Specialized Accounting

Unit 1

Accounting of Non-trading Institutions

Non-Trading Organizations

Non-trading organisations refer to the organisations that work for the welfare of the social groups or the society at large, earning of profits is not their main motive. Non-trading organisations unlike trading organisations normally, they do not manufacture, purchase, or sell goods and may not have credit transactions. The major sources of their income mainly include subscriptions from their members, membership fees, grants-in-aid, donations, and income from investments, etc. Since the non-trading organisations are formed for social welfare and earning of profits is not their main objective, these organizations do not prepare Profit and loss account. However, since these organisations make use of societal funds collected in the form of grant in aids, therefore they do maintain financial records to meet statutory requirements and to exercise control over utilization of their funds. Non-trading organisations do prepare Receipt and Payment account, Income and Expenditure Account and Balance Sheet at the end of the accounting year and submit these to the Registrar of Societies.

Accounting Records for Non-Trading Organizations

Non-trading organizations are required to maintain proper accounting records and also maintain effective control over utilization of funds as per statutory requirements. Because these organizations don't do any business, their main sources of income are subscriptions from members, donations, financial assistance from government and income from investments. As most of the transactions conducted by these organisations are in cash or through the bank, therefore, they usually keep a cash book in which all receipts and payments are duly recorded. A ledger containing the accounts of all incomes, expenses, assets, and liabilities is also maintained. Further, a stock register is maintained to keep complete record of all fixed assets and other inventory. Capital fund also called general fund is maintained to which all the collections from life membership fee, donation, legacies, and surplus generated etc. received from year to year is added. Non-trading organisations don't have any capital account.

Financial Statements for Non-Trading Organizations

Although non-trading organizations are non-profit making entities and don't indulge in any trading or business activities, but they are required to prepare financial statements at the end of the each accounting period. As per legal requirements they are required to provide the necessary financial information to the members, donors, contributors and also to the Registrar of Societies. The final accounts of a 'non-trading organization' include:

1. Receipt and Payment Account
2. Income and Expenditure Account, and
3. Balance Sheet.

Receipt and Payment Account

Receipt and Payment account is like a consolidated cash book made on annual basis. All the cash receipts and cash payments made in a year are recorded in receipt and payment account on consolidated basis e.g. subscriptions received from the members on different dates, shall be shown on the receipts side of the Receipt and Payment Account as one item with its total amount. In simple words it can be described as the summary of cash and bank transactions.

There is legal obligation on non-trading concerns to prepare Receipt and Payment account as it is required to be submitted to the Registrar of Societies along with the Income and Expenditure Account, and the Balance Sheet.

Format of Receipt and Payment Account

Receipt & Payment Account

(for the year ending _________)

Receipts	Amount	Payments	Amount
To balance b/d:		By balance b/d:	
Cash In Hand XXX		Bank-overdraft XXX	XXX
Cash At Bank XXX	XXX	By Wages and Salaries	XXX
To Subscription	XXX	By Rent	XXX
To General Donations	XXX	By Rates and Taxes	XXX
To Sale of Old Newspaper	XXX	By Insurance	XXX
To Sale of Old Furniture	XXX	By Printing & Stationery	XXX
To Entrance Fee	XXX	By Postage & Courier	XXX
To Life Membership Fees	XXX	By Advertisement	XXX
To Sale of Old Sports Material	XXX	By Sundry Expenses	XXX
To Investments	XXX	By Telephone Charges	XXX
To Interest on Fixed Deposits	XXX	By Entertainment Expenses	XXX
To Interest/Dividend in General	XXX	By Audit Fees	XXX
To Locker Rent	XXX	By Honorarium	XXX
To Sale of Scraps	XXX	By Repair and Renewals	XXX
To Proceeds from Charity Show	XXX	By Upkeep of Ground	XXX
To Miscellaneous Receipts	XXX	By Conveyance	XXX
To Grant-in-aid	XXX	By Newspaper & Periodicals	XXX
To Legacies	XXX	By Purchase of Assets	XXX
To Specific Donations	XXX	By Purchase of Investment	XXX
To Sale of Investments	XXX	By Balance c/d:	XXX
To Sale of Fixed Assets	XXX	Cash In Hand XXX	
To Balance c/d (bank overdraft)*	XXX	Cash At Bank* XXX	XXX
Total	**XXXX**	**Total**	**XXXX**

Preparation of Receipt and Payment Account

1. All Receipts and Payments made in a year are to be recorded on consolidated basis irrespective of whether they pertain to the current period, previous period or succeeding period.
2. While recording receipts or payments no distinction is made between receipts and payments of capital and revenue nature. All receipts and payments are to be recorded.
3. Noncash transactions/items like depreciation are not to be recorded.
4. None of the receivable income and payable expense is to be entered in this account as they do not involve inflow or outflow of cash.
5. The opening balance in Receipt and Payment Account represents cash in hand/ cash at bank which is shown on its receipts side. No distinction is made in receipts/payments made in cash or through bank. With the exception of the opening and closing balances, the total amount of each receipt and payment is shown in this account.
6. The closing balance of this account represents cash in hand and bank balance as at the end of the year, which appear on the credit side of the Receipt and Payment Account. However, if it is bank overdraft at the end it shall be shown on its debit side as the last item.

Income and Expenditure Account

It is akin to trading and profit and loss account of trading organizations and can be described as a summary of income earned and expenditure incurred during the accounting year. Accrual basis of accounting is followed to prepare this account. Like trading and profit and loss account only revenue income and expenses are considered for preparing Income and Expenditure account. Excess of income over expenditure represents surplus and excess of expenditure over income represents deficit. Net operating result i.e. surplus (i.e. excess of income over expenditure) or deficit (i.e. excess of expenditure over income), is added or deducted respectively to the capital fund shown in the balance sheet.

The Income and Expenditure Account is prepared with the help of Receipts and payments Account and additional information relating to outstanding expenses/incomes, prepaid expenses, and non-cash items like depreciation, etc.

Preparation of Income and Expenditure Account

1. Income and Expenditure statement is prepared on the basis of Receipt and Payment Account and additional information, if any.
2. Follow accrual basis of accounting for preparing Income and Expenditure account.
3. Only revenue income and expenditure is to be considered while preparing Income and Expenditure account. Exclude the capital receipts and capital payments as these are to be shown in the Balance Sheet. Exclude the donations received for specific purpose.
4. Only that portion of receipts and payments is to be recorded in Income and Expenditure which belongs to current accounting year. Make adjustments by excluding the amounts relating to the preceding and the succeeding periods and including the amounts relating to the current year not yet received.
5. Opening and closing balances of cash and bank will not appear in the Income and Expenditure account.
6. Even non-cash items of income and expenditure e.g. depreciation on fixed assets, provision for doubtful debts etc. are also to be considered while preparing income and expenditure account.

Format of Income and Expenditure Account

Name of the Organisation
Income and Expenditure Account
Dr. (for the year ended...) Cr.

Expenditure		Amount(₹)	Income		Amount(₹)
To Salaries	XXX		By Subscriptions	XXX	
Add: Outstanding at the end	XXX		Add: Outstanding at the end	XXX	
Less: Outstanding in the beginning	(XXX)	XXX	Advance in the beginning	XXX	
To Rent		XXX	Less: Outstanding in the beginning	(XXX)	
To Insurance Premium	XXX		Advance at the end	(XXX)	XXX
Less: Prepaid	XXX	XXX	By Entrance Fees (revenue receipts)		XXX
To Audit Fees		XXX	By Donations		XXX
To Printing and Stationery		XXX	By Sale of Old Newspapers		XXX
To Honorarium		XXX	By Hall Rent		XXX
To Telephone Expenses		XXX	By Sundry Receipts		XXX
To Repairs		XXX			
To Depreciation on fixed assets		XXX			
To Sports Materials used		XXX			
To Surplus (excess of income over expenditure)*		XXX	By Deficit (excess of expenditure over income)*		XXX
Total		**XXXX**	**Total**		**XXXX**

Balance Sheet

Non-trading organizations, like trading organizations, also prepare their balance sheet. Balance sheet of non-trading organizations is almost similar to the balance sheet of trading organizations with only one difference i.e. non-trading organizations have capital fund or general fund in their balance sheet in place of capital. The basic objective of preparing the balance sheet is to ascertain the financial position of the organization.

Preparation of Balance Sheet

1. Take the Capital/General Fund as per the opening balance sheet and add surplus or deduct deficit, as the case may be, to this as determined from the Income and Expenditure Account. Further, add entrance fees, legacies, life membership fees, etc. received during the year.
2. Record all the fixed assets on the asset side of the balance sheet. These assets are to be recorded after adjustments for the additions/sale made in the year and also after recording the effect of depreciation charged during the year.
3. Compare items on the receipt side of the Receipts and Payments Account with income side of the Income and Expenditure Account and items on the payments side of the Receipt and Payment Account with expenditure side of the Income and Expenditure Account. The comparison is made to ascertain the assets like subscriptions due but not yet received, incomes received in advance, sale of fixed assets made during the year, items to be capitalized (i.e. taken directly to the Balance Sheet) e.g. legacies, interest on specific fund investment and liabilities

like outstanding expenses, prepaid expenses, etc. This comparison will also help in identifying amount of fixed assets purchased during the year.

Accounting Treatment of Special Items Related to Non-Trading Organizations

- *Subscriptions*: Subscription is the main source of income of non-trading organizations. It is collected from the members on annual basis.
- *Donations*: Donations is a kind of gift received from an individual or an organization. It can be in the form of cash or kind. Donations can be categorized into two kinds i.e. Donation for specific purpose and General Donations.

Specific Donations and General Donations

- *Admission Fees*: It is onetime payment given by the members at the time of becoming member of the organization. Depending upon whether the receipt of income is a regular feature or not, we may treat this income as revenue income or capital receipt.
- *Life Membership Fees*: Life membership fee received in lump sum is treated as capital receipt and is credited directly to the capital/general fund.
- *Legacies*: It is the transfer of property by the deceased under will. Legacy is not a regular receipt and therefore it is recorded in the Receipt and Payment Account and is added to capital fund/general fund in the balance sheet.
- *Receipt from Sale of an old asset*: Total Receipts from the sale of an old asset will be shown in the Receipt and payment account. Profit or Loss on sale will be recorded in the Income and Expenditure account.
- *Receipt from Sale of Periodicals*: Receipts from sale of periodicals is of recurring nature and therefore is treated as revenue receipt and shown as the income in the Income and Expenditure Account.
- *Receipt from Sale of Sports Materials*: Sale of used sports materials is the regular feature with any Sports Club. Therefore, it is usually shown as income in the Income and Expenditure Account.
- *Payment of Honorarium*: Honorarium is the remuneration paid to a specially trained person who has rendered his special services to the organization on some special occasion like payment made to an artist for giving performance at the club is an example of honorarium.
- *Endowment Fund*: Endowment fund is the donation received for some specific purpose. It is a receipt of capital nature and therefore is shown on the Liabilities side of the Balance Sheet as an item of a specific purpose fund.
- *Government Grant*: Since the main aim of non-trading organizations is the social welfare, therefore government in order to help these organizations keep on extending grant to them. These grants may be received regularly, or they may be received once in a while.
- *Special Funds*: Non-trading organizations some time creates special funds for meeting the expenses of some special occasions or for the achievement of some specific objective like ‘Prevention of female feticide fund’ 'prize funds', 'match fund' and 'sports fund', etc. Income earned on the investments made from these funds is treated as capital receipt and is added to the respective fund in the balance sheet.
- *Stationery*: Stationery is a consumable item and normally expenses incurred on stationary are charged to Income and Expenditure Account. But in case opening and/or closing stock of stationery is given, work out the cost of stationery consumed and show that amount in Income and Expenditure Account.

Accounting for Joint ventures

Meaning

Joint venture is an agreement between two or more persons called co-venturers to undertake a particular venture or business and to share profits or losses of that venture in an agreed ratio. A Joint venture is generally formed for the purchase and sale of goods or for speculation in underwriting of shares or debentures of joint stock companies, for construction works etc.

The persons to the joint venture are called co-venturers. The joint venture is closed by settling the co-venturers account on the completion of the venture/work for which it is formed. Settlement of co-venturer's accounts may be in cash or through bank or by a bill.

Thus, joint venture is a particular/temporary partnership between two or more persons who have agreed to jointly carry out a specific venture.

Features of joint venture:

1. It is formed by two or more persons.
2. The purpose is to execute a particular venture.
3. A specific firm's name is used for the joint venture business.
4. It is of a temporary nature.
5. The co-venturers share profit or loss in the agreed ratio. However, in the absence of agreement the profits or losses are shared equally.

Objectives / Importance / Advantages:

1. To pool sufficient capital.
2. To share the skill, ability and experience for the common benefit of venture.
3. To spread the risk among the co-venturers.

Distinction between Joint Venture and Partnership:

Joint Venture	Partnership
1. There is no common name. 2. Persons involved in joint venture are called co-venturers. 3. Liability of the co-venturers depends on the mode of contract. 4. Cash system of accounting is followed. 5. Co-venturers have no implied authority. 6. There is no need for registration.	1. The business is carried on under the style of a firm's name. 2. Persons involved in partnership are called partners. 3. Partner's liability is joint and several. 4. Accrual system of accounting is followed. 5. Doctrine of implied authority is applicable to partners. 6. Registration can be made if partners desire.

Accounting Treatment:

It is necessary to maintain proper accounts of all the transactions of joint venture so as to know the correct profit or loss. Broadly speaking the accounts of joint venture can be kept in four ways. The following are the methods available to record the joint venture transactions.

1. In the books of one co-venturer.
2. In the books of all co-venturers.
3. Memorandum joint venture account.
4. Separate set of books.

In the books of one co-venturer: First Method:

This method is followed when all the transactions relating to joint venture are recorded by one co-venturer. He will prepare a joint venture account and the personal accounts of other co-venturers. The following journal entries are passed in his books –

1. For contributions made by the co-venturers:

Cash / Bank a/c Dr
 To Other Co-venturer's a/c
(Being contributions made)

2. For goods purchased:

Joint venture a/c Dr
 To Cash / Bank a/c
(Being goods purchased)

3. For goods supplied from his own stock:

Joint venture a/c Dr
 To Purchases a/c
(Being goods supplied)

4. For goods supplied by other co-venturers:

Joint venture a/c Dr
 To Other co-venturer's a/c
(Being goods supplied by co-venturers)

5. For expenses incurred:

Joint venture a/c Dr
 To Cash / Bank a/c
(Being expenses incurred)

6. For expenses paid by other co-venturers:

Joint venture a/c Dr
 To Other co-venturer's a/c
(Being expenses by other co-venturers)

7. For sales made by co-venturer:

a) For Cash Sales:

Cash / Bank a/c Dr
    To Joint venture a/c
(Being cash sales made)

b) For Credit Sales:

Debtors a/c Dr
    To Joint venture a/c
(Being credit sales made)

8. For sales made by other co-venturers:

Other co-venturer's a/c Dr
    To Joint venture a/c
(Being sales made by other co-venturers)

9. For cash / BR received from other co-venturers for sales made by them:

Cash / BR / Bank a/c Dr
    To Other co-venturer's a/c
(Being money received)

10. For recording commission of co-venturer:

Joint venture a/c Dr
    To Commission a/c
(Being commission earned)

11. For unsold stock taken over by the co-venturer:

Purchases a/c Dr
    To Joint venture a/c
(Being stock taken over)

12. For unsold stock taken over by other co-venturers:

Other Co-venturer's a/c Dr
    To Joint venture a/c
(Being stock taken over by other co-venturers)

13. For profit or loss in joint venture:

a) If profit:

Joint venture a/c Dr
    To P & L a/c (his share)
    To Other Co-venturer's a/c
(Being profit distributed)

b) If loss:

P & L a/c Dr
Other Co-venturer's a/c Dr

To Joint venture a/c
(Being loss distributed)

14. For amount paid to Other co-venturers:

Other Co-venturer's a/c Dr
To Cash / Bank a/c
(Being amount paid to other co-venturers)

Joint venture account:

Under this method Joint venture account is a nominal account and is debited with the cost of goods purchased or supplied by co-venturers out of their stock, all expenses and is credited with the sales and unsold stock. The balance in this account represents profit or loss which will be shared by the co-venturers in agreed ratio.

In the books of all co-venturers: Second Method:

Under this method, all transactions relating to joint venture are recorded in the books of all co-venturers. Each co-venturer opens a joint venture account and personal accounts of other co-venturers.

Memorandum Joint Venture Method: Third Method:

When all parties keep accounts, the method adopted for recording the transactions relating to joint venture is called Memorandum joint venture method. The summary of the procedure adopted under this method is as follows –

1. Each venturer opens one account in his books in which he records all the transactions relating to joint venture known as "Joint venture with _________ (name of co-venturer) Account and it is a personal account and does not disclose any profit or loss. Therefore, to find out the profit or loss on joint venture he prepares an account called Memorandum Joint Venture Account outside the regular books of account.
2. Each venturer records only those transactions which are effected by him. For example, if Hari and Giri are co-venturers, and when Hari purchases goods, it will be recorded only by Hari not by Giri. Similarly, if goods are sold by Giri it will be recorded only by Giri not by Hari.
3. Memorandum joint venture account is a combination of joint venture with __________ A/cs prepared by all the venturers. Memorandum Joint Venture Account will be debited with all items appearing on the debit side of joint venture with _______ account of all the co-venturers and credited with all items appearing on the credit side of joint venture with _______account of all the co-venturers. The difference represents either profit or loss which will be divided among co-venturers as per agreed ratio.
4. Each party finds the balance of the "Joint venture _____ account" appearing in his books and settles the difference by paying / receiving cash.

Fourth Method: Separate set of books or Common books:

When the joint venture transactions are numerous, a separate set of books or common books are maintained for recording all the joint venture transactions. For this purpose, the following accounts are maintained –

1. *Joint Bank Account*: for recording all cash transactions
2. *Joint Venture Account*: for ascertaining the profits or losses on joint venture and

3. *Each Venturer's Account*: for settlement of final balance of each venturer.

Accounting for Consignment

Consignment

Consignment accounting is a type of business arrangement in which one person send goods to another person for sale on his behalf and the person who sends goods is called consignor and another person who receives the goods is called consignee, where consignee sells the goods on behalf of consignor on consideration of certain percentage on sale.

Features:

1. *Two Parties:* Consignment accounting mainly involves two party's consignor and consignee.
2. *Transfer of Procession:* Procession of goods transferred from consignor to consignee.
3. *Agreement:* There is a pre-agreement between the consignor and consignee for terms and conditions of the consignment.
4. *No Transfer of Ownership:* The ownership of goods remains in the hands of the consignor until the consignee sells it. The only procession of goods is transferred to a consignee.
5. *Re-Conciliation:* At the end of the year or periodic intervals consignor sends Pro-forma invoice while consignee sends account sale details, and both reconcile their accounts.
6. *Separate Accounting:* There is independent accounting done of consignment account in the books of consignor and consignee. Both prepare consignment account and record the journal entries of goods through consignment account only.

Terms used in consignment a/cs

- *Consignor:* It is the person that sends goods.
- *Consignee:* The person who receives the goods is called the consignee.
- *Consignment:* Consignment is a business arrangement through which the consignor sends goods to the consignee for sale.
- *Consignment Agreement:* It is legally written communication between the consignor and consignee, which defines the terms and conditions of the consignment.
- *Pro-Forma Invoice:* When the consignor sends goods to the consignee, he also forwards statements showing details of goods such as quantity, price, etc. and that statement is called the Pro-forma invoice.
- *Non- Recurring Expenses:* Expenses that are incurred by the consignor to dispatch the goods from his place to place of the consignee are called non-recurring expenses. These expenses are added to the cost of goods.
- *Recurring Expenses:* The consignee incurs these expenses after the goods reached his place. These expenses are of maintenance of goods type's expenses.
- *Commission:* Commission is the reward/ consideration for the sale of goods on behalf of the consignor. It is as per the consignment agreement.
- *Account Sale:* It is the statement forwarded by the consignee to consignor showing details of goods sold, amounts received, expenses incurred, a commission charged, advance payment and balance due and stock in hand, etc.

Advantages

- *Increase in Business Exposure:* Due to consignment sales increase, thereby increase in business exposure. It is a cost-effective method to expand the business.
- *Lower Inventory Cost:* Less inventory holding costs for the consignor.
- *Incentives to Consignee:* When consignee sells on behalf of the consignor, the former receives a commission and other incentives.
- *Business Growth:* Consignment benefits both consignor and consignee. Consignor gets lower inventory bearing cost, and consignee without investment earns the commission by selling on behalf of the consignor.

Disadvantages

- *Lower Profit Margin:* Due to consignment, the consignor has to pay commission to the consignee, thereby resulting in a lower profit margin in the hands of the consignor.
- *Negligence by Consignee:* Consignee's negligence may create the problem.
- *Risk of Goods Damaged:* There is a high risk of goods damaged at the consignee's place or during transport, especially perishable goods.
- *High Charges:* Sometimes, there are high maintenance charges of goods to be borne by consignee and high shipping or conveyance charges to be borne by consignor. This is the place of the consignee, and the consignor is far away from each other.

Commission

There are **three** types of commission payable to consignee on sale of the goods −

- *Simple Commission* − This is usually a fixed percentage on the total sale, calculated as per mutually agreed terms.
- *Over-riding Commission* − In case of an extra-ordinary sale of the goods, some specific amount is payable to consignee in the form of an incentive is called overriding commission. Over-riding commission is also calculated on the total sales.
- *Del-credere Commission* − "An agreement by which an agent or factor, in consideration of an additional premium or commission (called a del credere commission), engages, when he sells goods on credit, to insure, warrant, or guarantee to his principal the solvency of the purchaser, the engagement of the factor being to pay the debt himself if it is not punctually discharged by the buyer when it becomes due."

Valuation of unsold Consignment

Valuation of unsold stock will be done like a closing stock of a Trading concern and should be valued at the cost or the market price whichever is low. This stock will be valued at −

- Proportionate cost price and
- Proportionate direct expenses.

Here, proportionate direct expenses mean — all expenses incurred by the consignor and the expenses of consignee, which are incurred by him till the goods reach the warehouse.

Invoicing Goods higher than Cost

Under this method, goods are charged at the cost + profit and the pro-forma invoice also shows this higher price of such goods. To know the actual profit, at the end of an accounting period, consignment account will be credited with excess price so charged. Value of the stock will also be adjusted to the extent of profit element. Main reason to adopt this policy by consignor is −

- To hide actual profit from consignee.
- Valuation of a stock at the consignor's warehouse is comparatively easy in this case.
- In this case, consignor usually directs consignee to sale goods on invoice price only. It prevents different sale price to different customers.

Loss of Goods

There may be two types of losses as explained below −

Normal Loss − Normal loss may occur due to inherent characteristics of goods like evaporation, drying up of goods, etc. It is not separately shown in the consignment account, but included in the cost of goods sold and the closing stock by inflating the rate per unit. To calculate the value of unsold stock, following formula is used.

Valueofclosingstock=TotalvalueofgoodssentNetquantityreceivedbyconsignee×UnsoldquantityValueofclosingstock=TotalvalueofgoodssentNetquantityreceivedbyconsignee×Unsoldquantity

Netquantityreceived=Goodsconsignedquantity−NormallossquantityNetquantityreceived=Goodsconsignedquantity−Normallossquantity

Abnormal Loss − An abnormal loss may occur due to any accidental reason. It is credited to the consignment account to calculate actual profitability. Valuation of closing stock is done on the same basis as explained earlier i.e. proportionate cost + proportionate direct expenses.