12th Accountancy – Study Materials

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CHAPTER-1 ACCOUNT FROM INCOMPETE RECORDS

I VERY SHORT ANSWER QUESTION

1. **What is meant by incomplete record?**

When accounting records are not strictly maintained according to double entry system. Them records are called incomplete records.

2. **State the accounts generally maintained by small sized sole trader when double entry accounting system is not followed?**

- Generally, cash and personal accounts are maintained fully.
- Real and nominal accounts are not maintained.

3. **What is a statement of affairs?**

- It is a statement showing the balances of assets and liabilities on a particular date.
- It is prepared under single entry system to find out capital.
- Capital = Assets -Liabilities

II SHORT ANSWER QUESTION

1. **What are the features of incomplete records?**

Nature

- It is an unscientific way of recordings transactions.
- Accounting principles are not followed properly.

Type of accounts maintained

- Only cash and personal accounts are maintained fully.
- Real and nominal accounts are not maintained properly.

Lack of uniformity

- Different organizations record their transactions according to their need and conveniences.

2. **What are the limitations of incomplete records?**

Lack of proper maintenance of records

- It is an unscientific way of maintaining records.
- Real and nominal accounts are not maintained.

Difficulty in preparing trial balance

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- The accounting records are incomplete.
- Hence, it is difficult to prepare trial balance.

Errors and frauds

- Errors and frauds cannot be easily detected from partial records.

3. State the difference between double entry system and incomplete records.

Basic	Double entry system	Incomplete records
Types of accounts maintained	All accounts are maintained	Only personal and cash accounts are maintained
Suitable	It is suitable for all types of organization	It is only suitable for sole trading and partnership firms
Preparation of trial balance	It can be prepared easily	It is difficult to prepare it
Reliability	It is reliable	It is not reliable
Recording of transactions	Both debit and credit aspects are recorded	Both debit and credit aspects are not recorded completely

4. State the procedure for calculating profit and loss through statement of affairs.

- The difference between the closing and opening capital are taken as profit or loss of the business.
- Due adjustments are to be made for drawings (+) and additional capital (-).

Statement of profit or loss for the year ended….

	Particulars	Rs.
	Closing capital	XXX
(+)	Drawings	XXX
		XXX
(-)	Additional capital	XXX
	Adjusted closing capital	XXX
(-)	Opening capital	XXX
	Profit or loss	XXX

- If adjusted closing capital is more than the opening capital- Profit
- If adjusted closing capital is lesser than the opening capital- Loss

5. Difference between statement of affairs and balance sheet.

Basic	Statement of affairs	Balance sheet
Reliable	It is not reliable	It is reliable
Accounting system	It is prepared from single entry system	It is prepared from double entry system

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Missing items	It is very difficult to trace the missing items	Missing items can be traced very easily
Basis of preparation	It is not fully based on ledger	It is fully based on ledger
Objective	It is prepared to find out the capital	It is prepared to find out the financial position

6. How is the amount of credit sale ascertained from incomplete records?

- **By preparing total debtors accounts credit sale can be prepared**

DR. TOTAL DEBTORS ACCOUNT CR.

Particulars	**Rs.**	**Particulars**	**Rs.**
To balance b/d	XXX	By cash a/c (received)	XXX
(opening balance)	XXX	By bank a/c (cheques	XXX
To sales a/c (credit	XXX	received)	
sales)		By discount allowed	XXX
To bank a/c (cheque	XXX	a/c	XXX
dishonoured)		By sales returns a/c	XXX
To bills receivable a/c	XXX	By bad debts a/c	XXX
(bills dishonoured)		By bills receivable a/c	XXX
		(bills received)	
		By balance c/d	XXX
		(closing balance)	
	XXX		XXX

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CHAPTER-2 ACCOUNTS OF NOT-FOR-PROFIT ORGANIZATIONS

I VERY SHORT ANSWERS

1. **State the meaning of not-for-profit organization.**
   - Some organizations are established for the purpose of rendering services to the public without any profit motive.
   - These organizations are called not for profit organization.
   - EX: art, culture, education, sports, etc.
2. **What is receipts and payments account?**
   - It is a summary of cash and bank transactions of not-for-profit organization prepared at the end of each financial year.
   - It is a real account in nature.
   - It begins with the opening of cash and bank balances.
3. **What is legacy?**
   - A gift made to a not-for-profit organization by a will, is called legacy.
   - It is a capital receipt.
4. **Write a short note on life membership fees.**
   - Amount received towards life membership fee from members.
   - It is a capital receipt.
   - It is non-recurring in nature.
5. **Give four examples for capital receipts of not-for-profit organization.**
   - Sale of fixed assets
   - Legacy
   - Life membership fees
   - Endowment fund
6. **Give four examples for revenue receipts of not-for-profit organization.**
   - Interest on fixed deposit
   - Sale of old news papers
   - Interest on investment
   - Subscription

II SHORT ANSWERS

1. **What is income and expenditure account?**
   - It is nominal account.
   - It is prepared to find out surplus and deficit relating to a particular year.
   - It is just like preparing profit and loss account.
   - Only revenue and income and expenditure items are recorded.
   - Depreciation and outstanding expenses are also recorded.
2. **State the difference between receipts and payments account and income and expenditure account.**

Basic	Receipts and payment account	Income and expenditure account
Nature of account	It is real account	It is nominal account
Basis of accounting	It is based on cash system	It is based on accrual system
Opening and closing balance	It commences opening balance and end with closing balance	There is no opening and closing balance

Nature of items	It contains actual receipts and payments	It contains only revenue expenses and incomes
Purposes	It is prepared to know the cash receipt and cash payment	It is prepared to know the surplus and deficit

3. How annual subscription is dealt with in the final accounts of not-for-profit organization?

The annual subscription is dealt with in the final accounts of following as:

- Treatment in income and expenditure account
- Treatment in balance sheet

DR. INCOME AND EXPENDITURE ACCOUNT FOR THE YEAR ENDED…. CR.

Expenditure	Rs.	Income	Rs.	Rs.
		By subscription	XXX	
		Less: subscription for the previous year	XXX	
			XXX	
		Less: subscription for the subsequent year	XXX	
			XXX	
		Add: outstanding subscription for the current year	XXX	
			XXX	
		Add: received in advance during the previous year for the current year	XXX	XXX

BALANCE SHEET AS ON…..

Liabilities	Rs.	Assets	Rs.
Subscription received in advance for the subsequent year	XXX	Outstanding subscription for the:	
		Current year	XXX
		Previous year	XXX

4. How the following items are dealt with in the final accounts of not-for- profit organization?

SALE OF SPORTS MATERIALS

- Consumable items such as sports material, stationary, medicines, etc. consumed during the year.
- Consumption= opening stock + purchases – closing stock.

LIFE MEMBERSHIP FEES

- Amount received towards life membership fee from members.
- It is a capital receipt.
- It is non-recurring in nature.

TOURNAMENT FUND

- If there are any specific funds such as tournament fund, prize fund, etc. it is shown on liabilities side of balance sheet.
- It is a revenue receipt.
- It is recurring in nature.

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CHAPTER-3 ACCOUNTS OF PARTNERSHIP FIRM FUNDAMENTALS

I VERY SHORT ANSWERS

1. **Define partnership.**
    - The relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

-Indian Partnership Act,1932

2. **What is meant by fixed capital method?**
    - The capital of the partners is not altered and remains generally fixed.
    - Two accounts are maintained for each partner
      (a)Capital account
      (b)Current account
3. **Why is profit and loss appropriation account prepared?**
    - It is prepared for the purpose of adjusting the transaction relating to the amount due to and amount due from partners.
4. **What is a partnership deed?**
    - It is a document in writing that contains the terms of the agreement among the partners.
    - It is also called articles of partnership.
5. **Why is profit and loss appropriation account prepared?**
    - It is prepared for the purpose of adjusting the transaction relating to the amount due to and amount due from partners.
6. **What is the journal entry to be passed for providing interest on capital to a partner?**
    - **For providing interest on capital**

Date	Particulars	L.F.	Debit	Credit
	Interest on capital a/c Dr. To partner capital / current a/c (Interest on capital provided)		XXX	 XXX

- **For closing interest on capital account**

Date	Particulars	L.F.	Debit	Credit
	Profit and loss appropriation a/c Dr. To interest on capital a/c (Interest on capital closed)		XXX	 XXX

II SHORT ANSWERS

1. **State the features of partnership.**
    - It is an association of two or more person.
    - Minimum 2 and maximum number of members 50 limited.
    - They agreement may be oral or written.
    - It's carried on by all or any of them acting for all.
2. **State the difference between fixed capital method and fluctuating capital method.**

Basic	Fixed capital method	Fluctuating method
Number of accounts	Two accounts are maintained (a)Capital account	Only pone account capital account is maintained.

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	(b)Current account	
Change in capital	The amount of capital not changes from period to period.	The amount of capital changes from period to period.
Closing balance	It always shows the credit balance.	It always shows the debit or credit balance.
Adjustments	All adjustments done in current account.	All adjustments done in capital account.

3. **State any six contents of a partnership deed.**
    - Name of the firm and nature and place of business
    - Date of commencement and duration of business
    - Names and addresses of all partners
    - Capital contributed by each partner
    - Profit sharing ratio
    - Amounts of drawings allowed to each partner
4. **Write a brief note on the applications of the provisions of the Indian partnership act, 1932 in the absence of partnership deed.**

Remuneration to partners:

- No salary or remuneration is allowed to any partner. [Sec 13(a)]

Profit sharing ratio:

- Profits and losses are to be shared equally. [Sec 13(b)]

Interest on capital

- No interest is allowed on capital. [Sec 13]

Interest on loans advanced by partners to the firm:

- Interest on loans is to be allowed at the rate of 6%. [Sec 13(d)]

Interest on drawings:

- No interest is charged on the drawings of the partners.

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CHAPTER-4 GOODWILL IN PARTNERSHIP ACCOUNT

I VERY SHORT ANSWERS

1. **What is goodwill?**
   - It is the good name or reputation of the business.
   - It is an intangible asset.
   - It has no physical existence.
   - It is shown under fixed assets in the balance sheet.
2. **What is acquired goodwill?**
   - Goodwill acquired by making payment in cash or kind is called acquired goodwill.
   - The excess of purchase consideration over the value of net assets acquired is treated as acquired goodwill.
   - It is also called purchased goodwill.
3. **What is super profit?**
   - It is the excess of average profit over the normal profit of the business.
   - Super profit = Average profit – Normal profit
4. **What is normal rate of return?**
   - It is the rate at which profit is earned by similar business entities in the industry under normal circumstances.
5. **State any two circumstances under which goodwill of a partnership firm is valued.**
   - Change in profit sharing ratio
   - Admission of a partner
   - Retirement or death of a partner
   - Dissolution of partnership firm

II SHORT ANSWERS

1. **State any six factors determining goodwill.**
   - Profitability of the firm
   - Favorable location of the business enterprises
   - Good quality of goods or service offered
   - Efficiency of management
   - Degree of competition
   - Tenure of the business enterprises
   - Other factors
2. **How is goodwill calculated under the super profit method?**
   - Average profit = Total profits / Number of years
   - Normal profit = Capital employed x NRR
   - Capital employed = Fixed assets + Current assets – Current liabilities
   - Super profit = Average profit – Normal profit
   - Goodwill = Super profit x No. of years of purchase
3. **How is the value of goodwill calculated under the capitalization method?**
   - Capitalized value of the business = Average profits / No. of years x 100
   - Capital employed = Fixed asset + Current asset – Current liabilities
   - Goodwill = Capitalized value of the business – Capital Employed

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CHAPTER-5 ADMISSION OF A PARTNER

I VERY SHORT ANSWERS

1. **What is meant by revaluation of assets and liabilities?**
   - When a partner is admitted into the partnership the assets and liabilities are revalued as the current value may differ from book value.
   - Determination of current value of assets and liabilities is called revaluation of assets and liabilities.
2. **How are accumulated profits and losses distributed among the partners at the time of admission of a new partner?**
   - Any reserve fund, accumulated profit and loss belong to the old partners and hence these should be distributed to the old partners in the old profit-sharing ratio.
   - Profit and losses of previous year which are not distributed to the partners are called accumulated profits and losses.
3. **Give the journal entry for writing off existing goodwill at the time of admission of a new partner.**

Date	Particulars	L.F.	Debit	Credit
	Old partner capital a/c Dr. To Goodwill a/c (Being existing goodwill is written off)		XXX	 XXX

4. **What is sacrificing ratio?**
   - It is ratio of share sacrificed by the old partners.
   - Share of the new partner is the sum of share sacrificed by the old partners.
5. **State whether the following will be debited or credited in the revaluation account.**
   (a)Depreciation on assets **(b)Unrecorded of liability**
   (c)Provision for outstanding expenses **(d)Appreciation of assets**

(a) Depreciation on assets - Debited

(b)Unrecorded of liability - Debited

(c)Provision for outstanding expenses - Debited

(d)Appreciation of assets - Credited

II SHORT ANSWERS

1. **What are the adjustments required at the time of admission of a partner?**
   - Distribution of accumulated profits, reserves and losses.
   - Revaluation of assets and liabilities.
   - Determination of new profit-sharing ratio and sacrificing ratio.
   - Adjustment for goodwill.
   - Adjustment of capital on the basis of new profit-sharing ratio.
2. **What are the journal entries to be passed on revaluation of assets and liabilities?**

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*For increase in the value of asset *For decrease in the amount of liability *For recording unrecorded asset

JOURNAL ENTRY

Date	Particulars	L.F.	Debit	Credit
	Concerned asset a/c Dr. Concerned liability a/c Dr. To Revaluation a/c (Assets and liabilities are recorded)		XXX XXX	 XXX

*For decrease in the value of asset *For increase in the amount of liability *For recording unrecorded liability

JOURNAL ENTRY

Date	Particulars	L.F.	Debit	Credit
	Revaluation a/c Dr. To Concerned asset a/c To Concerned liability a/c (Assets and liabilities are recorded)		XXX	 XXX XXX

*For profit on revaluation

JOURNAL ENTRY

Date	Particulars	L.F.	Debit	Credit
	Revaluation a/c Dr. To Old partner capital a/c (Revaluation of profit transferred to capital account)		XXX	 XXX

*For loss on revaluation

JOURNAL ENTRY

Date	Particulars	L.F.	Debit	Credit
	Old partner capital a/c Dr. To Revaluation a/c (Revaluation of profit transferred to capital a/c		XXX	 XXX

3. Write a short note on accounting treatment of goodwill.

When new partner brings cash towards goodwill

- When the new partner brings cash towards goodwill in addition to the amount of capital.
- It is distributed to the existing partners in the sacrificing ratio.

When the new partner does not bring goodwill in cash or in kind

- If the new partner does not bring goodwill in cash or in kind, his share of goodwill must be adjusted through the capital accounts of the partners.

When the new partner brings only a part of the goodwill in cash or in kind

- Sometimes the new partner may bring only a part of the goodwill in cash or assets.

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- In such a case, for the cash or the assets brought, the respective account is debited and for the amount not brought in cash or kind, the new partners capital account is debited.

Existing goodwill

- If goodwill already appears in the books of accounts, at the time of admission if the partners decide.
- It can be written off by transferring it to the existing partner capital or current account in the old profit-sharing ratio.

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CHAPTER-6 RETIREMENT AND DEATH OF A PARTNER

I VERY SHORT ANSWERS

1. **What is meant by retirement of a partner?**
   - When a partner leaves from a partnership firm, it is known as retirement.
   - It is also called outgoing or retirement partner.
   - On retirement of a partner, existing agreement comes to an end.
2. **What is gaining ratio?**
   - The continuing partners may gain a portion of the share of profit of the retiring partner.
   - Gaining ratio = New share – Old share
   - It is calculated at the time of retirement.
3. **What is the purpose of calculating gaining ratio?**
   - The purpose of finding the gaining ratio is to be bear the goodwill to be paid to the retiring partner.
4. **What is the journal entry to be passed to transfer the amount due to the decreased partner to the executor of the deceased partner?**

Date	Particulars	L.F.	Debit	Credit
	Deceased partner capital a/c Dr. To Deceased partner executor a/c (Being deceased partner amount transferred to capital account)		XXX	 XXX

II SHORT ANSWERS

1. **List out the adjustments made at the time of retirement of a partner in a partnership firm.**
   - Distribution of accumulated profits, reserves and losses.
   - Revaluation of assets and liabilities.
   - Determination of new profit-sharing ratio and gaining ratio.
   - Adjustment for goodwill.
   - Adjustment for current year profit or loss up to the date of retirement.
   - Settlement of the amount due to the retiring partner.
2. **Distinguish between sacrificing ratio and gaining ratio.**

Basic	Sacrificing ratio	Gaining ratio
Meaning	A share of profit sacrificed by the old partner to a new partner	A share of profit gained by existing partner from retiring partner
Time of calculation	It is calculated at the time of admission of a partner	It is calculated at the time of retirement of a partner
Formula	Sacrificing ratio = old ratio - new ratio	Gaining ratio = new ratio – old ratio
Purpose	It is calculated to determine the amount to be adjusted towards goodwill for the sacrificing partners	It is calculated to determine the amount to be adjusted towards goodwill for the gaining partners

3. **What are the ways in which the final amount due to an outgoing partner can be settled?**

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***Cash due paid immediately**

JOURNAL ENTRY

Date	Particulars	L.F.	Debit	Credit
	Retiring partner capital a/c Dr.		XXX	
	To Cash/Bank a/c			XXX
	(Being cash due paid immediately recorded)			

***Cash due not paid immediately**

JOURNAL ENTRY

Date	Particulars	L.F	Debit	Credit
	Retiring partner capital a/c Dr.		XXX	
	To Retiring partners loan a/c			XXX
	(Being cash due not paid immediately recorded)			

***Cash due paid partly immediately**

JOURNAL ENTRY

Date	Particulars	L.F.	Debit	Credit
	Retiring partner capital a/c Dr.		XXX	
	To cash/ Bank a/c			XXX
	To Retiring partners loan a/c			
	(Being cash due paid partly immediately recorded)			

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CHAPTER-7 COMPANY ACCOUNTS

I VERY SHORT ANSWERS

1. **What is share?**
   - The capital of a accompany is divided into small units of fixed amount.
   - These units are called shares.
2. **What is over subscription?**
   - When the number of shares applied fir is more than the number of shares offered for subscription.
   - It is said to be over subscription.
3. **What is meant by calls in arrear?**
   - Sometimes shareholders may fail to pay the amount due on calls.
   - The amount called up but not paid is called calls in arrears.
4. **Write a short note on securities premium account.**
   - When a company issue shares at a price more than the face value, shares are said to be issued at premium.
   - The excess is called as premium.
   - The amount of securities premium may be included in application money or allotment money or in call.
5. **Why are shares forfeited?**
   - If the shareholders fail to pay the amount due on calls, shares will be forfeited.

II SHORT ANSWERS

1. **What is reissue of forfeited shares?**
   - Shares forfeited can be reissued by the company.
   - The shares can be reissued at any price.
   - But the reissues price cannot be less than the amount unpaid on forfeited shares.
2. **Write a brief note on calls in advance.**
   - The excess amount paid over the called-up value of share is known as calls in advance.
   - It is the excess money paid on application or allotment or calls.
3. **State the difference between preference shares and equity shares.**

Basic	Preference shareholders	Equity shareholders
Meaning	Preference shares are those shares which have preferential rights regarding dividend and return of capital	Equity shares are those shares which have no preferential rights so, they are called ordinary shares
Rate of dividend	Fixed rate of dividend is payable	Rate of dividend changes according to profit earned by company
Voting power	They do not have any voting rights	They have voting rights according to number of shares held by members

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Affairs of company	They do not have any rights to appoint board of directors	They have to appoint the board of directors through voting
Payment of dividend	Dividend first distributed to preference shareholders	Dividend distributed after paying preference shareholders

4. Write a short note on (a)Authorized capital (b)Reserve capital

Authorized capital

- It means such capital as is authorized by the memorandum of association.
- It is the maximum amount which can be raised as capital.
- It is also known as registered capital or nominal capital**.**

Reserve capital

- The company can reserve a part of its subscribed capital to be called up only at the time of winding up.
- It is called reserve capital.

5. What is meant by issue of shares for consideration other than cash?

- A company may issue equity shares either for cash or for consideration other than cash.
- When shares are issued for cash, the cash may be received
  - (a) In instalments
  - (b) At one time

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CHAPTER-8 FINANCIAL STATEMENT ANALYSIS

I VERY SHORT ANSWERS

1. **What are financial statements?**
   - Financial statements are the statements prepared by the business concerns at the end of the accounting period to ascertain the operating results and the financial position.
2. **List the tools of financial statement analysis.**
   - Comparative statement
   - Common size statement
   - Trend analysis
   - Fund flow analysis
   - Cash flow analysis
3. **What is working capital?**
   - The capital of a business which is used in its day-to-day trading operation.
   - Working capital = Current asset – Current liabilities
4. **When is trend analysis preferred to other tools?**
   - When data of more than two years are to be analyzed it may be difficult to use comparative statement.
   - For this purposes trend analysis may be used.

II SHORT ANSWERS

1. **'Financial statements are prepared based on the past data'. Explain how this is a limitation.**
   - Financial statements are prepared based on historical data.
   - They may not reflect current position.
   - The previous data does not reveal the opening results and financial position of the business concern.
   - So, it is a limitation.
2. **Write a short note on cash flow analysis.**
   - It is concerned with preparation of cash flow statement which shows the inflow and outflow of cash and cash equivalents in a given period of time.
   - Cash includes cash in hand and demand deposits with banks.

3. **Briefly explain any three limitations of financial statements.**

   (a) Record of historical
   - Financial statements are prepared based on historical data.
   - They may not reflect the current position.

   (b) Ignore price level changes
   - Adjustments for price level changes are not made in the financial statements.
   - Hence, financial statements may not reveal the current position.

   (c) Lack of consistency
   - Different business concerns may use different accounting methods.
   - Hence comparison between two business concerns becomes difficult.

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4. **Explain the step involved in preparing comparative statement?**
    - **Column 1:** Particulars of items
    - **Column 2:** Enter absolute amount of year 1
    - **Column 3:** Enter absolute amount of year 2
    - **Column 4:** Show the different in amounts between year 1
    - **Calculations of percentage increases and decreases**

$$= \frac{\text{Absolute amount of increases or decreases}}{\text{Year 1 amount}} * 100$$

5. **Explain the procedure for preparing common-size statement?**
   Common – size statement can be prepared with three columns
    - **Column 1:** Particulars of items of income statement or balance sheet
    - **Column 2:** Enter absolute amount
    - **Column 3:** Choose a common base as 100
      For example, revenue from operations can be taken as the base for income statement and total of balance sheet can be taken as the base for balance sheet.

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Chapter – 9 RATIO ANALYSIS

I VERY SHORT ANSWER QUESTION

1. **What is meant by accounting ratio?**
    - When ratios are calculated on the on the basis of accounting information, these are called accounting ratios.
    - It is the numerical relationship between two items.
2. **What is quick ratio?**
    - Quick ratio gives the proportion of quick assets to current liabilities.
    - It is otherwise called liquid or acid test ratio.
    - It is calculated as follows:

      Quick ratio =Quick assets/Current liabilities
3. **What is meant by debit equity ratio?**
    - It is calculated to assess the long-term solvency position
    - It expresses the relationship between long term debt and shareholders funds
    - It is computed as follows:

      Debt equity ratio =Long term debt/Shareholders funds
4. **What does return on investment ratio indicate?**
    - It shows the proportion of net profit before interest and tax to capital employed
    - It is an overall measure of profitability of a business concern
    - It is computed as follows:

      Return on investment (ROI) = Net profit before interest and tax/Capital Employed
5. **State any two limitations of ratio analysis?**

   (a)Ratios are only means:
    - Ration are not end in themselves but they are only means to achieve a particular purpose.

   (b)Accuracy of financial information:
    - It depends on the accuracy of information taken from financial statements.

II SHORT ANSWER QUESTION

1. **Explain the objectives of ratio analysis.**
    - To simplify accounting figures
    - To facilitate analysis of financial statements
    - To analysis the operational efficiency of a business
    - To analyze the operational efficiency of a business
    - To help in budgeting and forecasting
    - To facilitate intra firm and inter firm comparison of performance
2. **What is inventory conversion period? How is it calculated?**
    - **Inventory conversion period is the time taken to sell the inventory.**
    - **A shorter inventory conversion period indicates more efficiency in the management of inventory.**
    - **It is computed as follows:**

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Inventory conversion Period (in days) = **Number of days in a year/Inventory turnover ratio**

Inventory conversion Period (in months) = **Number of months in a year/Inventory turnover ratio**

……………………………………………………………………….

Inventory turnover ratio

3. How is operating profit ascertained?

- Operating profit = Gross profit – Operating expenses
- Gross profit = Sales – Cost of goods sold

OR

- Gross profit = Revenue from operation – Cost of revenue from operation
- Operating expenses = Selling + Office + Distribution + Administration expenses

4. State any three advantages of ratio analysis.

(a)Measuring financial solvency

- Ratio analysis helps to ascertain the liquidity or short term.
- Solvency and long-term solvency of a business concern.

(b)Facilitating investment decisions

- Ratio analysis helps the management in making effective decisions regarding profitable avenues of investment.

(c)Analyzing the profitability

- Ratio analysis helps to analyze the profitability of a business in terms of sales and investments.

5. Bring out the limitations of ratio analysis.

(a)Ratios are only means

- Ratios are not end in themselves but they are only means to achieve a particular purpose.

(b)Accuracy of financial information

- It depends on the accuracy of information taken from financial statements.
- If the statements are inaccurate, ratios are also be inaccurate.

(c)Change in price level

- Ratio analysis may not reflect price level changes and current values as they are calculated based on historical data given in financial statements.

************ALL THE BEST ***********

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