8 ACCOUNTING FOR BRANCHES INCLUDING FOREIGN BRANCHES

INDEX

Quote:-

Start where you are. Use what you have. Do what you can.

-Arthur Ashe

SECTION A - CONCEPTS

1. INTRODUCTION

The branches are divided in two types:

1) Dependent Branch

A branch which does not maintain its own Books of Accounts

Its books are maintained by Head office.

2) Independent Branch

A branch which maintains its own Books of Accounts properly

(a) Domestic Branch

Branch Operating in same Country and in same Currency

(b) Foreign Branch (AS – 11)

Branch whose operation in other Foreign Currency different from HO Currency

Dependent Branches:

Since Head Office has to Maintain the Books of Accounts of Branch. Head Office can follow any of below Methods to find out Net Profit of Branch: -

a) Final A/c System (Cost Method)
b) Final A/c System (IP/WP Method)
c) Stock & Debtors Method
d) Debtors Method

Independent Branches:

These are the branches which maintain their own sets of accounting books and hence are in a position to extract Trial Balance and to ascertain their results thorough their Trial Balance.

2. IMPORTANT BASICS

Let's understand the important basics of Preparing Trading Account with some examples

EXAMPLE 1:

Opening Stock = 60,000; Purchases = 7,20,000; Sales = 8,16,000; Closing Stock = 90,000; Goods are Sold @20% margin above Cost.

SOLUTION:

Opening Stock – 60,000 Purchases - 7,20,000		
Total - 7,80,000		
COGS 8,16,000 / 120 x 100 = 6,80,000	**Closing Stock** 90,000	**Shortage (b/f)** 10,000

Trading A/c

To Opening Stock	60,000	By Sales	8,16,000
To Purchases	7,20,000	By Shortage	10,000
To Gross Profit	1,36,000	By Closing Stock	90,000
	9,16,000		**9,16,000**

EXAMPLE 2:

Opening Stock = 1,30,000; Purchases = 8,90,000 & Total Sales = 8,40,000. Normal GP% is 25% above cost some goods were sold @loss (Heavy Discount) where cost is 1,00,000 & Sale value is 90,000 Prepare Trading A/c.

SOLUTION:

Total Sales = 8,40,000

Heavy Discounted Sales: 90,000 costing 1,00,000

Normal Sale: 7,50,000

COGS = 7,50,000 / 125 x 100 = 6,00,000

Opening Stock – 1,30,000 Purchases - 8,90,000		
Total - 10,20,000		
COGS 7,00,000	**Closing Stock** 3,20,000	**Shortage (b/f)** NIL

Trading A/c

To Opening Stock	1,30,000	By Sales	8,40,000
To Purchases	8,90,000	By Closing Stock	3,20,000
To Gross Profit	1,40,000		
	11,16,000		**11,16,000**

There are Three Most Important Prices of Goods for Head Office & Branch: -

a) **Cost Price** = Price from Head Office Point of View.

b) **Invoice Price (Wholesale Price)** = Price at Which Goods are sent to Branch from Head Office (Cost + Head Office Margin) (IP means Cost from Branch point of view)

c) **Sale Price / List Price / Catalog Price (MRP)** = Price at which goods are ultimately Sold to Customers (SP for HO maybe different from SP for Branch)

Note - If any item like opening stock, closing stock, goods sent are given in question but price is not mentioned (i.e., which price is this Cost or Invoice Price) then always assume INVOICE PRICE

Normal and Abnormal loss

Normal Loss/wastage = Loss of stock which is already anticipated

Abnormal Loss/wastage = Loss of stock which was not anticipated earlier and which is over and above normal.

Treatment:

1) **Normal loss:** Credit side of trading account, only to find out correct gross profit.

2) **Abnormal loss:** Credit side of trading account, only to find out correct gross profit. And Debit side of Profit and loss account (actual cost) (Recognise the loss).

Note:

If nothing is mentioned in the question, we shall always assume that loss is of abnormal nature.

3. ACCOUNTING FOR DEPENDENT BRANCHES

3.1 FINAL ACCOUNT SYSTEM (COST BASIS)

1. Head Office shall prepare Branch Trading at its own Cost Price.
2. All items Such as Opening Stock of Branch, Branch Purchases (Goods Sent From Head Office), Branch Shortage, Branch Closing Stock shall be recorded at Cost Price (Cost to HO)
3. Branch sales shall be recorded at Actual SP
4. GP amount means Difference of SP & Cost Price
5. If any Item is given in Question at Invoice Price, we shall convert it into Cost First & then record in Trading A/c
6. HO Shall prepare Branch Trading as a working. Therefore, in solution we always use the word: "Memorandum Branch Trading A/c"

Dr. Branch Memorandum Trading and Profit & Loss A/c Cr.

Particulars	Amount	Particulars	Amount
To Opening Stock A/c	Cost	By Sales A/c	Sales Value
To Goods sent to Branch A/c	Cost	Less Sales Return	
Less goods returned to HO		By Loss of Stock	Cost
To Direct Purchases A/c	Cost	By Closing Stock	Cost
To Direct Expenses A/c			
To Gross Profit			

EXAMPLE 3:

Cost of Goods = 100; Invoice Price = 120; Selling Price = 130;

Opening Stock = 200; Goods Sent to Branch = 2500; Sales = 2860; Closing Stock = 400

Assume all figures are at Cost except Sales.

SOLUTION:

Branch's Trading A/c

To Opening Stock	200	By Sales	2,860
To Purchases (Goods sent from HO)	2,500	By Shortage	100
To Gross Profit	660	By Closing Stock	400
	3,360		**3,360**

EXAMPLE 4:

From the following information prepare Memorandum Branch Trading A/c (at Cost)
Branch Opening Stock = 90,000 (IP); Goods Sent to Branch = 7,00,000 (IP); Sales By Branch = 9,00,000; HO sent goods to Branch @25% above Cost. SP is 20% above Invoice Price.

SOLUTION:

Cost = 100; IP = 125 & SP = 125 + 20% = 150

Working Note: Calculation of Closing Stock (Cost)

Opening Stock – 72,000 (90,000 / 125 x 100) Goods sent from HO - 5,60,000 (7,00,000 / 125 x 100)		
Total - 6,32,000		
COGS 90,00,000 / 150 x 100 = 6,00,000	**Closing Stock** 3,20,000	**Shortage (b/f)** NIL

Memorandum Branch Trading A/c

To Opening Stock	72,000	By Sales	9,00,000
To Goods sent from HO	5,60,000	By Closing Stock	32,000
To Gross Profit	3,00,000		
	9,32,000		**9,32,000**

EXAMPLE 5: -

Opening Stock @IP = 1,50,000; Goods Sent to Branch @ Cost = 7,50,000; HO Sends goods to Branch @25% above Cost; Branch Credit Sales = 6,00,000; Branch Cash Sales = 4,37,500; Closing Stock = 1,37,500 (IP); Branch Sells Goods on Cash @IP, SP is 20% above IP.

SOLUTION:

Cost = 100; IP = 125 & SP = 150 (125 + 20%)

Working Note 1: COGS

On Credit Sales = 6,00,000 / 150 x 100 = 4,00,000
On Cash Sales = 4,37,500 (IP) / 125 (IP) = 3,50,000

Working Note 2: Shortage Calculation

Opening Stock	1,20,000
Goods Sent	7,50,000
	8,70,000
COGS	7,50,000
Closing Stock	1,10,000
Shortage (B/F)	10,000

Memorandum Branch Trading A/c

To Opening Stock	1,20,000	By Sales	10,37,500
To Goods sent from HO	7,50,000	By Shortage	10,000
To Gross Profit	2,87,500	By Closing Stock	1,10,000
	11,57,500		**11,57,500**

EXAMPLE 6:-

HO at Nagpur & Branch @ Patna HO invoiced goods to Branch @20% less than List price

List Price is Cost Plus 100%

Branch makes Cash Sales @IP & Credit Sales @List Price.

Opening Stock at Branch (IP)	12,000
Debtors Opening	10,000
Goods Received from HO	1,32,000
Sales: Cash Credit	46,000 1,00,000
Cash received from Debtors	85,000
Indirect Expenses of Branch	17,500
Closing Debtors	25,000
Closing Stock	17,600 (IP)
Remittance to HO	1,13,500

Find out Branch GP & NP by following 'Final A/c System Cost Basis'.

SOLUTION:

Cost = 100; List Price = 200 and IP = 200 – 20% = 160

Working Note 1: Calculation of Shortage

Opening Stock – 7,500 Goods from HO – 82,500		
Total - 90,000		
COGS 1) 1,00,000 / 200 x 100 = 50,000 2) 46,000 / 160 x 100 = 28,750 **= 78,750**	**Closing Stock** 11,000 at Cost	**Shortage (b/f)** 250

Memorandum Branch Trading and P&L A/c

To Opening Stock	7,500	By Sales Cash Credit	 46,000 1,00,000
To Goods sent to Branch	82,500	By Shortage	250
To Gross Profit	67,250	By Closing Stock	11,000
	1,57,250		**1,57,250**
To Abnormal Loss	250	By Gross Profit	67,250
To Expenses	17,500		
To Net Profit	49,500		
	67,250		**67,250**

EXAMPLE 7: (Master Problem)

Delhi HO sends goods to its Pune branch at 20% above cost. Branch has been instructed by HO to sell goods as under: -

Cash sales at IP

Credit sales at SP (Which is 50% above cost)

1) Opening stock = Rs. 75,000 (IP)
2) Goods sent to branch = Rs. 5,40,000 (IP)
3) Cash sales = Rs. 1,08,000 (IP)

4) Credit sales = Rs. 4,65,000 (SP)
5) Sales return by credit customer = Rs. 22,500 (SP)
6) Sales return by cash customer = Rs. 12,000 (IP)
7) Goods return by branch to HO = Rs. 48,000 (IP)
8) Goods received by branch till year end = Rs. 5,10,000 (IP)
9) Closing stock at the end = Rs. 72,000 (IP)

SOLUTION

Opening Stock (Cost) – 62,500 + Net Goods Sent to Branch – 4,10,000 ((5,40,000 – 48,000) / 120 x 100)				
Total (IP) – 4,72,500				
COGS (IP) 1) Cash Sales: Net Sales = 96,000 / 120 x 100 COGS (Cash) = 80,000 2) Net Credit Sales = 4,42,500 (SP) COGS = 4,42,500 / 150 x 100 = 2,95,000 Total COGS = 3,75,000	**Closing Stock** 60,000	**Goods in Transit** 25,000	**Shortage (b/f)** 12,500	**Gross Profit** 1,63,500

Memorandum Branch Trading and P&L A/c

To Opening Stock	62,500	By Sales Net Cash Net Credit	 96,000 4,42,500
To Net Goods sent to Branch	4,10,000	By Shortage	12,500
To Gross Profit	1,63,500	By Closing Stock In Hand In Transit	 60,000 25,000
	6,36,000		**6,36,000**
To Abnormal Loss	12,500	By Gross Profit	1,63,500
To Net Profit	1,51,000		
	1,63,500		**1,63,500**

3.2 FINAL ACCOUNT SYSTEM (WHOLESALE PRICE or INVOICE PRICE METHOD)

Under this system, the profit/loss made by branch is calculated by preparing the Trading and Profit & Loss account on Wholesale Price basis. This account is not made as a part of main accounting system and is prepared on Memorandum basis. Since the account is made on Wholesale price basis, following points are needed to be note as under:

1) Head Office shall prepare Branch Trading @IP Value
2) Means all items (Except Sales) shall be recorded at IP
3) Sales shall be recorded @ actual figure given
4) While Calculating Closing Stock & Shortage, COGS shall be determined at IP also.
5) Head Office Shall Calculate Stock Reserve (Unrealised Profit) on Opening Stock of Branch, Closing Stock of Branch & Shortage @Branch.

6) Why we are Calculating SR?

(i) **On Closing Stock / Shortage**

Since Goods are not Sold till year end by Branch & Such Goods are shown at IP Value, it means Head Office has already booked Profit on such Closing Stock & Shortage. Therefore, Head Office shall reverse the profit element included in Closing stock & Shortage.

Head office Books

P&L A/c Dr.

To SR A/c

(ii) **On Opening Stock:**

Last year this Opening Stock was closing stock & Profit portion was eliminated, in CY assuming it is actually sold by Branch. Therefore, Profit Portion is recognised.

SR A/c Dr.

To P&L A/c

EXAMPLE 8: -

Opening stock at Branch (Cost) = 90,000; Goods Sent to Branch (IP) = 7,50,000; Head Office sends goods to Branch at Cost + 50%; Branch sells goods to Customer at IP + 30%; Sales = 8,19,000 at Sale Price & Closing Stock = 1,50,000 (Cost)

Find out Profit of Branch by Final A/c System IP method.

SOLUTION:

Working Note 1: Shortage Calculation

Opening Stock (IP) – 1,35,000 + Goods Sent (IP) – 7,50,000		
Total (IP) – 8,85,000		
COGS (IP) 8,19,000 / 195 x 150 = 6,30,000	**Closing Stock** 2,25,000	**Shortage (b/f)** 30,000

Memorandum Branch Trading A/c

To Opening Stock	1,35,000	By Sales	8,19,000
To Goods sent from HO	7,50,000	By Shortage	30,000
To Gross Profit	1,89,000	By Closing Stock	2,25,000
	10,74,000		**10,74,000**

GP = Sale Price – Invoice Price = 195 – 150 = 45

Sale = 8,19,000 (SP) / 195 (SP) x 45 = 1,89,000

Working Note 2:

Unrealised Profit (Stock Reserve) on Opening & Closing Inventory

(i) Closing Inventory = 2,25,000 / 150 x 50 = 75,000 (SR)

(ii) Opening Stock = 1,35,000 / 150 x 50 = 45,000 (SR)

EXAMPLE 9: -

Head Office Purchased Goods Rs. 1,00,000

Out of Above 40% Sent to Branch at IP (IP = Cost + 20%)

Out of above 1,00,000 goods, Head Office Directly made Sales of 50% Purchased goods at cost + 20%

Out of goods received by Branch, 80% Sold by Branch to Customer at IP + 25%

Head Office Trading A/c

To Opening Stock	0	By Goods Sent to Branch	48,000
To Purchases	1,00,000	By Sales	60,000
To Gross Profit	18,000	By Closing Stock	10,000
	1,18,000		**1,18,000**

Branch Trading A/c

To Opening Stock	0	By Sales	48,000
To Purchases from HO	48,000	By Closing Stock	9,600
To Gross Profit	9,600		
	57,600		**57,600**

Head Office Books:

P&L A/c Dr. 1,600

To SR A/c 1,600

EXAMPLE 10: -

From the Following Information Prepare Memorandum Branch Trading (@IP)

Branch Opening Stock = 90,000 (IP); Goods sent to Branch = 7,00,000 (IP) & Sales by Branch = 9,00,000

HO sends goods to Branch @25% Above Cost.

SP is 20% above IP

SOLUTION:

Memorandum Branch Trading A/c

To Opening Stock	90,000	By Sales	9,00,000
To Goods sent from HO	7,00,000	By Closing Stock	40,000
To Gross Profit	1,50,000		
	9,40,000		**9,40,000**

Working Note: 1

Opening Stock (IP) – 90,000 + Goods Sent (IP) – 7,00,000		
Total (IP) – 7,90,000		
COGS (IP) 9,00,000 / 150 x 125 = 7,50,000	**Closing Stock** 40,000	**Shortage (b/f)** NIL

Working Note: 2

Calculation of SR

	Opening Stock	Closing Stock
Stock @ IP	90,000	40,000
IP	125	125
Loading (Cost – IP)	25	25
Working	90,000 / 125 x 25	40,000 / 125 x 25
SR	18,000	8,000
Journal Entry	SR A/c Dr. To P&L A/c	P&L A/c Dr. To SR A/c

EXAMPLE 11: -

Opening Stock @IP = 1,50,000; Goods Sent to Branch @Cost 7,50,000; HO Sent Goods to Branch @25% above Cost; Branch Credit Sales = 6,00,000; Branch Cash Sales (IP) = 4,37,500; Closing Stock = 1,37,500 (IP)

Branch Sells Goods on Credit @SP. Which is 20% above IP. Branch Sells goods on Cash @IP

SOLUTION:

Opening Stock (IP) – 1,50,000 + Goods Sent (IP) – 9,37,500		
Total (IP) – 10,87,500		
COGS (IP) 1) Credit Sale = 6,00,000 / 150 x 125 = 5,00,000 2) Cash Sale = 4,37,500	**Closing Stock** 1,37,500	**Shortage (b/f)** 12,500

Memorandum Branch Trading A/c

To Opening Stock	1,50,000	By Sales Credit Cash	 6,00,000 4,37,500
To Goods sent	9,37,500	By Shortage	12,500
To Gross Profit	1,00,000	By Closing Stock	1,37,500
	11,87,500		**11,87,500**

2.3 STOCK AND DEBTOR SYSTEM

Under this system, the HO maintains for every branch, Branch stock account, Branch debtor account, other Branch assets/liabilities accounts (individually), Branch expenses accounts (individually), Branch adjustment account and Branch profit & loss account.

1. **Branch Stock Account:** This account records the physical flow of goods between HO and branch at INVOICE PRICE. However, sales are recorded at selling price. The invoice price is the amount at which goods are transferred from HO to branch. The goods can also be transferred by HO to branch at cost to the HO. The basic relationship between the various components is as follows:

   Cost to HO + Mark-up (Loading) = Invoice Price (Cost to branch)

   Or Invoice Price - Mark-up (Loading) = Cost.

2. **Branch Adjustment Account:** This account is a nominal account and calculates the gross profit/loss by branch but is made in a different manner from the trading account. It basically records loading (i.e. difference of invoice price and cost) on opening stock, goods supplied, goods returned, closing stock etc.

3. **Branch Profit & Loss Account:** This account is a nominal account and calculates the net profit/loss earned by branch and is made in the same manner as usual profit and loss account.

4. **Branch Assets/Liabilities Account:** These accounts are made in the usual manner according to the double entry system.

The various journal entries made under this system are as follows:

(1) For goods supplied to branch by the HO.

Branch Stock A/c Dr.

To Goods sent to branch A/c (with invoice price of goods sent)

(2) For goods returned by branch to HO.

Goods sent to branch A/c Dr.

To Branch stock A/c

(3) For goods returned by debtors to branch.

Branch stock A/c Dr.

To Branch debtors A/c

(4) For goods returned by credit customers (debtors) or cash customers direct to HO

Goods sent to branch A/c Dr.

To Branch debtors A/c/Cash A/c

(5) For cash sales made by branch.

Branch Cash/Bank A/c Dr. (With selling price)

To Branch stock A/c

(6) For credit sales made by branch.

Branch debtors A/c Dr. (With selling price)

To Branch stock A/c

To determine gross profit, the excess of invoice price of goods over cost of goods sent to branch is recorded at the time of goods sent. If goods remain unsold at the end of the year stock reserve is created. At the time of sale, the difference of sales price and invoice price of goods sold is recorded. Following six entries are passed for these purposes:

(7) For mark-up (or loading) on opening stock

Stock reserve A/c Dr.

To Branch adjustment A/c

(8) For mark-up (or loading) on closing stock.

Branch adjustment A/c Dr.

To Stock reserve A/c

(9) For mark up on goods sent to branch

Goods sent to branch A/c Dr.

To Branch Adjustment A/c

(10) For mark up on goods received back (returned) by HO

Branch Adjustment A/c Dr.
To Goods sent to Branch A/c

(11) For goods sold at a price higher than Invoice Price

Branch Stock A/c Dr. (with excess of SP over IP)
To Branch Adjustment A/c

(12) For goods sold at a price lower than Invoice Price

Branch Adjustment A/c Dr. (with excess of IP over SP)
To Branch Stock A/c

(13) For Cash/Bank received from branch debtors by branch

Brach Cash/Bank A/c Dr.
To Branch Debtors A/c

(14) For remittance from HO to branch

Branch Cash/Bank A/c Dr.
To Cash/Bank A/c

(15) For remittance from branch to HO

Cash/Bank A/c Dr.
To Branch Cash/Bank A/c

(16) For shortage in branch stock which is considered normal

Branch Adjustment A/c Dr.
To Branch Stock A/c

(17) For shortage in branch stock which is considered abnormal

Branch Adjustment A/c Dr. (with loading on abnormal loss)
Branch P&L A/c Dr. (with cost of abnormal loss)
To Branch Stock A/c

(18) For closing goods sent to branch account

Goods sent to branch A/c Dr.
To Trading/Purchase A/c

Golden Rules under Stock and Debtors Method:

1) **Goods sent to branch accounts** – shall always be shown at cost price.
If it is not at cost (but any amount is at Invoice Price/Cost Price), then in the opposite side show the margin/markup which is over and above cost to make it at cost price. Such margin is known as "Branch Adjustment Account".

2) **Branch stock account:** shall always be shown at Invoice Price. If it is not at Invoice price (i.e., shown at other than Invoice Price) then on opposite side show the margin/markup to make it at Invoice price.
3) Under Branch Stock account, if closing stock is already recorded then while closing this account, if balancing figure appears on credit side then such balancing figure will be treated as shortage.
   Following Journal Entry is passed:

Branch Profit & Loss A/c	Dr.	Cost	
Branch Adjustment A/c	Dr.	Margin	
To Branch Stock A/c			Invoice Price

4) Opening stock and closing stock under branch stock account are shown at Invoice Price, therefore stock reserve (margin) shall be calculated shown under Branch Adjustment A/c
5) Under Branch Stock Account, if balancing figure appears on the debit side then it is to be treated as surplus (i.e., Goods sold to customer at above Issue Price) hence fully transferred to branch adjustment account.

EXAMPLE 12: -

Head Office sent goods to Branch @Cost Only.

Opening stock with Branch = 12,000; Goods sent to Branch = 1,08,000; Cash sales by Branch = 46,000; Credit sales by Branch = 60,000; Closing Stock at Branch = 30,000

Prepare Branch Stock A/c.

SOLUTION:

Branch Stock A/c

To Balance B/d	12,000	By Branch Cash	46,000
To goods sent to Branch	1,08,000	By Branch Debtors	60,000
To Branch Adjustment	16,000	By Balance C/d	30,000
	1,36,000		**1,36,000**

*Branch Adjustment A/c is a nominal Account & Under this A/c Margin / Loadings / Markups shall be shown.

Branch Stock is Valued at IP

Goods Sent to Branch is Valued at Cost

Head Office sent goods to Branch of Rs. 1,50,000 (IP)

IP = Cost + 20%

Journal Entry

Branch Stock A/c	Dr.	1,50,000	
To Goods sent to Branch A/c			1,50,000

Branch Stock A/c (IP)

To goods sent to Branch	1,50,000	By Branch Cash	1,50,000

Goods Sent to Branch A/c (Cost)

To Branch Adjustment	25,000	By Branch Stock (IP)	1,50,000

Branch Adjustment A/c (Nominal)

To Branch P&L	25,000	By Goods sent to Branch	25,000

HO Trading A/c

		By Goods sent to Branch	1,25,000

EXAMPLE 13: -

Opening stock with Branch = 50,000; Goods sent to Branch = 3,24,000; Goods returned by Branch = 25,000; Cash sales by Branch @IP = 87,500; Credit sales by Branch @SP = 2,70,000; Closing Stock at Branch = 36,500

Cost = 100; IP = 125 & SP = 150

SOLUTION:

Branch Stock A/c (IP)

To Balance B/d	50,000	By Goods Sent to Branch	25,000
To goods sent to Branch	3,24,000	By Branch Cash (4)	87,500
To Branch Adjustment (3)	45,000	By Branch Debtors (5)	2,70,000
		By Balance C/d (6)	36,500
	4,19,000		**4,19,000**

Goods Sent to Branch A/c (Cost)

To Branch Adjustment (2)	64,800	By Branch Stock	3,24,000
To Branch Stock	25,000	By Branch Adjustment (3)	5,000
To HO Trading A/c (7)	2,39,200		
	3,29,200		**3,29,200**

Branch Adjustment A/c (Loading)

To Goods Sent to Branch (3)	25,000	By Balance B/d (1)	10,000
To Branch P&L A/c (8)	1,07,500	By Goods sent to Branch (2)	64,800
To Balance C/d (SR) (6)	7,300	BR Branch Stock (5)	45,000
	1,39,800		**1,39,800**

Justification of Above Figures:

1) This 10,000 is a Loading on Opening Stock, Last year it was closing & We must have reversed last year profit since it was unsold.
   In CY we are assuming it will be SOLD, therefore we are again recording the profit 10,000 of HO.
2) 64,800/- is a profit of HO which we are showing separately when HO sent Goods to Branch. This Profit is not yet earned Since goods are not yet sold by Branch. Hence it is Credited in Branch Adjustment A/c (Suspense) A/c.
   When Goods will be sold by Branch this Profit will be earned & Accordingly Branch Adjustment (Suspense) to be reversed & Transfer to P&L A/c.
3) 5,000/- is a profit which is not to be earned since goods are returned by Branch to HO. Hence Branch Adjustment A/c is Debited by 5,000 to reflect the reversal of HO Profit.
4) No need to Calculate Loading because goods are actually Sold. Hence, HO has earned the profit & the profit on such Sale is already included in 64,800/- figure as credit of Branch Adjustment.

5) 2,70,000 is a sale which is above IP i.e. Branch has earned extra Profit of 45,000 which was earlier not recorded in Branch Adjustment (Suspense)

6) Since these are Unsold goods, therefore Profit credited by HO in Branch Adjustment earlier (i.e. 64,800), now Proportionate Profit i.e. 7,300 on Unsold Portion Shall be Reversed.

7) Goods Sent to Branch is as good as sales for HO therefore, this balance should be shown as Credit Sale of Trading A/c @Cost.

8) Cash Sale = 87,500 IP
Profit = 87,500 / 125 x 25 = 17,500
Credit Sale = 2,70,000 / 150 x 50 = 90,000

EXAMPLE 14:

Delhi HO sends goods to its Pune branch at 20% above cost. Branch has been instructed by HO to sell goods as under: -
Cash sales at IP
Credit sales at SP (Which is 50% above cost)

1) Opening stock = Rs. 75,000 (IP)
2) Goods sent to branch = Rs. 5,40,000 (IP)
3) Cash sales = Rs. 1,08,000 (IP)
4) Credit sales = Rs. 4,65,000 (SP)
5) Sales return by credit customer = Rs. 22,500 (SP)
6) Sales return by cash customer =Rs. 12,000 (IP)
7) Goods return by branch to HO = Rs. 48,000 (IP)
8) Goods received by branch till year end = Rs. 5,10,000 (IP)
9) Closing stock at the end = Rs. 72,000 (IP)

SOLUTION

Opening Stock (Cost) – 62,500 + Net Goods Sent to Branch – 4,10,000 ((5,40,000 – 48,000) / 120 x 100)				
Total (IP) – 4,72,500				
COGS (IP) 1) Cash Sales: Net Sales = 96,000 / 120 x 100 COGS (Cash) = 80,000 2) Net Credit Sales = 4,42,500 (SP) COGS = 4,42,500 / 150 x 100 = 2,95,000 Total COGS = 3,75,000	**Closing Stock** 60,000	**Goods in Transit** 25,000	**Shortage (b/f)** 12,500	**Gross Profit** 1,63,500

Memorandum Branch Trading and P&L A/c

To Opening Stock	62,500	By Sales Net Cash Net Credit	 96,000 4,42,500
To Net Goods sent to Branch	4,10,000	By Shortage	12,500
To Gross Profit	1,63,500	By Closing Stock In Hand In Transit	 60,000 25,000

	6,36,000		**6,36,000**
To Abnormal Loss	12,500	By Gross Profit	1,63,500
To Net Profit	1,51,000		
	1,63,500		**1,63,500**

2.4 DEBTORS SYSTEM

- Branch account is nominal account which calculates the profit/loss made by the branch.
- Under this system, entries are recorded assuming the Branch is the Debtor of HO.
- Here, only the transactions between HO and Branch are to be recorded (except one special transaction), i.e. any transaction between branch and outside party is to be ignored while preparing branch account.
- While preparing Branch A/c under this method, balances of various accounts such as stock a/c, debtor's a/c, cash a/c etc. may be missing and it is not possible to complete the Branch A/c without knowing such required missing figures.
- Such missing figures/balances can be found out with the help of 'Stock and Debtors' method and hence Stock and Debtors method is also prepared to complete the Branch A/c under Memorandum basis and only account prepared under double entry basis is the 'Branch A/c'.

The various journal entries made under this system are as follows:

(1) For goods supplied to branch from HO

Branch A/c Dr.
To Goods sent to branch A/c (with invoice price, if any)

(2) For goods returned by branch to HO

Goods sent to branch A/c Dr.
To Branch A/c (with invoice price, if any)

(3) For goods returned direct to HO (Special Transaction)

Credit Customers (Debtors):

Goods sent to branch A/c Dr.
To Branch A/c

Cash Customers:

Goods sent to branch A/c Dr. and Branch A/c Dr.
To Branch A/c To Cash A/c

(4) For remittance from HO to branch for expenses or for any purpose

Branch A/c Dr.
To Cash/Bank A/c

(5) For cash received by HO from branch

Cash/Bank A/c Dr.
To Branch A/c

(6) To remove loading on opening stock and closing stock

Opening Stock:

Stock Reserve A/c Dr.
    To Branch A/c

Closing Stock:

Branch A/c Dr.
    To Stock Reserve A/c

(7) Following Transactions Shall not be recorded in Branch A/c: -

(i) Sale made by Branch
(ii) Expenses Incurred by Branch
(iii) Shortage of Goods @Branch
(iv) Cash collection from Debtors by Branch
(v) Sales return to Branch

(8) Apart from above transaction which are to be recorded in Branch A/c, HO Shall maintain Opening & Closing Balances of Branch Assets & Branch Liabilities to prepare Consolidated Balance Sheet of Business

(a) To Maintain Closing Branch Assets: -

Branch Stock A/c Dr.
Branch Cash A/c Dr.
Branch Debtors A/c Dr.
Branch Other Assets A/c Dr.
    To Branch A/c

(b) To Maintain Closing Branch Liabilities: -

Branch A/c Dr.
    To Branch Liabilities A/c

(c) To eliminate Branch Assets & Branch Liabilities in the next year (i.e. Opening Branch Assets & Opening branch Liabilities): -

(i) Branch A/c Dr.
    To Branch Stock A/c
    To Branch Debtors A/c
    To Branch Cash A/c
    To Branch Other Asset A/c

(ii) Branch Liabilities A/c Dr.
    To Brach A/c

(9) Under this Method, if goods are recorded at IP Value, then on Opposite side of Branch A/c, Loading shall be recorded. So that the Ultimate effect can be Shown at Cost Only.

(10) Cash remittance is Very Important Figure to prepare Branch A/c. If it is missing in Question then it is to be found out by preparing Branch Cash A/c in working Note.

(11) If any Opening/Closing Balances are missing Like Stock / Debtors / Cash / Other Assets we shall prepare working note of that A/c

EXAMPLE 15: -

This is the First Year of Operation of Branch.

(a) Head Office Sent Goods to Branch 10,00,000 (Cost = IP)

(b) Out of above, 3,00,000 Cost of Goods sold at 4,00,000 in cash

(c) Out of above goods sent, Goods Costing 4,00,000 sold on Credit at 5,50,000

(d) Collection from Debtors by Branch 3,70,000

(e) Bad Debts of Rs. 20,000/-

(f) Branch return the goods to Head Office = 50,000

(g) Cash remitted to Head Office is 7,00,000

Assume no other Transaction by Branch during the Year

SOLUTION:

Branch A/c

To Goods Sent to Branch A/c	10,00,000	By Goods sent to Branch A/c	50,000
To Net Profit of Branch A/c (Balancing fig.)	2,30,000	By Cash (remittance)	7,00,000
		By Balance C/d Branch Debtors Branch Stock Branch Cash	 1,60,000 2,50,000 70,000
	12,30,000		**12,30,000**

31/3 – Taking Closing Balances of Branch Assets

Branch Debtors A/c Dr. Branch Cash A/c Dr. Branch Stock A/c Dr. To Branch A/c	1,60,000 70,000 25,000	 4,80,000

Memorandum Branch Trading A/c

To Opening Stock	0	By Sales	9,50,000
To Goods Sent to Branch	10,00,000	By Goods returned to HO	50,000
To Gross Profit	2,50,000	By Closing Stock	2,50,000
	12,50,000		**12,50,000**
To Bad Debts	20,000	By Gross Profit	2,50,000
To Net Profit	2,30,000		
	2,50,000		**2,50,000**

EXAMPLE 16: -

In Continuation of Above Example 15.

(a) Goods Sent to Branch = 12,00,000

(b) Goods Costing 5,00,000 sold @6,30,000 in Cash

(c) Goods Costing 7,00,000 Sold @9,00,000 on Credit

(d) Cash Collection from Debtors = 8,70,000

(e) Cash Remittance to HO is 14,50,000

(f) Branch Expenses in Cash by Branch is 30,000

(g) Branch Expenses incurred by HO is 10,000

(h) Shortage of goods at Branch = 25,000

SOLUTION:

Branche A/c

To Balance B/d Stock Debtors Cash	 2,50,000 1,60,000 70,000	By Cash (remittance)	14,50,000
To Goods Sent to Branch A/c	12,00,000	By Balance C/d Branch Stock Branch Debtors Branch Cash	 2,25,000 1,90,000 90,000
To Cash A/c (Exp met by HO)	10,000		
To Net Profit of Branch A/c (Bal. Fig.)	2,65,000		
	19,55,000		**19,55,000**

Memorandum Branch Trading A/c

To Opening Stock	2,50,000	By Sales Cash Credit	 6,30,000 9,00,000
To Goods Sent to Branch	12,00,000	By Shortage	25,000
To Gross Profit	3,30,000	By Closing Stock	2,25,000
	17,80,000		**17,80,000**
To Expenses (30+10)	40,000	By Gross Profit	3,30,000
To Abnormal Loss	25,000		
To Net Profit	2,65,000		
	3,30,000		**3,30,000**

Branche Cash A/c

To Opening	70,000	Cash remittance	14,50,000
Cash Sale	6,30,000	Expenses	30,000
Collection	8,70,000	Closing	90,000
	15,70,000		**15,70,000**

Branche Debtors A/c

To Opening	1,60,000	Collection	8,70,000
Sale	9,00,000	Closing	1,90,000
	10,60,000		**10,60,000**

EXAMPLE 17: -

Opening Balances at Branch

Stock – 50,000 (IP); Debtors – 1,20,000 & Cash – 30,000

(a) Goods Sent to Branch at IP = 6,25,000

(b) Sale by Branch = 5,50,000 (Credit Sale Only)

(c) No Cash Sale

(d) Collection from Debtors is 6,10,000

(e) Bad Debts = 5,000

(f) Expenses by Branch = 25,000

(g) Closing Cash = 15,000

(h) Closing Stock = 1,75,000 (IP)

IP = Cost + 25%

Prepare Branch A/c By Debtors Method

SOLUTION:

Branch Debtors A/c

To Opening	1,20,000	Collection	6,10,000
Sale	5,50,000	Bad Debts	5,000
		Closing	55,000
	6,70,000		**6,70,000**

Branche Cash A/c

To Opening	30,000	Cash remittance	6,00,000
Collection	6,10,000	Expenses	25,000
		Closing	15,000
	6,40,000		**6,40,000**

Branch A/c

To Balance B/d Stock Debtors Cash	 50,000 1,20,000 30,000	By Balance B/d (SR)	10,000
To Goods Sent to Branch A/c	6,25,000	By Goods Sent to Branch	1,25,000
To Net Profit of Branch A/c	1,20,000	By Cash	6,00,000
To Balance C/d (SR)	35,000	By Balance C/d Branch Stock Branch Debtors Branch Cash	 1,75,000 55,000 15,000
	9,80,000		**9,80,000**

3. ACCOUNTING FOR INDEPENDENT BRANCHES

(1) In case of independent branches both branch as well as HO maintain their books.

(2) Since branch maintains their own books, it can independently calculate its result by preparing its own Trail balance, Trading a/c and P&L a/c, also it can make its own Balance Sheet.

(3) The accounts are prepared in usual manner and both HO and Branch maintain an account for each other in their own books. (i.e., branch a/c in HO books and HO a/c in branch books)

(4) There are certain transactions which need to be focused. These are as under:

a) Inter-branch transactions

b) Accounting for Fixed Assets of the branch

c) Common expenses incurred by HO to be charged to the branch.

(a) INTER-BRANCH TRANSACTIONS:

For accounting point of view, whenever transactions between branches occur, they are recorded in the books of HO/Branches as if they have been done through the HO. The following journal entries shall be made in the books of HO and branches:

Example: Goods transferred by Bhopal branch to Delhi branch

Books of HO	Books of Bhopal Branch	Books of Delhi branch
Delhi Branch a/c Dr. To Bhopal Branch a/c	HO a/c Dr. To Goods received from HO. a/c	Goods received from HO a/c Dr. To HO a/c

(b) ACCOUNTING FOR FIXED ASSETS OF THE BRANCH:

There may be two possibilities as follows:

(i) Account of FA maintained by Branch:

Transactions	HO Books	Branch Books
Payment of FA made by branch	No Entry	FA a/c Dr. To Cash/Bank a/c
Payment of FA made by HO	Branch a/c Dr. To Cash/Bank a/c	FA a/c Dr. To HO a/c
Payment for FA to be made by branch	No Entry	FA a/c Dr. To Creditor for FA a/c
Depreciation on FA	No Entry	Depreciation a/c Dr. To FA a/c

(ii) Account of FA maintained by HO:

Transactions	HO Books	Branch Books
Payment of FA made by branch	Branch FA a/c Dr. To Branch a/c	HO a/c Dr. To Cash/Bank a/c
Payment of FA made by HO	Branch FA a/c Dr. To Cash/Bank a/c	No Entry
Payment for FA to be made by branch	Branch FA a/c Dr. To Branch a/c	HO a/c Dr. To Creditor for FA a/c
Depreciation on FA	Branch a/c Dr. To Branch FA a/c	Depreciation a/c Dr. To HO a/c

(c) COMMON HO EXPENSES CHARGED TO BRANCH:

(1) The expenses which are incurred for the sole benefit of the HO are to be fully charged to HO Trading/P&L a/c.

(2) The expenses which are incurred for the sole benefit of Branch are to be fully charged to Branch Trading/P&L a/c.

(3) The expenses which are incurred for the benefit of both are needed to be allocated between HO and Branch in the ratio of benefit derived by both of them. Following accounting entries are made:

HO BOOKS	BRANCH BOOKS
(1) Expenses a/c Dr. To Cash/Bank a/c And If the expenses a/c is not closed Branch a/c Dr. To Expenses a/c (Proportionate share of branch) (Or) If expenses a/c is closed Branch a/c Dr. To Trading/P&L a/c (Proportionate share of branch)	Expenses A/c Dr. To HO A/c (Proportionate Expenses of Branch)

RECONCILIATION OF HO AND BRANCH BALANCE:

1. In case of independent branches, branch prepares its own Trail balance.
2. Hence, we need to incorporate the branch trail balance in the books of HO in order to ascertain the position of the group as a whole.
3. But before incorporation of branch TB in the books of HO, it is to be ensured that branch a/c in the books of HO and HO a/c in the books of branch should have equal and reciprocal balance.
4. If the both accounts in either books are not matched then they need to be reconciled before incorporating the branch Trail balance in HO books. Following are some CASES by which we can understand the reconciliation process:

CASE 1

When disagreement in the two accounts is because of the transit items, it would mean that record of transaction in one set of books only. It can be corrected by recording the aspect in the set of books where it is still not recorded.

Example 1: HO has sent goods to branch of 50,000 but branch received goods of the value of 30,000 till the end of accounting year. Here, HO has already done its part of recording. The branch should record these goods as Goods in transit as follows:

Goods in Transit a/c Dr.
To HO a/c

Later on, when goods are actually received by the branch in the next accounting year, the branch can pass following entry:
Goods received from HO a/c Dr.
To Goods in Transit a/c

Example 2: Similarly, if branch has sent cash of 80,000 to HO but HO received cash of 70,000 till the end of accounting year. Here HO should record such transaction as follows:
Cash in transit a/c Dr.
To Branch a/c

Later on, when cash is actually received by the HO in the next accounting year, the HO can pass following entry:
Cash a/c Dr.
To Cash in Transit a/c

CASE 2

Disagreement in two accounts is because of items other than transit items. Following are some exampls:
Example 1: Entries for reconciliation needed in HO books:

Particulars	Entry in branch books already done	Entry in HO books needed for reconciliation
HO creditors paid by branch	HO a/c Dr. To Cash a/c	Creditors a/c Dr. To Branch a/c
HO debtors made payment to branch	Cash a/c Dr. To HO a/c	Branch a/c Dr. To Debtors a/c
HO income (e.g., rent received on behalf of HO) received by branch	Cash a/c Dr. To HO a/c	Branch a/c Dr. To Rent a/c

Example 2: Entries for reconciliation needed in branch books:

Particulars	Entry in HO books already done	Entry in Branch books needed for reconciliation
Branch creditors paid by HO	Branch a/c Dr. To Cash a/c	Creditors a/c Dr. To HO a/c
Branch debtors made payment to HO	Cash a/c Dr. To Branch a/c	HO a/c Dr. To Debtors a/c
Branch income (e.g., rent received on behalf of branch) received by HO	Cash a/c Dr. To Branch a/c	HO a/c Dr. To Rent a/c

4. INCORPORATION OF BRANCH TRAIL BALANCE IN HO BOOKS

For incorporation of Branch Trial balance in the books of HO, following entries are needed to be made in the books of HO:

1. **For incorporating branch profit/loss:**

   Branch a/c Dr. (With the amount of Branch Profit)

   To Branch Profit and Loss a/c

   Branch Profit and Loss a/c Dr. (With the amount of Branch Loss)

   To Branch a/c

2. **For incorporating the Assets of the branch:**

   Branch Assets a/c Dr.

   To Branch a/c

   (all assets individually including transit items recorded by branch)

3. **For incorporating the Liabilities of the branch:**

   Branch a/c Dr.

   To Branch Liabilities a/c (all liabilities individually excluding HO a/c)

5. Foreign Branch (AS 11)

1) There are two types of Currencies: -

(a) Reporting Currency

(b) Foreign Currency

2) Currency Used by Head Office is Called Reporting Currency

Currency Used by Branch is Called Foreign Currency

3) Foreign Currency means any currency which is other than Reporting Currency

4) We have to Convert Foreign Currency Trail Balance of Branch into Reporting Currency, why? Because Head Office wants to prepare Consolidated Financial Statement in Reporting Currency.

5) **Foreign Operation: -** Head Office Conducting its business in Foreign Country through a Branch / Subsidiary Company / Associate Company / Joint Venture

Types of Foreign Operations:

(a) Integral Foreign Operation (IFO):

IFO does not have its own separate management or BOD. It is dependent on Head Office for almost all Decisions.

E.g.: Branch

(b) Non-Integral Foreign Operation (NIFO):

NIFO has its own management e.g., BOD. It is not dependent on small day to day decision on Head Office.

E.g.: Subsidiary / Associate / Joint Venture

6) Integral Foreign Operation: -

Apply following Rules to convert Foreign Currency Train Balance into Reporting Currency:

(a) All Monetary Assets / Liabilities – Closing Exchange Rate

(b) Non-Monetary Assets / Liabilities which are measured at Cost (e.g., FA, Acc. Dep on FA) – Spot Rate (i.e., Historical Rate)

(c) Non-Monetary Assets / Liabilities which are measured at other than Cost (e.g., NRV / FV / MV) – Exchange Rate on the Date of Measurement

(d) All Incomes & Expenses (Revenue Items) – Average Exchange Rate

(e) Head Office A/c & Goods received from HO A/c – No Exchange Rate (Take same Balance appearing in HO Books)

(f) Opening Stock – Opening Exchange Rate

(g) Closing Stock – Closing Exchange Rate

Notes: -

a) Closing Exchange Rate: Means Exchange Rate as of Balance Sheet Date

b) Spot Rate: Means Exchange Rate as on actual Transaction Date

c) Average Exchange Rate: (Opening + Closing) / 2

d) Monetary Assets / Liabilities: - Means Cash/Bank or any asset which is recoverable in a Fixed Amount or any Liability which is to be settled in a Fixed Amount.

e) Non-Monetary Assets / Liabilities: - Other than Monetary (i.e., No Fixed Amount is Determinable)

7) After Conversion of train Balance from Foreign Currency to Reporting Currency, Exchange Difference may arise (Maybe Dr. Side is higher or lower than Credit side)
Exchange Difference shall be Transfer to Profit & Loss A/c of Branch (Loss Dr. / Gain Credit)

8) Rules for Conversion of Non-Integral Foreign Operation

(a) All Assets & Liabilities (Monetary & Non-Monetary) – Closing Exchange Rate

(b) All Revenue Items – either Actual Rate, if Possible, otherwise Average Rate.

(c) Opening Stock – Opening Exchange Rates

(d) Head Office A/c & Goods Received A/c – No Rate (Actual Balance as per HO Books)
Exchange Difference = Transfer to "Foreign Currency Translation Reserve A/c" (FCTR)
FCTR shall be shown in Balance Sheet Under Reserves & Surplus. Either positive figure if Credit Balance or Negative Figure if Debit Balance.
*FCTR shall be transfer to P&L A/c only when NIFO (E.g., Subsidiary) is Sold / Disposed.

Foreign Current Stock at Cost or NRV whichever is lower:

- Stock is always measured at lower of cost or NRV as per AS 2.
- If cost or NRV figures are given in foreign currencies then above measurement shall be applied in reporting currency as under:
  a) Cost (in reporting currency) – Purchase Price ($) × Spot Ex. Rate
  b) NRV (in reporting currency) – NRV ($) × Closing Rate
  Whichever is lower out of above shall be taken in Trial balance of Reporting Currency

Refer Q605

SECTION B – MCQ's

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).

ANSWERS	1.	2.	3.	4.	5.
	c	c	c	a	c

Student Notes: -

Student Notes: -