

ACCOUNTING FOR BRANCHES INCLUDING FOREIGN BRANCHES

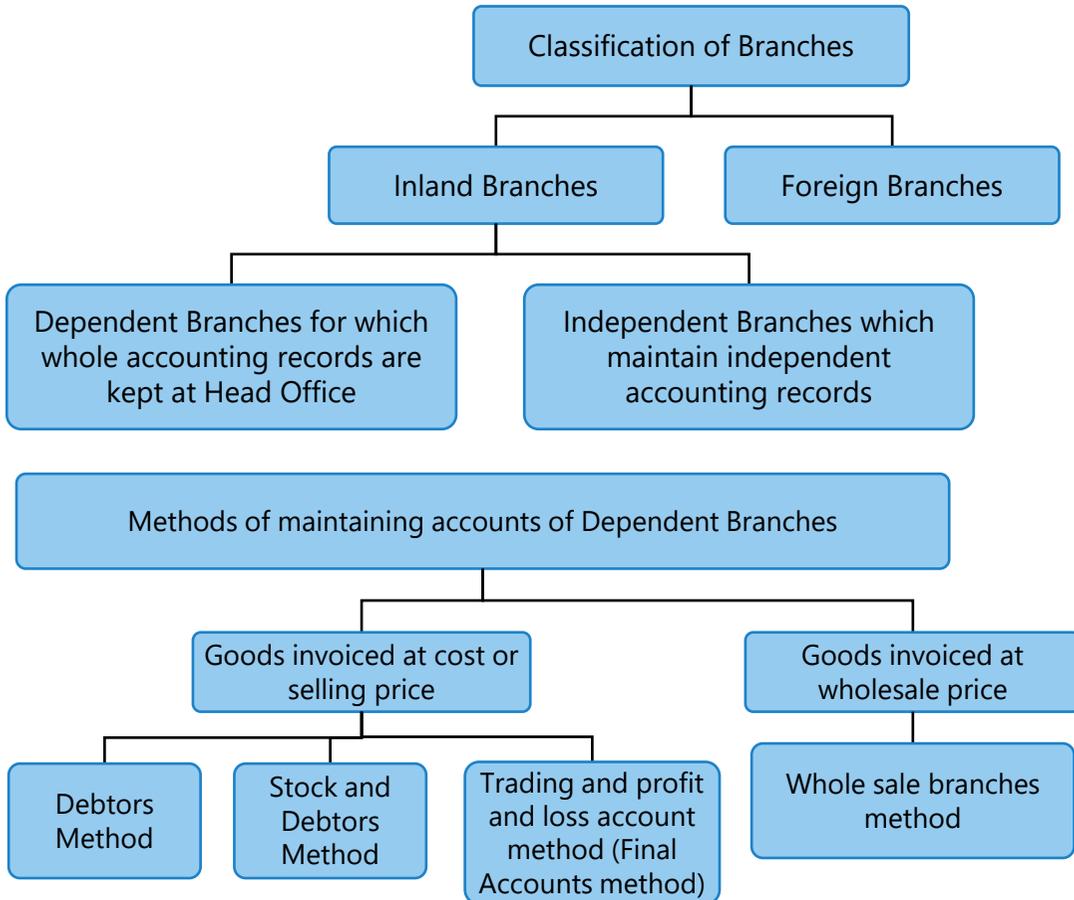


LEARNING OUTCOMES

After studying this chapter, you will be able to–

- ◆ Understand concept of branches and their classification from accounting point of view.
- ◆ Distinguish between the accounting treatment of dependent branches and independent branches.
- ◆ Learn various methods of charging goods to branches.
- ◆ Solve the problems, when goods are sent to branch at wholesale price.
- ◆ Prepare the reconciliation statement of branch and head office transactions after finding the reasons for their disagreement.
- ◆ Incorporate branch balances in the head office books.
- ◆ Differentiate between integral and non-integral foreign branches.
- ◆ Learn the techniques of foreign currency translation in case of foreign branches.

CHAPTER OVERVIEW



1. INTRODUCTION

A branch can be described as any establishment carrying on either the same or substantially the same activity as that carried on by head office of the company. It must also be noted that the concept of a branch means existence of a head office; for there can be no branch without a head office - the principal place of business. Branch offices are of a great utility in the sense that they allow business to be

expanded closer to the clients and hence they facilitate face to face interaction with customers.

From the accounting point of view, branches may be classified as follows:

- Inland Branches which can be further classified as:
 - (a) Independent Branches which maintain independent accounting records
 - (b) Dependent Branches for which whole accounting records are kept at Head Office
- Foreign Branches

Difference between branch and department

Branch: Establishment at location different from Head Office to carry either same or substantially same activity as carried on by Head Office

Department: Division of a large organization dealing with a various kind of activity at the same location.

Let’s take an example of a CA Firm working in the field of Auditing, Taxation and Finance having office at Mumbai, Chennai and Delhi practicing such fields. The CA firm has various branches in different cities, i.e., Mumbai, Chennai and Delhi, also it has various department of Auditing, Taxation and Finance at one particular branch (location).



2. DISTINCTION BETWEEN BRANCH ACCOUNTS AND DEPARTMENTAL ACCOUNTS

Basis of distinction	Branch Accounts	Departmental Accounts
1. Maintenance of accounts	Branch accounts may be maintained either at branch or at head office.	Departmental accounts are maintained at one place only.

2. Apportionment of common expenses	As expenses in respect of each branch can be identified, so the apportionment problem never arises.	Common expenses are distributed among the departments concerned on some equitable basis considered suitable in the case.
3. Reconciliation	Reconciliation of head office and branch accounts is necessary in case of Branches maintaining independent accounting records at the end of the accounting year.	Such problem never arises.
4. Conversion of foreign currency figures	At the time of finalization of accounts, conversion of figures of foreign branch is necessary.	Such problem never arises.



3. DEPENDENT BRANCHES

When the business policies and the administration of a branch are wholly controlled by the head office and its accounts also are maintained by it, the branch is described as Dependent branch. Branch accounts, in such a case, are maintained at the head office out of reports and returns received from the branch. Some of the significant types of branches that are operated in this manner are described below:

- (a) A branch set up merely for booking orders that are executed by the head office. Such a branch only transmits orders to the head office;
- (b) A branch established at a commercial center for the sale of goods supplied by the head office, and under its direction all collections are made by the H.O.; and
- (c) A branch for the retail sale of goods, supplied by the head office.

Accounting in the case of first two types is simple. Only a record of expenses incurred at the branch has to be maintained.

But however, a retail branch is essentially a sale agency that principally sells goods supplied by the head office for cash and, if so authorized, also on credit to approved customers. Generally, cash collected is deposited into a local bank to the credit of the head office and the head office issues cheques or transfers funds thereon for meeting the expenses of the branch. In addition, the Branch Manager is provided with a 'float' for petty expenses which is replenished from time to time on an imprest basis. If, however, the branch also sells certain lines of goods, directly purchased by it, the branch retains a part of the sale proceeds to pay for the goods so purchased.



4. METHODS OF CHARGING GOODS TO BRANCHES

Goods may be invoiced to branches (1) at cost; or (2) at selling price; or (3) in case of retail branches, at wholesale price.

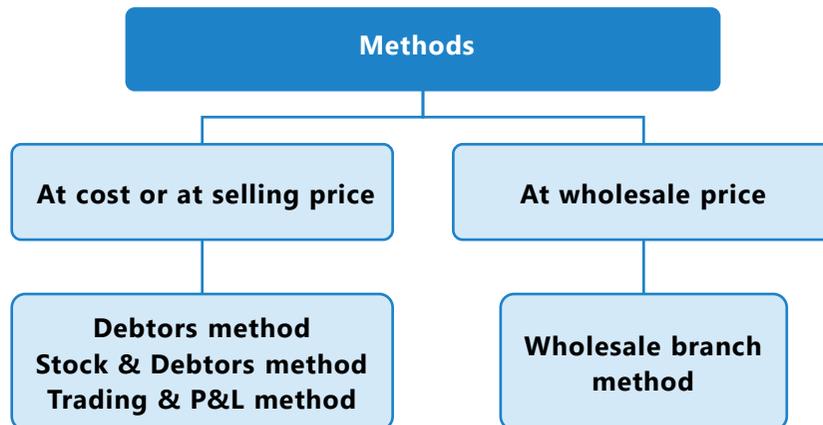
Selling price method is adopted where the goods would be sold at a fixed price by the branch. It is suitable for dealers in tea, petrol, ghee, etc. In this way, greater control can be exercised over the working of a branch in as much as that the branch balance in the head office books would always be composed of the value of unsold stock at the branch and remittances or goods in transit.





5. ACCOUNTING FOR DEPENDENT BRANCHES

Dependent branch does not maintain a complete record of its transactions. The Head office may maintain accounts of dependent branches in any of the following methods:



5.1 When goods are invoiced at cost

If goods are invoiced to the branch at cost, the trading results of branch can be ascertained by following any of the three methods: **(i) Debtors Method, (ii) Stock and Debtors method, (iii) Trading and Profit and Loss Account (Final Accounts) Method.**

For finding out the trading results of branch, it is assumed that the branch is an entity separate from the head office. On this basis, a Branch Account is stated in the head office books to which the price of goods or services provided or expenses paid out are debited and correspondingly, the value of benefits and cash received from the branch are credited.

Debtors method This method of accounting is *suitable for small sized branches*. Under this method, separate branch account is maintained for each branch to compute profit or loss made by each branch. Various accounting adjustments to respective branch account are as follows:

- The opening balance of stock, debtors (if any), petty cash (if any), are debited to the Branch Account; the cost of goods sent to branch as well as any direct purchases made by branch (for which Head Office makes the

payment), expenses of the branch paid by the head office, e.g., salaries, rent, insurance, etc., are also debited to it.

- Conversely, amounts remitted by the branch and the cost of goods returned by the branch are credited.
- At the end of the year, the value of unsold stock, the total of customers' balances outstanding and that of petty cash are brought into the branch account on the credit side.
- Accordingly, the branch account will reveal profit or loss; Debit 'balance' will be the loss suffered by the working of the branch and *vice versa*.

If the branch is allowed to make small purchases of goods locally as well as to incur expenses out of its cash receipts, it will be necessary for the branch to supply to the head office a copy of the Cash Account, showing details of cash collections and disbursements. To illustrate the various entries which are made in the Branch Account, the proforma of a Branch Account is shown below:

Proforma Branch Account

To Balance b/d	By Bank A/c (Cash remitted)
Cash	By Return to H.O.
Stock	
Debtors	By Balance c/d
Petty Cash	Cash
Fixed Assets	Stock
Prepaid Expenses	Debtors
To Goods sent to Branch	Petty Cash
To Bank A/c	Fixed Assets
Salaries	Prepaid Expenses
Rent	
Sundry Expenses	By Profit and Loss A/c—Loss
To Profit & Loss A/c—Profit	(if debit side is larger)
(if credit side is larger)	

Note:

1. Having credited the Branch Account by the actual cash received from debtors, it would be incorrect to debit the Branch Account, in respect of discount or allowances to debtors.
2. The accuracy of the trading results as disclosed by the Branch Account, so maintained, if considered necessary, can be proved by preparing a Memorandum Branch Trading and Profit & Loss Account, in the usual way, from the balances of various items of income and expenses contained in the Branch Account.

Example 1

XP Ltd opened a branch at Delhi and sent goods costing ₹50,000 to Delhi branch. Delhi Branch sold entire goods on credit at ₹ 62,000. No other transaction occurred at the branch. Prepare branch account in Head Office Books and find out the profit.

Solution

We know that branch earned net profit of ₹12,000, now see how same can be find out by branch account.

Branch Account

Particulars	Amount ₹	Particulars	Amount ₹
To Opening branch assets	Nil	By Closing branch assets	
To Goods sent to branch	50,000	Stock Nil	
To Net Profit	12,000	Debtor <u>62,000</u>	62,000
	62,000		62,000

Example 2

XP Ltd opened a new branch at Delhi. XP Ltd sent goods costing ₹ 50,000 to Delhi branch. Delhi branch sold entire goods in cash at ₹ 70,000. Branch paid expenses of ₹ 8,000. No other transaction occurred at the branch. Prepare branch account in HO Books and find out the profit.

Solution

We know that branch earned net profit of ₹12,000 (i.e. Gross Profit ₹ 20,000 less expenses of ₹ 8,000), Let's see how same can be find out by branch account:

Branch Account

Particulars	Amount	Particulars	Amount
To Opening branch assets	Nil	By Closing branch assets	
		Stock	Nil
To Goods sent to branch	50,000	Debtor	Nil
To Net Profit transferred to General P&L A/c	12,000	Cash	<u>62,000</u>
		(70,000 - 8,000)	62,000
	62,000		62,000

Example 3

Prepare branch account and find out profit earned by branch if transactions are as under:

Goods sent to branch	₹ 50,000
Furniture sent to branch	₹ 10,000 (at the beginning of year)
Credit sales at branch	₹ 62,000
Bad Debts	₹ 1,000
Other information:	
Closing stock at branch	₹ 10,000
Closing Debtor	₹ 61,000
Furniture (after depreciation@20%)	₹ 8,000

Solution

Branch Account

Particulars	Amount	Particulars	Amount
To Opening branch assets-			
(Furniture)	10,000	By Closing branch assets-	

To Goods sent to branch	50,000	Stock	10,000	
To Net Profit transferred to General P&L A/c	19,000	Debtor	61,000	
		Furniture	<u>8,000</u>	79,000
	79,000			79,000

Illustration 1 (a)

Buckingham Bros, Bombay have a branch at Nagpur. They send goods at cost to their branch at Nagpur. However, direct purchases are also made by the branch for which payments are made at head office. All the daily collections are transferred from the branch to the head office.

From the following, prepare Nagpur branch account in the books of head office by Debtors method:

	₹		₹
Opening balance (1-1-20X1) Imprest Cash	2,000	Bad Debts	1,000
Sundry Debtors	25,000	Discount to Customers	2,000
Stock: Transferred from H.O.	24,000	Remittances to H.O. (received by H.O.)	1,65,000
Direct Purchases	16,000	Remittances to H.O. (not received by H.O. so far)	5,000
Cash Sales	45,000	Branch Exp. directly paid by H.O.	30,000
Credit Sales	1,30,000	Closing Balance (31-12-20X1)	
Direct Purchases	45,000	Stock: Direct Purchase	10,000
Returns from Customers	3,000	Transfer from H.O.	15,000
Goods sent to branch from H.O.	60,000	Debtors	?
Transfer from H.O. for Petty Cash expenses	4,000	Imprest Cash	?
		Petty Cash expenses	4,000

Solution

**In the Books of Buckingham Bros, Bombay
Nagpur Branch Account**

Particulars	₹	Particulars	₹	₹
To Opening Branch Assets-		By Bank –		
		Remittances received		
		from branch		
Stock (24,000+16,000)	40,000	Cash Sales	45,000	
Debtors	25,000	Cash from Debtors *	1,20,000	
		Cash in transit *	5,000	1,70,000
Imprest Cash	2,000	By Closing Branch		
		Assets		
To Goods sent to Branch A/c	60,000	Stock (15,000		25,000
		+10,000)		
To Creditors (Direct	45,000	Debtors (W.N. 1)		24,000
Purchases)		Imprest Cash (W.N. 2)		2,000
To Bank (Sundry exp.)	30,000			
To Bank (Petty cash exp.)	4,000			
To Net Profit transferred to	15,000			
General Profit & Loss A/c				
	2,21,000			2,21,000

Working Notes:

1. Memorandum Debtors A/c

Particulars	₹	Particulars	₹
To To Bal b/d	25,000	By By Sales Return	3,000
To To Sales	130,000	By By Bad Debts	1,000
		By By Discount	2,000
		By By Cash *	125,000
		By By Bal c/d	24,000
	155,000		155,000

2. Memorandum Petty Cash

Particulars	₹	Particulars	₹
To Bal b/d	2,000	By Expenses (met by Branch)	4,000
To Transfer from H.O.	4,000	By Bal c/d	2,000
	6,000		6,000

* Collection from Debtors = Total Remittances (1,65,000+5,000) – Cash Sales (45,000) = ₹ 1,25,000

Stock and Debtors method

If it is desired to exercise a more detailed control over the working of a branch, the accounts of the branch are maintained under Stock and Debtors Method. According to this method, the following accounts are maintained by the Head Office:

Account	Purpose
1. Branch Stock Account (or Branch Trading Account)	Ascertainment of shortage or surplus
2. Branch Debtors Account	Ascertainment of closing balance of debtors
3. Branch Expenses Account	Ascertainment of total expenses incurred
4. Goods sent to Branch Account	Ascertainment of cost of goods sent to branch
5. Branch Cash / Bank Account	Know about cash flow at branch (eg: where branch is allowed to incur expenses locally)
6. Branch Fixed Asset Account	Control over branch Fixed Assets
7. Branch Profit and Loss Account	Calculation of net profit or loss

The manner in which entries are recorded in the above method is shown below:

	Transaction	Account debited	Account credited
(a)	Cost of goods sent to the Branch	Branch Stock A/c	Goods sent to Branch A/c

(b)	Remittances for expenses	Branch Cash A/c	Cash A/c
(c)	Any asset (e.g. furniture) provided by H.O.	Branch Asset (Furniture) A/c	Asset A/c
(d)	Cost of goods returned by the branch	Goods sent to Branch A/c	Branch Stock A/c
(e)	Cash Sales at the Branch	Branch Cash A/c	Branch Stock A/c
(f)	Credit Sales at the Branch	Branch Debtors A/c	Branch Stock A/c
(g)	Return of goods by debtors to the Branch	Branch Stock A/c	Branch Debtors A/c
(h)	Cash paid by debtors	Branch Cash A/c	Branch Debtors A/c
(i)	Discount & allowance to debtors, bad debts	Branch Expenses A/c	Branch Debtors A/c
(j)	Remittances to H.O.	Cash A/c	Branch Cash A/c
(k)	Branch Expenses directly paid by H.O.	Branch Expenses A/c	Cash A/c
(l)	Expenses met by Branch	Branch Expenses A/c	Branch Cash A/c

(m) *Closing Stock*: Credit the Branch Stock Account with the value of closing stock at cost. It will be carried down as opening balance (debit) for the next accounting period. The Balance of the Branch Stock Account, (after adjustment therein the value of closing stock), if in credit, will represent the gross profit on sales and vice versa.

Other Steps:

(n) Transfer Balance of Branch Stock Account to the Branch Profit and Loss Account.

- (o) Transfer Balance of Branch Expenses Account to the debit of Branch Profit & Loss Account.
- (p) The balance in the Branch P&L A/c will be transferred to the (H.O.) Profit & Loss Account.
- (q) The credit balance in the Goods sent to Branch Account is afterwards transferred to the Head Office Purchase Account or Trading Account (in case of manufacturing concerns), it being the value of goods transferred to the Branch.

Branch Trading and Profit and Loss Account (Final Accounts Method)

In this method, Trading and Profit and Loss accounts are prepared considering each branch as a separate entity. The main advantage of this method is that, it is easy to prepare and understand. It also gives complete information of all transactions which are ignored in the other methods. It should be noted that Branch Trading and Profit and Loss account is merely a memorandum account and therefore, the entries made there in do not have double entry effect.

Illustration 1 (b)

From the information given in the illustration 1(a), prepare Nagpur Branch Trading and Profit and Loss Account in the books of head office.

Solution

Buckingham Bros. Bombay Nagpur Branch-Trading and Profit and Loss Account for the year ending 31st December, 20X1

Particulars	₹	Particulars	₹	₹
To Opening Stock	40,000	By Sales		
To Goods transferred from Head Office	60,000	Cash	45,000	
To Purchases	45,000	Credit sales	1,30,000	
To Gross Profit c/d	52,000		1,75,000	
		Less: Returns	(3,000)	1,72,000
		By Closing Stock		25,000
	1,97,000			1,97,000
To Expenses	30,000	By Gross Profit b/d		52,000
To Discounts	2,000			

To Bad Debts	1,000			
To Petty Cash Expenses	4,000			
To Net Profit transferred to General P&L A/c	15,000			
	52,000			52,000

The students may note that Gross Profit and Net Profit earned by the branch are ascertainable in this method and also evaluating the performance of the branch is very much easier in this method than in the 'Debtors method'.

Solving Illustration by all three methods

Given below is a simple problem, the solution whereto has been prepared in all the three methods so as to show the distinguishing features of these methods.

Illustration 2

The Bombay Traders invoiced goods to its Delhi branch at cost. Head Office paid all the branch expenses from its bank account, except petty cash expenses which were met by the Branch. All the cash collected by the branch was banked on the same day to the credit of the Head Office. The following is a summary of the transactions entered into at the branch during the year ended December 31, 20X1.

	₹		₹
<i>Balances as on 1.1.20X1:</i>			
Stock	7,000	Bad Debts	600
Debtors	12,600	Goods returned by customers	500
Petty Cash,	200	Salaries & Wages	6,200
Goods sent from H.O.	26,000	Rent & Rates	1,200
Goods returned to H.O.	1,000	Sundry Expenses	800
Cash Sales	17,500	Cash received from Sundry Debtors	28,500
Credit Sales	28,400		
Allowances to customers	200	<i>Balances as on 31.12.20X1:</i>	
Discount to customers	1,400	Stock	6,500
		Debtors	9,800
		Petty Cash	100

Prepare: (a) Branch Account (Debtors Method), (b) Branch Stock Account, Branch Profit & Loss Account, Branch Debtors and Branch Expenses Account by adopting the Stock and Debtors Method and (c) Branch Trading and Profit & Loss Account to prove the results as disclosed by the Branch Account.

Solution

(a) Debtors Method

Delhi Branch Account

20X1		₹	₹	20X1		₹	₹
Jan. 1	To Opening branch assets:			Dec 31	24 Bank		
	Stock	7,000			Cash Sales	17,500	
	Debtors	12,600			Cash from sundry Debtors	28,500	46,000
	Petty cash	200	19,800				
Dec. 31	To Goods sent to Branch A/c		26,000		By Goods sent to Branch A/c –		
	To Bank:				Returns to H.O.		1,000
	Salaries & Wages	6,200			By Closing branch assets		
	Rent & Rates	1,200			Stock	6,500	
	Sundry Exp.	800	8,200		Debtors	9,800	
					Petty Cash	100	16,400
	To Net profits/f to General P&L A/c		9,400				
			63,400				63,400
Jan. 1, 20X2	To Balance b/d		16,400				

(b) Stock and Debtors Method

Branch Stock Account

20X1		₹	20X1		₹
Jan. 1	To Balance b/d - Opening Stock	7,000	Dec. 31	By Sales:	
Dec. 31	To Goods Sent to Branch A/c	26,000		Cash	17,500
	To Branch P&L A/c	19,900		Credit	28,400
				Less: Return	(500)
				By Goods sent to Branch A/c - Return	1,000
				By Balance c/d - Closing Stock	6,500
		52,900			52,900
20X2 Jan. 1	To Balance b/d - Opening Stock	6,500			

Delhi Branch Debtors Account

20X1		₹	20X1		₹
Jan. 1	To Balance b/d	12,600	Dec. 31	By Cash	28,500
Dec. 31	To Sales	28,400		By Returns	500
				By Allowances	200
				By Discounts	1,400
				By Bad debts	600
				By Balance c/d	9,800
		41,000			41,000
20X2 Jan. 1	To Balance b/d	9,800			

Delhi Branch Expenses Account

20X1		₹	20X1		₹
Dec. 31	To Salaries & Wages	6,200	Dec. 31	By Branch P&L A/c	10,500
	To Rent & Rates	1,200			
	To Sundry Expenses	800			
	To Petty Cash expenses (200-100)	100			
	To Allowance to customers	200			
	To Discount	1,400			
	To Bad Debts	600			
		10,500			10,500

Delhi Branch Profit & Loss Account

20X1		₹	20X1		₹
Dec. 31	To Branch Exp. A/c	10,500	Dec. 31	By Gross Profit b/d	19,900
	To Net Profit ts/f to General P & L A/c	9,400			
		19,900			19,900

(c) Branch Trading and Profit and Loss Account

	₹	₹		₹	₹
To Stock		7,000	By Sales:		
To Goods sent from H.O.	26,000		Cash	17,500	
Less: Returns to H.O.	(1,000)	25,000	Credit	28,400	
			Less: returns	(500)	
				27,900	45,400

To	Gross profit c/d	19,900	By	Closing Stock	6,500
		51,900			51,900
To	Salaries & Wages	6,200	By	Gross Profit b/d	19,900
To	Rent & Rates	1,200			
To	Sundry Exp.	800			
To	Petty Cash Exp.	100			
To	Allowances to Customers	200			
To	Discounts	1,400			
To	Bad Debts	600			
To	Net Profit	9,400			
		19,900			19,900

5.2 When goods are invoiced at selling price

Whenever, goods sent to branch are invoiced at selling price, certain considerations need to be kept in mind such as:

- It would be obvious that, if Branch Account is debited with the sales price of goods and subsequent to the debit being raised there is a change in the sale price, the amount of debit either has to be increased or reduced on a consideration of the quantity of *unsold stock* that was there at the branch at the time the change took place. Such an adjustment will be necessary as often as the change in sale price occurs.
- Moreover, the amount of anticipatory or unrealized profit, included in the value of unsold stock with the branch at the close of the year will have to be **eliminated** before the accounts of the branch are incorporated with that of the head office. This will be done by creating a reserve.

It may also be necessary to adjust the value of closing stock on account of the physical losses of stock due to either pilferage or wastages which may have

occurred during the year. This adjustment is made by debiting the cost of such goods to Goods Lost Account and the amount of loading (included in the lost goods), to the Branch Adjustment Account.

The three different methods that are usually adopted for maintaining accounts on this basis are described below:

(i) Stock and Debtors Method

Under this method, when goods are invoiced at selling price, one additional account i.e. 'Branch Adjustment account' is also prepared in addition to all the accounts which are maintained on cost basis. (Refer para 5.1)

- When goods are invoiced at selling price, the following points should be kept in mind under this method:

(i) Journal Entries:

Transaction	Accounts debited	Accounts credited
(a) Sale price of the goods sent from H.O. to the Branch	Branch Stock A/c (at selling price)	(i) Goods sent to Branches A/c with cost of the goods sent. (ii) Branch Adjustment A/c (with the loading <i>i.e.</i> , Difference between the selling and cost price).
(b) Return of goods By the Branch to H.O.	(i) Goods sent to Branch A/c (with the cost of goods returned). (ii) Branch Adjustment A/c (with the loading)	Branch Stock A/c
(c) Cash sales at the Branch	Branch Cash/Bank A/c	Branch Stock A/c
(d) Credit Sales at the Branch	Branch Debtors A/c	Branch Stock A/c

(e) Goods returned to Branch by customers	Branch Stock A/c	Branch Debtors A/c (at selling price)
(f) Goods lost in Transit or stolen	(i) Goods Lost in Transit A/c or Goods Stolen A/c (with cost of the goods) (ii) Branch Adjustment A/c (with the loading)	Branch Stock A/c

(ii) Closing Stock

The balance in the Branch Stock Account at the close of the year normally should be equal to the unsold stock at the Branch valued at sale price. But quite often the value of stock actually held at the branch is either more or less than the balance of the Branch Stock Account. In that event, as discussed earlier, it will be necessary that the balance in the Branch Stock Account is increased or reduced by debit or credit to Goods Lost Account (at cost price of goods) and Branch Adjustment Account (with the loading). The Stock Account at selling price, thus reveals loss of stock (or surplus) and serves as a check on the branch in this respect.

The discrepancy in the amount of balance in the Branch Stock Account and the value of stock actually in hand, valued at sale price, may be the result of one or more of the under-mentioned factors:

- An error in applying the percentage of loading.
- Goods having been sold either below or above the established selling price.
- A Commission to adjust returns or allowances.
- Physical loss of stock due to natural causes or pilferage.
- Errors in Stock-taking.

For example, the balance brought down in the Branch Stock Account is ₹ 100 in excess of the value of stock actually held by the branch when the goods were invoiced by the head office to the branch at 25% above cost and the discrepancy is either due to pilferage or loss by fire, the actual loss to the firm would be ₹ 80, since 20% of the invoice (same as 25% above cost) price would represent the element of profit. The adjusting entry in such a case would be:

		Dr. ₹	Cr. ₹
Goods Lost A/c	Dr.	80	
Branch Adjustment A/c	Dr.	20	
To Branch Stock A/c			100

If on the other hand, a part of the sale proceeds has been misappropriated, then in that case Loss by Theft A/c would be debited, rest of the entry being same.

Rebates and allowances allowed to customers debited to P&L A/c & credited to debtors A/c.

In the Goods Sent to Branch Account, the cost of the goods sent out to a branch for sale is credited by debiting Branch Stock Account. Conversely, the cost of goods returned by the branch is debited to this account. As such the balance in the account at the end of the year will be the cost of goods sent to the branch; therefore, it will be transferred either to the Trading Account or to Purchases Account of the head office.

The amount of profit anticipated on sale of goods sent to the branch is credited to the Branch Adjustment Account and conversely, the amount of profit not realized in respect of goods returned by the branch to head office or that in respect to stock remaining unsold with the branch at the close of the year is debited to Branch Adjustment Account. The balance in this account, at the end of year thus will consist of the amount of Gross Profit earned on sale by the branch. On that account, it will be transferred to the Branch Profit and Loss Account.

(iii) Elimination of unrealized profit in the closing stock

The balance in the Branch Stock account would be at the **sale price**; therefore, it would be necessary to eliminate the element of profit included in such closing stock. This is done by creating a reserve against unrealized profit, by debiting the Branch Adjustment Account and crediting Stock Reserve Account with an amount

equal to the difference in the cost and selling price of unsold stock. Sometimes instead of opening a separate account in respect of the reserve, the amount of the difference is credited to Branch Stock Account. In that case, the credited balance of such a reserve is also carried forward separately, along with the debit balance in the Branch Stock Account; the difference between the two would be the value of stock at cost. In either case, the credit balance will be deducted out of the value of closing stock for the purpose of disclosure in the balance sheet, so that the stock is shown at cost.

An Alternative method: Where the gross profit of each branch is not required to be ascertained separately, although the selling price is uniform, the amount of goods sent to the branch is recorded only in two accounts namely - Branch Stock Account and Goods Sent to Branch A/c.

In this method, at the end of the year the Branch Stock Account is closed by transfer of the balance representing the value of closing stock, at sale price, to the **Goods Sent to Branch Account**. This has the effect of altogether eliminating from the books the value of stock at the branch. The balance of Goods sent to Branch Account is afterwards transferred to the **Trading Account** representing the net sale price of goods sold at the branch. In that case, the value of closing stock at the branch at cost will be subsequently introduced in the Trading Account together with that of closing stock at the head office.

Illustration 3 (a)

Harrison of Chennai has a branch at New Delhi to which goods are sent @ 20% above cost. The branch makes both cash and credit sales. Branch expenses are met partly from H.O. and partly by the branch. The statement of expenses incurred by the branch every month is sent to head office for recording.

Following further details are given for the year ended 31st December, 20X1:

	₹
<i>Cost of goods sent to Branch at cost</i>	<i>2,00,000</i>
<i>Goods received by Branch till 31-12-20X1 at invoice price</i>	<i>2,20,000</i>
<i>Credit Sales for the year @ invoice price</i>	<i>1,65,000</i>
<i>Cash Sales for the year @ invoice price</i>	<i>59,000</i>
<i>Cash Remitted to head office</i>	<i>2,22,500</i>

Expenses paid by H.O.		12,000
Bad Debts written off		750
Balances as on	1-1-20X1	31-12-20X1
	₹	₹
Stock	25,000 (Cost)	28,000 (invoice price)
Debtors	32,750	26,000
Cash in Hand	5,000	2,500

Show necessary ledger accounts in the books of the head office and determine the Profit or Loss of the Branch for the year ended 31st December, 20X1.

Solution

Books of Harrison Branch Stock Account

	₹		₹
To Balance b/d – Op Stock	30,000	By Branch Debtors (Sales)	1,65,000
To Goods Sent to Branch A/c	2,40,000	By Branch Cash	59,000
To Branch Adjustment A/c	2,000	By Balance c/d	
(Balancing Figure – Excess of Sale over Invoice Price)		Goods in Transit (₹ 2,40,000 – ₹ 2,20,000)	20,000
		Closing Stock at Branch	28,000
	2,72,000		2,72,000

Branch Debtors Account

	₹		₹
To Balance b/d	32,750	By Bad debts written off	750
To Branch Stock A/c (Sales)	1,65,000	By Branch Cash (bal. fig.)	1,71,000
		By Balance c/d	26,000
	1,97,750		1,97,750

Branch Cash Account

	₹		₹
To Balance b/d	5,000	By Bank Remittance to H.O.	2,22,500
To Branch Stock	59,000	By Branch Expenses	10,000
To Branch Debtors	1,71,000	[met by Branch (Bal. fig.)]	
		By Balance c/d	2,500
	2,35,000		2,35,000

Branch Adjustment Account

	₹		₹
To Branch P &L - Gross Profit (Bal. fig.)	39,000	By Stock Reserve opening (25,000 × 20%)	5,000
To Stock Reserve (on closing stock (48,000 × 1/6)	8,000	By Goods sent to Branch A/c	40,000
	47,000	By Branch Stock A/c	2,000
	47,000		47,000

Branch Expenses

	₹		₹
To Cash (H.O)	12,000	By Branch P&L A/c	
To Branch Cash	10,000		22,000
	22,000		22,000

Branch Profit and Loss Account

	₹		₹
To Branch Expenses	22,000	By Gross Profit (from Branch Adjustment A/c)	39,000
To Branch Debtors (bad debts)	750		
To Net Profit	16,250		
	39,000		39,000

Goods Sent to Branch Account

	₹		₹
To Branch Adjustment A/c	40,000	By Branch to Stock A/c	2,40,000
To Purchase A/c - Transfer	2,00,000		2,40,000
	2,40,000		

(ii) Debtors Method

Under this method, the principal accounts that will be maintained are:

- The Branch Account;
- The Goods Sent to Branch Account; and
- The Stock Reserve Account.

Entries in these accounts will be made in the following manner:

	Transaction	Account debited	Account credited
(a)	Goods sent to Branch at selling price	Branch A/c	Goods Sent to Branch A/c
(b)	'Loading' being the difference between selling price and cost of goods	Goods Sent to Branch A/c	Branch A/c
(c)	Returns to H.O. at selling price	Goods Sent to Branch A/c	Branch A/c
(d)	'Loading' in respect of goods returned to H.O.	Branch A/c	Goods Sent to Branch A/c
(e)	'Loading' included in the opening stock to reduce it	Stock Reserve A/c	Branch A/c
(f)	Closing stock at selling price	Branch Stock A/c	Branch A/c
(g)	'Loading' included in closing stock to reduce it to cost	Branch A/c	Stock Reserve A/c

It will be observed that entries in the Branch Account in respect of goods sent to a branch or returned by it, as well as those for the opening and closing stock, will be at selling price. In consequence, the Branch Account is maintained at selling price.

Hence, the Branch Account will not correctly show the trading profit of the Branch unless these amounts are adjusted to cost. Such an adjustment is effected by making contra entries in 'Goods Sent to Branch A/c' and 'Stock Reserve Account'. In respect of closing stock at branch for the purpose of disclosure in the Balance Sheet, the credit balance in the 'Stock Reserve Account' at the end of the year will be deducted from the value of the closing stock, so as to reduce it to its cost; it will be carried forward as a separate balance to the following year, for being transferred to the credit of the Branch Account.

Illustration 3 (b)

Take figures from Illustration 3 (a) and prepare branch account following debtors' method.

Solution

**Books of Harrison
New Delhi Branch Account**

	₹		₹
To Balance B/d			
Stock	30,000	By Stock Reserve	5,000
Debtors	32,750		
Cash	5,000		
To Goods Sent to Branch A/c (2,00,000 + 20%)	2,40,000	By Goods Sent to Branch A/c	40,000
To Cash (Exp. paid by H.O.)	12,000	By Cash – Remittance from branch	2,22,500
To Net Profit ts/f to H.O. Profit & Loss A/c (Balancing Figure)	16,250	By Balance c/d Debtors	26,000

To Stock reserve (48,000X20/120)	8,000	Stock (including Transit – W.N 2)	48,000
		Cash	2,500
	3,44,000		3,44,000

Working Note:

Closing Stock = Stock at branch + Stock in Transit (Goods sent by HO – Goods Received by Branch) = ₹ 28,000 + (₹ 2,40,000 – ₹ 2,20,000) = ₹ 48,000.

Illustration 4

Sell Well who carried on a retail business opened a branch X on January 1st, 20X1 where all sales were on credit basis. All goods required by the branch were supplied from the Head Office and were invoiced to the branch at 10% above cost.

The following were the transactions:

	Jan. 20X1	Feb. 20X1	March 20X1
	₹	₹	₹
<i>Goods sent to Branch (Purchase Price)</i>	40,000	50,000	60,000
<i>Sales as shown by the branch monthly report</i>	38,000	42,000	55,000
<i>Cash received from Debtors and remitted to H.O.</i>	20,000	51,000	35,000
<i>Returns to H.O. (Invoice price to Branch)</i>	1,200	600	2,400

The stock of goods held by the branch on March 31, 20X1 amounted to ₹ 53,400 at invoice to branch.

Record these transactions in the Head Office books, showing balances as on 31st March, 20X1 and the branch gross profit for the three months ended on that date.

All workings should form part of your solution.

Solution

**Books of Sell Well
Branch Account**

	₹			₹
To Goods sent to Branch A/c (1,50,000+10%)	1,65,000	By Goods sent to Branch-Loading		15,000
To Goods sent to Branch A/c (4,200 X 10/110)	382	By Goods sent to Branch-returns		4,200
		By Bank		1,06,000
		By Balance c/d - Closing Branch Assets		
To Stock Reserve (53,400 X 10/110)	4,855	Stock	53,400	
To Net Profit (Bal fig) ts/f to General P&L A/c	37,363	Debtors (Sales-Collection)	<u>29,000</u>	82,400
	<u>2,07,600</u>			<u>2,07,600</u>

Working Note:

Memorandum Branch Debtors Account

	₹		₹
To Balance b/d	---	By Cash/Bank	1,06,000
To Sales	1,35,000	By Balance c/d	29,000
	<u>1,35,000</u>		<u>1,35,000</u>

Goods Sent to Branch Account

	₹		₹
To Branch A/c – Loading	15,000	By Branch A/c	1,65,000
To Branch A/c – Returns	4,200	By Branch A/c – Loading	382
To Purchases A/c	1,46,182	on returns	
	1,65,382		1,65,382

(iii) Trading and Profit and Loss Account (Final Accounts) Method

All items of memorandum Branch Trading and Profit and Loss Account are to be converted into cost price if the goods are invoiced to branch at selling price. Other points will remain same as already discussed in Para 5.1 for this method if goods are invoiced at cost.

Illustration 5

Following is the information of the Jammu branch of Best New Delhi for the year ending 31st March, 20X2 from the following:

- (1) Goods are invoiced to the branch at cost plus 20%.
- (2) The sale price is cost plus 50%.
- (3) Other information:

	₹
Stock as on 01.04.20X1 (invoice price)	2,20,000
Goods sent during the year (invoice price)	11,00,000
Sales during the year	12,00,000
Expenses incurred at the branch	45,000

Ascertain

- (i) the profit earned by the branch during the year.
- (ii) branch stock reserve in respect of unrealized profit.

Solution

- (i) **Calculation of profit earned by the branch
In the books of Jammu Branch
Trading Account and Profit and Loss Account**

Particulars	Amount	Particulars	Amount
	₹		₹
To Opening stock	2,20,000	By Sales	12,00,000
To Goods received by Head office	11,00,000	By Closing stock (Refer W.N.)	3,60,000
To Expenses	45,000		
To Net profit (Bal fig)	1,95,000		
	15,60,000		15,60,000

- (ii) **Stock reserve in respect of unrealised profit**

$$= ₹ 3,60,000 \times (20/120) = ₹ 60,000$$

Working Note:

	₹	
Cost Price	100	
Invoice Price	120	
Sale Price	150	
Calculation of closing stock at invoice price	₹	
Opening stock at invoice price	2,20,000	
Goods received during the year at invoice price	11,00,000	
	13,20,000	
Less: Cost of goods sold at invoice price	(9,60,000)	[12,00,000 x (120/150)]
Closing stock	3,60,000	

Illustration 6

Hindustan Industries Mumbai has a branch in Cochin to which office goods are invoiced at cost plus 25%. The branch sells both for cash and on credit. Branch Expenses are paid direct from head office, and the Branch has to remit all cash received into the Head Office Bank Account.

From the following details, relating to calendar year 20X1, prepare the accounts in the Head Office Ledger and ascertain the Branch Profit. Branch does not maintain any books of account, but sends weekly returns to the Head Office:

	₹
Goods received from Head Office at invoice price	6,00,000
Returns to Head Office at invoice price	12,000
Stock at Cochin as on 1st Jan., 20X1	60,000
Sales in the year - Cash	2,00,000
Credit	3,60,000
Sundry Debtors at Cochin as on 1st Jan. 20X1	72,000
Cash received from Debtors	3,20,000
Discount allowed to Debtors	6,000
Bad debts in the year	4,000
Sales returns at Cochin Branch	8,000
Rent, Rates, Taxes at Branch	18,000
Salaries, Wages, Bonus at Branch	60,000
Office Expenses	6,000
Stock at Branch on 31st Dec. 20X1 at invoice price	1,20,000

Prepare Branch accounts in books of head office by Stock and debtors method.

Solution

**Books of Hindustan Industries, Mumbai
Cochin Branch Stock Account**

	₹		₹
To Balance b/d – Op Stock	60,000	By Bank A/c – Cash Sales	2,00,000
To Branch Debtors A/c – Sales Return	8,000	By Branch Debtors A/c - Credit Sales	3,60,000
To Goods sent to Branch A/c	6,00,000	By Goods sent to Branch (Returns to H.O.)	12,000
To Branch Adjustment A/c (Excess of Selling Price over Invoice Price)	24,000	By Balance c/d - Closing stock	1,20,000
	6,92,000		6,92,000

Cochin Branch Stock Adjustment Account

	₹		₹
To Goods sent to Branch A/c (1/5 of ₹ 12,000) (on returns)	2,400	By Balance b/d (1/5 of ₹ 60,000)	12,000
To Branch P & L A/c (Profit on sale) – Bal fig	1,29,600	By Goods sent to Branch A/c (1/5 of ₹ 6,00,000)	1,20,000
To Balance c/d (1/5 of ₹ 1,20,000)	24,000	By Branch Stock	24,000
	1,56,000		1,56,000

Goods Sent to Branch Account

	₹		₹
To Cochin Branch Stock Adjustment A/c	1,20,000	By Cochin Branch Stock A/c	6,00,000
To Cochin Branch Stock A/c (Returns)	12,000	By Cochin Branch Stock Adj. A/c	2,400
To Purchases A/c	4,70,400		
	6,02,400		6,02,400

Branch Debtors Account

	₹		₹
To Balance b/d	72,000	By Bank	3,20,000
To Branch Stock A/c	3,60,000	By Branch P&L A/c Discount	6,000
		By Branch P&L A/c - Bad Debts	4,000
		By Branch Stock - Sales Returns	8,000
		By Balance c/d	94,000
	4,32,000		4,32,000

Branch Expenses Account

	₹		₹
To Bank A/c (Rent, Rates & Taxes)	18,000	By Branch Profit & Loss A/c (Transfer)	84,000
To Bank A/c (Salaries & Wages)	60,000		
To Bank A/c (office exp.)	6,000		
	84,000		84,000

Branch Profit & Loss Account for the year ending 31st Dec. 20X1

	₹		₹
To Branch Expenses A/c	84,000	By Branch Stock Adj. A/c	1,29,600
To Branch Debtors A/c	6,000		

To Branch Debtors A/c	4,000		
To Net Profit transferred to Profit & Loss A/c	35,600		
	1,29,600		1,29,600

Illustration 7

Arnold of Delhi, trades in Ghee and Oil. It has a branch at Lucknow. He dispatches 25 tins of Oil @ ₹ 1,000 per tin and 15 tins of Ghee @ ₹ 1,500 per tin on 1st of every month. The branch incurs some expenditure which is met out of its collections; this is in addition to expenditure directly paid by Head Office.

Following are the other details:

		Delhi	Lucknow
		₹	₹
<i>Purchases</i>	<i>Ghee</i>	14,75,000	-
	<i>Oil</i>	29,32,000	-
<i>Direct expenses</i>		3,83,275	-
<i>Expenses paid by H.O.</i>		-	14,250
<i>Sales</i>	<i>Ghee</i>	18,46,350	3,42,750
	<i>Oil</i>	27,41,250	3,15,730
<i>Collection during the year (including Cash Sales)</i>		-	6,47,330
<i>Remittance by Branch to Head Office</i>		-	6,13,250

		(Delhi)	
		1-1-20X1	31-12-20X1
<i>Balance as on:</i>			
<i>Stock:</i>	<i>Ghee</i>	1,50,000	3,12,500
	<i>Oil</i>	3,50,000	4,17,250
<i>Debtors</i>		7,32,750	-
<i>Cash on Hand</i>		70,520	55,250
<i>Furniture & Fittings</i>		21,500	19,350
<i>Plant/Machinery</i>		3,07,250	7,73,500

	(Lucknow)	
	1-1-20X1	31-12-20X1
<i>Balance as on:</i>		
Stock: Ghee	17,000	13,250
Oil	27,000	44,750
Debtors	75,750	?
Cash on Hand	7,540	12,350
Furniture & Fittings	6,250	5,625
Plant/Machinery	-	

Addition to Plant/Machinery on 1-1-20X1 ₹ 6,02,750.

Rate of Depreciation: Furniture / Fittings @ 10% and Plant / Machinery @ 15% (already adjusted in the above figures).

The Branch Manager is entitled to 10% commission after charging such commission whereas, the General Manager is entitled to 10% commission on overall company profits after charging such commission. General Manager is also entitled to a salary of ₹ 2,000 p.m. General expenses incurred by H.O. ₹ 24,000.

Prepare Branch Account in the head office books and also prepare the Arnold's Trading and Profit and Loss A/c (excluding branch transactions).

Solution

In the books of Arnold Lucknow Branch Account

	₹		₹
To Balance b/d		By Bank (Remittance)	6,13,250
-Opening Branch Assets		By Closing Branch Assets	
Opening stock:		Closing stock:	
Ghee	17,000	Ghee	13,250
Oil	27,000	Oil	44,750
Debtors	75,750	Debtors (W.N. 1)	86,900
Cash on hand	7,540	Cash on hand (W.N. 2)	12,350

Furniture & fittings	6,250	Furniture & fittings	5,625
To Goods sent to Branch A/c			
Ghee (15 x 1500 x 12)	2,70,000		
Oil (25 x 1000 x 12)	3,00,000		
To Bank (Expenses paid)	14,250		
To Branch Manager commission			
(₹ 58,335 × 1/11)	5,303		
To Net Profit transferred to General P & L A/c	53,032		
	7,76,125		7,76,125

Arnold

**Trading and Profit and Loss account for the year ended 31st December, 20X1
(Excluding branch transactions)**

	₹		₹
To Opening Stock:		By Sales:	
Ghee	1,50,000	Ghee	18,46,350
Oil	3,50,000	Oil	27,41,250
To Purchases:		By Closing Stock:	
Ghee 14,75,000		Ghee	3,12,500
Less: Goods sent to Branch (2,70,000)	12,05,000	Oil	4,17,250
Oil 29,32,000			
Less: Goods sent to Branch (3,00,000)	26,32,000		
To Direct Expenses	3,83,275		
To Gross Profit c/d	5,97,075		
	53,17,350		53,17,350
To Manager's Salary	24,000	By Gross Profit b/d	5,97,075

To General Expenses	24,000	By Branch Profit transferred	53,032
To Depreciation:			
Furniture @10% 2,150			
Plant & Machinery @ 15% (W.N.3) <u>1,36,500</u>	1,38,650		
To General Manager's Commission @ 10% (i.e., 4,63,457 × 1/11)	42,132		
To Net profit	4,21,325		
	<u>6,50,107</u>		<u>6,50,107</u>

Working Notes:**(1) Memorandum Branch Debtors Account**

	₹		₹
To Balance b/d	75,750	By Cash Collections (including Cash Sales)	6,47,330
To Sales (including Cash Sales)		By Balance c/d	86,900
Ghee	3,42,750		
Oil	3,15,730		
	<u>7,34,230</u>		<u>7,34,230</u>

(2) Memorandum Branch Cash Account

	₹		₹
To Balance b/d	7,540	By Remittance	6,13,250
To Collections	6,47,330	By Exp. (Balance fig.)	29,270
		By Balance c/d	12,350
	<u>6,54,870</u>		<u>6,54,870</u>

(3) Depreciation on Plant & Machinery

$$3,07,250 \times 15\% + 6,02,750 \times 15\% = ₹1,36,500$$

5.3 Goods invoiced at wholesale price to retail branches

Under this method, the Head Office (particularly, the manufacturing concern) supplies goods to its retail branches at wholesale price which is cost plus wholesale profit.

Profit of branch = Sale proceeds at shop - wholesale price of the goods sold.

For this purpose, it is assumed that Manufacturer would always be able to sell the goods on wholesale terms thereby Manufacturer profit = Wholesale price - Cost.

Many concerns, therefore, invoice goods to such shops at wholesale price and determine profit or loss on sale of goods on this basis.

Branch Stock Account or the Trading Account is debited with:

- (a) the value of opening stock at the Branch; and
- (b) price of goods sent during the year at wholesale price.

It is credited by:

- (a) sales effected at the shop; and
- (b) closing stock of goods valued at wholesale price.

The value of goods lost due to accident, theft etc. also is credited to the Branch Stock Account or Trading Account calculated at the **wholesale price**. At this stage, the Branch Stock or Trading Account will reveal the amount of gross profit (or loss). It is transferred to the Branch Profit and Loss Account. On further being debited with the expenses incurred at the shop and the wholesale price of goods lost, the Branch Profit and Loss Account will disclose the net profit (or loss) at the shop.

Since the closing stock at the branch has to be valued at wholesale price, it would be necessary to create a stock reserve equal to the difference between its wholesale price and its cost (to the head office) by debiting the amount in the *Head Office Profit and Loss Account*. This Stock Reserve is carried forward to the next year and then transferred to the credit of the (Head Office) Profit and Loss Account.

Illustration 8

M/s Rahul operates a number of retail outlets to which goods are invoiced at wholesale price which is cost plus 25%. These outlets sell the goods at the retail price which is wholesale price plus 20%.

Following is the information regarding one of the outlets for the year ended 31.3.20X2:

	₹
Stock at the outlet 1.4.20X1	30,000
Goods invoiced to the outlet during the year	3,24,000
Gross profit made by the outlet	60,000
Goods lost by fire	?
Expenses of the outlet for the year	20,000
Stock at the outlet 31.3.20X2	36,000

You are required to prepare the following accounts in the books of Rahul Limited for the year ended 31.3.20X2:

- (a) Outlet Stock Account.
- (b) Outlet Profit & Loss Account.
- (c) Stock Reserve Account.

Solution**Outlet Stock Account**

	₹		₹
To Balance b/d	30,000	By Sales (Working Note 1)	3,60,000
To Goods sent to outlet	3,24,000	By Goods lost by fire (b.f.)	18,000
To Gross Profit c/d	60,000	By Balance c/d	36,000
	4,14,000		4,14,000

Outlet Profit & Loss Account

	₹		₹
To Expenses	20,000	By Gross Profit b/d	60,000
To Goods lost by fire (W.N.2)	18,000		
To Profit transferred	22,000		
	60,000		60,000

Stock Reserve Account

	₹		₹
To HO P & L A/c – Transfer	6,000	By Balance b/d	6,000
To Balance c/d (Stock Res. required)	7,200	By HO P&L A/c (W.N. 3)	7,200
	13,200		13,200

Working Notes:

$$\begin{aligned}
 & \hspace{15em} ₹ \\
 (1) \quad \text{Wholesale Price} & \quad 100+25 & = 125 \\
 \text{Retail Price} & \quad 125 + 20\% & = 150 \\
 \text{Gross Profit at the outlet} & & \\
 \text{Wholesale Price – Retail Price} & \quad (150 – 125) & \quad 25 \\
 \text{Retail sales value} & = 60,000 \times \frac{150}{125} & = ₹ 3,60,000
 \end{aligned}$$

(2) Goods lost by fire

$$\begin{aligned}
 & \text{Opening Stock} + \text{Goods Sent} + \text{Gross Profit} - \text{Sales} - \text{Closing Stock} \\
 & 30,000 + 3,24,000 + 60,000 - 3,60,000 - 36,000 = ₹ 18,000
 \end{aligned}$$

(3) Stock Reserve

$$\begin{aligned}
 \text{Opening Stock} & \quad = 30,000 \times \frac{25}{125} = ₹ 6,000 \\
 \text{Closing Stock} & \quad = 36,000 \times \frac{25}{125} = ₹ 7,200
 \end{aligned}$$



6. ACCOUNTING FOR INDEPENDENT BRANCHES

When the size of the business is big, it is desirable that the branch maintains complete records of its transactions. These branches are called independent branches and each independent branch maintains comprehensive account books for recording their transactions; therefore, a separate trial balance of each branch can be prepared. The head office maintains one ledger account for each such branch, wherein all transactions between the head office and the branches are recorded.

Salient features of accounting system of an independent branch are as follows:

1. Branch maintains its entire books of account under double entry system.
2. Branch opens in its books a Head Office account to record all transactions that take place between Head Office and branch. The Head Office maintains a Branch account to record these transactions.
3. Branch prepares its Trial Balance, Trading and profit and loss Account at the end of the accounting period and sends copies of these statements to Head Office for incorporation.
4. After receiving the final statements from branch, Head Office reconciles between the two – Branch account in Head Office books and Head Office account in Branch books.
5. Head office passes necessary journal entries to incorporate branch trial balance in its books.

The Head Office Account in branch books and Branch Account in head office books is maintained respectively.

	Transactions	Head office books		Branch books	
(i)	Dispatch of goods to branch by H.O.	Branch A/c To Good sent to Branch A/c	Dr.	Goods received from H.O. A/c To Head Office A/c	Dr.
(ii)	When goods are returned by the Branch to H.O.	Goods sent to Branch A/c To Branch A/c	Dr.	Head Office A/c To Goods received from H.O. A/c	Dr.
(iii)	Branch Expenses are paid by the Branch	No Entry		Expenses A/c To Bank or Cash A/c	Dr.
(iv)	Branch Expenses paid by H.O.	Branch A/c To Bank or cash	Dr.	Expenses A/c To Head Office A/c	Dr.
(v)	Outside purchases made by the Branch	No Entry		Purchases A/c To Bank (or) Creditors A/c	Dr.

(vi)	Sales effected by the Branch	No Entry		Cash or Debtors A/c To Sales	Dr.
(vii)	Collection from Debtors of the Branch recd. by H.O.	Cash or Bank A/c To Branch A/c	Dr.	Head office A/c To Sundry Debtors A/c	Dr.
(viii)	Payment by H.O. for purchase made by Branch	Branch A/c To Bank	Dr.	Purchases (or) Sundry Creditors A/c To Head Office	Dr.
(ix)	Purchase of Asset by Branch	No Entry		Sundry Assets To Bank (or) Liability	Dr.
(x)	Asset purchased by the Branch but Asset A/c retained at H.O. books	Branch Asset A/c To Branch A/c	Dr.	Head office To Bank (or) Liability	Dr.
(xi)	Depreciation on (x) above	Branch A/c To Branch Asset	Dr.	Depreciation A/c To Head Office A/c	Dr.
(xii)	Remittance of funds by H.O. to Branch	Branch A/c To Bank	Dr.	Bank A/c To Head Office	Dr.
(xiii)	Remittance of funds by Branch to H.O.	Reverse entry of (xii) above i.e.		Reverse entry of (xii) above	
(xiv)	Transfer of goods from one Branch to another branch	(Recipient) Branch A/c To Supplying Branch A/c	Dr.	<u>Supplying Branch</u> H.O. A/c To Goods sent to H.O. A/c <u>Recipient Branch</u> Goods Received from H.O. A/c To Head Office A/c	Dr.

Students may find a few further practical situations and it is hoped that they can pass entries on the basis of accounting principles explained above.

The final result of these adjustments will be that so far as the Head Office is concerned, the branch will be looked upon either as a debtor or creditor, as a debtor if the amount of its assets is in excess of its liabilities and as a creditor if the position is reverse.

A debit balance in the Branch Account should always be equal to the net assets at the branch. The important thing to remember, when independent sets of accounts are maintained, is that the branch and head office books are connected with each other only through the medium of the Branch and the Head Office Account which are converse of each other. Also, when the accounts of branch and head office are consolidated, both the Branch and Head Office Accounts will be eliminated.



7. ADJUSTMENT AND RECONCILIATION OF BRANCH AND HEAD OFFICE ACCOUNTS

If the branch and the head office accounts, converse of each other, do not tally, these must be **reconciled** before the preparation of the final accounts of the concern as a whole.

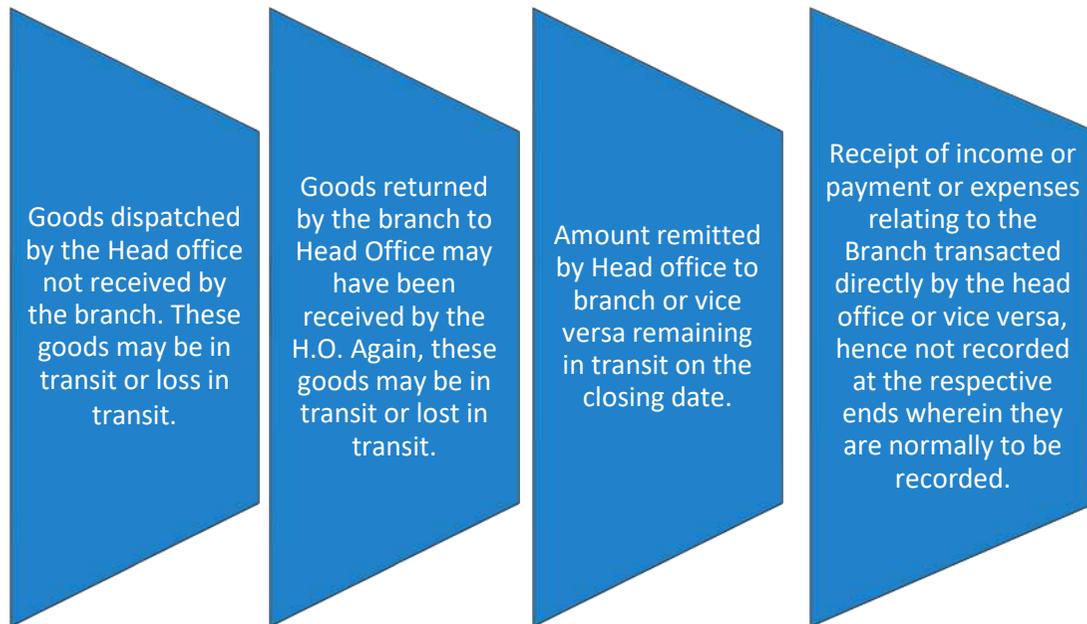
For example, if Head Office has sent goods worth ₹ 50,000 but the branch has received till the closing date goods only ₹ 40,000, then the branch should treat ₹ 10,000 as goods in transit and should pass the following entry :

	Dr.		Cr.
Goods in transit A/c	Dr.	10,000	
To Head Office A/c			10,000

However, there will be no entry in Head office books being the point where the event has been recorded in full, hence no further entries in Head office books.

7.1 Reasons for Disagreement

Following are the possible reasons for the disagreement between Branch A/c in Head office books and Head office A/c in Branch books on the closing date:



The technique of reconciliation has been illustrated through the example given below :

	Head office		Branch	
	Dr.	Cr.	Dr.	Cr.
Goods sent to Branch		1,50,000	-	
Goods recd. from H.O. A/c		-	1,40,000	
Branch A/c	1,12,000			
Head office A/c	-	-	-	78,500

On analysis of Branch A/c in Head office books and Head office A/c in branch books, you find:

- Goods valued ₹10,000 sent by head office has not been received by branch, hence not recorded in the branch books.
- ₹ 15,000 remitted by the branch has not been received, hence not recorded in the head office books.
- Direct collection of ₹ 10,500 from a customer of the branch by Head office not informed to the branch, hence not recorded by the branch.

- A sum of ₹ 14,500 paid by branch to the suppliers of head office not recorded at Head office.
- Head office expenditure allocation to the branch ₹12,000 not recorded in the branch.
- ₹ 7,500 being FD interest of head office received by the branch on oral instructions from H.O., not recorded in the head office books.

			Head Office Books			Branch Books	
			Dr. ₹	Cr. ₹		Dr. ₹	Cr. ₹
(i)	Goods in transit (₹ 10,000)		-	-	Goods in Transit A/c To Head office A/c (No Entry)	10,000	10,000
(ii)	Cash in Transit:	Cash in Transit A/c To Branch A/c	15,000	15,000			
(iii)	Direct Collection by H.O. on behalf of the Branch				Head Office A/c To Debtors A/c	10,500	10,500
(iv)	Direct payment of ₹ 14,500 by Branch on behalf of H.O	Sundry Creditors A/c To Branch A/c	14,500	14,500			
(v)	Expenditure Allocated to Branch				Branch Exp. A/c To H.O. A/c	12,000	12,000

(vi)	Fixed Deposit interest of ₹ 7,500 directly received by the Branch	Branch A/c To Sundry Income	7,500	7,500			
------	---	-----------------------------	-------	-------	--	--	--

**In Branch Books
Head Office Account**

	₹		₹
To Sundry Debtors A/c	10,500	By Balance b/d	78,500
To Balance c/d	90,000	By Goods in transit	10,000
		By Branch expenses	12,000
	1,00,500		1,00,500
		By Balance b/d	90,000

**In the Books of Head Office
Branch A/c**

	₹		₹
To Balance b/d	1,12,000	By Cash in Transit	15,000
To Sundry Income	7,500	By Sundry Creditors	14,500
		By Balance c/d	90,000
	1,19,500		1,19,500
To Balance b/d	90,000		

Important Points to be noted:

- (i) the balance of Head Office A/c in Branch books and Branch A/c in Head Office books have tallied.
- (ii) Adjustment are made only at the point:
Where the recording has been omitted, and
Other than the point where action has already been effected.

7.2 Other points

(1) Inter-Branch Transactions

Inter-branch transactions (i.e. transaction between two branches) are usually adjusted as if they were entered into only with the head office. It is a very convenient method of treating such transaction especially where the number of branches are large. Suppose Kolkata Branch incurred an expenditure on advertisement of ₹ 1,000 on account of Delhi Branch, the entries that would be made in such a case would be as follows:

		Dr.	Cr.
		₹	
In Kolkata Books:			
Head Office A/c	Dr.	1,000	
To Cash			1,000
In Delhi Books:			
Advertisement A/c	Dr.	1,000	
To H.O. A/c			1,000
In H.O. Books:			
Delhi Branch A/c	Dr.	1,000	
To Kolkata Branch A/c			1,000

(2) Fixed Assets

Often the accounts of fixed assets of a branch are kept in the head office books; in such a case, at the end of the year, the amount of depreciation on the assets is debited to the branch concerned by recording the following entry by head office:

Branch Account	Dr.
To Branch Asset Account	

The branch will pass the following entry:

Depreciation Account	Dr.
To Head Office Account	

(3) Head office Expenses charged to Branch

Usually the head office devotes considerable time in attending to the affairs of the branch; on that account, it may decide to raise a charge against the branch in respect of the cost of such time. In such a case the amount is debited to the branch (being receivable from branch) and is credited to appropriate expense head such as Salaries Accounts, General Charges Account, Entertainment Account etc (i.e. reducing the expense in head office books). The branch credits the H.O. Account and debits Expenses Account.

Illustration 9

Give Journal Entries in the books of an independent Branch to rectify or adjust the following:

- (i) *Branch paid ₹ 5,000 as salary to H.O supervisor, but the amount paid by branch has been debited to salary account in the books of branch.*
- (ii) *Asset Purchased by branch for ₹ 25,000, but the Asset account was retained in H.O Books.*
- (iii) *A remittance of ₹8,000 sent by the branch has not been received by H.O.*
- (iv) *H.O collected ₹ 25,000 directly from the customer of Branch but fails to give the intimation to branch.*
- (v) *Remittance of funds by H.O to branch ₹5,000 not entered in branch books.*

Solution

Journal Entries in Books of Branch

	Particulars		Dr. Amount ₹	Cr. Amount ₹
(i)	Head office account Dr. To Salaries account (Being the rectification of salary paid on behalf of H.O.)		5,000	5,000

(ii)	Head office account To Bank / Liability A/c (Being Asset purchased by branch but Asset account retained at head office books)	Dr.	25,000	25,000
(iii)	No Entry in Branch Books			
(iv)	Head office account To Debtors account (Being the amount of branch debtors collected by H.O.)	Dr.	25,000	25,000
(v)	Bank A/c To Head Office (Remittance of Funds by H.O. to Branch)	Dr.	5,000	5,000

Illustration 10

The following Trial balances as at 31st December, 20X1 have been extracted from the books of Major Ltd. and its branch at a stage where the only adjustments requiring to be made prior to the preparation of a Balance Sheet for the undertaking as a whole are to be done.

	Head Office		Branch	
	Dr. ₹	Cr. ₹	Dr. ₹	Cr. ₹
Share Capital		1,50,000		
Fixed Assets	75,125		18,901	
Current Assets	1,21,809		23,715	(Note 3)
Current Liabilities		34,567		9,721
Stock Reserve, 1st Jan., 20X1 (Note 2)		693		
Revenue Account		43,210		10,250
Branch Account	31,536			
Head Office Account				22,645
	2,28,470	2,28,470	42,616	42,616

You are required to record the following in the appropriate ledger accounts in both sets of books.

Note:

1. Goods transferred from Head Office to the Branch are invoiced at cost plus 10% and both Revenue Accounts have been prepared on the basis of the prices charged.
2. Relating to the Head Office goods held by the Branch on 1st January, 20X1.
3. Includes goods received from Head Office at invoice price ₹ 4,565.
4. Goods invoiced by Head Office to Branch at ₹ 3,641 were in transit at 31st December, 20X1, as was also a remittance of ₹ 3,500 from the Branch.
5. At 31st December, 20X1, the following transactions were reflected in the Head Office books but unrecorded in the Branch books.

The purchase price of lorry, ₹ 2,500, which reached the Branch on December 25th; a sum received on December 30, 20X1 from one of the Branch debtors, ₹ 750.

Solution

**H.O. Books
Branch Account**

20X1		₹	20X1		₹
Dec. 31	To Balance b/d	31,536	Dec. 31	By Cash in transit	3,500
				By Balance c/d	28,036
		31,536			31,536

Cash in transit Account

20X1		₹	20X1		₹
Dec. 31	To Branch A/c	3,500	Dec. 31	By Balance c/d	3,500

Stock Reserve Account

20X1		₹	20X1		₹
Dec. 31	To Balance c/d	746	Jan. 1	By Balance b/d	693
	(4,565+3,641) x 10/110			By Revenue A/c (b.f.)	53
		746			746

Revenue Account

20X1		₹	20X1		₹
Dec. 31	To Stock Reserve	53	Dec. 31	By Balance b/d	43,210
	To Balance c/d	43,157			
		43,210			43,210

Branch Books
Head Office Account

20X1		₹	20X1		₹
Dec. 31	To Current Assets	750	Dec. 31	By Balance b/d	22,645
	To Balance c/d	28,036		By Goods in transit	3,641
		28,786		By Motor Vehicle	2,500
					28,786

Goods in Transit Account

20X1		₹	20X1		₹
Dec. 31	To Head Office	3,641	Dec. 31	By Balance c/d	3,641

Motor Vehicle Account

20X1		₹	20X1		₹
Dec. 31	To Head Office	2,500	Dec. 31	By Balance c/d	2,500

Sundry Current Assets A/c

20X1		₹	20X1		₹
Dec. 31	To Balance b/d	23,715	Dec. 31	By H.O. (Remittance by Debtor)	750
				By Balance c/d	22,965
		23,715			23,715



8. INCORPORATION OF BRANCH BALANCE IN HEAD OFFICE BOOKS

The method that will be adopted for incorporating the trading result of the branch with that of the head office would depend on whether it is desired to prepare

- (a) Standalone P&L & Balance Sheet for each Branch, or
- (b) Consolidated statement of Branch & H.O.

Method I: Separate P&L & Balance Sheet for each Branch

Amount of P&L is shown by Branch & is transfer to H.O. in Branch books & converse entry is passed in H.O. Books as:

Branch A/c	Dr.
	To Profit & Loss A/c

In such a case, not only P&L but also separate Balance Sheet for Branch & H.O. is to be prepared. The Branch Balance Sheet would show the amount advanced by H.O. to it as "Capital." In H.O. Books such amount would be shown as "Advance to Branch"

Method II: Prepare a consolidated Profit & Loss Account and Balance Sheet

Individual balances of all the revenue accounts would be separately transferred to the Head Office Account by debit or credit in the branch books and the converse entries would be passed in the head office books. The effect thereof will be similar to the amount of net profit or loss of the branch having been transferred since it would be composed of the balances that have been transferred. In case it is also desired that consolidated balance sheet of the branch and the head office should be prepared, it will also be necessary to transfer the balance of assets and liabilities of the branch to the head office. The adjusting entries that would be passed in this respect in the books of branch are shown below:

(a) Head Office Account	Dr.
	To Asset (individual) Account

- (b) (Individual) Liability Account Dr.
 To Head Office Account

Converse entries are passed in the head office books.

It is obvious that after afore-mentioned entries have been passed, the Branch Account in the Head Office books and Head Office Account in the branch books will be closed and it will be necessary to restart them at the beginning of the next year.

In consequence, at the beginning of the following year, the under-mentioned entry is recorded by the branch:

- Asset Account (In Detail) Dr.
 To Liability Accounts (In Detail)
 To H.O. Account (The difference between assets and liabilities)

Illustration 11

KP manufactures a range of goods which it sells to wholesale customers only from its head office. In addition, the H.O. transfers goods to a newly opened branch at factory cost plus 15%. The branch then sells these goods to the general public on only cash basis.

The selling price to wholesale customers is designed to give a factory profit which amounts to 30% of the sales value. The selling price to the general public is designed to give a gross margin (i.e., selling price less cost of goods from H.O.) of 30% of the sales value.

KP operates from rented premises and leases all other types of fixed assets. The rent and hire charges for these are included in the overhead costs shown in the trial balances.

From the information given below, you are required to prepare for the year ended 31st Dec., 20X1 in columnar form.

- (a) A Profit & Loss account for (i) H.O. (ii) the branch (iii) the entire business.
 (b) Balance Sheet as on 31st Dec., 20X1 for the entire business.

	H.O.		Branch	
	₹	₹	₹	₹
<i>Raw materials purchased</i>	35,000			
<i>Direct wages</i>	1,08,500			
<i>Factory overheads</i>	39,000			
<i>Stock on 1-1-20X1</i>				
<i>Raw materials</i>	1,800			
<i>Finished goods</i>	13,000		9,200	
<i>Debtors</i>	37,000			
<i>Cash</i>	22,000		1,000	
<i>Administrative Salaries</i>	13,900		4,000	
<i>Salesmen Salaries</i>	22,500		6,200	
<i>Other administrative & selling overheads</i>	12,500		2,300	
<i>Inter-unit accounts</i>	5,000			2,000
<i>Capital</i>		50,000		
<i>Sundry Creditors</i>		13,000		
<i>Provision for unrealized profit in stock</i>		1,200		
<i>Sales</i>		2,00,000		65,200
<i>Goods sent to Branch</i>		46,000		
<i>Goods received from H.O.</i>			44,500	
	3,10,200	3,10,200	67,200	67,200

Note:

- (1) On 28th Dec., 20X1 the branch remitted ₹ 1,500 to the H.O. and this has not yet been recorded in the H.O. books. Also, on the same date, the H.O. dispatched goods to the branch invoiced at ₹ 1,500 and these too have not yet been entered into the branch books. It is the company's policy to adjust items in transit in the books of the recipient.
- (2) The stock of raw materials held at the H.O. on 31st Dec., 20X1 was valued at ₹ 2,300.
- (3) You are advised that:
 - there were no stock losses incurred at the H.O. or at the branch.
 - it is KP's practice to value finished goods stock at the H.O. at factory cost.
 - there were no opening or closing stock of work-in-progress.
- (4) Branch employees are entitled to a bonus of ₹ 156 under a bilateral agreement.

Solution

In the books of KP
Trading and Profit & Loss Account for the year ended 31st Dec., 20X1

	H.O.	Branch	Total		H.O.	Branch	Total
	₹	₹	₹		₹	₹	₹
To Opening stock of finished goods	13,000	9,200	22,200	By Sales	2,00,000	65,200	2,65,200
To Material consumed (W.N.1)	34,500	-	34,500				
To Wages	1,08,500	-	1,08,500	By Goods Sent to Branch	46,000	-	-
To Factory Overheads	39,000	-	39,000	By Closing stock including transit (W.N.2)	15,000	9,560 (Bal Fig)	24,560
To Goods from H.O.		46,000					
To Gross Profit c/d (W.N.3)	66,000	19,560	85,560				
	(Bal Fig)						
	2,61,000	74,760	2,89,760		2,61,000	74,760	2,89,760

To Admn. Salaries	13,900	4,000	17,900	By Gross Profit b/d	66,000	19,560	85,560
To Salesmen Salaries	22,500	6,200	28,700				
To Other Admn. & selling Overheads	12,500	2,300	14,800				
To Stock Reserve	47	-	47				
(W.N.4) To Bonus to Staff	-	156	156				
To Net Profit	17,053	6,904	23,957				
	66,000	19,560	85,560				

Balance Sheet as on 31st Dec., 20X1

		₹	H.O. ₹	Branch ₹	Total ₹			H.O. ₹	Branch ₹	Total ₹
Capital			50,000	-	50,000	Fixed Assets		-	-	-
Profit:	H.O.	17,053				Current Assets:				
	Branch	<u>6,904</u>	23,957		23,957	Raw material	2,300			2,300
Trade Creditors			13,000		13,000	Finished Goods	15,000	9,560		23,313*
Bonus Payable				156	156	(Less Stock Res.)				
H.O. Account*				10,404		Debtors	37,000		-	37,000
Stock Reserve (W.N.4)			1,247			Cash (including transit item)	23,500	1,000		24,500
						Branch A/c	10,404**			
			88,204	10,560	87,113		88,204	10,560		87,113

* $9,560 \times 100/115$ i.e., $(8,313 + 15,000) = ₹ 23,313$ or $(15,000 + 9,560) - 1,247$ (Stock reserve)

** $(5,000 + 6,904) - 1500 = ₹ 10,404$.

Working Notes:

(1) Material consumed

$$\begin{aligned} & \text{Opening raw material} + \text{Raw Material Purchased} - \text{Closing raw material} \\ & = 1,800 + 35,000 - 2,300 = 34,500 \end{aligned}$$

- (2) Closing stock at head office
- (a) Calculation of total factor cost = Material consumed + Wages + Factory overhead
 $= 34,500 + 1,08,500 + 39,000 = 1,82,000$
- (b) Cost (factory cost) of goods sold = Sales – Gross profit
 $= 2,00,000 - 2,00,000 \times 30\% = 1,40,000$
- (c) Stock transferred to branch = $46,000 \times 100/115 = 40,000$
- (d) Closing stock = 13,000 (Opening Stock) + 1,82,000 – 1,40,000 – 40,000
 $= 15,000$
- (3) Gross profit of Branch = Sales x Gross profit ratio
 $= 65,200 \times 30\% = 19,560$
- (4) Closing stock reserve = $9,560 \times 15/115 = 1,247$
 Charge to profit and loss = $1,247 - 1,200$ (existing) = 47

Illustration 12

AFFIX of Kolkata has a branch at Delhi to which the goods are supplied from Kolkata but the cost thereof is not recorded in the Head Office books. On 31st March, 20X1 the Branch Balance Sheet was as follows:

Liabilities	₹	Assets	₹
Creditors Balance	40,000	Debtors Balance	2,00,000
Head Office	1,68,000	Building Extension A/c closed by transfer to H.O. A/c	—
		Cash at Bank	8,000
	2,08,000		2,08,000

During the six months ending on 30-9-20X1, the following transactions took place at Delhi.

	₹		₹
Sales	2,40,000	Manager's Salary	4,800
Purchases	48,000	Collections from Debtors	1,60,000
Wages paid	20,000	Discounts allowed	8,000

<i>Salaries (inclusive of advance of ₹ 2,000)</i>	6,400	<i>Discount earned</i>	1,200
<i>General Expenses</i>	1,600	<i>Cash paid to Creditors</i>	60,000
<i>Fire Insurance (paid for one year)</i>	3,200	<i>Building Account (further payment)</i>	4,000
<i>Remittance to H.O.</i>	38,400	<i>Cash in Hand</i>	1,600
		<i>Cash at Bank</i>	28,000

Set out the Head Office Account in Delhi books and the Branch Balance Sheet as on 30-9-20X1. Also give journal entries in the Delhi books.

Solution

Journal Entries

20X1		Dr.		Cr.
30 Sept.		₹		₹
Salary Advance A/c	Dr.	2,000		
To Salaries A/c				2,000
<i>(The amount paid as advance adjusted by debit to Salary Advance Account)</i>				
Prepared Insurance A/c (3,200 x 6/12)	Dr.	1,600		
To Fire Insurance A/c				1,600
<i>(Six months premium transferred to the Prepaid Insurance A/c)</i>				
Head Office Account	Dr.	88,400		
To Purchases A/c				48,000
To Wages A/c				20,000
To Salaries A/c (6,400 – 2,000)				4,400
To General Expenses A/c				1,600
To Fire Insurance A/c (3,200 x 6/12)				1,600
To Manager's Salary A/c				4,800
To Discount Allowed A/c				8,000
<i>(Transfer of various revenue accounts (Dr.) to the H.O. Account for closing the accounts)</i>				

Sales Accounts	Dr.	2,40,000	
Discount Earned A/c	Dr.	1,200	
To Head Office A/c			2,41,200
[Revenue accounts (Cr.) transferred to H.O.]			
Head Office Account	Dr.	4,000	
To Building Account			4,000
(Transfer of amounts spent on building extension to H.O. A/c)			

Head Office Account

20X1		₹	20X1		₹
Sep. 30	To Cash-remittance	38,400	April 1	By Balance b/d	1,68,000
	To Sundries (Revenue A/cs)	88,400	Sep. 30	By Sundries (Revenue A/cs)	2,41,200
	To Building A/c	4,000			
	To Balanced c/d	2,78,400			
		4,09,200			4,09,200

Balance Sheet of Delhi Branch as on Sept. 30, 20X1

Liabilities	₹	Assets	₹
Creditors Balances	26,800	Debtors Balances	2,72,000
Head Office Account	2,78,400	Salary Advance	2,000
		Prepaid Insurance	1,600
		Building Extension A/c transferred to H.O.	—
		Cash in Hand	1,600
		Cash at Bank	28,000
	3,05,200		3,05,200

Cash and Bank Account

	₹		₹
To Balance b/d	8,000	By Wages	20,000
To Collection from Debtors	1,60,000	By Salaries	6,400
		By Insurance	3,200
		By General Exp.	1,600
		By H.O. A/c	38,400
		By Manager's Salary	4,800
		By Creditors	60,000
		By Building A/c	4,000
		By Balance c/d	
		By Cash in Hand	1,600
		By Cash at Bank	28,000
	1,68,000		1,68,000

Debtors Account

	₹		₹
To Balance b/d	2,00,000	By Cash Collection	1,60,000
To Sales	2,40,000	By Discount (allowed)	8,000
		By Balance c/d	2,72,000
	4,40,000		4,40,000
To Balance b/d	2,72,000		

Creditors Account

	₹		₹
To Cash	60,000	By Balance b/d	40,000
To Discount (earned)	1,200	By Purchases	48,000
To Balance c/d	26,800		
	88,000		88,000
		By Balance b/d	26,800

Illustration 13

Ring Bell Ltd. Delhi has a Branch at Bombay where a separate set of books is used. The following is the trial balance extracted on 31st December, 20X1.

Head Office Trial Balance

	₹	₹
Share Capital (Authorised: 10,000 Equity Shares of ₹ 100 each):		
Issued: 8,000 Equity Shares		8,00,000
Profit & Loss Account - 1-1-20X1		25,310
General Reserve		1,00,000
Fixed Assets	5,30,000	
Stock	2,22,470	
Debtors and Creditors	50,500	21,900
Profit for 20X1		52,200
Cash Balance	62,730	
Branch Current Account	1,33,710	
	9,99,410	9,99,410

Branch Trial Balance

	₹	₹
Fixed Assets	95,000	
Profit for 20X1		31,700
Stock	50,460	
Debtors and Creditors	19,100	10,400
Cash Balance	6,550	
Head Office Current Account		1,29,010
	1,71,110	1,71,110

The difference between the balances of the Current Account in the two sets of books is accounted for as follows:

- (a) Cash remitted by the Branch on 31st December, 20X1, but received by the Head Office on 1st January 20X2 - ₹ 3,000.

- (b) *Stock stolen in transit from Head Office and charged to Branch by the Head Office, but not credited to Head Office in the Branch books as the Branch Manager declined to admit any liability (not covered by insurance) - ₹ 1,700.*

Give the Branch Current Account in Head Office books after incorporating Branch Trial Balance through journal.

Solution

The Branch Current Account in the Head Office Books and Head Office Current Account in the Branch Books do not show the same balances. Therefore, in order to reconcile them, the following journal entries will be passed in the Head Office books:

Journal Entries

		Dr.	Cr.
20X1 Dec., 31	Cash in Transit A/c Dr. To Branch Current A/c (Cash sent by the Branch on 31st Dec., 20X1 but received at H.O. on 1st Jan., 20X2)	₹ 3,000	₹ 3,000
	Loss by theft A/c Dr. To Branch Current A/c (Stock lost in transit from H.O. to Branch)	1,700	1,700

In order to incorporate, in the H.O. books, the given Branch trial balance which has been drawn up after preparing the Branch Profit & Loss Account, the following journal entries will be necessary:

Journal Entries

20X1		₹	₹
Dec. 31	Branch Current Account Dr. To Profit & Loss Account (Branch Profit for the year)	31,700	31,700
	Branch Fixed Assets Dr.	95,000	
	Branch Stock Dr.	50,460	
	Branch Debtors Dr.	19,100	

The value of the closing stock will also be adjusted only in head office books.

In such a case, for closing its books at the end of the year, the branch will simply transfer various revenue accounts to the head office without drawing up a Trading and Profit & Loss Account.

On that basis, supplemented by the record of transactions maintained at the head office, it will be possible to construct the Trading and Profit & Loss Account of the branch.

Illustration 14

Messrs Ramchand & Co., Hyderabad has a branch in Delhi. The Delhi Branch deals not only in the goods from Head Office but also buys some auxiliary goods and deals in them. They, however, do not prepare any Profit & Loss Account but close all accounts to the Head Office at the end of the year and open them afresh on the basis of advice from their Head Office. The fixed assets accounts are also maintained at the Head Office.

The goods from the Head Office are invoiced at selling prices to give a profit of 20 per cent on the sale price. The goods sent from the branch to Head Office are at cost. From the following prepare Branch Trading and Profit & Loss Account and Branch fixed Assets Account in the Head Office Books.

Trial Balance of the Delhi Branch as on 31-12-20X1

Debit	₹	Credit	₹
Head office opening balance on 1-1-20X1	15,000	Sales	1,00,000
Goods from H.O.	50,000	Goods to H.O.	3,000
Purchases	20,000	Head Office Current A/c	15,000
Opening Stock		Sundry Creditors	3,000
(H.O. supplies goods at invoice prices)	4,000		
Opening Stock of other goods	500		
Salaries	7,000		

Rent	3,000		
Office expenditure	2,000		
Cash on Hand	500		
Cash at Bank	4,000		
Sundry Debtors	15,000		
	1,21,000		1,21,000

The Branch balances as on 1st January, 20X1, were as under: Furniture ₹ 5,000; Sundry Debtors ₹ 9,500; Cash ₹ 1,000, Creditors ₹ 30,000. The closing stock at branch of the head office goods at invoice price is ₹ 3,000 and that of purchased goods at cost is ₹ 1,000. Depreciation is to be provided at 10 per cent on branch assets.

Solution

Delhi Branch Trading and Profit & Loss Account for the year ended 31st Dec., 20X1

		₹			₹
To Opening Stock:			By Sales		1,00,000
Head office Goods	3,200		By Goods from Branch		3,000
(4,000 x 80%)			By Closing Stock:		
Others	<u>500</u>	3,700	Head Office goods	2,400	
			(3,000 x 80%)		
To Goods to Branch		40,000	Others	1,000	3,400
(50,000 x 80%)					
To Purchases		20,000			
To Gross Profit c/d		42,700			
		1,06,400			1,06,400

To Salaries		7,000	By Gross profit b/d		42,700
To Rent		3,000			
To Office Expenses		2,000			
To Dep. on furniture @ 10%		500			
To Net profit		30,200			
		42,700			42,700

Branch (Fixed) Assets Account (In Head Office Books)

20X1			₹	20X1			₹
Jan. 1	To	Balance b/d	5,000	Dec. 31	By	Delhi Branch A/c (Depreciation)	500
					By	Balance c/d	4,500
			5,000				5,000
20X2							
Jan. 1	To	Balance b/d	4,500				

Note: Furniture A/c is maintained in Head office books; it is not a part of either opening or closing balance.

10. FOREIGN BRANCHES

Foreign branches generally maintain independent and complete record of business transacted by them in currency of the country in which they operate. Thus, problems of incorporating balances of foreign branches relate mainly to translation of foreign currency into Indian rupees. This is because exchange rate of Indian rupee is not stable in relation to foreign currencies due to international demand and supply effects on various currencies. The accounting principles which apply to inland branches also apply to a foreign branch after converting the trial balance of the foreign branch in the Indian currency.



11. ACCOUNTING FOR FOREIGN BRANCHES

For the purpose of accounting, AS 11 (revised 2003) classifies the foreign branches may be classified into two types:

- Integral Foreign Operation;
- Non- Integral Foreign Operation.

Let us discuss these two types of foreign branches in detail.

11.1. Integral Foreign Operation (IFO)

It is a foreign operation, the activities of which are an integral part of those of the reporting enterprise. The business of IFO is carried on as if it were an extension of the reporting enterprise's operations. For example, sale of goods imported from the reporting enterprise and remittance of proceeds to the reporting enterprise.

11.2. Non-Integral Foreign Operation (NFO)

It is a foreign operation that is not an Integral Foreign Operation. The business of a NFO is carried on in a substantially independent way by accumulating cash and other monetary items, incurring expenses, generating income and arranging borrowing in its local currency. An NFO may also enter into transactions in foreign currencies, including transactions in the reporting currency. An example of NFO may be production in a foreign currency out of the resources available in such country independent of the reporting enterprise.

The following are the indicators of Non- Integral Foreign Operation-

- *Control by reporting enterprises* - While the reporting enterprise may control the foreign operation, the activities of foreign operation are carried independently without much dependence on reporting enterprise.
- Transactions with the reporting enterprises are not a high proportion of the foreign operation's activities.
- Activities of foreign operation are mainly financed by its operations or from local borrowings. In other words, it raises finance independently and is in no way dependent on reporting enterprises.

- Foreign operation sales are mainly in currencies other than reporting currency.
- All the expenses by foreign operations are primarily paid in local currency, not in the reporting currency.
- Day-to-day cash flow of the reporting enterprises is independent of the foreign enterprises cash flows.
- Sales prices of the foreign enterprises are not affected by the day-to-day changes in exchange rate of the reporting currency of the foreign operation.
- There is an active sales market for the foreign operation product.

The above are only indicators and not decisive/conclusive factors to classify the foreign operations as non-integral, much will depend on factual information, situations of the particular case and, therefore, judgment is necessary to determine the appropriate classification.

Controversies may arise in deciding the foreign branches of the enterprises into integral or non-integral. However, there may not be any controversy that subsidiary associates and joint ventures are non-integral foreign operation.

In case of branches classified as independent for the purpose of accounting are generally classified as non-integral foreign operations.



12. TECHNIQUES FOR FOREIGN CURRENCY TRANSLATION

12.1 Integral Foreign Operation (IFO)

Following are the standard recommendations for foreign currency translation:

- (1) All transactions of IFO be translated at the rate prevailing on the date of transaction. This will require date wise details of the transaction entered by that operation together with the rates. Weekly or monthly average rate is permitted if there are no significant variations in the rate.

- (2) Translation at the balance sheet date-
- (i) Monetary items¹ at closing rate;
 - (ii) Non-monetary items²: The cost and depreciation of the tangible fixed assets is translated using the exchange rate at the date of purchase of the asset if asset is carried at cost. If tangible fixed asset is carried at fair value, translation should be done using the rate existed on the date of the valuation.
 - (iii) The cost of inventories is translated at the exchange rates that existed when the cost of inventory was incurred and realizable value is translated applying exchange rate when realizable value is determined which is generally closing rate.
 - (iv) Exchange difference arising on the translation of the financial statement of integral foreign operation should be charged to profit and loss account.

12.2 Non-Integral Foreign Operation

Accounts of non-integral foreign operation are translated using the following principles:

- Balance sheet items i.e. Assets and Liabilities both monetary and non-monetary – apply closing exchange rate.
- Items of income and expenses – At actual exchange rates on the date of transactions. However, accounting standard allows average rate subject to materiality.
- Resulting exchange rate difference should be accumulated in a “foreign currency translation reserve” until the disposal of “net investment in non-integral foreign operation”.

¹ *Monetary items are money held and assets and liabilities to be received or paid in fixed or determinable amounts of money. Cash, receivables and payables are examples of monetary items.*

² *Non-monetary items are assets and liabilities other than monetary items. Fixed assets, investments in equity shares, inventories are examples of non-monetary assets.*

Items	Integral Foreign Operations	Non Integral Foreign Operations
Monetary Items (Cash, Bank Balance, Debtor, Creditor, Loans, Bills receivable, Bills Payable)	Closing rate	Closing rate
Non-Monetary Items (Fixed Assets)	Rate on date of purchase	Closing rate
Inventory	Generally, closing rate (but if rate on the date of purchase of inventory is available, then that rate)	Closing rate
Profit and Loss items (revenue items)	Average rate (but if rate on the date of transaction is available, then that rate)	Average rate (but if rate on the date of transaction is available, then that rate)
Exchange Difference	Charge to P&L account.	Accumulated in Foreign Currency Translation reserve.



13. CHANGE IN CLASSIFICATION

When there is a change in classification, accounting treatment is as under-

13.1 Integral to Non-Integral

- (i) Translation procedure applicable to non-integral shall be followed from the date of change.

- (ii) Exchange difference arising on the translation of non-monetary assets at the date of re-classification is accumulated in foreign currency translation reserve.

13.2 Non-Integral to Integral

- (i) Translation procedure as applicable to integral should be applied from the date of change.
- (ii) Translated amount of non-monetary items at the date of change is treated as historical cost.
- (iii) Exchange difference lying in foreign currency translation reserve is not to be recognized as income or expense till the disposal of the operation even if the foreign operation becomes integral.

Illustration 15

On 31st December, 20X2 the following balances appeared in the books of Chennai Branch of an English firm having its HO office in New York:

	Amount in ₹	Amount in ₹
Stock on 1st Jan., 20X2	2,34,000	
Purchases and Sales	15,62,500	23,43,750
Debtors and Creditors	7,65,000	5,10,000
Bills Receivable and Payable	2,04,000	1,78,500
Salaries and Wages	1,00,000	-
Rent, Rates and Taxes	1,06,250	-
Furniture	91,000	-
Bank A/c	5,68,650	
New York Account	-	5,99,150
	36,31,400	36,31,400

Stock on 31st December, 20X2 was ₹6,37,500.

Branch account in New York books showed a debit balance of \$ 13,400 on 31st December, 20X2 and Furniture appeared in the Head Office books at \$ 1,750.

The rate of exchange for 1 \$ on 31st December, 20X1 was ₹ 52 and on 31st December, 20X2 was ₹ 51. The average rate for the year was ₹ 50.

Prepare in the Head Office books the Profit and Loss a/c and the Balance Sheet of the Branch assuming integral foreign operation.

Solution

**In the books of English Firm (Head Office in New York)
Chennai Branch Profit and Loss Account
for the year ended 31st December, 20X2**

	\$		\$
To Opening stock	4,500	By Sales	46,875
To Purchases	31,250	By Closing stock	12,500
To Gross profit c/d	23,625	(6,37,500 / 51)	
	59,375		59,375
To Salaries	2,000	By Gross profit b/d	23,625
To Rent, rates and taxes	2,125		
To Exchange translation loss	2,000		
To Net Profit c/d	17,500		
	23,625		23,625

**Balance Sheet of Chennai Branch
as on 31st December, 20X2**

Liabilities	\$	\$	Assets	\$
Head Office A/c	13,400		Furniture	1,750
Add: Net profit	<u>17,500</u>	30,900	Closing Stock	12,500
Trade creditors		10,000	Trade Debtors	15,000
Bills Payable		3,500	Bills Receivable	4,000
			Cash at bank	11,150
		44,400		44,400

Working Note:

**Calculation of Exchange Translation Loss
Chennai Branch Trial Balance (converted in \$)
as on 31st December, 20X2**

	Dr. ₹	Cr. ₹	Conversion Rate	Dr. (\$)	Cr. (\$)
Stock on 1st Jan., 20X2	2,34,000		52	4,500	
Purchases & Sales	15,62,500	23,43,750	50	31,250	46,875
Debtors & creditors	7,65,000	5,10,000	51	15,000	10,000
Bills Receivable and Bills Payable	2,04,000	1,78,500	51	4,000	3,500
Salaries and wages	1,00,000		50	2,000	
Rent, Rates and Taxes	1,06,250		50	2,125	
Furniture	91,000			1,750	
Bank A/c	5,68,650		51	11,150	
New York Account		5,99,150			13,400
Exchange translation loss (bal. fig.)				2,000	
	36,31,400	36,31,400		73,775	73,775

Illustration 16

S & M Ltd., Bombay, have a branch in Sydney, Australia. Sydney branch is an integral foreign operation of S & M Ltd.

At the end of 31st March, 20X2, the following ledger balances have been extracted from the books of the Bombay Office and the Sydney Office:

	Bombay (₹ thousands)		Sydney (Austr dollars thousands)	
	<i>Debit</i>	<i>Credit</i>	<i>Debit</i>	<i>Credit</i>
<i>Share Capital</i>	–	2,000	–	–
<i>Reserves & Surplus</i>	–	1,000	–	–
<i>Land</i>	500	–	–	–
<i>Buildings (Cost)</i>	1,000	–	–	–
<i>Buildings Dep. Reserve</i>	–	200	–	–
<i>Plant & Machinery (Cost)</i>	2,500	–	200	–
<i>Plant & Machinery Dep. Reserve</i>	–	600	–	130
<i>Debtors / Creditors</i>	280	200	60	30
<i>Stock (1.4.20X1)</i>	100	–	20	–
<i>Branch Stock Reserve</i>	–	4	–	–
<i>Cash & Bank Balances</i>	10	–	10	–
<i>Purchases / Sales</i>	240	520	20	123
<i>Goods sent to Branch</i>	–	100	5	–
<i>Managing Director's salary</i>	30	–	–	–
<i>Wages & Salaries</i>	75	–	45	–
<i>Rent</i>	–	–	12	–
<i>Office Expenses</i>	25	–	18	–
<i>Commission Receipts</i>	–	256	–	100
<i>Branch / H.O. Current A/c</i>	120	–	–	7
	4,880	4,880	390	390

The following information is also available:

(1) Stock as at 31.3.20X2:

Bombay ₹ 1,50,000

Sydney A \$ 3,125

You are required to convert the Sydney Branch Trial Balance into rupees;

Use the following rates of exchange :

Opening rate A \$ = ₹ 20

Closing rate A \$ = ₹ 24

Average rate A \$ = ₹ 22

For Fixed Assets A \$ = ₹ 18

Solution

Sydney Branch Trial Balance (in Rupees) As on 31st March, 20X2

(₹ '000)

Conversion	Rate per A\$	Dr.	Cr.
Plant & Machinery (cost)	₹ 18	36,00	
Plant & Machinery Dep. Reserve	₹ 18		23,40
Debtors / Creditors	₹ 24	14,40	7,20
Stock (1.4.20X1)	₹ 20	4,00	
Cash & Bank Balances	₹ 24	2,40	
Purchase / Sales	₹ 22	4,40	27,06
Goods received from H.O.	–	1,00	
Wages & Salaries	₹ 22	9,90	
Rent	₹ 22	2,64	
Office expenses	₹ 22	3,96	
Commission Receipts	₹ 22		22,00
H.O. Current A/c			1,20
		78,70	80,86
Exchange loss (balancing figure)		2,16	
		80,86	80,86

Illustration 17

M/s Carlin has head office at New York (U.S.A.) and branch at Mumbai (India). Mumbai branch is an integral foreign operation of Carlin & Co.

Mumbai branch furnishes you with its trial balance as on 31st March, 20X2 and the additional information given thereafter:

	Dr.	Cr.
	Rupees in thousands	
Stock on 1st April, 20X1	300	–
Purchases and sales	800	1,200
Sundry Debtors and creditors	400	300
Bills of exchange	120	240
Wages and salaries	560	–
Rent, rates and taxes	360	–
Sundry charges	160	–
Computers	240	
Bank balance	420	–
New York office a/c	–	1,620
	3,360	3,360

Additional information:

- (a) Computers were acquired from a remittance of US \$ 6,000 received from New York head office and paid to the suppliers. Depreciate computers at 60% for the year.
- (b) Unsold stock of Mumbai branch was worth ₹ 4,20,000 on 31st March, 20X2.
- (c) The rates of exchange may be taken as follows:
 - on 1.4.20X1 @ ₹ 40 per US \$
 - on 31.3.20X2 @ ₹ 42 per US \$
 - average exchange rate for the year @ ₹ 41 per US \$
 - conversion in \$ shall be made upto two decimal accuracy.

You are asked to prepare in US dollars the revenue statement for the year ended 31st March, 20X2 and the balance sheet as on that date of Mumbai branch as would appear in the books of New York head office of Carlin & Co. You are informed that Mumbai branch account showed a debit balance of US \$ 39609.18 on 31.3.20X2 in New York books and there were no items pending reconciliation.

Solution

M/s Carlin
Mumbai Branch Trial Balance in (US \$)
as on 31st March, 20X2

	Conversion	Dr.	Cr.
	rate per US \$	US \$	US \$
	(₹)		
Stock on 1.4.X1	40	7,500.00	–
Purchases and sales	41	19,512.20	29,268.29
Sundry debtors and creditors	42	9,523.81	7,142.86
Bills of exchange	42	2,857.14	5,714.29
Wages and salaries	41	13,658.54	–
Rent, rates and taxes	41	8,780.49	–
Sundry charges	41	3,902.44	–
Computers	–	6,000.00	–
Bank balance	42	10,000.00	–
New York office A/c	–	–	39,609.18
		81,734.62	81,734.62

**Trading and Profit & Loss Account
for the year ended 31st March, 20X2**

	US \$		US \$
To Opening Stock	7,500.00	By Sales	29,268.29
To Purchases	19,512.20	By Closing stock	10,000.00
		(4,20,000/42)	
To Wages and salaries	<u>13,658.54</u>	By Gross Loss c/d	<u>1,402.45</u>
	<u>40,670.74</u>		<u>40,670.74</u>
To Gross Loss b/d	1,402.45	By Net Loss	17,685.38
To Rent, rates and taxes	8,780.49		
To Sundry charges	3,902.44		
To Depreciation on computers (US \$ 6,000 × 0.6)	3,600.00		
	<u>17,685.38</u>		<u>17,685.38</u>

**Balance Sheet of Mumbai Branch
as on 31st March, 20X2**

Liabilities		US \$	Assets		US \$	US \$
New York Office A/c	39,609.18		Computers	6,000.00		
Less: Net Loss	(17,685.38)	21,923.80	Less: Depreciation	(3,600.00)	2,400.00	
Sundry creditors		7,142.86	Closing stock		10,000.00	
Bills payable		5,714.29	Sundry debtors		9,523.81	
			Bank balance		10,000.00	
			Bills receivable		2,857.14	
		<u>34,780.95</u>			<u>34,780.95</u>	

SUMMARY

- **Types of branches**
 - Dependent branches
 - Independent branches
- **Classification of Branches from accounting point of view**
 - Branches in respect of which the whole of the accounting records are kept at the head office (Dependent Branches)
 - Branches which maintain independent accounting records (Independent Branches), and
 - Foreign Branches.
- **Systems of accounting followed by Dependent Branches**
 - Debtors System: under this system head office makes a branch account. Anything given to branch is debited and anything received from branch would be credited.
 - Branch trading and profit and loss account (Final accounts) method/branch account method: Under this system head office prepares (a) profit and loss account (b) branch account taking each branch as a separate entity.
 - Stock and debtors system: Under this system head office opens:
 - Branch Stock Account
 - Branch Profit and Loss Account
 - Branch Debtors Account
 - Branch Expenses Account
 - Goods sent to Branch Account
 - Branch Asset Account
- **Maintenance of comprehensive account books by Independent Branches** Preparation of separate trial balance of each branch in H.O. books.

- **Types of Foreign branches**

- Integral Foreign Operation (IFO): It is a foreign operation, the activities of which are an integral part of those of the reporting enterprise.
- Non-Integral Foreign Operation (NFO): It is a foreign operation that is not an Integral Foreign Operation. The business of a NFO is carried on in a substantially independent way by accumulating cash and other monetary items, incurring expenses, generating income and arranging borrowing in its local currency.

- **Non-Integral Foreign Operation -translation**

- Balance sheet items i.e. Assets and Liabilities both monetary and non-monetary – apply closing exchange rate.
- Items of income and expenses – At actual exchange rates on the date of transactions
- Resulting exchange rate difference should be accumulated in a “foreign currency translation reserve” until the disposal of “net investment in non-integral foreign operation”.

- **Integral Foreign Operation (IFO) - translation**

- All transactions at the rate prevailing on the date of transaction
Translation at the balance sheet date-
- Monetary items at closing rate;
- Non-monetary items: The cost and depreciation of the tangible fixed assets is translated using the exchange rate at the date of purchase of the asset if asset is carried at cost. If tangible fixed asset is carried at fair value, translation should be done using the rate existed on the date of the valuation.
- The cost of inventories is translated at the exchange rates that existed when the cost of inventory was incurred and realizable value is translated applying exchange rate when realizable value is determined which is generally closing rate.
- Exchange difference arising on the translation of the financial statement of integral foreign operation should be charged to profit and loss account.

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *If goods are invoiced to branches at cost, trading results of branch can be ascertained by*
 - (a) *Debtors method.*
 - (b) *Stock and debtors method.*
 - (c) *Either (a) or (b).*
 - (d) *Both (a) and (b).*
2. *Under branch trading and profit loss account method*
 - (a) *H.O prepares profit and loss account.*
 - (b) *Each branch is treated separate entity.*
 - (c) *Both (a) and (b).*
 - (d) *Either (a) or (b).*
3. *Goods may be invoiced to branch at*
 - (a) *Cost or Selling price.*
 - (b) *Wholesale price.*
 - (c) *Both (a) and (b).*
 - (d) *Either (a) or (b).*
4. *Under debtors method, opening balance of debtors is*
 - (a) *Debited to branch account.*
 - (b) *Credited to branch account.*
 - (c) *Debited to H.O account.*
 - (d) *Credited to H.O account.*
5. *Cost of goods returned by branch will have the following effect*
 - (a) *Goods sent to branch account will be debited.*
 - (b) *Branch stock account will be credited.*
 - (c) *Both (a) and (b).*
 - (d) *Either (a) or (b).*

Theoretical Questions

6. *Why goods are marked on invoice price by the head office while sending goods to the branch?*
7. *Differentiate Branch Accounts with Departmental accounts.*

Scenario based Questions

8. *Goods worth ₹ 50,000 sent by head office but the branch has received till the closing date goods for worth ₹ 40,000 only. Give journal entry in the books of H.O. and branch for goods in transit.*
9. *Alphs having head office in Mumbai has a branch in Nagpur. The branch at Nagpur is an independent branch maintaining separate books of account. On 31.3.20X1, it was found that the goods dispatched by head office for ₹ 2,00,000 was received by the branch only to the extent of ₹ 1,50,000. The balance goods are in transit. What is the accounting entry to be passed by the branch for recording the goods in transit, in its books?*
10. *Show adjustment journal entry in the books of head office at the end of April, 20X1 for incorporation of inter-branch transactions assuming that only head office maintains different branch accounts in its books.*
 - A. *Delhi branch:*
 - (1) *Received goods from Mumbai – ₹ 35,000 and ₹ 15,000 from Kolkata.*
 - (2) *Sent goods to Chennai – ₹ 25,000, Kolkata – ₹ 20,000.*
 - (3) *Bill Receivable received – ₹ 20,000 from Chennai.*
 - (4) *Acceptances sent to Mumbai – ₹ 25,000, Kolkata – ₹ 10,000.*
 - B. *Mumbai Branch (apart from the above) :*
 - (5) *Received goods from Kolkata – ₹ 15,000, Delhi – ₹ 20,000.*
 - (6) *Cash sent to Delhi – ₹ 15,000, Kolkata – ₹ 7,000.*
 - C. *Chennai Branch (apart from the above) :*
 - (7) *Received goods from Kolkata – ₹ 30,000.*

(8) *Acceptances and Cash sent to Kolkata – ₹ 20,000 and ₹10,000 respectively.*

D. *Kolkata Branch (apart from the above) :*

(9) *Sent goods to Chennai – ₹ 35,000.*

(10) *Paid cash to Chennai – ₹15,000.*

(11) *Acceptances sent to Chennai – ₹15,000.*

11. *Give Journal Entries in the books of Branch A to rectify or adjust the following:*

(i) *Head Office expenses ₹ 3,500 allocated to the Branch, but not recorded in the Branch Books.*

(ii) *Depreciation of branch assets, whose accounts are kept by the Head Office not provided earlier for ₹ 1,500.*

(iii) *Branch paid ₹ 2,000 as salary to a H.O. Inspector, but the amount paid has been debited by the Branch to Salaries account.*

(iv) *H.O. collected ₹ 10,000 directly from a customer on behalf of the Branch, but no intimation to this effect has been received by the Branch.*

(v) *A remittance of ₹ 15,000 sent by the Branch has not yet been received by the Head Office.*

(vi) *Branch A incurred advertisement expenses of ₹ 3,000 on behalf of Branch B.*

12. *Widespread invoices goods to its branch at cost plus 20%. The branch sells goods for cash as well as on credit. The branch meets its expenses out of cash collected from its debtors and cash sales and remits the balance of cash to head office after withholding ₹ 10,000 necessary for meeting immediate requirements of cash. On 31st March, 20X1 the assets at the branch were as follows:*

	₹ ('000)
<i>Cash in Hand</i>	10
<i>Trade Debtors</i>	384
<i>Stock, at Invoice Price</i>	1,080
<i>Furniture and Fittings</i>	500

During the accounting year ended 31st March, 20X2 the invoice price of goods dispatched by the head office to the branch amounted to ₹ 1 crore 32 lakhs. Out of the goods received by it, the branch sent back to head office goods invoiced at ₹ 72,000. Other transactions at the branch during the year were as follows:

	(₹ '000)
Cash Sales	9,700
Credit Sales	3,140
Cash collected by Branch from Credit Customers	2,842
Cash Discount allowed to Debtors	58
Returns by Customers	102
Bad Debts written off	37
Expenses paid by Branch	842

On 1st January, 20X2 the branch purchased new furniture for ₹ 1 lakh for which payment was made by head office through a cheque.

On 31st March, 20X2 branch expenses amounting to ₹ 6,000 were outstanding and cash in hand was again ₹ 10,000. Furniture is subject to depreciation @ 16% per annum on diminishing balance method.

Prepare Branch Account in the books of head office for the year ended 31st March, 20X2.

13. *On 31st March, 20X2 Kanpur Branch submits the following Trial Balance to its Head Office at Lucknow :*

Debit Balances	₹ in lacs
Furniture and Equipment	18
Depreciation on furniture	2
Salaries	25
Rent	10
Advertising	6
Telephone, Postage and Stationery	3

<i>Sundry Office Expenses</i>	1
<i>Stock on 1st April, 20X1</i>	60
<i>Goods Received from Head Office</i>	288
<i>Debtors</i>	20
<i>Cash at bank and in hand</i>	8
<i>Carriage Inwards</i>	7
	448
<i>Credit Balances</i>	
<i>Outstanding Expenses</i>	3
<i>Goods Returned to Head Office</i>	5
<i>Sales</i>	360
<i>Head Office</i>	80
	448

Additional Information:

Stock on 31st March, 20X2 was valued at ₹ 62 lacs. On 29th March, 20X2 the Head Office dispatched goods costing ₹ 10 lacs to its branch. Branch did not receive these goods before 1st April, 20X2. Hence, the figure of goods received from Head Office does not include these goods. Also, the head office has charged the branch ₹ 1 lac for centralized services for which the branch has not passed the entry.

You are required to:

- (i) Pass Journal Entries in the books of the Branch to make the necessary adjustments
 - (ii) Prepare Final Accounts of the Branch including Balance Sheet, and
 - (iii) Pass Journal Entries in the books of the Head Office to incorporate the whole of the Branch Trial Balance.
14. M/s Marena, Delhi has a branch at Bangalore to which office goods are invoiced at cost plus 25%. The branch sells both for cash and on credit.

Branch Expenses are paid direct from head office and the Branch has to remit all cash received into the Head Office Bank Account.

From the following details, relating to calendar year 20X1, prepare the accounts in the Head Office Ledger and ascertain the Branch Profit under Stock and Debtors Method'.

Branch does not maintain any books of account, but sends weekly returns to the Head Office.

	₹
Goods received from Head Office at invoice price	45,00,000
Returns to Heads Office at invoice price	90,000
Stock at Bangalore as on 1st January, 20X1	4,50,000
Sales during the year - Cash	15,00,000
- Credit	27,00,000
Sundry Debtors at Bangalore as on 1st January, 20X1	5,40,000
Cash received from Debtors	24,00,000
Discount allowed to Debtors	45,000
Bad Debts in the year	30,000
Sales returns at Bangalore Branch	60,000
Rent, Rates and Taxes at Branch	1,35,000
Salaries, Wages and Bonus at Branch	4,50,000
Office Expenses	45,000
Stock at Branch on 31st December, 20X1 at invoice price	9,00,000

15. *Beta, having head office at Mumbai has a branch at Nagpur. The head office does wholesale trade only at cost plus 80%. The goods are sent to branch at the wholesale price viz., cost plus 80%. The branch at Nagpur is wholly engaged in retail trade and the goods are sold at cost to H.O. plus 100%.*

Following details are furnished for the year ended 31st March, 20X1:

	Head Office (₹)	Branch (₹)
Opening stock	2,25,000	
Purchases	25,50,000	

Goods sent to branch (Cost to H.O. plus 80%)	9,54,000	
Sales	27,81,000	9,50,000
Office expenses	90,000	8,500
Selling expenses	72,000	6,300
Staff salary	65,000	12,000

You are required to prepare Trading and Profit and Loss Account of the head office and branch for the year ended 31st March, 20X1.

16. Pass necessary Journal entries in the books of an independent Branch of a business entity to rectify or adjust the following:
- Income of ₹ 2,800 allocated to the Branch by Head Office but not recorded in the Branch books.
 - Branch paid ₹3,000 as salary to a Head Office Manager, but the amount paid has been debited by the Branch to Salaries Account.
 - Branch incurred travelling expenses of ₹5,000 on behalf of other Branches, this was not recorded in the books of Branch.
 - A remittance of ₹ 1,50,000 sent by the Branch has not received by Head Office on the date of reconciliation of Accounts.
 - Head Office allocates ₹75,000 to the Branch as Head Office expenses, which has not yet been recorded by the Branch.
 - Head Office collected ₹30,000 directly from a Branch Customer. The intimation of the fact has been received by the Branch only now, not recorded till now.
 - Goods dispatched by the Head office amounting to ₹10,000, but not received by the Branch till date of reconciliation. The Goods have been received subsequently.
17. The Washington branch of XYZ Mumbai sent the following trial balance as on 31st December, 20X1:

	\$	\$
Head office A/c	–	22,800
Sales	–	84,000

Debtors and creditors	4,800	3,400
Machinery	24,000	-
Cash at bank	1,200	-
Stock, 1 January, 20X1	11,200	-
Goods from H.O.	64,000	-
Expenses	5,000	-
	1,10,200	1,10,200

In the books of head office, the Branch A/c stood as follows:

Washington Branch A/c

		₹			₹
To	Balance b/d	8,10,000	By	Cash	28,76,000
To	Goods sent to branch	<u>29,26,000</u>	By	Balance c/d	<u>8,60,000</u>
		<u>37,36,000</u>			<u>37,36,000</u>

Goods are sent to the branch at cost plus 10% and the branch sells goods at invoice price plus 25%. Machinery was acquired in past, when \$ 1.00 = ₹ 40.

Rates of exchange were:

1 st January, 20X1	\$ 1.00	=	₹ 46
31 st December, 20X1	\$ 1.00	=	₹ 48
Average	\$ 1.00	=	₹ 47

Machinery is depreciated @ 10% and the branch manager is entitled to a commission of 5% on the profits of the branch.

You are required to:

- (i) Prepare the Branch Trading & Profit & Loss A/c in dollars.
- (ii) Convert the Trial Balance of branch into Indian currency and prepare Branch Trading & Profit and Loss A/c and the Branch A/c in the books of head office.

ANSWERS/HINTS

Answer to the Multiple Choice Questions

1.	(c)	2.	(c)	3.	(c)	4.	(a)	5.	(c)		
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Answer to the Theoretical Questions

6. Goods are marked on invoice price to achieve the following objectives:
- To keep secret from the branch manager, the cost price of the goods and profit made, so that the branch manager may not start a rival and competitive business with the concern; and
 - To have effective control on stock i.e. stock at any time must be equal to opening stock plus goods received from head office minus sales made at branch.
 - To dictate pricing policy to its branches, as well as save work at branch because prices have already been decided.
7. Branch accounts may be maintained either at branch or at head office and no allocation problem arises since the expenses in respect of each branch can be identified. However, Departmental accounts are maintained at one place only. Common expenses are distributed among the departments concerned on some equitable basis considered suitable in the case. For details, refer Para 2 of the Chapter to know the differences.

Answer to Scenario based Questions

8. **Journal entry in the books of Head Office**
No entry
Journal entry in the books of Branch

		₹	₹
Goods-in-transit account	Dr.	10,000	
To Head Office account			10,000
(Being goods sent by head office is still in transit)			

9.

Nagpur branch must include the inventory in its books as goods in transit.

The following journal entry must be made by the branch:

Goods in transit A/c	Dr.	50,000	
To Head office A/c			50,000

[Being Goods sent by Head office is still in transit on the closing date]

10.

Journal entry in the books of Head Office

Date	Particulars	Dr.	Cr.
		₹	₹
30th April, 20X1	Mumbai Branch Account Dr.	3,000	
	Chennai Branch Account Dr.	70,000	
	To Delhi Branch Account		15,000
	To Kolkata Branch Account		58,000
	(Being adjustment entry passed by head office in respect of inter-branch transactions for the month of April, 20X1)		

Working Note:

Inter – Branch transactions

	<i>Delhi</i>	<i>Mumbai</i>	<i>Chennai</i>	<i>Kolkata</i>
	₹	₹	₹	₹
A. Delhi Branch				
(1) Received goods	50,000 (Dr.)	35,000 (Cr.)		15,000 (Cr.)
(2) Sent goods	45,000 (Cr.)		25,000 (Dr.)	20,000 (Dr.)

(3) Received Bills receivable	20,000 (Dr.)		20,000 (Cr.)	
(4) Sent acceptance	35,000 (Cr.)	25,000 (Dr.)		10,000 (Dr.)
B. Mumbai Branch				
(5) Received goods	20,000 (Cr.)	35,000 (Dr.)		15,000 (Cr.)
(6) Sent cash	15,000 (Dr.)	22,000 (Cr.)		7,000 (Dr.)
C. Chennai Branch				
(7) Received goods			30,000 (Dr.)	30,000 (Cr.)
(8) Sent cash and acceptances			30,000 (Cr.)	30,000 (Dr.)
D. Kolkata Branch				
(9) Sent goods			35,000 (Dr.)	35,000 (Cr.)
(10) Sent cash			15,000 (Dr.)	15,000 (Cr.)
(11) Sent acceptances			15,000 (Dr.)	15,000 (Cr.)
	15,000 (Cr.)	3,000 (Dr.)	70,000 (Dr.)	58,000 (Cr.)

11.

Books of Branch A
Journal Entries

	Particulars		Dr. Amount ₹	Cr. Amount ₹
(i)	Expenses account To Head office account (Being the allocated expenditure by the head office recorded in branch books)	Dr.	3,500	3,500
(ii)	Depreciation account To Head office account (Being the depreciation provided)	Dr.	1,500	1,500
(iii)	Head office account	Dr.	2,000	

	To Salaries account (Being the rectification of salary paid on behalf of H.O.)			2,000
(iv)	Head office account	Dr.	10,000	
	To Debtors account (Being the adjustment of collection from branch debtors)			10,000
(v)	No entry in branch books			
(vi)	Head Office account	Dr.	3,000	
	To Cash account (Being the expenditure on account of Branch B, recorded in books)			3,000

Note: Entry (vi) Inter branch transactions are routed through Head Office.

12.

**In the Head Office Books
Branch Account
for the year ended 31st March, 20X2**

	₹ '000		₹'000
To Balance b/d		By Balance b/d	
Cash in hand	10	Stock reserve ₹ 1,080 × $\frac{1}{6}$	180
Trade debtors	384		
Stock	1,080	By Goods sent to branch	72
Furniture and fittings	500	A/c (Returns to H.O.)	
To Goods sent to branch	13,200	By Goods sent to branch	2,188
A/c	100	A/c (Loading on net	
To Bank A/c (Payment for furniture)	245	goods sent to branch –	
To Balance c/d		$\left(13,128 \times \frac{1}{6}\right)$	
Stock reserve $\left(1,470 \times \frac{1}{6}\right)$		By Bank A/c (Remittance from branch to H.O.)	11,700
		(W.N.5)	

To Net profit transferred to General P/L account	1,096	By Balance c/d	
To Balance c/d - Outstanding expenses	6	Cash in hand	10
		Trade debtors (W.N.3)	485
		Stock (W.N.1)	1,470
		Furniture and fittings (W.N.4)	516
	16,621		16,621

Working Notes:**1. Invoice price and cost**

Let cost be	100
So, invoice price	120
Loading	20
Loading: Invoice price = 20 : 120	= 1 : 6

2. Memorandum Branch Stock Account

	₹ '000		₹ '000
To Balance b/d	1,080	By Goods sent to branch	72
To Goods sent to branch	13,200	By Branch Cash	9,700
To Branch debtors	102	By Branch debtors	3,140
		By Balance c/d	1,470
	14,382		14,382

3. Memorandum Branch Debtors Account

	₹ '000		₹ '000
To Balance b/d	384	By Branch cash	2,842
To Branch stock	3,140	By Branch expenses discount	58
		By Branch stock (Returns)	102
		By Branch expenses	

		(Bad debts)	37
		By Balance b/d	485
	3,524		3,524

4. Memorandum Branch Furniture and Fittings Account

	₹ '000		₹ '000
To Balance b/d	500	By Depreciation [(500x16%) + (100 x 16% x 3/12)]	84
To Bank	100	By Balance c/d	516
	600		600

Note: Since the new furniture was purchased on 1st Jan 20X2 depreciation will be for 3 months.

5. Memorandum Branch Cash Account

	₹ '000		₹ '000
To Balance b/d	10	By Branch expenses	842
To Branch stock	9,700	By Remittances to H.O. (b.f)	11,700
To Branch debtors	<u>2,842</u>	By Balance b/d	<u>10</u>
	<u>12,552</u>		<u>12,552</u>

**13. (i) Books of Branch
Journal Entries**

		(₹ in lacs)	
		Dr.	Cr.
Goods in Transit A/c	Dr.	10	
To Head Office A/c			10
(Goods dispatched by head office but not received by branch before 1st April, 20X2)			
Expenses A/c	Dr.	1	

To Head Office A/c (Amount charged by head office for centralised services)		1
--	--	---

(ii) **Trading and Profit & Loss Account of the Branch
for the year ended 31st March, 20X2**

	₹ in lacs		₹ in lacs
To Opening Stock	60	By Sales	360
To Goods received from		By Closing Stock including transit	72
Head Office 288+10			
Less: Returns (5)	293		
To Carriage Inwards	7		
To Gross Profit c/d	72		
	432		432
To Salaries	25	By Gross Profit b/d	72
To Depreciation on Furniture	2		
To Rent	10		
To Advertising	6		
To Telephone, Postage & Stationery	3		
To Sundry Office Expenses	1		
To Head Office Expenses (centralised services)	1		
To Net Profit Transferred to Head Office A/c	24		
	72		72

Balance Sheet as on 31st March, 20X2

Liabilities	₹ in lacs		Assets	₹ in lacs	
Head Office	80		Furniture & Equipment	20	
Add: Goods in transit	10		Less: Depreciation	(2)	18
Head Office Expenses	1		Stock in hand		62
Net Profit	<u>24</u>	115	Goods in Transit		10
Outstanding Expenses		3	Debtors		20
		<u>118</u>	Cash at bank and in hand		8
					<u>118</u>

(iii)

**Books of Head Office
Journal Entries**

	₹ Dr.	₹ Dr.
Branch Trading Account Dr.	365	
To Branch Account		365
(The total of the following items in branch trial balance debited to branch trading account:		
		₹ in lacs
Opening Stock	60	
Goods received from Head Office	288	
Goods purchased but not received	10	
Carriage Inwards	7	

Branch Account	Dr.	437	
To Branch Trading Account			437
(Total sales, closing stock and goods returned to Head Office credited to branch trading account, individual amount being as follows:			
		₹ in lacs	
Sales		360	
Closing Stock		62	
Goods in transit		10	
Goods returned to Head Office		5)	
Branch Trading Account	Dr.	72	
To Branch Profit and Loss Account			72
(Gross profit earned by branch credited to Branch Profit and Loss Account)			
Branch Profit and Loss Account	Dr.	48	
To Branch Account			48
(Total of the following branch expenses debited to Branch Profit & Loss Account:			
		₹ in lacs	
Salaries		25	
Rent		10	
Advertising		6	
Telephone, Postage & Stationery		3	
Sundry Office Expenses		1	
Head Office Expenses		1	
Depreciation on furniture		2)	
Branch Profit & Loss Account	Dr.	24	
To Profit and Loss Account			24
(Net profit at branch credited to general Profit & Loss A/c)			

Branch Furniture & Equipment	Dr.	18	
Branch Stock	Dr.	62	
Branch Debtors	Dr.	20	
Branch Cash at Bank and in Hand	Dr.	8	
Goods in Transit	Dr.	10	
To Branch			118
(Incorporation of different assets at the branch in H.O. books)			
Branch	Dr.	3	
To Branch Outstanding Expenses			3
(Incorporation of Branch Outstanding Expenses in H.O. books)			

14. Bangalore Branch Stock Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance b/d	4,50,000	By Goods sent to branch A/c	90,000
Goods sent to branch A/c	45,00,000	(Returns)	
To Branch debtors A/c (Returns)	60,000	By Bank A/c (Cash sales)	15,00,000
To Branch adjustment A/c (Surplus over invoice price)*	<u>1,80,000</u>	By Branch debtors A/c (credit sales)	27,00,000
	<u>51,90,000</u>	By Balance c/d	9,00,000
			<u>51,90,000</u>

**Alternatively, this may directly be transferred to Branch P&L A/c without routing it through Branch Adjustment Account.*

Bangalore Branch Adjustment Account

<i>Particulars</i>	<i>Amount (₹)</i>	<i>Particulars</i>	<i>Amount (₹)</i>
To Stock reserve - 20% of ₹ 9,00,000 (closing stock)	1,80,000	By Stock reserve - 20% of ₹ 4,50,000 (Opening stock)	90,000
To Branch profit & loss A/c (Gross profit)	9,72,000	By Goods sent to branch A/c – 20% of ₹ 44,10,000 (45,00,000 – 90,000)	8,82,000
	<u> </u>	By Branch stock A/c	<u>1,80,000</u>
	<u>11,52,000</u>		<u>11,52,000</u>

Branch Profit & Loss Account

<i>Particulars</i>	<i>Amount (₹)</i>	<i>Particulars</i>	<i>Amount (₹)</i>
To Branch expenses A/c	6,30,000	By Branch adjustment A/c (Gross Profit)	9,72,000
To Branch debtors A/c (Discount)	45,000		
To Branch Debtors A/c (Bad debts)	30,000		
To Net profit (transferred to Profit & Loss A/c)	<u>2,67,000</u>		<u> </u>
	<u>9,72,000</u>		<u>9,72,000</u>

Branch Expenses Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Bank A/c (Rent, rates & taxes)	1,35,000	By Branch profit and loss A/c (Transfer)	6,30,000
To Bank A/c (Salaries, wages & bonus)	4,50,000		
To Bank A/c (Office expenses)	<u>45,000</u>		
	<u>6,30,000</u>		<u>6,30,000</u>

Branch Debtors Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance b/d	5,40,000	By Bank A/c	24,00,000
To Branch stock A/c	27,00,000	By Branch profit and loss A/c (Bad debts and discount)	75,000
		By Branch stock A/c (Sales returns)	60,000
		By Balance c/d (bal. fig.)	<u>7,05,000</u>
	<u>32,40,000</u>		<u>32,40,000</u>

Goods sent to Branch Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Branch stock A/c	90,000	By Branch stock A/c	45,00,000
To Branch adjustment A/c	8,82,000		
To Purchases A/c	<u>35,28,000</u>		
	45,00,000		<u>45,00,000</u>

15.

**Trading and Profit and Loss A/c
For the year ended 31st March 20X1**

	Head office ₹	Branch ₹		Head office ₹	Branch ₹
To Opening stock	2,25,000	-	By Sales	27,81,000	9,50,000
To Purchases	25,50,000	-	By Goods sent to branch	9,54,000	-
To Goods received from head office	-	9,54,000	By Closing stock (W.N.1 & 2)	7,00,000	99,000
To Gross profit c/d	16,60,000	95,000			
	44,35,000	10,49,000		44,35,000	10,49,000
To Office expenses	90,000	8,500	By Gross profit b/d	16,60,000	95,000
To Selling expenses	72,000	6,300			
To Staff salaries	65,000	12,000			
To Branch Stock Reserve (W.N.3)	44,000	-			
To Net Profit	13,89,000	68,200			
	16,60,000	95,000		16,60,000	95,000

(iv)	No entry in Branch Books is required.			
(v)	Expenses Account To Head Office Account (Being allocated expenses of Head Office recorded)	Dr.	75,000	75,000
(vi)	Head Office Account To Debtors Account (Being adjustment entry for collection from Branch Debtors directly by Head Office)	Dr.	30,000	30,000
(vii)	Goods -in- transit Account To Head Office Account (Being goods sent by Head Office still in-transit)	Dr.	10,000	10,000

17. (i) **In the Books of Head Office**
Branch Trading and Profit & Loss A/c (in Dollars)
for the year ended 31st December, 20X1

<i>Particulars</i>	\$	<i>Particulars</i>	\$
To Opening stock	11,200	By Sales	84,000
To Goods from H.O.	64,000	By Closing stock (W.N.2)	8,000
To Gross profit c/d	16,800		
	92,000		92,000
To Expenses	5,000	By Gross profit b/d	16,800
To Depreciation (24,000 x 10%)	2,400		
To Manager's commission (W.N.1)	470		
To Net profit c/d	8,930		
	16,800		16,800

(ii) (a) Converted Branch Trial Balance (into Indian Currency)

Particulars	Rate per \$	Dr. (₹)	Cr. (₹)
Machinery	40	9,60,000	–
Stock January 1, 20X1	46	5,15,200	–
Goods from head office	Actual	29,26,000	–
Sales	47	–	39,48,000
Expenses	47	2,35,000	–
Debtors & creditors	48	2,30,400	1,63,200
Cash at bank	48	57,600	–
Head office A/c	Actual	–	8,60,000
Difference in exchange rate (b.f.)		47,000	–
		49,71,200	49,71,200
Closing stock \$ 8,000 (W.N. 2)	48		₹ 3,84,000

(b) Branch Trading and Profit & Loss A/c for the year ended 31st December, 20X1

	₹		₹
To Opening stock	5,15,200	By Sales	39,48,000
To Goods from head office	29,26,000	By Closing stock (W.N.2)	3,84,000
To Gross profit c/d	8,90,800		
	43,32,000		43,32,000
To Expenses	2,35,000	By Gross profit b/d	8,90,800
To Depreciation @ 10% on ₹ 9,60,000	96,000		
To Exchange difference	47,000		
To Manager's commission (W.N.1)	22,560		
To Net Profit c/d	4,90,240		
	8,90,800		8,90,800

(c) Branch Account

	₹			₹
To Balance b/d	8,60,000	By Machinery	9,60,000	
To Net profit	4,90,240	Less: Depreciation	(96,000)	
To Creditors	1,63,200			8,64,000
To Outstanding commission	22,560	By Closing stock		3,84,000
		By Debtors		2,30,400
		By Cash at bank		57,600
	15,36,000			15,36,000

Working Notes:**1. Calculation of manager's commission @ 5% on profit**

i.e. 5% of \$[16,800 – (5,000 + 2,400)]

Or 5% × \$9,400 = \$ 470

Manager's commission in Rupees = \$ 470 × ₹ 48 = ₹ 22,560

2. Calculation of closing stock

	\$
Opening stock	11,200
Add: Goods from head office	<u>64,000</u>
	75,200
Less: Cost of goods sold (at invoice price)	
i.e. $\frac{100}{125} \times 84,000$	<u>(67,200)</u>
Closing stock	<u>8,000</u>
Closing stock in Rupees = \$8,000 × ₹ 48 = ₹ 3,84,000.	

Note: Manager is entitled to commission on profits earned at the end of the year.

CASE SCENARIOS



Case Scenario 1

RTS Ltd, ("RTS" or the "Company"), is engaged in the business of manufacturing of equipments/components. The Company has a contract with the Indian Railways for a brake component which is structured such that:

- ◆ The Company's obligation is to deliver the component to the Railways' stockyard, while the delivery terms are ex-works, the Company is responsible for engaging a transporter for delivery.
- ◆ Railways sends an order for a defined quantity.
- ◆ The Company manufactures the required quantity and informs Railways for carrying out the inspection.
- ◆ Railways representatives visit the Company's factory and inspect the components, and mark each component with a quality check sticker.
- ◆ Goods once inspected by Railways, are marked with a hologram sticker to earmark for delivery identification by the customer when they are delivered to the customer's location.
- ◆ The Company raises an invoice once it dispatches the goods.

The management of RTS is under discussion with the auditors of the Company in respect of accounting of a critical matter as regards its accounting with respect subsequent events i.e. events after the reporting period. They have been checking as to which one of the following events after the reporting period provide evidence of conditions that existed at the end of the reporting period?

- i. Nationalisation or privatization by government
- ii. Out of court settlement of a legal claim
- iii. Rights issue of equity shares
- iv. Strike by workforce
- v. Announcing a plan to discontinue an operation

The Company has received a grant of ₹ 8 crores from the Government for setting up a factory in a backward area. Out of this grant, the Company distributed ₹ 2 crores as dividend. The Company also received land, free of cost, from the State Government but it has not recorded this at all in the books as no money has been spent.

RTS has a subsidiary, A Ltd, which is evaluating its production process wherein normal waste is 5% of input. 5,000 MT of input were put in process resulting in wastage of 300 MT. Cost per MT of input was ₹ 1,000. The entire quantity of waste was on stock at the end of the financial year.

- (i) When should RTS Ltd recognize revenue as per the Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006? Would your answer be different if inspection is normally known to lead to no quality rejections?
 - (a) Revenue should be recognized on dispatch of components. The assessment would not change even in case where inspection is normally known to lead to no quality rejections.
 - (b) Revenue should be recognized on completion of inspection of components. The assessment would not change even in case where inspection is normally known to lead to no quality rejections.
 - (c) Revenue should be recognized on dispatch of components. The assessment would change where inspection is normally known to lead to no quality rejections.
 - (d) Revenue should be recognized on delivery of the component to the Railways' stockyard. The assessment would change where inspection is normally known to lead to no quality rejections.

- (ii) In respect of A Ltd, state with reference to Accounting Standards notified under the Companies (Accounting Standards) Rules, 2006, what would be value of the inventory to be recorded in the books of accounts?
- (a) ₹ 4,700,000.
 - (b) ₹ 5,000,000.
 - (c) ₹ 4,950,000.
 - (d) ₹ 4,947,368.
- (iii) Please guide regarding the accounting treatment of both the grants mentioned above in line with the requirements of Accounting Standard 12.
- (a) Distribution of dividend out of grant is correct. In the second case also not recording land in the books of accounts is correct.
 - (b) Distribution of dividend out of grant is incorrect. In the second case, not recording land in the books of accounts is correct.
 - (c) Distribution of dividend out of grant is correct. In the second case, land should be recorded in the books of accounts at a nominal value.
 - (d) Distribution of dividend out of grant is incorrect. In the second case, land should be recorded in the books of accounts at a nominal value.

Answers

(i)	(b)	(ii)	(d)	(iii)	(d)
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Case Scenario 2

Suman Ltd. is in the business of manufacturing electronics equipment and selling these at its various outlets. It provides installation services for the equipment sold and also provide free 1 year warranty on all the sold products.

Beach Resorts are leading resorts in the city. It purchased 5 air conditioners (AC) from Suman Ltd. for its resort. Suman Ltd. sold 5 AC to Beach resort for ₹ 45,000 each which includes installation fees of ₹ 1,000 for each AC. The Company also offers 1 year warranty for any repair etc. The Company also offered ₹ 500 per AC as trade discount. Beach resort placed order on March 15, 2024 and made payment on March 20, 2024. The ACs were delivered on March 27, 2024 and the installation was completed on April 5, 2024.

- (i) How much revenue should be recognised by the Company as on March 31, 2024:
- (a) ₹ 2,25,000
 - (b) ₹ 2,17,500
 - (c) ₹ 2,00,000
 - (d) ₹ 2,30,000
- (ii) How much revenue should be recognised by the Company in the financial year 2024-25:
- (a) ₹ 5000
 - (b) ₹ 2,20,000
 - (c) ₹ 10,000
 - (d) ₹ 2,40,000
- (iii) What will be the accounting for trade discount:
- (a) The same will be recognised separately in the profit and loss.
 - (b) The trade discounts are deducted in determining the revenue.
 - (c) Trade discount will be recognised after one year, when the warranty will be over.
 - (d) Trade discount will be recognised after installation is complete.
- (iv) Is the Company required to do any accounting for 1 year warranty provided by it:
- (a) No accounting treatment is required till some warranty claim is actually received by the Company.
 - (b) As there exist a present obligation to provide warranty to customers for 1 year, the Company should estimate the amount that it may have to incur considering various factors including past trends and create a provision as per AS 29.
 - (c) Accounting for claims will be done on cash basis i.e. expense will be recognised when expense is made.

- (d) As the Company is not charging separately for the warranty provided, there is no need to create any provision.

Answers

(i)	(b)	(ii)	(a)	(iii)	(b)	(iv)	(b)
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Case Scenario 3

Mars Ltd. is a manufacturing enterprise which is starting a new manufacturing plant at X Village. It has commenced construction of the plant on April 1, 2023 and has incurred following expenses:

- ◆ It has acquired land for installing Plant for ₹ 50,00,000
- ◆ It incurred ₹ 35,00,000 for material and direct labour cost for developing the Plant.
- ◆ The Company incurred ₹ 10,00,000 for head office expenses at New Delhi which included rent, employee cost and maintenance expenditure.
- ◆ The Company borrowed ₹ 25,00,000 for construction work of Plant @12% per annum on April 1, 2023. Director finance of the Company incurred travel and meeting expenses amounting to ₹ 5,00,000 during the year for arranging this loan.
- ◆ On November 1, 2023, the construction activities of the plant were interrupted as the local people alongwith the activists have raised issues relating to environmental impact of plant being constructed. Due to agitation the construction activities came to standstill for 3 months.
- ◆ With the help of Government and NGOs, the agitation was over by February 28, 2024 and the work resumed. However, to balance the impact on environment, government ordered the company to install certain devices for which the Company had to incur ₹ 6,00,000 in March 2024.
- ◆ The rate of depreciation on Plant is 10%.

Based on the above information, answer the following questions.

- (i) Which of the following expenses cannot be included in the cost of plant:
- (a) Cost of Land

- (b) Construction material and labour cost
- (c) Head office expenses
- (d) Borrowing cost
- (ii) How much amount of borrowing cost can be capitalised with the plant:
- (a) ₹ 300,000
- (b) ₹ 2,00,000
- (c) ₹ 7,00,000
- (d) ₹ 6,00,000
- (iii) The total cost of plant as on march 31, 2024 will be:
- (a) ₹ 85,00,000
- (b) ₹ 98,00,000
- (c) ₹ 93,00,000
- (d) ₹ 95,00,000
- (iv) The amount of depreciation to be charged for the year end March 31, 2024
- (a) ₹ 4,30,000
- (b) ₹ 9,30,000
- (c) ₹ 9,80,000
- (d) Nil

Answers

(i)	(c)	(ii)	(b)	(iii)	(c)	(iv)	(d)
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Case Scenario 4

Beloved Finance Ltd. is a financial enterprise which is in the business of lending loan to small businesses and earn interest on loans.

- ◆ During the year the Company has lend 50 crores and earned ₹ 1.5 crore as interest on loans.

- ◆ The Company had surplus funds during the year and invested then in Fixed Deposits with bank and earned interest on fixed deposits of ₹ 20 lacs.
- ◆ The Company also acquired a gold loan unit for ₹ 10 crore during the year and the Company provided interest free loan of ₹ 15 crore to its wholly-owned subsidiary.
- ◆ The Company paid a total income tax of ₹ 75 lacs for the year.

Based on the above information, answer the following questions.

- (i) In the Cash Flow Statement as per AS 3, the interest income of ₹ 1.5 crore earned on loans given by the Company will be disclosed as:
 - (a) Cash Flow from Operating Activities
 - (b) Cash Flow from Investing Activities
 - (c) Cash Flow from Financing Activities
 - (d) Non-cash Items
- (ii) In the Cash Flow Statement as per AS 3, the interest income of ₹ 20 Lacs earned fixed deposits with bank will be disclosed as:
 - (a) Cash Flow from Operating Activities
 - (b) Cash Flow from Investing Activities
 - (c) Cash Flow from Financing Activities
 - (d) Non-cash Items
- (iii) In the Cash Flow Statement as per AS 3, amount paid for acquiring gold loan unit will be disclosed as:
 - (a) Cash Flow from Operating Activities
 - (b) Cash Flow from Investing Activities
 - (c) Cash Flow from Financing Activities
 - (d) Non-cash Items
- (iv) In the Cash Flow Statement as per AS 3, total income tax of ₹ 75 lacs paid for the year will be disclosed as:
 - (a) Cash Flow from Operating Activities

- (b) Cash Flow from Investing Activities
 - (c) Cash Flow from Financing Activities
 - (d) Non-cash Items
- (v) Is any specific disclosures required to made in relation to the interest free loan of ₹ 15 crore provided by the Company to its wholly-owned subsidiary, if yes, as per which Accounting Standard:
- (a) Yes, disclosure is required to be made as per AS 3, Cash Flow Statements.
 - (b) Yes, disclosure is required to be made as per AS 18, Related Party Disclosures
 - (c) Yes, disclosure is required to be made as per AS 13, Accounting for Investments
 - (d) No specific disclosures are required.

Answers

(i)	(a)	(ii)	(a)	(iii)	(b)	(iv)	(a)	(v)	(b)
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Case Scenario 5

Venus Limited received a parcel of land at no cost from the government for the purpose of developing a factory in an outlying area. The land is valued at ₹ 75 lakhs, while the nominal value is ₹ 10 lakhs. Additionally, the company received a government grant of ₹ 30 lakhs, which represents 25% of the total investment needed for the factory development. Furthermore, the company received ₹ 15 lakhs with the stipulation that it be used to purchase machinery. There is no expectation from the government for the repayment of these grants.

Answer the following questions based on the above information:

- (i) The land received from Government, free of cost should be presented at:
- (a) ₹ 75 Lakhs
 - (b) ₹ 30 Lakhs
 - (c) ₹ 10 Lakhs
 - (d) ₹ 45 Lakhs

- (ii) As per AS 12, how the Government Grant of ₹ 30 Lakhs should be presented:
- (a) It should be recognised in the profit and loss statement as per the related cost.
 - (b) It will be treated as capital reserve.
 - (c) It will be treated as deferred income.
 - (d) It will not be recognised in the financial statements.
- (iii) As per AS 12, how the Government Grant of ₹ 15 Lakhs with a condition to purchase machinery may be presented as:
- (a) Capital Reserve
 - (b) Shareholders Fund
 - (c) Deferred Income
 - (d) Income in statement of profit and loss as received.
- (iv) Which of the above grants are required to be recognised in the statement of profit and loss on a systematic and rational basis over the useful life of the asset:
- (a) Land received as Grant
 - (b) Government Grant of ₹ 30 Lakhs
 - (c) Government Grant of ₹ 15 Lakhs with a condition to purchase machinery
 - (d) None of the above

Answers

(i)	(c)	(ii)	(b)	(iii)	(c)	(iv)	(c)
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Case Scenario 6

Axis limited is a manufacturing company. It purchased a machinery costing ₹ 10 Lakhs in April 2023. It paid ₹ 4 lakhs upfront and paid the remaining ₹ 6,00,000 as deferred payment by paying instalment of ₹ 1,05,000 for the next 6 months. During the year, the Company sold a land which was classified as its 'property, plant and equipment' for ₹ 25,00,000 and paid ₹ 1,00,000 as income tax as long term capital gain on such sale. During the year, the Company also received

income tax refund along with interest.

- (i) As per the requirements of AS 3, 'Cash Flow Statements', how the amount for purchase of machinery should be presented:
 - (a) ₹ 10 lakhs as 'Cash flows from Investing Activities' and ₹ 30,000 will simply be booked in profit and loss with no presentation in Cash Flow Statement.
 - (b) ₹ 10.30 lakhs as 'Cash flows from Investing Activities' as entire amount is spent on purchase of machinery.
 - (c) ₹ 10 lakhs as 'Cash flows from Investing Activities' and ₹ 30,000 as 'Cash flows from Financing Activities'.
 - (d) ₹ 10.30 lakhs as 'Cash flows from Financing Activities' as the machinery has been purchased on finance.
- (ii) At what amount, the machinery should be recognised in the financial statements:
 - (a) ₹ 400,000
 - (b) ₹ 10,30,000
 - (c) ₹ 600,000
 - (d) ₹ 10,00,000
- (iii) How should the income tax paid on sale of land be disclosed in the Cash Flows Statement:
 - (a) Cash flows from Operating Activities
 - (b) Cash flows from Investing Activities
 - (c) Cash flows from Financing Activities
 - (d) No disclosure in Cash Flow Statement
- (iv) How should the interest on income tax refunds be disclosed in the Cash Flows Statement:
 - (a) Cash flows from Operating Activities
 - (b) Cash flows from Investing Activities
 - (c) Cash flows from Financing Activities

- (d) No disclosure in Cash Flow Statement

Answers

(i)	(c)	(ii)	(d)	(iii)	(b)	(iv)	(b)
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Case Scenario 7

SEAS Ltd., the "Company", is in the business of tours and travels. It sells holiday packages to the customers. The Company negotiates upfront with the Airlines for specified number of seats in flight. The Company agrees to buy a specific number of tickets and pay for those tickets regardless of whether it is able to resell all of those in package.

The rate paid by the Company for each ticket purchased is negotiated and agreed in advance. The Company also assists the customers in resolving complaints with the service provided by airlines. However, each airline is responsible for fulfilling obligations associated with the ticket, including remedies to a customer for dissatisfaction with the service.

The Company bought a forward contract for three months of US\$ 1,00,000 on 1 March 2024 at 1 US\$ = INR 83.10 when exchange rate was US\$ 1 = INR 83.02. On 31 March 2024, when the Company closed its books, exchange rate was US\$ 1 = INR 83.15. On 1 April 2024, the Company decided for premature settlement of the contract due to some exceptional circumstances.

The Company is evaluating below mentioned schemes:

- i. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement.
- ii. Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of ₹ 20,000 per month. Earlier there was no such scheme of pension in the organization.

SEAS Ltd. has a subsidiary, ADI Ltd., which is in the business of construction having turnover of ₹ 200 crores. SEAS Ltd. and ADI Ltd. hold 9% and 23% respectively in an associate company, ASOC Ltd. Both SEAS Ltd. and ADI Ltd. prepare consolidated financial statements as per Accounting Standards notified under the Companies (Accounting Standards) Rules, 2021.

- (i) What would be the basis of revenue recognition for SEAS Ltd. as per the requirements of Accounting Standards?
- (a) Gross basis.
 - (b) Net basis.
 - (c) Depends on the accounting policy of the Company.
 - (d) Indian GAAP allows a choice to the Company to recognize revenue on gross basis or net basis.
- (ii) Please suggest accounting treatment of forward contract for the year ended 31 March 2024 as per Accounting Standard 11.
- (a) MTM (marked to market value) of contract will be recorded on 31 March 2024.
 - (b) MTM (marked to market value) of contract will be computed as at 31 March 2024 and only if there is loss, it will be recorded during the year ended 31 March 2024.
 - (c) No accounting will be done during the year ended 31 March 2024.
 - (d) Premium on contract will be amortized over the life of the contract.
- (iii) You are requested to advise the Company in respect of the accounting requirements of above schemes related to employee benefits as to which one of those schemes should be considered as a change in accounting policy during the year.
- (a) 1 – Change in accounting policy. 2 – Change in accounting policy.
 - (b) 1– Not a change in accounting policy. 2 – Change in accounting policy.
 - (c) 1 – Not a change in accounting policy. 2 – Not a change in accounting policy.
 - (d) 1– Change in accounting policy. 2 – Not a change in accounting policy.
- (iv) Please comment regarding consolidation requirements for SEAS Ltd. and ADI Ltd. using the below mentioned options as to which one should be correct.
- (a) ADI Ltd. would use equity method of accounting for 23% in ASOC Ltd. SEAS Ltd. would consolidate ADI Ltd. and consequently automatically

equity account 23% and separately account for the balance 9% as per AS 13.

- (b) ADI Ltd. would account for 23% in ASOC Ltd. as per AS 13. SEAS Ltd. would consolidate ADI Ltd. and consequently automatically account 23% and separately account for the balance 9%.
- (c) ADI Ltd. would account for 23% share in ASOC Ltd using equity method of accounting. SEAS Ltd. would consolidate ADI Ltd. and consequently, automatically account for ASOC Ltd 23% share and separately account for 9% share in ASOC Ltd. using equity method of accounting in consolidated financial statements.
- (d) ADI Ltd. would account for 23% in ASOC Ltd. as per AS 13. SEAS Ltd. would consolidate ADI Ltd. and using equity method of accounting 23% in ASOC Ltd. and separately account for the balance 9% as per AS 13.

Answers

(i)	(a)	(ii)	(d)	(iii)	(c)	(iv)	(c)
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Case Scenario 8

On 1st April, 2022, Shubham Limited purchased some land for ₹ 30 lakhs for the purpose of constructing a new factory. This cost of 30 lakhs included legal cost of ₹ 2 lakhs incurred for the purpose of acquisition of this land. Construction work could start on 1st May, 2022 and Shubham Limited provides you the details of the following costs incurred in relation to its construction:

	₹
Preparation and levelling of the land	80,000
Employment costs of the construction workers (per month)	29,000
Purchase of materials for the construction	21,24,000
Cost of relocating employees to new factory for work	60,000
Costs of inauguration ceremony on 1 st January, 2023	80,000
Overhead costs incurred directly on the construction of the factory (per month)	25,000

General overhead costs allocated to construction project by the Manager is ₹ 30,000. However, as per company's normal overhead allocation policy, it should be ₹ 24,000. The auditor of the company has support documentation for the cost of ₹ 15,000 only) and raised objection for the balance amount.

The construction of the factory was completed on 31st December, 2022 and production could begin on 1st February, 2023. The overall useful life of the factory building was estimated at 40 years from the date of completion. However, it was estimated that the roof will need to be replaced 20 years after the date of completion and that the cost of replacing the roof at current prices would be 25% of the total cost of the building.

The construction of the factory was partly financed by a loan of ₹ 28 lakhs borrowed on 1st April, 2022. The loan was taken at an annual rate of interest of 9%. During the period when the loan proceeds had been fully utilized to finance the construction, Shubham Limited received investment income of ₹ 25,000 on the temporary investment of the proceeds.

You are required to assume that all of the net finance costs to be allocated to the cost of factory (not land) and interest cost to be capitalized based on nine months' period.

Based on the information given in the above scenario, answer the following multiple choice questions:

- (i) Which of the following cost (incurred directly on construction) will be capitalized to the cost of factory building?
- (a) ₹ 2,00,000 incurred as legal cost
 - (b) ₹ 60,000 – costs of relocating employees
 - (c) ₹ 80,000 costs of inauguration ceremony
 - (d) ₹ 24,000 – allocated general overhead cost
- (ii) What amount of employment cost of construction workers will be capitalized to the cost of factory building?
- (a) ₹ 2,90,000
 - (b) ₹ 3,48,000
 - (c) ₹ 2,32,000
 - (d) ₹ 29,000

- (iii) What is the amount of net borrowing cost capitalized to the cost of the factory?
- (a) ₹ 1,89,000
 - (b) ₹ 1,68,000
 - (c) ₹ 1,44,000
 - (d) ₹ 1,64,000
- (iv) What will be the carrying amount (i.e. value after charging depreciation) of the factory in the Balance Sheet of Shubham Limited as at 31st March, 2023?
- (a) ₹ 30,00,000
 - (b) ₹ 57,78,125
 - (c) ₹ 27,78,125
 - (d) ₹ 58,00,000

Answers

(i)	(a)	(ii)	(c)	(iii)	(d)	(iv)	(b)
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