



MADURAI KAMARAJ UNIVERSITY

(University with Potential for Excellence)

DIRECTORATE OF DISTANCE EDUCATION



M.Com.

(COMMERCE)

& M. Com. Co-operative Management

First Year

FINANCIAL ACCOUNTING

VOLUME - 1

LESSONS: 1-2

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Dear Student
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DISTANCE EDUCATION**

M.Com & M.Com (Co-op.Management)

FIRST YEAR

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Madurai Kamaraj University

Madurai – 625 021

Dear Student

It gives us immense pleasure in welcoming you to the first year M.Com. Degree course through correspondence. While extending our warm welcome we also take this opportunity to wish you a bright academic year. You are expected to take the University examination in all the four papers.

1. Business Environment and Policy
2. Financial Accounting
3. Banking and Insurance
4. Computer Applications in Business

Each paper carries 100 marks with 3 hour duration for each examination.

Teaching Accountancy through correspondence is not so easy particularly at post graduate level. Though we try to elucidate the principles involved in different chapters with carefully selected illustrations, mere reading of these problems alone will not help you. Accountancy is a subject which requires constant practice. Moreover, as you are going to face the post graduate examination a sound and deep knowledge of the subject matter is normally expected. As such you are directed to work out as many advanced problems as possible on each and every chapter falling under the syllabus. Constant exercise alone will give you courage and confidence to face the University examination. We agree that the time at your disposal is very short. But it is up to you to provide it substantial part of the day towards your study to have a regular systematic preparation. Only sheer hard working during this academic year is going to fetch you a bright and prosperous future, the fruits of which you are going to enjoy throughout your life.

In this lesson we have provided you with the syllabus, list of reference books, list of lessons that you will get in accountancy.

Yours Sincerely,

Staff

SYLLABUS

1.2 Financial Accounting

Unit I : Principles of Book keeping – Rules for debit and Credit – Journalizing –
Subsidiary books Ledger – Trial Balance – Rectification of Errors.

Unit II : Final Accounts and Balance Sheet of Sole Trader – Trading Account,
Profit and Losses Account – Balance Sheet – Opening Entries – Closing Entries
Adjusting entries.

Unit III: Bills of Exchange – Trade Bills – Accommodations Bills – Mutual
Accommodation Bills – Journal entries and ledger.

Unit IV: Consignment and Joint Venture, Account Current, Average Due date.

Unit V : Depreciation – Methods -- necessity – various methods of providing
depreciation Account Treatment.

Unit VI: Accounting for Non-Trading Concern-Final Accounts-Receipts and
Payments account – Income and Expenditure account – Balance Sheet.

Unit VII: Single entry and preparation of accounts from incomplete records –
Memorandum Method – Conversion method.

Unit VIII: Branch Accounts – Independent Branch – Dependent Branch including
stock and debtor system.

Unit IX: Departmental Accounts – Preparation of departmental trading accounts,
allocating of expenditure in the Profit and Loss Account

Unit X : Accounting for Insurance claims for stock destroyed, Assets destroyed
Loss of Profit Policy – average clause Policy

Books for References:

1. JAIN AND NARANG - Advanced Accountancy
2. SHYKLA AND GREWAL - Advanced Accounts
3. R.L.GUPTA - Advanced Accountancy
4. WILLIAM PICKLES - Accountancy
5. SPICER AND PEGLER - Book-keeping and Accounts
6. M.A.ARULANDAM & RAMAN - Advanced Accounting.

Note: Distribution of marks between theory and problem in the ratio of 40:60 respectively.

List of Lessons

(M.Com & M.Com Co-op Management)

First Year

FINANCIAL ACCOUNTING

LESSON NO.	TOPICS
1.	Book-keeping
2.	Final Accounts and Balance Sheet
3.	Bills of Exchange
4.	Consignment, Joint-Venture, Account Current and Average Due Date
5.	Depreciation
6.	Accounting for Non-Trading Concern
7.	Single Entry
8.	Branch Accounts
9.	Departmental Accounts
10.	Accounting for Insurance Claims.

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Lesson No.	Topic	Page No.
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LESSON NO.	TOPICS
1.	Book-keeping
2.	Final Accounts and Balance Sheet
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4.	Consignment, Joint-Venture, Account Current and Average Due Date
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7.	Single Entry
8.	Branch Accounts
9.	Departmental Accounts
10.	Accounting for Insurance Claims

LESSON – 1

BOOK-KEEPING

Though the origin of Book-keeping dates back five centuries ago, its development as a science is a recent phenomenon and it is still in its growth process. Book-keeping has now become a part of business. A business organisation constantly enters into transactions with others. It is essential for the organization to record systematically all organizations involving transfer of money or money's worth in broader sense, "it is information and designed to communicate significant facts".

We give below a few definitions of Book-keeping A.H.ROSENKAMPE defines: "Book-keeping is the art of recording business transactions in systematic manner"

R.N. CARTER gives the following definition:

"Book-keeping is the science and art of correctly recording in books of account all those business transactions that result-in the transfer of money's worth".

I.C.COOPPER defines Book-keeping as follows:

"Book-keeping may be described as the science of recording transaction in money or money's worth in such a manner that, at any subsequent date, their nature and effect may be clearly understood and that when required a combined statement of their result may be prepared".

Book-keeping is said to be statistical procedure for the collection, classification and summarization of financial information.

Book-keeping is an art and science of recording business transactions in terms of money. in books of accounts with a view to arriving at the financial state of the business at any time.

Definition of Book Keeping

According to R.N.CARTER "Book keeping is the science and art of correctly recording in books of account all those business transactions that result-in the transfer of money's worth."

NOTES

Subject-matter: The subject-matter of Book-Keeping is business transactions, in terms of money, of any given business for a given period.

These transactions result from the purchase and sale of goods and purchase and sale of services by the given business house. They may be expressed in different currencies as Rupees and Paise. Dollars and Cents, etc.

Objectives of Book-keeping:

A businessman always tries to expand his business, increase his turnover and reduce the operating expenditure. His main aim is to earn maximum profit with minimum expenses. This is indicated by the properly maintained business record.

Therefore the objects of Book-keeping are twofold.

Objectives of Book-Keeping:

1. To record all business transaction.
2. To find out the profit or loss of the firm
3. To know the financial position of the business.

1. To record permanently all business transactions and

2. To show the effect of each transactions and also the combined effect of all such transactions for a given period so as the find out profit the business has earned or loss incurred and also to know the correct financial position on a particular date.

BOOK KEEPING Vs ACCOUNTING

The terms book keeping and accounting are used interchangeably by laymen. In practice, they are different in their nature and scope.

Book-Keeping is concerned with the recording of business transactions in a systematic manner. This work is mechanical and respective in nature. It does not need specialized skill and knowledge. It is usually entrusted to the junior level employees of the accounts department who are known as Book-Keepers.

Book-Keeping is responsible for recording business transactions of financial nature in the books of original entry. Each transaction is recorded with as many details as possible. The date of the transactions, quantities and prices involved, the accounts to be debited and credited respectively, the ledger folio number are all shown

systematically. Each entry is made on the basis of supporting, verifiable documentary evidence. Book-Keeping prepares the ground for the important steps of finalization and interpretation which are usually performed by "accounting".

Accounting includes the designing of suitable accounting system, preparation of financial statements; cost studies, income tax work etc. It is also responsible for analyzing and interpreting the accounting information for internal as well as external end users. Accounting work requires some skill, imagination and experience. The person in charge of this work is called the Accountant.

Accounting has to devise a suitable system of maintaining accounts after studying the requirements and characteristics of the organization. The various books of accounts have to be organized as per the needs of the system developed. Different forms, books, sheets etc., have to be designed and printed.

When accounts are finalized, accounting is responsible for making various adjustments essential for ascertain profit or loss for the period, and showing the financial position of the business. The financial statements are to be analyzed and interpreted to extract additional and useful information as per the requirements of the management, owners, creditors etc.

In a broad sense, accounting includes book-keeping also. But in practice, book-keeping and accounting differ in their scope and nature of their functions. In small business, both functions may be divided into book keeping and accounting sections.

Science and Art of Book-keeping

'Book-keeping' is a science as well as art. What is Science? The word "Science" is used for systematized knowledge of any subject. Then, what is an art? Art is the revelation of an individual's skill in various form of action. Principles of record-keeping constitute science; actual keeping of record is art. It is science because; it's based on principles of accounting and provides for methods of proving the accuracy of account-keeping. It is an art because; it is based on the art of writing.

Functions of Book-Keeping:

1. Keeping systematic records
2. Protecting properties of the business
3. Meeting legal requirements

NOTES

Book-keeping is a practical subject. Because of its practical utility, it has over shadowed its theoretical study.

METHODS OF ACCOUNTING

Basically all methods of accounting are classified under two headings:

1. Single Entry system
2. Double Entry system

Meaning of single entry system:

A simple bookkeeping system; transactions are entered in only one account.

Single Entry System

The term single entry is vaguely used to define the method of maintaining accounts which do not conform to strict principles of double entry. It is wrong to define it as system. The term "Single entry" does not mean that there is only one entry for each transaction. It simply signifies that principles of double entry book-keeping have not been observed in all cases. Under this system, only the personal accounts of the debtors and creditors and cash book of the trader are maintained. Impersonal accounts such as sales accounts, purchase accounts etc., as well as the assets accounts are ignored. The absence of the two fold effect of each transaction makes it impossible to prepare a trial balance and to check the arithmetical accuracy of the books of accounts, engendering a spirit of laxity and inviting fraud and misappropriations. Owing to the absence of purchases and sales accounts, the preparation of trading account is not possible. Again profit & Loss account and Balance sheet cannot be prepared due to the absence of nominal accounts and real accounts and real accounts are also not reliable.

Double Entry System

This system was invented by an Italian named Iuco Pacioli in 1494 A.D. and it has spread all over the world, becoming as popular as Arabic numerals, According to this system, every transaction has two aspects. One is benefit receiving aspect or income g aspect and the other one is benefit giving aspect or outgoing aspect. The benefit receiving aspect is said to be a "Debit" and the benefit giving aspect is said to be a

What is double entry system?

Bookkeeper debits the transaction to one account and credits it to another.

“Credit”. For every transaction, one account is to be debited and another account is to be credited in order to have a complete record of the transaction. Therefore, every transaction affects two accounts in opposite direction.

Meaning of debit and Credit

The word Debit is derived from the Latin Word Debitum which means Due for that.

In short, the benefit receiving aspect of a transaction is known as debit.

The word Credit is derived from the Latin word Ceder which means Due to that.

The benefit giving aspect of a transition is known as credit.

The abbreviations “Dr” for debit and “Cr” for credit for usually used.

By convention, the left hand side of an account is termed as debit side and right hand side of an account is termed as credit side.

ADVANTAGES OF DOUBLE ENTRY BOOK-KEEPING

The Double Entry System which was believed to be used by the Venetian merchants in the 15th century is the only method fulfilling all the objects of systematic Book-keeping. The following are the merits of this system:

1. It keeps a complete record of both personal accounts (i.e. accounts of persons) and impersonal accounts (i.e., accounts of things, profits and losses)
2. It helps us to check the arithmetical accuracy of the books by preparing what is known as Trial Balance.
3. It helps us to find out the profit made or loss incurred during any given period and the various sources of income and heads of expenditure by preparing what is known as Balance Sheet.

What is debit?

An accounting entry acknowledging sums that are owing.

4. It helps us to find out financial position of the business on any particular date (i.e., the amount of Assets, the amount of Liabilities and Capital) by preparing what is known as Balance Sheet.
5. Any Information regarding any item can be had at any time.
6. A comparison of expenditure, income, purchases, sales, stock etc., of the current year with those of the previous years can be made, thereby enabling a trader to control and regulate his business to maximize his profits.
7. It is easy for taxation authorities to make correct assessments.

Limitations of Double Entry Book-keeping

The system, though scientific and accurate is not free from defects. They are:

1. If a transaction is completely omitted to be recorded or recorded in wrong accounts or with wrong amounts, it may remain undiscovered.
2. As it requires the maintenance of a number of books of accounts and a number of persons to look after them the system is sophisticated.

Differences between Double Entry and Single Entry System:

DOUBLE ENTRY SYSTEM	SINGLE ENTRY SYSTEM
1. It is the only scientific system of keeping Books of accounts	1. It is not a system at all. It is unscientific.
2. It maintains a complete record of both Personal accounts and impersonal accounts	2. It maintains a partial record. Only personal accounts and cash accounts are maintained
3. A Trial Balance can be prepared to test The arithmetical accuracy of the books Accounts.	3. A Trial Balance cannot be prepared since debits and credit do not agree

- | | |
|--|---|
| 4. Both Profit and Loss Account and Balance Sheet can be prepared. | 4. With the incomplete records Profit And Loss Account and Balance Sheet Cannot be easily prepared. |
| 5. Comparison with the previous record is Possible | 5. Comparison with the previous records is impossible. |
| 6. The taxation authorities will not accept It for assessment purposes | 6. The taxation authorities will not accepts it for assessment purposes. |

SOME IMPORTANT BOOK-KEEPING TERMS:

Before we start the study of the subject of 'Book Keeping' it will be worthwhile to clarify some of the terms which are commonly used again and again.

1. Business Transaction: It implies exchange of money (Cash) or money's worth (things, good or services) between two persons. Something having value is received and something having value is given it.

(e.g.) Bought Furniture for Cash Rs.300/-. This is a business transaction. Here, Cash is exchanged for Furniture (Furniture is received. Cash goes out)

Buying and Selling goods, receipts and payment of cash and other similar dealings are called business transactions.

2. Goods: The things which a trader sells are called goods.

A furniture dealer deals in furniture. A clock dealer deals in clocks. All articles whether, clock, cycle, paper, pencil or pen are goods when purchased for the purpose of selling.

Goods bought are recorded as purchases.

Goods Sold are recorded as Sales.

Goods returned by us to our suppliers are recorded as Purchases Returns.

NOTES

What is business transaction?

Business transaction means exchange of money (Cash) or money's worth (things, good or services) between two persons.

NOTES

Goods unsold at the end of the year are Closing Stock.

The same Closing Stock is recorded at the beginning of the next year as Opening Stock.

3. Cash Trade & Credit Trade: When 'goods' are bought and sold by a 'trader' for hard cash, it is cash trade. It is credit trade when payment for goods purchased or receipt for goods sold is postponed to some future date.

What is Assets?

Assets are anything of material value or usefulness that is owned by a person or company.

4. Assets: Assets are properties belonging to a person or a business such as cash, buildings etc., and includes money owing to him or the business.

5. Proprietor: A proprietor is a person who introduces capital with the object of earning profits.

6. Capital: The amount with which the proprietor starts his business is called Capital. In a running business, it is the excess of Assets over Liabilities.

The same can be expressed by means of an equation.

$$C = A - L$$

$$C = \text{Capital}$$

$$A = \text{Assets and}$$

$$L = \text{Liabilities}$$

Or

$$A = C + L$$

What are drawings?

Drawings are the withdrawals of money or money's worth by the proprietor from the business for his personal use.

7. Liabilities: Capital of the proprietor and the debts which are due by the business to other parties are known as Liabilities.

8. Drawings: Drawings are the withdrawals of money (cash) or money's worth (Goods) by the proprietor from the business for his personal use.

9. **Debit:** It denotes receiving aspect.

10. **Credit:** It denotes giving aspect.

11. **Debtor (Dr.):** A Debtor is one who receives the benefit and he owes money to the business. (e.g.) Mr. Senthil Sold goods to Raman on credit for Rs.300. Raman is the receiver of goods. As such is a debtor. That is, he owes Rs.300 to the business.

12. **Creditor (Cr):** A Creditor is one who gives the benefit and to whom, the business owes money. (e.g.) Bought goods from Gafoor on credit for Rs.100. Gafoor is the giver of goods. As such he is a creditor. This is business owes him Rs.100.

13. **Cash Discount:** Cash Discount is an allowance against the amount due.

14. **Trade Discount:** Trade Discount is an allowance against the Invoice (Bill) price.

15. **Received:** Cash received on account (e.g.) Rs.500 received from George.

16. **Paid:** Cash paid on account (e.g.) Paid Raman Rs.75.

17. **Entry:** A record of transaction in account books is called Entry.

18. **Books of accounts:** It includes both Journal and Ledger

19. **Journal:** Journal is a book in which the very first record of any business transaction is made.

20. **Ledger:** Transactions from Journal are recorded here in a classified form.

21. **Account:** Account is a statement containing transactions regarding a particular person or a particular article or particular item of expenses grouped together for specified period.

22. **Journalisation:** Entering the business transaction in the Journal is called Journalizing.

Who is debtor?

Debtors are a person who owes a creditor; someone who has the obligation of paying a debt.

What is journal?

Journal is a book in which the very first record of any business transaction is made.

NOTES

23. Journal Entry: What we write in the Journal is called Journal Entry.

24. Narration: Narration is nothing but a brief explanation which is added after each Journal Entry.

25. Posting: The process of transferring the entries from Journal and recording them in the Ledger is called Posting.

26. Folio: Two pages facing each other is called folio.

27. Contra: It is a Latin term which means opposite or on the other side.

28. Profit: The amount by which capital increases at the end of trading period is called Profit.

Mr.X's Capital on 1st Jan., 1995 Rs.40, 000

Mr.X's Capital on 31st Dec., 1995 Rs.45, 000

Profit Rs. 5,000

The Capital has increased by Rs.5, 000 (Rs.45, 000-40,000) which represents profit.

29. Loss: The amount by which Capital decreases is called loss.

30. Gross Profit: The excess of the selling price over cost of goods sold.

31. Net Profit: Net profit is the remaining amount after meeting all business expenses against gross profit.

32. Solvent: A solvent is one whose assets are in excess of liabilities.

33. Insolvent: If a trader's liabilities are in excess of his assets, he is said to be an insolvent.

What is Folio?

It is the system of numbering pages.

CLASSIFICATION OF ACCOUNTS

Every business.....

- (i) Deals with other persons (including individual, concerns, firms, companies, corporate bodies etc.)
- (ii) Possesses Assets (like Cash, Land, Buildings, Furniture, Stock of goods etc.,)
- (iii) Pays expenses (such as Rent, Salary, Postage, Advertising etc.,) Receives incomes (such as Commission, Interest, and Dividend etc.)

From this, we can derive that every business has to keep:

- (i) An account for each person
- (ii) An account for each asset
- (iii) An account for each expense and income

In order to keep a complete record of all business transactions a business man keeps:

- (i) Accounts in the name of persons known as Personal Accounts.
- (ii) Accounts in the name of assets known as Property Accounts.
- (iii) Accounts under the head of expenses or income known as Nominal Accounts.

Accounts are classified in this manner, so that, transaction can be recorded systematically. An account is nothing but a brief history of statement for grouping together all transactions which have taken place between two parties.

We can classify the accounts as under:

NOTES

Classification of Accounts:

1. Personal account:
2. Real accounts
3. Nominal account:

NOTES

liabilities.
Assets are in excess of
A solvent is one whose

Meaning of solvent:

What is Impersonal Accounts?

All accounts other than personal accounts are impersonal accounts.

Classification of Accounts

(A) Personal Accounts and

(B) Impersonal Accounts

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(A) **Personal Accounts** are accounts of persons, in which are recorded the transactions relating to Persons like X 'Co., Ltd., "Madurai Kamaraj University Co-operative Stores Ltd., Madurai Corporation etc. They represent the accounts of your debtors and creditors in your ledger with you. A person may be either a receiver of something or giver of something. As such, the rule is

Debit the receiver and

Credit the giver

(B) **Impersonal Account:** All Accounts other than Personal Accounts are **impersonal** accounts. They are divided into

(i) Property or Real accounts and

(ii) Nominal or Fictitious accounts

(i) **Property Accounts:** Real Accounts or Property Accounts are accounts that record the real things owned by the business. They record transactions relating to properties like Cash, Land, and Buildings Stock of Goods etc. They represent the accounts of assets owned by you as a businessman.

A property may come into the business or it may go out of the business. As such, the rule is

Debit what comes in and

Credit what goes out

(ii) Nominal Accounts: Nominal Accounts are accounts that record all business expenses, losses gains and incomes. They record transactions relating to expenses, and incomes like Salaries, Wages rent, Commission, Interest, Dividend etc. They represent the accounts of expenses of various nature incurred as well as incomes earned by you as a businessman. They are not real. That is why they are called Fictitious Accounts. Either you incur a loss or earn a gain. As such the rule is,

Debit all expenses& losses and
Credit all incomes & gains

What is Nominal Accounts?

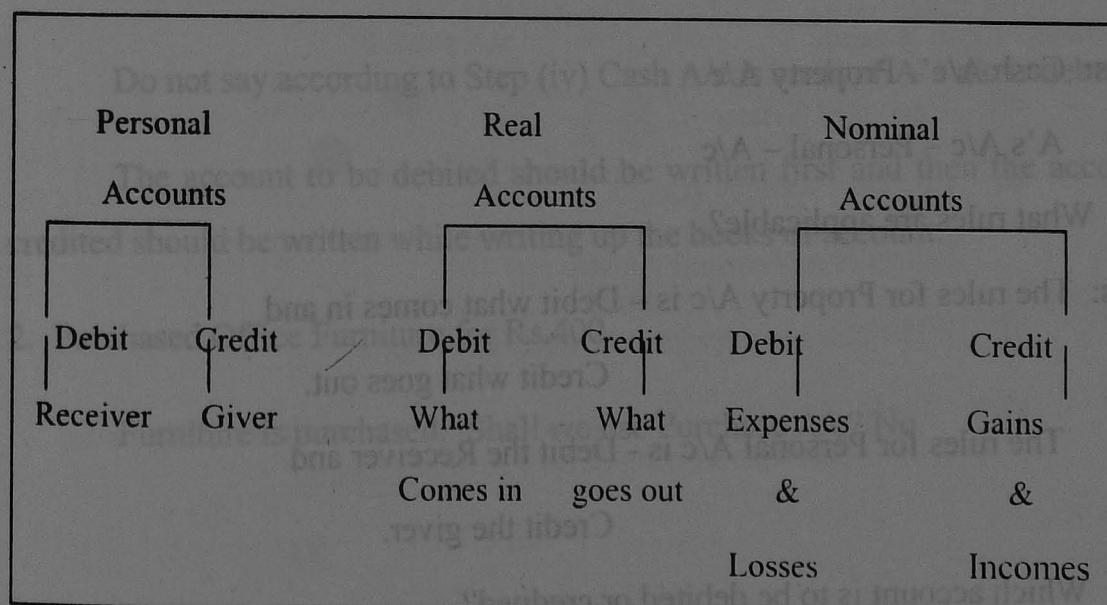
Nominal accounts are accounts that record all business expenses, losses gains and incomes.

Fundamental Rules of Double Entry

No	Class of Account	Rule
1.	PERSONAL	Debit the Receiver Credit the Giver
2.	PROPERTY OF REAL	Debit what comes in Credit what goes out
3.	NOMINAL OR FICTITIOUS	Debit all Expenses and Losses Credit all incomes and Gains

These three basic rules are once again explained:

Fundamental Rules of Double Entry



ILLUSTRATIONS

Let us now take a few transactions and find out the Debtor and Creditor aspects:

1. Paid Cash Rs.50 to Mr. A

Before finding out the two aspects, ask yourself the following questions:

- (i) What are the two accounts involved in this transaction?
- (ii) What is their classification? Does it belong to personal property or nominal group?
- (iii) What rules are applicable?
- (iv) What account is to be debited and which one to be credited?

If you are able to give answers to the above questions it will help you to record it in the books of account.

Let us study our transactions involved?

- (i) What are the two accounts involved?

Ans: Cash Account, and A's Account

- (ii) What is their classification?

Ans: Cash A/c – Property A/c

A's A/c – Personal – A/c

- (ii) What rules are applicable?

Ans: The rules for Property A/c is – Debit what comes in and
Credit what goes out.

The rules for Personal A/c is - Debit the Receiver and
Credit the giver.

- (iv) Which account is to be debited or credited?

Ans: Cash A/c is to be credited, since, cash goes out. A A/c is to be debited since A is the receiver.

The above method implies 4 steps

- (i) Two Accounts are identified
- (ii) Classification of the two accounts is made
- (iii) Rules of journalisation are applied
- (iv) Debit & Credit aspects are recorded

At the time of writing or giving the answer you will have to say

("So and so Account is Debtor")

To So and so Account is Creditor")

For the above transaction, you will say

	Rs.	Rs.
A's A/c.	Dr.	50
To Cash A/c.		50

If one account is debtor, the other automatically becomes a creditor. Therefore we need not say or write creditor at the time of final analysis.

This is read as A's account debtor fifty rupees. To Cash account fifty rupees.

Do not say according to Step (iv) Cash A/c is creditor A's a/c is debtor.

The account to be debited should be written first and then the account to be credited should be written while writing up the books of account.

2. Purchased Office Furniture for Rs.400

Furniture is purchased. Shall we use Purchase A/c? No.

NOTES

The reason is that Furniture is not meant for re-sale.

Therefore was should not use Purchases A/c. As such, we can use Furniture Account.

What about the second account? We are purchasing furniture against cash. Therefore, Cash is implied.

Apply the questions and get your answers so as to give the correct answer.

Step - (i) Furniture and Cash

Step - (ii) Both are property accounts

Step - (iii) Debit what comes in and Credit what goes out

Step - (iv) Furniture A/c is to be debited and Cash A/c is to be credited
because furniture comes in and Cash goes out.

	Rs.	Rs.
Furniture A/c	400	
To Cash A/c		400

3. Paid Salary Rs.35

Paid means Cash is paid

Step - (i) Cash and Salary

Step - (ii) Cash is Property A.c

Salary is a Nominal A/c

Step - (iii) What comes in and credit what goes out

Step - (iv) Cash goes out. So Cash A/c is to be credited: salary is an expense as such Salary is to be debited.

Rs.	Rs.
-----	-----

Salary Dr. 35

To Cash A/c. 35

4. Received Rent Rs.150

Go through the steps mentally and find out the answers

(i) Received means Cash – So Cash and Rent

(ii) Cash – Property

Rent – Nominal

(iii) Debit what comes in a Credit what goes out

Debit all expenses and Credit incomes.

Rent A/c is to be debited, since it represents an income

(iv) Cash A/c is be debited, since it comes in

	Rs.	Rs.
Cash A/c.	Dr.	150

To Rent A/c	150
-------------	-----

Books used for recording transactions are called Books of Accounts. Every business must invariably maintain two books of accounts. These are.....

1. Journal and

2. Ledger

What is journal?

A daily written record of (usually personal) experiences and observations in business

The Journal is the 'day-by-day' book of the business wherein both the aspects of all transactions are recorded in chronological order. The first entry of a business transaction is made in the Journal. The Journal is thus, a Book of Prime Entry. It is otherwise known as Book of Original Entry. These entries are then posted from the Journal into the Ledger. As such the Ledger is known as the Principal Book or Main Book. The Ledger is otherwise known as Book of Final Entry.

The Journal merely helps the posting of entries from Journal into the Ledger. Hence, Journal is known as Subsidiary Record or Subsidiary Book. The Journal is sub-divided into a number of Subsidiary books, for convenience are described by other names, and have certain specialized, functions. One Book is meant for Credit Purchases and another for Credit Sales and so on.

Similarly the Ledger is divided into a number of separate accounts. For instance, one Ledger may contain the accounts of all persons from whom a trader purchases goods on credit' and another the accounts of all persons to whom he sells goods on Credit. ** All other accounts are maintained in a ledger known as General Ledger.

Relation between Journal & Ledger

JOURNAL

1. The Journal is the Subsidiary Book
2. Transactions are first entered in it

LEDGER

1. This Ledger is the Main Book.
2. These entries are subsequently
Posted to the appropriate

Accounts in the Ledger.

3. The Journal is a daily record

3. Posting is done as per the

Convenience of the business

4. Entering the transactions in the Journal is
Called Journalizing

4. The Process of recording in the
Ledger is called posting.

The Journal has the following five columns:

1. Date

2. Particulars

3. LF (Ledger Folio)

4. Debit Amount

5. Credit Amount

The act of entering transactions in a Journal is called Journalizing. What we write in the Journal is known as Journal Entry.

Procedure:

Before a Journal Entry is actually made, it is necessary to analyze each transaction as to know:

(i) What accounts are involved?

(ii) What is their classification?

(iii) What rule of entry is applicable? And

(iv) Which account is to be debited and which one to be credited?

Soon after analyzing a transaction, it must be noted in the Journal in the manner explained below:

The date, month and year of the transaction is entered in the First Column

NOTES

A reference to the paged (or folios) in the Ledger to which the entries are posted is made in the Third Column.

The amount to be debited is written in the Fourth Column.

The amount to be credited is written in the Fifth Column.

Note: A short explanation known as narration must be written between the date line and the folio line. Finally, a red line should be drawn between each transaction from the date column to the folio column.

Theoretically, it is possible to carry out a complete system of Book-keeping by writing Ledger. As such, there would be no record of all the business transacted in the date order in which it occurred. It is for this reason that the Journal is used in addition to the Ledger.

Example: 1

1st Sep 2003 'X' started a business with cash Rs.5, 000

Step (i) What are the accounts involved?

Cash and X's Capital.

Step (ii) What is their classification?

Cash is a property Account

X's Capital is a Personal Account

Step (iii) what rules are applicable?

Debit what comes in

Credit the giver

Step (IV) Which account is to be debited and which one to be credited?

Cash account is to be debited

X's Capital Account is to be credited

This transaction should be viewed that the business and proprietor (X) are two distinct entities, from book-keeping point of view.

Answer

DATE	PARTICULAR	L.F.	Dr	Cr.
2003 Sept. 1	Cash A/c. Dr.* To X's Capital A/c.** (being the amount invested in the business)***	7 10	5,000	5,000

Note: The Ledger Folio column indicates 7 against Cash Account which means that cash account is to be found on page 7 in the ledger and this debit of Rs.5, 000 to Cash Account can be seen on that page.

The Ledger Folio indicates 10 against X's Capital Account which means that 'X' Capital account is to be found on page 10 in the Ledger and this credit of Rs.5,000 to X's Capital Account can be seen on that page. (Students are advised not to mark or number anything in the L.F. Columns.)

We have already seen that Drawings are the withdrawals of money or money's worth. The proprietor is the receiver.

Example: 2

2003 Oct.1: Paid into Bank Rs.2, 000

(Or Opened a Current Account with Canara Bank Rs.(2,000))

Answer

DATE	PARTICULARS	L.F.	Dr.	Cr.
------	-------------	------	-----	-----

Debit Expenses A/c

Credit Cash A/c

Debit Expenses A/c

Credit Bank A/c

NOTES

2003 Oct.1	Bank A/c To Cash A/c (being the amount paid into Bank)	Dr.	2,000	2,000
---------------	--	-----	-------	-------

Example: 3

2003 Oct.1: Paid Yusuf Rs.200 on account by cheque

Answer:

DATE	PARTICULARS	L.F	Dr.	Cr.
2003 Oct.1	Yusuff's A/c To Bank A/c (being the amount paid to Yusuf by cheque)		200	200

Example: 4

2003 Oct.15: Receive letter from Yusuf saying that he has not received the cheque; cancelled the cheque and paid cash.

Answer:

DATE	PARTICULARS	L.F.	Dr.	Cr.
2003 Oct 15	Bank A/c To Yusuf's A/c. (being the cheque issued to Yusuf on 8 th Oct., now cancelled due to loss in transit)		200	200
	Yusuff's A/c To Cash A./c, (being the cash paid to Yusuff for cheque not received by him)		200	200

If you want to cancel the effect of an entry simply reverse the entry. Don't erase or cross out the original entry.

Example: 5

2003 Oct., 16: Received Rs.700 from Abdhul (or Abdhul paid us Rs.700)

Answer:

DATE	PARTICULARS	L.F.	Dr.	Cr.
2003 Oct.15	Cash A/c. Dr. To Abdhul's A/c. (being the amount received from Abdhul)		700	700

CREDIT CASH A/c under all these circumstances

If they acquired on credit basis: -

CREDIT THE PERSONAL A/c.

Example: 6

Oct. 17, 2003 bought goods for Cash from Mr.K.Kesavan Rs.600

Bought a Cycle for Rs.300

Bought Packing Materials for Rs.50.

Here goods are bought from Mr.K. Kesavan for cash. Therefore, the affected accounts are Purchases and Cash. Kesavan's A/c should not be credited for the goods he sent and has been paid for it. Here, the students must remember one point that in every transaction only two accounts will be affected; more than two accounts won't be affected.

Answer

DATE	PARTICULARS	L.F.	Dr. Rs.	Cr. Rs.
2003 Oct.15	Purchase A/c. Dr. To Cash A/c (Being the Cash Purchased)		600	600
	Cycle A/c. Dr. To Cash A/c (Being the cycle bought for cash)		300	300
	Packing Materials A/c. Dr. To Cash A/c (Being the packing materials bought for cash)		50	50

Example: 7

Oct., 18, 2003 Bought of Rajasekaran Rs.1000.

Answer:

DATE	PARTICULARS	L.F.	Dr.	Cr.
2003 Oct.15	Purchase A/c., Dr. To Rajasekaran A/c. (Being the goods bought from Rajasekaran on Credit)		1000	1000

A business always sells goods. When the asset becomes old they are sold.

Example: 8

2003 Oct.17, Sold goods for Cash Rs.1, 000

Sold old Machine for Cash Rs.700

Answer

DATE	PARTICULARS	L.F.	Dr. Rs.	Cr. Rs.
2003 Oct.19	Cash A/c Dr. To Sales A/c (Being the cash sales)		1000	1000
	Cash A/c. Dr. To Machine A/c. (Being the Machine sold for cash)		700	700

Example: 9

2003 Oct.20: Goods sold to Baby for Rs.500 or Baby bought goods from us.

Answer:

DATE	PARTICULARS	L.F	Dr. Rs.	Cr. Rs.
2003 Oct.20	Baby's A/c Dr. To Sales A/c (Being the goods sold to Baby on Credit)		500	500

Here, the name of the personal account is given. It is not clear whether it is a cash transaction or credit one. It is the convention to assume that such a transaction is a credit transaction.

NOTES

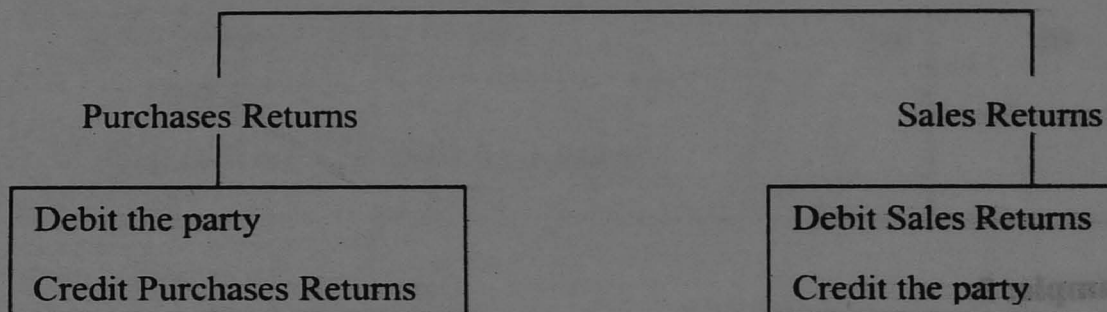
What are purchase returns?

When the goods are not up to the standard or defective the trader returns the goods to the suppliers from whom he had purchased. Such returns are known as Purchases Returns

When the goods are not up to the standard or defective the trader returns the goods to the suppliers from whom he had purchased. Such returns are known as Purchases Returns.

Similarly, the customers of the trader may return defective goods. This is known as Sales Returns.

RETURNS



Example: 10

2003 Oct.21: Returned goods worth of Rs.400 to Rajasekaran

Answer:

DATE	PARTICULARS	L.F.	Dr.	Cr.
			Rs.	Rs.
2003 Oct. 21	Rajasekaran A/c. Dr. To Purchases Returns A/c (Being the goods returned to Rajasekaran)		400	400

Example: 11

2003, Oct.22: Baby returned goods of Rs.50

Answer:

DATE	PARTICULARS	L.F	Dr. Rs.	Cr. Rs.
2003 Oct.22	Sales Returns A/c. Dr To Baby's A/c (Being the goods returned by Baby)		50	50

Compound Entry: When two or more transactions of the same nature take place on the same date, they can be entered in the Journal by means of a combined journal entry instead of making separate entry for each transaction. Such a combined Journal Entry is called Compound Entry.

Example: 12

2003, Oct. 21: Paid Rent Rs. 700

Paid Salary Rs.1, 300

Advertising Rs. 500

(The above three transactions are expenses on October 31, 2003.)

DATE	PARTICULARS	L.F.	Dr. Rs.	Cr. Rs.
2003 Oct.31	Rent A/c Dr. Salary A/c Dr. Advertising A/c Dr. To Cash A/c. (Being the rent, salary, advertising etc. paid)		700 1,300 500	2,500

Example: 13

2003: Nov. 1: Paid Rajasekaran Rs.580 in full Settlement of Rs.600

(i) Rajasekaran receives: Rs.580 goes out.

(ii) We are paying Rs.580 instead of Rs.600. There is a gain (i.e.,) Discount of Rs.20. As such Discount A/c. should be credited according to Rule No.3. Total debit of Rs.600 goes to Rajasekaran A.c,

Answer

DATE	PARTICULARS	L.F.	Dr. Rs.	Cr. Rs.
2003 Nov.1	Rajasekaran's A/c Dr. To Cash To Discount A/c (Being the amount paid to Rajasekaran in full settlement)		600	580 20

Example: 14

2003 Nov.7: Received Cash Rs.400 in full-settlement of Rs.450 from Baby.

(1. We have received Rs.400; cash comes in and Baby is a giver II Baby sends Rs.400 only instead of Rs.450. Discount A/c should be debited according Rule No.3 Credit of equal amount goes to Baby).

Answer

DATE	PARTICULARS	L.F.	Dr. Rs.	Cr. Rs.
2003 Nov.7	Cash A/c. Dr. Discount A/c. Dr. To Baby's A/c (Being the cash received from Baby in full settlement)		400 50	450

Example: 15

2003: Nov.10: Sales amounting to Rs.6, 000 have become unrealizable from Mohan and the debt is to be written off as bad debt.

[The amount is totally irrecoverable. It is a loss. According to Rule No.3, debit all Expenses and Losses. As such Bad Debt is a loss. So Bad Debts A/c should be debited. Credit automatically goes to Mohan]

Answer

DATE	PARTICULARS	L.F.	Dr. Rs.	Cr. Rs.
2003 Nov.10	Bad Debts A/c. Dr. To Mohan's A/c (Being the amount written off as bad debt)		6,000	6,000

Example: 16

2003 Nov.23: Raman becomes insolvent only

1. We received Rs.8, 000(i.e.) 50% out of Rs.16, 000-cash comes in and Mohan gives it. The balance of Rs.8,000 (16,000-8,000) represents bad debt. It should be written off. Bad Debt is a loss. Therefore, Bad Debts account should be debited. Credited automatically goes to Mohana.

Answer

DATE	PARTICULARS	L.F.	Dr. Rs.	Cr. Rs.
2003 Nov.10	Cash A/c. Dr. Bad Debts A/c Dr. To Raman's A/c (Being the amount received and the balance written off as bad debt)		8,000 8,000	16,000

OPENING JOURNAL ENTRY

After the first year of its working, a business will start new books of account. The entry to start, the new business is called Opening Entry. In the new set of books, all assets and liabilities of the previous period are recorded.

The rule is

Debit all Assets

Credit all Liabilities

Example: 17

Prepare on Opening Journal Entry On 1st January, 2003

Assets		Liabilities	
	Rs.		Rs.
Cash	300		
Bank	1,000		
Furniture	700	Amount owing to 'B'	2,000
Buildings	5,000		
Stock of goods	2,000		
Amount due from 'K'	1,000		

Answer:

Date	Particulars	L.F.	Dr. Rs.	Cr. Rs.
2003 Jan. 1	Cash A/c Dr.		300	
	Bank A/c Dr.		1,000	
	Furniture A/c Dr.		700	
	Buildings A/c Dr.		5,000	
	Stocks A/c Dr.		2,000	
	K's A/c Dr.		1,000	
	To B's A/c			2,000
	To Capital A/c			8,000

Example: 18**NOTES**

Raman commenced business with Cash Rs.1, 000, Bank Balance Rs.3, 000 Machinery Rs.10, 000 on 1.6.2003. Show the Journal Entry

Answer:

Date	Particulars	L.F.	Dr. Rs.	Cr. Rs.
2003 June 1	Cash A/c Dr. Bank A/c Dr. Machinery A/c Dr. To Raman's Capital A/c (Being the various asset invested in the business)		1,000 3,000 10,000	14,000

Illustration – 1

Journalize the following transactions:

2003 July.1: Edward started a business with

- (i) Cash Rs.13, 000
- (ii) Goods Worth Rs.10, 000
- (iii) Buildings Worth Rs.17, 000

2 Opened Current Account with Canara Bank Rs.10, 000

5 Bought of Kumar Rs.4, 000

6 Sales to R.G.Emporium Rs.5, 000

8 Bought a portable Typewriter for Rs.600

10 Purchased a bicycle for personal use for Rs.300 and paid by cheque

13 Two chairs bought at Rs.30 per chair

15 Received cheque from R.G.Emporium for Rs.2, 000

16 Paid R.G.Emporium's cheque into Bank

NOTES

18 Returned goods to kumar Rs.600

20 Stationery purchased Rs.10

25 Bought Neon Sign costing Rs.300

28 Issued a cheque to Kumar for Rs.3, 400 in full settlement of Rs.3, 500

30 One Chair stolen

31 Paid Rent Rs.100 in Cash

Salaries to clerk by cheque Rs.500

Insurance Premium Rs.300 by cheque.

Answer:

JOURNAL OF EDWARD\

Date	Particulars	L. F.	Dr.		Cr.	
			Rs.	P.	Rs.	P
2003	Cash A/c. Dr.		13,000	00		
July 1	Stock A/c. Dr.		10,000	00		
	Building A/c Dr.		17,000	00		
	To Capital A/c				40,000	00
	(Being the various assets brought into the business)					
2.	Canara Bank A/c. Dr.					
	To Cash A/c		10,000	00		
	(Being the amount paid into Bank)				10,000	00
	Purchases A/c. Dr.					
5.	To Kumar's A/c					
	(Being the credit purchases from Kumar)		4,000	00		
					4,000	00
	R.G.Emporium's A.c Dr.					
6.	To Sales A/c					
	(Being the credit sales to R.D. Emporium)		5,000	00		
					5,000	00
	Typewriter A/c Dr.					

8.	To Cash A/c (Being the portable typewriter brought for cash)		600	00		600	00
	Drawing A/c. Dr.						
10.	To Bank A/c. (Being the bicycle brought for personal use and paid by cheque)		300	00		300	00
	Cash A/c Dr.						
12.	To Commission A/c (Being the Commission received)		100	00		100	00

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2003	Furniture A/c. Dr.		60	00		
July	To Cash A/c				60	00
13	(Being the two chairs bought for Rs.30 each)					
	Cash A/c Dr.		2,000	00		
15	To R.G. Empirum's A/c (Being the cheque received from R.G.Emporium)				2,000	00
	Bank A/c Dr.		2,000	00		
16	To Cash A/c (Being the above cheque paid into Bank)				2,000	00
	Kumar's A/c Dr.		600	00		
18	To Purchase Return A/c (Being the goods returned to Kumar)				600	00
	Stationery A/c Dr.		10	00		
20	To Cash A/c (Being the stationery bought for cash)				10	00
			300	00	300	00

NOTES

25	Fixtures A/c	Dr.					
	To Cash A/c				3,500	00	
	(Being the Neon Sign bought for cash)						3,400 00
28	Kumar's A/c.	Dr.					100 00
	To Bank A/c						
	To Discount A/c						
	(Being the amount paid to Kumar in full settlement)				30	00	
30	Loss by Theft A/c	Dr.					30 00
	To Furniture A/c						
	(Being the loss of one chair)						

When a cheque is received, it will be treated as equivalent to cash. Hence Cash Account should be debited. When the same is deposited with bank, the bank will be receiver of it. As such, Bank, A/c. Should be debited. Yesterday, it was treated as cash. So, Cash goes out, Credit Cash A/c. However, if a cheque is deposited on the date of receipt itself, the above procedure is unnecessary. Here, Bank A/c will be debited and credit goes to the giver of the cheque.

The cost of chair is Rs.30. Refer transaction on 13th, it is a loss. According to Rule No.3 Debit at Expenses ad Losses Credit goes in Furniture.

31	Rent A/c.	Dr.			100	00	
	To Cash A/c.						100 00
	(Being the rent paid)						
2003	Salaries A/c	Dr.			500	00	
July 31	Insurance A/c.	Dr.			300	00	
	To Bank A/c						800 00
	(Being the salaries and insurance paid by cheque)						

MODEL QUESTIONS

1. What is book-keeping? What are its different forms? Bring out its advantages and drawbacks.
2. Differentiate Double Entry system from 'Single Entry System'.
3. What is Ledger? Differentiate it from Journal?
4. Journalize the following transactions:

2003 July:-

5. Mr. Ram Mohan started a business with:

(i) Cash Rs.15, 000

(ii) Goods worth Rs.15, 000

(iii) Buildings Rs.18, 000

6. Opened a bank account with Canara Bank with Rs.8, 000

7. Bought of Karikalan Rs.3, 000

8. Sales of M.K. Complex Rs.8, 000

9. Bought a Portable Typewriter for Rs.800

10. Purchased a Cycle for personal use Rs.800

11. College fees for Ram Mohan's son paid Rs.400

12. Tables bought for Rs.800

13. Received a cheque for Rs.4, 000 from M.K. Complex and deposited the same with bank.

14. Stationery purchased for Rs.800

15. Issued a cheque to Mr. Karikalan for Rs.2, 000

NOTES

16. Neon Sign bought for Rs.350
17. Stationeries worth Rs.500 stolen
18. Paid rent by cheque Rs.300 Paid Salaries Rs.100

LEDGER

Ledger is a book of accounts. Ledger contains accounts representing persons, properties and nominal items like expenses.

WHY SHOULD A LEDGER BE KEPT?

The journal records all the transactions separately and date wise. As such the Journal fails to bring together transactions of similar nature. Transactions relating to a person or property or expense gain are recorded in different places as they occur on different dates. Moreover the Journal simply dissects the given transaction as to which account is to be debited and which one to be credited without much bothering as to what is the 'final result'.

To get the picture as a whole, journals are further processed. All similar transactions relating to a particular account. (e.g. Cash A/c or Raman's a/c or Salary A/c) for a given period are brought together. In other words, they are recorded at one place in a ledger.

It is from Ledger that the businessmen can know the position of a person or property or particular item of gain or loss at any date.

It has already been pointed out in the previous lesson that a Journal is kept to facilitate the posting of entries in the Ledger.

Businessmen will be anxious to find out the profit or loss of the business and the financial position of his business. For this, he has to prepare Profit and Loss Account and Balance Sheet.

From the above discussion, one can clearly understand that there are 3 stages in the work of entering business transactions in books of accounts.

- | | | |
|-----------|---|--|
| I Stage | - | The Journal (or Subsidiary Books) |
| II Stage | - | The Ledger |
| III Stage | - | The Profit & Loss Account and the Balance Sheet. |

NOTES

What is Ledger?

Ledger is a book of accounts. Ledger contains accounts representing persons, properties and nominal items like expenses.

NOTES

Generally, the Ledger is a bound volume will pages numbered consecutively. In a big business house, 'Loose Leaf Ledger' may be used instead of a bound book. Under the Loose Leaf Ledger the pages are secured in a binder and locked with a key. Completed accounts or pages may be removed and additional pages or accounts may be inserted.

CLASSIFICATION OF LEDGER

Classification of Ledger:

Ledger may be classified as follows:

1. Creditors Ledger
2. Debtors Ledger
3. General Ledger

1. **CREDITOR'S LEDGER** : It contains the accounts of those persons from whom the goods are purchased on credit.
2. **DEBTOR'S LEDGER** : It contains the accounts of those persons to whom the goods are sold on credit.
3. **GENERAL LEDGER** : It records the transactions relating to Real and Nominal Accounts and certain personal accounts other than trade debtors and trade creditors.

.....Account

HOW POSTINGS ARE MADE

Let us proceed to learn how the posting are made in a ledger A/c.

Example: 1

Received Cash Rs.1, 000 from Jeyanthan (In this transaction, the receiving account is Cash A/c and Jeyanthan's account is the giving A/c. So the Journal entry is)

		Rs.	Rs.
Cash A/c	Dr.	1,000	
To Jeyanthan A/c			1,000

(Being the cash received from Jeyanthan)

The Journal entry indicates that the Cash A/c is to be debited and the account of Jeyanthan should be credited. The posting will be completed if we record on the debit side of the Cash A/c and on the credit side of Jeyanthan a/c in the Ledger.

First Step : Make out a list of accounts that you will have to open in the Ledger

Second Step : Open the account in the Ledger

Dr.	Cash Account	Cr.
	Rs.	
To Jeyanthan's A/c	1,000	
Dr.	Jeyanthan's Account	Cr.
	Rs.	
By Cash A/c	1,000	

Debiting an account means entering the transaction on the debit side (left-hand side) of that account.

'Crediting an account means entering the transaction on the credit side (right-hand side) of the account.

INSTRUCTION

1. Keep the Journal open your side
2. Read the entry, Cash A/c is debtor To Jeyanthan's A/c
(This implies Cash A/c should be debited and Jeyanthan's A/c credited.)
3. Take the cash a/c in the ledger; write down on the debit side like this
To Jeyanthan's A/c. 1,000
4. Jeyanthan's A/c is to be credited by Cash A/c. Take Jeyanthan's a/c go to the credit side (right-hand side) Post on top most line like this: By Cash A/c. 1, 000

MORE ABOUT ACCOUNTS

Each transaction involves; thus two entries (i.e., two accounts.....Cash account and Jeyanthan's account_ - e debit entry and a credit entry. In other words transaction affection two accounts in the opposite direction. In short, every debit must have a corresponding credit and vice versa.

A ledger entry shows two things:

1. Whether it is a debit or credit
2. The amount and the direction

Look at the ledger entry made in Cash account. It tells us.....

1. It is a debit and
2. The amount is Rs.1, 000 and the direction (viz) Jeyanthan...account.

From this one can derive the original Journal Entry. (Cash Account Dr. To Jeyanthan's Account 1,000)

Illustration: 1

Journalize the following transactions and prepare ledger accounts.

2003 May. 1: William started a business with the following assets:

1	Cash	Rs.2, 000
1	Furniture	Rs.1, 000 and
1	Stock of goods	Rs.3, 000
7	Sales to Rani Stores	Rs.2, 000
22	Received Rs.1, 900 from Rani Stores in full Settlement.	

Answer:

NOTES

JOURNAL OF WILLIAM

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2003 May 1	Cash A/c Dr. Furniture A/c Dr. Stock A/c Dr. To Capital A/c (Being the various assets brought into the business)		2,000	00		
			1,000	00		
			3,000	00		
					6,000	00
7	Rani Stores A/c Dr. To Sales A/c (Being the credit sales)		2,000	00		
					2,000	00
22	Cash A/c Dr. Discount A/c Dr. To Rani Stores A/c (Being the amount received in full settlement)		1,900	00		
			100	00		
					2,000	00

The Total of debts (Rs.2, 000 + 1,000 + 3,000 = Rs.6,000) is equal is to the credit i.e., 6,000. This satisfies the fundamental rule that for every debit there must be a corresponding credit of equal amount.

LEDGER OF WILLIAM

CASH A/c

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003 May 1	To Capital A/c		2,000	00					
22	To Rani Stores A/c		1,900	00					

FURNITURE A/C

Dr.

Cr

			Rs.	P.				Rs.	P.
2003									
May 1	To Capital A/c		1,000	00					

STOCK A/C

Dr.

Cr

			Rs.	P.				Rs.	P.
2003	To Capital A/c		3,000	00					
May 1									

CAPITAL A/C

Dr.

Cr

								Rs.	P.
					2003	By Sundries*		6,000	00
					May 1				

RANI STORES A/C

Dr.

Cr

			Rs.	P.				Rs.	P.
2003	To Sales A/c		2,000	00	2003	By Cash A/c		1,900	00
May					May	By Discount			
7					22	A/c		100	00

NOTE!

SALES A/CDr. Cr

			Rs.	P.				Rs.	P.
					2003 May 7	By Rami Stores A/c		2,000	00

DISCOUNT A/CDr. Cr

			Rs.	P.				Rs.	P.
2003 May 22	To Rami Stores A/c		100	00					

BALANCING LEDGER ACCOUNTS

At the end of every month (or any other period), all the accounts in a Ledger are balanced. An account is balanced by totaling each side and ascertaining the difference between the totals. The difference called "Balance" is entered on the lighter side of the account as Balance, "C/d". This balance is afterwards taken to the opposite side and entered therein as "Balance b/d".

1. Find out the total of the two sides in a separate sheet.
2. Incorporate the heavier total on the side obtained
3. Extend the same total on to the other side
4. Find out the difference between the two sides and place it on the lighter side writing the last date of the month on the date column
5. Bring down the balance on the heavier side of the account on the first of next month

NOTES

CASH ACCOUNT

Dr.

Cr.

		Rs.			Rs.
2003			2003		
Jan.1	To Capital A/c	4,000	Jan.3.	By Purchases A/c	1,000
Jan. 15	To Sales A/c	2,000	Jan. 31	By Rent A/c	300

I. Step: Find out the total of two sides in a separate sheet.

Debit Side = Rs.6, 000

Credit Side = Rs.1, 300

II. Step: Incorporate the heavier total on the side obtained

		Rs.			Rs.
2003			2003		
Jan.1	To Capital A/c	4,000	Jan.3.	By Purchases A/c	1,000
Jan. 15	To Sales A/c	2,000	Jan. 31	By Rent A/c	300
	(2)	6,000			

III. Step: Extend the same total on to the other side

		Rs.			Rs.
2003			2003		
Jan.1	To Capital A/c	4,000	Jan.3.	By Purchases A/c	1,000
Jan. 15	To Sales A/c	2,000	Jan. 31	By Rent A/c	300
	(2)	6,000		(3)	6,000

IV. Step: Find out the difference between the two sides and place it on the lighter side on the last date of the month.

2003		Rs.	2003		Rs.
Jan. 1	To Capital A/c	4,000	Jan. 3.	By Purchases A/c	1,000
Jan. 15	To Sales A/c	2,000	Jan. 31	By Rent A/c	300
				By Balance c/d (4)	4,700
		6,000			6,000

V. Step: Bring down the balance of the heavier side of the account on the first date of the next month.

CASH ACCOUNT

Dr.

Cr.

2003		Rs.	2003		Rs.
Jan. 1	To Capital A/c	4,000	Jan. 3	By Purchases A/c	1,000
Jan. 15	To Sales A/c	2,000	Jan. 31	By Rent A/c	300
			Jan. 31	By Balance c/d	4,700
		6,000			6,000
Feb. 1	To Balance b/d	4,700	(5)		

This Account shows a debit balance. The debit balance may indicate either an asset or an expense. Here, Cash represents an asset.

(2) (3) (4) & (5) indicate successive steps in balancing.

2003		Rs.	2003		Rs.
Feb. 1	To Sales A/c	1,000	Feb. 3	By Cash	1,000
Feb. 10	To Sales A/c	300	Feb. 30	By Cash	2,000

Example: 3**ISMAIL'S ACCOUNT**

Dr.

Cr.

2003		Rs.	2003		Rs.
Feb. 9	To Purchases		Feb.1	By Purchases A/c.	43,000
	Returns A/c.	2,000			
Feb.16	To Cash A/c	40,100	Feb.7	By Purchases A/c.	6,000
Feb 16	To Discount A/c	900			
Feb.28	To Balance c/d	6,000			
	(4)	49,000	2003	(2)	49,000
	(3)		Mar.1	By Balance b/d (5)	6,000

I Step: Involves that finding out the total of two sides in a separate sheet.

Note: This account shows a credit balance. Credit Balance will always indicate either:-

1. A Liability or

2. An income, Here, Ismail is a creditor (i.e.,) the business owes Ismail Rs.6, 000. In other words, the business has a liability to the extent of Rs.6, 000 towards Ismail.

Example: 4**JOHN'S ACCOUNT**

Dr.

Cr.

2003		Rs.	2003		Rs.
Feb 1	To Sales A/c	1,700	Feb.5	By Cash	1,000
Feb.10	To Sales A/c	300	Feb.26	A/c	1,000
		2,000		By Cash	2,000
				A/c	

Note: This account is closed and there is no balance. If both sides are equal, then there will be no balance.

NATURE OF LEDGER BALANCES

Debit Balance: If the total of the debit side of an account is more than the total of its credit side, the balance is said to be a debit balance.

A Debit.....

1. In a Personal a/c implies that money is due from him
2. In a Real a/c indicates the final balance of the asset
3. In a Nominal a/c., means that the money has been spent or lost.

Credit Balance: If the total of credit side of an account is more than the total of its debit side, the balance is said to be a credit balance.

A Credit.....

1. In a Personal a/c. implies that money is due to him
2. In the case off a Nomine a/c. implies that an income or a gain has been made.

SUMMARY OF LEDGER BALANCES

Under the Double Entry System, every debit must have a corresponding credit. Therefore, the total debits must be equal to total credits, if it is so, the debit balances total should be equal to the credit balances total. To test this arithmetical accuracy, a list can be prepared from the ledger balances. The debit balances are placed in the debit column and the credit balances are placed in the credit column. Such a list is known as 'Trial Balance'. This is prepared to test the arithmetical

Meaning of Trial Balance:

A balance of debits and credits in double-entry bookkeeping; drawn up to test their equality.

NOTES

accuracy of the entries in the books of account. If it does not tally, we can safely assume that there are errors in the books of accounts.

Steps 1 – relates to the totaling of the 2 sides of account in a separate sheet (2), (3), (4) & (5) indicate the successive steps.

Note: You need not write the same in your answer paper. Steps are written to emphasize the process.

PURCHASE A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003					2003				
June 15	To Bank A/c		1,000	00	June 30	By Balance c/d			
	To Raja's A/c		2,000	00		(4)		3,000	00
	(2)		3,000	00		(3)		3,000	00
July 1	To Balance b/d								
	(5)		3,000	00					

GUPTA'S A/C

NOTES

Dr.

Cr.

Date	Particulars	J F	Amount		Date	Particulars	J F	Amount	
			Rs.	P.				Rs.	P.
2003 June 8	To Sales A/c		800	00	2003 June 24	By Sales Return A/c		80	00
	(2)		800	00	June 30	By Balance c/d (4)		750	00
July 1	To Balance b/d (5)		750	00		(3)		800	00

SALES A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003 June 30	To Balance A/c (4)		2,300	00	2003 June 8	By Gupta A/c		800	00
	(3)		2,300	00		By Cash A/c (4)		1,500	00
								2,300	00
					July 1	By Balance b/d (5)		2,300	00

RAJU'S A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003					2003				
June 23	To Gupta's A/c		50	00	June 30	By Balance c/d			
	(2)		50	00		(4)		80	00
July 1	To Balance c/d		50	00		(3)		80	00

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PURCHASE RETURNS A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003					2003				
June 30	To Balance c/d		500	00	June 23	By Raja's A/c		500	00
	(4)					(2)			
	(3)		500	00	July 1	By Balance b/d		500	00
						(5)		500	00

SALES RETURNS A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003					2003				
June 24	To Gupta's A/c		50	00	June 30	By Balance		50	00
	(2)		50	00		(4)		50	00
July 1	To Balance b/d		50	00		(3)			

RENT A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003					2003				
June 24	To Cash A/c		200	00	June 30	By Balance c/d		200	00
	(2)		200	00		(4)		200	00
July 1	To Balance b/d(5)		200	00		(3)		200	00

SALARIES A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003					2003				
June 30	To Cash A/c		300	00	June 30	By Balance c/d(4)		300	00
	(2)		300	00		(3)		300	00
July 1	To Balance b/d (5)		300	00					

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003					2003				
June 30	To balance c/d (4)		75	00	June 30	By Cash A/c		75	00
	(3)					(2)		75	00
			75	00	July 1	By Balance b/d (5)		75	00

TRIAL BALANCE OF BABU

As on 30th June, 2003

SERIAL NO.	NAME OF THE ACCOUNT	Dr.		Cr.	
		Rs.	P.	Rs.	P.
1.	Cash A/c	8,075			
2.	Capital A/c			10,000	
3.	Bank A/c	2,000			
4.	Purchases A/c	3,000			
5.	Gupta's A/c	750			
6.	Sales A/c			2,300	
7.	Raja's A/c			1,500	
8.	Purchases Return A/c			500	
9.	Sales Returns A/c	60			
10.	Rent A/c	200			
11.	Salaries A/c	300			
12.	Commission A/c			75	
	Total	14,375		14,375	

Exercise

1. Journalize the following transaction and post them into appropriate ledger account and prepare Trial Balance as on 31st March 2003.

March 1 Daniel commenced his business with the following assets:

1. Cash	11,000
Plant and Machinery	20,000
Shares	2,000
Stock of goods	3,000

His transactions for the month were:

3. Sold goods to Janata stores	2,000
5. Bought from Excellent Traders	6,000
6. Janata Stores paid us cash	1,000
10. Returned goods to Excellent Traders	500
15. Paid Excellent Traders in full Settlement	5,400
18. Cash Sales	1,800
22. Received cash from Janata Stores	1,500
28. Salaries	1,000
31. Received dividend	30

SUBSIDIARY BOOKS

The Journal is the only book of original entry in which all transactions are entered before being posted to the Ledger. The bulk of the transactions in any business firm will be of purchases and sales of goods. Is it possible for a single clerk to journalize the whole of the business transactions? Even if a business firm employs a number of clerks, it is physically impossible for them to work simultaneously on one book (i.e., Journal). Therefore, it becomes necessary to divide or split up the old "Journal" into several journals or Subsidiary Books. "These Subsidiary Books or Special Journals occupy an important place in big business firms having numerous transactions. For them, the maintenance of one journal is a cumbersome and impracticable job.

To day, credit purchases and credit sales are considerable in number. If there was no credit facility, business could be carried out only in their most elementary form. The whole fabric of commerce rests on this.

The credit sales effected by a trader ordinary constitute the major part of his every day transactions. Example, if 4 credit sales were made to "W", "X", "Y" and "X" the rough journal entries would be.

DATE	PARTICULARS	L.F.	Dr.		Cr.	
			RS.	P.	Rs.	P.
	W's A/c Dr. To Sales A/c (Being the credit sales)		100	00	100	00
	X's A/c Dr. To Sales A/c. (Being the credit Sales)		200	00	200	00
	Y's A/c Dr. To Sales A/c		200	00	200	00

(Being the credit sales)					
Z's A/c	Dr.	400	00		
To Sales A/c				400	00
(Being the credit sales)					

Look at the entries. **Sales a/c is credited every time** in every Journal entry. Every time we repeat the same narration. But if a journal is kept specially for transactions relation to credit sales, we can avoid these repetitions (i.e.) unnecessary clerical work can be eliminated and record there in the four credit sales like this. It will take like.

SALES BOOK

		Rs.	P.
W		100	00
X		200	00
Y		300	00
Z		400	00
Total		1,000	00

To record four credit sales in Journal, 12 lines have been used, while writing the sales Book only 4 lines have been used. Thus, the unnecessary clerical work can be eliminated by entering the credit sales transaction in the Sale Book from which the individual debits' are posted to the respective personal accounts and the total of the credits + to the Sales Account, thus :

W's A/c

Dr.			Cr.
	Rs.		Rs.
To Sales A/c*	100.....1		
	X's A/c		
To Sales A/c	200.....1		
	Y's A/c		

What are sales?

Income (at invoice values) received for goods and services over some given period of time.

NOTES

To Sales A/c 300.....1

Z's A/c

To Sales A/c 400.....1 &

SALES A/C

1 By Sundries 1,000

DOUBLE ENTRY IS COMPLETED

All the four credit transactions of Sale of goods are recorded on the Sales Book. That is the giving of the benefit (of the goods) to different persons is entered. All such transactions are daily posted into the (ledger) debit of the different persons to whom the goods have been sold. Instead of crediting it as many times as there are transactions a total credit is given to the Sales Account. Even if we have 1,000 credit sales, we have to make only one entry in the Sales Account under this method. At the end of every month, the total value of all the sales is totaled up and this total amount is posted to the credit of Sales Account. In this way, double entry principle is follows: The double entry can be proved from the following Trial Balance:

TRIAL BALANCE OF

As on.....

	Dr. Rs.		Cr. Rs.
W's A/c	100		
X's A/c	200		
Y's A/c	300		
Z's A/c	400		
		Sales A/c	1,000
Total	1,000		1,000

The Journal is split into a number of Subsidiary Books each of which is kept for recording one particular class of transactions.

Thus,

1. all credit sales are entered in a	Sales Book
2. all credit purchases are entered in a	Purchases Book
3. all goods returned by the trader are entered in a	Purchases Returns Book
4. all goods returned by our customers are entered in a	Sales Returns Book

1. What about Cash Sales? It will be recorded in the Cash Book:

2. Similarly Cash Purchases will be recorded in the Cash Book. (i)

5. all cash transactions are entered in a	Cash Book,
6. all petty cash transactions are entered in a	Petty Cash book;
7. all bills received by the trader are entered in a	Bills Receivable Book'.
8. all bills accepted by the trader are entered in a	Bills Payable Book and
9. all other transactions are recorded in a	Journal Paper.

ADVANTAGES OF HAVING THESE SUBSIDIARY BOOKS

1. Nearly 50% of the clerical work can be eliminated.
2. Reference to any particular item is made easier
3. By division of work, one or more clerks work, independently in entering transactions in these Special Journals
4. It promotes not only efficiency of the work but also saves much time, labour and money.
5. Moreover, opportunities for committing of fraud will be reduced, since internal check is more effective.

NOTES

What is Trade Discount?

Trade discount means a discount from the list price of a commodity allowed by a manufacturer or wholesaler to a merchant.

TRADE DISCOUNT

Trade discount is the margin of profit allowed by manufacturers to wholesale dealers and wholesale dealers to retailer on making sales. It is a percentage allowed off the catalogue prices of goods supplied. As these price lists are often shown by retailers to prospective customers, the trade discount which forms part of the retailer's profit is not disclosed in the price list.

1. PURCHASES BOOK

This is a book of original entry. It is used to record credit purchases of goods. Two things are to be noted about this book.

(i) Cash Purchases are recorded in the Cash Book and

(ii) Credit Purchase of an asset is not recorded in the Purchases Book. It is passed through the Journal Proper.

RECORDING

It is not necessary to give the details contained in the invoice. It is enough if we record the day, month, year and the name of the person from whom the goods have been purchased on credit together with the net amount. Find out the total.

POSTING:

When goods are purchased on credit goods are coming into the business and the suppliers give the same. As such,

DEBIT:

The total at the end of the month to the purchases A/c in the ledger.

CREDIT:

Individually the persons from who the goods have been purchased with respective amount.

Illustration: 1**NOTES**

Enter the following transactions in the Purchases Book and post to the ledger.

Rs.

2003 Jan	1	Purchased Goods from Damodaran	2,000
"	10	Bought from Sankar	1,500 less 33 ½% T.D.
"	15	Excellent Co., Sold us goods	2,500
"	27	Bought goods from Ghouse	5,000 less 20% T.D.

PURCHASES BOOK

Date	Particulars	Inward Invo. Invoice No.	L. F.	Amount	
				Rs.	P.
2003					
Jan. 1	Damodaran	1		2,000	00
10	Sankar	2		1,000	00
15	Excellent Co.,	3		2,500	00
27	Ghouse	4		4,000	00
	Total			9,500	00

Purchases A/c

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003									
Jan.31	To Sundries		9500.00						

Damodaran's A/c

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
					2003				
					Jan.	By Purchases		2000.00	

NOTES

1. Invoice numbers are imaginary.
2. It means several persons.
3. The abbreviation 'A/c' need not be written here.

Sankar's A/c

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
					2003 Jan. 15	By Purchases		2,500.	00

Excellent Co's A/c

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
					2003 Jan. 15	By Purchases		2,500.	00

Ghouse's A/c

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
					2003 Jan. 27	By Purchases		4,000.	00

2. Sales Book

Sales Book is another subsidiary Book. This book is used to record credit sales of good. Two things are to be noted about this book:-

- (i) Cash Sales are recorded in the Cash Book, and
- (ii) Sale of any asset is not recorded in the Sales Book. It is passed through the Journal proper.

What is sales book?

Sales Book is another subsidiary Book. This book is used to record credit sales of good.

(iii) Therefore, only credit sales of goods will be recorded in the Sales Book.

RECORDING

Details contained in the invoice need not be given here, since it can be referred to the concerned invoice in the file. It is enough if we record the date, month, year and the name of the person to whom the goods have been sold on credit together with the net amount. Find out the total.

When goods are sold out, goods go out of the business and the customers and receivers of the same, As such,

Debit.....

Individually, the Personal accounts with individual amounts then and there without any delay

Credit.....

The total at the end of the month to the Sales A/c in the Ledger.

Illustration: 2

Record the following transactions in the Sales Book and Post to Ledger.

2003		Rs.
Feb. 1	Sold goods in Gaffoor	3,000
7	Muthu & Co bought goods from us	4,000
19	Sales to Koay & Co.,	2,600 less 10%TD
27	Goods sold to Premnath	1,400 less 20%TD
28	Sales to Muthu & Co.,	2,000

SALES BOOK

Date	Particulars	Out-ward Invoice E.No.	L.F.	Amount	
				Rs.	P.
2003					
Feb. 1	Gaffoor			3,000	00
7	Muthu & Co.,			4,000	00
19	Koya & Co.,			2,340	00
27	Premnath			1,120	00
28	Muthu & Co.,			2,000	00
	Total			12,460	00

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SALES A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003									
Feb 28	By Sundries		12,460.00						

GAFFOOR'S A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003									
Feb.1	To Sales		3,000.00						

MUTHU & CO., A/C

Dr.

Cr.

Date	Particulars	JF	Amount		Date	Particulars	JF	Amount	
			Rs.	P.				Rs.	P.
2003									
Feb 7	To Sales		4,000.00						
28	To Sales		2,000.00						

KOYA & CO'S A/C

Dr.

Cr.

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
			Rs. P.				Rs. P.
2003							
Feb.19	To Sales		2,340.00				

PREMNATH'S A/C

Dr.

Cr.

Date	Particulars	JF	Amount	Date	Particulars	JF	Amount
			Rs. P.				Rs. P.
2003							
Feb.27	To Sales		1,120.00				

Debit Note:

When goods are returned to the suppliers on account of damage in transit etc., a Debit Note is sent to them. It is so called because of the debit given to the concerned party's account. It is also sent to correct an error or omission in the invoice, since no new invoice will be issued.

PURCHASES RETURNS BOOK

This book is used to record the goods returned to the suppliers. A businessman may have to return the goods that he bought or credit as they may not be according to the sample shown or they may have been damaged in transit or for some other reason. It is a book of original entry.

RECORDING: Record the date, month, year and the name of the person to whom the goods have been returned together with the net amount. Find out the total.

POSTING: When goods are returned to our suppliers, goods are going out and suppliers are receivers of the same. As such

NOTES

What is debit note?

When goods are returned to the suppliers on account of damage in transit etc., a Debit Note is sent to them. It is so called because of the debit given to the concerned party's account.

NOTES

What is credit note?

A note issued to a person or company when goods are returned - this cancels the original invoice.

DEBIT.....individually the Personal account with individual amounts then and there without any delay.

CREDIT.....the total of the Purchases Returns Book to Purchases Returns A/c at the end of the month.

CREDIT NOTE

A note issued to a person or company when goods are returned - this cancels the original invoice

SALES RETURN BOOKS

Sometimes, some of our customers may find the goods supplied by us are defective or damaged. They may return such goods. The goods so returned are called Sales Returns and they are recorded in this book. On receipt of the goods. Credit Note is sent to the Party who has returned us goods.

RECORDING: Record the date, month, year and the name of the person who returned us goods together with the net amount. Find out the total.

POSTING: When goods are returned by our customers, they are the givers and the goods are coming in. As such,

DEBIT..... The Sales Returns A/c with the total of Sales Returns Book at the end of the month.

CREDIT..... individually the personal accounts with individual amounts then and there without any delay.

CASH BOOK

The Student has been previously told of the prevailing practice that most of the business transactions are carried on credit basis. All these credit transactions are going to be cash transactions one day or the other. Hardly a day passed without hundreds of items being received or paid by a business firm. A book may be used to record all these receipts and payments. Such a book is known as Cash Books.

As its name implies, it is a book where every such transaction is recorded. A Cash Book may be defined as the book in which are recorded all moneys received and paid. The person who is in charge of the Cash Book is known as cashier.

How do you record the receipt and payment of cash? On receipt, cash account is debited and on payment, cash account is credited. On this basis the Cash Book is ruled.

RECEIPTS

PAYMENTS

(a) Receipts on Personal Accounts

(a) Payments on Personal Accounts

(b) Receipts on Sales of Goods or Assets

(b) Payments on Purchase of goods or Assets

(c) Receipts for Income

(c) Payments on Expenses.

Note: There are modern business firms which keep altogether separate books for receipts and payments.

If properly kept, a cash Book will enable the business firm.

1. To know what has been its receipts and payments for a given period.
2. By deducting the payments from the receipts, to find out the Cash Balance on hand at any time without actually counting cash, and
3. To verify the correctness of Cash Book Balance.

There are several types of Cash Book. They are as follows:

1. 'Simple Cash Book with the column for Cash alone.
2. Double column Cash Book with columns for Cash and Discount.
3. Triple Column Cash Book with columns for Bank Cash and Discount.
4. Cash Book with Bank and Discount Columns.

NOTES

How to record in the Cash Book?

Ask yourself

Is it a receipt?

Or

Is it a payment?

If it is a receipt, go to the debit side (left hand side) of the Cash Book. Write the account involved with date and amount.

If it is a payment, go to the credit side (right hand side) of the Cash Book. Write the account involved with date and amount.

Then balance the cash Book just like an account.

Illustration: 1

1. SINGLE COLUMN CASH BOOK

Enter the following transactions in a Single Column Cash Book.

2003		Rs.
Sept. 1	Babu started a business with cash	5,000
2	He purchased goods for cash	2,000
4	Sold goods for cash and received a cheque for	700
7.	Paid for Stationery	10
10.	Received from Balu a Postal Order on account for	20
12	Paid for "Typewriter"	1,000
14	Paid Muthu by Money Order on account	50

Balance the Cash Book and bring down it on 15th September

CASH BOOK

NOTES

Dr.

Cr.

Date	Particulars	R. No.	L F	Amount		Date	Particulars	V, N o.	L F	Amount	
				Rs.	P.					Rs.	P.
2003	To Capital					2003	By Purchases				
Sep.1	A/c \$			5000	00	Sep.3	A/c. \$			2000	00
4	To Sales			700	00	7	By Stationery			10	00
10	To Balu			20	00	12	By Typewriter			1000	00
						14	By Muthu			90	00
							By Balance c/d			2660	00
				5720	00					5720	00
16	ToBalance b/d			2660	00						

Note: The debit side begins with the prefix "To" and the credit side with "By"

(Cash means actual coins, currency notes, cheques, postal order, Stamps etc.)

Hints:

Step 1 – It is a receipt, Go to the debit side and write the account involved with date and amount.

3 - It is a payment. Go to the credit side and write the account involved with date and amount.

4 - It is a receipt **7** – It is a payment **10**-It is a receipt **12**-It is a Payment **14**- It is a payment. Balance the Cash Book just like an account and bring down the same.

POSTING THE CASH BOOK:

- Receipts are entered on the debit side of the Cash Book and are subsequently posted to the credit side of the appropriate accounts in the Ledger.
- Payments are entered on the credit side of the Cash Book and are subsequently posted to the debit side of the appropriate accounts in the Ledger.

NOTES

Accounts credit in the Cash Book

Will need be debited in the Ledger

Accounts debited in the Cash Book

will need be credited in the Ledger

Purchase a/c

Stationery A/c

Typewriter A/c

Muth's A/c

Capital A/c

Sales A/c

Balu's A/c

DUAL PURPOSE OF THE CASH BOOK:

Unlike other subsidiary Books, the cash Book is both a Book of Original Entry (i.e.,) Journal and a Main Book (i.e.,) Ledger.

Journal: All cash transaction – receipts and payments are first entered in the Cash Book. Therefore, Cash Book is a Book of Original Entry Entries are then posted from Cash Book into Ledger.

Ledger: The ruling of the Cash Book is not similar to Purchases Book, Sales Book, Purchases Returns Book, and Sales Returns Book. The Cash Book is ruled just like an account. This Book is also divided into two sides as in an account, (i.e.,) one is debit side and other credit side. Hence, one can easily find out the Cash Balance by balancing it. Therefore, there is no need to open a Cash Account in the Ledger, it looks like an account and serves like an account.

Journal & Ledger: Cash Book is a Cash Journal and Cash Account. Cash Book thus is not only a Book of Original Entry; but also forms part of ledger.

DISCOUNT*

Trade Discount: The student has been previously told of prevailing practice in every trade to allow a Trade Discount overprices printed in price lists. Trade Discount is deducted from the invoice value as to arrive at the net amount that is payable; only the net amount is taken into account. This means, that the above discount is not at all recorded in the books of account

Cash Discount: It is also trade practice to sell goods on credit. To ensure payment within specified time, the seller offers a Cash Discount and is stated in the invoice. "Three present, one month". It means a discount of 3% will be allowed from the amount due if payment is made within one month from the date of the invoice. It means that a debt of Rs.1,000 can be discharged by paying only Rs.970. Cash discount received is a gain and Cash Discount allowed to customers is a loss.

DIFFERENCES BETWEEN CASH DISCOUNT AND TRADE DISCOUNT

CASH DISCOUNT	TRADE DISCOUNT
1. Discount deducted from the amount paid or received is called Cash Discount.	1. Discount deducted from the invoice price is called Trade Discount.
2. Cash Discount is allowed by the receiver of cash to the payer of cash.	2. Trade Discount is allowed by the manufacturer to the wholesaler and by the wholesaler to the retailers.
3. Cash Discount is an inducement to settle the debts promptly.	3. Trade Discount allows a firm margin of profit to the retailers.
4. Cash Discounts received are gains and Cash Discount allowed are losses. Therefore they are recorded in the books of account.	4. Trade Discount is allowed off the invoice price. As such, it is not recorded in the books of account.
5. To earn if a person has to settle his account within the period of credit. As such Cash Discount is conditional.	5. No such condition is prevailing here. As such Trade Discount is unconditional.
6. It depends upon the amount and period of credit.	6. It varies from the trade to trade and article to article.

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2. DOUBLE COLUMN CASH BOOK

Cash Discount accompanies cash receipts from customers and Payments to suppliers. Cash Discount, is thus, closely related to Cash receipts and payments. If we add Discount column in the Cash Book on each side, the resulting cash book is known as Double Column Cash Book.

NOTES

In the Cash Book, there is no separate Bank Column. Therefore transactions involving Bank must be recorded in a separate Bank Account which should be opened in the Ledger.

This book contains two columns –

Discount & Cash

The specimen ruling of a Double column Cash Book is given below:-

Cash Book (with Discount Columns)

Dr.

Cr.

Date	Particulars	R.No.	L.F.	Discount	Cash	Date	Particulars	V.No.	L.F.	Discount	Cash
				Rs.P.	Rs.P.					Rs. P.	Rs.P.
To						By					

Recording Steps: 1. is it receipt or payment?

(Receipt means, go to the debit side. Payment means go to the credit side)

2. Is Discount allowed or received?

Discount Allowed

Is a loss

Discount Received

is a gain

Discount Account

Is debited

Discount Account

is credited

3. TRIPLE COLUMNS CASH BOOK*

Most of the business firms make and receive payment in cash or by cheque and give or take discount. It column for 'Bank is provided on each side in the Cash

Book, it will be very useful. Such a Cash Book is known as Triple Column Cash Book.

CASH BOOK

With Cash, Bank & Discount Columns

Date	Particulars	R.No.	L.F.	Discount	Cash	Bank	Date	Particulars	V.No.	L.F.	Discount	Cash	Bank
				Rs.	Rs.	Rs.					Rs.	Rs.	Rs.
	To							By					

This book has got 3 amount columns:

1. Discount

2. Cash

3. Bank

This type of Cash Book contains 2 accounts [viz.,]:

1. Cash A/c – We need not open a separate Cash Account in the Ledger.

2. Bank a/c – We need not open a separate Bank Account in the Ledger.

But, we have to open a separate Discount Account in the Ledger, since, Discount columns in the Cash Book are only Memorandum Columns which permit the simultaneous posting to the individual personal accounts.

CONTRA ENTRIES ["C"]

1. If cash is deposited in the Bank, an entry will be made in Bank Column [Debit side] saying "To cash: it must also be entered in the Cash Column [Credit side] saying 'By Bank'".

2. If cash is withdrawn from the Bank for office use, an entry will be made in the Cash Column [Debit side] saying "To Bank"; it must also be entered in the Bank Column (Credit side) saying "By Cash"

NOTES

These are known as Contra Entries. In the L.F. column the letter "C" should be written to indicate that this is a contra entry. This means, that the double entry is completed in the Cash Book itself. No further posting is required.

1. Bank Drafts, Cheques, Postal Orders and Money Orders received should be treated as cash.
2. When a party directly pays into our Bank Account it is entered on the debit side in the Bank Column.
3. Cheques received and Deposited immediately into the Bank should be entered on the debit side in the Bank Column.

Explanation: 1: Paid into Bank Rs.1, 000

1. Bank is a receiver and
2. Cash goes out

Bank Account is to be debited and Cash Account is to be credited. Since, the Cash Book contains two accounts.

- (a) Cash A/c, and (b) Bank A/c. the debit and credit may be found in the two accounts. The debit is found in the Bank Account [Column] and the credit entry is found in the Cash Account [Column]. The debit and credit aspects are found in the opposite sides of the Cash Book.

Explanation : 2

With drawn Rs.700 from Bank for office use,

1. Cash comes in and
2. Bank is a giver

Both aspects can be found in the Cash Book – itself.

1. Cash Account should be debited and

2. Bank Account should be credited

3. Use Cash Column (Debit side)

4. Use Bank Column (Credit side)

The amount was entered in the cash column. What about the other account?

The other account involved is Bank. So write "To Bank".

4. CASH BOOK WITH BANK AND DISCOUNT COLUMNS ONLY

The development of banking and the extension of the use of cheques made unnecessary the use of cash for the settlement of all accounts. The common practice in big business firms is to bank all cash and cheques each day as received and to make all payments by cheque. For Small expenses like Postage, Carriage etc., are entered in a separate book by name Petty Cash Book.

PETTY CASH BOOK

Introduction: Most business firms follow the practice of paying the daily cash receipts into their bank account and of drawing cheques for all payments to be made. Except for money received at the office after banking hours, there will be no cash at office and even such moneys are paid into the bank next day morning.

Petty Cashier: A business firm has always got to make small payments like postage, Cargate, carriage, conveyance, printing and stationery, travelling expenses repairs etc. If the chief Cashier is given the work of making these small payments his position would become difficult. He is expected to make heavy and important payments. For the purpose of making these small payments another cashier/ (Petty Cashier) is therefore appointed.

Petty Cash: To meet petty expenses which are necessarily to be paid in cash, a small sum of cash has got to be maintained in the hands of the petty cashier. That portion of cash kept for meeting small expenses of recurring nature is known as Petty Cash.

What is petty cash?

Petty cash means a small fund of cash that a firm keeps for the payment of incidental expenses.

NOTES

Petty Cash Book: The book in which we record frequent petty payments of small amounts is known as Petty Cash Book.

The book has two sides (though unequal). It records the receipt of petty cash on the left hand side and payments on the right hand side. The right hand side is vertically divided into a number of columns (one for Postage, another for Carriage and so on for the purpose of analyzing petty expenses). A separate Column, "Ledger" is usually provided to accommodate payments relating to personal accounts. The infrequent items are grouped under "Sundry Expenses".

The Petty Cash book may be ruled as follows:

(Debit Petty Cash A/c for the receipt and posted	The totals of these columns are
Credit Bank A/c.	credit of the Petty Cash A/c and Debited to the concerned ledger Accounts)

The Imprest System: The best system of recording and maintaining the Petty Cash Book is known as the imprest System. By experience, the firm knows the average weekly (periodical) expenditure on petty expenses. In this system, a specified round sum is handed to the Petty Cashier in the first instance. During a given period the Petty Cashier goes on paying the petty expenses.

On the last working day of every week the totals the Petty Cash Book and presents it to the Chief Cashier for verification. The Chief Cashier verifies the Petty Cash Book with vouchers and gives the Petty Cashier a cheque for the exact amount spent. This amount together with the unspent balance will bring up to the amount with which the originally started (i.e.) the imprest sum.

(e.g.) Rs.100/- the estimated amount is given to the Petty Cashier for meeting small expenses in the business for a week. Suppose he had spent Rs.90/- during the week. This sum together with the unspent balance of Rs.10 will restore him the imprest (original) amount of Rs.100.

What is Imprest system?

The best system of recording and maintaining the Petty Cash Book is known as the imprest System.

Advantage:

1. It relieves the Cash Book and Chief Cashier with the burden of small Payments.
2. Opportunities for commission of fraud will be reduced because the Chief Cashier is expected to verify the Petty Cash Book with vouchers. This will make the Petty Cashier more responsible.
3. The total expenditure under each item can be easily ascertained and only the periodical total of column need be posted to the ledger.

Posting the Petty Cash Book

Open Petty Cash Account. It is credited on the last date of the month for the total amount spent 'By Sundries'

1. Open a separate Petty Cash Account in the Ledger. It is debited for the receipt of money. The corresponding credit goes to Bank.
2. The periodical total of each column in the Petty Cash Book is posted to the debit of the concerned ledger Account. The corresponding credit goes to Petty Cash account.

The Journal Entry on 31st Jan. 2003 will be as follows:

2. Open a Petty Cash Book with proper rulings
3. Enter the amount received in the first column with the words. "To Bank – Cheque received".
4. Enter the expenses 'By.....' & put the amount in the appropriate column as well as in the Total amount paid column.
5. Total up the analysis column & 'Total amount paid column'. See whether it tallies. Balance the book as usual and bring down the same.
6. An amount equal to the amount spent with recorded in the first column with the words "To Bank-cheque received".

1. Note: If postings are required, open the nominal accounts. Write the words 'To Petty Cash' on the debit side of each nominal account against its monthly total on the last of the month.

BILLS RECEIVABLE AND BILLS PAYABLE BOOKS

We find that some transactions are settled by cash, some by cheques and some by documents known as Bills of Exchange. When a trader draws Bills of Exchange for goods sold on credit, and accepts Bills of Exchange for goods purchased on credit, it becomes necessary to keep a record of them. To economise time, labor and stationery. Bills Receivable and Bills payable Books are used as Subsidiary Books.

The whole of trader's transactions in bills of exchange may be adequately recorded in the Journal and Ledger, but in practice this is done only in small business, and a trader whose dealings in bills are numerous makes the original entries in one of the two books, termed as the 'Bills Receivable Books' and the "Bills payable Book".

1. Bills Receivable Book:

It is used to record all the bills, pro-notes and hundies received by us on which we will receive money in future. They are entered in this Book as and when these bills are received and party's account it credited at once. Periodically this book is totaled up and the Bill Receivable A/c in the Ledger is debited with the total as "To Sundries". This book discloses the value of the bills received during the period and when a bill becomes due.

2. Bills Payable Book: It is used to record all the bills, pro-notes and hundies accepted by us on which we will pay money in future. They are entered in this Book as and when these bills are accepted and the party's account debited at once. Periodically, this book is totaled up and the bills Payable A/c in the Ledger is credited with the total as By Sundries. This book discloses the total value of the bills accepted by us and when we have to make payment.

When a bill is endorsed or dishonored, the transaction is passed through the Journal Paper.

JOURNAL PROPER

NOTES

Till now we have learnt 8 Subsidiary Books viz., purchase Book, Sales Book, Purchase Returns Book, Cash Book, Petty Cash Book, Bills Receivable Book and Bills Payable Book. There are certain transactions which cannot be recorded in any of the above Subsidiary Books. Such transactions are recorded through Journal Proper.

Originally all transactions were passed through the Journal. In modern Book-keeping, the use of the Journal has been restricted to the following types of transactions.

1. Transfer Entries
2. Adjustment Entries
3. Opening Entries
4. Rectification Entries
5. Closing Entries
6. Consignment Transactions

1. TRANSFER ENTRIES

Journal entries are passed for transferring amount from one account to another account. They are known as transfer entries.

Example 1

Pass the Transfer Entries to deal with the following:

- (A) Babu accepted to bear the debt of Rs.100 which was originally due from Balan
- (B) Transfer Rs.600/- from a debtor say, A's to B's A/c.

Transfer Entries:

		Rs.	Rs.
(A) Babu's A/c	Dr.	100	
	To Balan's A/c		100

[Being the amount transferred to Babu's A/c]

(B) B's A/c	Dr.	600	
	To A's A/c		600

[Being the amount transferred to B's A/c from A's a/c]

2. ADJUSTING ENTRIES

In the course of running the business some expenses may be paid in advance of the period of accounting while in some cases later also. To record such prepayments and post payments. Adjusting Entries are passed.

Example 2

Pass journal Entry for prepaid Insurance Rs.750.

Adjusting Entries:

		Rs.	Rs.
Prepaid Expenses A/c	Dr.	750	
	To Insurance A/c		750

[Being the prepaid insurance adjusted]

Example 3:

Interest at 4% on Government Bonds of Rs.20, 000 for the last quarter was not received.

$$\text{Rs.20,000} \times \frac{4}{100} \times \frac{3}{12} = \text{Rs.200}$$

100 12

Rs.200 is an Outstanding Income.

Adjusting Entry:

	Rs.	Rs.
Outstanding Debtors A/c	Dr. 200	
To Interest A/c		200
[Being the interest on Bonds for the last quarters adjusted]		

3. OPENING ENTRIES:

A trader started a business on 1.1.2002. He closed his accounts by 31.12.2002. At the beginning of the next period (1.1.2003) he has to bring into record all the Assets and Liabilities of the previous period (31.12.2002) in the new set of books. For this purpose journal entries are passed. These entries are called Opening Entries.

Dr. 2,000	Cash A/c
Dr. 4,000	Bank A/c
Dr. 1,500	Investment A/c
Dr. 2,500	Stock-in-Trade A/c
Dr. 8,000	Building A/c
Dr. 2,000	To Sundry creditors A/c
Dr. 1,500	To Bills Payable A/c
Dr. 2,500	To X's Loan A/c
Dr. 11,000	To Capital A/c

Example 4:

Ganesan's Balance Sheet on 31st December, 2002 was as under:

BALANCE SHEET OF GANESAN

As at 31st December, 2002

Liabilities			Assets		
	Rs	P.		Rs.	P.
Sundry Creditors	5,000	00	Cash on Hand	2,000	00
Bills Payable	1,500	00	Cash at Bank	4,000	00
X's Loan	2,500	00	Investments	3,500	00
Capital	11,000	00	Stock-in-Trade	2,500	00
			Buildings	8,000	00
	20,000	00		20,000	00

Pass the Opening Entry in his book on 1st January 2003

Opening Entry:

		Rs.	Rs.
1.1.2003	Cash A/c	Dr.	2,000
	Bank A/c	Dr.	4,000
	Investment A/c	Dr.	3,500
	Stock-in-Trade A/c	Dr.	2,500
	Building A/c	Dr.	8,000
	To Sundry creditors A/c		5,000
	To Bills Payable A/c		1,500
	To X's Loan A/c		2,500
	To Capital A/c		11,000

[Being the various assets and liabilities of the previous period brought into account]

4. RECTIFICATION OF ERRORS

When an entry was taken place in the books of accounts, the rectification of the error is not cancelled by banking that particular entry but by passing another journal entry. Such as entry is known as Rectification Entry.

Example 5:

Pass Rectification Entries for the following Errors.

(a) Rs.250 received from Ramu has been wrongly posted to Somu's A/c.

(b) Goods purchased from Balu for Rs.2,500 have not been passed through Purchases Book.

Rectification Entries:

S 214 v1

		Rs.	Rs.
(a) Some's A/c	Dr.	250	
To Ramu's A/c			250

[Being the entry to rectify wrong credit given to somu's a/c]

(b) Purchases A/c	Dr.	2,500	
To Balu's A/c			2,500

[Being the entry to record the purchases from Balu]

5. CLOSING ENTRIES

The preparation of the final account can be done only after transferring the balances of nominal account to the Trading and Profit and Loss Account. For this purpose, closing entries have to be passed in the Journal.

What is Rectification of Errors?

When an entry was taken place in the books of accounts, the rectification of the error is not cancelled by banking that particular entry but by passing another journal entry.

NOTES

Purchases and Sales Accounts are Real or Property Accounts so far as the goods they are concerned but they are Nominal Accounts in relation to the Profit and Loss arising from such concerns.

Example 6

Close the following accounts:

PURCHASES A/C

Dr.

Cr.

		Rs.	P.			Rs.	P.
2002	To Sundries	1,500	00				
Dec.31							

SALES A/C

Dr.

Cr.

		Rs.	P.			Rs.	P.
				2003	By Cash A/c	500	00
				Dec.31	By Sundries	12,000	00

WAGES A/C

Dr.

Cr.

		Rs.	P.			Rs.	P.
2002							
Dec.31	To Cash A/c	400	00				

RENT A/C

NOTES

NOTES

Dr.					Cr.		
		Rs.	P.		Rs.	P.	
2002	To Bank A/c	500	00				
Dec.31							

INTEREST A/C

Dr.					Cr.		
		Rs.	P.		Rs.	P.	
				2003			
				Dec.31	By Cash A/c	150	00

LEGAL FEES A/C

Dr.					Cr.		
		Rs.	P.		Rs.	P.	
2002	To Cash A/c	250	00				
Dec.31							

Closing Entries

		Rs.	Rs.
2002	Trading A.c		
Dec. 31	To Purchases A/c	1,500	
	[Being the entry to close the purchases A/c and to transfer it to Trading A/c]		1,500

NOTES

Dec. 31	Sales A/c To Trading A/c [Being the entry to close the Sales A/c and to transfer it to Trading A/c]	Dr. 12,500	12,500
Dec. 31	Trading A/c. To Wages [Being the entry to close the Wages A/c to transfer it to Trading A/c]	Dr. 400	400
Dec. 31	Profit & Loss A/c To Rent A/c [Being the entry to close the Rent A/c and to transfer it to P & L A/c]	Dr. 500	500
Dec. 31	Interest A/c To Profit & Loss A/c [Being the entry to close the interest A/c and to transfer it to P & L A/c]	Dr. 150	150
Dec.31	Profit & Loss A/c To Legal Fees A/c [Being the entry to close the Legal Fees A/c and to transfer it to P & L A/c]	Dr. 250	250

Ledger Accounts after Posting and Closing Entries:

PURCHASES A/C

Dr.				Cr.			
2002		Rs.	P.	2002		Rs.	P.
Dec.31	To Sundries	1,500	00	Dec.31	By Trading A/c	1,500	00
					Transfer		

SALES A/C

NOTES

Dr.

Cr.

		Rs.	P.			Rs.	P.
2002	To Trading A/c	12,500	00	2002	By Cash A/c	2,500	00
Dec.31				Dec.31	By Sundries	10,000	00
		12,500	00			12,500	00

WAGES A/C

Dr.

Cr.

		Rs.	P.			Rs.	P.
2002	To Cash A/c	400	00	2002	By Trading A/c	400	00
Dec.31				Dec.31	Transfer		
		400	00			400	00

RENT A/C

Dr.

Cr.

		Rs.	P.			Rs.	P.
2002	To Bank A/c	500	00	2002	By Profit & Loss		
Dec.31				Dec.31	A/c	500	00
		500	00			500	00

INTEREST A/C

Dr.				Cr.			
		Rs.	P.			Rs.	P.
2002	To Profit & Loss	150	00	2002	By Cash A/c	150	00
Dec.31				Dec.31			
		150	00			150	00

LEGAL FEES A/C

Dr.				Cr.			
		Rs.	P.			Rs.	P.
2002	To Cash A/c	250	00	2002	By Profit & Loss		
Dec.31				Dec.31	A/c Transfer	250	00

MODEL QUESTIONS

1. Explain the various types of Subsidiary Books and bring out its advantages.
2. Enter the following transactions in proper subsidiary books and post them to ledger.

2003

Jan 1	Goods bought from Govindan	5,000
4	Goods sold to Madhan	1,200
8	Kathiresan bought goods from us	3,000
12	Goods returned to Govindan	500
16	Goods received returned by Madhan	100
20	Ganesan bought goods from us	1,000
24	Goods purchased from Renga & Co.,	2,000
28	Goods returned to Renga & Co.,	250
31	Kathiresan returned goods	100

3. Write short notes on the following:

(a) Triple column cash book

(b) Petty Cash Book

4. What is Cash Discount?

Distinguish between Trade Discount and Cash Discount.

5. From the particulars given below Prepare a Three – Column Cash Book:

2003

NOTES

- Aug 1 Cash in hand, Rs.950 and bank, Rs.7,000
- 2 Received from Krishna Rs.990; discount allowed Rs.10
- 3 Deposited into Bank Rs.300
- 4 Bought goods for Rs.2,5000 and paid by cheque
- 5 Sold goods to Mohan on credit Rs.700
- 7 Received from Mohan on account Rs.700
- 8 Sold goods for cash Rs.700
- 9 Paid of Dhandu, Rs.980 by cheque; discount received Rs.20
- 10 Paid Salaries Rs.100
- 11 Remitted telephone bill, Rs.60
- 13 Bought goods for Cash Rs.400
- 17 Paid Cash to Kasturi Raman Rs.185, discount received Rs.15
- 21 Purchased goods for Rs.700 and paid by cheque
- 23 Sold goods for Rs.500 and recorded payment by cheque
- 25 Paid rent by cheque Rs.70
- 27 Received from Nagaraj Rs.590, in full settlement of his account for Rs.600
- 29 Deposited into bank, Rs.800
- 31 Paid for stationery Rs.15 .

6. Enter the following transactions in three column Cash Book

2003

Mar. 1	Cash balance	5,000
1	Cash at Bank	4,000
4	Furniture bought for Cash	1,000
8	Cash Sales	3,000
9	Cash paid into Bank	10,000

NOTES

11 Goods bought and paid by cheque	1,500
13 Goods sold to Kumar and received a cheque	700
15 Cheque received from Kumar on 13 th was paid into Bank And settled his account	
15 Raman who owes Rs.2,100 paid Rs.2,000 and settled his A/c	
15 Cheque received from Kumar on 13 th was paid into Bank	
17 Paid Gopal a cheque for rs.940 and settled his account Rs.1,000	
20 Withdraw from Bank for Office use	800
24 Madan directly paid into our bank account	3,000
29 Withdraw from bank for private use	1,000
28 A cheque received from Moorthy and paid into Bank Immediately	2,000
31 Paid salaries by cheque	1,000
31 Paid Telephone charges	300

NOTES

What is Trial balance?

A balance of debits and credits in double-entry bookkeeping; drawn up to test their equality.

TRIAL BALANCE

Perhaps, you know how to prepare ledger accounts from the Journal entries or other Subsidiary Books. We hope, you might have noticed how the two aspects of each business transaction are recorded while making entries in the books of accounts. That is, if one amount is debited to a given account, an equivalent amount is credited to another account for accounts that is affected by the transaction. Thus, the fundamental principle of Double Entry System of Book-keeping is that for every debit there must be a corresponding credit and vice versa of the equal amount.

You must have realized this fact yourself by now. Both the aspects of a transaction are recorded in the preparation of Journal as well as Ledger. This being so, it follows that the total of the debit amount column must be equal to the total of the credit amount column in the journal. If journal entries are correctly posted to different ledger accounts, the total of all debit postings in the Ledger must be equal to the total of all the credit postings in the Ledger. Also, instead of taking the totals of debit and credit entries in the Ledger, if we take the debit and credit balances only of all the accounts in the Ledger, the two totals must agree. This affords a way of checking the arithmetical accuracy of postings. To satisfy him a businessman always prepares a statement known as Trial Balance, after the ledger postings are completed. It can be prepared monthly or annually or at any other time, if so desired.

Definition

A Trial Balance is a list of debit and credit balances (including Cash & Bank) standing in the books of a concern on a particular date; the debits appearing on the debit column and credits in the credit column.

Objectives

There are two objectives for preparing a Trial Balance. They are as follows:

1. It provides a very good check on the accuracy of the work done in preparing ledger accounts. It brings us to the conclusion that some errors have been made in the books if the Trial Balance does not tally.

2. It facilitates the preparation of

- (i) Trading and Profit and Loss Account to find out whether the dealing have resulted in a profit or loss and
- (ii) Balance Sheet to ascertain the financial position of the business based upon assets and liabilities.

Construction

It is very easy to construct a Trial Balance on a given date. It is prepared on loose sheets of paper ruled similar to that of Journal.

A. Trial Balance can be constructed in two ways:

1. by means of TOTALS

2. by means of BALANCES

It must be pointed out that a Trial Balance is merely a statement prepared to check the arithmetical accuracy of the books up to the date stated at the head of the Trial Balance. It is not part of Journal or Ledger. It is not an account. It is only a list of statement. As such, no posting can ever be made to a Trial Balance

ERRORS

There is always the possibility of some mistakes being committed while writing up the books of accounts. Although a Trial Balance gives a prima facie evidence that the accounts are correct from the arithmetical point of view. It does not necessarily mean that the books of accounts are free from errors. Ie. Agreement of Trial Balance itself is not the conclusive proof that everything in the accounts is alright. For instance, instead of debiting Sharmila & Co., a debit is given to Nirmala & Co., the total of the debit column of the Trial Balance will still be the same. Such an error will not be discovered unless the entries are checked after being posted. Of course, it will be pointed out either by Sharmila & Co., or by Nirmala & Co., or by both, because the accounts as maintained by you will not agree with your accounts as

What are errors?

Errors are a misconception resulting from incorrect information.

NOTES

maintained by each of them. Therefore, Trial Balance should not be regarded as a conclusive and absolute proof of arithmetical accuracy.

A Trial Balance is not an Absolute Proof

Even if the two sides of a Trial Balance agree, there may remain more some errors undisclosed. It is clear that a Trial Balance fails to disclose certain types of errors. Why? Because the agreement of the Trial Balance will not be affected when certain types of errors are committed.

1. ERRORS NOT DISCLOSED BY A TRIAL BALANCE

The following are the errors which are not disclosed by a Trial Balance.

1. ERRORS OF OMISSION: These are the errors where the transactions have been altogether omitted (both aspects) from being entered in the books. Such errors do not affect the agreement of Trial Balance.

(e.g.) A credit purchase of goods from Baby has not been recorded in the Purchases Book. This means, Purchases Account is not debited and Baby's Account is not credited. As such, the two sides of the Trial Balance will show the same total.

2. ERRORS OF COMMISSION: These are the errors wherein the employees have committed some mistakes in making entries in the books. Such errors do not affect the agreement of the Trial Balance.

(e.g.) If a credit purchase of goods worth of Rs.700/- from Baby is entered in the Purchases Book as Rs.70/- the same figure of Rs.70/- will be posted to the credit of Baby's Account in the Ledger, thus reducing the Purchases Account and Baby's Account by Rs.630 (700-70). The Trial Balance will still agree.

(e.g.) If Nirmala & Co., Account is debited with a sale of Rs.300 instead of Sharmila & Co's Account to whom the sales has been made the Trial Balance will still agree and it will not disclose such errors.

Classification of errors:

1. Errors of principle
2. Errors of omission
3. Errors of commission
4. Compensating errors.

3. COMPENSATING ERRORS: These are the errors which cancel themselves out. That is, one error is compensated by the other error of opposite nature.

(e.g.) It Purchases and Sales Book are both overcast by Rs.100/- one error offsets the other and thus do not affect at the agreement of the Trial Balance.

4. ERRORS OF PRINCIPLE: These are the errors where transactions are not recorded according to the fundamental principles of book-keeping due to lack of knowledge. Such errors do not affect the Trial Balance.

(e.g.) If a purchase of a Typewriter is recorded on the debit side of Purchase Account instead of on the debit side of Typewriters Account the Trial Balance will not be affected.

(e.g.) Treating an asset as Purchase of goods.

Treating an asset as expense

Treating a liability as income

This does not mean that these errors can never be detected. They may come to light in a number of ways. An error of principle will be detected when the books are being audited. Or, a complaint from our supplier or customer may reveal the fact that he has been over charged or undercharged. Such errors are rectified either by making necessary adjustments or passing fresh entries and not by crossing or erasing the original entries.

H. ERRORS DISCLOSED BY A TRIAL BALANCE

The following are the errors which are disclosed by a Trial Balance.

1. POSTING OMITTED: If a credit sale to Rama Rs.100 is entered in the Sales A/c alone but not in Rama's account, the trial balance will disagree.

What is error of principle?

An error of principle is one where a transaction is recorded in total disregard to the fundamental principles of double entry, i.e., not as per the rule of debit and credit or in violation of some other principle.

NOTES

2. POSTING OF WRONG AMOUNT: (e.g.) If a credit sale of Rs.70/- is posted to customer's account alone as Rs.17/- the Trial Balance will disagree to the extent of Rs.53.

3. POSTING ON THE WRONG SIDE: (e.g.) If a credit sale of Rs.70/- is posted to the credit side of customers account, the Trial Balance will disagree to the extent of Rs.140.

4. TALLING OR CASTING MISTAKE: (e.g.) If the total of the Sales Book is under cast by Rs.70/- the Trial Balance will be short by Rs.70/-

5. OMISSION OF AN AMOUNT FROM THE TRIAL BALANCE (e.g.) If Cash Book balance is not brought into the Trial Balance. The Trial Balance will disagree.

6. REPEAT POSTING IN THE SAME ACCOUNT: (e.g.) If Rs.100/- paid by way of Salary is posted twice to Salary Account, the Trial Balance will disagree to the extent of Rs.100/-

TYPES OF ERRORS

Broadly speaking, errors can be classified into two types (viz.,)

1. Errors which do not affect the agreement of the Trial Balance.
2. Errors which affect the agreement of the Trial Balance.

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LOCATION THE ERRORS

Should the Trial Balance disagree, the following outline steps can be taken to discover the errors.

1. Add up both side of the Trial Balance
2. See whether any ledger balance like cash or Bank Balance is left out.
3. See no balance has been missed while extracting lists of debtors and creditors.

4. Check up where no debit balance has been entered in the credit column of the Trial Balance and vice-versa.
5. See any account shows the exact differences in the Trial Balance
6. Divide the actual difference by 2. See if half of the difference represents the balance of an account which has been recorded on the wrong side of the Trial Balance.
7. Totaling and balancing of all ledger balances should be re-done.
8. If the mistake remains unallocated, check up the total of all subsidiary Books and see whether they have been properly posted.
9. Compare the Trial Balance of the previous year and large differences if any be enquired into
10. If the mistake is still unallocated, posting of all accounts will have to be checked.

ERRORS AND THEIR RECTIFICATION

An error is not corrected by erasing the entry but by passing another entry. This new entry will counteract the effect of the error as also provides for a correct entry. The errors may be discovered either before or after closing the books.

SUSPENSE ACCOUNT

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If the Trial Balance is correctly extracted from the ledger and still does not agree, the difference in the Trial Balance may be placed in a suspense account. This will happen if the errors are not discovered before the Final Accounts are prepared. This will be shown on the Assets side of the Balance Sheet if it is a debit and on the liability side if it is credit. If a suspense account has been opened, the errors which normally require a single entry will then be effected by a double entry. As and when the errors are discovered and corrected, the suspense account will be automatically closed. As long as there is a balance on the suspense account there are still some errors not found.

What is suspense account?

An account used temporarily to carry doubtful receipts and disbursements or discrepancies pending their analysis and permanent classification.

NOTES

If the Trial Balance has agreed then there will be no need to open a suspense account. The errors subsequently discovered after the preparation of the agree Trial Balance will be corrected ordinarily.

The errors for purposes of correction may be divided into two. They are (a) One sides errors and (b) Double sides errors.

ONE SIDED ERRORS

An error may have been committed on only one side – debit or credit of an account. Such a one-sided error can be corrected by passing an additional entry on the debit or credit of the account as the case may be:

(e.g.) A credit sale Rs.80 to Mathew correctly record in the Sales Book but posted to the debit of Mathew at Rs.18.

No Journal Entry is required Debit Mathew with Rs.62 saying “To Mistake in position on.....”

@ Explanation: $\text{Rs.}80 - 18 = \text{Rs.}62$ being under – debited to Mathew. Hence he should be debited Rs.62

(e.g.) If however, the mistake is discovered after the preparation of Trial Balance and a Suspense Account has been opened, the correcting entry will be:

Answer:

	Rs.	Rs.
Mathew's A/c	Dr.	62
To Suspense A/c		62

[Being the rectifying entry to correct the under – debit in Mathew's A/c]

Explanation: Mathew's Account is to be debited with Rs.62. The journal entry will be completed by crediting Suspense Account with Rs.62.

2. DOUBLE – SIDES ERRORS:

Double sided errors affect two accounts – debit and credit, and will therefore be corrected by means of an ordinary journal entry (e.g.) A credit sale of goods worth Rs.100 to Sharmila & Co., is debited to Nirmala & Co., A/c.

Answer :

		Rs.	Rs.
Sharmila & Co's A/c	Dr.	100	
To Nirmala & Co's A/c			100

[Being the rectifying entry to correct the wrong debit]

Explanation :

It is obvious that the debit placed wrongly to the account of Nirmala & Co., should be transferred to the account of Sharmila & Co.. This Chapter on rectification of errors will present great difficulty to students. Before trying to solve the problems on rectification, the students should master the correct journal entries in double entry in respect of the types of business transactions.

1. For Cash received :		1. For Cash paid	
Cash A/c	Dr.	X's a/c	Dr.
To X's A/c		To Cash A/c	
2. For Cash Purchases :		2. For Credit Purchases:	
Purchases A/c	Dr.	Purchases A/c	Dr.
To Cash A/c		To X's A/c	
3. For Cash Sales		3. For Credit Sales :	
Cash A/c	Dr.	X's A/c	Dr.
To Sales A/c		To Sales A/c	
4. For Purchases Returns :		4. For Sales Returns :	
X's A/c	Dr.	Sales Returns A/c	Dr.
To Purchases Returns A/c		To X's A/c	

5. For Expenses Paid : [Rent etc] Rent A/c Dr. To Cash A/c 6. For Purchases of an asset say Typewriter on cash basis: Typewriter A/c Dr. To Cash A/c 7. For withdrawal of money for private use: Drawing A/c Dr. To Cash A/c 8. For discount allowed to X by us: Discount A/c Dr. To X's A/c	5. For Income received : [Dividend etc] Cash A/c Dr. To Dividend A/c 6. For Purchases of an assets say Typewriter on credit basis: Typewriter A/c Dr. To Halda & Co's A/c 7. For withdrawal of goods for Private use: Drawing A/c Dr. To Purchases A/c 8. For Discount allowed by 'X' (to us) X's A/c Dr. To Discount A/c
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Purchases = Debit Balance

Sales = Credit Balance

Debtor = Debit Balance

Creditor = Credit Balance

Sales Returns = Debit Balance

Purchase Returns = Credit Balance

Expenses = Debit Balance

Incomes = Credit Balance

HOW TO CORRECT ERRORS

ERRORS	SOLUTION
1. If an account is not debited	DEBIT that account
2. If an account is not credited	CREDIT that account
3. If an account is wrongly debited	CREDIT that account
4. If an account is wrongly credited	DEBIT that account
5. Excess (over)debit in an account	CREDIT that account
6. Excess (over) credit in an account	DEBIT that account
7. Short (under) debit in an account	DEBIT that account
8. Short (under) credit in an account	CREDIT that account

Example : 1

Rectify the following errors:

- (1) A Purchases of Rs.1,000 from Ravi was omitted to be entered in the Purchases Book.

(a) Explanation: Here the entire transaction is not recorded. Hence, the rectification involves journalising the above transaction.

Answer :

		Rs.	Rs.
Purchases A/c	Dr.	1,000	
	To Ravi's A/c		1,000

[Being the rectifying entry to record purchases from Ravi]

2. A credit sale of Rs.700 to Xavier was omitted to be entered in the Sales Book.

(a) Explanation: Hence the credit sales are not recorded. Hence journalize the above transaction.

Answer

		Rs.	Rs.
Xavier's A/c	Dr.	700	
	To Sales A/c		700

[Being the rectifying entry to record the sales to Xavier]

3. Goods returned to Mohan Rs.70 was not recorded in the Returns Outward Book.

(a) Explanation: This is Purchases Returns. The entire transaction is not recorded. Now record it by passing the usual entry.

Answer

		Rs.	Rs.
Mohan's A/c	Dr.	70	
	To Purchases Returns A/c		70

[Being the rectifying entry to record the purchases returns]

4. Received goods worth of Rs.50 returned by Eswaran not recorded in the book.

(a) **Explanation:** This is Sales Returns. The entire transaction is not recorded. So pass a journal entry.

Answer:

		Rs.	Rs.
Sales Returns A/c	Dr.	50	
	To Eswaran's A/c		50

[Being the rectifying entry to record the sales returns]

Example: 2

1. Rs.300/- received from Yesudoss was wrongly credited Jesudoss.

*Working steps	Answer :	Rs.
Rs.		
(A) Fact:Rs.300 received from Yesudoss	Jesudoss A/c	Dr. 300
(B) C.J.E.: Cash	To Yesudoss A/c	300
To Yesudoss		
(C) Error: Yesudoss A/c is wrongly credited (i.e) Yesudoss A/c is not credited	(Being the rectifying entry to Record the amount received From Yesudoss)	

(D) Solution : Credit Yesudoss To remove wrong credit in Jesudoss A/c., gave him a debit	
--	--

Example : 1 (1), (2), (3) & (4) are errors or omissions

CJE Correct Journal Entry.

2. Paid Kamaraj Rs.100 was wrongly debited to Ramaraj.

*Working steps	Answer	Rs.	Rs.
(A) Fact : Rs.100 paid Kamaraj	Kamaraj's A/c Dr.	100	
(B) C.J.E. : Kamaraj to Cash	To Ramaraj A/c		100
(C) Error : Ramaraj's A/c is debited (i.e.,) Kamaraj's A/c is not debited	[Being the rectifying entry to record]		
(D) Solution: Debit Kamaraj's A/c To remove wrong Debit in Ramaraj's A/c given him a credit			

Example: 2

(1) A purchase of Machinery from T.V.S. for Rs.10,000 was wrongly passed through Purchase Book.

*Working Steps	Answer:	Rs.	Rs.
(A) Fact : Purchase of Machinery	Machinery A/c Dr.	10,000	
(B) C.J.E.: Machinery to T.V.S.	To Purchase A/c		10,000
(C) Error: Entered in the Purchases Book (i.e.,) Machinery A/c is not Debited	[Being the rectifying entry to record The machinery purchases]		
(D) Solution : Debit Machinery A/c To remove the wrong debit to Purchases give a credit			

Example: 3 (1) and (2) are errors of commission

Correct Journal Entry – CJE

(2) Rs.100 received as commission from Babu was wrongly credited to Babu's A/c.

*Working Steps	Answer:	Rs.	Rs.
(A) Fact : Commission Received			
(B) C.J.E.: Cash to Commission	Babu's A/c Dr.	100	
(C) Error : Babu's A/c is credited (i.e.,) Commission A/c is not Credited	To Commission A.c		100
(D) Solution : Credit Commission A/c To remove the wrong credit in Babu's A/c given him a debit	[Being the rectifying entry to record The commission received]		

(3) Furniture costing Rs.600 purchased for the proprietor was wrongly posted to Furniture Account.

*Working steps	Answer	Rs.	Rs.
(A) Fact : Drawings			
(B) C.J.E. : Drawings to Cash	Drawings A/c Dr.	600	
(C) Error : Furniture A/c is debited (i.e.,) Drawings a/c is not debited	To Furniture A/c		600
(D) Solution : Debit Drawings A/c To remove the wrong debt in Furniture, credit it.	[Being the rectifying entry to record The purchase of furniture for the proprietor]		

(4) Repairs to Buildings Rs.300 have been debited to Building A/c

*Working Steps	Answer	Rs.	Rs.
(A) Fact : Repairs	Repairs A/c	Dr.	300
(B) C.J.E. : Repairs To cash	To Building A/c		300
(C) Error : Building A/c is debited (i.e.,) Repairs A/c is not debited	[Being the rectifying entry to Record the repairs to building]		
(D) Solution : Debit Repairs A/c To remove the wrong debit In Building A/c. give a credit			

Example: 4

1. A credit sale to Parameswaran Rs.170 was recorded in the books as Rs.117

*Working Steps	Answer	Rs.	Rs.
(A) Fact: Credit Sale to 'P' Rs.170			
(B) C.J.E. : Parameswaran Rs.170 To sales Rs.170	Parameswaran's A/c	Dr.	53
(C) Error : Recorded in the book as (i.e.,) Parameswaran 117 To Sales 117	To Sales A/c		53
(D) Solution : (170-117) Shortage Rs.53 Debit to Parameswaran Rs.53 Credit to sales	[Being the rectifying entry to correct The short debit and credit]		

Example : (1) (2) (3) & (4) are Errors of Principle

2. A credit sale to Raju Rs.117 was recorded in the book as Rs.170

*Working steps	Answer	Rs.	Rs.
(A) Fact : Credit Sale to Raju 117			
(B) C.J.E.: Raju 117 To Sales 117	Sales A/c		53
(C) Error : Raju 170 To Sales 170	To Raju's A/c		53
	[Being the rectifying entry to correct The debit & credit]		

(D) Solution : (117-170) -53 Excess Rs.53 is in Raju's A/c Excess Rs.53 is in Sales A/c To remove this excess, Debit Sales A/c Credit Raju's A/c	
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3. A credit sale of Rs.170 to Gopal was wrongly posted to Gopal's A/c as Rs.117

*Working Steps	Answer	Rs.	Rs.
(A) Fact : Credit Sale to Gopal Rs.170	No Journal entry is required – Debit		
(B) C.J.E. : Gopal Rs.170	Gopal's A/c with Rs.53.		
To Sales Rs.170			
(C) Error: Gopal's A/c alone Rs.117	Saying "To Mistake in position		
(i.e.,) There is no mistake in sales	on.....		
A/c. Hence only one account, namely			
Gopal's a/c alone is affected.			
(D) Solution: one-sided error. No			
Journal. (170-117)-Rs.53 shortage			

4. A credit sale of Rs.117 to 'M' was wrongly posted to 'M' Account as Rs.170

*Working Steps	Answer	Rs.	Rs.
(A) Fact : Credit Sale to 'M' Rs.117	No Journal Entry is required		
(B) C.J.E. : 'M' Rs.117	Credit 'M' A/c with Rs.53 saying		
To Sales Rs.117	"by mistake in posting on.....		
(C) Error: 'M' A/c alone Rs.170			
(i.e.,) There is no mistake in sales			
A/c Hence, only 'M' account is			
Affected.			
(D) Solution: One sided error (170-117)			

53 No Journal To remove this excess Debit, give him a credit	
---	--

Example : 5

A sale of goods to Radhs for Rs.100 has been entered in the Purchase Book:

*Working Steps	Answer	Rs.	Rs.
(A) Fact : Sales to Radha			
(B) C.J.E.: Radha To Sales	Radha's A/c	Dr. 200	
(C) Error : Entered as Purchases	To Sales A/c		100
(D) Soilution:	To Purchases A/c		100
(i) This is aburd. Cancel the same by Reversing the original entry [Purchase to Radha]	[Being the rectifying entry to record the sales]		
(ii) Sales not entered: That is it is Not recorded at all; record it by Journalising (i.e.,) it needs 2 Entries	5214 v1		

Example : 6

Rs. 300 received from Bala on 31.12.2002 but had been entered in the Cash Book on 3rd Jan. 2003

*Working steps	Answer	Rs.	Rs.
(A) Fact : Cash from Bala			
(B) C.J.E.: Cash to Bala	Cash A/c	Dr. 300	
	To Bala's A/c		300
(C) Error : Entered on 3.1.2003 (i.e.,) not entered on 31.12.2002	[Being the rectifying entry to record the amount received from Balu on 31.12.2002 entered by mistake on 3.1.2003]		
(D) Solution: Pass the correct entry Rectify the one sided mistake			

In Cash Book (3.1.2003)	The Cash Book on 3.1.2003 will be Rectified by Bablu's a/c on the credit side.
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Illustration : 1

Correct the following errors without opening a Suspense Account.

- (a) Rs.75 paid for proprietor medial bill was debited to Sundry Expenses.
- (b) A credit purchase of goods from Ismail for Rs.700 was not recorded in the books, but the payment made subsequently stands debited to an account opened in his name.
- (c) A credit sale to Ramesh of Rs.533 was posted to his account as Rs.355
- (d) The total of Purchases Book was short by Rs.100
- (e) Sales book carried forward Rs.54 instead of Rs.45
- (f) Duplicator purchased from Stationery company for rs.5,000 on credit was passed through the Purchases Book.
- g) Rent paid to the Landlord Mr.Dayanand, Rs.300 was debited to his personal account.
- (h) Rs.200 received from A.V.K. was credited to the account of K.V.A.

Answer:

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DATE	PARTICULARS	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
(a)	Drawing A/c Dr. To Sundry Expenses A/c [Being the rectifying entry to record the amount Of proprietor's medical bill]		75	00	75	00
(b)	Purchases A/c Dr. To Ismail's A/c [Being the credit purchases from Ismail now Recorded]		700	00	700	00
(c)	No Journal Debit Ramesh's a/c with Rs.198 [533-335] Saying "To Mistake in position on....."					
(d)	No Journal Debit Purchase a/c with Rs.100 Saying "To Mistake in Totalling on...."					
(e)	No Journal Debit Sales A/c Rs.9 [54- 45] Saying "To Mistake in position on....."					
(f)	Duplicator A.c Dr. To Purchases A/c [Being the rectifying entry to record the Purchase of duplicator]		5000	00	5000	00
(g)	Rent A/c Dr. To Dayanand's A/c [Being the rectifying entry to record the rent paid]		300	00	300	00

(h)			200	00	200	00
	K.V.A's A/c. Dr. To A.V.K's A/c [Being the rectifying entry to record the amount received from A.V.K.]					

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Illustration : 2

A book keeper while balancing his books finds that he is out of excess debit by Rs.549/

Being required to prepare the final accounts, he places the difference in newly opened Suspense account which he carries forward to the next period. Subsequently, the following mistakes were discovered.

- The Purchase Book for December was under cost by Rs.70.
- A purchase of Rs.354 from Wilson was correctly entered in the Purchase Book but it was credited to Wilson's account at Rs.435.
- Rs.700 spends for erecting a new shed had been charged to Wages Account.
- A Purchase of Rs.300 from Jogi was debited to his account.
- Sundry items of plant sold amounting to Rs.930 had been entered in the Sales Account.
- The returns inward Book was overcast by Rs.100

Draft the, Journal entries necessary for rectifying the above mistakes. Prepare the Suspense Account.

Answer:

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NOTES

DATE	PARTICULARS	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
(a)	Purchase a/c Dr. To Suspense A/c [Being the rectifying entry to correct the short debit]		70	00	70	00
(b)	Wilson's A/c Dr. To Suspense A/c [Being the rectifying entry to correct the excess credit]		81	00	81	00
(c)	Building's a/c Dr. To Wages A/c [Being the erection charges wrongly debited to wages now rectified]		700	00	700	00
(d)	Suspense A/c Dr. To Jogi's A/c [Being the rectifying entry to correct the wrong debit and to record the correct credit]		600	00	600	00
(e)	Sales A/c Dr. To Plant A/c [Being the rectifying entry to record the plant sold]		930	00	930	00
(f)	Suspense A/c Dr. To Sales Returns A/c [Being the rectifying entry to correct the excess debit]		100	00	100	00

NOTES

SUSPENSE A/C

Dr.

Cr.

	Rs.		Rs.
[4] To Jogi's A/c	600	By Difference in Trial Balance	549 [1]
[5] To Sales Returns A/c	100	By Purchase A/c	7 [2]
		By Wilson's A/c	81 [3]
[6]	700	[6]	700

PROFIT & LOSS ADJUSTMENT ACCOUNT

What is profit and loss account?

An account compiled at the end of an accounting period to show gross and net profit or loss.

All debits and credits in respect of Purchases, Sales, Purchases, Returns, Sales Returns and all expenses and incomes for errors committed in the previous trading period should be passed through this account. In other words, use, Profit & Loss Adjustment Account instead of using the Nominal accounts mentioned above.

(e.g.) Usual Rectifying Entries

Changed into

Purchase A/c	Dr.	P&L Adjustment A/c	Dr.
To Suspense A/c		To Suspense A/c	
Wilson's A/c	Dr.	No Change	Dr.
To Suspense A/c			
Building A/c	Dr.	Building a/c	Dr.
To Wages A/c		To P&L Adjustment A/c	
Sales A/c	Dr.	P & L Adjustment A/c	Dr.
To Plant A/c		To Suspense A/c	
Discount A/c	Dr.	P & L Adjustment A/c	Dr.
To Suspense A/c		To Suspense A/c	
Suspense A/c	Dr.	Suspense A/c	Dr.
To Sales A/c		To P&L Adjustment A/c	

LESSON – 2

NOTES

Final Account and Balance Sheet

In the preceding lessons, we have seen how the business transactions are recorded in the journal (Subsidiary Books) and then in the concerned ledger account. As already state, the Trial Balance is extracted from the balances of ledger accounts to test the arithmetical accuracy of books of accounts. If there is any error in the books of account, they need proper rectification. But the matter does not end there.

We have mentioned that the primary aim of Book Keeping is to enable the businessmen to know clearly whether the business is progressing and to know the exact financial position of the business. Moreover, every business man is anxious to know how the business has fared during the period just over. As such the business man is interested in finding out two important facts.

1. The profit earned or loss incurred by him during a given period (usually a year)
2. The financial position of the business based upon assets and liabilities on a given date.

To ascertain this, the businessman has to prepare certain accounts and statements.

To find out the profit or loss, he prepares an Account known as Trading and Profit and Loss Account.

To find out the exact financial position of the business, he prepares a statement known as Balance Sheet.

Sheet:

The preparation of Trading and Profit and Loss Account and Balance Sheet is known as the preparation of Final Accounts. The term Final Account is the general

What is profit?

Profit means excess of revenues over outlays in a given period of time (including depreciation and other non-cash expenses).

and collective name give for the Trading and Profit and Loss Account and the Balance Sheet. This lesson is concerned with the basic concepts of Final Account.

Procedure:

It is the Trial Balance that is the basis for the final account. The Trial Balance contains both debit and credit balances of all ledger accounts.

The debit balances of a Trial Balance represent either.

Assets or Losses or Expenses

If the debit balance of any account is realizable, it is an asset otherwise it is a loss. Items such as Cash, Bank Balance, Investments, Bills Receivable Sundry Debtors, Stock of Goods, Lands, Buildings, Plant and Machinery, Furniture and Fitting etc., all are realizable. Items of expenditure paid and incurred such as Carriage, Wages, Salaries, Rent etc., are all not realizable.

The credit balances of a Trial Balance represent either:

All assets appear on the Balance Sheet

All losses and expenses are transferred to the Trading and Profit and Loss

Account liabilities gains or Incomes

If the credit balance of any account represents amount payable it is a liability. If it is not, it is a gain items such as Bank Overdraft, Sundry Creditors, Bills Payable, Loans etc., are all payable by the business (i.e.,) these are all liabilities of the business. Items of income like Dividend, Commission, Discount, interest etc., are gain.

All liabilities appear on the Balance Sheet

All gain are transferred to the Trading and Profit and Loss Account

Revenue account:

Profits and losses are shown in the Profit and Loss Account or Revenue Account. 'Revenue Account' generally means an account where the profit or loss is determined. The name of the 'Revenue Account' for an organisation varies according to the nature of business.

Following is a table of different names of Revenue Accounts of different organisations:

Nature of the Business	Name given to the Revenue Account
1. A Trading concern	1. Trading and Profit and Loss Account.
2. A Manufacturing concern	2. Manufacturing account (in addition to the Trading and Profit and Loss Account)
3. A Banking Company	3. Profit and Loss Account
4. An Insurance Company	4. Revenue Account
5. Social Clubs, Colleges, Schools, Hospital, Cultural Societies and Non Profit making institutions.	5. Income and Expenditure Account
6. Professional concerns of Lawyers, Accountants, Engineers and Doctors.	6. Income and Expenditure Account

Let us now take up for study the Revenue Account of trading concern and the name to be given to the Revenue Account is Trading and Profit and Loss Account. That is, the Revenue Account of a trading concern is divided into 2 Sections.....

1. The first section is known as Trading Account; and

2. The second section is known as Profit and Loss Account

TRADING ACCOUNT

This account is constructed for the purpose of finding out the profitability of trading transactions of an organization (i.e., goods" bought and sold by the business man). The difference between the 'Selling Price' and the 'Cost Price' of the goods is

the 'gross earning' of the businessmen. Such 'gross earning' is known as 'Gross Profit'. When the cost of buying goods is more than the selling price there is a 'Gross Loss'.

In order to find out gross profit, a Trading Account is opened and all the accounts relating to goods such as Opening Stock, Purchases, Purchase Returns and Sales Returns are transferred to it.

- | | | |
|----------------------|---|---|
| 1. Opening stock A/c | - | Shows balance of goods in hand in the beginning of the period |
| 2. Purchase A/c | - | Shows total purchases made |
| 3. Sales A/c | - | Shows total sales made |
| 4. Purchases Returns | - | Shows the value of goods returned to suppliers. |
| 5. Sales Returns A/c | - | Shows the value of goods returned by customers. |

The Trading Account, will, thus be opened and all these accounts of a given period are closed by transferring them to the Trading Account.

COST OF GOODS SOLD

Candidates should note the difference between "cost of goods sold" with that of "cost of goods" purchased. "For example, if 5 pens are purchased for Rs.10 each and out of them only 3 pens are sold, then the cost of goods purchased is $5 \times \text{Rs.}10 = \text{Rs.}50$ but the cost of goods sold is $3 \times \text{Rs.}10 = \text{Rs.}30$. From this, we can understand that in order to calculate the cost of goods sold we must deduct from the total cost of goods purchased, the cost of goods in hand. Thus by deducting Rs.20 from Rs.50 which are cost of goods in hand and cost of goods purchased respectively, we can say, the cost of goods sold is Rs.30.

If there is already a stock of goods in hand (i.e. opening stock) at the beginning of the year, then the cost of goods sold is calculated with an example as under

	Rs.
Stock in hand at the commencement of the year (say)	5,000
Purchase made during the year (say)	70,000
Total stock available for sale	<u>75,000</u>
Bless: Stock in hand at the close of the year (say)	10,000
Cost of goods sold	<u>Rs. 65,000</u>

It include all the expenses of bringing the goods in saleable condition and to the place of business premises (say expense such as insurance, cartage, freight, duly etc.,)

Thus, the terms 'cost of goods' includes the 'purchase price as well as the 'buying and bringing' expenses which are of a direct nature.

The Trading Account contains on the debit side items like opening stock of goods, purchases of goods, purchases returns, manufacturing expense and all buying and bringing expenses and on the credit side items like sales, sales returns and closing stock of goods. Of course, these items will be related to a particular period and their account will be closed and transferred to trading account by means of closing entires. The difference between the two sides of this account represents both a gross profit and gross loss. The gross profit or the gross earning may be expressed in the following equations.

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Gross Profit = [Sales less sales returns + Closing Stock] less

[Opening Stock + Purchases less Purchases returns + Purchase expenses]

Or Gross Profit = Sales – Cost of goods sold

Or Gross Profit + Cost of goods sold = Sales

Alternatively we can say

Credit side Total – Debit side Total = Gross Profit

Debit side Total – Credit side Total = Gross Loss

CONSTRUCTION OF A TRADING ACCOUNT

We have learnt that Trading Account is prepared to calculate the gross profit earned or gross loss incurred by the business for a given period. Therefore, a trading account is opened and all the aforesaid accounts pertaining to a given period and closed by transferring them to the Trading Account. Any unsold stock at the end is valued and it is compared with the market price. The lower value, of the two is brought into Trading Account by passing the following adjustment entry.

Closing Stock A/c Dr.

To Trading A/c

[Being the closing Stock brought into account]

If the trader fails to take account the value of the closing stock then what he arrives in the form of gross profit or gross loss will be a false figure. Similarly as a prudent account only anticipated loss is taken into account and not the anticipated profit. That is the reason why, the cost or market price of the stock, whichever lower, is taken into account.

Further, as the business operations continue from the next accounting date, the books of accounts have to be opened with the opening balances of different account. One among these accounts is the stock account and it is nothing but the closing stock of the previous period. Thus, the closing stock of one year of period becomes the "opening stock" of the next accounting period. At the end of the accounting period, the balance of this stock account is transferred to the Trading Account by passing the following closing entry.

Trading Account Dr.

To Stock Account

[Being the transfer of the stock account]

Usual items debited to a Trading Account are:

1. Opening Stock
2. Purchases less Returns Outwards
3. Direct expenses, which may be divided into
 - (a) Purchase expenses
 - (b) Manufacturing expenses

Purchase expenses comprise of (i) Carriage or carriage inwards (ii) Freight on Purchases, freight inwards and Landings charges (iii) Exercise Duty (iv) Import Duty and Custom Duties etc., (v) Dock charges (vi) Dock Charges (vii) Clearing Charges.

(b) Manufacturing expenses comprise of

- (i) Wages productive wages, workshop wages, manufacturing wages, wages and salaries, foreman and supervisor salary.
- (ii) Factory Expenses, Factory Rent, Factory Insurance, Factory Lighting, Factory maintenance and cleaning, all Factory and Work shop expenses.
- (iii) Fuel, Fuel and Power, Motive Power and Heating, Coal, Coke Gas, Wood, Oil, Water, Grease, Candies, Timber, Rope, Powder, Cotton Waste, Soft Soap etc.,
- (iv) Royalties if it is on the purchases or produced goods and Trade expenses when it is accompanied by office expenses. Usual items credited to a Trading account are:

Thus, while constructing a Trading Account. "Closing entries are passed to close and to incorporate in trading account the following:

- (a) Stock Account (i.e., opening stock)
- (b) Goods Accounts viz., (i) Purchases Account (ii) Sales Account (iii) Returns Inwards Account (iv) Returns Outwards Account.
- (c) Nominal Accounts connected with purchases expenses and
- (d) Nominal accounts connected with manufacturing expenses

- (e) Adjustment entries are passed to incorporate closing stock as well as to adjust the balance of accounts appearing in the Trading Account.

TRADING ACCOUNT OF A MANUFACTURER

Trading Account of a manufacture is divided into 2 sections viz., Manufacturing and Trading. This is due to the fact that a purchases finished or ready goods for resale whereas a manufacturer buys raw materials, produces certain articles finished products by incurring certain expenses and then sells them. Therefore, in order to find out the cost of manufacture or to ascertain the profit earned by the manufacturing department, it is prepared in two sections viz., Manufacturing Account and Trading Account.

The manufacturing account is debited with (a) opening stock of raw materials (b) work in progress or semi-finished goods (c) purchase of raw materials less returns, if any (d) all manufacturing and factory expenses and (e) depreciation of Plant and Machinery. Tools, Building and repairs to these assets. Again this account is credited with (a) Closing stock of raw materials. (b) work in progress at the end and (c) sale of waste and scrap. The difference between the two side of the Manufacturing Account represents the cost of goods manufactured and is transferred to the debit of the Trading Account.

The Trading Account is debited with the opening stock of the finished goods and the cost of goods produced and it is credited with the sales less returns and closing stock of finished goods. The gross profit or gross loss shown by the Trading Account is transferred to the Profit and Loss Account. Thus, the Manufacturing Account shows the result of the manufacturing department and the Trading Account reveals the result of the trading department.

The Trading Account will appear as follows:

BASKARA & BROS

Trading Account

For the year ending 31st December, 2002

Dr.

Cr.

	Rs.	Rs.		Rs.	Rs.
To Opening Stock			By Sales		
To Purchases			Less:	S.	
Less P. Returns			Returns		
To (a)			By Closing Stock		
To (b)					
To Gross Profit c/d					
(Transferred to Profit & Loss A/c.)					

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(a) Manufacturing Expenses (Wages Factory, Expenses, Power, Fuel etc.,)

(b) Buying, Bringing Expenses etc., (Carriage, Freight, Dock Charges & Duties like Excise, Octroi, Import).

Example .1

Prepare a Trading Account of Aryabhata for the year ending 30th June 2003 by using the following information.,

	Rs.
Opening Stock	70,000
Purchases Returns	15,000
Sales	2,50,000
Wages	60,000
Sales Returns	1,00,000
Purchases	17,000

NOTES

1. Closing Stock was valued at Rs.60, 000.

Adjustment Entry

		Rs.	Rs.
1. Closing Stock A/c	Dr.	60,000	
To Trading A/c			60,000

[Being the closing stock brought into account]

ARYABHATA

TRADING ACCOUNT

For the year ending 30th June, 2003

	Rs.	Rs		Rs.	Rs.
To Opening Stock		70,000	By Sales	2,50,000	
To Purchase	1,00,000		Less: S .Returns	20,000	
Less: P.Returns	15,000	85,000			2,30,000
To Wages		60,000	By Closing		60,000
To Carriage		17,000	Stock		
To Gross Profit c/d					
(transferred to Profit					
&		58,000			
Loss A/c		2,90,000			2,90,000

ADVANTAGES OF PREPARING A TRADING ACCOUNT

The advantages derived from the Trading Account are as follows:

1. It shows the Gross Profit or Gross Loss made after buying and selling of Goods.
2. It helps us in finding the ratio of gross profit to the turnover so that the selling price can be fixed.
3. It helps us to find out the ratio of gross profit to the direct expenses so that unnecessary expenses can be avoided.
4. It helps us to compare purchases, sales, returns etc., of the current year with those of the previous year.
5. That goes profit found out through this account acts as a basis for fixing the prices of goods over future period.

PROFIT AND LOSS ACCOUNT

The Profit and Loss Account is the second part of the Revenue Account and is prepared in order to find out whether there is a net profit or net loss for a given period of the business. Of course, the trader has to incur a number of expenses apart from those spent for purchase and manufacturing of goods. Those expenses which are necessary for running of the business just like administrative or management expenses, selling expenses, distributive expenses, etc., are debited to this account. In addition, depreciation, provision, etc., are also charged to this amount. These expenses which are relevant to the period under consideration are deducted from Gross Profit and then the net profit or the net loss is arrived at.

In other words, the expenses which are not debited to the Trading Account are debited to the Profit and Loss Account. Similarly, any income besides gross profit is also transferred to the credit of the Profit and Loss Account. But one fundamental principle to note here is that only the expenses and income for the trading period under consideration are taken to the Profit and Loss Account. Generally, an expenses would have been incurred but not yet been paid for, should be treated as a liability for

NOTES

the unpaid amount and accounted for before the profit or loss for the period is arrived at.

For example, usually the salary for a particular a month is paid on the first of next month. If the accounts are being closed on 31st December, then the salary, which is not paid during December, must be taken into account in order to show a true picture of the Revenue Account.

The construction of Profit and Loss Account is similar to Trading Account. Since the Profit and Loss Account is prepared to show the net profit or net loss during a particular period, it is headed as follows:

NAME OF THE BUSINESS **PROFIT AND LOSS ACCOUNT**

For the Period/ year ended.....

Date. , month and year

Usual items that appear in the Profit and Loss Account are:

On the debit side

(For easy remembrance they are classified as under)

(i) Administrative Expenses:

Office Salaries

Rent

Postage and telegrams

Printing and Stationery

Insurance

Repairs and renewals

Telephone

(ii) Selling expenses:

Salesmen's Salaries

Selling Commission

travelling expenses

Brokerage, Advertisement

Discount allowed

Bad debts

Free samples

Bank charges

Bank Commission

Lighting (except factory)

Interest, Interest on capital

Audit Fees

Legal Fees

Accountancy Fee

(ii) Distribution expenses

Warehouse, Rent, Expense

Insurance etc.,

Carriage outwards

Packing expenses

Delivery van expenses

Trade Expenses or Trading Expenses

(iv) Depreciation, Provisions, Reserves etc.

Depreciation of various assets,

Provision for Bad and Doubtful debts

Provision for Discount on Debtors

Provision for Repairs and Renewals

Provision for other expenses

On the credit side:

Commission received

Rent received

Discount received

Interest or income from investment

Special bonuses received from suppliers

Amount previously written off recovered

Profit on Sale of assets

Provision for Discount on creditors.

Preparation of the Profit and Loss Account

The Trading Account is closed by transferring the Gross Profit or Loss to the Profit and Loss Account and thereby the Profit and Loss Account is opened. The closing entry incorporated for affecting such a transfer as follows:

Trading A/c Dr. When there is a Gross Profit

To Profit and Loss A/c

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Or

Profit and Loss A/c Dr. When there is a Gross Loss

To Trading A/c

By doing so, the Gross Profit is transferred to the credit side of the Profit and Loss Account. In case of Gross Loss it is placed to its debit side. Then the Profit and Loss Account is debited with all indirect expenses. For these necessary closing entries are passed to close all indirect expense accounts (Nominal accounts). Again, the Profit and Loss Account is credited with miscellaneous gains and incomes and thus the respective nominal accounts are closed by passing closing entries after debiting at the indirect expenses to the Profit and Loss Account and crediting all the miscellaneous incomes to the Profit and Loss Account. The result of this account is arrived at. If the debit side total is smaller than the total of the credit side, the difference represents net profit, on the other hand, if the credit side total of the Profit and Loss Account is smaller than the debit side total, then it is net loss. The net profit or net loss, whatever it may be, is transferred to the capital or current account and thereby the Profit and Loss Account is closed. The closing entry to transfer the net profit or net loss to capital or current account runs as follows:

Profit and Loss A/c Dr.

To Capital or Current A/c

when there is Net Profit

Capital (or current) A/c Dr.

When there is Net Loss

To Profit and Loss A/c

In a Trial Balance we find a number of accounts showing expenses and a few showing gains. Some of the manufacturing, buying and bringing expenses have already been transferred to the Trading Account. The remaining accounts showing expenses are closed by transferring their balances to the debit side of the Profit & Loss Account. The accounts showing gains are closed by transferring their balances to the credit side of the Profit & Loss Account.

When all expenses, losses, gains and incomes have been transferred to the Profit and Loss Account, this account discloses 'Net Profit' or 'Net Loss'

Credit side total – Debit side total = Net profit

Debit side total – Credit side total = Net Loss

This balance (N.P. or N.L.) will be transferred to the Capital Account (i.e., the account of the proprietor)

The Profit and Loss Account will appear as follows:

PROFIT & LOSS ACCOUNT

For the year ending.....

Dr.

Cr.

	Rs.	Rs.		Rs.	Rs.
To +			By Gross Profit b/d		
To			(transferred from		
To			Trading		
To Net Profit			Account)		
(transferred to Capital			By		
Account)					

Differences between Trading Account and Profit and Loss Account

Trading Account	Profit and Loss Account
1. The first section of the revenue account is known as Trading Account	The second section of the revenue account is known as the Profit and Loss Account.
2. The object of Trading Account is to ascertain the Gross Profit or Gross Loss by comparing the cost price with the selling price of the goods.	The object of this section is to ascertain the Net Profit or Net Loss by taking into consideration all profits and losses.
3. The account deals with items that make up cost and selling price of goods together with opening and closing stock (e.g.) Purchases, Direct charges on Purchases and direct expenses like wages, power and other factory expenses.	This account deals with the establishment of Administrative Expenses, Selling expenses and Distributive expenses. Whereas non-trading organizations prepare an equivalent of this account called income and expenditure account.
4. Non-trading organizations do not prepare this account.	

Example: 2

Complete a Trading and Profit and Loss Account of Rohini for the year ending 31st March 2003

	Rs.		Rs.
T Stock on hand [1.4.2002]	15,000	P Carriage out	4,000
T Purchases	1,65,000	T Factory Wages	10,000
T Returns outward	10,000	T Returns Inwards	5,000
P Postage and Telephone	300	P Salaries	5,000
P Commission received	500	P Printing and Stationery	1,000
P Bad debts	100	P Interest Paid	800
T Sales	3,00,000	P Insurance	500

Adjustment: Closing Stock was valued at Rs.80, 000

Adjustment Entry

Ans:

		Rs.	Rs.
1. Closing Stock A/c	Dr.	80,000	
	To Trading A/c		80,000

[Being the Closing Stock brought into account]

Items marked as 'T' should go to the Trading Account and marked as 'P' should go to the Profit and Loss A/c.

ROHINI

TRADING AND PROFIT AND LOSS ACCOUNT

For the year ending 31st March, 2003.

Dr. Cr.

	Rs.	Rs.		Rs.	Rs.
To Opening Stock		15,000	By Sales	3,00,00	
To Purchases	1,65,000		Less Returns	0	
To Less Returns Outwards	10,000	1,55,000	Inward		
		10,000			
To Factory Wages				5,000	2,95,000
GROSS PROFIT			By Closing Stock		80,000
transferred to Profit					
Loss A/c		1,95,000			
		3,75,000			
To Salaries		5,000			
To Postage and		300			3,75,000

NOTES

Telephones		100			
To Bad Debts		4,000	By GROSS		
To Carriage out		1,000	PROFIT		
To Printing and Stationery		800	Transferred from		1,95,000
To Interest Paid		400	Trading A/c		
To Insurance			By Commission		500
NET PROFIT transferred		1,83,900	received		
to					
Capital A/c		1,95,000			1,95,000

What is Balance sheet?

Balance sheet is a record of the financial situation of an institution on a particular date by listing its assets and the claims against those assets.

BALANCE SHEET

Balance Sheet is a simple statement prepared at regular intervals with a view to measure or shows the correct financial position of a business enterprise as on a particular date. It reveals what a business owns and what it owes. As such, this statement contains the properties and assets owned as well as the liabilities owed by the business on a particular day. In other words, it is nothing but a consolidation of all the unclosed ledger balances of 'real and "Personal:" accounts. The ledger balances of assets and properties extracted from the book will be just equal to the capital and liabilities of the business as on a particular day. This is due to the fact that either, the asset and properties are fully owned by the trader or financed by some one else. This is the reason why, the total value of the assets is always equal to the total value of capital and liabilities and the Balance Sheet too always balances. In an equation, it can be explained as under:

$$\text{Assets} = \text{Liabilities} + \text{Capital}$$

WHAT A BALANCE SHEET TELLS US?

I give us information about:

- (1) The nature and value of assets.
- (2) The nature and extend the liabilities
- (3) The businessman is solvent
- (4) The business is sound.

Controversy:

A balance sheet has two sides.

The Left hand side is Liability side

The right hand side is Assets Side.

In the Ledger the debit balances [Assets] appear on the left hand side, and the credit balances [Liabilities] appear on the right hand side. But in the Balance Sheet, the sides are reversed. The more correct form is used in Scotland and U.S.A. assets on the left and the liabilities on the right.

The Balance Sheet is prepared at a certain date (i.e.,) at a certain point of time. It is true only on its date. It would not have been true on the previous day and if will not be true on the next day. This is due to the fact that even a single transaction will change assets and liabilities. For example, when we pay off our creditors on 1.1.2003 the cash balance will be less. Similarly if we sell goods on 1.1.2003 for cash, this will increase the cash balance and reduce the stock of goods.

2. The two sides of the Balance Sheet must agree. Otherwise there is definitely something wrong.

Example: 3

A started a business on 1.1.2003 with Rs.10, 000 Balance Sheet will be changed 2.1.2003 it will look like.

BALANCE SHEET

As at 1st January, 2003

Liabilities		Assets	
Capital	Rs. 10,000	Cash	Rs. 10,000
	10,000		10,000

Example: 4

On 2.1.2003 'A' buys Furniture for Cash Rs.3, 000. Balance Sheet will be changed like this.

A

BALANCE SHEET

As at 2nd January 2003

Liabilities		Assets	
Capital	Rs.		Rs.
	10,000	Cash	7,000
		Furniture	3,000
	10,000		10,000

Example: 5

When 'A' borrows Rs.2, 000 from his friend 'B' on 3.1.2003 the Balance Sheet will exhibit the following details:

A

BALANCE SHEET

As at 3rd January 2003

Liabilities		Assets	
Loan from 'B' Capital	Rs.		Rs.
	2,000	Cash	9,000
	10,000	Furniture	3,000
	12,000		12,000

ORDER OF STATING ASSETS & LIABILITIES

Which items should come first? Which should follow? What is the reason for any particular order?

Different methods are in vogue Business. By one method, the assets are arranged in the order of reliability, that is, in the order in which they can be converted into

cash. By another method, the assets are arranged in the order of permanence that is, in the order of desire to keep them in use.

Order or reliability		Order of Performance
Cash in Hand	A	Fixed Assets
Cash in Bank	S	Prepaid Expenses
Investments	S	Closing Stock
Bill Receivable	S	Sundry Debtors
Sundry Debtors	E	Bills Receivable
Closing Stock	T	Investments
Prepaid Expenses	T	Cash – in – Bank
Fixed Assets Etc.,	S	Cash – in – hand

Sole Proprietorship, Partnership, Bank
Etc., adopt this method for showing their
Assets on a Balance Sheet

Joint Stock Companies use this method
of exhibiting their assets on Balance
Sheet

Similarly, Liabilities can be grouped in 2 ways (viz.,) in the order of urgency of payment or in the reverse order.

ORDER OF URGENCY OF PAYMENT

Outstanding Creditors

Sundry Creditors

Bills Payable

Loan

Income Received in Advance

Reserves

Capital

In the assets are arranged in the order of reliability, liabilities should be arranged in the order of urgency of payment and if the assets are arranged in the order of permanence, liabilities should be arranged in the reverse order.

NOTES

Note: The student should carefully study the method of dating the Trading and Profit and Loss Account and Balance Sheet. Being summary of transactions, the Trading and Profit and Loss Account is prepared for a period and the heading should be

.....
TRADING AND PROFIT AND LOSS ACCOUNT

For the year ending.....

But the Balance Sheet is not prepared for a period. As such the heading should be

**DIFFERENCES BETWEEN TRADING AND PROFIT AND LOSS ACCOUNT
 AND A BALANCE SHEET**

TRADING AND PROFIT AND LOSS ACCOUNT	BALANCE SHEET
1. It is a nominal Account	1. It is a statement of assets and liabilities.
2. The preparation of this account common to the principles of double entry, closing Journal books are required for the preparation of this account.	2. Journal entries are not required for the preparation of the Balance Sheet. It has no debit or credit side. It is a mere statement of assets and liabilities prepared after the closure of the nominal accounts like Trading and Profit and Loss Account.
3. All the revenue items are transferred to this Account.	3. All the capital items representing Assets and Liabilities are grouped in the statement in a classified form
4. This account shows the Gross Profit and Net Profit and Net Loss.	4. This statement shows Assets and Liabilities
5. This Account is usually prepared for a particular period (usually one year)	5. Balance Sheet is prepared on a particular date.

The Balance Sheet has two sides, viz., one is referred as the right hand side and the other is the left hand side but it cannot be compared with a ledger account as it is only a summary of the ledger balances of real and personal account. Hence, Dr. or Cr. And To or By are not used in the Balance. The right hand side is referred as "Properties and Assets" side in which the debit balances of real and personal accounts remaining in the order to ledger are written down either in the order of liquidity or in the permanence. The left hand side is referred as Capital and Liabilities side in which the credit balances of the personal accounts remaining in the ledger are recorded. The order of arranging the liabilities will be corresponding to the order of the asset side.

A specimen Balance Sheet on an ordinary business concern is given below on the principles of "liquidity" for better understanding of the items appearing therein.

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Balance Sheet as at

CAPITAL & LIABILITIES	AMOUNT	PROPERTIES & ASSETS	AMOUNT
Current Liabilities:	Rs.	Current Assets:	Rs.
Outstanding expenses		Cash in hand	
Income Received in advance		Cash at Bank	
Bills Receivable			
Bank Overdraft		Sundry Debtors:	
Sundry Creditors		Income due but not yet received	
Bill Payable		Prepaid Expenses	
		Closing Stock	
Fixed Liabilities :		(Finished Goods partly	
(Long Term Loans)		Finished, Raw Materials	
Bank Loan		Stationery Goods sent on	
Loan on Mortgage		Consignment etc.,	
Loan from Partner		Fixed Assets:	
		Goodwill	
		Land and Buildings	
		Plant and Machinery	
		Tools	
		Furniture and Fixtures	
		Vehicles	
		Patents & Patterns	

NOTES

Liabilities to Owner:		Trade Mark	
Capital Account		Fictitious Assets:	
Current Account		Preliminary Expenses	
		Advertising Expenses	
		Underwriting	
		Commission	
		Other expenses not	
		written off.	

What are assets?

Assets are the properties, possessions and belongings of every description belonging to the trader.

Assets are the properties, possessions and belongings of every description belonging to the trader. They are of various types. They are classified according to their nature as fixed assets liquid assets, intangible assets and fictitious assets. Assets may be classified as follows:

Tangible assets are those which can be seen and touched (e.g.) Building, Machinery, Furniture, etc.,

Intangible assets are those assets which have not material existence (e.g.,) Goodwill, Prepaid Expenses etc.

Tangible assets may again be divided into Fixed Assets and Floating Assets. By Fixed Assets, we mean those assets which are acquired and held permanently in the business and not for resale. (i.e.,) Plant and Machinery. Floating Assets are those which are acquired in the course of the business and held temporarily in the business and are intended for the purpose of resale (e.g.,) Stock – in trade, Floating assets otherwise known as Circulating Assets.

The nature of the business distinguishes the Fixed and Floating Assets. Machinery may be fixed assets to an ordinary dealer, but it is a floating asset to a machinery manufacturer.

Assets which are represented by cash or those which can be easily converted into cash such as Government Bonds. Bill Receivable etc. are called Liquid Assets.

Assets which are consumed through being worked or get exhausted in the course of operation are known Wasting Assets. (e.g.) A stone quarry will be useless when the available stone has been quarried.

Thus, some of the Flatting assets like Cash, B/R Investment etc., are known as liquid assets, in while, some of the fixed assets like Patents, Leases, Mines etc., are known as as wasting assets.

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The intangible Assets are divided into Real and Fictitious assets. Goodwill is an intangible asset. It is real in the sense that it can be exchanged for money. Prepaid expense is an intangible asset; it is fictitious in the sense that it cannot fetch anything if sold. Fictitious assets are also known as paper Assets of a Trade.

VALUATION OF ASSETS

Correct estimation of profit depends largely upon the valuation of assets and liabilities. Any improper valuation would exhibit a wrong picture. Only when the assets and liabilities are properly valued Balance Sheet will show a true and fair view of the state of affairs.

Fixed Assets should be value either at the cost price or market price whichever is lower (i.e.,) at the realizable value.

Both valuations should be made on the basis of a going concern. If assets are overvalued or undervalued, the profit would not be a correct one. This should be avoided.

VALUATION OF CLOSING STOCK

At the end of the accounting period, by means of a journal entry, closing stock is recorded in the books. The over valuation of stock increases the profits, while the undervaluation decreases the profits. Any anticipated loss should be provided for. In other words, Profit on goods will arise only when it is actually sold. The only exception to the above rule is to be found in the case of Timber and Wine traders where stocks appreciate in value from year to year according to its maturity.

NOTES

What is FIFO?

Inventory accounting in which the oldest items (those first acquired) are assumed to be the first sold.

However, in any case, it should not exceed the then market value. The accepted principle is that closing stock should be valued according to the cost or market price whoever is lower. In this connection the cost may be based on.....

1. FiFo (First in first Out): This method is based on the assumption that the earliest lost are exhausted first and hence closing stock is valued accordingly:

	15 th Oct.,	10 Units at Rs.10
Purchased on	18 th Nov.	20 Units at Rs.11
	17 th Dec.,	25 Units at Rs.12

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The closing stock consists of 30 units. It will be valued.

$$25 \times \text{Rs.12} = 300$$

$$5 \times \text{Rs.11} = 55$$

$$355$$

2. LIFo (Last in First Out): This method is based on the assumption that the latest lots are exhausted first and hence closing stock is valued accordingly.

$$10 \times \text{Rs.10} = 100$$

$$20 \times \text{Rs.11} = 220$$

$$330$$

The Lifo Method is not commonly used and is not generally accepted for taxation purposes.

3. Average (Simple or weighed): All the lots are merged together and the value of closing stock is as follows:

a) Simple Average:

$$\text{Rs.10} + \text{Rs.11} + \text{Rs.12} = 33 - 3 = 11$$

$$\text{Rs.11} \times 30 = \text{Rs.330}$$

b) Weighted average:

$$\text{Rs. } 10 \times 10 = 100$$

$$\text{Rs. } 11 \times 20 = 220$$

$$\text{Rs. } 12 \times 25 = 310$$

$$55 \quad \underline{\quad} \quad \underline{\quad} \quad 620$$

$$620$$

$$\text{---} = \text{Rs. } 11.27$$

$$55$$

$$= 11.27 \times 30 = \text{Rs. } 238$$

4. Base Stock Method: Where such stock is permanently retained at a fixed original cost say 20 units at Rs.8 plus 10 units at 11 or Rs.12 or Rs.11.27.

2. LIABILITIES

Liabilities are sums owing by a business concern to others. Broadly speaking, liabilities may be divided into 2 classes.

1) External Liabilities: and

2) Internal Liabilities

External Liabilities represent those amounts due to various persons who are not the owners of the business.

(e.g.,) Sundry Creditors (for goods purchased etc.)

Bank Overdraft:

Internal Liabilities represents the indebtedness of the business concern to its proprietor.

(e.g.,) Capital

Sometimes, External Liabilities are classified as Fixed and Floating Liabilities. The Fixed Liabilities are those obligations – which are more or less permanent.

What are liabilities?

Liabilities are anything that is owed to someone else.

Classification of Liabilities

1. Internal liabilities
2. External liabilities.

NOTES

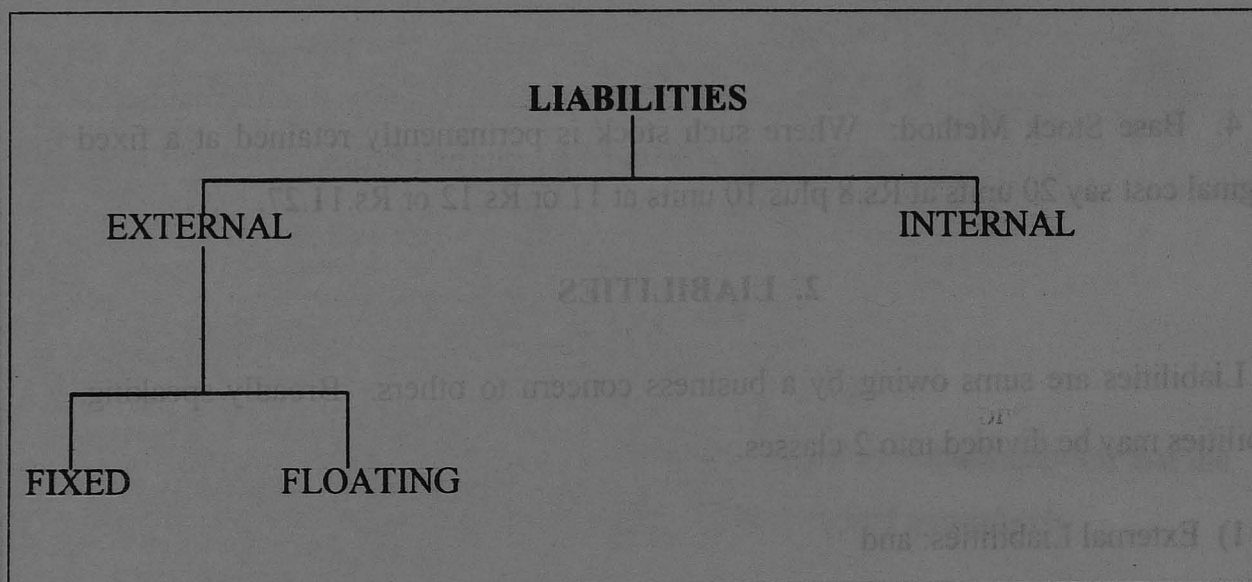
(e.g.) Mortgage

If the obligations have to pay within a short period then such liabilities are called Floating Liability. They are otherwise known as Current Liabilities.

What are current Assets?

All those assets which can be converted to cash within the normal course of period or one year which is called as current assets.

(e.g.) Bank O/D, Bills Payable etc.



3. CAPITAL & REVENUE

Suppose, a businessman starts his business with Rs.20,000. On 1st January 2003 (i.e.,) The business has a capital of Rs.20,000. Let it be further assumed that he has earned a profit of Rs.1, 500 in the course of year. The revenue for the year is Rs.1, 500.

Capital is the source of revenue, it comes out of Capital

The capital brought in the form of cash is employed in acquiring assets. Similarly, the capital will be increased by bringing in additional capital or by transferring profit to capital account.

It must be remembered that capital items and revenue items should not be confused with each other.

CAPITAL EXPENDITURE AND REVENUE EXPENDITURE

Proper distinction and appointment between Capital and Revenue Expenditure is of great importance and it affects the fundamentals of account. (i.e.,) the amount of profit or loss and correctness of Balance Sheet. Hence, proper adjustment of these items must receive careful attention at the time of the preparation of Final Account. Capital items will form part of the Balance Sheet and Revenue items will be included in the Revenue items will be included in the Revenue Account (i.e.,) Profit and Loss Account which consists of Trading and Profit and Loss A/c. Any incorrect allocation would falsify the result shown by the Final Account.

(e.g.) To credit the amount realized on the sale of old assets to Sale Account.

CAPITAL EXPENDITURE:

All expenditure which results in the acquisition, extension or improvement of permanent assets (which are permanently held and used in the business) for the purpose of earning revenue is called Capital Expenditure.

(e.g.) Cost of Building, Furniture, Fixture, Machinery, amount spent to repair second hand machinery, Purchase of goodwill of a running business etc.

Any amount spent which tends to improve the revenue earning capacity of these assets may rightly be treated as capital expenditure. If finds its place in the Balance Sheet, in short, presents an asset or repayment of a liability and its benefit is available for a long time.

REVENUE EXPENDITURE:

Expenditure incurred in buying goods for re-sale, distribution and financial expenses incurred to carry on the business from day-to-day and to maintain the fixed assets in working condition are termed as Revenue Expenditure.

Examples of Revenue Expenditure are

Salary, Wages, Rent, Discount, Repairs

What is capital expenditure?

Capital expenditure means the cost of long-term improvements.

NOTES

Any amount spent by ways of repairs, replacement etc., which does not increase the revenue earning capacity of the business, will come under the heading of Revenue Expenditure. It finds its place in the Profit and Loss Account. In short, it represents a loss and its benefit is available only for the present.

(e.g.) Making a gallery to seat more people in a cinema theatre is Capital Expenditure.

Making a new exit in a cinema theatre is Revenue Expenditure because capacity is not increased.

It must be pointed out that not only the purchase price of a fixed assets, but also the expenditure incurred in acquiring the fixed assets should be treated as capital expenditure.

(e.g.) Carriage is Revenue Expenditure. But Carriage on Plan and Machinery or Furniture should be debited to the concerned asset account. Wages, revenue expenditure, when paid to laborers for construction of a Building is a capital account or Capital Reserve Account. This account is shown on the liability side of the Balance Sheet.

CAPITAL LOSSES AND REVENUE LOSSES:

Revenue Losses are those which are incurred in the ordinary course of the business whereas Capital Losses are those which occur when selling fixed assets at a loss.

Generally capital losses are written off against capital profits as and when they arise. However, if capital losses are huge, they are written off over a number of years.

DEFERRED REVENUE EXPENDITURE

Deferred Revenue Expenditure is that class of expenditure which is incurred during an accounting period but is applicable either wholly or in part to future profits. Where any business concern incurs heavy expenditure of a revenue nature in any year

Definition of capital

Capital loss means the loss incurred by which the purchase price of an asset exceeds the selling price; the loss is incurred when the asset is sold.

and the benefit of which is likely to extend over a number of years. It is but provides that expenditure is spread over the number of years for which the benefit is derived.

Pickels and Dunkerly have classified it into four distinct types.

1. Expenditure wholly paid for in advance, where service has not yet been rendered necessitating its being carried forward (e.g.) Telephone Rental or Office Rent paid in advance.

2. Expenditure partly paid in advance, where a proportion to the benefit has been derived within the period under review, the balance being "unused" and therefore shown in the Balance Sheet as an asset.

(e.g.) Special advertising expenditure incurred in introducing a new product or developing a new market.

3. Expenditure in respect of service rendered which for any sound reason is considered as an asset.

(e.g.) Development costs in mines and plantations.

4. Amounts representing losses of an exceptional nature.

(e.g.) Heavy loss of non-insured assets.

As a rule an item falling under this head is a fictitious asset. Although it is shown on the asset side of the Balance Sheet. It is only really an asset at all but an abnormal loss which is to be written off. Every year only the proportionate amount is written off as loss and the balance will remain in the account as temporary asset.

In one word, such expenses are temporarily capitalized, as their writing off to Profit and Loss Account is temporarily postponed or deferred.

DIFFERENCE BETWEEN CAPITAL EXPENDITURE & REVENUE EXPENDITURE

If a proper distinction between capital Expenditure and Revenue is not made, the Final Account would be misleading. But it is not very easy to make such distinctions.

What is Capital Expenditure and what is Revenue Expenditure depends on the nature of the business. Machinery will be Capital Expenditure for an ordinary business but it will be a Revenue Expenditure for a machine manufacturer.

To find out whether a particular expenditure is Capital Expenditure or Revenue Expenditure, ask yourself, whether the expenditure results in the purchase of fixed assets or increases the earning capacity of the business or reduces costs in producing goods. If the answer is 'Yes' the expenditure is Capital otherwise Revenue Expenditure.

The following are the main points of distinction between Capital Expenditure and Revenue Expenditure.

CAPITAL EXPENDITURE	REVENUE EXPENDITURE
1. Capital Expenditure is of a non-recurring nature incurs for the running of the business.	1. Revenue Expenditure is of a recurring nature incurred for the maintenance of the existing assets.
2. Expenditure whose benefit is available for a long time is Capital Expenditure. Examples are money spent to acquire permanent assets like Land & Building, Plant & Machinery, Tools, Furniture & Fixtures; Purchasing Goodwill of a running business, Repairing second hand assets etc.	2. Expenditure whose benefit is available only of the present is Revenue Expenditure. Examples are money spent for the payment of Salary, Wages, Rent, etc.
3. It adds to the revenue earning capacity of the business (e.g.) making a gallery in a Cinema theatre is Capital Expenditure	3. It could not do so, (e.g.) Making exit in a Cinema theatre is Revenue Expenditure because capacity is not increased.

because capacity is increased.	
4. It will be shown on the assets of the Balance Sheet.	4. It will be shown in the Profit and Loss Account.

Example : 6

The following Trial Balance was extracted from the books of Kumar on 31st December .2002.

KUMAR

TRIAL BALANCE

As on 31st December 2002

Debit Balances	Rs.	Credit Balances	Rs.
P Salaries and Wages	4,000	L Capital	2,05,000
T purchases	2,00,000	P Discount Received	300
T Duty and Clearing Charges	7,000	T Sales	3,00,000
P Legal & Accountancy Charges	2,000	T Purchases Returns	4,000
T Sales Returns	10,000	L Sundry Creditors	16,000
A Cash Balance	10,000	L Bank O/D	3,000
T Stock at Commencement (1.1.2002)	15,000	L Bills Payable	1,000
P Advertisement	1,000	L Loan	10,000
A Land & Buildings	1,60,000	P Income from Investment	700
A Plant & Machinery	50,000		
A Investments	5,000		
(Special) Drawings	6,000		
A Sundry Debtors	60,000		
A Bills Receivable	10,000		
	<u>5,40,000</u>		<u>5,40,000</u>

Adjustment: Stock at the end 3.12.2002 Rs.30, 000. Prepare the Final Account

T= Trading A/c P= P & L A/c; A=Assets; L = Liabilities

NOTES

Solution:

Adjustment Entry

		Rs.	Rs.
Closing Stock A/c	Dr.	30,000	
To Trading A/c			30,000

[Being the closing stock brought into account]

KUMAR

TRADING AND PROFIT AND LOSS ACCOUNT

For the Year ending 31st December 2002

	Rs.	Rs.		Rs.	Rs.
To Opening Stock		15,000	By Sales	3,00,000	
To Purchases	2,00,000		Less: Sales	10,000	2,90,000
Less: P. Returns	4,000	1,96,000	Returns		30,000
To Duty & Clearing			By Closing		
Charges		7,000	Stock		
To GROSS PROFIT -					
Transferred to Profit					
&		1,02,000			3,20,000
Loss A/c		3,20,000			
To Salaries & Wages		4,000	By GROSS		
To Legal &		2,000	PROFIT -		1,02,000
Accountancy Charges		1,000	Transferred		300
To Advertisement			from		
To NET PROFIT -		96,000	Trading		700
Transferred to capital			account		
		1,03,000			1,03,000
			By Discount		
			received		
			By Income		
			from		
			Investments		

KUMAR**BALANCE SHEET**As at 31st December 2002

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
Sundry Creditors		16,000	Cash Balance		10,000
Bills Payable		1,000	Investments		5,000
Bank O/D		3,000	Bills Receivable		10,000
Loan		10,000	Sundry Debtors		60,000
Capital	2,05,000		Closing Stock		30,000
Add Net Profit	96,000		Land & Building		1,60,000
	3,01,000		Plant & Machinery		50,000
Less: Drawings	6,000				
		2,95,000			
		3,25,000			3,25,000

DIFFERENCES BETWEEN A TRIAL BALANCE AND A BALANCE SHEET

TRIAL BALANCE	BALANCE SHEET
1. A trial balance is a list of all the balances standing on the ledger accounts and books at any given date.	1. A balance sheet is a statement of assets and liabilities of the business on a given date.
2. It is prepared before the preparation Trading and Profit and Loss Account.	2. A Balance Sheet is prepared after the preparation of the Trading and Profit and Loss Account.
3. The object of Trial Balance is to test the arithmetical accuracy of ledger postings.	3. The object of the Balance Sheet is to find out the 'true and fair' view of the financial position of a concern on a given date.
4. A trial balance contains the stock at commencement.	4. The Balance Sheet includes the closing stock (but not the opening stock)
5. The trial balance is prepared before	

NOTES

the adjusting entries are passed and so the effect of adjustments cannot be seen in the Trial Balance.	5. The Balance Sheet is prepared after adjusting entries are passed and so includes the effect of all adjustment.
6. It contains all types of accounts.	6. Balance Sheet does not contain Nominal accounts.
7. The debit and credit balances are listed in a Trial Balance on the left hand and right hand sides respectively.	7. While assets (debit balances) and liabilities (credit balance) are show on right hand and left hand sides respectively in the Balance Sheet.
8. There is no order as to the arrangement of items in the Trial Balance.	8. In Balance Sheet assets are arranged in the order of liquidity or permanence and liabilities are arranged in the order of urgency of payment or in the reverse order.
9. Different forms like statement form, tabular form 'T' shirt form are in vogue for the preparation of Trial Balance.	9. Balance Sheet is prepared usually in the form prescribed by tax authorities and according to the Companies Act.
10. Trial Balance does not form part of the Final Accounts so it is not subjected to audit.	10. Whereas Balance Sheet forms part the final accounts, so it is subjected to the audit.

MANUFACTURING ACCOUNT

A businessman may purchase goods from others who manufacture them and then sell them to his customers. Or, he may manufacture the goods himself and then sell them to consumer.

Where manufacturing takes place, a Manufacturing Account is prepared. It is prepared by a manufacturer who converts the raw materials into finished products. The Manufacturing Account tells us of the cost that has been incurred in manufacturing the goods for a given period.

The manufacturing Account is debited with the following items:

1. Opening Stock of Raw Materials.
2. Work in Progress of Work-in-processor Partly Manufactured Goods or Semi Finished Goods.
3. Purchase of Raw Materials less returns if any
4. All Manufacturing and Factory Expenses.
5. Depreciation on Plan and Machinery, Tools, Factory and Repairs to those assets.

The Manufacturing Account is credited with the following items;

1. Closing stock of Raw Materials
2. Work-in-Progress at the end, and
3. Sale of Waste and Scrap

The cost of goods manufactured as shown in the Manufacturing Account is transferred to the debit of Trading Account. The Manufacturing Account shows the result of the Manufacturing Department while the Trading Account show the result of the Selling Department.

In addition to the Manufacturing Account, the businessman will also prepare a Trading Account which is debited with the Opening Stock of Finished goods and Cost of goods produced and credited with Sales Less Returns and Closing Stock of Finished Goods. The Gross Profit shown by the Trading Account will be transferred to Profit & Loss Account. The Profit and Loss Account is debited with expenses, & losses (except those already transferred to Manufacturing Account) and credited with gains and incomes. If any (except that by the sale of waste and scarp). The Net Profit shown by the Profit and Loss Account will be transferred to Capital Account. As already explained the Balance Sheet is prepared in the usual way.

We shall proceed with the case of a manufacturer.

Example : 7

Draw up Bombay Walah's Manufacturing Account showing cost of production and the Trading Account showing gross profit from the following information:

₹ 2,14,201

Factory Wages	14,000
Purchase of Raw Materials	4,000
Sales	56,000
Sales Returns	2,000
Opening stock (1-1-2002)	
Raw Materials	8,000
Work-in-progress	2,000
Finished goods	4,000
Factory Insurance	2,000
factory on Materials	1,000
Salary to works Manager	3,600
Carriage on Raw Materials	1,400
Power	1,600
Repairs to machinery	600
Depreciation on Plant & Machinery and Building	5,000

Adjustment: The Closing Stock 31.12.2002 was valued at:

Rs.

Raw Materials	6,000
Work-in-progress	3,000
Finished Goods	2,000

BOBAY WALAH'S

MANUFACTURING AND TRADING ACCOUNT

For the year ending 31st December 2002

	Rs.	Rs.		Rs.	Rs.
To Opening Stock			By Closing Stock :		
Raw Materials	8,000		Raw Materials		
Work-in Progress	2,000		Work-in-Progress	6,000	
		10,000			9,000
To Purchases of Raw Materials		4,000		3,000	
To Factory Wages		14,000	By Cost of goods		
To Factory Insurance		2,000	Manufactured		33,600
To Octroi on Materials		1,000	transferred to Trading		
To Salary to works			A/c		
Manager		3,600			
To Carriage on Raw					
Materials		1,400			
To Power		1,000			
To Repairs to machinery		600			
To Depreciation on Plant		5,000			
etc.,					
		42,600			42,600
To Opening Stock of					
Finished Goods		4,000			
To Cost of Goods			By Sales		48,500
manufactured Transferred			Good Returned		
from manufacturing A.c			Closing Stock	50,000	
To Gross Profit		33,600			2,000
Transferred to Profit and			Finished Goods		
Loss Account		12,400		2,000	
		50,000			50,000

METHOD OF WORKING FINAL ACCOUNT

You are now familiar with the nature of the items appearing in the Trading and Profit and Loss Account and the Balance Sheet. The capacity to recognize at sight the adjustment items that will appear in Trading and Profit and Loss Account and the Balance Sheet should also be developed by students of accountancy. An effort is made to explain the important aspects to satisfy the needs of the beginners.

1. Go through the balance marking as to where they will appear

T – Trading P – Profit and Loss B- Balance Sheet

2. If the figures given are not in the Trial Balance from, they should be scored out debits and credits by preparing a Trial Balance.

3. Mark with a asterisk* those items which require adjustment (Remember that adjustments appear twice in the Final Accounts) Always pass Adjustment Entries.

4. Tick-off the items as they are entered in the Final Account.

SUMMARY OF ADJUSTMENT

Serial No.	Adjustment	Entry	Place in Revenue A/c	Place in Balance Sheet
1.	Closing Stock	Closing Stock A/c Dr. To Trading A/c [Being the closing stock brought into Account]	Trading A/c	Assets Side
2.	Outstanding Expenses creditors for	Expenses A/c Dr. To outstanding Creditors A/c	Add to expenses in Trading or P & L A/c	Liabilities Side Outstanding expenses
3.	Prepaid Expenses	Prepaid expenses A/c Dr. To Expenses A/c [Being the prepaid expense adjustment]	Less from expenses in Trading or P & L A/c.	Assets Side
4.	/Outstanding Income	Outstanding Income A/c Dr. To income A/c [Being the outstanding income adjusted]	Add to income in P & L A/c	Assets Side

5.	Income Received In Advance	Income A/c Dr. To Income Received in Advance A/c	LESS from Income in P & L A/c	Liabilities side
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		[Being the Income received in advance deposited]		
6.	Depreciation	Depreciation A/c Dr. To Asset A/c [Being % depreciation on asset provided for]	Debit P & L A/c	Less from the respective asset in B/S
7.	Writing of Bad	Bad Debts A/c Dr. To sundry Debtors A/c [Being bad debts written off]	ADD to Bad Debts in P & L A/c	Less from Sundry Debtors in B/S.
8.	Provision for Doubtful Debts	Profit & Loss A/c Dr. To Reserve for Doubtful Debts [Being the provision created]	P & L A/c (Debit Side)	Less from Sundry Debtors on Assets Side
9.	Provision for Discount on Debtors	Profit & Loss A/c Dr. To Reserve for Discount on Debtors A/c [Being the provision created]	P & L A/c (Debit Side)	Less from the Amount of good sundry debtors on Assets side
10.	Provision for Discount on creditors	Reserve for Discount on Creditors A/c Dr. To Profit & Loss A/c [Being the provision created]	P & L A/c (credit Side)	Less from sundry creditors on Liabilities side
11.	Interest on Capital	Interest on Capital A/c Dr. To Capital A/c [Being the interest on Capital provided for]	P & L A/c (Debit Side)	Add to Capital on the Liabilities side
12.	Interest on Drawings	Drawing A/c Dr. To Interest on Drawings A/c	P & L A/c (Credit Side)	Add to drawing and then
13.	Miscellaneous items	[Being the interest on drawing provided for]	5214 v1	Less the total of the drawings from capital on the Liabilities side.

Note: "To Provide" for an expense or for an income means add so much amount to expenses or income amount. 'Accrued' or 'Accrued and Due' or "Accrued but not received/paid" means to add so much amount to the expense or income.

Chart – 2

PROVISIONS AT A GLANCE

Serial No.	Item	To Create Provision	To Increase a Provision	To Reduce a Provision
1.	For Bad & Doubtful Debts	Profit & Loss A/c Dr. To R.B.D.A/c	Profit & Loss A/c Dr. To R.B.D.A/c (with the amount of increased	R.B.D. A/c Dr. To Profit & Loss A/c. (with the amount by which the provision is to be reduced)
2.	For Discount on Debtors	Profit & Loss A/c Dr. To R.D.D. A/c.	Profit & Loss A/c Dr. To R.D.D. A/c (with the amount of increase)	R.D.D. A/c Dr. To Profit & Loss A/c (with the amount by which the provision is to be reduced)
3.	For Discount on Creditors	R.D.C. A/c Dr. To Profit & Loss A/c	R.D.C. A/c Dr. To Profit & Loss A/c. (with the amount of increase)	Profit & Loss A/c Dr. To R.D.C. A/c (with the amount by which the provision is to be reduced)

R.B.D. Reserve for Bad Debts (i.e.,) Provision for Doubtful Debts.

R.D.D. Reserve for Discount on Debtors (i.e) Provision for Discount on Debtors.

R.D.C. Reserve for Discount on Creditors (i.e) Provision for Discount on Creditors

Wrong Usage

Correct Usage

Illustration: 1

From the following Trial Balance of Arul, prepare the Trading and Profit and Loss Account (after passing the requisite Adjusting and Closing Entries) for the year ended 31st December 2002 and a Balance Sheet as at that date.

TRIAL BALANCE

NOTES

DEBIT	Rs	LIABILITIES	Rs.
Wages	35,000	Arul's Capital Account	75,000
Carriage inwards	2,000	Sundry Creditors	60,000
Trade Expenses	9,500	Sales	2,40,000
General Expense	8,000	Provision for Doubtful Debts	2,350
Factory Lighting	900	Purchase Returns	1,200
Horses and Carts	5,200	Bank Loan	7,600
Postages and telegrams	800		
Insurance and Taxes	4,150		
Carriage outwards	1,800		
Salaries	16,200		
Sundry Debts	80,000		
Stable Expenses	2,000		
Purchases	95,000		
Bad Debts	1,600		
Plant and Machinery	20,000		
Fixtures and Fitting	9,000		
Freehold Premises	25,000		
Goodwill	40,000		
Fuel and Power	1,350		
Stock, 1 st Jan.2002	15,000		
Sales Returns	3,200		
Discount	750		
Interest and Bank Charges	450		
Cash at Bank	8,135		
Cash in hand	665		
	<u>3,86,150</u>		<u>3,86,150</u>

NOTES

Adjustments:

1. Stock on 31st December 2002 Rs.30,000
2. Unexpired insurance Rs.250 and Taxes Rs.200
3. Provide Depreciation as under :
 - (a) Plant and Machinery @ 10%
 - (b) Fixtures and Fittings @ Rs.15%
 - (c) Horse and Carts @ 20%
4. Maintain the Provision for Doubtful Debts @ 5%
5. A Commission of 2 percent on the Gross Profit to be provided for Works

Manager.

6. A commission of 4 percent of Net Profit (after charging the works Manager's Commission) to be credited to the General Manager.

Solution:

The following are adjustment Entries:

		Rs. P.	Rs. P.
Prepaid Expenses A/c Dr		450.00	
To Insurance and Taxes A/c			450. 00
[Being the unexpired expenses adjusted]			
Depreciation A.c Dr.		4,390.00	
To Plant and Machinery A/c			2,000. 00
To Furniture and Fittings A/c			1,350. 00
To Horses and Carts A/c			1,040. 00
[Being the Depreciation provided on various assets]			
Profit and Loss A/c Dr.		1,650.00	
To Provision for Doubtful Debts A/c			1,650.00
[Being the provision for Doubtful Debts amount increased to maintain 5%on Debtors]			
Commission A/c Dr.		4,796.00	
To Outstanding Creditors A/c			4,796.00

[Being the commission payable to Works and General Manager at the rate of 2% and 4% on Gross Profit and Net Profit respectively]			
Purchases Returns A/c	Dr.	1,200.00	
To Purchase A/c			1,200.00
[Being the transfer of purchase returns to latter account]			
Sales A/c	Dr.	3,200.00	
To Sales Returns A/c			3,200.00
[Being the transfer of Sales Returns to former account]			
Stock A/c	Dr.	30,000.00	
To Trading A/c			30,000.00
[Being the value of the closing stock brought into account]			

The following are the closing entries:

		Rs.	P.	Rs.	P.
Trading A/c	Dr.	1,58,750.00			
To Stock A/c				15,000.00	
To Purchases A/c				95,000.00	
To Wages A/c				35,000.00	
To Carriage Inwards A/c				2,000.00	
To Fuel and Power A/c				1,350.00	
To Factory Lighting A/c				900.00	
To Trade Expenses A/c				9,500.00	
[Being the transfer of latter accounts to the former]					
Sales A/c	Dr.	2,40,000.00			
To Trading A/c				2,40,000.00	
[Being the transfer of sales to Trading Account]					
Profit and Loss A/c	Dr.	46,586.00			

NOTES

To Salaries A/c			16,200.00
To General Expenses A/c			8,000.00
To Insurance and Taxes A/c			3,700.00
To Carriage Outwards A/c			1,800.00
To Stable Expenses A/c			2,450.00
To Discount A/c			750.00
To Postage and Telegrams A/c			800.00
To Bad Debts A/c			3,250.00
To Interest and Bank charges A/c			450.00
To Depreciation A/c			4,390.00
To Commission A/c			4,796.00
[Being the transfer of various nominal accounts to P & L A/c]			
Profit and Loss A/c	Dr.		
To Capital A/c		62,664.00	62,664.00
[To Capital Account]			

ARUL

TRADING PROFIT AND LOSS ACCOUNT

For the year ended 31st Dec.2002

To Stock 1-1-2002	Rs.	Rs.		Rs.	Rs.
To Purchases					
To Less: Returns		15,000	By Sales	24,000	
To Wages	95,000		By Less: Returns	3,200	2,36,800
To Carriage Inward	1,200	93,800	By Stock 31.12.02		30,000
To Fuel and Power		35,000			
To Factory Lighting		2,000			
To Trade Expenses		1,350			
To Gross Profit		900			
Transferred to P&L A/c		9,500			
		1,09,250			
To Salaries		2,66,800			2,66,800
To General		16,200			
Expenses		8,000			
To Insurance &		3,700			
Taxes		1,800			

To Carriage Outwards		2,450	By Gross Profit		
To Stable Expenses		750	Transferred from		
To Discounts		450	Trading A/c		1,09,250
To Interest and Bank Charges		800			
To Postage and Telegrams	4,000				
To Provision for Doubtful Debts	1,600				
To Add:Bad Debts	5,600	3,250			
	2,350				
To Less:Old Reserve					
To Depreciation:	2,000				
Plant & Machinery at 10%	1,350				
Fixtures & Fittings at 15%	1,040	4,390			
Horses & Carts at 20%	2,185				
	2,611	4,796			
To Commission:					
Works Manager at 2%		1,09,250			
General Manager at 4%					
To Net Profit Transferred to Capital A/c					1,09,250

BALANCE SHEETAs at 31st December 2002

CAPITAL AND LIABILITIES			PROPERTIES AND ASSETS		
	Rs.	Rs.		Rs.	Rs.
Outstanding Commission Payable	2,185		Cash in hand		605
Works Manager	2,611	4,796	Cash in Bank		8,135
General Manager		60,000	Sundry Debtors	80,000	
Sundry Creditors		7,600	Less Provision for Doubtful Debts		
Bank Loan			@5%	4,000	76,000
Capital Account	75,000		Stock		30,000
Balance on 1.1.2002					
Add Net Profit During the year	62,664	1,37,664	Expenses prepaid		450
			Plant and Machinery		25,000
			Freehold Property	20,000	
			Less: Depreciation		
			@ 10%	2,000	18,000
			Fixtures and Fittings	9,000	
			Less: Depreciation @15%	1,350	7,650
			Horses and Carts	5,200	
			Less: Depreciation @ 20%	1,040	4,160
			Goodwill		40,000
		2,10,060			2,10,060

Illustration: 2

From the following Trial Balance and adjustment of Krishnamurthy prepare his Final Accounts.

	Rs.	Rs.
Sundry Debtors	32,000	
Stock (1 st Oct.2002)	22,000	

Cash Balance	1,580	
Bank Overdraft		9,000
Plant & Machinery	17,500	
Sundry Creditors		10,650
Trade Expenses	175	
Good sold		1, 34,500
Salaries	2,225	
Carriage outwards	300	
Rent	900	
Bill Payable		7,600
Goods bought	1,18,870	
Insurance	1,200	
Business Premises	34,500	
Commission	500	
Capital		70,000
Carriage Inwards	1,000	
	<u>2,32,250</u>	<u>2,32,250</u>

1. The Stock on 30th September 2003 was Rs.11,000
2. Rent Rs.100/- per month for the last quarter is unpaid
3. Depreciation Plant & Machinery k10% and Business Premises by 20% p.a.
4. Commission earned but not received amounts to Rs.200
5. Carry forward unexpired insurance on 30th September 2003, Rs.400.

ADJUSTMENT ENTRIES

Date	Particular	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2003 Sept 30	Closing Stock Dr. To Trading A/c [Being the closing stock brought in to account]		11,000	00	11,000.00	
	Rent A/c Dr. To Outstanding Expenses A/c [Being the unpaid rent adjusted]		300	00	300.00	
	Depreciation A/c Dr. To Plant & machinery A/c To Business Premises A/c [Being 10% depreciation on Plant and 20% on premises provided for]		8,650	00	1,750.00 6,900.00	
	Outstanding Income A/c Dr. To Commission A/c [Being the accrued Commission Adjusted]		200	00	200.00	
	Prepaid Expenses A/c Dr. To Insurance A/c [Being the prepaid insurance adjusted]		400	00	400.00	

KRISHNAMURTHY'S

TRADING AND PROFIT AND LOSS ACCOUNT

For the year ending 30th September 2003

	Rs.	Rs.		Rs.	Rs.
To Opening Stock		22,000	By Sales		1,34,500
To Purchases		1,18,870	By Closing Stock		11,000
To Carriage Inwards		1,000			
To Gross Profit c/d		3,630			
		1,45,500			1,45,500
To Trade Expenses		175	By Gross Profit b/d		3,630
To Salaries		2,225	By Commission	500	
To Carriage Outwards		300	Add Outstanding	200	700
To Rent	900				

Add Outstanding To Insurance	300	1,200		
To Less Prepaid To Depreciation Plant & Machinery @10%	1,200			
Business Premises @20%	400			
	1,750		Net Loss Transferred To Capital A/c	9,020
	6,900	8,650		
		13,350		13,350

KRISHNAMURTHY'S

BALANCE SHEET

As at 30th September 2003

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
Outstanding Creditors rent		300	Cash Balance		1,580
Sundry Creditors		10,650	Sundry Debtors		32,000
Bill Payable		7,600	Closing Stock		11,000
Bank Overdraft		9,000	Prepaid Expenses		400
Capital	70,000		Plant & Machinery	17,500	
Less: Net Loss	9,020	60,980	Less: 10% Depreciation	1,750	15,750
			Business Premises	34,500	
			Less: 20% Depreciation	6,900	27,600
			Outstanding Debtors		
			Commission		200
		88,530			88,530

Illustration: 3

Edward's Book shows the following balances. Prepare his Trading and Profit and Loss A/c for the year ended 31st December 2002 and Balance Sheet as at that date.

	Rs.		Rs.
Drawings	5,000	Capital	1,08,850
Bills Receivable	4,500	Loan @ 6% p.a	20,000
Land Buildings	37,770	Sales	3,50,000
Sundry Debtors	62,000	Interest on Investments	5,640
Wages & Salaries	40,970	Sundry Creditors	59,000

NOTES

Returns inwards	2,780	Commission Received	630
Purchases	2,56,590	Returns outwards	6,430
Postage & Telegram	5,620		
Stock at Commencement	89,680		
Printing & Stationery	880		
Travelling Expenses	12,000		
Interest on Loan Paid	300		
Petty Cash	70		
Bank Balance	8,800		
Commission	470		
Repairs	3,620		
Furniture	500		
Investments	19,000		
	<u>5,50,550</u>		<u>5,50,550</u>

Adjustment: (1) The Closing Stock Rs.1,28,960 – on 31.12.2002

(2) Commission received but not earned Rs.130

(3) Travelling Expenses were overdrawn by the employee to the extent of Rs.2, 000.

(4) Create a 5% Reserve for Doubtful Debts on Sundry Debtors and 2% Reserve for discount on Debtors and Creditors.

(5) Interest on loan due for 9 months

(6) $\frac{1}{4}$ th of Wages and Salaries should be charged to Trading Account.

Pass Closing journal entries only.

Solution:

NOTES/

EDWARD'S

TRADING AND PROFIT AND LOSS ACCOUNT

For the year ending 31st December 2002

Dr.

Cr

	Rs.	Rs.		Rs.	Rs.
To Opening Stock		89,680	By Sales	3,50,000	
To Purchases	2,56,590		Less: Returns		
Less Returns			Inwards	2,780	3,47,220
Outwards	6,430	2,50,160	By Closing Stock		1,28,960
To Wages & Salaries (1/4)		10,242			
Gross Profit c/d		1,26,097			
		4,76,180			4,76,180

Dr.

Cr

	Rs.	Rs.		Rs.	Rs.
To Wages & Salaries		30,727	By Gross Profit b/d		1,26,097
To Postage & Telegrams		5,620	By Interest on		
To Printing & Stationery		880	Investments		5,460
To Travelling Expenses	12,000		By Commission		
Less: Overdrawn (Prepaid)	2,000	10,000	received	630	
To Interest on loan	300		Less: Commission		
Add: Outstanding	900	1,200	Received but not		
			earned	130	
To Commission		470			500
To Repairs		3,620			
To Reserve for Discount			By Reserve for		
On Debtors		3,100	Discount on		
To Reserve for Doubtful		1,178	Creditors		1,180
Debts					
NET PROFIT transferred		76,622			
to Capital A/c		1,33,417			1,38,417

BALANCE SHEET

As at 31st December 2002

LIABILITIES			ASSETS		
	Rs.	Rs.		Rs.	Rs.
Outstanding Interest On Loan		900	Petty Cash		70
Sundry Credits	59,000		Bank Balance		8,800
Less: Reserve for Discount on Creditors @ 2%	1,180	57,820	Investments		19,000
Loan @ 6% p.a. Capital	1,08,850	20,000	Bill Receivable		4,500
			Sundry Debtors	62,000	
Add Net Profit in	76,622		Less: Reserve for Doubtful Debts @5%	3,100	
	1,85,472			58,900	
Less: Drawings	5,000	1,80,472	Less: Reserve for Discount on Debtors @2%	1,178	57,722
Commission received in Advance		130	Closing Stock		1,28,960
		2,59,322	Prepaid Expenses		2,000
			Land and Buildings		37,770
			Furniture		500
					2,59,322

CLOSING ENTRIES

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Date	Particulars	L.F.	Dr. Rs. P.	Cr. Rs. P.
2003 Dec.31	Returns Outwards A/c Dr. To Purchases A/c [Being the purchases returns transferred to Purchases A/c]		6,430.00	6,430.00
	Sales A/c Dr. To Sales Returns A/c [Being the Sales returns transferred to Sales A/c]		2,780.00	2,780.00
	Trading A/c Dr. To Stock A/c To Purchases A/c To Wages A/c [Being the above accounts transferred to Trading A/c.]		3,50,082.00	89,680.00 2,50,160.00 10,242.00
	Sales A/c Dr. To Trading A/c [Being the sales account transferred to Trading A/c.]		3,47,220.00	3,47,220.00

CLOSING ENTRIES

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2003 Dec.31	Trading A/c Dr. To Profit & Loss A/c [Being the gross profit transferred to P & L A/c]		1,26,097.50		1,26,097.50	
	Profit & Loss A/c Dr. To Wages & Salaries A/c To Postage & Telegrams A/c To Printing & Stationery A/c To Travelling Expenses A/c To Interest A/c. To Commission A/c To Repairs A/c [Being the transfer of above items to Profit & Loss A/c]		52,517.50		30,727.50 5,620.00 880.00 10,000.00 1,200.00 470.00 3,620.00	
	Interest A/c Dr. Commission A/c Dr. To Profit & Loss A/c [Being the transfer of above items to Profit & Loss A/c]		5,640.00 500.00		6,140.00	
	Profit & Loss A/c Dr. To Capital A/c [Being the transfer of Net Profit to Capital A/c]		76,622.00		76,622.00	

Illustration: 4

From the following ledger balances extracted at the close of Trading year ended 31st December 2002, Prepare a Trading Account, Profit & Loss Account and Balance Sheet at the date, after giving effect to the under mentioned adjustments.

	Rs.		Rs.
Capital on 1.1.2002	50,000	Business Premises	55,000
Stock on 1.1.2002	8,000	Furniture and Fixtures	2,500
Purchases	20,000	Bills Receivable	3,500
Sales	80,000	Bills Payable	3,000
Returns Inwards	1,500	Sundry Debtors	20,000
Returns Outwards	400	Sundry Creditors	15,800
Wages	6,900	Packing Machinery	4,500
Advertisement	5,500	Smith's loan(Dr)@10%	
Apprenticeship Premium	1,200	On 1.1.2002	5,000
Interest on Smith's Loan	300	Investment	3,000
Proprietor's withdrawals	3,000	Cash in Hand	250
Office Expenses	8,050	Cash at Bank	3,500

Adjustments to be made for the current period.

1. Stock in hand as on 31st December 2002 Rs.7, 000
2. Apprenticeship Premium are for the three years paid in advance on 1st January 2002.
3. Interest on Capital to be allowed at 5% for the year
4. Interest on Drawings to be charged him as ascertained for the year Rs.80
5. Rs.6,000 out of the advertisement expenses are to be carried forward
6. Stock valued at Rs.3,000 destroyed by fire on 25.12.2002 but the Insurance Co., admitted claim of Rs.2,000 only and paid it in 2003

7. Included in Sales in an amount of Rs.10,000 representing good on "Sales or Return: the customer still having the right to return the Goods. The goods were invoiced sharing a profit of 20% on sales.

8. The stock includes materials worth Rs.1,000 for which bills had not been received and therefore not yet accounted for.

5214 v1

To Opening Stock	Rs.	Rs.	By Sales	Rs.	Rs.
To Purchases	20,000	8,000	Less: Sales Returns	80,000	
Less Returns	400			1,500	
	19,600			78,500	
Add Material not Accounted for	1,000	20,600	Less Goods Sold on Return Basis	10,000	68,500
To Wages		6,900	By Closing Stock	7,000	
To Gross Profit c/d		51,000	Add Stock lying with customers sold on return basis	8,000	15,000
		86,500	By Loss of Stock of fire		3,000
To Interest on Capital		2,500			86,500
To Advertisement	5,500		By Gross Profit b/d		51,000
Less Carried Forward	5,000	500	By Apprentice Premium	1,200	
To Lose (Stock) by Fire		1,000	Less: Received in Advance	800	400
To Office Expenses		8,050			
To Net Profit transferred to Capital A/c		39,930	By Interest on Drawings		80
			By Interest on Smith's Loan	300	
			Add Accrued Interest	200	600
		51,980			51,980

Balance Sheet

As on 31st December 2002

Liabilities					
	Rs.	Rs.		Rs.	Rs.
Sundry Creditors	15,800		Cash in hand		250
And Purchase of material not accounted for	1,000	16,000	Cash at Bank		3,500
Bill Payable		5,000	Investment		3,000
Apprentice Premium		800	Sundry Drs.	20,000	
Received in advance	50,000		Less Goods sold on Return basis	10,000	10,000
	2,000		Insurance Company		2,000
Capital			Closing Stock (7,000+8,000)		15,000
Add Interest	39,930		Bills Receivable		3,500
	91,930		Smith's Loan	5,000	
Add Net Profit			Add Accured Internet	200	5,200
	3,080	88,850	Packing Machinery		4,500
Less Drawings and interest			Furniture and Fittings		2,500
			Businees Premises		55,000
			Advertisement		5,000
		1,09,450			1,09,450

S214 v1

Adjustment items within the Trial Balance

Closing Stock, Prepaid Expenses, Outstanding Expenses, Outstanding Incomes, and Depreciation may appear in the T/B.

The student should be careful about such items. Since, they are in the Trial Balance; double entry process has already been completed. Therefore, the various accounts stand already adjusted. As such, such items will be transferred either to the Revenue Account or to the Balance Sheet without affecting any other account. In other words, no further adjustment in the form of addition or deduction need be made and the relevant accounts have prepaid already.

Adjustment items usually appear outside the Trial Balance; however, some of these may be incorporated in the Trial Balance for instance.

Example:

Where do you record the following items?

TRIAL BALANCE

As on 31st December 2002

S.No.	Name of Account	Dr,	Cr.
1 to 6	Sundry Debit Balance of various items	80,000	
7	Salaries	5,800	
8	Outstanding Expenses		1,000
9	Freehold Land	22,500	
10	Commission received		300
11	Depreciation (on Land)	2,500	
12	Prepaid Expenses	360	
13	Income Received in advance		700
14	Outstanding Income	200	
15 to 20	Sundry Credit Balance of various items		1,09,360
		1,11,360	1,11,360

7. Salaries would be transferred to Profit & Loss A/c
8. Outstanding Expenses would be shown as a liability in the Balance Sheet.
9. Freehold Land would be shown as an asset in the Balance Sheet.
10. Commission received would be transferred to the credit side of the Profit & Loss a/c.
11. Depreciation would be transferred to Profit & Loss A/c
12. Prepaid Expenses would be shown as an asset in the Balance Sheet.

NOTES

13. Income Received in Advance would be shown as a liability in the Balance Sheet.

14. Outstanding income would be shown as an asset in the Balance Sheet.

	Rs.	Rs.		Rs.	Rs.
To Miscellaneous		100	By Gross Profit b/d		14,625
Expenses		300			
To Repairs	150				
To Insurance	50	150			
Less Prepaid		325			
To Carriage on Sales		300			
To Discount		600			
To Loss by Fire		500			
To Free Samples		600			
To Depreciation					
To Net Profit-transferred		11,800			
to					
Capital A/c		14,625			14,625

MAKESH

BALANCE SHEET

As on 30th June 2003

LIABILITIES			ASSETS		
	Rs.	Rs.		Rs.	Rs.
Expenses Payable		700	Cash		25
Sundry Creditors	2,100		Bank Balance		2,000
Add: Omission of Invoices	1,000		Sundry Debtors		3,200
		3,100	Due from insurance Co.,		1,500
Capital	13,000		Stock-in-Trade		8,000
Add Net Profit	11,800		Prepaid Exepenses (Insurance)		50
	24,800		Loose Tools		500
Less Drawings (goods used)	800		Patent Rights		1,500
		24,000	Land		
Differences in Trial Balance			Machinery		4,000

Suspense A/c	375	Installation Expenses	5,400	
		Add Transferred from Wages	2,000	7,400
	28,175			28,175

Illustration: 6

The following is the Trial Balance of Thiru. Arasu

	Dr. Rs.	Cr. Rs.
Capital and Drawings	2,00,000.00	20,000.00
Debtors and Creditors	1,00,000.00	48,000.00
Goods purchased and sold	2,40,000.00	4,00,400.00
Returns of Goods	20,000.00	30,000.00
Bills Accepted and received	30,000.00	44,000.00
Cash Balance	10,000.00	
Heating and Lighting	10,000.00	
Factory Wages	20,000.00	
General Expenses	2,000.00	
Machinery on 1.1.2002	1,00,000.00	
Additions to Machinery 1.10.2002	20,000.00	
Furniture & Fixtures	30,000.00	
Salaries	40,000.00	
Loan to Mahadevan	20,000.00	
Dividend Received		2,000.00
Stock of Goods as on 1.1.2002	62,400.00	
	7,24,400.00	7,24,400.00

Adjustments:

1. Stock on hand on 31.12.2002

Goods Rs.80, 000

Stationery Rs.400

2. Goods destroyed but covered by insurance (not yet paid) Rs.10, 000

3. General Expenses include stationery purchased for Rs.900

4. Interest for 6 months @ 6% pa is due on loan to Mahadevan.

5. Depreciate Machinery and Furniture by 10% p.a

6. Include in sales is Rs.5. 000 being sale of Fixtures book value Rs.8,000 depreciation thereon to date of sale Rs.400

NOTES

7. The Manager is entitled to get a commission of 10% on the profit before charging such commission. Prepare his final accounts after taking into account the above adjustment.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2002 Dec.31	Closing Stock A/c Dr. To Trading A/c [Being the closing stock brought into account]		80,000.00		80,000.00	
1						
2	Stock Destroyed A/c Dr. To Trading A/c [Being the entry to record the stock destroyed]		10,000.00		10,000.00	
3	Insurance Company A/c Dr. To Stock Destroyed A/c [Being the claim admitted in full by the Insurance company]		10,000.00		10,000.00	
4	Stationery A/c Dr. To General Expenses A/c [Being the entry to remove purchase of stationery wrongly included in the latter-account]		900.00		900.00	
5	Outstanding Debtors A/c Dr. To Interest A/c [Being the interest due on loan advanced to Mahadevan @ 6% per month for 6 months.]		600.00		600.00	
5	Depreciation A/c Dr. To Machinery A/c To Furniture [Being the 10% Depreciation on Machinery and Furniture provided]		7,000.00		5,500.00 1,500.00	
6	Commission (due to manager A/c) Dr. To Outstanding Creditors A/c [Being the 10% commission due on net profits before charging such commission]		11,400.00		11,400.00	

	Rs.	
Furniture	30,000	
Less Sale of old Furniture		
@ book value	<u>8,000</u>	
	22,000	
Less Depreciation @ 10%		
For 6 months	<u>1,100</u>	
	<u>20,900</u>	

Solution :

ARASU

TRADING AND PROFIT AND LOSS ACCOUNT

For the half year ended 31st December 2002

	Rs.	Rs.		Rs.	Rs.
Opening Stock		62,400	By Goods sold	4,00,400	
To Goods Purchased	2,40,000		Less Sale of fixture		
To Less Purchases Returns			transferred to	5,000	
Factory Wages	30,000	2,10,000	fixtures	<u>3,95,000</u>	
Gross Profit-transferred to P & L A/c		20,000		20,000	3,75,400
		1,73,000	Less Sales Returns		<u>80,000</u>
		<u>4,65,400</u>	By Closing Stock		10,000
			By Stock destroyed		<u>4,65,400</u>
To Heating and Lighting					
To General Expenses		10,000	By Cross Profit b/d		1,73,000
Less: Purchases of Stationery	2,000		By Dividend Received		2,000
To Stationery use	900	1,100			
Purchases			Outstanding interest on loan to Mahadevan		900
Less Stock	900				
To Salaries	400	500			
To Loss on Sale of Fixtures		40,000			
To Depreciation Machinery @ 10%		2,600			
Furniture & Fixtures @ 10% (Rs. 1100+Rs. 400)	5,500				
To Commission due to	<u>1,500</u>	<u>7,000</u>			

NOTES

Manager (@ 10%(N.P.before charging such commission)Rs.1,14,400 Net Profit-transferred to Capital A/c					
			11,440		
			1,02,960		
			1,75,600		1,75,600

ARASU

BALANCE SHEET

As at December 2002

LIABILITIES			ASSETS		
	Rs.	Rs.'		Rs.	Rs.
Outstanding Creditors		11,440	Cash Balance		10,000
Commission due to Manager		48,000	Bill Received		30,000
Sundry Creditors		44,000	Sundry Debtors		1,00,000
Bills Accepted			Loan to Mahadevan		
Capital	2,00,000		Closing Stock		20,000
Add : Net Profit	1,02,960		Due from Insurance Co.,		80,000
	3,02,960		Machinery(1.1.2002)	1,00,000	
			Add:Addition(1.10.02)	20,000	
			Less Depreciation @ 10% on Rs.1,00,000 for 6months	1,20,000	
Less: Drawings	20,000	2,82,960	Rs.(5,000) and on Rs.20,000 for 3 months Rs.(500)	5,500	1,14,500
			Furniture and Fixtures	30,000	
			Less:Book value of the asset sold	8,000	
			Less:Depreciation @ 10% on Rs.22,000 for 6 months	22,000	
				1,100	20,900
			Outstanding Debtors		600
		3,86,400			3,86,400

Illustration: 7**NOTES**

	Rs.	Rs.
Stock at Commencement (1.7.2002)	10,000	
Capital		20,000
Telephone	3,000	
Bank O/D		1,000
Machinery	10,000	
Sundry Debtors	10,000	
Sales Returns	1,000	
Premises	21,000	
Purchases	20,000	
Drawings	5,000	
Mortgage		12,000
Bills Receivable	1,500	
Bills Payable		2,200
Sales	48,000	
Petty Cash	50	
Fittings	550	
Trade Expenses	880	
Wages	4,000	
Trade Creditors		3,700
	86,900	86,900

1. Mr. ANBU, an electrical dealer, used electrical goods and fittings for the shop for Rs.3, 000 out of purchases.
2. Goods worth Rs.200 returned by customers were included in purchases.
3. Machinery worth of Rs.1, 000 had been acquired during the period but the transaction was not passed through the books not was the machine paid for.
4. The Telephone was obtained during the beginning of the year under Own Your Telephone Scheme free for rent for 5 years.
5. Stock on 30.6.2003 Rs.11, 000
6. Included amongst the debtors Rs.1, 000 due from Babu and included amongst the creditors Rs.1, 000 to him.

NOTES

7. Mr. Anbu's wife works in the business and is allowed a salary of Rs.100 per month. This amount has been included in drawings.
8. It was discovered that the stock sheets (31.6.2002) i.e., Opening Stock on 1.7.2002 were overcast to extent of Rs.2,000
9. A commission of 10% on Net Profit is due to manager after deduction of his commission. Prepare his final accounts after taking into account the above adjustment.

ADJUSTMENT ENTRIES

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2003 June 31						
(1)	Fittings A/c Dr. To Purchases A/c [Being the entry to record the fittings used for the shop out of purchases]		3,000.00			3,000.00
(2)	Sales Returns A/c Dr. To Purchases A/c [Being the entry to transfer the value of goods returned by customers wrongly included in Purchases]		200.00			200.00
(3)	Machinery A/c Dr. To Creditors A/c [Being the entry to record the machine purchased on credit]		1,000.00			1,000.00
(4)	Prepaid Expenses A/c Dr. To Telephone A/c [being the prepaid telephone charges carried for the ensuring 4 years]		2,400.00			2,400.00
(5)	Closing Stock A/c Dr. To Trading A/c [Being the closing stock brought into account]		11,000.00			11,000.00
(6)	Sundry Creditors A/c Dr.		1,100.00			

	To Sundry Debtors A/c [Being the entry to adjust the amount due from Babu and due to him]			1,000.00
(7)	Salaries A/c Dr. To Drawings A/c [Being the entry to transfer the salary paid to Mrs. Anbu wrongly included in Drawings A/c]		1,200.00	1,200.00
(8)	Capital A/c Dr. To Opening Stock A/c [Being the excess valuation now adjusted]		2,000.00	2,000.00
(9)	Commission (Due to Manager) A/c Dr. To Outstanding Creditor A/c [Being the 10% commission due to Manager]		2,400.00	2,400.00

Assume that the Manager gets commission of Rs.10 and the profit left after deduction of such commission is Rs. = 100

Then the profit prior to commission must be Rs. = 110

$$\text{Thus} = 26,400 \times \frac{10}{110} = 2,400$$

ANBU'S

TRADING AND PROFIT & LOSS ACCOUNT

For the year ended 30th June 2003

	Rs.	Rs.		Rs.	Rs.
To Stock at commencement	10,000		By Sales	48,000	
Less: Over valuation	2,000	8,000	Less Sales Returns		
To Purchases	20,000		1,000 Goods returned by customers		
Less Good Etc., used for Shop	3,000		wrongly included in purchases not transferred 200	1,200	46,800
	17,000				
Less Goods Returns by Customers included			By Closing Stock		11,000

NOTES

wrongly	200	16,800		57,800
To Wages		4,000		
To Gross Profit C/d		29,000	By Gross Profit b/d	29,000
		57,800		
To Telephone	3,000			
Less Prepaid	2,400	600		
To Trade Expenses		800		
To Salary (paid to Mr. Anbu wrongly include in Drawings now transferred		1,200		
To Manager;s commission		2,400		
To NET PROFIT transferred to Capital A/c		24,000		
		29,000		29,000

ANBU'S BALANCE SHEET

As on 30th June 2003

LIABILITIES			ASSETS		
	Rs.	Rs.		Rs.	Rs.
Commission due to Manager		2,400	Petty Cash		50
Creditor for Machine		1,000	Bills Receivable		1,500
Trade Creditors	3,700		Sundry Debtors	10,000	
Less Amount due to Babu adjusted	1,000	2,700	Less: Amount due from Babu adjusted	1,000	9,000
Bill Payable		2,200	Closing Stock		11,000
Bank O/d		1,000	Prepaid Expenses (Telephone)		2,400
Mortgage		12,000	Machinery	10,000	
Capital	20,000		Add: Addition and recorded	1,000	
Less Over valuation of Stock	2,000		Premises		11,000
	18,000		Fittings	500	21,000
Add Net Profit	24,000		Add: Addition (goods Used out of Purchases)		
	42,000			3,000	3,550
Less Drawings 5,000					
Salary paid to Mrs. Anbu wrongly Included 1,200	3,800	38,200			
		59,500			59,500

Illustration: 8

The following are the closing balances in the ledger of M/s. Suresh for the ended 31st March 2003.

	Rs.
Discount	2,500
Carriage	22,600
Rent, Taxes and Rate	12,400
Printing and Stationery	2,600
Purchases of Raw Material	3,49,800
Sales	5,60,000
Stock of Raw Material (1.4.02)	1,24,400
Stock on finished goods (1.4.02)	63,800
Bank Loan	1,15,600
Plant and Machinery	1,16,900
Capital Account	2,53,000
Factory Wages	59,700
Sundry Creditors	73,800
Goodwill Account	25,000
Bad Debts	4,500
Advertisements	9,600
Miscellaneous Expenses	3,300
Interest Paid	6,300
Loan from Sri Prakash	30,000
Furniture and Fixtures	28,600
Drawings A/c of Mr.Suresh	36,500
Sundry Debtors	83,600
Fuel and Coal	11,200
Income Tax Account	13,700
Factory Power Account	22,900

Insurance (fire)	2,200
Staff Salaries	12,700
Electricity	2,300
Reserve for Doubtful Debts	2,600
Cash on Hand	5,600
Cash at Bank	12,300

Prepare Manufacturing, Trading and Profit and Loss Account for the year ending 31st March, 2003 and Balance Sheet of Mr. Suresh after taking into account the following information.

1. Insurance is paid up to 30th June, 2003.
2. Interest is payable at 7 percent p.a. on Bank Loan and 9 percent on the Loan taken from Shri. Prakash. Interest is not paid or payable on any other account. Both the Loan has been outstanding since 31st March 2002.
3. Carriage includes Rs.12, 400 towards Outward Carriage.
4. Stock as at 31.3.2003 Raw Materials Rs.46, 900 and finished goods Rs.1, 49,900
5. The following provisions have to be made:
 - a) Depreciation at 10 percent on Plant and Machinery and Furniture and Fixtures. There have been no returns on sales on purchases during the year.
 - b) 5 percent of debts outstanding is to be provided towards Bad and doubtful debts.
6. The following expenses are outstanding and payable

	Rs.
a) Salaries	1,100
b) Rent	900

c) Electricity 200

d) Factory Power 2,100

7. Good costing Rs.2, 400 were given free to public as samples by way of Adjustment. No entries had been made in books in this regard.

ADJUSTMENTS ENTRIES

Date	Particulars	L.F.	Dr.	Cr.
			Rs. P.	Rs. P.
2003 Mar.31				
1	Prepaid Expenses Dr. To Insurance A/c [Being the prepaid insurance adjusted]		400.00	400.00
2	Interest on Loan A/c Dr. To Outstanding Creditors A/c [Being the interest on Bank Loan @7% and Prakash's loan @9% adjusted.]		4,492.00	4,492.00
3	Outward Carriage A/c Dr. To Carriage A/c [Being the amount transferred to the former A/c]		12,400.00	12,400.00
4	Closing Stock A/c Dr. To Manufacturing A/c To Trading A/c [Being the closing stock of raw materials and finished goods brought into account]		1,96,800.00	46,900.00 1,49,900.00
5	Depreciation A/c Dr. To Plant and Machinery A/c To Furniture and Fixtures A/c [Being the depreciation @ 10% provided for]		14,550.00	11,690.00 2,860.00
6	Salaries A/c Dr. Rent A/c Dr. Electricity A/c Dr. Factory Power A/c Dr. To Outstanding Creditors A/c		1,100.00 900.00 200.00 2,100.00	

NOTES

7	(Being the outstanding expenses adjusted]			4,300.00
	Advertisement A/c Dr.		2,400.00	
	To Purchases A/c			2,400.00
	[Being the entry to record the distribution of goods free to the public as samples]			

MANUFACTURING TRADING AND PROFIT AND LOSS ACCOUNT

For the year ending 31st March 2003

	Rs.	Rs.		Rs.
To Opening Stock of Raw Materials	1,24,400		By Cost of Finished Goods transferred to Trading A/c	5,45,090
Add: Purchase of Materials	3,49,800			
	4,74,200			
Less: Closing Stock of Materials	49,900	4,27,300		
To Carriage	22,600			
Less: Outward Charges	12,400	10,200		
To Factory Wages		59,700		
To Fuel and Coal		11,200		
To Factory Power	22,900			
Add: Outstanding	2,100	25,000		
To Depreciation on Plant & Machinery		11,690		
		5,45,090		5,45,090
To Opening Stock of finished goods	68,800		By Sales	5,60,000
Less: Samples distributed	2,400	61,400	By Closing Stock of Finished Goods	1,49,900
To Cost of finished goods Transferred from Manufacturing A/c		5,45,090		
Gross Profit's		1,03,410		
		7,09,900		7,09,900
To Outstanding Charges		12,400		
To Discounts		2,500		
To Rent and Taxes	12,400		By Gross Profit	1,03,410
Add Outstanding	900	13,300		
To Printing and Stationery	2,600			
To Advertisement	9,600			
Add: Free Samples	2,400	14,600		
To Miscellaneous		3,300		
To Insurance (fire)	2,200			
Less : Prepaid	440	1,760		
To Interest	6,300			

Add: Ourstanding	4,492	10,792		
Interest on Bank Loan at 7% 8.92				
Add: Interest to Shri Prakash's Loan at 9%	2,700			
To Staff Salaries	12,700			
Add: Outstanding	1,100	13,800		
To Electricity	2,300			
Add: Outstanding	200	2,500		
To Reserve for Doubtful Debts				
New Reserve	4,180			
Add: Bad Debts	4,500			
	8,650			
Less: Old Reserve	2,600	6,080		
To Depreciation Furniture & Fitting at 10%		2,860		
Net Profit transferred		19,518		
Capital A/c		1,03,410		1,03,410

The final account for this problem related to the period starting from 1st of April 2002 to 31st March 2003, insurance has been paid upto 30th June. So, it is assumed that Insurance Rs.2, 200 related to 15 months up to 30.6.2003.

SURESH

BALANCE SHEET

As at 31st March 2003

LIABILITIES			ASSETS		
	Rs.'	Rs.		Rs.	Rs.
Outstanding Creditors		8,792	Cash on hand		5,600
Salaries	1,100		Cash at Bank		12,300
Rent	900		Sundry Debtors	83,600	
Electricity	200		Less: Reserve for Doubtful Debts		
Factory Power	2,100		At 5%	4,180	79,420
Interest on Bank Loan & Shri Prakash's Loan	10,792		Closing Stock		

NOTES

Less Already Paid	6,300	4,492		Raw Materials	46,900	
Sundry Creditors			73,800	Finished Goods	1,49,900	1,96,800
Bank overdraft			1,15,600	Prepaid Expenses (Insurance)		400
Loan from Shri Prakash				Plant and Machinery	1,16,900	
Capital		2,53,000		Less Depreciation at 10%	11,690	1,05,210
Add: Net Profit		19,518		Furniture and Fixtures	28,600	
Less Drawing	36,500			Less Depreciation at 10%	2,860	25,740
Income Tax	13,700	50,200	2,22,318	Goodwill		25,000
			4,50,510			4,50,510

EXERCISE

1. From The following particulars you are required to prepare the final accounts of Ramakrishna as on 31st December 2002

	Rs.		Rs.
Salaries & Wages	21,000	Capital	80,000
Cash at Bank	20,500	Creditors	10,000
Cash in hand	6,200	Sales	1,20,000
Insurance	700	Returned outward	1,000
Drawings	6,000	Provision for Doubtful	
Plant & Machinery 1.1.2002	20,000	Debts	400
Additions 1.7.2002	5,000	Discounts	800
		Rent of premises sublet for	
Stock 1.1.2002	15,000	The year ended 30 th June	
Purchases	82,000	2003	1,200
Returns Inwards	2,000		
Debtors	20,600		
Furniture	5,000		
Duty & Clearing	2,000		
Carriage out	500		
Rent rate & taxes	4,600		
Printing	800		
Trade Expenses	400		
Postage	800		
	<u>2,13,400</u>		<u>2,13,400</u>

Adjustments:

1. Stock on 31.12.2002 was valued at Rs.1, 46,000
2. A fire occurred on 24.12.2002 in the premises and stock of the value of Rs.6,000 was destroyed. It was however fully insured and insurer admitted the claim in full.
3. Write off Rs.600 as Bad Debts. The provision for Doubtful Debts is to be maintained @5%
4. Provide for Depreciation on Furniture @5% and on Plant @ 10% p.a.
5. Insurance prepaid was Rs.200

NOTES

(Ans: GP Rs.40, 600, NP Rs.9, 400 B.S.Rs.94, 000)

Hints:

1. Depreciation on Plant @ 10% on Rs.20, 000 for one year and on Rs.5,000 for 6 months
2. Rent received in-advance for 6 months Rs.600
3. Debit Stock Destroyed A/c and Credit Trading A/c with Rs.6, 000
4. To record the claim due from Insurance Company debit Insurance Co., A/c and credit Stock Destroyed (Good) A/c with Rs. 6,500
5. Provision for Doubtful debts shows be calculated on the amount of Good Debtors (i.e.) Rs.20,000 and not Rs.20,600.
2. From the following Trial Balance of Kavi Arasu on 31st December 2002 prepare the Trading, Profit and Loss Account and the Balance Sheet as on that date after making necessary adjustments.

	Rs.		Rs.
Book Debts	2,000	Trade Creditors	1,400
Drawing	420	Capital	2,500
Stock (1.1.2002)	1,200	Sales	7,302
Purchases	6,200	Bank Balances	290
Sales Return	60	Provision for Doubtful	
		Debts	210
Wages	900		
General Expenses	350		
Fixtures & Equipments	400		
Bad Debts	172		
	<u>11,702</u>		<u>11,702</u>

Adjustments:

1. Closing Stock Rs.1,470
2. Stock destroyed by fire but covered by Insurance yet paid Rs.150
3. Provide 20% on Book Debts.
4. Included in Sales is Rs.50 being sale of Fixtures book value Rs.80 Depreciation thereon to date of Sale Rs.5
5. Expenses accruing Rs.25.
6. Included in purchases is a Fixture for Rs.13 bought on 31st Dec. 2002
7. Write off 10% Depreciation on Fixture and Equipment

(And: GP Rs.525; Net Loss Rs.274; B/s Rs.3,521)

Hints:

1. Books Debts i.e., Sundry Debtors
2. Debit Fixture A/c and Credit Purchases A/c with Rs.13. Remove Rs.13 from purchases and show an addition to Fixture.
3. Debit sales A/c and credit Fixtures and Equipments A/c with Rs.50 (being value of the asset sold) i.e. Remove Rs.50 both Sales A/c and Fixture and Equipment ac/. Depreciation @ 10% on Fixture and Equipments should be calculated on Rs.320 and not Rs.400.

10

This amount on Rs.32 ($320 \times \frac{10}{100}$) the depreciation on

100

The asset sold Rs.5 should be transferred to the P & L A/c. Total depreciation Rs.37

No depreciation is to be provided on addition of fixtures as it was bought on the last day of the year viz., 31.12.2002.

Rs.

Fixtures and Equipments	400
Less Book value fixtures sold	80
	320
Less: Dep @ 10% on Rs.320	32
	288
Add : Additions on 31.12.2002	13
	301
Expenses accruing i.e. unpaid	

3. From the following Trial Balance of Mr. Ramesh as on 30th September 2003 you are required to prepare a Trading and Profit and Loss Account for the year ended 30th September, 2003 and a Balance Sheet as at that date after making necessary adjustment.

	Rs.	Rs.
R.Ramesh's Capital Account		1,00,000
R.Ramesh's Drawings Account	12,000	
Land and Building	60,000	
Plant and Machinery	20,000	
Furniture and Fixtures	5,000	
Less hold Premises (Lease to run for 5 years)		
From 1.10.2002	30,000	
Sales		1,40,000
Returns Outwards		4,000
Sundry Debtors	18,400	
Loan from David @ 6% taken on 1.1.2003		30,000
Purchases	80,000	
Returns Inwards	5,000	

Freight and duty	10,000	
Sundry Expenses	600	
Printing and Stationery	500	
Insurance Charges	1,000	
Reserve for Doubtful Debts	1,000	
Reserve for Discount on Debtors	380	
Bad Debts	400	
Profit on Textiles Department	10,000	
Stock of General Goods on 1.10.2002	21,300	
Salaries and Wages	18,500	
Sundry Creditors	12,000	
Trade Expenses	800	
Stock of Textiles Goods on 30.9.2003	8,000	
Cash at Bank	4,600	
Cash in hand	1,280	
	<u>2,97,380</u>	<u>2,97,380</u>

Adjustments:

1. The Stock on September 2003 was valued at Rs.2,73,000
2. On 23rd September 2003 a fire broke out and destroyed stock of value of Rs.10,000. The Insurance Company admitted the claim for loss of stock to the Value of Rs.6,000 only and paid the amount on 10th October, 2003.
3. Of the Sundry Debtors Rs.400 are be and should be written off. The Reserve for Doubtful Debts should be maintained at 5% on Debtors and the Reserve for Discount on Debtors at 5% on Debtors. Also maintain a Reserve for Discount on creditors at 2%
4. Goods of the value of Rs.6,000 had been received on 27th September 2003 but the purchase Invoice was omitted to be recorded in the Purchases Book.
5. R.Ramesh had utilized good worth Rs.2,000 for his personal use but no record was made of it.

NOTES

6. Depreciation on Land and Buildings at 2% p.a. Plant and Machinery at 20% p.a. and Furniture and Fixture at 5% p.a.

7. Prepaid Insurance was Rs.200

(Ans.: G.P.Rs.61, 000; N.P.Rs.32, 698; B/s Rs.1, 67,688)

Hints:

1. Lease for 5 year from 1.10.2002 Rs.30, 000
Depreciation for the year from 1.10.2002 to 30.9.2003 Rs. 6,000
2. Loan Interest @ 6% on Rs.30, 000 for 9 months from 1.1.2003 to 30.09.2003 Rs. 1,350
3. Profit on Textiles Department Transfer to the Credit side of P & L A/c Rs.10,000
4. Stock of General goods 1.10.2002 i.e., Opening Stock Rs.21,300
5. Trade Expenses P & L A/c Rs. 800
6. Stock of Textiles goods 30.9.2003 Asset side Since it is a Closing Stock.
7. Goods destroyed should be credited to Trading A/c Rs.10,000 but Rs.4,000 should be debited to P & L A/c (being irrecoverable and Rs.6,000 should be shown as an asset in the Balance Sheet (as recoverable)
8. Additional Bad Debts Rs.400 should deducted from total Sundry Debtors Rs.18,400. Then 5% Reserve should be calculated on the Good Debtors i.e., Rs.18,000. Lastly 2% Reserve for Discount on Debtors should be calculated on the balancing debtors.
9. Goods bought on 27.9.2003 should be added in purchases and the sundry creditors should be increased by Rs.6,000
10. Reserve for Discount on Sundry Creditors should be calculated Rs.18,000 [i.e.] Rs.12,000, 6,000 (Additional Creditors)
11. Goods used by R. Ramesh Rs.2,000 should be deducted from purchase & add to Drawings.

4. From the following information prepare the final accounts of Mr. Somu.

TRIAL BALANCE AS ON 31ST MARCH 2003.

Debit Balances:	Rs.	Credit Balance	Rs.
Plant and Machinery	80,000	Capital	50,000
Purchases	60,000	Sales	1,77,000
Returns	1,000	Returns	750
Opening Stock	30,000	Discount	800
Discount	350	Sundry Crs.	25,000
Bank Charges	75	Interest	525
Sundry Drs.	45,000		
Salaries	6,800		
Wages	10,000		
Carriage in	750		
Carriage out	1,200		
Rent, Rates & Taxes	10,000		
Advertisements	2,000		
Cash in hand	900		
Cash at bank	6,000		
	<u>2,54,075</u>		<u>2,54,075</u>

Closing Stock was Rs.35,000

5. State the Differences between Trial Balance and Balance Sheet.

