



MANONMANIAM SUNDARANAR UNIVERSITY

**DIRECTORATE OF DISTANCE AND CONTINUING EDUCATION
TIRUNELVELI-627012, TAMILNADU**

BBA Second Year (Third Semester)

FINANCIAL ACCOUNTING

(From the Academic Year 2021-22)



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FINANCIAL ACCOUNTING

CourseObjective:

To enable students to

1. Understand the significance of accounting concepts and conventions in the preparation and presentation of financial reports.
2. Prepare financial statements of the company.
3. Analyze and interpret financial statements of a company.

UNIT-1:INTRODUCTION

Meaning and Scope of Accounting - Need for Accounting - Nature and Objectives of Accounting - Developing of Accounting - Book Keeping and Accounting. Accounting Concepts and Conventions - Accounting Standard in India- IFRS.

UNIT-II: BOOKS OF ACCOUNTS

Double Entry System of Book-Keeping - Journal - Rules of Debit and Credit - Ledger Posting - Rules Regarding Posting - Relationship Between Journal and Ledger - Trial Balance.

UNIT-III: SUBSIDIARY BOOKS

Benefits Basic Documents - Preparation of Purchase Book, Sales Book-Purchase Return Book-Sales Return Book-Cash Book-Single, Double and Triple Column Cash Book-Petty Cash Book.

UNIT-IV: FINAL ACCOUNTS

Manufacturing Account-Trading Accounts Profit and Loss A/C Balance Sheet - Adjustment entries.

UNIT-V:DEPRECIATION ACCOUNTING

Meaning-Causes - Objectives - Methods of Depreciation-Reserves and Provisions

(Marks:Theory 40% and Problems60%)

TEXT BOOKS:

1. Gupta, R.I. and Radhaswamy M., Financial Accounting.- Sultan and Chand Sons- New Delhi.
2. Maheswari, SN and Maheshwary, S.K., Fundamental of Accounting. Vikas Publications

REFERENCE BOOKS:

- i. T.S.Reddy&Y.Hariprasad Reddy, Financial & Management Accounting. Margham Publications, Chennai
- ii. M.C.Shukla, T.S.Grewal&S.C.Gupta, Advanced Accounts, S.Chand, New Delhi

- iii. S.Pandian, Accounting for Managers, Ane Book Pvt.Ltd, New Delhi
- iv. R.S.N.Pillai&Bagavathi, Management accounting, S.Chand, New Delhi
- v. P. C. Tulsian, Financial Accounting-Pearson Education, New Delhi

WEB RESOURCES:

- 1. <https://www.swayamprabha.gov.in/>
- 2. <https://swayam.gov.in/>
- 3. <https://epgp.inflibnet.ac.in/>
- 4. <https://www.icai.org/>

FINANCIAL ACCOUNTING

CONTENT

UNIT - I	BASIC CONCEPT OF ACCOUNTING	1
UNIT- II	BOOKS OF ACCOUNTS	25
UNIT - III	SUBSIDIARY BOOKS	46
UNIT- IV	FINAL ACCOUNTS	90
UNIT - V	DEPRECIATION ACCOUNTING	126



UNIT - I

BASIC CONCEPT OF ACCOUNTING

INTRODUCTION:

A businessman invests capital with objective of making profit and thereby increasing his resources. He incurs various expenses like salaries, rent and stationery to operate his business. He receives income from different sources like Commission, interest and discount. He deals with several persons in the course of buying and selling of goods, purchasing and selling of assets and borrowing money for financing for financing the business. He acquires various properties and assets like machinery, furniture, building to generate revenue.

Effective management of business requires control over expenses to reduce the cost of operation and to make the business profitable. Assets must be properly maintained to increase their productivity. Liabilities of a business have to be repaid in due time. Dealings with customers and suppliers must be managed properly to keep satisfied. In order to maintain properly in good condition, to repay debts in time, to reduce the expenses and to increase sales, the businessman requires complete information about all his business transactions.

In practice, it is impossible for any businessman to memorize and recollect all his business dealings. Moreover, he will be interested in knowing at the end of each year (i) what he owns? (ii) what he owes? (iii) how much profit he has earned? (iv) what his financial position is? To relieve businessmen from the burden of memorizing all the business dealings and for providing necessary information, Accounting was developed.

Businessmen also require accounting records to submit in courts to prove their claims or to defend in courts against made by outsiders. They are required to produce business records to tax authorities whenever demanded. Similarly, financiers require accounting records of businessmen to decide about sanctioning of loans. Thus, transactions relating to business have become so important that their recording has become a necessity.

ACCOUNTING – DEFINITION:

According to the American Institute of Certified Public Accountant defined



Accounting as “Accounting is the art of recording, classifying and summarizing in a significant manner and in term of Money, transactions and events which are, in part at least, of a financial character and interpreting the results thereof.”

American Accounting Association defined accounting as “the process of identifying, measuring and communicating economic information to permit informed judgment and decisions by users of the information”.

This definition highlights in a logical sequence the different steps in the accounting process and some important attributes of accounting.

Scope of Accounting

The scope of accounting includes all financial transactions and activities of a company. It includes recording, classifying, and summarizing financial information to provide accurate and timely reports.

Accounting tracks the performance of a business and helps make crucial decisions about its future. It can measure profitability, liquidity, and solvency. Financial statements prepared by accountants can also assess the creditworthiness of a company.

To make sure that your accounting system works well for your business, it's imperative to understand what accounting is. Accounting is the process of tracking financial information for a company. It includes understanding what transactions and activities need to be included in your books, as well as which financial reports you should be preparing.

Attributes And Steps Of Accounting:

1. **Recording :** Systematic recording of business transactions is the first step in the accounting process. Each and every transaction is recorded as and when it occurs, in chronological order. Every entry recorded has to be supported by reliable documentary evidence. Recording of business transactions is usually done in journal or in subsidiary books which are ‘ books of original entry’.
2. **Classification:** It is the process of grouping transactions or entries on a predetermined basis. The classification takes the form of ‘accounts’ in a separate book known as Ledger. Separate accounts are opened for each expense, income, property , liability and persons with whom the



business has dealings. Classification facilitates segregation of numerous business transactions into identifiable groups.

3. **Summarising :** The classified data in the ledger is presented periodically in a manner which is understandable and useful to the owners and other interested parties. Summarising takes place in the form of trial balance , trading account, profit and loss account and balance sheet. The trial balance ensures the arithmetical accuracy of the recording and classification process. The trading account reveals the gross profit of the business . Profit and loss account shows net profit or loss for the accounting period. The balance sheet portrays the financial position of the business.
4. **Significant manner:** The accounting process of recording , classifying and summarizing must be carried on in a significant manner . Each business has its own peculiarities, special problems and particular requirements. The management of the business needs specific types of information for controlling and decision-making purposes. Sales and purchases may have to be shown for each product , division , department , and branch separately. Profit or loss may be required independently for each product or service.
5. **In terms of money :** All business transactions have to be recorded in terms of money. It is the medium through which all the business transactions are expressed. Land and buildings in square feet, furniture and fixtures in number, stock in units are all recorded as per their monetary values. ‘Money measurement ‘ is the basis for accounting.
6. **Transactions and events of financial character:** All those business transactions and events which are financial in character are recorded in accounts. All the events , dealings and happenings which have to no financial effect are completely ignored in the accounting process. For example, working conditions, skilled work force, sales policies , employees, morale etc., are all important for a business. But they have no ‘financial character’ and are omitted from accounting process.
7. **Interpreting the results:** Interpretation of the results is needed for various purposes. The trends observed in sales, purchases, expenses etc., are useful for future planning of operations. Data about customers and suppliers have to be interpreted to decide about credit policies. The owners are interested in the amount and growth of profit. The creditors are interested in the liquidity and stability of the business.

Interpretation is usually done through Ratios and Flow statements. They are useful in evaluating past performance and providing guidance for future plans and operations.



NEED FOR ACCOUNTING

Reliable Records

Transactions cannot be stored up in memory even in the case of small shops. The reliable record of transaction is necessary for reference at any time. Since all the transactions are recorded in the books, there is no need to rely on memory.

Calculation of Profit or Loss

The objective of any business is to earn profit. Therefore, the owner wishes to find out the profit or loss in his business at any time. With the help of accounting information, the profit and loss account is prepared to find out profit and loss of the business.

Calculation of Dues

The businessman has to know, how much others have to pay him and how much he has to pay others. This information can be gathered with the help of proper accounting records.

Prevention of Errors and Frauds

Proper accounting not only prevents and discovers errors but also prevents and discovers frauds.

Control over assets

The owner has to keep a check over the assets and find out the values year after year. Accounting provides such information which helps the owners and the management to make use of the assets in the best possible manner.

Ascertainment of the growth of business

When a owner prepares financial statements for several years, he is in a position to make year to year comparison. This will enable him to ascertain the growth of his business.

Fixing the selling price

Accounting information is essential for determining the selling price of the goods produced.

Taxation



For the income tax and sales tax purposes, the accounting information is essential.

BRANCHES OF ACCOUNTING

The Modern business world has become highly competitive and technology oriented. Management of the business units has become highly complex, needing varied types of information. To satisfy the additional demand of management for information, several new branches of accounting have been developed.

1. **Financial Accounting** : The accounting for revenues, expenses , assets and liabilities that is commonly carried on the general offices of business is known as Financial Accounting. The financial accounting information is expressed in two main types of financial statements, viz:
 - (i) Profit & Loss Account(showing the incomes and expenses of the accounting period to ascertain the profit or loss)
 - (ii) The Balance sheet (showing assets and liabilities, revealing financial position as on that date)

The owners, creditors, management, employees, financiers etc., make use of information provided by financial accounting.

2. **Cost Accounting** : It is that branch of accounting which deals with classification, recording , allocation, summarization of current and prospective cost. It determines cost of production and distribution by departments, functions, products etc. Cost accounting is essential for pricing of products and services and for cost reduction and cost control. Cost accounting data is useful to the management of the business ; outsiders are not usually provided with costing data.
3. **Management Accounting** : It is that branch of accounting which is meant exclusively for managerial decision making . It provides necessary information to the management for discharging its functions of planning, organizing, co-ordinating, directing and controlling. It usually provides data on the funds and cash flows, investment projects, preparation and implementation of budgets etc. Almost all the policy decisions of management are made on the basis of primary data provided by management accounting.



4. **Social Responsibility Accounting:** With the increasing awareness about the social issues and involvement of the various business houses in view to work for profit and support a cause along with the advancement in the laws relating the CSR there has been a significant increase in the spending towards social causes. The companies who are spending towards CSR are highly interested in knowing whether the amount spent by them is able to fulfill the cause and generate the impact it had expected through the spending. The measurement of the social benefits created and the lives impacted is the main objective of the Social Responsibility Accounting. For Example: If Company ABC had spent Rs.1.00 Cr during F.Y.2017-2018 for promoting education among the low income kids. It would like to know the number of kids who got enrolled in the schools via their programs for which they had spent amount of Rs.1.00 Cr.
5. **Human Resource Accounting:** Of all the expenditure incurred by the businesses they can be measured by using the standards, measurements and valuation principles provided by various laws, regulations and AS. Except for the Human Resource, which is the only expenditure incurred by the company to develop and maintain the human resource which will be able to provide the company benefits across the years. However, it is written off as expense in the year it is incurred. Human Resource Accounting attempts to identify measure and report the investment made in the Human Resource of the entity.

FUNCTIONS OF ACCOUNTING

The functions of accounting include the systemic tracking, storing, recording, analysing, summarising and reporting of a company's financial transactions. Through the functions of the accounting department, the company can maintain a fiscal history that they can make accessible for audits. They can also use it to prepare reports, create budgets, reduce costs, increase profits, avail growth opportunities, assess future expenditure requirements and make financial predictions.

Keeping financial records: Accounting helps businesses maintain an accurate and up-to-date record of the day-to-day financial transactions of the company, such as supply purchases, product sales, receipts and payments.



Monitoring financial transactions: Accountants may track multiple financial transactions related to payments due to the company to ensure it receives the revenue and remains profitable.

Making Bill payments: Accounting involves checking invoices to ensure the legitimacy of the charges, setting payment dates and paying the bills that the company owes to various vendors and suppliers.

Paying employee salaries: Companies can use accounting to make payroll payments from company funds, manage employee benefits and issue employee work-related bonuses.

Keeping digital records: Accounting may involve creating, maintaining and updating digital accounting systems to store and calculate the company's financial data.

Writing financial reports: Accounting involves preparing detailed quarterly and annual financial reports about the company's assets, profits and losses for internal and external stakeholders.

Maintaining fiscal history: Accountants assist with creating, documenting and storing the fiscal history of the company's transactions and making it available for audits and assessments.

Achieving business goals: An accountant can analyse financial data to formulate and implement comprehensive financial policies and strategies to advance the company's business goals.

Preparing Budgets: The accounts department may reference the company's financial data to prepare the overall company budget, the department budgets and the project budgets.

Making financial projections: Accounting involves analysing the company's available financial resources, expected revenues and business goals and using this information to predict future business expansion and growth.

Auditing finances: Accountants may conduct financial audits of the company, identify accounting discrepancies and implement corrective solutions



Assessing Financial resources: Companies can use accounting to identify the financial weaknesses and strengths of the organisation, determine how to counter weaknesses and boost strengths and implement appropriate strategies.

Reviewing Performances: Accounting involves performing regular financial reviews of the company's departments to assess their performance and make changes to reduce waste, increase productivity and streamline expenses.

Complying Legal requirements: Accountants make sure the company complies with industry and government rules, regulations and policies related to taxation, financial reporting and employee wages.

Preventing mismanagement: The accounting department can keep accurate track of the company's financial transactions to ensure no mismanagement or wastage of money occurs in the company.

Ensuring Vigilance Fraud: Accounting includes implementing strong security measures to protect the company assets against data breaches and internal and external fraud

BOOK KEEPING – MEANING AND DEFINITION

Book keeping is an art and science of recording business transactions in terms of money, in the books of accounts with a view to arriving at the final state of the business at any date. Few definitions of book-keeping are stated below:

I.C. Cropper defines Book-keeping as follows: “Book-keeping may be described as the science of recording transactions 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 a statistical procedure for the collection, classification and summarization of financial information.

BOOK –KEEPING Vs ACCOUNTING

Book – keeping is concerned with the recording of business transactions in a systematic manner. This work is mechanical and repetitive in nature. It does not need



specialized skill and knowledge. It is usually entrusted to the journal 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 is also responsible for posting every transaction to the ledger. The debit and credit aspects are posted separately to the respective accounts with the correct amount. In the ledger, the date of the transaction, the journal folio number and the amount are clearly shown whenever a posting is made into an account.

Balancing of all the ledger accounts and subsidiary books at the end of the accounting year, is another major work for book – keeping . Each account in the ledger has to be balanced by totaling both sides of the account and the balance may be debit balance or credit balance depending on which side of the account shows larger total amount. Balances have to be carried forward to the subsequent accounting period.

Extracting Trial Balance is also a task for book –keeping. The Trial Balance ensures arithmetical accuracy of the accounts maintained. When there is any difference between the debits and credits, verifying the ledger accounts, postings and balancing is essential to identify mistakes and adjust the trial balance.

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 te 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 ascertaining profit or loss for the period, and showing the financial position of the business. Examples are depreciation of fixed assets, outstanding and prepaid expenses, accrued incomes, provisions etc. Trading and profit & loss account is to be prepared in a systematic manner on the basis of generally accepted accounting practices. Similarly, Balance sheet has to be prepared, portraying true and fair picture of 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.

INA 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 businesses, both the functions may be performed by a single accountant. In bigger firms, the accounts department may be divided into book keeping and accounting sections.

METHODS OF ACCOUNTING

Basically all methods of accounting are classified under two headings:-

1. Single entry system
2. Double entry system

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.



Double entry system

This system was invented by an Italian named Juco 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 incoming 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 '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.

TYPES OF ACCOUNTS

1. PERSONAL ACCOUNTS:

An account of each person, or company with which the business deals or Accounts of persons with whom the business has dealings are known as personal Accounts .

(a) Natural Persons: The name of an individual - customers or suppliers.

(e.g) Murugan 's account , Raja's account

(b) Artificial persons or legal bodies: Firms's accounts, limited companies' accounts, educational institutions' accounts, bank account, co-operative society account etc., are known as artificial persons' accounts.

(c) Represetative personal accounts: All accounts representing outstanding expenses and accrued or prepaid incomes are personal accounts.

(e.g.) Prepaid insurance, outstanding wages, salary , rent etc.

2. REAL ACCOUNTS:

Accounts in which the business records the records the real things owned by it. i.e., assets of the business are known as real accounts. Real accounts are of two types.

a) Tangible Real Accounts: Building, Furniture , Machinery , Cash etc.,

b) In **Tangible Real Accounts: Trademark , goodwill , patents and copyright etc.,**



3. NOMINAL ACCOUNTS:

It relates to the items which exist in name only. Expenses, incomes etc., are there in business activities. Accounts which record expenses, losses, incomes and gains of the business are known as nominal accounts.

e.g., rent A/c, salaries A/c, telephone charges A/c, postage A/c, advertising A/c, commission received A/c, interest received A/c.

ACCOUNTING RULES

The benefit receiving aspect and benefit giving aspect. A transaction should be divided into two aspects.

1. Debit aspect
2. Credit aspect

The rules for making entries under double entry system can be summarized as follows:-

1.	Personal Accounts	Debit the receiver
		Credit the giver
2.	Real Accounts	Debit what comes in
		Credit what goes out
3.	Nominal Accounts	Debit all expenses and losses
		Credit all incomes and gains

ACCOUNTING CONCEPTS

The term accounting concepts refer to the basic assumption and conditions upon which the science of Accounting is based. There is no authoritative list of these concepts. In other words, concept means such ideas which are compiled with different accounting procedures. E.g. Appropriation and charge, reserve and provisions, depletion and amortization etc. The following are some of the important accounting concepts.

1. Separate Entity Concept
2. Dual Aspect Concept
3. Going Concern Concept
4. Money Measurement Concept
5. Cost Concept



6. Accounting Period Concept
7. Realization Concept
8. Matching Concept
9. Accrual Concept
10. Objective Concept

1. Separate Entity Concept

For accounting purposes, a business is considered to be different from the persons who own it. The accounting system deals only with the accounts of the firm and not that of the owners. Otherwise, the affairs of the business would get mixed up with the affairs of the owners. The balance sheet of a sole trader does not disclose the private assets of its owner, even though such assets might be claimed by the creditors in case of loss in the business. Thus, this concept prescribes the boundaries for recording and reporting the economic information of an enterprise. This concept also helps to record in the books of the firm, the transactions that take place between the business and its owners. Moreover, when a large business is divided into different departments or divisions, this principle of separate entity helps to measure the efficiency of such departments.

2. Dual Aspect Concept

Modern accounting is based on the dual aspect concept. For every debit, there should be a corresponding credit. Hence, the total of the debits will always be equal to the total of the credits. Further, assets of a firm are purchased by the funds provided by the owners and the creditors. Therefore, the total of the assets should always be equal to the total of the liabilities or equities. Equities are the claims of the owners and outsiders on the assets of the firms. Hence, the equation,

$$\text{Assets} = \text{Liabilities} + \text{Capital (or) Assets} - \text{Liabilities} = \text{Capital}$$

3. Going Concern Concept

The general assumption is that a business will exist for a long time to come and will not be liquidated in the near future. People will not like to deal with a business that is to be closed down. Suppliers may not provide goods, workers may not provide their services and financial institutions may not provide credit facilities. If a business is to be closed



down, its assets should be valued at current realizable values. But this is not so in case of going concern. Since the assets are meant for use, they are valued at their original cost only.

4. Money Measurement Concept

All the transactions of a business are recorded only in terms of money. Because, money is the medium of exchange and a common measure of value. This serves as a measuring rod with which different kinds of resources are measured. For instance, a business may own 2000 square meter of building space, cash Rs.1,00,000, raw materials of 5,000 tons, motor trucks 5 numbers, motor cars 3 numbers and 100 sets of table and chair. All these items cannot be added together to give a meaningful information. However, when the value of all these assets are expressed in terms of rupees or dollars, then they can be added together to give a meaningful information and a clear picture about the total value of the business.

5. Cost Concept

The meaning of this concept is that an asset will be recorded at its cost, that is price paid or to be paid for acquiring it. Any change in the market value of the asset is not recorded. The market value may fluctuate from time to time and create confusion if the change in value is recorded. The change is unrealized, hence they need to be recorded.

When the value of an asset is reduced due to its constant use, due to wear and becoming obsolescence, then they are shown as depreciation and reduced from the original cost of the asset.

6. Accounting Period Concept

The business activity is a continuous process and we cannot wait till the end of the business to evaluate its financial position. Hence for reporting purpose, the entire life of a business is divided into different accounting period. A period normally may cover 12 months. A profit and loss account is prepared once in a year and the balance sheet is prepared as on the closing date of the accounting period.

7. Realisation Concept

This concept is related to realization of revenue which arises from sale of goods or services. But the question arises as to when the revenue should be recognized and how



much of it should be taken into account. One must ascertain the revenue of the current year, past year and of the next year. Revenue arises when title to goods is transferred or when services is rendered to the customer. In the case of a credit sale, revenue arises when the sale is made, and not when the cash is received. Likewise, when an advance is received for supply of goods, it does not amount to revenue. Revenue, in fact, arises only when goods are supplied.

8. Matching Concept

The meaning of expenses against revenues for ascertaining the net profit or loss of a business is known as the matching concept. The matching concept required that costs should be recognized as expenses in the period in which the associated revenue is recognized. For example, when a radio is sold in the current year, all the costs associated with the production and sale of that radio should be recognized as expenses of the year, even though some of these expenses have not been paid. In other words, profits made by a business during a period can be measured only when the revenue earned during the period is compared with the expenses incurred for earning that revenue. The question as to when the payment for the expense is made does not arise at all.

Because of matching concept, adjustments are made for all outstanding and prepaid expenses and incomes receivable and received in advance at the time of preparing final accounts.

9. Accrual Concept

Under this concept, revenue recognition depends on its realization and not on actual receipt. Likewise, costs are recognized when they are incurred and not when paid. This necessitates certain adjustments in the preparation of Income statement. In relation to revenue, the accounts should exclude amounts relating to subsequent period and provide for revenue recognized but not received in cash.

Likewise in relation to costs, the accounts should exclude amount relating to subsequent period, provide for costs incurred but not paid and exclude costs paid for subsequent period.

The matching principle is not followed in the case of cash system of accounting and the operating results prepared on this basis are not in conformity with generally accepted



accounting principles.

10. Objectivity Concept

As per this concept, all accounting must be based on objective evidence. In other words, the transaction recorded should be supported by various documents. Only in such an event, it would be possible for the auditors to verify accounts and certify them as true or otherwise. The evidence substantiating the business transactions should be objective and free from the bias of the accountants. It is not for this reason that assets are recorded at historical cost and shown thereafter at historical cost less depreciation. If the assets are shown on replacement cost basis, the objectivity is lost and it becomes difficult for auditors to verify such values.

ACCOUNTING CONVENTIONS

Accounting conventions refer to the traditions, customs and practices followed by accountants as a guide in the preparation of financial statements. That is, it is an accounting procedure followed by the accounting community on the basis of long- standing customs.

Convention of Disclosure

It implies that accounts must be honestly prepared and all material information must be disclosed therein. The contents of balance sheet and profit and loss account are prescribed by the Indian Companies Act. These are designed to make disclosure which means that there is to be a sufficient disclosure of information which is of material interest to proprietors, potential creditors and investors.

Now-a-days business is increasingly managed by professionally qualified managers. They owe a duty to make a full disclosure to the persons who have contributed the capital. Financial accounting requires the disclosure of all signified accounting policies adopted in the preparation of financial statements.

Events like bad debts, destructions of plant and equipment due to natural calamities, and acquisition of another major asset are likely to have a substantial influence on the earnings of the enterprise. Hence, their non-disclosure would affect the ability of the users of such statements to make proper evaluations and decisions.



Convention of Materiality

This convention deals with the relative importance of the accounting information. Information which is unimportant need not be disclosed in the financial statements. It is left to the discretion of the accountant to decide what is material and what is immaterial. Generally information is said to be material if it would influence the judgement of an investor or creditor. Sometimes, an accountant may not go into minute details because the work involved may not justify the usefulness of the result.

For instance, in a large concern the entire value of stationery items issued for use in the office may be written off as expenses of the period. Strictly speaking stationery consumed should be treated as expenses and that which remains unused, should be treated as an asset. But it is difficult to find out the value of that part of the stationery which has been used up and that part which remains as stock. Many of the expenses for a period are mere estimates and an attempt to find out the exact amount of expenses involved may not be worthwhile. Moreover, while preparing financial statements, unimportant items can be merged with other items and decimal figures may be rounded off to the nearest rupees.

Convention of Consistency

In any organization, accounting practice should be followed consistently year after year. For example, if depreciation for a particular asset is provided on the basis of diminishing balance method, then the same method should continue in the subsequent years also. If there is no consistency in the accounting method, then comparison of accounting figures and the trading results of different years would become meaningless.

Convention of Conservation

This is the Policy of “Playing Safe”. A business man is always conservative in estimating his profits. He never takes into account expected profits but takes into account all expected losses. This is rather a pessimistic attitude and is reflected in the preparation of accounting statements also. Stock is always valued at cost or market price whichever is lower. Provision for doubtful debts and discount on debtors is created. This convention is against the convention of full disclosure and is attracting a lot of criticism.



Indian Accounting Standards

Accounting is known as the art of recording the exchanges in a manner to assist the perusers with showing up at the decisions or reaching a financial decision about the entity. This becomes fundamental that it ought to be joined into some normalized rules which are for the most part known to account for approaches.

Indian Accounting Standard is the Accounting standard taken on by organizations in India and given under the oversight of the Accounting Standards Board which was composed as a body in the year 1977.

The concocting of these strategies permits different organizations to adjust their accounting standards to repair for their own benefit. Standards are acquainted with quenching all disarrays, and these should have been set by the perceived accounting bodies. This idea repaired the way for the development of Accounting Standards. The Accounting Standards in India are given by the Institute of Chartered Accountants of India (ICAI).

Objectives of the Indian Accounting System

There are many objectives of an Indian Accounting system. We will discuss each and every point under IAS and understand its importance.

- This way, the global scope of Indian companies is expanded and they have a wider platform to perform on.
- This way the Indian companies can imply their rates and demands according to the global rates.
- This way the company accounts and the annual financial statements are transparent.
- It is easy and can be understood by companies worldwide.
- It lets us have a single framework for a single accounting framework.



Indian Accounting System: Benefits

As we already know that without benefits, nobody will try to pursue an accounting system like this. There are many benefits gained while following the Indian Accounting System, let us discuss all of them in detail.

- **International Base** - This lets the business have an international base and platform for companies to perform.
- **Harmonization** - This lets the companies harmonize their rules.
- **Compliance** - Increase compliance in companies.
- **Global Acceptance** - Globally reaches other companies and benefits them. This also gives global or international recognition.

Indian Accounting Standards List:

Indian Accounting Standard Number	Name of Indian Accounting Standard
Ind AS 101	Adoption of Indian Accounting Standard. Share-Based Payment
Ind AS 102	Business Combinations
Ind AS 103	Insurance Contracts
Ind AS 104	Non-Current Assets are held for sale and are Discontinued Operations.
Ind AS 105	Exploration for and the evaluation of the Mineral Resources.
Ind AS 106	Financial Instruments: Disclosures
Ind AS 107	Operating Segments
Ind AS 108	Financial Instruments
Ind AS 109	Consolidated Financial Statements
Ind AS 110	



Ind AS 111	Joint Arrangements
Ind AS 112	Disclosure of Interest to Other Entities
Ind AS 113	Fair Value Measurement
Ind AS 114	Regulatory Deferral Accounts
Ind AS 115	Revenue from contract with customers
Ind AS 1	Presentation of Financial Statements
Ind AS 2	Inventories
Ind AS 7	Statement of Cash Flows
Ind AS 8	Accounting Policies, Changes in the Accounting Estimates and Errors
Ind AS 10	Events after Reporting Period
Ind AS 12	Income Taxes
Ind AS 16	Property, Plant, Equipment.
Ind AS 17	Leases
Ind AS 19	Employee Benefits
Ind AS 20	Accounting for government grants.
Ind AS 21	The result for the changes in Foreign Exchange Rates
Ind AS 23	Borrowing Costs
Ind AS 24	Related Party Disclosures
Ind AS 27	Separate Financial Statements
Ind AS 28	Investments in Associates and in the Joint Ventures
Ind AS 29	Financial Reporting in Hyperinflationary Economies
Ind AS 32	



Ind AS 33	Financial Instruments Presentation
Ind AS 34	Earnings per share
Ind AS 36	Interim Financial Reporting
Ind AS 37	Impairment of Assets
Ind AS 38	Provisions, Contingent Liabilities, and Assets
Ind AS 40	Intangible Assets
Ind AS 41	Investment Property
	Agriculture

Accounting Standards Applicability:

The Indian Accounting Standards are followed by all the companies. They shall follow Ind AS either Voluntarily or Mandatorily. When a company follows the Indian AS, either mandatory or voluntarily, it cannot return to its old method of Accounting.

Mandatory Applicability

Companies with a Net worth of not less than 500 crores are required to follow Ind AS.

Mandatory Applicability from Accounting Period beginning on or after 1 April 2017

- By every Listed Company.
- Also, by the Unlisted Companies with a Net worth which is greater than or equal to Rs. 250 crores but less than Rs. 500 crores

International Financial Reporting Standards (IFRS)

International Financial Reporting Standards (IFRS) are a set of accounting rules for the financial statements of public companies that are intended to make them consistent, transparent, and easily comparable around the world.



IFRS currently has complete profiles for 167 jurisdictions, including those in the European Union. The United States uses a different system, the generally accepted accounting principles (GAAP).

The IFRS is issued by the International Accounting Standards Board (IASB).

The IFRS system is sometimes confused with International Accounting Standards (IAS), which are the older standards that IFRS replaced in 2001.

- International Financial Reporting Standards (IFRS) were created to bring consistency and integrity to accounting standards and practices, regardless of the company or the country.
- They were issued by the London-based Accounting Standards Board (IASB) and address record keeping, account reporting, and other aspects of financial reporting.
- The IFRS system replaced the International Accounting Standards (IAS) in 2001.
- IFRS fosters greater corporate transparency.
- IFRS is not used by all countries; for example, the U.S. uses generally accepted accounting principles (GAAP).

IFRS specify in detail how companies must maintain their records and report their expenses and income. They were established to create a common accounting language that could be understood globally by investors, auditors, government regulators, and other interested parties.

The standards are designed to bring consistency to accounting language, practices, and statements, and to help businesses and investors make educated financial analyses and decisions.

They were developed by the International Accounting Standards Board, which is part of the not-for-profit, London-based IFRS Foundation. The Foundation says it sets the standards to “bring transparency, accountability, and efficiency to financial markets around the world.”



IFRS vs. GAAP

Public companies in the U.S. are required to use a rival system, the generally accepted accounting principles (GAAP). The GAAP standards were developed by the Financial Standards Accounting Board (FSAB) and the Governmental Accounting Standards Board (GASB).

The Securities and Exchange Commission (SEC) has said it won't switch to International Financial Reporting Standards but will continue reviewing a proposal to allow IFRS information to supplement U.S. financial filings.

There are differences between IFRS and GAAP reporting. For example, IFRS is not as strict in defining revenue and allows companies to report revenue sooner. A balance sheet using this system might show a higher stream of revenue than a GAAP version of the same balance sheet.

IFRS also has different requirements for reporting expenses. For example, if a company is spending money on development or on investment for the future, it doesn't necessarily have to be reported as an expense. It can be capitalized instead.

Standard IFRS Requirements

IFRS covers a wide range of accounting activities. There are certain aspects of business practice for which IFRS set mandatory rules.

- **Statement of Financial Position:** This is the balance sheet. IFRS influences the ways in which the components of a balance sheet are reported.
- **Statement of Comprehensive Income:** This can take the form of one statement or be separated into a profit and loss statement and a statement of other income, including property and equipment.
- **Statement of Changes in Equity:** Also known as a statement of retained earnings, this documents the company's change in earnings or profit for the given financial period.
 - **Statement of Cash Flows:** This report summarizes the company's financial transactions in the given period, separating cash flow into operations, investing, and financing.



In addition to these basic reports, a company must give a summary of its accounting policies. The full report is often seen side by side with the previous report to show the changes in profit and loss. A parent company must create separate account reports for each of its subsidiary companies.



UNIT-II

DOUBLE-ENTRY BOOKKEEPING

Introduction:

Double-entry bookkeeping is a method of recording transactions where for every business transaction, an entry is recorded in at least two accounts as a debit or credit. In a double-entry system, the amounts recorded as debits must be equal to the amounts recorded as credits. The key feature of this system is that the debits and credits should always match for error-free transactions. The double-entry bookkeeping system works on the basic accounting equation, which is as follows:

$$\text{Assets} = \text{Liability} + \text{Owners Equity}$$

Assets: The money that the company owns

Liabilities: Anything that the business owes

Owner's equity: Owner's investment in the company

Income: Money the business earns by selling its products

Expense: Money the company spends to run the business

You should always remember that each side of the equation must balance out. This is how we arrive at the term “balancing the books.” A small example will help you understand this equation.

Let us take the same example that we used above, but this time use double-entry bookkeeping. Assume you are recording debit and credit entries for the transactions that take place in a week, using double-entry bookkeeping.

The starting balance for the week is Rs. 5000. In one week, you pay your rent (Rs.1000).



Account	Debit	Credit
Rent	1000	
Cash		1000

You purchase some office furniture (Rs.1500).

Account	Debit	Credit
Furniture	1500	
Cash		1500

Meanwhile, Excel Technologies pays an invoice with a value of Rs.500.

Account	Debit	Credit
Cash	500	
Excel Tech (Invoice)		500

If you look at all three transactions, you can observe that total credit and total debit are the same: they both add up to Rs.3000.

What documents are used to record entries?

In single-entry bookkeeping, the income and expenses for the transactions are recorded in a cash register, whereas the double-entry system starts with a journal, followed by a ledger, a trial balance, and finally financial statements.

1. **Journal:** This is an accounting book where the transactions are recorded sequentially, in chronological order. It need not be balanced.



2. **Ledger:** This is a book of final entries where the transactions are divided and recorded in separate accounts. It must be balanced.
3. **Trial balance:** This is a bookkeeping worksheet that reflects the credit and debit balance of all ledger accounts. One of the important features of the trial balance is that it maintains the arithmetic accuracy of transactions.
4. **Financial statements:** These are a collection of summary-level reports that reflect the organization's financial results, position, and cash flow.

JOURNAL

Books used for recording transactions are called Books of Account. Every business must invariably maintain two books of accounts. They are: i) Journal and ii) Ledger.

The journal is the “day-by-day” book of the business where in both aspects of all transactions are recorded in chronological order (i.e.) date-wise. The very first record of a business transaction is made in order of date in the journal. The journal is thus, a “Book of Prime Entry”. It is otherwise known as “Book of Original Entry”. It is 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 subdivided into a number of Subsidiary Books which, for convenience and have certain specialized functions, i.e. one book is meant for Credit Purchases and another for Credit Sales and so on.

Specimen

Journal Entry

Date	Particulars	L.F.	Debit		Credit	
			Rs.	P.	Rs.	P.



LEDGER

So far we have learnt the method of recording the business transactions in the journal. Now we shall learn the second book namely ledger. Ledger is a main book of accounts. It contains accounts representing persons, properties and nominal items like expenses and gains.

All the transactions are recorded in the journal separately and date-wise. As such, the transactions of a similar nature or those relating to a person or property or expenses/gain are recorded in different places as they occur on different dates. Moreover, the journal simply dissects the given transactions 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 particular account (eg.) 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 ledger.

Specimen:

Ledger

Dr.

Cr.

Date	Particulars	J. F.	Amount Rs.	Date	Particulars	J. F.	Amount Rs.

Illustration: 1

Journalise the following transactions in the books of Mr. Shankar

2022		Rs.
August		
1	Shankar commenced a business from cash	1,00,000



2	Cash deposit in to the Canara bank	9,000
4	Goods purchased for Cheque	2000
5	Sales to Mr. Kumar	1600
12	Purchased from Mr. Rajesh	4000
20	Cash sales	3000
22	Goods return to Mr. Rajesh	1000
24	Goods returns from Mr. Anurn	100
30	Rent paid	400
	Salary paid	600
	Commission received	150

Solution:

Journal Entries of Mr. Shankar

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2022 August 1	Cash a/c Dr. To Capital a/c (Shankar start business)		1,00,000	1,00,000
2	Bank a/c Dr. To Cash a/c (cash deposited in Canara Bank)		9,000	9,000
4	Purchase a/c Dr. To Bank a/c (Goods purchase for Cheque)		2,000	2,000
5	Mr. Kumar a/c Dr.		1,600	



	To Sales (Sales to Mr. Kumar)			1,600
12	Purchases a/c To Mr. Rajesh (Goods from Mr. Rajesh)	Dr.	4,000	4,000
20	Cash a/c To Sales a/c (Cash sales)	Dr.	3,000	3,000
22	Mr. Rajesh a/c To Purchases returns a/c (Goods returns to Mr. Rajesh)	Dr.	1,000	1,000
24	Sales returns a/c To Mr. Arun a/c (Goods returns from Mr. Arun)	Dr.	100	100
30	Rent a/c To Cash (Rent paid)	Dr.	400	400
	Salary a/c To Cash (Salary paid)	Dr.	600	600
	Cash a/c To Commission a/c (Commission received)	Dr.	150	150

Illustration: 2

Journalise the following transactions in the books of Mr. Selvam

Jan. 2014		Rs.
1	Mr. Selvam commenced business with cash	2,00,000



2	Purchased goods for cash	15,000
5	Purchased goods from Sethuraman on credit	7,000
7	Paid into bank	5,000
10	Purchased furniture	2,000
20	Sold goods to Petchimuthu on credit	5,000
25	Cash sales	3,500
26	Paid to Sethuraman	3,000
31	Paid salaries	5,000

Solution:

Journal Entry of Mr. Selvam

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2014 Jan. 1	Cash a/c Dr. To Capital a/c (Mr. Selvam started business)		2,00,000	2,00,000
2	Purchases a/c Dr. To Cash a/c (Cash purchases)		15,000	15,000
5	Purchases a/c Dr. To Sethuraman a/c (Credit purchases)		7,000	7,000
7	Bank a/c Dr. To Cash a/c (Deposited in bank)		5,000	5,000
10	Furniture a/c Dr. To Cash a/c (Furniture purchased)		2,000	2,000



20	Petchimuthu a/c To Sales a/c (Credit sales)	Dr.	5,000	5,000
25	Cash a/c To Sales a/c (Cash sales)	Dr.	3,500	3,500
26	Sethuraman a/c To Cash a/c (Paid to Sethuraman)	Dr.	3,000	3,000
31	Salary a/c To Cash a/c (Salary paid)	Dr.	5,000	5,000

Illustration: 3

Journalise the following transactions in the books of Manikandan and post them in the ledger

2014 March		Rs.
1	Bought goods for cash Rs. 25,000	25,000
2	Sold goods for cash Rs. 50,000	50,000
3	Bought goods for credit from Kannan Rs. 19,000	19,000
5	Sold goods on credit to Rakesh Rs. 8,000	8,000
7	Received from Rakesh Rs. 6,000	6,000
9	Paid to Kannan Rs. 5,000	5,000
20	Bought furniture for cash Rs. 7,000	7,000

Solution:

Journal Entry of Manikandan

Date	Particulars	L.F.	Debit	Credit
------	-------------	------	-------	--------



			Rs.	Rs.
2014				
March 1	Purchases a/c To Cash a/c (Cash purchases)	Dr.	25,000	25,000
2	Cash a/c To Sales a/c (Cash sales)	Dr.	50,000	50,000
3	Purchases a/c To Kannan a/c (Credit purchases)	Dr.	19,000	19,000
5	Rakesh a/c To Sales a/c (Credit sales)	Dr.	8,000	8,000
7	Cash a/c To Rakesh a/c (Cash received)	Dr.	6,000	6,000
9	Kannan a/c To Cash a/c (Cash paid)	Dr.	5,000	5,000
20	Furniture a/c To Cash a/c (Furniture purchased)	Dr.	7,000	7,000

Ledger of Mr. Manikandan Cash Account

Dr.

Cr.

Date	Particulars	J.F.	Amount	Date	Particulars	J.F.	Amount
			Rs.				Rs.



2014				2014			
Mar. 5	To Sales a/c		50,000	Mar. 1	By Purchases a/c		25,000
	To Rakesh a/c		6,000	9	By Kannan a/c		5,000
				20	By Furniture a/c		7,000

Purchases Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
2014							
Mar. 1	To Cash a/c		25,000				
3	To Kannan a/c		19,000				

Sales Account

Dr.

Cr.

Date	Particulars	J. F.	Amount Rs.	Date	Particulars	J. F.	Amount Rs.
				2014			
				Mar. 2	By Cash a/c		50,000
				5	By Rakesh a/c		8,000

Furniture Account

Dr.

Cr.



Date	Particulars	J. F.	Amount Rs.	Date	Particulars	J. F.	Amount Rs.
2014 Mar 20	To Cash a/c		7,000				

Kannan Account

Dr.

Cr.

Date	Particulars	J. F.	Amount Rs.	Date	Particulars	J. F.	Amount Rs.
2014 Mar 9	To Cash a/c		5,000	2014 Mar 3	By Purchase a/c		19,000

Rakesh Account

Dr.

Cr.

Date	Particulars	J. F.	Amount Rs.	Date	Particulars	J. F.	Amount Rs.
2014 Mar 5	To Sales a/c		8,000	2014 Mar 7	By Cash a/c		6,000

Trial Balance



Meaning:

All business transactions are initially recorded in Journal or Subsidiary books. Then they are transferred to ledger by posting to relevant accounts. After balancing the ledger accounts of a business enterprise, a statement is prepared to show separately the debit and credit balances. Such a statement is known as 'Trial balance'. It is not an account. It is a statement in which debit and credit balances of all the accounts in the ledger are shown to test the arithmetical accuracy of the books of accounts.

The fundamental principle of double entry system of book-keeping is that every debit has a corresponding credit and Vice versa. Therefore the total of the debit balances must be equal in aggregate to the total of the credit balances when the accounts are balanced. Thus, to find out the arithmetical correctness of the book-keeping work, we prepare a summary of balances as they appear in the ledger at some particular date. This summary of balances is known as a 'Trial balance'. Or to put in other words, we take a 'trial' of ledger balances, like a tailor taking a trial of a suit, for the purpose of proving the arithmetical accuracy of the records.

Therefore it is called "Trial balance". No doubt it is a useful device and it helps in preparation of final accounts since it contains all the Personal, Real and Nominal accounts. As it is prepared by taking up the balances of ledger accounts, both debit and credit sides of a trial balance must always be equal.

Definition:

According to M.S. Gosay (The Substance of Accountancy) "Trial balance is a statement containing the balances of all ledger accounts, as at any given date, arranged in the form of debit and credit columns placed side by side and prepared with the object of checking the arithmetical accuracy of ledger postings."

Objectives of Preparing a Trial Balance

Following are the objectives of preparing Trial Balance

(i) To check arithmetical accuracy



Arithmetical accuracy in ledger posting means writing correct amount, in the correct account and on its correct side while posting transactions from various original books of accounts, such as Cash Book, Purchases Book, Sales Book, etc. It also means not only the correct balance of ledger account but also the totals of the special purpose Books.

(ii) To help in preparing Financial Statements

The ultimate objective of the accounting is to prepare financial statements i.e. Trading and Profit and Loss Account, and Balance sheet of a business enterprise at the end of an accounting year. These statements contain balances of various ledger accounts. As Trial Balance contains balances of all ledger accounts, in financial statements the balances of ledger accounts are carried from the Trial balance for proper analysis.

(i) Helps in locating errors

If total of two columns of the trial balance agrees it is a proof of arithmetical accuracy in the ledger posting. However, if the totals of the two columns do not tally it indicates that there is some mistake in the ledger accounts. This prompts the accountant to find out the errors.

(ii) Helps in comparison

Comparison of ledger account balances of one year with the corresponding balances with the previous year helps the management taking some important decisions. This is possible by using the Trial Balances of the two years.

(iii) Helps in making adjustments

While making financial statements adjustments regarding closing stock, prepaid expenses, outstanding expenses etc are to be made. Trial balance helps in identifying the items requiring adjustments in preparing the financial statements.

Trial Balance is generally prepared at the end of the year. However it can be prepared at any time during the accounting year to check the accuracy of the posting.

PREPARATION OF TRIAL BALANCE:

Trial Balance is not an account. It is only a list or schedule of balances of ledger



accounts including cash and bank balances. It is prepared on a particular date. The accounts having a debit balance are entered in the debit amount column and credit balance accounts are entered in the credit amount column. The totals of the two sides of the accounts may also be used to prepare trial balance. The sum of each column should be equal. The standard format of a trial balance is given below :

Trial Balance of

As at(closing date)

Name of the Account	LF	Dr. Balance (Rs.)	Cr. Balance (Rs.)

The name of the business firm is written on the top of the statement with Trial Balance. Under this we write the date on which Trial Balance is prepared.

Trial Balance has three columns : Name of the Ledger Account, Debit Amount and Credit Amount.

In the ledger account column we write the name of the account. In the Debit amount column we write the amount of debit balance of the account (or the total of the debit side of the account). Similarly in the credit amount column we write the amount of credit balance of the account (or the total of the credit side of the account).

Steps to prepare Trial Balance

- (i) At first ascertain the balance account wise of all the ledger accounts.
- (ii) Write the name of the ledger account in the ledger account column.
- (iii) Write against the name of the ledger account, the balance amount/total amount, debit balance/total in the



debit column; and credit balance/ total in the credit column.

(iv) Add the debit balance/total amount column and credit balance/total amount column.

Illustration - 1

From the following ledger accounts of a trader closed as on 31st January, 2006, prepare Trial Balance.

Capital A/c

Dr.

cr

Date	Particulars	JF	Amount Rs	Date	Particulars	JF	AmountRs
2006				2006			
Jan 31	Balance c/d		100000	Jan	Bank A/c		100000
			100000				<u>100000</u>
				Feb. 1	Balance b/d		100000

Sales A/c

Dr.

Cr

Date	Particulars	JF	Amount Rs	Date	Particulars	JF	AmountRs
2006				2006			
Jan 31	Balance transferred to Trading A/c		70000	Jan. 8	Bank A/c		24000
				Jan. 15	Vikram's A/c		46000
			70000				<u>70000</u>

Purchases A/c

Dr.

Cr

Date	Particulars	JF	Amount Rs	Date	Particulars	JF	AmountRs



2006				2006			
Jan. 5	Pranaya's A/c		40000	Jan. 31	Stock A/c		15000
Jan. 14	Bank A/c		55000	Jan. 31	Balance		80000
					transferred to		
					Trading A/c		
			95000				95000

Vikram's A/c

Dr.

Cr

Date	Particulars	JF	Amount Rs	Date	Particulars	JF	AmountRs
2006				2006			
Jan. 15	Sales A/c		46000	Jan. 31	Balance cld		46000
			46000				46000
Feb. 1	Balance b/d		46000				

Pranaya's A/c

Dr.

Cr

Date	Particulars	JF	Amount Rs	Date	Particulars	JF	AmountRs
2006				2006			
Jan. 31	Balance cld		40000	Jan. 5	Purchases A/c		40000
			40000				40000
				Feb. 1	Balance b/d		40000

Rent Received A/c

Dr.

Cr.

Date	Particulars	JF	Amount Rs	Date	Particulars	JF	Amount Rs
2006				2006			
Jan. 31	Balance transferred to Profit and Loss A/c		1500	Jan. 31	Bank A/c		1500
			1500				1500



Bank A/c

Dr				Cr			
Date	Particulars	JF	Amount Rs	Date	Particulars	JF	Amount Rs
	Capital A/c		100000		Purchases A/c		55000
	Sales A/c		24000		Commission A/c		18000
	Rent received		1500		Drawings A/c		2200
					Balance c/d		66700
			125500				125500

Commission A/c

Dr				Cr			
Date	Particulars	JF	Amount Rs	Date	Particulars	JF	Amount Rs
2006 Jan. 20	Bank A/c		1800	2006 Jan. 31	Balance transferred to Profit and Loss A/c		1800
			1800				1800

Stock A/c

Dr.				Cr			
Date	Particulars	JF	Amount Rs	Date	Particulars	JF	Amount Rs
2006 Jan. 31	Purchases A/c		15000	2006 Jan. 31	Balance cld		15000
			15000				15000
Feb. 1	Balance b/d		15000				

Drawings A/c

Dr.				Cr			
Date	Particulars	JF	Amount Rs	Date	Particulars	JF	Amount Rs
2007 Jan. 31	Bank A/c		2000	2007 Jan. 31	Balance cld		2000
			2000				2000



Feb. 1	Balance b/d		2000				
--------	-------------	--	------	--	--	--	--

Solution.

Trial Balance

Name of the Ledger Account	Dr.	Cr.
	Balance(Rs.)	Balance(Rs.)
Capital		100000
Sales		70000
Purchases	80000	
Vikram	46000	
Pranaya		40000
Commission	1800	
Rent received		1500
Drawings	2000	
Closing Stock	15000	
Cash at Bank	66700	
	211500	211500

Illustration : 2.

From the following balances extracted from the books of a trader, prepare Trial Balance as on 31st March, 2006.

Particulars	Rs
Cash in hand	4200
Cash at Bank	16800
Bills Receivable	18000
Bills payable	16000
Sundry debtors	24600
Sundry creditors	32400



Capital	50000
Drawings	18000
Sales	105000
Purchases	75000
Carriage Inward	2700
Salaries	12000
Advertisement	2400
Insurance	1600
Furniture	7500
Stock	18600
Office Rent	2000

Solution :

Trial Balance

	Dr	Cr
Name of the Account	Balances (Rs)	Balances (Rs)
Cash	4200	
Bank	16800	
Bills Receivable	18000	
Bills payable		16000
Sundry Debtors	24600	
Sundry creditors		32400
Capital		50000
Drawings	18000	
Sales		105000
Purchases	75000	
Carriage Inward	2700	
Salaries	12000	
Advertisement	2400	
Insurance	1600	



Furniture	7500	
Rent	2000	
Stock	18600	
Total	203400	203400

Problems:

1. Prepare Trial Balance of M/s Multiplying enterprise as on 31st December, 2006.

Accounts	Balances (Rs.)	Accounts (Rs.)	Balances
Cash in hand	2500	Debtors	18200
Cash at Bank	14500	Creditors	16600
Capital	70000	Opening stock	8700
Drawing	9000	Wages	6700
Purchases	60000	Rent	5000
Sales	82000	Salary	8400
Machine	35000	Bills Payable	11400
Furniture	12000		

2. Prepare Trial Balance as on 31st March, 2006 from the following balances of Sabana :

Dr.	Cr.	
Accounts	Balances (Rs.)	Balances (Rs.)
Cash in hand	3100	
Bank overdraft		18250
Opening stock	24600	
Purchases	59800	
Sales		72350
Sabana's Capital		50000
Drawings	12000	
Carriage Inward	1600	
Rent	2400	
Commission		2100
Interest	780	



Furniture	5220	
Creditors		13600
Debtors	27800	
Building	20000	1000
Suspense	157300	157300



UNIT - III

SUBSIDIARY BOOKS

Introduction:

Maintaining a single 'journal book' in which journal entries are written for each transaction and posting them to ledger is practicable in small businesses where a single accountant can maintain accounts or the owner himself can do the accounts work. In bigger businesses, transactions are so numerous and varied that a single journal book is absolutely inadequate and cumbersome.

Several accounts assistants may have to do accounts work as a team and share the burden. It may be necessary to group similar transactions even at journal stage in the shape of 'special journals' to minimize and facilitate ledger work. Thus, the system of Subsidiary Books as an alternative for single journal was developed.

Subsidiary books comprise of the following:

- (a) Purchases book to record credit purchases of goods;
- (b) Sales book to record credit sales of goods;
- (c) Purchase returns book to record returns to suppliers.
- (d) Sales returns book to record returns from customers.
- (e) Cash book to record all cash receipts and payments.
- (f) Bills receivable book to record bills received.
- (g) Bills payable book to record bills payable accepted.
- (h) General journal or journal proper to record any other transactions which cannot be entered in the above specialised subsidiary books.

Benefits of Subsidiary Book system

Subsidiary books result in the following benefits:



-
- (a) **Reduction in work:** Overall work reduces in this system compared to a single journal because one posting alone is made on the date of the transactions. Consolidated monthly posting is made for the second aspect.
- (b) **Permits group work:** Single journal can be written by one person alone. Work on subsidiary books can be carried on by many accountants.
- (e) **Accuracy:** Accounts will be more accurate because of specialised work and monthly summarised postings.
- (d) **Better information:** A lot of useful data like total credit sales, credit purchases, returns, etc., is made available which is not possible in journal system.
- (e) **Cash book:** Cash book itself takes the place of journal as well as ledger account. Thus, separate cash account is not needed. In case of three column cash book, even bank A/c is not needed in the ledger.

Basic documents for Subsidiary Books

- (a) **Inward invoice:** This is the document sent by the suppliers of goods giving details of goods sent, price, value, discount etc. It is the basis for entries in purchases book.
- (b) **Outward Invoice:** This is a document sent by the firm to the customers, showing the details of goods supplied, their price and value, discounts, etc. It is the basis for writing sales book.
- (c) **Debit note:** When goods purchased from suppliers are returned, a debit note is sent to them showing the goods returned and their value. It is the basis for purchase returns book.
- (d) **Credit Note:** When customers return goods, a credit note is prepared by the firm and sent to them mentioning the amount credited to them based on the goods received as returns. This note is the basis to write sales returns book.
- (e) **Cash Receipts and Vouchers:** These are the vouchers and receipts for cash received and paid. Entries in cash book are made on the strength of the vouchers and receipts. They are also useful for auditing purpose.

Preparation of Individual Subsidiary Books



(A) PURCHASES BOOK

Purchases book is also known as 'bought book purchase day book', 'invoice book', and 'purchase journal'.

- (a) All credit purchases of goods are recorded in this book. Periodical total of this book provides total credit purchase of goods made by the firm.
- (b) Cash purchase of goods and credit or cash purchase of assets are ignored in this book.
- (c) Inward invoices' received from suppliers, duly verified, form the basis for entries in purchase book.

Method of Recording

In the chronological order of goods purchased on credit, the names of suppliers with details of goods bought and number of inward invoice are recorded in the book with net amount payable. Any trade discount allowed is deducted from the gross invoice value of goods received.

Method of Posting:

- (a) Whenever a credit purchase of goods is made and recorded in purchases book, immediately the supplier's account in the ledger is credited with the net purchase value.
- (b) At the end of the month, the purchases book is totalled. The total amount of credit purchases for the month is debited to the 'purchases account' in the ledger. Thus, the 'double entry' in the ledger is completed at the end of every month.

Purchases book saves the need for separate journal entry for every credit purchase of goods and daily posting to purchases account in the ledger. It can provide the total of credit purchases any time it is needed. Reducing such figure from the total purchases can provide total cash purchases also. Thus, purchases book results in saving of time, labour and more comprehensive information.



(B) SALES BOOK:

Sales book is also known as 'Day book, Sales day book, 'Sold book', 'Sales journal' etc.

- (a) All credit sales of goods are recorded in this book. Periodical totals of this book provide the total credit sales of goods by the firm.
- (b) Cash sales of goods and credit sales of assets are not shown in this book.
- (c) Outward invoices' form the basis for making entries in the sales book. The invoices must be properly authenticated.

Method of Recording:

According to the dates and time of credit sales taking place, they are recorded in the sales book. The name of customer with details of goods sold and the net amount receivable is recorded. Trade discount if any, is deducted in arriving at the net sale value. (See Illustration 11)

Method of posting:

- (a) Whenever a credit sale of goods is made and it is recorded in the sales book, the customer's account in the ledger is debited immediately with the net sale value.
- (b) Sales book is totalled at the end of each month. The total credit sales for the month are credited to the sales account in the ledger. This posting completes the 'double entry' in the ledger for credit sales.

Sales book avoids the need for a separate journal entry and its posting to two ledger accounts whenever goods are sold on credit. It provides the total credit sales of goods at any given time. The difference between total sales shown by the sales account in the ledger and the sales book total represents the total cash sales. Thus, sales book saves time and effort and also provides more useful information for decision-making.

(C) PURCHASE RETURNS BOOK:

It is also called 'Returns outward book' and 'Purchase returns journal'



(a) Goods returned to suppliers which were originally purchased on credit are recorded in this book. Periodical totals of this book provide data on purchase returns by the firm.

(b) 'Debit notes' sent by the firm to the suppliers when goods are returned form the basis for entries in this book.

Method of Recording:

As per the dates of returns made, entries are recorded in purchase returns book. Name of supplier, with details of goods returned and the relevant debit note number are shown along with the net amount. (See Illustration 12)

Method of posting:

(a) When goods are returned to supplier, entry is made in the purchase returns book. Immediately, the supplier's account is debited in the ledger.

(b) Purchase returns book is totalled at the end of every month. The total is credited to the purchase returns account in the ledger. This posting completes 'Double Entry in the ledger for the purchase returns during the month.

Purchase returns book saves time and effort in the recording and posting of the returns. It also gives data about total purchase returns at any given time.

(D) SALES RETURNS BOOK:

This book is also called 'Returns Inward Book' and 'Sales Returns Journal'.

(a) Goods returned by customers which were originally sold on credit are recorded in this book. Monthly totals of this book provide data on 'sales returns'.

(b) 'Credit notes' sent to the customers after receiving the goods returned by them form the basis for entries in this book.



Method of Recording:

According to the dates of returns received from customers, entries are made in sales returns book. Name of customer with details of goods returned and credit note number are shown along with net amount.

Method of posting

(a) When return is received from customer, entry is made in the sales returns book. Immediately customer's account is credited in the ledger.

(b) Sales returns book is totalled at the end of every month. The total is debited to 'Sales returns Account' in the ledger which completes double entry in the ledger for the sales returns during the month. Sales return book saves time and effort in the recording and posting of the returns.

It also provides summarised returns from credit customers at any given time.

(E) CASH BOOK

Business firms of every size have a large number of payments and receipts- either in the form of cash or through bank. In the traditional journal - ledger system, writing entries for every receipt and payment and posting them to cash and bank Accounts in the ledger constitutes majority of the accounting work. In the subsidiary book system, the entire work relating to cash and bank transactions is minimised and simplified through "Cash book

Cash Book plays a dual role' by serving as a subsidiary book and also as a ledger account.

It is the book of original entry because receipts and payments are recorded in the cash book and they are posted to the different accounts in the ledger.

Cash book also serves the purpose of a ledger because it is written like an account with opening and closing balances and with debit and credit sides. There is no need to open cash account in the ledger.

There are four types of cash book:

(a) Simple cash book or single column cash book:



- (b) Two column cash book with cash and discount columns
- (c) Two column cash book with bank and discount columns, and
- d) Three column cash book with cash, bank and discount columns.

(a) Simple Cash Book

This type of cash book contains debit side and credit side, showing all receipts of cash on debit side and payments of cash on credit side. Debit side is called receipts side and credit side is called payments side.

Postings from simple cash book: As and when a transaction is entered in the cash book, it has to be posted to the corresponding account in the ledger. Expenses are shown on credit side of cash book and the respective nominal accounts are debited in the ledger. Incomes are shown on the debit side and the concerned nominal accounts are credited in the ledger. Similar procedure is adopted for personal accounts and real accounts also.

Balancing of Simple Cash Book: Debit side of cash book should always be more because it is not possible to pay more cash than what is available. The closing balance of cash is taken to balance sheet as an asset.

(b) Two column Cash book with cash and discount columns:

The method of maintaining this cash book is almost like simple cash book. However, on the debit side as well as on credit side. a discount column is maintained, When payments are made, discount received on payments is shown in the discount column on the credit side. Similarly, when cash is received. discount may be allowed to the customers which is recorded in the discount column on the debit side.

Posting to Ledger

Cash received and paid is posted to the respective accounts in the ledger just as in simple cash book. Discount shown on the credit side of cash book is immediately credited to discount received account in the ledger. Similarly, discount shown on the debit side of the cash book is debited to the discount allowed account in the ledger. The discount columns are



separately totalled at the time of balancing of the cash book. The totals represent discount allowed and discount received during the period.

(c) Two column cash book with bank and discount columns

Large corporations and big firms usually make all payments through cheques and receipts are also through cheques. Such companies and firms maintain a cash book with bank and discount columns only. All cheques issued are shown on payments side, all cheques received and deposited in bank are shown on the receipts side. Discount allowed and received columns are also maintained on the receipts side and payments side respectively.

Postings from the cash book are made into the ledger as and when transactions take place.

(d) Three columnar cash book :

This type of cash book is of maximum utility because it minimises work relating to accounts and presents a summarised picture of the liquidity position of a business.

On both sides of the cash book, separate columns are opened for discount, cash and bank. All transactions relating to cash receipts and cash are shown in the cash columns on receipts side and payment side respectively. Similarly, all cheques issued for payment are shown in bank column on credit side. All deposits- both cash and cheques - are shown on the debit side in the bank column. Discount allowed on both cash and cheques received is shown on debit side. Discount received on both cash paid and cheques issued is shown on credit side.

Posting of receipts and payments - both cash and bank - are debited and credited in the ledger in the usual way, as and when transactions take place.

Some Special items:

(1) Contra entries:

When cash is deposited into bank. it is debited in bank column on debit side and credited in cash column on the credit side. Similarly, when cash is withdrawn for business use, cash column is debited on the receipts side and bank column is credited on the payments side. Thus, both debit and credit aspects of 'contra entries are completed in cash book itself.



There is no need to post them to ledger. Such transactions are marked with 'c' on both sides in Three columnar cash book.

(2) Cheques Received:

The general principle is cheque received is like cash received. So cheques received are shown in the cash column on the debit side of cash book. When the cheques are deposited in bank after some time, a 'contra entry is written. However, when cheques received are sent on the same day to Bank for collection. they can be directly shown in Bank column on debit side without entering in cash column.

(3) Cheques dishonoured:

They are shown on the credit side of cash book in the bank column because to the extent of the cheque returned, balance at bank reduces. The account of the person whose cheque is dishonoured will be debited in the Ledger.

(4) Balance of Cash Book:

Cash column and bank column are separately balanced. In cash column, there must be some balance always. In bank column. there can be balance or overdraft. depending on deposits and payments out of hank.

PETTY CASH BOOK

Meaning and Purpose: Petty is a derivation of the French word "PETIT which means small. So. it is meant to be a small cash book, not in physical size but in recording small payments. A business makes numerous routine small payments day after a day like postage, stationery, cartage, refreshments, cleaning, etc. If all these payments are recorded in the main cash book, it becomes too bulky and the principal cashier becomes overburdened.

In most of the medium and large-sized business establishments, a separate cashier is entrusted with the job of making all the small routine payments and maintain accounts for them. He is called 'petty cashier and the book he maintains is called 'petty cash book'. Thus, the basic purpose of petty cash book is to relieve the burden of main cashier and avoid cluttering of the cash book with numerous small payments.



Imprest system:

The amount which may be needed during a specific period (say, a month) for small payments is estimated and fixed as 'Imprest amount'. It can be revised periodically with growth and expansion in payments. At the beginning of the period the imprest amount is handed over to petty cashier.

He makes all the payments and collects vouchers relevant for the transactions. He records the payments in the petty cash book. At the end of the period he submits the account and the vouchers to the main cashier who examines them and after satisfying himself about their accuracy hands over to the petty cashier sufficient amount to make up the imprest amount. The petty cashier starts the next period with the 'predetermined imprest amount' afresh.

For example, if imprest amount is Rs. 1,000 per month and during a month, the petty cashier has a closing balance of Rs. 70 in his hand he has spent Rs. 930 during the month. After submission of account and vouchers, the main cashier gives cash or cheque for Rs. 930 to the petty cashier so that he can start the next month with Rs.1,000 again.

The imprest system provides control and systematised approach to the petty cash payments.

Analytical petty cash book or Columnar petty cash book

Unclassified petty cash payments may lead to uncontrolled expenses. Showing the entire amount paid by petty cashier as 'petty expenses' is undesirable from control point of view. The Analytical petty cash book' system was devised to make petty cash payments more organised and recording more convenient and efficient.

Based on past experience, all the petty cash payments are classified into a limited number of homogenous and compact groups. Separate columns are opened for each group in the petty cash book with a column for overall total expenditure. The left hand side of the Analytical petty cash book shows opening balance for the period and amount received from the main cashier. The right hand side shows total payments and analytical columns for different groups of expenses.



At the end of the period, all the analytical columns are individually totalled. Total of all these columns should tally with the Total payments column. Receipts and total payments columns are balanced and the balance is carried forward to the next period.

Benefits or merits of petty cash book on imprest system with analytical columns:

1. Main cash book is not made unduly bulky with numerous small payments.
2. Main cashier is relieved of the burden of making all the small payments.
3. Petty cashier is made responsible for making small payments and maintaining petty cash book with appropriate vouchers. This method ensures proper control over small payments. The petty cashier is under the control of the main cashier.
4. The imprest system provides a sort of 'ceiling' on small payments.
5. Columnar system ensures 'single posting of most of the 'Nominal Accounts instead of daily posting of all small payments into those expense accounts.

Posting of Entries from Petty cash book

- a) A petty cash account is opened in the ledger. When cash or cheque is handed over to the petty cashier, it is recorded on the payments side of the main cash book. Petty cash account in the ledger is debited.
- (b) At the end of a period, the total amount spent on various expense groups is ascertained by totalling each of the analytical columns. The respective nominal accounts are debited and petty cash account is credited in the ledger after passing a journal entry in the 'general journal
- (c) The balance shown in petty cash book and that shown in the petty cash account in the ledger should be the same. Such balance is taken to trial balance from the ledger and finally to the assets side of the balance sheet .



Purchases Book

Purchases book also known as **Bought Day Book** is used to record all credit purchases of goods which are meant for resale in the business. **Cash purchases of goods, cash and credit purchases of assets are not entered in this book.**

Before discussing the Purchase Day Book, in detail we are to explain the most significant terms, Trade Discount and Cash Discount.

Format:

Date	Particulars	Inward Invoice No.	L.F.	Amount		Remarks
				Details Rs.	Total Rs.	

Trade Discount

Trade discount is an allowance or concession granted by the seller to the buyer, if the customer purchases goods above a certain quantity or above a certain amount. The amount of the purchase made, is always arrived at after deducting the trade discount, ie., only the net amount is considered.

For example, if the list price (price prescribed by the manufacturers or wholesalers) of a commodity is Rs.100, and trade discount granted by manufacturer to the wholesaler is 20% then cost price of the commodity to the wholesaler is Rs.80. Trade discount is not recorded in the books. They are used for determining the net price.

Cash Discount

Sale of goods on credit is a common phenomenon in any business. When goods are sold on credit the customers enjoy a facility of making payment on some date in the future. In order to encourage them to make the payment before the expiry of the credit period a deduction is



offered. The deduction so made is known as

cash discount.

For example, If Ram purchases goods worth Rs.5,000 on 30 days credit then, as per the terms of contract, he is authorised to make payment 30 days after the date of purchase. If he is offered a cash discount of 2% on payment within 10 days and if he does so, he is entitled to deduct Rs.100 from the invoice price and pay Rs.4,900. In this case Rs.100 is cash discount. But if he does not choose to make payment within 10 days then he will not get any cash discount. In this case he will pay Rs.5,000 after 30 days.

Distinction between cash discount and trade discount

Trade discount differs from cash discount in the following respects.

S.No	Basis of Distinction	Trade Discount	Cash Discount
1.	Parties	It is a reduction granted by a manufacturer/ supplier	It is a reduction granted by a wholesaler (creditor) to the buyer (debtor).
2.	Purpose	To help the retailer to earn some profit.	To encourage prompt payment within a stipulated period.
3.	Time when allowed	It is allowed on the purchase of goods.	It is allowed when payment is made within the specified period.
4.	Variation	It is usually given at the same rate which is applicable to all customers and will vary with the quantity purchased.	It varies from customer to customer depending on the time and period of payment.
5.	Disclosure	It is shown by way of deduction in the invoice itself.	It is not shown in the invoice.
6.	Ledger Account	A separate Account is not opened in the Ledger.	A separate Account is opened in the Ledger for discount received and discount

Posting and Balancing

Once transactions are properly recorded in purchases journal, they are posted into the ledger. The procedure for posting is stated as under.

Step 1 :

Entries will be posted to the credit side of the respective creditors (supplier) account in the



ledger by writing “By Purchases A/c” in the particulars column.

- i. Date Column – Represents the date on which the transaction took place.
- ii. Particulars Column – This column includes the name of the seller and the particulars of goods purchased.
- iii. Inward Invoice No. Column – Reveals the serial number of the inward invoice.
- iv. LF. Column – This column shows the page number of the suppliers account in the ledger accounts.
- v. Details Column – Reveals the amount of goods purchased and the amount of trade discount.
- vi. Total Column – This column represents the net price of the goods, i.e, the amount which is payable to the creditors after adjusting discount and expenses if any.
- vii. Remarks Column – Contains any extra information.

At the end of each month, the purchase book is totalled. The total shows the total amount of goods or materials purchased on credit

Step 2:

Periodic total is posted to the debit of purchases account by writing “To sundries as per purchases book” in the particulars column.

Illustration 1: From the following transactions of Ram for July, 2003 prepare the Purchases Book and ledger accounts connected with this book.

2003

July 5 Purchased on credit from Kannan & Co.
50 Iron boxes @ Rs. 500
10 Grinders @ Rs. 3,000

6 Purchased for cash from Siva & Bros. 25 Fans @ Rs. 1,250



- 10 Purchased from Balan & Sons on credit 20 Grinders @ Rs. 2,500
 10 Mixie @ Rs. 3,000
- 20 Purchased, on credit, one Computer from Kumar for Rs. 35,000.

Solution:

In the book of Ram Purchase Book

Date	Particulars	Inward Invoice No.	L.F.	Amount	
				Details Rs.	Total Rs.
2003 July 5	Kannan & Co. 50 Iron boxes @ Rs. 500 10 Grinders @ Rs. 3,000 Goods purchased vide their bill No..... Dated.....			25,000	55,000
				30,000	
1 0	Balan & Co. 20 Grinders @ Rs.2,500 10 Mixie @ Rs. 3,000 Goods purchased vide their bill No..... Dated.....			50,000	80,000
				30,000	
	Total				1,35,000

Ledger Accounts

Purchase Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
2003 July 31	To Sundries as per Purchases Book		1,35,000				

Kannan & Co Accounts

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
				2003 July 5	By Purchases A/c		55,000



Balan & Co. Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
				2003 July 10	By Purchases A/c		80,000

Note : July 6th transaction is a cash transaction and July 20th transaction is purchase of an asset, so both will not be recorded in the purchases book

Sales Book

The sales book is used to record all credit sales of goods dealt with by the trader in his business. **Cash sales, cash and credit sales of assets are not entered in this book.** The entries in the salesbook are on the basis of the invoices issued to the customers with the net amount of sale. The format of sales book is shown below:-

Format:

Sales Book

Date	Particulars	Outward Invoice No.	L.F.	Amount		Remarks
				Details Rs.	Total Rs.	

i Date Column

Represents the date on which the transaction took place.

ii. Particulars Column

This column includes the name of purchasers and the particulars of goods sold.



iii. Outward Invoice No. Column	Reveals the serial number of the outward invoice.
iv. L.F. Column	The page number of the customers accounts in the Ledger is recorded.
v. Details Column	Contains the amount of goods sold and the amount of trade discount if any.
vi Total Column	This column shows the net amount which is receivable from the customers.
vii. Remarks Column	Any other extra information will be recorded.

Posting and Balancing

At the end of the month the individual entries and the total of the sales book column are posted into the ledgers as under.

Step 1 Individual amounts are daily posted to the debit of Customers' Accounts by writing "To Sales A/c" in the particulars column.

Step 2 Grand total of the sales book is posted to the credit of sales account by writing "By Sundries as per Sales Book" in the particulars column

Illustration 2 From the transactions given below prepare the Sales Book of Ram for July 2003.

2003
July 5 Sold on credit to S.S. Traders
10 Chairs @ Rs. 250
10 Tables @ Rs. 850
Less 10% Discount

8 Sold to Raja for cash

15 Chairs @ Rs. 250



20 Sold to Mohan & Co.

5 Almirah @ Rs. 2,200
10 Tables @ Rs. 850

23 Sold on credit to Narayanan

old computer for Rs. 5,000

28 Sold to Kumaran for cash

15 Chairs @ Rs. 250

Solution:

In the books of RamSales Book

Date	Particulars	Outward Invoice No.	L.F.	Amount	
				Details Rs.	Total Rs.
2003 July 5	S.S. Traders & Co. 10 Chairs @ Rs. 250 10 Tables @ Rs. 850 Less : 10% Discount Sold to S.S. Traders, InvoiceNo. dated			2,500 8,500 11,000 1,100	9,900
20	Mohan & Co. 5 Almirah @ Rs. 2,200 10 Tables @ Rs. 850 Sales as per Invoice No.. dated			11,000 8,500	
Total					29,400

Ledger Accounts

Sales Account

Dr.

Cr

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F	Amount Rs.
				2003 July 31	By Sundries as per sales book		29,400



S.S.Traders Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F	AmountRs.
2003 July5	To Sales A/c		9,900				

Mohan & Co's Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F	AmountRs.
2003 July 20	To Sales A/c		19,500				

RETURNS BOOKS

Returns Books are those books in which the goods returned to the suppliers and goods returned by the customers are recorded.

The reasons for the return of goods are

- i. not according to the order placed.
- ii. not upto the samples which were already shown.
- iii. due to damage condition.
- iv. due to difference in the prices charged.
- v. undue delay in the delivery of the goods

Kinds of Returns Books

The following are the kinds of Returns Books;

- i Purchases Return or Returns outward book**
- ii Sales Return or Returns inward book**

When the business concern returns a part of the goods purchased on credit, the returns fall under the category **Purchases Return or Returns Outward.**



When the business concern receives a part of the goods sold on credit, the returns fall under the category of **Sales Return** or **Returns Inward**.

Purchases Return Book

This book is used to record all returns of goods by the business to the suppliers. The entries in the Purchases Returns Book are usually made on the basis of debit note issued to the suppliers or credit note received from the suppliers. We call it a debit note because the party's (supplier) account is debited with the amount written in this note. The same note is termed as credit note from the receiving party's point of view because he will credit the account of the party from whom he has received the note together with goods.

Format :

Purchase Return Book

Dr.

Cr.

Date	Particulars	Debit Note No.	L.F.	Amount		Remarks
				Details Rs.	Total Rs.	

Note : The reason for goods returned is recorded in Remarks column.

Posting and Balancing

The individual entries and the periodic total of the Purchase Return Book are posted into the Ledger as under:

Step 1 Individual amounts are daily posted to the debit of supplier accounts by writing "To Purchases Return A/c" in the particulars column.

Step 2 Periodic total is posted to the credit of purchases return account by writing "By Sundries as per Purchases Return Book" in the particulars column.

Illustration 3

Enter the following transactions in the purchases return book of Hari and post them into



the ledger.

2003 Jan 5 Returned goods to Anand 5 chairs @ Rs.200 each, not in accordance with order.

14 Returned goods to Chandran 4 chairs @ Rs.200 each and 10 tables @ Rs.350 each, due to inferior quality

Solution:

In the books of Hari Purchases Return Book

Date	Particulars	Debit Note No.	L.F.	Amount		Remarks
				Details Rs.	Total Rs.	
2003 Jan 5	Anand 5 Chairs @ Rs.200				1,000	Not in accordance with order Due to inferior quality
14	Chandran 4 Chairs @ Rs.200			800		
	10 Tables @ Rs.350			3,500		
					4,300	
	Total				5,300	

Ledger Accounts

Purchase Return Account.

Dr

Cr

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
				2003 Jan 31	By Sundries as per Purchases return book		5,300

Anand Account

Dr

Cr

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
2003 Jan 5	To Purchases Return		1,000				



	A/c						
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Chandran Account

Dr

Cr

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J. F	Amount Rs.
2003 Jan 14	To Purchases Return A/c.		4,300				

SALES RETURN BOOK

This book is used to record all returns of goods to the business by the customers. The entries in the sales return book are usually on the basis of credit notes issued to the customers or debit notes issued by the customers.

Format :

Sales Return Book

Date	Particulars	Credit Note No.	L. F.	Amount		Remarks
				Detail s Rs.	Total Rs.	

Note : Remarks column is meant to record the reason for return of goods.

Posting and Balancing

The individual entries and the periodic total of sales return book are posted into the ledger as under.

Step 1 Individual amounts are daily posted to the credit of customers account by writing "By Sales return A/c" in the particulars column.



Step 2 Periodic total is posted to the debit of sales return account by writing “To Sundries as per sales return book “ in the particulars column.

Illustration 4

Enter the following transactions in Returns Inward Book:

2003

April 6 Returned by Shankar 30 shirts each costing Rs.150, due to inferior quality.

8 Amar Tailors returned 10 Baba suits, each costing Rs.100, on account of being not in accordance with their order.

21 T.N. Stores returned 12 Salwar sets each costing Rs.200, being not in accordance with order

Solution:

Sales Return Book

Date	Particulars	Credit Note No.	L.F.	Details Rs.	Amount Rs.	Remarks
2003 April 6	Shankar 30 shirts @ Rs.150			4,500	7,900	Due to inferior quality
8	Amar Tailors 10 Baba suits @ Rs. 100			1,000		Not in accordance with the order
21	T.N Stores 12 Salwar sets @ Rs.200			2,400		Not in accordance with the order
	Total				7,900	

Ledger Accounts

Sales Return Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F.	Amount Rs.
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2003 April 30	To Sundries as per Sales return book		7,900				
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Shankar Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J. F	Amount Rs.
				2003 April 6	By Sales Return A/c.		4,500

Amar Tailors Account

Dr.

Cr.

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F	Amount Rs.
				2003 April 8	By Sales Return A/c.		1,000

T.N.Stores Account

Dr.

Cr

Date	Particulars	J.F.	Amount Rs.	Date	Particulars	J.F	Amount Rs.
				2003 April 21	By Sales Return A/c.		2,400



Single Column Cash Book

Single column cash book (simple cash book) has one amount column in each side. All cash receipts are recorded on the debit side and all cash payments on the credit side. In fact, this book is nothing but a Cash Account. Hence, there is no need to open cash account in the ledger. The format of a single column cash book is given below.

Format

Debit Side **Single Column Cash Book of** Credit Side

Date	Particulars	R. N.	L. F.	Amount Rs.	Date	Particulars	V. N.	L. F.	Amount Rs.

Explanation :

- i. **Date** : This column appears in both the debit and credit side. It records the date of receiving cash at debit side and paying cash at credit side.
- ii. **Particulars** : This column is used at both debit and credit side. It records the names of parties (personal account), heads (nominal account) and items (real account) from whom payment has been received and to whom payment has been made.
- i. **Receipt Number (R.N)**: This refers to the serial number of the cash receipt
Voucher Number (V.N) : This refers to the serial number of the voucher for which payment is made.
- ii. **Ledger Folio (L.F)**: This column is used in both the debit and credit side of cash book. The ledger page (folio) of every account in the cash book is recorded against it.
- iii. **Amount** : This column appears in both sides of the cash book. The actual amount of cash receipt is recorded on the debit side. The actual payments are entered on the credit



side.

Balancing :

The cash book is balanced like any other account. The total of the receipt (debit side) column will always be greater than the total of the payment column (credit side). The difference will be written on the credit side as “By Balance c/d”. In the beginning of the next period, to show the cash balance in hand, the balance amount is recorded in the debit side as “To balance b/d”.

Illustration 1

Enter the following transactions in a single column cash book of Mr. Kumaran.

2004 Jan	1	Started business with cash	...	Rs.	1,000
	3	Purchased goods for cash	...	Rs.	500
	4	Sold goods	...	Rs.	1,700
	5	Cash received from Siva	...	Rs.	200
	12	Paid Balan	...	Rs.	150
	14	Bought furniture	...	Rs.	200
	15	Purchased goods from Kala on credit	...	Rs.	2,000
	20	Paid electric charges	...	Rs.	225
	24	Paid salaries	...	Rs.	250
	28	Received commission	...	Rs.	75

Solution:

Cash Book of Mr. Kumaran

Date	Particulars	R. N.	L. F.	Amount Rs.	Date	Particulars	V. N.	L. F.	Amount Rs.
2004				1,000	2004				
Jan 1	To Capital A/c				Jan 3	By Purchases			
4	To Sales A/c			1,700	12	A/c			500
5	To Siva A/c			200					150
28	To Commission A/c			75	14	„ Balan A/c			200
					20	„ Furniture A/c			225
						„ Electric charges A/c			250
					24				1,650
					31	„ Salaries A/c			2,975
				2,975					2,975



Jan. 1	Cash in hand	4,000
6	Cash Purchases	2,000
10	Wages paid	40
11	Cash Sales	6,000
12	Cash received from Suresh and allowed him discount	1,980 20
19	Cash paid to Meena and discount received	2,470 30
27	Cash paid to Radha	400
28	Purchased goods for cash	2,070

Double Column Cash Book of Mr.Gopalan
(Cash book with Discount Column)

R. L.	Date	Particulars	V. L.	Amount	Discount	Amount
	31 Jan	By Purchases		4,000		4,000
	10	A/c By Wages		6,000		6,000
	10	A/c By Meena		1,980	20	2,000
	27	A/c By Radha		400		400
	28	A/c				2,070
	31	By Purchases				5,000
		A/c		11,980	30	11,980
		Balance c/d		5,000		5,000



Particulars	To Balance b/d To Sales A/c To Suresh A/c
Date	2004 Jan 1 11 12

ii. Cash Book with Cash and Bank Columns

When bank transactions are more in number, it is advisable to open a cash book by providing a separate column on either side of the cash book to record the bank transactions therein.

In such case, it is not necessary to open a separate Bank Account in the Ledger because the two columns in the cash book serve the purpose of Cash Account and Bank Account respectively. It is a combination of Cash Account and Bank Account. The format of this cash book is given below

Format

Double Column Cash Book

(Cash book with Discount and Cash Column)

Debit Side
Side

Credit

Date	Particulars	R. N.	L. F.	Dis- count Allowed Rs.	Rs.	Date	Particulars	V. N.	L. F.	Dis- count Received Rs.	Rs.

It should be noted that in the double column cash book, cash column is balanced like any



other ledger account. But the discount column on each side is merely totalled. The total of the discount column on the debit side shows the total discount allowed to customers and is debited to Discount Allowed Account. The total of the discount column on the credit side shows total discount received and is credited to Discount Received Account.

Illustration 2: Prepare a Double Column Cash Book from the following transactions of Mr. Gopalan:

		Rs.
2004		
Jan. 1	Cash in hand	4,000
6	Cash Purchases	2,000
10	Wages paid	40
11	Cash Sales	6,000
12	Cash received from Suresh and allowed him discount	1,980 20
19	Cash paid to Meena and discount received	2,470 30
27	Cash paid to Radha	400
28	Purchased goods for cash	2,070

Double Column Cash Book of Mr. Gopalan

(Cash book with Discount Column)

Date	Particulars	V. L.	Discou nt	Amou nt
2004				
Jan 1	By Purchases			4,000
6	A/c By Wages			40
10	A/c By Meena		30	2,470
11	A/c By Radha			400
12	A/c			2,070
19	By Purchases			5,000
27	A/c			
28	By			
31	A/c		30	11,980
	Balance c/d			



Date	Particulars	R.	L.	Amount
2004 Jan 1	To Balance			4,000
11	b/d To Sales			6,000
12	To A/c Suresh A/c		20	1,980
				11,980
				5,000

Cash Book with Cash and Bank Columns

When bank transactions are more in number, it is advisable to open a cash book by providing a separate column on either side of the cash book to record the bank transactions therein.

In such case, it is not necessary to open a separate Bank Account in the Ledger because the two columns in the cash book serve the purpose of Cash Account and Bank Account respectively. It is a combination of Cash Account and Bank Account. The format of this cash book is given below.

Double Column Cash Book

Debit Side (Cash book with Cash and Bank Columns) Credit Side

Date	Particulars	R	L	Cash Rs.	Bank Rs.	Date	Particulars	V.	L.	Cash Rs.	Bank Rs.
		N	F					N.	F.		
		.	.								
		.	.								



--	--	--	--	--	--	--	--	--	--	--

There are two amount columns on debit side one for cash receipts and the other for bank deposits (i.e., payment made into Bank Account). Similarly there are two amount columns on the credit side, one for payments in cash and the other for payments by cheques respectively.

Contra Entry

When an entry affect both cash and bank accounts it is called a **contra entry**. Contra in Latin means *opposite*. In contra entries both the debit and credit aspects of a transaction are recorded in the cash book itself

Example 1: Cash paid into bank

Bank A/c	Dr.	x x x	
To Cash A/c			x x x

(Cash paid into bank)

This is a contra entry. As the cash book with cash and bank columns is a combined cash and bank account, both the aspects of the transaction will be entered in the same book. In the debit side 'To Cash A/c' will be entered in the particulars column and the amount will be entered in the bank column. In the credit side 'By Bank A/c' will be entered in the particulars column and the amount will be entered in the cash column.

Such contra entries are denoted by writing the letter 'C' in the L.F. column, on both sides of the cash book. They indicate that no posting in respect thereof is necessary in the ledger.

Example 2: Cash withdrawn from bank for office use.



Cash A/c	Dr.	x x x
To Bank A/c		x x x
(Cash withdrawn for office use)		

This is also a contra entry. In the debit side 'To Bank A/c' will be entered in the particulars column and the amount will be entered in the cash column. In the credit side 'By Cash A/c' will be entered in the particulars column and the amount will be entered in the bank column.

Such contra entries are denoted by writing the letter 'C' in the L.F. column, on both sides of the cash book. They indicate that no posting in respect thereof is necessary in the ledger.

Illustration 3

Enter the following transactions in the double column cash book of Mr. Rajesh and balance it.

2003

Aug. 1 Opening Balance : Cash in Hand Rs.4,250
Cash at Bank Rs.13,750

- 2 Paid to petty cashier Rs.2,500
- 2 Cash sales Rs.1,750
- 3 Paid to Arun by cheque Rs.3,750
- 3 Received a cheque from Mr. Ram Babu Rs.4,500 paid into bank.
- 5 Received cheque from Mr. Jayaraman Rs.6,000 paid into bank
- 8 Cash purchases Rs.2,500
- 8 Paid rent by cheque Rs. 2,500
- 9 Cash withdrawn from bank for office use Rs.2,500
- 10 Cash sales Rs.3,750
- 14 Stationery purchased Rs.1,000
- 20 Cash sales Rs.6750
- 21 Paid into bank Rs.10,000
- 23 Withdrew cash for personal use Rs.1,000



25 Salaries paid by cheque Rs.9000.

Solution:

Double Column Cash Book of Mr.Rajesh

(Cash book with Cash and Bank Column)

Date	Particulars	R.	L.	Cash	Bank	Date	Particulars	V.N.	L.	Cash	Bank
2003						2003					
Aug 3	To Balance b/d			4,250	13,750	Aug 7	By Petty Cash A/c			2,500	3,750
1	Sales A/c					8	Arin's A/c				0
2	" Ram Babu's A/c			1,750	4,500	8	Purchases A/c			2,500	2,500
3	" Jayaramans A/c				6,000	9	Rent A/c		C		0
5	" Jayaramans A/c				0	14	Cash A/c				2,500
9	Bank A/c		C	2,500		21	Stationery A/c			1,000	0
10	Sales A/c					23	Bank A/c				0
20	Sales A/c		C	3,750		25	Drawings A/c		C	19,000	34,250
21	" Cash A/c			19,000	34,250	31	Salary A/c			3,000	15,500
				3,000	15,500						

Points to be remembered while preparing cash Book



S. No.	Transaction	Debit/Credit side of cash book	The column in which the amount to be entered
1.	Cash/ M.O./P.O. - received	Debit	Cash
2.	Cash paid	Credit	Cash
3.	Discount allowed	Debit	Discount allowed
4.	Discount received	Credit	Discount received
5.	Cash deposited in the bank	Debit (C) Credit (C)	BankCash
6.	Cash withdrawn for office use	Debit (C) Credit (C)	CashBank
7.	Cheque received	Debit	Cash
8.	Cheque deposited into bank	Debit (C) Credit (C)	BankCash
9.	Cheque received and deposited into bank for collection immediately	Debit	Bank
10.	Cheque issued	Credit	Bank
11.	Customer directly paid into bank	Debit	Bank
12.	Cheque deposited and dishonoured	Credit	Bank
13.	Cheque issued and dishonoured	Debit	Bank
14.	Bank charges	Credit	Bank
15.	Interest allowed by bank	Debit	Bank
16.	Interest on overdraft	Credit	Bank
17.	Payments directly made by the bank as per standing instructions	Credit	Bank
18.	Amounts directly received by bank as per standing instructions	Debit	Bank



TRIPLE COLUMN CASH BOOK

Large business concerns receive and make payments in cash and by cheques. Where cash discount is a regular feature, a Triple Column Cash Book is more advantageous. This cash book has three amount columns (cash, bank and discount) on each side. All cash receipts, deposits into bank and discount allowed are recorded on debit side and all cash payments, withdrawals from bank and discount received are recorded on credit side.

Format:

Triple Column Cash Book of Mr.....

(Cash book with Discount, Cash and Bank Columns)

Ban k	
Cas h	
Dis .	Rec
V L. F.	
V .	
Particulars	
Date	
Ban k	
Cas h	
Di s. All	
R L. F.	
.	



Particulars	
Date	

Illustration 4

Compile three column cash book of Mr.Sundar from the following transactions:
2002

Aug 1 Sundar started business with cash Rs.2,00,000

2 Deposited into Bank Rs.50,000.

4 Cash purchases Rs.5,000.

5 Purchases by cheque Rs.6,000.

6 Goods sold to Nathan on credit Rs. 5,000.

8 Received cheque from Mano Rs.490, Discount allowed Rs.10.

10 Paid carriage Rs.1,000.

12 Withdrew from Bank for office use Rs.10,000.

15 Paid to Sundari Rs.4,960, Discount allowed by her Rs.40.

20 Received a cheque for Rs.4950 from Nathan in full settlement of his account, which is deposited into Bank

Solution:

Triple Colum Cash Book of Mr. Sundar

Dr.

Cr.

Date	Particulars	R. N.	L.F.	Dis. Allo-wed	Cash Rs.	Bank Rs.	Date	Particulars	V. N.	L.F.	Dis. Recei-ved	Cash Rs.	Bank Rs.
2002							2002						
Aug 1	To Capital A/c				2,00,000		Aug 2	By Bank A/c		C		50,000	
2	„ Cash A/c		C			50,000	4	„ Purchases A/c				5,000	
8	„ Mano's A/c			10	490		5	„ Purchases A/c					6,000
12	„ Bank A/c		C		10,000		10	„ Carriage A/c				1,000	
20	„ Nathan's A/c			50		4,950	12	„ Cash A/c		C			10,000
							15	„ Sundari's A/c			40	4,960	
							31	„ Balance c/d				1,49,530	38,950



			60	2,10,490	54,950				40	2,10,490	54,950
Sep 1	To Balance b/d			1,49,530	38,950						

Note: Transaction dated 6th August will not appear in the cash book as it is a credit transaction.

Illustration 5

Enter the following transactions in three column cash book of Mr.Muthu and balance the same.
2003

- Aug 1 Cash in hand Rs.75,000
- 1 Cash at bank Rs.40,000
- 4 Paid into bank Rs.20,000.
- 6 Purchased machinery by cheque Rs.10,000.
- 8 Received from Mohan Rs.2,560 , Discount allowed Rs. 40.
- 10 Paid to Somu by cheque Rs.3,970 in full settlement of his account Rs.4,000.
- 11 Withdrew cash from Bank for personal use Rs.5,000.
- 15 Received cheque from Balan Rs.4,900. Allowed him discount Rs.100.
- 19 Balan's cheque deposited into Bank
- 24 Anandan our customer has paid directly into our bank account Rs.10,000.
- 27 Rent paid by cheque Rs.3,000

Solution:

Triple column cash book of Mr. Muthu

Bank Rs.		10,000	20,000	5,000	3,000	52,930	74,900
Cash Rs.			20,000		4,900	57,560	82,460
Dis. Recei-ved Rs.			30				30
L.F.		C		C			
V. N.							



Date	Particulars	R.	L.F.	Dis. Allo- wed Rs.	Cash Rs.	Bank Rs.
					75,000	
			C			20,000
				100	4,900	
			C			10,000
24	Anandan's A/c					
						10,000
27	Rent A/c					
						10,000
31	Balance c/d					
				140	82,460	74,900
					57,560	52,930
Sep 1	To Balance b/d					

Illustration 6

Prepare three column cash book of Mrs.Eswari from the following transactions and balance the cash book on 30th June 2003.

- 2003
- June 1 Cash in hand Rs.50,000
- Bank overdraft Rs.15,000
- 3 Paid into bank Rs.25,000
- 5 Parthiban settled his account for Rs.3,750 by giving a cheque for Rs.3,690.
- 8 Parthiban's cheque sent to bank for collection.
- 10 Cash withdrawn from bank Rs.8,000.
- 14 Parthiban's cheque returned dishonoured
- 15 Received from Ramesh a currency note for Rs.5,000 and gave him a change for it.
- 18 Paid rent Rs.500.
- 20 Bank charges as per pass book Rs.150.
- 30 Deposited into Bank all cash in excess of Rs.5,000



Solution:

Triple column Cash book of Mrs.Eswari

Dr.

Cr.

Date	Particulars	R. N.	L.F.	Dis. Allo -wed	Cash Rs.	Bank Rs.	Date	Particulars	V. N.	L.F.	Dis. Recei -ved	Cash Rs.	Bank Rs.
2003							2003						
June 1	To Balance b/d				50,000		June 1	By Balance b/d					15,000
3	„ Cash A/c		C			25,000	3	„ Bank A/c		C		25,000	
5	„ Parthiban's A/c			60	3,690		8	„ Bank A/c		C		3,690	
8	„ Cash A/c		C			3,690	10	„ Cash A/c		C			8,000
10	„ Bank A/c		C		8,000		14	„ Parthiban's A/c					3,690
30	„ Cash A/c		C			27,500	18	„ Rent A/c				500	
							20	„ Bank Charges					150
							30	„ Bank A/c		C		27,500	
							30	„ Balance c/d				5,000	29,350
				60	61,690	56,190						61,690	56,190
July 1	To Balance b/d				5,000	29,350							

Note: Transaction dated 15th June will not be recorded in the cash book

Petty Cash Book

Petty Cashier received Rs. 600 on April 1, 1999 from the head cashier. Prepare a Petty cash book on the imprest system for the month of April 1999 from the following items:

	Rs.
3 Stamps Taxi fare	50
5 Pencils & Pads	100
6	
7 Speed Post	75
10	
Telegram	25
12	
Registry Refreshment	45
15	
Auto fare	35



16		55
	Typing Paper	
19		20
	Bus fare	60
20		15
	Trunk calls	43
22		
	Office cleaning	18
25		
	Courier Services	17
30		

Show the analysis of payments as Postage & Stamps, Telephone and Telegrams, Conveyance, Stationery and Sundry expenses. Assume imprest amount of Rs. 600.

Amount Received	CBF.N	Date	Particulars	V.N	Total payment	Postage & Stamps	Telephone & Telegram	Conveyance	Stationery	Sundries
600		1999	To Cash		-					
		Apr								
		1	By Stamps		50	50				
		3								
		5	By Taxi fare		100			100		
		6	By Pencils & Pads		75				75	
		7			25	25				
		10	By Registry		45	45				
		12	By Speed post		35		35			
		15	By Telegram		55					55
		16	By Refreshment		20			20		
		19	By Auto fare		60				60	
		20	By Typing paper		15			15		
		22	By Bus Fare		43		43			
		25	By Trunkcalls		18					18
		30	By Office Cleaning		17	17				
		30			558	137	78	135	135	73
		May	By Courier Services		42					
600		1	By Balance C/d		600					
42			1 To Balance b/d							
558			To Cash							

The Journal Entry will be as follows:



Date	Particulars	LF.	Debit	Credit
30-4-99	Postage A/c Dr		137	
	Telephone & telegram A/c Dr		78	
	Conveyance A/c Dr		135	
	Stationery A/c Dr		135	
	Sundry Expenses A/c Dr		73	
	To Petty Cash A/c			558
	[Being the analysis of Petty Cash book for the month of April]			

Problems:

1. Enter the following transactions in the Purchase Book of M/s. Subhashree.

2003

- March 1 Purchased 100 Kg. of coffee seeds from Suresh @ Rs.40 per Kg.
5 Purchased 80 Kg. of tea dust from Hari @ Rs.20 per Kg.
12 Bought from Rekha Sugars, Trichy 1,200 Kg. of Sugar @ Rs.8 per Kg.
18 Bought from Perumal Sweets, Chennai, 40 tins of Sweets @ Rs.200 per tin.
20. Purchased from Govinda Biscuit Company, Chennai 20 tins of biscuits @ Rs.400 per tin.

[Answer : Purchases book total Rs.31,200]

2. From the following particulars prepare the sales book of Modern Furniture Mart

2003

- June 5 Sold on credit to Arvind & Co.
20 tables @ Rs.600 per table
20 chairs @ Rs.300 per chair
7 Cash sales to Anand & Co.,
10 tables @ Rs.300 per table
20 chairs @ Rs.150 per chair
10 Sold to Baskar & Co., on credit
10 almirahs @ Rs.3,000 per almirah
10 tables @ Rs.200 per table
15 Sold old typewriter for Rs.1,000 to Madan on credit
20. Sold to Gopinath on credit.



10 tables @ Rs.1,000 per table
2 revolving chairs @ Rs.1,200 per chair

[Answer : Sales book Rs.62,400]

3. Enter the following transactions in proper subsidiary books.2003

March 1 Purchased goods from Balaraman Rs.2000
2 Sold goods to Senthil Rs.1,000
3 Goods purchased from Durai Rs.1,000
5 Sold goods to Saravanan Rs.700
8 Sold goods to Senthil Rs.500
10 Purchased goods from Elangovan Rs.600
14 Purchased goods from Parthiban Rs.300
20 Sold goods to Sukumar Rs.600

[Answer : Purchase book Rs.3,900; Sales book Rs.2,800]

4. Record the following transactions in the proper subsidiary books of M/s.Ram & Co., and post them to the ledger.

2003

April 1 Goods sold to Ramesh Rs.1,000
5 Sold goods to Kumar Rs.2,200
8 Sold goods to Shankar Rs.300
10 Goods returned by Kumar Rs.600
15 Credit Note sent to Shankar for Rs.200 being the invoice overcharged.

[Answer : Sales book Rs.3,500; Sales return book Rs.800]

5. Write the following transactions in proper subsidiary books of Mr.Rajasekaran.

2003

May 10 Purchased goods from Raman Rs.15,000
14 Returned goods to Raman Rs.500
18 Purchased goods from Sekaran Rs.10,000
20 Pradeep sold goods to us Rs.20,000
24 Sent a debit note to Sekaran for goods damaged in transit Rs.1,000.

[Answer : Purchases book Rs.45,000; Purchases return book Rs.1,500]

6. Enter the following transactions in the proper subsidiary books of Mr.Somu

2003

Nov. 1 Bought from Gopal 300 bags of wheat Rs.1,000 per bag less trade discount 10%



- 3 Purchased from Madhavan 150 bags of rice Rs.900 per bag less trade discount 10%
- 5 Returned to Gopal 10 bags of wheat which were purchased on 1.11.03.
- 7 Sold to Shiva 50 bags of rice Rs.1,200 per bag less Trade Discount 5%.
- 12 Sold to Sharma 25 bags of Wheat Rs.1,300 per bag less Trade Discount 10%.
- 14 Returned 15 bags of rice to Madhavan.
- 15 Shiva returned 5 bags of rice.
- 17 Bought from Rajan 200 bags of wheat Rs.950 per bag
- 24 50 bags of wheat returned to Rajan

[Answer : Purchases book Rs.5,81,500; Sales book Rs.86,250; Purchases return book Rs.68,650; Sales return book Rs.5,700]

7. Enter the following transactions in the appropriate Special Journal of M/s. Sita & Co.

2002

- Oct 2 Bought goods from Satish Rs.2,400 as per invoice No.63.
- 4 Sold to Sivagami goods Rs.1,600 as per invoice No.71.
- 7 Returned to Satish goods of Rs.250 as per debit note No.4
- 8 Sivagami returned goods Rs.150 as per credit note No.8
- 12 Sold to Vijaya goods of Rs.950 as per invoice No.72
- 14 Purchased from Velan goods worth Rs.1,100
- 18 Returned to Sampath goods of Rs.150 as per debit note No.5
- 22 Vijaya returned goods of Rs.240 Credit Note No.9

[Answer : Purchases book Rs.3,500; Sales book Rs.2,550; Purchases return book Rs.400; Sales return book Rs.390]



UNIT-IV

FINAL ACCOUNTS

Introduction:

While the Trial Balance checks the accuracy of ledger balances, the final account reveals two facts:

1. Whether the business is in profit or loss during the period covered by the Trial Balance. A Trading and Profit & Loss account also known as income statement is prepared for this purpose.
2. What is the financial position (financial position means picture of assets and liabilities) of the business? This is judged by preparing a balance sheet for the business.

Thus, income statement represents the summary of all the expenses and incomes occurred during the financial year whereas balance sheet represents the financial position of the concerned organization at a particular point of time, usually at the end of financial year *i.e.*, 31st March (in India, financial year starts from 1st April to 31st March).

Trading Account:

Trading means buying and selling. The trading account shows the result of buying and selling of goods.

Specimen

Trading Account for the year ending 31st March, 2021

Dr.

Cr.

<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Opening stock	—	By Sales (less return)	—
To Purchases (less return)	—	**By Gross loss b/d	—
To Direct wages	—		(Balancing fig.)
To Direct expenses	—		
- Carriage inward			
- Duty and clearing charges			



- Fuel and energy		
- Octroi duty	etc.	
To Gross profit (GP) b/d	_____	
	(Balancing fig.)	
Total	=	Total =

Items appearing in the debit side of Trading account

1. Opening stock

Stock on hand at the beginning of the year is termed as opening stock. The closing stock of the previous accounting year is brought forward as opening stock of the current accounting year. In the case of new business, there will not be any opening stock.

2. Purchases

Purchases made during the year, includes both cash and credit purchases of goods. Purchase returns must be deducted from the total purchases to get net purchases.

3. Direct expenses

Expenses which are incurred from the stage of purchase to the stage of making the goods in saleable condition are termed as direct expenses. Some of the direct expenses are:

- i. Wages: it means remuneration paid to workers
- ii. Carriage or carriage in wards: It means the transportation charges paid to bring the goods from the place of purchase to the place of business.
- iii. Octroi duty: Amount paid to bring the goods within the municipal limits.
- iv. Customs duty, dock dues, clearing charges, import duty etc.,: These expenses are paid to the Government on the goods imported.
- v. Other expenses: Fuel, power, lighting charges, oil, grease, waste related to production and packing expenses.

Items appearing in the credit side of Trading account

1. Sales

This includes both cash and credit sale made during the year. Net sales is derived



by deducting sales return from the total sales.

2. Closing stock

Closing stock is the value of goods which remain in the hand of the trader at the end of the year. It does not appear in the trial balance. It appears outside the trial balance. (As it appears outside the trial balance, first it will be recorded in the credit side of the trading account and then shown in the assets side of the balance sheet).

Balancing

The difference between the two sides of the trading account indicates either gross profit or gross loss. If the credit side total is more, the difference represents gross profit. On the other hand, if the total of the debit side is more, the difference represents gross loss. The gross profit or gross loss is transferred to profit & loss account.

Closing entries

Like ledger accounts, trading account will be closed by transferring the gross profit or gross loss to the profit and loss account.

If Gross Profit

Journal Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Trading a/c Dr.		***	
	To Profit & Loss a/c			***
	(Gross profit transferred to Profit and loss a/c)			

If Gross Loss

Journal Entry



Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Profit & Loss a/c Dr. To Trading a/c (Gross loss transferred to Profit and loss a/c)		***	***

Profit and Loss Account

After calculating the gross profit or gross loss the next step is to prepare the profit and loss account. To earn net profit a trader has to incur many expenses apart from those spent for purchases and manufacturing of goods. If such expenses are less than gross profit, the result will be net profit. When total of all these expenses are more than gross profit the result will be net loss.

Specimen:

Profit and Loss Account for the year ending 31st March, 2015

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Gross Loss b/d (Transferred from trading a/c)	***	By Gross profit b/d (Transferred from trading a/c)	***
To Salaries	***	By Commission earned	
To Rent & Rates		By Rent received	***

To Stationeries	***	By Interest received	***
To Postage expenses	***	By Discount received	***
To Insurance	***	To Net Loss	***
To Repairs expenses	***	(Transferred to capital a/c)	



To Office expenses	***		
To Interest paid	***		
To Bank charges	***		
To Sundry expenses	***		
To Commission paid	***		
To Discount allowed	***		
To Advertisement	***		
To Carriage outwards	***		
To Travelling expenses	***		
To Distribution expenses	***		
To Repacking charges	***		
To Bad debts	***		
To Depreciation	***		
To Net profit (Transferred to capital a/c)	***		
	***		***

Items appearing in the debit side of Profit and Loss account

Those expenses which are chargeable to the normal activities of the business are recorded in the debit side of profit and loss account. They are termed as Indirect expenses.

1. Office and Administrative expenses

Expenses incurred for the functioning of an office are office and administrative expenses – office salaries, office rent, office lighting, printing and stationery, postage, telephone charges etc.,

2. Repairs and Maintenance expenses

These expenses relates to the maintenance of assets – repairs and renewals, depreciation etc.,



3. Financial expenses

Expenses incurred on borrowings – interest paid on loan.

4. Selling and Distribution expenses

All expenses relating to sales and distribution of goods – Advertising, travelling expenses, salesmen salary, commission paid to salesmen, discount allowed, repacking charges etc.,

Items appearing in the credit side of Profit and Loss account

Besides the gross profit, other gains and incomes of the business are shown on the credit side. The following are some of the incomes are gains.

- 1) Interest received on investment
- 2) Interest received on fixed deposits
- 3) Discount earned
- 4) Commission earned
- 5) Rent received

Balancing

The difference between the two sides of profit and loss account indicates either net profit or net loss. If the total on the credit side is more the difference is called net profit. On the other hand if the total of debit side is more the difference represents net loss. The net profit or net loss is transferred to capital account.

Closing entries

Profit and loss account should be closed by transferring the net profit or net loss to capital account.



If Net Profit

Journal Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Profit & Loss a/c Dr. To Capital a/c (Net profit transferred to capital a/c)		***	***

If Net Loss

Journal Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
	Capital Dr. To Profit & Loss a/c (Net loss transferred to Profit and loss a/c)		***	***

BALANCE SHEET

This forms the second part of the final accounts. It is a statement showing the financial position of a business. Balance sheet is prepared by taking up all personal accounts and real accounts (assets and properties) together with the net result obtained from profit and loss account. On the left hand side of the statement, the liabilities and capital are shown. On the right hand side, all the assets are shown. Balance sheet is not an account but it is statement prepared from the ledger balances. So we should not prefix the accounts with the words “To” and “By”

Balance sheet is defined as „a statement which sets out the assets and liabilities of a



business firm and which serves to ascertain the financial position of the same on any particular date".

Specimen

Balance sheet as on 31st March 2021

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital	***	Cash in hand	***
Add:		Cash at bank	***
Net Profit	***	Bills receivable	***
	***	Sundry debtors	***
(Or)		Investments	***
Less:		Closing stock	***
Net Loss	***	Prepaid expenses	***
	***	Furniture & fittings	***
Less: Drawings	***	Plant & machinery	***
Less:	***	Land & buildings	***
Income Tax		Business premises Patents & Trade marks	***
	***		***
Sundry creditors	***	Goodwill	***
Bills payable	***		
Bank overdraft	***		
Loan	***		
Reserve fund	***		
Outstanding expenses	***		
	***		***

Assets



Assets represents everything which a business owns and has money value. In other words, asset includes possessions and properties of the business. Asset are classified are as

1. Tangible assets
2. Intangible assets
3. Fictitious assets
4. Wasting Assets

1. Tangible assets

Assets which have some physical existence are known as tangible assets. They can be seen, touched and felt, e.g. Plant and Machinery tangible assets are classified into

- a) Fixed assts
- b) Current assets or Floating Assets

a) Fixed assets

Assets which are permanent in nature having long period of life and cannot be converted into cash in a short period are termed as fixed assets.

b) Current assets or Floating Assets

Assets which can be converted into cash in the ordinary course of business and are held for a short period is known as current assets. This is also termed as floating assets. For example, cash in hand, cash at bank, sundry debtors etc.

2. Intangible assets

The assets which have no physical existence and cannot be see or felt. They help to generate revenue in future, e.g., goodwill, patents trademarks, etc.,

3. Fictitious assets

These assets are nothing but the unwritten off losses or non-recoupable expenses. They are really not assets but are worthless items. For example: Preliminary expenses.



4. Wasting assets

These assets which certainly lose value with usage are termed as wasting assets. Mines, forests etc., become waste once the mineral is fully extracted or the timber is fully cut.

LIABILITIES

The amount which a business owes to other is liabilities. Credit balance of personal and real accounts together with the capital account and liabilities.

1. Long Term liabilities
2. Current liabilities
3. Contingent liabilities

1. Long Term liabilities

Liabilities which are repayable after a long period of time are known as long term liabilities. For example, capital, long term loans etc.,

2. Current liabilities

Current liabilities are those which are repayable within a year. For example, creditors for goods purchased, short term loans etc.,

3. Contingent liabilities

It is an anticipated liability which may or may not arise in future. For example, liability arising for bills discounted. Contingent liabilities will not appear in the balance sheet. But shown as foot note

Difference between Trial Balance and Balance Sheet

No.	Basis Distinction	Trial balance	Balance sheet
1.	Objective	To know the arithmetical accuracy of the accounting Work	To know the true and fair financial position of the Business



2.	Format	The columns are debit balances and credit balances	The two sides are assets and Liabilities
3.	Content	It is summary of all the ledger balances – personal, real and nominal account	It is statement showing closing balances of personal & real accounts
4.	Stage	It is the middle stage in the preparation of accounts	It is the last stage in the preparation of accounts
5.	Period	It can be prepared periodically say at the end of the month, quarterly or half yearly etc.,	It is generally prepared at the end of the accounting period
6.	Preparation	It is prepared before the preparation of trading, profit and loss account.	It is prepared after the preparation of trading, profit and loss account.

Illustration: 1

Prepare a trading account from the following information of a trader.

Total purchases made during the year 2022 Rs. 3,00,000 Total sales made during the year 2022 Rs. 4,00,000

Solution:

Trading Account for the year ending 31st March 2022

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.



To Purchases	3,00,000	By Sales	4,00,000
Gross profit c/d (transferred to P & L a/c)	1,00,000		
	4,00,000		4,00,000

Illustration: 2

From the following information, prepare a trading account for the year ended 31.12.2022

Particulars	Amount
Opening stock	16,000
Purchases	16,500
Sales	40,600
Closing stock	13,500

Solution:

Trading Account for the year ending 31.12.2022



Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	16,000	By Sales	40,600
To Purchases	16,500	By Closing stock	13,500
To Gross profit c/d (transferred to P & L a/c)	12,600		
	45,100		45,100

Illustration: 3

Prepare trading account for the year ending 31st March 2022 from the following information.

Solution:

	Rs.
Opening stock	1,70,000
Purchase returns	10,000
Sales	2,50,000
Wages	50,000
Sales returns	20,000
Purchases	1,00,000
Carriage inwards	20,000
Closing stock	1,60,000



Trading Account for the year ending 31st March 2022

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.	Particulars
To Opening stock		1,70,000		By Sales
To Purchases 1,00,000				Less
Less:				Sales return
Purchases return	10,000	90,000		20,000
To wages		50,000		By Closing stock
To Carriage inwards		20,000		1,60,000
To Gross profit c/d (transferred to P & L a/c)		60,000		
		3,90,000		3,90,000

Illustration: 4

Prepare profit and loss account, from the following balances of Mr. RAM for the year ending 31.12.2022.

	Rs.		Rs.
Office rent	30,000	Salaries	80,000
Printing expenses	2,000	Stationeries	3,000
Tax, Insurance	4,000	Discount allowed	6,000



Advertisement	36,000	Travelling expenses	26,000
Gross profit	2,50,000	Discount received	4,000

Solution:

Profit and Loss Account of Mr. RAM for the year ending 31st December 2022

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Office rent	30,000	By Gross profit b/d	2,50,000
To Printing expenses	2,000	(transferred from the	
To Tax, Insurance	4,000	trading a/c)	
To Advertisement	36,000	By Discount received	4,000
To Salaries	80,000		
To Stationeries	3,000		
To Discount allowed	6,000		
To Travelling expenses	26,000		
To Net profit	67,000		
(transferred to capital a/c)			
	2,54,000		2,54,000

Illustration: 5

From the following trial balance of M/s Ram & Sons, prepare trading and profit and loss account for the year ending on 31st March 2012 and the balance sheet as on the date

Trial balance as on 31st March 2012



Particulars	Debit	Credit
	Rs.	Rs.
Opening stock (1.4.2011)	5,000	
Purchases	16,750	
Discount allowed	1,300	
Wages	6,500	
Sales		30,000
Salaries	2,000	
Travelling expenses	400	
Commission	425	
Carriage inwards	275	
Administration expenses	105	
Trade expenses	600	
Interest	250	
Building	5,000	
Furniture	200	
Debtors	4,250	
Creditors		2,100
Capital		13,000
Cash	2,045	
	45,100	45,100

Stock on 31st March 2012 was Rs. 6,000

Solution:

M/S Ram & Sons Trading and Profit and Loss Account for the year ending 31st

March 2012



Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	5,000	By Sales	30,000
To Purchases	16,750	By Closing stock	6,000
To Wages	6,500		
To Carriage inwards	275		
To Gross profit c/d (transferred to P & L a/c)	7,475		
	36,000		36,000
To Discount allowed	1,300	By Gross profit b/d	7,475
To Salaries	2,000	(transferred from the	
To Travelling expenses	400	trading a/c)	
To Commission	425		
To Administration expenses	105		
To Trade expenses	600		
To Interest	250		
To Net profit (transferred to capital a/c)	2,395		
	7,475		7,475

Balance sheet as on 31st March 2012

Liabilities	Amount Rs.	Assets	Amount Rs.



Capital	13000		Cash	2,045
Add:			Debtors	4,250
Net Profit	2395	15,395	Stock	6,000
Creditors		2,100	Furniture	200
			Building	5,000
		17,495		17,495

Adjustments:

Some important and common items, which need to be adjusted at the time of preparing the final accounts are discussed below.

<i>S.No.</i>	<i>Particulars</i>	<i>L. F.</i>	<i>Debit (Rs.)</i>	<i>Credit (Rs.)</i>
1.	Closing stock A/c ...Dr. To Trading A/c			
2.	Expenses A/c ...Dr. To Outstanding expenses A/c			
3.	Prepaid expenses A/c ...Dr. To Expenses A/c			
4.	Accrued income A/c ...Dr. To Income A/c			
5.	Income A/c ...Dr. To Unearned income A/c			
6.	Depreciation A/c ...Dr. To Asset A/c			
7.	Bad Debts A/c ...Dr. To Debtors A/c			
8.	P & L A/c ...Dr. To Provision for bad debts A/c			
9.	P & L A/c ...Dr. To Provision for discounton debtors A/c			



10.	Provision for discount on creditors A/c To P & L A/c	...Dr.			
11.	Interest on capital A/c To Capital A/c	...Dr.			
12.	Drawing A/c To Interest on drawing A/c	...Dr.			
13.	Interest on loans A/c To Loan A/c	...Dr.			
14.	Loans A/c To Interest on loan A/c	...Dr.			
15.	Loss of Stock A/c Trading A/c or To Purchase A/c	...Dr. To			
16.	Advertisement A/c To Purchase A/c	...Dr.			
17.	Charity A/c To Purchase A/c	...Dr.			

Illustration 6: Prepare a trading and P & L A/c for the year ending 31.03.2021 and a balance sheet as on that date from the following trial balance:

Trial Balance

<i>Particulars</i>	<i>Dr. (Rs.)</i>	<i>Cr. (Rs.)</i>
Opening Stock	16,000	
Capital		45,000
Salaries	13,000	
Drawings	4,000	
Carriage Inwards	500	
Carriage Outwards	1,000	
Sales Return	1,000	
Purchase Return		7,00
Loan to Mr. X	11,000	



Loan from Mr. Y		7,000
Rent	1,300	
Rent Outstanding		200
Purchase	40,000	
Sales		73,100
Debtors	25,000	
Creditors		8,000
Bad Debt	800	
Reserve for Bad Debt		1,200
Discount Allowed/Received	600	
Furniture	11,700	
Wages	500	
Insurance Premium	1,200	
Rent by Sub-letting		800
Cash	700	
Bank	8,000	
Total	1,36,300	1,36,300

Adjustments

1. Closing Stock Rs. 10,500, but the market value of closing stock was Rs. 9,500.
2. Insurance premium prepaid Rs. 200.
3. Loan to Mr. X, given at 10% interest p.a. and loan taken from Mr. Y carries 9% interest p.a.
4. Depreciation is to be provided at 5% on furniture.
5. Goods worth Rs. 500 have been taken by the proprietor for private use.
6. Bad and doubtful debts are to be provided at 10%.

Solution

Trading Account for the Year ending March 31, 2021

<i>Dr.</i>		<i>Cr.</i>	
<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Opening Stock	16,000	By Sales:	73,100
To Purchase: 40,000		0	
Less Return 700	39,000	Less Return: 1,000	72,100
To Carriage Inward 500		By Proprietor ^[I]	500
		By Closing Stock ^[II]	9,500



To Wages	500		
To Gross Profit b/d	25,800		
Total	82,100	Total	82,100

Profit and Loss Account for the Year ending March 31, 2021

Dr.

Cr.

<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Salary	13,000	By Gross Profit c/d (From Trading A/c)	25,800
To Carriage Outward	1,000		
To Rent	1,300		
To Reserve for Bad Debts	2,100	By Discount Received	300
To Discount Allowed:	600	By Rent by Sub-letting	800
To Insurance Premium: 1,200		By Interest Receivable	1,100
Less pre-paid 200	1,000		
To Interest Payable to Mr. Y	630		
To Depreciation A/c:	585		
To Net Profit	7,785		
Total	28,000	Total	28,000

Balance Sheet as on March 31, 2021

<i>Liabilities</i>	<i>Amount</i>	<i>Assets</i>	<i>Amount</i>
Capital 45,000		Fixed Assets:	
Less Drawings [I] 4,000		Furniture 11,700	
Less Goods taken		Less Depreciation 585	
by owner 500		[VI]	11,115
Add Profit during year 7,785		Current Assets:	
	48,285	Loan to Mr. X 11,000	
Loan from Mr. Y [V] 7,000		Add Outstanding	
Add Interest 630		Interest [VII] 1,110	
	7,630		12,100
Rent Outstanding 200		Debtors 25,000	



Creditors	8,000	Less Provision for Bad Debt [III]	2,500	22,500
		Prepaid Insurance [IV]		200
		Cash		700
		Bank		8,000
		Closing Stock [II]		9,500
Total	64,115	Total		64,115

Illustration: 7

From the following trial balance of a trader, make out a Trading and Profit and Loss account and Balance sheet as on 31st March 2014

Particulars	Debit Rs.	Credit Rs.
Sales		4,20,000
Purchases	1,05,000	
Printing charges	2,500	
Wages	77,500	
Salaries	12,500	
Opening stock	2,25,000	
Carriage inwards	8,800	
General expenses	26,250	
Trade marks	5,000	
Rates and taxes	2,500	
Capital		1,74,800
Discount received		1,250



Loan		1,75,000
Buildings	2,00,000	
Furniture	25,000	
Machinery	50,000	
Cash	1,000	
Bank	30,000	
	7,71,050	7,71,050

Adjustments

1. The closing stock was value at Rs. 3,20,000
2. Outstanding salaries Rs. 10,000
3. Prepaid rates & taxes Rs. 500

Solution:

Trading and Profit and Loss Account for the year ending 31st March, 2014 Dr. Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	2,25,000	By Sales	4,20,000
To Purchases	1,05,000	By Closing stock	3,20,000
To Wages	77,500		
To Carriage inwards To	8,800		
Gross profit c/d (Transferred to Profit and Loss a/c)	3,23,700		
	7,40,000		7,40,000



To Printing charges		2,500	By Gross profit b/d (Transferred from trading a/c)	3,23,700
To Salaries	12,500		By Discount received	
Add: Outstanding	10,000	22,500		1,250
To General expenses				
To Rates and taxes	2,500	26,250		
Less: Prepaid	500	2,500		
To Net profit		2,000		
(Transferred to capital a/c)		2,71,700		
		3,24,950		3,24,950

Balance sheet as on 31st March 2014

Liabilities		Amount	Assets	
		Rs.		
Capital	1,74,800		Trade marks	5,000
Add:			Building	2,00,000
Net Profit	2,71,700	446500	Furniture	25,000
Outstanding salary		10000	Machinery	50,000
Loans		175000	Cash	1,000
			Bank	30,000
			Prepaid rates & taxes	500
		631500		6,31,500



Problem 8

From the following ledger balances, prepare trial balance, income statement and balance sheet:

<i>Particulars</i>	<i>Amount</i>
Mr. X's capital	5,00,000
Drawing	20,000
Purchase	2,00,000
Loan	1,00,000
Machinery	50,000
Return to suppliers	50,000
Sales	4,00,000
Return inward	6,00,000
Carriage outward	20,000
Bad debts	5,000
Sundry Drs.	1,00,000
B/R	20,000
Sundry Crs.	50,000
Carriage inward	10,000
Salary and wages	5,000
Depreciation	20,000
Cash in hand	1,00,000
Sale of scrap	5,000
Closing stock	50,000
Prepaid tax	10,000
Outstanding wages	5,000

Open Suspense A/c to balance trial balance if needed.

Solution:

Trial Balance

<i>Particulars</i>	<i>Debit</i>	<i>Credit</i>
Mr. X's Capital	—	5,00,000
Drawing	20,000	—



Purchase	2,00,000	—
Loan	—	1,00,000
Machinery	50,000	—
Return to supplies	—	50,000
Sales	—	4,00,000
Return inward	60,000	—
Carriage outward	20,000	—
Bad debts	5,000	—
Sundry Debtors	1,00,000	—
Bills receivable	20,000	—
Sundry creditors	—	50,000
Carriage inward	10,000	—
Salary and wages	5,000	—
Depreciation	2,000	—
Cash in hand	1,00,000	—
Sale of scrap	—	5,000
Closing stock	50,000	—
Prepaid tax	10,000	—
Outstanding wages	—	5,000
Suspense A/c	4,40,000	—
Total	11,10,000	11,10,000

Trading and P & L A/c

<i>Dr.</i>		<i>Cr.</i>	
<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Purchase	2,00,000	By Sales	4,00,000
Less: Returns	50,000	Less: Returns	60,000
To Direct Expense:			
Carriage inward	10,000		
To Gross profit	1,80,000		
Total	3,40,000	Total	3,40,000

Profit and Loss Account

<i>Dr.</i>		<i>Cr.</i>	
<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Salaries and wages	5,000	By Gross profit	1,80,000
To Depreciation	20,000	By Sale of scrap	5,000
To Carriage outward	20,000		



To Bad debts	5,000		
To Net profit	1,35,000		
Total	1,85,000	Total	1,85,000

Balance Sheet

<i>Liabilities</i>		<i>Amount</i>	<i>Assets</i>		<i>Amount</i>
Capital	5,00,000		Fixed Assets:		
Less: Drawing	20,000		Machinery		50,000
	4,80,000				
Add: Net Profit	1,35,000		Current Assets:		
		6,15,000	B/R		20,000
Loan		1,00,000	Sundry Debtors		1,00,000
Current liability			Cash in hand		1,00,000
Sundry Creditor		50,000	Closing stock		50,000
Outstanding wages		5,000	Prepaid tax		10,000
			Suspense A/c		4,40,000
Total		7,70,000	Total		7,70,000

Problem 9. Prepare final accounts from the trial balance given below:

Trial Balance as on 31st March 2002

<i>Particulars</i>	<i>Debit</i>	<i>Credit</i>
Cash in hand	30	
Purchases	8990	
Cash at bank	885	
Fixtures and fitting	225	
Freehold premises	1500	
Lighting and heating	65	
B/R	825	
Returns inward	30	
Salaries	1075	
Debtors	5700	
Opening stock	3000	
Printing	225	
Rents and taxes insurance	190	



Discount allowed	200	
Capital		7610
Sales		11060
Creditors		1950
B/P		1875
Discount received		445
Total	22940	22940

Additional Information

- Closing stock at the end of year amount Rs. 5000.
- Outstanding wages was Rs. 1000.
- Dep. charges at the rate of 10% on furniture and fixture.

Solution

Trading and P & L A/c

<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Opening stock	3000	Sales (less return)	11030
To Purchase	8990		
To Out. Wages	1000	Closing stock	5000
To Gross profit	3040		
	16030		16030
To Salary	1075	By Gross profit	3040

..

<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Printing	225	By Discount received	445
To Rents and tax insurance	190		
To Discount allowed	200		
To Lighting and heating	65		
To Depreciation	23		
To Net profit	1708		
	3485		3485

Balance Sheet

<i>Liabilities</i>	<i>Amount</i>	<i>Assets</i>	<i>Amount</i>
--------------------	---------------	---------------	---------------



Capital	7610	Furniture and fitting	202
Net profit	9318	Freehold Premises	1500
Creditors	1950	<i>Current assets:</i>	
Bills payable	1875	Cash in hand	30
Out. Wages	1000	Cash at bank	885
		B/R	825
		Drs.	5700
		Current liabilities	5000
Total	14142	Total	14142

Problem 10.

Following is the trial balance as on 30th June 2001.

Trial Balance

<i>Particulars</i>	<i>Debit</i>	<i>Credit</i>
Land and building	20000	
Machinery	50000	
Furniture and fixtures	4000	
Opening stock	16300	
Purchases	80000	
Salaries	6000	
Carriage on sales	1500	
Freight on purchases	2000	
Custom duty on purchases	8000	
Advertising	5400	
Wages	15000	
Rent	3000	
Repairs to Machinery	2000	
Loan to Kumar @ 9%	5000	
Prepaid insurance	200	
Sundry debtors	20000	



Cash in hand	250	
Cash at bank	3100	
Capital		80000
Sundry creditors		8000
Discount received		400
Outstanding expenses		1550
Sales		150500
Repairs and rewards (provision)		6000
Total	246450	246450

The additional information is as follows:

1. Closing stock was worth Rs. 14900.
2. Dep. is to be written of @ 3% on land and building, 10% on machinery and 5% on furniture and fixture.
3. Provision for repairs and renewals are credited with Rs. 1500 every year.
4. Provision for bad debts is 5% on Sundry debtors.

Prepare income statement and balance sheet.

Solution

Trading and P & L A/c
(for the year ending 30th June 2001)

<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Opening stock	16300	By Sales	150500
To Purchase	80000	By Closing stock	14900
To Freight on purchase	2000		
To Custom duty	8000		
To Wages	15000		
To Gross profit	44100		
	165400		165400
To Provision for R and R	1500	By Gross profit	44100
To Depreciation	5800	By Discount received	400
To Carriage on sales	1500		
To Pro. for bad debts	1000		
To Advertisement	5400		
To Salaries	6000		



<i>Particulars</i>	<i>Amount</i>	<i>Particulars</i>	<i>Amount</i>
To Rent	3000		
To Postage and stationary	1500		
To General expenses	3200		
To Repair of machinery	2000		
To Net profit	13600		
Total	44500	Total	44500

Balance Sheet
(as on 30th June 2001)

<i>Liabilities</i>	<i>Amount</i>	<i>Assets</i>	<i>Amount</i>
Capital	8000	Land & Building (less-dep)	19400
Add N.P.	13600	Machinery (less-dep)	45000
Creditors	8000	For Furniture (less-dep)	3800
Outstanding expenses	1550	Prepaid insurance	200
Prov. for Repairs & Rewards	6000	Sundry debtors	
Add: Provision every year	1500	Less: Prov. for bad debts	19000
		Cash in hand	250
		Cash at bank	3100
		Loan to Kumar	5000
		Closing stock	14900
Total	110650	Total	110650

Exercises

1. Record the following transactions in the Journal of Mr.Perumal

2022 Feb.	Rs.
3 Bought goods for cash	84,500
7 Sold goods to Dhanalakshmi on credit	55,000
9 Received commission	3,000
10 Cash sales	1,09,000
12 Bought goods from Mahalakshmi	60,000



15 Received five chairs from Revathi & Co., at Rs. 400	2,000
20 Paid Revathi & Co., cash for five chairs	2,000
28 Paid salaries	10,000
Paid Rent	5,000

2. Enter the following transactions in journal and post them in the Ledger Mr.Rajan and balance on 31st December. 2022

2022 Dec.		Rs.
1	Govindarajan commenced his business with the following assets and liabilities	
	Plant and Machinery	2,50,000
	Stock	90,000
	Furniture	7,000
	Cash	50,000
	Sundry creditors	1,50,000
2	Sold goods to Sundar	1,50,000
3	Bought goods from Natarajan	65,000
4	Sundar paid cash	1,25,000
6	Returned damaged goods to Natarajan	2,000
10	Paid to natarajan	28,000
31	Paid rent	5,000
	Paid salaries	9,000



3. The trial balance of Mrs. Kaviya shows the following balances on March 31, 2022

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Purchase	1,40,000	Capital	2,40,000
Sales returns	10,000	Sales	3,00,000
Opening stock	40,000	Discount received	2,000
Discount allowed	4,000	Commission received	8,000
Bank charges	1,000	Sundry creditors	58,000
Salaries	9,000		
Wages	10,000		
Freight inwards	8,000		
Freight outwards	2,000		
Rent, Rates & Taxes	10,000		
Advertising	12,000		
Cash in hand	2,000		
Plant & machinery	1,00,000		
Sundry debtors	1,20,000		
Cash at bank	1,40,000		
	6,08,000		6,08,000

Adjustments

The closing stock was valued at Rs. 60,000

You are required to prepare the profit and loss account for the year ending 31st March 2022 and the balance sheet as on that date.



(Ans. Gross profit Rs. 1,52,000; Net Profit Rs. 1,24,000;

Balance sheet Rs. 4,22,000))

4. The following balances have been extracted from the books of Mrs. Ganesh as on 31st March, 2022

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Buildings	30,000	Capital Purchase	40,000
Machinery	31,400	returns Sales	2,000
Furniture	2,000	Sundry creditors	2,80,000
Motor car	16,000	Discount received	9,600
Purchases	1,88,000	Provision for bad and doubtful debt	1,000
Sales returns	1,000		
Sundry debtors	30,000		600
General expenses	1,600		
Cash at bank	9,400		
Rates and taxes	1,200		
Bad debts	400		
Insurance premium	800		
Discount allowed	1,400		
Opening stock	20,000		
	3,33,200		3,33,200

Adjustments

- 1) Outstanding rates and taxes Rs. 1,600
- 2) Insurance premium prepaid Rs. 2,000



- 3) Maintain provision for bad and doubtful debts at 5% on debtors
 - 4) Depreciate Motor car by 10%. Furniture by 4% and Buildings by 3% 5) Stock on 31.12.2022
 - 5) Rs. 20,000
- (Ans. Gross profit Rs. 93,000; Net Profit Rs. 83,720;
Balance sheet Rs. 1,34,920))

5. Trial balance of Ramesh Krishna as on 31.03.2021

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Drawings	1,800	Capital	80,000
Buildings	15,000	General reserve	20,000
Furniture & Fittings	7,500	Loan 6%	15,000
Computer	25,000	Sales	1,00,000
Interest on loan	900	Commission received	7,500
Loose tools	6,100	Sundry creditors	10,000
Purchase	75,000		
Stock (1.4.2010)	25,000		
General expenses	15,000		
Freight inwards	2,000		
Freight outwards	1,000		
Sundry debtors	28,000		
Bank	20,200		
Goodwill	10,000		
	2,32,500		2,32,500



Adjustments

- 6) Closing stock is Rs. 32,000
- 7) Depreciate computer @ 10%; Buildings @ 5%; Furniture and Fittings @ 10%
- 8) Provide for bad and doubtful debts @ 5% and for discount on debtors @ 2%.
- 9) Provide interest on drawings @ 6% and on capital @8%

Prepare final accounts for the period after giving effect to the adjustments.

(Ans. Gross profit Rs. 30,000; Net Profit Rs. 8,376;

Balance sheet Rs. 1,37,868)



UNIT -V

DEPRECIATION

INTRODUCTION:

The term 'depreciation' refers to the reduction in or loss of quality or value of a fixed asset through wear or tear in use, effusion of time, obsolescence through technology and market changes or from any other cause. Depreciation take place in case of all fixed assets with certain possible exceptions e.g. land and antiques etc, although the process may be invisible or gradual. Depreciation does take place irrespective of regular repairs and proper maintenance of assets.

The word 'depreciation' is closely related to the concept of business income. Unless it is charged against revenues, we cannot say that the business income has been ascertained properly. This is because of the fact that the use of long-term assets tend to consume their economic value and at some point of time these assets become useless. The economic value so consumed must be recovered from the revenue of the firm to have a proper measure of its income. Hence, the reader's must understand that the process of charging depreciation is the technique used by accountants for recovering the cost of fixed assets over a period.

The following definition will make the understanding of the concept of depreciation more convenient to the learner's. According to IAS-4, "Depreciation is the allocation of the depreciable amount of an asset over its estimated useful life,"

DEFINITION

i. According to AS-6, "depreciation is a measure of wearing out, consumption or other of value of a depreciable asset arising from use, effusion of time or obsolescence through technology and market changes. Depreciation is allocated so as to charge a fair proportion of the depreciable amount in each accounting period during the expected useful life of the



assets. Depreciation includes amortisation of assets whose useful life is pre determined.”

The American Institute of Certified Public Accountants (AICPA) employed the definition as given below:

ii. “Depreciation Accounting is a system of accounting which aims to distribute the cost or other basic value of tangible capital assets, less salvage value (if any) over the estimated useful life of unit (which may be a group of assets) in a systematic and rational manner. It a process of allocation not of valuation. Depreciation for the year is the portion of the total charge under such a system that is allocated to the year.”

From the above definitions, it is clear that each accounting period must be charged with a fair proportion of the depreciable amount of the asset, during the expected useful life of the asset. Depreciable amount of an asset is its historical cost less the estimated residual value. Finally, it could be concluded that depreciation is a gradual reduction in the economic value of an asset from any cause.

Depreciation, Depletion and Amortisation

The terms ‘depreciation’, ‘depletion’ and ‘amortisation’ are used often interchangeably. However, these different terms have been developed in accounting usage for describing this process for different types of assets. These terms have been described as follows:

Depreciation

Depreciation is concerned with charging the cost of man made fixed assets to operation (and not with determination of asset value for the balance sheet). In other words, the term ‘depreciation’ is used when expired utility of physical asset (building, machinery, or equipment) is to be recorded.

Depletion

This term is applied to the process of removing an available but irreplaceable resource such as extracting coal from a coal mines or oil out of an oil well. Depletion



differs from depreciation in that the former implies removal of a natural resource, while the latter implies a reduction in the service capacity of an asset.

Amortisation

The process of writing off intangible assets is termed as amortisation. The intangible assets like patents, copyrights, leaseholds and goodwill are recorded at cost in the books of account. Many of these assets have a limited useful life and are, therefore, written off.

Obsolescence

It refers to the decline in the useful life of an asset because of factors like (i) technological advancements, (ii) changes in the market demand of the product, (iii) legal or other restrictions, or (iv) improvement in production process.

CAUSES OF DEPRECIATION

The depreciation occurs because of the following:

- 1. Constant use:** The constant use of assets results into their wear and tear, which in turn reduces their working capacity. Hence, a decrease in the value of assets may be seen due to reduced capacity. The value of assets like, machinery, furniture, etc., declines with the constant use of them.
- 2. Passage of Time:** Many fixed assets lose their value with the passage of time. This holds true in case of intangible fixed assets such as patents, copy rights, lease hold properties, etc. The term “amortisation” is generally used to indicate the reduction in the value of such assets.
- 3. Depletion:** Depletion also causes decline in the value of certain assets. This is true in case of wasting assets such as mines, oil wells and forest-stands. On account of continuous extraction of minerals or oils, these assets go on declining in their value and finally they gets completely exhausted.



4. **Obsolescence:** There may not be any physical deterioration in the asset itself. Despite of this, there may be reduction in the utility of an asset that results from the development of a better method, machine or process. For example, an old machine which is still in good working condition may have to be replaced by a new machine because of the later being more economical as well as efficient. In fact, new inventions, developments in production processes, changes in demand for product or services, etc. make the asset out of date.
5. **Accidents:** An asset may get reduction in its value if it meets an accident.
6. **Permanent Fall in the Market Value:** Certain assets may get permanent fall in their value and this decline in their value is treated as depreciation. For example, a permanent decline in the market value of securities and investment may be assumed as depreciation

NEED FOR PROVIDING DEPRECIATION

The need for providing depreciation arises on account of the following points:

To Ascertain the Profits or Losses: The true profits or losses could be ascertained when all costs of earning revenues have been properly charged against them. Fixed assets like building, plant and machinery, furniture, motor vehicles etc. are important tool in earning business income. But the cost of the fixed asset is not charged to profit and loss of the accounting period in which the asset is purchased. Therefore, the cost of the fixed asset less its salvage value must be allocated rationally to the periods that receive benefit from the use of the asset. Thus, depreciation is an item of business expense and must be provided for a proper matching of costs with the revenue.

➤ **To show the Asset as its Reasonable Value:** The assets get decrease in their value over a period of time on account of various such as passage of time, constant use, accidents, etc. Therefore, if the depreciation is not charged then the asset will appear in the balance sheet at the over stated value. This practice is unfair as the Balance Sheet fail to present the true financial position.



- Replacement of assets: Business assets become useless at the expiry of their life and, therefore, need replacement. The cash resources of the concern are saved from being distributed by way of dividend by providing for depreciation. The resources so saved, if set aside in each year, may be adequate to replace it at the end of life of the asset.
- To Reduce Income Tax: If tax is paid on the business income without providing for depreciation then it will be in excess to the actual income tax. This is a loss to the business man. Thus, for calculating tax, depreciation should be deducted be from income similar to the other expenses.

Basic Elements of Depreciation

In order to assess depreciation amount to be charged in respect of an asset in an accounting period, the following three important factors should be considered:

Cost of the asset: The knowledge about the cost of the asset is very essential for determining the amount of depreciation to be charged to the Profit and Loss Account.

The cost of the asset includes the invoice price of the asset less any trade discount plus all costs essential to make the asset usable. Cost of transportation and transit insurance are included in acquisition cost. However, the financial charges such as interest on money borrowed for the purchase for the purchase of the asset should not be included in the cost of the asset.

Estimated life of the asset: Estimated life generally means that for how many years or hours an asset could be used in business with ordinary repairs for generating revenues. For estimating useful life of an asset, one must begin with the consideration of its physical life and the modifications, if any, made, factors of obsolescence and experience with similar assets. In fact, the economic life of an asset is shorter than its physical life. The physical life is based mostly on internal policies such as intensity of use, repairs, maintenance and replacements. The economic life, on the other hand, is based mostly on external factors such as obsolescence from technological changes.



i) The following journal entries are passed in this method:

ii) Depreciation Account Dr.

To Asset Account

(Entry for providing depreciation)

iii) Profit and Loss Account Dr.

To Depreciation Account

(Entry for closing Depreciation Account)

iv) In case the asset is sold, the amount realised is credited to the Asset Account. Any profit or loss on sale of the asset is transferred to the Profit and Loss Account.

Methods of calculating depreciation

The following are various methods of depreciation in use:

1. Fixed instalment method or straight line method.
2. Machine hour rate method.
3. Diminishing Balance method.
4. Sum of years digits method
5. Annuity method
6. Depreciation Fund Method
7. Insurance Policy Method
8. Depletion Method.

The detailed description of all these methods is as follows:

1. Straight Line Method



This is also known as fixed instalment method. Under this method, the depreciation is charged on the uniform basis year after year. When the amount of depreciation charged yearly under this method is plotted on a graph paper, we shall get a straight line. Thus, the straight line method assumes that depreciations is a function of time rather than use in the sense that each accounting period received the same benefit from using the asset as every other period. The formula for calculating depreciation charge for each accounting period is:

$$\text{Amount of annual Depreciation} = \frac{\text{Original cost of the fixed assets} - \text{Residual value}}{\text{Estimated Life in years}}$$

For example, if an asset cost ₹ 50,000 and it will have a residual value of ₹ 2000 at the end of its useful life of 10 years, the amount of annual depreciation will be ₹ 4800 and it will be calculated as follow:

Depreciation

This method has many shortcomings. First, it does not take into consideration the seasonal fluctuations, booms and depression. The amount of depreciation is the same in that year in which the machine is used day and night to that in another year in which it is used for some months. Second, it ignores the interest on the money spent on the acquisition of that asset. Third, the total charge for use of asset (i.e., depreciation and repairs) goes on increasing from year to year though the assets might have been use uniformly from year to year. For example, repairs cost together with depreciation charge in the beginning years is much less than what it is in the later year. Thus, each subsequent year is burdened with greater charge for the use of asset on account of increasing cost on repairs.

Illustration 1: H. Ltd. purchased a machinery on 1st January 2010 for ₹ 29000 and spent ₹ 2000 on its carriage and ₹ 1,000 on its erection. Machinery is estimated to have a scrap value of ₹ 5000 at the end of its useful life of 5 year. The accounts are closed every year on 31st December. Prepare the machinery account for five years charging depreciation according to straight line method.

Solution



MACHINERY ACCOUNT

Date	Particular	₹	Date	Particular	₹
2010	To Bank	22000	2010	By Depreciation	4000
Jan. 1			Dec. 31		
	To Bank	2000		By Balance c/d	21000
	To Bank	1000			
		25000			25000
2011	To Balance b/d	21000	2011	By Depreciation	4000
Jan.1			Dec.31	Balance c/d	17000
		21000			21000
2012	To Balance b/d	17000	2012	By Depreciation	4000
Jan.1			Dec. 31	By Balance c/d	13000
		17000			17000
2013	To Balance b/d	13000	2013	By Depreciation	4000
Jan.1			Dec.31	By Balance c/d	9000
		13000			13000
2014	To Balance b/d	9000	2014	By Depreciation	4000



Jan.1		Dec.31	By Balance c/d	
				5000
		9000		9000

This method is very suitable particularly in case of those assets which get depreciated more on account of expire of period e.g. lease hold properties, patents, etc.

2. *Written Down Value Method / Diminishing Balance Method*

This is also known as Written Down Value method [WDV]. Under the diminishing balance method, depreciation is charged at fixed rate on the reducing balance (i.e., cost less depreciation) every year.

Thus, the amount of depreciation goes on decreasing every year. Under this method also, the amount of depreciation is transferred to Profit and Loss Account in each of the year and in the Balance Sheet the asset is shown at book value after reducing depreciation from it. For example, if an asset is purchased for ₹ 10,000 and depreciation is to be charged at 20% p.a. on reducing balance system, then the depreciation for the first year will be ₹ 2000. In the second year, it will ₹ 1600 (i.e. 20% of 8000), in the third year ₹ 1280 (i.e. 20% of 6400) and so on. The rate of depreciation under this method can be computed by using the following formula:

$$\text{Depreciation rate} = \sqrt[n]{\frac{\text{Netscrap value}}{\text{Acquisition cost}}}$$



For example, if the cost of an asset is ₹ 27000, scrap value ₹ 3375, economic life 3 year, the rate of depreciation would be:

$$\text{Depreciation Rate} = \sqrt[3]{\frac{3375}{27000}}$$

$$= 1 - \frac{15}{30} = 50\%$$

30

Merits of Diminishing Balance Method

(i) It is very easy to understand and calculate the amount of depreciation despite the early variation in the book value after depreciation (ii) This method put an equal burden for use of the asset on each subsequent year since the amount of depreciation goes on decreasing for each subsequent year while the charge for repairs goes on increasing for each subsequent year. (iii) This method has also been approved by the Income Tax Act applicable in India (iv) Asset is never reduced to zero.

Demerit

(i) It ignores the interest on the capital committed to purchase that asset. (ii) It does not provide adequately for replacing the asset at the end of its life. (iii) The calculation of rate of depreciation is not so simple. (iv) The formula for calculating the rate of depreciation can be applied only when there is some residual of the asset.

Suitability

This method is suitable in those cases where the receipts are expected to decline as the asset gets older and, it is believed that the allocation of depreciation of depreciation ought to be related to the pattern of assets expected receipts.

Illustration 2: A company purchases Machinery on 1st April 2010 for ₹ 20,000. Prepare the



machinery account for three years charging depreciation @ 25% p.a. according to the Written Down Value Method.

MACHINERY ACCOUNT

Date	Particular	₹	Date	Particular	₹
2010 Apr. 1	To Bank	20000	2010 Mar. 31	By Depreciation	5000
				By Balance c/d	15000
		20000			20000
2011 Apr. 1	To Balance b/d	15000	2011 Mar. 31	By Depreciation	3750
				By Balance c/d	11250
		15000			15000
2012 Apr 1	To Balance b/d	11250	2012 Mar. 31	By Depreciation	2812.5
				By Balance c/d	8437.5
		11250			11250

3. Annuity Method

So far we have described such methods of charging depreciation which ignore the interest factor. Also, sometimes it becomes inconvenient for a company to follow any of the methods discussed earlier. Under such circumstances, the company may use some special depreciation systems. Annuity method is one of these special systems of depreciation. Under this system, the depreciation is charged on the basis that besides losing the acquisition cost of the asset the business also loses interest on the amount used for purchasing the asset. Here, interest refers to that income which the business would have earned otherwise if the money used in buying the asset would have been committed in some other profitable investment. Therefore, under the annuity method, the amount of total depreciation is determined by adding the cost and interest



thereon at an expected rate. The annuity table is used to help in the determination of the amount of depreciation. A specimen of Annuity Table is as follows:

ANNUITY TABLE

Year	3%	4%	5%	6%
4	0.269027	0.275490	0.282012	0.288591
5	0.218335	0.224627	0.230975	0.237376
6	0.184598	0.190762	0.197012	0.203363
7.	0.160506	0.166610	0.172820	0.179135
8.	0.142456	0.148528	0.154722	0.161036
9.	0.128434	0.134493	0.140690	0.147022
10.	0.117231	0.12391	0.129505	0.135868

In case depreciation is charged according to this method, the following accounting entries are passed:

(i) Purchase of an asset Asset

Account Dr.

To Bank A/c

(ii) For charging interest

Asset Account Dr.

To Interest Account

(iii) For charging depreciation:

Depreciation Account Dr.

To Asset Account



Evaluation of Annuity Method

Illustration 3: On 1st January, 2010 a firm purchased a leasehold property for 4 year at a cost of ₹ 24000. It decides to depreciate the lease by Annuity Method by charging interest at 5% per annum. The Annuity Table shows that the annual necessary to write off ₹ 1 at 5% ₹ 0.282012. You are required to prepare the lease Hold Property Account for four years and show the net amount to be charged to the Profit and Loss Account for these four years.

Solution

LEASE HOLD PROPERTY ACCOUNT

Date	Particular	₹	Date	Particular	₹
2010 Jan. 1	To Bank	24000.00	2010 Dec. 31	By Depreciation	6768.29
	To interest	1200.00	Dec.31	By balance c/d	18431.71
		25200.00			25200.00
2011 Jan.1	To balance b/d	18431.71	2011 Dec.31	By Depreciation	6768.29
Dec.31	To Interest	921.59	Dec.31	By Balance c/d	12585.01
		19353.30			19353.30
2012 Jan.1	To balance b/d	12585.01	2012 Dec.31	By Depreciation	6768.29
Dec. 31	To Interest	629.25	Dec.31	By Balance c/d	6445.97
		13214.26			13214.26



2013	To balance b/d	6445.97	2013	By Depreciation	6768.29
Jan.1			Dec.31	By Balance c/d	9000
Dec.31	To Interest	322.30			13000
		6768.27			6768.27

NET AMOUNT CHARGEABLE TO THE PROFIT AND LOSS ACCOUNT

Year	Depreciation Debited	Interest Credited	Net Charge against Profit
2010	6768.29	1200.00	5568.29
2011	6768.29	921.59	5846.70
2012	6768.29	629.25	6139.04
2013	6768.29	322.30	6445.99
	27073.16	3073.14	24000.02

Exercises:

Straight Line Method:

1. Hasan purchased a machine on 1st Jan. 1992 at Rs. 14,400. The scrap value after ten years time is expected to be Rs. 3,400. If depreciation is written off by equal instalments every Dec. 31, show the Machinery A/c for the first three years. Calculate the rate of depreciation.

[Ans: Balance of Machinery A/c on 31-12-94 Rs. 11,100 Rate of depreciation 7.64%]

2. An asset is purchased for Rs. 25,000. Depreciation is to be provided annually according to the straightline method. The useful life of the asset is 10 years and the residual value is Rs. 5,000.



You are required to find out the rate of depreciation and prepare the Asset A/c for the first three years.

[Ans: Rate of Depreciation : 8%; Asset A/c Balance Rs. 19,000]

3. A company purchased a second hand plant for Rs. 30,000. It immediately spent on it Rs. 5,000. The plant was put to use on 1-1-90. After having used it for six years, it was sold for Rs. 15,000. You are required to prepare the Plant A/c for 6 years, providing depreciation at 10% on original cost.

[Ans: Profit on sale of plant Rs. 1,000]

4. Mr. Shanmugavel purchased (second hand) a machine for Rs. 8,000 on 1st April 1990. He spent Rs. 3,500 on its installation. Depreciation is written off @ 10% p.a. on the original cost. On 30th June 1993, the machine was found to be unsuitable and sold for Rs. 6,500. Prepare the Machine account from 1990 to 1993 assuming that the accounts are closed on 31st Dec. every year.

[Ans: Loss on Sale of Machine Rs. 1,262.50]

5. On 1st January 1996, Machinery was purchased for Rs. 2,50,000. On 1st June, 1997 additions were made by purchasing a machinery for Rs. 50,000. On 1st March 1998, another machinery was purchased for Rs. 32,000. On 30th June 1999, machinery of the original value of Rs. 40,000 on 1-1-1996 was sold for Rs. 30,000. Depreciation is charged at 10% on original cost. Show the machinery account for the years 1996 to 1999 closing the accounts on 31st December each year.

[Ans: Balance in Machinery A/c: Rs. 1,89,216; Gain on sale of Machinery: Rs. 4,000]

6. A company whose accounting year is the calendar year purchased on 1st April 1986 machinery costing Rs. 30,000. It purchased further machinery on 1st October 1986 costing



Rs. 20,000 and on 1st July 1987 costing Rs. 10,000. On 1st Jan. 1988 one- third of the machinery installed on 1st April 1986 became obsolete and was sold for Rs. 3,000. Show how the machinery A/c would appear in the books of the company. Machinery is depreciated at 10% p.a. under fixed instalment method.

[Ans: Loss on sale of Machinery Rs. 5,250; Balance of Machinery A/c on 31.12.88 Rs. 38,500]

7. On 1.1.90 there was machinery worth Rs. 1,80,000 in a business firm. On 30.6.1990 a machine was purchased for Rs. 20,000. On 31.12.1990, a machine was sold for Rs. 4,200 which was purchased for Rs. 4,000 on 1.1.90.

On 31.12.91, a machine which was purchased on 1.1.90 for Rs. 12,000 was sold for Rs. 8,000.

Depreciation is provided at 10% per annum on fixed instalment basis. Assuming that provision for depreciation A/c is not maintained, prepare Machinery A/c for 1990 and 1991.

[Ans: Machinery A/c balance on 31.12.91 Rs. 1,48,200;

Profit on sale of 1st Machine Rs. 600; Loss on sale of 2nd Machine Rs. 1,600]

8. On 1.7.1978 'A' Co. Ltd. purchased a second hand machine for Rs. 20,000 and spent Rs. 3,000 on reconditioning and installing it. On 1.1.79 the firm purchased new machinery worth Rs. 12,000. On 30.6.80, the machinery purchased on 1.1.79 was sold for Rs. 8,000 and on 1.7.80 fresh plant was installed at a cost of Rs. 15,000.

The company writes off 10% on the original cost of Machinery each year. The accounts are closed every year ending 31st March. Show the Machinery A/c for three years ending 31.3.81.

[Ans: Closing balance of Machinery A/c Rs. 30,550; Loss on sale of machine Rs.



2,200]

9. A company purchased a second-hand machinery on 1st January, 1991 for Rs. 37,000 and immediately spent Rs. 2,000 on its repairs and Rs. 1,000 on its erection. On 1st July 1992, it purchased another machine for Rs. 10,000 and on 1st July, 1993, it sold off the first machine purchased in 1991 at Rs. 28,000. On the same date it purchased machinery for Rs. 25,000. On 1st July, 1994 the second machinery purchased for Rs. 10,000 was sold off for Rs. 2,000. Depreciation was provided on Machinery at the rate of 10% on the original cost annually.

Give the Machinery Assent for four years commencing from 1st January, 1991.

[Ans: Cl. Balance of Machinery A/c at the end of 1991: Rs. 36,000; 1992: Rs. 41,500; 1993: Rs. 32,250; 1994: Rs.21,250; Loss on sale on 1-7-93: Rs. 2,000; On 1-7-94: Rs. 6,000]

Diminishing Balance Method/ Written Down Value Method

10. A machine is purchased for Rs. 51,200. Its life is expected to be 4 years and the scrap value is expected to be Rs. 16,200. You are required to determine the rate of depreciation when diminishing balance method of depreciation is adopted.

11.. A machine was purchased from abroad for Rs. 10,000. Import duty, shipping and other forwarding charges were Rs. 9,000 and the installation expenses were Rs. 1,000. Calculate depreciation for two years @ 10% per annum on diminishing balance method. Prepare machinery account for two years.

[Ans: Balance in Machinery A/c Rs. 16,200}

12. A boiler was purchased from abroad for Rs. 20,000. Shipping and forwarding charges amounted to Rs. 4,000, import duty Rs. 14,000 and expenses of installation amounted to Rs.



2,000.

Calculate depreciation for the first three years (separately for each year) @ 10% on Written down value method.

[Ans: Balance of Machinery A/c after 3 years: Rs. 29,160]

13. On 1-7-1980, Raja gopal purchased a second hand car for Rs. 18,000 and spent Rs. 2,000 on its repairs. On 30-6-1983, the car was disposed off for a sum of Rs. 13,600. Assuming that the books are closed on Dec. 31 each year and the depreciation is 10% on diminishing balances, calculate the amount chargeable to Profit & Loss account for the year 1983.

[Ans: Amount chargeable to P&L A/c in 1983 - Rs. 1,790 which includes depreciation of Rs. 769.50 and Loss on sale of Rs. 1,020.50]

14. A company purchased a second hand plant for Rs. 30,000 and immediately spent Rs. 5,000 on repairs. The plant was put to use on January 1985. After using it for six years it was sold for Rs. 15,000. You are required to prepare the plant A/c for 6 years providing depreciation at 10% on diminishing balance method. Accounts are closed on 31st December.

[Ans: Loss on Sale Rs. 3,600.43]

15. Machinery was purchased on 1-1-86 for Rs. 40,000. On 30th June, another second hand machine was purchased for Rs. 15,000 and Rs. 5,000 was spent for repairs. On 30th June 1987 the second machine was sold for Rs. 15,000. Prepare machinery account after allowing depreciation of 10% p.a. on the written down value. [Kerala, B.Com., April 1988]

[Ans: Balance of machinery A/c on 31-12-87- Rs. 32,400; Loss on sale of machine - Rs. 3,050]

16. On 1st January, 1992, a company purchased machinery for Rs. 12,000 and on 30th June,



1993, it acquired additional machinery at a cost of Rs. 2,000. On 31st March, 1994, one of the original machines which had cost Rs. 500 was found to have become obsolete and was sold for Rs. 50. It was replaced on that date by a new machine costing Rs. 800. Depreciation to be provided at the rate of 15 per cent per annum on the written down value. Show Machinery Account for the first three years.

[Ans: Balance of Machinery A/c on 31-12-94 : Rs. 9,344.94; Loss on sale of machine: Rs. 297.70]

Prepared By

DR. MARIMUTHU. K.N MBA, M.Phil, Ph.D, M.Com, PGDCA, PGDPM, CGT

Assistant Professor, Department of Management Studies
Manonmaniam Sundaranar University , Tirunelveli - 627012
Tamilnadu, India
e-mail: marimuthumsu@gmail.com