



B. COM. - I YEAR

DJC1C : PRINCIPLES OF FINANCIAL ACCOUNTING

SYLLABUS

Unit I

Accounting concepts – accounting conventions – preparation of final accounts – trading and profit and loss account – balance sheet – with advanced adjustment entries – provision for bad and doubtful debts – provision for discount on debtors and creditors – capital and revenue expenditure – deferred revenue expenditure – bank reconciliation statement – rectification of errors

Unit II

Bills of exchange – honouring and dishonouring of bills – renewal of bills – retirement of bills – insolvency of acceptor – trade and accommodation bills

Unit III

Accounts of non-trading concerns – receipts and payment accounts – income and expenditure account – differences – preparation of balance sheet

Unit IV

Depreciation – need – causes – methods of providing depreciation – straight line method – diminishing balance method – sinking fund method – annuity method – insurance policy method – machine hour rate method

Unit V

Single entry system – features – advantages and disadvantages – single entry system Vs double entry system – calculation of profit by comparing capitals – conversion of single entry system into double entry by finding out missing information



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SCHEMES OF LESSONS

Unit 1	Chapter 1	Basic Concept of Accounting	1
	Chapter 2	Capital and Revenue Transactions	79
	Chapter 3	Bank Reconciliation Statements	85
	Chapter 4	Rectification of Errors	95
Unit 2	Chapter 5	Bills of Exchange	104
Unit 3	Chapter 6	Accounts of Non-trading Concern	128
Unit 4	Chapter 7	Depreciation	165
Unit 5	Chapter 8	Single Entry System	195



UNIT I : ACCOUNTING CONCEPTS

Accounting concepts – accounting conventions – preparation of final accounts – trading and profit and loss account – balance sheet – with advanced adjustment entries – provision for bad and doubtful debts – provision for discount on debtors and creditors – capital and revenue expenditure – deferred revenue expenditure – bank reconciliation statement – rectification of errors

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.

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.

(i) BOOK KEEPING – MEANING AND DEFINITION

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



I.C. Cropper defines Book-keeping as follows: “Book-keeping may be described as the science of recording transactions in money or money’s worth in such a manner that, at any subsequent date, their nature and effect may be clearly understood, and that when required, a combined statement of their result may be prepared”.

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

(ii) 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 which provide 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.

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

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

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.

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,

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

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

3. Going Concern Concept

The general assumption is that a business will exist for a long time to come and will not be liquidated in the near future. People will not like to deal with a business that is to be closed down. Suppliers may not provide goods, workers may not provide their services and financial institutions may not provide credit facilities. If a business is to be closed down, its assets should be valued at current realizable values. But this is not so in case of going concern. Since the assets are meant for use, they are valued at their original cost only.

4. Money Measurement Concept

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



5. Cost Concept

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

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

6. Accounting Period Concept

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

7. Realisation Concept

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

8. Matching Concept

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



earning that revenue. The question as to when the payment for the expense is made does not arise at all.

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

9. Accrual Concept

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

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

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

10. Objectivity Concept

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

ACCOUNTING CONVENTIONS

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



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.

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.

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.

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.

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.

Specimen

Journal Entry

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

LEDGER

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



All the transactions are recorded in the journal separately and date-wise. As such, the transactions of a similar nature or those relating to a person or property or expenses/gain are recorded in different places as they occur on different dates. Moreover, the journal simply dissects the given transactions as to which account is to be debited and which one to be credited without much bothering as to what is the 'final result'.

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

Specimen

Ledger

Dr.

Cr.

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

Illustration: 1 Journalise the following transactions in the books of Mr. Raman

2015 June		Rs.
1	Raman commenced a business from cash	20000
2	Cash deposit in to the Canara bank	6000
4	Goods purchased for Cheque	2000
5	Sales to Mr. Arun	1600
12	Purchased from Mr. Ruban	4000
20	Cash sales	3000
22	Goods return to Mr. Ruban	1000
24	Goods returns from Mr. Anurn	100
30	Rent paid	400
	Salary paid	600
	Commission received	150



Solution:

Journal Entries of Mr. Raman

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2015 [[d; 1	Cash a/c To Capital a/c (Raman start business)	Dr.	20,000	20,000
2	Bank a/c To Cash a/c (cash paid for Bank)	Dr.	6,000	6,000
4	Purchase a/c To Bank a/c (Goods purchase for Cheque)	Dr.	2,000	2,000
5	Mr. Arun a/c To Sales (Sales to Mr. Aurn)	Dr.	1,600	1,600
12	Purchases a/c To Mr. Ruban (Goods from Mr. Ruban)	Dr.	4,000	4,000
20	Cash a/c To Sales a/c (Cash sales)	Dr.	3,000	3,000
22	Mr. Ruban a/c To Purchases returns a/c (Goods returns to Mr. Ruban)	Dr.	1,000	1,000
24	Sales returns a/c To Mr. Arun a/c (Goods returns from Mr. Arun)	Dr.	100	100
30	Rent a/c To Cash (Rent paid)	Dr.	400	400
	Salary a/c	Dr.	600	



	To Cash (Salary paid)			600
	Cash a/c	Dr.	150	
	To Commission a/c (Commission received)			150

Illustration: 2

Journalise the following transactions in the books of Mr. Kumaran

Jan. 2014		Rs.
1	Mr. Kumaran commenced business with cash	50,000
2	Purchased goods for cash	10,000
5	Purchased goods from Saravanan on credit	6,000
7	Paid into bank	5,000
10	Purchased furniture	2,000
20	Sold goods to Suresh on credit	5,000
25	Cash sales	3,500
26	Paid to Saravanan	3,000
31	Paid salaries	2,800

Solution:

Journal Entry of Mr. Kumaran

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2014 Jan. 1	Cash a/c To Capital a/c (Mr. Kumaran started business)	Dr.	50,000	50,000
2	Purchases a/c To Cash a/c (Cash purchases)	Dr.	10,000	10,000
5	Purchases a/c To Saravanan a/c (Credit purchases)	Dr.	6,000	6,000
7	Bank a/c	Dr.	5,000	



	To Cash a/c (Deposited in bank)			5,000
10	Furniture a/c To Cash a/c (Furniture purchased)	Dr.	2,000	2,000
20	Suresh a/c To Sales a/c (Credit sales)	Dr.	5,000	5,000
25	Cash a/c To Sales a/c (Cash sales)	Dr.	3,500	3,500
26	Mohan a/c To Cash a/c (Paid to Mohan)	Dr.	3,000	3,000
31	Salary a/c To Cash a/c (Salary paid)	Dr.	2,800	2,800

Illustration: 3

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

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



Solution:

Journal Entry of Amar

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2014 March 1	Purchases a/c To Cash a/c (Cash purchases) Dr.		25,000	25,000
2	Cash a/c To Sales a/c (Cash sales) Dr.		50,000	50,000
3	Purchases a/c To Gopi a/c (Credit purchases) Dr.		19,000	19,000
5	Robert a/c To Sales a/c (Credit sales) Dr.		8,000	8,000
7	Cash a/c To Robert a/c (Cash received) Dr.		6,000	6,000
9	Gopi a/c To Cash a/c (Cash paid) Dr.		5,000	5,000
20	Furniture a/c To Cash a/c (Furniture purchased) Dr.		7,000	7,000



Ledger of Mr. Amar

Cash Account

Dr.				Cr.			
Date	Particulars	J. F.	Amount Rs.	Date	Particulars	J. F.	Amount Rs.
2014				2014			
Mar. 5	To Sales a/c		50,000	Mar. 1	By Purchases		
	To Robert a/c		6,000		a/c		25,000
				9	By Gopi a/c		5,000
				20	By Furniture		
					a/c		7,000

Purchases Account

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

Sales Account

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



Furniture Account

Dr.

Cr.

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

Gopi Account

Dr.

Cr.

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

Robert Account

Dr.

Cr.

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

Final Accounts

The final account of business concern generally includes two parts. The first part is Trading and Profit and Loss account. This is prepared to find out the net result of the business. The second part is Balance sheet which is prepared to know the financial position of the business.

Trading Account

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



Specimen

Trading Account for the year ending 31st March, 2015

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	***	By Sales	***
To Purchases	***	Less: Sales	
Less: Purchase		returns	***
returns	***	By Closing stock	***
To Wages	***	To Gross Loss c/d	***
To Fright	***	(Transferred to Profit	
To Carriage inwards	***	and Loss a/c)	
To Clearing charges	***		
To Packing charges	***		
To Power	***		
To Octroi Duty	***		
To Gross profit c/d	***		
(Transferred to Profit			
and Loss a/c)			
	***		***

Items appearing in the debit side of Trading account

1. Opening stock

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

2. Purchases

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



3. Direct expenses

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

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

Items appearing in the credit side of Trading account

1. Sales

This includes both cash and credit sale made during the year. Net sales is derived by deducting sales return from the total sales.

2. Closing stock

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

Balancing

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

Closing entries

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



If Gross Profit

Journal Entry

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

If Gross Loss

Journal Entry

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

Profit and Loss Account

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

Specimen

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

Dr.

Cr.

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



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

Items appearing in the debit side of Profit and Loss account

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

1. Office and Administrative expenses

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

2. Repairs and Maintenance expenses

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



3. Financial expenses

Expenses incurred on borrowings – interest paid on loan.

4. Selling and Distribution expenses

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

Items appearing in the credit side of Profit and Loss account

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

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

Balancing

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

Closing entries

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

If Net Profit

Journal Entry

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



If Net Loss

Journal Entry

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

Balance sheet

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

Balance sheet is defined as ‘a statement which sets out the assets and liabilities of a business firm and which serves to ascertain the financial position of the same on any particular date’.

Specimen

Balance sheet as on 31st March 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital	***	Cash in hand	***
Add:		Cash at bank	***
Net Profit	***	Bills receivable	***
	***	Sundry debtors	***
(Or)		Investments	***
Less:		Closing stock	***
Net Loss	***	Prepaid expenses	***
	***	Furniture & fittings	***
Less: Drawings	***	Plant & machinery	***



	***		Land & buildings	***
Less:			Business premises	***
Income Tax	***	***	Patents & Trade marks	***
Sundry creditors		***	Goodwill	***
Bills payable		***		
Bank overdraft		***		
Loan		***		
Reserve fund		***		
Outstanding expenses		***		
		***		***

Assets

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

1. Tangible assets
2. Intangible assets
3. Fictitious assets

1. Tangible assets

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

- a) Fixed assts
- b) Current assets

a) Fixed assets

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

b) Current assets

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



2. Intangible assets

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

3. Fictitious assets

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

Liabilities

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

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

1. Long Term liabilities

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

2. Current liabilities

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

3. Contingent liabilities

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

Difference between Trial Balance and Balance Sheet

No.	Basis Distinction	Trial balance	Balance sheet
1.	Objective	To know the arithmetical accuracy of the accounting work	To know the true and fair financial position of the business
2.	Format	The columns are debit balances and credit balances	The two sides are assets and liabilities



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

Illustration: 4

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

Total purchases made during the year 2013 Rs. 2,00,000

Total sales made during the year 2013 Rs. 2,50,000

Solution:

Trading Account for the year ending 31st March 2013

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Purchases	2,00,000	By Sales	2,50,000
To Gross profit c/d (transferred to P & L a/c)	50,000		
	2,50,000		2,50,000

Illustration: 5

From the following information, prepare a trading account for the year ended 31.12.2013

		Rs.
2013 Jan. 1	Opening stock	15,000
2013 Dec. 31	Purchases	16,500



Sales	30,600
Closing stock	13,500

Solution:

Trading Account for the year ending 31.12.2013

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	15,000	By Sales	30,600
To Purchases	16,500	By Closing stock	13,500
To Gross profit c/d (transferred to P & L a/c)	12,600		
	44,100		44,100

Illustration: 6

Prepare trading account for the year ending 31st March 2012 from the following information.

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

Solution:

Trading Account for the year ending 31st March 2012

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	1,70,000	By Sales	2,50,000
To Purchases	1,00,000	Less	
Less:		Sales return	20,000
			<u>2,30,000</u>



Purchases return	10,000	90,000	By Closing stock	1,60,000
To wages		50,000		
To Carriage inwards		20,000		
To Gross profit c/d (transferred to P & L a/c)		60,000		
		3,90,000		3,90,000

Illustration: 7

Prepare profit and loss account, from the following balances of Mr. Kandan for the year ending 31.12.2013.

	Rs.		Rs.
Office rent	30,000	Salaries	80,000
Printing expenses	2,000	Stationeries	3,000
Tax, Insurance	4,000	Discount allowed	6,000
Advertisement	36,000	Travelling expenses	26,000
Gross profit	2,50,000	Discount received	4,000

Solution:

Profit and Loss Account of Mr. Kandan for the year ending 31st December 2013

Dr.

Cr.

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



Illustration: 8

Prepare trading and profit loss account for the year ending 31st March 2012 from the books of Mr. Siva Subramanian.

	Rs.		Rs.
Stock (31.3.2011)	15,000	Carriage outwards	4,000
Purchases	1,65,000	Wages	30,000
Purchases return	10,000	Sales return	5,000
Postage	3,000	Salaries	20,000
Discount received	5,000	Stationeries	2,000
Bad debts	1,000	Interest	8,000
Sales	3,00,000	Insurance	4,000
Stock (31.3.2012)	80,000		

Solution:

Trading and Profit & Loss Account of Mr. Siva Subramanian for the year ending 31st March 2012

Dr.	Amount Rs.	Cr.	Amount Rs.
To Opening stock	15,000	By Sales	3,00,000
To Purchases	1,65,000	Less	
Less:		Sales return	5,000
Purchases return	10,000	By Closing stock	80,000
To wages	30,000		
To Gross profit c/d (transferred to P & L a/c)	60,000		
	3,75,000		3,75,000
To Postage	3,000	By Gross profit b/d (transferred from the trading a/c)	1,75,000
To Bad debts	1,000		
To Carriage outwards	4,000	By Discount received	5,000
To Salaries	20,000		
To Stationeries	2,000		
To Interest	8,000		
To Insurance	4,000		



To Net profit (transferred to capital a/c)	1,38,000	
	1,80,000	1,80,000

Illustration: 9

From the following trial balance of Mr. John, prepare Trading, profit and loss account for the year ending 31.12.2012.

Particulars	Debit Rs.	Particulars	Credit Rs.
Purchases	5,40,000	Sales	10,40,000
Salaries & wages	3,50,000	Returns outwards	12,000
Office expenses	4,000	Discount received	6,000
Trading expenses	8,000	Interest received	3,000
Factory expenses	11,000	Capital	1,78,000
Carriage inwards	8,000		
Returns inward	12,000		
Discount allowed	4,000		
Commission	2,000		
Stock	60,000		
Income tax	40,000		
Cash in hand	2,00,000		
	12,39,000		12,39,000

Closing stock is valued at Rs. 1,35,000

Solution:

**Trading and Profit & Loss Account of Mr. Siva Subramanian
for the year ending 31st March 2012**

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	60,000	By Sales	10,40,000
To Purchases	5,40,000	Less	
Less:		Sales return	12,000
Purchases return	12,000	By Closing stock	1,35,000
	528,000		



To Trading expenses	8,000		
To Factory expenses	11,000		
To Carriage inwards	8,000		
To Gross profit c/d (transferred to P & L a/c)	5,48,000		
	11,63,000		11,63,000
To Salaries & wages	3,50,000	By Gross profit b/d	5,48,000
To Office expenses	4,000	(transferred from the	
To Discount allowed	4,000	trading a/c)	
To Commission	2,000	By Discount received	6,000
To Net profit (transferred to capital a/c)	1,97,000	By Interest received	3,000
	5,57,000		5,57,000

Illustration: 10

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

Trial balance as on 31st March 2012

Particulars	Debit Rs.	Credit Rs.
Opening stock (1.4.2011)	5,000	
Purchases	16,750	
Discount allowed	1,300	
Wages	6,500	
Sales		30,000
Salaries	2,000	
Travelling expenses	400	
Commission	425	
Carriage inwards	275	
Administration expenses	105	
Trade expenses	600	
Interest	250	



Building	5,000	
Furniture	200	
Debtors	4,250	
Creditors		2,100
Capital		13,000
Cash	2,045	
	45,100	45,100

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

Solution:

**M/S Ram & Sons Trading and Profit and Loss Account
for the year ending 31st March 2012**

Dr.

Cr.

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

Balance sheet as on 31st March 2012



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

Adjustments

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

1. Closing stock
2. Outstanding expenses
3. Prepaid expenses
4. Accrued incomes
5. Incomes received in advance
6. Interest on capital
7. Interest on drawings
8. Interest on loan
9. Interest on investments
10. Depreciation
11. Bad debts
12. Provision for bad and doubtful debts
13. Provision for discount on debtors
14. Provision for discount on creditors

Note: All adjustments are given outside the trial balance

1. Closing stock

Illustration: 11

The value of closing shown outside the trial balance on 31.03.2014 is Rs. 1,00,000



Adjustments

Remuneration for March 2014, Rs. 3,000 not yet paid.

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Remuneration a/c Dr. To Remuneration outstanding a/c (Salary outstanding)		3,000	3,000

Outstanding Remuneration

- On the debit side of profit and loss account by way additions to the particular expenses.
- On the liabilities side of the balance sheet.

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
Remuneration 25,000			
Add: Outstanding remuneration 3,000	28,000		

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Outstanding remuneration	3,000		

3. Prepaid expenses

Expenses which have been paid in advance are called as prepaid expenses.

Illustration: 13

31st March, 2014 Trial balance shows Loan Rs. 32,000



Adjustments

Prepaid interest on loan Rs. 4,300

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Prepaid interest on loan a/c Dr. To Interest a/c (Prepaid interest on loan)		4,300	4,300

Prepaid interest on loan

- i. On the debit side of the profit and loss account by way of deduction from the particular expenses
- ii. On the assets side of the balance sheet.

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
Interest 32,000			
Less: Prepaid interest			
on loan 4,300	27,700		

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
		Prepaid interest on loan	27,700

4. Accrued incomes

Income which has been earned but not received during the accounting period is called as accrued income.



Illustration: 14

Credit side of Trial balance shows commission received Rs. 3,000

Adjustment

Commission accrued but not yet received Rs. 1,500

Solution

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Accrued commission a/c To Commission a/c (Accrued commission)	Dr.	1,500	1,500

Accrued commission

- i. On the credit side of profit and loss account by way addition to particular income.
- ii. On the assets side of the balance sheet.

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
		By Commission	3,000
		Add: Accrued commission	1,500
			4,500

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
		Accrued commission	1,500



5. Incomes received in advance

Income received during a particular accounting period for the work to be done in future period is called as income received in advance.

Illustration: 15

Trial balance for the period ending 31st March 2014 shows received dividend 22,000

Adjustment

Dividend received in advance Rs. 3,000

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Dividend received Dr. To Dividend received in advance (Dividend received in advance)		3,000	3,000

Dividend received in advance

- On the credit side of the profit and loss account by way of deducting from the particular income.
- On the liabilities side of the balance sheet.

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
		By Dividend received 22,000	
		Less: Dividend received in advance 3,000	
			19,000



Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Dividend received in advance	3,000		

6. Interest on capital

In order to see whether the business is really earning profit or not, it is desirable to charge interest on capital at a certain rate.

Illustration: 16

As per trial balance, capital as on 31.3.2014 Rs. 2,00,000

Adjustment

Provide 6% interest on capital

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Interest on capital a/c Dr. To Capital a/c (Interest on capital)		12,000	12,000

Interest on capital

- i. On the debit side of profit and loss account.
- ii. On the liabilities side of the balance sheet by way of addition to the capital

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Interest on capital a/c	12,000		



Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital	2,00,000		
Less: Interest on capital	12,000		
	2,12,000		

7. Interest on drawings

Amount withdrawn by the owner for his personal use is called as drawings. When interest on capital is allowed, then interest on drawings charged from the owner. Interest on drawings is an income for the business and will reduce the capital of the owner.

Illustration: 17

The trial balance shows the following

	Rs.
Capital	4,00,000
Drawings	30,000

Adjustment

Charge interest on drawings @ 5%

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Capital a/c Dr. To Interest on drawings a/c (Interest on drawings)		1,500	1,500

To bring interest on drawings to profit and loss account the following transfer entry is required.

Transfer Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Interest on drawings a/c Dr.		1,500	



To Profit and Loss a/c (Interest on drawings)			1,500
--	--	--	-------

Interest on drawings

- i. On the credit side of profit and loss account
- ii. On the liabilities side of the balance sheet by way of addition to the drawings which are ultimately deducted from the capital.

Trading account for the year ending 31st March, 2014

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
		To Interest on drawings a/c	1,500

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital	4,00,000		
Less			
Drawings 30,000			
Interest on drawings 1,500	31,500		
	3,68,500		

8. Interest on investments

Interest receivable on investments is an income for the business.

Illustration: 18

The trial balance 31.03.2014 shows investments @ 10% Rs. 1,00,000. Interest received on investments Rs. 90,000

Adjustment

Provide for accrued interest on investments Rs. 10,000



Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Accrued interest on investments Dr. To Interest received a/c (Accrued interest on investments)		10,000	10,000

Accrued interest on investments (outstanding interest receivable will be shown)

- i. On the credit side of the profit and loss account by way of addition to the appropriate interest account.
- ii. On the asset side of the balance sheet by way of addition to the investment account.

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
		By Interest received 90,000	
		Add: Accrued interest 10,000	1,00,000

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
		Investments 10,00,000	
		Add: Accrued interest 10,000	10,10,000

9. Interest on loan

Borrowing from banks, financial institutions and outsiders for business are called loans. Amount payable towards interest on loan is an expense for the business.



Illustration: 19

The trial balance (31.3.2014) shows the following:

Bank loan @ 10% on 1.4.2013 Rs. 4,00,000

Interest paid Rs. 14,000

Adjustment

Provide for interest on bank loan outstanding

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Interest on bank loan a/c Dr. To Interest on outstanding a/c (Interest on bank loan)		26,000	26,000

Interest outstanding on Loan

- On the debit side of the profit and loss account by way of addition to the appropriate interest account.
- On the liability side of the balance sheet by way of addition to the particular loan account.

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Interest on loan 14,000			
Add:			
Interest outstanding 26,000	40,000		

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
To Bank loan 4,00,000			
Add:			



Interest				
outstanding	26,000	4,26,000		

10. Depreciation

Depreciation is the reduction in the value of fixed assets due to its use or obsolescence. Generally depreciation is charged at some percentage on the value of fixed assets.

Illustration: 20

The trial balance shows the value of machinery 31.3.2014 as Rs. 50,000.

Adjustment

Furniture is to be depreciated at 10%.

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Depreciation a/c Dr. To Machinery a/c (Depreciation on machinery)		5,000	5,000

To bring depreciation into profit and loss account the following transfer entry is required.

Transfer Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Profit & Loss a/c Dr. To Depreciation a/c (Depreciation transferred to Profit and Loss a/c)		5,000	5,000

Depreciation

- i. On the debit side of profit and loss account
- ii. On the assets side of the balance sheet by way of deducted from the value of concerned asset.



Trading account for the year ending 31st March, 2014

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Depreciation on machinery	5,000		

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
		Machinery 50,000	
		Less: Depreciation 5,000	
			45,000

11. Bad debts

Debts which cannot be recovered are called bad debts. It is a loss for the business.

Illustration: 21

The trial balance on 31st March 2014 shows, Sundry debtors Rs. 60,000.

Adjustment

Write off Rs. 4,000 as bad debts.

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Bad debts a/c Dr. To Sundry debtors a/c (Bad debts written off)		4,000	4,000

To transfer bad debts to profit and loss account the following transfer entry is required.



Transfer Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Profit & Loss a/c Dr. To Bad debts a/c (Bad debts transferred to Profit and Loss a/c)		4,000	4,000

Bad debts

- i. On the debit side of profit and loss account
- ii. On the assets side of the balance sheet by way of deduction from sundry debtors.

Trading account for the year ending 31st March, 2014

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Bad debts a/c	4,000		

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
		Sundry Debtors	60,000
		Less: Bad debts	
		Written off	4,000
			56,000

12. Provision for bad and doubtful debts

Every business suffers a percentage of bad debts over and above the debts definitely known as irrecoverable and irrecoverable. If sundry debtors figure is to be shown correctly in the balance sheet provision for bad and doubtful debts must be adjusted. This provision for bad and doubtful debts is generally provided at a certain percentage on debtors, based on past experiences.



Illustration: 22

The trial balance shows on 31.3.2013, sundry debtors as Rs. 60,000

Adjustments

Provide 5% provision for bad & doubtful debts on sundry debtors.

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Profit & Loss a/c Dr. To Provision for bad & doubtful debts a/c (5% provision for bad and doubtful debts)		3,000	3,000

Provision for bad and doubtful debts

- On the debit side of profit and loss account
- On the assets side of the balance sheet by way of deduction from sundry debtors.

Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Provision for bad & doubtful debts a/c	3,000		

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
		Sundry Debtors	60,000
		Less: Bad debts Written off	-
			60,000
		Less: Provision for	



		bad and doubtful debts	3,000	57,000
--	--	---------------------------	-------	--------

13. Provision for discount on debtors

To motivate the debtors to make prompt payments, cash discount may be allowed to them. After providing provision for bad and doubtful debts, the remaining debtors are called as good debtors. They may pay their dues in time and avail themselves of the cash discount permissible. So a provision for discount on good debtors at a certain percentage may have to be created.

Illustration: 23

The trial balance as on 31st March 2014 shows sundry debtors Rs. 45,000

Adjustments

Create 2% provision for discount on debtors.

Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Profit & Loss a/c Dr. To Provision for discount on debtors a/c (2% provision for discount of debtors)		900	900

Provision for discount on debtors

- On the debit side of profit and loss account
- On the asset side of the balance sheet by way of deduction from sundry debtors after deducting bad debts written off and provision for bad and doubtful debts.



Trading account for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Provision for discount on debtors a/c	900		

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
		Sundry Debtors	45,000
		Less: Bad debts	
		Written off	-
			<u>45,000</u>
		Less: Provision for bad and doubtful debts	
			-
			<u>45,000</u>
		Less: Provision for discount on debtors	
			900
			<u>44,100</u>

14. Provision for discount on creditors

Similar to cash discount allowed to debtors, the firm may have a chance to receive the cash discount from the creditors for prompt payment. Provision for discount on creditors is calculated a certain percentage on sundry creditors.

Illustration: 24

The trial balance for the year ended 31st March 2014 shows sundry creditors Rs. 50,000.

Adjustment

Create a provision for discount on creditors @ 2%.



Solution:

Adjusting Entry

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
31.03.14	Provision for discount on creditors Dr. To Profit and Loss a/c (Provision for discount on creditors)		1,000	1,000

Provision for discount on creditors

- i. On the credit side of profit and loss account.
- ii. On the liabilities side of the balance sheet by way of deduction from sundry creditors.

Trading account for the year ending 31st March, 2014

Dr.	Cr.
Particulars	Amount Rs.
	Particulars
	Amount Rs.
	Provision for discount on creditors
	1,000

Balance sheet as on 31st March, 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry creditors	50,000		
Less: Provision for discount on creditors	1,000		
	49,000		

Illustration: 25

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



Particulars	Debit Rs.	Credit Rs.
Sales		4,20,000
Purchases	1,05,000	
Printing charges	2,500	
Wages	77,500	
Salaries	12,500	
Opening stock	2,25,000	
Carriage inwards	8,800	
General expenses	26,250	
Trade marks	5,000	
Rates and taxes	2,500	
Capital		1,74,800
Discount received		1,250
Loan		1,75,000
Buildings	2,00,000	
Furniture	25,000	
Machinery	50,000	
Cash	1,000	
Bank	30,000	
	7,71,050	7,71,050

Adjustments

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

Solution:

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

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	2,25,000	By Sales	4,20,000
To Purchases	1,05,000	By Closing stock	3,20,000
To Wages	77,500		



To Carriage inwards		8,800		
To Gross profit c/d (Transferred to Profit and Loss a/c)		3,23,700		
		7,40,000		7,40,000
To Printing charges		2,500	By Gross profit b/d	3,23,700
To Salaries	12,500		(Transferred from trading a/c)	
Add: Outstanding	10,000	22,500	By Discount received	1,250
To General expenses		26,250		
To Rates and taxes	2,500	2,500		
Less: Prepaid	500	2,000		
To Net profit (Transferred to capital a/c)		2,71,700		
		3,24,950		3,24,950

Balance sheet as on 31st March 2014

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

Illustration: 26

The following trial balance has been extracted from the books of Mr. Bhaskar on 31.03.2013

Particulars	Debit Rs.	Credit Rs.
Machinery	40,000	



Cash at bank	10,000	
Cash in hand	5,000	
Wages	10,000	
Purchases	80,000	
Stock (1.4.2012)	60,000	
Sundry debtors	40,000	
Bills receivable	29,000	
Rent	4,000	
Interest on Bank loan	500	
Commission received		3,000
General expenses	12,000	
Salaries	7,500	
Discount received		4,000
Capital		90,000
Sales		120,000
Bank loan		40,000
Sundry creditors		40,000
Purchase returns		5,000
Sales returns	4,000	
	3,02,000	3,02,000

Adjustments

1. Closing stock Rs. 80,000
2. Interest on bank loan not yet paid Rs. 400
3. Commission received in advance Rs. 1,000

Prepare Trading and Profit and Loss Account for the year ended 31.03.2013 and Balance Sheet as on that date after giving effect to the above adjustments.

Solution:

Trading and Profit and Loss Account of Mr. Bhasker for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	60,000	By Sales	1,20,000



To Purchases	80,000		Less: Sales		
Less: Purchase			returns	4,000	1,16,000
returns	5,000	75,000	By Closing stock		80,000
To Wages		10,000			
To Gross profit c/d (Transferred to Profit and Loss a/c)		51,000			
		1,96,000			1,96,000
To Rent		4,000	By Gross profit b/d		51,000
To Interest on bank loan	500		(Transferred from trading a/c)		
Add: Outstanding	400	900	By Commission received	3,000	
To General expenses		12,000	Less: Received in		
To Salaries		7,500	Advance	1,000	2,000
To Net profit (Transferred to capital a/c)		32,600	By Discount received		4,000
		57,000			57,000

Balance sheet of Mr. Bhaskar as on 31st March 2014

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital	90,000		Cash in hand		5,000
Add:			Cash at bank		10,000
Net Profit	32,600	1,22,600	Bills receivable		29,000
Sundry creditors		40,000	Sundry debtors		40,000
Bank Loan	40,000		Closing stock		80,000
Add: Outstanding			Machinery		40,000
Interest	400	40,400			
Commission received in advance		1,000			
		2,04,000			2,04,000



Illustration: 27

The following are the balances extracted from the books of Mrs. Suguna as on 31st March, 2014

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Drawings	40,000	Capital	200,000
Cash at bank	17,000	Sales	1,60,000
Cash in hand	60,000	Sundry creditors	45,000
Wages	10,000		
Purchases	20,000		
Stock (31.3.2013)	60,000		
Buildings	1,00,000		
Sundry debtors	44,000		
Bills receivable	29,000		
Rent	4,500		
Commission	2,500		
General expenses	8,000		
Furniture	5,000		
Machinery	5,000		
	4,05,000		4,05,000

Adjustments:

1. Closing stock of Rs. 40,000 valued as on 31.03.2014
2. Interest on capital at 6% to be provided
3. Interest on drawings at 5% to be provided
4. Depreciate buildings at the rate of 10% per annum
5. Write off bad debts Rs. 1,000
6. Wages yet to be paid Rs. 500

Prepare Trading and Profit & Loss account and Balance Sheet as on 31st March 2014.



Solution:

**Trading and Profit and Loss Account of Mrs. Suguna
for the year ending 31st March, 2014**

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	60,000	By Sales	1,60,000
To Purchases	20,000	By Closing stock	40,000
To Wages 10,000			
Add: Outstanding 500	10,500		
To Gross profit c/d (Transferred to Profit and Loss a/c)	1,09,500		
	2,00,000		2,00,000
To Rent	4,500	By Gross profit b/d	1,09,500
To Commission	2,500	(Transferred from trading a/c)	
To General expenses	8,000	By Interest on drawings	2,000
To Interest on capital	12,000		
To Depreciation on buildings	10,000		
To Bad debts written off	1,000		
To Net profit (Transferred to capital a/c)	73,500		
	1,11,500		1,11,500

Balance sheet of Mrs. Suguna as on 31st March 2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital 2,00,000		Cash at bank	17,000
Add:		Cash in hand	60,000
Net Profit 73,500		Sundry debtors 44,000	
2,73,500		Less: Net bad debts	
Add:		Provision 1,000	43,000



Interest on capital	12,000		Bills receivable	29,000
	<u>2,85,500</u>		Machinery	5,000
Less: Drawings	40,000		Furniture	5,000
	<u>2,45,500</u>		Buildings	1,00,000
Less: Interest on			Less: Depreciation	10,000
Drawings	2,000	2,43,500		90,000
Sundry creditors		45,000		
Outstanding wages		500		
		2,89,000		2,89,000

Illustration: 28

Mr. Senthil's book shows the following balances. Prepare Trading and Profit and Loss account for the year ended 31st March 2015 and Balance sheet as on that date.

Particulars	Debit Rs.	Credit Rs.
Stock on 1.4.2014	1,50,000	
Purchases	1,30,000	
Sales		3,00,000
Carriage inwards	2,000	
Salaries	50,000	
Printing and stationery	8,000	
Drawings	17,000	
Sundry creditors		20,000
Sundry debtors	1,80,000	
Furniture	10,000	
Capital		2,50,000
Postage & Telephone	7,500	
Interest paid	4,000	
Machinery	41,500	
Loan		25,000
Bank overdraft		5,000
	6,00,000	6,00,000



Adjustments

1. Closing stock Rs. 1,20,000
2. Provide 5% for bad & doubtful debts on debtors
3. Depreciate machinery & furniture by 5%
4. Allow interest on capital at 5%
5. Prepaid printing charges Rs. 2,000

Solution:

Trading and Profit and Loss Account of Mr. Senthil

for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	1,50,000	By Sales	3,00,000
To Purchases	1,30,000	By Closing stock	1,20,000
To Carriage inwards	2,000		
To Gross profit c/d (Transferred to Profit and Loss a/c)	1,38,000		
	4,20,000		4,20,000
To Salaries	50,000	By Gross profit b/d (Transferred from trading a/c)	1,38,000
To Printing & Stationery 8,000	8,000		
Less: Prepaid 2,000	6,000		
To Postage & Telephone	7,500		
To Interest paid	4,000		
To Bad and doubtful debts	9,000		
To Depreciation			
Machinery 2,075	2,075		
Furniture 500	2,575		
To Interest on capital	12,500		
To Net profit (Transferred to capital a/c)	46,425		
	1,38,000		1,38,000



Balance sheet of Mr. Senthil as on 31st March 2015

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital	2,50,000		Sundry debtors	1,80,000	
Add:			Less: Bad and		
Net Profit	46,425		doubtful debts	9,000	1,71,000
	<u>2,96,425</u>		Prepaid charges in		
Add:			printing & stationery		2,000
Interest on capital	12,500		Furniture	10,000	
	<u>3,08,925</u>		Less: Depreciation	500	9,500
Less: Drawings	17,000	2,91,925			5,000
Sundry creditors		20,000	Machinery	41,500	
Loan		25,000	Less: Depreciation	2,075	39,425
Bank overdraft		5,000	Closing stock		1,20,000
		3,41,925			3,41,925

Illustration: 29

From the Trial balance of Mr. Raghuraman as on 31st March, 2013 prepare final accounts.

Particulars	Debit Rs.	Credit Rs.
Capital		3,60,000
Drawings	6,400	
Stock (1.4.2012)	18,000	
Purchase	1,29,000	
Sales		2,38,000
Sales returns	4,000	
Wages	32,000	
Insurance premium	3,000	
Packing expenses	4,000	
Postage	200	
Advertisement	2,000	
Carriage outwards	16,000	



Bad debts	600	
Commission received		1,000
Bills payable		18,000
Bank overdraft		6,000
Land & Buildings	2,61,000	
Plant & Machinery	1,80,000	
Sundry debtors	50,800	
Sundry creditors		84,000
	7,07,000	7,07,000

Adjustments

1. Closing stock on 31.03.2013 Rs. 15,000
2. Write off bad debts Rs. 800 and make provision for doubtful debts @ 5% on Sundry debtors
3. Commission accrued but not received Rs. 2,000

Solution:

Trading and Profit and Loss Account of Mr. Raghuraman for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	18,000	By Sales	238,000
To Purchases	1,29,000	Less: Sales	
To Wages	32,000	returns	4,000
To Backing expenses	4,000	By Closing stock	15,000
To Gross profit c/d (Transferred to Profit and Loss a/c)	66,000		
	2,49,000		249,000
To Insurance	3,000	By Gross profit b/d	66,000
To Postage	200	(Transferred from trading a/c)	
To Advertisement	2,000	By Commission	
To Carriage outwards	16,000	received	1,000
To Bad debts	600	Add: Accrued	2,000
			3,000



Add: Bad debts			
Written off	800	1,400	
To Provision for bad & doubtful debts		2,500	
To Net profit (Transferred to capital a/c)		43,900	
		69,000	69,000

Balance sheet of Mr. Raghuraman as on 31st March 2014

Liabilities		Amount	Assets		Amount
		Rs.			Rs.
Capital	3,60,000		Sundry debtors	50,800	
Add:			Less: Bad debts		
Net Profit	43,900		Written off	800	
	<u>4,03,900</u>			<u>50,000</u>	
Less: Drawings	6,400	3,97,500	Less: Provision for		
Sundry creditors		84,000	Bad & doubtful		
Bills payable		18,000	debts	2,500	47,500
Bank overdraft		6,000	Closing stock		15,000
			Accrued commission		2,000
			Land & Buildings		2,61,000
			Plant & Machinery		1,80,000
		5,05,500			5,05,500

Illustration: 30

From the following particulars of Mrs. Sulochana, prepare Trading and Profit and Loss Account and Balance sheet for the year ending 31st March 2014

Particulars	Debit	Credit
	Rs.	Rs.
Capital		7,50,000
Cash	40,000	
Buildings	4,00,000	
Salary	1,10,000	



Rent & Taxes	21,000	
Opening stock	1,20,000	
Machinery	1,20,000	
Drawings	40,000	
Purchases	5,00,000	
Sales		75,000
Carriage inwards	5,000	
Fuel, Gas	37,000	
Sundry debtors	2,50,000	
Sundry creditors		1,20,000
Bills receivable	53,000	
Dividend		28,000
Loan		60,000
Bad debts	2,000	
Advertisement	16,000	
Provision for bad & doubtful debts		6,000
	17,14,000	17,14,000

Adjustments

1. Closing stock Rs. 1,40,000
2. Write off Rs. 10,000 as bad debts; Provide 5% for bad and doubtful debts.
3. Make provision for discount on debtors at 2%
4. Provision for discount on creditors at 2%

Solution:

Trading and Profit and Loss Account of Mrs. Sulochana for the year ending 31st March, 2014

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	1,20,000	By Sales	7,50,000
To Purchases	5,00,000	By Closing stock	1,40,000
To Carriage inwards	5,000		
To Fuel, Gas	37,000		
To Gross profit c/d	2,28,000		



(Transferred to Profit and Loss a/c)			
	249,000		2,49,000
To Salary	1,10,000	By Gross profit b/d	2,28,000
To Rent & Taxes	21,000	(Transferred from trading a/c)	
To Advertisement	16,000		
To Old Bad debts	2,000	By Dividend	28,000
Add: New bad debts		By Provision for discount on	
Written off	10,000	creditors	2,400
	1,400		
	<u>12,000</u>		
Add:			
New Provision	12,000		
	<u>24,000</u>		
Less:			
Old Provision	6,000		
	<u>18,000</u>		
To Provision for			
discount on debtors	4,560		
To Net profit	88,840		
(Transferred to capital a/c)			
	2,58,400		2,58,400

Balance sheet of Mrs. Sulochana as on 31st March 2014

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital	7,50,000		Sundry debtors	2,50,000	
Add:			Less: New		
Net Profit	88,840		Bad debts	10,000	
	<u>8,38,840</u>			<u>2,40,000</u>	
Less: Drawings	40,000	7,98,840	Less: Provision for		
Sundry creditors	1,20,000		Bad & doubtful		
Less: Provision for			debts	12,000	
discount	2,400	1,17,600		<u>2,28,000</u>	
Loan		60,000	Less: Provision for		



		discount	4,560	2,23,440
		Cash		40,000
		Bills receivable		53,000
		Building		4,00,000
		Machinery		1,20,000
		Closing stock		4,00,000
	976,440			9,76,440

Exercises

Theory Questions

1. What is trading account?
2. What is outstanding expense?
3. What is prepaid expense?
4. What is accrued income?
5. What is income received in advance?
6. What is bad debt?
7. Write notes on provision for bad and doubtful debts.
8. Write notes on provision for discount on debtors.
9. Write notes on provision for discount on creditors.
10. What are the items appearing in the debits and credit side of trading account?
11. What are the items appearing in the debits and credit side of profit and loss account?
12. Write the difference between trial balance and balance sheet.

Problems

1. Journalise the following transactions of Mrs. Rama

2014 March	Rs.
1 Mrs. Rama commenced business with cash	30,000
2 Paid into bank	21,000
3 purchased goods by cheque	15,000
7 Drew cash from bank for office use	3,000
15 Purchased goods from Siva	15,000
20 Cash sales	30,000
25 Paid to Siva	14,750



	Discount receive	250
31	Paid rent	500
	Paid salaries	2,000

2. Journalise the following transactions of Mr. Moorthi

2014 June		Rs.
3	Received cash from Ramkumar	60,000
4	Purchased goods for cash	15,000
11	Sold goods to Domodaran	22,000
13	Paid to Ramkumar	40,000
17	Received from Damodaran	20,000
20	Bought furniture from Jagadeesan	5,000
27	Paid rent	1,200
30	Paid salary	2,500

3. Record the following transactions in the Journal of Tmt. Bhanumathi

2014 Feb.		Rs.
3	Bought goods for cash	84,500
7	Sold goods to Dhanalakshmi on credit	55,000
9	Received commission	3,000
10	Cash sales	1,09,000
12	Bought goods from Mahalakshmi	60,000
15	Received five chairs from Revathi & Co., at Rs. 400 each	2,000
20	Paid Revathi & Co., cash for five chairs	2,000
28	Paid salaries	10,000
	Paid Rent	5,000

4. Journalise the following transactions in the Journal Mr. Shanmugam, post them in the ledger and balance them.

2014 Aug.

- 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 Settled Rangasamy's account
- 31 Salaries paid, Rs. 12,000

5. Enter the following transactions in journal and post them in the ledger of Mr. Govindarajan and balance them.

2013 Dec.	Rs.
1 Govindarajan commenced his business with the following assets and liabilities	
Plant and Machinery	2,50,000
Stock	90,000
Furniture	7,000
Cash	50,000
Sundry creditors	1,50,000
2 Sold goods to Sundar	1,50,000
3 Bought goods from Natarajan	65,000
4 Sundar paid cash	1,25,000
6 Returned damaged goods to Natarajan	2,000
10 Paid to natarajan	28,000
31 Paid rent	5,000
Paid salaries	9,000

6. Post the following transactions direct into ledger of Thiru Karthik and balance them.

2013 Oct.
1 Received cash from Ramesh Rs. 1,60,000
5 Bought goods for Cash Rs. 60,000
7 Sold to Suresh Rs. 30,000
15 Bought from Dayalan Rs. 40,000
18 Sold to Ganesan Rs. 50,000



- 20 Withdrew cash for personal use Rs. 18,000
- 25 Received commission Rs. 20,000
- 30 Paid rent Rs. 5,000
- 31 Paid salary Rs. 10,000

7. The trial balance of Mrs. Kalpana shows the following balances on March 31, 2011

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

Adjustments

The closing stock was valued at Rs. 60,000

You are required to prepare the profit and loss account for the year ending 31st March 2011 and the balance sheet as on that date.

**(Ans. Gross profit Rs. 1,52,000; Net Profit Rs. 1,24,000;
Balance sheet Rs. 4,22,000))**



8. The following balances have been extracted from the books of Mrs. Kumar as on 31st March, 2016

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

Adjustments

- 1) Outstanding rates and taxes Rs. 1,600
- 2) Insurance premium prepaid Rs. 2,000
- 3) Maintain provision for bad and doubtful debts at 5% on debtors
- 4) Depreciate Motor car by 10%. Furniture by 4% and Buildings by 3%
- 5) Stock on 31.12.2016 Rs. 20,000

**(Ans. Gross profit Rs. 93,000; Net Profit Rs. 83,720;
Balance sheet Rs. 1,34,920))**

9. From the under mentioned trial balance of Mr. Seleem as on 31.3.2011, prepare trading and profit and loss account and balance sheet as on that date.

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Cash in hand	1,500	Capital	80,000



Purchases	1,20,000	Bank loan @ 4%	20,000
Opening stock	40,000	Bills payable	25,000
Sundry debtors	60,000	Sundry creditors	25,000
Plant and machinery	50,000	Sales	2,00,000
Furniture	20,000	Provision for bad & doubtful	
Bills receivable	15,000	debts	1,500
Rent and taxes	10,000	Interest	1,000
Wages	16,000		
Salaries	20,000		
	3,52,500		3,52,500

Adjustments

- 1) Closing stock Rs. 50,000
- 2) Provide for outstanding liabilities

Rent and taxed	Rs. 2,000
Wages	Rs. 3,000
Salaries	Rs. 4,000
- 3) Depreciation on Plant and Machinery @ 5% and on furniture @ 10%.
- 4) Provide 4% interest on bank loan
- 5) Write off bad debts Rs. 2,000

**(Ans. Gross profit Rs. 71,000; Net Profit Rs. 30,200;
Balance sheet Rs. 1,90,000)**

10. Trial balance of Anuradha Agencies as on 31.03.2011

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



General expenses	15,000		
Freight inwards	2,000		
Freight outwards	1,000		
Sundry debtors	28,000		
Bank	20,200		
Goodwill	10,000		
	2,32,500		2,32,500

Adjustments

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

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

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

Balance sheet Rs. 1,37,868)

11. The following balance have been extracted from the books of Mrs. Padma as on 31st March 2012

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Furniture	30,000	Capital	2,00,000
Cash in hand	8,000	Commission	14,000
Openings stock	1,00,000	Sales	6,00,000
Purchases	3,20,000	Creditors	1,00,000
Investments @ 10%	20,000	Interest	1,500
Drawings	60,000		
Bad debts	12,000		
Salaries	60,000		
Carriage inwards	20,000		
Insurance	12,000		
Rent	26,000		
Debtors	1,80,000		
Advertising	40,000		



Printing & Stationery	12,000	
General expenses	15,500	
	9,15,500	9,15,500

Adjustments

- 1) Closing stock was valued at Rs. 80,000
- 2) Provide for accrued interest on investments Rs. 500
- 3) Commission received in advance Rs. 4,000
- 4) A provision for bad and doubtful debts is to be created to the extent of 5% on sundry debtors
- 5) A provision for discount on sundry creditors is to be created to the extent of 2% on sundry creditors.

(Ans. Gross profit Rs. 2,40,000; Net Profit Rs. 67,500;

Balance sheet Rs. 3,09,500)

12. From the following Trial balance of Mr. Joeseph, prepare trading and profit and loss account for the year ended 31st March, 2013 and a balance sheet as on that date.

Particulars	Debit Rs.	Credit Rs.
Capital		1,20,000
Sales		75,000
Purchases	45,000	
Salaries	6,000	
Rent	4,500	
Insurance premium	900	
Drawings	15,000	
Machinery	84,000	
Bank	13,500	
Cash	13,500	
Stock (1.4.2012)	15,600	
Sundry debtors	7,500	
Sundry creditors		10,500
	2,05,500	20,5,500



Adjustments

- 1) Stock on 31.3.2013 Rs. 14,700
- 2) Salaries unpaid Rs. 1,000
- 3) Rent paid in advance Rs. 750
- 4) Create 5% provision for bad and doubtful debts on sundry debtors.

(Ans. Gross profit Rs. 29,100; Net Profit Rs. 17,075;

Balance sheet Rs. 1,33,575)

13. The following balances are extracted from the book of Mr. Venugopal as on 31st March 2014. Prepare trading, profit and loss account and the balance sheet.

Particulars	Debit Rs.	Credit Rs.
Capital		1,20,000
General expenses	16,500	
Drawings	16,000	
Commission		11,000
Bank overdraft		25,000
Cash in hand	2,500	
Stock (1.4.2013)	1,00,000	
Furniture	80,000	
Purchases	3,00,000	
Sales		5,00,000
Wages	50,000	
Insurance premium	1,000	
Salaries	15,000	
Sundry creditors		50,000
Sundry debtors	1,50,000	
Bills payable		25,000
	7,31,000	7,31,000

Adjustments

- 1) Closing stock Rs. 1,00,000
- 2) Write off bad debts Rs. 20,000



- 3) Create provision for bad and doubtful debts @ 5%
- 4) Create provision for discount on debtors @ 2%
- 5) Create provision for discount on creditors @ 2%.

**(Ans. Gross profit Rs. 1,50,000; Net Profit Rs. 1,00,530;
Balance sheet Rs. 3,03,530)**

14. The following are the balance extracted from the books of Mrs. Nandini as on 31.03.2012

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Drawings	40,000	Capital	2,00,000
Cash in hand	17,000	Sales	1,60,000
Cash at ban	65,000	Sundry creditors	45,000
Wages	10,000		
Purchases	20,000		
Stock (1.4.2011)	60,000		
Buildings	1,00,000		
Sundry debtors	44,000		
Bills receivable	29,000		
Rent	4,500		
Commission	2,500		
General expenses	8,000		
Furniture	5,000		
	4,05,000		4,05,000

Adjustments

- 1) Closing stock Rs. 40,000
- 2) Interest on capital at 6% to be provided
- 3) Interest on drawings at 5% to be provided
- 4) Wages yet to be paid Rs. 1,000
- 5) Rent prepared Rs. 900

Prepare trading and profit and loss account and balance sheet on 31.03.2012.

**(Ans. Gross profit Rs. 1,09,000; Net Profit Rs. 84,900;
Balance sheet Rs. 3,00,900)**



15. From the following trial balance of Thiru. Rehman as on 31st March 2015, prepare trading and profit and loss account and balance sheet taking into account the adjustments.

Debit balances	Amount Rs.	Credit balances	Amount Rs.
Land and Buildings	42,000	Capital	62,000
Machinery	20,000	Sales	98,780
Patents	7,500	Returns outwards	500
Stock (1.4.2014)	5,760	Sundry creditors	15,300
Sundry debtors	14,500		
Purchases	40,675		
Cash at bank	3,170		
Return inwards	680		
Wages	8,480		
Fuel & Power	4,730		
Carriage inwards	2,040		
Carriage outwards	3,200		
Salaries	15,000		
General expenses	8,245		
Insurance	600		
	1,76,580		1,76,580

Adjustments

- 1) Stock on 31.03.2015 was Rs. 6,800
- 2) Salary outstanding Rs. 1,500
- 3) Insurance prepaid Rs. 150
- 4) Depreciate machinery @ 10% and patents @ 20%
- 5) Create a provision of 2% on debtors for bad debts.

(Ans. Gross profit Rs. 43,715; Net Profit Rs. 11,530;

Balance sheet Rs. 90,330)



CHAPTER – 2

CAPITAL AND REVENUE TRANSACTIONS

Once the trial balance is prepared the next step is to find out the net result (profit or loss account) and financial position (balance sheet) of the business concern. The business concern's financial position is bound to be affected by the result of its operations. “**Matching Principle**” governs the preparation of these two statements. According to this principle the revenues and relevant expenditures incurred during a particular period should be matched. Thus a proper distinction must be accounted for between capital and revenue transactions. Business transactions can be capital transactions or revenue transactions.

CAPITAL TRANSACTIONS

The business transactions, which provide benefits or supply services to the business concern for more than one year or one operating cycle of the business, are known as capital transactions.

The transactions which relate to capital are again sub-divided into capital expenditure and capital receipts.

Examples

- i. Expenses incurred in the acquisition of Land, Building, Machinery, Furniture, Car, Goodwill, Copyright, Trade Mark, Patent Right, etc.,
- ii. Expenses incurred for increasing the seating accommodation in a cinema hall.
- iii. Expenses incurred for remodeling and reconditioning an existing asset like remodeling a building.

CAPITAL RECEIPT

Capital receipt is one which is invested in the business for a long period. It includes long term loans obtained from others any amount realized on sale of fixed assets. It is generally non-recurring in nature.

Examples

- i. Capital introduced by the owner
- ii. Borrowed loans
- iii. Sale of fixed asset



REVENUE TRANSACTIONS

The business transactions, which provide benefits or supplies services to a business concern for an accounting period only, are known as revenue transactions. Revenue transactions can be revenue expenditure or revenue receipt.

REVENUE EXPENDITURE

Revenue expenditures consist of those expenditures, which are incurred in the normal course of business. They are incurred in order to maintain the existing earning capacity of the business. It helps in the upkeep of fixed assets. Generally it is recurring in nature.

Examples

- i. Cost of goods purchased for resale.
- ii. Office and administrative expenses.
- iii. Selling and distribution expenses.
- iv. Depreciation of fixed assets, interest on borrowing etc.,
- v. Repairs, renewals, etc.,

REVENUE RECEIPT

Revenue receipt is the receipt of income which is earned during the normal course of business. It is recurring in nature.

Examples

- i. Sale of goods or services
- ii. Commission and discount received
- iii. Dividend and interest received on investments etc.,

DEFERRED REVENUE EXPENDITURE

A heavy revenue expenditure, the benefit of which may be extended over a number of years, and not for the current year alone is called deferred revenue expenditure. For example, a new firm may advertise very heavily in the beginning to capture a position in the market. The benefit of this advertisement campaign will last for quite a few years. It will be better to write off the expenditure in three or four years and not only in the first year.



Examples

- i. Expenses incurred on research and development.
- ii. Abnormal loss arising out of fire or lightning (incase the act has not been insured).
- iii. Huge amount spent on advertisement.

CAPITAL PROFIT AND REVENUE PROFIT

In order to find out the correct profit and the true financial position there must be a clear distinction between capital profit and revenue profit

1. Capital profits

Capital profit is the profit which arises not from the normal course the business. Profit on sale of fixed asset is an example for capital it.

2. Revenue profits

Revenue profit is the profit which arises from the normal course of business.
i.e. Net profit – the excess of revenue receipts over revenue expenditures.

3. Capital loss and Revenue loss

In order to ascertain the loss incurred by a firm it is important to distinguish between capital losses and revenue losses.

4. Capital losses

Capital losses are the losses which arise not from the normal course of business. In order words, 'net loss' – i.e. excess of revenue expenditures over revenue receipts.

Illustration: 1

Kumar & Co., incurred the following expenses during the year 2013 classify the following items under capital or revenue.

- i. Purchase of furniture Rs. 10,000
- ii. Purchase of second hand machinery Rs. 40,000
- iii. Rs. 500 paid for carriage on goods purchased.
- iv. Rs. 1,750 paid for repairs on second hand machinery as soon as it was purchased.
- v. Rs. 6,000 wages paid for installation of plant.

**Solution:**

- i. Capital expenditure – as it results in the acquisition of fixed asset.
- ii. Capital expenditure – as it results in the acquisition of fixed asset.
- iii. Revenue expenditure – expenses incurred on purchases of goods for sale.
- iv. Capital expenditure – as it is spent for bringing the asset into working condition.
- v. Capital expenditure – as it is spent for bringing the asset into working condition.

Illustration: 2

Suresh Co incurred the following expenses during the year 2013 classify the expenses as capital and revenue.

1. Rs. 7500 spent towards replacement of a worn out part in a machinery.
2. Rs. 1,500 spent for legal expenses in relation to raising of a loan for the business.
3. Rs. 3,000 spent for ordinary repairs of plant.
4. Rs. 6,000 spent of replacing a petrol driven engine by a diesel driven engine.
5. Electricity charges Rs. 1,2000 per month.

Solution:

1. Capital expenditure – as it helps to increase the working condition of the machinery.
2. Capital expenditure – as it spent as it helps to get a capital receipt.
3. Revenue expenditure – as it is spent for the maintenance of the asset.
4. Capital expenditure – as it helps to reduce cost of production.
5. Revenue expenditure – expenditure incurred in the normal course of business.

Illustration: 3

ABC companies give the following expenses which were incurred in his the business during the year classify them into capital revenue or deferred revenue

1. Rs. 50,000 a meeting in order to increase sale
2. New machine was purchased Rs. 5,000
3. Rs. 50,000 spent on research and development.



4. Rs. 500 paid for fuel.

Solution:

1. Deferred revenue expenditure
2. Capital expenditure
3. Deferred revenue expenditure
4. Revenue expenditure

Theory Questions

1. What do you mean by Capital and Revenue Income and Expenditure?
2. What is Deferred Revenue Expenditure?
3. Write short notes on Capital Loss and Revenue Loss.

Exercises

1. Classify the following into capital or revenue
 - i. Repair of Rs. 500 for machine
 - ii. Rs. 2,000 for purchasing old machines
 - iii. Rs. 560 spent on carriage inwards
 - iv. Profit on Rs. 700 for old assets.
 - v. Rs. 500 for loss on sale of furniture.

(Ans. Capital expenditure – i, ii; Revenue expenditure – iii;
Capital Profit – iv; Capital Loss – v)

2. 2014 Sunder gives you the following transaction in his business classified capital, revenue.

- i. The expenses for copy writing Rs. 1,00,000
- ii. Fright charge paid Rs. 800.
- iii. Rs. 635 for repairing furniture.
- iv. Rs. 10,000 paying for rain water saving scheme for Government instructions.
- v. Advertisement charges Rs. 15,000

(Ans. Capital expenditure – i, ii, iv; Revenue expenditure – iii;
Deferred Revenue Expenditure – v)



3. Mr. Rahavadran gives you the following transaction in his business classified capital, revenue.

- i. Rs. 10,000 for goods purchased.
- ii. Rs. 2,400 fire insurance for the building for business.
- iii. Renewal of magazine subscription fee Rs. 75
- iv. Cost of Rs. 2,00,000 and building a godown
- v. Purchased land for Rs. 2,00,000

(Ans. Capital expenditure – iv, v; Revenue expenditure – i, ii, iii)

4. Classify the following expenses into capital and revenue

- i. The registration expenses incurred for the purchased land Rs. 10,000
- ii. Repairing charges paid for remodeling the purchase of old building Rs. 2,00,000
- iii. Profit earned on the sale of old furniture Rs. 5,000
- iv. Carriage paid on goods purchased Rs. 500
- v. Maintenance for building Rs. 5,000
- vi. Rs. 10,000 expenses paid for whitewash in office building.
- vii. Wages paid to workmen Rs. 15,000
- viii. Received for rent Rs. 20,000
- ix. Loss on sale of old furniture Rs. 500

(Ans. Capital expenditure – i, ii, v; Revenue expenditure – iv, vi, vii;
Capital Profit – iii; Capital Loss – ix; Revenue Income – viii)



CHAPTER – 3

BANK RECONCILIATION STATEMENT

MEANING

Many transactions involving receipt and payment of money take place every day in a business unit whenever a businessman deposits money into bank or withdraws from the bank he records the same in his cash book. The business man can relieve himself from his botheration of receiving and making payment by opening current account in the bank every business man opens a current account in the bank in usually given a pass book which makes a record of the businessman's transaction with the bank. This pass book swritten by the bank.

The specimen of a Pass book can be as follows

Name Account No.

Address

Current Account with SBI

Date	Particulars	Dr. Withdrawals	Dr. Deposits	Balance Dr. / Cr.	Accountant initials

Bank Pass Book in nicety a copy of the customer's account in the books of a bank. It shows all the deposits, withdrawals and the balance available in the customer's account.

In the date column, the date of the transaction are recorded. In the particular column withdrawals and deposits are recorded. The balance after each traction is recorded in the next column and the bank official sings in the last column.

The main point to be remembered is that entries are made only after cash is received or paid except in the case of interest and bank charges interest and bank charges are mere bonk adjustments are in these, there are neither receipt of cash or payment of cash.



Difference between cash book and pass book

Basis	Cash book	Pass book
Maintained	It is maintained by cashier	It is maintained by banker
Cash deposits	Cash deposited is entered on the debits side of the cash book	Cash deposited is entered on the credit side of the pass book
Cash withdrawals	Cash withdrawals in entered on the credit side of the cash book.	Cash withdrawals in entered on the debt side of the pass book
Cheque deposited	It is entered on the debit side of the cash book on the date of deposit the cheque into bank	It is entered in the pass book on the date of the realiation of the cheque.
Cheque issued	It is entered on the credit side of the cash book	It is entered on the debit side of the pass book
Collection and payments	It is entered in the cash book after seeing the pass book	It is entered in the pass book first
Signature	It is not signed by the cashier	It is signed by the banker
Balancing	It is balanced at the end of a specified period	It is balanced after each transaction

Bank Reconciliation Statement (BRs)

All the end of a particular period, cash book of a trader may disclosed a balance amount and that amount will not be the same as shown in his pass book. A bank reconciliation statement is a statement which a prepared in order to find out the reasons (or) cashier for the different amount of balance shown in a cash book with that of his pass boo. It is called as a Bank Reconciliation Statement because is reconciles the bank balance as shown by the cash book with the bank balance as shown by the pass book by making suitable adjustments for the items cashing the disagreement.



Bank Reconciliation Statements is a statement which indicates the various items that cause a difference between the bank balance as per cash book and pass book on any given date.

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.

NEED AND IMPORTANCE

After tracing the various different items in the bank reconciliation statement is prepared. The following are its advantages in which lies its importance.

- 1) The error that might have been taken place in the cash book in connection with bank transaction can be early found.
- 2) It is prepared regular, so reduced the frauds.
- 3) It is an indirectly imposed moral check on the account staff.
- 4) It is preparation of bank reconciliation statement uncredited cheque can be detected and steps can be taken for their collection.

REASON TO PREPARATION OF BANK RECONCILIATION STATEMENT

The following are the reason to preparing of bank reconciliation statement.

- 1) The cheques deposited but not credited in the pass book within particular period.
- 2) Cheques issued to suppliers but not encashed by them within a particular period.
- 3) Cheques received and entered in the cash book but omitted to deposit into the bank.
- 4) Cheques dishonored and debited in the pass book but omitted to inform the customer.
- 5) Wrong debit or credit amount entered in pass book.
- 6) Wrong debit or credit amount entered in cash book.



STEPS TO PREPARE A BANK RECONCILIATION STATEMENT

A pass book (or) a cash book may show either a debit balance (or) a credit balance.

a) If a cash book shows a debit balance, these the following steps may be followed.

Bank Reconciliation Statement

Particulars	Debit Rs.	Credit Rs.
Balance as per cash book		***
Add		
Cheques issued but not presented	***	
Interest credited in pass book	***	
Dividend, interest on securities collected and credited in the		
pass book	***	***
Less		
Cheque deposited but not credited	***	
Amount remitted by banker on behalf of customer	***	
Interest on overdraft debited in pass book	***	
Cheques dishonoured and entered in pass book	***	
Cheque received and debited in cash book but not		
deposited in bank	***	
Bank charges debited in pass book only	***	***
Balance as pass book		***

Illustration: 1 When balance as per cash book is favourable

From the following details, make out a bank reconciliation statement for Ms. Kumaran Company as on December 31, 2013 to find out the balance as per pass book.

		Rs.
1	Cheque deposited but not yet collected by the bank	3,000
2	Cheque issued to Mr. Raju has not yet been presented for payment	5,000



3	Bank charges debited in the pass book	400
4	Interest allowed by the bank	200
5	Insurance premium directly paid by the bank as per standing instruction	1,000
6	Balance as per cash book	4,000

Solution:

Bank reconciliation statement as on 31st December 2013

Particulars	Amount Rs.	Amount Rs.
Balance as per cash book		4,000
Add:		
Cheque issued to Mr. Raju has not yet been presented for payment	5,000	
Interest allowed by the bank	200	5,200
		5,600
Less:		
Cheque deposited but not yet collected by the bank	3,000	
Insurance premium directly paid by the bank as per standing instruction	1,000	
Bank charges debited in the pass book	400	4,400
Balance as per pass book		1,200

Illustration: 2

Mr. Abdul pass showed a balance of Rs. 50,000 on June 30, 2013. Her cash book shows a different balance. On examination it is found that

- 1 No record has been made in the cash book for a dishonor of a cheque for Rs. 500
- 2 Cheques paid into bank amounting to Rs. 7,000 were paid into the bank on June 28, 2013 and the same had not been entered in the pass book.
- 3 Bank charges of Rs. 600 have not been entered in the cash book



- 4 Cheques amounting to Rs. 18,000 issued to Mr. Karim not been presented for payment still.
- 5 Mr. Balu who owned Rs. 6,000 has directly paid the sum into the bank account.

Solution:

Bank Reconciliation Statement as on June 30, 2013

Particulars	Amount Rs.	Amount Rs.
Balance as per pass book		50,000
Add:		
Dishonor of a cheque not record in the cash book	500	
Chequees paid into bank, not collected	7,000	
Bank charges as per pass book not entered in the cash book	600	8,100
		58,100
Less:		
Cheques issued but not presented for the payment of Mr. Karim	18,000	
Amount directly paid by Mr. Balu in the bank	6,000	24,000
Balance as per cash book		34,100

Illustration: 3 When overdraft as per cash book is given

Prepare a bank reconciliation statement as at June 30, 2013 for Mr. Infant sales Private Limited for the information given below.

- 1 Bank overdraft as per cash book Rs. 11,045
- 2 Cheque issued on June 20, 2013 but not yet presented for payment Rs. 1,500
- 3 Cheques deposited but not yet credited by bank Rs. 2,275
- 4 Bills receivable directly collected by bank Rs. 4,720
- 5 Interest on overdraft debited by bank Rs. 1,211
- 6 Amount wrongly debited by bank Rs. 240



Solution:

Bank Reconciliation Statement as on June 30, 2013

Particulars	Amount Rs.	Amount Rs.
Overdraft balance as per cash book		11,045
Add:		
Cheques deposited but not yet credited by bank	2,275	
Interest on overdraft debited by bank	1,211	
Wrongly debited by bank	240	3,726
		14,771
Less:		
Cheque issued but not yet presented for payment	1,500	
Bills receivable collected by bank	4,720	6,220
Overdraft balance as per bank pass book		8,551

Illustration: 4

Mr. Anbu gives the following information regarding her bank account. It shows an overdraft balance of Rs. 13,000 on March 2013. This does not agree with the cash book balance.

- 1 Cheque amounting Rs. 3,000 were paid in to bank out of which only cheque amounting to Rs. 9,000 were credited by the bank
- 2 Cheque issued during March amounted in all to Rs. 22,000 out of this cheque amounting to Rs. 6,000 were unpaid till March 31, 2013
- 3 The bank was wrongly debited Account No. 1 with Rs. 1,000 in respect of a cheque drawn on Account No. 2
- 4 The account stands debited with Rs. 300 interest and Rs. 60 for bank charge
- 5 The bank has paid annual subscription of Rs. 200 to club according instruction.

Your are required to ascertain balance as per cash book.



Solution:

Bank Reconciliation Statement as on March 31, 2013

Particulars	Amount Rs.	Amount Rs.
Overdraft balance as per pass book		13,000
Add		
Cheque issued but not presented		6,000
		19,000
Less		
Cheque paid in to bank but not collected (30,000 – 9,000)	21,000	
Wrong debited in pass book in Account No. 1 instead of Account No. 2	1,000	
Interest and bank charges not entered in the cash book (300 +60)	360	
Subscription paid as per standing instruction	200	22,560
Balance as per cash book		- 3,560

Illustration: 5

The cash book of Mr. Selvakumar showed a bank balance on Rs. 2,760 on 31.7.2009. On comparison with the bank pass book the following particular were ascertain.

- i. Cheque paid but not yet credited in the pass book Rs. 6,000
 - ii. Cheque issued but not yet presented for payment Rs. 2,500
 - iii. Life insurance premium limited by the bank but not yet entered in the cash book Rs. 8,320
 - iv. Interest on debenture collected by the bank in pass book only Rs. 6,000
 - v. Bank column on the credit side of the cash book undercast by Rs. 110.
 - vi. Bank charges entered in the pass book only Rs. 70
- Prepare bank reconciliation statement.



Solution:

Bank Reconciliation Statement as on 31.07.2009

Particulars	Amount Rs.	Amount Rs.
Balance as per cash book		2,760
Add		
Cheque issued but not yet presented for payment	2,500	
Interest on debenture collected by the bank in pass book	6,000	8,500
		11,260
Less		
Cheque paid but not yet credited in the pass book	6,000	
Life insurance premium limited by the bank but not yet entered in the cash book	8,320	
Bank column on the credit side of the cash book	110	
Bank charges entered in the pass book	70	14,500
Overdraft as per pass book		- 3,240

Exercises

Theory Questions

1. What is bank pass book?
2. What is bank reconciliation statement?
3. When bank reconciliation statement is prepared?
4. Who prepared a bank statement?
5. Why is the preparation of bank reconciliation statement necessary?

Problems

1. Make a bank reconciliation statement of Mr. Sivakumar from the following particulars
 - i. Balance as per cash book Rs. 3,000
 - ii. Cheque deposited but not cleared Rs. 200
 - iii. Cheques issued but not presented for payment Rs. 300
 - iv. Interest allowed by bank Rs. 40
2. Prepare a Bank Reconciliation Statement as at 30 June 2012 for Gandhimathi & Co., from the information is given below.
 - i. Bank overdraft as per cash on 30 June 2012 Rs. 1,00,000



- ii. Cheque issued on 20 June but not yet presented Rs. 45,000
- iii. Cheque deposited but not yet credited to account Rs. 32,750
- iv. Bill for collection not advised by bank but credited to the account Rs. 47,200
- v. Interest deposited by bank on 27th June but no advised received Rs. 12,000
- vi. Subsidy received from Government Authority by bank on the customer behalf and credited to the account Rs. 22,000
- vii. Amount wrong debited by the bank Rs. 12,400
- viii. Amount wrong credited by the bank Rs. 25,000

3. From the following particulars ascertain the balance that would appear in the cash book of Thiruselvam on 30.6.2010.

- i. Overdraft as per pass book as on 30th June 2010 Rs. 5,640
- ii. Cheque issued but not presented for payment Rs. 2,800
- iii. Cheque deposited but not cleared 30th June 2010 Rs. 3,900
- iv. Interest on overdraft as per pass book Rs. 250
- v. Insurance premium paid the bank directly not entered in the cash book Rs. 400.
- vi. Interest on investment collected and credited by the bank Rs. 500.
- vii. In June 2010 Thiruselvem deposited a cheque for Rs. 500 and had entered this amount in the cash book but not proceeds credited in the pass book amounted Rs. 490.

4. On 31.3.2015 the cash book of Kanna showed a bank balance of Rs. 4,850. While verifying with the pass book the following facts were noted.

- i. Cheques sent in for collection before 31.3.2015 and not credited by the bank amounted to Rs. 845.
- ii. Cheques issued before 31.3.2015 but not presented for payment amounted to Rs. 885.
- iii. The banker has charged a sum of Rs. 100 towards incidental charges and credited interest Rs. 250.
- iv. The banker has given a wrong credit for Rs. 250.
- v. A customer has paid into bank directly a sum of Rs. 300 on 28.3.2015 which has not been entered in cash book.
- vi. A cheque for Rs. 200 sent for collection and returned unpaid has not been in the cash book

Prepare a Bank Reconciliation Statement.



CHAPTER – 4

RECTIFICATION OF ERRORS

MEANING

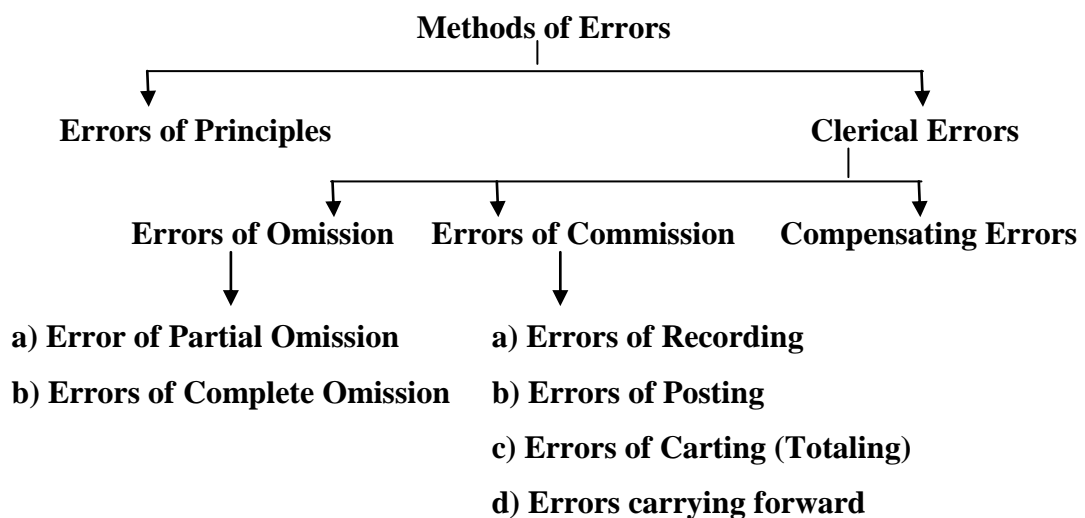
The fundamental principles of the double entry system are that every debit has a corresponding credit of equal amount and vice-versa. Therefore, the total of all debit balance in different accounts must be equal to the total of all credit balance in different accounts.

The transactions which are entered in the subsidiary books will be posted to ledger accounts and the ledger account would be closed at the end of an accounting period end a list of balances would be prepared know as trial balance. The agreement of the trial balance is not final and conclusive proof of accuracy of books of accounts. Thus, errors may be committed while recording, classifying or summarizing the financial transactions whether the trail balance agree or does not agree.

KINDS / METHODS OF ERRORS

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

- I) Errors of Principles and
- II) Clerical Errors





I) Errors of Principles

Transaction are recorded as per generally accepted a/c principles. When the transaction are entered in the books of principle. This error would not affect the trial balance.

For example

If the purchase of assets, the transaction recorded in the purchase book – so it errors of principle, because the purchase book is meant for recording credit purchase of goods meant for resale and not fixed assets.

II) Clerical Errors

These errors arise because of mistakes committed in the ordinary course of accounting work. The clerical errors in the three types.

1) Errors of Omission

The errors arises when a transaction is omitted to recorded in the boos of account. This error also does not affected the trial balance.

For example

If the purchase of goods from Raman is left unrecorded it is error of omission.

a) Errors of Complete Omission

This errors arises when a transaction is totally united to be recorded in the books accounts.

For example

Sales goods to Kumar this transaction completely omitted to be recorded in the journal, sales book. This error does not affected the trial balance.

b) Error of Partial Omission

This type of error arises when only are aspect of the transaction either debit or credit is recorded.

For example

Credit sale of goods to Arul recorded in sales book but omitted to be posted in the Arul accounts. This error affects the trial balance.

2) Errors of Commission

When the amount of a transaction is wrongly recording. posting, casting, balancing, camping forward etc., Errors of commission may be classified as follows.



a) Errors of Recording

This error arises when a transaction is wrongly recorded in the books of original entry.

For example

Good Rs. 10,000 purchased on credit from Raja, is recorded in the books for 10,500. This error does not affected the trial balance.

b) Errors of Posting

This error arises when information recorded in the books of original entry are wrongly entered in the ledger.

c) Errors of Carting (Totaling)

This error arises when a mistake is omitted while totaling the subsidiary books.

d) Errors carrying forward

This error arises when a mistake is omitted in carrying forward a total of one page to another page.

For example

Total purchase book in page 152 of the ledger Rs. 20,856, while carrying forward the balance to the next page it was recorded on Rs. 20,866.

3) Compensating Errors

The errors arising from excess debit or under debts of account being neutralized by the excess credits on under credits to the same extent of some other account is compensating error.

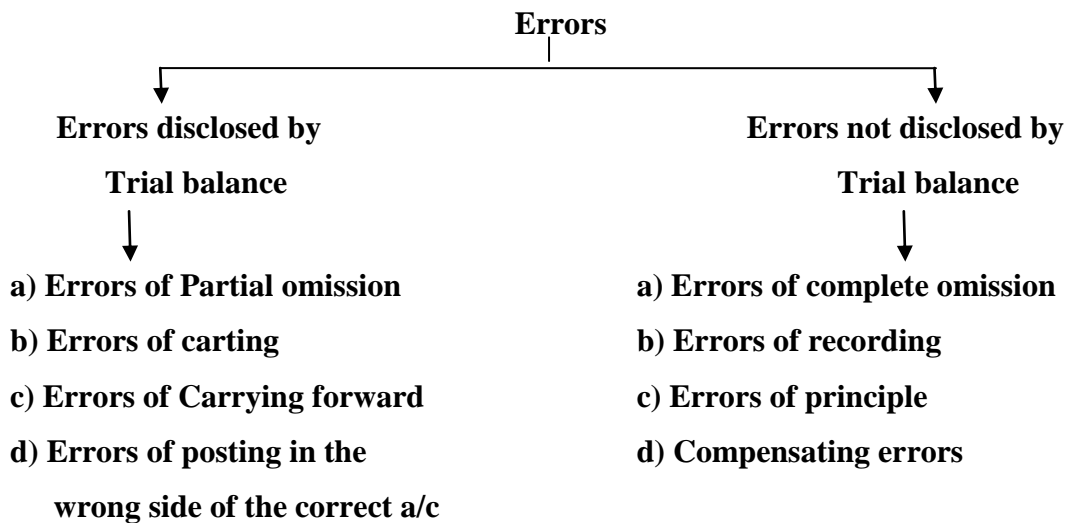
For example

If the purchase book and sales books are both overcast (excess totaling) Rs. 10,000. The errors mutually compensate each other. This error will not affected the agreement of trail balance.



ERRORS DISCLOSED AND NOT DISCLOSED BY TRIAL BALANCE

These are some errors which do not affect and affected the agreement of trial balance they are as follows.



Suspense Accounts

If the errors cannot be located immediately the difference in the trial balance may be temporary transferred to an account called “Suspense Account”, suspense account is prepared to avoid the delay in the preparation of final accounts. If the total debit balance of the trial balance exceeds the total credit balance the difference is transferred to the credit side of the suspense account.

Suspense account is a temporary and imaginary account which is closed later when the errors are located suspense account enables the final account to be prepared even before the location of the errors and avoids delay in the preparation of final accounts.

Illustration: 1

Rectify the following errors

- a) Purchase books is under cast by Rs. 500
- b) Sales book is overcast by Rs. 400
- c) Purchase returns boo has been under cast by Rs. 150
- d) Sales returns books has been overcast by Rs. 60



Solution:

- a) Debit: Purchase a/c with Rs. 500
- b) Debit: Sales /c with Rs. 400
- c) Credit: Purchase returns a/c with Rs. 150
- d) Credit: Sales returns a/c with Rs. 60

Illustration: 2

Rectify the following errors

- a) The total of sales books Rs. 867 has been carried forward as Rs. 876
- b) Purchase from Sudhan for Rs. 400 has been omitted to be posted to his account.
- c) Sales to Arun for Rs. 460 has been posted to his account as Rs. 640.
- d) Purchase from Anand for Rs. 300 has been posted to be debit of his account.
- e) Sales to Rajan for Rs. 530 has been posted to his credit as Rs. 350.

Solution:

- a) Debit: Sales a/c with Rs. 9
- b) Credit: Sudhar a/c with Rs. 400
- c) Credit: Aurn a/c with Rs. 180
- d) Credit: Anand a/c with 600 (300 + 300)
- e) Debit: Rajan a/c with 880 (530 + 350)

Illustration: 3

Rectify the following errors

- a) Purchase of machinery for Rs. 8,000 has been passed through purchase book.
- b) A credit purchase of Rs. 4,000 from Raja & Co., was omitted to be passed through the invoice book.
- c) Goods returned by Rani & Co., Rs. 700 posted to Vani & Co.,
- d) Rent paid Rs. 900 to proprietor's home was debited to rent.
- e) A credit purchase form Jayam Stores has been passed through the sales books day books Rs. 4,000.



Solution:

Rectification of journal entries

Particulars		Debit Rs.	Credit Rs.
a)	Machinery a/c Dr. To Purchase	8,000	8,000
b)	Purchase a/c Dr. To Rajan	4,000	4,000
c)	Vani & Co a/c Dr. To Rani a/c	400	400
d)	Drawings a/c Dr. To Rent	900	900
e)	Sales a/c Dr. Purchase a/c Dr. To Jeyam Stores	4,000 4,000	8,000

Illustration: 4

The trial balance showed Rs. 261 excess debit. It was made to agree by opening a suspense a/c. Later the following errors were discovered.

- A credit item of Rs. 349 has been debited to Sivakumar a/c Rs. 439
- A sum of Rs. 625 written off furniture has not been posted to depreciation.
- Rs. 9,000 spent for the purchase of machinery was charged to purchase.
- Rs. 154 being the discount allowed to a customer was posted to his a/c as Rs. 145
- A sale of Rs. 594 was posted to sales a/c as Rs. 495
- The total of the returns inwards book has been added Rs. 10 short

Rectify the above errors using suspense a/c



Solution:

Rectification of journal entries

Particulars		Debit Rs.	Credit Rs.
a)	Suspense a/c Dr. To Sivakumar a/c To Credit items a/c	788	439 349
b)	Depreciation a/c Dr. To Suspense a/c	625	625
c)	Machinery a/c Dr. To Purchases a/c	9,000	9,000
d)	Suspense a/c Dr. To Customer a/c	9	9
e)	Suspense a/c Dr. To Sales a/c	99	99
f)	Returns inwards a/c Dr. To Suspense a/c	10	10

Suspense a/c

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Sivakumar a/c	439	By Difference in trial balance	261
To Credit items a/c	349	By Depreciation a/c	625
To Customer a/c	9	By Returns inwards	10
	896		896



Exercises

Theory Questions

1. What do you mean by rectification of errors?
2. Explain the types of errors by giving suitable examples.
3. What do you mean by suspense account?
4. List out the errors disclosed and not disclosed by trial balance

Problems

1. Rectify the following errors
 - a) The sales book is under cast by Rs. 4,000
 - b) The purchase book is overcast by Rs. 3,000
 - c) The sales returns book is overcast by Rs. 10,000
 - d) The purchase books is overcast by Rs. 2,000
2. Rectify the following errors
 - a) Sales to Ravi Rs. 14,000 posted to Mathi a/c
 - b) Sales to Ravi Rs. 400 debited to Mathi a/c
 - c) Sales to Ravi Rs. 400 credited to Mathi a/c
 - d) Sales to Ravi Rs. 2,400 debited to Mathi a/c Rs. 400
3. Pass the Journal entries to rectify the following errors.
 - a) Rs. 1,000 spent for repairs on building has been posted to building a/c
 - b) A sale of Rs. 730 to Mothi has been entered in the sales book, as Rs. 370
 - c) Goods worth of Rs. 500 purchased from Bala have been omitted to be recorded in the books
 - d) Rs. 400 paid as salary to a clerk has been debited to his personal a/c
 - e) Rs. 75 discount allowed by a creditors has been debited to discount a/c
 - f) The total of sales book has been added Rs. 100 excess.
 - g) Office furniture purchased for Rs. 1,800 has been passed through the purchase book.



4. Give journal entire to rectify the errors in the following transactions
- a) Furniture and fittings for Rs. 230 purchase has been entered in the purchase books.
 - b) Repairs to furniture Rs. 130 has been debited to furniture and fittings a/c
 - c) Wages paid Rs. 250 for installation of new machine are debited to wage a/c
 - d) Purchase book was under cast by Rs. 100
 - e) Salary Rs. 500 paid to Ram was debited to his a/c
5. The book keeper of affirm having been unable to agree the trial balance on 31st December 2015 realized a suspense account as investigation for final the following errors.
- a) Good purchased form cash a Dass & Co., amounting to Rs. 1,760 has been posted to the debit of their amount as Rs. 17.60 from the purchase book.
 - b) The purchase book has been under cast on page 14 by Rs. 500
 - c) Rs. 4,600 paid for repair to building was charged to building a/c
 - d) A cheque for Rs. 301.02 received from Gopalan has been posted to his account as Rs. 302.01.

Show the journal entire which are necessary to correct the above errors.



UNIT II : BILLS OF EXCHANGE

Bills of exchange – honouring and dishonouring of bills – renewal of bills – retirement of bills – insolvency of acceptor – trade and accommodation bills

CHAPTER – 5 BILLS OF EXCHANGE

BILLS OF EXCHANGE – MEANING

A trader very often buys and sells goods on credit. In such cases, the value of goods will be paid or received only at a future date. A written proof or document is prepared to acknowledge the amount payable or receivable. Such a document is called a Bills of Exchange. For example, Rajan sells goods on credit to Balan. In such case, Rajan drawn a Bills of Exchange of Balan for the amount due, directing Balan to pay the amount at a certain future date. Balan accepts the bill by signing it without the word ‘Accepted and sends the bills to Rajan.

DEFINITION

Section 5 of the Negotiable Instruments Act 1881 defines a Bills of Exchange as “an instrument in writing containing an unconditional order signed by the maker, directing a certain person to pay a certain sum of money only to or to the order of a certain person or to the bearer of the instrument”.

The following is the specimen of a bill of exchange.

Rs. 5,000	420 Kamarajar Street Thoothukudi August 5, 2015
Two months after date, pay to us or our orders, the sum of Rupees five thousand only for value received.	
For Mr. Selvan Gandhi Nager Tirunelveli	

FEATURE 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 related to the payment of certain sum of money with must be easily determinable.
5. The person on whom the order is directed 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 ager a certain period.

PROMISSORY NOTE – MEANING

A promissory note is an instrument is writing, containing an unconditional undertaking signed by the maker to pay a certain sum of money only to or to the order of certain person. Under Section 31(2) of the Reserve Bank of India Act, a promissory note cannot be made payable to a bearer.

FEATURES

1. It must be in writing.
2. It must contain a clear promise to pay. Mere acknowledgement of debt is not a promise.
3. The Promise to pay must be unconditional. “I promise to pay Rs. 50 as soon as I can” – It is not an unconditional promise.
4. The promisor or maker must sign the promissory note.
5. The maker must be a certain person.
6. The payee (the person to whom payment is promised) must also be certain.
7. The sum payable must be certain “I promise to pay Rs. 500 plus all fines” is not certain.
8. Payment must be in legal money of the country.
9. It should not be made payable to bearer.
10. It should be properly stamped.



SPECIMEN OF A PROMISSORY NOTE

PROMISSORY NOTE	
Rs. 10,000/-	Madurai
	November 5, 2015
Three months after date we promise to pay M/S Chendur& Co., or order the sum of Ten thousand rupees with interest 6% per annum for value received	
	Stamp
	M/S Chendur& Co.,

HUNDIES

Instruments drawn in Indian languages and made payable according to the custom prevailing in the local markets are known as Hundies. The practical effect of hundies is the same as that of bills of exchange and promissory notes.

DIFFERENCE BETWEEN BILL OF EXCHANGE AND PROMISSORY NOTE

No.	Bills of Exchange	Promissory Note
1	In a bill of exchange, there is an order to pay	In a promissory note, there is a promise to pay
2	A bill of exchange requires to be accepted by the drawee	For a promissory notes no acceptance is necessary
3	There are three parties – The drawer, drawee and the payee	There are two parties – the maker and the payee
4	Its drawer is liable only when the drawee does not accept or pay the amount due	Its maker is primarily liable
5	In case of dishonor, a foreign bill must e protested if it is necessary accounting to law of the place where it is drawn.	In case of dishonor, protest is not necessary.



ADVANTAGES OF BILLS OF EXCHANGE

1. Since it is a written and signed acknowledgement of debt, it serves as a conclusive proof of indebtedness.
2. It fixes the date of payment.
3. It ensures prompt payment by a debtor.
4. The debtor enjoys the full period of credit, because he will not be called upon to pay the amount of the bill before the due date.
5. Even before the due date, the creditor of a bill can realize money by discounting it with a banker.
6. It can be transferred like the coin of the country since it is a negotiable instrument.
7. It enables the trader to get goods on credit basis. This increases the volume of trade.

TYPES OF BILLS OF EXCHANGE

1. Inland Bills

Inland bills are drawn and payable in the same country. For instance, if a merchant in Chennai draws a bill on a merchant in Kolkatta, it becomes an inland bill.

2. Foreign Bills

Foreign bills are drawn in one country but payable in another country. For instance, if a merchant in Chennai draws a bill on a merchant in London, it becomes a foreign bill.

3. Time Bill

A bill which is payable at the expiry of a certain period after date or after sight, it is called a time bill.

4. Demand Bill

A bill of exchange which is payable on demand is known as demand bill.

5. Order Bill

A bill of exchange which is expressed to be payable to order is called an order bill. It should not contain words restricting any transfer. Example: Pay to Mr. R Seshadhri Only.

6. Bearer Bill

A bill of exchange which is expressed to be payable to a bearer is called a bearer bill. Example: Pay to Mr. Seshadhri or bearer



7. Documentary Bill

A documentary bill is a bill of exchange drawn by the exporter on the importer which is accompanied by shipping documents to be handed over to the importer upon his acceptance or payment of the bill. The shipping documents are usually attached to documentary bill. A documentary bill may be either (a) D/A bill or (b) D/P bill.

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 due 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.	<p>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</p>	<p>Debit the personal a/c of the drawer, because he receives the bill Credit B/P a/c, since the bill goes out</p>
2.	<p>When a B/R is duly honoured Debit cash a/c, since it comes in Credit B/R a/c, since it goes out</p>	<p>When a B/P is duly honoured Debit B/P a/c, since it comes in Credit Cash a/c, since it goes out</p>
3.	<p>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</p>	<p>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</p>
4.	<p>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</p>	No entry is required
5.	<p>When a B/R is endorsed to a person Debit the Received a/c</p>	No entry is required



	Credit B/R a/c since it goes out	
6.	When discounted (or) endorsed bill is honoured <p style="text-align: center;">No entry</p>	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 is dishonoured Debit the Acceptor'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 Acceptor'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 a Bill is noted by the drawer Debit B/P a/c with the value of the bill to cancel the original bill. Debit Nothing 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 since the amount (inclusive of nothing charges) is due from him. Credit the Bank a/c with nothing charges	When a B/P is noted by the Banker Debit B/P a/c with the value of the bill to cancel the original bill. Debit Nothing charges a/c, since it is a loss to us Credit the Drawer's a/c, because we are liable to pay him
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<p>11.</p>	<p>When a B/R is noted by the endorse Debit the Acceptor's a/c since the amount is due from him (including nothing charges) Credit the endorsee's a/c with nothing charges. Credit B/R a/c, Since it goes out</p>	<p>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 Nothing charges a/c, since it is a loss to us Credit the Drawer's a/c, because we are liable to pay him</p>
<p>12</p>	<p>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</p>	<p>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.</p>
<p>13</p>	<p>When a B/R is retired Debit Cash a/c, since cash comes in. Rebate a/c, since it is a loss to us. Credit B/R a/c, since it goes out.</p>	<p>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.</p>
<p>14.</p>	<p>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</p>	<p>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</p>



	<p>(or) b) When it is dishonoured</p> <p>Debit the Drawee's a/c</p> <p>Credit Bill for Collection a/c</p>	<p>Debit B/P a/c is order to cancel the original bill</p> <p>Credit the Drawer's a/c. Since we are liable to pay the amount due to him.</p>
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Now you know the entries for bills. Let us illustrate the above entries in the following examples.

Illustration: 1 When bill is drawn, accepted and honoured

On 1st Jan.2014 'A' drew a two months bill on 'B' for Rs. 5,000 and the latter accepted the same. On the due date 'B' met the bill. Show the Journal Entries.

Solution:

In the books of 'A'

Date	Particulars	Debit Rs.	Credit Rs.
01.01.2014	Bills receivable a/c Dr. To 'B' a/c (being the entry for the receipt of the bill)	5,000	5,000
04.03.2014	Cash a/c Dr. To Bills receivable a/c (being the realization of the bill)	5,000	5,000

In the books of 'B'

Date	Particulars	Debit Rs.	Credit Rs.
01.01.2014	A's a/c Dr. To Bills payable a/c (being the acceptance given to A)	5,000	5,000
04.03.2014	Bills payable a/c Dr. To cash a/c (being the entry for the honour of the bill)	5,000	5,000



Illustration: 2 When bill is drawn, accepted and dishonoured

For goods supplied, 'A' draws a bill on 'B' for 2,000. '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 To sales a/c (being the goods sold 'B' on credit)	Dr.	2,000	2,000
Bills receivable a/c To B's a/c (being the bill received from B)	Dr.	2,000	2,000
B's a/c To Bills receivable a/c (being B refuse to honour the bill)	Dr.	2,000	2,000

In the books of 'B'

Particulars		Debit Rs.	Credit Rs.
Purchase a/c To A's a/c (being the acceptance given to X)	Dr.	2,000	2,000
A's a/c To Bills payable a/c (being the acceptance given to A)	Dr.	2,000	2,000
Bills Payable a/c To A's a/c (being the payment not made)	Dr.	2,000	2,000

Illustration: 3 When bill is dishonoured and the Noting Charges paid



'N' owes 'M' 1,000. 'M' draws a two months bill for Rs.100 on 'N' on 01.07.2013 '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. 50 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. To 'N' a/c (being the bill received)	1,000	1,000
04.09.2013	N's a/c Dr. To Cash a/c To Bills receivable a/c (being the bill dishonoured and noting charges paid)	1,050	50 1,000

In the books of 'N'

Date	Particulars	Debit Rs.	Credit Rs.
01.07.2013	M's a/c Dr. To Bills payable a/c (being the bill accepted)	1,000	1,000
04.09.2013	Bills payable a/c Dr. Noting Charges a/c Dr. To M's a/c (being the bill dishonoured and noting charges paid by the drawer)	50 1,000	1,050

Illustration: 4 When bill is discounted and honoured

Aurnsold goods to Raman on 5th February 2013 and draws a 3 months bill on Raman for Rs. 5,000 Aurn 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 2013. The discount charge should be calculated for the period of 3 months, i.e., from 8th February to 8th May. Hence the discount is:

$$5,000 \times 10 / 100 \times 3 / 12 = \text{Rs. } 125$$

Solution:

In the books of 'Aurn'

Date	Particulars	Debit Rs.	Credit Rs.
Feb 5.	Raman a/c Dr. To sales a/c (being credit sales)	5,000	5,000
Feb. 5	Bills receivable a/c Dr. To Raman a/c (being the acceptance received)	5,000	5,000
Feb. 8	Bank a/c Dr. Discount a/c Dr. To Bills receivable (being the amount received on discounting the Bill)	4,875 125	5,000
May 8	No entry		

In the books of 'Raman'

Date	Particulars	Debit Rs.	Credit Rs.
Feb 5.	Purchase a/c Dr. To Aurn a/c (being credit purchase)	5,000	5,000
Feb. 5	Aurna/c Dr.	5,000	



	To Bills payable a/c (being the acceptance given)		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. 4,500. On the same date Ram drew a few 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 bank. Show journal entries

Solution:

Journal of Ram

Date	Particulars	Debit Rs.	Credit Rs.
2014			
Jan. 6	Mohan a/c Dr. To sales a/c (being credit sales)	4,500	4,500
Jan. 6	Bills Receivable a/c Dr. To Mohan a/c (being the acceptance received)	4,500	4,500
Jan. 9	Bank a/c Dr. Discount a/c Dr. To Bills receivable a/c (being the amount received on discounting the bill)	4,350 150	4,500
April 9	Mohan Dr. To Bank a/c (being the amount paid on dishonor of)	4,500	4,500



	Mohan's acceptance)		
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Journal of Mohan

Date	Particulars	Debit Rs.	Credit Rs.
2014			
Jan. 6	Purchase a/c Dr. To Ram a/c (being credit purchase)	4,500	4,500
Jan. 6	Ram a/c Dr. To Bills Payable a/c (being the acceptance given)	4,500	4,500
Jan. 9	No entry		
April 9	Bills payable a/c Dr. To Ram a/c (being the credit given to Ram on dishonout of our acceptance of Jan.6)	4,500	4,500

Note: Discount = $4,500 \times 10/100 \times 4/12 = 150$

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.
2004			
Jan. 1	Q a/c Dr. To Sales a/c (being credit sales)	2,000	2,000



”	Bills receivable To Q a/c (being the acceptance received)	Dr.	2,000	2,000
”	R a/c To Bills Receivable a/c (being the transfer of Q’s acceptance in favour of R)	Dr.	2,000	2,000
March 4	No entry			

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.
2004 Jan. 1	Purchase a/c To P a/c (being credit purchase)	Dr.	2,000	2,000
”	P a/c To Bills Payable a/c (being the acceptance received)	Dr.	2,000	2,000
”	No entry			
March 4	Bills payable To Cash a/c (being the cash paid on maturity of our acceptance)	Dr.	2,000	2,000

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 2003 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.
2013			
Oct. 3	Y a/c Dr. To Sales a/c (being credit sales)	4,000	4,000
Oct. 3	Bills receivable a/c Dr. To Y a/c (being the acceptance received)	4,000	4,000
Oct. 3	Z a/c Dr. To Bills Receivable a/c (being the transfer of Y's acceptance in favour of Z)	4,000	4,000
2014			
Jan. 6	Y a/c Dr. To Z a/c (being the credit to Z on dishonor of Y's acceptance)	4,000	4,000

Journal of 'Z'

Date	Particulars	Debit Rs.	Credit Rs.
2013			
Oct. 3	Purchase a/c Dr. To P a/c (being credit purchases)	4,000	4,000
Oct. 3	X a/c Dr. To Bills Payable a/c	4,000	4,000



	(being the acceptance received)		
	No Entry		
2014			
Jan. 6	Bills payable a/c To X a/c (being dishonour of our acceptance dated Oct. 3)	Dr. 4,000	 4,000

Illustration: 8 On retiring the bill

On 1st June.2013, '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 'X'

Date	Particulars	Debit Rs.	Credit Rs.
01.06.2013	Bills receivable a/c To 'Y' a/c (being the entry for the receipt of the bill)	Dr. 300	 300
”	Cash a/c Rebate a/c To Bills receivable a/c (being the entry for the realization of the bill before the due date)	Dr. Dr. 295 5	 300

In the books of 'Y'

Date	Particulars	Debit Rs.	Credit Rs.
01.06.2013	X's a/c To Bills payable a/c (being the acceptance given to X)	Dr. 300	 300



”	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. 200 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.	500	
	To B/R a/c			500
	(being cancellation of the original bill)			
b)	B's a/c	Dr.	15	
	To interest a/c			15
	(being the interest due)			
c)	B's a/c	Dr.	200	
	B/R a/c	Dr.	315	
	To B a/c			515
	(being cash and 2 nd bill received)			

Journal of ‘B’

	Particulars		Debit Rs.	Credit Rs.
a)	Bills payable a/c	Dr.	500	
	To A a/c			500
	(being the cancellation of the bill)			
b)	Interest a/c	Dr.	15	
	To A a/c			15
	(being the interest due)			



c)	A's a/c	Dr.	515	
	To cash a/c			200
	To bills payable a/c			315
	(being cash and new acceptance given)			

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 Goul for Rs. 4,000 on 1st March, 2014, the same day he gave a promissory note for the amount payable after two months. On 4th March, this was discounted by Goul with his baners at the rate of 6% per annum. The promissory note was dishonoured on the due date and that the baners have incurred noting charges of Rs. 20. When approached by Rahul, Goul 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. To Sales a/c (being the sale of goods on credit to Rahul)	4,000	4,000
March 1	Bills Receivable a/c Dr. To Rahul (being Receipt of promissory note from Rahul)	4,000	4,000
March 4	Bank a/c Dr. Discount a/c Dr. To Bills receivable a/c (being Amount received on discounting the bill)	3,960 40	4,000
May 4	Rahul a/c Dr. To Bank a/c (being the bill is dishonoured and noting charges paid by the Bankers)	4,020	4,020
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 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 To Bills Receivable a/c (being the bill dishonoured to Trishul)	Dr.	1,000	1,000
July 7	No entry			
Aug. 7	Rahul a/c To Bills Receivable a/c (being the bill dishonoured this day)	Dr.	2,000	2,000
Aug. 7	Cash a/c Bad debts a/c To Rahul a/c (being receipt of first and final dividend of 40 paise in the Rupee from the estate of Rahul)	Dr. Dr.	800 1,200	2,000

Journal of Rahul (Acceptor)

Date	Particulars		Debit Rs.	Credit Rs.
2014				
March 1	Purchase a/c To Gokul a/c (The purchase of goods from Gokul)	Dr.	4,000	4,000
March 1	Gokul a/c To Bills payable a/c (Our promissory note given to Gokul)	Dr.	4,000	4,000
May 4	No entry			
May 4	Bills payable a/c Noting Charges a/c To Gokul a/c (The bill dishonoured this day)	Dr. Dr.	4,000 200	4,200



May 4	Gokul a/c To Cash a/c To Bills Payable a/c (payment of cash and issue of two promissory notes – one at months for Rs. 1,000 and the other at 3 months for Rs. 2,000 to Gokul)	Dr.	4,060	1,060 3,000
May 4	No entry			
July 7	Bills payable a/c To Cash a/c (The bill met at maturity)	Dr.	1,000	1,000
Aug. 7	Bills Payable a/c To Gokul a/c (the bill dishonoured this day)	Dr.	2,000	2,000
Aug. 7	Gokul a/c To Cash a/c To Deficiency a/c (Payment of 40 paise in the Tupee as first and final dividend to Gokul)	Dr.	2,000	800 1,200

Ledger in the books 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	
May 4	To bank a/c	4,00		a/c	4,000
May 4	To interest a/c	40	May 4	By cash a/c	1,060
Aug. 7	To bills receivable		May 4	By bills receivable	
	a/c	2,000		a/c	3,000



			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

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?

Exercise

- 1) On 1st Jan 2015, 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 bank 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.

3) Mohan purchased goods from Shanmugam for Rs. 4,000 on 1.1.2014. Mohan accepted three months bill for the amount due. At its due date the bill is dishonoured nothing charged are paid by Shanmugam Rs. 15. Give journal entries in the books of Shanmugam.

4) On 1st August 2000 X sold goods of Rs. 500 to Y and draw a three months bill on Y. Y accepted the bill and return it to X. On due date, Y unable to meet the bill and approached X to renew the bill for two months with interest 6% p.a. X agreed for this on the due date the second bill was honoured pass journal entries in the books of two parties



UNIT III : ACCOUNTS OF NON-TRADING CONCERNS

Accounts of non-trading concerns – receipts and payment accounts – income and expenditure account – differences – preparation of balance sheet

CHAPTER – 6

ACCOUNTS FOR NON – TRADING CONCERN

MEANING

Non – Trading concerns (or) association are those concerns which are established for the purpose of rendering service to the public. They are also called as non-profit motive organisation. Eg. Schools, Colleges, Library, Sports clubs, Social clubs, Hospitals etc.,

Non – Trading concerns are non – profit organisation they do not prepare trading and profit and loss a/c like a business or trading organisation. But in order to know the closing cash and bank balance and the surplus (or) deficit, they prepare the following books of accounts.

- a) Receipts and Payments a/c
- b) Income and Expenditure a/c and
- c) Balance sheet

a) Receipts and Payments a/c

It is a summary of cash transactions under various heads, prepared at the end of the year to know the nature of the transactions. Both of the capital and revenue receipts and payments are entered here. It takes into account the receipts and payments relating to previous, current and subsequent years. It starts with opening cash and bank balance and ends with closing cash and bank balance. It is like a cash book

The format of a Receipts and Payments a/c is given below.

Receipts and payment a/c for the year ended 31st March 2016

Dr.

Cr.

Date	Receipts	Amount Rs.	Date	Payments	Amount Rs.
1.4.15	To Balance b/d			By Honorarium	***
	Cash	***		By Rent	***
	Bank	***		By Interest	***



31.3.16	To Subscription	***	By Sport expenses	***	
	To Entrance fees	***		By Balance c/d	
	To Sale of old news paper	***		Cash	***
		***		Bank	***
		***			***

INCOME AND EXPENDITURE ACCOUNT

Income and Expenditure a/c is the summary of income and expenditures of the whole year. It is like a profit and loss a/c prepared on accrual basis to find out the surplus and deficit unlike the receipts and payment a/c the income and expenditure a/c takes into a/c only the revenue expenditure and receipts. Also it takes into a/c of the expenditure and income of the whole year whether paid / received or not. It is a nominal account.

The format of a Income and Expenditure a/c is given below

Income and Expenditure a/c for the year ended 31st March 2016

Dr.

Cr.

Expenditure	Amount Rs.	Income	Amount Rs.
To Rent	***	By Subscription	***
Add: O/S for the current year	***	Add: O/S for the current year	***
Less: O/S for the previous year	***	Less: O/S for the previous year	***
Less: Prepaid during the current year	***	Less: Prepaid during the current year	***
Add: Paid in advance in the previous year	***	Add: Paid in advance in the previous year	***
To Salary	***	By Sports receipts	***



To Depreciation	***	By Sale of news paper	***
To Surplus (or) Excess of Income over Expenditure	***	By Deficit on Excess of Expenditure over Income	***
	***		***

Distinguish between Receipts and Payments a/c and 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 a summary of cash a/c	It is summary of income and expenditure
3.	It starts with opening balance of cash, and bank	It does not start with opening balance
4.	All receipt are entered on the debit side, all payment are entered on the credit side.	All income are entered on the credit side, all the expenses are entered in the debit side.
5.	It takes into a/c both revenue and capital receipts, it takes into a/c both revenue and capital receipts.	It takes into account only the revenue income. It takes into a/c only the revenue expenditure.
6.	It takes into a/c the receipts relating to previous, current and subsequent years.	It takes into a/c of income only current year.
7.	It ends with the closing balance of cash and bank	It ends with the surplus (or) deficit

How would you deal with the important items like donation, legacy etc., in the final accountant of a non-trading concern

The non-trading organisation prepare a balance sheet as prepared by any trading organisation. But the only difference is that the 'capital' is here denoted as 'capital fund' or 'special fund'. If capital fund is not give directly in the problem, it is to be found by preparing a opening or previous year balance sheet. Meaning of some items relating to non-trading organisations are:



a) Subscription

It is the fee to be remitted by the members of the club/association to the non-trading organisation, either monthly or quarterly or half-yearly or annually. It is a revenue receipt, to be credited to income & expenditure a/c

b) Legacy

It is the amount of gift given to non-trading concerns by the members as per their will. It appears on the receipts side or receipts and payments a/c. as it is a capital receipt, it is directly added to the capital fund on the liability side of the balance sheet.

c) Donations

It is the amount of gift given by any person / body / company to the non-trading concerns. It appears on the receipt side of receipts and payments a/c. The accounting treatment (whether revenue or capital receipt) of donations is not the same in all problems. It depends on the directive given in the problem. If the problem does not specify, the accounting treatment, the following may be assumed.

If the amount of donation is greater than Rs. 500, treat it as capital receipt. Hence transfer this to liability side of balance sheet.

If the amount of donation is less than Rs. 500 treat it as revenue receipt. Transfer the same to the credit side of the Income & Expenditure a/c.

d) Entrance fee

It is the amount paid by the members of the concerns at the time of admission. Its accounting treatment is as per the directive given in the problems. If it is silent about its treatment, treat it as capital receipt. Hence transfer this to the liability side of balance sheet.

e) Life membership fee

Instead of paying the subscription on a periodic basis, members may pay a one time lump-sum amount as their subscription which is called life membership fee. It appears on the receipt side of the receipts & payments a/c. it is capital receipt, hence taken to the liability side of the balance sheet.

f) Sale of old newspapers

It appears on the receipt side of the receipts & payments a/c. it is a revenue receipt, therefore it is to be credited to the income & expenses a/c.



g) Sale of old assets

Only the loss or gain on sale of assets is debited or credited to income and expenditure a/c, as the case may be the book value of the assets sold is deducted from the total value of the asset and only the balance is shown on the asset side of the balance sheet, after providing depreciation.

h) Sale of old sport material

The appears on the receipt side of the receipts & payments a/c. it is a revenue receipt, hence it is credited to income and expenditure a/c

i) Purchase of sports materials

This appears on the payments side of the receipts & payments a/c. As a revenue expenditure, debited to the income and expenditure a/c.

j) Purchase of billiard tables

This appears on the payments side of the receipt & payment a/c. It is a capital expenditure. Hence it is taken to the assets side of the balance sheet.

k) Purchase of Bi-cycle, bonds

These items appear on the payments side of receipts & payments a/c. They are capital expenditures and shown on the asset side of the balance sheet.

l) Payment of Honorarium to the secretary

It appears on the payments side of receipts & payments a/c. It is a revenue expenditure and shown on the debit side of income and expenditure a/c.

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	It revenue expenditure there is no such right	In deferred revenue expenditure also there is no such right

BALANCE SHEET

Balance sheet of a non-trading concern is prepared in the usual way as it is prepared for a trading concern. The excess of asset, over liabilities is known as capital fund (or) general fund. Any surplus (or) deficit from the income and expenditure account is adjusted with the capital fund. Special funds are shown separately in the liabilities side and any income with to the special fund and any expenditure incurred for that purpose are adjusted in the special fund is sale.

Specimen of Balance sheet



Balance sheet

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital fund	***	Cash in hand	***
Add: Surplus	***	Cash at bank	***
	***	Sports equipment	***
Specific fund	***	Furniture	***
Subscription received in advance	***	Building	***
Outstanding expenses	***	Prepaid expense	***
	***	Outstanding income	***
	***		***

Illustration: 1

The Receipt and Payment account for the year ended 31.12.2012 showed a debit entry of Rs. 1,00,000. From the information available, it is found that.

Subscription outstanding on 31.12.2011 was Rs. 20,000

Subscription outstanding on 31.12.2012 was Rs. 40,000

Subscription received in advance as on 31.12.2011 was Rs. 30,000

Subscription received in advance as on 31.12.2012 was Rs. 20,000

Calculate the income from subscription for the year ended 31.12.2012

Solution:

Calculation of the Income from subscription for the year ending 31.12.2012

Particulars	Amount Rs.	Amount Rs.
Subscription as per receipts and payments a/c 2012		1,00,000
Add:		
Subscription outstanding as on 31.12.2012	40,000	
Subscription received in advance as on 31.12.2011 for 2012	30,000	70,000
		1,70,000
Less:		
Subscription outstanding as on 31.12.2011 received in 2012	20,000	



Subscription received in advance as on 31.12.2012 for 2013	20,000	40,000
Income from Subscription for the year ending 31.12.2012		1,30,000

Note: Income outstanding for the current year is added and income received in advance is deducted and reverse is the treatment for the previous year's figures.

Any income / Expenses hereby to last year (or) next year of included in the current year should be deducted.

Illustration: 2

From the following information, preparing the Income and Expenditure a/c

	Rs.
Subscription received during the year 1.1.2015	12,000
Subscription receivable for 1.01.2015	400
Subscription received in advance during the year 31.12.2015	600
Subscription received in advance during the year 1.1.2015	800
Subscription receivable for 31.12.2015	750

Solution:

Income and Expenditure Account for the year ended 31st March 2016

Dr.

Cr.

Expenditure	Amount Rs.	Amount Rs.	Income	Amount Rs.	Amount Rs.
			By Subscription		12,000
			Add: Subscription received in advance during 31.12.2015	600	
			Add: Subscription o/s for 31.12.2015	750	1,350
					13,350
			Less: Subscription received in advance during 1.01.2015	800	



			Less: Subscription		
			o/s for 31.12.2015	400	1,200
					12,150

Illustration: 3

How will the following appear in the final accounts Tirunelveli sports club

Stock of sports materials on 1.1.2015	Rs. 10,000
Sports materials purchased during 2015	Rs. 36,000
Sale of old sports materials during 2015	Rs. 800
Stock of sports materials on 31.12.2015	Rs. 4,000

Solution

Tirunelveli Sports Club

Income and Expenditure Account for the year ended 31st December 2015

Dr.

Cr.

Expenditure	Amount Rs.	Amount Rs.	Income	Amount Rs.	Amount Rs.
To Sports Materials			By Sale of old sports materials		800
Opening stock	10,000				
Add: Purchases	36,000				
	46,000				
Less: Closing stock	4,000	42,000			

Balance sheet as on 31st December 2015

Liabilities	Amount Rs.	Assets	Amount Rs.
		Stock of sports materials	4,000

Sports materials consumed during the year is Rs. 42,000 (i.e. 10,000 + 36,000 – 4,000 = 42,000) which appears on the debit side of the income and expenditure account for



the year ended 31.12.2015. Sale of sports materials Rs. 800 being revenue receipt will appear on the credit side of the income and expenditure account.

The closing stock of sports materials Rs. 4,000 will appear as an asset in its balance sheet as on 31.12.2015.

Illustration: 4

From the following information, determine the amount to be debited to Income and Expenditure a/c and the amount to be shown on the balance sheet.

	Rs.
Stock of Stationery on 1.4.2015	2,500
Stock of Stationery on 31.3.2016	1,000
Purchase of Stationery during the year 2015 – 2016	28,000
Stationery bill O/S for 1.4.2015	1,200
Stationery bill O/S for 31.3.2016	2,000
Stationery paid in advance on 31.3.2015	1,400
Stationery paid in advance on 31.3.2016	1,800

Solution:

Income and Expenditure Account for the year ended 31st December 2015

Dr.

Cr.

Expenditure	Amount Rs.	Amount Rs.	Income	Amount Rs.	Amount Rs.
Opening stock of stationery		2,500			
Add:					
Purchases Stationery bill paid in advance on 31.3.2015	28,000 1,400				
O/S on 31.3.2016	2,000	31,400			
		33,900			
Less: Closing stock Stationery bill paid	1,000				



in advance on 31.3.2016	1,800				
O/S on 1.4.2015	1,200	4,000			
		29,900			

Illustration: 5

From the following information of Tirunelveli Sports Clube you are required to prepare the receipts and payment a/c for the year ended 31st March 2015

	Rs.		Rs.
Balance on 1.4.2014		Honorarium paid	80,000
Cash	50,000	Billiard table purchased	4,00,000
Bank	30,000	Sports meet collection	1,80,000
Transaction during the year		Sports expenses	1,20,000
Entrance fee	45,000	Interest paid	56,000
Donation	2,70,000	Purchase of news paper	10,000
Legacy	1,60,000	Sale of news papers	6,000
Life membership fee	60,800	Balance on 31.03.2016	
Rent paid	90,000	Cash	25,000
Stationery purchased	18,000		
Subscription			
2013 – 2014	58,000		
2014 – 2015	3,70,000		
2015 – 2016	32,000		

Solution:

**Receipts and payments a/c of Tirunelveli Sports Clubs
for the year ended 31.03.2016**

Dr.	Amount Rs.	Amount Rs.	Cr.	Amount Rs.	Amount Rs.
To Balance b/d			By Rent paid		90,000
Cash	50,000		By Stationery		
Bank	30,000	80,000	purchased		18,000



To Entrance fee		45,000	By Honorarium	
To Donation		2,70,000	paid	80,000
To Legacy		1,60,000	By Billiard table	
To Life membership fee		60,800	purchased	4,00,000
			By Sports expenses	1,20,000
To Subscription			By Interest paid	56,000
2013 – 2014	58,000		By Purchase of	
2014 – 2015	3,70,000		news paper	10,000
2015 – 2016	32,000	4,60,000	By Balance c/d	
To Sports meet collection		1,80,000	Cash	25,000
To Sale of news papers		6,000	Bank (b.f.)	4,62,800
		12,61,800		12,61,800

Illustration: 6

From the following particulars prepare income and expenditure account of the Nagerkovil Sports Society for the period ending 31st March 2014

Particulars	Received or	Outstanding
	Paid	on 31.3.2014
	Rs.	Rs.
Subscription from members	4,60	–
Subscription from societies	1,40	20
Life membership fees	2,00	–
Gifts received	3,00	–
Interest received	16	–
Committee expenditure		
Executive	1,50	20
Planning	1,44	64
Tournament	42	12
Printing, Postage & Stationary	1,14	16
Office furniture	2,00	–



Investments purchased

3,00

–

Solution

Nargerkovil Sport Society

Income and Expenditure Account for the year ended 31st March 2014

Dr.

Cr.

Expenditure	Amount Rs.	Amount Rs.	Income	Amount Rs.	Amount Rs.
To Committee			By Subscription		
Expenditure			from members		460
To Executive	150		By Subscription		
Add: Outstanding	20	170	from societies	140	
To Planning	144		Add: Outstanding	20	160
Add: Outstanding	64	208	By Gifts received		300
To Tournament	42		By Interest		
Add: Outstanding	12	54	received		16
To Printing, Postage & Stationary	114				
Add: Outstanding	16	130			
To Surplus (b.f.)		374			
		936			936

Note: Life membership fees are a capital receipt and so it was not taken in will not come into the income and expenditure account. Purchase of furniture and investments being capital expenditure, they were also not taken in the income and expenditure account.

Illustration: 7

From the information given below prepare an Income and Expenditure a/c for 2015

	Rs.		Rs.
Opening Balance		Salaries	48,000
Cash	2,000	Rent	5,000



Bank	16,000	Stationery & Postage	2,000
Subscriptions		Bicycle purchased	3,000
2014	5,000	National savings certificates	30,000
2015	83,000	Help to poor students	20,000
2016	6,000	Closing Balance	
Sale of investments	20,000	Cash	3,000
Sale of old furniture (Book value Rs. 400)	3,000	Bank	24,000

Subscription for 2015 still receivable was Rs. 7000, interest due on saving certificates Rs. 1,000 and rent unpaid but due was Rs. 600.

Solution:

Income and Expenditure Account for the year ended 2015

Dr.

Cr.

Expenditure	Amount Rs.	Amount Rs.	Income	Amount Rs.	Amount Rs.
To Salaries		48,000	By Subscription		
To Rent	5000		2015	83,000	
Add: Outstanding	600	5,600	Add: Outstanding		
To Stationery & Postage		2,000	Subscription 2016	7,000	90,000
To Help to poor students		20,000	By Accrued interest on N.S.C		1,000
To Loss on sale of old furniture (4,000 – 3,000)		1,000			
To Surplus (b.f.)		14,400			
		91,000			91,000

Illustration: 8

From the following information relation to Tiruchendur 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	80,00	By Maintenance	50,00
To Members subscription	1,10,00	By Tournament expenses	14,00
To Sale of old balls, bats etc.,	1,00	By Rates & Insurance	4,00
To Hire of ground	6,00	By Telephone charges	1,00
To Members admission fees	6,00	By Printing & Stationery	2,00
To Subscription for		By General charges	1,00
tournament	20,00	By Secretary's Honararium	5,00
To Donations	2,00,00	By Grass seeds	60
		By Bats & balls	14,00
		By Bank balance	3,31,00
		By Cash balance	40
	4,23,00		4,23,00

Additional information

On 1.4.2014 subscription due Rs. 1,000; advance subscription received Rs. 500; Stock of bats & balls Rs. 3,000; Printing & Stationery Rs. 400. Donation and surplus on account of tournament should be kept in reserve for permanent pavilion.

Subscriptions due on 31.3.2015 Rs. 1500; Stock of bat & balls Rs. 2,000; Printing & stationery Rs. 100;

Capital fund in the beginning is Rs. 11,900; Members admission fees is to be treated as capital receipts.

Solution:

Tiruchendur Cricket Club

Income & Expenditure a/c for the year ended 31st March 2015

Expenditure	Amount Rs.	Income	Amount Rs.
To Maintenance	5,000	By Subscription	11,000
To Rates & Insurance	400	Less:	
To Telephone charges	100	Last year	
To Printing & Stationery		subscription	1,000
Opening stock	400		10,000



Add: Purchase	200		Add: This year		
	<u>600</u>		received in last year	500	
Less:				<u>10,500</u>	
Closing stock	100	500	Add:		
To General charges		100	Outstanding	1,500	12,000
To Secretary's			By Sale of old balls, bats		100
Honararium		500	By Hire of ground		600
To Grass seeds		60			
To Bats & balls					
Opening stock	3,000				
Add: Purchase	1,400				
	<u>4,400</u>				
Less:					
Closing stock	2,000	2,400			
To Surplus (b.f.)		3,640			
(transferred to capital fund)					
		12,700			12,700

Tiruchendur Cricket Club
Balance sheet as on 31st March 2015

Liabilities		Amount	Assets	
		Rs.		
Capital fund	11,900		Cash	40
Add: Admission fees	600		Bank	33,100
	<u>12,500</u>		Stock of printing &	
Add: Surplus	3,640	16,140	stationery	100
Reserves			Stock of bats & balls	2,000
Surplus	20,000		Subscription outstanding	1,500
Donations &				
on Tournament				
(2,000 – 1,400)	600	20,600		
		36,740		36,740



Illustration: 9

The following information relates to a PalayamKottai Sports Club.

Receipts and Payment Account

Receipts	Amount Rs.	Payments	Amount Rs.
To Subscription (including Rs. 500 for 2013)	8,600	By Buildings	62,000
To Locker rent	320	By Salary	1,025
To Interest	140	By Tennis expenses	1,315
To Sale of cricket material	130	By Insurance	120
To Sundry receipts	20	By Furniture	1,520
To Tennis fees	1,350	By Printing	715
To Billiards table	310	By Expenses of matches	8,770
To Receipts table matches	9,900	By Billiards table (new)	2,000
To Entrance fees	4,220	By Telephone	237
To Special donation to building fund	60,000	By Sundry expenses	303
		By News paper	300
		(subscription Rs. 75 for the year ending 31 st March 2015)	
		By Advance to clerk	140
		By Purchase of investments	6,125
		By Balance c/d	420
	84,990		84,990

Additional information

1. Subscription due Rs. 1,120
2. Salaries unpaid Rs. 125
3. Insurance prepaid Rs. 60
4. Write off Rs. 1,000 as depreciation of building and Rs. 50 on furniture.
5. One half of the entrance fees are to be capitalized.

Prepare Income and Expenditure account and balance sheet of the club on 31.12.2014.



Solution:

**PalayamKottai Sports Club Income & Expenditure a/c
for the year ended 31.12.2014**

Expenditure	Amount Rs.	Income	Amount Rs.
To Salary	1,025	By Subscription	8,600
Add: Unpaid salary	125	Less: Received in advance	500
To Tennis expenses	1,150		8,100
To Insurance	120	Add: Subscription due	1,120
Less: Prepaid insurance	60		9,220
To Expenses of matches	8,770	By Locker rent	320
To Printing	715	By Interest	140
To Telephone	237	By Sale of cricket material	130
To Sundry expenses	303	By Sundry receipts	20
To News paper	300	By Tennis fees	1,350
Less: Prepaid	75	By Receipts table matches	9,900
	225	By Entrance fees (4,220 / 2)	2,110
Add: Advance	75		
To Depreciation			
Building	50		
Furniture	1,000		
To Surplus (b.f.)	9,290		
	23,190		23,190

PalayamKottai Sports Club Balance sheet as on 31.12.2013

Liabilities	Amount Rs.	Assets	Amount Rs.
Opening Capital fund	385	Billiards table	310
		Prepaid for news paper	75
	385		385

Note: Since opening capital fund is not given, balance sheet as on 31.12.2013 is prepared to find out opening capital fund.



PalayamKottai Sports Club Balance sheet as on 31.12.2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Advance subscription received	500	Subscription outstanding	1,120
Special donation to building	60,000	Building (62,000 – 1,000)	61,000
Outstanding salary	125	Insurance prepaid	60
Capital fund	385	Furniture (1,520 – 50)	1,470
Less: 1/2 Entrance		Billiards table	2,000
fees	2,110	News paper prepaid	75
	2,495	Advance to clerk	140
Add: Excess	9,290	Investment	6,125
	11,785	Cash in hand	420
	72,410		72,410

Illustration: 10

Prepare an Income and Expenditure account for the year ended 31st March 2015 and the balance sheet as on that date of College from the following.

Receipts and Payment Account for the year ended 31st March 2015

Receipts	Amount Rs.	Payments	Amount Rs.
To Cash on (01.04.2014)	20,000	By Pay and allowance	70,500
To Tuition fees	59,000	By Provident fund	
To Fines	1,000	contribution	5,540
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 equipments	480
		By Laboratory expenses	500
		By Construction of new	
		building	4,700
		By Repairs & maintenance	600
		By Audit fees	300



		By General charges	580
		By Cash on 31.12.2015	22,000
	1,11,300		1,11,300

Additional information

The college had the following assets on 31.3.2014. Furniture Rs. 35,000; Land and Buildings Rs. 1,60,000; Library books Rs. 24,000; Investments Rs. 10,000; and Outstanding tuition fees Rs. 2,200. Provide for depreciation on the closing balances of the following assets: Land and Buildings @ 5%; Furniture @ 15%; Library books @ 20%.

Solution

Income & Expenditure a/c for the year ended 31st March 2015

Dr.

Cr.

Expenditure	Amount Rs.	Income	Amount Rs.
To Pay and allowance	70,500	By Tuition fees	59,000
To Provident fund contribution	5,540	Less: Outstanding Tuition fees	2,200
To Printing & stationery	700	By Fines	1,000
To Postage & telegrams	500	By Grants from State Govt.	30,000
To Newspaper, etc.,	300	By Interest on securities	300
To Laboratory expenses	500	By Rent from use of hall	1,000
To Repairs & maintenance	600	By Deficit (Excess of Expenditure over income)	9,625
To Audit fees	300		
To General charges	580		
To Depreciation			
Land & Building 5% of (1,60,000 + 4,700)	8,235		
Furniture (15% of 35,000)	5,250		
Library books 20% of			



(24,000 + 4,600)	5,720	19,205	
		98,725	98,725

Balance sheet as on 31st March 2015

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital fund	2,51,200	2,41,575	Cash		22,000
Less: Deficit	<u>9,625</u>		Furniture	35,000	
			Less: Depreciation	5250	29,750
			Land & Building	<u>1,60,000</u>	
			Add: Additions	4,700	
				<u>1,64,700</u>	
			Less: Depreciation	8,235	1,56,465
			Library books	<u>24,000</u>	
			Add: Additions	4,600	
				<u>28,600</u>	
			Less: Depreciation	5,720	22,880
			Science equipments		480
			Investments		10,000
		2,41,575			2,41,575

Working notes

To find out opening capital, balance sheet as on 31.3.2014 is to be prepared.

Balance sheet as on 31st March 2014

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital fund	2,51,200	2,51,200	Cash		20,000
(Balancing figure)			Furniture		35,000
			Land & Building		1,60,000
			Library books		24,000
			Investments		10,000
			Outstanding tuition fees		2,200
			2,51,200		



Illustration: 11

Income and Expenditure Account of the Kanniyakumari Sports Club for the year ended 31st March, 2015 is as follows.

**Kanniyakumari Sports Club Receipts and Payment Account
for the year ended 31st March 2015**

Dr.	Amount	Cr.	Amount
Receipts	Rs.	Payments	Rs.
To Salaries	24,750	By Subscriptions	37,500
To General expenses	500	By Entrance fees	250
To Audit fees	1,250	By Contribution for annual	
To Secretary's Honorarium	1,000	dinner	11,000
To Stationery and printing	450	By Profit on annual sports	
To Annual Dinner expenses	11,500	meet	750
To Interest and bank charges	150		
To Depreciation	9,300		
To Excess of income over expenditure	600		
	49,500		49,500

This account had been prepared after the following adjustments.

Subscriptions outstanding on 31st March 2014 Rs. 600

Subscription received in advance on 31st March 2014 Rs. 450

Subscription received in advance on 31st March 2015 Rs. 270 and

Subscription outstanding on 31st March 2015 Rs. 750

Salaries outstanding on 31st March 2013 and 31st March 2015 were respectively Rs. 2,000 and Rs. 2,250. General expenses include insurance prepaid to the extent of Rs. 60. Audit fees for 2014-2015 are yet unpaid, during 2014 – 2015. Audit fees for 2013 – 2014 were paid amounting to Rs. 1,000

The club owned a freehold lease of ground valued at Rs. 10,000. The club has sports equipment on 1st April 2014 valued at Rs. 12,600. At the end of the year, after depreciation, this equipment amounted to Rs. 13,700. In 2013 – 2014 the club had



raised a bank loan of Rs. 2,000. This was outstanding throughout 2014 – 2015. On 31st March, 2015 cash in hand amounted to Rs. 1,600.

Prepare Receipts and Payments Account for the year ended 31st March 2015 and the balance sheet at end of the year.

Solution:

**Receipts and payments a/c of Kanniyakumari Sports Club
for the year ended 31.03.2015**

Dr.

Cr.

Receipts	Amount Rs.	Amount Rs.	Payments	Amount Rs.	Amount Rs.
To Balance b/d (balancing figure)		1,990	By Salaries	24,750	
To Subscription	37,500		Add: Paid for 2013 – 2014	2,000	
Add: Outstanding on 31.3.2014	600			26,750	
Add: Received on 31.3.2015	270		Less: Payable for 2014 – 2015	2,250	24,500
	38,370		By General expenses	500	
Less: Received in advance on 31.3.13	450		Add: Prepaid 2015 – 2016	60	560
	37,920		By Audit fees (2013 – 2014)		1,000
Less: Outstanding on 31.3.2015	750	37,170	By Secretary's Honorarium		1,000
To Entrance fees		250	By Stationery and printing		450
To Contribution for annual dinner		11,000	By Annual Dinner expenses		11,500
To Profit on annual sports meet		750	By Interest and bank charges		150
			By Sports equipments		



		{ 13700 – (12600 – 9,300)}	10,400
		By Balance c/d	1,600
	51,160		51,160
To Balance b/d	1,600		

Balance sheet of Kanniyakumari Sports Club as on 31.3.2015

Liabilities		Amount Rs.	Assets		Amount Rs.
Subscription			Freehold grounds		10,000
received in advance		270	Sports equipments	12,800	
Audit fee outstanding		1,250	Additions during		
Salaries outstanding		2,250	the year	10,400	
Bank Loan		2,000		<u>23,000</u>	
Capital fund	19,740		Less: Depreciation	9,300	13,700
Add: Surplus	<u>600</u>	20,340	Subscription outstanding		750
			Insurance prepaid		60
			Cash in hand		1,600
		26,110			26,110

Balance sheet of Kanniyakumari Sports Club as on 31.3.2014

Liabilities		Amount Rs.	Assets		Amount Rs.
Subscription			Freehold grounds		10,000
received in advance		450	Sports equipments		12,500
Salaries outstanding		2,000	Subscription outstanding		600
Audit fee unpaid		1,000	Cash in hand		1,990
Bank Loan		2,000			
Capital fund (b.f.)		19,740			
		25,190			25,190



Illustration: 12

Given below are receipts and payments account and income and expenditure account for a club for the year ending 31st March 2013.

Receipts and Payment Account for the year ended 31st March 2015

Dr.

Cr.

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 (2012)	1,300
		By Investments 4% at 96 purchased on 1.7.2012	1,920
		By Balance c/d	1,280
	23,000		23,000

Income and Expenditure account for the year ending 31st March 2013

Dr.

Cr.

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 at 4% on Rs. 2,000	80
To Audit fees	300	By Entertainment	4,000
To Provision	6,000	By Deficit (Excess of expenditure over income)	2,370
To Printing & stationery	750		
To Sports material	2,000		
	16,850		16,850

Prepare balance sheets both in the beginning and at the end.



Solution:

Balance sheet as on 1st January 2013

Liabilities	Amount Rs.	Assets	Amount Rs.
Creditor for investments	1,920	Cash in hand	4,000
Creditors	1,300	Investments	1,920
Capital fund	3,500	Furniture	800
	6,720		6,720

Balance sheet as on 31st March 2013

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 sports material	800
Subscription in advance	200	Interest accrued	800
Entrance fees	400	Investments	80
Donation for books	1,300		1,920
Capital fund	3,500		
Less: Deficit	2,370		
	6,080		6,080

Illustration: 13

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	By News papers	400
	1,450		



To Sale of old furniture (Cost Rs. 100)	60	By Postage	50
To Rent received	740	By Furniture	250
To Entertainment gains	400	By Balance c/d	500
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 (31.12.15) 100		Add: Outstanding 250	1,250
	1,300	By Rent received	740
Less: Outstanding (1.1.15) 100	1,200	By Entertainment gains	400
To General expenses	300	By Sale of news papers	100
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	Books	500
Salary outstanding	100	Add: Purchases	100
Subscription received in advance	200	Furniture	600
		Add: Purchases	250
			850
		Less: Sales	100
		Land & Building	10,000
		Subscription outstanding	
		2015	250
		Subscription outstanding	
		2014	50
	12,150		12,150

Illustration: 14

From the given Receipts & Payments a/c and additional information of a club. prepare Income and Expenditure a/c and balance sheet for the year ended 31st December 2016

	Rs.		Rs.
To Balance Jan 1, 2016		By Crockery purchases	265



Cash	352	By Maintenance	682
Bank	2,738	By Match expenses	1,324
Fixed deposit at 6%	3,000	By Salary	1,100
To Subscription	4,000	By Conveyance	82
(including Rs. 600 for 2015)		By Unkeep on lawn	424
To Entrance fee	2,075	By Postage	105
To Donation	501	By Purchase of cricket goods	972
To Interest on FD	90	By Sundries	200
To Tournament fund	2,000	By Investments	570
To Sale of Crockery		By Tournament expenditure	1,880
(book value Rs. 120)	200	By Balanced 31 Dec. 2016	
		Cash	200
		Bank	2,332
		Fixed deposit	3,000
	13,156		13,156

Additional information

1. Monthly salary is Rs. 100
2. The value of unused postage in 2015 Rs. 75, 2016 Rs. 90
3. Stock of Cricket goods 2015 Rs. 321, 2016 Rs. 280
4. Arrears of subscription 2015 Rs. 660, 2016 Rs. 800

Solution:

Income & Expenditure a/c for the year ended 31st March 2015

Dr.

Cr.

Expenditure	Amount Rs.	Income	Amount Rs.
To Maintenance	682	By Subscription	4,000
To Match expenses	1,324	Less: Previous	600
To Salary	1,100		3,400
Add: Outstanding	100	Add: Current year	800
To Conveyance	82	By Interest on FD	90
To Unkeep on lawn	424	Add: Accrued	
To Postage used		interest	90
			180



Opening stock	75		By Profit on sale of	
Add: Purchases	105		Crockery (200 – 120)	80
	180		By Deficit (b.f.)	555
Less: Closing stock	90	90		
Cricket goods used				
Opening stock	321			
Add: Purchases	972			
	1,293			
Less: Closing stock	280	1,013		
To Sundries		200		
		5,015		5,015

Balance sheet as on 31.12.2016

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital fund	7,266		Subscription 2015		60
Less: Deficit	555	6,711	Accrued interest on FD		90
Entrance fees		275	Crockery Purchased		265
Donation		501	Closing stock of postage		90
Salary outstanding		100	Closing stock of cricket		
Tournament fund	2,000		goods		280
Less: Expenses	1,880	120	Investments		570
			Cash in hand		220
			Cash at Bank		2332
			Fixed deposit		3,000
			Current subscription o/s		800
		7,707			7,707

Opening Balance sheet as on 1.1.2016

Liabilities		Amount Rs.	Assets		Amount Rs.
Capital fund (b.f.)		7,266	Cash in hand		352
			Cash at Bank		2738



	Fixed deposit	3,000
	Subscription o/s	660
	Crockery	120
	Stock of postage	75
	Stock of cricket goods	321
	7,266	7,266

Illustration: 15

Following is the so-called receipts and payment account.

Receipts and payments a/c for the year ended 31.12.2013

Dr.

Cr.

Receipts	Amount Rs.	Payments	Amount Rs.
To Balance b/d	50	By Expenses	700
To Annual income from subscription 510		(including payments for sport material Rs. 300)	
Add: Outstanding of last year		By Loss on sale of furniture (cost price Rs. 50)	20
received this year 20		By Balance c/d	10,050
530			
Less: Prepaid of last year 10	520		
To Other fees	200		
To Donation for building 10,000	10,000		
	10,770		10,770

Additional information

Club had on 1.1.2013; Furniture Rs. 200; Investments at 5% Rs. 3,000; Sports material Rs. 740; On 31.12.2013 Subscription outstanding Rs. 30; Subscription prepaid Rs. 10; Stock of sport material Rs. 200.

If you do not approve of it; prepare correct receipts and payments account, income and expenditure account and balance sheet.



Solution:

Receipts and payments a/c for the year ended 31.12.2013

Dr.

Cr.

Receipts	Amount Rs.	Amount Rs.	Payments	Amount Rs.	Amount Rs.
To Balance b/d		50	By Expenses		
To Subscription			sundries		400
Annual income	510		By Sports		
Less: Outstanding			materials		300
at the end	30		By Balance c/d		
Add: Prepaid	480		(balancing figure)		10,000
at end	10				
	490				
Add: Outstanding					
at the beginning	20				
	510				
Less: Prepaid in					
the beginning	10	500			
To Other fees		200			
To Donation		10,000			
To Sale of furniture		30			
		10,780			10,780

Income & Expenditure a/c for the year ended 31.12.2013

Dr.

Cr.

Expenditure	Amount Rs.	Income	Amount Rs.
To Sundry expenses	400	By Subscription annual	
To Sports Materials	740	income	510
Add: Additions	300	By Other fees	200
	1040	By Interest form investment	
Less: Stock in hand	200	accrued (3,000 X 5/100)	150
To Loss on sale of furniture	20	By Deficit	400



(450 – 430)		
	1,260	1,260

Balance sheet as on 31.12.2013

Liabilities	Amount Rs.	Assets	Amount Rs.
Subscription		Furniture	200
paid in advance	10	Less: Sold	50
Donation	10,000	Investments (5%)	3,000
Capital fund	4,000	Interest accrued	150
Less: Deficit	400	Sports equipments	200
	3,600	Subscription outstanding	30
		Bank	10,000
	13,610		13,610

Note: Capital fund in the beginning has been calculated as follows:

Balance sheet as on 1.1.2013

Liabilities	Amount Rs.	Assets	Amount Rs.
Subscription prepaid	10	Furniture	200
Capital fund	4,000	Investments	3,000
(balancing figure)		Sports equipments	740
		Subscription outstanding	20
		Bank	50
	4,010		4,010

Theory Questions

1. Define non-trading concern
2. How do prepare receipts and payments account?
3. Write short notes on income and expenditure account.
4. Differentiate receipts and payment account and income expenditure account.
5. How do prepare a final account for non trading concern.



Problems

1. From the following information given below calculate the amount of Miscellaneous expenses to be transferred to the income and expenditure account for the year ended 31st December 2008.

Actual payment in 2008 for expenses Rs. 25,000

Prepaid expenses as on 31st December 2007 Rs. 800

Outstanding expenses as on 31st December 2007 Rs. 600

Prepaid expenses as on 31st December 2008 Rs. 2,000

Outstanding expenses as on 31st December 2008 Rs. 1,000

2. From the following details ascertain the amount of subscription to be carried to income and expenditure account for the year ending 31st December 2014

Subscription received during 2014 Rs. 25,000

Arrear of subscription of 2013 Rs. 1,000

Subscription of 2015 received in 2014 in advance 2000 (including in subscription received)

Outstanding subscription of 2014 Rs. 500

3. What amount will be shown in the income and expenditure account?

Stock of sports goods as on 1.1.2015 Rs. 1,000

Stock of sports goods as on 31.12.2015 Rs. 400

Sport goods purchased during 2015 Rs. 3,600

Old sports goods sold during 2015 Rs. 80

4. Prepare Receipts and Payments account for the following details for the year ended 31.12.2014

	Rs.
Balance as on 1.1.2014	7,000
Subscription received	43,000
Donation received	20,000
Entrance fee	5,000
Sport goods purchased	15,000
Special subscription	7,000



Special subscription expenses	5,000
Day-to-day expenses	12,000
Deposit in to the bank	40,000

Additional Information

1. Donation and Entrance fee are to capitalized.
2. Special subscription surplus to be treated as income.
3. Outstanding subscription Rs. 2,000

5. Dr. Kishore commenced practice in January 2009. His receipts and payment account for the year 2009.

Receipts	Rs.	Payments	Rs.
To Capital	6,000	By Furniture	2,000
To Income from practices	8,000	By Equipments	3,000
To Income from drugs	6,000	By Drugs	2,000
To Other receipts	100	By Salary	1,200
		By Rent	600
		By Conveyance	1,000
		By Stationery	200
		By Lighting	150
		By Newspaper	150
		By Investments	6,800
		By Cash balance	3,000
	20,100		20,100

Adjustments:

Rs. 1,500 were still to be received on accounts 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 equipments are subject to depreciation at 5%. Prepare the final account 2009.

6. From the following particulars related to Thoothukudi Club for the year ending 31.12.2015 you are required to prepared income and expenditure account and a balance sheet the same date.



Receipts	Rs.	Payments	Rs.
To Balance b/d	640	By Salary	1445
To Subscription arrear	24	By Stationary	240
To Subscription during the year	1,226	By Rate and Taxes	360
To Subscription advance	48	By Telephone charges	60
To Profit from canteen	900	By Investments	750
To Miscellaneous income	45	By Advertisement	105
To Sale of old news papers	112	By Postage	100
To Dividend	485	By Sundries	350
		By Balance c/d	70
	3,480		3,480

Adjustment

1. There are 450 members each paying an annual subscription of Rs. 3, Rs. 27 being arrears for 2015
2. Stock of stationery on 1.1.2015 was Rs. 30 and on 31.12.2015 was Rs. 54.
3. Cost of building was Rs. 6,000, Depreciated at the rate 5% p.a.

7. The following is the receipts and payments account of the Tirunelveli Sports Club for the year ending 31.12.2015.

Receipts and Payment Account

Receipts	Amount Rs.	Payments	Amount Rs.
To Balance 1.1.2015	300	By Rent	5,200
To Entrance fees	550	By Stationery	3,068
To Subscriptions		By Wages	5,330
2014	200	By Billiards Table	3,900
2015	16,900	By Repaid and Renewals	806
2016	300	By Interest	1,500
Locker rent	500	By Balance 31.12.2015	2,396
Special subscriptions for governor's party	3,450		
	22,200		22,200



Locker rent Rs. 60 referred to 2014 and Rs. 90 is still owing. Rent Rs. 1,300 pertaining to 2014 and Rs. 1,300 is still due. Stationery expenses Rs. 312 related to 2014, still owing Rs. 364. Subscription unpaid for 2015 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 31.12.2015.



UNIT IV : DEPRECIATION

Depreciation – need – causes – methods of providing depreciation – straight line method – diminishing balance method – sinking fund method – annuity method – insurance policy method – machine hour rate method

CHAPTER – 7 DEPRECIATION

MEANING AND DEFINITION

Depreciation is the reduction in the value of the assets due to constant use. This is a process of spreading the cost of fixed assets is termed as depreciation.

L.C. Cropper defines depreciation as, “the diminution in the financial value of an asset owing to wear and tear, effluxion of time, obsolescence’s or similar causes”.

NEED FOR PROVIDING DEPRECIATION

The need for providing depreciation in accounting records arises due to any one or more of the following reasons.

1. To ascertain correct profit / loss

For proper matching of cost with revenues, it is necessary to charge depreciation against revenue in each accounting year, to calculate the correct net profit or net loss.

2. To present a true and fair view of the financial position

If the amount of depreciation is not provided on fixed assets in the books of accounts, the value of fixed assets will be shown at a higher value than it’s real value in the balance sheet. As such it will not reflect the true and fair financial position of the business, it is necessary that depreciation must be deducted from the book value of the assets in the balance sheet.

3. To ascertain the real cost of production

Ascertaining the real cost of production, it necessary to provide depreciation.

4. To comply with legal requirements

As per Section 205(1) of the Companies Act 1956, it is compulsory for companies to provide depreciation on fixed assets before it declares dividend.

5. To replace assets

Depreciation is provided to replace the assets when it becomes useless.



CAUSES OF DEPRECIATION

Causes of depreciation may be divided into

- 1) Internal causes
- 2) External causes

1) Internal causes

a) Wear and tear

It arises due to constant use of the assets. It arises mainly in case of fixed assets like buildings, machines, furniture, etc.,

b) Depletion

It arises due to the extraction of assets. It arises mainly in case of wasting assets like mines, quarry, oil, well, etc.,

2) External causes

a) Obsolescence

It arises due to new invention, change of style, legislation, etc.,

b) Effluxion of time

Some assets decrease in the value due to passage of time. Example leasehold property, patents, copy rights.

OBJECTIVES (OR) PURPOSE OF PROVIDING DEPRECIATION

1. To find out correct cost of production

If a machine is used to manufacture an article, the depreciation of the machine should also be added with the cost to calculate correct cost of production.

2. To calculate proper profits

The correct profit can be calculated only after providing for depreciation.

3. To show the asset at reasonable value

If the depreciation is not provided the assets will not show the real value.

4. To replace the old asset

Provision of depreciation is made to replace the old plant with the latest model available.

5. To declare the dividend properly

If the depreciation is not provided, dividend cannot be declared properly.



FACTORS INFLUENCING THE TOTAL AMOUNT OF DEPRECIATION

The following three factors are to be considered for the determining the total amount of depreciation.

- 1) Total cost of assets
- 2) Scrap value
- 3) Estimated useful life of the assets

1) Total cost of assets

It includes invoice price less cash discount.

2) Scrap value

It is an estimated value of the assets at the end of the economic life of the assets.

3) Estimated useful life of the assets

It can be calculated in terms of time or output.

a) Depreciation and Depletion

Depreciation is the gradual diminution in the value of assets due to wear and tear and / or lapse of time. But depletion is the decrease in the value of assets due to extraction.

Depreciation is used for fixed assets where as depletion is used for wasting assets.

b) Depreciation and obsolescence

Depreciation is the gradual diminution in the value of assets due to wear and tear and / or lapse of time. But obsolescence is the loss in the value of asset due to new invention.

Depreciation arises due to internal or external causes whereas obsolescence arises due to external causes.

METHODS OF DEPRECIATION

1. Straight Line Method (or) Original Cost Method (or) Fixed Installment Method

Under this method a fixed percentage is calculated on original cost and written off as depreciation every year during the life time of the assts.

$$\text{Depreciation Amount} = \frac{\text{Original cost} - \text{Scrap value}}{\text{No. of years or Life of the assets}}$$



$$\text{Depreciation Rate} = \frac{\text{Depreciation Amount}}{\text{Cost of the Assets}} \times 100$$

This method is simple to adopt. But his method does not consider the seasonal fluctuations. The total charge in respect of an asset is not equal from year to year through the depreciation is the same for all the years.

Illustration: 1

ABC company purchased machinery for Rs. 10,00,000. Its installation costs amounted to Rs. 1,00,000. It's estimated life is 5 years and the scrap value is Rs. 5,000. Calculate the amount and rate of depreciation.

Solution:

$$\begin{aligned} \text{Total cost} &= \text{Purchase price} + \text{Installation charges} \\ &= 10,00,000 + 1,00,000 \\ &= \text{Rs. } 11,00,000 \\ \text{Amount of depreciation} &= \frac{\text{Total cost} - \text{Scrap value}}{\text{Estimated life}} \\ &= \frac{11,00,000 - 5,000}{5} \\ &= \frac{10,50,000}{5} \\ &= \text{Rs. } 2,10,000 \\ \text{Rate of depreciation} &= \frac{\text{Amount of depreciation}}{\text{Original cost}} \times 100 \\ &= \frac{2,10,000}{11,00,000} \times 100 \\ &= 19.09\% \end{aligned}$$

2. Diminishing balance method (or) Reducing balance method (or) Written down value method

Under this method depreciation is charged at fixed rate on the reducing balance (cost depreciation) every year.



Illustration: 2

XYZ Limited assets purchased for machinery of Rs. 5,00,000 and depreciation is to be provided 10% p.a. on reducing balance method. Calculate the three year depreciation.

Solution:

First year depreciation

$$\begin{aligned} &= \text{Rs. } 5,00,000 \text{ on } 10\% \\ &= 5,00,000 \times \frac{10}{100} \\ &= \text{Rs. } 50,000 \end{aligned}$$

Second year depreciation

$$\begin{aligned} &= \text{Rs. } 4,50,000 \text{ on } 10\% \\ &\quad (5,00,000 - 50,000) \\ &= 4,50,000 \times \frac{10}{100} \\ &= \text{Rs. } 45,000 \end{aligned}$$

Third year depreciation

$$\begin{aligned} &= \text{Rs. } 4,05,000 \text{ on } 10\% \\ &\quad (4,50,000 - 45,000) \\ &= 4,05,000 \times \frac{10}{100} \\ &= \text{Rs. } 40,500 \end{aligned}$$

Demerits

- Asset is never reduced to zero.
- This method can be applied only when there is some residual value of assets.

3. Annuity method

Under this system the amount of total depreciation is determined by adding the cost of the asset and interest there on at an expected rate. The annual amount of the depreciation is determined with the help of annuity table.

Illustration: 3

A trader takes a lease for five years for Rs. 4,00,000. He decides to write off lease by annuity method presuming the rate of interest at 5% p.a. The annuity table



show that the annuity amount necessary to write off of Re. 1 in 5 years at 5% is Re. 0.230975. Calculate amount of depreciation

Solution:

$$\begin{aligned}\text{Depreciation} &= \text{Cost price} \times \text{Annuity table value} \\ &= 4,00,000 \times 0.230975 \\ &= \text{Rs. } 92,390\end{aligned}$$

4. Depreciation fund method

Under this system, the amount written off as depreciation should be debit aside and invested in government securities. The securities accumulate. When the life of the asset expires, the securities are sold and a new asset is purchased with the help of sale proceeds. So this system incorporates the advantages of depreciating the asset as well as accumulating the necessary amount for its replacement.

5. Insurance policy method

Under this method the business take a policy form an insurance company. The objective is to replace the asset when it is workout. Every year premium is paid (equal to the amount of depreciation) to the insurance company. On the date of maturity the insured sum will be received from the insurance company, with this sum, new asset will be purchased.

6. Revaluation method

According to the method assets are revalued at the end of each year. The difference between the past estimated (as per the past balance sheet) and at the present estimated value represents depreciation. It is followed in the case of small items such as loose tools etc.,

7. Depletion method

This method is applied in recording the extraction of natural resources.

It is used in case of mines, quarries etc., where an estimates of total quantity of output likely to be calculated.

Illustration: 4

It a mine is purchased for Rs. 2,00,000 and its estimated that quantity taken from the mine is 50,000 tonne.

$$\text{Depreciation} = \frac{\text{Cost of the mine}}{\text{Total quantity}}$$



$$\begin{aligned} \text{Depreciation} &= \frac{2,00,000}{50,000} \\ &= 4 \end{aligned}$$

8. Sum of years digit method

In this method, the amount of depreciation goes on decreasing in the future years.

The rate of depreciation is determined by the fraction, where the denominator (it does not change) is the sum of the digits representing the life of the asset and the numerators are individual digits used in the life of the asset taken in the reverse order.

9. Machine hour method

This method taken into consideration the life time of the asset in terms of machine hours for the purpose of calculating the amount of depreciation.

$$\text{Depreciation per service hour} = \frac{\text{Cost of the asset} - \text{Scrap value}}{\text{No. of hours}}$$

Difference between straight line method & Diminishing balance method

S. No.	Straight Line Method	Diminishing Balance Method
1.	The total amount of depreciation is fixed	The amount of depreciation decreases as the asset value decreases.
2.	The depreciation is calculated on the original cost of the asset.	Depreciation is calculated on the diminishing balance of the asset.
3.	The system is not accepted by the income tax authorities.	The system is accepted by income tax authorities.

Difference between annuity method and depreciation fund method

S. No.	Insurance Policy Method	Sinking Fund Method
1.	The amount received is certain	The amount received depends on the quality of investments and market conditions.
2.	The premium is paid in the beginning of the year.	The investment is made at the end of the year.



Differences between a provision and a reserve

- 1) A reserve is an amount which is set aside for any unknown liability whereas a provision is an amount set aside for a known liability.
- 2) The purpose of creating a reserve is to strengthen the financial position of a business whereas the purpose of creating a provision is to meet out a specific loss or a specific liability or to replace an asset.
- 3) A reserve is created only when there is sufficient profit whereas a provision is created even if there is a loss.
- 4) The amount which is kept in a reserve may be utilized to distribute dividend to the shareholders. But the amount which is kept in a provision may not be used like reserve.
- 5) Reserve is an appropriation of profits. So it is recorded in the profit and loss appropriation account.

A provision is charge against profits. Therefore, it is recorded in the profit and loss account.

Straight Line Method

Journal entries

S. No.	Particulars	Debit Rs.	Credit Rs.
1.	When assets is purchased		
	Assets a/c Dr. To Cash a/c (Being asset is purchased)	***	***
2.	When depreciation is provided		
	Depreciation a/c Dr. To Assets a/c (Being depreciation is provided)	***	***
3.	When assets sold as a profit		
	i) For sales		
	Cash a/c Dr. To Assets a/c	***	***
ii) For profit			
Assets a/c Dr.	***		



4.	To Profit & Loss a/c			***
	When assets sold as a loss			
	Cash account a/c	Dr.	***	
	Profit & Loss a/c		***	
	To Assets a/c			***

Recording Depreciation

Depreciation is directly charged against the asset by debiting depreciation account and crediting the asset account. Depreciation account is closed by transferring to profit and loss account at the end of the year. The entries will be as under.

1) For the amount of depreciation to be provided at the end of the year

Depreciation a/c	Dr.	(With the amount of
To Assets a/c		depreciation)

2) For transferring the amount of depreciation at the end of the year

Profit and Loss a/c	Dr.	(With the amount of
To Depreciation a/c		depreciation)

Asset account will be shown at cost less depreciation i.e. written down value at the end of the year in the balance sheet.

Illustration: 5

Rahavan & Co., purchased a fixed asset on 1.4.2010 for Rs. 2,50,000. Depreciation is to be provided @ 10% annually according to the Straight line method. The books are closed on 31st March every year.

Pass the necessary journal entries, prepare fixed asset account and depreciation account for the first three years.

Solution:

Amount of Depreciation

$$\begin{aligned}
 &= 2,50,000 \times \frac{10}{100} \\
 &= \text{Rs. } 25,000
 \end{aligned}$$



**In the books of Rahavan & Co.,
Journal Entries**

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2010 April 1	Fixed asset a/c Dr. To Bank a/c (Fixed asset purchased)		2,50,000	2,50,000
2011 Mar. 31	Depreciation a/c Dr. To Fixed asset a/c (Depreciation provided)		25,000	25,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		25,000	25,000
2012 Mar. 31	Depreciation a/c Dr. To Fixed asset a/c (Depreciation provided)		25,000	25,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		25,000	25,000
2013 Mar. 31	Depreciation a/c Dr. To Fixed asset a/c (Depreciation provided)		25,000	25,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		25,000	25,000



Ledger Accounts
Fixed assets account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2010 April 1	To Bank a/c	2,50,000	2011 Mar. 31	By Depreciation a/c	25,000
			”	By Balance c/d	2,25,000
		2,50,000			2,50,000
2011 April 1	To Balance b/d	2,25,000	2012 Mar. 31	By Depreciation a/c	25,000
			”	By Balance c/d	2,00,000
		2,25,000			2,25,000
2012 April 1	To Balance b/d	2,00,000	2013 Mar. 31	By Depreciation a/c	25,000
			”	By Balance c/d	1,75,000
		2,00,000			2,00,000
2013 April 1	To Balance b/d	1,75,000			

Depreciation Account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2011 Mar. 31	To Fixed Asset a/c	25,000	2011 Mar. 31	By Profit and Loss a/c	25,000
		25,000			25,000
2012 Mar. 31	To Fixed Asset a/c	25,000	2012 Mar. 31	By Profit and Loss a/c	25,000
		25,000			25,000
2013			2013		



Mar. 31	To Fixed Asset a/c	25,000	Mar. 31	By Profit and	
				Loss a/c	25,000
		25,000			25,000

Illustration: 6

A company purchased machinery for Rs. 50,000 on 1st April 2012. It is depreciated at 20% per annum on written down value method. The accounting year ends on 31st March of every year.

Pass necessary journal entries, prepare machinery account and depreciation account for three years.

Solution:

Journal Entries

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2012 April 1	Machinery a/c Dr. To Bank a/c (Fixed asset purchased)		50,000	50,000
2013 Mar. 31	Depreciation a/c Dr. To Machinery a/c (Depreciation provided)		5,000	5,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		5,000	5,000
2014 Mar. 31	Depreciation a/c Dr. To Fixed asset a/c (Depreciation provided)		4,500	4,500
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to		4,500	4,500



	profit and loss account)				
2015					
Mar. 31	Depreciation a/c	Dr.		4,050	
	To Fixed asset a/c				4,050
	(Depreciation provided)				
Mar. 31	Profit and loss a/c	Dr.		4,050	
	To Depreciation a/c				4,050
	(Depreciation transferred to profit and loss account)				

Ledger Accounts
Machinery account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2012			2013		
April 1	To Bank a/c	50,000	Mar. 31	By Depreciation a/c	5,000
			”	By Balance c/d	45,000
		50,000			50,000
2013			2014		
April 1	To Balance b/d	45,000	Mar. 31	By Depreciation a/c	4,500
			”	By Balance c/d	40,500
		45,000			45,000
2014			2015		
April 1	To Balance b/d	40,500	Mar. 31	By Depreciation a/c	4,050
			”	By Balance c/d	36,450
		40,500			40,500
2015					
April 1	To Balance b/d	36,450			



Depreciation Account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2011		
Mar. 31	To Machinery a/c	5,000	Mar. 31	By Profit and Loss a/c	5,000
		5,000			5,000
2014			2012		
Mar. 31	To Machinery a/c	4,500	Mar. 31	By Profit and Loss a/c	4,500
		4,500			4,500
2015			2013		
Mar. 31	To Machinery a/c	4,050	Mar. 31	By Profit and Loss a/c	4,050
		4,050			4,050

Illustration: 7

Deepak manufacturing company purchased on 1st April 2012, Machinery for Rs. 2,90,000 and spent Rs. 10,000 on its installation. After having used it for three years it was sold for Rs. 2,00,000. Depreciation is to be provided every year at the rate of 15% per annum on the fixed instalment method.

Pass the necessary journal entries, prepare machinery account and depreciation account for three years ends on 31st March every years.

Solution:

Calculation of profit or loss on sale of machinery

	Rs.
Cost price (Rs.2,90,000 + Rs. 10,000)	3,00,000
Less: Depreciation for (2012 – 13) @ 15%	45,000
	2,55,000
Less: Depreciation for (2013 – 14) @ 15%	45,000
	2,10,000
Less: Depreciation for (2014 – 15) @ 15%	45,000
	1,65,000
Book value as on the date of sale	1,65,000



As book value is less than selling price the difference is profit.

	Rs.
Machinery selling price	2,00,000
Less: Book value as on the date of sale	1,65,000
Profit	35,000

Solution:

Journal Entries in the books of Deepak Manufacturing Company

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2012 April 1	Machinery a/c Dr. To Bank a/c (Machinery purchased and installation charges paid)		3,00,000	3,00,000
2013 Mar. 31	Depreciation a/c Dr. To Machinery a/c (Depreciation provided)		45,000	45,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		45,000	45,000
2014 Mar. 31	Depreciation a/c Dr. To Machinery a/c (Depreciation provided)		45,000	45,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		45,000	45,000
2015 Mar. 31	Depreciation a/c Dr.		45,000	



	To Machinery a/c (Depreciation provided)			45,000
Mar. 31	Profit and loss a/c	Dr.	45,000	
	To Depreciation a/c (Depreciation transferred to profit and loss account)			45,000
2012				
April 1	Bank a/c	Dr.	2,00,000	
	To Machinery a/c (Machinery sold)			2,00,000
2013				
Mar. 31	Machinery a/c	Dr.	35,000	
	To Profit and Loss a/c (Profit on sale of machinery)			35,000

Ledger Accounts

Machinery account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2012			2013		
April 1	To Bank a/c	3,00,000	Mar. 31	By Depreciation a/c	45,000
			"	By Balance c/d	2,55,000
		3,00,000			3,00,000
2013			2014		
April 1	To Balance b/d	2,55,000	Mar. 31	By Depreciation a/c	4,500
			"	By Balance c/d	2,10,000
		2,55,000			2,55,000
2014			2015		
April 1	To Balance b/d	2,10,000	Mar. 31	By Depreciation a/c	45,000
	To Profit and loss a/c (profit on sale)	35,000	"	By Bank	2,00,000
		2,45,000			2,45,000



Depreciation Account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2011		
Mar. 31	To Machinery a/c	45,000	Mar. 31	By Profit and Loss a/c	45,000
		45,000			45,000
2014			2012		
Mar. 31	To Machinery a/c	45,000	Mar. 31	By Profit and Loss a/c	45,000
		45,000			45,000
2015			2013		
Mar. 31	To Machinery a/c	45,000	Mar. 31	By Profit and Loss a/c	45,000
		45,000			45,000

Illustration: 8

Machinery account showed a balance of Rs. 80,000 on 1st April 2011. On 1st October 2013, another machinery was purchase for Rs. 48,000. On 30th September 2013, a machinery which has book value Rs. 80,000 on 1.4.2011 was sold for the Rs. 48,000. Depreciation is to be provided at 10% per annum on written down value method. The accounting year ends on 31st March.

Prepare machinery account and depreciation account for three years.

Solution:

Calculation of profit or loss on sale of machinery

	Rs.
Cost of machinery (1.4.2011)	80,000
Less: Depreciation for 2011 – 12	8,000
	72,000
Less: Depreciation for 2012 – 13	7,200
	64,800
Less: Depreciation till the date of sale (30.9.13)	3,240
	61,560



Book value as on the date of sale

61,560

As book value is greater than selling price the difference is loss.

	Rs.
Book value as on the date of sale	61,560
Less: Machinery selling price	48,000
Loss	13,560

Ledger Accounts
Machinery account

Dr.			Cr.		
Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2011			2012		
April 1	To Bank a/c	80,000	Mar. 31	By Depreciation a/c	45,000
			”	By Balance c/d	2,55,000
		80,000			3,00,000
2012			2013		
April 1	To Balance b/d	72,000	Mar. 31	By Depreciation a/c	4,500
			”	By Balance c/d	2,10,000
		72,000			2,55,000
2013			2013		
April 1	To Balance b/d	64,800	Sep. 30	By Depreciation a/c	45,000
Oct. 1	To Bank a/c	48,000	”	By Bank	2,00,000
				To Profit and loss a/c (loss on sale)	35,000
		1,12,800	2014		
			Mar. 31	By Depreciation a/c	2,400
			”	By Balance c/d	45,600
		1,12,800			1,12,800
2014					
April 1	To Balance b/d	45,600			



Depreciation Account

Dr.			Cr.		
Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2012			2011		
Mar. 31	To Machinery a/c	8,000	Mar. 31	By Profit and Loss a/c	8,000
		8,000			8,000
2013			2012		
Mar. 31	To Machinery a/c	7,200	Mar. 31	By Profit and Loss a/c	7,200
		7,200			7,200
2015			2013		
Mar. 31	To Machinery a/c	3,240	Mar. 31	By Profit and Loss a/c	5,640
2015					
Mar. 31	To Machinery a/c	2,400			
		5,640			5,640

Illustration: 9

Vimal & Brothers purchased a machinery for Rs. 3,75,000 on 1st July 2012. It is depreciated at 20% per annum on Straight Line Method for three years. Having become obsolete was sold for Rs. 75,000 on 31.3.2015.

Pass the journal entries, prepare machinery account and depreciation account. Accounts are closed 31st March every year.

Solution:

Calculation of profit or loss on sale of machinery

	Rs.
Cost of machinery (1.7.2012)	3,75,000
Less: Depreciation for 2012 – 13 (for 9 months at the rate of 20%)	56,250
	3,18,750
Less: Depreciation for 2013 – 14	75,000
	2,43,750



Less: Depreciation for 2014 – 15 75,000

Book value as on the date of sale 1,68,750

As book value is greater than selling price the difference is loss.

	Rs.
Book value as on the date of sale	1,68,750
Less: Machinery selling price	48,000
Loss	<u>93,750</u>

Journal Entries in the books of Vimal & Brothers

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2012 July 31	Machinery a/c Dr. To Bank a/c (Machinery purchased)		3,75,000	3,75,000
2012 Mar. 31	Depreciation a/c Dr. To Machinery a/c (Depreciation provided)		56,250	56,250
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		56,250	56,250
2014 Mar. 31	Depreciation a/c Dr. To Machinery a/c (Depreciation provided)		75,000	75,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		75,000	75,000
2015				



Mar. 31	Depreciation a/c To Machinery a/c (Depreciation provided)	Dr.		75,000	75,000
Mar. 31	Profit and loss a/c To Depreciation a/c (Depreciation transferred to profit and loss account)	Dr.		75,000	75,000
Mar. 31	Bank a/c To Machinery a/c (Machinery sold)	Dr.		75,000	75,000
Mar. 31	To Profit and Loss a/c Machinery a/c (Loss on sale of machinery)	Dr.		93,750	93,750

Ledger Accounts

Machinery account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2012			2013		
July 1	To Bank a/c	3,75,000	Mar. 31	By Depreciation a/c	56,250
			”	By Balance c/d	3,18,750
		3,75,000			3,75,000
2013			2014		
April 1	To Balance b/d	3,18,750	Mar. 31	By Depreciation a/c	75,000
			”	By Balance c/d	2,43,750
		3,18,750			3,18,750
2014			2015		
April 1	To Balance b/d	2,43,750	Sep. 30	By Depreciation a/c	75,000
			”	By Bank	75,000
				To Profit and loss a/c (loss on sale)	93,750
		2,43,750			2,43,750



Depreciation Account

Dr.			Cr.		
Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2013			2011		
Mar. 31	To Machinery a/c	56,250	Mar. 31	By Profit and Loss a/c	56,250
		56,250			56,250
2014			2012		
Mar. 31	To Machinery a/c	75,000	Mar. 31	By Profit and Loss a/c	75,000
		75,000			75,000
2015			2013		
Mar. 31	To Machinery a/c	75,000	Mar. 31	By Profit and Loss a/c	75,000
		75,000			75,000

Illustration: 10

On April 1, 2011 Machinery was purchased for Rs. 4,00,000. On 1st October 2012, a new machine costing Rs. 2,40,000 was purchased. On 30th September 2013, the machinery purchased on 1st April 2011 having become obsolete was sold for Rs. 2,40,000. The accounting year ends on 31st March and depreciation is to be provided at 10% p.a. on straight line method.

Pass journal entries and prepare important ledger accounts for three years.

Solution:

Calculation of profit or loss on sale of machinery

	Rs.
Cost of machinery (April, 2011)	4,00,000
Less: Depreciation for 2011 – 12	40,000
	3,60,000
Less: Depreciation for 2012 – 13	40,000
	3,20,000
Less: Depreciation till the date of sale (30.9.13)	20,000
	2,40,000



Book value as on the date of sale

3,00,000

As book value is greater than selling price the difference is loss.

	Rs.
Book value as on the date of sale	3,00,000
Less: Machinery selling price	2,40,000
Loss	60,000

Journal Entries

Date	Particulars	L.F.	Debit Rs.	Credit Rs.
2012 April 31	Machinery a/c Dr. To Bank a/c (Machinery purchased)		4,00,000	4,00,000
2012 Mar. 31	Depreciation a/c Dr. To Machinery a/c (Depreciation provided)		40,000	40,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c (Depreciation transferred to profit and loss account)		40,000	40,000
2012 Oct 1	Machinery a/c Dr. To Bank a/c (Machinery purchased)		2,40,000	2,40,000
2014 Mar. 31	Depreciation a/c Dr. To Machinery a/c (Depreciation provided)		52,000	52,000
Mar. 31	Profit and loss a/c Dr. To Depreciation a/c		52,000	52,000



	(Depreciation transferred to profit and loss account)			
2013				
Sep. 30	Depreciation a/c To Machinery a/c (Depreciation provided on first machine till the date of sale)	Dr.	20,000	20,000
	Bank a/c To Machinery a/c (First machinery sold)	Dr.	2,40,000	2,40,000
Mar. 31	Profit and loss a/c To Machinery a/c (Loss on sale of machinery)	Dr.	60,000	60,000
2014				
Mar. 31	Depreciation a/c To Machinery a/c (Depreciation provided on second machine)	Dr.	24,000	24,000
Mar. 31	To Profit and Loss a/c To Depreciation a/c (Depreciation transferred to profit and loss account)	Dr.	44,000	44,000

Ledger Accounts
Machinery account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2011			2012		
July 1	To Bank a/c	4,00,000	Mar. 31	By Depreciation a/c	40,000
			”	By Balance c/d	3,60,000
		4,00,000			4,00,000
2012			2013		



April 1	To Balance b/d	3,60,000	Mar. 31	By Depreciation a/c	52,000
Oct 1	To Bank a/c	2,40,000	”	By Balance c/d	5,48,000
		6,00,000			6,00,000
2013			2013		
April 1	To Balance b/d	5,48,000	Sep. 30	By Depreciation a/c	20,000
			”	By Bank	2,40,000
			”	To Profit and loss a/c (loss on sale)	60,000
			2014		
			Mar. 31	By Depreciation a/c	24,000
			”	By Balance c/d	2,04,000
		5,48,000			5,48,000
2014					
April 1	To Balance b/d	2,04,000			

Depreciation Account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2012			2012		
Mar. 31	To Machinery a/c	40,000	Mar. 31	By Profit and Loss a/c	40,000
		40,000			40,000
2013			2013		
Mar. 31	To Machinery a/c	52,000	Mar. 31	By Profit and Loss a/c	52,000
		52,000			52,000
2013			2014		
Sep. 30	To Machinery a/c	20,000	Mar. 31	By Profit and Loss a/c	44,000
2014					
Mar. 31	To Machinery a/c	24,000			
		44,000			44,000



Illustration: 11

Aravinth & Brothers purchased a Machinery for Rs. 90,000 on 1st April 2011. They spent Rs. 10,000 for installation charges. But the machinery was brought into use from 1st October 2011. It further purchased a machinery costing Rs. 20,000 on 1st January 2014. Accounts are closed 31st March every year. Depreciation is to be provided at the rate of 10% per annum on written down value method.

Prepare Machinery account & Depreciation account for three years.

Solution:

Ledger Accounts Machinery account

Dr.			Cr.		
Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2011			2012		
April 1	To Bank a/c	1,00,000	Mar. 31	By Depreciation a/c (1,00,000 × 10/100 × 6/12)	5,000
			"	By Balance c/d	95,000
		1,00,000			1,00,000
2012			2013		
April 1	To Balance b/d	95,000	Mar. 31	By Depreciation a/c	9,500
			"	By Balance c/d	85,500
		95,000			95,000
2013			2014		
April 1	To Balance b/d	85,500	Mar. 31	By Depreciation a/c	9,050
2014			"	By Balance c/d	96,450
Jan 1	To Bank a/c	20,000			
		1,05,000			1,05,000
2014					
April 1	To Balance b/d	96,450			



Depreciation Account

Dr.

Cr.

Date	Particulars	Amount Rs.	Date	Particulars	Amount Rs.
2012			2012		
Mar. 31	To Machinery a/c	5,000	Mar. 31	By Profit and Loss a/c	5,000
		5,000			5,000
2013			2013		
Mar. 31	To Machinery a/c	9,500	Mar. 31	By Profit and Loss a/c	9,500
		9,500			9,500
2014			2014		
Mar. 31	To Machinery a/c	9,050	Mar. 31	By Profit and Loss a/c	9,050
		9,050			9,050

Exercises

Theory questions

1. Define and meaning of depreciation.
2. Explain the causes of depreciation
3. What are objectives of depreciation?
4. Difference between straight line method and diminishing balance method.
5. Difference between annuity method and depreciation fund method.
6. Why do provide depreciation?
7. Explain the various method of depreciation.

Additional Problems

1. An asset is purchased for Rs. 40,000. Depreciation is to be provided annually according to the straight line method. The useful life of the assets is ten years and the residual value is Rs. 10,000. You are required to find rate of the depreciation.

(Ans. Depreciation – 3,000; Rate of Depreciation 7.5%)



2. An assets is purchased for Rs. 25,000. Depreciation is to be provided annually according to the straight line method. The useful life of the asset is 10 years and residual value is Rs. 5,000. You are required to find rate of the depreciation.

(Ans. Depreciation – 2,000; Rate of Depreciation 8%)

3. A machine was purchased on 1st January 2011 at a cost Rs. 19,000 and Rs. 1,000 was spent it is installation. The depreciation is written off at 10% on the original cost method every year. The machine was sold for Rs. 10,000 on 30th September 2011. So the machinery account for the two years.

(Ans. 1st year Depreciation – 2,000; 2nd year Depreciation – 1,500)

4. A machine was bought on 1.4.2012 for Rs. 34,000 and Rs. 6,000 was spent on it for repairs. Depreciation was provided at 10% under diminishing balance method on every December. On 30.06.2015 it was sold for Rs. 36,000. Show the machinery account.

(Ans. Profit on sale – 4, 365)

5. A second hand machine was purchased on 1.1.2012 for Rs. 45,000 and got it repaired for Rs. 5,000. Depreciation was provided at 10% under diminishing balance method on every December. On 31.12.2015 the machine was sold for Rs. 27,400. Show the machine account and provision for depreciation a/c

(Ans. Profit on sale of asset Rs. 1,480)

6. On 1.1.2003 machinery was purchased for Rs. 30,000. On 31.12.2006 the machinery was sold for Rs. 15,000. Rate of depreciation is 10%. Prepare machinery account under

i) Fixed percentage method

ii) Diminishing method

(Ans. i) Loss on sale of asset = Rs. 3,000

ii) Loss on sale of asset = Rs. 3,000)



7. Mr. X Purchased a second hand machinery on 1.2.2010 for Rs. 50,000; paid Rs. 11,000 for its overhauling and Rs. 5,000 for its installation which was completed by 31.3.2010.

The company provides depreciation on its machinery at 15% per annum on diminishing balance method from the date it is put to use and closes its books on December 31st every year.

On 1.10.2011, a repair work was carried out on the machine and Rs. 5,000 were paid for the same.

The machine was sold on 31.10.2012 for a sum of Rs.11,000 and an amount of Rs. 1,000 was paid as dismantling charges. Prepare machinery account 2010 – 2012.

(Ans. Profit Rs. 33,565)

8. A trader takes a lease for five years for Rs. 3,25,000. He decides to write off lease by annuity method presuming the rate of interest at 5% p.a. The annuity table show that the annuity amount necessary to write of Re. 1 in 5 years at 5% is Re. 0.230975. Calculate amount of depreciation

(Ans. Depreciation Rs. 75,067)

9. A firm purchased a lease on 1.1.2005 for Rs. 10,000 to be depreciate over a period of four years under Annuity system. The rate of interest is 5% per annum. The annuity table shows that the annual amount required to write off rupee one in four years at 5% per annum is Re. 0.282012. Prepare the lease account for four years.

(Ans. Depreciation Rs. 2,820)

10. A company purchased 3 years lease on January 1, 2006 for Rs. 25,000. It decided to provide for the replacement of the lease at the end of three years by setting up depreciation fund. Sinking fund table shows that to provided to requisite sum at 5% at the end of three years and investment all Rs. 7,932 is required every year. Investment are made to the nearest ten rupee. On 31st December 2008 the investment are sold for Rs. 16,550. Show the journal entry.



UNIT V : SINGLE ENTRY SYSTEM

Single entry system – features – advantages and disadvantages – single entry system Vs double entry system – calculation of profit by comparing capitals – conversion of single entry system into double entry by finding out missing information

CHAPTER – 8 SINGLE ENTRY SYSTEM

INTRODUCTION

Generally tiny organizations, do not have any knowledge of accounting. They do not want to follow any systematic or scientific methods of accounting. They prefer to maintain only few accounts. To ascertain profit or loss of their business, they prepare only the statement of profit or loss.

They record two transactions according to their desire. At the end of the year, with the help of the available data, the profit or loss of the business are ascertained through a system known as single entry system. In this chapter, an attempt is made to ascertain the profit or loss under single entry system.

SINGLE ENTRY SYSTEM – MEANING AND DEFINITION

Under this system, cash book and personal accounts are maintained. This system does not totally follow the principles of Double Entry System. According to R.N.Carter, Single Entry system cannot be termed as a system, as it is not based on any scientific system like Double Entry System. For this purpose, Single Entry System is now a days known as preparation of accounts from incomplete records. Particularly this system is followed by those firms whose transactions are limited and at the same time, who maintain only the essential records. There is no hard and fast rule for maintaining records under this system, i.e. it depends on the circumstances and the necessity of the firm.

FEATURES OF SINGLE ENTRY SYSTEM

Books according to this system can be kept only in sole trader or partnership firm organizations. Limited companies, because of legal provisions, cannot keep books on Single Entry System.



In this system it is very common to keep only personal accounts and to avoid real and nominal accounts. Therefore, this system is defined as a system where only personal accounts are kept.

It is very common in this system to keep one cash book which mixes up business as well as private transactions.

It is also quite often seen that for information, one has to depend on original vouchers. For example, in case of credit sales, proprietor may keep the invoice without recording it anywhere and at the end of year the total of the invoices gives an idea of total credit sales of the business.

This system lacks uniformity as it is a mere adjustment of double entry system according to the conveniences of the person.

MERITS OF SINGLE ENTRY SYSTEM

1. Since this system is very simple, anyone can maintain it without any adequate knowledge of accounting.
2. Limited accounts are to be opened under this system since the transactions relating to only personal accounts are recorded.
3. Since the numbers of books are limited, expenses relating to the keeping of records are also nominal.
4. In the case of accounting for an event, i.e. household, social and festival, etc., it is very helpful.

LIMITATIONS OF SINGLE ENTRY SYSTEM

1. Arithmetical accuracy of the books of account is not found out since the Trail Balance cannot be prepared under this system.
2. It is also not possible to ascertain the correct amount of profit or loss of the firm, (i.e. results from operation) since the nominal accounts are missing under this system,
3. Similarly, Balance Sheet cannot be prepared since the real accounts are not recorded. Therefore, the real financial position cannot be known at the end of the accounting period.
4. As the arithmetical accuracy is not possible, the possibility of committing fraud or manipulation is greater in comparison with Double Entry System.



5. Any statistical information relating to the business or the comparison between the two firms or the interim accounts, etc. which help the management to take decision or to formulate policy in future is not possible under this system.
6. Outsiders (e.g. Income-tax authorities, Bank, etc.) do not rely on this system.

METHODS OF ASCERTAINMENT OF PROFIT OR LOSS UNDER SINGLE ENTRY SYSTEM

Under Single Entry System, the following two methods are followed to ascertain profit or loss (1) Statement of affairs method/Increase in Net worth Method and (2) Conversion method.

STATEMENT OF AFFAIRS METHOD / INCREASE IN NET WORTH METHOD

Under this method, Profit or Loss made by the business is ascertained by comparing the capital at the end of the trading period with that at the beginning. If the Capital at the close is higher, the increase is the measure of Profits and if the Capital at the close is lower the decrease is the measure of loss. The Capital either at the beginning or at the close- can be ascertained by preparing a statement of affairs at the opening and also as at the closing date.

Statement of Affairs

A statement of affairs, like Balance Sheet, is a statement of all assets and liabilities. One should consider different adjustments, like depreciation on assets, outstanding and prepaid expenses, etc. at the time of preparing a statement of affairs.

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

Statement of Affairs as on

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry creditors	***	Cash in hand	***
Bills payable	***	Sundry debtors	***
Outstanding expenses	***	Fixed assets	***
Bank overdraft	***	Bills Receivable	***
Capital (Opening / Closing)	***	Prepaid expenses	***



		Stock	***
	***		***

Specimen Profit and Loss

Profit and Loss for the year ended.....

Particulars	Amount Rs.
Closing capital	***
Add: Drawings	***

Less: Additional Capital	***

Less: Opening Capital	***
Profit / Loss	***

Difference between Double Entry System and Single Entry System

No.	Basis of Distinction	Double Entry System	Single Entry System
1.	Principle	For every debit there is a corresponding credit and vice versa.	Debit and credits do not agree.
2.	Recording of transaction	Debit and credit aspects of all transactions are recorded	Debit and credit aspects of all transactions are not recorded.
3.	Nature of accounts maintained	Maintains complete record of personal, real and nominal accounts.	All incomplete record. Only personal and cash accounts are maintained.
4.	Trial balance	Arithmetical accuracy of the records can be checked by preparing a trial balance.	Trial balance cannot be prepared.
5.	Determination of profit or loss and	A profit and loss account and balance sheet can be	A profit & loss account and balance sheet cannot be



	financial position	conveniently prepared since the book of accounts present a complete picture.	conveniently prepared since the accounting records are incomplete.
6.	Suitability	It is suitable for all types of traders.	It is suitable for only small traders.
7.	Dependability	It is the only scientific system of keeping books of accounts.	It not a system. It is incomplete and unscientific.
8.	Acceptability	Records are acceptable for the purpose of tax, loans, etc.,	Records are not acceptable for the purpose of tax claims, loans, etc.,
9.	Internal check	Internal check is possible	Internal check is not possible.

Difference between Statement of Affairs and Balance Sheet

Balance Sheet is also a statement of assets and liabilities just like that of statement of affairs. But there are some differences between these two. Let us now see that differences between Statement of affairs and Balance Sheet.

No.	Statement of Affairs	Balance sheet
1	It is drawn under the Single Entry System	It is drawn under the Double Entry System
2	It is drawn from the incomplete and unsystematic records.	It is compiled out of the ledger balances as disclosed in complete and systematic records.
3	It cannot be relied upon since the preparation of Trial Balance is not Possible	It is arithmetically proved since it is drawn after the Trial Balance has proved arithmetical accuracy.
4	It shows the financial position without any explanation.	It shows the financial position with some explanations.



Differences between Profit and Loss account and Statement of the profit or Loss

No.	Profit and Loss account	Statement of Profit (Or) Loss
1	Gross Profit and Net profit can be found out.	Only Net profit can be found out.
2	The performance of the business can be measured.	The performance of the business cannot be measured properly
3	It helps the users in taking important decisions.	The users cannot rely this system because the profit is ascertained from incomplete records.
4	It helps to ascertain the income from the business and income from other sources	No such allocation is possible under this system.
5	Expenses are divided into direct and indirect.	There is no such division of expenditure.

Illustration: 1

The capital at the beginning of the year is Rs.30,000 and that at the end is Rs.38000. Calculate the amount of profit earned during the period, assuming that there is no additional capital introduced or no drawings.

Solution:

Statement of profit or Loss

Particulars	Amount Rs.
Capital at the end	38,000
Less: Capital in the beginning	30,000
Profit	8,000

Illustration:2

Calculate the missing information:

	Rs.
Closing Capital	32,000
Drawings	4,800



Additional Capital	8,000
Profit made during the year	9,600

Solution:

Statement of Profit or Loss

Particulars	Amount Rs.
Closing capital	32,000
Add: Drawings	4,800
	36,800
Less: Additional Capital	8,000
	28,800
Less: Opening Capital (Balancing figure)	19,200
Profit	9,600

Illustration: 3

Calculate the missing information:

	Rs.
Closing capital	1,63,000
Additional Capital	42,300
Drawings	25,200
Loss	12,600

Solution:

Statement of profit or loss

Particulars	Amount Rs.
Closing capital	1,63,800
Add: Drawings	25,200
	1,89,000
Less: Additional Capital	42,300
	1,46,700
Less: Opening Capital (Balancing figure)	1,59,300
Loss	12,600



Illustration: 4

Calculate the missing information

	Rs.
Capital in the beginning	24,000
Profits made during the year	9,000
Capital introduced during the year	12,000
Capital at the end	39,000

Solution:

Statement of profit or loss

Particulars	Amount Rs.
Closing capital	39,000
Add: Drawings (Balancing figure)	6,000
	45,000
Less: Additional Capital	12,000
	33,000
Less: Opening Capital	24,000
Profit	9,000

Illustration: 5

Mrs. Revathi Started business with Rs.1,20,000 as capital on 1.4.2013. During the year for his personal use, withdrawn at the rate of R.1,000 per month. He introduced Rs.20,000 as additional capital. His position on 31.3.2014 was as follows:

	Rs.
Bank balance	8,000
Stock	80,000
Sundry Debtors	50,000
Furniture	2,500
Cash in hand	2,000
Sundry Creditors	25,000
Expenses outstanding	1,000



She keeps her books under single entry system. Determine his profit or loss for the year 2013-14

Solution:

Statement of affairs of Mrs. Ravathi as on 31.3.2013

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	25,000	Stock	80,000
Outstanding expenses	1,000	Sundry Debtors	50,000
Capital (Balancing figure)	1,16,500	Furniture	2,500
		Cash in hand	2,000
		Bank balance	8,000
	1,42,500		1,42,500

Statement of profit of Mrs. Ravathi for the period ended 31.3.2014

Particulars	Amount Rs.
Closing Capital	1,16,500
Add: Drawings (1000 X 12)	12,000
	1,28,500
Less: Additional Capital	20,000
	1,08,500
Less: Opening Capital	1,20,000
Loss	11,500

Illustration: 6

Mr. Gundurao keeps his books under single entry system, Assets and liabilities on 31.3.2009 and 31.3.2010 stood as follows:

	31.3.2009	31.3.2010
	(Rs.)	(Rs.)
Sundry creditors	15,000	30,000
Furniture	15,000	15,000
Sundry Debtors	75,000	1,00,000



Stock	35,000	50,000
Cash Balance	5,000	60,000

He introduced an additional capital of Rs.15,000 during the year. He withdrew Rs.35,000 for domestic purpose. Find out the profit or loss for 2009-10

Solution:

Statement of affairs of Mr. Gundurao as on 31.3.2009

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	15,000	Furniture	15,000
Capital (Balancing figure)	1,15,000	Sundry Debtors	75,000
		Stock	35,000
		Cash Balance	5,000
	1,30,000		1,30,000

Statement of affairs of Mr. Gundurao as on 31.3.2010

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	30,000	Furniture	15,000
Capital (Balancing figure)	1,95,000	Sundry Debtors	1,00,000
		Stock	50,000
		Cash Balance	60,000
	2,25,000		2,25,000

Statement of profit & loss of Mr. Gundurao for the period ended 31.3.2010

Particulars	Amount Rs.
Closing Capital	1,95,000
Add: Drawings	35,000
	2,30,000
Less: Additional Capital	15,000
	2,15,000



Less: Opening Capital	1,15,000
Profit	1,00,000

Illustration: 7

The balances appearing in Bharanidharan's books which are kept on single entry basis are as follows:

	1 st April, 2009	31 st March 2010
	Rs.	Rs.
Furniture	2,000	2,000
Stock	5,000	6,000
Sundry Debtors	6,000	4,000
Cash	10,000	20,000
Sundry Creditors	2,000	3,500
Bills Receivable	1,000	500
Loan (Dr.)	--	1,000
Investment	--	4,000

His drawings during the year were Rs.2,000. Depreciate furniture by 10% and provide a reserve for bad and doubtful debts at 5% on sundry debtors.

Prepare a statement showing profit for the year.

Solution:

Statement of affairs of Mr. Bharanidharans as on 1st April, 2009

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	2,000	Furniture	2,000
Capital (Balance figure)	22,000	Stock	5,000
		Sundry Debtors	6,000
		Cash	10,000
		Bills Receivable	1,000
	24,000		24,000



Statement of affairs of Mr.Bharanidharans as on 31st March,2010

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	3,500	Cash	20,000
Capital (Balance figure)	33,600	Stock	6,000
		Sundry Debtors 4,000	
		Less: Reserve for bad doubtful debts 5% 200	3,800
		Bills Receivable	500
		Investment	4,000
		Loan	1,000
		Furniture 2,000	
		Less: Depreciation 10% 200	1,800
	37,100		37,100

Statement of profit & loss of Mr.Bharanidharans for the period ended 31.3.2010

Particulars	Amount Rs.
Closing Capital	33,600
Add: Drawings	2,000
	35,600
Less: Opening Capital	22,000
Profit	13,600

Illustration: 8

A trader has not kept proper books of accounts. His position as on 31.3.2009 and 31.3.2010 was as follows:

	31.3.2009	31.3.2010
	Rs.	Rs.
Cash at Bank	75,000	50,000
Cash in hand	5,000	10,000



Stock	5,00,000	3,25,000
Sundry Debtors	2,00,000	4,00,000
Furniture	50,000	50,000
Machinery	4,00,000	4,00,000
Sundry Creditors	6,00,000	7,00,000

During the year he introduced Rs.1,00,000 as additional capital and withdrew Rs.10,000 per month for domestic purpose. Depreciate furniture and machinery by 10% per year. Ascertain profit or loss for the year ended 31.3.2010.

Solution:

Statement of affairs as on 31.03.2009

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	6,00,000	Cash at bank	75,000
Capital (Balance figure)	6,30,000	Cash in hand	5,000
		Stock	5,00,000
		Sundry Debtors	2,00,000
		Machinery	4,00,000
		Furniture	50,000
	12,30,000		12,30,000

Statement of affairs as on 31.03.2010

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry Creditors	7,00,000	Cash at Bank	50,000
Capital (Balance figure)	4,90,000	Cash in hand	10,000
		Stock	3,25,000
		Sundry Debtors	4,00,000
		Furniture	50,000
		Less:	
		Depreciation	5,000
		Machinery	4,00,000
		Less:	
			45,000



	Depreciation	40,000	3,60,000
			11,90,000
			11,90,000

Statement of profit & loss for the period ended 31.3.2010

Particulars	Amount Rs.
Closing Capital	4,90,000
Add: Drawings (10,000 X 12)	1,20,000
	6,10,000
Less: Additional Capital	1,00,000
	5,10,000
Less: Opening Capital	6,30,000
Loss	1,20,000

Illustration: 9

From the following, find out credit sales

	Rs.
Opening sundry debtors	50,000
Cash received from sundry debtors	80,000
Discount allowed to sundry debtors	2,000
Sales return	5,000
Closing sundry debtors	75,000

Solution:

Total Debtors account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Balance b/d (Opening balance)	50,000	By Cash received	80,000
To Credit sales	1,12,000	By Discount allowed	2,000
(Balancing figure)		By Sales returns	5,000
		By Balance c/d (Closing balance)	75,000
	1,62,000		1,62,000



Illustration: 10

From the following details, find out credit purchases

	Rs.
Opening sundry creditors	75,000
Closing sundry creditors	90,000
Cash paid to sundry creditors	22,500
Discount received	15,000
Purchase returns	7,500

Solution:

Total Creditors account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Cash paid	22,500	By Balance b/d	75,000
To Discount received	15,000	(Opening balance)	
To Purchases returns	7,500	By Credit purchases	60,000
To Balance c/d (Closing balance)	90,000	(Balancing figure)	
	1,35,000		1,35,000

Illustration: 11

From the following information calculate total purchases.

	Rs.
Cash purchase	85,000
Creditors as on April 1, 2012	40,000
Cash paid to creditors	1,65,000
Purchase returns	5,000
Creditors as on March 31, 2013	67,000



Solution:

Total Creditors Account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Cash a/c	1,65,000	By Balance b/d	40,000
To Purchase Return a/c	5,000	By Credit Purchases a/c	1,97,000
To Closing balance	67,000	(Balancing figure)	
	2,37,000		2,37,000

Note: Cash Purchases will find no place in Creditors a/c

Total Purchases

Particulars	Amount Rs.
Cash Purchases	85,000
Add: Credit Purchases	1,97,000
	2,82,000

Illustration: 12

From the following, you are required to calculate total sales made during the year.

	Rs.
Debtors on April 1, 2012	51,000
Cash received from debtors during the year (as per cash book)	1,52,000
Returns inwards	13,500
Bad debts	6,000
Debtors as on March 31, 2013	69,000
Cash Sales (as per Cash Book)	1,42,000



Solution:

Total Debtors Account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To balance b/d	51,000	By Cash a/c	1,52,000
To Credit Sales	1,89,500	By Returns inwards	13,500
(Balancing Figure)		By Bad debts a/c	6,000
		By Balance c/d	69,000
	2,40,500		2,40,500

Note: Cash sales will find no place in the debtors account.

Total Sales

Particulars	Amount Rs.
Cash sales	1,42,000
Add: Credit Sales	1,89,500
	3,31,500

Illustration: 13

From the following particulars, calculate closing balances Debtors and Creditors

	Rs.
Sundry debtors as on 1.4.2015	57,360
Sundry creditors as on 1.4.2015	83,620
Credit purchases	3,02,800
Credit sales	3,31,800
Discount earned	10,400
Discount allowed	9,600
Return outwards	14,880
Return inwards	12,888
Cash received form debtors	3,01,072



Cash paid to creditors

2,87,530

Solution:

Total Debtors account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Balance b/d	57,360	By Cash received	3,01,072
To Credit sales	3,31,800	By Discount allowed	9,600
		By Sales returns	12,888
		By Balance c/d	63,600
		(Balancing figure)	
	3,89,160		3,89,160
To Balance b/d	63,600		

Total Creditors account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Cash paid	2,87,530	By Balance b/d	83,620
To Discount received	10,400	(Opening balance)	
To Purchases returns	14,880	By Credit purchases	3,02,800
To Balance c/d	73,610		
(Balancing figure)			
	3,86,420		3,86,420
		By Balance b/d	73,610

Illustration: 14

Mrs. Malathy maintained her account books of single entry system on 1.4.2013 her capital was Rs. 2,50,000.

Additional Information:

	Rs.
Opening stock	1,25,000
Cash received form sundry debtors	25,000



Cash sales	1,00,000
Cash paid to sundry creditors	30,000
Opening sundry debtors	20,000
Opening sundry creditors	91,500
Business expenses	60,400
Free hold premises (31.3.2014)	2,00,000
Furniture (31.3.2014)	3,600
Closing stock	1,30,000
Closing sundry debtors	40,000
Closing sundry creditors	1,00,000
Closing cash balance	27,500

Prepare trading and profit & loss account for the year ended 31.03.2014 and balance sheet as on that date.

Solution:

Total Debtors account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Balance b/d (opening)	20,000	By Cash received	25,000
To Credit sales	45,000	By Balance c/d (closing)	40,000
(Balancing figure)	65,000		65,000

Total Creditors account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Cash paid	30,000	By Balance b/d (Opening)	91,500
To Balance c/d (Closing)	1,00,000	By Credit purchases	38,500
	1,30,000	(Balancing figure)	1,30,000



Trading and Profit & Loss account of Mrs. Malathy for the year ended 31.3.2014

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	1,25,000	By Sales	
To Purchase (Credit)	38,500	Cash	1,00,000
To Gross profit c/d	1,11,500	Credit	45,000
		By Closing stock	1,30,000
	2,75,000		2,75,000
To Business expenses	60,400	By Gross profit b/d	1,11,500
To Net profit	51,100		
	1,11,500		1,11,500

Balance sheet of Mrs. Malathy as on 31.3.2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital	2,50,000	Freehold premises	2,00,000
Add: Net profit	51,100	Furniture	3,600
	3,01,100	Closing stock	1,30,000
	1,00,000	Sundry debtors	40,000
		Cash in hand	27,500
	4,01,100		4,01,100

Illustration: 15

From the following details, prepare Trading and Profit and Loss account for the period ended 31.3.2014 and a balance sheet on that date

	31.3.2013	31.3.2014
	Rs.	Rs.
Stock	50000	25000
Sundry debtors	125000	175000
Cash	12500	20000
Furniture	5000	5000



Sundry creditors 75000 87500

Other details

	Rs.
Drawings	20,000
Discount received	7,500
Discount allowed	5,000
Sundry expenses	17,500
Cash paid to creditors	2,25,000
Cash received form debtors	2,67,500
Sales return	7,500
Purchase return	2,500
Cash sales	2,500

Solution:

Statement of affairs as on 31.03.2013

Liabilities	Amount Rs.	Assets	Amount Rs.
Sundry creditors	75,000	Stock	50,000
Capital	1,17,500	Sundry debtors	1,25,000
(Balancing figure)		Cash	12,500
		Furniture	5,000
	1,92,500		1,92,500

Total Debtors account

Dr.

Cr.

Particulars	Amount Rs.	Particulars	Amount Rs.
To Balance b/d	1,25,000	By Cash received	2,67,500
To Credit sales	3,30,000	By Discount allowed	5,000
(Balancing figure)		By Sales returns	7,500
		By Balance c/d	1,75,000
	4,55,000		4,55,000



Total Creditors account

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Cash paid	2,25,000	By Balance b/d	75,000
To Discount received	2,500	(Opening balance)	
To Purchases returns	7,500	By Credit purchases	2,47,500
To Balance c/d	87,500	(Balancing figure)	
	3,22,500		3,22,500

Trading and Profit & Loss account for the year ended 31.3.2014

Dr.		Cr.	
Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	50,000	By Sales	
To Purchases	2,47,500	Cash	2,500
Less: Returns	2,500	Credit	3,30,000
To Gross profit c/d	55,000		3,32,500
	3,50,000	Less: Returns	7,500
To Discount paid	5,000	By Closing stock	25,000
To Sundry expenses	17,500		3,50,000
To Net profit	40,000	By Gross profit b/d	55,000
	62,500	By Discount received	7,500
			62,500

Balance sheet as on 31.3.2014

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital	1,17,500	Furniture	5,000
Add: Net profit	40,000	Sundry debtors	1,75,000
	1,57,500	Closing stock	25,000
Less: Drawings	20,000	Cash	20,000
	1,37,500		



Sundry creditors	87,500	
	2,25,000	2,25,000

Exercises

Theory questions

1. What do you mean by single entry system?
2. What are the features of single entry system?
3. What are the merits and demerits of single entry system?
4. Difference between single entry system and double entry system.
4. Difference between single entry system and statement of affairs.
4. Difference between single statement of affairs and profit loss account.

1. The capital at the beginning of the year Rs. 60,000 and that the end is Rs. 57,000 calculate the amount profit earned or loss incurred during the period.

(Ans. Rs. 3,000)

2. The capital at the beginning of the year Rs. 40,000 and that the end is Rs. 50,000 during the year Rs. 3,000 has been withdrawals for personal uses calculate the amount profit earned or loss incurred during the period.

(Ans. Rs. 13,000)

3. The capital at the beginning of the year Rs. 20,000 and that the end is Rs. 31,000 withdrawals at the rate of Rs. 500 per month and additional capital introduced during the year Rs. 2,000. Calculate the amount profit earned or loss incurred during the period.

(Ans. Rs. 15,000)

4. What shall be the profit of the concern if

	Rs.
Opening capital	1,60,000
Closing capital	1,80,000
Drawings	36,000
Additional capital	10,000

(Ans. 46,000)



5. Find out Missing figure

	Rs.
Closing capital	64,000
Drawings	9,600
Additional capital	16,000
Profit	19,200
Opening capital	?

(Ans. Opening Capital Rs. 38,400)

6. Calculate the missing information

	Rs.
Drawings	50,000
Additional capital	10,000
Opening capital	1,00,000
Closing capital	?
Profit	25,000

(Ans. Closing Capital Rs. 85,000)

Statement of Affairs

7. Mr. Selvan Started business with Rs.2,40,000 as capital on 1.4.2013. During the year for his personal use, withdrawn at the rate of R.2,000 per month. He introduced Rs.40,000 as additional capital. His position on 31.3.2014 was as follows:

	Rs.
Bank balance	16,000
Stock	1,60,000
Sundry Debtors	1,00,000
Furniture	5,000
Cash in hand	4,000
Sundry Creditors	50,000
Expenses outstanding	2,000

He keeps his books under single entry system. Determine his profit or loss for the year 2013-14

(Ans. Loss: Rs. 23,000)



8. Mr. Vetrivel keeps his books under single entry system, Assets and liabilities on 31.3.2014 and 31.3.2015 stood as follows:

	31.3.2014	31.3.2015
	(Rs.)	(Rs.)
Sundry creditors	7,500	15,000
Furniture	7,500	7,500
Sundry Debtors	37,500	50,000
Stock	17,500	25,000
Cash Balance	2,500	30,000

He introduced an additional capital of Rs.7,500 during the year. He withdrew Rs.17,500 for domestic purpose. Find out the profit or loss for 2014-15

(Ans. Profit Rs. 50,000)

9. The balances appearing in Mr. Vijay's books which are kept on single entry basis are as follows:

	1 st April 2015	31 st March 2016
	Rs.	Rs.
Furniture	4,000	4,000
Stock	10,000	12,000
Sundry Debtors	12,000	8,000
Cash	20,000	40,000
Sundry Creditors	4,000	7,000
Bills Receivable	2,000	1,000
Loan (Dr.)	—	2,000
Investment	—	8,000

His drawings during the year were Rs. 4,000. Depreciate furniture by 10% and provide a reserve for bad and doubtful debts at 5% on sundry debtors.

Prepare a statement showing profit for the year.

(Ans. Profit Rs. 27,200)



Conversion Method

10. From the following, find out credit sales

	Rs.
Opening sundry debtors	25,000
Cash received from sundry debtors	40,000
Discount allowed to sundry debtors	1,000
Sales return	2,500
Closing sundry debtors	37,500

(Ans. Credit Sales Rs. 56,000)

11. From the following details, find out credit purchases

	Rs.
Opening sundry creditors	1,50,000
Closing sundry creditors	1,80,000
Cash paid to sundry creditors	45,000
Discount received	30,000
Purchase returns	15,000

(Ans. Credit purchases Rs. 1,20,000)

12. From the following information calculate total purchases.

	Rs.
Cash purchase	1,70,000
Creditors as on April 1,2012	80,000
Cash paid to creditors	3,30,000
Purchase returns	10,000
Creditors as on March 31, 2013	1,34,000

(Ans. Total Purchases Rs. 5,64,000)

13. From the following, you are required to calculate total sales made during the year.

	Rs.
Debtors on April 1,2012	25,500
Cash received from debtors during the year (as per cash book)	76,000



Returns inwards	6,750
Bad debts	3,000
Debtors as on March 31, 2013	34,500
Cash Sales (as per Cash Book)	71,000

(Ans.: Total sales Rs. 1,65,750)

14. Arun keeps his book by single entry on 1st January 2010 his capital was Rs. 6,900 analysis the of his cash book for 2010 gives the follows.

	Rs.
Debit side	
Received from debtors	6,000
Paid on capital accounts	500
Credit side	
Due to bank 1.1.2010	740
Payment to creditors	2500
General expenses	1000
Salaries	1550
Drawings	300
Balance at bank on 31.12.2010	400
Balance of cash in hand 31.12.2010	10

Assets and Liabilities	January, 1	December, 31
	Rs.	Rs.
Debtors	5,300	8,800
Creditors	1,500	1,950
Plant	2,000	2,000
Furniture	140	140
Stock	1,700	1,900

Provide 5% interest on capital, depreciation on plant and furniture and reserve 5% of debtors. Prepare final account and balance sheet of Arun.

(Ans. Cash book Rs. 500;

Debtors a/c Rs. 9,500; Creditors a/c Rs. 2,950;

Net profit Rs. 3,308; Balance sheet Rs. 12,703)



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