



CA FOUNDATION • PAPER 1 • ACCOUNTING

Student Notes

Topic by Topic • October 2026 Edition



11 Chapters • 33 Units • 228 Topics • 524 Classified Questions

ICAI Study Material 2026 July + Scanner Accounting 2026 October V1

How this book works

For each topic, first read the Study Material paragraphs named in the “Read first” line. Then work down the skill bands — each band names the skill the examiner has actually used on that topic, and lists the exact Scanner questions to practise at it.

The section that follows the Contents — **How to Use These Notes** — explains the question lines, ICAI’s Manner of Assessment, and what the skill mix should change about your preparation. Read it once before you begin.

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BEFORE YOU START

How to Use These Notes

Every question in the Scanner has been read and classified — **524 of them in this paper** — against the skill framework ICAI itself publishes. These notes are built around that classification rather than around the syllabus order. Ten minutes spent on this page will change how you use the rest of the book.

1. How a topic is laid out

	Read it like this
Read first	The exact Study Material paragraphs the topic rests on. Open the Study Material and read them before the notes — the notes assume you have.
Notes	What the topic actually turns on, written for the examination rather than for coverage. Short, and meant to be re-read the night before.
Skill bands	One band for each skill the examiner has actually used on that topic, each with a few lines of guidance and the exact Scanner questions to practise. Work down the bands in the order printed: they run from the least demanding skill to the most.
Concept base	A topic the examiner has not yet reached. It is not optional — it has simply not been asked, and it is examinable. This paper carries 84 of them .

2. Reading a question line

PQ 5.24 · PYQ 2026-Sep [2] (b) · 10M · Pg 173

LEVEL II
Application

Hard

Part of the line	What it tells you
PQ 5.24	The Scanner's own question number. PQ is a practical question, TQ a theory question.
PYQ 2026-Sep [2] (b)	Where it was asked — PYQ past examination, MTP mock test paper, RTP revision test paper — then the sitting, and its number in that paper.
{C}	A case-scenario question.
DESC · TF · SN · DB	The kind of theory question: descriptive, true/false, short note, distinguish between. Practical questions carry no such tag.
10M	Marks, as printed in the Scanner. Blank where the source does not print them — RTPs often do not.

Part of the line	What it tells you
Pg 173	The page of the Scanner where the question and its answer are printed.
LEVEL II Application	ICAI's skill level, and the skill within it. Section 3 explains these.
asked 8×	The same question has been set that many times across past papers, mock tests and revision tests. Treat these as the highest priority.
Hard	How demanding the question is — judged on the marks it carries and the number of separate things it asks for.

3. The Manner of Assessment — what each skill asks of you

ICAI publishes a **Skill Assessment Specification Grid**. It states three skill levels, and in its **Manner of Assessment of Skills** column it describes each level as two distinct skills. Those six skills are the band headings that run through this book.

Skill	Rolls up to	What the examiner is asking you to do	Directive verbs to watch for
Remembering	Level I	Reproduce what you have learnt, as you learnt it.	Define · List · State · Name · Enumerate · Recognise
Understanding	Level I	Explain it, and place it in context — show you have grasped why the rule is what it is.	Describe · Explain · Distinguish · Identify · Illustrate · Outline
Application	Level II	Use or demonstrate the knowledge, concept or technique. Work the problem.	Apply · Calculate · Determine · Prepare · Reconcile · Record · Perform · Use · Conduct · Demonstrate
Analysis	Level II	Examine the interrelationships between distinct areas to identify root causes and find evidence that supports a judgement.	Analyse · Discuss · Compare and Contrast · Examine · Develop · Monitor · Prioritise · Align · Communicate
Evaluation	Level III	Assess the problem and use judgement to reach a conclusion.	Advise · Evaluate · Recommend · Review · Select · Assess
Synthesis	Level III	Integrate data and information, separating the relevant facts from the irrelevant.	ICAI lists no verb for synthesis.

ICAI prints the verbs for **Application** and **Analysis** as two separate lists, so that division is the Institute's own. For Level I and for Level III it prints one combined list each — so the line between **Remembering and Understanding**, and between **Evaluation and Synthesis**, follows ICAI's description of the manner of assessment rather than a published list of verbs.

CA Foundation is assessed at Levels I and II only — the Prospectus prints no Level III column for this course, which is why the last two rows above are greyed. Evaluation and Synthesis begin at Final.

4. What the skill mix should change about your preparation

ICAI grades this paper **Level I 5–20%** and **Level II 80–95%** of marks. Two things follow that are easy to miss.

- **Reading is not preparing.** Four marks in five are for working a problem, not for describing one. A topic you can explain but have never worked through is a topic you have not prepared.
- **The paper's balance is not each chapter's balance.** Every chapter opens with its own **ICAI Skill Profile** panel, showing how that chapter's marks actually divide and what that means for preparing it. Some chapters are almost all theory; others carry almost none. Read the panel before you start the chapter.

5. Two guides at the front of the book

	What it is for
Topic Ranking	Every examined topic ranked by its share of the classified Scanner questions, and graded A , B or C on cumulative coverage. Category A carries the first 60% of all questions — secure those to full command first.
Importance grade	The A–D grade printed against each chapter and unit in the Contents. This is ICAI's syllabus weightage signal as the Scanner publishes it, and it is separate from the question-frequency ranking. Where the two disagree, prepare to the higher of the two.

STUDY PRIORITY GUIDE

Topic Ranking — Exam Weightage

Read first: Every topic in this booklet that the examiner has actually asked is ranked below by its share of the 524 classified Scanner questions, aggregated across all 33 Units — and graded A, B or C on cumulative coverage. **Category A (ranks 1–30)** covers the first 60% of all classified questions. **Category B (ranks 31–52)** adds the next 15%, taking coverage to about 75%. **Category C** is the remaining 25%: a long tail that is slower to mine for marks, much of which gets covered automatically while preparing A and B. The **Pg.** column cross-references the page on which that topic's study notes begin.

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
1	A	Accounting Process	Rectification of Errors	5.0%	5.0%	88
2	A	Theoretical Framework	Concepts, Principles and Conventions - An Overview	4.8%	9.7%	29
3	A	Bank Reconciliation Statement	Methods of Bank Reconciliation	4.6%	14.3%	96
4	A	Financial Statements of Non-Profit Organisations	Balance Sheet	3.8%	18.1%	153
5	A	Accounts from Incomplete Records	Techniques of Obtaining Complete Accounting Information	3.6%	21.8%	161
6	A	Depreciation and Amortisation	Profit or Loss on The Sale/Disposal of Property, Plant and Equipment	2.9%	24.6%	111
7	A	Theoretical Framework	Capital Expenditures and Revenue Expenditures	2.5%	27.1%	33
8	A	Company Accounts	Re-issue of Forfeited Shares	2.3%	29.4%	221
9	A	Company Accounts	Methods of Redemption of Fully Paid-Up Shares	2.3%	31.7%	237
10	A	Inventories	Inventories Taking	2.1%	33.8%	105
11	A	Financial Statements of Non-Profit Organisations	Income and Expenditure Account	2.1%	35.9%	151
12	A	Preparation of Final	Integrated Problems	1.9%	37.8%	143

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
		Accounts of Sole Proprietors				
13	A	Theoretical Framework	Capital Receipts and Revenue Receipts	1.5%	39.3%	35
14	A	Accounting Process	Types of Errors	1.5%	40.8%	86
15	A	Partnership and LLP Accounts	Revaluation Account or Profit and Loss Adjustment Account	1.5%	42.4%	179
16	A	Partnership and LLP Accounts	Integrated Problems	1.5%	43.9%	189
17	A	Partnership and LLP Accounts	Integrated Problems	1.5%	45.4%	195
18	A	Depreciation and Amortisation	Methods for Providing Depreciation	1.3%	46.8%	109
19	A	Depreciation and Amortisation	Change in the Method of Depreciation	1.3%	48.1%	113
20	A	Company Accounts	Issue of Bonus Shares	1.3%	49.4%	232
21	A	Accounting Process	Journal	1.1%	50.6%	60
22	A	Accounting Process	Sales Book	1.1%	51.7%	75
23	A	Preparation of Final Accounts of Sole Proprietors	Design of A Manufacturing Account	1.1%	52.9%	147
24	A	Partnership and LLP Accounts	Methods for Goodwill Valuation	1.1%	54.0%	174
25	A	Partnership and LLP Accounts	Loss arising from Insolvency of a Partner	1.1%	55.2%	201
26	A	Accounting Process	Kinds of Cash Book	1.0%	56.1%	81
27	A	Inventories	Basis of Inventory Valuation	1.0%	57.1%	100
28	A	Bills of Exchange and Promissory Notes	Insolvency	1.0%	58.0%	129
29	A	Partnership and LLP Accounts	Main Clauses in A Partnership Deed	1.0%	59.0%	168
30	A	Partnership and LLP	Piecemeal Payments	1.0%	59.9%	202

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
Accounts						
31	B	Company Accounts	Methods of Redemption of Debentures	1.0%	60.9%	243
32	B	Accounting Process	Accounting for GST	0.8%	61.6%	62
33	B	Inventories	Formulae/Methods to Determine Cost of Inventory	0.8%	62.4%	103
34	B	Depreciation and Amortisation	Introduction	0.8%	63.2%	107
35	B	Preparation of Final Accounts of Sole Proprietors	Profit and Loss Account	0.8%	63.9%	136
36	B	Preparation of Final Accounts of Sole Proprietors	Certain Adjustments and their Treatments	0.8%	64.7%	138
37	B	Preparation of Final Accounts of Sole Proprietors	Balance Sheet	0.8%	65.5%	139
38	B	Financial Statements of Non-Profit Organisations	Nature of Receipts and Payments Account	0.8%	66.2%	149
39	B	Partnership and LLP Accounts	Limited Liability Partnership	0.8%	67.0%	165
40	B	Partnership and LLP Accounts	Fixed and Fluctuating Capital	0.8%	67.7%	171
41	B	Partnership and LLP Accounts	Reserves in the Balance Sheet	0.8%	68.5%	181
42	B	Theoretical Framework	Distinction Between Contingent Liabilities and Provisions	0.6%	69.1%	40
43	B	Theoretical Framework	Change in Accounting Policies	0.6%	69.7%	43
44	B	Theoretical Framework	Benefits and Limitations of Accounting Standards	0.6%	70.2%	50
45	B	Accounting Process	Advantages of Double Entry System	0.6%	70.8%	55
46	B	Accounting Process	Rules of Preparing the Trial	0.6%	71.4%	71

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
Balance						
47	B	Accounting Process	Introduction	0.6%	71.9%	72
48	B	Accounting Process	Purchases Book	0.6%	72.5%	74
49	B	Accounting Process	Sales Return Books or Returns Inward Book	0.6%	73.1%	77
50	B	Accounting Process	Purchase Returns or Returns Outward Book	0.6%	73.7%	78
51	B	Depreciation and Amortisation	Revaluation of Property, Plant and Equipment	0.6%	74.2%	115
52	B	Bills of Exchange and Promissory Notes	Renewal of Bill	0.6%	74.8%	127
53	C	Bills of Exchange and Promissory Notes	Accommodation Bills	0.6%	75.4%	130
54	C	Accounts from Incomplete Records	Ascertainment of Profit by Capital Comparison	0.6%	76.0%	159
55	C	Partnership and LLP Accounts	Profit and Loss Appropriation	0.6%	76.5%	170
56	C	Company Accounts	Calls-In-Arrears and Calls-In Advance	0.6%	77.1%	218
57	C	Company Accounts	Forfeiture of Shares	0.6%	77.7%	220
58	C	Company Accounts	Issue of Debentures	0.6%	78.2%	227
59	C	Company Accounts	Treatment of Discount/Loss on Issue of Debentures	0.6%	78.8%	230
60	C	Company Accounts	Interest on Debentures	0.6%	79.4%	231
61	C	Theoretical Framework	Distinction Between Book-Keeping and Accounting	0.4%	79.8%	24
62	C	Theoretical Framework	Limitations of Accounting	0.4%	80.2%	27
63	C	Theoretical Framework	Contingent Liabilities	0.4%	80.5%	37
64	C	Accounting Process	Accounting Equation Approach	0.4%	80.9%	58
65	C	Accounting Process	Posting	0.4%	81.3%	65
66	C	Accounting Process	Objectives of Preparing the	0.4%	81.7%	68

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
			Trial Balance			
67	C	Accounting Process	Cash Book -- A Subsidiary Book and a Principal Book	0.4%	82.1%	80
68	C	Accounting Process	Petty Cash Book	0.4%	82.4%	83
69	C	Bank Reconciliation Statement	Bank Reconciliation Statement	0.4%	82.8%	93
70	C	Bank Reconciliation Statement	Importance of Bank Reconciliation Statement	0.4%	83.2%	94
71	C	Inventories	Inventory Record Systems	0.4%	83.6%	102
72	C	Depreciation and Amortisation	Factors in the Measurement of Depreciation	0.4%	84.0%	108
73	C	Bills of Exchange and Promissory Notes	Differences - Bill of Exchange and Promissory Note	0.4%	84.4%	121
74	C	Bills of Exchange and Promissory Notes	How to Calculate Due Date of a Bill	0.4%	84.7%	125
75	C	Bills of Exchange and Promissory Notes	Noting Charges	0.4%	85.1%	126
76	C	Bills of Exchange and Promissory Notes	Retirement of Bills of Exchange & Rebate	0.4%	85.5%	128
77	C	Preparation of Final Accounts of Sole Proprietors	Trading Account	0.4%	85.9%	135
78	C	Partnership and LLP Accounts	Definition and Features of Partnership	0.4%	86.3%	164
79	C	Partnership and LLP Accounts	Goodwill	0.4%	86.6%	173
80	C	Partnership and LLP Accounts	Hidden Goodwill	0.4%	87.0%	183
81	C	Partnership and LLP Accounts	Closing of Partnership Books on Dissolution	0.4%	87.4%	199
82	C	Partnership and LLP Accounts	Winding up of a Limited Liability Partnership (LLP)	0.4%	87.8%	204
83	C	Partnership and LLP	Integrated Problems	0.4%	88.2%	205

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
Accounts						
84	C	Company Accounts	Issue of Shares for Cash	0.4%	88.5%	214
85	C	Company Accounts	Shares Issued at Discount	0.4%	88.9%	215
86	C	Company Accounts	Interest on Calls-in-Arrears and Calls-in- Advance	0.4%	89.3%	219
87	C	Company Accounts	Issue of Debentures in Consideration other than for Cash	0.4%	89.7%	229
88	C	Company Accounts	Right Issue	0.4%	90.1%	234
89	C	Company Accounts	Redemption of Preference Shares by Capitalisation of Undistributed Profits	0.4%	90.5%	239
90	C	Theoretical Framework	Functions of Accounting	0.2%	90.6%	22
91	C	Theoretical Framework	Sub-Fields of Accounting	0.2%	90.8%	25
92	C	Theoretical Framework	Users of Accounting Information	0.2%	91.0%	25
93	C	Theoretical Framework	Role of Accountant in the Society	0.2%	91.2%	28
94	C	Theoretical Framework	Considerations in Determining Capital and Revenue Expenditures	0.2%	91.4%	32
95	C	Theoretical Framework	Distinction Between Contingent Liabilities and Liabilities	0.2%	91.6%	39
96	C	Theoretical Framework	Meaning of Accounting Policies	0.2%	91.8%	41
97	C	Theoretical Framework	Selection of Accounting Policies	0.2%	92.0%	42
98	C	Theoretical Framework	Valuation Principles	0.2%	92.2%	46
99	C	Theoretical Framework	Objectives of Accounting Standards	0.2%	92.4%	49
100	C	Theoretical Framework	Process of Formulation of Accounting Standards in India	0.2%	92.6%	51

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
101	C	Accounting Process	Double Entry System	0.2%	92.7%	54
102	C	Accounting Process	Transactions	0.2%	92.9%	57
103	C	Accounting Process	Modern Classification of Accounts	0.2%	93.1%	60
104	C	Accounting Process	Advantages of Journal	0.2%	93.3%	62
105	C	Accounting Process	Introduction	0.2%	93.5%	64
106	C	Accounting Process	Balancing an Account	0.2%	93.7%	66
107	C	Accounting Process	Limitations of Trial Balance	0.2%	93.9%	69
108	C	Bank Reconciliation Statement	Introduction	0.2%	94.1%	91
109	C	Inventories	Inventory Valuation	0.2%	94.3%	99
110	C	Depreciation and Amortisation	Revision of the Estimated Useful Life of Property, Plant and Equipment	0.2%	94.5%	114
111	C	Depreciation and Amortisation	Amortisation	0.2%	94.7%	117
112	C	Bills of Exchange and Promissory Notes	Bills of Exchange	0.2%	94.8%	119
113	C	Bills of Exchange and Promissory Notes	Promissory Notes	0.2%	95.0%	120
114	C	Bills of Exchange and Promissory Notes	Days of Grace	0.2%	95.2%	123
115	C	Bills of Exchange and Promissory Notes	Integrated Problems	0.2%	95.4%	133
116	C	Preparation of Final Accounts of Sole Proprietors	Limitations of Financial Statements	0.2%	95.6%	142
117	C	Preparation of Final Accounts of Sole Proprietors	Manufacturing Costs	0.2%	95.8%	146
118	C	Financial Statements of Non-Profit Organisations	Educational Institution	0.2%	96.0%	156

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
119	C	Accounts from Incomplete Records	Introduction	0.2%	96.2%	158
120	C	Partnership and LLP Accounts	Distinction Between an Ordinary Partnership Firm and An LLP	0.2%	96.4%	167
121	C	Partnership and LLP Accounts	Accounting Treatment of Goodwill in Case of Retirement or Death of a Partner	0.2%	96.6%	177
122	C	Partnership and LLP Accounts	Calculation of Gaining Ratio	0.2%	96.8%	184
123	C	Partnership and LLP Accounts	Joint Life Policy	0.2%	96.9%	187
124	C	Partnership and LLP Accounts	Introduction	0.2%	97.1%	191
125	C	Partnership and LLP Accounts	Special Transactions in Case of Death: Joint Life Policy	0.2%	97.3%	192
126	C	Partnership and LLP Accounts	Special Transactions in Case of Death: Separate Life Policy	0.2%	97.5%	193
127	C	Partnership and LLP Accounts	Special Transactions in Case of Death: Payment of Deceased Partner's Share	0.2%	97.7%	194
128	C	Partnership and LLP Accounts	Consequences of Dissolution	0.2%	97.9%	198
129	C	Company Accounts	Introduction	0.2%	98.1%	207
130	C	Company Accounts	Types of Companies	0.2%	98.3%	209
131	C	Company Accounts	Share Capital	0.2%	98.5%	212
132	C	Company Accounts	Types of Shares	0.2%	98.7%	213
133	C	Company Accounts	Shares Issued at Premium	0.2%	98.9%	216
134	C	Company Accounts	Over Subscription and Pro-Rata Allotment	0.2%	99.0%	217
135	C	Company Accounts	Meaning	0.2%	99.2%	224
136	C	Company Accounts	Features of Debentures	0.2%	99.4%	225

#	CAT.	CHAPTER	TOPIC	SHARE	CUM.	PG.
137	C	Company Accounts	Types of Debentures	0.2%	99.6%	226
138	C	Company Accounts	Issue of Debentures as Collateral Security	0.2%	99.8%	228
139	C	Company Accounts	Debenture Redemption Reserve	0.2%	100.0%	242

Share % is a question-frequency signal drawn from the Scanner — what has actually been asked. The **Importance grade (A-D)** printed against each Chapter and Unit is ICAI's own weightage signal as published in the Scanner's front matter. The two measure different things, and where they diverge, prepare to the higher of the two standards. A further **84 topics** are declared in the Scanner's frequency tables but carry no question yet; they are badged **CONCEPT BASE** in the notes and are not ranked here.

CHAPTER 1

Theoretical Framework

37 Topics · 72 Classified Questions · Importance: A

ICAI SKILL PROFILE Level I 5–20% · Level II 80–95% — this chapter reads **theory-heavy**

Level I — Remembering & Understanding **93.9%** 154 of 164 marks

Level II — Application & Analysis **6.1%** 10 of 164 marks

Unit 1.1: Meaning and Scope of Accounting

P1-C1-U1.1 · Importance B · Rank 3 in chapter · Category B · 11.1% of chapter questions · 8 questions

Topic 1: Introduction

P1-C1-U1.1-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.1: economic activities carried through transactions and events, with the stationery-shop and municipal-corporation examples.

NOTES

Economic activities: every individual/entity (salaried person, club, business, company, local authority, Government) performs economic activities — not always for individual benefit, some create social benefit; such activities are performed through “transactions and events”.

Transaction vs event: transaction means “a business, performance of an act, an agreement” while event means “a happening, as a consequence of transaction(s), a result” — e.g. purchase/sale of goods, investment and rent paid are transactions; the surplus earned (₹42,000 in the SM example) and goods still in hand are events.

Why accounting: everybody wants records of transactions/events and adequate information as an aid to decision-making — accounting deals with measurement of economic activities involving inflow and outflow of economic resources, has universal application, and aims to meet the information needs of rational decision-makers — hence called the language of business.

Topic 2: Meaning of Accounting

P1-C1-U1.1-T02

Read first Read Para 1.2 of the Study Material: the 1961 AICPA definition, the 1966 American Accounting Association definition, and the six procedural aspects of accounting (recording, classifying, summarising, analysing, interpreting, communicating).

NOTES

1961 (AICPA Committee on Terminology): "Accounting is the art of recording, classifying, and summarising in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character, and interpreting the result thereof."

1966 (American Accounting Association): "The process of identifying, measuring and communicating economic information to permit informed judgments and decisions by the users of accounts." — communication to users is now part of accounting itself.

Six procedural aspects: (1) Recording — the basic function; Journal/subsidiary books. (2) Classifying — grouping like transactions; the Ledger. (3) Summarising — trial balance and financial statements. (4) Analysing — relationships between P&L and Balance Sheet items. (5) Interpreting — explaining meaning and significance for users. (6) Communicating — the final stage: transmitting the results through reports, ratios, graphs. The first two (plus trial balance) are book-keeping; the rest are accounting.

Understanding explain with reasons — no question in this edition

- Be able to justify that accounting DOES involve communication - the modern (1966 AAA) definition treats accounting as 'the process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users'.
- Explain why the old 1961 definition (recording, classifying, summarising, interpreting) is incomplete today - diversified ownership and globalisation make communicating results an essential accounting function.
- For True/False answers, always link the reason to the procedural stages: recording is the basic function, communicating is the final stage transmitting analysed information to end-users.

Topic 3: Evolution of Accounting as a Social Science

P1-C1-U1.1-T03

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §1.3: history from Egypt/Babylonia/Greece/Rome/China/Kautilya to Luca Pacioli, the four phases of evolution, and why accounting is a social science.

NOTES

History: roots around 4000 BC (Egyptian treasuries); Babylonia used it to detect fraud losses; Kautilya's Arthashastra described maintenance of accounting records in India; Luca Pacioli's Summa de Arithmetica, Geometria, Proportio et Proportionalita (Venice, 1494) is the first book on double entry book-keeping and used the terms Debit (Dr., from Italian debito — owed to the proprietor) and Credit (Cr., from credito/Latin credo — trust or belief).

Four phases: (i) Stewardship Accounting — stewards of wealthy men rendered periodic account of their stewardship, the root of financial accounting; (ii) Financial Accounting — with joint stock companies and divorce of ownership from management, disclosure of financial statements moulded by law; (iii) Management Accounting — 20th-century development aiding management decision-making; (iv) Social Responsibility Accounting — formative stage, accounting for social costs incurred (pollution, use of society's resources) and social benefits created (employment, better products).

Social science: usefulness of accounting to society as a whole is the fundamental criterion — it generates information for social good, serves social purpose, contributes to and adapts with social progress, hence a social science.

Topic 4: Objectives of Accounting

P1-C1-U1.1-T04

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §1.4 and its chart: the five objectives from systematic recording to solvency.

NOTES

Five objectives: (i) Systematic recording of transactions (book-keeping — journal, ledger, trial balance); (ii) Ascertainment of results — P&L A/c shows profit (revenue exceeds expenses) or loss for the period; (iii) Ascertainment of financial position — Balance Sheet states assets (what he owns) and liabilities (what he owes) at a point of time; (iv) Providing information to users for rational decision-making through financial statements; (v) To know the solvency position — ability to meet liabilities in short run (liquidity) and long run (solvency) as and when they fall due.

Topic 5: Functions of Accounting

P1-C1-U1.1-T05

Read first Study Para 1.5 - the six main functions of accounting: Measurement, Forecasting, Decision-making, Comparison & Evaluation, Control, and Government Regulation and Taxation.

NOTES

Six functions: (a) Measurement — past performance and current financial position; (b) Forecasting — future performance from past data; (c) Decision-making — relevant information for rational decisions; (d) Comparison & Evaluation — performance against targets, disclosure of policies and contingent liabilities; (e) Control — identifying operational weaknesses, giving feedback; (f) Government Regulation and Taxation — information for control and tax collection.

Keep separate — the four OBJECTIVES: systematic recording (book-keeping); ascertainment of results (P&L); ascertainment of financial position (Balance Sheet); communicating information to users (financial reports).

Understanding explain with reasons · 1 question

- Be ready to explain any four functions in one or two lines each for a 4-mark question - e.g. Measurement (measures past performance and current financial position), Forecasting (projects future performance using past data).
- Explain Comparison & Evaluation as assessing performance against targets and disclosing policies/contingent liabilities, and Control as identifying operational weaknesses and giving feedback.
- Do not confuse functions of accounting with objectives of accounting (systematic recording, ascertaining results, financial position, solvency) - keep the two lists separate.

TQ 5.1 · PYQ 2025-Jan [1] (b) {C} · Descriptive · 4M · Pg 3

LEVEL I
Understanding

Medium

Topic 6: Book-keeping

P1-C1-U1.1-T06

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.6 and §1.6.1: meaning of book-keeping, its legal implications and its two objectives.

NOTES

Meaning: book-keeping is an activity concerned with recording of financial data relating to business operations in a significant and orderly manner — covers procedural aspects of accounting work, embraces record-keeping function, and its procedures are governed by the end product, the financial statements; accounting is based on a careful and efficient book-keeping system.

Objectives: (i) Complete recording of transactions — complete and permanent record of all transactions in a systematic and logical manner to show financial effect on the business; (ii) Ascertainment of financial effect — combined effect of all transactions of the period upon the

financial position of the business as a whole.

Legal side: books and financial statements of companies are guided by the Companies Act, banks/insurance by their special Acts; no specific legislation for sole-proprietorship and partnership.

Topic 7: Distinction Between Book-Keeping and Accounting

P1-C1-U1.1-T07

Read first Learn the six-point tabular distinction in Para 1.7 and the idea that book-keeping is the recording phase while accounting is the summarising phase; accounting starts where book-keeping ends.

NOTES

Core idea: book-keeping is the recording phase; accounting is the summarising phase — accounting starts where book-keeping ends. Hierarchy: Book-keeping $\subset$ Accounting $\subset$ Accountancy. The six-point distinction:

1. Book-keeping is a process concerned with recording of transactions.	Accounting is concerned with summarising of the recorded transactions.
2. It constitutes a base for accounting.	It is considered the language of the business.
3. Financial statements do not form part of this process.	Financial statements are prepared on the basis of book-keeping records.
4. Managerial decisions cannot be taken with the help of these records.	Management takes decisions on the basis of these records.
5. There is no sub-field of book-keeping.	It has several sub-fields: financial accounting, management accounting etc.
6. Financial position of the business cannot be ascertained.	Financial position is ascertained on the basis of accounting reports.

Understanding explain with reasons · 2 questions

- Reproduce at least four contrast points: book-keeping records transactions/is the base; accounting summarises/is the language of business; financial statements and managerial decisions belong to accounting, not book-keeping.
- Explain that book-keeping has no sub-fields and cannot show financial position, whereas accounting has sub-fields (financial, management accounting etc.) and ascertains financial position.
- Remember the hierarchy chart: Book-keeping is within Accounting, which is within Accountancy.

TQ 7.2 · PYQ 2025-Jan [1] (a) (v) {C} · True/False · 2M · Pg 4

LEVEL I
Understanding

Easy

TQ 7.1 · PYQ 2024-Sep [1] (b) {C} · Distinguish Between · 4M · Pg 3

LEVEL I
Understanding

Medium

Topic 8: Sub-Fields of Accounting

P1-C1-U1.1-T08

Read first Memorise the five sub-fields in Para 1.8 with a one-line description of each: Financial, Management, Cost, Social Responsibility and Human Resource Accounting.

NOTES

Five sub-fields: (i) Financial Accounting — historical; ends in P&L and Balance Sheet for external users. (ii) Management Accounting — internal reporting for planning, control, decision-making; includes cost accounting. (iv) Social Responsibility Accounting — social costs incurred and social benefits created. (v) Human Resource Accounting — identifies, quantifies and reports investments in human resources not covered by conventional accounting.

(iii) Cost Accounting (ICMA, England): “the process of accounting for cost which begins with the recording of income and expenditure or the bases on which they are calculated and ends with the preparation of periodical statements and reports for ascertaining and controlling costs.”

Remembering memorise · 1 question

- List: (i) Financial Accounting - historical, prepares P&L and Balance Sheet for external users; (ii) Management Accounting - internal reporting for planning, control, decision-making; (iii) Cost Accounting - cost ascertainment and control.
- (iv) Social Responsibility Accounting - accounts for social costs incurred and social benefits created; (v) Human Resource Accounting - identifies, quantifies and reports investments in human resources not covered by conventional accounting.
- Memorise the ICMA (England) definition of cost accounting for a 5-mark descriptive answer.

TQ 8.1 · PYQ 2023-Dec [6] (b) · Descriptive · 5M · Pg 4

LEVEL I
Remembering

Medium

Topic 9: Users of Accounting Information

P1-C1-U1.1-T09

Read first Study Para 1.9 - classification into internal and external users and the eight user groups (Investors, Employees, Lenders, Suppliers/Creditors, Customers, Government, Public, Management) with what each seeks.

NOTES

Two classes: internal users (owners/management — detailed reports) and external users (general-purpose financial statements).

Eight user groups and their interests: (i) Investors — buy/hold/sell; ability to survive, prosper, pay dividend. (ii) Employees — stability, growth; remuneration and retirement benefits. (iii) Lenders — repayment of principal and interest when due. (iv) Suppliers/creditors — ability to pay dues; sets their credit policy. (v) Customers — continued supply depends on the enterprise's stability and profitability. (vi) Government — regulation, resource allocation, price control, duties and taxes. (vii) Public — contribution to the local economy: employment, patronage of local suppliers. (viii) Management — effects of its decisions, basis for further decisions.

Understanding explain with reasons · 1 question

- True/False trap: 'Customers are not users of accounts' is FALSE - customers are concerned with stability and profitability because their own functioning depends on continued supply of goods (e.g. a pharma company depending on a chemical supplier).
- Be able to state each user's interest: investors - buy/hold/sell and dividend-paying ability; lenders - repayment of principal and interest; employees - stability, growth and retirement benefits; government - regulation and taxes.
- Distinguish internal users (owners/management, get detailed reports) from external users (served by general-purpose financial statements).

TQ 9.1 · PYQ 2025-Jan [1] (a) (ii) {C} · True/False · 2M · Pg 6

LEVEL I
Understanding

Easy

Topic 10: Relationship of Accounting with other Disciplines

P1-C1-U1.1-T10

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.10 (a)–(e): accounting's overlap with Economics, Statistics, Mathematics, Law and Management.

NOTES

Economics: accountants got ideas of value, income and capital maintenance from economists but moulded them for practice (e.g. acquisition cost as workable valuation base instead of present value of future earnings); micro-level accounting data summed up gives the macro-level database for economic decision models.

Statistics and Mathematics: accounting data is precise to the last paisa while statistics deals with

typical values/trends — statistical methods (ratios, time series, cross-sectional comparison, multiple discriminant analysis for sickness symptoms) aid interpretation; double entry can be put in algebraic/matrix form, and arithmetic/algebra are pre-requisites for interest, annuity, depreciation, hire-purchase and lease computations.

Law and Management: transactions are governed by Contract Act, Sale of Goods Act, Negotiable Instruments Act, and Companies Act prescribes financial-statement formats — accounting influences law and is influenced by law; in management, accountants play a key role since a large portion of accounting information is prepared for management decision-making and the system can be moulded to serve management purpose.

Topic 11: Limitations of Accounting

P1-C1-U1.1-T11

Read first Learn the seven limitations in Para 1.11 that must be kept in mind while evaluating financial statements, flowing from the assumptions, conventions and personal judgement underlying accounts.

NOTES

Root cause: accounting's assumptions, conventions and the accountant's personal judgement become its limitations — statements are never free from subjectivity. **The seven instances:** (1) non-monetary factors (loyalty, skill of personnel) find no place; (2) Balance Sheet shows the position only on the date of preparation, not the future; (3) changes like inflation are ignored; (4) accounting principles sometimes conflict; (5) estimates rest on personal judgement (doubtful debts, depreciation method, inventory valuation); (6) human resources are not shown — no accepted money valuation; (7) alternative policies for the same item invite manipulation.

Understanding explain with reasons · 2 questions

- Explain 4-5 limitations with reasons: non-monetary factors (staff loyalty, skill) are excluded; Balance Sheet shows only the position on the date of preparation, not the future; inflation/price-level changes are ignored.
- Also: accounting principles sometimes conflict with each other; estimates (provision for doubtful debts, depreciation method, inventory valuation) rest on personal judgement; alternative policies for the same item invite manipulation.
- True/False: 'Results and position disclosed by final accounts are not exact' is TRUE - figures are largely the outcome of the accountant's personal judgement and policy choices, so statements are never free from subjectivity.

TQ 11.1 · PYQ 2018-Nov [1] (b) {C} · Descriptive · 4M · Pg 6 asked 8×

LEVEL I
Understanding

Medium

Topic 12: Role of Accountant in the Society

P1-C1-U1.1-T12

Read first Study Para 1.12 (Areas of Service) - the services a Chartered Accountant renders to society, plus the CA's role in industry, public sector, fiscal policy and economic growth.

NOTES

Intro line: accountancy has crossed its usual domain of preparing, interpreting and auditing financial statements — CAs now serve in company law, taxation and general management. Goethe: “the fairest invention of the human mind”.

Six service areas: (i) Maintenance of Books of Accounts — net result and financial position; (ii) Statutory Audit — true and fair view reported for every limited company; (iii) Internal Audit — a management tool checking that accounts are properly maintained with adequate safeguards; (iv) Taxation — handling and representing before tax authorities; (v) Management Accounting & Consultancy — internal reporting for planning, control and special decisions; (vi) Financial Advice — investments, insurance, business expansion, investigations, pensions.

Remembering memorise · 1 question

- Memorise the main service heads: Maintenance of Books of Accounts, Statutory Audit, Internal Audit, Taxation, Management Accounting & Consultancy Services, Financial Advice.
- Under Financial Advice, recall the sub-areas: investments, insurance, business expansion, financial investigations, pension schemes.
- Other services to list if asked for more: secretarial work, share registration, company formation, receiverships/liquidations, arbitrations, cost accounts and information services.
- For the 4-mark answer, write the intro line - the practice of accountancy has crossed its usual domain of preparing, interpreting and auditing financial statements; CAs now serve in company law, taxation and general management matters - then list and briefly describe five or six service areas.

TQ 12.1 · PYQ 2020-Nov [1] (b) {C} · Descriptive · 4M · Pg 7 asked 6×

LEVEL I
Remembering

Medium

Unit 1.2: Accounting Concepts, Principles and Conventions

P1-C1-U1.2 · Importance A · Rank 1 in chapter · Category A · 34.7% of chapter questions · 25 questions

Topic 1: Concepts, Principles and Conventions - An Overview

P1-C1-U1.2-T01

Read first Master Para 2.5 - all twelve concepts (Entity, Money measurement, Periodicity, Accrual, Matching, Going Concern, Cost, Realisation, Dual aspect, Conservatism, Consistency, Materiality) - plus Para 2.6 on fundamental accounting assumptions.

NOTES

Twelve concepts (Para 2.5): (a) Entity – business is separate from owner; owner's personal payments from business funds are drawings charged to capital, not business expense; (b) Money measurement – only transactions measurable in money are recorded, in a uniform monetary unit (the ruling currency of the country); (c) Periodicity – infinite life is split into workable accounting periods (usually 1 April–31 March) so performance can be measured and 'accrual' becomes meaningful; (d) Accrual – “recognition of revenue and costs as they are earned or incurred and not as money is received or paid” (mercantile, not cash, basis); (e) Matching – Periodic profit = Periodic revenue – Matched expenses (based on accrual); (f) Going Concern – enterprise “will continue in operation for the foreseeable future”, having neither intention nor need to liquidate or curtail materially the scale of operations; (g) Cost – asset valued at historical/acquisition cost, chosen for objectivity; (h) Realisation – change in asset value counted only when realised; (i) Dual aspect – every transaction has two aspects, giving Equity + Liabilities = Assets (core of double entry); (j) Conservatism – anticipate no future income, provide for all possible losses; (k) Consistency – same accounting policies followed from period to period; (l) Materiality – insignificant items may be ignored, significant ones must be disclosed.

Three fundamental accounting assumptions (Para 2.6): Going Concern, Consistency, Accrual – if followed, nothing need be written (they are presumed); if any is NOT followed, the fact must be specifically disclosed in the financial statements.

Conventions & measurement (short notes): accounting conventions emerge out of accounting practices/usage adopted over a period of time, may be changed by the accountancy bodies of the world to improve information quality, and need not have universal application; measurement is in money terms – the four bases are historical cost, current cost, realisable value and present value.

Conservatism in practice: the current-asset rule ‘cost or market price whichever is lower’ originates here; it requires prudence, neutrality and faithful representation, and (per critics) leads to understatement of income and Balance Sheet assets; anticipated gains are never booked – hence no provision is made for discount on creditors.

True/False anchors: matching IS based on accrual (adjusts prepaid/outstanding expenses, accrued/unearned income); accrual is NOT recording when cash is received/paid – that is cash basis; materiality depends not only on the amount but also on size of business, nature and level of information and the level of the decision-maker; entity concept means the enterprise is liable to the owner for his capital; consistency does not bar introduction of improved accounting methods.

Remembering memorise · 2 questions

- Memorise the three fundamental accounting assumptions - Going Concern, Consistency, Accrual - and the disclosure rule: if followed, no disclosure needed; if NOT followed, the fact must be specifically disclosed.
- Short note on 'Measurement': transactions are measured in money (the ruling currency); the four bases are historical cost, current cost, realisable value and present value.
- Short note on 'Accounting conventions': they emerge from accounting practice/usage over time, may be changed by accountancy bodies, and need not have universal application.

TQ 1.13 · RTP 2023-Dec [19] (iv) · Short Note · --- · Pg 16 asked 8×	LEVEL I Remembering	Easy
TQ 1.19 · RTP 2024-Sep [18] (i) · Short Note · --- · Pg 19 asked 9×	LEVEL I Remembering	Easy

Understanding explain with reasons · 23 questions

- Explain each concept in 2-3 lines with an example - exams repeatedly ask Going Concern, Accrual vs Cash/Mercantile basis, Periodicity, Materiality, Conservatism, Money Measurement, Realisation and Matching.
- True/False traps: conservatism DOES understate Balance Sheet assets (True); accrual does NOT mean cash basis (False); matching IS based on accrual (True); money measurement = recording in a uniform monetary unit (True); materiality depends not only on amount but also on size of business, nature of information and decision-maker's level; goods withdrawn by proprietor are credited to Purchases, not Capital.
- Practise distinguish-between pairs: Going Concern vs Cost concept, Money Measurement vs Matching, and Fundamental Accounting Assumptions (assumed, only three) vs Accounting Policies (chosen methods, disclosed).
- Conservatism = provide for all possible losses, anticipate no profit ('cost or market price whichever is lower'); nuance - provision for discount on creditors (an anticipated gain) is NOT made, in keeping with conservatism.

TQ 1.8 · PYQ 2023-Jun [1] (a) (i) {C} · True/False · 2M · Pg 13	LEVEL I Understanding	Easy
TQ 1.9 · PYQ 2023-Jun [1] (b) {C} · Descriptive · 2M · Pg 14	LEVEL I Understanding	Easy
TQ 1.11 · PYQ 2023-Dec [1] (a) (i) {C} · True/False · 2M · Pg 14 asked 8×	LEVEL I Understanding	Easy
TQ 1.12 · PYQ 2023-Dec [1] (b) {C} · Descriptive · 2M · Pg 15 asked 4×	LEVEL I Understanding	Easy
TQ 1.14 · PYQ 2024-Jun [1] (b) (ii) (1) {C} · Descriptive · 1M · Pg 17	LEVEL I Understanding	Easy
TQ 1.15 · PYQ 2024-Jun [1] (b) (ii) (2) {C} · Descriptive · 1M · Pg 17 asked 3×	LEVEL I Understanding	Easy

TQ 1.16 · RTP 2024-Sep [1] (a) · True/False · --- · Pg 18 asked 7×	LEVEL I Understanding	Easy
TQ 1.21 · PYQ 2025-Jan [1] (a) (i) {C} · True/False · 2M · Pg 20	LEVEL I Understanding	Easy
TQ 1.1 · PYQ 2019-Jun [1] (b) · Distinguish Between · 4M · Pg 10 asked 4×	LEVEL I Understanding	Medium
TQ 1.2 · PYQ 2020-Nov [1] (a) (vi) {C} · True/False · 2M · Pg 11	LEVEL I Understanding	Medium
TQ 1.3 · MTP 2021-Oct [1] (a) (i) {C} · True/False · 2M · Pg 11 asked 3×	LEVEL I Understanding	Medium
TQ 1.4 · PYQ 2021-Dec [1] (c) (i) {C} · Descriptive · 4M · Pg 12	LEVEL I Understanding	Medium
TQ 1.5 · PYQ 2022-May [1] (b) (ii) {C} · Descriptive · 4M · Pg 12 asked 3×	LEVEL I Understanding	Medium
TQ 1.6 · PYQ 2022-Nov [1] (a) {C} · True/False · 4M · Pg 12	LEVEL I Understanding	Medium
TQ 1.7 · MTP 2023-Apr [1] (a) (i) {C} · True/False · 2M · Pg 13	LEVEL I Understanding	Medium
TQ 1.10 · RTP 2023-Dec [1] (i) · True/False · --- · Pg 14	LEVEL I Understanding	Medium
TQ 1.17 · RTP 2024-Sep [1] (g) · True/False · --- · Pg 18 asked 2×	LEVEL I Understanding	Medium
TQ 1.18 · RTP 2024-Sep [2] · Descriptive · --- · Pg 18 asked 9×	LEVEL I Understanding	Medium
TQ 1.20 · MTP 2024-Dec S1 [1] (b) {C} · Distinguish Between · 4M · Pg 19 asked 6×	LEVEL I Understanding	Medium
TQ 1.22 · RTP 2025-Jan [2] (a) · Distinguish Between · --- · Pg 20 asked 2×	LEVEL I Understanding	Medium
TQ 1.23 · PYQ 2025-May [1] (a) (ii) {C} · True/False · 2M · Pg 21	LEVEL I Understanding	Medium
TQ 1.24 · PYQ 2025-Sep [1] (a) {C} · True/False · 6M · Pg 21	LEVEL I Understanding	Medium
TQ 1.25 · PYQ 2026-Sep [1] (b) {C} · Descriptive · 4M · Pg 22	LEVEL I Understanding	Medium

Unit 1.3: Capital and Revenue Expenditure and Receipts

P1-C1-U1.3 · Importance C · Rank 2 in chapter · Category A · 30.6% of chapter questions · 22 questions

Topic 1: Introduction

P1-C1-U1.3-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §3.1: why transactions must be analysed as capital or revenue before ascertaining periodical business results.

NOTES

Distinction: Revenue Expense relates to operations/revenue of the accounting period or items whose benefit does not extend beyond that period; Capital Expenditure generates enduring benefits and helps revenue generation over more than one accounting period — expenditure can be capitalised only when traceable directly to definable streams of future benefits.

Placement: revenue expenditures go to the P&L A/c of the year of spending, capital expenditures go to the asset side of the Balance Sheet and are transferred to P&L on the basis of utilisation of benefit in each year — so both ultimately reach P&L, the TIME factor being the main determinant; expenses are recognised through the matching principle (when and how much to charge against revenue).

Caution: the distinction creates considerable difficulty — in many cases the borderline between capital and revenue is very thin.

Topic 2: Considerations in Determining Capital and Revenue Expenditures

P1-C1-U1.3-T02

Read first Study Para 3.2 - the five basic considerations for distinguishing capital from revenue expenditure: nature of business, recurring nature, purpose of expense, effect on revenue-generating capacity, and materiality of amount.

NOTES

Five basic considerations (Para 3.2): (a) Nature of business – furniture is revenue expenditure for a furniture dealer but capital expenditure (asset) for any other trade; (b) Recurring nature – frequent expenses (monthly salary, rent) are revenue; infrequent, non-recurring outlays (purchase of assets) are capital unless immaterial; (c) Purpose of expense – normal maintenance/repairs are revenue, but major repairs increasing productive capacity are capital; (d) Effect on revenue-generating capacity – benefit confined to the current period = revenue; expenditure helping to generate revenue over more than one accounting period = capital; (e) Materiality of the amount involved – relative proportion of the amount is the final filter.

Improvement-vs-repair rule: expenditure on improvement/repair of a fixed asset is charged to P&L if expected future benefits do NOT change, but is added to the book value of the asset where expected future benefits increase.

Understanding explain with reasons · 1 question

- Explain each consideration with an example: nature of business (furniture is revenue expenditure for a furniture dealer but capital for others); recurring vs non-recurring (monthly rent vs purchase of an asset).
- Purpose of expense: normal maintenance/repairs are revenue, but major repairs increasing productive capacity are capital.
- Effect on revenue-generating capacity: benefit confined to the current period = revenue; benefit over more than one accounting period = capital; materiality of the amount involved is the final filter.

TQ 2.1 · PYQ 2021-Jul [1] (b) · Distinguish Between · 4M · Pg 26 **asked**
5x**LEVEL I**
Understanding**Medium****Topic 3: Capital Expenditures and Revenue Expenditures**

P1-C1-U1.3-T03

Read first Study Para 3.3 (key differences table) and especially Illustrations 1, 2, 6 and 8 - the classic True/False items on huts, overhauls, renovations, licenses, replacements and demolition are lifted straight from them.

NOTES

Core distinction (Para 3.3): capital expenditure contributes to revenue-earning capacity over more than one accounting period (enduring benefit, shown as asset in Balance Sheet, reaches P&L as benefit is utilised); revenue expenditure generates revenue of the current period only and is charged to P&L in the year of spending – time factor is the main determinant.

Capital expenditure	Revenue expenditure
Benefit over a long-term period	Benefit during the current period only
Increases capacity of business or reduces its costs	Maintains the earning capacity of the business
Examples: purchase of machine, car, furniture	Examples: repairs and maintenance, salary of staff

Standard CAPITAL verdicts (Illus. 1, 2, 6, 8): temporary huts necessary for constructing the cinema house (part of construction cost); overhaul of second-hand machinery (puts it in working condition – enduring advantage); first-time repairs/white-washing of an old building purchased; license to run a cinema/start a factory (right to carry on business, pre-operative, amortised); money spent to reduce working expenses (long-term benefit); rings and pistons changed for fuel efficiency (improvement – raises earning capacity by cost reduction); demolition of old building to construct

a bigger building on the same site; renovation increasing restaurant cabins from 10 to 13 (raises future revenue capacity); wages/transportation for erection of machinery (added to machinery cost); legal fee to acquire property; directors' travelling abroad for purchase of capital assets.

Standard REVENUE verdicts: replacement of a worn-out part of a machine (maintenance cost); inauguration expenses of a new unit in an existing business (no enduring benefit); lawyer's fee to defend a suit claiming the firm's factory site (maintenance of the asset – no added benefit or capacity); legal expenses to recover instalments from customers (normal recurring expense); removal of inventory to a new site; fine for contravening rules; compensation to workers under voluntary retirement.

Answer anchor: in every 'state with reasons' answer tie the verdict to enduring benefit / increase in earning capacity (capital) versus maintaining existing capacity for the current period (revenue); renewal fee paid for next year = prepaid (revenue of next year); deposit with MTNL for telephone = asset, not expenditure.

Understanding explain with reasons · 11 questions

- Memorise the standard verdicts with reasons - Capital: temporary huts needed for constructing a cinema house; overhaul of second-hand machinery; first-time repairs of an old building; license to run a cinema/factory; wages for erection of machinery (added to machinery, not P&L); money spent to reduce working expenses (long-term benefit); demolition of an old building to construct a new factory on the site; renovation increasing cabins from 15 to 18.
- Memorise the standard Revenue items: replacement of a worn-out part of a machine (maintenance); inauguration expenses of a new unit in an existing business; lawyer's fee to defend a title suit; legal expenses to recover instalments from customers.
- In every 'State with reasons' answer, anchor the reason in enduring benefit / increase in earning capacity (capital) versus maintaining existing capacity for the current period (revenue).

TQ 3.8 · MTP 2024-Aug [1] (a) (i) {C} · True/False · 2M · Pg 30	asked 3×	LEVEL I Understanding	Easy
TQ 3.1 · PYQ 2019-Jun [1] (a) (i) · True/False · 2M · Pg 27	asked 6×	LEVEL I Understanding	Medium
TQ 3.2 · PYQ 2019-Nov [1] (a) (ii) {C} · True/False · 2M · Pg 28	asked 4×	LEVEL I Understanding	Medium
TQ 3.3 · PYQ 2021-Dec [1] (a) {C} · True/False · 4M · Pg 28		LEVEL I Understanding	Medium
TQ 3.4 · PYQ 2022-May [1] (a) (iv) {C} · True/False · 2M · Pg 29		LEVEL I Understanding	Medium
TQ 3.6 · PYQ 2023-Jun [1] (a) (ii) {C} · True/False · 2M · Pg 30	asked 4×	LEVEL I Understanding	Medium
TQ 3.7 · PYQ 2023-Dec [1] (a) (v) {C} · True/False · 2M · Pg 30		LEVEL I Understanding	Medium
TQ 3.9 · PYQ 2024-Sep [1] (a) (ii) {C} · True/False · 2M · Pg 31	asked 3×	LEVEL I	Medium

	Understanding	
TQ 3.10 · MTP 2025-Jan S2 [1] (a) (iii) {C} · True/False · 2M · Pg 31 asked 2×	LEVEL I Understanding	Medium
TQ 3.12 · PYQ 2026-Jan [1] (a) (i) {C} · True/False · 2M · Pg 34	LEVEL I Understanding	Medium
TQ 3.13 · PYQ 2026-May [1] (a) (iii) {C} · True/False · 2M · Pg 34	LEVEL I Understanding	Medium

Application practise the procedure · 2 questions

- Practise 5-6 item classification lists: engine replaced by CNG kit, directors' foreign travel to buy capital assets, extension of railway tracks in factory area, rings and pistons changed for fuel efficiency, removal of inventory to a new site.
- Write a one-line reason per item; for borderline items apply the tests of Para 3.2 (purpose, enduring benefit, capacity enhancement vs maintenance).

TQ 3.5 · MTP 2022-Nov S1 [6] (c) · Descriptive · 5M · Pg 29 asked 2×	LEVEL II Application	Medium
TQ 3.11 · RTP 2026-Jan [3] (b) · Descriptive · ---- · Pg 31 asked 17×	LEVEL II Application	Medium

Topic 4: Capital Receipts and Revenue Receipts

P1-C1-U1.3-T04

Read first Study Para 3.4: revenue receipts arise from normal business activities and are credited to P&L; capital receipts (sale of fixed assets/investments, loans, owners' contributions) are not directly credited to P&L - only the profit/loss element goes to P&L. Illustrations 4 and 7 give the exam examples.

NOTES

Rule (Para 3.4): receipts obtained in the course of normal business activities are revenue receipts (sale of goods or services, interest income) – recognised on accrual as soon as the right of receipt is established, NOT equal to actual cash received, and credited to P&L; receipts not revenue in nature are capital receipts (sale of fixed assets or investments, secured/unsecured loans, owners' contributions) – taken to the Balance Sheet, not directly credited to P&L.

Profit element only to P&L: fixed asset costing ₹90,000 sold for ₹92,000 – the ₹92,000 is a capital receipt, but the profit of ₹2,000 (proceeds – book value) is computed and credited to P&L; similarly machine with book value ₹10 lakh sold for ₹12 lakh gives ₹2 lakh profit.

Classification verdicts (Illus. 4, 7 & MCQs): Capital – share premium, insurance claim for machinery damaged/destroyed by fire, maturity proceeds of a fixed deposit (recovery of deposit), medium-term loan from IDBI even if for working capital, entrance/life membership fee (non-recurring); Revenue – cash sales, amounts received from trade receivables (realisation of an

existing asset), interest on investments/fixed deposit, government subsidy for working capital.

Presentation: capital receipts go to the Balance Sheet; revenue receipts to the credit of P&L; a Receipts and Payments Account records BOTH capital and revenue items.

Understanding explain with reasons · 7 questions

- True/False verdicts to master: life membership fee is a CAPITAL receipt (non- recurring); insurance claim for machinery fully destroyed by fire is a capital receipt; subsidy from government for working capital is a REVENUE receipt; sale of office furniture is a capital receipt - only profit on sale (proceeds minus book value) is credited to P&L, not the whole amount.
- Gain on sale of a capital asset IS credited to P&L when computing net profit (e.g. asset costing ₹90,000 sold for ₹92,000 gives ₹2,000 profit to P&L), even though the ₹92,000 receipt itself is capital.
- Definition question: revenue receipts arise in the course of normal business (sale of goods/services, interest income), are recognised on accrual - not equal to cash received - and are credited to P&L; note that a Receipts and Payments Account records BOTH capital and revenue items (True).

TQ 4.1 · PYQ 2018-Nov [1] (a) (iii) {C} · True/False · 2M · Pg 35	asked 2×	LEVEL I Understanding	Easy
TQ 4.2 · PYQ 2020-Nov [1] (a) (iii) {C} · True/False · 2M · Pg 35	asked 2×	LEVEL I Understanding	Easy
TQ 4.5 · PYQ 2022-Nov [1] (a) (v) {C} · True/False · 2M · Pg 36		LEVEL I Understanding	Easy
TQ 4.3 · PYQ 2021-Jan [1] (a) (ii) {C} · True/False · 2M · Pg 35	asked 4×	LEVEL I Understanding	Medium
TQ 4.4 · RTP 2022-May [1] (i) · True/False · --- · Pg 36		LEVEL I Understanding	Medium
TQ 4.6 · RTP 2022-Nov [2] (b) · Descriptive · --- · Pg 36	asked 3×	LEVEL I Understanding	Medium
TQ 4.7 · RTP 2025-Jan [1] (ii) · True/False · --- · Pg 37	asked 2×	LEVEL I Understanding	Medium

Application practise the procedure · 1 question

- Practise classifying mixed lists: share premium (capital), amounts received from debtors (revenue - realisation of an existing asset), insurance claim on damaged machinery (capital), maturity of fixed deposit (capital) vs interest thereon (revenue).
- State the treatment along with the label: capital receipts go to the Balance Sheet; revenue receipts to the credit of P&L.

TQ 4.8 · RTP 2025-Jan [3] (b) · Descriptive · --- · Pg 37

asked 5×

LEVEL II
Application

Medium

Unit 1.4: Contingent Assets and Contingent Liabilities

P1-C1-U1.4 · Importance D · Rank 4 in chapter · Category C · 8.3% of chapter questions · 6 questions

Topic 1: Contingent Asset

P1-C1-U1.4-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §4.1: definition of contingent asset, non-recognition under prudence, and its disclosure treatment.

NOTES

Definition: a contingent asset is a possible asset that arises from past events and whose existence will be confirmed only after occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise — usually from unplanned/unexpected events giving possibility of an inflow of economic benefits; e.g. a claim the enterprise is pursuing through legal process with uncertain outcome.

Treatment: per prudence and present accounting standards an enterprise should NOT recognise a contingent asset (recognition may result in income that may never be realised) and it need NOT be disclosed in the financial statements — it is usually disclosed in the report of the approving authority (Board of Directors for a company) if an inflow of economic benefits is probable.

Continual assessment: contingent assets are assessed continually — when inflow becomes virtually certain it ceases to be contingent, and the asset and related income are recognised in the financial statements of the period in which the change occurs.

Topic 2: Contingent Liabilities

P1-C1-U1.4-T02

Read first Study Paras 4.1 and 4.2 - the two-limb definition of contingent liability, the definition of contingent asset, and their treatment (not recognised; contingent liability disclosed in notes to accounts, contingent asset disclosed in the report of the approving authority when inflow is probable).

NOTES

Contingent liability (SM, two limbs): “(a) a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or (b) a present obligation that arises from past events but is not recognised because (i) it is not probable that an outflow of

resources embodying economic benefits will be required to settle the obligation, or (ii) a reliable estimate of the amount of the obligation cannot be made.”

Contingent asset (SM): “a possible asset that arises from past events and whose existence will be confirmed only after occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise” – arises from unplanned/unexpected events giving the possibility of an inflow of economic benefits; e.g. a claim the enterprise is pursuing through legal process with uncertain outcome is a contingent ASSET (not a contingent liability – a claim against the enterprise would be the liability).

Treatment: contingent liability is never recognised in the balance sheet but is disclosed in the notes to accounts unless the possibility of outflow is remote; assessed continually – if outflow becomes probable, a provision is recognised in the period the change in probability occurs (except where no reliable estimate can be made); examples – claims not acknowledged as debts, guarantees for third parties, bills discounted, statutory liabilities under dispute.

Contingent asset treatment (prudence): never recognised – recognition could bring in income that may never be realised; need not be disclosed in the financial statements but is usually disclosed in the report of the approving authority (Board of Directors for a company) if inflow is probable; assessed continually and recognised with related income only when realisation becomes virtually certain (it then ceases to be contingent).

Remembering memorise · 1 question

- Definition: a contingent liability is (a) a possible obligation from past events confirmed only by uncertain future events not wholly within the enterprise's control, OR (b) a present obligation not recognised because outflow is not probable or the amount cannot be reliably estimated.
- Contingent asset: a possible asset arising from past events whose existence is confirmed by uncertain future events - never recognised (prudence); disclosed in the approving authority's (Board's) report if inflow is probable; recognised only when realisation becomes virtually certain.
- Treatment: contingent liability is disclosed in notes unless the possibility of outflow is remote; if outflow later becomes probable, a provision is recognised in that period; examples - claims not acknowledged as debts, guarantees, bills discounted, disputed statutory liabilities.

TQ 2.2 · PYQ 2021-Dec [1] (c) · Short Note · 2M · Pg 43 **asked 3x**

LEVEL I
Remembering

Easy

Understanding explain with reasons · 1 question

- True/False trap: a claim the enterprise is PURSUING through legal process with uncertain outcome is a contingent ASSET, not a contingent liability (a claim against the enterprise would be the liability).
- Explain why prudence forbids recognising contingent assets - it could recognise income that may never be realised.

TQ 2.1 · PYQ 2022-May [1] (a) (i) {C} · True/False · 2M · Pg 42 asked 3×

LEVEL I
Understanding

Medium

Topic 3: Distinction Between Contingent Liabilities and Liabilities

P1-C1-U1.4-T03

Read first Study Para 4.3 - a liability is a present financial obligation arising from past events whose settlement causes an outflow of resources; contrast this with the contingent liability definition.

NOTES

Two-line difference (Para 4.3): a liability is the present financial obligation of an enterprise arising from past events whose settlement results in an outflow of resources embodying economic benefits; in a contingent liability, either the outflow of resources to settle is not probable OR the amount cannot be measured with sufficient reliability – the distinction rests on management's judgement.

Liability	Contingent liability
Present financial obligation from past events	Possible obligation, or present one failing recognition tests
Settlement will cause outflow of economic benefits	Outflow not probable or amount not reliably measurable
Recognised in the balance sheet	Only disclosed by way of notes to the balance sheet

Examples of contingent liabilities: claims against the enterprise not acknowledged as debts, guarantees given in respect of third parties, liability in respect of bills discounted, statutory liabilities under dispute.

Understanding explain with reasons · 1 question

- State the difference in two lines: liability = present obligation from past events, settlement will cause outflow of economic benefits; contingent liability = either outflow is not probable or the amount cannot be measured with sufficient reliability.
- Add presentation: liabilities are recognised in the balance sheet; contingent liabilities are only disclosed by way of notes.
- Support with examples of contingent liabilities: claims not acknowledged as debts, third-party guarantees, bills discounted, statutory liabilities under dispute.

TQ 3.1 · PYQ 2025-May [1] (b) (ii) {C} · Distinguish Between · 2M · Pg

LEVEL I
Understanding

Easy

43 asked 3×

Topic 4: Distinction Between Contingent Liabilities and Provisions

P1-C1-U1.4-T04

Read first Study Para 4.4 - the definition of provision and the four-point table distinguishing provisions from contingent liabilities, with the Central Excise penalty (Alpha Ltd.) example.

NOTES

Provision (SM): “any amount written off or retained by way of providing for depreciation, renewal or diminution in the value of assets or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy”.

Provision	Contingent liability
Present liability of uncertain amount, measurable reliably by substantial estimation	Possible obligation that may or may not crystallise on uncertain future events
Meets the recognition criteria	Fails to meet the recognition criteria
Recognised when present obligation exists, outflow probable and reliable estimate possible	Includes present obligations where outflow not probable or amount not reliably estimable
Outflow probable – recognise provision in balance sheet	Outflow less likely – disclose as contingent liability

Alpha Ltd. example: Central Excise Officer imposes a penalty, company appeals – if management estimates payment is probable it recognises a provision; if it anticipates a favourable appellate judgement (payment less likely) it discloses a contingent liability instead.

True/False trap: 'a present financial obligation of uncertain amount measurable by substantial estimation is a liability' – FALSE, that is the definition of a PROVISION; 'when payment of the obligation is probable, it gives rise to a contingent liability' – FALSE, that gives rise to a provision.

Sorting rule of thumb: known liability whose amount is estimable = provision (provision for doubtful debts, depreciation, taxation) – these are charges against profit; appropriations of profit (proposed dividend, retained profit) are reserves/appropriations, not provisions; determinable obligations (e.g. liability for income tax assessed) are liabilities proper.

Understanding explain with reasons · 2 questions

- Four-point distinction: provision is a present liability of uncertain amount measurable reliably by substantial estimation and meets recognition criteria; contingent liability is a possible obligation that may or may not crystallise and fails the recognition criteria.

- Recognition logic: outflow probable + reliable estimate = recognise a provision in the balance sheet; outflow less likely or not reliably estimable = disclose as contingent liability.
- True/False trap: 'a present financial obligation of uncertain amount measurable by substantial estimation is a liability' - FALSE, that is the definition of a PROVISION (a liability proper is of determinable obligation).

TQ 4.1 · PYQ 2022-Nov [1] (b) {C} · Distinguish Between · 4M · Pg 44
asked 5×

LEVEL I
Understanding

Medium

TQ 4.2 · PYQ 2026-Jan [1] (a) (iii) {C} · True/False · 2M · Pg 45

LEVEL I
Understanding

Medium

Application practise the procedure · 1 question

- Practise sorting a given list of P&L/appropriation items (liability for income tax, retained profit, proposed dividend, provision for doubtful debts, depreciation etc.) into provisions, liabilities and reserves/appropriations with reasons.
- Rule of thumb for such questions: known liability with amount estimable = provision; charge against profit (depreciation, doubtful debts, tax) vs appropriation of profit (proposed dividend, retained profit).

PQ 4.1 · PYQ 2021-Jul [5] (b) (ii) · Practical · 5M · Pg 46 asked 2×

LEVEL II
Application

Medium

Unit 1.5: Accounting Policies

P1-C1-U1.5 · Importance D · Rank 5 in chapter · Category C · 6.9% of chapter questions · 5 questions

Topic 1: Meaning of Accounting Policies

P1-C1-U1.5-T01

Read first Study Para 5.1 - the definition of accounting policies and the illustrative areas where different policies are encountered (valuation of inventories, valuation of investments), plus Para 5.2 on selection of policies.

NOTES

Definition (Para 5.1): "Accounting Policies refer to specific accounting principles and methods of applying these principles adopted by the enterprise in the preparation and presentation of financial statements" – they rest on the accounting concepts, principles and conventions of Unit 2.

No universal list: enterprises operate in diverse and complex situations, so the choice of policy appropriate to the circumstances calls for considerate judgement by management; frequently-encountered areas – valuation of inventories, valuation of investments (illustrative, not exhaustive); e.g. choosing FIFO or weighted average for valuing shares/inventory IS an accounting

policy; ICAI reduces acceptable alternatives via Guidance Notes and Accounting Standards.

Selection (Para 5.2): three major characteristics guide selection and application – Prudence, Substance over form, Materiality; the chosen policies must exhibit a true and fair view of the Balance Sheet and P&L; inappropriate selection may understate OR overstate performance and position; disclosure of the treatment adopted is necessary in any case, but disclosure CANNOT rectify a wrong or inappropriate treatment.

Understanding explain with reasons · 1 question

- Definition to explain: accounting policies are the specific accounting principles AND the methods of applying those principles adopted by an enterprise in preparing and presenting financial statements.
- Explain that there is no single universal list of policies - enterprises operate in diverse circumstances, so management must exercise judgement (e.g. FIFO vs weighted average for inventory/investment valuation is a policy choice).
- Know the three major characteristics guiding selection - Prudence, Substance over form, Materiality - and that the chosen policies must give a true and fair view; disclosure cannot rectify a wrong treatment.

TQ 1.1 · PYQ 2005-Nov [3] (b) · Descriptive · 3M · Pg 50 **asked 2x**

LEVEL 1
Understanding

Easy

Topic 2: Selection of Accounting Policies

P1-C1-U1.5-T02

Read first Read §5.2: the three characteristics governing choice of accounting policies and the SM's examples of policy selection.

NOTES

Importance: choice of accounting policy affects performance measurement and financial position — an inappropriate policy may lead to understatement or overstatement of both, so policies must be selected with due care considering the effect from the angle of various users of accounts; no unified and exhaustive list of accounting policies of universal application can be suggested.

Three major characteristics: Prudence, Substance over form, and Materiality — the financial statements should be prepared on accounting policies which exhibit a true and fair view of the state of affairs of the Balance Sheet and P&L A/c.

Examples and caveat: inventories valued at cost except finished goods (lower of cost or market value) and by-products (net realisable value); long-term investments at acquisition cost with provision for permanent diminution — disclosure of the treatment adopted is necessary in any case, but disclosure cannot rectify a wrong or inappropriate treatment.

Understanding explain with reasons · 1 question

TQ 2.1 · PYQ 2026-Sep [1] (a) (i) · True/False · 2M · Pg 51

LEVEL 1
Understanding**Easy**

Topic 3: Change in Accounting Policies

P1-C1-U1.5-T03

Read first Study Para 5.3 - the two conditions permitting a change in accounting policy and the requirement to quantify the material effect of a change, with the inventory cost-formula and Omega Enterprises examples.

NOTES

Two conditions for change (Para 5.3): (a) it is required by some statute or for compliance with an Accounting Standard, (b) the change would result in a more appropriate presentation of the financial statements.

Material effect must be quantified: a change can materially affect statement items – e.g. changing the inventory cost formula from weighted average to FIFO, capitalising interest not capitalised earlier, or charging proportionate interest to inventory can increase/decrease net profit; unless the effect is quantified (on assets, liabilities, profit/loss) the statements will not help users; Omega Enterprises example – revised inventory valuation policy to include applicable production overheads for a more appropriate presentation.

4-mark answer skeleton: definition of accounting policies + three selection characteristics (prudence, substance over form, materiality) + the two conditions permitting a change.

Understanding explain with reasons · 3 questions

- The two (exam-standard) conditions for change: (a) required by statute or for compliance with an Accounting Standard, (b) the change would result in a more appropriate presentation of the financial statements.
- Explain with an example that a change can materially affect financial statement items: switching inventory valuation from weighted average to FIFO, or starting to capitalise interest, can increase/decrease profit - hence the effect must be quantified and disclosed, otherwise statements will not help users.
- For the combined 4-mark question, structure the answer as: definition of accounting policies + three selection characteristics (prudence, substance over form, materiality) + the two conditions for change.

TQ 3.1 · PYQ 2024-Jun [1] (b) (i) {C} · Descriptive · 2M · Pg 52

LEVEL 1
Understanding**Easy**

TQ 3.2 · RTP 2025-Jan [2] (b) · Descriptive · --- · Pg 52

LEVEL 1
Understanding**Medium**

TQ 3.3 · PYQ 2026-May [1] (b) {C} · Descriptive · 4M · Pg 52

LEVEL I
Understanding

Medium

Unit 1.6: Accounting as a Measurement Discipline

P1-C1-U1.6 · Importance D · Rank 7 in chapter · Category C · 1.4% of chapter questions · 1 questions

Topic 1: Meaning of Measurement

P1-C1-U1.6-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation**Read first** Read §6.1: Chambers' and Kohler's definitions of measurement and the three basic elements.

NOTES

Definition: Prof. R. J. Chambers defined measurement as “assignment of numbers to objects and events according to rules specifying the property to be measured, the scale to be used and the dimension of the unit”; Kohler defined it as assignment of a system of ordinal (position — first, second) or cardinal (how many — one, two) numbers to the results of a scheme of inquiry in accordance with logical or mathematical rules.

Three elements: (1) identification of objects and events to be measured; (2) selection of standard or scale to be used; (3) evaluation of dimension of measurement standard or scale — Chambers' definition is widely used to judge how far accounting is a measurement discipline.

Topic 2: Objects or Events to be Measured

P1-C1-U1.6-T02

CONCEPT BASE — no exam question asked yet · essential for full preparation**Read first** Read §6.2: what accounting measures and why prediction of future events is not measurement.

NOTES

Information as object: accounting essentially includes measurement of “information” — decision-makers need past, present and future information (external users are generally given past information), and there is no uniform set of events/transactions required for decision-making (e.g.

cash management needs receipts/expenses data, lending needs debt-servicing ability).

Limit: past and present objects and events can be measured with some degree of accuracy, but future events are only PREDICTED, not measured — prediction is nevertheless an essential part of accounting information.

Topic 3: Standard or Scale of Measurement

P1-C1-U1.6-T03

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.3: money as the scale of measurement and its lack of universal denomination.

NOTES

Money as scale: in accounting, money is the scale of measurement (money measurement concept), though quantitative information is also communicated as supplement; money has no universal denomination — it takes the shape of the ruling currency (₹ in India, Pound-Sterling in U.K., Dollar in U.S.A.) with no constant exchange relationship among currencies.

Volatility: a \$5,000 loan recorded at ₹2,50,000 (\$1 = ₹50) becomes ₹2,75,000 when the rate changes to ₹55 — money lacks universal applicability across country boundaries and, with fluctuating exchange rates, is a volatile measurement scale.

Topic 4: Dimension of Measurement Discipline

P1-C1-U1.6-T04

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.4 with the two-year production/sales example: instability of money in dimension.

NOTES

Instability: an ideal scale is stable over time (1 kg or 1 metre never changes), but money is not — continuous price changes mean the same money may not buy the same goods at different dates, so money-measured information of one year may not be comparable with another.

Illustration: sales rose from ₹5,00,000 (5,000 pcs) to ₹5,40,000 (4,500 pcs) — an apparent 8% sales growth actually hides a 10% decline in production/sales and a 10% fall in gross profit (₹1,00,000 down to ₹90,000); the growth in monetary figures is only due to price change — hence accounting

is not an exact measurement discipline.

Topic 5: Accounting as a Measurement Discipline

P1-C1-U1.6-T05

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.5: measurement as part of accounting and the governing fundamental assumptions.

NOTES

Measurement in accounting: unless the measurement base is settled the record-keeping function cannot progress — by recording, classifying and summarising, accounting measures performance (profit/loss) and financial position; the measurement sub-system is governed by theorems, three of which — going concern, consistency and accrual — are the fundamental accounting assumptions taken for granted.

Not purely measurement: recording, classifying, summarising and communication of information do not fall within the purview of measurement discipline, so accounting cannot simply be called a measurement discipline; all transactions are recorded in money terms, quantitative information being only supplementary.

Topic 6: Valuation Principles

P1-C1-U1.6-T06

Read first Study Para 6.6 - the four generally accepted measurement bases (Historical Cost, Current Cost, Realisable Value, Present Value) with the Mr. X machine/bank-loan example, and Para 6.1 for the meaning and three elements of measurement.

NOTES

Measurement (Chambers, Para 6.1): “assignment of numbers to objects and events according to rules specifying the property to be measured, the scale to be used and the dimension of the unit”; **three elements:** (1) identification of objects and events to be measured, (2) selection of standard or scale to be used, (3) evaluation of dimension of the measurement standard or scale; in accounting money is the scale, but it lacks universal applicability and stability of dimension, so accounting is not an exact measurement discipline.

Four measurement bases (Para 6.6): (i) Historical Cost – acquisition price: assets at cash/cash equivalent paid at acquisition (machine ₹7,00,000 + installation ₹1,00,000 = ₹8,00,000), liabilities

at proceeds received in exchange for the obligation (bank loan recorded at ₹5,00,000 received) or, e.g. income tax, at the amount expected to be paid to discharge it; (ii) Current Cost – assets at the cash that would have to be paid if the same or an equivalent asset were acquired currently, liabilities at the UNDISCOUNTED amount needed to settle the obligation currently (machine ₹25,00,000; loan with 1% prepayment penalty ₹5,05,000); (iii) Realisable Value – assets at cash currently obtainable by selling in an ORDERLY disposal (machine ₹20,00,000), liabilities at settlement values, the undiscounted cash expected to be paid in the normal course (loan ₹5,00,000); (iv) Present Value – assets at the present discounted value of future net cash inflows expected in the normal course ($₹1,00,000 \text{ p.a.} \times 10 \text{ yrs @ } 20\% = ₹4,19,246$), liabilities at the present discounted value of future net cash outflows to settle (loan ₹4,70,094).

Formulae: discounting: $P = A \div (1 + i)^n$ (time value of money – future money is devalued to today's rupees); annuity: $PV = (A \div i) \times [1 - 1 \div (1 + i)^n]$.

True/False & links to practice: 'Current cost gives an alternative measurement base' – TRUE; 'Future value' is NOT one of the four bases; historical cost is used for long-term assets (machinery, furniture, licenses) and the traditional system is historical cost accounting; realisable value is applied to inventories (lower of cost and net realisable value); present value is common for investments and loans; Mohan MCQ set – machine bought 2001 at ₹10,00,000 (historical), similar machine now ₹20,00,000 (current cost), sale estimate ₹15,00,000 (realisable), discounted inflows ₹12,00,000 (present value).

Understanding explain with reasons · 1 question

- True/False: 'Current cost gives an alternative measurement base' is TRUE - assets are carried at the cash that would have to be paid if the same or equivalent asset were acquired currently; liabilities at the undiscounted amount needed to settle currently.
- Explain each base for both assets and liabilities: historical cost = acquisition price (cost paid plus installation, e.g. $₹7,00,000 + ₹1,00,000 = ₹8,00,000$); realisable value = cash obtainable by selling in an orderly disposal / settlement value of liabilities; present value = discounted future net cash inflows/outflows.
- For the 'Define Measurement' part, quote Chambers - assignment of numbers to objects and events per rules specifying the property, scale and dimension - and list the three elements: identification of objects/events, selection of scale, evaluation of dimension of the scale.
- Link bases to practice: historical cost is used for long-term assets, realisable value for inventories (lower of cost and NRV), present value for investments and loans; the traditional system is historical cost accounting.

Topic 7: Measurement and Valuation

P1-C1-U1.6-T07

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.7: value as utility to the economist versus the monetary surrogate used in accounting.

NOTES

Value vs measurement: value relates to benefits derived from objects, abilities or ideas — to the economist it is the utility (satisfaction) of an economic resource; in accounting a monetary surrogate is used, i.e. value is measured in terms of money (a car bought for ₹2,50,000 is valued at acquisition/historical cost).

Scales: economists often use ordinal scales to indicate levels of satisfaction, but accountants use only cardinal scales — value is indicated by measurement, and in accounting value is always measured in terms of money.

Topic 8: Accounting Estimates

P1-C1-U1.6-T08

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.8 with its four examples: why estimates are needed and what a change in estimate means.

NOTES

Need: items which have not yet occurred cannot be measured by valuation principles yet must be recorded (e.g. provision for doubtful debts) — reasonable estimates based on existing situation and past experience are made; owing to uncertainties inherent in business, many financial statement items can only be estimated, involving judgement on the latest information available.

Areas: depreciation, amortisation and impairment losses, accruals, provisions, employee benefit obligations, bad debts, useful life and residual value of plant and machinery, inventory obsolescence, useful life of a patent, provisions on construction contracts, tax provisions.

Change in estimate: revision is required when circumstances change or from new information/more experience/subsequent developments — change in accounting estimate means a difference between parameters estimated earlier and re-estimated (or actual results) during the current period; e.g. a ₹10 lakh machine's expected life cut from 10 years to 6 on obsolescence —

such change is NOT given retrospective effect.

Unit 1.7: Accounting Standards

P1-C1-U1.7 · Importance D · Rank 6 in chapter · Category C · 6.9% of chapter questions · 5 questions

Topic 1: Introduction of Accounting Standards

P1-C1-U1.7-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §7.1: why accounting principles are standardised and the four issues Accounting Standards deal with.

NOTES

Why standards: if the financial accounting process is not properly regulated, financial statements can be misleading, tendentious and distorted — to ensure transparency, consistency, comparability, adequacy and reliability of financial reporting, accounting principles and policies are standardised so financial statements of different enterprises become comparable.

Definition: Accounting Standards are written policy documents issued by the expert accounting body or by the government or other regulatory body covering the aspects of recognition, measurement, presentation and disclosure of accounting transactions and events in the financial statements.

Four issues dealt with: (i) recognition of events and transactions, (ii) measurement of these transactions and events, (iii) presentation in a manner meaningful and understandable to the reader, (iv) disclosure requirements enabling stakeholders and potential investors to take prudent and informed business decisions.

Topic 2: Objectives of Accounting Standards

P1-C1-U1.7-T02

Read first Study Para 7.2 - accounting standards standardise diverse accounting policies to harmonise practices; also skim Para 7.1 for what standards are and the four issues they deal with (recognition, measurement, presentation, disclosure).

NOTES

Meaning (Para 7.1): accounting standards are written policy documents issued by the expert accounting body or by the government or other regulatory body covering the aspects of recognition, measurement, presentation and disclosure of accounting transactions and events in the financial statements – the four issues every standard deals with.

Objectives (Para 7.2): the whole idea centres on harmonisation of accounting policies and practices – standards standardise diverse accounting policies with a view to (i) eliminate the non-comparability of financial statements and thereby improve their reliability, and (ii) provide a set of standard accounting policies, valuation norms and disclosure requirements.

Effect: standards reduce the accounting alternatives in preparing financial statements within the bounds of rationality, thereby ensuring comparability of financial statements of different enterprises; standardisation ensures transparency, consistency, comparability, adequacy and reliability of financial reporting.

Remembering memorise · 1 question

- Objectives to state: standardise diverse accounting policies so as to (i) eliminate non-comparability of financial statements and improve their reliability, and (ii) provide a set of standard accounting policies, valuation norms and disclosure requirements.
- Add: standards reduce accounting alternatives within the bounds of rationality, ensuring comparability of financial statements of different enterprises.
- One-line meaning: accounting standards are written policy documents issued by the expert accounting body/government/regulator covering recognition, measurement, presentation and disclosure of transactions and events.

TQ 2.1 · PYQ 2025-May [1] (b) (i) {C} · Descriptive · 2M · Pg 62 asked 9x **LEVEL I**
Remembering

Easy

Topic 3: Benefits and Limitations of Accounting Standards

P1-C1-U1.7-T03

Read first Study Para 7.3 - the three benefits and two limitations of accounting standards, along with the definition of accounting standards from Para 7.1 for the combined 4-mark question.

NOTES

Three benefits (Para 7.3): (i) Standardisation of alternative accounting treatments – reduce to a reasonable extent or eliminate altogether confusing variations in treatments; (ii) Requirements for additional disclosures – standards may call for disclosure beyond that required by law; (iii) Comparability of financial statements – of different companies in the same country and, to a limited extent, of companies in different parts of the world (limited because institutions, traditions

and legal systems differ across countries).

Two limitations: (i) Difficulties in making choice between different treatments – alternative solutions to certain accounting problems may each have arguments to recommend them; (ii) Restricted scope – accounting standards cannot override the statute and must be framed within the ambit of prevailing statutes.

True/False: 'Accounting Standards can override the statute' – FALSE, they can never override the statute; 'difficulty in choosing between treatments is a benefit' – FALSE, it is a limitation; 'additional disclosure requirement is a limitation' – FALSE, it is a benefit.

4-mark structure: open with the definition (written policy documents on recognition, measurement, presentation, disclosure), then list the three benefits and two limitations.

Understanding explain with reasons · 3 questions

- Benefits (explain each): (i) standardisation of alternative accounting treatments - reduce/eliminate confusing variations; (ii) requirements for additional disclosures - beyond what law requires; (iii) comparability of financial statements across companies and, to a limited extent, across countries.
- Limitations: (i) difficulty in choosing between alternative treatments where each has merit; (ii) restricted scope - standards cannot override the statute and must be framed within prevailing laws.
- True/False: 'Accounting Standards can override the statute' is FALSE - they are required to be framed within the ambit of prevailing statutes.
- For the full 4-mark question, open with the definition (written policy documents on recognition, measurement, presentation, disclosure) before listing advantages and limitations.

TQ 3.2 · PYQ 2024-Jun [1] (a) (iii) {C} · True/False · 2M · Pg 64

LEVEL I
Understanding

Easy

TQ 3.1 · PYQ 2006-Nov [6] (v) · Descriptive · 5M · Pg 63 **asked 5x**

LEVEL I
Understanding

Medium

TQ 3.3 · PYQ 2026-Jan [1] (b) {C} · Descriptive · 4M · Pg 65

LEVEL I
Understanding

Medium

Topic 4: Process of Formulation of Accounting Standards in India

P1-C1-U1.7-T04

Read first Study Para 7.4 - ICAI constituted the Accounting Standards Board (ASB) in 1977; learn the standard-setting steps (area identification, study groups, draft circulation, exposure draft, comments, finalisation by the Council) and who issues which set of standards.

NOTES

ASB (Para 7.4): ICAI constituted the Accounting Standards Board in 1977; ASB considers IFRSs while framing Indian standards, integrating them in the light of applicable laws, customs, usages

and business environment; composition includes industry representatives (ASSOCHAM, CII, FICCI), regulators, academicians, government departments; ASB is independent – the Council of ICAI cannot modify a draft standard formulated by ASB without consulting the ASB.

Standard-setting steps: (1) identification of broad areas by ASB, (2) constitution of study groups to prepare preliminary drafts (objective, scope, definitions, recognition/measurement, presentation and disclosure), (3) consideration and revision of the draft by ASB, (4) circulation to Council members and specified outside bodies – DCA, SEBI, C&AG, CBDT, SCOPE etc., (5) meeting with those bodies to ascertain views, (6) finalisation and issue of the Exposure Draft inviting public comments, (7) consideration of comments and finalisation by ASB for submission to the Council, (8) Council considers, modifies if necessary in consultation with ASB, and the standard is issued.

Who issues which set: Ind AS – applicable to all listed companies and NBFCs, and to unlisted companies/NBFCs with net worth of ₹250 crores or more; AS notified under the Companies (Accounting Standards) Rules, 2021 (Central Government) – for companies other than Ind AS companies; AS prescribed by ICAI – for entities other than companies; True/False – 'Accounting Standards for non-corporate entities in India are issued by the Central Government' is FALSE, they are issued by the ICAI.

Ind AS background: India decided to CONVERGE with (not adopt) IFRS issued by the IASB – Ind AS are kept in line with corresponding IFRS with departures only where absolutely essential, considering the country's economic environment; ASB = Accounting Standards Board (not 'Accounting standardisation benchmarking').

Understanding explain with reasons · 1 question

- True/False: 'Accounting Standards for non-corporate entities in India are issued by the Central Government' is FALSE - standards for non-corporate entities are issued by the ICAI; the Central Government notifies AS for companies under the Companies (Accounting Standards) Rules, 2021.
- Know the three sets of standards and applicability: Ind AS for listed companies/NBFCs and unlisted companies with net worth of ₹250 crores or more; notified AS for other companies; ICAI-prescribed AS for non-company entities.
- Understand ASB's consultative process (drafts to DCA/SEBI/C&AG/CBDT etc., exposure draft for public comment) and that the ASB is independent - the ICAI Council cannot modify a draft standard without consulting the ASB.

TQ 4.1 · PYQ 2021-Jan [1] (a) (vi) {C} · True/False · 2M · Pg 66 asked 5×

LEVEL I
Understanding

Easy

Topic 5: List of Accounting Standards in India

P1-C1-U1.7-T05

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §7.5: the table of applicable AS issued by the Accounting Standards Board and the note on Ind AS convergence.

NOTES

Applicable AS: AS issued by the Accounting Standards Board must be complied with so that financial statements follow GAAP — currently AS 1 to AS 29 (with gaps), e.g. AS 1 Disclosure of Accounting Policies, AS 2 Valuation of Inventories, AS 3 Cash Flow Statements, AS 9 Revenue Recognition, AS 10 Property Plant and Equipment, AS 16 Borrowing Costs, AS 19 Leases, AS 22 Taxes on Income, AS 26 Intangible Assets, AS 29 Provisions, Contingent Liabilities & Contingent Assets (the detailed list is for knowledge only, not part of syllabus).

Ind AS: ICAI, the standard-setting body, initiated the move towards IFRS in 2006; the Government of India in consultation with ICAI decided to CONVERGE with and not adopt IFRS — Ind AS are kept in line with corresponding IFRS as far as possible, with departures only where absolutely essential considering India's economic environment.

CHAPTER 2

Accounting Process

38 Topics · 90 Classified Questions · Importance: A

ICAI SKILL PROFILE Level I 5–20% · Level II 80–95% — this chapter reads **theory-heavy**Level I — Remembering & Understanding **29.8%** 97 of 325.5 marksLevel II — Application & Analysis **70.2%** 228.5 of 325.5 marks

Unit 2.1: Basic Accounting Procedures: Journal Entries

P1-C2-U2.1 · Importance B · Rank 2 in chapter · Category A · 21.1% of chapter questions · 19 questions

Topic 1: Double Entry System

P1-C2-U2.1-T01

Read first Read Para 1.1 of the Study Material: meaning of the double entry system, its origin with Luca Pacioli, and the two-fold (debit-credit) aspect of every transaction.

NOTES

Meaning (SM): the system “which recognises and records both the aspects of transactions” — every transaction has two-fold aspects, debit and credit, so at least two accounts are affected; it is the only scientific system of accounting.

Origin: more than 500 years old; first described by “Luca Pacioli”, an Italian friar and mathematician, in Summa de Arithmetica, Geometria, Proportioni et Proportionalita — the first book describing a double entry accounting system.

Standard example: on purchase of furniture a new asset (furniture) is acquired AND either the cash balance is reduced or a liability to the supplier arises — both aspects are recorded; system useful for all entities requiring use of money.

Remembering memorise · 1 question

- Definition: the double entry system recognises and records BOTH aspects (debit and credit) of every transaction, so at least two accounts are affected.
- It is the only scientific system of accounting, over 500 years old; first described by Luca Pacioli, an Italian friar and mathematician, in 'Summa de Arithmetica'.

- Standard example for the short note: purchase of furniture --- new asset (furniture) comes in AND either cash reduces or a liability to the supplier arises.
- Be ready to write this as a 2.5-mark short note in 4-5 crisp points.

TQ 1.1 · MTP 2023-May [6] (c) (i) · Short Note · 2.5M · Pg 70 asked 5x

LEVEL I
Remembering

Easy

Topic 2: Advantages of Double Entry System

P1-C2-U2.1-T02

Read first Study Para 1.2 --- the five advantages of the double entry system; also contrast it with single entry (incomplete records) for True/False questions.

NOTES

Five advantages (Para 1.2): (i) accuracy of the accounting work can be established through the device of the trial balance; (ii) profit earned or loss incurred during a period ascertained together with details; (iii) financial position of the entity ascertained at the end of each period through preparation of financial statements; (iv) accounts can be kept in as much detail as necessary, giving significant information for control and reporting; (v) results of one year may be compared with previous years and reasons for change ascertained.

Each advantage flows from recording both aspects: debits always equal credits, so books can be arithmetically checked, and complete account-wise detail exists for results, position, control and comparison.

True/False trap: nominal accounts are NOT kept under single entry (incomplete records keep mainly cash and personal accounts); real and nominal accounts are maintained under the double entry system.

Remembering memorise · 1 question

- Memorise the 5 advantages: (i) accuracy checked via trial balance, (ii) profit/loss ascertained with details, (iii) financial position known through financial statements, (iv) detailed accounts aid control and reporting, (v) year-on-year comparison of results.
- A 5-mark descriptive answer needs all five points with one-line explanations.

TQ 2.1 · PYQ 2025-Jan [6] (b) · Descriptive · 5M · Pg 71

LEVEL I
Remembering

Medium

Understanding explain with reasons · 2 questions

- Trap (True/False): 'Nominal Accounts are kept under Single Entry System' is FALSE --- single entry keeps mainly cash and personal accounts; nominal and real accounts are maintained under double entry.
- Be able to reason WHY each advantage flows from recording both aspects of a transaction.

TQ 2.2 · PYQ 2026-Jan [1] (a) (iv) {C} · True/False · 2M · Pg 72 asked 2×

LEVEL I
Understanding

Easy

TQ 2.3 · PYQ 2026-Sep [6] (b) · Descriptive · 5M · Pg 72

LEVEL I
Understanding

Medium

Topic 3: Account

P1-C2-U2.1-T03

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.3: how the T-form account grows out of recording increases and decreases of cash in two columns.

NOTES

Why an account: altering the cash balance with every transaction is cumbersome — instead all increases are recorded in one column and all decreases in another; opening balance + total increases - total decreases = closing balance, giving significant information about the item.

T form: the two columns are put in the form of an account called the “T” form — increases of cash (an asset) on the LEFT side, decreases on the RIGHT; each entry carries a number or date since T-accounts show only amounts, not descriptions.

Proper form: ruled with Date · Particulars · Amount (₹) on both left and right sides; e.g. initial capital ₹25,00,000 increases Cash (left) and increases Capital (right); cash paid to creditors decreases Cash (right) and decreases Creditors (left).

Topic 4: Debit and Credit

P1-C2-U2.1-T04

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.4: Dr./Cr. as the formal names of the two sides, the expanded accounting equation, and the increase/decrease rules.

NOTES

Meaning: accountants use Debit (Dr.) to denote an entry on the LEFT side of any account and Credit (Cr.) to denote an entry on the RIGHT side — debit and credit do NOT mean favourable and unfavourable things; they merely describe the two sides of accounts.

Equation base: Assets = Liabilities + Stockholders' Equity, where equity = contributed capital +

beginning retained earnings + revenue - expenses - dividends; a change on one side of the equation is matched by a similar change on the other side or an opposite change on the same side.

Rules: increases in assets are debits, decreases credits; increases in liabilities are credits, decreases debits; increases in owner's capital are credits, decreases debits; increases in expenses/purchases are debits; increases in revenue/incomes/sales are credits.

Topic 5: Transactions

P1-C2-U2.1-T05

Read first Study Para 1.5 --- meaning of a transaction as a two-way, money- measurable event supported by source documents, and the two approaches (accounting equation and traditional) to analyse its dual aspect.

NOTES

Meaning: a transaction is an event, generally external, determinable in terms of money, and a two-way process — value is transferred between two parties (each party receives as well as passes value); it must be supported by substantial documents: purchase invoices, bills, pay-slips, cash-memos, passbook etc.

Two approaches to analyse the dual aspect: (1) Accounting Equation Approach and (2) Traditional Approach — accounts affected and entries passed remain the SAME under both; recording is independent of the method of analysis.

Special entries (Gamma Bros type): inventory taken by employees against salary — Dr. Salaries ₹75,000 / Cr. Purchases at COST (not sale price ₹1,00,000); wages ₹18,000 for erection of machinery capitalised — Dr. Machinery / Cr. Bank (not Wages); proprietor's income-tax paid — Dr. Drawings / Cr. Petty Cash.

Discount chain: purchase list price ₹2,00,000 less 10% trade discount recorded at ₹1,80,000 (TD never enters books); on quick payment: Dr. Naveen ₹1,80,000 / Cr. Bank ₹1,75,000, Cr. Discount Received ₹5,000.

Application practise the procedure · 1 question

- Practise journal entries for unusual events: goods taken by employees against salary (credit Purchases/Sales at cost or agreed price, debit Salaries/Employees), wages paid for asset erection (capitalise --- debit Asset, not Wages).
- Drill entries for drawings of goods, abnormal loss, and expenses that must be capitalised versus revenue expenses.
- Always identify the two accounts affected, their nature, then apply debit/credit rules before writing the entry with narration.

PQ 5.1 · RTP 2025-Sep [3] (a) · Practical · --- · Pg 73 asked 6×

LEVEL II
Application

Medium

Topic 6: Accounting Equation Approach

P1-C2-U2.1-T06

Read first Study Para 1.6 --- the accounting equation (Assets = Liabilities + Capital), its expanded form Equity + Long-term Liabilities = Fixed Assets + Current Assets - Current Liabilities, and computing profit as change in equity (E1 - E0).

NOTES

Equation: Assets = Liabilities + Capital; expanded form: Equity + Long-term Liabilities = Fixed Assets + Current Assets - Current Liabilities; holds good at all points of time and for any number of transactions, EXCEPT when there are errors in the accounting process.

Profit = change in equity: $E = A - L$ at any date; Profit = $E1 - E0$ ($E_n > E_{n-1}$ means profit, $E_n < E_{n-1}$ means loss); Opening capital = Closing capital - profit + drawings adjustments; e.g. closing capital ₹35,000 - profit ₹5,000 = opening capital ₹30,000, so opening assets = 12,000 + 30,000 = ₹42,000.

Missing-figure rule: Capital = Assets - Liabilities; treat bracketed liabilities as negative, e.g. Assets ₹57,00,000 and Liabilities (₹2,80,000) give Capital ₹59,80,000.

Rearrangement check: any variant is tested algebraically from Assets = Liabilities + Capital; adding Cash separately to Current Assets double-counts it and makes the equation FALSE.

Effect analysis: credit purchase of furniture (+asset, +liability), cash collected for services (+asset), hiring an employee or a mere purchase agreement (no change) — only money-measurable transactions alter the equation.

Understanding explain with reasons · 1 question

- True/False trap: 'Equity + LTL - CL = FA + CA' is TRUE (just a rearrangement of Equity + LTL = FA + CA - CL); check any given variant by algebraic rearrangement of Assets = Liabilities + Capital.
- Trap: 'Capital + Long Term Liabilities = Fixed Assets + Current Assets + Cash - Current Liabilities' is FALSE because cash is already part of current assets --- it gets double counted.
- Be ready to give the reason: the equation holds at all points of time for any number of transactions, except when there are accounting errors.

TQ 6.1 · MTP 2022-Nov S2 [1] (a) (ii) {C} · True/False · 2M · Pg 74 asked 3×

LEVEL I
Understanding

Medium

Application practise the procedure · 1 question

- Practise missing-figure sums using Capital = Assets - Liabilities; note negative liabilities in brackets, e.g. Assets ₹1,71,00,000 and Liabilities (₹8,40,000) give Capital ₹1,79,40,000.

- Practise: Opening capital = Closing capital - profit; Profit = E1 - E0; then rebuild the closing Balance Sheet.

PQ 6.1 · MTP 2024-Aug [1] (c) {C} · Practical · 4M · Pg 75 asked 2×

LEVEL II
Application

Easy

Topic 7: Traditional Approach

P1-C2-U2.1-T07

Read first Study Para 1.7 --- classification of accounts into Personal (natural, artificial, representative) and Impersonal (Real, Nominal), plus the golden rules of debit and credit for each type.

NOTES

Classification: Personal accounts — (a) natural (Ram, Rita), (b) artificial/legal (Government, companies, clubs, co-operative societies), (c) representative (outstanding liability, prepaid, capital, drawings); Impersonal accounts — Real (assets of the firm but not debt: land, building, investment, fixed deposits, cash) and Nominal (expenses, losses, gains, revenue: salary, interest paid, commission received).

Golden rules: Personal — debit the receiver, credit the giver; Real — debit what comes in, credit what goes out; Nominal — debit expenses and losses, credit incomes and gains.

Care points: Bank A/c and Bank Fixed Deposit are PERSONAL (bank is an artificial person), only Cash in Hand is Real; Rent Outstanding is a REPRESENTATIVE PERSONAL account; both rent paid and rent received are NOMINAL (expense/income); salary paid to Ram is debited to Salary A/c (payment for services, an expense), not Ram's account.

Balances: debit balance in a nominal account shows expenses/losses, credit balance shows incomes/gains; the net result of all nominal accounts (profit or loss) is transferred to the Capital account — nominal accounts are therefore temporary.

Understanding explain with reasons — no question in this edition

- Both rent paid AND rent received are Nominal accounts (expense/income) --- so 'rent received is a Real account' is FALSE.
- Salary paid to Ram is debited to Salary A/c (Nominal), NOT Ram's personal account --- the payment is for services, an expense.
- Cash at Bank is a PERSONAL account (bank is an artificial person); only Cash in Hand is Real. 'Rent Outstanding' is a REPRESENTATIVE PERSONAL account, not Nominal.
- Debit balance in a Nominal account shows expenses/losses, NOT gains (credit balance shows income/gains).

Topic 8: Modern Classification of Accounts

P1-C2-U2.1-T08

Read first Study Para 1.8 --- the six modern account types (Asset, Liability, Capital, Revenue, Expenditure, Withdrawal), their normal balances, and when each is debited or credited; compare with Illustration 6's dual classification table.

NOTES

Six types with normal balances: Asset (Dr.), Expenditure (Dr.), Withdrawal/Drawings (Dr.); Liability (Cr.), Capital (Cr.), Revenue (Cr.) — an account is debited/credited on increase on the side of its normal balance and gets the opposite entry on decrease.

Dual classification (Illustration 6): prepaid salary — personal / asset; rent outstanding and rent received in advance — personal / liability; bad debts recovered — nominal / gain; drawings and personal income-tax — personal / capital reduction (Capital – Drawings); closing inventory — real / asset; GST payable — personal / liability.

Trap: Outstanding Expenditure is NOT nominal — representative personal under the traditional approach and a LIABILITY under the modern approach.

Understanding explain with reasons · 1 question

- Trap: 'Outstanding Expenditure is a nominal account' is FALSE --- under traditional approach it is a representative personal account; under modern approach it is a LIABILITY.
- Memorise normal balances: Assets/Expenses/Drawings = debit; Liabilities/Capital/Revenue = credit; increases go on the side of the normal balance.
- Practise dual classification of items like prepaid salary (personal/asset), bad debts recovered (nominal/gain), drawings (personal/capital reduction).

TQ 8.1 · RTP 2025-Sep [1] (b) · True/False · 2M · Pg 75

LEVEL 1
Understanding

Easy

Topic 9: Journal

P1-C2-U2.1-T09

Read first Study Para 1.9 --- journal as the book of original entry recording transactions chronologically, the five-column format, journalising process, and compound/composite entries; practise Illustrations 5 and 7 thoroughly.

NOTES

Definition: the book of original (first) entry in which transactions are entered on a daily basis in chronological order, showing the accounts to be debited and credited with a narration; recording

in journal = journalising; two types — general journal and specialised journal (used for many repetitive transactions of the same nature).

Five columns: (1) Date (year at top, then month and date), (2) Particulars — account debited with “Dr.”, account credited preceded by “To”, then narration, (3) Ledger Folio, (4) Dr. Amount, (5) Cr. Amount; page totals written with “Carried forward”/“Brought forward”; a compound/composite entry combines two or more transactions — total debits must equal total credits.

Full-settlement entries (Illus. 5): received ₹2,300 from Arvind settling ₹2,400 — Dr. Bank 2,300, Dr. Discount (Allowed) 100 / Cr. Arvind 2,400; paid Amrit ₹9,450 settling ₹9,500 — Dr. Amrit 9,500 / Cr. Bank 9,450, Cr. Discount (Received) 50.

Memorise pro-formas: drawings of goods — Dr. Drawings / Cr. Purchases at COST; free samples — Dr. Advertisement Expenses / Cr. Purchases; goods returned to supplier — Dr. Supplier / Cr. Purchases Returns; capital introduced — Dr. Bank / Cr. Capital; cash withdrawn from bank — Dr. Cash / Cr. Bank.

Bad debts: debtor insolvent paying 50 paise in a rupee on ₹600 — Dr. Cash 300, Dr. Bad Debts 300 / Cr. Debtor 600; debts written off later recovered are credited to Bad Debts Recovered A/c.

Remembering memorise · 1 question

- Definition for short note: Journal is the book of original entry in which transactions are entered daily in chronological order, showing accounts to be debited and credited with narration.
- Know the 5 columns: Date, Particulars, Ledger Folio, Dr. Amount, Cr. Amount; recording in journal = journalising; two types --- general and specialised journal.

TQ 9.1 · RTP 2023-Jun [20] (iv) · Short Note · --- · Pg 76 **asked 4x**

LEVEL I
Remembering

Easy

Application practise the procedure · 5 questions

- Practise full-settlement entries with discount: cheque ₹9,000 settling ₹10,000 means Discount Allowed ₹1,000 Dr.; on dishonour, discount earlier allowed is also written back.
- Drawings of goods: credit Purchases at COST (not sales price); free samples: debit Advertisement, credit Purchases.
- Practise closing/transfer entries: transfer Opening Inventory, Purchases, Carriage Inwards, Wages, Returns to Trading A/c; compute Gross Profit and transfer to P&L.
- Practise business-purchase entries (debit assets, credit liabilities taken over, balance to Capital) and outstanding/prepaid adjustments.

PQ 9.1 · RTP 2022-May [3] (a) · Practical · --- · Pg 76

LEVEL II
Application

Medium

PQ 9.2 · MTP 2022-Nov S1 [5] (b) · Practical · 5M · Pg 78 **asked 3x**

LEVEL II
Application

Medium

PQ 9.3 · MTP 2024-Apr [5] (b) (i) · Practical · 5M · Pg 79 asked 2×	LEVEL II Application	Medium
PQ 9.4 · RTP 2025-Jan [3] (a) · Practical · --- · Pg 81 asked 6×	LEVEL II Application	Medium
PQ 9.5 · RTP 2025-May [3] (a) · Practical · --- · Pg 82	LEVEL II Application	Medium

Topic 10: Advantages of Journal

P1-C2-U2.1-T10

Read first Study Para 1.10 --- the three advantages (importance) of maintaining a journal under the double entry system.

NOTES

Frame first: journal is the book of original entry recording transactions chronologically under the double entry system; “importance of Journal” = “advantages of Journal”.

Three advantages (Para 1.10): (i) transactions recorded in chronological order give complete information about business transactions on a timely basis; (ii) each entry is supported by a narration — a precise explanation of the transaction for proper understanding of the entry; (iii) journal forms the basis for posting the entries in the ledger and reduces the chances of error.

For 5 marks: expand each point and add that recording the debit and credit aspects together ensures debits equal credits, aiding accuracy of the accounts.

Remembering memorise · 1 question

- Memorise the 3 advantages: (i) chronological (date-wise) record gives complete and timely information about business transactions; (ii) each entry is supported by a narration --- a precise explanation for proper understanding of the entry; (iii) journal forms the basis for posting entries into the ledger and reduces the chances of error.
- Note the exam wording --- 'importance of Journal' means the same as 'advantages of Journal'; frame the answer with a one-line definition (book of original entry, chronological record under double entry) before listing the points.
- For a 5-mark answer, expand each point to 2-3 lines and add that recording both debit and credit aspects together helps ensure debits equal credits, aiding accuracy of the accounts.

TQ 10.1 · PYQ 2023-Jun [6] (b) · Descriptive · 5M · Pg 83	LEVEL I Remembering	Medium
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Topic 11: Accounting for GST

P1-C2-U2.1-T11

Read first Study Para 1.11 --- CGST/SGST on intra-state and IGST on inter-state supplies, Input GST

(asset) vs Output GST (liability), reversal situations, ITC set-off order, and Illustrations 8-10 on GST journal entries.

NOTES

Framework: GST is a single, destination-based consumption tax on supply of goods and services with no cascading (tax-on-tax); intra-state supply — CGST (Centre) + SGST/UTGST (State/UT); inter-state supply — IGST (Centre), where $IGST = CGST + SGST$; Input GST (tax paid on purchases, a credit availed) is an ASSET; Output GST (tax charged on supplies) is a LIABILITY; purchases, expenses and sales are posted net of GST.

Pro-forma entries: Purchase — Dr. Purchases (net) + Dr. Input CGST/SGST or IGST / Cr. Creditor-Bank (gross); Sale — Dr. Debtor/Bank (gross) / Cr. Sales (net) + Cr. Output CGST/SGST or IGST; ITC utilisation — Dr. Output GST A/c / Cr. Input GST A/c.

Discount rule: GST is computed AFTER trade discount but BEFORE cash discount; e.g. list ₹1,00,000 – 20% TD = ₹80,000, CGST+SGST @6% each on 80,000; the 5% cash discount ₹4,000 is a separate Discount Allowed entry with NO GST reversal; GST-inclusive price: value = gross $\times 100/112$ (e.g. ₹44,800 furniture = ₹40,000 + IGST ₹4,800 @12%).

Reversals: reverse INPUT GST on purchases returns, drawings, free samples, gifts not qualifying as supply, and goods lost in fire/theft (Dr. Drawings gross / Cr. Purchases + Cr. Input CGST/SGST); reverse OUTPUT GST on sales returns and rebates for defective goods (Dr. Sales Return + Dr. Output GST / Cr. Customer), but NOT on prompt-payment rebates.

ITC set-off order: IGST credit — first against IGST, balance against CGST or/and SGST in any order/proportion; CGST credit — first CGST then IGST, never against SGST; SGST credit — first SGST then IGST, never against CGST.

Application practise the procedure · 4 questions

- Golden template: Purchases --- Dr. Purchases (net of trade discount) + Dr. Input CGST/SGST/IGST, Cr. Supplier (gross). Sales --- Dr. Customer (gross), Cr. Sales (net) + Cr. Output CGST/SGST/IGST.
- GST is always computed AFTER trade discount but BEFORE cash discount; cash discount is a separate Discount Allowed/Received entry with no GST effect.
- Practise pricing chains: cost ₹20,000 + 25% markup = ₹25,000, less 10% TD = ₹22,500, then CGST and SGST \@6% each on ₹22,500.
- Reverse Input GST on purchase returns, drawings, free samples and goods lost; reverse Output GST on sales returns; practise ITC utilisation entry (Output A/c Dr. To Input A/c).

PQ 11.3 · RTP 2026-May [3] (a) (ii) · Practical · --- · Pg 87

LEVEL II
Application

Easy

PQ 11.1 · PYQ 2024-Jun [1] (c) {C} · Practical · 4M · Pg 84 asked 2×

LEVEL II
Application

Medium

PQ 11.2 • PYQ 2026-Jan [1] (c) {C} • Practical • 4M • Pg 85

LEVEL II
Application

Medium

PQ 11.4 • PYQ 2026-Sep [1] (c) {C} • Practical • 4M • Pg 87

LEVEL II
Application

Medium

Unit 2.2: Ledgers

P1-C2-U2.2 • Importance D • Rank 6 in chapter • Category C • 4.4% of chapter questions • 4 questions

Topic 1: Introduction

P1-C2-U2.2-T01

Read first Study Para 2.1 and 2.2 --- meaning of the ledger as the book containing all personal, real and nominal accounts (the 'principal books of account') and the specimen T-format with its four columns on each side.

NOTES

Ledger (SM): "The book which contains all set of accounts (viz. personal, real and nominal accounts), is known as Ledger" — the principal books of account in which the account-wise balance of each account is determined; it gives full information regarding all transactions of every individual account and is the base for preparing the trial balance and financial statements (so the True/False "ledger is the principal book of accounts" is TRUE).

Specimen: T-format with debit (left) and credit (right) sides; EACH side has four columns — (i) Date, (ii) Particulars, (iii) Journal Folio (page from where entries are posted) and (iv) Amount (₹).

Journal vs Ledger: distinguish on these bases —

Journal: book of original entry	Ledger: principal book of accounts
Records transactions in chronological order	Records in analytical, account-wise order
Transaction-wise record of debit and credit	Account-wise consolidated balance of each account
Every entry supported by narration	No narration; only 'To'/'By' references
Forms basis for posting into the ledger	Forms basis for trial balance and financial statements

Understanding explain with reasons · 1 question

- Distinguish Journal vs Ledger on 4-5 bases: book of original entry vs principal book; chronological vs analytical order; transaction-wise record vs account-wise balance; journal has narration, ledger does not; trial balance is prepared from the ledger.
- True/False: 'A ledger is also known as the principal books of accounts' is TRUE --- reason: it classifies all amounts account-wise and is the base for preparing the trial balance and financial statements.
- Know the specimen: each side (Dr. left, Cr. right) has Date, Particulars, Journal Folio and Amount columns.

TQ 1.1 · PYQ 2025-Jan [1] (a) (vi) {C} · True/False · 2M · Pg 90 asked 2×

LEVEL I
Understanding

Easy

Topic 2: Specimen of Ledger Accounts

P1-C2-U2.2-T02

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.2: the ruled form of a ledger account with its two sides and four columns each.**NOTES**

Form: a ledger account has two sides — debit (left side) and credit (right side); each side has four columns: (i) Date, (ii) Particulars, (iii) Journal Folio (J.F. — page from where entries are taken for posting) and (iv) Amount (₹) — headed “Dr.” on the left and “Cr.” on the right.

Usage: items posted on the debit side are prefixed “To” and on the credit side “By” in the Particulars column — these words have no meaning of their own but conventionally point to the account debited/credited.

Topic 3: Posting

P1-C2-U2.2-T03

Read first Study Para 2.3 --- definition of posting and the three rules regarding posting of entries in the ledger, including the use of 'To' and 'By'.**NOTES**

Definition (SM): “The process of transferring the debit and credit items from journal to classified accounts in the ledger is known as posting” — journal → ledger, never ledger → journal (common True/False trap).

Three rules of posting: (i) a separate account is opened in the ledger for each distinct account and

journal entries are posted to the respective account accordingly; (ii) 'To' is used with accounts written on the debit side and 'By' with accounts on the credit side — these words have no real meaning, they merely mark the account debited and credited; (iii) the account debited in the journal is also debited in the ledger, but with reference to the corresponding credit account (and vice versa).

5-mark frame: first define the ledger as the principal books of account containing all personal, real and nominal accounts and providing full information of every account, then list the three posting rules.

Understanding explain with reasons · 2 questions

- Posting = the process of transferring debit and credit items from the journal to the classified accounts in the ledger (not ledger to journal --- common True/False trap).
- Explain the 3 rules: (i) a separate account is opened for each distinct account and entries posted to it; (ii) 'To' prefixes accounts on the debit side, 'By' on the credit side (words have no real meaning); (iii) the account debited in the journal is debited in the ledger but with reference to the corresponding credit account.
- For the 5-mark version, first define principal books of account (ledger containing all personal, real and nominal accounts giving full information of every account), then list the posting rules.

TQ 3.1 · PYQ 2021-Dec [6] (b) (ii) · Descriptive · 2.5M · Pg 91 asked 9x

LEVEL I
Understanding

Easy

TQ 3.2 · PYQ 2026-Jan [6] (b) DESC 5 Marks · · --- · Pg 91

LEVEL I
Understanding

Medium

Topic 4: Balancing an Account

P1-C2-U2.2-T04

Read first Study Para 2.4 --- the technique of totalling both sides, carrying down the difference as 'Balance c/d' and bringing it down as 'Balance b/d', and which types of accounts are balanced.

NOTES

Technique: total both sides and deduct the smaller total from the bigger to get the difference; if the credit side is bigger it is a CREDIT balance — written on the debit side as "To Balance c/d" (carried down) so the two sides equalise, then written on the credit side as "By Balance b/d" (brought down) = the opening balance of the new period; a debit balance is treated vice versa (By Balance c/d on credit side, To Balance b/d on debit side); e.g. goods bought ₹1,000, paid ₹850 — balance owing ₹150.

Nominal accounts are NOT balanced (True/False: "nominal accounts are balanced at year end" is FALSE) — at period end their totals are transferred to the Profit and Loss Account, since they are

revenues/gains or expenses/losses.

Carried forward: only personal and real account balances are ultimately shown in the Balance Sheet at the end of the accounting period; the Capital account is adjusted for profit or loss (the net of nominal accounts).

Understanding explain with reasons · 1 question

- True/False trap: 'Nominal accounts are balanced at the end of the year' is FALSE --- nominal accounts are NOT balanced; their totals are transferred to the Profit and Loss Account.
- Only personal and real account balances are carried forward and shown in the Balance Sheet; the net of nominal accounts (profit/loss) is adjusted in the Capital account.
- Understand the mechanics: if credit side is bigger it is a credit balance, written as 'To Balance c/d' on the debit side, then brought down as 'By Balance b/d' --- the opening balance of the new period (and vice versa for debit balances).

TQ 4.1 · PYQ 2024-Sep [1] (a) (i) {C} · True/False · 2M · Pg 92 asked 3×

LEVEL I
Understanding

Easy

Unit 2.3: Trial Balance

P1-C2-U2.3 · Importance D · Rank 5 in chapter · Category C · 6.7% of chapter questions · 6 questions

Topic 1: Introduction

P1-C2-U2.3-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §3.1: trial balance as the third phase of the accounting process and what its agreement proves.

NOTES

Meaning: after posting the ledger, a statement is prepared showing separately the debit and credit balances (or the totals of debit and credit sides of every account) — the trial balance; the totals of the two columns should agree because under Double Entry the amount written on debit sides always equals amounts entered on credit sides.

What agreement proves: agreement indicates ARITHMETIC accuracy — reasonable confidence the work is free from clerical errors, but not proof of cent per cent accuracy, since errors of principle and compensating errors may still remain; disagreement means arithmetic error(s).

Nature and timing: trial balance is a STATEMENT, not an account; generally prepared at monthly intervals, it can be prepared any time under double entry but preferably at the end of the reporting period (month/quarter/year end) before preparation of financial statements.

Topic 2: Objectives of Preparing the Trial Balance

P1-C2-U2.3-T02

Read first Study Para 3.1 and 3.2 --- trial balance as the third phase of the accounting process (a statement, not an account) and its three objectives.

NOTES

Definition: preparation of the trial balance is the THIRD phase of the accounting process — after posting to the ledger, a statement is prepared showing separately the debit and credit balances (or totals) of all ledger accounts as on a particular date; it is a STATEMENT, not an account; it can be prepared any time, but preferably at the end of the reporting period (month/quarter/year) before preparing financial statements.

Three objectives (Para 3.2): (i) enables one to establish that posting and other accounting processes are free from arithmetical errors — i.e. establishes arithmetical accuracy of the books; (ii) financial statements are normally prepared on the basis of an agreed trial balance, otherwise they will not give a true and fair picture; (iii) serves as a summary of what is contained in the ledger — the ledger need be seen only when details of an account are required.

Reason it tallies: under the Double Entry System amounts written on the debit sides of accounts always equal amounts entered on the credit sides, so total debits must equal total credits; agreement gives reasonable confidence that the books are free from clerical errors.

True/False traps: a tallied trial balance proves only ARITHMETICAL accuracy, not cent-per-cent accuracy — errors of principle and compensating errors may still remain (so “agreement is conclusive/absolute proof of accuracy” is FALSE); but “trial balance does not ensure arithmetical accuracy” is also FALSE — that is precisely its purpose.

Remembering memorise · 1 question

- Memorise the 3 objectives: (i) establishes arithmetical accuracy of the books; (ii) financial statements are normally prepared from an agreed trial balance; (iii) it serves as a summary of what is contained in the ledger.
- Definition: a statement showing debit and credit balances (or totals) of all ledger accounts as on a particular date; trial balance is a statement, NOT an account.

TQ 2.2 · PYQ 2006-May [6] (ii) · Short Note · 5M · Pg 95 asked 9x

LEVEL 1
Remembering

Easy

Understanding explain with reasons · 1 question

- True/False trap: a tallied trial balance proves only ARITHMETICAL accuracy, not that books follow accepted accounting principles --- errors of principle and compensating errors may still exist (statement FALSE).
- 'Trial Balance does not ensure arithmetical accuracy' is FALSE --- checking arithmetical accuracy is precisely its purpose; but 'Trial Balance is an absolute/conclusive proof of accuracy' is also FALSE.
- Reason to quote: under double entry, total debits always equal total credits, so agreement gives reasonable (not absolute) confidence that the books are free from clerical errors.

TQ 2.1 · PYQ 2003-May [5] (viii) · True/False · 2M · Pg 94 asked 4x

LEVEL I
Understanding

Medium

Topic 3: Limitations of Trial Balance

P1-C2-U2.3-T03

Read first Study Para 3.3 --- the five types of errors that remain undetected even when the trial balance agrees.

NOTES

Agreement is not conclusive proof of accuracy — five errors remain undetected even when it tallies (Para 3.3): (i) a transaction has not been entered at all in the journal; (ii) a wrong amount has been written in BOTH columns of the journal; (iii) a wrong account has been mentioned in the journal; (iv) an entry has not at all been posted in the ledger; (v) an entry is posted TWICE in the ledger.

Also recall: compensating errors (they cancel out) and errors of principle do not disturb the agreement of the trial balance; a trial balance cannot find a missing entry from the journal.

5-mark frame: first define the trial balance (statement of ledger balances on a date, basis for final accounts), then state agreement is not conclusive proof and explain the five error types; conclude that it is still very useful — without it, preparation of financial statements would be difficult.

Understanding explain with reasons · 1 question

- Agree with the statement and list the 5 undetected errors: (i) transaction not entered in the journal at all; (ii) wrong amount written in both columns of the journal; (iii) wrong account mentioned in the journal; (iv) entry not posted in the ledger at all; (v) entry posted twice in the ledger.
- For the 5-mark answer, first define trial balance (statement of ledger balances on a date, basis for final accounts), then state agreement is not conclusive proof of accuracy and explain the error types.
- Also recall: compensating errors and errors of principle do not disturb the agreement of the trial balance.

TQ 3.1 · PYQ 2026-May [6] (b) · Descriptive · 5M · Pg 95

LEVEL I
Understanding

Medium

Topic 4: Methods of Preparation of Trial Balance

P1-C2-U2.3-T04

CONCEPT BASE — no exam question asked yet · essential for full preparation**Read first** Read §3.4 with Illustrations 1-2: the Total, Balance, and Total-and-Balance methods.

NOTES

Total method: every ledger account is totalled and the total of both debit and credit sides is transferred to the trial balance — can be prepared as soon as accounts are totalled, saving balancing time, but is not commonly used since financial statements need only NET balances, so this trial balance cannot be used directly for their preparation.

Balance method: every ledger account is balanced and only those balances are carried to the trial balance — the method commonly used by accountants; financial statements are prepared on the basis of ledger balances.

Total and balance method: combines both — the trial balance shows four amount columns (debit total, credit total, debit balance, credit balance) for each head of account.

Topic 5: Adjusted Trial Balance (Through Suspense Account)

P1-C2-U2.3-T05

Read first Study Para 3.5 --- use of a suspense account to tally a disagreeing trial balance when errors cannot be located in time.

NOTES

Rule (Para 3.5): if the trial balance does not agree after transferring all ledger balances (including cash and bank) and the errors are not located timely, it is tallied by transferring the difference of the debit and credit sides to a Suspense Account — so “the rationale behind opening a suspense account is to tally the trial balance” is TRUE, enabling financial statements to be prepared on time.

Nature: Suspense A/c is a TEMPORARY account (not permanent — False in True/False), opened only to proceed further; it is closed when the errors are located and rectified.

Side rule: if the DEBIT column is short, the difference is DEBITED to Suspense A/c (and vice versa); e.g. corrected trial balance with Dr. ₹24,405 vs Cr. ₹25,580 shows Suspense A/c ₹1,175 on the debit side as balancing figure.

Understanding explain with reasons — no question in this edition

- True/False: 'The rationale behind opening a suspense account is to tally the trial balance' is TRUE --- the difference between debit and credit totals is transferred to Suspense A/c so financial statements can be prepared on time.
- Suspense account is a TEMPORARY account, opened only when errors are not located timely; it is closed when the errors are found and rectified.
- If the debit column is short, the difference is DEBITED to Suspense A/c (and vice versa).

Topic 6: Rules of Preparing the Trial Balance

P1-C2-U2.3-T06

Read first Study Para 3.4 and 3.6 --- methods of preparation (Total, Balance, Total- and-Balance) and the rules for placing balances: assets, expenses, losses and drawings in the debit column; liabilities, incomes, gains and capital in the credit column. Work Illustrations 3-5 on corrected trial balances.

NOTES

Three methods (Para 3.4): (1) Total method — the totals of both sides of every ledger account are carried to the trial balance; quick (no balancing needed) but not commonly used since financial statements need net balances; (2) Balance method — only the balance of each ledger account is carried; commonly used by accountants, basis for financial statements; (3) Total-and-Balance method — combines both, with four amount columns.

Placement rules (Para 3.6): DEBIT column — balances of all assets, expenses, losses and drawings (thus opening inventory, sales/returns inward, discount allowed, bad debts, carriage inward, trade receivables/dues from customers, cash, Input CGST/SGST/IGST); CREDIT column — balances of all liabilities, incomes, gains and capital (thus purchases/returns outward, discount received, interest received, bank overdraft, trade payables, bills payable, Output CGST/SGST).

Corrected-TB drill (Singhania/Fintech type): a tallied trial balance may still be wrong — scan every item and reclassify by nature of the account: dues from customers = asset = Dr.; purchases return = Cr. (assets go out); trade payables and bills payable = liability = Cr.; opening inventory = Dr.; sales return = Dr. (assets come in); re-tally the columns, putting any residual difference to Suspense A/c.

Closing inventory: normally valued outside the trial balance and treated only as an adjustment item (in Illustration 4 closing inventory ₹574 is NOT a trial balance item) — but it appears IN the trial balance when purchases are already adjusted (Adjusted Purchases method), so “closing stock will never appear in the trial balance” is FALSE.

Understanding explain with reasons · 1 question

- Trap: 'Closing stock will never appear in the Trial Balance' is FALSE --- it appears when purchases are already adjusted (Adjusted Purchases method); normally it stands outside as an adjustment item.
- Know the placement rules cold: Dr. column --- assets, expenses, losses, drawings, sales returns; Cr. column --- liabilities, incomes, gains, capital, purchase returns.

TQ 6.1 · PYQ 2006-May [5] (iv) · True/False · 2M · Pg 96

LEVEL I
Understanding**Medium****Application** practise the procedure · 1 question

- Practise preparing a trial balance from a list of ledger balances (Balance method) and totalling both columns to agreement.
- Watch typical items: Discount Allowed/Carriage Inward Dr.; Bank Overdraft, Discount Received Cr.; Input GST accounts Dr., Output GST accounts Cr.

PQ 6.2 · RTP 2025-May [4] (a) · Practical · --- · Pg 98

LEVEL II
Application**Medium****Analysis** work through mixed data · 1 question

- Practise 'corrected trial balance' problems (Mr. X / Singhanian type): scan every item, reclassify wrongly placed balances (e.g. purchase returns wrongly shown Dr., debtors wrongly shown Cr.), and re-tally.
- Reason from the nature of each account: dues from customers = asset = Dr.; bills payable = liability = Cr.; opening inventory = Dr.; use Suspense A/c for any residual difference.
- Note the interlinkage: closing inventory given outside the trial balance is only an adjustment, not a trial balance item.

PQ 6.1 · PYQ 2022-May [1] (c) {C} · Practical · 4M · Pg 97 **asked 8x****LEVEL II**
Analysis**Medium**

Unit 2.4: Subsidiary Books

P1-C2-U2.4 · Importance A · Rank 3 in chapter · Category A · 20.0% of chapter questions · 18 questions

Topic 1: Introduction

P1-C2-U2.4-T01

Read first Study Para 4.1 of Unit 4 (Subsidiary Books): the meaning of books of original/prime entry, the list of eight subsidiary books, their advantages, and the distinction between subsidiary books and principal books (Para 4.2).

NOTES

Books of original/prime entry (Para 4.1): separate registers kept for each class of transactions, in which transactions are first recorded and on whose basis ledger accounts are then prepared without further journal entries — the Practical System of Book-keeping (English System); there is no departure from the rules of double entry.

Eight subsidiary books: (i) Cash Book — receipts/payments of cash and bank; (ii) Purchases Book — credit purchases of goods dealt in or materials/stores; (iii) Purchase Returns Book; (iv) Sales Book — sales of goods dealt in; (v) Sales Returns Book; (vi) Bills Receivable Book — promissory notes/hundies received; (vii) Bills Payable Book — notes/hundies issued; (viii) Journal Proper — whatever cannot be recorded in the other seven; the word “Journal” may replace “book”, and B/R and B/P books ARE subsidiary books (alternatives to the journal).

Five advantages: (a) division of work among a number of clerks; (b) specialisation and efficiency — same work allotted to one person over time; (c) saving of time — processes undertaken simultaneously; (d) availability of information — each class of transaction at one place; (e) facility in checking — location of errors when the trial balance disagrees is facilitated, and errors and frauds are checked.

Subsidiary vs principal books (Para 4.2): transactions are FIRST recorded in subsidiary books to enable further processing; the ledger and the cash book are the principal books since they furnish information for preparation of the trial balance and financial statements.

Subsidiary books	Principal books
Books of original/prime entry — transactions first recorded here	Ledger and Cash Books
Purchases, Sales, both Returns books, B/R, B/P books, Journal Proper	Ledger; Simple, discount-column and bank-discount-column cash books
Ledger accounts are posted on their basis	Furnish data for trial balance and financial statements

Remembering memorise · 1 question

- Memorise the standard list of subsidiary books: Cash Book, Purchases Book, Purchase Returns Book, Sales Book, Sales Returns Book, Bills Receivable Book, Bills Payable Book and Journal Proper --- this exact 5-mark list is repeatedly asked.
- Learn the five advantages of subsidiary books: division of work, specialisation and efficiency, saving of time, availability of information, facility in checking errors/fraud.
- Remember alternative names: books of original entry / prime entry; ledger and cash book = principal books.

TQ 1.3 · MTP 2024-Jul [6] (Or) (c) · Descriptive · 5M · Pg 103 asked 3x

LEVEL I
Remembering

Easy

Understanding explain with reasons · 2 questions

- Be able to justify (True) that Bills Receivable and Bills Payable books ARE subsidiary books --- they are alternatives to the journal.

- Explain each advantage of subsidiary books with one line of reasoning for the 5- mark descriptive answer.
- Understand that subsidiary books follow double entry --- ledger accounts are posted from them without separate journal entries.

TQ 1.2 • MTP 2024-Jul [1] (a) (vi) {C} • True/False • 2M • Pg 103 asked 2×

LEVEL I
Understanding

Easy

TQ 1.1 • PYQ 2024-Jun [6] (b) • Descriptive • 5M • Pg 102 asked 5×

LEVEL I
Understanding

Medium

Topic 2: Distinction between Subsidiary Books and Principal Books

P1-C2-U2.4-T02

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §4.2 and its chart classifying the financial books of accounts.

NOTES

Distinction: subsidiary books are the books in which transactions are FIRST recorded to enable further processing; the ledger and the cash book are principal books since they furnish information for preparation of the trial balance and financial statements.

Principal Books	Subsidiary Books
Ledger	Purchase Book • Sales Book
Cash Books — simple cash book, cash book with discount column, cash book with bank & discount column, petty cash book	Purchase Return Book • Sales Return Book • Bills Receivable Book • Bills Payable Book • Journal Proper

Topic 3: Purchases Book

P1-C2-U2.4-T03

Read first Study Para 4.3: the Purchases Book records only credit purchases of goods dealt in; learn the format (Particulars, Details, Amount columns), treatment of trade discount and packing/freight charges, and posting to Purchases A/c (debit total) and suppliers' accounts (credit).

NOTES

Scope (Para 4.3): records only CREDIT purchases of goods dealt in or materials used in the business; cash purchases go to the Cash Book, and credit purchases of items other than

goods/materials (office furniture, typewriter, computer) are journalised in the Journal Proper — never entered here.

Format and computation: Particulars column names the supplier, articles and quantities; per-article amounts in the Details column; total the amounts of one purchase, ADD packing/other charges (freight), DEDUCT trade discount, and carry the net to the Amount column — e.g. gross ₹72,000 less 10% trade discount ₹7,200 = ₹64,800 plus freight ₹150 = ₹64,950 (Illustration 2); the Amount-column total = total credit purchases of the period.

Posting: total of the Amount column debited to Purchases A/c; each supplier (now a trade payable) credited individually — Illustration 1: Purchases A/c Dr. ₹5,022 against Brown & Co. ₹3,042, Paper Co. ₹1,800, Verma Bros. ₹180, so total credits equal the debit and double entry is complete; freight charged is posted separately (supplier credited via Purchases A/c and Freight A/c).

Understanding explain with reasons · 1 question

- True/False trap: credit purchase of fixed assets (furniture, computer, machinery) is NOT recorded in the Purchases Book --- it goes to the Journal Proper.
- Cash purchases go to the Cash Book, never the Purchases Book; only credit purchases of goods dealt in are entered.

TQ 3.1 · PYQ 2026-Jan [1] (a) (ii) {C} · True/False · 2M · Pg 104

LEVEL I
Understanding

Easy

Application practise the procedure · 2 questions

- Practise the calculation: gross amount less trade discount, then add packing/freight charges; e.g. purchases ₹75,800 less 5% trade discount = ₹72,010 --- the FULL ₹72,010 enters the Purchases Book even if half is paid in cash immediately (cash payment does not split the book entry when purchased on credit).
- Practise preparing the Purchases Book with quantity × rate workings per supplier, deducting trade discount and excluding cash purchases and asset purchases.
- Know the posting: total of amount column debited to Purchases A/c; each supplier credited individually.

PQ 3.1 · PYQ 2021-Jul [5] (a) · Practical · 5M · Pg 104 asked 3×

LEVEL II
Application

Medium

PQ 3.2 · PYQ 2025-Sep [1] (c) {C} · Practical · 4M · Pg 105

LEVEL II
Application

Medium

Topic 4: Sales Book

P1-C2-U2.4-T04

Read first Study Para 4.4: the Sales Book records only credit sales of goods dealt in by the firm;

learn its format, trade-discount treatment, and posting (customers debited individually, total credited to Sales A/c).

NOTES

Scope (Para 4.4): “a register specially kept to record credit sales of goods dealt in by the firm”; cash sales are entered in the Cash Book, and credit sales of items other than the goods dealt in (e.g. furniture) are journalised — rules are the same as for the Purchases Book.

Entry method: Particulars column records customer, goods and quantities; item amounts in the Details column; after totalling one sale add packing charges and deduct trade discount; net amount to the outer column — Illustration 3: ₹39,600 + ₹40,000 + ₹1,12,500 = ₹1,92,100 monthly total (cash sale of 13 shirts and credit sale of furniture excluded with a note).

Posting: each customer's account debited with the respective net invoice amount; the Sales Book total credited to Sales A/c — total debits equal the one credit, so double entry is preserved (Illustration 3: Sales A/c Cr. ₹1,92,100).

Sale or return: goods sent on approval and passed through the Sales Book are not sales while the customer's return option is open — at year-end reverse the sale (customer credited), remove the profit loading and take the unapproved goods into inventory at cost (cf. rectification entry: Dr. Sales/P&L Adj. with profit, Dr. Inventory at cost, Cr. Customer with invoice price).

Understanding explain with reasons · 1 question

- True/False trap: the Sales Book is NOT kept for both cash and credit sales --- cash sales go to the Cash Book; credit sale of assets (e.g. furniture) goes to the Journal Proper.
- Explain that the Sales Book total is credited to Sales A/c while each customer's account is debited --- double entry is preserved.

TQ 4.1 · PYQ 2021-Jan [1] (a) (iii) {C} · True/False · 2M · Pg 107 **asked 6x**

LEVEL I

Understanding

Easy

Application practise the procedure · 5 questions

- Practise Sales Book preparation: quantity × rate per item, less trade discount per invoice, net amount in outer column; exclude cash sales and sales of assets with a note.
- Practise 4--5 mark formats (e.g. Kamal & Sons, Gurgaon Engineers pattern): multiple invoices, different trade discount rates, monthly total.

PQ 4.5 · PYQ 2025-May [5] (b) (ii) · Practical · 2.5M · Pg 110

LEVEL II

Application

Easy

PQ 4.1 · PYQ 2020-Nov [1] (c) {C} · Practical · 4M · Pg 107

LEVEL II

Application

Medium

PQ 4.2 · RTP 2023-Jun [10] · Practical · --- · Pg 108	LEVEL II Application	Medium
PQ 4.3 · PYQ 2023-Jun [1] (c) {C} · Practical · 4M · Pg 109	LEVEL II Application	Medium
PQ 4.4 · RTP 2025-Jan [4] (a) · Practical · --- · Pg 110 asked 2x	LEVEL II Application	Medium

Analysis work through mixed data — no question in this edition

- Work through 'sale or return' situations: goods sent on approval are recorded as sales only on approval/expiry of return period; at year-end, unapproved goods must be removed from sales and included in inventory at cost.
- Watch the interlinkage between the Sales Book, customer accounts and closing inventory when the return option is still open at the balance sheet date.

Topic 5: Sales Return Books or Returns Inward Book

P1-C2-U2.4-T05

Read first Study Para 4.5: recording returns of goods by customers, the credit note issued to customers, and posting (Returns Inward A/c debited with the total, customers credited individually).

NOTES

Scope (Para 4.5): where customers frequently return goods sold to them, returns are recorded in the Sales Returns Book or Returns Inward Book; rules and entries are the same as the Sales Book — quantity × rate less trade discount at the ORIGINAL sale rate (SM example: 6 copies @ ₹7 = ₹42 less 10% = ₹37.80); only returns of goods sold on credit pass through it — a return refunded in cash is a Cash Book transaction.

Credit note: on goods being received and accepted back from customers, a CREDIT note is issued to the customer concerned, showing the amount to be credited to his account (debit notes belong to purchase returns, not this book).

Posting: sales returns reduce sales, so the total may be debited to Sales A/c, but usually a separate Returns Inward A/c is opened and debited with the total; the customers who returned goods are credited individually with the respective amounts.

Understanding explain with reasons · 2 questions

- True/False trap: if money is refunded immediately on return, the transaction is recorded in the Cash Book, NOT in the Sales Return Book (True that it will not be recorded there).
- Documents trap: a CREDIT note (issued to the customer) supports the Sales Return Book --- debit notes relate to purchase returns, so 'debit notes are used to prepare Sales Return Book' is False.

TQ 5.1 · PYQ 2006-Nov [5] (ii) · True/False · 2M · Pg 111	LEVEL I Understanding	Easy
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TQ 5.2 · MTP 2025-Jan S2 [1] (a) (v) {C} · True/False · 2M · Pg 112 **asked** **LEVEL I**
9× Understanding

Easy

Application practise the procedure · 1 question

- Practise preparing the Sales Return Book with quantity × rate less trade discount (same rate as original sale), and posting: total debited to Returns Inward A/c, each customer credited.
- Remember only returns of goods sold on credit in the ordinary course are entered.

PQ 5.1 · PYQ 2025-Jan [1] (c) {C} · Practical · 4M · Pg 112

LEVEL II
Application

Medium

Analysis work through mixed data — no question in this edition

- Practise sale-or-return problems: analyse each customer separately --- goods returned within the option period, goods retained/approved, and goods where the period has not expired at period-end; adjust Sales and value unapproved goods at cost in inventory.

Topic 6: Purchase Returns or Returns Outward Book

P1-C2-U2.4-T06

Read first Study Para 4.6: recording returns of goods to suppliers, the debit note issued to the supplier, and posting (suppliers debited individually, total credited to Returns Outward/Purchase Returns A/c) --- see Illustrations 4 and 5.

NOTES

Scope (Para 4.6): conveniently records returns of goods or material purchased to the suppliers (if returns are infrequent, the journal suffices); rules and entries mirror the Purchases Book — quantity × rate less trade discount at the original purchase rate (SM example: fan ₹200 less 10% = ₹180).

Debit note: the firm returning the goods issues a DEBIT note to the supplier, indicating the amount for which the supplier's account is being debited; the supplier in turn issues the necessary credit note.

Posting: each supplier whose name appears in the book is debited (he has received the goods); the total is credited — it can go to Purchases A/c but in practice a separate Purchase Returns or Returns Outward A/c is credited: "By Sundries as per Returns Outward Book" (Illustration 4: suppliers Dr. ₹180 and ₹100; Returns Outward A/c Cr. ₹280).

Exclusions (Illustration 5): return of goods that were purchased for CASH and return of assets not dealt in (e.g. defective computer ₹35,000 returned to B & Co.) are NOT entered in the Purchase Returns Book — only ₹5,000 + ₹13,000 = ₹18,000 of credit-purchase returns of sarees appear.

Understanding explain with reasons — no question in this edition

- True/False trap: the total of the Purchase Returns Book is posted to the CREDIT side of the Purchase Returns A/c (suppliers' accounts are debited), so 'posted to the debit side' is False.
- Know the document flow: the firm returning goods issues a debit note to the supplier; the supplier issues a credit note.

Application practise the procedure · 3 questions

- Practise the standard RTP/MTP format (Alpha & Co./Sampat & Co. pattern): date, debit note number, supplier name, amount; then post to ledger --- each supplier's A/c debited, Purchase Returns A/c credited with the total.
- Exclusions to practise: returns of goods purchased for CASH and returns of assets (e.g. defective computer/furniture not dealt in) are NOT entered in the Purchase Returns Book.
- Compute amounts as quantity × rate less trade discount at the original purchase rate.

PQ 6.1 · RTP 2022-Nov [4] (a) · Practical · --- · Pg 113	LEVEL II Application	Medium
PQ 6.2 · MTP 2023-Apr [1] (c) {C} · Practical · 4M · Pg 114 asked 3×	LEVEL II Application	Medium
PQ 6.3 · PYQ 2026-May [1] (c) {C} · Practical · 4M · Pg 114	LEVEL II Application	Medium

Topic 7: Importance of Journal

P1-C2-U2.4-T07

CONCEPT BASE — no exam question asked yet · essential for full preparation**Read first** Read §4.7: the residual role of the journal proper and its seven types of entries.**NOTES**

Residual role: cash transactions go to the cash book, credit purchases/sales of goods to the purchases/sales books, returns to the return books, bills to the bill books — if there is NO special book meant to record a transaction, it is recorded in the journal (proper).

Seven entry types: (i) opening entries — opening balances of assets/liabilities when books start for the new year; (ii) closing entries — transfer of nominal accounts to P&L at year end; (iii) rectification entries; (iv) transfer entries — amount moved from one account to another; (v) adjusting entries — outstanding expenses, prepaid expenses, interest on capital, depreciation; (vi) entries on dishonour of bills; (vii) miscellaneous — credit purchase of items other than goods dealt in (e.g. furniture/machinery), allowances/charges to customers after issue of invoice, receipt or issue of promissory notes where separate bill books are not kept.

Unit 2.5: Cash Book

P1-C2-U2.5 · Importance D · Rank 4 in chapter · Category C · 10.0% of chapter questions · 9 questions

Topic 1: Cash Book -- A Subsidiary Book and a Principal Book

P1-C2-U2.5-T01

Read first Study Para 5.1: why the Cash Book is a book of original entry (subsidiary book) and simultaneously serves as the Cash A/c and Bank A/c whose balances go directly to the trial balance (principal book).

NOTES

Dual character (SM, Para 5.1): "Cash transactions are straightaway recorded in the Cash Book and on the basis of such a record, ledger accounts are prepared. Therefore, the Cash Book is a subsidiary book. But the Cash Book itself serves as the cash account and the bank account; the balances are entered in the trial balance directly. The Cash Book, therefore, is part of the ledger also."

Standard two-line answer (True, with reasons): (1) subsidiary — it is a book of original entry where cash transactions are first recorded; (2) principal — it itself serves as the Cash A/c and Bank A/c whose balances go straight to the trial balance, so it is part of the ledger; hence the Cash Book is BOTH a subsidiary book and a principal book.

Contrast: the Petty Cash Book, also generally maintained in addition to the main Cash Book, is purely a subsidiary book.

Understanding explain with reasons · 2 questions

- Be ready to answer True with reasons: cash transactions are first recorded in the Cash Book (hence subsidiary), but it itself serves as the cash and bank accounts and its balances enter the trial balance directly (hence principal/part of ledger).
- Frame the standard 2-mark reasoning in two sentences: 'book of original entry' + 'serves as ledger account of cash and bank' --- this exact statement recurs across attempts (2021-Jul, 2026-May).
- Contrast with the Petty Cash Book, which is purely a subsidiary book.

TQ 1.1 · PYQ 2021-Jul [1] (a) (vi) {C} · True/False · 2M · Pg 118 asked 3×	LEVEL 1 Understanding	Easy
TQ 1.2 · PYQ 2026-May [1] (a) (vi) {C} · True/False · 2M · Pg 119	LEVEL 1 Understanding	Easy

Topic 2: Kinds of Cash Book

P1-C2-U2.5-T02

Read first Study Para 5.2: Simple, Two-column and Three-column Cash Books; balancing rules for cash, bank and discount columns; contra entries (marked 'C'); treatment of cheques received, endorsed and dishonoured; also the imprest petty cash format (Illustration 4).

NOTES

Three kinds (Para 5.2): (i) Simple Cash Book — one amount column each side, receipts on the left, payments on the right, balanced like an ordinary account; (ii) Two-column — cash plus discount columns OR cash plus bank columns; (iii) Three-column — cash, bank and discount columns; the Petty Cash Book is additional and purely subsidiary; only CASH discount is entered in the discount columns — trade discount is not shown in the books at all.

Balancing rules: cash column always shows a debit balance (payments cannot exceed available cash); the bank column can show a credit balance — overdraft, when the credit-side total is bigger, the difference being written on the DEBIT side as “To Balance c/d”; discount columns are NEVER balanced, only totalled — debit-side total = discount allowed, debited to Discount A/c; credit-side total = discount received, credited to Discount A/c (memorandum columns only).

Contra entries — mark “C” in L.F.: cash deposited into bank: bank column debit side + cash column credit side; cash withdrawn from bank for office: bank column credit side + cash column debit side (rule: the receiver Dr., the giver Cr.); no further posting is required; a cheque first entered in the cash column and later banked is treated as cash sent to bank.

Cheque treatment: customer's cheque dishonoured — enter in the bank column on the CREDIT side with the party's name; firm's own cheque not paid on presentation — bank column on the debit side; endorsed cheque — entered on the debit side on receipt and on the credit side on endorsement (both sides of the Cash Book; if endorsed the same day, no entry needed); in Illustration 5 the opening bank overdraft ₹500 sits on the credit side.

Credit/debit card sales (Para 5.5): for the seller these equal cash sales — entry 1: Dr. Bank A/c / Cr. Sales A/c; entry 2 for bank commission (1% to 4%, a selling expense): Dr. Commission A/c / Cr. Bank A/c — Illustration 5: 1% on card sales ₹2,800 + ₹3,200 = ₹60 commission.

Understanding explain with reasons · 3 questions

- True/False traps: cash column can NEVER show a credit balance (payments cannot exceed cash available), but the bank column can (overdraft); discount columns are never balanced --- only totalled and transferred to Discount Allowed/Received A/c.
- Trade discount is NOT recorded in the discount column (or anywhere in the books) --- only CASH discount appears in the triple-column cash book.
- Endorsed cheques: if a cheque first entered in the cash book is later endorsed to another party, it must be entered on both sides of the Cash Book (receipt side on receipt, payment side on endorsement).

TQ 2.1 · PYQ 2021-Dec [1] (a) (vi) {C} · True/False · 2M · Pg 119	LEVEL I Understanding	Easy
TQ 2.2 · PYQ 2025-May [1] (a) (i) {C} · True/False · 2M · Pg 119 asked 4×	LEVEL I Understanding	Easy
TQ 2.3 · PYQ 2026-Sep [1] (a) (iii) {C} · True/False · 2M · Pg 120	LEVEL I Understanding	Easy

Application practise the procedure · 2 questions

- Practise the Triple Column Cash Book end-to-end: opening balances (bank overdraft on credit side), contra entries for deposits/withdrawals marked 'C', cash discount allowed/received in memorandum columns, cheque dishonour entered in bank column (credit side), debit/credit card sales through bank with commission charged.
- Practise the Petty Cash Book on the imprest system with analysis columns (conveyance, cartage, stationery, postage, wages, sundries), balancing and reimbursement to restore the imprest.
- Balancing drill: cash and bank columns balanced; discount columns only totalled --- totals posted to the Discount A/c (debit side total = discount allowed, credit side total = discount received).

PQ 2.1 · RTP 2022-May [4] (a) · Practical · --- · Pg 120 asked 3×	LEVEL II Application	Medium
PQ 2.2 · PYQ 2023-Dec [5] (c) · Practical · 5M · Pg 122 asked 10×	LEVEL II Application	Medium

Topic 3: Posting the Cash Book Entries

P1-C2-U2.5-T03

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §5.3: how debit-side and credit-side cash book columns are posted to the ledger and how discount columns are treated.

NOTES

Nature of columns: the cash columns of the cash book are actually the Cash Account and the bank column the Bank Account, so they need no separate ledger posting; the discount columns are only memorandum columns giving total discount allowed and total discount received.

Posting rule: from the DEBIT side of the cash book (receipts), credit the various accounts with their respective amounts including any discount allowed (e.g. cash ₹450 + discount ₹35 from Warsi posted in Warsi's account "By Cash ₹450 / By Discount ₹35" or "By Sundries ₹485"); from the CREDIT side (payments), debit the accounts named in the particulars column including discount received ("To Bank ₹330 / To Discount ₹20" or "To Sundries ₹350").

Discount totals: total of the discount column on the debit side is DEBITED to Discount Account (discount allowed); total of the discount column on the credit side is CREDITED to Discount Account (discount received).

Topic 4: Petty Cash Book

P1-C2-U2.5-T04

Read first Study Para 5.4: purpose of the Petty Cash Book, the imprest system (fixed float, periodic reimbursement equal to actual disbursements), its advantages, and posting via a journal entry debiting expense heads and crediting Petty Cash A/c.

NOTES

Purpose (Para 5.4): a firm appoints a “Petty Cashier” entrusted with small payments (telegrams, taxi fare, cartage, postage — say below ₹200) so the main cash book is not made unnecessarily heavy and the main cashier is not overburdened; an analytical book has one receipts column (cash comes only from the main cashier) and analysis columns for each type of payment (conveyance, cartage, stationery, postage, wages, sundries).

Imprest system: a definite fixed sum is entrusted to the petty cashier at the beginning of the period (week/fortnight) and he is reimbursed at the end for the payments made, so he again holds the fixed amount at the start of the new period; reimbursement only against a statement of total payments supported by VOUCHERS and limited to actual disbursements.

Safeguards: the fixed amount should suffice for likely small payments of a short period; vouchers filed in order; no payment without proper authorisation; payments above a specified limit only by the main cashier; the petty cashier receives no cash except for reimbursement.

Three advantages: (i) saving of time of the chief cashier; (ii) saving in labour in writing up the cash book and posting into the ledger; (iii) control over small payments.

Posting and nature of balance: Petty Cash A/c is debited when cash is handed over (Dr. Petty Cash / Cr. Cash) and credited periodically with total payments; the expense heads are debited either directly from the column totals or by one journal entry (Illustration 4: Dr. Conveyance ₹6.50, Cartage ₹9.50, Stationery ₹6, Postage ₹12, Wages ₹6, Repairs ₹15, General Expenses ₹5 / Cr. Petty Cash ₹60); the balance in the petty cashier's hands is an ASSET, shown in the balance sheet as part of the cash balance.

Remembering memorise · 1 question

- Definition: Petty Cash Book is the book maintained by the petty cashier to record small payments (postage, cartage, conveyance, etc.) out of a fixed imprest.
- Memorise the three advantages: (i) saving of the chief cashier's time, (ii) saving in labour in writing up the cash book and ledger posting, (iii) control over small payments --- asked for 3--5 marks.

- Remember the safeguards: payments only against vouchers, authorisation required, petty cashier receives no cash except reimbursement.

TQ 4.1 · PYQ 2022-May [6] (b) · Descriptive · 5M · Pg 124

LEVEL I
Remembering

Easy

Understanding explain with reasons · 1 question

- True/False traps: petty cash is NOT an expense --- the balance in the petty cash book represents an ASSET (cash in the petty cashier's hands, shown in the balance sheet as part of cash).
- Explain the imprest system: a fixed sum is advanced at the start of the period and only actual vouched payments are reimbursed, restoring the float.

TQ 4.2 · MTP 2024-Jul [1] (a) (i) {C} · True/False · 2M · Pg 125 asked 3×

LEVEL I
Understanding

Easy

Topic 5: Entries for Sale Through Credit/Debit Cards

P1-C2-U2.5-T05

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §5.5: the card-sale procedure and the two journal entries in the seller's books.

NOTES

Procedure: credit card is issued after verifying the customer's credibility (income sources) while debit card is issued to a customer having an account with the bank (ATM cards also work as debit cards); the seller submits the day's card slips to his bank, which credits the seller's account and debits the card-issuing bank/company; the issuing bank charges commission of 1% to 4% per transaction, immediately debited to the seller's bank account; a debit card debits the holder's account immediately, a credit card holder pays monthly in full or part (interest if not full).

Accounting: from the seller's view a card sale is equivalent to a CASH sale and bank commission is a selling expense — entries: (1) Dr. Bank A/c / Cr. Sales A/c (sales made through credit/debit card); (2) Dr. Commission A/c / Cr. Bank A/c (commission charged by bank).

Unit 2.6: Rectification of Errors

P1-C2-U2.6 · Importance B · Rank 1 in chapter · Category A · 37.8% of chapter questions · 34 questions

Topic 1: Introduction

P1-C2-U2.6-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.1: meaning of errors and their illustrative cases — wrong entry, wrong casting of subsidiary books, wrong cash-book casting.

NOTES

Errors: unintentional omission or commission of amounts and accounts in the process of recording transactions — committed while collecting financial data or while recording it, and arising from mathematical mistakes, mistakes in applying accounting policies, misinterpretation of facts, or oversight (intentional mistakes are fraud, not errors).

Trial balance link: if the trial balance does not tally there are definitely errors requiring rectification; but some errors do NOT affect the trial balance at all, yet may affect determination of profit or loss, assets and liabilities.

Illustrative cases: wrong entry (credit purchases ₹17,270 entered as ₹17,720 in Purchases Day Book), wrong casting of subsidiary books (credit sales ₹1,75,700 totalled and posted as ₹1,76,700), and wrong casting in the cash book leading to wrong balance c/d.

Topic 2: Stages of Errors

P1-C2-U2.6-T02

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.2: the errors possible at each of the four stages of the accounting process and the resulting four broad categories.

NOTES

Four stages: (i) recording in journal — errors of principle, omission, commission; (ii) posting in ledger — omission (partial/complete) and commission (wrong account, wrong side, wrong amount); (iii) balancing the ledger accounts — wrong totalling, wrong balancing; (iv) preparing the trial balance — omission, and commission (taking wrong account, wrong amount, wrong side).

Four broad categories: on this basis errors are classified as Errors of Principle, Errors of Omission, Errors of Commission and Compensating Errors.

Topic 3: Types of Errors

P1-C2-U2.6-T03

Read first Study Paras 6.1--6.3: the four categories of errors --- errors of principle, errors of omission (complete/partial), errors of commission and compensating errors --- plus the two-way classification into errors that do and do not affect the trial balance.

NOTES

Errors of principle (SM): "When a transaction is recorded in contravention of accounting principles, like treating the purchase of an asset as an expense, it is an error of principle" — e.g. on purchase of a computer the office expenses account is debited, or revenue expense treated as capital expenditure (or vice versa), or sale of a fixed asset treated as ordinary sale; the trial balance STILL agrees because amounts sit on the correct side, though in the wrong account.

Clerical errors — three types: (i) **Omission** — transaction completely or partially omitted (complete: entry left out of the subsidiary book altogether; partial: posting to the ledger omitted); (ii) **Commission** — amount posted in the wrong account, written on the wrong side, wrong totals (under/over-casting of a subsidiary book) or a wrong balance struck; (iii) **Compensating** — effects of errors cancel out, so the trial balance AGREES (e.g. ₹10 from A not credited to his account offset by the sales book total ₹10 in excess).

Errors that AFFECT the trial balance: wrong casting of subsidiary books; wrong balancing of an account; posting an amount on the wrong side; posting the wrong amount; omitting to post an amount or the totals of a subsidiary book; omitting cash book balances or an account balance from the trial balance; writing a balance in the wrong column; totalling the trial balance wrongly.

Errors that do NOT affect the trial balance: omitting an entry altogether from the subsidiary book (complete omission); making an entry with the WRONG AMOUNT in the subsidiary book; posting to a wrong account but on the correct side (amount due to be debited to A debited to B) — plus errors of principle and compensating errors, which also leave the trial balance in agreement.

Classification drill: wrong amount entered in subsidiary book → commission, TB agrees; day-book under/over-cast → commission, TB disagrees; transaction not recorded at all → complete omission, TB agrees; asset purchase debited to expenses (furniture to General Expenses) → principle, TB agrees; posting on wrong side or wrong balancing → commission, TB disagrees.

Understanding explain with reasons · 7 questions

- Definitions with True/False traps: compensating errors are errors whose effects cancel out, so the trial balance WILL agree (statement saying it 'will disagree' is False).
- Posting to a wrong account, posting on the wrong side, wrong totals or wrong balancing = errors of COMMISSION, not errors of principle (a repeated False statement).
- Error of principle = recording in contravention of accounting principles, e.g. furniture purchase debited to General Expenses A/c --- that is an error of PRINCIPLE, not omission; trial balance still agrees.

- Under/over-casting of a subsidiary book IS an error of commission (True) and it DOES affect the trial balance.

TQ 3.2 • PYQ 2019-Jun [1] (a) (ii) • True/False • 2M • Pg 131	LEVEL I Understanding	Easy
TQ 3.5 • PYQ 2023-Jun [1] (a) (iii) {C} • True/False • 2M • Pg 132	LEVEL I Understanding	Easy
TQ 3.7 • PYQ 2024-Jun [1] (a) (ii) {C} • True/False • 2M • Pg 133 asked 2×	LEVEL I Understanding	Easy
TQ 3.8 • PYQ 2026-Sep [1] (a) (ii) {C} • True/False • 2M • Pg 133	LEVEL I Understanding	Easy
TQ 3.1 • PYQ 2018-May [1] (a) (iii) {C} • True/False • 2M • Pg 130 asked 10×	LEVEL I Understanding	Medium
TQ 3.3 • RTP 2020-May [1] (iii) • True/False • --- • Pg 131 asked 2×	LEVEL I Understanding	Medium
TQ 3.4 • PYQ 2020-Nov [1] (a) (iv) {C} • True/False • 2M • Pg 131	LEVEL I Understanding	Medium

Analysis work through mixed data • 1 question

- Practise classifying a mixed list of 5--6 errors into omission / commission / principle (MTP pattern):
wrong amount in subsidiary book → commission; transaction not recorded at all → complete omission;
asset purchase treated as expense (or capital vs revenue mix-up) → principle.
- For each error, also analyse the second dimension: does it affect trial balance agreement? Memorise the SM lists --- casting/posting/balancing errors affect it; complete omission, wrong amount entered in subsidiary book, and posting to wrong account on the correct side do not.

TQ 3.6 • MTP 2023-Nov [6] (c) • Descriptive • 5M • Pg 132 asked 6×	LEVEL II Analysis	Medium
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Topic 4: Steps to Locate Errors

P1-C2-U2.6-T04

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.4: the eight-step search sequence when the trial balance disagrees.

NOTES

Steps (i)–(iv): re-total the two trial balance columns (and re-check derived lists such as the list of trade receivables); see that cash and bank balances are included; establish the exact difference — a balance equal to the difference may be omitted, and HALVE the difference — a balance equal to half may be on the wrong column; re-balance the ledger accounts.

Steps (v)–(viii): re-check castings of subsidiary books (especially if difference is ₹1, ₹100 etc.); if the difference is very big, compare account balances with the previous period and scrutinise material variations (e.g. Sales ₹32,53,000 vs ₹36,45,000 last year); check postings equal to the difference or half the difference (possibly omitted or posted on wrong side); if still unresolved, complete checking of all entries including the opening entry, preferably beginning with nominal accounts.

Topic 5: Rectification of Errors

P1-C2-U2.6-T05

Read first Study Paras 6.5.1--6.5.3: rectification at three stages --- before trial balance (one-sided errors via statements in the account, two-sided via journal entries), after trial balance using a Suspense Account, and in the next period through P&L Adjustment A/c.

NOTES

Three stages (Para 6.5): never correct by overwriting — rectify by (a) BEFORE trial balance: one-sided errors (and multi-account errors where a complete entry is impossible) are corrected by a rectification STATEMENT in the concerned account (e.g. “To Undercasting of Purchases Book ₹100” on the debit of Purchases A/c), while two-sided errors get normal journal entries; (b) AFTER trial balance but before final accounts: EVERY error is corrected by a complete journal entry, the unknown side taken to Suspense A/c; (c) in the NEXT period: through P&L Adjustment A/c — so neither “all errors need journal entries” nor “all errors go through Suspense” is true.

Suspense Account: the trial balance is artificially agreed by putting the difference to a Suspense A/c — debited if the credit column exceeds the debit column and vice versa; its opening balance therefore equals the difference in the trial balance; after all rectifications Suspense should close — a remaining balance proves errors are still undetected (Mr. W & H / Mr. A patterns).

Mechanical rules: posting on the WRONG SIDE → rectify with DOUBLE the amount (₹200 debited to Ram instead of credited → “By posting on the wrong side ₹400”; sale ₹200 credited to Singh & Co. → Dr. Singh & Co. ₹400 / Cr. Suspense); WRONG AMOUNT → rectify with the difference (₹51 posted as ₹15 → Dr. ₹36); day-book casting error → one-sided, via account statement or Suspense (sales book short ₹100: Dr. Suspense / Cr. Sales ₹100); discount column total unposted → Dr. Discount A/c / Cr. Suspense.

Classic pro-forma entries: purchase of asset through Purchases Book: Dr. Furniture(Asset) / Cr. Purchases; sale of old machinery through Sales Book: Dr. Sales / Cr. Machinery; purchase from Ram passed through Sales Book: Dr. Purchases AND Dr. Sales / Cr. Ram (double effect); credit sale through Purchases Book (Ramesh ₹120): Dr. Ramesh ₹240 / Cr. Purchases ₹120, Cr. Sales ₹120; receipt from Kamal credited to Krishan: Dr. Krishan / Cr. Kamal; drawings debited to expenses: Dr. Drawings / Cr. Trade Expenses; customer's return in Sales Day Book: Dr. Sales and Dr. Sales Returns / Cr. Suspense.

Next-period rectification (Para 6.5.3): correcting nominal accounts in the next year through ordinary accounts would falsify that year's P&L, so all amounts concerning expenses/incomes go through "Profit and Loss Adjustment Account" (Prior Period Items) — material income or expenses arising in the current period from errors/omissions of prior periods, disclosed separately and charged AFTER deriving current-year profit; capitalised items carry depreciation (scooter ₹3,000 debited to conveyance → Dr. Motor Vehicles ₹2,700, i.e. ₹3,000 less 10% depreciation / Cr. P&L Adjustment); closing balances of P&L Adjustment A/c and Suspense A/c are transferred to Capital A/c (Mr. Roy pattern).

Understanding explain with reasons · 2 questions

- True/False traps: NOT all errors are rectified through Suspense A/c after the trial balance --- two-sided errors use ordinary journal entries; and 'all errors are rectified by journal entries' is False, since one-sided errors found before the trial balance are corrected by a statement in the account itself.
- Know why the Suspense A/c opening balance equals the trial balance difference, and why next-period rectification of nominal accounts goes through P&L Adjustment A/c (Prior Period Items) to avoid falsifying current-year profit.

TQ 5.1 · PYQ 2022-Nov [1] (a) (iv) {C} · True/False · 2M · Pg 134 asked 2x	LEVEL I Understanding	Medium
TQ 5.2 · PYQ 2024-Jun [1] (a) (v) {C} · True/False · 2M · Pg 134 asked 2x	LEVEL I Understanding	Medium

Application work the problem · 3 questions

PQ 5.4 · RTP 2023-Dec [3] (a) · Practical · --- · Pg 139 asked 3x	LEVEL II Application	Medium
PQ 5.9 · PYQ 2021-Jul [2] (a) · Practical · 10M · Pg 147 asked 6x	LEVEL II Application	Hard
PQ 5.24 · PYQ 2026-Sep [2] (b) · Practical · 10M · Pg 173	LEVEL II Application	Hard

Analysis work through mixed data · 21 questions

- Master the classic patterns: purchase/sale passed through the wrong day book (double effect on Purchases and Sales); returns entered in the Sales Day Book; wrong-side posting (rectify with DOUBLE the amount); wrong amount (rectify with the difference); day-book casting errors (one-sided, via Suspense).
- Practise full 10--12 mark questions: rectification entries with Suspense A/c, preparing the Suspense A/c to find the original difference, and next-year corrections via P&L Adjustment A/c with depreciation on capitalised items (Mr. Roy/Miss Daisy pattern).
- Classify each item before drafting the entry: errors of principle change profit but not the trial balance; casting errors affect the trial balance only.

- Also practise redrafting a wrongly prepared trial balance with items on wrong sides (2025-Aug MTP pattern).

PQ 5.1 · PYQ 2018-May [1] (c) {C} · Practical · 4M · Pg 135 asked 3×	LEVEL II Analysis	Medium
PQ 5.3 · PYQ 2018-Nov [2] (a) · Practical · 5M · Pg 137 asked 5×	LEVEL II Analysis	Medium
PQ 5.5 · PYQ 2019-Jun [1] (c) · Practical · 4M · Pg 140	LEVEL II Analysis	Medium
PQ 5.7 · PYQ 2020-Nov [5] (a) · Practical · 5M · Pg 144 asked 4×	LEVEL II Analysis	Medium
PQ 5.10 · PYQ 2021-Dec [5] (a) · Practical · 5M · Pg 149 asked 2×	LEVEL II Analysis	Medium
PQ 5.13 · RTP 2023-Dec [4] (b) · Practical · --- · Pg 153 asked 2×	LEVEL II Analysis	Medium
PQ 5.14 · MTP 2024-Jun [1] (c) {C} · Practical · 4M · Pg 155 asked 2×	LEVEL II Analysis	Medium
PQ 5.16 · PYQ 2024-Sep [1] (c) {C} · Practical · 4M · Pg 158	LEVEL II Analysis	Medium
PQ 5.17 · MTP 2025-Apr S1 [5] (a) · Practical · 5M · Pg 159	LEVEL II Analysis	Medium
PQ 5.19 · MTP 2025-Aug S1 [5] (a) · Practical · 5M · Pg 163	LEVEL II Analysis	Medium
PQ 5.21 · RTP 2025-Sep [4] (b) · Practical · --- · Pg 167	LEVEL II Analysis	Medium
PQ 5.2 · PYQ 2018-May [6] (b) · Practical · 10M · Pg 136	LEVEL II Analysis	Hard
PQ 5.6 · PYQ 2019-Nov [2] (b) · Practical · 10M · Pg 141	LEVEL II Analysis	Hard
PQ 5.8 · PYQ 2021-Jan [2] (a) · Practical · 10M · Pg 145 asked 4×	LEVEL II Analysis	Hard
PQ 5.11 · RTP 2022-May [4] (b) · Practical · --- · Pg 150	LEVEL II Analysis	Hard
PQ 5.12 · MTP 2023-May [2] (a) · Practical · 10M · Pg 151 asked 2×	LEVEL II Analysis	Hard
PQ 5.15 · PYQ 2024-Jun [2] (a) · Practical · 12M · Pg 156	LEVEL II Analysis	Hard
PQ 5.18 · PYQ 2025-May [2] (a) · Practical · 10M · Pg 160 asked 5×	LEVEL II Analysis	Hard
PQ 5.20 · PYQ 2025-Sep [2] (b) · Practical · 12M · Pg 164 asked 2×	LEVEL II Analysis	Hard
PQ 5.22 · PYQ 2026-Jan [2] (a) · Practical · 12M · Pg 168	LEVEL II Analysis	Hard
PQ 5.23 · PYQ 2026-May [2] (b) · Practical · 10M · Pg 171	LEVEL II Analysis	Hard

CHAPTER 3

Bank Reconciliation Statement

7 Topics • 29 Classified Questions • Importance: B

ICAI SKILL PROFILE Level I 5–20% • Level II 80–95% — this chapter reads **almost entirely problem-solving**

 Level I — Remembering & Understanding **3.9%** 7 of 178 marks

 Level II — Application & Analysis **96.1%** 171 of 178 marks

Topic 1: Introduction

P1-C3-U3-T01

Read first Read the Introduction and Bank Pass Book sections of the ICAI Study Material: services rendered by a bank, what a pass book/bank statement is, and how the nature of balances differs between the customer's cash book and the bank's books.

NOTES

Services rendered by a bank: (i) discounts promissory notes/hundies for a small charge called discount, (ii) allows overdraft to good customers, (iii) grants loans (working capital, term loan), (iv) collects dividend warrants and interest on securities, (v) pays insurance premium, rent etc. on standing instructions, (vi) buys/sells shares, debentures and government securities, (vii) remits money at low cost, (viii) furnishes security or guarantee, (ix) issues letters of credit and travellers' cheques, (x) international banking — currency exchange, cross-country payments, export-import credit.

Bank pass book (SM): “Bank pass book is merely a copy of the customer's account in the books of a bank” — the bank's way of keeping the customer informed of entries; the customer must check entries and report errors; a stamped, signed year-end bank certificate of balance should be obtained.

Nature of pass book balance: Cr. balance as per pass book = deposit made by the customer; Dr. balance as per pass book = overdraft (customer owes the bank).

Mirror relationship: debit balance in the pass book represents credit balance in the cash book and vice-versa, because the business treats the bank as a debtor/trade receivable while the bank treats the business as a creditor/trade payable — so Dr. cash book balance = money at bank (favourable), while an overdraft is a Cr. balance per cash book and a Dr. balance per pass book.

Understanding explain with reasons · 1 question

- Be able to explain that a debit balance in the cash book means money at bank (favourable), while an overdraft appears as a credit balance in the cash book and a DEBIT balance in the pass book --- a classic True/False trap.
- Grasp the mirror relationship: the business treats the bank as a debtor, the bank treats the customer as a creditor, so cash book and pass book balances are equal but opposite in nature.
- Remember the pass book is merely a copy of the customer's account in the bank's books; Cr. balance per pass book = deposit, Dr. balance per pass book = overdraft.

TQ 1.1 · RTP 2025-May [1] (c) · True/False · 2M · Pg 178

LEVEL I
Understanding

Easy

Topic 2: Background

P1-C3-U3-T02

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2: how past frauds through manipulated bank/cash entries made reconciliation a part of internal control.

NOTES

Why reconcile: many corporate frauds have occurred through manipulating entries in bank statements or the cash book (e.g. presenting an incorrect bank balance to mislead stakeholders) — hence reconciliation of bank and cash balances became an integral part of internal control maintained by management; it checks for fraudulent activity and helps prevent financial statement errors.

Frequency: reconciliation is typically done at regular intervals such as monthly or quarterly as part of normal accounting procedure — the frequency largely depends on the size of the organisation and the number of transactions.

Topic 3: Bank Pass Book

P1-C3-U3-T03

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §3: nature and form of the pass book and the opposite nature of its balance versus the cash book.

NOTES

Meaning: the bank pass book is merely a copy of the customer's account in the books of the bank — the bank sends periodical statements or gives a pass book recording all deposits and withdrawals, keeping the customer informed of entries in his account; the customer must check entries and immediately inform the bank of any error (statements now also accessible via Net Banking/ATM passbook printers).

Form: columns — Transaction Period/Date · Particulars · Cheque No. · Withdrawals Dr.(₹) · Deposits Cr.(₹) · Balance Dr. or Cr.; business houses should also obtain a stamped and signed year-end certificate from the bank showing the balance carried.

Opposite nature: credit balance as per pass book = deposit of the customer, debit balance as per pass book = overdraft; debit balance in the pass book represents credit balance as per cash book and vice-versa, because the enterprise treats the bank as a debtor while the bank treats the enterprise as a creditor.

Topic 4: Bank Reconciliation Statement

P1-C3-U3-T04

Read first Study Section 4 of the chapter: meaning of reconciliation, the two records (bank column of cash book vs pass book/bank statement) and the purpose of a BRS --- it reconciles causes of difference, it does not itself compute the bank balance for the books.

NOTES

Two records: every banking transaction is recorded at two places — bank column of the cash book (customer's books) and the bank statement/pass book (bank's books); hence the two balances should be equal and opposite in nature (deposit of ₹1,00,000 → Dr. side of cash book, Cr. entry in pass book) but in practice differ due to timing, bank-originated transactions and errors.

BRS (SM): the statement which reconciles “the bank balance as per cash book with the balance as per the pass book by showing all the causes of difference” — its purpose is to explain/reconcile the causes of difference, NOT merely to arrive at the bank balance.

Nature: the BRS is only a statement, not an account or part of the double-entry system; reconciliation can proceed either way — arrive at pass book balance from cash book or at cash book balance from pass book.

Working method: classify each item as timing difference (cheque issued not presented, cheque deposited not cleared), transaction carried out by the bank itself, or error; work out its directional effect on the other book's balance, then add/subtract from the starting balance; if opening balances also differ, split unticked items between opening-balance and closing-balance reconciliation.

Understanding explain with reasons · 1 question

- Be ready to justify True/False statements: a BRS is prepared to explain/reconcile the causes of difference between cash book and pass book balances, NOT merely 'to arrive at the bank balance'.
- Explain why the two balances should be equal and opposite (same transactions recorded at two places) and why in practice they differ.
- Know that the BRS is a statement, not an account/part of the double-entry system.

TQ 4.1 · RTP 2024-Sep [1] (c) · True/False · --- · Pg 179 asked 6x

LEVEL I
Understanding**Easy****Analysis** work through mixed data · 1 question

- Practise full BRS problems starting from a Dr. balance as per cash book (e.g., ₹37,25,000 type questions), classifying each item as timing difference, bank- originated entry, or error before deciding add/subtract.
- Watch for cheques issued but not presented, cheques deposited but not cleared, and items recorded in only one book; work out each item's directional effect on the other book's balance.

PQ 4.1 · PYQ 2026-May [5] (a) (Or) (ii) · Practical · 5M · Pg 179

LEVEL II
Analysis**Medium****Topic 5: Importance of Bank Reconciliation Statement**

P1-C3-U3-T05

Read first Learn Section 5: the salient features/importance of BRS as an internal- control tool and the three causes of difference --- timing, transactions carried out by the bank itself, and errors --- with the standard list of individual items.

NOTES

Internal control: BRS is a very important tool for internal control of cash flows — it helps detect errors, frauds and irregularities, intentional or unintentional, in the cash book or pass book, making accountants careful in record-keeping.

Five salient features: (i) brings out any errors committed in the cash book or pass book; (ii) shows up any undue delay in the clearance of cheques; (iii) regular reconciliation discourages embezzlement (cashiers who entered cash in the cash book but never deposited it escaped only for lack of reconciliation); (iv) helps find the actual/true bank position by incorporating uncleared funds; (v) ensures accounting of all financial transactions of the year.

Three causes of difference: (1) Timing — same transaction recorded at two different times (cash book records a cheque on issue/deposit, pass book only on presentation/collection); (2) Transactions carried out by the bank itself without intimation — interest allowed/charged, bank charges, direct payments on standing instructions, direct deposits by customers, interest/dividends and bills collected, dishonour of a discounted bill; (3) Errors by bank or customer — omission,

incorrect amount, wrong side, wrong totalling/balancing, other party's transaction recorded.

Direction of items: cash book > pass book due to cheques deposited but not cleared, interest and expenses charged by bank, direct payments by the bank, dishonour of a bill discounted; cash book < pass book due to cheques issued but not presented, interest allowed by bank, interest/dividends collected, direct payment into the bank by a customer, bills collected by the bank.

Timing-table logic: cheques issued/deposited enter the cash book first (pass book only on presentation or collection); bank charges, interest, direct payments/collections and dishonours enter the pass book first — the customer records them only when the pass book entry comes into notice.

Remembering memorise · 1 question

- Memorise the salient features for a short note: (i) brings out errors in cash book/pass book, (ii) shows up undue delay in clearance of cheques, (iii) regular reconciliation discourages embezzlement by staff, (iv) reveals the true bank position, (v) ensures all transactions are accounted --- key points for 'importance of BRS to an industrial unit'.
- Learn the three broad causes of difference: timing differences, transactions by the bank without intimation (interest, charges, direct payments/receipts), and errors.

TQ 5.2 · RTP 2025-Jan [18] (iv) · Short Note · ---- · Pg 181 **asked 5x**

LEVEL I
Remembering

Easy

Understanding explain with reasons · 1 question

- For a 5-mark 'causes of difference' answer, be able to list and briefly explain: cheques issued but not presented, cheques deposited but not cleared, interest allowed/charged by bank, bank charges, direct payments by bank on standing instructions, direct deposits by customers, dividends/bills collected by bank, dishonour of discounted bills, and errors.
- Explain for each cause which book records first and why the gap arises (use the SM timing table).

TQ 5.1 · MTP 2024-Jul [6] (c) · Distinguish Between · 5M · Pg 181 **asked 4x**

LEVEL I
Understanding

Medium

Topic 6: Procedure for Reconciling the Cash Book Balance with the Pass Book Balance

P1-C3-U3-T06

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §6: the four possible starting balances and the add/subtract logic when causes are or are not given.

NOTES

Four starting points: Dr. balance as per cash book (= deposits/cash at bank = Cr. balance as per pass book) or Cr. balance as per cash book (= overdraft = Dr. balance as per pass book) — reconciliation may start from any of the four balances; problems come as reconciliation with or without adjusting the cash book, with causes given or not given.

When causes are given: if on account of a cause the balance of the OTHER book is more, ADD the amount; if less, SUBTRACT — e.g. starting from Dr. cash book balance, a cheque deposited but not yet cleared makes the pass book balance less, so subtract it; if starting from Dr. cash book balance the final figure is positive it is Cr. balance as per pass book, if negative it is Dr. balance as per pass book.

When causes are not given: compare debit entries of the cash book with credit entries of the pass book and vice-versa — unticked (non-tallying) entries are the causes of difference; also verify the opening balances tally, else divide unticked items between reconciliation of opening balance and of closing balance.

Topic 7: Methods of Bank Reconciliation

P1-C3-U3-T07

Read first Master Section 7: BRS without adjusting the cash book (starting from any of the four balances, using the add/subtract table) and BRS after preparing an adjusted/amended cash book, including the 'Balance' and 'Plus & Minus' presentations.

NOTES

Two methods: (1) BRS without preparing an adjusted cash book — start from any of the four balances (Dr./Cr. as per cash book, Dr./Cr. as per pass book) and apply the add/subtract table; (2) BRS after preparing an adjusted/amended cash book; either can be presented in 'Balance' form or columnar 'Plus & Minus' form (both column totals agree).

From Dr. (favourable) cash book balance: ADD cheques issued but not presented, cheques directly deposited by a customer, income/interest/dividends directly received and bills collected by bank, wrong credit in cash book or pass book, undercast of Dr. side, overcast of Cr. side; SUBTRACT cheques deposited but not cleared, expenses/bank charges/locker rent paid by bank, interest on overdraft charged, dishonours, wrong debits, overcast of Dr. side, undercast of Cr. side — every sign reverses for Cr. (overdraft) cash book or Dr. pass book starts; Cr. pass book start mirrors Cr. cash book columns.

Result sign: starting from Dr. cash book balance, a positive final figure = favourable Cr. balance as per pass book, a negative figure = unfavourable Dr. (overdraft) balance as per pass book; starting from Cr. cash book, positive = Dr. (overdraft) per pass book.

Adjusted cash book: correct the cash book for all errors (incorrect amount, entry posted twice, over/undercasting, wrong balance b/d) and omissions (bank charges, interest debited, direct receipts/payments, dishonour of cheques/bills); carry ONLY timing differences (cheques issued not presented, deposited not cleared) and bank/pass-book errors to the BRS — items adjusted in the cash book are not carried to the BRS again, and pass book errors are never adjusted in the cash book.

When compulsory: adjusting the cash book is optional for interim months but must be done when books are closed at the financial year-end so the balance sheet reflects the correct bank balance; the BRS then starts from the corrected (adjusted) cash book balance.

Application practise the procedure · 9 questions

- Practise the standard 4/5-mark BRS format starting from balance per cash book or per pass book, applying the add/subtract table for each of the four starting balances (Dr./Cr. cash book, Dr./Cr. pass book).
- Drill the sign logic: from Dr. cash book balance --- add cheques issued not presented, interest/dividends collected, direct deposits; subtract cheques deposited not cleared, bank charges, direct payments, dishonours.
- Remember: a positive result from Dr. cash book = Cr. (favourable) pass book balance; a negative result = Dr. (overdraft) pass book balance.

PQ 7.1 · RTP 2018-May [5] · Practical · --- · Pg 182 asked 3×	LEVEL II Application	Medium
PQ 7.6 · PYQ 2021-Jan [1] (c) {C} · Practical · 4M · Pg 189 asked 3×	LEVEL II Application	Medium
PQ 7.8 · PYQ 2021-Jul [2] (b) · Practical · 5M · Pg 192 asked 2×	LEVEL II Application	Medium
PQ 7.10 · MTP 2021-Nov [1] (c) · Practical · 4M · Pg 194 asked 3×	LEVEL II Application	Medium
PQ 7.12 · PYQ 2022-May [2] (c) · Practical · 5M · Pg 196 asked 3×	LEVEL II Application	Medium
PQ 7.14 · PYQ 2023-Jun [2] (b) · Practical · 5M · Pg 198	LEVEL II Application	Medium
PQ 7.16 · PYQ 2024-Jun [5] (b) (ii) · Practical · 5M · Pg 201	LEVEL II Application	Medium
PQ 7.24 · PYQ 2026-SEP 5 (a) (i) · Practical · 5M · Pg 214	LEVEL II Application	Medium
PQ 7.20 · PYQ 2025-Jan [2] (b) · Practical · 10M · Pg 206	LEVEL II Application	Hard

Analysis work through mixed data · 15 questions

- Practise overdraft-based and pass-book-based questions (10-mark PYQ pattern): overdraft per cash book or Dr. balance per pass book reverses every add/subtract --- this is the most common examiner twist.

- Work amended-cash-book problems: correct the cash book for errors and omissions (bank charges, interest, dishonours, direct receipts, entries posted twice, undercasting, wrong balance b/d), then carry ONLY timing differences and bank errors to the BRS.
- Handle tricky items: cheque recorded but not deposited, bank's wrong debit/credit for another customer, out-of-date cheques, part-presentation of a batch of cheques; also practise reverse working --- deriving the cash book balance from the pass book balance.

PQ 7.3 · PYQ 2018-Nov [4] (b) · Practical · 10M · Pg 185 asked 2×	LEVEL II Analysis	Medium
PQ 7.7 · RTP 2021-May [5] · Practical · --- · Pg 190 asked 2×	LEVEL II Analysis	Medium
PQ 7.13 · RTP 2022-May [5] · Practical · --- · Pg 197	LEVEL II Analysis	Medium
PQ 7.15 · PYQ 2023-Dec [2] (a) · Practical · 8M · Pg 199 asked 3×	LEVEL II Analysis	Medium
PQ 7.22 · PYQ 2025-Sep [5] (a) (i) · Practical · 5M · Pg 211	LEVEL II Analysis	Medium
PQ 7.23 · PYQ 2026-Jan [5] (a) (i) · Practical · 5M · Pg 212	LEVEL II Analysis	Medium
PQ 7.2 · PYQ 2018-May [6] (a) · Practical · 10M · Pg 184 asked 2×	LEVEL II Analysis	Hard
PQ 7.4 · PYQ 2019-Nov [2] (a) · Practical · 10M · Pg 186 asked 9×	LEVEL II Analysis	Hard
PQ 7.5 · PYQ 2020-Nov [2] (a) · Practical · 10M · Pg 188	LEVEL II Analysis	Hard
PQ 7.9 · PYQ 2022-Nov [2] (a) · Practical · 15M · Pg 192 asked 5×	LEVEL II Analysis	Hard
PQ 7.11 · PYQ 2021-Dec [2] (c) · Practical · 10M · Pg 195 asked 3×	LEVEL II Analysis	Hard
PQ 7.17 · MTP 2024-Jul [5] (a) · Practical · 10M · Pg 202 asked 2×	LEVEL II Analysis	Hard
PQ 7.18 · MTP 2024-Aug [2] (b) · Practical · 10M · Pg 203 asked 2×	LEVEL II Analysis	Hard
PQ 7.19 · PYQ 2024-Sep [2] (a) · Practical · 10M · Pg 204	LEVEL II Analysis	Hard
PQ 7.21 · PYQ 2025-May [2] (b) · Practical · 10M · Pg 209 asked 5×	LEVEL II Analysis	Hard

CHAPTER 4

Inventories

6 Topics • 23 Classified Questions • Importance: A

ICAI SKILL PROFILE Level I 5–20% • Level II 80–95% — this chapter reads **theory-heavy**Level I — Remembering & Understanding **26.2%** 24.5 of 93.5 marksLevel II — Application & Analysis **73.8%** 69 of 93.5 marks

Topic 1: Meaning

P1-C4-U4-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §1: the three-limb definition of inventory and the composition of inventory for trading, manufacturing and construction concerns.

NOTES

Definition: inventory can be defined as assets held (i) for sale in the ordinary course of business, or (ii) in the process of production for such sale, or (iii) for consumption in the production of goods or services for sale, including maintenance supplies and consumables other than machinery spares, servicing equipment and standby equipment.

Types by business: trading concern — products purchased for resale in existing form plus supplies (wrapping paper, cartons, stationery); manufacturing concern — raw material, work-in-process, finished products, plus maintenance supplies, consumables, loose tools and spare parts; construction business — projects under construction; EXCLUDED are machinery spares/servicing/standby equipment usable only with a fixed asset item whose use is expected to be irregular — accounted for as fixed assets.

Year-end relevance: every entity must ascertain closing inventory (raw material, WIP, finished goods, consumables) — its value is put on the credit side of the Trading Account and the asset side of the Balance Sheet, so the accountant must know it before preparing final accounts.

Topic 2: Inventory Valuation

P1-C4-U4-T02

Read first Read Section 2 of the Inventories chapter: significance of inventory valuation for income determination ($\text{COGS} = \text{Opening inventory} + \text{Purchases} + \text{Direct expenses} - \text{Closing inventory}$), financial

position, liquidity analysis and statutory compliance.

NOTES

Income determination: Cost of goods sold = Opening inventory + Purchases + Direct expenses – Closing inventory; the effect of any inventory misstatement on net income is always through COGS — higher closing inventory lowers COGS and raises profit.

Over/under-statement table: closing inventory overstated → net income OVERSTATED; closing inventory understated → income understated; opening inventory overstated → income understated; opening inventory understated → income overstated.

Why valuation matters: (i) Determination of true income — COGS matched with revenue of the period; (ii) Ascertainment of financial position — inventory is a current asset, wrong value means balance sheet does not disclose truthful position (slow/non-moving stock a key symptom); (iii) Liquidity analysis — inventory is part of net working capital and significantly affects the current ratio relied on by bankers; (iv) Statutory compliance — Schedule III, Companies Act 2013 and Accounting Standards require disclosure of accounting policies/cost formula and total carrying amount classified as raw materials, WIP, finished goods, stock-in-trade, stores, spares and loose tools.

Understanding explain with reasons · 1 question

- Master the over/under-statement table for True/False questions: closing inventory overstated → net income OVERSTATED (so 'overstated closing inventory understates income' is False); opening inventory overstated → income understated.
- Be able to reason through COGS: higher closing inventory lowers cost of goods sold and raises profit --- the effect of any misstatement flows through COGS.
- Explain why correct valuation matters: true income, truthful balance sheet position, and current-ratio/liquidity analysis.

TQ 2.1 · RTP 2025-Jan [1] (iv) · True/False · ---- · Pg 218 asked 2x

LEVEL I
Understanding

Easy

Topic 3: Basis of Inventory Valuation

P1-C4-U4-T03

Read first Study Section 3: valuation at lower of cost or net realizable value (Principle of Conservatism), components of cost (purchase cost, conversion cost, other costs), the four exclusions from cost, and the meaning of NRV.

NOTES

Basis: inventories are valued at the LOWER of cost or net realizable value — Principle of Conservatism: any loss from a fall in selling price below cost is recognised immediately, gains only when realised; write-down is usually on an item-by-item basis (groups only for interchangeable items).

Cost (AS): comprises all costs of purchase + costs of conversion + other costs incurred in bringing the inventories to their present location and condition; purchase cost = price incl. non-recoverable duties/taxes + freight inwards + directly attributable expenditure LESS trade discounts, rebates and duty drawbacks — recoverable GST credit is excluded (100 units @ ₹100 + 18% GST → cost ₹10,000, not ₹11,800); conversion = direct labour + systematic allocation of fixed and variable production overheads; interest/borrowing costs generally excluded except long-production goods (wine, rice, timber).

Four exclusions from cost: (a) abnormal amounts of wasted materials, labour or overheads (normal wastage IS included); (b) storage costs, unless necessary in the production process prior to a further production stage (wine fermentation storage IS cost, finished-goods warehouse rent is NOT); (c) administrative overheads not contributing to location/condition; (d) selling and distribution costs.

NRV (SM): “the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale”; for WIP also deduct conversion costs still to be incurred; for raw materials, replacement cost is generally considered NRV; assessment is made at each balance sheet date.

Adjusted-profit drill: for every scrutiny item trace the twin effect — on purchases/COGS AND on closing inventory — before restating net profit (e.g. capital expenditure wrongly in purchases, goods invoiced in March but excluded from stock, goods in transit, free samples, goods on approval wrongly booked as sales).

Understanding explain with reasons · 4 questions

- True/False staples: inventories are valued at cost or NRV whichever is LOWER (never higher) --- based on the Principle of Conservatism (prudence).
- Cost of inventories comprises ALL costs of purchase + costs of conversion + other costs incurred in bringing inventories to their present location and condition; recoverable taxes (GST credit), trade discounts and rebates are deducted.
- Know the exclusions and be ready to justify: warehouse/storage rent for finished goods is NOT inventory cost (unless storage is necessary in the production process, e.g. wine); also excluded are abnormal wastage, general administrative overheads, and selling & distribution costs.
- NRV = estimated selling price less estimated costs of completion and costs necessary to make the sale; for raw materials, replacement cost is generally taken.

TQ 3.2 · MTP 2024-Jul [1] (a) (ii) {C} · True/False · 2M · Pg 219	asked 5×	LEVEL I Understanding	Easy
TQ 3.3 · PYQ 2024-Sep [1] (a) (iii) {C} · True/False · 2M · Pg 219	asked 2×	LEVEL I Understanding	Easy
TQ 3.4 · PYQ 2026-May [1] (a) (i) {C} · True/False · 2M · Pg 220	asked 2×	LEVEL I Understanding	Easy

Analysis work through mixed data · 1 question

- Practise adjusted-net-profit problems: recompute profit after correcting purchases/closing inventory for wrongly capitalised items, goods in transit, unrecorded purchases and wrongly valued stock (5-mark PYQ pattern).
- For each error, trace the double effect --- on closing inventory value AND on purchases/COGS --- before adjusting the net profit of ₹15,00,000-type figures.

PQ 3.1 · PYQ 2026-May [5] (a) (i) · Practical · 5M · Pg 220

LEVEL II
Analysis

Medium

Topic 4: Inventory Record Systems

P1-C4-U4-T04

Read first Learn Section 4: Periodic (physical) Inventory System vs Perpetual Inventory System --- how each determines COGS/closing inventory, and the 7-point distinction table.

NOTES

Periodic (physical) inventory system: ascertains inventory by an actual physical count/measure/weight of all items on hand at a particular date; $\text{COGS} = \text{Opening inventory} + \text{Purchases} - \text{Closing inventory (residual figure)}$; simple and cheap, suits small enterprises, but needs closure of business, hides pilferage/loss in COGS and permits no inventory control.

Perpetual inventory system: records balances after each receipt and issue through an inventory ledger on a continuous basis; cost of goods issued is directly determined and closing inventory is the residual/balancing figure; physical inventory should still be checked against recorded balances; overcomes periodic limitations but is costlier; the two systems are complementary, not mutually exclusive.

Based on physical verification	Based on book records
Information about inventory and COGS at a particular date	Continuous information about inventory and cost of sales
Determines inventory; COGS is the residual figure	Determines COGS directly; inventory is the balancing figure

COGS includes loss of goods (goods not in stock assumed sold)	Closing inventory includes loss of goods (all unsold assumed in stock)
Inventory control not possible	Inventory control can be exercised
Simple and less expensive	Costlier method
Requires closure of business for counting	Inventory determined without affecting operations

Understanding explain with reasons • 2 questions

- True: periodic inventory system ascertains inventory by an actual physical count at a particular date; COGS is the residual figure (Opening + Purchases – Closing counted).
- Perpetual system records balances after each receipt and issue through an inventory ledger; COGS is directly determined and closing inventory is the balancing figure.
- For the 5-mark distinction question, learn the table: basis (physical verification vs book records), information (periodic date vs continuous), residual figure (COGS vs closing stock), treatment of lost goods, inventory control possible only under perpetual, cost (cheap/simple vs costlier), and closure of business needed only for periodic.

TQ 4.1 • PYQ 2022-Nov [1] (a) (ii) {C} • True/False • 2M • Pg 221 **asked 3×** **LEVEL I**
Understanding

Easy

TQ 4.2 • PYQ 2024-Sep [6] (b) • Distinguish Between • 5M • Pg 222
asked 6×

LEVEL I
Understanding

Medium

Topic 5: Formulae/Methods to Determine Cost of Inventory

P1-C4-U4-T05

Read first Study Section 5: historical cost formulas --- Specific Identification, FIFO, LIFO, Simple and Weighted Average Price --- and non-historical methods (Adjusted Selling Price/retail method, Standard Cost), including their assumptions.

NOTES

Principal methods: historical cost — Specific Identification (for items not ordinarily interchangeable and of high value, e.g. expensive medical equipment; actual cost of each identified lot), FIFO and Weighted Average Price (both permitted by Accounting Standards), LIFO and Simple Average (not preferred/not permitted); non-historical — Adjusted Selling Price (retail) and Standard Cost (used where prices change frequently, e.g. crude oil).

FIFO vs LIFO: FIFO assumes earliest lots are issued first, so closing inventory consists of the latest consignments valued at latest prices (a cost-flow assumption only, not physical flow); LIFO charges

the latest costs to issues (matching current cost with current revenue), leaving closing inventory at earliest prices — LIFO “is based on an irrational assumption”, gives different results under periodic vs perpetual records, and is not permitted by Accounting Standards.

Inflation logic: under rising prices FIFO gives the LOWEST cost of goods sold (issues at older, cheaper prices) and the highest closing inventory and reported profit; LIFO does the opposite (500 @ ₹50 then 500 @ ₹60, issue 500: FIFO stock ₹30,000, LIFO ₹25,000, simple average ₹27,500).

Average price methods: Simple average = sum of prices ÷ number of prices (ignores quantities; periodic use only); **Weighted average:** rate = total cost of goods available for sale ÷ total units available; closing inventory = units in hand × WAP; under perpetual records a NEW average rate is computed after every fresh purchase and the next issue is priced at it; under periodic records one average for the whole period.

Stores ledger drill: prepare receipts–issues–balance columns and value each issue by the chosen formula, e.g. purchases 100 @ ₹30 and 200 @ ₹40 with issues of 250 units leave 50 units: FIFO closing stock 50 @ ₹40 = ₹2,000; weighted average (rate ₹38 after second purchase) = 50 @ ₹38 = ₹1,900.

Remembering memorise · 2 questions

- Short-note points on FIFO vs LIFO: FIFO assumes earliest lots are issued first so closing inventory is at latest prices; LIFO charges latest costs to issues so closing inventory is at earliest prices; LIFO rests on an irrational assumption and is not permitted by Accounting Standards.
- Principal methods of ascertaining cost: Specific Identification, FIFO, Weighted Average Price (permitted); LIFO and Simple Average (not preferred/permitted); non-historical: Adjusted Selling Price and Standard Cost.
- Adjusted Selling Price (retail) method: cost = selling value of inventory less an appropriate percentage of gross margin; used in retail where individual costs are not readily ascertainable.

TQ 5.1 · MTP 2023-May [6] (c) (iv) · Short Note · 2.5M · Pg 223

LEVEL I
Remembering

Easy

TQ 5.2 · MTP 2024-Aug [6] (c) · Short Note · 5M · Pg 223 **asked 4x**

LEVEL I
Remembering

Medium

Understanding explain with reasons · 1 question

- Inflation logic for True/False: under rising prices FIFO gives the LOWEST cost of goods sold (issues at older, cheaper prices) and the highest closing inventory and profit; LIFO does the opposite.

TQ 5.3 · PYQ 2025-Jan [1] (a) (iii) {C} · True/False · 2M · Pg 224

LEVEL I
Understanding

Medium

Application practise the procedure · 1 question

- Practise preparing a stores/stock ledger for FIFO (and weighted average) from dated opening inventory, purchases and issues --- e.g. 100 units @ ₹15, 300 @ ₹18, issues of 250 units --- valuing closing inventory correctly.
- Under weighted average (perpetual), recompute the average rate after every fresh purchase: total cost of goods available ÷ total units available.

PQ 5.1 · PYQ 2025-Jan [5] (Or) (b) (i) · Practical · 5M · Pg 224 asked 5x

LEVEL II
Application**Medium****Topic 6: Inventories Taking**

P1-C4-U4-T06

Read first Master Section 6: rolling back/forward a physical count taken before or after year-end (adjusting purchases, sales at cost using GP margin, returns), plus treatment of goods on sale-or-return, goods on consignment, and slow-moving/damaged items at NRV.

NOTES

Roll-back (count AFTER year-end): Stock at year-end = Stock on count date – purchases during the interval (only goods actually received) + cost of sales in the interval (Net sales × 100/(100 + markup on cost)) + sales returns at cost; e.g. ₹7,85,000 – ₹1,53,000 + ₹2,50,000 × 100/125 = ₹8,32,000;
margin conversion: 33.33% on cost = 25% on sales, 25% on cost = 20% on sales.

Count BEFORE year-end (e.g. 23rd June for 30th June): reverse the direction — ADD purchases (and goods in transit) and DEDUCT cost of sales for the intervening period from the counted stock.

GP-based ascertainment: Closing inventory = Opening stock + Purchases + Manufacturing expenses – Cost of goods sold (Sales – Gross profit); selling, administrative and financial expenses are EXCLUDED from inventory cost; strip abnormal items first — take them out of sales and carry opening stock at written-down value, applying the normal GP rate only to normal sales.

Sale-or-return and consignment: goods with customers pending approval are NOT sales — include at cost (selling value × 100/(100+markup)) and remove from sales; consignment inward stock belongs to the consignor (consignee excludes it); the consignor includes unsold consignment-outward stock at cost.

NRV adjustments: very old/slow-moving items and goods refused by customers are taken at their expected realizable value, not cost (cost ₹11,250 taken at ₹5,250; flood-delayed goods cost ₹15,500 at NRV ₹12,500) — every adjustment is finally tested at cost or NRV whichever is lower.

Application practise the procedure · 3 questions

- Practise the roll-back format: Stock on count date – purchases after year-end + cost of sales after year-end (Sales × 100/(100+markup)) ± returns = Stock at year-end; convert margins carefully (33.33% on cost = 25% on sales).

- Adjusted selling price computation: $\text{GP rate} = \frac{\text{Gross margin}}{(\text{Sales} + \text{closing inventory at selling price})}$; cost of closing stock = selling price of stock less GP rate.
- Ascertain closing inventory from $\text{Opening stock} + \text{Purchases} + \text{Manufacturing expenses} - \text{COGS (sales less GP)}$, EXCLUDING selling, administrative and financial expenses from inventory cost.

PQ 6.8 · PYQ 2021-Jul [2] (c) · Practical · 5M · Pg 236 asked 3×	LEVEL II Application	Medium
PQ 6.10 · PYQ 2025-Sep [6] (b) · Practical · 5M · Pg 238 asked 6×	LEVEL II Application	Medium
PQ 6.11 · PYQ 2026-Sep [5] (a) (Or) (ii) · Practical · 5M · Pg 239	LEVEL II Application	Medium

Analysis work through mixed data · 8 questions

- Work multi-adjustment problems: goods sent on approval (include unapproved goods at cost, remove from sales), consignment inward stock (belongs to consignor --- exclude; consignment outward unsold stock --- include at cost), goods in transit, and abnormal/slow-moving items written down to NRV.
- In adjusted-profit questions (₹5,75,000/₹32,00,000 pattern), trace each scrutiny item's twin effect on purchases/sales and on closing stock before restating net profit.
- When count date falls BEFORE year-end (e.g. 23rd June for 30th June), reverse the direction: add purchases and deduct cost of sales for the intervening period.

PQ 6.1 · PYQ 2019-Jun [6] (c) · Practical · 5M · Pg 227 asked 3×	LEVEL II Analysis	Medium
PQ 6.2 · PYQ 2023-Jun [2] (c) · Practical · 5M · Pg 228 asked 3×	LEVEL II Analysis	Medium
PQ 6.3 · RTP 2023-Dec [6] · Practical · --- · Pg 229 asked 5×	LEVEL II Analysis	Medium
PQ 6.5 · PYQ 2024-Jun [5] (a) · Practical · 5M · Pg 231 asked 2×	LEVEL II Analysis	Medium
PQ 6.6 · PYQ 2024-Sep [5] (a) · Practical · 5M · Pg 233 asked 4×	LEVEL II Analysis	Medium
PQ 6.9 · PYQ 2025-May [1] (c) {C} · Practical · 4M · Pg 237 asked 4×	LEVEL II Analysis	Medium
PQ 6.4 · MTP 2024-May [2] (a) · Practical · 10M · Pg 230 asked 4×	LEVEL II Analysis	Hard
PQ 6.7 · MTP 2025-Jan S2 [2] (a) · Practical · 10M · Pg 235 asked 9×	LEVEL II Analysis	Hard

CHAPTER 5

Depreciation and Amortisation

9 Topics · 40 Classified Questions · Importance: B

ICAI SKILL PROFILE Level I 5–20% · Level II 80–95% — this chapter reads **in line with the paper**

 Level I — Remembering & Understanding **12.9%** 29 of 224 marks

 Level II — Application & Analysis **87.1%** 195 of 224 marks

Topic 1: Introduction

P1-C5-U5-T01

Read first Read the 'Introduction' section of Chapter 5 (Depreciation and Amortisation): concept of depreciation, Schedule II (Companies Act, 2013) definition, causes of decrease in asset value, component-wise depreciation, and the four objectives of providing depreciation.

NOTES

Schedule II (Companies Act, 2013): “Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life” — depreciable amount = cost (or revalued amount substituted for cost) less residual value; useful life = period the asset is expected to be available for use, or number of production or similar units expected from it.

Causes of decrease in value: (1) wear and tear from use, (2) efflux of time (even when not used), (3) obsolescence from technological or other changes, (4) decrease in market value, (5) depletion (mines and natural reserves); depreciation begins when the asset is AVAILABLE for use, not only when actually used — hence a non-depreciating idle asset is a myth, but land (indefinite life) is not depreciated.

Nature: a non-cash operating expense and charge against profit — no cash outflow, yet it must be provided even in a loss year; follows the matching principle: expired cost (depreciation) to P&L, unexpired cost (WDV) to Balance Sheet; charging it also reduces distributable profits, keeping funds available for replacement.

Component depreciation: each part whose cost is significant to the item's total cost AND whose useful life/method differs must be depreciated separately (aircraft: airframe, engines, interiors); parts with same life and method may be grouped.

Four objectives: (1) correct income measurement, (2) true position statement — asset shown at unexpired cost, (3) funds for replacement, (4) ascertainment of true cost of production.

Understanding explain with reasons · 4 questions

- Be able to justify True/False: depreciation is a NON-CASH expense (no cash outflow), but it IS an operating expense and a charge against profit --- it must be provided even in a loss year, since it arises from use/efflux of time, not from profitability.
- Explain why land is NOT a depreciable asset: it has an indefinite useful life and its value does not decline with use or passage of time.
- Reason from the definition: depreciation is the systematic allocation of depreciable amount (cost less residual value) over useful life, and follows the matching principle --- expired cost to P&L, unexpired cost (WDV) to Balance Sheet.
- Remember for reasoning: depreciation begins when the asset is AVAILABLE for use, not when actually used; obsolescence and wear-and-tear occur even without use.

TQ 1.1 · PYQ 2018-Nov [1] (a) (ii) {C} · True/False · 2M · Pg 243	asked 4x	LEVEL I Understanding	Easy
TQ 1.3 · PYQ 2025-Sep [1] (a) (iv) {C} · True/False · 2M · Pg 243	asked 3x	LEVEL I Understanding	Easy
TQ 1.4 · RTP 2025-Sep [1] (e) · True/False · 2M · Pg 244		LEVEL I Understanding	Easy
TQ 1.2 · PYQ 2023-Dec [1] (a) (iii) {C} · True/False · 2M · Pg 243		LEVEL I Understanding	Medium

Topic 2: Factors in the Measurement of Depreciation

P1-C5-U5-T02

Read first Study the section 'Factors in the Measurement of Depreciation': cost of asset, estimated useful life, estimated residual/scrap value, depreciable amount, and the elements of cost of Property, Plant and Equipment with directly attributable costs and exclusions.

NOTES

Three factors: (1) cost of asset including installation, commissioning and trial-run expenses, (2) estimated useful life (in time or production units), (3) estimated scrap/residual value at end of useful life (regarded as nil if insignificant).

Depreciable amount: historical cost (or revalued amount) less estimated residual value; e.g. machinery ₹1,10,000 – residual ₹10,000 = ₹1,00,000 over 5 years → depreciation ₹20,000 p.a.

Cost of PPE: purchase price (including non-refundable import duties and purchase taxes, after deducting trade discounts and rebates) + costs directly attributable to bringing the asset to the location and condition for intended use + initial estimate of dismantling, removal and site-restoration costs.

Directly attributable (capitalise): (a) employee benefits arising directly from acquisition/construction, (b) site preparation, (c) initial delivery and handling, (d) installation and

assembly, (e) testing costs net of proceeds from selling test samples, (f) professional fees (e.g. engineers).

NOT capitalised: opening/inauguration costs of a new facility, cost of introducing a new product (advertisement/promotion), cost of a new location or customer class (incl. staff training), administration and general overheads, relocation costs; once ready for intended use, no further cost is capitalised even if the asset is idle or under-used, unless a major repair/addition extends life or capacity.

Remembering memorise • 1 question

- Memorise the 3 factors for calculating depreciation: (1) cost of asset (including installation, commissioning, trial run), (2) estimated useful life (in time or production units), (3) estimated scrap/residual value at end of useful life.
- Definition: Depreciable amount = historical cost (or revalued amount) less estimated residual value; Useful life = period of expected use OR number of production units expected.
- Cost of PPE = purchase price (incl. non-refundable duties/taxes, less trade discounts) + directly attributable costs + initial estimate of dismantling/site- restoration costs.

TQ 2.1 • PYQ 2020-Nov [6] (c) • Descriptive • 5M • Pg 244 **asked 2x**

LEVEL I
Remembering

Medium

Understanding explain with reasons • 1 question

- Be ready to give five examples of directly attributable costs: employee benefits from acquisition/construction, site preparation, initial delivery and handling, installation and assembly, testing costs (net of sale of test samples), professional fees (e.g. engineers).
- Explain what is NOT capitalised: inauguration/opening costs, cost of introducing new product (advertisement), cost of new location/customer class (staff training), administration and general overheads, relocation costs.

TQ 2.2 • PYQ 2022-Nov [6] (b) • Descriptive • 5M • Pg 245 **asked 2x**

LEVEL I
Understanding

Medium

Topic 3: Methods for Providing Depreciation

P1-C5-U5-T03

Read first Study all six methods --- Straight Line, Reducing/Diminishing Balance (WDV), Sum of Years' Digits, Machine Hour, Production Units and Depletion --- with their formulas, assumptions, merits/demerits and Illustrations 1--6.

NOTES

SLM (Fixed Instalment): Depreciation = (Cost of asset – Scrap value) ÷ Useful life; Rate = SLM depreciation ÷ Cost × 100; equal yearly charge assuming equal utility; simple, accurate for leases and plant; charge proportionately for part-year use (asset bought 1 July, 10% on ₹15,00,000 → 6-month charge ₹75,000).

WDV / Reducing (Diminishing) Balance: fixed percentage on opening WDV; Rate = $[1 - \sqrt[n]{\text{Residual value} \div \text{Cost}}] \times 100$; charge decreases yearly while repairs rise with age, so depreciation + repairs gives an almost equal burden every year; asset value is never completely extinguished; prescribed by Income-tax Rules (except power generation/distribution undertakings).

Sum of Years' Digits (accelerated): depreciation = (Cost – Scrap) × remaining life including current year ÷ $[n(n+1) \div 2]$; for 10-year life total digits = 55, so year 1 = 10/55, year 2 = 9/55 — higher charge in early years, a variation of the reducing balance idea.

Machine Hour, Production Units, Depletion: hour rate = (Cost – Scrap) ÷ total estimated machine hours, annual charge = hours worked × rate — an hourly variant of SLM which Schedule II echoes via extra-shift depreciation; Production Units = Depreciable amount × production during period ÷ estimated total production; Depletion (mines/quarries) rate = cost ÷ estimated total quantity, charge = quantity extracted × rate (quarry lease ₹1,00,00,000, 2,00,000 tonnes → 2,000 tonnes = ₹1,00,000).

Pro-forma entries (two alternatives): (i) asset kept at cost — Dr. Depreciation / Cr. Provision for Depreciation (Accumulated Depreciation); (ii) Dr. Depreciation / Cr. Asset; under both, close by Dr. Profit and Loss / Cr. Depreciation.

Remembering memorise · 2 questions

- Machine Hour Rate method: depreciation per hour = (Cost – Scrap)/Total estimated machine hours; annual charge = hours worked × rate; a variation of SLM computed per hour instead of per year; Schedule II recognises it via extra shift depreciation.
- Formulas: SLM depreciation = (Cost – Scrap)/Useful life; WDV rate = $[1 - \sqrt[n]{\text{Residual}/\text{Cost}}] \times 100$; SYD fraction = remaining life (incl. current year)/ $[n(n+1)/2]$; Depletion = (Quantity extracted/Total estimated quantity) × cost.

TQ 3.4 · RTP 2024-Sep [18] (iv) · Short Note · --- · Pg 247 **asked 5x**

LEVEL I
Remembering

Easy

TQ 3.5 · RTP 2026-May [18] (4) · Short Note · --- · Pg 247

LEVEL I
Remembering

Easy

Understanding explain with reasons · 3 questions

- True/False trap: SYD IS an accelerated method --- higher depreciation in early years, lower in later years (statement that accelerated methods give less in early years is FALSE).
- Explain Diminishing Balance Method: fixed percentage on opening WDV; charge decreases yearly; asset value never fully extinguished; used where repairs rise with age.

- Reason why WDV gives uniform total burden: depreciation falls as repairs/maintenance rise, so depreciation + repairs stays roughly equal each year (this statement is TRUE).

TQ 3.1 · PYQ 2023-Dec [1] (a) (iv) {C} · True/False · 2M · Pg 245	LEVEL I Understanding	Easy
TQ 3.2 · PYQ 2023-Dec [1] (b) (ii) {C} · Descriptive · 1M · Pg 246	LEVEL I Understanding	Easy
TQ 3.3 · MTP 2024-Apr [1] (a) (iii) {C} · True/False · 2M · Pg 246 asked 6x	LEVEL I Understanding	Easy

Application practise the procedure · 2 questions

- Practise Annuity method on leases: depreciation = cost × annuity factor; interest credited on opening balance each year.
- Practise Depletion method for mines/quarries: rate per tonne = cost/total estimated deposit; depreciation = tonnes extracted × rate (e.g. ₹2,00,00,000 lease, 4,00,000 tonnes).
- Practise Machinery A/c with SLM/WDV including part-year depreciation from purchase/erection date and sale of obsolete machine mid-year.

PQ 3.2 · RTP 2025-Sep [7] · Practical · --- · Pg 250	LEVEL II Application	Medium
PQ 3.1 · MTP 2022-Nov [2] S2 (a) · Practical · 10M · Pg 248 asked 3x	LEVEL II Application	Hard

Topic 4: Profit or Loss on The Sale/Disposal of Property, Plant and Equipment

P1-C5-U5-T04

Read first Study the section on profit/loss on sale of PPE and Illustrations 7--9: charging depreciation up to date of sale, computing WDV, transfer to P&L, and the two presentations --- with and without Provision for Depreciation Account, plus Machinery Disposal Account.

NOTES

Rule: charge depreciation for the period the asset was used in the year of sale; profit/loss = sale proceeds (or insurance claim) – WDV on date of sale, transferred to P&L; a gain on disposal is a capital profit credited to P&L, not part of revenue/turnover.

Worked logic (SM): book value 1-1-2022 ₹50,00,000, less 6 months' depreciation @ 10% ₹2,50,000 → WDV 1-7-2022 ₹47,50,000; sold ₹32,00,000 → loss ₹15,50,000 to P&L.

Provision for Depreciation version: Machinery A/c stays at original cost; on sale — transfer cost to Machinery Disposal A/c, transfer accumulated depreciation (Dr. Provision for Depreciation / Cr. Machinery Disposal), credit sale proceeds; balance of Disposal A/c = profit/loss to P&L.

Working-note discipline: compute machine-wise cost, yearly depreciation and WDV; capitalise

erection/installation and repair/reconditioning of second-hand machines (Illus. 9: ₹3,00,000 + ₹60,000 repairs + ₹40,000 installation = ₹4,00,000 cost); give proportionate depreciation for exact months on mid-year purchases and sales.

Understanding explain with reasons · 1 question

- True/False: gain on sale of a capital asset is NOT added to revenue/turnover --- it is a capital profit credited separately to P&L, distinct from operating revenue.
- Know the disposal logic: charge depreciation for the period used in the year of sale, compare WDV on date of sale with sale proceeds/insurance claim to get profit or loss transferred to P&L.

TQ 4.1 · PYQ 2023-Dec [1] (a) (ii) {C} · True/False · 2M · Pg 251

LEVEL I
Understanding

Easy

Application practise the procedure · 14 questions

- Master the Machinery Account with mid-year purchase, erection/installation cost capitalised, mid-year sale of a part/whole machine, and depreciation on SLM or WDV --- always compute machine-wise WDV in working notes.
- Practise the Provision for Depreciation Account version: Machinery A/c stays at cost; on sale, transfer cost to Machinery Disposal A/c, transfer accumulated depreciation, credit sale proceeds, balance = profit/loss.
- Practise insurance-claim disposals (truck/bus destroyed, claim received in full settlement) and replacement purchase on the same date.
- Watch typical twists: opening balance already net of depreciation (work back to cost), second-hand machine where repair/recondition cost is capitalised, and proportionate depreciation for exact months.

PQ 4.1 · PYQ 2019-Nov [1] (c) {C} · Practical · 4M · Pg 252	LEVEL II Application	Medium
PQ 4.3 · PYQ 2021-Jul [1] (c) {C} · Practical · 4M · Pg 254 asked 3×	LEVEL II Application	Medium
PQ 4.4 · PYQ 2021-Dec [2] (b) · Practical · 5M · Pg 255	LEVEL II Application	Medium
PQ 4.9 · PYQ 2023-Dec [5] (b) · Practical · 5M · Pg 264	LEVEL II Application	Medium
PQ 4.12 · PYQ 2025-May [5] (a) · Practical · 5M · Pg 268	LEVEL II Application	Medium
PQ 4.13 · PYQ 2026-Jan [2] (b) · Practical · 8M · Pg 269	LEVEL II Application	Medium
PQ 4.2 · PYQ 2021-Jan [2] (b) · Practical · 10M · Pg 253 asked 5×	LEVEL II Application	Hard
PQ 4.5 · PYQ 2022-May [2] (a) · Practical · 10M · Pg 256 asked 3×	LEVEL II Application	Hard

PQ 4.6 · MTP 2022-May [2] (b) · Practical · 10M · Pg 258	LEVEL II Application	Hard
PQ 4.7 · MTP 2022-Nov S1 [2] (a) · Practical · 10M · Pg 260	LEVEL II Application	Hard
PQ 4.8 · PYQ 2023-Jun [2] (a) · Practical · 10M · Pg 262	LEVEL II Application	Hard
PQ 4.10 · MTP 2024-Aug [2] (a) · Practical · 10M · Pg 265	LEVEL II Application	Hard
PQ 4.11 · MTP 2024-Dec S1 [2] (b) · Practical · 10M · Pg 266	LEVEL II Application	Hard
PQ 4.14 · PYQ 2026-May [2] (a) · Practical · 10M · Pg 271	LEVEL II Application	Hard

Topic 5: Change in the Method of Depreciation

P1-C5-U5-T05

Read first Study the section 'Change in the Method of Depreciation' and Illustration 10: a change in method is a change in accounting estimate applied prospectively --- depreciate the WDV under the new method/rate from the date of change (no retrospective recalculation).

NOTES

Rule: review the method at least at each financial year-end; change it if the expected pattern of consumption of future economic benefits has changed significantly; the change is a change in accounting ESTIMATE — applied prospectively on the WDV from the date of change, with its effect quantified and disclosed (no retrospective recalculation).

Drill: build machine-wise WDV under the old method up to the changeover date, then depreciate that WDV under the new method/rate; where remaining useful life is given, new annual depreciation = $(\text{WDV at change date} - \text{scrap, if any}) \div \text{remaining useful life}$.

SM example: machine ₹10,50,000, residual ₹50,000, life 10 years; SLM for 2 years = ₹2,00,000, WDV ₹8,50,000; switch to WDV @25% → 3rd-year depreciation ₹2,12,500 (vs ₹1,00,000 had SLM continued) — quantify this difference when asked (Illustration 10 pattern).

Application practise the procedure · 7 questions

- Practise the standard problem: build machine-wise WDV up to the date of change under the old method (usually SLM or WDV), then apply the new method/rate prospectively on that WDV over remaining life.
- Combine change of method with a mid-year sale: depreciate sold machine to date of sale, compute profit/loss, then switch method for the remaining machines.
- Where remaining useful life is given at changeover (e.g. WDV to SLM), new annual depreciation = $\text{WDV at change date} \div \text{remaining useful life (less scrap, if any)}$.
- Set out clean working notes per machine (cost, yearly depreciation, WDV) --- examiners award step marks; also quantify the difference in depreciation to be adjusted where asked.

PQ 5.2 • PYQ 2022-Nov [1] (c) {C} • Practical • 4M • Pg 275	LEVEL II Application	Medium
PQ 5.4 • PYQ 2024-Jun [2] (b) • Practical • 8M • Pg 278 asked 3×	LEVEL II Application	Medium
PQ 5.5 • PYQ 2024-Sep [5] (b) • Practical • 5M • Pg 280 asked 2×	LEVEL II Application	Medium
PQ 5.1 • PYQ 2019-Jun [2] (b) • Practical • 10M • Pg 273 asked 4×	LEVEL II Application	Hard
PQ 5.3 • MTP 2023-Nov [2] (b) • Practical • 10M • Pg 277 asked 2×	LEVEL II Application	Hard
PQ 5.6 • PYQ 2025-Jan [2] (a) • Practical • 10M • Pg 281	LEVEL II Application	Hard
PQ 5.7 • RTP 2025-Jan [7] • Practical • --- • Pg 283 asked 5×	LEVEL II Application	Hard

Topic 6: Revision of the Estimated Useful Life of Property, Plant and Equipment

P1-C5-U5-T06

Read first Study the section 'Revision of the Estimated Useful Life' and Illustration 11: useful life and residual value are reviewed at each year-end; on revision, the remaining WDV (less residual value) is spread over the revised remaining useful life.

NOTES

Rule: residual value and useful life must be reviewed at least at each financial year-end; if expectations differ, account for it as a change in accounting estimate — the WDV (balance depreciable amount) is charged over the REVISED remaining useful life, prospectively; prior years' depreciation is never recomputed.

Formula: revised depreciation = (WDV at revision date – residual value) ÷ revised remaining useful life.

Illustration 11: machine ₹6,00,000, SLM, 10-year life, nil residual; after 3 years depreciation ₹1,80,000, WDV ₹4,20,000; remaining life reassessed from 7 to 5 years → depreciation from 4th year = ₹4,20,000 ÷ 5 = ₹84,000 p.a.; in multi-machine tables compute each machine's accumulated depreciation and WDV before revising the affected machine's life.

Application practise the procedure • 1 question

- Practise the drill: depreciation charged so far → WDV at revision date → new depreciation = (WDV – residual value)/revised remaining life, applied prospectively.
- Handle multi-machine tables (different purchase dates, lives, scrap values): compute each machine's accumulated SLM depreciation and WDV before revising the life of the affected machine(s).

- Remember it is a change in accounting estimate --- no retrospective adjustment, prior years' depreciation is not recomputed.

PQ 6.1 · PYQ 2025-Sep [2] (a) · Practical · 8M · Pg 285 asked 2×

LEVEL II
Application

Medium

Topic 7: Revaluation of Property, Plant and Equipment

P1-C5-U5-T07

Read first Study the section 'Revaluation of PPE' and Illustration 12: revaluation model, treatment of upward/downward revaluation through Revaluation Surplus vs P&L, reversal rules, and depreciation on the revalued amount over remaining useful life.

NOTES

Model: an asset whose fair value can be measured reliably may be carried at revalued amount less subsequent accumulated depreciation and impairment; revalue at adequate intervals; if one item of PPE is revalued the WHOLE CLASS must be revalued; revaluation is an accounting policy choice, not mandatory.

Increase: credit Revaluation Surplus (accumulated in equity) — EXCEPT recognise in P&L to the extent it reverses a previous decrease of the same asset that was charged to P&L.

Decrease: charge to P&L — EXCEPT debit Revaluation Surplus to the extent of any credit balance existing in the surplus for that same asset; only the excess fall hits P&L (key for successive yearly revaluations).

Depreciation after revaluation (Illus. 12): cost ₹12,00,000, SLM 10 years; after 3 years WDV ₹8,40,000; revalued up ₹60,000 → depreciable amount ₹9,00,000 over revised remaining 9 years → ₹1,00,000 p.a.

Surplus disposal: Revaluation Surplus may be transferred directly to Retained Earnings on derecognition, or the excess depreciation on the upward revaluation transferred yearly — never routed through Profit or Loss.

Application practise the procedure · 3 questions

- Practise: WDV at revaluation date $\pm$ revaluation amount = new depreciable amount; depreciation thereafter = new amount $\div$ revised remaining useful life (e.g. ₹10,00,000 SLM 10 years, revalued up ₹40,000 after 4 years).
- Apply the increase/decrease rules: upward revaluation → credit Revaluation Surplus (except reversal of earlier P&L decrease → credit P&L); downward → debit P&L (except to extent of earlier surplus for the same asset → debit Revaluation Surplus).
- Practise successive yearly revaluations against an existing Revaluation Surplus balance --- a fall is first set off against that asset's surplus, only the excess hits P&L.

- Note: if one item of PPE is revalued, the whole class must be revalued; revaluation is an accounting policy choice, not mandatory.

PQ 7.1 · PYQ 2018-Nov [1] (c) {C} · Practical · 4M · Pg 288	asked 8×	LEVEL II Application	Medium
PQ 7.2 · MTP 2023-Apr [2] (a) · Practical · 5M · Pg 289		LEVEL II Application	Medium
PQ 7.3 · PYQ 2026-Sep [2] (a) · Practical · 10M · Pg 290		LEVEL II Application	Hard

Topic 8: Intangible Assets

P1-C5-U5-T08

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §8: definition and examples of intangible assets, the four recognition conditions, cost of separate acquisition and derecognition.

NOTES

Definition: an intangible asset is an identifiable non-monetary asset, without physical substance, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes — e.g. streaming/broadcasting rights, airport landing slots, patents, trademarks, copyrights, distribution rights, long-term customer contracts, customer data, purchased goodwill, computer software; intangibles can make entities more valuable than their tangible assets (Air India's prime landing slots).

Recognition and cost: recognised only if (i) identifiable — the entity could rent, sell, exchange or distribute its specific future economic benefits without disposing of benefits of other assets, (ii) the enterprise can CONTROL it (obtain benefits and restrict others' access), (iii) future economic benefits are probable, and (iv) cost can be measured reliably; cost of a separately acquired intangible = purchase price + non-recoverable import duties/taxes + directly attributable expenditure (e.g. legal fees) - trade discounts and rebates.

Derecognition and contrast: derecognised on disposal or when no future economic benefits are expected — gain/loss = net disposal proceeds - carrying amount, recognised in P&L; unlike tangibles (depreciated over life based on expected usage), intangibles are amortised — useful life is presumed not to exceed 10 years unless evidence exists to the contrary, though some (purchased goodwill) may have indefinite life.

Topic 9: Amortisation

P1-C5-U5-T09

Read first Study the sections 'Intangible Assets' and 'Amortisation': definition of intangible assets, recognition conditions, and amortisation as the systematic allocation of an intangible's depreciable amount over its useful life (Illustrations 13–14).

NOTES

Amortisation (SM): “the systematic allocation of the depreciable amount of an intangible asset over its useful life” — i.e. depreciation of an intangible; commences when the asset is available for use; an intangible asset is an identifiable non-monetary asset without physical substance held for production/supply of goods or services, rental to others or administrative purposes.

Examples: patents, trademarks, copyrights, computer software, purchased goodwill, streaming and broadcasting rights, airport landing rights/slots, theatrical distribution rights, long-term customer contracts, customer data.

Recognition conditions: (i) identifiable (separable benefits), (ii) enterprise controls it (can obtain benefits and restrict others' access), (iii) probable future economic benefits, (iv) cost measurable reliably; cost = purchase price + non-recoverable duties/taxes + directly attributable expenditure (e.g. legal fees), less trade discounts.

Presumptions: useful life presumed NOT to exceed 10 years unless evidence to the contrary (contractual rights beyond 10 years → amortise over that longer period); residual value presumed ZERO unless a third-party commitment to purchase or an active market exists; use straight-line if the consumption pattern cannot be determined reliably; review period and method at each year-end.

Illustrations 13–14: patent cost ₹28,00,000 + ₹2,00,000 legal/registration = ₹30,00,000, 10 years → ₹3,00,000 p.a. (₹1,50,000 for the half year of registration); streaming rights ₹18,00,000 over 10 years, life cut to 5 more years after year 3 → carrying amount ₹12,60,000 ÷ 5 = ₹2,52,000 p.a.

Understanding explain with reasons · 1 question

- Explain amortisation: depreciation of an intangible asset --- systematic allocation of depreciable amount (cost less residual value) of an intangible over its useful life, commencing when the asset is available for use.
- Key presumptions to state: useful life presumed not to exceed 10 years unless evidence exists to the contrary; residual value presumed NIL unless a third-party purchase commitment or an active market exists.
- If the consumption pattern cannot be determined reliably, use the straight-line method; review amortisation period and method at each year-end.
- Support the answer with examples of intangibles: patents, trademarks, copyrights, computer software, streaming/broadcasting rights, landing slots, purchased goodwill.

TQ 9.1 · PYQ 2021-Dec [1] (c) (ii) {C} · Descriptive · 4M · Pg 291

LEVEL I
Understanding**Easy**

CHAPTER 6

Bills of Exchange and Promissory Notes

19 Topics • 23 Classified Questions • Importance: C

ICAI SKILL PROFILE Level I 5–20% • Level II 80–95% — this chapter reads **theory-heavy**

Level I — Remembering & Understanding **32.0%** 20 of 62.5 marks

Level II — Application & Analysis **68.0%** 42.5 of 62.5 marks

Topic 1: Bills of Exchange

P1-C6-U6-T01

Read first Read Section 1 of Chapter 6: definition of a bill of exchange (unconditional order in writing), its eight characteristics, the three parties, endorsement, and foreign bills of exchange (drawn in triplicate).

NOTES

Definition (SM): an “instrument in writing containing an unconditional order signed by the maker directing 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”; it becomes a valid bill when the order is accepted in writing on the face of the order itself.

Eight characteristics: (1) in writing, (2) dated, (3) contains an order to pay a certain sum, (4) unconditional, (5) payable to a definite person, his order or the bearer, (6) accepted for payment by the party ordered, (7) properly stamped (except bills payable on demand), (8) payable in legal currency of the country.

Three parties: drawer (makes the order — the creditor/seller), drawee who becomes acceptor on signing, and payee (to whom payment is made); drawer and payee CAN be the same person; a bill is transferable by endorsement exactly as a cheque.

Liability: primary liability is the acceptor's; if he does not pay, the holder can recover from any of the previous endorser or the drawer.

Foreign bill: drawn in one country and payable in another (Sec. 12, Negotiable Instruments Act: all non-inland instruments are foreign); generally drawn in TRIPLICATE, each copy posted separately — payment on one copy makes the others useless.

Remembering memorise · 1 question

- Definition to reproduce: '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'.
- Parties: Drawer (makes the order, usually the creditor/seller), Drawee/Acceptor (on whom it is drawn; becomes acceptor on signing), Payee (to whom payment is made); drawer and payee can be the same person.
- List the characteristics: in writing, dated, order to pay a certain sum, unconditional, payable to a definite person/order/bearer, accepted by drawee, properly stamped (except bills on demand), payable in legal currency.
- Primary liability is of the acceptor; on his default the holder can recover from prior endorsers or the drawer.

TQ 1.1 · MTP 2025-Jan S2 [6] (b) (i) · Short Note · 2.5M · Pg 295 **asked**
10x

LEVEL 1
Remembering

Easy

Topic 2: Promissory Notes

P1-C6-U6-T02

Read first Read Section 2: definition of a promissory note (unconditional undertaking signed by the maker), its eleven characteristics, and the specimen format.

NOTES

Definition (SM): "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 RBI Act a promissory note CANNOT be made payable to bearer.

Essentials (11 characteristics condensed): in writing; a clear PROMISE to pay — mere acknowledgement of a debt is not a note; unconditional — "I promise to pay ₹50,000 as soon as I can" fails; sum certain — "₹50,000 plus all fine" fails; maker and payee both certain; signed by the maker; properly stamped; payable in legal currency; not payable to bearer.

Negatives: it is not a bank note or currency note, and it requires NO acceptance — the debtor himself makes and signs it.

Understanding explain with reasons · 1 question

- True/False trap: a promissory note CANNOT be made payable to bearer --- Section 31(2) of the RBI Act prohibits it (the statement 'payable to bearer' is FALSE).
- Explain the essentials with reasons: clear unconditional promise (mere acknowledgement of debt is not a note; 'as soon as I can' is conditional), certain sum, certain maker and payee, signed and stamped.

- Note the negatives: it is not a bank note or currency note, and it requires NO acceptance (made by the debtor himself).

TQ 2.1 · PYQ 2024-Sep [1] (a) (iv) {C} · True/False · 2M · Pg 295 asked 3x **LEVEL I**
Understanding

Easy

Topic 3: Differences - Bill of Exchange and Promissory Note

P1-C6-U6-T03

Read first Study the comparison table in Section 3: order vs promise, number of parties, who pays, who draws, drawer-payee identity, nature of liability, conditional acceptance, notice of dishonour, and noting/protest.

NOTES

Core contrast: a bill contains the creditor's ORDER to the drawee to pay; a note contains the debtor's own PROMISE to pay — every other difference flows from this.

Bill of Exchange	Promissory Note
Contains an order to pay a certain sum	Contains only a promise to pay
Generally 3 parties: drawer, drawee, payee	2 parties: maker and payee
Drawn by the creditor; paid by the acceptor	Made by the debtor; paid by the maker
Drawer and payee may be the same person	Maker and payee cannot be the same person
Drawer's liability secondary and conditional (only if acceptor defaults)	Maker's liability primary and absolute
Can be accepted conditionally; notice of dishonour must be given	Cannot be made conditionally; no notice of dishonour required
On dishonour must be noted and protested	Noting and protest not required

Understanding explain with reasons · 2 questions

- True/False: bill --- drawer and payee MAY be the same person; promissory note --- maker and payee CANNOT be the same (a common reversed-statement trap: read which instrument allows identity of parties).
- TRUE statement to defend: a bill is paid by the ACCEPTOR while a promissory note is paid by the MAKER; a bill is drawn by the creditor, a note is made by the debtor.
- Explain liability difference: drawer's liability on a bill is secondary and conditional; maker's liability on a note is primary and absolute.

- Other contrasts to cite as reasons: bill contains an order (3 parties), note a promise (2 parties); notice of dishonour and noting/protest needed only for bills; only a bill can be accepted conditionally.

TQ 3.1 · PYQ 2019-Nov [1] (a) (iv) {C} · True/False · 2M · Pg 296 **asked 3x**

LEVEL I
Understanding

Easy

TQ 3.2 · PYQ 2024-Jun [1] (a) (iv) {C} · True/False · 2M · Pg 296 **asked 2x**

LEVEL I
Understanding

Easy

Topic 4: Record of Bills of Exchange and Promissory Notes

P1-C6-U6-T04

Read first Study Section 4: Bills Receivable (asset) vs Bills Payable (liability), and journal entries for receipt, the three options of the holder (retain, endorse, discount), honour and dishonour under each option.

NOTES

Classification: the party RECEIVING a promissory note or an accepted bill records an asset — Bills Receivable (Dr. Bills Receivable / Cr. Drawee or Maker); the party issuing a note or accepting a bill records a liability — Bills Payable.

Holder's three options: (i) retain till maturity — no further entry; on honour Dr. Bank / Cr. Bills Receivable; (ii) endorse to a creditor Z — Dr. Z / Cr. Bills Receivable, and no entry on honour; (iii) discount with bank — Dr. Bank (net amount received), Dr. Discount / Cr. Bills Receivable, and no entry on honour.

Dishonour: always debit the drawee/maker (he is again liable); credit depends on where the bill lay — Bills Receivable if retained, the Creditor's account if endorsed, Bank if discounted.

Discharge by endorsement: one's own acceptance settled by endorsing another party's acceptance held — Dr. Bills Payable / Cr. Bills Receivable (Katrak discharging his ₹5,000 acceptance to Patel with Mody's acceptance); always confirm WHOSE books you are writing before choosing accounts.

Application practise the procedure — no question in this edition

- Practise the holder's three options: retain (no entry till maturity), endorse (Dr Endorsee, Cr Bills Receivable), discount (Dr Bank with net amount, Dr Discount, Cr Bills Receivable).
- Dishonour entries: always debit the drawee; credit Bills Receivable (if retained), the creditor (if endorsed) or Bank (if discounted).
- Practise settlement of one's own acceptance by endorsing another party's acceptance: Dr Bills Payable, Cr Bills Receivable (e.g. Katrak discharging Patel's bill with Mody's acceptance).
- Write precise narrations and keep drawer's and drawee's books distinct --- most questions ask journal entries in ONE party's books only.

Topic 5: Term of a Bill

P1-C6-U6-T05

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §5: duration of a bill and when the term begins to run for after-sight and after-date bills.

NOTES

Term: the term of a bill of exchange may be of any duration but usually does not exceed 90 days from the date of the bill; when a bill is drawn AFTER SIGHT the term begins to run from the date of “sighting” i.e. when the bill is accepted, while for a bill drawn AFTER DATE the term runs from the date of drawing the bill.

Topic 6: Expiry / Due Date of a Bill

P1-C6-U6-T06

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6 (with §7 Days of Grace): the date on which the term terminates.

NOTES

Due date: the date on which the term of the bill terminates is called the “Expiry/Due Date of the bill”; every instrument payable otherwise than on demand is entitled to three days of grace beyond it.

Topic 7: Days of Grace

P1-C6-U6-T07

Read first Study Sections 5--10: term of a bill, expiry/due date, three days of grace, date of maturity, and bills at sight vs bills after date.

NOTES

Rule (SM): “Every instrument payable otherwise than on demand is entitled to three days of grace”; date of maturity = expiry/due date + 3 days of grace.

No-grace exceptions: instruments expressed payable on demand, at sight or on presentment

mature without grace days (“at sight” and “presentment” mean on demand); a bill payable on a SPECIFIC date is a time instrument and DOES get the 3 days.

Bill at sight vs bill after date: at sight — no time for payment mentioned, payable on demand at any presentation, no grace; after date — time instrument (payable after a specified period, on a specific day, after sight, or on a certain-to-happen event) with grace days added; a cheque is always on demand and never a time instrument.

Understanding explain with reasons • 1 question

- Rule with reason: every instrument payable otherwise than on demand gets THREE days of grace; maturity date = due/expiry date + 3 days of grace.
- True/False trap: even a bill payable on a SPECIFIC date gets days of grace --- grace days are excluded only for instruments payable on demand/at sight/on presentment (so 'specific due date excludes grace days' is FALSE).
- Distinguish bill at sight (no time mentioned, payable on demand, no grace days) from bill after date/after sight (time instrument, grace days added).

TQ 7.1 • PYQ 2022-May [1] (a) (iii) [C] • True/False • 2M • Pg 297

LEVEL 1
Understanding

Easy

Topic 8: Date of Maturity of Bill

P1-C6-U6-T08

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §8: due date plus three days of grace, and the exceptions.

NOTES

Maturity: the date arrived at by adding three days of grace to the expiry/due date is the date of maturity — every promissory note or bill of exchange matures on the third day after the day on which it is expressed to be payable, EXCEPT when expressed payable (i) on demand, (ii) at sight, or (iii) on presentment (no grace days for these).

Topic 9: Bill at Sight

P1-C6-U6-T09

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §9: demand instruments where no time for payment is mentioned.

NOTES

Bill at sight: an instrument in which NO time for payment is mentioned; a note/bill is payable on demand when no time is specified or when expressed payable on demand, at sight or on presentment (“at sight” and “presentment” mean on demand) — no days of grace are added to calculate maturity, and such an instrument may be presented for payment at any time; a cheque is always payable on demand.

Topic 10: Bill after Date

P1-C6-U6-T10

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §10: time instruments and the meaning of after sight; note on stale cheques.

NOTES

Bill after date: an instrument in which time for payment IS mentioned — a note/bill is a time instrument when payable (a) after a specified period, (b) on a specific day, (c) after sight, or (d) on the happening of an event certain to happen; “after sight” means after presentment for sight (promissory note) or after acceptance/noting/protest for non-acceptance (bill of exchange).

Cheque: a cheque cannot be a time instrument as it is always payable on demand — it may be post-dated, and has validity of 90 days from its date, after which it becomes a void “Stale Cheque” which the bank will not honour.

Topic 11: How to Calculate Due Date of a Bill

P1-C6-U6-T11

Read first Study Section 11's table on computing due dates: bills payable on a specific day, after stated months, after stated days (date of bill excluded), and the holiday rules; note 'after sight' runs from acceptance, 'after date' from drawing.

NOTES

Computation table: (a) payable on a specific date → that date is the due date; (b) stated months after date → term expires on the corresponding day of that month, and if no corresponding day, the last day of the month (bill signed 31 Jan at 3 months → due 3 May with grace); (c) stated days

after date → add the days EXCLUDING the date of the bill.

Holiday rules: due date falls on a public holiday → PRECEDING business day is the due date; emergency/unforeseen holiday → NEXT following day.

After sight vs after date: the term of a bill AFTER SIGHT commences from the date of acceptance, of a bill AFTER DATE from the date of drawing — e.g. bill of 1.1.2022 at 3 months after sight, accepted 6.1.2022, matures 9.4.2022.

Understanding explain with reasons · 2 questions

- Holiday rules to state with reasons: due date falling on a PUBLIC holiday → PRECEDING business day (so 'next working day' is FALSE); emergency/unforeseen holiday → NEXT following day.
- Months rule: term expires on the corresponding day of the month; if no corresponding day, the last day of that month (bill dated 31 Jan at 3 months → due 3 May with grace).
- Red-Ink interest (True/False from average due date context): when a bill's due date falls AFTER the date of closing the account, interest from the due date to the closing date is written in red ink and DEDUCTED --- check the exact direction stated in the question.

TQ 11.2 · RTP 2025-Jan [1] (vi) · True/False · --- · Pg 297

LEVEL I
Understanding

Easy

TQ 11.1 · MTP 2023-Dec [1] (a) (iv) {C} · True/False · 2M · Pg 297

LEVEL I
Understanding

Medium

Topic 12: Noting Charges

P1-C6-U6-T12

Read first Study Section 12: role of the Notary Public in establishing the fact and causes of dishonour, noting charges as his fee, and their recovery from the party responsible for dishonour, with entries when the bill was retained, endorsed or discounted.

NOTES

Short note: to establish the fact and causes of dishonour, the bill is given to a Notary Public who presents it for payment, and on dishonour notes the fact with reasons and returns the bill; his small fee is called NOTING CHARGES, recoverable from the party responsible for the dishonour (the drawee).

Entries (bill ₹1,000, charges ₹10): retained — Dr. Y (drawee) 1,010 / Cr. Bills Receivable 1,000, Cr. Bank 10; endorsed to Z who paid charges — Dr. Y 1,010 / Cr. Z 1,010; discounted — Dr. Y 1,010 / Cr. Bank 1,010; drawee is ALWAYS debited with bill amount plus noting charges.

Withdrawal against cheque: where the endorsee is then paid off, Dr. Endorsee / Cr. Bank — Katrak: Gupta's endorsed ₹4,000 bill dishonoured, Mehta paid ₹20 noting → Dr. Gupta 4,020 / Cr.

Mehta 4,020, then Dr. Mehta 4,020 / Cr. Bank 4,020.

Remembering memorise · 1 question

- Short note points: on dishonour the bill is given to a Notary Public who presents it, notes the fact and reasons of dishonour and charges a small fee called noting charges; the amount is recoverable from the party responsible for the dishonour (drawee).

TQ 12.1 · RTP 2022-May [20] (i) · Short Note · --- · Pg 298 **asked 4×**

LEVEL I
Remembering

Easy

Application practise the procedure · 1 question

- Entries: drawee is always debited with bill amount PLUS noting charges; credit goes to Bills Receivable / endorsee / Bank depending on who held the bill and paid the charges.
- Practise the endorsed-bill case: endorsee pays noting charges → Dr Drawee (amount + charges), Cr Endorsee; if bill is withdrawn against cheque, then Dr Endorsee, Cr Bank.
- Practise dishonour of a discounted bill with GST-inclusive sale value (e.g. goods ₹25,000 + IGST 18%, two bills, one dishonoured with noting charges) --- dishonour restores the full amount plus charges to the drawee's account.

PQ 12.1 · RTP 2025-Jan [8] · Practical · --- · Pg 298 **asked 3×**

LEVEL II
Application

Hard

Topic 13: Renewal of Bill

P1-C6-U6-T13

Read first Study Section 13: cancellation of the old bill, interest for the extended period, and the three cases for the new bill amount (nothing paid / interest paid in cash / part payment), with Illustration 2.

NOTES

Short note: the acceptor, unable to pay, asks for extension of time and in consideration agrees to bear interest for the extended period (from maturity of the old bill to the expected settlement date); the old bill is cancelled — entries exactly as for dishonour — and a new bill is drawn.

New bill amount: (i) drawee pays nothing → original amount + interest for the extension; (ii) drawee pays the interest in cash → original amount only; (iii) drawee makes part payment → unpaid balance + interest on that balance for the extended period.

Entry sequence (drawer's books): Dr. Drawee / Cr. Bills Receivable (cancel old bill); Dr. Drawee / Cr. Interest; then Dr. Bills Receivable (new bill) and Dr. Cash (any interest/part payment) / Cr. Drawee; drawee mirrors with Bills Payable, Interest and Cash.

Illustration 2: Pritam's ₹1,06,000 three-month bill renewed for 2 months, interest 9% p.a. = ₹1,590 paid immediately in cash → new bill for ₹1,06,000 only, met on due date.

Remembering memorise · 1 question

- Short note: renewal = cancellation of old bill at drawee's request and drawing a new bill for the extended period with interest from maturity of old bill to expected settlement; contrast with accommodation bill (drawn for raising finance, not trade).
- New bill amount: (i) drawee pays nothing → old amount + interest; (ii) interest paid in cash → old amount only; (iii) part payment → unpaid balance + interest on that balance.

TQ 13.1 · MTP 2024-Apr [6] (Or) (b) · Short Note · 5M · Pg 300

LEVEL I
Remembering

Easy

Application practise the procedure · 2 questions

- Entry sequence to practise: cancel old bill (Dr Drawee, Cr Bills Receivable/B P reversed), record interest (Dr Drawee / Cr Interest in drawer's books), draw new bill for balance + interest.
- Practise renewal of a discounted/collection bill: on renewal or dishonour of a bill sent for collection, reverse through Bank/Bills for Collection appropriately before drawing the new bill.
- Practise consolidation-type problems (several bills of different dates/usances replaced by one new bill), computing interest on each from its maturity to the settlement date.

PQ 13.2 · MTP 2023-Nov [3] (b) · Practical · 5M · Pg 302

LEVEL II
Application

Medium

PQ 13.1 · PYQ 2021-Dec [3] (a) · Practical · 10M · Pg 300

LEVEL II
Application

Hard

Topic 14: Retirement of Bills of Exchange & Rebate

P1-C6-U6-T14

Read first Study Section 14 and Illustration 3: retirement means the acceptor pays before maturity and receives a rebate/discount for premature payment; rebate is income of the acceptor and expense of the payee.

NOTES

Short note: when the acceptor has spare funds well before maturity he pays the payee early and receives a rebate/interest/discount for premature payment for the unexpired period; $\text{rebate} = \text{bill amount} \times \text{rate} \times \text{unexpired months} \div 12$.

Whose gain: the rebate is INCOME of the acceptor (drawee) and EXPENSE of the payee (drawer) — it is the consideration for premature payment, so “discount on retirement is a gain for the drawee”

is TRUE.

Entries: drawer — Dr. Bank (net), Dr. Rebate on Bills (or Interest/Discount) / Cr. Bills Receivable; acceptor — Dr. Bills Payable / Cr. Bank (net), Cr. Rebate Income (Interest/Discount).

Illustration 3: Bhavika retires her ₹5,00,000 acceptance one month before maturity under rebate 12% p.a. → rebate ₹5,000, bank ₹4,95,000; mixed problems: compute rebate only for the unexpired period at the given rate.

Remembering memorise · 1 question

- Short note: when the acceptor has spare funds before maturity he pays early and gets a rebate (interest/discount) for the unexpired period; $\text{rebate} = \text{bill amount} \times \text{rate} \times \text{unexpired months}/12$.

TQ 14.2 · RTP 2026-May [18] (5) · Short Note · 2.5M · Pg 304 **asked 9×**

LEVEL I
Remembering

Easy

Understanding explain with reasons · 1 question

- True/False: 'discount at the time of retirement is a gain for the drawee' --- TRUE; the rebate is income of the drawee/acceptor and an expense of the payee/drawer (consideration for premature payment).

TQ 14.1 · RTP 2026-May [1] (f) · True/False · --- · Pg 304 **asked 13×**

LEVEL I
Understanding

Easy

Application practise the procedure — no question in this edition

- Drawer's entry: Dr Bank (net), Dr Rebate/Discount, Cr Bills Receivable; drawee's entry: Dr Bills Payable, Cr Bank (net), Cr Rebate/Discount Income.
- Practise mixed problems where some bills are retired with rebate and others met/renewed on maturity --- compute the rebate only for the unexpired period at the given rate.

Topic 15: Insolvency

P1-C6-U6-T15

Read first Study Section 15 and Illustrations 7--8: on insolvency the acceptance is treated as dishonoured; amounts received from the estate are recorded and the balance written off as bad debts (drawee credits the shortfall to Deficiency Account).

NOTES

Rule: insolvency means the drawee cannot pay his liabilities, so his acceptances stand DISHONoured — pass the dishonour entry first: Dr. Drawee / Cr. Bills Receivable (if held), Cr. Bank (if discounted), Cr. Endorsee (if endorsed).

Recovery and write-off: on receiving x paise in the rupee from the estate — Dr. Bank (amount

recovered), Dr. Bad Debts (balance) / Cr. Drawee; prepare the insolvent's personal account first to compute the recovery and bad debts precisely.

Drawee's books: the amount he ultimately fails to pay is credited to DEFICIENCY ACCOUNT — Dr. Drawer / Cr. Bank (paise in rupee paid), Cr. Deficiency A/c.

Illustration 8 chain: Rita's ₹1,00,000 bill discounted for ₹99,000; on renewal ₹50,000 cash + interest ₹1,500 (12% p.a. × 3 months on the ₹50,000 balance) received and a new bill for ₹50,000 drawn; Rita insolvent → dishonour entry, then 40% recovered ₹20,000 and Bad Debts ₹30,000.

Application practise the procedure · 5 questions

- Standard chain to master: draw bill → discount with bank → renewal request (part cash + interest at given % + new bill for balance) → drawee insolvent → dishonour entry → receive x paise in the rupee → write off balance as bad debts.
- On insolvency, first pass the dishonour entry (Dr Drawee, Cr Bank if discounted / Bills Receivable if held), then Dr Bank with the recovered fraction and Dr Bad Debts with the balance.
- Interest on renewal is charged on the OUTSTANDING balance for the extension period (e.g. 12% p.a. for 3 months on the unpaid portion) --- add it to the drawee's account before drawing the new bill.
- Prepare the insolvent's personal account to compute the recovery and the bad debts precisely; in the drawee's books the unpaid amount is credited to Deficiency Account.

PQ 15.1 · PYQ 2019-Jun [3] (b) · Practical · 5M · Pg 305 asked 4×	LEVEL II Application	Medium
PQ 15.2 · RTP 2023-Dec [8] · Practical · --- · Pg 306 asked 9×	LEVEL II Application	Medium
PQ 15.3 · RTP 2024-Sep [8] · Practical · --- · Pg 307 asked 5×	LEVEL II Application	Medium
PQ 15.4 · PYQ 2025-Jan [5] (b) (i) · Practical · 5M · Pg 309	LEVEL II Application	Medium
PQ 15.5 · PYQ 2025-Sep [5] (a) (Or) (ii) · Practical · 5M · Pg 310	LEVEL II Application	Medium

Topic 16: Accommodation Bills

P1-C6-U6-T16

Read first Study Section 16 and Illustrations 9--10: bills drawn for mutual financing rather than trade --- proceeds and discounting charges are shared in the agreed ratio, with remittances between the parties on the due date.

NOTES

Concept: trade bills finance genuine purchase/sale of goods; accommodation bills use the same

mechanism purely to RAISE FINANCE for one or both parties — the bill is discounted and the proceeds divided by mutual agreement; entries are the same as ordinary bills, plus remittances between parties and shared discount.

Sharing principle: discounting charges must be borne by the parties in the SAME ratio in which the discounted proceeds are divided; on the due date the acceptor receives the other party's share and meets the bill.

Due-date failure: if the drawer cannot remit his share, the drawee draws a second bill on him and discounts it to honour the first; the second discount is apportioned on the proceeds remitted plus the benefit each derived on the first bill.

Illustration 10: X's ₹30,000 bill on Y discounted for ₹28,800, ₹9,600 remitted to Y (Y debited ₹10,000 including ₹400 discount share = one-third); on failure Y draws ₹42,000 bill, discounts it for ₹40,110, sends ₹6,740; X insolvent, estate pays 50 paise in the rupee — X credits the unpaid ₹14,000 to Deficiency A/c, Y writes off ₹14,000 as Bad Debts.

Understanding explain with reasons · 1 question

- Trade bill vs accommodation bill: trade bill backed by a genuine sale of goods (consideration exists); accommodation bill drawn to raise funds for one/both parties without any trade transaction; accounting entries are the same, plus entries for remittances and shared discount.
- Explain the sharing principle: discounting charges are borne by the parties in the SAME ratio in which the discounted proceeds are shared.

TQ 16.1 · RTP 2023-Jun [20] (ii) · Short Note · --- · Pg 312 asked 5×

LEVEL I
Understanding

Easy

Analysis work through mixed data · 2 questions

- Work through mutual accommodation problems: bill discounted (note the effective discount rate), proceeds split (e.g. drawer keeps his share and remits the rest), and each party's account tracked for principal + proportionate discount.
- Handle the due-date failure twist: drawer cannot remit, so drawee (or drawer) draws a SECOND bill which is discounted to honour the first; apportion the second discount by the benefit each party derives; follow through to insolvency and partial recovery where given (e.g. T/J ₹1,80,000 bill discounted for ₹1,72,800, ₹57,600 remitted = one-third share).

PQ 16.1 · PYQ 2025-May [5] (b) (i) · Practical · 2.5M · Pg 313 asked 2×

LEVEL II
Analysis

Medium

PQ 16.2 · PYQ 2026-Jan [5] (a) (Or) (ii) · Practical · 5M · Pg 314 asked 7×

LEVEL II
Analysis

Medium

Topic 17: Bills of Collection

P1-C6-U6-T17

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §17: bills sent to the bank for safe custody and realisation at maturity, with the three journal entries.

NOTES

Meaning: a bill-holder may, for safety, send the bill to his bank with instructions to retain it till maturity and realise it on that date — this is a “Bill sent for collection”, NOT discounting, because the bank credits the client only when the amount is actually realised.

Entries: on sending — Dr. Bills for Collection A/c / Cr. Bills Receivable A/c; on realisation — Dr. Bank A/c / Cr. Bills for Collection A/c; on dishonour — Dr. Drawee's A/c (from whom the bill was received) / Cr. Bills for Collection A/c.

Topic 18: Bills Receivable and Bills Payable Books

P1-C6-U6-T18

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §18: the day books for bills and their ruled forms.

NOTES

Nature: bills receivable and bills payable books are journals (Day Books) recording in chronological order the details of B/R and B/P — convenient when large numbers of bill transactions occur; postings to individual debtors/creditors accounts are made from the Day Books, and periodic TOTALS of bills received/accepted are posted to Bills Receivable A/c and Bills Payable A/c respectively.

Utility and form: useful for following up the status of outstanding bills falling due on different dates and identifying reasons for dishonour; B/R Book columns — date of receipt, voucher no., party from whom received, acceptor, date of bill, due date, place of payment, amount, L.F., mode of disposal; B/P Book columns — date of acceptance, drawer, payee, date of bill, due date, place of payment, amount.

Topic 19: Integrated Problems

P1-C6-U6-T19

Read first Revise the full set of bill entries together --- renewal with part cash and interest, dishonour of endorsed bills with noting charges, retirement at a discount, and discharge by endorsing another's acceptance --- as combined in Illustration 4 (Katrak-type questions).

NOTES

Katrak (i) — renewal of own acceptance: acceptance to Basu ₹2,500 discharged by ₹1,000 cash + new bill with ₹50 interest: Dr. Bills Payable 2,500, Dr. Interest 50 / Cr. Cash 1,000, Cr. Bills Payable 1,550.

Katrak (ii) — endorsed bill dishonoured: Gupta's ₹4,000 acceptance endorsed to Mehta dishonoured, Mehta paid ₹20 noting charges: Dr. Gupta 4,020 / Cr. Mehta 4,020; bill withdrawn against cheque: Dr. Mehta 4,020 / Cr. Bank 4,020.

Katrak (iii)-(iv): Dalal retires a ₹2,000 bill at ₹10 discount — Dr. Bank 1,990, Dr. Discount 10 / Cr. Bills Receivable 2,000; acceptance to Patel ₹5,000 discharged by endorsing Mody's acceptance — Dr. Bills Payable 5,000 / Cr. Bills Receivable 5,000.

Method: for every transaction fix (a) whose books you are writing and (b) the bill's location — held, endorsed or discounted — before choosing the credit account; always add noting charges to the defaulting drawee's debit and include interest in the amount of any renewed bill.

Application practise the procedure · 1 question

- Master the four classic Katrak-style entries in one party's books: (1) own acceptance discharged by part cash + new bill including interest; (2) endorsed bill dishonoured with noting charges paid by endorsee, then withdrawn against cheque; (3) drawee retires a bill at a discount; (4) own bills payable discharged by endorsing a bill receivable held.
- For each transaction, identify the books you are writing in and the bill's location (held/endorsed/discounted) before choosing the credit account.
- Always add noting charges to the defaulting drawee's debit and include interest in the amount of any renewed bill.

PQ 19.1 · PYQ 2023-Jun [3] (b) · Practical · 5M · Pg 316

LEVEL II
Application

Medium

CHAPTER 7

Preparation of Final Accounts of Sole Proprietors

15 Topics • 32 Classified Questions • Importance: B

ICAI SKILL PROFILE Level I 5–20% • Level II 80–95% — this chapter reads **in line with the paper**

 Level I — Remembering & Understanding **8.0%** 14 of 174 marks

 Level II — Application & Analysis **92.0%** 160 of 174 marks

Unit 7.1: Final Accounts of Non-Manufacturing Entities

P1-C7-U7.1 • Importance B • Rank 1 in chapter • Category A • 78.1% of chapter questions • 25 questions

Topic 1: Introduction

P1-C7-U7.1-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §1.1 of the unit: financial statements of non-manufacturing (trading) entities and the Income Statement vs Position Statement comparison chart.

NOTES

Non-manufacturing entities: trading entities engaged in purchase and sale of goods for profit without changing the form/underlying use of goods — they sell goods in original form; at year-end they prepare financial statements to ascertain income and financial position.

Two-level structure: Income Statement = Trading A/c (Gross Profit/Loss) + Profit & Loss A/c (Net Profit/Loss); Position Statement = Balance Sheet showing position of assets, liabilities and capital as on a particular date.

Income Statement	Position Statement
Discloses net profit/loss after adjusting all expenses of the year from income earned	Discloses assets and liabilities position as on a particular date
Sub-divided into Trading A/c and Profit & Loss A/c	Besides balance sheet, additional statements (cash flow, changes in equity) may be prepared — not mandatory for non-corporate entities

Topic 2: Preparation of Final Accounts

P1-C7-U7.1-T02

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §1.2: basic principles for accumulating accounting-period data before drawing up Trading A/c, P&L A/c and Balance Sheet.

NOTES

Function: final accounts must exhibit truly and fairly the performance and financial position; basic principles — distinguish capital vs revenue receipts/payments, separate income and expenses of one period from another, accumulate items under significant heads.

Matters needing attention: (a) separate personal income/expenditure of proprietor from business, (b) capital vs revenue distinction with provision for accrued unpaid expenses on same basis as previous year, (c) disclose all material information (e.g. bonus in labour charges, substantial inventory write-offs), (d) record only current period transactions.

Topic 3: Trading Account

P1-C7-U7.1-T03

Read first Study Section 1.3 (Trading Account) of the ICAI Study Material: computation of cost of goods sold, the Trading Account format, individual items (opening inventory, purchases and returns, carriage inwards, wages, sales and sales returns, closing inventory) and the closing entries.

NOTES

Purpose (SM 1.3): Gross Profit is the difference between the selling price and the cost of the goods sold; it is ascertained by preparing a Trading Account, and the balance is transferred by Trading A/c Dr To Profit and Loss A/c (gross profit) or P&L A/c Dr To Trading A/c (gross loss).

Format: Dr — opening stock, purchases less returns outward, direct expenses (freight & carriage inwards, customs & insurance, wages, gas/water/fuel, factory expenses, royalty on production); Cr — sales less returns inward, closing stock; balancing figure = gross profit c/d (or gross loss on the credit side).

Formulas: COGS = Opening Stock + Net Purchases + Direct Expenses – Closing Stock; GP = Net Sales – COGS; rule for direct expenses — debit Trading A/c only with expenses of bringing goods to their present location and condition (freight on purchases, cartage, octroi, godown wages); freight or wages on a fixed asset are added to the cost of the asset, not debited to Trading A/c.

Closing stock: entry Closing Inventory A/c Dr To Trading A/c (or alternatively To Purchases A/c);

valued at cost or net realisable value whichever is lower (include goods with consignment agents and goods sent on approval); if closing stock appears IN the Trial Balance it has already been adjusted against Purchases, so it is NOT entered in the Trading A/c and appears only in the Balance Sheet.

Closing entries: (1) Trading A/c Dr To Opening Inventory / Purchases / Wages / Freight on Purchases; (2) Sales A/c Dr and Closing Inventory A/c Dr To Trading A/c; returns are first netted (Purchases Return A/c Dr To Purchases; Sales A/c Dr To Sales Return); goods received without invoice — debit Purchases, credit the supplier.

Understanding explain with reasons · 1 question

- Be able to justify: if Closing Stock appears in the Trial Balance, it is already adjusted against Purchases, so it is NOT entered in the Trading Account and appears only in the Balance Sheet (True --- a repeat T/F).
- Explain the rule for direct expenses: only costs of bringing goods to their present location and condition (freight/carriage inwards, octroi, godown wages) are debited to Trading A/c; freight or wages on a fixed asset are capitalised instead.

TQ 3.1 · PYQ 2024-Jun [1] (a) (i) {C} · True/False · 2M · Pg 323 asked 7×

LEVEL I
Understanding

Easy

Application practise the procedure · 1 question

- Practise the Trading A/c format: Dr --- opening stock, purchases less returns outward, direct expenses; Cr --- sales less returns inward, closing stock; gross profit as balancing figure carried to P&L.
- Drill $\text{COGS} = \text{Opening Stock} + \text{Net Purchases} + \text{Direct Expenses} - \text{Closing Stock}$, and $\text{GP} = \text{Sales} - \text{COGS}$; also work backwards (e.g. given COGS and sales, find GP and GP ratio).
- Practise short 4--5 mark problems like preparing a Trading A/c from a list of balances (opening inventory, purchases, carriage inwards, wages, sales, both returns, closing inventory).

PQ 3.1 · PYQ 2018-Nov [3] (b) · Practical · 5M · Pg 323

LEVEL II
Application

Medium

Topic 4: Profit and Loss Account

P1-C7-U7.1-T04

Read first Study Section 1.4 (Profit and Loss Account): classification of expenses (management, maintenance, selling and distribution, financial, abnormal losses), closing entries, and the specific treatments of drawings, income tax, trade vs cash discount, rebate, bad debts and bad debts recovered.

NOTES

Scheme (SM 1.4): starts with gross profit b/d on Cr (gross loss on Dr); debit expenses grouped by function — management (salaries, office rent/rates, printing, postage, insurance, audit and legal fees), maintenance (repairs, depreciation of office assets), selling & distribution (advertisement, godown rent, carriage outward, bad debts, provision for bad debts, commission), financial (bank charges, interest on loans, discount allowed) and abnormal losses (loss on sale of asset, loss by fire); credit other income (discount/commission received), non-trading income (bank interest, rent of property let out, dividends) and abnormal gains; balance = net profit (P&L A/c Dr To Capital A/c) or net loss (Capital A/c Dr To P&L A/c).

Only nominal accounts: expenses, losses, incomes and gains go to Trading/P&L A/c; personal and real accounts go to the Balance Sheet; drawings and the sole proprietor's income tax are NOT firm expenses — debit Capital A/c (Capital A/c Dr To Drawings; Capital A/c Dr To Income Tax A/c).

Trade vs cash discount: trade discount is allowed when the order is not below a certain figure, is deducted from the invoice and only the net amount is recorded — never debited to P&L; cash discount is an allowance for prompt payment before a certain date and IS recorded — discount allowed debited, discount received credited to P&L; **Rebate:** allowance when a customer's purchases in a period reach a set total (4% on purchases of ₹5,100 = ₹204), entered only at year end: Rebate A/c Dr To Customer, then P&L A/c Dr To Rebate A/c.

Bad debts: Bad Debts A/c Dr To Customer's A/c, then P&L A/c Dr To Bad Debts (or Provision for Bad Debts A/c Dr if a provision exists); amounts later recovered are a gain, credited to Bad Debts Recovered A/c and taken to the Cr of P&L — never credited to the party paying.

Understanding explain with reasons · 3 questions

- Trade discount is a reduction from LIST PRICE on business considerations (like bulk orders); CASH discount is for prompt payment --- the T/F trap merges the two definitions, so learn both exactly.
- Only nominal accounts (expenses, losses, incomes, gains) go to Trading/P&L A/c; personal and real accounts go to the Balance Sheet (so 'all personal & real accounts are recorded in P&L' is False).
- Provision for bad debts is debited to Profit and Loss A/c and deducted from Sundry Debtors in the Balance Sheet --- it is NOT debited to Sundry Debtors Account.
- Prior period items MUST be separately disclosed in the current statement of profit and loss so their effect on current profit can be perceived.

TQ 4.1 · PYQ 2019-Nov [1] (a) (i) {C} · True/False · 2M · Pg 324	asked 2×	LEVEL I Understanding	Easy
TQ 4.2 · PYQ 2021-Dec [1] (a) (iii) {C} · True/False · 2M · Pg 325	asked 5×	LEVEL I Understanding	Easy
TQ 4.3 · RTP 2023-Jun [1] (i) · True/False · --- · Pg 325	asked 2×	LEVEL I Understanding	Medium

Application practise the procedure · 1 question

- Practise income-received-in-advance computations (magazine subscriptions): income for the year = opening advance + amounts received – closing advance; advance balance goes to liabilities.
- Practise preparing a P&L A/c from given balances with closing entries, transferring net profit/net loss to Capital A/c.

PQ 4.1 · PYQ 2021-Jan [5] (b) · Practical · 5M · Pg 325

LEVEL II
Application**Medium****Topic 5: Certain Adjustments and their Treatments**

P1-C7-U7.1-T05

Read first Study the Adjustments portion of Section 1.4 (outstanding/prepaid expenses, accrued income, income received in advance, provisions for doubtful debts, discount and depreciation) plus Section 1.5 (abnormal loss by fire, goods sent on approval, goods used other than for sale, manager's commission on profit).

NOTES

Period adjustments: outstanding expense — Expense A/c Dr To Outstanding Expense A/c (add to expense in P&L, show as liability); prepaid — Prepaid Expense A/c Dr To Expense A/c (deduct, show as asset); accrued income — Accrued Income A/c Dr To Income A/c (add, asset); income received in advance — Income A/c Dr To Income Received in Advance A/c (deduct, liability); magazine subscriptions: income for the year = receipts + opening advance – closing advance); all such entries are reversed next year.

Provisions: P&L A/c Dr To Provision for Bad and Doubtful Debts; write off bad debts first against the existing provision, then raise the balance to the required % of debtors — P&L charge = bad debts written off + closing provision – opening provision; provision for discount on debtors is calculated AFTER deducting the provision for doubtful debts because discount is allowed only to good debtors; both are deducted from trade receivables in the Balance Sheet, and provision for depreciation from the asset concerned.

Abnormal loss by fire (SM 1.5): Loss by Fire A/c Dr To Purchases/Trading A/c with full cost; then Insurance Company's A/c Dr (claim admitted) and P&L A/c Dr (portion not compensated) To Loss by Fire A/c; the claim receivable appears on the assets side until received (goods ₹6,000, claim ₹4,500 → P&L bears ₹1,500).

Goods on approval: initially recorded as actual credit sales; at year end the unapproved sale is reversed at invoice price (Sales A/c Dr To Trade Receivables A/c) and the goods are brought into closing stock at COST (Stock on Approval A/c Dr To Trading A/c); **Goods used other than for sale:** credit Purchases A/c and debit Drawings (personal use), Donation, Free Samples/Advertisement, Building or Plant & Machinery (construction), or Repairs & Maintenance as per use.

Manager's commission on profit: before charging such commission = Profit $\times$ Rate/100; after charging = Profit before commission $\times$ Rate/(100 + Rate) — e.g. 10% on ₹1,00,000 after charging = ₹1,00,000 $\times$ 10/110 $\approx$ ₹9,091; entry Commission A/c Dr To Commission Payable A/c — commission debited to P&L, Commission Payable shown on the liabilities side.

Understanding explain with reasons · 3 questions

- Goods sold on approval ARE initially recorded as credit sales; at year end, unapproved sales are reversed (Sales A/c Dr To Trade Receivables) and the goods are included in closing stock at cost --- know this two-entry logic for the T/F.
- Outstanding salaries of the PREVIOUS year are a liability of that year; if paid during the current year they do not appear in the current year Balance Sheet --- reason carefully before answering True/False.
- Provision for discount on debtors is calculated AFTER deducting the provision for doubtful debts, because discount is allowed only to good debtors who pay.

TQ 5.2 · RTP 2025-Jan [1] (iii) · True/False · ---- · Pg 327

LEVEL I
Understanding

Easy

TQ 5.1 · MTP 2023-Dec [1] (a) (iii) {C} · True/False · 2M · Pg 326 **asked**
2×

LEVEL I
Understanding

Medium

TQ 5.3 · RTP 2025-Sep [1] (d) · True/False · 2M · Pg 327

LEVEL I
Understanding

Medium

Application practise the procedure · 1 question

- Practise expense computations with mid-year changes (e.g. salary raise from a date, new hires/trainees at half pay): compute the correct P&L charge, actual payments and the outstanding/prepaid balance for the Balance Sheet.
- Drill manager's commission formulas: before charging = Profit $\times$ r/100; after charging = Profit $\times$ r/(100 + r), plus the journal entry (Commission A/c Dr To Commission Payable A/c).

PQ 5.1 · PYQ 2020-Nov [5] (b) · Practical · 5M · Pg 327

LEVEL II
Application

Medium

Topic 6: Balance Sheet

P1-C7-U7.1-T06

Read first Study Section 1.6 (Balance Sheet): definition and characteristics, arrangement of assets and liabilities by liquidity or permanence, classification into current/fixed/intangible assets and current/long-term liabilities, and the capital account presentation (add net profit, less drawings).

NOTES

Definition (SM): “a statement which sets out the assets and liabilities of a firm or an institution as

at a certain date” — since a single transaction alters assets or liabilities, it is true only at that particular point of time (significance of “as at”).

Characteristics: (i) prepared at a particular date, not for a period; (ii) prepared only after the P&L A/c — together they are the Final Accounts (the Balance Sheet is not an account, its sides are not Dr and Cr); (iii) the two sides must have the same totals because capital always equals assets minus liabilities — unequal totals mean an error somewhere.

Marshalling and classification: assets arranged by liquidity (cash first, land & building last) or by permanence (the reverse); liabilities by urgency of payment; current assets are convertible into cash within one year (cash, bank, trade receivables, inventories), fixed/long-term assets are for continued use (machinery, building, long-term investments), intangible assets have no physical existence (patents, copyrights); current liabilities are settled within a year (creditors, bills payable), long-term liabilities beyond a year (term loans).

Capital section and grouping: Capital balance + Net Profit (or – Net Loss) – Drawings, where drawings include cash withdrawn, goods taken for personal use (Drawings A/c Dr To Purchases A/c — at cost, never via Capital or P&L) and income tax paid; usual groups — capital, long-term loans, short-term loans, current liabilities, provisions against tangible fixed assets, intangibles, investments, current assets.

Presentation points: provisions for doubtful debts and for discount are deducted from total book debts and provision for depreciation from the asset cost; intangible strengths like staff loyalty/calibre (human resources) cannot be shown as assets; salary paid in advance is an asset (cash converted into a prepayment), not an expense; outstanding salaries of an earlier year appear as a liability only if still unpaid at the date of the Balance Sheet.

Understanding explain with reasons · 3 questions

- Drawings (cash or goods withdrawn) are a reduction of capital debited to Capital/Drawings A/c --- never a P&L expense; goods taken for personal use are credited to PURCHASES A/c, not Capital A/c.
- Human resources are NOT shown as assets --- they cannot be measured in money terms (money measurement concept).
- Salary paid in advance is not an expense, but the correct reason is that it represents an asset (payment converts cash into prepaid asset) --- the T/F statement's reason 'neither reduces assets nor increases liabilities' is wrong because cash does reduce.
- Outstanding salaries of the previous year appear as a liability only if still unpaid; distinguish accrual of liability from its settlement.

TQ 6.1 · RTP 2018-May [1] (g) · True/False · --- · Pg 328 asked 3×

LEVEL I
Understanding

Easy

TQ 6.2 · RTP 2025-May [1] (i) · True/False · --- · Pg 329 asked 3×

LEVEL I
Understanding

Easy

TQ 6.3 · MTP 2023-Nov [1] (a) (i) {C} · True/False · 2M · Pg 329 asked 5×

LEVEL I

Medium

Understanding

Application work the problem · 1 question

PQ 6.1 · PYQ 2026-Jan [4] (b) · Practical · 10M · Pg 329

LEVEL II
Application**Hard****Synthesis** prepare end-to-end — no question in this edition

- Master preparing a full Balance Sheet from a schedule of balances with adjustments: depreciation, bad debts written off, provisions for doubtful debts and discount, outstanding/prepaid items, closing stock.
- Practise the capital section layout: Opening capital + Net profit – Drawings (including goods withdrawn and income tax) and grouping under fixed assets, investments, current assets, current liabilities and provisions.

Topic 7: Sequence of Accounting Procedure or the Accounting Cycle

P1-C7-U7.1-T07

CONCEPT BASE — no exam question asked yet · essential for full preparation**Read first** Read §1.7 listing the five steps of the accounting process in order.

NOTES

Accounting cycle: (i) journalising the transactions → (ii) posting into the ledger → (iii) taking out the trial balance to check arithmetical accuracy → (iv) preparing Trading and P&L A/c (income statement) for the period → (v) preparing the Balance Sheet to show financial position at period end.

Topic 8: Opening Entry

P1-C7-U7.1-T08

CONCEPT BASE — no exam question asked yet · essential for full preparation**Read first** Read §1.8 with Illustration 8: journalising previous year's closing balances as the first entry of the new year and posting it.

NOTES

Opening entry: first journal entry of the new year records closing balances of assets and liabilities of the previous year (per last balance sheet) as opening balances — Dr. all assets / Cr. all liabilities

and Capital A/c ("Being the balances brought forward").

Posting: each asset account opens with "To Balance b/d" on the debit side and each liability/capital account with "By Balance b/d" on the credit side — thereby all asset and liability accounts stand opened at the beginning of the year.

Topic 9: Provisions and Reserves

P1-C7-U7.1-T09

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.9 with Illustration 14: definitions of provision, reserve and reserve fund and the charge vs appropriation distinction.

NOTES

Provision: "any amount written off or retained by way of providing for depreciation, renewal or diminution in the value of assets or retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy" — a liability measurable only with a substantial degree of estimation; e.g. provision for doubtful debts, taxes still to be assessed, admissible but unascertained claims.

Reserve: portion of earnings, receipts or other surplus (capital or revenue) appropriated by management for a general or specific purpose other than depreciation/diminution or a known liability; types — capital reserves and revenue reserves; provisions in excess of the amount necessary are treated as reserves.

Key distinction: provisions are a charge against profits while reserves are an appropriation of profits; **Reserve Fund:** reserve amount invested outside the business in readily realisable securities (e.g. government securities).

Topic 10: Limitations of Financial Statements

P1-C7-U7.1-T10

Read first Study Section 1.10 (Limitations of Financial Statements) --- the five principal limitations to be kept in mind while evaluating financial statements, especially when comparing different companies.

NOTES

Five principal limitations (SM 1.10): (a) Historical cost — statements use the money value prevailing when transactions occurred, ignoring subsequent changes (a house built in 1980 for

₹15,000 gives the same occupation benefit as one built in 2022 for ₹30,00,000, yet appears at original cost); (b) Intangible strengths and weaknesses — e.g. loyalty and calibre of staff cannot be shown in the Balance Sheet; (c) Perpetual continuity and periodical accounts — the going concern assumption forces arbitrary distribution of non-revenue expenditure over the years benefited, so accounts are not absolutely correct; (d) Different accounting policies — e.g. annually funding pensions/gratuities vs recording only actual payments, or whether and how intangible assets are written off; (e) Different management policies for staff and public welfare.

Comparability: the limitations are less serious when appraising a single company over a period of years; comparing different companies for the same period can be misleading unless they have followed the same system and basis of accounting — hence inter-industry comparison on financial statements only if no other basis is practicable; historical cost still remains the accepted basis because continuous revaluation is costly and impracticable when the value of money keeps falling.

Understanding explain with reasons · 1 question

- Be ready to discuss the five limitations for a 4-mark answer: (a) historical cost basis ignores changes in money value (1980 house example), (b) intangible strengths/weaknesses like staff loyalty are not shown, (c) going concern forces arbitrary allocation of expenditure over periods, (d) different accounting policies (e.g. pension funding, intangibles write-off) impair comparability, (e) differing management policies.
- Explain why inter-company comparison is misleading unless the same system and basis of accounting is followed.

TQ 10.1 · MTP 2024-Apr [1] (b)DESC 4 Marks {C} · · --- · Pg 333 asked 5x LEVEL I Understanding

Medium

Topic 11: Integrated Problems

P1-C7-U7.1-T11

Read first Work through the comprehensive illustrations at the end of Unit 1 that combine Sections 1.3--1.6 --- preparing Trading and Profit & Loss Account and Balance Sheet from a trial balance or schedule of balances with multiple adjustments.

NOTES

Working order: from the trial balance or schedule of balances prepare Trading A/c → P&L A/c → Balance Sheet (Illustrations 9, 10 and 12); give every adjustment its two-fold effect — once in Trading/P&L and once in the Balance Sheet — record adjustments on rough working sheets first, and check that both Balance Sheet sides tally.

Standard adjustment set (Illustration 12 — Gavaskar Viswanath & Co.): closing stock; depreciation at given rates with error corrections first (steel table sold at cost but proceeds wrongly credited to Sales A/c; typewriter purchase ₹40,000 wrongly debited to Purchases —

remove and capitalise before depreciating); outstanding godown rent for two months; interest on loan accrued @ 12% p.a. from the date the loan was taken; provision for bad debts maintained at 5% of sundry debtors.

Exam variants: revise a wrongly drawn P&L before the Balance Sheet (Illustration 7 — debit forgotten outstanding expenses, credit prepaid insurance to get revised net profit); pass the opening entry from last year's Balance Sheet (assets Dr; trade payables, overdraft, provision for doubtful debts and capital Cr — Illustrations 8 and 11); settle GST balances by utilising Input CGST/SGST against Output liability and carry any unutilised input credit as a Balance Sheet asset (Illustrations 9 and 10 working notes).

Application work the problem · 10 questions

PQ 11.3 · RTP 2018-May [12] · Practical · --- · Pg 338 asked 5×	LEVEL II Application	Medium
PQ 11.1 · PYQ 2019-Jun [4] (b) · Practical · 10M · Pg 334 asked 4×	LEVEL II Application	Hard
PQ 11.2 · PYQ 2025-May [4] (b) · Practical · 10M · Pg 336 asked 4×	LEVEL II Application	Hard
PQ 11.4 · PYQ 2021-Jul [4] (a) · Practical · 10M · Pg 341 asked 3×	LEVEL II Application	Hard
PQ 11.5 · RTP 2022-May [13] · Practical · --- · Pg 343	LEVEL II Application	Hard
PQ 11.6 · PYQ 2024-Sep [3] (a) · Practical · 10M · Pg 346	LEVEL II Application	Hard
PQ 11.7 · RTP 2024-Sep [9] · Practical · --- · Pg 350 asked 5×	LEVEL II Application	Hard
PQ 11.8 · PYQ 2025-Jan [3] (a) · Practical · 15M · Pg 353 asked 13×	LEVEL II Application	Hard
PQ 11.9 · PYQ 2026-May [4] (b) · Practical · 10M · Pg 357	LEVEL II Application	Hard
PQ 11.10 · PYQ 2026-Sep [4] (b) · Practical · 10M · Pg 360	LEVEL II Application	Hard

Synthesis prepare end-to-end — no question in this edition

- Master the complete 10--15 mark final accounts problem: from trial balance/schedule of balances prepare Trading A/c, P&L A/c and Balance Sheet with working notes, ensuring both sides tally.
- Drill the standard adjustment set: closing stock, depreciation (including additions during the year, time-apportioned), further bad debts + provision for doubtful debts + provision for discount on debtors, outstanding/prepaid expenses and accrued/advance income, goods on approval, drawings of goods, abnormal loss with insurance claim, and manager's commission on profit.
- Practise variants seen in exams: first rewriting a wrongly drawn trial balance, building accounts from a transactions narrative of a new business (capital introduced, bank loan, asset purchases), and deriving missing figures before preparing the statements.

Unit 7.2: Final Accounts of Manufacturing Entities

P1-C7-U7.2 · Importance D · Rank 2 in chapter · Category C · 21.9% of chapter questions · 7 questions

Topic 1: Introduction

P1-C7-U7.2-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.1 of the unit: why manufacturing entities prepare a separate Manufacturing Account before Trading A/c, P&L A/c and Balance Sheet.

NOTES

Manufacturing Account: prepared by manufacturing entities as part of final accounts in addition to Trading A/c, P&L A/c and Balance Sheet — objective is to determine manufacturing cost of finished goods for assessing cost-effectiveness of manufacturing activities; this cost is then transferred to the Trading A/c.

Vs Trading A/c: Trading A/c shows Gross Profit while Manufacturing A/c shows cost of goods sold including direct expenses; Manufacturing A/c deals with raw materials and work-in-progress whereas Trading A/c deals with finished goods only.

Topic 2: Purpose

P1-C7-U7.2-T02

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.2 listing the three functions a Manufacturing Account serves.

NOTES

Functions: (1) shows total cost of manufacturing finished products with classified constituent elements — debited with cost of materials, manufacturing wages and expenses incurred directly or indirectly to manufacture; (2) provides details of factory cost, facilitates reconciliation of financial books with cost records and period-to-period comparison of manufacturing operations; (3) if output is carried to Trading A/c at market price it shows profit/loss on manufacture, and it may be used to fix production-linked bonus.

Topic 3: Manufacturing Costs

P1-C7-U7.2-T03

Read first Study Section 2.3 (Manufacturing Costs): classification into raw material consumed, direct manufacturing wages, direct manufacturing expenses and manufacturing overheads, plus the meaning and treatment of by-products.

NOTES

Cost build-up (SM 2.3): Raw Material Consumed + Direct Manufacturing Wages + Direct Manufacturing Expenses = Direct (prime) Manufacturing Cost; add Indirect Manufacturing Expenses / Manufacturing Overhead = Total Manufacturing Cost; **Formula:** Raw Material Consumed = Opening inventory of Raw Materials + Purchases – Closing inventory of Raw Materials.

Direct vs indirect: direct manufacturing expenses are costs other than material or wages incurred for a specific product — e.g. royalties for licence/technology and hire charges of plant, IF based on units produced (they vary directly with production); Overhead = Indirect Material (stores for repairs, small tools, fuel, lubricating oil) + Indirect Wages (maintenance wages, holding pay) + Indirect Expenses (training, depreciation and insurance of plant & machinery and factory shed).

By-products: secondary products from the same raw materials and same process without additional expense (molasses in sugar manufacture, butter milk in a dairy); their value is generally insignificant, so they are valued at NET REALISABLE VALUE where cost is not separately identifiable; correct treatment — credit the sale value to the MANUFACTURING Account (not the Trading Account, not merely other operating income) so as to reduce the cost of manufacture of the main product.

Understanding explain with reasons · 1 question

- The sale value of a by-product is credited to the MANUFACTURING Account (not the Trading Account) so as to reduce the cost of manufacturing the main product --- this exact T/F has been asked; also note by-products are valued at net realisable value.
- Be able to explain direct vs indirect manufacturing expenses: royalty or hire charges based on units produced are DIRECT; repairs, depreciation of plant/factory shed, insurance, indirect material/wages form OVERHEAD.
- Know Raw Material Consumed = Opening inventory of RM + Purchases – Closing inventory of RM, and the build-up: prime cost (RM + direct wages + direct expenses) plus overheads = total manufacturing cost.

TQ 3.1 · MTP 2023-May [1] (a) (iii) {C} · True/False · 2M · Pg 366 **asked**
4x

LEVEL I
Understanding

Easy

Topic 4: Design of A Manufacturing Account

P1-C7-U7.2-T04

Read first Study Section 2.4 (Design of a Manufacturing Account): the format with quantity and value columns, prime cost and factory cost, WIP treatment, transfer of cost of finished goods to the Trading Account, and the tutorial notes on deriving missing quantities/figures.

NOTES

Format (SM 2.4): no standardised design, but keep quantity and value columns; Dr — raw material consumed, direct wages, direct expenses (= Prime cost), factory overheads (royalty, hire charges, repairs & maintenance, depreciation) (= Factory cost), opening Work-in-Process; Cr — by-products at net realisable value, closing Work-in-Process, and the balancing transfer By Trading A/c — cost of finished goods; the Trading A/c debits this cost of production (with opening finished goods) against sales and closing finished goods to reveal gross profit.

Tutorial notes: use quantity columns so both sides balance — units sold = opening finished goods + units manufactured – closing finished goods; the Manufacturing A/c shows raw-material quantities and WIP values only, the Trading A/c shows finished-goods quantities only; in the absence of contrary instruction assume sales on FIFO basis, i.e. closing inventory consists as far as possible of goods produced during the year.

Unit-based computations (Illustration 2 — Mr. Vimal): read each rate base carefully — direct wages contracted @ ₹0.80 per unit manufactured PLUS @ ₹0.40 per unit of closing WIP ($5,00,000 \times 0.80 + 12,000 \times 0.40 = ₹4,04,800$); hire charges of machine @ ₹0.60 per unit manufactured are a direct expense, while hire of factory shed and repairs & maintenance are indirect expenses.

Missing-figure problems: derive credit purchases as the balancing figure of the Creditors A/c (To Bank + To Balance c/d – By Balance b/d), post them to the Raw Material A/c and balance it for raw material consumed or closing stock, then complete the Manufacturing A/c to the Trading A/c; exclude office items from the Manufacturing A/c and charge them to P&L (office labour wages, office share of electricity, delivery charges to customers) but keep fuel charges and freight inwards as direct expenses; remember omitted depreciation on unrecorded machinery.

Full manufacturer's final accounts (Illustration 3 — Mr. White): from a trial balance with three inventories prepare Manufacturing, Trading, P&L A/c and Balance Sheet — split shared expenses between factory and office (rent 3/4 : 1/4 by area occupied, lighting 2/3 : 1/3), credit sale of scrap to the Manufacturing A/c, add outstanding wages (Manufacturing) and outstanding salaries (P&L), depreciate plant in Manufacturing and office furniture in P&L, charge only the shortfall of the required provision for doubtful debts over the existing one, and carry all three closing stocks (raw materials, WIP, finished goods) to the Balance Sheet.

Application practise the procedure · 5 questions

- Practise preparing a Manufacturing A/c: Dr --- opening WIP, raw materials consumed, direct wages, direct expenses (unit-based hire charges/royalty), factory overheads; Cr --- by-products at NRV, closing WIP, and cost of finished goods transferred to Trading A/c.
- Drill unit-based computations: direct wages @ ₹x per unit manufactured plus a lower rate per unit of closing WIP, hire charges per unit produced --- read the rate basis carefully, and use quantity columns to check both sides balance.

PQ 4.1 · PYQ 2019-Nov [5] (b) · Practical · 5M · Pg 367 asked 5×	LEVEL II Application	Medium
PQ 4.5 · PYQ 2024-Jun [5] (b) (i) · Practical · 5M · Pg 376 asked 4×	LEVEL II Application	Medium
PQ 4.6 · PYQ 2025-Sep [5] (b) · Practical · 5M · Pg 377	LEVEL II Application	Medium
PQ 4.3 · PYQ 2021-Dec [5] (b) · Practical · 15M · Pg 371 asked 3×	LEVEL II Application	Hard
PQ 4.4 · PYQ 2022-May [5] · Practical · 20M · Pg 373	LEVEL II Application	Hard

Analysis work through mixed data · 1 question

- Work missing-figure problems interlinking Raw Material A/c, Creditors A/c, Manufacturing A/c and Trading A/c: derive credit purchases from the Creditors A/c, balance the Raw Material A/c for consumption, then complete the Manufacturing and Trading A/cs.
- Watch the interlinkages: Manufacturing A/c cost of production becomes the Trading A/c debit; assume FIFO for closing finished-goods valuation unless stated otherwise.

PQ 4.2 · PYQ 2020-Nov [5] (c) · Practical · 10M · Pg 368 asked 2×	LEVEL II Analysis	Hard
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Synthesis prepare end-to-end — no question in this edition

- Master the full 15--20 mark manufacturer's final accounts: Manufacturing, Trading, P&L A/c and Balance Sheet from a trial balance with three inventories (raw materials, WIP, finished goods) and sale of scrap.
- Practise splitting expenses between factory (Manufacturing A/c) and office (P&L A/c) --- rent, power, depreciation --- with the usual adjustments (closing stocks, outstanding wages, provisions) end-to-end.

CHAPTER 8

Financial Statements of Non-Profit Organisations

5 Topics • 36 Classified Questions • Importance: A

ICAI SKILL PROFILE Level I 5–20% • Level II 80–95% — this chapter reads **in line with the paper**

Level I — Remembering & Understanding **7.4%** 18 of 243 marks

Level II — Application & Analysis **92.6%** 225 of 243 marks

Topic 1: Introduction

P1-C8-U8-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §1 Introduction: nature of a non-profit organisation and the set of final accounts it prepares.

NOTES

Non-profit organisation: a legal accounting entity operated for the benefit of society as a whole rather than for a sole proprietor, partners or shareholders — main motive is to render service to society/members; e.g. public hospitals, public educational institutions, clubs, temples, churches.

Final accounts: Receipts and Payments Account plus Income and Expenditure Account to show periodic performance, and Balance Sheet to show financial position at period end.

Terminology: Income and Expenditure A/c is similar to a P&L A/c but excess of income over expenditure = SURPLUS and excess of expenditure over income = DEFICIT; total cash receipts and payments are highlighted through the Receipts and Payments Account.

Topic 2: Nature of Receipts and Payments Account

P1-C8-U8-T02

Read first Read Section 2 'Nature of Receipts and Payments Account' in the ICAI Study Material: its features as a summary of the cash book, its limitations, and (from Section 4.1) fund accounting for special funds like a Sports Fund.

NOTES

Meaning (SM): "A Receipts and Payments Account is a summary of the cash book" without date

column — receipts on the left, payments on the right, same sides as the cash book; an elementary account adopted by hospitals, clubs, societies, temples, churches etc.

Cash basis, not accrual (SM): “receipts and payments account is not based on the accrual system of book keeping as it records all the receipts and payments whether capital or revenue, pertaining to the current, previous or future periods.”

Features: (a) summary of cash and bank transactions — all receipts (capital or revenue) debited, all payments credited; (b) starts with opening cash and bank balances and ends with their closing balances; (c) usually not part of the double entry system; (d) its balance is always debit, being made up of cash in hand and at bank.

Limitations: surplus or deficit for the period CANNOT be ascertained from it — it shows only the cash/bank position, excludes all non-cash items (outstanding/advance subscriptions, depreciation) and mixes capital with revenue and past/future with current-period items; its preparation alone suits only very simple organisations with no assets other than cash and no liabilities.

Fund accounting (4.1): amounts collected for a special purpose (e.g. Sports Fund, match donations and ticket proceeds) are credited to that fund and the related expenses debited to the same fund on the liabilities side — on no account charged to the Income and Expenditure Account; only the expense in excess of the available fund is debited to I&E.

Understanding explain with reasons · 3 questions

- Be able to justify: R&P Account is a summary of cash/bank transactions (cash basis), NOT accrual --- it records all receipts and payments, capital or revenue, of past, current and future periods.
- True/False trap: 'R&P Account highlights total income and expenditure' --- False; it highlights total cash receipts and payments; surplus/deficit cannot be found from it as non-cash items are excluded.
- True/False trap: if a Sports Fund (specific fund) exists, sports-event expenses are charged to that Fund, never to the Income and Expenditure Account --- True (fund accounting).
- Remember it starts with opening cash/bank balances, ends with closing balances, and its balance is always debit.

TQ 2.1 · MTP 2024-Apr [1] (a) (vi) {C} · True/False · 2M · Pg 382 asked 5x	LEVEL I Understanding	Easy
TQ 2.2 · PYQ 2024-Sep [1] (a) (v) {C} · True/False · 2M · Pg 383	LEVEL I Understanding	Easy
TQ 2.3 · MTP 2024-Dec [1] (a) (v) {C} · True/False · 2M · Pg 383 asked 3x	LEVEL I Understanding	Easy

Application work the problem · 1 question

PQ 2.1 · PYQ 2019-Nov [4] (b) · Practical · 10M · Pg 383 asked 2x	LEVEL II Application	Hard
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Analysis work through mixed data — no question in this edition

- Practise the reverse problem: from a given Income and Expenditure Account plus Balance Sheets, work back to the R&P Account by removing accruals (outstanding/advance subscriptions, prepaid and outstanding expenses) and adding capital receipts/payments.
- Master the Subscription Account as a ledger: opening/closing outstanding and advance balances on both sides to derive cash subscriptions received.
- Watch interlinkages: depreciation and non-cash items in I&E must be eliminated; asset purchases and fund receipts appear only in R&P.

Topic 3: Income and Expenditure Account

P1-C8-U8-T03

Read first Study Section 3: features of the Income and Expenditure Account, its distinction from the R&P Account, main sources of income (subscriptions, donations, entrance fees, life membership), and the step-by-step procedure (3.3) for preparing I&E Account from an R&P Account.

NOTES

Nature: the NPO equivalent of the Profit and Loss Account, prepared on the accrual principle — only revenue items pertaining to the current period; Surplus = excess of income over expenditure, Deficit = excess of expenditure over income; non-cash items such as depreciation are included, all capital items excluded, no opening balance; NPOs registered u/s 8 of the Companies Act 2013 prepare I&E and Balance Sheet per Schedule III.

Main sources of income (3.1): subscriptions, ordinary donations, membership/entrance fees (if the amount is normal or per bye-laws), recurring grants from local authorities, income from investments; receipts of a special activity (sale of match tickets) are deducted from that activity's expenditure and only the net shown; capital receipts are credited to Capital Fund or a special fund (fund accounting), sale of a fixed asset to the asset account; life membership fee is a capital receipt (non-recurring) added direct to Capital Fund; trading profit of a separate trading activity is transferred to I&E on consolidation.

Receipts and Payments Account	Income and Expenditure Account
Classified summary of cash receipts and payments, capital or revenue	Only revenue expenditure (Dr) and revenue income (Cr) of the period
Cash basis — items of current, previous or future periods included	Accrual basis — includes amounts fallen due though not received/paid
Starts with opening cash/bank balances; balance always debit	No opening balance; balancing figure is surplus or deficit
Excludes non-cash items; surplus/deficit not	Non-cash items (depreciation) included; reveals

ascertainable

surplus/deficit

R&P → I&E procedure (3.3): (i) compute opening Capital/Accumulated Fund via an opening Balance Sheet (assets – liabilities); (ii) open ledger accounts for incomes/expenses needing accrual or outstanding adjustments and transfer the period amounts to I&E; (iii) post unadjusted items direct from R&P to I&E; (iv) post capital receipts/payments to asset or liability accounts — only capital profit/loss on asset sale enters I&E; (v) transfer the I&E balance to Capital Fund; (vi) prepare the Balance Sheet from the balances left over.

Subscription working: income for the year = cash received + outstanding at close – outstanding at start + advance received in earlier year for this year – advance received this year for next year; e.g. ₹42,000 received (incl. ₹1,600 for last year, ₹600 for next) with ₹3,000 still due → ₹42,800 credited to I&E; closing outstanding subscription is an asset, subscription received in advance a liability.

Understanding explain with reasons · 4 questions

- Explain: I&E Account is the NPO equivalent of P&L, on accrual basis; only current-year revenue items enter; Surplus = excess of income, Deficit = excess of expenditure.
- True/False traps: persons practising a vocation determine net income via I&E/Receipts & Expenditure Account, not P&L; Life Membership Fee is a capital receipt (non-recurring) added to Capital Fund --- 'revenue receipt' is False.
- Trading profit of a society's separate trading activity IS transferred to I&E; additional-information adjustments appear in TWO places (double entry), not one.

TQ 3.1 · RTP 2023-Jun [1] (vii) · True/False · --- · Pg 386 asked 7×	LEVEL I Understanding	Easy
TQ 3.2 · RTP 2023-Dec [1] (ix) · True/False · --- · Pg 386	LEVEL I Understanding	Easy
TQ 3.3 · PYQ 2025-May [1] (a) {C} · True/False · 4M · Pg 386 asked 4×	LEVEL I Understanding	Easy
TQ 3.4 · PYQ 2026-May [1] (a) (v) {C} · True/False · 2M · Pg 387	LEVEL I Understanding	Medium

Application practise the procedure · 7 questions

- Practise the subscription working: cash received ± outstanding (opening/closing) ± advance (opening/closing) = income for the year.
- Drill R&P → I&E conversion: strip capital items, adjust outstanding/prepaid expenses and incomes, charge depreciation, net special-activity income against its fund.
- Revenue-purpose donations are income; specific donations go to fund accounts; only profit/loss on sale of fixed assets enters I&E.

PQ 3.4 • MTP 2024-Dec S1 [4] (a) • Practical • 8M • Pg 394 asked 3×	LEVEL II Application	Medium
PQ 3.5 • RTP 2026-Jan [10] • Practical • 8M • Pg 396	LEVEL II Application	Medium
PQ 3.7 • PYQ 2026-May [5] (b) • Practical • 5M • Pg 402	LEVEL II Application	Medium
PQ 3.1 • PYQ 2018-Nov [5] (a) • Practical • 10M • Pg 387 asked 4×	LEVEL II Application	Hard
PQ 3.2 • PYQ 2019-Jun [5] (b) • Practical • 10M • Pg 389 asked 6×	LEVEL II Application	Hard
PQ 3.3 • PYQ 2021-Jan [4] (b) • Practical • 10M • Pg 392 asked 6×	LEVEL II Application	Hard
PQ 3.6 • RTP 2026-May [10] • Practical • --- • Pg 399	LEVEL II Application	Hard

Synthesis prepare end-to-end — no question in this edition

- Master preparing full R&P and I&E Accounts together from balances at two dates (club or doctor's practice) --- typical 8-10 mark questions.
- Compute opening Capital Fund via opening Balance Sheet, including accrued incomes and outstanding expenses.
- For cash-basis professionals (Dr. Deku type), handle interest on borrowings, depreciation and outstanding items end-to-end.

Topic 4: Balance Sheet

P1-C8-U8-T04

Read first Study Section 4: Capital Fund/Accumulated Fund, treatment of special items (4.1 --- donations, entrance fees, subscriptions, life membership, legacy, endowment fund) and the preparation steps in 4.2.

NOTES

Capital Fund: “the excess of total assets over total outside liabilities is known as Capital Fund” — built from members' legacies, special donations, entrance fees and accumulated surpluses; if members have contributed nothing it is termed “Accumulated Fund”; the year's surplus is added to (deficit deducted from) the fund brought forward.

Special items (4.1): specific donation, legacy (received under a will), entrance/admission fee and life membership fee → capitalise on the liabilities side (added to Capital Fund or a special fund; follow the question if it directs otherwise); general donations and sale of old newspapers → income in I&E; endowment fund — income from it added to, and its expenses deducted from, the fund on the liabilities side; sale of old fixed asset — capital receipt, only the profit/loss on sale enters I&E; honorarium — payment to a non-employee for services, a revenue expense.

“Fund” vs “Account”: the term Fund strictly applies when amounts collected for a special purpose

are invested (Scholarship Fund, Prize Fund) — such investments and accrued income are disclosed separately; when not invested, “Account” is more appropriate (Building Account, Tournament Account); life-member lump sums may alternatively be (1) carried until death, (2) released to I&E yearly at the normal subscription, or (3) spread over expected life.

Preparation steps (4.2): opening Capital Fund = opening assets – opening liabilities, taking prepaid expenses and accrued incomes as assets and outstanding expenses and advance incomes as liabilities; closing cash/bank comes from the R&P Account (bank overdraft → liabilities side); fixed assets: opening balance + purchases – sales – depreciation = closing balance; opening liabilities adjusted for increases/decreases.

Standard workings: only OUTSTANDING subscriptions are a current asset and advance subscriptions a liability (current-year subscriptions received are income, not an asset); consumables (sports material, medicines, foodstuff) charged to I&E = opening stock + purchases (derived through the creditors account) – closing stock; capitalised portion of entrance fees/donations (given %) goes straight to Capital Fund, the rest to I&E.

Understanding explain with reasons · 3 questions

- Capital Fund = excess of total assets over total OUTSIDE liabilities; called Accumulated Fund if members contributed nothing --- a standard True/False.
- True/False trap: subscriptions RECEIVED for the current year are income collected --- not a current asset; only OUTSTANDING subscriptions are an asset (advance subscriptions a liability).
- Capital vs revenue: entrance fees, legacies, life membership, specific donations → capitalise; general donations, recurring grants → income.

TQ 4.1 · MTP 2023-May [1] (a) (vi) {C} · True/False · 2M · Pg 404	LEVEL I Understanding	Easy
TQ 4.2 · MTP 2024-Jul [1] (a) (iii) {C} · True/False · 2M · Pg 404 asked 3x	LEVEL I Understanding	Easy
TQ 4.3 · PYQ 2026-Sep [1] (a) (v) {C} · True/False · 2M · Pg 404	LEVEL I Understanding	Easy

Application practise the procedure · 12 questions

- Practise consumable-stores workings (sports material): opening stock + purchases (via creditors account) – closing stock = amount consumed, charged to I&E.
- Roll fixed assets forward: opening balance + additions – sales – depreciation = closing balance.

PQ 4.11 · RTP 2024-Sep [10] · Practical · --- · Pg 433 asked 9x	LEVEL II Application	Medium
PQ 4.15 · PYQ 2025-Sep [4] (b) · Practical · 8M · Pg 442	LEVEL II Application	Medium
PQ 4.17 · PYQ 2026-Sep [5] (b) · Practical · 5M · Pg 448	LEVEL II Application	Medium

PQ 4.2 • PYQ 2022-May [4] (a) • Practical • 10M • Pg 408	LEVEL II Application	Hard
PQ 4.4 • MTP 2022-Nov S1 [5] (a) • Practical • 15M • Pg 413	LEVEL II Application	Hard
PQ 4.5 • PYQ 2023-Jun [4] (a) • Practical • 15M • Pg 417 asked 4×	LEVEL II Application	Hard
PQ 4.7 • RTP 2023-Dec [16] • Practical • --- • Pg 422 asked 6×	LEVEL II Application	Hard
PQ 4.8 • PYQ 2024-Jun [3] (a) • Practical • 12M • Pg 425	LEVEL II Application	Hard
PQ 4.9 • MTP 2024-Aug [3] (a) • Practical • 15M • Pg 428 asked 4×	LEVEL II Application	Hard
PQ 4.10 • PYQ 2024-Sep [4] (b) • Practical • 10M • Pg 430 asked 5×	LEVEL II Application	Hard
PQ 4.13 • RTP 2025-Jan [10] • Practical • --- • Pg 437 asked 2×	LEVEL II Application	Hard
PQ 4.14 • PYQ 2025-May [3] (a) • Practical • 12M • Pg 440	LEVEL II Application	Hard

Analysis work through mixed data • 5 questions

- Work reverse questions: from I&E Account plus additional information, reconstruct the R&P Account and opening/closing Balance Sheets --- track each adjustment to both its locations.
- Interlinkages: surplus/deficit flows into Capital Fund; specific-fund incomes and expenses (tournament, prize, building) bypass I&E and adjust the fund on the liabilities side.
- Handle pass-book vs cash-book balances, part-year depreciation and given entrance-fee capitalisation percentages.

PQ 4.1 • PYQ 2021-Jan [5] (c) • Practical • 10M • Pg 406 asked 2×	LEVEL II Analysis	Hard
PQ 4.3 • PYQ 2022-Nov [4] (b) • Practical • 10M • Pg 411 asked 2×	LEVEL II Analysis	Hard
PQ 4.6 • PYQ 2023-Dec [2] (b) • Practical • 12M • Pg 419	LEVEL II Analysis	Hard
PQ 4.12 • PYQ 2025-Jan [5] (a) • Practical • 10M • Pg 434	LEVEL II Analysis	Hard
PQ 4.16 • PYQ 2026-Jan [3] (a) • Practical • 10M • Pg 445	LEVEL II Analysis	Hard

Synthesis prepare end-to-end — no question in this edition

- Master the full 10-15 mark chain: opening Capital Fund → I&E Account → closing Balance Sheet from a given R&P Account.
- Drill typical adjustments: outstanding/advance subscriptions at both ends, prepaid and outstanding expenses, depreciation, funds with earmarked investments and accrued interest, capitalised entrance fees/legacies.

Topic 5: Educational Institution

P1-C8-U8-T05

Read first Study Section 5 'Educational Institutions': sources of finance (donations, fees, four kinds of Government grants), and treatment of specific items --- donations from public, capitation/admission fees, laboratory and library deposits, and use of term fees.

NOTES

Three sources of finance (5.1): (1) donations from the public; (2) fees — annual tuition fees, term fees, admission fees, laboratory fees etc.; (3) Government grants — of four kinds: Maintenance Grant, Equipment Grant, Building Grant and such other grants as sanctioned from time to time.

Grants: Maintenance Grant is recurring and received in instalments spread through the year — revenue income of I&E; Equipment and Building grants are capitalised; grant-in-aid usable per the School Code for staff salaries, rent-taxes-insurance, repairs, prizes, audit fees etc.; institutions are mostly Societies under the Societies Registration Act 1860 and all follow the financial year.

Specific items (5.2): public donations may be for recurring or non-recurring purposes, in cash or kind (land and building, shares, furniture); capitation/admission fees are collected by the Parent Body running the institution (such collections now severely attacked and banned); laboratory and library deposits collected from students remain with the institution till the student finally leaves — refundable, hence shown on the liabilities side of the Balance Sheet.

Term fees: a separate account of receipts and expenditures is maintained and the surplus carried over to the next year; usable for medical inspection, school magazine, examination expenses, tournaments, sports and games, newspapers, excursions, prizes, scouting, school band and similar co-curricular activities.

Exam pattern (Illustration 13 — Republic College): tuition and other fees (plus fees receivable from Government for backward-class scholars), revenue Government grants and net seminar/consultancy/hostel/mess receipts are income; security deposits of students, Provident Fund, Research and Building Funds appear on the liabilities side with their earmarked investments shown separately as assets; stores profit computed via net-profit % on sales; surplus added to Capital Fund.

Understanding explain with reasons — no question in this edition

- True/False: laboratory and library deposits taken from students are refundable when the student leaves, so they are shown on the liabilities side of the Balance Sheet --- True.
- Distinguish grants: maintenance grant is recurring income; equipment and building grants are capitalised.
- Know the three finance sources: public donations, fees (tuition, term, admission, laboratory), and Government grants.

Application work the problem · 1 question

PQ 5.1 · PYQ 2020-Nov [4] (b) · Practical · 10M · Pg 449

LEVEL II
Application

Hard

Synthesis prepare end-to-end — no question in this edition

- Master preparing an I&E Account and Balance Sheet for a college from a list of balances: tuition/admission fees as income, security deposits from students as liability, Capital Fund with surplus added.
- Practise adjustments typical of these questions: outstanding tuition fees, prepaid expenses, depreciation on buildings/equipment, grants received during the year.
- Present funds (building fund, scholarship fund) and their earmarked investments separately from the Capital Fund.

CHAPTER 9

Accounts from Incomplete Records

4 Topics · 23 Classified Questions · Importance: C

ICAI SKILL PROFILE Level I 5–20% · Level II 80–95% — this chapter reads **almost entirely problem-solving**

 Level I — Remembering & Understanding **0.0%** 0 of 165 marks

 Level II — Application & Analysis **100.0%** 165 of 165 marks

Topic 1: Introduction

P1-C9-U9-T01

Read first Read Section 1 'Introduction' and Section 2 'Types of Single Entry System' of the ICAI Study Material --- what incomplete records are, why they arise, the features of the single entry system, and its three types (pure, simple, quasi).

NOTES

Meaning (SM): “There is no such formal system as Single-Entry System as the accounts can only be prepared using Double Entry System” — single entry is truly a system of incomplete or improper records: for some transactions both aspects are entered, for some only one, for others none; normally only cash receipts/payments and personal accounts (receivables, payables, capital) are kept.

Why records are incomplete: lack of accounting knowledge, business too small to justify the time/effort, records destroyed by accident such as fire, or an essential figure unknown and to be derived as a balancing figure (e.g. inventory damaged or destroyed).

Five features of Single Entry System: (1) inaccurate, unscientific and unsystematic method of recording; (2) generally no record of real and nominal accounts — mostly only cash transactions and personal accounts; (3) cash book mixes up business and personal transactions of the owner; (4) no uniformity — the system differs from firm to firm per each firm's convenience; (5) profit is only an estimate from available information, so true profit and financial position cannot be determined.

Three types (Sec 2): pure single entry — only personal accounts (no cash/bank, sales or purchases data; exists only on paper); simple single entry — personal accounts + cash book; quasi single entry — personal accounts + cash book + some subsidiary books (Sales book, Purchases book, Bills book; discounts entered in personal accounts) — the type generally adopted as a substitute for double entry.

Remembering memorise · 1 question

- Memorise the five Features of Single Entry System for the short note: (1) inaccurate, unscientific and unsystematic method; (2) generally no real and nominal accounts --- only cash transactions and personal accounts recorded; (3) cash book mixes business and personal transactions of the owner; (4) no uniformity --- the system differs from firm to firm; (5) profit is only an estimate, so true profit and financial position cannot be determined.
- Also remember the three types: pure single entry (only personal accounts), simple single entry (personal accounts + cash book), quasi single entry (personal accounts + cash book + some subsidiary books).
- Note: 'single entry' is really a system of incomplete records --- accounts can only properly be prepared under double entry.

TQ 1.1 · RTP 2025-May [18] (iv) · Short Note · --- · Pg 454

LEVEL I
Remembering**Easy****Topic 2: Types of Single Entry System**

P1-C9-U9-T02

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2 of the unit: the three types of single entry system with the M/s Small shop and t-shirt shop examples.

NOTES

Pure single entry: only personal accounts are maintained — no information on cash and bank balances, sales, purchases etc.; exists only on paper with no practical application.

Simple single entry: only personal accounts and cash book are maintained; postings from cash book go only to personal accounts, and cash received from debtors/paid to creditors is simply noted on the bills issued or received.

Quasi single entry: personal accounts, cash book and some subsidiary books (Sales book, Purchases book, Bills book) are maintained; discounts have no separate record and are entered in personal accounts, with scattered information on expenses like wages, rent, rates — this is the method generally adopted as a substitute for double entry.

Topic 3: Ascertainment of Profit by Capital Comparison

P1-C9-U9-T03

Read first Study Section 3: the Net Worth/Statement of Affairs method --- the profit formula, preparation of Statements of Affairs at two dates (3.3), and the differences between a Statement of Affairs and a Balance Sheet (3.2).

NOTES

Net Worth / Statement of Affairs method — Formula: Profit = Closing capital + Drawings – Fresh capital introduced – Opening capital; alternatively profit is the balancing figure of the Capital Account (Dr: drawings, closing balance c/d; Cr: opening balance b/d, additional capital, net profit).

Statement of Affairs: Capital = Assets – Liabilities, prepared at the two dates; sources of figures — cash book for cash, bank pass book for bank, personal ledger for debtors/creditors, inventory by actual counting and valuation, fixed assets listed and included at written-down value after reasonable depreciation.

Statement of Affairs	Balance Sheet
Partly double/partly single entry; rests on estimates, assumptions, memory	Strictly double entry; every item verifiable from ledger and documents
Capital is merely the balancing figure — assets need not equal liabilities	Capital from the Capital A/c in the ledger; two sides always equal
Omitted assets/liabilities very difficult to identify	No omission possible; a missing item stops the sheet agreeing
Assets valued arbitrarily; no valuation method disclosed	Scientific valuation — cost less depreciation; changes disclosed
Object: find opening and closing capital figures	Object: show financial position on a particular date

Adjustments before comparison: closing assets marked “?” are derived first (e.g. depreciate opening building 2.5% and furniture 10% to get closing values); matured LIC money of the proprietor retained in business = fresh capital (deduct); monthly household withdrawals (₹2,000 p.m. × 12) added back as drawings; likewise handle accrued interest, bad debts/provisions, and apply drawings and interest proportionately for periods longer than a year.

Income-Tax-Officer pattern (Illustration 5): compute capitals from assets/liabilities at the two dates, then income of the period = closing capital + domestic drawings (₹4,000 × 24 months) – opening capital; compare with declared income — the excess is suppressed income, supporting the ITO's contention.

Analysis work through mixed data · 3 questions

- Master the formula: Profit = Closing capital + Drawings – Fresh capital introduced – Opening capital; alternatively find profit as the balancing figure of the Capital Account.

- Practise multi-step problems: prepare Statements of Affairs at both dates first (Capital = Assets – Liabilities), where some assets are '?' and must be derived --- e.g., closing building/furniture after depreciation on opening values.
- Work the Income-Tax-Officer pattern (undisclosed income): compare capitals over two years, adjust drawings/household expenses, additions to assets and fresh capital to estimate real income for each year.
- Watch adjustments before comparison: depreciation, accrued interest, bad debts/provisions, and periods longer than one year (e.g., 15-month accounts) --- apply drawings and interest proportionately.

PQ 3.2 · MTP 2024-Jul [5] (b) · Practical · 5M · Pg 457

LEVEL II
Analysis

Medium

PQ 3.3 · PYQ 2025-Jan [4] (b) · Practical · 5M · Pg 459

LEVEL II
Analysis

Medium

PQ 3.1 · PYQ 2022-Nov [3] (b) · Practical · 10M · Pg 455

LEVEL II
Analysis

Hard

Topic 4: Techniques of Obtaining Complete Accounting Information

P1-C9-U9-T04

Read first Study Section 4: the conversion method --- Cash and Bank Summary (4.2), analysis of sales and purchase ledgers with proforma Total Debtors, Total Creditors and Bills Receivable/Payable Accounts (4.3), distinction between business expenses and drawings (4.4), and building final accounts from these.

NOTES

Conversion method (4.1): preferable to mere capital comparison — start the ledger with opening balances of assets, liabilities and capital (opening Statement of Affairs), complete the double entry by posting unposted aspects from the cash book and each subsidiary book, draw up a Trial Balance, then prepare Trading and P&L Account and Balance Sheet; unidentified receipts/shortfalls of cash go to the Capital Account (credit fresh capital, debit drawings).

Cash and Bank Summary (4.2): tabulate all cash/bank receipts and payments under significant heads with both sides tallied and closing balances reconciled; a short debit side signals a missing receipt — usually CASH SALES — and a short credit side a missing payment, taken as the balancing figure.

Total Debtors / Creditors / Bills accounts (4.3): Total Debtors — Dr: opening balance, credit sales, bills/cheques dishonoured, interest; Cr: cash/bank received, discount allowed, B/R received, sales returns, bad debts, closing balance; Total Creditors — Dr: cash/bank paid, discount received, purchase returns, B/P accepted, B/R endorsed, closing balance; Cr: opening balance, credit purchases, B/P dishonoured; any ONE missing figure (credit sales, credit purchases, bad debts, cash received...) emerges as the balancing figure; endorsed and dishonoured bills affect TWO

accounts, and debtor–creditor ledger transfers need contra entries.

Shortcut — credit purchases: cash paid to creditors (including on bills payable) + closing creditors and B/P – opening creditors and B/P; **drawings vs business expenses (4.4):** drawings include the residence share of common rent/electricity/telephone (allocate equitably), proprietor's LIC premium, household expenses, private loans/gifts from business cash, goods taken for personal use; fresh capital includes LIC maturity money, interest/dividend on private investments brought in, and business expenses/creditors paid from private funds (Dr expense or asset, Cr Capital).

Full-question chain: opening Statement of Affairs → Cash and Bank Summary → Total Debtors, Total Creditors, B/R and B/P accounts → Trading and P&L Account → closing Balance Sheet; plug missing sales, purchases or closing/lost stock using gross profit % (e.g. GP 25% on sales) or credit-period ratios (1.5 months' credit ⇒ closing debtors = credit sales × 1.5 ÷ 12) and cash-to-credit sales mix; end-to-end adjustments — depreciation, outstanding/prepaid expenses, provision for doubtful debts, interest on loans for the broken period; in partnership variants distribute the net profit in the agreed ratio through partners' capital accounts and tally with the closing Balance Sheet.

Application work the problem · 14 questions

PQ 4.11 · MTP 2024-Dec S1 [3] (b) · Practical · 8M · Pg 486	LEVEL II Application	Medium
PQ 4.17 · RTP 2026-May [11] PQ · Practical · ---- · Pg 500	LEVEL II Application	Medium
PQ 4.1 · PYQ 2018-Nov [3] (a) · Practical · 15M · Pg 461	LEVEL II Application	Hard
PQ 4.2 · PYQ 2019-Nov [4] (b) · Practical · 10M · Pg 464 asked 5×	LEVEL II Application	Hard
PQ 4.3 · PYQ 2020-Nov [2] (b) · Practical · 10M · Pg 467	LEVEL II Application	Hard
PQ 4.4 · PYQ 2021-Jan [2] (b) · Practical · 10M · Pg 469	LEVEL II Application	Hard
PQ 4.5 · PYQ 2021-Jul [3] (b) · Practical · 10M · Pg 472	LEVEL II Application	Hard
PQ 4.7 · PYQ 2022-May [3] (a) · Practical · 12M · Pg 477	LEVEL II Application	Hard
PQ 4.8 · MTP 2024-May [4] (b) · Practical · 10M · Pg 480 asked 3×	LEVEL II Application	Hard
PQ 4.9 · PYQ 2024-Jun [4] (b) · Practical · 8M · Pg 483 asked 3×	LEVEL II Application	Hard
PQ 4.13 · RTP 2025-Jan [11] · Practical · ---- · Pg 490	LEVEL II Application	Hard
PQ 4.14 · PYQ 2025-Sep [3] (a) · Practical · 12M · Pg 494	LEVEL II Application	Hard

PQ 4.18 · PYQ 2026-May [3] (b) · Practical · 10M · Pg 503	LEVEL II Application	Hard
PQ 4.19 · PYQ 2026-Sep [3] (a) · Practical · 10M · Pg 506	LEVEL II Application	Hard

Analysis work through mixed data · 5 questions

- Practise deriving single missing figures as balancing figures: credit sales/credit purchases from Total Debtors/Total Creditors Accounts; bad debts from the Debtors Account (given cash received, discounts, B/R, returns); cash sales from the Cash and Bank Summary.
- Drill ratio-based deductions: debtors' credit period → credit sales (e.g., 1.5 months' credit means closing debtors = 1.5/12 of credit sales), cash-to-credit sales mix, and gross profit as a fixed % of sales to complete the Trading Account or find stock lost/missing inventory.
- Watch discount allowed/received, bills dishonoured and endorsed bills --- each affects two accounts; transfers between debtors and creditors ledgers need contra entries.

PQ 4.6 · PYQ 2021-Dec [6] (e) · Practical · 5M · Pg 476	LEVEL II Analysis	Medium
PQ 4.10 · PYQ 2024-Sep [5] (Or) (b) (ii) · Practical · 5M · Pg 485	LEVEL II Analysis	Medium
PQ 4.12 · MTP 2024-Dec S1 [5] (b) · Practical · 5M · Pg 489 asked 2×	LEVEL II Analysis	Medium
PQ 4.15 · RTP 2025-Sep [11] · Practical · ---- · Pg 497 asked 2×	LEVEL II Analysis	Medium
PQ 4.16 · PYQ 2026-Jan [5] (b) · Practical · 5M · Pg 499	LEVEL II Analysis	Medium

Synthesis prepare end-to-end — no question in this edition

- Master the full 10-16 mark conversion question: opening Statement of Affairs → Cash/Bank Summary → Total Debtors, Total Creditors, Bills accounts → Trading and P&L Account → closing Balance Sheet.
- Practise standard adjustments end-to-end: depreciation, outstanding/prepaid expenses, provision for doubtful debts, drawings (including goods withdrawn and expenses met from private funds credited to capital), and gross-profit-percentage workings to find sales or purchases.
- For partnership variants (Stevie & Alicia type), close with profit distribution in the agreed ratio and partners' capital accounts; always tally with a closing Balance Sheet.

CHAPTER 10

Partnership and LLP Accounts

46 Topics · 82 Classified Questions · Importance: C

ICAI SKILL PROFILE Level I 5–20% · Level II 80–95% — this chapter reads **in line with the paper**Level I — Remembering & Understanding **11.1%** 64 of 574 marksLevel II — Application & Analysis **88.9%** 510 of 574 marks

Unit 10.1: Introduction to Partnership Accounts

P1-C10-U10.1 · Importance D · Rank 1 in chapter · Category A · 23.2% of chapter questions · 19 questions

Topic 1: Introduction: Why Partnership?

P1-C10-U10.1-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation**Read first** Read §1.1 of the unit: rationale for pooling resources when a sole proprietor cannot cope alone.

NOTES

Why partnership: a sole proprietor may not be in a position to cope with the financial and managerial demands of present-day business, so two or more individuals pool their financial and non-financial resources to carry on a business — the succeeding units then cover final accounts of firms and admission, retirement and death of a partner.

Topic 2: Definition and Features of Partnership

P1-C10-U10.1-T02

Read first Read Section 4 definition of partnership under the Indian Partnership Act, 1932 and the features of partnership (agreement, business, sharing of profit, mutual agency, minor as partner, number of partners) in Sec 1.2 of the Study Material.

NOTES

Sec 4, Indian Partnership Act, 1932 (SM): “Partnership is the relation between persons who have agreed to share the profit of a business carried on by all or any of them acting for all.”

Six features: (a) agreement — arises from contract, not status (unlike HUF); written deed not necessary (Sec 5); (b) business — includes every trade, occupation and profession (Sec 2(b)); (c) sharing of profit — Sec 4 does not insist on sharing of LOSSES, so a loss-sharing clause is not essential; (d) mutual agency — business carried on by ALL or ANY of them acting for all, partners stand as principals and agents of one another; (e) minor — may be admitted to share PROFITS only, cannot be made to share losses (losses borne by major partners in PSR); (f) number of partners — minimum 2, maximum 50 (Rule 10, Companies (Incorporation) Rules, 2014 under Sec 464, Companies Act, 2013).

Key inferences: business need NOT be carried on by every partner (mutual agency suffices); PSR is fixed by agreement and is independent of capital ratio — absent agreement, profits are shared EQUALLY, never in capital ratio.

Understanding explain with reasons · 2 questions

- Be able to justify True/False: business may be carried on by ALL or ANY of the partners acting for all (mutual agency) --- it need not be carried on by every partner.
- Explain why profit sharing ratio and capital contribution ratio need not be the same --- PSR is fixed by agreement; in absence of agreement profits are shared EQUALLY, not in capital ratio.
- Know the reasoning behind each feature: partnership arises from contract (not status like HUF), sharing of losses is not essential per Sec 4, and a minor can be admitted only to profits.
- Remember limits for reasons: minimum 2 partners, maximum 50 (Rule 10 of Companies (Incorporation) Rules, 2014 under Sec 464 of Companies Act, 2013).

TQ 2.1 · PYQ 2005-Nov [5] (xi) · True/False · 2M · Pg 510 **asked 3x**

LEVEL I
Understanding

Easy

TQ 2.2 · PYQ 2025-Sep [1] (a) (iii) {C} · True/False · 2M · Pg 511

LEVEL I
Understanding

Easy

Topic 3: Limited Liability Partnership

P1-C10-U10.1-T03

Read first Study Sec 1.3 of the Study Material: definition of LLP and small LLP (LLP Act, 2008 as amended in 2021), nature of LLP, designated partners (Sec 7), their liabilities, limitation of liability, and financial disclosures.

NOTES

Definition (Sec 2, LLP Act, 2008): LLP is “a partnership formed and registered under this Act”; the LLP agreement is a written agreement between partners (or LLP and partners) fixing mutual rights

and duties. **Small LLP (2021 Amendment):** contribution $\leq$ ₹25 lakh (prescribable up to ₹5 crore) AND preceding-year turnover per Statement of Accounts and Solvency $\leq$ ₹40 lakh (prescribable up to ₹50 crore).

Nature: body corporate, legal entity SEPARATE from its partners, perpetual succession; change in partners does not affect its existence, rights or liabilities; the Indian Partnership Act, 1932 does NOT apply to an LLP (Sec 1.3.3).

Partners: any individual or body corporate; an individual is disqualified if found of unsound mind, an undischarged insolvent, or with insolvency application pending; minimum 2 partners — if reduced below 2 and business carried on beyond 6 months, the sole partner (with knowledge) becomes personally liable for obligations of that period.

Designated partners (Sec 7): at least two, who are INDIVIDUALS, at least one resident in India (stayed $\geq$ 120 days in the immediately preceding year); prior consent needed and particulars filed with Registrar within 30 days of appointment; they are responsible for all acts/compliances under the Act (filing documents, returns, statements) and liable to ALL penalties imposed on the LLP for contravention.

Liability and disclosures: obligations of the LLP are solely its own, met out of LLP property; a partner is not personally liable merely by being a partner; liability is UNLIMITED where partners act with intent to defraud creditors; books on cash or accrual basis under double entry, Statement of Account and Solvency within 6 months of year-end signed by designated partners and filed with Registrar; audit as prescribed (classes may be exempted).

Remembering — memorise — no question in this edition

- Memorise for short notes: every LLP must have at least 2 designated partners who are individuals, at least one resident in India (stayed in India not less than 120 days in the preceding year); prior consent and filing with Registrar within 30 days.
- Liabilities of designated partners: responsible for all acts/compliances under the LLP Act (filing documents, returns, statements) and liable to all penalties imposed on the LLP for contravention.
- Extent of liability of LLP and partners: LLP's obligations met solely out of LLP property; partner not personally liable merely by being a partner; liability unlimited in case of fraud.

Understanding — explain with reasons · 4 questions

- Explain the NATURE of LLP: body corporate, separate legal entity from partners, perpetual succession, change in partners does not affect its existence.
- Classic True/False trap: LLP is NOT governed by the Indian Partnership Act, 1932 --- it is governed by the LLP Act, 2008 (Sec 1.3.3: non-applicability of the 1932 Act).
- In absence of agreement, partners share profits EQUALLY, not in capital contribution ratio --- be ready with the statutory reason.
- Know who CAN be a partner (individual or body corporate) and who cannot (unsound mind, undischarged insolvent, insolvency application pending).

TQ 3.1 · PYQ 2019-Jun [1] (a) (v) · True/False · 2M · Pg 511	LEVEL I Understanding	Easy
TQ 3.3 · MTP 2024-Jun [1] (a) (iv) {C} · True/False · 2M · Pg 512 asked 2×	LEVEL I Understanding	Easy
TQ 3.4 · PYQ 2025-May [1] (a) {C} · True/False · 4M · Pg 513	LEVEL I Understanding	Easy
TQ 3.2 · PYQ 2022-May [4] (b) DESC 5 Marks · · --- · Pg 511	LEVEL I Understanding	Medium

Topic 4: Distinction Between an Ordinary Partnership Firm and An LLP

P1-C10-U10.1-T04

Read first Learn the tabular distinction between an ordinary partnership firm and an LLP given in Sec 1.4 of the Study Material (14 points of difference).

NOTES

Sec 1.4 (14 bases; table: LLP vs ordinary firm): other bases — creation by legal process of registration vs by agreement; name must carry 'LLP' suffix vs any name; only designated partners answerable for compliances vs all partners.

Regulating Act: LLP Act, 2008	Indian Partnership Act, 1932
Body corporate — separate legal entity; owns assets in its own name	No separate legal entity; partners own the firm's assets jointly
Perpetual succession — death/insanity/retirement/insolvency of partner no effect	No perpetual succession; such events may affect existence
Liability limited to agreed contribution (unlimited only for wilful fraud)	Liability unlimited — extends to personal assets of partners
Partner binds the LLP by his acts, but NOT the other partners	Each partner binds the firm AND the other partners
Registration mandatory; minimum 2, NO maximum; ≥2 designated partners	Registration voluntary (only registered firm can sue); maximum 50 partners
Foreign nationals can be partners; minor CANNOT be admitted to benefits	Foreign nationals cannot; minor admissible to benefits with partners' consent

Understanding explain with reasons — no question in this edition

- Be able to differentiate on the exact bases asked in exams: applicable/regulating law (LLP Act, 2008 vs Indian Partnership Act, 1932), perpetual succession (LLP unaffected by death/insolvency of partners), ownership of assets (LLP owns assets as separate legal entity; firm's partners own jointly), and liability (limited to agreed contribution vs unlimited).
- Explain the principal-agent relationship difference: in a firm each partner binds the firm AND other partners; in an LLP a partner binds only the LLP, not co- partners.
- Also revise: registration (mandatory for LLP, voluntary for firm), maximum partners (no limit vs 50), designated partners, foreign nationals and minors.

Analysis break down and compare · 1 question

TQ 4.1 · PYQ 2022-Nov [4] (b) · Descriptive · 5M · Pg 513

LEVEL II
Analysis**Hard****Topic 5: Main Clauses in A Partnership Deed**

P1-C10-U10.1-T05

Read first Study Sec 1.5: the 14 usual clauses of a Partnership Deed and, critically, the rules applicable in the ABSENCE of a partnership deed under the Indian Partnership Act, 1932.

NOTES

14 usual clauses: (1) name of firm and partners; (2) commencement and duration; (3) capital of each partner; (4) drawings allowed and their timing; (5) rates of interest on capital, on partner's loan and on drawings; (6) profit/loss sharing ratio; (7) partner's salary; (8) variations in mutual rights and duties; (9) method of valuing goodwill on change in constitution; (10) retirement procedure and payment of dues; (11) determination and payment of deceased partner's executors' dues; (12) treatment of losses from a partner's insolvency; (13) dispute-settlement procedure; (14) preparation and audit of accounts.

Rules in ABSENCE of deed (Act applies): NO salary to any partner; NO interest on capital; NO interest on drawings; interest @6% p.a. on a partner's LOAN to the firm; profits and losses shared EQUALLY (not in capital ratio) — deed clause, where it exists, overrides these defaults.

Registration: registration of the firm is not compulsory, but non-registration restricts the partners/firm from taking legal action.

Adjustment for wrong/omitted appropriation: compute per partner the amount already credited vs amount due, reverse the excess (recovery increases divisible profit, re-credited in PSR), and pass ONE entry for the net effect through capital/current A/cs — e.g. interest credited @12% instead of 10% (A:B:C = 2:3:5, capitals 15L:30L:60L): Dr. C's Current A/c ₹15,000, Cr. A ₹12,000, Cr. B ₹3,000.

Understanding explain with reasons · 4 questions

- Memorise and be able to justify the default rules when there is no deed: no partner's salary, no interest on capital, no interest on drawings, interest @ 6% p.a. on partner's LOAN to the firm, and profits/losses shared EQUALLY.
- True/False traps seen repeatedly: 'profits shared in capital ratio without agreement' is FALSE (equal sharing); 'interest on partner's loan @ 6% when no deed' is TRUE; 'a partnership firm cannot own assets' is TRUE only for an ordinary firm (no separate legal entity) --- assets are jointly owned by partners.
- Be ready for a 5-mark descriptive answer listing the rules if there is no partnership agreement, with section-based reasoning.

TQ 5.1 · PYQ 2005-May [5] (viii) · True/False · 2M · Pg 514	asked 13×	LEVEL I Understanding	Easy
TQ 5.2 · PYQ 2018-May [1] (a) (v) {C} · True/False · 2M · Pg 515	asked 3×	LEVEL I Understanding	Easy
TQ 5.3 · PYQ 2019-Nov [1] (a) (v) {C} · True/False · 2M · Pg 515	asked 4×	LEVEL I Understanding	Easy
TQ 5.4 · PYQ 2021-Jan [6] (b) · Descriptive · 5M · Pg 515		LEVEL I Understanding	Medium

Application practise the procedure · 1 question

- Practise numerical settlement of disputes/appropriations applying deed provisions: salary to a partner, interest on fixed capitals, and division of balance profit.
- Practise adjustment/rectification entries when appropriations (e.g., interest at wrong rate) are omitted or wrongly recorded --- compute net effect partner-wise and pass one adjusting journal entry through capital/current accounts.

PQ 5.1 · PYQ 2021-Dec [3] (c) · Practical · 5M · Pg 516	asked 7×	LEVEL II Application	Medium
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Topic 6: Powers of Partners

P1-C10-U10.1-T06

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.6: implied powers of a partner of a trading firm and the acts for which an individual partner cannot bind the firm.

NOTES

Implied powers (trading firm): unless public notice to the contrary, a partner's contracts bind the firm — (a) buying and selling goods, (b) receiving payments and giving valid receipts, (c) drawing cheques and drawing/accepting/endorsing bills of exchange and promissory notes in the firm's

name, (d) borrowing money with or without pledging inventories-in-trade, (e) engaging servants for the firm's business.

No implied power (all partners must agree): submitting a firm dispute to arbitration, opening a bank account in a partner's name, compromise/relinquishment of any claim, withdrawal of a suit filed on behalf of the firm, admission of liability in a suit against the firm, acquisition of immovable property belonging to the firm, entering into partnership on behalf of the firm; rights, duties and powers can be changed by mutual consent.

Topic 7: Accounts

P1-C10-U10.1-T07

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §1.7: how partnership accounts differ from a sole proprietorship's only in capital and drawings accounts.

NOTES

Accounts of a firm: the Partnership Act specifies no format, so accounts follow basic rules; the only difference from a sole proprietorship is that instead of one Capital Account there are as many Capital Accounts as partners, each credited with the capital brought in by that partner.

Drawings: money taken by a partner for domestic purposes is debited to his Capital A/c or to a separate Drawings A/c (often called Current A/c); the Drawings A/c may be transferred to Capital A/c for a net figure, but often remains separate — hence a firm's trial balance may show both Capital and Drawings accounts.

Topic 8: Profit and Loss Appropriation

P1-C10-U10.1-T08

Read first Study Sec 1.8: preparation of the Profit and Loss Appropriation Account (salary, commission, interest on capital and drawings, transfer to reserve, division of balance) and Sec 1.9.3 on guarantee of minimum profit.

NOTES

Technique: net profit is transferred from P&L A/c to the credit of P&L Appropriation A/c; debit partners' salary/commission and interest on capital (Dr. P&L Appropriation A/c, Cr. Partner's Capital/Current A/c), credit interest on drawings, transfer to reserve if required, then divide the

balance in PSR; DRAWINGS themselves never appear in the Appropriation A/c.

If no deed: interest on partner's loan @6% is first deducted from profit, then no salary, no interest on capital/drawings, and the remainder shared equally — e.g. profit ₹50,600 less loan interest ₹600 ($₹20,000 \times 6\% \times 6/12$) = ₹50,000 split ₹25,000 : ₹25,000.

Guarantee of minimum profit (Sec 1.9.3): if the guaranteed partner's normal share $\geq$ guaranteed amount, allocate normally; if less, he takes the minimum and the deficiency is borne by (a) one remaining partner, (b) two/all partners in agreed ratio, or (c) remaining partners in their MUTUAL PSR — if the question is silent, burden falls on remaining partners in mutual PSR.

Guarantee with interest on capital: first charge interest on capital (and salary) in the Appropriation A/c, compute the guaranteed partner's share of the REMAINING profit, compare with the guarantee, and debit the shortfall to the guaranteeing partner(s)' share — same drill when a new partner admitted for e.g. 1/6th share is guaranteed a minimum, deficiency adjusted against old partners.

Application practise the procedure · 3 questions

- Practise the standard format: Net profit b/d, less appropriations (partner's salary, interest on capital), add interest on drawings, then divide remaining profit in PSR; remember drawings themselves never appear in the Appropriation Account.
- Master guaranteed-minimum-profit problems: if guaranteed partner's normal share falls short, the deficiency is borne (a) by the firm, (b) by one guaranteeing partner, or (c) by remaining partners in agreed or mutual PSR --- practise all three cases in Appropriation Account form.
- Practise guarantee combined with interest on capital at a given rate (e.g., 5% p.a.) --- compute the guaranteed partner's share AFTER charging interest, then charge the shortfall to the guarantor.
- Work sums like admission of a partner for 1/6th share with a guaranteed profit --- compare 1/6 of total profit with the guaranteed figure and adjust deficiency against old partners.

PQ 8.1 · PYQ 2005-May [4] (b) · Practical · 8M · Pg 518 asked 5×

LEVEL II
Application

Medium

PQ 8.2 · PYQ 2023-Jun [4] (b) · Practical · 5M · Pg 519 asked 2×

LEVEL II
Application

Medium

PQ 8.3 · PYQ 2023-Dec [4] (b) · Practical · 5M · Pg 520

LEVEL II
Application

Medium

Topic 9: Fixed and Fluctuating Capital

P1-C10-U10.1-T09

Read first Study Sec 1.9: fixed capital method (capital + current accounts) vs fluctuating capital method, interest on capital and drawings (product method), effective capital ratio and profit sharing in capital ratio.

NOTES

Two methods: **FIXED** — capital A/c frozen at contribution; interest, salary, profit share and drawings pass through a **CURRENT A/c**; interest on capital computed on capital A/c balance only (never on current A/c). **FLUCTUATING** — no current A/c, all items pass through capital A/c, so the balance changes constantly. **Link:** fluctuating capital balance = fixed capital + current A/c balance.

Interest on capital: allowed only if agreed, and only out of profits; full year on opening balance plus proportionate interest on additions/withdrawals — **product method:** $\Sigma(\text{amount} \times \text{months outstanding}) \times \text{rate}/100 \times 1/12$; in case of net LOSS no interest; if profit is insufficient (< total interest), distribute the profit in capital ratio.

Interest on drawings: unequal drawings — product method ($\Sigma \text{amount} \times \text{months to year-end}$, interest at rate for one month); dates not given — 6 months on total drawings; equal monthly drawings — $6\frac{1}{2}$ months if at beginning of each month, $5\frac{1}{2}$ if at end; quarterly drawings — total $\times \text{rate} \times 7.5/12$ if at beginning of each quarter, $\times 4.5/12$ if at end; entry: Dr. Partner's Capital (or Current) A/c, Cr. P&L Appropriation A/c.

Capital ratio (Sec 1.9.4): where profits are shared in capital ratio — fixed capitals give the ratio directly; fluctuating capitals with introductions/withdrawals need month-wise weighted-average (effective) capital per partner; then prepare capital AND current A/cs (salary, interest on capital/drawings through current A/cs under fixed method) and, after rectifying errors in net profit, the P&L Appropriation A/c and revised Balance Sheet.

Application practise the procedure · 3 questions

- Practise interest on capital with additions/withdrawals during the year using the product method ($\text{amount} \times \text{months} \times \text{rate}/12$); under fixed capital method interest is computed on capital account balance only, not on current account.
- Practise interest on drawings: unequal drawings by product method; if dates not given take 6 months average; monthly drawings at beginning 6.5 months, at end 5.5 months; quarterly at beginning 7.5/12, at end 4.5/12.
- Practise computing effective capital month-wise when profits are shared in the ratio of effective capital, then prepare capital and current accounts (salary, interest on capital/drawings credited/debited to current accounts under fixed method).

PQ 9.3 · PYQ 2025-Jan [3] (b) · Practical · 5M · Pg 527

LEVEL II
Application

Medium

PQ 9.4 · RTP 2025-Jan [12] (a) · Practical · --- · Pg 528 asked 2×

LEVEL II
Application

Medium

PQ 9.1 · MTP 2022-Mar [4] (a) · Practical · 20M · Pg 521 asked 2×

LEVEL II
Application

Hard

Analysis work through mixed data · 1 question

- Work backward-calculation situations: given closing capitals AFTER profit division and drawings, reconstruct opening capitals, then recompute interest on capital/drawings omitted earlier and pass a single adjustment entry --- trace the net effect on each partner.
- Watch interlinkage: profit wrongly divided in PSR vs amounts that should first go as interest --- the correction ratio differs from the PSR.

PQ 9.2 · RTP 2023-Jun [13] · Practical · ---- · Pg 526 asked 2×

LEVEL II
Analysis

Medium

Synthesis prepare end-to-end — no question in this edition

- Master end-to-end preparation from a trial balance/balance sheet: rectify errors to arrive at corrected net profit, prepare P&L Appropriation Account, partners' capital AND current accounts, and the revised Balance Sheet.
- Remember: fluctuating capital balance = fixed capital + current account balance; show interest, salary, share of profit and drawings in the correct account under each method.

Unit 10.2: Treatment of Goodwill in Partnership Accounts

P1-C10-U10.2 · Importance D · Rank 6 in chapter · Category C · 11.0% of chapter questions · 9 questions

Topic 1: Goodwill

P1-C10-U10.2-T01

Read first Study Sec 2.1: meaning of goodwill (value of reputation yielding profits above normal), factors affecting it, and the Accounting Standard position that only PURCHASED goodwill may be recorded while self-generated goodwill is written off/adjusted through capital accounts.

NOTES

Meaning (SM): "Goodwill is the value of reputation of a firm in respect of profits expected in future over and above the normal rate of profits." — the probability that old customers will resort to the old place; an INTANGIBLE asset (not fictitious): cannot be seen or felt yet is very real, with monetary/saleable value.

Valuation needed when: (a) PSR among partners changes; (b) a new partner is admitted; (c) a partner retires or dies; (d) the business is dissolved or sold. **Factors:** quality of goods, personal reputation of owners, location, near-monopoly rights (e.g. main agency), trademarks and patents, managerial skill, R&D lowering cost, special contracts for materials.

AS position: an intangible is recognised only if identifiable (saleable separately), future economic benefits probable, and cost reliably measurable — internally generated (inherent) goodwill satisfies NONE of these, so only PURCHASED goodwill (consideration in money or money's worth,

e.g. paying ₹3,00,000 for net assets of ₹2,50,000 gives ₹50,000 goodwill) may be recorded.

On reconstitution: goodwill account is NEVER raised on admission, retirement/death or change in PSR — the valued goodwill is adjusted through partners' capital accounts; purchased goodwill is written off (amortised) over a period, and any goodwill account existing in the books at reconstitution is written off immediately, whether inherent or purchased.

Understanding explain with reasons · 2 questions

- True/False trap: 'Goodwill is a fictitious asset' is FALSE --- goodwill is an INTANGIBLE asset (real, has saleable value) unlike fictitious assets which have no realisable value.
- True/False trap: goodwill is not 'depreciated' by fixed instalment method --- being an intangible, purchased goodwill is AMORTISED/written off over a period; depreciation applies to tangible fixed assets.
- Be able to explain why internally generated (inherent) goodwill is not recognised: not identifiable, future benefits uncertain, cost cannot be measured reliably --- hence on reconstitution goodwill is adjusted through partners' capital accounts, never raised in the books.

TQ 1.1 · PYQ 2001-Nov [5] · True/False · 2M · Pg 535 **asked 5x**

LEVEL I
Understanding

Easy

TQ 1.2 · PYQ 2006-May [5] (x) · True/False · 2M · Pg 535

LEVEL I
Understanding

Easy

Topic 2: Methods for Goodwill Valuation

P1-C10-U10.2-T02

Read first Study Sec 2.2: the three bases of valuation --- average profit (simple/weighted), super profit (number of years' purchase, annuity, capitalisation of super profit) and capitalisation of average profit --- with their formulae and when weighted average is preferred.

NOTES

Average profit basis: Goodwill = Average profit × No. of years' purchase; use WEIGHTED average (highest weight to the latest year — more realistic view of future) when profits show a clear rising/falling trend, simple average otherwise; adjust past profits first for expected future changes, rectifications and abnormal items.

Super profit basis: Super profit = Average maintainable profit – Normal profit; Normal profit = Normal Rate of Return (NRR) × Capital employed; **Years' purchase:** Goodwill = Super profit × No. of years' purchase (e.g. capital ₹4,50,000, average profit ₹92,500, NRR 15% ⇒ super profit ₹25,000; 3 years' purchase ⇒ goodwill ₹75,000).

Annuity method: Goodwill = Super profit × annuity (present-value) factor — cures the years'-purchase defect of ignoring time value of money (e.g. ₹3,000 super profit for 5 years @ 15%: 3,000

$\times 3.3522 = ₹10,056.60$, not ₹15,000).

Capitalisation basis: of AVERAGE profit — Goodwill = Normal capital – Actual capital, where Normal capital = Average profit $\div$ NRR and Actual capital employed = Total assets – outside liabilities (e.g. $60,000 \div 12\% = ₹5,00,000$ less net assets ₹4,10,000 $\Rightarrow$ goodwill ₹90,000); of SUPER profit — Goodwill = Super profit $\div$ NRR (e.g. $17,000 \div 12\%$).

Adjusting maintainable profit: deduct partner remuneration/interest on capital employed where required before averaging (e.g. average ₹2,70,000 less interest 12% on ₹6,50,000 = ₹78,000 and salaries ₹72,000 $\Rightarrow$ adjusted profit ₹1,20,000) — any change here flows through super profit and hence goodwill.

Application practise the procedure · 6 questions

- Practise formulae: Super Profit = Average Maintainable Profit – Normal Profit; Normal Profit = NRR $\times$ Capital Employed; Goodwill = Super Profit $\times$ No. of years' purchase; Annuity method: Goodwill = Super Profit $\times$ annuity factor.
- Capitalisation methods: of average profit --- Goodwill = (Average Profit/NRR) – Capital Employed (Net Assets = Total Assets – External Liabilities); of super profit --- Goodwill = Super Profit/NRR. Practise both on the same data.
- Adjust average maintainable profit before valuing: deduct proprietor's remuneration from alternative employment, add back abnormal losses, exclude abnormal gains; add risk-return rate to market interest rate to get NRR where given.
- Use weighted average profit (highest weight to latest year) when profits show a clear rising/falling trend; simple average otherwise.

PQ 2.1 · RTP 2019-Nov [14] (a) · Practical · --- · Pg 535	LEVEL II Application	Medium
PQ 2.2 · PYQ 2022-May [3] (Or) (c) (ii) · Practical · 5M · Pg 536 asked 3×	LEVEL II Application	Medium
PQ 2.3 · PYQ 2022-Nov [5] (b) · Practical · 5M · Pg 537 asked 8×	LEVEL II Application	Medium
PQ 2.4 · RTP 2023-Jun [14] · Practical · --- · Pg 538 asked 5×	LEVEL II Application	Medium
PQ 2.5 · RTP 2025-Jan [12] (b) · Practical · --- · Pg 539	LEVEL II Application	Medium
PQ 6.1 · PYQ 2026-Sep [3] (b) · Practical · 10M · Pg 540	LEVEL II Application	Hard

Analysis work through mixed data — no question in this edition

- Work multi-step problems that start from a Balance Sheet: first compute capital employed (assets less outside liabilities), adjust past profits for rectifications (capital expenditure charged to revenue, stock over/under-valuation, abnormal items), THEN value goodwill by the required method.

- Watch interlinkages: change in depreciation policy or partner salary/interest deducted before computing adjusted average profit changes super profit and hence goodwill.

Topic 3: Need for Valuation of Goodwill

P1-C10-U10.2-T03

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.3: why goodwill must be valued whenever partnership rights are adjusted.

NOTES

Need: any change in the existing relationship of partners makes some partners sacrifice future profit and others gain — the gainers must compensate the sacrificers in proportion to the value of goodwill; such adjustment arises on admission of a new partner, change in profit sharing ratio, retirement or death of a partner and dissolution of the partnership.

Topic 4: Valuation of Goodwill in Case of Admission of a Partner

P1-C10-U10.2-T04

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.4 with the Nigam–Dhameja–Ghosh profit sharing pattern: compensation of old partners through goodwill in the sacrificing ratio.

NOTES

Chief problem on admission: the new partner acquires a share of profits and old partners stand to lose — even if profits grow, extra profits come from combined efforts of all, so old partners are entitled to compensation for the share given up; this compensation is tackled through goodwill.

Sacrificing ratio: goodwill compensates old partners for sacrifice, so it is credited to them in the profit sacrificing ratio (Old share – New share); the new partner's share may be sacrificed by old partners in old profit sharing ratio (sacrificing ratio = old ratio) or in different proportions when a specific new ratio is agreed.

Topic 5: Accounting Treatment of Goodwill in Case of Admission of a New Partner

P1-C10-U10.2-T05

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.5 with Examples 1–4: purchased vs inherent goodwill and the premium entries in sacrificing ratio.

NOTES

Only purchased goodwill recorded: goodwill is recorded in books only when consideration in money or money's worth is paid; on admission goodwill cannot be raised in the books — premium brought by the incoming partner is credited to the sacrificing old partners in profit sacrificing ratio (Old ratio – New ratio; positive difference = sacrifice, negative = gain).

Premium brought in cash: Dr. Bank/Cash A/c (capital + premium) / Cr. old partners' Capital A/cs (premium in sacrificing ratio) and Cr. new partner's Capital A/c (capital); if premium is paid privately to existing partners, no entry in the firm's books.

No premium brought: inherent goodwill is still not raised in books — adjust through capital accounts: Dr. New partner's Capital A/c with his share of goodwill / Cr. sacrificing partners' Capital A/cs in sacrificing ratio; if only the new partner's share is given, old partners sacrifice in their old profit sharing ratio.

Topic 6: Accounting Treatment of Goodwill in Case of Change in Profit Sharing Ratio

P1-C10-U10.2-T06

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §2.6 with Illustrations 7–8: gaining partner compensates sacrificing partner via capital accounts.

NOTES

Treatment: on change in profit sharing ratio the value of goodwill is determined and adjusted through partners' capital accounts on the basis of profit sacrificing ratio — Dr. gaining partner's Capital A/c / Cr. sacrificing partner's Capital A/c with (gain fraction × goodwill); e.g. equal partners A, B, C moving to 4:3:2 with goodwill ₹90,000 — A gains 1/9 and C loses 1/9, so Dr. A's Capital ₹10,000 / Cr. C's Capital ₹10,000.

Topic 7: Accounting Treatment of Goodwill in Case of Retirement or Death of a Partner

P1-C10-U10.2-T07

Read first Study Sec 2.7 (with Sec 2.4--2.5 as base): on retirement/death the continuing partners compensate the outgoing partner for his share of goodwill in their GAINING ratio; goodwill is valued on

the date of retirement/death and adjusted through capital accounts without raising a goodwill account.

NOTES

Rule (Sec 2.7): on retirement the continuing partners GAIN in PSR, so they pay the retiring partner his share of goodwill in the GAINING ratio (gain = new share – old share); on death the continuing partners likewise bear the share due to the heirs of the deceased; goodwill is valued on the DATE of retirement/death and adjusted through capital accounts — no goodwill account raised.

Pro-forma entry: Dr. Continuing partners' Capital A/cs (gaining ratio) / Cr. Retiring (or Deceased) partner's Capital A/c with his share of goodwill — e.g. equal partners A, B, C, goodwill ₹90,000, C retires: Dr. A ₹15,000, Dr. B ₹15,000, Cr. C ₹30,000; if the new ratio differs (Antoo 3:4:3 retiring, B and C continue equally), gains are computed partner-wise (new – old: B $1\frac{1}{2}-4/10=1/10$, C $1\frac{1}{2}-3/10=2/10$) and goodwill debited 1:2.

Checks for multi-stage problems: goodwill already standing in the books is written off immediately (in the OLD ratio) before the adjustment; at each successive reconstitution adjust only the CHANGE in goodwill value in the sacrificing/gaining ratio of that stage; total debits to gainers must equal the credit to the outgoing/sacrificing partner, and goodwill must never appear as an asset in the final Balance Sheet.

Analysis work through mixed data · 1 question

- Master the adjustment entry: gaining partners' capital A/cs Dr. (in gaining ratio = new share – old share) To retiring/deceased partner's capital A/c with his share of goodwill; existing goodwill in books must be written off first in the OLD ratio.
- Practise multi-event problems where the firm's constitution changes more than once (e.g., successive admissions/changes with goodwill revalued at each date, as in P admitting Q then R): at each stage compute sacrificing/gaining ratios and adjust only the CHANGE in goodwill value through capital accounts.
- Cross-check each stage: total debits by gainers must equal credit to the sacrificing/outgoing partner; goodwill should never appear as an asset in the final Balance Sheet.

PQ 7.1 · PYQ 2025-Sep [3] (b) · Practical · 8M · Pg 542

LEVEL II
Analysis

Hard

Unit 10.3: Admission of a New Partner

P1-C10-U10.3 · Importance C · Rank 3 in chapter · Category A · 17.1% of chapter questions · 14 questions

Topic 1: Introduction

P1-C10-U10.3-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §3.1: why an updated balance sheet is needed on the date of admission of a new partner.

NOTES

Purpose of admission: a new partner is admitted for the benefit of the firm — either to increase partnership capital or to strengthen management of the firm.

Entries on admission: bring into account all appreciation/reduction in asset values, unrecorded or unpaid liabilities, and all accrued but unrecorded profits/losses as on the date of admission, so old partners' Capital A/cs reflect proper figures and subsequent profits/losses are automatically shared by the incoming partner with old partners; goodwill is also to be valued and brought into account (per Unit 2 treatment).

Topic 2: Revaluation Account or Profit and Loss Adjustment Account

P1-C10-U10.3-T02

Read first Study Sec 3.2: purpose and entries of the Revaluation Account (also called Profit and Loss Adjustment Account) on admission, the Memorandum Revaluation Account when revised values are not to be shown, and the difference between the two.

NOTES

Purpose: on admission, assets are revalued and liabilities reassessed through a Revaluation Account — ALSO KNOWN AS Profit and Loss Adjustment Account — so the Balance Sheet is updated and old partners' capitals reflect accrued profits/losses; debit all reductions in assets and increases in liabilities, credit all increases in assets and decreases in liabilities; the balance (profit/loss) goes to OLD partners in the OLD PSR (never to all partners in new ratio), and assets/liabilities appear in the new Balance Sheet at revised figures.

Pro-forma entries: Dr. Revaluation A/c / Cr. Assets (decrease) and Cr. Liabilities (increase); Dr. Assets (increase) and Dr. Liabilities (decrease) / Cr. Revaluation A/c; profit: Dr. Revaluation A/c / Cr. Old partners' Capital A/cs (old ratio); loss: Dr. Old partners' Capital A/cs / Cr. Revaluation A/c.

Memorandum Revaluation A/c (revised values NOT to be shown): two parts — first part records the revaluation in the usual way (no ledger change to assets/liabilities), result to OLD partners in OLD ratio; second part REVERSES the first part's entries so book values stay unchanged, its result going to ALL partners INCLUDING the new one in the NEW ratio; a profit in the first part necessarily

means an equal loss in the second part (and vice versa).

Revaluation vs Memorandum: Revaluation A/c — assets/liabilities appear at revalued figures, single account, net result to old partners in old ratio; Memorandum — old figures retained in the new Balance Sheet, two parts, first part to old partners (old ratio) and second (reversing) part to all partners (new ratio); alternatively the changes may be adjusted directly through capital A/cs at old book values.

Full-problem drill: typical adjustments — appreciation/depreciation of assets, provision for doubtful debts, outstanding/unrecorded liabilities, unrecorded assets, joint life policy, investments; combine with goodwill adjusted through capital A/cs in SACRIFICING ratio (premium not brought in cash), reserves transferred in OLD ratio, then Capital A/cs, Cash/Bank A/c and new Balance Sheet — capitals may finally be made proportionate to the new PSR on the basis of the new partner's capital, excess/shortfall settled through cash or current A/cs (same technique for admission in an LLP).

Understanding explain with reasons · 3 questions

- True/False trap (asked repeatedly): profit/loss on revaluation on admission goes to OLD partners in the OLD profit sharing ratio --- 'transferred to all partners in new ratio' is FALSE.
- 'Revaluation Account is also known as Profit and Loss Adjustment Account' --- TRUE; know why: it records changes in values of assets/liabilities to adjust old partners' capitals.
- Explain Memorandum Revaluation Account: first part to old partners in old ratio, reversing second part to ALL partners (including new) in new ratio, book values unchanged.

TQ 2.1 · PYQ 2020-Nov [1] (a) (i) {C} · True/False · 2M · Pg 546 asked 4×	LEVEL I Understanding	Easy
TQ 2.2 · PYQ 2024-Jun [1] (a) (vi) {C} · True/False · 2M · Pg 547	LEVEL I Understanding	Easy
TQ 2.3 · MTP 2025-Jan S2 [1] (a) (iv) · True/False · 2M · Pg 547	LEVEL I Understanding	Easy

Application work the problem · 5 questions

PQ 2.1 · RTP 2023-Jun [15] · Practical · --- · Pg 547 asked 3×	LEVEL II Application	Hard
PQ 2.2 · PYQ 2024-Jun [4] (a) · Practical · 12M · Pg 550 asked 2×	LEVEL II Application	Hard
PQ 2.3 · MTP 2025-Jan S2 [4] (a) · Practical · 10M · Pg 553 asked 6×	LEVEL II Application	Hard
PQ 2.4 · PYQ 2026-Jan [3] (b) · Practical · 10M · Pg 556	LEVEL II Application	Hard
PQ 2.5 · PYQ 2026-May [3] (a) · Practical · 10M · Pg 559	LEVEL II Application	Hard

Synthesis prepare end-to-end — no question in this edition

- Master end-to-end admission problems: Revaluation A/c, Partners' Capital Accounts, Cash/Bank A/c and new Balance Sheet with typical adjustments --- appreciation/depreciation of assets, provision for doubtful debts, outstanding/unrecorded liabilities, unrecorded assets, joint life policy and investments.
- Combine revaluation with goodwill adjustment through capital accounts in sacrificing ratio (new partner's premium or goodwill not brought in cash) and transfer of reserves in old ratio.
- Practise capital adjustment requirements: making capitals proportionate to new PSR based on new partner's capital, with excess/shortfall settled through cash or current accounts.
- Also practise variants where past profits were wrongly shared or accounts kept on cash basis needing correction before admission (mercantile adjustments), and admission in an LLP setting --- the technique is identical.

Topic 3: Reserves in the Balance Sheet

P1-C10-U10.3-T03

Read first Study Sec 3.3: on admission, any General Reserve, Profit and Loss Account credit balance or other accumulated profits in the Balance Sheet must be transferred to the OLD partners' capital accounts in the OLD profit sharing ratio before other adjustments.

NOTES

Rule (Sec 3.3): whenever a new partner is admitted, any reserve etc. (General Reserve, P&L A/c credit balance, other accumulated profits) appearing in the Balance Sheet must be transferred to the OLD partners' Capital A/cs in the OLD PSR — **entry:** Dr. Reserves/P&L A/c / Cr. Old partners' Capital A/cs (old ratio); do not carry reserves into the new firm's Balance Sheet unless expressly required.

Accumulated losses: a debit balance of P&L A/c is likewise transferred (debited) to the old partners' capital A/cs in the old ratio.

Sequence for full problems: transfer reserves (old ratio) → Revaluation A/c for asset/liability changes (old ratio) → goodwill adjustment (sacrificing ratio) → new partner brings in capital → Capital A/cs and new Balance Sheet; drill provisions for doubtful debts at given %, revaluation of land and buildings/plant/inventory, outstanding liabilities, and new PSR where the incomer acquires his share from old partners — the closing Balance Sheet must tally.

Understanding explain with reasons · 1 question

PQ 3.1 · PYQ 2021-Dec [4] (b) · Practical · 10M · Pg 562 **asked 3×**

LEVEL I
Understanding

Medium

Application work the problem · 3 questions

PQ 3.2 • PYQ 2024-Sep [3] (b) • Practical • 10M • Pg 564 asked 3×	LEVEL II Application	Hard
PQ 3.3 • PYQ 2025-May [3] (b) • Practical • 8M • Pg 567 asked 2×	LEVEL II Application	Hard
PQ 3.4 • PYQ 2025-Sep [4] (a) • Practical • 12M • Pg 571	LEVEL II Application	Hard

Synthesis prepare end-to-end — no question in this edition

- Master the full admission question where General Reserve/P&L balance appears: entry --- Reserve/P&L A/c Dr. To old partners' capital A/cs in old ratio; never leave reserves in the new firm's Balance Sheet unless expressly required.
- Practise the complete chain end-to-end: transfer reserves (old ratio) → Revaluation A/c for asset/liability changes (old ratio) → goodwill adjustment (sacrificing ratio) → new partner brings capital → Capital Accounts and new Balance Sheet.
- Typical adjustments to drill: provision for doubtful debts at a given %, revaluation of land & buildings/plant, outstanding liabilities, and computing new PSR when the incoming partner acquires his share from old partners.
- Accuracy checks: Balance Sheet must tally after all transfers; accumulated losses (Dr. balance of P&L) are likewise debited to old partners in old ratio.

Topic 4: Computation of New Profit Sharing Ratio

P1-C10-U10.3-T04

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §3.4 Cases I–V with worked examples: computing new ratio from the share offered to the new partner.

NOTES

Default rule: absent contrary agreement, old partners continue inter se at old ratio — deduct new partner's share from 1 and divide the balance among old partners in old ratio; e.g. A:B = 3:2, C admitted for $\frac{1}{5} \rightarrow A = \frac{4}{5} \times \frac{3}{5} = \frac{12}{25}$, $B = \frac{8}{25}$, new ratio 12:8:5.

Other cases: (II) new partner purchases share from old partners in given ratio — deduct each portion given from that partner's old share; (III) old partners surrender a fraction of their own share — new share = old share – share surrendered, C's share = sum of surrenders; (IV) share acquired entirely from one partner — only that partner's share is reduced; (V) share acquired from old partners in a certain ratio.

Topic 5: Hidden Goodwill

P1-C10-U10.3-T05

Read first Study Sec 3.5: when goodwill value is not given, infer it as (incoming partner's capital × reciprocal of his share) LESS (total capitals of all partners including the new one plus accumulated profits/reserves); the inferred goodwill is adjusted through capital accounts in sacrificing ratio.

NOTES

Inference formula (Sec 3.5): when goodwill value is not given — Hidden goodwill = (Incoming partner's capital × reciprocal of his share) – (total capitals of old partners + net accumulated profits and reserves, if any + capital brought in by incoming partner).

Worked example: A and B, capitals ₹7,000 each, admit C for 1/4 share with capital ₹8,000 ⇒ implied firm capital = $8,000 \times 4/1 = ₹32,000$; hidden goodwill = $32,000 - (7,000 + 7,000 + 8,000) = ₹10,000$.

Adjustment entry (no goodwill account raised): Dr. New partner's Capital A/c with HIS share of the inferred goodwill / Cr. Old (sacrificing) partners' Capital A/cs in sacrificing ratio — e.g. Dr. C's Capital A/c ₹2,500 ($₹10,000 \times 1/4$) / Cr. A ₹1,250, Cr. B ₹1,250.

Combined problems and checks: include accumulated profits/reserves in the deduction when computing hidden goodwill; combine with reserves transfer, revaluation of assets/liabilities and capital rearrangement in the new ratio; verify that total of the new firm's capitals plus liabilities equals revalued assets and that NO goodwill appears in the closing Balance Sheet.

Application work the problem · 2 questions

PQ 5.1 · PYQ 2006-May [4] · Practical · 15M · Pg 574

LEVEL II
Application

Hard

PQ 5.2 · MTP 2024-Jul [4] (a) · Practical · 12M · Pg 578 asked 5×

LEVEL II
Application

Hard

Synthesis prepare end-to-end — no question in this edition

- Master full-length admission problems where goodwill must first be INFERRED from the new partner's capital and profit share (e.g., capital ₹18,000 for 1/4 share implies total capital ₹72,000; shortfall of actual combined capitals = hidden goodwill), then complete Revaluation A/c, Capital A/cs and Balance Sheet.
- Pass the goodwill adjustment without raising a goodwill account: new partner's capital A/c Dr. To old partners' capital A/cs (sacrificing ratio) for his share of the inferred goodwill.
- Practise combining hidden goodwill with reserves transfer, revaluation of assets/liabilities and capital rearrangement in the new ratio --- include accumulated profits and reserves in the deduction when computing hidden goodwill.

- Verify: total of new firm's capitals plus liabilities equals revalued assets; no goodwill appears in the closing Balance Sheet.

Unit 10.4: Retirement of a Partner

P1-C10-U10.4 · Importance D · Rank 5 in chapter · Category C · 12.2% of chapter questions · 10 questions

Topic 1: Introduction

P1-C10-U10.4-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §4.1: sequence of readjustments when a partner retires.

NOTES

Retirement: a partner may retire due to old age, illness etc.; the business generally does not end — continuing partners run it, and since they gain in profit sharing ratio they arrange the amount to discharge the retiring partner's claim.

Readjustment sequence: assets and liabilities are revalued, goodwill is valued, surrender value of joint life policy (if any) is taken into account, revaluation profit and reserves are transferred to partners' capital/current accounts, and finally the amount due to the retiring partner is determined and discharged.

Topic 2: Calculation of Gaining Ratio

P1-C10-U10.4-T02

Read first Study Section 4.2 of Unit 4 (Retirement of a Partner): calculation of new profit sharing ratio and gaining ratio in all cases --- new ratio given, new ratio not given, gain specified, and share of retiring partner acquired in a given ratio.

NOTES

Core rule: on retirement the continuing partners take over the retiring partner's share, so they always gain; Gaining ratio = New share – Old share, and New share = Old share + Gain — express all shares with a common denominator before subtracting; it is the mirror of sacrificing ratio (Old – New) used on admission.

Four SM cases: (i) new ratio given — gain = new – old; (ii) new ratio NOT given — remaining partners continue in their old inter-se ratio, so gaining ratio = old ratio between them (strike out retiring partner's share, e.g. 3:2:1, Bhaskar retires → 3:1); (iii) gain specified — New = Old + Gain

($2/6+2/6=4/6$, $1/6+1/6=2/6 \rightarrow 2:1$); (iv) retiring partner's share acquired in a stated ratio — gain = his share $\times$ stated fraction (Tasha's $2/6$ taken by Deepu:Honey $2:1 \rightarrow$ gains $4/18$ and $2/18$, new ratio $13:5$).

Worked example (SM 4.2): A, B, C share $5:3:2$; B retires, A and C agree $3:2 \rightarrow$ A gains $3/5-5/10 = 1/10$, C gains $2/5-2/10 = 2/10$, gaining ratio $1:2$; had they continued at $5:2$, the gained share is divided in the old ratio between them.

Use of gaining ratio: continuing partners' capital A/cs are debited in gaining ratio to credit the retiring partner with his goodwill share (goodwill not raised in books); also used when revalued figures/reserve are not to appear in the new Balance Sheet — net amount due to retiring partner borne by gainers in gaining ratio.

Understanding explain with reasons · 1 question

- Be able to justify the True/False point that when a partner retires, the continuing partners always gain --- the retiring partner's share is taken over by them, increasing their profit share.
- Explain why, when no new ratio is agreed, the remaining partners share future profits (and gain) in their old inter-se ratio.
- Distinguish gaining ratio (used to debit continuing partners for goodwill) from sacrificing ratio on admission.

TQ 2.1 · MTP 2022-Nov S2 [1] (a) (v) {C} · True/False · 2M · Pg 582
asked 3x

LEVEL I
Understanding

Easy

Application practise the procedure — no question in this edition

- Practise: Gaining ratio = New share - Old share; New share = Old share + share acquired from retiring partner.
- Work each case from the SM table: (i) new ratio given, (ii) new ratio not given (old ratio continues), (iii) gaining ratio given (New = Old + Gain), (iv) retiring partner's share surrendered in a specified ratio (e.g. B gives his share to A and C in original ratio vs. a stated ratio like $2:1$).
- Practise fraction work carefully --- express all shares with a common denominator before subtracting.

Topic 3: Revaluation of Assets and Liabilities on Retirement of a Partner

P1-C10-U10.4-T03

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §4.3: Revaluation A/c entries and the alternative when revalued figures are not to appear in the balance sheet.

NOTES

Revaluation A/c: profit or loss on revaluation is distributed to ALL partners including the retiring partner in the existing profit sharing ratio — “Dr. Revaluation A/c / Cr. Partners' Capital A/cs” for profit (reverse for loss); the account (also called Profit and Loss Adjustment A/c) closes automatically by this transfer.

If revalued figures not to appear: pass one net entry — Dr. continuing partners' Capital A/cs (in gaining ratio) / Cr. retiring partner's Capital A/c with his revaluation share; or record revaluation in old ratio and reverse it at the new ratio (two-entry method) — no separate Revaluation A/c needed; a Memorandum Revaluation A/c may also be used.

Topic 4: Reserves

P1-C10-U10.4-T04

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §4.4 with the A-B-C and X-Y-Z examples: transfer of undistributed reserves on retirement.

NOTES

Rule: undistributed profit/reserve in the balance sheet is credited to all partners' Capital A/cs in the OLD profit sharing ratio (“Dr. Reserve A/c / Cr. Partners' Capital A/cs”); alternatively only the retiring partner's share may be transferred to his Capital A/c — but this works only if continuing partners' inter se ratio is unchanged.

Ratio changed: if continuing partners share in a new inter se ratio (gaining ratio differs), full distribution in old ratio must be made; if they wish to retain the reserve in the balance sheet, pass adjustment — Dr. continuing partners' Capital A/cs in gaining ratio / Cr. retiring partner's Capital A/c with his share of reserve.

Topic 5: Final Payment to a Retiring Partner

P1-C10-U10.4-T05

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §4.5: adjustments determining the retiring partner's claim and modes of discharge.

NOTES

Claim: after adjusting (i) transfer of reserve, (ii) transfer of goodwill and (iii) profit/loss on revaluation, the credit balance of the retiring partner's Capital A/c is the amount payable; full discharge — “Dr. Retiring Partner's Capital A/c / Cr. Bank A/c”; partial retention as loan — “Dr. Retiring Partner's Capital A/c / Cr. Retiring Partner's Loan A/c and Cr. Bank A/c”.

Modes per agreement: (a) repayment in instalments with interest on outstanding balance treated as outgoing partner's loan, (b) amount treated as loan to the firm carrying fixed interest or a share of profit, (c) annuity to the retired partner for life or for an agreed number of years/life of a dependent.

Topic 6: Paying a Partner's Loan in Instalment

P1-C10-U10.4-T06

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §4.6 with the ₹30,000 loan example and the Retiring Partner's Loan Account.

NOTES

Method: divide the loan into equal parts; each payment = equal loan instalment + interest for the period on the outstanding balance; e.g. loan ₹30,000 in 4 annual instalments at 6% — Year 1 pay ₹7,500 + ₹1,800 = ₹9,300 leaving ₹22,500, Year 2 pay ₹7,500 + ₹1,350 = ₹8,850, and so on; the Retiring Partner's Loan A/c is credited with Capital A/c transfer and yearly interest, debited with cash paid and balance c/d.

Topic 7: Joint Life Policy

P1-C10-U10.4-T07

Read first Study Section 4.7: the three accounting treatments of JLP premium --- (1) premium as expense, (2) premium as asset (policy at surrender value), (3) Joint Life Policy Reserve method --- and the treatment of surrender value on retirement (Illustrations 7--9).

NOTES

JLP (SM): firm takes a policy on the lives of all partners, pays the premium, and the policy amount is payable to the firm on death of any partner or maturity, whichever is earlier — objective is to minimise financial hardship of paying a large sum to the legal representatives of a deceased partner or to a retiring partner.

Method 1 — premium as expense: Dr. JLP Insurance Premium / Cr. Bank, then Dr. P&L / Cr. JLP Premium each year; whole amount received (surrender value on retirement) is a gain — Dr. Bank /

Cr. Partners' Capital A/cs of ALL partners including the retiring one in OLD ratio.

Method 2 — premium as asset: Dr. JLP A/c / Cr. Bank; at year-end write off excess of book balance over surrender value to P&L, so JLP stands at surrender value; on realization only the excess over surrender value is a gain credited to capitals in profit sharing ratio.

Method 3 — JLP Reserve: premium Dr. JLP A/c; amount equal to premium transferred P&L Appropriation → JLP Reserve; JLP brought down to surrender value by debiting the Reserve — BOTH JLP A/c (asset) and JLP Reserve (liability) appear at surrender value; on retirement/death first transfer Reserve to JLP A/c, then balance to Partners' Capital A/cs.

Exam pattern (Ill. 7-9): policy ₹50,000, premium ₹3,000 p.a., surrender values 2018 nil, 2019 ₹900, 2020 ₹2,000, 2021 ₹3,600; Black (2/10) retires 2022 — premium method: ₹3,600 received credited Red:White:Black 5:3:2 (1,800:1,080:720); surrender-value method: JLP already at ₹3,600, Bank Dr / JLP Cr, no gain; if surrender value exceeds JLP shown in B/S, only the excess goes to Revaluation A/c.

Application practise the procedure · 1 question

- Practise ledger accounts under all three methods: premium charged to P&L; JLP A/c carried at surrender value (excess of premium over increase in surrender value written off to P&L); JLP A/c with JLP Reserve A/c (both shown at surrender value).
- On retirement, credit the surrender value (or its increase) to all partners including the retiring partner in the OLD profit sharing ratio; under the reserve method first transfer JLP Reserve to JLP A/c.
- Practise the exam pattern (e.g. policy ₹50,000, annual premium ₹3,000, year-wise surrender values): build the JLP/Premium accounts year by year, then account for the retirement adjustment.

PQ 7.1 · PYQ 2021-Jul [5] (b) (i) · Practical · 5M · Pg 583 asked 5×

LEVEL II
Application

Medium

Topic 8: Separate Life Policy

P1-C10-U10.4-T08

Read first Study Section 4.8: where individual policies are taken on each partner's life with premium paid by the firm, the retiring partner is entitled to his profit share of the surrender values of ALL partners' policies (Illustration 10).

NOTES

Rule (SM 4.8): where individual policies are taken on each partner's life with premium paid by the firm, the retiring partner is entitled to his proportionate (profit-sharing) share of the SURRENDER VALUES of ALL partners' policies — not merely the value of his own policy.

SM example: Sona, Gabbu, Amit share 3:1:1; surrender values ₹10,000 + ₹20,000 + ₹30,000 =

₹60,000; if Amit retires he gets $₹60,000 \times 1/5 = ₹12,000$.

Contrast with death: on death the firm receives the full assured value of the deceased's policy (plus surrender values of survivors' policies count for his share); on retirement only surrender values are relevant.

Understanding explain with reasons — no question in this edition

- True/False trap: the statement that a retiring partner gets the surrender value of HIS policy only is FALSE --- he gets a proportionate (profit-sharing) share of surrender values of all partners' policies, since premiums were paid by the firm.
- Be able to reason with the SM example: policies with surrender values ₹10,000 + ₹20,000 + ₹30,000 = ₹60,000; a retiring partner with 1/5 share gets $₹60,000 \times 1/5 = ₹12,000$.
- Note the contrast with death: on death the assured value of the deceased's policy is received; on retirement only surrender values are relevant.

Topic 9: Integrated Problems

P1-C10-U10.4-T09

Read first Study Sections 4.3--4.6 and the comprehensive illustrations: revaluation of assets and liabilities, goodwill adjustment through capital accounts in gaining ratio, transfer of reserves, settlement of the retiring partner (cash/loan account), capital adjustment and the new Balance Sheet.

NOTES

Full sequence: (1) Revaluation/P&L Adjustment A/c — profit or loss to ALL partners including retiring in OLD ratio; (2) transfer General Reserve/undistributed P&L in old ratio (Reserve Dr / To all capitals); (3) goodwill — continuing partners' Capital A/cs Dr in GAINING ratio / To retiring partner's Capital with his share, goodwill not raised (written off to comply with AS); (4) settle: Retiring Partner's Capital Dr / To Bank and/or To Retiring Partner's Loan A/c.

Typical adjustments: goodwill at 2–3 years' purchase of average or weighted-average profits (Ill. 10: profits 41,000/50,000/55,000, weights 1:2:3 → weighted avg 51,000, goodwill ₹1,02,000, retiring 1/6 share ₹17,000); provision for doubtful debts 5%, depreciation on machinery/furniture, appreciation of building, unrecorded assets/liabilities, investments taken over by a partner, dishonoured bills.

Loan in instalments (SM 4.6): divide loan into equal parts, pay instalment + interest on outstanding balance — ₹30,000 @6% in 4 annual instalments: Yr1 ₹7,500+1,800=9,300; Yr2 ₹7,500+1,350=8,850; Yr3 ₹8,400; Yr4 ₹7,950; other settlement modes: whole claim in cash, part cash + balance as loan, or annuity for life/agreed years.

Capital adjustment: where total capital of the new firm is fixed, compute each continuing partner's capital in the NEW ratio (total capital = revalued assets – outside liabilities – retiring

partner's loan); cash brought in/withdrawn is the balancing figure of Capital A/cs, proved through the Bank A/c.

Presentation (10–15 marks): prepare all four neatly — Revaluation A/c, Partners' Capital A/cs (columnar), Bank/Cash A/c, and post-retirement Balance Sheet; Bank A/c totals prove the solution.

Application work the problem · 8 questions

PQ 9.1 · PYQ 2006-Nov [4] · Practical · 15M · Pg 584 asked 5×	LEVEL II Application	Hard
PQ 9.2 · PYQ 2018-May [4] (b) · Practical · 10M · Pg 587 asked 3×	LEVEL II Application	Hard
PQ 9.3 · PYQ 2020-Nov [4] (a) · Practical · 10M · Pg 589 asked 6×	LEVEL II Application	Hard
PQ 9.4 · PYQ 2022-May [4] (b) · Practical · 10M · Pg 592 asked 2×	LEVEL II Application	Hard
PQ 9.5 · PYQ 2023-Dec [5] (a) · Practical · 10M · Pg 594	LEVEL II Application	Hard
PQ 9.6 · PYQ 2024-Sep [4] (a) · Practical · 10M · Pg 597	LEVEL II Application	Hard
PQ 9.7 · PYQ 2025-May [4] (a) · Practical · 10M · Pg 600 asked 2×	LEVEL II Application	Hard
PQ 9.8 · PYQ 2026-Jan [4] (a) · Practical · 10M · Pg 603	LEVEL II Application	Hard

Synthesis prepare end-to-end — no question in this edition

- Master the full sequence end-to-end: Revaluation A/c (profit/loss to ALL partners in old ratio) → transfer General Reserve/P&L in old ratio → goodwill adjustment (continuing partners' capitals Dr in gaining ratio, retiring partner Cr for his share; goodwill not raised in books) → settle retiring partner.
- Practise typical adjustments seen in PYQs: goodwill at 2--3 years' purchase of average profits, provision for doubtful debts at 5%, depreciation on machinery/furniture, appreciation of building, unrecorded assets/liabilities, existing goodwill in Balance Sheet written off in old ratio.
- Handle settlement variants: balance transferred to retiring partner's Loan A/c (with interest), part payment in cash with balance as loan, continuing partners bringing capital to pay him off, and adjusting capitals in the new ratio.
- Prepare all four required items neatly: Revaluation A/c, Partners' Capital A/cs (columnar), Bank/Cash A/c and the post-retirement Balance Sheet --- a 10--15 mark question format.

Unit 10.5: Death of a Partner

P1-C10-U10.5 · Importance D · Rank 4 in chapter · Category B · 14.6% of chapter questions · 12 questions

Topic 1: Introduction

P1-C10-U10.5-T01

Read first Study Section 5.1 of Unit 5 (Death of a Partner): death is a case of reconstitution of partnership, with problems similar to retirement --- revaluation, goodwill, reserves --- but the firm receives the joint life policy value.

NOTES

Death = reconstitution: business of the firm does NOT come to an end on death of a partner — surviving partners continue and the partnership is reconstituted; only when the business itself ceases is the FIRM dissolved.

Parallels with retirement: assets and liabilities revalued and the profit/loss transferred to ALL partners including the deceased in old ratio; goodwill and reserves dealt with exactly as on retirement (adjustment through gaining ratio).

Differences: the firm receives the full joint life policy value (not surrender value); the amount due is credited to the Deceased Partner's Executor's A/c; and the executor is additionally entitled to the share of profit from the beginning of the year up to the date of death.

Understanding explain with reasons • 1 question

- True/False trap: 'Business of partnership comes to an end on death of a partner' is FALSE --- the firm may be reconstituted and the surviving partners can continue the business.
- Explain how death parallels retirement (revaluation profit/loss and goodwill credited to all partners including the deceased, in old ratio) and how it differs (amount due goes to the Executor; share of profit up to date of death is payable).
- Distinguish dissolution of partnership (reconstitution) from dissolution of the firm.

TQ 1.1 • PYQ 2021-Jul [1] (a) (v) {C} • True/False • 2M • Pg 610 **asked 4×**

LEVEL I
Understanding

Easy

Topic 2: Right of Outgoing Partner in Certain Cases to Share Subsequent Profits

P1-C10-U10.5-T02

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §5.2 quoting Section 37 of the Indian Partnership Act with the A-B-C worked example of the two options.

NOTES

Section 37: where a partner has died or ceased to be a partner and continuing partners carry on business with the firm's property without final settlement, then absent a contrary contract the outgoing partner/his estate is entitled, at his option, to (i) such share of profits made since he ceased to be a partner as is attributable to the use of his share of the firm's property, OR (ii) interest at 6% per annum on the amount of his share; he is not bound to elect until his profit share is ascertained.

Proviso: if by contract the continuing partners have an option to purchase the outgoing/deceased partner's interest and duly exercise it, the estate gets no further share of profits; but a partner not complying in all material respects with the option's terms is liable to account under Section 37; e.g. C's capital ₹1,20,000 of total ₹2,45,000, subsequent profit ₹28,000 for 3 months — profit share ₹13,714 vs interest ₹1,800, so C's estate opts for the profit share.

Topic 3: Amount Payable to Legal Representatives of Dead Partner

P1-C10-U10.5-T03

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §5.3: entitlements and liabilities of legal representatives and the time/turnover bases for pre-death profit.

NOTES

Entitled to: (a) credit balance of deceased's capital account, (b) interest on capital (if deed provides) upto date of death, (c) share of goodwill, (d) share of undistributed profit/reserves, (e) share of revaluation profit, (f) share of profit upto date of death, (g) share of Joint Life Policy; **liable for:** drawings, interest on drawings, share of revaluation loss and share of losses till date of death.

Profit upto date of death: ascertained via P&L Suspense A/c by (i) Time basis — assume uniform profit, previous year's profit $\times$ months/12 $\times$ deceased's share, or (ii) Turnover/Sales basis — last year's profit-to-sales rate applied to sales upto date of death $\times$ deceased's share.

Settlement: balance of deceased's capital account is transferred to his Executor's A/c; payment depends on agreement — in its absence the legal representative is entitled to interest at 6% p.a. on the amount due from date of death till final payment.

Topic 4: Special Transactions in Case of Death: Joint Life Policy

P1-C10-U10.5-T04

Read first Study Section 5.4: journal entries when JLP does not appear in the books, appears at surrender value, or appears at surrender value with a JLP Reserve --- on death the firm receives the full policy (assured) value.

NOTES

Key rule: on DEATH the firm receives the FULL assured/policy value from the insurance company (surrender value is relevant only on retirement/surrender); the gain — policy value minus book value of JLP, if any — is credited to ALL partners including the deceased in the OLD profit sharing ratio.

Method 1 — JLP not in books: entire amount is gain: Bank Dr ₹1,00,000 / To JLP A/c; JLP A/c Dr ₹1,00,000 / To A, B, C Capital A/cs 50,000:30,000:20,000 (old ratio 5:3:2).

Method 2 — JLP at surrender value: policy ₹1,00,000 in B/S at surrender value ₹10,000: Bank Dr 1,00,000 / To JLP; JLP Dr 90,000 (excess over surrender value = gain) / To capitals in old ratio.

Method 3 — with JLP Reserve: same two entries plus JLP Reserve A/c Dr 10,000 / To capitals in old ratio (reserve written back to partners); i.e. transfer JLP Reserve before closing the JLP A/c.

Understanding explain with reasons · 1 question

- True/False trap: on DEATH of a partner the firm receives the full assured/policy value from the insurer, NOT the surrender value (surrender value is relevant on retirement/surrender of policy).
- Explain the entries: Bank Dr To JLP A/c with policy amount; the gain (policy value minus book value of JLP, if any) is credited to ALL partners including the deceased in the old profit sharing ratio.
- Know how treatment differs under the three methods: no JLP in books (entire amount is gain), JLP at surrender value (excess over surrender value is gain), JLP with Reserve (transfer reserve to JLP A/c first).

TQ 4.1 · RTP 2026-Jan [1] (h) · True/False · ---- · Pg 611 asked 5x

LEVEL I
Understanding

Easy

Topic 5: Special Transactions in Case of Death: Separate Life Policy

P1-C10-U10.5-T05

Read first Study Section 5.5: with individual policies premium-paid by the firm, the executor gets the deceased's profit-share of the assured value of the deceased's policy PLUS the surrender values of the surviving partners' policies. Exam questions combine this with interest on capital and profit up to death.

NOTES

Formula (SM 5.5): amount credited to executor = (ASSURED value of deceased partner's policy + SURRENDER values of surviving partners' policies) × deceased's profit share; surviving partners are credited their profit shares of the same total, since all premiums were paid by the firm and charged to P&L.

SM example: Sona, Gabbu, Amit 3:1:1; Amit (1/5) dies — executors get $3,00,000 \times \frac{1}{5} + \frac{1}{5} \times$

$(10,000 + 20,000) = 60,000 + 6,000 = ₹66,000.$

Pro-forma entry: Bank Dr (assured value) and SLP of Remaining Partners Dr (surrender values) / To SLP of Deceased Partner, To Executor's A/c and To remaining partners' capitals in profit sharing ratio.

Multi-element deed problems (Ill. 2): combine into one account due to the representative — interest on fixed capitals @ deed rate to date/year-end, share of profit (after charging interest on capital), goodwill at agreed years' purchase of average net profits AFTER charging interest on capital, plus policy share; with fixed capitals route drawings/profits through Current A/c; deduct drawings and unrecorded liabilities.

Analysis work through mixed data · 1 question

- Work multi-element deed problems (like the P, Q, R fixed-capital PYQ): interest on fixed capitals @ given %, share of profit to date of death, goodwill per deed, and life policy amounts --- combine all credits into the Executor's A/c.
- Apply the SM formula: amount credited = (assured value of deceased's policy + surrender values of surviving partners' policies) × deceased's profit share; surviving partners are credited their shares too.
- Watch interlinkages: fixed vs fluctuating capitals (adjustments through current accounts), premium charged to P&L each year, and apportionment of the year's profit up to the date of death.

PQ 5.1 · PYQ 2021-Jan [4] (a) · Practical · 10M · Pg 611 asked 2x

LEVEL II
Analysis

Hard

Topic 6: Special Transactions in Case of Death: Payment of Deceased Partner's Share

P1-C10-U10.5-T06

Read first Study Sections 5.2, 5.3 and 5.6: full list of amounts due to legal representatives, calculation of profit up to date of death (time basis and turnover basis) via P&L Suspense A/c, and Section 37 rights (subsequent profits or 6% interest).

NOTES

Executor entitled to (SM 5.3): (a) capital balance, (b) interest on capital up to date of death if the deed provides, (c) share of goodwill, (d) share of undistributed profits/reserves, (e) share of revaluation profit, (f) share of profit up to date of death, (g) share of JLP; **liable for:** drawings, interest on drawings, share of revaluation loss and losses up to death — so 'capital balance only' is FALSE.

Profit up to date of death: Time basis — last year's profit × months elapsed/12 × deceased's share; Turnover basis — rate of profit on last year's sales applied to sales up to death (sales 4,00,000,

profit 60,000 → 15%; sales to 31 May 1,00,000 → profit 15,000; Neha $1/6 = ₹2,500$); **entry:** P&L Suspense A/c Dr / To Deceased Partner's Capital A/c (Suspense closed to P&L at year-end).

Section 37 (SM): “the outgoing partner or his estate is entitled at the option of himself or his representatives to such share of the profits made since he ceased to be a partner as may be attributable to the use of his share of the property of the firm or to interest at the rate of six per cent per annum on the amount of his share in the property of the firm” — option not exercisable until the profit share is ascertained; e.g. C's funds 1,20,000 of 2,45,000, 3-months profit 28,000 → profit share ₹13,714 vs 6% interest ₹1,800, so he opts for profit.

Default rule: in the absence of agreement the legal representative gets interest @6% p.a. on the amount due from date of death to date of final payment.

Understanding explain with reasons · 1 question

- True/False trap: legal heirs are NOT entitled to the capital balance only --- they also get interest on capital up to death, share of goodwill, share of reserves/undistributed profits, revaluation profit and share of profit up to date of death, plus share of JLP; they are liable for drawings, interest on drawings and shares of losses.
- Explain profit up to date of death: time basis (last year's profit $\times$ months/12 $\times$ share) vs turnover basis (profit rate on sales applied to sales up to death); entry --- P&L Suspense A/c Dr To Deceased's Capital A/c.
- Know Section 37: if settlement is delayed, the executor may choose share of subsequent profits attributable to his funds OR interest @ 6% p.a. on the unpaid amount, whichever is chosen (option exercisable after profit is ascertained).

TQ 6.1 · PYQ 2024-Sep [1] (a) (vi) {C} · True/False · 2M · Pg 614

LEVEL I
Understanding

Easy

Topic 7: Integrated Problems

P1-C10-U10.5-T07

Read first Study the worked illustrations of Unit 5 combining revaluation, goodwill, reserves, profit to date of death, JLP/separate policies and the Deceased Partner's Executor's Account, with settlement by instalments or annuity.

NOTES

End-to-end sequence: revalue assets/liabilities, transfer reserves and goodwill (survivors' capitals Dr in gaining ratio, no goodwill account raised), credit profit to date of death via P&L Suspense, add JLP/SLP share — all credited to the deceased in OLD ratio — then close his Capital (and Current) A/c to the Executor's A/c; prepare Revaluation A/c, Capital A/cs, Executor's A/c and new Balance Sheet.

Deed clauses to read carefully: goodwill on average profits AFTER charging interest on capital and excluding abnormal items (profit on sale of assets, insurance claims, premium undercharged); part of profit carried to reserve ($B \frac{1}{2}$, $N \frac{1}{3}$, Reserve $\frac{1}{6} \rightarrow B:N = 3:2$); no interest on capital in the year of death; profit to death estimated as previous year's profit increased by an agreed % on proportionate basis.

Tricky PYQ items: car wrongly written off to travelling expenses added back net of depreciation when averaging profits; unrecorded liability charged through P&L Adjustment; JLP at surrender value in B/S — deduct book value from policy proceeds before distributing ($\text{₹}2,00,000 - 60,000 = 1,40,000$ in PSR); P&L Suspense appears on the asset side of the interim Balance Sheet.

Settlement patterns: immediate part payment with balance transferred to Executor's/Loan A/c carrying interest (e.g. ₹7,750 now, balance at 9% p.a.), or instalments; interest runs from date of death to settlement; be fluent with the standard entries so a 15–20 mark question finishes in time.

Application work the problem · 3 questions

PQ 7.5 · PYQ 2023-Jun [5] · Practical · 20M · Pg 625	LEVEL II Application	Hard
PQ 7.6 · MTP 2024-Dec S1 [4] (b) · Practical · 12M · Pg 629 asked 5×	LEVEL II Application	Hard
PQ 7.7 · PYQ 2025-Jan [4] (a) · Practical · 15M · Pg 632	LEVEL II Application	Hard

Analysis work through mixed data · 5 questions

- Work through death-mid-year problems: apportion profit to date of death (time or sales basis), value goodwill at 2--3 years' purchase of average profits, revalue assets, transfer reserves --- all credited to the deceased in OLD ratio, then close his capital to the Executor's A/c.
- Handle deed clauses carefully: profits allocated partly to reserve, interest on capital but not on undrawn profits, goodwill based on profits 'after charging interest on capital', and survivors purchasing the deceased's share on stated terms.
- Watch tricky items in PYQ balance sheets: advertisement suspense (fictitious asset written off in old ratio), investments taken over, and interest on the executor's unpaid balance from date of death to settlement.

PQ 7.1 · PYQ 2019-Jun [4] (a) · Practical · 10M · Pg 614 asked 5×	LEVEL II Analysis	Hard
PQ 7.2 · PYQ 2019-Nov [4] (a) · Practical · 10M · Pg 617 asked 2×	LEVEL II Analysis	Hard
PQ 7.3 · PYQ 2021-Jul [5] (c) · Practical · 10M · Pg 619 asked 2×	LEVEL II Analysis	Hard
PQ 7.4 · MTP 2022-Nov S1 [4] (a) · Practical · 10M · Pg 621	LEVEL II Analysis	Hard

PQ 7.8 • PYQ 2026-May [4] (a) • Practical • 10M • Pg 636

LEVEL II
Analysis

Hard

Synthesis prepare end-to-end — no question in this edition

- Master preparing end-to-end: Revaluation A/c, Partners' Capital A/cs, Deceased Partner's Executor's A/c, and the new Balance Sheet of the reconstituted firm.
- Practise settlement patterns: immediate part payment with balance in instalments plus interest, or transfer to Executor's Loan A/c; also full-length problems starting from a trial balance requiring the year's profit first.
- Be fluent with the standard journal entries (goodwill adjustment through gaining ratio without raising goodwill, P&L Suspense for profit to date of death) so a 15-- 20 mark question can be completed in time.

Unit 10.6: Dissolution of Partnership Firms and LLPs

P1-C10-U10.6 • Importance D • Rank 2 in chapter • Category A • 22.0% of chapter questions • 18 questions

Topic 1: Introduction

P1-C10-U10.6-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.1: scope of the unit — closing the books on dissolution and insolvency-related problems.

NOTES

Dissolution accounting: apart from readjusting partners' rights on change in ratio, admission, retirement or death, the other key aspect of partnership accounts is closing the books of account on dissolution — the unit covers circumstances leading to dissolution, accounting treatment to close the books, special problems on insolvency of partners and settlement of the partnership's liabilities.

Topic 2: Circumstances Leading to Dissolution of Partnership

P1-C10-U10.6-T02

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.2: dissolution of partnership vs dissolution of firm, the five cases of firm dissolution and the seven court grounds.

NOTES

Partnership dissolves on: (a) expiry of the term, (b) completion of the venture, (c) death of a partner, (d) insolvency of a partner — but remaining partners may continue the business (new partnership, firm continues); only when the business comes to an end is the FIRM dissolved.

Firm stands dissolved when: (i) partners agree to dissolve, (ii) all partners except one become insolvent, (iii) business becomes illegal, (iv) in partnership at will a partner gives notice of dissolution, (v) court orders dissolution.

Court may order dissolution where: a partner is of unsound mind, suffers permanent incapacity, is guilty of misconduct of business, persistently disregards the partnership agreement, transfers his interest/share to a third party, the business cannot be carried on except at a loss, or it appears just and equitable.

Topic 3: Consequences of Dissolution

P1-C10-U10.6-T03

Read first Study Section 6.3: order of settlement under Section 48 of the Partnership Act, distinction between dissolution of partnership and of the firm, and Section 6.3.1 on refund of premium when a firm is dissolved before the agreed fixed term.

NOTES

Section 48 order: (a) losses including capital deficiencies paid first out of profits, next out of capital, lastly by partners individually in profit sharing ratio; (b) assets (including sums contributed to make up deficiencies) applied: (i) debts of the firm to third parties, (ii) rateably to each partner for advances/loans as distinguished from capital, (iii) capitals, (iv) residue divided in profit sharing ratio.

Dissolution of partnership vs of firm: reconstitution vs extinction — key contrasts:

Dissolution of Partnership	Dissolution of Partnership Firm
Only the relation between partners is readjusted (admission/retirement/death)	Entire firm ceases to exist, relations among all partners end
Business continues as usual; firm is reconstituted	Business ceases altogether
Assets and liabilities revalued; Revaluation A/c; new Balance Sheet	Assets sold, liabilities paid off; Realization A/c prepared
No court intervention	Court can order dissolution of a firm
Books of accounts are not closed	Books of accounts are closed

Premium refund (6.3.1): a partner who paid a premium on admission with a stipulation of a fixed term is entitled to a reasonable/proportionate refund if the firm is dissolved before the term expires — regard to admission terms, agreed period and period expired (₹50,000 for 5 years, dissolved after 3 → unexpired $2/5 = ₹20,000$); refund borne by the other partners in profit sharing ratio.

No refund claim if: (1) firm dissolved due to death of a partner; (2) dissolution mainly due to the claiming partner's own misconduct; (3) dissolution in pursuance of an agreement containing no provision for return of the premium.

Application work the problem · 1 question

PQ 3.1 · PYQ 2018-Nov [6] (e) · Practical · 5M · Pg 642

LEVEL II
Application

Medium

Evaluation judge & justify — no question in this edition

- Be ready to judge premium-refund claims (Amit-type PYQ): a partner who paid a premium on admission with a fixed-term stipulation IS entitled to a reasonable/proportionate refund if the firm is dissolved early --- e.g. ₹50,000 paid for 5 years, dissolved after 3 years, refund of the unexpired $2/5 = ₹20,000$, borne by other partners in profit sharing ratio.
- Defend the exceptions --- NO refund claim arises if: dissolution is due to death of a partner, due to the claiming partner's own misconduct, or by an agreement with no provision for refund.
- Support answers with Section 48 order: losses out of profits, then capital, then partners personally; assets applied first to outside debts, then partners' advances/loans, then capitals, residue in profit sharing ratio.

Topic 4: Closing of Partnership Books on Dissolution

P1-C10-U10.6-T04

Read first Study Section 6.4: the Realization Account specimen --- which assets/liabilities are transferred, entries for realization expenses, assets/liabilities taken over by partners, unrecorded items, goodwill treatment, and closing capital and cash accounts.

NOTES

Realization A/c — what goes in: Dr side — all sundry assets at gross book value EXCLUDING cash/bank, debit balance of P&L (fictitious assets) and partners' current/capital/loan A/cs; payments of liabilities and unrecorded liabilities; realization expenses; Cr side — outside liabilities and provisions (e.g. provision for doubtful debts) at book figures, actual amounts realized, and assets taken over by partners (Dr that partner's Capital); balance = profit/loss on realization to

capitals in PROFIT SHARING ratio.

Goodwill on dissolution: if it appears in the B/S it is treated like any other asset and transferred to Realization A/c; if not in the books, no entry; anything realized for it (or purchase by a partner) is credited to Realization A/c.

Payment order interlinkage: cash applied to outside creditors first, then partners' loans (never through Realization A/c), then capitals; accumulated profits/reserves go straight to capitals, accumulated losses debited to capitals in PSR; unrecorded assets realized → Cr Realization, unrecorded liabilities paid → Dr Realization.

Death-then-dissolution problems: first settle the deceased partner's dues as a reconstitution (revaluation, goodwill, profit to date of death, Executor's A/c), then dissolve — transfer everything to Realization A/c and close capitals and cash to nil.

Application work the problem · 1 question

PQ 4.2 · PYQ 2026-Sep [4] (a) · Practical · 10M · Pg 648

LEVEL II
Application

Hard

Analysis work through mixed data · 1 question

- Work problems that combine a partner's death with subsequent dissolution (as in the M, N, O PYQ): first settle the deceased's dues (revaluation, goodwill, profit share), then close the books via Realization A/c.
- Keep the Realization A/c mechanics straight: transfer all assets except cash/bank, fictitious assets and partners' loan accounts; credit realized amounts and assets taken over by partners; debit payment of liabilities and expenses; profit/loss goes to capitals in profit sharing ratio.
- Watch interlinkages: partners' loans are paid after outside creditors but before capital; unrecorded assets realized are credited, unrecorded liabilities paid are debited to Realization A/c.

PQ 4.1 · PYQ 2022-Nov [4] (a) · Practical · 15M · Pg 643

LEVEL II
Analysis

Hard

Topic 5: Consequences of Insolvency of a Partner

P1-C10-U10.6-T05

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §6.5: the four legal consequences of adjudication and the Garner vs. Murray treatment of the debit balance.

NOTES

Consequences: (1) the partner adjudicated insolvent ceases to be a partner on the date of the order of adjudication, (2) the firm is dissolved on that date unless there is a contract to the contrary, (3) the insolvent partner's estate is not liable for any act of the firm after that date, (4) the firm is not liable for any acts of the insolvent partner after that date.

Deficiency: an unrecoverable debit balance in the insolvent partner's capital account is borne by the solvent partners — either in profit-sharing ratio, or per **Garner vs. Murray**: in proportion to their capitals and not in the profit-sharing ratio.

Topic 6: Loss arising from Insolvency of a Partner

P1-C10-U10.6-T06

Read first Study Sections 6.5 and 6.6: the Garner vs. Murray rule --- realization loss shared by ALL partners in profit sharing ratio, but the insolvent partner's capital deficiency borne by solvent partners in their CAPITAL ratio --- plus determination of the capital ratio (fixed vs fluctuating) and insolvency of all partners (Deficiency Account).

NOTES

Garner vs. Murray rule: normal loss on realization is borne by ALL partners (including the insolvent one) in the PROFIT SHARING ratio, but the insolvent partner's capital deficiency is borne by the solvent partners in their CAPITAL ratio — a statement saying deficiency is shared in profit sharing ratio is FALSE; if the deed provides a specific method, the deed prevails.

Capital ratio: fixed capitals — deficiency shared in the ratio of FIXED capitals (all adjustments for profits, drawings, interest, salary go through Current A/cs); fluctuating capitals — ratio of capitals AFTER adjusting reserves, accumulated profits, drawings and interest to date of dissolution but BEFORE profit/loss on Realization A/c.

When Garner vs. Murray does NOT apply: (i) a solvent partner has a debit capital balance (he cannot be asked to bear the deficiency); (ii) the firm has only two partners; (iii) agreement between partners to share the deficiency; (iv) all partners are insolvent; also whenever the deed prescribes its own method.

Insolvency of all partners: do NOT transfer creditors to Realization A/c — pay creditors what is available (including partners' contributions), transfer the unsatisfied balance to a Deficiency A/c / to capitals in profit sharing ratio, and close the worst-placed Capital A/c first, the last closing automatically.

Working pattern: prepare Realization A/c, Cash/Bank A/c and Capital A/cs; recover whatever the insolvent partner's estate pays, then distribute his remaining debit balance over solvent partners in capital ratio (e.g. loss shared by solvent P and Q in capitals 18,000:9,000 = 2:1).

Understanding explain with reasons · 2 questions

- True/False trap: under Garner vs. Murray the insolvency deficiency is borne in the CAPITAL ratio, NOT the profit sharing ratio --- a statement saying profit sharing ratio is FALSE.
- Memorise when Garner vs. Murray does NOT apply: partnership deed provides a specific method; only one solvent partner remains; all partners are insolvent; a solvent partner's capital account shows a debit balance (he cannot be asked to bear the deficiency).
- Explain the capital ratio: fixed capitals --- deficiency in fixed capital ratio (adjustments go through current accounts); fluctuating capitals --- ratio of capitals after adjusting reserves, drawings and interest but BEFORE realization profit/loss.

TQ 6.2 · PYQ 2026-May [1] (a) (ii) {C} · True/False · 2M · Pg 651

LEVEL I
Understanding**Easy**

TQ 6.1 · PYQ 2021-Dec [4] (b) · Descriptive · 6M · Pg 650

LEVEL I
Understanding**Medium****Application** work the problem · 4 questionsPQ 6.1 · MTP 2024-Dec S1 [3] (a) · Practical · 12M · Pg 651 **asked 2×****LEVEL II**
Application**Hard**

PQ 6.2 · RTP 2025-Jan [14] · Practical · --- · Pg 654

LEVEL II
Application**Hard**

PQ 6.3 · RTP 2025-May [14] · Practical · --- · Pg 658

LEVEL II
Application**Hard**

PQ 6.4 · RTP 2026-Jan [13] · Practical · --- · Pg 660

LEVEL II
Application**Hard****Synthesis** prepare end-to-end — no question in this edition

- Master the full 4-partner dissolution with one/two insolvent partners (P,Q,R,S 4:3:2:1-type): Realization A/c, Cash/Bank A/c and Capital A/cs, distributing each insolvent partner's deficiency over solvent partners in capital ratio.
- Practise variants: amounts recovered partly from the insolvent partner's estate, assets taken over by partners, and insolvency of all partners using a Deficiency Account (creditors not transferred to Realization A/c).

Topic 7: Piecemeal Payments

P1-C10-U10.6-T07

Read first Study Section 6.7: piecemeal distribution when assets are realized in instalments --- Maximum Loss Method (6.7.1) and Highest Relative Capital / Proportionate Capital Method (6.7.2), after paying outside liabilities and partners' loans in order.

NOTES

Payment order each instalment: provision for realization expenses first, then outside creditors (rateably if cash is short) — interest on loans from partners' SPOUSES ranks as an outside liability, then partners' loans (and interest thereon), and only then capitals; transfer reserves/undistributed profits to capitals and write off fictitious assets before distributing.

Maximum Loss Method (6.7.1): treat each instalment as the final payment — assume remaining assets are worthless; maximum possible loss = total of capitals – cash available, shared in PROFIT SHARING ratio and deducted from capitals; any notional debit balance is written off against the other partners in capital ratio (Garner vs. Murray) or PSR as applicable; pay the resulting credit balances.

Highest Relative Capital / Proportionate Capital Method (6.7.2): divide each capital by the profit share — smallest quotient gives the base capital; compute hypothetical capitals proportionate to the base and the EXCESS of actual over hypothetical capital (repeat among remaining partners); the partner with the largest excess is paid first until capitals stand in profit sharing ratio (capitals 15,000:18,000:9,000, PSR 2:2:1 → quotients 7,500/9,000/9,000, so B gets ₹3,000 and C ₹1,500 before A gets anything).

Both methods converge: final capitals must be left in profit sharing ratio, after which every further rupee is shared in PSR; present a Statement of Distribution of Cash with instalment-wise columns for creditors, partners' loans and each partner's capital — the standard 15–20 mark format.

Application work the problem · 3 questions

PQ 7.1 · PYQ 2018-Nov [4] (a) · Practical · 20M · Pg 662	LEVEL II Application	Hard
PQ 7.3 · PYQ 2021-Jan [3] (a) · Practical · 15M · Pg 668	LEVEL II Application	Hard
PQ 7.4 · MTP 2024-Apr [4] (a) · Practical · 10M · Pg 671 asked 2×	LEVEL II Application	Hard

Analysis work through mixed data · 2 questions

- Analyse the payment order in every instalment: realization expenses/provision first, then outside creditors (rateably if cash is short), then partners' loans (and interest on loans from partners' spouses ranks as an outside liability), and only then capitals.
- Under Maximum Loss Method, treat each instalment as final: assume remaining assets are worthless, compute maximum possible loss, share it in profit sharing ratio, apply Garner vs. Murray if a notional deficiency arises, and pay the resulting balances.
- Compare methods: both must leave partners' final capitals in profit sharing ratio; choose per the question's requirement.

PQ 7.2 · PYQ 2019-Nov [2] (a) · Practical · 15M · Pg 665	LEVEL II Analysis	Hard
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PQ 7.5 · MTP 2024-Jun [4] (a) · Practical · 8M · Pg 672

LEVEL II
Analysis

Hard

Synthesis prepare end-to-end — no question in this edition

- Master the full Statement of Distribution of Cash for 15--20 mark problems: instalment-wise columns for creditors, partners' loans and each partner's capital.
- Under Highest Relative Capital Method: divide capitals by profit shares to find the base capital, compute hypothetical capitals and excess capitals (repeat the process among remaining partners) --- pay the partner with the largest excess first until capitals reach the profit sharing ratio.
- Practise adjustments before distribution: transfer reserves/undistributed profits to capitals, write off fictitious assets, and handle contingencies like a fixed sum kept aside for realization expenses.

Topic 8: Winding up of a Limited Liability Partnership (LLP)

P1-C10-U10.6-T08

Read first Study Section 6.8: winding up of an LLP may be voluntary or by the Tribunal; memorise the six circumstances in which the Tribunal may wind up an LLP.

NOTES

Modes: winding up of an LLP may be either VOLUNTARY or by the TRIBUNAL, and the LLP so wound up may be dissolved; the Central Government may make rules for winding up and dissolution of LLPs.

Six Tribunal grounds (SM 6.8): (1) the LLP wishes to wind up; (2) it has fewer than 2 partners for more than 6 months; (3) it is unable to pay its debts; (4) it has not acted in the interest of the sovereignty and integrity of India; (5) it has failed to file Statements of Accounts and Solvency or annual returns with the Registrar for FIVE consecutive financial years; (6) the Tribunal thinks it just and equitable that it be wound up.

Number traps: quote the exact figures — 2 partners / 6 months, and 5 consecutive financial years of filing default ('three years' is FALSE).

Remembering memorise · 1 question

- Memorise the Tribunal winding-up grounds: (1) LLP wishes to wind up; (2) fewer than 2 partners for more than 6 months; (3) unable to pay its debts; (4) acted against the sovereignty and integrity of India; (5) failed to file Statements of Accounts and Solvency or Annual Returns for 5 consecutive financial years; (6) just and equitable in the Tribunal's opinion.
- Remember: winding up may be voluntary or by the Tribunal; the Central Government may make rules for winding up and dissolution of LLPs.

TQ 8.1 · PYQ 2020-Nov [6] (a) · Descriptive · 5M · Pg 674 **asked 2x**LEVEL I
Remembering

Medium

Understanding explain with reasons · 1 question

- True/False trap on the filing-default ground: the period is FIVE consecutive financial years of not filing Statements of Accounts and Solvency or Annual Returns --- a statement saying 'three consecutive years' is FALSE.
- Be able to give the reason with the correct ground when marking such statements, quoting the exact number (2 partners/6 months; 5 financial years).

TQ 8.2 · PYQ 2026-Jan [1] (a) (v) {C} · True/False · 2M · Pg 675

LEVEL I
Understanding**Easy****Topic 9: Integrated Problems**

P1-C10-U10.6-T09

Read first Study the comprehensive dissolution illustrations of Unit 6 combining Realization Account, capital adjustments, partner insolvency and special items like fraud losses, assets taken over and unrecorded items.

NOTES

Complete dissolution set: Realization A/c, Partners' Capital A/cs and Cash/Bank A/c carried through to nil balances — the Bank A/c totals prove the solution; distribute realization profit/loss in profit sharing ratio before final settlement of capitals.

Special items: assets taken over by a partner at agreed value — Dr his Capital, Cr Realization; liabilities settled at a discount — Dr Realization only with the amount actually paid; realization expenses borne/paid by a partner — Dr Realization, Cr his Capital; fraud/misappropriation discovered — write off against the partner concerned or through capitals; unrecorded assets and liabilities routed through Realization A/c.

Time management (8–15 marks): transfer all assets (except cash and fictitious items) and outside liabilities to Realization A/c first, then handle each adjustment one by one, then close partners' loans, capitals and cash in Section 48 order.

Application work the problem · 2 questions

PQ 9.1 · PYQ 2022-May [4] (a) · Practical · 15M · Pg 675

LEVEL II
Application**Hard**PQ 9.2 · PYQ 2024-Jun [3] (b) · Practical · 8M · Pg 678 **asked 3x****LEVEL II**
Application**Hard****Synthesis** prepare end-to-end — no question in this edition

- Master complete dissolution sets: Realization A/c, Partners' Capital A/cs and Cash/Bank A/c through to nil balances, with the Bank A/c totals proving the solution.

- Practise PYQ-style complications: frauds discovered before dissolution (write off against partners/profits), assets taken over by partners at agreed values, liabilities settled at a discount, realization expenses borne by a partner, and dishonoured/contingent items.
- Time-manage 8--15 mark problems: transfer everything to Realization A/c first, deal with adjustments one by one, and distribute realization profit/loss in the profit sharing ratio before final settlement.

CHAPTER 11

Company Accounts

42 Topics • 74 Classified Questions • Importance: A

ICAI SKILL PROFILE Level I 5–20% • Level II 80–95% — this chapter reads **in line with the paper**

 Level I — Remembering & Understanding **7.8%** 39 of 500 marks

 Level II — Application & Analysis **92.2%** 461 of 500 marks

Unit 11.1: Introduction to Company Accounts

P1-C11-U11.1 • Importance D • Rank 6 in chapter • Category C • 2.7% of chapter questions • 2 questions

Topic 1: Introduction

P1-C11-U11.1-T01

Read first Read paras 1.2 and 1.3 of Unit 1 (Introduction to Company Accounts): meaning of a company under the Companies Act, 2013 and the eleven salient features of a company, especially separate legal entity, perpetual existence, limited liability and common seal.

NOTES

Company in law (SM 1.2): an entity formed and incorporated under the Companies Act, 2013 or an existing company formed and registered under any previous company law; once formed it becomes a separate legal entity with perpetual succession, a distinct name and a common seal, and its existence is not affected by change of members.

Judicial definitions (SM): Justice Marshal — “A corporation is an artificial being, invisible, intangible and existing only in the contemplation of law”; Lord Justice Hanay — “an artificial person created by law with a perpetual succession and a common seal”.

Eleven salient features (para 1.3): (1) Incorporated association — registration under the Act is a must, no company exists without it (2) Separate legal entity — can contract, sue and be sued in its incorporated name (3) Perpetual existence — death, insolvency or change of members does NOT affect it (4) Common seal (5) Limited liability — only the amount agreed to be paid on shares; fully paid-up shares mean no further liability (6) Distinction between ownership and management (7) Not a citizen — legal existence but no citizenship rights (8) Transferability of shares (restricted in a private company) (9) Maintenance of books (10) Periodic audit by chartered accountants (11) Right of access to information per Articles.

Common seal now optional: documents that required the seal (bills of exchange, share certificates etc.) may instead be signed by two directors or one director plus a company secretary; every company registered in India must obtain a unique Corporate Identification Number (CIN) from the Registrar.

Understanding explain with reasons · 1 question

- Be able to justify True/False statements on company features with reasons --- e.g. perpetual existence: a company exists independent of its members, so death, insolvency or change of members does NOT affect its existence (True).
- Explain separate legal entity: a company can contract, sue and be sued in its own name; it is an artificial legal person created by law but not a citizen.
- Link limited liability to unpaid amount on shares --- a holder of fully paid-up shares has no further liability.
- Common trap: 'every public company is a listed company' is False; also note common seal is now optional (two directors or one director + company secretary may sign).

TQ 1.1 · PYQ 2019-Nov [1] (a) (vi) {C} · True/False · 2M · Pg 682 **asked**
5x

LEVEL I
Understanding

Easy

Topic 2: Meaning of Company

P1-C11-U11.1-T02

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.2: derivation of the word, the Companies Act definition and the judicial definitions of Justice Marshal and Lord Justice Hanay.

NOTES

Meaning: in law a company is one formed and incorporated under the Companies Act, 2013 or an existing company registered under any previous company law — once formed it becomes a separate legal entity having perpetual succession, a distinct name and a common seal, unaffected by change of members; capital generally consists of transferable shares and members have limited liability.

Judicial definitions: Justice Marshal — “A corporation is an artificial being, invisible, intangible and existing only in the contemplation of law”; Lord Justice Hanay — “an artificial person created by law with a perpetual succession and a common seal”; common thread — an association of persons created by law as a separate body for a special purpose.

Topic 3: Salient Features of a Company

P1-C11-U11.1-T03

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.3 listing the eleven salient features of a company.

NOTES

Eleven features: (1) incorporated association — created by operation of law, an artificial legal person; (2) separate legal entity — can contract, sue and be sued in its own name; (3) perpetual existence despite death/insolvency/change of members; (4) common seal — now optional, documents may instead be signed by two directors or one director and a company secretary; every Indian company gets a unique Corporate Identification Number (CIN); (5) limited liability — shareholder liable only upto amount agreed on shares allotted, no further liability if fully paid-up.

Continued: (6) distinction between ownership and management; (7) not a citizen — legal existence but no citizenship rights; (8) transferability of shares (private companies may restrict); (9) maintenance of prescribed books, failure attracts penalties; (10) periodic audit by chartered accountants appointed by shareholders on Board's recommendation; (11) shareholders' right of access to information per Articles, meetings and periodic reports.

Topic 4: Types of Companies

P1-C11-U11.1-T04

Read first Study para 1.4: the twelve types of companies with their section numbers under the Companies Act, 2013 --- Government (Sec 2(45), ≥51% paid-up capital), Foreign (2(42)), Private (2(68)), Public (2(71)), One Person (2(62)), Small (2(85)), Listed (2(52)), Unlimited, limited by shares/guarantee, Holding and Subsidiary companies.

NOTES

Twelve types (para 1.4): Government 2(45) · Foreign 2(42) · Private 2(68) · Public 2(71) · One Person 2(62) · Small 2(85) · Listed 2(52) · Unlimited 2(92) · limited by shares 2(22) · limited by guarantee 2(21) · Holding 2(46) · Subsidiary 2(87) — all of the Companies Act, 2013.

Government company (Sec 2(45)): not less than 51% of paid-up share capital held by Central Government and/or one or more State Governments, and includes a subsidiary of such a company;

Foreign (2(42)): incorporated outside India, having a place of business in India (itself, through an agent, or electronic mode) and conducting any business activity in India.

Private 2(68) vs Public 2(71): a private company by its articles (i) restricts the right to transfer shares (ii) limits members to 200 (excluding present and past employee-members; joint holders

count as one) and (iii) prohibits any invitation to the public to subscribe for securities; a public company is simply one which is not private — a subsidiary of a public company is deemed public even if private by its articles; no minimum paid-up capital is now prescribed for either.

Listed 2(52) and Small 2(85): listed company has ANY of its securities listed on ANY recognised stock exchange — an unlisted company may be public or private, and a listed public company that gets unlisted remains a public company; small company is a non-public company with paid-up capital not exceeding ₹4 crore AND turnover (preceding FY) not exceeding ₹40 crore, excluding holding/subsidiary companies, Sec 8 companies and bodies under a special Act.

Holding-Subsidiary 2(46)/2(87): subsidiary is a company in which the holding company controls the composition of the Board (power to appoint or remove all or a majority of directors) OR exercises/controls more than one-half of total share capital, alone or together with its subsidiaries — indirect control through subsidiaries also counts; **Others:** OPC 2(62) has only one member; unlimited company 2(92) has no limit on members' liability; company limited by guarantee 2(21) — liability limited to the amount members undertake to contribute on winding up.

Understanding explain with reasons · 1 question

- Listed company (Sec 2(52)) means a company having ANY of its securities listed on ANY recognised stock exchange --- not only equity shares and not only NSE; a statement restricting it to one exchange is False.
- Be ready with reasons for each definition-based True/False: private company limits members to 200 and restricts transfer; public company is one that is not private; an unlisted company can be public or private.
- Remember thresholds: Government company $\geq 51\%$ government holding; small company (other than public) paid-up capital $\leq$ ₹4 crore and turnover $\leq$ ₹40 crore; subsidiary --- holding company controls Board composition or more than half of total share capital.

TQ 4.1 · RTP 2023-Jun [1] (viii) · True/False · --- · Pg 683 asked 2×

LEVEL I
Understanding

Easy

Topic 5: Maintenance of Books of Account

P1-C11-U11.1-T05

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.5 on Section 128 of the Companies Act, 2013.

NOTES

Section 128: every company shall prepare and keep at its registered office books of account, other relevant books and papers and financial statement for every financial year giving a true and fair

view of the state of affairs (including branch offices) and explaining transactions at registered office and branches; books shall be kept on accrual basis and per the double entry system; books may be kept in electronic mode as prescribed.

Topic 6: Preparation of Financial Statements

P1-C11-U11.1-T06

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §1.6: Section 129, the Section 2(40) components and the three Divisions of Schedule III.

NOTES

Section 129: financial statements shall give a true and fair view, comply with notified accounting standards and be in the Schedule III form; the Board of Directors lays them before every annual general meeting.

Components — Sec 2(40): (i) balance sheet, (ii) profit and loss account (income and expenditure account for not-for-profit activity), (iii) cash flow statement, (iv) statement of changes in equity if applicable, (v) explanatory notes; One Person Company, small company and dormant company may omit the cash flow statement.

Schedule III: Part I — Balance Sheet format, Part II — Statement of Profit and Loss; Division I for companies applying Accounting Standards, Division II for those applying Ind AS, Division III for NBFCs applying Ind AS; specific Acts govern insurance, banking and electricity companies.

Unit 11.2: Issue, Forfeiture and Re-Issue of Shares

P1-C11-U11.2 · Importance A · Rank 1 in chapter · Category A · 37.8% of chapter questions · 28 questions

Topic 1: Introduction

P1-C11-U11.2-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.1: capital funding across forms of organisation and why the corporate form emerged.

NOTES

Capital by form: sole-proprietorship — proprietor's capital, unlimited liability; partnership — partners' capital, unlimited liability and only limited capital as member count is restricted; company — share capital from shareholders, liability limited to the issue price of shares held.

Emergence of company: with the industrial revolution capital requirements soared and risk of failure increased with technological pace; non-corporate entities could not cope with the pressure of increased capital and degree of risk, leading to the corporate form of organisation.

Topic 2: Share Capital

P1-C11-U11.2-T02

Read first Read para 2.2: meaning of share and share capital, and the categories --- authorised/nominal, issued, subscribed, called-up, paid-up and reserve capital (Sec 65) --- plus disclosure of share capital in Notes to Accounts.

NOTES

Share (SM 2.2): total capital is divided into a number of small indivisible units of a fixed amount, each unit being a share; the fixed value printed on the certificate is the nominal/par/face value, but issue price may differ; shareholder liability is limited to the issue price of shares acquired.

Six categories: Authorised/Nominal (maximum per Capital Clause of the Memorandum) · Issued (portion issued for cash or consideration other than cash; rest is Unissued, not shown in balance sheet) · Subscribed (part of issued capital applied for and allotted) · Called-up (portion of issue price demanded; balance is Uncalled) · Paid-up (called-up less calls-in-arrears) · Reserve capital (Sec 65 — subscribed uncalled capital which by resolution is callable only on winding up).

Chain: Authorised = Issued + Unissued; Called-up = Paid-up + Calls-in-arrears – Calls-in-advance; in Notes to Accounts every layer is disclosed, but ONLY paid-up capital (called-up less calls unpaid) is counted in the balance-sheet total.

Reserve Capital vs Capital Reserve (trap): reserve capital is uncalled share capital callable only on liquidation; capital reserve is part of Reserves and Surplus, created out of capital profits only and not available for declaration of dividend.

Understanding explain with reasons · 1 question

- Be able to answer True/False with reasons: a preference shareholder CAN also hold equity shares of the same company --- there is no bar; the statement is False.
- Explain the chain: Authorised = Issued + Unissued; Called-up = Paid-up + Calls-in-arrears; only paid-up capital enters the balance sheet total.
- Distinguish Reserve Capital (uncalled capital callable only on winding up) from Capital Reserve (part of Reserves and Surplus from capital profits) --- a favourite trap.

TQ 2.1 · PYQ 2021-Jul [1] (a) (iv) {C} · True/False · 2M · Pg 687 asked 3x

LEVEL 1
Understanding

Easy

Topic 3: Types of Shares

P1-C11-U11.2-T03

Read first Study para 2.3: preference shares (Sec 43) and their eight types --- cumulative/non-cumulative, participating/non-participating, redeemable/non-redeemable, convertible/non-convertible --- versus equity shares and their rights.

NOTES

Preference shares (Sec 43): assured preferential rights in (a) payment of dividend at a fixed rate and (b) repayment of capital on winding up; holders generally get NO voting rights; irredeemable preference shares are prohibited — redemption within 20 years of issue (beyond 20 years only for specified infrastructure projects, Sec 55).

Defaults (reason-based T/F): preference shares are cumulative, non-participating and non-convertible unless expressly stated otherwise; if cumulative preference dividend is in arrears for not less than 2 years, holders can vote on EVERY resolution in general meeting.

Eight types: cumulative (dividend accumulates till paid; arrears disclosed separately) / non-cumulative (right for the year expires) · participating (share in surplus profits and in winding-up surplus after equity paid) / non-participating · redeemable (repayable per Sec 55) / non-redeemable · convertible (holder's option to convert into equity per issue terms) / non-convertible.

Equity shares: shares which are not preference shares — no preferential right to dividend or capital repayment; dividend rate is variable, recommended by the Board depending on policy and profits left after preference rights; carry voting rights; equity with differential rights as to dividend/voting is permitted under prescribed rules.

Understanding explain with reasons · 1 question

- Preference shareholders generally do NOT enjoy voting rights --- so 'non-participating preference shareholders enjoy voting rights' is False; exception: cumulative preference dividend in arrears for 2+ years gives voting rights on every resolution.
- Reason out defaults: preference shares are cumulative, non-participating and non-convertible unless expressly stated otherwise.
- Know that irredeemable preference shares are prohibited; redemption beyond 20 years allowed only for specified infrastructure projects (Sec 55).
- Contrast equity shares: no preferential right to dividend or capital repayment, variable dividend recommended by the Board, voting rights attached, and differential-rights equity permitted under prescribed rules.

PQ 3.1 · PYQ 2021-Dec [1] (a) (iv) {C} · True/False · 2M · Pg 687 **asked 2×** **LEVEL I**
Understanding

Easy

Topic 4: Issue of Shares for Cash

P1-C11-U11.2-T04

Read first Read paras 2.4--2.5: procedure of issue through prospectus, minimum subscription (90% per SEBI), application/allotment/call instalments, and journal entries for full, under and over subscription.

NOTES

Procedure: public company issues a prospectus; issue price collected in instalments — application, allotment, first call ... final call; no allotment unless minimum subscription is received; **Sec 39:** application money at least 5% of NOMINAL (face) value; **SEBI:** minimum application money 25% of the ISSUE price, and minimum subscription 90% of the offer — failing 90%, refund all application money within 15 days of closure (70 days for an underwritten issue).

Pro-forma entries: Dr. Bank / Cr. Share Application (money received); Dr. Share Application / Cr. Share Capital (on allotment); Dr. Share Allotment / Cr. Share Capital (allotment due) then Dr. Bank / Cr. Share Allotment; each call — Dr. Share Call / Cr. Share Capital (due), Dr. Bank / Cr. Share Call; every amount = number of shares × instalment rate per share.

Combined account variant: Dr. Bank / Cr. Share Application and Allotment A/c; on allotment Dr. Share Application and Allotment / Cr. Share Capital with total application plus allotment money; Dr. Bank / Cr. Share Application and Allotment on receipt.

Under-subscription: applications fewer than shares offered — pass the same date-wise entries but base ALL amounts on shares actually applied/allotted (e.g. 40,000 of 43,000 issued); allotment valid only if minimum subscription received; unpaid amounts — Dr. Bank + Dr. Calls-in-Arrears / Cr. Share Allotment (or Call) A/c with total due.

Understanding explain with reasons · 1 question

- Sec 39: application money must be at least 5% of the NOMINAL (face) value; SEBI requires minimum 25% of the ISSUE price --- a statement quoting 25% as the Sec 39 limit is False.
- Interest on calls-in-arrears is payable BY the shareholder TO the company (max 10% per Table F); the company pays interest only on calls-in-advance --- watch this reversal trap.

TQ 4.1 · PYQ 2026-May [1] (a) (iv) {C} · True/False · 2M · Pg 688

LEVEL I
Understanding

Easy

Application practise the procedure · 1 question

- Practise the full journal-entry cycle: application received → transfer to capital → allotment due/received → each call due/received, computing amounts as shares × instalment rate.

- Handle under-subscription (base all entries on shares actually allotted, e.g. 40,000 of 43,000 issued) and record unpaid amounts in Calls-in-Arrears A/c.
- Practise date-wise entries (allotment, calls on specific dates) and closing entries at year end, including interest on calls-in-arrears/advance where dates are given.

PQ 4.1 · RTP 2022-May [17] · Practical · --- · Pg 688 asked 5x

LEVEL II
Application

Medium

Topic 5: Subscription of Shares

P1-C11-U11.2-T05

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §2.5 with Illustrations 2–4: full, under and over subscription and their entries.

NOTES

Full subscription: shares offered = shares subscribed; entries — application received: Dr. Bank / Cr. Share Application A/c; on allotment: Dr. Share Application / Cr. Share Capital; allotment due: Dr. Share Allotment / Cr. Share Capital; allotment received: Dr. Bank / Cr. Share Allotment; call due: Dr. Share Call / Cr. Share Capital, then Dr. Bank / Cr. Share Call on receipt.

Under subscription: shares applied are fewer than shares offered — same entries but amounts computed on shares actually applied and allotted; allotment can be made only when minimum subscription is received.

Over subscription: some applications rejected (Dr. Share Application A/c / Cr. Bank — refund) and others allotted partially (pro-rata) — excess application money is adjusted: Dr. Share Application A/c / Cr. Share Allotment A/c, Cr. Calls-in-Advance A/c, Cr. Bank (excess refunded).

Topic 6: Shares Issued at Discount

P1-C11-U11.2-T06

Read first Read para 2.6 and Section 53 of the Companies Act, 2013: prohibition of issue of shares at discount and the sweat-equity exception.

NOTES

Meaning: issue at less than nominal/par value; excess of nominal value over issue price = discount (₹100 share issued at ₹98 is a 2% discount).

Sec 53: a company CANNOT issue shares at a discount — any such issue is void and the company is punishable with fine; sole exception: sweat equity shares issued to directors or employees at a

discount or for consideration other than cash, for know-how, intellectual-property rights or value additions.

Exam contrast: debentures may be issued at any discount (no statutory limit), and re-issue of forfeited shares below face value is a sale, not a fresh issue at discount.

Understanding explain with reasons · 2 questions

- Sec 53: a company cannot issue shares at a discount --- any such issue is void and the company is punishable with fine; so 'a company is not allowed to issue shares at discount to the public' is True.
- Know the only exception: sweat equity shares issued to directors/employees for know-how, IPR or value additions.
- Note the contrast asked in exams: shares cannot be issued at discount but debentures can, and re-issue of forfeited shares below face value is not a fresh issue at discount.

TQ 6.1 · PYQ 2021-Jul [1] (a) (ii) {C} · True/False · 2M · Pg 690	asked 3×	LEVEL I Understanding	Easy
TQ 6.2 · PYQ 2025-Sep [1] (a) (vi) {C} · True/False · 2M · Pg 690		LEVEL I Understanding	Easy

Topic 7: Shares Issued at Premium

P1-C11-U11.2-T07

Read first Study para 2.7 and Section 52: meaning of premium, credit to Securities Premium Account (shown under Reserves and Surplus), and the five permitted uses of the account.

NOTES

Meaning: issue price above face value; premium = excess of issue price over face value (₹100 share at ₹105 is a 5% premium); premium is generally called with allotment, sometimes with application, rarely with calls.

Treatment: premium is NOT share capital — it is a gain of capital nature credited to a separate "Securities Premium Account", shown under Reserves and Surplus (shareholders' funds) and not available for dividend.

Five uses (Sec 52): (a) fully paid bonus shares to members (b) writing off preliminary expenses (c) writing off expenses of, or commission paid, or discount allowed on issue of securities or debentures (d) premium on redemption of redeemable preference shares or debentures (e) purchase (buy-back) of own shares or other securities.

Ind AS restriction: companies of the class prescribed under Sec 133 (Ind AS-compliant) cannot use securities premium for (b) preliminary expenses or (d) premium on redemption.

Entry (premium with allotment): Dr. Share Allotment / Cr. Share Capital + Cr. Securities Premium;
if called with application — Dr. Share Application / Cr. Share Capital + Cr. Securities Premium on allotment.

Understanding explain with reasons · 1 question

- Memorise the five uses of Securities Premium (Sec 52): fully paid bonus shares to members; writing off preliminary expenses; writing off expenses/commission/discount on issue of securities or debentures; premium on redemption of preference shares or debentures; buy-back of own shares --- so using it to write off preliminary expenses is True.
- Explain why premium is not share capital: it is a capital gain credited to a separate account and cannot be used for dividend.
- Note: Ind AS companies (Sec 133 class) cannot use it for preliminary expenses or premium on redemption.

TQ 7.1 · PYQ 2026-Jan [1] (a) (vi) {C} · True/False · 2M · Pg 691 asked 2× **LEVEL I**
Understanding

Easy

Topic 8: Over Subscription and Pro-Rata Allotment

P1-C11-U11.2-T08

Read first Read paras 2.5.3 and 2.8: treatment of over-subscription --- rejection with refund, pro-rata allotment, and adjustment of excess application money towards allotment and calls.

NOTES

Over-subscription: applications exceed shares offered; the company may reject some applications (refund money), allot others in full, or allot pro-rata — allotment in proportion of shares applied for (12,000 applied for 10,000 offered = 6:5, so an applicant for 6 shares gets 5).

Adjustment of excess: excess application money is adjusted against allotment dues and then future calls; balance is refunded — entries: Dr. Share Application / Cr. Bank (rejected applications); Dr. Share Application / Cr. Share Allotment + Cr. Calls-in-Advance + Cr. Bank (pro-rata adjustment and refund).

Defaulter working (crux of 15-markers): shares APPLIED by defaulter = shares allotted × (applied ÷ allotted ratio); excess paid on application = (applied – allotted) × application rate; actual arrears = amount due on allotment/call – excess already adjusted (e.g. Raj: applied 1,500, allotted 1,125, excess ₹3,375 adjusted against call, arrears ₹3,375).

Premium note: where pro-rata shares are issued at premium, excess application money is adjusted FIRST to capital and then to securities premium.

Application practise the procedure · 1 question

- Master the pro-rata working: shares applied ÷ shares allotted ratio (e.g. 8,00,000 applied for 6,00,000), excess application money credited to Share Allotment (and Calls-in-Advance if it exceeds allotment dues), balance refunded.
- For a defaulting shareholder under pro-rata, first compute shares APPLIED = allotted × ratio, then excess already paid, then actual allotment/call arrears --- this is the crux of 15-mark questions.
- Practise the full set of journal entries including premium with allotment, calls in two equal instalments, and final refund figures.

PQ 8.1 · PYQ 2024-Sep [6] (a) · Practical · 15M · Pg 691 asked 2×

LEVEL II
Application

Hard

Topic 9: Calls-In-Arrears and Calls-In Advance

P1-C11-U11.2-T09

Read first Read para 2.9: meaning and journal entries for Calls-in-Arrears (deducted from called-up capital) and Calls-in-Advance (a liability until the call is due), with Table F limits.

NOTES

Calls-in-arrears: total unpaid amount on one or more instalments (allotment/calls); shown as a DEDUCTION from called-up capital to arrive at paid-up capital; entry — Dr. Calls-in-Arrears A/c (unpaid) + Dr. Bank (received) / Cr. Share Allotment or Share Call A/c (total due).

Calls-in-advance: amount of calls not yet made but already paid by a shareholder — a liability (Other Current Liabilities), never capital; entry — Dr. Bank / Cr. Calls-in-Advance; when the call falls due — Dr. Calls-in-Advance + Dr. Bank (balance received) / Cr. the particular Call A/c.

Table F limits: interest chargeable on calls-in-arrears at maximum 10% p.a. (company's income) and payable on calls-in-advance at maximum 12% p.a. (company's expense); no dividend is payable on calls-in-advance; in the balance sheet show called-up capital less calls-in-arrears, with calls-in-advance as a separate liability.

Application practise the procedure · 3 questions

- Practise entries: Calls-in-Arrears A/c Dr with unpaid amounts; Bank Dr / To Calls-in-Advance on receipt of future call money; adjust Calls-in-Advance against the call when it falls due.
- Work 15-mark problems combining premium, partial payment by one holder (e.g. holder of 2,000 shares not paying allotment) and later receipt with interest.
- Prepare Bank/Cash Book alongside journal and show balance sheet extract: called-up capital less calls-in-arrears; calls-in-advance under Other Current Liabilities.
- Where a fresh issue with dates is given, track each instalment holder-wise before computing arrears/advance balances.

PQ 9.3 · RTP 2024-Sep [14] · Practical · --- · Pg 697 asked 5×	LEVEL II Application	Medium
PQ 9.1 · PYQ 2022-May [6] (a) · Practical · 15M · Pg 693 asked 4×	LEVEL II Application	Hard
PQ 9.2 · PYQ 2021-Jan [6] (a) · Practical · 15M · Pg 695 asked 9×	LEVEL II Application	Hard

Topic 10: Interest on Calls-in-Arrears and Calls-in- Advance

P1-C11-U11.2-T10

Read first Study para 2.10: Table F maximum rates --- 10% p.a. on calls-in-arrears (income), 12% p.a. on calls-in-advance (expense) --- periods of calculation and journal entries.

NOTES

Rule (para 2.10): interest per the Articles within Table F maxima — 10% p.a. on calls-in-arrears (recoverable BY the company from the shareholder) and 12% p.a. on calls-in-advance (payable BY the company); month-counting from exact dates is where marks are lost.

Interest on Calls-in-Arrears	Interest on Calls-in-Advance
Payable by shareholders to company on calls due but unpaid	Payable by company on call money received before it is due
Table F maximum: 10% p.a.	Table F maximum: 12% p.a.
Period: date call was due to date money finally received	Period: date money received to date call is finally made due
Directors may waive it in individual cases	No dividend is payable on calls-in-advance
Nominal a/c — credited to Statement of P&L as income	Nominal a/c — an expense in Statement of P&L

Entries: arrears — Dr. Shareholders'/Sundry Members' A/c / Cr. Interest on Calls-in-Arrears, then Dr. Bank / Cr. Shareholders'; advance — Dr. Interest on Calls-in-Advance / Cr. Shareholder's A/c, then Dr. Shareholder's / Cr. Bank on payment.

Worked cue (Illustration 9): advance of ₹25,000 held 3 months at 12% = ₹750 paid to Mr. Nair; arrears of ₹2,500 held 2 months at 10% = ₹41.67 received with the call money.

Application practise the procedure · 2 questions

- Compute interest on arrears from the due date of the call to the date of actual receipt, and on advance from the date of receipt to the date the call is made due --- month counting is where marks are lost.

- Practise entries: Shareholder/Sundry Members A/c Dr To Interest on Calls-in- Arrears (income); Interest on Calls-in-Advance A/c Dr To Shareholder, then payment --- interest on advance is an expense in the Statement of P&L.
- Solve full 15-mark issues (e.g. 3,00,000 shares at ₹5 premium) where one holder pays a call late and another pays calls early, combining pro-rata, premium and both interest computations.

PQ 10.1 · PYQ 2025-Jan [6] (a) · Practical · 15M · Pg 699 **asked 5×****LEVEL II**
Application**Hard**

PQ 10.2 · PYQ 2025-May [6] (a) · Practical · 15M · Pg 702

LEVEL II
Application**Hard**

Topic 11: Forfeiture of Shares

P1-C11-U11.2-T11

Read first Read para 2.11: conditions and entries for forfeiture of shares issued at par and at premium --- debit Share Capital with called-up amount, credit Forfeited Shares A/c with amount received, cancel unpaid Calls-in-Arrears; reverse Securities Premium only if premium was not received.

NOTES

Meaning: cancellation of shares by the company (power in Articles, after proper notice) for non-payment of allotment or calls; holder's title is extinguished and amounts already paid are NOT refunded; directors may cancel the forfeiture before re-allotment; fully paid-up shares are forfeitable only for realisation of the member's debts if the Articles so provide.

Entry, issue at par: Dr. Share Capital A/c with number of shares × CALLED-UP value per share / Cr. Share Allotment / Call A/cs (or Calls-in-Arrears) with amounts due but unpaid, and Cr. Forfeited Shares A/c with the amount actually RECEIVED — not with calls-in-arrears.

Premium rule: premium already received is NEVER cancelled on forfeiture; if premium was due but unpaid, also Dr. Securities Premium A/c to reverse the credit made at allotment — e.g. 5,000 shares of ₹100 at 20% premium, only ₹20 application paid: Dr. Share Capital ₹5,00,000 + Dr. Securities Premium ₹1,00,000 / Cr. Allotment ₹2,50,000 + Cr. First and Final Call ₹2,50,000 + Cr. Forfeited Shares ₹1,00,000.

Variants to drill: fully called shares (Cr. Forfeited Shares with total received, cancel unpaid final call), partly called shares (debit capital only with called-up ₹8, not face ₹10), and pro-rata cases — first compute shares applied and excess application money (adjusted to capital first, then premium) before finding arrears and the amount received on forfeited shares.

Understanding explain with reasons · 1 question

- The standard entry is True/False bait: Share Capital A/c is debited with CALLED- UP capital of forfeited shares and Forfeited Shares A/c is credited with the amount RECEIVED (not with calls-in-arrears) --- statement as framed is False.

- Explain premium rule: premium already received is never cancelled on forfeiture; premium due but unpaid requires debiting Securities Premium A/c.

TQ 11.1 · MTP 2024-Jul [1] (a) (iv) {C} · True/False · 2M · Pg 705 **asked**
7x

LEVEL I
Understanding

Easy

Application practise the procedure · 2 questions

- Practise forfeiture after letters of regret and pro-rata allotment (e.g. 25,000 shares of ₹100 at ₹25 premium) --- compute amount received on forfeited shares carefully.
- Drill three variants: forfeiture of fully called shares, partly called shares, and shares issued at premium with allotment (incl. premium) unpaid.

PQ 11.1 · PYQ 2023-Dec [6] (a) · Practical · 15M · Pg 705 **asked 3x**

LEVEL II
Application

Hard

PQ 11.2 · PYQ 2026-Sep [5] (c) · Practical · 10M · Pg 708

LEVEL II
Application

Hard

Topic 12: Re-issue of Forfeited Shares

P1-C11-U11.2-T12

Read first Study para 2.12: re-issue entries, the rule that loss (discount) on re-issue cannot exceed the forfeited amount on those shares, transfer of surplus to Capital Reserve, and proportionate transfer when only part of the forfeited shares is re- issued.

NOTES

Nature: a forfeited share merely remains vested in the company for disposal — re-issue is only a SALE, not an allotment; shares may be re-issued at any price so long as total received (original allottee plus new purchaser) is not less than the face value.

Entries: Dr. Bank (actual amount received) + Dr. Forfeited Shares A/c (loss/discount on re-issue) / Cr. Share Capital; surplus — Dr. Forfeited Shares / Cr. Capital Reserve; if re-issue price exceeds face value, the excess is credited to Securities Premium A/c.

Rules: loss on re-issue cannot exceed the amount forfeited on those shares; the balance of Forfeited Shares A/c is no surplus until re-issue (company may allow the new buyer a discount up to that credit); forfeited amount on shares not yet re-issued is shown under 'Share Capital' (Add: Forfeited shares).

Formula: Capital Reserve = amount forfeited on RE-ISSUED shares - discount allowed on re-issue, computed lot-wise (Ram: ₹3 forfeited - ₹2 loss = ₹1 × 500; Shyam: ₹6 - ₹2 = ₹4 × 750; total ₹3,500).

Part re-issue: transfer to Capital Reserve only for the portion re-issued — e.g. 1,500 of 2,000 forfeited shares re-issued at ₹65 paid-up ₹75: forfeited ₹25 per share - loss ₹10 = ₹15 × 1,500 =

₹22,500; credit on the remaining 500 shares is carried forward in Forfeited Shares A/c till re-issued.

Understanding explain with reasons · 2 questions

- Re-issue of forfeited shares is a SALE, not an allotment --- the forfeited share merely vests in the company for disposal; so 'reissue is allotment but not sale' is False.
- Restate the forfeiture entry correctly (Share Capital Dr with called-up; credit Forfeited Shares with amount received) and reason why the balance of Forfeited Shares A/c is no surplus until re-issue.
- If re-issue price exceeds face value, the excess goes to Securities Premium A/c.

TQ 12.1 · PYQ 2021-Jan [1] (a) (i) {C} · True/False · 2M · Pg 710 asked 5×	LEVEL I Understanding	Easy
TQ 12.2 · RTP 2023-Dec [1] (x) · True/False · ---- · Pg 711	LEVEL I Understanding	Easy

Application practise the procedure · 10 questions

- Formula to master: Capital Reserve = amount forfeited on re-issued shares – discount allowed on re-issue; transfer only for the portion re-issued (e.g. 3,000 of 4,000 shares re-issued).
- Practise end-to-end 15-mark problems: over-subscription + pro-rata + premium + forfeiture of two lots + re-issue as fully paid, preparing journal, Cash Book and balance-sheet extract.
- Drill part re-issue at different prices to different persons (e.g. 400 of 600 shares to Z) and short 4-mark forfeiture/re-issue entry sets.

PQ 12.1 · PYQ 2019-Jun [6] (a) · Practical · 10M · Pg 711 asked 7×	LEVEL II Application	Medium
PQ 12.4 · RTP 2022-May [18] · Practical · --- · Pg 717	LEVEL II Application	Medium
PQ 12.5 · MTP 2023-Apr [6] (a) · Practical · 10M · Pg 718 asked 2×	LEVEL II Application	Medium
PQ 12.7 · PYQ 2018-Nov [6] (a) (i) · Practical · 4M · Pg 724 asked 12×	LEVEL II Application	Medium
PQ 12.9 · PYQ 2026-Jan [5] (c) · Practical · 10M · Pg 729 asked 2×	LEVEL II Application	Medium
PQ 12.2 · PYQ 2021-Jul [6] (a) · Practical · 15M · Pg 713	LEVEL II Application	Hard
PQ 12.3 · PYQ 2021-Dec [6] (a) · Practical · 15M · Pg 715 asked 4×	LEVEL II Application	Hard
PQ 12.6 · PYQ 2023-Jun [6] (a) · Practical · 15M · Pg 720 asked 5×	LEVEL II Application	Hard
PQ 12.8 · PYQ 2025-Sep [6] (a) · Practical · 15M · Pg 725	LEVEL II Application	Hard
PQ 12.10 · PYQ 2026-May [6] (a) · Practical · 15M · Pg 732	LEVEL II Application	Hard

Topic 13: Issue of Shares for Consideration other than Cash

P1-C11-U11.2-T13

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §2.13 with Illustration 18: shares issued in exchange for assets or promoters'/lawyers' services.

NOTES

Nature: shares may be issued in direct exchange for land, buildings or other assets, or in payment for services of promoters/lawyers in formation; shown separately under 'Share Capital'; within specified time of allotment the company must produce before the Registrar a written contract of sale/of services for which shares were allotted.

Measurement: under accounting standards the acquisition cost of an asset acquired by issue of shares/securities is the fair value of the securities issued (may be indicated by issue price determined by statutory authorities) — not necessarily equal to nominal/par value.

Entries: Dr. Asset A/c / Cr. Vendor A/c on purchase, then Dr. Vendor A/c / Cr. Share Capital A/c on allotment of fully paid shares (or directly Dr. Assets A/c / Cr. Share Capital A/c).

Unit 11.3: Issue of Debentures

P1-C11-U11.3 • Importance D • Rank 2 in chapter • Category A • 20.3% of chapter questions • 15 questions

Topic 1: Introduction

P1-C11-U11.3-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §3.1: why companies turn to debt financing and debentures.

NOTES

Debt financing: with ever-growing needs of corporate expansion and growth, equity financing is not sufficient — issuing debt instruments for public subscription both reduces the cost of capital and helps design an appropriate capital structure; the debenture is one of the most commonly used debt instruments issued by a company to raise funds.

Topic 2: Meaning

P1-C11-U11.3-T02

Read first Read para 3.2: definition of debenture under Sec 2(30) of the Companies Act, 2013 (includes debenture stock, bonds or any instrument evidencing a debt, whether or not charged on assets) and para 3.4 distinction between debentures and shares.

NOTES

Debenture, Sec 2(30) (SM): “‘Debenture’ includes debenture stock, bonds or any other instrument of a company evidencing a debt, whether constituting a charge on the assets of the company or not” — so a debenture may be secured or unsecured.

Nature: a bond issued by a company under its seal acknowledging a debt, with provisions for repayment of principal and interest; a charge, if created, is valid only when registered with the Registrar; trustees are customarily appointed to safeguard mortgage-debenture holders; NO company may issue debentures carrying voting rights — holders are creditors, not owners.

Debentures	Shares
Holders are creditors of the company	Holders are owners of the company
No voting rights — no threat to control	Voting rights — control the company's affairs
Fixed-rate interest, payable whether or not there is profit	Dividend variable (equity), depends on profits
Interest is a charge against profit, tax-deductible	Dividend is an appropriation, not deductible
Shown under Long Term Borrowings	Shown under Shareholders' Funds — Share Capital
Cannot be forfeited; convertible per issue terms	Forfeitable for unpaid calls; never convertible
On liquidation, paid off BEFORE shareholders	Shareholders are paid last of all

Understanding explain with reasons · 1 question

- Debenture holders are CREDITORS, not owners --- they have no voting rights; the Act expressly bars issue of debentures carrying voting rights, so the statement 'debenture holders enjoy voting rights' is False.
- Explain with reasons: debentures may be secured or unsecured; interest is a charge against profit (tax-deductible) while dividend is an appropriation.
- Remember: debentures appear under Long Term Borrowings; on liquidation debenture holders are paid before shareholders.

TQ 2.1 · MTP 2024-May [1] (a) (vi) {C} · True/False · 2M · Pg 738 **asked**
3x

LEVEL I
Understanding

Easy

Topic 3: Features of Debentures

P1-C11-U11.3-T03

Read first Study para 3.3 (six features of debentures) and the footnote on charges: fixed charge = mortgage on specific assets; floating charge = covers all assets including future assets.

NOTES

Six features (para 3.3): (1) a document evidencing a loan made to the company (2) a fixed interest-bearing security with interest falling due on specific dates (3) interest at a predetermined fixed rate regardless of the level of profit (4) principal repaid at a specified future date or converted into shares/other debentures (5) may or may not create a charge on assets as security (6) generally tradeable through the stock exchange above or below face value.

Fixed vs floating charge (footnote): a FIXED charge is a mortgage on SPECIFIC assets which cannot be sold without the debenture holders' consent, their sale proceeds repaying holders first; a FLOATING charge generally covers ALL assets of the company including future assets — the swapped statement is the standard False trap.

Understanding explain with reasons · 1 question

- A FIXED charge is on specific assets which cannot be sold without debenture holders' consent; it is the FLOATING charge that generally covers all assets including future ones --- the swapped statement is False.
- Explain features: document evidencing loan, fixed-rate interest payable on specific dates irrespective of profits, repayable/convertible at a future date, tradeable on stock exchange above or below face value.

TQ 3.1 · PYQ 2022-Nov [1] (a) (vi) {C} · True/False · 2M · Pg 739 **asked**
2x

LEVEL I
Understanding

Easy

Topic 4: Distinction Between Debentures and Shares

P1-C11-U11.3-T04

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §3.4: the ten-point tabular distinction between debentures and shares.

NOTES

Debentures	Shares
Holders are creditors of the company	Holders are owners of the company
No voting rights — no threat to existing control	Voting rights — control affairs of the company
Interest at pre-determined fixed rate, payable whether profit or not; ranks ahead of all shares	Equity dividend at variable rate affected by profits (preference dividend fixed)
Interest is a charge against profits, tax-deductible	Dividend is an appropriation of profit, not deductible
Many kinds: secured/unsecured, redeemable/irredeemable, registered/bearer, convertible/non-convertible	Only two kinds — equity and preference
Shown under “Long Term Borrowings” in balance sheet	Shown under “Shareholders' Funds” — Share Capital
Convertible into other debentures or shares per terms of issue	Shares cannot be converted into other shares
Cannot be forfeited for non-payment of calls	Can be forfeited for non-payment of allotment/call money
Money back at maturity per redemption terms	Equity money back only on liquidation (preference earlier)
On liquidation, paid off before shareholders	On liquidation, paid last after debenture holders, trade payables etc.

Topic 5: Types of Debentures

P1-C11-U11.3-T05

Read first Read para 3.5: classification by security (secured/naked), convertibility (convertible/non-convertible), permanence (redeemable/irredeemable or perpetual), negotiability (registered/bearer) and priority (first/second mortgage).

NOTES

Five bases (para 3.5): Security — secured (fixed/floating charge) vs unsecured/naked (mere promise to pay, risky for investors); Convertibility — convertible (fully or partly, into equity at par/premium/discount per issue terms — holders get a chance to become shareholders) vs non-

convertible (simply repaid); Permanence — redeemable (repayable per terms, e.g. after 8 years) vs irredeemable/perpetual (not repayable during the company's lifetime, repaid only on liquidation); Negotiability — registered vs bearer; Priority — first vs second mortgage.

Registered vs bearer: registered — payable to the holder whose name/address/holding is in the Register of Debenture holders, not easily transferable, transfer per Companies Act, 2013 formalities; bearer — negotiable instruments transferable by mere delivery, no transfer deed and no company record, interest paid to the bearer irrespective of identity.

Priority: first mortgage debentures are payable first out of the property charged; second mortgage debentures are payable only after satisfying the first mortgage debentures.

Understanding explain with reasons · 1 question

- Irredeemable (perpetual) debentures are not repayable during the lifetime of the company and are repaid only on liquidation --- so 'perpetual debentures are payable at the time of liquidation' is True.
- Contrast registered debentures (transfer per Companies Act formalities) with bearer debentures (negotiable, transferable by mere delivery, interest paid to bearer).
- First mortgage debentures are paid first out of the charged property; second mortgage debentures only after them.
- Also be clear on convertibility: convertible debentures (fully or partly) can become equity shares per issue terms, giving holders a chance to become shareholders; non-convertible debentures are simply repaid.

TQ 5.1 · PYQ 2023-Jun [1] (a) (v) {C} · True/False · 2M · Pg 739

LEVEL I
Understanding

Easy

Topic 6: Issue of Debentures

P1-C11-U11.3-T06

Read first Study para 3.6: journal entries for debentures issued at par, discount or premium (premium credited to Securities Premium A/c), money payable in instalments, and issue with varying redemption terms.

NOTES

Basic cycle (at par): Dr. Bank / Cr. Debenture Application; on allotment Dr. Debenture Application / Cr. ...% Debentures; allotment call — Dr. Debenture Allotment / Cr. ...% Debentures, then Dr. Bank / Cr. Debenture Allotment; same pattern for calls; over-subscription — refund excess on the refund date: Dr. Debenture Application / Cr. Bank.

At discount: Dr. Debenture Application (cash) + Dr. Discount on Issue of Debentures A/c / Cr. ...% Debentures at nominal value — the Act places NO limit on debenture discount; **At premium:** Cr.

Securities Premium A/c — debentures are 'securities', so utilisation of the premium is governed by Sec 52.

Redeemable at premium: recognise the redemption premium at allotment itself (prudence) — Dr. Loss on Issue of Debentures / Cr. Premium on Redemption of Debentures A/c (a personal account, a liability); issued at par the loss equals the redemption premium (e.g. ₹100 debenture redeemable at ₹110: loss ₹10).

Discount plus redemption premium: Dr. Debenture Allotment + Dr. Discount/Loss on Issue (discount + premium on redemption) / Cr. ...% Debentures + Cr. Premium on Redemption — e.g. issue at 6% discount redeemable at 5% premium on ₹100: total loss ₹11 per debenture.

Pricing logic: debentures are issued at discount when the market interest rate exceeds the coupon rate (true rate $12 \div 90 \times 100 = 13.33\%$) and at premium when the market rate is lower (effective $12 \div 110 \times 100 = 10.91\%$).

Application practise the procedure · 3 questions

- Practise the basic cycle: Bank Dr To Debenture Application; Debenture Application Dr To ...% Debentures (and To Securities Premium if issued at premium); allotment due/received entries.
- Handle over-subscription of debentures --- refund excess application money on the refund date (e.g. 3,85,000 applied vs 3,50,000 issued).
- For partly convertible debentures, split the convertible portion converted into equity from the non-convertible balance, and compute interest on outstanding amounts for the period.
- Drill issue at discount redeemable at premium/at discount: debit Discount/Loss on Issue of Debentures with both discount and premium payable on redemption, crediting Premium on Redemption of Debentures A/c.

PQ 6.1 · PYQ 2021-Jul [5] (b) · Practical · 10M · Pg 740 asked 2×	LEVEL II Application	Medium
PQ 6.2 · RTP 2024-Sep [15] · Practical · --- · Pg 742 asked 4×	LEVEL II Application	Medium
PQ 6.3 · RTP 2025-May [16] · Practical · --- · Pg 742	LEVEL II Application	Medium

Topic 7: Issue of Debentures as Collateral Security

P1-C11-U11.3-T07

Read first Read para 3.7: meaning of collateral security and the two disclosure methods --- Method 1 (no entry; note under the secured liability) and Method 2 (Debentures Suspense A/c Dr To % Debentures A/c).

NOTES

Meaning: company's own debentures issued as secondary/supporting security for a loan or fluctuating overdraft; the lender can enforce them only if the loan is not repaid on the due date (then becomes a debenture holder with all rights); interest is payable ONLY on the loan, not on the collateral debentures; debentures are released when the loan is repaid.

Method 1 (preferred, no entry): no entry in the books — the fact of issue is shown by a note under the secured liability in Notes to Accounts, e.g. IDBI loan ₹1,00,00,000 “Collaterally secured by issue of ₹1,50,00,000 14% First Mortgage Debentures”.

Method 2: Dr. Debentures Suspense A/c / Cr. ...% Debentures A/c; Debentures Suspense appears on the ASSETS side under Other Non-Current Assets with the debentures on the liabilities side as per contra — a statement putting it on the liability side is False; the entry is reversed when the loan is repaid.

Understanding explain with reasons · 1 question

- Debentures Suspense Account appears on the ASSETS side (Other Non-Current Assets), with the debentures shown on the liabilities side as per contra --- so the statement that it appears on the liability side is False.
- Explain the mechanics: lender can enforce the debentures only if the loan is not repaid; interest is payable only on the loan, not on the collateral debentures; the entry is reversed when the loan is repaid.

TQ 7.1 · PYQ 2022-May [1] (a) (v) {C} · True/False · 2M · Pg 744 asked 4x LEVEL I Understanding

Easy

Topic 8: Issue of Debentures in Consideration other than for Cash

P1-C11-U11.3-T08

Read first Study para 3.8: entries when debentures are issued to vendors for assets/business taken over --- Sundry Assets Dr, To Liabilities, To Vendors; then Vendors Dr To Debentures (and Securities Premium, or with Discount on Issue debited), with goodwill or capital reserve balancing.

NOTES

Entries (vendor/business takeover): Dr. Sundry Assets (assets taken over) / Cr. Sundry Liabilities (liabilities assumed) + Cr. Vendors (purchase consideration); then Dr. Vendors / Cr. Debentures — with Cr. Securities Premium if issued at premium, or Dr. Discount on Issue of Debentures if at discount.

Number of debentures: purchase consideration ÷ issue price per debenture — at par: $PC \div \text{par value}$; at premium: $PC \div (\text{par} + \text{premium})$; at discount: $PC \div (\text{par} - \text{discount})$.

Goodwill/Capital Reserve: excess of purchase consideration over net assets taken over is debited to Goodwill; a shortfall is credited to Capital Reserve.

Mixed issue (Illustration 10): treat each leg separately — cash issue at 90% (Dr. Discount on Issue with the 10%), issue to vendor for fixed assets, and issue to bank as collateral for a loan (no entry; note under the liability).

Application practise the procedure · 2 questions

- Compute the NUMBER of debentures issued = purchase consideration ÷ issue price per debenture (par, premium or discount) --- e.g. ₹9,90,000 machinery settled by ₹100 debentures at par, at 10% premium (9,000 debentures) or at 10% discount (11,000 debentures).
- On business takeover, record: assets Dr, liabilities Cr, Vendor Cr with purchase consideration; excess of consideration over net assets = Goodwill, shortfall = Capital Reserve (e.g. assets ₹9,00,000, liabilities ₹1,20,000, consideration ₹8,80,000 → Goodwill ₹1,00,000).
- Practise mixed issues in one question: debentures to vendor, for cash at 90%, and to bank as collateral --- treat each leg separately.

PQ 8.1 · PYQ 2020-Nov [6] (b) · Practical · 5M · Pg 745 asked 8×

LEVEL II
Application

Medium

PQ 8.2 · RTP 2025-Jan [17] · Practical · --- · Pg 746 asked 4×

LEVEL II
Application

Medium

Topic 9: Treatment of Discount/Loss on Issue of Debentures

P1-C11-U11.3-T09

Read first Read para 3.9: discount/loss on issue is a capital loss amortised over the life of the debentures --- straight-line if redeemed at the end of a fixed period, or in the ratio of debentures outstanding when redeemed in instalments.

NOTES

Rule: discount/loss on issue is a capital loss amortised over the period between issue and redemption (normally 3–5 years, never beyond debenture tenure); annual write-off entry — Dr. Profit and Loss A/c / Cr. Discount (or Loss) on Issue of Debentures A/c; the unwritten-off balance is shown as Non-current/Current asset depending on the write-off period.

Fixed-period redemption (straight line): write off the total discount equally each year — e.g. 1,00,000 debentures × ₹6 discount = ₹6,00,000 over 5 years = ₹1,20,000 p.a.

Redemption by annual drawings: write off in the ratio of debentures outstanding each year — 1/5th redeemed annually gives 5:4:3:2:1, so ₹1,20,000 splits ₹40,000, ₹32,000, ₹24,000, ₹16,000, ₹8,000.

Discount and redeemable at premium: record total Loss on Issue = discount + premium payable on redemption at allotment, crediting Premium on Redemption of Debentures A/c — e.g. ₹10,00,000 at 10% discount redeemable at 5% premium: loss ₹1,50,000, written off ₹30,000 p.a.

over 5 years.

Application practise the procedure · 3 questions

- Fixed-period redemption: write off total discount equally, e.g. $\text{₹}0.60 \times 1,00,000 = \text{₹}60,000$ over 5 years = $\text{₹}12,000$ p.a. (P&L Dr To Discount on Issue of Debentures).
- Redemption by annual drawings: write off in the outstanding-amount ratio (5:4:3:2:1 pattern for equal annual redemptions).
- When issue is at discount AND redeemable at premium, record total Loss on Issue = discount + redemption premium at the time of allotment, crediting Premium on Redemption of Debentures A/c.
- Show unwritten-off balance as Non-current/Current asset split by the write-off period; remember interest entries alongside if the question spans a year.

PQ 9.1 · PYQ 2018-Nov [6] (b) · Practical · 5M · Pg 748 asked 5x	LEVEL II Application	Easy
PQ 9.2 · MTP 2022-Nov S1 [6] (b) · Practical · 5M · Pg 748 asked 2x	LEVEL II Application	Medium
PQ 9.3 · RTP 2025-Sep [15] · Practical · --- · Pg 749	LEVEL II Application	Medium

Topic 10: Interest on Debentures

P1-C11-U11.3-T10

Read first Study para 3.10: interest at coupon rate on nominal value is a charge against profits, payable irrespective of profits, with TDS deducted at source; entries for interest due, payment net of TDS, deposit of TDS and transfer to P&L.

NOTES

Nature: interest at the coupon rate on the NOMINAL value is a CHARGE against profits — payable whether or not there are profits, and debentures rank ahead of all shares, so interest is paid before both preference and equity dividend; dividend, by contrast, is an appropriation of profit and not tax-deductible.

TDS: the company pays interest net of tax deducted at source per the Income-tax Act, 1961 and deposits the TDS with the income-tax authorities.

Entry set: (1) interest due — Dr. Interest A/c / Cr. Debenture holders' A/c; (2) payment — Dr. Debenture holders' / Cr. TDS Payable + Cr. Bank; (3) deposit — Dr. TDS Payable / Cr. Bank; (4) year end — Dr. Profit and Loss / Cr. Interest A/c.

Computation (Illustration 13): half-yearly interest = nominal value $\times$ coupon $\times 6 \div 12$ — 12% on $\text{₹}10,00,000 = \text{₹}60,000$ each 30 June and 31 December; TDS at 10% = $\text{₹}6,000$, holders receive $\text{₹}54,000$; pair with the annual write-off of discount/loss on issue ($\text{₹}1,50,000 \times 1/5 = \text{₹}30,000$ to

P&L).

Understanding explain with reasons · 2 questions

- Debenture interest is a CHARGE payable whether or not there are profits --- losses do not excuse payment; it ranks BEFORE both preference and equity dividend, so 'payable after preference dividend' is False.
- Contrast interest (tax-deductible charge on nominal value) with dividend (appropriation of profit) to justify answers with reasons.

TQ 10.1 · MTP 2024-Aug [1] (a) (vi) {C} · True/False · 2M · Pg 752 **asked 5x** **LEVEL I** Understanding **Easy**

TQ 10.2 · RTP 2025-Jan [1] (x) · True/False · --- · Pg 752 **asked 3x** **LEVEL I** Understanding **Easy**

Application practise the procedure · 1 question

- Practise the entry set: Interest A/c Dr To Debenture holders; Debenture holders Dr To TDS Payable and Bank; TDS Payable Dr To Bank; year-end P&L Dr To Interest.
- Compute half-yearly interest on nominal value (e.g. 10% on ₹20,00,000 = ₹1,00,000 each 30 June and 31 Dec) with TDS at 10%, and pair it with annual write-off of discount on issue.

PQ 10.1 · PYQ 2019-Jun [6] (b) · Practical · 5M · Pg 753 **asked 6x** **LEVEL II** Application **Medium**

Unit 11.4: Accounting for Bonus Issue and Rights Issue

P1-C11-U11.4 · Importance D · Rank 4 in chapter · Category C · 12.2% of chapter questions · 9 questions

Topic 1: Issue of Bonus Shares

P1-C11-U11.4-T01

Read first Study Section 63 of the Companies Act, 2013 (sources and conditions for bonus issue), the journal entries for fully paid bonus shares and for making partly paid shares fully paid, and the preparation of post-bonus Balance Sheet extracts with Notes on Share Capital and Reserves and Surplus.

NOTES

Bonus issue (SM): “an issue of additional shares to existing shareholders free of cost in proportion to their existing holding” — also called capitalisation of profits / scrip issue; no new funds raised, net worth unchanged, effects: share capital up, EPS and per-share values down, accumulated

profits down, market takes it favourably and price adjusts.

Sec 63 sources & conditions: fully paid bonus shares only out of (i) free reserves, (ii) securities premium, (iii) capital redemption reserve — never out of revaluation reserve; conditions: authorised by articles, general-meeting approval on Board recommendation, no default in interest/principal on deposits or debt securities or in employees' statutory dues (PF, gratuity, bonus), partly paid shares made fully paid first, not in lieu of dividend, and once announced the Board cannot withdraw it.

Pro-forma entries (fully paid bonus): (1) Dr. Capital Redemption Reserve / Securities Premium / General Reserve / P&L → Cr. Bonus to Shareholders; (2) Dr. Bonus to Shareholders → Cr. Equity Share Capital; for “minimum reduction in free reserves” exhaust CRR and Securities Premium (collected in cash) first, then General Reserve, with P&L as balancing figure.

Partly paid shares: securities premium and CRR may be applied only for fully paid bonus shares — only free reserves can pay up unpaid amounts on existing shares; entries: Dr. General Reserve / P&L → Cr. Bonus to Shareholders; Dr. Share Final Call → Cr. Share Capital; Dr. Bonus to Shareholders → Cr. Share Final Call; where the final call is received in cash (Dr. Bank → Cr. Final Call), bonus is then computed on the fully paid shares (e.g. 1 for 4).

Balance Sheet extract: in Notes show each reserve “Less: Utilised for bonus issue” and disclose within issued capital the shares issued by way of bonus; ensure authorised capital is not less than post-bonus issued capital — else pass a general-meeting resolution to increase it, and file return of bonus issue with copy of resolution with the ROC.

Understanding explain with reasons · 1 question

TQ 1.1 · PYQ 2026-Sep [1] (a) (vi) · True/False · 2M · Pg 758

LEVEL I
Understanding

Easy

Application practise the procedure · 6 questions

- Practise the two-step entries: Dr. CRR / Securities Premium / General Reserve / P&L → Cr. Bonus to Shareholders; then Dr. Bonus to Shareholders → Cr. Equity Share Capital.
- Follow the priority order for 'minimum reduction in free reserves': use CRR and Securities Premium (collected in cash) first, then General Reserve, with P&L as balancing figure; never touch Revaluation Reserve.
- Where shares are partly paid (₹7.50 or ₹8 paid-up, or calls-in-arrear), first pass the final-call entries (Share Final Call Dr. to Share Capital; Bank Dr. to Final Call) --- bonus is computed only on fully paid shares; note CRR/Securities Premium cannot be used to pay up partly paid shares (only free reserves can).
- Practise computing bonus shares from the ratio (e.g. 1 for 4), checking/increasing authorised capital when issued capital after bonus exceeds it, and drafting the Balance Sheet extract showing reserves 'Less: Utilised for bonus issue'.

PQ 1.1 · PYQ 2024-Jun [5] (c) · Practical · 10M · Pg 759 asked 8×	LEVEL II Application	Medium
PQ 1.2 · MTP 2024-Jul [5] (c) · Practical · 10M · Pg 761 asked 3×	LEVEL II Application	Medium
PQ 1.3 · MTP 2024-Aug [5] (b) · Practical · 10M · Pg 763	LEVEL II Application	Medium
PQ 1.4 · MTP 2024-Dec S1 [5] (c) · Practical · 10M · Pg 766 asked 5×	LEVEL II Application	Medium
PQ 1.5 · RTP 2026-May [14] (b) PQ · Practical · --- · Pg 768	LEVEL II Application	Medium
PQ 1.6 · PYQ 2026-May [5] (c) · Practical · 10M · Pg 770	LEVEL II Application	Medium

Topic 2: Right Issue

P1-C11-U11.4-T02

Read first Read Section 62(1)(a) provisions on rights offers, advantages and disadvantages of a right issue, accounting for rights shares (same as ordinary issue, with securities premium), and the cum-right/ex-right value and value-of-right formulas.

NOTES

Sec 62(1)(a) right of first refusal: further shares must first be offered to existing equity shareholders in proportion to their holdings; offer by notice stating the number of shares, open not less than 15 and not more than 30 days (if not accepted, deemed declined); notice must state the deemed right of renunciation in favour of any other person (unless articles otherwise provide); after expiry or earlier decline, the Board may dispose of the shares in a manner not disadvantageous to shareholders and the company.

Exceptions (Sec 62): shares need not be offered to existing holders when issued (1) to employees under ESOP, (2) to any persons for cash/other consideration at a registered valuer's price (special resolution), (3) on exercise of a conversion option attached to debentures/loans approved by special resolution, (4) on Government-directed conversion of debentures/loans in public interest.

Five advantages: (1) maintains proportional holding and financial-governance rights (deterrent to management issuing shares to known persons); (2) dilution does not hurt existing holders — discounted price or renunciation preserves cum-right value; (3) natural hedge against public-issue expenses; (4) image enhancement; (5) better chance of success and logistically easier than public issue. **Two disadvantages:** invariable dilution in market value of the share; the attractive price must be objectively assessed against true worth.

Formulas: Ex-right value = $[\text{Cum-right value of existing shares} + (\text{Rights shares} \times \text{Issue price})] \div (\text{Existing shares} + \text{Rights shares})$; Value of right = Cum-right value – Ex-right value; e.g. 1-for-4 at ₹125 when cum-right price is ₹150: ex-right = $(150 \times 4 + 125 \times 1) \div 5 = ₹145$, value of right = ₹5 per share.

Accounting: same as ordinary issue — Dr. Bank → Cr. Equity Share Capital, and Cr. Securities Premium for excess of issue price over face value (e.g. 10,000 rights shares of ₹10 at ₹31: Bank Dr. 3,10,000; Share Capital 1,00,000; Securities Premium 2,10,000).

Remembering memorise · 1 question

- Memorise the 5 advantages of right issue: maintains proportional holding and governance rights; cum-right value protected via discounted price or renunciation; natural hedge against issue expenses; image enhancement; better success chance and easier logistics than public issue.
- Memorise the 2 disadvantages: invariable dilution in market value of the share; attractive price must be objectively assessed against true worth.
- Recall offer terms under Sec 62(1)(a): notice open 15--30 days, deemed right of renunciation (unless articles prohibit), Board may dispose of declined shares.

TQ 2.1 · RTP 2025-May [18] (v) · Short Note · --- · Pg 773

LEVEL I
Remembering

Easy

Application practise the procedure · 1 question

- Practise: Ex-right value = $(\text{Cum-right value of existing shares} + \text{Rights shares} \times \text{Issue price}) / (\text{Existing shares} + \text{Right shares})$; Value of right = Cum-right value – Ex-right value.
- Work problems that start from equity capital in ₹ lakh and market price per share (e.g. capital ₹40 lakh, market value ₹45) --- derive number of shares, apply the offer ratio, then compute ex-right price and value of right.
- Practise the journal entry on subscription: Bank Dr. → To Equity Share Capital and To Securities Premium (excess of issue price over face value), including questions combining final call, bonus and then rights issue.

PQ 2.1 · PYQ 2025-May [5] (c) · Practical · 10M · Pg 774

LEVEL II
Application

Medium

Unit 11.5: Redemption of Preference Shares

P1-C11-U11.5 · Importance D · Rank 3 in chapter · Category A · 18.9% of chapter questions · 14 questions

Topic 1: Introduction

P1-C11-U11.5-T01

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §5.1: meaning of redemption and the redemption date of preference shares.

NOTES

Redemption: the process of repaying an obligation at prearranged amounts and timings — a contract specifying the obligation to redeem preference shares within or at the end of a given period at an agreed price; the redemption (maturity) date is usually printed on the preference share certificate.

Use: through redemption a company can adjust its financial structure, e.g. eliminating preference shares and replacing them with other securities where future growth makes the change advantageous.

Topic 2: Purpose of Issuing Redeemable Preference Shares

P1-C11-U11.5-T02

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §5.2 listing the four reasons for issuing redeemable preference shares.

NOTES

Purposes: (1) a proper way of raising finance in a dull primary market; (2) investors hesitant to buy unlisted, hard-to-sell shares are encouraged if the shares are redeemable by the company; (3) shares may be redeemed when there is a surplus of capital that cannot be profitably used in the business; (4) no dividend is payable in case of loss or no profit — preference dividend is an appropriation of profits, unlike interest on debentures/loans which is a charge against profits payable even in loss.

Topic 3: Provisions of the Companies Act (Section 55)

P1-C11-U11.5-T03

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §5.3: conditions of Section 55 of the Companies Act, 2013 including the Capital Redemption Reserve requirement.

NOTES

Issue: a company limited by shares, if authorised by its Articles, may issue preference shares redeemable at its option within a period normally not exceeding 20 years from issue — irredeemable preference shares cannot be issued.

Conditions: (a) redemption only out of divisible/distributable profits or out of proceeds of a fresh issue of shares made for the purpose; (b) only fully paid shares can be redeemed; (c) premium on redemption to be provided out of profits (for prescribed AS-compliant companies), or out of profits or securities premium account (other companies and pre-Act issues).

CRR: where shares are redeemed out of profits, a sum equal to the nominal amount of shares redeemed (less proceeds of any fresh issue) is transferred from divisible profits to Capital Redemption Reserve Account — treated as paid-up capital for reduction provisions and usable only for issuing fully paid-up bonus shares; the object is that security of creditors is not reduced.

Topic 4: Methods of Redemption of Fully Paid-Up Shares

P1-C11-U11.5-T04

Read first Study Section 55 conditions, the three methods (fresh issue, capitalisation of profits, combination), pros/cons of redemption by fresh equity issue, the journal entries, and minimum fresh issue workings (paras 5.4.1–5.4.5).

NOTES

Sec 55 conditions: preference shares (redeemable normally within 20 years) can be redeemed only out of divisible/distributable profits or out of proceeds of a fresh issue of SHARES made for the purpose (debenture proceeds cannot be used); only fully paid shares can be redeemed; premium on redemption is provided out of profits (companies complying with AS under Sec 133 cannot use securities premium for it); where redeemed out of profits, transfer a sum equal to nominal value redeemed from divisible profits to Capital Redemption Reserve — CRR usable only for fully paid bonus shares; the “gap” is filled by (a) fresh issue, (b) capitalisation of profits, or (c) combination.

Why fresh equity + pros/cons: issued when capital is needed permanently (preference carries fixed dividend), divisible profits are insufficient, or liquidity is poor; advantages: no cash outflow — now or later, new shares may be valued at a premium, shareholders retain equity interest; disadvantages: dilution of future earnings, changed shareholding if issued to outsiders (mitigated by rights issue). “Proceeds” = amount credited to Share Capital — premium on the fresh issue is received in cash but is NOT proceeds for redemption/CRR purposes.

Pro-forma entries: Dr. Bank → Cr. Share Capital (+ Cr. Securities Premium if at premium); Dr. Redeemable Pref. Share Capital + Dr. Premium on Redemption of Pref. Shares → Cr. Preference Shareholders; Dr. Preference Shareholders → Cr. Bank; Dr. P&L → Cr. Premium on Redemption; Dr. P&L / General Reserve → Cr. CRR with (face value redeemed – proceeds of fresh issue).

Minimum fresh issue (4 steps): (1) maximum reserves available = balances less any stipulated minimum to be retained; (2) minimum proceeds = nominal value of preference shares – maximum reserves available (after adjusting premium on redemption payable out of profits); (3) minimum number of shares = minimum proceeds ÷ face value of one share; (4) round fractions UP (and up to

the next multiple of 50/100 if the question so requires). E.g. redeem ₹5,00,000 with profits ₹3,00,000, ₹9 shares $\rightarrow 2,00,000 \div 9 = 22,222.22 \rightarrow 22,223$ shares (22,250 in multiples of 50).

Fresh issue to provide funds: compare amount payable to preference shareholders (face value + premium) with funds available — sale proceeds of investments (profit/loss on sale to P&L) and bank balance above the minimum to be retained — and divide the shortfall by the ISSUE price of one share; e.g. payable ₹71,500 – investments ₹15,000 – available bank ₹19,000 = ₹37,500 $\div$ ₹50 = 750 shares, then CRR = 65,000 – 37,500 = ₹27,500.

Understanding explain with reasons · 2 questions

- Explain why equity shares are issued for redemption (permanent capital need, insufficient profits, poor liquidity), plus advantages (no cash outflow, premium possible, equity retained) vs disadvantages (earnings dilution, changed shareholding unless rights issue).
- True/False trap: only proceeds of a fresh issue of SHARES can fund redemption --- debenture proceeds cannot; 'proceeds' also exclude securities premium on the fresh issue.

TQ 4.2 · PYQ 2025-Jan [1] (a) (iv) {C} · True/False · 2M · Pg 780

LEVEL I
Understanding

Easy

TQ 4.1 · PYQ 2018-Nov [6] (d) · Descriptive · 5M · Pg 779

LEVEL I
Understanding

Medium

Application practise the procedure · 4 questions

- Practise the entry sequence: fresh issue; Pref. Share Capital + Premium on Redemption Dr. $\rightarrow$ Pref. Shareholders; payment; CRR = face value redeemed – fresh-issue proceeds; premium on redemption written off against P&L (not securities premium).
- Minimum fresh issue: proceeds = nominal value – reserves available (after retention conditions and premium on redemption); shares = proceeds $\div$ face value, rounded up.
- Redeem only fully paid shares --- receive the final call on calls-in-arrear first; count only divisible profits.

PQ 4.4 · PYQ 2022-Nov [6] (c) · Practical · 5M · Pg 791 asked 2×

LEVEL II
Application

Medium

PQ 4.7 · RTP 2025-May [17] · Practical · --- · Pg 800

LEVEL II
Application

Medium

PQ 4.8 · PYQ 2025-Sep [5] (c) · Practical · 10M · Pg 802

LEVEL II
Application

Medium

PQ 4.10 · PYQ 2026-Sep [6] (a) · Practical · 15M · Pg 807

LEVEL II
Application

Hard

Analysis work through mixed data · 6 questions

- Work full Balance-Sheet questions combining sale of investments (profit/loss), a minimum bank balance to retain, minimum fresh issue, CRR and payment --- then the post-redemption Balance Sheet.

- Watch: fresh-issue premium is cash but not 'proceeds' for CRR; retained minimums cut available reserves.
- Practise 15--20 mark problems where redemption is followed by a bonus issue out of CRR, or partly paid preference shares need the final call (or are left intact).

PQ 4.1 · PYQ 2019-May [5] (a) · Practical · 10M · Pg 780	LEVEL II Analysis	Hard
PQ 4.2 · PYQ 2021-Dec [4] · Practical · 20M · Pg 783	LEVEL II Analysis	Hard
PQ 4.3 · PYQ 2022-May [5] (a) · Practical · 10M · Pg 788	LEVEL II Analysis	Hard
PQ 4.5 · PYQ 2024-Jun [6] (a) · Practical · 15M · Pg 794 asked 4×	LEVEL II Analysis	Hard
PQ 4.6 · RTP 2025-Jan [16] · Practical · ---- · Pg 797	LEVEL II Analysis	Hard
PQ 4.9 · PYQ 2026-Jan [6] (a) · Practical · 15M · Pg 804 asked 2×	LEVEL II Analysis	Hard

Topic 5: Redemption of Preference Shares by Capitalisation of Undistributed Profits

P1-C11-U11.5-T05

Read first Study para 5.5: redemption wholly/partly out of divisible profits, transfer equal to nominal value redeemed to Capital Redemption Reserve, which profits are divisible, and the advantages/disadvantages of this method.

NOTES

Rule (SM): when shares are redeemed otherwise than out of a fresh issue, “there shall out of profits which would otherwise have been available for dividend ... be transferred to a reserve to be called the Capital Redemption Reserve Account a sum equal to the nominal amount of the shares redeemed”; divisible profit = profit legally distributable as dividend (General Reserve, P&L, free portion of Investment Allowance Reserve) — securities premium and capital reserve are non-divisible and cannot be used for CRR; transfer to CRR makes the profits non-divisible, so creditors' security is not reduced.

Entries: Dr. General Reserve / P&L / other divisible profits → Cr. CRR; Dr. Redeemable Pref. Share Capital (+ Dr. Premium on Redemption) → Cr. Preference Shareholders; Dr. Preference Shareholders → Cr. Bank; Dr. P&L (divisible profit) → Cr. Premium on Redemption of Preference Shares.

Pros/cons: advantages — no change in percentage of equity shareholding, surplus funds can be used; disadvantage — reduction in liquidity, investments may need to be sold (sale proceeds provide cash; profit/loss on sale goes to P&L).

Combination method — formula: CRR to be created = Face value of shares redeemed – Proceeds from new issue; equivalently, proceeds needed from new issue = Face value redeemed – Profits available for distribution; present the CRR working and number of shares as working notes — e.g. redeem ₹1,00,000 at 10% premium: available profits GR (80,000–20,000 retained) 60,000 + P&L (20,000–10,000 for premium) 10,000 + free IAR 5,000 = ₹75,000, so fresh issue ₹25,000 = 2,500 shares of ₹10; check the bank trail after fresh issue, investment sale and payment.

Analysis work through mixed data · 2 questions

- Work combined problems: part redemption from fresh issue, balance from profits --- CRR = face value redeemed – proceeds of fresh issue; use only divisible profits (General Reserve, P&L, free portion of Investment Allowance Reserve; not securities premium or capital reserve).
- Handle multi-element data: two classes of preference shares (redeem the fully paid class, or call up the balance first), premium on redemption charged to P&L, and sale of investments to raise cash.
- Check the cash trail: bank balance after fresh issue, investment sale and payment; retain any stipulated minimum reserve/bank balance when deciding amounts capitalised.
- Present journal entries plus working notes for the CRR amount and number of shares issued --- the CRR working carries marks.

PQ 5.1 · PYQ 2021-Jan [5] (a) · Practical · 12M · Pg 809

LEVEL II
Analysis

Hard

PQ 5.2 · MTP 2025-Jan S2 [5] (c) · Practical · 10M · Pg 811 **asked 3x**

LEVEL II
Analysis

Hard

Topic 6: Redemption of Partly Called-Up Preference Shares

P1-C11-U11.5-T06

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §5.6 with Illustration 9: assumptions where preference shares are partly called up.

NOTES

Rules: only fully paid-up preference shares can be redeemed — (1) if partly called-up shares are to be redeemed, assume the final call is demanded and received before redemption; (2) if both fully paid and partly paid shares exist, presume only fully paid shares are redeemed and partly paid left intact; (3) if call money is not received despite reminders, the company can forfeit the shares.

Topic 7: Redemption of Fully Called but Partly Paid-Up Preference Shares

P1-C11-U11.5-T07

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §5.7 with Illustration 10: treatment of calls-in-arrears received vs forfeiture before redemption.

NOTES

Arrears received: “Dr. Bank A/c / Cr. Calls-in-Arrears A/c” — shares become fully paid and redemption proceeds in the normal course.

Forfeiture: if calls remain unpaid despite proper notice, the Board may forfeit and cancel the shares — “Dr. Preference Share Capital A/c (called-up amount) / Cr. Calls-in-Arrears A/c and Cr. Shares Forfeited A/c (amount actually collected)”; shares to be redeemed reduce by the shares forfeited, and as forfeited shares are not reissued the Shares Forfeited balance goes to capital reserve — “Dr. Shares Forfeited A/c / Cr. Capital Reserve A/c”.

Unit 11.6: Redemption of Debentures

P1-C11-U11.6 • Importance D • Rank 5 in chapter • Category C • 8.1% of chapter questions • 6 questions

Topic 1: Introduction

P1-C11-U11.6-T01

CONCEPT BASE — no exam question asked yet • essential for full preparation

Read first Read §6.1: definition of debenture and the Section 71 provisions on convertible debentures, voting rights and DRR.

NOTES

Debenture: an instrument issued by a company under its seal, acknowledging a debt and containing provisions as regards repayment of principal and interest; a charge on assets, if created, is described therein and is not valid unless registered with the Registrar; trusteeship is customarily created for mortgage debentures to safeguard holders' interests.

Section 71: (1) debentures may be issued with an option to convert into shares wholly or partly at redemption — requires a special resolution at a general meeting; (2) no company can issue debentures carrying voting rights; (4) a debenture redemption reserve must be created out of

profits available for dividend, usable only for redemption of debentures.

Topic 2: Redemption of Debentures

P1-C11-U11.6-T02

CONCEPT BASE — no exam question asked yet · essential for full preparation

Read first Read §6.2: modes in which redeemable debentures may be redeemed.

NOTES

Modes: debentures are usually redeemable — in cash or convertible into equity shares after a period; redemption may be (i) after a fixed number of years, (ii) any time after a certain number of years since issue, (iii) on giving a specified notice, or (iv) by annual drawings; a company may also purchase its own debentures in the open market — profitable to purchase and cancel them when quoted at a discount on the stock exchange.

Topic 3: Debenture Redemption Reserve

P1-C11-U11.6-T03

Read first Read §6.3 including Rule 18(7) adequacy table: purpose, entries and DRR requirements by class of company.

NOTES

Purpose and entries: DRR is created out of profits available for dividend every year until debentures are redeemed and cannot be used for any other purpose — ensures liquid funds at redemption; entry: Dr. Profit and Loss A/c / Cr. Debenture Redemption Reserve; simultaneously invest outside — Dr. DRR Investment / Cr. Bank; investments are encashed at redemption; on default the Tribunal may order the company to redeem forthwith with principal and interest.

Adequacy — Rule 18(7): no DRR required for AIFs regulated by RBI and banking companies, all listed companies (including listed NBFCs/HFCs), and unlisted NBFCs/HFCs for privately placed debentures; other unlisted companies — DRR of 10% of the value of outstanding debentures issued.

Understanding explain with reasons · 1 question

TQ 3.1 · PYQ 2026-Sep [1] (a) (iv) {C} · True/False · 2M · Pg 818

LEVEL I
Understanding

Easy

Topic 4: Methods of Redemption of Debentures

P1-C11-U11.6-T04

Read first Study Section 71, the methods of redemption (lump sum, instalments, open-market purchase, conversion into shares), DRR adequacy (10% for other unlisted companies; nil for AIFI/banks/listed/NBFC/HFC), the 15% Debenture Redemption Investment rule, and related journal entries and ledger accounts (paras 6.3--6.4).

NOTES

Sec 71: debentures may be issued with an option to convert into shares wholly/partly at redemption (special resolution needed); no debenture can carry voting rights; DRR must be created out of profits available for payment of dividend and used for no purpose other than redemption; interest and redemption must follow the terms of issue — on default the Tribunal may, on application of debenture holders/trustee, order immediate redemption with interest.

Four methods: payment in lump sum at/before maturity; payment in instalments at specified intervals; purchase in open market (excluded at Foundation level); conversion into shares.

DRR adequacy (Rule 18(7), 2019): DRR = 10% of the value of outstanding debentures for 'other unlisted companies'; NO DRR required for AIFIs and banking companies, all listed companies (including listed NBFCs/HFCs), and unlisted NBFCs/HFCs for privately placed debentures; for partly convertible debentures DRR is created only on the non-convertible portion.

15% DRI rule: on or before 30th April each year, deposit/invest not less than 15% of debentures maturing during the year ending 31st March next, in scheduled-bank deposits free of charge/lien, unencumbered Central/State Government securities, or specified Indian Trusts Act securities/bonds; the amount is usable only for redemption of those debentures and must not at any time fall below 15%; in problems, make the DRR appropriation and DRI investment immediately on allotment (or on day 1 of the year if no date is given).

Cycle of entries: Dr. P&L → Cr. DRR (10% of outstanding debentures, net of existing DRR balance); Dr. DRR Investment → Cr. Bank (15%); Dr. Bank → Cr. Interest on DRR Investment (transferred to P&L); at redemption: Dr. Bank → Cr. DRR Investment (encashment); Dr. Debentures + Dr. Premium on Redemption → Cr. Debentureholders; Dr. Debentureholders → Cr. Bank; Dr. P&L → Cr. Premium on Redemption (charged fully in the year of redemption when the debenture term is not given); finally Dr. DRR → Cr. General Reserve.

Conversion & ledgers: equity shares issued = redemption value of converted debentures (face value + premium) ÷ issue price of one equity share, balance paid in cash — e.g. 40 debentures at ₹105 = ₹4,200 ÷ ₹20 = 210 shares; in ledger/mid-year questions apportion debenture interest and DRI interest up to the redemption date (e.g. Debenture Interest = 10,00,000 × 6% × 2/12; DRI interest = 1,50,000 × 4% × 2/12) before striking the final Bank balance, and draft the Debentures, Premium on Redemption, DRR, DRR Investment, Interest and Bank accounts year-wise.

Application practise the procedure · 4 questions

- Practise the DRR/DRI cycle: P&L Dr. → DRR (10% of outstanding debentures, net of existing balance); DRI Dr. → Bank (15% of debentures maturing); on redemption encash DRI, pay holders (premium on redemption to P&L), then transfer DRR to General Reserve.
- For own-debenture cancellation, distinguish cum-interest/ex-interest prices, account for accrued interest since the last interest date, and transfer profit on cancellation (nominal value – cost) to capital reserve.
- For partly convertible debentures, convert at redemption value (face + premium) ÷ issue price of equity share; pay the rest in cash; DRR only on the non-convertible portion.
- Practise redemption in equal annual instalments of debentures issued at discount, redeemable at premium --- draft the Debentures, DRR, DRI, Interest and Bank accounts year-wise.

PQ 4.1 · PYQ 2018-May [6] (c) · Practical · 5M · Pg 819	LEVEL II Application	Medium
PQ 4.5 · PYQ 2025-Jan [5] (c) · Practical · 5M · Pg 828 asked 8×	LEVEL II Application	Medium
PQ 4.3 · PYQ 2022-Nov [5] (a) · Practical · 12M · Pg 822 asked 2×	LEVEL II Application	Hard
PQ 4.4 · PYQ 2024-Sep [5] (c) · Practical · 10M · Pg 824	LEVEL II Application	Hard

Analysis work through mixed data · 1 question

- Work multi-date problems: apportion debenture interest and DRI interest up to a mid-year redemption date before striking the final Bank balance.
- Analyse option-based redemptions (par at maturity vs open-market purchase vs ₹102 after notice): compare costs and compute profit/loss on cancellation.
- Watch: DRR only out of profits available for dividend; DRI usable only for redemption; premium on redemption fully charged to P&L when the term is not given.

PQ 4.2 · PYQ 2018-Nov [5] (b) · Practical · 8M · Pg 821	LEVEL II Analysis	Hard
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