

UNIT 15 ACCOUNTS FROM INCOMPLETE RECORDS-I

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15.0 OBJECTIVES

After studying this unit you should be able to:

- explain the single entry system of accounting
- describe the salient features of incomplete records and their limitations
- numerate the two methods of ascertaining profit from incomplete records
- prepare statement of affairs to ascertain the opening and closing capitals
- ascertain profit or loss from incomplete records

15.1 INTRODUCTION

In Unit 1 you learnt about the two systems of accounting viz., the double entry system and the single entry system. Most firms follow the double entry system of accounting about which you have learnt in detail. The single entry system of accounting is usually followed by small traders and the professionals who cannot afford to employ qualified persons for the accounting work. Under this system they maintain only a cash book and the personal accounts of customers and suppliers. Thus, they keep partial and incomplete record of their transactions. This creates problem in ascertaining the profit or loss of their business and prepare proper final accounts. In such a situation there are two methods that can be adopted for ascertaining the profit or loss: (i) net worth method, and (ii) conversion method. In this unit you will learn about the net worth method of ascertaining the profit of a business owned by a sole proprietor or a partnership firm.

15.2 WHAT IS SINGLE ENTRY SYSTEM

The primary aim of every business, be it a trading concern or manufacturing establishment, is to earn profits. For this purpose every firm must keep proper records of transactions so that at the end of an accounting period the final accounts can be prepared and profits ascertained. The big business concerns usually have a separate Accounts Department and employ qualified and expert accountants for this purpose. But small traders, petty shopkeepers and persons in the profession cannot afford to employ qualified persons for the accounting work. Such persons usually keep the accounting records themselves which are often incomplete. Some of them keep only personal accounts of customers and suppliers, some keep only a Cash Book while others may keep personal accounts of customers' and suppliers' as well as the Cash Book. Thus, they maintain partial and incomplete records

The term Single Entry System is quite misleading. It gives an impression that under this system only one aspect of a transaction is recorded in books. This is not true. Single Entry System actually refers to incomplete records or the defective Double Entry System. Under this system, for certain transactions both the aspects are recorded while for others only one aspect is recorded. Some transactions may simply be ignored, they are not recorded at all. Take the case of a firm which maintains a Cash Book and personal accounts of customers and suppliers. When cash is paid to a creditor, it will be recorded on the payment side (credit) of the Cash Book and also debited to the personal account of the creditor. Thus you find that both the aspects of this transaction have been duly recorded and the double entry is complete. The same thing applies to cash received from a debtor. But, when rent is paid, it will be recorded in the Cash Book but no entry is made in the Rent Account because the nominal accounts are not maintained. Thus, in this case only one aspect has been recorded in books, the other is simply ignored. For items like depreciation such firms do not make any entry because no fixed assets accounts are maintained. The single entry system is thus a mixture of double entry, single entry and no entry. The accounts maintained under this system are incomplete and unsystematic. Kohler in his 'Dictionary for Accountants' has defined it as '*a system of book-keeping in which, as a rule, only records of cash and personal accounts are maintained, it is always incomplete double entry varying with the circumstances*'. Some people prefer to call it a 'Quasi Single Entry System' or simply 'Incomplete Records'. This system is generally adopted by small traders, petty shop-keepers, doctors, advocates, and other professionals. The system can be adopted by sole proprietor concerns and partnership firms. The limited companies, however, cannot adopt it because they have to maintain complete records of all transactions as well as those of assets and liabilities as per the requirements of the Indian Companies Act, 1956.

15.3 SALIENT FEATURES OF INCOMPLETE RECORDS

- 1 **Maintenance of Cash Book:** A Cash Book is usually maintained. But the business transactions and the personal transactions of the proprietor are usually mixed up.
- 2 **Maintenance of Personal Accounts:** If there are credit sales and credit purchases the Personal Accounts of customers (debtors) and suppliers (creditors) are maintained. But the Real and Nominal Accounts are avoided. In other words, the accounts of fixed assets, liabilities, expenses and incomes are not maintained.
- 3 **No Uniformity:** The adoption of this system is not uniform. It differs from firm to firm as per their individual requirements and convenience.
- 4 **Dependence on original vouchers:** To ascertain profit or loss or to collect information for any other purpose, necessary figures can be collected only from the original vouchers such as purchase invoice, sales invoice, etc. Thus, dependence on original vouchers is inevitable.
- 5 **Preparation of Final Accounts:** The final accounts cannot be prepared easily. It is possible to prepare the Trading and Profit & Loss Account only after the available information has been converted into double entry records and the missing figures have been found out. The figures of assets and liabilities computed from incomplete records are not very reliable as they are based on mere estimates. Hence the statement of assets and liabilities prepared at the end of the accounting period under this system is called as 'Statement of Affairs' instead of "Balance Sheet".

15.4 LIMITATIONS

Single Entry System signifies the incompleteness and insufficiency of information. Hence, it suffers from certain limitations which can be summarised as follows:

- 1 The arithmetical accuracy of the books of accounts cannot be checked as it is not possible to prepare a Trial Balance in the absence of real and nominal accounts.

- 2 Any information obtained under this system will not be free from doubt and so is unreliable.
- 3 It is not possible to prepare a Trading Account and find out the rate of gross profit earned by the firm. In the absence of gross profit margin, the performance of the firm cannot be compared with that of other firms or with the past. This also affects proper planning and sound decision-making.
- 4 True profit or loss and information about assets and liabilities, cannot be obtained with certainty. Hence, it is not possible to **assess** financial soundness of the firm.
- 5 In the absence of **proper** and reliable balance sheet, the firm may not be able to avail itself of the various financial facilities from banks such as overdraft facilities **or** loan facilities.
- 6 The system generates a **spirit** of laxity on the part of the employees which may result in frauds.

Check Your Progress A

- 1 State whether the following statements are True or False:
 - i) Partnership firms of professionals cannot keep their books of account on single entry system.
 - ii) Profits can be easily and quickly calculated if the books are kept on single entry system.
 - iii) Sole traders prefer to keep their books on single entry system.
 - iv) It is not possible to prepare Trial Balance if the account books are kept on single **entry** system.
 - v) As it is easier to keep accounts under single entry system, most of the limited companies adopt this system of accounting.
- 2 Fill in the blanks with appropriate word or words:
 - i) Trading and Profit & Loss Account be easily prepared to find out profit if the books are kept under single **entry** system of accounting.
 - ii) and usually keep their books on single entry **system**.
 - iii) Only and are **maintained** under single entry system of accounting.
 - iv) As per legal requirements cannot keep their accounts on single entry system.
 - v) **accounts** and accounts are not prepared when books are kept under single entry system.
- 3 Tick the **correct** answer.
 - a) **Records** under single **entry** system are maintained by:
 - i) **big business** houses
 - ii) small traders
 - iii) public limited companies
 - iv) government companies
 - b) Under single entry system the main account book kept is:
 - i) **Purchases** Book
 - ii) Sales **Book**
 - iii) Cash Book
 - iv) **Returns** Inwards **Book**
 - c) Under **single entry** system the type of accounts usually maintained are:
 - i) **personal accounts**
 - ii) **property** accounts
 - iii) **expense** accounts
 - iv) income accounts

15.5 METHODS OF ASCERTAINING PROFITS

You know that in every business the profit or loss must be worked out at the end of an accounting period, whether proper books of account have been kept or not and whether the records maintained are complete or not. This is necessary not only for the proprietors of the business but also for income tax purposes. It is all the more essential if the business happens to be a partnership firm, because the partners have to share the profits of the firm at the end of each accounting period. Now the question arises as to how to ascertain the profits when the accounting records are incomplete. In such a situation there are two methods which can be used for ascertaining the profits. They are:

1 Net Worth Method:

Under this method profits are computed by comparing the net worth or capital at the beginning of the accounting period with the net worth or capital at the end of the accounting period. This method does not involve the preparation of Trading and Profit and Loss Account. It is considered most suitable when the information available is too limited.

2 Conversion Method:

Under single Entry System the Debtors' Ledger and Creditors' Ledger are usually maintained along with the Cash Book. Thus, though the records are incomplete, they provide sufficient information for preparation of the Trading and Profit & Loss Account. Hence the Conversion Method is employed for ascertaining the profits which involve the preparation of proper final accounts after working out the missing figures. This method will be discussed in detail in Unit 16.

15.6 NET WORTH METHOD

Many small business firms simply maintain the personal accounts of Debtors and Creditors or only the Cash Book. In such a situation it is not possible to prepare the Trading and Profit and Loss Account. Hence, we have to use the net worth method for finding out the profit or loss at the end of an accounting period. This method is also known as 'Net Assets Method' or 'Statement of Affairs Method'.

The net worth method is based on a simple fact that any increase or decrease in the net worth (capital) of a business takes place as a result of the profit earned or the loss incurred during the year. For example, a person started his business with a capital of Rs. 20,000 on January 1, 1987. On December 31, 1987 when he analyses his assets and liabilities he finds that his capital had increased to Rs. 28,000. This would mean that he earned a profit of Rs. 8,000 (Rs. 28,000 - Rs. 20,000) during 1987. If however, his capital on December 31, 1987 worked out as Rs. 16,000 it would mean he incurred a loss of Rs. 4,000 (Rs. 20,000 - Rs. 16,000).

Thus under net worth method the profit can be ascertained by comparing the net worth (or capital) of the business as at the beginning of the accounting period (opening capital) with the net worth (or capital) as at the end of the period (closing capital). If, the net worth at the end is more as compared to the net worth at the beginning, the difference is treated as the profit earned during the period. If, on the other hand, the net worth at the end is less than the net worth at the beginning, it means the firm has incurred a loss during the period. Let us study first how the net worth at the beginning and the net worth at the end are to be worked out.

15.6.1 Computation of Net Worth

The net worth or capital on a particular date can be found out by adding all assets and deducting therefrom the total of all external liabilities. Thus opening capital can be calculated by adding all assets at the beginning of the year and deducting therefrom the total of all external liabilities on that date. Similarly, the closing capital can be calculated by adding the value of all assets on the last day of the year and deducting therefrom the total of all external liabilities on that date. This is done by preparing two **separate statements** of assets and external liabilities one as at the beginning and the other as at the

end. These, statements are called 'Statement of Affairs' which are virtually the Balance Sheets of the business.

Under double Entry System you get all the figures of assets and liabilities from the books of accounts. But under Single Entry System, you may get some figures from books but for others you will have to rely on vouchers or other documents and physical assessment. For example, cash and bank balances can be taken from Cash Book. The lists of debtors and creditors can be compiled from personal accounts. But, the value of fixed assets like furniture, machinery, buildings, etc. shall be ascertained from vouchers and other documents available. Similarly, the closing stock will be worked out by actual stock taking and their values ascertained on the basis of the invoices received from the suppliers.

15.6.2 Computation of Profits

You have learnt that under the net worth method the profit or loss of the business is ascertained by comparing its net worth at the beginning (opening capital) with its net worth at the end (closing capital). You know if the closing capital is more than the opening capital the difference is treated as profit because the increase in capital is primarily the result of the profit earned during the period. But we must also bear in mind that capital can be affected by two other factors (i) drawings made during the year, and (ii) additional capital introduced during the year. Hence, while calculating the profit by net worth method, these two aspects should also be taken into account.

Adjustment in respect of drawings: The proprietors always withdraw certain amount from the business for personal expenses. This decreases the closing capital. In other words, if there were no drawings, the closing capital would have been a higher figure. Hence, to find out the true closing capital it becomes necessary to add back the amount of drawings made during the year.

Adjustment in respect of additional capital: Any additional capital brought in by the proprietors increase the closing capital of the business. Thus, such increase in capital is not the result of profits but it is on account of the additional capital introduced during the year. Hence, to find out the true profits, it becomes necessary to reduce the closing capital by the amount of additional capital introduced by the proprietors during the year.

For ascertaining the profit or loss by net worth method, we usually prepare a statement called 'Statement of Profit' which clearly shows the comparison of opening and closing capitals with due adjustment of drawings and the additional capital. Look at Figure 15.1. It shows the form in which the Statement of Profit is to be prepared.

Figure 15.1
Statement of Profit
for the year ending

Look at Illustration 1 and study how opening and closing capitals are worked out with the help of Statements of Affairs and how profit is ascertained after making necessary adjustments for drawings and the additional capital.

Illustration 1

Rajeev keeps his books on single entry system. His position on March 31, 1987 was as follows:

Cash in hand Rs. 2,400; Cash at bank Rs. 25,500; Debtors Rs. 18,400; Stock Rs. 28,600; Furniture Rs. 5,000; Creditors Rs. 18,700; Expenses Outstanding Rs. 2,000.

On October 1, 1987 Rajeev introduced Rs. 10,000 as additional capital in the business out of which a machine costing Rs. 5,000 was purchased for the business. His drawings during the year totalled Rs. 2,000.

On March 31, 1988 his position was as follows:

Cash in hand Rs. 2,600; Cash at bank Rs. 27,500; Stock Rs. 31,500; Debtors Rs. 24,200; Furniture Rs. 4,500; Creditors Rs. 20,200; Prepaid Insurance Rs. 200.

Prepare the necessary Statement of Affairs and the Statement of Profit for the year ending March 31, 1988 and ascertain the profit or loss.

Solution

Statement of Affairs of Rajeev
as at March 31, 1987

Liabilities	Amount	Assets	Amount
	Rs.		Rs.
Creditors	18,700	Cash in hand	2,400
Expenses	2,000	Cash at Bank	25,500
Outstanding Capital	59,200	Debtors	18,400
(balancing figure)		Stock	28,600
		Furniture	5,000
	79,900		79,900

Statement of Affairs of Rajeev
as at March 31, 1988

Liabilities	Amount	Assets	Amount
	Rs.		Rs.
Creditors	20,200	Cash in hand	3,600
Capital	76,300	Cash at Bank	27,500
(balancing figure)		Stock	31,500
		Debtors	24,200
		Prepaid Insurance	200
		Furniture	4,500
		Machinery	5,000
	96,500		96,500

Statement of Profits of Rajeev
for the year ended March 31, 1988

Capital as on March 31, 1988	Rs.
Add Drawings	
	76,300
	2,000
	78,300
Less Further Capital introduced	
	10,000
	68,300
Less Capital as on March 31, 1987	
	59,200
Profit made during the year	
	9,100

Adjustment for Depreciation and Provision for Bad Debts: You know the purpose of providing depreciation and making a provision for bad debts at the time of preparing the final accounts. Such items are equally relevant for ascertaining the profit or loss from incomplete records. They may be given in the form of additional information and must be duly taken into account while preparing the Statement of Affairs for working out the closing capital. The depreciation will be deducted from the value of the concerned fixed asset and the provision for bad debts from Sundry Debtors. Look at Illustration 2 and study how these adjustments are made under the net worth method.

Illustration 2

A trader has not kept proper books of account on double entry system. The following balances **have** been supplied to you by the trader. You are required to prepare a Statement of Profit for the year ended December 31, 1987 and a Statement of Affairs as on that date:

	as on 1.1.88	as on 31.12.88
	Rs.	Rs.
Cash in hand	10,000	12,000
Bank Overdraft	30,000	40,000
Stock in Trade	60,000	80,000
Sundry Creditors	35,000	40,000
Sundry Debtors	40,000	45,000
Bills Receivable	20,000	15,000
Land and Buildings	80,000	80,000
Furniture & Fittings	8,000	8,000
Bills Payable	30,000	26,000
Outstanding Expenses	3,000	2,000

Drawings **during** the year amounted to Rs. 16,000. Depreciation is to be provided on land and buildings @ 2% and on furniture & fittings @ 10%. Also provide for doubtful debts @ 5% on debtors.

Solution:

Statement of Affairs as on January 1, 1988

Liabilities	Amount	Assets	Amount
	Rs.		Rs.
Bank overdraft	30,000	Cash in hand	10,000
Sundry Creditors	35,000	Stock in Trade	60,000
Bills Payable	30,000	Sundry Debtors	40,000
Outstanding Expenses	3,000	Bills Receivable	20,000
Capital (balancing figure)	1,20,000	Land & Buildings	80,000
	2,18,000	Furniture & Fittings	8,000
	2,18,000		

Statement of Affairs as on December 31, 1988

Liabilities	Amount	Assets	Amount
	Rs.		Rs.
Bank Overdraft	40,000	Cash in hand	12,000
Sundry Creditors	40,000	Stock in trade	80,000
Bills Payable	26,000	Sundry Debtors	45,000
Outstanding Expenses	2,000	Less Provision for Bad Debts	42,750
Capital	1,27,350	Bills Receivable	15,000
(balancing figure)	2,35,350	Land & Building	80,000
	2,35,350	Less Depreciation	1,600
	2,35,350	Furniture	8,000
	2,35,350	Less Depreciation	800
	2,35,350		

Statement of Profit for the year ending December 31, 1988

Capital at the end	1,27,350
Add Drawings during the year	16,000
Less Capital at the beginning	1,43,350
Profit earned during the year	1,20,000
	23,350

15.6.3 Partnership Firms

In case of a partnership firm, all partners will have some balance in their capital accounts and the profit of the business will have to be distributed amongst all the partners in the agreed profit sharing ratio (or equally if no ratio is given). The Statement of Affairs however reveals only the combined capital of all partners. Hence, the Statement of Profit will be prepared with the help of combined capitals and in order to work out the individual capital of each partner we may have to prepare the capital accounts of all the partners. It is also possible that the partnership deed provides for allowing interest on capital, interest on drawings, etc. In that case, we should prepare of Profit and Loss Appropriation Account to show the distribution of profit amongst the partners wherein the entries for interest on capital, interest on drawings etc. may also be made. Look at Illustration 3 which deals with a partnership firm keeping books on single entry system.

Illustration 3

A, B and C are partners sharing profits and losses in the ratio of 5:3:2 respectively. They keep their books on single entry system. Their Statement of Affairs as on December 31, 1987 was as follows :

Statement of Affairs as on December 31, 1987

Liabilities	Amount	Assets	Amount
	Rs.		Rs.
Creditors	5,000	Cash in hand	1,800
Bills Payable	2,000	Debtors	6,000
Capital Account:		Stock	4,000
A - 10,000		Furniture	3,000
B - 5,000		Machinery	12,000
C - 5,000	20,000	Prepaid Expenses	200
	27,000		27,000

The withdrawals by the partners during the year 1988 were A : Rs. 2,400 ; B : Rs. 1,800 and C : Rs. 1,800. B brought in additional capital of Rs. 5,000 on July 1, 1987. On December 31, 1987 Cash in hand was Rs. 3,400 ; Debtors Rs. 10,000; Stock in trade Rs. 7,500 ; Creditors Rs. 6,000; Bills Payable Rs. 2,500; Bills Receivable Rs. 4,000 ; Outstanding Expenses Rs. 500. Machinery is to be depreciated by 10% and Furniture by 20% per annum.

Provision for doubtful debts is to be made @ 5% on debtors. Interest is to be allowed on capitals @ 16% per annum but no interest is to be charged on drawings.

You are required to calculate profits earned by the firm during the year 1988 and its division amongst the partners. Also prepare the Balance Sheet of the firm as on December 31, 1988,

Solution

Statement of Affairs as on December 31, 1988

Liabilities	Amount	Assets	Amount
	Rs.		Rs.
Creditors	6,000	Cash in hand	3,400
Bills Payable	2,500	Debtors	10,000
		Less Provision for Bad Debts	500
			9,500
Outstanding Expenses	500	Stock in trade	7,500
Combined Capital (balancing figure)	28,600	Bills Receivable	4,000
		Furniture	3,000
		Less Depreciation	600
			2,400
		Machinery	12,000
		Less Depreciation	1,200
			10,800
	37,600		37,600

Combined Capital as at the end		Rs. 28,600
Add Drawings by the partners	A 2,400 B 1,800 C 1,800	
		6,000
Less Additional Capital by B		34,600
		5,000
Less Combined Capital as at the beginning		29,600
Profit earned during the year		20,000
		9,600

Profit & Loss Appropriation Account

Dr.	Rs.	Cr.
To Interest on Capital A 1,600 B 1,200 C 800	3,600	By Profit 9,600
To Share of Profit A 3,000 B 1,800 C 1,200	6,000	
	9,600	
		9,600

A's Capital Account

	Rs.		Rs.
To Drawings	2,400	By Balance b/d	10,000
To Balance c/d	12,200	By Interest on Capital	1,600
	14,600	By Share of Profit	3,000
			14,600

B's Capital Account

	Rs.		Rs.
To Drawings	1,800	By Balance b/d	5,000
To Balance c/d	11,200	By Cash A/c	5,000
	13,000	By Interest on Capital	1,200
		By Share of Profit	1,800
			13,000

C's Capital Account

	Rs.		Rs.
To Drawings	1,800	By Balance b/d	5,000
To Balance c/d	5,200	By Interest on Capital	800
	7,000	By Share of Profit	1,200
			7,000

Balance Sheet as on December 31, 1988

Liabilities	Amount	Assets	Amount
Creditors	Rs. 6,000	Cash in hand	Rs. 3,400

		Accounts from Incomplete Records I	
Bills Payable	2,500	Debtors Less Provision for Bad Debts	10,000 500
Outstanding Expenses	500		9,500
		Stock in trade	7,500
		Bills Receivable	4,000
		Furniture	3,000
		Less Depreciation	600
			2,400
Capital:		Machinery	12,000
A 12,200		Less Depreciation	1,200
B 11,200			10,800
C 5,200			
	28,600		
			37,600
			37.600

Check Your Progress B

- 1 Select the correct answer.
 - a) Under net worth method, the profit can be ascertained by preparing
 - i) Profit and Loss Account
 - ii) Cash Account
 - iii) Statement of Affairs
 - iv) Statement of Profit
 - b) The closing capital can be ascertained by preparing
 - i) Cash Account
 - ii) Statement of Affairs
 - iii) Trial Balance
 - iv) Profit and Loss Account
 - c) Profit under **net worth method**, when there are **no** drawings and no additional capital is the difference between:
 - i) Assets and Liabilities
 - ii) Capital and Liabilities
 - iii) **Assets and Capital**
 - iv) Closing Capital and Opening Capital.
 - d) To ascertain the real profit, the difference between the closing capital **and opening capital** is adjusted by:
 - i) deducting the drawings and adding the additional capital introduced
 - ii) adding the drawings and deducting the additional capital introduced
 - iii) deducting both the drawings and the additional capital.
 - iv) adding both the drawings and the additional capital
- 2 The amounts of opening assets and closing assets of a firm are Rs. 80,000 and Rs. 1,30,000 respectively, and the amounts of opening and closing external liabilities are Rs. 50,000 and Rs. 80,000 respectively. Calculate the profit earned during the year under the following circumstances :
 - i) if there are no drawings made and no additional capital brought in by the proprietors;
 - ii) if there are no drawings but Rs. 10,000 was introduced as additional capital by one of the partners;
 - iii) if drawings by the partners amounted to Rs. 8,000 but no additional capital was introduced;
 - iv) if drawing by partners amounted to Rs. 8,000 and one of the partners had introduced Rs. 10,000 as additional capital during the year.

15.7 LET US SUM UP

The system of keeping partial or incomplete records is popularly known as **Single Entry System**. It is usually employed by small traders or professionals. Limited companies cannot adopt this system of accounting.

Under this system only Cash Book and the personal accounts of **customers** and suppliers are **maintained**. No real and nominal accounts are maintained. One has to depend mainly on **original** vouchers and other documents to collect necessary data for ascertaining the assets and liabilities. Proper final accounts cannot be prepared. Hence, the profit or loss of the business is ascertained in an indirect manner by following either the net worth **method** or the conversion method.

Under net worth method, the profit or loss is calculated by comparing the opening capital with closing capital. Any increase in capital over the year is regarded as profit and the decrease as loss. To find out the opening and closing capitals we have to make use of the Accounting Equation (Capital=Assets– External Liabilities) and prepare the necessary Statement of Affairs.

To ascertain the true profit, adjustments have to be made in the closing capital in respect of additional capital introduced, drawings made and other items affecting the profits such as depreciation, etc. If it is the case of a partnership, items like **interest on capital** and **interest on drawings** may also be involved. The net profit or net loss will have to be distributed amongst the partners according to their **profit-sharing ratio** and the individual capitals of partners found out by preparing their capital accounts,

15.8 KEY WORDS

Net Worth : The difference between the total assets and the total external liabilities. It is equal to capital.

Profit and Loss Appropriation Account : An account prepared to show the distribution of profits amongst the partners.

Statement of Affairs : A statement of assets and liabilities based on incomplete records. It is prepared for ascertaining the opening or closing capitals.

15.9 SOME USEFUL BOOKS

Gupta R.L. and M. Radhakrishna, 1986. **Advanced Accountancy**, Sultan Chand & Sons: New Delhi. (Chapter 15 Section II).

Maheshwari S.N., 1986. **Introduction to Accounting**, Vikas Publishing House: New Delhi. (Chapter 16).

Patil, V.A. and J.S. Korlaiahalli, 1986. **Principles and Practice of Accounting**, R. Chand & Co., New Delhi. (Chapter 6, Section II).

Shukla, M.C. and T.S. Grewal, 1987. **Advanced Accounts**, S. Chand & Co: New Delhi (Chapter 8).

William Pickles, 1982. **Accountancy**, E.L.B.S. and Pitman, London. (Chapter 2).

15.10 ANSWERS TO CHECK YOUR PROGRESS

A 1 i) False ii) False iii) True iv) True v) False
2 i) can **not** ii) small traders; **professionals** iii) personal accounts; Cash Book
iv) limited companies v) **Real**; nominal
3 a) ii b) iii c) i

B 1 a) iv b) ii c) iv d) ii
2 i) Rs. 20,000
ii) Rs. 10,000
iii) Rs. 28,000
iv) Rs. 18,000

Questions

- 1 What is a Single Entry System? Distinguish it from Double Entry System.
- 2 Why do some persons prefer to keep their accounts in the form of incomplete records? State the salient features of such records:
- 3 Discuss the drawbacks of Single Entry System of accounting. Briefly explain the two methods of ascertaining profit when accounting records are incomplete.

Exercises

- 1 Calculate the profit or loss from the following data: Withdrawals by the proprietor during the year Rs. 15,000. Capital at the beginning of the year Rs. 60,000. Capital at the end of the year Rs. 1,00,000. Capital brought in by the proprietor during the year Rs. 25,000.

(Answer : Profit Rs. 20,000)

- 2 Calculate the net profit from the following information: Capital in the beginning of the year Rs. 40,000. Drawings during the year Rs. 10,750. Capital at the end of the Year Rs. 90,000. Capital introduced by the proprietor on July 1 Rs. 35,000. Interest allowed on capital @ 10% per annum.

(Answer : Profit after allowing interest on Capital of Rs. 5,750 is Rs. 20,000).

- 3 From the following information, prepare a Statement of Affairs and Calculate profits earned during the year ending December 31, 1988.

	as on 1.1.88	as on 31.12.88
	Rs.	Rs.
Cash in hand	8,000	10,000
Bank Overdraft	28,000	18,000
Stock in trade	37,000	43,000
Sundry Creditors	26,000	22,000
Sundry Debtors	32,000	30,000
Bills Receivable	8,000	5,000
Furniture & Fittings	5,000	4,000
Machinery	40,000	36,000
Buildings	50,000	49,000
Bills Payable	4,000	6,000
Motor Vehicle	—	24,000
Unpaid Expenses	800	600

(Answer : Opening Capital Rs. 1,21,200; Closing Capital Rs. 1,54,400; Profit Rs. 33,200)

- 4 Jai Prakash has not kept proper books of accounts. His position on December 31, 1987 was as follows:

Cash in hand Rs. 2,000; Cash at Bank Rs. 5,000; Stock in trade Rs. 36,000; Sundry Debtors Rs. 24,000; Fixtures and Fittings Rs. 12,000; Machinery Rs. 40,000; Sundry Creditors Rs. 28,000; Loan from his friend Rajesh Rs. 20,000; Prepaid Expenses Rs. 400. During the year Jai Prakash introduced additional capital on October 1, 1988 amounting to Rs. 20,000 and his drawings during the year were Rs. 500 per month.

On December 31, 1988 his position was as follows;

Cash in hand Rs. 15,000; Bank Overdraft Rs. 25,000;
Machinery Rs. 40,000;
Stock in trade Rs. 44,000; Sundry Debtors Rs. 32,000; Furniture and Fittings Rs. 20,000; Sundry Creditors Rs. 34,000; Outstanding Expenses Rs. 1,000.

He has purchased additional furniture worth Rs. 8,000 on May 1, 1988 and the loan from his friend still remains unpaid. Calculate profit earned during the year after allowing interest on capital @ 10% per annum and charging depreciation on Machinery @ 10% and on Furniture & Fittings @ 15% per annum.

(Answer: Opening Capital Rs. 71,400; Closing Capital Rs. 64,400; Loss for the year Rs. 28,640; Interest on Capital Rs. 7,640)

5. The following is the Statement of Affairs of A, B and C as on December 31, 1988 :

Liabilities	Amount	Assets	Amount
	Rs.		Rs.
Sundry Creditors	18,000	Cash in hand	2,400
Bills Payable	5,000	Sundry Debtors	24,000
Capital Accounts		Stock in trade	26,000
A - 30,000		Furniture	10,000
B - 20,000		Machinery	50,000
C - 15,000	65,000	Buildings	35,000
Bank Lомн	60,000	Prepaid Expenses	600
	1,48,000		
			1,48,000

The partners share profits in the ratio of 5 : 3 : 2 after allowing interest on capital @ 10% per annum. The drawings were A - Rs. 800, B - Rs. 600 and C - Rs. 500 per month. Interest charged on drawings was A - Rs. 480, B - Rs. 360 and C - Rs. 300.

On December 31, 1988 the assets and liabilities of the firm were as follows:

Cash in hand Rs. 3,600; Sundry Debtors Rs. 32,000; Stock in trade Rs. 35,000; Furniture Rs. 16,000; Machinery Rs. 50,000; Buildings Rs. 35,000; Sundry Creditors Rs. 20,000; Bills Payable Rs. 6,000; Unpaid Expenses Rs. 800.

New furniture worth Rs. 6,000 was purchased on April 1, 1988. The Bank Loan is repaid to the extent of 40%. Depreciation has to be provided @ 20% on furniture; 10% on machinery and 2% on buildings per annum. A brought additional capital of Rs. 10,000 on July 1, 1988. Calculate the profit and prepare the Statement of Affairs as on December 31, 1988 as it stands in the books of the firm.

(Answer: Closing Capital after providing for depreciation Rs. 1,00,200; Net Profit after accounting for interest on Capital and drawings Rs. 42,140)

Note: These questions will help you to understand the unit better. Try to write answers for them. But do not submit your answers to the University. These are for your practice only.

UNIT 16 ACCOUNTS FROM INCOMPLETE RECORDS-II

Structure

- 16.0 Objectives
- 16.1 Introduction
- 16.2 Conversion Method
 - 16.2.1 Full Conversion Method
 - 16.2.2 Abridged Conversion Method
- 16.3 Missing Items and Their Ascertainment
 - 16.3.1 Opening Capital
 - 16.3.2 Credit Sales
 - 16.3.3 Credit Purchases
 - 16.3.4 Cash and Bank Balances
- 16.4 Preparation of Final Accounts
- 16.5 Let Us Sum Up
- 16.6 Some Useful Books
- 16.4 Answers to Check Your Progress
- 16.8 Terminal Questions/Exercises

16.0 OBJECTIVES

After studying this unit you should be able to:

- explain full conversion method and describe how records maintained on single entry system can be converted into double entry records
- explain abridged conversion method and describe how missing items can be ascertained
- prepare Trading and Profit & Loss Account and Balance Sheet from incomplete records,

16.1 INTRODUCTION

You know there are two methods of ascertaining the profit or loss of a business which does not maintain complete accounting records. In Unit 15 you learnt in detail about the first method viz., Net Worth Method. No doubt, the Net Worth Method helps us to ascertain the profits earned during the accounting period and prepare the Statement of Affairs as at the end. But, certain vital information regarding operational aspects of the business cannot be ascertained and many important questions relating to the operational efficiency of the firm remain unanswered. For example, the information regarding sales, purchases and operating expenses is not available and so we cannot workout the rate of gross profit earned by the firm. Thus, neither a meaningful analysis of various aspects of business operations nor measurement of the comparative efficiency of the firm can be made. Hence, the second method viz., the Conversion Method is adopted by most of the firms. This helps in digging out the necessary information and prepare proper final accounts for the business. In this unit you will learn how such information is extracted from the incomplete records and how profit or loss is ascertained under the Conversion Method by preparing proper Profit & Loss Account and the Balance Sheet.

16.2 CONVERSION METHOD

In Unit 15 you learn that the Conversion Method involves preparation of proper Profit and Loss Account and the Balance Sheet. There are two ways of doing it: (1) preparation of final accounts after converting the single entry records into complete double entry records