DJA3B - ACCOUNTANCY

Syllabus

Unit 1

Introduction to Accounting – objectives – limitations – accounting concepts – accounting convention – double entry system – rules for debit and credit – journals – ledgers – subsidiary books – balancing of accounts.

Unit 2

Trial balance – rectification of errors – suspense accounts – bank reconciliation statement – difference between cash book and pass book – reasons

Unit 3

Bills of exchange – honour and dishonor of a bill – renewal of a bill – retirement of bill – insolvency of acceptors – accommodation bills

Unit 4

Final accounts – Trading and profit and loss account – balance sheet – adjustment entries – provision for bad and doubtful debts – provision for discount on debtors and creditors

Unit 5

Accounts of non-trading organisation – receipts and payments –income and expenditure account – balance sheet – income and expenditure of professional people

OVERVIEW

Accountancy is one of the papers prescribed for the third year students of ourManonmaniamSundarnar University, Directorate of Distance & Continuing Education. This material meets the requirements of the students preparing this subject.

This course material has been prepared under the self – Instruction Material (SIM) which enables the students to understand the contents of the subject by themselves. The main features of this material are as follows.

1) This material meets the requirements of the students preparing themselves for the BCA Degree Examinations

2) In each chapter, Objectives and Summary are clearly mentioned.

3) Lot of illustrations is given. In addition theoretical aspects of the topics of are well dealt.

4) Problems of varying degrees of difficulties have been presented in a graded manner along with their solutions at the appropriate points.

It is, therefore, fervently hoped that this course material, which has been prepared with such meticulousness, will fulfill the requirements of the students and will he much benefited to them in accomplishing their goal in the academic pursuit.

SCHEMES OF LESSONS

CHAPTER 1
BASIC CONCEPT OF ACCOUNTING

INTRODUCTION

In all activities (whether business activities or non-business activities) and in all organizations like a manufacturing entity or trading entity or non-business organizations like schools, colleges, hospitals, libraries, clubs, temples, political parties which require money and other economic resources, accounting is required to account for these resources. In other words, wherever money is involved, accounting is required to account for it. Accounting is often called the language of business. The basic function of any language is to serve as a means of communication. Accounting also serves this function.

OBJECTIVES

The objective of this Chapter is as follows:

- To understand the meaning and definition of accounting, book-keeping and accountancy.
- To know the advantages, limitations and objectives of accountancy.
- To know the persons interested in the study of accountancy.
- To study the accounting concept and conversion.
- To know the types of accounts.
- To know the rules for different types of accounts.

ACCOUNTING

Business involves a larger number of transactions which is more difficult to remember. In business, purchase and sale of goods are carried on more frequently. We have to make payments and receive payments now and then. So, unless we record them properly, we cannot remember all these transactions. Hence, it is necessary to maintain a proper record of all the transactions which take place from time to time. The recording of business transactions in a systematic manner is the main function of accounting. The accounting system has two stages: (i) Book-keeping and (ii) Accounting.

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:

A.H. Rosenkampff defines Book-keeping as "an art of recording business transactions in a systematic manner".

R.N. Carter gives the following definition: "Book-keeping is the science and art of correctly recording in books of account all those business transactions that result in the transfer of money or money's worth".

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.

ACCOUNTING - DEFINITION

Committee on Terminology appointed by the American Institute of Certified Public Accountants has defined Accounting as, “the art of recording, classifying and summarizing in a significant manner and in terms of money transactions and events which in part, at least of 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 judgements and decisions by users of the information”.

OBJECTIVES OF ACCOUNTING

Objective of accounting may differ from business to business depending upon their specific requirements. However, the following are the general objectives of accounting.

1. To keep systematic record

It is very difficult to remember all the business transactions that take place. Accounting serves this purpose of record keeping by promptly recording all the business transactions in the books of account.

2.To ascertain the results of the operation

Accounting helps in ascertaining profit earned or loss suffered in business during a particular period. For this purpose, it prepares either a Trading and Profit and Loss account or an Income and Expenditure account which shows the profit or loss of the business.

3.To ascertain the financial position of the business

In addition to profit, a businessman must know his financial position i.e. availability of cash, position of assets and liabilities etc. This helps the businessman to know his financial strength. Financial statements are the barometers of health of a business entity. This can be done by the preparation of balance sheet.

4. To portray the liquidity position

Financial reporting should provide information about how an enterprise obtains and spends cash, about its borrowing and repayment of borrowing, about its capital transactions, cash dividends and other distributions of resources by the enterprise to owners and about other factors that may affect an enterprise’s liquidity and solvency.

5. To protect business properties

Accounting provides up to date information about the various assets that the firm possesses and the liabilities the firm owes, so that nobody can claim a payment which is not due to him.

6. To facilitate rational decision-making

Accounting records and prepare financial statements whichprovide financial information which help the business in making rational decisions about the steps to be taken in respect of various aspects of business.

7. To satisfy the requirements of law

Entities such as companies, societies, public trusts are compulsorily required to maintain accounts as per the law governing their operations such as the Companies Act, Societies Act, Public Trust Act etc. Maintenance of accounts is also compulsory under the Sales Tax Act and Income Tax Act.

DISTINCTION BETWEEN BOOK-KEEPING AND ACCOUNTING

In general the following are the differences between book-keeping and accounting.

No.	Basis of Distinction	Book-keeping	Accounting
1	Scope	Recording and maintenance of books of accounts.	Not only recording and maintenance of books of accounts but also includes analysis, interpreting and communicating the information.
2	Stage	Primary stage	Secondary stage
3	Objective	To maintain systematic record of business transactions	To ascertain the net result of the business operation
4	Nature	Often routine and clerical in nature	Analytical and executive in nature
5	Responsibility	A book-keeper is responsible for recording business transactions	An accountant is responsible for the work of a book-keeper
6	Supervision	The book-keeper does not supervise and check the work of an Accountant	An accountant supervises and checks the work of the book-keeper
7	Staff involved	Work is done by the junior staff of the organization	Senior staff performs the accounting work

ADVANTAGES OF ACCOUNTING

1) 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.

2) 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.

3) 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.

4) Prevention of Errors and Frauds

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

5) 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.

6) Ascertainment of the growth of business

Whena 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.

7) Fixing the selling price

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

8) Taxation

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

LIMITATIONS OF ACCOUNTING

1. Accounting is historical in nature. It does not reflect the current financial position or worth of a business.
2. Transactions of non-monetary nature do not find place in accounting. Accounting is limited to monetary transactions only. It excludes qualitative elements like management, reputation, employee morale, labour strike etc.
3. Facts recorded in financial statements are greatly influenced by accounting conventions and personal judgements of the Accountant or management. Valuation of inventory, provision for doubtful debts,

valuation of goodwill and assumption about useful life of an asset may therefore, differ from one business house to another.

4. Accounting principles are not static. Therefore, accounting statements do not always present comparable data.
5. Cost concept is found in accounting. Price changes are not considered. Money value is bound to change often from time to time. This is a strong limitation of accounting.
6. Accounting statements do not show the impact of inflation.
7. The accounting statements do not reflect those increase in net asset values that are not considered realized.

ACCOUNTANCY - MEANING

The term 'Accountancy' refers to a systematized knowledge of accounting and is regarded as an academic subject like economics, statistics, chemistry etc. It explains 'why to do' and 'how to do' of various aspects of accounting. In other words, while accounting refers to the actual process of preparing and presenting the accounts, accountancy tells us why and how books of accounts are prepared and how to summarise the accounting information and communicate it to the interested parties. The accountancy is a science (a body of systematized knowledge) whereas accounting is the art of putting such knowledge into practice.

In general usage, however, accountancy and accounting are used as synonyms. But of late, the term accounting is becoming more and more popular.

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. Realisation 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,

Assets = Liabilities + Capital (or)

Assets – Liabilities = Capital

This is a fundamental equation. Whenever a transaction is recorded in the accounts, it affects both the assets and the equities. For example, when 'A' introduces a capital of Rs.1,00,000 for starting a business, the dual aspect of this transaction is that the business has a cash balance of Rs.1,00,000 (Asset) and at the same time if 'A' purchases furniture for Rs.10,000 from Godrej and Co., and pays Rs.5,000/- in part settlement, there would be a reduction of Rs.5,000/- in cash and an increase in the stock of furniture to the extent of Rs.10,000 (Asset) and Godrej and Company's claim for Rs.5,000/- would appear on the liability side. The balance sheet would be as follows:

Liabilities	Amount Rs.	Assets	Amount Rs.
A's Capital	1,00,000	Cash	95,000
Godrej & Co.	5,000	Furniture	10,000
	1,05,000		**1,05,000**

Thus every transaction will affect two items in such a way that the total assets are equal to the total capital and liabilities.

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. For example, if an asset worth Rs.25,000 is purchased for Rs.1,00,000, it is recorded only at Rs.1,00,000 and not at its real value of Rs.25,000. 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.

However, in many matters it is not possible to observe this principle altogether. Subjectivity cannot be avoided in matters such as provision of depreciation, provision for bad and doubtful debts and determining the market value of inventory. It is for this reason that accountants are required to disclose their policies in these matters.

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 customers.

1) 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.

2) 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.

3) 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.

4) 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.

SYSTEM OF BOOK-KEEPING

As already explained book-keeping is the art of recording the transactions. Broadly speaking there are three systems of book-keeping.

1. Cash system
2. Single entry system
3. Double entry system

1 Cash system

This system takes into account only cash receipts and payments on the assumption that there are no credit transactions. Even if there are any credit transactions, they will not be recorded, until the cash is actually received or paid as the case may be. The system is followed by non-profit making institutions like school, college, social club, charitable institution and professional people like doctor, lawyer etc.

2) Single entry system

There is no exact definition for single entry system. Broadly speaking, it is a defective double entry system. It rejects the strict rules of the double entry system,thus eliminates all the tediousness of the double entry system. Kohler (Dictionary of Accountants) defines it as "a system of book-keeping in which as a rule only records of cash and of personal accounts are maintained; it is always incomplete double entry, varying with circumstances". Small traders, general merchants, medical practitioners, lawyers and other professional people usually adopt this system. Joint Stock Company cannot adopt this system.

3) Double entry system

This system takes into account every business transactions in its double aspect i.e. receiving of benefit by one party and giving the like benefit by another. In other words, it records the two-fold aspects of every business transactions. When 'X' purchases a typewriter, he receives the benefit in the form of typewriter and gives the benefit in the form of money. Similarly, the typewriter seller receives the benefit in the form of money and gives the benefit in the form of a typewriter which is money's worth. This system, thus, records every business dealing in money or money's worth, in its double aspects.

Of all the systems, the double entry is the only scientific system of keeping of books of accounts.

FEATURES OF DOUBLE ENTRY SYSTEM

1) Every business transaction affects two accounts.
2) Each transaction has two aspects i.e. debit and credit.
3) It is based upon accounting assumptions, concepts and principles.
4) It helps in preparing trial balance which is a test of arithmetical accuracy in accounting.
5) It helps in the preparation of final accounts with the help of trial balance.

ADVANTAGES OF DOUBLE ENTRY SYSTEM

The following are the advantages of double entry system.

1) It keeps a complete record of both personal accounts (i.e. accounts of persons) and impersonal accounts (i.e. accounts of things, profits and losses).
2) It helps us to check the arithmetic accuracy of the books by preparing, what is known as trial balance.
3) It helps us to find out the profit made or loss incurred under any given period, and the various sources of income and heads of expenditure by preparing, what is known as profit and loss account.
4) It helps us to find out the financial position of the business at any particular date (i.e. the amount of assets, the amount of liabilities and capital) by preparing what is known as Balance sheet.
5) Any information regarding any item can be had at any time.
6) A comparison of expenditure, income, purchases, sales, stock etc. of the current year with those of the previous years can be made thereby, enabling a trader to control and regulate his business to maximize his profits.
7) It is easy for taxation authorities to make correct assessments.

DISADVANTAGES OF DOUBLE ENTRY BOOK-KEEPING

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

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

DIFFERENCES BETWEEN DOUBLE ENTRY AND SINGLE ENTRY SYSTEM

No.	Double Entry System	Single Entry System
1.	It is a scientific system of keeping books of accounts.	It is not a system at all. It is incomplete and unscientific.
2.	It maintains a partial record. Only personal accounts and cash	It maintains a complete record of both personal and impersonal

	accounts are maintained	accounts
3.	Both profit and loss account and balance sheet can be prepared	With the incomplete records, profit and loss account and balance sheet cannot be prepared
4.	Comparison with the previous records is possible	Comparison with the previous records is impossible
5.	The taxation authorities will accept it for assessment purposes	The taxation authorities will not accept this system for assessment purposes.

ACCOUNTING EQUATION

Every business transaction has two aspects. One aspect is debited and other aspect is credited. Both the aspects have to be recorded in accounts appropriately. American Accountants have derived the rules of debit and credit through a 'novel' medium, i.e. accounting equation. The equation is as follows:

Assets = Equities

The equation is based on the principle that accounting deals with property and rights to property and the sum of the properties owned is equal to the sum of the rights to the properties. The properties owned by a business are called assets and the rights to properties are known as liabilities or equities of the business. Equities can be subdivided into equity of the owners which is known as capital and equity of creditors who represent the debts of the business known as liabilities. These equities may also be called internal equity and external equity. Internal equity represents the owner's equity in the assets and external equity represents the outsider's interest in the asset. Based on the bifurcation of equity, the accounting equation can be restated as follows:

Assets = Liabilities + Capital

(or)

Capital = Assets – Liabilities

(or)

Liabilities = Assets – Capital

The equation is fundamental in the sense that it gives a foundation to the double entry book-keeping system. This equation holds good for all transaction and events and at all periods to time since every transaction and events has two aspects.

SUMMARY

It is humanly impossible to remember the numerous transactions taking place in a business during a particular period. Hence there is a need to record them. The recording of business transactions in a systematic manner is the main functions served by accounting.

Accounting is the process of identifying, measuring, recording, classifying and summarizing the transactions, and analyzing, interpreting and communicating the results there of. The accounting system has two stages: i) Book-keeping and ii) Accounting. Book-keeping is an art and science of recording business transactions while accounting is concerned with the design of the system of records, preparation of reports based on the recorded data, interpretation and communication of the results to persons who are interested in such reports.

With a view to making the accounting a standard one, certain concepts and conventions have been developed over a course of period. Accounting concepts mean certain assumptions or conditions upon which accounting is based. They are entity, dual aspect, going concern, money measurement and cost concept. Disclosure, materiality, consistency and conservatism are some of the accounting conventions (tradition or custom)

The systems of book keeping are i) cash system ii) double entry system and iii) single entry system. Under double entry system, both the aspects viz., receiving aspect and the giving aspect are recorded in the books of account. For convenience, accounts have been classified into personal, real and nominal accounts and separate rules have been framed for debiting and crediting different classes of accounts.

EXERCISES

SHORT ANSWER TYPE QUESTIONS

1) What is book-keeping?
2) Define Accounting.
3) What do you mean by the term accountancy?
4) How is the term book keeping related with accountancy?
5) Define financial accounting.

LONG ANSWER TYPE QUESTIONS

1) What are the objectives of book-keeping? How does book-keeping differ from accounting?
2) What are the basic functions of accounting?
3) Explain the uses and limitations of accounting.
4) Discuss the various concepts in accounting.
5) Discuss the various conventions in accounting.
6) Explain briefly accounting equations.
7) Write short notes on:

   a) Debtors b) Creditors c) Stock
8) Briefly explain the following terms:

   a) Voucher b) Invoice c) Account
9) Write short notes on:

   a) Revenue b) Purchase c) Assets

CHAPTER2
ACCOUNTING PROCESS

INTRODUCTION

When the business transactions take place, the first step is to record the same in the books of original entry or subsidiary books or books of prime entry or journal. Thus journal is a simple book of accounts in which all the business transactions are originally recorded in chronological order and from which they are posted to the ledger accounts at any convenient time. Journalizing refers to the act of recording each transaction in the journal and the form in which it is recorded, is known as a journal entry.

OBJECTIVES

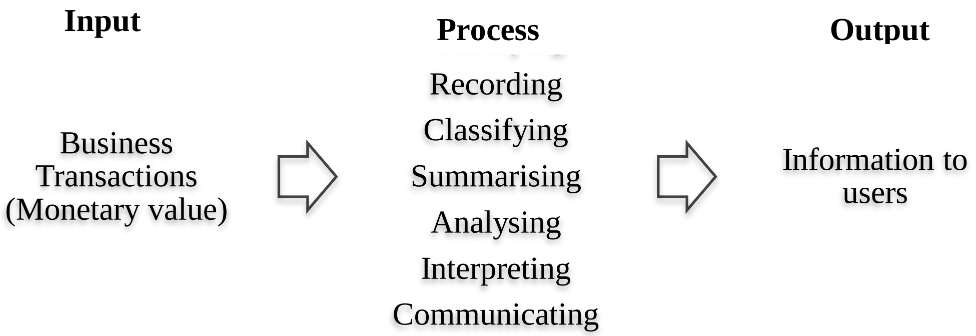
After the studying this unit, you can understand the following:

- Accounting process
- Accounting procedure
- How to write in the ledger

ACCOUNTING PROCESS

American Accounting Association defines accounting as “the process of identifying, measuring and communicating economic information to permit informed judgements and decision by users of information”.

The process of accounting as per the above definition is given below:



Thus, the accounting process consists of the following six stages:

1) Identifying the transactions
2) Recording the transactions
3) Classifying the transactions
4) Summarizing the transactions
5) Interpreting the results
6) Communicating the results

Let us now briefly discuss these stages.

1) Identifying the transactions

The first stage in the process of accounting is the identification of business transactions. It is to be identified from the documentary evidence. Documentary evidence means invoice, cash memo, passbook, pay-in-slip, cheque, debit note, credit note etc. After analyzing the documentary evidence, if the documents are dependable or reliable and measurable in terms of money, only then the particular transactions may be identified as a financial transaction. After identifying the transactions, they should be recorded.

2) Recording the transactions

The accounting process begins with the recording of all transactions in the book of original entry. This book is called 'Journal'. All transactions are recorded in the journal in a chronological order (date wise) with the help of various vouchers such as cash memos, cash receipts, invoices etc.

3) Classifying the transactions

The second stage consists of grouping the transactions of similar nature and posting them to the accounts concerned in another book called 'Ledger'. For example, all transactions related to cash are posted to cash account and the transactions related to different persons are entered separately in the account of each person. The objective of classifying the transactions in this manner is to ascertain the combined effect of all transactions of a given period in respect of each account. For this purpose, all accounts are balanced periodically.

4) Summarising the transactions

The next step is to prepare a year end summary known as 'Final Accounts'. But before preparing the final accounts, a statement called "Trial Balance" is prepared in order to check the arithmetical accuracy of the books of account. If the trial balance tallies, it means that the transactions have been correctly recorded and posted into ledger. Then, with the help of trial balance and some other relevant information, the final accounts are prepared. The objectives of preparing the final accounts are (i) to know the net result of business activities, and (ii) to ascertain the financial position of the business. The final account consists of an income statement called 'Trading and Profit and Loss Account' and a position statement called 'Balance Sheet'. The trading and profit and loss account gives us the information about the amount of profit made or the loss incurred during the year and the balance sheet shows the financial position of assets and liabilities of the business as at the end of the year.

5) Interpreting the results

The last stage consists of analyzing and interpreting the results shown by the final accounts. This involves computation of various accounting ratios to assess the liquidity, solvency and profitability of the business. Such analysis is meant for interested parties like management, investors, bankers, creditors etc. The balances on various accounts appearing in the balance sheet will then be transferred to the new books of account for the next year. Thereafter, the process of recording transactions for the next year starts again.

6) Communicating the results

The results obtained from the summarised, analysed and interpreted information are communicated to the interested parties.

ACCOUNT

Every business transaction has dual effect and under double entry system entries are made whose in both the accounts affected. It is learnt that the account which involves receiving aspect is debited and the account which involves giving aspect is credited. An account is a summarized record of a transaction relating to a particular person, a thing, or an item of income or expense. It is vertically divided into two-halves and resembles the shape of the English alphabet 'T' as under:

Name of the Account

Dr.	**Cr.**

The left hand side is called 'debit side'. It is indicated by 'Dr.' (Abbreviation for debit) on the left hand top corner of the account. The right hand side, known as the 'credit side' is indicated by 'Cr.' (abbreviation for credit) on the right hand top corner of the account. The name of the account is written at the top in the centre. The word 'Account' or its abbreviation 'a/c' is added to the name of the account. For example, if the account is related to Rajan, it is written as 'Rajan's Account'.

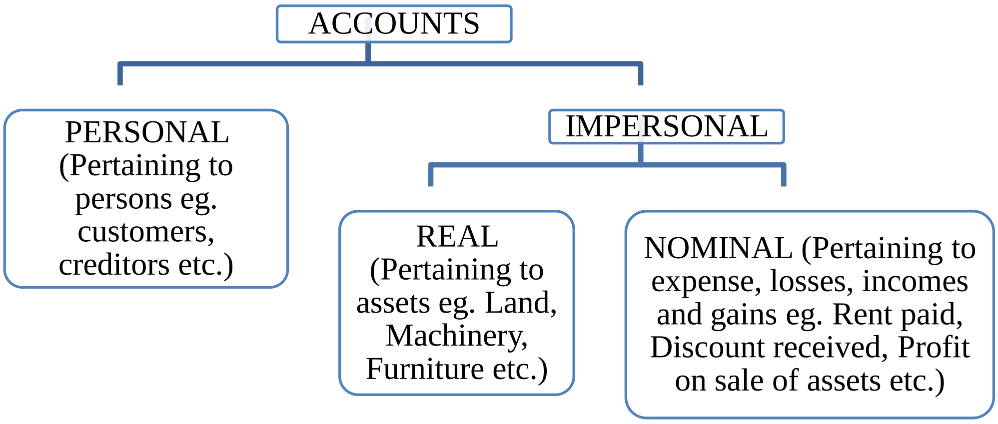
TYPE OF ACCOUNTS

The business must enter into transactions with a number of persons or firms. It will possess some property eg., cash, furniture, stock etc., to carry on the business, pay certain expenses, eg., rent, salaries, wages, advertisement, commission, electricity charges, legal charges etc., and receive certain incomes such as interest, commission, dividend etc., through its business. Thus, to keep a proper record of all aforementioned transactions, the following accounts are required to be maintained.

1) The account of a person or a firm with whom the business deals with is known as ***Personal Account***.
2) The account of property in the business is known as ***Real Account*** and
3) The account of each specific head of expense or income is known as ***Nominal Account***

The following chart shows clearly the types of accounts maintained by a business concern in accordance with the nature of transactions recorded.

Types of Accounts



A brief explanation of these types of accounts is as follows:

1) Personal Account

These are concerned with the accounts of persons or firms dealing with the business enterprise. In case of all proprietors, two accounts are maintained viz., Capital Account, Drawings Account. The Capital Account is credited whenever the proprietor gives cash or any benefit to the business and Drawing Account is debited whenever proprietor withdraws cash or any benefit from the business. The examples for natural personal accounts are Balan's a/c, Ganesh's a/c, Sanjay's a/c etc., and for artificial personal accounts are any limited company's a/c, Insurance Company's a/c, Government's a/c, Banking Company's a/c, Firms a/c etc.

2) Real Account

These are concerned with the accounts of assets which help the business to earn profits. The assets may be tangible or intangible. The tangible assets are those assets which can be seen, felt, touched, measured, purchased, sold etc., whilst intangible assets are those which cannot be seen, felt, touched, but can be measured in terms of money value. Thus, there are two types of real accounts, viz., tangible real accounts like Land a/c, Building a/c, Plant a/c, Machinery a/c, Stock a/c, Furniture a/c, Cash a/c etc. and intangible real accounts like Trade Marks a/c, Goodwill a/c, Patents a/c etc.

3) Nominal Account

These are concerned with the accounts of incomes, expenses, gains and losses. Examples are wages paid a/c, discount allowed or received a/c, commission paid or received a/c, interest paid or received a/c etc. Let us illustrate the above with the following examples.

Illustration: 1

Name the two accounts involved in the following transactions.

a) Commenced business with a capital of Rs.80,000
b) Purchased goods from Shyam Rs.10,000
c) Purchased goods for cash from Ram Rs.20,000
d) Sold goods to Ganesh for cash Rs.16,000

e) Sold goods worth Rs.12,000 to Balu on credit
f) Paid to Raghavan by cheque Rs.10,000

Solution:

The two accounts involved are:

a) Cash a/c and Capital a/c
b) Purchases a/c and Shyam's a/c
c) Purchases a/c and Cash a/c
d) Sales a/c and Cash a/c
e) Sales a/c and Balu's a/c
f) Raghavan's a/c and Bank a/c

Illustration:2

Classify the following into Personal a/c, Real a/c and Nominal a/c.

a) Land and building	b) Plant and Machinery
c) Investment	d) Purchases
e) Tata Ltd.	f) Rent
g) Carriage	h) Capital
i) Leasehold	j) Purchases returns
k) Goodwill	l) Depreciation
m) Sales	n) Sales returns
o) Outstanding salaries	

Solution:

a) Real a/c	b) Real a/c
c) Real a/c	d) Real a/c
e) Personal a/c	f) Nominal a/c
g) Nominal a/c	h) Personal a/c
i) Real a/c	j) Real a/c
k) Real a/c	l) Nominal a/c
m) Real a/c	n) Real a/c
o) Personal a/c	

RULES OF DEBIT AND CREDIT

Every transaction affects two accounts and according to double entry system, entries have to be made in both the accounts. Before recording a transaction, therefore, it is necessary to find out which of the two accounts is to be debited and which is to be credited. The general rule, as stated earlier, is to debit the account which involves a receiving aspect and credit the account which involves a giving aspect. But, for convenience, three different rules have been laid down for the three classes of accounts. These are as follows:

Personal Account:	Debit the Receiver
	Credit the Giver
Real Account:	Debit what comes in
	Credit what goes out
Nominal Account:	Debit expenses and losses

Credit incomes and gains

It is important to note that the above rules should be interpreted from the business point of view and not from the proprietor's point of view. Let us illustrate the rules of debit and credit with the following example.

Illustration: 3

From the following transactions, state the nature of accounts and state which account will be debited and which account will be credited.

1. Mr. Anand commenced business with cash Rs.1,00,000
2. Purchased plant for Rs.20,000
3. Purchased goods from Dayal Rs.16,000
4. Purchased goods for cash Rs.16,000
5. Sold goods to Balu Rs.20,000
6. Sold goods for cash Rs.22,000
7. Purchased furniture for Rs.16,000
8. Paid salaries Rs.8,000
9. Paid rent Rs.4,000
10. Received Commission Rs.2,000

Solution:

1. Mr. Anand commenced business with cash Rs.1,00,000 – The two accounts involved are Cash a/c and Anand's Capital a/c

    a) Cash a/c – Real – Debit (What comes in)

    b) Anand's Capital a/c – Personal – Credit (Giver)

2. Purchased plant for Rs.20,000 – The two accounts involved are Plant a/c and Cash a/c

    a) Plant a/c – Real – Debit (What comes in)

    b) Cash a/c – Real – Credit (What goes out)

3. Purchased goods from Dayal Rs.16,000 – The two accounts involved are Purchases a/c and Dayal's a/c

    a) Purchases a/c – Real – Debit (What comes in)

    b) Dayal's a/c – Personal – Credit (Giver)

4. Purchased goods for cash Rs.16,000 – The two accounts involved are Purchases a/c and Cash a/c

    a) Purchases a/c – Real – Debit (What comes in)

    b) Casha/c – Real – Credit (What goes out)

5. Sold goods to Balu Rs.20,000 – The two accounts involved are Balu's a/c and Sales a/c

    a) Balu'sa/c – Personal – Debit (Receiver)

    b) Salesa/c – Real – Credit (What goes out)

6. Sold goods for cash Rs.22,000 – The two accounts involved are Cash a/c and Sales a/c

    a) Cash a/c – Real – Debit (What comes in)

    b) Sales a/c – Real – Credit (What goes out)

7. Purchased furniture for Rs.16,000 – The two accounts involved are

Furniture a/c and Cash a/c

a) Furniturea/c – Real – Debit (What comes in)

b) Casha/c – Real – Credit (What goes out)

8. Paid salaries Rs.8,000 – The two accounts involved are Salaries a/c and Cash a/c

a) Salariesa/c – Nominal– Debit (expenses and losses)

b) Casha/c – Real – Credit (What goes out)

9. Paid rent Rs.4,000 – The two accounts involved are Rent a/c and Cash a/c

a) Rent a/c – Nominal– Debit (expenses and losses)

b) Casha/c – Real – Credit (What goes out)

10. Received Commission Rs.2,000 – The two accounts involved are Cash a/c and Commission a/c

a) Cash a/c – Real – Debit (What comes in)

b) Commissiona/c – Nominal – Credit (incomes and gains)

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 sub-divided 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.

ADVANTAGES OF JOURNAL

The following are the inherent advantages of using journal, though the transactions can also be directly recorded in the respective ledger accounts.

1) As all the transactions are entered in the journal chronologically, a date wise record can easily be maintained.
2) All the necessary information and the required explanations regarding all transactions can be obtained from the journal
3) Errors can be easily located and prevented by the use of journal or book of prime entry.

SUB-DIVISIONS OF JOURNAL

When innumerable number of transactions takes place, the journal, as the sole book of the original entry becomes inadequate. Thus, the number and type of journals required are determined by the nature of operations and the volume of transactions in a particular business. There are many types of journals and the following are the important ones.

1) Sales day book – to record all credit sales
2) Purchases day book – to record all credit purchases
3) Cash book – to record all cash transactions of receipts as well as payments
4) Sales returns day book –to record the return of goods sold to customers on credit
5) Purchase returns day book – to record the return of goods purchased from suppliers on credit
6) Bills receivable book – to record the details of all the bills received
7) Bills payable book – to record the details of all the bills accepted
8) Journal proper – to record all residual transactions which do not find place in any of the aforementioned books of original entry.

RULING OF A JOURNAL

The form of a Journal is given below.

Date (1)	**Particulars (2)**	**L.F. (3)**	**Dr. (4)**		**Cr. (5)**	
			Rs.	**P.**	**Rs.**	**P.**

Journal has the following five columns:

1) Date

In each page of the journal at the top of the date column, the year is written and in the next line, month and date of the first entry are written. The year and month need not be repeated until a new page is begun or the month or the year changes. Thus, in this column, the date on which the transaction takes place is alone written.

2) Particulars

In this column, the details regarding account titles and description are recorded. The name of the account to be debited is entered first at the extreme left of the particulars column next to the date and the abbreviation 'Dr.' is written at the right extreme of the same column in the same line. The name of the account to be credited is entered in the next line preceded by the word 'To' leaving a few spaces away from the extreme left of the particulars column. In the next line immediately to the account credited, a short explanation about the transaction is given which is known as ‘Narration’. ‘Narration’ may include particulars required to identify and understand the transaction and should be adequate enough to explain the transaction. It usually starts with the word ‘Being’ which means what it is and is written within parentheses. The use of the word ‘Being’ is completely dispensed with, in modern parlance. To indicate the completion of the entry for a transaction, a line is usually drawn all through the particulars column.

3. L.F. (Ledger Folio)

This column is meant to record the reference of the main book i.e. ledger and is not filled in when the transactions are recorded in the journal. The page number of the ledger in which the accounts are appearing is indicated in this column, while the debits and credits are posted to the ledger accounts.

4. Debit amount

Theamount to be debited along with its unit of measurement at the top of this column on each page is written against the account debited.

5. Credit amount

Theamount to be credited along with its unit of measurement at the top of this column on each page is written against the account credited.

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

PROCEDURE

Before a Journal Entry is actually made, each transaction has to be analysed to know:

1. What accounts are involved?
2. What is their classification?
3. What rule of entry is applicable? and
4. Which account is to be debited and which one is to be credited?

Soon after analyzing a transaction, it is recorded in the Journal in the manner explained below:

- The date, month and year of the transaction is entered in the first column.
- The account to be debited and the account to be credited is entered in the second column.
- A reference to the pages (or folios) in the ledger to which the entries are posted is made in the third column.
- The amount to be debited is written in the fourth column.
- The amount to be credited is written in the fifth column.

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

Steps are given to emphasize the process. You are expected to give the final result alone.

Example:1

July 1 2011: Kannan commenced business with Rs.15,000.

The amount with which a trader starts the business is known as capital. The business has received Rs.15,000 cash. Ask yourself the question "Who has given the sum to the business?" Obviously the proprietor Kannan. This aspect of the double entry is therefore recorded in Kannan's Capital Account.

First step: Capital account and cash account

Second step: Capital is personal a/c. Cash is a real a/c

Third step: Capital account is to be credited since the proprietor is the giver and cash account to be debited, since cash comes in.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July 1	Cash a/c Dr.* To Kannan's capital a/c (Being cash investedin business)		15,000	00	15,000	00

* The debit entry is followed by the abbreviation "Dr." (Debtor)

The name of the account to be debited is placed close to the left hand side date line and the name of the account to be credited must be commenced at a short distance from the date line. The use of the terms "Dr." and "To" indicate that, the first – named account is "debtor to" the second – named account.

The object of narration is to provide concise, yet adequate explanation of the transaction.

Example: 2

1st Sep. 2011 'X' started a business with cash Rs.5,000

Step (i) What are the accounts involved?

Cash a/c and X's Capital a/c

Step (ii) How are the accounts classified?

Cash a/c is a real account and X's capital a/c is a personal a/c

Step (iii) What are the rules applicable?

Debit what comes in (Real a/c)

Credit the giver (Personal a/c)

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

Cash a/c is to be debited and X's capital a/c is to be credited.

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

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Sep. 1	Cash a/c Dr. To X's capital a/c (Being the amount invested in the business)	7 10	5,000	00	5,000	00

N.B.: The ledger folio column indicates 7 against cash account which means that cash account is to be found on page 7 in the ledger and this debit of Rs.5,000 to cash account can be seen on that page.

The ledger folio column indicates 10 against X's capital account which means that X's capital account is to be found on page 10 in the ledger and this credit of Rs.5,000 to X's capital account can be seen on that page. (You are advised not to mark or number anything in the L.F. columns).

Example 3

1st July 2011: Received cash from Muthu Rs.500

First step: What are the accounts affected? Cash and Muthu

Second step: Classify the accounts, Cash is real a/c. Muthu is Personal a/c.

Third step: a) According to Rule No.2, cash account should be debited because cash comes into the business.

b) According to Rule No.1, Muthu account should be credited since Muthu has given the benefit.

Hence the Journal entry is:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011	Cash a/c Dr.	2	500	00		
July1	To Muthu a/c	41			500	00
	(Being cash received from Muthu)					

Example 4

3rd July 2011: Paid cash to Hari a/c Rs.300

First step: Accounts affected are cash and Hari

Second step: Cash is Real a/c. Hari is Personal a/c

Third step: a) Cash goes out and hence Cash a/c should be credited

b) Hari receives a benefit and hence Hari a/c should be debited

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011	Hari a/c Dr.	35	300	00		
July3	To Cash a/c	2			300	00
	(Being cash paid to Hari)					

Example 5

7th July 2011: Bought goods for cash Rs.560

First step: Purchases a/c and Cash a/c

Second step: Purchases and Cash a/c are real a/cs.

Third step: Purchases a/c should be debited since goods have come into business and cash a/c should be credited since cash has gone out.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July7	Purchases a/c Dr. To Cash a/c (Being cash purchase of goods)		560	00	 560	 00

Example 6

9th July 2011: Cash sales Rs.600

First step: Cash a/c and Sales a/c

Second step: Both are real a/cs.

Third step: Casha/c should be debited because cash comes in and sales a/c should be credited because goods have gone out of the business.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July9	Cash a/c Dr. To Sales a/c (Being cash sales)		600	00	 600	 00

Example 7

10th July 2011: Sold goods to Selvan on credit Rs.1,100

First step: Sales a/c and Selvan a/c

Second step: Sales is a real a/c and Selvan is a personal a/c

Third step: Salesa/c should be credited since goods go out of the business and Selvan a/c should be debited since he receives a benefit

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July10	Selvan a/c Dr. To Sales a/c (Being credit sales to Selvan)		1,100	00	 1,100	 00

Example 8

2ndJuly 2011: Paid into Bank (or) opened a current account with CanaraBank Rs.14,000

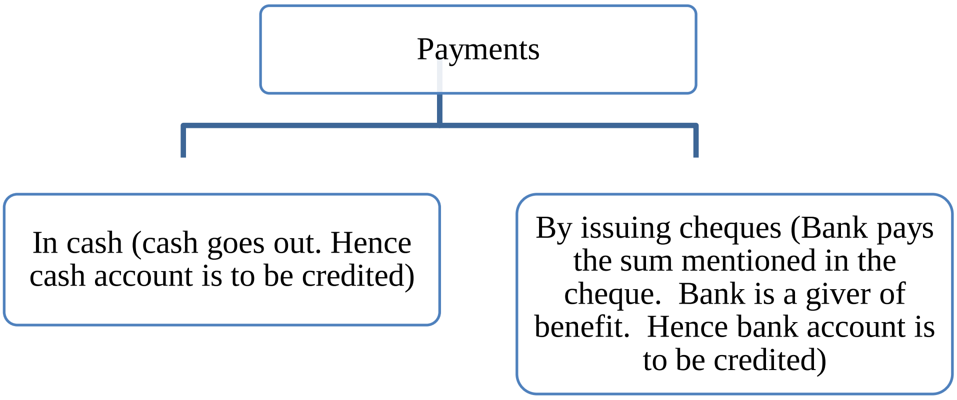
First step: Bank a/c and cash a/c

Second step: Bank account is a personal a/c and cash is a real a/c

Third step: Since bank has received Rs.14,000, Canara bank Account should be debited and since cash gone out of the business, cash account should be credited.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July2	Bank a/c Dr. To Cash a/c (Being the amount paid into Bank for opening a current account)		14,000	00	 14,000	 00

A trader has two alternatives for making business payments. He can pay cash or issue a cheque (an order on the bank for payment of money) to the party. Look at the following chart:



Example 9

31st July 2011: Paid rent by cheque Rs.250

First step: Bank a/c and renta/c

Second step: Rent is a nominal a/c and Bank is a personal a/c

Third step: Rent being an expense, it should be debited. Bank account should be credited

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July31	Rent a/c Dr. To Bank a/c (Being the rent for the month of July 2003 paid by cheque no…)		250	00	250	00

Example 10

31st July 2011: Paid salaries in cash Rs.420

First step: Salaries and cash a/c

Second step: Salaries account is a nominala/c and cash is a real a/c

Third step: Salaries account to be debited and cash account to be credited

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July31	Salaries a/c Dr. To Cash a/c (Being salaries for the month of July paid in cash)		420	00	420	00

Example 11

31st July 2011: Received commission Rs.750

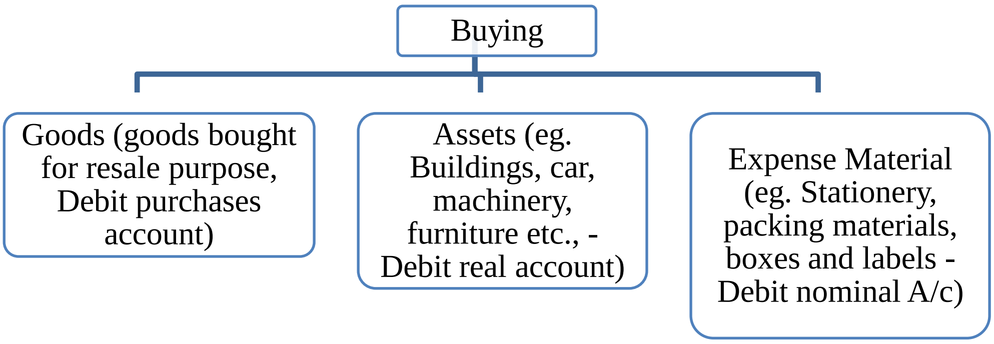
First step: Commissiona/c and cash a/c

Second step: Commission account is a gain (i.e.) a Nominal a/c and cash is a real a/c

Third step: Commission account to be credited and cash account to be debited

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 July31	Cash a/c Dr. To Commission a/c Being commission received)		750	00	750	00

You should classify the purchases made by the trader under three heads as indicated in the chart below:



1. When goods are bought by the trader – Debit purchases a/c
2. When assets are bought by the trader – Debit the appropriate asset a/c
3. When expense material is bought – Debit the appropriate nominal a/c

The account to be credited will depend on whether it is a cash transaction or a credit transaction. If bought for cash, Cash account will be credited. If it is a credit transaction, the personal account is credited. Let us illustrate the above with the following example.

Illustration 4: Journalise the following transactions:

			Rs.
Feb.	1	Bought goods from Senthil for Cash	730
	2	Bought Machinery	6,700
	3	Paid for stationery	120
	4	Bought goods from Arumugam	875
	5	Received five chairs from Godrej Co.	225
	6	Bought packing materials from Umanath and Co.	175

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
Feb.1	Purchases a/c Dr. To Cash a/c (Being cash purchases of goods)		730	00	730	00
2	Machinery a/c Dr. To Cash a/c (Being purchases of		6,700	00	6,700	00

	machinery for cash)					
3	Stationery a/c Dr. To Cash a/c (Being purchase of paper, covers,pens, pencils etc.)		120	00	120	00
4	Purchases a/c Dr. To Arumugam a/c (Being purchase of goods from Arumugam on credit)		875	00	875	00
5	Furniture a/c Dr. To Godrej & Co. a/c (Being purchase of 5 chairs from Godrej & Co. on credit)		225	00	225	00
6	Packing materials a/c Dr. To Umanath & Co. a/c (Being purchase of packing materials on credit)		175	00	175	00

Note: In the transaction of February 1, it is clearly mentioned that goods are bought from Senthil for cash. Hence the two accounts affected are purchases and cash. Senthil account should not be credited because the amount has been paid to him.

But in transactions on February 4th, 5th and 6th, the name of a personal account is mentioned without stating whether it is a cash transaction or a credit transaction. In such cases, it is the practice (convention) to assume that such transactions are on credit.

Examples

Cash transaction	Credit transaction
1. Cash purchases 2. Cash sales 3. Bought goods from A for cash 4. Bought furniture 5. Paid for purchases by cheque 6. Paid for stationery 7. Sold goods to P for cash	1. Bought goods from B on credit 2. Bought goods from C 3. Bought furniture from Curzon & Co. 4. Sold goods to M on credit 5. Sold goods to N

Selling: From the business, goods may be sold or old assets may be sold. If goods are sold, sales account is credited. If assets are sold, asset account is credited.

Example 12

1st Dec. 2011: Rs.300 worth of goods were sold.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 1	Cash a/c Dr. To Sales a/c (Being goods sold)		300	00	 300	 00

Example 13

20th Dec. 2011: Rs.200 worth of plant sold

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 20	Cash a/c Dr. To Plant a/c (Being Rs. 200 worth of plant sold)		200	00	 200	 00

Example 14

21st Dec. 2011: Sold goods to X for Rs.300

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 1	X a/c Dr. To Sales a/c (Being goods sold to X)		300	00	 300	 00

COMPOUND JOURNAL ENTRY

Any journal which contains only one debit and one credit is known as simple journal entry. But when there is either more than one debit or more than one credit, both such entries are called compound journal entry.

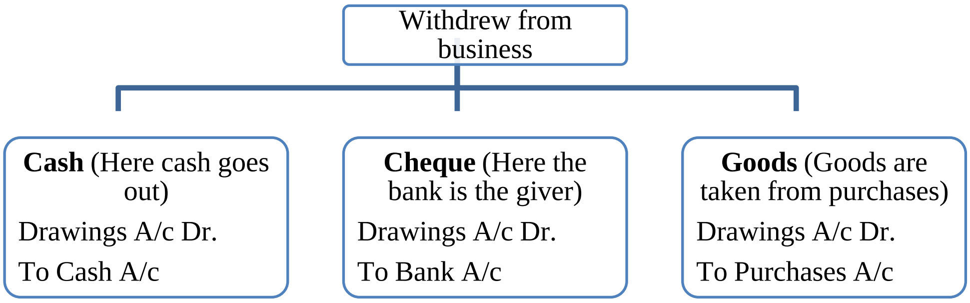
Example 15

1st Dec. 2011: Paid salary Rs.1,000
Paid wages Rs.200
Paid premium Rs.100
Paid rent Rs.50

The above four transactions are the payment of expenses on Dec.1st. They are recorded in the journal as under.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 1	Salary a/c Dr. Wages a/c Dr. Premium a/c Dr. Rent a/c Dr. To Purchases a/c (Being various expenses are paid)		1,000 200 100 50	00 00 00 00	 1,350	 00

Drawings: The proprietor may withdraw cash from the business for his personal use. Sometimes he also takes goods from the business for the personal use. These transactions are to be recorded in the separate account namely 'Drawings'.



Example 16

Journalise the following

1st Dec. 2011: A, the proprietor withdrew Rs.500 cash from the business for personal use

24th Dec.: A, the proprietor drew a cheque for Rs.500 for domestic purposes .

25th Dec.: A, the proprietor took Rs.200 worth of goods for his household purposes.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 1	Drawings a/c Dr. To Cash a/c (Being cash withdrawn for personal use)		500	00	500	00
24	Drawings a/c Dr. To Bank a/c (Being cash withdrawn from bank for personal use)		500	00	500	00
25	Drawings a/c Dr. To Purchase a/c (Being goods withdrawn for personal use)		200	00	200	00

Trade Discount: When goods are purchased in bulk quantities, the seller may give certain concession in price to the purchaser. It is called Trade discount, deducted from the list price of the goods. Trade discount will not be recorded in the books of account. It is deducted from the actual price and the net amount is shown in the invoice.

Example 17

1st Dec. 2011: Purchased goods worth Rs.5,000 from A at a trade discount of 10%

Actual Price	5,000
(-) 10% trade discount (5000 x 10/100)	500
Net amount	4,500

The entry is to be made only for Rs.4,500

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 1	Purchases a/c Dr. To A a/c (Being goods purchased on credit at 10% discount)		4,500	00	4,500	00

Cash Discount: It is a deduction given by the creditor to the debtor for prompt payment. Cash discount is given only when the debtor pays the amount in due time. It is a loss to the creditor and gain to the debtor.

Example 18

1st Dec. 2011: Received cash from A Rs.5,000 and allowed him discount of Rs.500

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 1	Cash a/c Dr. Discount a/c Dr. To A a/c (Being cash received from A by allowing him a cash discount of Rs.500)		4,500 500	00 00	5000	00

Example 19

1st Dec. 2011: Received cheque from A Rs.100

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Dec. 1	Cash a/c Dr. To A a/c (Being cheque received)		100	00	100	00

Note: When cheque is received, we have to assume that cash is received

Example 20

15th Mar. 2011:Cheque received from Santhosh Rs.30,000 and immediately banked.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Mar. 15	Bank a/c Dr. To Santhosh a/c		30,000	00	30,000	00

	(Being cheque received and immediately banked)					

Note: Usually when cheque is received, we have to assume that cash is received. But when cheque is received and immediately banked, the bank a/c is to be debited (Bank is the receiver of the cheque)

Differences between cash discount and trade discount

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

Bad Debts Recovered: Sometimes, it so happens that the bad debts previously written off are subsequently recovered. In such case, cash account is debited and bad debts recovered account is credited because the amount so received is a gain to the business.

Example 21

Received cash for a bad debt written off last year Rs.7,500 on 18th January 2011.

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 Jan. 18	Cash a/c Dr. To Bad debts recovered a/c (Being bad debts recovered)		7,500	00	7,500	00

SOME PRACTICAL EXAMPLES

Illustration 5: Journalise the following:

2011

June 10 Sold goods to Ramaiya Rs.500

16 Paid Atmaram Rs.1,000

19 Cash purchases Rs.1,000

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2011 June 10	Ramaiya a/c Dr. To Sales a/c (Being goods sold on credit)		500	00	500	00
16	Atmaram a/c Dr. To Cash a/c (Being cash paid)		1,000	00	1,000	00
19	Purchases a/c Dr. To Cash a/c (Being goods purchased for cash)		1,000	00	1,000	00

Illustration 6: Journalise the following transactions:

2013 Dec. 1 Salary paid to X Rs.100

Dec. 2 Goods withdrawn by proprietor for personal use Rs.100

Dec. 3 Discount received from a creditor Rs.200

Dec. 4 Rs.20,000 worth of stock was purchased at 25% trade discount

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2013 Dec. 1	Salary a/c Dr. To Cash a/c (Being salary paid)		100	00	100	00
2	Drawings a/c Dr. To Purchases a/c (Being goods withdrawn for personal use)		100	00	100	00
3	Creditor a/c Dr. To Discount received a/c (Being discount received)		200	00	200	00
4	Purchases a/c Dr. To Cash a/c (Being goods purchased at 25%		15,000	00	15,000	00

Illustration 7: Journalise the following transactions:

2013 Dec. 5 Insurance paid Rs.500

Dec. 8 Paid salary to Surender Rs.2,000

Dec. 9 A commenced business with Rs.10,000

Dec.10 Paid rent Rs.10,000

Dec.11 Goods returned by a customer for Rs.500

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2013 Dec. 5	Insurance a/c Dr. To Cash a/c (Being insurance paid)		500	00	500	00
8	Salary a/c Dr. To Cash a/c (Being salary paid)		2,000	00	2,000	00
9	Cash a/c Dr. To A's capital a/c (Being A commenced business with cash)		10,000	00	10,000	00
10	Rent a/c Dr. To Cash a/c (Being rent paid)		10,000	00	10,000	00
11	Sales returns a/c Dr. To Customers a/c (Being goods returned by customers)		500	00	500	00

Illustration 8: Journalise the following transactions:

2014 Dec. 5 House rent paid Rs.2,500

Dec. 6 Credit purchases from 'B' for Rs.3,000

Dec.10 Credit sales to 'A' for Rs.5,000

Dec.15 Discount paid Rs.1,000

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2014 Dec. 5	Drawings a/c Dr. To Cash a/c (Being house rent paid)		2,500	00	2,500	00
6	Purchases a/c Dr. To B a/c (Being goods purchased on credit)		3,000	00	3,000	00

10	A a/c Dr. To Sales a/c (Being goods sold on credit)		5000	00	5000	00
15	Discount allowed a/c Dr. To Cash a/c (Being discount paid)		1,000	00	1,000	00

Illustration 9: Journalise the following transactions:

2015 Dec. 4 Salary paid to X Rs.5,000

Dec. 6 Rent paid Rs.1,000

Dec.10 Credit purchases from Mr.A Rs.2,000

Dec.15 Discount received Rs.500

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2015 Dec. 4	Salary a/c Dr. To Cash a/c (Being salary paid)		5,000	00	5,000	00
6	Rent a/c Dr. To Cash a/c (Being rent paid)		1,000	00	1,000	00
10	Purchases a/c Dr. To A a/c (Being goods sold on credit)		2,000	00	2,000	00
15	Cash a/c Dr. To Discount received a/c (Being discount received)		500	00	500	00

Illustration 10: Journalise the following transactions in the books of Bharath:

2014 Apr. 1 Started business with cash Rs.10,000 and machine worth Rs.40,000

Apr.2 Opened a bank account by depositing Rs.6,000

Apr.3 Purchased goods for Rs.4,000 and issued a cheque

Apr.8 Paid electric charges Rs.1,850

Apr.9 Credit sales to Sundar for Rs.2,500

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2014 Apr. 1	Cash a/c Dr. Machine a/c Dr. To Capital a/c (Being cash and machine brought into business)		10,000 40,000	00 00	50,000	00

2	Bank a/c Dr. To Cash a/c (Being cash deposited into bank)		6,000	00	6,000	00
3	Purchases a/c Dr. To Bank a/c (Being purchases made by cheque)		4,000	00	4,000	00
8	Electric charges a/c Dr. To Cash a/c (Being electric charges paid)		1,850	00	1,850	00
9	Sundar a/c Dr. To Sales a/c (Being credit sales to Sundar)		2,500	00	2,500	00

Illustration 11: Journalise the following transactions:

2013 Apr. 1 Salary paid to Santhosh Rs.15,000

Apr.2 Bought goods from Shyam Rs.10,000

Apr.3 Sold goods to Raja Rs.12,000

Apr.4 Purchased furniture from Hari and Co. for cash Rs.1,500

Apr.5 Cash received from Raj Rs.18,000

Apr.6 Paid cash to Shyam Rs.6,000

Solution:

Date	**Particulars**	**L.F.**	**Dr.**		**Cr.**	
			Rs.	**P.**	**Rs.**	**P.**
2013 Apr. 1	Salary a/c Dr. To Cash a/c (Being salary paid)		15,000	00	15,000	00
2	Purchases a/c Dr. To Shyam a/c (Being credit purchases from Shyam)		10,000	00	10,000	00
3	Raja a/c Dr. To Sales a/c (Being credit sales to Raja)		12,000	00	12,000	00
4	Furniture a/c Dr. To Cash a/c (Being furniture purchased)		1,500	00	1,500	00
5	Cash a/c Dr. To Raj a/c (Being cash received from Raj)		18,000	00	18,000	00
6	Shyam a/c Dr. To Cash a/c (Being cash paid to Shyam)		6,000	00	6,000	00

Illustration 12: Journalise the following transactions:

2014 Dec. 1 Sold goods to Kannan Rs.2,000 at a trade discount of 10%

Dec. 2 Bought goods worth Rs.4,000 from Ramesh at a trade discount of 5%

Dec. 3 Paid to Raji Rs.1450 in full settlement of his account Rs.1,500

Dec. 4 Hussain paid us cash Rs.685 and he was allowed discount Rs.15

Dec. 5 Settle the account of Kumar Rs.1500 by paying him Rs.1,400

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2014 Dec. 1	Kannan a/c Dr. To Sales a/c (Being goods sold to Kannan, trade discount Rs.200)		1,800	00	1,800	00
2	Purchases a/c Dr. To Ramesh a/c (Being goods purchased from Ramesh, trade discount of Rs.200 is received)		3,800	00	3,800	00
3	Raji a/c Dr. To Cash a/c To Discount a/c (Being cash paid to Raji and discount received)		1,500	00	1,450 50	00 00
4	Cash a/c Dr. Discount a/c Dr. To Hussain a/c (Being cash received and discount allowed)		685 15	00 00	700	00
5	Kumar a/c Dr. To Cash a/c To Discount a/c (Being cash paid and discount received)		1,500	00	1400 100	00 00

Illustration 13: Journalise the following transactions:

2014 Jan. 1 Mohan commenced business with cash Rs.50,000

Jan. 3 Bought goods for cash Rs.5,000

Jan. 6 Sold goods to Arjun Rs.7,000

Jan. 7 Sold goods for cash Rs.2,000

Jan.10 Received cash from Kannan Rs.1,000

Jan.12 Purchased furniture from Ganesh and Co. Rs.2,000

Jan.18 Paid for office rent Rs.500

Jan. 24 Purchased goods from Senthil Rs.1,700
Jan.28 Cash paid to Rahim Rs.700
Jan.30 Received commission Rs.240

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2014 Jan. 1	Cash a/c Dr. To Mohan's capital a/c (Being cash brought in by Mohan)		50,000	00	50,000	00
3	Purchases a/c Dr. To Cash a/c (Being goods purchased for cash)		5,000	00	5,000	00
6	Arjun a/c Dr. To Sales a/c (Being the goods sold to Arjun for credit)		7,000	00	7,000	00
7	Cash a/c Dr. To Sales a/c (Being goods sold for cash)		2,000	00	2,000	00
10	Cash a/c Dr. To Kannan a/c (Being cash received from Kannan)		1,000	00	1,000	00
12	Furniture a/c Dr. To Ganesh and Co. a/c (Being furniture bought from Ganesh and Co.)		2,000	00	2,000	00
18	Rent a/c Dr. To Cash a/c (Being cash paid for rent)		500	00	500	00
24	Purchases a/c Dr. To Senthil's a/c (Being goods purchased from Senthil)		1,700	00	1,700	00
28	Rahim's a/c Dr. To Cash a/c (Being cash paid to Rahim)		700	00	700	00
30	Cash a/c Dr. To Commission a/c (Being commission received)		240	00	240	00

Illustration 14: Journalise the following transactions in the books of Glory:

2015	Jan. 1	Started business with cash Rs.9,000
	Jan. 2	Purchased goods for cash Rs.2,100
	Jan. 3	Sold goods for cash Rs.700
	Jan. 4	Deposited into Canara bank Rs.3,000
	Jan. 5	Cash received from Rajan Rs.400
	Jan. 6	Cash paid to Ananda Traders Rs.1,000
	Jan. 7	Paid salary Rs.300
	Jan. 8	Paid rent Rs.400
	Jan. 9	Received commission Rs.200
	Jan.10	Withdrew from Canara bank Rs.1,200

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	**P.**	**Rs.**	**P.**
2015 Jan. 1	Cash a/c Dr. To Glory's capital a/c (Being cash brought in by Glory)		9,000	00	9,000	00
2	Purchases a/c Dr. To Cash a/c (Being goods purchased for cash)		2,100	00	2,100	00
3	Cash a/c Dr. To Sales a/c (Being the goods sold for cash)		700	00	700	00
4	Canara Bank a/c Dr. To Cash a/c (Being cash paid into bank)		3,000	00	3,000	00
5	Cash a/c Dr. To Rajan a/c (Being cash received from Rajan)		400	00	400	00
6	Ananda Traders a/c Dr. To Cash a/c (Being cash paid to Ananda Traders)		1,000	00	1,000	00
7	Salary a/c Dr. To Cash a/c (Being salary paid)		300	00	300	00
8	Rent a/c Dr. To Cash a/c (Being rent paid)		400	00	400	00
9	Cash a/c Dr. To Commission a/c		200	00	200	00

	(Being commission received)					
10	Cash a/c Dr. To Canara bank a/c (Being cash withdrawn from bank)		1,200	00	1,200	00

Illustration 15: Journalise the following transactions:

2014 Jan.11 Purchased goods for Rs.1,500

Jan.12 Purchased goods from Jeyam stores Rs.900

Jan.13 Sold goods for Rs.1,100

Jan.14 Sold goods to Raju Rs.250

Jan.15 Bought furniture for cash Rs.2,000

Jan.16 Bought furniture from JFA Furniture Mart Rs.800

Jan.17 Goods returned to Jeyam stores Rs.200

Jan.18 Raju returned goods worth Rs.100

Jan.19 Drew for private use Rs.500

Jan.20 Electric charges amounted Rs.120

Solution:

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2014 Jan. 11	Purchases a/c Dr. To Cash a/c (Being goods purchased for cash)		1,500	00	1,500	00
12	Purchases a/c Dr. To Jeyam stores a/c (Being goods purchased for credit)		900	00	900	00
13	Cash a/c Dr. To Sales a/c (Being the goods sold for cash)		1,100	00	1,100	00
14	Raju a/c Dr. To Sales a/c (Being credit sales made)		250	00	250	00
15	Furniture a/c Dr. To Cash a/c (Being furniture purchased)		2,000	00	2,000	00
16	Furniture a/c Dr. To JFA Furniture Mart a/c (Being furniture purchased for credit)		800	00	800	00
17	Jeyam stores a/c Dr. To Returns outwards a/c		200	00	200	00

	(Being purchases returned to Jeyam stores)					
18	Returns inwards a/c Dr. To Raju a/c (Being sales returned from Raju)		100	00	100	00
19	Drawings a/c Dr. To Cash a/c (Being cash withdrawn for private use)		500	00	500	00
20	Electric charges a/c Dr. To Cash a/c (Being electric charges paid)		120	00	120	00

Illustration 16: Journalise the following transactions:

2015 Jan.21 Withdrew from Bank for personal use Rs.1,000

Jan.22 Purchased goods and paid by cheque Rs.2,500

Jan.23 Purchased from Jeya stores Rs.2,000

Jan.24 Sold goods to Baskar Rs.1,000

Jan.25 Paid Jeya stores amount due to them less 10% discount

Jan.26 Baskar settled his account by giving Rs.950

Jan.27 Paid advertisement charges to "The Daily Thanthi" Rs.600

Jan.28 Received cheque from Abi Rs.1,400

Jan.29 The proprietor has brought into the business further cash Rs.7,000, Furniture worth Rs.3,000, stock worth Rs.5,000 and gave for business purpose building worth Rs.25,000

Jan.30 Got a loan from Murali Rs.5,000

Jan.31 Drawn from bank for office use Rs.2,700

Solution:

Date	**Particulars**	**L.F.**	**Dr.**		**Cr.**	
			Rs.	**P.**	**Rs.**	**P.**
2015 Jan. 21	Drawings a/c Dr. To Bank a/c (Being cash withdrawn from bank for personal expenses)		1,000	00	1,000	00
22	Purchases a/c Dr. To Bank a/c (Being goods purchased by cheque)		2,500	00	2,500	00
23	Purchases a/c Dr. To Jeya stores a/c (Being the goods sold for cash)		2,000	00	2,000	00
24	Baskar a/c Dr. To Sales a/c		1,000	00	1,000	00

	(Being credit sales made)					
25	Jeya stores a/c Dr.		2,000	00		
	To Cash a/c				1,800	00
	To Discount a/c				200	00
	(Being Jeya stores account settled)					
26	Cash a/c Dr.		950	00		
	Discount a/c Dr.		50	00		
	To Baskar a/c				1,000	00
	(Being Baskar settled his account)					
27	Advertisement a/c Dr.		600	00		
	To Cash a/c				600	00
	(Being advertisement charges paid)					
28	Cash a/c Dr.		1,400	00		
	To Abi a/c				1,400	00
	(Being cheque received from Abi)					
29	Cash a/c Dr.		7,000	00		
	Furniture a/c Dr.		3,000	00		
	Stock a/c Dr.		5,000	00		
	Buildings a/c Dr.		25,000	00		
	To Capital a/c				40,000	00
	(Being various assets brought into the business)					
30	Cash a/c Dr.		5,000	00		
	To Murali's loan a/c				5,000	00
	(Being loan got from Murali)					
31	Cash a/c Dr.		2,700	00		
	To Bank a/c				2,700	00
	(Being withdrawal from bank)					

Illustration 17: Journalise the following transactions in the books of Murugan and Co.:

2015 Mar.5 Sold on credit to Sitaram and Co. Rs.325
Mar.8 Purchased on credit from Hari Rs.1,200
Mar.10 Purchased for cash from Mohan and Co. Rs.300
Mar.15 Sold to Gopal Bros. on credit Rs.125
Mar.18 Returned to Hari Rs.200
Mar.20 Purchased from Kassal and Co. Rs.500
Mar.26 Gopal Bros. returned goods Rs.25

Solution:

Journal Entry in the books of Murugan and Co.

Date	Particulars	L.F.	Dr. Rs.	Dr. P.	Cr. Rs.	Cr. P.
2015 Mar. 5	Sitaram & Co. a/c Dr.		325	00		
	To Sales a/c				325	00
	(Being credit sales)					
8	Purchases a/c Dr.		1,200	00		
	To Hari a/c				1,200	00
	(Being goods purchased on credit)					
10	Purchases a/c Dr.		300	00		
	To Cash a/c				300	00
	(Being the goods purchased for cash)					
15	Gopal Bros. a/c Dr.		125	00		
	To Sales a/c				125	00
	(Being credit sales made)					
18	Hari a/c Dr.		200	00		
	To Purchases returns a/c				200	00
	(Being the return of defective goods to Hari)					
20	Purchases a/c Dr.		500	00		
	To Kassal & Co. a/c				500	00
	(Being goods purchased from Kassal & Co.)					
28	Sales returns a/c Dr.		25	00		
	To Gopal Bros. a/c				25	00
	(Being defective goods returned by M/s. Gopal Bros.)					

Illustration 18: Journalise the following transactions:

2014 Jan.2 Started business with Rs.10,000; paid into bank Rs.5,000

Jan.3 Bought furniture Rs.500

Jan.5 Bought goods for Rs.3,000

Jan.6 Sold goods for Rs.600

Jan.10 Bought one typewriter for Rs.800 from the Remington Rand Inc. on credit.

Jan.13 Sold goods to M/s. Anand and Sons for Rs.1,000 on credit

Jan.15 Bought goods from M/s Mohindra & Co. for Rs.2,000 on credit

Jan.18 Paid telephone rent Rs.240 for one year

Jan.22 Paid Rs.100 for advertisement

Jan.26 Sold goods to M/s S. Lal and Co. for Rs.800 for cash

Jan.31 Paid salaries Rs.200

Jan.31 Paid rent Rs.100

Jan.31 Withdrew from bank Rs.300 for private use

Jan.31 Bought one delivery van for Rs.10,000 from the Delhi Motor Co. payment to be made by monthly instalments of Rs.500 each together with interest at 9%. First instalment paid by cheque.

Solution:

Date	Particulars	L.F.	Dr. Rs.	Dr. P.	Cr. Rs.	Cr. P.
2014 Jan. 2	Cash a/c Dr. To Capital a/c (Being cash brought into tart business)		10,000	00	10,000	00
2	Bank a/c Dr. To Cash a/c (Being amount deposited with bank)		5,000	00	5,000	00
3	Furniture a/c Dr. To Cash a/c (Being furniture purchased for cash)		500	00	500	00
5	Purchases a/c Dr. To Cash a/c (Being goods bought for cash)		3,000	00	3,000	00
6	Cash a/c Dr. To Sales a/c (Being cash sales made)		600	00	600	00
10	Typewriter a/c Dr. To Remington Rand Inc. a/c (Being typewriter bought from Remington Rand Inc.)		800	00	800	00
13	Anand Sons a/c Dr. To Sales a/c (Being credit sales made)		1,000	00	1,000	00
15	Purchases a/c Dr. To Mohindra & Co. a/c (Being credit purchases made)		2,000	00	2,000	00
18	Telephone rent a/c Dr. To Cash a/c (Being telephone rent paid)		240	00	240	00
22	Advertisement a/c Dr. To Cash a/c		100	00	100	00

	(Being advertisement charges paid)					
26	Cash a/c Dr. To Sales a/c (Being cash sales)		800	00	800	00
31	Salaries a/c Dr. Rent a/c Dr. To Cash a/c (Being salaries and rent paid)		200 100	00 00	300	00
31	Drawings a/c Dr. To Bank a/c (Being cash withdrawn for personal use)		300	00	300	00
31	Motor Van a/c Dr. To Delhi Motor Co. a/c (Being Motor Van bought on instalment basis)		10,000	00	10,000	00
31	Delhi Motor Co. a/c Dr. To Bank a/c (Being amount paid to Delhi Motor Co. a/c)		500	00	500	00

Illustration 19: Journalise the following transactions in the books of Murugan:

1.7.2013 Bought a cycle for office for Rs.1,600 in cash

4.7.2013 Sold goods on credit to the following customers:

Deva Rs.2,000
Kanna Rs.3,000
Krishna Rs.4,000

9.7.2013 Murugan, the proprietor has brought in following assets for the business:

Cash Rs.7,000
Furniture Rs.3,000
Stock Rs.5,000
Building Rs.25,000

13.7.2013 Bought goods from Ravindra and Bros. for Rs.2,400 on credit

Solution:

Journal entry in the books of Murugan

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2013 July 1	Cycle a/c Dr. To Cash a/c (Being cycle purchased for office use)		1,600	00	1,600	00

4	Deva a/c Dr. Kanna a/c Dr. Krishna a/c Dr. To Sales a/c (Being credit sales made)		2,000 3,000 4,000	00 00 00	 9,000	 00
9	Cash a/c Dr. Furniture a/c Dr. Stock a/c Dr. Buildings a/c Dr. To Murugan's capital a/c (Being various assets brought in by the proprietor)		7,000 3,000 5,000 25,000	00 00 00 00	 40,000	 00
13	Purchases a/c Dr. To Ravindra and Bros. a/c (Being goods bought for cash)		2,400	00	 2,400	 00

Illustration 20: Journalise the following transactions in the books of Ram:

1.7.2014 Started business with cash Rs.4,000
2.7.2014 Purchased machinery Rs.2,000
10.7.2014 Bought furniture from Suresh Rs.500
12.7.2014 Sold furniture Rs.100
15.7.2014 Purchased goods from Srinivas on account Rs.4,000
18.7.2014 Sold goods to Sridhar Rs.2,000
25.7.2014 Returned damaged goods to Srinivas Rs.500
27.7.2014 Received cheque from Sridhar Rs.1000

(B.U2007 and 2008)

Solution:

Journal entry in the books of Ram

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2014 July 1	Cash a/c Dr. To Capital a/c (Being business commenced)		4,000	00	 4,000	 00
2	Machinery a/c Dr. To Cash a/c (Being machinery purchased)		2,000	00	 2,000	 00
10	Furniture a/c Dr. To Suresh a/c (Being furniture purchased on credit)		500	00	 500	 00
12	Cash a/c Dr. To Furniture a/c (Being furniture sold)		100	00	 100	 00

15	Purchases a/c Dr. To Srinivas a/c (Being credit purchases from Srinivas)		4,000	00	4,000	00
18	Sridhar a/c Dr. To Sales a/c (Being credit sales made)		2,000	00	2,000	00
25	Srinivas a/c Dr. To Purchase returns a/c (Being defective goods returned to Srinivas)		500	00	500	00
27	Cash a/c Dr. To Sridhar a/c (Being cheque received)		1,000	00	1,000	00

Illustration 21: Passnecessary journal entries in the books of Mr. Kiran:

2015 Apr.1 Kiran started business with cash Rs.10,000 and plant and machinery Rs.20,000
Apr.2 Bought furniture from Raj Rs.2,000
Apr.8 Purchased goods worth Rs.6,000
Apr.12 Sold goods Rs.1,000
Apr.16 Purchased goods from Vishnu on account Rs.500
Apr.18 Sold goods to Rajesh Rs.2,000
Apr.20 Returned damaged goods to Rajesh Rs.100
Apr.27 Received cheque from Rajan Rs.1,000

(BU 2009)

Solution:

Journal entry in the books of Mr. Kiran

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2015 Apr. 1	Cash a/c Dr. Plant and machinery a/c Dr. To Kiran's capital a/c (Being business commenced)		10,000 20,000	00 00	30,000	00
2	Furniture a/c Dr. To Raj a/c (Being furniture bought on credit)		2,000	00	2,000	00
8	Purchases a/c Dr. To Cash a/c (Being goods purchased)		6,000	00	6,000	00
12	Cash a/c Dr. To Sales a/c		1,000	00	1,000	00

	(Being goods sold)					
16	Purchases a/c Dr. To Vishnu a/c (Being goods purchased on credit)		500	00	500	00
18	Rajesh a/c Dr. To Sales a/c (Being goods sold on credit)		2,000	00	2,000	00
20	Rajesh a/c Dr. To Purchase returns a/c (Being goods returned to Rajesh)		100	00	100	00
27	Cash a/c Dr. To Rajan a/c (Being cheque received)		1,000	00	1,000	00

Illustration 22: Journalise the following in the books of Shivaprakash:

2015 Jan.1 Started business with cash Rs.50,000
Jan.4 Opened an account in a bank Rs.10,000
Jan.9 Purchased goods Rs.9,800
Jan.13 Sold goods Rs.12,100
Jan.19 Purchased goods from Swetha Rs.15,000
Jan.25 Sold goods to Saraswathi Rs.10,900
Jan.26 Returned goods to Swetha Rs.1,200
Jan.28 Goods returned from Saraswathi Rs.2,000

(BU., Dec.2010)

Solution:

Journal entry in the books of Shivaprakash

Date	Particulars	L.F.	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2015 Jan. 1	Cash a/c Dr. To Capital a/c (Being business commenced)		50,000	00	50,000	00
4	Bank a/c Dr. To Cash a/c (Being opened an account with bank)		10,000	00	10,000	00
9	Purchases a/c Dr. To Cash a/c (Being goods purchased on cash)		9,800	00	9,800	00
13	Cash a/c Dr. To Sales a/c (Being goods sold)		12,100	00	12,100	00
19	Purchases a/c Dr.		15,000	00		

	To Swetha a/c (Being goods purchased on credit)				15,000	00
25	Saraswathi a/c Dr. To Sales a/c (Being goods sold to Saraswathi)		10,900	00	10,900	00
26	Swetha a/c Dr. To Purchase returns a/c (Being goods returned to Swetha)		1,200	00	1,200	00
28	Sales returns a/c Dr. To Saraswathi a/c (Being goods returned by Saraswathi)		2,000	00	2,000	00

Illustration 23: Journalise the following transactions:

2016

July 1 Edward started a business with
- i) Cash Rs.13,000
- ii) Goods worth Rs.10,000
- iii) Buildings Rs.17,000

2 Opened current account with Canara Bank Rs.10,000
5 Bought of Kumar Rs.4,000
6 Sales to R.G. Emporium Rs.5,000
8 Bought a portable Typewriter for Rs.600
10 Purchased a bi-cycle for personal use for Rs.300 and paid by cheque
12 Commission received Rs.100
13 Two chairs bought at Rs.30 per chair
15 Received a cheque from R.G. Emporium for Rs.2,000
16 Paid R.G. Emporium’s cheque into bank
18 Returned goods to Kumar Rs.500
20 Stationery purchased Rs.10
25 Bought fixtures costing Rs.300
28 Issued a cheque to Kumar for Rs.3,400 in full settlement of Rs.3,500
31 Paid rent Rs.100 in cash
Salaries to clerks by cheque Rs.500
Insurance premium Rs.300 by cheque

Solution: **Journal Entries**

Date	Particulars	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
July 1	Cash a/c Dr. Stock a/c Dr. Building a/c Dr. To Capital a/c (Being the various assets invested in the business)		13,000 10,000 17,000	00 00 00	40,000	00
2	Bank a/c Dr. To Cash a/c (Being the amount paid into bank)		10,000	00	10,000	00
5	Purchases a/c Dr. To Kumar's a/c (Being the credit purchases from Kumar)		4,000	00	4,000	00
6	R.G. Emporium's a/c Dr. To Sales a/c (Being the credit sales to R.G. Emporium)		5,000	00	5,000	00
8	Typewriter a/c Dr. To Cash a/c (Being the portable typewriter bought for cash)		600	00	600	00
10	Drawings a/c Dr. To Bank a/c (Being the bi-cycle bought for personal use and paid by cheque)		300	00	300	00
12	Cash a/c Dr. To Commission a/c (Being the commission received)		100	00	100	00
13	Furniture a/c Dr. To Cash a/c (Being the two chairs bought @ Rs.30 each)		60	00	60	00
15	Cash a/c Dr. To R.G. Emporium's a/c (Being the cheque received from R.G. Emporium)		2,000	00	2,000	00
16	Bank a/c Dr. To Cash a/c (Being the above cheque paid in		2,000	00	2,000	00

	Bank)					
18	Kumar's a/c Dr. To Purchase returns a/c (Being the goods returned to Kumar)		500	00	500	00
20	Stationery a/c Dr. To Cash a/c (Being the stationery bought for cash)		10	00	10	00
25	Fixtures a/c Dr. To Cash a/c (Being fixtures bought for cash)		300	00	300	00
28	Kumar's a/c Dr. To Bank a/c To Discount a/c (Being the amount paid to Kumar in full settlement)		3,500	00	3,400 100	00 00
31	Rent a/c Dr. To Cash a/c (Being the rent paid)		100	00	100	00
31	Salaries a/c Dr. Insurance a/c Dr. To Bank a/c (Being the salaries and insurance paid by cheque)		500 300	00 00	800	00

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.

FEATURES OF LEDGER

1. The debit and credit positions can be easily ascertained
2. Ledger gives the opening and closing position of all accounts
3. With the help of closing balances inthe ledger, trial balance can be easily prepared
4. With the help of the trial balance, trading, profit and loss account and balance sheet can be easily prepared
5. It maintains all accounts along with their details

ADVANTAGES OF LEDGER

1. It helps to prepare the trial balance. Hence, the arithmetical accuracy can be checked.
2. It helps to prepare trading and profit and loss account. Hence the profit or loss of the organization can be found out.
3. It helps to prepare the balance sheet of the organization. Hence the financial position of the organization can be found out.
4. It helps to detect the errors and frauds.
5. The exact amount receivable from debtors and the amount payable to creditors can be found out.
6. It is the main source of information to the management.

RELATION BETWEEN JOURNAL AND LEDGER

Journal	Ledger
1. The journal is a subsidiary book	1. The ledger is a main book
2. Transactions are first entered in it	2. These entries are subsequently posted to the appropriate accounts in the ledger
3. The journal is a daily record	3. Posting is done as per the convenience of the business
4. Entering the transactions in the journal is called journalizing	4. The process of recording in the ledger is called posting

SUB DIVISION OF LEDGER

In a big business, the number of accounts is numerous and it is found necessary to maintain a separate ledger for customers, suppliers and for others. Usually, the following three types of ledgers are maintained in such big business concerns.

1. **Debtors' Ledger:**It contains accounts of all customers to whom goods have been sold on credit. From the sales day book, sales returns book and cash book, the entries are made in this ledger. This ledger is also known as sales ledger.
2. **Creditors' Ledger:** It contains accounts of all suppliers from whom goods have been bought on credit. From the purchases day book,

purchases returns book and cash book, the entries are made in this ledger. This ledger is also known as purchase ledger.

3. **General Ledger:** It contains all the residual accounts of real and nominal nature. It is also known as nominal ledger

HOW TO WRITE AN ACCOUNT IN THE LEDGER

A page is taken for each account and the account is divided into two sides.

Dr. **Name of the Account** **Cr.**

Value received	Value given

The debit side records value received.
The credit side records value given.

How postings are made?

Let us proceed to learn how the postings are made in the ledger.

Example 1: Received cash Rs.1,000 from Joseph (in this transaction, the receiving account is Cash a/c and Joseph's a/c is the giving a/c)

The Journal entry is:

Date	Particulars	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
	Cash a/c Dr.		1,000	00		
	To Joseph's a/c				1,000	00
	(Being the cash received from Joseph)					

(The journal entry indicates that the Cash a/c is to be debited and the account of Joseph should be credited. The posting will be completed if we record on the debit side of the Cash a/c and on the credit side of Joseph a/c in the ledger)

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

Second step: Open the accounts in the ledger

Cash a/c

Dr. **Cr.**

Particulars	J.F.	Rs.	Particulars	J.F.	Rs.
To Joseph's a/c		1,000			

Joseph's a/c

Dr. **Cr.**

Particulars	J.F.	Rs.	Particulars	J.F.	Rs.
			By Cash a/c		1,000

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

Example 2: Enter the following transaction in the books of Raman and post them into Ledger Accounts:

1st Jan. 2012: Raman commenced a business with cash Rs.3,000

Solution:

Journal of Raman

Date	Particulars	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2012 Jan. 1	Cash a/c Dr. To Capital a/c (Being the amount invested in the business)		3,000	00	3,000	00

Ledger of Raman

Cash a/c

Dr. **Cr.**

Date	Particulars	Amount		Date	Particulars	Amount	
		Rs.	P.			Rs.	P.
2012 Jan.1	To Capital a/c	3,000	00				

Capital a/c

Dr. **Cr.**

Date	Particulars	Amount		Date	Particulars	Amount	
		Rs.	P.			Rs.	P.
				2012 Jan.1	By Cash a/c	3,000	00

BALANCING THE LEDGER ACCOUNTS

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

Illustration 24: Journalise the following transactions and post them into ledger

2013			Rs.
June	1	Babu commenced a business with cash	10,000
	2	Deposited with Syndicate Bank	3,000
	5	Purchased goods for and paid by cheque	1,000
	8	Sales to Gupta	800
	15	Bought of Raja	2,000
	18	Cash sales	1,500
	23	Returned to Raja	500

24	Received goods returned by Gupta	50
30	Paid rent	200
	Salaries	300
	Received commission	75

Solution:

Journal Entry

Date	Particulars	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2013 June 1	Cash a/c Dr. To Capital a/c (Being the amount invested in the business)		10,000	00	10,000	00
2	Bank a/c Dr. To Cash a/c (Being the amount deposited with the bank)		3,000	00	3,000	00
5	Purchases a/c Dr. To Bank a/c (Being the goods purchased and paid by cheque)		1,000	00	1,000	00
8	Gupta's a/c Dr. To Sales a/c (Being the goods sold to Gupta on credit)		800	00	800	00
15	Purchases a/c Dr. To Raja's a/c (Being the goods bought from Raja on credit)		2,000	00	2,000	00
18	Cash a/c Dr. To Sales a/c (Being the cash sales)		1,500	00	1,500	00
23	Raja's a/c Dr. To Purchase returns a/c (Being the goods returned to Raja)		500	00	500	00
24	Sales returns a/c Dr. To Gupta's a/c (Being the goods returned by Gupta)		50	00	50	00
30*	Rent a/c Dr. To Cash a/c (Being the rent paid)		200	00	200	00
30*	Salaries a/c Dr.		300	00		

	To Cash a/c (Being the salaries paid)				300	00
30	Cash a/c Dr. To Commission a/c (Being the commission received)		75	00	75	00

* A combined entry may be passed for this:

Date	Particulars	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2013 June 30	Rent a/c Dr. Salaries a/c Dr. To Cash a/c (Being the rent and salaries are paid)		200 300	00 00	500	00

N.B.: You cannot combine the third entry on 30th June.

Instructions: Open the first page of ledger. In the centre of the folio, write the heading "Ledger of Babu" and after leaving 2 lines, open (write) "Cash a/c" (as shown below).

Ledger of Babu

Cash a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2013		
June 1	To Capital a/c	10,000	June 2	By Bank a/c	3,000
18	To Sales a/c	1,500	30	By Rent a/c	200
30	To Commission a/c	75	30	By Salaries a/c	300
				By Balance c/d	8,075
		11,575			**11,575**
July 1	To Balance b/d	8,075			

Capital a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2013		
June			June 1	By Cash a/c	10,000
30	To Balancec/d	10,000			
		10,000			**10,000**
			July 1	By Balance b/d	10,000

Bank a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2013		
June 2	To Cash a/c	3,000	June 5	By Purchases a/c	1,000
			30	By Balance c/d	2,000
		3,000			**3,000**
July 1	To Balance b/d	2,000			

Purchases a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2013		
June			June		
5	To Bank a/c	1,000	30	By Balance c/d	3,000
15	To Raja's a/c	2,000			
		3,000			**3,000**
July 1	To Balance b/d	3,000			

Gupta's a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2013		
June 8	To Sales a/c	800	June		
			24	By Sales returns a/c	50
			30	By Balance c/d	750
		800			**800**
July 1	To Balance b/d	750			

Sales a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2013		
June			June 8	By Gupta's a/c	800
30	To Balance c/d	2,300	18	By Cash a/c	1,500
		2,300			2,300
			July 1	By Balance b/d	2,300

Raja's a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013 June 23	To Purchase returns a/c	500	2013 June 15	By Purchases a/c	2000
30	To Balance c/d	1,500			
		2,000			**2,000**
			July 1	By Balance b/d	1,500

Purchase returns a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013 June 30	To Balance c/d	500	2013 June 23	By Raja's a/c	500
		500			500
			July 1	By Balance b/d	500

Sales returns a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
June 24	To Gupta's a/c	50	June 30	By Balance c/d	50
		50			50
July 1	To Balance b/d	50			

Rent a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013 June 30	To Cash a/c	200	2013 June 30	By Balance c/d	200
		200			**200**
July 1	To Balance b/d	200			

Salaries a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013 June 30	To Cash a/c	300	2013 June 30	By Balance c/d	300
		300			**300**
July 1	To Balance b/d	300			

Commission a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2011 June 30	To Balance c/d	75	2011 June 30	By Cash a/c	75
		75			75
			July 1	By Balance b/d	75

Illustration 25: Journalise the following transactions and prepare ledger accounts:

2014 Feb.1 Sold goods for cash Rs.1,300

Feb.2 Purchased goods Rs.400

Feb.3 Purchased goods from Kumar Rs.3,000

Feb.4 Sold goods to Prabu Rs.2,000

Feb.5 Received cash from Prabu Rs.1,200

Feb.6 Paid to Kumar Rs.1,000

Feb.7 Paid salary Rs.700

Solution:

Journal Entry

Date	Particulars	L.F	Dr. Rs.	Dr. P.	Cr. Rs.	Cr. P.
2014 Feb. 1	Cash a/c Dr. To Sales a/c (Being cash sales made)		1,300	00	1,300	00
2	Purchases a/c Dr. To Cash a/c (Being cash purchases made)		400	00	400	00
3	Purchases a/c Dr. To Kumar a/c (Being credit purchases made)		3,000	00	3,000	00
4	Prabhu a/c Dr.		2,000	00		

	To Sales a/c (Being credit sales made)				2,000	00
5	Cash a/c Dr. To Prabhu a/c (Being cash received from Prabhu)		1,200	00	1,200	00
6	Kumar a/c Dr. To Cash a/c (Being cash paid to Kumar)		1,000	00	1,000	00
7	Salary a/c Dr. To Cash a/c (Being salary paid)		700	00	700	00

Ledger a/c

Cash a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
Feb 1	To Sales a/c	1,300	Feb 2	By Purchases	400
5	To Prabu a/c	1,200	6	By Kumar a/c	1000
			7	By Salary a/c	700
			28	By Balance c/d	400
		2,500			**2,500**
Mar.1	To Balance b/d	400			

Sales a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014			2014		
Feb.			Feb.1	By Cash a/c	1,300
28	To Balance c/d	3,300	4	By Prabu a/c	2,000
		3,300			**3,300**
			Mar.1	By balance b/d	3,300

Purchases a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014			2014		
Feb. 2	To Cash a/c	400	Feb.		
3	To Kumar a/c	3,000	28	By Balance c/d	3,400
		3,400			**3,400**
Mar.1	To balance b/d	3,400			

Kumara/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014			2014		
Feb. 6	To Cash a/c	1,000	Feb. 3	By Purchases	3,000
28	To Balance c/d	2,000			
		3,000			**3,000**
			Mar.1	By Balance b/d	2,000

Prabu a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014			2014		
Feb. 4	To Sales a/c	2,000	Feb. 5	By Cash a/c	1,200
			28	By Balance c/d	800
		2,000			**2,000**
Mar.1	To Balance b/d	800			

Salary a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014			2014		
Feb. 7	To Cash a/c	700	Feb.		
			28	By Balance c/d	700
		700			700
Mar.1	To Balance b/d	700			

Illustration: 26 Enter the following transactions in a journal and prepare only personal accounts in the ledger.

2015 Aug.1 Gupta started business with the following assets:

Cash Rs.7,000

Machinery Rs.10,000

Aug.2 Purchased goods from Peter Rs.12,000

Aug.3 Sold goods for cash Rs.6,000

Aug.5 Paid Peter on account Rs.10,000

Aug.7 Returned goods to Peter Rs.500

Aug.10 Sold goods to Nelson Rs.4,000

Aug.11 Purchased goods from John Rs.8,000

Aug.14 John returned goods Rs.400

Aug.22 Sold goods to Robert Rs.2,000

Aug.27Paid John on account Rs.5,000

Aug.30Paid wages Rs.2,000

Solution:

Journal Entry

Date	Particulars	L.F	Dr.		Cr.	
			Rs.	P.	Rs.	P.
2015	Cash a/c Dr.		7,000	00		
Aug.1	Machinery a/cDr.		10,000	00		
	To Capital a/c				17,000	00
2	Purchases a/c Dr.		12,000	00		
	To Peter a/c				12,000	00
3	Cash a/c Dr.		6,000	00		
	To Sales a/c				6,000	00
5	Peter a/c Dr.		10,000	00		
	To Cash a/c				10,000	00
7	Peter a/c Dr.		500	00		
	To Returns outwards a/c				500	00
10	Nelson a/c Dr.		4,000	00		
	To Sales a/c				4,000	00
11	Purchases a/c Dr.		8,000	00		
	To John a/c				8,000	00
14	John a/c Dr.		400	00		
	To Returns inwards a/c				400	00
22	Robert a/c Dr.		2,000	00		
	To Sales a/c				2,000	00
27	John a/c Dr.		5,000	00		
	To Cash a/c				5,000	00
30	Wages a/c Dr.		2,000	00		
	To Cash a/c				2,000	00

Ledger a/c

Peter a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
Aug.5	To Cash	10,000	Aug. 2	By Purchases	12,000
7	To Returns outwards	500			
30	To Balance c/d	1,500			
		12,000			12,000

Nelson a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
Aug. 10	To Sales	4,000	Aug. 30	By Balance c/d	4,000
		4,000			4,000

John a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
Aug. 14	To Returns inwards	400	Aug. 11	By Purchases	8,000
27	To Cash	5,000			
30	To Balance c/d	2,600			
		8,000			**8,000**

Roberta/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
Aug. 22	To Sales	2,000	Aug. 30	By Balance c/d	2,000
		2,000			2,000

SUMMARY

Journal is a prime book wherein all business transactions are recorded. But it does not provide all information relating to a particular period or item. Hence there is a necessity to maintain another book which is known as ledger. Ledger is the main book of the business containing personal, real and nominal accounts of the business. As account has two sides namely debit side and credit side. When the ledger accounts are balanced, you get the net result of all the transactions relating to that accounts during a given period. With the help of all the ledger balances, a statement which is known as trial balance is prepared in order to test the arithmetical accuracy of the accounts.

EXERCISES

MODEL QUESTIONS

1. Explain the process of accounting.
2. How are accounts classified?
3. What are the golden rules of accounting?
4. Explain journal.
5. How is the journal ruled?

6. What is narration?
7. What is journalizing?
8. Bring out the merits and demerits of journal.
9. What is a ledger?
10. Explain the utilities of a ledger.
11. What is posting? Explain the steps in posting.
12. What do you mean by balancing of accounts?
13. Differentiate journal and ledger.
14. Classify the following accounts into personal, real and nominal.
    a. Wages account
    b. Drawings account
    c. Carriage account
    d. Machinery account
    e. Land account
    f. Freehold property account
    g. Interest accrued account
    h. Ganesh account
    i. Bank account
    j. Discount received account
    k. Capital account
    l. Industrial Finance Corporation account
    m. Travelling expenses account
    n. Insurance account
    o. Goodwill account
    p. Buildings account
    q. Leasehold property account
    r. Wages outstanding account
    s. Kannan's account
    t. Somesh account
    u. Rent paid account
    v. Bank charges account
    w. Hindustan machine Tools Ltd. Account
    x. Current account
15. Find the two accounts involved in each of the following transactions.
    a. Bought goods from Babu
    b. Sold goods to Somesh
    c. Devi sold goods to us
    d. Sarathy bought goods from us
    e. Received goods returned by Somesh
    f. We returned goods to Babu
    g. Sold goods to Jothi
    h. Purchased goods from Eswaran
    i. Damaged goods returned to Devi
    j. Sold goods to Sankar

k. Sankar returned goods

l. Kannan sold us goods

16. Journalise the following transactions of Mr. Moorthi

2013 June 3 Received cash from Ramkumar Rs.60,000

4 Purchased goods for cash Rs.15,000

11 Sold goods to Damodaran Rs.22,000

13 Paid to Ramkumar Rs.40,000

17 Received from Damodaran Rs.20,000

20 Bought furniture from Jegadeesan Rs.5,000

27 Paid rent Rs.1,200

30 Paid salary Rs.2,500

17. Journalise the following in the journal of Thiru. Gowri Shankar.

2014 Oct. 1 Received cash from Siva Rs.75,000

7 Paid cash to Sayeed Rs.45,000

10 Bought goods for cash Rs.27,000

12 Bought goods on credit from David Rs.48,000

15 Sold goods for cash Rs.70,000

18. Record the following transactions in the journal of Mr. Radhakrishnan and post them in the ledger and balance the same.

2015 Jan 1 Radhakrishnan commenced business with cash Rs.15,00,000

3 Paid into bank Rs.5,00,000

5 Bought goods for Rs.3,60,000

7 Paid travelling charges Rs.5,000

10 Sold goods for Rs.2,50,000

15 Sold goods to Balan Rs.2,40,000

20 Purchased goods from Narayanan Rs.2,10,000

25 Withdrew cash Rs.60,000

CHAPTER 3
SUBSIDIARY BOOKS

INTRODUCTION

For a business having a large number of transactions, it is practically impossible to write all transactions in one journal due to the following limitations.

1. Periodical details of some important business transactions cannot be known, from the journal easily. E.g. monthly sales, monthly purchases.
2. Such a system does not facilitate the installation of an internal check system since the journal can be handled by only one person.
3. The journal becomes bulky and voluminous.

The introduction of subsidiary books enables to get the information and data quickly and easily at one time. In this chapter an attempt is made to understand the writing of information in the subsidiary books.

OBJECTIVES

- To know the meaning and advantage of trial balance
- To understand the different types of subsidiary books.

SUBSIDIARY BOOKS

MEANING

The system of subdividing the journal into many subsidiary books is known as the practical system or modern system of book-keeping. Under this system the transactions of the same nature are grouped together, thereby the repeated recording of one of the aspects affected by the transaction can be avoided. So,subsidiary books refer to subdivision of journal into various books recording transactions of similar nature.

ADVANTAGES

The following are the advantages of subsidiary books.

1. **Division of work:** Since there are so many subsidiary books, the accounting work may be divided amongst different clerks.
2. **Saving time:** By avoiding repetitions, time is saved.
3. **Availability of information:** Information relating to a particular account can be easily available.
4. **Checking is made easier:** Checking is facilitated, which will prevent errors and frauds.
5. **Work specialization:** A particular person becomes efficient in the particular work since he is allotted the same work over a period of time. So work can be performed more efficiently.

TYPES OF SUBSIDIARY BOOKS

The journal is sub divided into eight subsidiary books. They are:

1.	Purchases book	-	For recording credit purchases ofgoods only
2.	Sales book	-	For recording credit sales of goodsonly
3.	Purchase returns book	-	For recording returns outwards
4.	Sales returns book	-	For recording returns inwards
5.	Cash book	-	For recording receipts andpayments of cash
6.	Bills receivable book	-	For recording bills receivablereceived
7.	Bills payable book	-	For recording bills payableaccepted
8.	Journal proper	-	For recording any transactionwhich could not be recordedin any of the above seven subsidiary books

1. Purchase Book

The purchase book is used to record goods bought on credit. The sales invoice sent by the selling firm to its customer becomes a purchase invoice to that customer. Since purchase invoices received from different suppliers carry different numbers, they are again numbered serially by the purchaser and to be filed for future reference.

The net amount of invoice is recorded in the purchase day book and the items are then posted separately to the credit of the personal account of the suppliers opened in the purchase ledger. At the end of the period (month/week) the total of the purchases day book is posted collectively to the debit of the purchase a/c in the General ledger. The specimen of the Purchase Book is given below.

Purchase Book

Date	Particulars	Inward Invoice No.	L.F.	Amount Rs.

Example 1

Enter the following transactions in the purchases book of M/s Anand and post them in the ledger.

2013	Jan.9	Purchased from Karthick Stores, 15 boxes of pencil @ Rs.6 per box
	Jan.15	Purchased for cash 10 exercise books @ Rs.5 per book*
	Jan.18	Bought furniture from Fancy furniture mart Rs.2,000, Trade discount 10%**
	Jan.21	Purchased 25 bags of tea dust from Subam Traders @ Rs.20 per bag. Trade discount 5%

Solution

In the Books of M/s. Anand

Purchase Book

Date	Particulars	Inward Invoice No.	L.F.	Amount Rs.
2013				
Jan.9	Karthick Stores			90.00
Jan.21	Subam traders (-) 5% trade discount			475.00
				565.00

* It is a cash transaction. So it will not be recorded in the purchase book.

** This transaction is the purchase of an asset and not goods. So it will not be recorded in the purchase book.

Ledger postings

Karthik Stores a/c

Dr. Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2013		
			Jan.9	By Purchases a/c	90.00

Subam Stores a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2013		
			Jan.21	By Purchases a/c	475.00

Purchasesa/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013					
Jan. 31	To Sundries a/c (total amount)	565.00			

2.Sales Book

This book is used to record sales on credit. For each credit sales, the seller sends documents to the buyer showing full details of the goods despatched, price and the terms of payment. This document is known as invoice and to the seller it is known as Sales Invoice. The seller retains one or more copies of each sales invoice for his own use. Examples of some items included in such invoices are given below:

a) Cash Discount: This is given to debtors who pay promptly for their goods, when the time for payment arrives.

b) Trade Discount: This is a deduction from the catalogue price allowed by the manufacturer or wholesaler to the retailer. No entry is required for recording trade discount.

c) E & O.E.: This stands for Errors and Omissions Exempted. This indicates that if any error is found, it is liable for adjustment.

The specimen of the Sales Book is given below:

Sales Book

Date	Particulars	Outward Invoice No.	L.F.	Amount Rs.

Example 1

Enter the following transactions in the sales day book of Chokkalingam and post them to Ledger accounts

2014 May 1 Sold to Amirthalingam 200 copies of "Book keeping" at Rs.9 per copy 10% trade discount

May 2 Sold to Kotilingam 3 dozens of pens at Rs.5 per pen 20% trade discount

May 3 Sold to Sundaralingam 200 note books at Rs.6 per note less 10% trade discount

Solution

In the books of Chokalingam

Sales Book

Date	Particulars	Outward Invoice No.	L.F.	Amount Rs. Details	Amount Rs. Total
2014	Amirthalingam				
May 1	200 copies @ Rs.9			1,800	
	Less: Trade discount 10%			180	1,620
2	Kotilingam (3x12)				
	36 pens @ Rs.5			180	
	Less: Trade discount 20%			36	144
3	Sundaralingam				
	200 books @ Rs.6			1,200	
	Less: Trade discount 10%			120	1,080
	Total				**2,844**

Ledger

Sales a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2014 May 31	By Sundries a/c	2,844

Amirthalingam a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014 May1	To Sales a/c	1,620			

Kotilingam a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014 May 2	To Sales a/c	144			

Sundaralingam a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014 May 3	To Sales a/c	1,080			

3. Purchase Returns Book

If the goods are damaged, or it is not in accordance with the sample, the trader returns the goods to the supplier. For recording this return it is necessary to use Purchase Returns Book. This is also used for recording empties returned, outward charges and allowances received.

A debit note is issued advising the despatcher of the goods returned or the overcharge as the case may be. Debit note is the document through which the returned entries are made. The items in the purchase returns book are posted to the debit of the supplier's account. To complete the double entry the total of the purchase returns book for the period is transferred to the credit of Purchase Returns Account in the General Ledger.

The specimen of the Purchase Returns Book is given below:

Purchase Returns Book

Date	Name of the Supplier	L.F.	Debit Note No.	Amount Rs.

Example 1

Enter the following transactions in the purchase returns book of M/s Siva.

2013 Jan.1 Returned to Nellai stores goods worth Rs.750

Jan.8 Returned 15 boxes of soaps to Colombo stores Rs.2,000

Jan.21 Returned to Modern Culture Palace, 10 Tanjore paintings @ Rs.200 each subject to 20% trade discount.

Solution

In the book of M/s Siva

Purchase Returns Book

Date	Name of the Supplier	L.F.	Debit Note No.	Amount Rs.
2013				
Jan. 1	Nellai stores			750
8	Colombo stores			2,000
21	Modern Culture Palace			
	(-) Trade discount [2000 – 400]			1,600
	Total			**4,350**

Ledger

Purchase returns a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2013		
			Jan 31	By Sundries a/c	4,350

Nellai stores a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013					
Jan.1	To Purchase returns a/c	750			

Colombo stores a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013 Jan. 8	To Purchase returns a/c	2,000			

Modern Culture Palace a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013 Jan. 21	To Purchase returns a/c	1,600			

4. Sales Returns Book

Sometimes goods sold and delivered are returned in full or in part by the customer because of problems of poor quality, damage etc. For recording this, sales return book is used. This book is also used for recording empties returned such as packing cases, drums, etc.

A document known as credit note is used which is sent to the customer advising him that his account has been duly credited. Credit notes are generally printed in red colour. Items of sales return books are posted to the credit of the customers' accounts in the sales ledgers and the double entry is completed by posting the total of the items for the period transferred to the debit of the sales returns account (returns inward) in the general ledger.

The specimen of sales returns book is given below:

Sales Returns Book

Date	Name of the Customer	L.F.	CreditNote No.	Amount Rs.

Example 1

Record the following transactions in the returns inward book of M/s Rajan.

2014 Apr.2 Mahesh returned goods worth Rs.900

Apr.15 Rajesh returned goods worth Rs.700

Solution

In the books of M/s Rajan

Sales Returns Book

Date	Name of the Supplier	L.F.	CreditNote No.	Amount Rs.
2014				
Apr.2	Mahesh			900
15	Rajesh			700
Total				**1,600**

Ledger

Sales returns a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014					
Apr.30	To Sundries a/c	1,600			

Mahesh a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2014		
			Apr.2	To Sales returns a/c	900

Rajesh a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2014		
			Apr.15	To Sales returns a/c	700

Example 2

Enter the following transactions in the returns inward book.

2015 Apr.6 Returned by Kumar 30 shirts each costing Rs.150, due to inferior quality

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

Solution

Sales Returns Book

Date	Name of the Supplier	L.F.	CreditNote No.	Amount Rs.
2015				
Apr.6	**Kumar**			
	30 shirts @ Rs.150			4,500
8	**M.K. Tailors**			
	10 Baba suits @ Rs.100			1,000
	Total			**5,500**

Ledger

Sales returns a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2015					
Apr.30	To Sundries a/c	5,500			

Kumar a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2015		
			Apr.6	To Sales returns a/c	4,500

M.K. Tailors a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
			2015		
			Apr.8	To Sales returns a/c	1,000

5.Bills Receivable Book

Bills accepted by the customers in favour of the concern are entered in Bills Receivable Book. This book keeps the records about the bills receivable received with a certain period and provides the following information.

a. Name of the acceptor
b. Received from
c. Date of the bill

d. Term (i.e. period)
e. Date of maturity
f. Amount and remarks (if any)

Example 1

Enter the following transactions in the bills receivable book and post the same in the relevant ledger accounts.

2013 Aug.1 Received from Suresh Babu a bill duly accepted for Rs.1,500 payable 3 months after date.

Aug.9 Drew a 2 months bill on Vignesh for Rs.1,200 which was duly accepted and has been discounted

Aug.19 Tamilselvan accepted a 3 months bill drawn by us for Rs.1,100payable at Canara Bank

Solution

Bills Receivable Book

S.No.	**Date of receipt**	**L.F.**	**Drawer**	**Acceptor**	**Term**	**Date of the bill**	**Rs.**
1.	1.8.2013		Self	Suresh Babu	3 months	4.11.2010	1,500
2.	9.8.2013		Self	Vignesh	2 months	12.10.2010	1,200
3.	19.8.2013		Self	Tamil Selvan	3 months	22.11.2010	1,100
				Total			**3,800**

Note: Due date is calculated by adding 3 days of grace

Ledger

Bills receivable a/c

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
2013			2013		
Aug.31	To Sundries a/c	3,800	Aug.31	By Balance c/d	3,800
		3,800			**3,800**
Sep.1	To Balance b/d	3,800			

Suresh Babua/c

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
			2013		
			Aug. 1	To B/R a/c	1,500

Vignesha/c

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
			2013 Aug. 9	To B/R a/c	1,200

Tamilselvana/c

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
			2013 Aug. 19	To B/R a/c	1,100

6. Bills Payable Book

The bills accepted by the concern in favour of suppliers are entered in Bills Payable Book. It is maintained like the bills receivable book and provides the same information as is given in the bills receivable book.

Example 1

Enter the following transactions in the bills payable books and post them in the ledger.

2014 Sep.1 We accept Sundar Raj & Co.'s bill for Rs.1,000 2 months duration payable at bank of India

Sep.21 Madurai & Co. drew on us a 3 months bills for Rs.2,050 which we accepted and returned

Sep.28 Swami's bill for Rs.1,200 accepted by us, the bill being due after 3 months

Solution

Bills Payable Book

Date of acceptance	Drawer	Payee	L.F.	Where payable	Date of bill	Term in months	Due Date	Rs.
1.9.2014	Sundar Raj and Co.	Sundar Raj and Co.		Bank of India	1.9.09	2	4.11.09	1,000
21.9.2014	Madurai & Co.	Madurai & Co.		Bank of India	21.9.09	3	24.12.09	2,050
28.9.2014	Swami	Swami		Bank of India	28.9.09	3	31.12.09	1,200
Total								**4,250**

Ledger

Bills payable a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014 Sep.30	To Balance c/d	4,250	2014 Sep. 30	By Sundries a/c	4,250
		4,250			4,250
			Oct.1	By Balance b/d	4,250

Sundar Raj & Co. a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014 Sep.1	To B/P a/c	1,000			

Madurai & Co. a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2015 Sep.21	To B/P a/c	2,050			

Swami's a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2015 Sep.28	To B/P a/c	1,200			

7. Cash Book

Cash book is meant for recording the receipts and payments of cash. This book is different from other subsidiary books in the sense that it has two sides, just like an account, for recording receipts on the one side (debit side) and payments on the other side (credit side). Hence, no further posting from cash book is required and it serves the purpose of both a book of original entry as well as book of final entry. You should remember that transactions entered in the purchases book, sales book etc., will have to be posted to the purchases account, sales account etc., in the ledger but what is entered in the cash book need not be posted elsewhere.

The cash book can be any one of the following types:

1. Single column cash book

2. Two-column cash book
    a. With cash and discount column
    b. With cash and bank column
3. Three-column cash book and
4. Petty cash book

Features of a cash book

The features of the cash book are given below:

1. In the cash book, all types of cash transactions are recorded.
2. It serves the purpose of both journal and ledger
3. Cash receipts are recorded on the debit side
4. Cash payments are recorded on the credit side
5. It starts with the opening balance and ends with the closing balance
6. Cash and bank transactions are recorded in the cash book chronologically

Advantages of the cash book

The following are the advantages of the cash book.

1. It helps to know the closing balance of cash
2. It serves as a ledger. Hence we need not prepare cash account in the ledger
3. It helps to control the expenditure
4. It helps to verify the physical cash balances on any particular day
5. It helps the management to take important decisions connected with cash transaction
6. It helps the management to prepare cash budget

8. Journal Proper

To minimize the clerical work involved in recording the business transactions, the journal is subdivided into eight different subsidiary books like, purchases book, sales book etc. The eighth subsidiary book is known as journal proper. This subsidiary book is used for recording those transactions which cannot be recorded in other subsidiary books.

Generally speaking, the journal proper is used for recording the following types of entries.

a) Opening entries i.e. entries required to bring forward the various balances from the previous year accounts
b) Closing entries i.e. entries required to close the books of the current year
c) Transfer entries from one account to another
d) Adjusting entries i.e. entries required to adjust the pending transactions at the end of the accounting period for the purposes of preparing the final accounts
e) Rectification entries i.e. entries required for rectifying the errors found in the books of accounts
f) Entries which cannot be made in any other subsidiary books

The journal proper is exactly similar to the journal already seen and entries are made in the same way as in the case of journal. Thus both aspects of the transactions are entered in the journal proper.

Let us explain the preparation of subsidiary books in the following examples.

Illustration 1

Enter the following transactions in proper subsidiary books.

2013 Nov.1 Bought goods from Sumathi Rs.2,000
Nov.2 Sold goods to Vikram Rs.1,000
Nov.3 John sold goods to us Rs.1,000
Nov.8 Sundari bought goods from us Rs.1,000
Nov.12 Received goods returned by Vikram Rs.80
Nov.18 We returned goods to Sumathi Rs.50
Nov.20 Sold goods to Ravi Rs.500
Nov.22 Purchased goods from Vinod Rs.600
Nov.25 Returned goods to John Rs.100
Nov.30 Sold goods to Sekar Rs.600

Solution

Purchases Book

Date	Particulars	Inward Invoice No.	L.F.	Amount Rs.
2013				
Nov. 1	Sumathi			2,000
3	John*			1,000
22	Vinod			600
	Total			**3,600**

***** Treated as purchases for the business

Sales Book

Date	Particulars	Outward Invoice No.	L.F.	Amount Rs.
2013				
Nov. 2	Vikram			1,000
8	Sundari*			1,000
20	Ravi			500
30	Sekar			600
	Total			**3,100**

* Treated as sales for the business

Purchase returns Book

Date	Particulars	Debit Note No.	L.F.	Amount Rs.
2013				
Nov. 18	Sumathi			50
22	John			100
Total				**150**

Sales returns Book

Date	Particulars	Credit note No.	L.F.	Amount Rs.
2013				
Nov. 12	Vikram			80
Total				80

TYPES OF CASH BOOK

1. Single Column Cash Book

There is only one column in this type of cash book i.e. Cash column. The specimen is as follows.

Single Column Cash Book of Thiru ……………

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

Note: R.N. – Receipt No; L.F. – Ledger Folio; V.N – Voucher No.

HOW TO RECORD THE CASH TRANSACTIONS IN THE CASH BOOK

1. When we receive cash, record it in the debit side.

E.g. Received cash from Elango

Debit Cash A/c ***

Credit Elango A/c ***

Cash Book

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To Elango a/c	***			

2. When we pay, record it in the credit side.

Eg. Paid cash to Raman

Debit Raman A/c ***

Credit Cash A/c ***

Cash Book

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
				By Raman a/c	***

3. The cash book is balanced in the same manner as we balance the ledger accounts

4. The debit side total of the cash book will always be in excess than credit side total. Hence a cash book will always show only debit balance at the end of the period.

   This closing balance (i.e. balance c/d) of the cash will be shown as opening balance (i.e. balance b/d) for the next financial period.

Illustration7

Enter the following transactions in a single column cash book.

2014 Sep.1 Baby started a business with cash Rs.5,000

2 He purchased goods for cash Rs.2,000

4 Sold goods for cash and received a cheque for Rs.700

7 Paid for stationery Rs.10

10 Received from Balu a postal order on account for Rs.20

12 Paid for 'Typewriter' Rs.1,000

14 Paid Muthu by Money Order on account Rs.50

Balance the cash book and bring down it on 15th September.

Solution:

Cash Book

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
2014			2014		
Sep.1	To Capital a/c	5,000	Sep.3	By Purchases	2,000
4	To Sales	700	7	By Stationery	10
10	To Balu	20	12	By Typewriter	1,000
			14	By Muthu	50
			15	By Bal. c/d	2,660
		5,720			**5,720**
15	To Bal b/d	2,660			

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

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

Hints:

Steps: 1 It is a receipt. Go to the debit side and write the account involved with date and amount

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

4 It is a receipt

7 It is a payment

10 It is a receipt

12 It is a payment

14 It is a payment

Balance the cash book just like an account and bring down the same.

2. Double Column Cash Book

The most common double column cash books are,

a. Cash book with discount and cash columns
b. Cash book with cash and bank columns

a. Cash Book with discount and cash columns

On either side of the single column cash book, another column is added to record discount allowed and discount received. The format is given below:

Double Column Cash Book

(Cash book with discount and cash column)

Dr. Cr.

Date	Particulars	R. N	L. F	Discount allowed	Rs.	Date	Particulars	V. N	L. F	Discount received	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 totaled. 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 14

Prepare a double column cash book from the following transactions of Mr.Gopalan.

2015 Jan.1 Cash in hand Rs.4,000

6 Cash purchases Rs.2,000

10 Wages paid Rs.40

11 Cash sales Rs.6,000

12 Cash received from Suresh Rs.1,980 allowed him discount Rs.20

19	Cash paid to Meena Rs.2470 and discount received 30
27	Cash paid to Radha Rs.400
28	Purchased goods for cash Rs.2,070

Solution:

Cash Book

Dr. **Cr.**

Date	Particulars	Dis count allowed	Rs.	Date	Particulars	Dis count received	Rs.
2015 Jan.				2015 Jan.			
1	To Balance			6	By Purchases		2,000
1	b/d		4,000	10	By Wages		40
11	To Sales		6,000	19	By Meena	30	2,470
12	To Suresh	20	1,980	27	By Radha		400
				28	By Purchases		2,070
				31	By Balance		
				31	c/d		5,000
		20	**11,980**			**30**	**11,980**
Feb							
1	To Balance						
	b/d		5,000				

Illustration 15

Enter the following in a cash book with cash and discount columns only.

2014	Mar.1	Manmohan started business with Rs.10,000 paid into bank Rs.8,000
	3	Bought office furniture by cheque Rs.3,000
	5	Sold goods for cash Rs.1,000
	8	Paid Anand Rs.600 and was allowed a discount of Rs.60
	12	Received from Mania cheque for Rs.690 and allowed a discount of Rs.10; the cheque was deposited into bank
	18	Withdrew from bank for office use Rs.1,000
	24	Received for cash sales by cheque Rs.1,200
	31	Drew for personal use cash Rs.100; salaries paid Rs.500

Solution:

Cash Book of Manmohan

Dr. **Cr.**

Date	Particulars	Dis count allowed	Rs.	Date	Particulars	Dis count received	Rs.
2014 Mar.				2014 Mar.			
1	To capital		10,000	1	By bank		8,000
3	To bank		3,000	3	By furniture		3,000
5	To sales		1,000	8	By Anand	60	600
12	To Mani	10	690	12	By bank		690
18	To bank		1,000	31	By drawings		100
24	To sales		1,200	31	By salaries		500
				31	By balance c/d		4,000
		10	**16,890**			**60**	**16,890**
Apr. 1	To balance b/d		4,000				

Note:

1. In March 3 transaction, paid by cheque is treated as payment in cash.
2. In March 12 transaction, cheque received is taken as cash received and cheque deposited into bank is treated as case deposited in the bank.

b. Cash Book with cash and bank columns

When bank transactions are more in number, it is advisable toopen 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 books is given below.

Double Column Cash Book

(Cash book with cash and bank column)

Dr. Cr.

Date	Parti culars	R. N.	L. F.	Cash	Bank	Date	Parti culars	V. N.	L. F.	Cash	Bank

There are two amount columns on debit side one for cash receipts and the other for bank deposits (i.e. payments 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 cheque respectively.

Contra Entry

When an entry affects 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 the transaction are recorded in the cash book itself.

Contra Entries

When cash is paid into the bank, cash is withdrawn from the bank for office use; these two transactions are entered on both sides of the cash book one entry in the cash column and another entry in the bank column.

Both the debit aspect and credit aspect is recorded in the cash book itself; there is no need for "ledger folio" column because for the entry in the debit side, the corresponding credit entry appears on the other side. Therefore, in the L.F. column, "C" is put indicating "contra", a Latin word which means "the other side".

Illustration 17

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

2015	Aug.1	Opening balance:	Cash in hand Rs.4,250
			Cash at Bank Rs.13,750
	2	Paid to petty cashier Rs.2,500	
	3	Cash sales Rs.1,750	
	3	Received a cheque from Mr. Ram Banu Rs.4,500 and paid into bank	
	5	Received cheque from Mr. Jayaraman Rs.6,000and Immediatelypaid 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.6,750	
	21	Paid into bank Rs.10,000	
	23	Withdrew cash for personal use Rs.1,000	
	25	Salaries paid by cheque Rs.9,000	

Solution

Double Column Cash Book of Mr. Rajesh
(Cash book with cash and bank column)

Dr. **Cr.**

Date	Particulars	L F	Cash	Bank	Date	Particulars	L F	Cash	Bank
2015 Aug					2015 Aug				
1	To bal. b/d		4,250	13,750	2	By petty cash		2,500	
2	To sales		1,750		8	By purchases		2,500	
3	To Ram Babu			4,500	8	By rent			2,500
5	To Jeyaraman			6,000	9	By cash	C		2,500
9	To bank	C	2,500		14	By stationery		1,000	
10	To sales		3,750		21	By bank	C	10,000	
20	To sales		6,750		23	By drawings		1,000	
21	To cash	C		10,000	25	By salary			9,000
					31	By bal. c/d		2,000	20,250
			19,000	**34,250**				**19,000**	**34,250**
Sep. 1	To bal. b/d		3,000	15,500					

Note:

1. In the transactions of March 3 and 5, the cheque received is deposited into the bank on the same day and hence the amount is debited in the bank column.
2. In March 9, transaction the two accounts involved are cash and bank and hence a contra entry is made i.e. on the debit side "To Bank" with the amount in the cash column and on the credit side "By cash" with the amount in the bank column. The L.F. column is marked with C to represent that the entry made is a contra entry.
3. The transaction of March 21, is also a contra entry and in the debit side, the entry made is "To cash" with amount shown in the bank column and in the credit side, the entry made is "By bank" with the amount in the cash column.

3. Triple Column Cash Book (Three column cash book)

The three column cash book consists of Discount column, cash column and bank column.

There is no need for a separate bank account in the ledger. It is added to the cash book. This is more convenient, economical and advantageous. Therefore, many business concerns have adopted this method.

RULES FOR RECORDING IN THE THREE COLUMN CASH BOOK

1. The cash and bank columns represent cash and bank accounts respectively.
2. When cash / M.O./ Postal order is received, debit cash A/c
3. When cash is paid credit cash A/c
4. Discount allowed to our customers, it is a loss to us. Therefore, discount allowed account is debited.
5. Discount received from our creditors, is a gain to us. Therefore, discount account is credited.
6. When cash is deposited in the bank, debit bank A/c and credit cash A/c (Mark "C" in the L.F. column)
7. When cash is drawn for office use from the bank, debit cash A/c and credit bank A/c (Mark "C" in the L.F. column)
8. When cheque is received; treat it as cash; debit cash A/c
9. When the cheque is deposited in the bank for collection, debit bank A/c, credit cash A/c (Mark "C" in the L.F. column)
10. When a cheque is received and immediately deposited in the bank for collection, debit bank A/c and credit party's A/c. For Eg. Cheque received from Azad, immediately deposited in the bank, debit Bank A/c and credit Arun A/c
11. When payment is made by the cheque to any party or to meet any expense or to the proprietor's personal use, it can be directly recorded in bank column. Some examples are,
    a. Paid cheque for office rent: debit rent A/c and credit bank A/c
    b. Drew a cheque for proprietor's personal use: debit drawings A/c and credit bank A/c
    c. Paid to Mathivanan by cheque: debit Mathivanan A/c and credit bank A/c
12. When a customer directly pays into our bank account, debit bank A/c and credit the party's A/c
13. When a cheque already received from a customer and deposited in the bank, is returned dishonoured. E.g. Received a cheque from Sridhar, sent to Bank for the collection, returned dishonoured, debit Sridhar A/c and credit Bank A/c
14. When a cheque, issued earlier to a customer is reported to be dishonoured, E.g. Cheque issued to Raghavan, is reported to be dishonoured, debit Bank A/c and credit Raghavan A/c

The specimen for Triple Column cash book is given below:

TRIPLE COLUMN CASH BOOK

Dr. **Cr.**

Date	Particulars	R N	L F	Discount allowed	Cash	Bank	Date	Particulars	V N	L F	Discount received	Cash	Bank

Illustration 18

From the following transactions, compile three column cash book of Thiru. Sugumar.

2014 Mar.1		Sugumar commenced business with cash Rs.10,000
	3	Deposited in Bank Rs.4,000
	5	Bought goods on cash Rs.3,800
	10	Purchased goods by cheque Rs.1,500
	11	Sold goods to Nirmal on credit Rs.3,560
	12	Received cheque from Manohar Rs.290 Discount allowedRs.10
	15	Bought goods from Satheesh on credit Rs.2,800
	17	Cash sales Rs.1,500
	20	Paid carriage Rs.35
	24	Withdrew for office use by chequeRs.2,175
	25	Paid wages by cheque Rs.130
	28	Withdrew for personal use by cheque Rs.350
	29	Paid Satheesh by cheque Rs.2,760 Discount allowed by him Rs.40
	30	Paid into bank Rs.1,120
	31	Received a cheque for Rs.3,500 from Nirmal in full settlement of his account, which is deposited into bank

Solution

Cash book with discount, cash and bank column of Thiru. Sugumar

Dr. **Cr.**

Date	Particulars	R N	L F	Discount allow.	Cash	Bank	Date	Particulars	V N	L F	Discount rec.	Cash	Bank
2014 Mar							2014 Mar						
1	To capital				10000		3	By Bank		C		4000	
3	To cash		C			4000	5	By					
12	To							purchases				3800	
	Manohar			10	290		10	By					
17	To sales				1500			purchases					1500
24	To bank		C		2175		20	By					
30	To cash		C			1120		carriage				35	

31	To Nirmal			60		3500	24	By cash		C			2175
							25	By wages					130
							28	By drawings					350
							29	By Satheesh			40		2760
							30	By bank		C		1120	
							31	By Bal. c/d				5010	1705
				70	13965	8620					40	13965	8620
Apr.1	To bal. b/d				5010	1705							

Note:

1. The transaction dated March 11 and 15 will not be recorded in the cash book as it is a credit transaction.
2. Since the amount due from Nirmal is Rs.3,560, and the amount received is Rs.3,500 the balance amount Rs.60 has treated as discount allowed.

Illustration 19

Enter the following transactions in the cash book with cash, bank and discount columns.

2013 Apr.1		Balance of cash in hand Rs.400; overdraft at bank Rs.5000
4		Invested further capital of Rs.10,000 out of this Rs.6,000 was put into the bank
5		Sold goods for cash Rs.3,000
6		Collected from the debtors of last year Rs.8,000 Discount allowed to them Rs.200

Close the cash book on April 7^{th} 2013.

Solution

Three column cash book

Dr. **Cr.**

Date	Particulars	R N	L F	Dis count allow.	Cash	Bank	Date	Particulars	V N	L F	Dis count rec.	Cash	Bank
2013 Apr.							2013 Apr.						
1	To bal b/d				400		3	By bal b/d					5000
4	To capital				10000		4	By bank		C		6000	
4	To cash		C			6000	6	By Bal . c/d				15400	1000
5	To sales				3000								
6	To debtors			200	8000								
				200	21400	6000					–	21400	6000
Apr.7	To bal. b/d				15400	1000							

Note: Balance of overdraft at bank on April 1 is shown in the credit side

Illustration 20

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

2012 Aug.1		Sundar Raj 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

Three column cash book of Mr. Sundar Raj

Dr. **Cr.**

Date	Particulars	RN	LF	Discount allow.	Cash	Bank	Date	Particulars	VN	LF	Discount rec.	Cash	Bank
2012 Aug.							2012 Aug.						
1	To capital				200000		2	By bank		C		50000	
2	To cash		C			50000	4	By purchases				5000	
8	To Mano			10	490		5	By purchases					6000
12	To bank		C		10000		10	By carriage				1000	
20	To Nathan			50		4950	12	By cash		C			10000
							15	By Sundari			40	4960	
							31	By bal. c/d				149530	38950
				60	210490	54950					40	210490	54950
Sep. 1	To bal. b/d				149530	38950							

4. Petty Cash Book

In the course of every business there are many petty expenses to be incurred such as postage, stationery, carriage, cleaning etc. involving very small amount of money. If these transactions are recorded in the main cash book, recording would become quite cumbersome, and time consuming. Hence, such petty expenses may be recorded in a separate cash book known as petty cash book. The petty cash is usually maintained on the basis of imprest system. Under this system, a fixed sum say Rs.100 is advanced to the petty cashier at the beginning of the period by the main cashier. At the end of the month / quarter the petty cashier submits a statement of account of the expenses incurred by him during the month/quarter and gets a fresh advance, always by cheque, equivalent to the amount spent by him during the period. Thus, the petty cashier has a fixed balance at the beginning of every period and is not left with unnecessarily a high cash balance.

The best method of recording petty expenses is to enter them in an analytical petty cash book. The petty expenses are classified into different heads of expenses. Each head of expense will have a separate column in the petty cash book. Thus the various petty expenses can be conveniently recorded under certain heads making the posting from petty cash book easy. The cheque issued for petty cash would be debited to Petty cash account in the ledger and credited to the bank account. The total expenses incurred under each head is debited to the concerned nominal account and credited to petty cash account. Thus, the postings from petty cash book need not be done for individual transactions, but only with the periodical total of each head of expenditure at the end of the period, as shown by the analytical columns.

ANALYTICAL PETTY CASH BOOK

The petty expenses are classified into different heads of expenses. Each head of expense will have a separate column in the petty cash book. The analysis of payments will help us in identifying the type of expenditure on which some check could be exercised. It also throws light on the sundry expenditure pattern in a business concern.

Illustration 29

A petty cash book is kept on imprest system, the amount of the imprest being Rs.200 and has seven analysis columns for ‘postage and telegrams’, ‘printing and stationery’, ‘travelling expenses’, ‘repairs’, ‘carriage’, ‘office expenses’, and ‘ledger accounts’. Enter the following.

2015	Mar.1	Petty cash in hand Rs.20.75
	2	Received cash to make up imprest, Rs.179.25
	3	Bought stamps Rs.22.40
	7	Paid for stationery Rs.11.20
	8	Paid for railway fare Rs.19.25
	12	Paid office expenses Rs.5.00
	15	Paid to Sekar Rs.20.00
	18	Paid for carriage Rs.12.60
	20	Paid for repairs to typewriters Rs.41.50
	25	Paid for bus fare Rs.10.50
	27	Paid for telegrams Rs.6.50
	30	Paid for printing charges Rs.35.00

Solution

Analytical Petty Cash Book

Amt. rece.	Date	Particulars	Total pay ments	Postage and telegram	Printing and stationery	Travel ling	Re pairs	Carri age	Sund ries	Led ger A/c
20.75 179.25	Mar. 1 2	To bal. b/d To cash								

	3	By Postage	22.40	22.40						
	7	By stationery	11.20		11.20					
	8	By Railway	19.25			19.25				
	12	By Office expenses	5.00						5.00	
	15	By Sekar	20.00							20.00
	18	By Carriage	12.60					12.60		
	20	By repairs	41.50				41.50			
	25	By bus fare	10.50			10.50				
	27	By telegram	6.50	6.50						
	30	By printing	35.00		35.00					
			183.95	28.90	46.20	29.75	41.50	12.60	5.00	20.00
	31	By bal.c/d	16.05							
200.00			200.00							
16.05	Apr.1	To bal. b/d								
183.95	1	To cash								

SUMMARY

The sub-divisions of the journals into various book recording transactions of similar nature are called subsidiary boos. The subsidiary books are also known as book of original entry because transactions are first recorded in these books to be subsequently transferred to their respective accounts in the ledger.

EXERCISES

THEORY QUESTIONS

1. What are subsidiary books?
2. Explain the different types of subsidiary books.
3. Explain the utilities of subsidiary books
4. Differentiate trade discount and cash discount.
5. What is cash book? What are its features?
6. What are the advantages of cash book?
7. What are the various kinds of cash book?
8. Write short notes on contra entry.
9. Give the specimen of triple column cash book.
10. What is petty cash?
11. What is petty cash book?
12. What is the need for petty cash book?
13. Explain the imprest system of petty cash book.

14. Prepare purchase book from the following transactions.

2013 May 1 Purchased 100 bags of wheat @ Rs.50 per bag from M/s. Chenniyappan, Salem

3	Bought 20 tons of Vanaspathi Oil @ Rs.45 per ton from Kaveri Traders, less 10% trade discount
5	Purchased 10 boxes of chocolates @ Rs.20 per box from Selvan, Nazareth

15. Enter the following transactions in the sales book of Ramu and post them in the ledger.

2.1.2013	Sold 2 bags of sugar to Gopi stores at Rs.250 per bag at 5% trade discount
15.1.2013	Sold to Ravi 100 tons of Amul Milk Powder at Rs.20 per tin at 10% trade discount
20.1.2013	Sold to Solai 100 Kg coffee seeds at Rs.15 per kg.
25.1.2013	Sold to Vasu 50 kg tea at Rs.20 per kg.

16. Enter the following transactions in the proper subsidiary books.

2014 Apr.1	Purchased goods from Das Rs.1,000
2	Sold goods to Sen Rs.400
3	Sold goods to Ramesh Rs.250
5	Bought goods from Suresh Rs.200
7	Sold goods to A for cash Rs.300
8	Received goods returned by Sen Rs.50
9	Purchased goods from Shyam Rs.600
10	Returned goods to Suresh Rs.100

17. Enter the following transactions in the proper subsidiary books

2015 Dec. 1	Bought goods from Sekar Rs.3,000
2	Sold goods to Suresh Rs.2,000
3	Ganesh sold goods to us Rs.2,000
8	Nagaraj bought goods from us Rs.4,000
11	Received goods returned by Suresh Rs.800
13	We returned goods to Sekar Rs.50
19	Sold goods to Arul Rs.6,000
21	Purchased goods from Karthik Rs.7,000
24	Returned goods to Ganesh Rs.1,000
30	Sold goods to Chandra Rs.7,000

18. Enter the following transactions in a single column cash book of Mr.A.Praveen Samuel

2016 Jan. 1	Started business with cash Rs.10,000
5	Purchased goods for cash Rs.4,000
6	Purchased goods from X & Co. Rs.2,000
7	Paid into Bank Rs.3,000
12	Paid to X & Co. Rs.2,000
18	Sold goods for cash Rs.5,800

20 Sold on credit to Y & Co. Rs.3,200
25 Paid salaries Rs.600
27 Received cheque from Y & Co. Rs.2,200
28 Received commission Rs.400
30 Purchased furniture Rs.815
31 Drawn from Bank Rs.1,500

19. Enter the following transactions in cash book with cash and discount column of Mr. Nandakumar

2015 Jan. 1 Cash in hand Rs.60,000
3 Bought goods from Premnath Rs.10,000
4 Opened a current account with bank Rs.15,000
7 Withdrew from bank Rs.5,000
8 Sold goods to Kandan for Rs.10,000 credit on terms 2% cash discount if payable within two weeks.
10 Paid cash to Premnath, less 1% cash discount
14 Received a cheque from Arul Rs.3,400, allowed him discount Rs.100
15 Kandan settled his account

20. Enter the following transactions in cash book with cash and bank columns: Balance the cash book.

2014 May.1 Cash in hand Rs.30,000
2 Paid into bank Rs.10,000
3 Cash purchases Rs.2,500
4 Loan obtained from Vasan Rs.10,000
5 Cash deposited in bank Rs.7,500
6 Cash sales Rs.2,500
8 Rent paid by cheque Rs.2,000
10 Cash withdrew for office use Rs.4,000
14 Paid Nataraj Rs.300 by M.O.
15 Akilan directly paid into our bank account Rs.3,000
25 Cash withdrawn from bank Rs.5,000

21. Enter the following transactions of Syed Ali in columnar cash book.

2013 Mar.1 Opening balance: Cash Rs.6,830, Bank Rs.18,700
3 Sold goods for cash Rs.2,400
5 Paid dues to Deen Rs.1,400 by cheque
7 Paid office rent Rs.1,200
9 Received Rs.1,800 from Rabani in full settlement of his debt of Rs.2,000
11 Paid wages Rs.750
13 Withdrew Rs.4,000 from bank and paid salaries Rs.2,600 and advertising charges Rs.700

19 Settled a debt of Rs.1,000 at 3% discount by issuing a cheque

22. Enter the following transactions in a three column cash book.

2016 Jan. 1 Capital introduced (in cash) Rs.30,000

1 Paid into bank Rs.8,000

5 Purchased goods by cheque Rs.1,000

6 Received cheque from Raman Rs.2,000, Allowed discount Rs.100

10 Cash sales Rs.7,000

12 Paid into bank Rs.3,000

15 Paid Gopal by cheque Rs.3,000, discount received Rs.50

20 Paid salaries by cheque Rs.1,000

25 Withdrew for office use Rs.2,000

31 Draw a cheque for personal use Rs.500

23. Prepare a petty cash book on the imprest system from the following:

2015 Mar.1 Cheque received Rs.100

2 Telegram Rs.8

3 Stationery Rs.3

4 Taxi rent Rs.15

9 Registered post Rs.13

12 Printing of receipt book Rs.9

19 Ink bottle Rs.4.50

25 Carriage Rs.6

CHAPTER 4
TRIAL BALANCE

INTRODUCTION

After posting the journal entries into the ledger, we have to prepare a statement called Trial balance.

Perhaps, we know how to prepare ledger accounts from the journal entries. We might have noticed how the two aspects of each business transactions are recorded while making entries in the books of accounts. That is, if one amount is debited to a given account, an equivalent amount is credited to the other account (or accounts) that are affected by the transaction. Thus, the fundamental principle of double entry system of book-keeping is that for every debit there must be a corresponding credit and vice versa, of an equal amount.

Both the aspects of a transaction are recorded in the preparation of journal as well as ledger. This being so, it follows that the total of the debit amount column must be equal to the total of the credit amount in the journal. If journal entries are correctly posted to different ledger accounts, the total of all debit postings in the ledger must be equal to the total of all the credit postings in the ledger. To satisfy himself that it so, a businessman always prepares a statement known as “Trial balance”, after the ledger postings are completed. It can be prepared monthly or annually or at any other time, if so desired.

OBJECTIVES

The main objectives of this chapter is are as follows

- To know the meaning and definition of trial balance
- To understand the objective of preparing trial balance
- To understand the advantages of preparing trial balance
- To study how to prepare trial balance

DEFINITION OF TRIAL BALANCE

A trial balance is a list of debit and credit balances (including cash and bank) standing in the books of a concern on a particular date, debits appearing on the debit column and credits in the credit column.

OBJECTIVES OF PREPARING TRIAL BALANCE

1. It provides a very good check on the accuracy of the work done in preparing ledger accounts. It brings us to the conclusion that some errors have been made in the books if the Trial Balance does not tally.
2. It facilitates the preparation of
    a. Trading and profit and loss account to find out whether the dealings have resulted in a profit or loss and
    b. Balance sheet to ascertain the financial position of the business based upon assets and liabilities.

ADVANTAGES OF PREPARING TRIAL BALANCE

The advantages of the trial balance are:

1. It helps to prove the arithmetical accuracy of the book-keeping work done during the period.
2. It supplies in one place, ready reference of all the balances of the ledger accounts
3. If any error is found out by preparing a trial balance, the same can be rectified before preparing final accounts.
4. It is the basis on which final accounts are prepared.

CONSTRUCTION OF TRIAL BALANCE

It is very easy to construct a Trial Balance on a given date. It is prepared on a loose sheet of paper ruled similar to that of Journal. A specimen ruling of a Trial Balance is given below.

Trial Balance

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

Illustration 1

	Rs.		**Rs.**
Cash a/c	8,075	Sales a/c	2,300
Capital a/c	10,000	Raja's a/c	1,500
Bank a/c	2,000	Purchase returns a/c	500
Purchases a/c	3,000	Sales returns a/c	50
Gupta's a/c	750	Rent a/c	200
Salaries a/c	300	Commission received a/c	75

Prepare trial balance

Solution:

Trial Balance

Particulars	**L.F.**	**Debit**		**Credit**	
		Rs.	**P.**	**Rs.**	**P.**
Cash a/c		8,075	00	-	
Capital a/c		-		10,000	00
Bank a/c		2,000	00	-	
Purchases a/c		3,000	00	-	
Gupta's a/c		750	00	-	
Sales a/c		-		2,300	00
Raja's a/c		-		1,500	00
Purchase returns a/c		-		500	00
Sales returns a/c		50	00	-	

Rent a/c		200	00	-	
Salaries a/c		300	00	-	
Commission received a/c		-		75	
Total		**14,375**	**00**	**14,375**	**00**

PREPARATION OF TRIAL BALANCE FROM THE GIVEN LEDGER BALANCES

A trial balance contains balances found in all the ledger accounts which may be listed as follows:

1. Assets and Liabilities
2. Expenses or losses and incomes or gains
3. Trading account items and
4. Provisions and reserves

1. Assets and Liabilities:*Asset accounts always show debit balance*. Example: Land and building, plant and machinery, patents, copy rights, furniture, sundry debtors etc., On the other hand *Liability account always shows credit balance*. Example: Sundry Creditors, Bills Payable, Bank Overdraft, Capital etc.

2. Expenses or Losses and Incomes or Gains:*All expense or loss account show debit balance*. Example: Bad debts, discount allowed, commission, advertising, carriage inwards, rent, taxes, insurance, audit fee, printing and stationery. *All income or gain account show credit balance*. Example: Rent received, commission received, interest earned, discount received etc.

3. Trading a/c items:*Opening stock, purchases, sales returns a/c show debit balances* and *sales, closing stock, purchase return a/c show credit balances*.

4. Provisions and Reserves:*Provisions and Reserves a/c show credit balances*. Example: Provision for doubtful debts, provision for discount on debtors. Certain provision shows debit balance like provision for discount on creditors.

Let us illustrate the above with the following example.

Example: Classify the following ledger balances under the heads of debit and credit.

a. Carriage inwards b. Carriage outwards c. Returns inwards
d. Returns outwards e. Freight inwards f. Freight outwards
g. Discount received h. Drawings i. Capital
j. Loan from Ramprasad k. Loan to Krishnakant
l. Bills receivable
m. Bills payable

Solution:

a. Carriage inwards – Expense – Debit balance
b. Carriage outwards – Expense – Debit balance
c. Returns inwards – Goods comes in – Debit

d. Returns outwards – Goods goes out – Credit
e. Freight inwards – Expense – Debit
f. Freight outwards – Expense – Debit
g. Discount received – Income – Credit
h. Drawings – Personal a/c – The receiver – Debit
i. Capital – Personal a/c – Giver – Credit
j. Loan from Ramprasad – Liabilities – Credit
k. Loan to Krishnakant – Asset – Debit
l. Bills receivable – Asset – Debit
m. Bills payable – Liability - Credit

Illustration2

From the under mentioned balances extracted from the books of a trader on 31st March 2012, prepare a Trial Balance as on 31st March 2012.

	Rs.		Rs.
Cash in hand	2,400	Plant and Machinery	1,20,000
Capital	2,00,000	Sales	4,00,400
Purchases	2,40,000	Furniture and fittings	30,000
Bills payable	44,000	Bad debts reserve	2,000
Stock (opening)	70,000	Bills receivable	40,000
Sundry debtors	1,00,000	Rent and taxes	20,000
Sundry creditors	48,000	Salaries	40,000
Wages	32,000		

Solution:

Trial Balance

Particulars	L.F.	Debit		Credit	
		Rs.	P.	Rs.	P.
Cash in hand		2,400	00	-	
Capital		-		2,00,000	00
Purchases		2,40,000	00	-	
Bills payable		-		44,000	00
Opening stock (Asset)		70,000	00	-	
Sundry debtors (Asset)		1,00,000	00	-	
Sundry creditors		-		48,000	00
Wages		32,000	00	-	
Plant and Machinery		1,20,000	00	-	
Sales		-		4,00,400	00
Furniture and fittings		30,000	00	-	
Bad debts reserve		-		2,000	00
Bills receivable		40,000	00	-	
Rent and taxes		20,000	00	-	
Salaries		40,000	00	-	
Total		**6,94,400**	**00**	**6,94,400**	**00**

Illustration 3

From the following list of balances, prepare a trial balance as on 31.3.2013

	Rs.		Rs.
Capital	1,00,000	Buildings	15,000
Drawings	18,000	Furniture	7,500
Motor van	25,000	Loan from Arun	15,000
Interest paid	900	Sales	1,00,000
Purchases	75,000	Stock	25,000
Wages	3,000	Salaries	15,000
Commission received	7,500	Debtors	28,100
Bank balance	20,000	Creditors	10,000

Solution:

Trial balance as on 31.3.2013

Particulars	L.F.	Debit		Credit	
		Rs.	P.	Rs.	P.
Capital		-		1,00,000	00
Buildings		15,000	00	-	
Drawings		18,000	00	-	
Furniture		7,500	00	-	
Motor van		25,000	00	-	
Loan from Arun		-		15,000	00
Interest paid		900	00	-	
Sales		-		1,00,000	00
Purchases		75,000	00	-	
Stock		25,000	00	-	
Wages		3,000	00	-	
Salaries		15,000	00	-	
Commission received		-		7,500	00
Debtors		28,100	00	-	
Bank balance		20,000	00	-	
Creditors		-		10,000	00
Total		**2,32,500**	**00**	**2,32,500**	**00**

Illustration4

The following balances are extracted from the books of Siril on 31st Dec.2014. Prepare a Trial Balance.

	Rs.		Rs.
Siril's Capital	15,000	Discounts (Dr.)	800
Siril's Drawings	2,500	Discounts (Cr.)	1,000
Furniture and fittings	1,300	Taxes	1,000
Bank overdraft	2,100	General expenses	2,000
Sundry creditors	5,500	Salaries	4,500
Business premises	10,000	Commission (Dr.)	1,100

Stock (1.1.2014)	11,000	Carriage on purchases	900
Sundry debtors	9,000	Reserve for bad and	
Rent from tenants	500	Doubtful debts	1,000
Purchases	55,000		
Sales	75,000		
Returns inwards	1,000		

Solution:

Trial balance as on 31.12.2014

Particulars	L.F.	Debit		Credit	
		Rs.	P.	Rs.	P.
Siril's Capital		-		15,000	00
Siril's Drawings		2,500	00	-	
Furniture and fittings		1,300	00	-	
Bank overdraft		-		2,100	00
Sundry creditors		-		5,500	00
Business premises		10,000	00	-	
Stock (1.1.2014)		11,000	00	-	
Sundry debtors		9,000	00	-	
Rent from tenants		-		500	00
Purchases		55,000	00	-	
Sales		-		75,000	00
Returns inwards		1,000	00	-	
Discounts (Dr.)		800	00	-	
Discounts (Cr.)		-		1,000	00
Taxes		1,000	00	-	
General expenses		2,000	00	-	
Salaries		4,500	00	-	
Commission (Dr.)		1,100	00	-	
Carriage on purchases		900	00	-	
Reserve for bad and doubtful debts		-		1,000	
	Total	**1,00,100**		**1,00,100**	

Illustration 5

Prepare the Trial Balance from the following balances of Mrs. Dilshad as on 31.12.2013.

	Rs.		Rs.
Capital	4,20,000	Cash in hand	25,000
Building	1,15,000	Cash at bank	84,700
Machinery	60,000	Salaries	94,000
Furniture	11,000	Rent	48,000
Car	68,000	Commission	1,400
Opening stock	86,000	Rates and taxes	2,600
Purchases	94,000	Bad debts	3,200

Sales	1,96,000	Insurance	2,400
Sundry debtors	16,200	General expenses	800
Reserve for doubtful debts	7,300	Sundry creditors	68,000

Solution:

Trial balance as on 31.12.2013

Particulars	L.F.	Debit		Credit	
		Rs.	P.	Rs.	P.
Capital		-		4,20,000	00
Building		1,15,000	00	-	
Machinery		60,000	00	-	
Furniture		11,000	00	-	
Car		68,000	00	-	
Opening stock		86,000	00	-	
Purchases		94,000	00	-	
Sales		-		1,96,000	00
Sundry debtors		16,200	00	-	
Reserve for doubtful debts		-		7,300	00
Cash in hand		25,000	00	-	
Cash at bank		84,700	00	-	
Salaries		94,000	00	-	
Rent		48,000	00	-	
Commission		1,400	00	-	
Rates and taxes		2,600	00	-	
Bad debts		3,200	00	-	
Insurance		2,400	00	-	
General expenses		800	00	-	
Sundry creditors		-		68,000	00
Suspense a/c		-		21,000	00
Total		**7,12,300**	**00**	**7,12,300**	**00**

Note: Since the trial balance did not tally, the difference is transferred to Suspense a/c.

SUMMARY

With the help of ledger balances, a trail balance is prepared in order to test the arithmetical accuracy of accounts.

EXERCISES

SHORT QUESTIONS

1. What do you mean by trial balance?
2. What is the objective of preparing trial balance?
3. Explain the advantage preparing trial balance.

LONG QUESTIONS

1) How can you prepare trial balance from ledger?

2) From the following balances extracted from the books of Mahimaidoss, prepare a trial balance as on 31st March 2013.

	Rs.		**Rs.**
Capital	24,500	Loan (Cr.)	7,880
Drawings	2,000	Sales	65,360
General expenses	3,500	Purchases	47,000
Buildings	11,000	Motor car	2,000
Machinery	9,340	Reserve fund	900
Stock	16,000	Commission (Cr.)	2,370
Taxes and Insurance	1,315	Car expenses	1,800
Wages	7,200	Bills payable	3,800
Debtors	7,280	Cash	80
Bad debts	550	Bank overdraft	4,300
Creditors	2,500	Charity	105
Discount	2,440		

(Ans.: T.B. Total Rs.1,11,610)

3) The following are the balances extracted from the books of Mohamed as on 31st Dec.2013. Prepare a trial balance.

	Rs.		**Rs.**
Capital	20,000	Drawings	5,000
Cash in hand	5,000	Cash at bank	8,000
Buildings	20,000	Machinery	6,000
Stock on 1.1.2013	3,000	Sundry debtors	8,000
Sundry creditors	6,000	Repairs	400
Commission paid	700	Wages	1,700
Rent and rates	300	Insurance premium	1,150
Purchases	60,000	Sales	96,000
Purchase returns	750	Sales returns	400
Furniture and fixture	750	Carriage	200
Loan to Ram	1,000	Telephone charges	250
Discount allowed	50	Salaries	600
Bad debts	350	Discount earned	100

(Ans.: T.B. Total Rs.1,22,850)

4) Redraw correctly the trial balance given below:

Debit	Rs.	Credit	Rs.
Capital	8,000	Debtors	7,580
Bad debts recovered	250	Bank deposit	2,750
Creditors	1,250	Discount allowed	40
Returns outwards	350	Drawings	600
Bank overdraft	1,570	Returns inwards	450
Rent	360	Sales	14,690
Salaries	850	Bills payable	1,350
Postage	300		
Cash in hand	210		
Opening stock	2,450		
Purchases	11,870		
	27,460		**27,460**

5) Following are the balances of accounts in the ledger of a business on 31.12.2014. Prepare a trial balance on that date

	Rs.		Rs.
Capital	1,00,000	Machinery	25,000
Bills receivable	7,500	Bills payable	6,500
Purchases	1,25,000	Stock (1.1.2014)	27,500
Rent paid	8,000	Salary	15,000
Sales	1,75,000	Return inwards	2,000
Return outwards	2,500	Drawings	10,000
Wages	10,000	Cash on hand	5,000
Discount allowed	1,500	Discount received	3,000
Creditors	25,000	Debtors	22,500
Fixed assets	60,000	Bad debts	3,000

(Ans.: T.B. Total Rs.3,12,000)

CHAPTER 5

RECTIFICATION OF ERRORS

INTRODUCTION

The fundamental principle of the double-entry system is that every debit has a corresponding credit of equal amount and vice-versa. Therefore, the total of all debit balances in different accounts must be equal to the total of all credit balances in different accounts i.e., the total of the two columns should tally (agree).

The tallying of the two totals (debit balances and credit balances) of the trial balance ensures only arithmetic accuracy but not accounting accuracy. If however, the two totals do not tally, it implies that some errors have been committed while recording the transactions in the books of accounts. The following are the various kinds of errors.

OBJECTIVES

The main objective of this chapter is as follows

- To know the kinds of errors
- To know how to locate errors
- To know how to rectify the errors

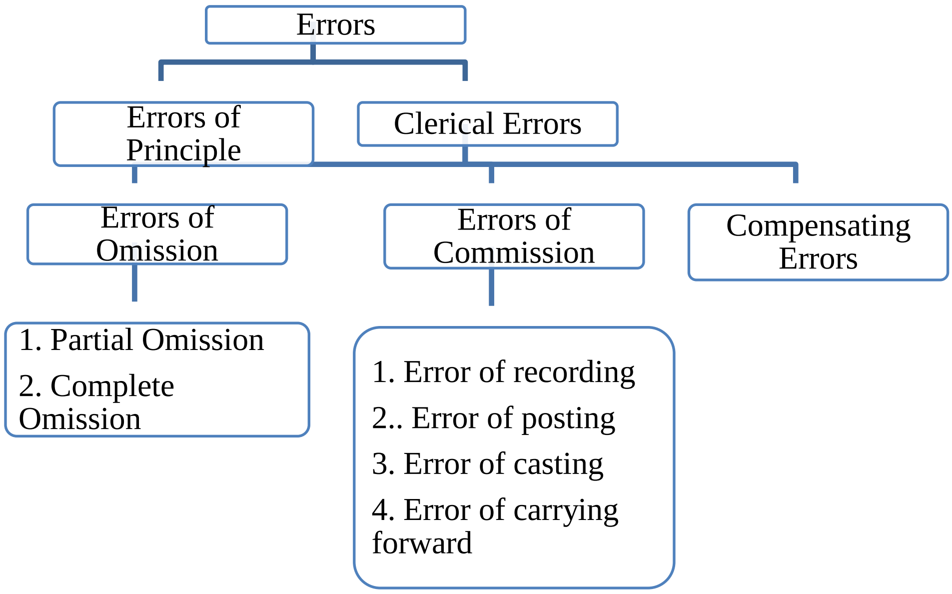
KINDS OF ERRORS

Keeping in view the nature of errors, all the errors committed in the accounting process can be classified into two.

i. Errors of Principle and

ii. Clerical Errors

Kinds of Errors



I. Errors of Principle

Transactions are recorded as per generally accepted accounting principles. If any of these principles is violated or ignored, errors resulting from such violation are known as **errors of principle.** For example, Purchase of assets recorded in the purchases book. It is an error of principle, because the purchase book is meant for recording credit purchases of goods and not for purchases of fixed assets. A trial balance will not disclose errors of principle.

II.Clerical Errors

These errors arise because of mistakes committed in the ordinary course of accounting work. These can be further classified into three types as follows.

a) Errors of omission

This error arises when a transaction is completely or partially omitted to be recorded in the books of accounts. Errors of omission may be classified as below.

i. Error of complete Omission: This error arises when a transaction is totally omitted to be recorded in the books of accounts. For example, goods purchased from Ram completely omitted to be recorded. This error does not affect the trial balance.

ii. Error of partial Omission: This error arises when only one aspect of the transaction either debit or credit is recorded. For example, a credit sale of goods to Siva recorded in sales book but omitted to be posted in Siva's account. This error affects the trial balance.

b) Errors of Commission

This error arises due to wrong recording, wrong posting, wrong casting, wrong balancing, wrong carrying forward etc. Errors of commission may be classified as follows:

i. Error of Recording: This error arises when a transaction is wrongly recorded in the books of original entry. For example, Goods of Rs.5,000, purchased on credit from Viji, is recorded in the book for Rs.5,500. This error does not affect the trial balance.

ii. Error of Posting: This error arises when information recorded in the books of original entry are wrongly entered in the ledger. Error of posting may be

i. Right amount in the right side of wrong account.
ii. Right amount in the wrong side of correct account.
iii. Wrong amount in the right side of correct account
iv. Wrong amount in the wrong side of correct account
v. Wrong amount in the wrong side of wrong account
vi. Wrong amount in the right side of wrong account, etc.

This error may or may not affect the trial balance.

iii. Error of Casting (Totalling): This error arises when a mistake is committed while totalling the subsidiary book. For example, instead of Rs.12,000 it may be wrongly totalled as Rs. 13,000. This is called **overcasting.** If it is wrongly totalled as Rs.11,000, it is called **under casting.**

iv. Error of Carrying Forward: This error arises when a mistake is committed in carrying forward a total of one page to the next page. For example, total of purchase book in page 282 of the ledger Rs.10,686, while carrying forward the balance to the next page it was recorded as Rs.10,866.

c) Compensating Errors

The errors arising from excess debits or under debits of accounts being neutralized by the excess credits or under credits to the same extent of some other account is compensating error. Since the errors in one direction are compensated by errors in another direction, arithmetical accuracy of the trial balance is not at all affected in spite of such errors. For example, if the purchases book and sales book are both overcast (excess totalling) by Rs.10,000, the errors mutually compensate each other. This error will not affect the agreement of trial balance.

ERRORS NOT DISCLOSED AND DISCLOSED BY TRIALBALANCE

If the impact of the errors on trial balance is considered, errors may be classified into two categories-Errors disclosed by trial balance, and Errors not disclosed by trial balance.

ERRORS NOT DISCLOSED BY A TRIAL BALANCE

1. Error of Omission

Certain transactions arenot recorded in the subsidiary books. Hence both debit and creditaspects of such transactions are omitted and hence the agreement of trial balance will not be affected.

Example: A Credit sales to Ravi is not entered in the sales book.

2.A wrong Entry in a subsidiary Book

A credit purchase of Rs.892 from Raju is wrongly written in the purchase book as Rs. 298. Such error will not be shown by Trial Balance because the posting of debit side of purchase a/c and credit side of Raju a/c will be with the wrong amount of Rs.298. Hence trial balance will agree.

3. Error of commission

When the book-keeper has committed some mistakes in making entries in the books, it is known as error of commission. Such error will not affect the trial balance.

Example: Cash Received from Mohan is wrongly credited to Sohan a/c.

4. Error of principle

An error of principle is an error which violates the fundamental principles of Book-keeping. This error will not affect the trial balance.

Example: Purchase of Machinery is recorded on the debit side of purchase a/c instead of Machinery a/c.

5. Compensating Errors

When one error is compensated by another error, it is called as compensating error. Such errors do not affect Trial Balance.

ERRORS DISCLOSED BY A TRAL BALANCE

The following errors are disclosed by Trial Balance, i.e. the Trial Balance will not agree if such errors are made:

1.An item omitted to be posted

A sale of goods to Babu of Rs.2,000 is omitted to be debited to Babu a/c. Hence debit side of the trial balance will be Rs.2000 less as compared to the credit side. Sothe trial balance will disagree to the extent of Rs.2000.

2. Posting of Wrong amount

Purchase of goods from Mala for Rs.3,500 has been wrongly posted to her account as Rs.2,500. Hence the credit side of the trial balance will be Rs.1,000 less as compared to debit side. Hence the trial balance will disagree to the extent of Rs.1,000.

3. Posting an amount on the wrong side

Rs.2,000 discount allowed to Ganesh wrongly credited discount a/c instead of debiting discount a/c. As a result credit side of trial balance will be more by Rs.4,000.

4. Wrong additions or balancing in ledger accounts

While balancing sales a/c if the credit side total of Rs.1,10,000 wrongly taken as Rs.1,00,000, the credit total of the trial balance will be Rs.10,000 under cast.

5. Error in carrying forward the total of one page to another page

Carrying forward the total Rs.1,876 of one page of debtors ledger to next page as Rs.1,786 the total debit balance will short by Rs.90

6. Error in preparation of debtors list and creditors list

If any name in the debtors list is omitted, the debit of trial balance will be short by that amount.

7. Omission of an account from trial balance

If machinery account is omitted in the trial balance, the trial balance will not tally.

LOCATING ERRORS

If the trial balance is not agreeing, the following steps are to be taken in order to locate errors.

1. Recheck the balancing of various accounts.
2. Check the postings
3. Check both debit and credit total again
4. Recheck the individual debtors and creditors account.
5. Verify whether cash and bank balance have been brought to the trial balance.
6. See that the totals of all subsidiary books are posted.
7. Compare the figures with the Trial balance of the previous year.
8. See that the opening balance has been correctly brought forward in current year books.
9. Recheck the totals of trial balance and find out the exact amount of difference in trial balance. This may represent any account which is omitted.

RECTIFYING THE ERRORS

Rectifying would mean correcting the mistake that has occurred.

Once the error is located, we should focus our attention to the correction of the error which is also described as Rectification of the Error.

PROCEDURE OF RECTIFICATION

The following three steps may usefully be adopted while attempting to rectify an error.

1. Ascertain what has actually been done, i.e. what is the error.
2. Make sure what ought to have been, i.e. the correct record.
3. Decide what is to be done in view of what has been done and what ought to have been done. i.eRectification.

Certain errors affect only one side of an Account. These one sided errors do not require journal entries for rectification. In the case of such errors what is to be done is (a) either to make an entry on the debit side of an Account to increase the debit value or to reduce the credit value of the Account or (b) to make an entry on the credit side of an Account to increase the credit value or to reduce the debit value of the Account.

There are other errors which affect both the accounts found in a transaction. These two-sided errors can be rectified by appropriate journal entries designed either to record an Omission or to rectify an Error of Commission or an Error of Principle.

RECTIFICATION OF ONE-SIDED ERRORS

ERRORS OF TOTALING OR CASTING

Example: 1

Rectify the following errors:

(i) Purchase Book is overcast by Rs.700(for the month of January)

(ii) Sales Book has been undercast by Rs.250.

(iii) Purchase Returns Book has been overcast by Rs.100.

(iv) Sales Returns Book has been undercast by Rs.80.

Explanation

S.No.	Name of Mistake	Effect of mistake	Rectification
1.	Over casting ofPurchase Book	Excess debit	Credit - Purchases a/c
2.	Under casting of Sales Book	Under Credit	Credit - Sales a/c
3.	Over casting of Purchases Returns Book	Excess Credit	Debit – Purchases Returns a/c
4.	Under casting of Sales Returns Book	Under debit	Give a further debit To Sales Returns a/c

Rectification

(i) Credit purchases a/c with Rs.700.

(ii) Credit Sales a/c with Rs.250.
(iii) Debit Purchases Returns a/c with Rs.100.
(iv) Debit Sales Returns a/c with Rs.80.

ERRORS OF CARRY FORWARD

This type of error is committed by taking wrong figure from one end of the page to the beginning of the next page.

Example: 2

(i) A total of Rs.798 in the Purchases Book has been carried forward as Rs.897
(ii) The total of the Sales Book, Rs.968 on page 15 was carried forward to page 16 as Rs.698.
(iii) A Purchases Returns Book was carried forward as Rs.3,280 instead of Rs.2,380.
(iv) A Sale Book total is carried forward Rs.450 more.
(v) A Purchases Book is carried forward Rs.100 less

Explanation

Name of Mistake	Effect of mistake	Rectification
1 Carrying forward higher amount in purchases Book	Excess debit	Credit the Purchases a/c
2 Carrying forward lower amount in sales Book	Under Credit	Give further Credit to Sales a/c
3 Carrying forward higher amount in purchases Returns Book	Excess Credit	Debit Purchases Returns a/c
4 Higher amount in Sales Book	Excess Credit	Debit Sales a/c
5 Carrying forward lower amount in purchase Book	Under debit	Give a furtherdebit to purchases a/c

Rectification

(i) Credit purchases a/c with Rs.99
(ii) Credit Sales a/c with Rs.270
(iii) Debit Purchase Returns a/c with Rs.900
(iv) Debit Sales a/c with Rs.450
(v) Debit Purchases a/c with Rs.100.

ERRORS OF POSTING

These errors, known as Errors of Commission, may occur as

(a) Failure to post to the personal a/c in the ledger
(b) Posting a wrong amount on the correct side of the Ledger and
(c) Posting the correct amount on the wrong side of the ledger
(d) Posting a wrong amount on the wrong side of the ledger.
(e) All these errors affect only one side of the account

Example: 3

Rectify the following errors

(a) Purchases from Kokila for Rs.500 has been omitted to be posted to the personal Account.

(b) Sales to Kumari for Rs.890 has been posted to her Account as Rs.98.

(c) Purchases from Amudha for Rs.750 has been posted to the debit side of her Account.

(d) Sales to Sundari for Rs.760 has been posted to her credit as Rs.670.

Rectification

(a) This is an omission to post to the Personal Account. Note that posting must be to the credit of Kokila's Account.For Rs.500.

(b) Here Kumai's a/c has been debited with a wrong amount. i.e. with excess amount. To rectify this error, the excess amount must be credited to her a/c.

(c) Purchases from Amutha must have been posted to the credit on Amutha's Account. But it has been debited.
Hence Credit Amutha's Account with double the amount i.e. Rs.1,500. (in order to cancel the wrong debit and to credit)

(d) Sales to Sundari must find itself on the debit side of Sundari's a/c. But her Account is credited with Rs.670. Sundri's a/c must show a debit of Rs.760.Hence, Debit Sundari's a/c with Rs.760+670 i.e., Rs.1,430

The Errors which Affect Two or More Accounts

No.	Error	Rectification
1.	**Error of Principle:** (e.g) Purchase of Furniture form Jayam furniture mart Rs.5000 was passed through Purchases book	Debit the Account which needs To be debited i.e. Furniture a/c Credit the account which is wrongly debited, i.e. Purchases Book a/c. Hence, the entry is Furniture a/c Dr. 5,000 To purchase a/c 5,000
2.	**Error of Complete Omission** (e.g) A credit purchase of Rs.20,000 from Aruna& Co was omitted to bePassed through Invoice book	Here the appropriate journal entry to record transaction is to be made. Hence, the rectification entry is Purchases a/c Dr. 20,000 To Aruna a/c 20,000
3.	**Wrong Amount Recorded in TheSubsidiary Book** (a) (e.g) A credit sales of Rs.5,000 to Raman &Co. was recorded in the Sales Book as Rs.500	This error results in lower amount recorded in Sales a/c as well as in Raman a/c Hence, Raman &Co a/c Dr. Rs.4,500 To Sales a/c Rs.4,500

	(b) A credit sales of Rs.5,000 fromRaman& co was entered in theSales Book as Rs.50,000	This error results in excess amount Recorded in Sales a/c as well as in Raman &Co's a/c. Hence reverse Entry for the excess amount is Sales a/c Dr. 45,000 To Raman&Co.a/c 45,000
4.	**Wrong posting** (a) Posting correct amount to correctSide, but to wrong Account. (e.g)Goods Returned by Kumaran Rs.1,000 posted to Guhan a/c (b) Posting to correct side but to wrong a/c and a wrong amount. (e.g)Rent Rs.450 for Proprietor's house was debited to Rent a/c as Rs.540	In this transaction, Kumaran a/c must be credited. But Guhan a/c has been credited. Hence: Guhan a/c Dr. Rs.1,000 To Kumaran a/c Rs.1,000 Wrong debit to rent a/c instead of Drawings a/c Principle is the same as the above. Drawings a/c Dr. 450 To Rent 540
5.	**Recording In a Wrong SubsidiaryBook (**e.g**)** A credit purchase of Goods from Ganesh & Co wasPassed through the Sales DayBook Rs.3,000.	This error involves three-fold mistakes (a) Sales a/c is wrongly Credited (b) Purchases a/c is omitted to be debited (c) Ganesh & Co has been wrongly debited. Hence Sales a/c Dr. 3,000 Purchases Dr. 3,000 To Ganesh & Co a/c 6,000
6.	**Compensating Errors** Excess credit in Sales Account Rs.1,600 is compensated by the excess Debit in Rent a/c Rs.1,400 and Michael a/c is totaled short Rs.200 credit.	These errors involve three Accounts. (a) Sales account shows an excess Credit of Rs.1,600 and so it is to be cancelled i.e reverse entry to be given. So, Sales a/c should be debited with Rs.1,600. (b) Rent account shows an excess Debit of Rs.1,400. To cancel this debit Rent a/c should be credited with Rs.1,400 (c) Michael's a/c shows a deficit in Credit Rs.200. To overcome this deficit an additional credit should be given for Rs.200

		Sales a/c Dr. Rs.1,600 To Rent a/c 1,400 To Michael a/c 200

SUSPENSE ACCOUNT

It was mentioned earlier that mistakes which affect one account affect agreement of the Trial Balance. If the errors cannot be located immediately, the difference in the Trial Balance is made good by entering the amount of difference on the lighter side under the heading “Suspense a/c”.

Suspense Account is temporary and imaginary account which is closed later when the errors are located & rectified.

The artificial tallying of the Trial Balance by the introduction of Suspense a/c enables the Final Accounts to be prepared even before the location of errors.

The Suspense a/c balance is shown on the asset side or on the liabilities side accordingly as debit balance or credit balance.

Example: 4

A book-keeper having failed to agree the Trial Balance, Opened a Suspense account and transferred the difference of Rs.3,790 to the credit of Suspense a/c. The following errors were later discovered. Give journal entries and show the Suspense Account.

(a) Sales Book was undercast by Rs.4,000
(b) Purchases of Machinery for Rs.6,000 was passed through the purchases Book.
(c) Goods Sold to Sakthivel for Rs.450 was posted to his account as Rs.540.
(d) Purchase Returns Book was overcast by Rs.200.
(e) The total of the sales Book from page 23 was carried forward as Rs.1,222 instead of Rs.1,122

Rectification entries (Using Suspense a/c)

Note:

In the case of those which affect only one account introduce Suspense a/c to make up a Journal Entry.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
(a)		Suspense a/c Dr. To sales a/c (Undercasting of Sales rectified)		4,000	 4,000
(b)		Machinery a/c Dr. To purchases a/c		6,000	 6,000

		(Debit to purchases instead of Machinery a/c rectified)			
(c)		Suspense a/c (540 - 480) Dr. To Sakthivel a/c (Excess debit given to Sakthivel rectified)		90	 90
(d)		Purchase Returns a/c Dr. To Suspense a/c (Overcasting Purchase Returns Book rectified)		200	 200
(e)		Sales a/c Dr. To Suspense a/c (Excess carry forward of the total of Sales Book rectified)		100	 100

Note: Suspense a/c is to be opened with a credit balance of Rs.3,790.

Suspense Account

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To Sales a/c To Sakthivel a/c	4,000 90		By Difference in Books By Purchase returns a/c By Sales a/c	3,790 200 100
		4,090			**4,090**

Example: 5

The following errors were discovered in the books of Sumathi on December 31, 2014.

(a) Rectify the errors without opening Suspense a/c

(b) Given that the difference in Trial Balance Rs.2,610 was debited to Suspense a/c, (give journal entries with Suspense a/c)

(c) Show the Suspense a/c.

1. The total of Purchases Book for December was undercast by Rs.1,000

2. Rs.760 paid for repairing Machinery had been debited to Machinery a/c.

3. Cash Rs.390 received from Rathinam though entered in the Cash book had not been posted to Rathinam's a/c

4. The Sales Book has been overcast by Rs.500.

5.A Sale of Rs.4,000 to Kathir has been passed through the purchases book.

6. Goods returned by Tamil Selvi Rs.750 have been entered in the Returns outwards Book. However, Tamilselvi's a/c is correctly posted.

Rectification without Suspense a/c

1. Debit Purchase a/c with Rs.1,000

2. Repairs a/c Dr. 760

To Machinery a/c 760

(Entry to rectify wrong debit to Machinery a/c)

3. Credit Rathinam's a/c with Rs.390

4. Debit Sales a/c with Rs.500

5. Kathir a/c Dr. 8,000

To Sales a/c 4,000

To Purchase a/c 4,000

(Entry to rectify wrong entry in Purchases Book)

6. Debit Returns outwards a/c 750

Debit Returns Inwards a/c 750

(Entry to rectify wrong credit given to Returns Outwards a/c)

Rectification with Suspense a/c

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
1.		Purchases a/c Dr. To Suspense a/c (Rectification of Purchasers Books undercast)		1,000	 1,000
2.		Repairs a/c Dr. To Machinery a/c (Entry to rectify wrong debit to Machinery a/c)		760	 760
3.		Suspense a/c Dr. To Rathinam a/c (Completion on double entry for cash receivedOmitted to be posted to personal a/c)		390	 390
4.		Sales a/c Dr. To Suspense a/c (Sales book overcast is rectified)		500	 500
5.		Kathir a/c Dr. To Sales a/c To Purchases a/c (Entry to rectify wrong entry in purchases book)		8,000	 4,000 4,000
6.		Returns outwards a/c Dr. Returns inwards a/c Dr.		750 750	

		To suspense a/c (Being correction of returns inwards wrongly credited to returns outwards a/c, the personal a/c being correctly credited)			1,500

Suspense Account

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To Difference in TB	2,610		By Purchase a/c	1,000
	To Rathinam a/c	390		By Sales a/c	500
				By Returns Outwards a/c	750
				By Returns Inwards a/c	750
		3,000			**3,000**

Practical Problems

Illustration 1

Following errors were committed. Rectify them by passing journal entries.

i) Sales to X Rs.2,000 were not recorded.

ii) Purchases from Y Rs.11,000 were omitted from the books.

iii) Bills receivable of Rs.4,500 endorsed to Bala was not entered in the book

iv) Sales Returns of Rs.250 from X were not recorded.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
i)		'X' a/c Dr. To Sales a/c (Being sales to 'X' is recorded)		2,000	2,000
ii)		Purchase a/c Dr. To 'Y' a/c (Being purchase to 'Y' is received)		11,000	11,000
iii)		Bala a/c Dr. To Bills Receivable a/c (Being Bills Receivable endorsed to Bala is recorded)		4,500	4,500
iv)		Sales Returns a/c Dr. To 'X' a/c (Being Sales Returns recorded)		250	250

Illustration 2

Rectify the following errors

i) Sale to Ravi Rs.14,000 posted to Mathi's a/c.

ii) Sales to Ravi Rs.400 debited to Mathi's a/c.

iii) Sales to Ravi Rs.400 credited to Mathi's a/c

iv) Sales to Ravi Rs.2,400 debited to Mathi's a/c as Rs.400.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
i)		Ravi a/c Dr. To Mathi a/c (Being wrong posting is rectified)		14,000	 14,000
ii)		Ravi a/c Dr. To Mathi a/c (Being wrong debit is rectified)		400	 400
iii)		Ravi a/c Dr. Mathi a/c Dr. To Suspense a/c (Being wrong credit is rectified)		400 400	 800
iv)		Ravi a/c Dr. To Mathi a/c To Suspense a/c (Being wrong debit is rectified)		2,400	 400 2,000

Illustration 3

The trial balance of Mr. Swamynathan on 31st December 2014 did not agree and on checking the records, the following errors were found out.

1. Wage paid for erection of machinery amounting to Rs.600 were debited to wages account as Rs.1,600.
2. The total of purchases return book was under cast by Rs.100.
3. Rs.7,500 paid for the purchase of motor cycle for the private use of the owner was charged to miscellaneous expenses a/c
4. A sales of Rs.300 was entered in the sales returns book. But the posting there from was made to the debit of the customers a/c.

You are required to rectify the above errors, by passing journal entries.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
1		Machinery a/c Dr. Suspense a/c Dr. To Wages a/c		600 1,000	 1,600

		(Being wrong debit to wage account is rectified)			
2		Suspense a/c Dr. To Purchase Return's a/c (Being under cast of purchase return book is rectified)		100	100
3		Drawings a/c Dr. To Miscellaneous expenses (Being wrong debit is rectified)		7,500	7,500
4		Sales Returns a/c Dr. To Sales a/c (Being wrong entry in sales returns book is rectified)		300	300

Illustration 4

1. A mistake of over casting by Rs.100 was deducted in discount column on the credit side of the cash book.
2. Value of goods worth Rs.500 was taken by the owner for his personal use from stock.
3. Purchase of Rs.750 worth of goods from S. Narayanan was posted from the purchase book to the debit of Narayanan's a/c.
4. Goods sold to Sri Rama Raofor Rs.2,000 has been wrongly entered in the sales book as Rs.200.
5. Salary paid to Sridar an employee for Rs.600 has been debited to his personal a/c in the ledger.

Pass rectifying journal entries.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
1		Discount a/c Dr. To Suspense a/c (Being wrong credit to discount a/c is rectified)		100	100
2		Drawings a/c Dr. To Purchases a/c (Being goods taken by the owner is recorded)		500	500
3		Suspense a/c Dr. To Narayanan a/c (Being wrong debit to Narayanan a/c is rectified)		1,500	1,500
4		Rama Rao a/c Dr.		1,800	

		To Sales a/c (Being sale to Rama Rao is recorded)			1,800
5		Salary a/c Dr. To Sridar a/c (Being wrong debit to Sridar a/c is rectified)		600	 600

Illustration 5

Rectify the following errors by passing necessary journal entries.

1. An amount of Rs.200 withdrawn by the owner for his personal use had been debited to tradeexpenses a/c.
2. The purchase of goods from Pandi amounting to Rs.400 had been wrongly entered through the sales book.
3. A credit sales of Rs.200 to Raman has been wrongly passed through purchase book.
4. A periodical total of the sales book was cast short by Rs.150

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
1		Drawings a/c Dr. To Trade expenses a/c (Being wrong debit to trade expenses is rectified)		200	 200
2		Purchases a/c Dr. Sales a/c Dr. To Pandi a/c (Being wrong entry in the sales book is rectified)		400 400	 800
3		Raman a/c Dr. To Purchases a/c To Sales a/c (Being wrong entry in the purchases book is rectified)		400	 200 200
4		Suspense a/c Dr. To Sales a/c (Being under cast of sales book is rectified)		150	 150

Illustration 6

1. A book keeper of a trading concern having been not agree the trial balance,opened a suspense a/c and entered the difference, in trial balance. The following errors were subsequently discovered.

a) Purchase of furniture Rs.300 was passed through invoice book and from there furniture a/c was posted as Rs.20.
b) Sold goods to Ram Rs.55 was posted as Rs.550.
c) Sales book was over cast by Rs.200.
d) Purchase returns book was carried forward as Rs.122 instead Rs.112.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
a)		Suspense a/c Dr. Furniture a/c Dr. To Purchases a/c (Being wrong entry in the purchases book is rectified)		20 280	 300
b)		Suspense a/c Dr. To Ram's a/c (Being wrong entry in Ram's a/c is rectified)		495	 495
c)		Sales a/c Dr. To Suspense a/c (Being over cast of sales a/c is rectified)		200	 200
d)		Purchase Returns a/c Dr. To Suspense a/c (Being carry forward mistake is rectified)		10	 10

Illustration 7

Correct the following errors before the preparation of the trial balance:

a) The total of the return outward book cast Rs.100 Short.
b) A welding machine purchased for Rs.5,800 has been entered in the purchases book.
c) A sale of Rs.175 to Mrs. Gupta has been entered in the sales day book as Rs.157.
d) A purchase of Rs.215 from Mr.Gupta has been posted to the debit of his account.
e) A Sale of Rs.200 for old furniture has been passed through the sales book.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
a)		Purchase returns a/c credited with Rs.100			
b)		Welding Machine a/c Dr. To Purchases a/c (Being wrong debit in purchase a/c is rectified)		5,800	5,800
c)		Gupta's a/c Dr. To Sales a/c (Being wrong entry sales book is rectified)		18	18
d)		Gupta's a/c is credited with Rs.430			
e)		Sales a/c Dr. To Furniture a/c (Being wrong credit in sales a/c is rectified)		200	200

Illustration 8

a) A payment of an electricity bill of Rs.210 was posted from the cash book to the debit of postage and telephone as Rs.120.

b) Rs.500 paid for repairs to owner's residence has been charged to sundry expenses a/c.

c) Credit side of debtors a/c has been over cast by Rs.200.

Pass rectifying journal entries.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
a)		Electricity a/c Dr. To Postage and telephone a/c (Being wrong debit to postage and telegram a/c is rectified)		210	210
b)		Drawings a/c Dr. To Sundry Expenses a/c (Being wrong debit to Sundry expenses a/c is rectified)		500	500
c)		Debtor's a/c Dr. To Suspense a/c (Being over cast of credit side of debtor a/c is rectified)		200	200

Illustration 9

There is a difference in the trial balance of Shri. 'M' Subsequently, the following errors were found to have been committed. Pass necessary rectification entries.

1. A Sale of Rs .2,000 to Shanthi& Co. was credited to their account.
2. The Returns Inwards Book had been cast Rs. 1,000 short.
3. A Sale of Rs. 10,000 had been passed through the purchases Day Book – the Customer's account had, however, been correctly debited.
4. Rs. 3,750 paid for wages to workmen for making show cases had been charged to wages account.
5. A Purchases of Rs. 6,710 had been posted to the debit of the Creditor's account as Rs. 6,170. The Creditor was Paul & Co.

Solution:

Rectification Entries

S.No	Date	Particulars	L.F	Debit Rs.	Credit Rs.
1.		Shanthi a/c Dr. To Suspense a/c (Being wrong credit to Shanthi a/c is rectified)		4,000	 4,000
2.		Sales Return a/c Dr. To Suspense a/c (Being under casting of sales return book is rectified)		1,000	 1,000
3.		Suspense a/c Dr. To Purchases a/c To Sales a/c (Being wrong entry in the purchases book is rectified)		20,000	 10,000 10,000
4.		Show Cases a/c Dr. To Wage a/c (Being wrong entry in the wage a/c is rectified)		3,750	 3,750
5.		Suspense a/c Dr. To Paul & Co. a/c (Being wrong posting is rectified)		12,880	 12,880

Suspense Account

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To Purchases a/c To Sales a/c	10,000 10,000		By Shanthi a/c By Sales	400

	To Paul& Co.	12,880		Returns a/c By Difference in T.B	10,000 22,480
		32,880			**32,880**

SUMMARY

Every concern is interested in knowing the true profit and financial position of the concern. Though best efforts are made in the preparation of the accounts, there may be errors. There are two types of errors namely errors of principle and clerical errors. First there errors are to be located and then rectified.

EXERCISES

THEORY QUESTIONS

1. Enumerate the various kinds of errors.
2. What types of errors does a Trial Balance fail to disclose?
3. Mention the steps to be taken to locate the difference in a Trial Balance.
4. What are the mistakes that the Trial Balance will disclose?
5. Does a Trial Balance reveal all mistakes that a Book-Keeper commits?
6. What do you understand by Rectification of errors?
7. Illustrate error of Commission with examples.
8. What is error of Principle?
9. What is Suspense account? When it is prepared?
10. It what ways may errors be rectified?

PROBLEMS

Problem: 1

Rectify the following errors which are located in the book of Mr.Ganesh.

i) The purchase return book overcast by Rs.1,500.
ii) Received Rs.2,000 from Shankar debited to his account.
iii) The sales book undercast byRs.1,500.
iv) Rs.1,500 received from Geetha was entered on the debit side of the cash book. No posting was done to Geetha's a/c.
v) Sale of old furniture for Rs.2,000 was treated as sale of goods.

Problem: 2

Rectify the following errors:

i) Rs.12,000 paid of salary to cashier Govind, stands debited to his personal account.
ii) An amount of Rs.5,000 withdrawn by the proprietor for his personal use has been debited to trade expenses a/c.
iii) Cash received from Bala Rs.300 was credited to Balu.
iv) A credit sale of Rs.2,000 to Janakiram has been wrongly passed through the purchase book.

Problem: 3

A book keeper found his trial balance not balanced, placed the difference amount in the Suspense Account and subsequently found the following errors:

a) Sales Book was overcast by Rs.1,500.
b) Rs.2,900 received from Vani in full settlement of his account of Rs.3,000 was posted in cash book but omitted to be entered in her account.
c) The total of the sales book Rs.12,000 was debited to sales returns account.
d) Rs.1,000 received as interest was credited to interest account as Rs.100.

Give rectifying entries and show the Suspense Account.

Problem: 4

A bookkeeper's Trial Balance out of Rs.520 excess credit. He placed that amount in the Suspense Account and subsequently found the following errors.

a) The total of discount column on the credit side of the cash Book Rs.230 was not posted in the ledger.
b) The total of the discount column on the debit side of the cash Book Rs.150 was omitted to be posted in the ledger.
c) The total of the purchases book was short by Rs.600.
d) A sale of Rs.675 to Kalpana was entered in the Sales book as Rs.975.
e) A sale of Rs.500 to Vimala has been entered in the purchase Book.

Rectify the above errors through Suspense Account. Also give journal entries for rectification.

CHAPTER 6
BANK RECONCILIATION STATEMENT

INTRODUCTION

All banking transactions are recorded in two books, namely i) cash book and ii) pass book. Thereof, at any time, the balances shown by these books must be equal. But usually the balance of these two books does not agree. The correct reason for the differences is to be found out. The bank reconciliation statement is prepared showing the reasons for disagreement.

OBJECTIVES

After studying this unit, you can understand

- Definition of the bank reconciliation statement
- Advantage of bank reconciliation statement.
- Causes for the disagreement between the balance shown by pass book and cash book

DEFINITION

Bank reconciliation statement is a list in which the various items that cause a difference between bank balance as per cash book and pass book on any given date are indicated.

ADVANTAGES

1. The errors that might have taken place in cash in connection with bank transactions can be easily found out.
2. It imposes moral check on the accounting staff indirectly.
3. If the bank reconciliation statement is regularly prepared, frauds can be easily prevented.
4. By the preparation of bank reconciliation statement, uncredited cheque can be detected and steps can be taken for their collection.

CAUSES FOR DIFFERENCE

The reasons for the disagreement between the balance shown by the cash book and the pass book are given below.

1.Cheques deposited but not yet credited:

When a concern deposits its'cheque into bank, it immediately debits its bank account in his passbook. But the bank takes some time for the collection. Only after collecting the cheque, the bank will credit its account. Till then, the balance shown in the bank column in the cash book will be more than that of the balance shown in the pass book. For example XYZ company Ltd. deposited a cheque on March 31st, 2011 for a sum of Rs.3,000. The cheque was collected on April 4th, 2011. The bank sends a statement of account upto 31st march

2011, there will be a difference between the balance shown by the cash book and the pass book.

2.Cheques issued but not presented for payment:

Similarly when cheque is issued, the bank account is credited immediately. But the party takes some time for presenting the cheque. It causes a difference. For example, XYZ company Ltd. Issued a cheque in favour of Mr.Krishna on March 28th, 2011 for a sum of Rs.45,000. The cheque is presented for payment at the bank only on April 4th, 2011. In case, bank sends a statement of account up to March 31st, 2011 there will be a difference of Rs.5,000 between the balance as shown by the cash book and the balance as shown by the pass book.

3.Amount credited by the banker in the pass book without the immediate knowledge of the customer:

The following are some of the examples for the above statement.

1. The bank might have collected rent, dividend, bills of exchange, interest etc., due for the customer as per standing instructions.
2. Some debtors might have directly paid into bank.
3. Bank credits interest on the credit balance of the customer's account.
4. The banker has wrongly credited this account instead of some other account.

In all the above cases, the entry will be first entered in the pass book. The customer will know this only after he verifies the entries in the pass book. So there may be a time gap of some days before the customer includes entries made in the pass book.

For example, the bank has credited XYZ CompanyLtd. Account for interest amounting to Rs.500 on March 31st, 2011. The bank prepares and sends a statement of account on March 31, 2011. If the customer receives the statement of account on April 4, 2011 there will be a difference of Rs.500 between the balance shown by the cash book and the balance shown by the pass book.

4.Amounts debited by the banker in the pass book without the immediate knowledge of the customer:

The following are some of the examples for this.

1. The banker has recorded bank charges, interest on overdraft etc.,
2. The banker has paid insurance premium, subscription for periodicals etc., on behalf of the customer as per the standing instructions.
3. The banker has wrongly debited this account instead of some other account
4. The banker has paid the bills payable of the customer as per standing instructions
5. Dishonor of a cheque deposited and discounted bills receivable.

In all the above cases, the entry will be first entered in the pass book of the customer. And the customer will know only after he verified the entries in the pass book or statement of account. So there may be a time gap of some days before the customer includes the entries made in the pass book.

For example, the bank has debited XYZ CompanyLtd. account for its charges amounting to Rs.250 on March 31, 2011. In case, the bank sends a statement of account upto March 31, 2011 there will be a difference of Rs.250 between the balance as per the cash book and the balance as per the pass book.

After tracing the various items of differences, a bank reconciliation statement is prepared by starting with the balance shown by any one of the two books. But in actual practice, a bank reconciliation statement is prepared by the customer starting with the balance as per cash book and will ensure that the balance as per pass book is arrived at.

MODEL I

BALANCE AS PER CASH BOOK IS GIVEN – YOU HAVE TO FIND OUT BALANCE AS PER PASS BOOK:

In this case, we have to find out whether the **cash book balance** increases or decreases (because of the transactions). When increases it is deducted.When decreases it is added. For example, in example1 there is,

i) Unpresentedcheque Rs.675. When cheque is issued, cash book balance decreases – Hence it is added.

ii) Uncreditedcheque Rs.500. When cheque sent to the bank for collection, in the cash book the bank account is debited and hence cash book balance increases. In the BRS it is deducted.

iii) Bank charges entered in the pass book. Because of this pass book balance decreases but cash book balance increases – Hence it is deducted.

iv) Dishonour of the cheque – Pass book balance decreases – cash book balance increases – Hence it is deducted.

v) Wrong debit in the pass book – pass book decreases – cash book increases – Hence it is deducted.

Illustration: 1

On 30.9.2013 the cash book of Mr. Gopal showed a favourable bank balance of Rs.2,500. This balance did not tally with the balance showed by the pass book.

From the following particulars ascertain the bank balance as per pass book.

a. Chequessent to the bank for collection but not credited up to 30.9.2013 Rs.500
b. Cheques issued to customer but not presented for payment up to 30.9.2013 Rs.675
c. Bank charges not entered in the cash book Rs.10
d. A cheque issued by Mr. Gopalasamy for Rs.120 has been wrongly debited to Gopal’s account by the bank.

e. A cheque for Rs.50 deposited into a bank for collection has been dishonoured, but the fact of dishonor not recorded in the cash book.

Solution

Bank Reconciliation Statement of Gopal as on 30.9.2013

Particulars	Amount Rs.	Amount Rs.
Bank balance as per cash book		2,500
Add		
Unpresentedcheque	675	675
		3,175
Less		
Uncredited cheque	500	
Bank charges not entered in cash book	10	
Wrong debit in pass book	120	
Chequedishonoured	50	680
Bank balance as per pass book		**2,495**

Illustration: 2

On 30th June 2014 the cash book of ABC Company Limited showed a balance of Rs.2,760 at bank. He had sent cheques amounting to Rs.10,000 to the bank, before 30th June but it appears from the pass book that cheques worth only Rs.4,000 had been credited before that date. Similarly out of cheque Rs.5,000 issued in the month of June,cheque for Rs.2,500 were presented and paid in July. The pass book showed the following payments:

1. Rs.320 premium on Joint Life Policy according to standing instructions and
2. Rs.2,000 against a promissory note as per instruction.

The pass book showed the bank had collected Rs.600 as interest on government securities. The bank had charged interest Rs.50 and bank charges Rs.20. There was no entry in the cash book for these payments receipts interest and charges.

It was found that the total of the credit column in the cash book on 20th June was Rs.110 short. Prepare the Bank Reconciliation Statement as on 30.6.2014.

Solution

Bank Reconciliation Statement of ABC company Ltd. as on 30.6.2014

Particulars	Amount Rs.	Amount Rs.
Bank balance as per cash book		2,760
Add		
Unpresentedcheque	2500	
Interest collected	600	3100
		5,860

Less		
Uncredited cheque (10,000 – 4,000)	6,000	
Premium on Joint Life Policy	320	
Payment for promissory note	2,000	
Interest charged	50	
Bank charges	20	
Under casting in credit column of cash book	110	8,500
Bank balance as per pass book		**-2,640**

Note: Since pass book balance is negative, it is the overdraft balance

Illustration: 3

From the following particulars, prepare Bank Reconciliation Statement as on 31.3.2015.

Balance as per cash book on 31st March 2015 Rs.4,200. Cheques for Rs.3,100 were issued during the month of March, but not presented for payment. Cheques received and deposited into bank Rs.5,900 during the month of March, but not collected. The bank paid during March Rs.400 as Life Insurance Premium but no corresponding entry in cash book.

(B.U. 2010)

Solution

Bank Reconciliation Statement as on 31.3.2015

Particulars	Amount Rs.	Amount Rs.
Bank balance as per cash book		4,200
Add		
Cheque issued but not presented for payment		3,100
		7,300
Less		
Cheques received and deposited into bank	5,900	
Life Insurance Premium	400	6,300
Bank balance as per pass book		**1,000**

MODEL II

OVERDRAFT BALANCE AS PER CASH BOOK IS GIVEN – YOU HAVE TO FIND OUT OVERDRAFT BALANCE AS PER PASS BOOK:

For this model the procedure adopted in the first model is to be adopted. But in the statement, overdraft balance as per cash book is marked as minus.

Illustration:4

From the following particulars, prepare Bank Reconciliation Statement as at 31st December 2013.

a. On 31.12.2013 bank overdraft as per cash book Rs.2,49,900
b. Interest debited in the bank pass book only Rs.27,870

c. Cheques issued but not presented for payment Rs.66,000
d. Draft deposited in the bank, but not yet credited in the pass book Rs.13,500
e. Dividend collected by the bank Rs.42,500 has not been entered in the cash book
f. A direct payment into the bank by a customer Rs.16,000 has not been recorded in the cash book
g. Bank column on the debit side of the cash book has been under cast by Rs.3,500

Solution

Bank Reconciliation Statement as on 31.12.2013

Particulars	Amount Rs.	Amount Rs.
Overdraft balance as per cash book		-2,49,900*
Add		
Unpresentedcheque	66,000	
Dividend collected by bank	42,500	
Direct payment by our customer in the bank	16,000	
Under casting the debit column of cash book	3,500	1,28,000
		-1,21,900
Less		
Interest debited in pass book	27,870	
Uncredited cheque	13,500	-41,370
Overdraft as per pass book		**1,63,270**

Illustration: 5

On 31st December 2014 the cash book of Balan showed an overdraft of Rs.10,500. But the pass book shows a different balance due to the following reasons.

1. Cheque No.51 for Rs.540 in favour of A has not yet been presented.
2. A post datedcheque for Rs.300/- has been credited to the bank account in the cash book. But it would not been presented for payment.
3. 4 cheques totaling Rs.1,200 sent to the bank for collection have not yet been credited, while a 5thcheque for Rs.400 deposited in the account has been dishonoured.
4. Fire insurance premium amounting to Rs.50 paid by the bank understanding instruction has not been entered in the cash book
5. A bill for Rs.1,000 was retired by the bank under a rebate of Rs.15, but the full amount of the bill was credited in the bank account in the cash book.

Find out the balance as per pass book.

Solution

Bank Reconciliation Statement as on 31.12.2014

Particulars	**Amount Rs.**	**Amount Rs.**
Overdraft balance as per cash book		-10,500
Add		
Unpresentedcheque of A	540	
Unpresentedpost datedcheque	300	
Rebate of bill retired	15	855
		-9,645
Less		
Uncredited cheque	1,200	
Dishonouredcheque	400	
Fire insurance premium	50	-1650
Overdraft as per pass book		**-11,295**

MODEL III

BALANCE AS PER PASS BOOK IS GIVEN – YOU HAVE TO FIND OUT BALANCE AS PER CASH BOOK:

In this model, you have to ascertain whether **pass book balance**is more or less. If the pass book balance is more, it is deducted in the statement. If the pass book balance is less, it is added in the statement.

1. Uncredited cheque–Not credited in the pass book – pass book balance is less – hence it is added.
2. Incidental charges debited in the pass book – pass book balance is less – added in the statement.
3. Unpresentedcheques – cheque issued cash book balance is less – But in the bank it is not presented – so pass book balance is more – deducted in the statement.

Illustration: 6

From the following particulars prepare a Bank Reconciliation Statement showing the balance as per cash book on 31st December 2015.

The following cheques were paid into bank in December 2015 but were credited by the bank in January 2016.

Sundaravel - Rs.700
Sakthivel - Rs.500
Vetrivel - Rs.400

The following cheques were issued by the firm in December 2015 but were presented for payment in January 2016.

Kumaravel - Rs.800
Gnanavel - Rs.900

A cheque for Rs.200 which was received from a customer was entered in the bank column of cash book in December 2015 but was omitted to be banked in the month of December. The passbook shows a credit of Rs.200 for interest and a debit of Rs.40 for bank charges.

The bank balance as per pass book was Rs.12,400 on 31st December 2015.

Solution

Bank Reconciliation Statement as on 31.12.2015

Particulars	**Amount Rs.**	**Amount Rs.**
Bank balance as per pass book		12,400
Add		
Uncredited cheque:		
Sundaravel	700	
Sakthivel	500	
Vetrivel	400	
Cheques received entered in cash book but not banked	200	
Bank charged debited in pass book	40	1,840
		14,240
Less		
Unpresentedcheque:		
Kumaravel	800	
Gnanavel	900	
Interest credited as per cash book	200	1,900
Bank balance as per cash book		**12,340**

Illustration: 7

On 30th June 2015 the pass book of M/s. Thin and Short showed a balance of Rs.2,000 at the bank. They had sent cheques amounting to Rs.10,000 to the bank before 30th June but it appears from the pass book that cheques worth Rs.9,000 had been credited before that date. Similarly out of cheques for Rs.5,000 issued during the month of June, cheques for Rs.4,000 were presented and paid in July. The pass book also showed the following payments:

a. Rs.320 as premium according to standing instructions and
b. Rs.2,000 against a promissory note as per instructions. The pass book showed that the bank had collected Rs.1,800 as interest on Government securities. The bank had charged as interest Rs.50 and incidental expenses Rs.20. There was no entry in the cash book for the payment of interest etc. A bill sent for collection was returned dishonoured on 28th June amounting to Rs.600

Prepare the Bank Reconciliation Statement as on 30th June 2015.

Solution

Bank Reconciliation Statement of M/s. Thin & Short as on 30.6.2015

Particulars	Amount Rs.	Amount Rs.
Balance as per pass book		2,000
Add		
Uncredited cheque (10000-9000)	1,000	
Premium	320	
Interest and incidental charges charged by bank	70	
Promissory note	2,000	3,390
		5,390
Less		
Unpresentedcheque (5000-4000)	1,000	
Bank collection of interest on securities	1,800	
Bill for collection was returned dishonoured	600	3,400
Balance as per cash book		**1,990**

MODEL IV

WHEN OVERDRAFT BALANCE AS PER PASS BOOK IS GIVEN – YOU HAVE TO FIND OUT BALANCE AS PER CASH BOOK:

In this model, you have to follow the procedure that is followed in Model III. But in the statement, overdraft balance as per pass book is written by putting minus sign.

Illustration: 8

From the following particulars ascertain the balance that would appear in the cash book of Ram and Co., as on 30th June 2015.

1. Overdraft as per pass book on 30th June 2015 Rs.540
2. Cheques drawn but not presented up to 30th June 2015 Rs.2,800
3. Cheque paid into bank but not cleared up to 30th June 2015 Rs.3,900

Solution

Bank Reconciliation Statement of Ram & Co. as on 30.6.2015

Particulars	Amount Rs.	Amount Rs.
Overdraft as per pass book		-540
Add		
Cheque paid into bank but not cleared	3,900	3,900
		3,360
Less		
Cheque issued but not presented	2,800	2,800
Bank balance as per cash book (favourable)		**560**

Illustration: 9

On 31.1.2014 the pass book of Govindan showed a debit balance of Rs.41,000. Prepare a bank reconciliation statement with the following information:

a) Cheques amounting to Rs.15,600 were drawn on 27.1.2014, out of which cheques for Rs.11,000 were cashed upto 31.1.2014.
b) A wrong debit of Rs.800 has been given by the banker in the pass book
c) A cheque of Rs.200 was credited in pass book but was not recorded in the cash book
d) Cheques amounting to Rs.21,000 were deposited for collection; but cheques for Rs.7,400 have been credited in the pass book only
e) Interest and bank charges amounted Rs.100 were not accounted in cash book
f) A cheque of Rs.500 debited in cash book omitted to be banked.

Solution

Bank Reconciliation Statement of Govindan as on 31.1.2014

Particulars	**Amount Rs.**	**Amount Rs.**
Overdraft as per pass book		-41000
Add		
Wrong debit in pass book	800	
Uncredited cheques (21,000 – 7,400)	13,600	
Interest and bank charges	100	
Cheque omitted to be banked	500	15,000
		-26,000
Less		
Unpresentedcheque (15,600-11,000)	4,600	
Cheque deposited directly	200	-4,800
Overdraft balance as per cash book		**-30,800**

MODEL V

WHEN CASH BOOK AND PASS BOOK ARE GIVEN:

Items recorded in both the books are excluded. (Debit side of one book is compared with the credit side of the other book). An entry found in any one book is the reason for the difference in balance of both the books. These items are considered and the statement is prepared by following the I or III model.

Illustration: 10

From the following entries in the bank column of cash book and bank pass book, prepare Bank Reconciliation Statement.

Bank column of cash book

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
June 1	To balance	4,000	June 3	By cheque book	800
4	To Manohar	3,200	5	By drawings	1,000
8	To A	500	10	By F	2,200
18	To B	3,700	15	By G	1,300
21	To C	1,400	28	By salary	1,800
28	To D	100	29	By H	1,900
30	To E	450	30	By Rajan	1,700
			30	By commission	20
			30	By balance c/d	2,630
		13,350			**13,350**

Bank pass book

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
June 3	To cheque book	800	June 1	By balance	4000
5	To drawings	1000	6	By Manohar	3200
14	To F	2200	10	By A	500
20	To G	1300		By B	3700
20	To salary	1800	25	By dividend on	
	To commission	20		Securities	700
30	To collection				
	Charges	4			
	To electric				
	charge	80			
	To balance c/d	4896			
		12100			12100

Solution

Bank Reconciliation Statement as on ……..

Particulars	**Amount Rs.**	**Amount Rs.**
Balance as per cash book		2,630
Add		
Unpresentedcheque		
H	1900	
Direct payment in the bank by Rajan	1700	
Dividend on securities in pass book	700	4,300
		6,930

Less		
Uncredited cheque		
C	1400	
D	100	
E	450	
Debit in pass book: Collection charges	4	
Electric charges	80	2,034
Balance as per pass book		**4,896**

SUMMARY

Bank reconciliation statement is a statement prepared on a particular date to reconcile the balance as per cash book with the balance as per pass book and to know the exact balance with the bank. There are many reasons for the difference in two balances. The reasons are found out by preparing bank reconciliation statement.

THEORY QUESTIONS

1. What is bank reconciliation statement?
2. What are the causes of bank reconciliation statement?

EXERCISES

1) On 31.3.2015 the cash book of Kannan showed a bank balance of Rs.4,850. While verifying with the pass book, the following facts were noted:

1. Cheques sent in for collection before 31.3.2015 and not credited by the bank amounted to Rs.845
2. Cheques issued before 31.3.2015 but not presented for payment amounted to Rs.885
3. The banker has charged a sum of Rs.100 towards incidental charges and credited interest Rs.250
4. The banker has given a wrong credit for Rs.250
5. A customer has paid into bank directly a sum of Rs.300 on 28.3.2015 which has not been entered in the cash book
6. A cheque for Rs.200 sent for collection and returned unpaid has not been entered in the cash book. Prepare bank reconciliation statement.

2) From the following particulars, prepare bank reconciliation statement as on 31st December 2015 of Prabu who had cash at bank as per cash book Rs.10,500

1. Cheques for Rs.300, Rs.500 and Rs.200 were deposited on 30th and 31st December, but were not collected by 31st December 2015
2. Cheques issued for Rs.600, Rs.200, Rs.489 and Rs.50 were not encashed by 31st December 2015
3. The bank collected a bill for Rs.1,500 on 31st December 2007 but the information was received by Prabu on 1.1.2016

4. The bank allowed interest Rs.203 and charged a commission of Rs.92 on 31.12.2015

3) From the following particulars relating to business of Kasinath, prepare bank reconciliation statement.

1. Balance as per pass book (cr.) Rs.9,000
2. Cheques issued but not presented for payment Rs.15,000
3. Cheques deposited but not credited Rs.1,500
4. The credit side of the bank column of the cash book has been over added by Rs.500
5. Banker has given credit in the pass book for interest Rs.150
6. Banker has also given a wrong credit relating to some other account Rs.300

4) Prepare a bank reconciliation statement of Mr. Srinivasan

Cash book

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
2014			2014		
Feb. 1	To balance b/d	22,148	Feb. 3	By Mani	2,822
			15	By Giri	750
18	To Kumar	12,000	20	By Chidambaram	87
19	To sales - Raman	200	20	By purchases (Padma)	182
28	To Balu	8,345	26	By salary(Somu)	150
28	To Commission - Babu	80	26	By salary(Chandra)	8,820
			28	By Rangan	2,346
			28	By balance c/d	31,758
28	To Venkatesh	3,412			
		46,915			**46,915**
Mar.1	To balance b/d	31,758			

Pass book

Date	**Particulars**	**Dr. Withdrawals**	**Cr. Deposits**	**Dr./Cr. Balance**
2015				
Feb.1	By balance b/d			22,148
4	To Mani	2,822		19,326
16	To Giri	750		18,576
19	By Kumar		12,000	30,576
20	By Raman		200	
20	To Chidambaram	87		

20	To Padma	182		30,507
26	To somu	150		30,357
28	To Insurance premium	92		
	To B/P a/c	2,500		
	By Babu		810	
	By Muthu		1,200	
	By Interest		32	
	By Interest on investment		135	
	By B/R a/c		750	30,692(Cr.)

CHAPTER 7
BILLS OF EXCHANGE

INTRODUCTION

You have learnt that goods may be sold either on cash basis or credit basis. Most of the present day business transactions are carried on credit basis, which means that the payment for purchase is made within a fixed time after the date of the transaction. If the buyer is not in a position to pay, it creates problems to the seller. But, the bill of exchange serves as a document to arrange matters so that each party is satisfied. In this context, let us discuss the meaning and nature of bills of exchange, and the entries made in the books of account relating to the trade bills and accommodation bills.

OBJECTIVES

After studying this unit, you should be able to

- State the meaning of bills of exchange and its features
- Record transactions of bills of exchange
- Prepare the account of the parties to bills of exchange.

MEANING OF BILLS OF EXCHANGE

A bill of exchange is a common credit instrument. Section 5 of the Negotiable Instrument Act. 1881, defines a bill of exchange as “an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay as certain sum of a money only to, or to the order of certain person or to the bearer of the instrument”.

A bill of exchange is a written acknowledgement of the debt, written by the creditor and accepted by the debtor.

PARTIES TO A BILL OF EXCHANGE

There are usually three parties to a bills of exchange namely, drawer, acceptor or drawee and payee. Drawer himself may be the payee.

1) Drawer and Drawee

When the creditor draws a bill on the debtors, he becomes the drawer. The debtor on whose name the bill is drawn becomes the drawee. Drawer himself may be the payee.

2) Acceptor

The creditor, after having drawn the bill, sends the bill to the drawee (debtor) for acceptance. Once the drawee accepts the bill the drawer becomes the acceptor.

3) Payee

The person who is entitled to receive the money in his name is called “Payee”. Sometimes the drawer himself is the payee.

ESSENTIAL FEATURES OF BILL OF EXCHANGE

A bill of exchange possesses many of the characteristics similar to the promissory note. The essential features of a bill of exchange may be summarized as follows:

1) It must be in writing
2) It contains an express order to pay money only.
3) It must be unconditional
4) It must be signed by the drawer
5) The drawer, drawee and payee must be certain
6) The sum payable must be certain.
7) It should be properly stamped.

ADVANTAGES OF BILLS OF EXCHANGE

1) The instrument must be in writing
2) The order contained in the instrument must be unconditional. No condition should be attached to the order of the bill
3) It must be duly signed by the maker or drawer.
4) The order contained in the instrument must relate to the payment of certain sum of money which must be easily determinable.
5) The person on whom the order is direct must be a certain person whose name must be mentioned in the bill.
6) The instrument must be drawn in favour of a payee whose name must also be mentioned in the bill.
7) The sum of money must be payable either on demand or after a certain period.

TYPES OF BILLS

Bills can be classified as follows

1) Inland bill and foreign bills
2) Time and demand bills
3) Trade and accommodation bills

1) Inland bill and foreign bills

Inland bills are drawn on Indian residents are called “inland bills”. That is, a bill which is drawn in India.

- On a person residing in India whether payable in or outside India or
- On a person residing outside India but payable in India.

Inland bills may be endorsed in a foreign country, or may remain circulation in foreign countries.

Example

1. A bill is drawn by Mr. A in Madurai on a person in Coimbatore. it is payable in Chennai. This bill is an inland bill.
2. A bill is drab by Mr. A in Madurai on a person in Coimbatore. It is accepted for payment in Japan. The bill is an inland bill.

3. A bill is drawn by Mr. A on a person in Japan bills made payable in India. The bill is an inland bill.

Foreign bills

A foreign bill of exchange is the bill which is drawn in one country and made payable in another country, or drawn upon a person resident in some other country. Foreign bill include the following.

1. Bills drawn India on a person residing outside India and made payable outside India.
2. Bills drawn outside India and payable either in or outside India.
3. Bills drawn outside India on persons residing in India.
4. Bills drawn outside India and made payable outside India.

   Foreign bills are drawn in sets of two or three and each copy is numbered and has a reference to others.

2) Time and demand bills

Time bill

A bill payable after a fixed time is termed as a time bill - A bill payable after certain date is a time bill.

Demand bill

A bill payable at sight or on demand is termed as a demand bill.

3) Trade and accommodation bills

A bill drawn and accepted for a genuine trade transactions is termed as 'trade bill'

A bill drawn and accepted not for a genuine trade transaction but one to provide financial help to some party is termed as an accommodation bill. A bill which drawn, accepted or indorsed without any consideration is called an accommodation bill.

Example

Mr. X is need of money for three months. He approaches his friend Mr. Y to accept a bill of exchange drawn on him for three months. The bill is accepted – This bill is an accommodation bill.

Documentary and Clean bill

When a bill of exchange is not accompanied by any document, it is known as clean bill of exchange.

When a bill of exchange is accompanied by some documents, it is known as documentary bill. Documentary bill may be

i. Documents against acceptance (D/A)

ii. Documents against payment (D/P)

In the case of D/A bill, the documents attached to the bill are passed on to the importer after he gives the acceptance on the bill.

In the case of D/P bill, documents attached to the bill are delivered to the importer only if he makes the payment

D/P bill may be

a) Sight D/P bill or
b) Usance D/P bill

In case of sight D/P bill, payment is to be made within the period of 24 hours of the presentation of the bill. In case of usance bill it is to be paid within a particular period after it is drawn. It is drawn in one country and payable in another country. Length of the bill differs according to the custom in force in each county.

Calculation of due date

Generally, indendbills are drawn to pay the amount after a certain period of time from a particular date. But foreign bills are drawn in different ways to pay the amount as "asking", "by seeing", "after a concern date", or "after seeing".

As far as "asking", or "seeing" bills are concerned, the drawee has to pay the bill when the bill is submitted for payment. The due date of the bill which is written as "after a particular date", starts from the date of the bill. The due date of the bill which is written as "After seeing", after the bill is seen.

For the bills payable except the bill which is written as "by asking" or " by seeing" three days are to be added after the due date. These three days are known as grace days. The period of bills of exchange ends on the last day of grace day this is the day on which the amount is to be paid.

Assume that on 1.6.2003, a two month bill was drawn. Can you find out the due date? Mostly you will say that the due date is 1.8.2003. but the actual due date is 4.8.2003 which is calculated by adding three days which is known as grace days. In India it is legalized.

When the due date of a bill falls on a public holiday (26.1.2003 Republic Day), then the bill is due and payable on the preceding working day (25.1.2003).

If the due date of the bill falls on a day which is declared as emergency or unforeseen holiday, then the due date shall be the next following day. For example assume that 14.7.2003 is declared as emergency holiday. Then the due date of the bill falls on 15.7.2003.

TERMS USED IN BILLS TRANSACTIONS

1. The act of transferring a bill by a holder or drawer of the bill to another person is known as "endorsement of the bill".
2. The person who endorses the bill is called "endorser".
3. The person to whom the bill is endorsed is known as "endorsee".
4. Date on which a bill becomes payable is called "due date" or " Date of Maturity".
5. When a bill is paid on the due date, it is said to be "honoured".
6. Failure to pay the bill on the due date is "dishonor".

The method of authenticating the fact of dishonor of a bill by a notary public is called "Noting".

7. The fee payable to the notary public for evidencing the fact of dishonor of a bill is called "Noting Charges".
8. To pay the bill before the date is "Retiring".
9. When a bill is retired a small "Rebate" is allowed for the unexpired period of the bill.
10. It is "Renewal" when the acceptor approaches the drawer before the due date and requests him to cancel the original bill and draw on him a fresh bill for the amount sue plus interest.

ACCOUNTING TREATMENT

After knowing the meaning and nature of bills of exchange, let us study the accounting treatment of bill transactions.

Even though a bill of exchange may differ from a promissory note in certain aspects, both are treated alike for the purpose of accounting treatment. When bills and promissory notes are received, they are called as "Bills receivable" and when bills and promissory notes are accepted, they are called as "Bills Payable". The accounting aspects of a bill of exchange are discussed below:

1. He can retain the bill till the maturity date and present it for payment with acceptor, the bill may be collected through a bank form the acceptor.
2. In order to meet his financial need he can discount the bill before the date of maturity with his banker.The banker charges interest for the amount given known as discount. The discount amount is deducted from the value of the bill and the balance amount is paid to the drawer.
3. He can transfer his right upon the bill infavour of a creditor in payment of his amount. This method of transferring the bill in favour of a creditor is known as "endoresing the bill"

   In all the above cases, the bill may honoured or dishonoured by the acceptor. Let us see the journal entries to be passed in the books of the drawer and the acceptor.

Entries for bill transactions

	In the books of drawer	In the books of Acceptors
1.	**When a B/R is received** Debit B/R a/c, because it is an asset Credit the personal a/c of the party, because he gives the bill	**When B/P is given** a debit the personal a/c of the drawer, because he receives the bill Credit B/P a/c, since the bill goes out
2.	**When a B/R is duly honoured** Debit cash a/c, since it comes in	**When a B/P is duly honoured** Debit B/P a/c, since it comes in

	Credit B/R a/c, since it goes out	Credit Cash a/c, since it goes out
3.	**When a B/R is dishonoured** Debit the Acceptor's a/c since the amount is due from him. Credit B/R a/c, since it goes out	**When a B/P is dishonoured** Debit B/P a/c in order to cancel the original bill Credit the Drawer's a/c. Since we are Liable to pay the amount due to him
4.	**When a B/R s discounted** Debit cash a/c, since it comes in Debit Discount a/c, since it is a loss Credit B/R a/c, since it goes out	No entry is required
5.	**When a B/R is endorsed to a person** Debit the Receiver a/c Credit B/R a/c since it goes out	No entry is required
6.	**When discounted (or) endorsed bill is honoured** No entry	**When discounted or endorsed bill is honoured** Debit Bills payable a/c because it comes in Credit cash a/c because it goes out
7.	**When a discounted B/R is dishonoured** Debit the Acceptor's a/c since the amount is due from him. Credit Bank a/c, since we are liable to pay amount to the banker	**When a discounted B/P is dishonoured** Debit B/P a/c in order to cancel the original bill Credit the Drawer's a/c, since we are liable to pay the amount due to him
8.	**When an endorsed B/R isdishonoured** Debit the Accepter's a/c, since the amount is due from him. Credit endorsee's a/c, since we are liable to pay the amount to endorse	**When an endorsed B/P is dishonoured** Debit B/P a/c in order to cancel the original bill Credit the Drawer's a/c, since we are liable to pay the amount due to him
9.	**When a B/R is noted by the drawer** Debit the Accepter's a/c, since the amount is due from him. Credit endorsee's a/c, since we are liable to pay the amount to endorsee	**When a Bill is noted by the drawer** Debit B/P a/c with the value of the bill to cancel the original bill. Debit Noting charges a/c, since it is a loss to us Credit the Drawer's a/c, because we are liable to pay him
10.	**When a B/R is noted by the Banker** Debit the Acceptor's a/c	**When a B/P is noted by the Banker** Debit B/P a/c with the value of the

	since the amount (inclusive of nothing charges) is due from him. Credit the Bank a/c with noting charges	bill to cancel the original bill. Debit Noting charges a/c, since it is a loss to us Credit the Drawer's a/c, because we are liable to pay him
11.	**When a B/R is noted by the endorse** Debit the Acceptor's a/c since the amount is due from him (including noting charges) Credit the endorsee's a/c with nothing charges. Credit B/R a/c, Since it goes out	**When a B/P is noted by the endorse** Debit B/P a/c with the value of the bill to cancel the original bill. Debit Noting charges a/c, since it is a loss to us Credit the Drawer's a/c, because we are liable to pay him
12	**When a B/R is renewed** a) Debit the Acceptor's a/c since it denotes the amount due from him Credit the B/R a/c, for cancellation of the old bill b) Debit the Acceptor's for the interest receivable from him. Credit the interest receivable from him Credit the a/c since it is an income c) Debit B/R a/c with the amount of the new bill. Credit the Acceptor's a/c, since he gives the bill	**When a B/P is renewed** a) Debit B/P a/c for cancellation of the old bill Credit the drawer's a/c in order to show the amount which is payable to him b) Debit the interest a/c, since it is a loss Credit the Drawer's a/c, since it is payable to him. c) Debit the Drawer's a/c, since he is the receiver of the bill. Credit B/P a/c for the value of the new bill, since it goes out.
13	**When a B/R is retired** Debit Cash a/c, since cash comes in. Debit the rebate a/c, since it is a loss to us. Credit B/R a/c, since it goes out.	**When a B/P is retired** Debit the Drawer's a/c, since he is the receiver of the bill. Credit B/P a/c for the value of the new bill, since it goes out.
14.	**When a B/R is sent to Bank for collection** Debit bills for collection a/c Credit the B/R a/c **a) When it is actually collected** Debit Bank a/c Credit Bills for collection a/c **(or) b) When it is dishonoured** Debit the Drawee's a/c	**When a B/R is sent to Bank for collection** No entry Debit B/P a/c, since it comes in Credit Cash a/c, since it goes out Debit B/P a/c is order to cancel the original bill

	Credit Bill for Collection a/c	Credit the Drawer's a/c. Since we are liable to pay the amount due to him.

Now you know the entries for bills. Let us illustrate the above entries in the following examples.

Illustration: 1When bill is drawn, accepted and honoured

On 1st Jan.2015 'X' drew a two months bill on 'Y' for Rs. 500 and the latter accepted the same. On the due date 'Y' met the bill. Show the Journal Entries.

Solution:

In the books of 'X'

Date	Particulars	Debit Rs.	Credit Rs.
01.01.2015	Bills receivable a/c Dr. To 'Y' a/c (being the entry for the receipt of the bill)	500	 500
04.03.2015	Cash a/c Dr. To Bills receivable a/c (being the realization ofthe bill)	500	 500

In the books of 'Y'

Date	Particulars	Debit Rs.	Credit Rs.
01.01.2015	X's a/c Dr. To Bills payable a/c (being the acceptance given to X)	500	 500
04.03.2015	Bills payable a/c Dr. To cash a/c (being the entry for the honour of the bill)	500	 500

Illustration: 2 When bill is drawn, accepted and dishonoured

For goods supplied, 'A' draws a bill on 'B' for 4,000. 'B' accepted the sale and returns it to 'A'. On the due date 'B' refuses to honour the bill. Show journal entries.

Solution:

In the books of 'A'

Particulars		Debit Rs.	Credit Rs.
B's a/c	Dr.	4,000	
To sales a/c			4,000
(being the goods sold 'B' on credit)			
Bills receivable a/c	Dr.	4,000	
To B's a/c			4,000
(being the bill received from B)			
B's a/c	Dr.	4,000	
To Bills receivable a/c			4,000
(being B refuse to honour the bill)			

In the books of 'B'

Particulars		Debit Rs.	Credit Rs.
Purchase a/c	Dr.	4,000	
To A's a/c			4,000
(being the acceptance given to X)			
A's a/c	Dr.	4,000	
To Bills payable a/c			4,000
(being the acceptance given to A)			
Bills Payable a/c	Dr.	4,000	
To A's a/c			4,000
(being the payment not made)			

Illustration: 3When bill is dishonoured and the Noting Charges paid

'N' owes 'M' 100. 'M' draws a two months bill for Rs.100 on 'N' on 01.07.003 'N accept it and returns it to 'M'. On the due date 'N' fails to honour his acceptance and 'M' gets the bill noted by paying Rs. 5 as Noting charges. Show the journal entries.

Solution:

In the books of 'M'

Date	Particulars		Debit Rs.	Credit Rs.
01.07.2013	Bills receivable a/c	Dr.	100	
	To 'N' a/c			100
	(being the bill received)			
04.09.2013	N's a/c	Dr.	105	
	To Cash a/c			5
	To Bills receivable a/c			100
	(being the bill dishonoured and noting charges paid)			

In the books of 'N'

Date	Particulars		Debit Rs.	Credit Rs.
01.07.2013	M's a/c	Dr.	100	
	To Bills payable a/c			100
	(being the bill accepted)			
04.09.2013	Bills payable a/c	Dr.	5	
	Noting Charges a/c	Dr.	100	
	To M's a/c			105
	(being the bill dishonoured and noting charges paid by the drawer)			

Illustration: 4 When bill is discounted and honoured

Murali sold goods to Gopi on 5th February and draws a 3 months bill on Gopi for Rs. 5,000 Murali discounted the bill on 8th February at 10 percent per annum. At maturity the bill is honoured. Journalise the transactions in the books of both the parties.

Note:

Remember that the date of maturity of the bill is 8th May. The discount charge should be calculated for the period of 3 months, i.e., from 8th February to 8th May. Hence the discount is:

$5000 \times 10/100 \times 3/12 = \text{Rs. } 125$

Solution:

In the books of 'Murali'

Date	Particulars		Debit Rs.	Credit Rs.
Feb 5.	Gopi a/c	Dr.	5,000	
	To sales a/c			5,000
	(being credit sales)			
Feb. 5	Bills receivable a/c	Dr.	5,000	
	To Gopi a/c			5,000
	(being the acceptance received)			
Feb. 8	Bank a/c	Dr.	4,875	
	Discount a/c	Dr.	125	
	To Bills receivable			5,000
	(being the amount received on discounting the Bill)			
May 8	No entry			

In the books of 'Gopi'

Date	Particulars	Debit Rs.	Credit Rs.
Feb 5.	Purchase a/c Dr. To Murali a/c (being credit purchase)	5,000	5,000
Feb. 5	Murali a/c Dr. To Bills payable a/c (being the acceptance given)	5,000	5,000
Feb. 8	No entry		
May 8	Bills payable Dr. To cash (being the cash paid for our acceptance)	5,000	5,000

Illustration: 5 When bill is discounted and dishonoured

On January 6, 2014 Ram sold goods to Mohan for Rs. 9,000. On the same data Ram drew a four months bill on Mohan which was duly accepted. The bill was discounted on Jan. 9 at 10%. At maturity the bill was dishonoured and Ram had to pay the amount to the ban. Show journal entries

Discount $=9{,}000\times10/100\times4/12=300$

Solution:

Journal of Ram

Date	Particulars	Debit Rs.	Credit Rs.
2014 Jan. 6	Mohan a/c Dr. To sales a/c (being credit sales)	9,000	9,000
Jan. 6	Bills Receivable a/c Dr. To Mohan a/c (being the acceptance received)	9,000	9,000
Jan. 9	Bank a/c Dr. Discount a/c Dr. To Bills receivable a/c (being the amount received on discounting the bill)	8,700 300	9,000
May 9	Mohan Dr. To Bank a/c (being the amount paid on dishonor of Mohan's acceptance)	9,000	9,000

Journal of Mohan

Date	Particulars	Debit Rs.	Credit Rs.
2014 Jan. 6	Purchase a/c Dr. To Ram a/c (being credit purchase)	9,000	9,000
Jan. 6	Ram a/c Dr. To Bills Payable a/c (being the acceptance given)	9,000	9,000
Jan. 9	No entry		
May 9	Bills payable a/c Dr. To Ram a/c (being the credit given to Ram on dishonout of our acceptance of Jan.6)	9,000	9,000

Illustration: 6 Bill is endorsed and honoured

On 1st Jan., 2014, P sold goods to Q for Rs. 2,000 and drew a two month bill for the amount. P owed R a sum, of Rs. 2,000. P endorsed Q's acceptance to R. At maturity Q met his acceptance. Journalise the transaction in the books of P and Q.

Solution:

Journal of 'P'

Date	Particulars	Debit Rs.	Credit Rs.
2014 Jan. 1	Q a/c Dr. To Sales a/c (being credit sales)	2,000	2,000
”	Bills receivable Dr. To Q a/c (being the acceptance received)	2,000	2,000
March 4	R a/c Dr. To Bills Receivable a/c (being the transfer of Q's acceptance in favour of R)	2,000	2,000

Note: On maturity, P will not pass any entry because Q will the pay the amount to R.

Journal of 'Q'

Date	Particulars		Debit Rs.	Credit Rs.
2014				
Jan. 1	Purchase a/c	Dr.	2,000	
	To P a/c			2,000
	(being credit purchase)			
"	P a/c	Dr.	2,000	
	To Bills Payable a/c			2,000
	(being the acceptance received)			
March 4	Bills payable	Dr.	2,000	
	To Cash a/c			2,000
	(being the cash paid on maturity of our acceptance)			

Note: When P endorses the bill to R no entry is made by Q.

Illustration: 7 Bill is endorsed and dishonoured

X sold goods to Y on 3rd October 2014 for Rs. 4,000. X drew a three month bill on Y for the amount. X endorsed the bill in favour of Z. At maturity the bill was dishonoured. Journalise the transactions in the books of X and Y.

Solution:

Journal of 'X'

Date	Particulars		Debit Rs.	Credit Rs.
2014				
Oct. 3	Y a/c	Dr.	4,000	
	To Sales a/c			4,000
	(being credit sales)			
Oct. 3	Bills receivable a/c	Dr.	4,000	
	To Y a/c			4,000
	(being the acceptance received)			
Oct. 3	Z a/c	Dr.	4,000	
	To Bills Receivable a/c			4,000
	(being the transfer of Y's acceptance in favour of Z)			
2015				
Jan. 6	Y a/c	Dr.	4,000	
	To Z a/c			4,000
	(being the credit to Z on dishonor of Y's acceptance)			

Journal of 'Z'

Date	Particulars		Debit Rs.	Credit Rs.
2014 Oct. 3	Purchase a/c	Dr.	4,000	
	To P a/c			4,000
	(being credit purchases)			
Oct. 3	X a/c	Dr.	4,000	
	To Bills Payable a/c			4,000
	(being the acceptance received)			
2015 Jan. 6	Bills payable a/c	Dr.	4,000	
	To X a/c			4,000
	(being dishonour of our acceptance dated Oct. 3)			

Illustration: 8 On retiring the bill

On 1st June.2014, 'A' drew a bill for Rs. 300 on 'B', payable after 3 months. Before the due date 'B' retired the bill for which a rebate of Rs. 5 was given. Show necessary journal entries.

Solution:

In the books of 'A'

Date	Particulars		Debit Rs.	Credit Rs.
01.06.2014	Bills receivable a/c	Dr.	300	
	To 'B' a/c			300
	(being the entry for the receipt of the bill)			
”	Cash a/c	Dr.	295	
	Rebate a/c	Dr.	5	
	To Bills receivable a/c			300
	(being the entry for the realization of the bill before the due date)			

In the books of 'B'

Date	Particulars		Debit Rs.	Credit Rs.
01.06.2014	A's a/c	Dr.	300	
	To Bills payable a/c			300
	(being the acceptance given to A)			
”	Bills payable a/c	Dr.	300	
	To cash a/c			295
	To rebate a/c			5

	(being the entry for the retirement of the bill)		

Illustration: 9 Renewal of the Bill

Before due date of the bill for Rs. 500, B, the acceptor, approaches A, the drawer, and pays Rs. 500 in cash and requests A to draw another bill for Rs. 315. Show the journal entries.

Solution:

Journal of 'A'

	Particulars	Debit Rs.	Credit Rs.
a)	B's a/c Dr. To B/R a/c (being cancellation of the original bill)	500	 500
b)	B's a/c Dr. To interest a/c (being the interest due)	15	 15
c)	B's a/c Dr. B/R a/c Dr. To B a/c (being cash and 2nd bill received)	200 315	 515

Journal of 'B'

	Particulars	Debit Rs.	Credit Rs.
a)	Bills payable a/c Dr. To A a/c (being the cancellation of the bill)	500	 500
b)	Interest a/c Dr. To A a/c (being the interest due)	15	 15
c)	A's a/c Dr. To cash a/c To bills payable a/c (being cash and new acceptance given)	515	 200 315

Insolvency of acceptor

Insolvency of a person means that he is unable to pay his liabilities. When the acceptor of a bill of exchange or marker of a promissory note becomes bankrupt or insolvent and unable to pay the amount of the bill on due date, the instrument should be treated as dishonoured and necessary entries have to be passed in this regard in the books of the parties concerned. It is also usual to find that a partial payment which is expressed as so many paise in the Rupee, e.g., 5 paise in the Rupee, in full satisfaction of the claims of the creditors. To determine how much is received in cash, it becomes necessary to prepare the insolvent's personal account. After posting the entry for the amount received from the insolvent's estate, the balance still owing by him which represents irrecoverable debt has to be written off as bad debt. By writing off the balance as bad debt the insolvent's account is closed.

Illustration 10

Rahul purchased goods from Gokul for Rs. 4,000 on 1st March, 2014, on the same day he gave a promissory note for the amount payable after two months. On 4th March, this was discounted by Gokul with his bankers at the rate of 6% per annum. The promissory note was dishonoured on the due date and that the bankers have incurred noting charges of Rs. 20. When approached by Rahul, Gokul agreed to receive a sum of Rs. 1,060 in cash and two promissory notes – one at two months for Rs. 1,000 and the other at 3 months for Rs. 2,000 in full settlement from him. The first promissory note which has been endorsed to Trisul was duly honoured at maturity. The second note was dishonoured due to Rahul's insolvency. Gokul could recover only 40 paise in the Rupee as first and final dividend from the estate of Rahul. Show journal entries and ledger accounts in the books of Gokul and Rahul.

Solution:

Journal of Gokul (Drawer)

Date	Particulars		Debit Rs.	Credit Rs.
2014				
March 1	Rahul a/c	Dr.	4,000	
	To Sales a/c			4,000
	(being the sale of goods on credit to Rahul)			
March 1	Bills Receivable a/c	Dr.	4,000	
	To Rahul			4,000
	(being Receipt of promissory note from Rahul)			
March 4	Bank a/c	Dr.	3,960	
	Discount a/c	Dr.	40	
	To Bills receivable a/c			4,000
	(being Amount received on discounting the bill)			
May 4	Rahul a/c	Dr.	4,020	
	To Bank a/c			4,020
	(being the bill is dishonoured and noting charges paid by the Bankers)			

May 4	Rahul a/c Dr. To interest a/c (being Amount of interest receivable from Rahul)	40	40
May 4	Cash a/c Dr. Bills receivable a/c Dr. To Rahul a/c (being Receipt of cash and two promissory notes one at two months for Rs. 1,000 and the other at 3 months for Rs. 2,000 from Rahul)	1,060 3,000	4,060
May 4	Trishul a/c Dr. To Bills Receivable a/c (being the bill endorsed to Trishul)	1,000	1,000
July 7	No entry		
Aug. 7	Rahul a/c Dr. To Bills Receivable a/c (being the bill dishonoured this day)	2,000	2,000
Aug. 7	Cash a/c Dr. Bad debts a/c Dr. To Rahul a/c (being receipt of first and final dividendof 40 paise in the Rupee from the estateof Rahul)	800 1,200	2,000

Journal of Rahul (Acceptor)

Date	Particulars	Debit Rs.	Credit Rs.
2014 March 1	Purchase a/c Dr. To Gokul a/c (The purchase of goods from Gokul)	4,000	4,000
March 1	Gokul a/c Dr. To Bills payable a/c (Our promissory note given to Gokul)	4,000	4,000
May 4	No entry		
May 4	Bills payable a/c Dr. Noting Charges a/c Dr. To Gokul a/c	4,000 200	4,200

	(The bill dishonoured this day)		
May 4	Gokul a/c Dr. To Cash a/c To Bills Payable a/c (payment of cash and issue of two promissory notes – one at two months for Rs. 1,000 and the other at 3 months for Rs. 2,000 to Gokul)	4,060	 1,060 3,000
May 4	No entry		
July 7	Bills payable a/c Dr. To Cash a/c (The bill met at maturity)	1,000	 1,000
Aug. 7	Bills Payable a/c Dr. To Gokul a/c (the bill dishonoured this day)	2,000	 2,000
Aug. 7	Gokul a/c Dr. To Cash a/c To Deficiency a/c (Payment of 40 paise in the Tupee as first and final dividend to Gokul)	2,000	 800 1,200

Ledger in the boos of Gokul

Rahul a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014			2014		
Mar. 1	To sales a/c	4,000	Mar 1	By bills receivable a/c	4,000
May 4	To bank a/c	4,000	May 4	By cash a/c	1,060
May 4	To interest a/c	40	May 4	By bills receivable a/c	3,000
Aug. 7	To bills receivable a/c	2,000	Aug. 7	By cash a/c	800
			Aug. 7	By bad debts a/c	1,200
		10,060			**10,060**

In the books of Rahul

Gokul a/c

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2014			2014		
Mar. 1	To bills payable a/c	4,000	Mar 1	By purchase a/c	4,000
May 4	To cash a/c	1,060	May 4	By bills payable a/c	4,000
May 4	To bills payable a/c	3,000	May 4	By noting charges	20
Aug. 7	To cash a/c	800	Aug. 7	By interest	40
Aug. 7	To deficiency a/c	1,200	Aug. 7	By bills payable	2000
		10,060			**10,060**

Illustration: 11

Ashok purchased goods from Badri for Rs. 1000 on March 1, 2014 and accepted a bill of exchange for two months drawn on him by Badri on same date for the amount. Badri got the bill discounted at his bank at 6 percent. At maturity the bill was dishonoured, and the noting charges paid amounted to Rs. 10. Badri agreed to receive from Ashok a sum of Rs. 225 in cash and a promissory note for Rs. 800 (in full settlement) at 3 months. On the due date, Ashok met the note. Pass the necessary Journal entries in the books of both and parties.

Solution:

In the books of Ashok

Date	Particulars	Debit Rs.	Credit Rs.
1.3.2014	Purchase a/c Dr. To Badri a/c (being goods purchased on credit)	1,000	 1,000
	Badri a/c Dr. To B/P a/c (being bill accepted)	1,000	 1,000
	No entry		
4.5.2014	B/P a/c Dr. To Badri a/c (being the bill dishonoured)	1,000	 1,000
	Noting charges a/c Dr. To Badri a/c (being noting charges payable)	10	 10
	Interest a/c Dr. To Badri a/c	15	 15

	(being interest payable)		
	Badri a/c Dr. To Cash a/c (being cash paid)	225	225
7.8.2014	Badri a/c Dr. To B/P a/c (being a bill accepted)	800	800
	Bardi a/c Dr. To Bank a/c (being the bill met)	800	800

In the books of Badri

Date	Particulars	Debit Rs.	Credit Rs.
1.3.2014	Ashok a/c Dr. To Sales a/c (being goods sold)	1,000	1,000
	Bills Receivable a/c Dr. To Ashok a/c (being 2 months bills received)	1,000	1,000
	Bank a/c Dr. Discount a/c Dr. To B/R a/c (being bills discounted)	990 10	 1,000
4.5.2014	Ashok a/c Dr. To Bank a/c (being the bill dishonoured)	1,000	1,000
	Ashok a/c Dr. To Bank a/c (being noting charges paid)	10	10
	Badri a/c Dr. To interest a/c (being interest receivable)	15	15
	Cash a/c Dr. To Ashok a/c (being cash received)	225	225
7.8.2014	Bills Receivable a/c Dr. To Ashok a/c (being 3 months bills received)	800	800
	Bank a/c Dr. To Ashok a/c (being the second bill honoured)	800	800

Note:

1) Discount= 1,000 × 6/100 × 2/12= Rs.10
2) Calculation of Interest

The amount paid by Asho = 225+800=1,025

First Bill of Exchange +Noting Charges (1,000+10)=1,010

The remaining amount Rs. 15 as the interest.

Illustration: 12

On October 1, 2015, Balan sold goods of the value of Rs. 5,000 to Raman. In turn, he has taken two Bills of Exchange – one for Rs.2 ,500 at 3 months. Balan discounted the first bill with the Central Bank, for Rs. 2,470. On maturity of the first bill, Raman dishonoured the bill, the noting charges being Rs. 25. Raman paid on that day Rs. 1,000 to Balan and requested him to retire the second bill also and agreed to give a fresh 3 months bill for the total balance amount due together with the charges incurred by Balan and an interest of Rs. 50. On the due date, this bill was duly honoured. Pass Journal entries in the books of Balan to record the above transactions.

Solution

In the books of Balan

Date	Particulars		Debit Rs.	Credit Rs.
1.10.2015	Raman a/c	Dr.	5,000	
	To Sales a/c			5,000
	(being goods sold)			
	Bills Receivable a/c	Dr.	2,500	
	To Raman			2,500
	(being a bill received)			
	Bills Receivable a/c	Dr.	2,500	
	To Raman			2,500
	(being a bill received)			
	Bank a/c	Dr.	2,470	
	Discount a/c	Dr.	30	
	To B/.R			2,500
	(being Bill discounted with bank)			
4.12. 2015	Raman a/c	Dr.	2,500	
	To bank a/c			2,500
	(being first bill dishonoured)			
	Raman a/c	Dr.	25	
	To bank a/c			25
	(being noting charges paid)			
4.12. 2015	Raman a/c	Dr.	2,500	
	To B/R a/c			2,500
	(being second bill dishonoured)			

	Raman a/c Dr. To interest a/c (being interest receivable)	50	 50
	Cash a/c Dr. B/R a/c Dr. To Raman a/c (being cash received and for the balance a third bill received)	1,000 4,075	 5,075
7.3. 2015	Cash a/c Dr. To Raman a/c (being third bill honoured)	4,075	 4,075

(Note: Third bill of exchange=2,500+2,500+25+50-1,000=4,075)

Illustration 13

Journalise the following transactions in boos of R. Krishana

a) R. Krishan's acceptance to B Balan for Rs. 2,000, discharged by a cash payment of Rs. 1,000 and an acceptance of new bill for the balance plus Rs. 10 for interest.
b) G. Gopal's acceptance for Rs. 4,000 which was endorsed over by R. Krishna to M. Mohan was dishonoured. M. Mohan paid Rs. 20 noting charges.
c) D. Devaraj retires a bill for Rs. 2,000 drawn on him by R. Krishna for Rs. 10 discount.
d) R. Krishna's acceptance to P. Palani for Rs. 5,000 discharged by M. Mody's acceptance for a similar amount to R. Krishan.
e) R. Krishna's acceptance to S. Somu for Rs. 4,000 was discharged by a cash payment of Rs. 2,020 which included Rs. 20 for interest; a new bill was accepted for the balance.

Solution:

In the boos of Krishna

Date	Particulars	Debit Rs.	Credit Rs.
a)	Bills payable a/c Dr. To B. Balan's a/c (being the bill cancelled)	2,000	 2,000
	B. Balan's a/c Dr. To cash a/c (being the amount paid)	1,000	 1,000
	Interest a/c Dr. To B. Balan's a/c (being the interest	10	 10

	payable to B. Balan)		
	B. Balan's a/c Dr. To Bills payable a/c (being the New bill accepted)	1,010	 1,010
b)	G. Gopal a/c Dr. To M. Mohan's a/c (being the entry to record the amount due from G. Gopal payable to M. Mohan due to dishonour)	4,020	 4,020
c)	Cash a/c Dr. Rebate a/c Dr. To Bills receivable a/c (being the bill retried)	1,990 10	 2,000
d)	Bills Payable a/c Dr. To Bills Receivable a/c (being our acceptance discharged)	5,000	 5,000
e)	Bills Payable a/c Dr. To S. Somu a/c (being the bill cancelled)	4,000	 4,000
	Interest a/c Dr. To S. Somu a/c (being the interest payable to S. Somu)	20	 20
	S. Somu's a/c Dr. To Cash a/c (being the cash paid)	2,020	 2,020
	S. Somu's a/c Dr. To Bills Payable a/c (being a new bill accepted)	2,000	 2,000

Accommodation Bills – Meaning and Definition

You have learn that in actual practice the bills are normally drawn and accepted in connection with genuine trade transactions.

Apart from that to meet a temporary financial need, bills can also be used. For instance, 'X' is in need of money and approaches his friend 'Y' who, instead of lending the money directly, proposed to draw an 'Accommodation bill' in his favour. This device enables 'X' to get an advance from bank or at the commercial rate of discount. Thus, there is no business transaction to support the accommodation bill. Thus a bill which is drawn and accepted without any consideration but with the aim of raising money for benefit of one or both parties involved in a bill is known as an **"Accommodation bill".** It is also defined as an instrument in writing containing an unconditional order, signed by the maker without any consideration but simply with an aim to accommodate the acceptor and drawer. Such a bill is also called **"Kite"** or **"Finance Bill"**

Usually, the bill is discounted with the banker and the proceeds are used either by one both in some agreed proportions. The discount charged by the banker is borne by the party or parties receiving the proceeds of the bill. Before the due date of the bill, the drawer sends the amount to the acceptor who pays it to the bank.

METHODS OF DRAWING ACCOMMODATION BILLS

There are three methods of drawing accommodation bills:

1) A who is in need of money draws a bill on B for his own accommodation.
2) P and Q who are in need of finance share the proceeds of a bill drawn by P and Q
3) X and Y draw bills on each other for mutual accommodation.

Let us illustrate the above methods with the following example

Illustration: 14 One who is in need of money draws on another for his own accommodation

On 2nd February, 2014 A draws a bill on B for 6,000 payable after 3 months. A discounts the bill on 5th February and pays Rs. 150 as discount charges. On 2nd May A hands over Rs. 6,000 to enable B to meet his acceptance. On 5th May B meets the bill. Journalise the transactions in the books of both the parties.

Solution:

Journal of 'A'

Date	Particulars		Debit Rs.	Credit Rs.
2014				
Feb. 2	Bills receivable a/c	Dr.	6,000	
	To B a/c			6,000
	(being the acceptance received)			
Feb. 5	Bank a/c	Dr.	5850	
	Discount a/c	Dr.	150	
	To Bills receivable a/c			6,000
	(being cash received)			
May 2	B's a/c	Dr.	6,000	
	To Cash a/c			6,000
	(being cash sent to B to enable him to meet his acceptance)			
May 5	No entry			

Journal of 'B'

Date	Particulars		Debit Rs.	Credit Rs.
2014				
Feb. 2	'A's a/c	Dr.	6,000	
	To Bills payable a/c			6,000
	(being the acceptance given)			
Feb. 5	No entry			
May 2	Cash a/c	Dr.	6,000	
	To A's a/c			6,000
	(being cash received)			
May 5	B/P a/c	Dr.	6,000	
	To Cash a/c			6,000
	(being cash paid for acceptance)			

Illustration: 15 One draws a bill on another and both share the proceeds.

On 2nd February 2014 P draws a Bill on Q for Rs. 6,000 payable after 3 months. The bill is discounted on 5th February at 10 percent per annum. On the same day he remits half the proceeds of the Bill to Q. On 2nd May 2014 P remits Rs. 3,000 to enable Q to meet his acceptance on 5th May. Q meets the bill on 5tth May. Show journal entries.,

Solution:

Journal of 'P'

Date	Particulars		Debit Rs.	Credit Rs.
2014				
Feb. 2	Bills receivable a/c	Dr.	6,000	
	To Q a/c			6,000
	(being the acceptance received)			
Feb. 5	Bank a/c	Dr.	5850	
	Discount a/c	Dr.	150	
	To Bills receivable a/c			6,000
	(being cash received on discounting)			
Feb. 5	Q's a/c	Dr.	3,000	
	To Bank a/c			2,925
	To Discount a/c			75
	(being the remittance of half the proceeds and half the discount to be borne by Q)			
May 2	Q's a/c	Dr.	3,000	
	To Bank a/c			3,000

	(being the remittance of balance due)		
May 5	No entry		

Journal of 'Q'

Date	Particulars	Debit Rs.	Credit Rs.
2014 Feb. 2	'P's a/c Dr. To Bills payable a/c (being the acceptance given)	6,000	6,000
Feb. 5	No entry		
Feb. 5	Bank/Cash a/c Dr. Discount a/c Dr. To P's a/c (being receipt of half the proceeds)	2,925 75	3,000
May 2	Bank / Cash a/c To P a/c (being cash received to meet of our acceptance)	3,000	3,000
May 5	Bills payable a/c To Bank / Cash a/c (being cash paid on maturity of out acceptance)	6,000	6,000

Illustration: 16 Each draw a bill on another for mutual accommodation

For mutual accommodation of X and Y, the former draws on Y a bill for Rs. 6,000 for three months on Feb. 2, 2014. Y accepted the same, X discounts it with his bank on Feb. 5 at 10 percent per annum. Y draws a bill on X for Rs. 6,000 on Feb. 2, 2014, payable after three months. Y discounts the bill on Feb. 5 at 10 percent per annum. At maturity both X and Y honoured their acceptances. Journalise the above transactions in the books of X and Y.

Solution:

Journal of 'X'

Date	Particulars	Debit Rs.	Credit Rs.
2014 Feb. 2	Bills receivable a/c Dr. To Y's a/c (being acceptance received)	6,000	6,000

Feb. 2	Y's a/c Dr. To Bills Payable a/c (being acceptance given)	6,000	6,000
Feb. 5	Bank a/c Dr. Discount a/c Dr. To Bills receivable a/c (being cash received on discounting Y's acceptance)	5,850 150	6,000
May 5	Bills payable a/c To Cash a/c (being cash paid for our acceptance dated Feb. 5)	6,000	6,000

Journal of 'Y'

Date	Particulars	Debit Rs.	Credit Rs.
2014 Feb. 2	X's a/c Dr. To Bills payable a/c (being acceptance given)	6,000	6,000
Feb. 2	Bills Receivable a/c Dr. To X a/c (being acceptance received)	6,000	6,000
Feb. 5	Bank a/c Dr. Discount a/c Dr. To Bills receivable a/c (being receipt of half the proceeds)	5,850 150	6,000
May 5	Bills payable a/c To Cash a/c (being cash paid for our acceptance dated Feb. 2)	6,000	6,000

Illustration 17

X draws a bill for Rs. 1,500 and Y accepts the same for the mutual accommodation of both of them to the extent of X 2/3 Y, 1/3. X discounts the same for Rs. 1,410 and remits 1/3rd of the proceeds to Y. Before the due date, Y draws another bill for 2,100 on X in order to provide funds to meet the first bill. The second bill is discounted for Rs. 2,040 with the help of which first bill is met and Rs. 360 are remitted to X. Before the due date of the second bill, X becomes bankrupt and Y receives a dividend of 50 paise in the rupee in full satisfaction. Pass necessary entries in the books of X and Y.

Solution:

Journal of 'X'

Particulars		Debit Rs.	Credit Rs.
Bills receivable a/c	Dr.	1,500	
To Y a/c			1,500
(being the acceptance received from Y)			
Bank a/c	Dr.	1,410	
Discount a/c	Dr.	90	
To bills receivable a/c			1,500
(being the bill discounted)			
Y a/c	Dr.	500	
To Bank a/c			470
To Discount a/c			30
(being1/3rd of the proceeds remitted to Y and charged the proportionate discount)			
Y a/c	Dr.	2,100	
To Bills payable a/c			2,100
(being the bill accepted drawn by Y)			
Bank a/c		360	
Discount a/c	Dr.	40	
To Y a/c			400
(being the Amount received from Y and the discount charged by him)			
Bills payable a/c	Dr.	2,100	
To Y a/c			2,100
(being the bill dishonoured)			
Y a/c	Dr.		
To Bank a/c		1,400	700
To Deficiency a/c			700
(being the amount due to Y discharged at 50 paise in a rupee)			

Y Account

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To Bank a/c	470	Mar 1	By Bills receivable a/c	1,500
	To Discount a/c	30	May 4		
	To bills payable a/c	2,100	May 4	By Bank a/c	360
	To Balance c/d a/c	1,400	Aug. 7	By discount a/c	40
				By Bills payable a/c	2,100
		4,000			**4,000**

	To Bank a/c To deficiency a/c	700 700	Aug. 7	By balance b/d	1,400
		1,400			**1,400**

Journal of Y

Particulars		Debit Rs.	Credit Rs.
X a /c	Dr.	1,500	
To Bills payable a/c			1,500
(being the bills accepted)			
Bank a/c	Dr.	470	
Discount a/c	Dr.	30	
To X a/c			500
(being the amount received from and the discount charged for the same)			
Bills receivable a/c	Dr.	2,100	
To X a/c			2,100
(being the acceptance received from X)			
Bank a/c	Dr.	2,040	
Discount a/c	Dr.	60	
To Bills receivable a/c			2,100
(being the bill discounted)			
Bills payable a/c	Dr.	1,500	
To bank a/c			1,500
(being the acceptance honoured)			
X a/c	Dr.	400	
To Bank a/c			360
To discount a/c			40
(being the amount remitted and the discount debited to X)			
X a/c	Dr.	2,100	
To Bank a/c			2,100
(being the amount paid to bank on dishonor by X)			
Bank a/c	Dr.	700	
Bad debts a/c	Dr.	700	
To X a/c			1,400
(being the amount received in final settlement)			

‘X’ Account

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To bills payable a/c	1,500	Mar 1	By Bank a/c	470
	To Bank a/c	360	May 4	By discount a/c	30
	To Discount a/c	40	May 4	By Bills receivable a/c	2,100
	To Bank a/c	2,100			
			Aug. 7	By balance b/d	1,400
		4,000			**4,000**
	To Balance c/d a/c	1,400	Aug. 7	By bank	700
				By bad debts	700
		1,400			**1,400**

Illustration: 18

C for the mutual accommodation of himself and V draws upon the later a bill at 3 months date for Rs. 800 dated January 1. The bill is discounted by C at 10 percent and half the proceeds are remitted to V.

V at the same time draws a bill at 3 months on C for Rs. 400. After securing C’s acceptance the bill is discounted at 1 percent by V, who remits half the proceeds to C. C becomes insolvent on March 31 and 5 paise in the rupee is received on May 15 first and final dividend from his estate.

Write Journal entries in the Books of Both the parties.

Solution:

In the books of “X”

Date	Particulars		Debit Rs.	Credit Rs.
Jan. 1	Bills receivable a/c	Dr.	800	
	To V a/c			800
	(being 3 months bills received)			
	Bank a/c	Dr.	780	
	Discount a/c	Dr.	20	
	To Bank a/c			800
	(being the bill discounted)			
	V a/c	Dr.	400	
	To Cash a/c			390
	To Discount a/c			10
	(being half proceeds sent to V)			
	V a/c	Dr.	400	
	To Bills payable a/c			400
	(being a 3 months bill accepted)			
	Discounting the bill by V			

	No entry		
	Cash a/c Dr. Discount a/c Dr. To V a/c (being half the proceeds of second bill received)	194 6	 200
April 4	Bills payable a/c Dr. To cash a/c (being the second bill honoured)	400	 400
May 15	Cash a/c Dr. Bad debts a/c Dr. To V a/c (being first and final claim received)	150 450	 600

In the books of "Y"

Date	Particulars	Debit Rs.	Credit Rs.
Jan. 1	C a/c Dr. To Bills payable a/c (being a 3 months bills accepted)	800	 800
	Nil		
	Cash a/c Dr. Discount a/c Dr. To C a/c (being half proceeds received)	390 10	 400
	Bills receivable a/c Dr. To C a/c (being a 3 months bill received)	400	 400
	Bank a/c Dr. Discount a/c Dr. To B/R a/c (being the bill discounted)	388 12	 400
	C a/c Dr. To Cash a/c To Discount a/c (being half the proceeds of the second bill remitted)	200	 194 6
April 4	Bills payable a/c Dr. To C a/c (being the first bill dishonoured)	800	 800

May 15	C a/c Dr. To Cash a/c To Deficiency a/c (being first and final claim paid)	600	 150 450

Note: V to be paid Rs. 400+200=600
25% of Rs. 600= Rs. 150

Illustration: 19

P draws a bill for Rs. 10,000 and R accepts the same for mutual accommodation equally. P discount the same for Rs. 9,990 an remits half to R. Before due date R draws a bill on P for Rs. 20,000 and discounts the same for Rs. 19,800. He honours the first bill and remits Rs. 4,900 to P. Before the due date of the 2nd bill P becomes bankrupt and R receives a final dividend of Rs. 0.50 per rupee. Pass Journal entries in the books of P and R.

Solution:

In the books of "P"

Date	Particulars	Debit Rs.	Credit Rs.
	Bills receivable a/c Dr. To R a/c (being the bill drawn)	10,000	 10,000
	Cash a/c Dr. Discount a/c Dr. To Bill Receivable a/c (being the bill discounted)	9,000 1,000	 10,000
	R a/c Dr. To Cash a/c To Discount a/c (being half of the proceeds sent to R)	5,000	 4,950 50
	R a/c Dr. To Bills payable a/c (being the second bill accepted)	20,000	 20,000
	No entry		
	No entry		
	Cash a/c Dr. Discount a/c Dr. To R a/c (being half of the proceed received	4,900 100	 5,000

	from R)		
	Bills Receivable a/c Dr. To R a/c (being the second bill dishonoured)	20,000	 20,000
	R a/c Dr. To cash a/c To deficiency (P becomes insolvent and 0.50 paise per rupee is received)	10,000	 5,000 5,000

In the books of "R"

Date	Particulars	Debit Rs.	Credit Rs.
	P a/c Dr. To Bills payable a/c (being the bill accepted)	10,000	 10,000
	No Entry		
	Cash a/c Dr. Discount a/c Dr. To Bill Receivable (being the second bill discounted)	4,950 50	 5,000
	Bills receivable a/c Dr. To P a/c (being the second bill is drawn)	20,000	 20,000
	Cash a/c Dr. Discount a/c Dr. To Bills Receivable a/c (being the bill discounted)	19,800 200	 20,000
	Bills payable a/c Dr. To Cash a/c (being the first bill honoured)	10,000	 10,000
	P a/c Dr. To Cash a/c To discount a/c (being the half of the proceed sent to R)	5,000	 4,900 100
	P a/c Dr. To bank a/c being first and second bill dishonoured)	20,000	 20,000
	Cash a/c Dr. Bad debts a/c Dr. To P a/c	5,000 5,000	 10,000

	(being 0.50 paise per rupee is sent in full settlement)		

'P' Account

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To bills payable	10,000		By Cash	4,950
	To Cash	4,900		By Discount	50
	To Discount	100		By Bills receivable	20,000
	To Bank	20,000		By Cash	5,000
				By Bad debts	5,000
		35,000			**35,000**

Illustration 20

For the mutual accommodation of Anbu and Velan on 6.2.2015, Anbu drew a three months bill of exchange on Velan for Rs. 3,000 and got it discounted with a bank for Rs. 2,900. On the same date, Velan drew a three months bill on Anbu for Rs. 4,000 and got it discounted with a bank for Rs. 3,880. They shared the proceeds equally. On the due date, Anbuhonoured his acceptance, but due to insolvency of Velan his bill was dishonoured. A dividend on forty paise per rupee was received from the eastates of Velan.

Pass Journal entries in the book of Velan.

Solution:

In the books of Velan

Date	Particulars		Debit Rs.	Credit Rs.
06.02.2015	Anbu a/c	Dr.	3,000	
	To Bill Payable a/c			3,000
	(being the bill accepted)			
06.02.2015	Bills Receivable a/c	Dr.	4,000	
	To Anbu a/c			4,000
	(being a bill drawn)			
06.02.2015	Cash a/c	Dr.	3,880	
	Discount a/c	Dr.	120	
	To Bill Receivable a/c			4,000
	(being the Bill is discounted with the bankers)			
06.02.2015	Anbu a/c	Dr.	2,000	
	To Cash a/c			1,940
	To Discount a/c			60
	(being half of the proceeds sent)			
06.02.2015	Cash a/c	Dr.	1,450	

	Discount a/c Dr. To Anbu a/c (being half of the proceeds of our acceptance received)	50	 1,500
09.05.2015	Bill payable a/c Dr. To bank a/c (being our acceptance dishonoured)	3,000	 3,000
06.02.2015	Anbu a/c Dr. To cash a/c To Deficiency a/c (being Velan's insolvency, 40 paise in a rupee is received)	3,500	 1,400 2,100

Illustration: 21

B draws a three months bill on S for Rs. 4,000 on 1st April 2015. S accepts the immediately remits Rs. 985 to S. On the due date B being unable to remit the amount due accepts a bill for Rs. 4,500 for three months which is discounted by S for Rs. 4,440. S sends Rs. 330 to B. before the maturity of the bill, B becomes insolvent, his estate paying 40 paise in the rupee.

Give entries in the books of B and S.

Solution:

In the books of "B"

Date	Particulars	Debit Rs.	Credit Rs.
	Bills receivable a/c Dr. To S a/c (being the bill drawn)	4,000	 4,000
	Cash a/c Dr. Discount a/c Dr. To Bill Receivable a/c (being the bill discounted)	3,940 60	 4,000
	S a/c Dr. To Cash a/c To Discount a/c (being 1/4 of the proceeds is sent)	1,000	 9 85 15
	S a/c Dr. To Bills payable a/c (being the bill accepted)	4,500	 4,500
	No entry		
	No entry		

	Cash a/c Dr. Discount a/c Dr. To S a/c (being 3/4 of the proceeds received)	4,900 100	 5,000
	Bills payable a/c Dr. To S a/c (being the second bill dishonoured)	4,500	 4,500
	S a/c Dr. To cash a/c To deficiency a/c (being 0.40 paise in a rupee is paid due to insolvency)	3,375	 1,350 2,025

In the books of "S"

Date	Particulars	Debit Rs.	Credit Rs.
	B a/c Dr. To Bills payable a/c (being the bill accepted)	4,000	 4,000
	No Entry		
	Cash a/c Dr. Discount a/c Dr. To P a/c (being ¼ of the proceeds is received)	985 15	 1,000
	Bills receivable a/c Dr. To B a/c (being the bill drawn)	4,500	 4,500
	Cash a/c Dr. Discount a/c Dr. To Bills Receivable a/c (being the bill discounted)	4,440 60	 4,500
	Bills payable a/c Dr. To Cash a/c (being the first bill honoured)	4,000	 4,000
	B a/c Dr. To Cash a/c To discount a/c (being 3/4 of the proceeds sent)	375	 330 45
	B a/c Dr.	4,500	

	To bank a/c (being the second bill dishonoured)		4,500
	Cash a/c Dr. Bad debts a/c Dr. To B a/c (Due to B's insolvency, 0.40 paise in a rupee is received)	1,350 2,025	 3,375

'P' Account

Dr. **Cr.**

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
	To bills payable	4,000		By Cash	985
	To Cash	330		By discount	15
	To Discount	45		By Bills receivable	4,500
	To Bank	4,500		By Cash	1,350
				By Bad debts	2,025
		8,875			**8,875**

SUMMARY

Credit transactions are very common in business. In such cases, the amount is paid or received only on a future date. A written document which is prepared to acknowledge the amount payable or receivable is called a Bills of Exchange or Promissory Note. A Bill of Exchange is drawn by the seller (a creditor) on the buyer (a debtor) asking him to pay the specified amount after a specified amount after a specified period to him or to his order. There is no need for acceptance of a promissory note.

For accounting purpose no distinction is made between a bill of exchange and a promissory note. The accounting aspects of a bill of exchange are dealt in three ways. (1) The bill is retained till the maturity date and presented for payment. (2) The bill is discounted with the bank (3) Endorsed the bill to the creditor. The acceptor may honour the bill, dishonour the bill, renew the bill or retire it.

Apart from the above said trade bill, an individual may accept a bill drawn by another person in consultation with him for the sake of helping the other person in creating the funds by discounting the bill. The amount may be used either by one person or by both. These bills are called as accommodation bills.

THEORY QUESTIONS

1) Define Bills of Exchange and bring out the features of it.
2) Differentiate Bills of exchange from promissory note
3) What is accommodation bill?

4) Explain the term “Noting Charges”
5) Give the specimen Journal entries for the renewal of the bill.
6) What are the advantages of Bills of Exchange?
7) Distinguish between Trade Bill and Accommodation bill.
8) What are days of Grace?
9) What do you mean by discounting of bills, endorsement of bills and retirement of bills?

EXERCISES

1) On 1st Jan 1999, Anand supplied goods to Ashok of the value of Rs. 9,000 and settled the account by means of three bills of Rs. 3000 each, due after two, three and four months respectively. A week later, Anand discounted the first bill at the discount of Rs. 60. The other two bills were held till maturity. On the due date the first two bills are duly met. On the maturity of the third bill, however, Ashok arranged to retire the bill by paying Rs. 1000 cash and giving Anand a fresh bill for four months to cover the balance together with 1% p.a. Anand discounted it for Rs. 2,000. Pass the necessary Journal entries in the books of Anand and Ashok.

2) Senthil sold goods at the value of Rs. 4000 to Kesavan, taking a bill at 3 months therefore. Senthil discounted the bill at 10% p.a. with his bank. On maturity the bill was returned by the ban dishonoured with Rs. 10 as noting charges. Kesavan paid Rs. 1,000 and the noting charges and gave another bill at 3 months for Rs. 3000 and 10% interest but before maturity he had become bankrupt and ultimately paid to his creditors 80 paise in the rupee. Pass Journal entries in the books of Senthil.

CHAPTER 8
FINAL ACCOUNTS

INTRODUCTION

Final accounts give a concise idea about the profitability and financial position of the business to the management, owners and other interested parties of the business. The financial accounts are prepared for a specific period by taking into account all the accounting information and data recorded in the subsidiary books and the ledger. All the revenue items in the Trial Balance are taken to the Trading and profit and Loss Account and all the capital items to the balance Sheet. Hence, the two parts of the final accounts are:

i. Trading and Profit and Loss Account; and
ii. Balance Sheet.

OBJECTIVES

The main objective of the study of

- To know to how to prepare trading and profit and loss account
- To understand the difference between trading profit and loss account and balance sheet.
- To differentiate balance sheet with trial balance.
- To know the different adjustments.

TRADING AND PROFIT AND LOSS ACCOUNT

This account has two parts, viz.,

1. Trading Account and
2. Profit and Loss Account

1. Trading account

The business concerns which purchase goods for resale, prepare the Trading Account. On the other hand, the concerns which manufacture the goods for the purpose of selling in the market, prepare Manufacturing account. The Trading Account is prepared to ascertain the trading results of the business, i.e. Gross profit earned or Gross Loss sustained by the business during a specific accounting period which is usually one year. The concern earns gross profit when the sale proceeds exceed the cost of the goods. Gross loss is incurred when the sale proceeds are less than the cost of goods sold.

Cost of Goods Sold = Opening Stock + Purchases+ Direct Expenses – Closing Stock

The specimen of a Trading Account is given below:

Trading Account for the year ended ……

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		***	By Sales	***	
To Purchases	***		**Less:** Sales Returns	***	***
Less: Purchases Returns	***	***	By Closing Stock		***
To Manufacturing Expenses		***	By Gross Loss (transferred to Profit & Loss a/c)		***
To Carriage in-wards		***			
To Freight		***			
To Wages		***			
To Power & Fuel		***			
To Direct Expenses		***			
To Coal, Water & Gas		***			
To Power		***			
To Octroi		***			
To Import duty		***			
To Customs duty		***			
To Foremen / works Manager's Salary		***			
To Royalty on Manufactured Goods		***			
To Gross Profit c/d (transferred to Profit loss a/c)		***			
		***			***

A. TRADING ACCOUNT ITEMS

Debit side:

1. **Opening Stock:** This represents the value of goods in hand in the beginning of the accounting period for which the trading account is prepared. The opening stock figure is usually obtained from the trial balance. In the case of a new business, there is no opening stock.
2. **Purchases:** This represents the total value of goods purchased both for cash and on credit basis, which are meant for resale. The purchases returns must be deducted from the total purchases and the net purchases

are shown on the debit side of the trading account. The following points are worth noting.

a) If the goods are purchased for personal use, it should be recorded as ordinary purchase by debiting purchases Account and crediting the supplier's Account. Then, this purchases should be treated as goods withdrawn by the proprietor for his personal use and the following journal entry is passed.

Drawings a/c	Dr.	****	
To Purchases a/c			****

b) Purchase of fixed assets such as furniture, machinery, etc., should not be included with the purchases and they must be shown as assets in the Balance Sheet

3. **Direct Expenses:** These are the expenses which are incurred for the purchase of goods or to bring the goods in a saleable form. They are shown on the debit side of the Trading account. The following are the examples of direct expenses.

(i) **Carriage, Cartage or Freight;** When these expenses are incurred on the purchase of goods, they are taken to the debit side of the Trading Account. However,when such expenses are incurred on purchasing any asset, then they should be capitalized and added to the cost of that asset and should not be taken to the Trading account. Any outstanding carriage, cartage or freight should be added with such expenses and should be shown as a liability in the Balance Sheet.

(ii) **Wages:** When wages are incurred on manufacturing goods or making them saleable, they are considered as direct expenses and debited to the Trading Account. Any outstanding wages should also be added with wages and will be shown as a liability in the balance Sheet. However, wage incurred on constructing a building or establishing any other asset should be excluded, while ascertaining the wage amount.

(iii) **Input Duty and Dock charges:** When goods are imported from abroad, customs duty, dock charges, etc., should be paid for clearing them from the ports. They are shown on the debit side of the trading account as they relate to the goods purchased.

(iv) **Octroi:**Octroi duty is paid when goods are purchased within the municipality and is debited to the Trading Account.

(v) **Fuel, Power, Coal and Gas:** Fuel and power expenses are incurred to produce goods and hence, are treated as direct expenses and debited to the Trading Account.

(vi) **Manufacturing Expenses:** Those expenses which are incurred in manufacturing the goods in the factory such as factory rent, factory insurance, factory lighting, etc., are treated as direct expenses and are debited to the Trading Account.

(vii) **Packaging Charges:** Packing charges incurred for those goods which cannot be sold without a container are taken to the Trading account. However, packing charges incurred for transportation, fancy purpose or advertisements are taken to the Profit and Loss Account.

(viii) **Consumable Stores:** Consumable stores are incurred to maintain the machinery in good working condition which may include engine oil, soft soap, cotton waste, oil grease and waste, etc.

(ix) **Royalties:** This represents the expenses incurred to pay the landlord, patentee or author for the right to use his land, patent or copyright. Hence, when the royalty is paid on the basis of production, it should be debited to Trading Account and when the same is based on sales, it should be debited to Profit and Loss Account.

Credit Side

1. **Sales:** This indicates the value of goods sold both for cash and on credit basis. Sometimes, goods may be returned by the customers, which are called as Sales Returns or Returns Inwards and the same should be deducted from total sales. While calculating the sales figure, the following points are to be considered.
   (a) Sale of any fixed assets such as furniture, machinery etc., should be excluded in the amount of sales
   (b) Sale on consignment or on hire purchase or sale or return basis should be entered separately.
   (c) When goods are sold on behalf of others and forward basis, they should be excluded from the sales.
   (d) Goods sold but not yet despatched should also be excluded from the sales.
2. **Closing Stock**: The stock of goods which remain at the end of trading period is called closing stock. Usually, the closing stock is given outside the trial balance. However, when purchases are adjusted through opening and closing stock, the figure of closing stock appears on debit balance of Trail balance. Hence, if closing stock is given outside the trial balance, it is taken to Trading Account and if it is given in the trial balance, it is merely shown as an asset in the Balance sheet. The closing stock is valued at the cost price or market price which is lower.

Closing Entries for Trading Account

The closing entries are those entries which are required to be passed to transfer opening stock, purchases, sales and returns to the trading account. This helps to close these accounts.

1. To transfer opening stock, net purchases and direct expenses to Trading Account:

Trading a/c	Dr.	***	
To Opening Stock a/c			****
To Purchase a/c		****	
To Direct Expenses a/c			****.

2. To transfer net sales and closing stock to Trading Account

Sales a/c	Dr.	****	
Closing Stock a/c	Dr.	****	
To Trading a/c			****

3. Transfer Gross profit/Gross Loss to P&L a/c

Trading a/c	Dr.	****	
To Profit and Loss a/c			****

(Or)

Profit and Loss a/c	Dr.	****	
To Trading a/c			****

Illustration 1

Ascertain cost of goods sold from the following figures:

	Rs.
Opening Stock	8,500
Purchases	30,700
Direct Expenses	4,800
Indirect Expenses	5,200
Closing Stock	9,000

Solution

Cost of goods sold = Opening stock + Purchases + Direct Expenses – Closing Stock

= 8,500 + 30,700 + 4,800 – 9,000

= Rs.35,000

Illustration 2

From the following ledger balances, prepare Trading a/c and ascertain the gross profit for the year ended 31st December 2013.

	Rs.
Opening Stock	5,570
Purchases	13,816
Sales	15,284
Purchase Returns	390
Returns Inwards	524
Wages paid	1,400
Import charges	252
Wages owing	40
Closing Stock	8,880

Solution

Trading Account for the year ended 31st December 2013

Dr. **Cr.**

Particulars	**Amount Rs.**	**Amount Rs.**	**Particulars**	**Amount Rs.**	**Amount Rs.**
To Opening Stock		5,570	By Sales	15,284	
To Purchases	13,816		**Less:** Sales Returns	524	14,760
Less: Purchases Returns	390	13,426	By Closing Stock		8,880
To Wages	1,400				
Add: Wages Owing	40	1,440			
To Import Charges		252			
To Gross Profit c/d (transferred to Profit & loss a/c)		2,952			
		23,640			**23,640**

Illustration 3

From the following ledger balances extracted at the close of a trading year ended 31st December 2014, prepare Trading Account.

	Rs.
Opening Stock	40,000
Purchases	1,00,000
Sales	4,00,000
Returns Inwards	7,500
Returns Outwards	2,000
Carriage Inwards	6,000
Wages	16,500
Freight and Dock Charges	12,000
Stock on 31.12.2014	35,000

Solution:

Trading Account for the year ended 31st December 2014

Dr. **Cr.**

Particulars	**Amount Rs.**	**Amount Rs.**	**Particular**	**Amount Rs.**	**Amount Rs.**
To Opening Stock		40,000	By Sales	4,00,000	
To Purchases	1,00,000		Less: Return Inwards	7,500	3,92,500

Less: Return Outwards	2,000	98,000	By Closing Stock		35,000
To Wages		16,500			
To Carriage Inwards		6,000			
To Freight & Dock Charges		12,000			
To Gross Profit c/d (transferred to Profit & loss a/c)		2,55,000			
		4,27,500			**4,27,500**

2. PROFIT AND LOSS ACCOUNT

After the preparation of trading account, the next step is to prepare the Profit and Loss Account. This account is prepared to ascertain the net profit/Loss of the business during a specific accounting period. As stated earlier, the closing balance of the Trading Account. i.e., Gross Profit or Gross Loss is transferred to the Profit and Loss Account with which this account starts and hence, the Profit and Loss Account is considered as sub-section of the Trading Account. For the calculation of the net profit/loss of the business, the Profit and Loss Account takes into consideration certain items of incomes and expenses which are of indirect nature. They are connected with the business and relating to the various activities of making the goods available to the consumers. Indirect expenses include administration/management expenses, selling and distribution expenses, financial expenses, extraordinary losses and expenses to maintain the assets in good working condition. On the debit side of the Profit and Loss Account, all expenses appearing in the trial balance, which cannot find place in the Trading Account are recorded and on the credit side of the profit and loss account all income including the non-trading incomes like interest on bank deposits or securities, dividend on shares, rent of let-out property, profit on sale of fixed assets, etc., are recorded.

As all the nominal accounts from the Trial Balance are transferred to the Profit and Loss Account, its balance, i.e. Net Profit (When credit side is more than the debit side) or Net Loss (When debit side is more than the credit side) is transferred to the Capital Account of the proprietor, which will increase or decrease it accordingly.

Specimen of a Profit and Loss Account

Profit and Loss Account for the year ended -------------

Dr. Cr.

Particulars	**Amount Rs.**	**Particulars**	**Amount Rs.**
To Gross Loss (transferred		By Gross Profit	
from Trading a/c)	***	(Transferred	
To Management Expenses:		from Trading a/c)	***
Rent, rates & taxes	***	By Other Income:	
Lighting	***	Discount received	***
Office salaries	***	Commission received	***
Printing & Stationery	***	By Non-trading Income:	
Postage & Telegrams	***	Interest received	***
Telephone Charges	***	Rent of let-out property	***
Legal Charges	***	Dividend on shares	***
Audit Fees	***	Interest on debentures	***
Insurance	***	Apprentice premium	***
General Expenses	***	By Abnormal Gains	
To Maintenance Expenses:		Profit on sale of asset	***
Depreciation	***	By Net Loss	***
Repairs	***	(Transferred to Capital	
Renewals	***	Account)	
To Selling and Distribution			
Expenses:			
Traveler's Salaries	***		
Expenses and	***		
commission	***		
Bad debts	***		
Godown Rent	***		
Export Expenses	***		
Carriage Outwards	***		
Samples	***		
Agent's Commission	***		
Upkeep of motor lorries	***		
To Financial Expenses:			
Discount allowed	***		
Bank Charges	***		
Interest on Capital	***		
Interest on Loan	***		
Discount on Bills	***		
To Abnormal Losses:			
Loss by fire (not			
covered by Insurance)			
Cash defalcations	***		

Loss on sale of asset To Net profit (Transferred to Capital Account)	*** ***		
	***		***

PROFIT AND LOSS ACCOUNT ITEMS

Debit Side:

The items which appear on the debit side of the Profit Loss Account are as follows.

a) **Gross Loss (if any):** This represents the balance of Trading Account transferred to the Profit and Loss Account, when it shows Gross Loss .
b) **Management Expenses:** Management Expenses are incurred to carry on the day-to-day administration of a business. They include rent, rates, taxes, salaries, printing and stationery, lighting, postage and telegrams, telephone charges, legal charges, audit fees, insurance, general expenses, etc.,
c) **Maintenance Expenses:** They are incurred to maintain the fixed assets of the administrative office in a good order. eg. repairs, renewals, depreciation etc. Repairs and small renewals or replacements relating to the plant and machinery, fixtures, fittings, etc., are generally included under this heading and the same is debited to the Profit and Loss Account.
d) **Selling and Distribution Expenses:**They are incurred to promote sales and distribution of goods. eg. godown rent, advertisement, bad debts, samples, carriage outwards, export expenses, agent's commission, etc.
e) **Financial Expenses:** They are incurred to arrange finance which is required to run the business. Eg. interest on Loan, interest on Capital, discount allowed, discount on bills etc. The owners of the business, who provide the required capital to the business, are paid interest on their capital.
f) **Abnormal Losses:**They are incurred, during an accounting period but not in the normal course of a business. All abnormal losses are considered as extraordinary expenses and debited to the profit and Loss Account. eg. Stock lost by fire which is not covered by insurance, cash defalcations, etc.

Personal Expenses – not to Appear in Profit Loss Account

The following personal expenses are not to be shown in the Profit and Loss Account.

(i) **Domestic and household expenses of proprietor or partners:**
As they represent personal expenses, they are treated as drawings and they should not be debited in the Profit & Loss a/c.

- **(ii)** **Life Insurance Premium:** The premium paid on the policy of the proprietor, or partners should not be charged to Profit and Loss Account and they should be charged to Drawings Account.
- **(iii)** **Income Tax:** As it represents a personal expense of the proprietor, it should be added to the drawings and not to be debited in the Profit and Loss Account.

2. Credit side

- **a)** **Gross Profit:** This represents the debit balance of the Trading Account transferred to the profit and Loss account.
- **b)** **Business Incomes:** The incomes which are earned during the normal course of business are known as business incomes, eg., discount received, commission received, etc.
- **c)** **Non-trading Incomes:** The business may earn income from other business activities, they are called as non-trading incomes. eg. interest received, dividend from shares, rent on letting of any property, interest on debentures, apprenticeship premium, etc.
- **d)** **Abnormal Gains:** They are earned during the accounting period but not in the ordinary course of business. Abnormal gains are considered as extraordinary incomes and are credited to the Profit and Loss Account. eg., Profit on sale of a fixed assets.

Closing Entries for Profit and Loss Account

The following entries are passed to close various accounts in the trial balance.

1. To transfer various expenses to profit and Loss Account.

Profit and Loss a/c	Dr.	****	
To Various Expenses a/c			****

2. To transfer various incomes and gains to Profit and Loss Account.

Various incomes and gains a/c	Dr.	****	
To Profit and Loss a/c			****

3. a) To transfer Net Profit

Profit and Loss a/c	Dr.	****	
To Capital a/c			****

b) To transfer Net Loss

Capital a/c	Dr.	****	
To Profit and Loss a/c			****

Now you have learnt the items to be debited and credited in the profit and loss account. Let us illustrate the preparation of profit and loss account from Illustrations 4and 5

Illustration 4

Prepare profit and loss account from the following balances extracted from the books of Mr.Ruban for the year ended 31st December 2013

	Rs.
Gross profit	1,85,000
Salaries	20,000
Rent and Rates	5,000
Stationery	1,000
Postage	500
Insurance	2,000
Repairs	1,500
Depreciation	5,000
Advertisement	5,000
Discount (Dr.)	500
Commission to sales man	5,000
Bad debts	2,000
Loss by fire	2,000
Interest on Investments	2,500
Profit on sale of investment	2,000

Solution

Profit and Loss Account of Mr. Ruban for the year endingDecember 31, 2013

Dr. **Cr.**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Salaries	20,000	By Gross Profit b/d	1,85,000
To Rent and Rates	5,000	(transferred from	
To Stationery	1,000	trading a/c)	
To postage	500	By Interest on Investments	2,500
To Insurance	2,000	By Profit on Sale of	
To Repairs	1,500	Investments	2,000
To Depreciation	5,000		
To Advertisement	5,000		
To Discount	500		
To Commission to			
Salesmen	5,000		
To Bad Debts	2,000		
To Loss by fire	2,000		
To Net Profit (transferred to			
Capital account)	1,40,000		
	1,89,500		**1,89,500**

Illustration 5

From the following balances extracted at the close of the year ended 31st December 2014, prepare the profit loss account.

	Rs.
Gross profit	1,53,000
Carriage outwards	7,500
Salaries	27,500
Discount (Dr.)	1,500
Apprentice premium (Cr.)	4,500
Rent	3,300
Travelling Expenses	600
Fire Insurance Premium	2,700
Rates and Taxes	1,050
Printing & Stationery	750
Trade Expenses	900
Bad debts	6,300

Solution

Profit and Loss Account for the year endingDecember 31, 2014

Dr. **Cr.**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Salaries	27,500	By Gross Profit b/d (transferred from trading a/c)	1,53,000
To Rent	3,300		
To Rates & Taxes	1,050		
To Carriage outwards	7,500	By Apprentice Premium	4,500
To Travelling Expenses	600		
To Discount	1,500		
To Bad debts	6,300		
To Fire insurance premium	2,700		
To Printing &Stationery	750		
To Trade Expenses	900		
To Net profit (Transferred to Capital a/c)	1,05,400		
	1,57,500		**1,57,500**

In practice, the trading account and the profit and loss account are combined together and an account called Trading and Profit and Loss account is prepared.

This account is divided into two parts. The first part shows the gross profit and the second part shows the net profit.

Look at the illustration 6 and know how combined trading and profit and loss account is prepared.

Illustration:6

From the following figures prepare trading and profit and loss account of Lakshmi & co, for the year ended December 31, 2015. Closing stock was valued at Rs. 26,000 on that date.

	Rs.
Stock on January 1,2015	40,000
Purchases	98,000
Commission Received	650
Rant, Rates and Taxes	8,600
Salaries & Wages	12,000
Sales	1,62,100
Return Inwards	2,400
Return Outwards	3,000
Sundry Expenses	2,500
Bank Charges	50
Discount Received	750
Carriage on Purchases	2,000
Discount Allowed	530
Carriage on Sales	1,700
Lighting and Heating	2,200
Postage	300
Income from Investments	500
Commission paid	1,000
Interest paid on a bank Loan	550

Solution

Trading and Profit and Loss Account of Lakshmi & Co.for the year ending December 31, 2015

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		40,000	By Sales	162,100	
			Less:		
To Purchases	98,000		Return inwards	2,400	1,59,700
Less:			By		
Return outwards	3,000	95,000	Closing Stock		26,000
To Carriage on Purchases		2,000			
To Gross Profit c/d (transferred to Profit & loss a/c)		48,700			
		1,85,700			**1,85,700**

To Rent, Rates and Taxes		8,600	By Gross Profit b/d (transferred from trading a/c)		48,700
To Salaries & Wages		12,000	By Commission Received		650
To Sundry Expenses		2,500	By Discount Received		750
To Bank Charges		50	By Income from Investments		500
To Discount Allowed		530			
To Carriage on Sales		1,700			
To Postage		300			
To Commission Paid		1,000			
To Interest paid on bank loan		550			
To Lighting & heating		2,200			
To Net profit (Transferred to Capital a/c)		21,170			
		50,600			**50,600**

BALANCE SHEET

A Balance sheet is a statement depicting the financial position of the business on a specific date. The financial position of a business is revealed by its assets and liabilities on a particular date. A balance sheet is also described as a "Statement showing the sources and application of capital". This Statement is prepared from the real and personal account balances. On the left hand side of the balance sheet, all the sources from which capital and other funds raised are entered. As against this, on the right side all the applications or uses of such capital and funds are entered. i.e. on the left side, capital and liabilities are recorded and on the right side all the assets are recorded.

1. Capital and liabilities

All credit balances in the personal account and real account represents liabilities. i.e. the amount owed by the business to various parties viz., owners, creditors, banks, financial institutions. The liabilities side gives the details of the sources from which the business has obtained the required resource funds. The sources may be internal or external. That part of funds which is generated internally or from owners is called capital and that which is generated externally or from outsiders is known as liabilities.

Liabilities

The liabilities of a business can be classified into

(i) Fixed Liabilities
(ii) Long –term Liabilities
(iii) Current Liabilities and
(iv) Contingent Liabilities

(i) Fixed Liabilities

Fixed liabilities are those liabilities which are payable only on the liquidation of a business. eg., capital which represents liability to the owner.

(ii) Long –term Liabilities

Long-term liabilities represent those liabilities which are generally repayable after a long period of time, say, 5 or 10 years. eg. Long-term bank loans.

(iii) Current Liabilities and

Current Liabilities are those which are generally repayable within an accounting year and the repayment of which is made by using or selling any current asset of the business. The example of current liabilities are-

Sundry Creditors: They are the suppliers who have supplied goods on credit to the business and in turn lies their legitimate claims against the business.

Bills Payable: These are the claims of the suppliers goods against the business as evidenced by a note or any written acknowledgement of debt.

Liability for taxes: This represents the provisions created/made by the business to pay the estimated liability in future or the next accounting year.

Income received in advance: These are the liabilities of the business which have been incurred because of the receipt of money in advance of a service to be rendered in the near future, say one year, eg., rent received in advance.

(iv) Contingent Liabilities

Contingent liabilities are those liabilities which may or may not occur, i.e., their occurrence is uncertain. Thus, a contingent liability is not an actual liability but will become an actual one on the happening of certain event, which is uncertain. Hence, the contingent liabilities are not recorded in the books of account and it is shown as foot note at the bottom of the balance sheet eg., claims against the business not acknowledged as debts, liability on a case pending in the court, guarantees given against a particular firm of person, etc.

1. **Assets**

They are the property on possession of any business. They increase the capacity to contribute to future cash inflows, i.e., earning capacity of a business. They are valuable resources, owned by the business, which are acquired at a cost which is measurable in monetary terms. There are different kinds of assets, such as fixed, current, intangible, fictitious and contingent.

(i) **Fixed Assets:** These assets are tangible in nature. i.e., they can be seen, touched and have volume and value. eg., Machinery, plant, Buildings, Land, Furniture, Fittings, etc. They are used for the purpose of earning profit. These assets are usually long-lived.

(ii) **Current Assets:** Current assets are those assets which can be converted into cash or consumed during thenormal operating cycle of the business or usually within a shorter period, say one year. The important distinction between the current assets and the fixed assets is the time factor. The current assets are usually held by the business for not more than one year, eg., Stock, Debtors, Bills Receivable, Investments, Prepaid Expenses, Outstanding incomes, Cash, etc., while the fixed assets are held by the business for more than one year. Thus, current assets are those assets which can be realised and readily available to discharge the current liabilities.

(iii) **Intangible Assets:** Intangible assets are those which cannot be seen, touched and have no volume but have value. eg., Goodwill, Patents, Trademarks, Copyright, etc.

(iv) **Fictitious Assets:** Fictitious assets are those assets which are virtually not assets. They represent usually past accumulated losses or expenses which are incurred for once in the life time of a business and are temporarily capitalized. eg. Profit and Loss Account (debit balance), Organisation expenses, Heavy advertisement Expenses.

Specimen of the Balance Sheet

Balance Sheet as on ………………..

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Fixed Liabilities **Capital**			**Intangible Assets** Goodwill		 ***

Add: Net profit	***		Patents		***
Less: Net Loss	***		Trade Mark		***
Less: Drawings	***	***	Copyright		***
Long-term Liabilities			**Fictitious Assets**		
			Advertisements		***
Loan from Bank		***	Profit and Loss Account		***
Current Liabilities			Preliminary Expenses		***
Bills Payable		***	**Fixed Assets**		
Sundry Creditors		***	Land & Buildings		***
Bank Overdraft		***	Plant & Machinery		***
Outstanding Expenses		***	Furniture and Fixtures		***
Income		***	Motor Car		***
received in advance		***	**Current Assets**		
			Sundry Debtors		***
			Bills Receivable		***
			Closing Stock		***
			Prepaid Expenses		***
			Outstanding Incomes		
			Liquid Assets		***
			Cash in hand		***
			Cash at Bank		***
		***			***

Illustration 7

From the following particulars, prepare a Balance Sheet as on 31st December, 2015

	Rs.		Rs.
Capital	75,000	Loan to 'B'	7,500
Buildings	82,500	Investments	4,500
Furniture	3,750	Cash in hand	300
Bills Receivable	5,250	Cash at Bank	5,250
Sundry Debtors	30,000	Drawings	4,500
Bills Payable	3,750	Net Profit	58,350
Sundry Creditors	23,700	Stock	10,500
Machinery	6,750		

Solution

Balance sheet as on 31 December 31, 2015

Liabilities	**Amount Rs.**	**Amount Rs.**	**Assets**	**Amount Rs.**	**Amount Rs.**
Capital	75,000		Buildings		82,500
Add: Net Profit	58,350		Furniture		3,750
	1,33,350		Machinery		6,750
Less: Drawings	4,500	1,28,850	Loan to 'B'		7,500
Sundry			Stock		10,500
Creditors		23,700	Bills Receivable		5,250
Bills Payable		3,750	Sundry Debtors		30,000
			Investments		4,500
			Cash at bank		5,250
			Cash in hand		300
		1,56,300			**1,56,300**

Now see illustration 8 to understand how the trading and profit and loss account and the balance sheet are prepared from a given trial balance.

Illustration 8

The following Trial Balance is extracted from the books of Rajan on 31st December, 2014. Prepare final accounts.

Trial Balance as on 31st December,2008

	Rs.		**Rs.**
Salaries and wages	4,000	Capital	2,05,000
Purchases	2,00,000	Discount received	300
Duty on purchases	7,000	Sales	3,00,000
Legal Charges	2,000	Purchase Returns	4,000
Sales Returns	10,000	Sundry Creditors	16,000
Cash Balance	10,000	Bank O/D	3,000
Stock at		Bills Payable	1,000
Commencement (1.1.14)	15,000	Loan	10,000
Advertisement	1,000	Income from Investments	700
Land & Building	1,60,000		
Plant & Machinery	50,000		
Investments	5,000		
Drawings	6,000		
Sundry Debtors	60,000		
Bills Receivable	10,000		

Adjustment: Stock at the end (31.12.14) Rs.30,000.

Solution

Trading and Profit and Loss Account of Mr. Rajanfor the year ending 31st December, 2014

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		15,000	By Sales	3,00,000	
To Purchases	2,00,000		Less: Sales Returns	10,000	2,90,000
Less: Purchases Returns	4,000	1,96,000	By Closing Stock		30,000
To Duty on Purchases		7,000			
To Gross Profit c/d (Transferred to Profit & Loss a/c)		1,02,000			
		3,20,000			**3,20,000**
To Salaries & Wages		4,000	By Gross Profit b/d (Transferred from Trading Account)		1,02,000
To Legal Charges		2,000			
To Advertisement		1,000			
To Net profit (Transferred to Capital a/c)		96,000	By Discount Received		300
			By Income from Investment		700
		1,03,000			**1,03,000**

Balance sheet of Mr. Rajan as on 31st Dec.2014

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	2,05,000		Cash Balance		10,000
Add: Net Profit	96,000		Investments		5,000
	3,01,000		Bills Receivable		10,000
Less: Drawings	6,000	2,95,000	Sundry Debtors		60,000
Sundry Creditors		16,000	Closing Stock		30,000
Bills Payable		1,000	Land &Buildings		1,60,000

Bank O/D		3,000	Plant &		
Loan		10,000	Machinery		50,000
		3,25,000			**3,25,000**

USES OF BALANCE SHEET

A Balance Sheet has the following uses:

1. It helps to calculate the actual capital employed in the business.
2. The financial position can be ascertained clearly with help of a Balance Sheet.
3. When a sale of business concerns iseffected, their Balance Sheets serve as a base for determining the purchase consideration of the takeover.
4. By comparing the Balance Sheet of different years, the change in the working capital can be measured and suitable correctives can be undertaken.
5. Ratio Analysis is facilitated with the help of the Balance Sheet and better management decisions can be taken.

LIMITATIONS OF BALANCE SHEET

Though every organisation or business prepares the Balance Sheet, it is subject to the following limitations:

1. A conventional Balance Sheet, which shows the value of fixed assets at historical cost less depreciation up-to-date, cannot reflect the real values of these assets. Intangible assets shown at book values may not have any relationship with their market values.
2. The Balance Sheet sometimes has some fictitious assets which have no market value. Such as profit and loss account (debit balance), preliminary expenses, discount, etc. This will unnecessarily inflate the total value of assets.
3. The value of factors like skill, loyalty of the staff, etc., cannot be disclosed in a Balance Sheet.
4. Under inflationary conditions, the Balance Sheet will certainly mislead the untrained readers.
5. The valuation of most of the current assets is based on some estimates and hence, real and true financial position of the business cannot be reflected through a Balance Sheet.

DISTINCTION BETWEEN TRADING & PROFIT & LOSS A/C AND BALANCE SHEET

S. No.	Trading and profit & Loss a/c	Balance sheet
1.	It is a Nominal Account	It is only a statement of Assets and Liabilities.
2.	The preparation of this account confirms to the	Journal entries are not required for the preparation of the Balance

	Principle of double entry.	Sheet.
3.	All revenue items are transferred to this account.	All capital items representing Assets and Liabilities are grouped in this Statement in a classified form.
4.	This account shows the Gross Profit and Net Profit or Net Loss	This statement shows Assets and Liabilities.
5.	This account is usually prepared for a particular period.	Balance Sheet is prepared on a particular date.

DIFFERENCES BETWEEN BALANCE SHEET AND TRIAL BALANCE

a. All the ledger accounts showing a balance find a place in the Trial Balance. But in a Balance Sheet only certain real accounts and personal accounts indicating liabilities and assets are entered.
b. A trial Balance is prepared even before the preparation of Trading and profit and Loss account. But a Balance Sheet can be prepared only after preparing the Trading and Profit and Loss Account.
c. A Trial balance shows only the arithmetical accuracy of the accounts entered. A Balance Sheet shows the financial position of the trader as on a particular date.
d. Opening stock is entered in the Trial Balance whereas closing stock finds a place only in the Balance Sheet.

ADJUSTMENTS

You know that after the agreement of the Trial Balance, steps are taken for the preparation of Final Account which includes the Trading and Profit and Loss Account and the Balance sheet. By preparing periodically what is known as the Final Account, the primary objects of the trader to know the exact financial position of the business and to know clearly whether the business is progressing.

In the foregoing parts, you have learnt how to compile the Trading and Profit and Loss Account and the Balance Sheet ina simple form fromthe Trial Balance. The stage has arrived when certain general observations may be made regarding the precise significance of the use of the Final Account. We have assumed, that all expenses and incomes shown in the Trial Balance relate to the current period. In practice, so many expenses and incomes relating to that period may not be fully disbursed or received. Therefore, adjustments like this will have to be made, before the Books of Accounts are closed and the Final Account is prepared. In order to make suitable adjustments for this purpose, Adjustment Entries are passed. It should be remembered, that necessary adjustments are brought about by means of adjustment entries before the accounts are closed and the final account is prepared.

Usual Adjustments:

Usually adjustments are required for the following items:

1. Closing Stock	2. Outstanding expenses
3. Prepaid expenses	4. Outstanding incomes
5. Income received in advance	6. Depreciation
7. Bad debts	8. Provision for doubtful debts
9. Provision for discount on debtors	10. Provision for discount on creditors
11. Interest on capital	12. Interest on drawings

S. No.	Journal Entry for the adjustments	Adjustment in Trading a/c or in P&L a/c	Adjustment in Balance Sheet
1.	**Closing stock** Closing Stock a/c Dr. To Trading a/c	Trading a/c Credit side as, "By closing stock"	Assets side as closing stock
2.	**Outstanding expenses** Expenses a/c Dr. To Outstanding expenses a/c	Trading a/c or P&L a/c debit side as added to concerned expenses	Liabilities side, as outstanding expenses
3.	**Prepaid expenses** Prepaid expenses a/c Dr. To Expenses a/c	Trading a/c or P&L a/c debit side deducted from the concerned expenses	Assets side, as Prepaid expenses
4.	**Accrued Income** Outstanding income a/c Dr. To Income a/c	P&L Credit side as added to the concerned income	Assets side, as outstanding income
5.	**Income received in advance** (received but not earned income) Income a/cDr. To Income Received advance a/c	P&La/c Credit side as deducted form the concerned income	Liabilities side, as income received in advance
6.	**Depreciation** Depreciation a/c Dr. To asset a/c	P&L a/c Debit side as "to depreciation"	Assets side, as deducted from the concerned asset.
7.	**Appreciation** Assets a/cDr. To P & L a/c	P&L Credit side as "By asset (Appreciation)"	Assets side, as added to the concerned assets
8.	**Interest on Capital** Interest on capital a/c Dr. To Capital a/c	P&L Debit side as "By Interest on Capital"	Liabilities side added to capital

9.	**Interest on Drawings** Drawings a/c Dr. To Interest on Drawings a/c	P&L Credit side as “To Interest on Drawing”	Liabilities side, deducted from capital
10.	**Interest on Loan** Interest on Loan a/c Dr. To Loan a/c	P&L Debit side as “To Interest on Loan”	Liabilities side
11.	**Additional Bad debts** Bad debts a/cDr. To Sundry debtors	P&L a/c debit side as Added to Bad debts a/c or added to a new provision for doubtful debts	Assets side, as less from Sundry debtors
12.	**Reserve (Provision) for doubtful debts** Provision for doubtful for debts a/c Dr. To Debtors a/c	P&L Debit side as “To Reserve for doubtful debts a/c	Assets side as deducted from sundry debtors after additional bad debts, if any
13.	**Reserve for discount on debtors** P & L a/c Dr. To Reserve for discount on debtors a/c	P&L a/c debit side as “To Reserve for discount on debtors a/c”	Assets side, as less from sundry debtors, after provision for doubtful debts, if any
14.	**Reserve for discount on creditors** Reserve for discount on creditors a/c Dr. To P & L a/c	P&L a/c credit side as “By reserve for discount on creditors a/c”	Liability side deducted from sundry creditors
15	**Deferred Revenue expenditure** (Amount so deferred is treated as balance on the expense a/c of c/f)	P&L a/c debit side as to expenses Less: balance carried forward.	Assets side, as unwritten off (expenditure like advt. etc.)
16.	**Stock destroyed or damaged** Stock destroyed a/cDr. To Trading a/c	a.) Trading a/c credit side, as “By stock destroyed a/c” b.) P&L a/c debit side, as “to stock destroyed a/c” to the extent of loss irrecoverable.	Treated as an Asset, if the loss is recoverable from any party.

Problems relating to provision for bad and doubtful debts and provision for discount on debtors and creditors

Illustration 9

The following information appear in the boos of a concern

	Rs.
Provision for doubtful debts on 1.1.2015	6,500
Bad debts written off during the year	8,000
Sundry debtors on 31.12.2015	1,12,500

Of the sundry debtors Rs. 20,000 was bad and provision for doubtful debts was to be maintained at 5% on sundry debtors.

Show bad debts and provision for doubtful debts and the relevant extracts of P & L and balance sheet.

Solution:

Bad debts a/c

Dr. **Cr.**

Year	**Particulars**	**Amount Rs.**	**Year**	**Particulars**	**Amount Rs.**
2015	To Balance b/d	8,000	2015	By Provision for	
	To Sundry debtors	2,000		doubtful debts	10,000
		10,000			**10,000**

Provision for Bad debts a/c

Dr. **Cr.**

Year		**Amount Rs.**	**Year**	**Particulars**	**Amount Rs.**
2015 Dec 31	To Bad debts	10,000	2015 Jan 1	By Balance b/d	6,500
	To Balance c/d	5,525	Dec 31	By Profit & Loss a/c	9,025
		15,525			**15,525**

Workings

Debtors	=	1,12,500
Less: New Bad debts	=	2,000
	=	1,10,500

Provision

5% on debtors = 5/100×1,10,500

= 5,525

Profit & Loss a/c

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Old Bad debts	8,000				
Add: New bad debts	2,000				
	10,000				
Add: New provision for bad debts (5%)	5,525				
	15,525				
Less: Old provision for bad debts	6,500	9,025			

Balance sheet

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
			Sundry Debtors	1,12,500	
			Less: New Bad debts	2,000	
				1,10,500	
			Less: New Provision for doubtful debts	5,525	1,04,975

Illustration 10

The following figures appear in the books of Vijay 2015

		Rs.
2015		
Jan 1	Bad and doubtful debts provision	1,200
	Discount allowed provision	560
Dec 31	Discount allowed during the year	930
	Bad debts written off	470
	Bad debts recovered	25
	Debtors	10,060

Write off further Rs. 240. Create a discount allowed provision of 2%. Create a bad and doubtful provision of 10%. Prepare provision for doubtful debts account, bad debts account and provision for discount account.

Solution:

Bad debts a/c

Dr. **Cr.**

Year	Particulars	Amount Rs.	Year	Particulars	Amount Rs.
2015	To Balance b/d	470	2015	By Recovery	25
	To Sundry debtors	240		By Balance c/d	685
		710			**710**

Provision for Bad debts a/c

Dr. **Cr.**

Year	**Particulars**	**Amount Rs.**	**Year**	**Particulars**	**Amount Rs.**
2015			2015		
Dec 31	To Bad debts	685	Jan 1	By Balance b/d	1,200
	To Balance c/d	982	Dec 31	By Profit & Loss a/c	467
		1,667			**1,667**

Provision for discount a/c

Dr. **Cr.**

Date	**Particulars**	**Amount Rs.**	**Date**	**Particulars**	**Amount Rs.**
2015			2015		
Dec 31	To Discount	930	Jan. 1	By Balance c/d	560
	To Balance c/d	177		By Profit & Loss	547
		1,107			**1,107**

Workings

Debtors	=	10,060
Less: New Bad debts	=	240
	=	9,820
Less: New provision for bad debts (10%)		982
		8,838
Less: Provision for discount 2%		177
		8,661

PREPARATION OF FINAL ACCOUNTS WITH ADJUSTMENTS

You have learnt that how the adjustments are to be made in the final account. You need not pass any adjustment entries unless specifically asked. All adjustments are to be shown directly in the final accounts.

Problem: 1

Prepare a trading account of Mr. Babufrom the following figures as on 31st December 2012.

	Rs.
Opening Stock	500
Purchases	2,500
Sales	3,600
Closing stock	300

Solution:

Trading account of Mr. Babu for the year ended 31st December 2012

Dr. **Cr.**

Particulars	**Amount Rs.**	**Particulars**	**Amount Rs.**
To Opening Stock	500	By Sales	3,600
To Purchases	2,500	By Closing Stock	300
To Gross Profit	900		
	3,900		**3,900**

Problem: 2

Prepare a trading account of Mr.Arun for the year ended 31st December2013

	Rs.
Opening Stock	5,700
Purchases	1,58,000
Purchases returns	900
Sales	2,62,000
Sales returns	600

Closing stock was valued at Rs.8,600

Solution:

Trading account of Mr. Arun for the year ended 31st December 2013

Dr. **Cr.**

Particulars	**Amount Rs.**	**Amount Rs.**	**Particulars**	**Amount Rs.**	**Amount Rs.**
To Opening Stock		5,700	By Sales	2,62,000	
			Less:		
To Purchases	1,58,000		Sales Returns	600	2,61,400
Less: Purchase Returns	900	1,57,100	By Closing Stock		8,600
To Gross Profit		1,07,200			
		2,70,000			**2,70,000**

Problem: 3

Thefollowing are some of the balance extracted from the ledger of Mr.Karuppasamy as on 31st December 2014. Prepare a trading account.

Particulars	**Debit Rs.**	**Credit Rs.**
Stock 1.1.2014	12,500	
Purchases	1,00,000	
Sales		1,50,000
Return outwards		5,000

Return inwards	10,000
Salaries	4,400
Wages	7,500
Rent	2,750
Carriage inwards	2,500
Carriage Outwards	750
Power, coal, gas	1,000

Stock on 31.12.2014 was valued at Rs.14,000

Solution:

Trading a/c of Mr. Karuppasamy for year ended 31.12.2014

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		12,500	By Sales	1,50,000	
			Less:		
To Purchases	1,00,000		Sales Returns	10,000	1,40,000
Less: Purchase Returns	5,000	95,000	By Closing Stock		14,000
To Wage		7,500			
To Carriage inwards		2,500			
To Power, Coal, Gas		1,000			
To Gross Profit		35,500			
		1,54,000			**1,54,000**

Problem: 4

Prepare Profit and loss account of Mrs. Nalini for the year ended 31st December 2013 from the following,

	Rs.		Rs.
Gross profit	1,25,000	Discount paid	600
Salaries	15,000	Discount received	1,000
Rent	5,000	Interest paid	500
Carriage outwards	1,000	Interest received	700
Selling expenses	500	Commission earned	2,000
Income from investments	1,500		

Solution:

Profit and Loss a/c of Mrs. Nalini for the year ended 31.12.2013

Dr. **Cr.**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Salaries	15,000	By Gross profit	1,25,000
To Rent	5,000	By Income from	
To Interest paid	500	Investments	1,500
To Carriage outwards	1,000	By Discount Received	1,000
To Selling expenses	500	By Interest Received	700
To Discount paid	600	By Commission earned	2,000
To Net Profit	1,07,600		
(Transfer to Capital a/c)			
	1,30,200		**1,30,200**

Problem: 5

The following balances are taken from the books of M/s. RSP Ltd. Prepare profit and loss account for the year ended 31st March 2014.

	Rs.		Rs.
Gross profit	5,25,000	Salaries & Wages	1,00,000
Rent	10,000	Depreciation	5,000
Interest on loan	5,000	Office expenses	1,500
Distribution charges	2,500	Salesman Salary	8,000
Bad debts	2,200	Stationery and printing	500
Commission Received	3,000	Discount received	2,000
Interest received	5,000	Advertising	9,000
Taxes and insurance	2,000		

Solution:

Profit and Loss a/c of M/S. RSP Ltd for the year ending 31.03.2014

Dr. **Cr.**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Rent	10,000	By Gross Profit	5,25,000
To Interest on Loan	5,000	By Interest received	5,000
To Distribution Charges	2,500	By Commission Received	3,000
To Bad debts	2,200	By Discount received	2,000
To Taxes & Insurance	2,000		
To Salaries & Wages	1,00,000		
To Depreciation	5,000		
To Office expenses	1,500		
To Salesman Salary	8,000		
To Stationery & Printing	500		

To Advertising	9,000		
To Net Profit	3,89,300		
	5,35,000		**5,35,000**

Problem: 6

From the following particulars, prepare a balance sheet of Mr. Venugopal as on 31st December 2015.

	Rs.		Rs.
Capital	40,000	Drawings	4,400
Debtors	6,400	Creditors	4,200
Cash in hand	360	Cash at bank	7,200
Furniture	3,700	Plant	10,000
Net profit	1,660	General reserve	1,000
Closing stock	14,800		

Solution:

Balance Sheet of Mr. Venugopal as on 31.12.2015

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	40,000		Debtors		6,400
Add: Net Profit	1,660		Cash in hand		360
	41,660		Furniture		3,700
Less: Drawings	4,400	37,260	Cash at bank		7,200
Creditors		4,200	Plant		10,000
General Reserve		1,000	Closing Stock		14,800
		42,460			**42,460**

Problem: 7

From the following information prepare balance sheet of Mrs. Nasreen khan as at 31st December 2014.

	Rs.		Rs.
Goodwill	10,000	Sundry debtors	25,000
Capital	90,000	Drawings	15,000
Cash in hand	10,000	Land & Buildings	30,000
Investment	500	Bank	10,000
Net profit	46,900	Creditors	31,500
Bills receivable	6,500	Plant & Machinery	20,000
Bills payable	5,350	Closing stock	40,000
Furniture	6,750		

Solution:

Balance Sheet of Mrs. Nasreen Khan as on 31.4.2014

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	90,000		Good will		10,000

Add: Net Profit	46,900		Cash in hand		10,000
	1,36,900		Investment		500
Less: Drawings	15,000	1,21,900	Sundry Debtors		25,000
Creditors		31,500	Land & Buildings		30,000
Bills Payable		5,350	Bank		10,000
			Bills Receivable		6,500
			Furniture		6,750
			Plant & Machinery		20,000
			Closing Stock		40,000
		1,58,750			**1,58,750**

Problem: 8

Given below is the trial balance of Shri.Hari Prakash. Prepare trading and profit and loss account and balance sheet for the year ended 31st March 2014.

Particulars	Debit Rs.	Credit Rs.
Stock as on 1.4.2013	50,000	
Sales		2,90,000
Sales returns	10,000	
Purchases	2,45,000	
Purchase returns		5,000
Carriage inwards	4,000	
Carriage Outwards	6,000	
Wages	12,000	
Salaries	18,000	
Printing and Stationary	900	
Discount allowed	900	
Discount received		1,500
Depreciation	3,000	
Buildings	2,08,100	
Trade expenses	5,600	
Capital		2,72,000
Bills receivable	20,000	
Bills payable		15,000
	5,83,500	**5,83,500**

Closing stock on 31.3.2014 Rs.65,000

Solution:

Trading & Profit and Loss Account of Shri. Hari Prakash for the year ending 31.03.2014

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		50,000	By Sales	2,90,000	
To Purchases	2,45,000		**Less:** Sales Returns	10,000	2,80,000
Less: Purchases Returns	5,000	2,40,000	By Closing Stock		65,000
To Carriage Inwards		4,000			
To Wages		12,000			
To Gross Profit c/d		39,000			
		3,45,000			**3,45,000**
To Salaries		18,000	By Gross Profit b/d		39,000
To Printing & Stationery		900	By Discount Received		1,500
To Discount Allowed		900			
To Depreciation		3,000			
To Trade Expenses		5,600			
To Carriage Outwards		6,000			
To Net profit		6,100			
		40,500			**40,500**

Balance Sheet of Shri. Hari Prakash as on 31.03.2014

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	2,72,000		Buildings		2,08,100
Add: Net Profit	6,100	2,78,100	Bills Receivable		20,000
Bills Payable		15,000	Closing Stock		65,000
		2,93,100			**2,93,100**

Problem: 9

The following information was extracted from the books of M/s. Sudha Ltd. Prepare final accounts on 31.12.2014

Particulars	Debit Rs.	Particulars	Credit Rs.
Opening Stock	12,500	Sales	1,89,000

Depreciation	7,000	Commission	2,000
Carriage inwards	700	Capital	1,71,300
Furniture	8,000	Creditors	17,500
Carriage Outwards	500	Bills Payable	5,000
Plant & Machinery	2,00,000	Return outwards	13,800
Cash	8,900		
Salaries	7,500		
Debtors	19,000		
Discount	1,500		
Bills receivable	17,000		
Wages	16,000		
Sales returns	14,000		
Purchases	86,000		
	3,98,600		**3,98,600**

Closing Stock on 31.12.2015 Rs.45,000

Solution:

Trading & Profit and Loss Account of M/S. Sudha Ltd for the year ending 31.12.2015

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		12,500	By Sales	1,89,000	
			Less:		
To Purchases	86,000		Sales Returns	14,000	1,75,000
Less: Returns Outwards	13,800	72,200	By Closing Stock		45,000
To Carriage inwards		700			
To Wages		16,000			
To Gross Profit c/d		1,18,600			
		2,20,000			**2,20,000**
To Salaries		7,500	By Gross Profit b/d		1,18,600
To Depreciation		7,000	By Commission		2,000
To Carriage Outwards		500			
To Discount		1,500			
To Net profit		1,04,100			
		1,20,600			**1,20,600**

Balance Sheet of M/S. Sudha Ltd as on31.12.2015

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	1,71,300		Furniture		8,000
Add: Net Profit	1,04,100	2,75,400	Plant &		
Creditors		17,500	Machinery		2,00,000
Bills Payable		5,000	Cash		8,900
			Debtors		19,000
			Bills Receivable		17,000
			Closing Stock		45,000
		2,97,900			**2,97,900**

Problem: 10

The trial balance of Mr.Uma Shankar shows the following balances on 31st March 2013. Prepare final accounts.

Debit Balance	Rs.	Credit Balance	Rs.
Purchases	70,000	Capital account	56,000
Sales returns	5,000	Sales	1,50,000
Opening Stock	20,000	Purchases returns	4,000
Discount allowed	2,000	Discount received	1,000
Bank charges	500	Sundry creditors	30,000
Salaries	4,500		
Wages	5,000		
Freight inwards	4,000		
Freight outwards	1,000		
Rent, rates and taxes	5,000		
Advertising	6,000		
Cash in hand	1,000		
Plant and Machinery	50,000		
Sundry debtors	60,000		
Cash at bank	7,000		
	2,41,000		**2,41,000**

Closing Stock on 31st March 2013 was Rs.30,000

Solution:

Trading & Profit and Loss Account of Mr.Uma Shankar
for the year ending 31.03.2013

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		20,000	By Sales	1,50,000	
			Less:		
To Purchases	70,000		Sales Returns	5,000	1,45,000
Less: Purchases			By		

Returns	4,000	66,000	Closing Stock		30,000
To Wages		5,000			
To Freight Inwards		4,000			
To Gross Profit c/d		80,000			
		1,75,000			**1,75,000**
To Discount Allowed		2,000	By Gross Profit b/d		80,000
To Bank Charges		500	By Discount Received		1,000
To Salaries		4,500			
To Freight Outwards		1,000			
To Rent, Rates &Taxes		5,000			
To Advertising		6,000			
To Net Profit		62,000			
		81,000			**81,000**

Balance Sheet of Mr.Uma Shankar as on31.03.2013

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	56,000		Cash in hand		1,000
Add: Net Profit	62,000	1,18,000	Plant and Machinery		50,000
Sundry Creditors		30,000	Sundry Debtors		60,000
			Cash at bank		7,000
			Closing Stock		30,000
		1,48,000			**1,48,000**

Problem: 11 From the following details, determine Gross Profit:

	Rs.
Opening Stock	2,000
Purchases	15,000
Sales	26,000
Closing Stock	3,000
Return Outwards	200
Return Inwards	700
Wages	1,000
Salaries	2,000
Advertisement	3000
Interest	500

Solution:

Trading account

Dr. **Cr.**

Particulars	**Amount Rs.**	**Amount Rs.**	**Particulars**	**Amount Rs.**	**Amount Rs.**
To Opening Stock		2,000	By Sales	26,000	
To Purchases	15,000		**Less:** Return Inwards	700	25,300
Less: Return Outwards	200	14,800	By Closing Stock		3,000
To Wages		1,000			
To Gross Profit c/d		10,500			
		28,300			**28,300**

Problem: 12

The Adjusted Trail Balance of Manian, after making all adjustments, as on 30th June 2014 is given below. Prepare the Trading and profit and Loss Account for the year ending on 30.06.2014 and the Balancesheet as on the date:

Adjusted Trial Balance as on 30.06.2014

Particulars	**Debit Rs.**	**Credit Rs.**
Capital and Drawings	7,500	1,20,000
Adjusted Purchases	2,97,400	
Net Sales		4,30,000
Stock on 30.06.2014	37,600	
Debtors and Creditors	42,000	27,000
Discount	3,000	2,500
Insurance	4,500	
Unexpired Insurance	1,500	
Bills Receivable & Payable	14,000	8,000
Advertisement	7,500	
Salaries	46,400	
Wages	27,500	
Outstanding Wages		5,600
Carriage Inwards	5,400	
Bad debts	1,500	
Provision for debts		3,500
Provision for discount debtors		500
Factory Rent	9,600	
Bank Loan		60,000
Sundry Expenses	2,000	

Depreciation on Machinery	7,000	
Depreciation on Building	11,000	
Interest on Loan	1,700	
Machinery	60,000	
Buildings	70,000	
	6,57,100	**6,57,100**

Solution:

Trading and Profit & Loss a/c of Manianfor the year ending on 30.06.2014

Dr. **Cr.**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Purchases	2,97,400	By Sales	4,30,000
To Wages	27,500		
To Carriage Inwards	5,400		
To Factory Rent	9,600		
To Gross Profit c/d	90,100		
	4,30,000		**4,30,000**
To Insurance	4,500	By Gross Profit b/d	90,100
To Discount allowed	3,000	By Discount received	2,500
To Advertisement	7,500		
To Salaries	46,400		
To Bad debts	1,500		
To Sundry Expenses	2,000		
To Depreciation on Machinery	7,000		
To Depreciation on Building	11,000		
To Interest on Loan	1,700		
To Net Profit	8,000		
	92,600		**92,600**

Balance Sheet of Manianas on 30.06.2014

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	1,20,000		Closing Stock		37,600
Add: Net Profit	8,000		Bills Receivable		14,000
	1,28,000		Debtors	42,000	
Less: Drawings	7,500	1,20,500	**Less:** Provision		
Creditors		27,000	for Bad debts	3,500	
Bills Payable		8,000		38,500	
Bank Loan		60,000	**Less:** Provision		
Out Standing			for Discount on		
Wages		5,600	debtors	500	38,000

			Buildings		70,000
			Machinery		60,000
			Unexpired Insurance		1,500
		2,21,100			**2,21,100**

Problem: 13

From the following Trial Balance and adjustments given, Prepare the Final Accounts on 31.3.2015

Debit Balance	Rs.	Credit Balance	Rs.
Drawings	20,000	Capital	2,00,000
Buildings	50,000	Loan @ 12%	30,000
Furniture	7,000	Sales	2,00,000
Motor Van	77,000	Commission Received	5,000
Rent Paid	1,800	Sundry Creditors	30,000
Purchases	1,20,000		
Stock (1.4.2014)	50,000		
Salaries	30,000		
Wages	11,000		
Insurance Premium	2,000		
Sundry Debtors	56,000		
Bank Balance	40,200		
	4,65,000		**4,65,000**

Adjustments:

a) Stock on 31.3.2015 Rs.30,000
b) Wages Outstanding Rs.500
c) ¼ of insurance is prepaid
d) Provide for outstanding interest on Loan**.**

Solution:

Trading and Profit and Loss a/c for the year ended 31.3.2015

Dr. **Cr.**

Particulars	**Amount Rs.**	**Amount Rs.**	**Particulars**	**Amount Rs.**	**Amount Rs.**
To Opening Stock		50,000	By Sales		2,00,000
To Purchases		1,20,000	By Closing Stock		30,000
To Wages	11,000				
Add: Outstanding Wages	500	11,500			
To Gross Profit c/d		48,500			
		2,30,000			**2,30,000**

To Interest		1,800	By Gross Profit b/d		48,500
To Salaries		30,000	By Commission Received		5,000
To Insurance	2,000				
Less: 1/4th prepaid	500	1,500			
To Interest on Loan		3,600			
To Net profit		16,600			
		53,500			**53,500**

Balance Sheet as on 31.3.2015

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	2,00,000		Bank		40,200
Add: Net Profit	16,600		Debtors		56,000
	2,16,600		Building		50,000
Less: Drawings	20,000	1,96,600	Furniture		7,000
Loan	30,000		Motor Van		77,000
Add:			Closing Stock		30,000
Outstanding Interest on Loan	3,600	33,600	Prepaid Insurance		500
Sundry Creditors		30,000			
Out Standing Wages		500			
		2,60,700			**2,60,700**

Problem: 14

The following is theTrail Balance of Ravi as on 31.3.2014. Prepare the final accounts.

Particulars	Debit Rs.	Particulars	Credit Rs.
Drawings	10,000	Capital	1,00,000
Buildings	25,000	Loan from wife@ 12% Interest p.a.	15,000
Furniture	7,000	Sales	1,00,000
Motor Van	35,000	Commission Received	2,500
Interest paid on Loan from Wife	900	Sundry Creditors	15,000
Purchases	60,000		
Stock (1.4.2013)	25,000		
Salaries	15,000		
Wages	5,500		
Insurance Premium	1,000		
Sundry Debtors	28,000		

Cash at Bank	20,100		
	2,32,500		**2,32,500**

Adjustment:

1. Value of Stock on 31.3.2014 Rs.30,000
2. Outstanding wages Rs.500.
3. 1/4 of insurance is prepaid
4. Allow interest on capital @ 107 p.a.
5. Depreciate building @ 3% furniture 10% and Motor van at 8%
6. Provide for outstanding interest on Loan.

Solution:

Trading and Profit & Loss a/c of Ravi for the year ended 31.3.2014

Dr. **Cr.**

Particulars	**Amount Rs.**	**Amount Rs.**	**Particulars**	**Amount Rs.**	**Amount Rs.**
To Opening Stock(1.4.2013)		25,000	By Sales		1,00,000
To Purchases		60,000	By Closing Stock		30,000
To Wages	5,500				
Add: Outstanding Wages	500	6,000			
To Gross Profit c/d		39,000			
		1,30,000			**1,30,000**
To Salaries		15,000	By Gross Profit b/d		39,000
To Insurance Premium	1,000		By Commission Received		2,500
Less: Insurance Prepaid	250	750			
To Interest Paid	900				
Add: Outstanding Interest	900	1,800			
To Interest on Capital		107			
To Depreciation:					
Building 3%	750				
Furniture 10%	700				
Motor Van 8%	2,800	4,250			
To Net profit		19,593			
		41,500			**41,500**

Balance Sheet as on 31.3.2014

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	1,00,000		Building	25,000	
Add: Net Profit	19,593		**Less:**		
	1,19,593		Depreciation	750	24,250
Add: Interest on			Furniture	7,000	
Capital	107		**Less:**		
	1,19,700		Depreciation	700	6,300
Less: Drawings	10,000	1,09,700	Motor Van	35,000	
			Less:		
Loan from wife		15,000	Depreciation	2,800	32,200
Outstanding			Prepaid		
Interest		900	Insurance		250
Sundry			Cash at Bank		20,100
Creditors		15,000	Debtors		28,000
Outstanding			Stock		30,000
Wages		500			
		1,41,100			**1,41,100**

Problem:15

Balance extracted from the Ledger of Mr. Murugan on 31.12.2014 is as follows:

Particulars	Amount Rs.
Capital	82,000
Sundry Debtors	14,500
Sundry Creditors	6,300
Cash	540
Bank Balance	12,630
Purchases	1,40,675
Sales	2,58,780
Returns Inwards	2,680
Returns Outwards	1,500
Salaries	15,000
General Expenses	13,000
Wages	20,480
Power and Fuel	4,730
Carriage	5,240
Stock (1.1.2014)	25,760
Buildings	30,000
Land	20,000
Machinery	20,000

Goodwill	7,500
Insurance	600
Drawings	15,245

Make the following adjustments and prepare the Trading and Profit and Loss account for the year ended 31.12.2014 and the Balance Sheet as on that date.

1. Closing Stock on 31.12.2014 Rs.26,800
2. Depreciation on Machinery at 10%
3. Outstanding Salary for the month of December Rs.1,500
4. Provision for bad debts at 5% on debtors.
5. Unexpired Insurance Rs.170

Solution:

Trading and Profit & Loss a/c of Mr. Muruganfor the year ended 31.12.2014

Dr. **Cr.**

Particulars	Amount Rs.	Amount Rs.	Particulars	Amount Rs.	Amount Rs.
To Opening Stock		25,760	By Sales	2,58,780	
To Purchases	1,40,675		**Less:** Return Inwards	2,680	2,56,100
Less: Return Outwards	1,500	1,39,175	By Closing Stock		26,800
To Wages		20,480			
To Power and Fuel		4,730			
To Carriage		5,240			
To Gross Profit c/d		87,515			
		2,82,900			**2,82,900**
To Salaries	15,000		By Gross Profit b/d		87,515
Add: Outstanding Salaries	1,500	16,500			
To General Expenses		13,000			
To Insurance	600				
Less: Unexpired Insurance	170	430			
To Depreciation Machinery 10%		2,000			
To Provision for					

Bad debts 5%		725			
To Net profit		54,860			
		87,515			**87,515**

Balance Sheet of Muruganas on 31.12.2014

Liabilities	Amount Rs.	Amount Rs.	Assets	Amount Rs.	Amount Rs.
Capital	82,000		Building		30,000
Add: Net Profit	54,860		Land		20,000
	1,36,860		Machinery	20,000	
Less: Drawings	15,245	1,21,615	**Less:**		
Outstanding			Depreciation	2,000	18,000
Salaries		1,500	Goodwill		7,500
Sundry			Prepaid		
Creditors		6,300	Insurance		170
			Cash		540
			Bank balance		12,630
			Sundry Debtors	14,500	
			Less: Provision		
			Bad debts	725	13,775
			Stock		26,800
		1,29,415			**1,29,415**

SUMMARY

Usually, at the end of the accounting period final accounts are prepared with the help of Trial balance. Final account consist of 1) Trading and profit and loss account and 2) Balance sheet. Trading account shows gross profit or gross loss. Profit and Loss account reveals Net profit or net loss. Balance sheet shows all asset and liabilities. Balance sheet shows the financial position of the business. Further the manufacturing concern prepares a manufacturing account to ascertain the cost of goods produced. At the time of preparing final accounts, a number of items are to be adjusted. Adjustments entries can be passed in the journal for each item of adjustment.

THEORY QUESTIONS

1. Explain the objectives of Preparing Final account.
2. Explain the objectives of preparing a Profit and Loss account.
3. Differentiate Trading account with Profit Loss account.
4. What are closing entries?
5. What is a Balance Sheet? Explain the differences between Trading and Profit and loss and Balance Sheet
6. What are adjustment entries?
7. What areoutstanding Expenses?

8. What is accrued Income?
9. What is prepaid expense?
10. What is Income received in advance?
11. What is a bad debt?
12. Write short notes on provision for bad and doubtful debts.
13. What are the uses and limitations of Balance Sheet?
14. How do you deal with the Loss ofstock byfire at the time of preparation of final accounts.
15. Discuss with examples the adjustments that may be made at the time of preparation of final accounts.

EXERCISES

1. From the following, Calculate Gross Profit

	Rs.
Opening Stock	1,00,000
Purchases	1,20,000
Carriage Inwards	10,000
Sales	5,00,000
Closing Stock	50,000

(Ans: Gross Profit 3,20,000)

2. From the information given below, prepare trading account

	Rs.
Opening Stock	1,00,000
Purchases	1,50,000
Purchases returns	25,000
Direct expenses	10,000
Carriage inwards	5,000
Sales	4,00,000
Closing Stock	50,000

(Ans: Gross Profit 2,10,000)

3. From the following information, ascertain gross profit and net profit

	Rs.		**Rs.**
Stock at start	2,400	Carriage inwards	524
Purchases	15,205	Manufacturing wages paid	2,800
Sales	20,860	Manufacturing wage owing	96
Closing Stock	3,840	Loss due to fire	1,000
Return Outwards	185	Indirect Expenses	200
Return Inwards	860		

(Ans: Gross Profit 3,000; Net Profit 1,800)

4. From the following particulars, calculate gross profit.

	Rs.
Opening Stock	30,000
Purchases	21,000
Purchases returns	1,000
Sales	78,000
Direct Expenses	5,000
Closing Stock	12,000

(Ans: Gross Profit 35,000)

5. From the following prepare profit and loss account

	Rs.
Gross profit	1,00,000
Salary paid	5,000
Rent paid	2,000
Discount received	1,000
Depreciation written off	500
Discount paid	100
Repair Expenses	1,500

(Ans: Net Profit 91,900)

6. From the following information prepare balance Sheet:

	Rs.
Capital	4,00,000
Furniture	1,00,000
Bank balance	50,000
Cash in hand	75,000
Profit	25,000
B/R	50,000
B/P	40,000
Sundry Debtors	30,000
Sundry Creditors	50,000
Goodwill	60,000
Building	1,50,000

(Ans: Balance Sheet 5,15,000)

7. The following is the trial balance of a person on 31st December 2010

Debit	Rs.	Credit	Rs.
Cash in hand	540	Sales	98,780
Cash at bank	2,630	Returns Outwards	500
Purchases	40,675	Capital	71,000
Returns Inwards	680	Creditors	6,300
Wages	10,480		

Fuel	4,730		
Carriage Outwards	3,200		
Carriage Inwards	2,040		
Opening Stock	5,760		
Premises	30,000		
Land	10,000		
Machinery	20,000		
Patents	7,500		
Salaries	15,000		
Sundry Expenses	3,000		
Insurance	600		
Drawings	5,245		
Debtors	14,500		
	1,76,580		**1,76,580**

Closing Stock Rs.16,800.

Prepare trading, P&L account and Balance Sheet.

(Ans: Gross Profit 51,715; Net profit 29,915, B/S 1,01,970)

8. From the trial balance given below, prepare final accounts for the year ending 31.3.2013

Trial Balance

Debit	Rs.	Credit	Rs.
Opening Stock	9,300	Bank Interest	200
Repairs	310	Purchases return	440
Machinery	12,670	Creditors	12,370
Furniture	1,330	Sales	20,560
Office Expenses	750	Capital	24,500
Trade Expenses	310	Loan	5,000
Land and Building	15,400		
Bank Charges	50		
Purchases	15,450		
Sales Return	120		
Advertisement	500		
Cash in hand	160		
Cash at Bank	5,870		
Sundry expenses	150		
Insurance	500		
Travelling expenses	200		
	63,070		**63,070**

Adjustments:

i) Closing Stock on 31.3.2011 Rs.7,585

ii) Prepaid insurance Rs.250

iii) Depreciate land and building @ 5%, Plant and Machinery @ 10%

(Ans: Gross Profit 3,715; Net Loss 625, B/S Total 41,228)

9. From the following trail balance prepare trading and profit and loss account for the year ended 31.12.2014 and a balance sheet as on that date.

Trail Balance as on 31.12.2010

Particulars	Debit Rs.	Credit Rs.
Capital		80,000
Sales		50,000
Purchases	30,000	
Salaries	4,000	
Rent	3,000	
Insurance	600	
Drawings	10,000	
Machinery	56,000	
Bank	9,000	
Cash	4,000	
Stock	10,400	
Debtors	5,000	
Creditors		2,000
	1,32,000	**1,32,000**

Adjustments:

(i) Closing stock Rs.9,800

(ii) Salaries Outstanding Rs.600

(iii) Rent paid in advance Rs.400

(iv) Depreciate Machinery at 10%

(v) Bad debts written off Rs.500

(Ans: GP19,400; NP 5,500, B/S Total 78,100)

10. From the Trail Balance given below, prepare trading account and profit and loss account for the year ended 31.3.2013 the balance sheet as on that date:

Debit	Rs.	Credit	Rs.
Stock (1.4.2012)	55,000	Discount received	200
Purchases	1,92,500	Interest	1,000
Wages	12,500	Sales	2,93,500
Carriage Inwards	4,000	Bills Payable	18,500
Insurance	3,500	Sundry Creditors	93,250
Bill Receivable	22,500	Capital	1,93,500
Sundry debtors	1,50,000		
Commission	4,000		
Interest	3,500		

Trade expenses	3,450		
Furniture (1.4.2012)	6,000		
Cash at Bank	42,250		
Rent & Rates	12,750		
Office expenses	8,000		
Buildings	20,000		
Plant and Machinery	60,000		
	5,99,950		**5,99,950**

Adjustments:

i) Closing Stock on 31.3.2013 Rs.50,000

ii) Outstanding expenses on 31.3.2013: Rent Rs.200

iii) Prepaid InsuranceRs.100

iv) Provide Rs.600 for doubtful debts

v) Depreciate: Building 2 ½ ; Machinery 10%

(Ans: GP 79,500; NP 38,300; B/S Total 3,43,750)

CHAPTER 9

ACCOUNTS OF NON- PROFIT ORGANISATION

INTRODUCTION

You have learnt the procedure involved in recording the business transaction in the journal, posting them into the ledger, preparation of trial balance and preparation of final accounts of a sole trading concern. In this chapter, you are going to learn the preparation of final accounts of Non-profit organisation.

Non-profit organisation's main objective is to promote the interest of the public and not to earn profit. Clear distinction between capital and revenue is important for the ascertainment of income of the non-profit organisation and their financial position. Hence, it is important to know whether a particular expenditure or receipt is of a capital nature or of a revenue nature. The final accounts of non-profit organisation consists of (1) Receipts and payment account; (2) Income and Expenditure Account and (3) Balance sheet. In this chapter, you are going to learn the basic framework of final account of non-profit organisations.

OBJECTIVES

After studying this unit you should be able to

- Explain the importance of distinction between capital and revenue.
- Identify correctly whether an expenditure / receipt is of a capital or revenue nature.
- Differentiate Receipts and Payments a/c from Income and Expenditure a/c.

CAPITAL EXPENDITURE

The term capital expenditure consist of expenditure incurred to

a) Increase the quantity of fixed assets.
b) Increase quality of fixed assets.
c) Results in replacement of fixed assets.

Examples

1) Expenditure resulting the purchases of fixed assets
   Example: Land, Building
2) Expenditure resulting in extension or improvement of fixed assets.
   Example: Amount spent of seating accommodation in the cinema theatre.
3) Expenditure in connection with the purchase, receipts / erection of the fixed assets.
4) Expenditure incurred for acquiring the business.
   Example: Goodwill, Copy Right, etc.,

REVENUE EXPENDITURE

An expenditure which benefits the current period is called revenue expenditure.

Examples

- Expenses incurred in the normal course of business.
  Example: Expenses of administration, manufacturing, selling, etc.,
- Expenses incurred to maintain the business.
- Cost of goods purchased
- Depreciation of fixed assets.

DEFERRED REVENUE EXPENDITURE

A heavy expenditure of revenue nature incurred for getting benefit over a number of years is classified as deferred revenue expenditure.

Examples

Heavy advertisement expenses, preliminary expenses, discount on issue of share and debenture.

Distinction between Capital Expenditure, Revenue Expenditure and Deferred Revenue Expenditure

No.	Capital Expenditure	Revenue Expenditure	Deferred Revenue Expenditure
1.	Capital expenditure is meant for enduring benefit beyond accounting year – last for a long time.	Revenue expenditure is the expenditure the benefit of which is consumed during the current year only – lasts only for the current year.	Deferred revenue expenditure is the expenditure the benefit of the which is continued for more than one accounting period – lasts for more than one accounting period.
2.	It represents unexpired cost	It represents expired cost	
3.	It relates to the acquisition of fixed assets	It relates only to the acquisition of current assets	It relates to heavy revenue expenditure
4.	It may be treated as non-recurring expenditure	It is treated as a recurring expenditure	It is treated as non-recurring expenditure
5.	It helps to increase the earning capacity of the business and also reduces the operating cost.	It helps to earn existing revenues.	It ensures the application of modern concept of matching cost against revenue.

6.	Capital expenditure is transferrable., i.e. it can be disposed off and transferred for money or money's work	Revenue expenditure is not transferable	Deferred revenue expenditure is also not transferable
7.	It is associated with property right belonging to the entity	In revenue expenditure there is no such right	In deferred revenue expenditure also there is no such right

CAPITAL AND REVENUE RECEIPTS

Receipts refer to amounts received by a business. i.e. cash inflows. Receipts may be classified as Capital Receipts and Revenue Receipts. It is necessary to note this distinction clearly because only the revenue receipts are taken to the Profit and Loss Account or Income and Expenditure and not the capital receipts.

CAPITAL RECEIPTS

Capital Receipts are the amounts received in the form of (a) additional capital introduced in the business, (b) loans received, and (c) sale proceeds of fixed assets. You are aware that a loan taken by the business is repayable sooner or later. Similarly, additional capital received represents an increase in the proprietor's claim over the business assets. Thus these two items represent the liabilities of the business and obviously are not incomes or revenues. These are capital receipts and should be treated as such. The sale proceeds of a fixed assets are also treated as a capital receipt because the amount received is not revenue earned in the normal course of business. The capital receipts may either increase the value of liabilities or reduce the value of assets. The capital receipt will not be shown in the Profit or loss and Income and Expenditure.

REVENUE RECEIPTS

Revenue receipts are the amounts received in the normal and regular course of business. They take the form of (a) sale proceeds of goods, and (b) income such as interest earned, commission earned, rent received, etc. These receipts are on account of some services rendered by the business and as such they are not repayable. All revenue receipts are treated as incomes and will be shown on the credit side of the profit and loss account (or) Income and Expenditure Account.

Let us illustrate the above concepts with the following examples.

Illustration: 1

State with giving reasons, whether the following items of expenditure are capital or revenue

1. Carriage paid on goods purchased.
2. Wages of workman employed for setting up new machinery
3. Replacement cost of a workout part of pant.
4. Repairs to furniture purchased on second hand.
5. Damages paid on account of a contract to supply certain goods.

Solution

1. The carriage paid on goods purchased is revenue expenditure as it has been incurred in connection with the purchase of goods meant for resale.
2. The wages of workmen employed for setting up new machinery are capital expenditure since they have been incurred in the acquisition of a fixed asset.
3. The replacement cost of workout part of plant is revenue expenditure, because it is the cost of maintenance of fixed asset. It does not in any way improve the asset or add its value.
4. Repairs to furniture purchased on second hand are capital expenditure and a part of the cost of furniture as they are necessarily incurred for placing furniture in a serviceable condition.
5. Damages paid on account of the breach of contract to supply certain goods are revenue expenditure because they are expense incurred in the ordinary course of trading.

Illustration: 2

Which of the following expenditures are capital, revenue and deferred revenue expenditure (Give Reasons)

a) Cost of air-conditioning the office of the general manager.
b) Cost of overhauling and painting a second hand truck newly purchased.
c) Cost of the annual taxes paid and the annual insurance premium paid on the truck mentioned above.
d) Wages paid to workers for installation of machinery.
e) Cost of making more exits in a cinema hall under orders of the Government.
f) Cost of re-decorating a cinema hall.
g) Cost of putting up a gallery in a theater hall.
h) Cost of acquiring the goodwill of an old firm.
i) Cost of heavy advertisements for a new product and removal of works to a new and better site.
j) Temporary rooms constructed for storing raw materials for the construction of a big building.
k) A machinery costing Rs. 5,000 has to be sold. It realizes Rs. 3,000. A new machine is purchased for Rs. 9,000

Solution:

a) This is capital expenditure because the benefit of this expenditure will be available for a number of years. The machine which has been installed will be there and can be disposed off whenever desired.

b) When a secondhand machine is purchased, all expenditure incurred in the beginning to make it fit for working is treated as capital expenditure. The value of the machine is increased by the amount spent. Therefore, the cost of overhauling and painting the truck will be capital expenditure.

c) Annual taxes and annual premium paid on the truck are revenue expenditure because they do not add to the value of the truck and their benefit will be exhausted within the year.

d) This is capital expenditure because it is necessary to put the machine in working condition. (see above (b))

e) Making more exits in a cinema hall does not increase the capacity of the hall and, therefore, it should be treated as revenue expenditure.

f) Cost of re-decorating a cinema hall is also not capital expenditure because it does not add to the capacity of the hall. But the cost is fairly heavy and benefit will be there for a number of years. Therefore, the cost of redecoration should be treated as deferred revenue expenditure.

g) When a new gallery is put up, it will increase the number of sales in (or capacity or) the hall. Therefore, this cost should be treated as capital expenditure.

h) This is capital expenditure because the use of that firm’s name will benefit the purchaser for a long time.

i) This expenditure is heavy but not of capital nature because no new asset is acquired. But since the benefit of the expenditure will be available for a number of years, it should be treated as deferred revenue expenditure.

j) The cost of construction of temporary room should be treated as capital expenditure because it is necessary for the construction of the main building. The cost of the rooms will be added to the cost of the building.

k) There is a loss of Rs. 2,000 on sale of the old machinery. This is a revenue loss. Rs. 9,000 has spent of acquiring a new machinery. It is capital expenditure.

PREPARATION OF FINAL ACCOUNTS

Final account comprise of

1. Income and expenditure a/c
2. Balance sheet

They are prepared with the help of the following:

a) B/S of the last year

b) Receipts and Payment a/c and

c) Additional information

1. Receipts and Payment a/c

This a/c shows the summary of cash transactions made during the particulars period. It is just like a cash book.

Features of Receipts and Payment a/c

a) The receipts and payments account is nothing but a summary of the cash book.
b) It starts with the opening balance of cash in hand and at bank and ends with the balance of cash in hand and at bank at the end of the period.
c) It records all cash receipts and cash payments irrespective of the face whether they are capital or revenue or whether they belong to the pervious , present or future year.
d) It does not take cognizance of outstanding amount of receipts or payments, either at the beginning or end of the period. In other words, only actual receipts and payments are entered.
e) It does not show either the final result to the effect whether the total income is more than expenditure or vice versa or the financial position but only shows the cash position.

2. Income and Expenditure a/c

It is the summary of incomes and expenditure of complete year. It is just like that of P & L a/c. The difference between the debit side and credit side of income & expenditure account give the excess of income over expenditure and vice versa.

Income meaning

i) It is a recurring nature and
ii) It is not earmarked for a particular use

Expenditure meaning

The expenditure is useful only for the current year. In other words no use can be derived out of it in the future period.

Features of Income and Expenditure

a) It is prepared at the end of the specific financial period, usually one year, to find out the surplus or deficit.
b) It is a nominal account.
c) It takes into account both cash and non-cash items such as depreciation, provision for doubtful debts, etc.,
d) It excludes both capital expenditure and income.
e) In considers only current year’s incomes and expenses.
f) It follows matching concept by matching expenses against the revenues of the period concerned.

Receipts and Payments a/c Vs Income and Expenditure a/c

No.	Receipts and Payment a/c	Income and Expenditure a/c
1.	It is a real account	It is a nominal a/c
2.	It is just like that of cash a/c	It is just like that the Profit and Loss a/c
3.	Receipts are recorded in the debit side	Expenditure are recorded in the debit side
4.	Payment are recorded in credit side	Income are recorded in the credit side
5.	It starts with opening cash	It starts with no opening balance
6.	It ends with closing cash	It ends with excess of income over expenses and vice versa.
7.	It records both capital and revenue items.	It records only revenue item.

TREATMENT OF IMPORTANT ITEMS

1. Entrance fees

The entrance fee is paid by a person at the time of becoming a member. It is treated as revenue receipt. If there is a specific instruction to treat the entire or the portion of the amount as capital, it will be taken to balance sheet.

2. Legacy

It is the amount which a non-trading concern will received as per the will of a deceased person. It is like a donation. The amount is directly added to capital fund in the balance sheet.

3. a) Donation

Donation is the amount received by way of gift. It is not an income. It will be taken to the balance sheet and added to the capital fund.

b) Donation for a specific purpose

Whenever donation is received for a specific purpose (eg) donation for building donation for library, it is capitalized and it taken to the liability side of the balance sheet.

4. Sale of old furniture

Sale of old furniture appears in the receipts and payment account. It is not taken to income and expenditure account. But any income or loss on the sale of asset is taken to the income and expenditure account.

5. Life membership fee

It will be taken to the balance sheet and added to the capital fund.

6. Sale of old news papers / obsolete items

It will be treated as income.

7. Treatment of items of expenses and income relating to specific fund

If there is a specific fund, then income on the fund will be added to the fund and expenses deducted from such fund on the liability side of the balance sheet (prize distribution, fund, building fund).

8. Payment to honorarium

It is the amount paid to the person who is not the employee of the organisation. It is treated as expenditure.

Illustration: 3

Subscription outstanding on 1.1.2015 Rs. 1,500

Subscription received during 2015 Rs. 16,500

Subscription received in advance on 1.1.2015 Rs. 2,500

Subscription outstanding on 31.12.2015 Rs. 3,500

Subscription received in advance Rs. 6,000 on 31.12.2015

How much to be created to Income & Expenditure account for 2015?

Solution:

Particulars	**Amount Rs.**	**Amount Rs.**
Subscription received during 2015		16,500
Add:		
Subscription outstanding on 31.12.2015	3,500	
Subscription received in advance on 1.1.2015	2,500	6,000
		22,500
Less:		
Subscription outstanding on 1.1.2015	1,500	
Subscription received in advance on 31.12.2015	6,000	7,500
Amount created to Income & Expenditure account		**15,000**

Illustration: 4

Subscription received during 2014 Rs. 25,000

1.1.2014	Subscription received in advance Rs. 3,000
	Subscription outstanding Rs. 4,000
31.12.2014	Subscription received in advance Rs. 2,000
	Subscription outstanding Rs. 3,000

Show how much subscription to be credited in the income & expenditure a/c

Solution:

Particulars	**Amount Rs.**	**Amount Rs.**
Subscription received during 2014		25,000
Add:		
Subscription outstanding on 31.12.2014	3,000	
Subscription received in advance on 1.1.2014	3,000	6,000
		31,000
Less:		
Subscription outstanding on 1.1.2014	4,000	

Subscription received in advance on 31.12.2014	2,000	6,000
Amount created to Income & Expenditure account		**25,000**

Illustration 5

What amount will be shown in the income and expenditure a/c

Stock of sports materials on 1.1.2015	Rs. 500
Sports materials purchased during 2015	Rs. 1,800
Sale of old sports materials during 2015	Rs. 40
Stock of materials on 31.12.2015	Rs. 200

Solution

Particulars	Amount Rs.	Amount Rs.
Stock of sports materials on 1.1.2015		500
Add:		
Sports materials purchased during 2015		1,800
		2,300
Less:		
Stock of materials on 31.12.2015		200
Amount Debited to Income & Expenditure account		**2,100**

(Note: Sale of old sport materials Rs. 40 is credited to income & expenditure a/c)

Illustration: 6

Prepare Income and Expenditure account form the following Receipts and Payment account of National Sports Club for the year ending 31st December 2015

National Sports Club

Receipts and payments Account for the year ending 31st December 2015

Receipts	Amount Rs.	Payments	Amount Rs.
To Balance b/d	1,520	By Rent	400
To Subscriptions	6,600	By Sundry expenses	420
		By Postage & Telegram	140
		By Stationery	60
		By Investments	2,000
		By Balance c/d	
		Cash in Bank	4,350
		Cash in hand	750
	8,120		**8,120**

Additional information

1. Subscriptions from members outstanding 31st December 2015, Rs. 400
2. Rent due but not paid on 31st December 2015, Rs. 120

Solution:

National Sports Club

Income and Expenditure account for the period ended 31st December 2015

Receipts		Amount Rs.	Payments		Amount Rs.
To Rent	400		By Subscription	6,600	
Add: Outstanding	120	520	**Add:** Outstanding	400	7,000
To Sundry expenses		420			
To Postage & Telegram		140			
To Stationery		60			
To Surplus (b.f.)		5,860			
		7,000			**7,000**

Illustration: 7

From the following particulars prepare income and expenditure account of the Central Sports Society for the period ending 31st March 2014

Particulars	Received or Paid Rs.	Outstanding on 31.3.2014 Rs.
Subscription from members	4,600	–
Subscription from societies	1,400	200
Gifts received	3,000	–
Interest received	160	–
Committee expenditure		
Executive	1,500	200
Planning	1,440	640
Tournament	420	120
Printing, Postage & Stationary	1,140	160
Office furniture	2,000	–
Investments purchased	3,000	–

Solution

Central Sport Society

Income and Expenditure Account for the year ended 31st March 2014

Expenditure	Amount Rs.	Amount Rs.	Income	Amount Rs.	Amount Rs.
To Committee Expenditure			By Subscription from members		4,600
To Executive	1,500		By Subscription from societies	1,400	
Add: Outstanding	200	1,700	**Add:** Outstanding	200	1,600
To Planning	1,440				
Add: Outstanding	640	2,080	By Gifts received		3,000

To Tournament	420		By Interest		
Add:			received		160
Outstanding	120	540			
To Printing, Postage & Stationary	1,140				
Add:					
Outstanding	160	1,300			
To Surplus (b.f.)		3,740			
		9,360			**9,360**

Illustration: 8

From the following details relating Madras Sports Club for the year ended 31st December 2015, prepare Income and Expenditure account and a Balance sheet.

Receipts	Amount Rs.	Payments	Amount Rs.
To Balance b/d		By Salaries	6,000
Cash	1,075	By Entertainment expenses	6,900
Bank	16,300	By Electricity charges	1,000
To Subscription 2014	1,010	By Telephone charges	1,200
To Subscription 2015	18,900	By Postage	200
To Subscription 2016	900	By Miscellaneous	700
To Donation	7,000	By Stationery	850
To Interest from bank	1,340	By Repairs	400
To Entertainment receipts	2,600	By Creditors for building	
To Telephone rent	900	purchased in 2009	12,000
		By Balance c/d	
		Cash	1,765
		Bank	19,010
	50,025		**50,025**

Additional information

Outstanding subscription for 2015 Rs. 1,100

Interest due on deposit but not received Rs. 200

Outstanding Salary Rs. 200

Capital Fund Rs. 1,06,385, Building Rs. 1,00,000 as on 31.12.2014

Solution:

Madras Cricket Club

Income & Expenditure a/c for the year ended 31st December 2015

Expenditure		Amount Rs.	Income		Amount Rs.
To Salaries	6,000		By Subscription	18,900	

Add: Outstanding 200	6,200	**Add:** Out standing 1,100	20,000
To Entertainment expenses	6,900	By Interest on Bank 1,340	
To Electricity charges	1,000	**Add:** Out standing 200	1,540
To Telephone charges	1,200	By Entertainment receipts	2,600
To Postage	200	By Telephone rent	900
To Miscellaneous	700		
To Stationery	850		
To Repairs	400		
To Surplus (b.f.)	7,590		
	25,040		**25,040**

Balance sheet as on 31 December 2015

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital fund 1,06,385		Interest due on deposit	200
Add: Surplus 7,590	1,13,975	Subscription outstanding	1100
Salary outstanding	200	Cash	1765
Subscription outstanding	900	Bank balance	19010
Donation	7,000	Buildings	1,00,000
	1,22,075		**1,22,075**

Illustration: 9

From the following information related to Mumbai Cricket Club, prepare income and expenditure account for the year ended 31st March 2015 and a balance sheet as at that date. An abstract of cash book for the year is as follows.

Receipts	Amount Rs.	Payments	Amount Rs.
To Opening bank balance	80,000	By Maintenance	50,000
To Members subscription	1,10,000	By Tournament expenses	14,000
To Sale of old balls, bats etc.,	1,000	By Rates & Insurance	4,000
		By Telephone charges	1,000
To Hire of ground	6,000	By Printing & Stationery	2,000
To Members admission fees	6,000	By General charges	1,000
		By Secretary's Honorarium	5,000
To Subscription for tournament	20,000	By Grass seeds	600
		By Bats & balls	14,000
To Donations	2,00,000	By Bank balance	3,31,000
		By Cash balance	400
	4,23,000		**4,23,000**

Additional information

On 1.4.2014 subscription due Rs. 10,000; advance subscription received Rs. 5,000; Stock of bats & balls Rs. 30,000; Printing & Stationery Rs. 4,000. Donation and surplus on account of tournament should be kept in reserve for permanent pavilion.

Subscriptions due on 31.3.2015 Rs. 15,000;Stock of bat & balls Rs. 20,000;Printing& stationery Rs. 1,000;

Capital fund in the beginning is Rs. 1,19,000; Members admission fees is to be treated as capital receipts.

Solution:

Mumbai Cricket Club

Income & Expenditure a/c for the year ended 31st March 2015

Expenditure		Amount Rs.	Income		Amount Rs.
To Maintenance		50,000	By Subscription	1,10,000	
To Rates & Insurance		4,000	**Less:**		
To Telephone charges		1,000	Last year		
To Printing & Stationery			subscription	10,000	
Opening stock	4,000			1,00,000	
Add: Purchase	2,000		**Add:** This year		
	6,000		received in last year	5,000	
Less:				1,05,000	
Closing stock	1,000	5,000	**Add:**		
To General charges		1,000	Outstanding	15,000	1,20,000
To Secretary's			By Sale of old balls, bats		1,000
Honararium		5,000	By Hire of ground		6,000
To Grass seeds		600			
To Bats & balls					
Opening stock	30,000				
Add: Purchase	14,000				
	44,000				
Less:					
Closing stock	20,000	24,000			
To Surplus (b.f.)		36,400			
(transferred to capital fund)					
		1,27,000			**1,27,000**

Mumbai Cricket Club
Balance sheet as on 31st March 2015

Liabilities		Amount Rs.	Assets	Amount Rs.
Capital fund	1,19,000		Cash	400
Add: Admission			Bank	3,31,000
fees	6,000		Stock of printing	
	1,25,000		& stationery	1,000
Add: Surplus	36,400	1,61,400	Stock of	
Reserves			bats & balls	20,000
Donations &			Subscription outstanding	15,000
Surplus				
on Tournament	2,00,000			
Surplus				
(20,000 – 14,000)	6,000	2,06,000		
		3,67,400		**3,67,400**

Illustration: 10

From the following details prepare an Income and Expenditure Account and Balance sheet for the year ending 31st December 2015

Receipts and Payment Account

Receipts		Amount Rs.	Payments	Amount Rs.
To Balance b/d		250	By Salaries	1,200
To Subscription for			By General expenses	300
2014	250		By Electricity	200
2015	1,000		By Books	100
2016	200	1,450	By News papers	400
To Sale of old furniture			By Postage	50
(Cost Rs. 100)		60	By Furniture	250
To Rent received		740	By Balance c/d	500
To Entertainment gains		400		
To Sale of news papers		100		
		3,000		**3,000**

Additional information

1) The club has 50 members each paying an annual subscription of Rs. 25. Subscription outstanding on 31st December 2014 were Rs. 300
2) On December 31, 2015 salaries outstanding amounted to Rs. 100. Salary paid included Rs. 100 for the year 2014
3) On 1.1.2015 the club owned land and building valued at Rs. 10,000; furniture Rs. 600 and books Rs. 500

Solution:

Income & Expenditure a/c for the period ended 31st December 2015

Expenditure		Amount Rs.	Income		Amount Rs.
To Salaries	1,200		By Subscription	1,000	
Add: Outstanding			**Add:** Outstanding	250	1,250
(31.12.15)	100		By Rent received		740
	1,300		By Entertainment gains		400
Less: Outstanding			By Sale of news papers		100
(1.1.15)	100	1,200			
To General expenses		300			
To Electricity		200			
To News papers		400			
To Postage		50			
To Loss on sale of Furniture (100 – 60)		40			
To Surplus (b.f.) (transferred to capital fund)		300			
		2,490			**2,490**

Balance sheet as on 01.01.2015

Liabilities	Amount Rs.	Assets	Amount Rs.
Salaries outstanding	100	Cash	250
Capital fund (b.f.)	11,550	Books	500
		Furniture	600
		Land & Building	10,000
		Subscription outstanding	300
	11,650		**11,650**

Balance sheet as on 31.12.2015

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital fund	11,550		Cash		500
Add: Surplus	300	11,850	Books	500	
Salary outstanding		100	**Add:** Purchases	100	600
Subscription received in advance		200	Furniture	600	
			Add: Purchases	250	
				850	
			Less: Sales	100	750
			Land & Building		10,000

		Subscription outstanding 2015	250
		Subscription outstanding 2014	50
	12,150		**12,150**

FINAL ACCOUNT OF PROFESSIONAL PEOPLE

Professional people like Doctors, Lawyers, etc., also prepare Income and Expenditure Account to ascertain their net income for a particular period. They record their cash transaction in the receipts and payments account. The income and expenditure account is prepared as usual by the professional people with an exception to their outstanding incomes. Professional people prepare their accounts on cash basis. i.e., all outstanding expenses are considered but outstanding incomes are to be ignored. As a matter of fact they cannot file a suit for collecting the outstanding fees. The account prepared by them is known as Receipts and Expenditure Account and not Income and Expenditure Account. The outstanding income is created as a reserve by debiting the receipts and expenditure account, after adding the accrued income with the income already received.

Illustration: 11

Given below are receipts and payments account and income and expenditure account for a club for the year ending 31st December 2015

Receipts and payments account for the year ending 31st December 2015

Receipts	Amount Rs.	Payments	Amount Rs.
To Balance b/d	4,000	By Salaries	6,000
To Endowment	2,000	By Advertisement	1,200
To Subscription	10,200	By Provision	6,800
To Entrance fees	800	By Printing & Stationery	700
To Donation for books	1,300	By Bank	1,000
To Entertainment	4,000	By Sports material	2,800
To Sale of furniture (book value Rs. 800)	700	By Creditors (2014)	1,300
		By Investments 4% at 96 purchased on 1.7.2014	1,920
		By Balance c/d	1,280
	23,000		**23,000**

Income and Expenditure Account for the year ending 31st December 2015

Expenditure	Amount Rs.	Income	Amount Rs.
To Loss on sale of furniture	100	By Subscription	10,000
To Salaries	6,700	By Entrance fees	400

To Advertisement	1,000	By Interest on investments	
To Audit fees	300	at 4 p.c on Rs. 2,000	80
To Provision	6,000	By Entertainment	4,000
To Printing & stationery	750	By Deficit (Excess of	
To Sports material	2,000	expenditure over income)	2,370
	16,850		**16,850**

Prepare balance sheet both in the beginning and at the end.

Solution:

Balance sheet as on 1st January 2015

Liabilities	Amount Rs.	Assets	Amount Rs.
Creditors for investments	1,920	Cash in hand	4,000
Creditor	1,300	Investments	1,920
Capital fund	3,500	Furniture	800
	6,720		**6,720**

Balance sheet as on 31stDecember2015

Liabilities		Amount Rs.	Assets	Amount Rs.
Salary outstanding		700	Cash in hand	1,280
Audit fees outstanding		300	Bank	1,000
Printing & stationery		50	Advertisement prepaid	200
Endowment fees		2,000	Stock of provision	800
Subscription in advance		200	Stock of sports material	800
Entrance fees		400	Interest accrued	80
Donation for books		1,300	Investments	1,920
Capital fund	3,500			
Less: Deficit	2,370	1,130		
		6,720		**6,720**

Illustration: 12

Dr. Getwell commenced practice in January 2015. His receipts and payment account for the year 2015.

Receipts and Payment Account

Receipts	Amount Rs.	Payments	Amount Rs.
To Capital	6,000	By Furniture	2,000
To Income from visits	8,000	By Equipment	3,000
To Income from dispensing	6,000	By Purchase Drugs	2,000
To Miscellaneous receipts	100	By Compounder's Salary	1,200
		By Rent	600
		By Conveyance	1,000
		By Stationery	200

		By Lighting	150
		By Newspaper	150
		By Investment	6,800
		By Cash balance	3,000
	20,100		**20,100**

Rs. 1,500 were still to be received on account of visits made. Salary of Rs. 300 and a bill of stationery for Rs. 100 are outstanding. Stock of drugs on hand was estimated at Rs. 500. Furniture and equipment are subject to depreciation at 5%

Solution:

Expenditure		Amount Rs.	Income		Amount Rs.
To Purchase of drugs	2,000		By Income from visits	8,000	
Less: Closing stock	500	1,500	**Add:** Outstanding	1,500	9,500
To Compounder's salary	1,200		By Income from dispensing		6,000
Add: Outstanding	300	1,500	By Miscellaneous receipts		100
To Rent		600			
To Conveyance		1,000			
To Stationery	200				
Add: Outstanding	100	300			
To Lighting		150			
To Newspaper		150			
To Depreciation Furniture (5%)	100				
Equipment (5%)	150	250			
To Reserve for outstanding fees		1,500			
To Surplus (b.f.)		8,650			
		15,600			**15,600**

Balance sheet as on 01.01.2015

Liabilities		Amount Rs.	Assets		Amount Rs.
Expenses outstanding			Cash in hand		3,000
Compounder's salary		300	Investments		6,800
Stationery		100	Equipment	3,000	
			Less:		
Capital	6,000		Depreciation	150	2,850
Add: Surplus	8,650	14,650	Furniture	2,000	

		Less: Depreciation	100	1,900
		Stock of drugs		500
		Outstanding fees	1,500	
		Less: Reserve	1,500	Nil
	15,050			**15,050**

SUMMARY

Trading concerns used to prepare final accounts, to know the business results for a given period and the financial position on a particular date. Non-trading concerns also prepare final accounts. But the style of maintaining and recording transactions is entirely different from Trading concerns. These institutions do not prepare profit and loss account. Instead, they prepare Income and Expenditure Account which shows "Excess of Income" or "Excess of Expenditure". In non-trading concerns, source of income come from member's subscription, donations, income from special programme, entrance fee etc., To maintain these concerns, they have to meet certain expenses like salaries, wages, maintenance charges, fees, etc. The difference between Income and Expenditure is 'Excess of Income over Expenditure' or vice versa.

Non-profit organisations prepare receipts and payment account. Actual receipts and payments irrespective of time and nature are recorded in this account. It is a summary of all cash transactions took place in a given period. The account is useful for the preparation of Income and Expenditure account and Balance sheet. Like trading concerns, they also prepare balance sheet to shown the financial position on a particular date.

Professional people like Doctors, Lawyers, etc., prepare Receipts and Expenditure account, instead of Income and Expenditure account, in which outstanding incomes are ignored. They maintain their books under cash system.

THEORY QUESTIONS

1. What do you mean by non-trading concern?
2. Write short notes on 'Surplus' and 'Deficit'.
3. What is capital fund?
4. Explain Receipt and Payment account.
5. Explain Income and Expenditure account.
6. What are the features of income and expenditure account?
7. Distinguish between receipts and payment account and income and expenditure account.
8. How will you prepare an income and expenditure account for a given Receipt and Payment account?
9. Explain the accounting treatment of

   a) Entrance fees b) Life membership fee

   c) Legacy d) Donation and

e) Receipt for a specific fund

EXERCISES

1. From the following find how much is to be shown in Income and Expenditure account for the year ending 31.12.2015 for subscriptions.

	Rs.
Subscription received during the year as per receipts and payments account	28,680
Subscription outstanding on 1.1.2015	2,400
Subscription outstanding on 31.12.2015	3,000
Subscription received in advance on 1.1.2015	1,800
Subscription received in advance on 31.12.2015	1,080

(Subscription received to be shown in income& expenditure a/c Rs. 30,000)

2. What amount will be shown in the income and expenditure?

Stock of sports goods as on 1.1.2014	Rs. 1,000
Stock of sports goods as on 31.12.2014	Rs. 400
Sports goods purchased during 2014	Rs. 3,600
Old goods sold during 2014	Rs. 80

(Amount spent on sport good Rs.4,200)

Note: Sale of old sports goods Rs. 80 to be credited to income and expenditure account

3. The following is the receipts and payments account of the Delhi Sports Club for the year ending 31.12.2010.

Receipts and Payment Account

Receipts	Amount Rs.	Payments	Amount Rs.
To Balance 1.1.2010	300	By Rent	5,200
To Entrance fees	550	By Stationery	3,068
To Subscriptions		By Wages	5,330
2009	200	By Billiards Table	3,900
2010	16,900	By Repaid and Renewals	806
2011	300	By Interest	1,500
Locker rent	500	By Balance 31.12.2010	2,396
Special subscriptions			
for governor's party	3,450		
	22,200		**22,200**

Locker rent Rs. 60 referred to 2009 and Rs. 90 is still owing. Rent Rs. 1,300 pertaining to 2009 and Rs. 1,300 is still due. Stationery expenses Rs. 312 related to 2009, still owing Rs. 364. Subscription unpaid for 2010 Rs. 468. Special subscriptions for governor's party outstanding Rs. 550.

You are required to prepare the Income and Expenditure account of the club for the year ending 31.12.2010.

(Surplus Rs. 2,492)

4. Following is the receipts and payments account for an entertainment club for the year ending 31st December 2009.

Receipts	Amount Rs.	Payments	Amount Rs.
To Balance b/d	3,000	By Expenses	200
To Subscriptions		By Salaries	1,200
2008	100	By Music Concert Expenses	1,000
2009	4,000	By Newspaper	240
2010	160	By Municipal Taxes	120
To Sale of Music		By Investments	4,000
Concert Tickets	2,100	By Charity	800
To Donations	1,100	By Electricity	400
To Sale of Old Newspaper	100	By Purchase of furniture	2,000
To Entrance Fees	600	By Balance c/d	1,200
	11,160		**11,160**

Additional Information

1) Municipal taxes amounting to Rs. 120 per annum paid upto 31st March 2010.
2) There are 400 members each paying Rs. 10 as annual subscriptions.
3) Subscriptions still outstanding for 2008 Rs. 120
4) Interest on investment has accrued for five months @ 6%.
5) The book value of building on 1.1.2009 Rs. 10,000

You are required to prepare Income and Expenditure Account for the year ended 31st December 2009 and balance sheet as on that date.

(Surplus Rs. 3,470; Balance Sheet 17,450)

5. Prepare an Income and Expenditure Account for the year ended 31st March 2012 and the balance sheet as on that date of college form the following.

Receipts	Amount Rs.	Payments	Amount Rs.
To Capital on 1.4.2011	6,000	By Pay and Allowance	70,500
To Tuition fees	59,000	By Provident fund contribution	5,540
To Fines	1,000		
To Grants from State Govt.	30,000	By Printing & Stationery	700
To Interest on securities	300	By Books for Library	4,600
To Rent from use of Hall	1,000	By Postage & Telegrams	500
		By Newspaper, etc.,	300

		By Science Equipment	480
		By Laboratory expenses	500
		By Construction of new building	4,700
		By Repair & Maintenance	600
		By Audit fees	300
		By General charges	580
		By Cash on 31.3.2012	22,000
	1,11,300		**1,11,300**

Additional information

The College had the following assets on 31.3.2011. Furniture Rs. 35,000; Land and Buildings Rs. 1,60,000; Library book Rs. 24,000; Investments Rs. 10,000; and Outstanding Tuition fees Rs. 2,200. Provide for depreciation on the closing balance of the following assets Land and Buildings @ 5%; Furniture @ 15%; Library books @ 20%.

(Deficit balance Rs. 9,625; B/S total 2,41,575; Opening capital fund 2,51,200)

6. Dr. Kabra commenced practice as a Dentist, investing Rs. 50,000 in equipment, on 1st January 2015. The receipts and payments account for the year was as follows

Receipts	Amount Rs.	Payments	Amount Rs.
To Fees	1,00,000	By Rent	6,000
To Miscellaneous receipts	200	By Salaries to Assistant	15,000
To Equipment sold	4,000	By Journals	2,000
		By Library books	6,000
		By Equipment's purchases	8,000
		By Drawing	24,000
		By Balance c/d	
		Cash at bank	43,000
		Cash in hand	200
	1,04,200		**1,04,200**

Rs. 3,000 of the fees were still outstanding. Equipment sold and purchased was on 1st October, 2015, the cost of the equipment sold being Rs. 6,000. Depreciation p.a. on equipment is 20% and Library book's 5%. Salaries to assistant still payable is Rs. 2,000. Prepare the Receipts and Expenditure account and the Balance sheet relating to 2015.

(Surplus Rs. 63,700; B/S total Rs. 91,700)

MODEL QUESTION PAPER
BCA DEGREE EXAMINATION
ACCOUNTANCY

Time: 3 hours **Max. Marks: 75**

Section – A (10 × 2 = 20)

Answer all questions

1. Define – Financial Accounting.
2. What are the golden rules of accounting?
3. What is meant by posting?
4. What is error of duplication?
5. What do you mean by contra entry?
6. What do you understand by "subsidiary books"?
7. Define – Final Account.
8. What is meant by gross profit?
9. What is Bank overdraft?
10. Define bank reconciliation statement.

Section – B (5 × 5 = 25)

Answer all questions choosing either (a) or (b)

11. a) Explain the uses of Accounting.

Or

b) Explain the business entity concept.

12. a) What are the importance of ledger?

Or

b) Prepare a Trial Balance of Vimala as on 31.3.2014 from the following ledger balances.

	Rs.		**Rs.**
Purchases	60,000	Expenses	20,000
Reserve fund	20,000	Outstanding expenses	2,000
Sales	1,00,000	Bank balance (Dr.)	5,000
Purchase returns	1,000	Fixed assets	50,000
Sales returns	2,000	Debtors	80,000
Opening stock	30,000	Creditors	30,000
Closing stock	40,000	Capital	94,000

13. a) Differentiate trade discount with cash discount.

Or

b) From the following transactions prepare a cash book

2014

May 1	Cash balance Rs. 1,000
May 2	Goods sold for cash Rs. 1,700
May 4	Purchases (Cash) Rs. 600

May 5	Received form Sam Rs. 700
May 7	Paid cash to Naresh Rs. 250
May 10	Received cash from Aurn Rs. 800
May 15	Deposited into Bank Rs. 1,200
May 19	Withdraw from Bank Rs. 400
May 22	Received dividend on shares Rs. 600
May 30	Paid Rent Rs. 400

14. a) From the following figures, prepare Trading Account of AH Ltd., for the year ending 31st December 2014

	Rs.		Rs.
Opening sock (Jan 1, 2014)	3,000	Factory Rent	750
Goods purchased (Dec 31, 2014)	15,000	Goods sold	30,000
Wages paid	1,500	Purchase returns	1,500
Coal, water	1,500	Sales returns	3,000
Power	750	Foreman's salary	2,250
Carriage inwards	2,250	Closing stock	7,500

Or

b) What are the characteristics of balance sheet?

15. a) Write short notes on

i) Cash book ii) Pass book

Or

b) From the following particulars prepare Bank Reconciliation Statement as on 31st December 2013 of Prabu who had cash at bank as per Cash book Rs. 10,500.

(i) Cheques for Rs. 300, Rs. 500 and Rs. 200 were deposited on 30th and 31st December, but were not collected by 31st December 2013.

(ii) Cheques issues for Rs. 600, Rs. 200, Rs. 489 and Rs. 50 were not enchased by 31st December 2013.

(iii) The bank collected a bill for Rs. 1,500 on 31st December 2013 but the intimation was received by Prabu on 1st January 2014.

(iv) The bank allowed interest Rs. 203 and a commission was charged Rs. 92 on 31st December 2013.

Section – C (3 × 10 = 30)

Answers any three questions

16. What are the basic functions of Accounting?

17. Journalise the following transactions in the journal of Mr. Shanmugam.

2011 August	1	Started business with Rs.4,50,000
	3	Goods purchased Rs.70,000
	5	Goods sold Rs.51,000

10	Goods purchased from Rangasamy Rs.2,00,000
16	Goods returned to Rangasamy Rs.5,000
23	Drew from bank Rs.30,000
26	Furniture purchased Rs.10,000
27	Cash with drawn for personal use Rs. 500
31	Salaries paid Rs.12,000

18. Enter the following in a cash book with cash and discount columns only.

2010	Mar.1	Manmohan started business with Rs.10,000 paid into bank Rs.8,000
	3	Bought office furniture by cheque Rs.3,000
	5	Sold goods for cash Rs.1,000
	8	Paid Anand Rs.600 and was allowed a discount of Rs.60
	12	Received from Mani a cheque for Rs.690 and allowed a discount of Rs.10; the cheque was deposited into bank
	18	Withdrew from bank for office use Rs.1,000
	24	Received for cash sales by cheque Rs.1,200
	31	Drew for personal use cash Rs.100; salaries paid Rs.500

19. The following Trial Balance is extracted from the books of Rajan on 31st December, 2014. Prepare final accounts.

Trial Balance as on 31st December, 2014

	Rs.		Rs.
Salaries and wages	4,000	Capital	2,05,000
Purchases	2,00,000	Discount received	300
Duty on purchases	7,000	Sales	3,00,000
Legal Charges	2,000	Purchase Returns	4,000
Sales Returns	10,000	Sundry Creditors	16,000
Cash Balance	10,000	Bank O/D	3,000
Stock at		Bills Payable	1,000
Commencement (1.1.14)	15,000	Loan	10,000
Advertisement	1,000	Income from Investments	700
Land & Building	1,60,000		
Plant & Machinery	50,000		
Investments	5,000		
Drawings	6,000		
Sundry Debtors	60,000		
Bills Receivable	10,000		

Adjustment: Stock at the end (31.12.2014) Rs. 30,000

20. On 30th June 2014, the pass book of Subhash showed a debit balance of Rs. 15,000. Prepare a Bank Reconciliation Statement on the basis of the following information.

(i) Uncredited cheques Rs. 5,000

(ii) The total of a page on the receipts side of the cash book adding upto Rs. 13,990 was carried to the next page as Rs. 13,909.

(iii) Bankers have given a wrong debit in respect of a cheque for Rs. 500 drawn by Subhash against his account No. 2 in the pass book.

(iv) Interest on overdraft debited in the pass book only Rs. 200

(v) Unpresented cheques amounted to Rs. 3,000

(vi) Interest on Investments collected by bankers, not yet entered in the cash book Rs. 800.

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