Chapter 8: Developments in Accounting

Prof. Ram Kumar Kakani

Prof. N. Ramachandran

Tanmoy Chatterjee

Depreciation

- Revenue generation process of any business reduces value of its long-term assets
- Only *fixed assets* are depreciated
- So, depreciation is a non-cash charge that represents a reduction in the value of assets due to wear and tear, age, or obsolescence
- Hence, it is a charge against the business profit
  - Purchase of fixed asset is like a prepaid expense for the business
  - Similar to rent that would have been payable if the machine was not purchased

Accounting for Depreciation

Depreciation Accounting

Charging the amount by reducing the respective fixed asset

- Depreciation amount reduced from the fixed asset
- Shown as a reduction in Balance Sheet

A provision for depreciation account is maintained

- Amount credited to the Provision account
- Balance shown in the liabilities side
- Asset shown at cost

Entry under 1st method (Year 1)

- Milind Kaapi Co., purchased a hut for Rs. 100,000 having a useful life of 10 years with the salvage value after 10 years becoming nil. Account for depreciation under both the methods.
- Solution: Assuming uniform cost allocation over the life

Depreciation Account	(Debit)	10,000	
Hut Account	(Credit)		10,000
(Being reduction in the value of hut on account of depreciation)			
The Hut in the balance sheet shall be shown at Rs. 90,000 after Year 1, Rs. 80,000 after Year 2 …			

Entry under 2nd method (Year 1)

- Under this method, the journal entries will be same with a slight difference that instead of crediting the hut account we will credit “Provision for Depreciation Account.” As a result the entry becomes

Depreciation Account	(Debit)	10,000	
Provision for Depreciation Account	(Credit)		10,000
(Being provision made for depreciation for the year)			

- Here, the Hut account in the balance sheet will stand at Rs. 100,000 for all the 10 years …

Contra Account

- In the second method, the ‘provision for depreciation’ account shall increase by Rs. 10,000 every year (popularly known as ‘accumulated depreciation’ account)
- Contra Account
- A contra-asset account has a credit balance and offsets the debit balance of the corresponding asset (such as, accumulated depreciation and provision for bad receivables)
- A contra-liability account has a debit balance and offsets the credit balance of the corresponding liability (such as, discount on trade payables and discount on bills payable)

Sale of Asset

- At the end of Year 1, Hut account in the balance sheet will look:

Gross Fixed Assets (Hut)	Rs 100,000
Less: Provision for depreciation	10,000
Net Fixed Asset (Hut)	Rs 90,000

- Assuming further that the hut is sold for Rs. 60,000 at the end of 5 years. The accounting entries in first method would be:

Cash Account	(Debit)	60,000	
Hut Account	(Credit)		60,000
(Being sale of hut for Rs. 60,000)			

Hut Account	(Debit)	10,000	
Profit & loss Account	(Credit)		10,000
(Being gain on sale of hut transferred to Profit & loss Account)			

Sale of Asset under Second Method

Cash Account	(Debit)	60,000	
Provision for Depreciation A/c	(Debit)	50,000	

What would be credited and by what amount?

Depreciation Methods

- Straight Line Method
- Written Down Value Method
- Sum of Years' Digit Method
- Depletion Method

Depletion Method

- It is suitable in cases of depreciating assets, such as mines, quarries, and oil exploration, where the depreciation is based upon pace of extraction of deposits
- Depreciation is computed by multiplying the units of output (or deposit) with the rate of depletion of resources
- Example
- If a mine with estimated minerals of 50,000 tonnes is purchased for Rs. 1,00,000, the rate of the mineral resource will be Rs. 2 per tonne of output (Rs. 1,00,000 / 50,000 tonnes)
- So if the output in year 1 is 10,000 tonnes, the depreciation to be charged for that year would be Rs. 20,000

Practice of Block Depreciation

- All the identical assets, having similar expected life are grouped as a single block
- The depreciation is calculated on the block as a whole and not on the individual asset
- The rate of depreciation is calculated on the expected life and the salvage values of the assets of that group
- Profit (or loss) on sale of asset is not computed until the block has no asset in it
  - Sale of individual asset from the block do not result in any gain or loss on account of sale
- Followed by Tax Authorities

Illustration

- A company purchases 5 machines for Rs. 10,000 each having an average life of 5 years with a salvage value of Rs. 2,000 each
- Assuming straight line depreciation method, the amount of depreciation expense would be Rs 8000 every year
- At the end of year 2 one machine was sold for Rs. 4,000 and another purchased for Rs. 8,000 having salvage value as zero

Year 1	Machinery Account	(Debit)	50,000	
	Bank Account	(Credit)		50,000
	(Being machinery purchased)			
	Depreciation Account	(Debit)	8,000	
	Provision for Depreciation	(Credit)		8,000
	(Being depreciation on the block charged at 20%)			

Journal Entries – Year 2

Year 2	Depreciation Account	(Debit)	8,000	
	Provision for depreciation	(Credit)		8,000
	(Being depreciation on the block charged for the 2nd year at 20%)			
	Bank Account	(Debit)	4,000	
	Provision for Depreciation	(Debit)	6,000	
	Machinery Account	(Credit)		10,000
	(Being machinery sold for Rs 4,000 and difference between Cost and Sale Value transferred to provision for Depreciation Account)			
	Machinery Account	(Debit)	8,000	
	Bank Account	(Credit)		8,000
	(Being machinery purchased)			

Journal Entries – Year 3

Year 3	Depreciation Account	(Debit)	8,000	
	Provision for depreciation Account	(Credit)		8,000
	(Depreciation on block consisting of 4 machines purchase[illegible] Rs 10,000 each and 1 machine purchased at 8,000 at 20%)			

Remaining machines in block (excluding new purchase[illegible]	[illegible]4
Value of 4 machines after reducing scrap value	32[illegible]0
Machinery purchased at the end of year 2	8[illegible]0
Value of Block	40[illegible]0
Depreciation @ 20%	8,000

Change in Method of Depreciation

- A method of depreciation selected has to be applied consistently
- Whenever there is a change in depreciation policy it results in influencing not only the amount of current depreciation but it will also affect the accumulated depreciation also and hence needs rewriting of the past figures of various items also
- Factors influencing the ‘Choice of Method of Deprecation’
- Easiness in understanding and implementation
- Want of higher profits during initial years or later years
- Taxation policies
- Management remuneration packages having profit linked bonus may also influence

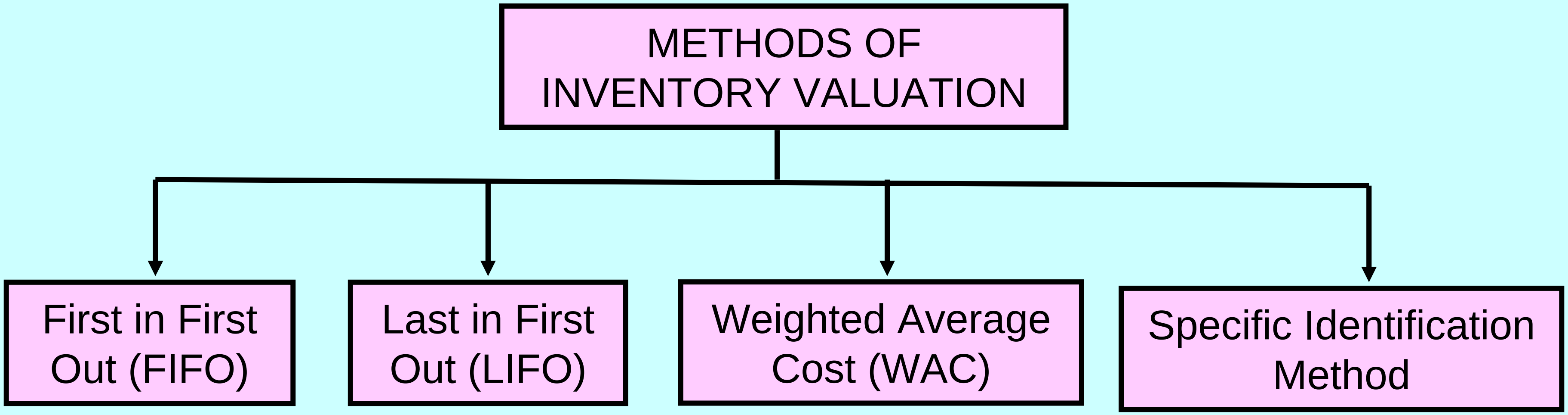
Accounting of Inventories

- Inventory is the part of goods purchased or manufactured that remained unconsumed or unsold
- Types of 'inventory'

Integrated Steel Manufacturing Firm	Steel Trading Firm
Raw Material Inventory Iron Ore, Limestone, and Coal ***Work-In-Progress Inventory*** Molten Metal and Steel Slabs ***Finished Good Inventory*** Cold Rolled Steel in Stockyards ***Stores and Spares Inventory*** Stationary, Bearings, and Grease in Stores	***Finished Inventory*** Steel and Steel Products kept in Warehouses

Methods of Inventory Valuation

- Inventory valuation and income measurement are inter-related
- For the ascertainment of income it is only the "*cost of goods sold*" that should be charged against revenue
- This is because not all the goods purchased (or produced) during the year are sold



Inventory Valuation: FIFO, LIFO, and WAC

Milk & Milk Limited Example			
		Balance Sheet on January 1	
Assets		**Equities**	
Cash	INR 26.00	Owners Equity	INR 26.00
Total Assets	26.00	Total Equity	26.00
Transactions during January			
Date		**Item**	
13-Jan	Bought	one kg sugar @ Rs 12	
22-Jan	Bought	one kg sugar @ Rs 14	
31-Jan	Sold	one kg sugar @ Rs 15	
Statement of Income for January			
	FIFO	Average Cost	LIFO
Sales	INR 15.00	INR 15.00	INR 15.00
Less: Cost of Sales	12.00	13.00	14.00
Trading Income	3.00	2.00	1.00

LIFO Vs FIFO

- The difference between LIFO and FIFO ending inventory is due to the rising prices. This leads to FIFO method showing higher ending inventory and lower cost of goods sold
- ➔ FIFO method would show higher profit than LIFO method.
- Accountants rarely use the physical movement of inventory to decide on the inventory methodology (due to difficulty in tracking)
- Instead they make assumptions about flow of costs
- LIFO is not recommended to be followed by the Accounting Standard 2 on “Valuation of Inventories.” In a few exceptions it is allowed

Observations ...

- Accounting policy adopted in relation to inventory valuation and depreciation can to a large extent influence income determination (by a firm) for a particular period
- Profits and financial performance can be manipulated by switching from one method of valuation to another
- So, Company Law requires that particular method accepted should be consistently tried at least for a period of three years

Cost of Goods Sold & Gross Profit

- Cost of Goods Sold

  = Beginning Inventory + Purchases– Ending Inventory
- Gross Profit = Sales – Cost of Goods Sold
- Every year the unsold inventory will be carried forward to the next year and charged against the revenue of next year and hence the above accounting equation can be re-written as:
- Gross Profit = Sales – (Ending Inventory of Last Period + Purchases – Ending Inventory of Present Accounting Period)
- In order to avoid situations of improper valuation accountants in such situations adopt the policy of valuing inventory at ‘lower of cost or market price’

Illustration on Presentation

- Market price indicates the 'net realizable value' by selling the inventory
- Govind started the business of vending milk in the city of Indore. He followed a weekly accounting period. He has been procuring milk at a steady rate of Rs 10 per liter from the nearby small farmers. Govind used to sell this milk to the local community at a rate of Rs 20 per liter. At the end of the first week, he had an ending inventory of 10 liters. During second week, he purchased 100 liters of milk and at the end of second week he found the stock of milk to be only 1 liter. Compute the gross profit of Govind's business and present it in as many possible ways as possible

Computation of Sales

Beginning inventory of 2^{nd} week was	Rs 100 (10 liters @ Rs 10 per liter)
Purchases in 2^{nd} week was	Rs 1000 (100 liters @ Rs 10 per liter)
Ending inventory of 2^{nd} week was	Rs 10 (being 1 liter @ Rs 10 per liter)
Cost of Goods Sold of 2^{nd} week would be	Rs 1090 (being 109 liters @ Rs 10 per liter)
Sales of 2^{nd} week would be	Rs 2180 (being 109 liters @ Rs 20 per liter)

Income Statement: Simplest Form

Sales	Rs 2180
Expenses	
Less Cost of Go	*Rs 1090*
Gross Profit	Rs 1090

Used by companies like Blue Dart Express and HLL

Other Forms of Presentation …

Sales	Rs 2180
Add Increase/(Decrease) in Stoc	*(Rs 90)*
Adjusted Sales	Rs 2090
Expenses	
Less Purchases	*Rs 1000*
Gross Profit	Rs 1090

Used by European and very few Indian firms

Sales	Rs 2180
Expenses:	
Less Purchases	*Rs 1000*
Less (Increase)/Decrease i	*Rs 90*
Gross Profit	Rs 1090

Used by Raymond & Television Eighteen

Stages in Accounting of Debentures

- Debentures are documents certifying (or acknowledging) debt
- They are large loans being split into standard small sized instruments, to enable companies raise money from multiple investors
- The debenture certificates contain the terms of repayment of principle amount and the interest thereon

Issue of Debentures → Interest Payments → Writing off discount on issue of debentures → Redemption of Debentures

Issue of Debentures

- The accounting entries for recording the issues of debentures are same as Share Capital except that a Debenture Account is opened instead of share capital account
- There is no restriction on the amount of discount that can be allowed on issue of debentures
- A private company can issue debentures but cannot issue any invitation to the public to subscribe to it
- If the issue of debentures consists of application, allotment and calls, the entries for due and receipt are passed accordingly
- The debentures can be issued for cash or for a consideration other than cash (say, for purchase of a fixed asset)

Illustration – Hari Ltd.

- Hari Limited purchased land from Virat Ltd., having a book value of Rs 1,50,000. It was agreed that the purchase consideration will be paid by issuing debentures of Rs. 100 face value each carrying a coupon rate of 12% and redeemable after five years. Pass necessary journal entries assuming the debentures were issued at Par

Land and Building Account	(Debit)	1,50,000	
Virat Ltd. Account	(Credit)		1,50,000
(Being assets purchased from Virat Ltd.)			

Virat Ltd. Account	(Debit)	1,50,000	
12% Debentures Account	(Credit)		1,50,000
(Being issue of debentures at par)			

Issue at Discount or Premium

Debentures issued at Discount

Virat Ltd. Account	(Debit)	1,50,000	
Discount on Debentures A/c	(Debit)	16,700	
12% Debentures Account	(Credit)		1,66,700
(Being issue of debentures of Rs 100 each at a discount of 10%)			

Debentures issued at Premium :

Virat Ltd. Account	(Debit)	1,50,000	
12% Debentures Account	(Credit)		1,36,400
Premium on Debentures A/c	(Credit)		13,600
(Being issue of 1364 debentures of Rs 100 each for Rs. 110)			

Issue of Debentures as Security

- Collateral security is a type of secondary security which is asked by the loan provider. The secondary security is utilized only when the principal security is not sufficient for repayment of loan
- In case where a company issues debentures as a collateral security, the provider of loan becomes the holder of debentures when the primary security fails to repay the money (since the relevant loan clause acts as the trigger)
- Hence on taking a loan, no formal entry is passed, instead under the loan item in the balance sheet a note is written that the loan is secured by issue of debentures as a collateral security
- When the loan is defaulted, the debenture entry is triggered

Interest on Debentures

- Interest on debentures is required to be paid whether the company earns a net profit or not which is in contrast to dividend on equity shares
- Illustration
- Jogi & Co. issues 50,000, 8% debentures of face value Rs 100 each on 1st January 20X6. The interest is payable half yearly on 30th June and 31st December every year. Income Tax Act at that time states that a TDS of 10% is to be deducted on behalf of the debenture holders (and is to be deposited with Income Tax Authorities)
- Pass Journal entries for the first interest payment

Jogi & Co. Solution

01-01-X6	Bank A/c	(Debit)	50,00,000	
	8% Debentures Account	(Credit)		50,00,000
	(Being amount received on account of issue of 50,000 debentures)			
30-06-X6	Interest on Debentures A/c	(Debit)	2,00,000	
	Income Tax Account	(Credit)		20,000
	Debenture Holders Account	(Credit)		1,80,000
	(Being half yearly interest due at 8% p.a. and tax at 10% there on)			
30-06-X6	Debenture Holders Account	(Debit)	1,80,000	
	Income Tax Account	(Debit)	20,000	
	Bank Account	(Credit)		2,00,000
	(Being interest and tax thereon paid at applicable dates)			

Comments ...

- These entries are required to be passed when the interest is due
- It has been assumed here that the interest is paid when it becomes due but if the due date and the date of actual payment are different, the entry for payment is passed on the date when it is actually paid
- Like interest expense on a loan, the interest on debentures is an allowable expenditure for the company. Therefore, at the end of each accounting year the amount paid on account of debenture interest is debited to the profit & loss account of that year

Discount on Issue of Debentures

- It is a loss for the company because the redemption is done at par (or even at premium)
- The discount is a facilitating asset and is required to be written off within the lifetime of the debentures
- Generally, discounts are written off equally every year
- Achintya Co. issues 14% debentures of Rs 100,000 redeemable after 5 years at a discount of 5%. The journal entry of writing off every year will be

Profit & loss Account	(Debit)	1000	
Discount on issue of Debentures A/c	(Credit)		1000
(Discount on issue of debentures written off)			

Redemption of Debentures

- Redemption is repayment of money
- It can be either at par or premium
- For redemption of debentures at par, the entry, which was passed at the time of issue, shall be reversed
- For redemption at premium there is a capital loss to the company which is known at the time of issue
- The loss on issue of debentures is required to be written off during the lifetime of the debentures (very similar to issue of debentures at a discount)
- Example: If a debenture of Rs 100 is to be redeemed at Rs 110 by FP Co., the following entry is passed on issue of debentures

Journal Entry

Bank Account	(Debit)	100	
Loss on issue of Debentures Account	(Debit)	10	
Debentures Account	(Credit)		100
Premium on redemption of Debentures Account	(Credit)		10

FP Co.

Balance Sheet as at the year end ...

ASSETS	Rs.	LIABILITIES	Rs.
Bank Account	100	Debentures Account	100
Miscellaneous expenditure to the extent not written off (loss on issue of debentures)	10	Premium on redemption Of debentures	10
	110		110

Accounting for Investments

- Investments may be in form of different types of securities
- For more than one type of investment, it is prudent to maintain separate account for each investment so that the interest, dividend and the profit (or loss) on the investment can be ascertained separately
- Journal Entries
- For all the purchases, expenses and losses, the investment account should be debited

➔ For all the incomes or gains, the account should be credited

- It is advisable to maintain a separate column in the investment account for income on investment due to interest and dividend

Important points …

- Purchase price – It always includes the price of securities and the cost of transfer i.e., brokerage, commission and other charges for acquiring the securities
- Sale Price – It should be reduced by the cost of transaction i.e., brokerage, commission, etc.
- Interest – Generally the price quoted for debentures and bonds do not include the interest portion. The interest till the time held by the seller is to be paid in addition to the price of the debentures (or government securities)
- "Cum-interest" price means the interest benefit goes to the buyer ➔ buyer need not pay anything over the agreed price

Example

- Leena on 1st August 20X6 purchases Rs 4000 worth, 12% coupon rate debentures at Rs 96 (net) per debenture cum-interest. The face value is Rs 100 per debenture
- If the interest is paid by the issuing company half-yearly (i.e., on 30th June and 31st December every year) then it would mean the interest component is included in Rs 4000
- This interest due at 12% per annum on Rs 4000 comes to Rs 80. In other words the value of debenture is Rs. 3760 [= (Rs 96 x 40 debentures) – Rs 80 interest accrued]
- Dividend. The treatment of ex-dividend or cum-dividend in similar to the treatment of interest

Important points…

- Bonus shares – Reward given by the company due to its consistently good current performance and also in the foreseeable future
- The bonus equity shares are issued at no cost
- These bonus shares are issued by companies by capitalizing the reserves of the companies
- Gangaram & Company has Rs 1 crore equity shares of Rs 10 par value and has reserves worth Rs 100 crores. If it decides to issue bonus shares in the ratio of 1 share for every 2 shares owned then the companies Balance Sheet would get modified as follows:

Bonus Issue & Balance Sheet

Gangaram & Company

Equity Portion of Balance Sheet before Issuing Bonus Shares:

Equity Share Capital	Rs. 10 crores
(Rs 10 par value for 1 crore shares)	
Reserves and Surplus	Rs. 100 crores
	===============
Total Shareholders Funds	Rs. 110 crores
	===============

Equity Portion of Balance Sheet after Issuing Bonus Shares:

Equity Share Capital	Rs. 15 crores
(Rs10 par value for 1.5 crore shares)	
Reserves and Surplus	Rs. 95 crores
	===============
Total Sh	Rs. 110 crores
	===============

Transfer of 5 crores from Reserves to Capital

Raising Additional Capital

Raising Additional Capital via Share Issue

Private Placement

Placement of shares of the company with exclusive investors

Usually done at a premium

Rights Issue

The existing shareholders given opportunity to invest in more shares of the same company on payment

Public Issue

'Invitation offer' to public at large

Refer to chapter on Joint Stock Companies

Rights Issue & Private Placement

- The journal entry for rights issue and private placement is similar to the journal entries passed for issue of additional securities (through public issue)
- This is because it is new issue of securities whether to same shareholders or new investors or exclusive investors
- Example: If Gangour Sweets Limited with Rs 1 crore shares of Rs 10 par value has reserves worth Rs 10 crores decides to make a rights issue in the ratio of 1 share for every 10 shares owned at a price of Rs 100 then the companies liability side of the Balance Sheet would get modified:

Rights Issue & Balance Sheet

Gangour Sweets Limited

Equity Portion of Balance Sheet before Issuing Rights Shares:

Equity Share Capital	Rs. 10 crores
(Rs 10 par value 1 crore shares)	
Reserves and Surplus	Rs. 10 crores
	===============
Total Shareholders Funds	Rs. 20 crores
	===============

Gangour Sweets Limited

Equity Portion of Balance Sheet after Issuing Rights Shares:

Equity Share Capital	Rs. 11 crores
(Rs 10 par value 1.1 crore shares)	
Reserves and Surplus	Rs. 20 crores
	===============
Total Shareholders Funds	Rs. 31 crores
	===============

Valuation of Investments

- In a scenario of a company investing in shares of another company - an entry is passed for purchase of securities i.e. debiting the investment account with amount paid to get the shares on account of right issues
- Long-term investments (like other long-term assets) are valued on cost basis (unless there is a decrease in the market value of a permanent nature)
- But, companies are required to also provide exhaustive information of each and every security held (including market prices if listed)
- Profit (or loss) on account of sale of investment should be transferred to profit & loss account for the period

Valuation of Investments …

- Same treatment is done for decrease in the market value of the investments
- Illustration
- Sawadhee & Co. held 10% coupon rate debentures of face value Rs 1000 of Rx Ice creams Ltd. on 1st April 20X6. The total face value of these debentures was Rs 100,000 (but was purchased for Rs 80,000). The market value of these debentures on 31st March 20X6 was Rs 110,000. Interest was paid on 31st March every year
- On 1st August 20X6 the firm purchased another set of debentures worth Rs 10,000 for Rs 8,000 ex-interest. On 31st December 20X6, debentures of nominal value of Rs 2,000 were sold cum-interest for Rs 1,900
- Prepare Investment account in the books of Sawadhee & Co. showing profit or loss on sale of investment

Solution

Date	Particulars	Nominal Value	Interest	Principal	Date	Particulars	Nominal Value	Interest	Principal
1.1.X6	To balance b/d	100000	---	80000	31.12.X7	By Bank	2000	150	1750
					31.3.X7	By Bank		10800	
1.8.X6	To Bank	10000	667	8000		ByBal c/d	10800		86400
31.12.X6	To Profit & Loss A/c (on sales of debentures)			150					
31.3.X7	To Profit & Loss A/c		10283						
		110000	10950	88150			110000	10950	88150

†Profit on sale of debentures is calculated on FIFO basis in the following way

Proportionate purchase price for debentures of 2,000 is	1600	$\frac{80,000 \times 2000}{100,000}$
Sale price of debentures excluding interest	1750	
Net Profit on sale	150	

Negotiable Instrument

- A document used in commercial transactions and monetary dealings
- Example: Promissory note, Bill of exchange, and a Cheque
- Can be “Bearer” instrument or “Order” instrument (i.e., The payment is to be made according to the order)
- The provision of the Negotiable Instruments Act 1881 is applicable to all negotiable instruments
- A Promissory Note is “an instrument in writing containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to or to the order of a certain person or to the bearer of the instrument.”

Specimen of Promissory Note

Rs. 10,000

JAMSHEDPUR
Jul. 31, 2006

Payee (Creditor)

.... months [or ...... days] after date, I promise to pay Ms Latha or order the sum of Rupees Ten thousand only for value received.

Maker (Debtor)

Rohan

Bills of Exchange

- A Bill of Exchange is “An instrument in writing containing an unconditional order, signed by the maker, directing certain person, to pay a certain sum of money only to, or to the order of a certain person or to the bearer of the instrument”

Same party can be both Drawer and Payee

Maker or Drawer

Also the creditor

Drawee

Liable to pay the money or debtor

Payee

Entitled to get the money

McGraw-Hill Education

Discussion on Negotiable Instruments

- In case of a Bill of Exchange the maker being the creditor, orders the drawee to pay a certain sum of money
- In case of a Promissory note, the maker being the debtor promises to pay to certain sum of money
- A Bill of exchange can also be made payable to the bearer
- A cheque is “a, *bill of exchange* drawn on a specified bank and payable on demand”
- A cheque is similar to a bill of exchange with a difference that it is always drawn on a specific banker and it is always payable on demand

Accounting Entries

- The negotiable instruments are transferable upon endorsement or mere delivery (in case of bearer instrument)
- When the receiver of Bill of Exchange keeps it till the date of maturity, he passes the entry through Bills receivable account while the drawee will pass the entry through Bills Payable account
- Ashutosh sells goods worth Rs. 10,000 to Santosh on 1st January 20X6 and receives a 90-day Bill of Exchange duly accepted by Santosh. The Bill of exchange gets matured on 31st March 20X6 and Ashutosh receives money. The following entries are passed in the book of Ashutosh:

Solution...

01-01- X6	Santosh A/c	(Debit)	10,000	
	Sales Account	(Credit)		10,000
	(Being goods sold to Santosh)			
	Bills Receivable Account	(Debit)	10,000	
	Santosh Account	(Credit)		10,000
	(Being Bill of Exchange duly accepted by Santosh received)			

31-3- X6	Cash Account	(Debit)	10,000	
	Bills Receivable Account	(Credit)		10,000
	(Being payment received on maturity of the Bill of Exchange)			

Endorsing a Bill

- Till the actual payment on Bill is made, it will be shown in the Balance Sheet of Ashutosh under the current assets as Bills Receivable while Santosh will show this amount under current liabilities as Bills Payable
- When the Bill of exchange is endorsed in favour of another creditor, the drawee is not concerned with the endorsement
- For drawer, the entries relating to sale of goods and receipt of Bill of Exchange will be same but the entry on exchange/ transfer will be changed
- For example, in the previous case, if Ashutosh endorses the Bill in favour of his creditor Wasi Ahmed, the entry will be:

Bill Discounting

Wasi Ahmed Account	(Debit)	10,000	
Bills Receivable Account	(Credit)		10,000
(Being the Bill of exchange endorsed in favour of Wasi Ahmed)			

- Discounting with a bank means relinquishing the right on Bill of Exchange in favour of bank and receiving the payment
- The bank makes the payment after deducting some charges known as discounting charges
- The drawee is not concerned with the act of discounting as it makes no difference for him whether the drawer keeps the Bill with him or gets discounted from his bankers
- However, it is a Contingent Liability for the drawer

Thank You

☺