 12% p.a.)			

18. BILLS RECEIVABLE AND BILLS PAYABLE BOOKS

Bills receivable and bills payable books are journals (Day Books) to record in a chronological order the details of bills receivable and bills payable. When large number of bill transactions take place in an organisation, it is convenient to maintain these books. Wherein any bill transaction takes place, the same is entered in the Day Books in the first instance. Postings to individual Debtors or Creditors accounts are made from the Day Books. Also totals of bills received or accepted are posted periodically to Bills Receivable Account and Bills Payable Account respectively.

Bills receivable book and bills payable book are very useful for following up the status of outstanding bills. When there are large number of bills and these bills fall due on different dates, some of these bills may not be honoured on maturity due to some reason or the other. It is possible from these Day Books to trace the details of the outstanding bills and to identify the reasons for not honouring the bills. Given below are forms of Day Books for both bills receivable and bills payable:

Bills Receivable Book (Folio No . . .)

Date of receipt	Voucher No.	Party from whom Received	Acceptor	Date of Bill	Due Date	Place of Payment	Amt. ₹	LF.	Mode of Disposal

Bills Payable Book (Folio No . . .)

Date of Acceptance	Drawer	Payee	Date of Bill	Due Date	Place of Payment	Amount ₹	L.F.	Mode of Disposal

SELF EXAMINATION QUESTIONS

Choose the most appropriate answer from the given options:

1. On 1.1.2011, X draws a bill on Y for ₹ 20,000 for 3 months maturity date of the bill will be:

   (a) 1.4.2011 (b) 3.4.2011 (c) 4.4.2011 (d) 4.5.2011

2. On 15.8.2011, X draws a bill on Y for 3 months for ₹ 20,000. 18th Nov. was a sudden holiday, maturity date of the bill will be:

   (a) 17th Nov (b) 18th Nov (c) 19th Nov (d) 15th Nov

3. On 16.6.2011 X draws a bill on Y for ₹ 25,000 for 30 days. 19th July is a public holiday, maturity date of the bill will be:

   (a) 19th July (b) 18th July (c) 17th July (d) 16th July

4. X draws a bill on Y for ₹ 30,000 on 1.1.2011. X accepts the same on 4.1.2011 for period of 3 months after date. What will be the maturity date of the bill:

   (a) 4.4.2011 (b) 3.4.2011 (c) 7.4.2011 (d) 8.4.2011

5. X draws a bill on Y. X endorsed the bill to Z. The payee of the bill will be

   (a) X (b) Y (c) Z (d) None

6. A bill of ₹ 12,000 was discounted by A with the banker for ₹ 11,880. At maturity, the bill returned dishonoured, noting charges ₹ 20. How much amount will the bank deduct from A's bank balance at the time of such dishonour?

   (a) ₹ 12,000 (b) ₹ 11,880 (c) ₹ 12,020 (d) ₹ 11,900

7. X draws a bill on Y for ₹ 20,000 on 1.1.2011 for 3 months after sight, date of acceptance is 6.1.2011. Maturity date of the bill will be:

(a) 8.4.2011 (b) 9.4.2011 (c) 10.4.2011 (d) 11.4.2011

8. X sold goods to Y for ₹ 1,00,000. Y paid cash ₹ 30,000. X will grant 2% discount on balance, and Y request X to draw a bill for balance, the amount of bill will be:

(a) ₹ 98,000 (b) ₹ 68,000 (c) ₹ 68,600 (d) ₹ 70,000

9. On 1.1.2011, X draws a bill on Y for ₹ 50,000 for 3 months. X got the bill discounted 4.1.2011 at 12% rate. The amount of discount on bill will be:

(a) ₹ 1,500 (b) ₹ 1,600 (c) ₹ 1,800 (d) ₹ 1,450

10. Mr. A draws a bill on Mr. Y for ₹ 30,000 on 1.1.2011 for 3 months. On 4.2.2011, X got the bill discounted at 12% rate. The amount of discount will be:

(a) ₹ 900 (b) ₹ 600 (c) ₹ 300 (d) ₹ 650

11. X draws a bill on Y for ₹ 20,000 for 3 months on 1.1.2011. The bill is discounted with banker at a charge of ₹ 100. At maturity the bill return dishonoured. In the books of X, for dishonour, the bank account will be credited by:

(a) ₹ 19,900 (b) ₹ 20,000 (c) ₹ 20,100 (d) ₹ 19,800

12. On 1.1.2011, X draws a bill on Y for ₹ 10,000. At maturity Y request X to renew the bill for 2 month at 12% p.a. interest. Amount of interest will be:

(a) ₹ 200 (b) ₹ 150 (c) ₹ 180 (d) ₹ 190

13. On 1.1.2011, X draws a bill on Y for ₹ 15,000 for 3 months. At maturity Y request X to accept ₹ 5,000 in cash and for balance to draw a fresh bill for 2 months together with 12% p.a. interest, amount of interest will be:

(a) ₹ 200 (b) ₹ 300 (c) ₹ 240 (d) ₹ 380

14. On 1.8.2011, X draws a bill on Y "for 30 days after sight". The date of acceptance is 8.8.2011. The maturity date of the bill will be:

(a) 8.9.2011 (b) 10.9.2011 (c) 11.9.2011 (d) 9.9.2011

15. On 1.6.2011, X draws a bill on Y for ₹ 25,000. At maturity Y request X to accept ₹ 5,000 in cash and noting charges incurred ₹ 100 and for the balance X draw a bill on Y for 2 months at 12% p.a. Interest amount will be:

(a) ₹ 410 (b) ₹ 420 (c) ₹ 440 (d) ₹ 400

16. On 1.1.2011, X draws a bill on Y for ₹ 50,000. At maturity, the bill returned dishonoured as Y become insolvent and 40 paise per rupee is recovered from his estate. The amount recovered is:

(a) ₹ 20,000 (b) Nil (c) ₹ 30,000 (d) 40 paise

17. X draws a bill on Y for ₹ 3,000. X endorsed to Z. Y will pay the amount of the bill to:

(a) X (b) Z (c) To himself (d) None

18. On 1.1.2011, X draws a bill on Y for 3 months for ₹ 10,000. On 4.3.2011, Y pay the bill to X at 12% p.a. discount, the amount of discount will be:

    (a) 100 (b) 200 (c) 300 (d) 50

19. Ram draws on Aslam a bill for ₹ 60,000 on 1.4.2011 for 2 months. Aslam accepts the bill and sends it to Ram who gets it discounted for ₹ 58,800. Ram immediately remits ₹ 19,600 to Aslam. On due date, Ram being unable to remit the amount due and accepts a bill for ₹ 84,000 for 2 months which is discounted by Aslam for ₹ 82,200. Aslam sends ₹ 14,800 to Ram out of the same. How much discount will be borne by Ram at the time of 14,800 remittance.

    (a) ₹ 1,200 (b) ₹ 1,800 (c) ₹ 1,100 (d) ₹ 800

20. Mr. Bobby sold goods worth ₹ 25,000 to Mr Bonny. Bonny immediately accepted a bill on 1.11.2011, payable after 2 months. Bobby discounted this bill @ 18% p.a. on 15.11.2011. On the due date Bonny failed to discharge the bill. Later on Bonny became insolvent and 50 paise is recovered from Bonny's estate. How much amount of bad debt will be recorded in the books of Bobby:

    (a) ₹ 12,500 (b) ₹ 9,437 (c) ₹ 11,687 (d) ₹ 13,650

21. The purpose of accommodation bill is:
    (a) To finance actual purchase or sale of goods
    (b) To facilitate trade transmission
    (c) When both parties are in need of funds
    (d) None of the above

22. M sold goods worth of ₹ 50,000 to N. On 1.10.2011, N immediately accepted a three month bill. On due date, N requested that the bill be renewed for a fresh period of 3 months. N agrees to pay interest @ 18% p.a. in cash. How much interest to be paid in cash by N?

    (a) ₹ 2,250 (b) ₹ 1,800 (c) ₹ 2,000 (d) ₹ 1,100

23. On 1.1.2011, X draws a bill on Y for ₹ 30,000. At maturity Y request X to draw a fresh bill for 2 months together with 12% pa. interest. Noting charges ₹ 100. The amount of interest will be:

    (a) ₹ 600 (b) ₹ 602 (c) ₹ 500 (d) ₹ 550

24. On 18.2.2011 A draw a bill on B for ₹ 10,000. B accepted the bill on 21.2.2011. The bill is drawn for 30 days after sight. The maturity date of the bill will be:

    (a) 24.3.2011 (b) 22.3.2011 (c) 26.3.2011 (d) 21.3.2011

25. X sold goods to Y for ₹ 3,00,000. ½ of the amount will be received in cash and balance in B/R. For what amount X should draw the bill on Y.

    (a) ₹ 1,50,000 (b) ₹ 3,00,000 (c) ₹ 1,00,000 (d) ₹ 1,20,000

26. A draws a bill on B for ₹ 50,000 for 3 months. At maturity, the bill returned dishonoured, noting charges ₹ 500. 40 paise in a rupee is recovered from B's estate. The amount of deficiency to be recorded on insolvency in the books of B will be:

(a) ₹ 20,200 (b) ₹ 30,300 (c) ₹ 19,800 (d) ₹ 19,000

27. A sold goods to B for ₹ 20,000. A will grant 5% discount to B. B requested A to draw a bill. The amount of the bill will be:

(a) ₹ 20,000 (b) ₹ 19,000 (c) ₹ 19,200 (d) Nil

28. Fees paid in cash to Notary Public is charged by:

(a) Drawer (b) Drawee (c) Holder of the bill of exchange (d) None

29. A draws a bill on B for ₹ 50,000. A endorsed it to C in full settlement of ₹ 50,500. Noting charges of ₹ 200 as the bill returned dishonoured. A want to pay the amount to C at 2% discount. The amount to be paid by A to C will be:

(a) ₹ 49,000 (b) ₹ 49,490 (c) ₹ 49,686 (d) ₹ 50,500

30. A draws a bill on B for ₹ 1,00,000. A endorsed the bill to C. The bill return dishonoured. Noting charges ₹1,000. B request A to accept the amount at 2% discount by a single cheque. The cheque amount will be:

(a) ₹ 98,000 (b) ₹ 98,980 (c) ₹ 99,000 (d) ₹ 99,980

31. S draws 2 bills of exchange on 1.1.2011 for Rs 3,000 and ₹ 5,000 respectively. The bill of exchange for ₹3,000 is for 2 months, while the bill of exchange for ₹ 5,000 is for 3 months. These bills are accepted by K. On 4.3.2011 K requests S to renew the first bill with interest at 18% p.a. for a period of 2 months. S agrees to this proposal. On 20.3.2011 K retires the acceptance for ₹ 5,000 the interest rebate i.e., discount being ₹ 50.

Before the due date of the renewed bill K becomes insolvent and only 60 paise in a rupee can be recovered from his estate. How much bad debt will be recorded in the books of S:

(a) ₹ 1,236 (b) ₹ 1,854 (c) ₹ 3,090 (d) ₹ 3,000

32. The promissory note should be signed by:

(a) Drawer (b) Drawee (c) Payee (d) Promiser

33. Kuntal draws a bill on Shyam for ₹ 3,000. Kuntal endorsed it to Ram. Ram endorsed it to Rahim. The payee of the bill will be:

(a) Kuntal (b) Ram (c) Shyam (d) Rahim

34. A bill is drawn on 29th Jan. 2011 for one month after date. The date of acceptance is 2nd Feb. 2011. The maturity date of the bill will be:

(a) 28th February (b) 1st March (c) 2nd March (d) 3rd March

35. Mr. Rex accepted a bill drawn by Mr. Rabin. Mr. Rabin endorsed the bill to Mr Shekar. On the due date, the bill is dishonored as Mr Rex became insolvent. To record the dishonor of the bill in the books of Mr. Rabin, which of the following accounts should be credited?

(a) Mr. Rex's account (b) Bills Receivable account

(c) Mr Shekar's account (d) Bills payable account

36. Which of the following statements is true?

(a) A bill cannot be endorsed more than two times

(b) A bill is drawn by purchaser

(c) A bill contains an unconditional promise to pay

(d) Noting charges are borne by the drawee in the event of dishonour of bill.

37. For mutual accommodation of A and B, B accepted a bill drawn on him by A for 2 months for ₹ 6,000. The said bill is discounted at 12% pa. and remitted $1/3^{rd}$ of the proceeds to B. The amount remitted by A to B will be:

(a) ₹ 2,000 (b) ₹ 1,960 (c) ₹ 1,920 (d) ₹ 1,900

38. Lara draws an accommodation bill on Sachin. The proceeds are to be borne between Sachin and Lara in the ratio of 3:1. The amount of bill ₹ 6000, discounting charges ₹ 120. Discount borne by Sachin will be:

(a) ₹ 90 (b) ₹ 120 (c) ₹ 100 (d) None

39. A draws a bill on B for ₹ 4,500 for mutual accommodation in the ratio 2:1. A got it discounted at ₹ 4,230 and remitted $1/3^{rd}$ of the proceeds to B. At the time of maturity, how much amount A should remit to B such that B can pay off the bill?

(a) ₹ 3,000 (b) ₹ 2,880 (c) ₹ 2,920 (d) ₹ 3,010

40. Suman drew a bill on Sonu for ₹ 4,500 for mutual accommodation in the ratio 2:1. Sonu accepted the bill and returned to Suman. Suman discounted the bill for ₹ 4,230 and remitted $1/3^{rd}$ proceeds to Sonu. Before the due date, not having funds to meet the bill, Sonu drew a bill on Suman for ₹ 6,300 on the same terms as to mutual accommodation. The second bill was discounted for ₹ 6,120. The first bill was honored on the due date and a net amount of ₹ 1,080 was remitted to Suman by Sonu. The proportionate discount charge on both the bills is to be borne by Suman is:

(a) ₹ 180 (b) ₹ 150 (c) ₹ 300 (d) ₹ 120

41. Which of the following instrument is not a negotiable instrument:

(a) Bearer cheque (b) Promissory note (c) Bill of exchange (d) Account Payee Crossed cheque

42. On 1.1.2011 Vikas draws a bill of exchange for ₹ 10,000 due for payment after 3 months on Ekta. Ekta accepts to this bill of exchange. On 4.3.2011, Ekta retires the bill of exchange at a discount of 12% p.a. Which of the discount is correct for premature payment in the books of Ekta?

(a) ₹ 120 (b) ₹ 100 (c) ₹ 140 (d) ₹ 160

43. Neelam sold goods to Dhiman for ₹ 4,000 on 1.5.2011. On the same day, she drew on Dhiman a bill for the amount for 3 months, which Dhiman duly accepted. Neelam got the bill discounted

with her bank before the due date, Dhiman became insolvent. Later, his estate could pay only 40% of the amount due. What will be the amount of deficiency in the books of Dhiman.

(a) ₹ 3,200 (b) ₹ 2,200 (c) ₹ 2,400 (d) ₹ 2,000

44. Which of the following is not a foreign bill:
    (a) A bill drawn in India, on a person resident outside India and made payable outside India.
    (b) A bill drawn outside India, on a person resident outside India
    (c) A bill drawn outside India, made payable in India
    (d) A bill drawn on a person resident in India made payable in India

45. A drew a bill on B for ₹ 50,000 for 3 months. Proceeds are to be shared equally. A got the bill discounted at 12% p.a. and remits required proceeds to B. The amount of such remittance will be:

    (a) ₹ 24,250 (b) ₹ 25,000 (c) ₹ 16,167 (d) ₹ 32,333

46. From the following information, find out who can draw the bill if Mr A sold goods to B:

    (a) A will draw a bill on B (b) B will draw a bill on A

    (c) None of these (d) Third party will draw a bill on A

47. When the bill are to be produced to notary public:

    (a) At the time of drawing the bill (b) At the time of acceptance of the bill

    (c) At the time of dishonour of the bill (d) At the time of "bill for collection"

48. Which of the following statement is false:

    (a) B/R is a negotiable instrument (b) B/R must be accepted by drawee.

    (c) There can be three parties in respect of bills of exchange – drawer, drawee & payee

    (d) Oral bill of exchange is also valid.

49. Under which circumstances drawer and payee is same person:
    (a) When drawer discounted the bill with banker
    (b) When drawer endorse the bill to the third party
    (c) When drawer held the bill till maturity
    (d) When drawee rejects to accept the bill

50. Which of the following statement is **true**:

    (a) Noting charge is an expense to be borne by drawer

    (b) Noting charge is an expense to be borne by drawee

    (c) Noting charge is an expense to be borne by payee

    (d) Noting charge is an expense to be borne by bank

51. Which of the following statement is **true**:

    (a) Account payables can draw a bill on Account receivables.

    (b) Account receivables can draw a bill on Account payables.

    (c) Bank will draw a bill on customer at the time of overdraft.

    (d) One can draw the bill on another under any circumstances.

52. Gouri sold goods to Gupta on 1.6.2011 for ₹ 1600. Gupta immediately accepted a three months bill. On due date Gupta requested that the bill be renewed for a fresh period of two months. Gouri agrees provided interest at 9% was paid immediately in cash. What will be the amount of interest in the books of Gouri?

    (a) ₹ 20 (b) ₹ 25 (c) ₹ 24 (d) ₹ 28

53. X draws a bill on Y on 1.1.2011 for ₹ 20,000 for 30 days. What will be the maturity date of the bill:

    (a) 2.2.2011 (b) 3.2.2011 (c) 1.2.2011 (d) 31.1.2011

54. Ram's acceptance to Din for ₹ 8,000 renewed at 3 months on the condition that ₹ 4,000 be paid in cash immediately and the remaining amount will carry interest @ 12% p.a. The amount of interest will be:

    (a) ₹ 120 (b) ₹ 80 (c) ₹ 90 (d) ₹ 160

55. A draws a bill on B for ₹ 30,000. A wants to endorse it to C in settlement of ₹ 35,000 at 2% discount with the help of B's acceptance and balance in cash. How much cash A will pay to B?

    (a) ₹ 4,300 (b) ₹ 4,000 (c) ₹ 4,100 (d) ₹ 5,000

56. Ram gets Ghosh's acceptance for ₹ 12,000 discounted at 2 months at 12% p.a. The amount of discount will be:

    (a) ₹ 240 (b) ₹ 120 (c) ₹ 360 (d) Nil

57. If the due date is a public holiday, what will be the due date of the bill:

    (a) Following day (b) Preceding day

    (c) The same day only (d) One month later

ANSWERS

1.	(c)	2.	(c)	3.	(b)	4.	(a)	5.	(c)	6.	(c)
7.	(b)	8.	(c)	9.	(a)	10.	(b)	11.	(b)	12.	(a)
13.	(a)	14.	(b)	15.	(d)	16.	(a)	17.	(b)	18.	(a)
19.	(a)	20.	(a)	21.	(c)	22.	(a)	23.	(b)	24.	(c)
25.	(a)	26.	(b)	27.	(b)	28.	(c)	29.	(c)	30.	(b)
31.	(a)	32.	(d)	33.	(d)	34.	(d)	35.	(c)	36.	(d)
37.	(b)	38.	(a)	39.	(a)	40.	(c)	41.	(d)	42.	(b)
43.	(c)	44.	(d)	45.	(a)	46.	(a)	47.	(c)	48.	(d)
49.	(c)	50.	(b)	51.	(a)	52.	(c)	53.	(b)	54.	(a)
55.	(a)	56.	(a)	57.	(b)						

CHAPTER - 7

ACCOUNTING FOR SPECIAL TRANSACTIONS

Unit 4

Sale of Goods on Approval or Return Basis

Learning Objectives

After studying this unit, you will be able to :

- ♦ Understand the nature of goods sent on approval or return basis.
- ♦ Learn the accounting treatment of sales on approval or return basis under different situations.

1. INTRODUCTION

With a view of pushing up the sales or for introducing a new product in the market, goods are sometimes sent to the customers on sale or approval basis. Here, goods sent on 'approval' or 'on sale or return' basis mean the delivery of the goods to the customers with the option to retain or return them within a specified period. Generally, these transactions take place between a manufacturer (or a wholesaler) and a retailer. The goods are transferred from the wholesaler to the retailer, under a sale or return basis, it implies a change in the possession of goods only and not a transfer of the ownership of goods. The ownership is passed only when the retailer gives his approval or if the goods are not returned within that specified period. The retailer (customer) does not incur any liability when the goods are merely sent to him.

As per the definition given under the Sale of Goods Act, 1930, in respect of such goods, the sale will take place or the property in the goods pass to the buyer:

(i) When he signifies his approval or acceptance to the seller;

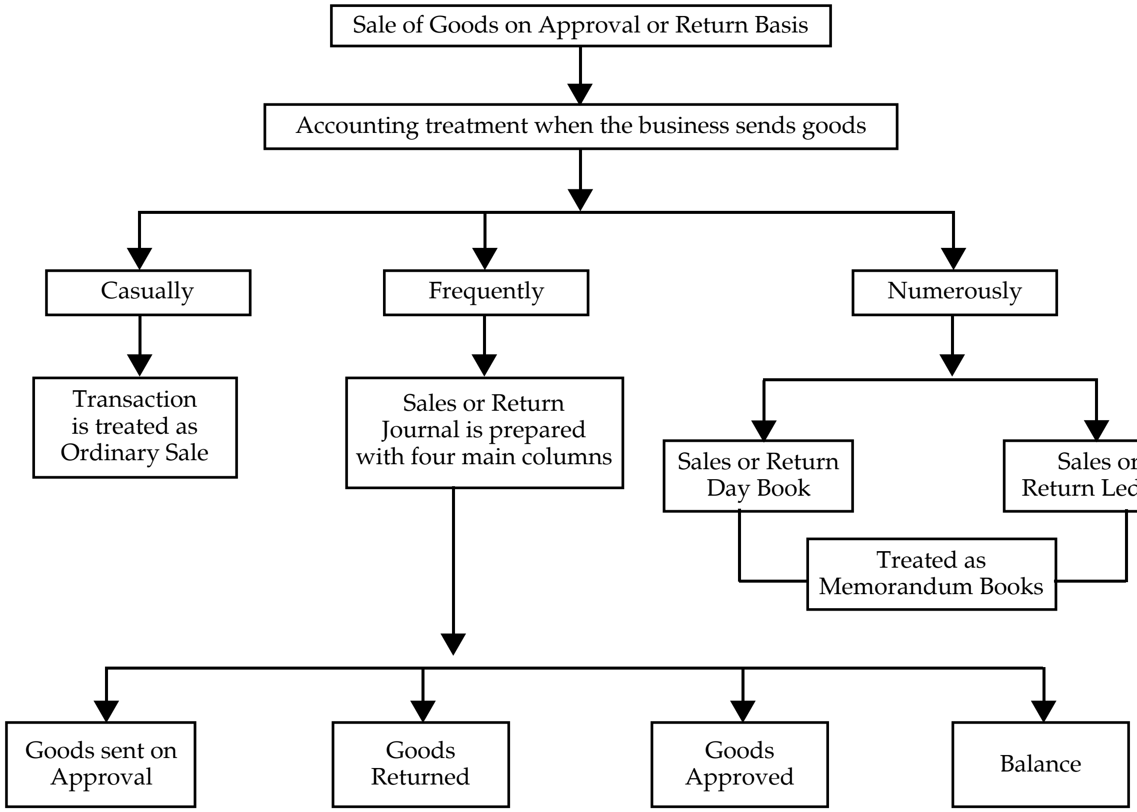
(ii) When he does some act adopting the transaction;

(iii) If he does not signify his approval or acceptance to the seller but retains the goods without giving notice of rejection, on the expiry of the specified time (if a time has been fixed) or on the expiry of a reasonable time (if no time has been fixed).

2. ACCOUNTING RECORDS

Accounting entries depend on the fact whether the business sends goods on sale or approval basis (i) casually; (ii) frequently; and (iii) numerously.

An overview of the accounting treatment for the goods sent on sale or approval basis can be depicted with the help of the chart given below :



2.1 WHEN THE BUSINESS SENDS GOODS CASUALLY ON SALES OR RETURN

When the transactions are few, the seller on sending the goods, treats them as an ordinary sale. If the goods are accepted or not returned or the business receives no intimation within the specified time limit, no extra entry is required to be passed because the transaction for sale or return becomes entry after the expiry of the specified period. If the goods are returned within a specified time limit, a reverse entry is passed to cancel the previous transaction. If, at the year-end, goods are still lying with the customers and the specified time limit is yet to expire, the entry for sales made earlier is cancelled and the value of the goods lying with the customers must be reduced from the selling price to the cost price, and treated as an ordinary Inventories for Balance Sheet purposes.

Journal Entries:

1. When goods are sent on approval or on sale or return basis

Trade receivables / Customers Account	Dr.	[Invoice price]
To Sales Account		

2. When goods are rejected or returned within the specified time

Sales/Return Inwards Account	Dr.	[Invoice price]
To Customers/Trade receivables Account		

3. When goods are accepted at invoice price

    [No entry]

4. When goods are accepted at a higher price than invoice price

Trade receivables / Customers Account		Dr.
To Sales Account		[Difference in price]

5. When goods are accepted at a lower price than the invoice price

Sales Account	Dr.	
To Trade receivables / Customers Account	[Difference in price]	

6. (i) At the year-end, when goods are lying with customers and the specified time limit is yet to expire

Sales Account	Dr.	[Invoice price]
To Trade receivables / Customers Account		

   (ii) These goods should be considered as Inventories with customers and in addition to the above, the following adjustment entry is to be passed

    Inventories with Customers on Sale or Return Account Dr.

    To Trading Account [Cost price or market price whichever is less]

No entry is to be passed for goods returned by the customers on a subsequent date.

Illustration 1

CE sends goods to his customers on Sale or Return. The following transactions took place during 2011:

2011

Sept. 15	Sent goods to customers on sale or return basis at cost plus $33^{1/3}$%	₹1,00,000
Oct. 20	Goods returned by customers	40,000
Nov. 25	Received letters of approval from customers	40,000
Dec .31	Goods with customers awaiting approval	20,000

CE records sale or return transactions as ordinary sales. You are required to pass the necessary Journal Entries in the books of CE assuming that accounting year closes on 31st December, 2011.

Solution

In the books of Capital Electronics

Journal Entries

Date	*Particulars*		*L.F.*	*Dr. (in ₹)*	*Cr. (in ₹)*
2011					
Sept. 15	Trade receivables A/c	Dr.		1,00,000	
	To Sales A/c				1,00,000
	(Being the goods sent to customers on sale or return basis)				
Oct. 20	Return Inward A/c (Note 1)	Dr.		40,000	
	To Trade receivables A/c				40,000
	(Being the goods returned by customers to whom goods were sent on sale or return basis)				
Dec. 31	Sales A/c	Dr.		20,000	
	To Trade receivables A/c				20,000
	(Being the cancellation of original entry of sale in respect of goods on sale or return basis)				
Dec. 31	Inventories with customers on Sale or Return A/c	Dr.		15,000	
	To Trading A/c (Note 3)				15,000
	(Being the adjustment for cost of goods lying with customers awaiting approval)				

Note: (1) Alternatively, Sales account can be debited in place of Return Inwards account.

(2) No entry is required for receiving letter of approval from customer.

(3) Cost of goods with customers = $\frac{₹\ 20,000 \times 100}{133.33}$ = ₹ 15,000

Illustration 2

S. Ltd. sends out its goods to dealers on Sale or Return basis. All such transactions are, however, treated as actual sales and are passed through the Day Book. Just before the end of the accounting year on 31.12.2011, 200 such goods have been sent to a dealer at ₹ 250 each (cost ₹ 200 each) on sale or return and debited to his account. Of these goods, on 31.12.2011, 50 were returned and 70 were sold, for the other goods date of return has not yet expired.

Pass necessary adjustment entries on 31.12.2011.

Solution

In the books of S. Ltd.

Journal Entries

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
2011					
Dec. 31	Return Inwards A/c (₹ 250 X 50)	Dr.		12,500	
	To Trade receivables A/c				12,500
	(Being the adjustment for 50 units of goods returned by customers to whom goods were sent on sale or return basis)				
Dec. 31	Sales A/c (₹ 250 X 80)	Dr.		20,000	
	To Trade receivables A/c				20,000
	(Being the cancellation of original entry for sale in respect of 80 units of goods not yet returned or approved by customers)				
Dec. 31	Inventories with Customers on Sale or Return A/c	Dr.		16,000	
	To Trading A/c				16,000
	(Being the cost of goods sent to customers on sale or return basis not yet approved, adjusted)				

Illustration 3

Caly Company sends out its gas containers to dealers on Sale or Return basis. All such transactions are, however, treated as actual sales and are passed through the Day Book. Just before the end of the financial year, 100 gas containers, which cost them ₹ 900 each have been sent to the dealer on 'sale or return basis' and have been debited to his account at ₹ 1,200 each. Out of this only 20 gas containers are sold at ₹ 1,500 each.

You are required to pass necessary adjustment entries for the purpose of Profit and Loss Account and Balance Sheet.

Solution

In the books of Caly Company

Journal Entries

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
	Trade receivables A/c	Dr.		6,000	
	To Sales A/c				6,000
	(Being the adjustment for excess price of 20 gas containers @ 300 each)				
	Sales A/c	Dr.		96,000	
	To Trade receivables A/c				96,000
	(Being the cancellation of original entry for sale in respect of 80 gas containers @ ₹ 1,200 each)				
	Inventories with Customers on Sale or Return A/c	Dr.		72,000	
	To Trading A/c				72,000
	(Being the adjustment for cost of 80 gas container lying with customers awaiting approval)				

Illustration 4

E Ltd. sends out its accounting machines costing ₹ 200 each to their customers on Sales or Return basis. All such transactions are, however, treated like actual sales and are passed through the Day Book. Just before the end of the financial year, i.e., on December 24, 2011, 300 such accounting machines were sent out at an invoice price of ₹ 280 each, out of which only 90 accounting machines are accepted by the customers ₹ 250 each and as to the rest no report is forthcoming. Show the Journal Entries in the books of the company for the purpose of preparing Final Accounts for the year ended December 31, 2011.

Solution

In the books of E Ltd.

Journal Entries

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
2011					
Dec. 31	Sales A/cs (₹ 30x90)	Dr.		2,700	
	To Trade receivables A/c				2,700
	(Being the adj. for reduction in the selling price of 90 accounting machines @ ₹ 30 each)				
Dec. 31	Sales A/c (₹ 280 x 210)	Dr.		58,800	
	To Sundry Debtor A/c				58,800
	(Being the cancellation of original entry for sale in respect of 210 accounting machines sent to customers not yet returned or approved)				
	Inventories with customers on Sale or Return A/c	Dr.		42,000	
	To Trading A/c				42,000
	(Being the cost of 210 accounting machines @ ₹ 200 each adjusted against Trading Account)				

Illustration 5

A sends out goods on approval to few customers and includes the same in the Sales Account. On 31.3.2011 the Trade receivables balance stood at ₹ 1,00,000 which included ₹ 7,000 goods sent on approval against which no intimation was received during the year. These goods were sent out at 25% over and above cost price and were sent to-

Mr. X - ₹ 4,000 and Mr. Y -₹ 3,000.

Mr. X sent intimation of acceptance on 30th April and Mr. Y returned the goods on 10th April, 2011.

Make the adjustment entries and show how these items will appear in the Balance Sheet on 31st March, 2011. Show also the entries to be made during April, 2011. Value of closing Inventories as on 31st March, 2011 was ₹ 60,000.

Solution

In the Books of A

Journal Entries

Date	*Particulars*		*L.F.*	*Dr.* ₹	*Cr.* ₹
2011	Sales A/c	Dr.		7,000	
March 31	To Trade receivables A/c (Being the cancellation of original entry for sale in respect of goods lying with customers awaiting approval)				7,000
March	Inventories with Customers on Sale or Return A/c	Dr		5,600	
31	To Trading A/c (Note 1) (Being the adjustment for cost of goods lying with customers awaiting approval)				5,600
April 30	Trade receivables A/c	Dr.		4,000	
	To Sales A/C (Being goods costing ₹ 3,200 sent to Mr. X on sale or return basis has been accepted by him)				4,000

Balance Sheet of A & Co. as on 31st March, 2011 (Extracts)

Liabilities	₹	*Assets*	₹	₹
		Trade receivables (₹ 1,00,000 - ₹ 7,000)		93,000
		Inventories-in-trade	60,000	
		Add: Inventories with customers on Sale or Return	5,600	65,600
				1,58,600

Notes:

(1) Cost of goods lying with customers = 100/125 x ₹ 7,000 = ₹ 5,600

(2) No entry is required on 10th April, 2011 for goods returned by Mr. T. Goods should be included physically in the Inventories-in-trade.

2.2 WHEN THE BUSINESS SENDS GOODS FREQUENTLY ON SALE OR RETURN BASIS

When goods are sent out on sale, on approval or return basis, an immediate sale obviously does not take place. Only when the customer signifies his intention to purchase the goods or takes some action whereby it is indicated that he has decided to purchase the goods, the property in the goods passes to the buyer. So long as the property does not pass to the buyer, the seller should not record it as a sale and, therefore, should not debit the customer with the sales price.

Where a large number of articles are sent out on a sale or return basis, it is necessary to maintain a specially ruled Sale or Return Journal / Day Book: This Day Book is divided into 4 main columns - (1) Goods sent on Approval; (2) Goods Returned: (3) Goods Approved; and (4) Balance.

Goods sent on approval				Goods returned				Goods approved				Balance
1	2	3	4	5	6	7	8	9	10	11	12	13
Date	Particulars	Fol.	Amt.	Date	Particulars	Fol.	Amt.	Date	Particulars	Fol.	Amt.	Amt.

When such a Journal is kept the following procedure is adopted for recording transactions entered into on this basis.

When goods are sent out for sale on approval, entries are made only in column 1 to 4, the sale price of goods being entered in column 4. The sale price is also posted to the debit of the customers' account in 'Goods on Approval Ledger', and periodically total of column 4 is posted to the credit of Goods on Approval Total Account in the same ledger.

If goods are returned, entries are made in columns 5 to 8, the price of goods returned being entered to column 8. The individual amounts are credited to the Customers' Accounts, in the 'Goods on Approval' Ledger and the total of this column in periodically posted to the Total Goods on Approval Account.

If the goods are retained by the customer, entries are made in columns 9 to 12. The individual amounts are then posted to the debit of customer's accounts in the Sales Ledger and their total is credited to Sales Account in the General Ledger. Further the customer's accounts in the Goods on Approval Ledger are credited with the individual amounts of goods sold and periodically, the total of the amount is posted to the debit of Goods on Approval Total Account.

The value of goods sent out but not sold or returned till the close of the year is extended to column 13. The total of this column, afterwards, will show the value of goods with customers at the sale price.

The balance amount is calculated as follows:

Balance Value of Goods Sent on Sale or Return ***Less*** Value of Goods Returned ***Less*** Value of Goods Approved.

Information relating to goods delivered and goods returned is kept on Memorandum basis. However, information relating to goods approved and balance is duly accounted for by passing journal entries relating to sales and Inventories on approval basis.

(i) At the time of approval

Customer's A/c Dr.

To Sales A/c

The amount, after eliminating the element of profit, is included in the Trading Account representing the value of Inventories with customers at cost price. Like an ordinary closing Inventories, such goods are considered as Inventories lying with customers on behalf of seller and are valued at cost or net realisable value whichever is less.

(ii) At the time of preparing of Final Accounts

An adjustment entry is required for balance goods which is as follow:

Goods with Customers on Sale or Return Account To Trading Account	Dr.	[Cost or net realisable value whichever is less]

2.3 WHEN THE BUSINESS SENDS GOODS NUMEROUSLY ON SALE OR RETURN

When transactions are numerous, a business maintains the following books: (a) Sale or Return Day Book; and (b) Sale or Return Ledger. Ledger contains the accounts of the customers and the 'Sale or Return' Total account. It is important to remember that both are **Memorandum Books.**

In this case, when the goods are sent to the customers on a sale or return basis, they are recorded in the Sale or Return day Book. Thereafter, in the Sale or Return Ledger, all the customers are individually debited and the Sale or Return Account is credited with the periodical total of the Sale or Return Day Book.

When the goods are returned by the customers within the specified time, they are recorded initially in the Sale or Return Day Book. Thereafter, in the Sale or Return Ledger, the Sale or Return Account is debited with the periodical total of the Sale or Return Day Book and the individual customers are credited. The above mentioned records are all memorandum and hence cannot find a place in the regular books.

When the business receives information about the acceptance of the goods or no intimation is received within the specified time, they are recognised as sales and are recorded in the Sales Day Book. Periodically, the total of the Sales Day Book is credited to Sales Account and debited to the Individual Customers Account. To cancel the earlier entries, individual customers are credited and the Sale or Return Account is debited. The entries for the approved goods are shown below:

In the Memorandum Sale or Return Ledger		In the regular General ledger	
Sale or Return Account	Dr.	Individual Customer's Account	Dr.
To Individual Customer's Account		To Sales Account	

At the year end, in the Sale or return Ledger, the sum of the debit balances of the Individual Customers' Account must be equal to the credit balance of the Sale or return Account. It represents Inventories with customers waiting for approval at invoice price. To adjust the cost of such goods with customers in the Final Accounts, the following entry is passed:

Inventories with Customers on Sale or Return Account Dr. [Cost or net realisable value, To Trading Account whichever is less]

Illustration 6

A firm sends goods on sale or return basis. Customers having the choice of returning the goods within a month. During May 2011, the following are the details of goods sent:

Date (May)	2	8	12	18	20	27
Customers	P	B	Q	D	E	R
Value (₹)	15,000	20,000	28,000	3,000	1,000	26,000

Within the stipulated time, P and Q returned the goods and B, D, and E signified that they have accepted the goods.

Show in the books of the firm, the Sale or Return Account and Customer- P for Sale or Return Account on 15th June, 2011.

Solution

Sale or Return

Dr. Date	*Particulars*	₹	*Date*	*Particulars*	*Cr.* ₹
2011			2011		
May 31	To Sundries: Sales	24,000	May 31	By Sundries	
June 15	To Sundries: Returned	43,000		(Goods sent on sale or return basis)	93,000
June 15	To Balance c/d	26,000			
		93,000			93,000
				By Balance b/d	26,000

P's Account

Dr. Date	*Particulars*	₹	*Date*	*Particulars*	*Cr.* ₹
2011			2011		
May 2	To Sale or Return A/c	15,000	May 2	By Sale or Return A/c	15,000

Illustration 7

On 31st December, 2011 goods sold at a sale price of ₹ 3,000 were lying with customer, Ritu to whom these goods were sold on 'sale or return basis' and recorded as actual sales. Since no consent has been received from Ritu, you are required to pass adjustment entries presuming goods were sent on approval at a profit of cost plus 20%. Present market price is 10% less than the cost price.

Solution

Journal Entries

Date	*Particulars*		*Dr.* ₹	*Cr.* ₹
2011				
31st Dec.	Sales A/c	Dr.	3,000	
	To Ritu's A/c			3,000
	(Being cancellation of entry for sale of goods, not yet approved)			
	Inventories with customers A/c (Refer W.N.)	Dr.	2,250	
	To Trading A/c			2,250
	(Being Inventories with customers recorded at market price)			

Working Note:

Calculation of cost and market price of Inventories with customer

Sale price of goods sent on approval	₹3,000
Less: Profit (3,000 x 20/120)	₹ 500
Cost of goods	₹2,500

Market price = 2,500 - (2,500 x 10%) = ₹ 2,250.

SELF EXAMINATION QUESTIONS

1. When a large number of articles are sent frequently on a sale or return basis, it is necessary to maintain

   (a) Sale journal (b) Goods returned journal

   (c) Sale or return journal (d) None of the above.

2. On 31st December, 2011 goods sold at a sale price of ₹ 30,000 were lying with customer, Mohan to whom these goods were sold on 'approval or return basis' and recorded as actual sales. Since no consent was received from Mohan, the adjustment entry was made, presuming goods were sent on approval at a profit of cost plus 20%. In the balance sheet, the Inventories with customers account will be shown at ₹

   (a) 30,000. (b) 24,000. (c) 20,000. (d) 25,000.

3. A sent some goods costing ₹ 3,500 at a profit of 25% on sale to B on sale or return basis. B returned goods costing ₹ 800. At the end of the accounting period i.e. on 31st December, 2011, the remaining goods were neither returned nor were approved by him. The Inventories on approval will be shown in the balance sheet at ₹

   (a) 2,000. (b) 2,700. (c) 2,700 less 25% of 2,700. (d) 3,500.

4. A merchant sends out his goods casually to his dealers on approval basis. All such transactions are, however, recorded as actual sales and are passed through the sales book. On 31-12-2011, it was found that 100 articles at a sale price of 200 each sent on approval basis were recorded as actual sales at that price. The sale price was made at cost *plus* 25%. The amount of Inventories on approval will be amounting

   (a) ₹16,000. (b) ₹ 20,000. (c) ₹ 15,000. (d) None of the above.

5. Umesh sends goods on approval basis as follows:

Date January, 2011	*Customer's Name*	*Sale price of Goods Sent*	*Goods Accepted* ₹	*Goods Returned*
		₹		₹
8	Anna	3,500	3,000	500
10	Babu	2,800	2,800	–
15	Chandra	3,680	–	3,680
22	Desai	1,260	1,000	260

   The Inventories of goods sent on approval basis on 31st January will be

   (a) ₹ 500. (b) Nil. (c) ₹ 260. (d) None of the above.

6. A company sends its cars to dealers on 'sale or return' basis. All such transactions are however treated like actual sales and are passed through the sales day book. Just before the end of the financial year, two cars which had cost ₹ 55,000 each have been sent on 'sale or return' and have been debited to customers at ₹ 75,000 each, cost of goods lying with the customers will be

   (a) ₹ 1,10,000. (b) ₹ 55,000. (c) ₹ 75,000. (d) None of the above.

7. A trader has credited certain items of sales on approval aggregating ₹ 60,000 to Sales Account. Of these, goods of the value of ₹ 16,000 have been returned and taken into Inventories at cost ₹ 8,000 though the record of return was omitted in the accounts. In respect of another parcel of ₹ 12,000 (cost being ₹ 6,000) the period of approval did not expire on the closing date. Cost of goods lying with customers should be

   (a) ₹ 12,000. (b) ₹ 54,000. (c) ₹ 6,000. (d) None of the above.

8. Under sales on return or approval basis, the ownership of goods is passed only

   (a) when the retailer gives his approval
   (b) if the goods are not returned within specified period.
   (c) Both (a) and (b) (d) None of the above

9. Under sales on return or approval basis, when transactions are few, the seller, while sending the goods, treats them as

   (a) an ordinary sale but no entry is passed in the books
   (b) an ordinary sale and entry for normal sale is passed in the books
   (c) Approval sale and no entry is passed
   (d) None of the above

10. Under sales on return or approval basis, when transactions are few and the seller at the end of the accounting year reverse the sale entry, then what will be the accounting treatment for the goods returned by the customers on a subsequent date?

    (a) No entry will be passed for such return of goods
    (b) Entry for return of goods is passed by the seller
    (c) Only the Inventories account will be adjusted
    (d) None of the above

11. Which of the following is not a main column of sales or return journal?

    (a) goods sent on approval column (b) goods returned column
    (c) goods approved column (d) purchase column

12. Sale or Return Day Book and Sale or Return Ledger are known as

    (a) principal books (b) subsidiary books
    (c) memorandum books (d) none of the above

13. In the Sale or Return Ledger

    (a) all the customers are individually debited and the sale or return account is credited with the periodical total of the Sale or Return Day Book.
    (b) all the customers are debited in total and the sale or return account is credited with the periodical total of the Sale or Return Day Book.
    (c) all the customers are individually debited and the sale or return account is also credited with the individual total of the Sale or Return Day Book.
    (d) None of the above.

14. When the goods are returned by the customers within the specified time, they are recorded

(a) initially in the Sale or Return Ledger. Thereafter, in the Sale or Return Day Book

(b) initially in the Sale or Return Day Book. Thereafter, in the Sale or Return Ledger

(c) only in the Sale or Return Day Book

(d) only in the Sale or Return Ledger

ANSWERS

1. (c)	2. (d)	3. (b)	4. (a)	5. (b)
6. (a)	7. (c)	8. (c)	9. (b)	10. (a)
11. (d)	12. (c)	13. (a)	14. (b)	

NOTES