

Royalty Account Accounting-2.

**Prepared By: Prof.Dr.Dhaval Ardeshana
[M.Com./ M.Phil./ Ph.D]
B.Com. English Medium Department
Gurukul Mahila College- Porbandar.**

Meaning of Royalty

- The word Royalty means Payment made by lessee or tenant in form of rent to the person called lessor or landlord for using certain right or asset belonging to the latter. It is payment made of having privilege for using some right.
- For example: right to use certain patent, right to publish and sell books or right to extract minerals like coal, iron, etc.

Contract of Royalty and points included in the contract:

- contract of royalty is a written document between the lessor and lessee in which terms and conditions regarding the lease are mentioned.
- **Period of Contract:** In this clause, the period of Contract of royalty between lessor and lessee is shown. Generally period for contract are for long time, say 20 years or 25 years etc. the royalty contract and its conditions are bound to both parties till the end of contract period.

- **Rate of Royalty:** rate of royalty is decided either on production quantity or on units sold. It is calculated per ton or per unit etc. rate of royalty should be fixed after considering many factors because it has long terms effect for both the parties.
- **Minimum Rent:** it is also known as “ dead rent” or “ fixed rent” minimum rent means the rent payable by the lessee to lessor irrespective of the fact whether he has obtained any benefit or not, out of the property let out to him by lessor.

Minimum rent is fixed on following basis:

- Amount of minimum rent remain unchanged or stable for every year. Eg. Rs. 10,000 yearly for entire tenure of contract.
- Amount of minimum rent increase after certain period. Eg: For first two years annual Minimum rent is Rs.10,000 and after that 20 % increase in Minimum rent . i.e. it will be 12,000 per year.
- If production is held up due to strike, fire, or accident, if there is clause for reduction of minimum rent, then minimum rent is reduced either in term of percentage or in proportion of time work is closed.

- **Short working:** short working is the excess of minimum rent over the actual amount of royalty. In short $\text{Short working} = \text{minimum rent} - \text{actual royalty}$.
- For example, if the royalty for first year is rs. 30,000 and minimum rent is Rs. 50,000. Then Rs. 20,000 is termed as short working.
- Thus, the purpose of minimum rent is to protect the interest of landlord while purpose of right to recoupment of short working is to protect the interest of the tenant or lessee.
- Short working amount can be recouped only from excess of royalty over minimum rent. Land lord/ lessor always get the amount of minimum rent or royalty which ever is more. Short working can be recouped subject to time limit specified in the contract.

Royalty Table:

Year	Prod. In Ton.	Rate Of Royalty	Royalty In Rs.	M.R	S.W	S.W Recov erable	Short worki ng not recou pable	Bal. of short worki ng	Amt Payabl e To landlo rd

Journal entries in the books of lessee:

- **When Amt of royalty is ZERO or Nil:**

In this situation journal entries can be passed as following two ways.

1. Direct entry:

- Short working A/c dr.....
To land lord A/c

2. As per minimum rent method:

- a. short working A/c Dr.....
To Minimum rent A/c.....
- b. Minimum rent A/c Dr.....
To landlord A/c

OR

- When royalty and minimum rent are equal or royalty is more than the minimum rent but the short workings can not be recovered or the right to recoup short working is over.
- **[In this situation all the amount of royalty would be paid to landlord]**
- Royalty A/c Dr.....
To Landlord A/c.....

OR

- **When royalty is more than the amount of minimum rent and the short working amount is recoverable or the right to recoup the short working is not over.**
- Royalty A/c Dr.....
 - To Short Working A/c.....
 - To landlord A/c.....

- **2. When amount paid to landlord:**

Landlord A/c Dr.....

To Bank A/c

- **3. At the end of financial year, the amount of royalty is transferred to P & L A/c.**

- P & L A/c Dr.....

To Royalty A/c

- **4. At the end of financial year, the amount of short working not recovered due to expiry of the right, it will be written off and transferred to P & L A/c.**

- P & L A/c Dr.....

To Short workings A/c.....

Journal entries in the books of lessor:

[1] When royalty is Zero or nil:

- Lessee A/c Dr.....
To Short working suspense A/c.... Or

[1] Royalty is less than minimum rent:

- Lessee A/c Dr.....
To short working suspense A/c
To royalty receivable A/c..... Or

[1] when royalty and minimum rent is equal or royalty is more than minimum rent but amount from short working suspense A/c is not given as recouped short working to lessee due to finish the terms.

- Lessee A/c Dr.....
To royalty A/c..... Or

[1] When royalty is more than minimum rent and the amount of short working recoup is given from 'short workings suspense A/c' to lessee.

- Lessee A/c Dr.....
Short working A/c Dr.....
To Royalty receivable A/c

[2] When amount received by lessee

Bank A/c Dr.....

To lessee A/c ...

[3] At the end of financial year the amount of 'Royalty receivable' is credited to P & L A/c By transferring.

Royalty receivable A/c Dr.....

To P & L A/c

[4] At the end of financial year the amount of short working suspense account is credited to P & L A/c due to finish the terms and conditions of short working recoupable

Short working suspense A/c Dr.....

To P&L A/c

- NOTE: THE WORD “ROYALTY SUSPENSE A/C” IS ALSO USED INSTEAD OF THE WORD “SHORT WORKINGS SUSPENSE A/C”.

