1. PROFIT OR LOSS PRE AND POST INCORPORATION

ASSIGNMENT SOLUTIONS

PROBLEM NO: 1

Statement showing pre and post incorporation Profit for the year ended 31st March,2014

Particulars	Amount (Rs.)	Basis of Allocation	Pre-incorporation (Rs.)	Post-incorporation (Rs.)
Gross Profit	5,40,000	2:7	1,20,000	4,20,000
Less: Depreciation	1,23,000	1:2	41,000	82,000
Director's Fees	50,000	Post	-	50,000
Preliminary Expenses	12,000	Post	-	12,000
Office Expenses	78,000	1:2	26,000	52,000
Selling Expenses	72,000	2:7	16,000	56,000
Interest to vendors	5,000	Actual	4,000	1,000
Net Profit (Rs.33,000 being pre-incorporation profit is transferred to capital reserve Account)	**2,00,000**		**33,000**	**1,67,000**

WORKING NOTE:

1. **Sales ratio:** The sales per month in the first half year were half of what they were in the later half year. If in the later half year, sales per month is Rs.1 then it should be 50 paise per month in the first half year. So sales for the first four months (i.e. from 1st April, 2013 to 31st July, 2013) will be 4 x 0.50 = Rs.2 and for the last eight months (i.e. from 1st August, 2013 to 31st March, 2014) will be (2 x .50 + 6 x 1) = Rs.7. Thus sales ratio is 2 : 7.
2. **Time ratio:**

   1st April, 2013 to 31st July, 2013 : 1st August, 2013 to 31st March, 2014 = 4 months : 8 months = 1 : 2.

   Thus, **time ratio is 1 : 2.**
3. **Gross profit:**

   Gross profit = Net profit + All expenses

   = Rs.2,00,000 + Rs.(1,23,000 + 50,000 + 12,000 + 78,000 + 72,000 + 5,000)

   = Rs.2,00,000 + Rs.3,40,000 = Rs.5,40,000

PROBLEM NO: 2

Statement showing the calculation of Profit for the Pre - incorporation and Post - incorporation periods

Particulars	Amount (Rs.) (in lakhs)	Basis of Allocation	Pre-incorporation (Rs. in lakhs)	Post-incorporation (Rs. in lakhs)
Gross Profit (25% of Rs.1,600)	400	Sales	100	300
Less: Salaries	69	Time	23	46
Rent, Rates and insurance	24	Time	8	16
Sundry office expenses	66	Time	22	44
Traveller's commission	16	Sales	4	12
Discount allowed	12	Sales	3	9
Bad debts	4	Sales	1	3
Director's fee	25	Post	-	25
Audit Fees	9	Sales*	2.25	6.75
Depreciation on tangible assets	12	Time	4	8
Debenture interest	11	Post	-	11
Net profit	**152**		**32.75**	**119.25**

WORKING NOTE:

1. **Sales ratio:** **(Rs. in Lakhs)**

Particulars	Amount (Rs.)
Sales for the whole year	1,600
Sales upto 31st July, 2012	400
Therefore, sales for the period from 1st August, 2012 to 31st March, 2013	1,200

Thus, sales ratio is = 400 : 1200 = 1 : 3

2. **Time ratio:**

1st April, 2012 to 31st July, 2012 : 1st August, 2012 to 31st March, 2013 = 4 months : 8 months = 1 : 2

Thus, **time ratio is 1 : 2**

3. Audit fees has been assumed to be related with audit and therefore apportioned into Pre and post incorporation periods on the basis of turnover.

Note: If the audit fees is related to the company then charged it to post incorporation period.

PROBLEM NO: 3

Statement showing calculation of profits for pre and post incorporation periods for the year ended 31.03.2014

Particulars	Pre-incorporation period (Rs.)	Post-incorporation period (Rs.)
Gross profit (1:3)	80,000	2,40,000
Less: Salaries (1:2)	16,000	32,000
Stationery (1:2)	1,600	3,200
Advertisement (1:3)	4,000	12,000
Travelling expenses (W.N.4)	4,000	8,000
Sales promotion expenses (W.N.4)	1,200	3,600
Misc. trade expenses (1:2)	12,600	25,200
Rent (office building) (W.N.3)	8,000	18,400
Electricity charges (1:2)	1,400	2,800
Director's fee (post)	-	11,200
Bad debts (1:3)	800	2,400
Selling agents commission (1:3)	4,000	12,000
Audit fee (1:3)(note 6)	1,500	4,500
Debenture interest (post)	-	3,000
Interest paid to vendor (2:1) (W.N.5)	2,800	1,400
Selling expenses (1:3)	6,300	18,900
Depreciation on fixed assets (W.N.6)	3,000	6,600
Capital reserve (bal. Fig.)	12,800	-
Net profit (Bal. Fig.)	-	74,800

Working Notes:

Pre incorporation period = 1^{st} April, 2013 to 31^{st} July, 2013 i.e. 4 months

Post incorporation period = 8 months

1. Time Ratio = 4 months : 8 months i.e. 1 : 2

2. **Sales ratio:**

Let the monthly sales for first 6 months (i. e. from 1.4..2013 to 30.9.13) be = x

Then, sales for 6 months = 6x

Monthly sales for next 6 months (i.e. from 1.10.13 to 31.3.2014) = $x+\frac{2}{3}x=\frac{5}{3}x$

Then, sales for next 6 months = $\frac{5}{3}x\,X6 = 10x$

Total sales for the year = 6x + 10x = 16x

Monthly sales in the pre incorporation period = Rs.19,20,000 / 16 = Rs.1,20,000

Total sales for pre-incorporation period = Rs.1,20,000 X 4 = Rs.4,80,000

Total sales for post incorporation period = Rs.19,20,000 - Rs.4,80,000 = Rs.14,40,000

Sales Ratio = 4,80,000 : 14,40,000 = 1 : 3

3. Rent:

Particulars	Rs.	Rs.
Rent for pre-incorporation period (Rs.2,000 X 4)		8,000 (pre)
Rent for post incorporation period		
August, 2013 & September, 2013 (Rs.2,000 X 2)	4,000	
October, 2013 to March, 2014 (Rs.2,400 X 6)	14,400	18,400(post)

4. Travelling expenses and sales promotion expenses:

Particulars	Pre (Rs.)	Post (Rs.)
Traveling expenses Rs.12,000 (i.e. Rs.16,800 - Rs.4,800) distributed in 1:2 ratio	4,000	8,000
Sales promotion expenses Rs.4,800 distributed in 1:3 ratio	1,200	3,600

5. Interest paid to vendor till 30th September, 2013:

Particulars	Pre (Rs.)	Post (Rs.)
Interest for pre-incorporation period $\left(\frac{Rs.4,200}{6} X\,4\right)$	2,800	
Interest for post incorporation period i.e. for August, 2013 & September, 2013 = $\left(\frac{Rs.4,200}{6} X\,2\right)$		1,400

6. Depreciation:

Particulars	Rs.	Pre (Rs.)	Post (Rs.)
Total depreciation	9,600	-	-
Less: Depreciation exclusively for post incorporation period	600	-	600
	9,000	-	-
Depreciation for pre-incorporation period $\left[9,000 X \frac{4}{12}\right]$	-	3,000	-
Depreciation for post incorporation period $\left[9,000 X \frac{8}{12}\right]$	-	-	6,000
	-	3,000	6,600

Audit fees is assumed to be Tax audit fees, hence allocated on Sales ratio. i.e. 1 : 3

PROBLEM NO: 4

K V Trading Private Limited

Statement showing calculation of profit/loss for pre and post incorporation periods

(Rs. in lakhs)

Particulars	Ratio	Total	Pre Incorporation	Post Incorporation
Sales	1:6	240.00	34.29	205.71
Interest on Investments	Pre	6.00	6.00	-
Bad debts recovered	Pre	0.50	0.50	-
(i)		246.50	40.79	205.71
Cost of goods sold	1:6	102.00	14.57	87.43

Advertisement	1:6	3.00	0.43	2.57
Sales commission	1:6	6.00	0.86	5.14
Salary (W.N.3)	1:5	18.00	3.00	15.00
Managing directors remuneration	Post	6.00	-	6.00
Interest on Debentures	Post	2.00	-	2.00
Rent (W.N.4)		5.50	0.93	4.57
Bad debts (1 + 0.5)	1:6	1.50	0.21	1.29
Underwriting commission	Post	2.00	-	2.00
Audit fees	Post	2.00	-	2.00
Loss on sale of Investment	Pre	1.00	1.00	-
Depreciation	1:3	4.00	1.00	3.00
(ii)		153.00	22.00	131.00
Net Profit [(i) - (ii)]		93.50	18.79	74.71

Working Notes:

1. **Calculation of Sales Ratio**

   Let the average sales per month be x

   Total sales from 01.04.20X2 to 30.06.20X2 will be 3x

   Average sales per month from 01.07.20X2 to 31.03.20X3 will be 2x

   Total sales from 01.07.20X2 to 31.03.20X3 will be 2x X 9 =18x

   Ratio of Sales will be 3x: 18x i.e. 3:18 or 1:6

2. **Calculation of time Ratio:** 3 Months: 9 Months i.e. 1:3

3. **Apportionment of Salary**

   Let the salary per month from 01.04.20X2to 30.09.20X2 is x

   Salary per month from 01.10.20X2 to 31.03.20X3 will be 2x

   Hence, pre incorporation salary (01.04.20X2 to 30.06.20X2) = 3x

   Post incorporation salary from 01.07.20X2 to 31.03.20X3 = (3x + 12x) i.e.15x

   Ratio for division 3x: 15x or 1: 5

4. **Apportionment of Rent**

	Rs. Lakhs		
Total Rent	5.5		
Less: additional rent from 1.7.20X2 to 31.3.20X3	1.8		
Rent of old premises for 12 months	3.7		
Apportionment in time ratio		0.925	2.775
Add: Rent for new space		-	1.800
Total		0.925	4.575

PROBLEM NO: 5

Pre-incorporation period is for two months, from 1st April, 2017 to 31st May, 2017.

Pre-incorporation period is for ten months, from 1st June, 2017 to 31st March, 2018.

Statement showing calculation of profit/losses for pre and post incorporation periods

Particulars	Pre - Incorporation (Rs.)	Post - Incorporation (Rs.)
Gross Profit	50,000	4,00,000
Bad debts Recovery	14,000	
	64,000	4,00,000
Less: Salaries	24,000	1,20,000
Audit fees	-	12,000

Depreciation	3,000	16,250
Sales commission	2,000	16,000
Bad Debts (49,000 + 14,000)	7,000	56,000
Interest on Debentures	-	36,000
Rent	4,000	34,400
Net Profit	24,000	1,09,350

Working Notes:

i) Calculation of ratio of Sales:

Sales from April to September = Rs. 6,00,000 (Rs. 1,00,000 p.m. on average basis)

Oct. to March = Rs. 12,00,000 (Rs. 2,00,000 p.m. on average basis)

Thus, sales for pre-incorporation period = Rs. 2,00,000

post-incorporation period = Rs. 16,00,000

Sales are in the ratio of 1:8

ii) Gross profit, sales commission and bad debts written off have been allocated in pre and post incorporation periods in the ratio of Sales.

iii) Rent, salary are allocated on time basis.

iv) Interest on debentures is allocated in post incorporation period.

v) Audit fees charged to post incorporation period as relating to company audit.

vi) Depreciation of Rs. 18,000 divided in the ratio of 1:5 (time basis) and Rs. 1,250 charged to post incorporation period.

vii) Bad debt recovery of Rs. 14,000/- is allocated in pre-incorporation period, being sale made in 2014-15.

viii) Rent: Rs. 38,400 - Additional rent for 6 months)	**Amount (Rs.)**
[38,400- 14,400 (2,400 x 6)]	24,000
1/4/17 -31/5//17 (2,000 x 2)	4,000
1/6/17 -31/3/18 - [(2,000 x 10) +14,400]	34,400
	38,400

PROBLEM NO: 6

Statement showing calculation of profits for pre and post incorporation periods for the year ended 31.03.15 (15 Months)

Particulars	Total (Rs.)	Ratio	Pre (Rs.)	Post (Rs.)
Gross profit	1,40,40,000	1:8	15,60,000	1,24,80,000
Less: Salaries	23,40,000	1:12	1,80,000	21,60,000
Depreciation	3,60,000	1:4	72,000	2,88,000
Advertisement	14,04,000	1:8	1,56,000	12,48,000
Discount	23,40,000	1:8	2,60,000	20,80,000
Managing director's remuneration	1,80,000	Post	-	1,80,000
Office cum showroom rent	14,40,000	Actual	1,80,000	12,60,000
Miscellaneous office expenses	2,40,000	1:4	48,000	1,92,000
Interest	19,02,000	Actual	7,02,000	12,00,000
Goodwill (bal. fig.)			38,000	--
Net profit (B.f.)			--	38,72,000

Note: Since the profits prior to incorporation are in the negative, they would be treated as goodwill.

Working Notes:

1.	**Calculation of Time Ratio:**	
	Pre-Incorporation Period	Post-Incorporation Period
	1st January, 2014 to 31st March, 2014 (3 months)	1st April, 2014 to 31st March, 2015 (12 months)
	3:	12
	1:	4
2.	**Calculation of Sales Ratio:**	
	Pre-Incorporation Period	Post-Incorporation Period
	3 Months	12 Months
	3 x 1	12 x 2
	3:	24
	1:	8
3.	**Calculation of Staff Salary Ratio:**	
	Pre-Incorporation Period	Post-Incorporation Period
	3 Months	12 Months
	3 x 1	12 x 3
	3:	36
	1:	12
4.	**Calculation of Interest:**	
	Pre-Incorporation Period	Post-Incorporation Period
	2,34,00,000 x 3/12 x 12/100 = Rs. 7,02,000	1,00,00,000 x 12/100 = Rs. 12,00,000
5.	**Calculation of Rent:**	
	Rent on additional space	
	1st July 2014 to 31st March, 2015	= 9 Months
	Total additional rent = 60,000 x 9	= Rs. 5,40,000
	Remaining rent on earlier space	= 14,40,000 - 5,40,000 = Rs. 9,00,000
	Rent per month = $\frac{\text{Rs. 9,00,000}}{\text{15 months}}$ = Rs. 60,000 p.m.	
	Pre-Incorporation Period rent = 60,000 x 3	= 1,80,000
	Post-Incorporation Period rent = 60,000 x 12	= 7,20,000
	Additional rent	= 5,40,000
		12,60,000

6. Calculation of Gross Profit:

Dr. **Trading Account** **Cr.**

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Cost of goods sold	3,27,60,000	By Sales	4,68,00,000
To Gross profit (Bal. fig.)	1,40,40,000		
	4,68,00,000		4,68,00,000

Note:

1. Pre incorporation period is 3 months upto 31st March 2014 and post incorporation period is of 12 months
2. As advertisement cost and discounts are directly related to sales, it is proper to assume that they would be incurred in the same ratio of time as Sales. Hence, 1 : 8
3. Since Managing Director is a position which is appointed in a company, it is proper to consider that his pay is incurred during the post incorporation period.
4. Interest on money borrowed to pay the purchase consideration is a post incorporation cost whereas the interest on purchase consideration for 3 months till payment will be pre incorporation cost.

PROBLEM NO: 7

Fellow Travellers Ltd.

Statement showing calculation of profit /losses for pre and post incorporation periods

		Ratio	Pre-incorporation	Post-incorporation
Gross profit allocated on the basis of sale		1:2	20,000	40,000
Less: Administrative Expenses allocated				
On time basis:				
(i) Salaries and wages	10,000			
(ii) Depreciation	1,000			
	11,000	5:7	4,583	6,417
Selling Commission on the basis of sales		1:2	3,000	6,000
Interest on Purchase Consideration (Time basis)		5:1	7,500	1,500
Expenses applicable wholly to the Post-incorporation period:				
Debenture Interest (1,50,000 x 7% x 6/12)	5,250			
Director's Fee	600			5,850
Preliminary expenses				900
Provision for taxes				6,000
Balance c/d to Balance Sheet			**4,917**	**13,333**

Time Ratio:

Pre incorporation period = 1 January 20X1 to 31 May 20X1 = 5 months

Post incorporation period = 1 June 20X1 to 31 December 20X1 = 7 months

Time ratio = 5: 7

Sales Ratio:

Sales in pre incorporation period (1 January 20X1 to 31 May 20X1) = Rs. 60,000

Sales in post incorporation period (1 June 20X1 to 31 December 20X1) = Rs. 1,20,000

Sales ratio = 1:2

Fellow Travellers Ltd.

Extract from the Balance Sheet as on 31st Dec., 20X1

Particulars	Notes	Amount (Rs.)
Equity and Liabilities		
1. Shareholders' funds		
a) Share capital	1	2,00,000
b) Reserves and Surplus	2	33,250
2. Non-current liabilities		
a) Long-term borrowings	3	1,50,000
3. Current liabilities		
a) Short term provisions	4	6,000
Total		**3,89,250**

Notes to accounts:

Particulars		Amount (Rs.)
1. Share Capital		
20,000 equity shares of Rs. 10 each fully paid		2,00,000
2. Reserves and Surplus		
Profit Prior to Incorporation		4,917
Securities Premium Account		20,000
Profit and loss Account	13,333	
Less: Dividend on equity share	(5,000)	8,333
Total		33,250
3. Long term borrowings		
Secured		

7% Debentures	1,50,000
4. Other Current liabilities	
Provision for Taxes	6,000

PROBLEM NO: 8

Statement showing the calculation of profits/losses for pre incorporation and Post incorporation period profits for the year ended 31st March, 2014

Particulars	Basis	Pre	Post
Sales (given)		10,000	40,000
Less: Purchases	1:3.3	5,814	19,186
Carriage Inwards	1:3.3	237	782
Gross Profit (i)		3,949	20032
Less: Selling Expenses & Variable Expenses	1:4	700	2800
Preliminary Expenses			1200
Salaries	1:3	900	2700
Director Fees			1200
Interest on capital		700	
Depreciation	1:3	700	2100
Rent	1:3	1200	3600
Total of Expenses(ii)		4200	13,600
Capital Loss/Net Profit (i -ii)		**(251)**	**6,432**

Working Notes:

1. Sales Ratio = 10,000 : 40,000 = 1 :4

2. **Time** Ratio = 3:9 = 1:3

3. **Purchase** Price Ratio

$\therefore$ Ratio is 3 : 9

But purchase price was 10% higher in the company period

$\therefore$ Ratio is 3 : 9 + 10%

3:9.9 = 1:3.3.

THE END