

(Answer: Net Profit Rs. 933; Missing Figure; Closing Debtors Rs. 1,110)

- 3) Royal Store of **Kanpur** opened a selling branch at Madras on July 1, 1988. Goods are sent to branch from the head office at cost plus 25%. The branch is advised to deposit cash every day in the bank in head office account. From the following particulars, prepare Branch Account in the books of head office for the period ending **December 31, 1988**. Petty Cash at branch is maintained on **imprest** system.

	Rs.		Rs.
Cash sent to branch for meeting petty expenses	1,500	Cash sales by the branch	80,000
Furniture purchased for the branch	12,000	Credit sales during 6 months	30,000
Goods sent to branch at invoice price	1,60,000	Cash received from the debtors	22,000
Expenses paid by the Head Office :		Discount allowed to debtors	400
Rent	2,200	Goods returned by debtors (at invoice price)	800
Advertisement	800	Bad debts written off	100
Salaries	4,600	Petty expenses paid by the branch	1,000
Insurance (up to June 30, 1989)	400	Stock at invoice price on December 31 (excluding stock received from debtors)	40,000

Provide depreciation on furniture at 10% p.a.

(Answer: Profit Rs. 3,940; Debtors at the end Rs. 6,700)

- 4) X Ltd. of Bombay has a branch in Delhi. The head office sends goods to the branch at cost plus 50%. From the following data, prepare the necessary accounts in the books of head office under Stock and Debtors System.

	Rs.		Rs.
Goods sent from Head Office (at invoice price)	50,000	Credit Sales	8,000
Returns to Head Office	1,000	Opening Stock	10,000
Cash Sales	35,500	Closing Stock	11,000

(Answer: Profit Rs. 11,500; Shortage of Goods Rs. 4,500)

- 5) **Shyam Brothers** of Delhi has a branch at Hyderabad. In order to maintain strict control over stocks, it invoices goods to the branch at selling price including profit of 25% on selling price. From the following particulars, prepare Branch Stock Account, Branch Debtors Account, Goods Sent to Branch Account, Branch Adjustment Account, and Branch Profit and Loss Account.

	Rs.
Stock January 1, 1989	30,000
Debtors on January 1, 1989	22,800
Goods invoiced to Branch at invoice price	1,34,000
Sales at the branch	
Cash	62,000
Credit	74,800
Cash received from Debtors	80,000
Bad Debts written off	500
Discount allowed to customers	600
Expenses at the branch	13,400
Stock on December 31, 1989	26,800

(Answer: Gross Profit Rs. 34,200; Net Profit Rs. 19,400)

Note: These questions will help you to understand the unit better. **Try** to write answers for them. But do not submit your answers to the University. These are for your practice only.

UNIT 2 BRANCH ACCOUNTS – II

Structure

- 2.0 Objectives
- 2.1 Introduction
- 2.2 Accounting System of an Independent Branch
- 2.3 Some Peculiar **Items**
 - 2.3.1 Goods in Transit
 - 2.3.2 Cash in Transit
 - 2.3.3 Head Office Expenses Chargeable to Branch
 - 2.3.4 Depreciation on Branch Fixed Assets, Accounts Maintained by Head Office
 - 2.3.5 Inter-branch Transactions
- 2.4 Incorporation of Branch Trial Balance in the Head Office Books
 - 2.4.1 Detailed Incorporation
 - 2.4.2 Abridged Incorporation
- 2.5 Closing Entries in Branch Books
- 2.6 A Comprehensive Illustration
- 2.7 Let Us Sum Up
- 2.8 Key Words
- 2.9 Answers to Check Your Progress
- 2.10 Terminal Questions/Exercises

2.0 OBJECTIVES

After studying this unit you should be able to:

- describe the features of the accounting system of an independent branch.
- make adjustment entries in the books of both head office and branch for certain peculiar items relating to independent branches
- pass necessary journal entries for the incorporation of branch balances in the books of the head office
- make closing entries in the books of the branch
- prepare consolidated balance sheet of the business.

2.1 INTRODUCTION

In Unit 1 you learnt about the systems of accounting for a dependent **branch**. Dependent branch is usually a small branch which merely functions as a sales depot. It does not keep full system of accounting. The main accounting records for such branches are maintained at the head office level. But, when a branch functions as an independent unit and enjoys certain amount of operational autonomy, it keeps full system of accounts. Such branches are termed as independent branches and maintain complete set of **books on** double entry system. They **prepare** their own Trial Balance, Profit & Loss Account and Balance Sheet. At the end of the accounting year, their **summarised** results and the assets and liabilities are **incorporated** in the books of the head office. In this unit you will learn how does the head office incorporate all branch balances in its books and what sort of records are maintained for mutual transactions between the branch and the head office.

2.2 ACCOUNTING SYSTEM OF AN INDEPENDENT BRANCH

You know an independent branch enjoys certain amount of operational autonomy. Besides receiving goods from the head office, it may also purchase goods from **the** outside parties. It maintains its own bank account and remits money from time to time to head office as per the instructions of the head office. **It is** treated as a separate accounting entity. The main features of the accounting system of such branches are as follows:

- 1) **The branch** maintains complete set of books on double entry **system**.
- 2) **The branch** opens a **Head Office Account** in its books. It is a personal account wherein all transactions between the branch and the head office are recorded at the branch level. This account is debited with cash sent to the head office and the goods returned or supplied to the head office, and is credited by goods received from the head office and the head office expenses charged to the branch for **centralised** services.
- 3) The Head Office also maintains a Branch Account in its books for all transactions, it makes with a particular branch. It is also a personal account which shows the same entries as the **Head Office Account** in branch books, but on the reverse sides.
- 4) At the end of the accounting period, the branch prepares its trial balance and the **final accounts**, and send their copies to the head office.
- 5) As soon as the head office receives the trial balance from a branch, it compares the balance in Head Office Account as shown in the branch Trial Balance with the balance in the **Branch Account** as it appears in the head office books. The difference, if any, is investigated and, after ascertaining the causes thereof, the necessary adjustment entries are passed.
- 6) After reconciling the **Head Office Account** balance with the Branch Account balance, the head office passes the necessary entries for incorporating various branch balances in its books.

2.3 SOME PECULIAR ITEMS

In respect of independent branches, there are certain items which require special accounting treatment. These items are:

- i) Goods in transit
- ii) Cash in transit
- iii) Head Office expenses chargeable to branch
- iv) Depreciation on branch fixed assets, the accounts of which are maintained at the head office level
- v) Inter-branch transactions.

Let us discuss **these items** one by one.

2.3.1 Goods in Transit

The head office and the branch send goods to **each** other quite frequently. When goods are sent by the **head office** to the branch, the head office debits the Branch Account in its books **immediately**. But the branch credits the **Head Office Account** only when it receives the goods. Similarly when the branch **sends** or **returns some** goods to the **head office**, it (the branch) debits the **Head Office Account** in its books immediately but the **head office** credits the Branch Account only when it receives the same. It is quite possible that **goods** sent in the later part of the accounting year may not have been received by the closing date **of** the accounting year by the head office or the branch, as the case may be. Such goods are called '**goods in transit**' for **which** no entry will appear in the books at the receiving end at the time of the closing the accounts. Hence, the balance in the **Head Office Account** in branch books will not tally with the balance in the Branch Account in the head **office** books. **This** will require an adjustment entry which may be passed either in the head **office** book or in the branch books, but not in **both sets of books**.

If the head office decides to pass the adjustment entry, it will be as **follows**:

Goods in Transit A/c	Dr.
To Branch A/c	

If, however, the adjustment is made in branch books, the entry will **be**:

Goods in Transit A/c	Dr.
To Head Office A/c	

It should be noted that the adjustment entry for **goods** in transit **shall** be passed only in **one** set of books, either at the head **office** level or the branch level. **Usually, such entry is made in the books of the head office.**

2.3.2 Cash in Transit

Like goods, cash is also regularly remitted by the head office and the branch to each other. For this the entries are made in both sets of books in the same **manner**, as they are made for the **goods**. In this case also it is possible that some remittances are in transit at the time of closing the books for the accounting year. This would again lead to difference in Branch Account balance in the head office books and Head Office Account balance in branch books. Hence, an adjustment entry will **have to be** passed to reconcile the same. This may be done either by the head office or by the branch, but not by **both**.

In case the head office decides to pass the adjustment entry, it will be as follows:

Cash in Transit A/c	Dr.
To Branch A/c	

If, however, the adjustment is made in the branch books, the entry will be:

Cash in Transit A/c	Dr.
To Head Office A/c	

It should be noted that for cash in transit also, the entry shall be **passed** in one set of books, either at the head office level or at the branch level. This entry is also made usually at the head office level. The reason for passing such **adjustment entries** in head office books lies in the fact that all in-transit items are noticed by the head office at the time of receiving the branch Trial Balance and, at this stage, it is not considered desirable to alter the balances in the branch books.

Look at Illustration 1 and see how are the amounts of goods in transit and cash in transit ascertained and the adjustment entries passed to reconcile the difference between the Branch Account balance and the Head Office Account balance.

Illustration 1

Following are the extracts from the Trial Balances of a head office and a branch. You are required to pass the necessary journal entries for reconciling the balances of the Head Office Account and the Branch Account.

Trial Balance

Particulars	Head Office		Branch Office	
	Dr.	Cr.	Dr.	Cr.
	Rs.	Rs.	Rs.	Rs.
Current Accounts	1,00,000			90,000
Goods sent/received by Branch		1,50,000	1,45,000	

Solution

The current accounts represent the Branch Account in the head office books and the Head Office Account in the branch books. As per the above Trial Balance, there is a difference of Rs. 10,000 between the two current account balances. It is observed that there is a difference of Rs. 5,000 in the goods sent/received by branch. This can be attributed to goods in transit. The remaining difference of Rs. 5,000 may be taken to be on account of the cash in transit. The required adjustment entry may be passed in the books of head office as follows:

Cash in Transit A/c	Dr.	5,000	
Goods in Transit A/c	Dr.	5,000	
To Branch A/c			10,000

(Being cash in transit and goods in transit adjusted)

If, however, this entry is passed in the books of the branch, it will be as follows:

Cash in Transit A/c	Dr.	5,000	
Goods in Transit A/c	Dr.	5,000	
To Head Office A/c			10,000

(Being cash in transit and goods in transit adjusted)

2.3.3 Head Office Expenses Chargeable to Branch

The Head Office may like to allocate a part of its expenses to branches for the centralised services at the head office level. As a matter of fact, quite a good amount of time of the head office staff may be spent in doing the work of the branches. Hence, it may decide to charge a part of its expenditure on salaries to the branches. The same thing may be true of certain other items of expenses. If the head office so decides to charge some expenses to the branch, the journal entry passed in the books of the head office is as follows:

Branch A/c	Dr.
To Expenses (Salaries A/c)	
(Being head office expenses chargeable to branch)	

The branch will also pass a corresponding entry in its books as follows:

Head Office Expenses A/c	Dr.
To Head Office	
(Being head office expenses chargeable to branch)	

Like all other expenses, accounts, the Head Office Expenses Account will be closed by transferring its balance to the Profit & Loss Account at the end of the accounting year.

2.3.4 Depreciation on Branch Fixed Assets, Accounts Maintained by Head Office

Sometimes, the accounts for the fixed assets of independent branches are maintained at the head office level. In such a situation, all entries in respect of branch fixed assets are made in the head office books. For example, when a fixed asset is purchased for the branch, the head office debits the Branch Fixed Assets Account and credits the Cash Account. No entry for this transaction is passed by the branch unless the payment is made by the branch for this purchase. Even if the payment for the purchase of such fixed assets is made by the branch it will not debit the Fixed Assets Account. In fact such payment is treated like a remittance to the Head Office and so it is debited to the Head Office Account. But when it comes to depreciation on such fixed assets, the branch has to pass the necessary entry in its books because the assets were used by the branch and not by the head office. Normally an entry for the depreciation on fixed assets is passed by debiting the Depreciation Account and crediting the Fixed Asset Account. But in this situation, the branch cannot credit the Fixed Asset Account because the accounts for its fixed assets are maintained at the head office level. Hence, the entry passed for depreciation on such fixed assets is different from the normal entry for depreciation. It is as follows:

Depreciation A/c	Dr.
To Head Office A/c	
(Being depreciation on fixed assets)	

Since the account for the branch fixed assets is maintained in head office books, the head office must reduce the balance in Branch Fixed Assets Account by the amount of depreciation thereon. But, it cannot debit the Depreciation Account because the loss relates to the branch. Hence, it makes the following journal entry for depreciation on branch fixed assets when their accounts are maintained by the head office:

Branch A/c	Dr.
To Branch Fixed Assets A/c	
(Being depreciation on branch fixed assets)	

It should be noted that the above entries are passed only for such branch fixed assets accounts of which are maintained by the head office. Any branch fixed assets for which the branch itself maintains the accounts, the branch will pass the normal entry for depreciation. The head office need not pass any entry in its books for the amount of depreciation on such fixed assets.

2.3.5 Inter-branch Transactions

When an organisation has more than one branch, it is possible that some transactions take place between one branch and the other. This usually happens under instructions

from the head office. For example, a branch may be asked to transfer its surplus stock to some other branch which may need the same (it may be facing shortage). In such a situation, the usual practice for the sending branch is to regard it as a transaction of returning the goods to the head office. Similarly, the receiving branch shall regard it as a transaction of receiving the goods from the head office. Hence, entries are passed on the same basis in the books of the branches and the head office. These are as follows:

In the books of the head office

Receiving Branch A/c . Dr.
 To Sending Branch A/c
 (Being goods transferred from branch
 to branch)

In the books of the sending branch

Head Office A/c Dr.
 To Goods Sent to H.O. A/c
 (Being goods sent to branch
 under instructions from H.O.)

In the books of the receiving branch

Goods from H.O. A/c Dr.
 To Head Office A/c
 (Being goods received from branch
 under instruction from H.O.)

Look at Illustration 2 and see how the above-mentioned peculiar items are recorded in the books of the head office and the branches.

Illustration 2

Give the journal entries that would be passed in the books of the head office to record the following transactions:

- i) Goods amounting to Rs. 1,000 transferred from Madras branch to Bombay branch under instructions from the head office.
- ii) Depreciation on branch fixed assets accounts maintained by the head office: (Bombay Rs. 4,000 and Madras Rs. 6,000).
- iii) A remittance of Rs. 6,000 made by Bombay branch to head office on December 27, 1988 and received by head office on January 7, 1989.
- iv) Goods worth Rs. 10,000 sent by the head office to Madras branch on December 25, 1988 and received by the latter on January 15, 1989.
- v) A sum of Rs. 10,000 is to be charged to the Madras branch for administrative services rendered by the head office.

Solution

**Head Office Books
 Journal**

		Rs.	Rs.
i)	Bombay Branch A/c Dr. To Madras Branch A/c (Being goods transferred from Madras branch to Bombay branch)	1,000	1,000
ii)	Bombay Branch A/c Dr. To Branch Fixed Assets A/c (Being depreciation)	4,000	4,000
iii)	Madras Branch A/c Dr. To Branch Fixed Assets A/c (Being depreciation)	6,000	6,000
iv)	Cash in Transit A/c Dr. To Bombay Branch A/c (Being Cash in transit adjusted)	6,000	6,000

v)	Goods in Transit A/c To Madras Branch A/c (Being goods in transit adjusted)	Dr.	10,000	10,000
vi)	Madras Branch A/c To Gen. P & L A/c (Being Administrative expenses charged to Madras branch)	Dr.	10,000	10,000

Check Your Progress A

1) What do you mean by Cash in Transit?

.....

2) Why does head office charge a part of its expenses to branches?

.....

3) Put tick (✓) mark against the correct answer:

- i) An independent branch
 - a) receives the goods from the head office.
 - b) purchases the goods from outside parties.
 - c) receives the goods from both (a) and (b) sources.
- ii) The Head Office Account in the books of branch is debited with
 - a) cash sent to the head office and goods returned to the head office.
 - b) cash and goods received from head office, and head office expenses allocated to branch by head office.
 - c) none of the above.
- iii) The adjustment entry for goods in transit is passed in the books of
 - a) either the branch or the head office.
 - b) branch as well as the head office.
 - c) none of them.
- iv) For depreciation on fixed assets, whose accounts are maintained by the head office, the head office
 - a) debits Fixed Assets A/c and credits Branch A/c.
 - b) debits Branch A/c and credits its Fixed Assets A/c.
 - c) none of the above.
- v) In case of inter-branch transactions, each branch
 - a) opens separate accounts for other branches.
 - b) passes no entry.
 - c) may treat such transactions as the transactions with the head office.
- vi) The Head Office Account maintained by the branch is of the nature of
 - a) Real Account.
 - b) Personal Account.
 - c) Nominal Account.

2.4 INCORPORATION OF BRANCH TRIAL BALANCE IN THE HEAD OFFICE BOOKS

Just because an independent branch keeps full system of accounting and prepares its own final accounts does not mean that its year-end results will not form part of the final accounts of the head office. In fact, as in case of dependent branches, the profit or loss made by an independent branch shall also be included in the General Profit and Loss Account which shows the profit or loss of the company as a whole. Similarly, its assets and liabilities shall also be shown as part of the assets and liabilities of the company. This is done by preparing the combined (consolidated) Balance Sheet of

the head office and its branches. Thus, it becomes necessary for the head office to incorporate the branch balances in the head office books by means of suitable journal entries at the end of the accounting period.

The incorporation of branch balances involves two steps;

- i) incorporation of branch profit or loss, and
- ii) incorporation of branch assets and liabilities.

For incorporation of the branch profit or loss, the head office may either pass various entries to include all revenue items and prepare a proper Branch Trading and Profit & Loss Account or simply pass one entry for profit or loss made by the branch after working it out with the help of a Memorandum Branch Trading and Profit & Loss Account. The first method is called 'detailed incorporation' and the second method is called 'abridged incorporation' (or simply short cut method). Whatever the method for incorporating branch profit or loss, the entries for incorporating branch assets and liabilities remain the same.

2.4.1 Detailed Incorporation

As stated earlier, under this method, the head office prepares a proper Branch Trading and Profit & Loss Account and makes entries for all revenue items before incorporating the branch assets and liabilities in its books. The entries passed under this method are as follows:

- 1) For items on the debit side of the Trading Account

Branch Trading A/c	Dr.
To Branch A/c	

 (This entry is passed for the total amount of items like opening stock, net purchases, wages, goods received from H.O., carriage inwards, etc.)
- 2) For items on the credit side of the Trading Account

Branch A/c	Dr.
To Branch Trading A/c	

 (This entry is passed for the total amount of items like net sales, closing stock, etc.)
- 3) For branch gross profit

Branch Trading A/c	Dr.
To Branch Profit & Loss A/c	

 (In case of gross loss, the entry will be reserved)
- 4) For items on the debit side of the Profit and Loss Account

Branch Profit & Loss A/c	Dr.
To Branch A/c	

 (This entry is passed for the total amount of items like salaries, rent, bad debts, repairs, depreciation, etc.)
- 5) For items on the credit side of the Profit & Loss Account

Branch A/c	Dr.
To Branch Profit & Loss A/c	

 (This entry is passed for total amount of items like interest received, discount received, commission received, etc.)
- 6) For branch net profit

Branch Profit & Loss A/c	Dr.
To General Profit & Loss A/c	

 (If there is net loss, the entry will be reversed)
- 7) For branch assets

Branch Assets A/cs	Dr.
To Branch A/c	

 (Each asset should be debited individually)
- 8) For Branch liabilities

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

 (Each liability credited individually. This should not include H.O. A/c balance)

As a result of the last two entries (7 and 8), the Branch Account in the head office books will stand closed because the net assets (assets minus liabilities) of the branch are equal to the balance in the Branch Account after branch net profit or net loss has been incorporated in head office books. In order to open the Branch Account in the next year's books of the head office and show the amount due from the branch, the entries for branch assets and branch liabilities (7 and 8 above) shall be reversed at the beginning of the next year..

Look at Illustration 3 and see how branch balances are incorporated in the head office books when detailed incorporation method is followed.

Illustration 3

On December 31, 1988, the Trial Balance of the Kanpur branch stood as follows:

	Dr. Rs.	Cr. Rs.
Stock on January 1, 1988	12,000	
Furniture	4,800	
Debtors	11,200	
Goods received from H.O.	32,000	
Salaries, rent and expenses	4,400	
Cash in hand	3,600	
Head Office Account		22,000
Sales		45,600
Sundry Creditors		400
	68,000	68,000

Stock on December 31, 1988 was Rs. 9,200.

Pass the necessary journal entries to incorporate Kanpur branch balances in the head office books, and prepare the Kanpur Branch Account in the books of the head office.

Solution

Head Office Books
JOURNAL

1988		Dr.	Rs.	Cr.	Rs.
Dec. 31	Kanpur Branch Trading A/c	Dr.	44,000		
	To Kanpur Branch A/c			44,000	
	(Being incorporation of opening stock and goods received from H.O.)				
" 31	Kanpur Branch A/c	Dr.	54,800		
	To Kanpur Branch Trading A/c			54,800	
	(Being incorporation of branch sales and closing stock)				
" 31	Kanpur Branch Trading A/c	Dr.	10,800		
	To Kanpur Branch P & L A/c			10,800	
	(Being gross profit transferred to Branch P & L A/c)				
" 31	Kanpur Branch P & L A/c	Dr.	4,400		
	(Being incorporation of branch expenses)			4,400	
" 31	Kanpur Branch P & L A/c	Dr.	6,400		
	To General Profit & Loss A/c			6,400	
	(Being incorporation of branches net profit)				

31	Branch Closing Stock A/c	Dr.	9,200	
	Branch Furniture A/c	Dr.	4,800	
	Branch Debtors A/c	Dr.	11,200	
	Branch Cash A/c	Dr.	3,600	
	To Kanpur Branch A/c			28,800
	(Being incorporation of branch assets)			
31	Kanpur Branch A/c	Dr.	400	
	To Branch Creditors A/c			400
	(Being incorporation of branch liabilities)			

Kanpur Branch Account			
Dr.			Cr.
	Rs.		Rs.
To Balance b/d	22,000	By Branch Trading A/c	44,000
To Branch Trading A/c	54,800	By Branch P & L A/c	4,400
To Creditors	400	By Closing Stock	9,200
		By Furniture	4,800
		By Debtors	11,200
		By Cash	3,600
	<u>77,200</u>		<u>77,200</u>

2.4.2 Abridged Incorporation

Incorporation of branch balances in the head office books can **also** be effected with the help of a short cut method known as the 'abridged incorporation'. Under this method, we prepare a Memorandum Branch Trading and Profit & Loss Account and pass a journal entry only for the net profit or net loss. Thus, the six entries passed under the detailed incorporation method are replaced by just one entry which is as follows :

Branch Account Dr.
 To General Profit & Loss A/c
 (Being branch net profit incorporated)

In case of net **loss**, the **above entry shall be reversed**.

Look at Illustration 4 and see **how branch balances are** incorporated in the Head Office **books** with the help of the short cut method.

Illustration 4

From the particulars given in Illustration 3, prepare **Memorandum** Branch Trading and Profit & Loss Account, **pass** the necessary **journal** entries to incorporate the Kanpur **branch balances**, and **prepare Kanpur Branch Account in the books of the** head office.

Books of Head Office

Memorandum Kanpur Branch Trading and Profit & Loss Account
for the year ended December 31, 1988

Dr.	Rs.	Cr.	Rs.
To Opening Stock	12,000	By Sales	45,600
To Goods Received from H.O.	32,000	By Closing Stock	9,200
To Gross Profit c/d	10,800		
	54,800		54,800
To Salaries, Rent and Expenses	4,400	By Gross Profit b/d	10,800
To Net Profit	6,400		
	10,800		10,800

Journal

1988	Dr.	Rs.	Rs.
Dec. 31	Kanpur Branch A/c To General Profit & Loss A/c (Being branch net profit incorporated)	6,400	6,400
" 31	Kanpur Branch Closing Stock A/c Kanpur Branch Furniture A/c Kanpur Branch Debtors A/c Kanpur Branch Cash A/c To Kanpur Branch A/c (Being branch assets incorporated)	9,200 4,800 11,200 3,600	28,800
" 31	Kanpur Branch A/c To Kanpur Branch Creditors A/c (Being branch liabilities incorporated)	400	400

Kanpur Branch Account

Dr.	Rs.	Cr.	Rs.
To Balance b/d	22,000	By Closing Stock	9,200
To General Profit & Loss A/c	6,400	By Furniture	4,800
To Creditors	400	By Debtors	11,200
	28,800	By Cash	300
			28,800

2.5 CLOSING ENTRIES IN BRANCH BOOKS

At the end of the accounting period, the branch books **have** also to be closed. For this purpose, the **branch can** pass the usual closing entries for transferring all revenue items to its Trading and Profit & Loss Account and ascertaining its net profit or net **loss**. The amount of net profit or net loss should be transferred to the Head Office Account by **passing** the following journal entry,

In case of net profit
 Profit and Loss A/c Dr.
 To Head Office A/c

In case of net loss
 Head Office A/c Dr.
 To Profit and Loss A/c

After the above entry for transferring net profit or net loss to the Head Office Account has been passed, the balance in the Head Office Account will be equal to the branch net assets (assets minus liabilities). The branch can then prepare its Balance Sheet by showing the Head Office Account balance on the liabilities side as this account would normally show a credit balance. If, however, the Head Office Account shows a debit balance, the same will appear on the assets side of the Balance Sheet.

The accounts pertaining to assets and liabilities can also be closed, if required, by transferring their balances to the Head Office Account. For this purpose, the following two journal entries will be passed in the branch books.

1) For transfers of assets
 Head Office A/c Dr.
 To Assets A/cs
 (The assets should be credited individually)

2) For transfer of liabilities
 Liabilities A/cs Dr.
 To Head Office A/c
 (The liabilities should be credited individually)

As a result of the above entries, the Head Office Account shall also be closed as it will not show any balance.

Look at Illustration 5 and see how does a branch close its books.

Illustration 5

A Delhi trader has independent branch at Patna. Its Trial Balance for the year ending December 31, 1989 is given below. Pass journal entries to close the books of Patna branch and prepare its Head Office Account.

Dr.		Trial Balance		Cr.	
	Rs.				Rs.
Purchases	25,600	Creditors			5,400
Stock on 1-1-89	16,400	Sales			69,900
Wages	13,101	Head Office			28,000
Factory Expenses	6,800	Discount			300
Salaries	8,000	Purchase Returns			600
Rent	3,400				
Sundry Expenses	4,000				
Goods Received H.O.	14,400				
Debtors	11,000				
Cash	1,500				
	1,04,200				1,04,200

Additional information

- The accounts of the branch fixed assets were maintained in the head office which show machinery of Rs. 50,000 and furniture of Rs. 2,000.
- Depreciation is to be charged @ 10% on Machinery and 15% on Furniture.
- Rs. 300 are due for salaries.
- A remittance of Rs. 8,000 made by branch on December 29, 1989, was received by head office on January 3, 1990.
- Closing stock at branch was Rs. 28,700.

Books of Patna Branch
Journal

		Rs.	Rs.
1989			
Dec. 31	Depreciation A/c To Head Office A/c (Being depreciation on fixed assets, accounts maintained by head office)	Dr. 5,300	5,300
" 31	Cash in Transit A/c To Head Office A/c (Being outstanding salaries)	Dr. 8,000	8,000
" 31	Salaries A/c To Salaries Outstanding A/c (Being outstanding salaries)	Dr. 300	300
" 31	Profit & Loss A/c To Head Office A/c (Being net profit transferred)	Dr. 2,200	2,200
" 31	Head Office A/c To Debtors To Cash A/c To Cash in Transit A/c To Closing Stock A/c (Being assets account balance transferred)	Dr. 49,200	11,000 1,500 8,000 28,700
" 31	Creditors Salaries Outstanding A/c To Head Office A/c (Being liabilities account balances transferred)	Dr. 5,400 Dr. 300	5,700

Head Office Account			
Dr.	Rs.	Cr.	Rs.
To Balance c/d	43,500	By Balance b/d	28,000
		By Depreciation A/c	5,300
		By Cash in Transit A/c	8,000
		By Profit & Loss A/c	2,200
	<u>43,500</u>		<u>43,500</u>
To Debtors	11,000	By Balance b/d	43,500
To Cash A/c	1,500	By Creditors	5,400
To Cash in Transit A/c	8,000	By Salaries outstanding A/c	300
To Closing Stock A/c	28,700		
	<u>49,200</u>		<u>49,200</u>

Working Notes

Trading and Profit & Loss Account			
Dr.	Rs.	Cr.	Rs.
To Opening Stock	16,400	By Sales	69,900
To Purchases 25,600		By Closing Stock	28,700
Less Returns 600			
	<u>25,000</u>		

To Goods from H.O.	14,400		
To Wages	13,100		
To Factory Expenses	6,800		
To Gross Profit c/d	22,900		
	<u>98,600</u>		<u>98,600</u>
To Salaries	8,000		
Add O/s	300		
	<u>8,300</u>	By Gross Profit b/d	22,900
To Rent	3,400	By Discount	300
To Depreciation	5,300		
To Sundry Expenses	4,000		
To Net Profit	2,200		
	<u>23,200</u>		<u>23,200</u>

- Notes: 1) The closing entries for transfer of revenue items have been omitted.
 2) The balance in Head Office Account after adjustment entries and transfer of net profit is Rs. 43,500. This is equal to the net assets at Patna as given below:

		Rs.	Rs.
Assets :	Debtors	11,000	
	Cash	1,500	
	Cash in Transit	8,000	
	Closing Stock	28,700	49,200
		<u>5,400</u>	
Liabilities:	Creditors	300	5,700
	Salaries O/s		
			<u>its. 43,500</u>

- 3) After the assets and liabilities are transferred to Head Office Account, it stands closed.

Check Your Progress B

- 1) Why is the incorporation of branch balances necessary in the books of the head office?

.....

- 2) Name the two methods of incorporating branch balances in the books of the head office?

.....

- 3) Fill in the blanks:

- i) The short cut method of incorporating the branch balances is called
- ii) The branch net profit can be incorporated in the head office books by debiting the Account and crediting the Account.
- iii) The net assets of the branch are equal to the of the Branch Account after the entry of branch net profit or net loss has been passed in head office books.
- iv) The balance in the Head Office Account in branch books represents the branch after the net profit or net loss has been transferred to this account.

2.6 A COMPREHENSIVE ILLUSTRATION

As stated earlier, any organisation having branches has to present the final accounts of the **organisation** as a whole and not separately for the head office and for the branches. Hence, it prepares General Profit and Loss **Account** which includes the profit or loss made by the branches and draws a consolidated Balance Sheet to show the assets and liabilities of both the head office and the branch office. Illustration 5 will help you to understand the preparation of a consolidated Balance Sheet.

Illustration 6

Following are the Trial Balances of the head office and its branch as on December 31, 1988.

	Head Office		Branch	
	Dr.	Cr.	Dr.	Cr.
	Rs.	Rs.	Rs.	Rs.
Capital		1,50,000		
Fixed Assets	86,000		26,000	
Stock	34,700		20,700	
Debtors and Creditors	17,820	13,900	14,800	23,000
Cash	10,740		1,500	
Profit & Loss		14,720		13,100
Branch Office	29,360			26,900
Head Office A/c				26,900
	<u>1,78,620</u>	<u>1,78,620</u>	<u>63,000</u>	<u>63,000</u>

Prepare the Balance Sheet of the business as on December 31, 1988 and pass the necessary journal entries in both sets of books to record the adjustments dealing with the following.

- On December 28, the branch had sent a cheque for Rs. 1,600 to the head office but not yet received by them.
- Goods valued at Rs. 560 had been forwarded by the head office to the branch and invoiced on December 30, but were not yet received by the branch.
- It was agreed that the branch should be charged with Rs. 400 for administration services rendered by the head office during the year.
- Rs. 1.250 for depreciation on branch assets, the accounts of which are maintained by the head office, is to be provided for.
- The balance of profit shown by the branch is to be transferred to the head office books.

Solution

Head Office Journal

		Dr.	Cr.
		Rs.	Rs.
1989			
1	Cash in Transit A/c To Branch A/c (Being cash sent by branch but not received by H.O. till December 31)	Dr. 1,600	1,600
2	Goods in Transit A/c To Branch A/c (Being goods invoiced on December 31. not yet received by the branch)	Dr. 460	460
3	Branch A/c To Gen. Profit & Loss A/c (Being administrative expenses charged by H.O. to the Branch)	Dr. 400	400

4	Branch A/c To Branch Fixed Assets A/c (Being depreciation on branch fixed assets accounts provided by H.O.)	Dr.	1,250	1,250
5	Branch A/c To General P & L A/c (Being profit of branch transferred to General P & L A/c)	Dr.	11,450	11,450

Branch Journal

		Dr.	Cr.
1989		Rs.	Rs.
1	Profit & Loss A/c To Head Office A/c (Being administrative expenses charged by H.O.)	Dr.	400
2	Depreciation A/c To Head Office A/c (Being depreciation on Branch fixed assets accounts for which are maintained by H.O.)	Dr.	1,250
3	Profit & Loss A/c To Head Office A/c (Being transfer of profit credited to Head Office A/c)	Dr.	11,450

Balance Sheet as on December 31, 1988

Liabilities	Rs.	Assets	Rs.
Capital	1,50,000	Fixed Assets	
Creditors		H.O.	86,000
H.O.	13,900	Branch	26,000
Branch	23,000	Less Dep.	<u>1,250</u>
Profit & Loss A/c			24,750
H.O.	15,120	Stock	
Branch	11,450	H.O.	34,700
	26,570	Branch	20,700
		Goods in Transit	<u>460</u>
			55,860
		Debtors	
		H.O.	17,820
		Branch	<u>14,800</u>
			32,620
		Cash	
		H.O.	10,740
		Branch	1,500
		Cash in Transit	1,600
		Cash for Exp.	<u>400</u>
			14,240
	<u>2,13,470</u>		<u>2,13,470</u>

Working Notes

1) The profits at branch and head office have been ascertained by preparing Profit and Loss A/c of the head office as well as that of branch.

Branch Profit and Loss Account

Dr.	Rs.	Cr.	Rs.
To Head Office Exp.	400	By Profit (as given)	13,100
To Depreciation	1,250		

Branch and Departmental Accounts

To Profit taken to General P&L A/c	Rs. 11,450		
	13,100		13,100

General (H.O.) Profit and Loss Account

To Profit c/d	Rs. 15,120	By Profit (as given) To Branch A/c	Rs. 14,720 400
	15,120		15,120
To Net Profit (taken to Balance Sheet)	26,570	By Profit b/d By Branch A/c (profit made by branch)	15,120 11,450
	26,570		26,570

2) The Head Office A/c in the books of branch and Branch A/c in the books of head office will appear as follows:

Branch Books
Head Office Account

Dr.			Cr.
To Balance c/d	Rs. 40,000	By Balance b/d By H.O. Exp. A/c By Depreciation By P & L A/c	Rs. 26,900 400 1,250 11,450
	40,000		40,000

Head Office Books
Branch Account

Dr.			Cr.
To Balance b/d To Branch Assets A/c To General P & L A/c	Rs. 29,360 1,250 11,450	By Goods in Transit By Cash in Transit By Balance c/d	Rs. 460 1,600 40,000
	42,060		42,060

3) The balance in the Branch Account in head office books and the balance in Head Office Account in branch books show the same amount. i.e., Rs. 40,000. But, the Branch Account balance is a debit balance while the Head Office Account balance is a credit balance. Having merged branch accounts with the head office accounts, these two balance cancel each other and so they do not appear in the consolidated Balance Sheet.

2.7 LET US SUM UP

Independent Branches are those branches which keep full system of accounting and enjoy certain amount of autonomy in functioning. They maintain complete records

on double entry system and prepare their own trial **balances**. The head office simply maintains a personal account for each branch which shows all transactions that take place between the branch and the head office. Similarly, each branch maintains a Head **Office** account to show the corresponding entries.

There are certain transactions which require special treatment both in head office and branch books. These are: (i) goods in transit (ii) cash on transit (iii) head office expenses chargeable to branch (iv) depreciation on branch fixed assets the accounts of which are maintained at the head office level, and (v) inter-branch transactions.

At the end of the accounting year, the branch sends its trial balance to the head office. This enables the head office to incorporate all branch balances in its books so as to include them in the final accounts of the organisation. The incorporation entries can be passed for all items given in branch Trial Balance (called detailed incorporation), or simply for branch **profit/loss** (based on Memorandum Branch Profit and Loss Account) and for branch assets and liabilities (called abridged incorporation or short cut method). After the incorporation entries have been passed, the Branch Account stands closed. At the beginning of the next year, the opening entries are **passed for** branch assets and liabilities which restores the balance in the Branch Account. The branch closes its books by transferring its profit or loss to Head Office Account which then shows a credit balance equal to the net assets with the branch.

2.8 KEY WORDS

Abridged Incorporation: A short cut method of incorporating the branch balances in head office books.

Cash-in-transit: Cash remitted by branch to head office but not received by head office by the end of the accounting year, or **vice versa**.

Consolidated Balance Sheet: **Combined** Balance Sheet showing both head office and branch assets and liabilities.

Goods-in-transit: Goods sent by head office to branch but not received by branch by the end of the **accounting** year, or **vice versa**.

Inter-branch transactions: The transactions between **two** or more branches under the same head office.

2.9 ANSWERS TO CHECK YOUR PROGRESS

- A 3) i) c
 ii) a
 iii) a
 iv) b
 v) c
 vi) b

- B 3) i) Abridged Incorporation
 ii) Branch Account. General Profit & Loss Account
 iii) balance
 iv) net assets

2.10 TERMINAL QUESTIONS/EXERCISES

Questions

- 1) How are branch **balances** incorporated in head office books at the end of the accounting year?
- 2) Write short notes including accounting treatment on the following:
 - a) Cash in Transit
 - b) Goods in Transit

- c) Head Office Expenses Chargeable to Branch
 d) Inter-branch Transactions.
- 3) How do you deal with purchase and depreciation of branch fixed whose assets accounts are maintained at the head office level?

Exercises

- 1) Show what entries would be passed by the Head Office to record the following transactions in their books.
- Goods amounting to Rs. 1,000 transferred from Varanasi branch to Allahabad branch under intimation from H.O.
 - Depreciation amounting to Rs. 2,000 on branch fixed assets when such assets' accounts are opened in the head office books.
 - A remittance of Rs. 3,000 made by the Calcutta branch to Head Office on December 25, 1988 and received by Head Office on January 4, 1989.
 - Goods of Rs. 10,000 sent by the Head Office on December 27, 1988 and received by Calcutta branch on January 10, 1989.
 - The Allahabad branch collected Rs. 4,000 from Allahabad customers of head office.
 - The Varanasi branch paid Rs. 25,000 for machinery purchased by the head office at Varanasi.
- 2) Show the journal entries that will be passed by Surat branch to record the following transactions in its books.
- Goods amounting to Rs. 6,000 transferred from Surat branch to Lucknow branch under instructions from Calcutta head office assuming that head office keeps a control on inter-branch transactions.
 - Depreciation on Lucknow Branch Machinery Rs. 4,000 and Surat Branch Machinery Rs. 3,000. When the Branch Machinery Account is maintained in head office books.
 - A remittance of Rs. 10,000 made by Surat branch to head office on December 28, 1988 but received by the head office on January 4, 1989.
 - Goods worth Rs. 15,000 sent by Head Office to Surat branch on December 26, 1988 but received by the latter on January 2, 1989.
- 3) On December 31, 1988, the Trial Balance of Varanasi branch stood as follows:

Particulars	Debit Rs.	Credit Rs.
Stock on January 1, 1988	12,000	
Furniture	4,800	
Debtors	11,200	
Goods Received from Delhi H.O.	32,000	
Salaries, rent and expenses	4,400	
Cash in hand	3,600	
Delhi Office Account		22,000
Sales		45,600
Sundry Creditors		400
Total Rs.	68,000	68,000

Stock on December 31, 1988 was Rs. 9,200. Prepare (1) Trading and Profit & Loss Account, Balance Sheet and Head Office Account in Varanasi branch books (2) Prepare journal entries necessary to incorporate the Varanasi Branch Trial Balance and show the Varanasi Branch Account in the head office books.

(Answer: Branch Profit Rs. 6,400; Balance Sheet Total Rs. 28,800; Head Office A/c Balance Rs. 28,400 and Total of Varanasi Branch A/c Rs. 77,200.)

- 4) The Kanpur branch of **Wahi Bros.** sent the following Trial Balance to Read office as on December 31, 1988:

	Rs.		Rs.
Sundry Debtors	12,000	Sundry Creditor	8,600
Cash in hand	6,250	Goods returned to H.O.	2,250
Furniture	1,900	Sales	1,12,500
Stock on 1-1-88	2,250	Head Office A/c	10,250
Goods from H.O.	34,000		
Purchases	66,450		
Wages & Salaries	5,500		
Trade Expenses	5,250		
	<u>1,33,600</u>		<u>1,33,600</u>

The stock on December 31, 1988 was Rs. 5,200. Pass the necessary journal entries to incorporate the above figures and show Branch A/c in head office books, and Trading and Profit & Loss A/c and Balance Sheet in the branch books.

(Answer: Branch profit Rs. 6,500; Balance Sheet Total Rs. 25,350; Total of Branch A/c Rs. 1,38,800.)

- 5) Following is the Trial Balance of Kanpur Branch of Varanasi head office. Prepare Trading and Profit & Loss A/c and Balance Sheet in the books of branch. Also show Head Office A/c in the books of branch:

	Rs.		Rs.
Furniture & Fixtures	1,500	Cash in Bank	3,000
Purchases	20,000	Carriage etc.	150
Goods from H.O.	40,000	Bad Debts	100
Sales	80,000	Allowances to Customers	200
Sundry Debtor	10,000	Bills Receivable	4,000
Sundry Creditors	12,000	Stock on 1-1-88	10,000
Head Office A/c Salaries	6,400	Returns inwards	1,000
General Exp.	600	Returns to H.O.	400
Rent & Taxes	600		

Closing Stock on December 31, 1988 Rs. 9,000

(Answer: Branch Net Profit Rs. 10,350; Balance Sheet Total Rs. 27,500; H.O. A/c Balance including net profit Rs. 15,500.)

- 6) From the following balances, prepare the Branch Current Account in the books of head office and Head Office Current A/c in the books of branch.

	Head Office		Branch	
	Dr. Rs.	Cr. Rs.	Dr. Rs.	Cr. Rs.
Branch Current A/c	5,000	-	-	-
Goods sent to Branch	-	7,800	-	-
Goods received from H.O.	-	-	7,000	-
Head Office Current A/c	-	-	-	1,400

(Answer: Goods in Transit Rs. 800; Cash in Transit Rs. 2,800.)

- 7) A limited company with its head office in Delhi has a branch at Kota which obtains goods from the head office as well as from outside suppliers. The branch keeps a separate set of books. On June 30, 1989 the trial balances of the head office and its branch were as follows:

	Head Office		Branch	
	Dr. Rs.	Cr. Rs.	Dr. Rs.	Cr. Rs.
Share Capital	-	30,000	-	-

Branch and Departmental Accounts

P & L Account balance on 1-7-88

Fixed Assets	16,000	4,000	8,000	-
Opening Stock	14,000	-	1,900	-
Debtors and Creditors	17,000	10,000	1,500	2,050
Cash	3,000	-	1,000	-
Purchases and Sales	1,20,000	1,40,000	6,750	20,500
Sundry Expenses	15,000	-	2,250	-
Goods from H.O. to Branch	-	12,000	11,500	-
Current Accounts on 30-6-89	11,000	-	-	10,350
	1,96,000	1,96,000	32,900	32,900

The difference between the balances of head office and the Branch Current Accounts is due to goods and cash being in transit at the close of the year. Fixed assets are to be depreciated at 10 per cent. Stocks on June 30, 1989 were : Head Office Rs. 10,000 and Branch Rs. 2,100.

Prepare consolidated Balance Sheet of the company. Also show journal entries for the adjustments and the incorporation of Branch Trial Balance.

(Answer: Balance Sheet Total Rs. 56,850.)

Hints: Goods in Transit Rs. 500; Cash in Transit Rs. 150; Branch Net Loss Rs. 600; H.O. Net Profit (excluding branch net loss) Rs. 11,400.

Note : These questions will help you to understand the unit better. Try to answer them, but do not send your answers to the University. These are for your practice only.

UNIT 3 DEPARTMENTAL ACCOUNTS

Structure

- 3.0 Objectives
- 3.1 Introduction
- 3.2 Meaning and Purpose of Departmental Accounts
- 3.3 Importance of Departmental Accounts
- 3.4 Recording of Transactions
- 3.5 Allocation of Expenses
- 3.6 Inter-Departmental Transfers
- 3.7 Let Us Sum Up
- 3.8 Key Words
- 3.9 Answers to Check Your Progress
- 3.10 Terminal Questions/Exercises

3.0 OBJECTIVES

After studying this unit, you should be able to :

- describe the nature and purpose of accounting for departmental transactions,
- outline the importance and advantages of departmental accounts,
- explain the process of recording departmental transactions and prepare departmental trading and profit & loss account, allocate the expenses between different departments by selecting some rational basis, explain the accounting treatment of inter-departmental transfers on the basis of cost price as well as transfer price,
- work out the amount of unrealised profit in respect of unsold/unused goods and explain its accounting treatment.

3.1 INTRODUCTION

You have learnt that a business unit may be operating through a network of branches like those of Bata which has branches all over the country or Snowwhite which has branches all over the city of Delhi. You also know that, in such a situation, each branch is treated as a separate profit centre and the profit or loss is worked out for each branch separately. Similarly, in many cases, the activities of the business unit may be divided into a number of divisions or departments that are usually located under the same roof and each dealing in different types of goods. For example, a Super Market or a Departmental Store may have separate sales counters/sections for ready-made garments, cosmetics, electrical appliances, medicines, gift items, etc. For purposes of meaningful supervision of the affairs of each section or department and the assessment of their individual performance it is advisable to maintain accounts in such a manner that we can prepare a trading and profit & loss account for each section or department separately and work out its profit or loss. In this unit, you will learn how are the departmental accounts maintained and how are the common expenses allocated to each section or department in order to arrive at its profit or loss separately,

3.2 MEANING AND PURPOSE OF DEPARTMENTAL ACCOUNTS

Departmental accounts refer to the maintenance of accounts of a business in a manner that makes it possible to ascertain the operational results of each activity, section or department by preparing separate trading and profit & loss account for each one of them. In fact, departmental accounts are nothing more than as many trading and profit & loss accounts as there are the departments.