1. PROFIT OR LOSS PRE AND POST INCORPORATION

NO. OF PROBLEMS IN 42e OF CA INTER: CLASSROOM - 06, ASSIGNMENT - 08

NO. OF PROBLEMS IN 41.5e OF CA INTER: CLASSROOM - 05, ASSIGNMENT – 06

NO. OF PROBLEMS IN 42.5(2nd Version) OF CA INTER: CLASSROOM - 05, ASSIGNMENT - 07

MODEL WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC & CA INTER

MODEL NO.	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)	M-19 (N)
Profit or loss Prior to incorporation	06	-	-	08	-	08	-	10	08	-	04	08	-	08	10	-	12	4

SIGNIFICANCE OF EACH PROBLEM COVERED IN THIS MATERIAL

Problem No. in this material	Problem No. in NEW SM	Problem No. in OLD SM	Problem No. in old PM	RTP	MTP	Previous Exams	Remarks
CR 1	ILL-7	ILL-4	-		-	M-15	
CR 2	-	-	-	-	-	N-18(N)	
CR 3	PQ-3	-	8	-	-	N-17	
CR 4	-	-		-	-	M-18(O)	
CR 5	-	-		-	-	N-11	
ASG 1	ILL-1	-	3	-	-	-	
ASG 2	ILL-6	-	2	-	M-18(N&O)	-	
ASG 3	PQ-2	-	7	-	-	-	
ASG 4	-	-	-	N-14	M-18(N&O)	-	
ASG 5	-	-	-	N-15	-	-	
ASG 6	ILL-3	ILL-2	-	-	-	-	
ASG 7	-	-	-	-	-	-	

THEORY

Introduction:

1. Profit or loss of a business for the period prior to the date the company incorporated is referred to as pre-incorporation profits or losses.
2. Such profits or losses, though belonging to the company or payable by it, are of capital nature.

Note: These profits will not be available for distribution as a dividend among the members of the company.

Treatment in Books of Accounts

If profit

1. It is transferred to Capital Reserve Account (i.e. Capitalized) (or) to the goodwill account, if any goodwill has been adjusted as an asset.
2. It can be used for
   - **a)** Writing off Goodwill on acquisition
   - **b)** Writing off Preliminary Expenses
   - **c)** Writing down over-valued assets
   - **d)** Issuing of Bonus shares
   - **e)** Paying up partly paid shares

If Loss

1. If there is a loss, it is either written off by debiting to the Profit and Loss Account or debiting to a special account described as "Loss Prior to Incorporation" and shown as an "asset" in the Balance Sheet,
2. Alternatively, it may be debited to the Goodwill Account.
3. It can be used for:
   - **a)** Setting off against Post-incorporation profit
   - **b)** Addition to Goodwill on acquisition
   - **c)** Writing off capital profit

<u>Methods of Computing Profit or Loss Prior to incorporation:</u> The profit or loss prior to incorporation can be ascertained in any of the following two methods:

1. Separate Final Accounts Method: By keeping all accounting details separately for the two periods and taking stock valuation on the date of incorporation, two separate trading and Profit & Loss Accounts as follows can be prepared.

- **a)** From the date of purchase to the date of incorporation (Pre-incorporation period) and
- **b)** From the date of incorporation to the date of year ending (Post-incorporation period)

But this is not always feasible and practical hence following method can be followed.

2. Single Final Accounts Method:

- **a)** Preparation of Trading A/c for that whole period and to find out the gross profit or gross loss in the usual way.
- **b)** Preparation of Profit & Loss A/c by splitting up into two periods (i.e. pre- incorporation & post-incorporation periods) by apportioning the items appearing in the Profit & Loss A/c on some equitable basis.

Item	Basis of Apportionment (Between Pre-and Post-Incorporation periods)
a) Gross Profit or Gross Loss: (Refer Example 1 below)	On the basis of turnover in the respective periods. **(Or)** On the basis of cost of goods sold in the respective periods in the absence of any information regarding turnover. **(Or)** On the basis of time in the respective periods in the absence of any information regarding turnover and cost of goods sold.
b) Variable expenses related to Turnover: [E.g.: Carriage/ Cartage Outward. Selling and Distribution Expenses, Commission to selling agents / traveling agents, Advertisement expenses, Bad debts (if actual bad debts for the two periods are not given), Brokerage, Travelling Expenses relating to Sales men etc.	On the basis of turnover in the respective periods.

Item	Basis of Apportionment (Between Pre-and Post-Incorporation periods)
c) **Fixed common expenses related to Time:** [**E.g.:** Salaries, Office and Administration Expenses, Rent, Rates and Taxes, Printing and Stationery, Telephone, Telegram and Postage, Depreciation, Insurance, Miscellaneous Expenses, Travelling Expenses relating to Office Staff, Advertisement expenses where contracted for monthly payments	On the basis of time in the respective periods.
d) **Expenses exclusively relating to pre-incorporation period:** [E.g. Vendors salary, Interest on Vendor's capital]	Charge to Pre-incorporation period.
e) **Expenses exclusively relating to post incorporation period:** [E.g. interest on Debentures, Director fees, Directors remuneration, Preliminary Expenses, Share issue Expenses, Underwriting Commission, Discount on issue of Share / Debentures, formation Expenses, Donation to political party by company]	Charge to Post-incorporation period.
f) **Interest on purchase consideration to Vendor:** **i)** For the period from the date of acquisition of business to date of incorporation. **ii)** For the period from the date of incorporation to the date of payment.	Charge to Pre-incorporation period Charge to Post-incorporation period
g) **Audit Fees:** **i)** For companies audit under Companies Act. **ii)** For Tax Audit under section 44 AB of the income Tax Act 1961	Charge to Post incorporation period on the basis of Turnover in the respective periods.

Example:

1. Lion Ltd. was incorporated on 01.08.20X1 to take over the running business of M/s Happy with assets from 01.04.20X1. The accounts of the company were closed on 31.03.20X2.

   The average monthly sales during the first four months of the year (20X1-X2) were twice the average monthly sales during each of the remaining eight months.

   Calculate time ratio and sales ratio for pre and post incorporation periods.

   Solution:

   Time ratio:

   Pre-incorporation period (01.04.20X1 to 01.08.20X1) = 4 months

   Post incorporation period (01.08.20X1 to 31.03.20X2) = 8 months

   Time ratio = 4: 8 or 1: 2

   Sales ratio: Average monthly sale before incorporation was twice the average sale per month of the post incorporation period. If weightage for each post-incorporation month is x, then

   Weighted sales ratio = 4 × 2x: 8 × 1x = 8x: 8x or 1: 1

PROBLEMS FOR CLASSROOM DISCUSSION

PROBLEM 1: **Computation of profit/loss for the period after adjustments:** ABC Ltd. was incorporated on 01.05.2014 to take over the business of DEF and Co. from 01.01.2014. The summarized Profit and Loss Account as given by ABC Ltd. for the year ending 31.12.2014 is as under:

	Particulars	Figures for the current reporting period
I.	Gross Profit	10,64,000
II.	Other Income (Interest on Investments)	36,000
III.	**Total Revenue (I + II)**	**11,00,000**
IV.	**Expenses:**	
	Finance costs (Interest on Debentures)	25,000
	Employee Benefit Expenses:	
	Salaries including manager's salary of Rs. 85,000	3,31,000
	Other expenses:	
	i) Rent & Taxes	90,000
	ii) Carriage Outwards	14,000
	iii) Printing & Stationary	18,000
	iv) Sales Commission	30,800
	v) Bad Debts (related to sales)	91,000
	vi) Underwriting Commission	26,000
	vii) Preliminary Expenses	28,000
	viii) Audit Fees	45,000
	ix) Loss on Sale Of Investments	11,200
	Total Expenses:	7,10,000
V.	Profit (Loss) for the period (III - IV)	3,90,000

Prepare a statement showing allocation of expenses and calculations of pre-incorporation and post-incorporation profits after considering the following information:

1. G.P. ratio was constant throughout the year.
2. Sales for January and October were 1½ times the average monthly sales while sales for December were twice the average monthly sales.
3. Bad debts are shown after adjusting a recovery of Rs.7,000 of Bad Debt for a sale made in July, 2011.
4. Manager's salary was increased by Rs.2,000 p.m. from 1.5.2014
5. All investments were sold in April, 2014.
6. The entire audit fees relates to company. ***(A) (NEW SM, SIMILAR: M15)***

(ANS.: NET PROFIT FOR THE PRE PERIOD = RS. 1,86,900, POST PERIOD = RS. 2,03,100)

Note:____

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PROBLEM 2: Sun Limited took over the business of a partnership firm M/s A & N Brothers with effect from 1st April, 2017. The company was incorporated on 1st September. 2017. The following profit and loss account has been prepared for the year ended 31st March. 2018.

Particulars	Rs.	Particulars	Rs.
To salaries	1,33,000	By Gross Profit b/d	7,50,000
To rent	96,000		
To carriage outward	75,000		
To audit fees	12,000		
To travelling expenses	66,000		
To commission on sales	48,000		
To pruning and stationery	24,000		
To electricity charges	30,000		

To depreciation	80,000		
To advertising expenses	24,000		
To preliminary expenses	9,000		
To Managing Director's remuneration	8,000		
To Net Profit c/d	1,45,000		
	7,50,000		**7,50,000**

Additional Information:

1. Trend of sales during April, 2017 to March, 2018 was as under:

April, May	Rs.85,000 per month
June, July	Rs.1,05,000 per month
August, September	Rs.1,20,000 per month
October, November	Rs.1,40,000 per month
December onwards	Rs.1,50,000 per month

2. Sun Limited took over a machine worth Rs.7,20,000 from A & N Brothers and purchased a new machine 1st February, 2018 for Rs.4,80,000. The company decides provide depreciation @ 10% p.a.

3. The company occupied additional space from 1st October, 2017 @ rent of Rs.6,000 per month.

4. Out of travelling expenses, Rs.30,000 were incurred by office staff while remaining expenses were incurred by salesmen.

5. Audit fees pertain to the company.

6. Salaries were doubled from the date of incorporation.

You are required to prepare a statement apportioning the expenses between pre and post incorporation periods and calculate the profit/ (loss) for such periods. ***(A) (N18 (N) - 12M)***

(SOLVE PROBLEM NO.1, 2 & 3 OF ASSIGNMENT PROBLEMS AS REWORK)

Note:____

PROBLEM 3: (PRINTED SOLUTION AVAILABLE) Computation of Pre and post profits when there is change in GP%: SALE Limited was incorporated on 01.08.20X1 to take-over the business of a partnership firm w.e.f. 01.04.20X1. The following is the extract of Profit and Loss Account for the year ended 31.03.20X2:

Particulars	Amount (Rs)	Particulars	Amount (Rs)
To Salaries	1,20,000	By Gross Profit	6,00,000
To Rent, Rates & Taxes	80,000		
To Commission on Sales	21,000		
To Depreciation	25,000		
To Interest on Debentures	32,000		
To Director Fees	12,000		
To Advertisement	36,000		
To Net Profit for the Year	2,74,000		
	6,00,000		**6,00,000**

i) SALE Limited initiated an advertising campaign which resulted increase in monthly average sales by 25% post incorporation.

ii) The Gross profit ratio post incorporation increased to 30% from 25%.

You are required to apportion the profit for the year between pre-incorporation and post-incorporation, also explain how pre-incorporation profit is treated in the accounts. *(A) (NEW SM, N17-8M)*

(ANS.: NET PROFIT FOR THE (POST) PERIOD RS. 2,05,000, NET PROFIT FOR THE (PRE) PERIOD RS. 69,000)

(SOLVE PROBLEM NO.4 OF ASSIGNMENT PROBLEMS AS REWORK)

Note:____

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PROBLEM 4: (PRINTED SOLUTION AVAILABLE) The partners of Maithry Agencies decided to convert the partnership into a private limited Company called MA (P) Ltd. with effect from 1st Jan., 2014. The consideration was agreed at Rs.1,17,00,000 based on the firm's Balance Sheet as at 31st Dec., 2013. However, due to some procedural difficulties, the Company could be incorporated only on 1st April, 2014. Meanwhile the business was continued on behalf of the Company and the consideration was settled on that day with interest at 12% p.a. The same books of A/c's were continued by the Company which closed its A/c's for the first time on 31st March, 2015 & prepared the following summarized Profit & Loss A/c.

Particulars	Rs.	Rs.
Sales		2,34,00,000
Cost of goods sold	1,63,80,000	
Salaries	11,70,000	
Depreciation	1,80,000	
Advertisement	7,02,000	
Discounts	11,70,000	
Managing Director's remuneration	90,000	
Miscellaneous office expenses	1,20,000	
Office-cum-show room rent	7,20,000	
Interest	9,51,000	(2,14,83,000)
Profit		**19,17,000**

The Company's only borrowing was a loan of Rs.50,00,000 at 12% p.a. to pay the purchase consideration due to the firm and for working capital requirements. The Company was able to double the average monthly sales of the firm, from 1st April, 2014 but the salaries trebled from that date. It had to occupy additional space from 1st July, 2014 for which rent was Rs. 30,000 per month.

Prepare statement of apportioning cost/revenue between pre-incorporation & post-incorporation periods and calculation of profits/losses for such periods. Also, suggest how the pre-incorporation profits are to be dealt with. *(A) (NEW SM, SIMILAR: M18 (O)-8M)*

(ANS.: NET PROFIT (POST) RS.19,36,000, PRE- INC. PERIOD (LOSS) RS. 19,000)

(SOLVE PROBLEM NO. 5 OF ASSIGNMENT PROBLEMS AS REWORK)

Note:____

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PROBLEM 5: Treatment of Bad debts and PBD: Ashok Company Limited was incorporated on 1st April to take over as from 1st January in the same year the existing business of Bijoy Brothers. Under the takeover agreement all profits made from 1st January are to belong to the Company. The purchase consideration was Rs.7,00,000. The vendors received half of it in cash on 1st July in the same year together with interest at 5% p.a. For other half of the purchase consideration, they were allotted 3,500 fully paid up shares of Rs.100 each in the Company. The following balances appeared in the Company's Ledger as at 31st December:

Particulars	Rs.	Particulars	Rs.
Share Capital: 4,500 shares of Rs.100 each fully paid (including vendor's shares)	4,50,000	Preliminary Expenses (These are to be fully written off) Salaries & Wages	8,000 48,000

Bank Overdraft	1,65,000	Rent Received	13,000
Sundry Creditors	65,000	Rates and Taxes	7,000
Fixed Deposits Received	35,000	Repairs to Building	3,000
Freehold Land at Cost	50,000	Miscellaneous Expenses	22,000
Building at Cost	1,30,000	Director's Fees	2,400
Furniture & Fixtures at Cost	15,000	Interest to Vendors	17,500
Transport Vehicles at Cost	35,000	Purchases	7,70,000
Stock-in-trade on 1st January	4,20,000	Sales	9,10,000
Book Debts	95,000	Goodwill	3,100
Cash on Hand	12,000		

The stock-in trade as at 31st December amounted to Rs. 4,80,000. Bad debts amounting to Rs. 1,000 out of which Rs. 500 related to book debts taken over by the Company, have to be written off and a provision of Rs. 5,000 to be made for doubtful debts as at 31st December. Depreciation has to be written off: Building at 5%. Furniture & Fixtures at 10% and Transport Vehicles at 20%.

You are required to prepare:

a) A Profit & Loss A/c for the period from 1st January to 31st December and to compute the profit prior to incorporation. For the purpose of determining the profit prior to incorporation you should assume the turnover to be spread evenly over the year.

b) Balance Sheet as on 31st December. *(A) (N11-6M)*

(ANS.: NET PROFIT (POST) RS. 63,850, CAPITAL RESERVE (PRE) RS. 20,250, TOTAL OF BALANCE SHEET RS. 8,01,000)

(SOLVE PROBLEM NO. 6 & 7 OF ASSIGNMENT PROBLEMS AS REWORK)

Note:____

PRINTED SOLUTIONS TO SOME SELECTIVE PROBLEMS

PROBLEM NUMBERS TO WHICH SOLUTIONS ARE PROVIDED: 3, 4

PROBLEM NO. 3

Statement showing the calculation of Profits for the pre-incorporation and post incorporation periods

Particulars	Total Amount (Rs.)	Basis of Allocation	Pre-incorporation (Rs.)	Post-incorporation (Rs.)
Gross Profit (W.N.2)	6,00,000	1:3	1,50,000	4,50,000
Less: Salaries	1,20,000	Time	40,000	80,000
Rent, rates and taxes	80,000	Time	26,667	53,333
Sales' commission	21,000	Sales (2:5)	6,000	15,000
Depreciation	25,000	Time	8,333	16,667
Interest on debentures	32,000	Post		32,000
Directors' fee	12,000	Post		12,000
Advertisement	36,000	Post		36,000
Net profit	2,74,000		69,000	2,05,000

Working Notes:

1. Sales ratio

Let the monthly sales for first 4 months (i.e. from 1.4.20X1 to 31.7.20X1) be = x

Then, sales for 4 months = 4x

Monthly sales for next 8 months (i.e. from 1.8.X1 to 31.3.20X2) = x + 25% of x= 1.25x

Then, sales for next 6 months = 1.25x X 8 = 10x

Total sales for the year = 4x + 10x = 14x

Sales Ratio = 4x: 10x i.e. 2:5

2. Gross profit ratio

From 1.4.20X1 to 31.7.20X1 gross profit is 25% of sales

Then, 25% of 4x= 1x

Gross profit for next 8 months (i.e. from 1.8.X1 to 31.3.20X2) is 30%

Then, 30% of 10x = 3x

Therefore gross profit ratio will be 1:3

3. Time ratio

1st April, 20X1 to 31st July, 20 X 1: 1st August, 20 X 1 to 31st March, 20 X 2

= 4 months: 8 months = 1:2

Thus, time ratio is 1:2.

PROBLEM NO. 4

Maithry Agencies (P) Ltd.

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

Particulars	Basis of allocation	Pre-inc. (Rs.)	Post-inc. (Rs.)
Sales	Sales ratio	26,00,000	2,08,00,000
Less: Cost of goods sold	Sales ratio	18,20,000	1,45,60,000
Salaries	W.N.4	90,000	10,80,000
Depreciation	Time ratio	36,000	1,44,000
Advertisement	Sales ratio	78,000	6,24,000
Discounts	Sales ratio	1,30,000	10,40,000
M.D.'s remuneration	Post-inc.	—	90,000
Misc. Office Expenses	Time ratio	24,000	96,000
Rent	W.N.5	90,000	6,30,000
Interest	Time ratio	3,51,000	6,00,000
Net Profit/(Loss)		(19,000)	19,36,000

Working Notes:

1. Calculation of Sales ratio:

   Let the average sales per month in pre-incorporation period be x. Then the average sales in post-incorporation period are 2x. Thus total sales are (3 × x) + (12 × 2x) or 27x. Ratio of sales will be 3x: 24x or 1:8.

   Time ratio is 3 months: 12 months or 1:4

2. Expenses apportioned on turnover ratio basis are cost of goods sold, advertisement, discounts.
3. Expenses apportioned on time ratio basis are Depreciation, and misc. office expenses.
4. Ratio for apportionment of Salaries:

   If pre-incorporation monthly average is x, for 3 months 3x.

   Average for balance 12 months 3x, for 12 months 36x.

   Hence ratio for division, 1:12.

5. **Apportionment of Rent:**

Particulars	Amount (Rs.)
Total Rent	7,20,000
Additional rent for 9 months (From 1st July 20X2 to 31st March, 20X3)	(2,70,000)
Rent for old premises for 15 months at Rs. 30,000 p.m.	4,50,000

	Pre-inc.	Post-inc.
Old Premises	90,000	3,60,000
Additional rent	-	2,70,000
	90,000	6,30,000

ASSIGNMENT PROBLEMS

PROBLEM 1: Computation of sales ratio & G.P.: Rama Udyog Limited was incorporated on August 1, 2013. It had acquired a running business of Rama & Co. with effect from April 1, 2013. During the year 2013-14, the total sales were Rs. 36,00,000. The sales per month in the first half year were half of what they were in the later half year. The net profit of the company, Rs. 2,00,000 was worked out after charging the following expenses:

(i) Depreciation Rs. 1,23,000, (ii) Directors' fees Rs. 50,000, (iii) Preliminary expenses Rs.12,000, (iv) Office expenses Rs. 78,000, (v) Selling expenses Rs. 72,000 and (vi) Interest to vendors up to August 31, 2013 Rs. 5,000. Please ascertain pre-incorporation and post-incorporation profit for the year ended 31st March, 2014.

(A) (OLD PM) (ANS.: NET PROFIT FOR THE PRE PERIOD = RS. 33,000, POST PERIOD = RS. 1,67,000)

PROBLEM 2: Computation of all ratios: ABC Ltd. took over a running business with effect from 1st April, 2013. The company was incorporated on 1st August, 2013. The following Profit and Loss Account has been prepared for the year ended 31.03.2014.

	Particulars	Figures for the current Reporting period
i)	Gross Profit	3,20,000
ii)	Total Revenue (I + II)	3,20,000
iii)	**Expenses:**	
	Finance costs(interest on debentures)	3,000
	Employee Benefit Expenses:	
	i. Salaries	48,000
	ii. Directors Fees	11,200
	Depreciation and amortization expenses	9,600
	Other expenses:	
	a) Stationary	4800
	b) Travelling Expenses	16,800
	c) Advertisement	16,000
	d) Miscellaneous trade expenses	37,800
	e) Rent (Office Building)	26,400
	f) Electricity Charges	4,200
	g) Bad debts	3,200
	h) Commission to selling agents	16,000
	i) Tax Audit Fee	6,000
	j) Interest paid to Vendor	4,200
	k) Selling Expenses	25,200
	Total Expenses:	2,32,400
iv)	Profit (Loss) for the period (II - III)	87,600

Additional Information:

a) Total sales for the year, which amounted to Rs.19,20,000 arose evenly up to the date of 30.09.2013. Thereafter they spurted to record an increase of two-third during the rest of the year.

b) Rent of office building was paid @ Rs. 2,000 per month up to September, 2013 and thereafter it was increased by Rs.400 per month.

c) Traveling expenses include Rs. 4,800 towards sales promotion.

d) Depreciation includes Rs.600 for assets acquired in the post incorporation period.

e) Purchase consideration was discharged by the company on 30th September, 2013 by issuing equity shares of Rs.10 each.

Prepare statement showing calculation of Profits and allocation of expenses between pre and post incorporation periods. *(A) (OLD PM, M10, MTP N17, MTP2 M18 (N&O))*

(ANS.: NET PROFIT FOR THE (POST) PERIOD RS. 74,800, NET PROFIT FOR THE (PRE) PERIOD RS. 12,800)

PROBLEM 3: Computation of all ratios & profit/loss for the period: The partners Kamal and Vimal decided to convert their existing partnership business into a private limited company called M/S. KV trading private ltd. With effect from 01.07.2014. The same books of accounts were continued by the company which closed its accounts for first term on 31.03.2015.

The summarized Profit and Loss account for the year ended 31.03.2015 is below:

Particulars	Rs. in lakhs	Rs. in lakhs
Turnover		240.00
Interest on Investment		6.00
		246.00
Less: Cost of Goods sold	102.00	
Advertisements	3.00	
Sales Commission	6.00	
Salary	18.00	
Managing Directors Remuneration	6.00	
Interest on Debentures	2.00	
Rent	5.50	
Bad Debts	1.00	
Under writing Commission	2.00	
Audit Fees	2.00	
Loss on Sale of Investments	1.00	
Depreciation	4.00	152.50
		93.50

The following additional information was provided:

i) The average monthly sales doubled from 01.07.2014. GP ratio was constant.

ii) All investments were sold on 31.05.2014.

iii) Average monthly salary doubled from 01.10.2014.

iv) The company occupied additional space from 01.07.2014 for which rent of Rs. 20,000 per month was incurred.

v) Bad debts recovered amounting to Rs.50,000 for a sale made in 2012, has been deducted from bad debts mentioned above.

vi) Audit fees pertain to the company.

Prepare a statement apportioning the expenses between pre and post incorporation periods and calculate the profit or loss for such periods. Also suggest how the pre-incorporation profits are to be dealt with. *(A) (NEW SM) (ANS.: NET ROFIT: PRE: RS. 18.79 LAKHS; POST: RS. 74.71 LAKHS)*

PROBLEM 4: Computation of COGS Ratio as purchase price had increased by 10% in post incorporation period: The business carried on by Khushilal under the name "Lost Horizon" was taken over as a running business with effect from 1st July, 2012 by North Horizon Ltd. which was incorporated on 1st October, 2012. The same set of books was continued since there was no change in the type of business and the following particulars of profits for the year ended 30th June, 2013 were available:

Particulars	Amount (Rs.)	Amount (Rs.)
Sales: Company period Prior period	40,000 10,000	50,000
Selling Expenses	2,000	
Preliminary Expenses written off	1,200	
Salaries	3,600	
Directors' Fees	1,200	
Interest on Capital (up to 30-09-12)	700	
Variable Expenses	1,500	
Deprecation	2,800	
Rent	4,800	
Purchases	25,000	
Carriage Inwards	1,019	(43,819)
Net profit		**6,181**

The purchase price (including carriage inwards) for the Company period had increased by 10% as compared to pre-incorporation period. No, stocks were carried either at the beginning or at the end.

You are required to draw up a statement showing the amount of pre and post-incorporation profits stating the basis of allocation of expenses.

(A) (RTP N14, RTP M18 (N&O)) (ANS.: CAPITAL LOSS (PRE) RS. (251), NET PROFIT (POST) RS 6,432)

PROBLEM 5: Computation of all ratios and Interest on Purchase consideration: The partnership of Surya Agencies decided to convert the partnership into Private Limited Company named Sohna Company Pvt. Ltd. with effect from 1st January, 2014. The consideration was agreed at Rs. 2,34,00,000 based on firm's Balance Sheet as on 31st December, 2013. However, due to some procedural difficulties, the company could be incorporated only on 1st April, 2014. Meanwhile, the business was continued on behalf of the company and the consideration was settled on that day with interest at 12% p.a. The same books of accounts were continued by the company, which closed its accounts for the first time on 31st March, 2015 and prepared the following summarized Profit and Loss account:

Particulars	Rs.	Particulars	Rs.
To Cost of goods sold	3,27,60,000	By Sales	4,68,00,000
To Salaries	23,40,000		
To Depreciation	3,60,000		
To Advertisement	14,04,000		
To Discount	23,40,000		
To Managing Director's remuneration	1,80,000		
To Miscellaneous office expenses	2,40,000		
To Office cum showroom rent	14,40,000		
To Interest	19,02,000		
To Profit	38,34,000		
	4,68,00,000		**4,68,00,000**

The company's only borrowing was a loan of RS. 1,00,00,000 at 12% p.a. to pay the purchase consideration due to the firm and for working capital requirements. The company was able to double the monthly average sales of the firm from 1st April, 2014, but the salaries trebled from the date. It had to occupy additional space from 1st July, 2014 for which rent was RS. 60,000 per month. Prepare a statement showing apportionment of costs and revenue between pre incorporation and post-incorporation periods. *(A) (RTP N15) (ANS.: NET PROFIT: PRE: RS.38,000, POST: RS.38,72,000)*

PROBLEM 6: Inder and Vishnu, working in partnership registered a joint stock company under the name of Fellow Travellers Ltd. on May 31, 20X1 to take over their existing business. It was agreed that they would take over the assets of the partnership from January 1st, 20X1 for a sum of Rs.3,00,000 and that until the amount was discharged they would pay interest on the amount at the rate of 6% per annum. The amount was paid on June 30, 20X1. To discharge the purchase consideration, the company issued 20,000 equity shares of Rs.10 each at a premium of Rs.1 each and allotted 7% Debentures of the face value of Rs.1,50,000 to the vendors at par. The summarized Profit and Loss Account of the "Fellow Travellers Ltd." for the year ended 31st December, 20X1 was as follows:

Particulars	Rs.	Particulars	Rs.
To Purchase, including Inventory	1,40,000	By Sales:	
To Freight and carriage	5,000	1st January to 31st May 20X1	60,000
To Gross Profit c/d	60,000	1st June to 31st Dec., 20X1	1,20,000
		By Inventory in hand	25,000
	2,05,000		**2,05,000**
To Salaries and Wages	10,000	By Gross profit b/d	60,000
To Debenture Interest	5,250		
To Depreciation	1,000		
To Interest on purchase Consideration (up to 30-6-20X1)	9,000		
To Selling commission	9,000		
To Directors' Fee	600		
To Preliminary expenses	900		
To Provision for taxes (entirely related with company)	6,000		
To Dividend paid on equity shares @ 5%	5,000		
To Balance c/d	13,250		
	60,000		**60,000**

Prepare statement apportioning the expenses and calculate profits/losses for the 'post and pre-incorporation' periods and also show how these figures would appear in the Balance Sheet of the company. *(A) (NEW SM) (ANS.: NET PROFIT FOR THE PRE PERIOD = RS. 4,917, POST PERIOD = RS. 13,333)*

PROBLEM 7: BRIGHT Ltd. was formed to take over a running business of Mr. BRIGHT with effect from 1st April 20X1. The company was incorporated in 1st Aug. 20X1 and the certificate of Commencement of business was received on 1st Oct. 20X1. No entries relating to the transfer of the business were entered in the books which were continued until 31st March 20X2. Trial Balance was extracted from the books as on 31st March 20X2.

Journal		
Particulars	**Dr. (Rs.)**	**Cr. (Rs.)**
Sales	-	9,60,000
Cost of Goods Sold	7,77,000	-
Rent	40,000	-
Salaries	21,000	-
Travelling Expenses	8,400	-
Depreciation	4,800	-
Carriage outward	400	-
Printing & Stationary	2,400	-
Advertisement	8,000	-
Miscellaneous Expenses	12,600	-
Directors' fees	600	-
Managing Director's Remuneration	4,100	-
Bad debts	1,600	-

Commission & Brokerage to Selling Agents	8,000	-
Audit Fees	3,000	-
Interest on Debentures	1,500	-
Interest paid to Vendors	2,100	-
Selling & Distribution Expenses	12,000	-
Preliminary Expenses	1,500	-
Underwriting Commission	900	-
Fixed Assets	3,65,000	-
Current Assets	43,800	-
BRIGHT's capital as on 01.04.20X1	-	2,78,000
Current Liabilities	-	30,700
Debentures	-	50,000

Additional Information:

a) Total Sales for the year arose evenly up to the date of certificate of Commencement where after they spurted to record an increase of two thirds during the rest of the year.

b) The Company deals in one type of product. The unit cost of goods sold was reduced by 10% since 1st Aug. 20X1 as compared to the pre-incorporation period.

c) Rent of old office building was increased to the by 20% since 1st Nov. 20X1. It had to occupy additional space from 1st July 20X1 for which rent was Rs.3,000 p.m.

d) The salaries were Tripled from 1st July 20X1

e) Travelling Expenses include Rs. 2,400 towards sales promotion.

f) Depreciation includes Rs. 300 for new assets acquired in Aug. 20X1.

g) Purchase consideration was discharged by the company on 30th Sept. 20X1 by issuing 30,000 Equity Shares of Rs. 10 each

Required: Prepare the Profit & Loss Account in a columnar form, showing the allocation of profits between pre-incorporation and post-incorporation periods indicating the basis of allocation.

(A) (ANS.: NET PROFIT FOR (POST) PERIOD RS. 49,300 NET PROFIT FOR (PRE) PERIOD RS. 800)

ADDITIONAL PROBLEMS FOR SELF PRACTICE

PROBLEM 1: Computation of Sales ratio & profit/loss: The promoters of Glorious Ltd. took over on behalf of the company a running business with effect from 1st April, 2012. The company got incorporated on 1st August, 2012. The annual accounts were made up to 31st March, 2013 which revealed that the sales for the whole year totalled Rs. 1,600 lakhs out of which sales till 31st July, 20l2 were for Rs.400 lakhs. Gross profit ratio was 25%.

The expenses from 1st April 2012, till 31st March, 2013 were as follows:

Particulars	(Rs. in lakhs)
Salaries	69
Rent, Rates and Insurance	24
Sundry Office Expenses	66
Travelers' Commission	16
Discount Allowed	12
Bad Debts	4
Directors' Fee	25
Audit Fee	9
Depreciation on Tangible Assets	12
Debenture Interest	11

Prepare a statement showing the calculation of Profits for the pre-incorporation and post incorporation periods. (**Note:** Audit fees assumed to be in relation to Tax Audit)

(A) (NEW SM, M13, M18 (N) - 10M) (ANS.: NET PROFIT PRE-RS.32.75, POST RS.119.25)

PROBLEM 2: Computation of Sales ratio & profit/loss: Sneha Ltd. was incorporated on 1st July, 2013 to acquire a running business of Atul Sons with effect from 1st April, 2013. During the year 2013-14, the total sales were Rs. 24,00,000 of which Rs. 4,80,000 were for the first six months. The Gross profit of the company Rs. 3,90,800. The expenses debited to the Profit & Loss Account included:

i) Director's fees Rs. 30,000

ii) Bad debts Rs. 7,200

iii) Advertising Rs. 24,000 (under a contract amounting to Rs. 2,000 per month)

iv) Salaries and General Expenses Rs. 1,28,000

v) Preliminary Expenses written off Rs. 10,000

vi) Donation to a political party given by the company Rs. 10,000.

Prepare a statement showing pre-incorporation and post-incorporation profit for the year ended 31st March, 2014.

(A) (NEW SM) (ANS.: NET PROFIT FOR THE PRE PERIOD = RS. 360, POST PERIOD = Rs.1,81,240)

PROBLEM 3: Roshani & Reshma working in partnership registered a joint stock company under the name of Happy Ltd. on May 31st 2017 to take over their existing business. The summarized Profit & Loss A/c as given by Happy Ltd. for the year ending 31st March, 2018 is as under:

Happy Ltd.
Profit & Loss Account for the year ending March 31, 2018

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Salary	1,44,000	By Gross Profit	4,50,000
To Interest on Debenture	36,000		
To Sales Commission	18,000		
To Bad Debts	49,000		
To Depreciation	19,250		
To Rent	38,400		
To Audit fees (Company Audit)	12,000		
To Net Profit	1,33,350		
Total	4,50,000	Total	4,50,000

You are required to prepare a Statement showing allocation of expenses and calculation of pre-incorporation and post- incorporation profits after considering the following information:

i) GP ratio was constant throughout the year.

ii) Depreciation includes Rs. 1,250 for assets acquired in post incorporation period.

iii) Bad debts recovered amounting to Rs. 14,000 for a sale made in 2014-15 has been deducted from bad debts mentioned above.

iv) Total sales were Rs. 18,00,000 of which Rs. 6,00,000 were for April to September.

v) Happy Ltd. had to occupy additional space from 1st Oct. 2017 for which rent was Rs. 2,400 per month. ***(B) (RTP N18 (N&O)) (ANS.: NET PROFIT (PRE): RS. 24,000; NET PROFIT (POST): RS. 1,09,350)***

THE END